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India Official Says Overhauls Remain on Track

Finance Minister Insists Political Allies Won't Block Market-Opening Measures

By Eric Bellman & John Larkin

New Delhi – India's strong economic growth and market-opening measures will continue, despite signs the ruling coalition government is struggling to push through unpopular overhauls, Finance Minister P. Chidambaram said.

Responding to growing criticism that the congress party-led government is allowing its communist-coalition allies to block changes, Mr. Chidambaram contented that he could keep India on the path of high growth with low inflation.

"These is convergence in many areas and these is divergence in many areas," he said in an interview. "In any coalition, it will require patience, persistence and perseverance."

In the 14 months since the Congress coalition came to power, India's gross domestic product has expanded at an annualized rate of about 7% and Mr. Chidambaram has been able to take steps towards making India more open and efficient by allowing more foreign investment in the telecommunications, airlines and real-estate industries as well as streamlining the country's tax system.

Still, many economists, investors and corporate executives are concerned that the overhaul process is being bogged down by opposition from the communist parties that the coalition government depends on for survival. The Congress party itself holds 145 seats in India's 545-seat Parliament and relies on the 61 seats held by communist parties in its coalition to maintain a majority.

In recent months, the anticipated opening of the retail industry to foreign investment, the divestment of holdings in some important state-run companies and the easing of labor laws have all been postponed or blocked by minority members of the fragile ruling coalition. This month, attention has focused on the government's struggle to convince the so called Left Front to drop objections to plans to sell 10% of Bharat Heavy Electricals Ltd, a state-controlled manufacturer of power equipment.

Since Mr. Chidambaram announced the stake sale two months ago, it has been viewed as a crucial test of the government's commitment to making the public sector more efficient. But the government could announce as early as this week that it has given up on the divestment plans, analysts said.

"The fact that it may not happen means that the government has reversed its stand on one of the key privatization issues," said Jon Thorn, managing director of the India Capital Fund in Hong Kong. "This is not a positive change."

Mr. Chidambaram played down concerns about the possible shelving of Bharat Heavy divestment. Foreign investors shouldn't be concerned, he said, because the government will

continue to look for ways to use the markets to make state-run companies stronger.

"We are not advocating disinvestment for the sake of disinvestment," he said. "We are saying that public-sector entities must be made more accountable and efficient."

Further opening of India's fragmented retail industry to foreign investment is still being discussed, Mr. Chidambaram said, but there are "no time limits" on a resolution. Meantime, while economists and companies have been expecting India to relax its historically pro-labor employment laws to attract foreign investment, Mr. Chidambaram said labor overhaul "is not in the agenda because it is a very difficult area."

New Delhi gets credit for the introduction of a value-added tax in most Indian states earlier this year, a step designed to help cut India's large fiscal deficit. Still, investors warn that the government has to further roll back government spending or risk triggering inflation that could subvert growth.

"We need more efforts to address the [government's] fiscal deficit through serious structural reform," such as slashing subsidies on fertilizer, power and petroleum, said Gopal Jain, managing director of Gaja Capital Partners, a private equity firm in Mumbai. "If you look at the government sector, it is actually backtracking on reforms."

India's fiscal deficit was a relatively high 4.1% of GDP in the year ended March 31. Mr. Chidambaram said it was too early to predict whether India will do better by the end of the current fiscal year. GDP is the total value of goods and services produced in the nation.

The Congress party, headed by Sonia Gandhi, needs to push through the tough changes if it wants to spur more growth and create jobs, most economists contend. One reason it is having trouble moving forward with revisions is that any politicians within the party continue to sympathize with the views of the Left, says Surjit Bhalla, managing director of OXUS Research & Investments, a corporate-advisory firm in New Delhi.

"The Left outside the government is not as bad as the Left within the government," he said. "The Left within the government goes right up to Sonia Gandhi."

Still, Mr. Chidambaram says he is happy with his track record on overhauls, which he vows will continue, though not always as fast as some investors and executives would like. "Many things have been done ... many things that have not been contemplated" before, the finance minister said. "One has to be patient."