

India: Expect Turbulence

Prime Minister Manmohan Singh's government allotted the key posts to veteran Congress figures, but nearly half of its parliamentary strength comes from outside his Congress Party. Now the government faces three big tasks: economic policy, reconciling its promises to spread more of India's growth to the poor; foreign policy, especially managing the dialogue with Pakistan; and managing a political coalition, a new requirement for a party that dominated India's politics for three decades. Relations with the United States will be powerfully affected by India's economic policy, and will require a deft touch on both sides.

The new cabinet: After confounding everyone with a surprise victory in the Indian elections, the Congress party has added parliamentary support from India's communist parties to its pre-election coalition to form a majority. The new cabinet, led by the dignified and cerebral Manmohan Singh, is dominated by veteran politicians who have served in various capacities under previous Congress administrations. Congress holds the four key cabinet posts. Foreign Minister Natwar Singh served in the same post between 1986 and 1989. He is widely regarded as an astute diplomat, having served in many high-ranking positions including a two-year ambassadorial stint in Pakistan. Defense Minister Pranab Mukherjee had previously served as both foreign minister and finance minister in the 1980s. P. Chidambaram, a Harvard Business School alumnus and former finance minister from 1996-1998, has been picked to do the same job. Home Minister Shivraj Patil, responsible for internal security, held several ministerial posts under previous Congress governments. Among non-elected senior officials, there are also some familiar faces: J.N. Dixit, the new National Security Adviser to the Prime Minister, is a former Foreign Secretary and high commissioner to Pakistan and Sri Lanka; and M. K. Narayanan, Special Adviser to the Prime Minister, is a former director of the Intelligence Bureau.

Some members of the government are more controversial. Railways minister Laloo Prasad Yadav, who heads the Rashtriya Janata Dal, the biggest coalition partner, faces a number of charges of involvement in a massive corruption scandal. Two other ministers from the same party also figure in reported corruption scandals.

Daunting economic task: The new government will be preoccupied for the next few months with economic policy. The Congress leadership has strong economic credentials. Prime Minister Singh began the country's economic reforms with a memorable budget speech in 1991, in which he yanked the country away from its statist policies and tentatively opened the

door to foreign capital in the midst of a severe debt crisis. Since then, he has earned a strong reputation both for reform policies and for scrupulous honesty. Chidambaram has been credited for stressing fiscal discipline and streamlining India's complicated tax structure in the budget he presented in 1997, on an earlier stint as finance minister. Besides the talent of the top two economic policy officials, the government inherits an economy growing at an estimated 7-8 percent this year, following a good monsoon in 2003.



But economic reforms invariably require dismantling existing relationships and making short-term sacrifices. In India, expenditure on agriculture and rural development has declined and so has the number of government jobs. Unemployment in 2002 was 8.8 percent. And the government's allies on the left will be pushing for changes in the tone of policy and the pattern of government spending.

Early policy statements: The new government's signals on economic policies have been mixed so far. The recently announced Common Minimum Program, the coalition parties' joint statement of their starting point for a joint policy, sets forth a goal of 8 percent gross domestic product (GDP) growth. It also pledges not to privatize profit-making state-owned enterprises, to disband the Ministry of Disinvestments, to boost education spending to 6 percent of the gross domestic product, from the present level of about 2 percent, and to increase spending on infrastructure and agriculture. The government has announced the formation of a National Commission on Farmers, headed by M.S. Swaminathan, the long-time head of the Indian Council of Agricultural Research and one of the fathers of the Green Revolution. The commission is to make recommendations on increasing agricultural productivity and improving the life of the rural poor.

The needs of India's poor and rural populations are beyond question. According to the World Bank, India is home to the world's largest number of illiterates and accounts for 20 percent of the world's out-of-school children. One quarter of India's population remains desperately poor and the 2003 UNDP Human Development Report for India states that 34.7% of the population was living below one dollar a day between 1990 and 2001.

The fiscal deficit will be the most difficult pressure point for the new team. India currently has a combined central and state

budget deficit equal to 10% of its economic output, and their new policies call for major new spending. The government has said that it would consolidate the fiscal position by streamlining India's tax base while targeting agricultural subsidies more efficiently. Its real challenge will be to find ways to enhance rural prosperity without new subsidies. To complicate matters, state governments may not agree. The first announcement of the newly-elected chief minister of Andhra Pradesh state, Rajasekhara Reddy, who defeated the reform-minded Chandrababu Naidu, was to promise farmers free electricity and debt writeoffs.

Investors cautiously optimistic: Markets rallied after their early dramatic fall on the news of the Congress victory. However, investors have mixed feelings about the new government and will watch the 2004 budget before making up their minds. Both Moody's Investors Service and Standard & Poor's (S&P) rating companies have urged the government to cut the budget deficit. "The 2004 budget will be the litmus test of either fiscal consolidation or the continuation of India's parlous fiscal record," S&P said in a statement. Both rating companies cite concerns about the deficit as a major reason for the non-investment grade ratings they give India's local-currency debt. A World Bank study in March also warned that without proper "fiscal adjustment", the domestic debt burden is likely to reach unmanageable levels by 2007.

Sustaining this year's growth: Most forecasts for the Indian economy expect it to fall back to 5-6 percent after the current year. In the short term, agricultural growth depends heavily on the weather and on the government's agricultural price policy. The big variables are industrial growth, which will depend on whether big domestic & foreign companies follow through with their investment plans, and the services and information technology sectors. Services now constitute 50.7 percent of GDP, up from 42.3 percent in 1992.



As leader of the Congress party, Sonia Gandhi will have considerable influence on government policies. (Photo courtesy: U.S. Department of State.)

Continuity but a new tone for foreign policy: Foreign policy

was not an issue in the elections, and many of the policies adopted by Vajpayee's government enjoyed broad consensus among India's political parties. The Common Minimum Program promised that the new government would continue talks with Pakistan and strong relations with the United States. The program document expresses these views in an idiom that was more commonly heard before the end of the Cold War, with ringing appeals to multipolarity and emphasis on India's independent voice in foreign affairs.

The government has pledged specifically to continue talks with Pakistan. The planned meeting on confidence-building measures scheduled for May 25 was postponed to give the new government a chance to get briefed, but it has already been rescheduled for June 19-20, preceding the meeting of the two countries' foreign secretaries on June 27-28. Ties with China, spearheaded by increasing bilateral trade, will continue to grow, though no major breakthroughs are expected on outstanding border issues. As for India's Middle East policy, Defense Minister Pranhab Mukherjee has stated several times since taking office that ties with Israel would remain firmly in place. Israel is the second largest supplier of military technology and equipment to the Indian armed forces, and the two countries have established close defense ties.

India-United States relations: Ties between India and the United States have improved dramatically since the Congress was last in power. Both the Common Minimum Program and statements by the new foreign minister have stressed that a strong U.S.-India relationship is a must for the new government. During the past five years, the security dialogue has become the most active part of government-to-government ties. The fact that the Defense Policy Group, which brings senior defense officials together, met just a few days into the tenure of the new government is one illustration of the place security issues occupy. In addition, the outgoing government had developed personal ties with two successive U.S. administrations. The Congress leadership may not be altogether comfortable with the high profile of security issues, and they and their U.S. counterparts will need both to develop common interests and to manage disagreements. The statement by India's Foreign Minister Natwar Singh that "differences" with the U.S., would not be aired publicly but "addressed diplomatically and tactfully" is a promising sign.

HIV/AIDS policy will have to move into high gear: The responsibility for managing India's HIV/AIDS pandemic has fallen on a 36-year old political novice, Anbumani Ramdoss, representing a key ally of the Congress government from Tamil Nadu state, one of the six states in which the AIDS epidemic is most advanced. Ramdoss, the youngest member of the cabinet, is a doctor but also attended the London School of Economics. He has promised to continue most of the policies of his

predecessor after consultations with health ministry officials and the prime minister. One of his biggest tasks will be to implement the ongoing program to provide antiretroviral (ARV) drugs to new HIV-positive parents (in practice, primarily mothers), infected children under age 15, and patients coming in to government hospitals, in the six high-prevalence states. But whether the health ministry has enough funds for the project remains unclear. Ramdoss will have to use his persuasive powers to secure adequate allocations from the finance ministry.

The Congress party has shown a strong interest in dealing effectively with India's HIV/AIDS crisis. Manmohan Singh, then leader of the opposition in the upper house of Parliament, met with a CSIS HIV/AIDS Task Force delegation to India in January 2004 and expressed a strong commitment to reversing current trends. Many senior Congress leaders took the initiative in forming a parliamentary committee on HIV/AIDS to involve politicians from a wide range of parties in discussions and to prepare legislation to deal with discrimination issues related to the disease.

Holding the government together: The most dramatic aspects of forming the government dealt with the allocation of portfolios to coalition members. A key partner from Tamil Nadu threatened to boycott the swearing-in unless their party's ministries were "upgraded." In the end, Sonia Gandhi helped to pour oil on the troubled waters. Coalition management is an unaccustomed task for Congress, which ran India single-handed for thirty years. In the end, however, the perks of power are likely to keep the coalition together, and Sonia Gandhi is likely to be an important player in preserving unity within the party and the coalition. The government's main political challenge is likely to come from the opposition Bharatiya Janata Party (BJP), which has already shown itself strident and quick to attack.

Issues for the United States: The outlook for U.S.-India relations depends not just on how the two governments deal with each other – though that will be important, and the next few months are a key opportunity to give the Congress part ownership of the new relationship. In addition, if, as some have suggested, the Congress government wants to build up the economic side of the relationship, the success of India's domestic economic policies in attracting investment and expanding trade will be crucial. On the U.S. side, the main danger is inattention, at a time when a U.S. election looms and Iraq is a huge preoccupation.

Pramit Mitra & Teresita C. Schaffer

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