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***“India is an incredible market—a sophisticated market place, even though it is a developing nation.”***

— J. Joseph Grandmaison,  
Director, US Trade and  
Development Agency  
(USTDA)

## Excerpts from Finance Minister P. Chidambaram's address at “The India Conference” Organized by The Washington Post



Finance Minister  
P. Chidambaram

A 4000-year old civilization has just turned 50. But India's economic revolution is only six years old. The reforms were triggered by a crisis engendered by long years of a state controlled and state-directed economy. They are now based on the conviction that deregulation, competition and the market system are better drivers of growth and prosperity that Indians now accept to be the essential prerequisites for true equal opportunity and tangible social justice.

We have a long way to go but we can look back with some satisfaction.

**Growth** has averaged 7% in the last three years. This has been achieved without any significant deterioration in the external account or in an upsurge of inflationary pressures. Currently, inflation is just a little over 4% and under control. Our objective and our determination is to sustain 7% growth and to attain 8% growth by the turn of the century.

If we are able to do this, we would have succeeded in abolishing poverty by 2020.

We are managing our **external debt** prudently. Our repayment record is impeccable. India's debt service ratio is around 23% of current receipts and the proportion of short-term debt is very small at around 5%. Total external debt has come down sharply from 36% of GDP to 27% in the last four years. The structure of our debt is also radically different: slightly over half of the total debt is to bilateral and multilateral creditors and is on concessional terms.

**Current account deficits** are at extremely safe levels, so safe that we are in the happy position of wanting a higher level of

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## Excerpts from Finance Minister P. Chidambaram's Address

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deficit in order to have a higher order of investment. This year I expect the current account deficit to be less than 2% of GDP. The rupee is relatively stable in a sea of turbulence and we wish to keep it that way. The exchange rate is market determined but we will ensure that there is no excessive speculation or volatility. **Full convertibility** is on the horizon over the next few years. The first steps have already been taken with the liberalization of gold imports, permission given to exporters to retain 50% of their earnings overseas and the flexibility given to mutual funds to invest in overseas markets. Banks have been allowed to borrow and invest-abroad up to certain limits. Interest rates, still high by world standards, have declined by over 400 basis points over the past six months and prime lending rates are now between 13% and 13.5% — the lowest in recent years.

**Foreign investment inflows** continue to be strong. In 1996/97, total foreign investment inflow was about \$5.6 billion, of which the equity component — both foreign direct investment and Global Depository Receipts — was about \$3.7 billion. This year, we expect equity inflows alone to touch \$5 billion. Our total foreign exchange reserves have crossed \$30 billion, equal to almost eight months of imports.

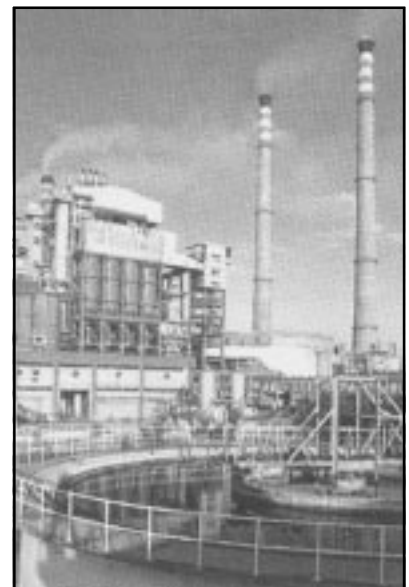
Demands on public expenditure are many and will escalate in a democracy where there are many equally deserving claims. Even so, I am determined to keep the **fiscal deficit** of the Central government under tight control.

In short, our macroeconomic fundamentals are sound.

The process of opening and deregulating the economy continues unabated. Permit me to give you a flavor of what has been accomplished by a 14-party coalition government that spans the entire spectrum of political, economic and social opinion. **My message is — invest in India not only for its promise and potential but, equally importantly, for its performance.** Our performance may not yet be stunning but it is definitely solid, robust and durable. The world knows what India must do but, sadly, is less informed on what has been done. What has been done may constitute small steps in the eyes of the world but are giant leaps judged by where we were just six years ago.

The **oil and gas industry** is in the midst of fundamental restructuring. We have announced that the Administered Price Mechanism for petroleum products will be dismantled in four to five years and tariffs brought down sharply. We are phasing out petroleum subsidies. Diesel is now on import parity prices. Subsidy will be confined to kerosene that is consumed as cooking and lighting fuel by the poor. Twenty-six exploration contracts and twelve production contracts will be signed with private companies, many of them American, over the next few weeks.

The learning period for **private power** that lasted about three years is over. Almost 5000 MW of IPP capacity is under construction and another 10,000 MW are poised for financial closure and will soon enter the implementation phase. We have identified 10,000 MW of coal pithead mega projects which will be offered to private investors through an international competitive bidding process. The tender for the first such 1000 MW power station along with the coal mines was issued last month. States like Orissa, Rajasthan, Haryana and Andhra Pradesh have initiated far-reaching reform measures to transform, financially and organizationally, their state electricity boards. These States are, incidentally, ruled by four different political parties.



In three States of India with a combined population of about half of the United States — Maharashtra, Madhya Pradesh and Gujarat — private basic **telecom** services will be launched shortly in competition with what the government provides. American companies are closely involved with two of these projects. Government monopoly over the provision of Internet services was ended last week.

Two **ports**, Pipavav and Dahej in the State of Gujarat, are under construction by the private sector, and at least five more in other States are on the anvil. In ports owned by the government, we allow leasing out existing assets of ports as well as private sector construction and operation of new facilities like container terminals, cargo berths, warehousing, dry docking and ship repair.

The detailed framework for private investment in **roads and highways** is now in place and 14 Build-Operate-Transfer (BOT) contracts will be awarded shortly. Over the next five years, about 4500 kms of two-lane national highways will be upgraded to four-lane and to world standards. We have announced the policy on tolls and more importantly have extended fiscal incentives to real estate development along highway corridors to make investment in these highways profitable.



Many of the **laws** that underpin economic activity are decades old in India and have outlived their utility. We have amended our arbitration regime to bring it in line with UNCITRAL rules. We have completely rewritten the Companies Act of 1956 and this is now before Parliament. The Foreign Exchange Regulation Act of 1973 has been recast into a Foreign Exchange Management Bill, which will be made public shortly. A new and transparent take-over code for companies has been put in place. This is already stimulating better corporate governance.

We believe that enhanced competition and focused regulation go hand-in-hand in strengthening the **financial services** industry. Almost all public sector banks, except two, now meet the 8% Basle norm for capital adequacy. There has been bit of a setback on opening of the insurance industry. The debate does not relate to opening up, on which there is majority support in Parliament, but rather to the extent foreign companies should be allowed to operate. I am confident that in the next two months, we will be able to bring insurance reforms back on track.

The **capital market** has witnessed a fundamental change and we are well on our way to a paperless trading system which will make for a cleaner, quicker and more transparent market. Twelve months ago, we launched India's first computerized securities depository. In this period, the depository has processed some half a billion shares. From January 15, 1998 all institutional investors — Indian and foreign — must use the electronic share depository to settle their transactions.

I have recounted at length some of the more significant initiatives that have been taken over the past few months. The very process of change is expanding the pro-reform constituency. We have had three governments at the Centre in the last fifteen months but the basics of the new economic policy, with its thrust on reforms, have not changed at all.

*(Continued on page 4)*

## Excerpts from Finance Minister P. Chidambaram's Address

(Continued from page 3)

Four weeks ago, Prime Minister Gujral met with President Clinton in New York. During the meeting it became clear that both countries desired to engage each other on a wide range of issues, the foremost being **trade** and investment. Two-way trade between the two countries has doubled between 1991 and 1996. Fully 19% of India's exports are to the United States and 12% of India's non-oil imports are from the US.

The next frontier to be conquered is **investment**. The US remains the largest new investor in India since 1991. Total FDI approvals from the US have been about \$10 billion; however, the actual flows to date are only about \$1.5 billion. This, of course, does not include investments flowing in through the Mauritius tax haven. If this is added, inflows from US companies would add up to about \$3 billion. During the meeting with President Clinton, we underlined the competitive edge of American companies in areas like power and petroleum and invited them to come to India in a big way. To the list of areas where US investors have a great opportunity, we can add telecommunications, airlines and airports, hotels, food processing and sports and recreational facilities.

I shall readily acknowledge that American companies, when they choose to invest abroad, have a variety of destinations to choose from. Why should they choose India? Allow me to offer **four compelling reasons why you must look at India seriously**.

First, India remains perhaps the **world's pre-eminent development frontier**. India is among the handful which simply have to expand at a furious pace. India is not just an expanding consumer market. It is a place where infrastructure has to be built to meet the needs and aspirations of over a billion people, and that is where there is an unprecedented opportunity for American business and industry.

Second, India is not just a low-wage country. It is a country that produces technicians, scientists, engineers and technical personnel of world-class. A survey of expatriate managers reported in the London Economist had placed India at the very top on the availability of **skilled manpower at competitive rates**.

Third, India has a **preponderance of entrepreneurial skills and entrepreneurs** who are taking on multinationals and global brands and competing effectively. With the increasing availability of venture capital and the freeing of licensing restrictions, there has been a mushrooming of new small and medium-sized companies, started and managed by professionals. American companies will find them enthusiastic partners.

Fourth, a market economy is founded on a **system of honoring contracts**, enforcing property rights and respecting legal obligations. India has a well-developed judicial infrastructure that has time and again demonstrated its independence, as in the Enron case. A number of independent regulatory authorities are also being set up in sectors that are being restructured.

Friends, India, like the United States is a completely open, fully representative and pluralistic democracy. And because we are open, there is a strong tendency to view us more critically and emphasize only the negatives. I am not suggesting that problems do not remain. But India is moving confidently ahead. With the help of our American friends, I am sure we will keep our trust with destiny before long.

**The full text of the Finance Minister's speech is available at the Ministry of Finance website at [www.nic.in/finmin](http://www.nic.in/finmin)**

# Economic Update

**Foodgrain Stocks:** Stocks of foodgrain stood at 17.8 million tonnes at the end of July 1997.

**Industrial Production:** During the financial year 1996-97 (April 1, 1996 - March 31, 1997) industrial production increased by 6.7%. Industrial production in the period April-June, 1997 increased by 5.2%.

**Infrastructure Industries:** During the period April-July 1997, production in basic infrastructure industries registered a better performance compared to the corresponding period last year. Electricity generation increased by 6.2%, Cement by 5.2%, Petroleum Products by 7.4%, Nitrogenous Fertilizers by 26.7% and Crude Petroleum by 3.2% while Saleable Steel declined by 3.9%.

**Money Supply:** During the current financial year 1997-98 till August 29, 1997 money supply (M3) growth was marginally lower at 4.7% as compared to 4.8% in the corresponding period of 1996-97.

**Foreign Trade:** In the financial year 1996-97, exports recorded an increase of 4% in dollar terms while imports increased by

6%. Exports increased by 1.8% in dollar terms during April-July 1997 as compared to their level in April-July 1996. Imports also increased by 7.9% during the same period.

**Foreign Exchange Reserves:** Foreign Exchange Reserves (excluding Gold & SDRs), were \$22.4 billion at the end of 1996-97 (March 31, 1997). These reserves have increased to \$26.4 billion at the end of August, 1997. This level of reserves is enough to finance more than 7 months of imports.

**Exchange Rates:** The average market exchange rate of the Rupee per unit of US Dollar, Pound Sterling, Deutsche Mark, French Franc and Japanese Yen was Rs.35.92, Rs.57.68, Rs.19.50, Rs.5.79 and Rs.0.30 during August 1997.

**Rate of Inflation:** The annual rate of inflation based on Wholesale Price Index (WPI) and measured on a point-to-point basis stood at 3.8% for the week ending September 20, 1997. The Consumer Price Index for Industrial Workers (CPI-IW) for August, 1997 recorded an increase of 4.7% over August 1996.

## India to Outdo USA in Buying Power: Economists

India and China, two fast emerging economies of the world, will soon overtake the United States in terms of purchasing power, the *Washington Post* quoted several economists as saying.

Buoyed by a booming US economy, these economists have dubbed Germany, the world's third economic superpower, France and all other European States except Britain as "newly declining states."

# Monetary and Credit Policy for Second half of 1997-98



*India's central bank, The Reserve Bank of India*

## **Background**

The Policy is set in the following background:

- Perceptible deceleration in inflation rate.
- Sharp downward movement in interest rates, both short-term and long-term.
- Government's market borrowing programme nearly complete.
- Stable foreign exchange market.
- Though industrial production in the first four months of 1997-98 was sluggish, demand expected to augment and result in improved consumption, investment and exports.
- Money Supply (M3) growth around projected trajectory of 15-15.5%.
- Strong growth in aggregate deposits.
- Non-food credit shows a pick-up in recent period.
- Strong growth in bank investments in corporate paper.
- Capital market somewhat sluggish.

## **Objectives**

The Policy attends to the twin-objectives of promoting price stability and ensuring availability of adequate bank credit for productive sectors.

## **Measures**

Some highlights of the Policy are:

- Bank Rate reduced by one percentage point to 9%.
- Cash Reserve Ratio (CRR) reduced by two percentage points and Statutory Liquidity Ratio (SLR) made uniform at 25%.
- Interest rates on domestic term deposits deregulated.
- Banks to prescribe a separate prime term lending rate.
- Interest rate on pre-shipment rupee export credit reduced by one percentage point.
- Bridge loans against equity issues/flows permitted.

- Improvement in credit delivery for sugar, small scale industries, trade, transport, services and housing.
- Ready forward in PSU bonds and debt securities permitted.
- Measures for further development of money and government securities market.

### **Rationale and approach**

The policy measures enunciated essentially reflect a multi-pronged approach to monetary management, facilitate the use of macro-economic and structural measures to deepen the financial markets as well as bring about integration of these markets. This is necessary to achieve financial stability and allocative efficiency. The thrust of the policy has been on reduction of direct methods of control and to use interest rates as signals to bring about efficient functioning of the financial system.

The measures aim at expanding the lendable resources of banks and reduction in the cost of funds without impairing their profitability. The deregulation of interest rates and the reduction of cash reserve ratio would give enough freedom to banks in the management of their portfolios so as to optimize their profits and productivity. It is expected that the gains arising out of these measures will be shared with borrowers.

The recent events in the international scene have demonstrated the criticality of the soundness of the financial system for maintaining macro-economic stability for ensuring sustained growth. In this context, it is imperative that banks, being the vital component of the financial system, should equip themselves to meet the challenges of the second phase of the financial sector reforms which will compel banks to operate in a more competitive environment. The response should be in terms of

improved organizational effectiveness and better risk management.

### **Commentary**

The Reserve Bank's monetary and credit policy for the second half of 1997-98 carries forward the process of deregulation of the financial sector and makes yet another attempt to increase credit off take by further lowering the cost of credit. Some of the deregulatory measures are significant. The RBI has let go the one deposit rate it still controlled - the rate on deposits up to one year; all that is retained is the minimum maturity period, which remains at 30 days. Banks have also been permitted to have separate prime lending rates for term loans of three years and above. Mutual funds have been allowed to invest up to \$500 million in overseas markets, and the overseas investment and borrowing limits of banks have been increased. These enhanced freedoms should push banks to compete more meaningfully amongst themselves and the financial sector in general to greater efficiency and resilience, factors that would stand the sector in good stead when it is called upon to deal with the forces unleashed by the full convertibility of the rupee.

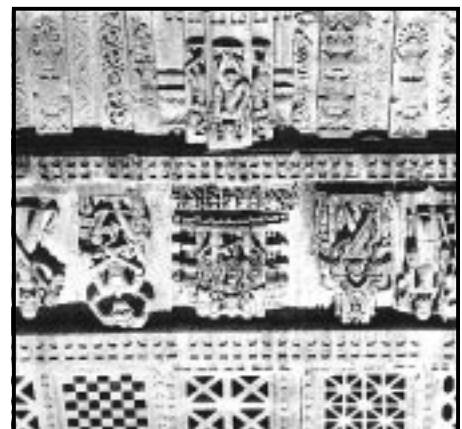
However, the focus in the run-up to the credit policy announcement was understandably not so much on deregulation as on what the central bank would do with regard to the bank rate and the cash reserve ratio (CRR). With credit off take sluggish and industrial growth in steep decline, the pressure, especially from industry, to induce a further reduction in interest rates has been substantial. The apex bank has responded with a reduction in the bank rate by one percentage point and a lowering of the CRR from 10% to 8%, the latter to be effected in phases over a five-month period.

***The full text of the Credit Policy is available at the Reserve Bank of India website at [www.reservebank.com](http://www.reservebank.com)***

# NEWS BRIEFS

- US-based **Scholastic Corporation**, claimed to be the world's largest publisher of children's books, is starting its India operations.
- Global software giant **Microsoft Corporation** has signed an agreement with Andhra Pradesh government to establish the "Microsoft School for Software Technology" (MSST) as part of the Indian Institute of Information Technology (IIIT) coming up in Hyderabad. Microsoft has also signed a MoU with Andhra Pradesh Technology Services (APTS) for "strategic technology alliance".
- The Industrial Credit and Investment Corporation of India (ICICI) has tied up with international giant **CapMAC** of the US to set up a 60:40 joint venture financial guarantee company. (Economic Times)
- **Textron** has set up a joint venture in India for providing commercial credit and consumer finance for automobile and white goods. (India Abroad)
- HCL Infosolutions Ltd. has signed a deal with **Dragon Systems Inc.**, one of the world's leading suppliers of speech and language technology, for marketing and supporting Dragon Systems' products in India. (India Abroad)
- **Federal Express**, the courier and express transportation major, has launched its India operations. (India Abroad)
- **Allied Signal**, a Fortune 500 company is setting up an industrial park in Gurgaon, Haryana, envisaging a total investment of about \$100 million. The park, which will be fully operational by 1999, will manufacture a wide range of high technology products ranging from amorphous metal transformers to aviation components. (Times of India)

**NOTE: This newsletter can also be seen at:**  
<http://www.indiaserver.com>



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