India faces double-digit inflation

Poor performance of infrastructure, populism, neglect, and the Gulf crisis conspire to institutionalize spiraling prices.

Despite brave claims by mandarins in India's Finance Ministry, that irrespective of fiscal problems the country's basic economy—agriculture and industry—is in good shape, the steep rise in prices of many mass consumption items indicates that this is not so.

India is expected to harvest a record 175 million tons of foodgrains this year, enabling foodgrain reserves to surpass the record 20-plus million ton mark of the mid-1980s. The industrial sector has clocked a vigorous growth rate of 9% or more, according to official statistics. But none of this "growth" has succeeded in keeping prices in check.

According to one estimate, the 1990-91 fiscal year (April 1990-March 1991) may end with a whopping 13% increase in wholesale prices over the previous year. Such items of mass consumption as foodgrains and petroleum products have led the price hikes. Since December 1989, foodgrain prices have gone up by 10%, edible oils by 20%, tea by 23%, processed food products by 12%, and mineral oils by 31%. All these hikes have boosted the wholesale index.

In the meantime, Finance Ministry officials' attention in the Shekhar government has been riveted to the unfolding fiscal crisis. First and foremost is the problem of depleted foreign exchange reserves, and accumulated foreign debt to the tune of $62 billion. Foreign debt servicing now eats up 28% of export earnings. Then there is a significant growth in domestic debt, which is close to $135 billion and about 34% of Gross Domestic Product. And there is the seemingly unbridgeable trade deficit, which in the first half of this fiscal year grew to $3.04 billion—an increase of 31.6% over the same period a year ago—despite a steady growth of exports.

There is also the miserable performance of some of the nationalized banks, into which some $450 million had been pumped last year to strengthen the capital base, and the inability to mobilize resources for the Eighth Five Year Plan (1990-94). Last but not least is the growing fear of a steep jump in future oil prices in the event of a Persian Gulf war.

Officials are now busy negotiating loan arrangements with the International Monetary Fund, while discussions on devaluing the Indian currency, measures to attract foreign investment, and a reduction of both imports and governmental spending are hogging the news media.

In the midst of such dramatic financial concerns, the inflationary price rises of essential commodities have been discussed only in whispers. Most economists admit that large governmental expenditures have given the inflationary tendency a firm boost. These economists' only "solution" to curb inflation is to advocate a tight money policy.

On the ground, there is ample evidence to suggest the real economy is in real trouble. The key to keeping prices stable is a smoothly functioning infrastructure. According to the *Economic Times,* India's premier economic daily, the key industries which constitute the infrastructural sector have performed poorly during this fiscal year. Production of electrical power, saleable steel, and cement remain well below target. Coal, crude oil, and petroleum products have slackened production. Hence infrastructure growth, which accounts for 30% of the industrial sector, has fallen to less than 3.5%, well below target.

At the same time, populist policies, a hangover from earlier years, and disinterest in the economy by the previous V.P. Singh government during its 11-month tenure, have had their own inflationary effect. The Bureau of Industrial Costs and Prices pointed out in a recent report that hiking foodgrain procurement prices steeply may have made some farmers happy, but also raised food prices. A subsequent $1.1 billion subsidy to enable the poor to buy food only partly offset the price rise. By Bureau calculations, food prices will come down only if both the procurement price and subsidy are abolished.

In its pursuit of political mileage, the V.P. Singh dispensation also fulfilled its electoral pledge to grant a $4.5 billion selected farm loan waiver. The move not only destabilized some banks, but has made repayment a problem throughout the farm sector. The total farm loan exposure of the banking sector could be as high as $12 billion.

The steep rise in crude oil and petroleum product prices reflects, beyond reduced Indian output, the impact of the Gulf crisis. And since transport and distribution of all products involves mineral oils, the effect of such price hikes is felt throughout the economy. Should the Gulf crisis—the only short-term variable in India's balance of payments equation—continue or worsen, India will have to cut back on importing goods directly related to industrial production. With factories idled for lack of raw materials, prices can be expected to continue to soar.