

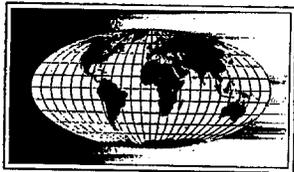
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*Economic  
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6 June 1998

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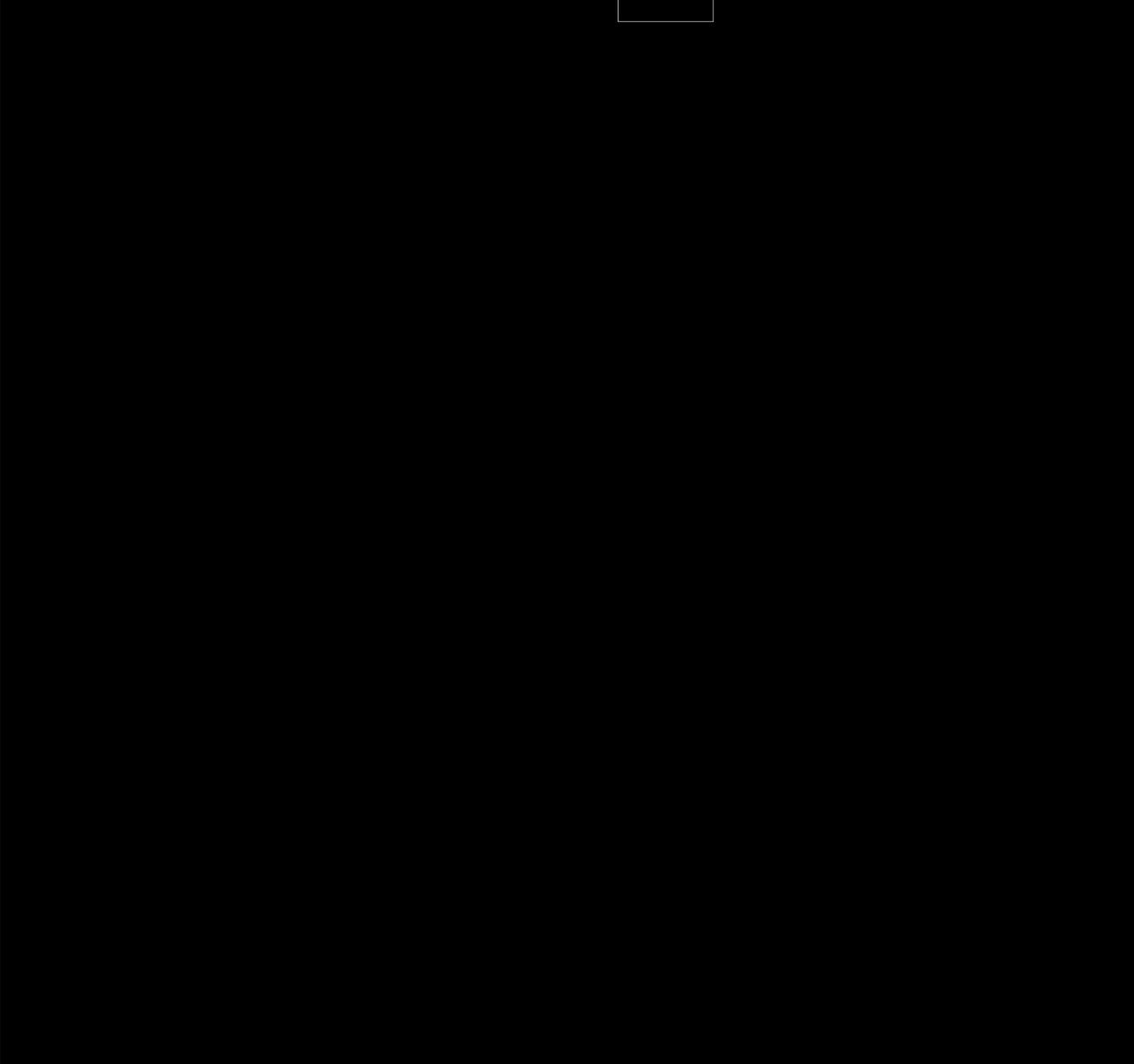
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India Plays With Inflation Fire



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**The BJP's Economic Vision: Main Street, Not Wall Street** [REDACTED]

The budget is further evidence that the BJP means what it says. Just as the nuclear tests aimed to change India's place on the international stage, the budget seeks to shift economic and social priorities in favor of middle-income Indians in small cities, towns, and the countryside, as promised in the postelection manifesto "Agenda for Governance." While monied interests bemoan the lack of a capital gains tax cut and permission for companies to buy back their shares, editorials in the local, indigenous-language press have applauded such features as:

- Greater access to credit for farmers and small-scale industrialists.
- Spending boosts for education, public health, clean water, and a strong defense.
- Tax increases on the rich and the products they consume such as gasoline.
- Repeal of the Urban Land Ceiling Act, which has restricted new housing construction.
- Removal of regulations that block economic activity and simplification of procedures to ease regulatory burdens [REDACTED]

Finance Minister Sinha's presentation speech spent little time on economic performance goals—the normal subject of the budget presentation—and in subsequent press interviews he expressed little concern about possible consequences such as inflation or a weaker rupee. Instead, he emphasized a social agenda grounded in the BJP's economic and social vision of India: thriving Indian farmers and artisans, industry unfettered by regulations and protected only when necessary from predatory foreign competitors, and better access for all Indians—including women—to basic amenities such as clean water, public health, housing, and education.

- It appears that the BJP is willing to risk and absorb some economic pain to carry out its social and economic agenda, just as it is willing to endure sanctions over nuclear weapons. [REDACTED]
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- [REDACTED]

## India Plays With Inflation Fire [REDACTED]

The first budget of the BJP-led government, presented last Monday, puts favored sectors and social programs ahead of general economic goals and could lead to double-digit inflation this year. Finance Minister Sinha's budget calls for a 14-percent boost in spending to \$64 billion, and projects 7- to 8-percent GDP growth to offset it.

- GDP grew only 5 percent during the last fiscal year.
- Major public investment hikes include 25 percent for agriculture and rural programs to \$3 billion, 42 percent for energy to \$7 billion, 29 percent for communications and transportation to \$7.4 billion, and 32 percent for social programs to \$3.8 billion. [REDACTED]

National security received a boost with a 14-percent nominal increase for the Defense Ministry to \$9.8 billion and increases of more than 60 percent for the Departments of Atomic Energy (DAE) and Space, each of which will now have about \$330 million. If inflation remains near present levels, these nominal increases will translate into an 8-percent real increase, the largest for defense at the beginning of any fiscal year this decade.

- Defense has usually received a midyear supplementary increase, however, and the raise this year so far is not out of line with past total annual increases.
- The DAE's increase restores funding to levels of the early 1990s. DAE had been reeling from budget cuts for most of this decade. [REDACTED]

Sinha is gambling that increased spending and deregulation will stimulate growth. Critics, more pessimistic because of the economy's recent sluggish performance and poor response to monetary stimulation, say they will only deprive the private sector of capital and fuel inflation.

— Sinha is seeking to cut the fiscal deficit from 6.1 to 5.6 percent, but he emphasized that the government considers growth more important.

— Inflation early last month hit 6.35 percent, the highest since April last year. [REDACTED]

Most public and business community reaction has been negative or neutral. Few businesses appear enthusiastic about Sinha's strategy, according to US diplomats and press reports.

- The Bombay Stock Exchange, having gained on Monday, fell in a special postbudget trading session that night and again on Tuesday. [REDACTED]

## "Mildly Protectionist" External Policy [REDACTED]

Sinha levied an 8-percent, across-the-board import duty to "level the playing field for domestic producers," but commentators expected more, given the BJP's antforeign rhetoric. Duties were adjusted up or down depending on whether the government judged that an industry could stand competition, in keeping with a campaign pledge that Indian industries will not be protected forever. [REDACTED]

Sinha said he seeks to double foreign direct investment in two to three years by creating an investment friendly environment. He promised projects will be approved within 90 days, raised limits on foreign ownership, and created numerous tax holidays for targeted sectors.

- In an interview, he said an attractive investment climate will counter the negative effects of sanctions, but critics complained the initiatives to attract foreign investment are skewed toward Indians living abroad at the expense of foreign investors in general. [REDACTED]