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News for the hour

Reforms were easier to do in 1989: Rahul Khullar

Nayanima Basu/New Delhi - Apr 27,2012 00:53 AM

India's merchandise exports crossed the government's target of $300 billion in the last fiscal and reached $303.7 billion. But according to Commerce Secretary Rahul Khullar, the present fiscal is going to be tougher. In an interview with Nayanima Basu. Edited excerpts:

Last fiscal we saw the highest-ever trade deficit in the history of India's foreign trade. Do you see any remedy for this?

Exports grew 21 per cent in FY12 over FY11 but imports have grown by over 32.1 per cent year-on-year — that is the real cause of the problem. Within imports, two specific sectors of petroleum products and gold and precious metals are the big-ticket items. Basically, gold and bullion imports this year had been $19 billion and petroleum imports had been $50 billion, so these have added $69 billion to the trade deficit and that explains its expansion. At $185 billion, we are basically looking at a trade deficit that is in excess of 10 per cent of GDP and that is very large. The silver lining, so to speak in gold imports, which increased this year by over 45 per cent, is that it is unlikely to grow as rapidly this fiscal quite simply because domestic inflation is declining so gold's value as an asset will weaken. Then there has been an increase in tariff on gold. So, the growth in gold imports will be tempered because of all these things.

On petroleum, there have been two effects. One, there was a very large increase in prices, which means you effectively paid a price that was, on an average, 40 per cent higher in FY12 over FY11. So that is the explanation for higher petroleum product imports. At the same time, I can also say this sort of growth would not be achieved in 2012-13 simply because it does not seem likely that crude prices would increase by 40 per cent on an average this fiscal. Thus, there will be tempering of growth in oil imports because international prices will not increase as much and simultaneously there would be some pass-through effect domestically. So, both on the supply side as well as the demand side there will be some positive news.

The sectors that face difficulties, which are not related only to external prices but more to domestic supply constraints, are edible oils, fertiliser and coal. Coal imports are 80 per cent higher, fertiliser imports are 60 per cent higher and vegetable oil is 48 per cent higher in FY12 over FY11. Now, those are very large import increases, accounting for an extra $15 billion in the import bill. We cannot carry on like that and we need to do something on expanding the domestic production of these products. This will require policy action.

Is this deceleration in exports is going to continue? What is your outlook on India's trade for 2012-2013?

This fiscal is definitely going to be more difficult for trade than FY12. In 2011-12, it was a story of two halves. The first half of the year was very good and exports were booming and in the second half growth rates almost collapsed. This year, as we begin, there is already nothing to cheer about in terms of news from our markets. Yes, the US economy has started reviving but it is not clear how long that will go on. The news in Europe is not good. Many economies are going through the problems of exchange rates adjustments like in Brazil. Argentina, on the other hand, has introduced an import control regime. So clearly, the atmosphere is far from positive. It would be premature to guess but I would imagine that even getting 20 per cent growth this year will be hard.

The Prime Minister's Economic Advisory Council had projected the current account deficit (CAD) at 3.6 per cent of the GDP for FY13.What do you foresee keeping in mind a ballooning trade deficit?

In 2011-2012, we will end up with a CAD in the neighbourhood of four per cent or more. The forecast for FY13 was 3.6 per cent. I agree with that because exports would grow at a slower rate but imports growth would slow perceptibly owing to the reasons that I outlined. And, thus, I believe it would be possible to compress the CAD to 3.6 per cent. All this is predicated on several factors. A sudden spike in the prices of our imports or on food items can make the calculations go haywire.

Of late we are seeing some serious data reporting problems by the government. It started with the GDP data, then exports and now IIP. Isn't this detrimental to India's image with international investors?

Let me start with exports, since I was responsible for it. Let us be clear on this. I was the first person who admitted that a mistake has occurred and it was only once. The moment I came to know, I immediately corrected it and, as I have maintained many times, it is better for us, who are releasing the data, to spot mistakes and admit to them immediately because it restores credibility in the data and in the data gathering process. Second, why does it happen? Well, for most part, it is a human error. Also, every time data is released, it is provisional and I have always maintained that caveat. I agree that not only investors, but businesses and clients and everybody should have faith in our numbers, be it IIP, GDP or wholesale prices. If we keep revising the numbers every other day or if we make major corrections, then there is a factor of unreliability that comes into play. Saying such errors impact investment decisions is carrying the criticism too far.

Recently, you had said the crisis today is reminiscent of the 1989 crisis. But foreign exchange reserves then were in a bad shape, today it is different. So how do you draw the similarity?

What I said was many problems we face today and many of the solutions to them we know and we have known for quite some time. In that context, I had said in 1989 we were drawing up a list of things that the new government should do and we had mentioned setting power tariffs right, sorting out coal since Coal India prices were very poor, we had problems with food subsidies and we needed to bring the fiscal deficit under control and get a sound fertiliser policy. Today, the sectors are the same but the problems have changed but the gravity of the problem is no less serious. I said in 1989 the central utilities did not have money and could not pay the coal companies. The difference today is that power generation companies in the states are not recovering enough from their downstream distribution and they cannot pay the coal companies. Entire power projects have been set up but few supplier arrangements are tied up. Some of these problems are getting solved as we speak but the point I was trying to make is it is not that we don't know what the problems or the solutions are, we have known them for the past 20 years. I think the inability of our system to put things together and implement is what is costing us.

Another point I made that day was it was easier doing reforms in 1989 than in 2012, quite simply because all the low-hanging fruit are all done and over with. Now we have to take care of the much more difficult parts of reforms. Then there is the problem of counterfactuals, which is that it is one thing to tell people that we will grow at six per cent but today growing at eight per cent has become a reality, so when your growth slips, everybody is willing to believe the worst. No one is willing to give latitude or listen to another point of view. Right now, over the last one year or so, we have seen all sorts of accusations being made pertaining to corruption, policy matters, governance and all. And somehow, each time that happens, the public is willing to believe it, industry is willing to believe it. But there are other difficulties involved and I think there is a need to think more carefully before jumping to conclusions about what is causing what. Finally, I believe that some things have to be done immediately.

It is my personal view that citizens must learn that they need to pay a higher price for some goods because without that there would be no conservation, there would be no restriction on demand because implicitly we are subsidising what we are consuming. We cannot afford that luxury anymore because we then get clobbered on our fiscal deficit and balance of payments. If oil companies are in the red, at some point that has to be corrected. Similarly, I believe that we need to do something urgently on fertiliser and food prices.

Lastly, central issue prices were last increased eight years ago. Prices cannot be kept frozen like this. And it is not as if poverty has not declined and it is not as if incomes have not increased in the past seven to eight years. So everybody's capacity to pay has increased. I do not see why rice will be sold at '2 and we cannot increase it to '3. Has the paying capacity of our poor not increased sufficiently to pay for that? I am not underestimating the political difficulties in taking these decisions. Today, we cannot say let's forget about fiscal prudence but let's be fiscally-profligate and growth will take care of the rest.

Finance Minister Pranab Mukherjee recently said the government will take sufficient measures to boost investment.

We have seen the RBI take steps towards that. But looking at a limited fiscal room, do you think it is possible to take more measures?

Honestly, the problem is fiscal manoeuvre is very narrow and that is because there is a limit to which expenditure can be cut and tax revenues can be increased. To that extent, we need to be able to leverage every dollar or every rupee of public expenditure and get the best out of it. That is where the public-private-partnership comes in. The second area is to recognise that there are some sectors where a huge injection of capital is required and that is not forthcoming from public coffers, and one has to rely on private coffers, which themselves cannot do it. So you have to then depend on external capital in the form of FDI [foreign direct investment]. This realisation has to dawn on all of us collectively. So decisions on opening up sectors for FDI and on leveraging public-private investment have to be taken and that is the only way to go. It is simply not possible to look elsewhere for capital.

There's a lot of debate on the recent Budget proposals on retrospective tax amendments and provisions under General Anti-Avoidance Rules (GAAR). How do you view these proposals and do you think it would hamper foreign capital inflows?

There is more heat than light right now. Let things cool down, the Budget has barely been presented. Everybody has agreed that as a general rule you should not be doing it but there are always exceptions and provided we can make sure that the exceptions are one-off and that India would not resort to retrospective taxation at every turn of events, then I think we should be able to limit damage. On GAAR, my general perception is that provided the contours are clear and not open ended, people will be able to live with it. The difficulty is when GAAR is open-ended and virtually any measure can be justified as anti-avoidance rule and they can look into your behaviour on the excuse that it is anti-avoidance — that would become a problem. Asurance has to be given to both the domestic and foreign corporate sectors and to individuals.

Coming to your initiatives in creating a stable trading relationship with Pakistan. This month marks one year since you took the first step and had your first meeting with Pakistan Commerce Secretary Zafar Mahmood. When do you think India will finally take the crucial steps of allowing FDI from Pakistan and liberalising the visa regime?

Well, first, the credit for all this goes to both the political leaders and the commerce ministers for providing a clear strategy. The credit also goes to a very brave set of bureaucrats in Islamabad who are working overtime and cooperating with us. Yes, things have moved much faster than anyone anticipated in the last 50 weeks. Now we are clearly on a firm path towards trade normalisation. In less than a year Pakistan has moved from a positive to a negative list and the trade infrastructure at Attari-Wagah has become operational. We have signed agreements on customs cooperation. Progress has been made on trade in electricity, power and petroleum products. Now we are also progressing on establishing banking channels and allowing FDI from Pakistan.

I am going to Islamabad next month and hope to achieve further progress on these and draw up an even more ambitious agenda for the next year. The issue of FDI will be handled by other departments but it will be done soon. As far as visas are concerned, the home secretaries are meeting in Islamabad towards the end of May and, hopefully, at that point of time the visa agreement will be signed heralding a whole new visa regime that will be far more liberal than what it is today.

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