

go for this. . . . I don't think there will be any U-turns.

**Q:** You're not worried about populists saying, "We've got enough foreign exchange, please get out now"?"

**Mansa:** No. There was a major scam on the Bombay market two years ago, which was a catalyst for anyone against foreign banking to rise up and try to produce sanctions and to try to exclude foreign banks.

But there is no doubt now that the Indian government feels that it needs the major foreign banks in a very big way to assist with the liberalization—and to be in place to assist the major new trade flows which India will soon have as a result of liberalization. Banks such as ours, and also Citibank, Bank of America, Hongkong and Shanghai, are absolutely vital to this process. There doesn't seem to be any sentiment contrary to foreign banks. . . .

**Q:** Minister Singh will be able to ride straight on?

**Mansa:** He's had a rocky time, but now this is an issue of which he's in control, yes.

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## Interview: Gregar Dolenc

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*Mr. Dolenc, World Bank loan officer for India, was interviewed in Washington.*

**Q:** Will the Rao government backpedal on reforms now that the public is so upset about the plague outbreak?

**Dolenc:** Have you seen any indication that they are backpedaling? The answer is no, they won't. The reforms are on course. It's slow, but it's on course. . . . Anything that happens in India can be made into a drama, but it's not necessarily a real drama. What have you seen in India, which has reversed the flow of foreign investment? Anything? We have not seen any such thing.

**Q:** What is the size of foreign investment in India?

**Dolenc:** The investment flows to India in fiscal 93-94 ended March 31, 1994 was to the tune of approximately \$5 billion, of which direct investment [in factories] was 20% and the rest was portfolio investment [hot money, stocks—ed.]. Based on what I've seen since then, such a flow has essentially continued at comparable levels. Prior to the opening in late 1991 the average inflow was perhaps \$200 million per year.

**Q:** How do you judge India's budget deficit?

**Dolenc:** We think that the fiscal discipline is being maintained. However, notwithstanding, the fiscal deficit is still too high. The deficit must be controlled in order to handle the stock of government debt.

What must be looked at is that the fiscal deficit in India;

the stock of public debt entails problems not dissimilar from those of the United States. About one-third of the budget is interest payments on the debt, and the servicing costs are even higher, quite substantial. In addition you have obligations on current expenditures. . . . So the government has precious little room left for investment. . . .

**Q:** Won't there be pressure to increase social and health spending because of the plague outbreak?

**Dolenc:** Yes, but so what? Social spending is under control; they are trying all sorts of cost-saving measures. They have improved collection of tax revenue, the shortfall of which in '93-94 caused the deficit.

The point is that a large part of U.S. government current expenditure is circumscribed by the fact that it has to maintain the debt service at market terms. You mentioned social spending in India. The government has little room to increase social spending because their existing revenues are earmarked already at the gate.

Singh has made changes to cut off the government's former unlimited access to borrowing from the Reserve Bank of India [central bank]. . . .

In the past, the banking sector was nationalized and the banks were forced to hold in their portfolio a minimum amount of government securities. . . . The government was at liberty to offer to pay any rate it wanted, which resulted in relatively cheap servicing costs on the public sector debt. This prompted too liberal spending. . . .

So within India's reforms one of the key events which happened this year was that the government has now been subjected to servicing its debt, the bulk of its debt, at market terms. This is a big element of the stabilization plan. . . . So the low-cost funding the government has used in the past will now be subjected to market pressure and such financing will be substantially controlled. . . .

The rates on the old debt were in high single digits, which is relatively cheap compared to what the market will charge now . . . 11 or 12%.

There was also "priority lending," in which financial institutions, government and private, had to have a certain share of their portfolio invested into a priority activity, i.e., agriculture, rural credit. That will have to go. At present, much has been eliminated, statutory reserves have been reduced, mandatory cash reserves have been reduced, much has been done to free the banks from previous controls—but there is still quite a bit of control and these things will have to go.

**Q:** Is the World Bank now going to lend separately to state governments?

**Dolenc:** The World Bank can only lend with the Union government guarantee. Some states need to restructure their finances because they won't be viable in the long run, provided the federal government favors such an

operation. We can't just walk in.

**Q:** What kinds of reforms do you want the state governments to undertake?

**Dolenc:** The revenue base is not properly developed. Their expenditures could be streamlined, collection has to be improved. Spending for human resources in some cases could be improved, be better targeted to get more bang for the buck. We would not be lending for current expenditures, but rather to improve the system. Consolidation of state finances, having states acquire market training so they can issue their own securities. . . . We are thinking about it but we have not yet approved a loan for this type of program. In the future we would.

**Q:** The economy is 70-80% agricultural?

**Dolenc:** Seventy percent of the population derives their livelihood from the land, but that's not the share in GDP. The share of agriculture in GDP is about a third. Agriculture is 38%, industry is 26%, and services are 36%. Services are very large; they also include transportation, not just financial services. There is also tourism.

**Q:** But will Singh be able to get rid of the agricultural subsidies?

**Dolenc:** These are issues which clearly need to be addressed, especially as the ability of the fiscal budget to support these subsidies is beginning to shrink, so by force, they'll have to address it. It's not something you just take scissors and cut.

The fact is that India solved its hunger, food production and distribution problem, by intervening with a large spoon. Now that the food production problem and distribution and feeding of the population is solved, now the time comes for this system to gradually become self-sustaining, which means phasing the subsidies out. But that is a long process and they're not there yet. So it is a problem.

For example, electric power is delivered to farmers at nominal rates, and even that is not collected; it's a major problem, probably the first one to be dealt with. Then comes the problem of subsidized fertilizer. Food production is market based, why should you really require subsidies?

But to disassemble such a system in India without disrupting the production is a major task, it should not be taken lightly. Rather than throw agricultural production into disarray, having seen what's happened to Russia, Indians want to be very certain that they're not causing more disruption under the guise of "bringing market forces to bear" in agricultural production.

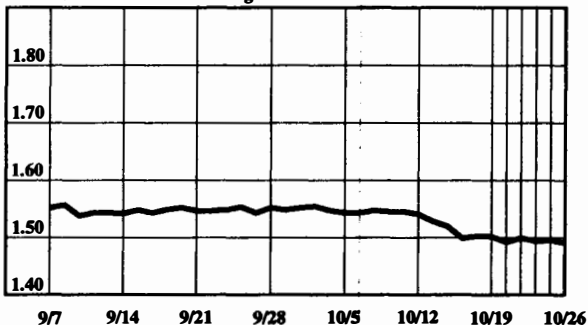
**Q:** Minister Singh has the support of the World Bank, then, in doing this gradually, but in doing it?

**Dolenc:** It's an ongoing dialogue but clearly the bank would say "if subsidies have to be targeted, subsidies have to be targeted; they must be cut."

## Currency Rates

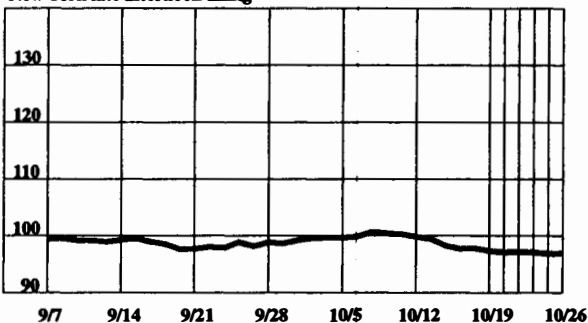
### The dollar in deutschemarks

New York late afternoon fixing



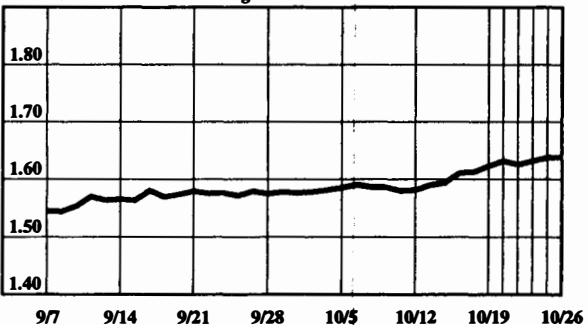
### The dollar in yen

New York late afternoon fixing



### The British pound in dollars

New York late afternoon fixing



### The dollar in Swiss francs

New York late afternoon fixing

