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As Growth Slows, India Awakens to Need for Foreign Investment

By VIKAS BAJAJ

NEW DELHI — When India’s finance minister, Pranab Mukherjee, flew to Chicago recently to address a group of American executives, it was to deliver an urgent message: India is still open for business.

Usually a cautious speaker who offers only vague promises, Mr. Mukherjee eagerly promoted specific new deals from New Delhi, where the national government has become alarmed by the sudden slowdown of India’s economy.

He listed pro-business policies his government recently approved or soon would: foreign individuals could invest directly in the Indian stock market; overseas specialty retailers like Gap could open wholly owned stores in the country, and bigger retailers like Walmart would soon be admitted. And though Mr. Mukherjee did not cite it, he could just as easily have mentioned a proposal the cabinet is considering to let foreign airlines buy as much as a 49 percent stake in India’s airlines.

“I urge you to seize this moment and contribute to our collective prosperity in the times to come,” Mr. Mukherjee told his audience, the Chicago Council on Global Affairs.

The flurry of activity by the Indian government has helped push Indian stock indexes up by 15 percent this year, and the rupee has climbed 8 percent against the dollar.

Skeptics wonder, though, whether Indian politics will really allow Mr. Mukherjee and his boss, Prime Minister Manmohan Singh, to force significant change on the nation’s hidebound protectionism. But there is no question that after years of taking rapid economic growth for granted, the government is finally awakening to the need for new policies and greater foreign investment.

The change is occurring as analysts and India’s central bank conclude that growth — which was at 8.4 percent or higher for much of the last decade — will fall sharply to 7 percent in the current fiscal year and remain sluggish in the next one, which begins in April.
The signs of new salesmanship from Mr. Mukherjee are a notable departure from his demeanor, and that of other Indian officials, for much of 2011, even as their economy was slowing and inflation was gathering steam. Preoccupied by a big anticorruption protest movement and internal bickering among politicians, officials tended to dismiss the gloomy data as unimportant or as temporary setbacks.

But this year, Indian leaders have begun publicly acknowledging the nation’s economic problems.

“The growth slowdown was a nice wake-up call for us,” Kaushik Basu, the chief economic adviser to the Finance Ministry, said in an interview.

Although Mr. Basu noted that some of the slowdown could be attributed to global economic problems, policy makers now recognize that “decision making had slowed down, reforms had slowed down,” he said. “This has the saving grace of avoiding the trap of denial, which is always a risk in policymaking.”

And so officials are pushing ideas that would have seemed anathema just a few months ago — including the proposal to let foreign airlines buy big stakes in Indian airlines. While nationalist sentiments have long blocked such a move, steep losses at some big airlines, including Kingfisher Airlines, Jet Airways and state-owned Air India, seem to be forcing policy makers to reconsider.

A new aviation minister, Ajit Singh, who joined the government in December, has been pushing the foreign investment proposal since a severe cash squeeze at Kingfisher late last year forced the airline to cancel scores of flights and delay paying salaries to pilots and other employees. Many analysts say the company, which is owned and run by the flamboyant liquor baron Vijay Mallya, probably cannot survive unless it finds new investors.

Before Kingfisher’s troubles became big news, bureaucrats quibbled for months about whether foreign airlines should be allowed to buy stakes of about 25 percent. Current rules do not allow any investment by foreign airlines in Indian carriers — although other foreign investors can own up to 49 percent. Soon, the Indian cabinet is expected to consider letting foreign airlines also invest at that level.

In January, the government began allowing retailers that sell just one brand of products, like Gap or Nike, to open wholly owned stores in India — as long as they buy 30 percent of their goods from Indian artisans and small Indian companies.
The chief executive of Ikea, the Swedish furniture and furnishing retailer that has long hoped to set up stores in India, publicly balked at the 30 percent requirement, saying it might force Ikea to table its India plans. That prompted the Indian commerce minister, Anand Sharma, to meet in Paris with the Ikea chief, Mikael Ohlsson, hoping to allay his concerns.

It is unclear how effective that was, or what potential inducements Mr. Sharma might have offered. But according to the government’s account of the meeting, Mr. Ohlsson told Mr. Sharma that he would soon return to India to speak to officials. An Ikea spokesman did not respond to a message seeking comment.

Investors and analysts said they were heartened by the single-brand decision, which was quickly followed by Starbucks’s announcement that it would proceed with long-simmering plans to enter India — even though its initial venture, this year, will be in collaboration with the Indian conglomerate Tata.

But many India watchers say they remain unconvinced that Indian leaders can push through bigger changes — such as opening India to multibrand retailers like Walmart or revamping government policies that have prolonged market and agricultural inefficiencies by awarding $33.8 billion a year in subsidies for food, fuel and fertilizers.

The steps that have been taken indicate “some appetite for economic reform,” said Mark Martyrossian, a fund manager for Tiburon Partners, a London-based firm that has invested in Indian companies. But he predicted the process would be slow and painful because of the “vested interests at play.”

Skeptics point to the politically disastrous effort by the government late last year to open India’s $500 billion retail market to foreign companies.

Less than two weeks after Prime Minister Singh’s administration announced that it would admit big retailers like Walmart and Tesco, it indefinitely suspended the decision. The reversal occurred after a Singh government ally — the Trinamool Congress led by the firebrand politician Mamata Banerjee — threatened to withdraw its support. Losing Ms. Banerjee’s backing could have forced the government to hold new national elections more than two years ahead of schedule.

Ms. Banerjee and other opponents of the retailing plan argued that foreign merchants would hurt small shopkeepers. Proponents, including Mr. Mukherjee, the finance minister, struggled to make the counter argument that foreign supermarkets would help farmers who must sell their produce to an oligarchy of Indian wholesale traders.
“It’s really going to be an uphill battle to convince investors that India is the place to come to,” said Eswar S. Prasad, an economics professor at Cornell University who often advises the Indian government. “The sense right now is that one politician’s whims can very easily close arms that have been opened with great difficulty.”

Professor Prasad argued that India must further liberalize its economy and welcome foreign investors if it is serious about bolstering growth and creating more opportunities for its population of 1.2 billion.

Technocrats like Mr. Basu, the economic adviser to Mr. Mukherjee and also a professor at Cornell, agree with those recommendations in principle. But they have had difficulty convincing India’s divided polity of the merits of that approach.

Much will depend on how Indians vote in elections for state legislatures under way in five states including Uttar Pradesh, India’s largest, with 200 million people, and one of its poorest. A victory for the Congress Party, which rules in New Delhi but controls only two of the five states voting, could empower the government.

Soon after the elections, the results of which will be announced March 6, Mr. Mukherjee plans to present the government’s budget for the coming fiscal year. Based on recent comments by the minister and his aides, some analysts expect him to act to rein in India’s deficit, while proposing new economic changes.

Surjit Bhalla, an economist and fund manager in New Delhi who has long been critical of the government, predicted that India’s slowing economy and ballooning deficit would force policy makers to change their approach.

“They have learned their lesson,” Dr. Bhalla said. “I have not been more optimistic on India than I am now in a long, long time.”

This article has been revised to reflect the following correction:

**Correction: February 13, 2012**

An article on Wednesday about India’s renewed efforts to attract foreign investment misstated the name of the organization that hosted a recent address by India’s finance minister, Pranab Mukherjee, to American executives. It is the Chicago Council on Global Affairs, not the World Affairs Council of Chicago.