



India's quiet reform movement

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Time flies. Later this month sees the second anniversary of the election of Narendra Modi as India's Prime Minister. At the time, expectations were sky high that Modi could set his country on the path to economic success and improve its global standing.

Satisfying or even exceeding the hopes and expectations of well over a billion people was always going to be an uphill battle. But Modi has done admirably well thus far.

A notable achievement that Modi has fulfilled his promise on is bankruptcy law. This can rarely be considered exciting but the Insolvency and Bankruptcy Code 2016 represents a watershed moment. The new code promises to streamline and accelerate the process through which creditors can recover their money when a company goes out of business.

This is important because bad debts are a big problem for the country's government-controlled banks. They are also preventing these state-backed lenders from fully supporting the infrastructure investment that is vital for Prime Minister Narendra Modi's reforms.

India's fractured insolvency regime means the current process takes far longer than in many other major economies, while recovery rates are typically lower.

The new code will help clear up bank balance sheets to allow lending for more productive purposes. This will, in turn, help support economic growth within a more stable financial system.

Yet the significance may run deeper. This legislation was approved by the upper house of parliament, a body packed with Modi's political opponents, which has routinely blocked other reform efforts to undermine the government.

It was a refreshing change to see opposition politicians set aside party politics to work with the ruling Bharatiya Janata Party (BJP). This period of cooperation may not last, but it will serve as a powerful example of what can be achieved when other items on the reform agenda are revisited later.

Sentiment towards India has weakened since last year as the reform story loses its lustre.

While change is taking place it is the sort of incremental, under-the-radar transformation that can easily be overlooked.

For example, individual states are making progress securing land for infrastructure development, even if the politicians cannot agree on new legislation to achieve this at a national level.

A separate drive to slash red-tape and boost transparency has led to the creation of one-stop-shop online and mobile portals, as well as simplified registration procedures for starting businesses.

One scheme in Delhi, soon to be adopted in other parts of the country, has cut the time required to incorporate a company to just one day – something that is unheard of in the emerging markets.

Yet the pace of reform appears too slow for investors and voters alike. The MSCI India index has fallen over 12% since the record high reached in March last year. Some two years after India's electorate swept the BJP to power, newspaper headlines speak of unfulfilled pledges and disillusionment.

But if these people had been honest with themselves they would have acknowledged that hopes for rapid change were unrealistic. India's vast geography, messy democracy and legendary bureaucracy made sure of that.

Anyone who has been stuck in gridlocked Delhi will appreciate that few things move fast in a country where almost 600 insolvency cases remain unresolved after more than 20 years.

Given the size of the task facing Modi and his government, we should give credit for what has been achieved in such a short time.

India's economy is certainly in better shape than it was even a few years ago – inflation is down, as are interest rates. This is a big deal in a country where prices used to rise at a double-digit pace.

Foreign exchange reserves of some US\$362 billion are near record levels. India has been a key beneficiary of the windfall gains from cheaper oil, but policymakers should be praised for seizing this chance to scale back expensive fuel subsidies. Government finances are healthier.

There's also evidence to suggest that senior public officials are more responsive; that efforts to open bank accounts for millions of rural Indians (so that subsidy payments go straight to recipients) have reduced opportunities for corruption by intermediaries; that coal production has increased, as have contracts awarded to build more roads.

A few of these initiatives were inherited by Modi, but whereas the previous government was unsuccessful in getting some off the ground, the current administration has made them happen.

That said we won't be seeing the impact from the Insolvency and Bankruptcy Code anytime soon. There are some 70,000 bankruptcy cases that will take years to clear and new institutions need to be set up, while a new class of insolvency professional will need to manage the resolution process and debtors' assets.

But at least we can say with confidence that two years on, Modi's government is putting India on the right track.

Image credit: Bloomberg/Bloomberg/Getty Images

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