Expanding U.S.-India Economic Co-operation

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Thank you, Ramesh. I am pleased to be with you today for the American Chamber of Commerce's 13th annual meeting. Ladies and gentlemen. I would first like to congratulate and thank you, the members and staff of the American Chamber of Commerce in India, for all your efforts this past year in strengthening the economic and commercial ties between the U.S. and India. We at the Embassy look forward to further collaboration in the year ahead.

I would also like to take a moment to congratulate our representatives from the Boeing Company if they are in the audience. On Tuesday Air India awarded a contract worth $ 8.5 billion (rupees 30 crores) for the purchase of as many as 50 Boeing aircraft for its growing fleet. I would also like to congratulate General Electric since all the engines on the planes will be manufactured by GE. Well done.

We look forward to many more such success stories in the future. We have made great progress but there is much that needs to be done.

I have been asked to speak today on "Expanding U.S.-India Economic Co-operation." That's a timely topic. It has been the theme of several high-level contacts between Indian and U.S. leaders in recent weeks. The U.S. commitment to develop deep economic and commercial ties with India has never been stronger. In March Secretary of State Condoleezza Rice visited New Delhi to underscore the importance of developing those ties.

That visit, along with one by Minister of External Affairs Natwar Singh to Washington earlier this month, marked a notable watershed in further expanding the strategic partnership between the U.S. and India. Our two Ministers agreed that it is time to broaden and accelerate our strategic relations on a number of fronts:

- Secretary Rice and Minister Singh launched a strategic dialogue between our two countries;
- they established a joint working group to discuss how the U.S. and India can expand cooperation in space;
- they agreed to accelerate progress in the Next Steps in the Strategic Partnership Initiative by combining Phases 2 and 3;
- and they formally announced an energy dialogue to be headed by U.S. Secretary of Energy Sam Bodman and Deputy Planning Commission Chairman Montek Singh Ahluwalia.

The energy discussions will address energy security, renewable energy, and -- for the first time -- the civilian use of nuclear power. We also are revitalizing the Economic Dialogue by introducing a CEO Forum. This will give the private sector greater input into the process.

In New Delhi recently, U.S. Secretary of Transportation Norman Mineta and Civil Aviation Minister Praful Patel signed the "Open Skies Agreement." This will empower the private sectors in both countries to expand and improve air service.

Last week Planning Commission Co-Chairman Dr. Montek Singh Ahluwalia met in Washington with U.S. Energy Secretary Bodman on laying the foundation for the High Level Energy Dialogue. Dr. Ahluwalia also met with Dr. Allan Hubbard, the top economic official in the White House, on advancing the Economic Dialogue. They plan another such meeting shortly.

On April 21, Lt. Gen. Jeffrey B. Kohler, Director of the Defense Security Cooperation Agency, visited Delhi to begin discussions about the capabilities of Lockheed Martin's F-16 fighter and Boeing's F-18. Both aircraft are under consideration in India's important Multi-Role Combat Aircraft tender.

On Monday of this week in New Delhi we hosted a 65-member trade and education delegation from the state of Virginia, led by Virginia Governor Mark Warner.

On the calendar ahead, we look forward to a visit to the U.S. this June by Minister Nath, to advance our Trade Policy Forum and meet with Commerce Secretary Gutierrez and U.S. Trade Representative Portman, assuming he is confirmed. President Bush has invited Prime Minister Singh to visit the U.S. We expect that visit will take place in July. We hope the first meeting of the Economic Dialogue's CEO Forum will take place before that event. In late summer, we expect Treasury Secretary John Snow to visit India for a Cabinet-level session of the Economic Dialogue. Finally, late this year or early next year, President Bush will visit India.

That is quite an agenda. It marks an intense level of high-level contacts.

The objective of all these contacts is to deepen American strategic and economic ties with India -- to put them on a sustainable commercial basis so that the private sectors in both countries can unlock the full potential of their productive energies.

We also want to join with India to open up new fields -- areas in which historically there has been little or no commercial or technical exchange -- such as space research, civil nuclear energy, and the joint production of weapons systems. This is new ground for all of us -- policy makers, government officials, businesses, and trade associations like the American Chamber of Commerce.

Even as we look ahead to new opportunities, we will also use our high-level dialogues to address the trade and investment issues of the past. These are the so-called "legacy issues." They include disputes involving specific companies, such as the U.S. investors in the power sector. They also include more general "policy" issues, such as government subsidies for fertilizer and LPG and non-tariff barriers and non-transparent standards.

These practices restrict trade and investment opportunities for U.S. companies. The Government of Prime Minister Singh is committed to market-oriented reforms. Last week the Prime Minister said in Jakarta "We are committed to be more open -- a more open economy (and a) more open society

… (the) winds of change are creating a situation for growth of India. We want to see the growth rate go up to 7.5 per cent in the future." That sounds like a clear call for additional economic reforms.

We encourage the UPA Government to move forward with the next generation of economic reforms. Further reform would benefit Indian consumers by increasing their choice of goods and services. And they would establish the policy framework needed to pursue new opportunities with the U.S. in a variety of high-tech fields and "sunrise" industries.

Let me give a few examples of areas needing further reform:
First, tariffs. I am glad the Minister is here and I know he won't mind if I speak frankly as good friends do. India has made important progress in lowering the peak rate. This year it is 15 percent, compared to 40 percent in 1999. But tariffs still have room to come down, especially to achieve the Government's goal of aligning them with the tariff structure in the ASEAN countries. Even as tariff rates have fallen, other forms of protection appear to have gone up.

The Government imposes sanitary and phyto-sanitary rules, technical standards, and registration rules, sometimes in non-transparent ways. For example, the Government recently imposed sanitary measures that have stopped imports of pet food, poultry, and dairy products from the United States.

Moreover, tariffs on agricultural imports remain very high by world standards. The average tariff on most foodstuffs is about 40 percent. According to the IMF, only four countries on a list of 134 emerging markets have higher agricultural tariffs. Thus, despite the reduction in tariff rates, India still has a restrictive trade regime. Because trade is restricted, Indian consumers have fewer choices and pay higher prices.

The situation with Foreign Direct Investment (FDI) is a similar story: although progress has been made, India still imposes restrictions on many types of FDI. To the outside observer, it appears as though the investment door is half open and half closed. The recently released "roadmap" for FDI in the banking industry is an example. It features a five-year delay before the door is open to FDI. And there is no full guarantee that will happen. The five years is intended to give domestic banks time to become more efficient so that they can meet the challenges of global banking. It is unclear under what circumstances any domestic bank would be allowed to merge with a foreign partner.

Indian banks are small and undercapitalized. They need foreign capital to grow. The delay in preventing foreign capital from entering India will be costly in terms of slower growth, fewer jobs, and less innovation in banking services. It will hinder India's emergence as a global economic power.

India's banking industry -- indeed, its entire financial sector -- has matured to the point where it can accommodate a faster pace of reform. This would facilitate the delivery of credit and other types of financial services to small-scale enterprises and to households with modest incomes.

These are large segments of the economy. They are untapped markets. When they need credit, they typically rely on family and the informal financial sector for loans. Only the private sector can pull these segments of society into the formal banking system. Liberalized foreign investment in banking would accelerate that process. Liberalizing FDI in banking would have another positive effect: it would help India finance its infrastructure needs.

India cannot be a world economic power without world-class infrastructure. It's as simple as that. There are many factors that have led to the inadequacy of infrastructure in India. One of them is the lack of a long-term debt market. In the United States, we have credit markets where borrowers can find financing for 30 years or longer for development projects. India does not yet have such a market.

To stimulate the creation of that market, the Government should allow the private sector to increase the number and the different types of financial players. The creation of a long-term bond market depends on banks, insurance companies, pension funds, mutual funds, Foreign Institutional Investors, venture capital funds, even retail investors. They all have different incentives and different time horizons for their investments.

Policies that restrict the numbers and the types of financial players tend to result in shallow credit markets that are unable to provide long-term financing. Liberalizing FDI in banking – as well as in insurance and pension fund management – will bring in more capital, stimulate the creation of the long-term credit market, and provide financing for long-term infrastructure needs.

The retail industry is another example of an area needing reform. When I arrived in India in 2003, there was virtually no public discussion about opening up the retail sector to foreign investment. Although retailing is still off limits for FDI, today there is a public discussion about liberalizing that policy. India should allow foreign investors to participate directly in retailing -- as well as in related industries like accountancy, real estate, and law practice. It would be a driver of economic growth. It would offer Indian consumers a wider variety of goods and services at lower prices. And it would have a truly transforming effect on the economy, unifying existing market fragments into a national whole.

Because of a variety of tax policies and government restrictions, India's market is fragmented. Allowing foreign retailers to enter would introduce "supply chain" business models. This would create a truly national market in terms of both the price and the quality of goods. Today, international retail giants like Wal-Mart buy billions of dollars worth of goods in India and sell them to foreign consumers abroad through their own outlets. However, the Government prohibits these same companies from selling the same goods to consumers in India! That does not make sense.

Years ago the retail industry was closed in such markets as Mexico and China. But after U.S. retailers entered, they passed along cost savings to the consumer of up to 30 percent on many goods. For those with modest incomes, lower retail prices effectively means an increase in their disposable income.
Opponents sometimes argue that opening retail would hurt local producers. But an editorial in the *Indian Express* on Monday pointed out that the presence of big local retail malls has not hurt local kirana stores. The same editorial noted that FDI in retail would be a boon to the exchequer because foreign retailers would pay the taxes that are currently evaded by thousands of informal retailers in the cash economy.

In sum, the U.S. is launching a comprehensive relationship with India on economic, commercial, and strategic issues. This year will likely be remembered as a watershed year in U.S.-India relations.
All of you will have a crucial role to play. We count on your guidance and counsel as we move forward.
Thank you.

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