Coalition govt may find it difficult to pass major reforms: Rating agencies

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Passing major and contentious reforms like land and labour could prove more difficult for the next Bharatiya Janata Party (BJP)-led coalition government, rating agencies, such as Fitch and Moody's, said on Wednesday. They, however, said broad policy continuity may persist.

Jeremy Zook, director and primary sovereign analyst for India at Fitch Ratings, said a weakened majority could pose challenges for the more ambitious elements of the government's reform agenda, even as the strong medium-term growth outlook remains intact, underpinned by the government capex drive and improved corporate and bank balance sheets.

"As the BJP fell short of an outright majority and will need to rely more heavily on its coalition partners, passing contentious reforms could prove more difficult, particularly around land and labour, which have recently been flagged as priorities by the BJP to boost India's manufacturing competitiveness," Zook said.

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The upsides to medium-term growth prospects are likely to be more modest if reforms prove more challenging to advance, he said.

Christian de Guzman, senior vice-president, Moody's Ratings, echoed the view. Policy continuity is expected, especially with regards to budgetary emphasis on infrastructure spending and boosting domestic manufacturing, to support robust economic growth, Guzman said.

"However, the National Democratic Alliance (NDA's) relatively slim margin of victory, as well as the BJP's loss of its outright majority in Parliament, may delay more far-reaching economic and fiscal reforms that could impede progress on fiscal consolidation," said Guzman in a note.

India's fiscal outcomes will remain weaker than BAA-rated peers, even as the final Budget for 2024-25 to be released in the next few weeks will provide some indications of the fiscal policy over the course of the term of the incoming government through 2029, Guzman said.

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Moody's Ratings said near-term economic momentum masks structural weaknesses that pose risks to long-term potential growth with high levels of youth unemployment across sectors and weakness in productivity growth in the sovereign's large agriculture sector continuing to constrain its growth potential.

Pranjul Bhandari, chief India economist at HSBC, expects 'easy' reforms like capex thrust on infrastructure, improving food supply management, maintaining inflation at 4 per cent, and providing easy credit to small firms to continue, which generates the base case of 6.5 per cent growth potential. "Interestingly, most of these reforms were via executive action, so a slower legislative process may not impact them immediately," she adds.

However, reforms that require legislative action like improving the goods and services tax structure, land, labour, farm, judiciary, and bureaucratic reforms may prove hard to undertake.

Samiran Chakraborty, chief economist at CitiGroup, said there was brisk fiscal space available to the government, which can be used for some new spending focused on the poor, women, and rural areas, but capex focus is likely to remain.

"The broad agenda of infrastructure, manufacturing, and technology to take India's economy forward, most likely would not take a back seat. However, the contentious structural reforms might be delayed till some of the political headwinds for NDA recede," said Chakraborty. "Welfare spending could rise, but that can coexist with gradual fiscal consolidation as tax growth is strong. Moreover, the economy appears in good shape in terms of growth and stability," he said.