By Ruchir Sharma

In the end, there’s a limit to the wall of wishes that the market can climb. For too long, the country’s share markets marched on, seemingly oblivious to the growing list of negative factors ranging from flagging reform momentum and high valuations to a deteriorating political backdrop. But the events of the past few weeks, culminating in the presentation of a rather insipid annual budget by India’s finance minister yesterday, seems to have finally broken the market’s momentum. This may take some gloss off the “India Rising” story.

In the fourth year of the strongest economic expansion in history, it is being very difficult to grapple with the problems of increasing inflation and, more worryingly, a political class that doesn’t believe in the economics that makes for good politics. That’s ironic, given that Finance Minister P. Chidambaram has been at the wheel. He’s counted as one of the few Indian politicians with a vision for reform, and it has developed over the years, been instrumental in implementing several path-breaking reforms, such as introducing corporate and personal taxes. But in a sign of changing times, he presented a budget yesterday that was long on rhetoric and short on any new reform initiatives.

It is fortunate that Mr. Chidambaram delivered the budget speech at day after a clutch of state elections results were announced, in which the Congress-led coalition suffered major reversals. Had there been time, odds are that the finance minister would have had a few more policy statements to take into account the rapidly rising political perception that high economic growth could be enabling the government to lose elections in spite of strong economic growth because of the abnormal conditions of issues that the government should be mainly accountable for, from law and order to basic infrastructure. The government’s delivery mechanisms are broken and until they are fixed, no amount of spending will be of any social consequence.

The disconnect between the Bank’s low inflation assessments and the rise of inflationary expectations has been only the first year of India’s strong economic expansion. As the new government viewed its victory as a vote against economic reforms. As a result, it has done very little on that front, focusing instead on policies apparently meant to help the “common man.”

Luckily, taking that tack didn’t seem to derail the Indian economy—one on the contrary, India kept moving along a higher growth trajectory, powered by the violation of its mandate. The job of the erstwhile masters, including that of the finance minister, was thus redefined to keeping bad ideas out and allowing the economy to benefit from globalization. In his address to the budget speech, Mr. Chidambaram performed this role admirably. He often re-packaged old spending plans, giving the impression that the government was indulging in a more “inclusive” growth model, but in reality, the increase in government spending well in check, as the nearly chart shows. It is indeed possible that despite falling real pressures, India’s government spending as a share of the gross domestic product has gone up by 1% from its levels of the last few years. This has allowed the country’s fiscal deficit to fall to 3.7% of GDP.

Given the outcome of Monday’s state elections in Punjab, Uttarakhand and Manipur, the government is increasing seems that the appeal of populist policies may be too hard to counter. Political analysts, for instance, said inflation as one of the key reasons for the Congress Party’s electoral defeat. While a resolve to fight inflation is about as noble an objective as much of the political class has arrived at the conclusion that inflation is a consequence of high economic growth, which in their view only benefits the privileged classes—and is therefore “unfair.” At nearly 7%, it’s true that India’s inflation rate is on the higher side of an average 5.5% of developing economies consuming food prices, which form a large part of the average household consumption basket, not inflationary pressures. But the solution to inflation in India is in what seems to be the government’s inability to come to terms with the problem—increasing government spending and banning forward trading in key commodities. The answer, instead, is to reduce import duties that let the Reserve Bank of India carry on with its job of normalizing interest rates. There needs to be any certainty that the public between growth and inflation are steps to end productivity are taken by making the economy open and competitive.

If the budget wasn’t all bad news. In an effort to address supply-side shortages, Mr. Chidambaram did announce a cut in the peak import tariff to 10% from 15% on the average. However, given the revenue windfall from a fast expanding economy, there was scope for further cuts, especially on high customs duties that among other advantages. India’s fiscal deficit to fall to 3.7% of GDP. The answer, instead, is to reduce import duties that let the Reserve Bank of India carry on with its job of normalizing interest rates. There needs to be any certainty that the public between growth and inflation are steps to end productivity are taken by making the economy open and competitive.

To keep the growth momentum going, India will need a new set of economic reforms, ranging from policy. Much of its greater globalization to further liberalization of foreign direct investment caps in important sectors such as insurance and retail. The current political context doesn’t make such moves likely to happen anytime soon. Realistically, the best one can hope for is that the Indian economy continues to profit from global trends—and that the current political quarters is kept to a minimum. But the India story then becomes a tale less exciting than it was even a few weeks ago.

Mr. Sharma is head of emerging markets at Morgan Stanley Investment Management.

By Anil K. Kashyap

The Bank of Japan is yet again sailing without a rudder. Consider the farce that’s been playing out before the February meeting, and what might be viewed as “approving of the deflation doctrine.”

The heart of the problem is the BoJ’s strange definition of price stability. While the BoJ, in a meeting that “as world financial markets

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