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Indian economy on right track

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The Indian government released the second-quarter GDP (gross domestic product) numbers on December 31, virtually unnoticed in the aftermath of the devastation caused by the tsunami. Economic growth, according to the figures released by the government, slowed to 6.6% during the second quarter ended September from 7.4% in the previous quarter due to a negative growth in the agriculture sector, once again reflecting the Indian economy's dependence on the vagaries of monsoon. The agricultural slowdown was so pronounced that even the robust performance of the manufacturing sector - 9.3% against 8% in the previous quarter - failed to contain the fall in overall GDP growth.

Consolidated growth in the first six months this fiscal (April-September) stood at 7%, against 6.9% in the same period last year, recording a minor improvement. The agriculture sector registered a negative growth of 0.8% compared with 3.4% in the first quarter this fiscal. Apart from agriculture, other sectors contributing to the economic slowdown were mining, financial, real estate and insurance services. The construction sector, however, grew by a healthy 5.2%, against 3.6% in the previous quarter. GDP at factor cost on constant prices (1993-94) stood at Rs3.47308 trillion (US$79 billion). For the six months ended September, GDP grew to Rs6.99427 trillion from Rs6.53699 trillion in the same period last year.

One remarkable part of last quarter's development is the clear pickup in overall industrial activity, probably indicating a turnaround in its fortune. With manufacturing showing a growth of 9.3% during the quarter, the overall growth of the industrial sector has been as much as 8.02%, slightly lower than the growth in service sector - 8.25%. After a long time, industrial activity has shouldered the burden of GDP growth in India. It's the service sector that generally does so. However, only the coming quarters will tell whether this becomes a trend.

QUARTERLY GDP

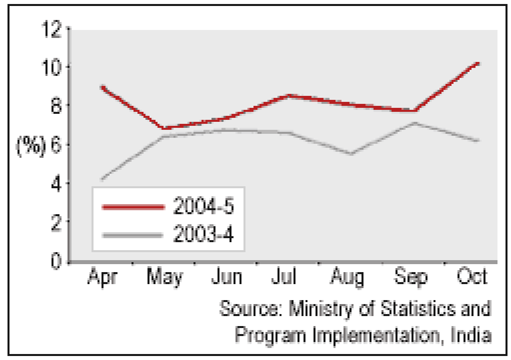
	GDP (Rs. billion) - constant prices					
	2002-03		2003-04		2004-05	
	Q1	Q2	Q1	Q2	Q1	Q2
Agri	721.26	542.05	721.94	579.18	746.15	574.60
Ind	776.23	793.68	823.39	846.77	880.26	914.68
Serv	1615.87	1665.08	1733.09	1832.61	1894.79	1983.79
GDP	3,113.36	3,000.81	3,278.42	3,258.56	3,521.20	3,473.07

Source: Ministry of Statistics and Programme Implementation, India

%age chg over previous yr			
2003-04		2004-05	
Q1	Q2	Q1	Q2
0.09	6.85	3.35	-0.79
6.08	6.69	6.91	8.02
7.25	10.06	9.33	8.25
5.30	8.59	7.41	6.58

The trend, however, continues to be positive. Even during October, the Index of Industrial Production showed a growth of 10.1%, buoyed by the 11.3% growth recorded by the manufacturing sector (chart below).

Even if one goes by the performance of the capital-goods sector, there is clear indication that India is possibly experiencing resurgence in industrial activity. Every month in the April-October period saw the capital-goods sector recording a double-digit growth against only twice during the same period in the previous year. The corporate sector is clearly in a bullish mood.



India's balance of payments (BoP) slipped into a deficit - the first time since September '02. According to the Reserve Bank of India (RBI), the deficit stood at $634 million as of September '04 against a BoP surplus of $7.5 billion at the end of June '04 and a surplus of $13.5 billion in September '03. The BoP is a combination of current account - which captures India's imports, exports and services transactions with the rest of the world - and the capital account - which comprises various debt, aid and equity flows, a part of which could be hot money.

After posting a surplus for four consecutive quarters, the current account ended in a deficit on September 30, thanks to lower remittances and higher imports. The current account showed a deficit of $6.4 billion compared with a surplus of almost $2.1 billion a year ago. However, the capital account showed a surplus of $5.8 billion - the same as it was in the year-ago period.

In the second quarter, merchandise imports surged by 53.5%, more than doubling the 24.6% growth in the previous quarter. Crude oil and petroleum products were the key drivers of the surge in import payments. Volume of oil imports was up by 12.7% in the second quarter, with prices ranging $32-$41 per barrel as against $29-$35 in the first quarter. The trade deficit stood at $12.3 billion during the second quarter as against $5.1 billion in first quarter. For the first half of 2004-05, the trade deficit was at $17.4 billion, higher by 86% on a year-on-year basis and already running above the level of the full year 2003-04. During this period, non-oil imports also showed a steady growth, indicating a pickup in economic activity.

External sector ($million)

	2004-05		H1	
	Q1	Q2	2004-05	2003-04
Exports	18,189	16,262	34,451	27,960
Imports	23,329	28,563	51,892	37,319
Trade Balance	-5,140	-12,301	-17,441	-9,359
Invisibles, net	8,299	5,882	14,182	11,550
Current account balance	3,159	-6,419	-3,259	2,191

Source: RBI

Foreign direct investments (FDI) into India rose by 26.83% to $2.04 billion in the first half of the current fiscal ending September 2004, as against $1.61 billion in April-September 2003. FDI rose by $1.27 billion in July-September 2004 (Q2) as against the April-June quarter (Q1). While the numbers are not earth-shattering, there is clear indication that India is becoming a more attractive FDI destination. In the FDI Confidence Survey, 2004, A T Kearney rated India as the third-most-attractive investment destination (behind China and the United States), compared with its 15th position two years ago and sixth last year. It also ranked India as the best BPO (business process outsourcing) destination. Even according to the United Nations Conference on Trade and Development (UNCTAD) and Corporate Location, India is among the top three investment "hot spots" for the next four years. The latest World Economic Forum's "Global Competitiveness Report" ranks India 41st out of 102 countries in terms of restrictions on foreign ownership. In comparison, Malaysia is ranked 65th, Thailand 72nd and China 81st. None of the major developing economies is ranked higher than India.

There is now more evidence to suggest that the Indian economy may be entering a phase of sustained investment-led growth. Major capacity expansions are being planned in the manufacturing sector. The last time such big investments took place in the industry was during 1993-96. There are clear signs that most industry segments are operating at full capacity. Further capacity building exercise has begun in sectors such as steel, cement, aluminum, paper, textiles and automobiles.

An overall growth of 8%-plus in the service sector seems achievable going by the quarterly trend. Similarly, the manufacturing sector could just about touch 8% if the current momentum is maintained for the rest of the financial year. Thus the service and manufacturing sectors alone could propel the GDP growth to more than 6%.

For the first time in many years, private power projects are being funded by banks and financial institutions. This is happening possibly because the new electricity laws allow private producers to sell power to anyone they please. Steel manufacturers are planning capacity expansions to the tune of Rs100 billion over the next three to four years. Auto majors are planning new units, either for the domestic market or for exports. Suzuki Motors expects the Indian car market to grow from 1 million a year to 2 million by 2008. So Maruti Udyog Ltd, which has a 55%-plus share in the passenger-car market, has decided to double its own capacity to 1 million over the next four to five years. This will entail an additional investment of Rs60 billion. Clearly, the Indian economy is on the right track.

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