India

Economics

Economic

Credit Agencies:

Moody's: Baa3

S&P: BBB-

Fitch: BBB-

Nominal GDP (2008):

USD 1,164 billions

Population (2008):

1,148 millions

Total Trade / GDP (2008):

41.4%

Currency:

Indian rupee

Exchange regime:

Managed float

Merchandise imports from Canada (Jan-Sep 2009)

CAD 1,386 mn (-6.0%)

Main sources of Foreign Exchange (excl. FDI):

Manufactured goods

Remittances

Main Merchandise Export Destination:

US (17 %)

Main imports:

Manufactured goods (30%)

Mineral fuels (8.7%)

Risks to the Outlook

Higher government pre-election spending

Weaker External demand
Trade deficit surge
Higher fiscal deficit

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Market Spotlight: Economic performance remained fairly resilient despite the global downturn aided by robust private consumption and a substantial fiscal stimulus. GDP is forecast to clock in at 6.4% for the Calendar (CY) and 6.5% for the Fiscal Year (FY) in 2009. Short term, poor monsoon rainfall will exacerbate the downside, and going forward, a precarious fiscal situation, if left to worsen further, will ultimately weigh on long term growth potential...

Recent performance: Growth in the third quarter accelerated to 7.9% y/y from 6.2% in the second and 5.8% in first. Growth had slowed to 7.4% for 2008 and is expected to remain below trend over the next few quarters. Continued high government stimulus spending and resilient and improving private demand were the main drivers. Industrial production expanded 9.2% y/y in September, following an 11% y/y increase in August, but the latter's expansion benefited from base effects due to the slow growth a year earlier. The lower monsoon rains this year have so far not had the anticipated negative effects on growth.

Fiscal policy: The budget for the FY09/10 fiscal year projected a worsening of the deficit to 6.8% of GDP from 6.0% the previous year and a decline in tax revenues to 10.9% of GDP from 11.6%. Total expenditure of the central government is to increase to 17.4% of GDP on the back of higher food subsidies and outlays on welfare and job creation programs particularly in rural areas to boost demand and maintain the growth trajectory. The time given to small farmers to pay their overdues under the debt waiver and the debt forgiveness scheme has been extended to end of year. More money will be pumped into the National Rural Employment Guarantee scheme which ensures each rural family 100 days of work on public sector projects. Much-needed infrastructure spending will increase. Fiscal consolidation is to be sacrificed for short term growth and is to return in the medium long term. The budget does not contain major reforms to benefit private business and foreign investors. The higher deficit will exacerbate the debt to GDP ratio which is projected to reach over 80% by the end of the fiscal year.

Monetary policy: The aggressive monetary easing cycle has come to an end, the repo rate and the reverse repo rate will remain at 4.75% and 3.25% respectively until year end. Some gradual withdrawal of accommodative measures has begun as signs of an economic recovery are proving more robust and are putting upward pressure on prices. October Whole Sale Price Index (WPI) rose 1.3% y/y from 0.5% y/y in September, while the Consumer Price Index (CPI) surged 11.5% y/y due to the heavier weighting of food prices (affected by low agricultural output due to weak rains) in the consumer price basket compared to the whole sale price basket. Lower policy rates are slowly translating into lower commercial bank lending rates, but businesses remain cautious about borrowing and investing and domestic credit sluggish.

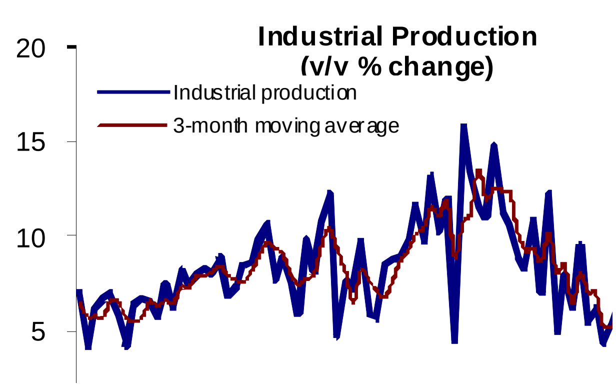
The external sector: Record trade deficits in 2008 were due to surging oil prices. The subsequent plunge in commodity prices failed to materialize into substantial current account gains in late 2008 due to dismal export performance. The significant drop in imports in 2009 has lead to an improvement in the current account deficit in the first quarter of this year after a marked deterioration in the last three quarters of 2008. The overall balance of payment (BOP) figures for the first half of 2008 showed a surplus, but by the second half of the year this no longer held true. The BOP is now once again in positive territory due to a firming on the capital account side but the current account side has weakened substantially. Foreign reserves, while sizeable, had been pressured in recent months, but picked up again in September reaching over USD 264 billion and representing over 9.4 months of current account debit cover. The external debt is small at 18.7% of GDP supporting solvency. The rupee depreciated in 2008, losing 20.7% against the USD, but in 2009 it has regained its lost strength.

Outlook: Growth will slide to 6.4% in CY-2009 6.5% in CY-2010 (6.5% in FY-2009 and 7.0% in FY-2010), while the medium term outlook remains favourable. While elections have ended, the push for substantial reforms is expected to be limited despite reformist appetite. The move towards gradual liberalization and deregulation will continue under the new government; but a major overhaul is unlikely. The dire state of the country's infrastructure will need to be addressed, since it is not at par with the economy's stance as Asia's second powerhouse. The effect of pre-election spending and the stimulus package as growth boosters will begin to fade with added pressure due to agricultural sector woes. We expect medium term growth to return to its current growth potential of over 7% but not before 2011.

Economic Indicators

	03-07 avg.	2008	2009	2010
GDP (% growth, real)	8.9	7.4	6.4	6.5
Inflation (%, year-end)	4.9	8.2	5.4	4.4
Fiscal Balance (% of GDP)	-3.8	-6.0	7.0	-4.8
Exports (% growth)	24.3	20.1	-8.0	10.6
Imports (% growth)	30.7	33.1	-8.5	12.1
Current Account (% of GDP)	-0.3	-3.6	-4.0	-3.9
Reserves (month of imports)	9.9	7.6	7.7	6.5
External Debt (% of GDP)	16.0	14.0	14.6	13.8
Debt Service ratio	10.5	6.2	7.1	6.5
Currency (per USD, year-end)	43.6	48.8	47.0	45.8

Source: EIU, EDC Economics



Source : Bloomberg

India

Economics

General Political Environment: The Indian National Congress (Congress) and its allies in the United Progressive Alliance (UPA) have ruled since 2004 and recently was re-elected to a second five-year term in May 2009. The UPA coalition's victory wasn't overly surprising; however, the margin of its victory was astonishing. The UPA secured 261 of the 543 seats available in the lower house of parliament. The opposition coalition led by the Bharatiya Janata Party (BJP) finished a distant second with 158 seats.

The biggest surprise of the election was not the success of Congress, but more the stumbling of several of the more prominent regional parties that contested the polls. In the lead-up to the elections, there were plenty of predictions that the virtually uncontested reign of the national parties (i.e. Congress and BJP) had come to an end and that the country's political future lay with the plethora of regional parties, if not as kings then at least as king-makers. While certain of these did succeed in increasing their parliamentary seat-count, the majority of seats that changed hands went to Congress, a party which has experienced increased success in each of the last three parliamentary elections.

The rise in prominence of regional parties (i.e. parties with a political presence in fewer than four states) in Indian national politics has been one of the most significant political developments to occur in contemporary India, with over 30 political parties represented in Parliament. While this phenomenon will continue in India, thereby requiring coalitions of parties to form governments, the 2009 election results reflect the continued prominence of national parties, namely Congress, on the political scene.

Investment Environment: Despite India's foreign investment policy allowing 100% FDI in most sectors, India has thus far failed to reach its full potential as a destination for FDI. The government's attempts at increasing FDI inflows have been hampered by the several impediments including pervasive corruption, an unwieldy bureaucracy, and a significant deficit in critical infrastructure. India is known for diverse operating environments with regulations varying from state to state.

Significant reform in investment-related matters, particularly regarding foreign investment, was delayed over the past few years largely due to the UPA's reliance on India's communist parties for support in parliament. The ending of this support in 2008 enabled limited reforms to be passed. For example, in February, the government initiated changes that further opened-up certain sectors such as insurance, telecom and retail, to FDI. The government's move didn't alter the FDI caps in place in these sectors but instead permitted foreign equity investments beyond the limit to occur indirectly.

One expectation is that the re-elected UPA government, that no longer relies on India's main leftist parties for support, will now be in a position to push through further economic and investment reforms, many of which will provide opportunities for foreign investors. Reforms are moving forward at a gradual pace as a result of the global recession and the diversity of views on the issues, even within the Congress party itself. Plans to overhaul the tax system, create an independent debt-management office and partly-privatize state owned firms are being proposed and discussed.

Political Violence: Several terrorist attacks in 2007-2008, including bombings in Delhi, Ahmedabad, Bangalore, Jaipur and Hyderabad have highlighted the threat posed by Islamist terror groups within India. In November 2008 a dozen gunmen struck several targets in Mumbai, killing over 180 people. Although the majority of the known victims were Indian nationals, the attackers singled out foreigners during the hotel sieges, particularly UK and US nationals.

Tensions with Pakistan have threatened regional stability since 1947. Several years of peace talks on the Kashmir issue have resulted in little progress and the area witnessed considerable unrest in mid-2008 as anti-government demonstrations were met with force by security forces. The Mumbai attacks led to a deterioration in Indo-Pakistani relations as many of the attackers were Pakistani with the Indian government claiming that Pakistani government agencies may have also been involved.

Other political violence issues include sporadic Hindu/Muslim communal violence and ongoing separatist insurgencies in the northeastern states, particularly Assam. The ongoing Maoist (Naxalite) insurgency in central and eastern India proliferated in 2009 and in October New Delhi announced its largest campaign against Naxals, deploying more than 100,000 federal forces to fight the insurgency.

Political

Political Structure
Federal State
Parliamentary Democracy

President
Pratibha Patil

Prime Minister
Manmohan Singh, Indian National Congress (INC)

National Legislative Bodies
- Lok Sabha (Lower House) 545 members (chosen through direct election)
- Rajya Sabha (represents interests of Indian states) 245 members (233 elected, 12 appointed by President)

Major Parties
- Indian National Congress (INC)
- Bharatiya Janata Party (BJP)
- Samajwasi Party
- Bahujan Samaj Party
- Communist Party of India-Marxist (CPI-M)

Last Elections
April/May 2009

Next Elections
April/May 2012

Press Freedom Survey:
- 2008 Score: 35 - partly free

(0: Free; 100: Not Free)
freedomhouse.org

Control of Corruption Index:
- 2008 Score: -0.37

(-2.5: Worst; +2.5: Best)
worldbank.org

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Political Outlook

Elections held in April/May 2009 provided the Congress-led UPA coalition with a strengthened mandate, which should ensure its uninterrupted rule over the next five years. Economic and investment reforms will move forward gradually as a result of the global recession and a wide range of views on the issues. Although political violence is a fairly common occurrence in India, the Mumbai attacks of November 2008 were shocking due to the level of sophistication and the selection of targets, including the focus on foreigners. The Mumbai attacks underscore the ongoing risk of terrorist attacks throughout the country, and also set Indo-Pakistani relations back several years. Although outright war is unlikely, bilateral relations will be tense for the foreseeable future.