Euler Hermes Economic Research

Country Report

India

Gathering pace

General Information

GDP	USD1876.8 bn (World ranking 10, World Bank 2013)
Population	1252.1 mn (World ranking 2, World Bank 2013)
Form of state	Federal Republic
Head of government	Narendra Modi (Prime Minister)
Next elections	2017, Presidential

Strengths

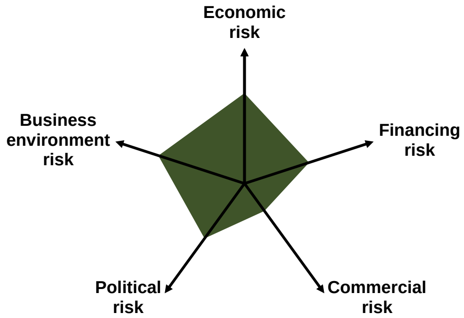
- Stable democracy, with peaceful changes in government.
- Large internal market, providing some insulation from the global business cycle.
- Successful diversification into manufacturing (motor vehicles) and services (including call centres, IT and biotechnology).
- High annual GDP growth
- External debt is low relative to earnings and repayment capacity.
- Strong FX reserves.

Weaknesses

- Vulnerable to natural disasters (including tsunami, droughts, floods and earthquakes).
- The Kashmir region remains volatile and a source of potential conflict.
- The political system tends to engender coalition governments that lack the ability to push through economic reforms.
- Poverty remains pervasive and income distribution uneven.
- Structural weaknesses include inadequate infrastructure for a country of its status, current and fiscal account deficits and state involvement crowds out private sector initiatives in some sectors.
- Weak structural business environment.

Country Rating

B1



Source: Euler Hermes

Trade structure

By destination / origin

Exports		Rank		Imports
United States	13%	1	11%	China
United Arab Emirates	10%	2	8%	Saudi Arabia
China	5%	3	7%	United Arab Emirates
Singapore	4%	4	5%	Switzerland
Hong Kong	4%	5	5%	United States

By product

Exports		Rank		Imports
Mineral Fuels	21%	1	40%	Mineral Fuels
Pearls, Precious stones	13%	2	14%	Pearls, Precious stones
Vehicles	4%	3	7%	Machinery
Organic Chemicals	4%	4	6%	Electrical Equipment
Machinery	4%	5	4%	Organic Chemicals

Source: ITC, (2014)

Economic Overview

GDP growth to outpace China in 2015-2016

India's GDP growth is set to accelerate to +7.7% in FY2015-16 (after +7.5% in FY2014-15), a pace faster than China (+7.1% in 2015). This outlook reflects first a base effect due to a change in methodology in Indian GDP calculation. This led to significant revisions and suggests that India enjoyed a sharp acceleration during the 2 previous years with growth now estimated at +6.9% in FY2013-14 and +5.1% in FY2012-13 which were previously estimated at just +4.7% from +4.5% under the old methodology. Secondly, the pace is set to accelerate in the coming years due to a more favorable policy mix with less fiscal consolidation and greater monetary accommodation. Domestic demand is set to rise on the back of (i) higher public and private investment for infrastructure, (ii) increasing domestic consumption as lower inflationary pressures boost purchasing power. This will be supported further by a gradual improvement in external trade.

Policy mix is supportive but under control

Importantly the RBI operating framework has been strengthened, with government and central bank officials agreeing the adoption of a formal inflation target and creating a legal mandate for the RBI to target inflation. For the year ending March 2017, the inflation target is 4% (+/-2pps). While inflation is in the target range, this policy directive was followed by an interest rate cut (the second since the beginning of the year) of -25bps. This will likely support credit growth which has been the main Achilles' heel for growth of late. The pace of fiscal consolidation has been reduced as the government wants to increase investment in the country's infrastructure – planned spending is over USD11 bn to upgrade the country's overloaded roads, railways, ports and power plants. Against this background, the government decided to delay by one year their official target to bring down the central government deficit to -3% of GDP by FY2017/18. As a result, the deficit target for the next fiscal year will be -3.9% of GDP (compared with -4.1% in FY2014/15). Public debt will remain under control, stabilizing at around 60%.

External risk is contained

The current account deficit narrowed over the two past years thanks to the authorities' responsiveness, conservative monetary policy and stringent regulation on commodity imports. The outlook is favorable (circa -1% of GDP in 2015 and 2016). Import pressures are also alleviated due to lower energy prices. Exports are set to progress gradually reflecting further price competitiveness (due to currency depreciation) and improving demand from key partners (US and Gulf countries). Currency risk is moderate compared to 2013 as the RBI has gained credibility and external imbalances have decreased. Some turbulence may be experienced in H2 if the FED hikes interest rates more than expected as India remains reliant on short term capital flows.

Economic forecasts

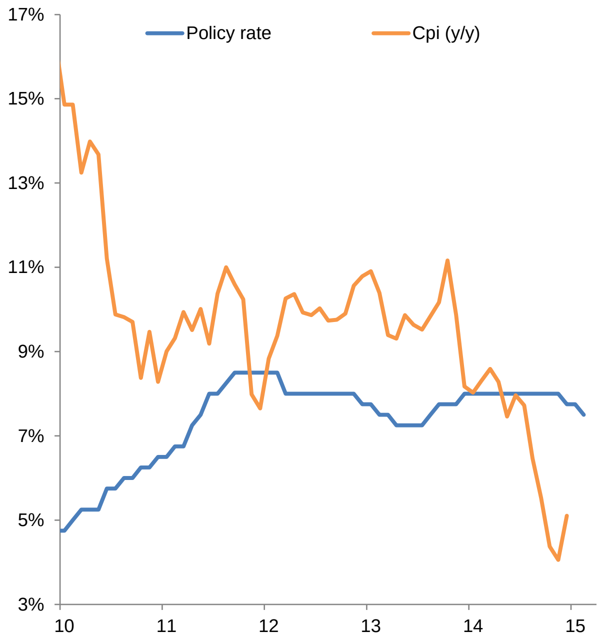
	2013*	2014e	2015
GDP growth (% change)	6.9	7.5	7.7
Inflation (%, year average)	8.4	5.2	5.0
Fiscal balance (% of GDP)**	-4.6	-4.1	-3.9
Public debt (% of GDP)	61.4	60.2	59.8
Current account (% of GDP)	-1.7	-1.1	-0.8
External debt (% of GDP)	23.2	22.7	22

*FY2013-14

** Central government balance

Sources: National sources, IIF, Euler Hermes

Monetary policy



Sources: National sources, IHS, Euler Hermes

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