

Defining the Business of Politics

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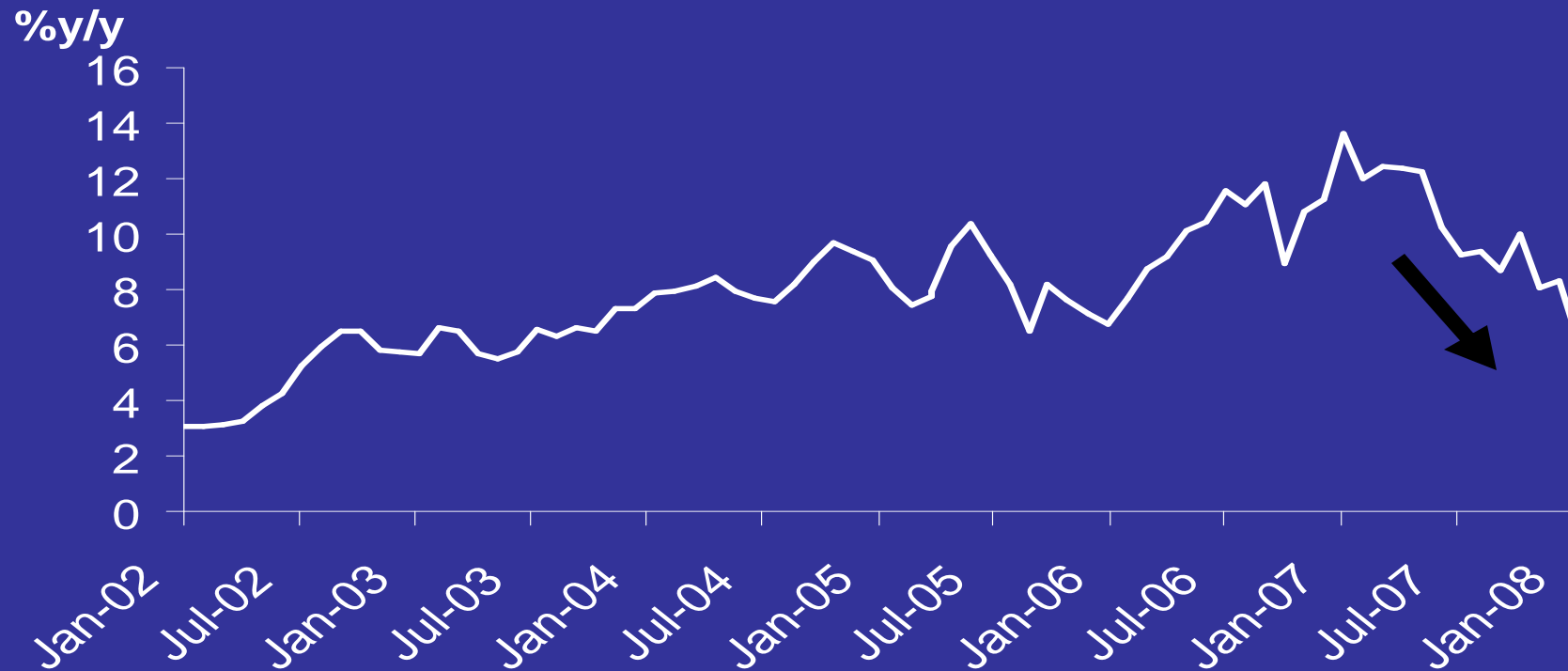


INDIA: Short- and medium-term economic outlook

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Unmistakable economic slowdown gathering pace



Industrial production

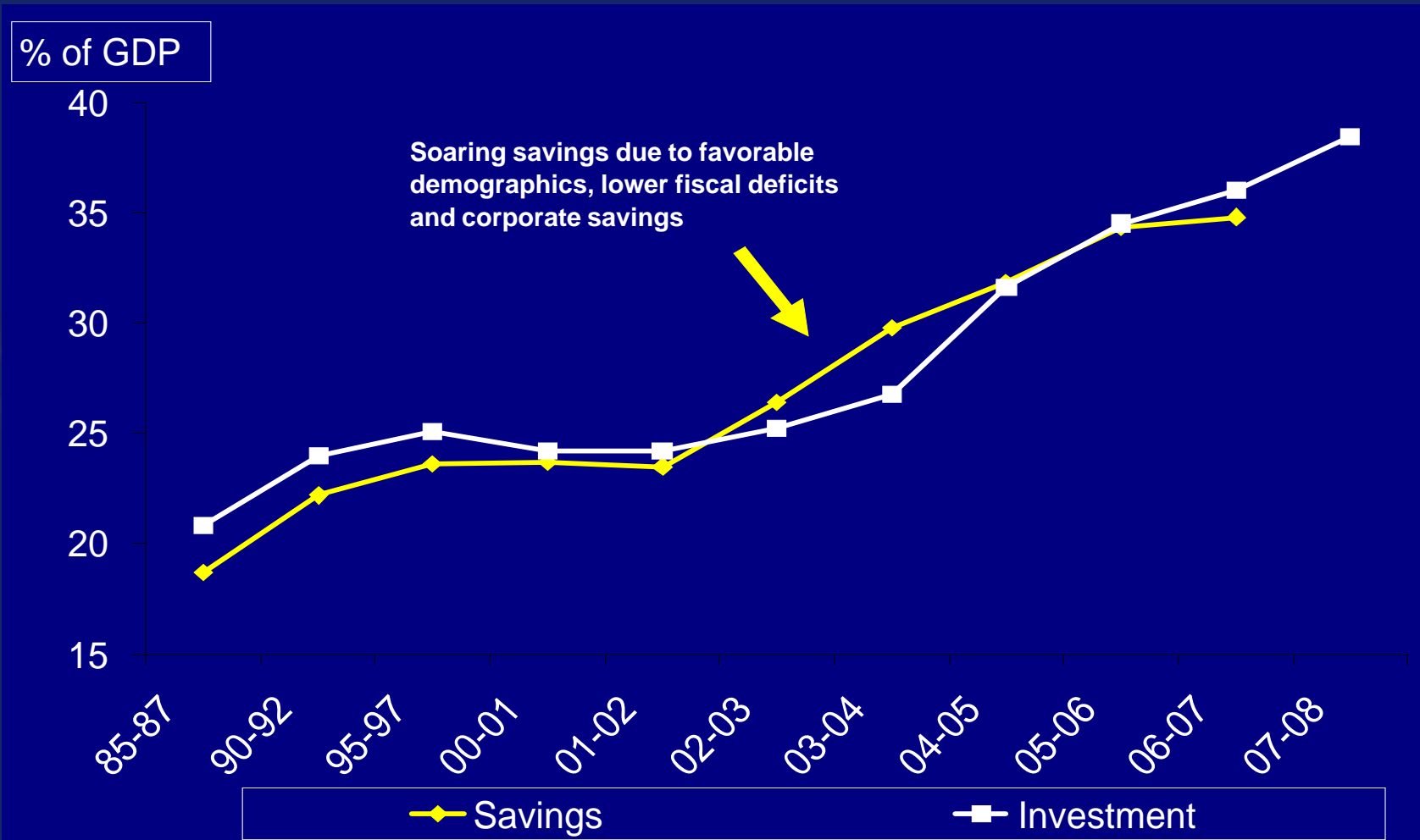
Economic outlook for 2008-2010

- Government facing growth/inflation trade-off; economy is slowing while inflation remains high (6.5%, above central bank comfort level of 5%)
- At this stage of India's political cycle (national elections due within a year) low inflation takes priority => monetary policy stays tight
- Because the current economic cycle was driven by corporate expenditure, the high interest rate regime could push the economy into outright recession
- Sub-prime woes and economic troubles in the US could hit India badly if capital inflows dry up
- Wide range of forecasts for GDP growth in both magnitude and more importantly, *direction*. Asian Development Bank (ADB) forecast: 2008: 8%, 2009: 8.5%. Private sector growth forecasts indicate an economy picking up late 2009.

Sustainable rate of real GDP growth believed to be 8.0-8.5%



Longer term: high investment rates fuelled by growing savings ratios



Huge infrastructure development aims to raise sustainable GDP growth towards 10%

- **India's 11th five year plan (2007-12):** half trillion dollar infrastructure investment program. The plan is to increase spending on ports, roads and highways, airports, power plants from 5% of GDP in 2006-07 to 9% of GDP by 2011-12, and to 10.25% by 2016-17

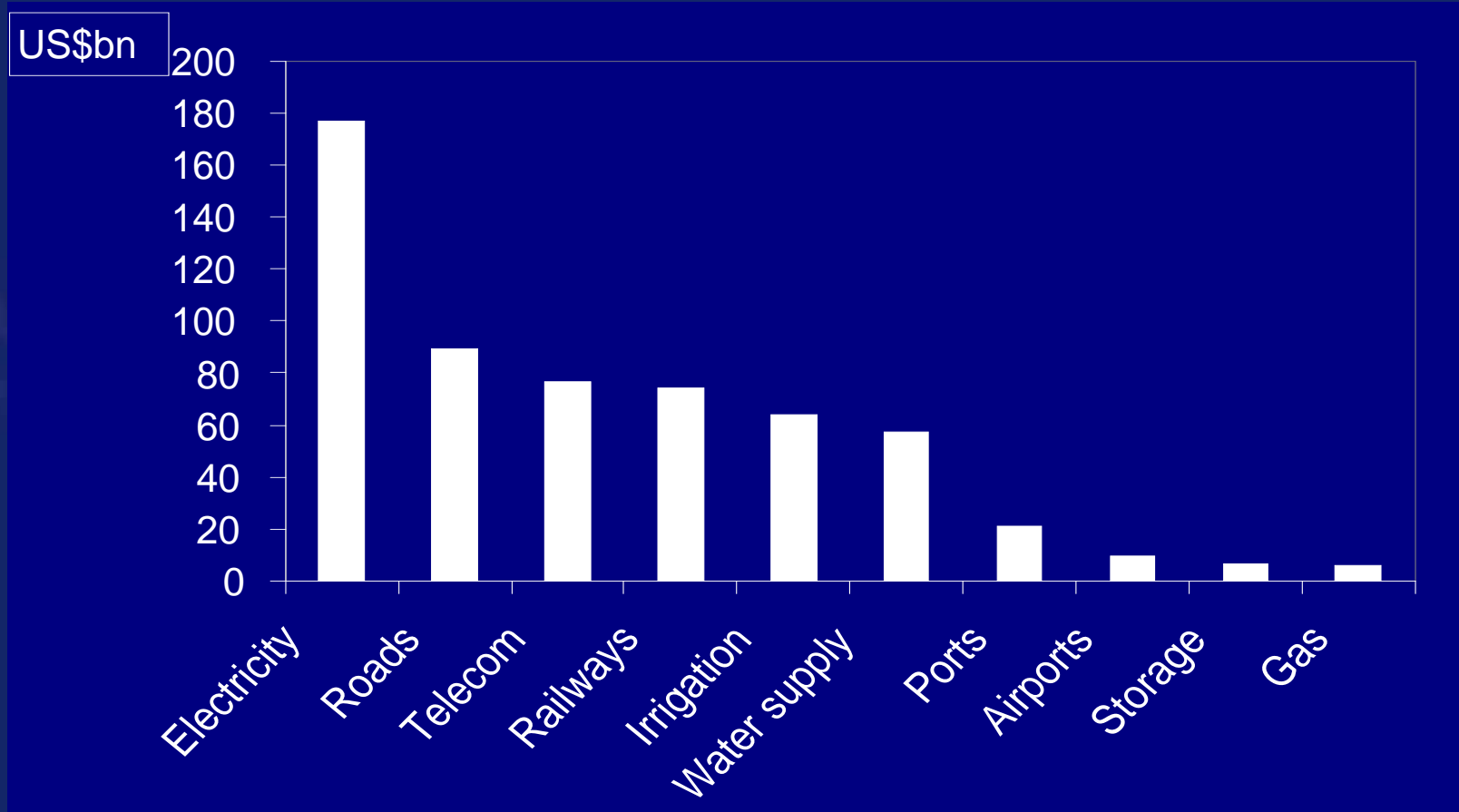
- **This will further fuel demand for universal intermediates – steel, cement, petroleum.**

- **The government's National Steel Policy estimates that steel production will rise from 40 mt in 2006 to 80 mt by 2011 and 120 mt by 2016, making India the world's second-largest steel producer.**

- **Funding is expected to come partially from the government's budget (30%) the public sector or from pure private investment and public private partnership (PPP) projects.**



Expected spending by sector



Power and transport sector growth projections

- A capacity addition of 78,577 MW (of which thermal power plants will be 58,644 MW) has been proposed by 2011

- Government projections: power sector will grow at 9.5% per year



- Government's decision to expand the national highway and road network dramatically is likely to further stimulate car and vehicle ownership

- Passenger car ownership has doubled in the last five years, from 509088 cars to 1076408 cars. Estimates of 12% CAGR.

- Launch of Tata's Nano in late 2008 – “the world's cheapest car” – will further stimulate demand for cars

- Explosive growth in civil aviation: Domestic air travel grew 32% in 2007. 35 airports across the country are being modernized

Risks to India's economic outlook

- India's fiscal problems re-emerge, diverting funds from economic development
- Difficulties in investment implementation:
 - public private partnership (PPP) model largely untested
 - hurdles/public protests over land acquisition (faced by steel projects, ultra mega power projects)
 - infrastructure development at state government level could be particularly problematic.
- Power sector reforms are still ongoing - aggregate technical and commercial losses of state transmission and distribution utilities continue to be high (more than 40% nationwide, as high as 60% in some states). Historically, capacity additions have fallen short of targets
- Political uncertainties – messy, highly fragmented coalition governments may find it difficult to implement plans; there could be backsliding.

The politics of petroleum price subsidies

- Government subsidizes retail prices of
 - (i) Kerosene and liquified petroleum gas (LPG) - the main domestic fuels
 - (ii) Petrol and high speed diesel – the main transport fuels
- Market-based reforms announced in 2002 were reversed in 2003 – politically difficult to streamline subsidies
- Oil Marketing Companies losing \$88 million every day – eventual liability will fall on government fiscal deficit
- The most recent petrol and diesel price hike in mid-February was 4%, a small fraction of the rise in oil prices since mid-2006 (30-40%). Further price rises unlikely as elections approach.

Oil demand estimates (Mt)

	Power Generation		Non-Power use		TOTAL	
	8%	9%	8%	9%	8%	9%
2003-04	6	6	113	113	119	119
2006-07	6	6	126	142	132	148
2011-12	8	8	158	178	166	186
2016-17	9	10	205	231	214	241
2021-22	12	12	266	299	278	311
2026-27	14	15	351	395	365	410
2031-32	17	20	469	528	486	548

Source: Planning Commission, India

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