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Indian growth story still intact: Citi

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MUMBAI: Even as the current financial year is likely to be crucial for India due to factors such as rising current account deficit and lower inflows, financial major Citi feels that the pressure could ease slightly from the next fiscal when trade deficit is expected to come down. Citi, in a recent report, mentions that while India growth story is not over, the growth would be lower and the currency would remain weak. The foreign financial major feels that India would gain from fresh hydrocarbon discoveries despite a likely 5% contraction in exports. It is also of the view that India has sufficient reserves to manage possible outflows. "Despite a likely 5% contraction in exports, lower oil prices (assuming the Indian basket at \$62/bbl) and a 66% volume increase in petroleum product exports from 43.8mt in FY09 to 72.7mt in FY10, we expect India's trade deficit to narrow to \$105 billion, down from \$117 billion in the current year," says Citi in its report dated December 4. On a positive note, India has sufficient reserves to finance even a worst case situation of all possible outflows, it adds. According to Citi, India's combined fiscal deficit for FY09, including all below-the-line items, is likely to come in at 8.6% of GDP, compared to around 6% during the previous year. However, it attributes this largely to various below-the-line items such as oil bonds, farm waivers, pay commissions and fertilizer subsidies. "Going forward, we expect to see an improvement in FY10 as a large part of the additional expenditure is oil related (additional fertilizer subsidies and oil bonds)," explains the report. Citi, however, does expect the overall deficit to remain in a range of 6.5-7% due to pressure from coalition politics and low tax to GDP ratio (16% of GDP). "As a result, we expect India's public debt to GDP ratio to remain over 75%. However, a silver lining would be eventual implementation of GST in 2009-10," says the report. On a different note, Citi expects the Indian currency to remain weak until de-leveraging subsidies and risk levels normalize. "Although our trade and current account deficit forecasts indicate an improvement, given the outlook for capital flows, we expect only marginal appreciation," it says. City's March FY09 and FY10 estimates now stand at Rs 48.50/\$ and Rs 48/\$, respectively. However, timing the reversal is difficult and would depend on risk appetite normalizing, it adds. Regarding politics, Citi notes that since 1989 parliamentary elections, no single party has won a majority on its own strength that has led to a lot of "defections, shifts in loyalties and horse-trading". The foreign financial major also feels that the 2009 elections would result in yet another fractured verdict. "Thus, while the base case is that the outcome could well be polarized between the BJP and the Congress (the two main parties), there is concern that the formation of a coalition government or a third front could impede reforms," says the report. While Citi acknowledges the fact that a fall in commodity prices has made Reserve Bank of India's job much easier, it also feels that the fall is likely to lead to deflation. "Similar to most other economies, the collapse in commodity prices coupled with slowing aggregate demand makes deflation likely in 2H09," says the report. The report concludes by saying that India would need to continue attempts to address key challenges such as bridging physical and social infrastructure constraints and ensuring inclusive growth across states. "This we believe will serve India well once risk appetite returns to normal," it says.