

Economic crisis will deepen, say business leaders

Chatterjee, Clifford Alvares with BS Bureau inputs | Mumbai August 21, 2013

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Most blame it on govt inaction, expect the rupee to weaken further and interest rates to fall



For corporate India, there seems to be just one villain in the worsening India story: The government.

A poll of 20 respondents comprising leading CEOs, bankers, market players and economists paints quite a grim picture. An overwhelming majority of the respondents said the Indian economy was heading for an unprecedented crisis due to mismanagement, lack of reforms, weak political leadership and policy paralysis that had led to infrastructural bottlenecks and stalled projects.

On the rupee, a majority said it would weaken by more than five per cent by the end of the year but interest rates would either fall or remain unchanged. The safe places to park money in these volatile times were specific stocks and bank fixed deposits, the poll showed.

“It’s the lack of political will in implementing bold economic reforms, poor infrastructure, overdue labour and land reforms, power deficit and unfriendly business regulations that are responsible for this mess,” says Kiran Mazumdar-Shaw, chairman and managing director of Bangalore-based Biocon.

Bajaj Auto Chairman Rahul Bajaj agrees. He says the country is paying for the past four years of inaction and absence of reforms. “The government has spent a lot of money in loan waivers, the National Rural Employment Guarantee Scheme and the food security programme. All these populist measures have now added to the deficit. We should be treating the disease and not the symptom,” he adds.

State Bank of India Chairman Pratip Chaudhuri, however, blames it on global factors as well. “The economy is facing problems mainly due to the global economic situation and liquidity squeeze in the domestic market,” he says.

Videocon Group Chairman Venugopal Dhoot says the sooner the government solves the capital account deficit problem, the better. His prescription: Boost exports and make acquisitions by Indian companies easier. There is a silver lining for companies with assets abroad, though. Every 100-paisa fall in the rupee against the dollar is adding Rs 1,000 crore to the valuation of Videocon’s overseas oil assets, estimated to be worth \$10 billion.

What went wrong?

Respondents say the Indian economy – once a darling of foreign investors — went into a tailspin in 2012 after former finance minister Pranab Mukherjee came out with the retrospective taxation proposal in his Budget. “Retrospective taxation was the biggest setback. It scared foreign as well as domestic investors,” says Ankit Miglani, deputy managing director, Uttam Galva Steels, in which steel magnate LN Mittal owns a significant stake. The tax vitiated the atmosphere when foreign investors in the telecom industry lost billions following a Supreme Court decision to cancel 2G licences.

Respondents say the threat of the US Federal Reserve’s tapering of its bond-purchase programme (quantitative easing) is another reason why the equity and money markets are nervous, but government inaction takes the cake. According to most, inflation will not fall in the next six months, even if the monsoon is good, though there is no threat of a downgrade of India’s sovereign rating by agencies in the near future.

CARE Ratings Chief Economist Madan Sabnavis says the economic slowdown can be attributed to a sharp decline in demand from consumption, investment, government orders and exports. Consumption is down due to high inflation, as households spend more on food.

Investment is down due to issues like \$120-billion projects being stalled, power plants going without gas, SC banning mining in many key states, etc. Government spending is down due to fiscal constraints and exports have fallen due to depressed global conditions. “Therefore, while one tends to look at interest rates only, these factors have kept growth down,” says Sabnavis. Respondents say until these issues are sorted, it will not be possible for the economy to revive.

On the rupee, JPMorgan’s Adrian Mowat says policy options are limited for the government and the Reserve Bank of India. “They have announced reform-plus-technical measures to support the currency. These have not worked,” he says. The International Monetary Fund (IMF) would typically prescribe higher interest rates to suppress domestic demand and lower imports to address the current account deficit. “This option is politically unpalatable, especially with general elections next year. Arguably, and more importantly, the equity flows are important in funding CAD. Higher interest rates and lower growth would likely result in foreign selling,” he says.

Miglani says it’s time the government relaxed norms for Indian companies to dollar debt. “When interest rates are high, dollar should flow in, but foreign direct investments and those from foreign institutional investors will not happen because investors are scared. So, the only option is debt. But right now, most of the debt is for capital expansion,” he adds.

U R Bhat, MD, Dalton Capital, says: “A general sense of drift among policy makers is the prime reason for this mess. This is probably because of the prosecution of some senior government functionaries for unfair decisions in the past that led to ineffective governance.”

Where to invest?

So where does an individual or a company deploy cash? Thirty-nine per cent of respondents say investing in specific stocks is a good option, while 33 per cent pitch for bank deposits.

Respondents say RBI has done its bit and now the ball is in the government’s court to change policies and improve sentiments. The long-term measures should make sure the economy revives and short-term measures improve the sagging market sentiment. “Opening up of FDI has been a good step but we need to see government doing away with non-essential controls in a big way. India should make a negative list for FDI and everything else should be free, irrespective of the amount an Indian company wishes to borrow,” says Siddharth Shankar, economist and advisor to financial firm, KASSA.

Govt says steps taken to narrow current account deficit

CAD touched a record high of 4.8% of GDP in 2012-13



The government today said it has taken several steps to narrow the current account deficit (CAD), which touched a record high of 4.8% of GDP in 2012-13 mainly due to high petroleum product and gold imports.

In a written reply in the Rajya Sabha, Minister of State for Finance Namo Narain Meena said the high CAD mainly reflected widening of the trade deficit on account of subdued external demand and relatively inelastic imports of petroleum, oil, lubricants, gold, silver and lower invisible surplus.

"The government has taken a slew of initiatives to boost exports and reduce imports to lower trade deficit and thereby CAD, and also to encourage capital flows to facilitate the financing of CAD," he said.

In absolute terms, the CAD in 2012-13 was \$88.2 billion, compared with \$78.2 billion in the previous financial year.

Measures to increase exports include extension of the interest subvention scheme, widening of the incremental exports incentivisation scheme and dollar-rupee swap facility.

The government also decided to increase the rate of interest subvention from 2% to 3% to benefit exporters in the small and medium enterprises segment and most labour-intensive sectors.

To reduce imports, duty on gold imports has been increased to 8% and inward shipments of the metal have been linked to their exports. The government has

also revised diesel prices and capped subsidised LPG cylinders to contain the subsidy bill.

To another query, Meena said several steps have been taken to revive growth in the economy, including setting up of the Cabinet Committee on Investment to speed up project implementation, liberalisation of FDI norms and new gas pricing guidelines.

Economic growth slowed to 5% in 2012-13 as against 6.2% in the previous fiscal.