

INDIA - ECONOMIC OUTLOOK FOR 2012

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As it has become clearer that Indian economy will not be able to achieve its GDP growth forecast of 8% or thereabouts, it might have to possibly settle for a figure slower than the government's revised estimate of 7.5%. This has been clearly visible on the performance of the domestic stock markets, which has been one of the world's worst performers, worse than the stock markets of other BRIC economies. We are not expecting the sentiments to improve in a flash, ie within the next few months and see a rally thereafter, even though we are a structurally strong economy with good fundamentals, India as a country in the present economic scenario cannot isolate itself from the risk posed by the global economic turmoil.

Factors hurting the domestic economy

Inflation and Capital Runaway has been the 2 main factors hurting the economy. Inflation has so far remained above 9% and RBI had done around 13 interest rate hike decision since December 2010 to curb inflation. Country's economic momentum has been dragging due to the monetary tightening and inflation issues.

Capital outflows, domestic corruption and policy paralysis (lack of policy developments) have also given a massive blow to the economic sentiments here. Foreign investors have also pulled out massive amounts of fund from India in order to cut their risk exposure to India. Foreign investors have only \$530 million in Indian equities this year, compared with \$28.9 billion a year ago, according to the Securities and Exchange Board of India (SEBI). India is a country with trade deficit, unlike China which is mainly an export driven economy India is a relatively smaller player with its exports account to only 10% of GDP and it needs a strong Rupee to make the imports cheaper and attract more foreign investments. A slowdown in FII inflows will severely affect India, which is structurally a current account deficit economy where the current account deficit is usually financed by the steady FII inflows, which actually helped to offset the capital deficit.

Don't expect RBI to cut rates in a hurry

We have seen a cycle of interest rate hike by RBI from Dec 2010 onwards and in its last policy meeting on 16th Dec 2011, it has hinted that they will look at reducing rates in the coming policy meetings. Some of the analyst's communities are expecting RBI to cut rates in a hurry; however we are of the view that it won't happen so fast.

If RBI proceeds with the reduction cycle, then it will be a breather for companies which are struggling for cash. Strong policy decisions from the government side will make India an attractive investment destination which will attract Strong fund flows and makes Rupee stronger. Inflation, in the longer run is expected to moderate to levels of around 4%. Beaten down sectors like Banking, Capital Goods, Infrastructure and Auto space will be the key sectors that will be in focus once the economy starts rebounding.

India might start outperforming by late 2012

The global economic outlook is still very uncertain, with the risks of a renewed recession in advanced economies and widespread financial crisis growing. Further deterioration of the economic crisis cannot be ruled out and it won't be good news for emerging economies including India. However we expect the current scenario to be a temporary scenario and considering the strong fundamentals India enjoys, along with improvement in domestic issues India is well positioned to outperform fellow Asian powerhouse China in terms of GDP growth in 2013. Both of these countries still remains among the top performers in the group of 25 so called Rapid Growth Markets (RGMs), which also includes Brazil and Russia.

Our advice to investors would be to adopt a cautious approach and start investing in smaller portions keeping a time frame of 2-3 years for earning better returns.

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