Economic Windfall for India as Global Growth Slows

Victor Mallet in New Delhi

Amid gloom over global economic growth and uncertain prospects for emerging markets, India is beginning to stand out as uniquely well-placed to gather the windfall benefits of an international slowdown.

Unlike Brazil, Russia or South Africa, India reaps immediate advantages for its terms of trade and its domestic budget from the fall in commodity prices triggered by renewed concerns about the world economy.

And unlike China, India will not suffer much from any decline in global demand for manufactured goods because its export sector is relatively small.

Commodities – mostly oil – account for more than half of India's imports but only 9 per cent of its exports, mainly food. The current account deficit falls by about $1bn a year for every $1 decline in the price of a barrel of oil, and the reduced cost of fuel subsidies is also easing the burden on the budget.

Another benefit of weaker commodity prices is falling inflation, long the bane of the Indian economy.

Annual consumer price inflation fell to 6.5 per cent in September on the back of softer food prices, with wholesale inflation hitting a five-year low of 2.4 per cent. Lower inflation should lead in turn to a decline in interest rates that would boost domestic investment. It all adds up to what Deutsche Bank calls "unambiguously positive" effects for India from falling oil prices.

Economists conclude that India could, in a year or two, overtake China to become the world's fastest-growing large economy.

But there are snags. International investors, for a start, are expected to shun what they perceive as risky emerging markets, and a global slowdown accompanied by lower oil prices would leave capital-surplus countries – in the Gulf, for example – with less money to invest in places such as India.

Nor is India's recovery guaranteed after the resurgence of business confidence that followed the election of Narendra Modi as prime minister five months ago.

The latest figures for industrial production showed output stagnating in August, rising just 0.4 per cent year-on-year, with manufacturing and capital goods both falling over the year. That was well below expectations and reinforced worries among investors about how tentatively the Modi government has embarked on the process of economic reform and revitalisation.

HSBC researchers lamented a "broad-based malaise in manufacturing". Raghuram Rajan, governor of the Reserve Bank of India, predicted that Indian growth would accelerate from about 5 per cent to 6 per cent next year, but warned of the need to eschew "grand-sounding announcements" and "do the basic stuff" to get the economy back on track. "We need to fix the plumbing," he said.

Economists and investors are urging the Modi government not to waste its strong electoral mandate or its recent luck with commodity prices.

If India is to profit from the "global windfall", says Rajeev Malik, senior economist at broker CLSA, the government needs to contain inflation, maintain fiscal discipline and clear the backlog of delayed infrastructure projects.

"The results of those would actually be pretty powerful," he says. "Modi's success would not be getting the cyclical recovery to 6.5 or 7 per cent growth. It's getting growth upward of 8 per cent on a sustained basis."