

**Asia Business Generator Project**

**Indian Economy**

**Annual Report (2008 – 2009)**

**Osaka International Business Promotion Center**

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### Overview of Indian Economy

The Indian economy had moved to a high growth phase during 2003 to 2008, but suffered a major decline in 2008-09 on account of the global financial crisis. The factors responsible for rapid expansion of the economy from 2003-2008: robust investment growth, high rate of domestic savings, strong corporate performance and good tax buoyancy were largely undone by the global financial and economic crisis in the second half of 2008-09.

The impact of the slowdown has been broad-based in nature. Growth in Industrial and Agricultural sectors moderated significantly during the year. The services sector managed to minimize the effects of the slowdown with a 9.5% growth (compared to 10.9% last year). Merchandise exports grew by a mere 5.7% during 2008-09 as compared to a 26% growth during last year.

The outlook for the Indian economy continues to be subdued with recovery expected only in the second half of 2009-10.

### **Gross Domestic Product (GDP)**

Gross Domestic Product (GDP) at current market prices is estimated at USD<sup>1</sup> 1.18 trillion in 2008-09 by the Central Statistical Organisation (CSO) in its advance estimates (AE) of Gross Domestic Product.

GDP at factor cost at constant 1999-2000 prices is estimated by the CSO to grow at 7.1% in 2008-09. This represents a deceleration from the high growth rates of 9.7% and 9.0%, respectively, in the previous two years.

### **Rate of Growth of GDP at factor cost at 1999-2000 prices**

Particulars	2006-07	2007-08	2008 – 2009(E)
GDP	9.7%	9.0%	7.1%
Manufacturing Sector	11.8%	8.2%	4.1%
Mining and Quarrying	8.8%	3.3%	4.7%
Finance, Insurance and real estate	13.8%	11.7%	8.6%
Construction	11.8%	10.1%	6.5%
Agriculture and allied activities <sup>2</sup>	4.0%	4.9%	2.6%

- Agricultural growth decelerated to 2.6% in 2008-09.

<sup>1</sup> Taking average USD-INR exchange rate for April 2008-March 2009 (INR45.95 / USD)

<sup>2</sup> Includes Forestry, Logging and Fishing

- Manufacturing which grew at 8.2% in 2007-08, decelerated by about 4.1 percentage points in 2008-09. The Construction sector also slipped by about 3.6 percentage points to a 6.5% growth rate in 2008-09.
- The Index of Industrial Production<sup>3</sup> suffered its worst year in 2008-09. After having grown between 8-11% in the preceding 4 years, it witnessed a growth of only 3.4% in 2008-09.

### **Inflation**

The Wholesale Price Index (WPI) touched double digit growth rate in the month of June 2008 and peaked to 12.8% during August 2008. This prompted the Government to take action on the monetary policy to curb rising prices.

Year	Whole Sale Price Index				
	Primary Articles <sup>4</sup>	Manufacturing products <sup>5</sup>	Fuel and lubricants	Overall	Inflation <sup>6</sup>
2006 . 2007	209	179	324	206	5.42%
2007 . 2008	225	188	327	216	4.70%
2008 . 2009	248	203	357	234	8.40%

Within a span of seven months, the WPI came down from the high of August 2008 (12.8%) to 0.27% during the week ending March 14, 2009. The crash in commodity prices (especially crude oil, metals and agricultural commodities) in the international markets has been largely responsible for such a steep fall in inflation in the domestic economy.

The Consumer Price Index (CPI-IW) has been relatively rigid as compared to the WPI. After a slight moderation in December 2008, it went back to its previous level (10.4 % in October . November 2008) in January 2009. The relative rigidity is on account of the higher weight of food items (46%) in the index whose prices have remained relatively high.

### **Foreign investment Inflows**

During the year 2008 - 2009 (April 2008 . January 2009), inflows under Foreign Investment were USD 15.55 billion as compared to USD 63.76 billion in the previous financial year (April 2007 . March 2008).

<sup>3</sup> Index of Industrial Production (IIP) represents the status of production in the industrial sector for a given period of time as compared to a reference period of time. The general index of industrial production compiled in India currently includes mining, manufacturing, and electricity sectors only

<sup>4</sup> Primary articles include Food grains, Minerals and non . food articles

<sup>5</sup> Manufactured products include Textiles, Machinery and machine tools, Chemicals and food products

<sup>6</sup> Measured as % growth of overall price index over previous year

<b>Particulars</b>	<b>2006 – 2007*</b> (USD Billion)	<b>2007 – 2008*</b> (USD Billion)	<b>2008 – 2009**</b> (USD Billion)
Direct investment (FDI)	22.08	34.36	27.43
Equity <sup>7</sup>	16.48	26.87	24.22
Reinvested earnings	5.09	7.17	3.01
Other capital	0.51	0.32	0.20
Portfolio investment	7.00	29.40	-11.88
GDRs / ADRs	3.78	8.77	1.14
FIIIs	3.22	20.33	-13.02
Offshore funds and others	0.00	0.30	0.00
<b>Total</b>	<b>29.08</b>	<b>63.76</b>	<b>15.55</b>

\* April to March, \*\* April to January.

The sharp fall has been on account of withdrawal of more than USD 13 billion from the Indian markets by the Foreign Institutional Investors (FII) during the period April 2008 . January 2009.

It needs to be highlighted that most of the FDI is routed through Mauritius on account of tax exemptions. Singapore, USA, UK, Netherlands and Japan are the other key contributors of FDI inflows in India.

<b>Country</b>	<b>2007 – 2008*</b> (USD Billion)	<b>2008 – 2009**</b> (USD Billion)	<b>Cumulative FDI equity inflows<sup>8</sup></b> (USD Billion)	<b>% of total cumulative FDI equity inflows</b>
Mauritius	11.096	9.545	35.180	41%
Singapore	3.073	3.237	7.594	9%
USA	1.089	1.639	6.172	7%
UK	1.176	0.791	5.154	6%
Netherlands	0.695	0.826	3.531	4%
Japan	0.815	0.264	2.390	3%
Other countries	6.635	7.583	26.375	30%
<b>Total FDI Equity Inflows<sup>9</sup></b>	<b>24.579</b>	<b>23.885</b>	<b>86.396</b>	<b>100%</b>

<sup>7</sup> Includes FIPB (foreign investment promotion board), Automatic and Acquisition routes, and Equity capital of unincorporated bodies

<sup>8</sup> April 2000 to December 2008

<sup>9</sup> Does not include Equity Capital of unincorporated bodies

\* April to March, \*\* April to December.

Services sector, Computer software & hardware and Telecommunications were major sectors for FDI inflows during 2008-09 followed by Housing & Real Estate and Construction.

Sector	Amount of FDI Equity inflows <sup>10</sup>			
	2007 – 2008* (USD Billion)	2008 – 2009** (USD Billion)	Cumulative inflows <sup>11</sup> (USD Billion)	% of total cumulative inflows
Services sector <sup>12</sup>	6.615	5.061	18.118	21%
Computer software & hardware	1.410	1.599	8.876	10%
Telecommunications <sup>13</sup>	1.261	2.374	6.216	7%
Housing & Real Estate	2.179	2.408	5.119	6%
Construction <sup>14</sup>	1.743	1.866	5.029	6%
Automobile industry	0.675	1.074	3.310	4%
Other sectors <sup>15</sup>	10.696	9.503	39.728	46%
<b>Total</b>	<b>24.579</b>	<b>23.885</b>	<b>86.396</b>	<b>100%</b>

\* April to March \*\* April to January

## **Domestic Financial Markets**

### **Trends in the Primary markets**

The primary market witnessed a decline during the period April 2008- February 2009. The total amount of funds mobilised by the corporate sector were merely 13% of the amount mobilised last year for the same period. The number of issues also declined from 152 in 2008-09 to only 44 during 2008-09.

<sup>10</sup> Does not include Equity Capital of unincorporated bodies

<sup>11</sup> April 2000 to January 2009

<sup>12</sup> Financial and non . financial services

<sup>13</sup> radio paging, cellular mobile, basic telephone services

<sup>14</sup> Includes roads and highways

<sup>15</sup> Indicative list of other sectors are drugs & pharmaceuticals, power, petroleum, mining, chemicals, housing and real . estate. Total number of sectors covered in others - 58

Particulars	2007 -08*		2008 – 09**	
	No of Issues	Amount (USD Billion)	No of Issues	Amount (USD Billion)
1. Public Issues	88	11.76	21	0.45
IPOs <sup>16</sup>	81	9.16	21	0.45
FPOs <sup>17</sup>	7	2.60	0	0
2. Rights Issues	26	6.63	21	2.61
3. QIP <sup>18</sup>	38	5.61	2	0.04
<b>Total</b>	<b>152</b>	<b>23.99</b>	<b>44</b>	<b>3.10</b>

\*\* April to February

#### Private Placement of corporate debt

In contrast, funds raised by the corporate sector through debt issues witnessed a growth of 60% over the amount raised last year during the same period (April - February). The number of issues also increased from 872 to 1011 during 2008-09.

Year	BSE		NSE		Total	
	No of Issues	Amount (USD Billion)	No of Issues	Amount (USD Billion)	No of Issues	Amount (USD Billion)
2007 -08*	284	6.23	588	19.37	872	25.60
2008 -09*	362	7.81	649	33.09	1011	40.90

\*April to February

#### Trends in the Secondary markets

The Bombay Stock exchange (BSE) Sensex which touched the 21,000 mark in January 2008, witnessed progressively sharp decline during the year and reached 8160 in the second week of March 2009. Similarly, the National Stock exchange (NSE) Index NIFTY after having touched 6100 levels in 2007, closed at 2764 in February 2009. The equity market movements largely followed the global cues against the backdrop of weak domestic indicators from the economy.

<sup>16</sup> IPO: Initial Public Offering

<sup>17</sup> FPO: Follow on Public Offering

<sup>18</sup> QIP: Qualified Institutional Placement

This fall in market indices was not only due to the global economic recession but also on account of slowdown in the Indian industry and eroding corporate profitability during the year.

Month	BSE Sensex		NSE 50 Index	
	Index*	QoQ % change	Index*	QoQ % change
March 2008	15,644	-22.9%	4,734	-22.9%
June 2008	13,462	-13.9%	4,041	-14.6%
September 2008	12,860	-4.5%	3,921	-2.9%
December 2008	9,647	-24.9%	2,959	-24.5%
March 2009	9,708	0.6%	3,021	2.1%

\* Index value on the last day of the month

The stock markets reflected the state of the Indian economy and registered negative return to the tune of 38% during the year 2008-09.

On the positive side, the valuation of Indian stocks as reflected in P/E multiples was around 12.5 times at end of February 2009, which was the highest amongst the select emerging market economies such as South Korea, Thailand and Taiwan

Both the BSE Sensex and the NSE 50 Index have shown marginal recovery in the month of March 2009. However, the market observers are skeptical about the sustainability of the capital markets given the further slowdown expected in the economy.

### **Foreign Trade**

Merchandise exports were significantly impacted by the global economic slowdown. The value of exports was USD 168 billion during 2008-2009 registering a meagre 6% growth as against 26% last year.

Merchandise imports also reflected the economic slowdown in the country with only 21% growth as compared to 29% in the previous year.

Year	Exports (USD Billion)	Imports (USD Billion)	Exports (% growth*)	Imports (% growth*)	Trade Balance (USD Billion)
2007 . 2008	159.0	238.6	26%	29%	-79.6
2008 . 2009 <sup>19</sup>	168.6	287.7	6%	21%	-119.1

\* Over previous year

<sup>19</sup> Includes quick estimates for March 2009 by the Ministry of Commerce

Trade deficit increased by about 50% during 2008-09 to touch USD 119 Billion. The trade deficit is expected to narrow during the next year on account of falling cost of crude oil and other commodity prices.

### Commodity Exports

During the period April - October 2008, manufactured goods were the most important commodity in India's export basket contributing 64% share. However, it exhibited the slowest growth among the categories. This was because the exports of labour-intensive sectors such as textiles, gems and jewellery and leather had been adversely affected under the impact of demand recession, mainly in the developed regions viz., the European Union and the United States.

Commodity Exports	April – Oct 2007 (USD Billion)	April – Oct 2008 (USD Billion)	% Growth*
Primary products	12.61	15.96	27%
Manufactured goods	57.62	69.53	21%
Petroleum products	15.12	20.45	35%
Others	2.46	2.46	0%
<b>Total</b>	<b>87.81</b>	<b>108.40</b>	<b>23%</b>

\* April – October 2007 to April - October 2008.

### Commodity Imports

During the period April - October 2008, Petroleum, Petroleum products and related materials were the most important commodity (in terms of value as well as growth) in India's import basket contributing more than 50% share.

Commodity Imports	April – Oct 2007 (USD Billion)	April – Oct 2008 (USD Billion)	% Growth*
Petroleum, Petroleum products and Related Material	60.20	98.01	63%
Capital Goods <sup>20</sup>	30.93	37.08	20%
Pearls, Precious and semi . precious stones	5.49	4.72	-14%
Others	36.53	44.44	22%
<b>Total<sup>21</sup></b>	<b>133.15</b>	<b>184.21</b>	<b>38%</b>

\* April – October 2007 to April - October 2008.

<sup>20</sup> Includes Machinery . electrical and non . electrical, Machine tools and transport equipment

<sup>21</sup> Difference in total imports due to difference in months for which data is reported

The high growth in Petroleum imports during the above period was largely due to higher international crude oil prices that prevailed during May-August 2008.

### **Exchange Rate**

The exchange rate of the Indian Rupee was Rs. 50.95 per USD on March 31<sup>st</sup> 2009. The rupee weakened vis-à-vis the US Dollar, Euro and the Japanese Yen but gained vis-à-vis the British Pound.

<b>Exchange rate<sup>22</sup></b>	<b>2006 – 2007</b>	<b>2007 – 2008</b>	<b>2008 – 2009</b>	<b>Depreciation*</b>
1 US Dollar	Rs. 43.441	Rs. 39.945	Rs. 50.950	21.6%
1 Pound Sterling	Rs. 85.255	Rs. 79.695	Rs. 72.861	- 9.4%
1 Euro	Rs. 57.930	Rs. 63.113	Rs. 67.480	6.47%
100 Japanese Yen	Rs. 36.840	Rs. 40.270	Rs. 51.870	22.36%

\* From 2007 – 2008 to 2008 – 2009

The Rupee weakened against the UD Dollar on account of net FII outflows to the tune of nearly USD 0.6 Billion in the last week of February. The general strengthening of the dollar against emerging market currencies also contributed to the depreciation.

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<sup>22</sup> Exchange rates at the end of the year.

## **Government Policy**

### **Fiscal Policy Changes**

With the objective of stimulating the economic growth, the government declared three fiscal stimulus packages during the period December 2008 to February 2009. Key measures taken are outlined below.

#### **Duty reductions:**

- Central value-added tax (CENVAT)<sup>23</sup> reduced by 4% from 14% to 10%
- Service tax reduced by 2% from 12% to 10%
- Excise duty<sup>24</sup> reduced by 4% for cement, household appliances, textiles, steel and by 2% on items that currently attract the 10% rate
- Export duty on iron ore fines withdrawn and on iron ore lumps and pellets reduced to 5%
- Import duty on naphtha for use by the power sector reduced to zero
- Exemptions from counter-vailing duties (CVD) on TMT bars and structurals, and CVD and Special CVD on cement

#### **Incentives for the automobile sector:**

- Accelerated depreciation of 50% will be provided on commercial vehicles bought on or after January 1, 2009 upto March 31, 2009
- SPV created to provide liquidity support to NBFCs for financing Commercial Vehicles

#### **Incentives for housing and infrastructure sector:**

- Loans less than USD 0.04 million granted by banks to be classified under priority sector
- USD 0.8 billion re-finance facility for National Housing Bank (NHB)

#### **Incentives for infrastructure sector:**

- India Infrastructure Finance Company Ltd (IIFCL)<sup>25</sup> authorized to raise USD 2 billion via tax-free bonds by March 2009, with approval to raise an additional USD 6 billion

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<sup>23</sup> In India, an excise tax is levied on the manufacturer of goods when those goods leave the place of manufacture. Formerly called the Central Excise Duty, this tax is now known as the Central Value Added Tax (CENVAT). Manufacturers may offset duty paid on materials used in the manufacturing process by using that duty as a credit against excise tax through a process known as Central Value Added Tax Credit (CENVAT Credit). The offsetting process was formerly known as Modified Value Added Tax (MODVAT).

<sup>24</sup> Central Excise duty is an indirect tax which is levied and collected on the goods/commodities manufactured in India

- IIFCL to refinance 60% of commercial bank loans for PPP projects involving an investment of USD 20 billion over the next 18 months

**Incentives for exports:**

- Interest subsidy of 2% for pre and post-shipment export credit till March 31, 2009 for labour-intensive exports like textiles, leather, marine products and SME sector.
- Interest rate ceiling on external commercial borrowings (ECBs) scrapped under RBI approval route

**Monetary Policy changes**

The RBI has been easing its monetary policy stance over the last two quarters. It has made the following changes:

- Reduced the Cash Reserve Ratio (CRR)<sup>26</sup> by 4% (from 9% to 5%) . this has facilitated a release of huge liquidity through the banking system
- Reduced the Repo rate<sup>27</sup> by 4% (from 9% to 5%)
- Reduced the Reverse repo rate by 2.5% (from 6% to 3.5%)

The above measures have resulted in not only in release of liquidity to over USD 76 billion, but also softening of lending rates of the banks by about 250 to 350 basis points for many class of borrowers

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<sup>25</sup> IIFCL is a dedicated institution purported to assume an apex role for financing and development of infrastructure projects in the country

<sup>26</sup> CRR : The portion (expressed as a percent) of depositors' balances banks must have on hand as cash or with the Reserve Bank of India

<sup>27</sup> Repo-rate: Discount rate at which a central bank repurchases government securities from the commercial banks, depending on the level of money supply it decides to maintain in the country's monetary system

### **Impact of fiscal and monetary changes on select sectors**

<b>Industry Sectors</b>	<b>Impact of fiscal and monetary policies</b>	<b>Overall effect</b>
Automobiles	<ul style="list-style-type: none"> <li>Reduction in ownership cost for vehicles due to cut in excise duty, fuel prices and car finance rates ⇒ <i>Demand for automobiles expected to improve</i></li> </ul>	Marginally positive
Banking and Finance	<ul style="list-style-type: none"> <li>Fiscal and monetary measures facilitating better credit availability ⇒ <i>Domestic and corporate consumption expected to revive</i></li> <li>RBI allowance for restructuring commercial loans with banks until June 2009 ⇒ <i>Asset quality expected to weaken leading to greater stress on the banking sector</i></li> </ul>	Neutral
Cement	<ul style="list-style-type: none"> <li>Reduction in home loan interest rates and increased infrastructure outlay by the government ⇒ <i>Demand expected to increase</i></li> </ul>	Marginally positive
Construction	<ul style="list-style-type: none"> <li>The government has increased the outlay for developing urban infrastructure and highways ⇒ <i>Healthy order book for construction companies</i></li> <li>IIFCL authorized to raise funds via tax free bonds ⇒ <i>Reduction in order execution delays</i></li> </ul>	Marginally positive
Household appliances	<ul style="list-style-type: none"> <li>Reduction in excise duty from 16% to 12% ⇒ <i>Limited impact as majority of manufacturers have passed on the benefits</i></li> </ul>	Neutral
Housing	<ul style="list-style-type: none"> <li>Classification of loans under Rs. 2 million as priority sector lending ⇒ <i>Lending by banks/NBFCs expected to increase</i></li> <li>Reduction in home loan rates by banks ⇒ <i>Demand for housing expected to improve</i></li> </ul>	Marginally positive
Media and entertainment	<ul style="list-style-type: none"> <li>Exemption of customs duty on newsprint, uncoated paper for publishing newspapers and lightweight coated paper for printing magazines ⇒ <i>Relief on margins for publishers</i></li> </ul>	Marginally positive
Steel	<ul style="list-style-type: none"> <li>Imposition of import duties on flat and long products and classification of HR coils under restricted category ⇒ <i>Demand for domestic steel expected to increase on account of competitive pricing</i></li> <li>Withdrawal of export duty on iron ore fines and reduction of export duty on iron ore lumps and pellets ⇒ <i>Export of iron ore expected to increase</i></li> </ul>	Marginally positive

## **Other policy developments**

### **Daily foreign newspapers allowed 100% FDI**

Owners of the daily foreign newspapers would be allowed to make up to 100% FDI in their facsimile editions published in India. However, Government's prior approval for publication of facsimile edition will be required. Earlier, the facsimile editions of foreign newspapers were allowed FDI up to 26%. For the publication of Indian editions of foreign magazines dealing with news and current affairs, up to 26% of FDI would be permitted.

### **Guidelines for transfer of ownership and control of Indian companies in sectors with caps**

The Department of Industrial Policy and Promotion (DIPP)<sup>28</sup> has made it mandatory for Indian companies to seek Foreign Investment Promotion Board's (FIPB)<sup>29</sup> approval, if it intends to transfer ownership or control to a foreign company in restricted sectors such as telecom, defence production, air transport services and broadcasting.

### **Implementation of Mobile Number Portability (MNP) likely in 2009**

The Department of Telecommunications (DoT) has selected two companies (Syniverse and Telecordia) to implement MNP services in the country in 2009. These companies will provide Indian operators with number portability clearing house and centralized database solutions. The MNP implementation will first focus on the larger metropolitan service areas before moving into rural locations.

### **3G auctions postponed indefinitely**

3G auctions, which were scheduled to be held during the last quarter of 2008-09, have been postponed indefinitely on continued uncertainty on base price for the auction. The auctions are now likely to take place only post the central elections scheduled during April-May 2009.

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<sup>28</sup> The DIPP is the body responsible for facilitating investment and technology flows and monitoring industrial development in the liberalized environment

<sup>29</sup> FIPB is the body to consider and recommend foreign direct investment (FDI), which do not come under the automatic route

## **Select Sector overview**

### **Automobile Sector**

The automobile sector in India, after a very healthy performance of the previous four years (2004 to 2008), grew by only 3% (in volume terms) during 2008-09. Indeed, the domestic sales received a setback with a mere 0.7% growth. Stringent credit disbursement norms, longer processing periods and adverse financing conditions, coupled with weak consumer sentiment due to uncertainty over income growth were responsible for the slow growth during the large part of this period.

However, the sector exhibited initial signs of recovery in the last quarter of 2008-09 (14% QoQ volume growth) after a dismal performance in the third quarter (-20% QoQ volume growth). The sales volumes witnessed a revival on account of government's stimulus package, robust farm income and new product launches by the manufacturers.

Easing monetary policy and excise rate cuts are expected to drive the demand improvement in 2009-10. Renewed focus of Public sector banks and manufacturer tie-ups with vehicle financiers are expected to improve the availability of vehicle finance. In addition, reduction in prices of key raw materials like steel, aluminum and rubber would help the manufacturers improve their margins.

### **Real Estate Sector**

The real estate sector experienced a substantial slowdown in 2008-09 after registering buoyant growth in the previous 3 years. Overall weak sentiment, low affordability, substantial increase in interest rates (during September to December 2008) and risk aversion by banks on the exposure towards the real estate sector negatively affected the developers. Net sales declined sharply (by 17%), with reduction in the number of transactions as well as sale prices.

Since February 2009, the sector has witnessed a gradual pick-up in demand for the affordable housing segment in certain regions. Mortgage rate cuts by lending majors and the debt rescheduling / restructuring window presented by RBI have prompted renewal of construction activities by the developers during the last quarter. However, the commercial, retail and premium housing continue to remain under pressure with no signs of demand pick-up in the near term.

## **Telecom Sector**

The telecom sector in India managed to keep itself insulated from the economic slowdown and exhibited robust growth. It grew by about 50% with more than 120 million mobile subscribers being added in 2008-2009 to the subscriber base of 261 million at the end of March 2008.

Subscriber net addition momentum accelerated during the last quarter of 2008-09. Monthly additions averaged 14.5 million during January-March 2009 v/s an average of about 10 million during second half of 2008. The increase in net additions was well distributed across regions.

On the regulatory front, 3G auctions (originally scheduled for the fourth quarter of 2008-09) have been postponed, termination charges have been cut by 33% effective April 1 2009, and selection process for third-party Mobile Number Portability (MNP) operator has been concluded, paving way for likely implementation by end of 2009. The cut in service tax from 12% to 10% is expected to impact the sector positively.

## **IT Services sector**

The IT services sector, after a remarkable buoyancy of the previous nearly two decades, grew by at a moderate pace of 9.7% (in dollar terms) during the period April 2008- December 2008. The global economic slowdown prompted the IT consumers across various sectors (especially BFSI<sup>30</sup>) to cut IT budgets and freeze non-discretionary spending during 2008-09. The appreciation of the rupee in the early part of the year led to lower realizations for the IT companies in India. Furthermore, there had been price cuts across the board. The top five IT companies in India renegotiated almost \$1.5 billion worth of outsourcing contracts since September 2008 at around 15% lower rates.

The prospects of the IT sector is dependent on clients lifting their freeze on IT spends and adopting off-shoring to cut costs. The large IT players would need to spend more on their selling and marketing efforts in order to garner business, thereby increasing their costs. Infosys, the second largest IT player in India, underlined the domestic IT industry's vulnerability on the global developments with a forecast of a fall in revenue and earnings (in dollar terms) for 2009-10.

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<sup>30</sup> Banking, Financial Services and Insurance

## **Outlook for 2009 – 2010**

The factors that were responsible for rapid expansion of the economy in the last five years: high private consumption expenditure, robust investment growth supported mostly by high rate of domestic savings, strong corporate performance, acceleration of exports and good tax buoyancy have been affected adversely by the global financial and economic crisis in the second half of 2008-09. The crisis, which started with high default rates in sub-prime mortgages in the US, spread to financial markets around the world and led to a global economic recession in 2008-09.

The continued fallout from the global economic slowdown is also expected to pull down the growth further in 2009-10. Industrial growth is expected to remain weak due to slowdown in demand . both in exports and domestic markets. The main driver, the services sector is also expected to witness sharp moderation in growth rates. Even so, we expect India's overall real GDP growth to remain fairly high in 2009-10, and it would continue to be the second fastest major growth economy in the world after China.

The inflation rate (WPI) is already close to 0% and is expected to enter negative territory during the first half of 2009-10 since international crude oil prices are expected to remain at a relatively low level due to global economic slowdown. The inflation rate would start picking up during the latter half of the year as demand recovers.

The business and industry are expecting further softening of interest rates, given the current scenario of zero inflation. The rupee is expected to depreciate further by 4-5% during the first half of 2009-10. This is on account of the expanding trade deficit, expected recovery in crude oil prices and expectations of low foreign capital inflows into the country.

Taking account of global developments and the Indian factors, we expect India's overall real GDP growth rate to decelerate to 5.5% - 6% in 2009 -10, as compared to likely revised estimate of growth rate around 6.5% for the previous year.

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