India set for fair growth despite reform headwinds

REUTERS, *Beijing*

Twenty years ago, India was in the throes of a balance-of-payments crisis that forced it to airlift 47 tonnes of gold to London to pledge with the Bank of England as collateral for an emergency $400 million loan.

Since that national humiliation, nearly 200 million people have climbed out of extreme poverty and India's share of global output has more than doubled. Per capita GDP, measured in dollars at purchasing power parity, has risen more than five-fold.

The architect of India's renaissance is the current prime minister, Manmohan Singh, who took over as finance minister in June 1991 and lit the blue touch paper for growth by dismantling the "Licence Raj" that had India tied up in red tape.

As prime minister, Singh has disappointed reformers.

He has failed to overcome opposition to market opening in sectors such as retailing and financial services; infrastructure, the sinews of any economy, is woeful; and a long-awaited national goods and service tax has still not been launched.

Given these shortcomings and Delhi's perennial struggle to cap inflation and the budget deficit, it speaks volumes for the underlying vibrancy of the economy that many forecasters remain confident about India's chances in coming years.

"I am very very hopeful of the next five to seven years. I think we can sustain this growth," said S. Narayan, who was economic adviser to former Prime Minister Atal Bihari Vajpayee.

REUTERS
Labourers work on reinforcing bars at a construction site to build a bridge on the outskirts of Ahmedabad, India.

The International Monetary Fund says India has the potential to grow between 8 percent and 8.5 percent a year over the medium term. Economists at Citi are even more bullish: they project 8.8 percent annual gross domestic product growth between 2010 and 2015, shading the rate of 8.7 percent pencilled in for China.

"I think 8 percent is the new normal," said Sanjaya Baru, editor of the Business Standard newspaper and Singh's former press adviser.

In his annual budget presented on Monday, Finance Minister Pranab Mukherjee forecast 9 percent growth in the fiscal year starting in April, up from an expected 8.6 percent this year.

The optimism is anchored by India's favourable age profile. With a young population, private saving increased from 24 percent of GDP in 2000 to 35 percent in 2009, fueling a spurt in investment-led growth. The working-age ratio will keep rising rapidly until 2021 before levelling off perhaps a decade later.

"The demographic dividend is projected to peak over the next two decades, adding about 2 percentage points to annual per capita income growth over the period," IMF economists Shekhar Aiyar and Ashoka Mody said in a recent Working Paper.

And as incomes rise, some households that now consume all they produce will be able to start saving for the first time.

As a result, the IMF expects India's gross savings to reach 41.7 percent of GDP by 2015, propelling investment to 44 percent of GDP from less than 38 percent today.

It all sounds too good to be true, and for Razeen Sally, director of the European Centre for International Political Economy, a Brussels research outfit, it is.

Sally bemoans "exuberant optimism" and says India is more protected against imports and inward investment than China and other regional rivals. Its public finances, infrastructure and lower-education system are also much weaker, he argues.

"Absent further market reforms, India will not have what it desperately needs: east Asian-style, labour-intensive agricultural, services and industrial growth," he wrote in a paper.

As expected, Mukherjee's budget was light on deep-seated reforms.

Narayan, the former adviser, is not optimistic about the prospects for market-opening measures, for instance to lure more foreign direct investment. But he and Baru, the newspaper editor, both said they were hopeful that Singh's agreement to hold an enquiry into a telecoms scandal would usher in better governance.

The country's auditor estimates that India lost up to $39 billion when the telecoms ministry gave out licences at below-market prices in 2007/2008.

The telecoms scandal is grist to the mill of those who argue that India's economy thrives despite, not thanks to, the government. In China, many would say the opposite is true, even though official corruption is widespread.

In GDP per capita, China and India were neck and neck at the start of the 1990s. Now the average Chinese is three times richer. India's share of world output has doubled since then, but China's has quadrupled. China's infant mortality rate is a third of that in India.

"China is a great success story and we need to do more to catch up. Certainly, among policy makers there is an awareness that China's economy is far stronger and its relations with the world are on a firmer footing," said Baru.

The overriding priority, he said, is to improve the quality of infrastructure -- from roads, railways and power to education, health care and urban services such as sanitation.

Narayan, who is head of research at the Institute of South Asian Studies at the National University of Singapore, said he would like India to emulate China's rapid construction of a high-speed cross-country rail network.

A 1,300 km, $33 billion line linking Beijing and Shanghai, due to open in June, was built in just over three years.

The inconvenient truth, though, is that things can get done faster in a single-party state than in a boisterous democracy.

Eurozone ups growth forecast

AFP, *Brussels*

The European Commission raised its eurozone 2011 growth forecast to 1.6 percent on Tuesday but warned that markets remain fragile and unrest in the Arab world threatens to drive up inflation.

The European Union's executive arm, which last November had forecast 2011 growth of 1.5 percent, said the improved outlook was supported by "better prospects for the global economy and upbeat EU business sentiment."

But the recovery is expected to remain uneven among the 17 nations that share the euro, with the export-driven German economy leading the pack while debt-stricken southern countries lag behind as they slash spending.

"While exports should continue supporting the recovery, a rebalancing of growth towards domestic demand is expected for 2011, resulting in more sustainable growth," said EU economic affairs commissioner Olli Rehn.

"However, the recovery remains uneven and many member states are going through a difficult phase of adjustment," he said after the commission released an interim forecast based on data from the EU's seven biggest economies.

Growth in 2011, despite the upgrade, will be slightly lower than last year.

The eurozone economy expanded by 1.7 percent in 2010 after the global financial crisis caused it to shrink by a record 4.1 percent in 2009.

The commission also raised its growth forecast for the 27-nation European Union, which includes non-euro countries such as Britain and Poland, by 0.1 percentage points to 1.8 percent.

Financial markets are recovering from the sovereign debt crisis in the eurozone, which forced Greece and Ireland to take bailouts last year, but the overall situation remains "relatively fragile," the commission said.

The borrowing costs of nations with high public deficits have stayed at elevated levels, while "important vulnerabilities" remain in the sustainability of public finances in some states and the funding of private banks.

The commission also hiked its 2011 inflation forecast for the eurozone from 1.8 percent to 2.2 percent, above the European Central Bank's 2.0 percent threshold for price stability.

"To a large extent this can be attributed to the surge in commodity prices towards the end of the year," the EU executive said in its report.

Inflation will peak in the first quarter of 2011 before gradually falling back towards 2.0 percent by the end of the year, the commission forecast.

At the same time, inflation "may prove to be volatile in the course of 2011" due in part to geopolitical tensions, with turmoil in oil-producing nations in North Africa and the Middle East threatening to weigh on eurozone prices.

"Should geopolitical tensions spread further in the MENA (Middle East-North Africa) region, disruptions to oil supply could not be excluded, fuelling oil-price increases beyond what is assumed in this forecast," it said.

AFP
Visitors have a close look at a Hyundai i40 displayed at the car maker's booth yesterday at Geneva motor show in Geneva. Car makers display 170 new models as the automobile industry preview the 81st edition of the show.

BoJ says yen strength not a risk

AFP, *Tokyo*

The strength of the yen is not currently a major threat to Japan's economy and has helped offset rising import costs, the governor of the Bank of Japan said in comments published Tuesday.

"At this moment, it is not working as an additional risk factor," Masaaki Shirakawa told The Wall Street Journal and Dow Jones Newswires when asked whether he felt the yen's current level was a concern.

However, he warned that the currency could rise again, particular as Middle Eastern instability fuels safe-haven demand. "Nobody knows the course of exchange rates," he said.

Japan's central bank has been closely watching the yen's value since it began to rise sharply in the middle of last year, eroding the profitability of big exporters that help drive economic growth.

Grumbles in Vietnam as power prices shoot up

AFP, *Hanoi*

Vietnam on Tuesday raised electricity prices by 15 percent as data showed inflation soared further in February, prompting complaints from some small businesses struggling to cope.

The higher electricity rates follow an 18 percent increase in petrol prices last week in the wake of a currency devaluation that pushed up the cost of imported fuel.

The Communist country is already grappling with double-digit inflation and the price hikes have stirred discontent among some Vietnamese.

"The increase in the electricity price by 15 percent is too much," said Do Thi Lan, 64, who sells tea from a makeshift stand beside the road in Hanoi.

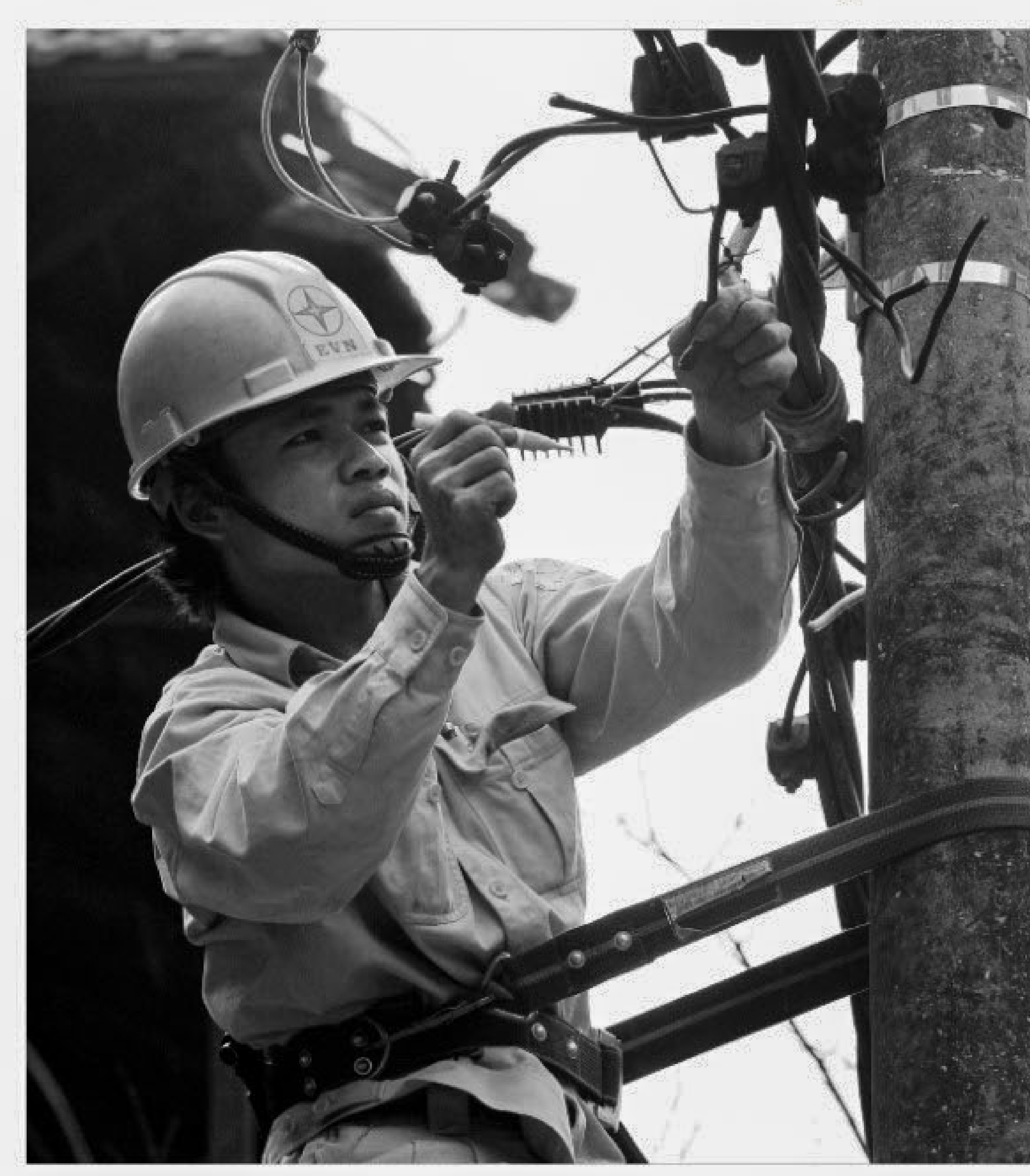
"I think now I have to cut unnecessary spending and reduce the use of electricity," she said.

Pham Minh Hai, a furniture-maker, said he might have to lay off workers because he cannot pass on the higher costs to customers.

"The petrol price has been raised. Now electricity. I don't know whether my clients would accept it if I add another 15 percent to my product prices," said Hai.

Rising consumer prices are emerging as a top concern for policymakers in Asia, particularly with oil prices shooting up on world markets. Vietnam is among the countries in the region which subsidise petrol prices.

In Vietnam inflation reached 12.31 percent year-on-year last month, according to official data, far higher than neighbouring states. It has accelerated every month since August 2010.



AFP
An electrician installs meters on a pole in Hanoi yesterday. Vietnam raised its electricity rates by 15 percent as inflation soared further in February.

An official from the Ministry of Industry and Trade, who declined to be identified, confirmed the electricity price rise had taken effect Tuesday in line with an announcement last week.

The government says the increase is needed to attract investment for new power plants to meet growing power demand.

The move is "a step in the right direction", said Matthias Duhn, executive director of the European Chamber of Commerce in Vietnam (Eurocham).

But he said a separate price which the monopoly distributor Electricity of Vietnam pays to producers is still far below neighbouring countries, giving foreign investors no incentive to enter the sector.

Eurocham has cited estimates that Vietnam needs $40 billion-$50 billion worth of investment in energy infrastructure over the next five to 10 years.

German unemployment edges lower in February

AFP, *Frankfurt*

The number of unemployed in Germany dropped sharply last month as warmer temperatures and strong order books drove job creation in Europe's biggest economy, official data showed Tuesday.

When adjusted for seasonal effects, the standard used by economists for comparisons, the number of unemployed dropped by 52,000 to 7.3 percent of the workforce, the national labour office said in a statement.

That is the lowest rate since 1991, just after east and west Germany were reunited, IHS Global Economics economist Timo Klein noted.

It was also much better than a revised decline of 18,000 in January and analyst forecasts for a drop of 15,000, as compiled by Dow Jones Newswires.

In January, the adjusted unemployment rate stood at 7.4 percent.

On an unadjusted basis, which serves as the basis for public debate, the rate eased to 7.9 percent in February from a revised 8.0 percent the previous month.

The unadjusted number of people out of work declined by 33,000 to 3.3 million, the labour office added.

"The labour market remains the show case of the German recovery," ING senior economist Carsten Brzeski said.

"The unemployment rate has been dropping for almost two years and, for more than a year, employment is growing," he added.

Economy Minister Rainer Bruederle hailed the results as well, noting that "the number of unemployed has fallen back with surprising strength."