



## Update on Indian Economy

January 2005

### Economic Snapshot

| Contents   | Item              | Units               | December  | November  | December  | (% ) Change |           |
|--|-------------------|---------------------|-----------|-----------|-----------|-------------|-----------|
|  |                   |                     | 2004      | 2004      | 2003      | [1] / [2]   | [1] / [3] |
|  |                   |                     | [1]       | [1]       | [3]       | [4]         | [5]       |
|  |                   |                     |           |           |           |             |           |
| <b>Editorial</b><br><b>Capital Market</b><br><b>Country-Malaysia</b><br><b>Other Markets</b><br><b>Important Policy</b><br><b>Pronouncements</b> | WPI -Index*       | 1993-94=100         | 189.1     | 190.3     | 176.7     | -0.63       | 7.02      |
|  | WPI -Inflation**  | Per cent            | 7.02      | 7.76      | 5.68      | -           | -         |
|  |                   | Week ended          | 4/12/04   | 6/11/04   | 6/12/03   | -           | -         |
|  | IIP (93-94=100)   | 2 months lag        | 203       | 198.9     | 176       | 2.06        | 15.34     |
|  |                   |                     | (Oct 04)  | (Sept 04) | (Oct 03)  | -           | -         |
|  | INR / US\$        | Month End           | 43.79     | 45.06     | 45.55     | -2.82       | -3.86     |
|  | M3                | Rs. '000 Cr.        | 2152.04   | 2132.68   | 1890.78   | 0.91        | 13.82     |
|  | [i] Agg. Deposits | Rs. '000 Cr.        | 1806.83   | 1784.87   | 1409.94   | 1.23        | 28.15     |
|  | [ii] Currency     | Rs. '000 Cr.        | 345.21    | 347.81    | 303.19    | -0.77       | 13.86     |
|  |                   | (Outstanding as on) | 10/12/04  | 12/11/04  | 27/12/03  | -           | -         |
|  | Call Money        | % Range             | 2.25-5.20 | 4.75-6.95 | 3.00-4.70 | -           | -         |
|  | (Lendings)        | Week ended          | 10/12/04  | 12/11/04  | 12/12/03  | -           | -         |

Source: RBI Weekly Statistical Supplement December 25, 2004 & Central Statistical Organization, Govt. of India.  
 \*All Commodities. \*\*Over the year.

### Editorial

#### A) Domestic

Dr. C. Rangarajan, Chairman of the 12th Finance Commission submitted its report to the President, Dr. A.P.J. Abdul Kalam on Friday, December 17th, 2004. The Commission has reported to have followed the “equalization principle” amongst States with the result there was a marginal tilt of grant to the backward states to maintain balance between devolution of taxes and grants. The idea is to effect corrections in the widening imbalances among States, and the recommendation is to increase the share of States in divisible tax pool to 30.5% notwithstanding the complaints from high (rich) income States that system of Center - States transfer was punishing the rich States rather than rewarding them.

Chairman indicated that milestones to be achieved by the Centre as well as the States have been indicated in the Report. In regards to taxation of services, the Chairman indicated that constitutional amendment effected last year was yet to come into force. It was indicated that service tax is currently part of the divisible pool. The Report now submitted will come into force from April 1, 2005 for a period of five years.

#### B) International

In a recent interview with IMF Managing Director, Rodrigo de Rato, it was emphasized that there was a vital need to correct global imbalances among the major players such as the United States, Europe, Japan and emerging Asia – if global growth is to be sustained. He indicated that two options are available, - one is to address the issue with a change in

policies and the other is to allow the market forces resolve the problem in due course. However leaving to the market could be costly and risky. He urged US to speed up reduction of its public deficit, and Europe to accelerate its growth potential because the growth in Europe has remained weak. As for Japan, the need is to accelerate reforms and perform in a more dynamic way. For the emerging market economies of Asia he urged them to move towards exchange rate mechanisms which reflect economic fundamentals so that the countries are able to absorb changes in the world economy and external shocks. The global imbalances could be reduced in a positive way and help the world economy if the major players adopt these policies. As far as USA is concerned, the Federal reserve increased the Federal Funds rate by 25 basis points to 2.5%. This was the fifth straight increase this year. The market reaction to this increase was limited because the dollar dipped and Treasury bond prices rose.

### **Capital Market Review**

During the month of December 2004, the sensx rose from 6234.29 on November 30, 2004 to 6,602.69 on December 31, 2004, and thus registered a hefty gain of 368.40 points. The market was lifted mainly by the blue chips and mid cap stocks especially the momentum was provided by Pharma scrips like Dr. Reddy's, Ranbaxy and Cipla.

After RBI announced that Foreign Investors can now start by buying share of Bharat Televentures because the foreign ownership limit was lower than that stipulated by RBI mark, and therefore the Foreign Institutional Investors could invest upto permissible limit after getting the board approval. It was announced that Hero Honda would invest Rs.70 crore with the result the production at the companies' two plants would increase from Rs.2.4 million units to 2.8 million units.

In the capital market the issue ownership of Reliance Industries between two brothers remained one of the key, and finally the Reliance Industries decided to buyback shares at Rs.570 per share and the buyback was limited to the 5% of the holdings of the shareholders. It was estimated that the company would spend Rs.3000 crore on the buyback and this amount is roughly 10% of its existing capital and free result put together. Despite quantum jump in the Sensx the market participants continue to remain bullish in the near future.

|                                       | Dec     | Nov     | Dec     | Nov     | (% Change) |           |           |
|---------------------------------------|---------|---------|---------|---------|------------|-----------|-----------|
|                                       | 2004    | 2004    | 2003    | 2003    | [1] / [2]  | [1] / [3] | [2] / [4] |
|                                       | [1]     | [2]     | [3]     | [4]     | [5]        | [6]       | [7]       |
| <b>Major Indices</b>                  |         |         |         |         |            |           |           |
| BSE Sensex – Close                    | 6602.69 | 6234.29 | 5791.85 | 5044.82 | 5.91       | 13.99     | 23.58     |
| Monthly High                          | 6609.78 | 6248.43 | 5920.76 | 5050.56 | 5.78       | 11.64     | 23.72     |
| Monthly Low                           | 6541.38 | 6194.61 | 5762.6  | 4991.24 | 5.59       | 13.51     | 24.11     |
| S&P CNX Nifty – Close                 | 1781.10 | 1646.45 | 1873.25 | 1615.25 | 8.18       | (4.92)    | 1.93      |
| P/E Ratio : BSE – 30                  | 16.88   | 17.31   | 18.68   | 16.28   | (2.48)     | (9.64)    | 6.33      |
| <b>FII Investments (Equity+ Debt)</b> |         |         |         |         |            |           |           |
| Inflows – Rs. Cr.                     | 25841.3 | 21302.2 | 14114.9 | 11124   | 21.31      | 83.08     | 91.49     |
| Outflows – Rs. Cr.                    | 15702.2 | 13117   | 8161    | 7530    | 19.71      | 92.41     | 74.19     |
| Net – Rs. Cr.                         | 10139.7 | 8185.3  | 5953.7  | 3594.1  | 23.88      | 70.31     | 127.74    |
| Cum Net Inv – US\$ Mn. (Month End)    | 32086.9 | 29858   | 22805.5 | 21495.4 | 7.47       | 40.69     | 38.91     |

*The scrips, which can be considered for investment in the present bullish environment are : **IPCL (Rs.180) Sail (Rs.65), Goetze (Rs.150), Morepen (Rs.10.50) and TISCO. (Rs.360).***

*(The Authors do not hold any position in the above mentioned scrips)*

## Malaysia

### **I Introduction :**

Malaysia with a population of 23 million had a chequered history because of early efforts by Indonesia to control Malaysia, Phillipines claim to Saba and Singapore succession from the Federation in 1965. It was only after 1965, the country had real independence and pursued the path of development with ethnic peace. Its natural resources are tin, platinum, copper, iron ore, natural gas and bauxite. Little more than 60% of its population is in the range of 16-54 years and a small proportion of the population (5%) is aged 65 years and above. It's a middle income country and from 1971 to late 1990 it has emerged from the producer of raw material into a multi sector economy. Its growth during this period was driven by exports especially electronics. The economy experienced recession in 2001 and 2002 when its GDP growth was estimated at 0.5% which moved up slightly in 2002. In 2003, it grew by 4.9% but the economy continues to remain vulnerable to a protracted slow down in Japan and USA which are the major destinations for its exports. Sector-wise agriculture accounts for about 8%, industry 33% and services 59% in its GDP. Inflation measured by the consumer price index is low around 1% - 2%. Its labour force is around 10.3 million. The Malaysian currency is Ringget which is pegged to the US dollar.

## II The Economy :

Malaysia has embarked upon reforming the financial and corporate sectors, developing capital markets and enhancing the business climate. In this respect, significant progress has been made in the last few years and banking soundness has been continuing to improve and implementation of the Financial Sectors Master Plan is proceeding on the course. Based on three months classification, ratio of non performing loans (NPLs) has steadily declined to 9% of the total loans. The aggregate risk-weighted capital adequacy ratio at 13% is robust. The ringgit exchange rate does not appear to be substantially misaligned, despite a sizeable depreciation during the last two years. Now Malaysia enjoys a large amount of current account surplus, a comfortable level of foreign exchange reserves, and low inflation. From agriculture the country is now embarked upon gradually diversifying its economy. Shares of Malaysian export to Europe, Japan and the U.S. is relatively stable. However, the share of its exports to the rest of Asia is gradually rising.

The financial system is well capitalized and the exposure of finance companies through their link with banking system has been gradually reduced. There is a need for further consolidation so as to increase efficiency and resilience of the banking system. Further, elimination of remaining restrictions on operations of foreign banks would also help to increase competition in the financial sector. The country is trying to boost competitiveness so as to sustain high growth in the near to medium term.

### Malaysia : Important Macro-economic Statistics

|            | 2000   | 2001  | 2002 | 2003 | 2004 |       |
|------------|--|-------|------|------|------|-------|
| <b>I</b>   | <b>Real sector (percent change)</b>                      |       |      |      |      |       |
|            | - Real GDP growth  | 8.6   | 0.3  | 4.1  | 4.5  | 5.3   |
|            | - Real domestic demand                                   | 16.3  | 0.0  | 7.0  | 3.3  | 5.1   |
|            | - Inflation rate CPI (period average)                    | 1.5   | 1.4  | 1.8  | 1.1  | 2.2   |
| <b>II</b>  | <b>Saving and investment (percent of GDP)</b>            |       |      |      |      |       |
|            | - Gross domestic investment                              | 27.2  | 24.0 | 24.5 | 23.0 | 22.7  |
|            | - Gross national saving                                  | 36.6  | 32.2 | 32.0 | 33.6 | 32.6  |
| <b>III</b> | <b>Balance of payments (in billions of U.S. dollars)</b> |       |      |      |      |       |
|            | - Exports, f.o.b.  | 98.4  | 88.0 | 93.4 | 98.4 | 105.9 |
|            | - Imports, f.o.b.  | 77.6  | 69.6 | 75.2 | 75.2 | 81.8  |
|            | - Trade balance  | 20.8  | 18.4 | 18.1 | 23.2 | 24.1  |
|            | - Services account                                       | -10.4 | -8.9 | -8.2 | -9.9 | -10.1 |
|            | - Current account balance (CAB)                          | 8.5   | 7.3  | 7.2  | 10.7 | 10.7  |
|            | - (CAB as percent of GDP)                                | 9.4   | 8.3  | 7.6  | 10.6 | 9.9   |

### III India – Malaysia : Trade Relation

In May 2001, the then Prime Minister, Mr. Atal Bihari Vajpayee, visited Malaysia with the large delegation, the strategy being “Look East”. Now the Malaysian Prime Minister came to India in December 2004, with equally large delegation “to build new bridges, construct, new economic alliances and generate fresh economic cooperation”, and the strategy is towards India and West Asia. There is therefore convergence of views between the two countries which can yield large benefits to both. In 2001, the Indian-Malaysian bilateral trade was US\$ 2.5 billion, and now the Malaysian Prime Minister has visualized the Indian-Malaysian bilateral trade at US\$ 4.5 billion.

India’s import from Malaysia, is mainly palm oil used in cooking while Indian export to Malaysia amounted to less than 1 per cent of Malaysia’s overall import bill. Earlier, Indian-Malaysian trade has been dominated by agricultural products and trade relations have run into sporadic disputes over tariff barriers and protectionist campaigns by local farm lobbies. He mentioned that India’s entrepreneurs have already invested about a billion dollar in Malaysia but given the vastness of the opportunities this is very little.

During the visit of Mr. Abdullah Ahmad Badawi 12 MoUs were signed in areas ranging from railways to biotechnology, though two agreements of note were on cooperation in space (pooling of satellite capacities) and the construction of a new international airport at Hyderabad. Malaysian Prime Minister has sought Indian investment and technical expertise in the field of information technology, manufacturing, biotech, engineering and pharmaceuticals.

### Other Markets

#### Debt Market

| Name of the Issuer                                 | Rate%                             | Duration           | Amount<br>Rs. Crore | Type of instrument                        |
|--|-----------------------------------|--------------------|---------------------|---|
| Housing Development Finance Corporation            | 5.89 to 55 bps above NSE Mibor    | 6 months to 3 year | 1450                | Combination of CP and floating rate bonds |
| National Housing Bank (NHB)                        | 5.65% to 10 bps above 1 year gilt | 6 months to 4 year | 550                 | Combination of CP and floating rate bonds |
| ILFS   | 5.89                              | 6 months           | 25                  | CP  |
| Cholamandalam Investments and Finance Company Ltd. | 5.7 to 10 bps above NSE Mibor     | 89 days            | 35                  | Short term bonds                          |
| Bajaj Auto Finance Ltd.                            | 6.12                              | 1 year             | 20                  | CP  |
| Finolex Industries                                 | 100 bps below 1 year gilt         | 5 year             | 75                  | Privately placed bonds                    |
| HCC Ltd.   | 5.58                              | 90 days            | 10                  | CP  |
| L&T Finance  | 6.1                               | 89 days            | 10                  | Short term bonds                          |
| United Phosphorous Ltd                             | 5.77                              | 90 days            | 10                  | CP  |
| Apollo Tyre Ltd.                                   | 5.7                               | 90 days            | 10                  | CP  |
|  |                                   | <b>TOTAL</b>       | <b>2230</b>         |   |

## **CP - Commercial Paper**

The month of November 2004 saw hectic activity in the issue of debt; the amount raised through debt instruments of commercial paper and bonds aggregated to Rs.2230 crore. The largest amount raised was by HDFC and National Housing Bank which together raised Rs.2000 crore.

## **Call Money Market**

The call money market rate on December 17, 2004 in respect of borrowings ranged between 3.50% and 6.15% as compared to 3.00% and 4.97% on December 19, 2003 i.e. a year ago. A month ago, the rates were 4.75% - 6.55% on November 19, 2004 reflecting that there were variations in the rate pointing towards relative stability during the month. The average daily turnover in the call money market was Rs.9,564 crore for the week ending December 17, 2004, and this daily turnover declined to Rs.8,868 crore in the week ending December 24, 2004.

## **Foreign Exchange Market**

The exchange rate (RBI reference rate) on December 24, 2004 was Rs.43.81 per US dollar as compared to Rs.45.58 per US dollar on December 26, 2003. This reflected a nominal appreciation of the rupee vis-a-vis US dollar. Further the six month forward premia was 1.64% on December 24, 2004 as compared to 0.18% on December 26, 2003 (a year ago), and this reflects a rising demand for dollar in the forthcoming months. The foreign currency asset were US \$ 125.0 billion on December 24, 2004, and inclusive of gold and SDRs and the reserve position in the Fund, the foreign exchange reserves aggregated to US\$ 131.0 billion. From end-March 2004, the foreign exchange reserves registered an increase of US\$ 18.7 billion. The market rate (buying) was Rs.43.43 per US dollar on December 31, 2004.

## **Important Policy Pronouncements – Tsunami Disaster**

On December 26, 2004 two undersea earthquakes occurred within hours of each other with epicenter south of Sumatra island in Indonesia. These caused huge volume of displaced water where tides rose as high as 40 meters, and these traveled around the epicentre at a terrific speed, and thereby causing huge volume of displaced water at shores as far as 2000 km away. Though estimates are still being worked out, the disaster resulted in more than 100,000 people dead in South Asia including about 10,000 in India. The worst affected in India were coastal areas of Tamil Nadu, Andhra Pradesh and Orissa. Sri Lankan economy is the hardest hit and Thailand important tourism industry which recently started recovering after suffering set backs from SARS disease, and political unrest was severely affected. The strongest earthquake in the seas called 'Tsunami' virtually led to the siege of Indian Ocean. The loss to the human life is tremendous, and so far as India is concerned the Prime Minister immediately announced an aid of Rs.500 crore, and promised Rs.1 lakh relief to every family for each life lost.

In addition, the Reserve Bank of India issued instructions and requested the banks to immediately initiate a package of measures in the calamity affected areas for agriculturists, small-scale industrial units, artisans, small businesses and trading establishments affected by this natural calamity immediately after the district or State authorities declare the area as calamity affected one. Further, banks have also been asked to convert, reschedule and restructure existing loans in the case of crop failure due to 'Tsunami' tragedy.

Internationally, countries like Sri Lanka has appealed for aid. An international agency like IMF indicated that it is ready to help in any way, it could. However the overall perception is that the financial markets would not be affected much because South East Asian bourses are dominated by property firms, banks, and export oriented manufacturing units, the effect of which will only be moderate.

**TABLES & GRAPHS ARE ENCLOSED IN A SEPARATE EXCEL SHEET**

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