

US Tapering: Least Impact on Indian Economy

A Study of Indian Policy Tackling Global Threats

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The economy of India is the tenth-largest in the world by nominal GDP and the third-largest by purchasing power parity (PPP). The country is one of the G-20 major economies and a member of BRICS. On a per-capita-income basis, India ranked 141st by nominal GDP and 130th by GDP (PPP) in 2012, according to the IMF. India is the 19th-largest exporter and the 10th-largest importer in the world. The economy slowed to around 5.0% for the 2012–13 fiscal year compared with 6.2% in the previous fiscal. According to Moody's, the Economic Growth Rate of India would be 5.5% in 2014–15. On 28 August 2013, the Indian rupee hit an all time low of 68.80 against the US dollar. In order to control the fall in rupee, the government introduced capital controls on outward investment by both corporates and individuals. India's GDP grew by 9.3% in 2010–11; thus, the growth rate has nearly halved in just three years. GDP growth rose marginally to 4.8% during the quarter through March 2013, from about 4.7% in the previous quarter. The government has forecast a growth rate of 6.1%–6.7% for the year 2013–14, whilst the RBI expects the same to be at 5.7%. Besides this, India suffered a very high fiscal deficit of US\$ 88 billion (4.8% of GDP) in the year 2012–13. The Indian Government aims to cut the fiscal deficit to US\$ 70 billion or 3.7% of GDP by 2013–14.

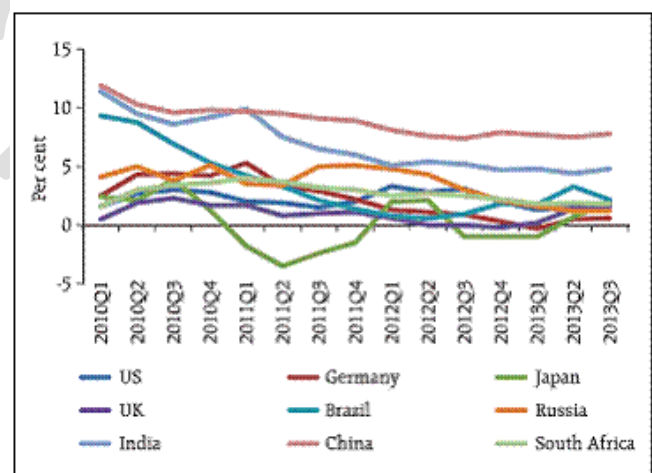
Indian economy has recently faced a lot of threats from the world, but it has successfully faced all these problems with its efficient policy decisions. We have studied about the Indian economy in this study and had our observations as follows:

Initial reaction to the tapering announcement has been positive. Growth differential between developed economies (DEs) and emerging & developing economies (EDEs) has been narrowing, while the inflation differential has been widening. Thereby, resulting risk-return dynamics seem to be in favor DEs, thereby increasing the vulnerability of the EDEs.

While monetary policy is largely guided by the growth-inflation dynamics, it is also tempered by considerations of risks of external imbalances. Policy initiatives were taken in mid-July to address exchange rate volatility so that it does not risk macroeconomic stability and growth sustainability.

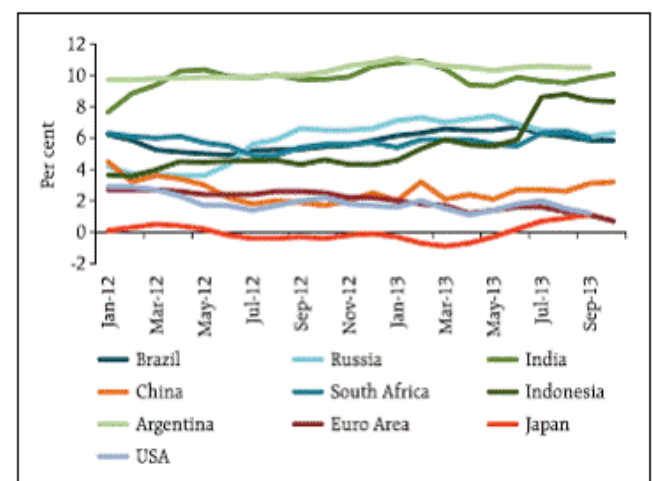
India utilized the delay in tapering to bring about adjustment in the current account deficit (CAD) and built buffers by replenishing its foreign exchange reserves. Consequently, external sector risks have been considerably reduced and the effect of the tapering on the economy is expected to be limited and short lived. However, macroeconomic adjustment is quite incomplete, with persistence of high inflation irrespective of growth slowdown. Fall in domestic savings rate and high fiscal deficit continue to pose challenges for Indian economy.

Chart 1.1: GDP Growth



Source: Bloomberg

Chart 1.2: CPI Inflation



Source: Bloomberg

The Indian economy staged a small recovery in the second quarter of the current fiscal year with growth at 4.8 per cent, an improvement over the previous quarter's 4.4 per cent with improvement in growth spread across sectors. On the external front, the CAD moderated sharply to 1.2 per cent of GDP during Q2 2013-14 due to a decline in the trade deficit.

Boom period expansions that led to excess capacities and structural impediments continue to weigh on corporate performance. Asset composition of corporate balance-sheets shows a shift towards increased financial investments.

Foreign Institutional Investors (FIIs) continue to remain significant players in the domestic equity markets, despite some fall in their ownership of index stocks after June 2013. As such, entities with equity market exposure need to brace for any future volatilities which might result from perceived changes in relative returns across markets.

All the market are facing a decline, despite a slow and Minimal decline is observed in case Indian markets as compared to other Global and Asian economies after this round of tapering. It depict outs the success of Indian economic policy to cope out the global threats including the renowned Fed Tapering.

Some **other facts** revealed in this study are as follows:

Developments in the external sector since the third week of May 2013 brought to fore not just stress in the financial markets and asset prices, but also their impact on other macroeconomic parameters, including growth, public finances and inflation, as also financial stability. The buffers built and the fresh responses during the stress period have helped India to contend with a precipitous situation.

However, global financial conditions remain stressed and domestic policy changes have not sufficiently improved business conditions. Growth continues to be slack, while inflation concerns, especially in the form of high consumer price inflation linger. Consequently, policy choices will need to be carefully evaluated and would need to preserve stable macroeconomic and financial conditions while addressing the growth concerns. In this context, structural reforms become important to reduce CAD to sustainable levels and to support growth.

In the actual execution of the tapering decision for the first time it had an initial adverse impact on the markets except the UK economy. Later on, all the economies has shown recovery, with Indian economy being registering the higher growth. Hong Kong, Malaysian, Japanese and Chinese economies registered a low steeper and/or declining growth altogether.

All the economies except London have shown a rising uptrend, showing their financial rigidness and policy effectiveness. Markets have shown its well response to the shift and have grown well positively thereby, except the case of US, Canada and Korea.

Apart, china has even well performed during this period, with an overall increasing trend nullifying the effect of tapering, depicting its superiority on the globe. Economies like Malaysia and Korea started recovering earlier than rest, whereas Japan and London are at their most facing heats of it, starting the most belated recovery from the decline.

TABULAR ANALYSIS OF GLOBAL MARKET PRICES

The ratio of change (in %) in respective months in comparison to the last month prices is as follows:

| Country | Stock Exchange | Indices (Closing Prices ->) | Sep 2012 | Oct 2012 | Nov 2012 | Dec 2012 | Jan 2013 | Feb 2013 |
|-----------|----------------|------------------------------------|----------|----------|----------|----------|----------|----------|
| INDIA | BSE | S&P BSE SENSEX | 7.64896 | -1.37165 | 4.509607 | 0.448865 | 2.410444 | -5.19448 |
| | NSE | CNX NIFTY | 8.458686 | -1.46582 | 4.629251 | 0.429433 | 2.19556 | -5.66221 |
| | | CNX NIFTY Junior | 2.512852 | 7.198105 | 1.613885 | 7.312701 | 2.869036 | -3.9098 |
| | | CNX Finance | 3.217405 | 5.659073 | 1.380213 | 7.044565 | 1.119702 | -3.40749 |
| USA | NYSE | Dow Jones Industrial Average Index | 2.645285 | -2.53529 | -0.54121 | 0.603121 | 5.772527 | 1.399004 |
| | NASDAQ | NASDAQ Composite Index | 1.606477 | -4.46052 | 1.108749 | 0.307949 | 4.060924 | 0.574769 |
| UK | LSE LONDON | FTSE 100 | 0.535761 | 0.707058 | 1.454338 | 0.528397 | 6.427821 | 1.336647 |
| HONG KONG | HKSM | HANG SENG | 6.969358 | 3.845611 | 1.795459 | 2.843935 | 4.734139 | -2.98893 |
| MALAYSIA | KLSE | KLSE Composite Index | -0.57408 | 2.224653 | -3.72011 | 4.849674 | -3.63539 | 0.619336 |
| KOREA | KSE | KOSPI Composite Index | 4.781326 | -4.21549 | 1.089924 | 3.318847 | -1.75809 | 3.290111 |
| JAPAN | TSE TOKYO | Nikkei 225 | 0.342198 | 0.655343 | 5.798647 | 10.04837 | 7.152161 | 3.776935 |
| CANADA | TORONTO | S&P TSX Composite Index | 3.081352 | 0.855693 | -1.47711 | 1.585862 | 2.02437 | 1.076845 |
| CHINA | SHANGHAI | SSE Composite Index | 1.887649 | -0.82879 | -4.29024 | 14.59558 | 5.124872 | -0.8313 |

NOTE FROM THE AUTHOR

In this paper, it is tried to make the information and analysis the best summative and confirmatory. Still, it is well accepted that there may be an unintentional error / mistake while interpreting the analysis and quoting the referencing.

For any such or other mistakes held in thereby, I apologize to the concerned party in advance. I humbly invite you to send your valuable suggestions / feedback for improvements at my e-mail id 'rajputlakshya@yahoo.com'. for any clarifications, please write on the same.

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