

INDIA

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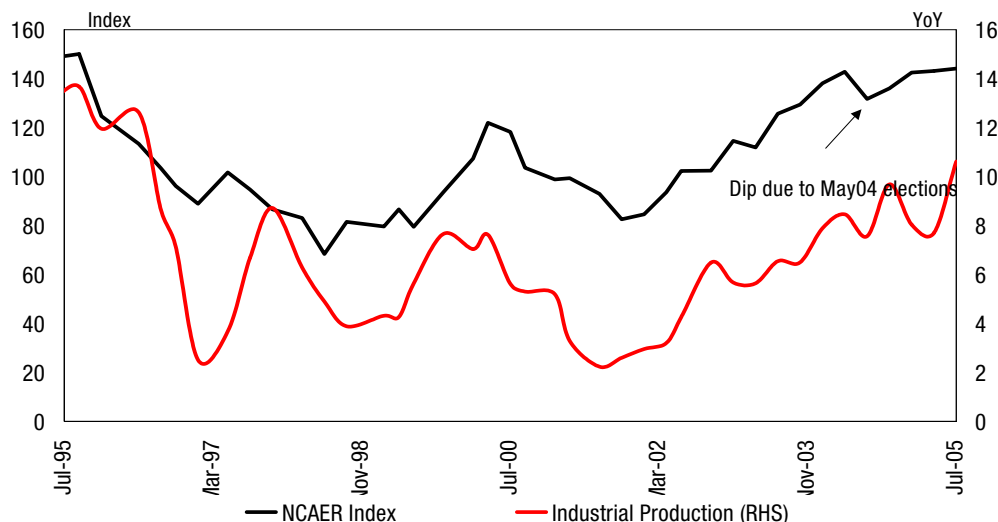
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India Economics

Business Confidence Touches a 10-year High But its Components Indicates Some Caution

- **BCI rises 0.7% QoQ:** The National Council of Applied Economic Research (NCAER) business confidence index (BCI)¹ touched a 10-year high for the quarter ending July 2005. The overall rise in the index reflects the buoyancy in the industrial sector, strong corporate earnings and relatively benign macro variables
- **BCI Components Reveal Caution:** An analysis of the components of the BCI indicates a QoQ contraction in overall economic conditions (-1.9%) and investment climate (-0.5%). This reflects uncertainties arising on account of the impact of higher oil prices, higher global rates and the impact of further dollar weakness. Expectations on the other two components remain positive — financial position of firms (4.2%) and capacity utilization (1.1%).
- **Sectoral trends Encouraging:** As compared to the earlier survey ended April 05 which saw a contraction in consumer goods (both durables and non-durables) as well as capital goods, the survey ended July registered positive growth across all sectors except intermediate goods.
- **We remain positive on the economy:** Despite concerns on oil, currency and rates, we maintain our view that due to the structural changes in the economy over the last few years, the Indian economy is resilient to these external challenges. With growth drivers intact, we maintain our FY06 GDP estimate of 7.5%, led by 8% growth in industry, 9% in services and 3% in agriculture

Trends in Business Confidence and Industrial Production



Source: NCAER, CSO

¹ The NCAER constructs its BCI (May 1994=100) on corporation's perceptions of four key indicators (1) the investment climate (2) future economic conditions (3) financial position of firms and (4) capacity utilization.

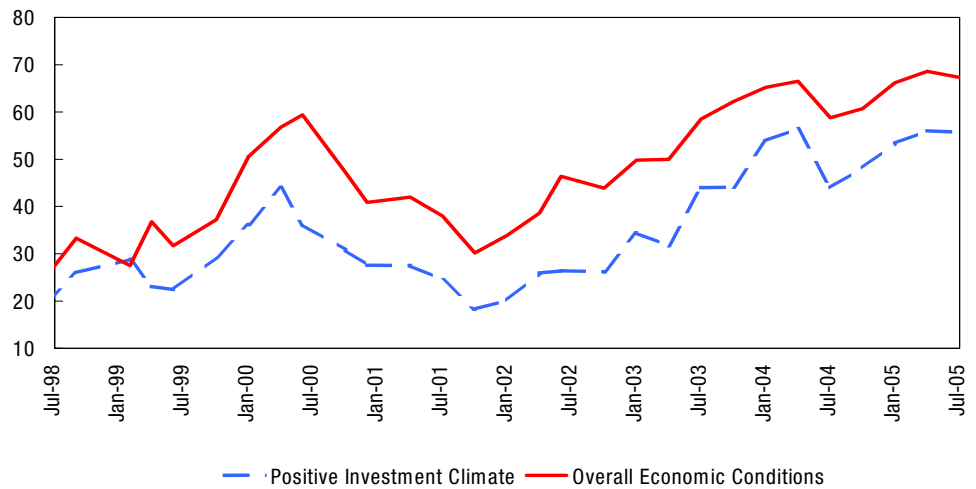
Business Confidence By Components

Examining the components of the BCI reveals that the current global environment has acted as a drag on economic sentiment in the country. The impact of higher oil prices, geopolitical tensions, and higher expected interest rates have created uncertainties on future economic conditions and the investment climate which registered a QoQ contraction of 2% and 0.5% in the survey ended July. However on a YoY basis, they were up 14.5% and 27% respectively. This sharp YoY increase is attributed to the dip last July following the elections. The other two components - expectations on financial performance as well as capacity utilization remain positive. This is indicative of rising demand levels and supports our view of the investment cycle upturn.

Expectations on trends in Economic Conditions and the Investment Climate – Forward Looking Criteria

Expectations on Economic Conditions contracted by 2% QoQ, but on a YoY basis, were up 14.5%

Expectations on Investment Climate were also down 0.5% QoQ, but up 27% YoY

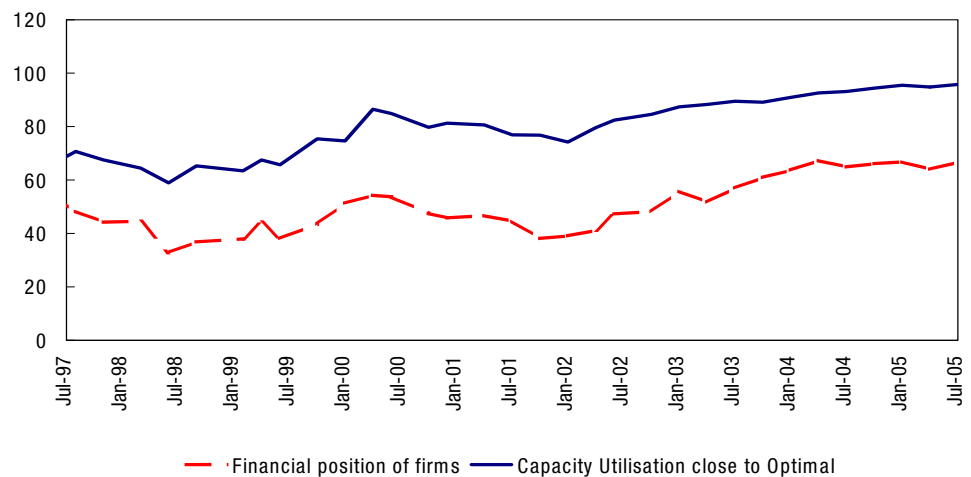


Source: NCAER.

Expectations on Indicators of Firms' Financial Positions and Capacity Utilization – The Current Criteria

Expectations on financial positions of firms were up 4.2% on a QoQ basis, and 2.8% on a YoY basis

Expectations on capacity utilization were up 1.1% QoQ, and nearly 3% YoY.

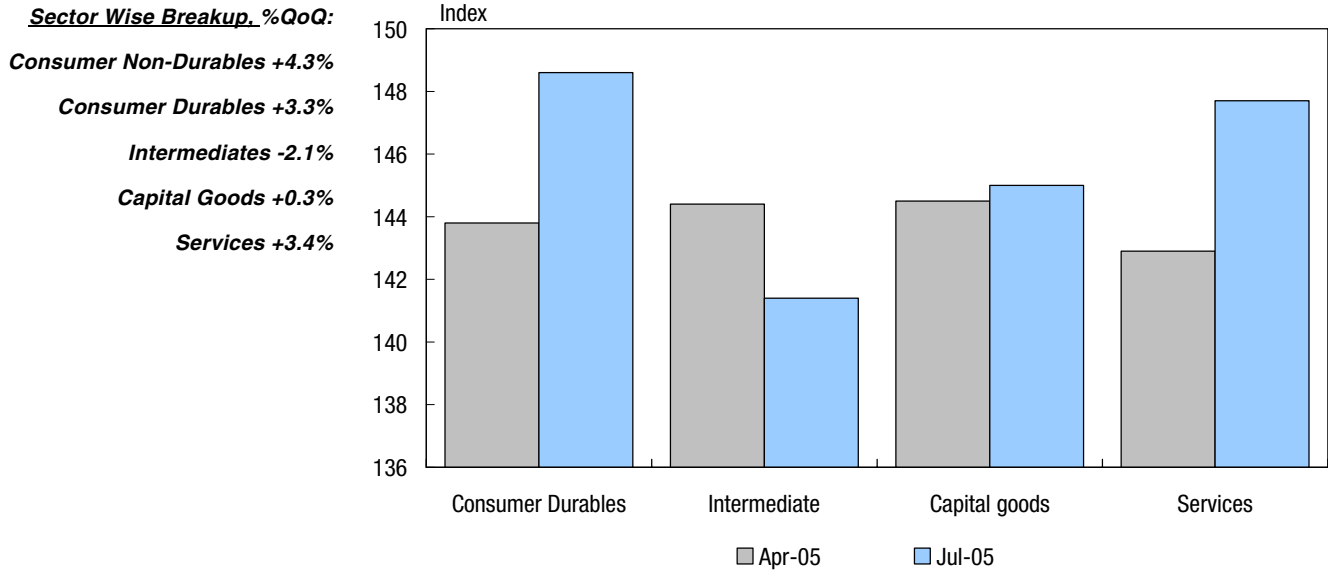


Source: NCAER

Business Confidence by Sectors

A sector-wise breakup of the BCI suggests a positive picture, with all sectors apart from Intermediate Goods reflecting an increase on a QoQ basis.

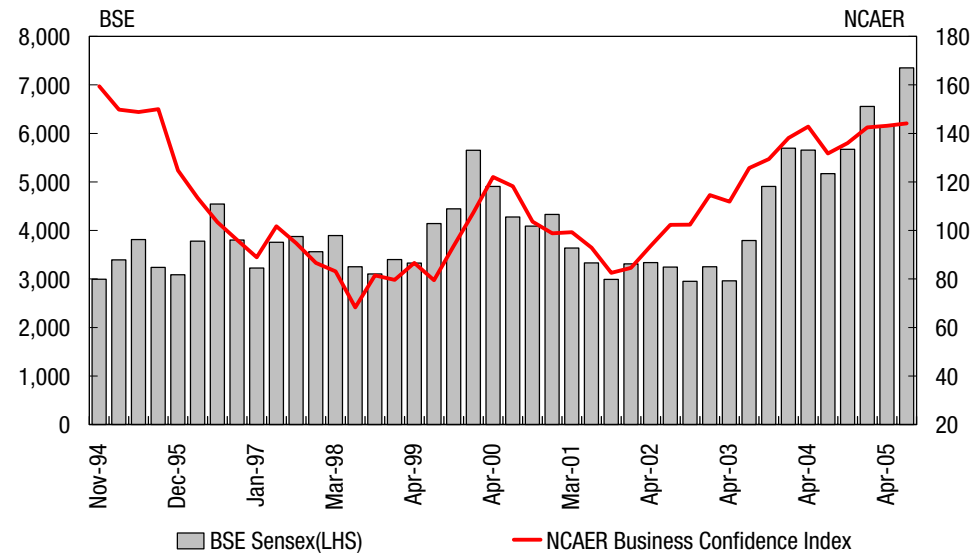
Business Confidence Index- Sector-Wise Breakup



Source: NCAER

Trends in the Business Confidence Index and the Bombay Stock Exchange (BSE) Sensex

Overall trends in the BCI and the Stock Exchange show a strong correlation, with improvements in the BCI reflected in the BSE Sensex after a short lag



Source: BSE, NCAER

Disclosure Appendix

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