

# Oh, CNY? Storm in a *chai* cup ...II

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## Bottom line: Growth, not CNY, drives India-China trade

- Does a stronger CNY, clients ask, impact India? Not really, we reply. The India-China trade deficit – US\$20.8bn in 2010 – largely runs on India's and China's growth rather than CNY/INR, in our view. Anyway, our fx strategists see limited appreciation ahead, with the USD-CNY forecast to end 2011 at 6.30 and 2012 by 6.20. Second, the CNY, in fact, has appreciated just 3.8% *vis a vis* the INR since the PBoC began revaluing in mid-2010, with both currencies appreciating against the US Dollar. Third, CNY's appreciation *vis a vis* the INR, since July 2005, has been broadly in line with that of some other key currencies. Finally, the INR is likely the least sensitive to the CNY among all Asian currencies. For details, do read our previous report, Oh, CNY? Storm in a *chai* cup, *India Economics*, May 6, 2010.

*Chai*: Indian tea, planted 1820s, by the British, to end Chinese monopoly.

## Why it matters: Chinese rebalancing impacts relatively little

- We continue to believe that India's and China's industrial growth – rather than CNY revaluation or rebalancing – will drive India-China trade. To begin with, Ting Lu, our China economist, expects the pace of reduction of the current account surplus itself to moderate to 3.5% of GDP in 2012 and 4% in 2011 from 5.2% in 2009-10 and 9.1% in 2008. Second, India-China trade should also be relatively less impacted by rebalancing, because it is dominated by industrial commodities and engineering goods. Third, in any case, India is a bit player in China's trade, accounting for 2.6% of exports and 1.5% of imports in 2010. In 2009, India accounted for just 2.9% of the reduction in the Chinese current account surplus. Finally, Indian and Chinese product price differentials are too substantial to be eroded by 5-10% CNY-INR movements.

## Key points: Trade deficit wider despite stronger CNY

- We have always argued that growth – rather than CNY – drives India-China trade. Not surprisingly, the India-China trade deficit has widened to US\$20.8bn in CY2010 (1.2% of GDP) from US\$1.5bn (0.2% of GDP) in FY05, despite the 25.7% appreciation in the CNY *vis a vis* the INR (Chart 1).
- Chinese iron ore and copper demand, which accounts for 50-60% of India's exports to China, for example, should be far more sensitive to investment.
- Key segments of India's imports from China – such as machinery and chemicals – are also essentially driven by industrial growth.
- CNY's appreciation *vis a vis* the INR, since July 2005, has been broadly in line with that of some other key currencies (Chart 2).

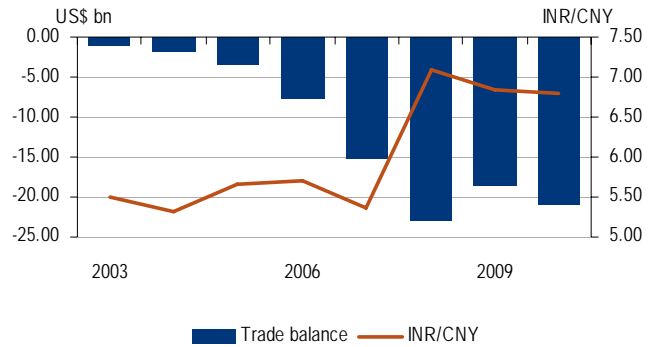
## Next up in India: Good rainfall

- India: Rainfall data (August 17), Wednesday, 17 August 2011.

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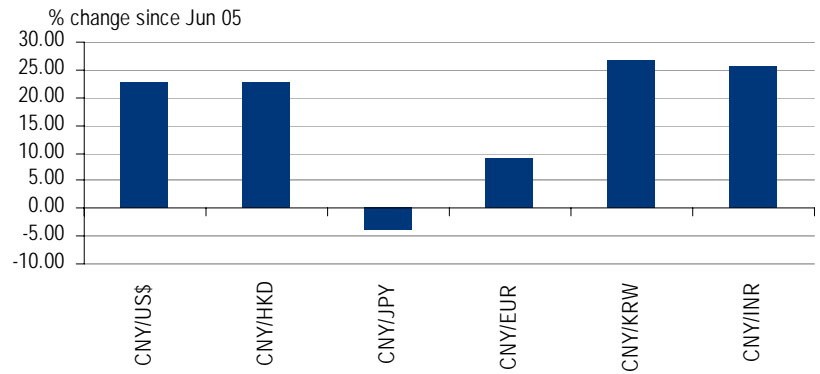
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**Chart 1: India -China trade deficit swings on growth, not CNY**



Source: CEIC, BofA Merrill Lynch Global Research estimates.

**Chart 2: CNY appreciation vs. INR in line with other key currencies**



Source: CEIC, x-rates.com, BofA Merrill Lynch Global Research estimates.



16 August 2011

**Table 1: India story in numbers**

INDIA	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13
Summary Data										
Nominal GDP (US\$ bn)	599.5	721.6	834.0	948.1	1,239.1	1,215.8	1,381.4	1,727.6	2,055.3	2,317.1
GDP per capita (US\$)	568	663	759	846	1,084	1,052	1,124	1,458	1,712	1,905
Population (millions)	1,072	1,089	1,106	1,122	1,138	1,154	1,170	1,185	1,201	1,216
Economic Activity										
Real GDP growth (% yoy)	8.5	7.5	9.5	9.6	9.3	6.8	8.0	8.5	7.6	8.0
Agriculture (% YoY)	10.0	0.1	5.1	4.2	5.8	-0.1	0.4	6.6	2.0	3.0
Industry (% YoY)	6.0	8.4	8.5	12.9	9.2	4.0	8.3	7.8	6.4	6.9
Services (% YoY)	8.8	10.2	11.2	10.1	10.4	9.5	9.7	9.2	9.1	9.4
Domestic demand growth (% yoy)	7.4	8.5	10.5	9.7	11.1	6.2	8.3	7.6	7.2	8.1
Real investment growth (% yoy)	13.6	18.9	15.3	14.3	15.2	2.7	7.3	8.4	9.1	8.0
Real consumption growth (% yoy)	5.4	4.9	8.5	7.7	9.2	7.9	8.7	7.3	6.3	8.1
Real private consumption growth (% yoy)	5.9	5.2	8.4	8.5	9.1	7.4	7.3	8.2	7.0	7.7
Real government consumption growth (% yoy)	2.6	3.6	8.9	3.7	9.5	10.7	16.4	2.6	2.9	10.6
Real export growth (% yoy)	9.6	27.2	25.9	21.8	5.2	13.4	-5.5	12.0	5.4	8.0
Real import growth (% yoy)	13.8	22.2	32.5	22.0	10.0	22.2	-1.8	6.3	8.0	8.0
Prices										
WPI inflation (% yoy, eop)	4.8	5.3	3.9	6.8	7.7	1.5	10.2	9.8	6.7	6.0
WPI inflation (% yoy, avg)	5.5	6.5	4.4	6.5	4.8	8.1	3.6	9.6	8.5	6.0
USD - INR (eop)	43.4	43.8	44.6	43.6	40.0	50.9	45.1	44.7	44.0	45.0
USD - INR (avg)	46.0	44.9	44.3	45.3	40.2	45.9	47.4	45.6	44.5	45.0
REER (% yoy, + dep)	3.2	-0.8	3.1	-1.8	7.1	-9.9	-3.1	7.7		
Monetary Sector										
Reserve money (% yoy)	18.3	12.1	16.9	23.9	31.0	6.4	17.0	17.2	16.8	17.1
M3 growth (% yoy)	16.7	12.0	21.1	21.7	21.4	19.3	16.8	16.0	16.8	17.1
Non -food credit (% yoy)	18.40	28.99	28.46	27.32	22.60	17.50	16.90	21.30	18.80	20.00
RBI policy rate - Reverses repo (%)	4.5	4.75	5.5	6	6	3.5	3.5	5.75	7.25	6.50
Repo rate	6	6	6.5	7.5	7.75	5	5	6.75	8.25	7.5
CRR	4.5	5	5	6	7.5	5	5.75	6	6	6
1-month interbank rate -Call rate (%)	4.62	4.65	5.60	7.22	6.07	7.06	3.24	5.25	6.00	6.50
Long-term yield (%)	5.2	6.7	7.5	8.0	8.0	7.0	7.8	8.0	8.0	8.0
PLR	10.25	10.25	10.25	12.25	12.25	12.25	11.75	13	14.75	14.25
External Sector										
Current Account balance (% of GDP)	2.3	-0.3	-1.2	-1.0	-1.3	-2.4	-2.8	-2.6	-2.7	-3.0
Current Account balance (US\$ bn)	14.1	-2.5	-9.9	-9.6	-15.7	-28.7	-38.4	-44.1	-55.0	-69.5
Trade Balance (US\$ bn)	-14.3	-28.0	-46.1	-59.3	-88.5	-118.4	-118.4	-130.4	-145.0	-169.5
Exports, f.o.b. (US\$ bn)	63.8	83.5	103.1	126.4	162.9	185.3	182.2	250.5	276.0	310.5
Imports, c.i.f. (US\$ bn)	78.1	111.5	149.2	185.7	251.4	303.7	300.6	380.9	421.0	480.0
Invisibles (US\$ bn)	27.80	31.23	42.00	52.22	75.73	89.92	79.99	86.2	90.0	100.0
Foreign direct investment (US\$ bn)	2.4	3.7	3.0	7.7	15.9	17.5	18.8	7.0	18.0	20.0
International reserves (US\$ bn)	113.0	141.5	151.6	199.2	309.8	251.9	279.0	303.5	320.5	337.0

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**Table 1: India story in numbers**

<b>INDIA</b>										
Public Sector										
Consolidated Fiscal deficit (% of GDP)	-8.4	-7.4	-6.7	-5.7	-4.5	-10.0	-9.6	-7.6	-8.3	-8.3
Central Gov. Budget Deficit (% of GDP)	-4.5	-3.9	-4.0	-3.9	-2.9	-7.4	-6.3	-5.1	-5.8	-5.8
<b>Central Gov. Revenues (% of GDP)</b>	9.6	9.5	9.4	10.1	10.9	9.7	8.8	10.0	8.2	8.3
Debt Indicators										
Gross External Debt (% of GDP)	18.8	18.6	16.7	18.2	18.1	18.5	19.0	17.7	16.6	16.0
<b>Gross Government Debt (% of GDP)</b>	81.1	78.6	77.4	74.1	71.4	71.5	68.8	62.6	59.9	60.0
Savings - Investment Balance										
Savings (nominal - % of GDP)	28.2	32.4	33.5	34.6	36.9	32.2	33.7	33.7	33.7	33.7
Investment (real - % of GDP)	26.7	31.3	33.2	34.5	36.7	34.9	34.7	34.7	35.2	35.2

Source: Government of India, BofA Merrill Lynch Global Research estimates.

## Link to Definitions

### Macro

Click [here](#) for definitions of commonly used terms.

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