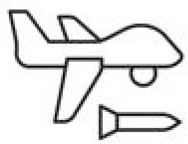
Inflexion point

Escalation of West Asia conflict could hurt India



On Saturday, External Affairs Minister S Jaishankar expressed valid apprehensions over the "widening" of the conflict in West Asia and how the 'Houthis firing in the Red Sea... is actually costing us'. The converse also perhaps holds true — that if the conflict remains confined to one between Israel and Iran-supported non-state actors such as Hezbollah, Houthis and Hamas, as has been the case for a year, its economic fallout on India may not be too damaging, even as the human costs of the war itself have been alarming.

But if the conflagration turns into a war between Iran and Israel, commodity and financial markets could turn volatile — especially if Iran's oil and nuclear facilities are impacted. A war could involve hitherto neutral players in the Gulf Cooperation Council, if not China and Russia. There are indications that India's exports have been dented, but perhaps not too seriously, by the disruptions of the last one year. Shipping costs rose as vessels went around the Cape of Good Hope to get to Europe and the US, instead of the Suez Canal, to escape the threat of Houthi attacks. This 15-20 per cent cost increase hurts India's low margin, high volume exports. The Houthis are estimated to have made about 130 strikes over the last year, as a result of which average global daily transits through the Suez Canal have dropped from 80 last October to less than 30, according to an IMF database. Meanwhile, a dip in global demand for petroleum amidst a bearish oil market seems to have impacted India's refiners.

Petroleum has dragged down India's overall export growth. In August this year, petroleum exports fell 37 per cent to $5.95 billion, against $9.54 billion last year. Exports excluding petroleum and gems and jewellery were up 2.3 per cent to $26.8 billion. This trend applies to the current fiscal; overall merchandise exports for April-August rose just 1.14 per cent to $179 billion, but exports excluding petroleum and gems and jewellery were up by 4.6 per cent to about $136 billion. According to an analysis by Global Trade Research Initiative, India's exports to countries in the theatre of the conflict such as Israel, Jordan and Lebanon have dropped sharply this calendar year (till July), but increased by 18 per cent to the GCC countries, which have so far stayed out of the conflict. Interestingly, India's exports to Iran were up 15.2 per cent over this period. EU exports were up 6.8 per cent. An escalation of the conflict could flatten these distinctions.

A flare-up will rock movement of freight, and financial and commodity markets. As reported by this newspaper, India's benchmark equity indices fell 4 per cent last week, with a net outflow of $3.19 billion in equities as foreign portfolio investors withdrew. While there is no cause for alarm given India's forex and strategic oil reserves, the prospect of a rate cut decision this week might have receded just a bit in a situation where safe-haven investment seems to be picking up. India needs to be circumspect, while holding the course.