

India will rise above terror attack

Carnage of Nov 26-29 will have moderate, short-lived impact as the country's fundamental attributes still remain

By AMITENDU PALIT

THE Mumbai terrorist carnage of Nov 26-29 have given rise to many new worries. Foremost among these are apprehensions over the repercussions of the attack on India's economic outlook. Terrorism is not new to India. Mumbai, in particular, has suffered most from terrorist violence. Since March 1993, when a series of blasts ripped the city, Mumbai has experienced terror attacks on several occasions. The latest, however, was unprecedented in terms of loss of human lives and material resources. The attack also occurred at a time when India is trying to cope with the adverse fallout of the global financial crisis.

Concerns have been expressed at two levels. The first is on Mumbai. It is not just another city. It has been one of the largest centres for trade and finance in Asia for centuries. It figures among the top 10 global financial hubs. The city accounts for the bulk of India's sea trade and financial transactions. It also houses the central bank, two national stock exchanges (the Bombay Stock Exchange and the National Stock Exchange), the Securities and Exchange Board of India, one of India's largest mints and the multi-commodity exchange. Most of India's banks and financial institutions have their headquarters in Mumbai. So do multinational corporations as well as leading domestic firms like Reliance and Tata.

South Mumbai was the focal point of the attack. This is where most major financial institutions and corporate offices are located. The intention was clearly to inflict as much damage as possible, albeit in a partially indirect manner, to the financial "core" of Mumbai. The Taj Mahal Palace Hotel and Oberoi Trident Hotel – two of Mumbai's best known hotels seized by terrorists – have had large business visitors.

Indeed, the dead from the attack include prominent business personalities such as Ashok Kapur, chairman of Yes Bank India, and Andrea Liveras, a British shipping tycoon. There is no doubt that business visits to Mumbai will drop in the immediate future. There are already reports of bulk cancellations, particularly in high-end hotels, which are perceived to be key targets for terrorists. These perceptions will ebb both leisure and business tourist traffic. Travel advisories issued by several countries cautioning their citizens from travelling to Mumbai will adversely affect the city's tourism and hospitality industries.

The drop in tourist flow is also bad news for retail and entertainment service providers. This impact on Mumbai, however, is expected to be largely short-term. The jitters are unlikely to last for too long. Mumbai is too important a spot in the global business map to be ignored. The city has shown remarkable character and resilience by brushing off catastrophes that have included not only terror at-



Fly past: Pigeons taking flight on Sunday, with the Trident-Oberoi hotel (centre) in the background. The reduction in tourist flows is unlikely to have a major adverse impact on India's economic prospects because tourism is a relatively small industry for the country

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tacks, but also natural disasters.

Notwithstanding repeated setbacks, Mumbai continues to attract investments. Commercial and residential real estate prices in the city continue to remain among the highest in the country, underscoring the high premium on Mumbai property. So while leisure travel may take more time to recover, business travel is expected to resume after a few weeks.

Beyond Mumbai, concerns have been expressed over the impact of the attack on the Indian economy. These effects, again, can be distinguished between short and long-term consequences. The short-term repercussions pertain to a drop in tourist flows and travel. Terror attacks inevitably damage prospects for tourism wherever they occur. This is evident from the declines in tourist arrivals experienced by New York and Bali after terrorist violence in 2001 and 2002 respectively.

India has also had similar experiences in the past. This time, however, the extent of the repercussions may be somewhat greater than in previous occasions. The reason is simple – the terrorists targeted specific nationalities in the attack, particularly

Americans, British and Israelis. Unfortunately, India receives the most number of tourists from the United States and the United Kingdom.

In 2007, there were 800,000 and 796,000 tourists from these two countries respectively to India. Together, they made up almost one-third of total tourist arrivals in India in 2007. Both countries have issued advisories to their citizens against travelling to India.

From a macro-economic perspective, however, the reduction in tourist flows is unlikely to have a major adverse impact on India's economic prospects. Tourism is a relatively small industry for India. This is in sharp contrast to several other economies in the Asian region where tourism is one of the main generators of economic activity.

India's foreign exchange earnings from tourism stood at US\$10.73 billion in 2007. This is barely one per cent of gross domestic product (GDP) which is currently more than US\$1 trillion. Thus, in spite of a drop in tourist flows, the impact on GDP and foreign exchange reserves is expected to be minimal.

The latest terror attack could, how-

ever, see changes in insurance policies for compensating damages arising from such incidents. Though the final value of the losses are yet to be assessed, tentative estimates indicate that the damage could amount to US\$100 million. The bulk of this damage is attributable to losses suffered by the Taj Mahal Palace Hotel.

India has a terror insurance corpus of around US\$140 million. Preliminary calculations suggest that more than 70 per cent of this corpus may be wiped out in compensating claims due to the current attack. The shrinkage in the size of the corpus may have other implications. The attack has shown that India needs a much larger terror insurance pool to cover future losses.

Contributors to the corpus will, therefore, have to charge much higher premiums from corporate clients. This implies an escalation in corporate budgets. Several firms are, in fact, planning to revamp their internal security to guard against possible attacks. Coupled with higher insurance premiums, this may result in substantially higher fixed costs for companies.

Despite the recent Mumbai attack,

prospects for the Indian economy remain largely unaffected. Irrespective of their severity, terror attacks in the last decade and a half have not significantly dented economic activity in the country. Mumbai and Delhi experienced large scale attacks in July 2006 and October 2005 respectively.

In both these years, the Indian economy grew by more than 9 per cent. Attacks on Mumbai in March 2003 and March 1993 were also unable to upset the growth momentum. India's long-term prospects remain unaffected since such terror attacks do not influence its fundamental attributes as an investment location.

It continues to enjoy advantages of cheap and skilled labour, developed technological capabilities, efficient financial architecture and enabling policies. These advantages assure high long-term returns from investments in India. Whatever downside risks India faces in its economic outlook are outcomes of the global financial meltdown. The terror attack will have only moderate, short-lived impact on the country.

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