



Index of Industrial Production September 2009: Robust Growth Exceeding Expectations

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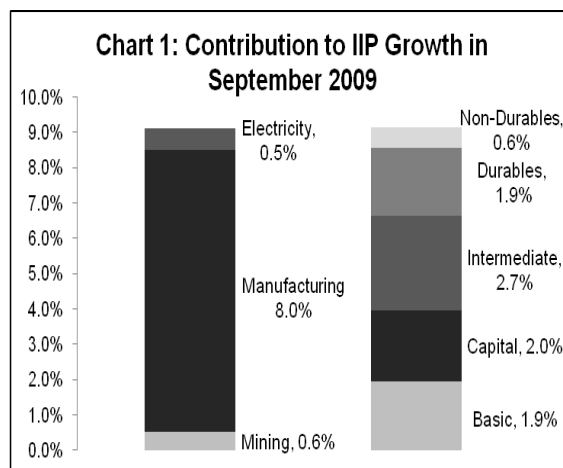
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The Index of Industrial Production (IIP) expanded by a robust 9.1% in year-on-year (y-o-y) terms in September 2009, exceeding expectations and pointing towards buoyant demand and consumer confidence ahead of the festive season. While growth slowed relative to the 11% growth witnessed in August 2009, the latter had been propped up by a favourable base effect. Moreover, the upturn in IIP growth has been sustained over several months, and growth of 6.5% in H1 2009-10 is higher than the growth of 5% in the corresponding period in the previous year.

IIP growth in September 2009 was led by strong growth of 9.3% in manufacturing, and aided by 8.6% and 7.9% growth in mining & quarrying and electricity, respectively. However, the healthy manufacturing growth rate conceals a worrying trend: the number of sub-categories within manufacturing experiencing contraction has increased to five in August and September 2009 from one in July 2009, indicating uneven growth. Moreover, according to provisional data, the level of monthly exports has declined in September and October 2009, raising some doubts regarding whether the recent revival in exports in month-on-month (m-o-m) terms will sustain in the medium term.

In terms of the use-based classification, consumer durables, capital goods and intermediate goods displayed double-digit growth in September 2009. However, growth for intermediate goods decelerated relative to y-o-y growth in August 2009. In a similar vein, growth of basic goods and consumer non-durables too slowed relative to the y-o-y growth displayed in August 2009. While growth of capital goods in H1 2009-10 remains substantially lower than in H1 2008-09, the upswing in growth of capital goods in the last two months is a welcome sign as it suggests that the industrial recovery may be developing beyond a consumption-driven upturn, with higher capacity utilisation and restocking of inventories.

		September		April-Sept.	
	Weight	2008	2009	2008	2009
IIP	100.0%	6.0%	9.1%	5.0%	6.5%
Mining	10.5%	5.8%	8.6%	3.9%	8.3%
Manufacturing	79.4%	6.2%	9.3%	5.3%	6.3%
Electricity	10.2%	4.4%	7.9%	2.6%	6.8%
Use Based Classification					
Basic	35.6%	5.0%	6.7%	3.9%	6.7%
Capital	9.3%	20.8%	12.8%	10.7%	4.5%
Intermediate	26.5%	-2.5%	10.8%	0.5%	9.5%
Durables	5.4%	14.7%	22.2%	7.2%	18.8%
Non-Durables	23.3%	4.8%	2.6%	7.7%	-0.1%



Source: Central Statistical Organisation (CSO)

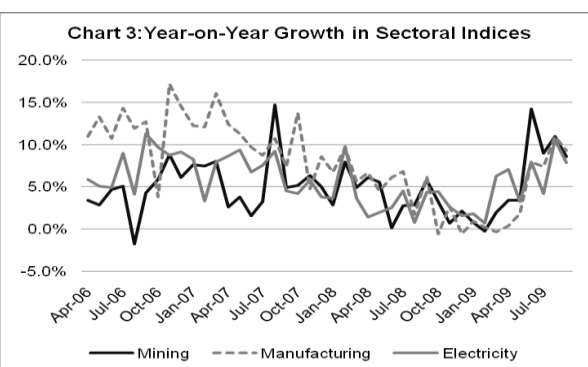
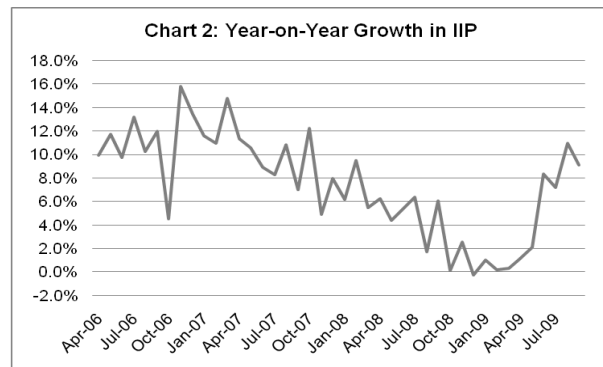
Sectoral Growth

Manufacturing growth was robust for the fourth consecutive month in September 2009, thereby bringing the average growth for the current fiscal to 6.3%, which is higher than the average growth for April-September 2008 (5.3%). Within manufacturing, industries such as basic chemicals, rubber, plastic, petroleum & coal products, machinery & equipment, transport equipment and other manufacturing industries reported high growth in September 2009 over the same month in the preceding year. However, in a disappointing trend, the number of sub-categories undergoing contraction increased to five each in August (with a weight of 16.16% in IIP) and September 2009 (with a weight of 17.51% in the IIP) from one in July. Notably, food products and metal products & parts, which have a weight of 9.1% and 2.8% in the total IIP, respectively, continued the trend of contraction that they have displayed for much of the calendar year.

Recently released data regarding monthly exports provided some disconcerting news: after displaying m-o-m growth for four consecutive months, the level of exports declined in September and October 2009 in US dollar terms.¹ The recent appreciation of the Indian rupee relative to currencies such as the US dollar and the British pound has heightened concerns regarding the relative competitiveness of and demand for Indian exports, particularly in view of the eventual phasing out of fiscal stimulus packages by India's trading partners.

Electricity generation expanded by 7.9% in September 2009 in y-o-y terms, largely reflecting higher thermal generation. However, thermal and hydroelectric generation in September 2009 was lower than that in the preceding month² and the y-o-y growth rate too was lower than the 10.6% growth displayed in August 2009.

Mining growth slowed to 8.6% in September 2009 from 11% in August 2009 and the level of the sub-index was lower in September as compared to the preceding month. This is likely to have been on account of higher rainfall in September relative to August 2009 and mining growth is expected to be lower in the coming months as well.



Source: CSO

¹ Provisional data released by the Ministry of Commerce and Industry, Government of India (GoI)

² As per the data available on the website of the Central Electricity Authority

Use-based Classification

In terms of the use-based classification, IIP growth in September 2009 was fairly broad-based, with the exception of the low growth displayed by consumer non-durables. Additionally, all the five use-based categories displayed expansion for the fourth consecutive month.

Growth displayed by capital goods increased to 12.8% in September 2009 from 8.7% in August 2009. The y-o-y growth displayed in September 2009 is especially impressive, considering that capital goods had expanded by 20.8% in September 2008. While the 4.5% growth of capital goods in H1 2009-10 remains substantially lower than the 10.7% growth displayed in H1 2008-09, the recent upswing in growth of capital goods is an encouraging trend, which suggests that the industrial recovery may be developing beyond a consumption-driven upturn, characterised by higher capacity utilisation and restocking of inventories.

With 22.2% growth in September 2009, consumer durables continued the trend of growth in excess of 20% for the third consecutive month and double-digit growth for the sixth month in a row. The growth displayed by consumer durables in September 2009 is remarkable, given that the sector had displayed strong growth of 14.7% in September 2008, and points towards strong consumer demand and confidence ahead of the festive season. Momentum may continue in the short term with restocking post the festive season while the release of the second instalment of Pay Commission related arrears to Central Government employees may fuel further demand. Regardless, the sector is expected to display high growth in the next quarter, given a favourable base effect. However, the inherent factors driving consumer demand are likely to weaken over the medium term, with the waning of the impact of the Pay Commission related benefits and eventual reversal of excise cuts effected as part of the fiscal stimulus packages of the Government of India.

Continuing with the robust growth witnessed in recent months, intermediate goods expanded by 10.8% in September 2009, albeit lower than the 14.2% growth displayed in August 2009. With sustained contraction in intermediate goods between August 2008 and February 2009, growth is expected to remain healthy over the next two quarters. Expansion in basic goods too slowed to 6.7% in y-o-y terms in September 2009 from 9.6% in August 2009.

After displaying growth of 5.8% and 6.4%, respectively, in July and August 2009, growth displayed by consumer non-durables slowed to 2.6% in September 2009. Moreover, growth for H1 2009-10 remains negligible relative to the 7.7% growth witnessed in H1 2008-09. While monsoon rainfall revived substantially in September, thereby improving the outlook for the *rabi* harvest, however the floods over parts of India in October are likely to have further damaged the *kharif* crop, which suffered from delayed South west monsoon rainfall in 2009. In ICRA's view, overall agricultural production and the level of rural incomes are expected to have a bearing on the demand for non-durables in coming months.

Outlook

Initial estimates had indicated that the IIP index contracted in October 2008 relative to the level of the index in the same month in 2007, the first such occurrence in 13 years. While IIP growth was subsequently revised upwards, it remained marginal at 0.1% in October 2008, with a contraction of 0.6% in the manufacturing index. As a result, the base effect is particularly favourable for manufacturing growth in October 2009. Regardless of the base effect, manufacturing growth is expected to remain strong on account of festive demand, particularly for consumer durables, while basic and intermediate goods are likely to benefit from restocking of inventories. However, mining growth is likely to be dampened on account of heavy rains during the month, while data released by the Central Electricity Authority suggests that electricity generation slowed to 4% in y-o-y terms in October 2009. Taking into account the favourable base effect for manufacturing, overall IIP growth is expected to be around 10% in October 2009.



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