



Index of Industrial Production June 2011: Improvement in growth to 8.8% led by a sharp growth of capital goods does not signal a sustainable trend

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The Index of Industrial Production (IIP) expanded by a stronger-than-expected 8.8% in June 2011, higher than the 7.4% growth in June 2010, which marks a considerable improvement relative to the moderate 5.8-5.9% growth in the previous two months. Although the overall pace of growth was favourable, IIP growth in June 2011 was highly uneven across sub-sectors, with a favourable performance of capital and basic goods amidst sluggish growth of intermediate and consumer goods.

IIP growth was primarily led by a sharp 37.7% expansion in capital goods output, as compared to the growth of 7.3% and 6.1% displayed in April 2011 and May 2011, respectively, highlighting the persistence of volatility in the growth of this sub-sector despite the switch to the new IIP index with an updated base year. In month-on-month (m-o-m) terms, the capital goods index increased by a steep 30% in June 2011 relative to May 2011, which may be related to completion of orders prior to the end of the quarter. Additionally, the sharp 37.7% growth in June 2011 in year-on-year (y-o-y) terms benefitted from a favourable base effect, following a low 3.7% growth in June 2010. With the base effect turning adverse in July 2011 (following a 41% growth of capital goods in July 2010) the growth of capital goods is likely to slow considerably in the coming month and the uptick in IIP growth recorded in June 2011 is unlikely to sustain over the coming months.

IIP growth was supported by a 7.5% expansion of basic goods in June 2011, marking a steady improvement for the fourth consecutive month. However, consumer durables, consumer non-durables and intermediate goods displayed low growth (1.0%, 2.1% and 1.9%, respectively) in June 2011, substantiating the weakening momentum of domestic consumption demand as indicated by other data, particularly the slowing growth of domestic sales of passenger vehicles.

In terms of the sectoral classification, IIP growth in June 2011 was led by the healthy 10.0% expansion of the manufacturing sector and the 7.9% growth of electricity generation. However, manufacturing growth remained concentrated, with the five sub-sectors making the highest contribution to manufacturing growth accounting for 9.6% of the 10% growth recorded in June 2011. IIP growth was dampened by the marginal 0.6% growth of mining & quarrying in June 2011.

In terms of the quarterly trends, mining & quarrying and electricity displayed similar growth rates in Q1, 2011-12 (1.1% and 8.2%, respectively) as compared to Q4, 2010-11, whereas the pace of growth of manufacturing declined to 7.5% from 8.9% in Q1, 2011-12 in Q4, 2010-11. The pace of growth of capital goods increased sharply (to 17% from 4.7%) and that of basic goods improved somewhat (to 7.2% from 6.6%) in Q1 2011-12 as compared to Q4, 2010-11. However, the pace of growth eased substantially in Q1 2011-12 relative to the previous quarter in the case of consumer durables (to 3.3% from 15.2%), consumer non-durables (to 5.0% from 8.9%) and intermediate goods (to 2.2% from 5.6%).

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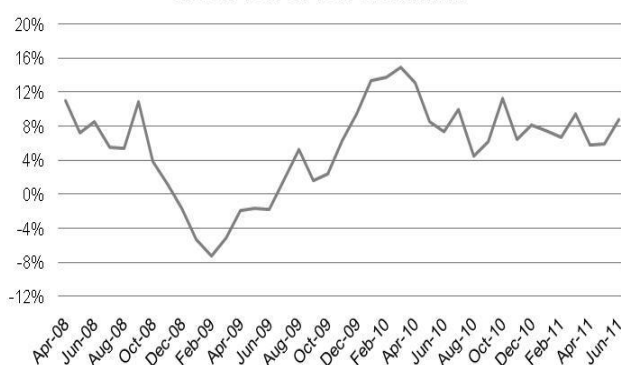
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Table 1: Trend in IIP Growth

	IIP	Sectoral			Use-Based Classification				
		Mining	Manu- facturing	Electrici- ty	Basic	Capital	Interme- diate	Durables	Non- Durables
Weight	100.00%	14.16%	75.53%	10.32%	45.68%	8.83%	15.69%	8.46%	21.35%
Month									
May-10	8.5%	7.9%	8.9%	6.1%	6.1%	15.8%	11.7%	14.7%	1.9%
June-10	7.4%	6.9%	7.9%	3.5%	3.7%	3.7%	8.5%	21.2%	7.5%
May-11	5.9%	1.3%	6.1%	10.3%	7.3%	6.1%	0.3%	5.2%	7.9%
June-11	8.8%	0.6%	10.0%	7.9%	7.5%	37.7%	1.9%	1.0%	2.1%
Apr-June FY11	9.7%	8.0%	10.4%	5.4%	5.5%	18.3%	10.7%	19.7%	5.4%
Apr-June FY12	6.8%	1.1%	7.5%	8.2%	7.2%	17.0%	2.2%	3.3%	5.0%

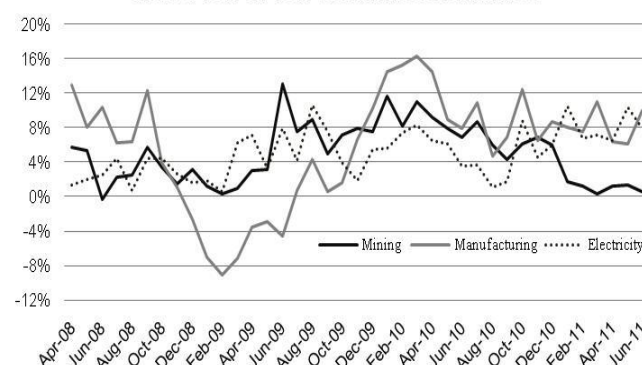
Source: Central Statistics Office (CSO)

Chart 1: Year-on-Year Growth in IIP



Source: CSO

Chart 2: Year-on-Year Growth in Sectoral Indices



Source: CSO

Sectoral Growth

Manufacturing: The manufacturing sector, which accounts for over 75% of the IIP Index, recorded a robust expansion of 10.0% in June 2011, higher than the 7.9% growth recorded in June 2010. The pace of growth improved appreciably relative to the 6.1-6.3% growth recorded in the previous two months. Of the 22 sub-sectors of the manufacturing sector, the number of sub-sectors displaying expansion improved to 15 in June 2011 from 13 in May 2011 (refer *Table 2*). Nevertheless, growth remained concentrated, with the five sub-sectors making the highest contribution to manufacturing growth accounting for 9.6% of the 10% growth in the manufacturing sector in June 2011.

Electrical machinery & apparatus, with a weight of less than 2% in the IIP index, recorded a surprisingly strong growth of 88.9% in June 2011, benefitting from a favourable base effect arising from a 23% contraction in June 2010, and particularly a 232.4% growth of 'cables, rubber insulated' in June 2011 (refer *Annexure B*). The sharp pace of growth of this sub-sector is likely to be related to filling of orders at the end of the quarter, following a poor performance in the previous five months (contraction of 12.1%, 39.3% and 5.9% in January 2011, February 2011 and May 2011, respectively and growth of 7.3% and 2.2% in March 2011 and April 2011, respectively).

Growth of basic metals, with a weight of over 11% in the IIP Index, improved to 17.7% in June 2011, from the 11.8-13.6% growth recorded in the previous three months. Growth in June 2011 benefited from the high growth of items such as 'sponge iron' and 'stainless/alloy steel' among others (refer *Annexure B*).

Growth of motor vehicles, trailers & semi-trailers declined, albeit to a healthy 14.5% in June 2011 from the 22-32% growth recorded between December 2010 and May 2011. The data released by the Society of Indian Automobile Manufacturers (SIAM) indicate that the growth of total automobile production slowed mildly to 16.6% in June 2011 from 20.3% in April 2011 and 18.5% in May 2011. Additionally, SIAM data indicates that domestic sales of passenger vehicles slowed considerably to 4% in June 2011 from 8% in

May 2011, highlighting the weakening domestic consumer demand, even as domestic sales of commercial vehicles improved to 18% in June 2011 from 16% in May 2011.

Food products, with a weight of over 7% in the IIP Index, displayed a growth of 6.7% in June 2011, substantially lower than the revised growth of 19.5% in May 2011. Growth in June 2011 benefited from the significant growth recorded by 'sugar' (247%), 'molasses' (180%) and 'industrial alcohol' (31%), which form around 26% of the food products sub-index. Other transport equipment expanded by 18.6% in June 2011, in line with the 18-20% growth recorded in the previous three months.

Table 2: Contribution to the Growth of the Manufacturing Sector by Sub-Sectors

Sub-sector	Weight	Growth in June 2011	Contribution to Manufacturing Growth
Electrical Machinery & Apparatus N.E.C.	1.98	88.9%	5.0%
Basic Metals	11.34	17.7%	2.6%
Motor Vehicles, Trailers & Semi-Trailers	4.06	14.5%	1.0%
Food Products and Beverages	7.28	6.7%	0.5%
Other Transport Equipment	1.82	18.6%	0.5%
Others Displaying Expansion	25.41	6.2%	1.9%
Others Displaying Contraction	23.64	-4.4%	-1.4%
Manufacturing	75.53	10.0%	10.0%

Source: CSO; ICRA Analysis

Of the 22 manufacturing sub-sectors, the number of sub-sectors experiencing contraction declined to seven in June 2011 (with a combined weight of 23.6%) from nine in May 2011 (with a combined weight of 22.4%). However, the combined weight of the sub-sectors recording a contraction increased in June 2011 relative to May 2011 (refer *Table 3*), largely on account of chemicals & chemical products (with a weight of 10.06%), which underwent a shallow contraction in June 2011 following a slowdown in growth in the previous month (8% growth in April 2011 and 4.4% growth in May 2011).

Additionally, wearing apparel, dressing & dyeing of fur; underwent a contraction of 5.5% in June 2011 following a slowdown in the pace of growth over the previous three months (9.9%, 5.4% and 0.4% in March 2011, April 2011 and May 2011, respectively). Moreover, medical, precision & optical instruments, watches & clocks underwent a sharp contraction of 10.3% in June 2011 following a high 21% growth over the previous three months.

Textiles displayed a contraction for the third consecutive month in June 2011; the extent of de-growth ranged from 3.4% to 5.3% between April 2011 and June 2011. Rubber & plastic products displayed a de-growth for the fourth consecutive month, however, the pace of de-growth has eased in each of these months (7.4%, 3.4%, 2.5% and 0.3% in March 2011, April 2011, May 2011 and June 2011).

The sub-sector wood & products of wood & cork except furniture; articles of straw & plating materials underwent contraction for the tenth consecutive month, with a marginal de-growth of 0.3% in June 2011. The extent of contraction in radio, TV & communication equipment & apparatus became sharper in June 2011 (10.1%) as compared to May 2011 (0.7%).

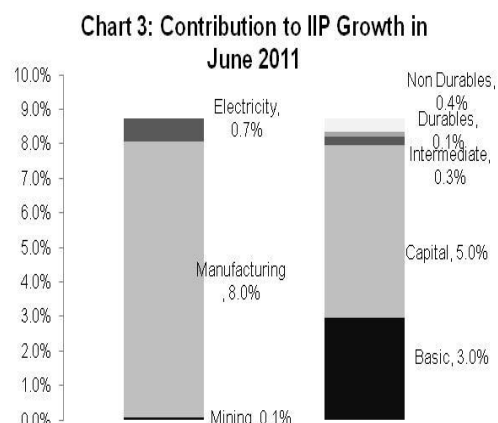
Electricity: The pace of growth of electricity generation declined to 7.9% in June 2011 from 10.3% in May 2011. According to the data released by the Central Electricity Authority (CEA), the pace of growth of thermal generation eased in June 2011 even as that of hydroelectric generation recorded an improvement in June 2011. On an average, coal output has displayed a marginal 0.15% growth in Q1, 2011-12, as indicated by data on the Eight Core Industries. In the coming months, the availability of domestic and imported coal and gas would critically impact the pace of growth of thermal generation. Additionally, the progress of the monsoon rainfall in the catchment areas of reservoirs for hydel plants would crucially determine the pace of growth of hydroelectricity generation.

Table 3: Sub-sectors Displaying Contraction in June 2011

Sector	Weight	Growth in June 2011
Textiles	6.16	-4.3%
Wearing Apparel; Dressing & Dyeing of Fur	2.78	-5.5%
Wood & Products of Wood & Cork Except Furniture; Articles of Straw & Plating Materials	1.05	-0.3%
Chemicals & Chemical Products	10.06	-1.0%
Rubber & Plastics Products	2.02	-0.3%
Radio, TV & Communication Equipment & Apparatus	0.99	-10.1%
Medical, Precision & Optical Instruments, Watches & Clocks	0.57	-10.3%
Total of Above	23.64	-4.4%

Source: CSO; ICRA Analysis

Mining & Quarrying: The pace of growth of the mining & quarrying sub-index eased further to a marginal 0.6% in June 2011, from the 1.3% growth recorded in both April 2011 and May 2011. The growth of this sub-index averaged a lack-lustre 1.1% in H1 2011 as compared to a healthy 9.1% in H1 2010, led by the contraction in natural gas and coal output for a number of months. The low growth of mining & quarrying in recent months dampened the pace of growth of the IIP, both through the first order impact and the second order impact through forward linkages with other sectors. The recent Supreme Court rulings imposing a ban on mining in the iron-ore rich Bellary district of Karnataka by all operators except National Mineral Development Corporation (NMDC), following the uncovering of illegal mining of iron ore in the district, may further dampen the growth of mining & quarrying to an extent in the coming months. *Source: CSO; ICRA Analysis*



Use-based Classification

Capital Goods: The capital goods sub-sector, which has a weight of over 9% in the IIP Index, expanded by a sharp 37.7% in June 2011, benefiting from a favourable base effect, with a low 3.7% growth recorded in June 2010. The growth of capital goods in June 2011 received a boost from the sharp growth rate recorded by a number of items (refer *Table 4*); these items have a combined weight of less than 0.7% in the IIP Index.

Growth of this sub-index in June 2011 was sharply higher than the moderate growth of 7.3% and 6.1% displayed in April 2011 and May 2011, respectively, highlighting the persistence of volatility in the growth of this sub-sector in spite of the introduction of the revamped IIP index with an updated base year.

In m-o-m terms, the capital goods sub-index rose by 30% in June 2011 relative to May 2011, which may reflect completion of orders at the end of the quarter, further supporting the argument that the sharp growth in capital goods is unlikely to sustain in the coming months.

Basic Goods: Basic goods expanded by 7.5% in June 2011, marginally higher than the 7.3% growth recorded in May 2011. Growth of basic goods in June 2011 was boosted by high growth in some items such as 'sponge iron', 'stainless/alloy steel' and 'molasses', with a combined weight of around 2.5% in the IIP index (refer *Table 5*).

The pace of growth of basic goods improved somewhat to 7.2% in Q1 2011-12 from 6.6% in Q4, 2010-11.

Intermediate Goods: Intermediate goods output expanded by a low 1.9% in June 2011, relative to the healthy 8.5% growth in June 2010. However, this marked a slight improvement relative to the 0.3% growth recorded in May 2011.

On an average, the pace of growth of intermediate goods declined considerably to a low to 2.2% in Q1 2011-12 from 5.6% in Q4, 2010-11.

Table 4: Components of Capital Goods displaying Significant Expansion in June 2011

Component	Growth in June 2011
Cable, Rubber Insulated	232.4%
Printing Machinery	81.1%
Rubber Transmission and V Belts	57.0%
Packaging Machinery	48.5%
Textile Machinery	47.9%
X-Ray Equipment	33.1%
Industrial Chains	32.0%

Source: CSO

Table 5: Components of basic Goods displaying Significant Expansion in June 2011

Component	Growth in June 2011
Molasses	179.5%
Stainless/ Alloy Steel	72.4%
GP/GC sheets	54.1%
Sponge Iron	38.0%
CR Sheets	33.4%

Source: CSO

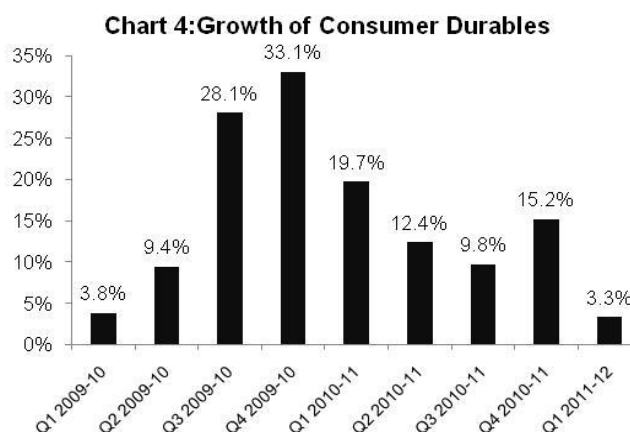
Table 6: Components of Intermediate Goods displaying Significant Expansion in June 2011

Component	Growth in June 2011
Industrial Alcohol	31.0%
Viscose Staple Fibre	72.9%
Tanned or Chrome Skins and Leathers	53.6%

Source: CSO

Consumer Durables: The growth of consumer durables slowed to 1% in June 2011, as compared to the 3.8% and 5.2% growth recorded in April 2011 and May 2011, respectively. The low growth recorded by this sector in June 2011 was partly led by an adverse base effect, with a robust 21.2% growth recorded in June 2010.

The pace of growth of consumer durables declined sharply to 3.3% in Q1 2011-12 from 15.2% in Q4, 2010-11, despite an easing of the base effect (refer *Chart 4*). Although the base effect is likely to ease further in the coming months, consumer durables are likely to display low growth reflecting the impact of persistently high inflation and rising interest rates on the demand for such products.



Source: CSO

Consumer Non-Durables: The pace of growth of consumer non-durables eased sharply to 2.1% in June 2011 from a revised growth of 7.9% in May 2011. However, this was partly on account of an adverse base effect, with a growth of 7.5% in June 2010 as compared to 1.9% in May 2010. Growth in June 2011 benefits from the continuing sharp growth of 'sugar' (refer *Table 7*).

Table 7: Components of Consumer Non-Durables displaying Significant Expansion in June 2011

Component	Growth in June 2011
Sugar	246.9%

Source: CSO

The pace of growth of consumer non-durables recorded a decline to 5.0% in Q1 2011-12 from 8.9% in Q4, 2010-11.

Outlook

With an adverse base effect in July 2011, following a 41% growth of capital goods in July 2010, the growth of capital goods is likely to slow considerably relative to the 37.7% growth recorded in June 2011.

Overall, the trend of dampening growth of consumer durables, consumer non-durables and intermediate goods in Q1 2011-12 relative to Q4 2010-11, suggests a moderation of domestic consumption demand, which is likely to persist over the coming months. Nevertheless, with a favourable base effect following de-growth of 0.9% in July 2010, growth of consumer non-durables may display an improvement in July 2011. The potential impact of global economic uncertainties on the domestic growth outlook may dampen domestic consumption demand further in the coming months. Additionally, although commodity prices have weakened, the sustainability of this trend is uncertain and manufacturers are unlikely to reduce prices given the higher inventory costs. Quick estimates released by the Ministry of Commerce & Industry, Government of India indicate that exports displayed a robust growth of 82% in July 2011, which may reflect in a boost in manufacturing growth output in the immediate term. However, exports growth is likely to ease considerably in the coming months led by the base effect, and the magnitude of new orders would be critically impacted by the global economic conditions.

The growth of the mining & quarrying and electricity sectors is expected to remain at similar levels in July 2011 relative to the previous month. Overall, in ICRA's view, IIP growth in July 2011 is likely to moderate relative to the level recorded in June 2011.

Annexure A:

Chart 5: Year-on-Year Growth in Mining

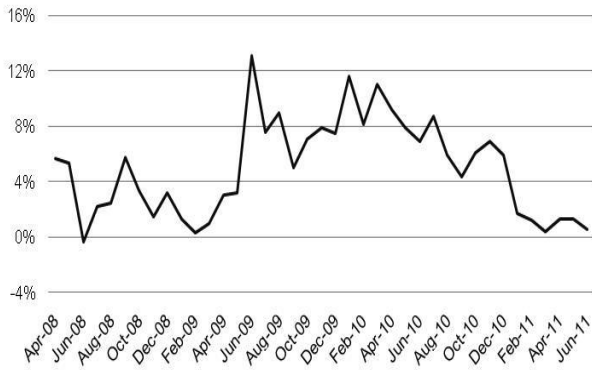


Chart 6: Year-on-Year Growth in Manufacturing

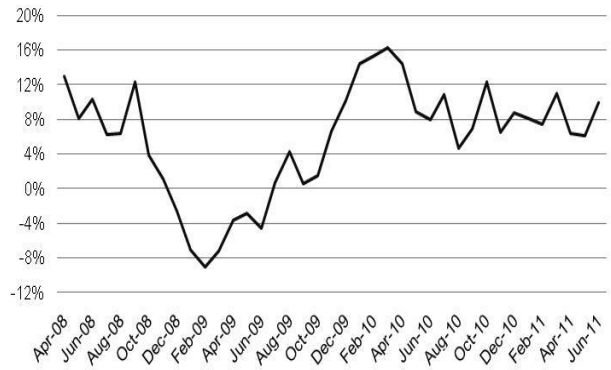


Chart 7: Year-on-Year Growth in Electricity

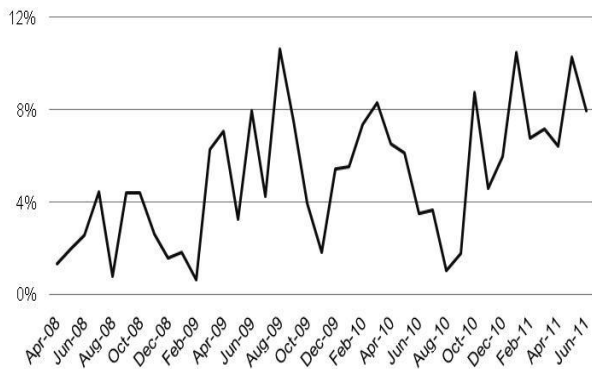


Chart 8: Year-on-Year Growth in Basic Goods

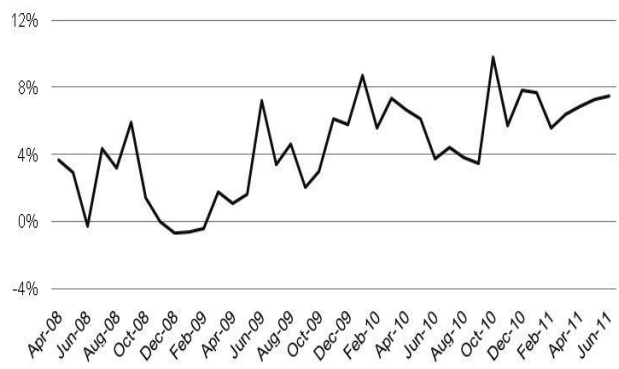


Chart 9: Year-on-Year Growth in Capital Goods

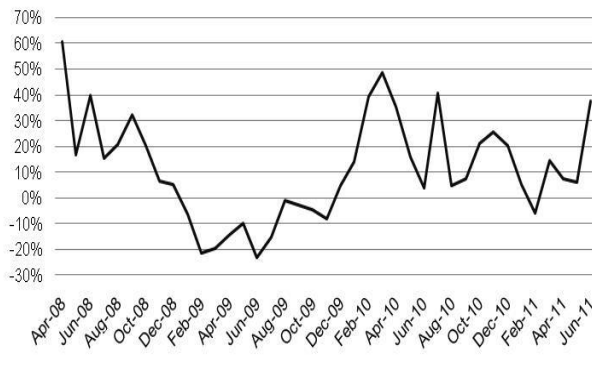


Chart 10: Year-on-Year Growth in Intermediate Goods

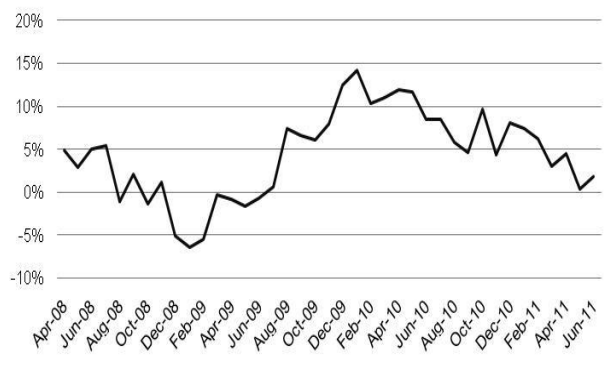


Chart 11: Year-on-Year Growth in Durables

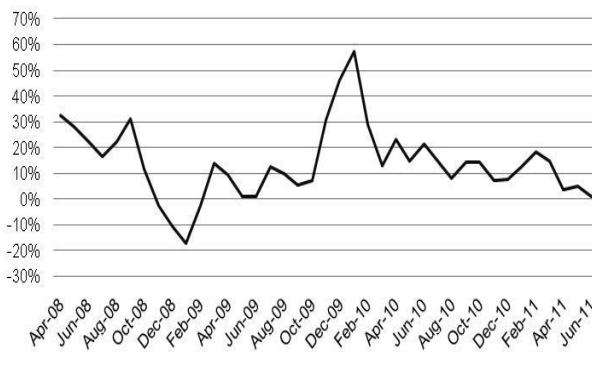
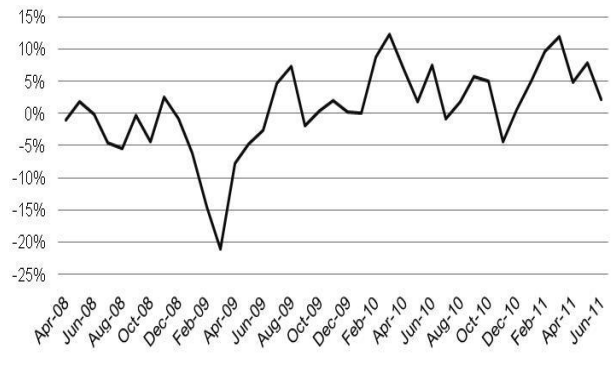


Chart 12: Year-on-Year Growth in Non-Durables



Source: CSO

Annexure B:

Items	Weight	Growth In June 2011 (%)	Manufacturing Sub-Sector	Use-Based Classification
Molasses	0.11	179.50%	Food Products & Beverages	Basic Goods
Sponge Iron	1.00	38.00%	Basic Metals	
Stainless/ Alloy Steel	0.64	72.40%	Basic Metals	
GP/GC Sheets	0.25	54.10%	Basic Metals	
CR Sheets	0.56	33.40%	Basic Metals	
Cable, Rubber Insulated	0.12	232.40%	Electrical Machinery & Apparatus n.e.c.	Capital Goods
Rubber Transmission & V Belts	0.06	57.00%	Rubber & Plastics Products	
Printing Machinery	0.08	81.10%	Machinery & Equipment n.e.c.	
Packaging Machinery	0.06	48.50%	Machinery & Equipment n.e.c.	
Textile Machinery	0.17	47.90%	Machinery & Equipment n.e.c.	
X-Ray Equipment	0.10	33.10%	Machinery & Equipment n.e.c.	
Industrial Chains	0.06	32.00%	Machinery & Equipment n.e.c.	
Industrial Alcohol (Rectified/Denatured Spirit)	0.26	31.00%	Food Products & Beverages	Intermediate Goods
Viscose Staple Fibre	0.03	72.90%	Chemicals & Chemical Products	
Tanned Or Chrome Skins And Leathers	0.13	53.60%	Luggage, Handbags, Saddlery, Harness & Footwear; Tanning & Dressing of Leather Products	
Sugar (Including Sugar Cubes)	1.52	246.90%	Food Products & Beverages	Consumer Non-Durables

Source: CSO

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