IIP Watch: Industrial production growth in May supported by consumer-related segments

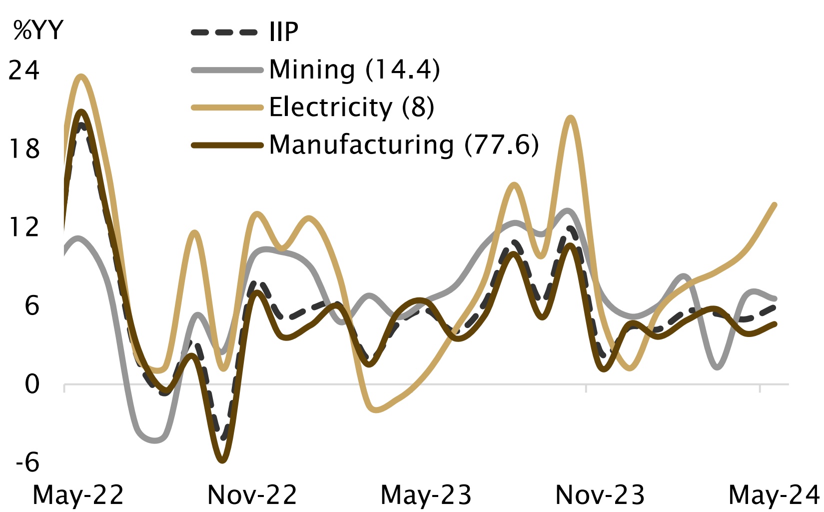
TRUST
In Partnership. With Trust.

19 July, 2024

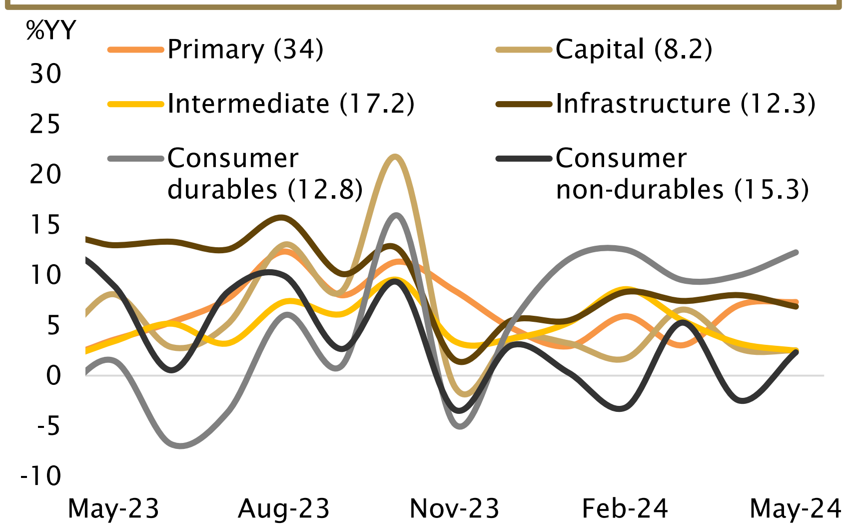
Key takeaways

- Industrial production growth improved to a seven-month high in May after easing for three straight months. Year-on-year growth at 5.9% was above market expectations (Bloomberg estimate: 4.9%), higher than 5.0% in April and supported by month-on-month momentum amidst unfavorable base effects.
- By industry, year-on-year growth in mining and electricity was higher than in manufacturing for the second straight month, though the contribution from latter was stronger due to its weight in the IIP index. Within manufacturing, 17 of 23 sub-sectors expanded, with the largest contributions from metals and electrical equipment. Electricity sector posted double-digit growth amid heatwave conditions during the month.
- By type of goods, growth was driven by the consumer segment. Consumer durables posted double-digit growth, continuing the trend from April, while consumer non-durables grew after contracting in the previous month. Year-on-year growth in construction and capital goods moderated amid the model code of conduct ahead of the general elections that constrained government spending on capex.
- In RBI's latest monthly bulletin, authors of the 'State of the economy' article noted that an enduring movement of CPI inflation towards 4% target could be sufficient for a policy stance change. However, in another article of the bulletin, there was an upward revision to the economy's neutral rate of interest to 1.4-1.9% for Q4-FY24 from 1.1-1.3% for Q3-FY22 (revised up from earlier estimate of 0.8-1.0%), which suggests that the MPC has less space for rate cuts (10-60bps) to shift policy towards a neutral setting.

IIP growth at seven month high in May



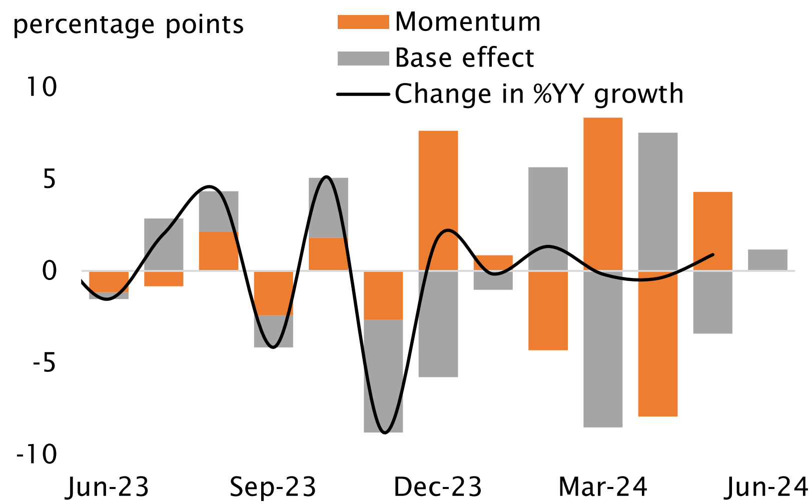
Both consumer durables and non durables grew in May



High IIP due to month-on-month growth amid unfavorable base effect

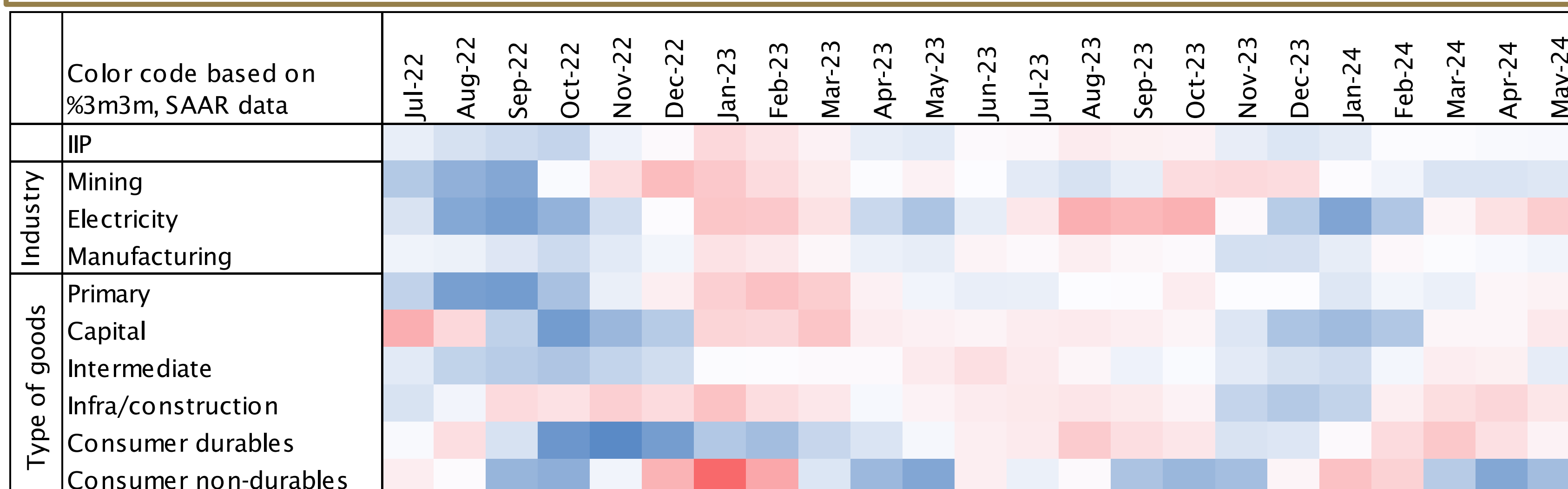
- The increase in industrial output growth in May (5.9%YY) compared to the previous month (5.0%) was due to 4.4% month-on-month growth in output in non-seasonally adjusted terms, even as base effect was unfavorable. However, the monthly increase in production was lower than the median for the month (FY13-24) at 5.5%. On a seasonally adjusted basis (accounting for uneven dates of the festive season), production growth eased from April, and so did the momentum, measured by 3-month/3-month annualized rate.
- In terms of sectors, higher momentum was driven by mining and electricity, while by type of goods, improvement in momentum was noted in case of primary and capital goods. Despite improvement in May, momentum in consumer non-durables output remains muted due to volatility in growth in recent months.

Growth momentum drove higher IIP growth in May



Red shows high momentum, blue indicates the opposite

Improved momentum in electricity amid heatwave conditions; consumer nondurables yet to see sustained growth



Manufacturing, electricity posted higher growth compared to April

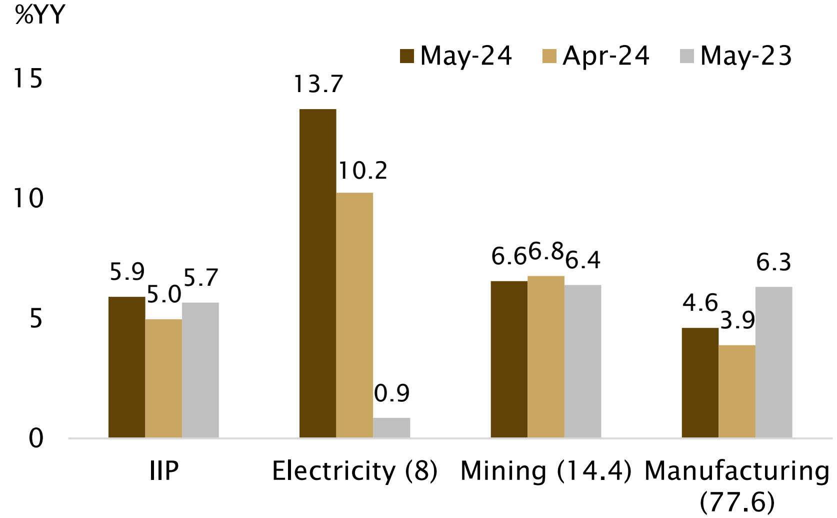
- Higher year-on-year industrial output growth in May compared to April was driven by improvement in manufacturing and electricity production. Mining growth was slightly lower than in April. In terms of contribution to growth, manufacturing continued to add the most due to its high weight in the index.

- Electricity posted year-on-year double-digit expansion in May for the second straight month amid higher demand due to heatwave conditions. Manufacturing growth was supported by revival in production of certain consumer-related segments. Consumer durables posted double-digit growth for the second straight month, while production of consumer non-durables grew after contracting in April. While consumer durables output has been growing for the past six months, production of non-durables has been volatile.

- The output of capital goods and infrastructure-related sub-sectors was impacted and lower than the previous month due to constrained government spending amid the model code of conduct ahead of general elections.

- Within manufacturing, production improved in 17 out of 23 sub-sectors, up from 16 in April. Basic metals continued to add the most, though growth moderated for the third consecutive month. Electrical equipment, (which includes consumer durable items), and computers and electronic products, added strongly to growth. Within non-durables, pharmaceuticals added to growth, while food products segment was a laggard.

Manufacturing growth higher in May compared to April



Numbers in parenthesis denote weights

Improved growth in 17 of 23 manufacturing sub-groups

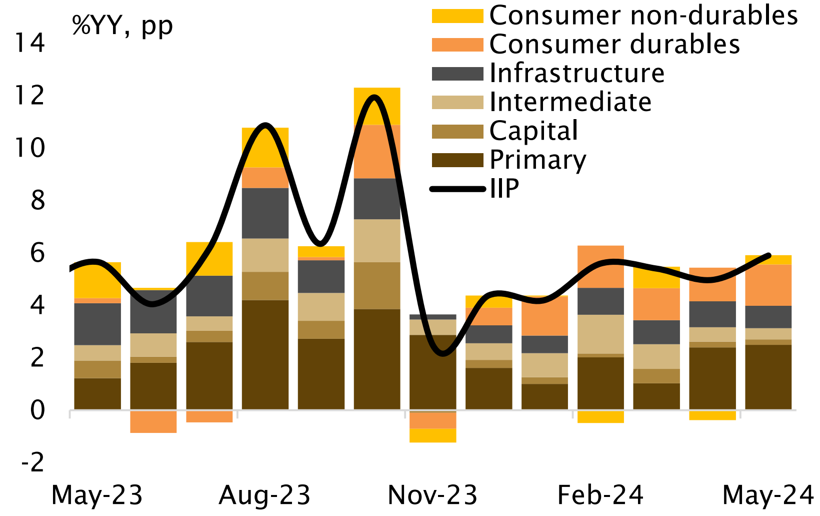
Top / bottom manufacturing sub-sectors by contribution to IIP growth (percentage pts.)	
Basic metals (12.8)	1.29
Electrical equipment (3)	0.57
Pharmaceuticals (5)	0.48
Fabricated metal pdts. (2.7)	0.42
Computer, electronic pdts. (1.6)	0.41
Food products (5.3)	-0.38
Other manufacturing (0.9)	-0.10
Chemicals (7.9)	-0.05
Rubber, plastic pdts. (2.4)	-0.03
Textiles (3.3)	-0.03

Numbers in parenthesis denote weights

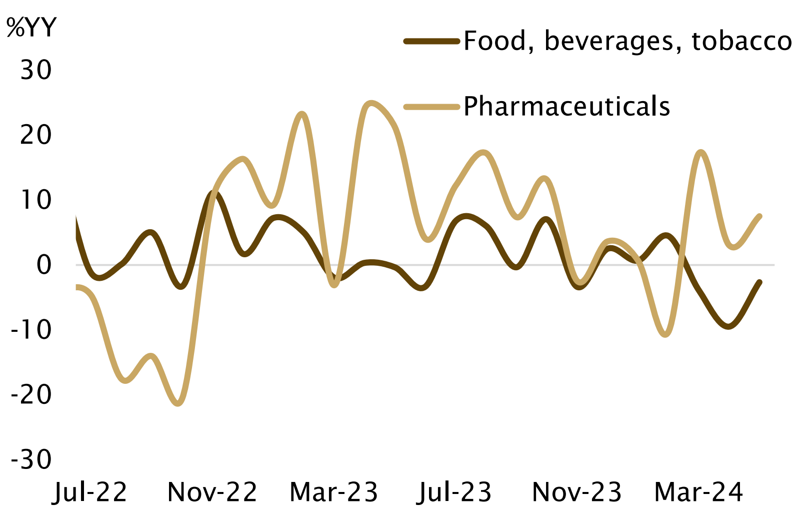
Consumer-related segments supported production growth in May

- Though the production of infrastructure and capital goods remains strong relative to pre-pandemic levels, in terms of contribution to year-on-year growth, consumer durables has been adding strongly to industrial output growth over the past five months.
- In May, year-on-year growth in the manufacture of computers and electronics was the highest in almost two years at around 20%. A recent article in the Economist, also cited in the RBI's monthly bulletin section on 'State of the economy', highlights growth in India's electronics industry, which is reflected not only in production numbers but also in exports data. The support from government in the form of PLI schemes is attracting investment from domestic and foreign firms.
- Though consumer non-durables output rebounded in May, it needs to be seen if the trend is sustainable.

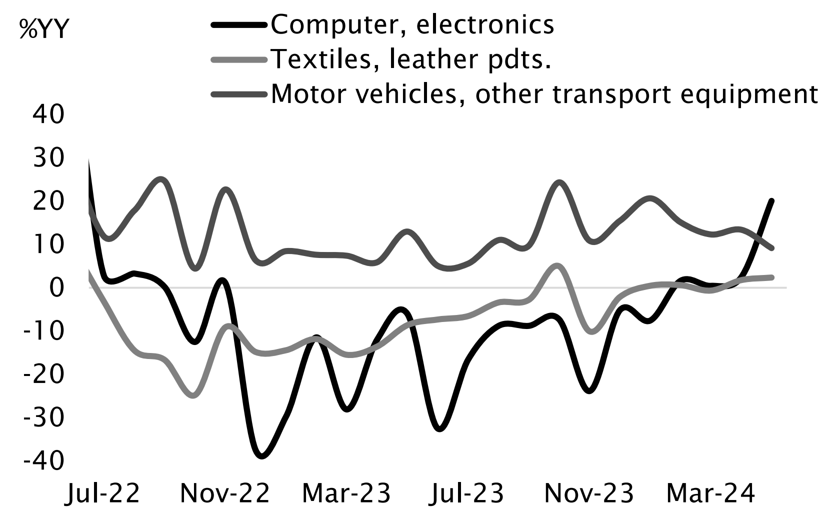
Consumer durables has been adding strongly to growth



Pharmaceuticals output drove rebound in nondurables

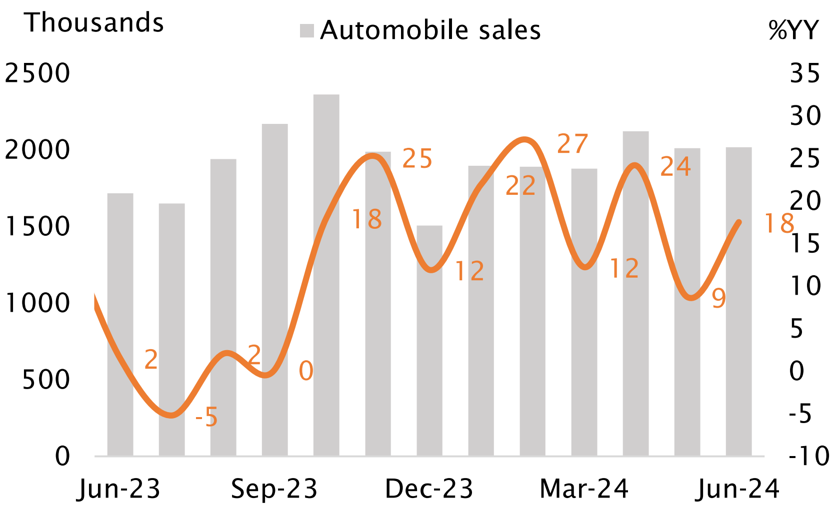


Computers and electronics posted strong growth

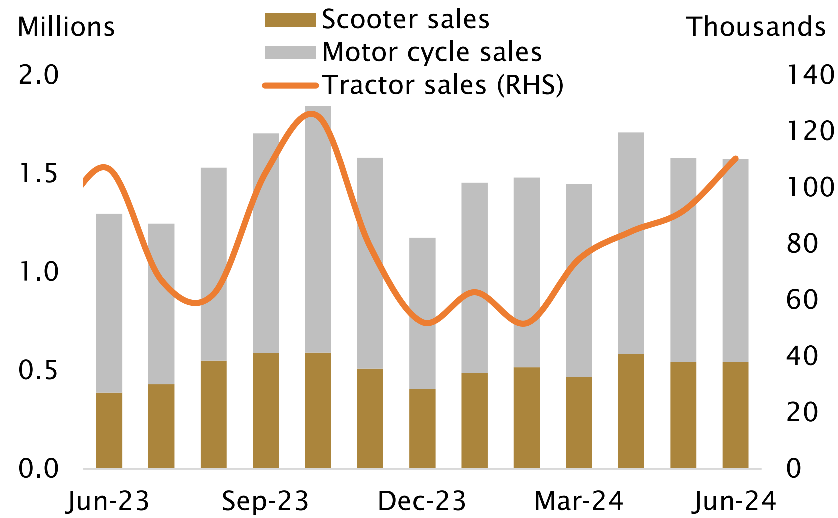


High frequency indicators: Auto sales show revival in rural demand

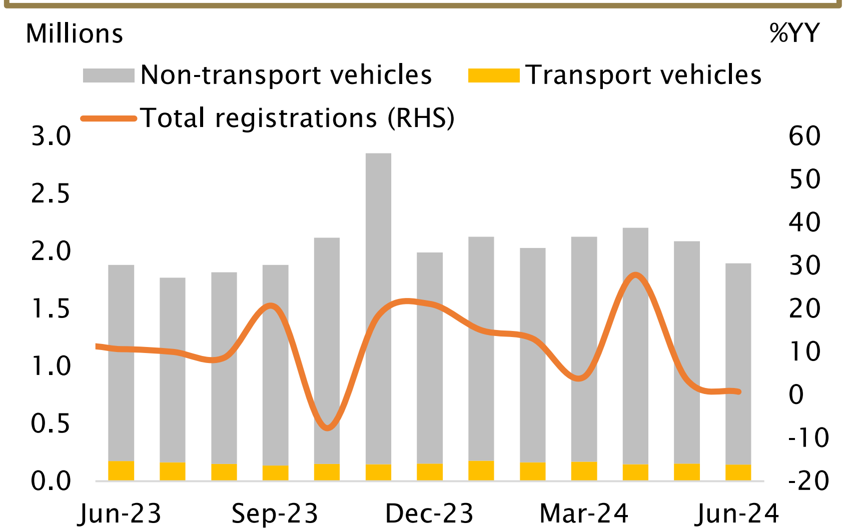
Automobile sales



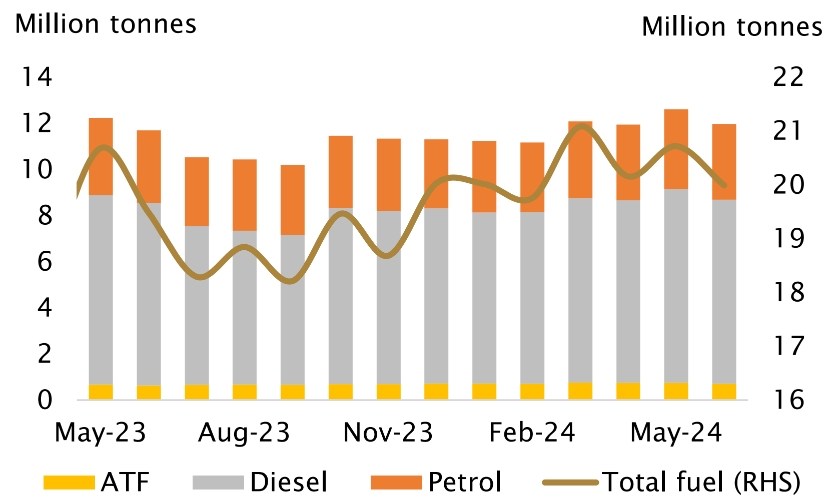
Rural demand



Vehicle registrations

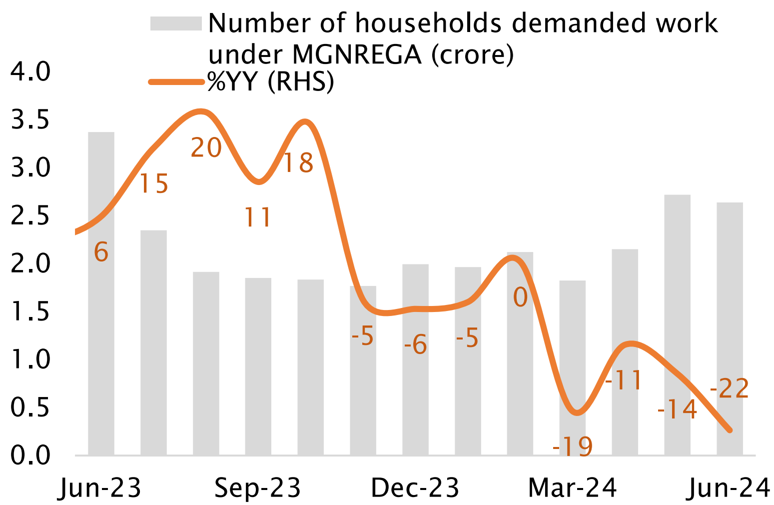


Fuel consumption

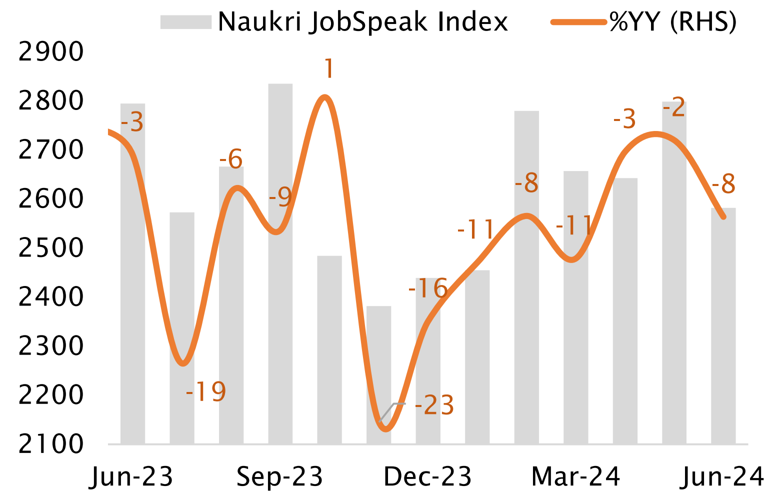


Goods movement shows continued strength in economic activity

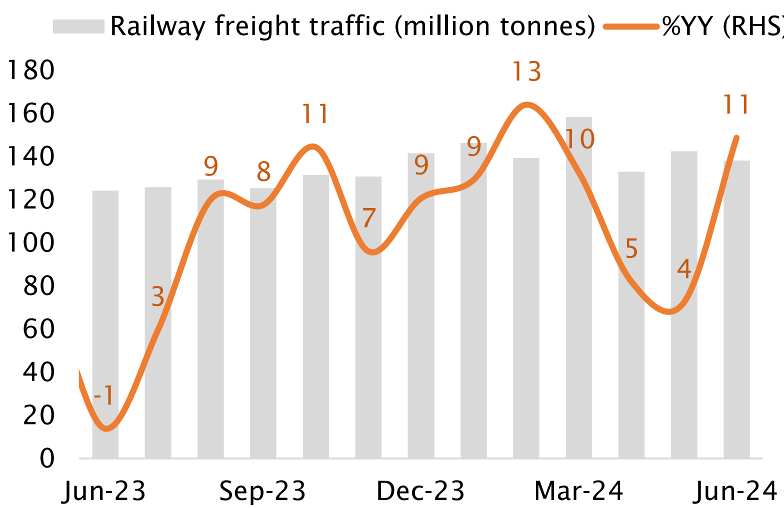
Less demand for work under MGNREGA in June



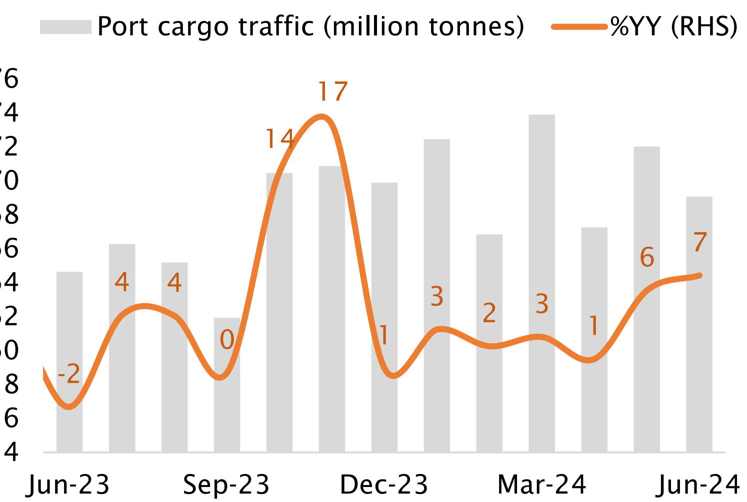
White-collar hiring momentum moderated in June



Double-digit growth in railway freight traffic

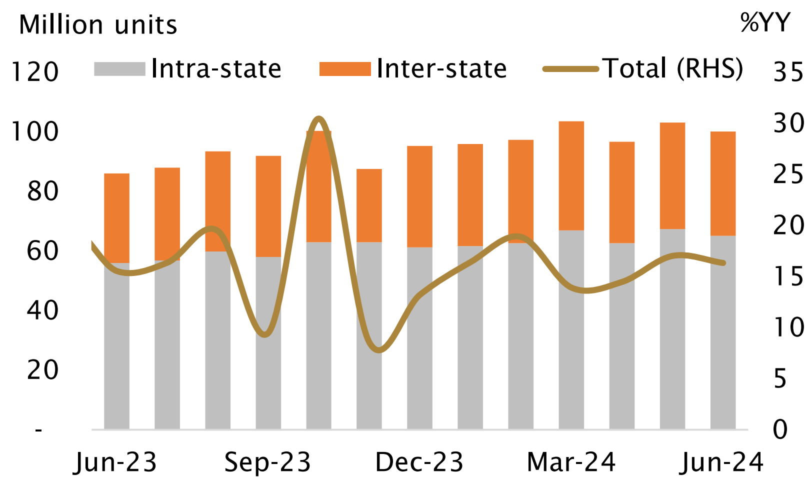


Higher growth in port cargo traffic amid m-o-m easing

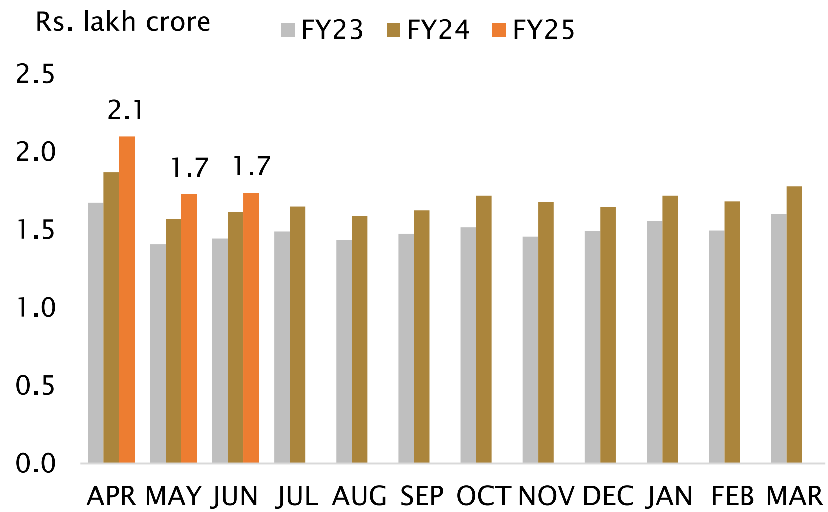


High frequency data: GST collections, PMI data remain solid

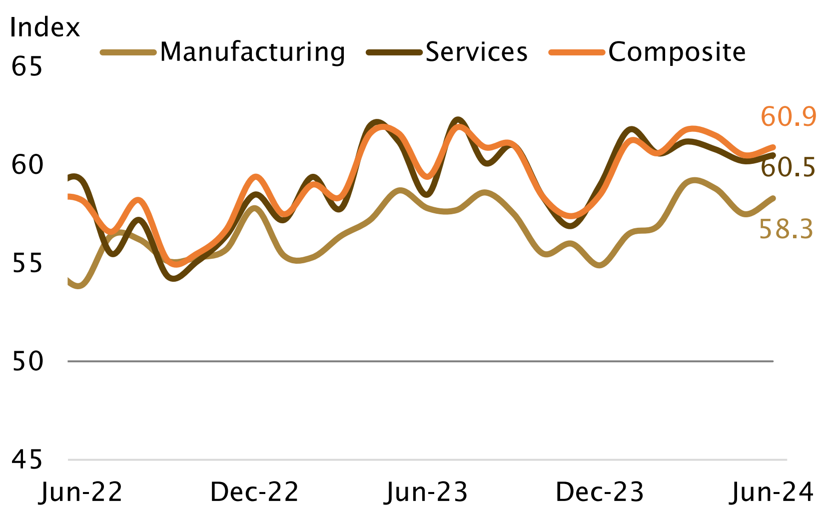
GST e-way bill



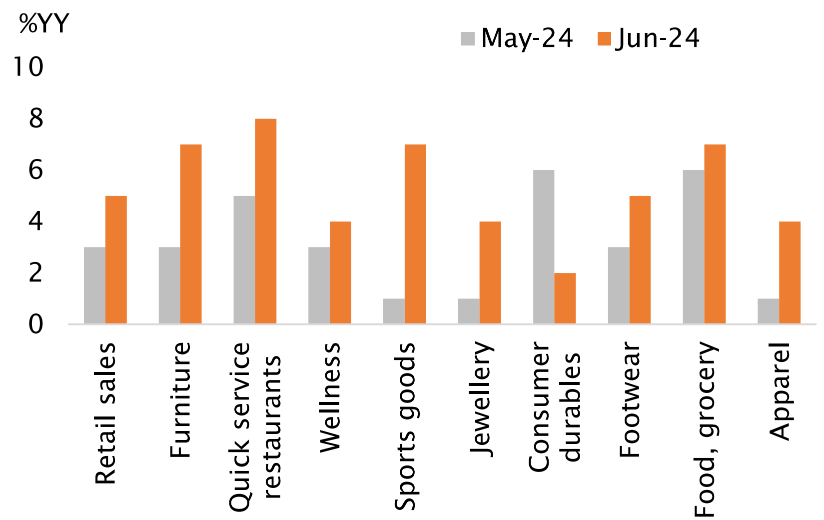
Monthly GST revenue collection



India PMI



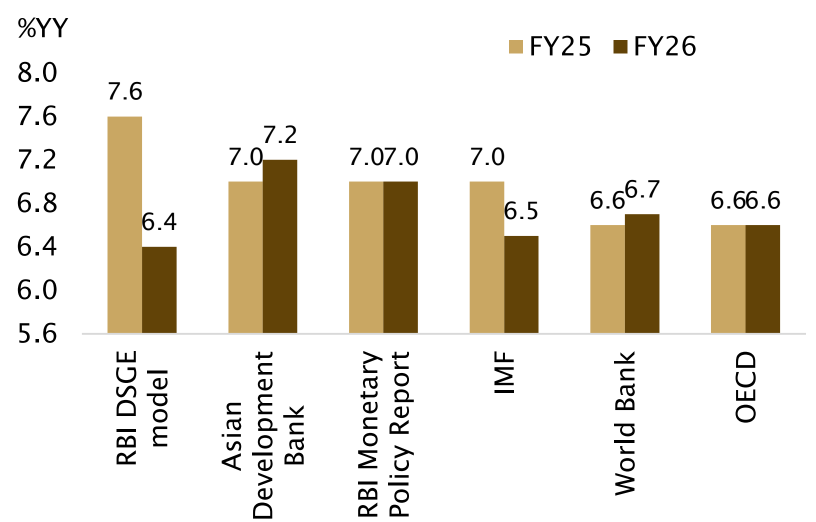
Retail sales growth improved in June



Upward revision to neutral rate implies less space for policy easing

- The RBI's latest Survey of Professional Forecasters pegs median estimate for IIP growth at 5.0%YY in Q1-FY25, which implies growth of 4.1% in June. Base effects is expected to be favorable in June and historical data shows that even marginal month-on-month momentum can push production growth close to 7%, which would take Q1 growth to around 6%. The RBI's latest monthly bulletin's 'State of the economy' article indicates real GDP growth of 7.4%YY in Q1-FY25, which is marginally higher than the MPC's latest forecast of 7.3%.
- For FY25, the MPC raised real GDP growth forecast at its June meeting by 20bps to 7.2%, which is optimistic compared to estimates from leading multilateral agencies, though lower than the RBI's own model estimates.
- Recovery in rural consumption, indicated by improvement in FMCG sales as reported by private research firms, bodes well for consumer-related segments production. Prospects for farm output have improved due to forecasts of an above-normal monsoon, with tractor sales reaching an eight-month high and easing demand for work under MGNREGA. Urban demand remained solid in June, amid growth in retail sales, passenger vehicle sales and air traffic. Consumer demand could be critical to prop up growth in the coming years as the government shifts focus to fiscal consolidation. In the near to medium-term, lagged impact of monetary policy tightening, macro-prudential measures to curb credit growth could weight on consumer spending, while higher input costs could impact production. Any announcements in the Union Budget to support production (such as extending PLI schemes to other sectors) or consumption (by means of higher welfare spending) could support economic activity.
- In RBI's latest monthly bulletin, authors of the 'State of the economy' note, stated that an enduring movement of CPI inflation towards the central bank's 4% target could be sufficient for MPC to consider change in stance but in another article of the bulletin, there was also an upward revision to the estimate of the economy's neutral rate of interest to 1.4-1.9% for Q4-FY24 from the estimate of 1.1-1.3% for Q3-FY22 (revised higher from earlier estimate of 0.8-1.0%), which suggests that the MPC has less space for easing. Considering CPI forecast of 4.5% for FY25 and current policy rate of 6.5% leaves room for 10-60bps cut for the MPC to shift policy towards a neutral setting.

Real GDP growth forecasts for India



DISCLAIMER:

We are committed to providing completely independent views to help our clients reach a better decision. This document is provided for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Nothing in this document should be construed as investment or financial advice, and nothing in this document should be construed as an advice to buy or sell or solicitation to buy or sell the securities of companies referred to in this document. The intent of this document is not in recommendary nature. The recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. Trust Group has not independently verified all the information given in this document. Accordingly, no representation or warranty, express or implied, is made as to the accuracy, completeness or fairness of the information and opinions contained in this document. The Company reserves the right to make modifications and alternations to this statement as may be required from time to time without any prior approval. Trust Group, its affiliates, their directors and the employees may from time to time, effect or have effected an own account transaction in, or deal as principal or agent in or for the securities mentioned in this document. They may perform or seek to perform investment banking or other services for, or solicit investment banking or other business from, any company referred to in this report. Each of these entities functions as a separate, distinct and independent of each other. The recipient should take this into account before interpreting the document. This report has been prepared on the basis of information, which is already available in publicly accessible media or developed through analysis of Trust Group. The views expressed are those of analyst and the Company may or may not subscribe to all the views expressed therein. Neither the Firm, not its directors, employees, agents or representatives shall be liable for any damages whether direct or indirect, incidental, special or consequential including lost revenue or lost profits that may arise from or in connection with the use of the information. This document is being supplied to you solely for your information and may not be reproduced, redistributed or passed on, directly or indirectly, to any other person or published, copied, in whole or in part, for any purpose.

Trust Group

1101, Naman Centre, Bandra Kurla Complex, Bandra (E), Mumbai -400 051, Maharashtra.

Ph: +91 22 4084 5000 • Fax: +91 22 4084 5052 • www.trustgroup.co.in