

Industry

The industrial recovery that started in mid 2002-03 has continued both in terms of Index of Industrial Production (IIP) and Gross Domestic Product (GDP). The IIP-General (IIP-G) and GDP grew by 10.2 per cent and 9.7 per cent respectively in the first quarter of FY 2005-06. Manufacturing did even better by posting a growth of 11.1 per cent and 11.3 per cent respectively for IIP-M and GDP during the same period (Fig I.1). Although there was a dip in IIP growth during July, it bounced back in August by clocking a growth rate of 7.4 per cent for IIP-G and 8.2 per cent for IIP-M. Despite firm and volatile crude oil prices, this growth is noteworthy as it suggests a long term trend. The question we have to ask is, if this kind of growth is possible without labour reforms, what would happen if labour reforms were undertaken?

The buoyancy of the industrial sector is also noticeable in the latest round of the Business Expectations Survey of NCAER. It shows that Business Confidence Index (BCI), which in October 2004 was at 136.0, has jumped to an impressive figure of 146.0 in the month of October 2005. This is the highest level BCI has attained since December 1995. Moreover, the impetus provided by the Budget 2005-06 to sectors such as rural infrastructure, irrigation etc. should further add to the positive outlook. The National Employment Guarantee Programme would also provide some impetus to industrial demand from rural areas.

Industrial Output: Broad Trends

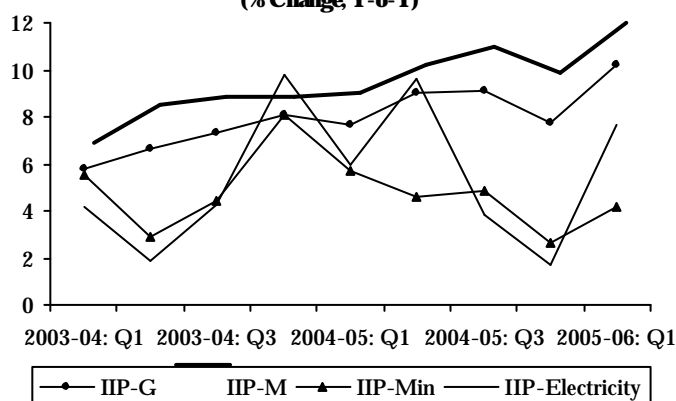
Industrial output in first five months of this fiscal grew by 8.8 per cent as measured by the IIP (Table I.1), which covers manufacturing, mining and electricity. This is 0.8 percentage point higher than the growth recorded in same period in 2004-05. As in the previous years, manufacturing has been the major driver. IIP-M grew by 9.8 per cent in April-August 2005-06 as compared to 8.4 per cent same period last year.

However, the infrastructure sector's performance has been rather lacklustre in the first six months of FY 2005-06. Infrastructure industries, which have a weight of 26.88 per cent in IIP, grew only by 4.4 per cent in April-September this year compared to 5.3 per cent growth in the same period last year (Table I.2).

Coal, cement and steel registered 5.3 per cent, 11.4 per cent and 7.2 per cent

The industrial recovery that started in mid-2002-03 has continued

Fig I.1: Trend in Industrial Growth
(% Change, Y-o-Y)



**Table I.1: Growth of Index of Industrial Production
(Percentage Change, Y-o-Y)**

Sector	2004-05	2004-05 (April-August)	2005-06 (April-August)
General	8.4	8.0	8.8
Manufacturing	9.1	8.4	9.8
Mining & Quarrying	4.4	5.1	2.0
Electricity	5.2	7.8	5.9
Basic Goods	5.5	4.9	7.0
Capital Goods	13.9	13.1	11.8
Intermediate Goods	6.1	8.7	3.2
Consumer Goods	11.7	9.2	15.1
Consumer Durable	14.3	15.4	13.2
Consumer Non-Durable	10.8	7.2	15.8

Source: Central Statistical organisation

growth respectively during this period. However, crude petroleum and petroleum products registered a decline in their production. A fire on the ONGC platform in Bombay High has been mainly responsible for the decline in crude production growth. Electricity generation grew by 4.7 per cent during this period. Last year growth was 7.8 per cent. Both hydel and thermal electricity generation recorded lower growth this year. Hydel electricity generation declined from 22.8 per cent growth in first five months of 2004-05, to 18.1 per cent in same period this year.

Thermal electricity generation also declined from 5.3 per cent to 3.5 per cent in the corresponding periods. The slowdown in thermal electricity generation

growth is mainly due to a shortfall in coal production. Although coal production during April-September period increased by 5.3 per cent, during July 2005, it declined by one per cent over July 2004 and in June it grew only by 3.3 per cent. This resulted in thermal energy growth of (-) 3.7 per cent and 2.8 per cent respectively in June and July 2005.

Meanwhile, the real estate and infrastructure sector projects such as the National Highway Development Programme (NHDP) are driving the growth of the cement and steel sectors. Cement demand is cyclical and slows down in the monsoon season. Cement despatches during April-July 2005 grew by 9.2 per cent and exports during the same period grew

Coal production during April-September 2005 grew by 5.3 per cent

**Table I.2: Performance of Infrastructure Industries
(Percentage Change, Y-o-Y)**

Sector	Weights	2004-05	2004-05 (April-September)	2005-06 (April-September)
Crude petroleum	4.17	1.8	4.3	-4.9
Petroleum products	2.00	4.3	7.3	-0.7
Coal	3.22	6.1	6.3	5.3
Electricity	10.17	5.2	7.8	4.7
Cement	1.99	6.6	4.8	11.4
Steel	5.13	4.8	1.3	7.2
Total	26.88	4.9	5.6	4.4

Source: Ministry of Industry

by 11.3 per cent. Prospects of the cement sector in the short- and medium-term look bright because of the real estate boom and widening of roads under NHDP III. With 4,846 kilometres of all National Highway Authority of India (NHAI) projects under implementation and nearly 7,300 kilometres to be awarded, prospects for the cement sector are good.

Compared to 9.8 per cent growth in 2003-04, the steel sector in 2004-05 could only clock 5.1 per cent growth. However, it is showing a better performance this fiscal — finished steel production grew by 7.7 per cent during April-July 2005-06 compared to 5.3 per cent last year. Although the demand for steel has been guided both by domestic and export demand, the build up of inventory during April and May 2005 in Europe and North America has softened export demand and, consequently, steel prices in the international market. After witnessing a downward trend in steel prices during May, June and July 2005, steel prices started rising again. The WPI of iron and steel in September was back at May 2005 levels. According to the Steel ministry, steel demand is expected to increase to 100 million tonnes by 2020. All big steel plants are in expansionary mode.

Corporate Sector Performance

Corporate sector performance remained good in the first quarter of this financial year. But it declined in the first quarter of FY 2005-06 compared to the first quarter of FY 2004-05. Both topline and bottomline have declined in the first quarter this year. The growth of net sales declined from 21.9 per cent in the first quarter last year, to 16.2 per cent this year (Table I.3).

Profitability, too, has declined. The growth of profit before depreciation and tax (PBDT) declined from 29.3 per cent in the first quarter of 2004-05 to 13.5 per cent in the first quarter of 2005-06. Profit after tax (PAT), which is a better yardstick for measuring financial performance, declined from 39.0 per cent to 21.9 per cent for the same period. Fierce competition among corporates to absorb the rise in input prices, movement of interest rate regime from soft to neutral/hard and, above all, the fringe benefit tax are some of the reasons for this decline in corporate sector profitability.

Use-based Classification

Use-based classification of industrial data shows capital and consumer goods to be the key drivers of industrial growth. During FY 2004-05 capital goods grew by 13.9 per cent. Even in this fiscal for the

Growth of Profit after tax declined from 39.0 per cent in the first quarter of 2004-05 to 21.9 per cent in the first quarter of 2005-06

**Table I.3: Performance of Corporate Sector
(Percentage Change, Y-o-Y)**

	2004-05: Q1	2005-06: Q1
Net Sales	21.9	16.2
Other Income	8.0	3.8
Non Recurring Income	8.4	110.2
PBDIT	14.5	10.4
Interest	-4.5	5.0
PBDT	29.3	13.5
PBT	35.6	16.7
PAT	39.0	21.9

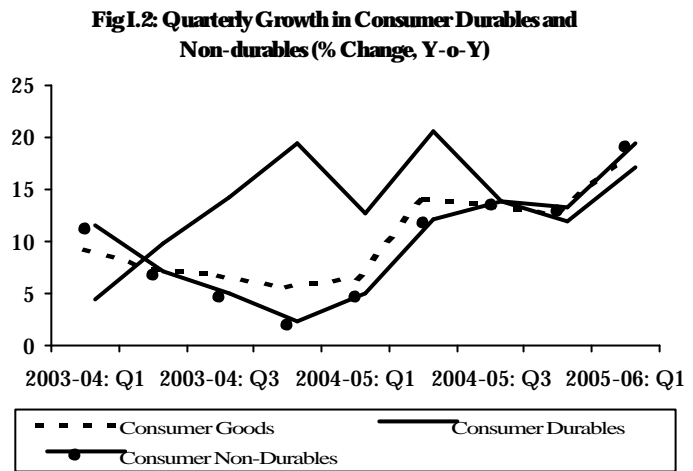
Number of Companies: 3483

Source: CMIE Prowess Database

first five months this sector has clocked a growth of 11.8 per cent (Table I.1). The creditable performance of capital goods sector in 2005-06 is indeed praiseworthy, as it has been attained on a high growth base of 2004-05. Despite high growth base, except for the months of August, its growth has been more than 10 per cent. Growth of machinery and equipment in the first five months slowed down to 8.8 per cent as compared to 11.1 per cent for transport equipment. However, performance of machinery and equipment has been commendable, as this growth is achieved over a high base of 26.5 per cent growth same period last year as compared to 0.7 per cent growth for transport equipment. At disaggregate level, production of furnaces went up by 57 per cent, textile machinery grew by 40.4 per cent in the first five months of this fiscal. Production of boilers, dumpers, broad-gauge covered wagons, and industrial machinery went up by 104 per cent, 43 per cent, 88 per cent and 34 per cent respectively. Even import of capital goods during April-July 2005 grew by 30.4 per cent. Thus, higher domestic production and imports of capital goods implies that investment activity in the economy is buoyant.

The production of consumer goods increased by 15.1 per cent in the first five months of this fiscal, up from 9.3 per cent during the same period last year. Production of consumer durables declined as compared to last year, whereas production of non-durables grew at more than double (15.8 per cent) the growth observed in the same period last year (7.2 per cent).

Except for July, consumer durables growth each month of this fiscal has been in double digits. Some segments of the consumer durable segment that have been doing well during April-August 2005 are: bicycle tyres (39 per cent) and window ACs (57 per cent). On the other hand, the consumer non-durable sector has consis-



tently posted 12 per cent or more growth every month except August 2005 (9.7 per cent). The major drivers of consumer non-durable growth in April-August 2005 were sugar, Indian made foreign liquor, cigarettes, sulphur drug, trimethoprim and hair oil/ayurvedic hair oil. It is heartening to note that the growth momentum of both consumer durable and non-durable segments is continuing in this fiscal as well (Fig I.2).

Basic goods sector grew at seven per cent in first five months of this fiscal up from 4.9 per cent during same period last year. Continued buoyancy of the construction sector is pushing up the growth of this sector. Salt, soda ash, carbon steel, HR sheets and aluminium extrusions are the major segments that are pushing up the growth of the basic goods sector.

Performance of the intermediate goods sector has been very poor. In the first five months of this fiscal, the intermediate goods sector grew by just 3.2 per cent. This is less than 40 per cent of the growth achieved during same period last year (8.7 per cent).

Industrial Output at Two-Digit Level

Only three out of 17 industry groups at the two-digit level showed negative growth in the first five months of this fiscal as compared to five last year (Table

Despite the 27 per cent growth in the production of textile products, the 1.5 per cent decline in exports of textiles and the 16.2 per cent growth in exports of readymade garments in post quota regime is a conundrum

I.4). Textile products (including wearing apparel) showed highest growth of 21.5 per cent in April-August 2005, followed by beverage, tobacco and related products (16.8 per cent), basic metal and alloy industries (16.8 per cent) and other manufacturing industries (16.1 per cent). Basic chemical and chemical products, transport equipment and parts, and cotton textiles are other three sectors that registered double digit growth.

The performance of textile products (including wearing apparel) registered 33.3 per cent, 32.4 per cent and 27 per cent growth respectively in the third quarter of 2004-05, fourth quarter of 2004-05 and first quarter of 2005-06. However, a 1.5 per cent decline in exports of textiles (excluding ready-made garments) and

16.2 per cent growth in exports of ready-made garments in the post-quota dismantling regime is a conundrum. The four-industry group, which registered negative growth in first five months of FY 2004-05 — food products, jute and other vegetable fibre textiles (except cotton), non-metallic mineral products, and basic metal and alloys — posted positive growth during the first five months of this fiscal. However, wood and wood products continue to post negative growth (10.8 per cent in April-August 2004 to 1.5 per cent in April-August 2005). Production of wool, silk and man-made fibre textiles, which grew by 16.4 per cent in April-August 2004, posted a decline of 1.8 per cent in the same period this year. Similarly, metal products and parts, which grew by 8.2 per

**Table I.4: Industrial Performance at Two-digit Level
(Percentage Change, Y-o-Y)**

Two-digit Industries	2004-05	2004-05 (April- August)	2005-06 (April- August)
Food Products	-0.4	-6.4	5.1
Beverages, Tobacco and Related Products	10.8	9.6	16.8
Cotton Textiles	7.5	8.2	10.4
Wool, Silk and Man-made Fibre Textiles	3.5	16.4	-1.8
Jute and other Vegetable Fibre Textiles (Except Cotton)	3.7	-7.8	2.7
Textile Products (Including Wearing Apparel)	19.2	5.7	21.5
Wood and Wood Products, Furniture & Fixtures	-8.5	-10.8	-1.5
Paper and Paper Products and Printing, Publishing and Allied Industries	10.5	4.8	7.6
Leather and Leather and Fur Products	6.8	6.6	4.8
Basic Chemicals and Chemical Products (Except Products of Petroleum and Coal)	14.5	20.0	12.7
Rubber, Plastic, Petroleum and Coal Products	2.4	3.8	3.6
Non-metallic Mineral Products	1.5	-1.2	7.5
Basic Metal and Alloy Industries	5.4	-1.9	16.8
Metal Products and Parts (Except Machinery and Equipment)	5.8	8.2	-3.5
Machinery and Equipment other than Transport Equipment	19.8	26.6	8.8
Transport Equipment and Parts	4.1	0.7	11.0
Other Manufacturing Industries	18.6	12.1	16.3

Source: Central Statistical Organisation

cent in the first five months last year declined by 3.5 per cent this year. On the whole, the data at the two-digit level suggests the broadening and deepening of economic activity across various industrial sectors.

Prospect 2005-06

Industrial growth in the first five months of 2005-06 reflects a continuation of the trend observed last year. Although IIP growth dipped in July, it bounced back in August by registering 7.4 per cent growth for IIP-G and 8.2 per cent for IIP-M. Domestic demand and external demand are driving this growth.

A concern has been voiced that industrial demand is riding on the back of a soft interest rate regime, and as the interest rates harden it will impact industrial growth adversely. High oil prices could also be a major obstacle for sustained industrial recovery. The impact of high oil prices has started being reflected on prices of certain products. However, the strength of oil prices and other prod-

uct prices is getting weaker, mainly due to fierce competition. With the construction boom in the country, demand for iron and steel, and cement is going to remain strong. With other infrastructure projects and 'Bharat Nirman' in place, domestic demand is expected to grow.

As far as external demand is concerned, Indian companies are demonstrating their new competitiveness. Goods export has been registering more than 20 per cent growth consecutively from 2002-03, and in first six months of this fiscal, export growth has been 21 per cent. In the last couple of years this was achieved in spite of the strengthening rupee. With the rupee depreciating this year, Indian manufactured products will become more competitive in the global market.

In spite of this encouraging picture, there are a few downside risks as well coming from the volatile international oil prices and the fast emerging infrastructure bottlenecks.

Volatile international oil prices and fast emerging infrastructure bottlenecks are the major downside risks for industrial growth