Drivers of Poor Manufacturing Growth

Other than high raw material cost, high interest rates also took toll on the growth of capital goods.

THE FISCAL YEAR (FY) 2013–14 was marked with slow growth and high inflation. Besides, the year saw the rupee plummeting to its record low level against the United States dollar. The current levels of inflation were largely driven by the spurt in prices of primary food and non-food articles.

Another threat to the overall inflation came from the intermediate goods. This accounted for over 30 per cent of the total inflation since the beginning of FY 2013–14 (Table I.1). This category posted double-digit inflation during the second quarter of FY 2013–14, marking its highest at 10.1 per cent in August 2013. The intermediate goods feed into the production of consumer durables and capital goods as important raw materials. Hence, their high prices i.e. the increasing cost of inputs adversely affect the production of consumer durables and capital goods in a direct fashion. The correlation of rising intermediate goods inflation and falling production is evident in Figure I.1, with the former rising and the latter, consumer durables and capital goods growth rates, falling.

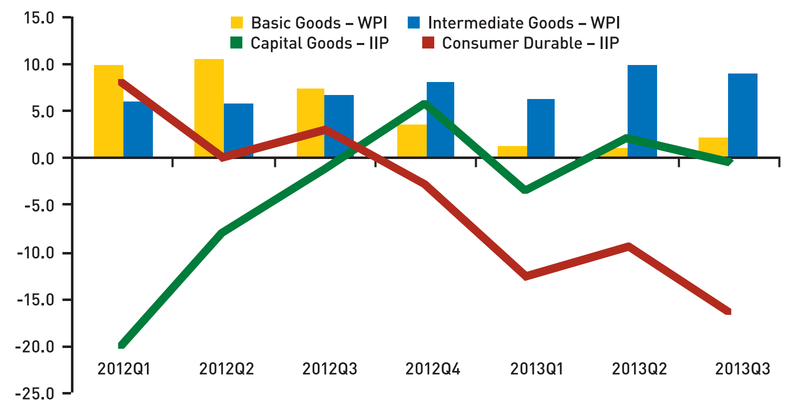
The growth of consumer durable goods, an indicator of consumer spending, has been in the negative territory since the fourth quarter of FY 2012–13. It showed a contraction of 16.5 per cent in the third quarter of FY 2013–14. Barring a few months, growth in capital goods, an investment barometer, has also been shrinking for long since 2012. While weak consumer and investment sentiments and high cost of credit have contributed to the poor performances of durable and capital goods, the high cost of raw materials added further downward pressure.

Table I.1: Contribution to Overall Inflation (per cent)

	FY2012–13Q1	FY2012–13Q2	FY2012–13Q3	FY2012–13Q4	FY2013–14Q1	FY2013–14Q2	FY2013–14Q3
Food and Non-food articles	29.21	28.95	29.87	36.49	37.78	48.97	49.91
Basic Goods	31.22	31.98	24.45	12.68	6.77	4.19	7.90
Capital Goods	2.24	2.53	2.55	2.83	4.47	2.68	2.70
Intermediate Goods	19.64	17.49	22.41	28.90	30.79	35.37	31.00
Consumer Durable	5.80	4.52	3.74	3.49	1.59	0.44	1.15
Consumer Non-durable	11.89	14.53	16.98	15.61	18.61	8.36	7.34
Overall	100.00	100.00	100.00	100.00	100.00	100.00	100.00

Source: Office of the Economic Advisor, Authors' computation.

Figure I.1: Correlation of High Raw Material Price and Production of Consumer Durables and Capital Goods



Sources: Office of the Economic Advisor, CSO, Authors' computation.

These findings have been compared with the quarterly data for a balanced panel of 2,151 manufacturing firms, extracted from the Centre for Monitoring Indian Economy's Prowess database. The year-on-year growth of net sales of capital goods has been in the red zone since the second quarter of FY 2012–13 and it has also been sliding fast in the case of consumer durables. Other than high raw material cost, high interest rates also took toll on the growth of capital goods. The Prowess data reveal that the cost of credit or interest expenses as per cent to total expenses has been increasing in the case of both capital goods and consumer durables, while the other use-based categories were not much impacted. Going forward, with inflation showing signs of easing and with a pause in fiscal tightening, industry is expected to gain momentum in the next fiscal year.