Press Release

Six month high Core Sector print masks underlying challenges

Coal shortages may impact core sector output in the near term

02-June-2022

The output of eight core sectors rose to a six-month high of 8.5% YoY in Apr-22 from 4.9% in Mar-22 primarily on account of the favourable statistical base related to the second Covid wave last year. On sequential basis, in line with seasonal phenomenon, the index contracted by 9.5% MoM in Apr-22 from an expansion of 15.2% in Mar-22. While it is not appropriate to assess the performance of the core sector on a sequential basis particularly in the month of April (the production levels usually drop after a year-end run up in Mar-22), barring electricity, all other sectors recorded a contraction with output of coal, fertilizers, steel and cement recording a double-digit contraction. This clearly highlights the challenges that are emerging from raw material supply constraints apart from a spurt in their prices. That said, the overall contraction, however, was lower than the seasonal average of 11.0% recorded in the last three years (FY20 is excluded on account of the pandemic). The marginal increase in electricity generation over Mar-22 primarily reflects the higher power demand from the residential segment due to the severity of the summer in the current year.

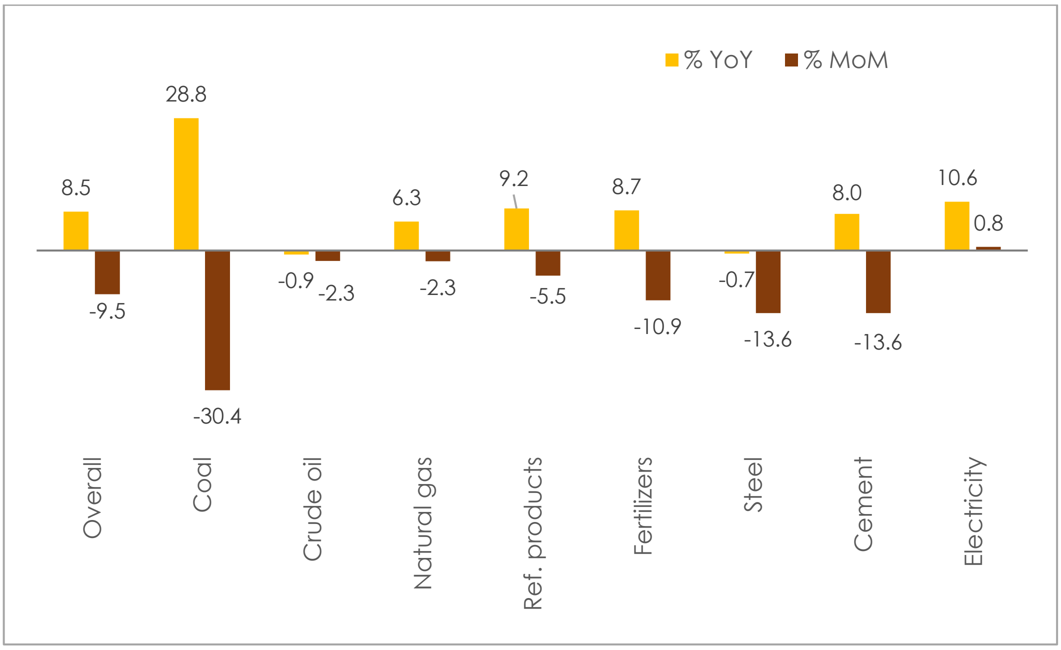
Domestic coal production, nevertheless, continues to be inadequate given the spurt in demand from the power sector particularly in the context of the sharp rise in global coal prices and a substantial drop in imports. As per the latest CEA report, the coal inventory stands at just 21.6 mn tonnes, only 35% of the required stock levels. With onset of monsoon, the mining activities will further dampen and will also hamper transportation of coal from mines to power stations thereby weighing on the electricity output. An inadequate coal stock at the power plants before monsoon could lead to yet another power crisis as was faced in the second quarter of last year. However, to avoid a fuel shortage and create buffer stocks, the government has initiated negotiations with a few countries like Russia, Australia and Indonesia to help Coal India Limited import coal at a discounted rate ahead of the onset of monsoon, which may ease the heightened supply pressures in power and other end use sectors.

The heightened activity in the infrastructure sector led steel and cement production to remain strong in FY22, with the sectors recording an expansion of 4.0% and 4.8% respectively as compared to their pre-pandemic levels i.e. FY20. However, the impact of significant increase in commodity prices such as that of coal and the challenges in imports of coking coal amid Russia-Ukraine standoff has put pressure on steel output and has started manifesting in the monthly production levels. That said, over the longer term of 1-3 yrs, we expect government's initiatives in the form of PLI scheme for the steel sector and its focus on infrastructure segment to play a pivotal role in driving steel and cement output.

Overall, the spurt in prices of key commodities and importantly, the fresh supply chain bottlenecks induced by the continuing Russia-Ukraine conflict are likely to slow down the revival in the industrial and core sector output in the near term. From growth perspective, we expect GDP growth for FY23 at 7.2% with support to emerge from the capital expenditure focused government expenditure, expectation of a normal southwest monsoon and the benefits from the full unlocking of the economy post the Omicron wave with more than 70% of population fully vaccinated.

Annexure

Chart 1: Performance of core sector growth in Apr-22



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