Press Release

Base factor pushes up IIP in Apr-22 to an 8-month high

Higher commodity prices to weigh on industrial production in FY23

10 June 2022

India's Index of Industrial production (IIP) moved to an 8-month high of 7.1% YoY in Apr-22 from an upwardly revised print of 2.2% in Mar-22 (earlier 1.9%). On sequential basis, in line with seasonal phenomenon the index contracted by 9.2% MoM in Apr-22 from an expansion of 12.9% in Mar-22. While it is not appropriate to assess the performance of IIP on a sequential basis particularly in the month of April (the production levels usually drop after a year-end run up in Mar-22), all the other sectors barring electricity, recorded a contraction with mining followed by capital goods, consumer goods, and construction goods recording a significant double-digit contraction.

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 drop in imports. This is clearly reflected in the mining output which contracted significantly by 19.7%, albeit lower than the seasonal average of 22% usually recorded in the month of April. 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 advised Coal India Limited to import coal at a discounted rate ahead of the onset of monsoon, which could likely help to improve coal availability to the thermal power plants.

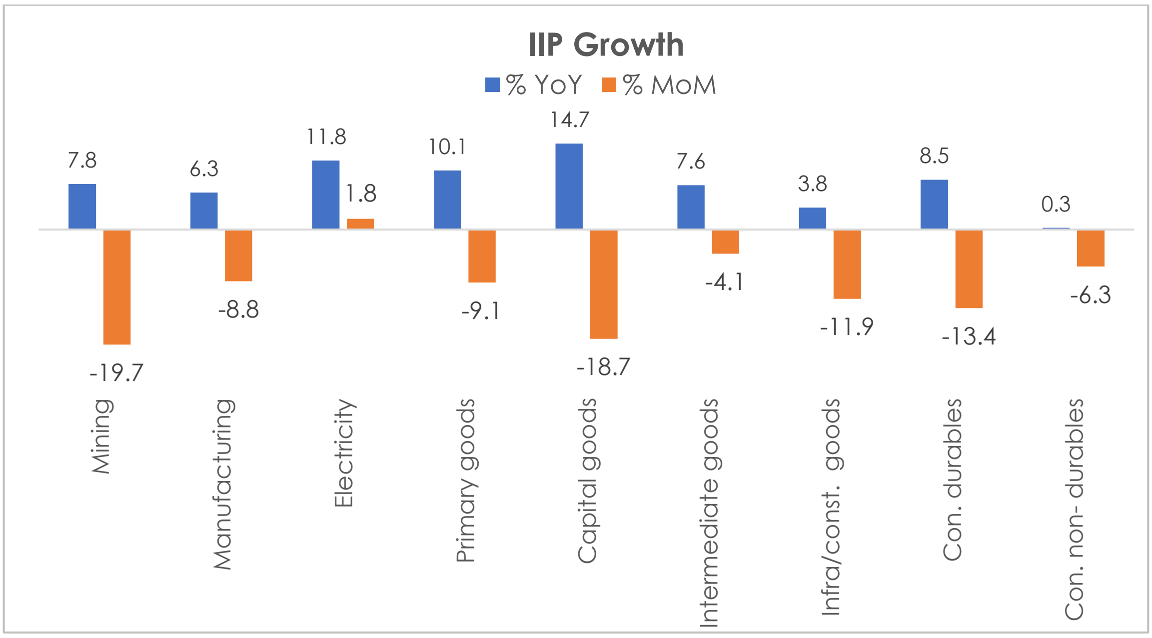
Despite improvement in capacity utilization levels (as per RBI survey the early results for capacity utilization stands at 75% in Q4 FY22), the overall trend in manufacturing segment since Sep-21 has remained subdued reflecting incomplete demand revival and supply shortages in some sectors. Nevertheless, on an encouraging note, manufacturing sector has recorded a lower contraction of 8.8% in Apr-22 as compared to the average contraction of 13% recorded in the past 4 years (excluding FY21 on account of the pandemic).

On the use-based side, demand for consumer goods (including consumer durables and non-durables) is likely to remain subdued in the near term reflecting an uneven demand recovery especially in the rural sector which has been impacted by high inflation in commodities and its derivatives. However, prospects of a normal monsoon and recent hike in MSP could help support rural demand marginally. On the other hand, production of infrastructure and construction goods is likely to find support from the capex focused government spending.

Overall, the spurt in prices of key commodities and importantly, the fresh supply chain bottlenecks triggered by the continuing Russia-Ukraine conflict are likely to slow down the revival in the industrial output in the near term. From growth perspective, we have retained GDP growth for FY23 at 7.5% with moderate downside risk. While the global growth slowdown and the higher inflation will be a dampener to the domestic economic recovery, we expect some support to emerge from the capital expenditure focused government expenditure, expectation of a normal southwest monsoon and the benefits to the service sector from the full unlocking of the economy with more than 70% of population fully vaccinated.

Annexure

<u>Chart 1: IIP growth jumps to an 8-month high on account of favorable base</u>



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