

# IIP & CPI

## UPDATE REPORT



**13th July, 2017**

**Research Analyst (Economy)**

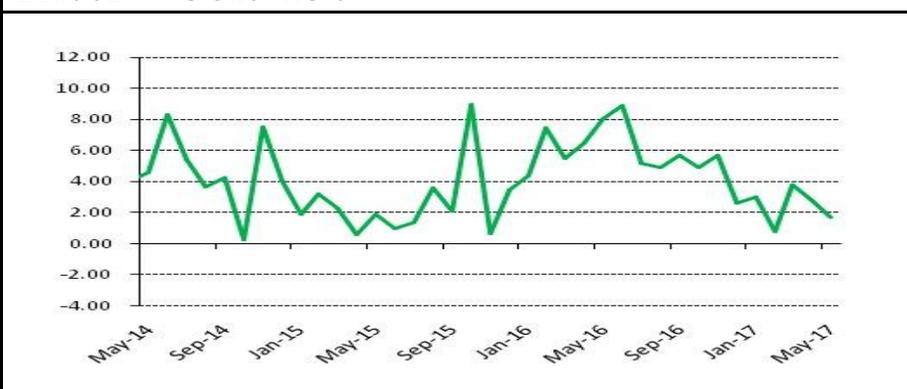
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Pulled down by Manufacturing, Mining and Capital goods the index of Industrial Production grew by 1.7% YoY in May compared with an annual growth of 2.8% for the previous month.

India's Industrial Production growth slowed to a three month low in May 2017. Pulled down by Manufacturing, Mining and Capital goods, the index of Industrial Production grew by 1.7% YoY in May compared with an annual growth of 2.8% for the previous month. During the month, Mining witnessed a sharp slowdown, contracting 0.9% YoY from a growth of 3.2% YoY in April. Manufacturing activity also slowed to 1.2% YoY in May from 2.3% YoY in April. In manufacturing some of the major sectors like auto components and commercial vehicles have shown de-growth during the month. Electricity sector was one of the few to witness an uptick in activity, growing by 8.7% YoY in May from 5.4% YoY in April. On the use based front, Consumer durables and Capital Goods registered de-growth in May. On the other hand Consumer non-durables continues to remain on a robust footing.

**Exhibit 1: IIP Growth Trend**



Source: Bloomberg

In Manufacturing sector, 11 out of 23 industry groups have shown negative growth.

## Manufacturing Sector

In Manufacturing sector, 12 out of 23 industry groups have shown positive growth during the month of May 2017. Industry group 'Manufacture of pharmaceuticals, medicinal chemical and botanical products' has shown the highest positive growth of 24.5% YoY followed by 24.4% YoY in 'Other manufacturing' and 11.8% YoY in 'Manufacture of other transport equipment'. On the other hand, the industry group 'Manufacture of beverages' has shown the highest negative growth of 16.5% YoY, followed by -15.1% YoY in 'Manufacture of motor vehicles, trailers and semi-trailers' and -15.0% YoY in 'Manufacture of electrical equipment'.

## Use-based Sectors

Among the use-based segment, production of consumer durables sector declined by 4.5% YoY, after registering a fall of 5.4% YoY in April and Capital Goods production declined by 3.9% YoY, after registering a de-growth of 2.9% YoY last month. Some important items which were showing high positive growth during May include Digestive enzymes and antacids (incl. PPI drugs) (90.5% YoY), 'Textile machinery' (51.8% YoY), 'Meters (electric and nonelectric)' (48.7% YoY), 'Jewellery of gold (studded with stones or not)' (36.7% YoY), 'Industrial Valves of different types -

safety, relief and control valves (nonelectronic, non-electrical)' (32.8% YoY), 'Telephones and mobile instruments' (29.2% YoY), 'Aluminium Billets/ingots' (23.6% YoY) and 'Tea' (21.8% YoY). Important items that have registered high negative growth include 'Air filters' (-63.7% YoY), 'Shelled cashew kernel' (-63.3% YoY), 'Axle' (-47.0% YoY), 'Plastic jars, bottles and containers' (-41.1% YoY), 'Kerosene' (-40.6% YoY), 'Rice (excluding basmati)' (-36.1% YoY), 'Tooth Paste' (-33.8% YoY), 'API & formulations of vitamins' (-32.0% YoY), 'Commercial Vehicles' (-26.5% YoY) and 'Beer & other alcoholic liqueurs other than wines' (-24.9% YoY).

**Exhibit 2: IIP Growth Table**

Particulars	May-17 yoy (%)	Apr-17 yoy (%)	Apr-May FY18 yoy(%)	Apr-May FY17 yoy (%)
Industrial Production	2.7	-0.1	0.6	2.7
Manufacturing	2.3	-1.7	-0.2	2.5
Mining	5.3	5.5	1.4	2.2
Primary Goods	3.4	3.1	3.3	8.4
Intermediate Goods	0.7	4.2	2.4	2.3
Consumer Durable	-4.5	-5.4	-5.0	14.3
Consumer Non Durable	7.9	8.4	8.2	6.3
Infrastructure Goods	0.1	5.2	2.5	4.2
Capital Goods	-3.9	-2.9	-3.4	11.1

Source: Bloomberg

## Consumer Price Inflation

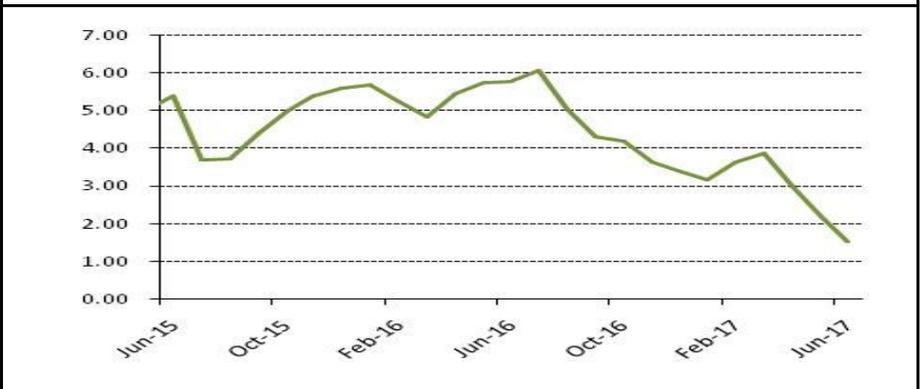
**Consumer Price Index (CPI) based Inflation fell sharply to 1.54% YoY in June 2017 against 2.18% YoY in May 2017.**

India's Consumer Price Index (CPI) based inflation fell sharply to 1.54% YoY in June 2017 against 2.18% YoY in May 2017. However, it is likely to be short-lived. Increase in House Rent Allowance (HRA) under the Seventh Central Pay Commission (CPC) alone is likely to push up Inflation by about 100bps. So, inflation is likely to be above the Reserve Bank of India's (RBI) 4.5% YoY forecast in 2HFY18. The RBI in its recent policy statement has lowered the range for inflation trajectory for FY18 sharply to 2-3.5% for H1 and 3.5-4.5% YoY for H2.

Slowdown in inflation number was largely driven by soft food prices and favorable base. Food inflation slowed to -1.17% YoY in June 2017 against -0.2% YoY in May. Within the food category, vegetables inflation decreased to -16.53% YoY and that of pulses and products to -21.92% YoY. On the other hand, the protein rich meat and fish turned costlier as the inflation spiked to 3.49% YoY in June from 1.87% YoY in May.

During June 2017, Core CPI inflation also slowed to 3.9% YoY from 4.3% YoY in May. Slowdown in core prices was broad based. All the major categories, such as housing, clothing and services witnessed a slowdown in prices. Inflation in clothing and footwear slowed to 4.17% YoY in June from 4.4% YoY in May, Inflation in housing fell to 4.7% YoY from 4.8% YoY in the previous month while the fuel and light category witnessed a sharper slowdown, with the reading easing to 4.54% YoY in June from 5.46% in May.

**Exhibit 3: CPI Trend**



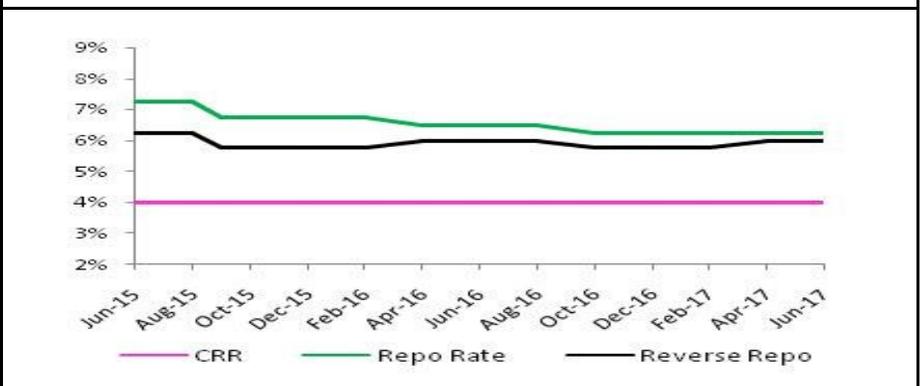
Source: Bloomberg

## Outlook

The slowdown in industrial growth is broad based. Revival of investment demand remains an area of concern as reflected in the steep decline of the Capital Goods sector. Moreover, de-stocking and inventory control due to GST impacted growth during the month of May. June is likely to be worse due to a possibly stronger GST-related adjustment. Manufacturing Purchasing Manager's Index (PMI) data is also indicating the same. Manufacturing PMI dropped to 50.9 in June from 51.6 the previous month. During June, growth of total orders eased to a four-month low, with the intermediate goods category being the key source of weakness. This further underlines the need for major reforms to improve the investment climate. While bumper agricultural output on account of normal monsoons is likely to support Consumer non-durables growth, Consumer durables may continue to see headwinds.

On the other hand, inflation fell sharply in June 2017 but it is likely to be short-lived. Increase in House Rent Allowance (HRA), rise in minimum support prices, farm loan waivers and base effect will contribute to the pick-up in Inflation going forward. So, we think Inflation will be above the RBI's 4.5% YoY forecast in 2HFY18 and August policy meeting is likely to witness no rate cut.

**Exhibit 4: Interest Rate Trend**



Source: Bloomberg



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Stock Recommendation	Expected absolute returns (%) over 12 months
Strong Buy	>20%
Buy	between 10% and 20%
Hold	between 0% and 10%
Sell	0 to <-10%
Neutral	No Rating

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