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Note Released: 12-Nov-07

India Econ Flash

**September Industrial Production:
Below expectations at 6.4%, with consumer durables contracting
7.6%**

Industrial Production Growth — Forecasts and Actual (Percent)

Event	Actual	Citigroup Forecast	Consensus	Previous Data (Aug)	Previous Data(Jul)
Sept Industrial Production	6.4	9.7	9.9	10.7	7.5

Source: CSO, Bloomberg, and Citi

- **Industrial production rose 6.4% in September.** This was below expectations as well as the 10.7% growth recorded last month and 12.0% last Sept. While sectoral trends in industrial production have been choppy this fiscal (e.g. mining was up 15% last month), the slowdown in Sept is largely due to a contraction in consumer durables. On a cumulative basis, industrial growth during 1HFY08 was 9.2% v/s 11.1% last year.
- **Key Highlights:** 1) Similar to trends in recent months, growth continues to be investment led with capital goods up 18.6% while the consumer goods sector contracted by 0.6%. This is a result of a slowdown in both non-durables (2.2%) as well as the interest sensitive durables sector (-7.6%). 2) While growth in mining came in at 6%, electricity slowed to 4.5% v/s the 8.3% average in the first five months of this year. 3) Wood products remained high at 72%.
- **Monetary Policy Implications:** If dollar inflows remain strong, we expect the CRR to continue to be used as a tool to absorb liquidity. But given the slowdown in loan growth coupled with inflation likely to remain below 5% (even assuming a 10% domestic fuel price hike), we expect policy rates (repo and reverse repo) to be lower by 1QFY08.
- **Maintain our 9.3% GDP estimate for FY08:** Due to the impact of higher rates, our numbers have incorporated a deceleration in industrial activity from 11% in FY07 to 10% in FY08 currently. Given current trends in industrial growth, this may appear optimistic. But we are maintaining our 9.3% GDP estimate given that agriculture could surprise on the upside while services remain buoyant. Key risks remain a US recession and domestic politics.

KEY DATA REVISIONS for Aug

- Overall IP unchanged at 10.7%**
- Internal Changes include:**
- Mining revised downward from 17.1% to 15.4%**
- Basic goods revised from 13.3% to 12.8%**
- Consumer durables revised upward from -6.2% to -5.8%**
- Non Durables revised from 3.2% to 2.6%**

Trends in Industrial Production (% YoY)

	WTS	Apr-07	May-07	Jun-07	Jul-07	Aug-07	Sep-07	Sep-06	Apr-Sept FY08	Apr-Sept FY07
Sectoral Classification										
Mining	10.5	2.6	3.8	1.5	3.7	15.4	6.0	4.3	5.3	3.1
Manufacturing	79.3	12.4	11.3	9.7	7.9	10.5	6.6	12.7	9.7	12.3
Electricity	10.2	8.7	9.4	6.8	7.5	9.2	4.5	11.3	7.7	6.6
General	100	11.3	10.6	8.9	7.5	10.7	6.4	12.0	9.2	11.1
Use-based Classification										
Basic goods	35.5	8.6	10.3	9.2	8.8	12.8	6.7	11.5	9.4	8.8
Capital goods	9.7	10.9	22.4	23.1	11.9	30.0	18.6	9.5	19.6	17.5
Intermediate gds	26.4	10.6	8.8	8.6	6.5	13.1	9.3	13.8	9.5	10.9
Consumer gds	28.4	14.7	8.7	3.6	5.7	0.2	-0.6	12.1	5.3	11.5
Durables	5.1	2.4	-0.7	-3.6	-2.5	-5.8	-7.6	11.8	-3.2	15.2
Non-durables	23.3	18.7	12.1	6.3	8.7	2.6	2.2	12.2	8.4	10.2

Source: CSO

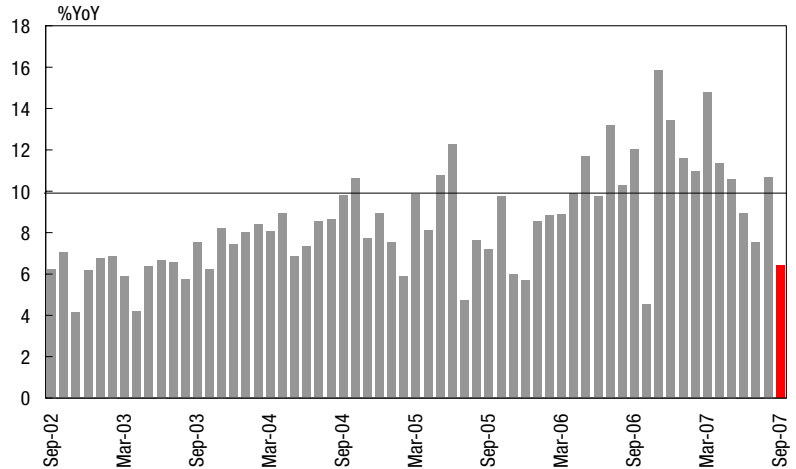


Charting Trends in Industrial Production

Industrial Production – Impacted by higher rates

- Industrial production slowed to 6.4% in September, lower than expectations. On a cumulative basis, industrial growth during Apr-Sept was up 9.2% v/s 11.1% last year.
- Although trends across most segments remained on track, the slowdown was primarily due to a contraction in consumer durables; a result of monetary tightening earlier in the year
- Looking ahead, we expect trends in production to recover, given our view that policy rates could be eased early next year. Our GDP estimate remains unchanged at 9.3% for FY08.

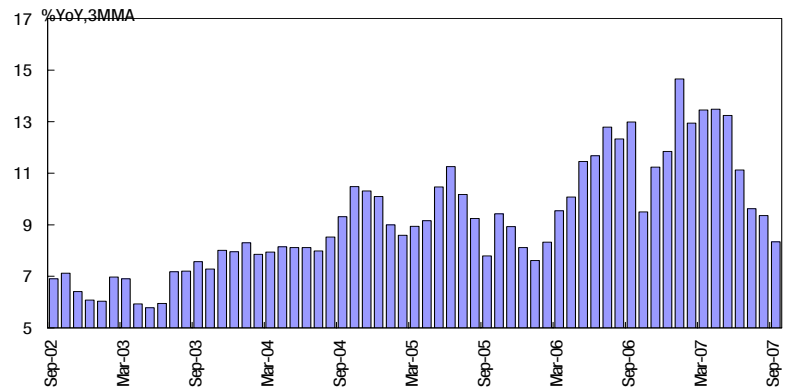
Monthly trends in Industrial Production (%YoY)



Manufacturing – Wood remains the Outlier

- Trends were lower than in previous months. Growth was up 6.6% in Sept07 v/s 12.7% last Sept.
- On a sectoral basis, 15 of 17 industry groups showed positive growth. Trends were led by basic metals and alloys (+14%), leather products (+9%), and petroleum and coal products (+7.7%). Wood and wood products remain an outlier, up 72.5% in the month.
- Two sectors that saw negative growth were food products (-1.5%) and transport equipment (-1.6%)

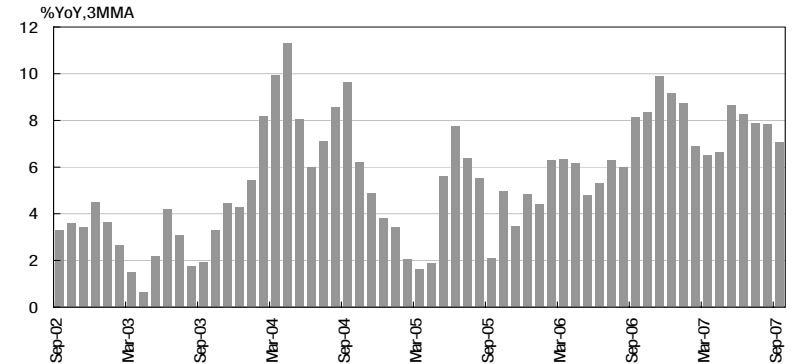
Trends in Manufacturing (%YoY, 3mma)



Electricity – Future Looks OK

- Trends in electricity, which had picked up in recent months, also posted slower growth; up 4.5% in Sep07 vs. vs. 11.3% in Sept06. However, on a cumulative basis, growth was up 7.7% during 1HFY08 vs. 6.6% during the same period last year
- Looking ahead, we expect an uptrend in this segment; as efforts to bridge India's acute power shortage come underway. This should also help spur construction and infrastructure development.

Trends in Electricity (%YoY)



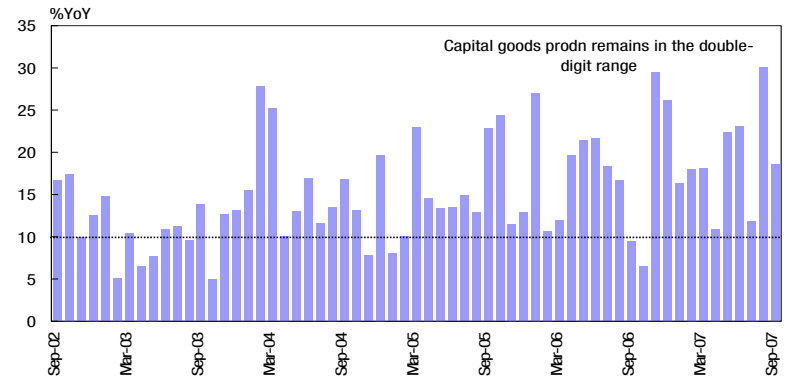
Source: CSO,



Capital Goods – Strong Growth Continues

- Capital goods production remained encouraging, up 18.6% in Sept07 v/s 9.5% last year. On a cumulative basis, growth during 1H FY08 was up 19.6% v/s 17.5% last year.
- As the government's renewed thrust on infrastructure continues, we expect the capex upturn to continue. The Planning Commission has estimated infrastructure investment to the tune of US\$492bn over the 11th Plan period; which should boost growth in the sector.

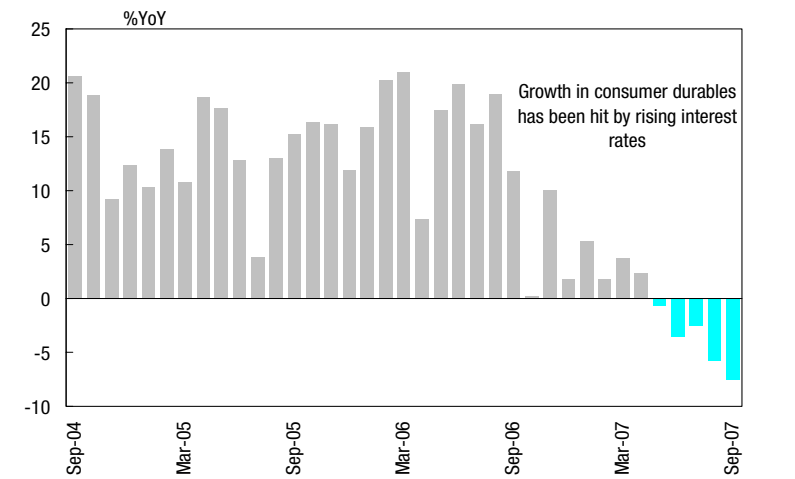
Monthly trends in Capital Goods (%YoY)



Consumer Durables – The Key Culprit

- Consumer durables have been a key reason behind the slowdown in overall production.
- Durables, which have a weight of 5.1% in the overall index and include telephone instruments, two wheelers, autos, and transport equipment; contracted by 7.6% in Sept07 vs. 11.8% in Sept06.
- While higher interest rates could be a key reason for the dip, negative growth also suggests that its components may need to be revised to keep pace with technological change. (See <http://www.financialexpress.com/news/Nothing-durable-about-it/232327/0>)

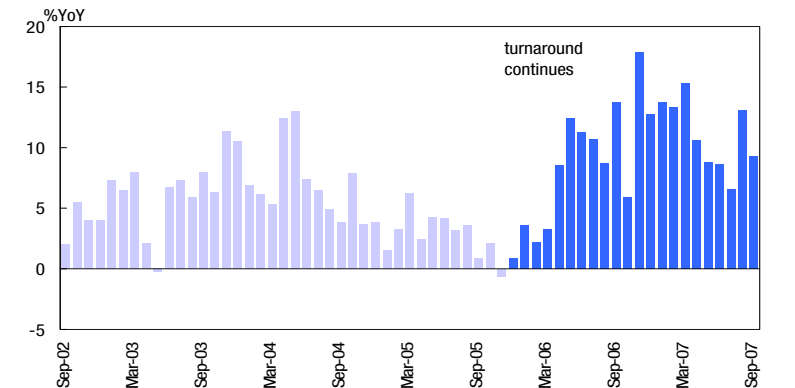
Trends Consumer Durables (% YoY)



Intermediate Goods- growth is still healthy

- Intermediate goods production continued to post healthy growth- a continuation of the turnaround seen since 2005 (growth was up 9.5% during 1HFY08, vs. 10.9% during the same period last year).
- The sustained turnaround in intermediate goods suggests an uptrend in its components, which include cotton yarns, filaments, pipes, auto ancillaries, LPG and natural gas, and polyester fibers, paints and varnishes

Trends in Intermediate Goods (%YoY)



Source: CSO



Appendix: Manufacturing Classification – Detailed Breakdown

Break-Up of Manufacturing (% YoY)

	Wts	May-07	Jun-07	Jul-07	Aug-07	Sept-07	Sept06	Apr-Sept FY08	Apr-Sept FY07
Manufacturing	79.4	11.3	9.7	7.9	10.5	6.6	12.7	9.7	12.3
Food Products	9.1	24.8	1.3	-4.1	1.4	-1.5	12.2	13.3	1.9
Beverages, Tobacco & Related	2.4	6.5	9.8	6.7	8.1	4.8	17.0	8.3	14.2
Cotton Textiles	5.5	6.9	8.1	5.1	3.7	5.1	14.8	6.1	12.8
Wool, Silk, Manmade fibres	2.3	10.9	5.0	6.9	4.8	7.0	4.6	5.1	6.7
Jute, Veg, and Fibre Textiles	0.6	40.4	35.2	16.1	9.5	4.7	0.2	18.9	-0.3
Manf of Textile Prod	2.5	9.9	14.6	3.6	-2.1	1.3	5.1	3.4	14.9
Wood, Wood Products	2.7	132.8	103.9	21.1	62.2	72.5	10.6	78.8	-0.1
Paper, Prod, Printing, Pub.	2.7	0.0	2.3	-4.6	4.2	3.6	9.2	1.1	8.1
Leather and Leather Products	1.1	5.7	7.7	4.2	7.0	9.0	4.3	7.8	-5.2
Basic Chem ,Chemical Products	14.0	5.9	4.3	11.7	9.2	5.4	11.1	7.8	10.5
Rubber, Plastic, Petro, Coal Prod	5.7	9.4	9.3	6.4	19.0	7.7	16.4	12.0	10.9
Non-Metallic Mineral Products	4.4	6.7	4.0	9.2	11.9	6.7	17.7	8.3	13.7
Basic Metal and Alloy Industries	7.5	21.1	21.1	17.5	19.1	14.0	20.3	18.5	19.4
Metal Products and Parts	2.8	8.4	-7.7	-5.1	-2.6	4.3	11.7	-0.8	5.0
Machinery and Equipment	9.6	22.8	18.6	7.7	10.0	4.4	16.9	10.9	16.3
Transport Equipment and Parts	4.0	-0.1	0.8	-3.0	10.6	-1.6	12.3	1.7	17.7
Other	2.6	-5.0	32.5	11.9	21.8	27.1	-9.2	12.4	15.1
Mining	10.5	3.8	1.5	3.7	15.4	6.0	4.3	5.3	3.1
Electricity	10.2	9.4	6.8	7.5	9.2	4.5	11.3	7.7	6.6
General	100	10.6	8.9	7.5	10.7	6.4	12.0	9.2	11.1

Source: CSO

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