

INDIA

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India Economics

September Industrial Production Beats Expectations, but Capital Goods Data Is Puzzling

Industrial Production Growth — Forecasts and Actual (Percent)

Event	Actual	Citigroup Forecast	Consensus	Previous Data (Aug)*	Previous Data (Jul)
Sept Industrial Production	11.4	9.5	9.8	9.9	12.7

*Aug General Index revised upward from 9.7% to 9.9% , June Index revised from 9% to 9.7% Source: CSO, Bloomberg, and Citigroup

- **Sept Industrial Production beats expectations:** Industrial production in September'06 rose 11.4%, beating our as well as consensus expectations. Growth was led by double-digit growth in manufacturing and electricity, up 12% and 11.3% respectively, and a turnaround in mining (+3.9% vs. a contraction in August). On a cumulative basis, growth during Apr.-Sept. '06 was 10.9% as compared with 8.5% seen last year.
- **Key Highlights include:** (1) Seventh consecutive month of double-digit growth in **manufacturing** (2) A 10-year high in **intermediate goods** production (which include paints, yarn, filaments, pipes and auto -ancillaries) up 14.7% - the highest since Nov. '97 ; (3) Growth in **capital goods** decelerating to 2.2% from 15.2% seen earlier this year. This appears to be a bit of an anomaly given the strong order backlogs of the engineering companies
- **Maintain our macro forecasts for FY07:** We maintain our positive stance on the economy and retain our full-year FY07 GDP estimate of 8.3%, led by industry (9.2%), services (9.9%) and agriculture (3%). While we expect the RBI to hike its reverse repo rate once more this fiscal, key risks to our outlook remain politics and rates rising more than 100bps

KEY DATA REVISIONS

Aug. General Index revised upward from 9.7% to 9.9%

June Index revised up from 9% to 9.7% %

Trends in Industrial Production (% YoY)

	WTS	Apr-06	May-06	Jun-06	Jul-06	Aug-06	Sept-06	Apr-Sept FY07	Apr-Sept FY06
Sectoral Classification									
Mining	10.5	3.4	2.9	4.7	4.8	-1.2	3.9	3.1	1.1
Manufacturing	79.3	11.0	13.3	10.7	13.8	11.4	12.0	12.1	9.5
Electricity	10.2	5.9	5.0	4.9	8.9	4.1	11.3	6.6	4.8
General	100	9.9	11.7	9.7	12.7	9.9	11.4	10.9	8.5
Use-based Classification									
Basic goods	35.5	9.3	9.1	8.5	9.8	4.8	11.3	8.8	6.2
Capital goods	9.7	19.6	21.4	21.6	16.1	13.9	2.2	15.2	15.6
Intermediate gds	26.4	8.5	12.5	11.2	9.5	8.4	14.7	10.8	3.1
Consumer gds	28.4	8.9	10.5	6.1	17.3	15.0	12.5	11.6	13.4
Durables	5.1	7.4	17.5	19.9	18.6	19.7	12.6	15.9	13.4
Non-durables	23.3	9.4	8.2	1.8	16.9	13.2	12.5	10.1	13.4

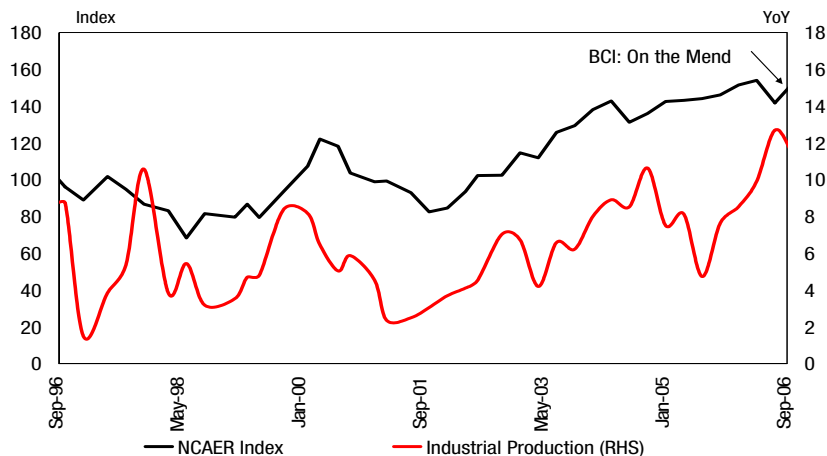
Source: CSO

Charting Trends in Industrial Production

Industrial Production Remains Buoyant

- Industrial Production in Sept. was up 11.3%, beating ours as well as consensus expectations. Growth in Sept. was due to double digit growth both in manufacturing and electricity.
- Interestingly, NCAER's Business Confidence Index also posted an increase of 7.6% for the quarter. Strong data on industrial production thus supports the positive economic sentiment
- Going forward, we expect industrial growth to average 9% in the coming months and maintain our view that the RBI will hike the reverse repo rate once more this fiscal

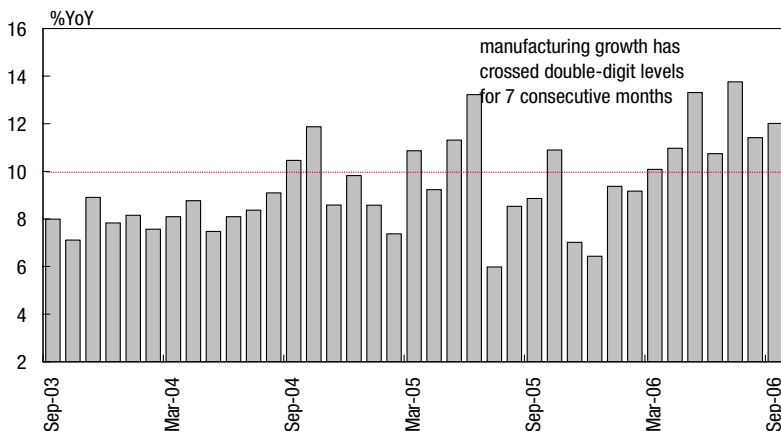
Trends in Industrial Production and the Business Confidence Index (%YoY)



Manufacturing – Double-Digit Growth continues

- Manufacturing sustained double-digit levels for the seventh consecutive month, up 12% in Sept.
- Key components that recorded strong growth within manufacturing include beverages and tobacco (+19.8%), basic metals (+19.8%), rubber, petroleum and coal products (+15.3%), non-metallic minerals (16.75) and cotton textiles (+14.5%)
- Surprisingly, textile products, including ready-mades, witnessed a slowdown to 5.6%yoY, as compared with 12%+ levels previously.

Trends in Manufacturing (%YoY, 3mma)



Sectoral Trends: Still Going Strong

- Trends in CVs and two-wheelers continue to remain strong; led by a sustained pick-up in infrastructure activity and a focus on infrastructure spends.
- Our autos analyst Jamshed Dadabhoy believes that a strong replacement cycle in India is also a key driver for growth (27% of the existing fleet in India is more than 15 years old and needs to be replaced both for commercial and environmental reasons).

Sectoral Trends (%YoY)

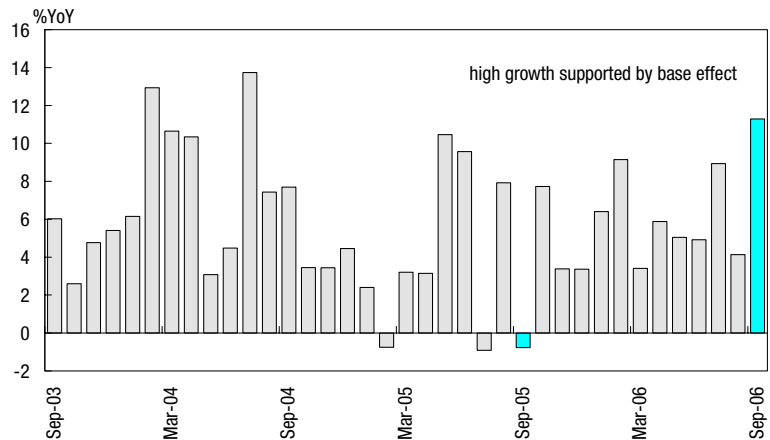
	Apr-06	May-06	Jun-06	Jul-06	Aug-06	Sept-06	Apr-Sept05	Apr-Sept06
CV sales	77.1	41.2	30.9	38.6	28.9	33.1	10.1	41.6
Two-wheelers sales	12.7	20.4	23.6	19.7	3.5	19.1	16.9	16.5
Car Sales	19.9	25.8	25.4	20.5	13.9	19.8	7.6	20.9
Cement Dispatches	11.6	7.6	12.1	15.4	2.1	17.0	10.5	10.9
Diesel consumption	10.4	15.1	-2.9	3.9	-1.2		0.3	5.1
Infrastructure index	6.8	6.0	6.4	9.0	5.8	9.9	6.1	7.3
Overall IP	9.4	8.2	1.8	16.9	13.2	12.5	10.1	13.4

Source: NCAER, CSO, Citigroup, SIAM, Oil and Gas Monitor

Electricity : Sept. Sees Sharp Rise of 11.3%

- Trends in Electricity reported a sharp turnaround, growing 11.3% yoy in Sept. '06 as compared with just 4.1% last month. This can partly be attributed to a base effect (electricity contracted by 0.8% in Sept. '05)
- Our power analyst, V. Balasubramaniam, believes that secular growth prospects for the power sector in India appear good, given current shortages, and low usage and penetration levels. Moreover, robust growth forecasts for the economy imply that the propensity to consume power can only increase.

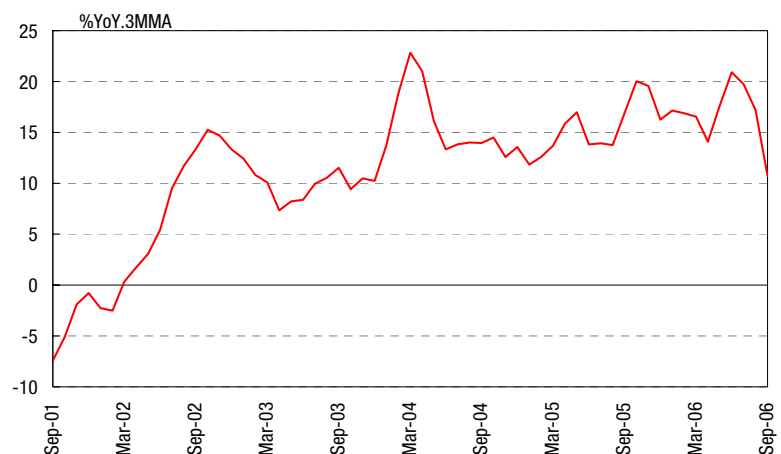
Trends in Electricity (%YoY)



Capital Goods: Decelerates Sharply in Sept. to 2.2%

- Surprisingly, production in capital goods was a disappointment; down to just 2.2% yoy in Sept. as compared with 15%+ seen earlier this year.
- While the base effect could explain part of the deceleration, (growth in Sept. '05 was 22% yoy), this does appear to be an anomaly given the strong order books of the engineering companies
- Going forward, we expect double-digit growth given the capex surge and a thrust on infrastructure development

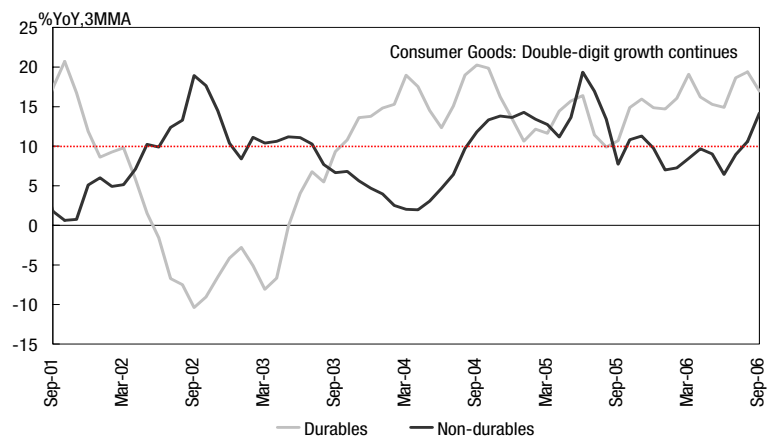
Trends in Capital Goods Production (% YoY, 3mma)



Consumer Goods – Still Strong

- Similar to previous trends, growth in consumer goods remained healthy- up 12.5% in Sept.
- Growth was led by consumer durables, up 12.6%, while consumer non-durables were up 12.5%.
- Going forward, we expect production in consumer goods to remain strong on the back of increased demand from the rural sector with the trickle-down impact coming into play.

Trends in Consumer Goods – Durables and Non-Durables (%YoY, 3mma)



Source: CSO

Disclosure Appendix

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