



Asia Ex-Japan Comment

12 April 2007

India: Industrial output stronger-than expected

- ♦ Industrial output grew by a stronger than expected 11.0% y-o-y in February, from an upward revised 11.4% in January.
- ♦ Growth is fueled by the manufacturing sector, though consumer durables growth has decelerated.
- ♦ We continue to expect GDP to grow at 9.6% in 2007 implying further tightening ahead by the RBI.

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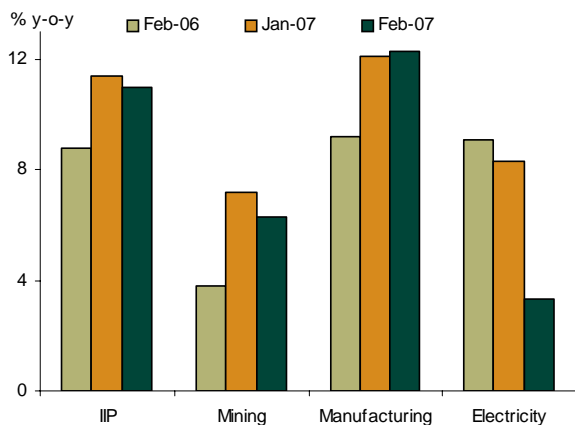
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India's industrial output grew by a stronger than expected 11.0% y-o-y in February (Consensus: 11.2%, Lehman: 10.7%) and the January number was revised up to 11.4% from 10.9% previously (Figure 1). Manufacturing sector contributed to more than 93% of the total rise with an impressive growth of 12.3% y-o-y (versus 12.1% in January), while electricity output disappointed at 3.3% (versus 8.3% in January).

Fifteen out of the seventeen manufacturing sectors posted a positive growth in February and the top performers were: wood & wood products, furniture and fixtures (128.9% y-o-y in February); basic metal and alloy industries (27.4%); cotton textiles (16.1%) and wool, silk & man made fibre textiles (15.0%). The ongoing investment boom has had a positive effect on the demand for both capital and intermediate goods with their output up by 18.2% y-o-y and 13.7% respectively. Meanwhile, rising interest rates and higher automobile prices have dampened demand for cars and commercial vehicles – consumer durables grew at 1.6% y-o-y in February versus 5.3% in January and March vehicle output numbers signal further moderation next month (Figure 2). While this suggests that monetary tightening is set to have an impact, it is too early to sound the alarm bells as vehicle output growth has been very volatile.

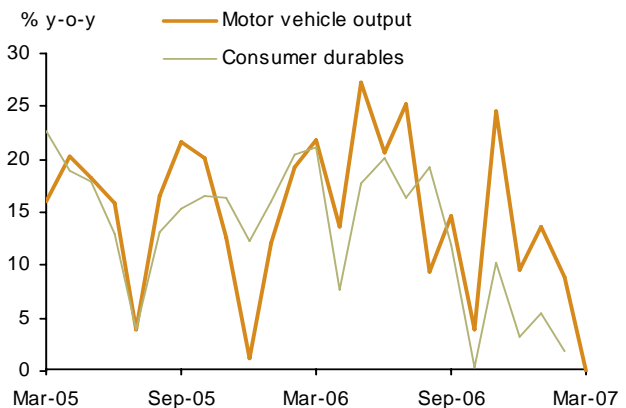
Overall, the twin-engines of manufacturing and services continue to propel India's growth and we expect GDP to grow at 9.6% in 2007. In conjunction with a firm inflation rate, this suggests further monetary tightening by the RBI. We expect the RBI to hike repo rate by 25 bp to 8.0% and cash reserve ratio by 50 bp to 7.0% in 2007. ■

Figure 1. India's industrial output



Source: Bloomberg and Lehman Brothers

Figure 2. Consumer durable output and vehicle production



Source: Bloomberg and Lehman Brothers

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