



Asia Ex-Japan Comment

12 March 2007

India: Industrial output is stronger and broader

- ♦ Industrial output grew by a stronger than expected 10.9% y-o-y in January, after gaining 12.5% in December.
- ♦ Growth is broadening from the manufacturing to the electricity sector, with positive secondary effects also visible.
- ♦ We continue to expect GDP to grow at 9.6% in 2007 implying further tightening ahead by the RBI.

Rob Subbaraman
+852 2252 6249
rsuba@lehman.com

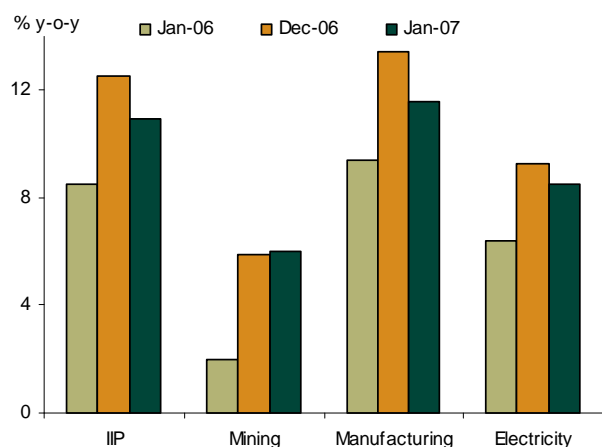
Sonal Varma
+91 22 4037 4087
sonal.varma@lehman.com

India's industrial output grew by a stronger than expected 10.9% y-o-y in January (Lehman 10.4%; Consensus 10.1%), and also the December number was revised up to 12.5% (initial estimate: 11.1%). Encouragingly, there is increasing evidence that the expansion in output is broadening from services to manufacturing and recently, the electricity sector too (Figure 1). Manufacturing output grew by a solid 11.6% y-o-y (versus 13.4% in December), while electricity output expanded by 8.5% (versus 9.3% in December).

Within the manufacturing sector, output of basic metals & alloy, transport equipment and cotton textiles surged in January due to rising demand for capital goods, motor vehicles and exports of Indian textiles. Indian consumer demand remains strong, underpinned by strong wage growth and positive wealth and confidence effects from rising asset prices. Use-based classification indicates a weakening in capital good output to 8.6% in January from 20.9% last month (Figure 2). However, this sharp drop is largely due to a strong base effect (the sector grew by 27% a year ago), and so we are not overly concerned. Meanwhile, the strength in industry is having positive secondary effects on the demand for both basic and intermediate goods, which has contributed to the rise in WPI inflation.

Overall, the January numbers support our claim that industry has caught up with services and highlights the sustainability of the growth this year. We continue to expect GDP to grow at 9.6% in 2007 implying further tightening ahead by the RBI.

Figure 1. India's industrial output



Source: Bloomberg and Lehman Brothers

Figure 2. India's industrial output by use

| % y-o-y | Jan 2007 | Dec 2006 | Jan 2006 | Apr-Jan FY07 | Apr-Jan FY06 |
|-----------------------|----------|----------|----------|--------------|--------------|
| IIP | 10.9 | 12.5 | 8.5 | 11.0 | 8.0 |
| Basic Goods | 11.6 | 12.3 | 7.5 | 10.0 | 6.2 |
| Capital Goods | 8.6 | 20.9 | 27.0 | 16.8 | 16.9 |
| Intermediate Goods | 12.7 | 12.2 | 3.6 | 11.4 | 2.4 |
| Consumer Goods | 9.9 | 10.2 | 8.0 | 9.8 | 11.9 |
| -Consumer Durable | 6.8 | 3.1 | 15.9 | 10.9 | 14.2 |
| -Consumer Non-durable | 10.9 | 12.4 | 5.7 | 9.4 | 11.2 |

*IIP = Index of industrial production

Source: Bloomberg and Lehman Brothers

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