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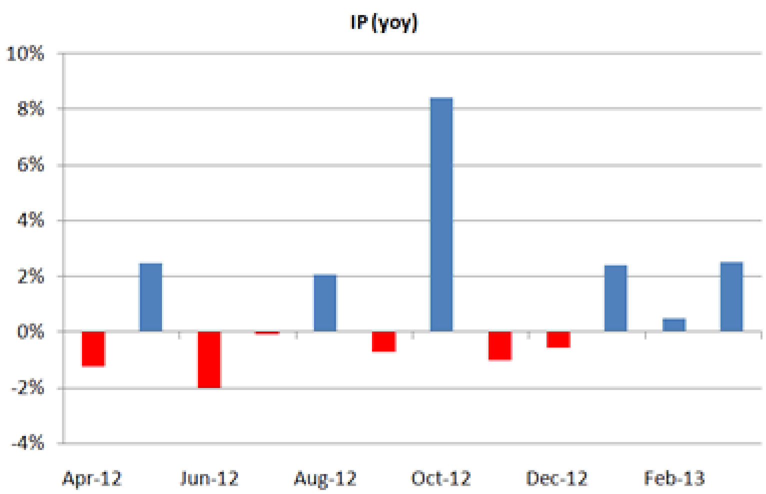
Dark shadows in data haunt India's output
By Kunal Kumar Kundu

NEW DELHI - The reversal of India's downward trend in industrial production (IP) in the three months to the end of March provided some sense of comfort for the government of Prime Minister Manmohan Singh, which has been beleaguered by several corruption cases and a parliamentary deadlock.

Industrial production grew 2.51% year-on-year (yoy) in the last quarter of the financial year, according to data released this week, expanding in all three months after contracting in six of the first nine months.

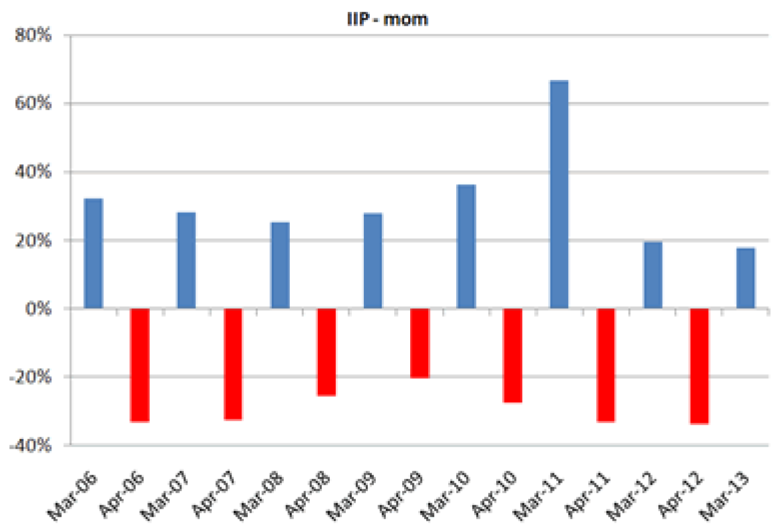


Source: CEIC Data

Industrial production grew by 1% yoy during the full fiscal year, down from 2.9% yoy expansion in the previous 12 months. Within this, manufacturing grew by 1.2% yoy in the 12 months through March 2013, less than half the 3% yoy growth recorded in the preceding year.

Also heartening, the capital goods sector is showing some signs of stability after contracting during nine out of the first 10 months. Even so, it contracted by 6.3% in the full year, following a 4% contraction the year before. This does showcase the fact that investment in India has been badly hit.

While the capital goods segment is one of the more volatile components of IP, there is one trend that repeats with unerring regularity. Every year, the index of capital goods production shoots up in March compared with February, only to retrace in April from the March highs.



Note: mom – month on month. Source: CEIC Data, author's calculation.

Given this, it is difficult to conclude that capital goods production has indeed bottomed out. One needs to keep an eye on the data for another three months to be able to arrive at a conclusion.

While the performance of the index over the last three months does lend credence to the belief that the worst may be over for the economy, the sense of comfort vanishes as one takes a closer look at the data.

For starters, the February IP Index was revised downward (though at the margin) to 0.46% yoy from 0.57% yoy. During six out of the past 11 months, the index was revised downward when we moved from preliminary to final data. More importantly, the quality of data continues to remain suspect.

When one considers the disaggregated data at the two-digit level, a major distortion is visible in the category "wearing apparel; dressing and dyeing of fur". The index value for this segment dropped to 68.4 in March 2012 from 154.2 in February 2012 and then jumped back to 124.2 by April 2012. Clearly, a major base effect came into play here during March 2013 as a result of which production for this category jumped by 152.3% yoy in March, thereby pulling up the index considerably.

In fact, despite having a weight of only 2.78% in the IP, this segment contributed as much as 2.9 points to the overall index on an annual basis, while the IIP in itself increased by only 4.7 points over the same period.

Like most other categories, manufacturing of this product also exhibits a high degree of volatility. If we extrapolate the average growth rate in production of this segment for the first 11 months (April till February) to March, it would have grown by only 3.3% and not 153% as is the situation at present.

Had that been the case, overall IP would have increased by only 0.99% yoy in March and not 2.51% yoy as the official data suggests. Correspondingly, for the full year, the IP would have increased by 0.49% rather than 1% official growth rate.

Even if we go by the official data, a mere 1% growth in industrial production has implications for overall economic growth. According to the Advanced National Accounts Estimates released by the Central

Statistics Office, industry is estimated to grow by 2% in the 12 months through March 2013. The weak IP data indicates that the industrial performance might have been over estimated.

As a result, final gross domestic product growth for the year may well be below 5%. For the current financial year, ending next March, while I do expect the growth numbers to improve, I do believe that India will struggle to expand its economy by as much as 6%. That is less than the latest World Bank forecast, released this month, of 6.1%, itself lower than its 7% estimate six months earlier. India's fourth quarter GDP came in at 4.5%, the lowest in more than 10 years.

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