Dun & Bradstreet
ECONOMY OBSERVER
Issue 22 | February 2009

Decide with Confidence

Contents

View from the top

The sharp slowdown in global demand coupled with heightened uncertainty in the domestic market has weighed on the Indian economy as reflected in the Index of Industrial Production (IIP) growth number for the month of December 08. IIP declined by as much as 2% during Dec 08, marking the second dip in three months. In view of significant deceleration in economic activity, especially in the first four months of H2 FY09, growth in Real GDP is expected to moderate to 6.4% in H2 FY09 (CSO Advance Estimates) as compared to 8.8% during H2 FY08.

Further, the slowing investment momentum as reflected in moderation in growth of Gross Fixed Capital Formation (GFCF) to 8.87% (y-o-y) in FY09 as against a growth of 12.95% in FY08 is a cause of concern. However, the Government is expected to step up spending especially in the infrastructure sector and thereby provide some support to the waning investment demand. Although the government expenditure is likely to increase in the near future, private consumption expenditure might remain subdued in the short run given the uncertainty prevailing in the labour market owing to job layoffs and pay cuts.

According to a survey conducted by the Labour Bureau of India (of 2581 units belonging to important sectors viz. Mining, Textiles, Metals, Gems & Jewellery, Automobile, Transport and IT/BPO) about half a million workers have lost their jobs during Oct-Dec FY09. As per the survey, the major impact of the slowdown is felt in the export oriented units, where employment declined at an average monthly rate of 1.13% during Oct - Dec FY09 as compared to a decline of 0.81% in non-exporting units. Slowdown in the global economy and increase in unemployment across the world are adversely affecting the overseas demand for Indian products, thereby taking a toll on production and employment in export oriented units.

Significant deceleration in key economic activities indicates that the impact of the earlier fiscal and monetary measures has been muted so far. We therefore expect the RBI to cut policy rates further in an attempt to stimulate demand. While the government is also expected to increase its developmental expenditure to support growth and employment, a high fiscal deficit and the upcoming elections could constrain the extent of government spending in the near future.

Dun & Bradstreet's Macro Economic Forecasts

		ACTUALS	
	FORECAST	Latest Period	Previous Month
Inflation (W.P.I)	3.60%-3.80%(Feb-09)	5.19%(Jan-09)	6.43%(Dec-08)
IIP Growth	0.50%-1.50%(Jan-09)	-1.97%(Dec-08)	1.72%(Nov-08)
15-91-day T-Bills	4.50%-4.80%(Feb-09)	4.52%(Jan-09)	5.22%(Dec-08)
INR/US$	48.50-48.70(Feb-09)	48.83(Jan-09)	48.64(Dec-08)

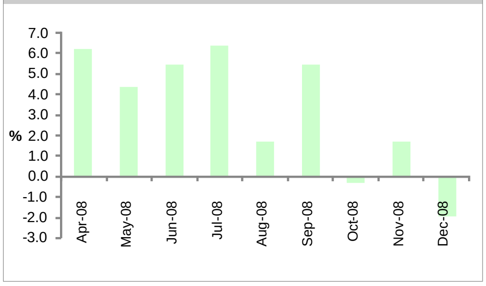
All figures are monthly averages

Real Economy

IIP declines by 2% in Dec-08

The knock-on effects of the global financial crisis and the subsequent slowdown in global growth coupled with crisis of confidence across the world have weighed on overall economic activity as is manifested in the growth estimates of 7.1% (AE) for FY09 released by the CSO. Expected fall in Kharif crop production and adverse impact of warm weather (during Jan & Feb) on the Rabi crops production is likely to contain agriculture growth to 2.6% (AE) in FY09 as against 4.9% in FY08. As per CSO's advance estimates, slowdown in the 'financing, insurance, real estate and business services' and 'trade, hotels, transport and communication' is likely to pull down the services sector growth to a single digit level of 9.6% (AE) in FY09. Further, industry has also experienced a considerable slowdown and is estimated to grow by 4.8% during FY09.

Growth in Index of Industrial Production



Source: CSO

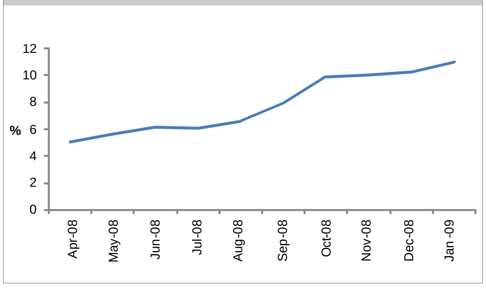
Infact, the industrial production (as measured by the IIP) declined by as much as 2% during Dec-08, marking the second dip in Q3 FY09. The sharp decline in the IIP growth during Dec-08 can in part also be attributed to the high base of the last fiscal. The slowdown in IIP growth was more pronounced in the manufacturing sector, which witnessed a decline of 2.5% during Dec-08 as against a growth of 8.6% during Dec-07. Further, a substantial slowdown witnessed across the manufacturing sector has adversely impacted demand for intermediate goods. Growth in intermediate goods declined substantially by 8.5% during Dec-08 as compared to 7.6% during Dec-07. Consumer durable sector also registered a decline of as much as 12.8% in Dec-08, thereby pulling down the production of consumer goods by 2.7%. Increasing layoffs, pay cuts and uncertainty in the economic environment might have led to holding back of consumption by households which in turn could have hampered the production of consumer goods. Given that demand conditions in domestic as well as international markets are subdued, D&B expects IIP to have grown within the 0.5-1.5% range during Jan-09.

Price Scenario

Inflation slips further on fuel price cut

Inflation, as measured by WPI, moderated to a one year low of 4.39% during the week ended 31-Jan-09 taking the average inflation for the month of Jan-09 to 5.19%. Significant decline in global crude oil prices have led to moderation in the prices of industrial fuels in the domestic market, necessitating the Central Government to cut the prices of Petrol, Diesel and LPG in Jan-09. This led to a deflation of 1.69% in the fuel group in Jan-09 as compared to a deflation of 0.23% during Dec-08. As a consequence, the contribution of fuel group to overall inflation was at -4.37% in Jan-09.

WPI Food Articles



Source: Ministry of Commerce

The primary articles inflation moderated to 10.32% in Jan-09 as compared to 11.90% in Dec-08 on account of receding prices of non-food articles and minerals. However, primary article inflation continues to be at elevated levels mainly due to high prices of food article such as fruits & vegetables and food grains. The eight-day transporter's strike, which began on Jan 5, might have affected supplies of primary food articles which in turn led to higher food article prices. The food article inflation increased to 10.99% in Jan-09 as compared to 10.28% in Dec-08. The inflation in manufactured food products has also inched up to 5.74% in Jan-09 as compared to 3.79% in Dec-08 driven by high prices of oil cakes and sugar, khandsari and gur. Continued moderation in prices of manufactured products such as 'non-metallic mineral products', 'basic metal alloys & metal products' and 'transport equipment & parts' has however helped to bring down the inflation in manufactured products to 5.79% during Jan 09 as compared to 6.85% in Dec-08.

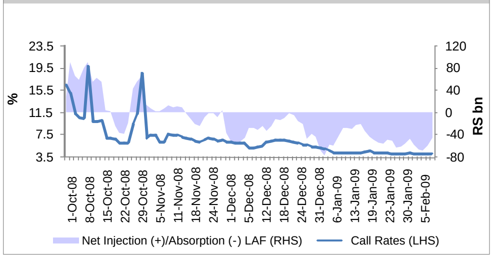
Going forward, the recent cut in petrol & diesel prices, which is expected to result in lower transportation costs, might ease inflationary pressures in agricultural and manufactured products as well. D&B therefore expects WPI inflation to average between 3.6-3.8% during Feb-09.

Money & Finance

Bank credit growth moderates

Comfortable liquidity condition and expected lagged effects of the aggressive cut in policy rates during Oct 08 - Jan 09 might have induced the RBI to maintain a status quo on key interest rates during the third quarter monetary policy review. In a span of just four months, the RBI aggressively eased its monetary stance by reducing the CRR, Repo and Reverse repo rate by 400 bps, 350 bps and 200 bps respectively. Although few banks have reduced their lending rates in consonance with the RBI rate cuts, the extent of rate cuts has been low given that deposit rates are at high levels. Further, the slew of policy measures taken by the RBI since mid-Sep 08 have infused significant liquidity into the system thereby easing liquidity pressures as indicated by lower call rates and increase in funds parked by the banks in reverse repo window.

Liquidity Conditions



Source: RBI

The increase in the amount of funds parked with the RBI via the reverse repo window (at a time when reverse repo rate is at an all-time low) in part also reflects the heightened risk aversion by the banks. Increase in banks SLR holdings to 28.9% in early Jan-09 from 25.8% in mid-Oct 08 further corroborates this fact. Growing concerns about asset quality coupled with moderating demand for bank credit in the wake of slowdown in economic activity have weighed on bank credit growth in last few months. Growth in bank credit has moderated to 22.1% as on 16-Jan-09 as compared to 29.1% as on 24-Oct-08.

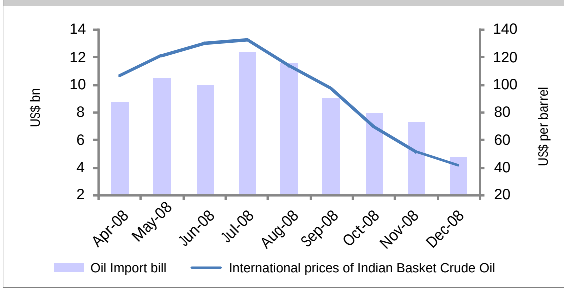
A status quo by RBI in terms of policy rates in the monetary policy review coupled with Government's announcement regarding increase in borrowing dampened sentiments in the gilt market. The yield on the ten-year benchmark gilt closed at 6.17% on 30-Jan-09, up by 110 basis points as compared to 02-Jan-09. 15-91 day Treasury bill yield were in the range of 4.4%-4.8% for week ended 30-Jan-09. D&B expects 15-91 day T-Bills yields to average at around 4.5-4.8% in Feb-09.

External Sector

Exports decline for the third consecutive month

Exports declined for the third consecutive month during Dec-08 as slowdown in the global economy and increase in unemployment across the world are adversely affecting the overseas demand for Indian products. The decline in exports by 1.05% in Dec-08 (US$ terms), however, was moderate compared to the decline of 12.1% & 9.9% in the month of Oct and Nov-08. In rupee terms, exports grew by around 22% (y-o-y) primarily due to 23.33% (y-o-y) depreciation in the rupee against the dollar during Dec-08. However, declining export orders amid tight access to credit is likely to limit the benefits of rupee depreciation to the exporters. In an attempt to provide some respite to the exporters, the RBI raised the ceiling rate on export credit in foreign currency by banks to Libor plus 350 basis points from the earlier ceiling rate of Libor plus 100 basis points. Further, with significant reduction in international prices of crude oil, India's oil imports bill has declined by as much as 30.9% (y-o-y) during Dec-08 leading to moderation in overall imports growth to 8.8%. However, non-oil imports registered a significant increase of 31.9% (y-o-y) to US$ 15.5 bn in Dec-08 after showing some deceleration during Oct & Nov-08. With lower oil import bill, the trade deficit has also narrowed to a single digit level of US$ 7.6 bn in Dec-08.

Oil Imports



Source: Ministry of Commerce

In the forex market, the rupee witnessed high volatility during the month of Dec-08. Rupee declined to touch 49.27/US$ on 23-Jan-09 as compared to 48.58 on 2-Jan-08 primarily due to strengthening of the US dollar against major global currencies and dollar demand from corporates, exporters and oil importers. Rupee rebounded to some extent subsequently and closed at 48.67/US$ on 6-Feb-09, drawing support from dollar sales by foreign banks and some recovery in the domestic stock markets. D&B expects the rupee to remain in the range of 48.50-48.70 to a US$ during Feb-09.

Please send your feedback to Yashika Singh, Head-Operations, Economic Analysis Group

Dun & Bradstreet Information Services India Pvt. Ltd., ICC Chambers, Saki Vihar Road, Powai, Mumbai 400 072

Tel: 91-22-28574190 / 92 / 94 Fax: 91-22-28572060 Email: D&BEconomyObserver@mail.dnb.co.in www.dnb.com