Economic growth slowed down in the second quarter of fiscal 2016-17

Indian economic growth decelerated marginally on a year-on-year basis as real GDP growth during the second quarter (Q2) of fiscal 2016-17 was recorded at 7.3% as against 7.6% in the same quarter last fiscal. However, GDP growth accelerated over the previous quarter as the first quarter managed GDP growth at 7.1%. Another measure of economic activity, GVA, grew by a slower 7.1% in the reporting quarter as against 7.3% in the previous quarter as well as during the same quarter last year.

The slowdown in GVA growth was attributed to slower growth of manufacturing, mining, electricity, gas & water supply and financial sector. Manufacturing grew by 7.1% during the reporting quarter as against 9.2% during the same quarter last year while mining conceded 1.5% decline from a growth of 5.0% during the same quarter last year. Growth of electricity and financial sector also conceded substantial decline over the same quarter last year.

On the other hand, agriculture, construction and public administration achieved higher growth on a year-on-year basis. ‘Public administration, defence & other services’ grew by an impressive 12.5% growth in Q2 of the current fiscal as against 6.9% during the same period last fiscal while agriculture grew by 3.3% as against 2% during Q2 of the last fiscal.

Outlook

The demonitization of high-value bank notes in Nov 2016 is apprehended to weigh on the pace of growth in the next two quarters of the current fiscal and the growth of entire fiscal in turn. GDP growth for fiscal 2016-17 was estimated at a lower 7.1% as against 7.6% in the previous fiscal.
Industrial Production

Industrial production dropped again in Oct 2016

Industrial output in India, as measured by the Index of Industrial production (IIP), dropped once again in Oct 2016 by 1.8% over the same period last year after managing marginal growth in the previous month. The decline in production was attributed to 2.4% fall in manufacturing output during the month. Mining also conceded 1.1% decline in production while only electricity achieved 1.1% growth over the same period last year among the major sectors.

![Fig1: Industrial Output Growth from May 2014](image)

Use-based analysis exhibited decline in consumer goods after five months: Capital goods once again was the spoilsport among the segments of manufacturing conceding decline for the twelfth straight month and more than 20% decline for the fourth month in a row. Basic goods and intermediate goods however recorded 4.2% and 2.7% rise in production respectively during Oct 2016. On the consumer goods sector, non-durable production declined by 2.9% but durable segment grew by a meagre 0.6% during the reporting month. Consumer sector as a whole recorded 1.4% year-on-year drop in output during Oct 2016.

Cumulative IIP during Apr - Oct 2016 remained much lower than that of the previous fiscal: Cumulative Industrial production during the first seven months of fiscal 2016-17 conceded 0.3% decline as against 4.8% growth during the same period last year mainly due to dismal manufacturing that witnessed 1.0% decline in output during Apr - Oct 2016-17 as against 5.1% growth in the same period last fiscal. Mining output also declined by 0.2% during this period as against a growth of 2.2% during Apr - Oct 2015-16. Only electricity achieved a better growth over the previous fiscal. The obvious reason behind the decline in manufacturing output was depressing capital goods sector conceding 22.1% fall in output as against 9.0% growth during the first seven months of the previous fiscal. Consumer non-durables was another segment that recorded decline in production (2.5%) during the first eight months of the current fiscal.
Industry group-wise analysis of engineering products during Apr - Oct 2016

Among the nine industry groups fall under engineering, three concede decline in output during Apr - Oct 2016 over the same period last fiscal. Output of 'Electrical machinery & apparatus' tumbled by 51.8% on a cumulative basis during these seven months and recorded 58.3% drop in output during Oct 2016. 'Office, accounting & computing machinery' witnessed a 7.6% decline in production during Apr - Oct 2016 driven by a substantial 29.5% fall in output during the reporting month. Among the leading sectors, 'Radio, TV and communication equipment & apparatus' registered highest cumulative growth at 10.1% during Apr - Oct 2016 but output declined by 2.9% during Oct 2016. 'Other Transport Equipment' was the immediate follower with 8.0% on a cumulative basis.

Outlook: The month of November 2016 may see a better scenario due to lower base as IIP suddenly dropped in November 2015. However, overall trend is not likely to see a sudden reversal during the rest of the fiscal as capital goods, a reflection of weak investments and consumer non-durables, a sign of consumption demand are likely to remain weak.
Inflation

Retail price inflation in Nov 2016 dropped to two-year low

India’s retail (or CPI) inflation softened sharply to 3.63% in Nov 2016 from 4.2% in the previous month. While a cash crunch arising out of the demonetization of high-value currency notes by the Indian govt. on 8th Nov 2016 was considered responsible for this decline in inflation, a base effect was also attributed to lower CPI inflation in the reporting month as CPI inflation witnessed a sudden 41 basis point month-on-month jump during Nov 2015. However, cash crunch probably led to depressing consumer demand as food inflation tumbled to 2.11% in Nov 2016 from 3.38% in Oct 2016. The weightage of Food articles in retail commodity basket was around 47% and therefore it was worst hit of the cash crunch. CPI inflation is now well below the target of RBI at 5% for the end of the current fiscal.

Wholesale Price Inflation also dropped to 3.15% in Nov 2016 from 3.39% in the previous month and food inflation, with around 15% weightage in the wholesale commodity basket declined by 1% year-on-year in Nov 2016.

![WPI and CPI Inflation from April 2014](image)

**Fig 6: WPI and CPI Inflation from April 2014**

Outlook - The next month may see further easing of inflation as the effect of demonetization is expected to continue in Dec 2016. However, retail inflation may again go up to around 5% by the end of the ongoing fiscal on account of the waning of the base effect and the impact of higher consumer demand on prices, but is not likely to go beyond the comfort level of RBI.

Non-food credit disbursal to industry remained weak in Oct 2016

Non-food bank credit growth slowed down to 6.7% in Oct 2016 from 10.8% in Sep 2016. The slowdown was also observed on a year-on-year basis as non-food bank credit growth was recorded at 8.3% in Oct 2015. Credit disbursal to industry contracted by 1.7% in Oct 2016 as against 0.9% increase in Sep 2016 and 4.6% in Oct 2015. Major sub-sectors which witnessed deceleration/contraction in credit include infrastructure, food processing, gems and jewellery and basic metal and metal products. Credit disbursal to manufacturing sector contracted by a
worrisome 8.9% in Oct 2016 as against a contraction of 1.5% in Sep 2016. Credit growth to manufacturing was recorded at 4.9% during Oct 2015.

Indian Rupee continued to depreciate against the US Dollar for the second straight month to Nov 2016

The Indian rupee again weakened over the US Dollar for the second straight month to Nov 2016 and this time the depreciation was substantial at 2.5% as against a mild 0.3% during the previous month. The possibility of benchmark interest rate hike by the US Federal Reserve in Dec 2016 weighted on currencies of the emerging market including Rupee.

Table 1: Performance of Indian Rupee vs. Major Traded Currencies

<table>
<thead>
<tr>
<th>% Change in Nov 2016</th>
<th>USD</th>
<th>GBP</th>
<th>EURO</th>
<th>YEN</th>
</tr>
</thead>
<tbody>
<tr>
<td>Direction</td>
<td>Depreciation</td>
<td>Depreciation</td>
<td>Appreciation</td>
<td>Appreciation</td>
</tr>
<tr>
<td>% Change in 2016</td>
<td>2.50%</td>
<td>5.21%</td>
<td>-0.09%</td>
<td>-4.18%</td>
</tr>
<tr>
<td>Direction</td>
<td>Depreciation</td>
<td>Appreciation</td>
<td>Depreciation</td>
<td>Depreciation</td>
</tr>
<tr>
<td>Source: RBI Reference Rates</td>
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</tbody>
</table>

Outlook for rupee is weak – Rupee is likely to remain weak in the near term mainly due to the possibility of rate tightening by the US Federal Reserve.

Global News

US Federal Reserve raised benchmark interest rate by 25 basis points

Janet Yellen, the chairperson of the US Federal Reserve announced in the last meeting of the Federal Open Market Committee (FOMC) on 14th Dec 2016 that the FOMC decided to raise the target range for the federal funds rate by ¼ percentage point, bringing it to ½ to ¾ percent. The benchmark Federal fund Rate is now between 0.50% and 0.75%. The FOMC members were of the opinion that the economy has shown considerable progress towards maximum employment and price stability and can accommodate this increase in the interest rate.

Source: RBI; MOSPI, Govt. of India; Other Govt. of India Websites, ICRA, Newspapers & Periodicals