

IIP contracts sharply; Food inflation rises amid supply-side bottlenecks

The nation-wide lockdown and consequent shutdown of non-essential manufacturing has severely impacted industrial activity. Industrial production contracted by 16.6% YoY in March'20—the steepest decline ever, and much lower than the Consensus Estimate of -8.7% (source: Refinitiv Datastream), translating into a drop of 0.7% in FY20. This was led by a sharp dip in manufacturing activity as well as decline in electricity production owing to low industrial/commercial demand, even as mining production remained largely steady. However, with the response rate being lower than usual, revisions to March figures are inevitable. Industrial production is expected to witness a much sharper contraction in April given the extended and stringent lockdown for the entire month.

The decline in food inflation witnessed over the last couple of months has been expectedly halted, albeit temporarily, owing to lockdown-induced supply-side bottlenecks. Food inflation (36.7% of the CPI basket) picked up by ~80bps MoM to 8.6% led by a jump across the board (except fruits). Within core inflation, while health inflation moderated to series-low levels, housing inflation inched up modestly. Price collection of other categories has not happened owing to unavailability of transaction data. A meaningful deterioration in consumption demand, coupled with a sharp drop in commodity prices, is expected to keep core inflation benign.

Even as data collection is expected to be a challenge in April/May, other high frequency indicators viz., auto sales, merchandise trade and PMI, amongst others, confirm the extent of economic shock caused by COVID-19 and attendant measures undertaken to contain the spread. The PM yesterday unveiled a massive stimulus package worth Rs 20trn or 10% of GDP, inclusive of fiscal/monetary measures undertaken thus far (Rs 7.7trn or 3.9% of GDP), translating into an additional package of Rs 12.3trn. With the quantum of the policy announcement being much higher than the increase in Government's borrowing for FY21 (2% of GDP), details are awaited on the package, that would be spelt out over the next week. We continue to expect policy rates to fall by another 50-75bps, ceteris paribus, and continued liquidity injection in the system.

- **Lockdown impacts data collection:** Retail prices are collected from field visits to selected 1114 urban and 1181 villages in the country on a weekly roster. In the wake of nation-wide lockdown, price collection through personal visits were suspended w.e.f. March 19th. Data collection for the month of April has taken place from 674 urban and 524 villages for commodities that were transacted and were available during the lockdown. Due to limited transactions in April, price movement for several sub-groups were not compiled. Similarly, data flow from factories/establishments in March was impacted due to lockdown, with the weighted response rate of 73% being much lower than 94% in December 2019.
- **Industrial production declines sharply owing to lockdown:** After improving to a seven-month high of 4.6% in February, industrial production growth fell sharply to -16.6% in March 2020—the steepest decline in the new series and much lower than the Consensus estimates (-8.7% as per Refinitiv Datastream poll). This translates into a decline of 0.7% in FY20 vs. +3.8% in FY19. The sharp drop in March was largely led by a 20.6% YoY contraction in manufacturing output and a 6.8% YoY decline in electricity production amid low demand from industrial and commercial establishments, even as mining production remained largely steady as compared to the same period last year. All sub-sectors within the manufacturing space witnessing a contraction, with biggest laggards being motor vehicles, trailers & semi-trailers (-50% YoY), computer, electronic & optical products (-42% YoY), fabricated metal products (-33% YoY) and machinery & equipment (-32%).

On the use-based side, capital goods and consumer durables got impacted the most, contracting by 36% and 33% YoY in March, translating into a drop of 11.5% and 6.2% in FY20 respectively.

Industrial production declined by 16.6% in March 2020—the steepest decline in the new series.

Contraction in April is expected to be much sharper amid an extended and stringent lockdown during the entire month.

- Food inflation picks up amid supply bottlenecks:** The lockdown-induced supply-side bottlenecks have temporarily halted the decline in food inflation witnessed over the previous few months. Food inflation (36.7% of the CPI basket) picked up by ~80bps MoM to 8.6% led by a jump across the board (except fruits). Among major food items, inflation in cereals/pulses (~12% of the CPI basket) jumped to 71/45-month high of 7.8%/22.8%, spices inflation surged to the series-high (since Jan'12) of 12.8% and inflation in oils & fats picked up to 86-month high of 10.8%. While fruit inflation moderated for third month in a row, vegetable inflation remained elevated (+23.6% in Apr'20) amid supply constraints. Within core inflation, while health inflation moderated to series-low levels, housing inflation inched up by a modest 25bps MoM to 3.9%. Price collection in other categories has not happened due to limited transaction data.
- Government announces a Rs 20trn stimulus but devil lies in the details:** The Prime Minister, yesterday, unveiled a mega stimulus package of Rs 20trn or 10% of GDP, much higher than market expectations. However, this includes fiscal as well as monetary measures already undertaken over the last couple of months, amounting to ~Rs 7.7trn or 3.9% of GDP (refer Figure 11 of this note). This effectively translates into an additional package of Rs 12.3trn or 6.1% of GDP. However, details are awaited to ascertain the extent of actual spending by the Government and fiscal implications, particularly given a much lower increase in the borrowing plan for the year (Rs 4.2trn or ~2% of GDP).
- RBI to ease further:** Even as data collection is expected to be a challenge in April/May, other high frequency indicators viz. auto sales, merchandise trade and PMI, amongst others, confirm the extent of economic shock caused by COVID-19 and attendant measures undertaken to contain the spread. Food inflation may temporarily remain elevated amid supply constraints, but a significant deterioration in domestic demand, coupled with a sharp drop in commodity prices included crude oil, is likely to keep core inflation benign. The RBI's preliminary estimates point to a sub-3% reading by Q3 FY21. With inflation unlikely to be an impediment to rate cuts, we expect the RBI to slash policy rates by another 50-75bps, *ceteris paribus*, with particular focus on ensuring adequate systemic liquidity through conventional as well as unconventional tools.

Food inflation picked up in April amid supply-side bottlenecks.

The Government's Rs 20trn stimulus package announced yesterday includes Rs 7.4trn worth fiscal/monetary measures undertaken over the last couple of months. Details awaited to gauge the exact spending boost and fiscal implications.

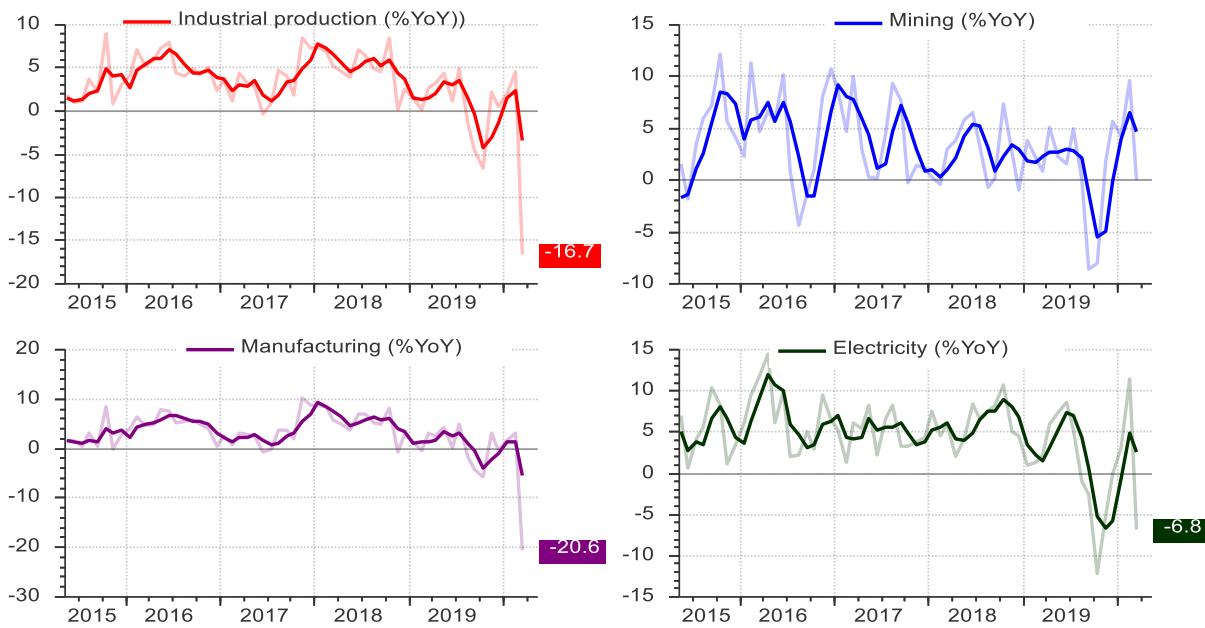
Expect RBI to cut policy rates by another 50-75bps, ceteris paribus, with particular focus on injecting adequate liquidity in the system.

Figure 1: India industrial production for March 2020 (%YoY)

		Weight (%)	Mar-20	Feb-20	Mar-19	FY20TD	FY19TD
IIP			(16.6)	4.6	2.7	(0.7)	3.8
Sector-based indices	Mining	14.4	-	9.7	0.8	1.7	2.8
	Manufacturing	77.6	(20.6)	3.1	3.1	(1.3)	3.8
	Electricity	8.0	(6.8)	11.5	2.2	1.1	5.2
Use-based Goods	Primary Goods	34.0	(3.1)	8.3	2.6	1.2	3.5
	Capital Goods	8.2	(35.6)	(9.5)	(9.1)	(11.5)	5.7
	Intermediate Goods	17.2	(18.5)	19.4	12.4	11.9	(0.2)
	Infra/Construction Goods	12.3	(23.8)	(0.1)	5.1	(2.0)	8.2
	Consumer Goods	28.2	(23.2)	(1.5)	(0.5)	(1.4)	5.6
	Consumer Durables	12.8	(33.1)	(5.8)	(3.2)	(6.2)	6.5
	Consumer Non-durables	15.3	(16.2)	1.5	1.4	2.2	4.9

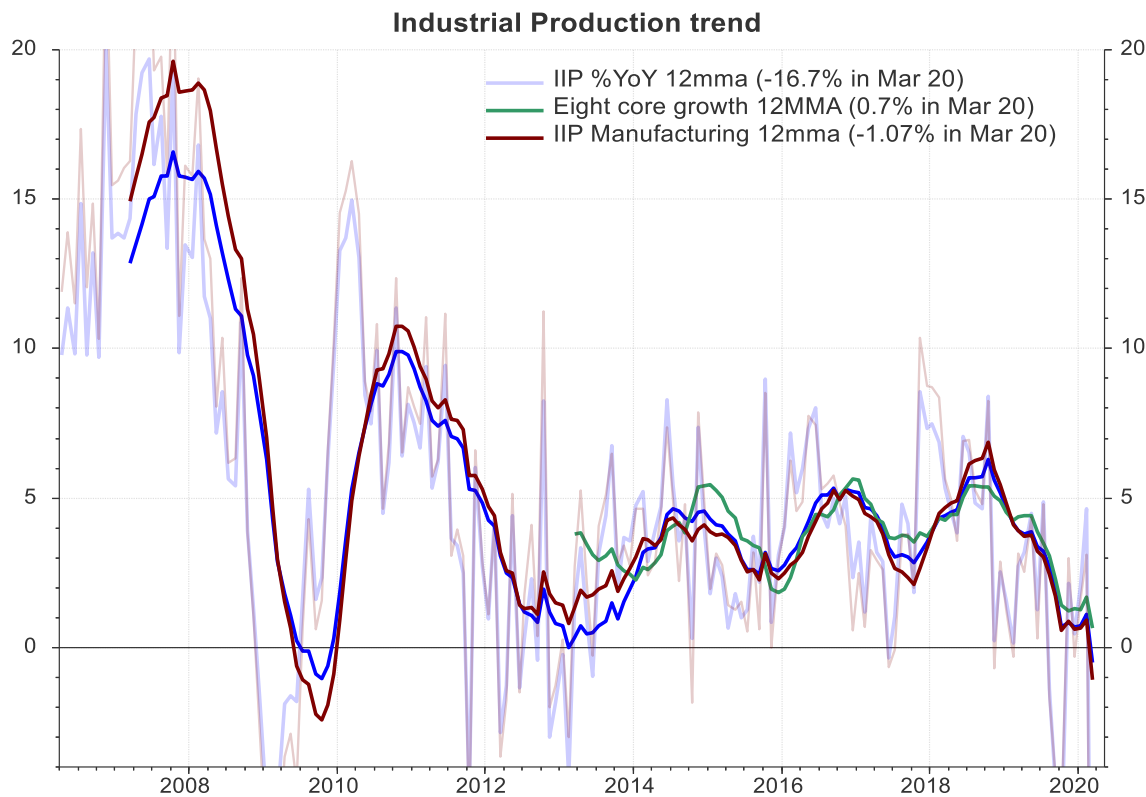
Source: CSO, NSE

Figure 2: India industrial production (3MMA)



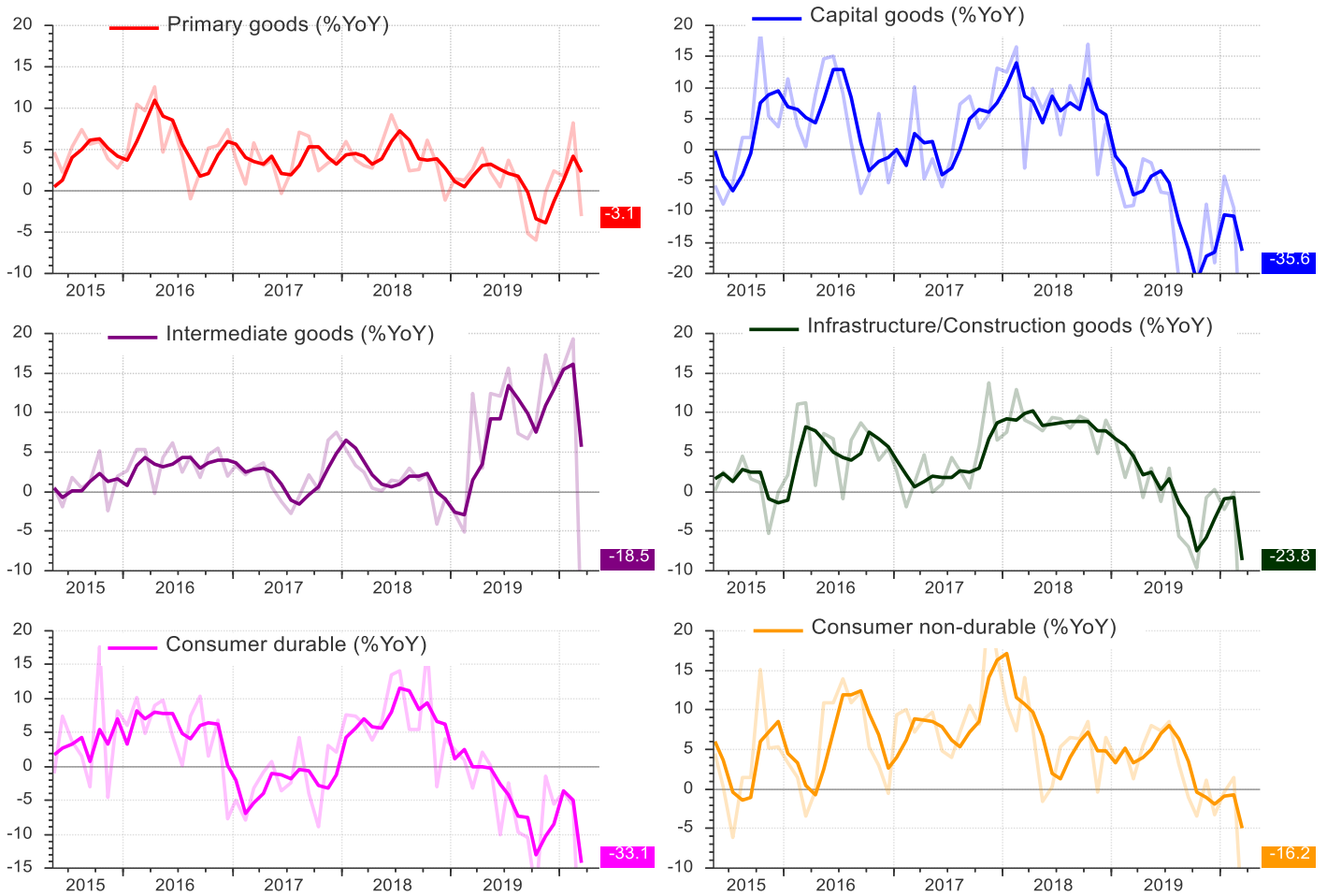
Source: Refinitiv Datastream, NSE

Figure 3: Long-term industrial production trend (12MMA)



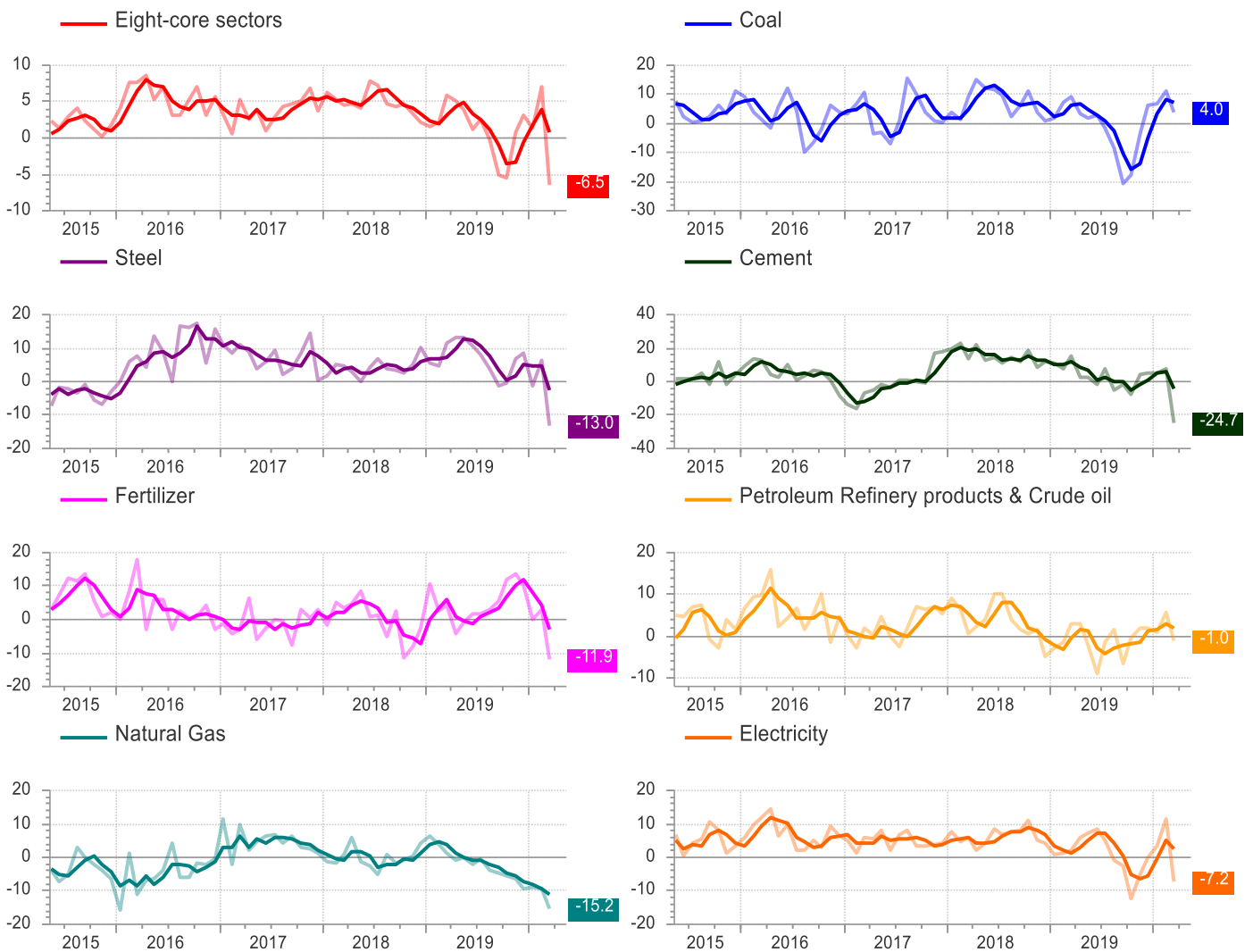
Source: Refinitiv Datastream, NSE

Figure 4: India industrial production use-based goods (3MMA)



Source: Refinitiv Datastream, NSE

Figure 5: India eight-core sector growth (3MMA)

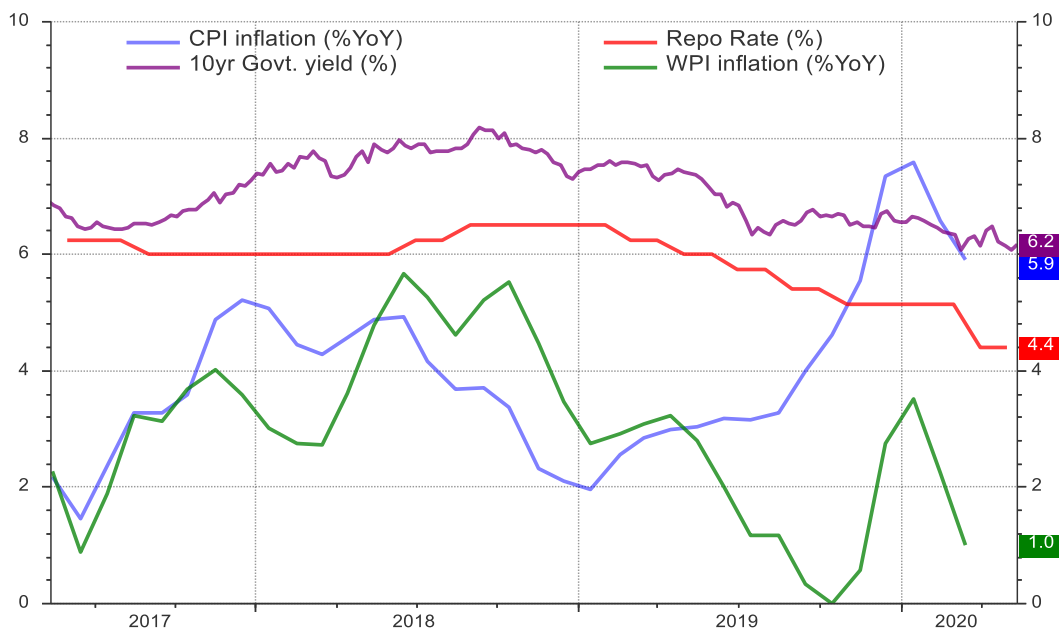


Source: Refinitiv Datastream, NSE

Figure 6: Consumer price inflation in April 2020 (%YoY)

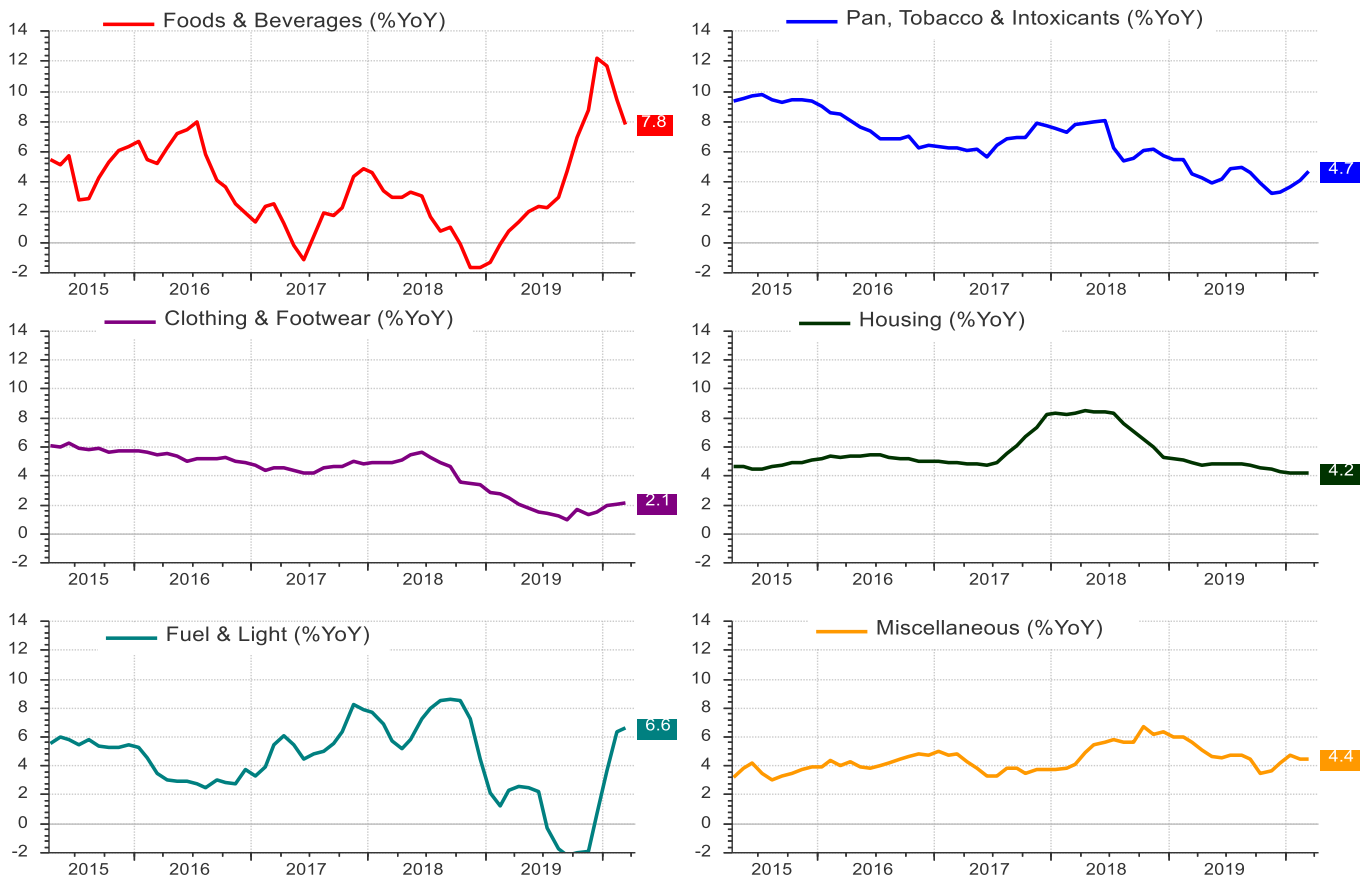
	Weight (%)	Apr-20	Mar-20	Apr-19	FY20	FY19
CPI		NA	5.8	3.0	4.8	3.4
Core CPI inflation*	44.9	NA	3.9	4.6	4.0	5.8
Food & Beverages	45.9	8.6	7.8	1.4	6.0	0.7
Cereals and products	9.7	7.8	5.3	1.2	2.1	2.8
Egg	0.4	9.0	5.6	1.9	2.3	4.5
Milk and products	6.6	9.4	6.5	0.4	1.8	2.9
Oils and fats	3.6	10.8	7.5	0.7	2.1	2.9
Fruits	2.9	2.7	3.6	(4.9)	2.3	0.7
Vegetables	6.0	23.6	18.6	2.9	(5.2)	21.3
Pulses and products	2.4	22.8	15.8	(0.8)	(8.3)	9.9
Sugar and confectionary	1.4	10.3	3.9	(4.0)	(7.0)	0.8
Spices	2.5	12.8	9.8	0.8	2.2	4.4
Non-alcoholic beverages	1.3	2.2	2.2	3.2	2.6	2.6
Pan, Tobacco & Intoxicants	2.4	NA	4.7	4.3	4.2	6.2
Clothing & Footwear	6.5	NA	2.1	2.0	1.6	4.1
Housing	10.1	3.9	3.7	4.8	4.5	6.7
Fuel & Light	6.8	NA	6.6	2.6	1.3	5.7
Miscellaneous	28.3	NA	4.4	5.1	4.4	5.8
Health	5.9	2.8	4.2	8.4	6.3	7.1

Source: CSO, NSE. * Headline inflation excluding food & beverages, pan, tobacco & intoxicants and fuel & light. NA = Not Available.

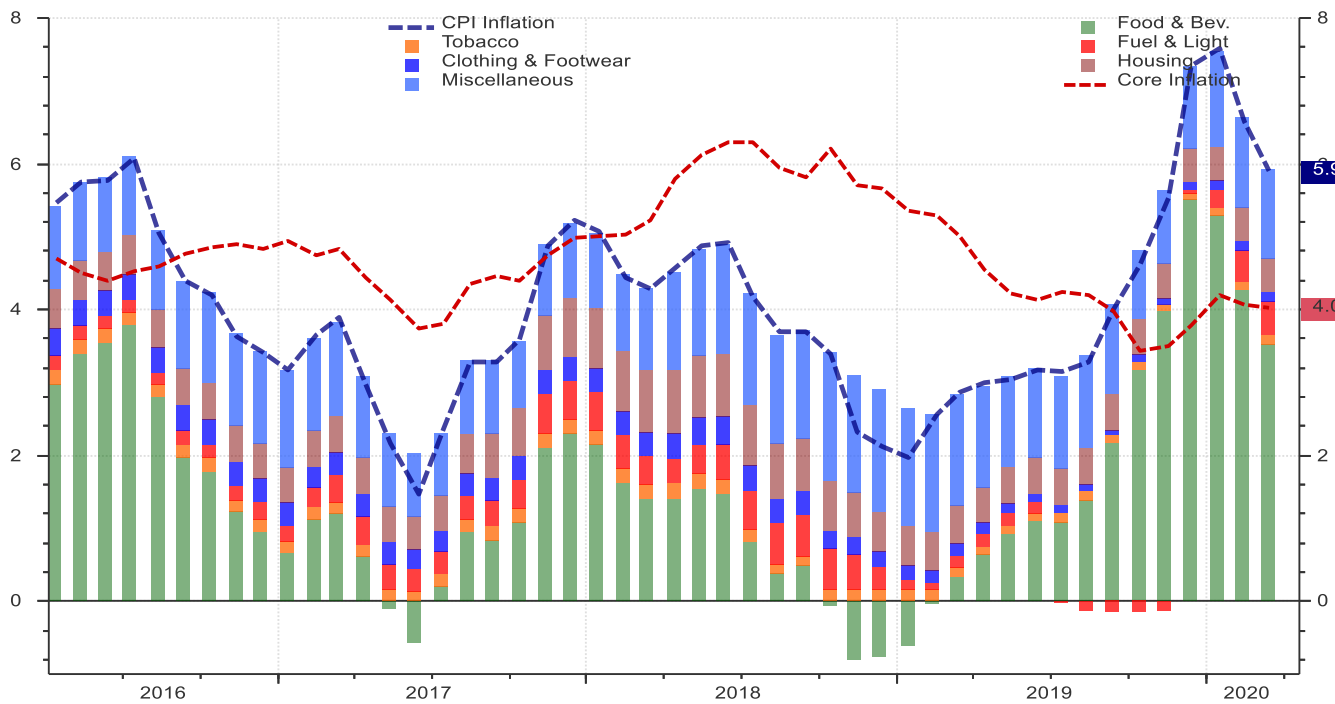
Figure 7: India inflation vs. interest rates


Source: Refinitiv Datastream, NSE

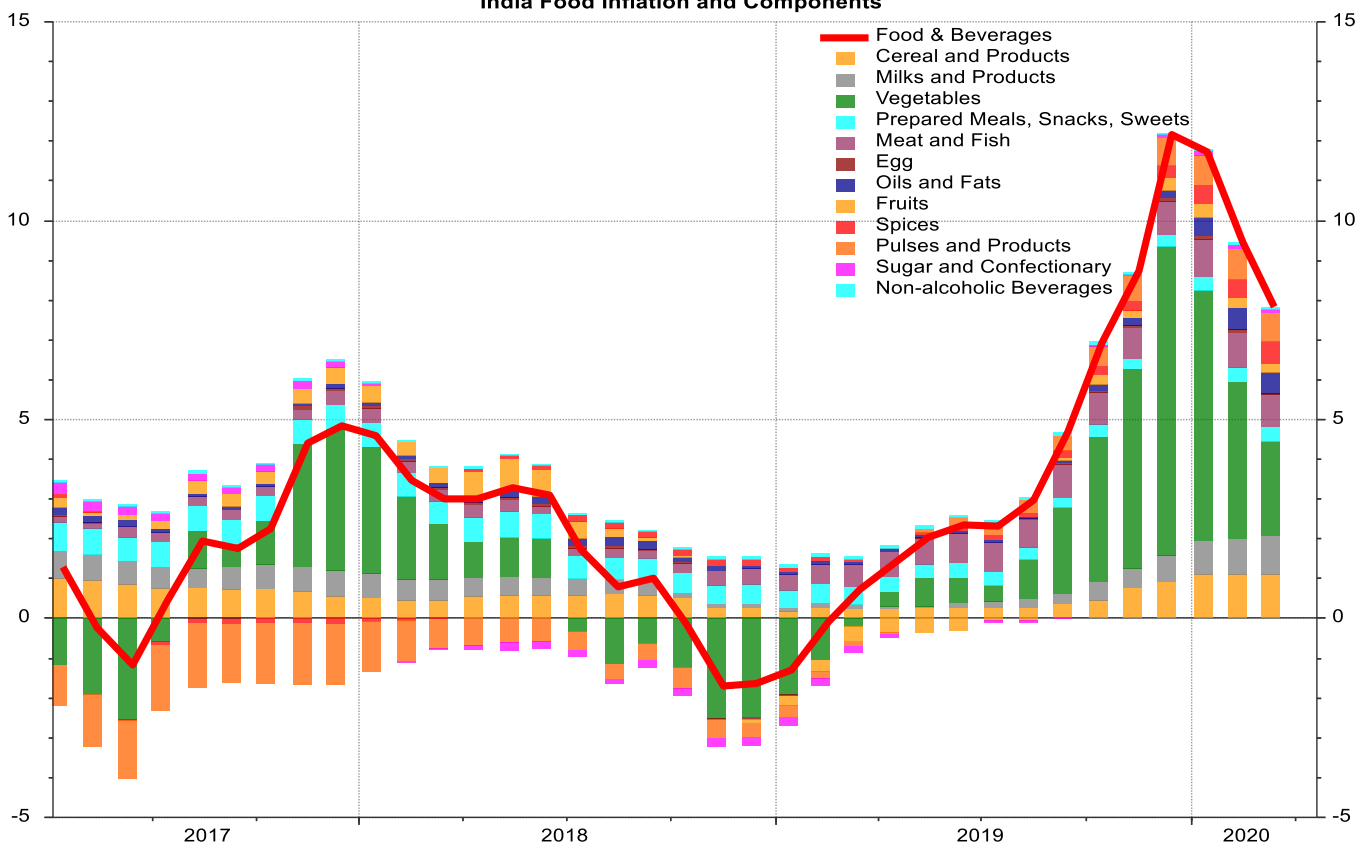
Figure 8: India consumer price inflation (CPI)



Source: Refinitiv Datastream, NSE

Figure 9: Category-wise contribution to India consumer price inflation (CPI)
India Consumer Inflation and Components (Mar 20)


Source: Refinitiv Datastream, NSE

Figure 10: Category-wise contribution to India Food and Beverages inflation (CPI)
India Food Inflation and Components


Source: Refinitiv Datastream, NSE

Figure 11: Fiscal and monetary measures announced since February 2020

Measures	Announcement date	Amount (Rs trn)
Monetary measures		
Long-term repo operations (LTROs)	06-Feb-20	1.25
Targeted long-term repo operations (TLTROs)	27-Mar-20	1.00
100bps cut in Cash Reserve Ratio	27-Mar-20	1.37
Enhanced borrowing under Marginal Standing Facility (MSF)	27-Mar-20	1.37
Targeted long-term repo operations 2.0 (TLTRO 2.0)	17-Apr-20	0.50
Special Liquidity Facility for mutual funds (SLF-MF)	27-Apr-20	0.50
Total monetary measures		5.99
<i>% of GDP</i>		<i>3.0%</i>
Fiscal measures		
PM Kisan Yojana	26-Mar-20	0.16
PM Jan Dhan Yojana	26-Mar-20	0.31
Free gas cylinders	26-Mar-20	0.13
PF contribution	26-Mar-20	0.05
Cash transfers to other sections	26-Mar-20	0.03
MGNREGA wage hike	26-Mar-20	0.06
Food-grain distribution	26-Mar-20	0.40
Pulses distribution	26-Mar-20	0.05
District Mineral Fund	26-Mar-20	0.25
Construction Workers Fund	26-Mar-20	0.31
Total fiscal measures		1.75
<i>% of GDP</i>		<i>0.9%</i>
Total measures announced thus far		7.74
<i>% of GDP</i>		<i>3.9%</i>
Stimulus announced by the PM	12-May-20	20
<i>% of GDP</i>		<i>10%</i>
Balance stimulus		12.26
<i>% of GDP</i>		<i>6.1%</i>

Source: RBI, Government, Media, NSE.

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