

Dip in industrial growth: time to change gears

It's more bad news for the United Progressive Alliance (UPA) government on the economic front, even as it looks forward to the general election in 2009. Industrial growth has dipped to a six-year-low of three percent in March this year. Coupled with raging inflation, the economic outlook is far from satisfactory at a time when both Prime Minister Manmohan Singh and Finance Minister P. Chidambaram were expecting to pat themselves on the back for a great five-year performance.

After having achieved consistent eight to nine percent growth, along with buoyant industrial output and a soaring Sensex, it looked as if the economic duo could do little wrong, despite the weak spot of low farm output and farmers' suicides.

Things seem to have gone horribly wrong lately, as inflation has reared its ugly head, probably the worst thing that can happen in an election year. The gloom continues with the latest news about the dip in industrial growth in March, the last month of fiscal 2007-08. This is a significant indicator as it can drag down the overall growth rate for the year. It also points to a continuing slowdown for industry in the current fiscal, which must be extremely disappointing as the corporate sector has virtually been on a roll for the last few years. At the same time, it is the galloping industrial growth in recent years that seems to have been one of the reasons for the sudden dip in March. The low three percent growth for the month came on the back of a phenomenally high 14.8 percent growth at the same time last year. It would have been difficult to top that level of increase this year.

The fact is that the government is in the proverbial cleft stick. The Reserve Bank of India (RBI) has been raising interest rates to combat inflation but this in turn has affected the growth story that could conceivably wind down in the next few months. For the UPA, of course, inflation is the priority as this can have potentially deadly consequences in next year's elections. But by putting the focus on prices, it has to hope that economic growth does not slow down. The latest data, however, shows that the RBI's moves to combat inflation by raising interest rates have begun to take their toll on industry, including the crucial manufacturing sector. There is a school of thought that has been arguing for a cut in interest rates to boost growth, but the RBI has decided to tackle the menace of high inflation and worry about growth later.

Clearly, it is time for both the RBI and the government to pause and reflect on their strategy to deal with inflation and growth. High interest rates have begun to hurt industry and are showing up in the slower growth data. Such high rates will not only give a push to inflation in the medium term but ultimately hit the common man in various ways, including rising cost of home loans. Besides, both the RBI and the government have repeatedly been emphasising that the major issue on the inflation front is the need to deal with supply side problems. So it is for the government to continue its efforts to improve availability of food products as well as critical raw materials like cement and steel to douse the flames of inflation.

Also one must not forget that a main reason for rising prices is globalisation and the fact that the entire planet is facing a crisis with regard to food and oil. Food prices are soaring all over the world and, to add to the problem, international crude oil prices have hit the roof. These are not issues that can be dealt with by the central bank.

Industry is already clamouring for a cut in interest rates to boost growth, especially in the manufacturing sector. It may be wise for the RBI to consider such demands favourably over the next

few months, especially if the fiscal and monetary measures already taken yield positive results and bring inflation below the high seven percent mark.

On the plus side, consumer electronics associations are reported to be contesting the data on consumer durables in the Index of Industrial Production (IIP), pointing out that new products like LCDs and laptops are not included in the index and older items like black and white TVs are still forming part of the data. There is in fact a feeling in the consumer durables industry that sales have been buoyant in contrast to the data released by the government. On the two-wheeler front, however, manufacturers are agreed that there has been a definite slowdown as sales have fallen largely due to higher interest rates on consumer loans. Capital goods have grown by a dismal 2.3 percent.

Most agencies are already revising their growth estimates for 2008-09. The expectation is that it will not reach the target of 8.5 percent and could be significantly lower. The overall growth for industry during 2007-08 is now pegged at around 8.1 percent, far lower than the double digit 11 percent growth recorded in the previous year. In the manufacturing sector, the situation is even worse with 2.9 percent recorded during March as against 16 percent a year ago. The government will clearly have to act fast to ensure that the slump in the manufacturing sector does not extend well into 2008-09. In case industrial growth does not pick up in the current fiscal, hopes of having consistently high growth over the next 10 years could well be dashed. This is clearly not the legacy that either Manmohan Singh or Chidambaram want to leave behind; so now is the time for them to revise their strategies to deal with the many ailments plaguing the economy.

(Sushma Ramachandran is an economic and corporate analyst. She can be reached at sushma.ramachandran@gmail.com)

Sushma Ramachandran (© IANS / India eNews)