Economic Slowdown - May 2019

What is the issue?

The recent numbers on Index on Industrial Production and other indicators signal an economic slowdown across sectors.

What are the recent indicators?

- **Automobiles** - Domestic sales of cars, commercial vehicles and two wheelers all contracted in April, 2019 from a year earlier.
- There is a decline of almost 16% in total automobile industry sales.
- This is an indication that consumption demand across markets - urban and rural, institutional and individual - is affected.
- Sales of commercial vehicles, a fair proxy for overall economic activity, slid 6% last month.
- A 16.4% drop in demand for two-wheelers extended the segment's slump into the new financial year, reflecting the rural distress.
- The data on passenger vehicles, which saw the steepest drop in almost 8 years, add to the weakening trend.
- **IIP** - The latest industrial output figures underscore the widespread nature of the demand drought.
- The Index of Industrial Production (IIP) for March shows output fell 0.1% from a year earlier to a 21-month low.
- The capital goods sector shrank by 8.7% on the back of an 8.9% contraction in the preceding month.
- Output of consumer durables fell 5.1% from a year earlier.
- The growth in consumer non-durables production slid to 0.3% from the 14.1% pace in March 2018.
- **Manufacturing**, which has a weight of almost 78% in the index, continues to be the biggest drag.
- Manufacturing output contracted by 0.4% after shrinking by a similar extent in February.
- Overall, the sector's growth slowed to 3.5% in the last fiscal, from 4.6% in 2017-18.

What are the possible reasons?

- The possible factors for the slowdown include declining growth of private consumption, weak increase in fixed investment, and muted exports.
- It could be a result of endemic demand deficiency, deepened by demonetisation.
- This was later made worse by the NBFC crisis triggered by the implosion of IL&FS and others.
- It is not clear if the remonetisation of the economy resolved the woes of small firms hit by disruption of working capital cycles and their inability to repay debt.
- On the other hand, the IBC mechanism has not been able to release the locked assets quickly.
- This could have added to the uncertain investment scenario.
- It is, however, true that there were feeble signs of an investment pick-up in 2018-19.
- This was reflected in higher credit offtake by corporates from SBI and ICICI Bank.
- However, it is not clear if the rise in bank credit offtake and external commercial borrowings by corporates will translate into greenfield investments.
- Banks went on a credit spree during the first phase, and unviable infrastructure was created.
- Resultantly, now the economy is dealing with legacy NPAs, with infirmities in the financial sector still haunting.

What are the implications?

- All these indicators make CSO's implicit fourth-quarter GDP growth assumption of 6.5% an overly optimistic number.
- At the global level, challenges are increasing against the backdrop of an escalating trade war between the U.S. and China.
- Also, the rising tensions in West Asia are beginning to push up energy costs.
- Given all these, Indian policymakers have to contend with an external sector that would likely only add to the domestic pressure.

What lies ahead?

- The distress in the farm sector may just ease marginally if the monsoon does turn out to be "near normal" as forecast.
- It could also help marginally encourage demand revival in the rural hinterland.
- However, concerted measures are needed by the government to help

reinvigorate demand.

- The government must also ensure that such a revival is robust, across-the-board and enduring.

Source: The Hindu, Business Line