Manufacturing: Is it Growing or Sluggish?

Guest Column

BL CHANDAK

IIP data on manufacturing sector for November 2014 shows a 3% growth over November 2013. This growth is due to low base effect as the manufacturing index in November 2013 and 2012 had declined by 2.8% and 0.8%, respectively over their corresponding month in the previous years. The manufacturing index was 177.8 in November 2011 which declined to 176.4 in November 2012 and further to 171.8 in November 2013. In the same month in 2014 the index at 177.0 is still lower than it was in November 2011.

The manufacturing index is based on physical output of various industries. From this it is clear that manufacturing production volume in November 2014 is even marginally lower than that in November 2011. The growth in manufacturing for April-November 2014 is mere 1.1%. The yearly average of manufacturing index increased marginally from 181.0 in FY12 to 181.9 in FY14 [growth of just 0.5 % over two years].

Over the past six years ending March 2014, the manufacturing index increased by just 3.3% p.a. All these are way behind the 12-14% growth envisaged under the New Manufacturing Policy. Even over a longer period manufacturing CAGR, at 6.8%, was lower than the 7.1% GDP growth during FY01-14. Manufacturing is the growth engine in an emerging economy. Its growth should be higher than that of GDP. Despite very high growth optimism, manufacturing growth prospects continue to be uncertain and discouraging.

Experiences world over show that many times persistent under-performance of industry despite favourable fundamentals is caused by systemic impairment in the financial system which affects saving-investment-growth nexus. In our case, it is essentially triggered by trust-deficit-induced systemic weaknesses in the inter-firm sales on credit arrangement or trade credit (TC) system as there is no apparent disorderly development in bank credit architecture.

In terms of financial intermediation, credit volume/activities, reach, inclusiveness and credit redistribution, the role of TC network is truly stupendous. The Intensity/pattern of intermediation of bank credit, private savings and suppliers' credit by firms through TC determine the volume of credit supply, level of demand for bank credit, credit multiplier, micro-liquidity and market liquidity. TC is too interconnected to financial networks and real sector to ignore. Systemic weaknesses in TC expose the financial system to contagion risk. Understanding and mapping these complex and dynamic interconnections in financial networks are essential to identify fault lines as these impact saving-investment-growth nexus and more so credit-intensive manufacturing sector.

> !
> Manufacturing index was 177.8 in Nov 2011 and 177 in Nov 2014

Explaining the sluggishness in manufacturing in terms of policy issues is oversimplification. Prof Nassim Taleb states that today in a highly interconnected world, consequences from small disturbances in one place can lead – very rapidly – to large effects in another or even generalised cascades. It is quite logical to construe that systemic weaknesses in all important TC can set off deep, widespread and enduring economic slowdown when with a less than 5% share in total US mortgage market, the subprime mortgage crisis could trigger prolonged global economic crisis.

Research is needed on generalised cascades arising from systemic weaknesses in TC. We have to understand its magnitude and mechanism of propagation for a meaningful intervention. Ignoring these will continue to impact manufacturing growth. NPA environment may deteriorate further as TC continues to be the lender of the last resort in respect of working capital for vast majority of firms.

BL Chandak, Ex-DGM, Small Industries, Development Bank of India

US Fed may Stick to Mid-year Rate Hike Plan Despite Volatility

Officials think US will be ready for tightening by June-Sept and falling oil prices are a positive for economy

Jonathan Spicer & Ann Saphir

US Federal Reserve Janet Yellen

New York | San Francisco: Tumbling oil prices have strengthened, rather than weakened, the Federal Reserve's resolve to start raising interest rates around midyear even as volatile markets and a softening US inflation outlook made investors push back the timing of the "liftoff". Interviews with senior Fed officials and advisors suggest they remain confident the US economy will be ready for a modest policy tightening in the June-September period, while any subsequent rate hikes will probably be slow and depend on how markets behave.

While they are hard-pressed to explain why bond yields have fallen so low, their confidence in the recovery stems in part from in-house analysis that shows falling oil prices are clearly positive for the US economy.

Internal models also suggest that a decline in longer-term inflation expectations probably does not signal a loss of faith in the Fed's 2% inflation goal.

Instead, the models attribute much of the recent decline in market-based measures of inflation expectations to increased investor confidence that prices will not spiral out of control, officials say.

Policymakers' public comments reflect that, as they sound unperturbed by what has been a steep drop in recent months. "I am watching the inflation expectation numbers but not drawing a conclusion that they call for any action or that they change in any serious way my outlook," Atlanta Fed President Dennis Lockhart told reporters earlier this week.

Some of those interviewed stressed that in the light of last year's strong jobs gains waiting until mid-year represented a cautious approach rather than an aggressive one, allowing the Fed to delay the rate liftoff if needed, particularly if inflation expectations turned sharply down.

However, with markets increasingly gripped by fears of global deflation and economic stagnation, futures traders are now betting the Fed will stay put at least until October, possibly until December.

Yet interviews with the Fed insiders reveal that while they keep an eye on volatile markets they remain confident that unexpected overseas headwinds will not derail the US economy.

Cheap Gas Boost

So far, signs of domestic price weakness, such as slow-growing wages, have not shaken the central bank's faith that inflation will rebound once energy markets stabilise, the interviews showed. In fact, cheaper gasoline and the boost it gives particularly to lower- and middle-income households could be just the shot of economic confidence the Fed needs to tighten policy after six years of near-zero rates.

Consumer Prices Fall 0.4% in Dec

Washington: US consumer prices recorded their biggest decline in six years in December and a gauge of underlying inflation held steady, which could bolster the case for delaying the first interest rate increase from the US Federal Reserve. The Labor Department said on Friday its Consumer Price Index fell 0.4% last month, the largest drop since December 2008, after sliding 0.3% in November. In the 12 months through December, CPI increased 0.8%. It was the weakest YoY reading since October 2009, and followed a 1.3% rise in November. – Reuters

Fed to Establish a Community Advisory Council

Washington: The US Federal Reserve said on Friday that it will establish a community advisory council of 15 citizens to meet regularly with central bank officials for a broad conversation on the state of the economy.

The move comes as the Fed is pressured by labour and low-income groups arguing for continued low interest rates. Fed Chair Janet Yellen and other Fed officials have met with these groups from late last year to hear their concerns, a departure from the practice of previous central bank leaders. The Fed said the panel will have "a particular focus on the concerns of low- and moderate-income populations." – Reuters

'No Commercial Sale from Auctioned Coal Blocks'

Our Bureau

Kolkata: None of the 204 coal blocks that are to be auctioned in two tranches, this year and the next, will be given away for commercial mining for sale in open market, coal secretary Anil Swarup said in Kolkata on Friday.

"In the first tranche, under which 101 blocks will be auctioned, the government intends to place under the hammer blocks meant for projects which are ready for production — be it in power, steel or any other segment," said Swarup, making it clear that the blocks will not be given for commercial market sale.

The second tranche of 103 blocks is likely to be taken up after March 2016, the secretary said. "In this tranche, the government may auction blocks to projects that may have units under construction. A final decision on eligibility for participating in auctions for the second tranche will be decided later," he added.

The government is targeting total production of 500 million tonnes for these 204 blocks by 2020. By then, monopoly miner Coal India is expected to double its production to 1 billion tonnes and meet the nation's projected demand of 1.5 billion tonnes of coal per year.

The tranche of 101 coal blocks will be auctioned in three sets. In the first set, 42 blocks with peak production potential of 90 million tonnes every year will be sold. The second set of 32 blocks is expected to have capacity of 140 million tonnes, while the third set of 27 blocks could produce 140 million tonnes per annum – totalling around 350 million tonnes. The second tranche of 103 blocks is expected to produce 150 million tonnes a year.

In Touch with Environment Ministry

Swarup said that the coal ministry will be monitoring project status and will be in constant touch with the environment ministry so that clearances are received in time. The government has also decided that clearances received by former block operators will be transferred to the new operators after auctions. "They need not apply afresh for clearances already received," he said.

A project monitoring group has been formed that will keep tabs on project progress for both the private sector and Coal India. This group will also facilitate block operators so that projects come up in time.