FICCI QUARTERLY SURVEY

ON

INDIAN MANUFACTURING SECTOR

March 2011

Federation of Indian Chambers of Commerce & Industry

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Introduction

FICCI has conducted its Quarterly Manufacturing Survey for the quarter January-March 2011 (Q-4). The survey has tried to gauge the expectations of manufacturers for Q-4 from major sectors like textiles, capital goods, metals, chemicals, machine tools, tyres, cement, consumer electronics, automotive, leather & footwear, paper, forging etc. Responses have been drawn from over 400 manufacturing units belonging to both large and SME segment.

Growth Scenario

Overall the sentiments and expectations of manufacturing sector for Q-4 have seen a dip vis-à-vis last quarters. In the survey, 60% respondents reported that they expect higher growth in their sector for Q-4 vis-à-vis Q-4 2009-10. This is a significant fall with regard to previous two quarters in which around 68% (Q-3) and 71% (Q-2) respondents felt that they were expecting higher growth in their sectors.

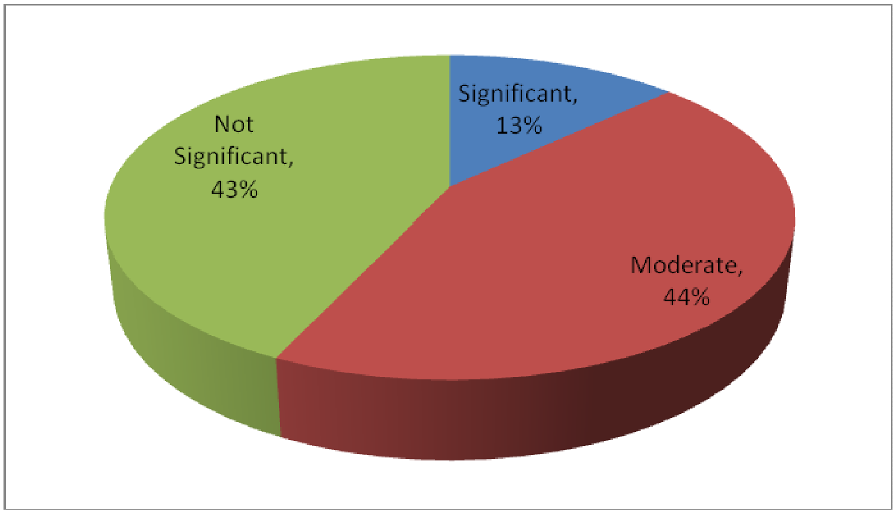
Around 77% respondents feel that the growth in the manufacturing sector is going to moderate for Q-4. While a number of factors are constraining the growth of manufacturing sector, but most important being the rise in the cost of capital due to monetary tightening measures of RBI. Below, we have given the response on RBI's monetary tightening measures.

Cost of Finance

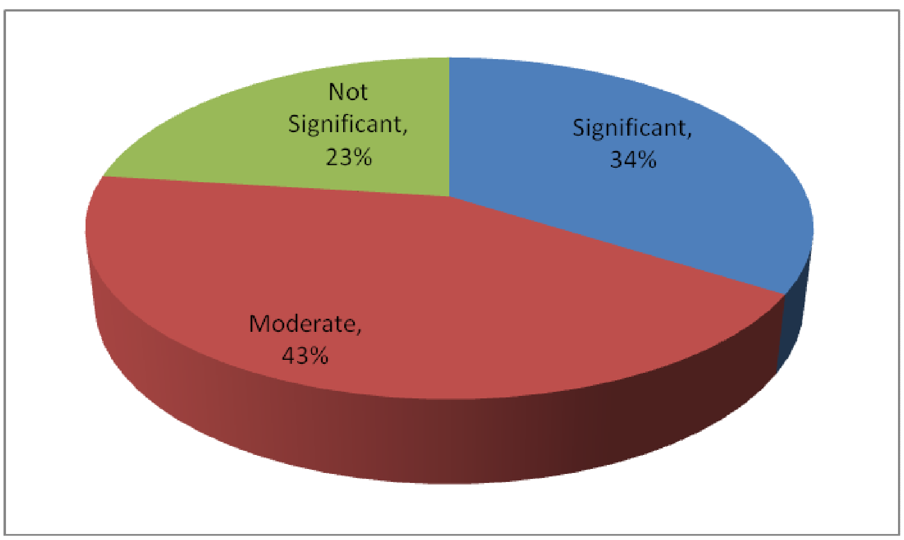
Hike in the policy rates of RBI in the last few months has significantly affected the cost of borrowing for manufacturers. In Q-4, over 34% respondents reported that their cost of borrowing has increased significantly in last two to three months. Around 43% respondents felt that the hike in policy rates had a moderate impact on their cost of borrowing. But compared to previous Quarter (Q-3) the situation has worsened. In Q-3, as per FICCI Survey, only 13% respondents felt that their cost of borrowing had increased significantly, whereas in Q-4 34% respondents are feeling the heat of rising interest rates. Sectors where the impact is seen the most are Automotive, Cement and Tyres.

Impact of Hike in RBI Policy Rates on Cost of Financing

Quarter-3 2010-11



Quarter-4 2010-11



Source: FICCI Survey

Economic environment

Quite a few respondents in the survey have reported that uncertainty in economic environment has increased further. Over 40% respondents of the survey reported that economic uncertainty is acting as a significant constraint for the growth of the sector. Another 28% respondents saw economic uncertainty as a moderate constraint for the growth of the sector.

Capacity Utilization

In terms of capacity utilization there is not much difference or variation between Q-4 and Q-3. In Q-4, around 53% respondents reported that they were operating at higher capacities vis-à-vis last year, as compared to 52% in Q-3. Similarly, around 32% respondents reported that they were operating at same level of capacity utilization as last year in Q-4- same percentage as in Q-3.

Capacity Addition

In terms of capacity addition, around 52% respondents plan to have capacity additions in next 6 months. However, a significant proportion i.e. 48% still feels that there are number of constraints to capacity additions. Sectors where majority of the respondents reported that their capacity additions are not coming through significantly are textiles and steel. In other sectors like Automotive, Capital Goods, Machine Tools, Leather, Chemicals, Cement, Paper and Forging there is going to be moderate increase in capacities.

Order Books

The demand conditions for manufacturing sector in Q-4 is similar to that in Q-3. In both the quarters around 54-55% respondents have higher order books for the quarter compared to previous quarter.

Employment

Around 44% respondents reported that they intend to increase their workforce in next 3 months. Sectors where majority of the respondents intend to hire new workforce are Automotive, Tyre, Leather, Capital Goods, Electronic Goods and Forging.

Sectoral Growth

Looking at growth expectation in different sectors, five out of fourteen sectors in the survey are likely to witness strong growth of over 10% in Q-4. These sectors are Capital Goods, Automotive, Machine Tools and Consumer Durables. For three sectors namely Chemicals, Forging and Tyre growth is likely to be moderate (between 5 to 10%) in Q-4 as compared to last year. Sectors like Cement, Paper, Steel, Metals, Textiles and Miscellaneous are likely to witness low growth of less than 5% in Q-4.

Sector	Growth
Cement	Low
Paper	Low
Steel & Metals	Low
Textiles	Low
Miscellaneous	Low
Chemicals	Moderate
Forging	Moderate
Tyre	Moderate
Machine Tools	Strong
Automotive	Strong
Electronics & Consumer Durables	Strong
Leather & footwear	Strong
Capital Goods	Strong

Note : Strong > 10%; 5% < Moderate < 10%; Low < 5%

Source: FICCI Survey

Exports

Exports seem to be picking-up for the manufacturing sector in Q-4. Over 54% respondents reported that they are expecting higher exports in Q-4 vis-à-vis last year. Almost, all the sectors are expecting growth in their exports for Q-4 vis-a-vis last year.

TEXTILES

- In the current quarter i.e. January- March 2011, 87% respondents are expecting increased or same production levels. However, average production growth is expected to be around 4% during January- March 2011 implying that the sector may witness a marginal slowdown vis-à-vis last quarter.
- In January- March 2011, 73% of textiles firms are expecting to have either same or higher number of orders as in October- December 2010.
- Average capacity utilization is hovering around 84% in the textiles sector with almost half of the respondents operating at a capacity utilization more than that of last year. However, majority of respondents (60%) are not planning to increase their capacity in next 6 months but those who are planning to increase their capacity are planning to increase it in the range of 5-50%. Firms in textiles sector are facing the following problems in adding capacity:
  - ✓ High real estate costs making business unavailable
  - ✓ TUF scheme has been put on hold by Ministry of Textiles, it is a great cause of concern for the sector
  - ✓ Labor Issues
  - ✓ Shortage in power
  - ✓ Raw material prices of cotton
  - ✓ Rising cost of capital
- Around 60% respondents have reported that their exports in October- December 2010 were higher than the same quarter last year. But textile exports may see a downturn in the current quarter since only 33% respondents are expecting higher exports vis-à-vis the year ago quarter. More so because of the existing restrictions on yarn exports.
- Two third of the respondents in the textiles sector are not planning to hire new workers in the next three months and one third of the respondents in the textiles sector who are planning to hire new workforce are thinking of increasing their manpower by 4-25%.

- 73% respondents are expecting the manufacturing growth rate to be moderate but they feel the following incentives need to be provided by the Government to enhance growth:
  - ✓ Restore the suspended TUFs Scheme for textile industry.
  - ✓ Remove quantitative ceiling on cotton yarn exports
  - ✓ Check on Cotton Prices
  - ✓ Finance availability needs to be smooth and interest rates need to be lowered
  - ✓ Amend labour laws to make them industry friendly
  - ✓ Need to have a strong focus on improving infrastructure & utilities
- 87% respondents in the sector reported that policy rates hike by Government has impacted their costs of borrowing. For some respondents the impact was significant while for others the impact on cost of borrowing was moderate.
- Units in the textiles sector are significantly affected by high prices of raw materials/intermediates, deficiency of raw materials, deficiency of power, labour related issues and availability of skilled manpower. Other issues faced by textile sector are shortage of finance, lack of domestic and export demand, competition from imports and uncertainty of economic environment.
- Restriction on cotton yarn exports will have serious implications on expansion plans of spinning industry and delay in release of incentives like TUFS, power subsidy, sales tax reimbursement are also hurting the textile producers.

Capital Goods sector

- In the current quarter, almost all the respondents expect either an increase in production vis-à-vis January-March 2010. The average increase is expected to be around 23%. Almost all the respondents have reported that their order books are likely to experience an increase in January-March 2011 compared to October-December 2010 Quarter.
- Currently, the capacity utilization in this sector is hovering around 80-85% and for 88% respondents the capacity utilization is higher as compared to previous year. Most of the

respondents have plans to add capacity in next 6 months. On an average, the capacity addition is expected to be around 10-20%.

- The scenario is not that encouraging in export for this sector. Most of the respondents reported either same or lower level of exports in October-December 2010 quarter as compared to October-December 2009. The situation is likely to improve in the current quarter as around 60% respondents expect their exports to increase in the current quarter vis-à-vis last year and merely 15% expect them to fall as compared to January-March 2010.
- 75% of the respondents in this sector indicated that they are planning to hire new workforce in the range of 3-20% in the near future.
- Almost all the respondents in the sector expect the growth rate of manufacturing sector to moderate in the coming months.
- Almost all the respondents reported that RBI's monetary policy tightening has moderately impacted their cost of borrowing.
- High price of raw material and lack of skilled manpower are two most significant constraints for the sector which can affect growth of the sector. Apart from this, the sector has also urged the Government to provide level playing field vis-à-vis imports.

Machine Tool Industry

- Most of the respondents are expecting higher levels of production in January-March 2011 quarter as compared to same quarter of previous year. The increase is reported to be as high as 50% as compared to January-March 2010 but some of them have specified the reason for this increase to be lower production levels in January – March 2010. Respondents are also expecting almost same level of orders in January - March 2011 compared to October-December 2010.
- At present, the machine tools industry is operating at a capacity of 90% and above. Majority of the respondents reported an increase in capacity utilization as compared to last year and they have plans to add further capacity in next six months by around 50%. As per the

respondents, one of the main hindrances in their expansion plans is bottlenecks in the supply chain.

- Majority of the respondents reported an increase in their exports in October-December 2010 as compared to October-December 2009. The similar situation is expected to prevail in the current quarter i.e. January-March 2011 also as most of the respondents expect an increase in exports as compared to last year.
- Most of the respondents do not have plans to hire new workforce.
- Majority of the respondents believe that the growth rate of manufacturing sector is going to moderate in the coming months. Machine Tool industry has also suggested that Government needs to control inflation, reduce rate of interest for manufacturing sector to revive growth in manufacturing sector.
- The sector also reported a moderate increase in the cost of borrowing due to increased policy rates by RBI.
- Some of the significant constraints for this sector are shortage of working capital finance, competition faced from imports and lack of skilled manpower. Apart from this, prices of raw material, deficiency of power and labour related issues are other important constraints cited by the industry.

CEMENT

- Growth is likely to continue in Cement Sector in the next quarter with production expected to grow by 5% in January- March 2011 compared to 2010.
- Around 90% respondents have reported that their order books are likely to see a downturn in January- March 2011 compared to the previous quarter.
- Capacity utilization is in the range of 70 to 90% in the cement sector, which is less than that of last year for 95% respondents. Majority of the firms are planning to add capacity in next six months. On an average, capacity addition is likely to be 10%. Cement producers are hampered by high coal costs and environment clearances while adding capacity.

- Exports of Cement have declined in October- December 2010 compared to last year. Exports are not likely to see a revival in the next quarter also and are likely to be 20% less than January- March 2010 quarter.
- Most of the firms in the cement sector are planning to hire new work force in next three months but only moderately.
- Most of the respondents in the cement sector believe that the growth rate of manufacturing is likely to be moderate in 2010-11. Respondents feel that following steps need to be taken by the Government to enhance growth of the sector:
  - ✓ Investment in the infrastructure sector is required to boost the demand for cement products and speed up the planned projects
  - ✓ Interest rates need to be reduced.
  - ✓ Excise duty and VAT need to be reduced
  - ✓ Inflation needs to be tackled on an urgent basis
  - ✓ GST needs to be implemented soon
- 50% respondents in the Cement sector reported that monetary tightening by the Reserve Bank of India has significantly impacted their costs of borrowing. However, the remaining respondents are moderately affected by Monetary tightening.
- High prices of raw materials is acting as a significant constraint for the sector. Other issues which are significantly affecting growth of cement sector are deficiency of raw materials, uncertainty of economic environment and lack of domestic demand. Some of the respondents reported deficiency of power, shortage of working capital finance, lack of export demand, competition faced from imports and inadequate availability of skilled labor as factors moderately affecting their growth.

Consumer Electronics

- In the current quarter, i.e. January-March 2011 also majority of respondents expect increased level of production. Most respondents have reported that their orders are expected to increase in January-March 2011 as compared to October-December 2010.

- On an average the capacity utilization in this sector stands at around 90% and above. Most of the firms have reported that their capacity utilization is higher as compared to last year's capacity utilization. But most of the firms are not planning any further increase in capacity in next 6 months.
- Most of the electronics producers reported an increase in exports during October-December 2010 compared to same quarter last year and the trend is likely to continue in the next quarter also.
- Most of the respondents reported that they are planning to hire new workforce in next 3 months.
- Most of the respondents believe that the manufacturing sector will continue to experience high growth rate in the coming months.
- Around 60% respondents reported that tightening of monetary policy by RBI has moderately impacted their cost of borrowing.
- For electronic industry prices of raw material has been identified as the most significant factor affecting their progress. Other important constraints to the industry are deficiency of power and competition faced from imports.

Forging Industry

- Most of the respondents expect an increase in the production levels in January-March 2011 quarter vis-à-vis last year. The average increase is reported to be around 10%. Almost all the respondents expect an increase in orders in January-March 2011 quarter as compared to October-December 2010 quarter indicating better demand conditions.
- Currently, forging industry is operating at an average capacity utilization of 50%-70%. Most of the respondents have reported an increase in their capacity utilization as compared to last year. Some of them also reported that they have plans to increase their capacity further in the next 6 months.
- Exports for most of the respondents increased in October- December 2010 via-a-vis the same quarter last year and are likely to grow in the next quarter as well.

- Most respondents are planning to hire workforce in next 3 months.
- The forging industry is very confident of growth of Indian manufacturing sector in coming months.
- The sector also reported a moderate increase in the cost of borrowing due to increased policy rates by RBI.
- Most of the respondents in this sector reported high prices of raw materials, deficiency of power and labour related issues to be the most significant constraints to their growth.

Metal and Metal Products

- In the quarter January-March 2011, around 88% respondents expect either higher or same production levels as compared to January-March 2010. The average increase in the production level is expected to be around 5%. 75% of the respondents expect same number of orders in the quarter January-March 2011 as compared to October-December 2010. The rest of respondents expect an increase in number of orders.
- Currently, the industry is operating at an average capacity utilization of 85% and for 40% respondents it is higher than that of last year. For the rest of them the capacity utilization is the same as compared to the last year. Around 88% respondents reported that they are not planning to increase their capacity in next 6 months. Some of the problem areas mentioned by the industry are as follows:
    - Volatility in raw material prices like, scrap, DRI, Fuel
    - Power shortage
- Almost 75% respondents reported higher level of exports for October-December 2010 via-a-vis October-December 2009. In the current quarter also, almost 50% respondents expect higher level of exports as compared to January-March 2010 and 25% respondents expect same level of exports as last year.
- Around 88% respondents reported that they do not have any plans to hire new workforce in next 3 months.

- Almost all the respondents expect the manufacturing growth to moderate in the coming months. The following points have been suggested by the industry to revive the growth rate of the sector:
    - More emphasis on infrastructure development and creating more demand by way of spending on new infrastructure.
    - Lower interest rate for working capital & long term.
    - Power and fuel cost regulation should not change frequently, that too post consumption.
- Over 50% respondents feel that tightening of monetary policy by RBI has significantly impact the cost of borrowing of the industry.
- Higher price of raw material has been reported as the most significant constraint for manufacturers in this industry. Around 65% respondents reported it to be the most significant constraint. Other major problems faced by this industry have been identified as shortage of power and raw material, competition faced from imports and lack of availability of skilled labour.

CHEMICALS, FERTILIZERS AND PHARMACEUTICALS SECTOR

- 90% respondents are expecting either same or increased production in the current quarter vis-à-vis the same quarter last year but growth is likely to slow down in the current quarter and the average growth is likely to be 8%.
- 89% respondents are expecting either same or higher number of orders in January-March 2011 compared to what prevailing in October- December quarter. Only 11% respondents are expecting a fall in the number of orders.
- Capacity utilization stands at around 80% in chemical, fertilizers and pharmaceuticals sector. Current capacity utilization is higher than last year for two third of the respondents. Also, 67% manufacturers are planning to add capacity in next six months in the range of 10 – 50%. Firms in this sector are constrained by inadequate supply of

inputs like natural gas. Also, Government policies related to environment need to be more investor friendly.

- In October- December 2010, 56% respondents reported an increase in exports vis-à-vis last year. Exports scenario is likely to remain same in the current quarter also i.e January - March 2011.
- Around 67% respondents are not planning to hire any new workforce in next 3 months and those who are planning to hire are planning to do so at a marginal rate only (5%).
- 67% respondents are hopeful that the manufacturing sector will grow in 2010-11 though at a moderate rate, following actions need to be taken by the Government:
    - ✓ Need clarity and transparency in Government regulations on licensing and setting up of new facilities.
    - ✓ Interest rates need to be lowered and liquidity needs to be improved.
    - ✓ Petroleum prices need to be stabilized
    - ✓ Government should encourage manufacturing
    - ✓ Inflation control and fiscal management
    - ✓ Need to have a favorable policy for investment in fertilizer sector
- For one third of respondents, hike in policy rates by RBI has lead to a significant rise in cost of borrowing and for another 44% respondents RBI rate hike has increased the cost of borrowing but by a moderate magnitude.
- High prices of raw materials, uncertainty of economic environment, shortage of skilled labour and competition faced from imports are significantly impacting the growth of chemical sector. Deficiency of Power, labour issues, shortage of working capital finance, deficiency of raw materials, lack of domestic and export demand are other constraints faced by chemical and fertilizer firms.

Automotive

- In the current quarter, almost 70% respondents expect an increase in their production as compared to last year's quarter. The increase is expected to be around 30%. 90% of the respondents are expecting an increase in number of orders in January-March 2011 compared to October-December 2010 quarter.

- More than 60% respondents have reported an increase in capacity utilization in October-December 2010 quarter vis-à-vis last year. The average capacity utilization in the industry stands at around 80%. 60% of the respondents in the automotive sector are planning to expand their capacity further by an average of 25-30%. Some of the respondents have mentioned lack of skilled manpower, land acquisition etc as some of the problems faced by industry in planning their capacity expansion.
- 60% respondents in automotive sector have reported an increase in exports in October-December 2010 quarter. Similar situation is likely to prevail in the current quarter also with 60% respondents expecting their exports to increase as compared to last year.
- 90% respondents are planning to hire new workforce in coming 3 months by an average of around 40%.
- 90% respondents expect the growth rate of manufacturing to moderate in the coming months and following are some of the suggestions given by the industry to revive the growth in the sector:
    - Easier land acquisition norms
    - Lower interest rates, lower inflation, man power availability.
    - Proper power at reasonable rate. Good infrastructure.
    - Training institutes to develop skilled labour.
    - Control over prices of crude oil and other important raw materials.
    - Constant check of industrial inflation
    - Boost to JNNURM (Jawaharlal Nehru National Urban Renewal Mission) projects
    - Reduction in PLR for term and short terms
    - Single window facilities declared by Government should be made available to the industry.
    - Control inflation & increase demand stimulus measures. Investment in new infrastructure projects is required.
    - Manage political instability.

- Almost all the firms in this sector have felt that hike in policy rates by RBI has resulted in increased cost of borrowing for them and 67% of them have indicated that the impact has been significant.
- Prices of raw material, archaic labour laws and inadequate availability of skilled labour have been identified as some of the most important constraints for automotive industry. Some of the manufacturers have also reported uncertainty of economic environment as a constraint to their growth.

Tyre Industry

- For January-March 2011 quarter, most of the respondents expect higher production levels. The production is expected to increase by 8-10%. Almost all the respondents expect either higher or same number of orders in Q-4, indicating robust demand.
- On an average, the capacity utilization in the tyre industry is in the range of 70-90%. It is higher than October-December 2009 quarter for most of the respondents. Also, majority of respondents are planning to add capacity in next 6 months.
- On exports front, majority of the respondents have experienced an increase for October-December 2010 quarter as compared to same quarter in 2009. In January-March 2011 quarter also, tyre manufacturers expect higher level of exports as compared to same quarter of 2010.
- The tyre industry is planning to hire workforce in next 3 months.
- Almost all the respondents in the sector believe that the manufacturing growth rate is expected to moderate in the coming months and to revive the growth, the industry has suggested the government to lower tariff rates on raw materials which are not available domestically, facilitate FDI and reduce interest rate and thereby improve access to credit.
- One of the major & significant constraints for this sector is hardening of raw material price and deficiency of raw material, particularly of natural rubber. Shortage of working capital finance, uncertainty in economic environment and competition faced from imports are some of the other important challenges for the sector.

LEATHER AND FOOTWEAR

- Leather sector is likely to see a revival in growth in the current quarter (January- March) 2011 as 86% respondents are expecting higher production level vis-à-vis January- March 2010. Production is likely to increase in the range of 5-60%.
- Order books of almost all the respondents are likely to remain same or increase in January- March 2011 compared to previous quarter.
- The average capacity utilization in this sector is reported to be 70% in October-December 2010. Most of the respondents have reported an increase in their capacity utilization vis-à-vis last year. Around 86% respondents are planning to add capacity in next six months and addition is likely to be in the range of 10 – 50%. Leather and Footwear producers are having following issues in capacity addition:
  - ✓ Shortage of working capital finance
  - ✓ Delay in clearances from Government departments
  - ✓ Inadequate Infrastructure
  - ✓ Shortage of power
- During October- December 2010, exports of half of the respondents registered a growth. Scenario is likely to strengthen in January- March quarter as 85% respondents are expecting higher exports vis-à-vis the same quarter last year.
- Majority of the firms in the leather sector reported that they are planning to expand their workforce in next three months. Average increase in workforce is likely to be around 11%.
- 86% of the respondents in this sector are sanguine about growth in manufacturing sector in 2010-11. However, following steps need to be taken by Government to sustain this growth:
  - ✓ Need to check rise in prices of raw materials
  - ✓ Easier credit facility with lower interest rates.
  - ✓ Improve existing infrastructure

- ✓ Training to unskilled labor
- ✓ More incentives like drawback benefits need to be provided

- Monetary tightening by RBI has impacted the cost of borrowing of 86% leather & footwear firms. Impact was significant for half of the borrowers but for the other half impact was moderate.
- Firms in leather and footwear sector are significantly constrained by high prices of raw materials, deficiency of raw materials, lack of export demand, uncertainty of economic environment and availability of skilled manpower for their operations. Other factors acting as impediments for leather sector are deficiency of power and labour issues.

PAPER

- Production is likely to slowdown in January- March compared to the last quarter as average growth is reported at 5%.
- Order books of paper manufacturers are likely to show the same trend in January-March as October- December quarter.
- Capacity utilization stands at 90% in paper sector which is more than last year for majority of producers. Also, most of the producers are planning to expand their capacity, on an average by 5%.
- Exports of paper manufacturers have witnessed growth in October- December 2010 compared to the same quarter last year. In January- March also respondents in this sector are expecting higher exports than last year.
- Most respondents in the paper industry are not planning to hire workforce in near future.
- Paper manufacturers believe that manufacturing growth rate will be moderate in 2010-11 and government needs to carry on with stimulus measures.
- Also, hike in policy rates by RBI has moderately impacted the cost of borrowing of paper producers.

- High prices of raw material and deficiency of raw material are acting as significant constraint for the paper manufacturers. Labor related issues, competition faced from imports and availability of skilled labor are other issues faced by the paper industry.

MISCELLANEOUS INDUSTRY

- Production is likely to grow further in January- March since 80% of the respondents are expecting an increase in production. Average rise in production is expected to be around 3%.
- 80% respondents are expecting higher orders in January- March 2011 compared to October- December quarter.
- Units under the miscellaneous category are reportedly running at around 64% of their capacity. For most of the respondents the capacity utilization is same or more than last year. One fifth of the units are planning to enhance their capacity by around 10-15%. Firms belonging to Miscellaneous sector are facing following problems while adding capacity:
    - ✓ Uncertainty in economic condition
    - ✓ Uncertainty in future orders
    - ✓ Power shortage
- Exports of two third of the units in the miscellaneous category were higher than last year in October- December 2010 and most of the firms are expecting higher exports in January- March 2011 also vis-à-vis the same quarter last year.
- Around 80% respondents reported that they are not planning to increase their workforce. Rest of the respondents are planning to increase 3-5% of their workforce in next few months.
- 50% of the respondents are sanguine about the growth prospects of manufacturing but they expect the following things needs to be done in order to sustain this growth:
    - ✓ Control over raw material cost & availability
    - ✓ Provide training to enhance the skills of labor

  - ✓ Continuous power availability
  - ✓ Support to manufacturing sector through existing stimulus

- For majority of the respondents, hike in policy rates by RBI has resulted in increase in their borrowing costs.
- High prices and deficiency of raw materials, deficiency of power, uncertainty of economic environment and lack of skilled manpower are significantly affecting the growth rate of this sector. Lack of domestic and export demand, labor issues, shortage of finance and competition from imports are other hindrances for the miscellaneous sector.