

Developments during 2003-04

5.6 After the drought of 2002 and the POL price increases resulting from tension in the Gulf region, the year 2003-04 began with an inflation rate of 6.7 per cent. However, with the ebbing of hostilities in Iraq and the end of the war, the pressure on crude prices gradually eased off, giving temporary relief on the inflation front. The annual point-to-point inflation rate based on the WPI after peaking at a high of 6.9 per cent in the first week of May 2003, decelerated continuously, reaching a low of 3.9 per cent in end-August, 2003.

5.7 The interplay of different factors— increase in energy prices, rise in prices of food articles- led to a firming of the inflation rate during September-November 2003 and it

hovered around the 6 per cent level in December 2003. A further firming of energy and primary product prices resulted in the inflation rate crossing 6 per cent in January 2004. However, inflation rate softened during March 2004 and fell to below 5 per cent. The year 2003-04 ended with an annual point-to-point inflation rate of 4.6 per cent, while the 52 week average inflation rate was 5.5 per cent (Table 5.3). The high point-to-point inflation through much of 2003-04, and its sharp deceleration in March 2004, was partly because of the carry over of the price increase that took place in the last quarter of 2002-03, especially March 2003 (Table 5.2).

Table 5.2 : Point-to-Point inflation rate based on WPI

(Per cent)

Month	WPI (Base : 1993-94=100)		
	2001-02	2002-03	2003-04
APR	5.5	1.5	6.6
MAY	5.5	1.6	6.5
JUN	5.4	2.4	5.4
JUL	5.3	2.8	4.6
AUG	5.4	3.3	3.9
SEP	4.5	3.5	4.9
OCT	2.9	3.1	5.1
NOV	2.6	3.4	5.4
DEC	2.1	3.3	5.8
JAN	1.5	4.2	6.5
FEB	1.4	5.3	6.1
MAR	1.8	6.0	4.8
Average	3.6	3.4	5.5

Table 5.3 : Annual inflation rate based on Wholesale Price Index (base 1993-94=100)

(Per cent)

	End of year	52 week average
1995-96	4.4	8.0
1996-97	5.4	4.6
1997-98	4.5	4.4
1998-99	5.3	5.9
1999-00	6.5	3.3
2000-01	5.5	7.2
2001-02	1.6	3.6
2002-03	6.5	3.4
2003-04	4.6	5.5

5.8 The manufacturing sector is the major contributor to inflation accounting for nearly 80 per cent of the inflation in 2003-04. While the year end point to point inflation rate for the primary group in 2003-04 remained below 2 per cent, the same for the manufactured and fuel products groups were 6.7 and 2.5 per cent, respectively (Figure 5.1). Non-food articles in the primary products group, including fibres, raw cotton, oilseeds and sugarcane, recorded a high price rise during

the year 2003-04, consequent to the production shortfalls resulting from the drought of 2002. Within the manufacturing sector, food products, edible oils, textiles, leather and leather products, basic metal and alloys and iron and steel were the prime movers.

i. Manufactured products

5.9 Though there were some signs of a revival of the manufacturing sector at the end of 2002-03, the year 2003-04 started with sure signs of a pick up in industrial activity. The annual point-to-point inflation rate for the manufacturing sector remained in the range of 4-7 per cent during the year. The inflation rate in some major products in 2003-04 is given in Table 5.4.

Table 5.4 : Price increase in some major manufactured products

Major groups	Rate of inflation (per cent)	
	52 weeks average 2003-04	End March 2003-04
Manufactured products	5.7	6.7
Sugar	0.7	16.9
Edible oils	14.4	6.6
Textiles	7.7	8.8
Wood & wood products	0.2	0.3
Leather & leather prod	12.9	15.1
Chemicals & chemical prod	1.9	0.1
Urea	0.2	0.0
Cement	1.2	1.3
Basic metals & alloys	15.6	28.5
Iron & steel	26.3	34.6

5.10 The price rise in the manufactured products group witnessed during the first two months of 2004 was largely due to a rise in the prices of steel and sugar. Steel prices were pushed up by demand-supply imbalances and high international prices. Though the custom duty on steel imports was reduced from 25 per cent to 20 per cent in the month of December, and DGFT notification imposing non-tariff barriers on import of hot rolled coils withdrawn, domestic prices remained high. The rise in prices has been attributed to a rise in the prices of raw materials like coke, iron ore, scrap iron, sponge iron and nickel. Iron

and steel have a weight of 3.63 per cent in the WPI, and the steep rise in steel prices had a significant bearing on the overall inflation rate.

5.11 Like steel, sugar too has a large weight of 3.62 per cent in the WPI. Sugar prices rose because of the decline in production during the sugar season in 2003-04 (October-September). The rise in prices during January-February 2004 were reported to be on account of an artificial shortage created by mills not releasing any sugar during the first half of February 2004. Prices of sugar stabilised during March 2004.

5.12 The price rise in the manufactured products group has helped arrest the erosion in the domestic terms of trade of manufactured vis-à-vis agricultural products. Thus, the terms of trade for the manufacturing sector after deteriorating since 2000-01, staged a mild recovery in 2003-04 (Table 5.5).

Table 5.5 : Movement of manufactured prices vis-à-vis agricultural prices	
	Domestic terms of trade manufactured vis-à-vis agricultural price indices
1993-94	100.0
1994-95	96.7
1995-96	96.7
1996-97	91.2
1997-98	91.2
1998-99	85.0
1999-00	86.2
2000-01	86.6
2001-02	85.1
2002-03	84.5
2003-04	85.6

Note: Agricultural Prices Index is computed using the composite index of the sub-groups— Food Articles and Non-food Articles in the Primary Products group of the WPI.

ii. Primary products

5.13 The seasonality in primary product prices - an uptrend during summer months followed by a downtrend during winter months - was observed in 2003-04 as well, with price rise of primary products (on a point-to-point basis) in the range of 5-7 per cent till July 2003.

Thereafter, prices softened and the inflation rate in this group hovered close to 4 per cent till end January 2004. The inflation rate for this group declined further to below 2 per cent by end March 2004 (Table 5.6).

Table 5.6 : Price increase in some major primary products		
Some major groups	Rate of inflation (per cent)	
	52 weeks average 2003-04	End March 2003-04
Primary articles	4.3	1.6
Food articles	1.2	0.2
Rice	1.7	-2.0
Wheat	3.2	6.1
Fruits & vegetables	2.8	-4.9
Pulses	-2.2	-2.6
Non food articles (oilseeds, cotton, jute, sugarcane etc.)	12.6	4.1

5.14 The supply shortfalls for oilseeds, raw cotton and sugarcane, because of the 2002 drought, resulted in large increases in the prices of these commodities during 2003-04. However, despite the drought, prices of major staples - rice and wheat - remained quite stable with output shortfalls made up by releases from the buffer stocks of foodgrains with the Food Corporation of India (FCI). Onion prices firmed up during September-October, 2003 and then again during December, 2003-January, 04.

5.15 The September rains in onion producing areas had delayed both the harvesting of kharif onions as well as the sowing of the late kharif crop. As a result, the late kharif onion crop from Maharashtra, which was scheduled to arrive in the first week of January arrived late and led to a rise in onion prices, feeding into overall inflation.

iii. Fuel group

5.16 The Indian economy's dependence on crude oil imports from West Asia has made it vulnerable to changes in the international price of crude oil. The environment of uncertainty

created by the likelihood of war in the Gulf region had led to a hardening of crude oil prices towards the end of 2002-03. Consequently, the year 2003-04 started with a double-digit inflation of 11.2 per cent for the fuel group. The end of Iraq war and the subsequent softening of crude oil prices led to a moderation of domestic fuel inflation, which dipped to below 5 per cent by June 2003. Inflation started to pick up again after August 2003 to cross 8 per cent in December 2003, but moderated after February 2004 to reach 2.5 per cent in end March, 2004.

Table 5.7 : Price increase in energy products		
Some major groups	Rate of inflation (per cent)	
	52 weeks average 2003-04	End March 2003-04
Fuel group	6.4	2.5
Coal mining	6.9	9.2
Mineral oils	7.7	0.0
Electricity	4.5	4.9

5.17 Organisation of Petroleum Exporting Countries' (OPEC) decision to cut crude oil production quota from November 1, 2003 gave a clear direction that crude oil prices would maintain a bullish trend during the winter months. Persistent terrorist activities in the region, non-resumption of normal supplies from Iraq, low commercial inventories of petroleum and increased energy demand in the US and Europe due to the severe winter created an environment of supply uncertainty, and put upward pressure on crude prices after November 2003. In response, domestic energy prices rose twice during December 2003. In spite of hardening of international petroleum prices, public sector oil marketing companies did not raise domestic energy prices after the hike announced on December 31, 2003. The OPEC announced a further cut in the production quota from April 1, 2004. Even though demand in the April-June quarter is expected to decline, the announcement did result in an immediate firming of prices.

5.18 The inflation rate pertaining to coal and electricity also remained at a fairly high level contributing to the above six per cent average inflation rate for the fuel group in 2003-04 (Table 5.7 and Figure 5.1).