

# **CPI heating up, IIP cools down**

CRISIL First Cut | December 2017

## **CPI nears 5% mark as food inflation surges; core inflation also rises**

Consumer price index (CPI)-based inflation surged to a fifteen-month high of 4.9% in November from 3.6% in October. CPI inflation is now nearly 340 basis points (bps) higher than the lowest point of 1.5% in June - reason why the Reserve Bank of India remains cautious.

Inflationary pressures are again in the spotlight with the crude oil price seeing a sustained rise, impact of payment of higher house rent allowances to government employees, rising rural wages, some indication of return of pent up demand in the economy and a weak base.

In November, the pick-up in inflation was broad-based, driven mainly by a 250 bps on-month rise in food inflation, a 110 bps rise in fuel inflation on the back of higher global oil prices, and a 40 bps pick-up in core inflation reflecting the impact of payment of higher house rent allowances.

Food inflation continued to creep higher to 4.4% from 1.9% led by vegetable prices, mainly onion and tomato. Retail prices of onion and tomatoes – which have large weights in the food index – nearly doubled since September with consumers paying nearly Rs 40 per kg for each in November as per the data released by Department of Consumer Affairs. Inflation in cereals and pulses continued to ease backed by near-normal southwest monsoon and bumper crop from last year.

Meanwhile, core inflation jumped 40 bps up on-month to 4.9% November, led mainly by higher housing inflation, but also a pick-up in other core inflation items indicating an impact of both – the return of some pent up demand and higher tax rates on services under the goods and services tax (GST).

Overall fuel inflation (*fuel and light and petrol and diesel*) rose to 7.2% from 6.1% in October, mainly due to higher inflation in liquefied petroleum gas (LPG), kerosene and other imported fuels.

For the fiscal, while overall food inflation is expected to stay benign, mild pressures could arise due to some shortfall in rabi sowing so far (especially oilseeds and wheat) and the mild recent upturn in global food prices. Of bigger concern is the firming up of housing inflation (due to award of higher house rent allowances), the sharp and sustained rise in global oil prices and impact of fiscal spending (especially farm loan waivers) on inflation. On the downside, items of mass consumption could see softer prices if the recent downward revision in GST rates on some items is passed on to consumers. The interplay among factors will therefore determine the pressures on inflation.

**CRISIL maintains its average inflation forecast for fiscal 2018 at 4%. Accordingly, we also expect the Monetary Policy Committee (MPC) to keep policy rates on hold for the remainder of this fiscal. That said, there could be room for a rate cut only if the downside risks to growth materialise, and inflation undershoots the MPC's estimates.**

### **Data snapshot**

- Food inflation jumped to 4.4% in November from 1.9% in October. There was a steep pick-up in inflation in eggs (to 8% from 0.8%), vegetables (22.5% from 7.5%) and fruits (6.2% from 5%). Vegetables' inflation stood at a 16-month high driven by continued rise in the prices of onion and tomatoes. Meanwhile, inflation in cereals and pulses continued to climb down (to 3.3% for each from 3.7% and 3.1%, respectively), which capped the upside to the food index.
- Fuel inflation, calculated by adding petrol, diesel, fuel and light components, rose to 7.2% from 6.1% in October. Within this category, while inflation in petrol and diesel eased to 4.5% from 5.1%, that in fuel and light jumped to 7.9% from 6.4% driven by higher inflation in LPG and kerosene. During November, prices for the Indian crude oil basket surged 9.4% on month and 37.9% on-year, pushing up the import bill and offsetting the marginal gains to rupee during the month.
- Core inflation (CPI excluding food, fuel and light, petrol and diesel) saw steep climb – to 4.9% in November, from 4.5% in October. This was primarily led by a sharp jump in housing inflation (up to 7.4% from 6.7%) reflecting the impact of revision of house rent allowance of government employees. But other than housing, other items also saw inflation rise. These included household goods and services (up to 4.5% from 4%), clothing and footwear (5% from 4.7%), health (4.6% from 4.1%) and education (4.4% from 4.2%).

## Weakness re-surfaces in IIP

After putting in two consistent months of healthy growth – 4.5% on-year in August and 4.1% (revised upward from 3.8% earlier) in September – the Index of Industrial Production (IIP) growth almost halved to 2.2% in October. The moderation is not a good sign as it may suggest that the healthier growth of the previous two months may largely be on account of restocking activity. The subdued industrial performance in October is also attributable to poor performance in exports, which slumped by 1.1% after rising by an average 13.2% in the previous three months.

- Industrial activity moderated in October despite it being a festive month when demand is expected to be robust. IIP growth almost halved to 2.2% in October from 4.1% (revised upward from 3.8% earlier) in September. While the electricity sector (having 7.9% weight in IIP) at 3.2% continued its slow pace of growth from the past, it was the mining sector that led the slowdown in IIP. The mining sector (14.4% weight in IIP) almost stagnated, registering 0.2% growth over a very low base of last year. The manufacturing sector (the largest contributor to IIP, having 77.6% weight) too saw its growth moderating to 2.5% in October from 3.8% in September.
- Within manufacturing, 10 out of 23 industry groups showed positive growth on an annual basis, while 13 posted a decline in growth. Sectors which displayed high positive growth were, 'pharmaceuticals, medicinal chemical and botanical products', growing by 23%, followed by 'motor vehicles, trailers and semi-trailers', which was up 12.8%, and 'computer, electronic and optical products, which clocked a growth rate of 9.7%. Sectors that displayed high negative growth were, 'Other manufacturing' (-36.4%), followed by tobacco products (-20.9%) and 'rubber and plastic products' (-16.1%). Another important thing is that October was the second consecutive month that saw the industrial & investment-oriented manufacturing sectors growing at a faster pace (1.03%) than the consumer-oriented sectors (accounting for 37% of the manufacturing sector IIP) that grew by 0.62%.
- According to use-based classification, while all other segments saw their growth moderating, the infrastructure and construction goods sectors saw growth jumping to 5.2% in October from 0.4% in November. Capital goods displayed a positive growth (6.8%), but coming on a negative base may not really indicate a pick-up. Growth in consumer durables declined for the second consecutive month (-6.9% in Oct and -3.4% in Sep) indicating fragility in urban demand. Growth in non-durables, though healthy at 7.7%, was lower than 10.3% in September.

## Analytical Contacts

### Dharmakirti Joshi

Chief Economist, CRISIL Ltd.  
 dharmakirti.joshi@crisil.com

### Dipti Deshpande

Senior Economist, CRISIL Ltd.  
 dipti.deshpande@crisil.com

### Adhish Verma

Economist, CRISIL Ltd.  
 adhish.verma@crisil.com

## Media Contacts

### Saman Khan

Media Relations  
**CRISIL Limited**  
 D: +91 22 3342 3895  
 M: +91 95940 60612  
 B: +91 22 3342 3000  
 saman.khan@crisil.com

### Shruti Muddup

Media Relations  
**CRISIL Limited**  
 D: +91 22 3342 5916  
 M: +91 98206 51056  
 B: +91 22 3342 3000  
 shruti.muddup@crisil.com

### Khushboo Bhadani

Media Relations  
**CRISIL Limited**  
 D: +91 22 3342 1812  
 M: +91 72081 85374  
 B: +91 22 3342 3000  
 khushboo.bhadani@crisil.com

## About CRISIL Limited

CRISIL is an agile and innovative, global analytics company driven by its mission of making markets function better. We are India's foremost provider of ratings, data, research, analytics and solutions. A strong track record of growth, culture of innovation and global footprint sets us apart. We have delivered independent opinions, actionable insights, and efficient solutions to over 100,000 customers.

We are majority owned by S&P Global Inc., a leading provider of transparent and independent ratings, benchmarks, analytics and data to the capital and commodity markets worldwide.

## About CRISIL Research

CRISIL Research is India's largest independent integrated research house. We provide insights, opinion and analysis on the Indian economy, industry, capital markets and companies. We also conduct training programs to financial sector professionals on a wide array of technical issues. We are India's most credible provider of economy and industry research. Our industry research covers 86 sectors and is known for its rich insights and perspectives. Our analysis is supported by inputs from our large network sources, including industry experts, industry associations and trade channels. We play a key role in India's fixed income markets. We are the largest provider of valuation of fixed income securities to the mutual fund, insurance and banking industries in the country. We are also the sole provider of debt and hybrid indices to India's mutual fund and life insurance industries. We pioneered independent equity research in India, and are today the country's largest independent equity research house. Our defining trait is the ability to convert information and data into expert judgments and forecasts with complete objectivity. We leverage our deep understanding of the macro-economy and our extensive sector coverage to provide unique insights on micro-macro and cross-sectoral linkages. Our talent pool comprises economists, sector experts, company analysts and information management specialists.

## CRISIL Privacy Notice

CRISIL respects your privacy. We use your contact information, such as your name, address, and email id, to fulfil your request and service your account and to provide you with additional information from CRISIL and other parts of S&P Global Inc. and its subsidiaries (collectively, the "Company") you may find of interest.

For further information, or to let us know your preferences with respect to receiving marketing materials, please visit <http://www.crisil.com/privacy>. You can view the Company's Customer Privacy at <https://www.spglobal.com/privacy>.

**Last updated: April 2016**

## Disclaimer

CRISIL Research, a division of CRISIL Limited (CRISIL) has taken due care and caution in preparing this Report based on the information obtained by CRISIL from sources which it considers reliable (Data). However, CRISIL does not guarantee the accuracy, adequacy or completeness of the Data / Report and is not responsible for any errors or omissions or for the results obtained from the use of Data / Report. This Report is not a recommendation to invest / disinvest in any company covered in the Report. CRISIL especially states that it has no financial liability whatsoever to the subscribers/ users/ transmitters/ distributors of this Report. CRISIL Research operates independently of, and does not have access to information obtained by CRISIL's Ratings Division / CRISIL Risk and Infrastructure Solutions Limited (CRIS), which may, in their regular operations, obtain information of a confidential nature. The views expressed in this Report are that of CRISIL Research and not of CRISIL's Ratings Division / CRIS. No part of this Report may be published / reproduced in any form without CRISIL's prior written approval.