Research

# CPI flatlines, IIP rebounds

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## CPI holds on at 3.3%; food dips but fuel and core inflation climb up

Consumer price index (CPI)-based inflation for September was unchanged at 3.3% from August. While food inflation fell 23 basis points (bps) on-month to 1.3%, fuel inflation rose 35 bps to 6.4%, and core inflation was marginally up 10 bps to 4.4%.

Food inflation fell in September, reversing a two-month trend. At 1.3%, it was lower than 1.5% in August, led by continued decline in inflation in cereals and pulses, and a fall in inflation in vegetables.

This year's near-normal monsoon suggests agriculture production growth is likely to follow trend. This, coupled with last year's bumper crop, will keep food inflation in check. Meanwhile, global food inflation is also forecast to stay benign, which will provide a further downside to domestic food inflation.

Meanwhile, core inflation edged up 10 basis points to 4.4%, primarily led by higher inflation in housing, recreation and personal care and effects. The nature of these items – mostly services -- suggests that part of the higher inflation could have been due to the implementation of Goods and Services Tax (GST). GST rates for most services are higher than the erstwhile service tax rate and is likely to have pushed up prices.

Fuel inflation jumped to 6.4% from 6.1% in August, led by higher inflation in the fuel and light category, mainly liquefied petroleum gas and kerosene.

In the months ahead, inflation could see an upside from some bump up in oil prices, and higher household spending led by (i) implementation of farm loan waiver and (ii) an expected upward revision in salary and allowances of state government employees. Yet, domestic food inflation is expected to stay low aided by a good monsoon, and this will play a key role in keeping overall inflation in fiscal 2018 low.

***CRISIL expects CPI to average 4% in fiscal 2018 (down from 4.5% in fiscal 2017). Going ahead, if the risks to growth rise, and inflation undershoots the Monetary Policy Committee's forecast, then there is a possibility of a rate cut. Second-quarter GDP data will be a key deciding factor here. If growth declines further, it can potentially bring down core inflation, too. A dip in core can provide a faster downside to overall inflation.***

- Food inflation fell in September, reversing its climb over the preceding two months. At 1.3%, food inflation was lower than 1.5% in August. The decline was primarily led by pulses (inflation fell -22.5% in September from -24.4% in August), cereals (3.7% from 3.9%) and vegetables (3.9% from 6%). Inflation also softened in fruits, sugar and spices, while there was a modest rise in eggs, meat and fish, and milk.
- Fuel inflation, calculated by adding petrol, diesel, fuel and light components, rose to 6.4% from 6.1% in August. Within this category, inflation in fuel and light rose to 5.6% from 5%, while in petrol and diesel, it dipped to 9.7% from 10.3%.
- Core inflation (CPI excluding food, fuel and light, petrol and diesel) rose slightly to 4.4% in September, from 4.3% in August. This was primarily led by higher inflation in housing (up to 6.1% from 5.6%), recreation and amusement (4.5% from 4%) and personal care and effects (2.9% from 2.5%). The nature of these items – mostly services -- suggest that part of the higher inflation could have been due to the implementation of the Goods and Services Tax (GST). GST rates for most services are higher than the erstwhile service tax rate and is likely to have pushed up prices.

## IIP shows a sharp, broad-based upturn in August

Industrial activity shrugged off the weakness of past few months and put up a strong performance in August, suggesting that GST-related disruptions could have somewhat settled. The Index of Industrial Production (IIP) grew 4.3% on-year in August, after a meagre 0.94% in July and a negative growth in June. Not only this, the improvement in IIP was broad-based, barring mining which got a 'base effect' boost. The sharp upturn in IIP may be indicative of restocking exercise before the commencement of festive season in the economy.

- There is good news as far as industrial activity in the economy is concerned. After poor performance in previous two months – as the GST was rolled out – IIP rebounded sharply in August registering an annual growth of 4.3%. The uptick in growth was supported by a healthy 3.09% growth in the manufacturing sector (the largest contributor to IIP, having 77.6% weight and which had grown negatively in each of the two previous months) and a strong 8.3% growth in the electricity sector. The mining sector, at 9.5%, clocked the highest growth among the three but this was largely on account of a low-base effect (mining had grown negatively in the year ago period).
- Within manufacturing, many sectors displayed high positive growth. For instance, 'computer, electronic and optical products' grew by 24.9%, followed by 'pharmaceuticals, medicinal chemical and botanical products', which was up 16.5%, and 'other transport equipment', which clocked a growth rate of 11.1%. Overall, 10 out of 23 industry groups in the manufacturing sector showed positive growth on an annual basis. Some sectors that displayed high negative growth were, 'furniture' (-16.0%), followed by tobacco products (-15.1%) and 'printing and reproduction of recorded media' (-11.4%). But broadly, in August both the industrial & investment-oriented manufacturing sectors and consumer-oriented sectors (accounting for 37% of the manufacturing sector IIP) managed to display positive growth at 0.99% and 1.24%, respectively.
- According to the use-based classification, capital goods displayed a positive growth (5.4%) - after four consecutive monthly declines – albeit on the back of a low base. Infrastructure and construction goods grew by a healthy 2.5%, suggesting some revival in the construction space. Consumer goods, too, displayed healthy growth with both the durables and non-durables growing positively - by 1.6% and 6.9%, respectively.


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