



Inflation Watch: Apr-2024: Early signs of core inflation bottoming out

15 May, 2024





Key takeaways

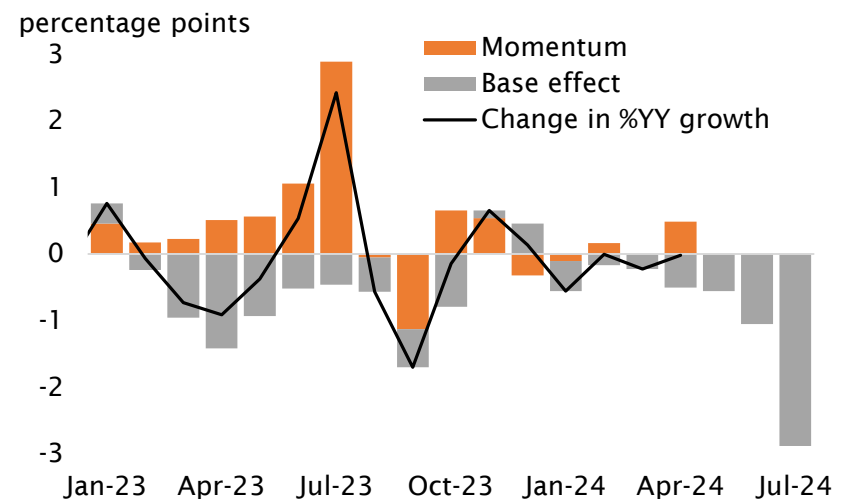
- Headline CPI inflation was steady in April at 4.83%YY vs 4.85% in March, and in line with market expectations (Bloomberg estimate: 4.8%). The stability was driven by base effects, even as prices rose month-on-month across major categories. In terms of year-on-year change, inflation increased in food and miscellaneous categories. The deflation in fuel category steepened further following price cuts in petrol, diesel and LPG. Core inflation was stable at 3.2%. However, amid variants of core inflation and filters used for seasonal adjustment, there is evidence of stability, easing and even an uptick in core inflation in April; albeit all in fractional terms. This suggests that core inflation could be bottoming out at current rates.
- The forecast of above normal southwest monsoon bodes well for agriculture and food prices outlook. The impact of heat wave days is likely to be muted, as Rabi harvesting is slated to have been completed before their onset. But food inflation needs monitoring amid pockets of stickiness and supply intervention will remain key to address near-term shocks. Global commodity prices is another wildcard, with possible first and second-round effects on inflation. Improved consumer confidence and recovering rural consumption pose upside risks to inflation, though lagged impact of policy tightening could limit demand pressures. The stability in the latest inflation print is likely to boost the RBI's confidence that its goal of 4% target inflation is in sight. This could pave the way for a gradual shift in stance by its August meeting, but the MPC might adopt a wait and watch approach before starting with rate cuts to gain clarity on actual monsoon outcome, and beginning of easing cycle by systemic central banks.

Headline inflation remained stable in April due to...

India headline CPI and main sub-indices				
%YY	Weight	Feb-24	Mar-24	Apr-24
Headline CPI	100.0	5.09	4.85	4.83
Food	45.9	7.76	7.74	7.87
Intoxicants, etc.	2.4	3.12	3.11	2.99
Clothing	6.5	3.14	2.97	2.85
Housing	10.1	2.88	2.71	2.68
Fuel and light	6.8	-0.77	-3.35	-4.24
Miscellaneous	28.3	3.63	3.50	3.54

Red indicates higher inflation compared to previous month.
Blue shows the opposite.

... favorable base even as prices rose month-on-month

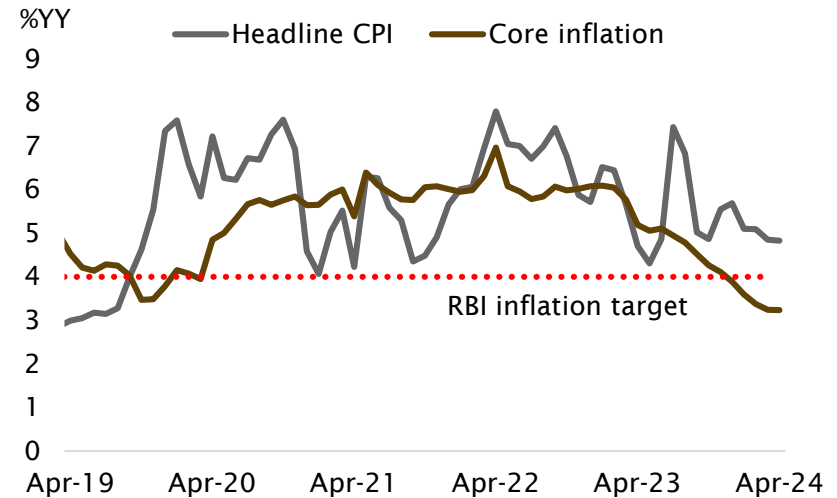




CPI inflation stable due to base effects amid monthly rise in prices

- Headline inflation was steady in April at 4.83%YY compared to 4.85% in March. This stability was due to a favorable base effect, and masks the month-on-month gains across major categories. However, the 0.5%MM increase in headline CPI was lower than the historical (FY12-24) average of 0.8% for the month.
- During the month, there was an increase in inflation in food and miscellaneous items (i.e. personal care and effects), the latter due to higher global prices of gold.
- There was a slight rise in the proportion of items with inflation above the RBI's upper tolerance of 6%, though inflation in more than half of items in the CPI basket was within the target range of 2%-6%.
- Core inflation was stable from previous month at 3.2%. Core services inflation fell below 3%, and core goods inflation eased to levels close to overall core inflation.

Both headline and core inflation stable in April

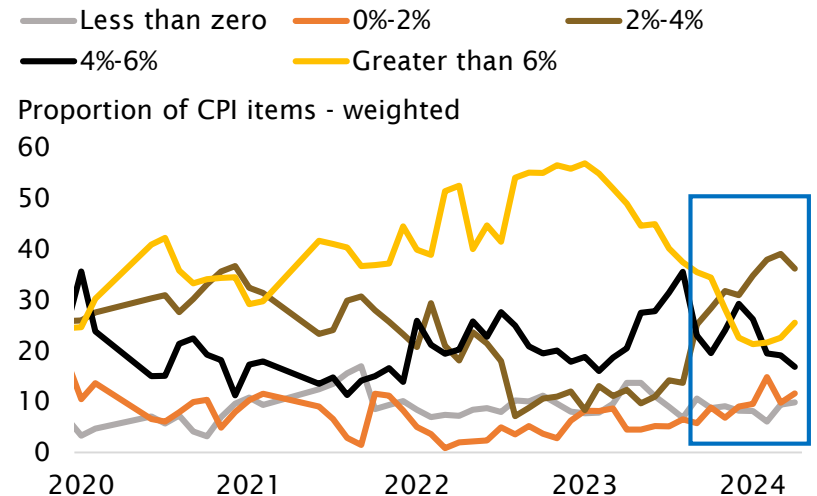


Monthly increase in prices across categories in April

India headline CPI and main sub-indices				
%MM, NSA	Weight	Feb-24	Mar-24	Apr-24
Headline CPI	100.0	0.16	0.00	0.48
Food	45.9	0.11	0.21	0.63
Intoxicants, etc.	2.4	0.24	0.24	0.44
Clothing	6.5	0.16	0.16	0.21
Housing	10.1	0.51	-0.17	0.95
Fuel and light	6.8	-0.11	-2.71	-1.02
Miscellaneous	28.3	0.22	0.22	0.55

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Slight rise in proportion of items with inflation above 6%

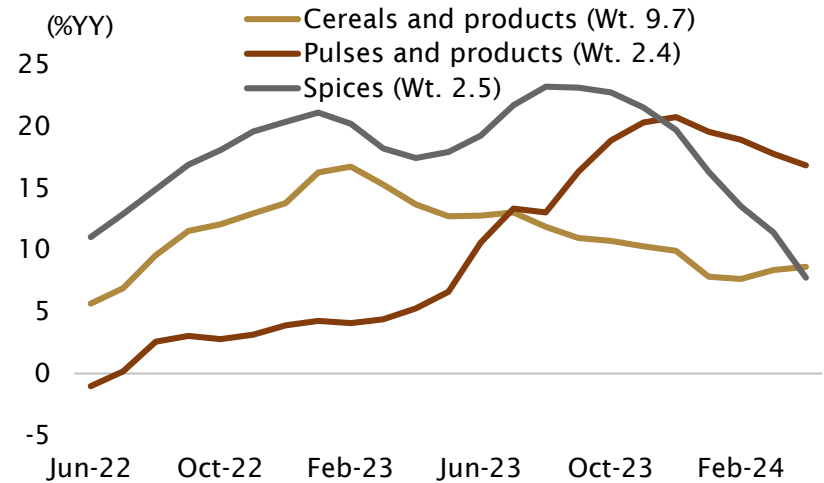




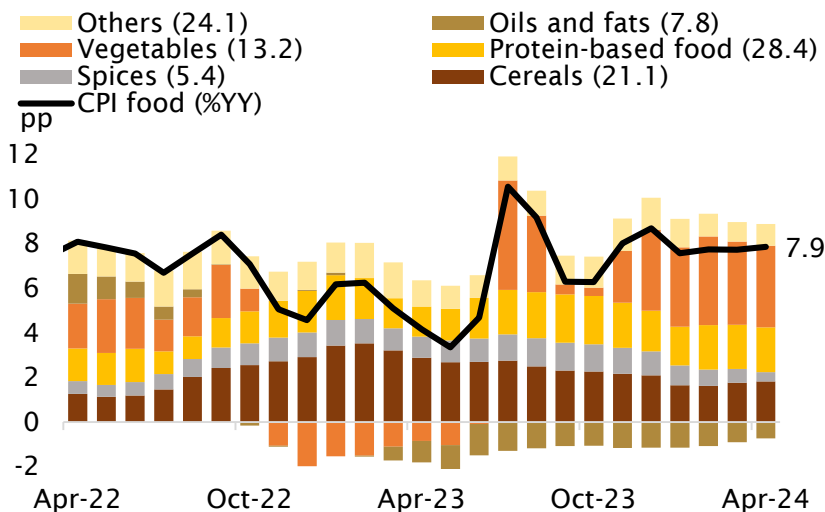
Food inflation remains elevated, though internal data looks favorable

- Inflation in the food and beverages category posted a marginal uptick in April and remained elevated at 7.9% versus 7.7% in March. The latest print marked the tenth straight month of above 6% inflation for the sub-index.
- Vegetables continued to contribute the most to food inflation followed by protein-based food, cereals and spices. The contribution from pulses and spices has been moderating, while inflation in cereals is proving to be stickier. Even as inflation in pulses has been easing, its contribution to inflation in protein-based food remains strong, with eggs, meat and fish also adding to price pressures in recent months. Inflation in fruits also spiked during the month. Sugar prices have been moderating over the past two months after gaining for almost a year.
- During April, there was a spike in the number of food items with lower-than-average monthly price increases.

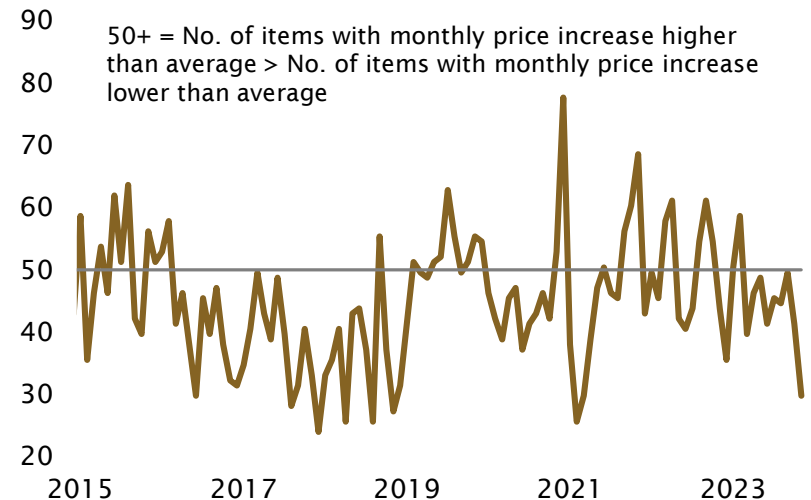
Cereals inflation proving to be stickier than other items



Contribution to food inflation - select items



Food diffusion index turned further favorable in April

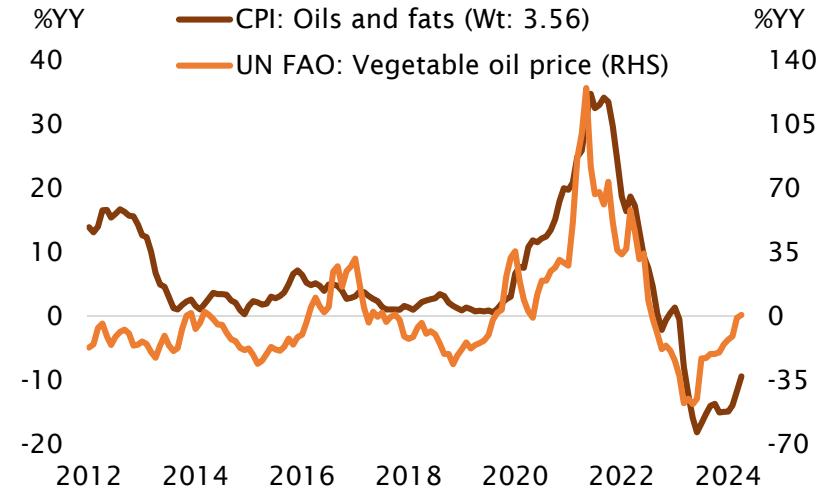




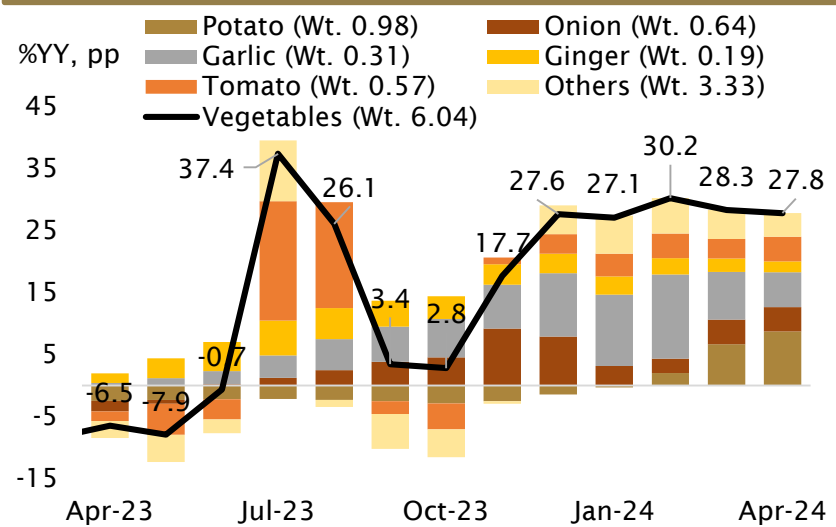
Sticky prices in pockets of food basket; lower deflation in edible oils

- The oils and fats sub-index had been in double-digit deflation for a year, aided by lower global prices and policy measures to ease imports. In April, the deflation in edible oils fell to single-digits amid firming up of global prices.
- Inflation in vegetables was driven higher by tomato prices in July and August, and thereafter by onion in November and December. More recently, potato prices have been on the rise. In addition to these key vegetables, garlic has also been adding to price pressures. High frequency data till May 15 indicates easing of inflation in potato and tomato compared to April, but an increase in case of onion.
- Within cereals, inflation has been sticky in case of rice (non-PDS), hovering between 10%-13% since Oct-2022. There has also been an uptick in wheat (non-PDS) inflation since last month. Daily data till May 15 shows higher inflation for rice compared to April and stability for wheat.

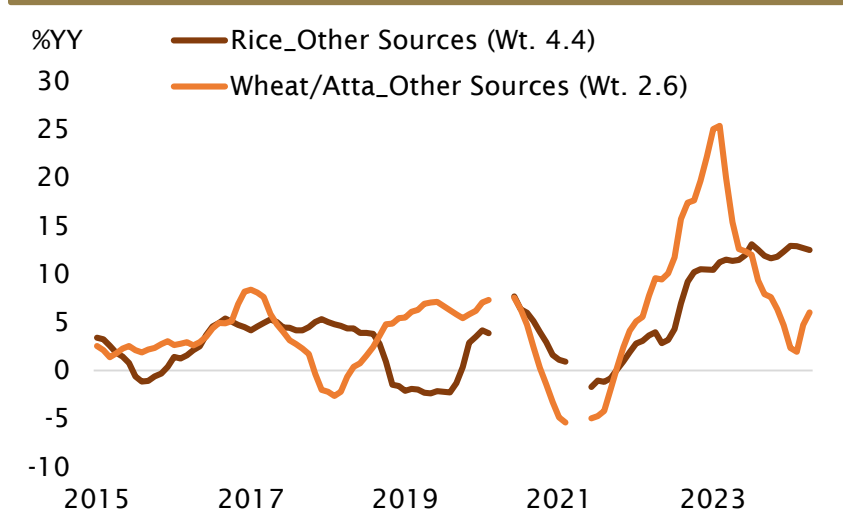
Global edible oil prices are firming up



Contribution to vegetables inflation - select items



Sticky inflation in cereals driven by rice

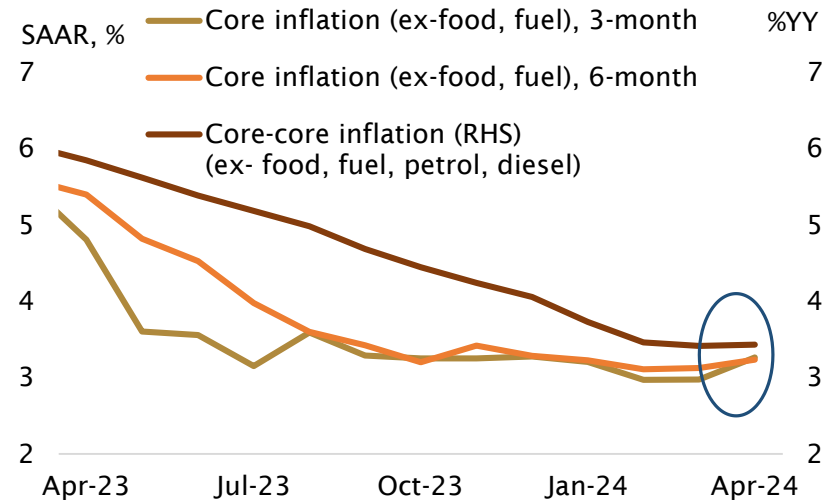




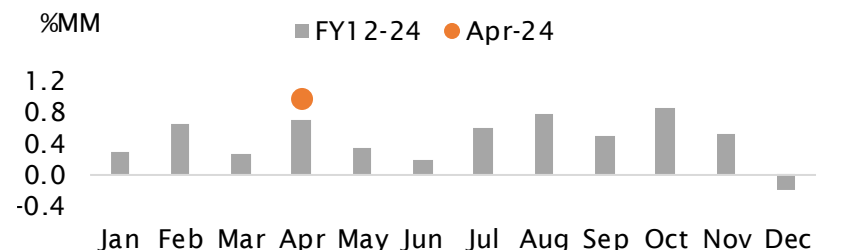
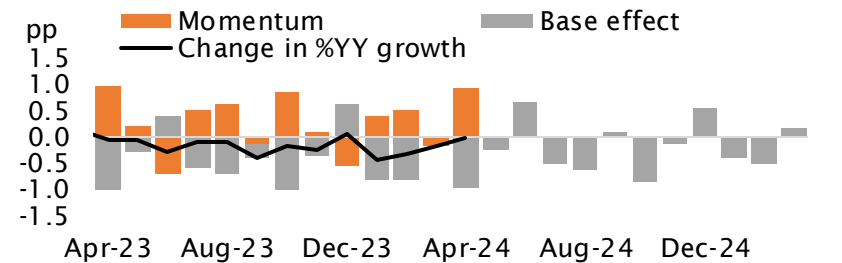
Early signals of core inflation bottoming out

- Core inflation (ex-food, fuel) was stable in April from the previous month at 3.2%. However, amid variants of core inflation and filters used for seasonal adjustment, there is evidence of stability, easing and even an uptick in core inflation in April; albeit all in fractional terms. This indicates that core inflation could be bottoming out at current rates. RBI's latest round of Survey of Professional Forecasters suggests median forecast of core inflation at 3.4% for Q1-FY24, slightly higher than the latest monthly print. However, the upside is expected to be capped by favorable base effects, paving the way for range-bound movements.
- The upside risk to core inflation could manifest from higher imported inflation amid increase in select global commodity prices such as gold and from likely increase in housing inflation that has been printing lower than anecdotal evidence, attributable to issues pertaining to data collection methods used in its compilation.
- Keeping aside the idiosyncrasies associated with the measurement of the housing index, analysis of past data trends shows housing price momentum tends to be weak in the months of May and June, but mostly picks up in FY-Q2, though the upside will likely be limited due to favorable base effect. Also, though the month-on-month increase is likely to be muted in June, unfavorable base effect during the month could lead to some upside pressure to the housing index starting June. The pace of disinflation in housing index in April was the slowest in four months.

Select indicators suggest core inflation bottoming out



CPI housing index

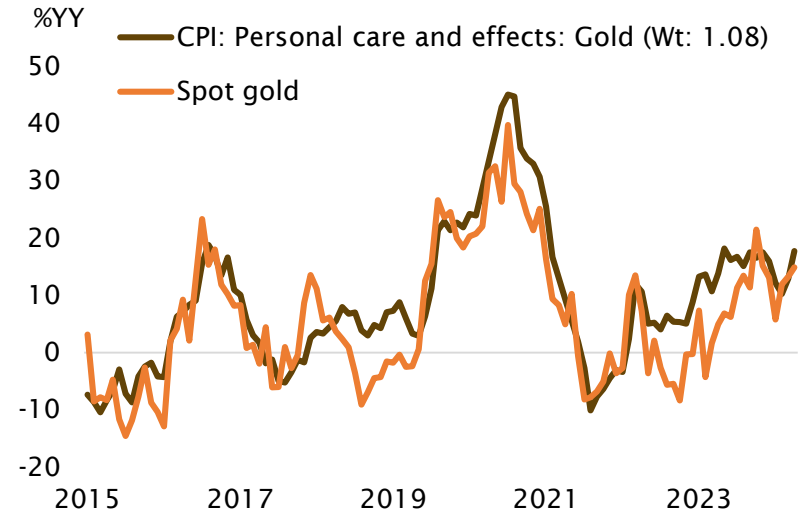




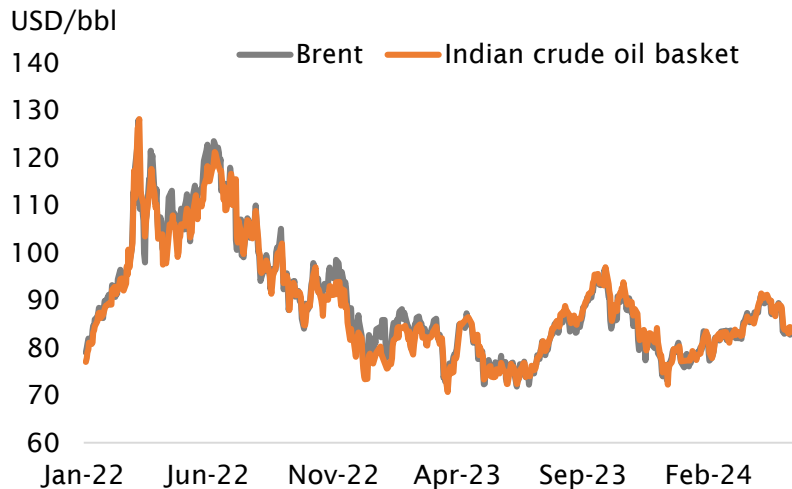
Fuel deflation deepened further; mixed trends in global prices

- In April, the deflation in fuel and light sub-index steepened to -4.2%YY from -3.4% in March, aided by the recent cuts in prices of LPG, petrol and diesel.
- The outlook for global commodity prices remains uncertain amid ongoing geopolitical tensions. Crude oil prices eased in May after posting gains since December, though the domestic consumer has remained largely insulated from these gyrations.
- Global gold prices have gained recently amid safe haven demand, as financial markets remain volatile due to uncertainties around monetary policy easing by systemic central banks. In April, the rise in gold prices led to an uptick in personal care and effects component of CPI.
- There has also been a surge in prices of industrial metals, and a corresponding rise in input costs could trickle down to consumer prices, though with a lag.

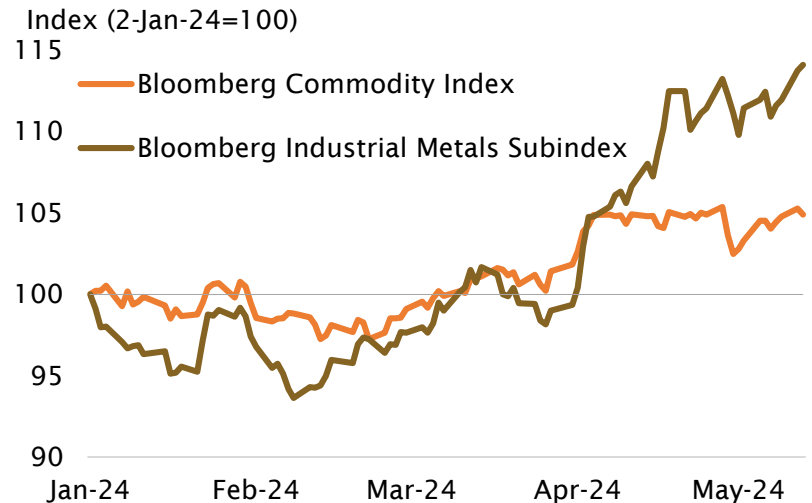
Rise in global gold prices adding to domestic inflation



Crude oil prices - Indian basket and Brent



Recent surge in global prices of industrial metals

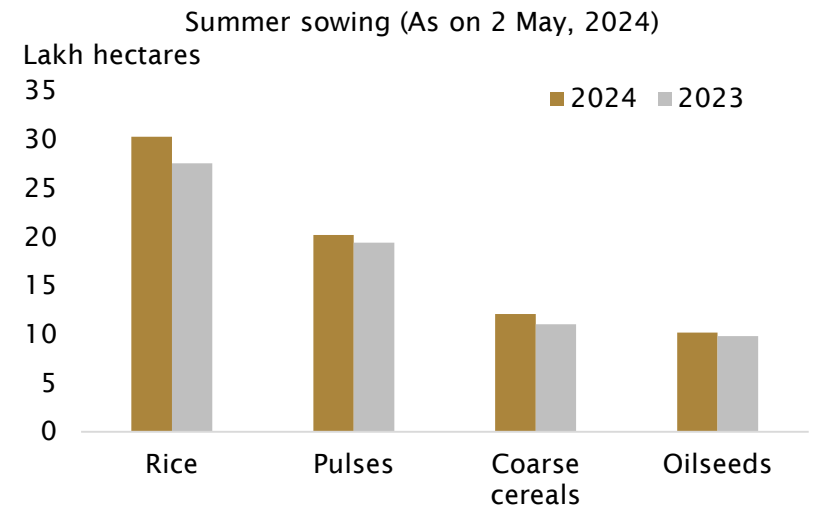




Outlook and policy implication

- Headline inflation is likely to remain stable over the next couple of months amid supportive base effects, though there are risks to watch out for. The early signs of core inflation bottoming out and the fuel index already in deflation indicates that the mantle of keeping consumer inflation in check will likely be passed on to the food basket. Food inflation will remain key to assessing trajectory of the headline print, and outlook has turned positive due to forecast of above normal southwest monsoon for the year. Summer sowing is progressing well though reservoir levels remain below last year's and long-term average levels. The impact of heat wave days on farm output is likely to be muted, as Rabi harvesting is slated to have been completed before their onset. But food inflation needs monitoring amid pockets of stickiness and sudden swings in prices of key vegetables. Supply intervention will remain key to address near-term shocks.
- Global commodity prices is another wildcard, with possible first and second-round effects. While an increase in gold prices tends to reflect directly in CPI inflation, risks prevail from the pass-through of higher input costs from producers, depending on firms' pricing power and demand conditions. Latest PMI data show that in April, manufacturers were able to pass on higher costs to consumers. Improved consumer confidence and signs of recovery in rural consumption also pose upside risks to inflation, though lagged impact of policy tightening could limit the upside to demand pressures.
- The stability in the latest headline inflation print is likely to boost the central bank's confidence that its goal of 4% target inflation is in sight. While this could pave the way for a gradual shift in stance, the MPC might adopt a wait and watch approach before embarking on policy rate cuts to gain clarity on actual monsoon outcome, and beginning of easing cycle by systemic central banks.

Summer sowing above last year's levels for major crops



IMD south-west monsoon forecast for 2024

Category	Rainfall (% of LPA)	Probability (%)
Excess	> 110	30
Above normal	104 - 110	31
Normal	96 - 104	29
Below normal	90 - 96	8
Deficient	< 90	2



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