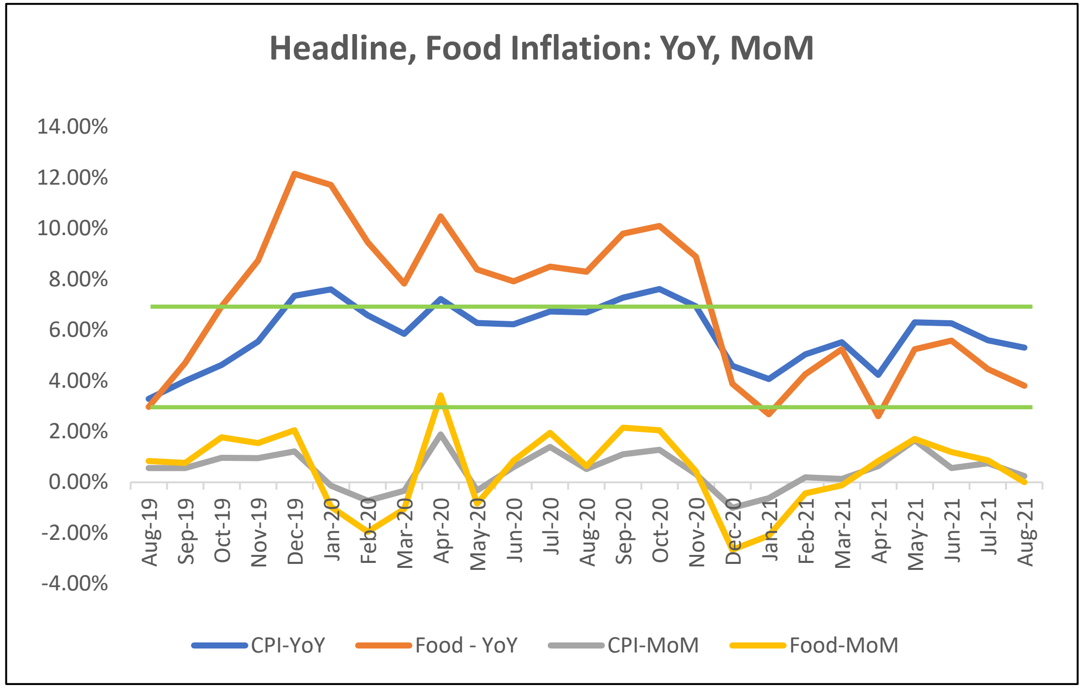
Comments on:
CPI and WPI Data - Aug' 21

Moderation in headline inflation driven by benign food prices



- CPI inflation eased to a 4-month low of 5.30% YoY in Aug-21 from 5.59% in Jul-21, thereby remaining well within RBI's inflation target band for the second consecutive month.
- Sequential momentum in the index has moderately significantly to 0.25 % MoM vis-à-vis 0.74% in the previous month primarily due to moderation in food prices (food and beverages inflation at 3.8%YoY and 0.0%MoM)

Favourable base and lower food inflation to keep CPI inflation under control

- Significant moderation in vegetable inflation along with a contraction in pulses, fruits and animal protein price indices on a sequential basis augur well for food inflation in the near term.

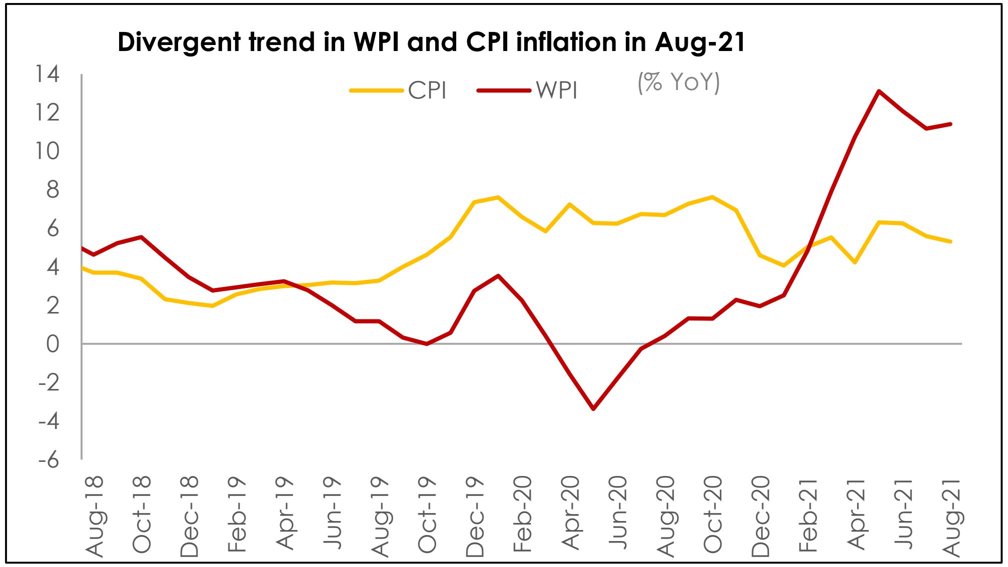
- Recent measures taken by the government to ease supplies through customs duty cuts in the case of pulses and edible oils have played an important role in mitigating food price pressures seen in May-Jun'21.

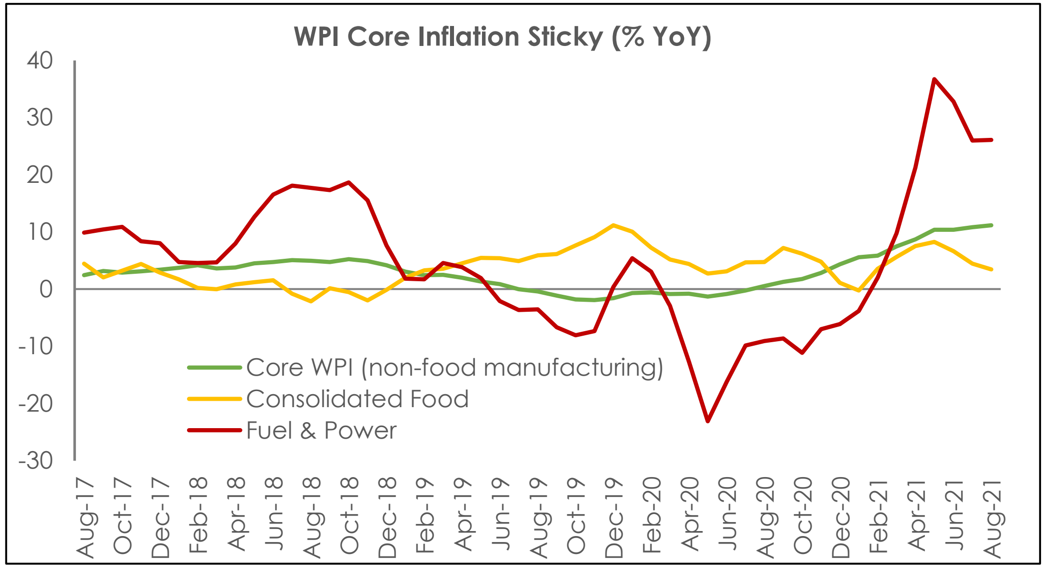
- Core inflation print has provided slight solace, printing at 5.9% YoY and 0.4% MoM in Aug-21 respectively, led by a moderation in personal care segment, in turn influenced by lower gold prices.

- We expect headline inflation to moderate further in the near term on account of a favourable base-effect, easing of supply- side disruptions, plateauing of global commodity prices compared to the Jun-21 peak and prospects of strong kharif output.

- Nevertheless, pass through of higher input price pressures along with improvement in consumer sentiment supported by steady vaccination progress could fan some demand side price pressures thereby keeping core inflation sticky at elevated levels. Taking these factors into consideration, we continue to expect FY22 CPI inflation at 5.5% with risks balanced on either side.

Divergent trend in WPI reflects passthrough of higher commodity prices





- Unlike a moderating trajectory for CPI which is driven primarily by food inflation, the WPI inflation has remained firm in Aug-21 and actually increased to 11.39% vs 11.16% recorded in Jul-21.
- Apart from an unfavourable base, there is a sequential uptick of 1.04%, the highest seen for WPI in the last 4 months. This has been driven by higher fuel inflation including prices of natural gas as well as the continuing pass through of higher commodity prices in manufacturing costs where the sequential print was 0.76%; also, by a substantial price rise in the case of minerals which posted a double-digit expansion after a hiatus of 13-months.
- However, the progress in Kharif sowing along with the recent government measures for pulses and oilseeds led to food inflation declining on a sequential basis, offsetting some of the manufacturing price pressures.

Core inflation trajectory is a monitorable but no short term concerns

- The divergent trend between CPI and WPI inflation indicates that the current inflationary risks are primarily emerging from the impact of commodity prices on manufacturing sector where further pass through is likely as demand continues to improve.

- Although the food category may continue to provide relief in the near term, such transmission of higher production costs may keep core inflation at elevated levels.

- Nevertheless, we expect MPC to derive significant comfort from the moderating CPI inflation print and reinforce its accommodative stance in the ensuing Oct meeting. However, the monetary landscape may change by end of Q3FY22 if there are strong signs of a demand pickup going forward.

- We expect an increase in reverse repo rate by Q4FY22 which will signal a transition from an accommodative to a neutral monetary policy.