Press Release

Moderation in both CPI and WPI print in Oct-22

Not adequate, though for a pause; 30-40 bps rate hike likely by MPC in Dec-22

14-Nov-2022

Elevated CPI inflation of the previous year (Oct-21) has helped to rein in the annualized inflation print for the month of Oct-22 to 6.77% YoY from a five-month high of 7.41% in Sep-22. To recall, sequential momentum in the Oct-21 had surged to 1.41% (the highest for the month of October in nearly six years), led by significant rise in food price pressures particularly for perishables. Going forward, we expect the annualized CPI print to ease further amidst the statistical impact of favorable base coming into play. While the inflation print has eased, the pace of build-up in consumer prices, has been gaining momentum for three consecutive months with the month of Oct-22 recording a further increase of 0.8% MoM from an 0.57% in Sep-22. The sequential rise is primarily due to food & beverages, fuel, and housing inflation.

Sequentially, food and beverages index rose by 0.96% MoM in Oct-22 from an increase of 0.85% in Sep-22 led by an increase in price of vegetables, followed by cereals, meat & fish, and spices. However, some offsetting impact emerged from fruits and edible oils. The retail price of edible oils has been in a contraction mode for five consecutive months amidst a series of pre-emptive measures taken by the government in the form of reduction in its import duties along with sharp decline in global edible oil prices. The UN Food Price registered its seventh consecutive monthly decline on the back of sharp contraction in edible oil prices (-18.8% MoM in Oct-22 vs. -9.5% in Sep-22), of which India is a major importer. The vegetable prices however, continued to remain elevated amidst uneven rains and late withdrawal of monsoon which not only impacted the harvest season but also damaged the harvested stock creating shortages in the retail market. Additionally, lower sowing in case of paddy and pulses in the current kharif season amid irregular monsoon along with the extension of PM Garib Kalyan Yojana (Central Government's free foodgrain scheme) has led the price of cereals to creep up sequentially; annualized cereal inflation stood at 12.08% in Oct-22, a multi-year high. However, the positive impact of government's efforts to tame supply side inflation in the form of export restrictions and imposition of export duty on certain categories of wheat and rice is visible in the sequential price of cereals which has been easing gradually.

Overall, despite the uneven distribution of monsoon, the Kharif season closed with near normal acreage. While we do not rule out a modest shortfall in the crop production and the resultant price pressure especially for cereals (i.e., wheat and rice), the downside in agriculture output is likely to be capped. Looking ahead, we expect the food price pressures to ease amid bountiful reservoir levels which will aid rabi sowing, the higher than previous year's hike in wheat MSP for 2022-23 season, prospects of additional government measures to tame cereal prices, and onset of winter seasonality that would likely keep the price of vegetables in check.

On the other hand, while annualized fuel and light inflation further eased to 9.93% in Oct-22 from 10.39% YoY in Sep-22, sequentially it inched up by +0.56% MoM from an increase of 0.39% in Sep-22. The uptick in sequential momentum was on account of rise in the price of electricity, kerosene, coke, coal, charcoal, and dung cake. While the significant easing in crude oil prices (USD 96 levels currently) amid looming recessionary risk has brought in a major relief to the OMC's profit margins, we don't expect them to pass on the benefits to the retail fuel prices anytime soon given the persistent higher levels of under recoveries.

Core (i.e., CPI ex indices of Food & Beverages, Fuel and Light) inflation momentum rose further by 0.60% MoM in Oct-22 from 0.41% in Sep-22 even as annualized Core CPI eased marginally by 10 bps to 6.23% YoY in Oct-22. While clothing & footwear registered a slight moderation, housing and miscellaneous category recorded an increase in prices. Going forward, we expect the sticky core inflation to persist with a strong pick-up in retail demand, lagged pass-through of elevated input prices to end consumers and impact of GST rate hike on certain household consumption items.

On the other hand, inflation at the wholesale level eased to 8.39% YoY in Oct-22 after trailing in double-digits for nearly eighteen-months in a row supported by favorable base at play and some comfort from core WPI inflation (non-food manufacturing). Sequentially, the momentum ticked-up marginally by +0.3% MoM in Oct-22 after declining for three consecutive months led by sequential increase in consolidated food (comprising of manufactured and primary food prices) and fuel inflation (comprising of crude petroleum and fuel & power).

Food inflation played a spoilsport both at the wholesale and the retail level. On the wholesale price front, consolidated food inflation rose by 1.3% MoM in Oct-22 from -0.5% in Sep-22 with price pressures recorded in perishables especially fruits & vegetables and foodgrains. While consolidated fuel inflation eased on an annualized basis to 26.2% YoY in Oct-22 from 34.2% in Sep-22, on sequential basis, it increased by 1.1% MoM in Oct-22 due to increase in prices of coal while mineral oil prices declined led by ATF, petrol, and kerosene.

WPI core inflation (non-food manufacturing inflation) is estimated to have eased somewhat to nearly a two-year low of 4.0% YoY in Oct-22 from 7.0% in Sep-22, with sequential print increasing significantly by 0.5% MoM from a contraction of 0.23 % in the previous month. With easing of commodity prices, the margin pressure on producers seems to be gradually on the wane. Nevertheless, with further pick-up in demand we expect the accrued pressure from higher input to get further transmitted to retail inflation, albeit at a moderate pace, keeping core CPI inflation sticky at around 6.0% in FY23. The gradual pass-through of higher cost pressure from the wholesale to the retail level has become increasingly evident as the gulf between WPI and CPI core inflation has continued to narrow, indicating the impact of pass-through of higher input prices.

The ongoing disinflation in most international commodity prices is getting captured by WPI inflation. If the current trend persists, then WPI inflation could briefly touch negative territory in Q1 FY24. This makes us hopeful of expecting a decelerating trend in CPI inflation in H2 FY23. The favorable base-factor of the previous year is also expected to play a pivotal role in taming the retail price pressures in H2 FY23. Additionally, easing of supply chain pressures, kharif harvest coming onboard, winter seasonality in perishables kicking-in, and a slower pass-through of commodity price would offer support to the inflation trajectory in the second half of the fiscal. On the other hand, the impact of hike in GST rates on some items of mass consumption along with hike in electricity tariffs by state discoms (which is yet to be fully captured) and significant rupee depreciation in CY2022 could keep the gains capped. Taking these factors into consideration, the risks to our FY23 CPI inflation estimate of 6.7% appear to be somewhat well balanced at the current juncture.

From monetary policy perspective, we expect the central bank to balance the growth-inflation dynamics in a nuanced manner. As such, we expect the RBI to slow down the pace of interest rates hike with a likelihood of 35-40 bps rate hike in the Dec-22 policy review and decide on the next steps depending on the incoming inflation data. The recent declining pressure on the INR will also help MPC to take a less hawkish call on the rates in the upcoming policy review.

Says Suman Chowdhury, Chief Analytical Officer, Acuité Ratings & Research "The issue on the domestic inflation front today is not so much the direction of the trajectory but the pace of the decline. While global commodity prices have continued to moderate due to the global slowdown and that is clearly reflected in the WPI inflation print, we believe that the decline in the headline CPI inflation print will take more time due to the entrenched core inflation which continues to hover well above 6% apart from the supply challenges in some food categories and the impact of the rupee depreciation. The average CPI inflation is likely to drop by a moderate 50-60 bps in Q3FY23 from the 7%+ levels in Q1 and Q2. This implies a strong likelihood of another round of rate hike of the order of 30-40 bps in the next MPC of Dec-22."

Annexure

Chart 1: Base impact leads CPI inflation to ease to 6.77% YoY in Oct-22

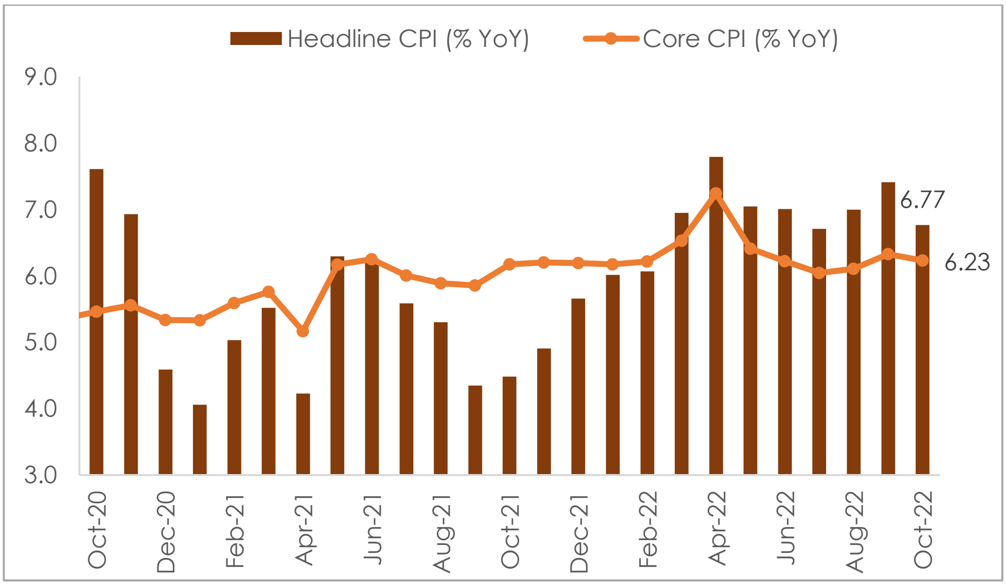


Chart 2: Global food prices ease led by significant correction in edible oil prices

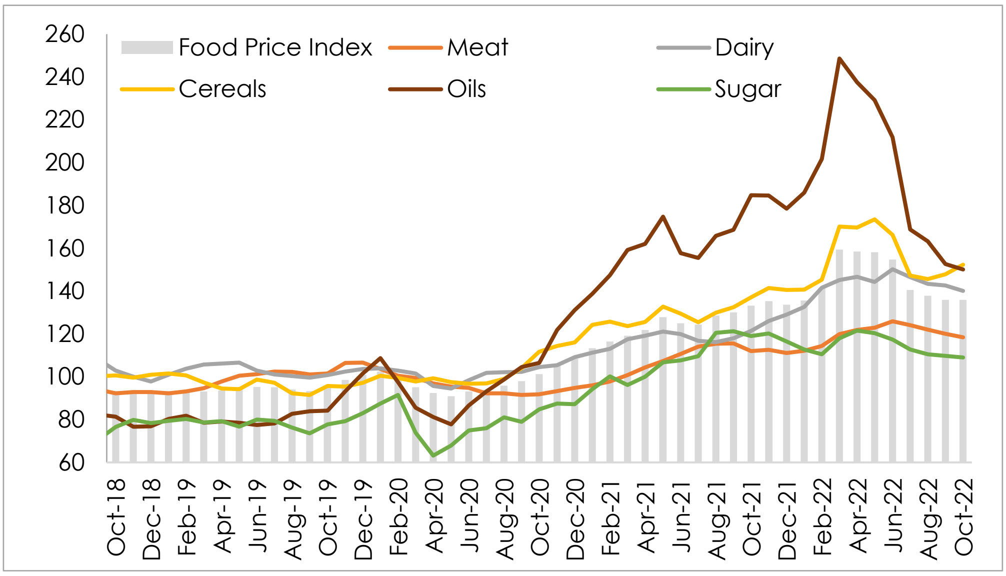
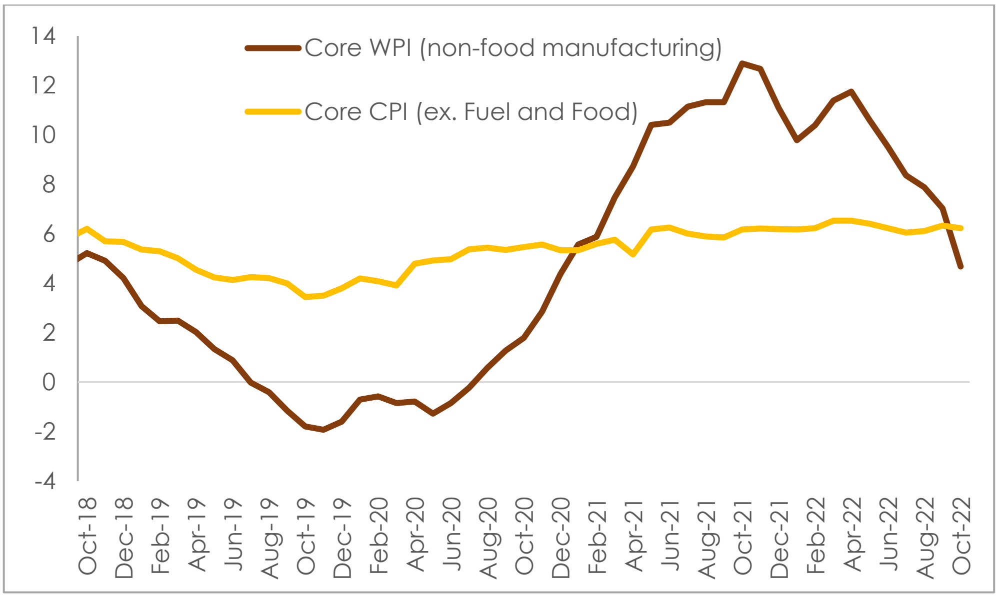


Chart 3: Closing gap b/w core WPI and CPI inflation show pass-through of higher input cost



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