Macroeconomics | First cut

Sticky food, higher IIP

April 2024

Softer core, sharp fall in fuel offset the stubbornness in food inflation

Consumer price index (CPI) inflation eased to a five-month low of 4.9% in March from 5.1% in February. While core inflation declined to a record low of 3.3%, fuel deflated 3.2% on the back of lower domestic fuel prices. The worry, though, remains on persistently high food inflation, at 8.5%. Higher cereals inflation, erratic vegetable inflation and elevated pulses inflation are a cause of concern given the India Meteorological Department's (IMD) prediction of higher-than-normal temperatures between April and June.

Although headline inflation eased to 5.4% on-year in fiscal 2024 from 6.7%, food inflation surged to 7.5% from an already high 6.6% in fiscal 2023. The March 2024 reading of 8.5% food inflation creates some disquiet given the prediction of higher-than-average temperatures over the next few months that can stress vegetable production and some of the rabi crop that is yet to be harvested.

Beyond that, we expect food inflation to ease a tad on the back of the prediction of a favorable monsoon (above-normal rains as per the IMD), some benefit from a high food inflation base and an expected season downturn in pulses inflation.

In our base case, we expect non-food inflation to remain comfortable, supported by softness in consumer demand, a pass-through of the previous year's oil price decline to domestic fuel (petrol and liquefied petroleum gas (LPG)) prices and an expectation of benign crude prices in the base case.

Under these assumptions, we expect CPI inflation to average 4.5% this fiscal. Intensification/persistence of geopolitical concerns and weather shocks, if any, pose an upside risk to this call.

Meanwhile, the government's budget is slimmer, which means the fiscal impulse to growth is also leaner and, therefore, less inflationary. All these create favourable grounds for rate cuts this fiscal lest the notorious food inflation or geopolitical escalations get in the way and delay this decision.

Key data points in March

- CPI inflation eased to a five-month low of 4.9% from 5.1%
- Food inflation moderated marginally from 8.7% but remained high at 8.5%
- Fuel[1] inflation declined to -3.2% from -0.8%
- Core CPI[2] inflation eased to 3.3% from 3.4%

[1] Refers to CPI fuel and light
[2] CPI excluding food and beverages, and fuel and light

Food inflation remains high

- Inflation in vegetables softened ~20 basis points (bps) to 28.3% in March from 30.2% in February. Inflation in key vegetables such as onions (36.9% vs 21.9%) and potatoes (41% vs 12.4%) hardened while inflation in tomatoes eased but remained high (32.5% vs 41.8%). Vegetables inflation excluding tomatoes, onions and potatoes (TOP) moderated to 24.4% from 34%. This was led by cooling inflation in garlic (150.7% vs 263.9%), brinjal (18.9% vs 23.2%) and lady's finger (-7.7% vs -1.4%)
- Foodgrain inflation inched up to 10.2% from 9.8% in February, with cereals inflation rising (8.4% vs 7.7%). Wheat inflation (from non-Public Distribution System (PDS) sources) accelerated to 4.7% from 2% partly due to an adverse base. Rice inflation, on the other hand, inched down (12.7% vs 12.9%). However, easing pulses inflation (17.7% vs 18.9%) capped the rise in foodgrains inflation. Among pulses, inflation eased in arhar (33.5% vs 36.8%) and moong (11.5% vs 12%)
- Inflation in meat and fish accelerated for the second straight month to 6.4% from 5.2% driven by chicken, (8.5% vs 5.6%) and fish and prawn (6.6% vs 6.1%)
- The pace of deflation in edible oils slowed significantly. Prices declined 11.7% on-year compared with 14% in the previous month
- Spices inflation moderated for the seventh straight month to 11.4% from 13.5%
- Inflation in sugar eased for the first time in over a year to 7.3% from 7.5%

Fuel prices fall further

- Fuel prices fell 3.2% on-year in March compared with a 0.8% decline in the previous month, remaining negative for the seventh straight month
- LPG prices fell by a sharper 22.3% on-year compared with a 13.3% decline in February. This was due to the central government cutting prices since March
- Inflation remained unchanged in electricity, at 10.4%, for the third consecutive month
- Inflation picked up in PDS kerosene (-7.4% vs -11.2%) and fire and woodchips (3.2% vs 3%)

Core inflation eases to record low

- Core inflation inched down to a record low of 3.3% from 3.4% the previous month
- Inflation eased in the essential categories of education (4.7% vs 4.8%), health (4.3% vs 4.5%) and housing (2.8% vs 2.9%)
- On the other hand, inflation picked up in personal care and effects (6% vs 5.2%), led by rising gold prices (12.9% vs 10.2%). There was a slight uptick in recreation and amusement inflation (2.8% vs 2.7%).
- Core goods[3] eased to 2% from 2.5%, while services inflation remained unchanged at 3.3%

[3] *Refers to CPI excluding services and food*

Price pain greater in rural India

The effect of inflation varies with income groups since the share of spending on food, fuel and core categories differs across classes. Items such as food and fuel, being essential, occupy a greater share in the consumption basket of lower income classes.

Inflation moved in opposite directions in urban and rural areas in March. While inflation inched up in rural areas to 5.4% from 5.3%, urban inflation eased markedly (4.1% from 4.8%). This can be attributed to rising food inflation in rural areas (8.6% vs 8.3%). Urban food inflation declined compared with the previous month (8.4% vs 9.2%). Higher rural food inflation relative to urban was primarily a result of higher rural inflation in vegetables and cereals. Additionally, fuel inflation was significantly lower in urban areas (-8.2%) compared with rural areas (-0.2%). Since the weight of core items is higher in the urban consumers' basket, soft core inflation benefited urban inflation to a greater extent.

Rural inflation outpaces urban inflation across categories in March

Category	Rural	Urban
Headline	5.4	4.1
Food	8.6	8.4
Fuel	-0.2	-8.2
Core	3.3	3.2

Source: National Statistical Office, CEIC, CRISIL

Accordingly, all income segments in rural areas faced a higher burden than their urban counterparts. The top urban segment faced the lowest burden since core items occupy a 60% share in their consumption basket. Due to high food inflation, the poorest segment, particularly in rural India, faces a higher burden.

CPI inflation across income classes (% on-year)

Income segment	March		February	
	Rural	Urban	Rural	Urban
Top 20%	5.2	4.1	5.1	4.7
Middle 60%	5.5	4.4	5.4	5.3
Bottom 20%	5.6	4.5	5.5	5.5

Note: Using data from the National Sample Survey Organisation (NSSO), CRISIL has mapped the expenditure baskets of three broad income groups – bottom 20%, middle 60% and upper 20% of the population – with March inflation trends. The table above presents the average inflation faced by each income class.

Source: NSSO, National Statistical Office, CEIC, CRISIL

IIP rises on the back of broad-based growth

The Index of Industrial Production (IIP) increased to 5.7% on-year in February from 4.1% in January, boosted by healthy performance in both consumption and industrial sectors. Meanwhile, January's reading was revised up from the previous estimate of 3.8%. IIP growth picked up in all three subsectors of manufacturing, mining and electricity.

IIP data till February indicates slower growth in the fourth quarter so far – averaging 4.9% in January-February compared with 6.2% previous quarter. Yet, the year is likely to close with healthy industrial performance, as indicated by PMI manufacturing rising to a 16-year high of 59.1 in March. A revival in government capex and exports has driven the recent rise in IIP.

However, the fiscal support to growth is expected to wane in fiscal 2025 as government targets reducing fiscal deficit to 5.1% of GDP from 5.8% of GDP previous fiscal. A pickup in private capex is critical to sustain the investment momentum.

Exports continue to face risks from heightened geopolitical tensions in the Middle-East. Uneven growth in India's major trading partners could restrict India's export recovery. S&P Global expects the United States to grow 2.5% in 2024 calendar year, but weaker growth in Eurozone at 0.7%. Unfavourable crude prices – currently hovering around $90 per barrel – could also drag domestic industrial activity.

Rural demand – which was a key drag for consumption last fiscal – could revive in current fiscal. The IMD's forecast of above monsoon this year bodes well for agriculture incomes and demand. However, the lagged impact of RBI's rate hikes and regulatory tightening of credit could have a moderating impact, especially for urban consumption.

We expect these factors to contribute to a moderation in GDP growth to 6.8% in current 2025 from an estimated 7.6%[4] past year.

Data highlights

- IIP growth increased to 5.7% on-year in February from 4.1% the previous month. The index grew 1.2% on-month after seasonal adjustments
- Growth in all three IIP subsectors picked up, led by mining (8.0% on-year in February versus 5.9% in the previous month), electricity(7.5% vs 5.6%) and manufacturing (5.0% vs 3.6%)
- Manufacturing growth was driven by consumer durables (12.3% vs 11.9%), intermediate goods (9.5% vs 5.3%), infrastructure and construction goods (8.5% vs 5.5%) and primary goods (5.9% vs 2.9%). On the other hand, the contraction in consumer non-durables output was more pronounced (-3.8% vs -0.2%), while growth in capital goods slowed (1.2% vs 3.4%)

[4] *NSO's second advance estimate*

Manufacturing picks up

- The increase in manufacturing IIP (5.0% on-year in February vs 3,6% the previous month) was led by increasing output growth in electrical equipment (10.0% vs 3.1%), basic metals (8.8% vs 7.3%), coke and refined petroleum products (4.9% vs -2.2%) as well as textiles (3.7% vs 3.1%)
- The performance of export-oriented sectors was mostly positive, with improving output growth for basic metals, coke and refined petroleum products as well as chemicals; output declined for pharmaceutical products. This reflected the sharp increase in merchandise export growth to 11.9% on-year in February, from 3.1% in the previous month

Consumer durables perform better than non-durables

- There was an uptick in the output growth of consumer durables (12.3% in February versus 11.9% in the previous month), led by better performance by furniture (22.7% vs 15.1%), computer and electronic products (1.9% vs -7.4%) and textiles (3.7% vs 3.1%). Despite declining relative to the previous month, automobile output growth remained healthy in double digits (11.6% vs 19.0%)
- Durables recorded a better performance than non-durables, whose output contracted further in February (-3.8% vs -0.2%).

Industrial goods record better performance overall

- Output growth picked up in infrastructure and construction goods (8.5% vs 5.5%) on the back of higher government capex growth in February
- Electricity IIP growth picked up to 7.5% in February from 5.6% in January

Analytical contacts

Dharmakirti Joshi
Chief Economist, CRISIL Limited
dharmakirti.joshi@crisil.com

Dipti Deshpande
Principal Economist
dipti.deshpande@crisil.com

Pankhuri Tandon
Senior Economist
pankhuri.tandon@crisil.com

Sharvari Rajadhyaksha
Economic Analyst
sharvari.rajadhyaksha@crisil.com

Bhavi Shah
Economic Analyst
bhavi.shah@crisil.com

Media contacts

Aveek Datta
Media Relations
CRISIL Limited
M: +91 99204 93912
aveek.datta@crisil.com

Roma Gurnani
Media Relations
CRISIL Limited
M: +91 70662 92142
roma.gurnani@ext-crisil.com

Prakruti Jani
Media Relations
CRISIL Limited
M: + 91 98678 68976
PRAKRUTI.JANI@crisil.com