Macroeconomics | First cut

Striking decline in food inflation, IIP slackens

August 2024

High-base effect saves the blushes

Consumer inflation eased dramatically to 3.5% on-year in July — dipping below the Reserve Bank of India's (RBI) medium-term target of 4% for the first time since August 2019 — largely due to statistical high-base effect.

Interestingly, while the high-base effect was supportive for food inflation, it had an adverse bearing on core inflation.

Food inflation plunged to 5.4% from 9.4%, as the high base offset the sequential rise in prices. Vegetables inflation saw the biggest drop to 6.8% from 29.3%.

The big worry now is food prices continue to be elevated with the on-month rise being slightly higher than usual for July.

At the same time, core inflation rose for the first time in over a year to 3.3%.

The good part is monsoon and sowing have been progressing better than last year and the expectation is that the arrival of fresh supplies in the market should curb prices over the next few months. As of August 12, rains were at 6% above their long period average.

Core prices are facing upward pressure from rising geopolitical uncertainties, higher input costs and the dial-up in telecom tariffs. That said, only a mild increase is expected this fiscal.

Overall, though, we expect inflation to ease and average 4.5% this fiscal mostly owing to softer food prices. This should allow the RBI to begin cutting rates earliest by October.

Key data points in July

- CPI inflation slid to 3.5% from 5.1%
- Food inflation eased sharply to 5.4% from 9.4%
- Fuel[1] prices fell 5.5% on-year
- Core CPI[2] inflation rose 20 bps to 3.3%, up for the first time since January 2023

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

Food inflation declines

- Food inflation declined to its lowest level since June 2023, sliding 400 bps to 5.4%
- Lower vegetables inflation was the main driver of the drop in food inflation in July. Vegetables inflation plunged to 6.8% from 29.3%, led by a sharp decline in tomato inflation (-42.9% vs 26.5%). Other vegetables also saw softer inflation, including leafy vegetables, brinjal, garlic, green chillies, etc. That said, rising inflation in potatoes (65.6% vs 57.6%) and onion (60.5% vs 58.4%) – the two items having the highest weight in the vegetables index – limited the decline in vegetables inflation
- Foodgrain inflation eased to 9.5% from 10.2%, driven by both cereals and pulses. Cereals inflation stood at 8.1% against 8.8%, led by lower inflation in non-PDS rice (10.9% vs 12.2%). Pulses inflation moderated to 14.8% from 16.1%
- An adverse base pushed up inflation in meat and fish (6% vs 5.4%) even as prices dropped on-month
- The pace of deflation in edible oil prices slowed for the sixth consecutive month to -1.2% on-year from -2.7%
- Prices of spices fell 1.4% on-year from a 2.1% on-year rise in June. Jeera (-18.5%), dhania (-0.1%) and dry chillies (-6.6%) were the key spices that logged a drop in prices

Negative fuel inflation

- Fuel inflation was negative for the 11th straight month. The on-year fall in prices was sharper in July at 5.5% compared with 3.6% on-year in June. Although global energy prices rose in July, government support kept domestic fuel inflation negative
- Electricity inflation fell sharply to 4.8% from 8.8%, supported by a high base from last year
- Prices of liquified petroleum gas continued to deflate (-24.7%) owing to the subsidy from the government
- Fire and woodchips, too, saw lower inflation at 2.1% against 2.7%

Core inflation picks up

- Core inflation picked up for the first time since January 2023, driven by services inflation (3.4% vs 2.9%)
- A hike in tariffs by major domestic telecom companies drove up services inflation
- Inflation in transport and communication accelerated to 2.5% from 1%
- Inflation in personal care and effects rose for the fifth straight month to 8.4% from 8.2%
- Core goods[3] inflation was down 10 bps to 3.1%

[3] *Refers to CPI excluding services, food and fuel and light*

The poor get reprieve in inflation burden

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

Inflation affected different income groups in urban and rural areas as follows:

- Rural inflation outpaced urban inflation across categories in July – food (4.6% in urban vs 5.9% in rural) and fuel (-9.5% in urban vs -3% in rural) and core (3.2% in urban vs 3.6% in rural)
- The urban poor faced the lowest inflation burden in July, given lower urban inflation and higher weight of food in the consumption basket of the poor
- In rural areas, too, households with income in the bottom 20% saw a lower burden compared to their richer counterparts

CPI inflation across income classes (% on-year)

Income segment	July		June	
	Rural	Urban	Rural	Urban
Top 20%	4.1	3.0	5.3	4.4
Middle 60%	4.1	2.9	5.8	4.9
Bottom 20%	4.0	2.7	5.8	5.0

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 July inflation trends. The table above presents the average inflation faced by each income class.

Source: NSSO, National Statistical Office, CEIC, CRISIL

IIP moderates as manufacturing, electricity slows

The Index of Industrial Production (IIP) moderated to 4.2% on-year in June, down from 6.2% in May. The moderation was mainly driven by a slowdown in manufacturing and electricity, while output growth in mining picked up significantly.

Manufacturing saw a broad-based slowdown in June. Consumer non-durables fell the most; durables slowed down as well, suggesting consumption recovery is yet to gain ground. Further, investment momentum seems to have cooled with government capital expenditure falling in the first quarter – which weighed on industrial goods.

A lower fiscal impulse could drag industrial growth this year, unless private capex picks up.

Industrial growth hinges on consumption revival, particularly in the rural areas. Monsoon remains critical for boosting agricultural growth and easing food inflation. The urban economy could be tempered by tighter credit conditions this year.

On a brighter note, better global trade prospects could benefit India's exports this fiscal.

Overall, we expect India's GDP growth to moderate to 6.8% this fiscal, over a strong 8.2% recorded in the previous year.

Data highlights

- IIP growth decreased to 4.2% on-year in June from 6.2% in the previous month. The index contracted 1.2% on-month after seasonal adjustments. The May reading was revised upwards from 5.9% previously
- The slowdown was driven by manufacturing (2.6% on-year versus 5.0% in the previous month), electricity (8.6% versus 13.7%), but growth in mining (10.3% versus 6.6%) picked up significantly
- The slowdown in manufacturing growth was broad-based across all use-based sectors. The worst performance was seen in consumer non-durables (-1.4% vs 2.5%), followed by capital goods (2.4% vs 2.9%), intermediate goods (3.1% vs 3.9%), infrastructure and construction goods (4.4% vs 6.3%), primary goods (6.3% vs 7.3%) and consumer durables (8.6% vs 12.6%)

Slowdown in industrial goods

- Primary goods recorded a moderation (6.3% on-year in June vs 7.3% in the previous month), driven by a significant decrease in electricity production growth (8.6% vs 13.7%) as well as contracting output of coke and refined petroleum products (-0.8% vs 2.0%)
- The moderation in capital goods (2.4% on-year in June vs 2.9% in the previous month) was driven by slowing output growth in machinery and equipment (1.5% vs 2.1%), fabricated metals (3.1% vs 12.3%) and other transport equipment (8.5% vs 16.8%)
- A drastic drop in output growth of basic metals (4.9% vs 8.3%) moderated output growth of infrastructure and construction goods (4.4% vs 6.3%). Further on-year contraction in government capex in June is also reflective of the moderation in this sector
- The performance in most export-oriented sectors such as pharmaceuticals, coke and refined petroleum products, machinery and equipment, fabricated metals and basic metals worsened. This deterioration was reflected in a sharp decrease in merchandise export growth in June (2.6% vs 12.8%)

Consumer goods also decelerates

- Consumer non-durables output shrunk on-year in June after some recovery in May (-1.4% vs 2.5%), driven by contraction in textiles (-1.7% vs -0.5%) and beverages (-1.0% vs 8.2%), as well as slowing output growth in wearing apparel (2.2% vs 9.8%). The weak performance of consumer non-durables in June is reflective of uncertainty regarding the revival of the rural economy, given scanty rainfall in most parts of India during the month
- Consumer durables recorded a moderation in on-year output growth (8.6% in June versus 12.6% in the previous month), driven by decreasing output growth in automobiles (4.1% vs 6.6%), computer and electronic products (10.7% vs 20.1%) and furniture (16.0% vs 33.9%)

Outlook

Industrial growth hinges on consumption revival this fiscal. In particular, rural demand that had slipped last fiscal, awaits better agricultural growth.

While the monsoon has been above normal so far, its intensity and distribution will determine agricultural prospects. That said, higher kharif sowing than last year augurs well for production.

The slowdown in consumer durables suggests the urban economy is shedding some buoyancy. This could be a reflection of the lagged impact of the RBI's rate hikes. The RBI's consumer confidence survey also shows urban consumer sentiment weakening since May.

A lower fiscal impulse is expected to weigh on industrial growth this year, as the government moves to curtail fiscal deficit. A pick-up in private capex is critical to sustain the investment momentum.

Slower global growth can restrict upside to goods exports owing to normalisation of supply chains and an expected pick-up in the volume of trade in 2024.

Overall, we expect India's GDP growth to moderate to 6.8% this fiscal, over a strong 8.2% recorded in the previous year.

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

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

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

Sanjay Lawrence
Media Relations
CRISIL Limited
M: +91 89833 21061
sanjay.lawrence@crisil.com

About CRISIL Market Intelligence & Analytics

CRISIL Market Intelligence & Analytics, a division of CRISIL, provides independent research, consulting, risk solutions, and data & analytics. Our informed insights and opinions on the economy, industry, capital markets and companies drive impactful decisions for clients across diverse sectors and geographies.

Our strong benchmarking capabilities, granular grasp of sectors, proprietary analytical frameworks and risk management solutions backed by deep understanding of technology integration, make us the partner of choice for public & private organisations, multi-lateral agencies, investors and governments for over three decades.

About CRISIL Limited

CRISIL is a leading, agile and innovative global analytics company driven by its mission of making markets function better.

It is India's foremost provider of ratings, data, research, analytics and solutions with a strong track record of growth, culture of innovation, and global footprint.

It has delivered independent opinions, actionable insights, and efficient solutions to over 100,000 customers through businesses that operate from India, the US, the UK, Argentina, Poland, China, Hong Kong, UAE and Singapore.

It is majority owned by S&P Global Inc, a leading provider of transparent and independent ratings, benchmarks, analytics and data to the capital and commodity markets worldwide.

For more information, visit www.crisil.com

CRISIL Privacy Notice

CRISIL respects your privacy. We may use your personal information, such as your name, location, contact number and email id to fulfil your request, service your account and to provide you with additional information from CRISIL. For further information on CRISIL's privacy policy please visit www.crisil.com/privacy.

Disclaimer

CRISIL Research, a division of CRISIL Limited (CRISIL) has taken due care and caution in preparing this Report based on the information obtained by CRISIL from sources which it considers reliable (Data). However, CRISIL does not guarantee the accuracy, adequacy or completeness of the Data / Report and is not responsible for any errors or omissions or for the results obtained from the use of Data / Report. This Report is not a recommendation to invest / disinvest in any company covered in the Report. CRISIL especially states that it has no financial liability whatsoever to the subscribers/ users/ transmitters/ distributors of this Report. CRISIL Research operates independently of, and does not have access to information obtained by CRISIL's Ratings Division / CRISIL Risk and Infrastructure Solutions Limited (CRIS), which may, in their regular operations, obtain information of a confidential nature. The views expressed in this Report are that of CRISIL Research and not of CRISIL's Ratings Division / CRIS. No part of this Report may be published / reproduced in any form without CRISIL's prior written approval.

Argentina | China | Hong Kong | **India** | Poland | Singapore | UK | USA | UAE

CRISIL Limited: CRISIL House, Central Avenue, Hiranandani Business Park, Powai, Mumbai – 400076. India
Phone: + 91 22 3342 3000 | Fax: + 91 22 3342 3001 | www.crisil.com

/company/crisil-global-research-&-risk-solutions @CRISILGRRS /CRISILLimited /user/CRISILLimited Follow us on @lifeatcrisil

CRISIL
An S&P Global Company