India: CPI seen at 3.7% on base effects, IIP slowed to 5.2%

06th August 2024

July CPI likely clocked c.5 year low of 3.74% led by base effects

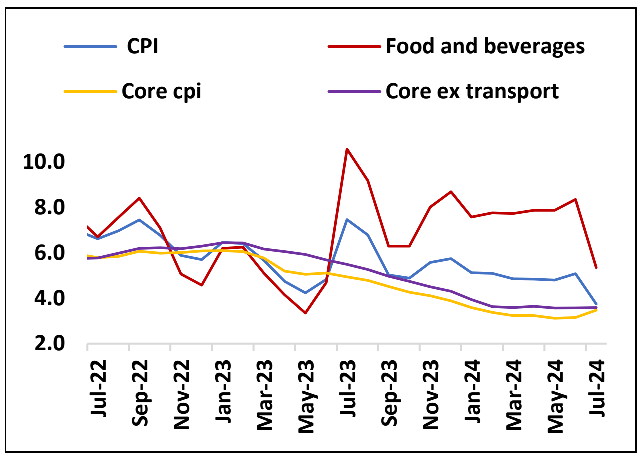
- **High base effect likely pulled CPI down to multi month low in July'24:** We estimate the headline inflation to slow down to 3.74% in July'24 vs 5.08% in last month mainly due to high base effect even as core inflation likely took a U turn. CPI was a 15-month high of 7.44% in July'23 pushed by food inflation prevailing at 11.5% (*refer fig.1*). Sequentially food prices, especially vegetables have been rising at a fast pace; base effect is only playing a role in suppressing y/y inflation. The base effect however is a temporary reprieve and will likely fade in the coming months.

- Rainfall has improved to 7% cumulative surplus as on 05th August'24 from a deficit of 11% in June end. Subsequently, the reservoir levels as % of live capacity has also seen a sharp pickup in July. The level of storage in water reservoirs has bounced up sharply from 20% in last week of June'24 to 51% on 01st August'24. Notwithstanding the surplus rainfall, spatial distribution continues to be uneven and needs close watch. While central India has seen a sharp recovery during the month from a 14% rainfall deficit to 21% surplus, north-west region is still in a deficit of 8% and east & northeast region in deficit of 13%. South India continues to be the region with consistently high surplus.

- With the progress of monsoon, sowing of kharif crops has also picked up satisfactorily signaling supply side relief in the coming months soothing the food inflation positively. Total crop sowing area which was just 24.1 million hectares on 28th June has gone up sharply to 90.5 million hectares as on 02nd August this year. This is 3% higher as compared to the sowing area a year back. Pulses' sowing has seen the highest pickup y/y (11%) that may help provide salutary effect on pulses' inflation in the coming months. Going forward, however, the key north west region with concerns of prolonged deficit, will have to be keenly watched out.

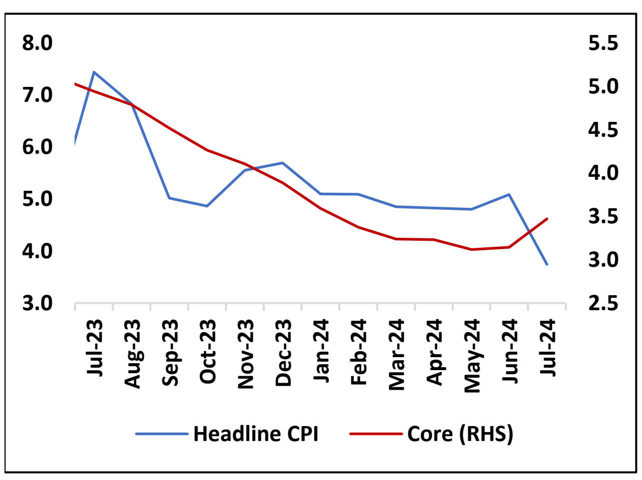
- Food inflation which was 11.5% in July'23 and 9.3% in June'24 is expected to ease to 5.7% in July'24 on back of high base effect, especially in vegetables inflation (37.4% in July'23). Y/Y vegetable inflation in July likely eased to 7.1% this year though sequentially, m/m inflation possibly continues in double digit (our estimate: 14.4%). Cereals inflation too is expected to see a fall from 13% July last year to 7.1% July this year. On sequential basis, mainly vegetables prices remain elevated even as on-the-ground prices of cereals and oils etc are either seeing some softening or staying more or less at the same levels. CPI ex-vegetables is seen easing further to 3.4% in July (3.5% in June) (*refer fig.3&4*).

Fig 1: Headline CPI likely cooled off in July'24 while core CPI inches up; % y/y



Source: CEIC, UBI Research

Fig.2. Core inflation likely saw a pickup in July'24 on telecom tariff hikes



Source: CEIC, UBI Research

Note: Figures for July are our projections

Fig 3: Vegetables index shows a sharp seasonal spike even as the food CPI sees some softening

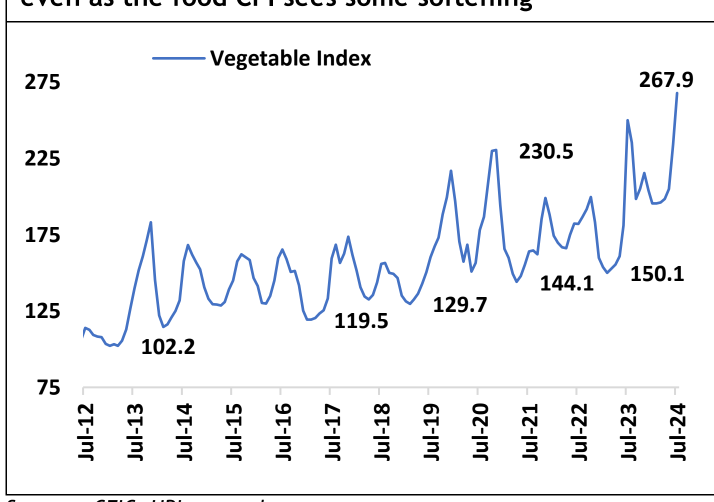
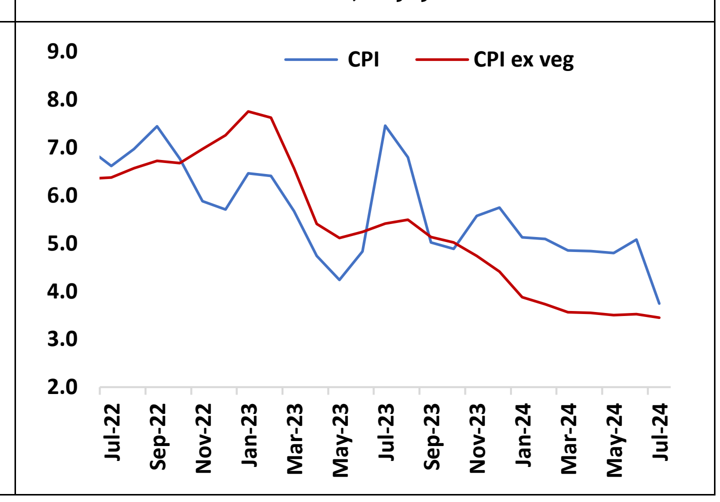


Fig 4: CPI ex veggies at 3.4% slips below previous month's number of 3.52%; % y/y



Sources: CEIC, UBI research

- Noticeably, core inflation likely saw first significant pickup in 20 months after remaining at record lows in Q1FY25, on account of steep mobile tariff hikes of 10-25% across various packs during the month. We expect core inflation to move up from 3.14% in June'24 to 3.47% in July'24 (*refer fig.2*) on account of telecom tariff hikes even as core ex transport inflation likely remained unchanged at 3.6%. The spill over may continue for next few months as well. Given weight of mobile tariffs at 1.84% in headline CPI and a tariff hike of 10-25%, we assume a proportional impact of close to 15bps in headline inflation.
- In the coming months, the focus is likely to remain on food inflation which is vulnerable to monsoon trends especially spatial distribution. Given the good pickup in monsoon and crop sowing, food inflation outlook appears favourable yet needs close watch. Apart from this, the spillover impact of global growth concerns and downward pressure on commodity prices poses downside risk to our and MPC's forecast of 4.5% inflation in FY25 vs 5.4% in FY24.

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Industrial Production likely to have moderated in June'24

- Industrial production growth, as indicated by IIP, is likely to be lower at 5.2%, from the higher than expected 5.9% in previous month and vs 4.0% in June'23.
- High frequency indicators showed a mixed trend in June'24 vs May'24. Indicators such as e-way bills, toll collections, automobile sales and domestic tractor sales, pointed towards sustained momentum in domestic demand conditions. However, vehicle registrations, average daily petroleum consumption, moderated in June. While exports growth was muted at 2.6%, auto production growth continued to stay in double digits.
- Core sector has 40% contribution in IIP and has declined to 4.0% in June'24 (slowest growth since Nov'22) from 6.4% in May'24. The decline was driven by lower growth in five of the eight sectors, except coal, fertilizer, and cement, compared to May.
- The YoY performance of electricity generation slowed in June'24 relative to May'24, due to lower demand with the start of the monsoon season. Power production in June declined due to fall in hydropower generation and delays in the commissioning of 3.6 GW of new coal-fired plants, which could have led to supply disruptions.
- Mining growth likely to have improved, as demand for coal and natural gas has stayed strong as reflected in core sector data.
- Consumer non-durables continued to show signs of recovery with consumer durables staying strong.
- Capital goods and infrastructure/construction goods IIP growth may have slowed in June due to a combination of factors including the impact of above normal monsoons in some parts of the country and contraction by 35% in capex expenditure growth during an election quarter.
- Going forward, we continue to expect IIP growth to stay in single digits, with a watch on monsoon effect on rural demand.

Fig 5: IIP likely to have eased in Jun'24; % y/y

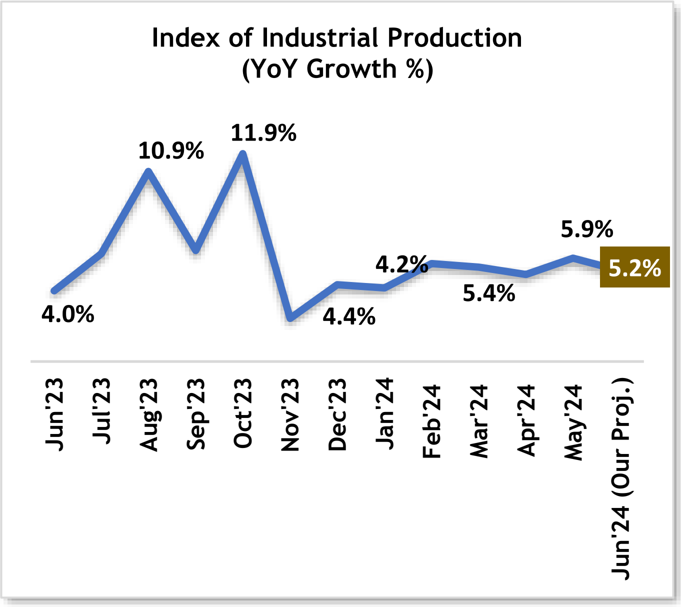

Fig 6: Slowdown in electricity likely lowered Jun'24 IIP growth; % y/y

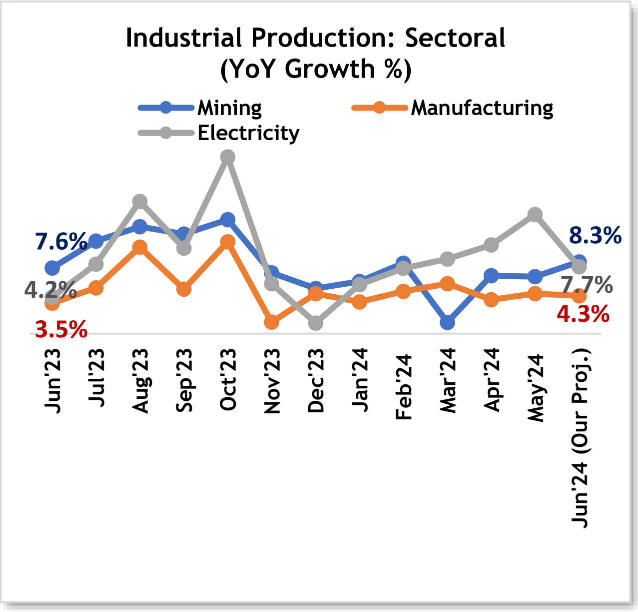

Fig 7: Consumer durables likely continued to show strong performance in Jun'24

Industrial Production: Sectoral				
Sector	Weight	YoY Growth %		
		Apr'24	May'24	Jun'24
Mining	14.4	6.7%	6.6%	8.3%
Manufacturing	77.6	3.9%	4.6%	4.3%
Electricity	8.0	10.2%	13.7%	7.7%
Industrial Production: Use-based				
Primary goods	34.0	7.0%	7.3%	5.9%
Capital goods	8.2	2.7%	2.5%	1.9%
Intermediate goods	17.2	3.2%	2.5%	2.5%
Infrastructure / Construction Goods	12.3	8.0%	6.9%	5.8%
Consumer durables	12.8	10.0%	12.3%	13.4%
Consumer non-durables	15.3	-2.5%	2.3%	2.4%

Source: CEIC, UBI Research

Note: Jun'24 is our estimate.

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