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Some degree of comfort on inflation

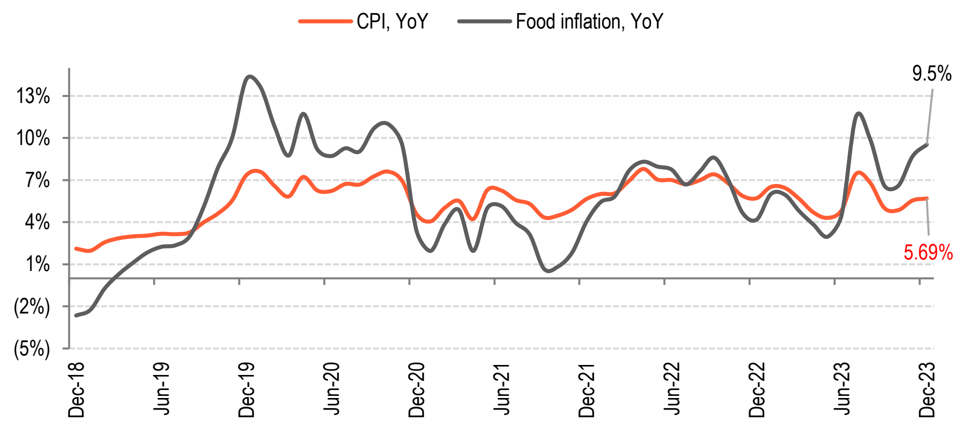
CPI print came in lower than expected at 5.69% (BoB estimate at 5.55%). Food inflation picture is better understood this month by looking at the sequential picture. Major correction was seen in vegetable prices. Notably, CPI excluding vegetables and pulses is at 4% in Dec'23. Core continued to be on the downside and major driven demand components showed moderation. In Jan-24, CPI is likely to moderate further as seen in softer high frequency indicator of prices. Even the current flare up of tensions in the Red Sea is likely to have limited impact on retail inflation as pump prices have remained sticky. So we don't see significant upside risk to inflation going ahead.

CPI inflation slightly higher due to base effect

CPI below estimates: CPI inflation surprised, coming in at lower than expected at 5.69% in Dec'23, on YoY basis (BoB Best: 5.55%) and against street estimate of 5.9%. The moderate inching up of CPI is on account of a slight unfavourable base. Food inflation remained sticky inching up to 9.5% from 8.7% in Nov'23. This was led by firming up of prices in vegetables (27.6% from 17.7%), pulses (20.7% from 20.3%) and sugar (7.1% from 6.6%). Despite some stickiness, moderation in 7 out of 20 broad categories of food has been observed. Among them, the most notable was meat and fish (1.1% from 2.2%), cereals (9.9% from 10.3%), spices (19.7% from 21.5%), amongst others.

On sequential basis, food inflation has fallen for the first time since Sep'23 by 0.3%. Among major commodities, the drop was sharpest for vegetables, fruits, pulses, sugar and spices. Correction in tomato, onion prices have provided the comfort to inflation. Seasonality came into play in bringing down prices as on a seasonally adjusted basis, food inflation inched up subtly by 0.8%.

Figure 1: CPI inched up slightly led by food



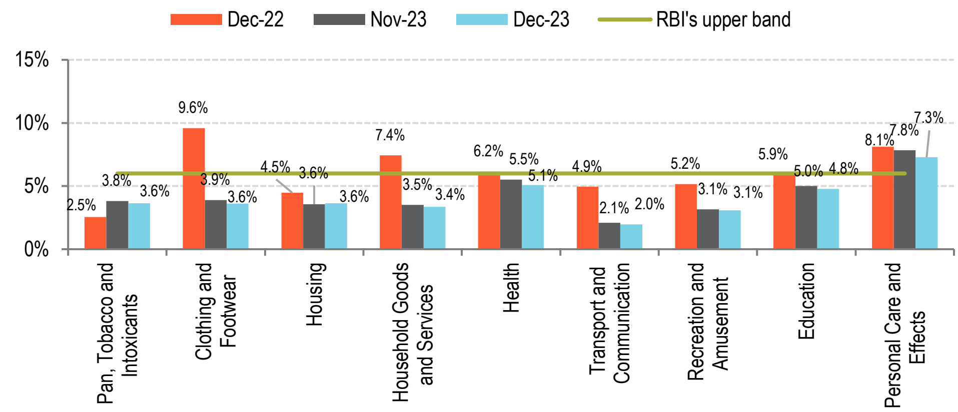
Source: CEIC, Bank of Baroda Research

Notably, CPI excl. vegetables is at 4.5% and CPI excl. vegetables and pulses has reached 4% in Dec'23.

Core CPI (excl. food and fuel) has moderated further to 3.9%. All broad sub components of core noticed a drop in inflation in Dec'23. Especially the demand driven components such as clothing and footwear (3.6% from 3.9%), household goods and services (3.4% from 3.5%), personal care and effects (7.3% from 7.8%), are easing considerably. Apart from this, other services inflation such as health (5.1% from 5.5%), education (4.8% from 5%) and recreation and amusement (at 3.1%) are all losing its earlier stickiness. Some of it is partly attributable to base effect. In fact core services inflation as per our analysis is trailing ~3-3.1%.

The sequential picture also shows moderation (0% against 0.2% increase in Nov'23) led by education, personal care and effects (due to lower gold prices in Dec'23) and transport and communication component. However, the sequential built up of household goods and services remains to some extent.

Figure 2: Core remains comfortable



Source: CEIC, Bank of Baroda Research

Fuel and Light inflation has fallen by 1% from 0.8% decline seen in Nov'23, on YoY basis. This is on account of lower Kerosene prices.

Way forward: CPI print came in slightly higher than our estimate. However, the moderation of prices was evident from the correction in major items of vegetables, which is now coinciding with the harvest month. Further correction is also forthcoming. The high frequency price data of Jan-24 enumerates the same. Our in house BoB ECI has fallen by 0.8% in Jan-24, with major sequential drop seen in onion, tomato, salt, sugar, pulses and cereals. Rabi sowing is also slightly lagging behind.

Thus we do not see any immediate upside risk to inflation. However, the recent developments in Red Sea might pose upside risk to international crude prices. The transmission to domestic prices is limited, as pump prices are unlikely to change in the immediate to medium term. The next two months will also witness favorable base and CPI is likely to be in the range of 4.5-5%.

Growth in Industrial Production slows down

IIP growth eases: IIP growth moderated down to 8-month low of 2.4% in Nov'23 much below our expectations (6%) and compared with a growth of 11.6% in Oct'23. The slowdown was primarily attributable to moderation across all the sectors. Growth in mining and electricity sector eased to 6.8% (13.1% in Oct'23) and 5.8% (20.4% in Oct'23) in Nov'23. Output of manufacturing sector decelerated down to 1.2% in Nov'23 against a growth of 10.2% in Oct'23. Amongst manufacturing sectors, barring one subdivison, all the other subdivisions have registered much slower growth in Nov'23. Manufacture of leather products (-16.2% versus 16.5% in Oct'23), electrical equipment (-16.8% versus 13.2%), machinery and equipment (-0.9% versus 26.1%) and manufacture of furniture (-30.5% versus -7.2%) have recorded sharpest contraction in Nov'23. The only subdivision that has registered positive growth is manufacture of coke and petroleum products at 14.2% (2.4% in Oct'23). On a FYTD basis (Apr-Nov), industrial growth has edged up to 6.4% in FYTD'24 from 5.6% in FYTD'23. Mining and manufacturing growth has expanded to 9.1% and 5.8% respectively in FYTD'24, while electricity growth has moderated by 7.7% in FYTD'24 (9.8% in FYTD'23).

Broad based slowdown: Within use-based, all the sectors have registered much lower growth in Nov'23. Growth in primary goods slipped down to 8.4% against a growth of 11.4% in Oct'23. Even intermediate and infra goods have registered sharp deceleration at 3.5% (9.4% in Oct'23) and 1.5% (11.3% in Oct'23) respectively in Nov'23. The subdued growth raises some concerns for construction and real estate activity. Capital goods output contracted sharply down to (-) 1.1%, a 13-month low from a double digit growth registered in Oct'23. Moreover, growth in rural demand has been tepid and has added to concerns around consumption story, the output of both consumer durable and FMCG output has also declined in Nov'23 to (-) 5.4% and (-) 3.6% respectively.

Way Forward: Going ahead, the focus is expected to shift towards interim budget which is a vote on account with the possibility of higher capital outlay with the objective to support growth. As the global economy is likely to witness slowdown, exports are expected to be weaker and needs to be monitored carefully. For other indicators, domestic economy remains resilient with the advance estimate also suggesting a much higher growth in FY24. Industrial output for Oct-Nov'23 has expanded to 7% against a growth of 1.8% in Oct-Nov'22.

Table 1: IIP growth moderates

Sectoral (%)	Weight	Nov-23	Oct-23	Nov-22	Apr-Nov'24	Apr-Nov'23
IIP	100.0	2.4	11.6	7.6	6.4	5.6
Mining	14.4	6.8	13.1	9.7	9.1	4.7
Manufacturing	77.6	1.2	10.2	6.7	5.8	5.1
Electricity	8.0	5.8	20.4	12.7	7.7	9.8
Use-Based						
Primary Goods	34.1	8.4	11.4	4.8	7.2	7.7
Capital Goods	8.2	(1.1)	21.3	20.7	7.5	14.8
Intermediate Goods	17.2	3.5	9.4	3.5	4.9	5.1
Infrastructure and Construction Goods	12.3	1.5	11.3	14.3	11.1	7.8
Consumer Durables Goods	12.8	(5.4)	15.9	5.0	0.6	5.3
Consumer Non-Durables Goods	15.3	(3.6)	8.6	10.0	5.6	(2.2)

Source: CEIC, Bank of Baroda Research

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