

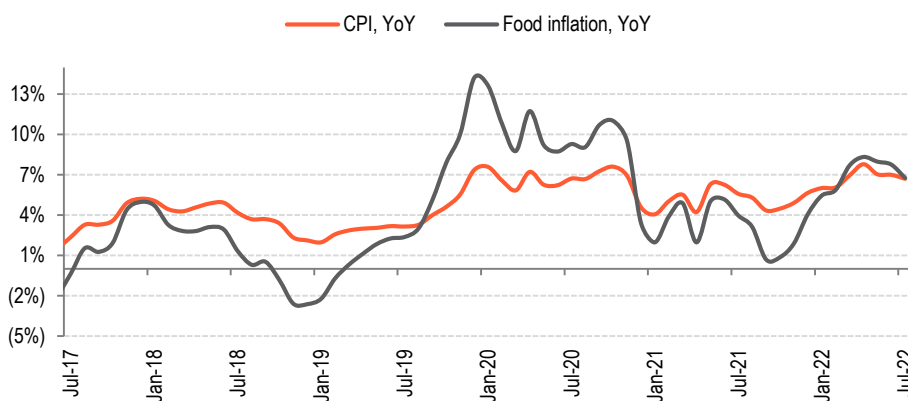
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CPI moderates, IIP growth weakens

Headline CPI cooled off to 6.9% in Jul'22 from 7% in Jun'22. Food inflation eased to 6.8% (7.7% in Jun'22) led by vegetables, meat and fish and oils and fats. Core inflation eased further to 5.7% in Jul'22 on the back of softening of prices for transport and communications, personal care and health. Despite cooling-off, CPI remains above RBI's target level. On the other hand, industrial growth decelerated to 12.3% in Jun'22 (19.6% in May'22) led by broad based moderation across manufacturing, mining and electricity sectors. Going ahead, investors will monitor geopolitical tensions emerging from China-Taiwan as this could impact global demand.

CPI inflation begins to ease: Against our estimate of 6.9%, CPI came in slightly lower at 6.7% in Jul'22, also down from 7% in Jun'22. Food inflation moderated further to 6.8% from 7.7% in Jun'22. This was supported by softening prices of vegetables (10.9% in Jul'22 versus 17.3% in Jun'22), meat and fish (3% versus 8.6%), oils & fats (7.5% versus 9.4%) and milk & milk products (5.8% versus 6.1%). On the other hand, prices of fruits (6.4% versus 3.1%), cereals (6.9% versus 5.7%), sugar (4.8% versus 4.2%) and spices (12.9% versus 11%) inched even higher in Jul'22. Prices of eggs contracted less sharply (-3.8% versus -5.5%) and that of pulses (0.2% versus -1%) increased after falling in the previous two months. However, outlook for food inflation in the coming months might get some comfort from retailers agreeing to reduce prices of edible oils and a normal monsoon (8% above LPA).

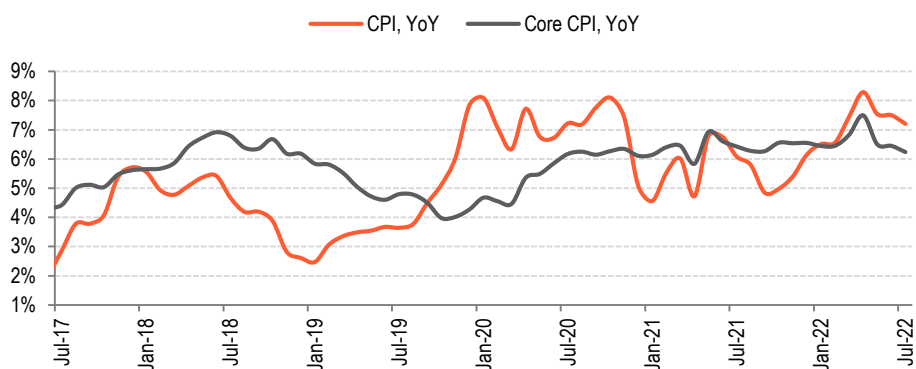
Fig: 1 CPI falls below 7%, aided by food inflation



Source: CEIC, Bank of Baroda Research

Core inflation continues to ease: Core inflation edged down by 30bps to 5.7% in Jul'22 from 6% in Jun'22, on YoY basis. Moderation was on account of sharp dip in transport and communication inflation (5.6% from 6.9% in Jun'22), followed by personal care and effects (6% versus 6.7%) and health (5.4% versus 5.5%). International gold prices too declined in Jul'22 by 2.7% (YoY), following 2.1% increase in Jun'22. On the other hand, demand side pressure continued. Inflation in the Clothing and footwear segment inched up to 9.9% in Jul'22 from 9.5% in Jun'22. For recreation and amusement (7.1% from 7%) and education (5% versus 4.5%) as well, the uptick was visible.

Fig: 2 Core CPI also cooling down



Source: CEIC, Bank of Baroda Research

Inflation still above RBI's target: While the latest print brings in relief, led by easing food and fuel inflation, it still remains above RBI's target band. However, with easing international commodity prices and normalizing of supply chain logistics, it can be expected that inflation might cool down further. However, key downside risks remain. These include geo-political tensions in the Taiwan Strait which could impact the supply of semi-conductor chips and overheating of global demand led by easing inflation which could in turn put pressure on international oil prices. In addition, with gradual easing of monsoon, we expect services to return running at full capacity in the coming months. We expect inflation to still be heated at around 6.5% in FY23.

Industrial Production

IIP growth eases: Industrial output slowed to 12.3% in Jun'22 from 19.6% in May'22. This was led by moderation across sectors, manufacturing (12.5% from 20.6% in May'22), mining (7.5% from 11.2% in May'22) and electricity (16.4% from 23.5% in May'22). Within manufacturing, other transport equipment (30.2% from 128.5%), beverages (44.8% from 128.1%), motor vehicles (31.2% from 88.7%), leather products (0.9% from 48.9%) and electrical equipment (11.8% from 59.6%) registered the sharpest dip in Jun'22 compared with last year. Notably, IIP growth has improved by 6.7% in Jun'22 compared with the pre-pandemic levels.

Consumer durable and Capital goods disappoints: Within use-based, broad based moderation was noticed across all the sectors. Consumer durable (23.8% from 58.4%), capital goods (26.1% from 54.4%) and Infra goods (8% from 18.1%) registered sharp moderation in Jun'22. Output of primary (13.7% from 17.8%) and intermediate goods (11% from 17.5%) also decelerated in Jun'22. The only bright spot was FMCG production which improved by 2.9% in Jun'22 (1% in May'22).

Recovery may face headwinds: The economy continues to ride the wave of recovery (expected to be higher in H2FY23) as has also been reflected by high frequency indicators led by manufacturing PMI soaring to 8-month high, along with surge in GST collections. However, the recovery might face global headwinds on the back of ongoing geopolitical tensions emerging between US and China-Taiwan. This might have an impact on semiconductors availability as Taiwan remains a leader with largest market share, globally.

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