

INFLATION

13 August 2020

Accelerating inflation, RBI to maintain status quo

CPI inflation accelerated to 6.9% in Jul'20 (6.2% in Jun'20) led by higher food and core inflation. Only 3 food items have reported an inflation level below 4%. The drivers of core inflation are personal care at 13.6% and transport and communication at 10%. Housing and recreation are muted and expected to remain so. However, core tends to be sticky and supply bottlenecks are impacting food. This implies that CPI inflation is likely to remain above RBI's target of 4% making further rate cuts difficult for now.

Sameer Narang

+91 22 6698 5713

chief.economist@bankofbaroda.com

Dipanwita Mazumdar

dipanwita.mazumdar@bankofbaroda.com

Aditi Gupta

aditi.gupta3@bankofbaroda.com

CPI accelerates further: CPI surprised negatively at 6.9% in Jul'20 compared with 6.2% in Jun'20. Notably, Jun'20 estimate has been revised upwards from 6.1%. Both food and core inflation inched up. While food inflation went up 80bps MoM, core increased by 50bps MoM.

Food inflation picks up: Food inflation increased to 9.6% in Jul'20 from 8.7% in Jun'20 led by higher vegetable prices (11.3% from 4% in Jun'20). One can see a broad based increase in food inflation. Out of 12 food and beverages items, as many as 5 are showing double digit growth led by meat and fish at 18.8% and pulses at 15.9%. Egg at 8.8%, cereals at 7%, milk at 6.6% and beverages at 4.4% are in the range of 4-10%. Only 3 items, have reported an inflation less than 4%. Given the above backdrop, we see relatively elevated food inflation in coming months before easing in winter when base effect plays out.

Core inflation also rises: CPI excluding food and fuel rose by 50bps to 5.9% in Jul'20 from 5.4% in Jun'20. The upward momentum was led by household goods and services (3.1% from 1.8%), transport and communication (10% from 8.3% in Jun'20), education (3.2% from 2.6%) and personal care items (13.6% from 12.9%). Rising crude (6% in Jul'20), gold (6.3%) and other commodity prices (4.9%), contributed towards higher core. In the last 8 years, core inflation has been at 4% or less only once, that too in FY20. The current trajectory shows it is unlikely to average 4% this year.

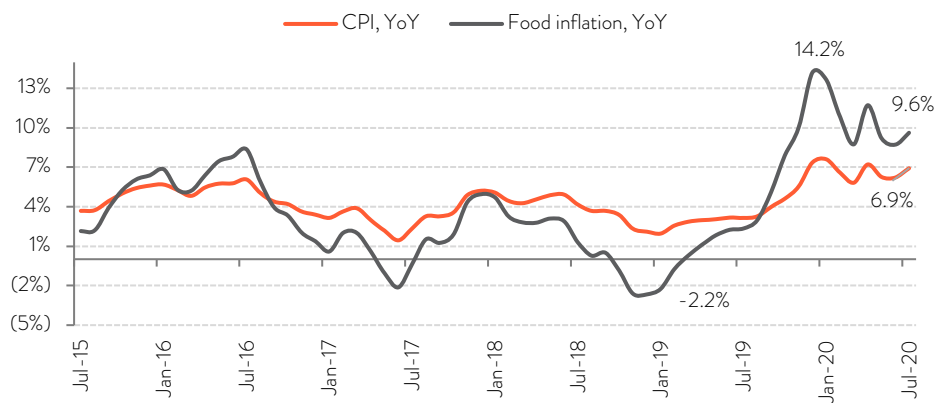
Further easing difficult: The current trajectory of inflation implies a low probability of any further rate cut. CPI inflation for this and next year is estimated at 5.5% and 4.5% which is higher than RBI's target of 4%. Only a sharp fall in both core and food inflation can change our view. We believe, supply side bottlenecks are likely to ensure food inflation remains elevated in the near-term. Core inflation is also expected to remain sticky.

KEY HIGHLIGHTS

- CPI rose to 6.9% in Jul'20 from 6.2% in Jun'20.
- Led by food inflation, fuel and light and core inflation.
- RBI's rate cut cycle seems to be behind us.

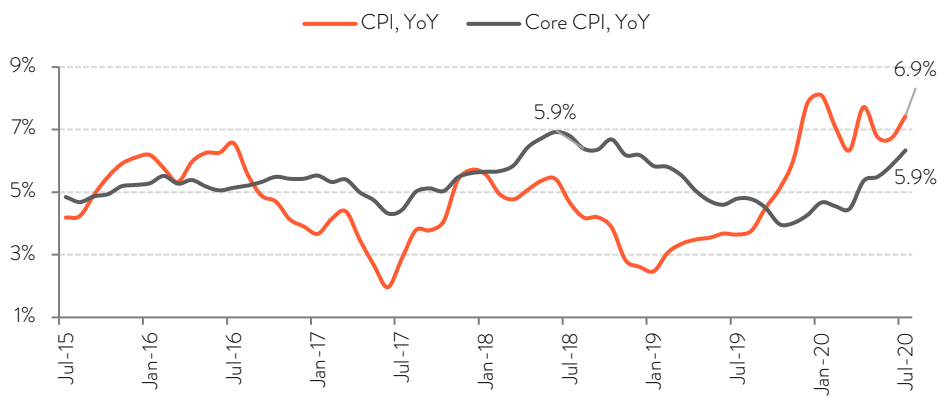


FIG 1 – CPI ROSE TO 6.9% IN JUL'20 FROM 6.2% IN JUN'20, LED BY FOOD (9.6% FROM 8.7% IN JUN'20)



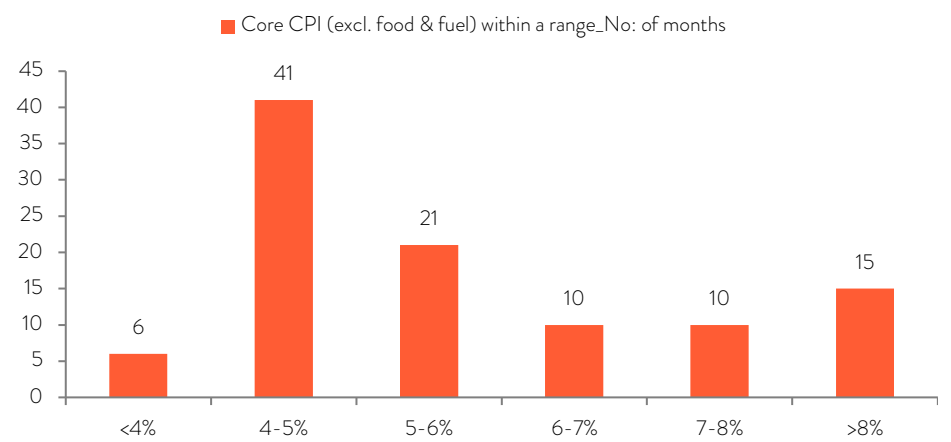
Source: CEIC, Bank of Baroda Research

FIG 2 – ...CORE ALSO CONTRIBUTED TO THIS ACCELERATION (5.9% FROM 5.4% IN JUN'20)



Source: CEIC, Bank of Baroda Research

FIG 3 – CORE MOSTLY SETTLES ABOVE 4%



Source: CEIC, Bank of Baroda Research

Disclaimer

The views expressed in this research note are personal views of the author(s) and do not necessarily reflect the views of Bank of Baroda. Nothing contained in this publication shall constitute or be deemed to constitute an offer to sell/ purchase or as an invitation or solicitation to do so for any securities of any entity. Bank of Baroda and/ or its Affiliates and its subsidiaries make no representation as to the accuracy; completeness or reliability of any information contained herein or otherwise provided and hereby disclaim any liability with regard to the same. Bank of Baroda Group or its officers, employees, personnel, directors may be associated in a commercial or personal capacity or may have a commercial interest including as proprietary traders in or with the securities and/ or companies or issues or matters as contained in this publication and such commercial capacity or interest whether or not differing with or conflicting with this publication, shall not make or render Bank of Baroda Group liable in any manner whatsoever & Bank of Baroda Group or any of its officers, employees, personnel, directors shall not be liable for any loss, damage, liability whatsoever for any direct or indirect loss arising from the use or access of any information that may be displayed in this publication from time to time.

Visit us at www.bankofbaroda.in



For further details about this publication, please contact:

Economics Research Department

Bank of Baroda

+91 22 6698 5713

chief.economist@bankofbaroda.com