

## INFLATION AND IIP

12 February 2019

### Core drags inflation to 19-month low

**CPI surprised positively at 2.1% vs estimate of 2.5%. This was led by 30bps decline in core to 5.4%. It was quite broad-based with dip seen in transport & communication, education, recreation and clothing. Food prices continued to deflate and outlook is benign. While inflation has moderated further, IIP growth inched up to 2.4% in Dec'18 led by infra/ construction, capital and FMCG sectors. Jan'19 PMI shows the trend may sustain. Given the growth and inflation mix, we believe MPC to cut rate by another 25bps in Apr'19.**

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**IIP growth recovers:** Industrial output rose by 2.4% in Dec'18 versus 0.3% in Nov'18 led by manufacturing sector which grew 2.7% versus (-) 0.6% in Nov'18. This was partly driven by base effect. Infra/ construction goods clocked double digit growth of 10.1% in Dec'18 from 5% in Nov'18 led by cement and steel. Despite lower government spending, growth in capital goods increased to 5.9% (vs -3.1% in Nov'18). Even FMCG growth improved to 5.3% (-0.6% in Nov'18) in Dec'18. Notably, manufacturing PMI has further improved in Jan'19 which may support manufacturing growth.

**Food inflation remains benign:** Food inflation continued to deflate for the 4<sup>th</sup> consecutive month in Jan'19 at (-) 2.2% YoY compared with (-) 2.6% in Dec'18. This was led by (-) 13.3% decline in vegetables prices in Jan'19 (vs -16.4% in Dec'18). Fruit prices also fell by (-) 4.2% versus (-) 1.5% dip in Dec'18. Cereals prices moderated to 0.9% in Jan'19 from 1.3% in Dec'18. However, upside pressure is seen building in certain protein based items such as meat & fish. However, given that Indian cereal prices are at or far below international prices, food inflation is likely to remain benign.

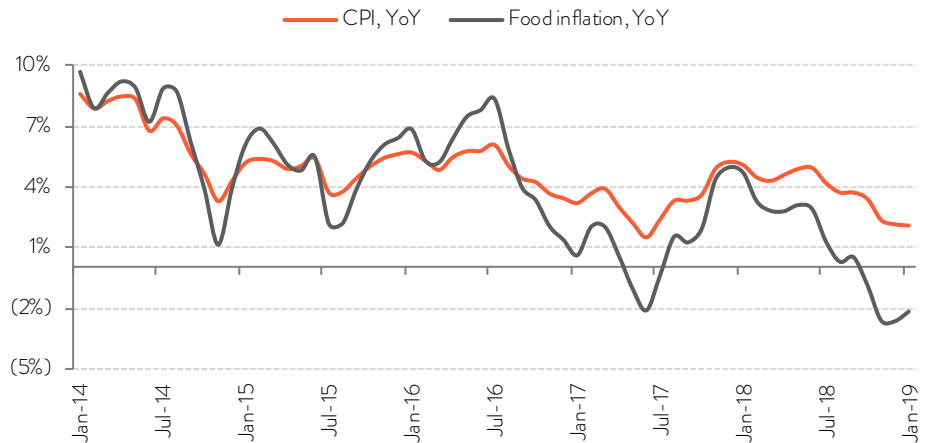
**Core inflation down to 10-month low:** Core inflation moderated by 30bps to 5.4% in Jan'19 vs 5.7% in Dec'18. This was led by transport & communication at 3.4% in Jan'19 compared with 4.3% in Dec'18. This was despite a 15% increase in international crude prices in Jan'19. Other core items also saw deceleration. For instance, inflation in recreation & amusement decelerated by 60bps to 5.4% in Jan'19 versus Dec'18, in education it decelerated by 40bps to 8% in Jan'19, and in clothing & footwear it decelerated by 40bps to 3% in Jan'19. However, in household goods & services and health categories inflation continued to remain sticky. The broad-based dip in core inflation is a positive sign, however some increase in transport segment is likely in the next month.

#### KEY HIGHLIGHTS

- CPI inflation at 19-month low of 2.1% in Jan'19.
- Core inflation down to 5.4%. vs 5.7% in Dec'18.
- IIP growth revives to 2.4% in Dec'18.

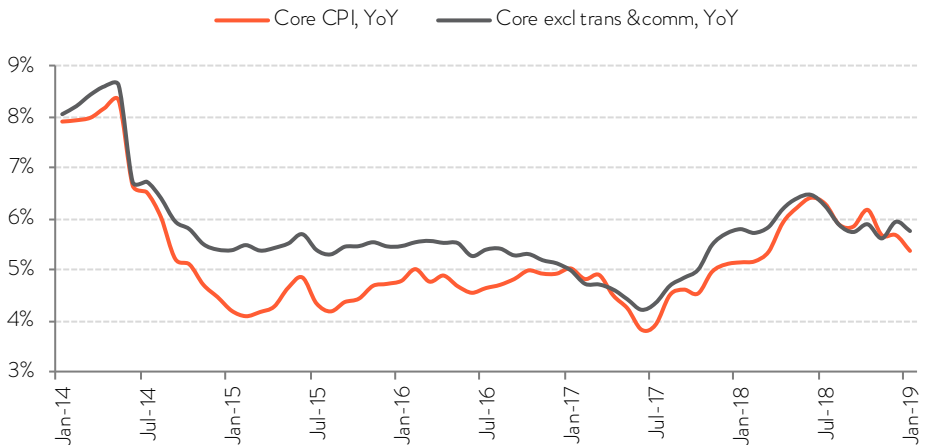


**FIG 1 – CPI AT 19-MONTH LOW OF 2.1%**



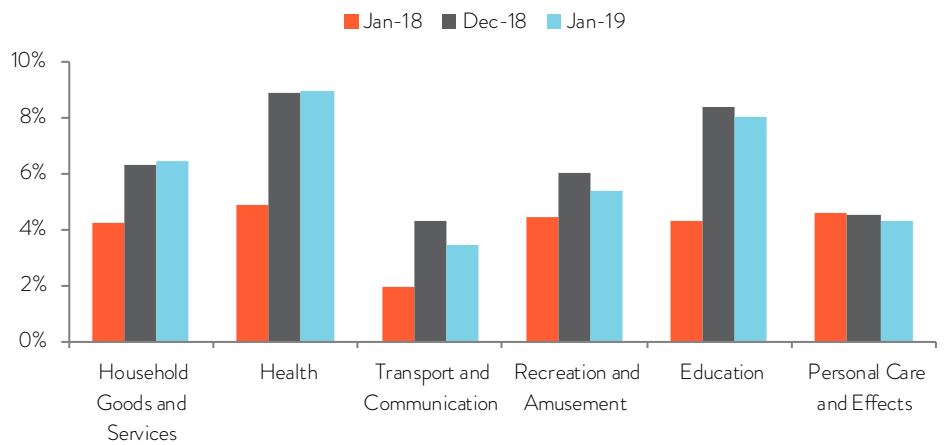
Source: CEIC, Bank of Baroda Research

**FIG 2 – CORE INFLATION LOWEST SINCE MAR'18**

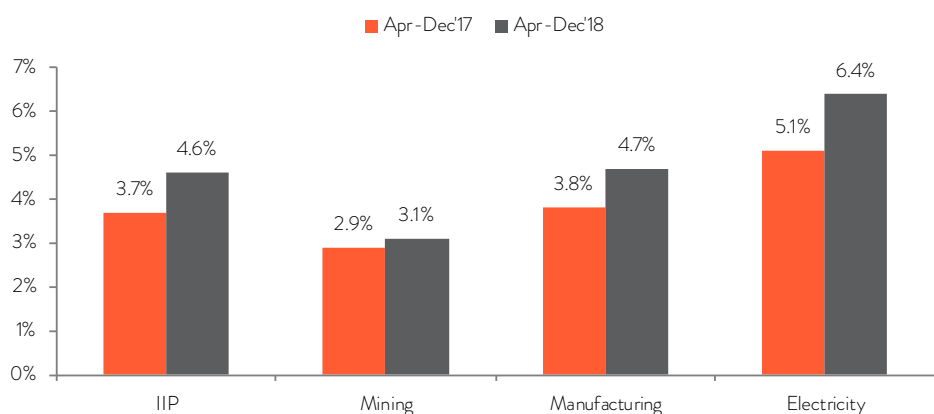


Source: CEIC, Bank of Baroda Research

**FIG 3 – DECLINE IN CORE WAS BROAD BASED**



Source: CEIC, Bank of Baroda Research

**FIG 4 – IIP GROWTH REVIVES**

Source: CEIC, Bank of Baroda Research

**FIG 5 – IMPROVEMENT LED BY INFRA/CONSTRUCTION GOODS**

Sectoral (%)	Weight	Dec-18	Nov-18	Dec-17	Apr-Dec'18	Apr-Dec'17
IIP	100.0	2.4	0.3	7.3	4.6	3.7
Mining	14.4	(1.0)	2.7	1.2	3.1	2.9
Manufacturing	77.6	2.7	(0.6)	8.7	4.7	3.8
Electricity	8.0	4.4	5.1	4.4	6.4	5.1
<b>Use-Based</b>						
Primary Goods	34.1	(1.2)	3.2	3.8	4.1	3.5
Capital Goods	8.2	5.9	(3.1)	13.2	7.1	2.7
Intermediate Goods	17.2	(1.5)	(4.9)	7.5	0.3	1.8
Infrastructure and Construction Goods	12.3	10.1	5.0	6.5	8.5	4.3
Consumer Durables Goods	12.8	2.9	(2.1)	2.1	7.5	(1.1)
Consumer Non-Durables Goods	15.3	5.3	(0.6)	16.8	4.1	10.5

Source: CEIC, Bank of Baroda Research

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