

INFLATION AND IIP

12 June 2020

Food inflation falls, industrial output contracts sharply

India's industrial production contracted by 55.5% in Apr'20 on the back of a nationwide lockdown led by 95.7% and 92% reduction in consumer durables and capital goods respectively. As supply side restrictions eased in May'20, food inflation fell to 9.3% from 10.5% in Apr'20. However, core inflation data was not available apart from housing and health. Notably, health inflation did inch up. We do believe sharp contraction in growth warrants another rate cut by RBI to mitigate the impact on the economy.

Sameer Narang

+91 22 6698 5713

chief.economist@bankofbaroda.com

Dipanwita Mazumdar

dipanwita.mazumdar@bankofbaroda.com

Jahnavi

jahnavi@bankofbaroda.com

IIP growth plummets: Industrial output declined by 55.5% in Apr'20 from a decline of 18.3% in Mar'20 on the back of nationwide lockdown. The decline was led by manufacturing sector which contracted by 64.3% compared with a decline of 22.4% in Mar'20. Within manufacturing, consumer durables contracted by 95.7% in Apr'20, capital goods declined by 92% and infrastructure goods fell by 83.9%. Mining and electricity output also contracted by 27.4% and 22.6% respectively. Industrial activity will see improvement in coming months as unlocking of the economy has begun though there are supply side challenges in the form of labour availability.

Food inflation falls: Consumer food inflation moderated by 120bps to 9.3% in May'20 from 10.5% in Apr'20. This was led by sharp fall in vegetable inflation to 5.3% against 23.6% in Apr'20. It was expected as lockdown restrictions have been eased. Apart oils and fats and non-alcoholic beverages, deceleration was seen across the food group. Food inflation is likely to ease further as supply side bottlenecks have been further removed. Even international food prices are moderating which bode well for domestic food prices. In addition, a normal monsoon will ensure ample production and thus lower food inflation.

Within core, only housing and health indices were reported. Housing inflation moderated to 3.7% from 3.9% in Apr'20. However, health index rose sharply by 150bps to 4.3% against 2.8% in Apr'20. Lower demand should drive core inflation lower, though labour availability is a challenge.

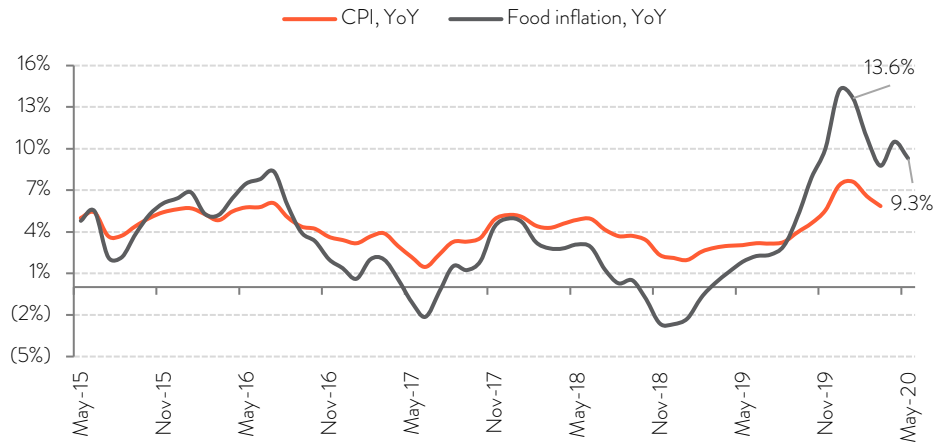
Policy space remains: The sharp decline in industrial production shows growth challenges will require fiscal and monetary policy intervention. While RBI has reduced policy rate by 115bps, we believe there is room for another 25bps rate cut as moderating food inflation shows inflation will be below RBI's target in H2FY21.

KEY HIGHLIGHTS

- Food inflation eases to 9.3% in May'20 from 10.5% in Apr'20.
- Health inflation rises, housing moderates.
- IIP growth plummets by 55.5% in Apr'20, led by manufacturing.

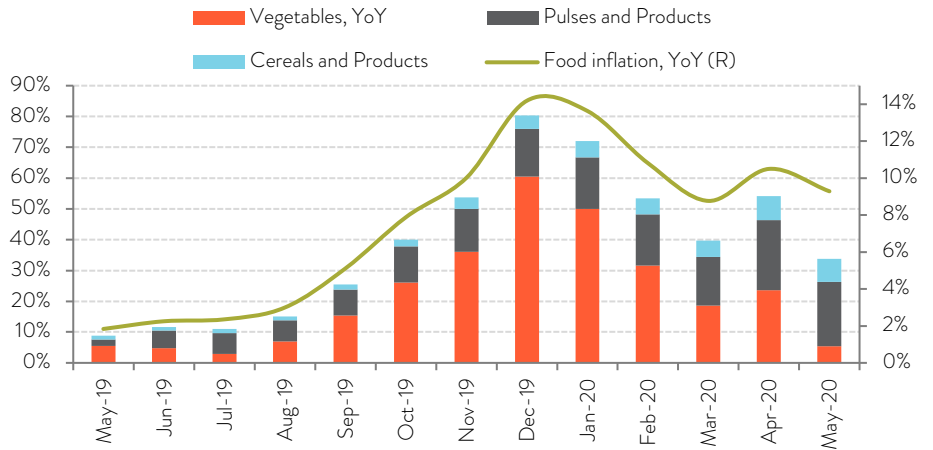


FIG 1 – FOOD INFLATION FELL BY 120BPS TO 9.3% IN MAY'20



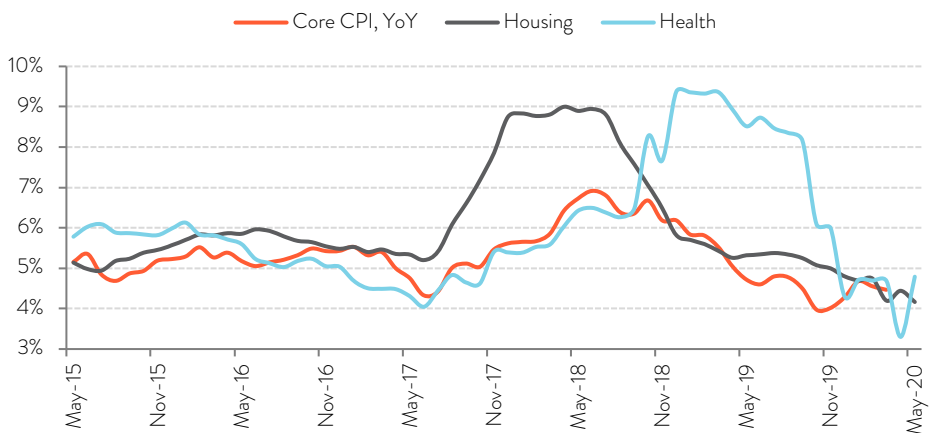
Source: CEIC, Bank of Baroda Research

FIG 2 – ...LED BY FALL IN VEGETABLE PRICES



Source: CEIC, Bank of Baroda Research

FIG 3 – HEALTH INFLATION INCHES UP; HOUSING MODERATES



Source: CEIC, Bank of Baroda Research

FIG 4 – IIP GROWTH SHRINKS FURTHER

Sectoral (%)	Weight	Apr-20	Mar-20	Apr-19
IIP	100.0	(55.5)	(18.3)	3.2
Mining	14.4	(27.4)	(1.4)	5.1
Manufacturing	77.6	(64.3)	(22.4)	2.5
Electricity	8.0	(22.6)	(8.2)	6.0
Use-Based				
Primary Goods	34.1	(26.6)	(4.1)	5.1
Capital Goods	8.2	(92.0)	(38.3)	(1.4)
Intermediate Goods	17.2	(66.0)	(18.5)	3.0
Infrastructure and Construction Goods	12.3	(83.9)	(25.2)	(0.7)
Consumer Durables Goods	12.8	(95.7)	(36.5)	2.2
Consumer Non-Durables Goods	15.3	(36.1)	(20.2)	5.4

Source: CEIC, Bank of Baroda Research

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For further details about this publication, please contact:

Economics Research Department

Bank of Baroda

+91 22 6698 5713

chief.economist@bankofbaroda.com