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CPI above RBI's upper band

Discomfort again appeared from an elevated CPI print in Jan'23. We were also expecting an above 6% print. What poses concern is the dissemination of price pressure in majority food items. Now it is not limited to vegetable inflation, but 6 out of 12 broad group of food and beverage items noticed inflation above 6%. Even in Feb'23, price pressure exists for majority of vegetables such as garlic, ginger, potato and tomato which constitute major share of the vegetable basket. Excl. the volatile component of CPI as well, it remains well above RBI's 6% target. Core also poses considerable risk from higher gold prices and rising housing inflation. Going forward stickiness in core would persist from higher discretionary spending and pass through of input costs to output prices which is yet to materialize. We expect CPI to average around 6.5% in FY23 and 5.7% in FY24. RBI would be highly cautious of this discomforting print and be in a wait and watch mode till Q4FY23. Any large deviation from its forecast will be viewed with caution.

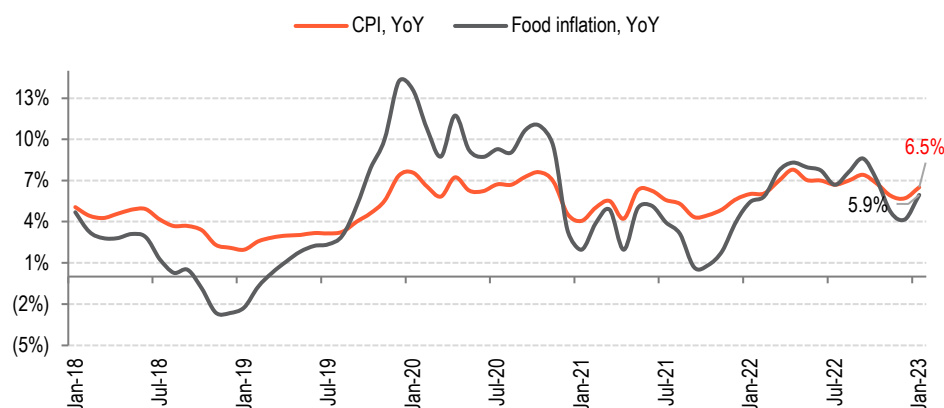
CPI inflation inched up

CPI inflation edged up: CPI inflation data again posed concern as it edged up to 6.5% in Jan'23, after dropping to a 13-month low of 5.7% in Dec'22. This is despite a favourable base of 6% seen in Jan'22. Food inflation noted considerable uptick; a jump of around 180bps. Stickiness of core (inflation excl. food and fuel) continued to persist.

Food inflation poses upside risk: CPI food index rose to 5.9% in Jan'23 from 4.2% in Dec'22, on YoY basis. Amongst major food items, sharpest pace of increase was led by vegetable prices where pace of disinflation went down from -15.1% in Dec'22 to -11.7% in Jan'23. Other than this, cereals and product also rose to 16.1% from 13.8% in Dec'22. Egg inflation also rose to 8.8% from 6.9%. Even inflation in meat and fish category also rose to 6% from 5.1% in Dec'23. Notably, 6 out of 12 broad group of food and beverage noticed inflation above 6%, with double digit inflation being noticed in cereal and spices category.

On MoM basis, vegetables (-3.8% from -12.7% in Dec'22), fruits (0.1% from -1.7% in Dec'22), cereal (2.6% in Jan'23 from 1.1% in Dec'22) and meat and fish (0.8% from -0.2% in Dec'22) items pose considerable risk. The pickup in momentum of vegetable prices has resulted from items such as ginger, garlic, chilly, brinjal and cabbage. Rise in wheat prices (as per Department of Consumer Affairs data) have exhibited considerable risk on cereal inflation. Going forward, the risk of adverse weather might weigh on cereal prices and the outlook on food inflation still remains uncertain.

Figure 1: CPI inflation rose to 6.5% led by food

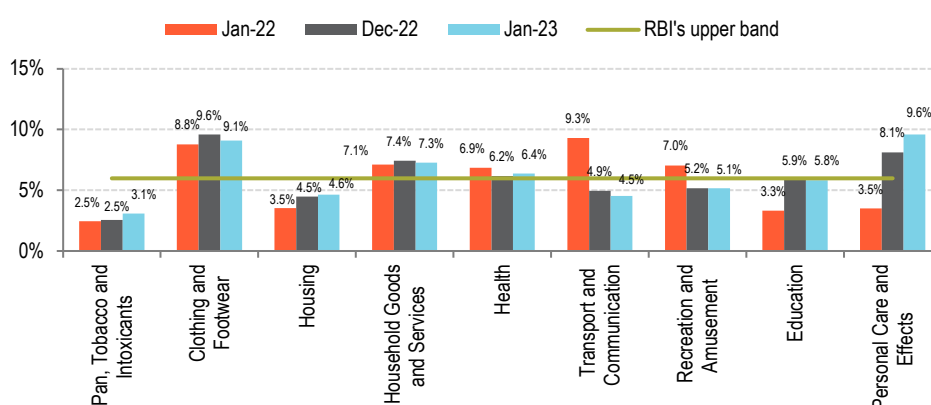


Source: CEIC, Bank of Baroda Research

Core CPI (excl. food and fuel) remained sticky at 6.1% in Jan'23 as well. Excl. Pan and tobacco, the print of core inflation further goes up to 6.3% in Jan'23 from 6.2% in Feb'22. Amongst major items of core, housing inflation rose to 4.6% in Jan'23 from 4.5% in Jan'22. Health inflation rose to 6.4% from 6.2% in Dec'22. Rising gold prices have contributed to personal care and effect inflation to go upto 9.6% from 8.1% in Dec'22. However, transport and communication, clothing and footwear have given slight comfort with regard to moderation in inflation. Amongst the 8 major broad group of core inflation, 4 of the items have remained above 6%.

On a sequential basis, housing inflation went up to 0.8% from -0.6% in Dec'22. Other than that recreation and amusement (0.4% from 0.2% in Dec'22) and personal care and effects (1.6% from 1.3% in Dec'22, following a 5.8% MoM increase in international gold prices) pose considerable risks.

Figure 2: Core inflation remains sticky:



Source: CEIC, Bank of Baroda Research

Fuel inflation: It moderated to 10.8% in Jan'23 from 10.9% in Dec'22, on account of fall in Kerosene prices and flat LPG prices. On sequential basis as well, fuel inflation moderated to 0% from 0.4% in Dec'22.

CPI excl. volatile items: CPI excl. vegetables which have been the major driver of inflation has also been considerably higher at 7.7% in Jan'23 from 7.3% in Dec'22, on YoY basis. Consumer food price Index excluding vegetables have also remained elevated at 9%, which also shows considerable price pressure have been from other food items as well, which needs to be monitored carefully.

Inflationary pressures to persist

- CPI print came in line with our expectations. Some upward momentum in vegetable prices is still visible in Feb'23 especially for heavy weighted consumption items such as ginger, garlic, potato and tomato. Apart from this, higher commodity prices from better demand outlook of China and considerable soft landing for economies such as Germany, UK, might put further pressure on commodity prices in the near term.
- The domestic macros also indicate resilient economic activity in Feb'23 as visible from rail freight, air passenger traffic and toll collection data. Discretionary spending is also picking pace, which is expected to keep core inflation under pressure.
- Going forward, we expect the pressure on inflation would continue. We expect CPI to average around 6.5% in FY23 (in line with RBI's projection), for FY24, we expect it to be at 5.7% higher than RBI's forecast of 5.3%. This month and print of the current quarter hold relevance since RBI would be watchful of the persistence in core and volatility in food inflation to take a call on rates. For now we remain with our earlier forecast of pause in the near to medium term.

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