

INFLATION

14 June 2021

CPI springs a negative surprise

CPI surprised negatively to 6.3% in May'21 led by higher food and core inflation. While food inflation increased to 5% (2% in Apr'21), core inflation went up to 6.6% (5.4% in Apr'21). The increase was broad based and likely to persist with pass-through of commodity, oil and precious metal prices. We now expect CPI inflation to average 5.5% in FY22 led by higher core inflation at 6.2%. While MPC is likely to focus on growth over inflation in the near-term, medium term policy normalisation will also be on the discussion agenda.

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CPI overshoots: CPI inflation surprised negatively and rose to a 6-month high of 6.3% in May'21 (consensus estimate of 5.4%). At the same time, Apr'21 CPI inflation has been revised to 4.2% (earlier 4.3%).

Food inflation accelerates: Food inflation rose to 5% in May'21 from 2% in Apr'21. This was led by oils and fat (30.8% from 25.9%), eggs (15.2% from 10.6%), fruits (12% from 9.7%), and pulses (9.4% from 7.5%). Vegetable prices fell by -1.9% (-14.5% in Apr'21), sugar by -1.4% (-6%) and cereal by -1.4% (-3%). However, rate of price increase in meat and fish moderated to 9% (16.7%). While vegetable and cereal inflation is likely to remain moderate, edible oils, pulses, egg and meat and fish will remain elevated.

Core inflation firms up: CPI excluding food and fuel rose by 120bps to 6.6% in May'21 from 5.4% in Apr'21. The increase was broad based led by 260bps jump in personal care and effects (8% from 5.4%), 190bps jump in household goods and services (3.9% from 1.9%), 180bps jump in recreation and amusement (6.3% from 4.6%), 180bps jump in clothing and footwear (5.3% from 3.5%) and 160bps jump in transport and communication (12.4% from 10.8%). Despite weak demand, the broad based increase points to pass-through of higher commodity, oil and precious metal prices into consumer inflation.

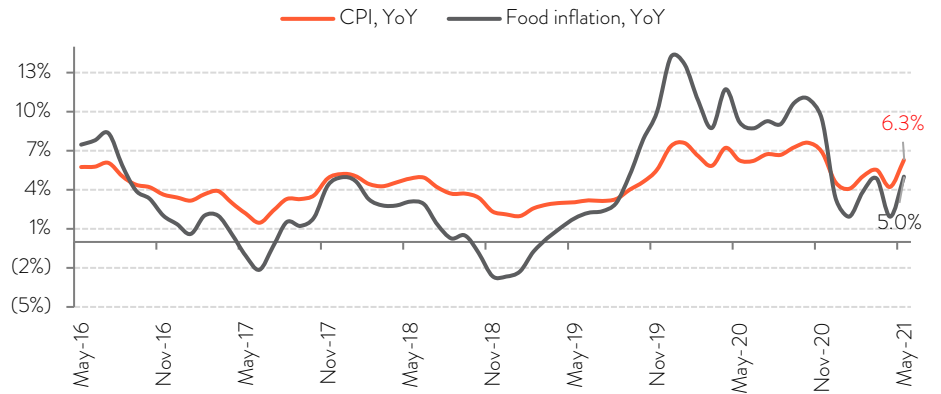
CPI Inflation now estimated at 5.5%: We now expect CPI to overshoot RBI's estimate of 5.1% in FY22. This will be largely driven by higher core inflation (already at 6.6%) and likely to average 6.2% in FY22. Fuel and light inflation will also be on higher side. Food inflation will be relatively lower at less than 5%. While MPC will continue to focus on growth, an upward revision in inflation trajectory implies discussion on accommodative policy exit will also be on the table. Risk to our estimates is from cut in excise duties on petroleum products.

KEY HIGHLIGHTS

- CPI rose to a 6-month high of 6.3% in May'21 from 4.2% in Apr'21.
- Food inflation rose to 5% from 2% in Apr'21, core increased to 6.6% from 5.4% in Apr'21.
- Revised our forecast for FY22 CPI to 5.5% led by core elevated at 6.2%.

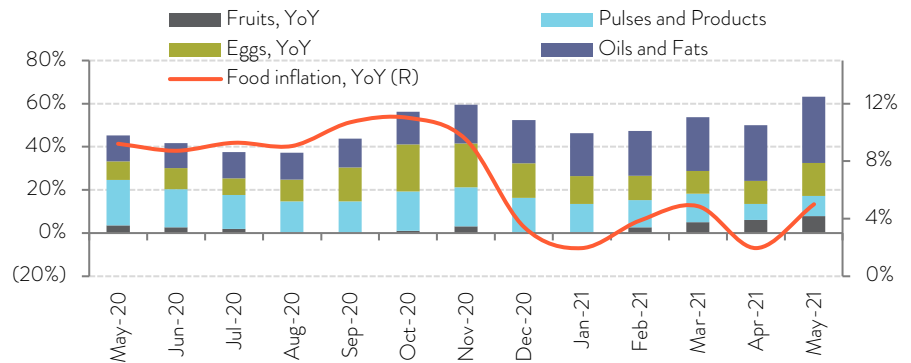


FIG 1 – CPI SHOT UPTO 6.3% IN MAY'21, LED BY FOOD AND CORE



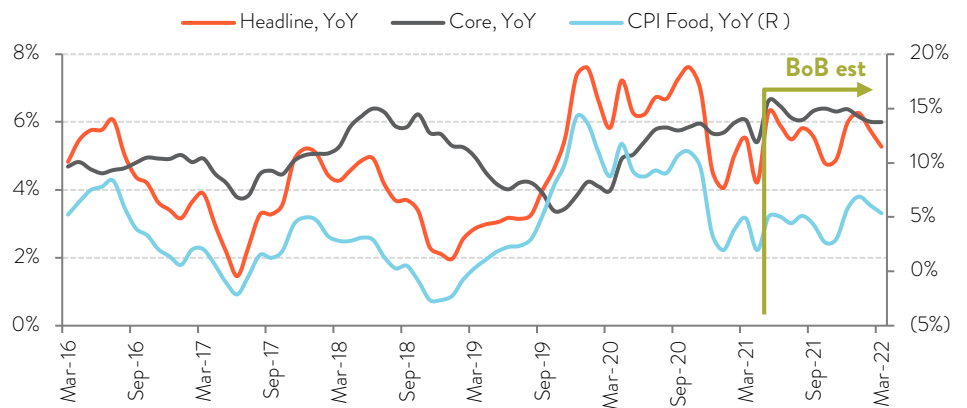
Source: CEIC, Bank of Baroda Research

FIG 2 – PULSES, OIL AND FATS, FRUITS AND EGG REMAIN ELEVATED



Source: CEIC, Bank of Baroda Research

FIG 3 – CPI TO REMAIN ELEVATED AT 5.5% IN FY22



Source: CEIC, Bank of Baroda Research

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