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CPI cools, IIP growth falters

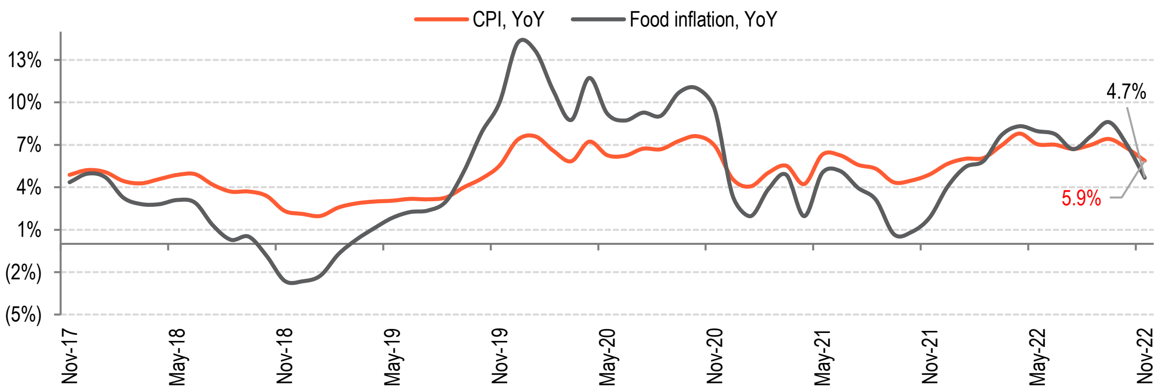
India's headline inflation cooled off to an 11-month low of 5.9% in Nov'22 from 6.8% in Oct'22. This can be attributed to a sharp fall in vegetable prices as well as moderation in prices of fruits. Core inflation edged up marginally to 6% from 5.9%. We expect CPI inflation to inch upwards as the base effect wanes. Further, with a likely slowdown in the economy, core inflation too will remain stable though the pressure to pass on higher input cost will remain. Recent indicators too point towards a slowdown in demand. Notably, IIP growth plunged sharply by 4% in Oct'22 led by a sharp decline in manufacturing output. Output for both consumer durables and non-durables declined sharply. Given this backdrop and the fact that inflation will probably go below 6% in march, we expect that the RBI is likely to draw the curtains on its rate hike cycle with a 25bps rate hike in Feb'23, bringing the terminal repo rate to 6.5%.

CPI inflation moderates

CPI inflation eased:

CPI inflation eased much more than expected to 5.9% in Nov'22 (12-month low), (our estimate 6%) from 6.8% in Oct'22. This is the first time in FY23 that inflation was below RBI's upper threshold of 6%. Food inflation moderated to an 11-month low at 4.7% in Nov'22 compared with 7% in Oct'22. This can almost entirely be explained by a decline in vegetable inflation (decline of 8.1% in Nov'22 compared with an increase of 7.8% in Oct'22), due to seasonal factors. Some moderation was also visible in fruits (2.6% versus 5.2% in Oct'22). Other items in the food basket however continued to show underlying price pressures. Cereals inflation inched up by 13% to its highest since Sep'13, from an already elevated level of 12.1%. Prices of eggs which had been declining since Apr'22, inched up sharply by 4.9% in Nov'22. Other commodities such as meat and fish and milk and milk products showed upward momentum. Fuel and light inflation inched up sharply to 10.6% in Nov'22 from 9.9% in Oct'22. This is even though global oil prices are now below US$ 80/bbl, as prices have not been lowered at the consumer end.

Figure 1: CPI cools down; led by food

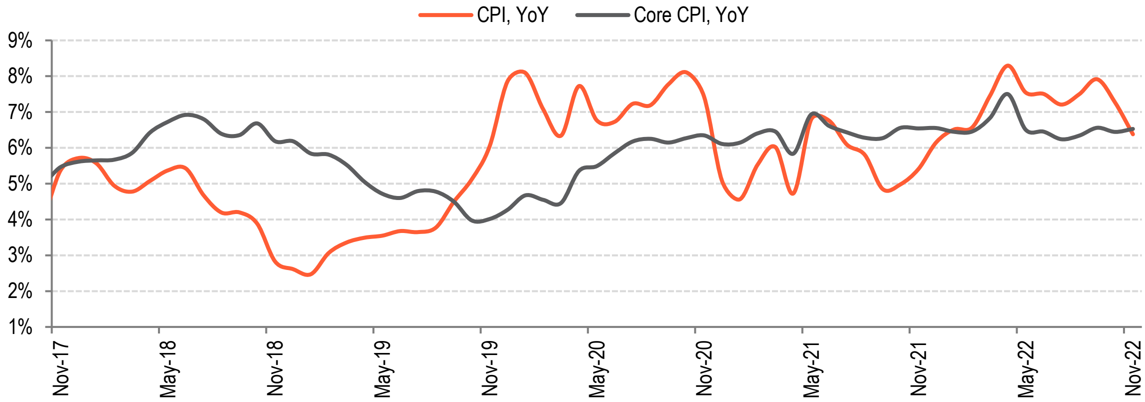


Source: CEIC, Bank of Baroda Research

Core inflation inches up:

Core CPI (excl. food and fuel) edged up to 6% in Nov'22 from 5.9% in Oct'22. Barring amusement and recreation, clothing and footwear and housing, all other components of core inflation showed acceleration. Maximum traction was seen in transport and communication (5.3% in Nov'22 from 4.6% in Oct'22) and pan, tobacco and intoxicants (2% versus 1.9% in Oct'22). High prices may have deterred consumption of amusement and recreation services by individuals. Inflation in this category eased to 5.4% in Nov'22 from 6.1% in Oct'22.

Figure 2: Core CPI edges up



Source: CEIC, Bank of Baroda Research

Inflationary pressures to come down?

Inflation print for Nov'22 comes as a welcome relief as CPI inflation eased much more than estimates and fell below the RBI's upper tolerance band for the first time this year. The decline was led by lower food inflation, which in turn can be attributed to lower prices of fruits and vegetables. However, other items in the food basket continue to show upward traction, most notably, cereal inflation continues to scale higher and needs to be monitored closely. We expect inflation to remain above 6% for the next couple of months as the process of passing on higher input cost is on. Further lower crude oil prices is not translating to lower retail prices.

RBI had sounded a word of caution while slowing down the pace of rate hike in its Dec'22 meeting. RBI may wait to see the trajectory for the next couple of months before taking a call on rates. We expect another 25bps rate hike by RBI in Feb'23 which will take the repo rate to 6.5%, where it is likely to stay for some time.

IIP growth dips:

IIP growth fell by 4% in Oct'22 compared with an increase of 3.5% in Sep'22. This was a much sharper fall than both consensus (estimated 1% decline) and our estimates (increase of 0.5%) and also marked the biggest pace of decline in industrial output since Aug'20. This was led by a sharp decline in manufacturing output which fell by 5.6% in Oct'22 versus 2.2% increase in Sep'22. Out of the 23 sub-groups within manufacturing, output in 19 industries declined. Within this, output of wearing apparel (37.1%), electrical equipment (33.2%), leather (24.3%) and pharma products (21.4%) declined the most. Electricity output too moderated markedly to 1.2% in Oct'22 versus 11.6% in Sep'22. Even mining output decelerated to 2.5% from 5.2% in Sep'22. Compared with the levels seen in 2019 (pre-pandemic period), IIP growth was up by 4.5% in Oct'22 versus 9% in Sep'22.

Broad-based slowdown:

Within use-based, output of both consumer durables (15.3%) and non-durables (13.4%) registered double-digit decline. Further, while capital goods output declined by 2.3% (from 11.4% in Sep'22), even intermediate goods output was 2.8% lower. Sharp slowdown was also visible in the output of primary goods (2% in Oct'22 versus 9.5% in Sep'22) and infrastructure and construction goods (1% versus 7.7% in Sep'22).

Table 1: IIP growth moderates

Sectoral (%)	Weight	Oct-22	Sep-22	Oct-21	Apr-Oct'22	Apr-Oct'21
IIP	100.0	(4.0)	3.5	4.2	5.3	20.5
Mining	14.4	2.5	5.2	11.5	4.0	20.4
Manufacturing	77.6	(5.6)	2.2	3.3	5.0	21.8
Electricity	8.0	1.2	11.6	3.1	9.4	11.4
Use-Based						
Primary Goods	34.1	2.0	9.5	9.0	8.2	14.7
Capital Goods	8.2	(2.3)	11.4	(1.6)	14.0	35.4
Intermediate Goods	17.2	(2.8)	1.7	4.6	5.3	28.0
Infrastructure and Construction Goods	12.3	1.0	7.7	6.6	6.5	32.0
Consumer Durables Goods	12.8	(15.3)	(3.2)	(3.2)	6.6	30.4
Consumer Non-Durables Goods	15.3	(13.4)	(6.3)	0.7	(4.2)	7.2

Source: CEIC, Bank of Baroda Research

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