13 January 2024

EcoScope
The Economy Observer

Inflation inches up but lower than expected; industrial output remains muted

Prospects of interest rate cuts still far away

- **Headline CPI inflation came in at 5.7% YoY in Dec'23 vs. 5.6% in Nov'23, mainly led by 48-month low core inflation at 3.8% (vs. 4.1% in Nov'23). It was partly offset by higher food inflation at 9.5% in Dec'23 vs. 8.7% in Nov'23 (Exhibit 1). The number was lower than the Bloomberg consensus of 5.9% and our forecast of 6.3% as inflation in core components and vegetables came in lower than our expectations. CPI inflation averaged 5.4% in 3QFY24, which is lower than the RBI expectations of 5.6%.**
- **Food inflation came in at 9.5% YoY in Dec'23 vs. 8.7% in Nov'23 and 4.2% in Dec'22. It decreased 0.9% MoM in Dec'23. Details suggest that the acceleration in food inflation was mainly due to vegetable prices (weight = 6%), which rose 27.6% YoY, following a 17.7% YoY increase in Nov'23. CPI ex-veggies slid to a 48-month low of 4.4% YoY (lowest since Dec'19) from 4.7% last month. At the same time, inflation in cereals, pulses, and spices remained sticky in double digits.**
- **Notably, core CPI (excluding food & beverages and fuel & light) came down to 3.8% in Dec'23 from 4.1% in Nov'23, the lowest in almost 48 months. The deceleration was broad-based.**
- **Other details suggest that: (1) Goods inflation remained firm at 6.4% in Dec'23 (6.2% in Nov'23), while services inflation came in at 3.4% (vs. 3.5% in Dec'23), lowest since 2015. Core services inflation slid to 3.3%, the lowest since 2015 (Exhibit 3). (2) Details of 299 items suggest that 64% of the basket posted less than 5% inflation in Dec'23 (vs. 58% in Nov'23), the highest since Feb'20 (Exhibit 4). (3) Prices of imported items declined further by 2.1% YoY in Dec'23 (vs. -1.7% in Nov'23), while domestically generated inflation increased to 6.9% YoY in Dec'23 vs. 6.6% in Nov'23, the highest in four months.**
- **IIP decelerated to a 13-month low of 2.4% YoY in Nov'23 (vs. 11.6% in Oct'23, revised lower from 11.7%). The deceleration in growth was mainly led by a high base (7.6% in Nov'22) and fewer working days in Nov'23 due to Diwali holidays. The number is lower than the Bloomberg consensus of 4% and our forecast of 4.9%. During Apr-Nov'23, industrial output grew 6.5%.**
- **Growth in manufacturing activity decelerated to 1.2% in Nov'23 vs. 10.2% in Oct'23 and 6.7% in Nov'22. Lower growth in manufacturing output was mainly due to lower factory activity in Nov'23 during Diwali holidays. Details of the manufacturing sector confirm that as much as 80.6% of the items within the sector grew at a lower rare than last year (vs. 1% in Oct'23) and 55.3% of the items posted a contraction (vs. 4.1% growth in Oct'23).**
- **According to the use-based classification, output of capital goods and infra & construction goods contracted in Nov'23. Capital goods output contracted by 1.1% in Nov'23 (worst in 13 months) vs. 21.3% growth in Oct'23 and 20.7% in Nov'22. Growth in infra & construction goods decelerated to 1.5% in Nov'23 vs. 11.3% in Oct'23 and 14.3% in Nov'22. Consumer goods contracted by 4.3% in Nov'23 vs. a growth of 11.7% in Oct'23 and 8.1% in Nov'22.**
- **Overall, inflation came in much better than expected; however, industrial output growth remained weak. With the Dec'23 print at 5.7%, CPI averaged 5.4% in 3QFY24, lower than the RBI forecast of 5.6%. Though the inflation number is better than expected, we believe that the prospects of rate cuts are still far away. Going forward, we expect moderation in 3QFY24 real GDP growth and expect inflation to remain at ~5.8% YoY in 4QFY24. Poor rabi sowing and deteriorating reservoir levels are upside risks to the food inflation trajectory and need to be monitored.**

- **CPI inflation at 5.7% in Dec'23, much lower than market expectations:** Headline CPI inflation came in at 5.7% YoY in Dec'23 vs. 5.6% in Nov'23, mainly led by 48-month low core inflation at 3.8% (vs. 4.1% in Nov'23). It was partly offset by a higher food inflation at 9.5% in Dec'23 vs. 8.7% in Nov'23 (Exhibit 1). The number was lower than the Bloomberg consensus of 5.9% and our forecast of 6.3% as inflation in core components and vegetables came in lower than our expectations. CPI inflation averaged 5.4% in 3QFY24, which is lower than the RBI expectations of 5.6%.
- **Food inflation at 9.5% in Dec'23:** Food inflation came in at 9.5% YoY in Dec'23 vs. 8.7% in Nov'23 and 4.2% in Dec'22. It decreased 0.9% MoM in Dec'23. Details suggest that the acceleration in food inflation was mainly due to vegetable

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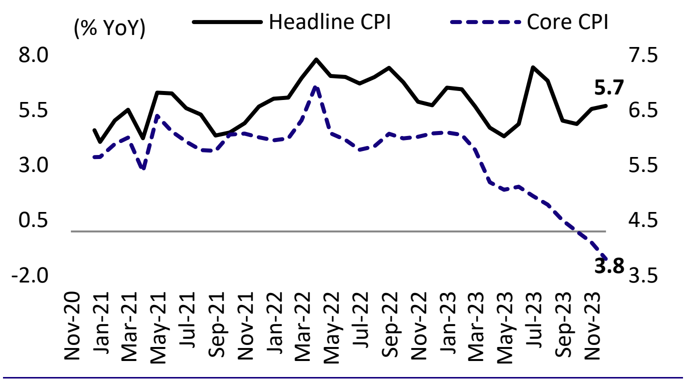
prices (weight = 6%), which rose 27.6% YoY, following a 17.7% YoY increase in Nov’23. CPI ex-veggies slid to a 48-month low of 4.4% YoY (lowest since Dec’19) from 4.7% last month. At the same time, inflation in cereals, pulses, and spices remained sticky in double digits. Inflation in pulses increased to 20.7% in Dec’23 (0.5% MoM) vs. 20.3% last month, led by lower rabi sowing and below-normal rainfall in pulses-growing states. Inflation in protein-based products came down in Dec’23. The prices of fuel and light items contracted 1% YoY in Dec’23, lowest since Nov’19. Standard core CPI came in at a 42-month low of 4.0% in Dec’23 vs. 4.2% in Nov’23. *(Exhibit 2)*

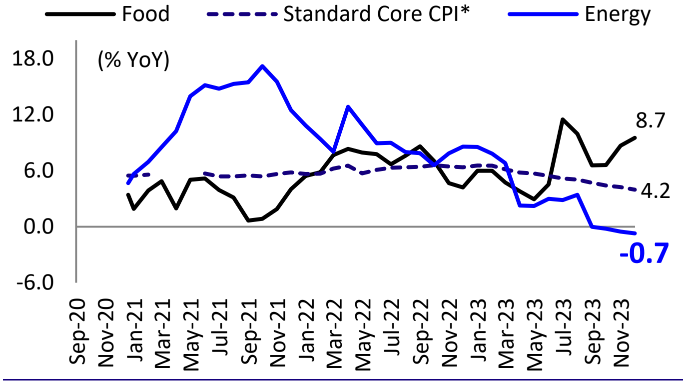
- **Core inflation at a 48-month low in Dec’23:** Core CPI (excluding food & beverages and fuel & light) came down to 3.8% in Dec’23 from 4.1% in Nov’23, the lowest in almost 48 months. The deceleration was broad-based.
- **Other details suggest that:** (1) Goods inflation remained firm at 6.4% in Dec’23 (6.2% in Nov’23), while services inflation came in at 3.4% (vs. 3.5% in Dec’23), the lowest since 2015. Core services inflation slid to 3.3%, the lowest in record since 2015 *(Exhibit 3)*. (2) Details of 299 items suggest that 64% of the basket posted less than 5% inflation in Dec’23 (vs. 58% in Nov’23), the highest since Feb’20 *(Exhibit 4)*. (3) Prices of imported items declined further by 2.1% YoY in Dec’23 (vs. -1.7% in Nov’23), while domestically generated inflation increased to 6.9% YoY in Dec’23 from 6.6% in Nov’23, the highest in four months.
- **Our view:** Overall, inflation came in much better than expected; however, industrial output growth remained weak. With the Dec’23 print at 5.7%, CPI averaged 5.4% in 3QFY24, lower than the RBI forecast of 5.6%. Though the inflation number is better than expected, we believe that the prospects of rate cuts are still far away. Going forward, we expect moderation in 3QFY24 real GDP growth and expect inflation to remain at ~5.8% YoY in 4QFY24. Poor rabi sowing and deteriorating reservoir levels are upside risks to the food inflation trajectory and need to be monitored.

Exhibit 1: Retail inflation at 5.7% in Dec’23 vs. 5.6% in Nov’23…



Core CPI excludes food & beverages and fuel & light

Exhibit 2: …led by higher food inflation



* Excluding food & energy

Exhibit 3: Services inflation at 3.4% in Dec'23, lowest since 2015

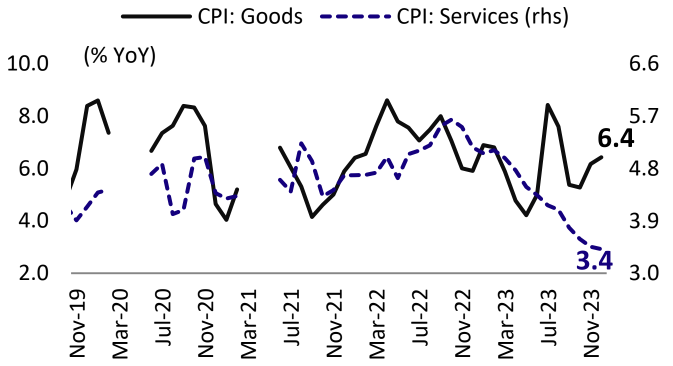
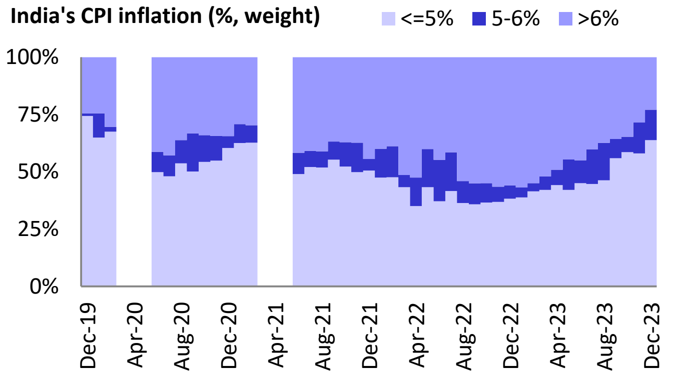


Exhibit 4: 64% of CPI basket posted less than 5% inflation in Dec'23 vs. 58% in Nov'23



Based on 299 items

Exhibit 5: CPI and key components

	FY21	FY22	FY23	Dec-22	Oct-23	Nov-23	Dec-23
Overall CPI	6.2	5.5	6.7	5.7	4.9	5.6	5.7
Food and beverages	7.3	4.2	6.7	4.6	6.3	8.0	8.7
Cereal and products	3.8	0.5	11.0	13.8	10.7	10.3	9.9
Pulses and products	16.4	6.0	2.4	3.9	18.8	20.3	20.7
Meat and fish	15.4	7.9	4.2	5.1	3.3	2.2	1.1
Milk and products	5.4	2.8	7.4	8.6	6.4	5.7	5.1
Vegetables	5.8	-7.2	3.0	-15.1	2.8	17.7	27.6
Pan, tobacco, and intoxicants	9.9	4.5	2.2	2.5	3.9	3.8	3.6
Fuel and light	2.7	11.3	10.3	10.9	-0.4	-0.8	-1.0
Housing	3.3	3.7	4.3	4.5	3.8	3.6	3.6
Clothing and footwear	3.4	7.2	9.5	9.6	4.3	3.9	3.6
Miscellaneous	6.6	6.7	6.3	6.2	4.5	4.4	4.1
Transport and communication	9.9	10.1	5.9	4.9	2.0	2.1	2.0
Core CPI	5.6	6.0	6.1	6.1	4.3	4.1	3.8

*Excluding food & beverages and fuel & light

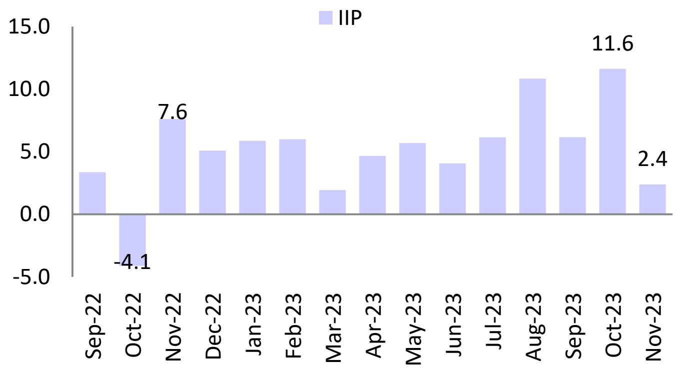
Source: Central Statistics Office (CSO), MOFSL

IIP growth declined to 2.4% in Nov'23

- **IIP growth decelerated to 13-month low:** IIP decelerated to a 13-month low of 2.4% YoY in Nov'23 (vs. 11.6% in Oct'23, revised lower from 11.7%). The deceleration in growth was mainly led by a high base (7.6% in Nov'22) and fewer working days in Nov'23 due to Diwali holidays. The number is lower than the Bloomberg consensus of 4% and our forecast of 4.9%. During Apr-Nov'23, industrial output grew 6.5%. *(Exhibit 1)*
- **Driven mainly by manufacturing:** Growth in manufacturing activity decelerated to 1.2% in Nov'23 vs. 10.2% growth in Oct'23 and 6.7% in Nov'22. Lower growth in manufacturing output was mainly due to lower factory activity in Nov'23 due to Diwali holidays. Details of the manufacturing sector confirm that as much as 80.6% of the items within the sector grew at a slower rate than last year (vs. 1% in Oct'23) and 55.3% of items posted a contraction (4.1% in Oct'23). *(Exhibit 4)*
- Electricity output grew 5.8% in Nov'23 vs. a growth of 20.4% in Oct'23 and 12.7% in Nov'22. Mining output grew 6.8% in Nov'23 (lowest in 5 months) vs. 13.1% in Oct'23 and 9.7% in Nov'22. *(Exhibit 2)*
- **Infra & construction goods and capital goods remained weak:** According to the use-based classification, output of capital goods and infra & construction goods

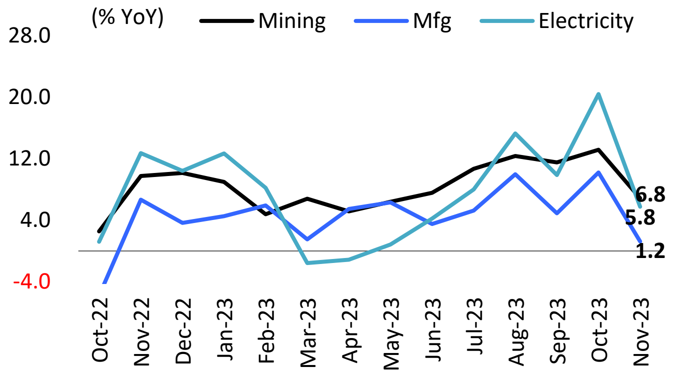
contracted in Nov'23. Capital goods output contracted by 1.1% in Nov'23 (worst in 13 months) vs. 21.3% growth in Oct'23 and 20.7% in Nov'22. Infra & construction goods growth decelerated to 1.5% in Nov'23 vs. 11.3% in Oct'23 and 14.3% in Nov'22. Consumer goods contracted by 4.3% in Nov'23 vs. a growth of 11.7% in Oct'23 and 8.1% in Nov'22. *(Exhibit 3)*

Exhibit 6: IIP growth decelerated to 2.4% YoY in Nov'23…



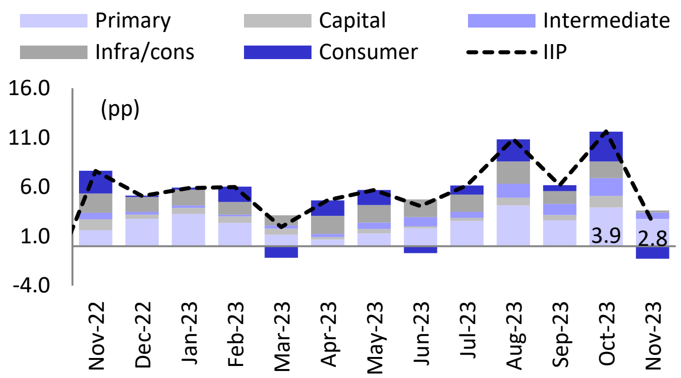
Source: CSO, MOFSL

Exhibit 7: …led by manufacturing



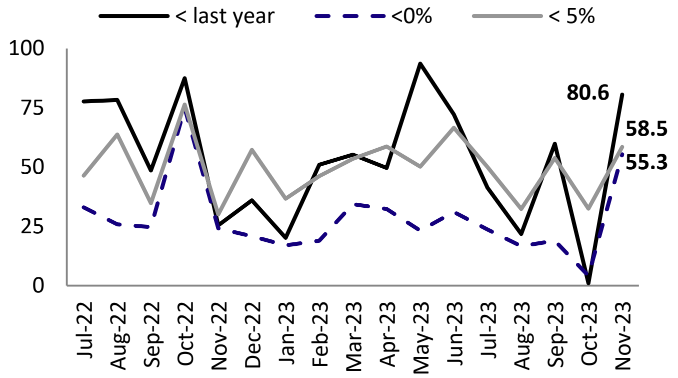
Source: CSO, MOFSL

Exhibit 8: Infra & construction goods and capital goods remained weak



Source: CSO, MOFSL

Exhibit 9: 58.5% of the manufacturing basket grew slower than 5% vs. 32.5% in Oct'23



Source: CSO, MOFSL

Exhibit 10: Key components of IIP

% YoY	Weight	FY20	FY21	FY22	FY23	Nov-22	Sep-23	Oct-23	Nov-23
Industry-based classification									
Mining	14.4	1.6	(7.8)	12.2	5.8	9.7	11.5	13.1	6.8
Manufacturing	77.6	(1.4)	(9.6)	11.7	4.7	6.7	4.9	10.2	1.2
Electricity	8.0	0.9	(0.5)	8.0	8.9	12.7	9.9	20.4	5.8
IIP	**100.0**	(0.8)	(8.5)	11.4	5.3	7.6	6.2	11.6	2.4
Use-based classification									
Primary Goods	34.0	0.7	(7.0)	9.6	7.5	4.8	8.0	11.4	8.4
Capital Goods	8.2	(14.0)	(18.7)	17.0	13.0	20.7	8.4	21.3	(1.1)
Intermediate Goods	17.2	9.1	(9.4)	15.4	3.8	3.5	6.1	9.4	3.5
Infrastructure/Construction	12.3	(3.6)	(8.7)	18.8	8.4	14.3	8.9	11.3	1.5
Consumer Goods	28.2	(3.8)	(7.3)	6.6	0.6	8.1	2.2	11.7	(4.2)
Durable Goods	12.8	(8.8)	(14.9)	12.4	0.6	5.0	1.1	15.9	(5.4)
Non-Durable Goods	15.3	(0.1)	(2.1)	3.2	0.7	10.0	3.0	8.7	(3.6)

Source: CSO, MOFSL

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