

## INFLATION AND IIP

12 March 2020

### Inflation falls, growth rebounds

**CPI inflation edged down to 6.6% in Feb'20 (7.6% in Jan'20) led by moderation in prices of vegetables and fruits. Core also fell by 10bps to 4.1% due to fall in retail fuel prices. While industrial output rebounded to 2% in Jan'20, we expect domestic economic activity to decelerate on the back of supply and demand disruption from advisories and travel restrictions because of COVID-19. The current growth-inflation mix calls for 25-40bps cut in policy rate as demonstrated by large central banks in the last few weeks.**

Sameer Narang

Dipanwita Mazumdar | Jahnavi

chief.economist@bankofbaroda.com

**IIP growth rebounds:** Industrial output rose to a 6-month high of 2% in Jan'20 from 0.1% in Dec'19. This was led by improvement in both manufacturing at 1.5% (-0.7% in Dec'19) and electricity at 3.1% (-0.1% in Dec'19). Within manufacturing, intermediate goods continue to grow in double digits at 15.8% in Jan'20 compared with 12.5% in Dec'19. Primary goods output moderated to 1.8% in Jan'20 (vs 2.2% in Dec'19). On the other hand, pace of decline slowed significantly for capital goods (-4.3% vs -18.2% in Dec'19) and consumer non-durable goods (-0.3% vs -3.7% in Dec'19). Within FMCG, manufacture of tobacco products was the biggest contributor to the growth rising by 22.8%.

**CPI inflation moderated to 6.6%:** CPI inflation edged down by 100bps to 6.6% in Feb'20 from 7.6% in Jan'20. This was led by 280bps drop in food inflation (10.8% in Feb'20 compared with 13.6% in Jan'20). Vegetable prices fell sharply to 31.6% in Feb'20 compared with 50.2% in Jan'20. Fruits, eggs, meat and fish and sugar showed softening in inflation in Feb'20. Outlook for food inflation is favourable with improved Rabi sowing and further dip in vegetable prices in Mar'20. In addition, dip in global food prices will be a tailwind for muted domestic food prices as well.

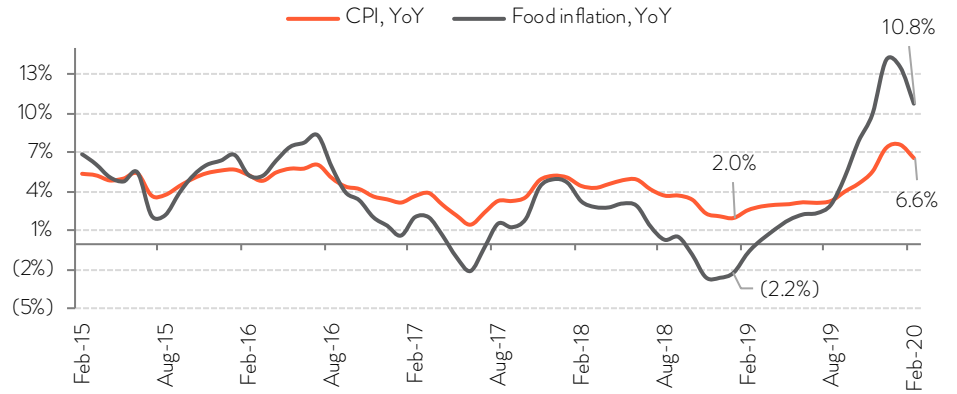
**Core inflation edged down:** Core inflation fell by 10bps to 4.1% in Feb'20 compared with 4.2% in Jan'20. This was led by 100bps fall in transport and communication inflation (5.2% in Feb'20 compared with 6.2% in Jan'20), because of transmission of 13% fall in crude prices in Feb'20. Inflation in personal care items also moderated by 20bps to 6.9% in Feb'20. We expect core inflation to moderate in the coming months as 1) as oil prices have fallen further by (-) 29% in Mar'20 and 2) domestic demand remains weak and COVID-19 will hit domestic demand further—particularly services. In our opinion, this gives RBI room to reduce rates by 25-40bps in Apr'20.

#### KEY HIGHLIGHTS

- CPI moderates to 6.6% in Feb'20 versus 7.6% in Jan'20.
- Core inflation edged down by 10bps to 4.1%.
- IIP growth rebounds by 2% in Jan'20, led by manufacturing.

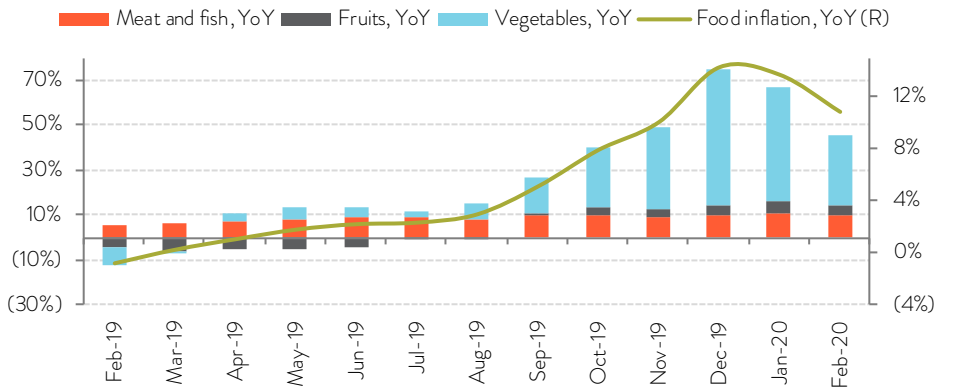


**FIG 1 – CPI FELL BY 100BPS TO 6.6% IN FEB'20 VS 7.6% IN JAN'20**



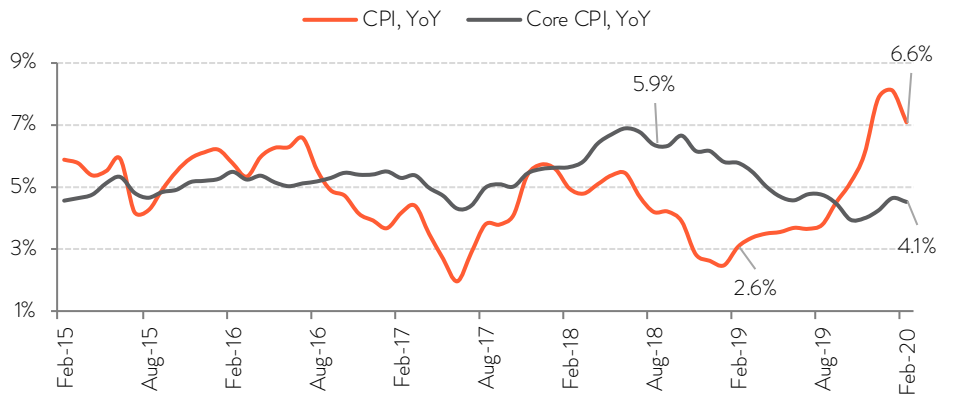
Source: CEIC, Bank of Baroda Research

**FIG 2 – FOOD INFLATION MODERATES**

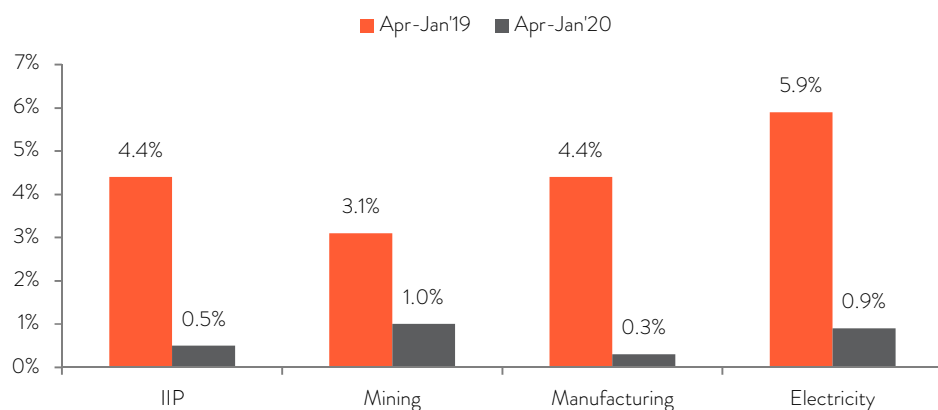


Source: CEIC, Bank of Baroda Research

**FIG 3 – CORE EDGED DOWN**



Source: CEIC, Bank of Baroda Research

**FIG 4 – BROAD BASED SLOWDOWN**

Source: CEIC, Bank of Baroda Research

**FIG 5 – IIP GROWTH REBOUNDS IN JAN'20**

Sectoral (%)	Weight	Jan-20	Dec-19	Jan-19	Apr-Jan'20	Apr-Jan'19
IIP	100.0	2.0	0.1	1.6	0.5	4.4
Mining	14.4	4.4	5.7	3.8	1.0	3.1
Manufacturing	77.6	1.5	(0.7)	1.3	0.3	4.4
Electricity	8.0	3.1	(0.1)	0.9	0.9	5.9
<b>Use-Based</b>						
Primary Goods	34.1	1.8	2.2	1.4	0.5	3.8
Capital Goods	8.2	(4.3)	(18.2)	(3.6)	(11.5)	5.7
Intermediate Goods	17.2	15.8	12.5	(2.8)	11.1	0.2
Infrastructure and Construction Goods	12.3	(2.2)	(2.6)	6.4	(2.6)	8.2
Consumer Durables Goods	12.8	(4.0)	(6.7)	2.5	(6.2)	7.0
Consumer Non-Durables Goods	15.3	(0.3)	(3.7)	3.8	2.3	4.2

Source: CEIC, Bank of Baroda Research

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For further details about this publication, please contact:

### **Economics Research Department**

Bank of Baroda

[chief.economist@bankofbaroda.com](mailto:chief.economist@bankofbaroda.com)