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ICRA

CONSUMER PRICE INDEX JUNE 2020

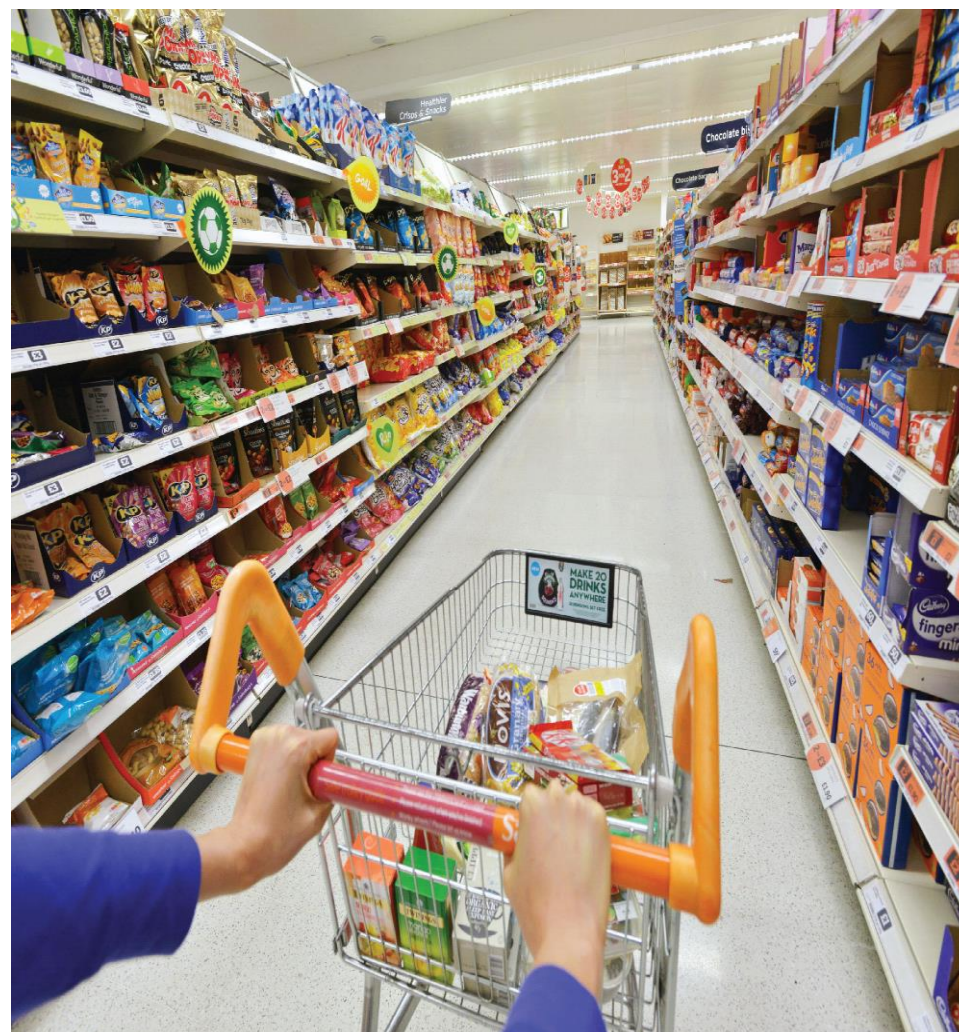
CPI inflation printed at higher-than-expected 6.1% in June 2020, exceeding the MPC's 2-6% medium term target range

JULY 2020



HIGHLIGHTS

- The year-on-year (YoY) CPI inflation, that was released by the CSO after a gap of three months, posted a negative surprise, revealing an inflation of 6.1% for June 2020, well above expectations (ICRA exp: 5.3%). Additionally, retail inflation in June 2020 was higher than the level of 5.8% in March 2020, when the lockdown was first imposed, challenging the view that demand destruction would cool inflation despite the supply-side hiccups. Moreover, the CPI inflation exceeded the upper end of the MPC's medium-term inflation target range of 4%+/-2% in June 2020.
- In terms of the trajectory, the data released by the CSO reveals that the YoY CPI inflation had increased from 5.8% in March 2020, to an imputed 7.2% in April 2020 (ICRA exp: 7.0%), before easing to an imputed 6.3% in May 2020 (ICRA exp: 6.0%). Subsequently, the CPI inflation has eased only mildly to 6.1% in June 2020 (+3.2% in June 2019) from 6.3% in May 2020 (+3.0% in May 2019).
- The mild sequential dip in the YoY CPI inflation in June 2020 was driven by a softening in the inflation for food and beverages, and to a smaller extent, housing. The impact of this was partly offset by the increase in the inflation for pan, tobacco and intoxicants, fuel and light and clothing and footwear. The YoY inflation for miscellaneous items in June 2020 remained in line with the print for the previous month.
- The YoY inflation for the food and beverages sub-index eased to 7.3% in June 2020 from 8.4% in May 2020, reflecting the sharp downtick in vegetables, pulses and products and fruits, as well as a milder softening in eggs, cereals and products, milk and products, and sugar and confectionery.



OVERVIEW

- The headline CPI inflation rate that was released by the CSO after a gap of three months, posted a negative surprise, revealing an inflation of 6.1% for June 2020, well above expectations (ICRA exp: 5.3%), driven by miscellaneous items, clothing and footwear, and pan, tobacco and intoxicants.
- Retail inflation in June 2020 was higher than the level of 5.8% in March 2020 led by pan, tobacco and intoxicants, miscellaneous items and clothing and footwear, when the lockdown was first imposed, challenging the view that demand destruction would cool inflation despite the supply-side hiccups. Moreover, the CPI inflation exceeded the upper end of the MPC's medium-term inflation target range of 4%+/-2% in June 2020.
- In terms of the trajectory, the data released by the CSO reveals that the YoY CPI inflation had increased from 5.8% in March 2020, to an imputed 7.2% in April 2020 (ICRA exp: 7.0%), before easing to an imputed 6.3% in May 2020 (ICRA exp: 6.0%). Subsequently, the CPI inflation has eased only mildly to 6.1% in June 2020 (+3.2% in June 2019) from 6.3% in May 2020 (+3.0% in May 2019).
- The mild sequential dip in the YoY CPI inflation in June 2020 was driven by a softening in the inflation for food and beverages, and to a smaller extent, housing. The impact of this was partly offset by the increase in the inflation for pan, tobacco and intoxicants, fuel and light and clothing and footwear. The YoY inflation for miscellaneous items in June 2020 remained in line with the print for the previous month.
- The YoY inflation for the food and beverages sub-index (with a weight of 45.9% in the CPI) declined to 7.3% in June 2020 (+2.4% in June 2019) from 8.4% in May 2020 (+2.0% in May 2019). This was led by a sharp correction in vegetables (to +1.9% from +5.5%), pulses and products (to +16.7% from +21.1%), fruits (to -0.7% from +2.0%), as well as a milder decline in eggs (to +7.4% from +8.7%), cereals and products (to +6.5% from +7.3%), spices (to +11.7% from +12.5%), milk and products (to +8.4% from +8.8%) and sugar and confectionery (to +4.4% from +6.0%; refer Exhibit 3). However, the YoY inflation hardened for the remaining categories of this sub-index, namely, non-alcoholic beverages (to +4.5% from +3.3%), oils and fats (to 12.3% from +11.9%), meat and fish (to +16.2% from +16.0%), and prepared meals, snacks, sweets (to +4.3% from +4.2%), in June 2020 relative to the previous month. In month-on-month (MoM) terms, the food and beverages sub-index rose by a mild 0.3% in June 2020, as compared to the 1.3% increase recorded in June 2019 (refer Exhibit 4), led chiefly by the trend for vegetables (+1.7% in June 2020; +5.2% in June 2019).
- Moreover, the inflation for housing (with a weight of 10.1% in the CPI Index) moderated to 3.5% in June 2020 from 3.7% in May 2020. In MoM terms, the sub-index recorded a 0.6% fall in June 2020, similar to the 0.5% fall recorded in June 2019.
- The inflation for miscellaneous items (with a weight of 28.3% in the CPI) eased marginally to 5.7% in June 2020 (+4.5% in June 2019) from the imputed 5.8% in May 2020 (+4.6% in May 2019), even as its components displayed a mixed trend. There was a considerable easing in the inflation for recreation and amusement (to +3.0% from +5.5%), and household goods and services (to +2.3% from +3.8%) in June 2020 relative to the previous month. However, there was an uptick in the YoY inflation in June 2020 relative to May 2020 for healthcare (to +4.2% from +4.1%), personal care and effects (to +12.4% from +10.7%), education (to +5.5% from +5.3%) and transport and communication (to +7.1% from +6.1%). On an MoM basis, the sub-index for miscellaneous items rose by 0.2% in June 2020, lower than the same in June 2019 (+0.3%).

- In contrast, the inflation for pan, tobacco and intoxicants (with a weight of 2.4% in the CPI) hardened to a multi-year high 9.7% in June 2020 from the imputed value of 6.3% in May 2020. This sub-index increased by a sharp 3.7% in MoM terms in June 2020, as compared to the 0.5% rise in June 2019.
- In addition, the inflation pertaining to clothing and footwear (with a weight of 6.5% in the CPI) rose to 3.5% in June 2020 from the imputed value of 3.4% in May 2020. In MoM terms, this sub-index increased by 0.2% in June 2020, higher than the MoM rise in June 2019 (+0.1%).
- The inflation for the fuel and light sub-index (with a weight of 6.8% in the CPI) rose to 2.7% in June 2020 from the revised 1.6% in May 2020. This sub-index increased by 1.8% in MoM terms in June 2020, considerably higher than the MoM uptick of 0.6% recorded in June 2019.
- Overall, the core-CPI inflation (CPI excluding food and beverages, and fuel and light)¹ stood at 5.1% in June 2020, marginally higher than the imputed print for May 2020 (+5.0%; refer Exhibit 5). On an MoM basis, this sub-index rose by 0.2% in June 2020, slightly higher than the 0.1% uptick in June 2019. Moreover, on a YoY basis, the headline CPI inflation exceeded the core-CPI inflation by 90 bps in June 2020.
- The YoY rural CPI inflation stood at 6.2% in June 2020, similar to the print of 6.1% in March 2020 and imputed value of 6.2% for May 2020. The YoY print hardened for pan, tobacco and intoxicants (to +9.9% from +4.8%), clothing and footwear (to +3.1% from +1.7%), and miscellaneous items (to +5.3% from +4.4%) in June 2020 compared to imputed values of May 2020, the impact of which was offset by the softening for food and beverages (to +7.8% from +8.8%) and fuel and light (to -0.9% from -0.3%).
- The urban CPI inflation eased to 5.9% in June 2020 from the imputed value of 6.4% in May 2020, driven by food and beverages (to +6.5% from +7.6%), pan, tobacco and intoxicants (to +9.1% from +10.3%), clothing and footwear (to +4.2% from +6.0%) and miscellaneous items (to +6.1% from +7.3%), offset partly by the sharp increase in inflation for fuel and light (to +9.2% from +5.3%).
- Accordingly, the imputed rural CPI inflation exceeded the urban CPI inflation by 29 basis points in June 2020.
- The average computed CPI inflation for Q1 FY2021 stood at 6.5%, significantly higher than the same for Q1 FY2020 (+3.1%), driven by food and beverages (to +8.7% in Q1 FY2021 from +1.9% in Q1 FY2020).

¹ Core-CPI inflation does not exclude the petrol and diesel index for vehicles, since the detailed version of data is not available from March 2020 to June 2020.

OUTLOOK

Retail prices of various items have recorded a mixed trend in the initial part of July 2020, with a moderation displayed by some cereals and pulses, even as oilseeds and vegetables have recorded a rise. In particular, the prices of tomatoes have increased significantly in the recent weeks. These trends may result in an uptick in the food inflation in the ongoing month, particularly in urban areas. However, with the monsoon rainfall exceeding the LPA by 13% as on July 12, 2020, kharif sowing having spread to more than half of last year's total acreage, and demand from the hotels and restaurants segment remaining subdued, the outlook for food inflation over the subsequent months is muted. Moreover, the provision of free foodgrains under the Pradhan Mantri Garib Kalyan Ann Yojana is expected to ease the overall demand-supply balance for certain cereals and pulses, and aid in cooling their prices.

Crude oil prices have largely stabilised at moderate levels, whereas the hikes in excise duty and VAT have pushed the retail prices of petrol and diesel to multi-month highs, imparting stickiness to the retail inflation.

The headline CPI inflation for June 2020 has exceeded the upper end of the MPC's target range, posing a dilemma in terms of the appropriate policy response as the economy gradually extricates itself from the supply and demand shock created by the pandemic.

In our view, the MPC will choose to frontload its assessment of the space for further rate cuts, in a bid to support sentiment and hasten transmission amid the substantial surplus in systemic liquidity, although the decision is unlikely to be unanimous. We expect an asymmetric cut of 25 bps in the Repo rate and 35 bps in the Reverse Repo rate in the next policy meeting.

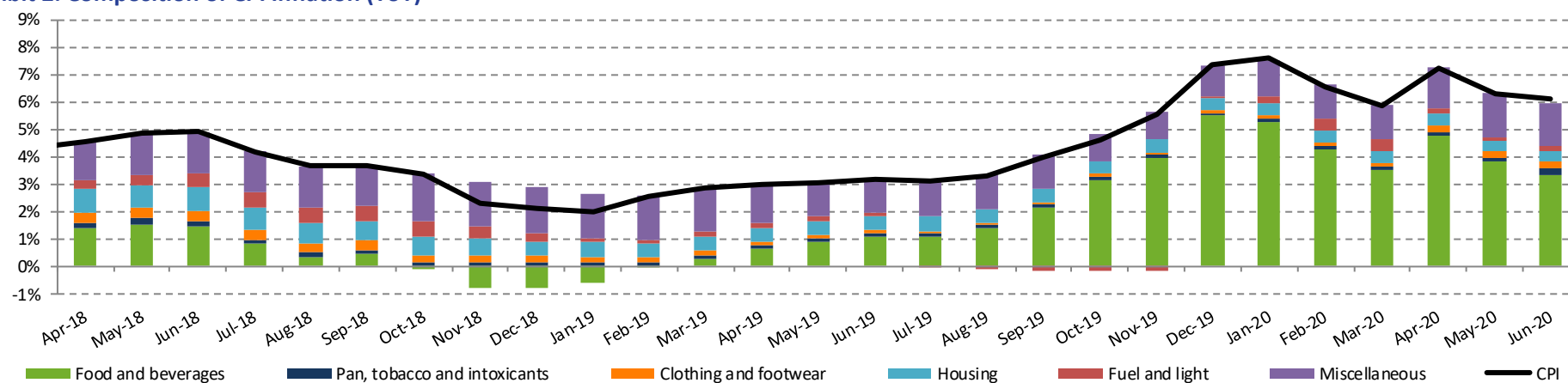


Exhibit 1: Trend in CPI Inflation (YoY)

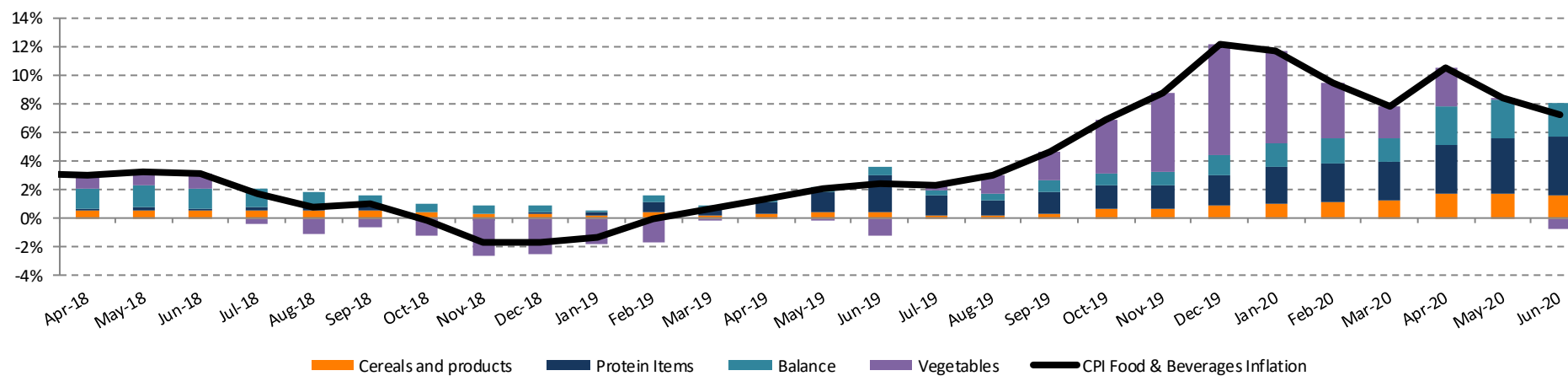
	Weight	Y-o-Y Inflation 2012 Base				M-o-M	Buildup
		Mar-20	Apr-20	May-20	June-20	June-20	June-20
		Final	Final	Final	Provisional	Provisional	Provisional
CPI (combined)	100.00	5.8%	7.2%	6.3%	6.1%	0.5%	2.0%
Food and beverages	45.86	7.8%	10.5%	8.4%	7.3%	0.3%	2.8%
Cereals and products	9.67	5.3%	7.8%	7.3%	6.5%	-0.5%	1.8%
Meat and fish	3.61	9.2%	9.3%	16.0%	16.2%	2.5%	12.8%
Egg	0.43	5.6%	9.0%	8.7%	7.4%	0.1%	-0.1%
Milk and products	6.61	6.5%	9.4%	8.8%	8.4%	0.2%	2.6%
Oils and fats	3.56	7.5%	10.8%	11.9%	12.3%	0.5%	4.6%
Fruits	2.89	3.6%	2.7%	2.0%	-0.7%	-2.4%	2.3%
Vegetables	6.04	18.6%	23.6%	5.5%	1.9%	1.7%	-2.5%
Pulses and products	2.38	15.8%	22.8%	21.1%	16.7%	-1.0%	6.1%
Sugar and confectionary	1.36	3.9%	10.3%	6.0%	4.4%	-0.5%	2.4%
Spices	2.50	9.8%	12.8%	12.5%	11.7%	-0.2%	2.5%
Pan, tobacco and intoxicants	2.38	4.7%	5.9%	6.3%	9.7%	3.7%	5.7%
Clothing and footwear	6.53	2.1%	3.5%	3.4%	3.5%	0.2%	1.9%
Housing	10.07	3.7%	3.9%	3.7%	3.5%	-0.6%	0.1%
Fuel and light	6.84	6.6%	2.9%	1.6%	2.7%	1.8%	-2.6%
Miscellaneous	28.32	4.4%	5.4%	5.8%	5.7%	0.2%	1.9%
Household goods and services	3.80	1.8%	3.8%	3.8%	2.3%	-1.4%	0.5%
Health	5.89	4.2%	2.8%	4.1%	4.2%	0.5%	0.9%
Transport and communication	8.59	4.3%	5.9%	6.1%	7.1%	0.8%	2.8%
Recreation and amusement	1.68	4.4%	5.7%	5.5%	3.0%	-2.0%	0.1%
Education	4.46	3.9%	5.3%	5.3%	5.5%	0.8%	3.1%
Personal care and effects	3.89	8.8%	10.7%	10.7%	12.4%	2.2%	4.0%
CPI-Food	36.55	8.8%	11.7%	9.2%	7.9%	0.3%	3.0%
CPI-Core*	44.97	4.0%	4.8%	5.0%	5.1%	0.2%	1.7%
CPI Rural		6.1%	7.2%	6.2%	6.2%	0.9%	1.8%
CPI Urban		5.6%	7.3%	6.4%	5.9%	-0.1%	2.2%

Source: Central Statistics Office (CSO); CEIC; ICRA research

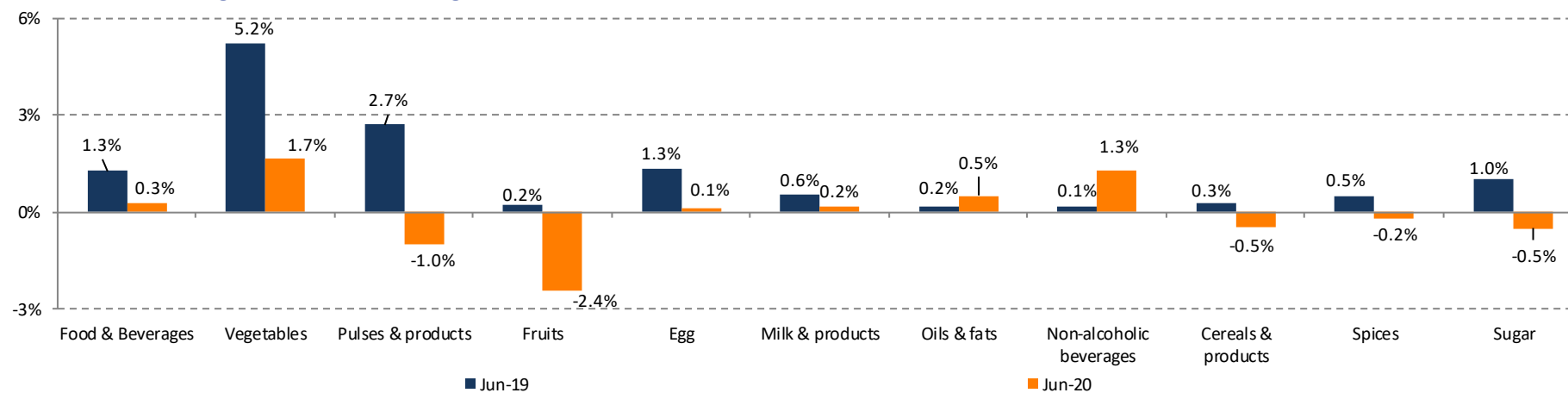
*CPI excluding food and beverages, and fuel and light, but including petrol and diesel for vehicles

Exhibit 2: Composition of CPI Inflation (YoY)

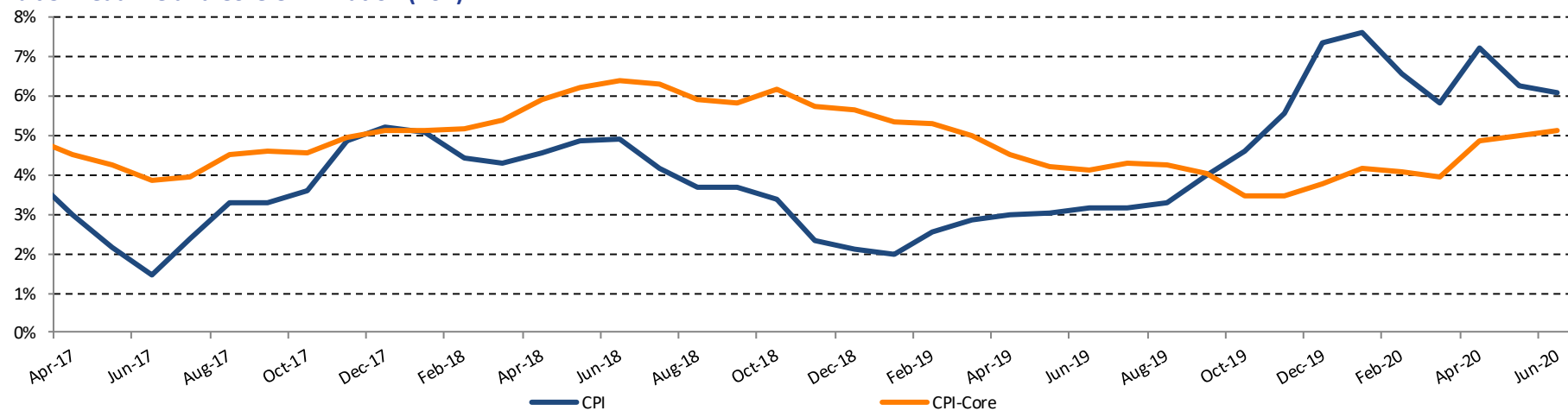
Source: CSO; CEIC; ICRA research

Exhibit 3: Composition of Food and Beverages Inflation (YoY)

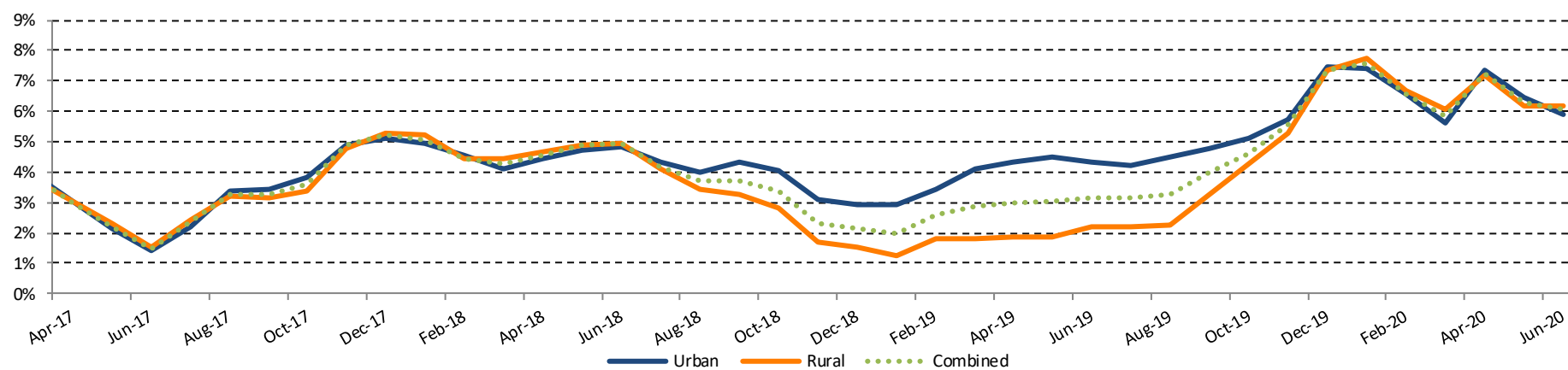
Source: CSO; CEIC; ICRA research

Exhibit 4: MoM Change in Food and Beverage Sub-Index

Source: CSO; CEIC; ICRA research

Exhibit 5: Headline and Core CPI Inflation (YoY)

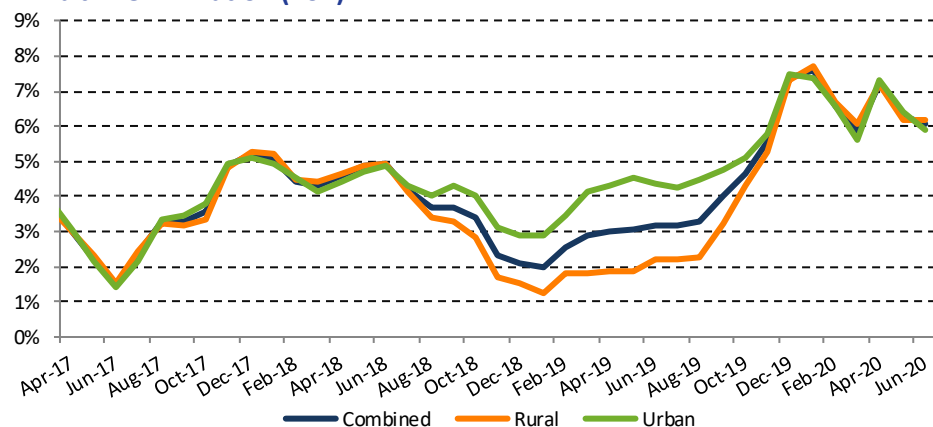
Source: CSO; CEIC; ICRA research

Exhibit 6: Rural and Urban CPI Inflation (YoY)

Source: CSO; CEIC; ICRA research

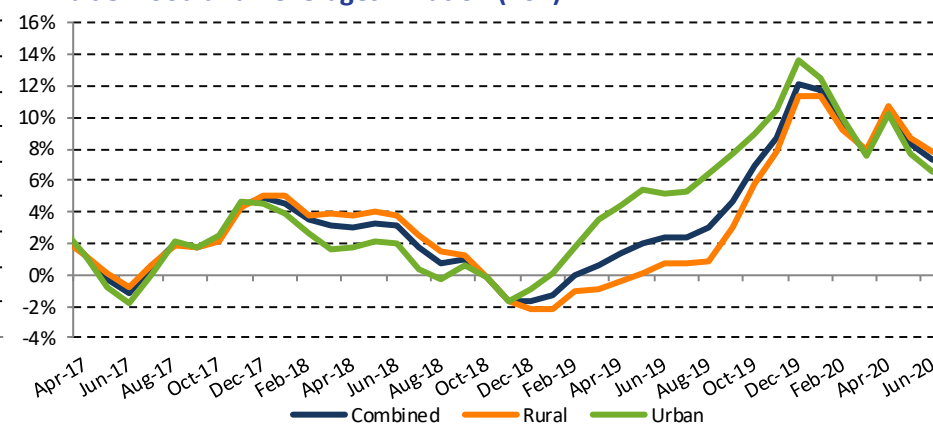
ANNEXURE

Exhibit 7: CPI Inflation (YoY)



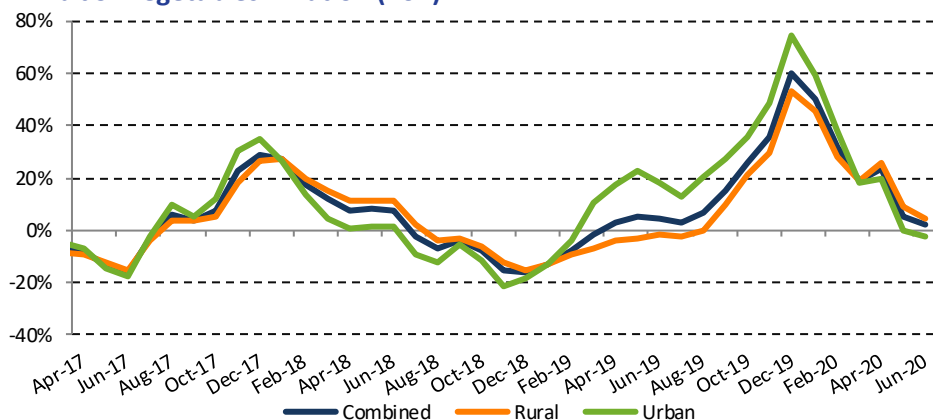
Source: CSO; CEIC; ICRA research

Exhibit 8: Food and Beverages Inflation (YoY)



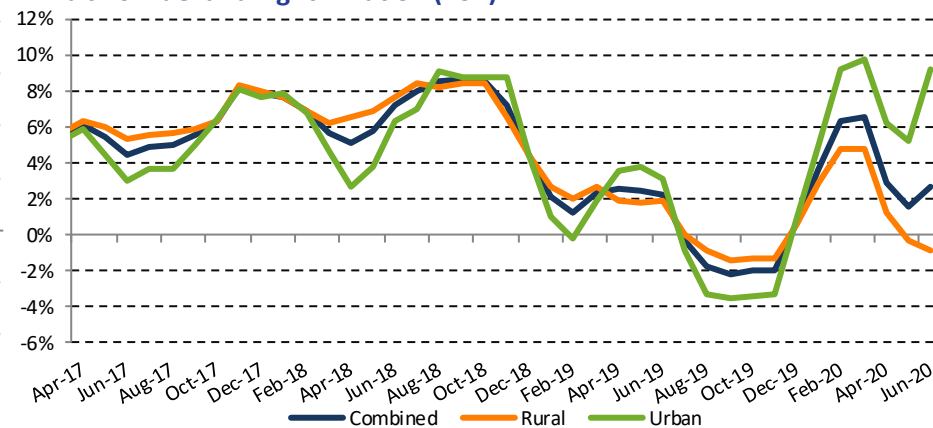
Source: CSO; CEIC; ICRA research

Exhibit 9: Vegetables Inflation (YoY)

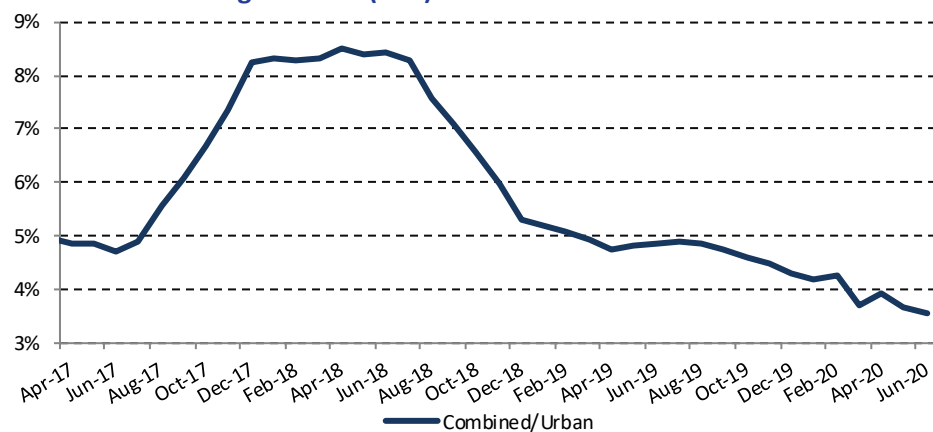


Source: CSO; CEIC; ICRA research

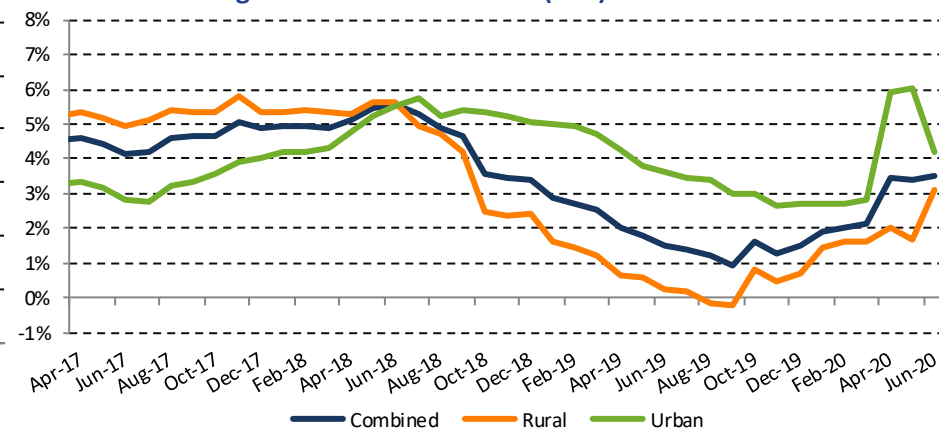
Exhibit 10: Fuel and Light Inflation (YoY)



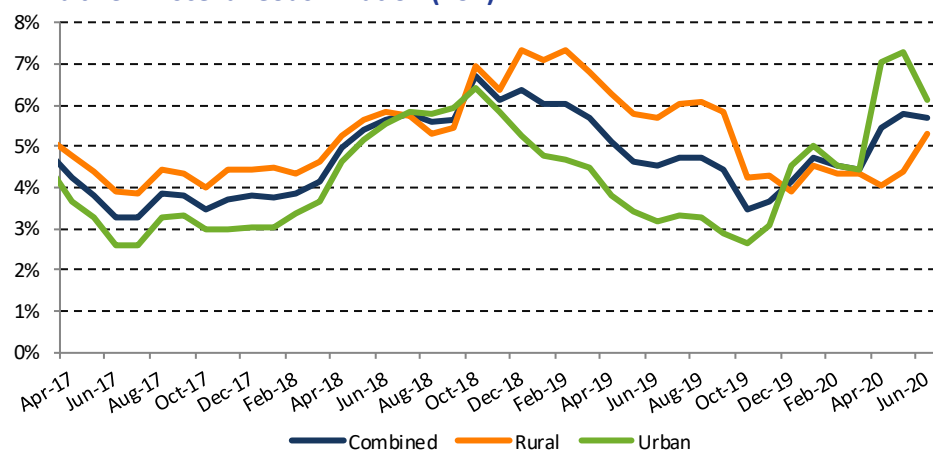
Source: CSO; CEIC; ICRA research

Exhibit 11: Housing Inflation (YoY)

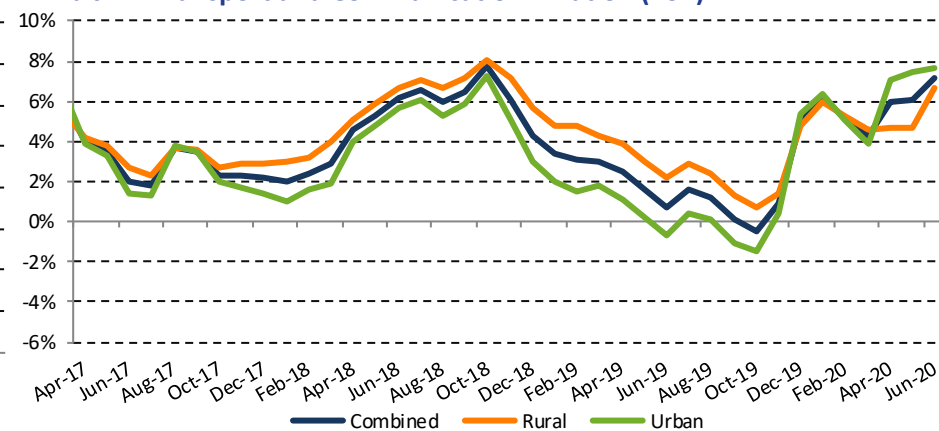
Source: CSO; CEIC; ICRA research

Exhibit 12: Clothing and Footwear Inflation (YoY)

Source: CSO; CEIC; ICRA research

Exhibit 13: Miscellaneous Inflation (YoY)

Source: CSO; CEIC; ICRA research

Exhibit 14: Transport and Communication Inflation (YoY)

Source: CSO; CEIC; ICRA research

ABOUT ICRA

ICRA Limited (formerly Investment Information and Credit Rating Agency of India Limited) was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange.

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- Assist the regulators in promoting transparency in the financial markets;
- Provide intermediaries with a tool to improve efficiency in the funds raising process.

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