

Food inflation: a continued discomfort

CPI surprised on the upside led by food inflation. Sharp spiral in vegetable inflation coupled with increase in oils and fat inflation resulted in the same. The latter showed the impact of elevated international prices and an increase in customs duty to support domestic production. Core inflation showed upward correction with frontloading of festival demand. Higher gold prices also impacted subcomponent of personal care and effects. Some correction in prices especially tomatoes are already visible in Nov'24 high frequency price data. This couple with a favourable base in Q3 will lend support to CPI. On rate action, there seems to be a delay as growth recovery is visible in sub segments and inflation, especially items of daily food consumption, are getting entrenched. Thus, we expect a nimble data dependent approach by RBI on the back of elevated global food prices, climate shocks and a stronger dollar. Our estimate of CPI remains at 4.5-5%, with risks tilted to the upside.

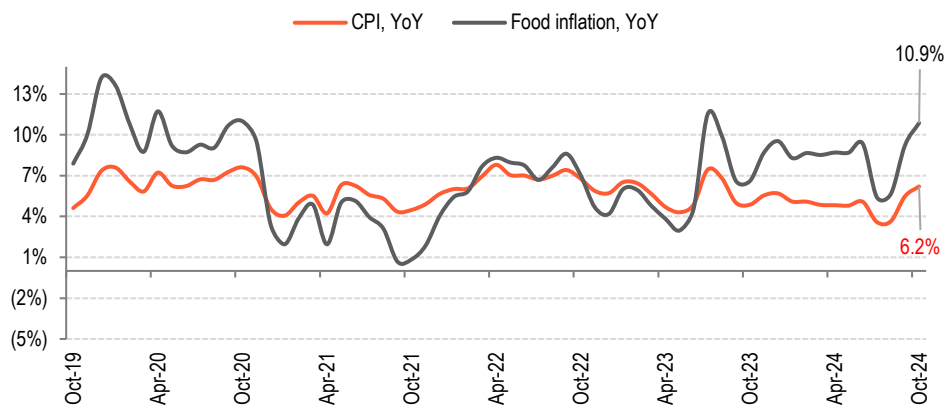
Food inflation overhang continues, core bottomed out

CPI inflation surprised significantly on the upside: CPI inflation came in at its highest since Sep'23 at 6.2% in Mar'24, on YoY basis, compared to last month's reading of 5.5%. Most of the increase in headline CPI was attributable to food inflation which went up by 164bps to 10.9% in Oct'24 from 9.2% in Sep'24. Within food, the increase was broad based. 7 out of 20 broader categories of food registered an increase in inflation. Among them, the most was visible in case of vegetable inflation (42.2% in Oct'24 compared to 36% in Sep'24). The vegetable price cycle is now becoming more entrenched, lasting for more than a year now. Other than vegetables, even oils and fat components went up considerably (9.5% from 2.5%), on account of an increase in basic custom duty to support domestic production. Adding to that, even international oilseed prices went up due to supply constraints, that also fed on domestic prices. Other items where some momentum was noticed was cereals due to rise in international price of wheat on account of harsh weather conditions in major exporting countries such as Australia and Russia.

On sequential basis, food inflation has inched up by 2.6% in Oct'24 from 1.2% in Sep'24. The strongest sequential pickup was seen in the case of vegetable inflation which firmed up by 8.2% in Oct'24 from 3.5% in Sep'24. Here our expectations have undershot, thus resulting in a lower number than the actual reading. Vegetable inflation was followed by an increase in oils and fats (6% compared to 3%) and fruit inflation (1.5% compared to 0%). On a seasonally adjusted basis, the sequential increase in food inflation is softer at 1.1%, thus some part also hinges on the seasonal phenomenon.

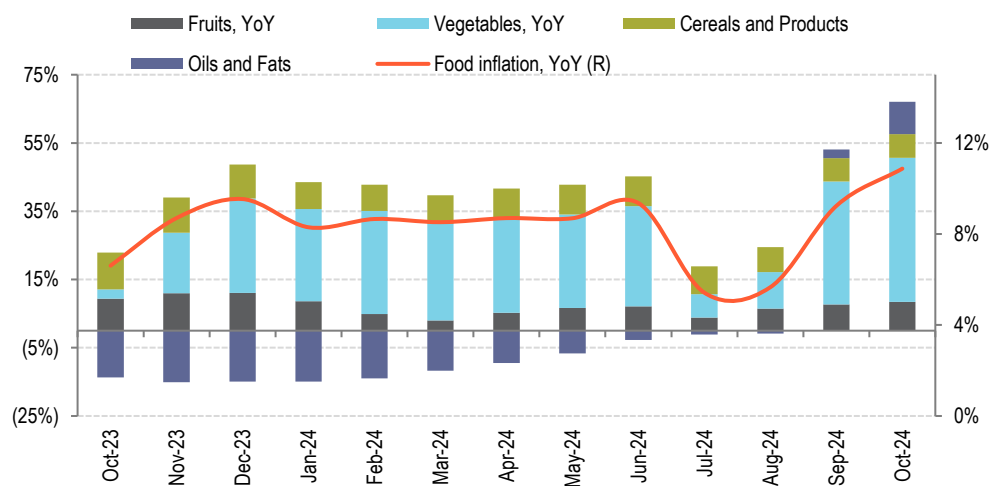
Going forward, uncertainty on the outlook of food inflation persists. Climate risks have resulted in significant distortion of the trajectory of food. However, generally the trend of vegetables which has caused maximum deviation in CPI from the targeted level tends to correct with arrival of fresh winter crops. But with elevated global prices, stickier dollar and lower arrivals of some perishable items in mandi in Nov'24, some stickiness in food inflation, cannot be ruled out.

Figure 1: Food inflation picked up



Source: CEIC, Bank of Baroda Research

Figure 2: ...led by vegetables, oils and fats, amongst others



Source: CEIC, Bank of Baroda Research

Core CPI (excl. food and fuel) has inched up to 3.7%. Core inflation inched up to 3.7% in Oct'24 from 3.5% seen in Sep'24. Some demand driven components such as household goods and services (2.7% from 2.5%), recreation and amusement (2.5% from 2.4%) and personal care and items (11% from 9%), have remained upbeat. For personal care and services, even elevated gold prices contributed to the increase.

On a sequential basis as well, personal care and effects rose the most followed by housing (due to increase in house rent and garage subcomponent) and clothing and footwear.

Fuel and Light inflation softened both on a YoY and sequential basis led by falling Kerosene prices.

Way forward: Food inflation has become a repeated discomfort diverging CPI from its targeted level. The question is how long? Oct'24 upside surprise print is solely led by continued spiraling of vegetable prices. Excluding vegetables, CPI is at 3.6% in Oct'24. However, continued increase in prices of daily items of consumption is a key watchable and unless that cools off, rate action by central bank seems to be delayed. Going forward, some respite might come in the form of a statistical base. High

frequency data of Nov'24 is also showing some downward correction, especially tomato prices. Our BoB ECI is increasing at a slow sequential pace of 0.4% in Nov'24 (first 11 days) and on a YoY basis by 5.5%. However, elevated global prices, firmer dollar and lower mandi arrivals in the domestic market lurk on the outlook of food inflation going ahead. Thus, appropriate supply management policies with focus on improved logistics might help in keeping inflation tackled.

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For further details about this publication, please contact:

Economics Research Department
Bank of Baroda
+91 22 6698 5143
chief.economist@bankofbaroda.com