

India Flash

WPI inflation jumps on weak currency and rising food prices

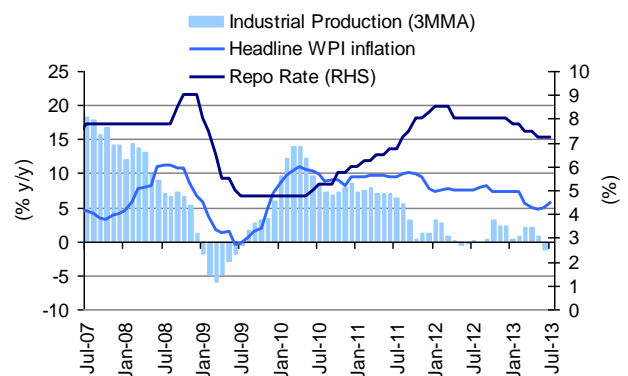
India's closely-watched wholesale price inflation jumped in July to a higher-than-expected 5.8% y/y (BBVA: 5.2%; consensus: 5.0%; prior 4.9%) led by upward energy price adjustments, rising food prices and the pass-thru of a weakening rupee (Table 1 and Chart 1). Reassuringly, core inflation stayed benign at 2.3% y/y (from 2.1% y/y in June). The jump in headline WPI inflation, which reached a 5-month high, was influenced by the import pass-thru of a near 10% rupee depreciation during May-July, accentuated by a hike in regulated diesel prices (3% m/m) and a surge in prices of fruits and vegetables (10.5% m/m) amid temporary supply distortions from heavy rains. Looking ahead we maintain expectations of average WPI inflation at 5.5% y/y over 2H13 as a bumper agricultural crop alleviates food price pressures going forward. That said, the latest WPI complicates the Reserve Bank of India's policy response amidst a worsening growth-inflation dynamic and external financing concerns. We continue to expect another 25bp rate cut once the rupee stabilizes, although recent external pressures and today's WPI outturn reduce the likelihood somewhat.

- Risks to our 5.7% growth projection for 2013 are skewed to the downside.** Most high frequency indicators suggest India's growth prospects have dampened amid easing domestic demand, elevated retail inflation, supply side bottlenecks, including raw material shortages and frequent power cuts, and external financing concerns that have hurt business sentiment. The June industrial production outturn, reported early this week, declined for a second straight month by -2.2% y/y (consensus: -1.1%) from a downwardly revised -2.8% in May, led by a contraction in mining and manufacturing activity. On a three month moving average basis, the June IIP (-1.0% y/y) posted its sharpest dip since June 2009.
- Recent measures to alleviate external vulnerability to aid rupee stability going forward.** Early this week, the government promised steps to compress domestic oil demand and imports of gold, silver and non-essential items, and boost capital inflows. The patchwork of measures include further hikes in import duties, fuel price reforms, easier norms on external commercial borrowings, issuance of quasi sovereign bonds by public sector financial institutions and easing dollar funding norms for domestic oil companies. While a longer term solution to India's external pressures lies in implementation of structural reforms to boost investment manufacturing output, the government's efforts are helping to ease the trade deficit (which fell in July by 30% y/y).

Table 1
July WPI inflation jumps on higher food and fuel prices

India WPI Inflation						
% Change Y/Y	Weight	Jul-13	Jun-13	May-13	Apr-13	Mar-13
Headline	100	5.8	4.9	4.6	4.8	5.7
Primary Articles (Non food)	4	5.5	7.6	4.9	7.6	9.3
Food	26	9.5	8.6	7.7	6.5	8.2
Fuel	15	11.3	7.1	7.3	8.3	7.8
Manufactured Non-food (Core)	55	2.3	2.1	2.5	3.0	3.6

Chart 1
Inflation ticks up even as growth slows



Source: RBI, BBVA Research

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