

India Watch

Getting to the core of it

Core disinflation: the hero of 2023 CPI story

Despite sharp move in food CPI inflation, which varied from 3.3% yoy to 10.6% yoy in FY24 (Until Dec), steady disinflation in core CPI (multiple measures of core) has been the hero of CPI inflation trajectory this year. Since Nov'22 core CPI inflation has softened by 225bps and core-core CPI (headline minus food, fuel, petrol, diesel, gold) has moderated by 345bp. By averaging at 4.65% yoy FY24TD, core CPI inflation is closer to the target than headline or food CPI inflation (5.5% yoy and 6.8% yoy respectively, Exhibit 2). Even in the [just released Dec CPI data](#), although headline inflation inched up 14bp to 5.69% yoy, core and core-core CPI fell further by 29bp and 50bp respectively to 3.76% and 3.35% yoy (Exhibit 1). In this note we delve deeper. Our analysis shows that, even though core disinflation is becoming more broad-based (in count terms), in value terms, the top drivers of disinflation may not have much room to continue further, limiting the downward impact it may have on headline CPI going into FY25.

Slicing, dicing core CPI: Some durable gains, some fleeting

Price build-up: Since Nov'22, while food & beverages CPI has cumulatively built-up to 7.2%, corresponding figure for core CPI stands at 4.1%. In case of fuel & light, build up is still negative, but narrowing (Exhibit 3).

% Point wise contribution to core: Housing has contributed the most to core CPI, followed by clothing and health (Exhibit 4).

Top items & drivers: Top 5 items account for 44% of core-core CPI, of this, house rent has the highest weight, followed by medicine, tuition fee, petrol & telephone charges (Exhibit 5). As for drivers of disinflation, since Nov'22 of the 225bp of overall disinflation, 60% can be explained by top eight items with telephone charges, house rent, soap, bus fare etc. taking the lead (Exhibit 6). On the other hand, gold alone added 25bp to core CPI since Nov'22, but there was a long tail of items that added further (Exhibit 7). In sum, we see less room for further disinflation in the top two drivers, in fact if data capturing issues get resolved, house rent could potentially start to add to core CPI rather than taking away from it.

Broadening of disinflation: Core CPI disinflation has become broad based with time. In Nov'22 74% of core CPI items were inflating at 4%+ rate, which has steadily moderated to 36% by Dec'23 (Exhibit 8). Thus, more than half of core CPI is inflating at or below 4% target. This is encouraging and suggests durability.

Goods & services CPI inflation: Most of the disinflation has emanated from services CPI. FY24TD, services CPI inflation has averaged at 4.1% yoy as against goods CPI inflation which has averaged at 4.8% yoy (Exhibit 9). We see further disinflation in goods CPI to bring down headline CPI in FY25. Services disinflation is expected to stagnate at low levels.

Input-output composite PMI & core CPI: An interesting visual correlation between composite PMI input output price gap and core CPI yoy suggests a reasonable measure of nowcasting core CPI (Exhibit 10).

Momentum effect vs base effect: Since Nov'22, for 10/14 months momentum effect (current m-o-m) has been lower than base effect (m-o-m same month last year, Exhibit 11). This indicates that favorable base effect has played a key role in falling core CPI inflation. As that diminishes for FY25, further meaningful core CPI disinflation is less likely.

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RBI: Reserve Bank of India

MPC: Monetary Policy Committee

CPI: Consumer Price Index

IIP: Index of Industrial production

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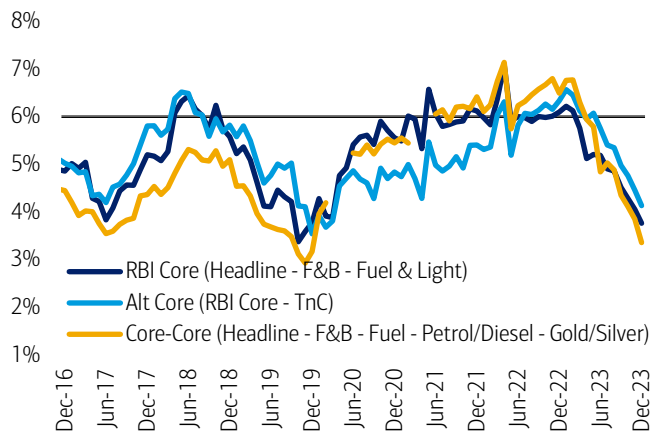
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Getting to the core of it

Exhibit 1: Various measures of core CPI (% yoy, monthly)

Since Nov'22 various measures of core are down by 225-345bp, partly offsetting upward pressure emanating from higher food inflation

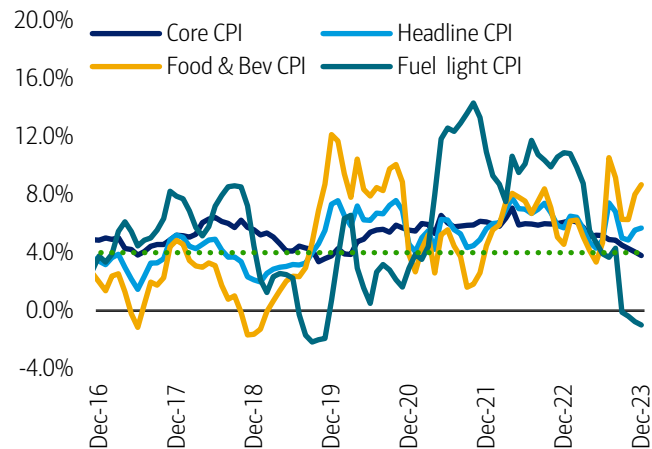


Source: MOSPI

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Exhibit 2: Difference in trajectories of food, fuel & core CPI vs target

FY24TD, headline, food, fuel & core CPI have averaged at 5.5, 6.8, 2.1 & 4.5% yoy, respectively. Core has trended closer to target than headline

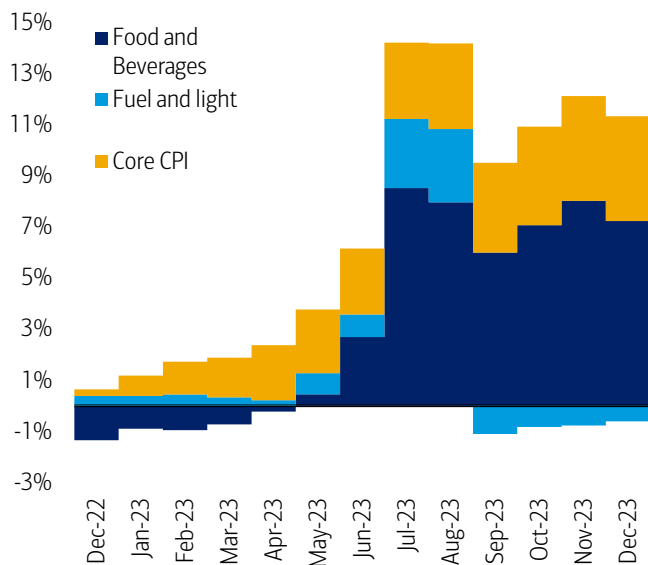


Source: MOSPI, RBI

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Exhibit 3: Price build-up in food, fuel & core CPI since Nov'22

Food price build up has been much higher than build-up in core CPI

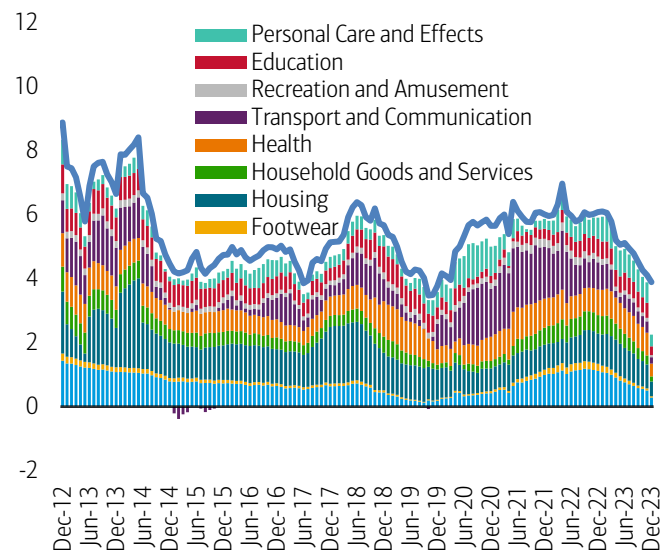


Source: MOSPI

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Exhibit 4: Sub-component wise % pt contribution to core CPI

Housing, clothing & health have continued to most to core CPI



Source: MOSPI

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Exhibit 5: Top weight bearers in core-core

These five make for 44% of core-core CPI

Top five weight wise items	Weight
House rent, garage rent	9.5
Medicine (non-institutional)	4.0
Tuition and other fees (school, college, etc.)	2.9
Petrol for vehicle	2.2
Telephone charges: mobile	1.8

Source: MOSPI

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Exhibit 6: Top drivers of core disinflation

60% of overall core CPI disinflation was driven by these top 8 items

Top drivers of core disinflation since Nov'22	Contribution (in bp)
Telephone charges: mobile	(25)
House rent; garage rent	(21)
Toilet soap washing	(19)
soap/soda/powder	(17)
Bus/tram fare	(15)
Saree (no.)	(14)
Tuition and other fees [school; college; etc.]	(13)
Cloth for shirt; pyjama; Kurta; salwar; etc. (metre)	(10)

Source: MOSPI

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Exhibit 7: Top drivers of higher core inflation

The tail is quite flat, with 8 items adding only 44bp together to core CPI

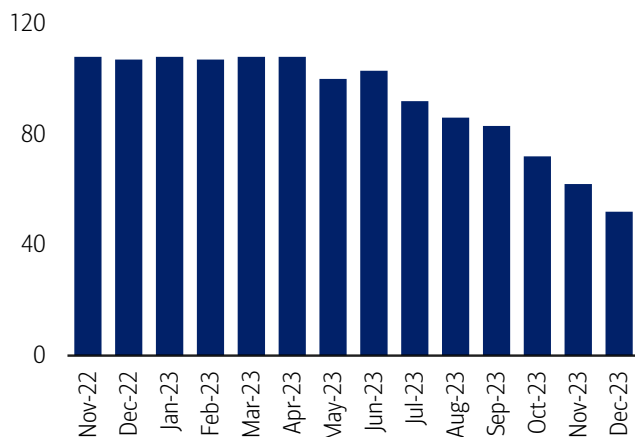
Top drivers of increase in core CPI inflation	Contribution (in bp)
Gold	25
Petrol for vehicle	6
Silver	5
Private tutor/coaching centre	4
Books; journals: firsthand	2
Coat; jacket; sweater; windcheater (no.)	1
Other medical expenses [non-institutional]	1
Motor car; jeep	1

Source: MOSPI

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Exhibit 8: Number of items \leq 4% inflation (in core)

In Nov'22 74% of core CPI was inflating at rates greater than or equal to 4%, that fell sharply to 36% by Dec'23 thus showing broad-based disinflation

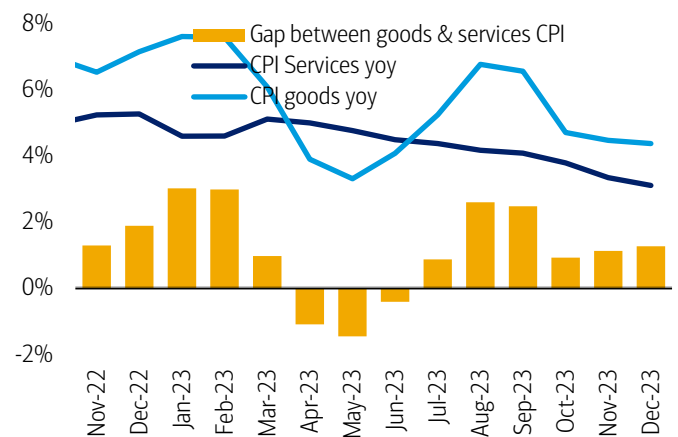


Source: MOSPI

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Exhibit 9: CPI goods vs services inflation (% yoy, annually)

While services inflation has steadily softened, goods CPI inflation has seen a bumpy ride, mostly surpassing services CPI

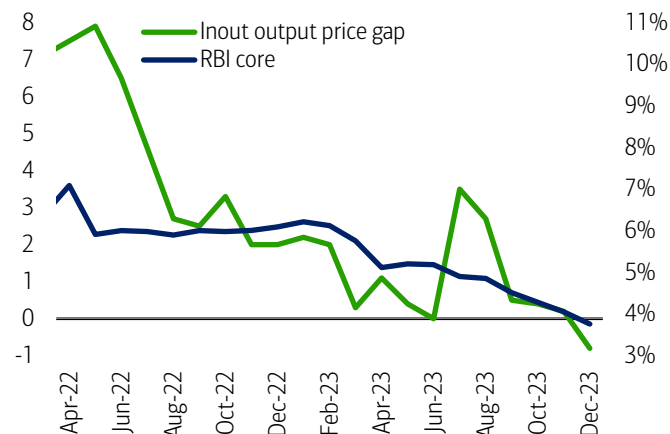


Source: MOSPI, CEIC

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Exhibit 10: Directional correlation between core CPI & composite PMI input output price gap

The input-output price gap from composite PMI offers meaningful directional correlation with core CPI yoy

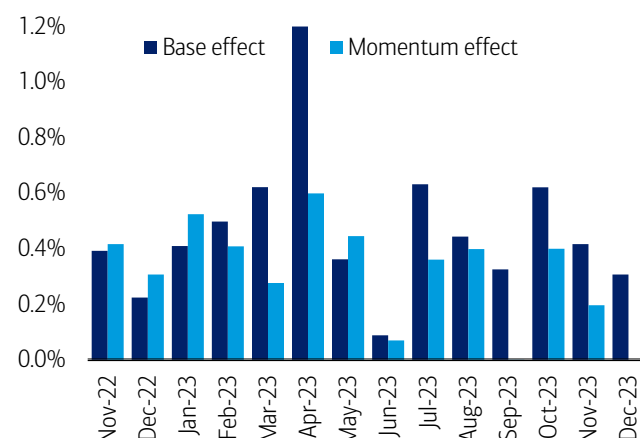


Source: Bloomberg, MOSPI, RBI core on RHIS

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Exhibit 11: Core CPI: Base effect vs momentum effect since Nov'22

Favorable base effect has been a bigger driver of core CPI disinflation vs momentum effect, the latter has been lower than base each month this FY



Source: MOSPI

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