

INFLATION PRESSURE EASES

Relevant for: Indian Economy | Topic: Issues relating to Growth & Development - Inflation & Monetary Policy

Inflation at both the retail and wholesale levels has been falling for the last 4-5 consecutive months. Inflation as measured by the Consumer Price Index (CPI), which captures retail inflation, and the Wholesale Price Index (WPI) has been falling in general for the last year or so. The CPI, for example, was as high as 5.21% in December 2017, following which it fell quite steadily (except for a mid-year blip in 2018) till it reached 2.05% in January 2019, the lowest it has been in 19 months. The WPI has similarly seen an overall decline, but has been more volatile than the CPI.

The main reason why inflation has been falling is the drop in global oil prices. After rising in the middle of 2018 to average \$80 a barrel in October, the Indian basket of crude oil prices fell to \$57 a barrel in December 2018. It was \$59 in January 2019. Prices in February have been slightly higher than that, but the increase is not much.

The nature of the Indian economy is such that a change in oil prices has knock-on effects on almost every sector such as food, manufacturing, transport and infrastructure. Any sector that uses fuel or energy as an input is affected by global oil prices because India is still overwhelmingly dependent on imported oil to meet its needs.

When global oil prices fall, inflation falls across the board, most notably in energy-intensive sectors. And within this, falling prices in each of these sectors have an impact on the other sectors dependent on them. For example, falling inflation in the transport sector means that every sector that needs to transport goods will also benefit.

Another aspect of falling inflation is that the Reserve Bank of India has more leeway to go easy on interest rates, one of its key inflation targeting tools. In its last Monetary Policy Review, the central bank cut the benchmark interest rate by 25 basis points. Some experts feel there is scope for even more cuts. Politically, low and falling inflation is always to the benefit of the government. This is especially noteworthy in the run-up to the general election. In contrast, the CPI inflation averaged about 7.6% in the three months leading up to the 2014 elections.

Economists have pointed out the divergence for quite some time now. The main reason behind it is that the two indices measure different products and assign each of the categories different weights in the calculation of the overall index.

This divergence has intensified since the implementation of the Goods and Services Tax because the new tax system affects retail inflation far more than it does wholesale inflation, since it is included in the final price of the product.

The outlook on oil prices is a stable one. The consensus is that crude oil prices will remain in the range of \$55-65 a barrel for the next three to four quarters. Given how important this is for inflation in India, experts feel retail inflation will remain subdued at 2-3% and wholesale inflation at 3-4% in the near future.

Pakistan's identity crisis, going back to the debates since its creation, remains unresolved

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