

# India Flash

## WPI inflation rises on higher food prices, while core holds steady

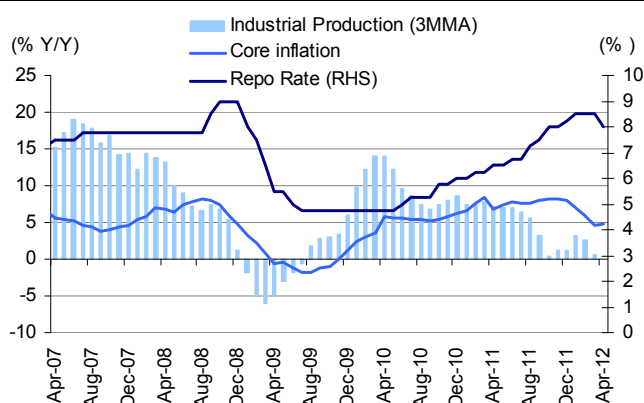
India's wholesale price inflation edged up by more than expected in April, to 7.2% y/y (BBVA: 7.0%, Consensus: 6.7%) from 6.9% in the previous month driven by higher food prices. Reassuringly, core inflation remained subdued at 4.8% y/y (4.6% in March) as demand pressures eased. Looking ahead, inflation risks are broadly balanced as demand compression is offset by pending energy price hikes, a weakening rupee and rising food prices. Given contained core inflation and downside risks to growth (see below), we expect the RBI to ease policy rates by another 50 bps, to 7.5%, over the course of this year. Meanwhile, recent measures to combat rupee weakness are likely to be of only marginal help in the near term, although we expect some appreciation during the second half of the year. As discussed in our recent [Asia Outlook](#), we expect India's growth and inflation to average 6.8% y/y and 6.9% y/y respectively in 2012.

- Slackening investment drives India's industrial production down 3.5% y/y in March.**  
 Failing market expectations, India's factory activity, released last Friday, fell in March by -3.5% y/y (consensus: +1.7%; +4.1% in February), driven by a contraction in manufacturing and mining activity. The weak IP outturn aggravates India's growth concerns amid delayed investment reforms, waning exports growth, narrowing profit margins, deteriorating asset quality of banks and fiscal imbalance.
- Measures to combat rupee weakness to help only at the margins.** The past two weeks have seen a spate of measures by the RBI to stem persistent rupee depreciation and restore stability. These include lifting interest rate ceilings on foreign currency deposits, deregulating interest rates on export credit, mandating partial conversion of fx earnings into rupees for exporters and fixing stricter limits on overnight open positions for traders. While these moves may be helpful at the margin in stemming further rupee weakness, they are unlikely to alter the currency's trajectory in the near term. Looking ahead, the rupee should remain under pressure amid little efforts to address India's widening current account deficit, worsening investment climate and fiscal imbalance.

Table 1  
India's Inflation table

India WPI Inflation						
% Change Y/Y	Weight	Apr-12	Mar-12	Feb-12	Jan-12	Dec-11
<b>Headline</b>	<b>100</b>	<b>7.2</b>	<b>6.9</b>	<b>7.4</b>	<b>6.9</b>	<b>7.7</b>
<b>Primary Articles (Non food)</b>	<b>6</b>	<b>1.6</b>	<b>-1.2</b>	<b>-2.5</b>	<b>0.7</b>	<b>1.8</b>
<b>Food</b>	<b>24</b>	<b>9.1</b>	<b>8.5</b>	<b>5.9</b>	<b>1.5</b>	<b>2.7</b>
<b>Fuel</b>	<b>15</b>	<b>11.0</b>	<b>10.4</b>	<b>13.6</b>	<b>14.6</b>	<b>15.0</b>
<b>Manufactured Non-food (Core)</b>	<b>55</b>	<b>4.8</b>	<b>4.6</b>	<b>5.9</b>	<b>7.0</b>	<b>8.0</b>

Chart 1  
Weakening factory activity, along with stable core inflation, increases probability of further rate cuts by the RBI



Sumedh Deorukhkar  
sumedh.deorukhkar@bbva.com  
+91 2226598581

Stephen Schwartz  
stephen.schwartz@bbva.com.hk  
+852 2582 3218