

## India: September inflation plunges

Inflation has dropped sharply this month and there is probably more to come in the months ahead



Reserve Bank of India  
Governor Shaktikanta  
Das

**5.02%** CPI inflation YoY%

down from 6.83%

Lower than expected

### Food prices normalizing and have further to go

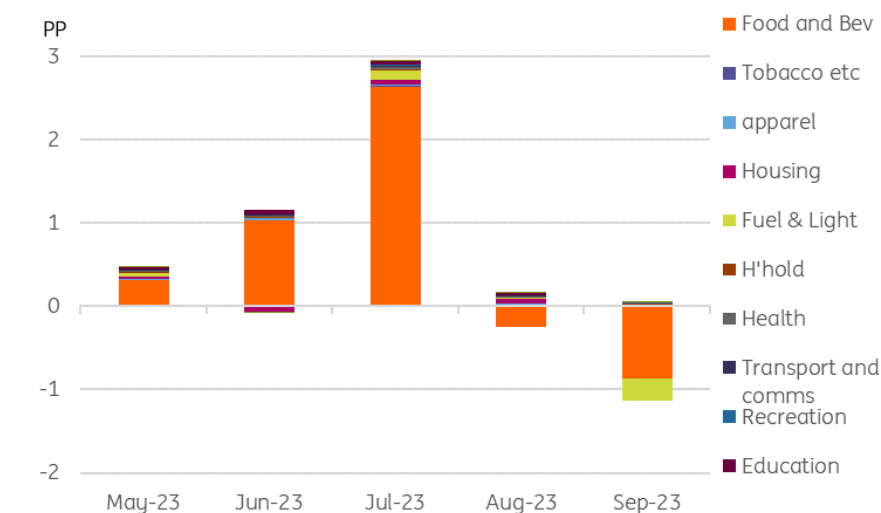
The big surprise in India's inflation numbers wasn't the direction. After months where inflation had been buoyed by spikes in seasonal food, it was clear that prices were reverting to normal again and given food's large weight in the CPI basket (about 46%) this was going to have a substantial negative impact on inflation.

But both we and the market underestimated how large an impact this was going to have. Food and beverage prices were down 1.8% MoM in September, on top of the 0.5% MoM decline in August. But this comes after they rose 2.2% in June, and then 5.7% in July.

When you look at the contributions to inflation chart below, what is immediately apparent is that recent volatility is almost entirely due to food price fluctuations. And on the assumption that food prices revert to something close to where they started before the recent supply shocks so that the positive contributions are largely netted out by current and future negative contributions, there is clearly still a long way to go.

That could mean headline inflation dropping into the lower half of the Reserve Bank of India's (RBI) 2-6% inflation target range in the coming months.

### Contribution to MoM change in CPI (pp)



Source: CEIC, ING

### No green light yet for RBI rate cuts

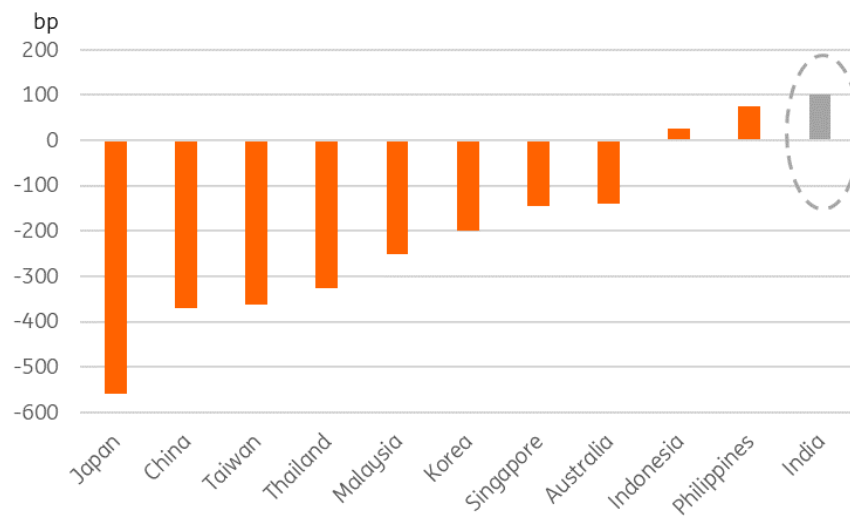
It would be premature, however, to think that this drop in inflation, and the further declines that seem likely in the months ahead, will provide a green light for the RBI to consider cutting policy rates anytime soon.

What comes up, must come down. But in terms of inflation, it will eventually settle at the underlying rate, absent further shocks. So the decline in inflation we are seeing now, and the further declines in the months ahead, will need to be looked through in just the same way as the RBI looked through the spike in inflation to 7.44% in July.

Not only that, but while US Treasury yields are boosting the USD, and putting Asian currencies like the INR under weakening pressure, it doesn't make much sense for the RBI to make its FX management job even harder by cutting rates.

That said, at 6.5%, the RBI's policy rate spread over Fed funds (100bp over the upper Fed bound) is one of the highest in the region, and when inflation settles down and the USD story shifts next year to a less supportive one, then the RBI is in a good position to be one of the first central banks regionally to consider easing policy rates.

## Asia policy rate spreads over Fed funds upper bound (bp)



Source: CEIC, ING

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