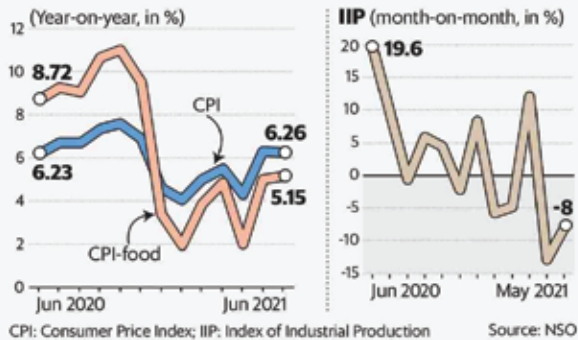


Growth hurdles

Retail inflation stood at 6.26% in June, down from 6.3% in May, though food inflation accelerated to 5.15%. Factory output continued to contract month-on-month in May.



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Retail inflation eases marginally in June

Asit Ranjan Mishra
asit.m@livemint.com
NEW DELHI

India's retail inflation cooled marginally in June while remaining above the upper limit of the central bank's inflation target for the second straight month as petrol and diesel prices rose, maintaining pressure on the government to cut taxes on fuel.

Data released by the National Statistical Office showed that retail inflation slowed to 6.26% in June from 6.30% in May, even though food inflation quickened marginally to 5.15%. During the month, prices of eggs, edible oils, fruits and pulses accelerated in double digits. Fuel inflation grew 12.7% as oil marketing

companies continued to increase petrol and diesel prices, raising the cost of transport and communication services. However, core inflation excluding food and fuel items eased to 6.2% in June from 6.4% in May.

The Reserve Bank of India's (RBI) monetary policy committee (MPC) aims to achieve a retail inflation target of 4%, plus or minus 2%. Even though elevated inflation will put pressure on RBI, it is expected to maintain policy rates unchanged at the next monetary policy review in August to protect the nascent economic recovery from the devastating impact of the pandemic.

Radhika Rao, an economist

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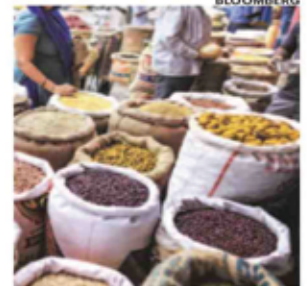
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at DBS Group Research, said the MPC may stay focused on growth, with an eye on the risks of a third pandemic wave. Still, its members are likely to express discomfort on the recent bout of sticky inflation in the absence of supply-side corrective steps such as fuel excise cuts, she said.

M. Govinda Rao, chief economic adviser at Brickwork Ratings, said first-quarter inflation has already breached RBI's inflation outlook by 40 basis points to 5.6%. "With this, the inflation outlook of 5.1% for the full fiscal by RBI looks challenging. With the lifting of lockdown in phases, domestic demand conditions are expected to improve gradually, and this may lead to a further increase in prices. We expect MPC to revise its inflation outlook upwards both for Q2 as well as for the full fiscal in its upcoming policy meeting. With commodity prices rising and uncertainty surrounding the inflation outlook, it remains to be seen for how long MPC will continue with the accommodative monetary policy stance. If the situation persists, balancing growth and inflation would become a real challenge and would call for close monitoring," he added.

On the escalating inflationary situation, the finance ministry last week said the localized restrictions due to the second wave could have led to some supply-side disruptions, contributing to price pressures. "With the encouraging progress of the southwest monsoon, supply-side interventions in the pulses and edible oils market, and gradual unlocking of states with declining caseload would mitigate cost pressures going forward. However, rising global commodity prices, especially of crude and logistics costs, pose upside risks to the infla-



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During the month, prices of eggs, edible oils, fruits and pulses accelerated in the double digits.

tion outlook," it added.

Separately, data released by NSO showed factory output grew 29.3% year-on-year in May, lifted by an extraordinary base effect as industrial activity had come to a halt the same month a year earlier due to the national lockdown to limit the spread of covid. In May 2020, the Index of Industrial Production (IIP) contracted 33.4%. The favourable base may bump up the index till August this year. However, sequentially, IIP continued to contract for the second consecutive month in May at 8% month-on-month, down from a 12.9% expansion in April.

Most economists suggested looking through the exaggerated growth number, which presents a false sense of normalcy even as the rampaging second wave of the pandemic in April forced many states to impose lockdowns, hurting industrial activity.

However, with states easing restrictions, high-frequency indicators signal a nascent recovery has begun in June. Aditi Nayar, chief economist at ICRA Ltd, said the sequential improvement engendered by the states' phased unlocking over the course of June is expected to be offset by a normalizing base a year ago. "Accordingly, we expect a further step-down in the pace of IIP growth to 15-20% (y-o-y) in June," she added.

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