

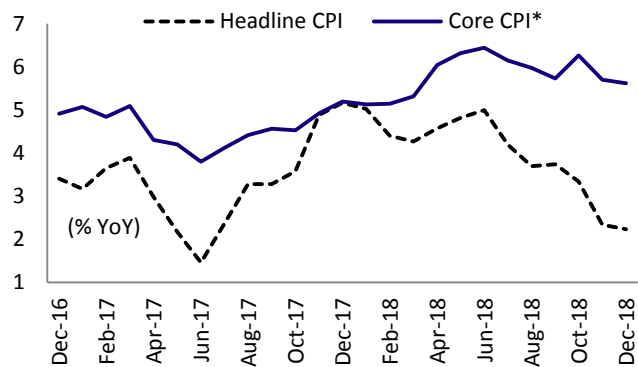
## CPI inflation at 18-month low

### Low inflation prints and weak growth momentum likely to drive rate cuts

- Headline CPI inflation stood at 2.2% YoY in Dec'18, in line with market consensus (our estimate: 2.3%) and slightly lower than 2.3% in the previous month. This was the lowest level of inflation in 18 months.
- Food prices declined by 2.5% YoY in Dec'18, sharper than our estimate of -1.7% YoY, largely on account of vegetables and cereals.
- Core inflation, however, eased marginally to 5.6% in Dec'18 from 5.7% in the previous month. This was much higher than our estimate of ~5%. Inflation in core services rose to a 48-month high of 7.4% in the month.
- In our view, low inflation prints and weaker growth momentum are likely to prompt the RBI to cut rates by 25bp in its monetary policy meeting next month. Further, depending on the Union Budget 2019-20, there could be another rate cut of 25bp in the April policy meeting, as inflation is likely to remain sub-4% by Mar'19.

- **CPI inflation at 18-month low...:** CPI-based retail inflation eased marginally to an 18-month low of 2.2% in Dec'18 from 2.3% in the previous month (*Exhibit 1*). The number was in line with market consensus but marginally lower than our estimate of 2.3%.
- **...on account of a fall in food prices...:** Food prices declined by 2.5% YoY in Dec'18 (our estimate: -1.7%). This was the third straight month of a fall in prices. The sharper-than-expected decline can largely be attributed to vegetables (prices down by 16.1% YoY after declining 15.6% in Nov'18) and cereals (inflation unchanged at 1.3%). Prices of pulses, eggs, fruits and sugar & confectionary also declined YoY in Dec'18.
- **...and lower core inflation:** Further, core inflation (all items excluding 'food & beverages', 'pan, tobacco and intoxicants' and 'fuel & light') eased marginally to 5.6% in Dec'18 from 5.7% YoY in the preceding month (*Exhibit 3*), but came in much higher than our estimate of ~5%. Core-core inflation (excluding petrol/diesel from core inflation) also eased marginally to 5.5% from 5.6% in Nov'18. Inflation in the fuel & light group eased to an 18-month low of 4.5% from 7.2% in the previous month.
- **Inflation in 'core services' at 48-month high:** Further refinement of CPI items shows that inflation in 'core services' rose sharply to a 48-month high of 7.4% in Dec'18 from 6.7% in the preceding month (*Exhibit 4*). Inflation in this segment has risen by ~390bp since the beginning of 2018. Inflation in housing eased sharply by ~70bp to a 17-month low of 5.3%, while that in goods eased to 1% from 1.2% in Nov'18.
- **Overall, low inflation, along with weaker growth momentum, is likely to prompt the RBI to cut rates by 25bp in its monetary policy meeting next month. Further, depending on the Union Budget 2019-20, there could be another rate cut of 25bp in the April policy meeting, as inflation is likely to remain sub-4% by Mar'19.**

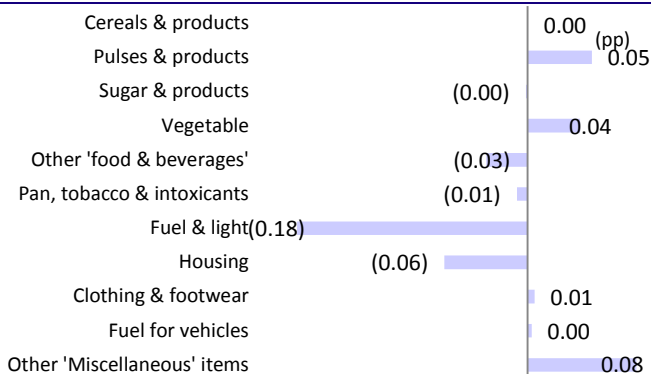
**Exhibit 1: Retail inflation eases to 2.2% in Dec'18**



\* Excluding F&B and F&L

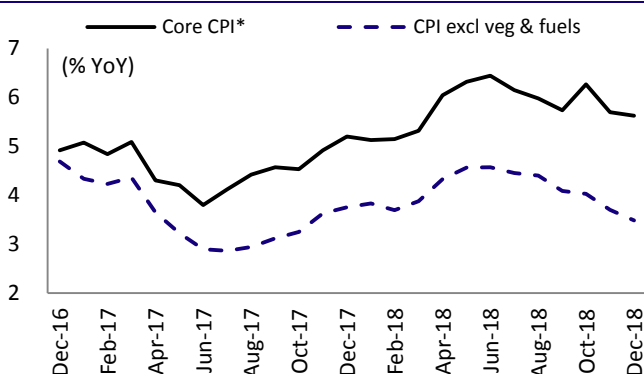
Source: Central Statistics Office (CSO), MOSL

**Exhibit 2: Inflation in fuel & light group eases sharply**



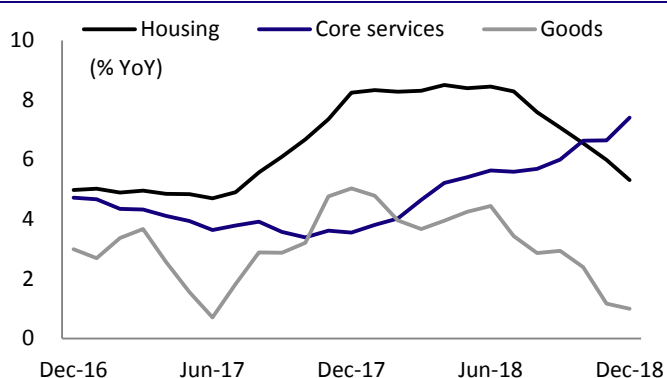
Source: CSO, MOSL

**Exhibit 3: Core CPI eases to 5.6% in Dec'18...**



Source: CSO, MOSL

**Exhibit 4: ...and inflation in 'core services' rises to 7.4%**



Source: CSO, MOSL

**Exhibit 5: CPI and key components (% YoY)**

	Weight	FY16	FY17	FY18	Dec-17	Oct-18	Nov-18	Dec-18
<b>Overall CPI</b>	<b>100.0</b>	<b>4.9</b>	<b>4.5</b>	<b>3.6</b>	<b>5.2</b>	<b>3.4</b>	<b>2.3</b>	<b>2.2</b>
<b>Food &amp; beverages</b>	<b>45.9</b>	<b>5.1</b>	<b>4.4</b>	<b>2.2</b>	<b>4.9</b>	<b>(0.2)</b>	<b>(1.6)</b>	<b>(1.5)</b>
Cereal & products	9.7	1.8	4.2	3.5	2.6	2.6	1.3	1.3
Pulses & products	2.4	31.9	9.3	(21.0)	(23.5)	(10.4)	(9.2)	(7.1)
Meat & fish	3.6	6.3	5.6	3.2	4.1	3.2	4.8	5.0
Milk & products	6.6	5.2	4.1	4.1	4.4	0.9	0.7	0.9
Fruits & vegetables	8.9	1.4	(0.1)	5.5	21.5	(5.6)	(12.7)	(10.1)
<b>Pan, tobacco &amp; intoxicants</b>	<b>2.4</b>	<b>9.3</b>	<b>9.5</b>	<b>6.9</b>	<b>7.8</b>	<b>6.1</b>	<b>6.1</b>	<b>5.8</b>
<b>Fuel &amp; light</b>	<b>6.8</b>	<b>5.3</b>	<b>5.8</b>	<b>6.2</b>	<b>7.9</b>	<b>8.5</b>	<b>7.2</b>	<b>4.5</b>
<b>Housing</b>	<b>10.1</b>	<b>4.9</b>	<b>5.2</b>	<b>6.5</b>	<b>8.2</b>	<b>6.6</b>	<b>6.0</b>	<b>5.3</b>
<b>Clothing &amp; footwear</b>	<b>6.5</b>	<b>5.8</b>	<b>5.0</b>	<b>4.7</b>	<b>4.9</b>	<b>3.6</b>	<b>3.5</b>	<b>3.5</b>
<b>Miscellaneous</b>	<b>28.3</b>	<b>3.7</b>	<b>4.5</b>	<b>3.8</b>	<b>3.8</b>	<b>6.7</b>	<b>6.2</b>	<b>6.5</b>
Transport & communication	8.6	0.4	3.0	2.7	2.2	7.7	6.1	4.3
<b>Core CPI#</b>	<b>47.3</b>	<b>4.3</b>	<b>4.7</b>	<b>4.5</b>	<b>5.2</b>	<b>6.3</b>	<b>5.7</b>	<b>5.6</b>
<b>Core CPI excl petrol, diesel etc</b>	<b>42.9</b>	<b>5.1</b>	<b>4.9</b>	<b>4.6</b>	<b>5.3</b>	<b>5.8</b>	<b>5.6</b>	<b>5.5</b>

# Excluding F&B, PT&I and F&L

Source: CSO, MOSL

Explanation of Investment Rating	
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SELL	< - 10%
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