Why volatile food prices will keep the heat on India's consumer inflation level this year

Lower rainfall in some parts of the country is expected to keep food prices elevated in the coming months. Which means inflation will be above 6%.

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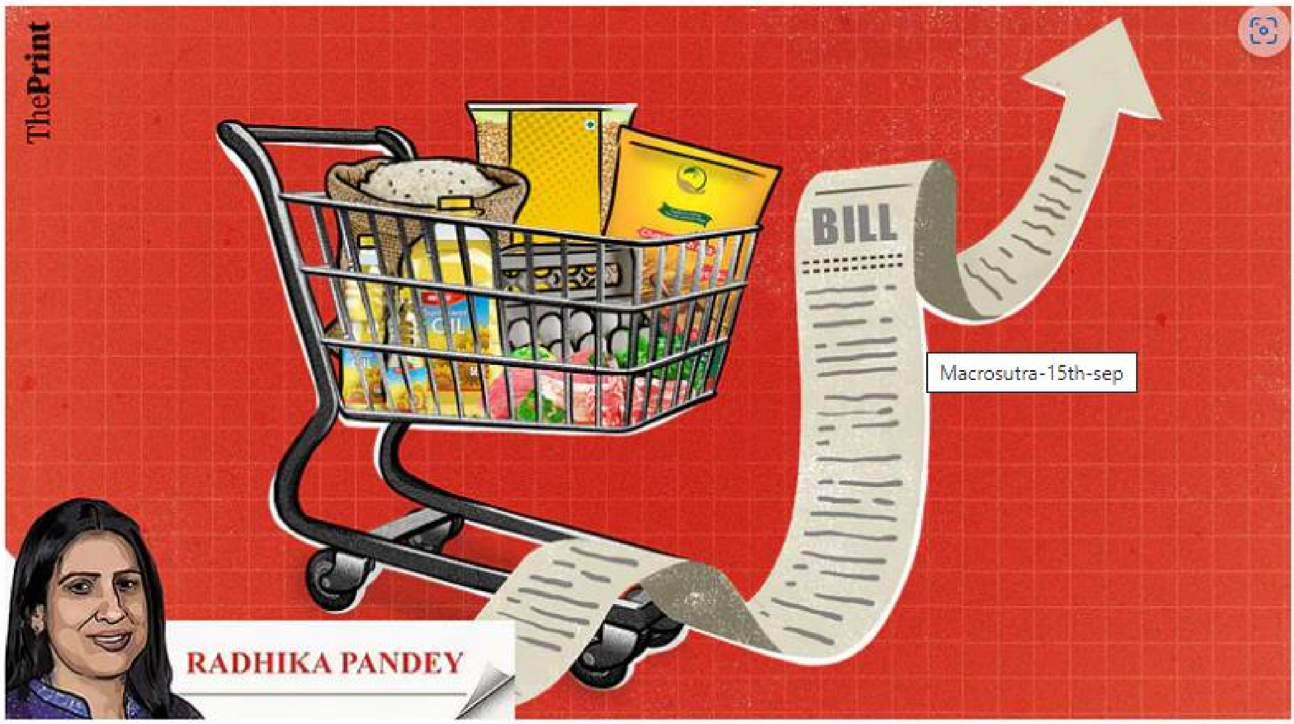
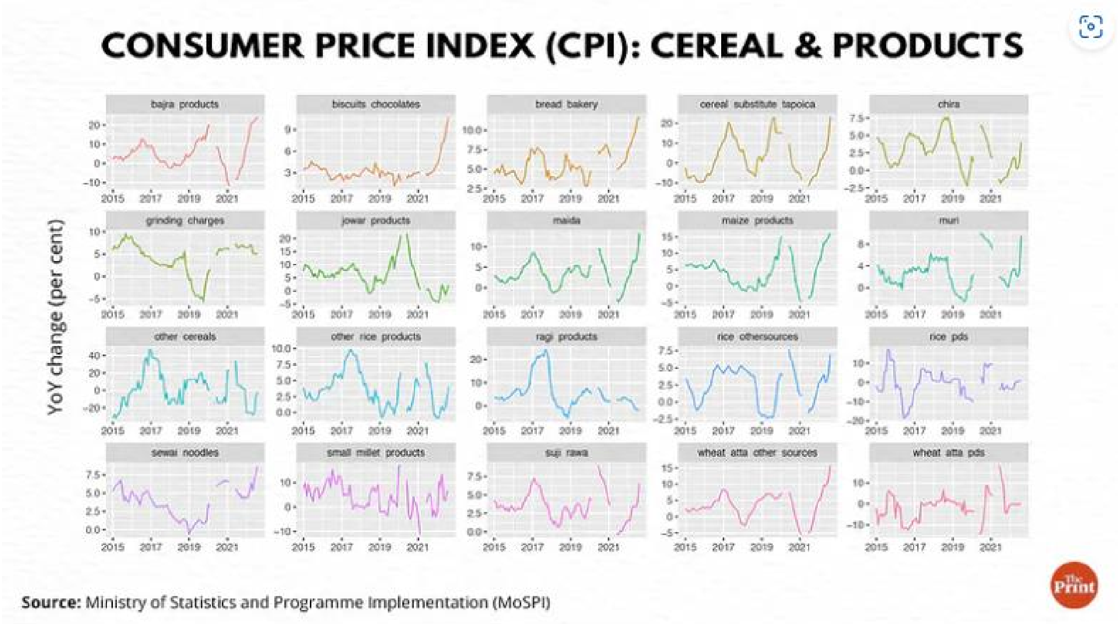


India's retail inflation surged to 7 per cent in August from a five-month low of 6.7 per cent in July. Food, which accounts for nearly half of the Consumer Price Index (CPI) basket, grew 7.62 percent as against 6.69 per cent in July. While the prices of edible oils eased, the prices of cereals, pulses, milk, fruits, vegetables and prepared meals and snacks saw an uptick.



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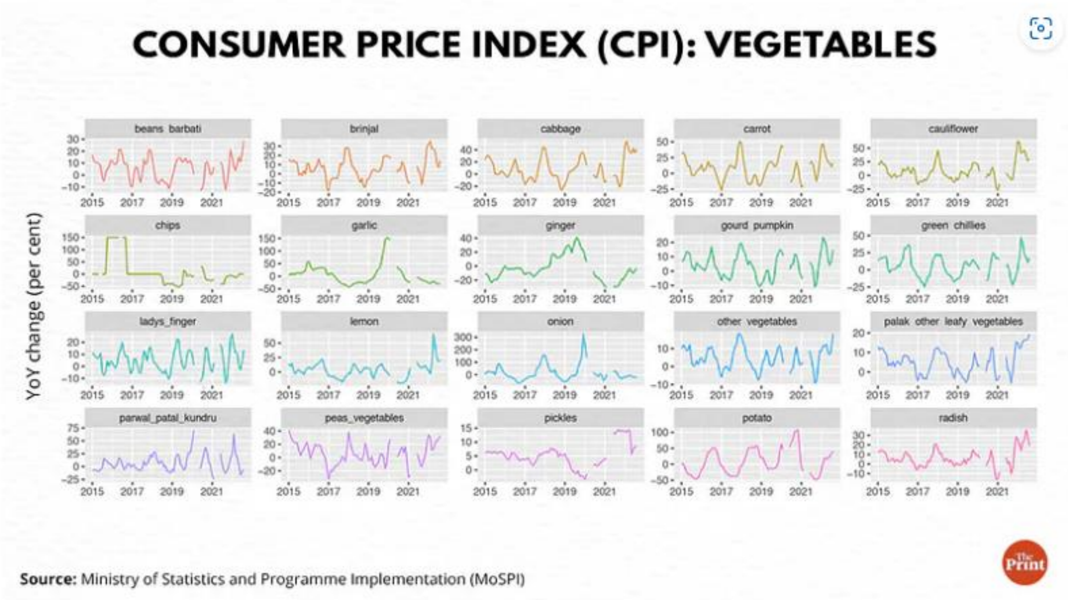

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Cereal inflation rose sharply to 9.57 per cent in August against 6.9 per cent in July. Cereals prices were impacted by adverse weather conditions and lower procurement. Prices of vegetables continue to remain in double-digits, increasing from 10.9 per cent in July to 13.23 per cent in August. Given the lower rainfall in some parts of the country, food prices are likely to remain elevated in the coming months.

Moderation in edible oil prices

Domestic edible oil prices are influenced by international edible oil prices. After peaking in March, the international edible oil prices measured by the Food and Agricultural Organisation's (FAO) Vegetable Oil index have seen a moderation.

The continued decline of the index was driven by lower world prices of palm and sunflower oil. Palm oil prices have fallen owing to increasing export availability from Indonesia. The gradual resumption of shipments from Ukraine's seaports has resulted in decline in sunflower oil prices.

There is a strong correlation between international and domestic inflation of edible oils as India meets 60 of its edible oil requirements through imports. Unlike edible oils, the correlation between international and domestic cereal inflation is weak. Thus, while international cereal prices have started to moderate in the last few months, the domestic prices of cereals have inched up.

Spike in cereal prices

Wheat production was impacted by lower harvest due to the unusual heat wave in March. The Fourth Advance Estimates of production for food grains released by the Ministry of Agriculture, put wheat production at 106.84 million tonnes, lower than last year's production of 109.59 million tonnes.

The procurement of wheat fell by more than 5 6 per cent as farmers sold to private players for exporting wheat in large quantities to take advantage of the situation created by the Russia-Ukraine war. Later, the government had to ban the export of wheat. The public stock of wheat has fallen to 26.65 million tonnes as on August 1. This is the lowest in more than a decade for this date.

With lower stocks, the government replaced around 5.5 million tonnes of wheat under the Pradhan Mantri Garib Kalyan Anna Yojana (PMGKAY) with rice. Later, another 6 million tonnes of wheat was replaced with rice under the National Food Security Act (NFSA).

The abnormal distribution of rains in the current monsoon season has caused damage to the paddy crop. The government has indicated that rice production could fall by 4-5 million tonnes this Kharif season due to low monsoon rainfall in Uttar Pradesh, Bihar, Jharkhand, and West Bengal. It then imposed a 20 per cent duty on exports of certain varieties of rice. Further, it imposed a blanket ban on exports of broken rice.

Cereal prices are seen to be elevated this month as well. Price Monitoring Division (PMD) in the Department of Consumer Affairs under the Ministry of Consumer Affairs monitors retail and wholesale prices of 22 essential commodities on a daily basis. The daily prices released by the PMD give early indications of the trajectory of food prices. According to the PMD, the retail price of rice was Rs 38.3 per kg as on September 12, up from Rs 36.6 per kg two months back. The price of pulses such as Tur Dal have risen by more than 7 per cent in a span of two months.

Key drivers of food inflation

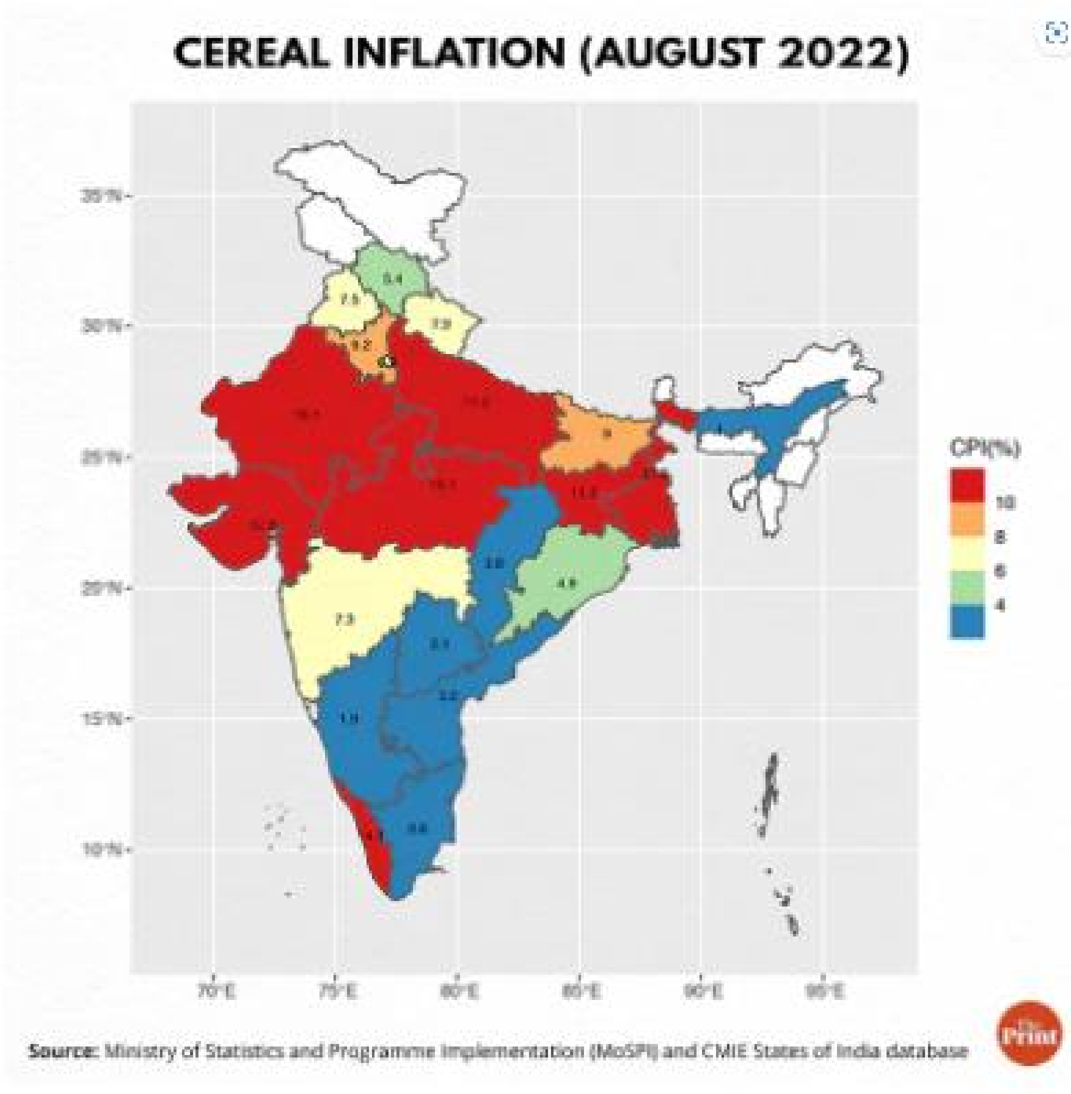
Food inflation was the key driver of the overall headline inflation in August. It contributed 50 per cent to the 7 per cent headline inflation. Within food, the contribution of cereals and pulses to food inflation has seen a steady increase since May. This is in contrast to last year, when the contribution of cereals to the food inflation was negative.

In the Covid year (2020-21), India produced an all-time high of 310 million tonnes of food grains, which was 4.5 per cent higher than the output in the previous year. All major crops registered record outputs in 2020-21. Bumper crop led to record purchases of rice and wheat. Coupled with huge carry over stocks, the government was able to sell food grains under various welfare schemes. As an outcome cereal prices remained controlled during most part of the last year.

In contrast, during the Covid year, the key drivers of inflation were, egg, fish and meat and vegetables. Higher demand for protein-rich food to recover from Covid along with increase in feed prices had pushed the prices of eggs, meat and fish in 2020-21. As pointed out by an RBI study, the prices of vegetables surged due to collapse of various mobility indicators: arrivals in mandi dropped, daily movement of trucks collapsed and agri-markets were closed.

Food inflation in states

Among states, the highest inflation in August was recorded by West Bengal, Gujarat and Telangana. These states recorded more than 8 per cent inflation. West Bengal, Gujarat and Rajasthan recorded double-digit growth in food inflation. Worryingly, West Bengal logged a whopping 21.2 per cent rise in cereal prices. This was a sharp increase from 13.9 per cent cereal inflation recorded in July. Uttar Pradesh, Rajasthan, Jharkhand and Gujarat also recorded cereal inflation in double-digits.



In fact, excluding the southern states, the country is seen to be experiencing higher cereal inflation. Persistent food inflation will likely keep the headline inflation above the upper tolerance level of 6 per cent till the end of this year.

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Views are personal.