

## India Macro Flash

### RBI Maintains Status Quo; Inflation Internals Dominate Headline

- **RBI Keeps Rates on Hold (for now)...** — The RBI surprised all market participants by keeping the repo rate unchanged at 7.75%. We along with the market were pricing in a 25bps hike, primarily due to recent “**headline**” inflation prints – with both [WPI](#) and [CPI](#) coming in well above the RBI’s base-line estimates. The decision does appear pragmatic, given that vegetables contributed [300bps](#) to the Nov CPI print of 11.2% and [180bps](#) to the WPI headline of 7.5% (see page 2).
- **Admits Today’s Policy Decision Was a “Close” One** — Given elevated levels of headline inflation, the RBI has said that “today’s policy decision is a close one”. However, considering weak growth, coupled with (1) soft sampling indicating a fall in vegetable prices and (2) disinflationary factors – viz negative output gap, recent INR appreciation (up 11% from the lows) and lagged effect of past tightening measures, it said that “**there is merit in waiting for more data to reduce uncertainty**”.
- **Maintains Guard on Inflation - Food and Core Are Key** — While today’s rate decision clearly caught the markets by surprise, the RBI emphasized in both the media/analyst call that it remains “vigilant” of risks (including taper). Moreover, its forward guidance states that (1) If the expected softening of [food inflation](#) does not materialize and translate into a significant reduction in headline inflation in the next round of data releases and (2) If inflation [excluding food and fuel](#) does not fall, the Reserve Bank “**will act, including on off-policy dates** if warranted”
- **“Food” Inflation Outlook:** As mentioned in our earlier notes, “[all things being equal](#)”, a sharp correction in veggie prices could lead to a substantial drop in the headline numbers e.g., a 25% fall in the vegetable price index from current levels would pull down WPI by ~100bps and CPI by ~200bps. Interestingly, latest available data indicate a moderation in onion prices at the wholesale level from Rs 50/kg in Oct to ~Rs10/kg currently.
- **Rate Implications:** Going forward, in addition to the recommendations of the Urjit Patel Committee on monetary framework due end Dec, the “**internals**” of the WPI and CPI prints due on 13 and 14 Jan would be key to watch. While easing vegetable prices are likely to result in headline inflation trending lower in the coming months, given the stickiness in core CPI (at ~8%), we still expect a 25bps repo-rate hike in 4QFY14. However, given the weak state of the economy, we believe the hurdle to hike rates is rising.
- **Market Impact:** Both rates and equity markets reacted favorably to the RBI rate decision today. The benchmark 10-year bond yield slid by 13bps while 1 OIS declined by 15bps as traders pared down their interest rate expectations. Equity markets on the other hand climbed by 1.5% intraday. However, the reaction on exchange rate was muted, with the Rupee trading at Rs61.91/US\$.

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*With thanks to  
Abha Agarwal*

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#### WHAT’s INSIDE

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**See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.**

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## Policy Highlights – “Veggies” in Focus....

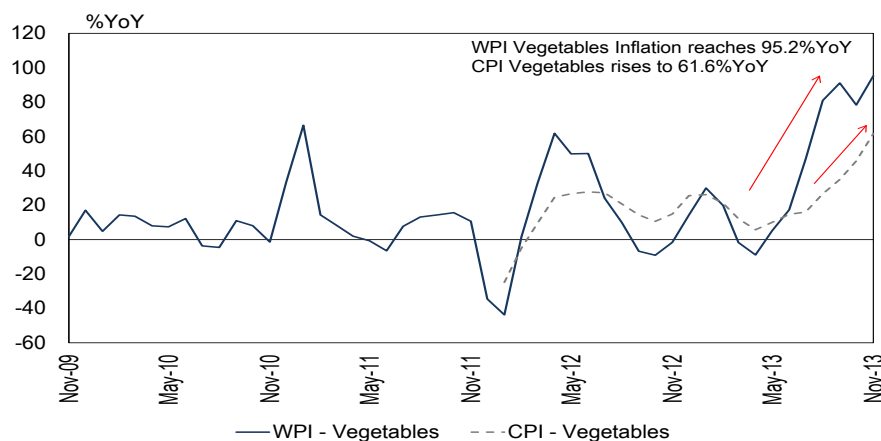
### VEGETABLE PRICES: MAIN FOCUS

The RBI is watchful of the “unseasonal upturn” in vegetable prices and will look through short-term spikes in vegetables inflation.

On the wholesale level, vegetable prices were up 95.2% YoY in November.

On the retail level, vegetable prices were up 61.6% YoY in November

Figure 1. Trends in Vegetables Inflation – WPI and CPI (%YoY)



Source: Office of the Economic Advisor, CSO

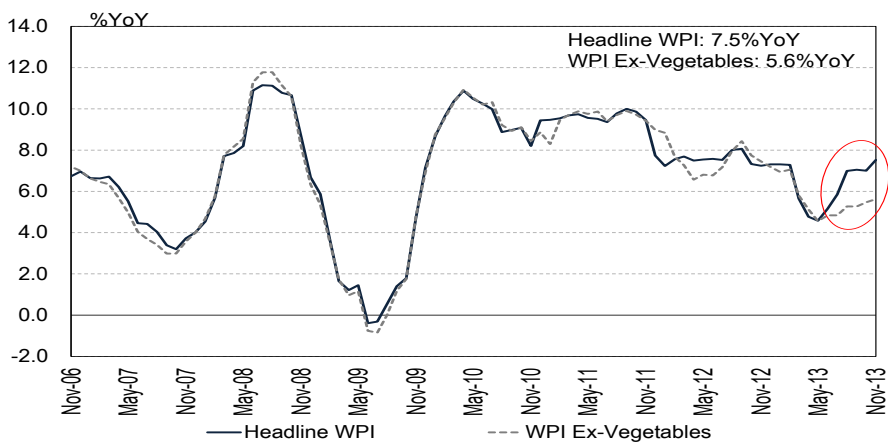
### WPI: VEGETABLES A KEY DRIVER

Headline WPI rose to 7.5%YoY in November. Excluding the surge in Vegetables inflation, WPI would have come in ~180bps lower, at 5.6%YoY.

Wt of Vegetables in WPI: 1.7

(See [Latest WPI Update](#))

Figure 2. Trends in WPI – Headline and Ex-Vegetables (%YoY)



Source: Office of the Economic Advisor, Citi Research

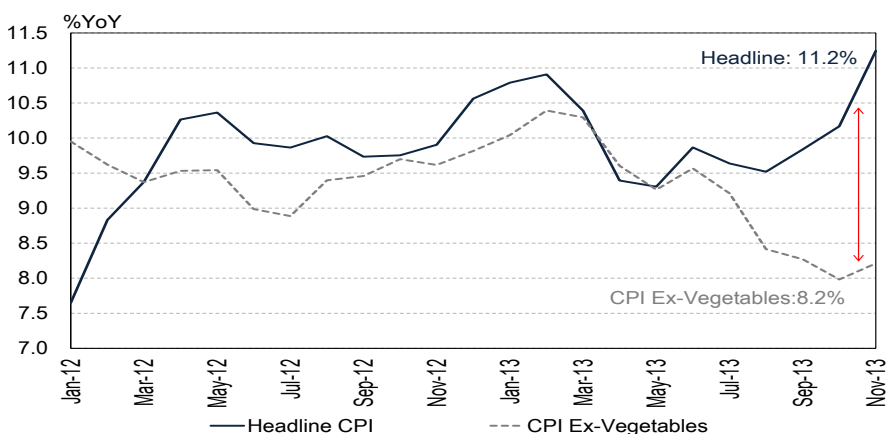
### CPI: HIGHER WEIGHTAGE, HIGHER INFLATION

Headline CPI surged to 11.2%YoY in November. Excluding vegetables, CPI was 300bps lower, at 8.2%YoY.

The larger difference between CPI and CPI ex-vegetables is due to the higher weighting of vegetables in the index. (Wt = 5.44)

(See [Latest CPI Update](#))

Figure 3. Trends in CPI – Headline and Ex-Vegetables (%YoY)



Source: CSO; Citi Research

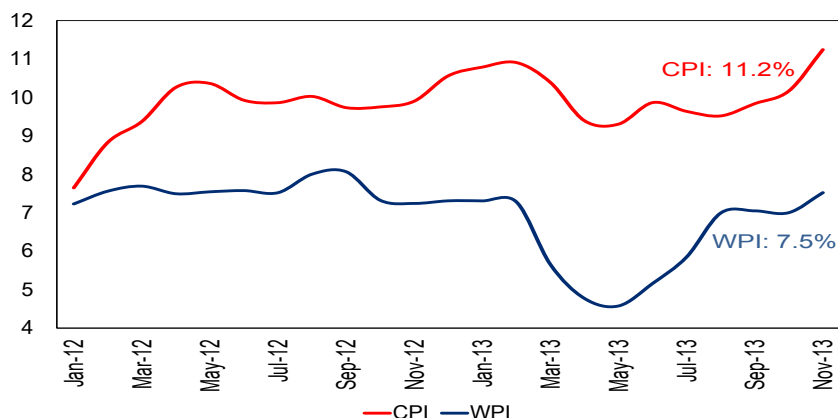
## ..But Other Inflation Components Matter Too

### HEADLINE INFLATION: AT UNCOMFORTABLE LEVELS

Both WPI and CPI have risen substantially in the past few months and are currently above RBI's comfort levels.

The RBI emphasizes that "high inflation at both wholesale and retail levels risks entrenching inflation expectations at unacceptably elevated levels, posing a threat to growth and financial stability"

Figure 4. Trends in Headline Inflation – CPI and WPI (%YoY)



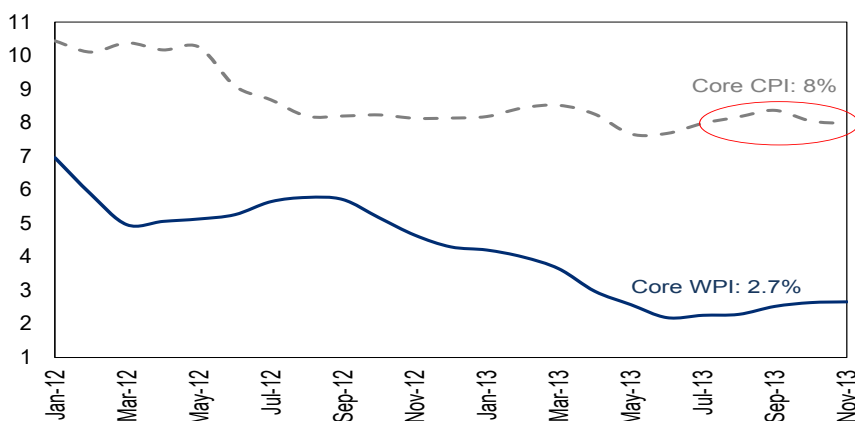
Source: Office of the Economic Advisor, CSO

### CORE INFLATION: STABLE, BUT ELEVATED

Core CPI (ex-food, ex-fuel) stabilizes at 8% but is still high..

The RBI has stated that the "high level of CPI inflation excluding food and fuel leaves no room for complacency"

Figure 5. Trends in Core Inflation – CPI and WPI (%YoY)



Source: Office of the Economic Advisor, CSO

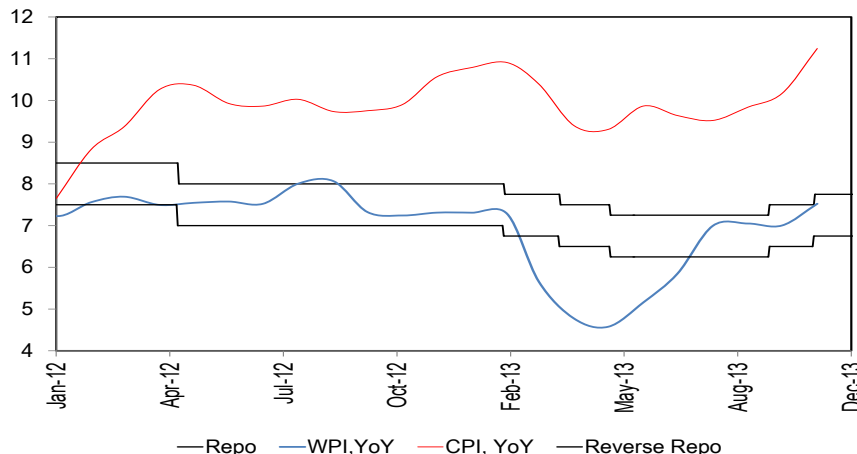
### POLICY STANCE: RBI REMAINS VIGILANT ON INFLATION

While current inflation is high, there is a lot of uncertainty over the short-term path of inflation...

Surges in vegetable prices could be "short-term spikes", which would not then be factored into monetary policy that has "long lags"...

The RBI thus admits that "The policy decision is a close one"... "there is merit in waiting for more data to reduce uncertainty"

Figure 6. Trends in Key Policy Rates and Inflation (%)



Source: RBI, Citi Research

## Interest Rates and Inflation

**Repo Rate: UNCHANGED at 7.75%**

The RBI's lending rate or liquidity injection rate is usually the 'independently varying' policy rate.

**Reverse Repo :UNCHANGED at 6.75%**

This is the liquidity absorption rate and is pegged 100bps below the repo rate to help improve monetary transmission.

**MSF: Unchanged at 8.75%**

100bps corridor over repo.

**CRR: Unchanged at 4%**

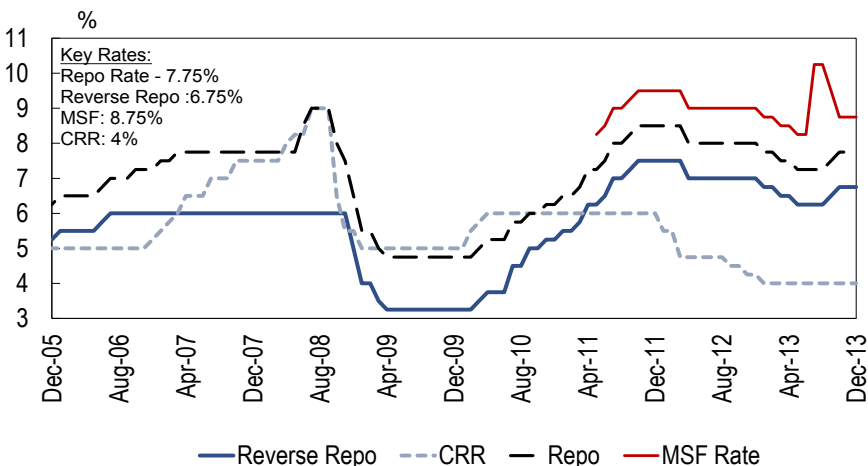
Proportion of deposits required to be held in cash by banks with the RBI.

Figure 7. India – Key Interest and Inflation Rates (%)

Effective Since	Reverse Repo	Repo Rate	CRR	WPI Inflation	CPI Inflation
16-Dec-10	5.25	6.25	6	9.5	9.5
25-Jan-11	5.50 (+0.25)	6.50 (+0.25)	6	9.5	9.3
17-Mar-11	5.75(+0.25)	6.75(+0.25)	6	9.7	8.8
3-May-11	6.25 (+0.50)	7.25(+0.50)	6	9.6	8.7
16-Jun-11	6.50(+0.25)	7.50(+0.25)	6	9.5	8.6
26-Jul-11	7.00(+0.50)	8.00(+0.50)	6	9.4	8.4
16-Sep-11	7.25(+0.25)	8.25(+0.25)	6	10.0	10.1
25-Oct-11	7.5 (+0.25)	8.5(+0.25)	6	9.9	9.4
16-Dec-11	7.5	8.5	6	7.7	6.5
24-Jan-12	7.5	8.5	5.50(-0.5)	6.9	7.6
9-Mar-12	7.5	8.5	4.75(-0.75)	7.7	9.4
17-Mar-12	7.5	8.5	4.75	7.7	9.4
17-Apr-12	7.0 (-0.5)	8.0 (-0.5)	4.75	7.5	10.3
18-Jun-12	7	8	4.75	7.6	9.9
31-Jul-12	7	8	4.75	7.5	9.9
17-Sep-12	7	8	4.5(-0.25)	8.1	9.7
30-Oct-12	7	8	4.25(-0.25)	7.5	9.8
18-Dec-12	7	8	4.25	7.2	9.9
29-Jan-13	6.75 (-0.25)	7.75 (-0.25)	4.00 (-0.25)	7.3	10.8
19-Mar-13	6.50 (-0.25)	7.50 (-0.25)	4	5.7	10.4
3-May-13	6.25 (-0.25)	7.25 (-0.25)	4	4.8	9.4
17-Jun-13	6.25	7.25	4	5.2	9.9
30-Jul-13	6.25	7.25	4	5.8	9.6
20-Sep-13	6.50(+0.25)	7.50(+0.25)	4	7.0	9.8
29-Oct-13	6.75(+0.25)	7.75(+0.25)	4	7.0	10.2
18-Dec-13	6.75	7.75	4	9.52*	11.24*

\*WPI and CPI numbers as of Sep'13; Source: RBI, CSO, Office of the Economic Advisor

Figure 8. Trends in Long-Term Rates (%)



Source: RBI

## Statistical Snapshot

Figure 9. India Macroeconomic Summary FY02 – 15E

Fiscal Year to 31 March	FY02	FY03	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14E	FY15E
<b>National Income Indicators</b>														
Nominal GDP (Rs bn)	23,676	25,500	28,617	32,422	36,934	42,947	49,871	56,301	64,778	77,953	89,749	100,206	112,932	128,743
Nominal GDP (US\$ bn)	493	528	623	720	834	950	1,241	1,224	1,367	1,710	1,866	1,856	1,848	2,066
Per Capita GDP (US\$)	474	500	582	662	754	847	1,090	1,061	1,168	1,442	1,552	1,521	1,471	1,644
<b>Real GDP growth (%)</b>	<b>5.5</b>	<b>4.0</b>	<b>8.1</b>	<b>7.0</b>	<b>9.5</b>	<b>9.6</b>	<b>9.3</b>	<b>6.7</b>	<b>8.6</b>	<b>9.3</b>	<b>6.2</b>	<b>5.0</b>	<b>4.8</b>	<b>5.6</b>
Agriculture growth (%)	6.0	-6.6	9.0	0.2	5.1	4.2	5.8	0.1	0.8	7.9	3.6	1.9	4.8	3.0
Industry growth (%)	2.6	7.2	7.3	9.8	9.7	12.2	9.7	4.4	9.2	9.2	3.5	2.1	1.5	4.4
Services growth (%)	6.9	7.0	8.1	8.1	10.9	10.1	10.3	10.0	10.5	9.8	8.2	7.1	6.3	6.7
<b>By Demand (%YoY)</b>														
Consumption	5.3	2.3	5.4	2.3	8.6	7.9	9.3	7.6	8.2	8.1	8.1	3.9	4.9	6.4
Pvt Consumption	6.0	2.9	5.9	2.1	8.5	8.7	9.2	7.1	7.1	8.6	8.0	4.0	4.5	6.5
Public Consumption	2.3	-0.4	2.6	3.4	8.9	3.8	9.6	10.4	13.9	5.9	8.6	3.9	7.0	6.0
Gross Fixed Capital Formation	7.4	6.8	13.6	20.7	16.2	13.8	16.2	3.5	7.7	14.0	4.4	1.7	2.5	5.5
<b>Cons; Invst, Savings * (%GDP)</b>														
Consumption	78.9	77.2	75.0	70.1	69.2	68.0	67.2	68.6	69.1	67.2	68.0	68.7	69.1	68.8
Gross Capital Formation	22.3	24.6	26.9	32.8	34.7	35.7	38.1	34.3	36.3	37.0	35.4	35.6	36.0	36.0
Gross Domestic Savings	22.6	25.4	28.7	32.4	33.4	34.6	36.8	32.0	33.7	34.0	30.8	30.2	30.5	30.8
<b>Real Indicators (%YoY)</b>														
Commercial vehicle sales	-4.5	40.4	36.2	22.4	10.1	33.3	4.2	-21.4	39.2	27.0	19.5	-1.9	-12.0	5.0
Car sales	3.2	5.3	27.2	17.8	7.7	20.7	12.1	0.3	25.7	29.2	3.9	2.4	-5.0	3.0
Two-wheelers	15.3	15.8	11.3	15.7	13.6	11.5	-7.8	2.7	25.9	25.8	13.9	2.7	5.0	10.0
Diesel consumption	-3.7	0.3	1.2	6.9	1.4	6.7	11.1	8.5	8.9	6.5	5.0	6.8	0.0	4.0
Mobile Tele density	0.6	1.3	3.1	4.8	8.2	14.1	22.0	33.0	48.5	66.8	75.1	79.0	87.9	89.7
<b>Monetary Indicators (% YoY)</b>														
Money supply	16.0	16.1	13.0	14.0	15.9	20.0	22.1	20.5	19.2	16.2	15.8	13.4	17.0	18.0
Inflation – WPI (Avg)	3.6	3.4	5.5	6.5	3.7	6.5	4.8	8.0	3.6	9.6	8.8	7.4	6.5	6
CPI (Avg)	4.3	4.1	3.8	3.9	4.2	6.8	6.2	9.1	12.3	10.5	8.4	10.2	10.0	8.3
Bank credit growth	15.3	23.7	15.3	30.9	37.0	28.1	22.3	17.5	16.9	21.5	17.0	14.1	15.0	15
Deposit growth	14.6	16.1	17.5	13.0	24.0	23.8	22.4	19.9	17.2	15.9	13.5	14.3	13.5	14
<b>Fiscal Indicators (% GDP)</b>														
Centre's fiscal deficit	-6.0	-5.7	-4.3	-3.9	-4.0	-3.3	-2.5	-6.0	-6.5	-4.8	-5.7	-4.9	-5.0	-4.8
State fiscal deficit	-3.6	-3.5	-3.9	-3.4	-2.5	-2.1	-1.4	-2.3	-2.9	-3.2	-2.3	-2.1	-1.9	-1.9
Combined deficit (Centre+State)	-9.6	-9.2	-8.2	-7.2	-6.5	-5.4	-4.0	-8.3	-9.4	-8.0	-8.1	-7.0	-6.9	-6.7
Off Balance Sheet Items					-0.5	-0.9	-0.6	-1.7	-0.2					
Combined liabilities ( dom+ext)	87.2	90.7	90.0	88.8	84.6	79.9	76.1	76.8	75.6	70.2	69.9	70.4	69.3	67.3
<b>External Sector (% YoY)</b>														
Exports (US\$bn)	44.7	53.8	66.3	85.2	105.2	128.9	166.2	189.0	182.4	256.2	309.8	306.6	323.4	355.8
% YoY	-1.6	20.3	23.3	28.5	23.4	22.6	28.9	13.7	-3.5	40.4	20.9	-1.0	5.5	10.0
Imports (US\$bn)	56.3	64.5	80.0	118.9	157.1	190.7	257.6	308.5	300.6	383.5	499.5	502.2	489.7	533.8
%YoY	-2.8	14.5	24.1	48.6	32.1	21.4	35.1	19.8	-2.6	27.6	30.3	0.5	-2.5	9.0
Trade deficit (US\$bn)	-11.6	-10.7	-13.7	-33.7	-51.9	-61.8	-91.5	-119.5	-118.2	-127.3	-189.8	-195.7	-166.2	-178.0
Invisibles (US\$bn)	15.0	17.0	27.8	31.2	42.0	52.2	75.7	91.6	80.0	79.3	111.6	107.5	115.9	122.6
Current Account Deficit (US\$bn)	3.4	6.3	14.1	-2.5	-9.9	-9.6	-15.7	-27.9	-38.2	-48.1	-78.2	-88.2	-50.4	-55.4
% to GDP	0.7	1.2	2.3	-0.3	-1.2	-1.0	-1.3	-2.3	-2.8	-2.8	-4.2	-4.8	-2.7	-2.7
Capital Account (US\$bn)	8.6	10.8	16.7	28.0	25.5	45.2	106.6	6.8	51.6	63.7	67.8	89.3	63.6	75.6
% GDP	1.7	2.1	2.7	3.9	3.1	4.8	8.6	0.6	3.8	3.7	3.6	4.8	3.5	3.3
Forex Assets (excl gold) (US\$bn)	51.0	71.9	106.1	135.1	145.1	191.9	299.1	241.6	252.8	273.7	260.9	264.7	277.9	298.0
Months of imports	10.9	13.4	15.9	13.6	11.1	12.1	13.9	9.4	10.1	8.6	6.3	6.3	6.8	6.7
External Debt (US\$bn)	98.8	104.9	112.7	134.0	139.1	172.4	224.4	224.5	260.9	305.9	345.5	392.1	388.5	403.5
Short Term Debt (US\$bn)	2.7	4.7	4.4	17.7	19.5	28.1	45.7	43.3	52.3	65.0	78.2	96.7	96.8	101.8
<b>Exchange Rate</b>														
US\$/INR - annual avg	48.0	48.3	45.9	45.0	44.3	45.2	40.2	46.0	47.4	45.6	48.1	54.0	61.1	62.3
% depreciation	5.0	0.6	-5.0	-2.0	-1.6	2.0	-11.1	14.4	3.0	-3.8	5.5	12.3	13.1	2.0

\* At current prices.

Source: CSO, RBI, Ministry of Finance, Citi Research estimates

## Appendix A-1

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