

Inflation both at the retail and wholesale level accelerated in May 2016 on the back of rising food prices. While retail inflation was at a 21-month high at 5.76%, wholesale price inflation was at a 19-month high. WPI was up 0.79%, the second consecutive month of increase after 17 consecutive months of decline.

Consumer Price Index (y-o-y Change %)

	May-16
General Index	5.8
Food and beverages	7.2
Food	7.6
Vegetables	10.8
Pulses and products	31.6
Sugar and condiments	14.0
Pan, tobacco and intoxicants	7.8
Clothing & footwear	5.4
Housing	5.4
Fuel & light	2.9
Miscellaneous	4.0

Wholesale Price Index (y-o-y Change %)

	May-16
All Commodities	0.79
Primary articles	4.55
Food articles	7.88
Pulses	35.56
Vegetables	12.94
Potato	60.01
Non-Food Articles	4.48
Fuel & Power	-6.14
Manufactured products	0.91
Sugar	22.3
Beverages, Tobacco & Tobacco products	6.36

Retail inflation rose to 5.8% in May 2016 from 5.5% in April 2016. Retail inflation for the first two months of the year was higher than the target set by RBI for 2016-17. Food inflation, which accounts for around 46% of the index rose to 7.6% in May 2016 from an upwardly revised 6.4% in April 2016, as prices of pulses shot up by 32% and that of vegetables and sugar rose by around 11-12% (over the previous year). Retail food inflation was also at a 21-month high.

Compared to April 2016, the other major heads of inflation were down marginally in May 2016 restraining the rise in overall inflation. Fuel and lights inflation at 2.9% in May 2016 was the lowest in the series (since Jan 2012). Core-CPI inflation (excluding food & beverages and fuel & light) eased to 4.7% in May 2016 from 4.9% in April 2016, remaining lower than headline CPI inflation for the ninth consecutive month.

Prices of pulses have been on the rise for over a year and pulse inflation in May 2016 was the lowest in last eight months. Sugar and confectionery become dearer by around 14% in May 2016, the fourth consecutive month of price rise signaling a reversal in price trend, after registering declines during November 2014 to January 2016.

Wholesale price inflation rose to 0.79% in May 2016 up from 0.34% in April 2016 and -2.2% in the year-ago month. Build-up inflation for the financial year so far stood at 2.34% as compared to build-up rate of 1.08% in the corresponding year-ago period. The rise in prices of pulses, fruits, vegetables, potato and sugar (manufactured products) contributed to the rise in inflation in May 2016.

Primary articles index rose by 4.6% (y-o-y) in May while primary food inflation shot up to 7.9% in May 2016 from 4.2% in previous month and a much lower 2.7% in May 2015. Vegetable prices rose sharply taking inflation in vegetables to 12.94% in May 2016 from 2.2% in April 2016, while in fruits the rise was 3.8% in May 2016 reversing the trend of decline in the preceding 10 months. Inflation in pulses remained steady at around 36%. Prices of egg, meat and fish rose to the highest in almost 2 years recording a 9.75% year-on-year rise in May 2016.

Inflation in manufactured goods rose marginally to 0.9% in May 2016 from 0.7% in the previous month. In this segment, sugar followed by food products and beverages, tobacco and tobacco products recorded sharp year-on-year rise in prices. Inflation in the power and fuel segment continued its downward trend, with inflation in the segment contracting 6.1% in May 2016.

What is driving prices?

Lower rainfall in the last two years and resultant drought in several parts of the country appears to be the major contributing factor for the sharp rise in food inflation.

Inflation in pulses at the retail and wholesale level has been consistently over 30% in the last few months. The huge gap between demand and supply is one of the major reasons for the consistent rise in prices. Poor rainfall in the previous two years and drought in several parts of the country has adversely affected pulses production. In India, pulses are mostly grown as a rain-fed crop with only around 16% of area under irrigation. Production was at 17.15 million tonnes in 2014-15 and 17.06 million tonnes in 2015-16 down from 19.25 million tonnes in 2013-14. Demand for pulses in India is pegged around 23.5 million tonnes, thus creating a shortfall of around 7 million tonnes which would have to be catered through imports. Around a quarter of total demand for pulses in the country is met through imports, however the global supply constraints for pulses is also leading to higher global prices and in turn higher prices for imported pulses in the Indian market.

Rise in fruit prices could be due to unfavourable weather conditions and resultant demand-supply mismatches. Vegetable prices tend to be on the higher side during the summer season due to inadequate storage facilities impacting supply. This year the higher than expected heat destroyed some vegetable crops which may have constrained its supply. Tomato price have risen sharply and the rise in prices has been as much as 100-200% in most cities. Excessive heat (high temperatures) during April and May adversely affected the tomato crop at its flowering stage in key growing belts of North India and Maharashtra leading to severe shortage in supply, while unseasonal rain affected the tomato crop cultivation in the Southern states. Interestingly in Andhra Pradesh, bountiful rains have prompted some farmers to switch to paddy from tomato.

Potato production was hit by the blight disease crop that swept across the potato fields in West Bengal. West Bengal is the second largest potato producing state in the country and accounts for around 25% of country's potato production. Certain portion of the crop also goes into cold storage.

Sugar prices rose due to supply shortages and reduced production from the major sugar producing states Maharashtra and Uttar Pradesh on account of severe drought conditions. Sugar output for the beginning

of the season (October 2015) till April 2016 was 24.6 million tonnes, 11% lower compared to production in the corresponding year-ago period. During the period October 2015-April 2016, the major sugar producing states Maharashtra and Uttar Pradesh recorded drop in sugar output of 19% and 3.4% respectively, while sugar output in Karnataka was 16% down during the same period.

Restricted arrivals from the mills and higher demand from stockists and bulk consumers such as soft-drink and ice-cream makers also contributed to the rise in prices.

Measures adopted to rein in inflation

Pulses

The government is adopting a multi-pronged approach to address the rise in pulse prices. It includes higher imports, building of buffer stock, crackdown on cartels, and curb on futures trade. The government has decided to import pulses to bridge the gap between demand and supply of pulses and also ensure that Food Corporation of India procures more quantity of pulses from market.

The government has ordered import of around 6.5 lakh tonnes of pulses (3 lakh tonnes of green lentil, 2 lakh tonnes of yellow peas, 1 lakh tonne red lentil and 20,000 tonnes each of arhar and urad dal). Government-to-government long-term contracts are being planned to import pulses as these would also play a role in limiting the role of private trades and maintain stability of prices. A high-level committee would visit Myanmar and Mozambique to deliberate and finalise the same. It is also considering leasing land in Mozambique and other African countries to grow pulses through contract farming.

The Ministry has decided to enhance the buffer stock of pulses to 8 lakh tonnes from 1.5 lakh tonnes to check the rise in prices. The buffer stock is being created through domestic procurement as well as through imports. The government is also undertaking efforts to sell larger quantities of pulses at subsidised rate of Rs. 120/kg through government agencies and outlets.

The government has directed Shipping Ministry to keep vigil on pulses being imported into the country (landing at the ports) from shipment to final delivery point to prevent any hoarding. Enforcement agencies have been directed to check cartelization and hoarding of pulses.

SEBI (Securities and Exchange Board of India) suspended futures trading in Chana with immediate effect on 16 June and no new contracts or fresh positions in existing contracts would be allowed. It asked the investors to wind down their existing positions.

Earlier in June, the MSP (Minimum Support Price) for pulses for Kharif season 2016 were hiked and also announced an increase in bonus for pulses grown in the season to incentivize domestic production of pulses.

Vegetables

With respect to veggie prices, government has asked states to keep vigil on prices and ensure that traders are not artificially hiking prices. Efforts to reduce wastage during transportation and handling have also been asked to be taken. Efforts are also on improving the cold storage facilities for vegetables in the country.

Sugar

An export duty of 20% has been imposed on export of raw sugar, white and refined sugar in a measure to boost supply in domestic market and check the rise in prices of sugar. Prices of sugar have risen sharply in the global markets following a delayed harvest in Brazil, the world's largest sugar producer. India is the second largest producer of sugar in the world.

Stock holding limits have been imposed by the government on sugar traders to control prices and hoarding. Production subsidy given to sugar mills in December 2015 was withdrawn in May 2016 in the view of rising prices. The subsidy which was given to aid farmers tide over the liquidity crunch was subject to a condition to export certain quota of sugar and supply of ethanol to local oil marketing companies.