Wholesale and Retail Inflation Rates

What is the issue?

- The Wholesale Price Index (WPI) inflation for October, 2019 has touched a 40-month low while the Retail inflation, a 16-month high.
- The measurement of Inflation in India is done by Wholesale Price Index (WPI) and Consumer Price Index (CPI) or Retail Inflation.

What are WPI and CPI?

- Wholesale Price Index (WPI) tracks inflation at the producer level.
- All transactions at the first point of bulk sale in the domestic market are included.
- Consumer Price Index (CPI) tracks Retail Inflation.
- CPI measures price changes from the perspective of a retail buyer.

What does the data reveal?

- The official data showed that the WPI inflation in the country for October, 2019 grew by just 0.16%. In October 2018, it grew by 5.5%.
- The rate of wholesale inflation has been falling steadily.
- This deceleration in wholesale prices has happened despite a significant jump in wholesale food prices. WPI food inflation rose to 7.6%.
- The spike was essentially led by an almost 40% surge in vegetable prices and a 17% surge in the price of pulses.
- Increases in prices of spices and cereals, too, contributed to increasing wholesale food inflation.
- But what continued to pull down overall wholesale inflation number was the continued “deflation” (i.e., prices falling from one month to the next) in manufactured goods.

How does the WPI inflation trend compare with CPI inflation trend?

- The WPI inflation for October, 2019 has touched a 40-month low.
- The CPI or retail inflation has touched a 16-month high.
- This essentially means that while prices are falling or growing at a marginal rate at the wholesale level.
- But, the trend reverses at the retail consumer level, where prices are growing at a faster clip every successive month.

Why does this happen?

- At one level, it makes no sense why prices would fall or grow at a marginal level at the wholesale level while rising at the retail level.
- But one must consider a couple of issues.
- One is the way this information is reaching us i.e., the WPI and CPI indices.
- Some part of the difference between the wholesale and retail inflation trends is explained by the way these indices are made.
- For instance, food articles have a much higher weight **over 45% in CPI**. Their weight is **less than 30% in WPI**.
- So even a similar spike in prices will show up a much higher impact in the retail inflation index than the wholesale inflation index.
- Similarly, fuel and energy have a much higher weight in WPI inflation.
- Then there are other items such as “services” which have a weight of about 30% that can only be found in retail inflation.
- A spike in these prices obviously bumps up only the retail inflation while leaving the wholesale inflation unaffected.

Has this happened before?

- Yes, it has. Between 2012 and 2015, there was a growing divergence between retail and wholesale inflation indices.
- By October 2015, wholesale inflation was negative i.e., actual prices were declining - while retail inflation was over 7%.
- While raging food inflation was a contributor, the spike in services such as education and medical facilities was the biggest reason for this divergence in 2015.

How does this impact policymaking?

- To some extent, the difference between CPI and WPI inflation is not only understandable but also reasonable.
- After all, the two indices have been made to better under how prices behave between the wholesale and retail levels.
- However, a growing divergence between the two creates a serious worry for all policymakers concerned.
- None more so than the central bankers.
- If the RBI looks at retail inflation (4.6%) and is expected to stay above the 4% mark till March 2020, it would be expected to raise interest rates and bring down inflation.
- But if the RBI were to look at WPI, it would then be expected to cut rates further and quite sharply to raise inflation.
- That’s because such a low inflation rate - as the WPI is showing at present -

is essentially a reflection of a weakening economy.

Source: The Indian Express

