

## Retail Inflation softens to 3.61% y-o-y in Feb'25

### **Key takeaways**

- ❖ India's CPI inflation eased to 3.61% y-o-y in Feb'25 compared to 4.26% in Jan'25 due to deflation in vegetable prices. The inflation print is below median market estimate of 3.90%.
- ❖ Core inflation (Excluding food & fuel) rose to 3.95% in Feb'25.

India's retail (CPI) inflation eased to 3.61% in Feb'25 from 4.26% in Jan'25, supported by easing in food inflation to 3.84% from 5.68% in the previous month.

The moderation in food inflation is attributable to deflation in vegetable prices to -1.07% in Feb'25 from 11.35% in the previous month. Vegetable inflation alone averaged more than 24% y/y in 2024.

Inflation in oil and fat products however, continues as India is a net importer of edible oils due to inadequate domestic production and its contribution to food inflation in February was 35.7%. Prices of fruits also surged by 14.86% while cereal inflation was 6.1%. Fruits and cereals together constitute a weight of 13% in food segment while the weight of vegetables is 6%.

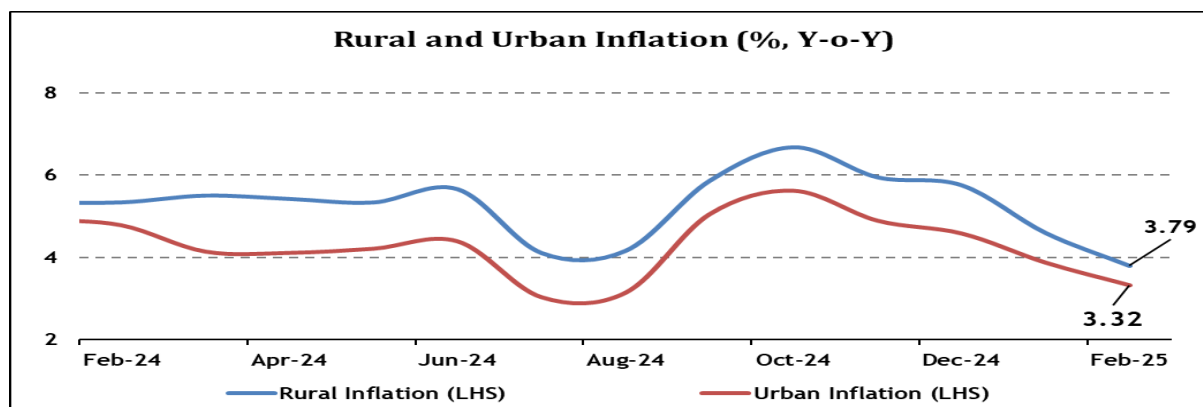
### **Major highlights of February CPI inflation**

- Overall food inflation eased significantly to 3.8% in Feb'25 compared to 5.7% in Jan'25.
- Cereal prices eased to 6.1% in Feb'25 compared to 6.24% in Jan'25.
- Vegetable prices deflated to -1.07%
- Protein inflation eased to 1.74% in Feb'25 compared to 3.46% in Jan'25.
- On the 'fuel & light' front, the disinflation trend continued with a deflation of 1.49% and 1.33% y/y in Jan'25 and Feb'25 respectively. Expectations of additional supply from US and muted global growth prospects due to trade wars and geo-political uncertainties could keep fuel prices under check.
- Core inflation (CPI excl. food and fuel) on the other hand rose to 3.95% in Feb'25 (Prior: 3.67%), driven by Housing inflation (2.91%) and inflation in the Miscellaneous category (4.78%) with a combined weight of 38% in headline retail inflation.
- Rural inflation eased to 3.79% in Feb'25 and urban inflation eased to 3.32% in Feb'25. Higher rural inflation can be attributed to higher weight for food as well as logistical and infrastructural constraints in rural areas compared to urban areas. However, both urban and rural inflation is well below the 4% mark.

With the February inflation data, retail inflation has averaged 3.9% in the first two months of the last quarter of FY25. Assuming CPI inflation March to be 4.2%, retail inflation in Q4 of FY25 will average 3.94% which is well below the initial MPC expectation of 4.8%. For the entire financial year 2024-25, CPI inflation is expected to be in the 4.6-4.7% range depending on March data.

**Table 1: CPI Inflation (% y.o.y)**

CPI Inflation (% y.o.y)					
	Weight	Feb-24	Dec-24	Jan-25	Feb-25
<b>Headline</b>	100	5.09	5.22	4.26	3.61
<b>Food and beverages</b>	46	7.76	7.69	5.68	3.84
Cereals and products	10	7.65	6.51	6.24	6.10
Protein	13	7.03	3.88	3.46	1.74
Fruits	3	4.83	8.60	12.16	14.82
Vegetables	6	30.25	26.56	11.35	-1.07
<b>Fuel and light</b>	7	-0.77	-1.33	-1.49	-1.33
<b>Core (ex Food &amp; Fuel)</b>	47	3.37	3.58	3.67	3.95
Pan, tobacco and intoxicants	2	3.12	2.49	2.30	2.39
Clothing and footwear	7	3.14	2.74	2.68	2.68
Housing	10	2.88	2.71	2.82	2.91
Miscellaneous	28	3.63	4.19	4.35	4.78
of which: Transport & Comm.	9	1.83	2.64	2.76	2.87

**Fig 1: Rural and urban inflation****Table 2: Spread between CPI and 10 yr bond yields**

	CPI (%)	10Yr yield (%)	Spread
United States	2.8	4.3	1.5
United Kingdom	3.0	4.7	1.7
Germany	2.3	2.9	0.6
China	-0.7	1.9	2.6
Russia	10.1	14.8	4.7
Brazil	5.1	14.9	9.8
India	3.6	6.7	3.1
Indonesia	-0.1	6.9	7.0
Japan	4.0	1.5	-2.5

As retail inflation has seen a significant decline and likely to average below 4% in the current quarter a 25 bps repo rate cut is almost certain the April MPC. For the whole of FY26, a cumulative cut of 75 bps is likely given the trajectory of CPI inflation to 4.2%. This should take the repo rate to 5.5% by the end of FY26. Moreover, as shown in Table, India has a higher G-Sec-CPI spread over U.S, UK, Germany, China and Japan which would make it more attractive for foreign portfolio investors to bet on India, supporting a benign yield regime.

The benchmark 10 Yr bond yield is expected to soften to 6.4-6.5% range by the middle of FY26 though yields will stay unchanged at 6.7% levels till the end of March 2025 due to deficit in liquidity and state government bond supplies. A higher real interest rate might also aid savings growth which has been

languishing for some time.

Deposit rates are expected to decline only slowly due to intense competition among banks to mobilize resources so that reasonable credit growth is not constrained. Deposit rates will also be influenced by interest rates on government small savings schemes. Repo linked loans, however, will see an immediate cut in rates.

According to latest RBI data, aggregate bank credit is Rs 180 lakh crore and assuming 40% is repo linked, total repo linked loans are Rs 72 lakh crore. A 75 bps cut in repo rate will reduce interest income of the banking sector by Rs 54000 crore. This might reduce margins of banks as deposit rates are unlikely to adjust fast due to higher credit growth and intense competition.

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