

Inflation likely to rise in April as favourable base effects disappear

Inflation, measured by the officials' preferred gauge Colombo Consumer Price Index (CCPI), falling to a surprisingly lower level of 0.9 percent in the year through March 2024, from 5.9 percent in February, has left many questioning the validity of the numbers. Reason is, it is too good to be true, given that the majority have not felt this impact on their pocketbooks.

However, this is in fact the true inflation in Sri Lanka, as inflation is the pace of price increases and its decline doesn't mean that the sticker prices of the goods and services that one purchases have to necessarily come down. There is the exception of a few, which in fact, came down.

In effect, the prices have continued to increase but at a slower pace of 0.9 percent from the levels seen a year ago or March 2023.

Regarding the March inflation numbers, there were two predominant factors that caused inflation to fall sharply to the current levels - i.e., the favourable base effects of last year and true fall in the prices in some of the sub-categories in the non-food basket.

For instance, not so long ago, the government revised the electricity prices down, followed by fuel prices, in



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line with the cost-reflective pricing. To be exact, the government passed down the benefit of the 6 percent appreciation in the rupee against the dollar seen until then, which had a favourable impact on the energy prices.

If the same would be true couldn't be foretold, as the fuel prices in the global market have firmed up in recent weeks.

A less than a percentage point inflation in March was possible from the higher base effects in March 2023, as the prices rose at the time, taking the CCPI index value to 195.0, rising from 189.5.

But a year later in March 2024, the index value was recorded at 196.7, falling from 200.6 in February 2024, as the index was pushed upwards from the one-time effects of the Value Added Tax increase and supply disruptions caused at the start of the year from adverse weather.

However, based on the point-to-point inflation, inflation cannot continue to fall from the current levels in April 2024, unless the sticker prices of goods come down sharply.

This is because Sri Lanka runs out of the favourable base effects in April 2024, as a year ago, the CCPI index value relapsed to 192.3, from 195.0 in March 2023.

And hence, unless the prices continue to fall significantly on a month-on-month basis from March to April 2024, Sri Lanka is unlikely to see its disinflation below 0.9 percent.

This was what gave the Central Bank the confidence to cut rates by 50 basis points last week, as it said that it expects inflation, despite the sporadic variations, to converge to the target level of between 4 and 6 percent over the medium term and more specifically in the next 12 to 18 months.

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