SHANKAR IAS PARLIAMENT
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Usefulness of WPI

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What is WPI?

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- The wholesale price index is an index that measures and **tracks the changes in the price of goods** in the stages before the retail level.
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- WPI is used as a measure of inflation in some economies.
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- WPI includes three components viz,\n
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  - Manufactured products - 64.2%
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  - Primary articles - 22.6%
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  - Fuel and power - 13.1%
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- Instead of the earlier 2004-05, base year for the WPI will be 2011-12.
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- The number of items covered in the new series of the WPI has increased from 676 to 697.
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What are the issues with WPI?

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- Following the Urjit Patel Committee recommendations, the RBI Act has been amended and flexible inflation targeting (FIT) has been put in place with **CPI inflation as the nominal anchor.**
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- Under the FIT, as the RBI has been mandated to achieve price stability

measured in terms of CPI inflation, **the use of WPI inflation has been completely done away with.**
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- All projections relating to inflation are currently done in terms of CPI.
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- As of now, **WPI is predominantly used for converting GDP/GVA at current prices to the same at constant prices.**
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- In fact, the GDP deflator (often argued as the true indicator of inflation), which is defined as a ratio of GDP at current prices to GDP at constant prices multiplied by 100, closely tracks WPI inflation.
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- The sharp decline in the GDP deflator and the dramatic decline in WPI inflation coincided. This contributed significantly to real GDP growth in India.
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- Also, separate services sector input/output price indices are required to deflate services sector GDP for which WPI is anyway not appropriate.
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- One of the striking features of the new WPI series is that the item level averaging is being **done by using geometric mean**. This is as per international best practice.
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- The geometric mean itself has significantly moderated WPI inflation, besides other factors such as change in the composition of basket.
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- Moderation of WPI as per revised base has **pushed up real GDP considerably** during recent years.
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- Exclusion of excise duty from the computation of WPI has also partly contributed to lower WPI inflation during recent years, which in turn has pushed real GDP up to some extent.
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What could be done?

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- A better way to estimate GDP accurately is to deflate input and output prices through separate indices, popularly known as **double deflation.**
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- When output prices move relatively faster than the input prices, the single deflation method overestimates GDP/GVA and vice versa.

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- **In order to ensure accuracy,** it is high time to discard the single deflation method to estimate GDP/GVA by using WPI as a deflator.

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Source: Business Line

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