RBI FOCUSSED ON GROWTH, SEEN LAGGING ON INFLATION FIGHT

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Reserve Bank of India is concerned that Russia's invasion of Ukraine is damaging the global economy

Inflation is picking up in India, but the country's central bank is likely to maintain its loose policy even as its global peers raise rates, potentially forcing it to play catch-up aggressively later, economists and analysts say.

This view represents a shift in expectations, as market participants say the Reserve Bank of India is concerned that Russia's invasion of Ukraine is damaging the global economy and India's recovery prospects, not just boosting prices.

A Reuters poll in early February found just over half of forecasters expecting the RBI to raise rates at its April meeting, but the war launched three weeks later has upended those predictions.

RBI watchers now expect the bank to stand pat on April 8, even though inflation has broken above the 6% upper end of the bank's target band for two months.

Saugata Bhattacharya, chief economist at Axis Bank, who had earlier expected the RBI to raise its reverse-repurchase rate next week, now says global uncertainties mean that "it makes sense to remain at a status quo."

Supporting such expectations, RBI Governor Shakikanta Das recently warned against a "premature demand compression through monetary policy".

Deputy Governor Michael Patra said India's growth was as weak as in 2013, when a U.S. policy shift sent capital gushing out of emerging markets. "The recent reverberations of war have in fact, tilted the balance of risks downwards" for the economy, he said.

But economists warn inflation could spin out of control, hurting investors and savers alike - and most market participants say the RBI is already behind the curve on tackling inflation.

STOKING RISK OF OVERHEATING

Economists expect the RBI to raise its retail-inflation projection for the fiscal year starting on Friday by 50 to 80 basis points from the current 4.5%.

Upward price pressure is expected to continue as the war and resulting economic sanctions on Moscow send prices soaring for the grain, energy and other exports that Russia and Ukraine provide.

"In the aftermath of the Russia-Ukraine war, the probability that higher-than-expected inflation will persist has increased. The longer we wait to address that, the faster that we may have to play catch-up with it eventually," said Churchil Bhatt, executive vice president of debt investments at Kotak Life Insurance.

Rising asset prices could feed through to demand-side inflation, while savers are being hurt as

their returns lag behind inflation, said Rupa Rege Nitsure, chief economist at L&T Financial Services.

"By keeping interest rates artificially low, the chances of more aggressive tightening at a later stage have gone up significantly," she said.

Abhay Gupta, emerging Asia fixed income and forex strategist at BofA Securities, said the RBI must "be vigilant for broader inflationary pressures."

"Higher uncertainty would reduce room for error and markets would have to price in higher chances of a policy mistake," he said. Risks of eventual economic overheating suggest market interest rates must rise while the rupee should weaken, he said.

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