A forced hike

Here’s why you should binge-watch Damaged, India’s first show about female serial killer

The decision of the Monetary Policy Committee (MPC) of the RBI to raise its benchmark repo rate by 25 basis points to 6.25 per cent — the first such hike in well over over four years — may not have been anticipated by many economists and analysts who had bet on the central bank’s interest rate setting committee maintaining status quo. What has driven the MPC to raise rates is the upside risk to inflation flagged off earlier in April — in the form of higher crude oil prices, a rise in inflation expectations of households reflected in the May round of the central bank’s survey, the staggered impact of HRA revisions and the impact of the revision in MSP for kharif crops — all of which could mean a CPI inflation of above 4 per cent in 2018-19, well above the medium term headline inflation target of plus or minus 4 per cent. The MPC’s hand was also forced by global financial market developments, which, it says, have emerged as an important source of uncertainty. That is obviously a reference to the outflows most emerging markets are facing, the pressure on their currencies, a strong US dollar and rising interest rates.

Emerging market peers such as Indonesia, Philippines, Turkey and Argentina have already raised rates with indications of a further tightening depending on the US Federal Reserve which is meeting next week in the backdrop of growing expectations of a few more rate hikes in the US. India, too, has seen foreign portfolio investors pulling out $4.4 billion in the first five months of this year, leading to the weakening of the rupee which is now one of the worst performing currencies — having fallen over 6 per cent against the US dollar this year. The Indian stock markets appear to have interpreted the MPC’s decision to keep its neutral policy stance as a positive signal — with the Sensex up 276 points on Wednesday, though RBI Governor Urjit Patel has said that the central bank was keeping all options open. In a way, today’s rate hike may not make much of a difference considering that some of the bigger banks had already raised their lending and deposit rates while bond yields too had moved up. The other positive is the improvement in loan offtake and capacity utilisation and the MPC’s assessment of investment activity continuing to remain robust promoting it to retain GDP growth projections at 7.4 per cent for FY 19 — reinforcing recent data which pointed to a recovery underway and the fact that the economy may have shrugged off the disruption caused by demonetisation and GST.

What the government should do now is to heed the RBI rate action as a warning and desist from politically motivated MSP rate increases or fiscal adventurism. Compared to many other emerging market economies, despite a widening current account deficit, India still stands out given its relatively lower inflation and growth. Surely, the government with under a year to go in office would not want to risk jeopardising growth prospects.

END