

# DON'T SURRENDER IRAN CUSHION AGAINST AN OIL SHOCK

Relevant for: International Relations | Topic: India - Middle East

GDP growth of 8.2% in Q1 2018-19 has added more strength and credibility to the ongoing economic recovery after two back to back disruptions from demonetisation and the Goods and Services Tax. A good monsoon will make sure that even agriculture will reap the fruits of this growth. However, it is important that the policy makers do not lose sight of the growing economic headwinds from external factors.

Rising oil prices are perhaps the biggest challenge on this front. A mix of factors, such as falling inventories in the US, fall in oil production in Venezuela and Trump administration's Iran sanctions could lead to a spike in oil prices. Combined with an environment in which the rupee has been depreciating, this will significantly increase import costs for India. Rising oil prices have direct bearings on inflation and fiscal indicators in the Indian economy. Strong demand in a growing economy can add to inflationary pressures from rising oil prices. Three major state elections scheduled later this year and the general elections next year will raise the political costs of adhering to fiscal discipline in the event of rising pressures on the oil front. Rising inflation could also lead to further rate hikes by the Reserve Bank of India, which is committed to keeping inflation under control by rising policy rates under the new monetary policy framework.

To be sure, oil shocks to the Indian economy are not new. Unless the country finds viable and sustainable replacements for its energy needs, international oil price movements will continue to be an important fault line in India's political economy. This is not a goal which can be achieved in the short-run.

But India should also look at ways to cushion itself against the impact of oil price shocks in the short-term. Donald Trump has recently threatened that the US will quit the World Trade Organization. Such statements, even if they are mere threats, are clear indication that the US's own interests are more important to it than adhering to well-established rules of the game in the global economy. India should think seriously about defying the US sanctions on oil imports from Iran.

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