

India Economic Flash

RBI keep rates on hold, further policy tightening looks less likely

In line with expectations, the Reserve Bank of India held its benchmark repo rate unchanged at 8.0% today and signaled a probable end to further policy tightening in the near term. At its previous meeting on January 28th, RBI had surprised with a 25 bps rate hike given concern over high and stick inflation. Today's policy decision was based on the recent sizable moderation in headline inflation as well as a more benign near term CPI inflation outlook led by a high base effect. Furthermore, a wait-and-watch approach should allow the previous 3 rate hikes (cumulative 75 bps since last September) to fully transmit through the economy. The central bank warned, however, that core CPI remains elevated and that uncertainty surrounding the nature of monsoon rains, adjustments to minimum support prices for agriculture, fiscal outlook and international geo-political developments pose medium term upside risks to inflation. Against this background, **we expect RBI to stay on hold going forward until it draws comfort from a sustainable decline in core CPI inflation and greater clarity emerges on the medium term inflation trajectory.**

However, it should also be noted that **a fractured mandate at upcoming elections on April 7th poses a risk to India's growth-inflation balance.** Regardless of which major political party comes to power, we believe that a strong and stable mandate is necessary to expedite the revival of stalled infrastructure projects, implement taxation reforms such as the goods and services tax and the direct tax code and keep fiscal consolidation on track. On the flipside, a fragmented coalition of regional parties with conflicting policy agendas could impair ongoing economic recovery and in turn increase India's credit risk. (See our [recent note](#) on India's upcoming elections).

Chart-1

RBI keeps interest rates on hold led by moderating inflation pressures and a subdued growth outlook

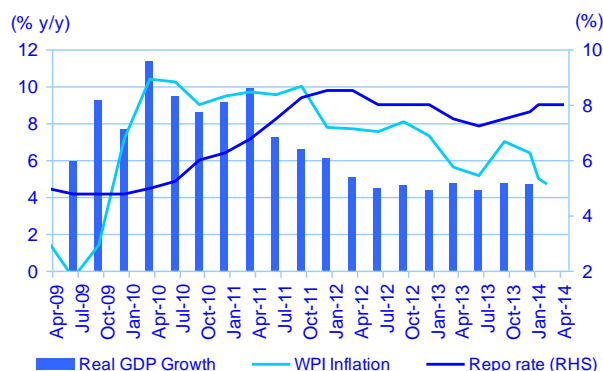
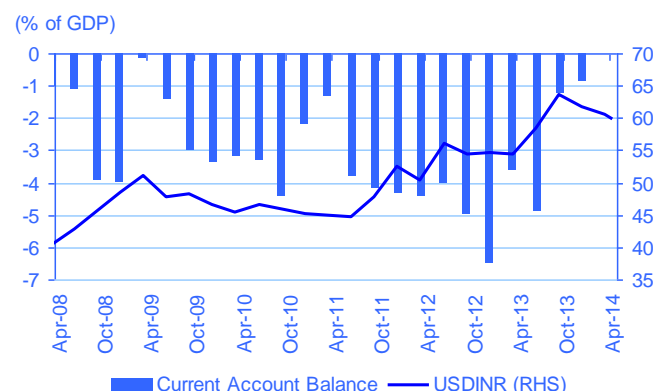


Chart-2

A stabilizing rupee bodes well to keep imported price inflation in check going forward



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