# Interest Rates Unchanged - Monetary Policy Review

## Why in news?

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The Reserve Bank of India decided to leave interest rates unchanged in the recent monetary policy review.

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## How is the inflation scenario?

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- The RBI now expects retail inflation to stay below the legally mandated 4% mark for the coming 12 months.
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- Resultantly, RBI has sharply cut its inflation forecast for the second half of the current fiscal year - from 3.9-4.5% to 2.7-3.2%.
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- For the first half of the next financial year, it has been revised from around 4.8% to 3.8-4.2%.
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- The RBI's own household survey of inflation has shown a 40 basis point downward movement over the last round.
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- Retail inflation is expected to fall further. E.g. the November data is estimated at 3%
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- The dip in retail inflation is largely a result of the unexpected deflation in food items such as pulses, vegetables and sugar.
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## What is RBI's rationale?

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- Over the policy reviews, RBI has maintained its single-minded focus on targeting only retail inflation and inflation expectations.

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- But despite a favourable inflation trajectory, the monetary policy committee did not cut the repo rates.
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- An analysis of the components of retail inflation explains this.
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- Evidently, the headline retail inflation, mapped by year-on-year changes in the consumer price index, has decelerated sharply.
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- This is primarily driven by the sharp decline in food and fuel prices.
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- However, the non-food, non-fuel retail inflation has actually risen to over 6%.
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- Moreover, the RBI is worried about
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i. the residual impact of minimum support prices
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ii. possible fiscal slippages
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iii. a sudden increase in oil prices if the OPEC countries decides on production cuts
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- So the RBI wants to pause and decide only after ensuring the decline in inflation is of a more robust nature.
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## What is RBI's stance on growth?

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- The Q2FY19 gross domestic product (GDP) data undershot the RBI's projection.
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- However, the RBI maintains its annual forecast of 7.4% GDP growth in the current financial year.
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- Economic growth has suffered in most of the advanced world.
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- Both the US and the euro area have slowed even as Japan has contracted in the past quarter.
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- Moreover, several emerging economies such as China and Russia, too, have decelerated.
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- Yet, the RBI sounded relatively confident about the domestic economy.
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- It highlighted the increased capacity utilisation in manufacturing sector, improving credit offtake and lower crude oil prices that may boost consumption.
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- Notably, capacity utilisation in manufacturing sector rose to 76.1% in Q2, higher than the long-term average of 74.9%.
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- Also, industrial firms reported an improvement in the demand outlook for Q4.
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- But besides these, RBI has once again raised a cautionary signal to governments, both at the Centre and in the States.
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- Fiscal slippages risk impacting the inflation outlook, heightening market volatility and crowding out private investment.
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- Instead, this may be an opportune time to bolster macroeconomic fundamentals through fiscal prudence.
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**Source: Business Standard, The Hindu**

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