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Will Fuel Price Hike, Rupee Hold Reserve Bank from Cutting Rate?

By Sumit Sharma | Published: 18th May 2015 06:00 AM Last Updated: 18th May 2015 04:58 AM

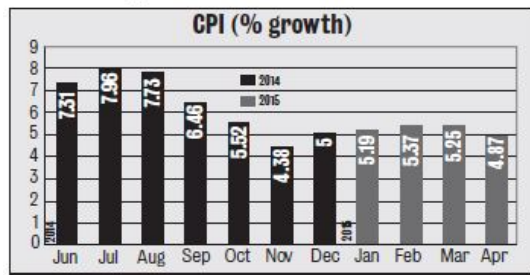
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MUMBAI:As the government made hefty increases in price of diesel and petrol for the second time in two weeks, a key issue is its potential impact on inflation, especially since the RBI now uses inflation data as the bedrock to decide on interest rates changes.

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Yet, diesel and petrol prices are not the only elements that may influence the Reserve Bank of India on its next monetary policy review on June 2.

A week before the previous policy of April 7, external members at RBI's technical advisory committee on monetary policy said were concerned at slowing industrial growth, and four of the seven recommended that RBI should cut repo rate. The governor then ruled for status quo. They also

expressed concern at exports becoming noncompetitive to euro denominated economies and the dollar gaining.

For April data, Consumer Price Index slowed to 4.87% rise y-o-y from 5.25% in March. The Wholesale Price Index fell to 2.65% y-o-y compared with a decline of 2.33% in March. Index of Industrial Production (IIP) too slowed to 2.1 per cent in March.

Madan Sabnavis, chief economist at CARE Ratings said CPI Inflation will continue to be RBI's main focus for deciding on repo rate changes.

"CPI inflation is ruling below 6 per cent-target rate set by RBI for months," said Sabnavis. "Year-on-year CPI is unlikely to get elevated since the crude same time last year was ruling around \$120 a barrel. Last week's increase in petrol, diesel prices are unlikely to make a perceptible impact on inflation."

The economy is crawling, and the rupee unlikely to be an overriding factor and with the US Federal Reserve indicating a decision on raising its rates unlikely soon, the RBI may go in for 25 bps repo rate cut from the 7.5% at present. After a June rate cut, RBI may go in for another similar cut later in the year, he said.

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further. Dhananjay Sinha, head of institutional research Emkay Global Financial Services says RBI may follow an accommodative policy approach. It will have to keep one eye on the rupee and won't like any of its actions to accentuate the depreciation.

actions will be gradual," said Sinha. "Earlier cuts have not been transmitted into lower rates e extent."

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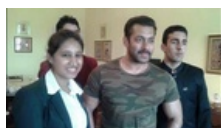
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