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MPC Meet: Reserve Bank of India raises repo rate by a smaller 35 bps amid moderating inflation pressure

Diksha Tripathy, Dec 07, 2022.

The Reserve Bank of India-led rate-setting panel on Wednesday raised the country's policy rate by a modest 35 basis points in its last policy review of the calendar year amid moderating inflation pressure.

The Monetary Policy Committee (MPC) increased the repo rate, or the key rate at which the RBI lends short-term funds to commercial banks, to 6.25% from 5.9%. With this hike, the RBI has broken the 50-basis-point-hike trend that it opted for in each of the last three policy meetings. The key rate has now been raised by 225 (190 + 35) bps since May by the panel. The panel also decided to remain focused on withdrawal of accommodative stance.

The more modest RBI rate hike also coincides with indications that the Federal Reserve will shift to smaller rate increases at its policy meeting this month, as the US monetary authority too have to perk up growth while it probably has done a lot with 375 bps of rate hikes to control inflation.

The policymakers opted for a smaller rate increase to fuel growth amid bets of easing inflation pressure. Retail inflation, which is one of the key factors taken into consideration by RBI while deciding the monetary policy, moderated in October to a three-month low. It nonetheless remained above RBI's tolerance band of 2-6% for the 10th consecutive month.

"The moderation in rate hike is on expected lines. With CPI inflation likely to moderate further supported by base effect and the relief provided by moderating global commodity prices, RBI could take a breather," Rajani Sinha, chief economist at CareEdge said. "However, core inflation and household inflationary expectations still remain high , hence the Central Bank would remain vigilant on the inflation front."

As central banks are perhaps preparing for a potential low inflation regime, global growth slowdown has emerged as a new pain point for them to act on policies. India's economic growth for the July-September quarter slowed to 6.3% from 8.4% a year earlier, and 13.5% in the previous quarter, owing to slower growth of the manufacturing and mining sectors.

The moderate pace of growth has raised RBI's concern and it largely shifted the focus from inflation to growth.

"Central banks across the world are facing the challenge of walking the tightrope between growth and inflation," HDFC Bank's Principal Economist Sakshi Gupta had said. "For the RBI, given the fact inflation is beginning to show signs of moderation and growth continues to broadly hold up, the trade off has been less pressing as compared to the US Fed where inflation is almost f ..

India is likely close to the end of its rate hiking cycle and the front loaded rate hikes are likely to keep inflation and its second round impact under control as we move into 2023, Gupta had stated.

In addition, the impact of past rate hikes and liquidity tightening measures have yet to be seen. Thus, going overboard with the monetary policy could hurt growth recovery.