India will need to keep raising policy interest rate: IMF

The Reserve Bank of India will need to continue raising its policy interest rate given the sticky nature of inflation, the International Monetary Fund said on Thursday.

"The ingrained nature of inflation and inflation expectations mean that reducing inflation — even over a protracted horizon — will require significant increases in policy rates, which will weigh on growth," the IMF said in a report.

"Should high inflation expectations persist and inflation remain sticky, a more front-loaded path of interest rate increases may be needed," the IMF said.

RBI Governor Raghuram Rajan, a former IMF chief economist, has raised the key repo rate by 75 basis points to 8.00 percent since becoming head of India`s central bank in September. He has made consumer prices its key inflation barometer, a shift away from using wholesale price inflation.

The latest 25 basis point increase, which surprised the market, was on January 28. Rajan, a former IMF chief economist, said in his last policy review that further rate hikes were not anticipated if the inflation trajectory remained subdued.

The consumer price index touched a two-year low in January at 8.79 percent as food prices cooled but was still much higher than the wholesale price index of 5.05 percent, an eight-month low.

The IMF expects India`s consumer price index to remain near double digits well into next year driven by food prices.

It endorsed giving more emphasis to consumer prices for making policy decisions.

"Headline CPI should provide the principal nominal anchor for monetary policy, as food and fuel price shocks propagate rapidly into core inflation, and inflation expectations and wage formation are closely linked to CPI inflation," the IMF said.

The IMF expects India`s economy to grow at 4.6 percent in the current fiscal year ending in March, picking up to 5.4 percent in the fiscal year that starts in April, which is in line with the RBI`s expectations.

(Zee News)