

RBI may hike interest rates further by at least 50 bps by December 2022

Reserve Bank of India (RBI) hiked the policy repo rate by 40 basis points to 4.4% on May 4, 2022 in response to rising inflation. This is the first policy repo rate hike since August 2018. The central bank also hiked Cash Reserve Ratio (CRR) by 50 basis points, which would absorb banking liquidity to the extent of Rs. 87,000 crore.

The policy rate hike by RBI is aimed at stopping capital outflow. RBI has already signalled that it would be gradually unwinding its accommodative policy stance by absorbing excess liquidity of up to Rs. 6 lakh crore in the banking system.

Impact on trade and industry

The hike in interest rate is expected to increase the cost of borrowing for businesses and consumers as already the 10-year government bond yield rose to 7.4% from less than 7.1%. On the other hand, it may help in retaining foreign capital. If inflation is allowed to get unchecked for long it can penetrate into labour wages expectation which would lead to higher labour cost.

This policy rate hike is supposed to help in managing future expectation regarding inflation and thus managing labour cost. The hike in policy rate may prevent further depreciation of Indian rupee, thereby providing some comfort in servicing the widening trade deficit and also keeping in check the imported cost of crude oil and edible oil. Preventing further depreciation of Indian rupee can make our export less price competitive but we do not expect it to have much impact on our exports considering the current geo-political scenario.

Even though this policy rate hike may hinder the speed of the economic recovery but we believe it's a very crucial step towards maintaining long term macroeconomic stability. We should expect further rate hike gradually atleast up to the pre-covid level in coming months. With CPI inflation above 6% level, we expect RBI to hike policy repo rate by at least another 50 basis points to prevent the real interest rate from going below the negative territory.

Notifications

Press Information Bureau

India sees the emergence of the 100th unicorn. Rise of 14 unicorns in last 14 months

<https://www.pib.gov.in/PressReleasePage.aspx?PRID=1823347>

India's Services exports set a new record of USD 254.4 Billion in FY 2021-22

<https://www.pib.gov.in/PressReleasePage.aspx?PRID=1822664>

New financial year begins with record exports of USD 38.19 billion in April

<https://www.pib.gov.in/PressReleasePage.aspx?PRID=1822318>

CBIC

Exchange rate notification

<https://www.cbic.gov.in/resources//htdocs-cbec/customs/cs-act/notifications/notfns-2022/cs-nt2022/csnt40-2022.pdf>

RBI

RBI hints at unwinding accommodative stances, hikes Policy rate and CRR to tackle rising inflation

Governor's statement- https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=53651

Change in CRR - <https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=12313&Mode=0>

Change in Bank rate - <https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=12312&Mode=0>

