Prudence prevails

Bottom Line: That inflation is a concern for policymakers is reassuring for consumers and savers.

Highlights:

1. The Finance Ministry has put to rest all speculation about the inflation targeting framework that will guide the interest rate decisions of the RBI's Monetary Policy Committee over the five-year period starting on April 1.
2. In a terse notification, the Department of Economic Affairs announced that the inflation target for the quinquennium ending on March 31, 2026, will be 4%, with an upper tolerance level of 6% and a lower tolerance level of 2%.
3. The government's announcement is a welcome step in reiterating that inflation targeting remains the centrepiece of the monetary policy framework and signals that the fiscal and monetary authorities are in lockstep in ensuring the primacy of price stability as the bedrock for all macro-economic development.
4. This is particularly apposite at a time when inflation pressures are mounting in an economy that is still struggling to regain its footing from the devastating contraction in the just-ended fiscal year when the COVID-19 pandemic and the drastic measures to curb its spread resulted in widespread precarity.
5. The latest Consumer Price Index data show retail inflation accelerated by almost 100 basis points to a three-month high of 5.03% in February, with food and fuel costs continuing to remain volatile.
6. Also, with the prices of multiple raw materials on an upward trajectory, an IHS Markit India Business Outlook survey last month showed companies were planning to raise selling prices over the coming 12 months to cope with rising costs.

Seeking a balance for stable economic growth

1. The RBI has in recent months maintained an unwavering focus on emphasising the need to retain the flexible inflation targeting framework.
2. Observing that there had been a steady decline in trend inflation to a 4.1%-4.3% band since 2014, they said a target far lower than the trend ran the risk of imparting a 'deflationary bias' that would dampen economic momentum,

while a goal much above the trend could engender expansionary monetary conditions that would likely lead to inflation shocks.

3. And in February, the RBI's researchers authoring its Report on Currency and Finance — themed 'Reviewing the Monetary Policy Framework' — made clear that the framework had served the economy well, attested by a decline in inflation volatility and more credible anchoring of inflation expectations.
4. That the government's economic officials have heeded these calls will certainly reassure investors and savers that inflation remains a central concern for all policymakers.