TACKLING INFLATION SHOULD BE THE IMMEDIATE FOCUS: PMEAC

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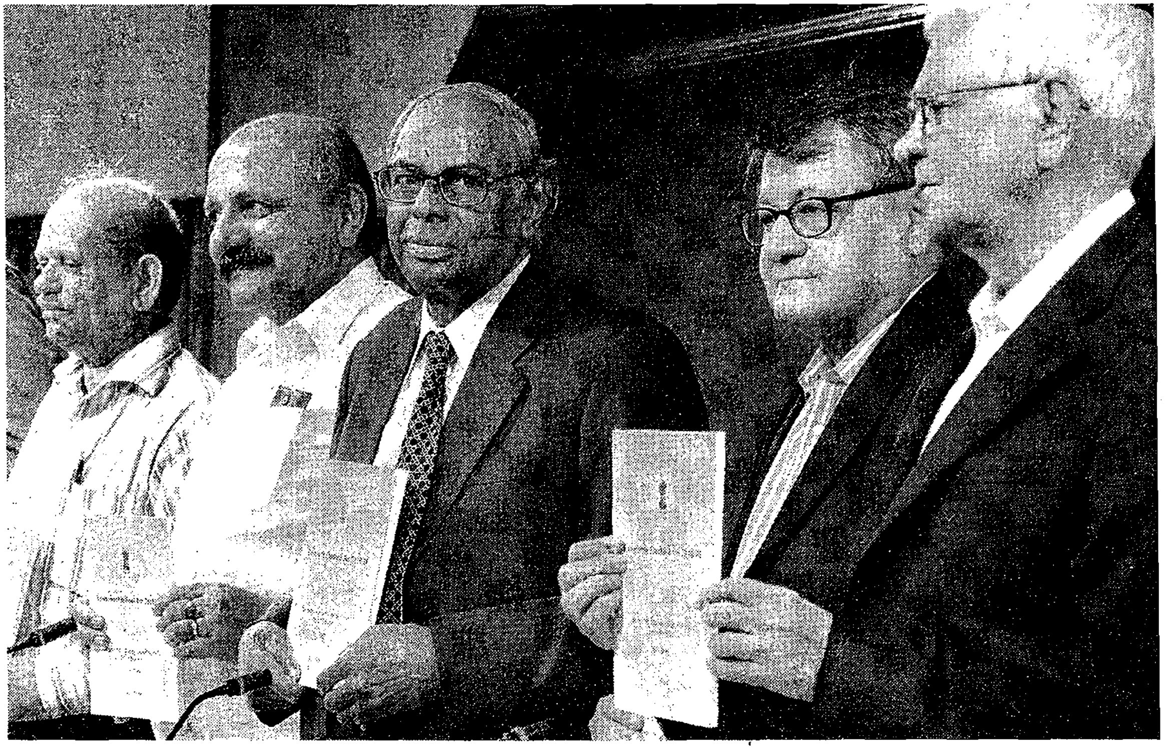

(From left) **Prime Minister's Economic Advisory Council Members M Govinda Rao and Saumitra Chaudhuri, Chairman C Rangarajan, Members Suman K Bery and V S Vyas at the release of the 'Review of the Economy 2010-11', in New Delhi on Friday.** PHOTO: SANJAY K SHARMA

The Prime Minister's Economic Advisory Council (PMEAC) today said the Reserve Bank of India (RBI) should undertake further monetary measures and the government should initiate steps to increase food grain availability to tame inflation.

Inflation is a major cause for concern in an otherwise healthy economic environment. Former RBI Governor C Rangarajan said containing inflation should be the immediate focus for the government, while targeting an improvement in farm productivity and closing the infrastructure gap in the medium term.

The Council, headed by Rangarajan, revised the growth forecast from the 8.2 per cent projected earlier to 8.5 per cent, driven by a 4.5 per cent growth in agricultural output and 9.2 per cent expansion in the non-farm sector comprising industry and services.

The 86-page document released today estimated the industrial sector to grow by 9.6 per cent this year and inch up to 10.3 per cent next year. It said manufacturing and the index of industrial production are likely to post 10 per cent growth this year. Similarly, services are poised to grow by 9 per cent this year, and by 9.6 per cent in 2011-12, as most sectors were witnessing higher demand.

Rangarajan told a press conference that PMEAC's optimism on agriculture stemmed from the fact that kharif sowing would be strong on the back of normal monsoon forecast by the met department. "The better seed and fertilizer availability and the construction of a large number of water harvesting structures through MNREGA (Mahatma Gandhi National Rural Employment Guarantee Act) lend strength to these expectations," the panel said in the Economic Outlook for 2010-11.

Normal monsoons would also augur well for inflationary expectations. Inflation, based on the wholesale price index, has remained in the double-digit zone for the last five months, and along with softening of food prices and the base effect, it is expected to moderate to 7-8 per cent by the end of 2010 and reach around 6.5 per cent by March 2011.

Though food prices have already started to soften, Rangarajan said it was essential for the government to ensure stocks were released in a manner where there is a dampening effect on prices.

Besides, he said it was essential that RBI, which is scheduled to present its first quarter review of the Annual Policy Statement on Tuesday, maintains a bias towards further tightening as "inflation rates are more than twice the comfort zone". Since March, RBI has already increased rates thrice by a quarter-point each, in what governor D Subbarao has described as baby steps.

"Strong monetary policy action is required... There could be a series of small steps (by the central bank) rather than one strong step," Rangarajan said.

"As far as monetary policy is concerned, controlling inflation at this particular moment may become more important and the emphasis could be more on that," he added.

Terming the present bout of liquidity tightness as temporary, Rangarajan said the RBI can always take steps to ensure adequate cash was available in the system.

PMEAC also said capital flows would remain strong and are expected to rise by 36 per cent to $73 billion this year, compared to $53.6 billion last year. This is despite portfolio flows shrinking to around $25 billion this year, compared to $32.4 billion last year — a rise of around 23 per cent. Net foreign direct inflows are projected to increase by over 50 per cent to $30 billion from 19.7 billion last year.

Exports could rise by 18.6 per cent to $216.1 billion this year, while imports could rise by around 18.1 per cent to $353.9 billion. Invisibles, too, are expected to rise by around 6.3 per cent to $96 billion. "This (capital flows) would be adequate to finance the large current account deficit and leave a modest $31 billion (2 per cent of GDP) to be absorbed in foreign exchange reserves," the report said.

However, it said at these levels capital flows were unlikely to pose problems in exchange rate management.