INTERVIEW: C RANGARAJAN

CHAIRMAN, PRIME MINISTER'S ECONOMIC ADVISORY COUNCIL

Tweak trade policy to trim current a/c deficit

The central bank should increase the pace of monetary tightening as demand needs to be controlled, says **C Rangarajan**, *chairman, Prime Minister's Economic Advisory Council. Speaking to* FE*'s* **Anto Antony** *after unveiling the economic outlook for 2010-11 here on Friday, he said capital inflows are expected to be strong not only in the current year, but the next year also. Excerpts from the interview:*

What steps are required to be taken to target the double digit inflation? As the monetary policy tightening will get transmitted through the system only with a time lag, shouldn't the policymakers resort to fiscal tightening?

The headline inflation has been in double digit territory since February. It is more than double of our comfort levels. These numbers are expected to fall below 10% by September. We believe that a three-pronged strategy should be taken to target this high inflation rate. To start with, more food grains should be released from the buffer stocks in a timely manner. Continuation of the zero import duty regime on food items like sugar and wheat will also help in keeping the prices in check.

Most importantly, the central bank should continue with the tightening of the monetary policy regime. We already have seen some "baby steps" from central bank in this direction. The pace of this tightening should be increased as the demand needs to be controlled.

Fiscal policy tightening can be done only in the budget. It is an annual process. But monetary policy formulation is something that can be done on a continuous basis.

Clouds of gloom are gathering again on the global economic horizon as some of the Spanish banks failed the stress test. Does the Outlook of the council factor in chances of another dip in the global economy?

There are still some uncertainties in the global economic front. We are expecting a moderate recovery in the European region. We have not factored in a V shaped recovery in global economic growth while predicting the 8.5% growth for the Indian economy in the current year. At the same time, we were not expecting a second dip in the global economy either.

> Inflation is more than double of our comfort levels...The central bank should continue with the tightening of the monetary policy regime. We already have seen some baby steps from RBI in this direction. The pace of this tightening should be increased as the demand needs to be controlled

Our current account deficit is one of the highest in the region. Wouldn't the new uncertainties trigger risk aversion in the global financial markets making it difficult for us to fund this deficit from inflows into the financial markets?

Due to robust foreign capital inflows we are not expecting any problems in financing the current account deficit. The inflows are expected to be strong not only in the current year, but in next year also. A slow economic recovery in other parts of the world will make India a more attractive destination for funds currently lying idle. We should also be looking at reworking the trade policies to keep the current account deficit at healthy levels.

With fiscal deficit remaining as a matter of concern, does the council advise a complete roll back in the fiscal stimulus measures?

Fiscal deficit in the current year is expected to be the targeted 5.5% or even a tad lower. According to the borrowing targets announced by the states so far the state level deficit will amount to 3.4% of the national GDP. We are expecting the government to stick to the fiscal consolidation road map already announced at time of the budget.

The council does not recommend any immediate roll back of the fiscal stimulus measures. As you remember the budget presented earlier this year had announced some partial roll back in the stimulus measures. As the Goods and Services Tax comes into effect by the next financial year further changes will come into effect.