

Anti-Inflationary Measures

5.26 High inflation hurts the poor with their incomes not indexed to prices. It also puts pressure on interest rates, and adversely affects both savings and investment. Because of its implications for the poor and its possible destabilizing effects on macro-economic stability, containment of inflation is high on the Government's agenda.

5.27 The anti-inflationary policies of the government include strict fiscal and monetary discipline; rationalization of excise and import duties of essential commodities to lighten the burden on the poor; effective supply-demand management of sensitive items through liberal tariff and trade policies; and strengthening the public distribution system. Various fiscal and monetary measures taken by the government since February 2005 include the following:

- (a) Tariff values for crude palm and other palm oils were reduced in line with international prices. Simultaneously, import duties were increased on crude palm oil and crude palmolein from 65 per cent to 80 per cent, and on refined palm oil and RBD palmolein from 75 per cent to 90 per cent with effect from February 15, 2005 to reconcile the interests of both the farmers and the consumers. Excise duty on edible oils/vanaspati/fat was withdrawn with effect from March 1, 2005.
- (b) From April 29, 2005, the RBI increased the reverse repo rate by 25 basis points under the liquidity adjustment facility (LAF) from 4.75 per cent to 5 per cent.
- (c) In June 2004, Government decided to continue the subsidy on PDS kerosene and domestic LPG on a flat rate basis till March 31, 2007. The same policy continues with the overall subsidy burden shared with the upstream and downstream oil companies.
- (d) The Budget for 2005-06 rationalized the duty structure on petroleum products in a revenue neutral manner. Import duty on crude oil was reduced from 10 per cent to 5 per cent and excise and customs duties on PDS kerosene and domestic LPG were completely removed. The loss of revenue through such reductions was made good through revision of excise duties on motor spirit and HSD. To soften the impact of crude price volatility in the world market, the specific components of excise duty on motor spirit and HSD were enhanced with a corresponding reduction in the ad valorem components.
- (e) Keeping in view the inflationary risks of a liquidity overhang in the economy, the RBI, while announcing the Mid-Term Review of the Annual Policy Statement for 2005-06, effective from October 26, 2005, raised both the fixed reverse repo and fixed repo rates by 25 basis points each to 5.25 percent and 6.25 percent, respectively, with the spread between the two unchanged at 100 basis points.
- (f) From January 24, 2006 the RBI further increased the fixed reverse repo rate under the liquidity adjustment facility (LAF) by 25 basis points from 5.25 per cent to 5.50 per cent. The fixed repo rate will be 6.50 per cent.