Case Study

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India's New Impossible Trinity

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ABSTRACT

This case focuses on the recent development in Indian economy resulting in an Impossible trinity. In June 2020, with the fiscal stimulus packages announced across the globe, to combat the fall in growth in the pandemic has resulted in higher inflow of FIIs to Indian subcontinent. The higher appreciation of INR was partially sterilized by RBI, allowing a depreciation to augment exports. The intervention is particularly amusing in the backdrop of falling GDP growth and rising inflation. During Q1 2020-21 the real growth in the economy have plummeted by -23.4% in Q1 2020 and lesser fall of -7.9% was recorded in the Q2 2020. All the major components of GDP have registered negative growth with an exception to net exports largely due to the fall in imports than the fall in exports. Surprisingly, even with the fall in the demand in the Indian economy, the inflation figures were higher than 6% (exhibit 6 and exhibit 7) largely due to the supply disruptions during the Q1 and Q2 further removing GDP growth from its upward trajectory. The challenges facing the Indian economy left many market analysts and international investors wondering whether the "India growth story" was over. The Reserve Bank of India (RBI) governor, Dr ShaktiKanth Das, faced the difficult task of fighting inflation, when growth had slowed significantly. Additionally, he must control the capital inflows which is making currency appreciation resulting in lesser export competitiveness. Though India faced various episodes of Impossible trinity, the current situation is quite complex. The Expectations were high for an appropriate action from the central bank, while room for policy maneuverability was limited.

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