Reserve Bank of India Governor Raghuram Rajan cut interest rates in an unscheduled review to revive growth in Asia’s third-largest economy after inflation eased. Stocks, bonds and the rupee surged.

Rajan lowered the benchmark repurchase rate to 7.75 percent from 8 percent, he said in a statement today, the first reduction since May 2013. Consumer-price inflation will probably be below the central bank’s target of 6 percent by January 2016, he said.

“Key to further easing are data that confirm continuing disinflationary pressures,” Rajan said in the statement. “Also critical would be sustained high quality fiscal consolidation as well as steps to overcome supply constraints and assure availability of key inputs such as power, land, minerals and infrastructure.”

Rajan has focused on quelling inflation since taking office in September 2013, and today’s move signals confidence that price pressures will remain under control. It sets India on a different path from Brazil and Russia, which raised rates in December to tame inflation and support their currencies.

“Today’s rate cut should be seen as a carrot” before Prime Minister Narendra Modi’s government unveils its fiscal budget next month, said Mole Hau, a Hong Kong-based economist at BNP Paribas SA. “The ball is in the government’s court.”

Markets Gain

The benchmark S&P BSE Sensex index rose 1.9 percent as of 11:23 a.m. in Mumbai, the best performer in Asia. The rupee strengthened as much as 0.6 percent to 61.72 per dollar, the strongest since November. The yield on the benchmark 10-year sovereign bond dropped 10 basis points to 7.67 percent, the lowest since July 2013.

Commerce Minister Nirmala Sitharaman called the move “a great step forward although cautious” in an interview with Bloomberg TV India. She said that Finance Minister Arun Jaitley “is hard at work getting a good budget out.”

“Credit particularly for those who have international access to funds is still available far cheaper outside than here,” Sitharaman said. “But i will not harp on them today, a day when a much-
awaited cut has happened from the RBI.”

Rajan had signaled possible easing early in 2015, including outside of planned meetings, at the Dec. 2 rate review. The central bank doesn’t “intend to flip flop” once it moves, he said. The next scheduled review is Feb. 3.

**More Cuts**

“This does signal a shift in the underlying stance going forward,” Arvind Subramanian, the chief economic adviser to India’s finance ministry, told CNBC today. “It shouldn’t just be seen as one cut.”

The disinflationary process is “quite strong and taking hold” due to the decline in oil prices and rural wages, he said, adding that it will create room for more easing.

Rajan had earlier resisted calls for a rate cut from government officials including Jaitley, saying entrenched inflation needed to be fought to lay the ground for sustainable growth. India’s consumer prices rose 5 percent in December, while industrial production rose 3.8 percent in November.

“What has been strongly surprising is the persistence to which food inflation has remained low,” said Jahangir Aziz, Singapore-based chief economist for Asia at JPMorgan Chase & Co. “Maybe we are underestimating the impact lower oil prices have had on inflation.”

Brent crude prices have tumbled 55 percent in the past year, lowering India’s import bill and inflation as the nation ships in about 80 percent of its oil.

**Bank Rates**

By contrast with India, South Korea’s central bank chief today signaled he’s unwilling to reduce borrowing costs in response to an inflation rate pulled down in part by the slide in oil. Governor Lee Ju Yeol said the current interest rate of 2 percent is “not insufficient to support growth” and that the central bank will set future inflation targets soon.

Rajan’s move today will spur commercial banks to lower lending rates for borrowers, K. Subrahmanyam, executive director at state-run Union Bank of India in Mumbai, said in a phone interview. State Bank of India, the country’s largest bank by assets, has left its base rate at 10 percent since November 2013.

“The falling cost of funds will help in reviving the economy and help the banking system,” Subrahmanyam said.

Jaitley has pledged to narrow the fiscal shortfall to a seven-year-low of 4.1 percent of gross domestic product in the year through March 2015. The central bank cited the government’s
commitment to meeting the target in its statement today.

“If there is any slippage on the fiscal front, the RBI may have to reconsider,” said Rupa Rege-Nitsure, chief economist at Bank of Baroda in Mumbai. “But otherwise it is possible that the central bank cuts rates again after the budget.”

To contact the reporters on this story: Kartik Goyal in Mumbai at kgoyal@bloomberg.net; Sandrine Rastello in Mumbai at srrastello@bloomberg.net

To contact the editors responsible for this story: Daniel Ten Kate at dtenkate@bloomberg.net

Jeanette Rodrigues

©2015 BLOOMBERG L.P. ALL RIGHTS RESERVED.