Third Bi-Monthly Monetary Policy of Fiscal 2020

The MPC (Monetary Policy Committee) of the RBI has decided to maintain the rate cut on interest rates and slashed the repo rates for fourth time in a row under the new governor by unusual 35 bps to 5.40%. The reverse repo too was slashed by 35 bps to 5.15%. The Statutory liquidity ratio (SLR) was maintained at the same rate of 19.25%. CRR was also kept unchanged at 4%. The reduction of interest rates was on expected lines as market consensus had predicted easing of monetary policy due to benign inflation on account of lower crude prices.

The RBI has decided to reduce the repo rates by unusual 35 bps to 5.4%.

The tone of the MPC was dovish with the 'accommodative' stance from earlier 'Neutral' stance.

Reduces GDP forecast to 6.9% for FY20

The MPC member slashed the GDP growth forecast to 6.9% for FY20 from 7%for FY20. The GDP forecast for H1FY20 is projected at 6.4-6.7%. The MPC members have lowered the GDP range in the near term on account of global slowdown and consumption slowdown due to liquidity issues in the home country and expect recovery in H2FY20, thereby projecting GDP at 7.2-7.5%. The policy has made some vital announcements that under the revised guidelines on Large Exposure Framework (LEF) that came into effect from April 1, 2019, a bank's exposure to a single NBFC is restricted to 15% of its Tier I capital, while for entities in the other sectors the exposure limit is 20% of Tier I capital of the bank, which can be extended to 25% by bank's boards under exceptional circumstances. The RBI has also taken a bold step to make NEFT available 24/7 from December 19 to boost liquidity.

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Status Quo on inflation target.

On inflation front, the committee has started to feel the ease stating to be at comfortable levels and has maintained status quo to the earlier CPI targets of 3-3.1% from earlier mentioned 2.9-3% for H1FY20. The committee has set the range of 3.4-3.7% for H2FY20 from the earlier range of 3.5-3.8%. The primary reason for a status quo in inflation is chiefly due to fall in oil prices and normal monsoon across PAN India. Though the revised range broadly falls in the RBI's comfortable levels of 4 % (+/-2), we feel steep decline in the crude prices shall also weigh for either status quo or upward revision of the inflation targets to infuse growth back in the economy.

The MPC members maintained the inflation targets of 3-3.1% for H1FY20 and 3.4-3.7% for H2FY20.

Outlook

RBI for the fourth time in a row after the appointment of the new governor has cut Repo rates by 1.1 bps in totality to 5.4% and maintained the stance of 'accommodative' from the earlier stance of 'Neutral' followed by status-quo in the inflation targets to infuse growth back in the economy. Though the MPC has cut down the GDP growth rate in H1FY20, but the committee expects growth to be back in the system, by way of infusing liquidity in the system through various steps including NEFT made available 24/7 from December 19. On account of lower crude prices and stable inflation, we expect further 25 bps rate cuts which will aid the bond yields to hover around 6.2% – 6.4% on account of all the bold steps taken by the RBI to infuse liquidity.

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