RBI POLICY REVIEW

Event Update

DALAL & BROACHA
STOCK BROKING PVT. LTD.

Equity Research Desk

Maintains Accommodative Stance; Assures Liquidity as Economy Rebounds

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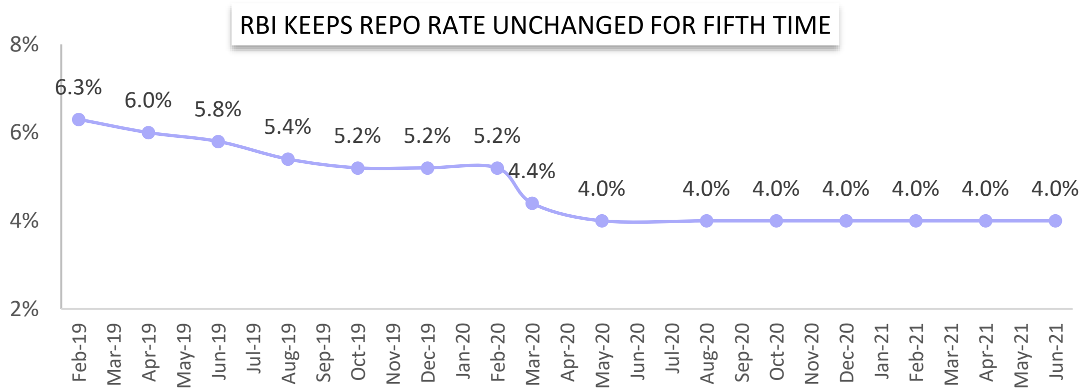
RBI's monetary policy committee has decided to keep key policy rates on hold and reiterated that it will maintain the accommodative stance for as long as necessary to sustain growth on a durable basis. This is the sixth time in a row that the RBI has maintained a status quo on policy rate. This indicates that the central bank is trying to mitigate the impact of COVID-19 on the economy, while ensuring that inflation remains within the target going forward. The repo rate was held at 4%, while the reverse repo rate was left unchanged at 3.35%. Meanwhile, additional measures to enhance liquidity to vulnerable sectors and increase credit exposure limit for resolution is a great move.



Policy Tools	Policy rates	Status
Repo	4.00%	Unchanged
Reverse Repo	3.35%	Unchanged
Marginal Standing Facility (MSF)	4.25%	Unchanged
Bank Rate	4.25%	Unchanged
SLR	18.0%	Unchanged

REDUCED GDP GROWTH PROJECTION AT 9.5% FOR FY22

The central bank revised real GDP growth rate downwards to a single-digit 9.5% amid second wave of Covid-19 and localised lockdowns. The economy is likely to grow at the rate of 18.5% in Q1FY22, 7.9% in Q2FY22, 7.2% in Q3FY22 and 6.6% in Q4FY22. Rural demand remains strong and the expected normal monsoon bodes well for sustaining its buoyancy, going forward. The increased spread of COVID-19 infections in rural areas, however, poses downside risks. On the other hand, urban demand has been dented by the second wave, but adoption of new COVID-compatible occupational models by businesses for an appropriate working environment may cushion the hit to economic activity, especially in manufacturing and services sectors that are not contact intensive. Meanwhile, the vaccination process is expected to gather steam in the coming months and should help to normalise economic activity quickly.

Lowers inflation projection to 5.1% for FY22

CPI inflation is projected at 5.1% for FY22, with 5.2% for Q1FY22, 5.4% for Q2FY22, 4.7% for Q3FY22 and 5.3% for Q4 FY22, with risks broadly balanced. A normal south-west monsoon along with comfortable buffer stocks should help to keep cereal price pressures in check. With declining infections, restrictions and localised lockdowns across states could ease gradually and mitigate disruptions to supply chains, reducing cost pressures. Weak demand conditions may also temper the pass-through to core inflation. However, the rising trajectory of international commodity prices, especially of crude, together with logistics costs, pose upside risks to the inflation outlook.

Outlook

RBI's decision to maintain an accommodative stance is on expected lines. This will continue to support the credit off-take and maintain a benign interest rate scenario in the money market system. While RBI tried to tick all the boxes, a lot will depend on how the COVID-19 scenario develops as it will have a huge impact on the economy and corporate earnings. The downward revision in FY22 GDP growth projection was also on expected lines. As the nation attempts to recover from the second wave of pandemic, the central bank has tried to support the economy by extending separate liquidity window for stress sectors along with additional liquidity to SIDBI and the expansion of the scope of restructuring 2 framework to more borrowers. We expect MPC to continue with its current policy stance for H1FY22 and may gradually start withdrawal of surplus liquidity from H2FY22 onwards.

Other Major Announcements

- **On Tap Liquidity Window for Contact-Intensive Sectors**
  - On May 5, 2021, RBI decided to open an on-tap liquidity window of Rs 500 Bn with tenors of up to three years at the repo rate till March 31, 2022 to boost provision of immediate liquidity for ramping up COVID-related healthcare infrastructure and services in the country. It has now been decided to open a separate liquidity window of Rs 150 Bn with tenors of up to three years at the repo rate till March 31, 2022 for certain contact-intensive sectors **i.e., hotels and restaurants; tourism – travel agents, tour operators and adventure/heritage facilities; aviation ancillary services – ground handling and supply chain; and other services that include private bus operators, car repair services, rent-a-car service providers, event/conference organisers, spa clinics, and beauty parlours/saloons.**
  - Banks will be eligible to park their surplus liquidity up to the size of the COVID loan book, created under this scheme, with the Reserve Bank under the reverse repo window at a rate which is 25 bps lower than the repo rate or, termed in a different way, 40 bps higher than the reverse repo rate.

This was necessary as second wave of Covid has affected the mentioned sectors in a bad way, now the onus is on the banks to lend to organizations in these sectors and get them running again.

- **Special Liquidity facility to SIDBI**
  - In order to meet MSMEs' short- and medium-term credit needs to kick start the investment cycle with additional focus on smaller MSMEs and businesses including those in credit deficient and aspirational districts, RBI has provided a further special liquidity facility of Rs160 Bn to SIDBI.
  - Funds will be provided at prevailing repo rate for a period of up to one year.

The funds will help MSMEs and small borrowers who will avail this liquidity from SIDBI via refinancing/on lending.

- **Enhancement of exposure thresholds under Resolution Framework 2.0**
  - RBI has decided to enhance the exposure threshold to Rs 0.50 Bn from Rs 0.25 Bn. Accordingly MSMEs/non MSME small businesses and loans to individuals for business purposes to whom the lending institutions have aggregate exposure of not more than Rs0.50 Bn as on March 31, 2021, and which have not been restructured earlier under any of the specified restructuring frameworks, shall be eligible to be considered for resolution under Resolution Framework 2.0.
  - All other conditions shall remain the same.

Sale of consumer/non consumer durables has been hit badly in the second wave due to covid and lockdowns. Restructuring will help MSME's and other borrowers with a bigger loan who have a standard classification ease their terms of repayment without falling into NPA. Icategory.

- **RBI announces Government Security Acquisition Programme 2.O**
  - RBI announced the second tranche of the bond buying program of Rs 1.2 lakh crore. The Government Securities Acquisition Program (GSAP 2.0), which is higher than the first tranche, will be conducted in the second quarter of the financial year.
  - The remaining Rs 400 Bn of GSAP 1.0 will be conducted on 27 June.
  - RBI's objective is to avoid volatility in GSEC market and will also enable flattening of yield curve.

This will enable Government to borrow at low cost for its expenses and will also flatten the yield curve. Many financial market instruments use G-sec for its pricing and this acquisition will keep long term rates in check.

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Name	Designation	Email	Phone	Sector
Mr. Kunal Bhatia	Head of Research	kunal.bhatia@dalal-broacha.com	022 67141442	Auto | Auto Ancillary | FMCG
Mrs.Charulata Gaidhani	Sr. Analyst	charulata.gaidhani@dalal-broacha.com	022 67141446	Pharma | Healthcare
Mr. Mayank Babla	Sr. Analyst	mayank.babla@dalal-broacha.com	022 67141412	IT | Telecom | Media
Mr. Avinash Tanawade	Sr. Analyst	avinash.tanawade@dalal-broacha.com	022 67141449	BFSI
Mr. Akshay Ashok	Analyst	akshay.ashok@dalal-broacha.com	022 67141486	BFSI
Ms. Timshar Dhamodiwala	Associate	timshar.dhamodiwala@dalal-broacha.com	022 67141441	IT | Telecom | Media

Address: - 508, Maker Chambers V, 221 Nariman Point, Mumbai 400 021.

Tel: 91-22- 2282 2992, 2287 6173, Fax: 91-22-2287 0092

E-mail: equity.research@dalal-broacha.com