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RBI Event Note @ Dalal & Broacha

RBI POLICY UPDATE:

- **Reserve Bank of India's (RBI) Monetary Policy Committee on Thursday decided to cut its benchmark repo rate by 25 bps to 6%, citing benign inflation and risks to the growth trajectory.**
- CPI inflation has remained within the central bank's four percent target for over seven months and is expected to remain within the target range at least for the next few months. Given these circumstances, **MPC has decided to ease interest rates, with the policy decision supported by a 4-2 vote**, with MPC members Chetan Ghate and Viral Acharya voting to keep the Repo rate unchanged.
- Consequently, the **reverse repo rate under the LAF stands adjusted to 5.75%**, and the marginal standing facility (**MSF) rate and the Bank Rate to 6.25%**. These decisions are in consonance with the objective of achieving the medium-term target for CPI inflation of 4% within a band of +/- 2%, while supporting growth.
- **Committee has maintained the policy stance at 'neutral', indicating that there may be scope of more rate cuts.** While five out of six members voted in favour of the decision to maintain the neutral stance of monetary policy. Ravindra Dholakia has voted to change the stance from neutral to accommodative.

Key Policy rates:

Policy Tools	Post policy	Pre policy	Status
Repo	**6.00%**	**6.25%**	Changed by 25 bps
Reverse Repo	**5.75%**	**6.00%**	Changed by 25 bps
Marginal Standing Facility (MSF)	**6.25%**	**6.50%**	Changed by 25 bps
Bank Rate	**6.25%**	**6.50%**	Changed by 25 bps
CRR	**4.00%**	**4.00%**	Unchanged
SLR	**19.25%**	**19.25%**	Unchanged

Growth Outlook:

- MPC has lowered the GDP growth forecast for FY20 to 7.2% from the earlier estimate of 7.4%, mainly due to weak domestic investment activity (reflected in the slowdown in production & imports of capital goods) & uncertain global economic outlook.
- GDP growth has been projected in the range of 6.8-7.1% in the first half of FY20 and 7.3-7.4% in the second half of FY20, with risks evenly balanced.
- Committee notes that the output gap remains negative and the domestic economy is facing headwinds, especially on the global front. The need is to strengthen domestic growth impulses by spurring private investment which has remained sluggish.
- Capacity utilisation (CU) in the manufacturing sector as measured by the Reserve Bank's order books, inventory and capacity utilisation survey (OBICUS), improved to 75.9% in Q3 from 74.8% in Q2 exceeding its long-term average; the seasonally adjusted CU rose to 76.1% from 75.4%.
- Credit flows to micro, small and medium industries remained tepid, though they improved for large industries. The business assessment index of the industrial outlook survey (IOS) points to an improvement in overall sentiments in Q4.

Inflation Outlook:

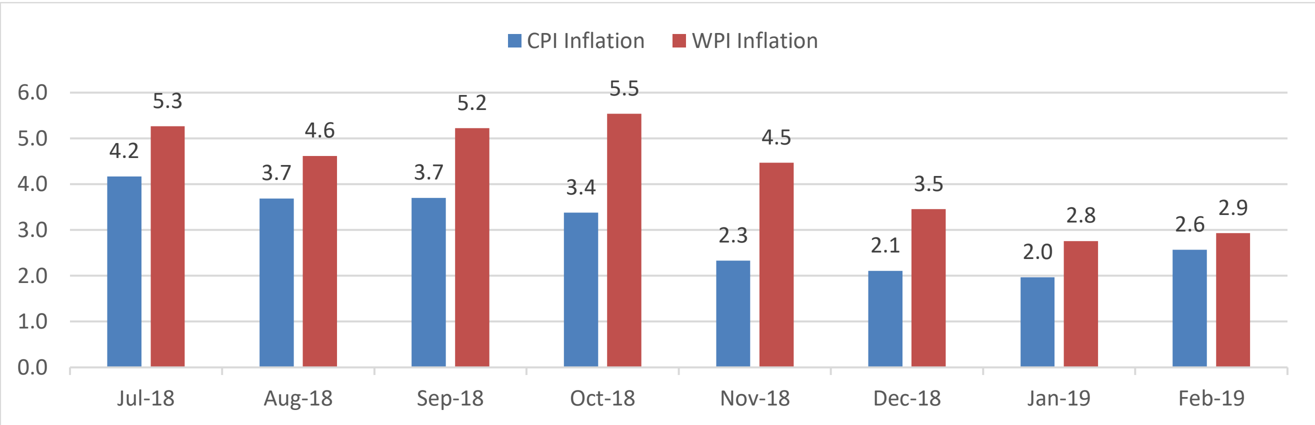
- MPC has also lowered its inflation forecast for the first half of FY20, citing factors including lower food prices and expectation of a normal rainy season. Committee is expecting that the inflation will remain in the range of 2.9-3.0% for the first half of FY20, and 3.5-3.8% in the second half of FY20, with risks broadly balanced.
- However, the central bank has also mentioned about the upside risk to inflation forecast, which includes the probability of El Nino effects on monsoon rains. There is also the risk of an abrupt reversal in vegetable prices, especially during the summer months.
- Besides, the outlook for oil prices continues to be hazy, both on the upside and the downside, considering continues production cuts by OPEC (Organization of the Petroleum Exporting Countries).

Other major announcements

- RBI in its Statement on Development & Regulatory policies has deferred the proposal to link all new floating rate personal or retail loans (housing, auto, etc.) to an external benchmark, a move which will increase transparency and speed of transmission of changes in interest rates in economy. Central Bank has decided to hold further consultations with stakeholders on issues such as management of interest rate risk by banks from fixed interest rate linked liabilities against floating interest rate linked assets and the related difficulties, and the lead time required for IT system upgradation.
- In order to improve the ease of undertaking forex transactions, RBI has allowed non-deposit taking systemically important Non-Banking Financial Companies (NBFCs-NDSI) in the category of Investment & Credit Companies (ICCs) to apply for grant of Authorised Dealer Category II licence.
- The central bank has decided to put in place a framework on TAT (Turn Around Time) for resolution of customer complaints and compensation framework across all authorised payment systems by the end of June 2019. RBI has also directed various authorised payment systems to put in place appropriate customer grievance redressal mechanism.
- RBI has decided to extend the eligibility of housing loan under priority sector lending to the Regional Rural Banks and Small Finance Banks. The Housing loan limits for eligibility under Priority Sector Lending were revised during June 2018 for Scheduled Commercial Banks (excluding Regional Rural Banks and Small Finance Banks). This move is aimed to bring these banks at a level-playing field with other scheduled commercial banks.
- In order to improve the cash position of banks, the central bank has permitted an additional 2% liquidity window to the lenders by tweaking liquidity coverage ratio (LCR) norms. The FALLCR (facility to avail liquidity for liquidity coverage ratio) was increased from the existing 13% to 15% of banks' net demand and time liabilities (NDTL). The mandate will be implemented in a phased manner between April 2019 to April 2020.

Effective Date	FALLCR (per cent of NDTL)	Total HQLA carve out from SLR (per cent of NDTL)
April 4, 2019	13.5	15.5
August 1, 2019	14.0	16.0
December 1, 2020	14.5	16.5
April 1, 2020	15.0	17.0

CPI inflation has been well below the threshold of 4% for the last seven months in a row



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