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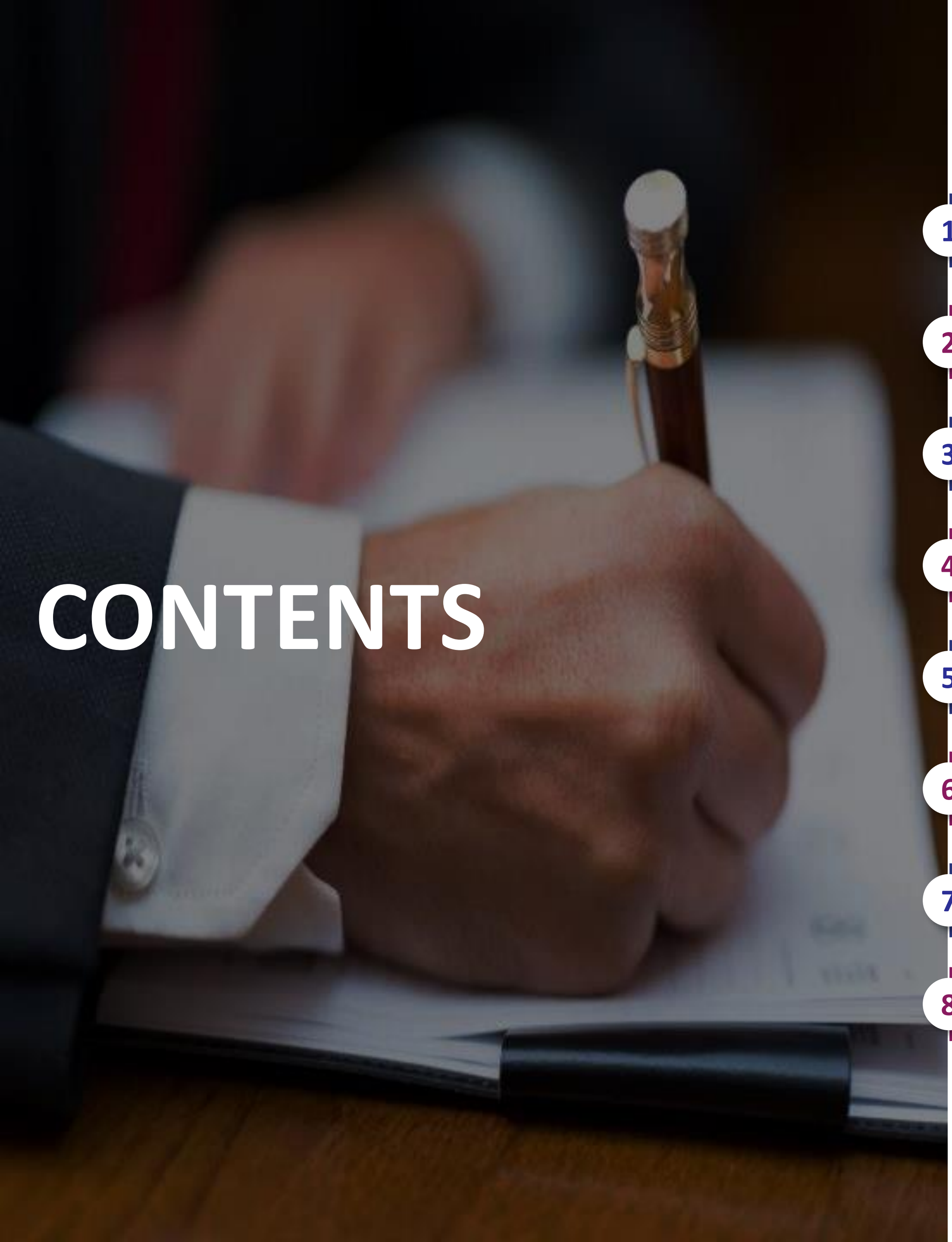
RBI MONETARY POLICY

Status quo policy: Herding the inflation elephant back to forest durably

April 2024



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A status quo policy - focal point to preserve economic expansion while concurrently managing disinflationary progress

Bidding adieu to the elephant (inflation) vexing over the past couple of years, RBI wants to make certain its durable return to forest, as the MPC steers the economy alongside statuesque growth. With real growth abating any concerns, external sector eminently managed and nimble management of liquidity, the focus of policyspeak inherently turns to *sustenance of the current macroeconomic environment while clinching on rate transmission and fending off any and every disruptions to the progress of disinflation.* Eclipsing domestic macros, momentous global growth are adjacent in MPC's wits, as they keep one eye on the actions of global Central Banks amid a challenging last mile of disinflation and high global public debt.

MPC maintains temper on rates and stance, both with a 5-1 vote

It was decided to keep the repo rate unchanged at 6.50%, in line with expectations. Akin to previous policy, the vote this time was also 5-1. All other policy rates such as MSF, bank rate, and SDF also remained unchanged. The MPC also retained its stance of being focused on withdrawal of accommodation, by a similar 5-1 vote as last time. Work-in-progress policy transmission to lending rates, last mile of disinflation, coupled with disjoining stance from liquidity conditions in the previous policy, fortifies RBI's decision to maintain the stance. ***In this backdrop, we expect the first rate cut not before Aug'24, as RBI remains vigilant of the unfolding global landscape's sway on external position and imported inflation, if any.***

Rejoicing on ebbing core, RBI maintains caution on transitionary shocks

With unhindered progress on ebbing core, inflation aptly doesn't seem to be a quandary for the rate steering committee anymore. Accordingly, CPI growth expectations of RBI were revised downwards for virtually all quarters of FY25, averaging 4.5% y/y assuming normal monsoons. Governor was eloquent on transient shocks as short amplitude of food pressures and rising crude due to global developments, deter a swifter fall to RBI's target of 4%. ***We concur with RBI's foresight of these risks to be evenly managed*** *on account of benign international food inflation* ***and anticipate the headline to moderate to 4.7% y/y in FY25, slightly (20 bps) higher than RBI projections*** *with monsoons and oil remaining a key monitorable.* Unwavering focus on inflation was ascribable to robust growth

Growth momentum to abide throughout FY25, with rural consumption and factory activity paving the way further crowding in private capex

Plausibly, after witnessing over-delivery with a stellar 8.4% y/y real growth in Q3FY24, the RBI ameliorated its promise by resolving GDP growth for FY25 at 7.0% y/y, in line with previous estimates, projecting higher growth in later quarters of FY25 when compared to Feb'24 projections. FY25 maintaining 7% growth momentum witnessed over the past 3 years is a reinforcement of recovery in agricultural economy, bargained for private capex, and stellar factory activity despite Union successfully maneuvering to fiscal consolidation. ***We anticipate the FY25 nominal GDP to grow at 10.5% y/y****, partially owing to higher base effects*

EXECUTIVE SUMMARY (2/2)

Fiscal prudence remains forefront of policyspeak, through conscious liquidity management and peripheral measures

The Central Bank is meticulously using every tool in its arsenal to ensure fiscal prudence and adequate countercyclical buffers, with the current spotlight on scraping any possible excess liquidity in the system while also allowing for diligently calibrated sufficient surpluses. Numerous LAF operations have ensured the commitment of apt flexible and durable liquidity, exhibited through the softening bias in WACR, maneuvering it close to the target repo. Abiding with this strategy and perpetuating salubrious and consultative relationship with regulated entities through RRA 2.0 remains RBI's focus. Abiding to regulations and giving priority to governance by Banks and NBFCs was underscored by the Governor.

External position eminently managed in FY24, as sturdy capital flows offset basal deficit

Sanguine service exports and lower imports in 11MFY24 humbled the overall trade deficit by 4.6% y/y to USD 72 bn, which were also greeted by improving equity FPIs, bond-inclusion oriented debt flows, and stellar growth in ECBs. India remains the largest recipient of remittances globally, with declining costs. In light of strong flows and forex reserves at all time highs, contemporarily appreciating USD can be comfortably managed. Relatively stable INR throughout recent volatilities for other EMs is a testament of Central Bank's commitment to sound financial and macro stability, which could be only tested by high global public debt and slower growth in global trade led by geopolitical disruptions

Key Additional Measures

- A scheme will be implemented to facilitate non-resident participation in SGrBs, enhancing their investment and trading opportunities in the IFSC
- Introduction of mobile app for RBI Retail Direct Scheme to enhance retail investor accessibility and deepen GSec market
- Technological advancements allowing instant withdrawal or transfer of funds pose challenges for banks, particularly in managing simultaneous mass withdrawals. This has underscored the urgency for a comprehensive review of the LCR framework

In the aftermath of the policy Gsec yields remained range bound

A status quo policy kept the yields range bound, with the 10 Year rising by 2 bps to 7.11% from last trading session, as RBI's stern commitment of returning inflation to 4% target durably, took forefront. In the near term, fiscal consolidation led lower borrowing, decelerating core inflation, bond inclusion in Global indices ***to draw yields lower than 7% threshold*** helped by cuts anticipated to start in the later part of CY24, not before Aug'24

RBI KEEPS POLICY RATE UNCHANGED AS EXPECTED

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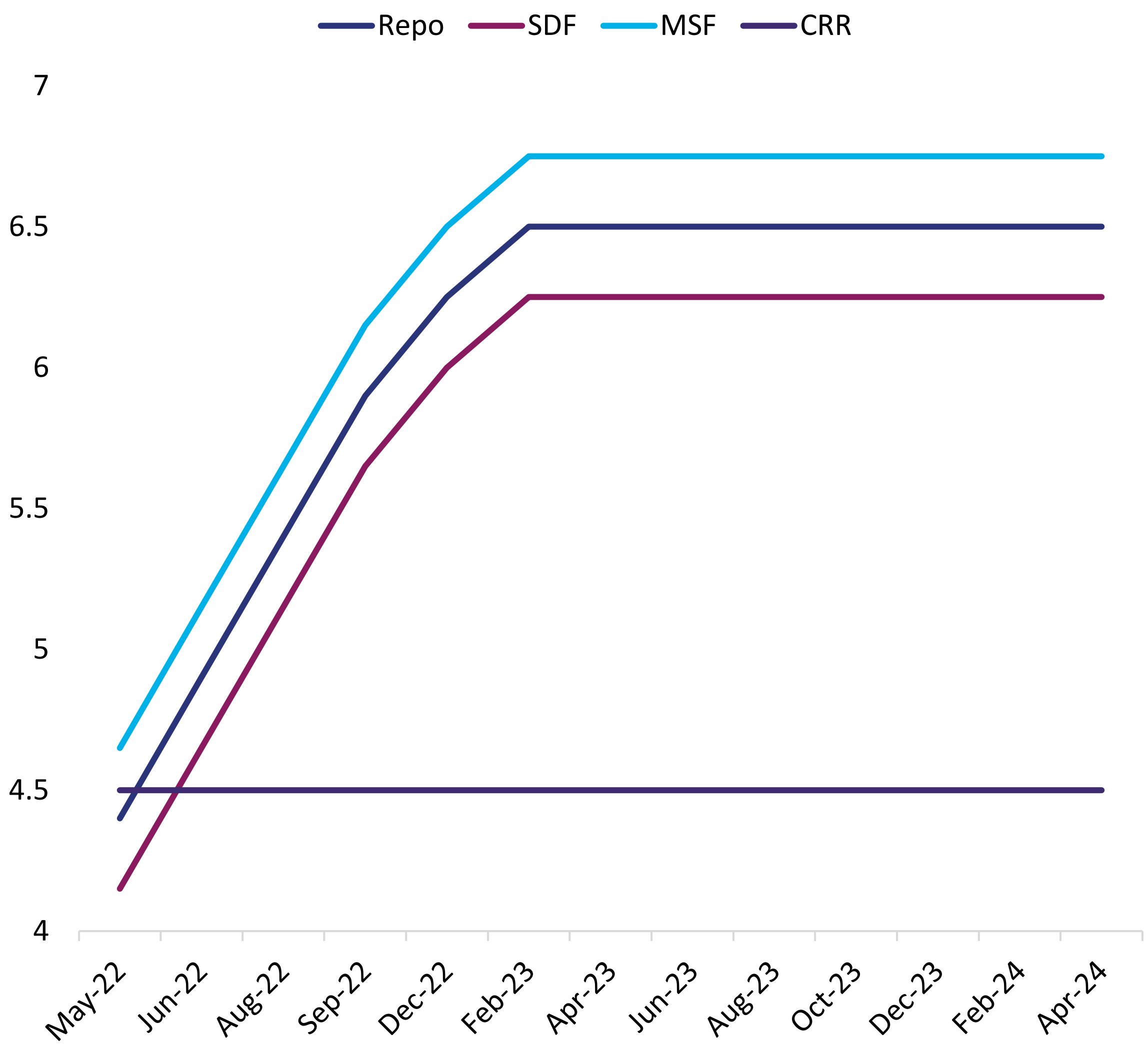
KEY RATES (%)



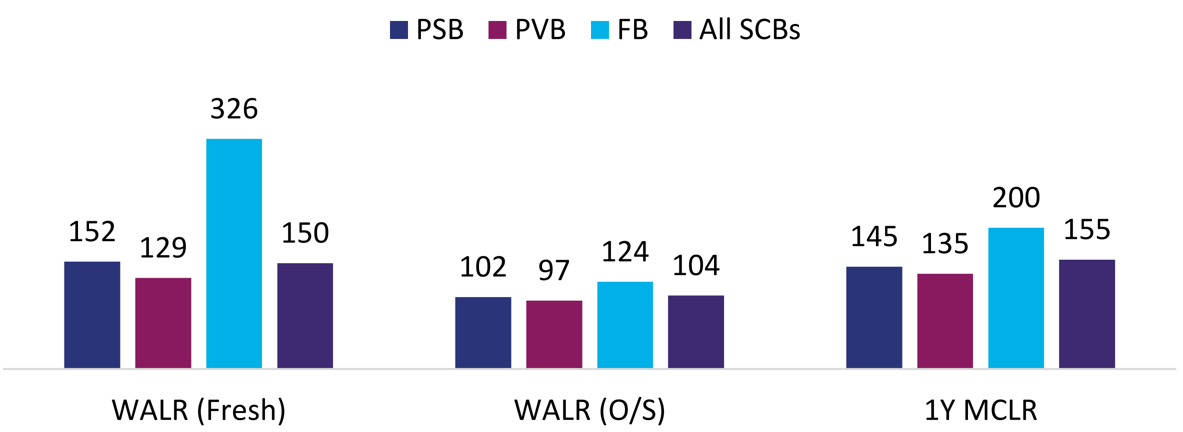
STANCE OF POLICY

Date	Stance	Vote
04-May-22	Remain accommodative, while focussing on withdrawal of accommodation	6-0
08-Jun-22	Withdrawal of Accommodation	6-0
05-Aug-22	Withdrawal of Accommodation	6-0
30-Sep-22	Withdrawal of Accommodation	5-1
07-Dec-22	Withdrawal of Accommodation	4-2
08-Feb-23	Withdrawal of Accommodation	4-2
06-Apr-23	Withdrawal of Accommodation	5-1
08-Jun-23	Withdrawal of Accommodation	5-1
10-Aug-23	Withdrawal of Accommodation	5-1
06-Oct-23	Withdrawal of Accommodation	5-1
08-Dec-23	Withdrawal of Accommodation	5-1
08-Feb-24	Withdrawal of Accommodation	5-1
05-Apr-24	Withdrawal of Accommodation	5-1

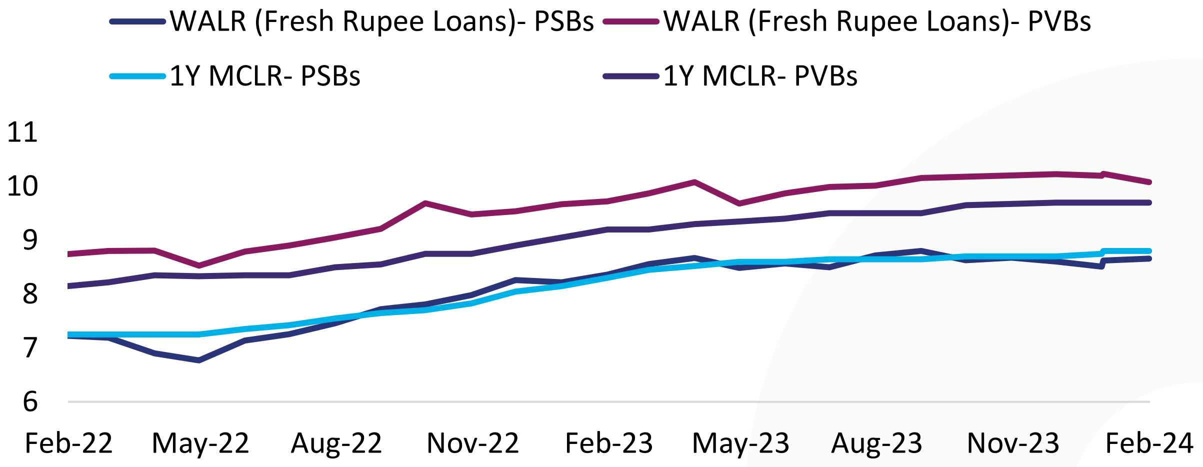
- RBI's MPC kept the repo rate unchanged at 6.50%, in line with market expectations, while it acknowledges resilience in global growth amid a tougher last mile progress on global disinflation. Vote for decision was 5-1.
- The stance was retained as **withdrawal of accommodation**. The vote for the stance was 5-1, as was the case in previous MPC too

RATE TRANSMISSION REMAINS A WORK-IN-PROGRESS

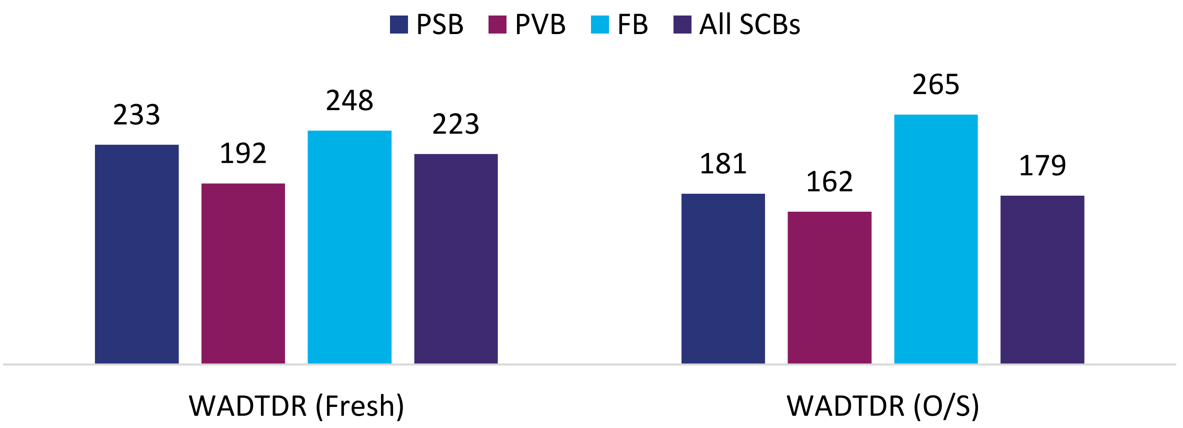
TRANSMISSION TO LENDING RATES FROM MAY'22 TO FEB'24 (BPS)



LENDING RATES OF DOMESTIC BANKS (%)



TRANSMISSION TO DEPOSIT RATES FROM MAY'22 TO FEB'24 (BPS)



- 250 bps of rate hikes have not been fully transmitted to lending rates. This assumes importance as RBI remains resolute for transmission of past policy actions
- Transmission to deposits is more complete, due to credit growth consistently outpacing deposits growth

Source: RBI, SBICAPS

DOMESTIC BUOYANCY AMID MOMENTOUS GLOBAL GROWTH

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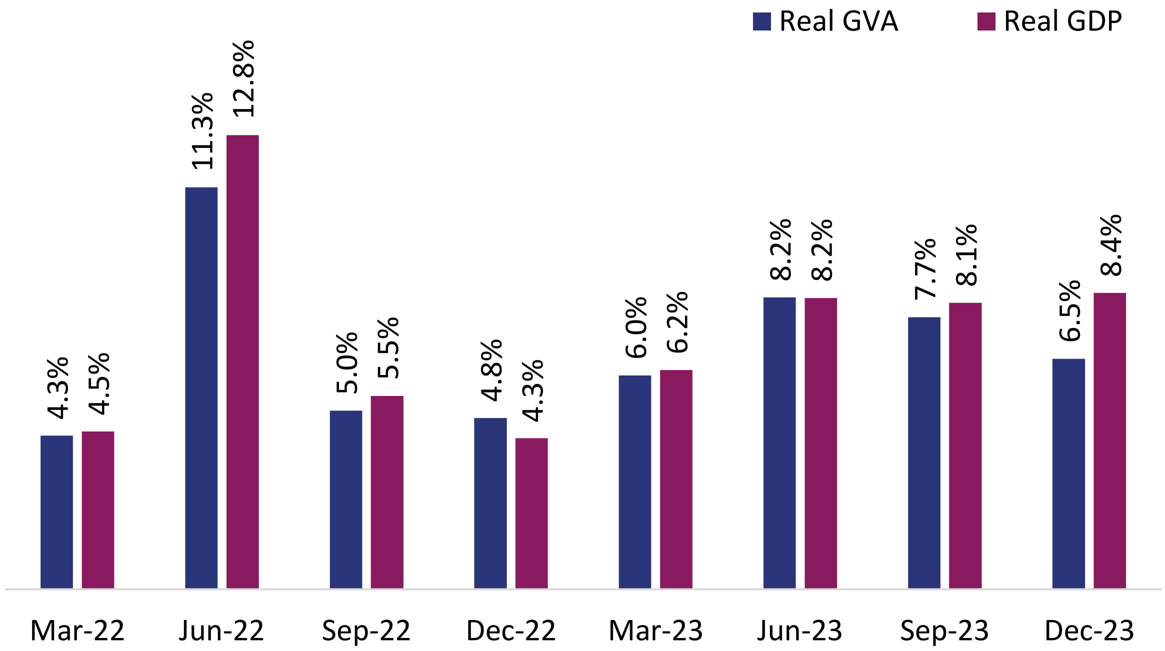
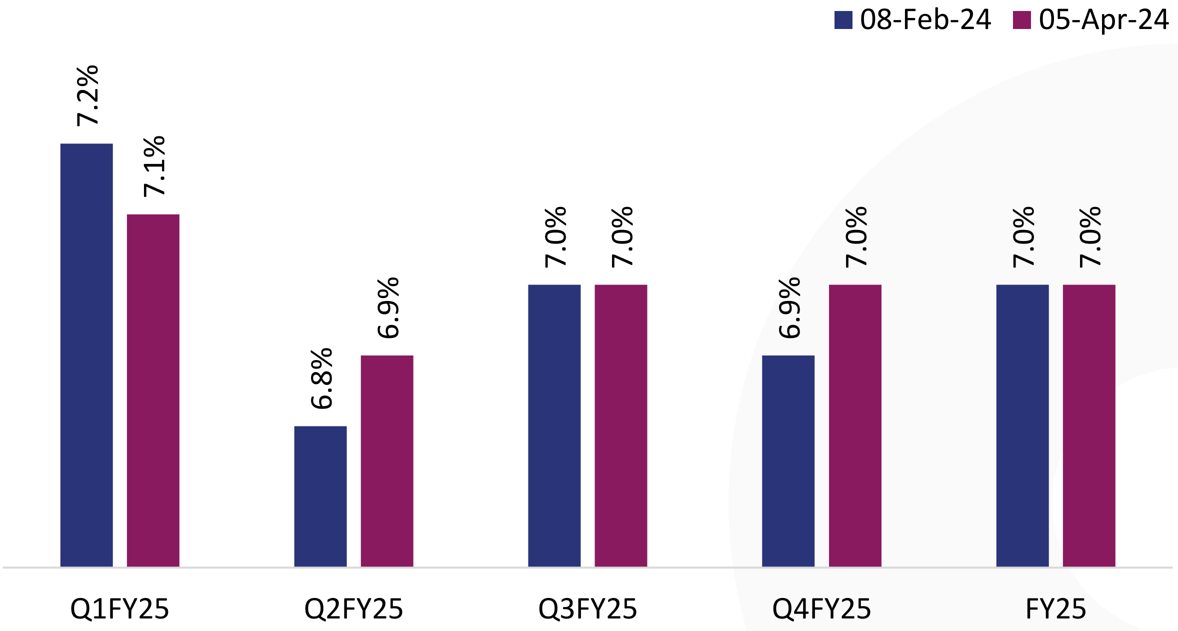
QUARTERLY REAL GDP & GVA GROWTH RATES (IN %Y/Y)



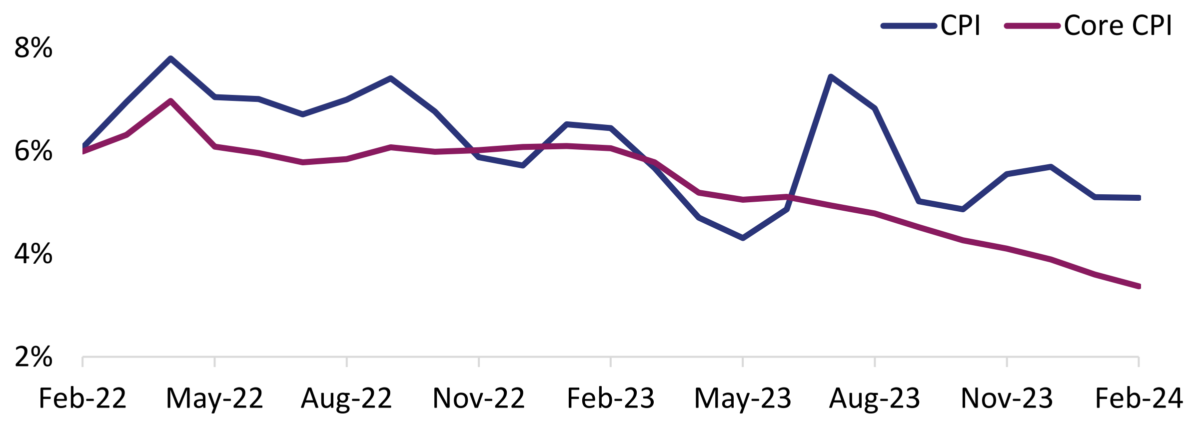
PROJECTED REAL GDP (IN % Y/Y) AS PER RBI



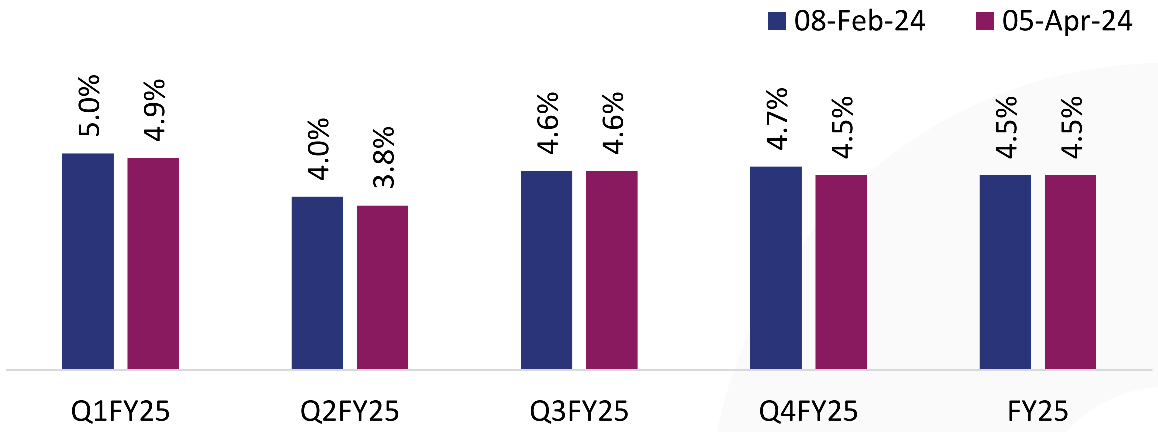
- Decelerating inflation, recovery in manufacturing and unwinding of supply-side issues has led to steady global economic growth evidenced by the upward revisions in the US and high growth in EMs, despite tight monetary conditions.
- With India continuing to beating all expectations, RBI has maintained domestic growth at 7% for FY25, with upward revisions in later part of FY25, indicating sustained momentum. Cheering 7%+ growth for 3 consecutive years and the momentum continuing in FY25 as well, slight moderation from FY24 is on account of base effects
- Thereby, we expect nominal growth in FY25 at 10.5% y/y led by of recovery in agricultural economy, bargained for private capex, and stellar factory activity

RBI COMFORTABLE WITH EBBING CORE, WARY OF TRASIENT SHOCKS

CPI AND CORE CPI (IN % Y/Y)



PROJECTED CPI (IN % Y/Y) AS PER RBI



BRENT CRUDE (USD/BBL)

- RBI maintained its inflation expectations of FY25 at 4.5%, while projecting lower inflation for virtually all quarter
- Amid significant progress, inflation doesn’t seem to be pose a quandary for MPC anymore, except transitionary shocks in food and rising Oil

STRONG MACROS DRIVES VOLATILITY IN US YIELDS

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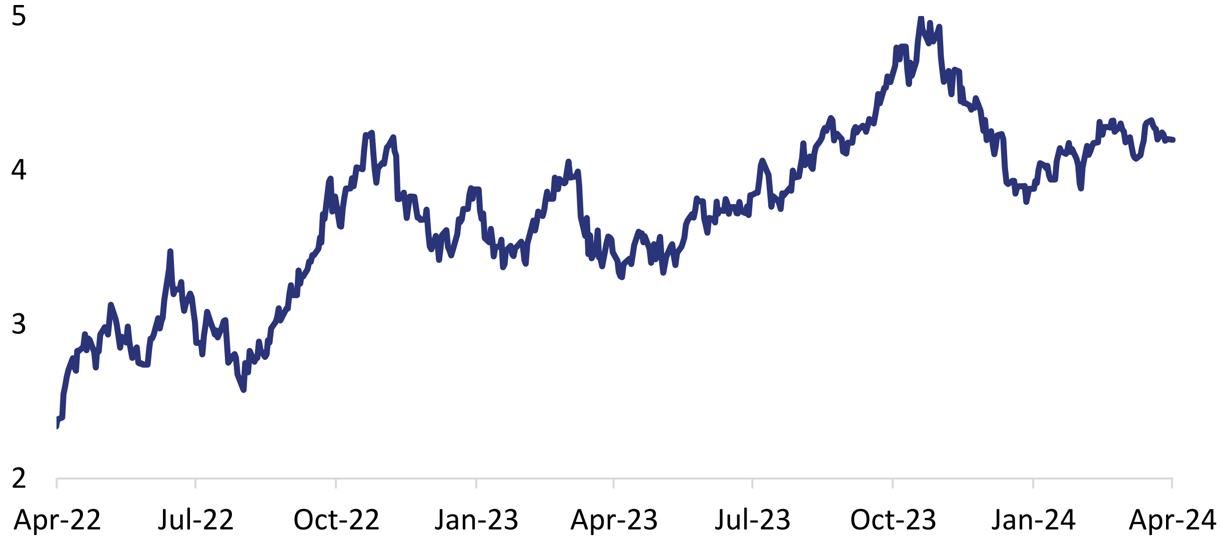
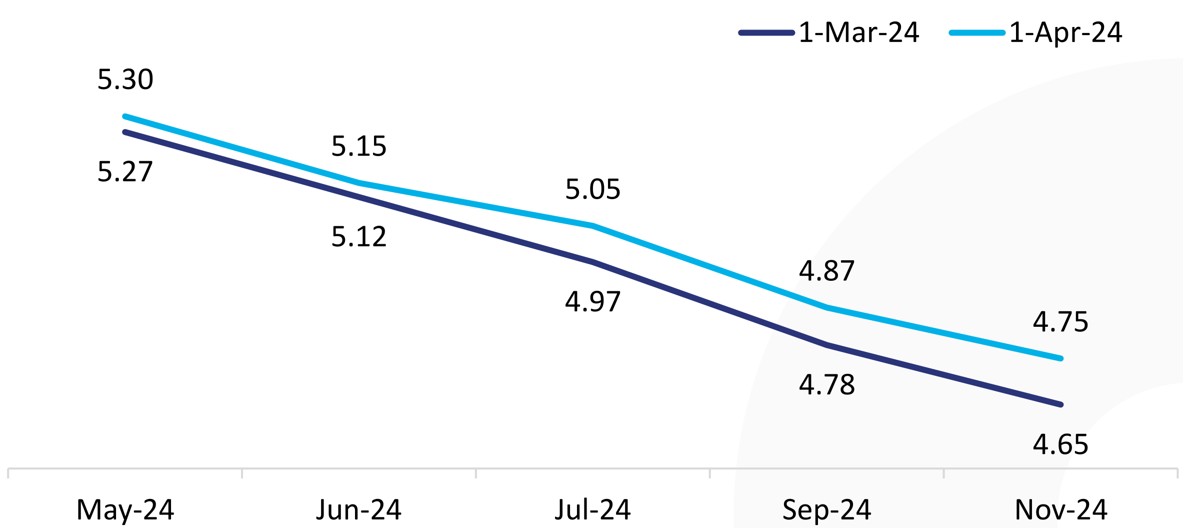
US 10Y G-SEC YIELD (IN %)



MARKET-IMPLIED PATH OF US FED POLICY RATE (IN %)

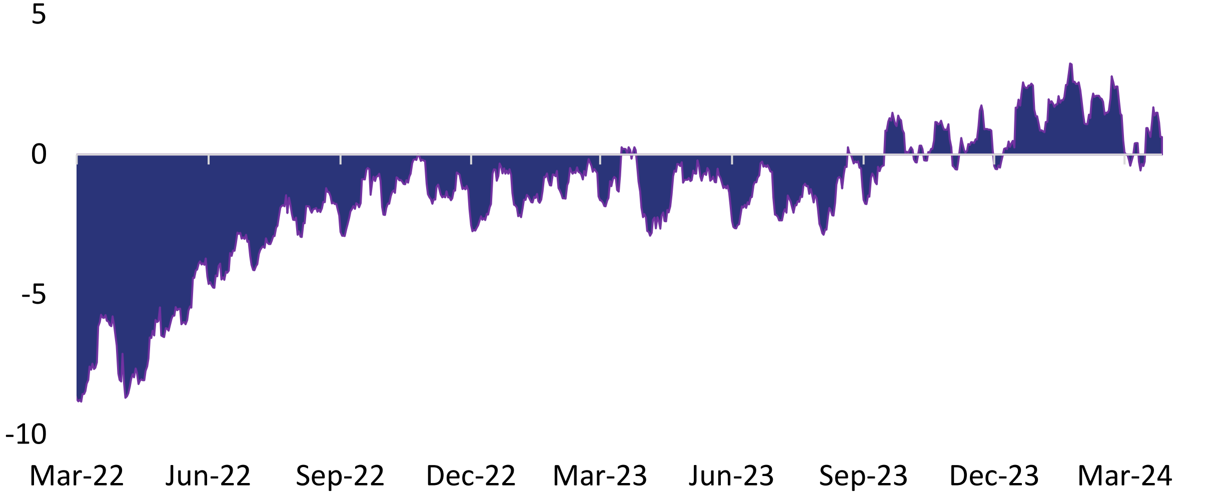


- US bond yields have remained volatile in Mar’24 despite 75 bps rate cut assumptions maintained in recent FOMC dot plot, as uncertainty looms about the timing of such cuts on account of strong macroeconomic data
- The impact of global bond price volatilities is not expected to be acute on domestic market

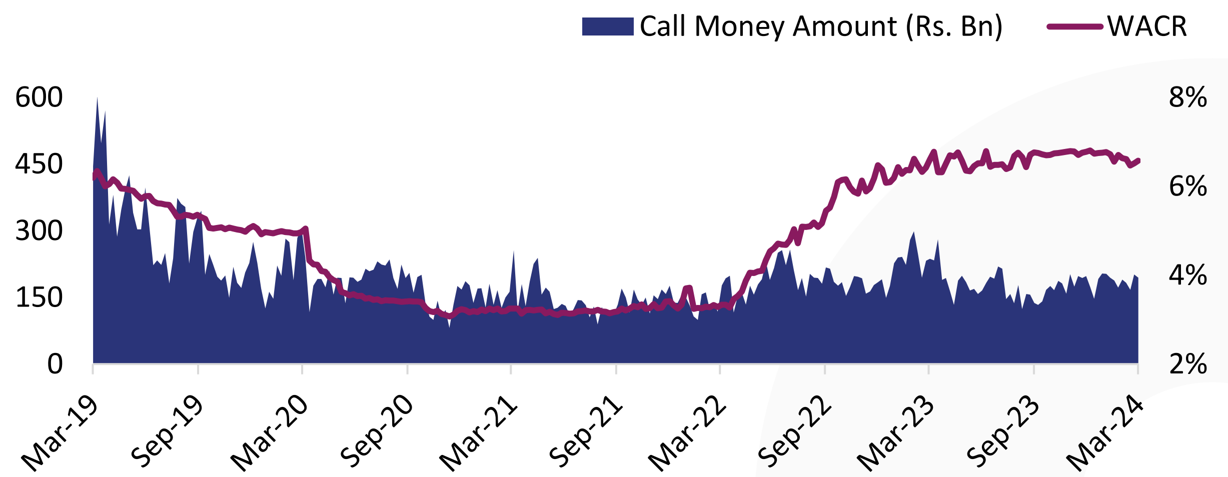
Source: Bloomberg, SBICAPS

RBI FOCUSSES ON NIMBLE LIQUIDITY MANAGEMENT

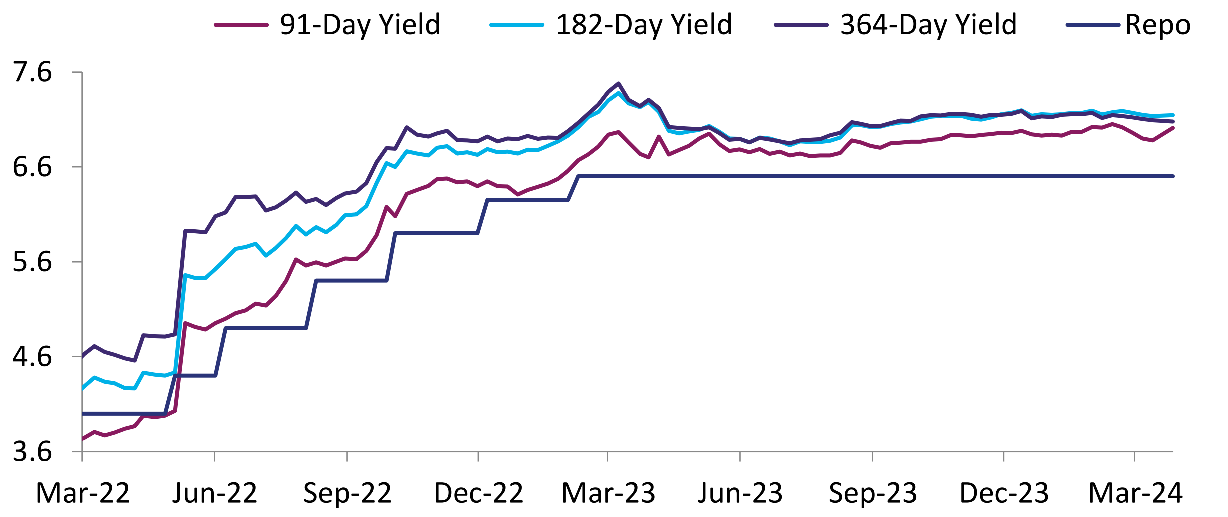
BLOOMBERG INDIA LIQUIDITY INDICATOR (RS. TRN.)



CALL MONEY AMOUNT (RS. BN.) VS CALL MONEY RATE (%)



T-BILL YIELDS VS. REPO (%)

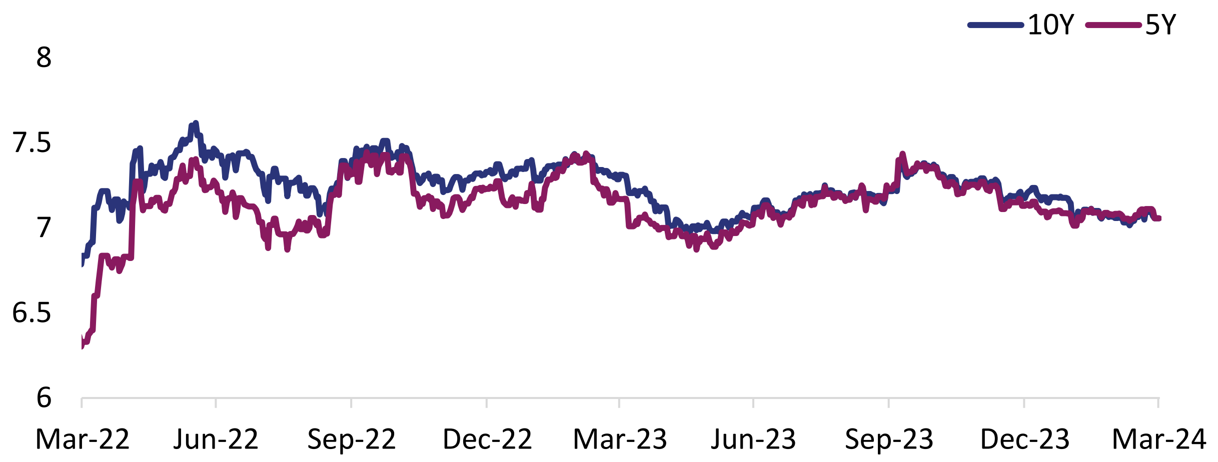


- As focus of the central bank progresses to prudence and financial stability, active management of liquidity has taken forefront
- Liquidity currently stands at a minor surplus in Apr'24, after tighter conditions in Mar'24 prevailed due to flows to exchequer
- Numerous LAF operations have ensured the commitment of apt flexible and durable liquidity, exhibited through the softening bias in WACR, maneuvering it close to the target repo.

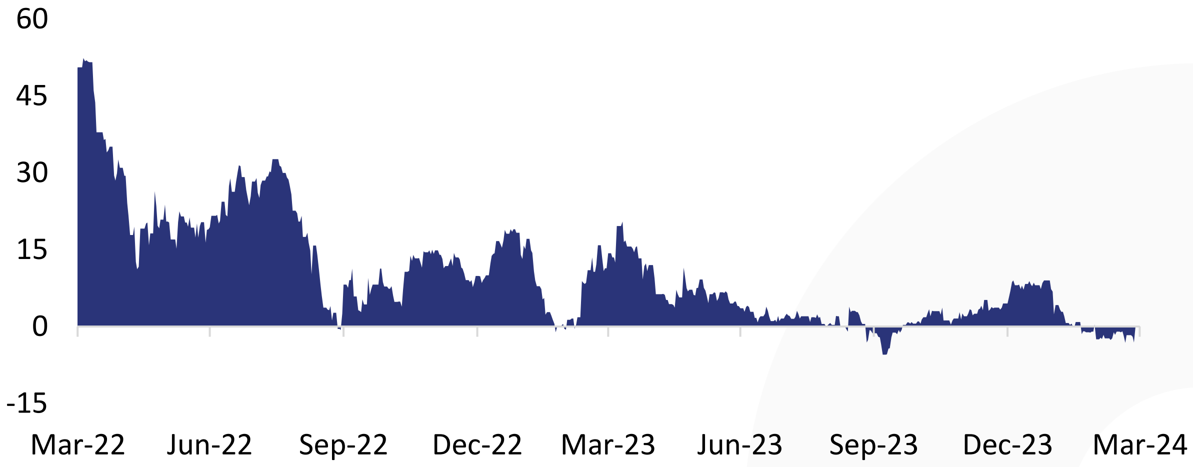
Source: Bloomberg, RBI, SBICAPS

INDIAN YIELDS REMAIN STABLE DESPITE GLOBAL VOLATILITIES

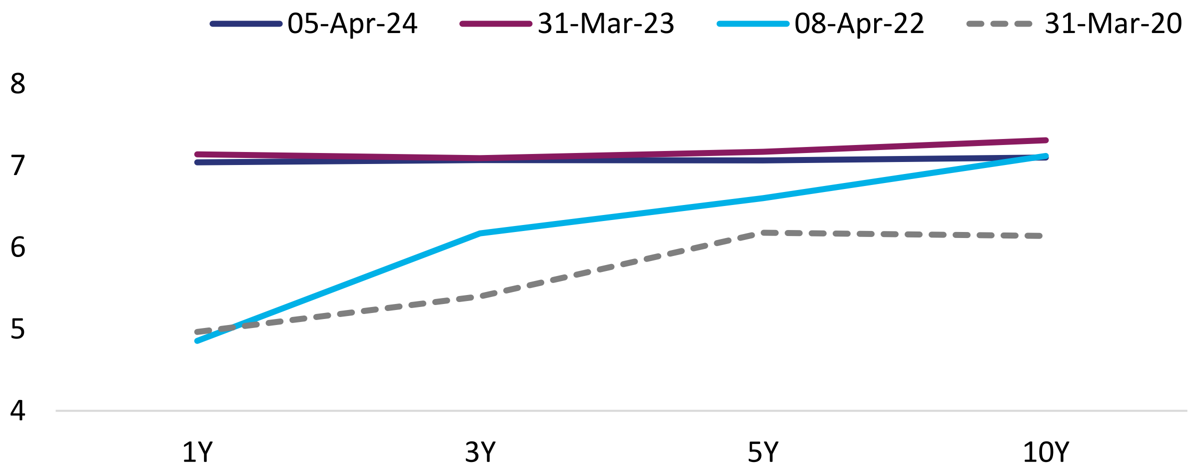
G-SEC YIELD – 10Y (IN %)



10Y-5Y G-SEC SPREAD (IN BPS)



EVOLUTION OF YIELD CURVE (IN %)



- Despite widely oscillating US 10-year yields over the past couple of months, Indian yields have largely remained stable
- Scanty inversion between 10 and 5 year and flattish curve is expected to reverse once RBI alters policy (stance followed by rates) only after Aug'24, as per our forecasts
- 10 year yield expected to trend lower than 7% in the near term, led by multitude of factors aforesaid

Source: Bloomberg, SBICAPS

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