RBI Monetary Policy Review

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RBI keeps repo rate unchanged at 6% for the fourth time; Central bank's stance signals positive change

The RBI Governor Urjit Patel-led monetary policy committee (MPC) maintained status quo on repo rate - at 6 per cent for the fourth time and retained its "neutral" stance, in its first bi-monthly policy review of 2018-19. The policy decision was in line with the market expectations. Reverse repo was kept unchanged at 5.75 per cent. No changes were made to cash reserve ratio (CRR) and statutory liquidity ratio (SLR), which stand at 4 per cent and 19.5 per cent. The statement was more dovish than expected particularly because of the cut in inflation forecasts. Five on the six-member monetary policy committee voted for the decision, with one seeking a hike.

Key Policy Stance

- The RBI revised CPI inflation projection for 2018-19 to 4.7-5.1 per cent in the first half of the financial year and 4.4 per cent in the second half, including the HRA impact for central government employees, with risks tilted to the upside. The central bank believes that inflation concerns have eased substantially in recent weeks following a crash in vegetable prices, which are expected to keep price pressures soft for the next few months. Howver, rising crude oil prices, hovering around $70 dollars a barrel, looming global trade war, risks from slippages in government borrowing plans, hike in minimum support prices (MSP) for the summer-sown kharif crop for this year, and a below normal monsoon rains can; however, lead to rise in inflation.

- Moreover, the major risk to inflation according to the statement is in the area of budgets of both the central and state governments. The first part is the deficit which will add to inflation. But the other aspect is more statistical where the revised pay commission allowance on HRA across states can prolong the effect through the second half of the year just as the Central HRA allowance plays off.

- The RBI believes that the Indian economy is poised to run to a fast growth lane, with GDP set to expand 7.4 percent in 2018-19, from the projected 6.6 percent in 2017-18, amid strong investment revival signs. The RBI warned, however, that even as global growth and trade have strengthened, rising trade protectionism and market volatility could derail the global recovery.

- The MPC said that there are now clearer signs of revival in investment activity as reflected in the sustained expansion in capital goods production and still rising imports, albeit at a slower pace than in January. Secondly, global demand has been improving, which might encourage exports and boost fresh investment.

Outlook

While markets widely expected rates to remain unchanged, participants positively reacted to the central bank's comments on growth and inflation. Some macro numbers such as the easing of consumer price index (CPI) and better GDP (gross domestic product) figure and latest monsoon reports projecting the normal forecast paved the way for RBI to keep its stance neutral.

However, the RBI chose to take a cautious path. There are plenty of uncertainties around the global trade such as hardening of crude oil prices, rising gold prices, the uncertainties surrounding the globe in the wake of trade wars and the U.S. Fed move on rate hike; have all combined to add up further to the policy challenges in the near term.

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