

## RBI surprises with status quo

### Rate cut in next MPC meeting unlikely

- As against widespread expectations of a rate cut, the Reserve Bank of India (RBI) maintained the policy repo rate at 5.15% in its monetary policy meeting on 5<sup>th</sup> Dec'19. With this, the reverse repo rate also stands unchanged at 4.9%. The MPC was unanimous on its decision to maintain status quo on both rates and 'accommodative' stance.
- Not surprisingly, the RBI revised up its inflation forecast but reduced its growth forecast sharply for 2HFY20. From 3.5-3.7% earlier, the inflation projection is now revised to 4.7-5.1% for 2HFY20. Real GDP growth forecast for 2HFY20 is cut from 6.6-7.2% earlier to 4.9-5.5% now. Consequently, real GDP growth forecast for FY20 has also been reduced sharply from 6.1% earlier to 5% (down by 240bp since the Feb'19 monetary policy meet). Moreover, the inflation projection for 1QFY21 is revised upward, while the growth forecast is revised down by almost 100bp.
- Interestingly, the MPC noted that there is monetary space for future action. It also decided to continue with the accommodative stance as long as it is necessary to revive growth while ensuring that inflation remains within the target.
- Overall, an unexpected status quo confirms that the RBI prioritized rising inflation over grim economic growth. Our estimates suggest that inflation will remain close to or above 5% by Mar'20, implying that a rate cut in the next MPC in Feb'20 is highly unlikely. Further, since our projections suggest that inflation will retreat toward 4% only by 3QFY21, there is a good probability of a prolonged pause over the next 3-4 quarters.

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- **RBI keeps policy rate unchanged:** As against widespread expectations of a rate cut, the Reserve Bank of India (RBI) maintained the policy repo rate at 5.15% in its monetary policy meeting on 5<sup>th</sup> Dec'19. With this, the reverse repo rate also stands unchanged at 4.9%. The MPC was unanimous on its decision to maintain status quo on both rates and 'accommodative' stance.
- **2HFY20 inflation forecast revised upward...:** The RBI revised up its 2HFY20 inflation forecast to 4.7-5.1% from 3.5-3.7%. Further, the RBI expects CPI to stay closer to 4% in 1HFY21. Factors driving the upward revision include higher prices of vegetables, proteins, pulses, sugar etc., volatility in the financial markets, and a likely rise in crude oil prices due to geo-political tensions.
- **...and growth forecasts cut sharply:** After decade-low real GDP growth of 4.5% in 2QFY20, the RBI expects 2HFY20 growth to be between 4.9% and 5.5%, much lower than 6.6-7.2% projected earlier. Consequently, it lowered the FY20 growth forecast sharply from 6.1% earlier to 5% now (down 240bp from the Feb'19 monetary policy forecast of 7.4%). While the RBI expects past measures such as monetary easing and the government's policy initiatives to spur domestic demand, weak domestic and external demand conditions have led to a cut in the growth forecast for FY20.
- **Rate cut in next MPC meeting unlikely:** Overall, an unexpected status quo confirms that the RBI prioritized rising inflation over grim economic growth. Our estimates suggest that inflation will remain close to or above 5% by Mar'20, implying that a rate cut in the next MPC in Feb'20 is highly unlikely. Further, since our projections suggest that inflation will retreat toward 4% only by 3QFY21, there is a good probability of a prolonged pause over the next 3-4 quarters.

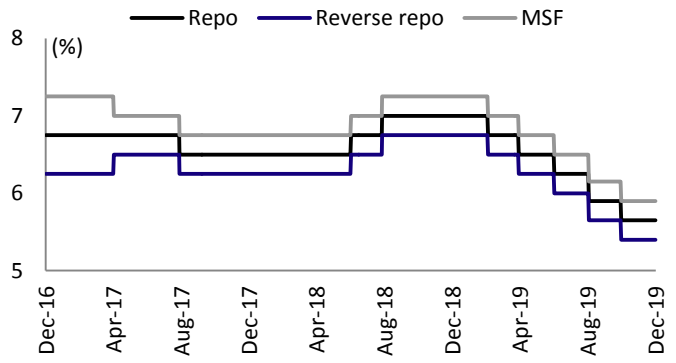
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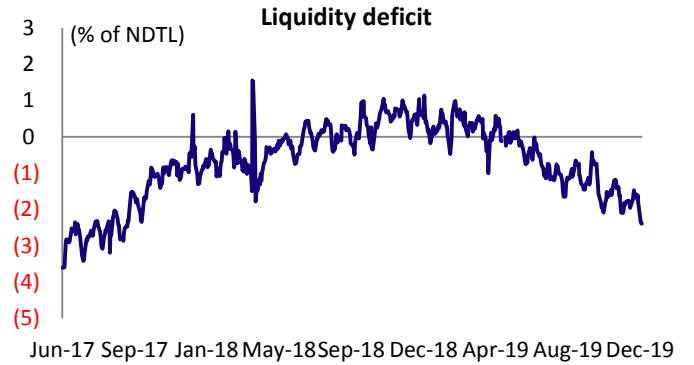
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**Exhibit 1: RBI keeps repo rate unchanged at 5.15%**



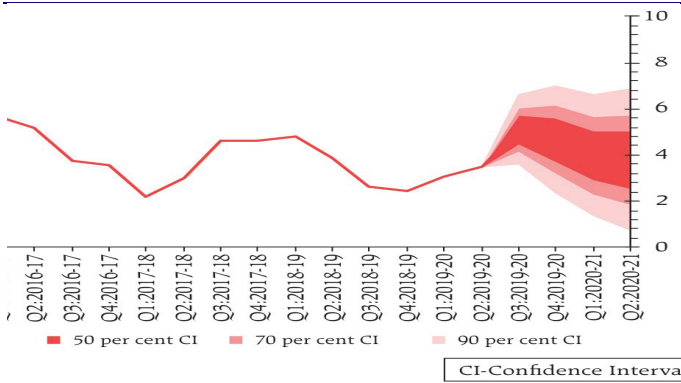
Source: RBI

**Exhibit 2: Liquidity balance in a comfortably surplus mode**



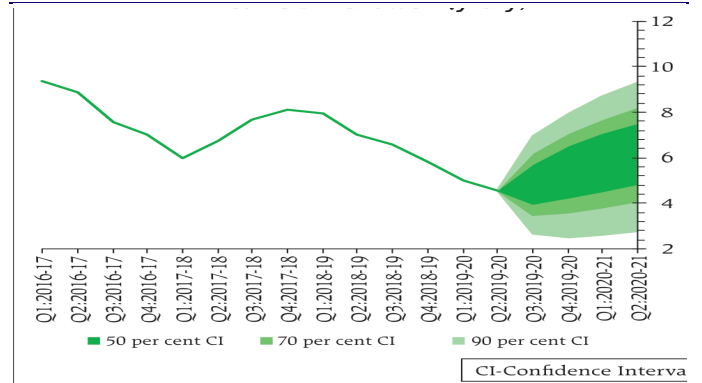
Negative data implies a liquidity surplus and vice-versa  
Data till 4<sup>th</sup> Dec, 2019  
Source: RBI

**Exhibit 3: RBI raises 2HFY20 inflation projection...**



Source: RBI

**Exhibit 4: ...but cut FY20 GDP growth forecast further**



Source: RBI

Explanation of Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
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