# Analysis of RBI Monetary Policy, February 2024

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Brickwork Ratings

# RBI Leaves Key Policy Rates Unchanged, Stresses on Sustained Efforts for Disinflation

## Key Takeaways

- Policy repo rate unchanged at 6.50%
- Standing deposit facility (SDF) rate unchanged at 6.25%
- Marginal standing facility (MSF) rate and the Bank Rate unchanged at 6.75%
- Continued focus on withdrawal of accommodation
- Medium-term target for CPI: 4% within a band of +/- 2%, while also supporting growth
- Emphasis on sustained efforts towards disinflation.

| RBI Estimates of Growth & Inflation | |
|---|---|
| **Growth** | |
| **2024-25** | **7%** |
| Q1 | 7.2%, |
| Q2 | 6.8%, |
| Q3 | 7.0% |
| Q4 | 6.9%. |
| **Inflation** | |
| **2023-24** | **5.4%** |
| Q4 | 5% |
| **2024-25** | **4.5%** |
| Q1 | 5% |
| Q2 | 4.0%, |
| Q3 | 4.6% |
| Q4 | 4.7% |

Source: RBI Monetary Policy Statements, 2023-24,February 08, 2024

The Monetary Policy Committee (MPC) at its bi-monthly meeting (December 6 - 8, 2023) kept the policy repo rate under the liquidity adjustment facility (LAF) unchanged at 6.50%. Accordingly, the standing deposit facility (SDF) rate also stands unchanged at 6.25% and the marginal standing facility (MSF) rate and the Bank Rate stand at 6.75%. The MPC's decisions are rooted in the resolve to achieve the medium-term target for consumer price index (CPI) inflation of 4% within a band of +/- 2%, while also supporting growth. The MPC reiterated its resolve to stay committed to "aligning inflation to the target" and to "remain focused on the withdrawal of accommodation to ensure that inflation progressively aligns to the target while supporting growth".

## The path of disinflation needs to be sustained

The rationale behind the decision to keep the policy rates unchanged is that the efforts to tame inflation need to be sustained and the policy transmission should be allowed to complete. Though the core inflation has moderated, significant and repetitive rises in food inflation have been impeding the pace of disinflation. Further, risks to inflation lie in the impact of geopolitical events on supply chains and volatility in international financial markets and commodity prices. The cumulative effect of a total 250 basis points hike in repo rate since May 2022 keeps working on the economy. Hence, the MPC will watch out for any effect of food prices on non-food prices which can impede the efforts for disinflation.

## RBI's take on inflation and growth

The MPC expressed optimism about the growth trajectory. The economy is in resilient mode and is supported by robust investment demand, high business sentiments, and consumer confidence. It reiterated its resolve to attain the inflation target while also supporting growth.

As per the National Statistical Office (NSO), real gross domestic product (GDP) is likely to grow by 7.3% in FY 2023-24, supported by robust public investment activity. The gross value added (GVA) saw a growth of 6.9% in FY 2023-24 on growth in manufacturing and services sectors. Growth in 2024-25 is also expected to stay strong on recovery in Rabi sowing and sustained growth in manufacturing and services. Demand side is likely to stay strong on expected rise in household consumption, pickup in private capex cycle, government's thrust on capex, high business sentiment. However, tensed geopolitical conditions, volatility in international financial markets may pose risks to the outlook.

Considering these factors, the MPC estimates real GDP for 2024-25 at 7%. It estimates the growth in Q1 at 7.2%, Q2 at 6.8%, Q3 at 7.0% and Q4 at 6.9%.

Regarding inflation, the RBI statement considers factors including the rise in inflation from 4.9% in October 2023 to 5.7% in December, driven by food prices. It also considers core inflation softening to a four-year low of 3.8 per cent in December on the cumulative effect of monetary policy actions and stance. Other factors considered are Rabi sowing surpassing the levels of last year, continuous seasonal correction in vegetable prices outlook, and crude oil prices likely to stay volatile. Further, manufacturing firms may see some softening in input costs while costs for services and infrastructure firms are likely to go higher.

Considering these factors, RBI views that the inflation trajectory would be driven by food inflation while food prices are also expected to be influenced by effective supply-side measures. It estimates CPI inflation at 5.4% for FY 2023-24 while inflation at Q4 is estimated `at 5.0%. On assumptions of a normal monsoon next year, RBI estimates CPI inflation for 2024-25 at 4.5%, with Q1 at 5.0%, Q2 at 4.0%, Q3 at 4.6% and Q4 at 4.7%

| RBI Estimates of Growth & Inflation | | |
|---|---|---|
| **Growth** | | |
| | Feb 2024 | December 2023 |
| **2024-25** | **7%** | -- |
| Q1 | 7.2%, | 6.7% |
| Q2 | 6.8%, | 6.5% |
| Q3 | 7.0% | 6.4% |
| Q4 | 6.9%. | -- |
| **Inflation** | | |
| | Feb 2024 | December 2023 |
| **2023-24** | **5.4%** | **5.4%** |
| Q1 | -- | -- |
| Q2 | -- | -- |
| Q3 | -- | 5.6% |
| Q4 | 5% | 5.2% |
| **2024-25** | **4.5%** | -- |
| Q1 | 5% | 5.2% |
| Q2 | 4.0%, | **4.0%** |
| Q3 | 4.6% | 4.7% |
| Q4 | 4.7% | -- |

Source: RBI Monetary Policy Statements, 2023-24, dated February 08, 2024 and December 08, 2023

## Announcement of new developmental and regulatory policy measures

- The RBI policy statement set out some developmental and regulatory policy measures relating to financial markets, regulations and payment systems and fintech, viz.

- The RBI would review the regulatory framework for electronic trading platforms (ETPs) introduced in October 2018. This would also take into account the market makers' requests to access offshore ETPs offering permitted Indian Rupee (INR) products.

- Resident entities would be allowed to hedge the gold price risk in the over-the-counter (OTC) segment in the International Financial Services Centre. The move would provide them enhanced flexibility and easier access to derivative products in hedging gold prices.

- All regulated entities will be mandated to provide the 'Key Fact Statement' (KFS) to the borrowers retail and MSME loans. This would benefit the borrowers in informed decision making

- With regards to Payment Systems and Fintech, to improve the security of Aadhaar Enabled Payment System (AePS) transactions, the onboarding process would be streamlined with mandatory due diligence for AePS touchpoint operators, to be followed by banks and additional fraud risk management. Also a principle-based "*Framework for authentication of digital payment transactions*" would be introduced for such transactions.

- Programmability and Offline Functionality in Central Bank Digital Currency (CBDC) Pilot would be introduced. While programmability will help users like government agencies to ensure that payments are made for the stated benefits, offline functionality in CBDC-R would facilitate transactions in areas with poor or limited internet connectivity.

## Outlook

It is a respite that the cumulative effect of rate hikes of 250 basis points is working on the economy. The RBI has raised the estimates of growth for the first three quarters of quarters of FY 2024-25 from its estimates in December 2023. It has also lowered the estimates of inflation for Q4 2023-24 and the first three quarters of FY 2024-25.

While the RBI has considered the possibility of the related impact of repetitive rise in food prices on headline inflation, it has also considered global factors including geo –political situation, expected volatility in crude oil prices and financial markets to influence inflation in India. Its macroeconomic assessment of the domestic and global economy strongly underlines the need to focus on sustained efforts towards disinflation and to watch out for spill over effect of food prices on headline inflation. Hence, as growth trajectory sustains and though the RBI may go for rate cuts by mid of FY2024-25, the target of 4% inflation prompts a strict vigil on prices including those of food

* Views are personal.

## CONTACTS

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