MPC maintains status quo to nurture growth

Brickwork Ratings, Bengaluru, 10 February 2022: The Reserve Bank of India (RBI) has maintained a status quo on policy rates and has continued the accommodative policy stance in its Monetary Policy Committee (MPC) decision announced today. Both these decisions of the MPC are in line with Brickwork Ratings' (BWR's) expectations.

Key takeaways from today's announcements

- No change in the key policy rates; repo rate maintained at 4%, reverse repo rate at 3.35%, and MSF rate at 4.25%
- Accommodative stance retained with a 5-1 majority
- The RBI projects 7.8% growth in the GDP for FY23; growth outlook retained at 17.2% for Q1FY23, Q2FY23 GDP revised downwards to 7.0% from 7.2% estimated in the MPC's December meeting
- CPI inflation outlook for FY23 pegged at 4.5%; FY22 outlook remains unchanged from the December forecast at 5.7%.
- Variable Rate Repo (VRR) and Variable Rate Reverse Repo (VRRR) auctions to operate as main liquidity management tools
- From 1 March 2022, fixed-rate reverse repo and MSF windows to be available from 5.30 pm to 11.59 pm daily

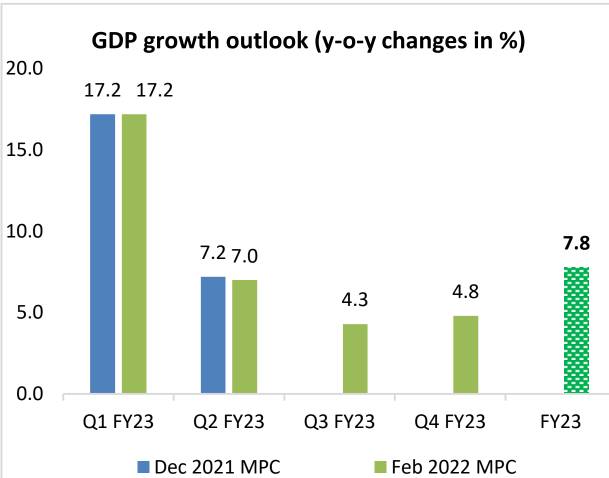
Liquidity Measures

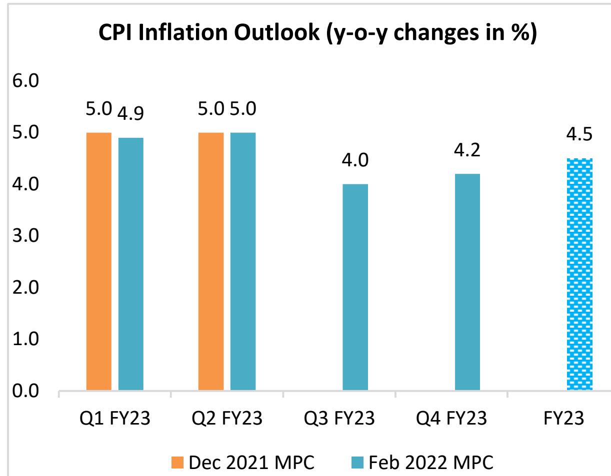
- Extension of term liquidity facility of Rs 50,000 crore to emergency health services
- Extension of on-tap liquidity window for contact-intensive sectors

Other Announcements

- Voluntary Retention Route (VRR) scheme– enhancement of limits
- Review of Credit Default Swap (CDS) guidelines
- Permitting banks to deal in offshore foreign currency settled rupee derivatives market
- Enhancement of the cap under e-RUPI (prepaid digital vouchers using UPI)
- Enabling better infrastructure for MSME receivables financing – increasing NACH mandate limit for TReDS settlements
- Master direction on its outsourcing and master direction on information technology governance, risk, controls and assurance practices

GDP and Inflation Outlook by RBI





Source: Monetary Policy Statement, BWR Research

Says Dr M Govinda Rao, Chief Economic Advisor, Brickwork Ratings, "The decision to hold policy rates by the MPC is on expected lines. The RBI's continued focus is on reviving growth reinforced by potential downside risks to economic activity from the highly contagious Omicron variant. Improving inflation outlook provides comfort for the RBI to continue with the current policy stance. The MPC was of the view that continued policy support is warranted for a sustained, durable and broad-based recovery. On the GDP guidance, the RBI forecasts 7.8% growth for FY23, which is slightly lower than the 8% to 8.5% GDP forecast made by the Economic Survey 2021-22. This, in part, may be due to the base effect arising from the revision of the GDP for 2020-21 from (-) 7.3% to (-) 6.6%. Growth concerns arising from the uncertainties related to Omicron and global spill-overs have warranted the RBI to maintain the policy rate stable to sustain the economic recovery. It has sounded a note of caution, as the persistent increase in international commodity prices, surge in volatility of global financial markets and global supply bottlenecks can exacerbate risks to the outlook. On the inflation front, the RBI sees prices softening from the current levels and forecasts an 4.5% inflation for FY23. The expectation of inflation moving within the MPC's upper range provides scope for the continuation of the accommodative policy stance. However, the forecast on inflation is largely dependent on normal monsoon and stability in international commodity prices, including other domestic factors such as demand and supply situation".

In the policy announcement, the MPC has also indicated the continuation of liquidity normalisation, keeping in view the requirements of the market. Continuing with its calibrated liquidity management policy to maintain financial stability, the RBI has proposed to extend the term liquidity facility of Rs 50,000 crore to emergency health services and Rs 15,000 crore to on-tap liquidity window for contact-intensive sectors. These announcements will help these sectors in their businesses with the availability of credit at lower rates. Permitting banks to deal in the offshore foreign currency settled rupee derivatives market helps in adding liquidity in the domestic OIS market, promotes diversity in participation and reduces the segmentation between onshore and offshore markets.

Says Rajee R, Chief Ratings Officer, Brickwork Ratings, “In line with BWR’s expectations, the RBI continued its dovish stance and remained accommodative by reiterating that despite economic recovery and aggregate demand gaining traction and improving inflation outlook, continued policy support is warranted to support domestic growth, which is the highest priority. Continuing with its calibrated liquidity management policy to maintain financial stability, The RBI has emphasized that VRR and VRRR would be the main tools for liquidity adjustment indicating gradual policy normalization on the liquidity front. While stating that headline inflation will peak in Q4 of the current fiscal, the RBI maintained its inflation projections at 5.30% for FY22 and a dovish forecast at around 4.50% for FY23. Enhancement of cap and multiple use under e-RUPI prepaid digital voucher, new CDS guidelines (to be announced today) and extension of on-tap liquidity for emergency health services and contact intensive sectors till 30 June 2022 are welcome steps. Hiking the limit under Voluntary Retention Route (VRR) Scheme from Rs 1.5 lakh crore to Rs 2.5 lakh crore will provide additional sources of capital for domestic debt markets and government securities. An increase in NACH mandate from Rs 1 crore to Rs 3 crore for TReDS related settlements is expected to improve the receivables financing and overall liquidity position of MSMEs."

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