Brickwork Ratings expects more rate cuts in upcoming RBI Monetary Policies; Slow growth rate and benign inflation will be the basis of the expectation

Brickwork Ratings, 04 October 2019, Mumbai: The Monetary Policy Committee (MPC) of the Reserve Bank of India (RBI) reduced the key policy repo rate by 25 bps to 5.15%; which is a fifth consecutive cut. The rate cut and stance both are in line with BWR expectations.

Brickwork Ratings expects the MPC to cut the repo rate further in the upcoming monetary policy meetings on the back of benign inflation coupled with slower pace of domestic economic growth.

The MPC release noted that several measures announced by the Government over the last two months are expected to revive sentiment and spur domestic demand, especially private consumption. Taking into consideration the above factors, real GDP growth for 2019-20 is revised downwards from 6.9% in the August policy to 6.1– 5.3% in Q2:2019-20 and in the range of 6.6-7.2% for H2:2019-20 – with risks evenly balanced; GDP growth for Q1:2020-21 is also revised downwards to 7.2%.

"The 25bps cut in the policy rate in addition to earlier 110 bps reduction (in last 8 months) has brought down the repo rate to 5.15%-the lowest in this decade. Expectations of benign inflation and better Rabi crop amid good monsoon, the rate cut will boost urban and rural demand. However, the slowdown in demand witnessed during the current fiscal so far has led the downward revision in the GDP growth estimates from 6.9% to 6.1%," said **Balkrishna Piparaiya, Senior Director-Ratings, Brickwork Ratings**.

Given the expectation of faster transmission of rates due to RBI directing banks to link the lending rates to external benchmark rates, the process will lead to availability of cheaper loans. Meanwhile, the recent tax sops to the corporates will also assist in lowering the selling price of goods. Thus, the agency expects this combined effect may boost the weakening demand and increase the credit flow to the corporate sector by banks. The NPA ratios of the Banks are expected to come down with credit expansion coupled with recovery in asset quality.

While more rate cuts are expected to follow, the G-Sec yields have not moved in tandem. The sops on taxation and other incentives by the GOI may cause higher fiscal deficit resulting in upward shift in the yield curve. However, in such a situation, **Brickwork Ratings** believes RBI may time the auctions and move in to take the devolvement on its books so as to maintain stability in interest rates.

"The announced rate cut coupled with the recent government's various measures announcement could see some growth in the economy. However, the sharp cut in the GDP forecast from 6.90 to 6.10 % for FY 20 could be reflection of widening negative output gap. Hence, we can expect more repo cuts in the coming MPC meetings. We may expect the CPI inflation at around 3.75 to 4% by the end of this financial year (FY20). Forex market have reacted positive to RBI announcement of allowing banks to freely offer forex price to non-residents. Further, RBI has also allowed Rupee derivative for trading at the International Finance Service centre. This would over a period of time stabilize the Rupee," said **AP Kamath, Senior Director - Ratings, Brickwork Ratings**.

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