



RBI Monetary Policy Meet Outcome – December 2024

**RBI Keeps Repo Rate Unchanged at 6.5%;
Cuts CRR by 50 bps to 4% and Lowers FY25
GDP Growth Projections to 6.6%**

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Inflation remains a pressing issue: RBI Raises Inflation Forecast for FY25 to 4.8%

Key Highlights from the RBI Monetary Policy Committee (MPC) Meeting:

• Repo Rate Unchanged

- The Reserve Bank of India (RBI) has decided to maintain a steady repo rate of 6.5% due to rising inflation and slowing India's GDP growth, which has reached a seven-quarter low of 5.4% for the July-September 2024 period
- This marks the 11th consecutive meeting where the rate has remained unchanged since February 2023, reflecting the central bank's cautious approach amid challenging economic conditions
- The committee's decision, based on a 4:2 majority, was made cautiously due to ongoing inflationary pressures and a slowing economic growth outlook

• Cut in Cash Reserve Ratio (CRR)

- The RBI has reduced its Cash Reserve Ratio from 4.5% to 4%, with the aim of improving liquidity and potentially reducing borrowing costs

• GDP Growth Projections Revised Downwards

- The RBI revised its FY25 GDP growth forecast to 6.6%, down from 7.2%, due to sluggish economic activity, with Q2 FY25 GDP growth at a seven-quarter low of 5.4%

Real GDP Growth Estimates		
Period	Current Forecast	Previous Forecast
FY 2024-25	6.6%	7.2%
Q3	6.8%	7.4%
Q4	7.2%	7.4%
Q1 FY2025-26	6.9%	7.3%
Q2 FY2025-26	7.3%	-

• Inflation Forecast Adjustments

- The inflation projection for FY25 was revised upwards to 4.8%, up from the earlier estimate of 4.5% driven by volatile food prices, which led to a CPI increase of 6.21% in October 2024

Inflation Estimates		
Period	Current Forecast	Previous Forecast
FY 2024-25	4.8%	4.5%
Q3	5.7%	4.8%
Q4	4.5%	4.2%
Q1 FY2025-26	4.6%	4.3%
Q2 FY2025-26	4.0%	

• Monetary Policy Stance

- The RBI maintained a 'Neutral' monetary policy stance, allowing flexibility to adapt to changing economic conditions while maintaining a balance between inflation control and growth support. The RBI has maintained its current interest rate despite calls for a cut to support economic growth due to concerns about price stability

• Future Outlook and Challenges

- RBI Governor Shaktikanta Das predicts a potential bottoming out of domestic activity due to festive demand and increased rural activity, but concerns remain about restrictive policies' impact on economic momentum

- Marginal Standing Facility (MSF)** and **Standing Deposit Facility (SDF)** rates has remained unchanged at 6.75 and 6.25, respectively

BWR ANALYSIS AND VIEW

This decision by the RBI comes as it aims to balance economic growth and inflation, with the MPC's cautious stance addressing concerns over high food prices and global economic uncertainties affecting domestic stability

The CRR cut benefits consumers seeking loans, but its impact on borrowing rates will depend on banks' response to increased liquidity and their decision to pass on benefits

The CRR cut aims to alleviate liquidity issues in the banking sector and boost lending capacity, which has been affected by reducing foreign exchange interventions and capital outflows, while maintaining moderate core inflation despite rising food prices

Maintaining Repo rate is a part of a broader strategy to balance inflation control with economic growth support, aiming to achieve sustainable inflation alignment and address growth challenges

The RBI's steady repo rate reflects a commitment to balancing inflation control with economic growth support, providing borrowers with stable borrowing costs and enabling financial planning without sudden changes

The revised GDP growth projections highlight Indian economy's challenges, but suggest certain sectors may perform well. Policymakers must navigate complexities to foster sustainable growth and manage inflation

Key Factors Influencing the RBI Decision:

• Inflation Concerns

- The RBI's decision to keep rates unchanged comes in the wake of persistent high inflation concerns, particularly food inflation, which has not shown signs of stabilizing and breached the RBI's tolerance limit in October 2024
- Retail Inflation as measured in terms of the Consumer Price Index (CPI) surged to 6.21% in October 2024, exceeding the Reserve Bank of India's target range of 2-6%, prompting the RBI to prioritize controlling price stability

• Economic Growth

- The Indian economy is experiencing a slowdown, with GDP growth at 5.4% in the July-September 2024 quarter, and the RBI is focusing on balancing inflation control and supporting economic growth. This slowdown has raised concerns regarding the overall economic momentum

• Cash Reserve Ratio (CRR) Adjustment

- In addition to keeping interest rate unchanged, the RBI has announced a 50 basis point cut in the Cash Reserve Ratio to 4%, aiming to improve liquidity in the banking system and support economic activity
- The decision to cut CRR marks the first since March 2020 and aims to inject approximately Rs 1.16 lakh crore into the banking system, enhancing liquidity and supporting economic growth amid high inflation and a slowdown in GDP
- The cut in CRR will be implemented in two equal tranches of 25 basis points each, effective from December 14 and December 28, 2024

Impact of CRR cut on Borrowing Rates

The RBI's reduction in the Cash Reserve Ratio is expected to significantly affect consumer borrowing rates

- **Increase Liquidity:** The CRR cut will inject Rs 1.16 lakh crore into the banking system, boosting liquidity and enabling more flexible lending
- **Potential Reduction in Borrowing Rates:** With more liquidity, banks may lower lending rates to attract borrowers, resulting in reduced interest rates on personal loans and mortgages, typically signalling downward interest rate adjustments
- **Stability of Existing Rates:** The RBI maintains a repo rate despite the CRR cut, indicating that while borrowing costs may decrease due to increased liquidity, they may not significantly decrease in the short term
- **Home loans** linked to repo rates provide stability for borrowers amid rising housing prices, ensuring no changes in interest rates or EMIs, making it crucial for managing finances in fluctuating economic conditions
- **For New Borrowers:** Borrowers can expect consistent interest rates for new loans, promoting borrowing without fear of immediate rate hikes

Impact on Specific Sectors

The CRR cut is expected to have significant implications across various sectors

1. Banking Sector

- **Increased Liquidity:** With the cut in CRR, the banks will have more liquidity, which can boost their Net Interest Income (NII), allowing them to effectively deploy freed-up funds
- **Net Interest Margins:** The CRR cut is expected to be net interest margin accretive for banks, potentially lowering borrowing costs for consumers and businesses

2. Real Estate Sector

- The banking system's increased liquidity could potentially enhance lending conditions for real estate developers and buyers, potentially increasing housing demand and construction activities

BWR ANALYSIS

Going ahead, RBI Governor Shaktikanta Das predicts that persistent food price pressures will likely keep inflation high in the near term, especially during the December 2024 quarter

RBI expects record kharif production is expected to lower staple prices, while adequate soil moisture and reservoir levels are predicted for a good rabi season, thereby reducing food inflation pressures

RBI expects record kharif production should ease elevated rice and tur dal prices, while vegetable prices are expected to experience a seasonal winter correction

3. Automobile Sector

- Banks' improved lending capacity could lead to increased vehicle loan offerings, potentially boosting the automobile sector's growth

4. Micro, Small, and Medium Enterprises (MSMEs)

- The CRR cut is expected to enhance credit access for the MSME sector, promoting efficient working capital management and operational modernization, thus enhancing their competitiveness

5. Consumer Durables

- Banks may offer easier financing options for consumers purchasing high-ticket items, similar to the automobile sector, potentially leading to increased sales in consumer durables

6. Infrastructure Projects

- Improved liquidity conditions may increase the willingness of banks to finance long-term infrastructure development projects

7. Overall Economic Growth

- The RBI's CRR cut is part of a broader strategy to stimulate economic growth by easing liquidity constraints, encouraging spending and investment across various sectors

RBI Revised GDP Growth Projections

- The RBI has revised India's GDP growth projections lower for the financial year 2025, from 7.2% to 6.6% during its monetary policy meeting on December 6, 2024 due to a slowdown in economic growth, with the July-September 2024 quarter's GDP growth at 5.4%
- RBI Governor Shaktikanta Das reported a sharper than anticipated slowdown in manufacturing, indicating a "bottomed out" domestic economy in Q3 2024, and expressed cautious optimism about a recovery in industrial activity

The downward revision of India's GDP Growth Projections was influenced by several critical factors:

1. Weak Manufacturing Performance

- The manufacturing sector experienced a significant slowdown, leading to a seven-quarter low in GDP growth, primarily due to poor performance in the manufacturing and mining sectors

2. Moderation in Investment Demand

- Investment demand has witnessed a notable decline, causing a slowdown in growth momentum and raising concerns about the sustainability of economic recovery

3. Decline in Government Capital Expenditure

- Government capital expenditure growth decreased from 14% in previous years to 4.4% in the first half of FY25, causing delays in infrastructure projects and public sector investments, affecting economic momentum

4. Global Economic Factors

- The RBI and government officials attribute the economic slowdown to geopolitical turmoil and global supply chain disruptions, resulting in increased inflation and market uncertainty

5. High Inflation Rates fuelled by rising food prices and other factors, limiting consumer spending and economic activity

6. Structural Challenges

- Economists argue that the slowdown is due to deeper structural issues in the economy, such as weak private investment and stagnant manufacturing output, which could compromise long-term growth prospects

RBI Announced Strategic Measures to Attract Capital Inflows

1. RBI Raises Interest Rate Ceilings on FCNR-B Deposits

- In a move to attract more capital inflows, the RBI has raised interest rates on Foreign Currency Non-Resident (FCNR-B) deposits to boost foreign investor appeal and support the Indian rupee amid global economic uncertainties and capital outflows

Impact of this on Foreign Investment

- **Increased Attractiveness of Indian Deposits:** The RBI has increased the interest rate ceiling on FCNR-B deposits to overnight Alternative Reference Rate (ARR) plus 400 basis points for maturities ranging from 1 to 3 years and 500 basis points for maturities above 3 years, potentially increasing capital inflows into India
- **Competitive Edge Against Global Rates:** Indian deposit rates may gain a competitive edge against global rates due to recent US Federal Reserve cuts, as investors seek higher yields and draw capital away from lower-yielding assets
- **Currency Stability:** Foreign capital can stabilize the Indian rupee against major currencies, lowering import costs and potentially challenging exporters. A stable currency is favourable for foreign investors seeking predictable returns
- **Sectoral Benefits:** Foreign investment boosts sectors like infrastructure, technology, and consumer goods, promoting growth and expansion, thereby attracting more investment
- **Long-term Confidence:** The RBI's proactive measures to boost deposit rates signal a commitment to maintaining a favourable investment climate, potentially boosting investor confidence in India's economic stability and growth prospects

2. Collateral Limit Increase for Agricultural Loans

- The RBI increased the collateral limit for agricultural loans from Rs 1.6 lakh per borrower to Rs 2 lakh, aiming to support farmers and improve credit availability in the agricultural sector
 - The higher limit enables farmers to access more funds without collateral, enhancing their ability to finance agricultural activities, purchase inputs, and invest in technology or equipment
 - This increase will provide farmers with additional resources to manage expenses related to seeds, fertilizers, and other essential inputs in the wake of rising agricultural input costs and inflation
 - The objective of raising the limit is also to encourage small and marginal farmers to participate in the formal credit system, potentially improving financial stability and reducing reliance on informal lending

3. Introduction of Secured Overnight Rupee Rate (SORR)

- The RBI has introduced the Secured Overnight Rupee Rate (SORR), a new benchmark to enhance the efficiency of the monetary policy framework. It represents a significant development in India's monetary policy framework, providing a new benchmark for short-term borrowing
 - SORR allows banks to access liquidity more quickly and flexibly without requiring collateral, especially during acute liquidity stress when banks may lack high-quality collateral
 - SORR enhances liquidity management by enabling banks to borrow without pledging securities, particularly during high cash demand periods
 - The absence of collateral requirements may facilitate a more flexible interest rate adjustment based on market conditions, enabling banks to swiftly adapt to changing liquidity requirements

4. The RBI has **proposed to link the FX-Retail platform with Bharat Connect platform of National Payments Corporation of India (NPCI)**. The integration aims to improve the efficiency and accessibility of digital payments across India, thereby facilitating the country's transition towards a digital economy

5. Pre-sanctioned Credit Lines through UPI – Extending the Scope to Small Finance Banks

- Small Finance Banks can now extend pre-sanctioned credit lines through UPI, extending the scope to new customers, a move aimed at enhancing financial inclusion and formal credit
- 6. The RBI will set up a committee to build a framework for responsible and ethical use of artificial intelligence (AI) in the financial sector
- 7. The RBI introduced Mule-hunter.AI to identify mule accounts

Implications of Revised GDP Growth Projections for Indian economy

The RBI's downward revision of GDP growth projections, will significantly impact the Indian economy in the following ways:

- **Investor Confidence**
 - The downgrade could potentially decrease investor confidence due to lower growth expectations, as brokers have adjusted their forecasts, indicating a cautious approach among investors
- **Capital Expenditure**
 - Lower growth projections may prompt businesses to reconsider or delay capital expenditures, potentially affecting job creation and expansion plans and potentially slowing private sector investment
- **Consumer Spending**
 - The services sector is resilient, but urban demand is moderating due to high base effects, potentially causing uneven consumption patterns, while rural demand may remain strong
- **Inflationary Pressures**
 - Inflation remains a concern, particularly with October's CPI at 6.21%, potentially eroding purchasing power and impacting consumer spending despite the GDP downgrade
- **Monetary Policy Adjustments**
 - The RBI's decision to maintain the repo rate suggests a cautious monetary policy amidst rising inflation and slowing growth, with future adjustments potentially necessary
- **Government Initiatives**
 - The government may implement targeted fiscal measures to stimulate growth and support sectors affected by the slowdown, including increased public spending or incentives for recovery-potential sectors
- **Sectoral Performance Variability**
 - Manufacturing sector weaknesses are expected to normalize post-monsoon, with recovery in mining and electricity output potentially supporting GDP figures in subsequent quarters
- **Global Economic Context**
 - The RBI warns of uncertain global economic conditions, with protectionist tendencies potentially impacting trade and inflation, suggesting a synchronized recovery in major economies could boost India's exports

* Views are personal.

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