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RBI ensures benign rate of interest, ample liquidity to support growth: Experts

RBI has projected India's GDP to contract by 7.5% in the current fiscal year (MINT_PRINT)

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- The RBI on Friday left interest rates unchanged for a third straight meeting as inflation stayed stubbornly high
- The MPC of RBI expects inflation to remain elevated, barring some transient relief in winter months

The RBI's decision to keep the key policy rate unchanged ensures a lower interest rate regime and availability of liquidity to support growth under the current economic situation, even as high inflation remains a risk, financial market experts said on Friday.

The Reserve Bank of India (RBI) on Friday left interest rates unchanged for a third straight meeting as inflation stayed stubbornly high, and said the economy was recuperating fast and would return to positive growth in the current quarter itself.

"The policy stance has, as expected continued to focus on reviving growth with the MPC maintaining its accommodative stance. At the same time, the statement reinforces the requirement of supply side actions to break the current inflationary spiral.

"However, not upsetting the status quo probably has been the theme with regards to liquidity management," said Rajeev Radhakrishnan, Head of Fixed Income, SBI Mutual Fund.

The Monetary Policy Committee (MPC) of RBI expects inflation to remain elevated, barring some transient relief in winter months and this has constrained monetary policy at the current juncture from "using the space available to act in support of growth", RBI Governor Shaktikanta Das said unveiling the policy review.

At the same time, the signs of recovery are far from being broad-based and are dependent on sustained policy support, he added.

Aditi Nayar, Principal Economist, ICRA said,"In our view, the adverse outlook for inflation, the concern that price pressures are spreading, and the strong commentary around monitoring threats to price stability to anchor macroeconomic and financial stability, indicate that the room for further rate cuts is negligible. However, an extended pause will mean that rates will remain low for a long period of time."

She said measures aimed at funnelling liquidity toward credit, and the signals that liquidity will not be withdrawn hurriedly, will serve well to boost sentiment, and cap yields.

Abheek Barua, Chief Economist, HDFC Bank termed as "puzzling" the absence of any major liquidity absorption measures in the midst of a prolonged inflationary episode and upward revision of both growth and inflation forecasts.

"In fact, given its emphasis on growth revival and the suggestion that there is still some more space left for monetary support, another 25-50 basis point cut in 1H CY2021 cannot be ruled out," he added.

RBI has expected the consumer price based retail (CPI) inflation at 6.8% in the current quarter of this fiscal, which is above its comfortable level of 4% with a bias of plus/minus on the either side.

However, it expects the retail inflation to moderate to 5.8% in fourth quarter of 2020-21 and further to 5.2-4.6% in first half of next fiscal year 2021-22.

The features and contents of the policy gives the reassurance that lower rates and the plenty of liquidity will continue for a longer time, till the time inflation rises so much as to derail it, said Joseph Thomas, Head of Research - Emkay Wealth Management.

"The policy is supportive of both equity and fixed income markets, with its moderating implications for rates. That all the liquidity measures initiated earlier will continue to be in force, is a consolation, especially in a high inflation scenario," he added.

Investment consulting firm Millwood Kane International's Founder & CEO Nish Bhatt said while the RBI hiking the inflation forecast is a cause of worry, the projection of growth rate swinging back to positive in Q3, Q4 indicates that the worst is over.

In its October policy review, RBI had projected retail inflation to be in the range of 5.4-4.5% during October-March period of this fiscal.

"Today's policy underscore the priority of supporting growth over near term inflation concerns. While there is little room for policy rates to move in the current situation, this MPC meeting de facto reaffirmed continuation of the liquidity support from the central bank," said Siddhartha Sanyal, Chief Economist and Head – Research, Bandhan Bank.

RBI has projected India's GDP to contract by 7.5% in the current fiscal year, as against its earlier projection of 9.55 contraction. Still, growth momentum is markedly weak and needs continued policy support, he added.

Maintaining an accommodative stance under this elevated inflation environment is a risk, but augurs well for the bond market that had started showing signs of tightening especially for NBFCs, said Rajat Bahl, Chief Knowledge Officer, Research Division Brickwork Ratings.

Amar Ambani, Senior President and Head of Research - Institutional Equities, Yes Securities said "Inflation will remain as a hindrance for next two quarters and will dissuade further policy rate cuts at least for FY21."

"The fact that liquidity remains high, while growth is gaining traction, makes us believe that RBI will adopt a wait and watch approach for next few months. Nevertheless, the MPC reiterated its accommodative stance given the transitional phase the economy is going through, in terms of recovery from the pandemic," Ambani said.