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RBI may keep rates on hold

The six-member rate setting panel (MPC) is meeting for three days starting Monday with the outcome being announced on Wednesday

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Mumbai: With the uncertainty around the new Covid omicron variant, the monetary policy committee (MPC) of the Reserve Bank of India (RBI) is likely to opt for status quo on interest rates and the accommodative stance in the monetary policy this week while continuing to drain out high banking system liquidity.

The monetary policy comes against the backdrop of the global scare of omicron amidst fragile economic recovery and high inflationary pressures, but the good thing is that around 125 crore people have been vaccinated. The six-member rate setting panel (MPC) is meeting for three days starting Monday with the outcome being announced on Wednesday.

If the RBI maintains status quo in policy rates on Wednesday, it would be the ninth consecutive time the rate remains unchanged. The RBI had last cut the repo rate by a 40 basis points on May 22, 2020 to 4 per cent to boost demand, and refrained from taking any action on interest rates.

The repo rate is the rate at which the RBI lends money to banks against government securities and currently stands at a historic low of 4 per cent. A status quo on interest rates means that the home, auto and personal loans will continue to remain low.

The RBI has been asked by the central government to ensure that the retail inflation based on the Consumer Price Index (CPI) remains at 4 per cent with a margin of 2 per cent on either side.

M. Govinda Rao, chief economic adviser at Brickwork Rating, said, "The accommodative stance will still continue as inflation is below the MPC's upper bound target of 6 per cent. But they may start draining out the excess liquidity as surplus liquidity poses a problem (to inflation). The economic growth is still nascent and needs to be supported. The RBI will also take note of the US Federal Reserve that has decided to stop bond purchases and could start draining liquidity by reducing open market purchases (OMO)."

A sharp pickup in services supported by a weak base helped the country clock a strong 8.4 per cent real GDP growth in the September quarter. On the other hand, the October headline CPI inflation rose to a more than expected 4.48 per cent from 4.35 per cent in September despite favourable base effects. Around 87 per cent of the 13 bps increase in headline was on account fuel prices.

System liquidity still remains in surplus, with the average daily net absorption under the liquidity adjustment facility at Rs 7.6 lakh crore in November. However, the RBI has made progress towards liquidity normalisation since the October policy, with the amount parked in overnight fixed reverse repo dipping to Rs 2.6 lakh crore from Rs 3.4 lakh crore at pre-October policy. The RBI has also largely achieved its objective of pushing up short-term rates, with the three-month treasury bill, which was below reverse repo for the major part of August, now at 3.52 per cent. Similarly, the six month and one-year T-bill rates have shifted upwards by 20-30 bps since the last MPC meeting.

"With uncertainty around the new Covid variant, the RBI would possibly wait for some clarity before moving decisively on rates," said Kotak Economic Research.