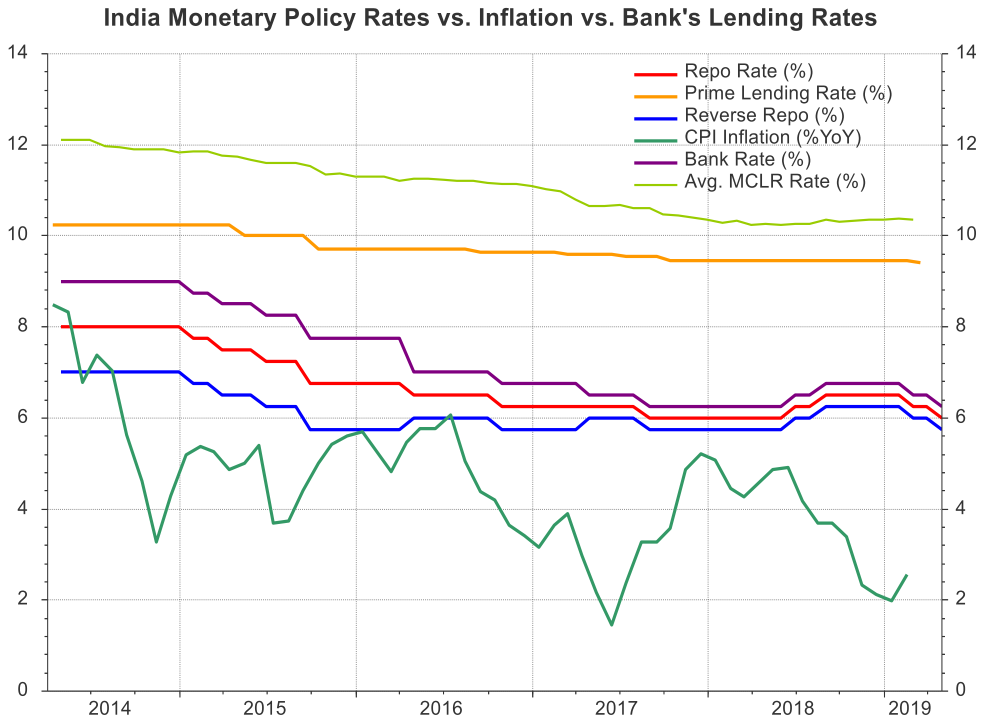
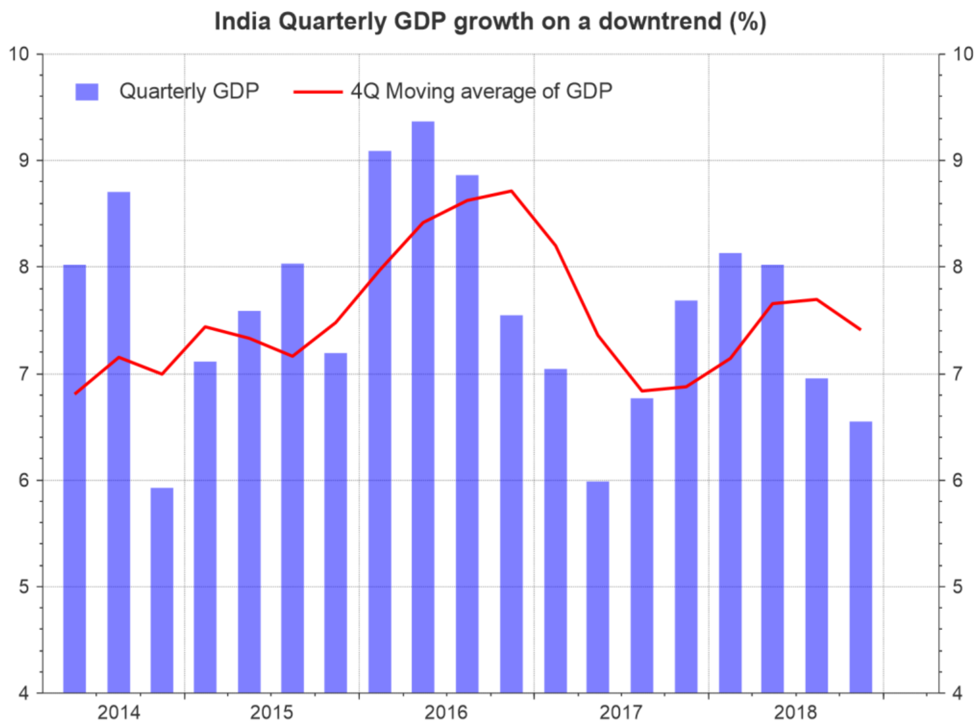
RBI cuts repo by another 25bps on expected lines

Policy rates were eased by 25bps in the first monetary policy statement of the fiscal, in line with a weak inflation and growth outlook for FY19 that is expected to continue next year as well. This was the second rate cut for 2019, with the first seen in the February policy. Outlook for consumer inflation remains benign in the near-term, but a number of impending risk factors prevented a change in the stance to 'Accommodative' from 'Neutral'.

Cheaper cost of funds follow a leaner growth/inflation scenario: FY20 Growth at 7.2% vs. 7.4% earlier; H1FY20 Inflation at 2.9-3.0% vs. 3.2-3.4% earlier. The statement also provided guidance on a number of developmental/regulatory policies.

- **Second rate cut of 2019**: The central bank has reduced the policy repo rate by another 25bps to 6.0%. In line, the reverse repo rate now stands at 5.75%, while the bank rate/Marginal Standing Facility (MSF) rate are at 6.25%. In the February policy meet, the RBI had projected Q4 FY19 inflation at 2.8%, while the actual inflation for January and February is close to 2.3%. This provided additional room for a cut that translated into the policy decision seen this time.
- **Inflation outlook remains benign**: The path of CPI inflation for FY20 has been revised downwards to 2.4% in Q4FY19 (vs. 2.8% earlier), 2.9-3.0% in H1FY20 (3.2-3.4% earlier) and 3.5-3.8% in H2FY20, with risks evenly balanced. This decision was taken based on several factors such as (1) low food inflation to impact near-term inflation outlook, (2) drop in fuel inflation has become more prominent, (3) core inflation (ex-food ex-fuel) has come lower than expected, (4) uncertainty in international crude oil prices, and (5) inflation expectations of households has moderated. Going forward, however, one could also see a reversal in the inflation trajectory—the recent Skymet projection for the summer monsoon has been tepid with expectations of *El-Nino* conditions appearing, and vegetable prices have a tendency to shoot up in summer, posing risks on the biggest component of the inflation basket, food and products.
- **GDP growth likely to slow down**: The RBI has also reduced India's growth forecasts for this fiscal, with GDP in FY20 projected at 7.2% (from 7.4% earlier) – in the range of 6.8-7.1% in HI FY20 and 7.3-7.4% in H2 with risks evenly balanced. India's output gap remains negative with concerns arising from both domestic and global factors; domestic investment activity has weakened on lower production and weak trade activity, while uncertainties surrounding the trade war and volatile oil prices continue to pose headwinds on global demand.
- **Feb 12 circular; a new hope**: Reiterating the RBI's commitment to addressing the NPA problem, Governor Das stated that the central bank will issue a fresh circular to banks on stressed asset resolution after the Supreme Court this week set aside the regulator's previous circular of February 12th, 2018, that had mandated a timeline-based procedure for lenders to refer large borrowers to the IBC, in the absence of a rescue plan within six months. The Governor also clarified that the Supreme Court's order did not cast any doubt on the powers of the RBI either under section 35AA of the Banking Regulation Act or under any other section.
- **Way forward**? Amidst the following inflation and growth outlook, we believe there is room for an incremental 25bps easing in this fiscal, *ceteris paribus*. Unfolding of the SW monsoons by June, and the global growth scenario would be key indicators that would dictate the rate trajectory going forward.





Source: RBI, Thomson Reuters

Decoding the Developmental and Regulatory Policies

Sr. No	Policy	What does it mean?	Notes
1	Liquidity Coverage Ratio (LCR), Liquidity Risk Monitoring Tools and LCR Disclosure Standards	Banks will be allowed to reckon an additional 2% of Government securities within the mandatory SLR requirement for the purpose of computing liquidity coverage ratio.	Provides more breathing space for banks towards meeting their liquidity requirements.
2	Committee on the Development of Housing Finance Securitisation Market	To propose measures to further develop the housing finance securitisation markets in India after assessing global practises	Could have significant implications on mortgage finance in India.
3	Task Force on the Development of Secondary Market for Corporate Loans	The Task Force will study global practises so as to propose measures to develop the secondary market for corporate loans in India (currently dominated by NPA transactions).	In the current mechanism, lenders bear the risks of default by corporates, but with sale of loans in the secondary market, these risks can be priced, and transferred.
4	Issue of Instructions on an External Benchmark	RBI delays adoption of an external interest rate benchmark as they want to have further consultations with stakeholders	Remains a WIP for now, but would be a step towards improved transparency for borrowers, with implications for the monetary transmission mechanism.
5	Countercyclical Capital Buffer (CCCB)	RBI believes that the current conditions do not require CCCB to be activated now.	This is a positive sign that the Indian banks have still not witnessed unexpected monetary circumstances (downtrend).
6	Permitting G-sec trading through International Central Securities Depositories (ICSDs)	Non-residents of India would now be allowed to undertake Government securities transactions.	Will open up a brand new channel of transactions for Government securities, which is a positive step for the debt market of India.
7	Licensing of Non-Banking Financial Companies (NBFCs) as Authorised Dealer Category II	NBFCs will now be eligible for the authorised foreign exchange dealer's license.	Likely rise in the number of last-mile players authorised to sell foreign exchange (for non-trade current account transactions).
8	Benchmarking India's Payment Systems	Indian payment systems will now be benchmarked to their global peers.	Impetus to deepening the digitisation of payments.
9	Framework for Harmonizing Turn Around Time for the Resolution of Customer Complaints and Compensation	The time taken to resolve customer complaints is still too high across all payment systems, which is why the RBI has proposed the Turn Around Time (TAT) framework	This step is in the right direction as it would ensure prompt and efficient customer service in all payment systems.
10	Convergence of PSL guidelines for housing loans between SCBs, RRBs, and Small Finance Banks	The housing loan limits for eligibility under Priority Sector Lending was only available to SCBs, but it has now been extended to regional rural banks and small finance banks as well.	This move aims to create a level playing field in this high priority area.
11	Extension of NBFC Ombudsman Scheme to cover Non-Deposit taking Non-Banking Financial Companies (NBFCs	This will bring all NBFC customers (including non-deposit taking) under the Ombudsman Scheme with customer interface and asset size of Rs 100 cr and above.	This would provide customers a cost-free and expeditious grievance redress mechanism.