MPC minutes: Members stay cautious (as) volatile food prices are the “True” core of inflation

22nd February 2024

Takeaways from the February MPC minutes

1. Minutes reveal that most members stay cautious about (food) inflation outlook

- MPC meeting with status quo decision on rates and stance (except for Varma, the dissenter on stance) saw most members (especially RBI Governor and DG Patra) showing caution towards inflation outlook
- While 4% core CPI provides relief, the RBI members are worried about food price uncertainty and volatility
  - *They well align with the paper "Are Food Prices the 'True' Core of India's Inflation?" co-authored by DG Patra in January RBI Bulletin*
- RBI Governor stays "committed to successfully navigate the last mile of disinflation"

2. Divide stays between the doves and hawks; doves are calling out for rate cut(s)

- Goyal and Varma reasserted that the high real rates (2% using the FY25 CPI forecast of 4.5%) create room for rate cut(s)
- The hawks (RBI Governor and Bhide) believe that while inflation is likely to cool towards 4.5% in FY25, there is a need to stay cautious about risks especially from food and commodity prices
- Hawks also are cautious of any pre-emptive move which can hurt the credibility of the MPC

3. Goyal calls for measures to manage liquidity and ensure that call rate is aligned with the repo rate

- Goyal is the only member who discussed about liquidity in the MPC minutes, signaling the need for steps towards liquidity management
- With weighted average call rate (WACR) staying above repo rate in past few months on tight liquidity due to unprecedented government cash balances, "(liquidity management) measures to ensure WACR largely stays at the repo rate are required"
- She believes that *"it is important to prevent illiquidity raising costs, turning into insolvency and creating BS stress"*

4. With members committed towards the 4% CPI target, we do not see policy easing prospects in the near term

- Given the cautious stance, we see the MPC maintain status quo in April with no policy change seen in the coming months
- With the RBI concerned about transmission of rate hikes, credit excesses etc we see it keep liquidity tight
- While liquidity is likely to ease on government spending by early April, the RBI is likely to use fine tuning operations to ensure that call rate stays close to the repo rate

Key statements of the members (1)

Member	Key statements (paraphrased unless in italics)
Dr. Shashanka Bhide	The growth and inflation scenarios are nearly the same as was seen in December. Growth momentum is surprisingly strong, despite the several adverse conditions. However, *"given the implications of current elevated levels of food inflation to the overall inflation pressures, and the prevailing strong overall growth, there is a need to remain focused on achieving the inflation target in a sustained way. As we had observed in the December 2023 meeting, the transmission of increases in policy rates effected up to February 2023 is still incomplete."*
Dr. Ashima Goyal	Goyal was of the opinion that **FY25 headline inflation projections of 4.5% gives room to cut** (rates). Interestingly, she was the only member discussing about liquidity. In her view, *"even if the WACR* (weighted average call rate) *exceeding the repo was due to unprecedented and extended large government cash balances, the toolkit to counter these and the many other shocks to which liquidity in India is subject to, can be expanded and activated." … (as)"*it *is also important to prevent illiquidity raising costs, turning into insolvency and creating BS* (balance sheet) *stress."*
Jayanth Varma	Varma dissented and continued to build a case for rate cut(s). In his view, *"compound average growth rate of real GDP from the pre pandemic level is quite low: 4¼% per annum from FY20 to FY24. …* Also, *real interest rate of 1-1.5% would then be sufficient to glide inflation to the target of 4%. A real interest rate of 2% creates the very real risk of turning growth pessimism into a self fulfilling prophecy."*

Key statements of the members (2)

Member	Key statements (paraphrased unless in italics)
Dr. Rajiv Ranjan	*"Core inflation has shown marked and durable signs of disinflation that gives us comfort from monetary policy perspective, but upside risks remain from food inflation…**avoiding any pre-mature move will help us guard against the biggest challenge to credibility**, i.e., having to backpedal later if faced with upside surprises to inflation. Today we are in a period of transition, which is a little delicate where neither forward guidance works nor pre-emptive policy actions."*
Dr. Patra	He opined that it is only when inflation subsides and stays close to the target lastingly that policy restraint can be eased. In his view, "***high inflation erodes purchasing power, especially for those least protected against the higher costs of essentials like food.*** *Restoring price stability is beneficial for all. Accordingly, monetary policy must remain restrictive and maintain downward pressure on inflation while minimizing the output costs of disinflation."*
RBI Governor Das	The Governor was of the view that policy imperative at the current juncture is to remain focused on achieving the 4% inflation target on a durable basis, keeping in mind the objective of growth. He firmly believes that *"we must remain committed to **successfully navigating the 'last mile' of disinflation** which can be sticky. As markets are front-running central banks in anticipation of policy pivots, any premature move may undermine the success achieved so far."*

Thank You !

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