यूनियन बैंक ऑफ इंडिया
भारत सरकार का उपक्रम
Union Bank of India
A Government of India Undertaking

RBI MPC Outcome: Status quo as expected; we see rate cuts by August

8th February, 2024

1. Status quo policy, in line with our expectations.

- MPC voted 5:1 to keep the policy repo rate unchanged at 6.50%. There was some divide in the markets with respect to a change in stance to neutral and measures on easing liquidity.

2. RBI intends to stay nimble with respect to liquidity management

- In line with our expectations, there was no incremental announcements to address liquidity deficit. The RBI appears to be comfortable in maintaining tight system liquidity.
- RBI Governor reasserted that the transmission of the cumulative 250 bps policy rate hike is still underway. Accordingly, VRRR and VRR tools to be used to actively manage system level liquidity.

3. Guidance reiterates focus on bringing inflation to 4% target on a durable basis while supporting growth

- The Governor highlighted optimistic outlook on both growth and inflation. Inflation expected to ease towards 4.5% next fiscal.
- While core inflation decline has been broad based, food inflation poses considerable uncertainty. Moreover, geopolitical developments and extreme weather events could adversely impact inflation outlook.

4. We expect a shallow rate easing cycle of 50 bps in FY25, with first repo rate cut likely in August 2024.

- Given the favourable inflation outlook we expect a shift in policy stance to ‘neutral’ in April creating conditions for rate easing later in year.
- We believe the MPC may start cutting rates by August 2024 with better visibility on inflation dynamics, monsoon progress, political stability, and fiscal path post Budget. We expect a shallow rate easing cycle of 50 bps in FY25.
- We will closely watch for a shift in liquidity stance as it will precede the start of rate cutting cycle

RBI's Policy Decision

Policy Decision	December 2023 Policy	February 2024 (Expected: Our view)	February 2024 (Actual)
Repo rate	6.50%	6.50%	6.50%
Stance	Withdrawal of accommodation	Withdrawal of accommodation	Withdrawal of accommodation
Growth Projection	Real GDP growth for FY24 revised to 7.0% (Q3: 6.5%; Q4: 6.0%). Real GDP growth for Q1:FY25 revised to 6.7% with Q2 at 6.5%; and Q3 at 6.4%. The risks are evenly balanced.	RBI likely to revise FY24 GDP growth to 7.3% (same as advance GDP estimate). High frequency data signal sustained growth resilience. FY25 growth numbers to be closely watched.	FY25 real GDP is projected at 7.0% with Q1: 7.2%; Q2: 6.8%; Q3: 7.0%; Q4: 6.9%. Risks are evenly balanced.
Inflation Projection	FY24 CPI inflation projected at 5.4% assuming normal monsoons (Q3: 5.6%, Q4: 5.2%). CPI inflation for Q1:FY25 is projected at 5.2%; Q2 at 4.0%; and Q3 at 4.7%. The risks are evenly balanced.	Inflation undershot RBI's Q3-FY24 projections by 20 bps at 5.4%. We see further cooling in inflation, with core CPI at sub-4% providing relief. We expect FY25 forecasts to be maintained.	CPI inflation for FY24 is projected at 5.4% and 5.0% in Q4. CPI inflation for FY25 is projected at 4.5%. (Q1: 5.0%; Q2: 4.0%; Q3: 4.6% and Q4: 4.7%). Risks are evenly balanced.

RBI's Policy Decision

Policy Decision	December 2023	February 2024 (Expected: Our view)	February 2024 (Actual)
Liquidity	Decided to allow reversal of liquidity facilities under both SDF and MSF even during weekends and holidays with effect from December 30, 2023. This measure will be reviewed after six months or earlier, if needed and is expected to facilitate better fund management by the banks.	RBI has preferred to keep liquidity tight since mid-Sep’23 with the deficit touching highs of c. Rs 3.5 lakh crores on elevated government cash balances. This kept the call rate closer to MSF. However, government spending has supported easing in liquidity in Feb’24. Meanwhile, the bias to keep liquidity tight remains with the RBI conducting two VRRR (variable reverse repo rate) auctions in last one week. We do not expect incremental liquidity measures, with the RBI expected to manage liquidity using VRR and VRRRs.	Adjusted for government cash balances, potential liquidity in the banking system is still in surplus. With Government spending continuing the liquidity to tightness to ease. RBI has proactively managed system level liquidity deficit using VRR and on rising government spending has undertook VRRR to absorb the liquidity surplus. Tight Liquidity has impacted short rate whereas Long term rate are stable. RBI will remain nimble in liquidity management, yet flexible and thereby will try to keep overnight call rate near to Repo rate.

RBI's Policy Decision

Policy Decision	December 2023 Policy	February 2024 (Expected: Our view)	February 2024 (Actual)
Guidance	The RBI refrained from providing any forward guidance on interest rates, given the prevailing uncertainty. Future policy decisions would depend on the evolving situation.	While the RBI would acknowledge the sharp fiscal consolidation in the Budget and cooling of core CPI to sub-4%, it is likely to continue to stay data dependent.	RBI would like to see further transmission of 250 bps hike into the system before taking any call on change in stance or to start cutting rate.

Regulatory Measures Proposed

Measures Proposed	Expected Implication
Review of regulatory framework for electronic trading platforms (ETP), put in place in October 2018 for executing transactions in financial instruments regulated by RBI.	Aims at ensuring fair access through transparent, safe, and efficient trading processes. Can make it possible to access offshore ETPs offering permitted Indian Rupee products.
Allowing resident entities hedging their exposure to gold, to hedge the price of gold in the over the counter (OTC) segment in the International Financial Services Centre (IFSC).	This will provide resident entities more flexibility and easier access to derivative products in hedging their exposure to gold prices.
Lenders will be required to provide their retail and MSME borrowers a Key Fact Statement (KFS) containing the key information regarding a loan agreement, including all-in-cost of the loan, in simple and easy to understand format.	Providing critical information about the terms of the loan agreement, including all-inclusive interest cost, will benefit the borrowers in making an informed decision.

Regulatory Measures Proposed

Measures Proposed	Expected Implication
To streamline the onboarding process, including mandatory due diligence, for AePS (Aadhaar enabled Payment system), touchpoint operators, to be followed by banks.	The measure is aimed at enhancing the security of AePS transactions and providing additional fraud risk management.
To adopt a principle based “Framework for authentication of digital payment transactions”.	The payments ecosystem has largely adopted SMS based one time password (OTP). With innovations in technology, alternative mechanisms have emerged in recent years. The proposal is in line to facilitate the use of such mechanisms for digital security.
Introduction of Programmability and Offline Functionality in Central Bank Digital Currency (CBDC) Pilot in gradual manner to expand reach beyond the currently enabled Person to Person (P2P) and Person to Merchant (P2M) transactions using Digital Rupee wallets provided by pilot banks.	Programmability will permit users like government agencies and corporates to program and ensure specified expenditures. Validity period and geographical area for usability of CBDC can also be programmed. Offline functionality will enable transactions in areas with poor or limited internet connectivity.

Research Team

1. Kanika Pasricha
2. Sujit Kumar
3. Suneesh K
4. R Gunaseelan
5. Nidhi Arora
6. Rajesh Ranjan
7. S. Jayalaxmi
8. Jovana Luke George
9. Ashish D Dhok
10. Ajinkya Tawde
11. Kanhaiya Jha
12. Manish Gupta
13. Rohit Yarmal

Thank you!