SHRIRAM Insight

09 February 2018

ECONOMIC UPDATE

RBI
6th Bi-Monthly Policy

RBI maintains status quo in 6th bimonthly policy

On expected lines the RBI in its 6th and final monetary policy review for the fiscal year, retained policy rates and has detailed its concerns about the prevalent and building inflation risks. The RBI continues to maintain a neutral policy stance indicating that it does not foresee an immediate surge in price levels.

The main considerations underlying the decision:

- Improvements in global and domestic economic environment.
- Sustained increase in domestic consumer price index (CPI).
- Increase in core inflation in November'17 and December'17 (CPI inflation excluding food & fuel).
- Elevated household inflation expectations.
- Deceleration in rural wage growth and firmness in organized sector wage growth.
- Prevalence of surplus liquidity in the system, which is moving towards neutrality.

Particulars	Current rates	Previous rates
Repo	6%	6%
Reverse Repo	5.75%	5.75%
Marginal Standing Facility Rate and Bank Rate	6.25%	6.25%
Cash Reserve Ratio	4.0%	4.0%
Statutory Liquidity Ratio	19.50%	19.50%

RBI Outlook for Inflation and Economic Growth

- The RBI has marginally raised its expectations for inflation in H2FY18 from its earlier target of 4.3-4.7% to 4.8% (average of Q3 and Q4). It expects inflation to inch up 5.1% in Q4 FY18 from 4.6% in Q3 Fy18.
- Inflation in FY19 is estimated to be 5.1-5.6% in H1 and 4.5-4.6% in H2. It is to be driven by the (i) Firming of international crude oil prices, (ii) Increase in non-oil international raw material prices and (iii) Indian Monsoons (expected to be normal).
- The RBI has detained the upside risk to inflation for the coming months. These include (i) The impact of HRA increases by the state governments ii) Rise in crude oil prices with the rise in global growth.(iii)Proposed revision in MSPs (minimum support price) of kharif crops (iv) Increase in custom duties on various items (announced in the budget) (v) Fiscal slippages (vi) Normalization of monetary policy in developed economies.
- GVA growth is projected at 6.6% for FY18, lower than the 6.7% growth estimated in its Dec'17 policy meet.
- Economic growth for FY19 is estimated to be 7.2% (7.3-7.4% in H1 and 7.1-7.2% in H2) and is expected to be influenced by the stabilization of GST implementation, revival in investment activity and recapitalization of banks and resolutions under IBC (Insolvency and Bankruptcy Code), which would help improve credit flow and fresh investments.

Developmental and Regulatory Policies Announced

- GST-registered Micro, Small and Medium Enterprises (MSMEs) with aggregate exposure of less than Rs. 250 million will be granted extension of max. 180 days to repay the unpaid dues between Sept'17-Jan'18 to banks and NBFCs, without a downgrade in the asset classification.
- The existing credit caps of Rs. 50 mn per borrower for micro and small and Rs. 100 mn per borrower for the classification under priority sector have been done away with.
- Foreign banks with at least 20 branches need to meet the sub-targets for lending to small and marginal farmers and micro enterprises which are currently applicable to Indian banks.
- It has been decided to harmonize the methodology of determining benchmark rates by linking the Base Rate to the MCLR with effect from April 1, 2018.
- Repo directions for government securities and corporate debt will be streamlined and simplified across different collateral types to harmonize regulation and encourage wider participation.
- NRIs will be allowed to dynamically hedge their currency and interest rate exposures onshore using any of the permitted instruments by making necessary changes in FEMA rules.
- The users in exchange traded currency derivatives (ETCD) will be provided a single limit of US $ 100 mn per user in all exchanges combined as against to existing up to US $ 15 mn per exchange for USD-INR and US $ 5 mn per exchange for other currency pairs involving the Rupee.
- Ombudsman Scheme for NBFCs has been introduced to provide customers with a grievance redressal mechanism for all deposit taking NBFCs and those with customer interface having asset-size of Rs. 1 bn and above
- Financial Benchmarks India Pvt. Ltd (FBIL) will be standardizing the GSec valuations and also will compute and disseminate of the daily "Reference Rate" for Spot USD/INR and other major currencies against the Rupee.
- The incentives for installation of Cash Recycler Machines (CRMs) and Automated Teller Machines (ATMs) have been discontinued. Some implications are - Policy aims at better transmission of interest rates changes by linking base rate with MCLR. - A more positive policy towards MSMEs would help increase in flow of credit to this sector.

Outlook

RBI is expected to closely track the developments on the inflation and economy front in the coming months. A loosening of monetary policy i.e. rate cut can be ruled out till H2 FY19. The April policy would be status quo unless there is a sharp increase in inflation, which is presently not expected.

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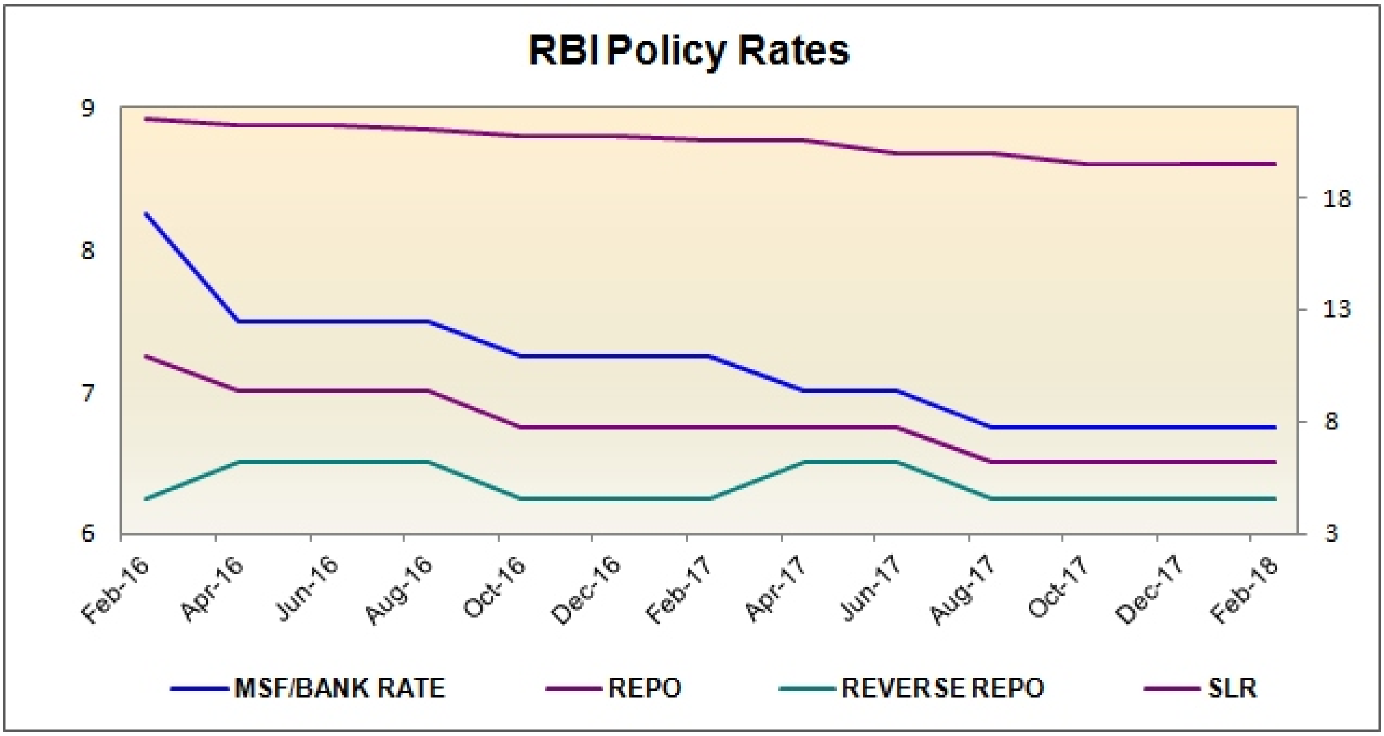

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