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THE RBI MONETARY POLICY EXPECTATIONS

07 February 2024

INTRODUCTION

The recently published ISM services data for US has increased at 53.4 in Jan'24, compared to 50.5 in Dec'23. Despite core inflation softening, in a recent interview the Fed Chairman Jerome Powell said that there is a need to wait further to ensure the recent softness of the inflation is sustainable at attaining 2 per cent target inflation rate. The market expectation, therefore, has shifted from March'24 to May-June 2024 for the first rate cut.

The RBI is also going to announce its monetary policy on 8 Feb 2024, and it is expected that RBI would not change its policy rate, namely repo rate. There is an expectation building up that the RBI could change its stance from withdrawal of accommodation towards neutral, however, it seems that the central bank would maintain both the stances unchanged.

Given the interim Budget has been presented, and India is going for the election in April'24, scope of policy manoeuvring is limited. One positive for the bond market and private sector investments is that the G-sec yield is expected to be range-bound given the gross borrowing programme by the government is set at ₹14.13 lakh crore in FY25, less than ₹15.43 lakh crore gross market borrowing programme announced in Budget 2023 for the financial year 2023-24. The net borrowing in FY25 is pegged at ₹ 11.75 lakh crore netting 2.38 lakh crore, which will be paid back during this financial year. India is in a sweet spot and tax revenues are "golden goose".



Expected dividend from RBI and PSBs though less at Rs. 1.02 trillion from Rs. 1.04 trillion (FY24) a tad 2.3 lower, still it will be the king relative to pessimistic disinvestment scenario. The key to achieve 5.1 per cent fiscal deficit in FY25 and further 4.5 per cent in FY26 is via revenue expenditure compression. However, still this may be easier said than done.

The RBI has conducted variable rate reverse repo (VRRR) auctions on 6 Feb'24 with the notified amount of ₹75,000 crore, whereas offers received from banks to the tune of ₹ 27,538 crore with a weighted average rate of 6.49 per cent.¹ On 7 Feb'24, the RBI has done another VRRR with the notified amount ₹50,000 crore as well as they would conduct another with similar amount on 8 Feb'24. The RBI conducted five fine-tuning variable rate repo (VRR) auctions (in lieu of the main operation) of 2-7 days maturity amounting to ₹5.5 lakh crore and a main operation (13 days) amounting to ₹1.75 lakh crore during December 16, 2023-January 14, 2024. Banks also took recourse to the marginal standing facility (MSF) and borrowed nearly ₹0.89 lakh crore on an average basis during December 16, 2023-January 14, 2024. The RBI continues its VRRR to realign the WACR with the repo rate to synchronised liquidity conditions.

The current CPI at 5.69 per cent in Dec'23 has increased from 5.55 per cent from Nov'23, which is marginally lower than the tolerable upper band target of the RBI (6 per cent; 4+-2 per cent). However, a positive indicator is that the core inflation has softened at 3.90 per cent and projected to fall further at 3.80 per cent in Dec'23. We have to wait for a rate cut initiation unless the RBI is confident that the inflation is declining at a sustainable basis towards 4 per cent or less than that.

¹ “Result of the Overnight Variable Rate Reverse Repo (VRRR) auction held on February 06, 2024” (6 February 2024), RBI Press Release; https://rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=57257