June 08, 2022 **ECONOMIC UPDATE**

# Monetary Policy- June 2022

## MPC hiked Repo Rate, Remains Focused on Withdrawal of Accommodative Stance

After the off-cycle meet held on 04th May, 2022 to address the concerns of inflation while at the same time being able to strike a cautious balance between demand recovery and taming inflation, the MPC was scheduled to meet from 06th-08th June for its bimonthly policy decision. While the industry veterans had already anticipated a rate hike, a major matter of concern were the standardized steps that the RBI would adopt for future policy actions along with any forward guidance and other measures to sustain the economic recovery.

***RBI hiked the repo rate by 50bps at 4.90% and continues to focus on withdrawal of Accommodative stance; reverse repo rate remains unchanged at 3.35%.***

### Highlights of Monetary Policy:

- **Repo Rate:** 4.90% (4.40% in May 2022)
- **Reverse Repo Rate:** 3.35% (3.35% in May 2022)
- **Standing Deposit Facility:** 4.65% (4.15% in May 2022)
- **Marginal Standing Facility:** 5.15% (4.65% in May 2022)
- **Bank Rate:** 5.15% (4.65% in May 2022)
- **GDP Projection**: Real GDP growth for FY23 retained at 7.2%. Q1FY23 at 16.2%, 6.2% for Q2FY23, 4.1% for Q3FY23 and 4.0% for Q4FY23
- **CPI Inflation:** Raised the forecast from 5.7% to 6.7% for FY23

### Some Highlights:

- Global economy continues to grapple with multi-decadal high inflation and slowing growth, persisting geopolitical tensions and sanctions, elevated prices of crude oil and other commodities and lingering Covid-19 related supply chain bottlenecks. CPI headline inflation rose further from 7.0% in March 2022 to 7.8% in April 2022, reflecting broad-based increase in all its major constituents
- According to the provisional estimates released by the National Statistical Office (NSO) on 31st May, 2022, India's real GDP growth in 2021-22 was 8.7%; which is 1.5% above the pre-pandemic level (2019-20). In Q4FY22, real GDP growth decelerated to 4.1% from 5.4% in Q3, dragged down mainly by weakness in private consumption on the back of the Omicron wave
- Urban demand is recovering and rural demand is gradually improving. Merchandise exports posted robust double-digit growth for the fifteenth month in a row during May
- Overall system liquidity remains in large surplus, with the average daily absorption under the LAF moderating to Rs5.5lk-cr during 04th-31st May from Rs7.4lk-cr during 08th April-03rd May, 2022 in consonance with the policy of gradual withdrawal of accommodation

### Other Measures Announced:

**(1) Regulation and Supervision:**

- **Individual housing loans by Cooperative Banks– limits enhancement:** Extant guidelines prescribe prudential limits on the amount of individual housing loans that can be extended by Primary (Urban) Co-operative Banks (UCBs), and Rural Cooperative Banks (RCBs-State Cooperative Banks and District Central Cooperative Banks) to their customers. These limits were last revised for UCBs in 2011 and for RCBs in 2009. Taking into account the increase in housing prices, the existing limits are expected to increase on individual housing loans by cooperative banks. Accordingly, the limits for Tier-I/Tier-II UCBs shall stand revised from Rs3mn/Rs7mn to Rs6mn/Rs14mn, respectively. As regards RCBs, the limits shall increase from Rs2mn to Rs5mn for RCBs with assessed net worth less than Rs1bn; and from Rs3mn to Rs7.5mn for other RCBs
- **Permitting RCBs to lend to Commercial Real Estate-Residential Housing (CRE-RH) sector:** As per the current guidelines, State Co-operative Banks (StCBs) and District Central Co-operative Banks (DCCBs) will be allowed to extend finance to CRE-RH within the existing aggregate housing finance limit of 5% of their total assets
- **Permitting UCBs to offer door-step banking:** In order to attain harmonization of regulatory framework across REs and to provide convenience of banking services to the customers at their door-step, it has been decided to permit UCBs to extend doorstep banking services to their customers on par with scheduled commercial banks

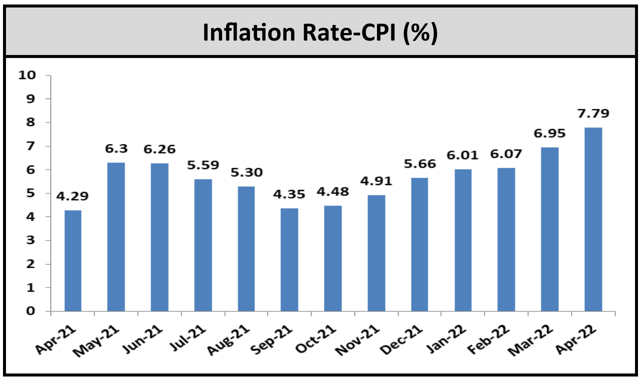
**Other Measures Announced (contd.):**

**(2) Financial Markets:**

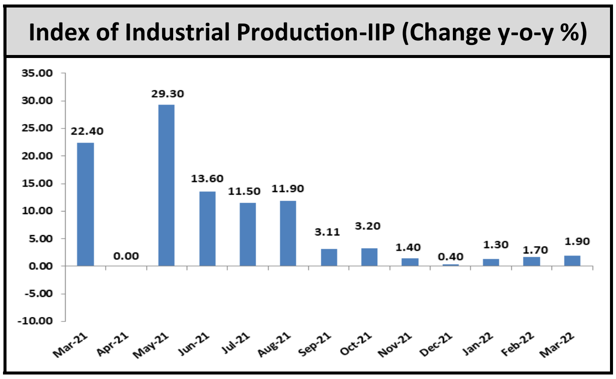
- **Margin requirements for Non-centrally Cleared Derivatives (NCCDs):** With the objective of strengthening the resilience of OTC derivative market, the RBI had earlier issued a discussion paper to implement global practices related to margin requirements for OTC derivatives. The promulgation of the Act for Bilateral Netting of Qualified Financial Contracts, 2020, ensuring legal recognition for bilateral netting of an OTC derivative transaction, has put in place a significant enabler for efficient margining. Against this backdrop, directions on exchange of Variation Margin (VM) for NCCDs were issued on June 1, 2022. Draft directions would be issued in due course

**(3) Payment and Settlement Systems:**

- **e-Mandates on cards for recurring payments:** The framework on processing of e-mandate based recurring payments provides an Additional Factor of Authentication (AFA) during registration, sending a pre-debit notification, subsequent recurring transactions to be executed without AFA, and an easier avenue to withdraw such mandates. It is proposed to enhance the limit from Rs5,000 to Rs15,000 per recurring payment
- **Enhancements to Unified Payments Interface (UPI):** UPI has become the most inclusive mode of payment in India currently facilitating transactions by linking savings/current accounts through debit cards of users. In order to further deepen the reach and usage, it is proposed to allow linking of credit cards to UPI
- **Review of Payments Infrastructure Development Fund scheme (PIDF):** The PIDF scheme was to incentivise the deployment of payment acceptance infrastructure such as physical Point of Sale (PoS), mPoS (mobile PoS), Quick Response (QR) codes in Tier-3 to 6 centres and North Eastern States. As at end-April 2022, over 1.18 crore new touch points have been deployed under the scheme. It is now proposed to make modifications to the PIDF scheme by enhancing the subsidy amount, simplifying the subsidy claim process, etc.




Source: tradingeconomics.com




Source: tradingeconomics.com

**Our View:** While the RBI has dropped the term accommodative, the panel seems to have taken very bold moves. The need for this front loading seems to be willingly or unwillingly accepted by the street, as there is no other option in the current scenario where system is pressured due to external macro-economic factors. Economies across the globe continue to deal with high inflation, slowing growth, geopolitical tensions, elevated crude oil prices, increased prices of commodities and supply chain bottlenecks adding to the fears of stagflation. These decisions are in agreement with the objective of achieving the medium-term target of CPI inflation of 4% (with a range of +/- 2%) while supporting growth. The domestic growth is indicating broadening of recovery, improving urban and rural demand coupled with growth of non-oil non-gold imports. Global geopolitical situation and elevated commodity prices add to the uncertainty to the domestic inflation, however the forecast of a normal south-west monsoon augurs well for the Kharif agricultural production and the food price outlook. Investment activities are anticipated to be supported by improving capacity utilisation, capex push by GOI and strengthening bank credit. The MPC remained focused on withdrawal of accommodation to ensure that inflation is tamed to some extent (with many uncertainties hovering), but clearly with a vision to support growth while at the same time ensure that inflation remains within the target going forward as well.

| FINAL VERDICT | | | |
|---|---|---|---|
| **MPC Meetings** | **REPO** | **REVERSE** | **CURRENT STANCE** |
| *June 2022* | *4.90%* | *3.35%* | **PARTIALLY HAWKISH** |
| **May 2022** | **4.40%** | **3.35%** | |

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