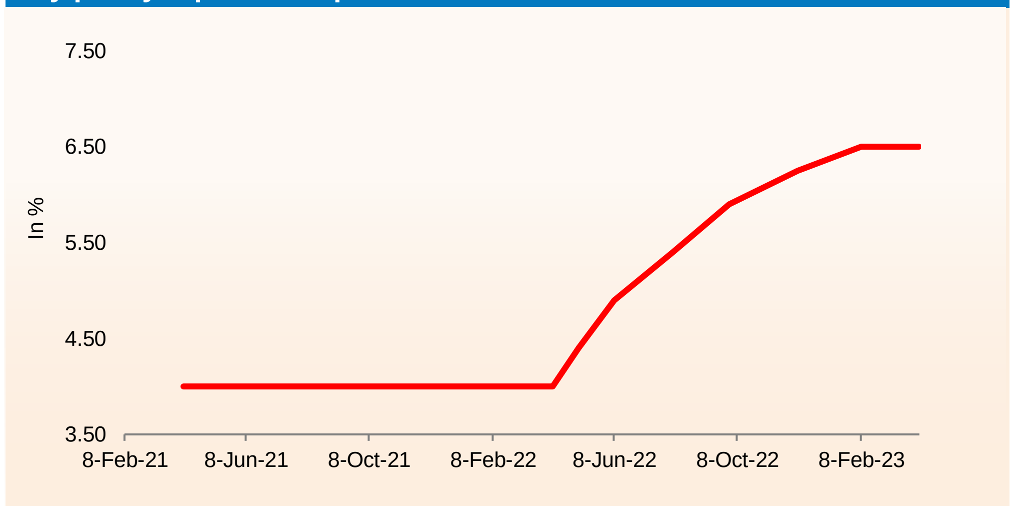
Monetary Policy Review

Summary - Stance and Rationale

- The Monetary Policy Committee (MPC) in its first bi-monthly monetary policy review of FY24 kept key policy repo rate unchanged at 6.50% with immediate effect, after six consecutive rate hikes. All six members unanimously voted to keep the policy repo rate unchanged. Since May 2022, the repo rate has been raised by 250 bps. The MPC also remained focused on withdrawal of accommodation to ensure that inflation progressively aligns with the target, while supporting growth. Five out of six members voted in favour of the same.
- Consumer inflation remained continously above the tolerance band. MPC decided to remain resolutely focused on aligning inflation with the target. Hence it is necessary to rein in the generalisation of price pressures and anchor inflation expectations. An environment of low and stable prices is required so that domestic economic activity can be sustained. Despite raising policy rates cumulatively by 250 bps since May 2022, MPC stated that there can be no room for letting down the guard on price stability. The MPC will continue to keep a strong watch on inflation and growth outlook and will not hesitate to take further action as may be required in its future meetings.

Key policy repo rate kept on hold at 6.50%

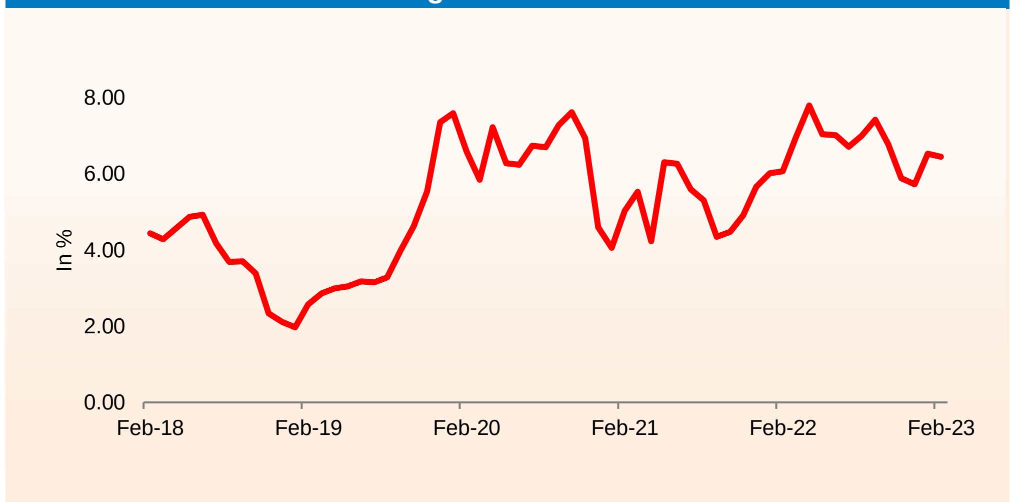


Source: Refinitiv

Inflation Outlook

- The inflation path for FY24 would be shaped by both domestic and global factors. The likelihood of a record rabi foodgrain yield is encouraging for the outlook on food prices. However, the effects of recent unseasonal rain and hailstorms need to be monitored. Increased global financial market volatility may have effects on risks associated with imported inflation.
- According to the Reserve Bank's enterprise surveys, easing cost circumstances are causing a moderating of the rate of output price increases in manufacturing and services. However, the lag in input cost pass-through might keep core inflation high.
- Taking into account above factors and assuming an annual average crude oil price (Indian basket) of $85 per barrel and a normal monsoon, CPI inflation is projected at 5.2% for FY24, with Q1 at 5.1%, Q2 at 5.4%, Q3 at 5.4% and Q4 at 5.2%.

Inflation eased from its last high

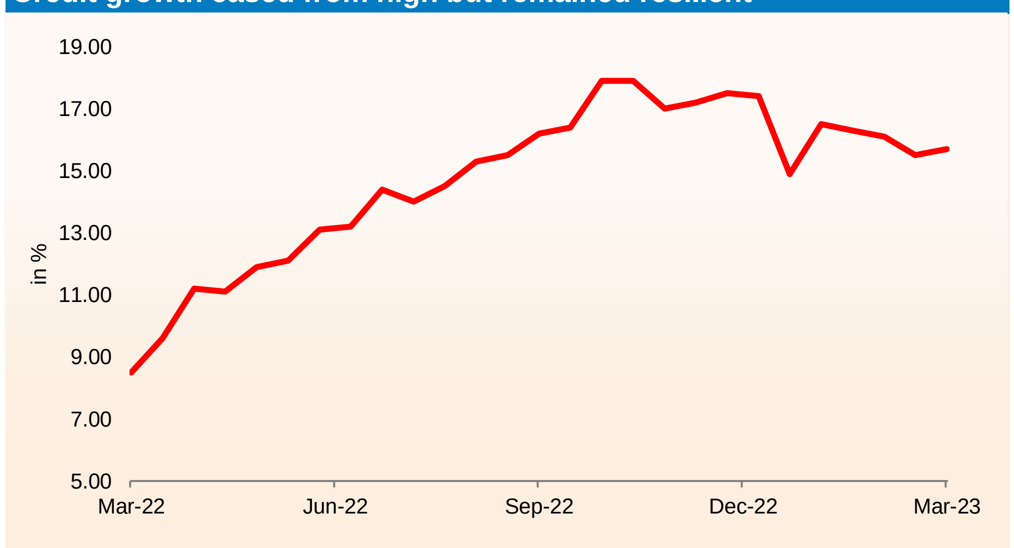


Source: Refinitiv

MPC outlook on Growth and Economy

- Stronger rural demand should result from a successful rabi harvest, and stronger urban demand should result from the ongoing expansion of contact-intensive services.
- Manufacturing and investment activities are anticipated to be boosted by the government's emphasis on capital expenditure, above trend capacity utilisation in manufacturing, double digit loan growth, and the stabilisation in commodity prices.
- Given that global commerce and output are decreasing, the external demand impact might become more pronounced. The forecast is at risk due to persistent geopolitical tensions, challenging global economic conditions, and volatile global financial markets.
- Taking above factors into consideration, real GDP growth for FY24 is projected at 6.5% with Q1:2023-24 at 7.8%; Q2 at 6.2%; Q3 at 6.1%; and Q4 at 5.9%.

Credit growth eased from high but remained resilient



Source: Refinitiv

Market Reactions

- Indian equity markets rose after the MPC surprisingly kept key policy repo rate unchanged at 6.50%. Key benchmark indices S&P BSE Sensex and Nifty 50 rose 0.24% each.
- Bond yields fell after the MPC kept key policy rates unchanged, which boosted investors sentiments. Yield on the 10-year benchmark paper (7.26% GS 2032) fell 5 bps to 7.23% as compared to the previous close of 7.28%.

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