Fact Sheet: Monetary Policy February 2020

FICCI

Sixth Bi-monthly Monetary Policy 2019-20: RBI maintains status quo

- *RBI in its Sixth Bi-monthly Monetary Policy statement, 2019-20 announced on February 6, 2020 maintained status quo on the repo rate*
- *The repo was last cut by 25 bps to 5.15 bps in October, 2019 policy announcement and has been cut by 135 bps between February, 2019 and October, 2019*
- *Consequently, the reverse repo rate under the LAF remains unchanged at 4.90 per cent, and the marginal standing facility (MSF) rate and the Bank Rate at 5.40 per cent*
- *The Monetary Policy Committee decided to maintain an accommodative stance for as long as it is necessary to revive growth, while ensuring that inflation remains within target*

Key Rates

Key rates	Feb-2019	Feb-2020
Repo rate	6.25%	5.15%
Reverse repo rate	6.00%	4.90%
MSF	6.50%	5.40%
CRR	4.00%	4.00%
SLR	19.25%	18.25%
Bank rate	6.50%	5.40%

Key Projections in Policy Statement

	Q4 FY 20	H1 FY21	Q3 FY21
CPI	6.5%	5.0-5.4%	3.2%

	FY 21	H1 FY21	Q3 FY21
GDP	6.0%	5.0-6.1%	6.2%

Factors Influencing Inflation Outlook

Policy Statement: Overall inflation Outlook Highly Uncertain

- Decline in prices expected to be more pronounced in Q4 FY20 on back of fall in onion prices as late kharif and rabi harvests arrive
- Vegetable production higher – expected to have a salutary impact on prices
- Demand conditions remain subdued – with muted pricing power of corporates and correction in energy prices will limit pass through to selling prices

- There has been a pick up in non-vegetable food prices especially milk and pulses
- Volatility in crude oil prices likely to remain as geo-political tension in Middle East remain on fore
- Increase in custom duties on items of retail consumption in the budget may result in a one time uptick in prices – though it is expected to be marginal
- Adjustment to telecom charges imparting cost-push pressures to CPI inflation

Source: *RBI's Sixth Monetary Policy Statement, Feb 6, 2020*

<u>RBI recognizes that there is policy space available for future action</u>: however pass through of remaining revisions in telecom charges, increase in price of drugs /pharmaceuticals and impact of new emission norms also pose as risks to inflation

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Factors Influencing GDP Outlook

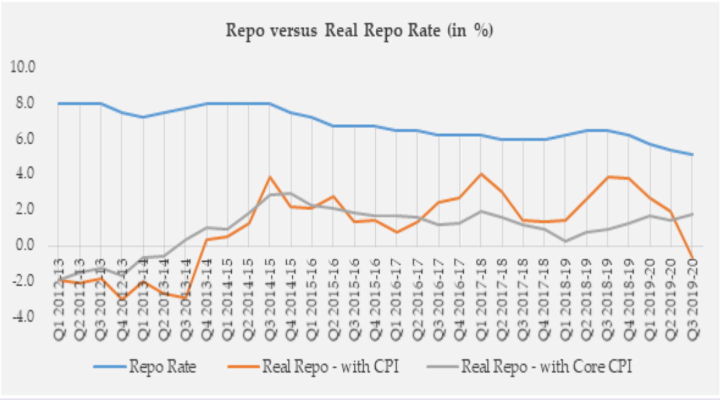
Policy Statement: Output gap remains negative

- Private consumption in rural areas is expected to recover on back of improved rabi prospects
- Rise in food prices to favor rural incomes
- Ease of global trade uncertainties to support exports and investments
- Improved transmission of monetary policy in terms of lending rates vis-à-vis last policy - to support consumption
- Rationalization of personal income tax will encourage demand

- Coronavirus breakout to impact tourist arrivals and global trade
- High frequency data though improving yet to indicate sustainable turn around
- Weak demand remains a concern and capacity utilization rates remain strained

***Source:** RBI's Sixth Monetary Policy Statement, Feb 6, 2020*

FICCI's stance

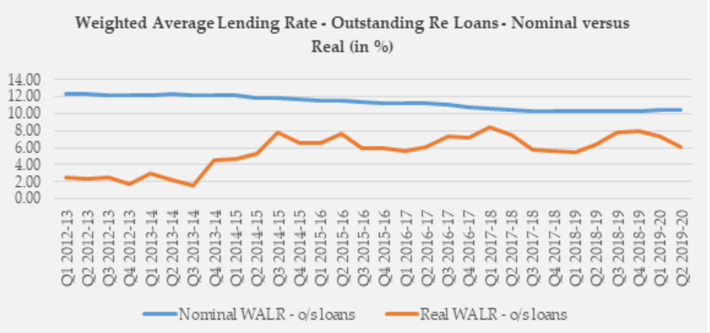


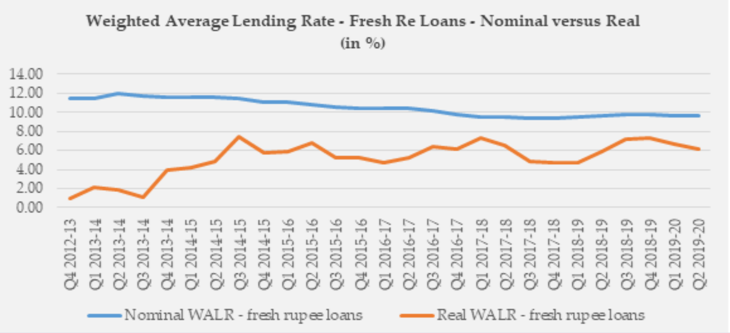
FICCI Survey Findings

- FICCI's latest Economic Outlook Survey estimates **GDP growth at 5.5% for FY21**; CPI estimated at 4.3% for FY 20
- Weak demand remains a major constraining factor for members of India Inc – **76% participants cite weak demand as a worry** in the latest Business Confidence Survey done by FICCI
- Capacity utilization rate remains poor. In the latest round of Business Confidence Survey, o**nly 28% respondents indicate a capacity utilization rate of over 75%**

- Recovery is still in a very early and fragile state
- Core inflation more reflective of demand conditions in the economy remains moderate
- Food prices increase temporary and showing some signs of coming down
- Oil prices have fallen below $50 / bbl. and are projected to remain there

A cut in repo rate by 15-25 bps would have been timely and a great sentiment booster





- Weighted average lending rates of scheduled commercial banks – on outstanding and fresh loans - remains high - close to 10 per cent
- Limited transmission of repo rate cut to the borrowers
- Banks unwilling to lend as they deal with existing NPA's and fear of vigilance action against their management - especially for larger corporate loans
- Further action to repair the larger and less fragile NBFC's would be a big help as they can revive credit in the system

Statement on Developmental and Regulatory Policies

These Additional Measures to Revive Credit Flow

Long Term Repo Operations (LTROs) for Improving Monetary Transmission

Reserve Bank to conduct term repos of one-year and three-year tenors of appropriate sizes for up to a total amount of ₹ 1,00,000 crore at the policy repo rate from the fortnight beginning on February 15, 2020.

Impact-
The measure is likely to bring down short term rates and prompt increased investment in corporate bonds. The central bank will offer funds at repo rate of 5.15 percent, thus pushing the yield on risk-free government securities of the similar tenors closer to the benchmark rate.

External Benchmarking of New Floating Rate Loans by Banks to Medium Enterprises

In pursuance of the recommendations of an Internal Study Group (Chairman: Dr. Janak Raj), all new floating rate personal or retail loans and floating rate loans to micro and small enterprises (MSEs) extended by banks were linked to external benchmarks effective October 1, 2019. Subsequent to the introduction of an external benchmark system, the monetary transmission has improved to the sectors where new floating rate loans have been linked to the external benchmark. With a view to further strengthening monetary transmission, it has been decided to link pricing of loans by scheduled commercial banks for the medium enterprises also to an external benchmark effective April 1, 2020

Impact-
The move will give a fillip to flow of funds to the MSME sector and help them access credit at competitive rates.

Incentivizing Bank Credit to Specific Sectors

Reserve Bank decided that scheduled commercial banks will be allowed to deduct the equivalent of incremental credit disbursed by them as retail loans for automobiles, residential housing and loans to micro, small and medium enterprises (MSMEs), over and above the outstanding level of credit to these segments as at the end of the fortnight ended January 31, 2020 from their net demand and time liabilities (NDTL) for maintenance of cash reserve ratio (CRR). This exemption will be available for incremental credit extended up to the fortnight ending July 31, 2020.

Impact-
Non-maintenance of CRR for additional loans will incentivize banks to lend to the specified sectors and will provide an impetus to credit growth.

Guidelines on Projects under Implementation in Commercial Real Estate sector

It has been decided to permit extension of date of commencement of commercial operations (DCCO) of project loans for commercial real estate, delayed for reasons beyond the control of promoters, by another one year without downgrading the asset classification, in line with treatment accorded to other project loans for non-infrastructure sector. This would complement the initiatives taken by the Government of India in the real estate sector.

Impact-
The move has come as a relief to the real estate sector as it will ease liquidity pressure due to repayment of debt

Extension of One-time Restructuring Scheme for MSME advances

Considering the importance of MSMEs in the Indian economy and for creating an enabling environment for the sector in its efforts towards formalization, a one-time restructuring of loans to MSMEs that were in default but 'standard' as on January 1, 2019, was permitted without an asset classification downgrade. The restructuring of the borrower account was to be implemented by March 31, 2020. The scheme has provided relief to a large number of MSMEs. As the process of formalization of the MSME sector has a positive impact on financial stability and this process is still underway, it has been decided by RBI to extend the benefit of one-time restructuring without an asset classification downgrade to standard accounts of GST registered MSMEs that were in default as on January 1, 2020. The restructuring under the scheme has to be implemented latest by December 31, 2020.

Impact –
This comes as a welcome respite to MSMEs that could not be restructured under the old scheme or have fallen under stressed category thereafter.