Fact Sheet: Monetary Policy
August 2020

FICCI

RBI leaves repo rate unchanged, allows restructuring of loans

- *RBI left the repo rate unchanged at 4.0 per cent in the monetary policy resolution announced today. The decision was unanimously backed by all six Monetary Policy Committee (MPC) members*

- *Consequently, the reverse repo rate under the LAF remained unchanged at 3.35 per cent, while the marginal standing facility (MSF) rate and the Bank Rate remained at 4.25 per cent*

- *Accommodative stance of monetary policy to be maintained as long as necessary to revive growth, mitigate the impact of COVID-19, while ensuring that inflation remains within the target. The Bank acknowledged that while space for further accommodative monetary policy action is available, it will important to use it judiciously and opportunistically*

Key Rates

Key rates	March-2020	April-2020	May-2020	August- 2020
Repo rate	4.40%	4.40%	4.0%	4.0%
Reverse repo rate	4.00%	3.75%	3.35%	3.35%
MSF	4.65%	4.65%	4.25%	4.25%
CRR	3.00%	3.00%	3.00%	3.00%
SLR	18.25%	18.25%	18.0%	18.0%
Bank rate	4.65%	4.65%	4.25%	4.25%

Outlook

Inflation

The MPC expects headline inflation to remain elevated in Q2 2020-21, before an anticipated moderation in the second half of 2020-21, aided by favorable base effects. Persistent disruption to supply chains on account of Covid-19 would have implications on both food as well as non-food prices. Elevated price levels of protein based food remain a key pressure point. Also, prices of certain vegetables have noted an increase in prices and any softening would depend on normalization of supplies. Nonetheless, a bumper rabi harvest can ensure easing of prices if open market sales and public distribution off take are expanded on back of higher procurement. The high taxes on petroleum items are expected to add to cost push pressures as well.

Growth

On the growth front, recovery in the rural economy is expected to be robust, supported by the progress in kharif sowing. Demand conditions, both domestic and external remain weak and there is considerable concern regarding that. Feedback received by RBI indicates mixed signal with regard to domestic demand. According to the Bank's Industry Outlook Survey, while manufacturing firms are expecting a recovery in domestic demand from Q2 2020-21 which is likely to sustain through Q1 2021-22, consumer confidence seems to have turned more pessimistic in the month of July. On the back of aforementioned downside risks, RBI has maintained its stance on FY21 GDP growth to be negative.

A more protracted spread of the pandemic, deviations from the forecast of a normal monsoon and global financial market volatility are the key downside risks. Successful containment of the pandemic would be the key upside to growth forecast.

Source: RBI's Monetary Policy Statement, August 6, 2020

Fact Sheet: Monetary Policy August 2020

Impact of the Monetary and Liquidity Measures taken by the RBI

- Borrowing costs in financial markets have dropped to their lowest in a decade on the back of abundant liquidity. Interest rates on instruments like the 3-month Treasury bill, commercial paper (CP) and certificates of deposit have fully priced in the reduction in the policy rate

- CPs of NBFCs have softened to 3.80 per cent on July 31, 2020. Rates have fallen to 3.40 per cent on July 31, 2020 for non-NBFC borrowers

- Spreads of 3-year AAA-rated corporate bonds over similar tenor government securities have declined from 276 basis points on March 26, 2020 to 50 basis points on July 31, 2020. Spreads on AA+ rated bonds softened from 307 basis points to 104 basis points; spreads on AA bonds narrowed from 344 basis points to 142 basis points over the same period. Even for the lowest investment grade bonds (BBB-), spreads have come down by 125 basis points as on July 31, 2020

- Lower borrowing costs have led to record primary issuance of corporate bonds of ₹2.09 lakh crore in the first quarter of (April-June) 2020- 21.

- Assets under management of Debt MFs, which fell to ₹12.20 lakh crore as on April 29, 2020 have recovered and improved to ₹13.89 lakh crore as on July 31, 2020

- The weighted average lending rate (WALR) on fresh rupee loans sanctioned by banks declined by 162 basis points during February 2019-June 2020, of which 91 basis points transmission was witnessed during March-June 2020

Regulatory & Developmental Announcements- August 6, 2020

Liquidity Management and Financial Markets

- Additional Standing Liquidity Facility of Rs. 5000 crore each to NABARD and National Housing Bank
- Introduction of a Flexible Automated Option for Managing CRR Balances

Regulation and Supervision

- Provision of a resolution window under the June 7th, 2019 Prudential Framework to enable lenders to implement a resolution plan in respect of eligible corporate exposures as well as personal loans subject to specified conditions
- Stressed MSME borrowers eligible for restructuring their debt under the existing framework, provided their accounts with the concerned lender were classified as standard as on March 1, 2020
- Permissible loan to value ratio (LTV) for loans against pledge of gold ornaments and jewellery for non-agricultural purposes increased from 75 per cent to 90 per cent
- Streamlining the Use of Multiple Operating Accounts by Large Borrowers
- Differential treatment existing currently for banks' Investment in Debt Mutual Funds and Debt Exchange Traded funds to be harmonized

Financial Inclusion

- Priority sector lending guidelines reviewed- incentive framework in place to address regional disparities; PSL status given to start-ups, limit of renewable energy increased to include solar power and compressed bio-gas plants

Payment and Settlement Systems

- A pilot scheme to be allowed for small value payments in off-line mode with built-in features for safeguarding interest of users, liability protection
- Introduction of Online Dispute Resolution (ODR) for Digital Payments
- Mechanism of Positive Pay for all cheques of value ₹50,000 and above introduced. Under this mechanism, cheques will be processed for 10 payment by the drawee bank based on information passed on by its customer at the time of issuance of cheque
- Reserve Bank Innovation Hub to be set up; to act as a centre for ideation and incubation of new capabilities

Source: RBI's Monetary Policy Statement, August 6, 2020

Fact Sheet: Monetary Policy
August 2020

FICCI's Comments

FICCI congratulates steps announced towards resolution of loans in the monetary policy by announcing restructuring of MSME loans that were in standard category till 1st March 2020 and for setting up a window under the June 7 stressed asset resolution framework to enable lenders to implement a resolution plan, without a change in ownership.

FICCI is encouraged by the guidance being provided by the Central Bank amid the current environment of continued uncertainty. Weak demand has been the key pain point for businesses and all levers need to be used to get consumption back on track. Front loading at least another 25 bps cut in the repo rate would have been well timed. The festive season has already set in and a cut in the repo rate would have given some guidance to businesses and consumers.

There has been a spurt in inflationary pressures. However, much of the stress in prices is on account of food led by lock down induced supply side distortions. Going ahead, as these constraints ease, the pressure on prices will subside and be back on RBI's indicative trajectory.

FICCI also acknowledges the impact of liquidity measures listed out by the Governor in today's statement. There has certainly been an improvement in the transmission of the past rate cuts. However, the feedback we have received from ground indicates that banks continue to remain risk averse. We would urge the banks to extend a lending arm in letter and spirit. Given that a sense of uncertainty continues to prevail for businesses, a comforting approach by the banks at this juncture is extremely critical.

The review of the priority sector guidelines is applauded. The incentive framework laid out with the objective of minimizing regional disparities is a step in the right direction. We also welcome the broadening of the scope of priority sector lending to include start-ups and inclusion of solar power and compressed biogas plants under the renewable energy limits. In fact, FICCI had been asking for these inclusions for some time now.

Further, the announcements pertaining to increase in the permissible loan to value ratio for loans against pledge of gold ornaments and jewellery for non-agricultural purposes from 75 per cent to 90 per cent is positive and will certainly ensure greater support to households, entrepreneurs and small businesses.