Fact Sheet: Monetary Policy
August 2022

Volume XXII, Issue 24

FICCI

RBI hikes repo rate by 50 bps to 5.40%

- ❖ Policy repo rate under the liquidity adjustment facility (LAF) increased by 50 bps to 5.40 per cent
- ❖ Standing deposit facility (SDF) rate stands adjusted to 5.15 per cent
- ❖ Marginal Standing Facility (MSF) rate and the Bank Rate stand adjusted to 5.65 per cent

Key Rates	June 2022	August 2022	Status
Repo Rate	4.90%	5.40%	Increased by 50 bps
Standing Deposit Facility	4.65%	5.15%	Increased by 50 bps
Marginal Standing Facility	5.15%	5.65%	Increased by 50 bps
Bank Rate	5.15%	5.65%	Increased by 50 bps

Recently, headline inflation has levelled off and the supply outlook is improving owing to easing of global supply chain constraints. However, the Monetary Policy Committee stated that through the first three quarters of FY23, inflation is expected to continue above its upper tolerance limit of 6 percent. The MPC noted that further calibrated monetary policy action is required to contain inflationary pressures, bring headline inflation back within the tolerance band of 4 +/- 2 percent, and keep inflation expectations anchored in order to ensure that growth is sustained in light of elevated global inflation.

RBI's Outlook on Growth & Inflation

Upsides

- ✓ Bright agricultural prospects likely to bolster rural demand
- ✓ Normal monsoon and rising Kharif sowing
- ✓ Possible respite from imported inflation- global fuel, food, and metal prices moderating
- ✓ Input cost pressures expected to soften
- ✓ A boost to discretionary spending owing to improving consumer and business sentiment
- ✓ Government's capex push, bank credit growth, capacity utilization to improve investment activity
- ✓ Expected expansion in firm's production volumes and new orders

Downsides

- ✓ Global inflation
- ✓ Volatile supply concerns
- ✓ Deglobalization of trade
- ✓ Weaking global demand and growth outlook
- ✓ Rising risks of recessions
- ✓ Pandemic & the war in Europe leading to greater fragmentation
- ✓ Tightening of external financial conditions and capital outflows
- ✓ Currency depreciations and reserve losses
- ✓ Shortfall in paddy sowing
- ✓ Cost pressures transmitted to output prices

RBI's Guidance on Growth & Inflation

	Gross Domestic Product (in %)					Consumer Price Index (in %)				
	FY23	Q1 FY23	Q2 FY23	Q3 FY23	Q4 FY23	FY23	Q2 FY23	Q3 FY23	Q4 FY23	Q1 FY24
August 2022 Monetary Policy	7.2	16.2	6.2	4.1	4.0	6.7	7.1	6.4	5.8	5.0
June 2022 Monetary Policy	7.2	16.2	6.2	4.1	4.0	6.7	7.4	6.2	5.8	-
Change in outlook	Unchanged					Unchanged for FY23, lowered for Q2, raised for Q3 FY23				

Source: RBI's Monetary Policy Statement, August 5, 2022

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RBI retains GDP growth projection of 7.2% for FY 2022-23 from the last monetary policy announcement

Domestic economic activity is picking up with a normal monsoon and above normal reservoir levels, improving area under kharif sowing, growing urban demand for consumer durables, air travel, and sale of passenger vehicles, and robust performance of high frequency indicators. However, rural demand somewhat showed a mixed trend. The import of capital goods also experienced significant growth in June, indicating that investment activity is increasing. Manufacturing and services PMI are also witnessing steady growth. The manufacturing sector's capacity utilization is currently higher than the long-term average, indicating the need for fresh investments. The expansion of bank credit indicates that industrial sector's demand, sales, and profitability remain strong. Owing to these factors, the MPC decided to retain its earlier growth projections.

RBI keeps CPI forecast for FY 2022-23 unchanged at 6.7% from the last monetary policy announcement

Going forward, the trajectory of inflation is expected to continue to be greatly influenced by changes in geopolitical developments including volatility in global commodity and financial markets, and the timing and spatial distribution of the south-west monsoon. The MPC noted that global commodity prices, notably those of industrial metals, edible oil and food, have moderated somewhat. However, the possibility of unseasonal and excessive rainfall and increased input cost pressures in the manufacturing and service sectors remains. Additionally, higher cost of living conditions may result in higher wages and further output price hikes. In light of this, inflation is kept unchanged at 6.7 percent in FY23, with Q2 forecast lowered to 7.1 percent, and Q3 forecast raised to 6.4 percent.

Source: RBI Governor's Statement, August 5, 2022

Developmental & Regulatory Announcements

Regulation and Supervision

Master Direction on Managing Risks and Code of Conduct in Outsourcing of Financial Services

Regulated Entities (REs) are increasingly using outsourcing as a means for reducing costs as well as for availing expertise not available internally. Although outsourcing of a permissible activity is an operational decision of REs, it exposes REs to various risks. The Reserve Bank of India has, from time to time, issued several guidelines/ directions on managing risks in outsourcing of financial services to Scheduled Commercial Banks (excluding Regional Rural Banks (RRBs)), Non-Banking Finance Companies (NBFCs), Housing Finance Companies (HFCs) and co-operative banks. With a view to update and harmonize the extant guidelines, adopt and incorporate global best practices as also enable REs to have all current instructions on outsourcing of financial services at one place for reference, the Reserve Bank will issue draft Reserve Bank of India (Managing Risks and Code of Conduct in Outsourcing of Financial Services) Directions, 2022, for public comments. The scope of these Directions is being expanded to also include RRBs, Local Area Banks (LABs), All India Financial Institutions, Credit Information Companies, and non-scheduled Payments Banks.

Inclusion of Credit Information Companies (CICs) under the Reserve Bank - Integrated Ombudsman Scheme (RB-IOS) 2021 and Extending the Internal Ombudsman (IO) Mechanism

The Reserve Bank-Integrated Ombudsman Scheme (RB-IOS) 2021, covers Regulated Entities (REs) such as scheduled commercial banks including urban cooperative banks, non-banking financial companies (NBFCs) and non-scheduled primary co-operative banks with a deposit size of ₹50 crore and above. In order to make the RB-IOS more broad based, it has been decided to bring Credit Information Companies (CICs) also under the ambit of RB-IOS 2021. This will provide a cost free alternate redress mechanism to customers of REs for grievances against CICs. Further, with a view to strengthen the internal grievance redress of the CICs and to make it more efficient, it has also been decided to bring the CICs under the Internal Ombudsman (IO) framework.

Payment and Settlement Systems

Enabling Bharat Bill Payment System (BBPS) to Process Cross-Border Inbound Bill Payments

Bharat Bill Payment System (BBPS), owned and operated by NPCI Bharat BillPay Ltd. (NBBL), has transformed the bill payment experience in the country. BBPS offers an interoperable platform for standardized bill payment experience, centralized customer grievance redress mechanism, uniform customer convenience fee, etc. BBPS is currently accessible only for residents in India. To facilitate Non-Resident Indians (NRIs) undertake utility, education and other bill payments on behalf of their families in India, it is proposed to enable BBPS to accept cross-border inward payments. This will also benefit payment of bills of any biller onboarded on the BBPS platform in an interoperable manner. Necessary instructions to be issued shortly.

Source: RBI's Statement on Developmental and Regulatory Policies, August 5, 2022

Financial Markets

Standalone Primary Dealers (SPDs) – expansion in scope of permitted activities

At present, Standalone Primary Dealers (SPDs) are permitted to undertake foreign currency business for limited purposes. With a view to strengthen the role of SPDs as market makers, on a par with banks operating primary dealer business, it is proposed to enable SPDs to offer all foreign exchange market-making facilities as currently permitted to Category-I Authorized Dealers, subject to prudential guidelines. This measure would give forex customers a broader spectrum of market-makers in managing their currency risk, thereby adding breadth to the forex market in India. Wider market presence would improve the ability of SPDs to provide support to the primary issuance and secondary market activities in government securities, which would continue to be the major focus of primary dealer activities. Regulations in this regard to be issued separately.

Permitting Standalone Primary Dealers to Deal in offshore Foreign Currency Settled Overnight Indexed Swap Market

Banks in India were permitted, in February 2022, to undertake transactions in the offshore Foreign Currency Settled Overnight Indexed Swap (FCS-OIS) market with non-residents and other market makers with a view to removing the segmentation between onshore and offshore OIS markets and improving the efficiency of price discovery. Standalone Primary Dealers (SPDs) are also market-makers, like banks, in the onshore OIS market. It has now been decided that SPDs authorized under section 10(1) of FEMA,1999 will also be permitted to undertake FCS-OIS transactions directly with non-residents and other market-makers. Necessary directions to be issued shortly.

Committee on MIBOR Benchmark

The Mumbai Interbank Outright Rate (MIBOR) based overnight indexed swap (OIS) contracts are the most widely used interest rate derivatives (IRDs) in the onshore market. The usage of MIBOR based derivative contracts has increased with steps taken by the Reserve Bank to diversify the participant base and facilitate the introduction of new IRD instruments. At the same time, the MIBOR benchmark rate, calculated based on call money deals executed on the NDS-call platform in the first hour after market opening, is based on a narrow window of transactions. Internationally, there has been a shift to alternate benchmark rates with wider participant bases (beyond banks) and higher liquidity. Amidst these developments, it has been proposed to set up a committee to undertake an in-depth examination of the issues, including the need for transition to an alternate benchmark, and suggest the most appropriate way forward.

Source: RBI's Statement on Developmental and Regulatory Policies, August 5, 2022

FICCI's Comments

Reserve Bank of India has maintained consistency in the policy statement made today by focusing on withdrawal of accommodation to contain inflation. The Central Bank has delivered the third consecutive increase in the policy rate today – increasing the benchmark repo rate by a total of 140 bps since May this year. Inflation has been over the comfort range of the Central Bank, however the recent moderation in global commodity prices should hopefully offer some respite going ahead. The uncertainty on external front remains on fore. Nonetheless, the Central Bank has retained the growth forecast for 2022-23 at 7.2 percent – which is encouraging. The capacity utilization rate for Q4 2021-22 at 75.3 is over the long-term average and should lead to improvement in investment activities going forward. The medium-term growth drivers for India are very much intact and recovery is expected to find a firmer ground by the latter part of this fiscal year. We further hope as inflation ebbs, RBI will dynamically manage its monetary policy stance and continue to support growth impulses in the economy.