

SPECIAL UPDATE

Monetary Policy

October 09, 2024

Monetary Measures

- Monetary Policy Committee (MPC) decided with a majority of 5 out of 6 members to keep the policy repo rate unchanged at 6.50%.
- Consequently, the Standing Deposit Facility (SDF) remains unchanged at 6.25%. The Marginal Standing Facility (MSF) rate and the Bank Rate remains at 6.75%.
- The MPC also unanimously decided to change the monetary policy stance to 'neutral' and to remain unambiguously focused on a durable alignment of inflation with the target, while supporting growth.

Analysis & Outlook

- **Inflation:** The September 2024, inflation print may see a significant pick-up as base effects turn adverse and food prices register an upturn. Food inflation, however, is expected to ease by Q4:2024-25 on better kharif arrivals and rising prospects of a good rabi season. Sowing of key kharif crops are higher than last year and the long-period average. Sufficient buffer stocks for cereals are available for ensuring food security. Adequate reservoir levels, the likelihood of a good winter and favorable soil moisture conditions augur well for the ensuing rabi season, though adverse weather events remain a risk. Firms polled in the Reserve Bank enterprise surveys expect input cost pressures to ease; however, the very recent upturn in key commodity prices, especially metals and crude oil needs to be closely monitored. Taking all these factors into consideration, CPI inflation for 2024-25 is projected at 4.5 per cent with Q2 at 4.1 per cent; Q3 at 4.8 per cent; and Q4 at 4.2 per cent. CPI inflation for Q1:2025-26 is projected at 4.3 per cent. The risks are evenly balanced.
- **Growth:** The global economy has remained resilient and is expected to maintain stable momentum over the rest of the year, amidst downside risks from intensifying geopolitical conflicts. In India, real gross domestic product (GDP) registered a growth of 6.7 per cent in Q1:2024-25, driven by private consumption and investment. Looking ahead, the agriculture sector is expected to perform well on the back of above normal rainfall and robust reservoir levels, while manufacturing and services activities remain steady. On the demand side, healthy kharif sowing, coupled with sustained momentum in consumer spending in the festival season, augur well for private consumption. Consumer and business confidence have improved. The investment outlook is supported by resilient non-food bank credit growth, elevated capacity utilisation, healthy balance sheets of banks and corporates, and the government's continued thrust on infrastructure spending. External demand is expected to get support from improving global trade volumes. Taking all these factors into consideration, real GDP growth for 2024-25 is projected at 7.2 per cent with Q2 at 7.0 per cent; Q3 at 7.4 per cent; and Q4 at 7.4 per cent. Real GDP growth for Q1:2025-26 is projected at 7.3 per cent. The risks are evenly balanced.
- **Liquidity:** System liquidity remained in surplus during August-September and early October, with a pickup in government spending and decline in currency in circulation. Liquidity conditions, however, had turned into deficit for a brief period during the latter half of September with the build-up of government cash balances on account of tax related outflows. In sync with the shifting liquidity conditions, the Reserve Bank proactively conducted two-way operations to ensure alignment of inter-bank overnight rate with the policy repo rate. Moving forward, the Reserve Bank will continue to be nimble and flexible in its liquidity management operations. During the current financial year (up to October 8), the exchange rate of the Indian rupee (INR) remained largely range-bound. The INR also continued to be the least volatile among peer EME currencies.

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- The benchmark 10-year paper yield fell by around 5bps from yesterday's close at the time of writing.

Position of Funds

Duration funds:

- The absolute yield levels are attractive from a medium to long-term investment horizon. Therefore, it represents a good opportunity for investors to invest in fixed income duration funds with a medium to long-term horizon.
- However geopolitical risks, extreme weather conditions, volatile food prices remain key risks. Markets may remain volatile in the near term.

Money market funds: The yields at the shorter end of the curve will move in tandem with the liquidity in the system. The short-end rates are expected to be anchored around the repo rate.

MUTUAL FUND INVESTMENTS ARE SUBJECT TO MARKET RISKS, READ ALL SCHEME RELATED DOCUMENTS CAREFULLY.

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