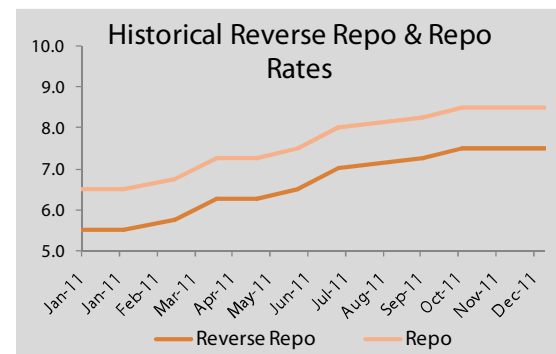
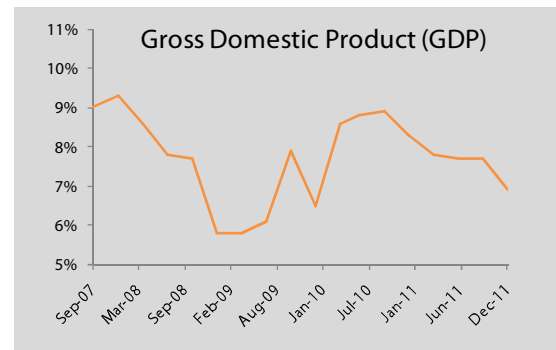
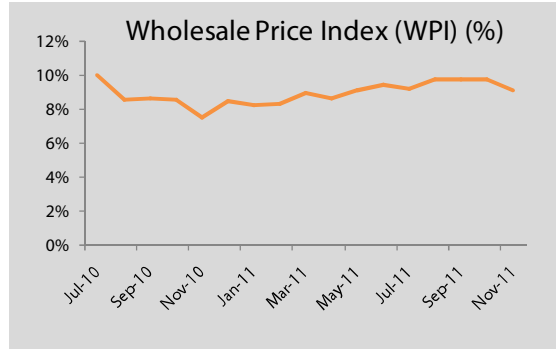


RBI POLICY MEET – Policy rates remain unchanged; change in policy stance

- The Reserve Bank of India (RBI) announced its mid quarterly monetary policy review and discontinued its 13 times rate hike cycle, which it embarked in March 2010. Thus, **the policy rate remained unchanged from its previous policy review at 8.50%, while reverse repo and marginal standing facility rate, were also left unchanged at 7.50% and 9.50% respectively.** The pause in the rate hike cycle came as respite to the market participant as high inflation and gloomy global scenario has already weighed the growth potential of the economy.
- The markets however remained disappointed as the passive policy stance **left CRR and SLR ratios unchanged at 6% and 24% respectively against an expected rate cut.**
- Although the headline inflation in terms of WPI currently remains much above the RBI's comfort zone, it has shown some moderation in the last few months. **WPI for the month of November 2011, declined to 9.11% as compared to 9.73% during October 2011. Going forward, the central bank is quite confident that headline inflation will start coming down to around 7% by March 2012. Food inflation also fell to nearly four year low at 4.35%.**
- Although the apex bank did not explicitly announce the change in its stance, its current actions do confirm that the policy will not only address inflation, but also it will look after economy growth which has taken a hit recently. Worse than the expected IIP (declined by 5.1%) data released last week, and GDP growth which slipped to 6.9%, the slowest in last nine quarters has compelled RBI to hold back its rate hike cycle. **RBI has however stated that, we may see reversal in the upcoming policy stance; thereby reducing key rates.**
- Rupee remained the worst performing currency in the Asian region during the last year as it depreciated around 20% against the greenback. Domestic currency went down to over Rs 54 against USD. **Sharp depreciation of the rupee remains a major threat as the current account deficit is likely to widen further.** Moreover, poor global economic scenario may reduce foreign inflows in capital account which may expose the economy towards Balance of Payment problem.
- The Y-o-Y money supply (M_3) growth moderated from 17.2 per cent at the beginning of the financial year to 16.3 per cent on December 2, 2011, although it is still higher than the projected trajectory of 15.5 per cent for the year. **However, annual non-food credit growth at 17.5 per cent on December 02, 2011 was below the indicative projection of 18 per cent.**
- Consistent with the stance of monetary policy, liquidity conditions have remained in deficit during this fiscal year. However, the deficit increased significantly beginning the second week of November 2011. **The average borrowings under the daily LAF increased to around Rs890bn during November-December (up to December 15, 2011) from around Rs490bn during April-October 2011.** Further, lack of clarity in terms of bond buy back schedule is likely to keep overnight borrowing rates on the elevated levels.
- While inflation remains on its projected trajectory, downside risks to growth have clearly increased. Thus, RBI stated that further rate hikes may not be warranted. However, movement in headline inflation, rupee movement and manufacturing sector growth are likely to remain major determinants of the upcoming policy reviews.**



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