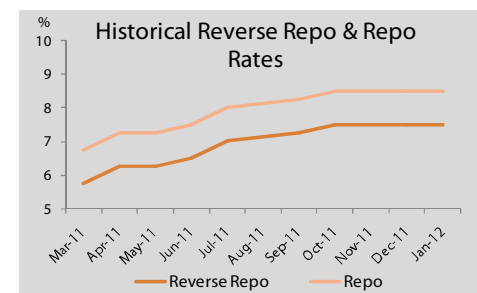
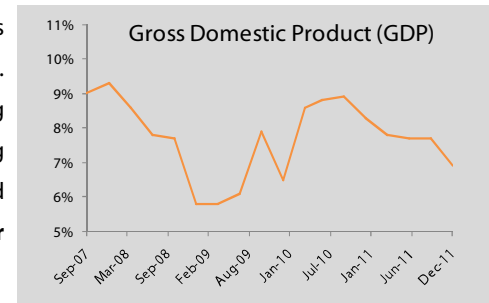
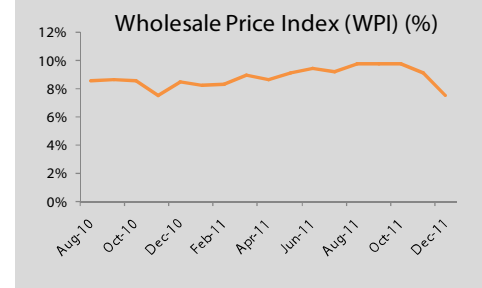


## RBI POLICY MEET – No change in policy rates; Liquidity crunch addressed

- The Reserve Bank of India (RBI) announced its monetary policy review and **kept the policy “Repo rate” unchanged at 8.50%**. With this, the reverse repo rate, which is established with a corridor of 100bps below the **repo rate remained unchanged at 7.50%**; while the rate to seek additional liquidity under **marginal standing facility (MSF) stood at 9.50%**.
- The policy however came as a rescue to the highly cash starved system. In an attempt to allay the acute liquidity crunch in the system, the portion of the bank deposits that has to be mandatorily set aside by the bank as cash reserve ratio (CRR), **has been brought down by 50bps to 5.50%**. **Liquidity in the system has consistently remained in the negative territory, as the average daily borrowings by the banks stood at around Rs 1.2tn**. It exceeded RBI’s target, which meant it to stay at around Rs 500bn (around 1% of the net demand and time deposits). **Reduction in CRR is likely to infuse Rs 300bn (0.5% of Rs 60tn NDTL) in the system**. Bond yields are likely to remain stable due to additional liquidity.
- During the previous couple of months, the headline inflation, WPI has moderated. Moderation in WPI was mainly aided by food inflation, which went down to its 2 year low at 0.7% in the month of December 2011. **However, the non food manufacturing inflation, still remains above 7%**. While indicators of pricing power suggest that the moderating trend will continue, upside risks to inflation remain significant. Keeping in view the expected moderation in non-food manufactured products inflation, domestic supply factors and global trends in commodity prices, **the RBI has projected baseline WPI inflation to stay at around 7% for FY12**.
- The growth momentum has moderated during the last couple of quarters as **real GDP growth moderated from 7.7% in the first quarter of 2011-12 to 6.9% in the second quarter**. This was mainly due to deceleration in industrial growth. **Growth was hurt, not only due to domestic slowdown but also by the fragile situation in the euro zone and slow recovery in the USA**.
- **Non-food credit growth has slipped below the indicative trajectory of 18%**. Keeping in view the increased government borrowings and the slowdown, **RBI has maintained 16% guidance for credit growth in FY12**.
- **Domestic currency remained under pressure in the third quarter of 2011-12, reflecting adverse global sentiments and moderation in capital inflows**. In order to curb further Rupee depreciation, RBI sold currency of around USD 300bn during the last month.
- Although the central bank did not explicitly reverse its policy stance by lowering policy rates, it has stated that ensuring growth along with controlling inflation will remain its key agenda in the upcoming policies. Considering the increased risk aversion of the banks as the bad assets continue to pile up in the system, the RBI hinted that we may see revision in the policy stance. However, **further actions are likely to be guided by many factors such as solution to euro zone crisis, growth momentum and inflationary pressures**.



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