STICKY ISSUE

RBI rate cut in Dec? Unlikely, say experts

ANJALI KUMARI & MANOJIT SAHA
Mumbai, 29 November

Despite gross domestic product (GDP) growth being lower-than-expected for the July-September quarter, the six-member Monetary Policy Committee (MPC) may not cut the policy repo rate in the review meeting scheduled for next week due to high inflation in October, according to experts.

"Consumer Price Index (CPI) inflation breaching the upper limit of the RBI's tolerance band in October (6.2 per cent year-on-year) is not a favourable backdrop for the MPC to commence the easing cycle, even as the growth outcome disappointed the MPC's expectations," said Shreya Sodhani, regional economist at Barclays, who expects the policy repo rate to be kept unchanged in the December meeting.

"That said, we do not think the MPC's decision will be unanimous, and we believe it is likely that more than one member may dissent in the meeting," Sodhani said.

Data released by the government on Friday showed GDP growth in the second quarter was 5.4 per cent, much lower than the market expectation of 6.6 per cent. The RBI's projection for real GDP growth in the second quarter was 7 per cent, and 7.2 per cent for FY25. Barclays has now lowered its FY25 GDP growth forecast to 6.5 per cent from 6.8 per cent earlier.

The yield on the benchmark 10-year govt bond fell 6 basis points following the release of the GDP data

"The GDP print was significantly below expectations, led by a slowdown in manufacturing, construction, and mining activity. This reflects a sharp slowdown in listed company profits in Q2 FY25," said Gaura Sen Gupta, chief economist at IDFC FIRST Bank.

"Post today's print, there is a high probability of an RBI rate cut in December," she added.

However, a section of the market now expects a possible reduction in interest rates during the February policy meeting, provided there is some relief on inflation. "In light of the recent spike in CPI inflation, we anticipate a status quo from the MPC next week," said Aditi Nayar, chief economist at ICRA.

"However, with the GDP growth print sharply undershooting the Committee's expectations, a February 2025 rate cut may be on the table if the next two inflation prints recede," she said.

The yield on the benchmark 10-year government bond fell by 6 basis points following the release of the GDP data. The benchmark yield settled at 6.74 per cent on Friday, down from 6.80 per cent on Thursday.

Market participants said traders stocked up on bonds in initial euphoria after the data release; however, yields might inch up in the coming trades as the market gains clarity around the rate cut trajectory set by the domestic rate-setting panel.

"The market reacted to the data on expectations of a rate cut, but a December cut seems unlikely. Selling will start soon," said Vikas Goel, managing director and chief executive officer of PNB Gilts.