RBI increases repo rate by 35 bps, hints at more hikes

LOWERS ITS GDP GROWTH FORECAST TO 6.8% FROM 7%

GOVERNOR AIRS CONCERN ABOUT CORE INFLATION REMAINING STICKY

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Mumbai, 7 December

The six-member Monetary Policy Committee (MPC) of the Reserve Bank of India (RBI) on Wednesday increased the policy repo rate by 35 basis points (bps) to 6.25 per cent, the highest level since February 2019. With this, the repo rate has been increased by 225 bps since May.

EDIT: More to come 7

The increase was lower than the three previous ones, but the MPC hinted at the possibility of further hikes as it refused to lower its guard against inflation.

RBI Governor Shaktikanta Das cautioned that "the battle against inflation is not over", while acknowledging that it was expected to moderate.

Average inflation has remained above 6 per cent for three consecutive quarters, which constituted a failure on the part of the central bank to meet its inflation mandate.

"...the MPC was of the view that further calibrated monetary policy action is warranted to keep inflation expectations anchored, break core inflation persistence and contain second round effects," Das said, while announcing the review of the policy. He added: "The main risk is that core inflation remains sticky and elevated."

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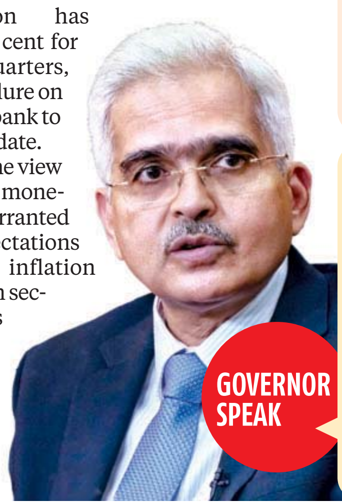
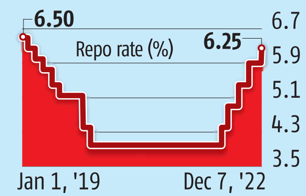
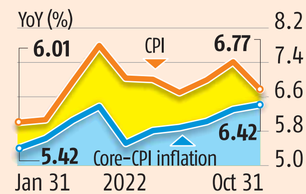


POLICY TRAJECTORY



CORE CONCERNS



Sources: Bloomberg, MoSPI, RBI

GOVERNOR SPEAK

GDP growth resilient, Indian economy holding on

Worst of inflation behind us, but no room for complacency

RBI to **inject liquidity** if needed

Story of **₹ is one of resilience and stability**

CAD eminently manageable

UPI to now allow blocking money for multiple debits

The RBI on Wednesday enhanced the capabilities of the Unified Payments Interface (UPI) by introducing a 'single-block-and-multiple debits' functionality. 4

Consumer-facing companies see no immediate impact

The repo rate hike is unlikely to have an immediate impact on consumer-facing sectors such as automobiles and consumer durables, top executives said. 5

Prepay home loan to combat impact of interest rate hike

Home loan rates (for loan amount of ₹30-75 lakh) are in the range of 8.25-10.5 per cent. If your pocket allows, opt for higher EMI, not a longer tenure. 10

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RBI...

The MPC's external member Jayanth Varma voted against the increase, while both Ashima Goyal and Varma voted against the stance, which was to remain focused on withdrawal of accommodation.

"The governor explicitly noted that the resurgence in domestic services sector activity could also lead to price increases, especially as firms pass on input costs. Thus, the nature of inflation risks has in some sense moved from external factors to internal ones. This to us is the most hawkish aspect of today's policy announcement," said Suyash Choudhary, head – fixed income, IDFC AMC.

Though the hike was in line with expectations, the central bank's comments were interpreted as hawkish as the market expected the MPC to indicate a pause after this hike. The yield of the 10-year benchmark government bond, which touched 7.3 per cent after Das' comments, ended the day at 7.27 per cent, 2 bps higher than the previous close. The yields of the shorter-term papers hardened more sharply.

The market is now pencilling in another 25 bps rate hike in February. "The RBI has down-shifted gears to 35 bps hike from 50 bps in the previous meetings, but yet to hit the brakes to bring the hiking cycle to a complete halt...We have a final hike in February of 25 bps, which remains a close call, and then a hold," said Aurodeep Nandi, India economist and vice president of Nomura, while adding that the firm expects a cumulative 75 bps cuts in the second half of 2023, taking repo rates back to 5.75% by end-2023.

The RBI retained its projection for the consumer price index (CPI)-based inflation for FY23 at 6.7 per cent though the projections for Q3 and Q4 were increased slightly to 6.6 per cent and 5.9 per cent, respectively. CPI inflation for Q1FY24 was projected at 5 per cent and for Q2 at 5.4 per cent.

Das sounded more sanguine on gross domestic product (GDP) growth, though the projection for FY23 was lowered slightly to 6.8 per cent from 7 per cent. Real GDP growth is projected at 7.1 per cent in Q1FY24 and 5.9 per cent in Q2. As nearly 50 per cent of fresh loans are linked to external benchmarks, mostly the repo rate, home loans and car loans are set to get dearer.

Soon after the RBI's decision, state-run lender Bank of India increased the repo-based lending rate by 35 bps to 9.1 per cent. Others are expected to follow suit.

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Very hard: ★★★★★

Solution tomorrow

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