Economists see 25-bp rate cut in Feb

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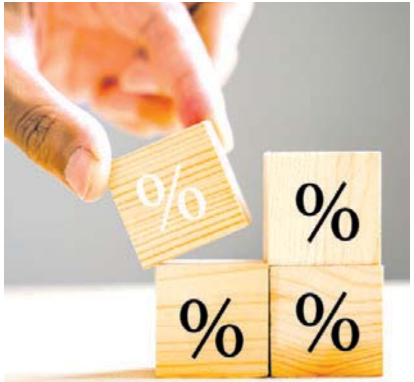
With the latest headline-inflation rate coming in at 5.48 per cent and expectations of it remaining below 6 per cent in the coming months, economists and the markets are betting on a cut in the policy repo rate of 25 basis points (bps) by the Reserve Bank of India's (RBI's) rate-setting body — Monetary Policy Committee (MPC) — in the February meeting.

The headline-inflation rate went below 6 per cent in November, falling within the RBI's tolerance band of 2-6 per cent, thanks to a moderation in food prices and a favourable base effect, among other factors.

The core-inflation rate too eased slightly to 3.7 per cent in November, down from 3.8 per cent in the previous month.

In comparison, the headline-inflation rate stood at 6.2 per cent in October and 5.49 per cent in September.

"We expect the RBI to cut rates in February 2025, with a cumulative 75 bps cut over the rate-cut cycle and such a decision is unlikely to be impacted by what could happen to the dollar, as was the case in 2018, when the RBI did not hike rates even as the rupee was under enormous pressure," said an SBI Research report, authored by Soumya Kanti Ghosh, group chief economic adviser, State Bank of India (SBI).



EXPERTS SPEAK

- Eased inflation in Nov to cushion rate cut
- Headline inflation may normalise to 4-5% with the passage of weather-related impact on food basket
- The RBI may cut cumulatively 75 bps with an eye on the US dollar
- Rate cut seems warranted after weak GDP growth in Q2

Stating similar views, Radhika Rao, executive director and senior economist, DBS Bank, said: "We maintain our call for a 25 basis point cut at the February meeting, with a cumulative 75 basis point cut in this cycle, keeping an eye on the dollar and dollar liquidity."

Rao expects the headline-inflation rate to normalise to 4-5 per cent. This would strengthen the case for a rate cut, especially when India's gross domestic product (GDP) growth rate fell to a seven-quarter low of 5.4 per cent in the July-September quarter.

According to Nomura, the daily data suggests that the December retail-inflation rate is also tracking 5.5 per cent so far, while the core-inflation rate should inch lower to 3.6 per cent.

Food inflation should moderate, and the drivers of both goods and services inflation suggest sustained core disinflation.

Even the MPC, in the recently concluded meeting on December 6, suggested that although the inflation rate surged above the upper tolerance band of 6 per cent in October, driven by a sharp uptick in food inflation, food-inflation pressures were likely to linger in the third quarter (Q3) this financial year and start easing from Q4, backed by a seasonal correction in vegetables prices, kharif harvest arrivals, likely good rabi output, and adequate buffer stocks of cereals.

In that scenario, Nomura economists have suggested they expect a 25 basis point rate cut in February, marking a belated policy pivot, and a 100 basis point cut in this easing cycle.

Meanwhile, the February MPC meeting will usher in a change of leadership, with the new RBI governor, Sanjay Malhotra, chairing his first meeting. Additionally, with Michael Patra's term ending in January, a new deputy governor will also join the MPC.

"The composition of the MPC will change now with the new governor coming and with Patra retiring next month. Since there will be a change of the guard, the markets have very little idea about the inclination," said Madan Sabnavis, chief economist, Bank of Baroda.

Sabnavis said although the time was not ideal for a cut because the inflation rate had not durably come down and remained above 5 per cent, with the expectation that prices would reduce in the coming months, it was most likely that the MPC would cut rates in February.

According to Gaura Sen Gupta, chief economist, IDFC First Bank, the core inflation rate has remained relatively benign and the headline inflation rate is being driven by high vegetable prices. However, this is a supply-side issue that cannot be addressed through monetary policy.

"We expect the MPC to implement a rate cut in February because economic growth slowed significantly in the second quarter. Given the economic slowdown, a rate cut at this juncture seems warranted to support growth," she added.