

**MPC maintains a status quo with “Calibrated Tightening” stance**

RBI’s monetary policy has emerged as a critical policy tool for achieving overall macroeconomic management, price stability and growth. The Monetary Policy Committee (MPC) met from 3rd December to 5th December 2018 to review the monetary policy framework of the country, decide on the repo rate, reverse repo rate, inflation projection and forecast of GDP growth rate.

All eyes were glued on MPC’s decision to maintain the repo rate (the key rate at which the RBI lends short-term funds to commercial banks) with the same “Calibrated tightening” policy stance. In its previous bi-monthly review, MPC surprised the market by keeping the repo rate unchanged to 6.5%. The MPC had already hiked the repo rate twice in this year, due to uncertainty in terms of inflationary risks. Since then, the falling crude oil prices, below than expected consumer inflation has created a notion amongst economists with a view of “status quo” status from the central bank.

**Highlights of December Monetary Policy:**

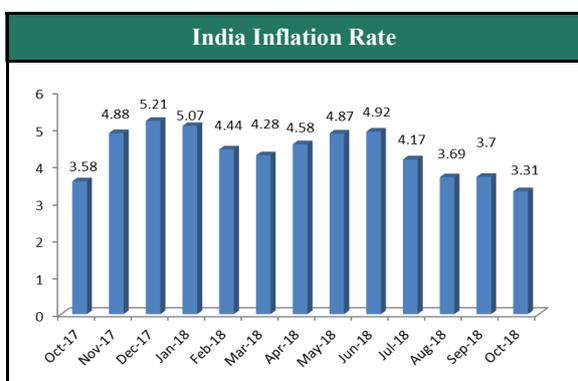
- Repo Rate: 6.5% (was kept unchanged to 6.5% in October 2018)
- Reverse Repo Rate: 6.25% (was kept unchanged to 6.25% and the bank rate at 6.75% in October 2018)
- RBI lowers the inflation projection at 2.7-3.2% in H2 FY19 and 3.8-4.2% in H1FY20
- The RBI has maintained the forecasted GDP growth of 7.4%. Further, the GDP growth has been projected at 7.2-7.3% in H2FY19 and 7.5% in H1FY20.

The RBI has kept the Repo Rate unchanged in the fifth bi-monthly monetary policy meeting, however maintaining a “Calibrated tightening” stance, with the objective of achieving medium-term target for CPI inflation of 4%(+/-2%), while supporting growth. Also, RBI has cut SLR by 0.25% in every quarter, starting from Jan-Mar 2019, reaching to 18% from recent 19.25% ( A rate cut of 25bps in this monetary policy has led the SLR rate to be 19.25% from 19.5%).

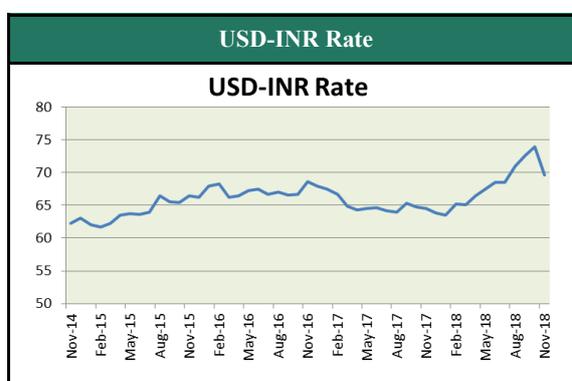
**Why a hike was not expected:**

Many analysts expected the RBI not to hike the repo rate, after two consecutive rate hikes in the last four bi-monthly meetings. The factors in favour are:

- Inflation, a key concern for India’s central bank, has eased to 3.31% below the medium term inflation target of around 4% given by RBI in October.
- The crude oil price has declined 30% from \$84/barrel to \$58/barrel. Also, rupee has shown signs of strengthening against the US dollar (from a low of 74.22 to 70).
- Yields on the 10-year government bonds have declined sharply from 8.05% (on 5th October) to 7.62%.
- No sign of interest rate hike, after three consecutive hikes in interest rate, by US Federal Reserve.



Source: tradingeconomics.com



Source: investing.com

**Our View:**

It was a unanimous status quo in the key policy interest rates expected on December 5. The line of interest was more on the commentary on the interest rates and outlook on the policy stance and liquidity which was keenly watched by the market. We were expecting a pause in the interest rates taking into consideration the current economic environment. The calibrated tightening stance in the previous meeting did rule out the probability of further rate cuts. The shift to Neutral was the key factor of interest. However, factors like sharp decline of crude oil prices, weakening of food prices, assumption of normal monsoon in 2019, with inflation risks tilted to upside, has led RBI to keep the “Calibrated Tightening” status with no interest hike. Our expectation of no rate hike along with majority of the market expectation was in line with the outcome of this MPC meet.

**The Final Verdict:**

POLICY AT A GLANCE			
REPO	REVERSE	SLR	MPC’s
UNCHANGED	UNCHANGED	CUT	Stance: CALIBRATED TIGHTENING
To 6.5%	To 6.25%	To 19.25%	

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Registered Office Address:  
Progressive Share Brokers Pvt. Ltd.  
122-124, Laxmi Plaza, Laxmi Indl Estate,  
New Link Rd, Andheri West,  
Mumbai-400053;  
www.progressiveshares.com  
Contact No.:022-4077500.

Compliance Officer:  
Mr. Shyam Agrawal,  
Email Id: compliance@progressiveshares.com,  
Contact No.:022-4077500.