

The Monetary Policy approach sound Hawkish after revised inflation estimates at 6.7% for FY23.

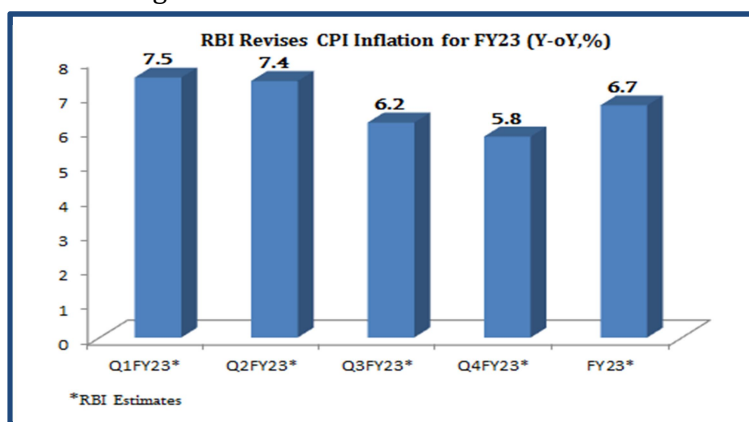
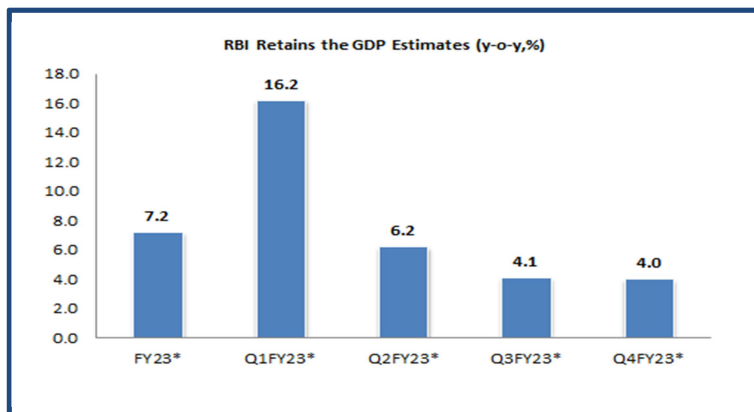
The Monetary Policy Committee (MPC) at its meeting decided to increase the policy repo rate under the Liquidity Adjustment Facility (LAF) by 50 basis points to 4.90% with immediate effect. As a result, the Standing Deposit Facility (SDF) rate stands adjusted at 4.65% and the Marginal Standing Facility (MSF) rate and the Bank Rate to 5.15%. The MPC decided to withdraw from the accommodative stance it had adopted since the beginning of the pandemic in March 2020 as taming inflation remains the top most priority while supporting growth. Against this background, the decisions so arrived was in consonance with the objective of achieving the medium-term target for consumer price index (CPI) inflation of 4% within a band of +/- 2%

Key Highlights

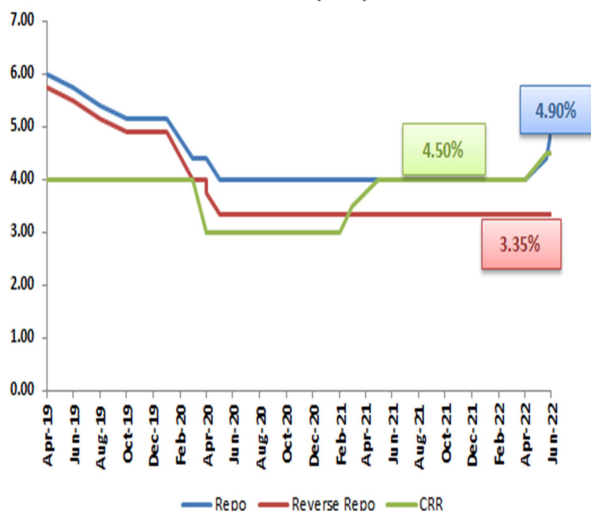
- RBI Projection of the real GDP growth for FY22-23 is estimated at 7.2%, with Q1 at 16.2%, Q2 at 6.2%, Q3 at 4.1% and Q4 at 4%. For the last Financial Year 2021-22, the real GDP is estimated at 8.7% as per the provisional estimates by the National Statistical Office (NSO) released on 31st May, 2022.
- The CPI inflation in April 2022 registered a sharp increase to 7.8% marking four months of constant rise where it remained above the upper tolerance level of 6%. For FY22-23, CPI inflation is projected at 6.7%, with Q1 at 7.5%, Q2 at 7.4%, Q3 at 6.2% and Q4 at 5.8%.
- The spike in inflation was mainly on account of increase in food prices of cereals, milk, fruits, vegetables, spices and prepared meals and on the other hand on account of fuel inflation led by a rise in LPG and kerosene prices. Apart from these two elements, core inflation increased across all components, mainly by transportation and communication sub-group.
- Overall system liquidity still remains in large surplus even though the average daily absorption under the LAF moderated to ₹5.5 lakh crore during May 4 - May 31st from ₹7.4 lakh crore during April 8 - May 3, 2022 in consonance with the policy of gradual withdrawal of accommodation.
- **Money Supply (M3) and bank credit from commercial banks rose 8% YoY and 12.1% YoY respectively. As on 27th May, 2022, India's foreign exchange reserves stood at US\$601.4 Bn.**
- The 10 year bond yield dropped 77 bps to 7.46% as the rate hike was on expected lines and there was no further hike in cash reserve ratio. The government had already planned to sell 14.31 trillion rupees of bond this fiscal.

Rational and Impact of policy discussion

In the wake of dynamic global scenario and current economic assessment, the RBI had to take the decision of gradual withdrawal of the “**Accommodative**” stance and commit to move towards normal monetary conditions in a calibrated manner. The rise in geo-political tensions with the beginning of the Russia-Ukraine war at the end of Feb 2022, led to huge spike in international crude oil prices and various commodities, thus increasing inflation above its comfort levels. While it expressed optimism in the sound financial system of the country to witness any external shock, one had to accept the hard truth that the country cannot stay immune to the changing global dynamics pertaining to growth and inflation. It expressed confidence that apart from the policy decisions taken by it, the recent reduction in excise duties on petrol and diesel along with a further reduction of State VATs on the same across the country can contribute in softening of inflation rate. Adding to it a normal monsoon can further mitigate the inflation risk.

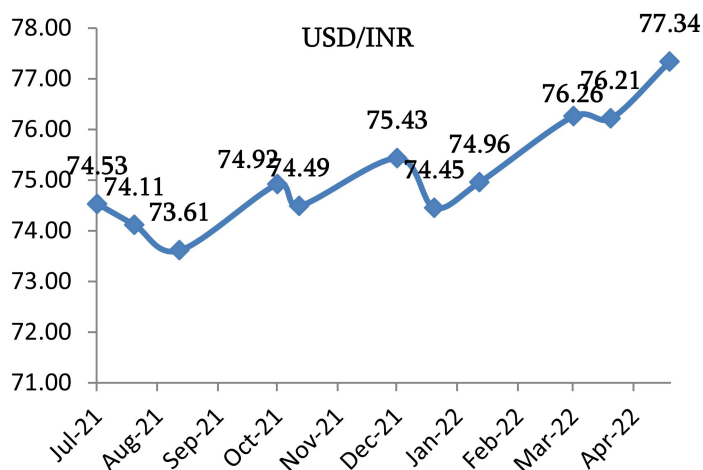


RBI's Monetary Policy Stance

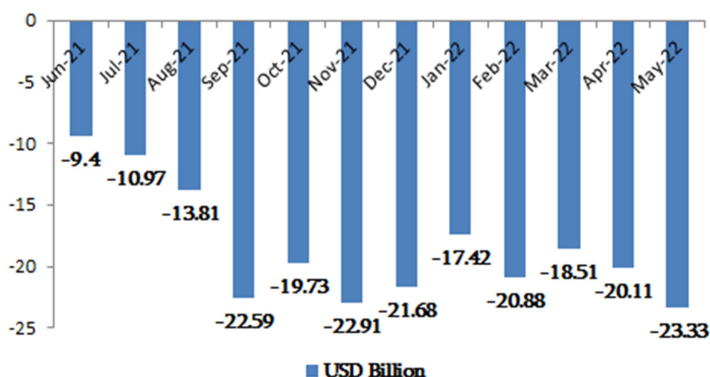


- The annual inflation in April 2022 was highest at 7.8% since May 2014 and above the upper tolerance level of 6% & the food inflation accelerated for the 7th straight month to 8.38%. The surge in headline inflation is seen across all categories.
- India's merchandise exports grew 15.46% YoY to \$37.29 billion in May despite weakening recovery across major trading partners. The impact of rising crude oil prices on petroleum, oil and lubricants import bills has been partly offset by export of petroleum products which benefitted from better price realization.
- The current account deficit is sustainable at current levels which can be financed by normal capital flows. The foreign exchange reserves of US\$601.1 billion acts as a cushion for ~10 month of oil imports going by current run rate of \$60 billion.
- The Indian rupee (INR) depreciated against the US dollar by 4.15% YTD amidst net sell-off in the equity market and concerns over rising crude oil prices.
- Under the ongoing Kharif marketing season (KMS) which runs from Oct-Sep, as on 28th April had procured 760 Lakh MT of paddy, which stands at 85% of total KMS procurement in FY21. The wheat procurement under Rabi Marketing Season which runs from April –March, has also started for FY22-23 and reached 156.9 Lakh MT benefitting approximately 9.5 lakh farmers.
- CAD for the month of April stood at USD (-) 20.11 billion as depicted in the graph below. This has widened to USD (-)23.33 billion in May. Widening of CAD had led to depreciation of nominal exchange rate, However, monthly export figures show that, despite the loss of price competitiveness, India's export continued to surge, driven by high global demand.

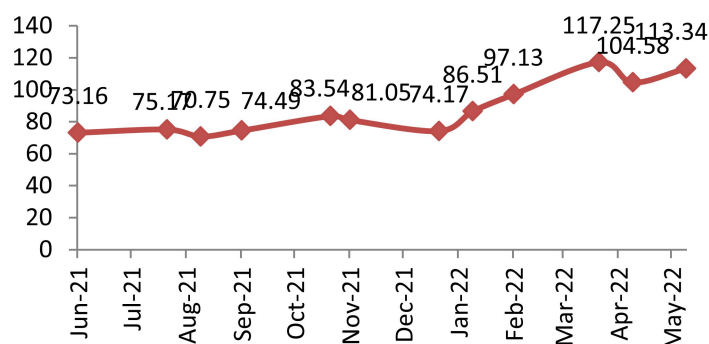
USD/INR



India's Trade Deficit



Brent Crude price in USD per barrel



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