



RBI Monetary Policy

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The **Reserve Bank of India** has announced first bi-monthly **Monetary Policy Statement** for the **financial year 2019-20**.

LAF Adjustment

- The **Monetary Policy Committee (MPC)** of the RBI has **reduced policy repo rate under the Liquidity Adjustment Facility (LAF)** by 25 basis points to **6.0% from 6.25%** with immediate effect.
 - Consequently, the reverse repo rate under the **LAF is adjusted to 5.75%**, and the marginal standing facility (MSF) rate and the Bank Rate to **6.25%**.
 - This is the **second consecutive rate cut (last one in February, 2019)** in the year 2019 and under **new RBI Governor Shaktikanta Das**.
- A rate cut by RBI **injects liquidity in the economy**. It also acts as a sentiment booster and aid companies that have to service large debts. Top sectors which are likely to benefit the most from a rate cut are **banking, NBFC, infrastructure and real estate**.
- The MPC has also decided to maintain the **neutral monetary policy stance**.
 - Neutral stance indicates that the **policy rates neither stimulates (speeds up) nor restrains (slows down) economic growth**.
 - The neutral stance also indicates that the RBI feels that the **correct interest rate levels have been reached**, and now It is upto the banks to lower the rates and ensure better transmission of RBI's objective of lower interest rate in the system fuelling faster growth.

Inflation Targeting

- The decision of MPC is in consonance with the objective of achieving the target for **consumer price index (CPI) inflation of 4% within a band of +/- 2%, while supporting growth.**
 - This inflation range (4% within a band of +/- 2%) was recommended by the committee headed by **Urjit Patel in 2014.** The same committee also **recommended the formation of MPC.**
 - **In May 2016, the Reserve Bank of India (RBI) Act, 1934** was amended to provide a statutory basis for the implementation of the flexible inflation targeting framework.
 - The amended RBI Act also provides for the **inflation target to be set by the Government of India,** in consultation with the Reserve Bank, **once in every five years.**
 - Accordingly, the Central Government has notified in the Official Gazette 4% Consumer Price Index (CPI) inflation as the target for the period from August 5, 2016 to March 31, 2021 with the upper tolerance limit of 6% and the lower tolerance limit of 2%.
 - Before the constitution of the MPC, a **Technical Advisory Committee (TAC)** on monetary policy advised the Reserve Bank on the stance of monetary policy. With the formation of MPC, the **TAC on Monetary Policy ceased to exist.**
- Although inflation is well under control at 2.6% and is projected to average 3.2% to 3.4% in the first half of 2019-20. This is below the 4% target set for the MPC. However, there are some concerns:
 - Early forecasts indicate a strong possibility of a **below-normal monsoon due to El Niño.** This would cast a shadow on agricultural output, and consequently the food prices.
 - Similarly, global oil prices are now edging close to the \$70 a barrel mark on the back of **production cuts by the OPEC cartel.**

GDP Growth

The MPC has lowered the **GDP growth for 2019-20 to 7.2% from 7.4%** which was projected in February policy meet. Reasons being:

- The signs of weakening in the **domestic investment activity** which is reflected in a slowdown in production and imports of capital goods.
- A moderation of growth in the **global economy might impact India's exports.**
- Recently, the **Central Statistics Office** has also revised the GDP growth for **2018-19 downwards to 7%.**

Linking Loans

The Reserve Bank of India (RBI) also decided to **hold further consultation** on the proposal to link retail loans with an **external benchmark (like: RBI's policy repo rate, 91-day treasury bill yield, 182-day treasury bill yield or any other benchmark market interest rate) for improving monetary transmission.**

- During the December review of monetary policy, the RBI had proposed to implement the system of linking floating rate personal or retail loans, and floating rate loans to Micro and Small Enterprises, to an external benchmark from April 1, 2019.
- At present, all loans are linked to the **Marginal Cost of Fund based Lending Rate (MCLR)**. For the smooth transmission of policy rates and to make this process transparent, RBI has, over the years, directed banks to price their loans against their benchmark prime lending rate, base rate, and, finally, MCLR.