# Growing feeling that a change is in the offing

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**THE CREDIT POLICY** did not throw up any surprises as such which can be gauged by almost an unchanged market reaction. It was business as usual. There are, however, some very interesting aspects of the narrative.

The first is that 2 of the 6 members had thought otherwise and voted for both a rate cut and a change in stance. This is different from the past when there was just one contrarian view. It can be concluded that there is a growing feeling that a change could be in the offing in future. The minutes of the monetary policy committee meeting would throw light on how economic data and prospects were interpreted differently by the two contrarian members.

Second, the RBI's take on inflation is significant. It has reiterated the number of 4.5%. However, the RBI has highlighted the impact of the recent heatwave on the output and prices of horticulture products which will remain a concern going forward.Also while acknowledging the IMD forecast of a normal monsoon, there is a direct hint that the progress of the rains will be important to be certain of the inflation trajectory. Further, while the forecast for Q2 is low at 3.8%, the RBI has stated that this is mainly due to the base effect.The forecasts for the following quarters are in the region of 4.5-4.6%.

Third, related to inflation the RBI has voiced concern over the possibility of higher food inflation having spillover effects on core inflation and hence inflationary expectations. This also fits in with the unchanged stance taken on the withdrawal of inflation as it hinges on both the transmission of rates as well as managing inflationary expectations.The footnotes do suggest that the transmission of the 250 bps in repo rate has increased by only 204 bps in average lending rate while that on deposits was up by 245 bps.

Fourth, the RBI has reiterated that the Fed's action should not be taken as a factor that is considered by the MPC for deciding as it is driven by local conditions.This should clear the air for the markets. Often any statement made by a Fed member which indicates a possible Fed cut in September is interpreted as being the cutoff mark for the RBI too. Theoretically, any Fed action will influence the flow of investment and currencies and would have a weak impact on domestic inflation (which is through the rupee depreciation route).

Fifth, the GDP growth rate for FY25 has been upped to 7.2% with the four quarters having around the same number. Alongside it has been pointed out that the average capacity utilisation rate has increased to 76.5% in Q4 -FY24. This is significant because contrary to the view that the high repo rate has militated against growth, it is clear the RBI believes that growth will continue on the high trajectory path.

Sixth, the RBI has also hence indirectly addressed the issue of growth being affected by high interest rates,which is a view in the market. There can be a reference made to the past when the policy had followed the tenet of doing everything to protect growth. But, that was during the Covid phase where the focus was on keeping interest rates low to support the economy. Clearly, this is not the situation todaywhere growth is robust. The average repo rate in the last ten years was in the region of 6-6.5% and hence is not above the path to come in the way of growth.

Last, the RBI has reaffirmed the use of VRR and VRRR auctions to manage liquidity which will assuage markets. This has worked well through different phases of surpluses and deficits and the markets should keep looking at the weighted average call rate which is what has been targeted and maintained in the corridor of 6.25-6.75% with the tendency to settle somewhere in the middle.

Hence while no action has been taken, the commentary has been cogent and indicative of how the central bank sees the state of the economy - both present and future. The overarching factor is inflation which has to not just come down towards 4% but should on a durable basis to trigger any change in stance.

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