TATA CAPITAL WEALTH

06 August 2020

RBI Policy Measures

RBI's Stance	→	Accommodative

Key Announcements:

- The RBI's **MPC has unanimously decided** to keep the repo rate **unchanged at 4.00% and to continue with the "Accommodative" stance.**
- All the other Policy Rates and the Reserve ratios were kept unchanged.
- Allow a special window for eligible **MSMEs, corporate and personal loans to be restructured.**
- A relaxation on **loan-to-value (LTV) ratio for gold loans from 75% to 90%.**

Policy Rates / Reserve Ratio	Current
Repo Rate	4.00%
Reverse Repo Rate	3.35%
MSF	4.25%
Bank rate	4.25%
CRR	3.00%
SLR	18.00%

Growth & Inflation Outlook by RBI:

- The MPC expects **headline inflation to remain elevated in Q2:2020-21, but likely to ease in H2:2020-21**, aided by favourable base effects. Being cognizant of its inflation target and due to uncertain CPI outlook, the MPC decided to stay put on the policy rates.

- Economic activity in India has started to recover and Kharif sowing suggests recovery in rural economy may be robust. **For 2021, real GDP growth is expected to be negative.**

- India's **foreign exchange reserves** have increased by US$ 56.8 billion in 2020-21 so far (April-July) to **US$ 534.6 billion (as on July 31, 2020)** – equivalent to 13.4 months of imports.

Additional Measures

RBI Announced a host of additional measures to combat the impact of coronavirus:

1. **Rs. 5,000 cr will be provided at the Repo rate to each NABARD** (Rs. 25,000 cr given earlier) **& NHB** (Rs. 10,000 cr given earlier) to support NBFCs, MFIs & HFCs.

2. Under the backdrop of the stress tests conducted by the RBI show that under the baseline scenario, where growth is assumed at -4.4%, the gross NPA ratio may rise to 12.5% and in a severe stress scenario of 8.9% contraction in the economy, the gross NPA ratio may rise to 14.7%, the RBI announced a **one-time restructuring of corporate loans.**

3. A restructuring framework for MSMEs that were in default but 'standard' as on January 1, 2020 is already in place. **Stressed MSME borrowers will be made eligible for restructuring their debt** under the existing framework, provided their accounts with the concerned lender were classified as standard as on March 1, 2020.

4. **Banks can now lend up to 90% of the gold ornaments & jewellery value, up from the existing limit of 75%.** The RBI increased the LTV (loan-to-value) ratio on gold loans to provide relief to borrowers looking to take gold loans to mitigate the financial exigencies caused by the pandemic.

5. As a measure to boost to corporate bond market, banks investment in **debt MFs and debt ETFs will be treated consistently with direct debt investments** in terms of capital allocation

6. To address regional disparities, **priority sector guidelines will be reviewed** and incentive-based framework will be put in place.

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Outlook

- There were mainly **two reasons why the MPC decided to keep the rates unchanged** - first **inflation** being above the upper tolerance limit of the RBI since the past 3 months upto June and second the committee has **already slashed the rates by 115 bps** since the outbreak of the COVID crisis and the **transmission by banks to the customers is still to kick in fully**. The Governor stated that though **there is space for further monetary action but it is advisable to be judicious** and the MPC will remain watchful w.r.t. inflation dynamics, to further use space available on monetary side when appropriate.

- With respect to restructuring of loans the rating agencies are of the view that while it could postpone the recognition of stress in the lender book in the near-term, high share of such assets would be a credit negative.

- On the announcement of restructuring of loans which was an industry demand the equity market rejoiced while the bond markets remained flat.

- Today's policy has made it clear that it the **RBI that has a material role to play** in the current scenario where there is excess liquidity in the market and RBI is using the **reverse repo** window to manage liquidity in the system making the repo rate is irrelevant for the time being.

- Over the period of the COVID crisis the **spreads between the corporate bonds and the respective tenure gilt has reduced considerably** on the shorter end leaving very little room for the yields to fall. Besides the interest rate are likely to remain range bound in the near future. <u>**Thus, we continue to reiterate our approach to remain on the shorter end of the curve with funds having high quality of papers.**</u>

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