

JUNE MPC MINUTES

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MPC to emphasise on inflation in next meeting

MPC members believe impact of second wave is lower than the first wave during the national lockdown. With sharp reduction in infections, activity is normalising. Growth will be led by government's capex, exports and a normal monsoon. However, a few members spoke of being data dependent on inflation risks getting generalised. With inflation above 6% in May'21, MPC is likely to discuss inflation trajectory in even greater detail in next meeting. We expect policy normalisation in Q4FY22 and repo rate hike in early FY23.

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Impact of second wave to be limited: MPC members stated that while the second wave did derail economic recovery, its impact is far less than last year. Dr. Goyal pointed out that "since the impact on demand is more than supply, output gap has widened". At the same time, Prof. Varma cautioned against the rise in precautionary savings which might keep demand subdued. Dr. Sagar pointed out that the policies laid out in the Budget focus on investment. RBI Governor, Shri Shaktikanta Das said that 30.5% increase in capital expenditure by Centre should reignite the investment cycle. MPC members agreed that exports and a normal monsoon bode well for the growth outlook in FY22.

Supply side pressure on inflation: MPC members agreed inflation risks are supply driven. Prof. Varma pointed "The only source of comfort is that inflation is being driven not by domestic demand, but by supply side factors". Even Dr. Patra pointed out "In the absence of strong demand, the pass-through to retail inflation is likely to be incomplete". Shri Das said "the fragile demand conditions could help limit the pass-through of input cost pressures". However, few members also spoke on being data dependent.

Focus on growth delays normalisation: Dr. Sagar summed up that "But for extra-ordinary circumstances that prevail, we would have moved to a neutral stance long back". He added that "Clear signs of generalisations in CPI inflation setting in could be a tipping point where growth-inflation dynamics could alter". Shri Das explained that "to revive" phrase has been brought in to strengthen forward guidance and demonstrate unambiguous commitment of MPC to revive and sustain growth process. We expect GDP growth at 9.7% in FY22 (RBI at 9.5%). Inflation forecast is at 5.5% for FY22 (RBI at 5.1%) on the back of rising core inflation. US FOMC members are now pencilling in a rate hike in CY23. We believe RBI will be normalising monetary policy in Q4FY22.

KEY HIGHLIGHTS

- MPC members agree impact of second wave on growth is lower than first wave.
- Supply side pressure to inflation. Demand side pressures absent.
- MPC statement added "to revive" to emphasise on forward guidance.



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