

OCTOBER MPC MINUTES

18 October 2019

Growth concerns imply another 25bps cut

MPC minutes show four out of six members favour accommodative stance and further rate cuts as long as economy is firmly on the path to recovery. The remaining two are data dependent. Growth indicators such as IIP, non-food credit, exports and non-oil-non-gold imports have disappointed since the last policy. However, led by higher vegetable prices, headline inflation did touch 4%. We believe this will ebb as fresh crop arrives in the market in the next few weeks/months. Thus another 25bps rate cut is on the cards.

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Growth faltering: MPC members noted that growth momentum has slowed further since the last policy meeting as seen in most high-frequency indicators and RBI's forward looking surveys. Q1 GVA growth slipped to 4.9% with manufacturing at 0.6%. GDP growth was at 5% with consumption at 3.6%. Thus output gap has widened further. This drove the decision to cut rates by 25bps. MPC members welcomed government's recent measures to boost growth and provide liquidity to NBFCs. Cut in corporate tax stands out. On balance, the MPC was of the view that government measures along with better transmission of rates (repo-linked) and a revival in rural demand will result in a cyclical recovery in growth in H2FY20.

Inflation outlook benign: MPC members opined that inflation is expected to be well anchored within MPC's target of 4%. The increase in headline inflation is driven by higher food prices. Core inflation has been trending down because of slowdown in the economy. Seasonal spike in food prices will ebb because above normal monsoon will result in adequate Rabi output. RBI had estimated Q2 CPI inflation at 3.4%. Actual is 3.5% as CPI inflation in Sep'19 increased to 4% led by accelerating food inflation which is mostly seasonal in nature rather than structural and thus should not change RBI's view.

More rate cuts on the card: Persistent negative output gap along with a benign inflation outlook warrant accommodative monetary stance and further cut in policy rate. Four out of six MPC members favour not only continuation of an accommodative stance, but also further reduction in policy rate to kickstart the economy. Two of them (Dr. Chetan Ghate and Dr. Pami Dua) are more inclined towards a data dependent approach. For them, Oct'19 inflation print and Q2FY20 GDP data to be released on 29 Nov'19 will set the framework for policy action. We believe another 25bps rate cut is due.

KEY HIGHLIGHTS

- Growth to remain weak in Q2 led by both domestic and global factors.
- Inflation expected to remain under RBI's target.
- RBI to cut rates further by 25bps to support growth.



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