

RESEARCH

BOB Economics Research | Monetary Policy Review

RBI open to change in policy stance/rates

SUMMARY

India Economics: Monetary Policy Review

While holding rates and its calibrated tightening stance, RBI indicated its willingness to change the same if inflation prints remain subdued. It has revised its H2FY19 inflation forecast lower by 1.2% on the back of muted food inflation and recent decline in oil prices. If the trend sustains, RBI will act accordingly.

While sounding cautious on global growth, RBI remained optimistic on domestic growth. It also indicated that output gap has virtually closed implying narrow range for repo rates. Much depends on global events.

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TOP PICKS

LARGE-CAP IDEAS

Company	Rating	Target
Axis Bank	Buy	750
Cipla	Buy	615
GAIL	Buy	525
Reliance Industries	Buy	1,340
TCS	Buy	2,360

MID-CAP IDEAS

Company	Rating	Target
Greenply Industries	Buy	250
L&T Infotech	Buy	2,070
Laurus Labs	Buy	495
Mayur Uniquoters	Buy	565
Mphasis	Buy	1,360

Source: BOBCAPS Research

DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	2.91	(6bps)	(30bps)	54bps
India 10Y yield (%)	7.57	(5bps)	(21bps)	49bps
USD/INR	70.51	(0.1)	2.7	(9.5)
Brent Crude (US\$/bbl)	62.08	0.6	(14.8)	(0.6)
Dow	25,027	(3.1)	(1.0)	3.0
Shanghai	2,666	0.4	(0.4)	(19.4)
Sensex	36,134	(0.3)	3.2	9.9
India FII (US\$ mn)	30 Nov	MTD	CYTD	FYTD
FII-D	(220.0)	(220.0)	(7,792.2)	(8,038.2)
FII-E	23.1	23.1	(4,866.6)	(6,992.1)

Source: Bank of Baroda Economics Research

BOBCAPS Research

research@bobcaps.in



MONETARY POLICY REVIEW

05 December 2018

RBI open to change in policy stance/rates

While holding rates and its calibrated tightening stance, RBI indicated its willingness to change the same if inflation prints remain subdued. It has revised its H2FY19 inflation forecast lower by 1.2% on the back of muted food inflation and recent decline in oil prices. If the trend sustains, RBI will act accordingly. While sounding cautious on global growth, RBI remained optimistic on domestic growth. It also indicated that output gap has virtually closed implying narrow range for repo rates. Much depends on global events.

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+91 22 6138 9300

research@bobcaps.in

Inflation forecast revised downwards: RBI reduced its inflation forecast to 3% in H2FY19 (earlier 4.2%) and projected H1FY20 print at 4% (earlier Q1 at 4.8%). The downward revision is on the back of muted food inflation and significant decline in oil prices (27% from last policy). Non-food inflation has been inching up as a result of higher fuel prices, currency depreciation and pricing pressure in services. With output gap virtually closed, core inflation in some of the segments is likely to remain on the higher side. However, softer food and fuel prices will ensure that near-term prints are below RBI's target.

KEY HIGHLIGHTS

- RBI keeps rate on hold, stance maintained at calibrated tightening
- Inflation projection for H2FY19 revised downward to 2.7-3.2% from 3.9-4.5% earlier
- GDP forecast retained at 7.4% for FY19

Growth forecast maintained: RBI kept its GDP growth forecast at 7.4% in FY19 as investment activity continues to remain strong. The MPC noted that credit offtake from the banking sector remains robust and is broad-based. In addition, decline in oil prices also augurs well for corporate profitability and consumption demand. Growth forecast for H1FY20 has been increased to 7.5% versus 7.4% in Oct'18. Our FY19 and FY20 growth estimates are slightly lower at 7.3% as moderation in government spending and liquidity issues with NBFCs will impact growth, in our view.

RBI open to change in policy stance/ rate: If the dip in international oil prices is durable and pass-through of MSPs moderate, RBI's new inflation forecasts will materialise. New forecasts suggest a neutral stance than calibrated tightening. RBI has an open mind on this. This did lead to a rally in the bond market with 10Y yield declining to 7.44% (13bps lower). In addition, RBI is likely to continue with OMO purchases (depending upon FX intervention and currency demand) which also supported lower yields. However, output gap is virtually closed so any uptick in international oil prices or US yields/currency may change the domestic inflation outlook materially. Hence, global events may play an important role in future monetary policy direction.



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BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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