

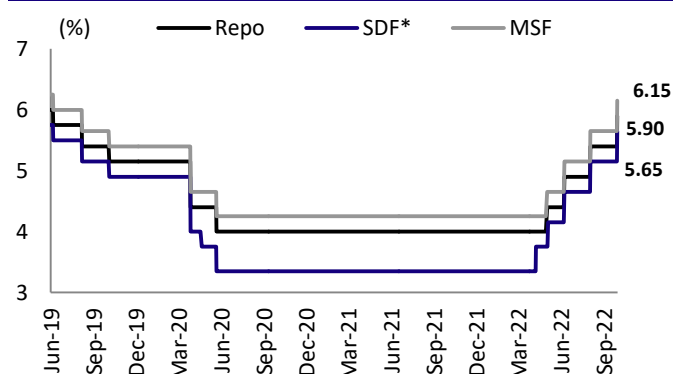
## MPC hikes the policy repo rate by 50bp to 5.9%

We revise our terminal repo rate assumption to ~6.5%

- The RBI hiked its key policy rate (repo) by 50bp to 5.9% on 30<sup>th</sup> Sep'22. Consequently, the SDF and the MSF/bank rate now stands at 5.65% and 6.15%, respectively. The hike was in line with the market and our expectations. This is the fourth rate action by the central bank in FY23 till date. Cumulatively, the RBI has hiked the repo rate by 190bp (excluding the 40bp hike in the SDF in Apr'22) in three scheduled and one out-of-turn policy meetings.
- The MPC reiterated its continued focus on 'withdrawal of accommodation' to contain inflation, while supporting growth. The rate hike decision was arrived at by a 5-1 majority, with Dr. Ashima Goyal voting for a 35bp rate hike. The decision on its stance too was made with a 5-1 majority as Dr. Jayanth Varma expressed reservations on the stance.
- While the RBI kept its inflation forecast unchanged at 6.7%, it revised its real FY23 GDP growth forecast downward to 7% YoY from 7.2% earlier. Its CPI inflation/real GDP growth assumptions stood at 5%/7.2% for 1QFY24.
- The RBI did not change its inflation forecast and seems confident about India's GDP growth. RBI has kept its 2QFY23 inflation projections unchanged at 7.1%, which implies that it expects headline inflation ~7.5% in Sep'22, up from 7% in Aug'22. If so, it will call for another 50bp rate hike in Dec'22 (especially if the US Federal Reserve repeats its 75bp rate hike in Nov'22). Our (revised) base case now is a 35bp hike in Dec'22, followed by another 25bp hike in Feb'23. It is, thus, very likely that the terminal rate during this hiking cycle can be as high as 6.5% by FY23-end.
- Notwithstanding the weaker-than-expected real GDP growth in 1QFY23, RBI has increased its projections for 2HFY23 (to 4.6% from ~4% earlier) and for FY24 (to 6.5% from 6.3% in Apr'22, as per the Monetary Policy Report). It reflects RBI's confidence in India's divergent growth which can fuel further rate hikes. As we do not see India remaining isolated from a global slowdown, we expect further growth downgrades in the economy, especially for FY24.

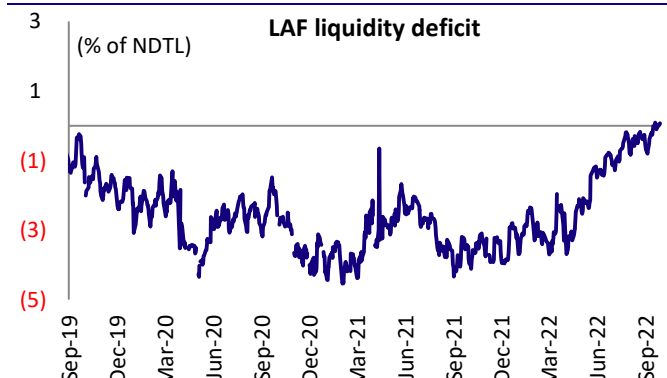
- **Policy repo rate raised to 5.9%:** The RBI hiked its key policy rate (repo) by 50bp to 5.9% on 30<sup>th</sup> Sep'22. Consequently, the SDF and the MSF/bank rate now stands at 5.65% and 6.15%, respectively. The hike was in line with the market and our expectations. This is the fourth rate action by the central bank in FY23 till date. Cumulatively, the RBI has hiked the repo rate by 190bp (excluding the 40bp hike in the SDF in Apr'22). The MPC reiterated its continued focus on 'withdrawal of accommodation' to contain inflation, while supporting growth. The rate hike decision was arrived at by a 5-1 majority, with Dr. Goyal voting for a 35bp rate hike. The decision on its stance too was made with a 5-1 majority as Dr. Varma expressed reservations on the stance.

**Exhibit 1: The RBI raised the repo rate to 5.9% at its Sep'22 monetary policy meeting**



\*Fixed Rate Reverse Repo (FRRR) was replaced by Standing Deposit Facility (SDF) on 8<sup>th</sup> Apr'22

**Exhibit 2: Liquidity deficit as of Sep'22 end stood ~INR187b**



Updated as of 29<sup>th</sup> Sep'22

Source: RBI, MOFSL

## II. The RBI retained inflation, but downgraded its growth forecast for FY23

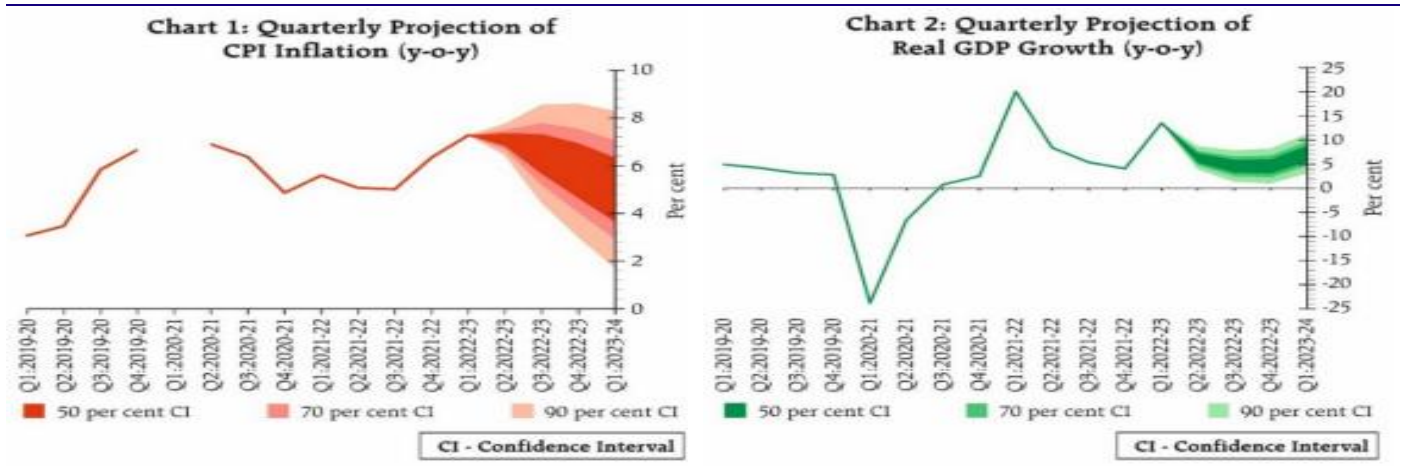
- **CPI inflation forecast retained at 6.7% YoY...:** The RBI Governor said spillovers from geopolitical shocks continue to impart considerable uncertainty to the inflation trajectory, and although global commodity prices have eased, imported inflation remains an upside risk. Other variables such as low Kharif sowing, appreciation of the USD, and transmission of enterprise cost pressures to output prices impart an upward pressure on the inflation trajectory. These factors, along with the assumptions of a normal monsoon in CY22 and average crude oil prices of USD100/bbl, kept RBI's inflation forecast unchanged at 6.7% YoY in FY23 (2Q/3Q/4Q: 7.1%/6.4%/5.8%). Moreover, the RBI expects CPI inflation at 5% YoY in 1QFY24.
- **...but real GDP growth projection for FY23 was revised downward to 7%:** Real GDP stood at 13.5% YoY v/s RBI's projection of 16.2% YoY in 1QFY23. The RBI downgraded its FY23 growth forecast to 7% YoY (2Q/3Q/4Q: 6.3%/4.6%/4.6%) from 7.2% YoY earlier. The RBI seems positive on the back of improving agriculture and allied activities and a rebound in the services sector. The government's thrust on capex, improvement in capacity utilization, and better rural demand may help the economy grow better. While headwinds from geopolitical tensions, tightening global financial conditions, and slowing external demand pose downside risks to India's net exports and its GDP growth outlook. RBI assumes 1QFY24 real GDP at 7.2% YoY.

## III. Our view

- **We revise our terminal rate expectation to ~6.5%:** There seems to be no respite in RBI's tone as far as reducing the pace of rate hikes is concerned. Even though the RBI did not change its inflation forecast and seems confident about India's GDP growth, global factors may influence its decision more than domestic factors. Our (revised) base case now is a 35bp hike in Dec'22, followed by another 25bp hike in Feb'23. It is, thus, very likely that the terminal rate during this hiking cycle can be as high as 6.5% by FY23-end. RBI has kept its 2QFY23 inflation projections unchanged at 7.1%, which implies that it expects headline inflation ~7.5% in Sep'22, up from 7% in Aug'22. If so, it will call for another 50bp rate hike in Dec'22 (especially if the Fed repeats its 75bp rate hike in Nov'22).
- **Real GDP growth forecast may see further downward revisions:** Notwithstanding the weaker-than-expected real GDP growth in 1QFY23, RBI has increased its projections for 2HFY23 (to 4.6% from ~4% earlier) and for FY24 (to 6.5% from 6.3% in Apr'22, as per the Monetary Policy Report). While the Fed, The Bank of England, and the European Central Bank have revised down their CY23 growth forecasts dramatically in the past six months, an upward revision by the RBI is very surprising to say the least. It reflects RBI's confidence in India's divergent growth, which can fuel further rate hikes. As we do not see India remaining isolated from a global slowdown, we expect further growth downgrades in the economy, especially for FY24.

Exhibit 3: Inflation forecast for FY23 retained at 6.7% YoY...

Exhibit 4: ...and real GDP growth downgraded to 7%



Source: RBI, MOFSL

Explanation of Investment Rating	
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SELL	< - 10%
NEUTRAL	> - 10 % to 15%
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