

RBI's Monetary Policy Review

06 Apr 2016

The Reserve Bank of India cut its main lending rate on Tuesday in a widely expected move to help accelerate growth after inflation stayed under control and the government stuck to its fiscal deficit roadmap.

The central bank lowered the repo rate to 6.5 per cent from 6.75 per cent and said the monetary policy stance will remain accommodative. This is the first reduction in six months and brings the repo rate—at which the RBI lends to banks—to its lowest level in five years.

RBI governor Raghuram Rajan had trimmed the repo rate by 125 basis points last year before keeping rates unchanged twice, in September last year and February this year, as he waited for positive signals on inflation and the government's commitment toward fiscal consolidation.

Highlights of the RBI's Monetary Policy Review

- 
- Repo rate cut to 6.5% from 6.75%
 - Cash reserve ratio unchanged at 4%
 - Reverse repo rate raised to 6% from 5.75%
 - Retail inflation to remain around 5% during 2016-17
 - Monsoon, commodity prices upturn risks to inflation
 - Wage hike for government staff upside risk to inflation
 - Tepid global demand, fiscal consolidation to offset risk to inflation
 - Uneven recovery in growth to strengthen in 2016-17
 - Corporate stress, risk aversion among banks risks to growth
 - FY17 growth projection based on gross value added at 7.6%
 - To explore licences for differentiated banks like custodian banks

"We are in a situation just ahead of the monsoon and there could be some nervousness in terms of weather patterns and the monsoon being good or bad, which is something RBI needed to factor in before it went for aggressive rate cut," Indranil Pan, Chief Economist, IDFC, said ahead of the rate-setting meeting.

Finance Minister Jaitley said ahead of the RBI meeting that interest rates needed to be more competitive in the country.

According to the most recent price data, retail inflation in February eased to a three-month of 5.18 per cent as food items turned cheaper. Also, the government has said that it managed to keep the fiscal deficit within the target of 3.9 per cent of gross domestic product for 2015-16 and that it will bring down the gap to 3.5 per cent this fiscal year.

The RBI estimated retail inflation to remain around 5 per cent during 2016-17 and retained the growth forecast for this fiscal year at 7.6 per cent after assuming a normal monsoon and a boost to consumption following an increase in wages of government employees. The uneven recovery in growth will strengthen this fiscal year, it said in its first bi-monthly monetary policy review in the fiscal year that began on April 1.

