

Status Quo on Repo Rate, hike in Reverse Repo.. Neutral Stance

Repo Rate unchanged at
6.25 per cent

Reverse Repo Rate at 6.00%

Marginal Standing Facility and
Bank rate at 6.50%.

GVA growth is projected to
strengthen to 7.4 per cent in
2017-18 from 6.7 per cent in
2016-17

Surplus liquidity at INR3141
billion till end March

RBI to allow banks to invest in
REITs and INVITs and will
issue rules regarding the same by
end of May 2017.

The next meeting of the MPC is
scheduled on 5th & 6th June, 2017
and resolution to be placed on 6th
June 2017.

The Reserve Bank of India (RBI), in its First Bi-Monthly Monetary Policy Review (2017-18), **maintained status quo on the Policy Repo rate** which stands at 6.25 per cent. The **decision was unanimous** with all the six members voting in favor of maintaining status quo.

Consequent upon the narrowing of the LAF corridor, the **Reverse Repo Rate under the Liquidity Adjustment Facility (LAF) has been hiked by 25 bps from 5.75 per cent to 6 per cent** and the **Marginal Standing Facility (MSF) rate and the Bank Rate has been cut by 25 bps from 6.75 per cent to 6.50 per cent.**

The RBI also left the **Cash Reserve Ratio (CRR) of scheduled Banks unchanged at 4% of their net demand and time liability (NDTL).**

The decision of the MPC is consistent with a **neutral stance of monetary policy** in consonance with the objective of achieving the medium-term target of 4 per cent within a band of +/- 2 per cent, while supporting growth.

The move to keep the benchmark rates unchanged was much anticipated. As per Bloomberg survey of 52 economist, all expected RBI to hold rates given its neutral stance in previous policy.

WPI Update

India's Wholesale price index (WPI) based Inflation flared up to two-and-a-half years high of **6.55% YoY in February** from 5.25% YoY in January mainly due to a **spurt in mineral and fuel prices while food prices started rising following demonetization.** The February WPI inflation was steepest since August 2013 when it printed at 6.99%.

CPI Update

India's Consumer Price Index (CPI) based Inflation **increased to 3.65% YoY in February 2017 on account of higher food and fuel prices.** CPI Inflation had dipped to a multi-year low of 3.17% YoY in January this year on account of cash crunch following demonetization. It was **5.26% YoY in February last year.** CPI Food Inflation firmed up to 2.01% YoY in February from just 0.61% YoY in the previous month.

Trade Balance

India's merchandise **exports registered double-digit growth in February 2017**, on the back of a 47% rise in engineering goods and improved international demand. Exports swelled by 17.48% YoY in February to \$24.5 billion but a **steeper increase in imports at 21% widened the trade deficit to \$8.8 billion from \$6.5 billion in the year-ago period.**

IIP

India's Industrial Production growth bounced back to **positive territory in January 2017, on account of a growth in Capital Goods production as well as a rise in the Manufacturing activities. Growth came in at 2.7% YoY in January 2017**, the second fastest monthly growth in FY2016-17, after 5.7% YoY recorded in November 2016. **In December production declined by 0.1% YoY due to a demonetization led contraction in demand.** Except Consumer Nondurables sector, all other subsectors reported growth in January, Capital Goods leading with a 10.7% YoY rise.

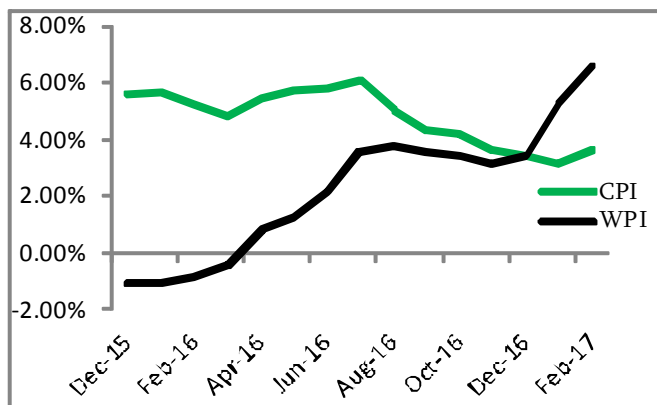
Key Notes

- **GVA growth is projected to strengthen to 7.4 per cent in 2017-18** from 6.7 per cent in 2016-17, with risks evenly balanced
- **RBI plans to allow banks to invest in REITs and INVITs** and will issue rules regarding the same by end of May 2017.
- To curb excess liquidity, RBI plans to continue using MSS and OMO and is **committed to revert the system liquidity to neutrality.**
- RBI sees **CPI inflation undershooting the 5 per cent target for Q4 of 2016-17** in view of the sub 4 per cent readings for January and February. **For 2017-18, inflation is projected to average 4.5 per cent in the first half and 5 per cent during October-March 2018.**
- RBI sees the **risk of inflation at this juncture to be evenly balanced.** However the upside risks going forward remains the uncertainty surrounding the outcome of south west monsoon and its implication on food inflation, 7th Pay Commission, GST and general government deficit further fuelled by farm loan waivers. On the downside, international crude prices have fallen and their pass-through to domestic prices of petroleum products can alleviate pressure on inflation.
- RBI sees government examining standing deposit facility introduction.
- RBI will start **pilot project on financial literacy in nine states.**
- RBI pegs minimum net owned funds for Asset Reconstruction Companies at INR1 billion.
- RBI will **issue new framework by mid April for banks which need corrective actions** which will depend on Net NPA and asset returns.
- Global growth indicators suggest signs of stronger activity in most advanced economies. The **outlook for emerging economies is improving with exports rising strongly.**
- The **future course of monetary policy will largely depend on incoming macroeconomic data.**
- With progressive remonetisation, the surplus **liquidity in the banking system declined from a peak of INR7,956 billion on January 4** to an average of INR6,014 billion in February and further down **to INR4,806 billion in March.**
- Progressive remonetisation, improved transmission of earlier rate cuts, GST, Budget proposals for capital expenditure, Insolvency and Bankruptcy Code, upsurge in IPO market will boost investor confidence and bring in efficiency gains.

Indian Government 10 Year Bond Yield



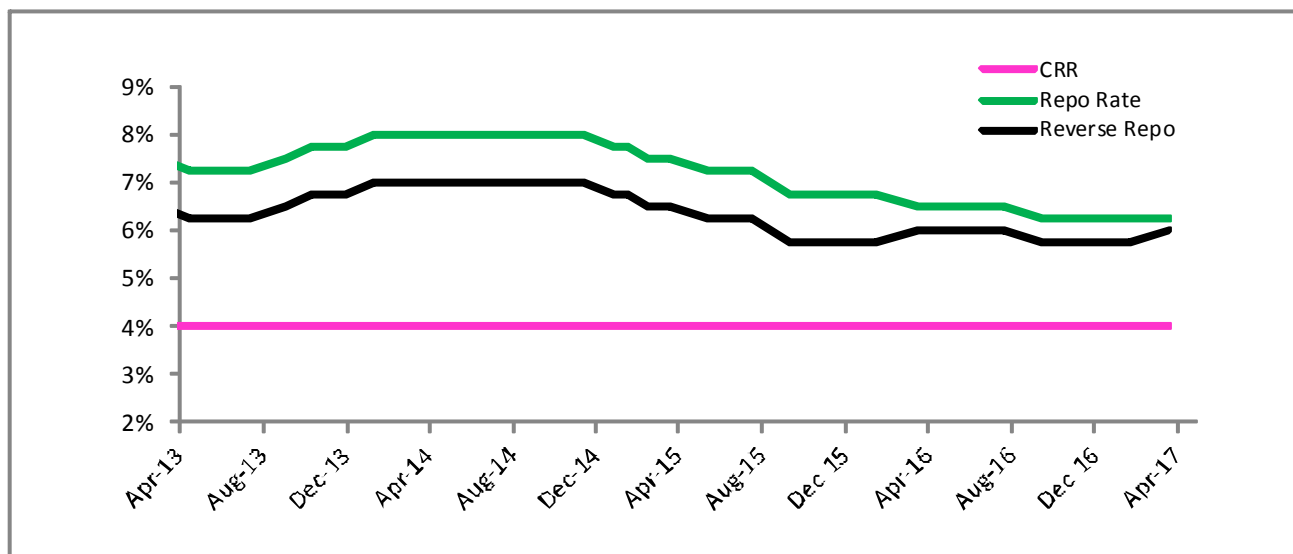
India's CPI and WPI Trend



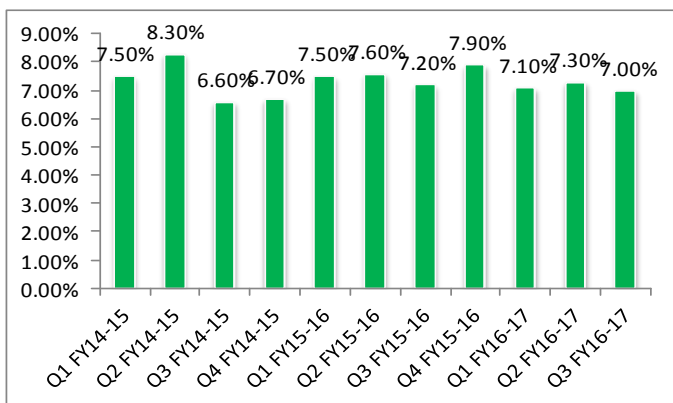
Key Quotes by MPC

- *MPC sees path of inflations challenged in second half of 2017-18*
- *As per Governor, well capitalized banks are key to policy transmission*
- *As per Deputy Governor, there is more demand for bank capital and bank's stressed assets have deteriorated*
- *Patel sees farm loan waivers have general moral hazard which undermines honest credit culture*
- *MPC sees Emerging economies stable and RBI prepared for Fed hikes and the neutral stance as adequate*

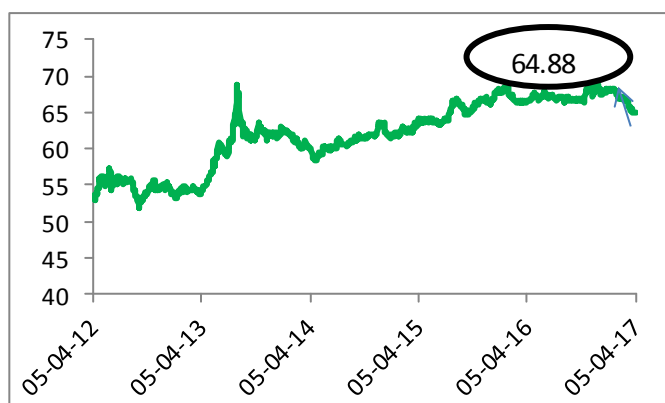
RBI's Monetary Policy Stance



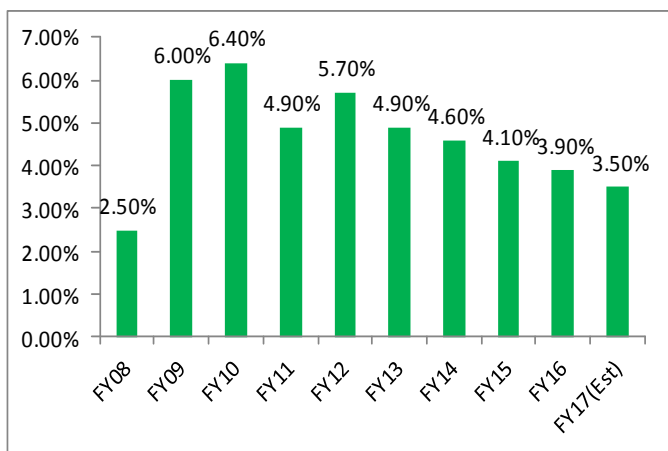
India's GDP Growth Trend



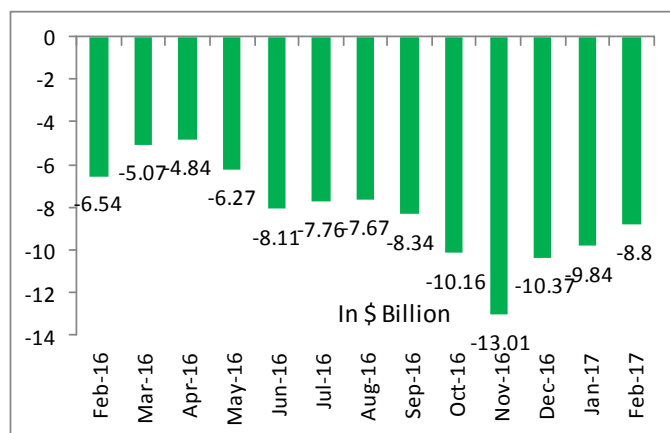
INR Vs US Dollar



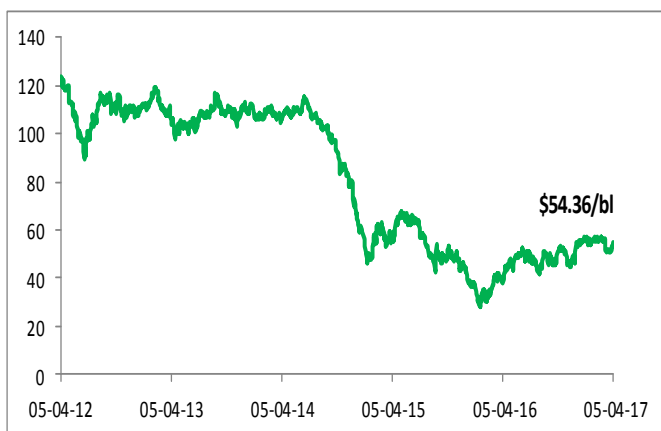
India's Fiscal Deficit Trend



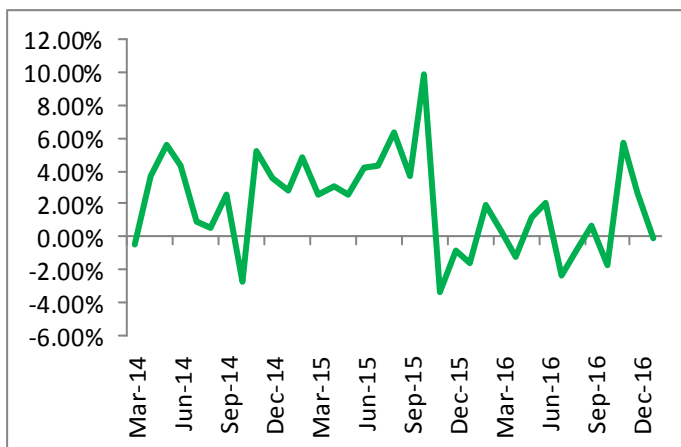
India's Trade Deficit Trend



Brent Crude Price Trend (In \$/bbl)



India's Industrial Production Trend



Market Impact

The market had already anticipated RBI to hold the repo rates at 6.25 per cent but what came in as a surprise was narrowing of the policy corridor to 25 bps. Consequently, RBI raised the reverse repo rate by 25 bps from 5.75 per cent to 6.00 per cent, effectively tightening policy by increasing the cost of overnight money.

The yield on the sovereign bonds due September 2026 was up 9 basis points from Wednesday's close of 6.65 per cent to 6.74 per cent immediately after the policy announcement. It furthered to 6.769 per cent as at 5 pm.

The rupee continued to appreciate against dollar and strengthened today by 0.54 per cent to end at 64.5338/\$.

The Bank Nifty recovered from the day's low of 21488.90 to move upto day's high of 21572.70 and settled at 21622.95.

One of the key highlights of the policy was RBI's decision to allow banks to invest in Real Estate Investment Trusts (REITs) and Infrastructure Investment Trust (INVITs) within limit. This led to gains in real estate and infrastructure sector.

Intraday Indian Government 10Y Bond Yield Chart



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Stock Recommendation	Expected absolute returns (%) over 12 months
Strong Buy	>20%
Buy	between 10% and 20%
Hold	between 0% and 10%
Sell	0 to <-10%
Neutral	No Rating

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