

# RBI Repo Rate Cut - October 2019

### Why in news?

The six-member Monetary Policy Committee (MPC) of the Reserve Bank of India (RBI) slashed the short-term lending rate, repo rate, by 25 basis points to 5.15%.

#### How is the rate cut trend?

- There was an unconventional 35 basis points cut in interest rates by the RBI in <u>August 2019</u>.
- The RBI has now returned to a normal 25 basis points cut.
- With this, the central bank has pruned rates by 135 basis points in just 7 months since the rate cut cycle started in February 2019.
- Of this, until August, banks had passed on just 29 basis points to borrowers.
- But, major banks recently shifted to an <u>external benchmark</u> mostly linked to the repo rate.
- So, the transmission of benefits to borrowers could be quicker from here onwards.

# What is the change in growth projections?

- The RBI has sharply marked down the GDP growth projections for the current fiscal to 6.1%.
- This is down from the 6.9% that it had projected in the August policy.
- The downgrade was inevitable after the shocking 5% growth reported in the first quarter.
- However, even the revised estimate is a bit too optimistic.
- If the projection of 6.1% for 2019-20 is to be met, the economy has to grow by about 7% in the second half, which does not look very likely.
- Given this, the basis for RBI's optimism appears unclear at this moment.

### How does the future look?

- The central bank has been taking a liberal stance in making repo rate cuts in the last few months.
- Given this, monetary policy may well be nearing its limits in so far as its ability to influence growth prospects is concerned.
- Inflation is well within the target giving space to the RBI to focus on growth.
- Crude oil prices are back in the comfort zone, retreating from the spike in

mid-September 2019.

- Food prices are projected to remain soft on the back of a good monsoon.
- The monetary policy statement is unambiguous that the RBI will continue with its accommodative stance "as long as it is necessary to revive growth".

## Why is fiscal policy measure crucial now?

- The problem is that the central bank can only facilitate lower rates and push banks to lend.
- It cannot force borrowers to borrow and this is evident from the soft trends in credit offtake in the last few months.
- As per latest available data, bank credit is growing at just 10.3%.
- The onus, therefore, is on fiscal policy which alone can boost borrowing and investment.

### What lies ahead?

- To be fair, the government has been engaging the levers, and the recent corporate tax cut measure is a major move to get private investment going.
- However, the Rs.1.45 lakh crore giveaway has set off fears in the market of a fiscal slippage and higher borrowings by the government.
- These concerns also explain the unenthusiastic response of the stock and bond markets to the current rate cut.
- The ongoing festival season consumption holds the key to revival of the economy this fiscal.

**Source: The Hindu** 

