

## RESEARCH

### BOB Economics Research | Monetary Policy Review

Rate cuts to resume in Q1FY21

## SUMMARY

### India Economics: Monetary Policy Review

RBI kept repo rate on hold as it revised its inflation trajectory upwards to 4.9% in H2FY20 from 3.6% in Oct'19. Inflation is likely to be within target range in Q2FY21. While growth is expected to pick-up from 5% in FY20 to 6.1% in H1FY21, it is still well below potential. Hence, we believe rate cut cycle is likely to resume in Q1FY21. In the interim, surplus liquidity conditions and anticipation of more rate cuts will ensure faster transmission. A change in fiscal stance or geo-political events driving oil prices are key risks to our view.

[Click here for the full report.](#)

## TOP PICKS

### LARGE-CAP IDEAS

Company	Rating	Target
<a href="#">Cipla</a>	Buy	570
<a href="#">ONGC</a>	Buy	210
<a href="#">Petronet LNG</a>	Buy	400
<a href="#">Reliance Industries</a>	Buy	1,670
<a href="#">TCS</a>	Add	2,230

### MID-CAP IDEAS

Company	Rating	Target
<a href="#">Alkem Labs</a>	Buy	2,290
<a href="#">Future Supply</a>	Buy	680
<a href="#">Greenply Industries</a>	Buy	210
<a href="#">Laurus Labs</a>	Buy	480
<a href="#">PNC Infratech</a>	Buy	245

Source: BOBCAPS Research

## DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	1.77	6bps	6bps	(114bps)
India 10Y yield (%)	6.47	0bps	2bps	(97bps)
USD/INR	71.53	0.2	(1.0)	(1.5)
Brent Crude (US\$/bbl)	63.00	3.6	2.1	2.3
Dow	27,650	0.5	1.1	10.5
Shanghai	2,878	(0.2)	(2.7)	8.6
Sensex	40,850	0.4	1.7	13.8
India FII (US\$ mn)	3 Dec	MTD	CYTD	FYTD
FII-D	167.7	171.8	4,416.6	3,871.9
FII-E	(14.4)	(216.2)	13,156.2	6,311.0

Source: Bank of Baroda Economics Research

## BOBCAPS Research

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## MONETARY POLICY REVIEW

05 December 2019

### Rate cuts to resume in Q1FY21

**RBI kept repo rate on hold as it revised its inflation trajectory upwards to 4.9% in H2FY20 from 3.6% in Oct'19. Inflation is likely to be within target range in Q2FY21. While growth is expected to pick-up from 5% in FY20 to 6.1% in H1FY21, it is still well below potential. Hence, we believe rate cut cycle is likely to resume in Q1FY21. In the interim, surplus liquidity conditions and anticipation of more rate cuts will ensure faster transmission. A change in fiscal stance or geo-political events driving oil prices are key risks to our view.**

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**MPC holds rates on inflation concerns:** Contrary to consensus and our forecast of a 25bps rate cut, MPC members kept repo rate unchanged at 5.15%. This was on the back of sharp jump in CPI inflation to 4.6% in Oct'19 and anticipated elevated trajectory in Q4FY20. For H2FY20, RBI has now revised its inflation forecast to 4.9% from 3.6% in Oct'19. Inflation expectations for 3-month and 1-year horizon have also risen by 120bps and 180bps respectively which seem to have restrained members from cutting rates now. As per RBI's revised guidance, CPI inflation is expected to fall below target only in Q2FY21.

**FY20 growth revised to 5% from 6.1%:** As expected RBI reduced its GDP forecast for FY20 by 110bps from Oct'19 to 5% now. Growth in H1FY21 is now expected at 6.1%. The up-tick in growth in FY21 is expected on the back of 1) transmission of earlier rate cuts, 2) economic measures announced by the government and 3) pick-up in rabi sowing with water reservoirs at 86% of capacity (61% last year). Credit and liquidity conditions in the real economy will also ease given the FDI/ FPI inflows this year and surplus liquidity in the banking system. Given the negative output gap, we expect RBI to cut rates again in Q1FY21 as growth remains well below potential in H1FY21 as well.

**Rate cut guidance maintained:** While all members unanimously voted for no change, the rate cut cycle will have to wait for inflation to be within the target range. At the same time, MPC members indicated that accommodative stance will continue as long as it is necessary to revive growth. Surplus liquidity and further rate cuts are important for transmission as 55% of deposits of SCBs are more than 1-year vintage. Hence, visible transmission is likely to happen from Feb'20, a year after beginning of rate cutting cycle. We see surplus liquidity conditions to drive faster transmission in H1FY21.

#### KEY HIGHLIGHTS

- Inflation forecast revised upward by 130bps in H2FY20 to 4.9%
- GDP growth forecast for FY20 revised downward to 5%
- Inflation concerns prompted status quo. Scope remains for 25bps rate cut in Q1FY21.



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### Recommendations and Absolute returns (%) over 12 months

**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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