Interest Rates Unchanged

Why in news?

Recently RBI's Monetary Policy Committee has opted for accommodative stance and kept its interest rates unchanged.

How did earlier RBI measures performed?

- Earlier Monetary Policy Committee has pulled out all stops in announcing liquidity enhancement measures, besides cutting the repo rate by 115 basis points.
- These steps did not improve the bank credit take off and in the yield curve the short-end fell below the reverse repo level.
- In the long-end, yields sharpened to rise above 6% amidst global fears of commodity-induced inflation and heightened government borrowing plan.
- Operation Twist, where the RBI purchases long-term instruments and sells short-term ones to keep the costs of government borrowing in check, seems to lose effect.

What was the statement after the meeting?

- It maintained its projection for GDP expansion in the current fiscal at 10.5%.
- The accommodative policy stance ensures that economic growth becomes durable and will support at a time when there is jump in COVID-19 infections.
- The rise in infection can dampen the demand for contact-intensive services, restrain growth impulses and prolong the return to normalcy.
- The MPC noted that consumer confidence has dipped which is a sign that uncertainty clouds the outlook for growth.
- Moreover IHS Markit's Manufacturing Purchasing Managers' Index (PMI) survey revealed that business sentiment slid to a seven-month low.
- It also reported that both manufacturers and services companies continued to shed jobs for a 13th month.
- With jobs and incomes remaining under stress, uncertainty over the efficacy and safety of the vaccines persisting, it is hard to foresee consumption demand rebounding to pre-COVID levels.

What are the other observations?

- Core inflation had hardened and increased by 50 basis points.
- RBI is cognisant of the fact that there are both upside and downside pressures which can impact the trajectory of retail inflation.
- RBI also stated that monsoon rains will have significant effect on food prices, which have been a recent source of upward pressure on price stability.
- It also stressed the vital need for the Centre and States to initiate some coordinated action to ease the tax burden on petroleum products.
- High international commodity prices and logistics costs are also threatening to push up input costs across the manufacturing and services sectors.
- Even RBI's own survey on inflation expectations shows that urban households expect prices to accelerate.

What is the strategy adopted now?

- RBI has unveiled a new instrument to tap secondary market G-Secs (G-SAP 1.0).
- It has decided to extend some credit and liquidity boosting steps beyond the March 31 deadline.
- This includes the targeted long-term repo operations for NBFCs by another six months in view of their interface with small businesses.
- States' Ways and Means Advances limits have been raised which can help them in the wake of Covid-induced fiscal stress.
- The onus now lies on fiscal policy to deliver on both growth as well as inflation reduction.

Source: The Hindu, Business Line