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US Federal Reserve's Stance and India

What is the news about?

US central bank's statement reiterating that it would maintain an 'accommodative stance' until inflation and employment targets had been met boosted Indian markets.

What is the US's quantitative easing about?

- The economy of US was faring poor with jobless rate of 5.2 percent in August due to lockdowns.
- The Fed opted for Quantitative Easing through Open Market Operations for injecting money into the economy.
- It started to buy bonds to keep long-term interest rates low inducing banks to give loans to genuine borrowers to uplift the economy.

What did the Federal Reserve say?

- Federal Reserve said that it would continue to maintain an **accommodative stance** of monetary policy until it achieves an inflation moderately above 2%.
- It has decided to keep the target range for the federal funds rate at 0 to 1/4%.
- It also said that if progress in the economy continues, moderation in the pace of asset purchase (tapering bond buying) may be guaranteed soon.

Tapering means gradual slowing down of purchases of securities and bonds. Once the tapering is complete, the Fed may go for reduction in the size of the balance sheet to slowly remove the monetary stimulus.

What does the Fed's decision mean?

- Low interest rates in the US will ensure continued fund flows from foreign portfolio investors (FPIs) into Indian equities
- An end to asset purchases by mid-2022 will strengthen the case for raising rates in 2023.
- Tapering bond buying could see some outflows from Emerging Markets

like India but RBI has prepared the economy well enough by accumulating sufficient foreign exchange reserves.

What will be the trend of Indian markets ?

- There is hope that the economy will witness further reopening and faster consumption-driven growth with faster vaccination.

- Improving domestic economic conditions and the reduction of concerns around Evergrande will boost the Indian markets.
- The progress made towards including Indian sovereign bonds in global bond indices is a welcome step.
- The introduction of Fully Accessible Route (FAR) for FPIs investing in G-secs in 2020 is an important move.
- Inclusion of G-Secs in GBI EM and GBI Aggregate indices by early 2022 will result in annual inflows of $18.5 billion over the next decade.
- Also these inflows are likely to be more stable and long-term in nature when compared to the hot money.
- Centre's clarity on taxation of these securities is needed when both the buyer and seller are not Indian citizens and the intermediary is also outside India.
- Other minor bottlenecks such as simplifying the registration process for FPIs wishing to invest in G-secs and providing access to hedging tools to FPIs should speed up.

Source: Businessline, The Indian Express