# RBI monetary Policy statement highlights

October 19, 2020

The **newly appointed Monetary Policy Committee (MPC) with Dr. Ashima Goyal, Professor Jayanth R. Varma and Dr. Shashanka Bhide as external members** conducted its first meeting and the 25th under the monetary policy framework that was instituted in June 2016.

## Content:

- The MPC evaluated domestic and global macroeconomic and financial conditions and left the **policy repo rate unchanged at 4 percent.**
- It also decided to continue with the accommodative stance of monetary policy as long as necessary.
- The **Marginal Standing Facility (MSF)** rate and the Bank rate remain unchanged at **4.25 per cent.**
- The reverse repo rate stands unchanged at 3.35 per cent.

## Charting the Recovery:

- After the steep decline in economy in the second quarter of 2020, global economic activity appears to have rebounded sequentially in the third quarter, but unevenly among and within economies.
- Improvement in manufacturing, labour markets and retail sales powered strong recoveries in some countries.
- A rise in new infections prompted a slower pace of unlocking or re-imposition of restrictions which stalled the upturn.
- Investment has remained in retrenchment while consumption and exports have started to improve.
- Massive policy support across all countries has prevented a deeper downslide, providing a floor

underneath employment, household incomes and businesses.
- Forward-looking business expectations are optimistic on the overall business situation, production, order books, employment, exports and capacity utilisation.

## Status of Indian economy:

- The Indian economy is entering into a decisive phase in the fight against the pandemic.
- The focus must now shift from containment to revival.
- Undeterred by the pandemic, the rural economy looks resilient.
- Kharif sowing has already surpassed last year's acreage as well as the normal sown area.
- Improved soil moisture conditions, along with healthy reservoir levels, have brightened the outlook for the rabi season.
- Early estimates suggest that food grains production is set to cross another record in 2020-21.
- Job creation under the Mahatma Gandhi National Rural Employment Guarantee Act (MNREGA) has provided incomes and employment in rural areas.
- Meanwhile, migrant labour is returning to work in urban areas, and factories and construction activity are coming back to life.
- This is also reflected in rising levels of energy consumption and population mobility.
- In the September 2020 round of the RBI's survey, households expect inflation to decline modestly over the next three months, indicative of hope that supply chains are mending.
- The manufacturing purchasing managers' index (PMI) for September 2020 rose to 56.8, its highest mark since January 2012, supported by acceleration in new orders and production.
- There has been talk of a **K-shaped recovery.** It is likely to predominantly be a **three-speed recovery,** with

individual sectors showing varying paces, depending on sector-specific realities.

1. Sectors that **would 'open their accounts' the earliest** are expected to be those that have shown resilience in the face of the pandemic and are also labour-intensive – Agriculture and allied activities, fast moving consumer goods, two wheelers, passenger vehicles and tractors, drugs and pharmaceuticals, and electricity generation, especially renewables, are some of the sectors in this category.
2. The second category of **sectors to 'strike form'** would comprise sectors where activity is normalising gradually.
3. The third category of sectors would include the **ones which face the 'slog overs',** but they can rescue the innings. These are sectors that are most severely affected by social distancing and are contact-intensive.

- Both private investment and exports are likely to be subdued, especially as external demand is still anaemic.
- For the year 2020-21 as a whole, real GDP is expected to decline by 9.5 percent.
- The limit for Ways and Means Advances (WMA) for the centre has been kept higher at ₹1.25 lakh crore compared to ₹35,000 crore in H2 of the previous year.
- Similarly, the 60 percent increase in WMA limit for states in the first half of 2020-21 has been extended till March 31, 2021.
- Headline inflation has moved up from March 2020 levels and has persisted above the tolerance band of the target, but would ease gradually towards the target over Q3 and Q4.
- The supply disruptions and associated margins/mark-ups are the major factors driving up inflation.
- Large excess supply conditions characterize food grains and horticulture production, and the outlook for

agriculture is bright.
- Crude prices remain range-bound.
- As the threat of COVID-19 is yet to abate, with the gradual lifting of restrictions on movement of people and opening of business establishments across the country, a resumption of economic activities is well underway.

## Focus of the Reserve Bank's regulatory actions:

- To provide an immediate relief to the borrowers from the impact of COVID-19, through extension of moratorium and other measures.
- To facilitate resolutions through the Resolution Framework for COVID-19 related stress.
- The lending institutions focusing on revival of activity and their core activity of lending.

These measures are intended to-

(i) enhance liquidity support for financial markets so as to revive activity in targeted sectors of the economy;

(ii) provide a boost to exports;

(iii) regulatory support to improve the flow of credit to specific sectors;

(iv) deepen financial inclusion;

(v) facilitate ease of doing business by upgrading payment system services.

***Liquidity Measures and Financial Markets***

- The focus of liquidity measures by the RBI will now include revival of activity in specific sectors that have both backward and forward linkages, and multiplier effects on growth.
- It has been decided to conduct on tap Targeted long-term

repo operations (TLTRO) with tenors of up to three years for a total amount of up to ₹1,00,000 crore at a floating rate linked to the policy repo rate.

- The scheme will be available up to March 31, 2021 with flexibility with regard to enhancement of the amount and period after a review of the response to the scheme.
- Liquidity availed by banks under the scheme has to be deployed in corporate bonds, commercial papers, and non-convertible debentures.
- The liquidity availed under the scheme can also be used to extend bank loans and advances to these sectors.
- To improve liquidity and facilitate efficient pricing, it has been decided to conduct open market operations (OMOs) in State Development Loans (SDLs) as a special case during the current financial year.

## *Support to Exports*

- As part of automation of Export Data Processing and Monitoring System (EDPMS), the 'Caution / De-caution Listing' of exporters was automated in 2016.
- Accordingly, the exporters were to be caution-listed automatically, if any shipping bill against them remained outstanding for more than 2 years in EDPMS.
- The normal system of caution-listing based on the recommendations of the Authorised Dealer (AD) bank before the expiry of 2 years in certain cases continued.
- In order to make the system more exporter friendly and equitable, it has been decided to discontinue the Automatic Caution-listing and RBI will continue with caution-listing based on the case-specific recommendations of the AD bank.

## *Regulatory Measures*

- As per the present RBI instructions, the exposures included in the regulatory retail portfolio of banks are assigned a risk weight of 75 per cent.

- In order to reduce the cost of credit for segments consisting of individuals and small businesses (i.e. with turnover of upto ₹50 crore), it has been decided to increase this threshold to ₹7.5 crore.
- This measure is expected to increase the much needed credit flow to the small business segment.

***Financial Inclusion***

- The RBI in 2018, put in place a framework for co-origination of loans by banks and a category of NBFCs for lending to the priority sector subject to certain conditions. The arrangement entailed joint contribution of credit at the facility level, by both the lenders. Now it has been decided to extend the scheme to all the NBFCs (including HFCs), to make all priority sector loans eligible for the scheme and give greater operational flexibility to the lending institutions. The proposed framework will be called the "**Co-Lending Model**".

***Payment and Settlement Systems***

- It has been decided to make the Real Time Gross Settlement System (RTGS) system round the clock on all days. With this, India will be one of the very few countries globally with a 24x7x365 large value real time payment system. It comes to effect from December 2020.
- Under the Payment and Settlement Systems Act, 2007 the RBI currently gives on tap authorisation to payment system operators (PSOs) for limited periods of up to five years. Now it has been decided to grant authorisation for all PSOs (new applicants as well as existing PSOs) on a perpetual basis, subject to certain conditions.
- This will reduce compliance costs and create a climate conducive for investment activities, increased employment, and infusion of new talent and technologies

into value chains.