

## Monetary Measures

CRR	Unchanged 5.00%
SLR	Unchanged 24.00%
Repo Rate	Cut 50 bps to 5.00%
Reverse Repo Rate	Cut 50 bps to 3.50%
Bank Rate	Unchanged 6.00%

## Observations

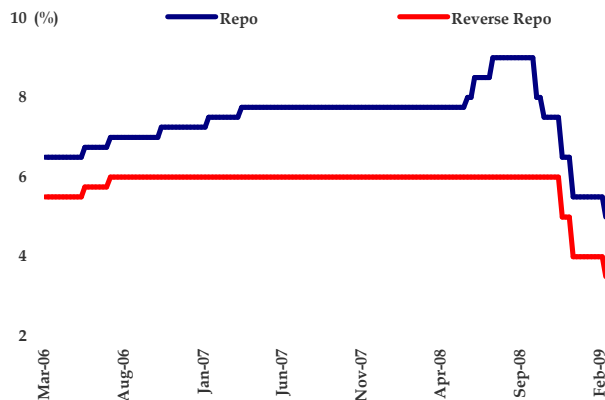
Frequent policy action by RBI in response to Market Call  
Market rates no longer move in tandem with policy rate  
Deposit and Lending rates to step down a bit  
Net Repo volumes indicate high risk perception leading to slowdown in credit offtake

## RBI cuts Repo and Reverse Repo Rate: Signals soft interest rate regime, tips banks to lend more

RBI has cut Repo & Reverse Repo rate each by 50bps. Within few days after the election announcement and code of conduct kicks in, after which of course government cannot take any fiscal action, regulator has announced its monetary action in terms of rate cut.

Rate cut is probably after taking clue from reverse repo window, which intensified and averages ~525 bn during last month. Rate cut is also a medium to show its concern on slowing industrial activity, higher unemployment & disappointing GDP advance estimates for Q3FY09.

Whether the rate cuts would converge in to PLR cuts and cut in lending rate is really questionable. In times of crisis, link between policy rates and effective lending rates do get broken to some extent. Even further cuts in repo and reverse repo seem to be limited as they are at their all time low. Repo at 3.5% is equal to the rate offered on saving bank deposits.



For cutting lending rate by banks, it will also have to cut deposit rate of similar magnitude to preserve their margins. Deposit growth is already struggling at 21% mainly on account of slowdown in economic activity and continuous outflow of foreign capital. With further decrease in interest on term deposit along with the fact that the government securities continue to offer ~8%, term deposit will continue to become unattractive. With the scarcity in source of funds, banks will not really be able to disburse credit at required rate, of course the pile up of investments might weight down a bit.

RBI has kept the CRR rate unchanged, as there seems to be adequate liquidity in the system, which is clearly reflected in the call rates and net repo volumes. Call Rates have started touching 4%, after crossing 15% in September. Net Repo volumes, despite rate cut are turning negative.

RBI has been doing much of the big-bang action out of scheduled monetary policy. Regulators have become much more pro active rather than waiting for the monetary policy. RBI seems to maintain its stance of achieving an optimal balance between preserving financial stability, maintaining price stability, anchoring inflation expectation and sustaining growth momentum.

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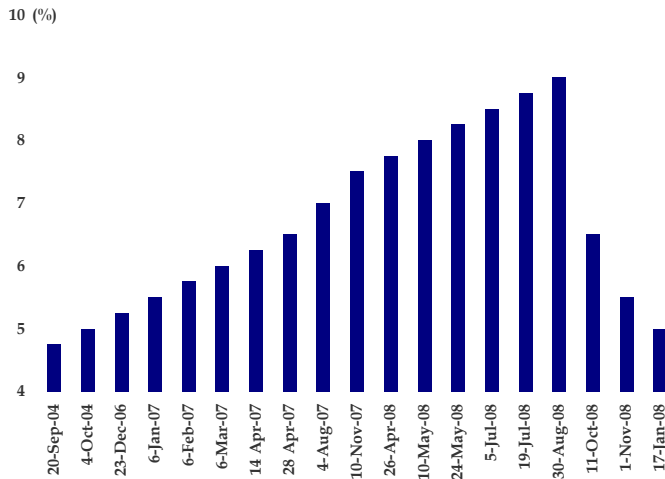
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### CRR Rate

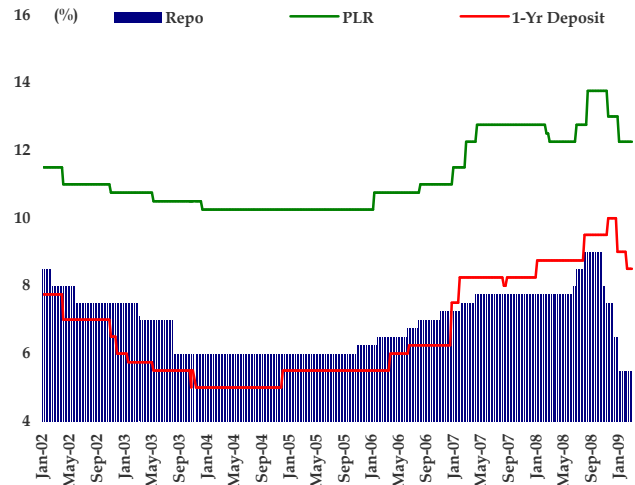
After a 50 bps cut in CRR in mid-January, regulators have kept the rate unchanged, as there seems to be adequate liquidity in the system.



Source: Khandwala Research, Bloomberg

### Repo/PLR/Deposit Rates

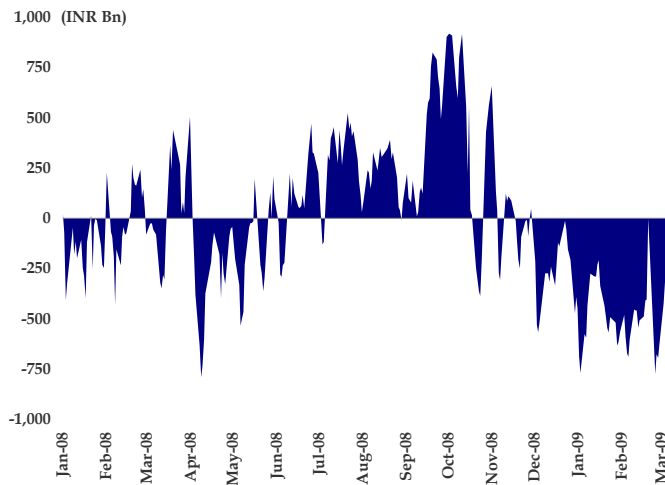
Difference between the repo and deposit rate has increased, reflecting a de-link between the policy rates and deposit rates.



Source: Khandwala Research, Bloomberg

### Net Repo Volumes

Net Repo volumes have turned negative, even after series of steps taken by RBI. Banks have parked daily average of Rs 525 billion with RBI since last month. It clearly indicates adequate liquidity scenario in the system.



Source: Khandwala Research, Bloomberg

### Inflation

On the positive side, headline inflation, as measured by the wholesale price index, has fallen sharply, and the decline has been sustained for the past two months, pointing to a faster than expected reduction in inflation.

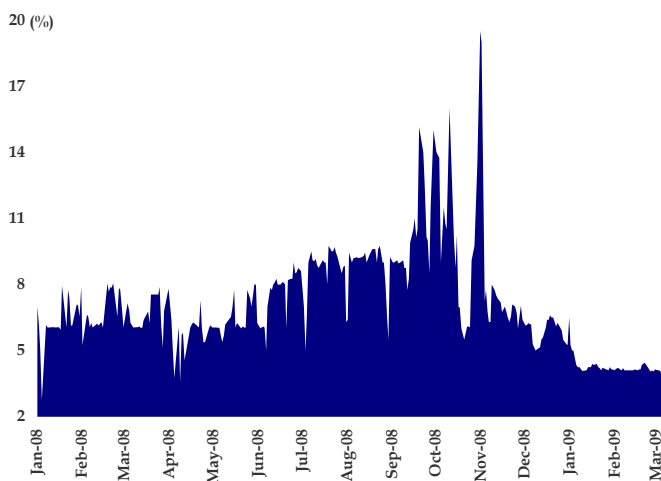


Source: Khandwala Research, Bloomberg



### Call Rate

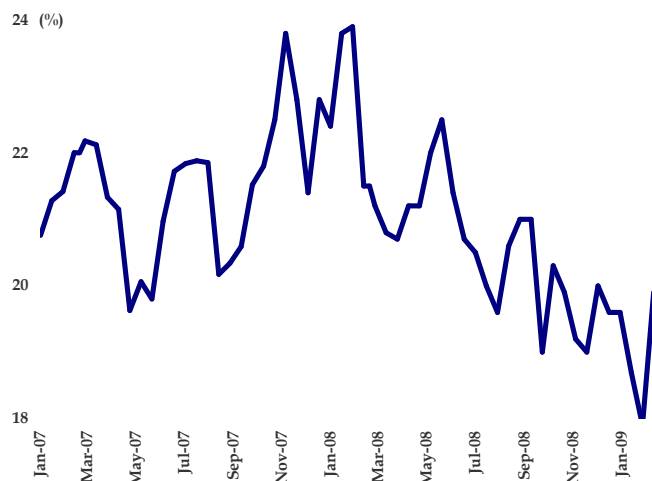
Call Rate have cooled down, as liquidity scenario improves significantly. Call rates are hovering between Repo and Reverse Repo rate, which also indicates call money market is back to its sustainable levels.



Source: Khandwala Research, Bloomberg

### Money Supply / Liquidity

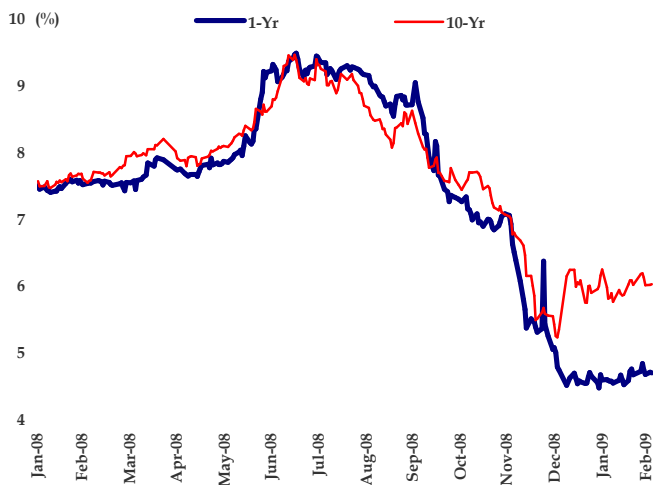
Money supply (M3) increased 19.9% as on Feb 13, 2009. RBI intends to moderate money supply growth to 17.0% in 2008-09. Although it has shown signs of cooling down, still the regulators would continue to monitor and act upon any surge.



Source: Khandwala Research, Bloomberg

### G-Sec Yield

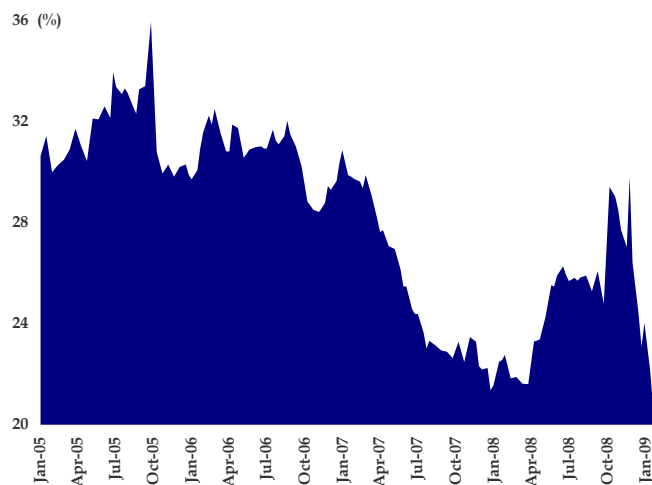
Gsec yields have corrected in line with inflation and money supply. However the long end of the yield tightened off late on account of announcement of additional government borrowings.



Source: Khandwala Research, Bloomberg

### Credit Growth

Credit growth has slowed down on account of increased risk perseverance within banks. Current credit growth of 19.5% is well below RBI's target of 24%.



Source: Khandwala Research, Bloomberg



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