

Fig 1: Macro projections, Feb'25 vs Dec'24 MPC

| RBI MPC's Projections | | | | |
|-----------------------|------------|------------|--------------|------------|
| | GDP | | CPI | |
| | Dec'24 MPC | Feb'25 MPC | Dec'24 MPC | Feb'25 MPC |
| Q3 FY25 | 6.8 | - | 5.6 (actual) | |
| Q4 FY25 | 7.2 | - | 4.5 | 4.4 |
| FY25 | 6.6 | 6.4 | 4.8 | 4.8 |
| Q1 FY26 | 6.9 | 6.7 | 4.6 | 4.5 |
| Q2 FY26 | 7.3 | 7.0 | 4.0 | 4.0 |
| Q3 FY26 | - | 6.5 | - | 3.8 |
| Q4 FY26 | - | 6.5 | - | 4.2 |
| FY26 | - | 6.7 | - | 4.2 |

| UBI vs RBI MPC Projections | | | | |
|----------------------------|------------|-----------|--------------|-----------|
| | GDP | | CPI | |
| | Feb'25 MPC | UBI Proj. | Feb'25 MPC | UBI Proj. |
| Q3 FY25 | - | 6.0 | 5.6 (actual) | |
| Q4 FY25 | - | 6.7 | 4.4 | 4.0 |
| FY25 | 6.4 | 6.0-6.2* | 4.8 | 4.7 |
| Q1 FY26 | 6.7 | - | 4.5 | 4.1 |
| Q2 FY26 | 7.0 | - | 4.0 | 4.0 |
| Q3 FY26 | 6.5 | - | 3.8 | 3.6 |
| Q4 FY26 | 6.5 | - | 4.2 | 4.2 |
| FY26 | 6.7 | 6.5 | 4.2 | 4.0** |

*currently tracking with downward bias;
** currently tracking and risks need close watch;

Source: RBI, UBI Research

▪ **Unanimous decision to cut rates; stance held as neutral to retain flexibility**

The RBI led Monetary Policy Committee (MPC) decided unanimously to reduce the policy repo rate by 25bps to 6.25% which was the first cut in five years. The MPC also voted unanimously to retain the monetary policy stance as 'neutral', and to remain unambiguously focused on a durable alignment of inflation with the target, while supporting growth. Excessive volatility in global financial markets and continued uncertainties about global trade policies coupled with adverse weather events pose risks to the growth and inflation outlook. This calls for the MPC to remain watchful. Accordingly, it decided to continue with a neutral stance. This will provide MPC the flexibility to respond to the evolving macroeconomic environment.

The MPC also noted that though growth is expected to recover from the low of Q2 FY25, it is much below that of last year. Supported by a favorable outlook on food and continuing transmission of past monetary policy actions, inflation is expected to further moderate in FY26, gradually aligning with the 4% target. These growth-inflation dynamics opens up policy space for the MPC to support growth, while remaining focused on aligning inflation with the target.

In conclusion, from a policy mix perspective, the Budget has played a crucial role in boosting the demand-side growth levers, while monetary policy is likely to attempt to do the supply-side growth heavy-lifting. They together attempt to shift the slowing "growth narrative" for global investors.

Market impact: The rate cut was on expected lines and the markets had already factored it in. The equity markets fell more than 500 points post the RBI announcement reflecting investors disappointment with RBI's decision and stance on future rate cuts. The 10-year bond yields spiked as the MPC unanimously voted to continue with a neutral stance while disappointment was seen on the back of any specific liquidity announcements. The rupee has shown a much better response on the back of Dollar weakness and as the event is largely priced in. Following the MPC announcement, the rupee strengthened by 25 paise against the US dollar intraday versus yesterday's close of 87.58 and closed 15 paise higher at 87.43 against the previous day's close.

▪ **We see scope for further downside risk to growth-inflation projections**

We see downside risk to even FY25 inflation projections with Q4 FY25 CPI tracking ~4% in our view versus 4.4% forecast from the MPC (revised downward from 4.5%). Our inflation forecast for FY26 is 4.0% versus 4.2% from the MPC, in line with the MPC even as risks related to commodity prices and climate shocks will stay on close watch. MPC revised FY25 growth projection to 6.4% from 6.6% previously even as it projects recovery to 6.7% in FY26. We see downside risk to 6.4% growth forecast for FY25 as it assumes Dec'24 quarter growth above 6.5% while its tracking close to 6% as of now. However, we are still pencilling in FY26 growth at 6.5% from 6-6.2% this year; 7% growth in Q2 FY26 looks optimistic to us in the current global environment.

▪ **Assurance provided on liquidity measures; deferment of LCR implementation is a key positive**

The RBI remains committed to provide sufficient system liquidity and will continue to monitor the evolving liquidity and financial market conditions and proactively take appropriate measures to ensure orderly liquidity conditions. From banking sector perspective, while the NIMs may see some pressure, yet the Governor's assurance on liquidity, providing sufficient time for implementation of regulations (LCR aspired to be implemented from March 31, 2026 now, with delay of one year) is very positive. He has indicated that project finance norms may also come to fruition by 2026. Meanwhile, ECL draft is still awaited.

▪ **RBI maintained its stance on the Rupee**

The current account deficit (CAD) for FY25 is expected to remain well within the sustainable level. As on 31st Jan'25, India's external sector remains resilient as key indicators stay robust. Prior to the policy, the consensus had emerged that in an inflation targeting framework, FX becomes the shock absorber of global volatility. On rupee, the Governor asserted that "our interventions in the forex market focus on smoothening excessive and disruptive volatility rather than targeting any specific exchange rate level or band. The exchange rate of the Indian Rupee is determined by market forces".

▪ **Our view on policy: We maintain view of a shallow rate cut cycle**

Before this meeting, our view was of a shallow 50bps rate cut cycle with 25bps cut already achieved. We see downside risk to 6.4% growth forecast for FY25 as it assumes Dec'24 quarter growth above 6.5% while its tracking close to 6% as of now. Our inflation forecast for FY26 is 4.0%, lower versus 4.2% for MPC even as risks related to commodity prices and climate shocks will stay on close watch. Given the heightened global volatility, we will assess prospects for further rate cut(s) around April.

From an academic perspective, RBI assesses equilibrium real rates at 1.4-1.9%, hence, with the MPC's 4.2% CPI forecast for FY26, repo rate as of now seen settling at 6%, with close watch on inflation risks.

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| Policy Decision | October 2024 | December 2024 | February 2025 |
|-----------------------------|--|--|---|
| Repo rate | 6.50% | 6.50% | 6.25% |
| Stance | Changed to 'Neutral' | Neutral | Neutral |
| Growth Projection | FY25 real GDP projection retained at 7.2%. Q2FY25 growth is projected at 7.0%, 7.4% in Q3FY25 and 7.4% in Q4FY25. Q1FY26 growth is projected at 7.3%. Risks are evenly balanced. | FY25 real GDP projection revised sharply downward to 6.6%, with Q3 and Q4 growth seen at 6.8% and 7.2% respectively. Q1FY26 growth also revised lower to 6.9% from 7.3% and Q2FY26 seen at 7.3%. Risks are evenly balanced as per the MPC. | FY26 real GDP projection at 6.7%, with Q1 at 6.7% (6.9% earlier), Q2 at 7.0% (7.3% earlier), Q3 at 6.5% and Q4 growth seen at 6.5% respectively. Risks are evenly balanced as per the MPC. |
| Inflation Projection | CPI inflation for FY25 projection kept unchanged at 4.5% with Q2 forecast at 4.1%, 4.8% in Q3, and 4.2% in Q4. Q1FY26 CPI growth is projected at 4.3%. Risks are evenly balanced. | CPI inflation for FY25 projection revised upwards to 4.8% with Q3 forecast at 5.7%, and 4.5% in Q4. Q1FY26 CPI growth is projected at 4.6% and Q2FY26 projected at 4.0%. Risks are evenly balanced. | CPI inflation for FY25 projection retained at 4.8% with Q4 at 4.4% (4.5% earlier). FY26 CPI projected at 4.2% with Q1 at 4.5% (4.6% earlier), Q2 at 4.0% (same as earlier), Q3 at 3.8% and Q4 at 4.2%. Risks are evenly balanced. |
| Liquidity | In tune with the changing liquidity conditions, the RBI conducted two-way operations under the LAF to ensure alignment of inter-bank overnight rate with the policy repo rate. The RBI will continue to be nimble and flexible in its liquidity management operations. | (i) CRR of all banks to be cut by 50 bps in two equal tranches of 25 bps each to 4.0% of NDTL with effect from the fortnight beginning 14.12.2024 and 28.12.2024, respectively. (ii) It has been decided to increase the interest rate ceilings on FCNR(B) deposits. | The RBI remains committed to provide sufficient system liquidity. It will continue to monitor the evolving liquidity and financial market conditions and proactively take appropriate measures to ensure orderly liquidity conditions. The RBI also observed that some banks are reluctant to onlend in the uncollateralised call money market. They are passively parking funds with the RBI and hence urged the banks to actively trade among themselves in the uncollateralised call money market to make it deeper and vibrant for better signal extraction from the weighted average call money rate (WACR). |
| Policy guidance | The balance between inflation and growth is well-poised. India's growth story remains intact. Inflation is on a declining path, although we still have a distance to cover. | MPC was balanced in its guidance, and it emphasised that " <i>strong foundations for high growth can be secured only with durable price stability</i> ". The RBI Governor asserted that " <i>at this critical juncture, prudence and practicality demand that we remain careful and sensitive to the dynamically evolving situation with all its complexities and ramifications</i> ". | The MPC gave a balanced guidance as focus on inflation remains to ensure a sustained growth trajectory. However, there was emphasis on risks to growth as global economic backdrop remains challenging and hence need to maintain flexibility with a neutral policy stance. This will provide MPC the flexibility to respond to the evolving macroeconomic environment. |

Other Regulatory Measures Proposed

- Introduction of forward contracts in Government securities to enable further market development.
- Access of SEBI-registered non-bank brokers to NDS-OM: It has been decided that non-bank brokers registered with SEBI can directly access NDS-OM, on behalf of their clients.
- Comprehensive review of trading and settlement timings across various market segments: It has been decided to set up a working group with representation from various stakeholders to undertake a comprehensive review of trading and settlement timing of financial markets regulated by the Reserve Bank.
- Enhancing Trust in the Financial Sector through 'bank.in' and 'fin.in' domains: This initiative aims to reduce cyber security threats and malicious activities like phishing; and, streamline secure financial services, thereby enhancing trust in digital banking and payment services.
- Enabling additional factor of authentication in cross-border card not present (online) transactions. This will provide an additional layer of security in cases where the overseas merchant is enabled for AFA.

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