

Fig 1: Macro projections: headline unchanged, quarterly nos revised

% y/y	GDP		CPI	
	Prior	Post	Prior	Post
Q1 FY25	7.3	7.1	-	-
Q2 FY25	7.2	7.2	3.8	4.4
Q3 FY25	7.3	7.3	4.6	4.7
Q4 FY25	7.2	7.2	4.5	4.3
FY25	7.2	7.2	4.5	4.5
Q1 FY26	-	7.2	-	4.4

Source: RBI, UBI research

### Status quo policy decision on rates, stance and liquidity was in line with our expectations

In line with our expectations, the Monetary Policy Committee (MPC) voted for status quo on repo rate at 6.5% and withdrawal of accommodation policy stance (*Pls refer: "[RBI August MPC decision: Will this be a non-event?](#)"*). This was again a 4:2 decision with dissenters Dr. Varma and Dr. Goyal voting for a 25bps rate cut and change in stance to neutral in their last policy meeting as tenor for the three government nominees ends by Oct'24. More importantly, in line with our expectations, the RBI Governor asserted that they would continue to manage liquidity by use of fine-tuning operations (VRRRs / VRRs) to help align overnight call rate with repo rate, while some sections of the market speculating about liquidity announcements like OMO sale auction calendar etc. Overall, in our view, the RBI Governor while signaling that rates are likely to stay higher for longer, managed market expectations well amid a fragile global and domestic investor backdrop. This indeed was a non-event from FX and bond market perspective.

### MPC sounded hawkish with concerns regarding food inflation pressures

In our view, the most important statement from the Governor was that "*food inflation pressures cannot be ignored as the public at large understands inflation more in terms of food inflation than the other components of headline inflation*". This is a clear assertion that the RBI stays focused on elevated food inflation (above 8% consistently since Nov'23) as it endangers a spillover impact on record low core CPI of c.3%. In fact, in Jan'24, RBI DG Patra released a paper titled, "[Are Food Prices the 'True' Core of India's Inflation?](#)". In our view, food inflation also has a spillover impact on financial stability (*covered in detail below*).

Overall, while the MPC kept FY25 inflation projection unchanged at 4.5% even as Q2 forecast was revised up by 60bps to 4.4% (*Refer Fig 1*). This was a hawkish signal from the MPC which stays focused on lowering the headline CPI inflation towards 4% target.

On the other hand, the commentary on growth continued to assert resilience with FY25 forecast kept unchanged at 7.2% despite downward revision in Q1FY25 growth forecast by 20bps 7.1%. This is likely to provide policy space to delay rate cuts, though global growth trends remain on watch. Interestingly with regards to recent emergence of US recession concerns post release of July'24 jobs print, the RBI Governor ruled out inference of the same based on one month's data (US).

### Financial stability stressed upon in line with our view

The RBI Governor raised concerns that high food inflation warrants attention as it is driving household inflation expectations - as per RBI research study, c.65% of household inflation expectations are explained by petrol/diesel and veggie prices. The latter has led the households to "hunt for yield" and allocate a large part of savings away from bank deposits to asset classes - equity, real estate and gold - all clocking much higher returns in recent years vis-à-vis long-term average. This has driven structural slowdown in low-cost CASA deposits and raising cost of funds for the banking system. There has been a fight for deposits by banks witnessing credit-deposit growth wedge during high growth phase with C-D ratio at record highs and incremental C-D ratio at close to 100% (*Pls refer, [India - Conundrum between C-D Ratio and Real Rates](#)*).

*The RBI Governor, considerate about the "silent depositor" (a phrase he used in recent CNBC interview) advised banks to focus more on mobilisation of household financial savings through innovative products and service offerings and by leveraging fully on their vast branch network. In his view, banks are facing (structural) liquidity management issues and hence taking greater recourse to short-term non-retail deposits (like CDs) and other instruments of liability to meet the incremental credit demand. He is also concerned about credit excesses in some retail loan segments (top-up housing loans, gold loans etc) as flow of funds needs to be carefully tracked.*

### We do not expect rate cuts in FY25, yet closely watching global trends

In the latest policy, the RBI sounded hawkish particularly about the (food) inflation trajectory. Macro projections were kept unchanged at 7.2% and 4.5% for FY25 growth and inflation respectively. Monsoon is in progress, yet the distribution is uneven, hence food inflation needs close watch. The slight upward revision in inflation trajectory in Q2FY25 despite favourable base effects signals caution on inflation. The Governor in press conference asserted that the path to disinflation remains uneven due to large and persistent supply shocks. In the current policy, the RBI has given lot of credence to financial stability while raising concerns about structural issues in liquidity management for the banks amid shift in household savings towards physical assets (real estate, gold) and financial assets except deposits.

*Going forward, we do not expect any rate cuts in this fiscal year while the US Fed is expected to start cutting rates in September, the RBI can wait with relatively stronger growth providing policy space. The risk to our view is from steep rate cuts in US is recession fears are realized and / or sharper than expected fall in domestic food inflation.*

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# Comparison of policy statements (*paraphrased*)

Policy Decision	June 2024 Policy Statement	August 2024 (Our expectation)	August 2024 (Actual)
Repo rate	6.5%	6.5%	6.5%
Stance	Withdrawal of accommodation	Withdrawal of accommodation	Withdrawal of accommodation
Growth Projection	FY25 real GDP projected to be stronger at 7.2% (7.0% earlier). Q1FY25 growth is projected at 7.3% (vs 7.1%), 7.2% (vs 6.9%) in Q2, 7.3% (vs 7.0%) in Q3, and 7.2% (vs 7.0%) in Q4. Risks are evenly balanced.	RBI likely to retain FY25 GDP growth projections. High frequency data signal moderation in Q1FY25 GDP growth numbers.	FY25 real GDP projection retained at 7.2%. Q1FY25 growth revised to 7.1% (7.3% earlier) and kept unchanged for other quarters. Q1FY26 GDP growth projected at 7.2%. Risks are evenly balanced.
Inflation Projection	CPI inflation for FY25 projection kept unchanged at 4.5% with Q1, Q2, Q3 and Q4 forecasts retained at 4.9%, 3.8%, 4.6% and 4.5% respectively. Risks are evenly balanced.	We expect FY25 forecasts to be maintained with a close watch on monsoon and global risks.	CPI inflation for FY25 projection kept unchanged at 4.5% with Q2 forecast at 4.4% (3.8% earlier), 4.7% in Q3 (vs 4.6%), and 4.3% in Q4 (vs 4.5%). Q1FY26 CPI projected at 4.4%. Risks are evenly balanced. <b>Sharp upward revision in Q2FY25 CPI forecast by 60bps to 4.4% signals hawkish guidance.</b>
Liquidity	System liquidity has transited from surplus to deficit conditions, and back to surplus in early June. Going forward, the RBI aims to deploy an appropriate mix of instruments to modulate both frictional and durable liquidity so as to ensure that money market interest rates evolve in an orderly manner and financial stability is maintained.	With RBI recently conducting OMO sales in secondary market totaling c.Rs 10,000cr, there has been growing speculation regarding announcement of liquidity absorption steps like OMO sale auction calendar, FX swaps, CRR among others. However, <b>in our view, the RBI may stick to fine tuning operations (VRRR, VRR, etc.) and closely watch the liquidity dynamics amid macro and market uncertainty.</b> Any macro prudential measures especially for addressing credit excesses (post unsecured credit, NBFC ex HFCs) will be in focus.	System liquidity transited from deficit since the June policy to surplus conditions in July/August. In tune with the changing liquidity conditions, the RBI conducted two-way operations under the LAF to ensure that the inter-bank overnight rate remained closely aligned to the policy repo rate. Going forward, the Reserve Bank will continue to be nimble and flexible in its liquidity management operations. <b>Certain segments of personal loans (like top-up housing loans, gold loans etc) continue to witness high growth.</b> However, regulatory prescriptions relating to loan to value (LTV) ratio, risk weights and monitoring of end use of funds are not being strictly adhered to by certain entities and need close watch.
<b>Regulatory Measures Proposed</b>			
<ul style="list-style-type: none"> <li>➤ To aid the customers in verifying the claim of Digital Lending App's (DLAs) association with regulated entities (REs), RBI is creating a public repository of DLAs deployed by the REs.</li> <li>➤ With a view to provide a more up-to-date picture of a borrower's indebtedness, RBI decided to increase the frequency of reporting to credit information companies (CICs) from monthly intervals to fortnightly basis or at such shorter intervals as mutually agreed between the credit institutions (CIs) and CIC.</li> <li>➤ Limit for tax payments through UPI enhanced from Rs 1 lakh to Rs 5 lakh per transaction.</li> <li>➤ To introduce "Delegated Payments" in UPI which would allow an individual (primary user) to set a UPI transaction limit for another individual (secondary user) on the primary user's bank account.</li> <li>➤ Transition Cheque Truncation System (CTS) from the current approach of batch processing to continuous clearing with 'on-realization-settlement'.</li> </ul>			

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