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RBI TAPS INTO UNCONVENTIONAL TOOLS TO REVIVE GROWTH

EXPERT VIEW

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The Reserve Bank of India (RBI) under the leadership of governor Shaktikanta Das has not ceased to surprise, both with its creativity in using unconventional tools and with the unambiguous nature of its actions. Today's policy fortified that belief. It not only showcased RBI's commitment to support growth through monetary policy and measures to deploy credit to sectors that has multiplier effects on the economy, but it also reinstated its efforts to keep yields anchored by easing financial conditions and taking steps to ensure efficient transmission.

The messaging, while acknowledging the green shoots in the recent economic data, tilted the overall commentary towards supporting growth, even while inflation was acknowledged to be subject to transient supply-side pressures. This was re-established with a strong forward guidance, a first for the MPC, of remaining accommodative for the rest of the fiscal year, and into the next, along with continued provisioning of ample system liquidity.

Second, was the nudge to the bond markets to collaborate with RBI to re-align market expectations to its actions and describing the yield curve as a "public good". Along with a request to the market to bid responsibly in government bond auctions, the policy has also taken some very strong measures to dispel any doubts regarding RBI's commitment to ensuring lower rates. These measures took the shape of a) doubling the size of open market operations (OMO) purchases in each auction to ₹20,000 crore, to ensure lower cut-off yields in the auctions and encourage offers at higher prices; b) extending the recently announced HTM limit hike to March 2022 that will help give confidence to banks to handle higher market risks from deploying higher liquidity in government bonds; c) announcement of OMOs in state development loans (SDLs), which ensures the expanding borrowing programme of states do not lead to a rise in credit spreads. SDLs are a key section of the bond market that, if left unattended, can hinder transmission of lower yields in both G-secs and corporate bonds; d) RBI also re-iterated its commitment to ensure smooth functioning of the borrowing programme.

Third, was to improve credit availability and transmission of rates to lower rated papers. The new on-tap TLTRO scheme will increase liquidity for specific sectors, both via corporate bond markets and lending with the investment classified as HTM along with an exemption from large exposure framework. This along with the other measures may lead to compression in corporate spreads.

Besides, the option provided to banks to reverse the borrowing done under the earlier TLTRO schemes, would assist in reducing the liquidity overhang in the system and provide space for RBI to perform more durable liquidity operations such as OMOs.

> Steps taken will dispel doubts regarding RBI's commitment to keeping rates low for long

Considering the need to provide incremental support to certain segments, additional measures were taken such as revision in limits for risk weights for the retail portfolio, rationalization of risk weights for housing loans, and extension of co-origination of loans to all NBFCs. The measures may assist in reducing cost and improve availability of credit to some sectors.

The moves, come at a time when green shoots are visible in the real economy. While we expect a last rate cut of 25 bps in Q4, we also expect the MPC to use all tools to keep rates low for as long as necessary to revive growth, prodding the real economy towards recovery.

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