Bajaj Finserv Mutual Fund

Note on RBI's Monetary Policy

(February 2024)

The recent deliberations of the Reserve Bank of India's (RBI) Monetary Policy Committee (MPC) held on February 8, 2024, resulted in a decision to maintain the repo rate at 6.5%, marking the sixth consecutive instance of maintaining the status quo. This decision was consistent with market expectations and reflects the RBI's stance amidst prevailing economic conditions. Notably, the MPC's decision was influenced by concerns over inflation persistently surpassing the targeted rate of 4%, necessitating a watchful approach to monetary policy. While some voices within the MPC advocated for rate cuts to address inflation uncertainties, the majority remained focused on maintaining policy stability and predictability.

An interesting observation from the meeting is the competitive forecasting exhibited by the RBI in projecting GDP growth for FY25 at 7%, alongside an anticipated inflation rate of 4.5%. However, it's noteworthy that the RBI refrains from signaling an imminent easing of monetary policy, highlighting the central bank's cautious stance amidst evolving economic dynamics.

In conclusion, the outcome of the recent RBI MPC meeting underscores the importance of stability and resilience within the financial system amidst inflation uncertainties and global economic challenges.

We are anticipating a stable interest rate environment in the near term, influencing bond yields and fixed-income securities. However, the potential impact of inflation on bond yields remains a key consideration, necessitating careful monitoring of economic indicators.

Amidst prevailing uncertainties, investors may adopt a cautious approach in navigating the debt market, considering factors such as liquidity dynamics, foreign flows, and global developments. While the RBI's commitment to financial stability is reassuring, investors should remain vigilant and adjust their strategies to capitalize on emerging opportunities while managing risks effectively.

We believe we may see extended pause in the present phase of the interest rate cycle as RBI may want the impact of the earlier rate hikes to play out fully through the system. The long duration yields is consequently likely to drift downward slowly as the demand-supply interplay in the debt market may become the key determinant of the rate curve for few months. The likelihood of foreign buying may cause gradual yield decline over next few months. Investors can use this period to increase their duration allocation to position favorably for the likely rate cut cycle. Short term investors can look at investing in short-medium duration funds with high quality portfolio to lock-in relatively high prevailing yields while reducing the duration exposure, Money market investors can allocate with around 3 month view before taking an allocation call on the interest rate cycle subsequently.

Data source: RBI

Cause	Effect
RBI Monetary Policy Committee decides to maintain repo rate at 6.5%	Policy stability and predictability maintained; Continuation of status quo observed
Persistent retail inflation above 4% target	Cautious approach to monetary policy; Focus on containing inflation
Forecast of GDP growth for FY25 at 7%, with inflation projected at 4.5%	Potential leeway for government in setting nominal GDP targets and fiscal deficit levels
RBI refrains from signaling imminent easing of monetary policy	Cautious stance amidst evolving economic dynamics
Stable interest rate environment anticipated in near term	Influence on bond yields and fixed-income securities

Data source: RBI