HSBC Mutual Fund

RBI Monetary Policy Update

7 February 2025

MPC Announcement: Going Easy

RBI strikes a balance in its policy given the existing macro-economic conditions and global uncertainties - The Monetary Policy Committee (MPC) came out with their bi-monthly policy statement on February 07, 2025. Some of the key takeaways are as follows:

- The MPC unanimously decided to lower the policy Repo Rate by 25 bps to 6.25% and retain the stance as 'neutral'. Consequently, the SDF rate stands at 6.00% and the MSF rate at 6.50%.
- The neutral stance implies that the MPC deliberately does not want to give any forward guidance on its future course of action.
- The Governor emphasised that the MPC will 'proactively' take liquidity measures both on the overnight and durable liquidity front. However, markets expected additional liquidity measures.
- Governor emphasised on the existing 'flexible inflation targeting framework' and reiterated that the policy remains unambiguously focused on a durable alignment of inflation with the target, while supporting growth.
- While inflation has been revised a shade lower, growth has seen a 20-30bps revision for 1HFY26 from the December policy.
- With inflation cooling from December highs, the RBI-MPC has used the elbow room to lower rates and support growth.

The growth and inflation forecasts have been revised as per the below mentioned table:

	Growth		Inflation	
Period	Dec 2024 forecast	Feb 2025 forecast	Dec 2024 forecast	Feb 2025 forecast
Q4 FY2025	7.20%	-	4.50%	4.40%
FY2025*	**6.60%**	**6.40%**	**4.80%**	**4.80%**
Q1 FY2026	6.90%	6.70%	4.60%	4.50%
Q2 FY2026	7.30%	7.00%	4.00%	4.00%
Q3 FY2026		6.50%		3.80%
Q4 FY2026		6.50%		4.20%
FY2026		**6.70%**		**4.20%**

Note: *GDP First Advance Estimates; Source: RBI MPC Policy Resolutions

The RBI-MPC policy outcome broadly meets market expectations with consensus expecting a 25 bps rate cut with stance as neutral. However, on the liquidity front, the RBI has somewhat disappointed the markets with expectations around OMO purchases or other measures similar to those announced on January 27, 2025 to quench the system liquidity deficit. On the exchange rate, the Governor emphasised that the FX interventions are to smoothen out volatility and does not target any specific level or band.

In his speech, the Governor stated that while strengthening and enhancing the regulatory framework is vital, there are trade-offs between stability and efficiency, and that the RBI will attempt to strike the right balance given that these are not devoid of costs. Much to the relief of the banking system, the Governor confirmed in his presser that LCR and ECL related regulatory changes might not be implemented till March 31, 2026.

Our Take:

The new RBI governor played out a balancing act, by easing rates, while clearly being mindful of the global market volatility and its potential impact on our currency, and hence maintaining a cautious tone. While more on the liquidity front was expected, the remarks from the Governor indicate that the RBI could inject liquidity in the ensuing days, as liquidity conditions are likely to remain tight despite the earlier announced measures. The RBI's "proactive" approach on liquidity suggests that more policy instruments might be deployed as and when required, basis the evolving liquidity conditions.

The neutral stance in some way rules out aggressive policy easing, while also not giving any forward guidance to the market on the future trajectory. We believe the MPC is likely to cut rates by another 25 bps in April 2025 given that risks to growth are on the downside and headline inflation is likely to trend closer to the medium-term target of 4.0%. While we still ascribe a limited probability to a third cut over June / September, it would be completely dependent on the global environment settling down and domestic growth-inflation balance evolving favorably.

While the initial reaction of bond markets has been one of disappointment, with yields inching up by 3-5 bps, we believe interest rates will continue to soften over the next few months. The policy action comes in the milieu of recent liquidity measures which coupled with fiscal consolidation leading to favorable G-Sec supply-demand dynamics (more so with RBI's OMO Purchases), all of which should keep rates benign. Given this backdrop, we continue to maintain a positive duration bias across the funds. We recommend investors to stay invested and add duration to their portfolios wherever possible subject to their risk return frameworks.

Abbreviations:

SDF: Standing Deposit Facility
MSF: Marginal Standing Facility
CRR: Cash Reserve Ratio
OMO: Open Market Operations
GDP: Gross Domestic Product
CPI: Consumer Price Index
G-Sec: Government Securities

Source - RBI, HSBC MF Research, Data as on Feb 7, 2025.

Note: Views provided above are based on information in public domain and subject to change. Investors are requested to consult their financial advisor for any investment decisions.

HSBC Mutual Fund, 9-11th Floor, NESCO - IT Park Bldg. 3, Nesco Complex, Western Express Highway, Goregaon East, Mumbai 400063. Maharashtra.

GST - 27AABCH0007N1ZS | Website: www.assetmanagement.hsbc.co.in