Quick comment on RBI 2nd Quarter Review (October 31, 2012)

A brief snapshot of the main parameters which form part of RBI monetary policy is given in the below which would help in assessing the stance taken by RBI –

Parameter	Position after 2nd Quarter Review	Changes, if any	Remarks
Cash Reserve Ratio (CRR)	4.25%	(-) 0.25%	An infusion of about Rs. 17500 crore additional free funds in the hands of banks. Similar infusion of Rs. 17000 crore was made during the last mid-term review.
Statutory Liquidity ratio (SLR)	23%	Nil	
Repo Rate	8%	Nil	
Reverse Repo Rate	7%	Nil	
Marginal Standing facility	9%	Nil	
Baseline projections for-			
GDP growth rate	5.8%		Reduced from 7.3% (April 2012) & 6.5% (July 2012)
Headline inflation (WPI)	7.5%		Increased from projected annual rate of 6.5% (in April 2012) & 7% (in July 2012)
Growth rate in			
Money Supply (M3)	14%		
Deposits	15%		
Non-food credit (credit for other than agriculture)	16%		

- Further, RBI has required banks to increase the provision for restructured advance from 2% to 2.75%. Analysts feel that this is likely to impact banks' profitability in terms of pre-tax earnings between 3% and 5%. Also it has stipulated that to address the issue of rise in NPAs and restructured advances of banks, and with a view to improving effective information sharing among banks on credit, derivatives and unhedged foreign currency exposures, banks are being advised to put in place, by end-December 2012, an effective mechanism for information sharing. Any sanction of fresh loans/ad-hoc loans/renewal of loans to new or existing borrowers with effect from January 1, 2013 should be made only after obtaining/sharing necessary information.

RBI has noted that over the last quarter, global risks have increased and domestic risks have become accentuated owing to halted investment demand, firmed up global commodity prices, increase in urban and rural wages without commensurate increase in productivity, continuing high current account and fiscal deficits (though there is serious intentions to contain them), moderation in consumption spending and continuing erosion in export competitiveness accompanied by weakening business and consumer confidence. The advance estimates of the

2012 kharif production have projected 10% lower output than during the last year. Given this backdrop and seen in the context of parameters mentioned in the above table, RBI has given more credence to the headline inflation than on the growth. Probably, it is of the opinion that unless supply side corrective measures are undertaken, the effect of monetary policy stance would have a limited impact on the inflation.

The ball is very much in the Governments court, which has to take measures at least to make investments on the infrastructure front, which may trigger a higher sustainable growth and also which may not additionally fuel inflation. The Finance Minister is right in saying that he will have to walk alone, as propelling infrastructure investment is an area in which a large role has to be undertaken by the Government in providing the enabling environment and timely clearances.

If as a result of the GOI efforts or even under the scenario of credit off-take growth rate remaining on expected lines of 16% projected by RBI, RBI may have to infuse additional liquidity by further reduction of CRR. Even now, there is limited room for increasing the interest rates given the low GDP growth rate.

Intent w.r.t. micro and small enterprises: The definition of sickness of micro and small enterprises is being modified to facilitate early rehabilitation of potentially viable sick units and to lay down a procedure for assessing viability of sick units in the sector. The details in this regard are awaited.