



GUINNESS

Redefining Services

RBI Q1 ANNUAL POLICY REVIEW

DATE: 28.07.2009

Highlights of RBI's first-quarter review of FY10 Annual Policy.

KEY MEASURES

- * Repo Rate, Reverse Repo Rate, CRR kept unchanged
- * Bank Rate kept unchanged at 6.0%
- * Keeps FY10 GDP growth outlook at 6% but with upward bias
- * Ups inflation projection to 5% vs 4% April policy
- * Ups FY10 M3 growth projection to 18% vs 17% earlier
- * Ups FY10 deposit growth forecast to 19% vs 18% earlier
- * Keeps credit growth projection at 20% for FY10
- * Second quarter monetary policy review on Oct 27

STANCE

- * To maintain accommodative policy stance until definite signs of recovery
- * Accommodative policy stance not "steady state stance"
- * RBI will have to reverse expansionary steps to curb inflation pressure
- * RBI's stance is to preserve growth momentum
- * RBI stance reversal strategy to be modulated with macro-economic events
- * Stance to keep vigil on trend, signal of inflation
- * To respond to inflation changes via policy adjustments
- * To manage liquidity actively to meet govt credit need
- * To ensure credit flow to private sector at viable rate
- * To keep monetary, rate regime consistent with price stability
- * To keep monetary, rate regime consistent with financial stability
- * Stance is to support economy to return to high growth trajectory
- * Endeavour is to maintain policy stance to accommodate growth
- * To be ready with roadmap for unwinding easy policy
- * To maintain easy policy stance till demand picks up

GROWTH

- * Uptrend in growth momentum unlikely before mid-2009
- * FY10 growth forecast marks slight improvement vs Apr policy
- * Overall macroeconomic scenario stays uncertain
- * Fiscal, monetary stimulus steps to boost demand FY10
- * Domestic, external finance condition more favourable
- * Business outlook positive, signals industry revival
- * Export demand to stay weak on world trade contraction
- * Downside risk to farm growth up on delayed monsoon
- * RBI FY10 GDP forecast reflects absence of global recovery
- * Challenge for econ to return to high growth path
- * India supply constrained, not demand constrained econ
- * Critical to up investment level to accelerate growth
- * Progressive signs of India econ recovery post Apr policy
- * Monsoon delay, high fiscal gap risks to economy
- * Medium term challenge to better investment climate
- * Medium term challenge to expand econ absorptive capacity
- * No econ can sustain high growth without investment rise
- * No econ can sustain high growth without productivity rise
- * Need to up financial inclusion, deepen market for sustained growth
- * Big thrust on govt reforms needed to sustain high growth
- * Fiscal consolidation challenge in immediate-medium term
- * Counter cyclical public spending insulated econ from worst impact of crisis

GOVT BORROWING

- * Abrupt, big rise in govt borrow pushed up ylds, impeded monetary transmission
- * Large govt borrow main reason for high M3 growth FY09
- * Committed to give ample liquidity on continuous basis
- * Govt borrow must not crowd out credit flow to companies
- * Money supply growth "will have to be higher" vs Apr policy



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- * Large, sustained fiscal gap can crowd out private investment
- * Large, sustained fiscal gap can trigger inflation pressure
- * Govt needs to lay down path for fiscal consolidation
- * Path for fiscal consolidation should go beyond mere FRBM target revision
- * Path for fiscal consolidation should detail revenue, spend adjustments
- * Need to focus on quality of fiscal adjustment while pursuing quantitative aim
- * Need to bring gross capital formation to pre-crisis level
- * Gross capital formation fell to 8.2% FY09 vs 12.9% FY08
- * Gilt yield rise militated against RBI low rate regime
- * Private credit demand likely to pick up
- * To manage liquidity to prevent crowding out of private demand
- * OMO buy, MSS unwinding to add 1.5 trln rupees Apr-Sep
- * OMO, MSS unwinding impact Apr-Sep equivalent to 3.5 percentage point CRR cut

INFLATION

- * Negative WPI inflation not contraction of demand
- * Negative WPI inflation not to persist beyond few months
- * Apr policy anticipated negative WPI inflation in Jun
- * CPI inflation stubbornly high, reflect firm food price
- * Uncertain monsoon outlook may accentuate food prices
- * Fall in inflation expectation not matching WPI fall
- * Global commodity prices likely bottomed out
- * Base effect on WPI inflation to wear off fully by Oct
- * Inflation to creep up even in absence of supply shock
- * To ensure price stability, anchor inflation expectation
- * To consider all price indices, components
- * Conduct of policy is to contain inflation perception 4.0-4.5%
- * Medium term objective of inflation at 3.0%
- * Food price rise, weak external demand risks to econ
- * See upside risks to FY10 GDP, inflation projections
- * Comfortable foodgrain stock to mitigate supply risks
- * To closely monitor liquidity to contain inflation expectation
- * Notes rise in food prices potential inflationary risks
- * Notes rise in global commodity prices pose inflationary risks
- * Notes expansionary policies pose potential inflationary risks
- * Challenge to manage short-term liquidity, potential inflation

LIQUIDITY

- * RBI policy step since Sep added actual/potential liquidity of 5.62 trln rupees
- * To maintain policy rates, liquidity to spur private loan demand
- * Permanent SLR cut added 400 bln rupees for credit growth
- * Liquidity expansion in tune with stance to ensure credit growth at viable rate
- * Banks indicated existence of refinance facility provided comfort
- * RBI to keep relying on repo, rev repo, CRR, OMO, SLR, MSS for liquidity mgmt
- * Banks' BPLR cut do not accurately reflect effective lending rates

GLOBAL

- * Seeing positive signs in global finance conditions
- * Global positive signs tentative, weak to hint firm turnaround
- * Real sector still in recession at global level
- * Firm recovery in global econ unlikely before 2010

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