



October 05, 2018

## Monetary Policy Update

---

### Repo Rate Unchanged: 6.5%, Policy Tone Changed to “Calibrated Tightening”

The Reserve Bank of India today decided to maintain the policy repo rate at 6.5% in a 5:1 vote. The MPC changed its stance from neutral to “calibrated tightening” on monetary policy and commitment to achieving a medium-term target for CPI of  $4\% \pm 2\%$ , while supporting growth.

### Key highlights of the RBI’s Monetary Policy

#### Strong Developed Economies, Weak Emerging Economies

Global trade has weakened as seen in export orders and automobile production and sales. The U.S. economy sustained pace in Q3CY18 driven by strong retail sales and robust industrial activity. In the Euro area, economic activity remained subdued due to overall weak economic sentiment, weighed down mainly by political uncertainty. However, emerging economies have overall been facing headwinds from both global and country-specific factors. China IIP growth has moderated with slowing exports and the ongoing deleveraging of the financial system weighing on growth prospects. In Brazil, economic activity is recovering from the setback in Q2, supported by improving business and consumer sentiment, though weak domestic demand and the sluggish pace of recovery in manufacturing activity weigh.

### Domestic Macro Indicators Remain In Focus

Led by real GDP growth surging to a 9-quarter high of 8.2% in Q1FY19 which in turn was spurred by strong GFCF, the domestic economy remains in good shape as seen in good print from IIP and eight core industries in Jul-18 and a rebound in seasonally adjusted capacity utilization to its long term average. Further, PMI as well remained in expansion zone above 50 in Aug-18 and Sep-18.

### Mixed Outlook on Inflation

Retail inflation, fell from 4.9% in Jun-18 to 3.7% in Aug-18, dragged down by a decline in food inflation. Some softening of inflation in items other than food and fuel also contributed to the decline. While the Sep-18 round of the Reserve Bank's survey of households reported a sharp uptick of 50 basis points in three-month ahead inflation expectations over the last round, one-year ahead expectations moderated by 30 basis points. Inflation expectations for both input prices and selling prices of manufacturing firms, polled by the Reserve Bank's industrial outlook survey, firmed up in Q2FY19.

### Systemic Liquidity In Focus

Liquidity in the debt market had been in focus in the recent past which arguably had an impact on equity markets as well. Investors feared underlying cash flow resilience of certain corporates (read Housing Finance companies) in the face of liquidity crunch. Systemic liquidity deficit had surged in the last month and the RBI conducted two open market purchase operations in the second half of September to inject ₹ 200 billion of durable liquidity.

### Market Reaction

- Absence of a rate hike weakened the INR by nearly 0.7% (vs. prior close) to 74.11 at the time of writing as currency markets appeared not to buy the change in tightening stance.
- The benchmark NIFTY50 index closed down -3.2% for the day as markets appeared spooked by the calibrated tightening accompanied with downward revision in real GDP.
- G-Sec yields initially tanked intra-day on the RBI announcement to 8.01% (down ~15bps from intra-day high) but again rebounded shortly thereafter to 8.08% levels (down vs. prior close).

## Outlook

The MPC guided for a **softening of headline inflation** (incl. HRA):

- 4.0% for Q2FY19 (vs. 4.6% for Q2FY19 as at Aug-18) and
- 3.9-4.5% for H2FY19 (vs. 4.8% earlier)
- 4.8% for Q1FY20

However, its trajectory is projected to rise above the Aug-18 print of 3.7% driven by upside risks stemming from MSP increases in agriculture, Crude Oil spikes and risks of fiscal slippage at the Centre and/or States.

While the RBI changed its neutral stance to “calibrated tightening”, this was also accompanied with a marginal toning down of real GDP expectations. The MPC expects:

- 7.4% for Q2FY19 (vs. 7.5% as at Aug-18)
- 7.1-7.3% for H2FY19 (vs. 7.3-7.4% earlier)
- 7.4% for Q1FY20 (vs. 7.5% earlier)

The RBI arguably has made the prudent choice, focusing on the domestic economy and slowing in auto and credit, and stress in the financial sector and the absence of a rate hike can be interpreted that the central bank is not overly concerned about INR depreciation.

# Sanctum Wealth Management

## Investment & Advisory

### Sunil Sharma

Chief Investment Officer & Executive Director

97177 19898,

sunil.sharma@sanctumwealth.com

### Ashish Chaturmohta

Chief Advisor – Technical Strategies

77386 48833

ashish.chaturmohta@sanctumwealth.com

### Viraj Vajratkar

Investment Analyst, Investment Office

98334 95395

viraj.vajratkar@sanctumwealth.com

### Hemang Kapasi

Portfolio Manager

983322 7605

hemang.kapasi@sanctumwealth.com

### Rohit Laungani

Investment Analyst, Investment Office

93241 68860

rohit.laungani@sanctumwealth.com

### Anway Bhujbal

Technical & Derivative Analyst

98702 12498

anway.bhujbal@sanctumwealth.com

## Offices

### Mumbai

**Sanctum Wealth Management Private Limited**

Unit 1501, Tower 2B, One Indiabulls Centre, 841, Jupiter Mills, Off Senapati Bapat Marg, Lower Parel, Mumbai – 400013

Telephone: +91 22 61064800

### Bengaluru

**Sanctum Wealth Management Private Limited**

Unit 1102, 11th Floor, HMG Ambassador, 137, Residency Road, Bengaluru – 560025

Telephone: +91 80 67427900

### Kolkata

**Sanctum Wealth Management Private Limited**

Regus Business Centre Office no. 131, The Legacy, 1st Floor 25-A, Shakespeare Sarani Kolkata – 700017 West Bengal

Telephone: +91 33 44000509

### Delhi

**Sanctum Wealth Management Private Limited**

812 – 816, 8th Floor, Narain Manzil, 23, Barakhamba Road, New Delhi – 110001

Telephone: +91 11 6612 5713

### Chennai

**Sanctum Wealth Management Private Limited**

Level 4, Suite no. 503, Apeejay Business Centre, 39/12, Haddows Road, Nungambakkam, Chennai - 600006

Telephone: +91 44 28224949

### Disclaimer

Different types of investments involve varying degrees of risk, and past performance is not indicative of future results. Do not assume that future performance of any specific investment or investment strategy (including the investments and/or investment strategies recommended or undertaken by us) will be profitable. Results may vary over time and from client to client. Any projections or other information illustrated in this presentation which may have been provided to you regarding the likelihood of various investment outcomes are hypothetical in nature, and do not necessarily reflect actual investment results nor should they be considered guarantees of future results. Historical performance results for investment indices and/or categories have been provided for comparison purposes and index returns may vary substantially from past performance in the future. Other investments not considered in the analysis and the recommendations resulting from this analysis may have characteristics similar or superior to those being analyzed. Please remember to contact Sanctum Wealth Management if there are any changes in your financial situation or investment objectives or if you wish to impose, add or modify any reasonable restrictions to our services.