Monetary Policy Report: RBI

Why in News

The **Reserve Bank of India (RBI)** has released the **Monetary Policy Report** (MPR) for the month of August 2021.

> It kept the **policy rate unchanged for the seventh time in a row**. And **appealed to the centre and states to reduce taxes** on fuels to curb inflationary pressures.

Monetary Policy Report

- The MPR is published by the **Monetary Policy Committee (MPC) of RBI.**
- The MPC is a statutory and institutionalized framework under the **RBI Act, 1934, for maintaining price stability, while keeping in mind the objective of growth.**
- The MPC **determines the policy interest rate** (repo rate) required to achieve the **inflation target of 4% with a leeway of 2% points on either side.**
- The **Governor of RBI is ex-officio Chairman** of the MPC.

Key Points

- **Unchanged Policy Rates:**
  - **Repo Rate** - 4%.
  - **Reverse Repo Rate** - 3.35%.
  - **Marginal Standing Facility (MSF)** - 4.25%.
  - Bank Rate- 4.25%.
- **GDP Projection:**

  Real **Gross Domestic Product (GDP)** growth for 2021-22 has been retained at 9.5%.
- **Inflation:.**

  RBI has revised the projection for **Consumer Price Index (CPI)** inflation to 5.7% from 5.1%.

- **Variable Rate Reverse Repos:**
  - In order to absorb additional liquidity in the system, the RBI announced conducting a **Variable Rate Reverse Repo (VRRR)** program due to the higher **yield prospects as compared to the fixed rate overnight reverse repo.**
    - The RBI has decided to **increase the quantum under the VRRR to Rs 4 trillion in a phased manner.**
  - It also **extended the liquidity support to banks** to lend to stressed businesses by another three months to 31th December 2021.
- **Interest Rates:**
  - Elevated inflation level and delayed recovery in the economy has prompted the panel to keep rates steady. **Interest rates in the banking system are expected to remain stable** in the next couple of months.
    - Recovery faced rough weather due to the **Covid second** wave and lockdowns in states
- **Accommodative Stance:**
  - It decided to continue with an **accommodative stance** as long as necessary to revive and sustain growth on a durable basis and continue to mitigate the impact of **Covid-19** on the economy, while **ensuring that inflation remains within the target going forward.**
    - An accommodative stance means a **central bank will cut rates to inject money into the financial system** whenever needed.
- **Optimism For Recovery:**
  - **Resilient Demand:**
    - After the **second wave** of infections, domestic economic activity had started to recover with accelerated **vaccination**.
  - **Economic Package:**
    - Although investment demand is still anaemic, improving capacity utilisation, rising steel consumption, higher imports of capital goods, congenial monetary and financial conditions and the **economic packages announced by the central government** are expected to kick-start a long-awaited revival.
  - **High Frequency Indicators:**
    - High-frequency indicators (electricity consumption, nighttime lights intensity and nitrogen dioxide emissions) suggest that **consumption** (both private and Government), **investment and external demand are all on the path of regaining traction.**
- **Concerns:**
  - Inflation management can pose a **serious challenge when the elevated fuel price pass through starts** to occur and thus inflation shock is unlikely to be transitory even by definition.

- **Suggestions:**
  - **Reduce Taxes:**
    With crude oil prices at elevated levels, a calibrated **reduction of the indirect tax component of pump prices by the centre and states can help** to substantially lessen cost pressures.
  - **Economic Stimulus:**
    On the economic front, despite the uptick, **it is important that a stimulus is provided by the government to give a thrust to consumption**. The timing of such measures will be apt at this juncture as the festive season is about to begin.
  - **Policy Use:**
    The **nascent and hesitant recovery in the economy needs** to be nurtured through **fiscal, monetary and sectoral policy levers.**

Key Terms

- **Repo and Reverse Repo Rate:**
  - Repo rate is the rate at which the c**entral bank of a country** (Reserve Bank of India in case of India) **lends money to commercial banks in the event of any shortfall of funds**. Here, the central bank purchases the security.
  - Reverse repo rate is the rate at which the **RBI borrows money from commercial banks within the country.**
- **Bank Rate:**
  It is the rate charged by the RBI **for lending funds to commercial banks.**
- **Marginal Standing Facility (MSF):**
  - MSF is a window for scheduled banks **to borrow overnight from the RBI in an emergency situation when interbank liquidity dries up completely.**
  - Under interbank lending, banks lend funds to one another for a specified term.
- **Inflation:**
  - Inflation refers to the rise in the prices of most goods and services of daily or **common use, such as food, clothing, housing, recreation, transport, consumer staples, etc.**
  - Inflation measures **the average price change in a basket of commodities and services** over time.
  - Inflation is indicative **of the decrease in the purchasing power of a unit of a country's** currency. This could ultimately lead to a deceleration in economic growth.
- **Consumer Price Index:**
  - It measures price changes **from the perspective of a retail buyer.** It is released by the **National Statistical Office (NSO)**.
  - The CPI calculates the difference in **the price of commodities and services such as food, medical care, education, electronics etc, which Indian consumers buy for use.**

Source: IE