Mizuho Flash: RBI

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RBI Hold: Of Inflection & Deflection

Central Bank Policy Outlook

Country	Central Bank	2021				2022				2023	
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
US	**Fed**	0.00-0.25%	0.00-0.25%	0.00-0.25%	0.00-0.25%	0.25-0.50%	1.00-1.25%	1.25-1.50%	1.50-1.75%	1.75-2.00%	1.75-1.2.00%
India	**RBI**	4.00%	4.00%	4.00%	4.00%	4.00%	4.25%	4.75%	5.00%	5.00%	5.00%

"Your path you must decide" – **Master Yoda, Star Wars**

- The **RBI** attempted a **Goldilocks policy compromise** *for the moment;* by *maintaining sufficient accommodation to reassure on downside risks to growth* but whilst *gently initiating a measured removal of accommodation* (via tweaks to the rate corridor floor) to restrain excessive inflation risks.

- Specifically, the RBI's **headline policy (repo rate) rate on hold** at 4.00%, **deflects worries of unnecessarily premature headwinds from policy tightening** by **reinforcing the accommodative policy stance**.

- ***Yet,*** **by supplementing the repo rate hold with the introduction of standing facility rate** of 3.75%, **to supplant** the reverse repo rate (3.35%) as the liquidity adjustment facility (LAF) **rate corridor floor**, the RBI has engineered **a sufficiently convincing signal of policy inflection**.

- In addition, the **upward revisions to inflation** to 5.7% for FY22-23 (from 4.5%) will **help to deflect criticism about the RBI being negligently too sanguine on inflation risks**, and the by inference, the **RBI's commitment to price stability** (inflation targeting) objectives.

- **For now though**, it appears that the **RBI has deflected pre-commitment rate hike cycle**, **conditioning the requisite tightening on geo-political outcomes**, which it has cited as the predominant driver of global price shocks and attendant inflation risks. This is reasonable.

- But that said, clearly, **an aggressively hawkish Fed may deny** the RBI with the **benefit of responding purely to growth-inflation dynamics** borne out of ebbing COVID and evolving geo-politics. Instead aggressive rate hikes and global USD liquidity drainage by the Fed **may impose a sharper RBI policy inflection** that takes its cues **from attendant macro-stability and capital (out-)flow risks**.

- As such, we maintain our call for a cumulative 100bps of hikes by end-2022 (or early-2023) as the cost of economic headwinds from higher rates are likely to be more than offset by the benefits of ensuring that inflation expectations are not unmoored nor are macro- and rupee stability compromised.

- Afterall, the latter could give rise to far larger and more enduring demand destruction from balance sheet shocks. And it is **far better to inflect policy sooner to deflect such risks**. *The RBI appears to have decided on its path* (of growth without endangering stability) with the transition to policy inflection.

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