

Why we expect India to cut rates again this week

The balance of risk is tilted towards one more 25 basis point policy rate cut by the Reserve Bank of India this week. This would probably mark the end of the current easing cycle



Reserve Bank of India
Governor Shaktikanta
Das

3.75%

RBI policy rate forecast

25bp cut this week

Loose consensus for an RBI rate cut

The Reserve Bank of India's Monetary Policy Committee is meeting on Thursday, 6 August, to decide the course of the policy. The consensus is skewed towards a further 25 basis point cut to key policy rates; at the time of this writing, 18 out of 29 estimates in the Bloomberg survey favoured a rate cut and the rest no change.

We also think we'll get a 25bp rate cut, bringing the RBI repurchase rate down to 3.75% and the reverse repo rate to 3.10%. These will be marked to be a record low for both rates, after eight cuts

in the repo rate and nine in the reverse repo rate in the current easing cycle that has been underway since early 2019.

We also share the consensus view that the central bank will leave commercial banks' cash reserve ratio unchanged at 3.00%. Nor do we anticipate any change to the accommodative policy bias as growth outweighs inflation as the policy driver. That said, we think we are near the end of this easing cycle.

Nose-diving economy warrants lower rates

The monetary easing expectations stem from prospects of a prolonged economic slump ahead resulting from an un-abating spread of the Covid-19 pandemic. India is the third worst-affected country in the world (after the USA and Brazil) with total infections poised to cross the two-million mark in the coming days.

Clearly, the April-June quarter, the first quarter of the fiscal year 2020-21, recorded its worst economic performance, probably in the living memory. We forecast close to 12% year-on-year GDP contraction in that quarter; the data is due on 31 August.

Supporting this, exports crashed by 37% YoY and imports were worse with a 53% plunge. These dented manufacturing sharply. The statistical office refrained from publishing the industrial production data recently, but the output of key infrastructure sectors (coal, crude oil, natural gas, petroleum products, fertilisers, steel, cement, and electricity) shrank 25% YoY in April-June, suggesting that the headline IP couldn't be any better than this.

The deteriorating fiscal situation also suggests action

Further reinforcing the need for more monetary accommodation are the deteriorating public finances as these are constraining the scope for any more fiscal stimulus.

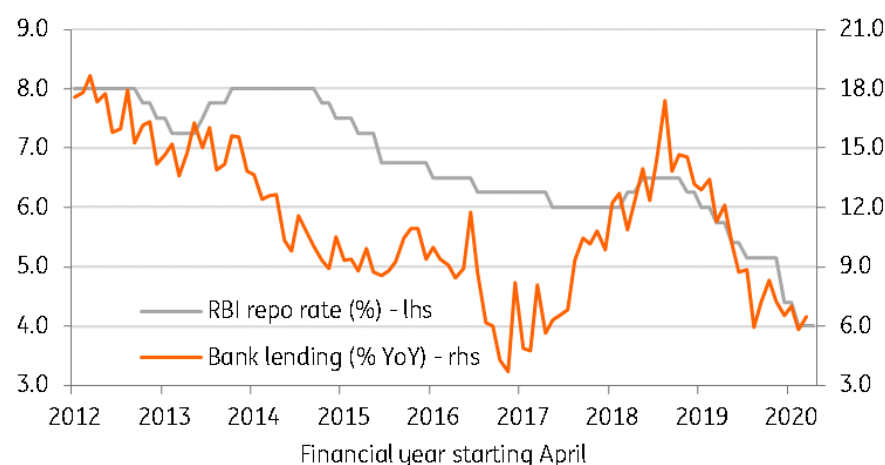
The fiscal deficit is through the roof

The contracting economy has dented government revenue, while stimulatory policy has boosted spending, shooting the fiscal deficit through the roof. The deficit in 1Q FY20-21 surged 53% YoY to INR 6.62 trillion and this was 83% of the official target for the entire fiscal year. This stems from a 47% YoY fall in revenue and a 13% rise in expenditure. Our view of the deficit equivalent to 6.5% of GDP this fiscal year remains at risk of an upside miss.

Record government borrowing to plug the budget gap is another reason why interest rates should fall further to ease the debt servicing burden. Despite aggressive RBI rate cuts so far this year the 10-year government bond yield has been sticky downward, at around 5.8% currently.

Meanwhile, the noise about monetisation of the deficit with direct purchases of government bonds by the central bank has been prevalent. This is despite the RBI dashing such hopes in an [off-cycle policy announcement in April](#), while some of its former policymakers continued to warn against this policy option, calling it as highly inflationary.

Aggressive monetary easing is still failing to stimulate lending



Source: CEIC, ING

Headwinds to lower rates

Talking about inflation, it has risen above the RBI's 2-6% policy range in recent months. Supply disruption and panic buying brought food prices back in play as the key inflation driver. And a recent hike in excise duty and retail fuel prices have pressured utilities and transport costs. We expect inflation to remain above or near the RBI's policy limit for the remainder of the year.

While high inflation explains why some favour a stable rate decision this week, another argument supporting it is a weak currency. The INR has been an underperforming emerging market currency this year with about 5% year-to-date depreciation. Although it gained some ground recently on the back of broad US dollar weakness and one-off inflows in India's telecom sector, we see nothing on the horizon to help it erase underperformance in the rest of the year.

Our end-2020 USD/INR forecast remains at 76.50 (spot 75.05).

Author

Amrita Naik Nimbalkar

Junior Economist, Global Macro

amrita.naik.nimbalkar@ing.com

Mateusz Sutowicz

Senior Economist, Poland

mateusz.sutowicz@ing.pl

Alissa Lefebvre

Economist

alissa.lefebvre@ing.com

Deepali Bhargava

Regional Head of Research, Asia-Pacific

Deepali.Bhargava@ing.com

Ruben Dewitte

Economist

+32495364780

ruben.dewitte@ing.com

Kinga Havasi

Economic research trainee

kinga.havasi@ing.com

Marten van Garderen

Consumer Economist, Netherlands

marten.van.garderen@ing.com

David Havrlant

Chief Economist, Czech Republic

420 770 321 486

david.havrlant@ing.com

Sander Burgers

Senior Economist, Dutch Housing

sander.burgers@ing.com

Lynn Song

Chief Economist, Greater China

lynn.song@asia.ing.com

Michiel Tukker

Senior European Rates Strategist

michiel.tukker@ing.com

Michal Rubaszek

Senior Economist, Poland

michal.rubaszek@ing.pl

This is a test author

Stefan Posea

Economist, Romania

tiberiu-stefan.posea@ing.com

Marine Leleux

Sector Strategist, Financials

marine.leleux2@ing.com

Jesse Norcross

Senior Sector Strategist, Real Estate

jesse.norcross@ing.com

Teise Stellema

Research Assistant, Energy Transition

teise.stellema@ing.com

Diederik Stadig

Sector Economist, TMT & Healthcare

diederik.stadig@ing.com

Diogo Gouveia

Sector Economist

diogo.duarte.vieira.de.gouveia@ing.com

Marine Leleux

Sector Strategist, Financials

marine.leleux2@ing.com

Ewa Manthey

Commodities Strategist

ewa.manthey@ing.com

ING Analysts

James Wilson

EM Sovereign Strategist

James.wilson@ing.com

Sophie Smith

Digital Editor

sophie.smith@ing.com

Frantisek Taborsky

EMEA FX & FI Strategist

frantisek.taborsky@ing.com

Adam Antoniak

Senior Economist, Poland

adam.antoniak@ing.pl

Min Joo Kang

Senior Economist, South Korea and Japan

min.joo.kang@asia.ing.com

Coco Zhang

ESG Research

coco.zhang@ing.com

Jan Frederik Slijkerman

Senior Sector Strategist, TMT
jan.frederik.slijkerman@ing.com

Katinka Jongkind
Senior Economist, Services and Leisure
Katinka.Jongkind@ing.com

Marina Le Blanc
Sector Strategist, Financials
Marina.Le.Blanc@ing.com

Samuel Abettan
Junior Economist
samuel.abettan@ing.com

Franziska Biehl
Senior Economist, Germany
Franziska.Marie.Biehl@ing.de

Rebecca Byrne
Senior Editor and Supervisory Analyst
rebecca.byrne@ing.com

Mirjam Bani
Sector Economist, Commercial Real Estate & Public Sector (Netherlands)
mirjam.bani@ing.com

Timothy Rahill
Credit Strategist
timothy.rahill@ing.com

Leszek Kasek
Senior Economist, Poland
leszek.kasek@ing.pl

Oleksiy Soroka, CFA
Senior High Yield Credit Strategist
oleksiy.soroka@ing.com

Antoine Bouvet
Head of European Rates Strategy
antoine.bouvet@ing.com

Jeroen van den Broek
Global Head of Sector Research
jeroen.van.den.broek@ing.com

Edse Dantuma

Senior Sector Economist, Industry and Healthcare
edse.dantuma@ing.com

Francesco Pesole
FX Strategist
francesco.pesole@ing.com

Rico Luman
Senior Sector Economist, Transport and Logistics
Rico.Luman@ing.com

Jurjen Witteveen
Sector Economist
jurjen.witteveen@ing.com

Dmitry Dolgin
Chief Economist, CIS
dmitry.dolgin@ing.de

Nicholas Mapa
Senior Economist, Philippines
nicholas.antonio.mapa@asia.ing.com

Egor Fedorov
Senior Credit Analyst
egor.fedorov@ing.com

Sebastian Franke
Consumer Economist
sebastian.franke@ing.de

Gerben Hieminga
Senior Sector Economist, Energy
gerben.hieminga@ing.com

Nadège Tillier
Head of Corporates Sector Strategy
nadege.tillier@ing.com

Charlotte de Montpellier
Senior Economist, France and Switzerland
charlotte.de.montpellier@ing.com

Laura Straeter
Behavioural Scientist
+31(0)611172684
laura.Straeter@ing.com

Valentin Tataru

Chief Economist, Romania

valentin.tataru@ing.com

James Smith

Developed Markets Economist, UK

james.smith@ing.com

Suvi Platerink Kosonen

Senior Sector Strategist, Financials

suvi.platerink-kosonen@ing.com

Thijs Geijer

Senior Sector Economist, Food & Agri

thijs.geijer@ing.com

Maurice van Sante

Senior Economist Construction & Team Lead Sectors

maurice.van.sante@ing.com

Marcel Klok

Senior Economist, Netherlands

marcel.klok@ing.com

Piotr Poplawski

Senior Economist, Poland

piotr.poplawski@ing.pl

Paolo Pizzoli

Senior Economist, Italy, Greece

paolo.pizzoli@ing.com

Marieke Blom

Chief Economist and Global Head of Research

marieke.blom@ing.com

Raoul Leering

Senior Macro Economist

raoul.leering@ing.com

Maarten Leen

Head of Global IFRS9 ME Scenarios

maarten.leen@ing.com

Maureen Schuller

Head of Financials Sector Strategy

Maureen.Schuller@ing.com

Warren Patterson

Head of Commodities Strategy

Warren.Patterson@asia.ing.com

Rafal Benecki

Chief Economist, Poland

rafal.benecki@ing.pl

Philippe Ledent

Senior Economist, Belgium, Luxembourg

philippe.ledent@ing.com

Peter Virovacz

Senior Economist, Hungary

peter.virovacz@ing.com

Inga Fechner

Senior Economist, Germany, Global Trade

inga.fechner@ing.de

Dimitry Fleming

Senior Data Analyst, Netherlands

Dimitry.Fleming@ing.com

Ciprian Dascalu

Chief Economist, Romania

+40 31 406 8990

ciprian.dascalu@ing.com

Muhammet Mercan

Chief Economist, Turkey

muhammet.mercan@ingbank.com.tr

Iris Pang

Chief Economist, Greater China

iris.pang@asia.ing.com

Sophie Freeman

Writer, Group Research

+44 20 7767 6209

Sophie.Freeman@uk.ing.com

Padhraic Garvey, CFA

Regional Head of Research, Americas

padhraic.garvey@ing.com

James Knightley

Chief International Economist, US

james.knightley@ing.com

Tim Condon

Asia Chief Economist
+65 6232-6020

Martin van Vliet

Senior Interest Rate Strategist
+31 20 563 8801
martin.van.vliet@ing.com

Karol Pogorzelski

Senior Economist, Poland
Karol.Pogorzelski@ing.pl

Carsten Brzeski

Global Head of Macro
carsten.brzeski@ing.de

Viraj Patel

Foreign Exchange Strategist
+44 20 7767 6405
viraj.patel@ing.com

Owen Thomas

Global Head of Editorial Content
+44 (0) 207 767 5331
owen.thomas@ing.com

Bert Colijn

Chief Economist, Netherlands
bert.colijn@ing.com

Peter Vanden Houte

Chief Economist, Belgium, Luxembourg, Eurozone
peter.vandenhoute@ing.com

Benjamin Schroeder

Senior Rates Strategist
benjamin.schroeder@ing.com

Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE
chris.turner@ing.com

Gustavo Rangel

Chief Economist, LATAM
+1 646 424 6464

gustavo.rangel@ing.com

Carlo Cocuzzo

Economist, Digital Finance

+44 20 7767 5306

carlo.cocuzzo@ing.com