

RBI cut its key policy rates i.e., Repo rate & MSF rate by 75 bps to 4.40% and 4.65%, respectively while Reverse Repo rate was cut by 90 bps to 4%. RBI refrained from its usual growth inflation projections but upped its near term (Q4FY20) inflation estimate by 30 bps and noted broadly easing factors ahead. On growth concerns over fallout of Covid-19 was expressed while noting the benefit of oil price and favourable policies. The decision was voted in favour of by a majority of 4-2. Along with this RBI unleashed significant liquidity boosting measures in the form of TLTRO, CRR and MSF with an object to inject a total liquidity of INR 3.74 tn to the system. Significant regulatory dispensation was granted to tide over the stress in financial market, lending institutions, corporates and borrowers as highlighted below.

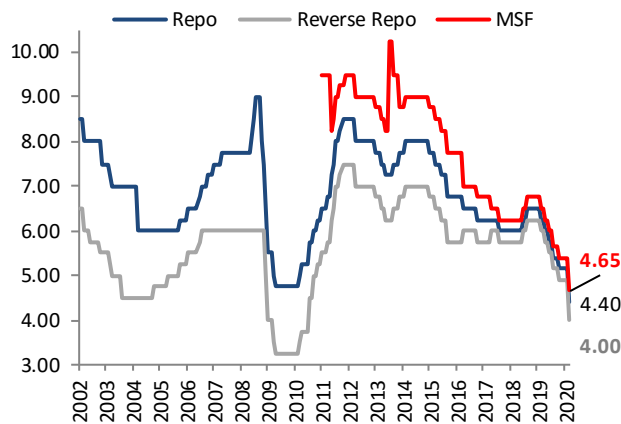
- i) **Targeted Long Term Repos Operations (TLTROs):** RBI will conduct auctions of targeted term repos of up to three years tenor of appropriate sizes for a total amount of up to ₹ 1,00,000 crore at a floating rate linked to the policy repo rate. Liquidity availed under the scheme by banks has to be deployed in investment grade corporate bonds, commercial paper, and non-convertible debentures over and above the outstanding level of their investments in these bonds as on March 27, 2020. Banks shall be required to acquire up to fifty per cent of their incremental holdings of eligible instruments from primary market issuances and the remaining **fifty per cent from the secondary market, including from mutual funds and non-banking finance companies.**
- ii) **CRR:** RBI reduced the cash reserve ratio (CRR) of all banks by 100 basis points to 3.0 per cent of net demand and time liabilities (NDTL) with effect from the reporting fortnight beginning March 28, 2020 for one year – lowest CRR ever. This reduction in the CRR would release primary liquidity of about INR 1.37 tn. This liquidity support is on top of LAF of the order of INR 2.86 tn on a daily average basis during March 1-25, 2020. Importantly, the requirement of minimum daily CRR balance maintenance has been reduced from 90 per cent to 80 per cent.
- iii) **Marginal Standing Facility:** Banks allowed to dip into their SLR holding upto 3% (from existing 2%) for the purpose of availing MSF upto end-June 2020. to avail an additional ₹ 1,37,000 crore of liquidity under the LAF window in times of stress.
- iv) **Monetary Policy Rate Corridor:** RBI decided to widen the existing policy rate corridor from 50 bps to 65 bps.
- v) **Moratorium on Term Loans:** All financial institutions under the purview of RBI were permitted to allow a moratorium of three months on payment of instalments in respect of all term loans outstanding as on March 1, 2020. Accordingly, the repayment schedule and all subsequent due dates, as also the tenor for such loans, may be shifted across the board by three months.
- vi) **Deferment and ease of Interest on Working Capital Facilities:** lending institutions are being permitted to allow a deferment of three months on payment of interest in respect of all such facilities outstanding as on March 1, 2020. The accumulated interest for the period will be paid after the expiry of the deferment period. In respect of working capital facilities sanctioned in the form of cash credit/overdraft, lending institutions may recalculate drawing power by reducing margins and/or by reassessing the working capital cycle for the borrowers.
- vii) **Deferment of Implementation of Net Stable Funding Ratio (NSFR):** RBI decided to further defer the implementation of the last tranche of 0.625 per cent of the CCB from March 31, 2020 to September 30, 2020.
- viii) **Offshore NDF Rupee Market:** Banks which operate International Financial Services Centre (IFSC) Banking Units (IBUs) to participate in the NDF market with effect from June 1, 2020. Banks may participate through their branches in India, their foreign branches or through their IBUs.

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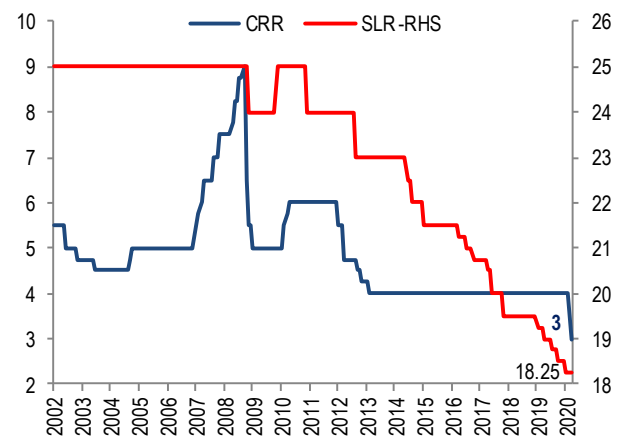
## RBI effects sizable cut in rates coupled with influx of liquidity

Exhibit 1: RBI cuts Repo/MSF rate by 75 bps and Reverse Repo by 90 bps



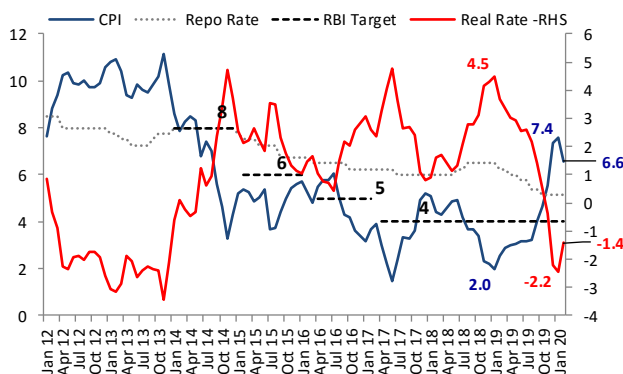
Source: RBI, ASKWA Research

Exhibit 2: CRR is cut down to lowest ever rate of 3% while SLR too stands at its historical low



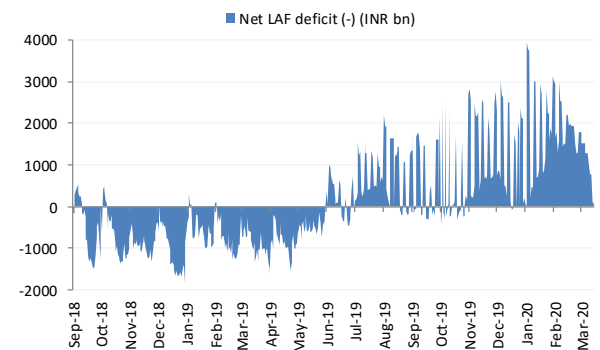
## Real rates to plunge further negative temporarily while record LAF support continues

Exhibit 3: Real rates plunge temporarily



Source: CMIE, RBI, ASKWA Research

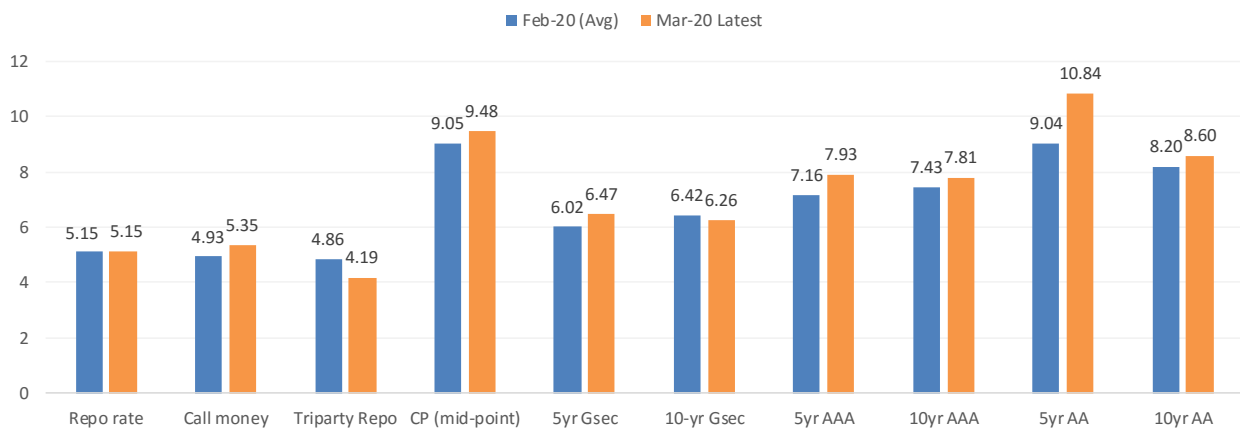
Exhibit 4: Huge liquidity support continues



Source: CMIE, RBI, ASKWA Research

## Was important for RBI to de-clog the liquidity freeze to effect transmission of both rates and liquidity

Exhibit 5: Various segments of money and Gsec shows temporary stress recently



Source: CMIE, RBI, ASKWA Research

## Implication and outlook:

RBI has delivered on most counts to tackle the economic fall out of Covid-19. Its not the nuclear options (yet) – like monetization of fiscal deficits, but it's a big Daisy Cutter. The fact that it effected an out of turn (unscheduled MPC meeting) and out of size (given recent benchmarks) of 75-90 bps, serves as a very strong signaling of its resolve to see interest rate structure down. In the near term this would ensure financial stability while in the medium term acting on top of a much smoothened transmission channel, it would reduce the rates once economic activities picks up in the post Covid-19 episode. Perhaps a stronger resolve of RBI can be deciphered from its carefully articulated stance “to continue with the accommodative stance **as long as it is necessary to revive growth and mitigate the impact of coronavirus (COVID-19) on the economy**, while ensuring that inflation remains within the target.” This serves as a guidance that not only the rate environment is likely to stay benign for long period, deeper rate cuts, extension of the liquidity and regulatory dispensation may well continue beyond their initially announced terminal date or even be deepened.

- Liquidity infusion via CRR/MSF and rate lowers rates as well as ease liquidity issues for banks.
- The over-sized cut in Reverse-repo (90 bps) over Repo (75 bps) disincentivizes lazy banking and forces banks to lend rather than lay off surplus liquidity with RBI.
- Loan moratorium partially offsets near-term challenges to asset quality.
- Banks are a straight beneficiary – of both liquidity and forbearance, as well as explicit commitment by the Governor that depositors' “money is safe”.
- TLTRO makes AAA-rated NBFCs and corporate access cheaper funding.
- Monetary transmission is expected to be fast, with a sharp drop expected in incremental corporate (and retail) borrowings.
- ***Market volatility should substantially ease, money market yields have already fallen 300 bps, and G-Secs across the yield curve would show softening bias.***

The sum-total of the measures taken above gives further fillip to our duration call of May 2019. We now revise our 10yr Gsec forward guidance to 5.50% to 6.50% (from 6 to 7.25% earlier). ***Fixed income strategy should continue to be geared towards benefiting from duration strategies focused on government securities and AAA papers and focused on in the 3-5 year maturity bucket and locking in yields across highest rated instruments at the short end of the curve.***

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