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## Status quo continues

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The outcome of the Monetary Policy Committee's (MPC) second bi-monthly policy review meeting was along expected lines, with the majority of the members voting for a status quo. However, the voting pattern on both the policy rates and the stance changed to 4:2 from 5:1 in the previous meeting, with Dr. Ashima Goyal incrementally changing her position in favour of a 25 bps rate cut and a change in the policy stance to neutral. This too was not entirely surprising, given her comments in the minutes of the last two MPC meetings.

Following the higher-than-expected growth prints for FY2024, the MPC has slightly tweaked its GDP growth projections for FY2025. It has raised its quarterly growth projections for FY2025 by 20-30 bps vis-à-vis the last policy, with the new projections centred on a very narrow range around the annual estimate of 7.2%. This is mildly higher than the forecast of 7.0% that was issued in the April 2024 meeting.

We are circumspect about the pace of the GDP expansion in H1 FY2025; ICRA forecasts the GDP growth to print below 6.5% in this period, dampened by transient factors such as the impact of the elections on activity in certain sectors. However, we expect it to improve to above 7.0% in H2 FY2025, aided by back-ended Government capex, a likely pick-up in private capex, improved rural demand if the monsoon turns out to be favourable, and some improvement in export growth. Consequently, ICRA expects the GDP growth to moderate to 6.8% in FY2025 from 8.2% in FY2024, lower than the MPC's forecast of 7.2% for the fiscal. The extent of the slowdown in the gross value added (GVA) growth would be relatively milder, as the wedge between the growth in GDP and GVA narrows in FY2025 vis-à-vis FY2024. Given this, we believe that the disclosure of the MPC's GVA forecasts would be quite helpful.

Interestingly, the RBI has highlighted that investment activity is likely to remain on track, with high-capacity utilisation (CU), healthy balance sheets of banks and corporates, the Government's continued thrust on infrastructure spending, and optimism in business sentiments. While we concur with this assessment, we believe that the sustenance of domestic demand amid global headwinds would impact the CU over the next couple of quarters and influence the pace of incremental capacity addition announcements through H1 FY2025. In ICRA's view, private sector capex is under way in a modest degree across various sectors, ranging from traditional ones such as cement and steel to new age sectors such as data centres and electric vehicles. Going forward, we expect the private sector capex cycle to remain measured and realistic, and unlikely to be excessively exuberant over the next few years.

On the inflation front, the MPC has left its quarterly and annual forecasts for the CPI inflation unchanged compared to the April 2024 meeting. It has reiterated the upside risks and uncertainty around the food inflation trajectory owing to adverse weather events. We expect the CPI inflation to average at 4.6%, marginally higher than the MPC's forecast of 4.5%, amid a softening in food inflation through the fiscal assuming a normal and well-distributed monsoon, even as the core inflation print is likely to see a mild uptick during the year.

The progress of the monsoon was uneven in June 2024, with cumulative rainfall at the all-India level lagging the normal by 11% during the month. Moreover, the spatial distribution was uneven, with a surplus rainfall in South Peninsula and deficient rains in the other three regions amid ongoing heatwaves. This is likely to have impacted the sowing of kharif crops. Considering that typically 75% of overall sowing gets completed by the end of July, a normal volume of rainfall over the critical sowing states in the coming weeks is crucial to facilitate the ramping up of sowing.

Overall, our assessment of growth-inflation dynamics and outlook, and the MPC's continued focus on aligning inflation to the 4.0% target on a durable basis suggest that the Committee is unlikely to change the stance and rates until there is greater clarity on the turnout of the monsoons, its impact on kharif output and the trajectory of food inflation. Consequently, ICRA foresees the earliest possible rate cut only in the December 2024 meeting.

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