

APRIL 20, 2017
UPDATE
BSE-30: 29,422

MPC minutes: Hint of contrasting views. The April 5-6 policy meeting minutes reiterated MPC's concerns on upside risk to inflation. While the sticky behavior of core inflation and possible mean reversion of food inflation remain key concerns, most committee members remain watchful of second round impact of 7CPC HRA increases.

There were two strong and contrasting views on inflation. On one hand, Dr Patra sounded extremely hawkish on inflation risks and even called for a preemptive 25 bps rate hike to avoid the need for back-loaded policy action later. On the other hand, Dr Dholakia sounded dovish as he deviated significantly from the RBI's inflation forecast and noted comfortable inflation dynamics (including core) through FY2018 (Exhibit 1).

While we expect ~50 bps of downside to RBI's March 2018 estimate of 5%, headline inflation is likely to remain higher than the medium-term target of 4%. Further, sticky core inflation leaves limited scope for further easing with growth expected to improve marginally. We maintain our call for a status quo on rates in FY2018.

Exhibit 1: Summary of MPC members' views and policy decision

Member	Rationale for action	Stance / Vote
Dr Urjit R. Patel	(1) Upside inflation risk emanating from 7CPC led HRA increases, GST rollout, sticky core inflation and geopolitics led crude prices increases (2) Outlook for inflation calls for close vigilance (3) Investment activity continues to be weak, despite some improvement to overall growth outlook (4) There is still room for banks to cut lending rates	Neutral to Hawkish / no change
Dr Viral Acharya	(1) Risks are evenly balanced around the inflation outlook; economic recovery underway amid structural constraints (2) Amid balanced risks, policy focus should be on resolving banks' balance sheet problem, mopping surplus liquidity, enhancing liquidity in the corporate bond market	Neutral / no change
Dr Michael D. Patra	(1) Core inflation remains sticky; upside in food coming from more sinister articles; inflation expectations hardened (2) Second round impact of 7CPC led HRA increase may be material on inflation; GST impact on inflation transient (3) Upside risks from possible increase in administered prices, El Nino effect on food prices, imported inflation, global inflation and consequent policy adjustments. (4) a pre-emptive 25 bps hike in policy rate now will point better at the target of 4% and obviate the need for back-loaded policy action later	Hawkish / no change
Dr Chetan Ghate	(1) Sticky core inflation adding upside risk to 4% target; output gap, while marginally negative, is closing; food inflation likely to reverse (2) 7CPC led HRA increase poses risk to 4% inflation target (3) Need to watch for any possible global market disruption due to tightening of Fed's balance sheet	Neutral to Hawkish / no change
Dr Pami Dua	(1) Modest softening of inflation and inflation expectations, (2) Narrowing output gap, implementation of 7th CPC led HRA increases, GST rollout, El Nino risks, higher global commodity prices, exchange rate volatility and increasing inflationary expectations warrant a cautious watch on inflation	Neutral to hawkish / no change
Dr Ravindra Dholakia	(1) Core inflation likely to show a decline; pass through from non-core to core inflation is weakening (2) Upside risks to inflation particularly arising out of the award of the 7CPC may not be as high as 1-1.5% in FY2018 (3) GST impact on inflation likely minimal; El Nino event may not impact prices much (4) Inflation to average 4% in 1HFY18 and 4.5% in 2HFY18	Dovish / no change

Notes:

- (a) Stance is our interpretation of the members' views in the minutes.
(b) Emphasis in text is our addition.

Source: RBI, Kotak Economic Research

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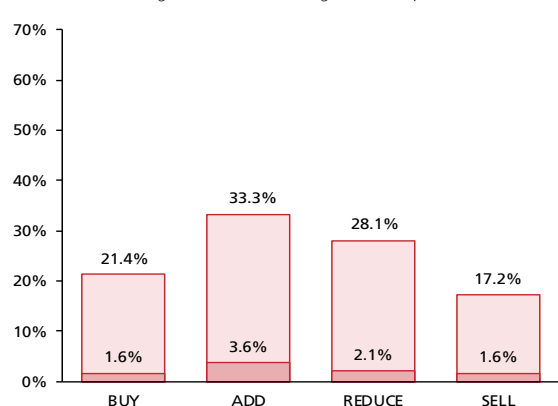
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Source: Kotak Institutional Equities

As of March 31, 2017

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