

THIRD QUARTER REVIEW OF ANNUAL MONETARY POLICY FOR THE FISCAL YEAR 2007-08.

On 29th January 2008, Dr. Y.V.Reddy, Governor, Reserve Bank of India, presented the **third quarter review of annual monetary policy for the fiscal year 2007-08**. The Review consists of three main sections:

1. Assessment of macroeconomic and monetary developments,
2. Stance of monetary policy and
3. Monetary measures.

Highlights of the monetary policy are:

- Unlike the earlier policies, this time the **RBI has adopted a steady policy**. Both the Policy Rates (Bank Rate, Repo Rate and Reverse Repo Rate) and Reserve Ratios (Cash Reserve Ratio and Statutory Reserve Ratio) **have remained unchanged** from the last policy. This was contrary to the overall market expectations.

Rates	Percentage
(I) Policy Rates	
Bank Rate	6.00
Repo Rate	7.75
Reverse Repo Rate	6.00
(II) Reserve Ratio	
Cash Reserve Ratio	7.50
Statutory Reserve Ratio	25.00

- The current policy has been formulated basically to achieve the twin objectives of sustaining the current economic **growth momentum of 8.5%** and also containing **inflation close to 5.00%** in the current fiscal year.
- In the wake of inflation control, liquidity management, gets priority in the monetary policy. The policy recognizes the fact that there is excess liquidity in the system, with money supply (M3) registering a growth of 23.0% as against the

target of 17.0 to 17.5%. The RBI is also concerned about the likely hike in global fuel and food prices.

- Quality of credit and credit delivery for employment-intensive sectors are given due emphasis while pursuing the financial inclusion goal.
- The policy reiterates the need to keep a tab on the rising global uncertainties and domestic situation which could impinge on inflation expectations, financial stability and growth.

Immediate reaction to the credit policy has not been very encouraging. On BSE, the Sensex closed at 18,090 – down by 60 points or -0.34%. However, the decline in bank stocks was much sharper as indicated by 3.5% fall in Bankex to 11,120.

What lies ahead?

The **neutral stand of the RBI in the current credit policy** can not be sustained for too long particularly in the context of the recent US FED rate cuts. On 22nd January 2008, Federal Reserve reduced its FED Fund rate by 75 basis points from 4.25% to 3.50%. This has been the sharpest rate cut by FED in the last 23 years.

Declining FED rate and the stable rates in India have resulted in a widening gap between the Indian and the US interest rates. The FED has also indicated that further rate cuts are not ruled out in the near future. In the likely event of this happening, the gap would be further increased. This will cause an inflow of funds into the economy. On the other hand such inflows can add to the money supply and adversely affect the inflation scenario in India.
