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RBI monetary policy: How it impacts your finances

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The much awaited RBI bi-monthly policy was announced on 5 April 2016. This time the RBI has cut the repo rates by 0.25% to 6.5%. RBI also took multiple measures to infuse more liquidity into the Indian monetary system. With these measures, the RBI is also focusing on the transmission of lower interest rates into the economy.

So let us understand what does this do to your personal finances?

Your loans:

• One of the concerns of RBI was that even though there have been rate cuts since Jan 2015, the same has not been transmitted by the banks to loans. As a result, loan rates have not gone down by the same level as the RBI rate cuts.
• RBI has introduced a new method of calculation of loan rates which has come into effect from 1 April 2016 called the Marginal Cost based Lending Rate (MCLR). This newly introduced MCLR calculation will mean that new loans should be available at lower rates. This means borrowers could look to refinance existing home loans at a lower rate. Auto loans and other loans could also become cheaper.

Your fixed income/debt investments:

• Bank FDs and corporate FD rates are expected to go down. This means that if an investor is renewing FDs that are maturing now, he may get to renew them at lower rates of interest. Hence investors could look at locking in to FDs for a higher tenure if suitable to their investment horizon, tax bracket and liquidity needs, to benefit from the rates available today. With the recent reduction in small savings rates and popular investment instruments like PPF and Post Office MIS, and a reset every quarter, quick action with respect to your fixed income instruments is recommended.
• RBI has mentioned that it is taking an accommodative stand on the monetary policy, which means there could be a further chance of rate cuts going forward and/ or greater liquidity infusion. This could mean that if you have investments in short term bond funds and accrual funds, these could possibly give you some capital appreciation in addition to the current yield, therefore becoming an attractive investment opportunity.
• The further rate cuts by the RBI will depend on domestic factors such as inflation, the monsoon and the seventh pay commission impact as well as global factors such as actions by US and China as regards their monetary policies. The consensus view is there may be further reduction in yields on deposits and bonds. Thus, an investment portfolio using a mix of accrual, dynamic bond funds and tax free bonds could be considered if you are an investor in a higher tax bracket.

Your equity investments:

• As interest rates reduce, for most corporates it could mean lower cost of borrowing and lower input costs. This could help improve earnings and bottomlines for companies, and thus this should boost the equity markets, though it may take a while before we see that effect.

Some of the other announced measures were:

• Payments - With respect to payments and settlement systems in India RBI will publish by end of April 2016 its Vision 2018 in order to move to less cash and a more digital society. Expect cash transactions to reduce and greater efficiency in how you pay for products and services, as well as invest.
• Easier market access to gilt account holders: The custodians will be required to provide all gilt account holders and foreign portfolio investors (FPI) access to online platform to enable them to trade directly. Detailed guidelines in this regard will be issued by June end 2016.
• Allowing NRIs to participate in Exchange Traded Currency Derivatives up to a certain limit and conditions stipulated by SEBI: Detailed guidelines in this regard by RBI in consultation with SEBI will be issued by end of June 2016.
• Broadening market participation: Introduction of electronic trading platform to broaden participation in Over the Counter (OTC) derivatives. The framework will also cover forex platforms to facilitate hedging by small and retail customers. The draft framework will be put on website for wider feedback by the end September 2016.

Overall investors can expect a lot of action in the money, debt and forex markets going forward by the measures being announced.

Shalini is a member of The Financial Planners' Guild , India (FPGI). FPGI is an association of Practicing Certified

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