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RESERVE BANK OF INDIA

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# RBI Bulletin – February 2023

Today, the Reserve Bank released the February 2023 issue of its monthly Bulletin. The Bulletin includes Monetary Policy Statement February 6-8, 2023, one speech, six articles and current statistics.

The six articles are: I. State of the Economy; II. A Recalibrated Quarterly Projection Model (QPM 2.0) for India; III. Union Budget 2023-24 - An Assessment; IV. ESG Disclosures and Performances: Cross-Country Evidence; V. Bankers' Sentiments on Credit Demand – Post Pandemic Recovery; and VI. The Long Shadow of Federal Reserve's Actions: Monetary Policy and Uncertainty Spillovers to India.

## I. State of the Economy

The year 2023 will probably be characterised by a milder global slowdown than earlier anticipated but the trajectory remains unpredictable. In India, domestic consumption and investment stand to benefit from stronger prospects for agricultural and allied activities, strengthening business and consumer confidence, and strong credit growth. Supply responses and cost conditions are poised to improve even though inflation witnessed a rebound in January. The Union Budget 2023-24's emphasis on capital expenditure is expected to crowd-in private investment, strengthen job creation and demand, and raise India's potential growth.

## II. A Recalibrated Quarterly Projection Model (QPM 2.0) for India

*By Joice John, Deepak Kumar, Asish Thomas George, Pratik Mitra, Muneesh Kapur and Michael Debabrata Patra*

This article presents the details of the updated quarterly projection model for India. The article revisits the model structure and coefficients with more India-centric characteristics to enrich its performance and relevance. It generates medium-term projections of inflation and growth, and undertakes policy analysis consistent with achieving targets/mandate set under the flexible inflation targeting (FIT) framework. The revised and updated model is dubbed as QPM 2.0. This project was carried out under UTKARSH 2022, the medium-term strategy of the RBI.

**Highlights:**

i) The major enhancements brought about in QPM 2.0 are inclusion of (i) fiscal-monetary policy interaction in the model, (ii) a more nuanced modelling of India-specific fuel pricing, (iii) capital flows, exchange rate dynamics and central bank's forex market interventions.

ii) For major macro variables like inflation, the analysis shows that the forecast performance of QPM 2.0 is better than alternate time series models for the medium-term horizon (5-8 quarters) – the horizon that matters most for the monetary policy decision.

iii) QPM 2.0 analysis also shows that the FIT framework helped in anchoring inflation expectations post introduction of FIT, leading to lower headline inflation as well as core inflation. The disinflation during this period was also supported by favourable shocks emanating from the supply side, both food and fuel, as well as from a prudent fiscal policy. In the post-COVID period, persistent supply chain disruptions and sustained input cost pressures, amidst a negative output gap have led to inflationary pressures.

## III. Union Budget 2023-24 - An Assessment

*By Saksham Sood, Ipsita Padhi, Anoop K. Suresh, Bichitrananda Seth and Samir Ranjan Behera*

This article presents an assessment of the Union Budget 2023-24. The Budget envisages capex as the key lever of growth while committing to credible fiscal consolidation for strengthening macro-stability.

**Highlights:**

i) In 2023-24, the gross fiscal deficit is budgeted to consolidate to 5.9 per cent of GDP from 6.4 per cent of GDP in 2022-23 (RE).

ii) Capital expenditure is budgeted to increase to 3.3 per cent of GDP in 2023-24 from an average of 1.7 per cent during 2010-20, while revenue expenditure growth has been capped at 1.2 per cent.

iii) On the receipts side, gross tax revenue is budgeted to increase by 10.4 per cent, with a budgeted buoyancy of 0.99 that is close to the trend level.

iv) Prudent fiscal management has contributed to a moderation in the public debt.

## IV. ESG Disclosures and Performances: Cross-Country Evidence

*By Saurabh Ghosh and Siddhartha Nath*

Policy makers across the globe are increasingly paying attention to the integration of “Environmental, Social and Governance (ESG)” principles into their regulatory frameworks. In the post-COVID era, credible disclosure has become a pre-requisite for integrated risk management framework. In this context, this article looks at the resilience of ESG leaders using cross-country MSCI-ESG Leaders’ Indices *vis-à-vis* broader market indices since 2010.

**Highlights:**

i) The ESG Indices generally outperformed the broader market indices in the sample period, both in terms of returns, and mitigation of risks measured by volatility clustering.

ii) The ESG indices withstood the unanticipated shock of COVID-19 better than the broad market indices as evinced by estimates derived from difference-in-difference and market models.

iii) India ranks high among the sample countries when a ranking score of the countries is generated in terms of the ESG indices' performances using the market model framework.

## V. Bankers' Sentiments on Credit Demand – Post Pandemic Recovery

*By Haridwar Yadav and Supriya Majumdar*

The Bank Lending Surveys (BLS) are used by major central banks to capture perceptions of banks on credit conditions and their outlook for the near term across major sectors which act as a lead indicator. This article looks at the evolution of sentiments of the scheduled commercial banks (SCBs) in India during the pandemic as captured through the quarterly BLS. It also looks at how expectations reacted to economic recovery and credit demand, based on outlook indicators incorporated in the survey.

**Highlights:**

i) Bankers' sentiments on lending in terms of assessment of credit conditions quickly improved after the adverse reaction witnessed during April-June 2020 and April-June 2021 due to the first and the second wave of the pandemic, respectively. The outlook on credit conditions continued to remain upbeat across the pandemic period.

ii) The rebound in assessment was faster in the case of retail/personal loans. These were the sectors for which outlook was severely hit during both the waves of the pandemic.

iii) Bankers' sentiments broadly corroborated the trends observed in the borrowers' perceptions captured in the Industrial Outlook Survey (IOS) indicating that both supply and demand for credit had a similar outlook.

iv) More recent data indicate that bankers' sentiments continue to remain optimistic for credit demand in the ensuing quarters.

## VI. The Long Shadow of Federal Reserve's Actions: Monetary Policy and Uncertainty Spillovers to India

*By Bhanu Pratap and Thangzason Sonna*

Cross-border transmission of economic shocks arising from changes in the macroeconomic policy stance in major advanced economies has emerged as a key challenge for emerging market economies in today's world with complex trade and financial linkages. This article analyses the impact of monetary policy actions of the US Federal Reserve on the Indian economy over the last two decades.

**Highlights:**

i) In line with international evidence, changes in the monetary policy stance of the US Federal Reserve tend to impact the Indian economy, altering domestic output and inflation.

ii) Changes in the US monetary policy worked like a cost-push shock in the pre-2008 period, consistent with the exchange rate channel of global spillovers. In the post-2008 period, however, the transmission of US monetary policy shocks has been mainly through the financial channel, *i.e.*, by altering the financial conditions, thereby impacting growth and inflation in India.

iii) Heightened uncertainty around the stance and actions of the US Federal Reserve is estimated to reduce aggregate demand in the Indian economy.

The views expressed in the Bulletin articles are of the authors and do not represent the views of the Reserve Bank of India.

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