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RBI MEASURES TO MAINTAIN LIQUIDITY: WE NEED TO BE BATTLE READY

The RBI Governor, Shaktikanta Das, announced fresh measures aimed at maintaining adequate liquidity in the system, facilitating and incentivising banks to ensure better credit flow and enabling normal functioning of the financial markets. Amongst other measures, the RBI Governor reduced the reverse repo rate by 25 basis points to 3.75 per cent. The rate cut was warranted due to the disruptive force of coronavirus.

The reduction of reverse repo rate by 25 basis points will enable banks to open up the credit flow for economic activities, instead of deploying funds with the central bank. This will boost investor confidence and the quarterly numbers will no longer be a horror story.

The repo rate is the rate at which the central bank lends money to commercial banks in the event of any shortfall of funds. Monetary authorities use this to control money supply in the economy and monitor inflation. A reverse repo rate is the rate at which RBI borrows funds from commercial banks.

The measures announced by RBI today are aimed at softening the impact of the pandemic Covid-19 on the financial markets. The aim is to bring in growth and improve economic development in the country. By reducing the repo rate and thereby bringing down the lending rate, consumers may borrow more from banks thus stabilising inflation. This also means that banks can now borrow money from RBI at a lower interest rate.

A cut in the repo rate usually leads to a decline in the interest rates on loans offered by various banks. It reduces interest rates and brings down the overall cost of a loan, which may be personal loans, car loans, home loans and thereby boosting consumption and propelling the economy.

The RBI's openness to provide further relief if the situation further worsens is a big relief in these distressed times.

-Sangeeta Lakhi, senior partner, Rajani Associates