

Banking System Liquidity Slips into Deficit, MPC Meet Likely to Focus on Infusing Cash

A deficit for first time in over 3 years on advance tax payments high govt cash balances

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Mumbai: Banking system liquidity slid to a deficit for the first time in over three years, squeezed by advance tax payments and ballooning government cash balances. The net liquidity injection was Rs 21,873.43 crore on Tuesday, bucking the trend of a surplus for the first time since May 2019, according to Reserve Bank of India (RBI) data compiled by India Ratings. Net surplus liquidity in the banking system was at Rs 8.03 lakh crore about a year ago.

This triggered speculation that the central bank may have to detail its liquidity management policy in the forthcoming monetary policy, pushing aside the commentary on interest rate increases, suggesting a possible shift in stance.

“Deficit banking system, though fric-



tional, validates shift in policy strategy from accommodative to tight,” said Soumyajit Niyogi, director at India Ratings. “This will enable the MPC (monetary policy committee) to shift the policy stance to neutral from accommodative.”

Following a review of liquidity conditions, the RBI decided Wednesday to conduct an overnight variable rate repo (VRR) auction on Thursday to infuse cash into the banking system. ET had reported September 19 that the RBI was likely to hold a repo auction. The central bank will announce the monetary policy on September 30.

“The RBI is likely to focus on longer-term variable rate repos to ease systemic liquidity with a lower likelihood of a reversal of the recent CRR (cash reserve ratio) hike,” said Aditi Nayar, chief economist at ICRA Ratings. “Some guidance on liquidity is likely to accompany the monetary policy outcome next week. While frictional stress related to tax outflows would ease going ahead, we are awaiting the data on durable liquidity to gauge whether that too has dropped.”