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OPINION

Predictions 2022: Demand spike from metals, power, chemicals, and engg

The RBI would be moving from an accommodative to neutral stance, which will be in harmony with the rate hikes, predicts Sanjiv Chadha of Bank of Baroda.

By **SANJIV CHADHA**, Dec 29, 2021
3 min read

Credit growth is expected to accelerate this year with all the segments showing buoyancy, says Sanjiv Chadha.

Any prognosis of the future must be based on a heroic assumption that the pandemic is behind us and even in case there is another wave, lockdowns will not be the answer. Without this assumption it will be hard to make a calculated guess as lockdowns can push back business significantly.

So how will things look for the banking sector under these assumptions? The last two years have been unique for the financial sector. The focus was on keeping the system solvent and the Reserve Bank of India (RBI) along with the banking system had a large role to play. The central [...] es like liquidity

support, moratorium, relaxation in regulatory norms and so on. Banks played their role by ensuring that the policies of the RBI, like the TLTRO, were implemented. In this setting, the core banking functions of deposit garnering and lending took a different shape. All this will change in 2022.

First is the action of the RBI. Now it seems more than likely that the central bank will increase rates. The minutes of the monetary policy committee (MPC) buttress this thought quite forcefully. We can expect 25-50 bps increase in the repo rate with the first hike in April. Also, there would be a tendency for the reverse repo rate to go back to the band of 25 bps below the repo rate, with the first step being taken in February.

Second, the tone of the RBI would be moving from an accommodative to neutral stance, which will be in harmony with the rate hikes. It should be mentioned here that the accommodative stance was to be interpreted as being one where there would be no immediate rate hike.

Third, the system will have to be drained of surplus liquidity and this would be the biggest challenge for the RBI. Presently the market is jumping the gun in getting nervous over the 3VR or any surprise term reverse repo auction. Reverse repo auctions, as often reiterated by RBI governor, are voluntary and only offer a choice to banks to park their surplus funds for a longer duration and earn a higher return. It is not like an OMO where the funds are taken out of the system as they return to the banks post the expiry of the term. Therefore, at some time a decision must be taken to remove these excess funds through OMOs or any other innovative instrument depending on the demand for credit. The mirror image here is that the GSAPs and TLTRO like measures will remain at the periphery of the framework but could always be used in times of tightness of liquidity.

Fourth, we do expect credit growth to accelerate this year with all the segments showing buoyancy. Banks are now comfortable with their portfolio and its stratification as the challenges posed by AQR have been addressed and the willingness-to-lend quotient has increased. Typically, we may expect higher demand from industries like metals, power, chemicals, and engineering.

Fifth, while we have still seen the dominance of cash in our daily lives, the migration to the digital mode will be significant with all banks working on the same. Talks are on for a central bank digital currency, which though an idea today would get cemented during the year. What this really means is an alternative experience being provided for customers. Alongside, one can also see the greater use of AI in credit evaluation which will add a new dimensic

Last, for banks, a hard look at their balance sheets will be called for. Higher rates would mean reworking margins. This will affect valuation of investment portfolio too and hence the gains on that end would be recalibrated. Growth of deposits is what bankers take for granted but stock markets, mutual funds and cryptos have provided competition as households weigh options. Therefore, demand for credit would increase and liquidity tighten.

These are possibilities that will keep bankers working during the day and thinking harder at night.

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