

RBI Holds Rates, Signals 'Lower for Longer' Bias with Focus on Policy Transmission



- The RBI's Monetary Policy Committee (MPC) voted unanimously to keep policy rates unchanged, with the policy repo rate at 5.25%. It retained a neutral policy stance to preserve policy flexibility amid an evolving macroeconomic environment.
- The decision reflects benign underlying inflation pressures and a resilient growth outlook, supported by domestic demand and potential tailwinds from trade agreements. Upcoming changes in the CPI and GDP series also support a pause at the February meeting.
- The RBI marginally revised inflation projections higher by 10-20 bps, raising FY26 CPI inflation to 2.1% and Q1 and Q2 FY27 estimates to 4.0% and 4.2% respectively, while deferring full-year FY27 projections to the April meeting pending the release of the new CPI series.
- Real GDP growth for FY26 is estimated at 7.4% (First Advance Estimates), while the RBI slightly raised H1 FY27 growth projections by 20 bps to 6.9%–7.0%, reflecting sustained domestic demand, Union Budget FY27 measures, and potential trade-related tailwinds.
- On liquidity management, the RBI reiterated its focus on improving policy transmission and proactively managing liquidity, even as it announced no new liquidity measures at this meeting.
- The RBI announced a range of regulatory and developmental measures to strengthen customer protection, improve credit flows to MSMEs, support real estate financing, enhance the ease of doing business for NBFCs, and deepen financial markets.
- In terms of the policy rate outlook, the Governor signalled a "lower for longer" bias, indicating that "*policy rates should continue to be at low levels for a long period of time*", with any further action contingent on evolving macroeconomic conditions.
- In our view, the RBI is likely to remain on an extended pause, with rate action unlikely unless growth weakens materially or macroeconomic conditions deteriorate; policy calibration for FY27 will be reassessed after the release of the new CPI and GDP data series.

Pramod Chowdhary

Chief Economist
pramod.chowdhary1@dmifinance.in

Bhawna Sachdeva

Economist
bhawna.sachdeva@dmifinance.in

Shantanu Sharma

Economist
shantanu.sharma@dmifinance.in



www.dmifinance.in



+91 11 4120 4444



DMI Finance Private Limited

Express Building, 9-10, 3rd Floor,
Bahadur Shah Zafar Marg,
Delhi – 110002.

RBI Leaves Policy Rates Unchanged, Indicates Rates to Remain at Low Levels for a Long Period of Time

The RBI's Monetary Policy Committee (MPC) unanimously voted to keep policy rates unchanged. Consequently, the policy repo rate remains at 5.25%, the Standing Deposit Facility (SDF) rate at 5.00%, while the Marginal Standing Facility (MSF) rate and the Bank Rate remain at 5.50%. **It also retained a neutral policy stance** to preserve policy flexibility amid an evolving macroeconomic environment.

The RBI's decision to maintain the status quo on rates was driven by multiple factors. **First**, despite a modest uptick in the RBI's inflation forecasts for H1-FY27, largely due to elevated precious metal prices, underlying inflation pressures are assessed to remain relatively low. **Second**, the economic growth outlook remains resilient, underpinned by strong domestic demand and is likely to be further supported by the successful conclusion of the EU-India FTA and a prospective US-India trade agreement. This is reflected in a slight upward revision to real GDP growth forecasts for H1-FY27. **Last**, as noted earlier, the MPC was expected to await the new CPI and GDP series to better calibrate its future reaction function; any policy change at this stage would therefore be premature. In this context, the RBI has deferred the release of full-year FY27 projections until the April policy meeting.

The policy statement indicated that **future policy actions will be data-dependent**, including assessments based on the new CPI and GDP series scheduled for release in February. **However, the RBI Governor, in the press conference, noted that the MPC voted to retain a neutral policy stance, implying that "given the state of the economy that is today and that we foresee over the next 9-12 months, this is the rate we expect to be there."** He further added that the economy is in a good spot, characterised by a Goldilocks environment and low underlying inflation, both currently and in the forecast. Accordingly, **the Governor expects that "policy rates should continue to be at low levels for a long period of time,"** and that any further reduction in rates will be determined by the MPC going forward, based on evolving macroeconomic conditions. **In our view, the RBI is expected to remain on an extended pause, unless growth outcomes surprise materially on the downside or the macroeconomic outlook deteriorates meaningfully.** Policy calibration for FY27 will be reassessed after the release of the new GDP and CPI inflation series in February 2026, both of which could influence the RBI's reaction function and forward guidance.

In liquidity management, the RBI will continue to focus on improving policy transmission and will proactively use the

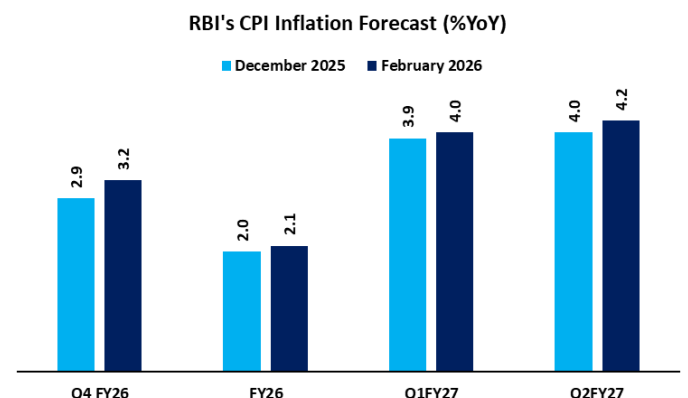
tools at its disposal. While the Governor did not announce any new liquidity measures, he reiterated that the RBI will pre-emptively manage evolving liquidity conditions. The absence of any fresh liquidity-related announcements likely disappointed markets, with the 10-year G-sec yield rising by around 9 bps from the previous close to 6.74% at today's closing. In our view, additional liquidity measures remain likely, particularly in light of seasonal liquidity pressures in Q4 and extending into FY27, given the government's large borrowing programme.

RBI Tweaks Inflation and Growth Projections; FY27 Estimates Deferred to the Next Meeting

The RBI tweaked its inflation projections modestly, while deferring the release of full-year FY27 projections to the meeting in April, in view of the impending revision to the CPI base and other technical changes.

The RBI raised its CPI inflation projection for FY26 to 2.1%, up from 2.0%, with Q4 FY26 inflation projected at 3.2%, bringing its inflation outlook closer to our forecasts of 2.1% for FY26 and around 3.0% for Q4 FY26. The RBI also nudged its inflation projections for Q1 FY27 and Q2 FY27 slightly higher to 4.0% and 4.2%, respectively, from 3.9% and 4.0% earlier, largely driven by elevated precious metal prices. Excluding this latter factor, underlying inflationary pressures remain muted. The food price outlook remains particularly favourable, supported by healthy kharif production, strong rabi sowing, and adequate reservoir levels. We presently expect CPI inflation to average 4.0%–4.5% in FY27, although this assessment will be revisited once the new CPI series is released.

Inflation Projections Increased Slightly for Q4 FY26 – Q2 FY27



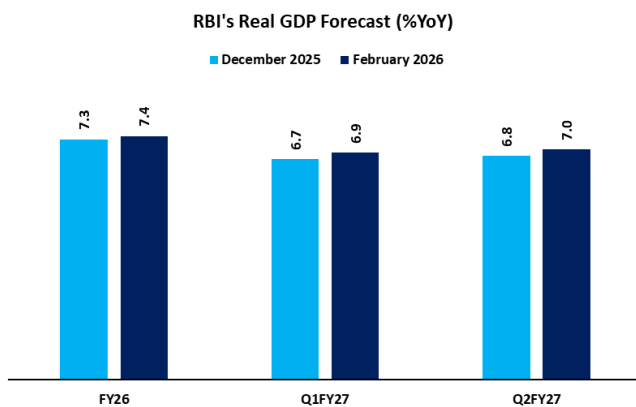
Source: RBI; Note: December 2025 and February 2026 refer to projections given by the RBI in its December 2025 and February 2026 MPC updates, respectively

The RBI noted that FY26 real GDP growth is estimated at 7.4% in the First Advance Estimates (FAE), marginally higher than the RBI's projection of 7.3% in the previous meeting and in line with our estimate. The RBI expects positive growth momentum to persist into FY27, with growth

forecasts for Q1 FY27 and Q2 FY27 revised upward to 6.9% and 7.0%, respectively, from 6.7% and 6.8% earlier. The upward revisions to H1 FY27 projections reflect continued momentum in domestic demand, measures announced in the Union Budget FY27, and tailwinds from ongoing trade developments, including the recently concluded India–EU free trade agreement (FTA) and the prospective India–US trade deal.

Nonetheless, the global geopolitical environment remains a key risk to monitor. Domestically, growth is expected to be supported by steady rural demand driven by a strong agricultural sector, improving urban consumption aided by GST cuts and monetary easing, and a gradual recovery in private investment. While we do not see material downside risks to the RBI's current projections, we will reassess the outlook once the new GDP series is released later this month.

Growth Projection for H1-FY27 Raised by 20 bps



Source: RBI; Note: December 2025 and February 2026 refer to projections given by the RBI in its December 2025 and February 2026 MPC updates, respectively. FY26 7.4% estimate is as per First Advance Estimates (FAE) released by MoSPI.

RBI to Manage Liquidity Conditions Proactively

On liquidity management, the RBI emphasised that it remains focused on ensuring effective policy transmission across money markets and bond markets. While no fresh liquidity measures were announced, the RBI reiterated its readiness to take proactive steps as warranted.

Systemic liquidity remained tight and volatile through December and January, with average surplus liquidity at Rs 0.7 lakh crore and Rs 0.6 lakh crore, respectively. These pressures largely reflected the RBI's foreign exchange interventions, which effectively neutralised a significant portion of the rupee liquidity injected through Open Market Operations (OMOs), dollar–rupee buy–sell swaps, and the CRR cut.

Since the December policy meeting, the RBI has announced durable liquidity infusions totalling Rs 6.3 lakh crore, including a Rs 50,000 crore injection scheduled for next

week. In the first week of February, liquidity conditions improved, with average surplus liquidity rising to around Rs 2.2 lakh crore. Nevertheless, with seasonal liquidity needs expected to increase in Q4, we anticipate the RBI to deploy a combination of measures, including OMOs, dollar–rupee buy–sell swaps, and longer-tenor Variable Rate Repos (VRRs).

RBI Assess the External Sector as Resilient and Confident of Meeting External Financing Requirements Comfortably

The RBI noted that India's external sector remains resilient and is confident it can comfortably meet the country's external financing requirements. Despite global uncertainty weighing on merchandise exports, the robust services account surplus, along with healthy inward remittance receipts, would keep the current account deficit moderate and sustainable. Gross FDI inflows strengthened by 16.1% in Apr–Nov 2025, while FPI registered capital outflows of US\$ 5.8 bn (April– February 3rd). India's external debt remained stable at 19.2% of GDP at the end of September 2025, and FX reserves remain substantial, covering over 11 months of goods imports, as of the end of January 2026. On the exchange rate front, the rupee has been showing some recovery due to the prospective US–India trade agreement. Nonetheless, it remains above the 90 level against the USD, and the RBI will continue to contain any excessive volatility in the domestic currency.

Other Developmental and Regulatory Measures

The RBI announced a set of regulatory and developmental measures aimed at strengthening customer protection, advancing financial inclusion, improving credit flows, reinforcing Urban Co-operative Banks, promoting ease of doing business for NBFCs, and deepening financial markets.

Advancing Financial Inclusion and Credit Flow

- To enhance credit availability for Micro and Small Enterprises (MSEs) with limited collateral, **the RBI has enhanced the limit of collateral-free loans to MSEs from Rs 10 lakh to Rs 20 lakh**, with this change being applicable to all loans to MSE borrowers sanctioned or renewed on or after April 01, 2026
- To support financing for the real estate sector, banks will be permitted to lend to Real Estate Investment Trusts (REITs), subject to prudential safeguards.
- The RBI has completed a comprehensive review of the Lead Bank Scheme, the Kisan Credit Card Scheme, and the Business Correspondent model,

and will issue draft revised guidelines for these schemes.

Promoting Ease of Doing Business for NBFCs

- The RBI proposed exempting eligible NBFCs that do not accept public funds and have no customer interface, including Type-I NBFCs, from registration requirements, subject to specified conditions. This exemption will apply to such Type-I NBFCs with asset sizes not exceeding Rs 1,000 crore, subject to specified conditions. Draft Amendment Directions will be issued for stakeholder feedback.
- The RBI also proposed dispensing with the requirement for NBFC - Investment and Credit Companies (ICCs) engaged in the business of lending against gold collateral with over 1,000 branches to obtain prior approval to open new branches, thereby improving operational flexibility.

Deepening Financial Markets

- The RBI indicated that the revised regulations for External Commercial Borrowings (ECBs), previously issued in draft form, have been finalised and will be notified shortly.
- It proposed removing the limit of Rs 2.5 lakh crore for investments under the Voluntary Retention Route (VRR). Investment through the VRR in each category of securities will be subject to the investment ceiling for the respective category under the General Route. Certain additional operational flexibilities will also be provided to FPIs investing under the VRR.
- In line with the Union Budget FY27 announcement, the RBI will issue the regulatory framework for derivatives on corporate bond indices and total return swaps on corporate bonds.
- Draft revised guidelines will also be issued for Authorised Dealer banks and Stand-alone Primary Dealers to provide greater flexibility in undertaking foreign exchange transactions.

Customer Protection and Empowerment

- The RBI will issue draft guidelines to strengthen customer protection, covering mis-selling practices by REs, loan recovery and engagement of recovery agents, and limiting customer liability in unauthorised electronic banking transactions.
- A new framework is proposed under which customers will be compensated up to an amount of Rs 25,000 for loss arising from small-value fraudulent transactions, subject to certain

conditions, with draft instructions to be issued for public consultation.

- The RBI will also publish a discussion paper on measures to enhance the safety of digital payments, including proposals such as lagged credits and additional authentication for specific user groups, including senior citizens.

Strengthening Urban Co-operative Banks (UCBs)

- Measures have also been announced to strengthen UCBs, including increases in the financial limits on unsecured loans and loans extended to nominal members by UCBs.
- The RBI also proposed removing tenor- and moratorium-related requirements on housing loans extended by Tier III and Tier IV UCBs.
- To strengthen managerial and technical capabilities, the RBI will launch Mission-SAKSHAM (Sahakari Bank Kshamta Nirman), which will train over 1.4 lakh personnel across UCBs.

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