Monetary Policy Review

February 6, 2025

PRIME RESEARCH
Empowering decisions

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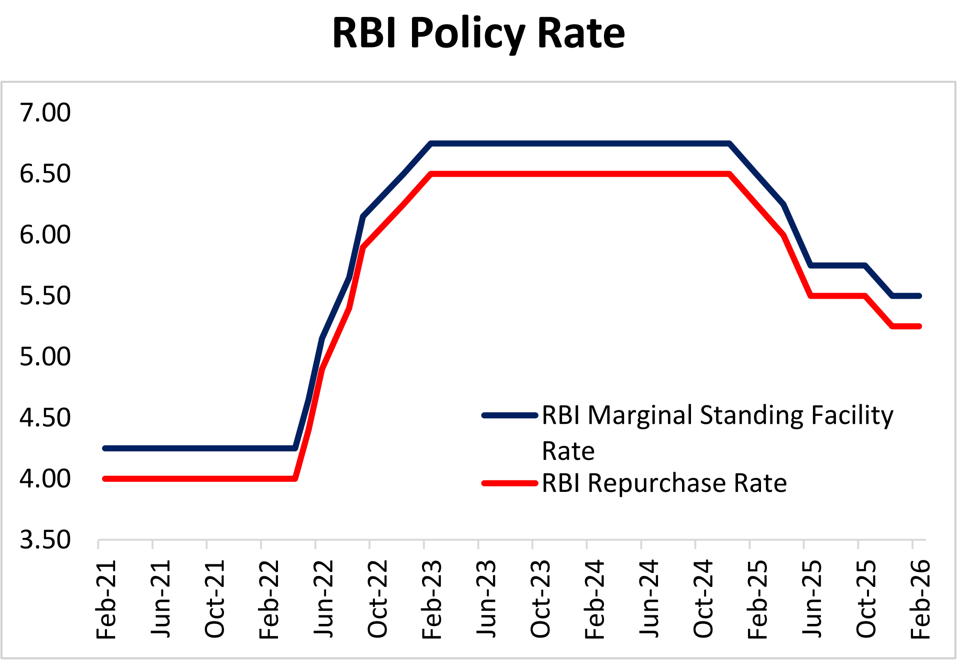
Key Highlights of The Policy

- The MPC voted unanimously to keep the policy repo rate unchanged at 5.25%; consequently, the standing deposit facility (SDF) rate under the liquidity adjustment facility (LAF) remains at 5.00% and the marginal standing facility (MSF) rate and the Bank Rate at 5.50%. The MPC also decided to continue with the neutral stance.
- Going forward, the MPC will be guided by the evolving macroeconomic conditions and the outlook based on data from the new series in charting the future course of monetary policy.
- In view of the impending release of the new CPI series (base 2024=100) on February 12, 2026, similar to growth, govt. will present CPI inflation projection for the full year 2026-27 in the April 2026 Policy Statement.
- *The RBI's policy marks a strategic reset rather than a pivot. With rate cuts largely behind, the focus is now on credit efficacy, market depth, and financial stability. Stable rates, benign inflation, targeted MSME support, and liberalised capital-flow mechanisms create a constructive medium-term backdrop for Indian equities and debt, reinforcing India's positioning as a high-growth, macro-stable emerging market.*



Inflation and Growth Dynamics

- **Inflation dynamics are equally supportive of policy stability.** Headline CPI inflation is expected at 2.1% in the current fiscal year, with a temporary uptick to 4.0%–4.2% in early FY2026–27 due largely to base effects—still well within the RBI's tolerance band.
- This benign inflation outlook provides the central bank with policy space to prioritise growth oriented structural interventions.

- **Macroeconomic fundamentals remain robust. Real GDP growth is projected at 7.4%** for FY2025–26, underpinned by resilient domestic consumption, sustained government capital expenditure, and the incremental impact of recently concluded trade agreements with the United States and the European Union.

RBI's Inflation Expectation: Revised upward to 2.1% from 2.0% for FY26

Inflation Expectations	2Q FY26	3Q FY26	4Q FY26	1Q FY27	2Q FY27	FY26
Feb'26 Projection			**3.2**	**4.0**	**4.2**	**2.1**
Dec'25 Projection	1.7	0.6	2.9	3.9	4.0	2.0
Oct'25 Projection	1.8	1.8	4.0	4.4	4.9	2.6
Aug'25 Projection	2.1	3.1	4.4	4.9	--	3.1
Jun'25 Projection	3.4	3.9	4.4	--	--	3.7

RBI's Growth projections: GDP growth revised upward to 7.4% for FY26

Growth Outlook	2Q FY26	3Q FY26	4Q FY26	1Q FY27	2Q FY27	FY26
Feb'26 Projection				**6.9**	**7.0**	**7.4**
Dec'25 Projection	8.2	7.0	6.5	6.7	6.8	7.3
Oct'25 Projection	7.8	7.0	6.4	6.2	6.4	6.8
Aug'25 Projection	6.7	6.6	6.3	6.6	--	6.5
Jun'25 Projection	6.7	6.6	6.3	--	--	6.5

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State of Economy

- As per the first advance estimates (FAE), private final consumption expenditure (PFCE) is estimated to grow at 7.0% in 2025-26 vis-à-vis 7.2% in the previous year. Gross fixed capital formation (GFCF) is estimated to expand strongly by 7.8% as against 7.1% growth in the last year.
- Core inflation hardened to 4.6% in December from 4.3% during October-November, owing to a surge in gold prices. Gold inflation (over 50% y-o-y since October 2025) contributed disproportionately to headline and core numbers.
- All-India reservoirs level stood at 66.6% of the total capacity as on February 5, 2026, as against 61.4% a year ago and a decadal average of 53.3%.
- Cement production growth accelerated to 11.1% in Q3:2025-26
- Bank credit to textiles, chemicals, base metals, and engineering goods increased y-o-y by 11.8%, 14.8%, 14.2%, and 30.4%, respectively, in December 2025. During Q3:2025-26, services exports at $111.2 billion grew at 7.5% y-o-y, while services imports at $53.7 billion expanded by 2.7%. Net services exports grew by 12.3 %y-o-y and stood at $57.5 billion during the same period.
- India's merchandise imports grew faster than merchandise exports, trade deficit rose to $91.5 billion in Q3:2025-26 from $88.0 billion in Q2:2025-26 and $78.7 billion in Q3:2024-25.
- India's inward remittances increased by 10.7% y-o-y to $39.0 billion in Q2:2025-26.
- Gross foreign direct investment (FDI) flows to India grew by 16.1% to $64.7 billion in April-November 2025-26 from $55.8 billion a year ago. Net FDI inflows stood higher at $5.6 billion during April- November 2025-26 from $0.8 billion a year ago.
- FPI to India recorded net outflows to the tune of $7.5 billion from the equity segment, while debt segment registered net inflows of $1.7 billion.
- India's external debt to GDP ratio rose marginally to 19.2% at end-September 2025 from 19.1% at end-March 2025.

Liquidity Conditions

- The average daily net absorption under the liquidity adjustment facility (LAF) during October and November stood at Rs. 0.9 lakh crore and Rs. 1.9 lakh crore, respectively. The average daily net absorption under the LAF declined to Rs. 0.8 lakh crore in December 2025 and January 2026. In February 2026 (up to February 4), average daily net absorption under the LAF increased to Rs. 1.8 lakh crore.
- The Reserve Bank conducted OMO purchase auctions amounting to Rs. 3,50,000 crore and long-term forex buy/sell swap auction of $15.1 billion in December 2025 and January 2026.
- The Reserve Bank conducted additional OMO purchase auctions amounting to Rs. 1,00,000 crore, long term forex buy/sell swaps of $10 billion, 90-day VRR operation of Rs. 25,000 crore and a second 90-day VRR operation of Rs. 1,11,500 crore for January and February 2026.
- Interest rate effect on transmission to weighted average lending rate (WALR) is calculated by keeping the weight constant (as of January 2025).
- The moderation in the weighted average lending rate (WALR) of outstanding rupee loans has been to the extent of 81 bps. Transmission has been broad-based across sectors.
- In response to the cumulative policy repo rate cut of 125 basis points (bps) in the current easing cycle, the WACR, the 3-month T-bill rate, the 3-month CP issued by NBFCs, and the 3-month CD rate declined by 89 bps, 119 bps, 143 bps, and 127 bps, respectively up to end-December, 2025. However, since the beginning of January and up to February 4, 2026, the 3-month T-bill rate, the 3-month CP issued by NBFCs, and the 3-month CD rate have hardened by 6 bps, 73 bps and 84 bps, respectively.
- Credit from all sources grew at 13.8 %(y-o-y), as compared to 11.6 %(y-o-y) a year ago.

Key Structural Measure

Regulations

- Advertising, Marketing and Sales of Financial Products and Services by Regulated Entities (REs)
- Conduct of Regulated Entities in Recovery of Loans and Engagement of Recovery Agents
- Review of framework of Limiting Customer Liability in digital transactions
- Commercial bank to extend Lending to Real Estate Investment Trusts (REITs)
- Review of Lending norms for UCBs: Unsecured loans, limits for lending to nominal members; and the tenor and moratorium requirements for housing loans
- Exemption from registration to eligible NBFCs not availing public funds and not having customer interface (including 'Type I NBFCs')
- Amendment of NBFC Branch Authorisation Directions-2025 : NBFC - Investment and Credit Companies (ICCs) engaged in the business of lending against gold collateral with over 1,000 branches are required to obtain prior RBI approval for opening new branches.

Payment System

- Exploring safeguards in digital payments to curb frauds: Introduction of lagged credits, additional authentication for specific class of users like senior citizens, etc.: compensation to customers up to an amount of Rs. 25000/- for loss incurred in small-value fraudulent transactions.

Financial Inclusion

- Revision in Lead Bank Scheme : A unified portal for reporting of Bank-wise LBS data
- Revision in the Guidelines of Kisan Credit Card (KCC) and tenure extension to six years
- Set up a committee to review of guidelines relating to use of Business Correspondents (BCs) by banks
- Enhancement in Collateral free loan limit from Rs. 10 lakh to Rs. 20 lakh to MSME, all loans to MSE borrowers sanctioned or renewed on or after April 01, 2026.

Financial Markets

- Development of corporate bond market: Total return swaps on corporate bonds and derivatives on corporate bond indices will be introduced.
- Foreign Exchange Dealings of Authorised Dealers with greater flexibility with respect to foreign exchange products, risk management and platforms.
- Removal of the Voluntary Retention Route for FPI investment in debt instruments (the current investment limit of Rs. 2.5 lakh crore)
  - (a) Investments under the VRR shall now be reckoned under the limit for FPI investments under the General Route; and
  - (b) Certain additional operational flexibilities will be provided to FPIs investing under the VRR.

Capacity Building

- Mission Saksham((Sahakari Bank Kshamta Nirman) – Capacity Building for the UCB Sector to cover about 1.40 lakh participants, across all functions

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