DALAL & BROACHA

Repo Rate – Status Quo maintained

Equity Research Desk

1 October 2025

Pro-growth measures announced for Banks & NBFCs !!!

The Monetary Policy Committee (MPC) of the Reserve Bank of India has maintained the repo rate at 5.5%, marking a cumulative rate cut of 100 basis points so far in 2025. This decision is grounded in the RBI's revised inflation forecast for FY26, which has been aggressively lowered by 110 basis points to 2.6%, primarily owing to reduced food and fuel prices and favorable base effects. While core inflation remains a concern, it is currently under control. Meanwhile, the real GDP growth forecast for FY26 has been raised to 6.8% from the earlier estimate of 6.5%. The MPC has adopted a prudent "wait and watch" approach to evaluate the full impact of the cumulative rate cuts before determining the next steps.

In response to the 100 basis points repo rate cut, the weighted average lending rate (WALR) of scheduled commercial banks has decreased by 58 basis points for fresh rupee loans and by 55 basis points for outstanding loans. On the deposit side, the weighted average domestic term deposit rate (WADTDR) has dropped by 106 basis points for fresh deposits and by 22 basis points for existing deposits. The surplus liquidity of ₹2.1 trillion in the system, along with the remaining phased reductions in the cash reserve ratio (CRR), is expected to further improve the transmission of monetary policy.

Looking ahead, there is an expectation of additional cumulative repo rate cuts amounting to another 100 basis points over the next 12 to 18 months, potentially bringing the repo rate down to around 4.5%. This could also trigger a similar decline in government securities yields. Recent banking sector reforms announced alongside the monetary policy, including the extension of the Expected Credit Loss (ECL) provisioning norms effective FY27, relaxation in lending norms for loans against shares and IPO financing, withdrawal of restrictions on large corporate lending, and reduced risk weights for NBFC infrastructure project financing, are all pro-growth measures that bode well for banks and the NBFC sector in general.

Rationale and Policy Outlook

- Inflation Management: The RBI has aggressively reduced its FY26 inflation forecast by 110 basis points to 2.6%, primarily due to lower food and fuel prices and favorable base effects. Core inflation remains a concern but is currently under control.
- Inflation Expectations: Household and professional surveys indicate declining inflation expectations, reinforcing the view that inflation is likely to stay within or below target levels in the near term.
- Global Factors: External risks including geopolitical tensions, tariffs, and commodity price volatility—especially crude oil—are influencing the cautious approach. Despite global uncertainties, India's strong macroeconomic fundamentals support a stable outlook.
- GDP growth forecast for FY26 has been increased from 6.5% to 6.8%

Key macro numbers & policy rates

Parameter	Before Jun 2025	Jun-25	Oct-25
Repo Rate	6.0%	5.5%	5.5%
CRR	4.0%	3.0%	3.0%
FY26 Inflation Outlook	4.0%	3.7%	2.6%
FY26 Growth Outlook	6.5%	6.5%	6.8%

Source: RBI

Inflation

- Headline inflation saw considerable moderation, mainly due to a sharp decline in food prices and GST rate rationalisation.
- FY26 CPI inflation projection was revised down to 2.6% (from 3.7% in June, 3.1% in August); Q4 FY26 and Q1 FY27 projections also lowered, aligning with the RBI target despite base effects.
- Benign food inflation prospects are supported by good monsoon, healthy kharif sowing, reservoir levels, and ample food grain buffer stocks.

Growth

- Economic activity remains resilient: Q1 FY26 GDP growth at 7.8%, GVA at 7.6%.
- FY26 real GDP growth forecast is 6.8% (Q2: 7.0%, Q3: 6.4%, Q4: 6.2%); Q1 FY27 projected at 6.4%.
- Growth supported by strong services, favorable monsoon, rationalisation of GST rates, and monetary easing; risks from trade headwinds and global uncertainties are noted.

Along with the policy, RBI has announced the slew of other measures for Banking & NBFC sector. Below are the details –

Banking Sector Measures

- **Expected Credit Loss (ECL) framework**: Applicable to all Scheduled Commercial Banks (excluding SFBs, PBs, RRBs) and All India Financial Institutions from April 1, 2027, with a glide path till March 31, 2031.

- **Revised Basel III norms**: Effective from April 1, 2027, excluding SFBs, PBs, and RRBs. A Standardised Approach for Credit Risk will be released, lowering risk weights for MSMEs and housing loans.

- **Capital requirements:** Operational risk standards already issued (2023); market risk standards under consultation.

- **Forms of Business & Investment Regulations:** Finalised guidelines after consultations; restrictions on overlap of business between banks and group entities removed — Boards to decide strategic allocation.

- **Risk-based deposit insurance premium:** Proposed to introduce risk-based deposit insurance premium with the currently applicable flat rate of premium as the ceiling. This will incentivise sound risk management by banks and reduce premium to be paid by better rated banks.

Improving Flow of Credit

- **Banks financing Indian corporates' acquisitions**: An enabling framework will be introduced.
- **Relaxation of regulations on lending:**
    - Removal of lending ceiling against listed debt securities.
    - Higher limits for lending against shares (increased from INR 20 lakh to INR 1 crore).
    - Higher IPO financing limit (increased from INR 10 lakh to INR 25 lakh per person).
- **Withdrawal of 2016 disincentive framework**: Earlier restrictions on lending to large borrowers (₹10,000 crore+ group exposure) will be scrapped. Systemic concentration risks to be managed with macroprudential tools.
- **NBFC lending to infrastructure:** Reduced risk weights for NBFC loans to operational, high-quality infrastructure projects.
- **Urban Co-operative Banks licensing**: Licensing, paused since 2004, may restart after release of a discussion paper.

Promoting Ease of Doing Business

- **Rationalisation of regulations:** About 9,000 RBI circulars and directions consolidated across 11 types of entities; drafts to be issued for consultation.
- **Flexibility in transaction accounts**: Banks may more freely manage borrowers' current, CC/OD, and collection accounts. Especially beneficial for borrowers regulated by financial sector regulators.

Export sector reforms:

- **Repatriation from exporters' foreign currency accounts in IFSC**: timeline extended from 1 month to 3 months.
- **Merchanting Trade forex outlay period**: extended from 4 months to 6 months.
- Simplified reconciliation of outstanding entries in EDPMS/IDPMS reporting portals for imports/exports.

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