RBI Monetary Policy Highlights – Oct'25

An Expected Pause; Room for Rate Cut Still Open

The RBI's decision to keep the repo rate unchanged was in line with our expectations. The recent GST rate rationalisation comes at an opportune time and is expected to support consumption demand during the festive season. The regulator has revised its growth forecast upwards for Q2 and FY26, while a marginal downward revision is seen in H2FY26 onwards. However, **inflationary pressures are expected to continue to ease in the near term**. **The pause in the current meeting leaves room for the RBI to opt for a 25bps rate cut in the forthcoming meeting, with growth buoyancy continuing and expectations of softening inflationary pressures**.

For banks, Q2 is expected to be another soft quarter, with tepid growth, NIM pressures, weaker treasury performance sequentially and higher credit costs. Banks are yet to see a meaningful recovery in credit growth, which is expected from H2 onwards. For banks, we expect NIMs to bottom out in Q2, so far. H2 margins should find support from deposit repricing and the CRR cut. Banks are seeing green shoots in terms of asset quality metrics and expect better outcomes from H2 onwards. **We believe valuations for most banks are comfortable, and clarity on pick-up in growth and improving asset quality metrics would warrant upside in banking stocks**. **At present, we continue to prefer banks with promising growth prospects, healthy deposit franchises, stable asset quality metrics, and strong and steady management teams.**

The regulator has also **prescribed additional measures** to strengthen the resilience and competitiveness of the banking sector. The measures are:

- ✓ **The Expected Credit Loss (ECL) framework** of provisioning with prudential floors is proposed to be made applicable to **all Scheduled Commercial Banks (excluding Small Finance Banks (SFBs), Payment Banks (PBs), Regional Rural Banks (RRBs))** and All India Financial Institutions (AIFIs) with effect from **1st April, 2027.** The RBI has also indicated that the banks will be given a **glidepath till 31st March, 2031**, to smooth the one-time impact of higher provisioning, if any, on their existing books.
- ✓ Further, the RBI has proposed to make the **revised Basel III capital adequacy norms** effective for commercial banks (excluding SFBs, PBs and RRBs) from **1st April, 2027**. The regulator will issue a draft of the Standardised Approach for Credit Risk shortly. Under the revised approach, **the proposed lower risk weights** on certain segments are expected to **reduce the overall capital requirements**, particularly for **MSMEs and residential real estate** (including home loans).
- ✓ A draft circular on Forms of Business and Prudential Regulation for Investments was issued in Oct'24. It has been finalised after public consultations and will be issued shortly. The **proposed regulatory restriction on overlap in the businesses undertaken by a bank** and its group entity(ies) is **being removed** from the final guidelines. The strategic allocation of business streams among group entities will be left to the wisdom of bank boards.
- ✓ The RBI further proposed to introduce risk-based deposit insurance premiums with the currently applicable flat rate of premium as the ceiling. This will incentivise sound risk management by banks and reduce premiums to be paid by better-rated banks.

*Stock Picks:

Private Banks – **HDFC Bank, Kotak Mahindra Bank, Federal Bank**

PSU Banks – SBI

NBFCs – Shriram Finance, Bajaj Finance

(*Pls note these are event-based picks)

Key Rates

	Current (%)	Previous (%)
Repo Rate	5.50	5.50
Reverse Repo Rate	3.35	3.35
MSF	5.75	5.75
SDF	5.25	5.25

GDP Growth Estimates

	Current (%)	Previous (%)
Q2FY26	7.0	6.7
Q3FY26	6.4	6.6
Q4FY26	6.2	6.3
FY26	6.8	6.5
Q1FY27	6.4	6.6

Inflation Estimates

	Current (%)	Previous (%)
Q2FY26	1.8	2.1
Q3FY26	1.8	3.1
Q4FY26	4.0	4.4
FY26	2.6	3.1
Q1FY27	4.5	4.9

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Additional Measures to Improve the Flow of Credit

The RBI announced 5 measures to improve the flow of credit.

- To expand the scope of capital market lending by banks, the regulator proposed to provide an enabling framework for Indian banks to finance acquisitions by Indian corporates.

- The RBI proposed to (a) **remove the regulatory ceiling on lending against listed debt securities** and (b) **enhance limits for lending by banks against shares** from Rs 20 Lc to Rs 1 Cr and for IPO financing from Rs 10 Lc to Rs 25 Lc per person.

- The regulator has also proposed to withdraw the framework introduced in 2016 that disincentivised lending by banks to specified borrowers (with a **credit limit from the banking system of Rs 10,000 Cr and above**).

- To reduce the cost of infrastructure financing by NBFCs, the regulator has proposed to **reduce the risk weights (RW) applicable to lending by NBFCs** to **operational, high-quality infrastructure projects**.

- Since 2004, licensing for Urban Co-operative Banks (UCBs) has been paused. Considering the positive developments in the sector during the last two decades and in response to the growing demand from the stakeholders, we propose to publish a discussion paper on the licensing of new UCBs.

Measures to Enhance Consumer Satisfaction

- The bouquet of services offered to Basic Savings Bank Deposit account holders without levy of minimum balance charges is proposed to be expanded to, inter alia, include digital banking (mobile/internet banking) services.

- The Internal Ombudsman mechanism is proposed to be strengthened to make grievance redressal by regulated entities more effective.

- The RBI Ombudsman Scheme is also being revised for improved grievance redressal, and rural cooperative banks are being included under the ambit of the Scheme.

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