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RBI POLICY STATEMENT REINFORCES NO RATE HIKES IN FY27: $36.7 BN FCNR(B) FLOWS TRANSLATE INTO ~$20 BN FOREX RESERVE RECOUP AND $13 BN DOLLAR SALES TO VACATE SHORT TERM FORWARDS

Issue No. 17, FY27
Date: 05 Aug 2026

As expected, RBI MPC unanimously decided to keep repo rate unchanged at 5.25% and continuing with the neutral stance. A 10 bps increase in growth forecast of FY27 (and Q1 estimate to 7.0%) and an equivalent reduction in CPI inflation forecast for FY27 reveal that the resilient domestic economy has been able to fathom headwinds with material parameters and indicators all showing an accelerated pace in Q1. Growth is supposed to be buoyant in Q1FY28 with RBI projections at 7.3% with inflation at 5.3% indicating that the growth inflation tradeoff will remain in fine balance.

Interestingly, a lexicon-based Natural Language Processing approach was employed to quantify the communication tone of the RBI Governor's statement into three communication dimensions i.e. Dovish, Hawkish and Uncertainty. Our **analysis indicates that the policy statement exhibits a predominantly dovish communication profile, with the Dovish Communication Index accounting for 50.9% of all policy-related lexical matches (increased from 40.83% in last policy), followed by the Uncertainty Communication Index at 25.4% (declined from 34.8% in last policy) and the Hawkish Communication Index at 23.7% (declining from 24.5% in last policy). Clearly, the RBI policy statement pushes out any rate hikes in FY27 with inflation also remaining benign at 5% and core inflation at 4.3%.**

Regarding regulatory measures, RBI has proposed to harmonize and standardize the regulatory framework on interest rates on advances across all regulated entities (REs). Pricing of bank loans has long history of evolution keeping in mind transparency and monetary policy transmission imperatives. Up till 2010 banks used the Prime Lending Rate, followed by the base rate. After 2016, the banks have migrated to MCLR that links the lending rates to marginal cost of fund. To further increase the transmission, in 2019 RBI permitted EBLR. Currently, 67.6% of the bank loan are under EBLR regime. These parallel regimes need some standardization to ensure uniformity, enhance transparency in loan pricing, strengthen monetary transmission and bolster consumer protection. The proposed measure is steering the loan pricing policy in this direction.

RBI has also decided to resume licensing of UCBs on 'on tap' basis. UCBs have long been an essential part of India's cooperative story, providing banking services to segments - often underserved by larger banks - small traders, self-employed individuals, salaried workers, and others in the informal sector. As of March 2025, there are around 1457 UCBs in India, which hold around 2% of the deposits. Licensing of new UCBs has been paused since 2004, so, this step will enhance financial inclusion but there is a need for stronger governance, professional management, timely oversight, and secure technology adoption for resilience.

RBI is also issuing directions after a comprehensive review of the credit monitoring arrangement for rural cooperative banks (RCB), considering experience gained and developments since the framework was last revised in 2008. Share of RCB in total assets of cooperative sector has increased from 66.9% in March 2020 to 71.2% in March 2024 (latest data). However, given the narrow business base on the lending side, RCB continue to face the challenges of lending portfolio concentration (sector and geographic) compared to UCBs. The current measure addresses this aspect of the RCB structure.

One of the interesting points in the policy statement is the statement on exchange rates. The RBI has clearly emphasized that the central bank will ensure that no self-fulfilling prophecy is built into foreign exchange market. The $36.7 bn FCNR (B) inflows till 31 July have enabled FX reserves (i.e., FCA) recoup of ~$20.0 bn and vacating outstanding forward position by $13 bn in the short end (up to 3 months) till June end.

MPC KEPT REPO RATE UNCHANGED AT 5.25%

- MPC unanimously decided to keep repo rate unchanged at 5.25%. The MPC also continued with the neutral stance. The future course of monetary policy will continue to remain data -dependent with RBI reaffirming its commitment to align inflation with the target.
- RBI has upgraded its FY27 real GDP growth projection by 10 bps to 6.7% with Q1 at 7.0% (earlier: 6.6%); Q2 at 6.4%; Q3 at 6.5% and Q4 at 6.8%. The domestic economic environment remained resilient amidst persisting global headwinds. Private consumption remained robust. Investment continues to be resilient. The downside risk emerges from energy prices and supply chain vulnerabilities. El Niño conditions poses some risks to agriculture sector's outlook and rural demand, but the adaptation measure have produced desired results so far.
- ♦ Regarding inflation forecast, RBI has downgraded its FY27 CPI inflation projection by 10 bps to 5.0%. The estimate of core CPI has also been cut by 40 bps to 4.3%. The estimate largely hinges upon temporal and spatial rainfall distribution and risks of higher food, fuel and other input prices due to geopolitical developments. RBI expects Q2 inflation at 4.7%; Q3 at 5.9%; and Q4 at 5.5%.

RBI Growth & Inflation Outlook for India

	CPI Inflation (%)			GDP Growth rate (%)		
	Jun'26 Policy	Aug'26 Policy	Change in bps	Jun'26 Policy	Aug'26 Policy	Change in bps
Q1 FY27	4.2	3.9*	-30	6.6	7	40
Q2 FY27	5.1	4.7	-40	6.3	6.4	10
Q3 FY27	5.9	5.9	0	6.5	6.5	0
Q4 FY27	5.4	5.5	10	6.8	6.8	0
FY27	5.1	5	-10	6.6	6.7	10
Q1 FY28	-	5.3	-	-	7.3	-
FY 27 Core Inflation	4.7	4.3	-40			

Source: RBI, SBI Research, *Q1 FY 27 Inflation is actual

REGULATORY MEASURES

- ♦ **Review of Guidelines on Interest Rates on Advances:** Pricing of bank loans has long history of evolution keeping in mind transparency and monetary policy transmission imperatives. Up till 2010 banks used the Prime Lending Rate, followed by the base rate. After 2016, the banks have migrated to MCLR that links the lending rates to marginal cost of fund. To further increase the transmission, in 2019 RBI permitted EBLR. Currently, 67.6% of the bank loan are under EBLR regime. These parallel regimes need some standardization to ensure uniformity, enhance transparency in loan pricing, strengthen monetary transmission and bolster consumer protection. The proposed measure is steering the loan pricing policy in this direction.
- ♦ **Draft guidelines for licensing of Urban Co-operative Banks (UBC)**: The on-tap licensing framework for banks has been put in place for commercial banks and small finance banks by RBI since 2024. Given the importance of UCB in extending last -mile credit and supporting localized financial intermediation, RBI has now introduced the on-tap licensing in UCB. This measure not only harmonizes the bank licensing policy but also opens way to introduce fresh capital and innovation in this sector.
- ♦ As of March 2025, there are around 1457 UCBs in India, which holds around 2% of the deposits. Licensing of new UCBs has been paused since 2004, so, this step will enhance financial inclusion but there is a need for stronger governance, professional management, timely oversight, and secure technology adoption for resilience.
- ♦ **Review of Guidelines on Concentration Risk Management - Rural Co-operative Banks (RCB)**: RCB is not a homogenous segment. It comprises of short-term credit institutions — comprising state and district central co-operative banks and primary agricultural credit societies who play a pivotal role in agricultural finance. Then we also have RCBs that have long term exposure. RCBs are structurally different from UCBs in terms of their balance sheet composition. While UCBs mainly depend on deposits to raise funds, RCBs rely heavily on borrowings.
- ♦ Short-term credit co-operatives depend primarily on deposits; long-term co-operatives rely more on borrowings and owned funds. Share of RCB in total assets of cooperative sector has increased from 66.9% in March 2020 to 71.2% in March 2024 (latest data). However, given the narrow business base on the lending side, RCB continue to face the challenges of lending portfolio concentration (sector and geographic) compared to UCBs. The current measure addresses this aspect of the RCB structure.

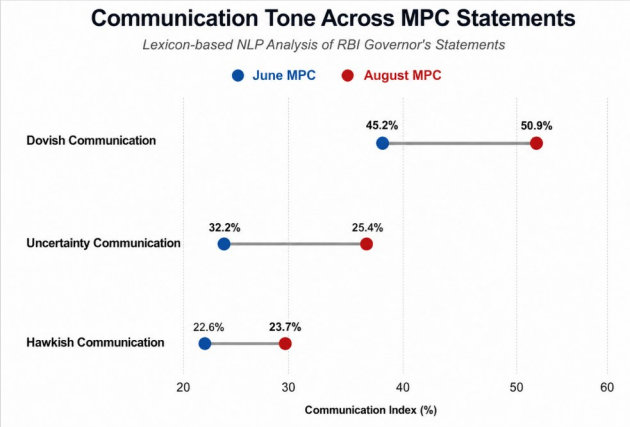
Distribution of UCBs (At end-March 2025)

Amount Rs crore	Deposits		Advances		Assets	
	No. of UCBs	Amount	No. of UCBs	Amount	No. of UCBs	Amount
0 ≤ X < 100	759	32750	927	32673	645	30894
% Share	52.1	5.6	63.6	8.8	44.3	4.2
100 ≤ X < 250	320	52,010	267	41,517	360	58,874
% Share	22.0	8.9	18.3	11.2	24.7	8.0
250 ≤ X < 500	167	59,779	137	48,504	193	68,858
% Share	11.5	10.2	9.4	13.1	13.2	9.3
500 ≤ X < 1000	109	74,624	69	48,066	136	96,262
% Share	7.5	12.8	4.7	13.0	9.3	13.0
1000 ≤ X	102	3,65,252	57	1,99,464	123	4,83,841
% Share	7.0	62.5	3.9	53.9	8.4	65.5
Total	**1,457**	**5,84,415**	**1,457**	**3,70,225**	**1,457**	**7,38,729**

Source: RBI, SBI Research

MPC TONE SHOWS INCREASED DOVISHNESS

- A lexicon-based Natural Language Processing approach was employed to quantify the communication tone of the RBI Governor's statement. A custom monetary policy lexicon was developed to classify policy-related terms into three communication dimensions i.e. Dovish, Hawkish and Uncertainty.
- **The analysis indicates that the statement exhibits a predominantly dovish communication profile, with the Dovish Communication Index accounting for 50.9% of all policy-related lexical matches (increased from 40.83% in last policy), followed by the Uncertainty Communication Index at 25.4% (declined from 34.8% in last policy) and the Hawkish Communication Index at 23.7% (declining from 24.5% in last policy).**



THE FALLACY OF REAL INTEREST RATE AND DEPOSITS GROWTH

- In response to the 125 bps cut in the policy repo rate cumulatively during Feb'25 to Jun'26, the weighted average domestic term deposit rate (WADTDR) on fresh deposits has declined by 63 bps while that on outstanding deposits has softened by 51 bps during the same period. The real interest rate declined from 2.52% in Jan'26 to 0.87% in Jun'26 and this has been brewing an unfounded fear that this will impact deposits growth.
- **There is no empirical evidence to suggest that in India real interest rates and deposits growth are not correlated. Deposits in fact are more influenced by the existing rate structure that are heavily loaded against such. Real deposit and policy rates moderated during Jan-Jun'26 due to higher inflation, while deposit growth improved from 12.3% in Jan'26 to 13.3% in Jun'26 (ex FCNR also: 13.0%). This suggests deposit mobilization remained resilient despite lower real returns.**
- Finally, the banking health indicators shows that banks remained strong during the last one year, with improvement in CRAR, and better asset quality.

Real Interest Rate and Deposit Mobilization

Month	Repo rate	CPI Inflation	Real Deposit Rate	Real Interest rate	Deposit Growth (% y-o-y)
Jan-2026	5.25	2.73	3.91	2.52	12.30
Jun-2026	5.25	4.38	2.20	0.87	13.30

Source: SBI Research

Financial Stability Indicators (%): SCBs vs NBFC

Parameters	SCB		NBFC	
	Jun-26	Jun-25	Jun-26	Jun-25
CRAR	17.8	17.5	25.4	25.8
GNPA	1.7	2.2	2.5	3.1
NNPA	0.4	0.5	0.8	1.0
NIM	3.2	3.3	5.4	5.0
RoA	1.3	1.3	3.4	3.0
RoE	13.2	13.0	-	
LCR	126.9	132.8		

Source: SBI Research, RBI

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