HSBC Mutual Fund

The Macro Sphere

RBI Monetary Policy Review

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MPC resists "peer pressure", maintains neutral hold

The MPC in a unanimous vote decided to maintain a pause on the Repo Rate at 5.25% while maintaining a neutral stance.

Our View: The RBI MPC delivered a neutral hold, but the communication has dovish undertones because it sees inflation pressures as mainly supply-driven and not broad-based, with benign core-core inflation and FY27 CPI revised down ~10bps to 5.0%, with inflation expected to peak at 5.9% in Q3 FY27 and then ease to 5.3% in Q1 FY28. That said, the path to any policy pivot is expected to remain calibrated and highly data-dependent, with West Asia conflict and weather risks (El Niño/monsoon) and US Fed actions key swing factors. While a rate hike in the latter half of FY27 is possible, the timing is unclear as the policy pivot is highly data sensitive.

The policy is in line with our expectations, with the shades of dovishness reflected in policy remarks such as supply-side led price pressures, inflation is not getting broad-based yet, underlying core inflation is running benign at 2.3-2.5% levels and lastly, the 10bps downward revision in inflation (largely due to softer inflation prints observed and estimated for 1H FY27); hence, for FY27 inflation forecast is set out at 5.0% YoY. The Q1FY28 forecast is forecasted at 5.3% YoY which also indicates that the RBI MPC is expecting inflation to glide lower after peaking at 5.9% in Q3FY27.

The softer core inflation prints, despite resilient economic growth, suggest that price pressures are not generalized, so far. Hence, even as growth continues to be resilient, the outlook remains 'hazy' - because of the uncertainties regarding south-west monsoon, El Niño, geopolitics and global trade policy. The MPC did emphasize on the need for greater clarity on inflation, not only the path but also its composition. Therefore, in our view, the policy pivot is likely to be far more calibrated.

Key policy highlights and our take

In June 2026 policy, the RBI turned on the dollar-mobilization spigot by incentivizing banks to raise fresh foreign currency deposits by absorbing banks' hedging costs, this is similar to the CY13 playbook and FCNR (B) specifically helped India mobilize about ~US$26bn back then. When we assess the current situation, the same has yielded favourable flows to the tune of ~US$ 41bn from 8-June to 31-July. The RBI Governor in his speech indicated that those capital flow measures have supported inflows and as a result, the balance of payments is expected to register a healthy surplus this year.

Governor also explicitly explained the RBI's stance on currency stating, "we will continue with our policy of it being determined by market forces, while curbing excessive volatility, checking speculative behavior and preventing disorderly movements to ensure that it is not out of sync with fundamentals or disruptive of economic activity. For this purpose, we have a broad range of effective regulatory and market-based instruments."

On liquidity, the RBI stated that it will ensure proactively ensure sufficient liquidity in the banking system, guided by the objective of aligning the weighted average call rate (WACR) to the policy repo rate. In similar context, the Governor at the presser mentioned that even though domestic liquidity may increase owing to strong NRI deposit dollar inflows, it may not remain in a large surplus for too long, given the demand for liquidity for growth and developments on the FX front. This coupled with the comment on using two-sided operations suggests that RBI may not be in a hurry to deploy permanent liquidity instruments such as OMO sales and incremental CRR hikes etc. to absorb system liquidity.

As we have mentioned before, in terms of operating target / implementation - RBI will use two-way operations to ensure sufficient liquidity, aiming to align WACR to the policy repo rate. While market rates saw some easing in May-June, there has been moderation in credit transmission to fresh lending rates in recent months reflecting robust credit demand.

Growth-inflation outlook altered, just a tad

On the growth-inflation dynamics, the West Asia conflict coupled with the brewing El Nino conditions has culminated into two exogenous shocks, impacting India's economic activity and also, putting pressure on inflation. However, for now, given the Q1FY27 data and outlook for next couple of months, 1H FY27 has altered the growth-inflation dynamics for full-year FY27. The table below elucidates the revised forecasts which evince that the

For FY27, growth forecast revised a tad higher by 10bps to 6.7% and it largely is due to the 40bps uptick forecasted for Q1FY27. For remaining quarters, forecasts remain largely unchanged, with growth expected to be in the 7% handle (at 7.3% in Q1 FY28) – the first 12-month ahead forecast. Outlook, however, remains 'hazy' as the MPC flagged risks from energy prices, supply-chain uncertainties and uneven rainfall precipitation. The offsets to growth come from supply-side measures, investment/capex spending and possibly there could be tailwinds from recent trade agreements.

On inflation, the MPC comments indicated vigilance, while the forecasts showed a less worrying outlook. The MPC lowered its CPI inflation forecast for FY27 to 5.0% from 5.1% in June, bulk of it concentrated in 1HFY27 figures as it retained its medium-term outlook. For 12 months ahead, CPI inflation is at 5.3% for Q1 FY28, expected to glide lower from the peak of 5.9% in Q3FY27 (table below). Key takeaways from inflation were the MPC's forecast for FY27 core inflation - which was lowered considerably by 40bps to 4.3% from 4.7% at the Jun'26 meet. Core inflation (excl. precious metals) it said is tracking even more soft at 2.3-2.5% YoY. These soft prints, as per MPC suggest that the demand pressures remain contained and are likely to align with core inflation prints (of 4.3%) by the end of FY27. All-in-all, the MPC is of the view that while the headline inflation flare-up is driven by food and fuel prices, there was limited evidence of a broadening of core inflation pressures.

Table 1: MPC's growth and inflation forecasts are laid out below:

	Growth Forecast				Inflation Forecast			
Period	Apr'26	Jun'26	Aug'26	Revision (last policy)	Apr'26	Jun'26	Aug'26	Revision (last policy)
Q1FY27	6.8%	6.6%	7.0%	0.4%	4.0%	4.2%	3.9%	-0.3%
Q2FY27	6.7%	6.3%	6.4%	0.1%	4.4%	5.1%	4.7%	-0.4%
Q3FY27	7.0%	6.5%	6.5%	0.0%	5.2%	5.9%	5.9%	0.0%
04FY27	7.2%	6.8%	6.8%	0.0%	4.7%	5.4%	5.5%	0.1%
FY27	6.9%	6.6%	6.7%	0.1%	4.6%	5.1%	5.0%	-0.1%
Q1FY28	-	-	7.3%	-	-	-	5.3%	-

Source: RBI MPC Policy Resolutions, Revision over last policy

Regulatory measures: The RBI said it will resume 'on tap' licensing for Urban Co-operative Banks and update concentration risk norms for Rural Co-operative Banks (revisiting 2008 CMA instructions), with drafts issued for consultation.

It will also rationalise interest-rate rules for all Regulated Entities, addressing MCLR/EBLR operations and standardising practices (e.g., day-count and benchmark reset dates) to improve transparency, transmission, and consumer protection.

In summary, the RBI MPC, for the third time since the West Asia conflict, has maintained a calm demeanor amid all the EM rate hike 'peer-pressure', thanks to the evolving inflation trajectory which allows the MPC to remain data-dependent and take a wait & watch approach. We believe policy exit is contingent upon the scale and size of the external shocks, and the US Fed policy action also becoming one of the key input parameters into the RBI-MPC's reaction function.

Abbreviations:

IGBs: Indian Government Bonds
RBI: Reserve Bank of India
MPC: Monetary Policy Committee
SDF: Standing Deposit Facility
VRR: Variable Rate Repo
VRRRs: Variable Rate Reverse Repo
MSF: Marginal Standing Facility
CRR: Cash Reserve Ratio
SDL: State Development Loan
OMO: Open Market Operations
GDP: Gross Domestic Product
CPI: Consumer Price Index
G-Sec: Government Securities
EMs: Emerging Markets
FX: Foreign Exchange
FCNR(B): Foreign Currency Non-Resident (Bank)
NRIs: Non-Resident Indians
OCIs: Overseas Citizens of India

Source - RBI MPC Policy Resolutions, HSBC MF Research, Data as on August 05, 2026, or mentioned otherwise.

Note: Views provided above are based on information in public domain and subject to change. Investors are requested to consult their financial advisor for any investment decisions.

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