

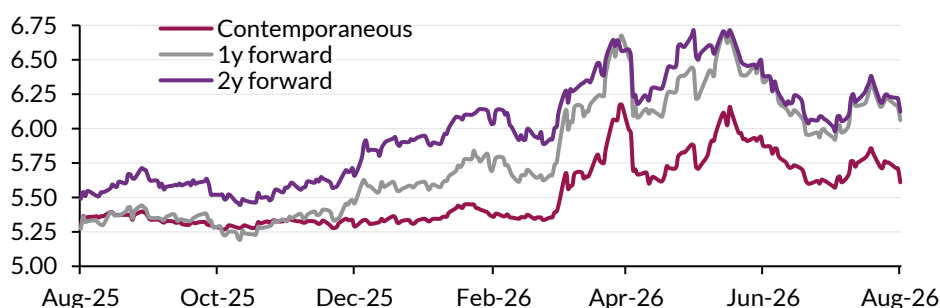
MPC holds, flags eventual recalibration

The MPC held unanimously, seeing inflation impulses fading after a Q3 peak and limited second round effects. However, language indicates a future recalibration of policy amid normalizing inflation; clarity on Monsoon and global factors being awaited. There is some transmission of impulses already seen. Stronger nominal growth is also a risk, harking back to experience of WPI transmitting to CPI inflation. These trends indicate Dec as the first potentially live meeting, with rates likely to rise to 'neutral' of 6.0% over time. Language also agreed with our projection of a temporary hump to liquidity – not actively seeking easier liquidity can expose benchmarks to widening global term premia.

August 05, 2026

MPC update

Exhibit 1 - Average 1y overnight levels backed out from OIS – 6% terminal seen



Source: Bloomberg, Axis Bank Research

MPC holds with base case of inflation fading after Q3

The MPC held rates unanimously. Inflation projections were trimmed focussing on Q2, after softer Q1 performance (Fig 2). Near-term growth forecasts were raised (Fig 3) in line with resilient high frequency indicators of late. Discretionary demand and GOI-driven capex were seen supporting growth outcomes ahead. The baseline inflation forecast was of a peak in Q3, matching our forecasts, with fading of the impulse afterwards (Fig 4). Here, inflation was seen as rising on supply side pressures with limited evidence of generalisation so far (FY27 core inflation projected at 4.3%). Supercore measures that are currently mixed (Fig 5) are seen aligning with core inflation by year-end.

Path of rates upward, but first move pushed back with clarity awaited

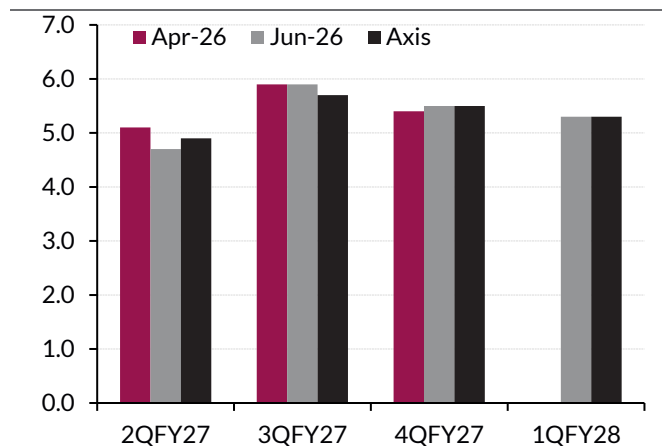
The above inflation forecast of 5.0% for FY27 was with balanced risks. However, language noted risks of second round impact of higher prices. There is some history to this, with WPI impulses feeding into CPI during times of good demand (Fig 6); some evidence is already seen (Fig 7). Stronger nominal growth this year (Fig 8) can also drive second round impulses. The MPC sought clarity on the Monsoon and global factors before acting, though with a mind to **recalibration of rates (upward) given normalisation of hitherto benign inflation**. Higher rates are also reflected in market pricing, with forward OIS pricing in a neutral rate of 6.0% (Fig 9) matching our modelled neutral rate (Fig 10). Current developments suggest Dec as the first potentially live meeting for this.

Liquidity improvement likely to be fleeting, global term premia are a risk to rates

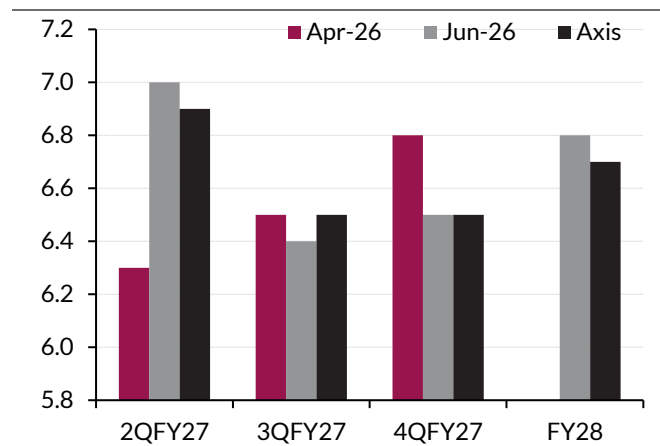
Our own projections of liquidity suggest a near-term hump (Fig 11). Active intervention, resumption of heavy currency note demand (Fig 12), and maturity of short forwards eat into swap inflows. Comments today appeared to confirm this, though language flipped back to providing 'sufficient' vs 'adequate' liquidity. Targeting less easy conditions can pose risks to even residual OMOs, further exposing benchmarks to rising global term premium (Fig 13).

Tanay Dalal

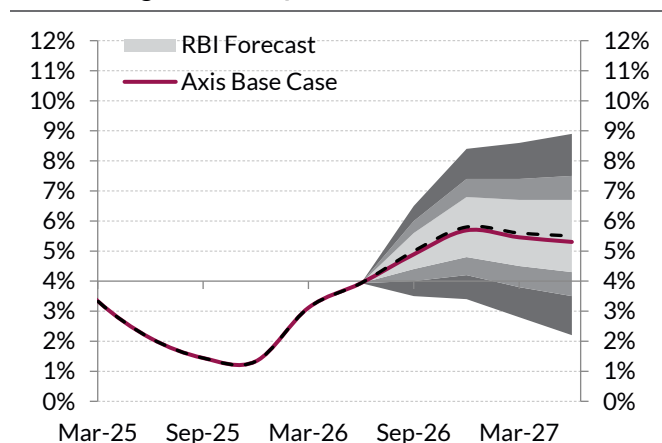
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Exhibit 2 - MPC lowers Q2 inflation projection with softer Q1 trends


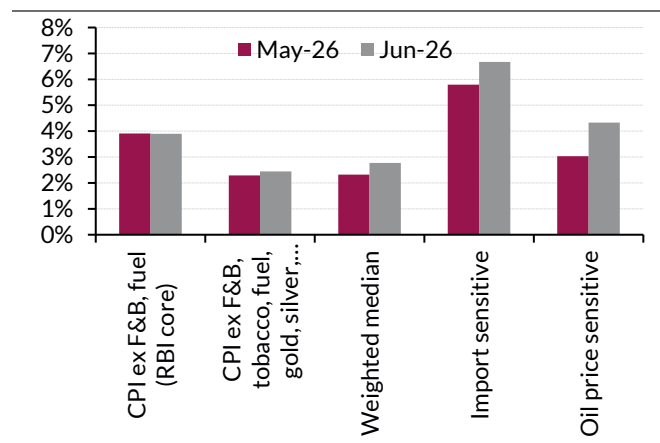
Source: RBI, MOSPI, Axis Bank Research

Exhibit 3 - Stronger high-frequency indicators push up GDP growth


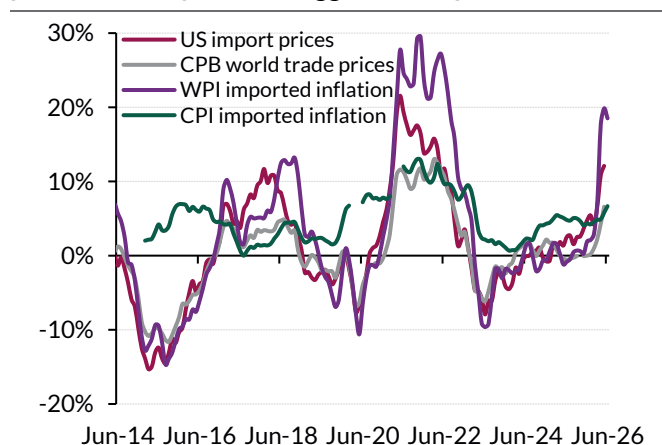
Source: RBI, MOSPI, Axis Bank Research

Exhibit 4 - Our forecasts are aligned with the RBI's some fading after a Q3 peak


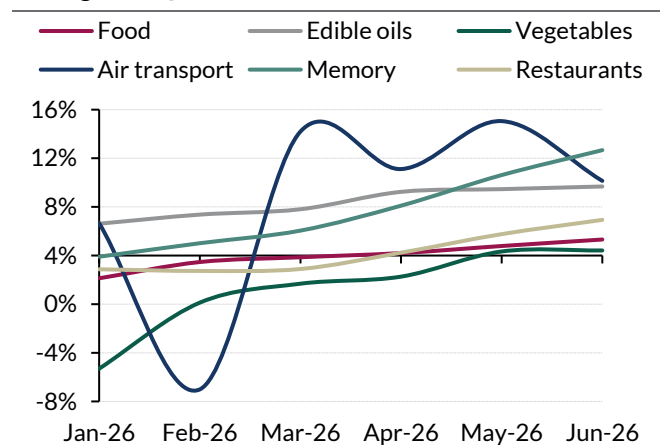
Source: RBI, MOSPI, Axis Bank Research

Exhibit 5 - Supercore inflation measures inching up, but still low


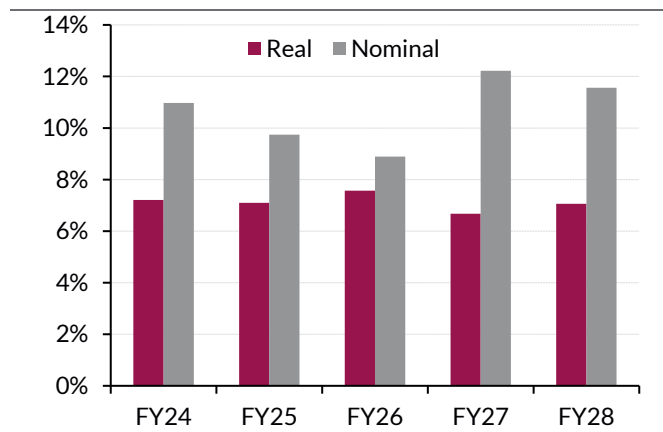
Source: MOSPI, Axis Bank Research

Exhibit 6 - Strong relationship between global traded prices, WPI import, and lagged CPI import inflation


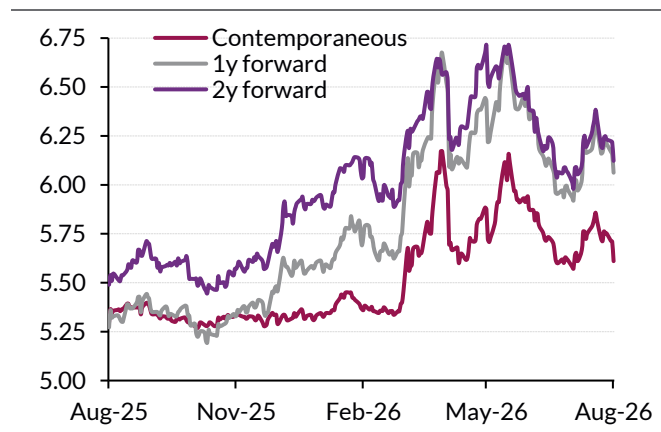
Source: MOSPI, eaindustry, CPB Netherlands, Bloomberg, Axis Bank Research

Exhibit 7 - A number of items are seeing impact from the higher impulse


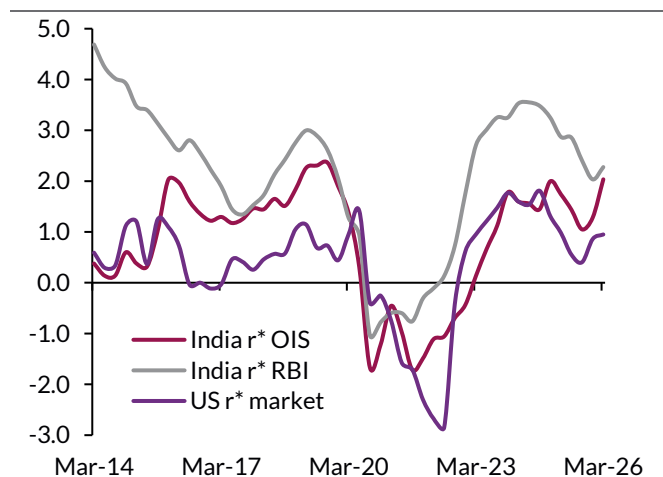
Source: MOSPI, Axis Bank Research

Exhibit 8 - Strong relationship between global traded prices, WPI import, and lagged CPI import inflation


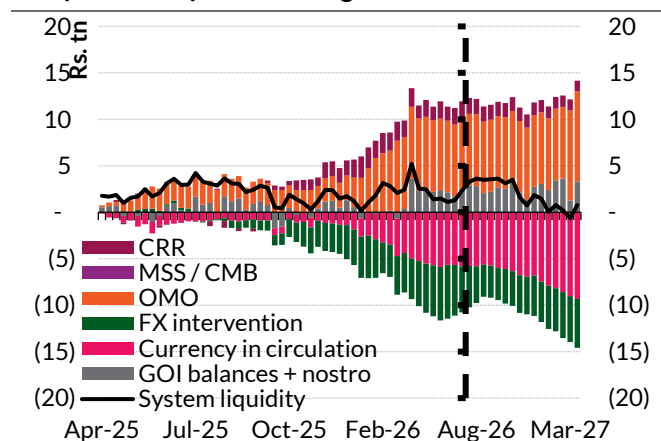
Source: RBI, MOSPI, Axis Bank Research

Exhibit 9 - 1y average rates backed out through OIS - neutral rate of 6.0% priced


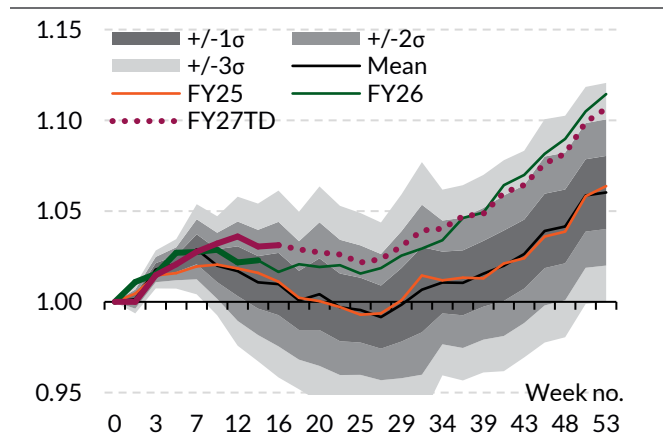
Source: RBI, MOSPI, Bloomberg, Axis Bank Research

Exhibit 10 - Modelled India r^* is at 2%, translating to a 6% nominal with a 4% inflation


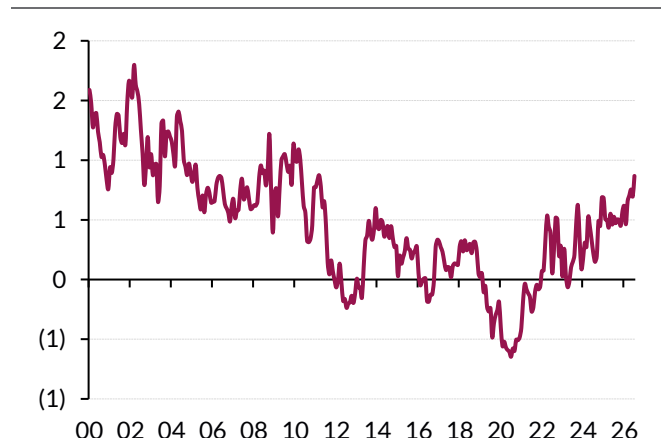
Source: RBI, MOSPI, Bloomberg, Axis Bank Research

Exhibit 11 - Our liquidity projections see a near-term hump with swap flows fading


Source: RBI, Axis Bank Research

Exhibit 12 - Currency in circulation, standardized - high pace so far, to pick up like last year after monsoon


Source: RBI, Axis Bank Research

Exhibit 13 - US 10y zero coupon term premium - has been rising on fiscal, lower forward guidance, QT


Source: RBI, Axis Bank Research

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