AXIS BANK

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Wealth Management | Axis Bank

RBI MONETARY POLICY

OCTOBER 2026

HIGHLIGHTS

MPC Raises Rates; Door Remains Open for Rates Above 6%

- **MPC's Fourth bi-monthly Monetary Policy Review: 2026-27:**
  The MPC unanimously raised the repo rate by 25 bps to 5.50% and shifted its policy stance to calibrated tightening from withdrawal of accommodation, reflecting growing concerns around the inflation outlook and the need to prevent second-round effects from supply-side shocks. The Committee simultaneously revised upward both its inflation and growth projections, highlighting the resilience of domestic economic activity while acknowledging persistent inflationary pressures stemming from a deficient monsoon, elevated commodity prices, volatile crude oil markets and signs of broader price pressures. Importantly, the Governor's statement underscored that rate cuts are off the table in the near term, with future policy action limited to either a pause or further rate hikes depending on evolving growth-inflation dynamics.

- **Policy Actions**
  - Repo rate hiked by 25bps to 5.50%.
  - SDF hiked by 25bps to 5.25% and MSF hiked by 25bps to 5.75%.
  - MPC change the stance to calibrated tightening.

- **RBI & GOI actions:**
  The change in stance and policy communication suggest that the MPC remains prepared to raise rates further.

GROWTH-INFLATION DYNAMICS

- Inflation projections were revised higher, with FY27 CPI inflation raised to 5.2% (vs. Axis Bank Economists estimate of 5.4%), driven by a higher crude oil assumption of USD 95/bbl (from USD 85/bbl), a weaker exchange rate assumption of INR 95/USD (from INR 94/USD), and elevated food prices amid adverse weather conditions. With crude oil prices and the currency already under pressure, the MPC's risk scenarios of an additional 50 bps inflation impact from a 10% rise in oil prices above the baseline and 40 bps from a 5% depreciation in the INR may already be coming into play. While acknowledging these upside risks, the MPC noted that inflation pressures remain largely supply-driven, with limited evidence so far of demand-side pressures or a broader generalisation of supply shocks across the economy.

- FY27 GDP growth projections were revised higher to 7.1% (vs. Axis Bank Economists estimate of 7.3%), reflecting continued resilience in economic activity. The upward revision was supported by positive high-frequency indicators, which point to sustained momentum across key sectors, aided by supportive financial conditions and continued government support that have helped economic activity remain robust despite higher prices. While the MPC acknowledged the strength in the growth outlook, it also highlighted risks on both sides, indicating that the evolving balance between growth and inflation will remain a key consideration for future policy decisions.

LIQUIDITY AND EXTERNAL SECTOR

- The MPC acknowledged the significant surplus liquidity created following the FCNR-related inflows and reiterated its readiness to deploy a range of liquidity absorption tools, including Variable Rate Reverse Repo (VRRR) auctions, open market operations (OMO) sales, and foreign exchange operations, as warranted by evolving liquidity conditions. The Governor indicated that a CRR hike remains the least preferred option, suggesting a preference for using market-based instruments to manage excess liquidity. Given the current macroeconomic backdrop and the available liquidity management toolkit, Axis Bank Economists do not expect the RBI to resort to OMO sales in the near term.

- The policy language continued to express confidence in India's external sector fundamentals, while reiterating the RBI's commitment to ensuring orderly movements in the currency. The Governor indicated that exchange rate adjustments in line with underlying macroeconomic fundamentals would be allowed, even as the RBI remains focused on containing excessive volatility and disorderly market conditions. This balanced approach suggests a preference for gradual and managed currency adjustments rather than defending any specific level, reinforcing Axis Bank Economists view that a measured and smooth INR depreciation remains the most likely path going forward.

POLICY STANCE AND GUIDANCE

- **The shift to a calibrated tightening stance marks a notable departure from the withdrawal of accommodation framework employed during the previous rate-hike cycle and underscores the MPC's heightened focus on inflation risks. While the Committee explicitly ruled out rate cuts in the near term, its communication suggested that the duration and magnitude of further policy tightening will depend on the extent to which current supply-side shocks become generalized, generate second-round inflation effects, and interact with the growth outlook. Importantly, the language signals that the policy rate may not necessarily stop at the estimated neutral level, if inflation risks persist. This interpretation is broadly consistent with market expectations, which are currently pricing in around 100-125 bps of cumulative rate hikes over the next year.**

KEY MEASURES ANNOUNCED BY THE RBI

Measures announced in chronological order in last 1 year.

Date	Measures Announced
February 7, 2025	• Introduction of Additional Factor of Authentication (AFA) for domestic digital payments and proposed to extend AFA to online international digital payments made to offshore merchants. • Proposed to include forward contracts in Government securities to facilitate long-term investors such as insurance funds to manage their interest rate risk across interest rate cycles. • Expand the access of NDS-OM for secondary market transactions in government securities, to non-bank brokers registered with SEBI. • Set-up working group to review of trading and settlement timings across various market segments, report to be submitted by 30th April of this year.
April 9, 2025	• Proposed to enable securitisation of stressed assets through market-based mechanism, in addition to the existing ARC route under the SARFAESI Act, 2002. • Co-lending arrangements are restricted to only priority sector loans by banks and NBFCs to be extended to all regulated entities for all loans. • RBI will introduce standardised guidelines for loans backed by gold jewellery and ornaments across all Res. • New norms will consolidate rules for non-fund based facilities like guarantees, letters of credit, and co-acceptances. • UPI Transaction limits to be made flexible by the NCPI in consultation with stakeholders. • RBI plans to shift the Regulatory Sandbox to an open-ended, theme-neutral format.
August 6, 2025	• Standardisation of procedure for settlement of claims in respect of deposit accounts of deceased customers of banks. • Introduction of Auto-bidding facilities in RBI Retail Direct for Investment and Re-investment in T-bills.
October 1, 2025	• Implementing the Expected Credit Loss framework and revised Basel III norms from April 2027 with glide path till 2031. • Enabling banks to finance corporate acquisitions and expand lending against shares/IPO financing • Easing infrastructure financing norms for NBFCs; considering new licences for urban co-operative banks; rationalising FEMA and ECB rules • Enhancing the consumer protection framework through an expanded Ombudsman scheme and digital banking access for basic accounts • RBI outlined steps to advance internationalisation of the rupee. • RBI proposes to publish a discussion paper on licensing of Urban Co-operative Banks (UCBs). • RBI proposes reforms in insurance premiums and lending limits

KEY MEASURES ANNOUNCED BY THE RBI

Measures announced in chronological order in last 1 year.

Date	Measures Announced
February 6, 2026	• RBI to issue three draft guidelines on mis-selling, loan recovery and recovery agents, and limiting customer liability in unauthorised electronic banking transactions. Proposal to introduce a compensation framework up to ₹25,000 for customers affected by small-value fraudulent transactions. • Collateral-free loan limit for MSMEs proposed to be enhanced from ₹10 lakh to ₹20 lakh. • To support real estate financing, proposal to allow banks to lend to REITs with prudential safeguards. • Proposals for UCBs include higher financial limits on unsecured loans and loans to nominal members, and removal of tenor and moratorium requirements for housing loans by Tier III and Tier IV UCBs. • NBFCs with no public funds and no customer interface, and with asset size ≤ ₹1000 crore, proposed to be exempted from registration. • Proposal to remove the ₹2.5 lakh crore cap on investments via the Voluntary Retention Route (VRR); investments will instead follow category-wise ceilings under the General Route. • RBI proposes to issue regulatory frameworks for derivatives on corporate bond indices and total return swaps on corporate bonds. • Draft revised guidelines to be issued for Authorised Dealer banks and stand-alone primary dealers, providing greater flexibility in foreign exchange transactions.
April 8, 2026	• Proposed to remove the condition regarding NPA provisioning for inclusion of quarterly profits in CRAR computation. • Enhancing the borrowing limit of SPDs in the term money market to non-bank entities
June 5, 2026	• Expanded the universe of securities eligible under the Fully Accessible Route (FAR) to include all new issuances of 15-year, 30-year and 40-year government securities. • exempted FPIs from income tax on interest income and capital gains arising from investments in government securities, effective April 1, 2026. • Facility of concessional forex swap will be provided till 30th September 2026 to incentivize ECBs by PSUs • Facility for bearing the full hedging cost shall be provided till 30th September 2026 to AD banks for raising fresh 3–5-year FCNR (B) deposits. • Proposed to restore the time for realisation of export proceeds to nine months.

IMPACT ON THE MUTUAL FUND INDUSTRY:

- **Liquid Funds**:

  These schemes will continue to generate returns around the operating rate due to their portfolio composition i.e. being invested at the shorter end of the money market segment. Liquid funds have low average maturity as they concentrate more on high quality papers including CPs, CDs and other debt securities with residual maturity of up to 3 months.

- **Ultra Short Term / Low Duration / Money Market Funds (Maturity Up to 1 Year):**

  These schemes predominantly invest in below 1 year maturity paper. The strategy adopted by these schemes is to hold the paper till maturity and capitalize on the running yield. Hence, returns in this category will continue to remain relatively attractive depending on the positioning of the fund.

- **Short Duration Funds**:

  Schemes in this category are predominantly invested in Corporate Bonds, CPs and CDs while a few of them also have some exposure to G-Secs. We continue to remain bullish at the shorter end of the curve. Investors may consider these funds (with an investment horizon commensurate with the maturity profile of such funds) and gain from current accruals and capital appreciation in the event of a fall in yields.

- **Medium Duration:**

  Given the flattened yield curve there are sufficient buffers in the intermediate duration (3-6 years) segment. Till the time RBI is anchoring the long end of the yield curve, the current yield curve may provide some cushion even if there are mark-to-market losses. Investors may consider those funds with high quality portfolios and where the investment horizon is commensurate with the maturity profile of the funds and also gain from current accruals and capital appreciation in the event of a fall in yields.

IMPACT ON THE MUTUAL FUND INDUSTRY:

- **Credit Risk Funds:**

  We remain cautious on Credit Risk Funds as they have failed to prove their mettle in the last 2-3 years with the overhang of defaults and erosions of NAV on the back of mark-to-market impacts due to the aforementioned. The uncertainty around credit funds which are in an open ended avatar continues to pose risks to investors. Much also depends on the liquidity conditions in the market and redemption pressure on these funds. Thus, we think there is a systemic risk in the market within the credit space. Hence, it makes sense for one to stay away from these funds.

- **Long Term Income Funds / Gilt Funds / Dynamic Bond Funds**:

  Indian debt markets entered October on a cautious footing. Expectations of RBI rate hikes, elevated US Treasury yields above 5%, higher crude oil prices, FPI outflows, a weaker rupee and rising inflation pushed the 10-year G-Sec yield higher by around 20 bps to 7.15% during September.

  Global developments remained the key driver of market sentiment. Elevated crude prices amid geopolitical tensions, tighter monetary policy across major economies and increased bond issuance continued to keep global yields elevated. The US dollar strengthened on resilient growth, firmer inflation and a hawkish Fed, while the INR remained supported by RBI intervention despite underlying depreciation pressures.

  On the domestic front, headline inflation remains under control, though uneven monsoon distribution and food inflation warrant monitoring. While reservoir levels and kharif output remain supportive, inflation persistence rather than a sharp spike is the key concern. Fiscal conditions continue to support bonds, aided by strong tax collections, resilient GST revenues, healthy capital expenditure and a lower-than-budgeted borrowing programme. Strong demand from banks, insurers and long-term investors has also supported market stability.

  The RBI has initiated its tightening cycle with a 25 bps repo rate hike to 5.50% and a shift in stance to Calibrated Tightening. While the move was largely anticipated, the focus now shifts to the extent of further policy tightening. Inflation risks from higher fuel prices, global electronics prices and telecom tariff revisions

IMPACT ON THE MUTUAL FUND INDUSTRY:

remain key variables, while OIS markets continue to price in a significant rate hiking cycle.

The key market question is whether the RBI limits the cycle to another 25 bps hike or extends tightening towards 75-100 bps, depending on inflation, crude oil prices, global financial conditions and currency pressures. Liquidity normalization is expected to continue alongside policy tightening, making RBI liquidity operations an important market indicator.

Despite near-term challenges, structural support for bonds remains strong, supported by demand from insurance companies, provident funds, retirement savings and mutual funds, along with fiscal discipline and a manageable government borrowing programme.

Looking ahead, market direction will be influenced by global bond yields, crude oil prices, developments in West Asia, movements in the US dollar and RBI guidance on inflation and liquidity. While the recent policy action may keep yields biased higher in the near term, a significant rise is not the central expectation as markets have already priced in a meaningful portion of the tightening cycle.

In this environment, carry is expected to remain the primary source of returns, while duration should be managed tactically. A preference for low-to-moderate duration portfolios, particularly in the 1-3 year segment, and high-quality sovereign, PSU and corporate issuers remains appropriate. The 10-year G-Sec yield is expected to trade in the 7.20%-7.50% range in the near term.

The 10-year Indian benchmark bond yield rose ~3 bps from the previous close to 6.21% (at the time of writing) and is up ~46 bps since the previous policy.

- **Conservative Hybrid Funds *(Erstwhile: Monthly Income Plans (MIPs)***:

  With a 10% to 25% allocation to equity, returns of CHFs are largely determined by the vagaries of the equity markets as against the debt markets. These funds are therefore suitable for investors who have a reasonably long-time horizon & are comfortable with taking exposure to equities.

OUTLOOK

- While the MPC's communication leaves the door open for further policy tightening if required, Axis Bank Econoists cautious stance on the government securities curve is driven not only by the policy rate outlook but also by evolving market dynamics. Elevated hedging costs are increasingly making domestic borrowing more attractive relative to overseas funding, which could influence demand-supply conditions in local bond markets. At the same time, US Treasury yields remain elevated, while a gradual depreciation of the INR in line with macroeconomic fundamentals remains our base case. Taken together, these factors suggest that bond yields may remain biased higher and volatility could persist. However, the outlook will ultimately be shaped by the trajectory of inflation, fiscal developments and global financial conditions, with future data determining the extent of any further repricing in the rates market.

- **We remain constructive on the shorter end of the yield curve. Short Duration funds, Banking & PSU Debt funds, Corporate Bond funds, Money Market funds, Low Duration funds and Ultra Short Duration** can be considered by investors with an investment horizon commensurate with the maturity profile of the schemes. Investors can consider **tactical allocation in Medium to Long Duration yield curve**, as per their risk appetite with an investment horizon of at least 2-3 years to avoid any intermittent volatility.

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