MIRAE ASSET Sharekhan

Arc Equity

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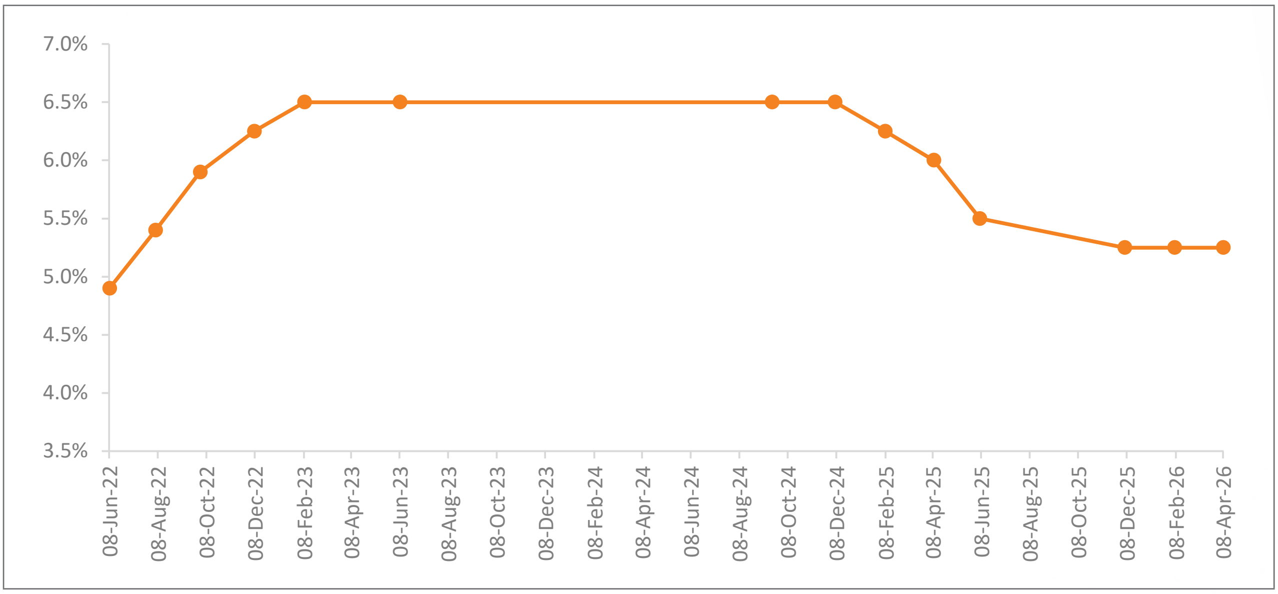
Key Insights | Outlook

Vigilance and proactiveness amid global uncertainties

Repo rate and stance

- The Reserve Bank of India's (RBI's) Monetary Policy Committee (MPC) unanimously decided to keep the repo rate unchanged at 5.25%. Consequently, the standing deposit facility (SDF) rate remains at 5%, and the marginal standing facility (MSF) remains at 5.50%.
- The RBI noted that while headline inflation is contained, upside risks have increased due to increased energy prices and supply disruption amidst West Asia conflict. Hence, the MPC felt that a "wait and watch" approach would be better to monitor the evolving growth-inflation outlook, the MPC retained its neutral stance that will allow to have the flexibility to respond judiciously to incoming information.

Repo rate trend



Source: Mirae Asst Sharekhan Research

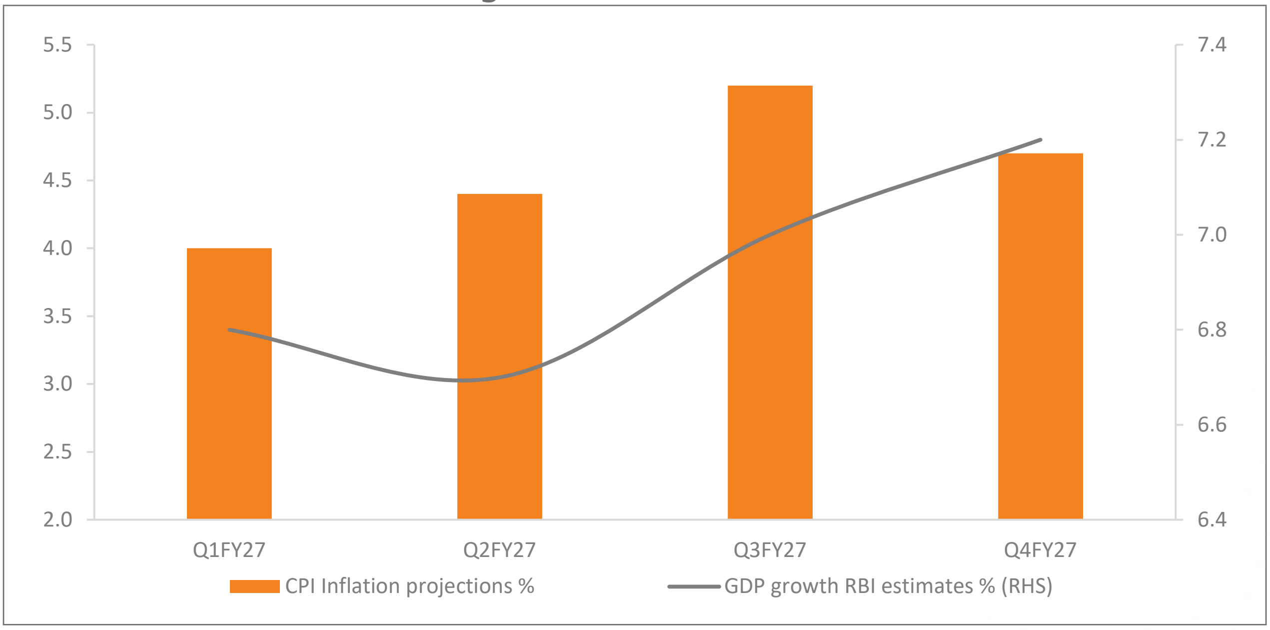
Inflation within targeted limits, but upside risks persist

- The RBI has estimated CPI inflation for FY27 to be at 4.6%, with a quarterly breakdown of Q1 at 4% (unchanged from previous estimates), Q2 at 4.4% (up from 4.2% projected earlier), Q3 at 5.2%, and Q4 at 4.7%. Core inflation for FY27 is projected at 4.4%.
- Upside risk to inflation primarily includes persistently elevated energy and commodity prices resulting from the ongoing conflict in West Asia and volatility in international markets. Additionally, probable weather disturbances, such as possible El Niño conditions, pose a significant upside risk as they could negatively impact the southwest monsoon and disrupt food prices.

Domestic growth and its outlook

- Real GDP growth as per new series for 2026-27 is projected at 6.9% (Q1 at 6.8%, Q2 at 6.7%, Q3 at 7.0%, and Q4 at 7.2%).
- The RBI highlighted several downside risks, including the escalation and geographical spread of the West Asia conflict, potential damage to energy infrastructure, weather-related events and disruptions in the Strait of Hormuz. Furthermore, severe global financial volatility and rising freight and insurance costs from shipping route disruptions could weigh on merchandise exports and growth prospects.
- On the positive side, the RBI pointed that Indian economy remains on a strong footing to withstand shocks, supported by sustained momentum in the services sector, the persistent impact of GST rationalisation, and rising capacity utilisation in manufacturing. Furthermore, robust private consumption, strong investment demand, healthy balance sheets of financial institutions and corporates, and the government's budget focus on scaling up domestic manufacturing provide substantial resilience.

RBI estimates for inflation and growth



Source: Mirae Asst Sharekhan Research

Liquidity and financial stability

- System liquidity has maintained an average daily surplus of Rs. 2.3 lakh crore since the last MPC meeting. Moving forward, the RBI will continue a proactive and pre-emptive approach to liquidity management, ensuring that the banking system has enough liquidity to support the productive requirements of the broader economy.
- Current account deficit (CAD) is projected to remain moderate and at a sustainable level in 2025-26, driven by strong services exports and steady inward remittances. Additionally, recent bilateral and regional trade agreements are expected to benefit the external sector by boosting investment opportunities and diversifying trading partners. However, looking ahead to in FY27, rising global uncertainties and elevated prices for key energy commodities pose upside risks to the deficit.
- The RBI maintains its long-standing policy of allowing the currency exchange rate to be market-determined, without targeting any specific band or level. Only the currency volatility would be managed.

Developmental and Regulatory Measures

- The RBI proposed to remove the condition regarding NPA provisioning for the inclusion of quarterly net profits in computation of Capital to Risk-weighted Assets Ratio (CRAR). Previously, banks could only include these profits if incremental NPA provisions at the end of any quarter did not deviate by more than 25% from the average of the previous four quarters. Hence, benefiting to the banks.
- Commercial banks will no longer be required to maintain an investment fluctuation reserve as an additional buffer against the depreciation of their investments. This requirement is being removed because these banks already maintain a capital charge for market risk as per new norms.
- To facilitate ease of doing business for MSMEs, the RBI proposes to dispense with the requirement of due diligence when onboarding them onto TReDS platforms. This will help MSMEs to manage working capital better and also reduce the compliance burden.

View

The RBI maintains a posture of cautious optimism balanced with strict vigilance. While the global economy faces unprecedented challenges from supply chain disruptions, higher prices, and lower growth driven by geopolitical conflicts, India's domestic macroeconomic fundamentals remain resilient. Overall, the RBI is firmly committed to closely monitoring incoming data and adjusting its neutral stance as necessary to manage the delicate balance of risks. Recent measures on supporting capital adequacy are positive for banks, but at with current levels of inflation, chances of a rate hike are less and as a result interest rate environment would be stable which is positive for rate sensitive sectors like Automobiles, real estate and NBFCs.

SOMIL RAMESH MEHTA

Digitally signed by SOMIL RAMESH MEHTA
Date: 2026.04.08 15:40:27 +05'30'

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Registered Office: 1st Floor, Tower No. 3, Equinox Business Park, LBS Marg, Off BKC, Kurla (West), Mumbai 400 070, Maharashtra, India. Tel: 022-67502000.

Correspondence/Administrative Office Address: Gigaplex IT Park, Unit No 1001, 10th Floor, Building No. 9, TTC Industrial Area, Digha, Airoli-West, Navi Mumbai – 400708. Tel: 022 61169000 / 61150000, Fax No. 61169699.

Registration and Contact Details: Name of Research Analyst - Sharekhan Limited - (AMFI-registered Mutual Fund Distributor), Research Analyst Regn No.: INH000006183. CIN: U99999MH1995PLC087498.

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Compliance Officer: Mr. Joby John Meledan; Tel: 022-4657 3809; email id: complianceofficer@sharekhan.com

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