

RBI to remain watchful

Globally, a lot has changed since the RBI announced its last policy in Feb'26. With the outbreak of Iran war, crisis in the Middle East has become a point of concern. Energy infrastructure of major oil exporting economies has been damaged. Strait of Hormuz is virtually closed. Oil prices continue to hover above US\$ 100/bbl and global central banks are preparing for its impact on inflation. Market also remains highly volatile which has pressurised FPI outflows from India, equity markets, bond yields and INR. Given this backdrop, RBI is likely to announce its full year growth and inflation forecasts keeping in view the impact of war on India. RBI will remain vigilant and hold rates steady for the time being, without changing its stance from neutral. We also believe this to be the end of the rate cut cycle. Further, if oil prices remain above US\$ 100/bbl for consistently long period of time and inflation breaches the upper tolerance band of RBI (6%), then there might be a chance of rate hike by the central bank towards the end of FY27.

What has changed since the last policy?: Since the last policy, world has gone through a period of turmoil, given the ongoing war between US and Iran. Towards the end of Feb'26, US and Israel launched attacks on Iran and since then the war has escalated in the West Asia region. Throughout last month markets remained volatile. The impact of war will be felt on global growth and inflation. India is also likely to get impacted and thus RBI may re-work its GDP and inflation forecasts for FY27.

Expectations from MPC: We expect the RBI to keep the repo rate steady at 5.25% in its Apr'26 policy. The stance is also expected to be maintained at neutral, as the central bank is likely to remain vigilant about the evolving situation. The tone will be more cautious than hawkish. We also believe this to be the end of the rate cut cycle, and RBI will now remain on a prolonged pause. However, there may be measures announced to support liquidity and INR.

Rationale for this decision:

- 1. Global developments:** With the ongoing crisis in the West Asia region, throughout last month global markets have registered significant volatility, and its impact has also been felt by Indian markets. Since the beginning of the war (27 Feb 2026):
 - Oil prices have risen by ~63% to US\$ 118/bbl as of 31 Mar 2026.
 - US 10Y treasury yield has risen by 38bps.
 - India's 10Y G-Sec yield has also gone up by same magnitude (38bps) as of 30 Mar 2026 as it breached the 7% mark—for the first time since early Jun'24.
 - Sensex had fallen by 11.5% in the month of Mar'26 versus 5.5% decline recorded by Dow Jones.
 - INR fell by 4.1% in Mar'26 on MoM basis and closed at record low of 94.83/\$.
 - The impact on currency and equity markets can be explained by foreign fund outflows, which exacerbate during times of stress.
 - NSDL data shows that in Mar'26 (up to 30 Mar), net FPI outflows in equity segment were US\$ 12.7bn and US\$ 0.9bn for. Overall total FPI outflow in Mar'26 was at US\$ 13.6bn.

- However, recently there have been signs of de-escalation of war with Iran, which has led to rally in global stock markets at the start of Apr'26. But in the current situation, it is difficult to gauge whether the relief is temporary or permanent. RBI will also be cognizant of the same.
2. **Domestic growth scenario:** On 27th Feb 2026, Mospi had released latest growth numbers based on new GDP series (base year 2022-23). Accordingly, FY26 GDP growth was estimated at 7.6%, up from 7.1% in FY25 data. Following this, Ministry Finance projected growth in FY27 to range between 7-7.4%. However, in the latest [monthly](#) economic bulletin released, CEA has cautioned that “there is considerable downside to this number...High-frequency data for April and possibly May may give us a better handle on the likely growth rate for the new financial year. Similarly, the current account deficit too will widen significantly in FY27”. RBI will also take note of the evolving situation when it presents its growth projections for the current fiscal year. We expect growth to range between 7-7.2%, accounting for 20-25bps impact on owing to the Iran war.
 3. **Fiscal pressure:** Given the steep rise in international oil prices, margins of OMCs have come under significant pressure as there are efforts being made to protect the consumer from this price shock. As a result, to support the OMCs, central government has reduced special additional excise duty on petrol from Rs 13/lit to Rs 3/lit and on diesel from Rs 10/lit to zero. This may have a sizeable impact on revenues, if the duties are not reversed once oil price situation improves. Our analysis expects duty will not remain in place for the full year and thus impact on fiscal deficit could range between 15-20bps. However, this impact can be cushioned to some extent as the government has also announced increase in export duty for diesel (by Rs 21.5/lit) and ATF (Rs 29.5/lit). Some indirect impact may also be felt through increase fertilizer subsidies and reduction in dividend from oil PSUs. Despite this, we still continue to believe that that fiscal deficit ratio will meet its target for FY27, as the impact of war on central government finances will be short-lived and can be met through rationalisation of expenditure.
 4. **Domestic inflation:** Currently CPI remains below RBI's targeted band at 3.2% in Feb'26 versus 2.7% in Jan'26. As per RBI's own projections CPI in Q1FY27 is estimated to inch up to 4% from 3.2% in Q4FY26 and further to 4.2% by Q2. This is mainly driven by adverse base-effect. However, now given the oil price shock, CPI can register an upside impact of around ~50bps and WPI can register ~100bps impact in FY27. The passthrough is already visible as price of 19kg commercial LPG cylinder has been hiked by over Rs 300 on cumulative basis (1 Mar and 1 Apr 2026). For 5kg cylinder the increase is by Rs 51. Even price of domestic 14.2kg LPG cylinder was hiked by Rs 60 earlier in Mar'26. The price of premium petrol (used in high-end cars and bikes) has been increased by Rs 11/lit. The impact of all this will be felt upon rise in transportation and input costs.
 5. **Banking sector growth:** Bank credit has seen pickup in momentum as it has risen by 13.8% in FYTD26 so far (Apr'25-15 Mar'26) versus 11% growth last year during the same period (till 21st Mar'25). Even deposit growth has improved, registering 10.8% this year so far versus 10.3% last year. As of Feb'26, credit to industries (13.5% versus 7.5%), services (16.3% versus 11.7%),

and personal loan segment (15.2% versus 11.7%)—all have recorded substantial increase compared with last year. Industrial sector has witnessed broad-based growth, with MSME segment taking the lead. Within services, growth is led by computer software, tourism, shipping, aviation, retail trade and commercial real estate segment. Within personal loan, vehicle loan, loans against gold jewellery, and other personal loans were the key drivers.

6. **Transmission of rates:** In measuring how transmission of interest rates as of Feb'26 across different spectrum have fared, the change is taken from Jan'25 just before RBI embarked on the journey of rate cuts.

In case of PSBs, the transmission on fresh term deposits has seen a decrease of 85bps, while on the lending side, WALR has fallen by 75bps. For PVBs the decrease on fresh deposits is lower at 83bps, while that on loans is higher at 104bps.

Table 1. Fresh term deposit and lending rates

Transmission of rates	Jan'25	Nov'25	Dec'25	Jan'26	Feb'26
WADTDR: PSBs	7.06	6.05	6.12	6.18	5.83
WADTDR: PVBs	6.70	5.77	5.85	6.21	5.87
WALR: PSBs	8.59	8.05	7.61	7.75	7.84
WALR: PVBs	10.20	9.44	9.14	9.32	9.16

Source: RBI, Bank of Baroda Research

7. **System liquidity:** On an average, liquidity has remained in surplus since the last policy (6 Feb-30 Mar) at Rs 2.03 lakh crore, but in Mar'26 alone it was lower at Rs 1.52 lakh crore. This was despite RBI injecting Rs 2.36 lakh crore through VRR operations. It is possible that more VRR auctions may be announced for this month to manage the impact on rupee liquidity, as banks will be lowering their NOP-INR position to US\$ 100mn by 10 Apr 2026, as directed by RBI.
8. **Hardening sovereign yields:** Since the last policy, yields on 10Y G-sec have risen by ~39bps and ended FY26 at 7.04% mark, compared with 6.65% before the Feb'26 policy. There are 3 factors which have impacted yields since then. The first is the outbreak of war in the Middle East region. This has impacted energy infrastructure of major oil exporting countries and has also led to closure of Strait of Hormuz (a critical sea route for India to refill oil supplies). The second is cut in excise duty by the central government to support the OMCs. More liquidity easing measures from the RBI will also help bring yields further down. Apart from the direct impact of this on fiscal deficit ratio, there is also risk of indirect impact through possible increase in fertilizer subsidies and decline in dividend received from oil PSUs. The third factor is the impact on domestic inflation that the elevated oil prices will have. Globally, there is now increased probability of major central banks hiking their policy rates by the end of CY26 if the impact of war on inflation becomes permanent. India could also head in the same direction if the war continues for long and oil prices become sticky at over US\$ 100/bbl.

To sum up: We expect RBI to hold policy repo rate unchanged at 5.25% and keep the stance as neutral. We also expect this to be the end of the rate cut cycle and expect a prolonged pause by the central bank. Impact of war on growth and inflation will become clearer in the next 3-4 months. RBI is likely to then take a call on the direction of its rate trajectory. If inflation overshoots its upper band of

tolerance (6%) then there will be a chance of rate hike towards the end of the year. In this policy, measures can be announced to support liquidity and INR.

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For further details about this publication, please contact:

Economics Research Department

Bank of Baroda

chief.economist@bankofbaroda.com