

## India

### RBI on hold; authorities unleash FX support

- The Reserve Bank of India (RBI) kept its policy rate unchanged at 5.25%, in line with expectations. We had expected a pre-emptive 25bp hike, however, RBI chose to amplify its second line of defence measures with more emphatic attempts to attract capital flows.
- RBI revised headline CPI forecasts for FY27 upward to 5.1% YoY from 4.6% while GDP growth was revised down to 6.6% from 6.9%. The external capital flows picture will remain material in the coming months. Past precedence shows that these measures can have material impact on capital flows but does not preclude policy rate hikes.
- We view rate hikes are a matter of time considering that inflation risks remain skewed to the upside and with a greater pass through of retail fuel prices onto headline CPI, second round impacts from inflation could materialise sooner rather than later.
- We expect a cumulative 50bp in hikes in FY27. The risk for more rather than less hikes as price pressures are building not just from energy but also food items.

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The Reserve Bank of India (RBI) kept its policy rate unchanged at 5.25%, in line with expectations and maintained a neutral stance. We had expected a pre-emptive 25bp hike, however, RBI chose to amplify its second line of defence measures with more emphatic attempts to attract capital flows.

### Measures to attract capital flows

Governor Sanjay Malhotra’s statement continued to highlight the downside risks to growth and upside risks to inflation, even after lowering the FY27 GDP growth and raising the headline CPI forecast. The more material announcements, however, were directed towards attracting capital inflows.

The most pertinent of the measures is RBI’s introduction of a facility to fully bear the hedging cost for fresh FCNR-B deposits. This will allow banks to raise foreign currency deposits. Ahead of the RBI’s meeting, it was reported that banks sought some reprieve on hedging costs. This, along with a facility of concessional forex swap to incentivize External Commercial Borrowings (ECBs) by PSUs, could raise significant capital inflows<sup>1</sup>. USD/INR spot moved from 95.67 to 95.02 (at the time of writing) on the back of RBI’s measures. In the press conference following the decision, the RBI Governor was non-committal on assessments of potential inflows. He did, however, note that he expected a “much better BoP”.

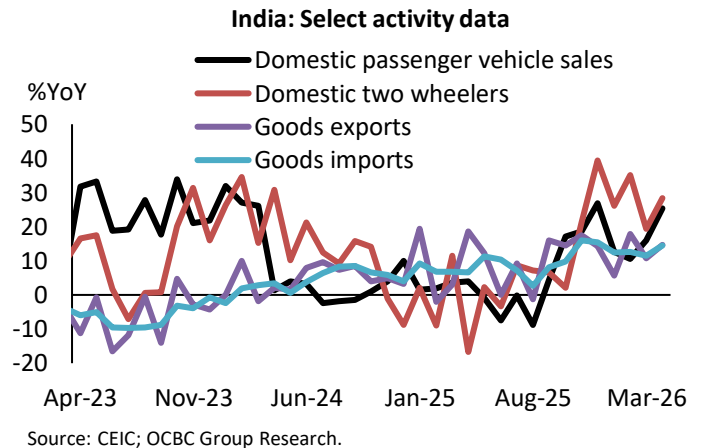
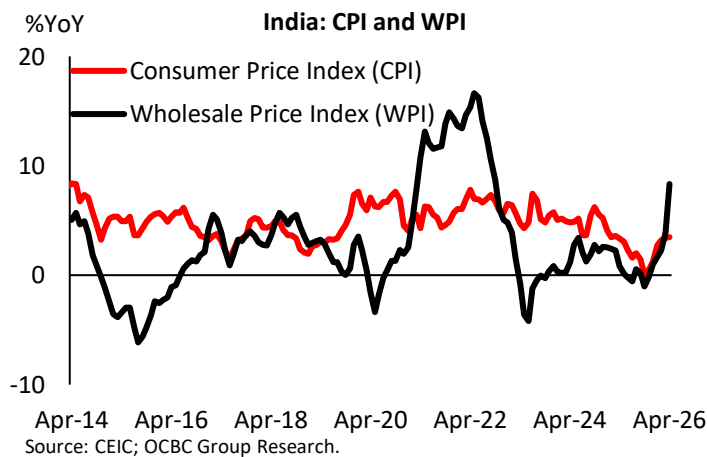
Measures to attract capital inflows	
Measure	OCBC view
First, for government securities under the Fully Accessible Route (FAR), we are expanding the universe of ‘specified securities’ by including all new issuances of 15-, 30- and 40-year tenor G-secs. In addition, limits pertaining to short-term investment, concentration and individual securities on FPI investment under the General Route are being removed.	These measures by RBI were complemented by the government's measures. The government removed the three restrictions, on short-term investment limit, concentration limit and the security-wise limit for investments by foreign portfolio investors in government securities. The quantitative investment limit of 6% of the outstanding stock of the CG securities and 2% of the SG securities is maintained. The Government will also exempt such investments from income tax on any interest or capital gain.
Second, the limits for investment by NRIs and OCIs in equity instruments traded on the stock market without SEBI registration are being increased. Further, the same facility is being extended to all individual Persons Resident Outside India (PROIs) at par with NRIs and OCIs.	The investment limit will be increased for an individual PROI under this scheme from 5% to 10% in any company, with an overall investment limit for all individual PROIs to 24%, from the current 10%.
Third, a facility of concessional forex swap will be provided till 30th September 2026 to incentivize ECBs by PSUs.	This will allow banks to raise foreign currency funds as RBI 'subsidies' the cost of hedging. Reuters reported on 25 May that banks viewed USD50bn could be raised through the concessional forex swap and RBI absorbing the hedging costs.
Fourth, a similar 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.	The FCNR-B facility was previously in place in 2013. NRI deposits from August 2013 until May 2014 were up by USD39.6bn, providing a credible backstop to further backsliding of INR versus USD in that period.
Fifth, it is proposed to restore the time for realisation of export proceeds to nine months.	This has been reduced from 15 months and could require exporters to adjust near-term cash flows.
Source: RBI, Reuters, Indian Express; OCBC Group Research.	

<sup>1</sup> Reuters noted a figure of USD50bn. Indian banks seek hedging cost subsidy from RBI to raise dollar funding, sources say, 25 May 2026, Reuters.

### Capital flow measures do not preclude rate hikes

While sentiment will likely stabilise in the near-term, the growth-inflation-external balance fundamentals will still justify policy rate hikes. The RBI’s statement was clear that inflation risks are to the upside, with the focus is now on second-round effects from higher retail fuel prices. Food inflation risks have also risen considering the “uncertainty about the spatial and temporal distribution of the south-west monsoon and El Niño conditions.”

Moreover, the rise in WPI inflation to 8.3%YoY in April from 3.9% in March underscores pipeline pressures. RBI noted that “prices of several inputs such as commercial LPG, industrial raw materials, chemicals, base metals, rubber, and plastic products, among others, have increased.” During the press conference, the RBI Governor stated that the inflation target range of 2-6% is “sacrosanct”. RBI raised its FY27 headline CPI forecast to 5.1% YoY from 4.6%, which is still within the target range but signs of inflation expectations and prices rising sharply and broadly will trigger a response from RBI.



The neutral stance maintained by RBI is also reflective of the downside risks to growth, in our view. RBI noted that “the rise in prices of energy and other inputs, coupled with supply disruptions, is likely to weigh on economic activity.” It added that “prolonged global supply chain disruptions, volatility in global financial markets, and weather-related shocks continue to pose downside risks to the domestic growth outlook.” That said, incoming data has held up quite strongly. The GDP growth forecast for FY27 was lowered to 6.6% from 6.9%. This, nonetheless, is still robust growth allowing the RBI room to manoeuvre.

While much depends on the situation in the Middle East, our baseline forecast has shifted to expecting a cumulative 50bp in rate hikes from RBI in FY27. These hikes will be aimed at addressing inflationary pressures but will also mitigate external pressures.

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