The Repo Rate and the Policy Stance: Calibrated Tightening

Study/source reference: the Monetary Policy Committee's resolution release: 7 October 2026
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Indian economy: monetary policy and inflation targeting

News Reference:

According to the release of 7 October 2026, the Reserve Bank of India's Monetary Policy Committee (MPC), in its 63rd meeting of 5-7 October 2026, unanimously raised the policy repo rate by 25 basis points to 5.50 per cent. With this, the standing deposit facility (SDF) rate became 5.25 per cent and the marginal standing facility (MSF) rate and the Bank Rate 5.75 per cent. The committee also changed its policy stance from neutral to calibrated tightening.

In the August 2026 meeting, the rate had been kept unchanged at 5.25 per cent and the stance was neutral. According to the October resolution, crude oil saw sharp volatility as the conflict in West Asia flared up again, inflation rose in major economies and the US Fed raised rates by 25 basis points in September.

The policy-rate corridor: MSF and Bank Rate: 5.75%: 25 basis points above the repo: the corridor's upper bound. Repo rate: 5.50%: the policy rate at which banks borrow under the liquidity adjustment facility. SDF rate: 5.25%: 25 basis points below the repo: the corridor's lower bound. **The policy signal is the repo rate in the middle of the corridor.**

What Is the Repo Rate:

The repo rate is the interest rate at which the RBI gives liquidity to banks; banks pledge approved securities in return. This facility comes under the liquidity adjustment facility (LAF). The SDF rate stays 25 basis points below the repo and the MSF rate 25 basis points above it; together these two form the LAF corridor, with the repo rate between them.

When the repo rises, borrowing money from the RBI becomes costlier for banks, so loan rates and EMIs can rise. As loans become costlier, spending and investment fall, demand is damped and pressure on prices eases. The effect travels link by link; not every loan rate or EMI changes immediately.

The Framework of Inflation Targeting:

The 2016 amendment to the RBI Act, 1934 gave flexible inflation targeting a statutory basis. Under Section 45ZA, the central government, in consultation with the RBI, fixes the target every five years on the basis of the Consumer Price Index (CPI). The target is 4 per cent and the tolerance band is 2 to 6 per cent.

In the second review of 25 March 2026, the central government retained the same target and band for the period 1 April 2026 to 31 March 2031. That is, the RBI does not fix the target alone, and it is not permanent either.

The Committee and the Signals Ahead:

The MPC has six members: three from the RBI (including the Governor) and three external experts nominated by the central government. The Governor chairs it and holds the casting vote in a tie. The October 2026 decision was unanimous.

According to the resolution, real GDP growth in the first quarter of 2026-27 was 7.8 per cent, higher than expected; even so, there are signs of price pressure ahead. In August, inflation stayed above 4 per cent in items carrying about 37 per cent weight in the CPI, core inflation stood at 4.2 per cent, and a weak monsoon plus a strong El Nino are risks for food prices.

Prelims: Practice Questions

Question 1. Which is the correct description of the October 2026 MPC meeting's decision?

(a) Repo cut by 50 basis points to 5.00%, stance neutral

(b) Repo raised by 25 basis points to 5.50%, stance calibrated tightening

(c) Repo unchanged at 5.25%, stance neutral

(d) Repo raised by 25 basis points to 5.50%, stance accommodative

View answer and reason
Answer: (b). In the 63rd meeting, a 25 basis-point rise happened unanimously and the stance changed from neutral.

Question 2. With reference to flexible inflation targeting, which statement is correct?

(a) The RBI fixes the target alone and it is WPI-based

(b) Once fixed, the target remains permanent

(c) The central government fixes the CPI target every five years in consultation with the RBI; the 4 per cent target and 2-6 per cent band have been retained from April 2026 to March 2031

(d) The target is 6 per cent CPI and the band 4-8 per cent

View answer and reason
Answer: (c). Under Section 45ZA, the central government fixes the target in consultation with the RBI; the second review happened in March 2026.

Question 3. With reference to the LAF corridor, which statement is correct?

(a) The SDF rate stays 25 basis points above the repo, the MSF 25 basis points below it

(b) The SDF rate stays 25 basis points below the repo, the MSF 25 basis points above it

(c) Both the SDF and MSF rates stay equal to the repo

(d) The corridor is linked not to the repo but to the CRR

View answer and reason

Answer: (b). After the October 2026 decision, the SDF is 5.25% and the MSF and Bank Rate 5.75%.

Sources:

RBI: the Monetary Policy Committee's resolution, 5-7 October 2026

RBI: the monetary-policy framework (overview)