

RBI's October 2025 Policy Shift: Bold regulatory reforms for a resilient future

The RBI's October 2025 policy overhaul focuses on price stability, strengthened Basel norms, AI regulation, and revamped credit frameworks. This shift aims to enhance financial resilience, encourage innovation, and sustain growth

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The Reserve Bank of India (RBI), following its recent monetary policy committee (MPC) meeting in October 2025, has undertaken a transformative shift in its approach to regulations and policy frameworks. This MPC meeting stands out as a turning point due to the substantial regulatory announcements, which have direct implications for India's banking landscape, financial sector stability, and the broader macroeconomic outlook.

The October meeting is considered a “paradigm shift” because, rather than deferring regulatory reform to government panels, including the Financial Sector Legislative Reforms Commission (FSLRC), the RBI is now assuming direct responsibility for proactive regulatory interventions, thereby supporting FSLRC mandates further. This move is both timely and welcome, given the complexity of current global financial markets and the radical technological changes taking place in the financial sector, particularly with the rise of artificial intelligence (AI).

RBI's New Monetary Framework: Prioritizing Price Stability

The RBI officially moved to a new monetary policy framework with the unequivocal primary objective of price stability. This change marks a departure from the earlier multiple-objective approach and shifts towards a more nuanced "dual mandate" of controlling inflation while promoting growth. The RBI has made it clear that, while economic growth is an important consideration, price stability through inflation targeting will be at the core of all decisions. The updated framework

aims for consumer price index (CPI) inflation within a 2–6% range, with a formal target of 4%.

The October 2025 MPC meeting reinforced this stance by holding the repo rate steady at 5.5%, following earlier cuts totaling 100 basis points in 2025 in response to moderating inflation and fiscal reforms. The approach is now unambiguously data-driven and forward-looking, acknowledging global headwinds and a tepid private investment environment, even as government capital expenditure remains robust.

The RBI is keenly aware that anchoring inflation expectations is a prerequisite for creating the confidence necessary for private investments to revive. As of August 2025, inflation stands at 2.07%. The MPC projected inflation and growth at 2.6% and 6.8% for FY26, respectively. This downward revision in inflation from 3.1% reflects easing food and fuel pressures, bolstered by favorable monsoons and supply chain stabilization. The upward GDP tweak from 6.5% signals optimism regarding domestic demand and the revival of capital expenditure (capex). However, quarterly breakdowns (Q1: 7.8%, Q2: 7.0%, Q3: 6.4%, Q4: 6.2%) highlight moderating momentum. These projections underscore the RBI's balanced vigilance, aiming to sustain growth with controlled price pressures amid global uncertainties such as US tariffs and geopolitical tensions.

Basel Norms

The RBI's October 2025 policy announcements also included a reaffirmed commitment to global regulatory standards—specifically, the implementation of revised Basel III capital adequacy norms for commercial banks (excluding small finance, payments, and regional rural banks), effective April 1, 2027.

Basel norms represent a global regulatory framework designed to strengthen bank capital requirements through enhanced risk assessment and more granular capital allocation principles. The RBI's draft guidelines aim to upgrade the Indian banking sector's risk sensitivity, granularity, and resilience. By recalibrating capital charges for credit risk and expanding eligible capital instruments—such as perpetual debt in both foreign and domestic denominations—banks will be better equipped to handle shocks and support global expansions. This move also aligns Indian regulatory practices with international best standards and provides a longer glide path (nearly four years) to ensure that banks adapt to higher provisioning and systemic stability requirements without sudden disruptions.

India's Basel III capital ratios are higher than the global minimum Basel III norms. Under the Basel III framework globally, the minimum capital adequacy ratio (CAR) is 8%, consisting of a common equity tier 1 (CET1) minimum of 4.5%, a tier 1 capital minimum of 6%, plus a capital conservation buffer of 2.5%, totaling 10.5%. To put this in perspective, CET1 capital is the highest quality capital a bank holds, mainly consisting of common shares and retained earnings, which absorb losses immediately as they occur. Tier 1 capital includes

certain preferred stocks, serving as core capital to support a bank's ongoing operations and withstand financial stress.

In contrast, the RBI mandates a higher minimum CAR of 9%, with a CET1 minimum of 5.5% and tier 1 minimum of 7% (excluding buffers). When including the capital conservation buffer of 2.5%, the effective minimum CAR in India rises to 11.5%, and the CET1 requirement goes to 8%. This elevated threshold reflects a more conservative and robust regulatory approach to ensure banking sector resilience.

Expected Credit Loss (ECL) Framework: A Step Forward

For banks operating in India, the adoption of the Expected Credit Loss (ECL) framework marks a significant regulatory reform. The ECL model moves away from the traditional incurred-loss approach to a forward-looking method, requiring banks to provision for possible future losses based on detailed credit risk assessment and broader data signals.

This framework will become operational from April 1, 2027, and is projected to improve the accuracy and timeliness of provisioning. By strengthening the banking sector's resilience to shocks, it is expected to further enhance confidence in the financial system, thereby attracting global capital and lowering borrowing costs for Indian corporates. The RBI's willingness to provide a long adjustment period underscores both its regulatory pragmatism and its commitment to sustained institutional stability.

ECB and Financing Patterns of Corporates

The RBI's October 2025 announcements propose a revamped external commercial borrowings (ECB) framework, easing access to foreign capital by allowing firms to raise up to \$1 billion or 300% of net worth annually—whichever is higher—replacing rigid \$750 million caps. This market-linked approach ties the minimum average maturity to borrower credit ratings, promoting cheaper global funding for infrastructure and expansions while mandating hedging for currency risks.

Amid moderating bank credit (down to 6.5% YoY growth in August 2025), the financing pattern of private corporates is diversifying. RBI data shows that ECB inflows hit \$61 billion in FY25 (up 26% YoY), comprising 14% of total funding, versus 11% in FY24. Bonds surged to 29% of the share, and equity (via IPOs) made up 10%, reducing bank reliance to 49%. This shift enhances liquidity but heightens forex exposure, aligning with RBI's stability mandate.

Looking in detail at the bank credit deployment in 2025, non-food bank credit growth in India moderated, reflecting cautious lending amid global uncertainties and high base effects. RBI data from 41 scheduled commercial banks, covering 95% of non-food credit, shows a 9.9% year-on-year (YoY) increase as of August 22, 2025, reaching ₹166.6 lakh crore, down from 13.6% in August 2024.

Industrial credit slowed to 6.5% YoY (₹38.7 lakh crore) from 9.7%, while services sector lending decelerated to 10.6% (₹48.2 lakh crore) from 13.9%. Personal [loans](#) grew 11.8% (₹54.1 lakh crore) from 13.9%, with vehicle loans at 10.2% and credit card advances at

14.1%. Agriculture credit fell to 7.6% (₹18.9 lakh crore) from 17.7%. MSMEs showed robust growth at 12.4% YoY, supporting economic resilience.

AI and the RBI's Regulatory Sandbox

Artificial intelligence is rapidly transforming financial services, from credit underwriting and fraud detection to risk modeling. Recognizing these potential 'use cases' of AI in central banking, the RBI rolled out its updated regulatory sandbox for AI applications, providing a safe and structured environment for fintechs, banks, and technology firms to test innovations with live customers and real data.

Before the MPC meetings, the RBI introduced its FREE-AI (Framework for Responsible and Ethical Enablement of Artificial Intelligence), a pioneering initiative to integrate AI into India's central banking. Anchored in an enhanced GenAI Digital Sandbox, as outlined in the RBI report, this framework enables fintechs, banks, and technology firms to test AI applications—such as predictive credit underwriting, real-time fraud detection, and advanced risk modeling—with live customer data in a controlled environment. Its 26 actionable recommendations, including fostering indigenous AI to reduce foreign tech dependency, prioritizing data privacy, algorithmic fairness, and cybersecurity, ensure innovation aligns with systemic stability.

Analytically, FREE-AI's strength lies in its dual focus: accelerating AI adoption, projected to add \$500 billion to India's GDP by 2025, while embedding robust risk controls. This contrasts with global approaches. The European Central Bank (ECB), through its May 2024 report and

July 2024 AI Act, emphasizes mitigating systemic risks like model opacity but lacks a testing sandbox, potentially slowing innovation. The U.S. Federal Reserve's AI Program (December 2024) focuses on supervisory AI for regulatory compliance, addressing bias and privacy but with less emphasis on market-driven innovation compared to RBI's outward-looking approach. Singapore's Monetary Authority (MAS), via its 2024 FinTech Sandbox and January 2025 Pathfin.ai initiative (backed by S\$27 million grants), mirrors RBI's experimental ethos, with shared interests in ethical AI governance and cross-border collaborations, such as quantum-AI sandboxes.

By blending ECB and Fed's risk mitigation with MAS's innovation-driven model, FREE-AI positions India as a fintech vanguard. It fosters inclusive growth by ensuring equitable access to AI-driven services while addressing digital divides. Challenges include scalability for smaller firms and stringent enforcement, but RBI's globally aligned framework signals a transformative commitment to ethical AI, balancing financial stability with cutting-edge innovation for India's economic future.

Liquidity Management, Global Headwinds & VRRR

Liquidity management has emerged as a central theme, especially with rising global volatility. The RBI has continued to maintain a 'neutral' stance, ensuring there is sufficient liquidity to cushion against global shocks while avoiding excesses that might stoke inflation or asset bubbles.

A notable change is the discontinuation of the Variable Rate Reverse Repo (VRRR) auctions, a move that underscores the RBI's growing confidence in the domestic liquidity situation and its focus on targeted liquidity management tools. The external context is challenging: new US tariffs, slow recovery in global trade, and ongoing geopolitical conflicts, particularly in the Middle East and Eastern Europe, add uncertainty to export growth and currency stability.

The RBI's forward guidance stresses a cautious path for interest rates—reactive to changing dynamics, but firmly anchored by the sole objective of price stability. The fiscal costs are minimal. Rather the rally in bond markets with long term cut off yield rate down to 6.51% helps in reducing borrowing costs and debt servicing.

To conclude, the October 2025 RBI MPC meeting stands as a watershed moment for monetary and regulatory policy in India. The direct assumption of regulatory reforms by the RBI, away from committee-driven frameworks, signifies a bold and pragmatic approach aligned with the complexities of the modern financial world. By mandating price stability as the sole objective of monetary policy, aligning capital, credit loss, and AI frameworks with global standards, and streamlining business and credit operations, the RBI has laid the foundation for the next phase of India's financial reforms. The ultimate challenge remains the revival of private investment and the full absorption of technological advances and AI, but the RBI as a regulator have set the stage for resilient, inclusive, and innovation-friendly growth.

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