

How a repo-rate change reaches demand

From the Reserve Bank of India's short-term lending rate to commercial bank credit and inflation

Repo Rate & Monetary Transmission

01

1 · RBI provides liquidity

- Repo Rate is the interest rate at which RBI lends short-term funds to commercial banks against securities.
- By contrast, Reverse Repo / SDF is for absorbing bank funds, and CRR is a mandatory cash reserve share.
- Uses a repurchase agreement over eligible government securities to inject short-term liquidity.



02

2 · Funding costs respond

- Raising the repo rate makes short-term central-bank liquidity costlier for commercial banks.
- Policy changes influence money-market rates and banks' financing conditions.
- Lowering the repo rate reduces banks' marginal borrowing cost and signals an easing policy stance.



03

3 · Lending rates adjust

- Commercial banks adjust the interest rates they charge on home, vehicle and corporate loans to the public.
- Transmission speed depends on banking-system liquidity, deposit repricing and credit conditions.
- Do not confuse Repo Rate (RBI to banks) with retail bank loan rates or government small-savings rates.



04

4 · Credit demand responds

- Higher borrowing costs can restrain spending and demand-driven inflation, other things equal.
- Thus the repo rate serves as the Monetary Policy Committee's primary policy rate for inflation targeting.
- Lower borrowing costs can support consumption and investment; the effect is not automatic.

REMEMBER Repo → funding costs → lending rates → credit demand. Transmission takes time and depends on conditions.