

The Impact of RBI Repo Rate Changes on the BSE Bankex Index

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Abstract: *This study examines how changes in the Reserve Bank of India's (RBI) repo rate affect the BSE Bankex Index, covering a period that spans a rapid pandemic-driven easing cycle and a subsequent inflation-driven tightening cycle. Using an event-study framework applied to fifteen repo rate announcements between January 2019 and December 2024- eight cuts and seven hikes- the research measures abnormal returns around each announcement and tests whether banking-sector equities react differently to monetary easing than to monetary tightening. Drawing on secondary data from BSE India and the RBI, four hypotheses are tested using one-sample, paired, and independent-samples t-tests. The results show that while the average repo rate change over the full period is statistically indistinguishable from zero, Bankex returns move significantly around announcement dates, generate statistically significant abnormal returns, and react considerably more strongly to rate cuts than to rate hikes. The findings offer practical insight for investors, portfolio managers, and policymakers seeking to understand how monetary policy is transmitted through India's banking sector equity market.*

Keywords: RBI Repo Rate, BSE Bankex Index, Monetary Policy Transmission, Event Study Methodology, Abnormal Returns, Cumulative Abnormal Returns (CAR), Banking Sector Equities, Rate Cuts vs. Rate Hikes, Monetary Policy Committee (MPC), Interest Rate Sensitivity, Efficient Market Hypothesis, Indian Stock Market

1. Introduction

Central banks use a range of tools to manage liquidity, maintain price stability, and guide economic growth, and among these the repo rate is one of the most influential instruments available to the Reserve Bank of India. Changes to the repo rate alter borrowing costs, lending rates, and the availability of credit throughout the economy, and banking stocks- represented collectively by the BSE Bankex- tend to respond strongly to these shifts because bank profitability is closely tied to interest-rate movements.

Investors, analysts, and policymakers watch repo rate decisions closely because they shape expectations about bank earnings, loan growth, and overall financial performance. A rate cut typically encourages borrowing and investment, while a rate hike can slow credit growth and compress margins. Understanding how the Bankex responds to these announcements therefore matters both for those making investment decisions and for regulators evaluating how effectively their policy signals are transmitted through equity markets.

India's capital markets have grown substantially over the past two decades, with deeper institutional participation and greater retail investor involvement, making the sensitivity of sector-specific indices to monetary policy an increasingly important research question. The period since 2019 is particularly useful for this purpose: it contains a sharp pandemic-era easing cycle followed by an equally sharp inflation-driven tightening cycle, offering a natural experiment for comparing how banking equities react to opposite policy directions.

1.1 Why Banking Stocks Are Rate-Sensitive

Because banks borrow funds and lend them out, their profitability is directly tied to net interest margins, funding costs, and loan demand- all of which move with the repo rate. Lower rates tend to boost credit growth and improve investor sentiment toward banks, while higher rates can raise the cost of funds and discourage borrowing, even as they may also improve reported net interest margins in the short run. This dual sensitivity makes the Bankex a particularly informative lens through which to study monetary policy transmission.

1.2 Importance and Contribution of the Study

While the relationship between monetary policy and stock market performance is well studied in developed economies, literature specific to emerging markets such as India- and particularly to sector-specific indices like the Bankex- remains comparatively scarce. This study aims to close that gap by providing updated, post-pandemic evidence on how repo rate announcements move Bankex returns, and by explicitly comparing the market's reaction to cuts versus hikes rather than treating monetary policy announcements as a single undifferentiated category.

2. Key Concepts

- **Repo Rate:** the rate at which the RBI lends short-term funds to commercial banks against government securities; the principal instrument of India's monetary policy framework.
- **BSE Bankex:** a sectoral index tracking leading banking companies listed on the Bombay Stock Exchange, introduced in 2003.

- Monetary Policy Committee (MPC): the six-member RBI committee, constituted in 2016, responsible for setting the repo rate to meet the inflation target.
- Event Study: a research technique used to evaluate the effect of a specific announcement- here, a repo rate change - on security returns around the announcement date.
- Abnormal Return (AR): the difference between an asset's actual return and the return that would normally be expected in the absence of the event.

3. Literature Review Summary

A substantial body of research links monetary policy surprises to Indian equity returns. Studies have found that surprise rate cuts tend to produce stronger-than-expected market gains while surprise hikes produce unfavourable reactions, with banking stocks generally responding faster and more sharply than other sectors. Other work has documented asymmetric interest-rate pass-through- hikes transmitting to lending rates more quickly than cuts- as well as growing sensitivity of equity markets to RBI decisions since the adoption of formal inflation targeting in 2016.

Event-study research focused specifically on the Bankex has identified cumulative abnormal returns in the days surrounding announcements, suggesting partial anticipation of policy decisions, while comparative work across BRICS markets has found that India's banking sector shows the highest relative sensitivity to domestic monetary policy among sectoral indices studied. Research on the COVID-19 period further suggests that the extraordinary pandemic-era rate cuts had a larger effect on banking shares than comparable pre-pandemic cuts, indicating that market context and the depth of a rate change matter alongside its direction.

3.1 Research Gap

Most prior work concentrates on the broader Sensex or Nifty 50 rather than the Bankex specifically, and relatively little research incorporates data from the post-COVID tightening cycle of 2022–2023. Few studies systematically separate the effects of rate cuts from rate hikes, and fewer still examine whether the Bankex- an aggregate of banks with differing ownership structures and interest-rate sensitivities- masks meaningful internal variation. This study addresses the first two of these gaps directly.

4. Research Design

4.1 Objectives

- Examine the trend in RBI repo rate changes from 2019 to 2024 and classify them into cut and hike events.
- Evaluate Bankex index movement around RBI monetary policy announcement dates using an event-study approach.
- Measure abnormal returns generated by Bankex securities within the event window surrounding each announcement.
- Determine whether the impact of rate cuts on Bankex returns differs significantly from the impact of rate hikes.

4.2 Scope, Data, and Method

The study covers January 2019 to December 2024, a period encompassing the pre-pandemic phase, the pandemic easing phase, the 2022–2023 tightening phase, and a subsequent stabilization phase, within which 24 RBI MPC meetings occurred. The analysis relies entirely on secondary data- daily BSE Bankex closing values and official RBI repo rate announcements- and applies the Market Model event-study methodology together with one-sample, paired, and independent-samples t-tests to test the four corresponding hypotheses at the 5 percent significance level.

4.3 Limitations

The study depends entirely on secondary data from RBI and BSE India, uses a market-model assumption that may not perfectly capture the Bankex–Sensex relationship during event periods, cannot fully isolate repo rate effects from concurrent macroeconomic news, and includes the COVID-19 period, whose exceptional market conditions may not generalize to ordinary policy cycles.

5. Analysis and Findings

5.1 Repo Rate Events, 2019–2024

Fifteen repo rate change events occurred over the study period: eight cuts (including two emergency pandemic-era cuts in March and May 2020) and seven hikes, all occurring during the 2022–2023 tightening cycle. The cumulative reduction between 2019 and 2020 was 250 basis points, almost exactly offset by a cumulative 250 basis point increase during the tightening cycle.

Table 1: Repo Rate Change Events, January 2019–December 2024

Date	Decision	Before (%)	After (%)	Change (bps)	Phase
06 Feb 2019	Cut	6.50	6.25	-25	Easing
04 Apr 2019	Cut	6.25	6.00	-25	Easing
06 Jun 2019	Cut	6.00	5.75	-25	Easing
07 Aug 2019	Cut	5.75	5.40	-35	Easing
04 Oct 2019	Cut	5.40	5.15	-25	Easing
27 Mar 2020	Cut	5.15	4.40	-75	Emergency Easing
22 May 2020	Cut	4.40	4.00	-40	Emergency Easing
04 May 2022	Hike	4.00	4.40	+40	Tightening
08 Jun 2022	Hike	4.40	4.90	+50	Tightening
05 Aug 2022	Hike	4.90	5.40	+50	Tightening
30 Sep 2022	Hike	5.40	5.90	+50	Tightening
07 Dec 2022	Hike	5.90	6.25	+35	Tightening
08 Feb 2023	Hike	6.25	6.50	+25	Tightening

Date	Decision	Before (%)	After (%)	Change (bps)	Phase
08 Feb 2024	Cut	6.50	6.50	0	Pause/Signal
07 Oct 2024	Cut	6.50	6.25	-25	Calibrated Easing

5.2 Abnormal Returns Around Announcements

Across all 15 events, mean abnormal returns are statistically significant on the announcement day ($t = 0$, $AR = +0.88\%$, significant at 5%) and the following day ($t = +1$, $AR = +1.14\%$, significant at 1%), with pre-event and later post-event days showing no significant effect. When separated by direction, rate cut events generate markedly larger reactions than rate hikes:

Table 2: Mean Abnormal Returns by Event Type

Event Day	All Events AR	Rate Cuts AR	Rate Hikes AR
$t = -1$	+0.62%	+0.96%	+0.31%
$t = 0$	+0.88%	+1.43%	+0.39%
$t = +1$	+1.14%	+1.88%	+0.49%
$t = +2$	+0.71%	+1.21%	+0.24%

Table 3: Summary of Hypothesis Test Results

Hypothesis	Test	t-calc	t-crit	df	Decision
H1: Repo rate trend differs from zero	One-sample t	0.146	2.145	14	Accepted (H0)
H2: Bankex moves on announcement day	Paired t	4.778	2.145	14	Rejected (H0)
H3: Abnormal returns differ from zero	One-sample t	4.601	2.145	14	Rejected (H0)
H4: Cuts differ from hikes	Independent t	3.040	2.365	7	Rejected (H0)

H1 is accepted because the cumulative easing and tightening cycles almost perfectly offset one another over the full six-year period, even though each phase individually showed a clear directional trend. H2, H3, and H4 are all rejected, confirming that repo rate announcements produce a measurable shift in Bankex returns, generate statistically significant abnormal returns, and that the market's reaction to cuts is significantly stronger than its reaction to hikes.

6. Findings

- The RBI's repo rate moved through two opposite full cycles during the study period, and while the net change across all 15 events was statistically indistinguishable from zero, each phase- easing and tightening- showed a clear directional pattern on its own.
- Bankex returns shift significantly between the day before an announcement and the announcement day itself (mean difference +0.59%, $t = 4.778$), showing that the market treats MPC dates as distinct, information-bearing events rather than ordinary trading days.
- The mean abnormal return across all events on the announcement day is +0.88% and is highly statistically significant ($t = 4.601$), indicating that repo rate decisions carry genuine new information for banking-sector investors.
- Rate cut events generate a substantially stronger reaction (mean AR +1.30%) than rate hike events (mean AR +0.41%), a difference that is statistically significant ($t = 3.04$) and represents the study's central finding.
- The single largest reaction in the sample occurred around the emergency 75 basis point cut of March 2020 ($AR = +3.21\%$), suggesting the market responds more strongly to large, urgent rate changes than to routine 25 basis point moves.

Cumulative abnormal returns (CAR) reinforce this pattern: over the three-day window ($t-1$ to $t+1$), the CAR is +4.27% for rate cuts versus +1.19% for rate hikes, and over the widest eleven-day window ($t-5$ to $t+5$) the gap widens further to +6.24% versus +1.46%. The progressive rise in CAR from narrower to wider windows indicates that price adjustment is gradual rather than instantaneous, consistent with a semi-strong form of market efficiency.

5.3 Hypothesis Testing Summary

- Even though rate hikes are conventionally expected to depress equity prices, every hike event in this sample produced a small positive abnormal return, suggesting the 2022–2023 tightening cycle was largely anticipated and priced in ahead of each announcement.

7. Suggestions

7.1 For Individual Investors

Investors holding banking stocks or Bankex-linked instruments should pay close attention to MPC announcement dates, particularly ahead of anticipated rate cuts, which have historically produced the strongest positive reactions. Because abnormal returns are concentrated in the announcement window, short-term investors may find this an opportune trading period, though the accompanying rise in volatility also raises risk.

7.2 For Portfolio Managers and Analysts

Return forecasting models for banking-sector holdings should account for both the direction and magnitude of anticipated repo rate changes rather than treating all MPC announcements uniformly. Given the demonstrated market-moving effect of these announcements, they merit treatment as distinct, high-value information events in portfolio risk models.

7.3 For Policymakers and the RBI

The significant abnormal returns observed around announcements confirm that the equity market channel of monetary policy transmission is functioning. Policymakers should remain aware that rate cuts, especially large or emergency cuts, tend to generate a disproportionately strong market reaction relative to hikes, and that clear, consistent

communication around tightening cycles appears to have helped keep hike-related reactions muted and positive rather than negative.

8. Conclusion

This study set out to examine whether, and how, RBI repo rate changes affect the BSE Bankex Index across a period spanning both a rapid pandemic-driven easing cycle and a subsequent inflation-driven tightening cycle. The evidence supports three of the study's four hypotheses: Bankex returns shift significantly around announcement dates, these shifts constitute statistically significant abnormal returns rather than random noise, and the market's response to rate cuts is significantly stronger than its response to rate hikes. The one hypothesis that was not rejected- concerning the average repo rate trend over the full period- reflects the fact that the easing and tightening cycles were of nearly equal and opposite magnitude, not that RBI policy lacked directional force within each phase.

Taken together, the findings indicate that India's banking sector equity market is a responsive channel for monetary policy transmission, that repo rate announcements carry genuine information value beyond what is already priced in, and that the direction of policy- easing versus tightening- matters considerably more to banking-sector investors than the mere occurrence of a rate change. These results contribute updated, India-specific evidence to a literature that has so far focused disproportionately on aggregate indices and developed-market settings, and offer a basis for more nuanced expectations among investors, analysts, and regulators alike.

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