

RBI MPC held policy rate at 5.50%, stance at neutral; inflation forecasts for H1-CY26 hint limited scope for further easing

August 13, 2025

TRUST
In Partnership With Trust

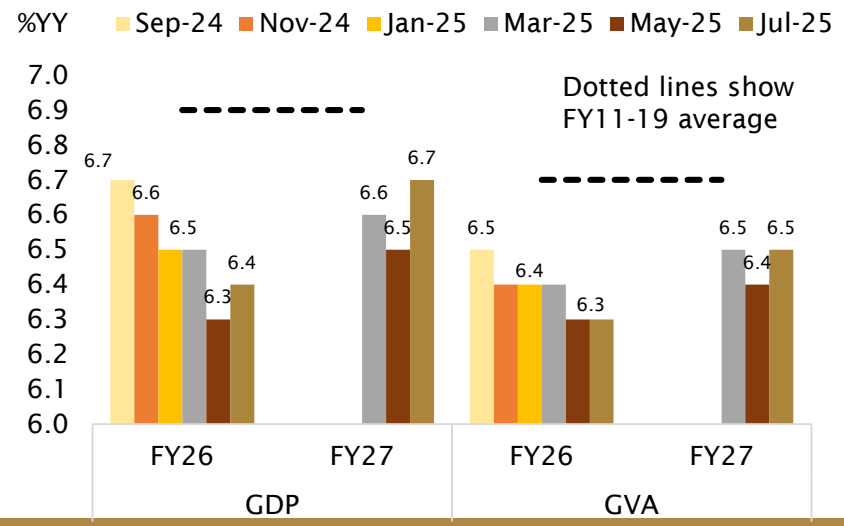
Key takeaways: RBI MPC meeting, August 2025

- At the monetary policy meeting that concluded on 6-Aug-2025, **the RBI MPC held the policy repo rate at 5.50% by a unanimous vote.** Accordingly, the standing deposit facility (SDF) rate was unchanged at 5.25%, and the marginal standing facility (MSF) rate and the Bank Rate at 5.75%. **The MPC also kept the policy stance at 'neutral'.** The policy decisions were largely in line with expectations, though there was a minor section of market participants anticipating a 25bp rate cut.
- The RBI MPC kept real GDP growth forecasts unchanged for FY26 and introduced forecast for Q1-FY27 at 6.6%. The MPC lowered CPI inflation forecast for FY26 to 3.1% from 3.7% projected at the meeting in June, amid downward revisions to forecasts for Q2 and Q3 by 130bps and 80bps, respectively. The MPC introduced inflation forecast for Q1-FY27 at 4.9%.
- **The introduction of CPI inflation forecast for Q1-FY27 at 4.9% implies H1-CY26 average inflation projection at 4.65%. The current policy repo rate at 5.5% further implies the year-ahead ex-ante real rate of 0.85%.** This would be below the 1.5% real neutral rate for the economy that the RBI Governor alluded to in the post policy conference in April and also below the range of neutral rate at 1.4% - 1.9% noted by the RBI in a recent study. Overall, this implies a limited scope for further rate cuts.
- **Even if the MPC were to allow for further easing below the neutral rate, it would highly likely be in a scenario where growth undershoots its estimates by a wide margin in coming quarters.** Hopefully, the lagged impact of domestic monetary, fiscal and regulatory easing will offset some of the negative impact from the ongoing challenging trade negotiations on domestic growth impulses.
- **Going forward, the MPC statement, and also the Governor's comments in the post policy conference suggest that the under the current neutral stance of policy, the MPC will be data-dependent in its policy-making and assess the evolving growth-inflation dynamics and their outlook before taking any further actions.** In that sense, the Q1-FY26 real GDP data due in end-August will be important for the upcoming meeting (Sep 29 – Oct 1), in addition to developments in the ongoing India-US trade talks. **The MPC expects inflation to rise from Q4-FY26 and growth to improve in the coming festive season.**
- In his statement, the Governor stated that an internal working group of the RBI that reviewed its liquidity management framework has recommended **continuation of overnight WACR as the operating target of monetary policy**. Some of the key additional recommendations of the report included:
  - Discontinuation of 14-day VRR/VRRR auctions as the main operation. Instead, transient liquidity to be managed through 7-day repo/ reverse repo operations and other operations of tenors from overnight up to 14-days at the discretion of the RBI based on its assessment of the system liquidity requirement.
  - Continuation of variable rate auction for conducting repo and reverse repo operations under the LAF.

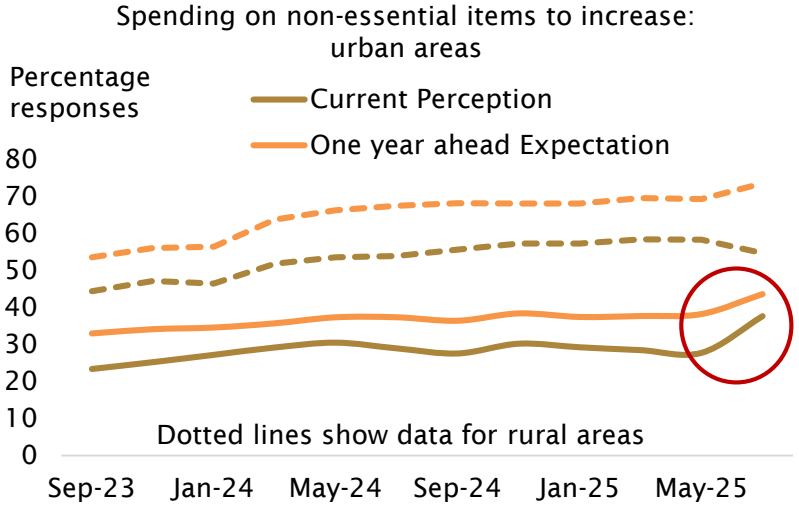
Growth resilient and evolving on expected lines, noted RBI MPC; made no changes to FY26 real GDP forecasts

- The RBI MPC held real GDP growth forecast for FY26 at 6.5% for the third straight meeting amid no changes to quarterly projections, with Q1 at 6.5%, Q2 at 6.7%, Q3 at 6.6%, and Q4 at 6.3%. The MPC introduced Q1-FY27 growth estimate at 6.6%. With growth forecast for Q1-FY27 mildly higher than the average for FY26, the MPC acknowledged resilience in domestic growth, despite it being below aspirational rates. Even as growth continued to evolve along expected lines, the MPC noted ongoing mixed activity signals from demand and supply sides.
- In terms of factors supportive of growth outlook, the MPC noted 1) above normal southwest monsoon and robust rural consumption 2) lower inflation 3) rising capacity utilization 4) congenial financial conditions 5) supportive regulatory, monetary and fiscal policies (including public capex) 6) buoyancy in services sectors.
- The MPC noted factors posing risks to growth, such as 1) subdued and uneven growth in industry 2) tepid urban consumption revival, particularly discretionary spending 3) uncertain impact on external demand from tariff related announcements and trade negotiation challenges 4) headwinds from prolonged geopolitical tensions, global uncertainties (including muted growth outlook), and volatility in global financial markets.
- Post the front-loading of policy easing in June via larger-than-expected repo rate cut of 50bps and staggered 100bp CRR rate cut, there have been upward revisions in median growth forecasts for real GDP for both FY26 and FY27, as per RBI's latest round of survey of professional forecasters (SPF). Also, even as the MPC noted the slack in urban discretionary spending, RBI's latest survey results show an uptick, offering a glimmer of hope.

Latest RBI SPF survey shows higher real GDP forecasts



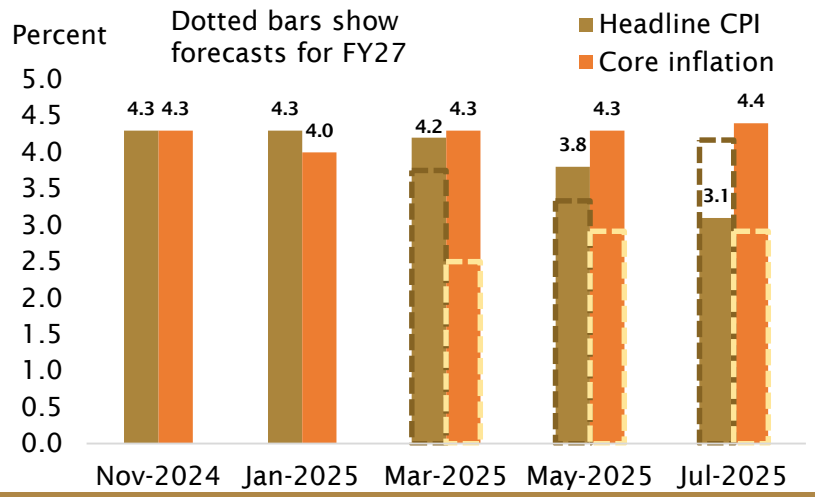
RBI surveys on urban and rural consumer confidence



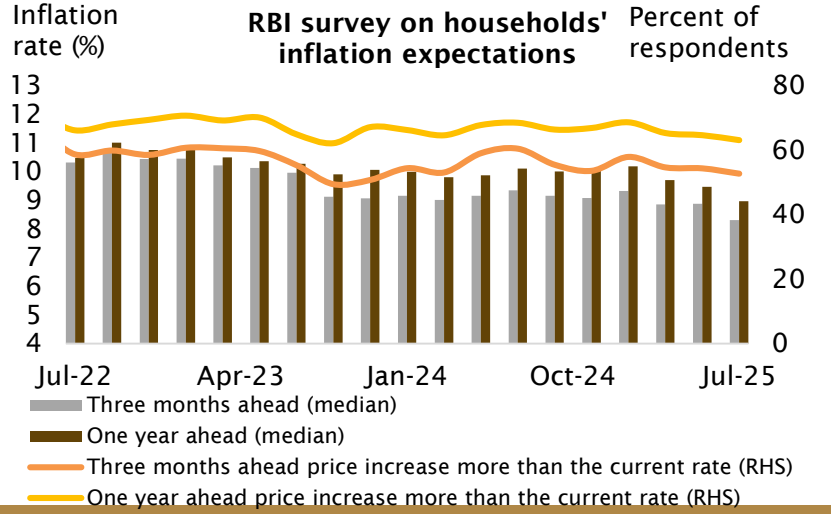
RBI MPC cut FY26 inflation estimate but underplayed ongoing disinflation by highlighting the role of volatile food prices

- The RBI MPC lowered its CPI inflation forecast for FY26 for the third successive meeting to 3.1% from 3.7% in the previous meeting amid cuts to quarterly projections with Q2 at 2.1% (-130bps), Q3 at 3.1% (-80bps), and Q4 at 4.4%. The forecast for Q1-FY27 was introduced at 4.9%, taking the H1-CY26 estimate to 4.65%.
- The MPC noted factors supporting the ongoing disinflation and improved outlook for FY26, such as 1) favorable base effects 2) progress of the southwest monsoon 3) healthy Kharif sowing 4) adequate reservoir levels 5) comfortable buffer stocks of food grains 4) deflation in food in June, driven by vegetables, pulses and cereals.
- The MPC acknowledged that headline inflation is expected to breach 4% in Q4-FY26 and beyond due to 1) unfavorable base effects 2) demand pull factors from past policy actions to spur growth 3) risks from weather-related shocks. The MPC somehow underplayed the ongoing disinflation by emphasizing the role of food group, particularly vegetables, in which inflation tends to be volatile. This point was reiterated by the Governor in the post policy conference. Another fine print in the foot notes to the Governor's statement that hinted a hawkish tint was the rise in core inflation to 4.4% in June after being steady between 4.1% - 4.2% in Feb-May.
- Even as households' inflation expectations remain broadly anchored, details show increases in expectations for services and household durables. Results of the RBI's latest consumer surveys show an increase in respondents in urban areas expecting inflation to rise, both current and one-year ahead. On the bright side though, the first round pass-through effect of global risks to domestic CPI inflation is expected to be muted, as also noted by Deputy Governor Poonam Gupta in the post policy conference.

SPF median CPI inflation forecasts for FY26



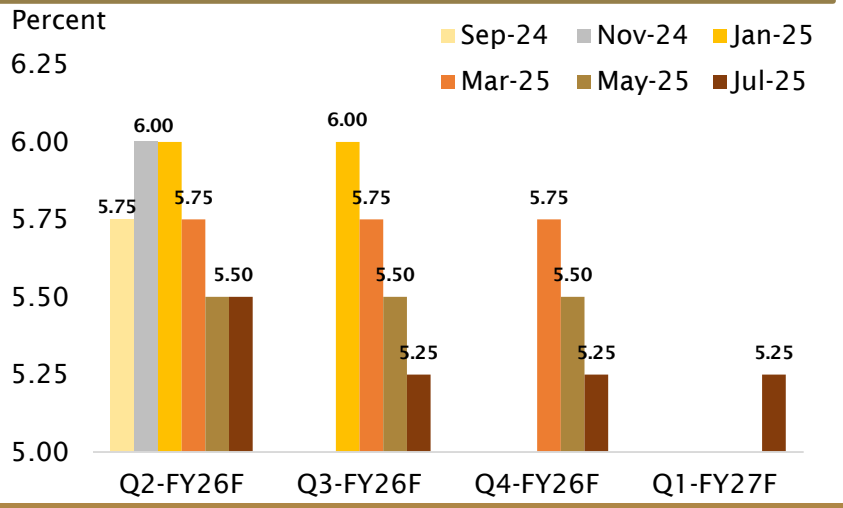
RBI survey on households' inflation expectations



H1-CY26 inflation estimate at 4.65% raises the bar for further easing; MPC to remain data-dependent in decision-making

- **Limited space for further easing:** Though these words were not retained from the previous policy statement, inflation projections for H1-CY27 do imply higher bar for further easing. The introduction of CPI inflation forecast for Q1-FY27 at 4.9% implies H1-CY26 average inflation projection at 4.65%. The current policy repo rate at 5.5% further implies the year-ahead ex-ante real rate of 0.85%. This would be below the 1.5% real neutral rate for the economy that the RBI Governor alluded to in the post policy conference in April and also below the range of neutral rate at 1.4% - 1.9% noted by the RBI in a recent study.
- Even if the MPC were to allow for further easing below the neutral rate, it would highly likely be in a scenario where growth undershoots its estimates by a wide margin in coming quarters. Hopefully, the lagged impact of domestic monetary, fiscal and regulatory easing will offset some of the negative impact from the ongoing challenging trade negotiations on domestic growth impulses.
- **Data-dependent approach:** Going forward, the MPC statement, and also the Governor's comments in the post policy conference suggest that the under the current neutral stance of policy, the MPC will be data-dependent in its policy-making and assess the evolving growth-inflation dynamics and their outlook before taking any further actions. In that sense, the Q1-FY26 real GDP data due in end-August will be important for the upcoming meeting (Sep 29 – Oct 1), in addition to developments in the ongoing India-US trade talks. The MPC expects inflation to rise from Q4-FY26 and growth to improve in the coming festive season.
- **Liquidity management:** In terms of keeping a vigil on incoming economic data, the MPC will also monitor impact of ongoing transmission of the front-loaded rate cuts to the broader economy. In his statement, the Governor noted that comfortable liquidity conditions were enabling transmission of policy easing to the money, bond and credit markets. The Governor stated that the RBI will remain nimble and flexible in its liquidity management, and maintain sufficient liquidity in the banking system.
- **Flow of resources to the economy:** In his statement, the Governor noted that though bank credit growth eased in FY25, overall flow of resources to the commercial sector rose year-on-year, and the trend continues, as large corporates increasingly rely on market-based instruments to source funds, including their internal resources.

SPF median forecasts show 5.25% as terminal repo rate

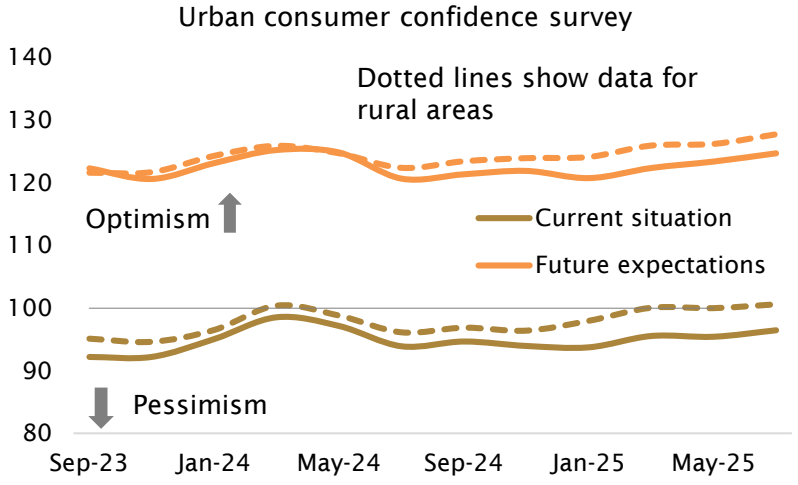


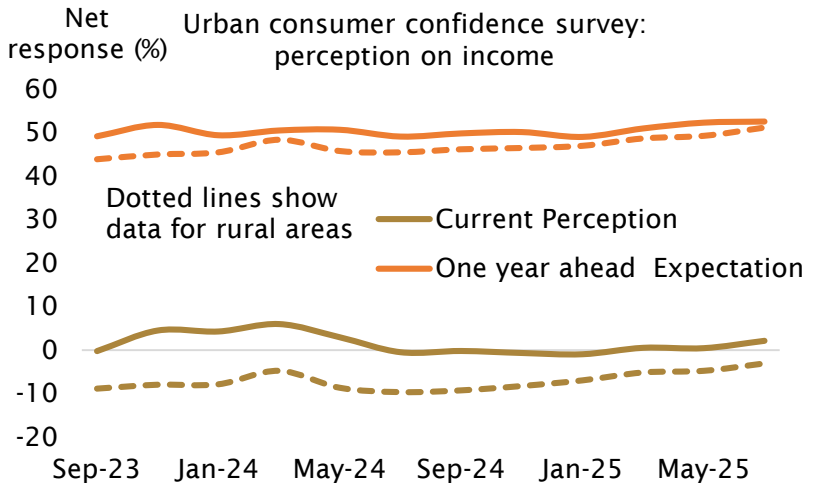
Excerpts from recommendations of the Internal Working Group that reviewed the Liquidity Management Framework

Key notes from the report by the RBI's internal working group that reviewed its liquidity management framework.

1. The overnight Weighted Average Call Rate to continue as the operating target of monetary policy.
2. Continuation of the existing corridor system with policy repo rate at the middle of the corridor. The corridor would remain symmetric, with SDF and MSF, which are 25 bps on either side of the policy repo rate, acting as the lower and upper bounds of the corridor system, respectively.
3. Discontinuation of 14-day VRR/VRRR auctions as the main operation. Instead, the transient liquidity to be managed primarily through 7-day repo/ reverse repo operations and other operations of tenors from overnight up to 14-days at the discretion of the RBI based on its assessment of liquidity requirement.
4. To reduce uncertainty in the market about the tenor, quantum and timing of the repo/reverse repo operations, the RBI would need to provide sufficient advance notice to market participants, at least by one day, while conducting any such liquidity operation.
5. In situations where the evolving liquidity conditions warrant conduct of liquidity operations on the same day of announcement, the RBI may conduct repo/reverse repo operations announced on the same day.
6. Continuation of variable rate auction for conducting repo and reverse repo operations under the LAF.

Additional insights from latest RBI surveys: Even as headline rural confidence stayed above that of urban consumer, details on urban consumer confidence showed either an improvement or stayed higher than that of rural counterparts, particularly for discretionary spending (chart on slide 3) and income (chart below).





DISCLAIMER:

We are committed to providing completely independent views to help our clients reach a better decision. This document is provided for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Nothing in this document should be construed as investment or financial advice, and nothing in this document should be construed as an advice to buy or sell or solicitation to buy or sell the securities of companies referred to in this document. The intent of this document is not in recommendary nature. The recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. Trust Group has not independently verified all the information given in this document. Accordingly, no representation or warranty, express or implied, is made as to the accuracy, completeness or fairness of the information and opinions contained in this document. The Company reserves the right to make modifications and alternations to this statement as may be required from time to time without any prior approval. Trust Group, its affiliates, their directors and the employees may from time to time, effect or have effected an own account transaction in, or deal as principal or agent in or for the securities mentioned in this document. They may perform or seek to perform investment banking or other services for, or solicit investment banking or other business from, any company referred to in this report. Each of these entities functions as a separate, distinct and independent of each other. The recipient should take this into account before interpreting the document. This report has been prepared on the basis of information, which is already available in publicly accessible media or developed through analysis of Trust Group. The views expressed are those of analyst and the Company may or may not subscribe to all the views expressed therein. Neither the Firm, not its directors, employees, agents or representatives shall be liable for any damages whether direct or indirect, incidental, special or consequential including lost revenue or lost profits that may arise from or in connection with the use of the information. This document is being supplied to you solely for your information and may not be reproduced, redistributed or passed on, directly or indirectly, to any other person or published, copied, in whole or in part, for any purpose.

Copyright in this document vests exclusively with Trust Group.

Trust Group
1101, Naman Centre, Bandra Kurla Complex, Bandra (E), Mumbai -400 051, Maharashtra.
Ph: +91 22 4084 5000 • Fax: +91 22 4084 5052 • www.trustgroup.co.in