



ICRA COMMENTS ON RBI'S 2nd BI-MONTHLY MONETARY POLICY MEETING FOR 2025-26

Reversal in policy stance to neutral,
unexpected CRR cut of 100 bps and front-
loaded 50-bps repo rate cut foretell a
pause in policy easing cycle

JUNE 2025



HIGHLIGHTS



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The MPC has upfronted repo rate cut of 50 bps in the June 2025 policy with a vote of 5:1.

The FY2026 CPI inflation forecast was pared by 30 bps to 3.7%, whereas the GDP growth projected was retained at 6.5%, in line with April 2025 policy.

Change in policy stance back to neutral and the surprise move of a 100-bps reduction in CRR appears a strong signal for a pause. ICRA expects a status quo on rates in August 2025 policy.

The Monetary Policy Committee's (MPC) second bi-monthly meeting for FY2026 was filled with surprises, including the front-loading of repo rate cut of 50 bps to 5.50% (against the consensus forecast of 25 bps cut), change in policy stance back to neutral from accommodative, and the 100-bps reduction in cash reserve ratio (CRR) to 3.00% of net time and demand liabilities (NDTL) in a staggered manner from early-September 2025. The latter is expected to inject durable liquidity to the tune of Rs. 2.5 trillion by December 2025 during the busy season and also aid in monetary transmission. While the decision of a 50-bps rate cut was non unanimous, with one of the six members voting for a 25-bps cut, the policy document did not provide any voting pattern on policy stance. The CPI inflation forecast for FY2026 was pared by 30 bps to 3.7% (ICRA P: +3.5%), owing to a large downward revision in H1 print, although the GDP growth projection for the fiscal was maintained at 6.5% (ICRA P: +6.2%). In ICRA's view, the change in policy stance back to neutral combined with a surprise CRR cut appears a strong signal for a pause. We expect the rates to be unchanged in August 2025 policy meeting.

- In the second bi-monthly monetary policy for FY2026, the MPC delivered a frontloaded repo rate cut of 50 bps to 5.50% under the liquidity adjustment facility (LAF) with a majority vote of 5:1. Accordingly, the standing deposit facility (SDF) rate was reduced to 5.25%, and the marginal standing facility (MSF) rate and the Bank Rate at 5.75% each. Moreover, it 'decided' to change the monetary policy stance back to neutral from accommodative. In addition, the RBI has announced a phased CRR cut of 100 bps to 3.00% of NDTL, which would inject durable liquidity of Rs. 2.5 trillion by December 2025.
- The benign near-term outlook for inflation reinforces confidence of durable alignment of headline inflation with the target of 4%, with likely undershooting of the target during the course of the year. Assuming a normal monsoon, the Committee revised its inflation expectation for FY2026 downwards to 3.7% from 4.0% projected earlier in April 2025. Besides, it has pared the CPI inflation projection for Q1 FY2026 (+2.9% in June 2025 vs. +3.6% in April 2025) and Q2 FY2026 (+3.4% vs. +3.9%) by 50-70 bps. While the projection for Q3 FY2026 (+3.9% vs. +3.8%) was slightly revised upwards, that for Q4 FY2026 was kept unchanged at 4.4%.
- The Committee expects the domestic private consumption and investment to improve in FY2026, although spillovers from geopolitical tensions, weather-related uncertainty, global trade pose downside risks to growth. Overall, it has maintained the annual GDP growth forecast for FY2026 at 6.5%, with Q1 FY2026 at 6.5%, Q2 FY2026 at 6.7%, Q3 FY2026 at 6.6% and Q4 FY2026 at 6.3%, in line with the levels indicated in April 2025.

Outlook: The upfronting in rate cuts along with the change in the policy stance, appears to be a fairly strong signal of an end to the current easing cycle, given the clear messaging in the April 2025 meeting that the stance is meant to provide forward guidance on policy rates. This suggests that we are most likely looking at a pause in the next meeting in August 2025, unless inflation-growth numbers differ materially from what the MPC has set out. While the bond markets reacted favourably to the policy decisions at the outset, the change in stance subsequently pushed up yields. We believe that a cumulative cut of 50 bps was largely priced in, and the only surprise was the frontloading. Looking ahead, we expect the 10-year yield to trade between 6.20%-6.40% in the remainder of the calendar year, unless expectations crystalise around another rate cut. In that case, the 10-year yield could ease to as low as 6.0%.

Higher than our expectation of 25 bps, the MPC reduced the repo rate by 50 bps to 5.50% from 6.00%, with a 5:1 majority; it also decided to change the monetary policy stance to neutral from accommodative.

Going ahead, the Committee expects food inflation to remain benign, amid healthy rabi production, upbeat outlook for Kharif crops, as well as declining crude oil prices. Nevertheless, global uncertainties, adverse weather events pose upside risks.

MPC WITH A 5:1 MAJORITY REDUCED REPO RATE BY 50 BPS TO 5.5% IN JUNE 2025; CHANGED STANCE TO NEUTRAL

In its second bi-monthly monetary policy meeting for FY2026, the MPC decided to frontload rate cuts with a 5:1 majority, reducing the policy repo rate under the LAF by 50 bps to 5.50% from 6.00% (refer Exhibit 1), higher than ICRA's expectation of 25 bps rate cut. This translates to cumulative rate cuts of 100 bps during February-June 2025. Accordingly, the SDF rate stands adjusted to 5.25%, and the MSF and Bank Rate at 5.75% each. Besides, to ensure adequate durable liquidity in the system and support monetary transmission, the Committee surprisingly reduced the CRR by 100 bps to 3.00% of NDTL in a staggered manner between early-September 2025 and end-November 2025. While the MPC continued to accord a higher weight on growth vis-à-vis inflation, it changed the monetary policy stance back to neutral from accommodative, highlighting very limited space left with monetary policy to support growth, going forward.

MPC expects CPI inflation to ease to 3.7% in FY2026: The year-on-year (YoY) CPI inflation continued its downward trajectory in the recent months, with the CPI inflation moderating to a 69-month low of 3.2% in April 2025 vs. 3.3% in March 2025, amid the continued compression in food and beverage (F&B) inflation (that witnessed the sixth consecutive monthly decline to +2.1% in April 2025 from 2.9% in March 2025; the lowest reading since October 2021), particularly driven by vegetables. Notably, the core-CPI inflation (CPI excluding food and beverages, fuel and light, and petrol and diesel indices for vehicles) largely remained steady, marginally inching up to 4.4% in April 2025 from 4.3% in March 2025, despite the slightly lower pressure from gold (to +30.9% from +34.1%).

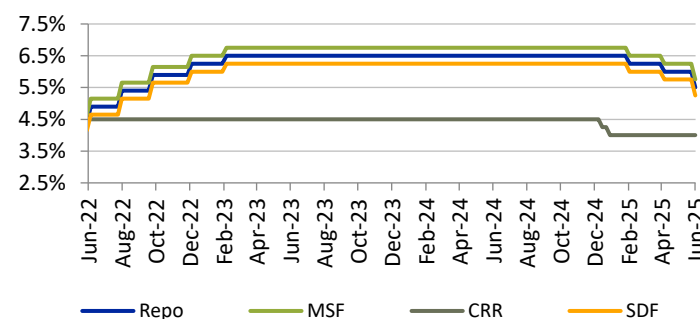
Going ahead, the MPC expects food prices to remain benign owing to the record wheat production as well as higher production of key pulses in the rabi crop season ensuring adequate food supply. This coupled with an early onset of South-west monsoon (eight days prior than the normal onset date of May 30), and expectation of above-normal rainfall in 2025 augurs well for kharif crop prospects. Additionally, the decline in inflation expectations for the three-month and one-year ahead periods would also anchor inflation expectations. Besides, the sharp fall in crude oil prices augurs favourably for the inflation trajectory. Nevertheless, weather-related supply disruptions and global uncertainties arising from US tariff-related policies and the consequent impact on imported inflation continue to pose an upside risk to the overall inflation outlook. Taking these factors into consideration and assuming a normal monsoon, the Committee revised its inflation expectation for FY2026 downwards to 3.7% from 4.0% projected earlier in April 2025. Notably, it has pared the CPI inflation projection for Q1 FY2026 (+2.9% in June 2025 vs. +3.6% in April 2025) and Q2 FY2026 (+3.4% vs. +3.9%) by a sizeable 50-70 bps. While the projection for Q3 FY2026 (+3.9% vs. +3.8%) was revised upwards slightly, that for Q4 FY2026 was kept unchanged at 4.4%. This implies a linear upward trajectory in inflation through the fiscal.

ICRA expects the CPI inflation to ease to 3.5% in FY2026 from 4.6% in FY2025, lower than MPC's revised forecast of 3.7%. While the prints for the first two quarters are broadly aligned with our expectations, we believe that those for the second half of the fiscal could somewhat undershoot the MPC's projections. In our view, the change in stance back to neutral appears to be a strong signal of a pause, especially when combined with the unexpected CRR cut. As of now, we expect rates to be unchanged in the August 2025 policy review.

The MPC pared its CPI inflation projection to 3.7% in FY2026 from the earlier estimate of 4.0%.

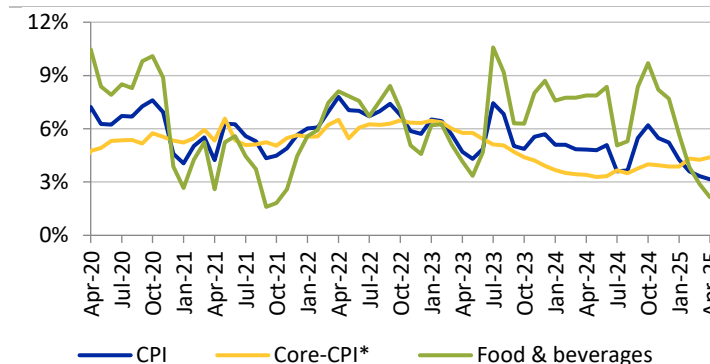
The Committee has revised its inflation projection for Q1-Q2 FY2026 downwards by 50-70 bps, relative to April 2025; the forecast for Q3 has been raised by 10 bps, while that for Q4 has been kept unchanged at 4.4%. This implies a linear upward trajectory in inflation through the fiscal.

EXHIBIT 1: Movement in Key Rates



Source: RBI; CEIC; ICRA Research

EXHIBIT 2: CPI Inflation, CPI-food and core-CPI inflation (YoY)



*Due to unavailability of data for March-May 2020, we have not excluded petrol and diesel indices for vehicles in computation of core CPI index for these months;
Source: NSO; CEIC; ICRA Research

EXHIBIT 3: RBI's earlier and current GDP growth and CPI inflation forecasts

YoY (%)	CPI Inflation*		GDP Growth (at constant 2011-12 prices)	
	April 2025	June 2025	April 2025	June 2025
MPC Policy Reviews				
Q1 FY2026	3.6%	2.9%	6.5%	6.5%
Q2 FY2026	3.9%	3.4%	6.7%	6.7%
Q3 FY2026	3.8%	3.9%	6.6%	6.6%
Q4 FY2026	4.4%	4.4%	6.3%	6.3%
FY2026	4.0%	3.7%	6.5%	6.5%

*Assuming a normal monsoon in FY2026; Source: RBI; ICRA Research

The Committee expects economic activity to maintain the momentum in FY2026, aided by domestic private consumption and fixed capital formation.

However, spillovers stemming from geopolitical tensions, global trade and weather-related uncertainties pose downside risks to growth.

Taking all these factors into consideration, the MPC has maintained its FY2026 GDP growth forecast at 6.5%.

The quarterly growth projections for Q1 (+6.5%), Q2 (+6.7%), Q3 (+6.6%) and Q4 (+6.3%) FY2026 have been retained at the levels indicated in April 2025.

Q4 FY2025 GDP growth at 7.4%, overall expansion slowed to 6.5% in FY2025: At end-May 2025, the NSO pegged the GDP growth for Q4 FY2025 at stronger-than-expected 7.4%, while the GVA growth was placed at relatively lower 6.8%, amid the surge in net indirect tax growth (at 4-quarter high 12.7% in Q4 from 5.0% in Q3). Nevertheless, manufacturing (at +4.8%), construction (at +10.8%), financial real estate and professional services (FRP: at +7.8%), and public administration, defence and other services (PADOS: at +8.7%) logged a higher pace of growth, relative to our projections. Amid an upward revision in the Q3 print, GDP growth has been placed at 6.5% for FY2025, in line with the National Statistical Office's (NSO's) second advance estimate.

MPC retained its FY2026 GDP growth forecast at 6.5%: The Committee highlighted that the agricultural prospects remain bright, on the back of an above-normal monsoon forecast, early onset of rainfall and resilient allied activities, thereby auguring well for rural demand. Moreover, it expects the services sector to maintain its momentum, which would support the revival in urban consumption demand. In addition, the MPC foresees an improvement in domestic investment activity in light of higher capacity utilisation (CU) levels, improving balance sheets of financial and non-financial corporates, and Government's capital expenditure push. However, the Committee noted that the trade policy uncertainty continues to dampen prospects for merchandise trade, while acknowledging that the recent trade agreement with the UK and progress in FTAs with other countries augurs well for India's trade activity. Overall, it anticipates the economic activity to maintain the momentum in FY2026 supported by private consumption and fixed capital formation. However, spillovers stemming from geopolitical tensions, global trade and weather-related uncertainties pose downside risks to growth.

Taking all these factors into account, the Committee maintained the FY2026 GDP growth forecast at 6.5%, in line with the level indicated in April 2025. In quarterly terms, the growth projections for Q1 FY2026 (at +6.5%), Q2 FY2026 (at +6.7%), Q3 FY2026 (at +6.6%) and Q4 FY2026 (at +6.3%) have been retained at the levels pencilled in the April 2025 policy.

In the June 2025 policy statement, the MPC stated that the growth remained lower than their aspirations amid heightened trade policy uncertainty and challenging global environment, which portends them to focus on stimulating domestic private consumption and investment through policy levers and step up the growth momentum. Consequently, the MPC front-loaded on the quantum of policy easing to 50 bps in today's policy compared to 25 bps rate cuts each in the prior two policy meetings in February and April 2025. Nevertheless, it highlighted that there is a very limited space left in monetary policy to provide further support to growth, and hence, incoming data and continuous monitoring of the evolving macroeconomic outlook presumes importance to chart out the future course of monetary policy in order to strike the right growth-inflation balance.

While FY2026 has begun with heightened uncertainty around global trade policies, the outlook for domestic drivers of growth, including private consumption and Government investment appears resilient, given the personal income tax relief, monetary easing, expectations of an above normal monsoon and lower food inflation, and a healthy growth in budgeted capex. However, the outlook for merchandise and IT exports, and private capex appears muted, although the relative tariff scenario will evolve as the year progresses. Overall, we forecast India's GDP growth at 6.2% in FY2026, lower than the MPC's projection of 6.5%. Given our lower inflation and growth forecasts, we are not ruling out a final 25 bps rate cut in October 2025.

After worsening in Q4 FY2025, systemic liquidity conditions improved in April-May 2025, amid substantial liquidity infusion by the RBI.

On a monthly basis, the size of the systemic liquidity surplus widened to Rs. 1.7 trillion in May 2025 from Rs. 1.4 trillion in April 2025.

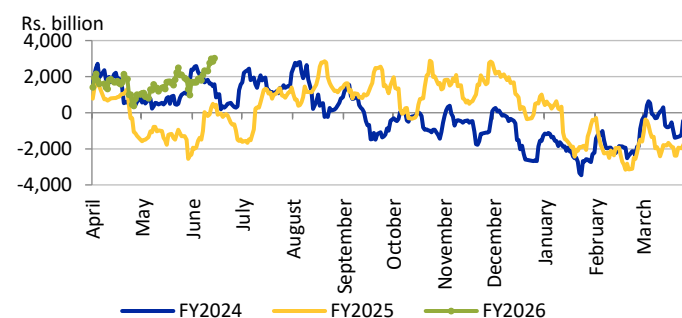
Correspondingly, the durable liquidity surplus nearly tripled to Rs. 3.5 trillion as on mid-May 2025 from mid-March 2025 levels, amid sharp drawdown in GoI cash balances.

Systemic liquidity transitioned to surplus during April-May 2025: Liquidity conditions have improved materially in the first two months of FY2026, with the daily average systemic liquidity reversing to a surplus of Rs. 1.6 trillion (+0.7% of NDTL) from the deficit of a similar size of Rs. 1.6 trillion seen in Q4 FY2025 (-0.7% of NDTL). In monthly terms, the systemic liquidity turned around from the deficit of Rs. 1.2 trillion in March 2025 (-0.5% of NDTL) to a sizeable surplus of Rs. 1.4 trillion in April 2025 (+0.6% of NDTL), which rose further to Rs. 1.7 trillion in May 2025 (+0.7% of NDTL). Nevertheless, the substantial cooling in liquidity conditions was attributed to measures undertaken by the RBI that injected durable liquidity to the tune of Rs. 9.5 trillion since January 2025, which includes ~Rs. 5.2 trillion via OMO purchases (of which Rs. 2.4 trillion were seen during April-May 2025), ~Rs. 2.2 trillion via the USD/INR swaps, and the remaining Rs. 2.1 trillion through four term VRR auctions (refer Exhibit 6). Besides, the Central Bank conducted main 14-day and daily VRR operations which injected liquidity amounting to Rs. 3.2 trillion during April-May 2025, after Rs. 49.3 trillion infused in Q4 FY2025. In June 2025, the surplus stands at an elevated Rs. 3.0 trillion up to June 5, 2025 (1.3% of NDTL), following the record RBI dividend pay-out of Rs. 2.7 trillion to the GoI. Furthermore, five daily VRR auctions have been conducted in the ongoing month (until June 5, 2025) that infused Rs. 186 billion.

Additionally, after net outflows of \$13.4 billion in Q4 FY2025, FPIs injected \$2.9 billion into capital markets in April-May 2025 which also supported systemic liquidity conditions.

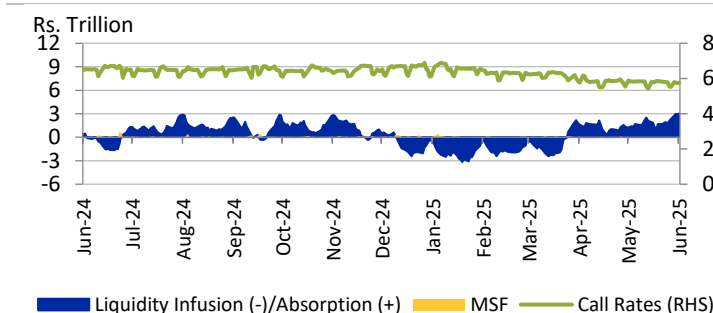
Durable liquidity surplus surged to Rs. 3.5 trillion by mid-May 2025: The durable liquidity surplus nearly tripled to Rs. 3.5 trillion or 1.5% of NDTL as on May 16, 2025, from Rs. 1.1 trillion as on March 21, 2025 (0.5% of NDTL), aided by aforesaid liquidity injection through various tools (OMOs and forex swaps).

EXHIBIT 4: Liquidity Infusion (-)/ absorption (+)



*Data for FY2026 is shown up to June 6, 2025; Source: RBI; ICRA Research

EXHIBIT 5: Call money rates



Source: RBI; ICRA Research

The RBI has injected durable liquidity of Rs. 9.5 trillion since January 2025. During April-May 2025, the injection stood at Rs. 2.7 trillion, largely via OMO purchase of G-secs amounting to Rs. 2.4 trillion.

Given the elevated durable liquidity, the response to VRR has remained tepid in recent months.

All these measures, along with sizeable RBI dividend pay-out have eased liquidity pressures, resulting in a systemic liquidity surplus of Rs. 3.0 trillion as on June 5, 2025.

CRR cut of 100 bps to inject durable liquidity of Rs. 2.5 trillion: After the durable injection of Rs. 9.5 trillion since January 2025 via term VRRs, OMO purchase of G-secs and USD/INR buy-sell swaps, the RBI has decided to reduce the CRR by 100 bps to 3.00% of NDTL in four equal tranches with effect from the fortnight of September 6, 2025. This big surprise action is expected to release primary liquidity of Rs. 2.5 trillion to the banking system by December 2025.

EXHIBIT 6: RBI's durable liquidity injection via VRR operations, OMOs and buy/sell dollar swap auction

Tool/Month	January-2025	February-2025	March-2025	April-2025	May-2025	Total
Term VRR (Rs. trillion)- A	0	1.83	0	0.26	0	2.09
OMO (Rs. trillion)- B	0.59	0.80	1.45	1.20	1.19	5.23
USD/INR buy/sell swap (Rs. trillion*)- C	0.44	0.88	0.87	0	0	2.18
Grand Total (A+B+C)	1.03	3.51	2.32	1.46	1.19	9.51
Outstanding durable liquidity~ (% of NDTL)	-0.1%	+0.1%	+0.5%	+0.9%	+1.5%	

**Based on average reference rates for USD/INR in that month; ~Used the second fortnightly data for these months; Source: RBI; ICRA Research*

The unexpected 100 bps CRR cut to 3.00% of NDTL in a staggered manner between early-September 2025 and end-November 2025, is expected to pump in durable liquidity to the tune of Rs. 2.5 trillion during the busy season, while aiding in monetary transmission. Moves to aid transmission must be supported through a modification in the GoI's small savings scheme rates for Q2 FY2026 as well. In addition, the RBI's pre-emptive liquidity action would assist in countering the potential tightness on account of the likely unwinding in its forward book, which remains at quite elevated levels, even though the maturity profile of the same is now elongated relative to that seen six months ago.

Money market rates moderated in April-May 2025, below the repo rate: The monthly weighted average call money rate (WACR) softened materially from 6.22% in March 2025 to 5.93% in April 2025 and further to 5.82% in May 2025, in light of improvement in the liquidity conditions. The rates remained below the then prevailing repo rate in April 2025 and May 2025, and trended towards the lower end of the LAF corridor. Correspondingly, the yields in the secondary T-bill market (91-day, 182-day and 364-day tenures) fell by 45-50 bps MoM in April 2025 to 5.97%, 6.04%, and 5.99%, respectively, and further by 16-22 bps in May 2025 to 5.81%, 5.82% and 5.83%. **The front-loaded rate cut of 50 bps is expected to further cool the money market rates in the near term.**

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