



ICRA COMMENTS ON RBI'S 5th BI-MONTHLY MONETARY POLICY MEETING FOR 2025-26

MPC eased repo rate by 25 bps to 5.25%
in December 2025; notwithstanding
dovish policy tone, ICRA expects rate cut
cycle to have ended

DECEMBER 2025



HIGHLIGHTS



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The MPC unanimously decided to cut the repo rate by 25 bps to 5.25% in December, while 5 of the 6 members voted to maintain neutral policy stance.

The FY2026 CPI inflation forecast was pared by 60 bps to 2.0%, while the GDP growth projection was raised by 50 bps to 7.3%.

ICRA now expects an extended pause on policy rates, unless growth materially undershoots projections.

The Monetary Policy Committee (MPC) unanimously decided to reduce the policy repo rate by 25 bps to 5.25% in the December 2025 policy review, while five of the six members voted to maintain the neutral policy stance. As expected, the Committee pared its FY2026 CPI inflation forecast by 60 bps to 2.0% relative to the October 2025 estimate, while simultaneously raising the GDP growth projection to 7.3% from the 6.8% indicated earlier. While the tone of the policy document was benign, we believe that today's rate cut is the final one in the current easing cycle. Any further rate easing from current levels would only be likely if there is a material downward undershooting in growth outcomes, which results in a cut in growth projections. Additionally, the RBI has decided to infuse durable liquidity in December 2025 via open market operation (OMO) purchase of G-secs (amounting to Rs. 1.0 trillion) and \$5 billion USD/INR 3Y buy-sell swap auction, amidst the likely seasonal tightening of liquidity conditions owing to advance tax outflows and higher currency leakages. This is expected to augur well for transmission as well as G-sec yields.

- The MPC unanimously reduced the policy repo rate by 25 bps to 5.25% in the December 2025 policy review. Consequently, the standing deposit facility (SDF) rate was lowered to 5.00%, and the marginal standing facility (MSF) rate and the Bank Rate to 5.50% each. Additionally, the MPC maintained the neutral policy stance, although one member voted for a shift to an accommodative stance.
- The Committee noted that the decline in headline and core inflation has become generalised. It pared the FY2026 CPI inflation forecast to 2.0% from 2.6% indicated in October 2025, reflecting a material downward revision in Q3 (+0.6% in December 2025 vs. +1.8% in October 2025) and Q4 (+2.9% vs. +4.0%). Besides, it lowered the Q1 FY2027 estimate by 60 bps to 3.9% and placed the Q2 FY2027 CPI inflation estimate at 4.0%.
- On the growth front, the MPC expects the consumption demand to remain firm, while merchandise exports may continue to face headwinds. Given the stronger-than-expected H1 print, the MPC has raised the FY2026 GDP growth forecast by 50 bps to 7.3%. Besides, the projections for Q3 FY2026 (to +7.0% from +6.4%) and Q4 FY2026 (to +6.5% from +6.2%) have been increased by 60 bps and 30 bps, respectively. Moreover, it also revised the Q1 FY2027 projection (to +6.7% from +6.4%) upwards by 30 bps, while estimating growth in Q2 FY2027 to print at 6.8%, with risks evenly balanced.
- To manage the impending liquidity tightness arising out of advance tax outflows as well as likely increase in currency leakages, the RBI has decided to conduct OMO purchase of G-secs worth Rs. 1.0 trillion and \$5 billion buy-sell swap (~Rs. 0.5 trillion) in December 2025; this would push up durable liquidity by ~Rs. 1.45 trillion in the month, auguring well for transmission and yields.

Outlook: While the tone of the policy document was benign, we believe that today's rate cut is the final one in the current easing cycle. Any further rate easing from current levels would only be likely if there is a material downward undershooting in growth outcomes, which leads to a cut in growth projections. However, interventions on the liquidity front may well continue, depending on how durable and systemic liquidity conditions evolve.

The MPC unanimously cut the policy repo rate by 25 bps to 5.25% in Dec 2025; it also maintained the monetary policy stance at neutral, with a 5:1 vote.

The Committee expects CPI inflation to remain benign in the near term, aided by higher kharif production, healthy rabi sowing, adequate reservoir levels, and conducive moisture, coupled with moderating international commodity prices.

MPC expects both headline inflation and core inflation to print around the inflation target of 4% in H1 FY2027.

MPC UNANIMOUSLY CUT THE REPO RATE TO 5.25% IN DECEMBER 2025; STANCE MAINTAINED AT NEUTRAL

In its fifth bi-monthly monetary policy meeting for FY2026, the MPC unanimously decided to cut the policy repo rate under the LAF by 25 bps to 5.25% in December 2025 review meeting (refer Exhibit 1), in contrast with ICRA's expectation of status quo. Accordingly, the SDF rate stands adjusted at 5.00%, and the MSF and Bank Rate at 5.50% each. Further, it decided to continue with the neutral stance, albeit with a majority of 5:1 members, with the only dissenting member voting in favour of an accommodative stance (as against two members in the October 2025 meeting). The Committee highlighted that "the benign inflation outlook on both headline and core, continues to provide the policy space to support the growth momentum".

MPC's CPI inflation projection for FY2026 pared by 60 bps to 2.0%: The YoY CPI inflation cooled to a record low of 0.3% in October 2025 from 1.4% in September 2025, given the widening deflation in the F&B segment (to -3.7% from -1.4%). Core inflation (CPI excluding food and beverages, fuel and light, and petrol and diesel for vehicles), stayed above 4% for the ninth consecutive month, printing at 4.5% in October 2025 (unchanged from the previous month), with the favourable impact of the GST rationalisation dulled by the spike in gold and silver prices during the festive season. Excluding gold and silver, core-CPI stood low at just 2.6%, down from 3.1% in September 2025.

Looking ahead, the MPC now expects the near-term CPI inflation trajectory to be more benign compared to its October 2025 assessment, amid higher kharif production, healthy rabi sowing, adequate reservoir levels, and conducive soil moisture levels. Additionally, moderating prices of international commodity prices (barring some metals) are likely to augur favourably for inflation prints, going forward. Considering all these factors, the Committee tempered its inflation expectation for FY2026 sharply by 60 bps to 2.0% (lower than ICRA's projection of 2.2%) from 2.6% projected earlier in October 2025. Notably, it has cut the CPI inflation projections for Q3 FY2026 (to +0.6% in December 2025 from +1.8% in October 2025), Q4 FY2026 (to +2.9% from +4.0%) by a sizeable 110-120 bps. Additionally, it has also pared the inflation forecast for Q1 FY2027 (to +3.9% from +4.5%) by 60 bps, and has issued a fresh forecast for Q2 FY2027 pegged at 4.0%, with risks evenly balanced.

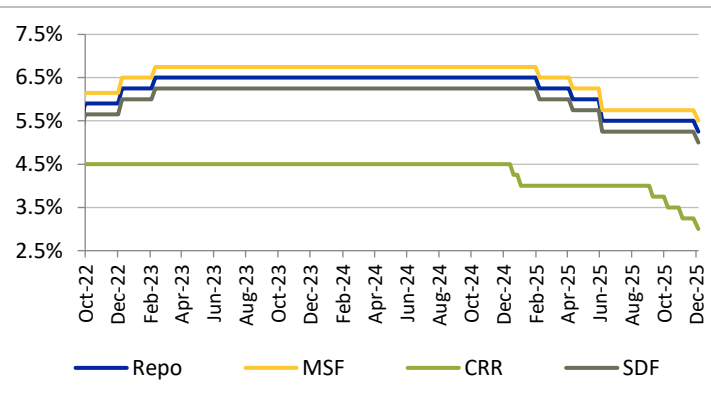
The MPC highlighted that the decline in inflation has become more generalised. We believe that is also partly on account of the GST rate rationalisation; this is reflected in the share of items in the CPI basket that witnessed a sequential decline in prices rising sharply to 54% in October 2025 from 39% in September 2025, while also significantly exceeding the typical average seen during October of a fiscal year.

In ICRA's view, the downward revision in the MPC's quarterly CPI inflation projections is largely along expected lines. However, some of the decline in inflation in October 2025 has stemmed from tax policy changes, owing to the GST rate cuts across several items in the CPI basket, which has led to the cooling in the core-CPI excluding gold in that month (and not weaker demand). The favourable impact of the tax cuts is expected to exert some downward pressure on the CPI inflation prints until Q2 FY2027.

Overall, while the tone of the policy document was benign, ICRA expects the rate cut cycle to have come to an end. Any further rate easing would only be likely if there is a material downward undershooting in growth outcomes, which leads to a cut in growth projections.

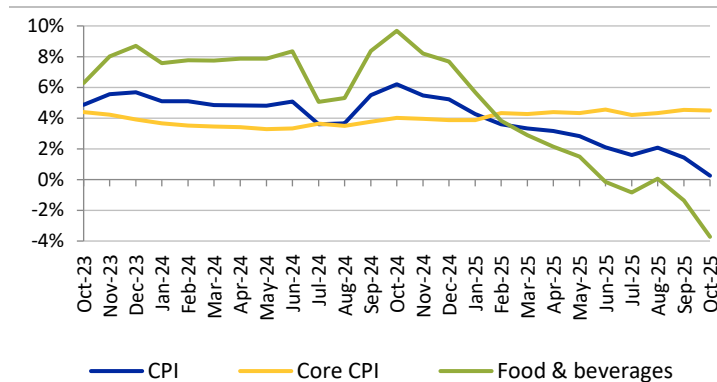
The MPC pared its FY2026 CPI inflation projection by 60 bps to 2.0% in Dec 2025 from the earlier estimate of 2.6%, slightly lower than ICRA's forecast of 2.2% for the year.

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

The Committee has revised its inflation projection for Q3-Q4 FY2026 downwards by 110-120 bps, relative to October 2025; thereafter, it expects CPI inflation to print around 4.0% in H1 FY2027.

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

YoY (%)	CPI Inflation		GDP Growth (at constant 2011-12 prices)	
	October 2025	December 2025	October 2025	December 2025
MPC Policy Reviews				
Q3 FY2026	1.8%	0.6%	6.4%	7.0%
Q4 FY2026	4.0%	2.9%	6.2%	6.5%
FY2026	2.6%	2.0%	6.8%	7.3%
Q1 FY2027	4.5%	3.9%	6.4%	6.7%
Q2 FY2027		4.0%		6.8%

Source: RBI; ICRA Research

The MPC expects rural demand to be aided by healthy kharif output and upbeat outlook for rabi sowing.

Moreover, domestic demand prospects are likely to have improved in Q3, aided by the GST rate rationalisation- and festive season-led uptick in spending.

Going ahead, the MPC highlighted that while investment activity is likely to hold up, external sector headwinds from steep tariffs would continue to impede the pace of economic growth, unless a trade deal is finalised.

Aided by the strong H1 print, the MPC raised its FY2026 GDP growth forecast to 7.3% from 6.8% indicated in Oct 2025.

GDP growth printed at a sharper-than-anticipated 8.2% in Q2 FY2026: India's GDP growth surged to a six-quarter high of 8.2% in Q2 FY2026 from 7.8% in Q1, well above the MPC's estimate (+7.0%). This was led by an acceleration in the private final consumption growth (PFCE; to +7.9% from +7.0%), even as government final consumption expenditure (GFCE; to -2.7% from +7.4%) contracted and growth in gross fixed capital formation (GFCF; to +7.3% from +7.8%) eased. On the GVA side, the eight-quarter high growth of 8.1% in Q2 FY2026 stemmed entirely from the industrial sector (to +7.7% from +6.3%, led by manufacturing), while growth eased in services (to +9.2% from +9.3%) and agriculture, forestry and fishing (to +3.5% from +3.7%).

MPC raised its FY2026 GDP growth forecast by 50 bps to 7.3%: The Committee stated that economic activity remains resilient in Q3 FY2026, given the impact of the GST rate cut- and festive season-led boost in consumer spending. Moreover, rural demand remains upbeat amid healthy kharif output and robust outlook for rabi sowing, while urban demand is recovering consistently. Additionally, the expansion in non-food bank credit and healthy capacity utilisation levels are likely to aid the private investment activity, going ahead. This along with healthy balance sheets of corporates and financial institutions should continue to support economic activity. While services exports are expected to hold up, merchandise exports are likely to slow down, as the external sector continues to face adverse headwinds from trade and tariff-related policies. Nevertheless, finalisation of the India-US trade deal could ease such pressures and continuing reform initiatives would provide a fillip to economic growth.

Taking all these factors into account as well as the higher-than-expected GDP growth prints for H1 FY2026, the Committee raised its FY2026 GDP growth forecast to 7.3% from 6.8% indicated in the October 2025 policy. Additionally, the projections for Q3 FY2026 (to +7.0% from +6.4%) and Q4 FY2026 (to +6.5% from +6.2%) have been raised by 60 bps and 30 bps, respectively. Moreover, the MPC has revised the Q1 FY2027 projection (to +6.7% from +6.4%) upwards by 30 bps, while also estimating growth in Q2 FY2027 to print at 6.8%, with risks evenly balanced.

ICRA expects the GDP growth to print at 7.4% in FY2026, marginally higher than the MPC's estimate of 7.3%. Nevertheless, in line with the MPC's expectation, we estimate the GDP growth to slow down to ~6.8% in H2 FY2026 (+6.9% in H2 FY2025) from 8.0% in H1 FY2026 (+6.1% in H1 FY2025), as the unfavourable base kicks in, merchandise exports feel the brunt of the US tariffs and headroom for capex spending by the GoI declines post the front-loading seen in H1.

The consumption volumes of goods and services as well as manufacturing volume growth are likely to witness a festive season-led boost in Q3 FY2026. However, while the well-timed GST rationalisation may result in a steady boost in volumes of consumer non-durables going ahead, consumer durables may see a trend of premiumisation instead of a sustenance of the spike in volumes that was seen during the festive season. Additionally, the drag from slowdown in exports would intensify during this period compared to H1 FY2026, unless a trade deal with the US materialises.

Nevertheless, the service sector prospects for H2 look bright, as the demand during the festive and wedding periods, as well as leisure travel picks up, that would support the sectors like aviation, hotels, etc. Business travel, however, may see some moderation in the upcoming months, especially in sectors vulnerable to higher US tariffs.

The size of the average systemic liquidity surplus moderated to 0.6% of NDTL in Oct-Nov 2025 from 1.0% in Q2 FY2026.

Currency leakages during the festive season and likely forex market intervention have exerted pressure on liquidity, particularly in Oct 2025.

However, durable liquidity surplus remains healthy at 1.5% of NDTL as at mid-Nov 2025, albeit lower than 2.2% of NDTL seen as on Sep 19, 2025, with drawdown of Gol cash balances with RBI.

This outweighed the impact of CRR cut of 100 bps that injected durable liquidity to the tune of Rs. 2.4 trillion between Sep-Nov 2025.

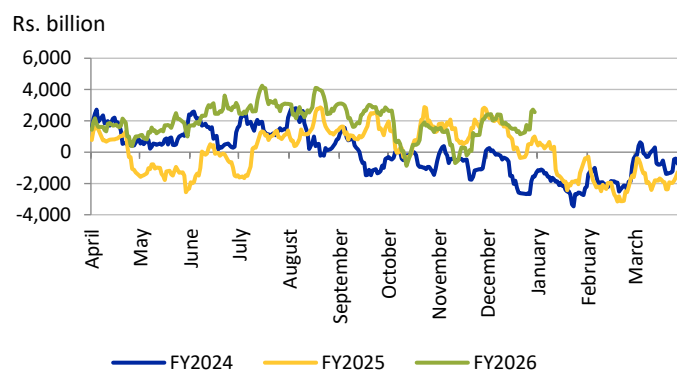
Systemic liquidity surplus dipped to 0.6% of NDTL in October-November 2025 from 1.0% in Q2 FY2026: Liquidity conditions remained comfortable during October-November 2025, although the monthly average size of the systemic liquidity surplus moderated to Rs. 1.4 trillion (0.6% of net time and demand liabilities; NDTL) during this period from Rs. 2.5 trillion (1.0% of NDTL) in Q2 FY2026. This has been driven by higher demand for cash during the festive season as well as GST-cut led boost in spending, as reflected in currency with the public (by +Rs. 445 billion from Sep 19, 2025 to Nov 14, 2025 vs. -Rs. 298 billion in Q2 FY2026).

In monthly terms, the average liquidity surplus has dipped from Rs. 1.5 trillion in September 2025 to Rs. 0.9 trillion in October 2025, likely owing to the forex market intervention by the RBI (foreign currency assets dipped by ~\$17.2 billion in October 2025), before rising sharply to Rs. 1.9 trillion in November 2025. In the ongoing month, the systemic surplus has averaged at a sizeable Rs. 2.6 trillion till December 3, 2025, aided by the liquidity injection of Rs. 0.6 trillion via last tranche of CRR cut of 25 bps on November 29.

The durable liquidity surplus also remains quite sizeable, although the extent of the same moderated to Rs. 3.6 trillion (1.5% of NDTL) as on November 14, 2025 from Rs. 5.2 trillion (2.2% of NDTL) as on September 19, 2025, despite the two tranches of CRR cut of 25 bps each, that led to liquidity injection of ~Rs. 1.2 trillion during this period.

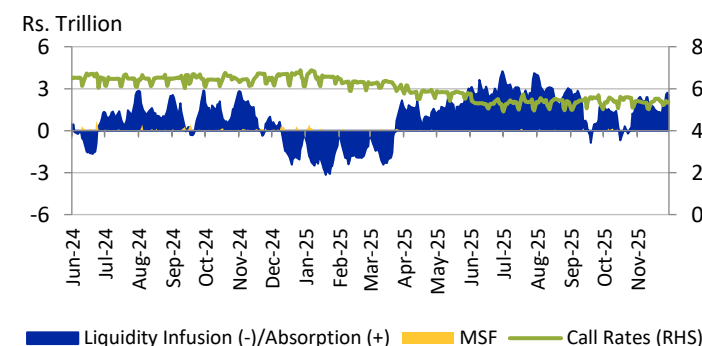
In addition, the Gol's cash balances with the RBI have reduced to Rs. 1.3 trillion as on November 14, 2025 from 4.9 trillion as on September 19, 2025, amid a likely pick up in the Gol spending after the festive season.

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



*Data for FY2026 is up to December 3, 2025; Source: RBI; ICRA Research

EXHIBIT 5: Call money rates



Source: RBI; ICRA Research

To ease tight conditions in Oct 2025, the RBI conducted 12 VRRs, with aggregate notified amount of Rs. 11.5 trillion, that resulted in liquidity injection of Rs. 6.3 trillion in the month.

WACR rose to a 5-month high 5.48% in Oct 2025, while printing a shade below the repo rate of 5.50%; thereafter it cooled to 5.41% in Nov 2025. Today's repo rate cut of 25 bps to 5.25% will further transmit into a lower WACR in the immediate term.

RBI's announced measures of conducting OMO of G-secs worth Rs 1.0 trillion and \$5 billion buy/sell swap auction in December 2025 are set to release durable liquidity of Rs. 1.5 trillion.

RBI conducted 12 VRRs in October 2025 to manage liquidity tightness related to festive season and forex operations: In view of intermittent liquidity deficits during October 2025 owing to currency leakages during festive season and forex operations, the RBI conducted 12 VRRs in the month, with a combined notified amount of Rs. 11.5 trillion, even as the liquidity injection amounted to a lower Rs. 6.3 trillion in the month. This was similar to the size of infusion done in the entire quarter ending September 2025 (Rs. 6.2 trillion) via VRRs. Thereafter, in November 2025, only one VRR was conducted that resulted in an injection of Rs. 164 billion, as liquidity conditions became favourable, with a sharp improvement in average systemic liquidity surplus as compared to October 2025.

In addition, the RBI has conducted 6 VRRRs to absorb excess liquidity to the tune of Rs. 3.0 trillion in Q3 FY2026 so far (till Dec 4), 80% of the amount notified in such auctions. Moreover, half of these VRRRs have been done in the first four days of December 2025 itself, amid sizeable increase in surplus liquidity to as high as Rs. 2.6 trillion.

WACR remains below the repo rate: The average monthly weighted average call money rate (WACR) rose to a 5-month high of 5.48% in October 2025 from 5.45% in September 2025, as liquidity conditions tightened during the month – nevertheless these rates remained lower than the prevailing repo rate of 5.50%. Thereafter, the WACR eased to 5.41% in November 2025, with the sharp increase in liquidity surplus. In response to the cumulative policy repo rate cut of 100 bps in the current easing cycle (up to December 3), the WACR, the 3-month T-bill rate, the rate on 3-month CPs issued by NBFCs, and the 3-month CD rate declined by 110 bps, 113 bps, 124 bps, and 140 bps, respectively.

25 bps rate cut to further translate into lower lending and deposit rates: In response to the cumulative 100 bps cut in the policy repo rate undertaken during February-June 2025, the weighted average lending rate (WALR) of Scheduled Commercial Banks has declined by 69 bps for fresh rupee loans during February-October 2025. Besides, the moderation in the weighted average lending rate (WALR) of outstanding rupee loans has been to the extent of 63 bps. On the deposit side, the weighted average domestic term deposit rate (WADTDR) on fresh deposits has declined by 105 bps, while that on outstanding deposits has softened by 32 bps over the same period.

RBI to inject Rs. 1.5 trillion of durable liquidity via OMOs and buy/sell swaps in December 2025: On a review of current liquidity and financial conditions, the RBI has decided to conduct the OMO purchase auctions of GoI securities for an aggregate amount of Rs. 1.0 trillion in two tranches of Rs. 500 billion each to be held on December 11, 2025, and December 18, 2025, respectively. Besides, it will also conduct USD/INR Buy/Sell Swap auction of \$5.0 billion for a tenor of 3 years on December 16, 2025, that may lead into a durable liquidity injection of ~Rs. 450 billion. In aggregate, the durable liquidity is estimated to increase by Rs. 1.5 trillion in the ongoing month, which is expected to ease pressures on account of advance tax and GST outflows in the month, as well as further increase in currency leakage related to higher demand during the wedding season and agri crop procurement in Q4 of a fiscal year.

Notably, the RBI Governor highlighted that the primary purpose of open market operations is to provide sufficient liquidity and not to directly influence G-sec yields. He also clarified that the objective of OMOs is to provide (absorb) durable liquidity, while the purpose of repo operations is to manage transient liquidity to align the WACR to the policy repo rate. As a result, the RBI would continue to conduct the VRRR operation to manage transient liquidity conditions, while simultaneously conducting OMOs of G-secs to inject liquidity on a durable basis.

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