MPC announces a 25bp rate cut to 6%

Changes stance from accommodative to neutral

- **At its first meeting of FY26, the MPC unanimously decided to reduce the benchmark repo rate by 25bp to 6.00%, marking its second consecutive cut, broadly in line with market expectations.**
- **The MPC also decided unanimously to change the stance to accommodative from neutral. The Governor mentioned that the stance of monetary policy signals the intended direction of policy rates going forward, which implies that the MPC is considering only two options in the upcoming meetings — status quo or a rate cut. "Our stance provides policy rate guidance without any direct guidance on liquidity management…," the Governor mentioned.**
- **The MPC noted that there is a decisive improvement in the inflation outlook (CPI is below the target), aided by a sharp fall in food inflation. However, growth is still on a recovery path after slowing down in 2QFY25. Moreover, there is a lot of uncertainty due to the tariff hikes announced by the US. The Governor stated, "In such challenging global economic conditions, the benign inflation and moderate growth outlook demands that the MPC continues to support growth…".**
- **The RBI reduced its FY26 real GDP projection to 6.5% (with 1Q/2Q/3Q/4Q at 6.5%/6.7%/6.6%/6.3%) from 6.7% (1Q/2Q/3Q/4Q at 6.7%/7.0%/6.5%/6.5%) in the Feb'25 policy on the back of a recent spike in global volatility and the impact of global trade and policy uncertainties. The RBI Governor mentioned that the dent in global growth due to trade frictions would impede domestic growth and higher tariffs would hurt net exports.**
- **The MPC noted that headline inflation moderated decisively in Jan-Feb'25, supported by a sharp correction in food inflation. The Governor mentioned that the uncertainties regarding rabi crops have abated considerably, and the second advance estimates point to a record wheat and pulses. Moreover, robust kharif arrivals and a fall in crude oil prices would set the stage for durable softening of inflation. Global market uncertainties and the recurrence of adverse weather-related supply disruptions, however, pose upside risks to the inflation trajectory. The RBI statement mentioned, "…Overall, while global trade and policy uncertainties shall impede growth, its impact on domestic inflation, while requiring us to be vigilant, is not expected to be of high concern…". Considering all these factors, the MPC lowered its inflation forecast to 4.0% in FY26 (with 1Q/2Q/3Q/4Q at 3.6%/3.9%/3.8%/4.4%) from 4.2% in the Feb'25 policy (with 1Q/2Q/3Q/4Q at 4.5%/4%/3.8%/4.2%).**
- **Overall, the monetary policy decisions were broadly in line with our and market expectations. We believe that a benign inflation outlook coupled with weak growth (impeded by global trade and policy uncertainties) would make RBI's task easy, providing room to support growth. Currency could be the only restraining factor, as global uncertainties might lead to currency pressures and imported inflation. In any case, we expect the RBI to cut rates further in the upcoming policies.**

I. MPC unanimously decides to cut the repo rate by 25bp

- At its first meeting of the fiscal year FY26, the MPC unanimously decided to reduce the benchmark repo rate by 25bp to 6.00%, marking its second consecutive cut, broadly in line with market expectations.
- The MPC also decided unanimously to change the stance to accommodative from neutral. The Governor mentioned that the stance of monetary policy signals the intended direction of policy rates going forward, which implies that the MPC is considering only two options in the upcoming meetings – status quo or a rate cut. *"…Our stance provides policy rate guidance without any direct guidance on liquidity management…," the Governor mentioned.*
- The MPC noted that there is a decisive improvement in the inflation outlook (CPI is below the target), supported by a sharp fall in food inflation. However, growth is still on a recovery path after slowing down in 2QFY25. Moreover, there is a lot of uncertainty on the back of tariff hikes announced by the US. The Governor stated, *"In such challenging global economic conditions, the benign inflation and moderate growth outlook demands that the MPC continues to support growth."*

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Exhibit 1: Repo rate cut to 6.0% in the Apr'25 policy, a 25bp reduction

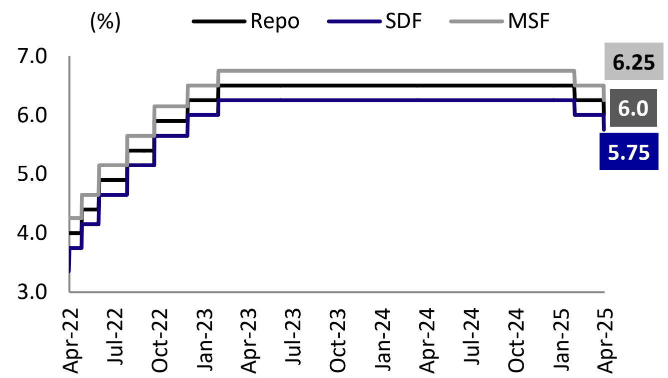
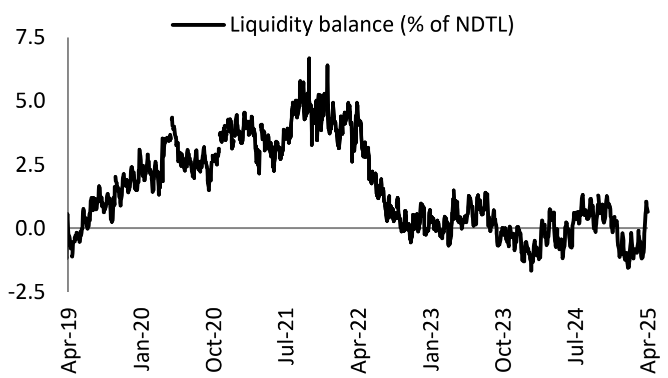


Exhibit 2: System liquidity deficit tapered during Feb-Mar'25 and remained in surplus in the last week



Updated as of 8th Apr'25 Source: RBI, MOFSL

II. Economic activity likely to moderate in FY26

- Real GDP is estimated to grow 6.5% in FY25, following a 9.2% growth in FY24. In FY26, prospects of the agriculture sector remain bright on the back of healthy reservoir levels and robust crop production. Manufacturing activity is showing signs of revival, while services sector activity continues to be resilient. However, headwinds from global trade disruptions continue to pose downward risks.
- The RBI reduced its FY26 real GDP projection to 6.5% (with 1Q/2Q/3Q/4Q at 6.5%/6.7%/6.6%/6.3%) from 6.7% (1Q/2Q/3Q/4Q at 6.7%/7.0%/6.5%/6.5%) in the Feb'25 policy due to a recent spike in global volatility and the impact of global trade and policy uncertainties. The RBI Governor mentioned that the dent in global growth due to trade frictions would impede domestic growth and higher tariffs would hurt net exports.

III. Inflation likely to come down to 4.0% in FY26 from 4.8% in FY25

- The MPC noted that headline inflation moderated decisively in Jan-Feb'25, supported by a sharp correction in food inflation. The Governor mentioned that the uncertainties regarding rabi crops have abated considerably, and the second advance estimates point to a record wheat and pulse production. Moreover, robust kharif arrivals and a fall in crude oil prices would set the stage for the durable softening of inflation. Global market uncertainties and the recurrence of adverse weather-related supply disruptions, however, pose upside risks to the inflation trajectory. "….Overall, while global trade and policy uncertainties shall impede growth, its impact on domestic inflation, while requiring us to be vigilant, is not expected to be of high concern….," the RBI statement mentioned.
- Considering all these factors, the MPC lowered its inflation forecast to 4.0% in FY26 (with 1Q/2Q/3Q/4Q at 3.6%/3.9%/3.8%/4.4%) from 4.2% in the Feb'25 policy (with 1Q/2Q/3Q/4Q at 4.5%/4%/3.8%/4.2%).

IV. Our view

Overall, the monetary policy decisions were broadly in line with our and market expectations. We believe that a benign inflation outlook coupled with weak growth (impeded by global trade and policy uncertainties) would make RBI's task easy, providing room to support growth. Currency could be the only restraining factor, as global uncertainties might lead to currency pressures and imported inflation. In any case, we expect the RBI to cut rates further in the upcoming policies.

Exhibit 3: Real GDP growth projected at 6.5%...

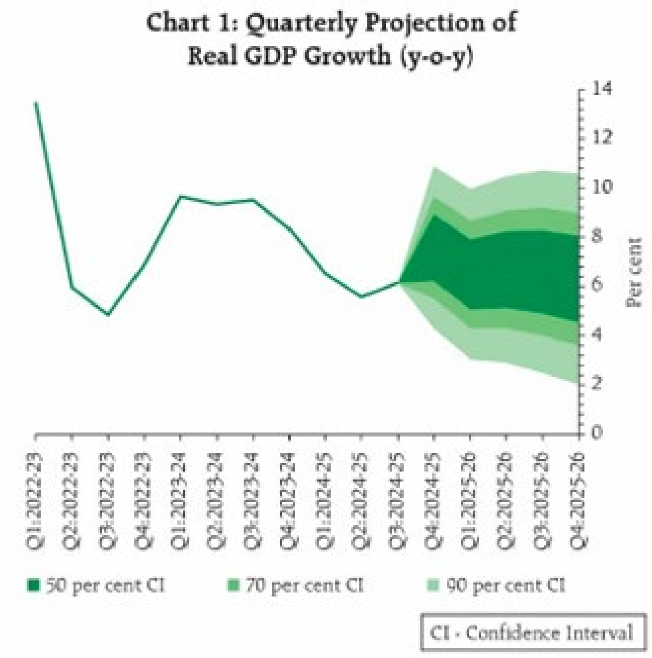
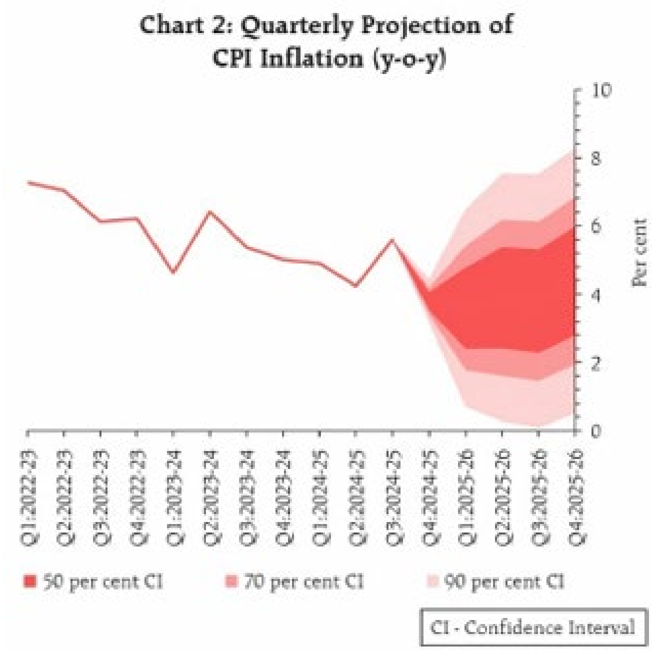


Exhibit 4: ...with inflation estimated at 4.0% for FY26



Source: RBI, MOFSL

NOTES

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