

SPECIAL UPDATE

Monetary Policy

June 06, 2025

Monetary Measures

- The MPC voted to reduce the policy repo rate by 50 basis points (bps) to 5.50 per cent.
- Consequently, the standing deposit facility (SDF) rate under the liquidity adjustment facility (LAF) shall stand adjusted to 5.25 per cent and the marginal standing facility (MSF) rate and the Bank Rate to 5.75 per cent.
- The MPC also decided to change the stance from accommodative to neutral.

Analysis & Outlook

- **Inflation:** CPI headline inflation continued its declining trajectory in March and April, with headline CPI inflation moderating to a nearly six-year low of 3.2 per cent (year-on-year) in April 2025. This was led mainly by food inflation which recorded the sixth consecutive monthly decline. Fuel group witnessed a reversal of deflationary conditions and recorded positive inflation prints during March and April, partly reflecting the hike in LPG prices. Core inflation remained largely steady and contained during March-April, despite increase in gold prices exerting upward pressure. The outlook for inflation points towards benign prices across major constituents. The record wheat production and higher production of key pulses in the Rabi crop season should ensure adequate supply of key food items. Going forward, the likely above normal monsoon along with its early onset augurs well for Kharif crop prospects. Reflecting this, inflation expectations are showing a moderating trend, more so for the rural households. Most projections point towards continued moderation in the prices of key commodities, including crude oil. Notwithstanding these favourable prognoses, we need to remain watchful of weather-related uncertainties and still evolving tariff related concerns with their attendant impact on global commodity prices. Taking all these factors into consideration, and assuming a normal monsoon, CPI inflation for the financial year 2025-26 is now projected at 3.7 per cent, with Q1 at 2.9 per cent; Q2 at 3.4 per cent; Q3 at 3.9 per cent; and Q4 at 4.4 per cent. The risks are evenly balanced.
- **Growth:** The uncertainty around the global economic outlook has ebbed somewhat since the MPC met in April 2025 in the wake of temporary tariff reprieve and optimism around trade negotiations. However, it continues to remain elevated to weaken sentiments and lower global growth prospects. Accordingly, global growth and trade projections have been revised downwards by multilateral agencies. Market volatility has eased in the recent period with equity markets staging a recovery, dollar index and crude oil softening though gold prices remain high. According to the provisional estimates released by the National Statistical Office (NSO) on May 30, 2025, real GDP growth in Q4:2024-25 stood at 7.4 per cent as against 6.4 per cent in Q3. On the supply side, real gross value added (GVA) rose by 6.8 per cent in Q4:2024-25. For 2024-25, real GDP growth was placed at 6.5 per cent, while real GVA recorded a growth of 6.4 per cent. Going forward, economic activity continues to maintain the momentum in 2025-26, supported by private consumption and traction in fixed capital formation. The sustained rural economic activity bodes well for rural demand, while continued expansion in services sector is expected to support the revival in urban demand. Investment activity is expected to improve in light of higher capacity utilization, improving balance sheets of financial and non-financial corporates, and government's capital expenditure push. Trade policy uncertainty continues to weigh on merchandise exports prospects, while the conclusion of free trade agreement (FTA) with the United Kingdom and progress with other countries is supportive of trade activity. On the supply side, agriculture prospects remain bright on the back of an above normal south-west monsoon forecast and resilient allied activities. Services sector is expected to maintain its momentum. However, spillovers emanating from protracted geopolitical tensions, and global trade and weather-related uncertainties pose downside risks to growth. Taking all these factors into account, real GDP growth for 2025-26 is projected at 6.5 per cent, with Q1 at 6.5 per cent, Q2 at 6.7 per cent, Q3 at 6.6 per cent, and Q4 at 6.3 per cent. The risks are evenly balanced.

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- **Liquidity:** The Reserve Bank remains committed to provide sufficient liquidity to the banking system. To further provide durable liquidity, it has been decided to reduce the cash reserve ratio (CRR) by 100 basis points (bps) to 3.0 per cent of net demand and time liabilities (NDTL) in a staggered manner during the course of the year. This reduction will be carried out in four equal tranches of 25 bps each with effect from the fortnights beginning September 6, October 4, November 1 and November 29, 2025. The cut in CRR would release primary liquidity of about ₹2.5 lakh crore to the banking system by December 2025.
- Corporate bond Yields in the near to medium term were down 15-20 bps from yesterday's close at the time of writing. Corporate bonds yields in the longer tenor were flatish.
- Gsec yield in the near term (upto 5 year) were down by 6-7 bps from yesterday's close at the time of writing. Gsec yields in the longer end (10 year and above) were up by 5 to 7 bps.

Position of Funds

Duration funds:

- The absolute yield levels are attractive from a medium to long-term investment horizon. Therefore, it represents an opportunity for investors to invest in fixed income duration funds with a medium to long-term horizon.
- However geopolitical risks and volatile food prices remain key risks. Markets may remain volatile in the near term.

Money market funds: The yields at the shorter end of the curve may move in tandem with the liquidity in the system. The short-end rates are expected to be anchored around the repo rate.

MUTUAL FUND INVESTMENTS ARE SUBJECT TO MARKET RISKS, READ ALL SCHEME RELATED DOCUMENTS CAREFULLY.

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