

SPECIAL UPDATE

Monetary Policy

Oct 01, 2025

Monetary Measures

- The MPC (Monetary Policy Committee) voted to keep the policy rate unchanged at 5.50 per cent.
- Consequently, the Standing Deposit Facility (SDF) rate under the Liquidity Adjustment Facility (LAF) remains unchanged at 5.25 per cent and the Marginal Standing Facility (MSF) rate and the Bank Rate at 5.75 per cent.
- The MPC also decided to retain the stance at neutral.

Analysis & Outlook

- **Inflation:** Headline Consumer Price Index (CPI) inflation declined to its eight-year low of 1.6 per cent (y-o-y) in July 2025 before rising to 2.1 per cent in August 2025 – its first increase after nine months. Benign inflation conditions during 2025-26 so far have been primarily driven by a sharp decline in food inflation from its peak of October 2024. Inflation within the fuel group moved in a narrow range of 2.4-2.7 per cent during June-August in 2025. Core inflation remained largely contained at 4.2 per cent in August 2025. Excluding precious metals, core inflation was at 3.0 per cent in August 2025. In terms of the inflation outlook for H2: 2025-26, healthy progress of the south-west monsoon, higher kharif sowing, adequate reservoir levels and comfortable buffer stock of foodgrains should keep food prices benign. The recently implemented GST (Goods and Services Tax) rate rationalisation would lead to a reduction in prices of several items in the CPI basket. Overall, the inflation outcome is likely to be softer than what was projected in the August, 2025 MPC resolution, primarily on account of the GST rate cuts and benign food prices. Despite the anticipation of moderate momentum during H2, large unfavourable base effects are likely to exert upward pressure on headline CPI inflation, especially in Q4. Considering all these factors, CPI inflation for 2025-26 is now projected at 2.6 per cent with Q2 at 1.8 per cent; Q3 at 1.8 per cent; and Q4 at 4.0 per cent. CPI inflation for Q1:2026-27 is projected at 4.5 per cent.
- **Growth:** In India, real Gross Domestic Product (GDP), driven by strong private consumption and fixed investment, recorded a robust growth of 7.8 per cent in Q1:2025-26. On the supply side, growth in gross value added (GVA) at 7.6 per cent was led by a revival in manufacturing and steady expansion in services. Available high frequency indicators suggest that economic activity continues to remain resilient. Rural demand remains strong, riding on a good monsoon and robust agriculture activity, while urban demand is showing a gradual revival. Revenue expenditure of the Union and State Governments registered robust growth during the fiscal year so far (April-July 2025). Investment activity, as suggested by healthy growth in construction indicators i.e., cement production and steel consumption in July-August in 2025, is holding up well even though production and import of capital goods witnessed some moderation. Recovery in manufacturing sector continues while services activity is sustaining its momentum. Looking ahead, an above normal monsoon, good progress of kharif sowing and adequate reservoir levels have further brightened prospects of agriculture and rural demand. Buoyancy in services sector coupled with steady employment conditions are supportive of demand, which is expected to get a further boost from the rationalisation of goods and services tax (GST) rates. Rising capacity utilisation, conducive financial conditions, and improving domestic demand should continue to facilitate fixed investment. However, ongoing tariff and trade policy uncertainties will impact external demand for goods and services. Prolonged geopolitical tensions and volatility in international financial markets caused by risk-off sentiments of investors also pose downside risks to the growth outlook. The implementation of several growth-inducing structural reforms, including streamlining of GST are expected to offset some of the adverse effects of the external headwinds. Taking all these factors into account, real GDP growth for 2025-26 is now projected

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at 6.8 per cent, with Q2 at 7.0 per cent, Q3 at 6.4 per cent, and Q4 at 6.2 per cent. Real GDP growth for Q1:2026-27 is projected at 6.4 per cent.

- **Liquidity:** System liquidity, as measured by the net position under the Liquidity Adjustment Facility (LAF), stood at an average daily surplus of ₹2.1 lakh crore since the last MPC meeting in August 2025. Going ahead, the Reserve Bank will continue to be nimble and flexible in its liquidity management. RBI will endeavour to maintain sufficient liquidity in the banking system so that the productive requirements of the economy are met and transmission to money markets and credit markets remains smooth.
- Yields rose by around 1-2 bps from yesterday's close at the time of writing.

Position of Funds

Duration funds:

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

Money market funds:

- The yields at the shorter end of the curve will 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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