

RBI MPC Review

Limited window for further policy easing



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The decision to maintain status quo and an unchanged “neutral” policy stance was unanimous. However the market was monitoring the language of the MPC rather than whether a rate cut would be delivered or not. The steep downward revision in inflation expectations for 2Q and 3QFY26, followed by elevated inflation in 4Q indicates that the window available for policy easing will be limited. Surprisingly, the RBI did not tinker with its growth expectations despite tariff-related headwinds, citing difficulty in predicting the impact of tariffs on growth. The call money rate will continue to remain the operating rate, as per the recommendations of the internal working group on liquidity management framework. The steep depreciation in the INR did not find any mention in the statement. Post the policy announcement, the entire yield curve hardened by ~5bps, indicating that the bond market is not expecting policy easing going forward.

- **Status quo with a neutral stance:** The RBI’s Monetary Policy Committee (MPC) unanimously decided to maintain status quo on policy rates (5.5%) and continue with the “neutral” policy stance. It is worth highlighting that, unlike in the previous policy, this time there is no mention of the potential growth rate to guide for expected policy actions. But the steep downward revision in inflation expectations coinciding with unchanged growth expectations will open up policy space for further easing. The MPC, through its signalling to the bond markets, is indicating that the rate cut cycle has not ended, to avoid any spike in bond yields (as seen post the 50bps cut in Jun’25).
- **Downward revision in inflation expectation; growth steady:** The downward revision in inflation expectations was broadly factored in; however, despite the tariff-related uncertainties, the central bank chose to keep growth expectations unchanged (6.5% FY26). At the global level, the RBI governor indicated that the emergence of a new equilibrium in the new global order would create challenges at the policy level. At the domestic level, high frequency indicators reflected mixed signals; government capex continued to support economic activity and rural consumption continued to be resilient while urban discretionary spending remained tepid. Inflation is projected to inch up from 4QFY26 due to unfavourable base effects after moderating to as low as 2.1% in 2QFY26. Governor Sanjay Malhotra’s comments were similar to those of US Fed Chairman Jerome Powell, indicating that it is difficult to predict the impact on tariffs.
- **Rate transmission still unfolding:** The governor highlighted that the transmission of the 100bps rate cut is still unfolding (71bps in lending, 87bps in deposit rates). Liquidity in the system (INR 4trln) is expected to improve further once the CRR cuts are effective. The internal working group for the review of liquidity management framework recommended that the Weighted Average Call Rate (WACR) should continue as the operating rate, considering it is highly correlated with other money market rates and also due to its effectiveness in transmitting signals across maturities. The group has also recommended continuation of auction of VRRRs and VRRs to align the operating rate with the policy rate. INR’s steep depreciation recently did not find any mention in the statement; however, it is worth highlighting that of the ~2.7% depreciation since Apr’25, bulk of the depreciation (~1.7%) was since 21st July as markets started factoring in the elevated tariffs and the strengthening US dollar.
- **Limited window for further policy easing:** We believe that the market was closely monitoring the language of the governor in today’s policy decision rather than whether a rate cut is delivered or not. With the downward revision in inflation expectation, the RBI effectively indicated that the rate cut cycle has not ended and the terminal rate is lower from here. But the elevated inflation expectation (due to unfavourable base) from 4Q onwards would mean that the window available for policy easing is limited. Hence, the chances of the RBI delivering a rate cut in October increases; moreover, by then, the US Fed would have eased as well. However, the entire yield curve hardened by ~5bps post the policy, indicating that the bond market is not expecting policy easing, going forward.

Key Highlights

- The MPC unanimously maintains status quo along with a neutral stance.
- Steep downward revision in inflation expectation; which reverts in Q4FY26
- Growth projection left unchanged at 6.5% despite tariff related uncertainties.
- The call money rate will continue to remain the operating rate.
- We see limited room for further policy easing between now and Q4FY26.

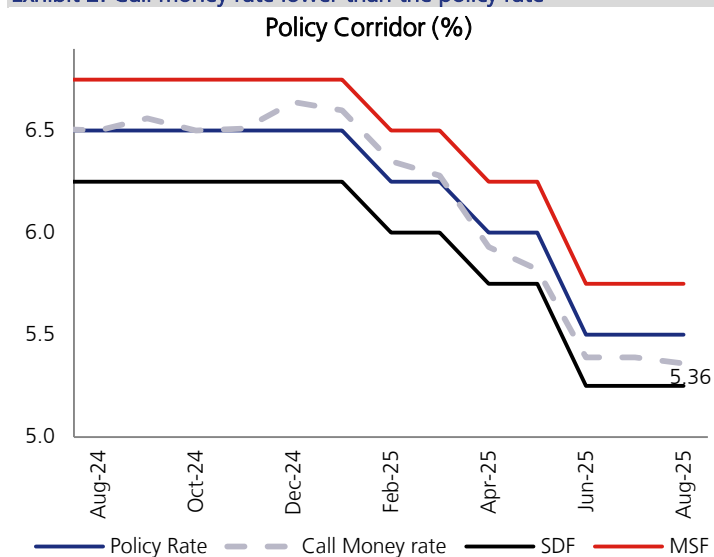
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Exhibit 1. Downward revision in inflation expectation; growth steady

MPC Projections (%)	Q2FY26	Q3FY26	Q4FY26	FY26	Q1FY27
MPC (Aug'25)					
CPI inflation	2.1	3.1	4.4	3.1	4.9
GDP growth(RHS)	6.7	6.6	6.3	6.5	6.6
MPC (Jun'25)					
CPI inflation	3.4	3.9	4.4	3.7	
GDP growth(RHS)	6.7	6.6	6.3	6.5	
Change from Jun'25					
CPI inflation	-1.3	-0.8	0.0	-0.6	
GDP growth	0.0	0.0	0.0	0.0	

Source: RBI, JM Financial

Exhibit 2. Call money rate lower than the policy rate

Source: CMIE, JM Financial

Exhibit 3. Benchmark yields hardened by 6bps post the policy

Source: CMIE, JM Financial

Exhibit 4. Liquidity fine-tuning by RBI

Date	4-Jul	9-Jul	11-Jul	14-Jul	18-Jul	23-Jul	24-Jul	25-Jul	29-Jul	1-Aug	Sub Total
Announced	1,00,000	1,00,000	2,50,000	1,00,000	2,00,000	-50,000	-50,000	1,25,000	50,000	2,00,000	10,25,000
Offers accepted	1,00,010	97,315	1,51,633	57,450	2,00,000	-50,001	-1,421	1,25,008	46,058	1,71,795	8,97,847
Cut off Rate (%)	5.47	5.49	5.49	5.49	5.49	5.53	5.51	5.49	5.49	5.49	

Source: RBI, JM Financial

Exhibit 5. Depreciation in INR post elevated tariff announcement

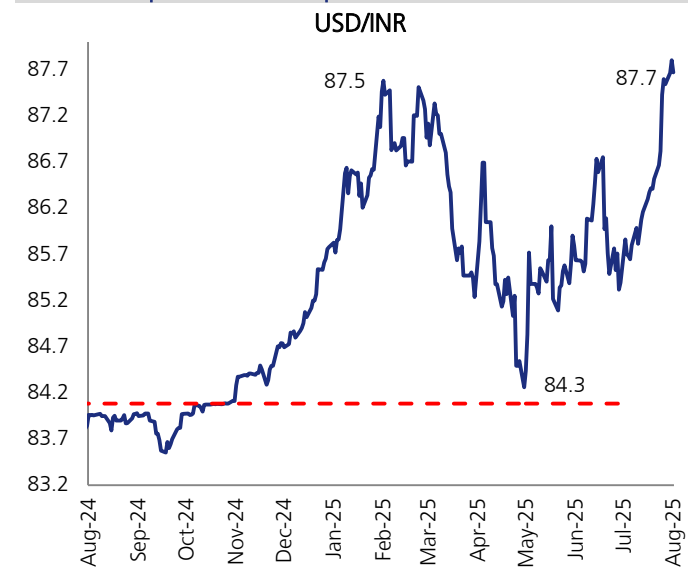
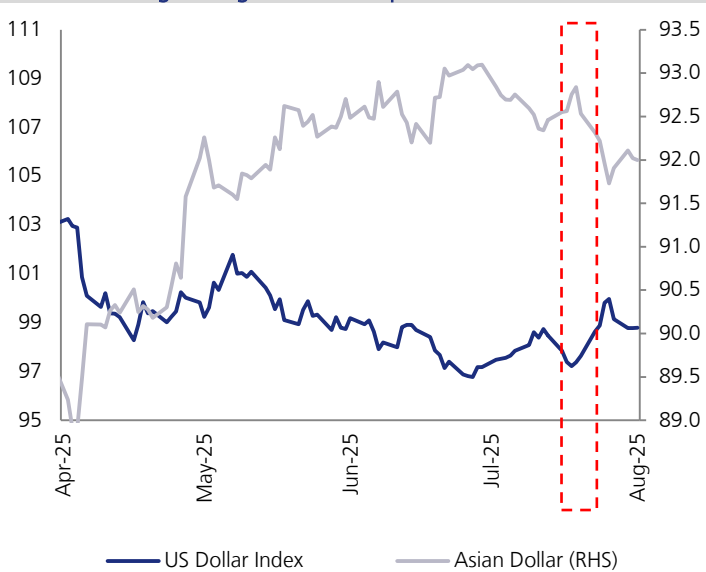


Exhibit 6. Strengthening USD exerted pressure on INR



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