

RBI Monetary Policy Review

1 October 2025



Pause before Play: Buckle up for a 25bps cut in Dec

MPC holds steady as it lets it all play all out: The RBI MPC unanimously decided to maintain a status-quo on policy rates with the Repo Rate held steady at 5.50% and retained the policy stance as neutral. **We see today's policy decision as a dovish pause with the expectation of couple of more rate cuts in this policy easing cycle. We think the factors may play out positively for the RBI-MPC to reduce the Repo rate by 25bps at the December policy while keeping the space open to act again in the current easing cycle.**

On policy stance, while there is no voting, interestingly, two external members of the six panel members opined to change the policy stance to accommodative from neutral earlier. This in a way suggests that the room to cut rates more than once appears more likely as compared to the previous two policies.

So, what changed from the June 2025 policy when it stated 'limited space' to 'opened up policy space' at the October policy? - The growth-inflation forecast table below underpins the change in policy tone, especially when compared to the June 2025 policy decision.

But then, why did the MPC choose to pause at this policy when the outlook has already turned more favorable than the Aug policy? – The MPC is letting the policy actions to play out – both, monetary and fiscal. The policy cited, "...the impact of the front-loaded monetary policy actions and the recent fiscal measures is still playing out."

A quick recap, the RBI-MPC has cut the Repo Rate by 100bps to 5.50% since February 2025 and it also cut the reserve ratio requirement (the CRR) by 100bps which would fully reflect in the system by the time the MPC meets for its Dec'25 policy. The MPC awaits these steps to play out while keeping an eye on monetary policy transmission. In terms of fiscal measures, earlier this year, the govt. announced reduction in income tax rates and recently, rationalized the GST tax rates as well. These steps are seen stimulate growth and consumption.

The growth-inflation dynamics in the current global backdrop and the external headwinds to domestic growth have shaped the monetary policy outlook and policy tone. When compared to the last two policies, after the 50bps rate cut in June 2025, India retail inflation has surprised positively so far in FY26; leading to sharp revisions in forecasts.

The sharp downward revisions in the Aug-Oct MPC policies reflect the rationale behind the changed policy tone. At the same time, the MPC has also revised lower its forward-looking growth forecasts, mainly for 2HFY26 and Q1FY27. Due to a 7.8% GDP growth in Q1FY26, the full-year FY26 GDP growth is revised higher to 6.8% s 6.5% earlier. However, the 50% tariffs imposed on Indian exports by the US administration which kicked in from end-August are seen drag down economic growth. Resultantly, in the wake of the current inflation-growth dynamics the RBI-MPC's policy tone and guidance has turned dovish and the policy resolution thereby has explicitly cited, "...the outlook has opened up policy space for further supporting growth."

Table 1: MPC's growth and inflation forecasts laid out below:

Period	Growth Forecast				Inflation Forecast			
	Jun-25	Aug-25	Oct-25	Revision	Jun-25	Aug-25	Oct-25	Revision
Q1 FY2026*	6.50%	6.50%	7.80%	1.30%	2.90%	2.70%	2.70%	-
Q2 FY2026	6.70%	6.70%	7.00%	0.30%	3.40%	2.10%	1.80%	-0.30%
Q3 FY2026	6.60%	6.60%	6.40%	-0.20%	3.90%	3.10%	1.80%	-1.30%
Q4 FY2026	6.30%	6.30%	6.20%	-0.10%	4.40%	4.40%	4.00%	-0.40%
FY2026	6.50%	6.50%	6.80%	0.30%	3.70%	3.10%	2.60%	-0.50%
Q1FY27	-	6.60%	6.40%	-0.20%	-	4.90%	4.50%	-0.40%

Source: RBI MPC Policy Resolutions, Note: *Provisional GDP data released in August

Growth-inflation outlook: GDP Growth at 7.8% surprised positively in Q1FY26 and despite downward revisions in the 2HFY26 outlook, the growth is estimated at 6.80% YoY for FY26. The Q1FY27 estimate too has been revised lower by 20bps to 6.4% YoY. Growth is seen impacted due to ongoing trade & tariff related uncertainties. However, 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.

The inflation outlook has turned more benign compared to what was projected at the Aug'25 policy aided by GST rate cuts and benign food prices. While the base effects would play out for Mar-Jun 2026 quarters, the forecasts remain largely aligned to the medium-term target of 4.00% YoY. The outlook remains supported by a good monsoon year, higher summer crop sowing, adequate reservoir levels and comfortable buffer stock of foodgrains. For FY26, CPI inflation is revised lower by 50bps to 2.6% YoY and from June policy it has been revised lower by 1.10%; hovering near the lower band of the 4% +/-2% inflation targeting framework. Even for Q1FY27, forecasts have edged lower to 4.5% vs 4.9% earlier.

Liquidity: The RBI did not announce any fresh measures, but did indicate that it will actively manage liquidity to anchor short-term rates. At this policy, the Governor emphasized on policy transmission citing the remaining tranches of the CRR cuts would further facilitate policy transmission. Apart from these monetary policy instruments, we would also be watching for any FX related measures which could influence liquidity levels. More so, because we note that the RBI Governor in his speech stated that, despite the robust domestic macroeconomic fundamentals, the INR has witnessed some depreciation accompanied by phases of volatility. "RBI is keeping a close watch on movements of the INR and will take appropriate steps, as warranted." As per RBI's Monetary Policy Report (MPR), the volatility in global financial markets owing to slowing global trade and demand may exert downward pressure on the currency, going ahead.

Regulatory measures: Apart from the monetary policy, the RBI has announced several regulatory measures which are seen enhance lending activity across sectors. The Governor announced a package of 22-additional measures which were aimed at strengthening the resilience and competitiveness of the banking sector, improving the flow of credit, promoting ease of doing business, simplifying foreign exchange management, consumer-centric measures which aim to enhance consumer satisfaction, and internationalisation of the Indian Rupee. For instance, the focus will be on easing credit standards which include lowering risk weights for lending for non-banking institutions and infrastructure sector; rationalizing several measures for foreign exchange transactions. The steps would reduce bottlenecks for lending, esp. to the MSME sector, and also for giving greater flexibility for lending against financial assets. These measures are a positive, but the immediate impact on credit demand needs to be watched.

Our Take:

The policy outcome was broadly in-line with our expectations, including our assessment on its growth-inflation outlook as well as a dovish (re)positioning of the policy. The pivot in policy tone from "limited space" seen at June policy to "outlook has opened up policy space" is a clear signal to the markets on policy direction. In the current settings of inflation-growth dynamics with inflation likely to surprise positively and headwinds to growth persisting, we believe there is space for the MPC to cut rates by 25-50bps – with the 25bps cut seen delivered at the Dec'2025 meet. After the Dec'25 cut, the next policy move would be contingent upon incoming data and external developments. The two external members opinion to change the policy stance to accommodative from neutral suggests the members might be leaning towards a more accommodative policy. However, we continue to believe that the Dec'25 policy will see a 25bps cut with a neutral stance while leaving the room to cut rates in this easing cycle. The rationalization of GST rates, benign food price levels, good monsoon are seen keep inflation aligned to the medium-term target with inflation seen settle at ~2% near the lower band of the inflation targeting framework. The growth side story too appears a bit somber especially following the recent developments around trade, tariffs and visa fees which together have dampened the growth outlook.

The Governor did highlight that the growth levels are still below the aspirational levels and policy space to act to support growth indicate that the MPC would pay more heed to growth outturn given the comfort around inflation trajectory.

We reiterate that the easing cycle is not over yet and that the room to cut opens-up in the backdrop of the abovementioned scenarios playing out. Since, we believe there is scope for future rate cuts, it has increased our conviction on increasing duration bias across our portfolios. While the SDL calendar will be closely watched, and any higher-than-expected calendar amount might increase the pressure on yields on the extreme long end of the yield curve. We believe the 10–15 year point on the curve offers good relative value with yields softening as rate cut expectations get built in.

Additionally, we continue to remain positive on 2-4 year corporate bonds as this segment may continues to offer favourable spreads. This we believe is the sweet spot on the corporate yield curve. Given liquidity is expected to remain in surplus for the near future, we believe corporate bond spread compression story will continue and provides for an opportunity for further compression in corporate bonds.

Abbreviations:

RBI: Reserve Bank of India
MPC: Monetary Policy Committee
SDF: Standing Deposit Facility
MSF: Marginal Standing Facility
CRR: Cash Reserve Ratio
SDL: State Development Loan
OMO: Open Market Operations
GDP: Gross Domestic Product
CPI: Consumer Price Index
G-Sec: Government Securities
EMs: Emerging Markets
FX: Foreign Exchange

Source - RBI MPC Policy Resolutions, HSBC MF Research, Data as on October 1, 2025.

Note: Views provided above are based on information in public domain and subject to change. Investors are requested to consult their financial advisor for any investment decisions.

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HSBC Mutual Fund, 9-11th Floor, NESCO - IT Park Bldg. 3, Nesco Complex, Western Express Highway, Goregaon East, Mumbai 400063. Maharashtra.

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