

# MPC PREVIEW AUG'25

## Pause in the rate cut with a neutral stance

**Growth Finds Its Feet Amid Persistent External Headwinds:** India's growth momentum in Q1FY26 appears firmly on track, buoyed in part by the RBI's early-FY26 rate cut. While global trade jitters have lingered, the extended tariff pause has brought some respite. Against this uncertain backdrop, the domestic economy has kept up its pace, with high-frequency indicators such as the manufacturing PMI and E-Way bill collections pointing to resilient activity. Once again, government capex remains the primary growth engine, compensating for a still-wobbly external sector. Reflecting this resilience, the IMF recently nudged its India growth forecast up by 20 basis points to 6.4%, just before US declared 25% tariff on Indian exports. The RBI is expected to trim the 6.5% projection, in view of at least limited tariff fallout on exports. With headline inflation subdued, a soft GDP deflator is likely to flatten nominal GDP growth further..

**Inflation: Well Below the Comfort Zone:** June CPI inflation plunged to 2.1%—the second-lowest print since the inception of the current series—marking a fifth straight month below the RBI's 4% target. The lion's share of this downside stems from food prices tipping into deflation, as vegetables posted a tepid seasonal rise and cereals, pulses, and spices eased amid robust supply. Core inflation, once bullion is stripped out, remains tranquil; only minor tremors have been felt from precious metals and a handful of service categories. The disinflationary trend seems set to persist, barring a supply-side shock. On current trends, FY26 inflation should undercut the RBI's 3.7% estimate by a wide margin, leaving the door ajar for further policy easing if external risks crystallise.

**Liquidity: Surplus and Set to Grow:** System liquidity is in rude health, with end-July surplus at Rs. 2.7 trillion—twice April's level. The phased 100 bps CRR cut from September promises to inject another Rs. 2.5 trillion by year-end, while the RBI's record Rs. 2.7 trillion dividend transfer to government coffers adds further ballast. Despite this glut, the central bank is likely to watch the cooling in credit growth with concern: SCB credit expanded just 9.8% year-on-year as of mid-July, down sharply from 14% a year ago. Year-to-date, credit growth is running well behind last year's pace. With inflation well anchored and liquidity management via VRRRs and forex operations already in play, the RBI seems inclined to maintain its surplus stance to nurture credit demand and neutralize the impact of substantial short dollar position of the central bank.

**August Policy: The Case for a Pause:** With inflation well contained but underlying risks still bubbling, the RBI is expected to hold the repo rate steady at 5.50%, having already frontloaded easing through both a rate cut and a 100 bps CRR reduction earlier this year. Surplus liquidity has prompted renewed VRRR operations, underlining the central bank's nimble, data-driven approach. A pause now would allow policymakers to assess the full impact of the monsoon on food prices, the pass-through of earlier easing on economic activity and the impact of disruptive trade policy of the US. The policy stance, in all likelihood, will remain neutral with a dovish bias—entirely in keeping with the RBI's annual report, which puts a premium on supporting growth as inflation ebbs and economic momentum gradually recovers.

**No News is Good News.** With inflation subdued and global uncertainties clouding the horizon, the stage is set for the RBI to continue on a path of policy easing. Yet, given the robust domestic growth and a balance of risks to the inflation outlook, the MPC is likely to keep its powder dry for now. True to its preference for maintaining steady-state real rate in the 100–150 bps range, the RBI is expected to deliver a further 50 basis points of rate cuts over the course of this cycle. In the meantime, a near-term pause and the prospect of more easing ahead both augur well for the economy and financial markets alike.

### Latest figures, y/y %

GDP

7.4

GVA

6.8

CPI

2.1

Core CPI

3.6

Repo Stance

Pause

Liquidity Stance

Accommodative

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