

Reserve Bank of India cuts rates and injects liquidity amid benign inflation

The Reserve Bank of India (RBI) has cut the repo rate by 25bp to 5.25% and announced liquidity measures, including open market bond purchases and FX swaps. With inflation staying below target and growth expected to moderate, we see scope for another 25bp cut in the first quarter of 2026



Indian GDP expanded by a robust 8.2% in the third quarter of 2025

The RBI lowers policy rate and announces measures to inject liquidity

The Reserve Bank of India cut the repo rate by 25bp to 5.25%, in line with our expectations, based on structurally weaker inflation and a cyclical growth correction in 2026. Consensus expectations had shifted against a rate cut following last week's strong third-quarter GDP print.

Alongside the rate cut, the RBI announced open market purchases of government securities worth INR 1 trillion this month and USD/INR buy-sell swap auctions totalling USD 5 billion to inject liquidity into the system.

Importantly, the RBI maintained a neutral policy stance, noting that CPI inflation has eased

significantly, remaining below the lower bound of its target range. While inflation is expected to pick up, it should stay under 4% – the RBI's baseline inflation target – for the first half of next year.

On the growth front, GDP expanded by a robust 8.2% in 3Q, but the RBI projects moderation to 7% YoY in 4Q25 and 6.5% YoY in 1Q26. Overall, the RBI's assessment of the growth-inflation trade-off aligns with ours, suggesting scope for further policy easing.

Growth-inflation balance suggests more room to cut rates

We expect another 25bp rate cut from the RBI in 1Q26, for the following reasons:

1. Stronger monetary policy transmission: The easing cycle that began in February 2025 has gained traction. Banks have steadily reduced repo-linked lending rates, while the marginal cost of funds-based lending rate (MCLR) – which typically adjusts more slowly – has also declined. Notably, the 1-year median MCLR for scheduled commercial banks has fallen by 45bp since February. In turn, the weighted-average lending rate on new rupee loans dropped by about 80bp, while rates on outstanding loans eased by roughly 60bp over the same period. The transmission of lending rates to the market has accelerated significantly since October, when the RBI held rates unchanged.
2. Better transmission of GST rate cuts: October CPI inflation data suggests that the goods and services tax (GST) reductions announced in September have been partially passed on to consumers. Lower prices, particularly for automobiles and electronic goods, helped drive down inflation. Prices of 30 out of 54 daily-use items monitored by the government, including electronics and food items, have seen reductions being made further than expected; others are yet to fully reflect the intended benefits. We estimate that this partial pass-through, combined with sharply lower food prices, will keep inflation well below the RBI's target for the remainder of 1H2026.
3. We expect GDP growth to ease from 7.6% in 2025 to 6.5% in 2026 as momentum slows over the coming quarters from the peak seen in 3Q25. We estimate a 70% likelihood of a trade agreement between India and the US, given recent progress on several contentious issues. However, export growth is expected to remain subdued as the full impact of tariffs takes hold. In addition, the government's commitment to fiscal consolidation, coupled with revenue pressures from lower GST rates, will constrain public spending.

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