

MPC meet October 2025: Decoding RBI's dovish, yet disciplined, hold

Maintaining the repo rate at 5.5% with a neutral stance, RBI Governor Sanjay Malhotra's announcement after the Monetary Policy Committee meeting on October 1 underscores a calibrated approach to India's macroeconomic landscape

By Lekha Chakraborty Updated: October 03, 2025



RBI governor Sanjay Malhotra | PTI/ YouTube

In the intricate stance of monetary policy, where domestic resilience meets global headwinds, the RBI's Monetary Policy Committee (MPC) on October 1, 2025, executed a deft "dovish hold".

Maintaining the repo rate at 5.5 per cent with a neutral stance, Governor Sanjay Malhotra's announcement underscores a calibrated approach to India's macroeconomic landscape: one characterised by sharply easing inflation (revised to 2.6 per cent for FY26), upwardly revised GDP growth (6.8 per cent), and lurking external risks like prospective US tariffs.

I view this decision as strategic prudence, amid subdued inflationary pressures and structural reforms like GST 2.0. At its core, the RBI's stance reflects a forward-looking central bank navigating volatility, ensuring policy transmission aligns with India's growth imperatives.

Interest rate announcement and rally in bond market

The MPC's verdict to hold the repo rate at 5.5 per cent—unchanged since the August status quo, following a cumulative 100 basis points (bps) of cuts in 2025, including a bold 50 bps slash in June—was met with measured market approval.

This neutral stance signals room for future easing without immediate action—a classic dovish pivot amid benign inflation (headline CPI at 2.7 per cent in August, below the 4 per cent target for seven months).

Governor Malhotra's emphasis on “evenly balanced” risks to growth and prices, coupled with quarterly inflation projections (1.8 per cent for Q2 and Q3 FY26, rising to 4 per cent in Q4 and 4.5 per cent in Q1 FY27), reassured stakeholders that the RBI is attuned to softening dynamics driven by GST rate reductions (effective September 22).

Markets indeed responded swiftly. Indian government bonds rallied in early trade, with the 10-year benchmark yield compressing to 6.5578 per cent from 6.5770 per cent the prior day.

This 2 bps dip, amid thin volumes ahead of the announcement, reflects traders' bets on a dovish tilt—guidance hinting at potential 25 bps cuts in December.

Latest monetary policy decisions by Jay Powell and Christine Lagarde

In September 2025, Federal Reserve Chair Jay Powell led the Federal Open Market Committee (FOMC) to cut the federal funds rate by 25 basis points to 4-4.25 per cent—the first easing since December 2024.

This “risk management cut” addresses softening labour demand amid persistent inflation—projected at 2.5 per cent for 2025—while signalling two more cuts by the year-end.

Powell emphasised a data-dependent approach, scrapping the prior “makeup strategy” for inflation overshoots and shifting focus to balanced risks in a resilient, yet challenged, US economy growing at 2.1 per cent.

Meanwhile, ECB President Christine Lagarde’s Governing Council unanimously held key rates steady on September 11—deposit facility at 3 per cent, main refinancing at 3.25 per cent, and marginal lending at 3.5 per cent.

Upward revisions show eurozone inflation at 2.1 per cent for 2025 (from 2 per cent) and GDP growth at 1.2 per cent (from 0.9 per cent), driven by easing energy pressures, but volatile food costs.

Lagarde stressed meeting-by-meeting vigilance to anchor inflation at 2 per cent, ensuring transmission amid tight financing. These moves reflect cautious easing in the US versus steady restriction in Europe, prioritising stability.

Trump tariff effects and RBI policy rates

The shadow of a potential tariff escalation by the Trump administration—potentially hiking duties on Indian exports like textiles, pharmaceuticals, and IT services—loomed large over the MPC’s deliberations, amplifying the rationale for a hold.

With US-India bilateral trade at \$190 billion annually, tariffs could shave 0.5-1 per cent off India’s GDP, disrupting export-led momentum despite Q1 FY26’s stellar 7.8 per cent growth. The RBI’s neutral stance stems from these geopolitical uncertainties.

Central bank stress tests on ‘reserves’ amid geopolitical uncertainties

Geopolitical fissures—from the Middle East tensions to US election volatility—have elevated central bank reserves as a bulwark against exogenous shocks. The RBI’s \$700.2 billion forex buffer stands as a testament to prudent accumulation.

Governor Malhotra’s announcement of a Cash Reserve Ratio (CRR) cut—releasing approximately Rs 1.5 lakh crore in liquidity—targets enhanced banking system fluidity, facilitating credit expansion without eroding reserve adequacy.

Against the IMF’s September 2025 guidance on central bank stress tests—which models balance sheet risks like interest rate and forex shocks to gauge capital needs—implications for India are not insignificant.

Such tests can bolster RBI's resilience, ensuring credibility during balance sheet expansion from liquidity operations.

For emerging markets, it aids risk-based capital decisions, mitigating vulnerabilities in volatile global environs, fostering stable easing without eroding independence.

India's credit deployment

Despite the dovish hold's liquidity infusion via CRR cut, India's credit deployment conundrum persists: a structural chasm between policy signals and real-economy flows.

August's IIP growth deceleration to 4 per cent (manufacturing drag at 3.2 per cent) belies uneven sectoral lending: MSMEs and infrastructure lag at 8-10 per cent YoY growth, versus 15 per cent for large corporates.

Banks parking in RBI's VRRR amid policy corridor

The RBI's policy corridor, centred on the 5.50 per cent repo rate, features a symmetric band: Standing Deposit Facility (SDF) at 5.25 per cent as the absorption floor, and Marginal Standing Facility (MSF) at 5.75 per cent as the lending ceiling.

This framework anchors the weighted average call rate (WACR) near the repo, ensuring stable transmission.

Post-October 1, 2025, MPC's 75 bps CRR cut injected roughly Rs 1.5 lakh crore liquidity, swelling surplus to approximately Rs 5.5 lakh crore.

Banks are parking excess funds via overnight Variable Rate Reverse Repo (VRRR) auctions, which absorb liquidity at auction-determined rates (typically 5.25-5.5 per cent), supplementing SDF utilisation (now roughly Rs 3 lakh crore).

This prevents call rates from dipping below the corridor floor, supporting a neutral stance while curbing inflationary risks from surplus.

However, the Reserve Bank of India (RBI) announced on September 30, 2025—as a part of its revised liquidity management framework ahead of the October MPC meeting—the discontinuation of 14-day Variable Rate Reverse Repo (VRRR) operations as primary tools for short-term liquidity absorption.

These will be replaced by shorter tenors (primarily 7-day options, alongside overnight to 14-day options based on needs), while retaining the overnight VRRR for fine-tuning.

This shift aims to align the weighted average call rate (WACR) more closely with the 5.50 per cent repo rate amid persistent surplus liquidity (roughly Rs 5.5 lakh crore, post-CRR cut).

Daily VRR (injection) auctions were earlier discontinued from June 11, 2025, due to easing tightness.

Fiscal costs

No direct fiscal costs emerged from the decisions; instead, the dovish pause supports fiscal sustainability by stabilising bond yields (the 10-year G-sec dipped by about 6 bps post-announcement), reducing government borrowing expenses amid a 90 per cent debt-GDP ratio.

Fiscal-monetary coordination—a linchpin of India's stability—shines through the RBI's hold, affording the Centre breathing room amid a projected 5.1 per cent deficit (FY26) and gross debt at 82 per cent of GDP.

GST 2.0's rate rationalisations—slashing effective rates by 100-200 bps on essentials—have catalysed disinflation (SBI's October CPI at 1.1 per cent) and revenue buoyancy (Rs 1.8 lakh crore collections in September).

To conclude, the RBI's October pivot—dovish yet disciplined—navigates India's ascent with foresight, leveraging reserves, macro-fiscal reforms, and synergies for resilient economic growth.

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