Implications of December 2025 MPC

The Monetary Policy Committee (MPC) which met on December 3-5, 2025 announced the following measures after deliberating the current global and domestic scenario:

1. A cut in the policy repo rate by 25 bps to 5.25% with a neutral stance. Consequently, the MSF and SDF rate stand at 5.5% and 5.0% respectively.
2. Open market Operations of government securities aggregating to Rs 1 lakh crore in two tranches starting December 15.
3. A dollar -Rupee buy/sell swap worth $ 5 Bn for a tenor of 3 years.

Majority of market participants had expected a pause in rates taking a cue from better-than-expected GDP growth for the second quarter. The neutral policy stance signifies the central bank's commitment to flexibility for future rate actions.

As expected, GDP growth estimate for FY26 has been revised upwards by 50 bps to 7.3% from the earlier 6.8%. This revision reflects the strong momentum in the domestic economy, supported by robust Q2 growth of 8.2% and the impact of US tariffs being mitigated to a great extent by export diversification and robust services exports. The MPC also alluded to strong external sector metrics.

MPC Growth (Real GDP) forecasts:

	Q2FY26	Q3FY26	Q4FY26	FY26	Q1FY27	Q2FY27
June 2025	3.4	3.9	4.4	**3.7**	4.5	-
August 2025	6.7	6.6	6.3	**6.5**	6.6	-
October 2025	7.0	6.4	6.2	**6.8**	6.4	-
Dec 2025	8.2	7.0	6.5	7.3	6.7	6.8

CPI inflation forecasts

	Q2FY26	Q3FY26	Q4FY26	FY26	Q1FY27	Q2FY27
June 2025	3.4	3.9	4.4	**3.7**	4.5	-
August 2025	2.1	3.1	4.4	**3.1**	4.9	-
October 2025	1.8	1.8	4.0	**2.6**	**4.5**	**-**
Dec 2025	1.7	0.6	2.9	**2.0**	**3.9**	4.0

The announcement of OMOs were also widely expected as liquidity could be under pressure due to advance tax outflows, credit growth outpacing deposit growth and RBI intervention to support the rupee which has depreciated by more than 5% so far this calendar year. The $5 Bn buy sell swaps is also aimed at facilitating orderly liquidity conditions.

After the measures announced today, overall liquidity scenario would be as below:

Particulars	**(Rs lakh Cr)**
Current surplus	2.66
Injection due to 5 Bn swaps	0.45
Deposit growth @ 0.8%	2.0
OMOs announced	1.0
Total surplus	6.11
Advance tax payments	1.5
GST (net of refunds)	-1.7
FX intervention $3 Bn	-0.27
IPO related	-0.3
Total expected outflows	-3.5
Net surplus	2.34

Taking into account likely sources of inflows and outflows net surplus liquidity of Rs 2.34 lakh crore is expected by end December which would be approximately 0.97% of NDTL. This aligns with the central bank target of maintaining liquidity surplus at 1% of NDTL and helps to keep the weighted average call rate closely aligned to the repo rate, as per the liquidity management framework of RBI.

As on December 4, Government cash balances with RBI amounts to Rs 7.16 lakh crore some of which could return to the system and facilitate improvement in liquidity conditions.

10-year benchmark yields softened by 3 bps immediately after the policy but settled unchanged at 6.52% later. The 10-year G-Sec repo spread is currently 125 bps which is almost similar to past trends (at the current level of repo rate). Hence, yields are not expected to soften due to the current rate cut. However, if bond index inclusion brings in flows of $20-25 Bn, there could be some softening of yields while also supporting the exchange rate. The outcome of US Federal Reserve meeting on December 10 would be the next major policy move to watch out for further cues on exchange rates.

Implication Monetary developments & Regulatory developments

1. By announcing the repo rate cut. MPC has stuck to the original mandate of inflation targeting framework. As average inflation for Q3 at 1.7% is below the lower bound of 2%, the rate cut was triggered. Producers impacted by lower realization due to subdued inflation will benefit by way of lower cost of funds while savers will not be affected even if nominal rates fall as real interest rates will remain high due to low inflation. Repo linked rates will come down immediately. Retail loans including housing, vehicle and education loans will become cheaper and will add to the impact of 100 bps reduction since February to augment consumption. Transmission of past repo rate cut of 100 bps has been satisfactory with weighted average lending rates on fresh rupee loans declining by 69 bps during Feb-October 2025. As regards the impact of rupee depreciation RBI study observes that a 5% depreciation has a 25-bps impact on inflation but will also boost GDP growth by 25 bps due to stronger exports.

Repo rate cut impact on banking sector

Particulars	Rs lakh Crore
Gross domestic advances (1)	193.45
Assuming repo linked adv @50% (2)	95.22
Loss in int income due to 25bps cut (3)	**0.24**
Reduction in yield on advances (bps) (3/1) (4)	12.4
Total time deposits (5)	211.0
Cut in term deposit rates to offset loss (bps)(3/5)	**11 bps**

For the industry as a whole, an overall reduction of 12 bps in yield on advances is expected and term deposit rates might see a reduction of around 10 bps to offset the impact.

2. The announcement 0f OMOs will help to maintain orderly liquidity conditions. The impact on yields would depend on the tenor of the OMOs. In any case, the yield impact due to OMOs would be incidental and temporary as the objective is primarily to manage liquidity. By resorting to OMOs, durable liquidity of Rs 1 lakh crore will be injected.
3. Dollar-rupee buy sell swaps of $5bn will inject around Rs 45000 Crore and complement OMOs while adding marginally to the forex reserves. Forex reserves are currently $688 bn, sufficient for 11 months of imports. However, after accounting for forward book of $63bn 'core reserves' would be $625 bn which will increase to $630 bn after the swap which would still be sufficient for 10 months of imports.

The MPC has tuck to the fine print of flexible inflation targeting framework while announcing the 25-bps repo rate cut. Inflation targeting, rather than growth is the primary mandate of the MPC. Liquidity injections using OMOs and buy sell swaps have been done to ensure orderly liquidity conditions and by maintaining a neutral stance, necessary policy flexibility has been retained.

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Madhavankutty G (Chief Economist)