

Policy Brief

RBI's 50 bps Rate Cut: A Bold Move Amid Growth Concerns

Summary:

On June 6, 2025, the Reserve Bank of India (RBI) reduced the repo rate by 50 basis points — its steepest cut in recent years — signaling a shift from policy caution to growth support. This move comes at a time when inflation has moderated but growth remains uneven. The RBI's own 2025–26 growth forecast of 6.5% stands in contrast to the **World Bank's revised projection of 6.3%**, released just four days later. The divergence underscores the uncertainty in India's macroeconomic outlook and raises key questions about the durability of growth momentum.

Background:

India's post-COVID recovery has been robust, but recent indicators suggest some cooling. Exports have been impacted by slowing global trade, private investment remains uneven, and household consumption shows signs of fatigue. Meanwhile, inflation has eased and remains within the RBI's 2–6% comfort band, offering policy space to support growth.

Globally, major central banks like the U.S. Federal Reserve and the ECB have either paused or moderated their rate hikes, reducing pressure on emerging economies like India to maintain high interest rate differentials.

The June 6 Decision:

The Monetary Policy Committee (MPC) voted to cut the repo rate by 50 basis points, bringing it to 5.50%. The RBI cited persistent slack in certain segments of the economy and the need to reinforce the growth impulse. The move was sharper than market expectations, reflecting either stronger internal concerns or a strategic preemptive shift.

Critical Analysis:

The steepness of the cut suggests deeper worries:

- **Is growth flattening?**

The RBI's 6.5% growth projection appears optimistic in light of the World Bank's new 6.3% estimate (Global Economic Prospects, June 2025). This discrepancy hints at increasing external and domestic risks to growth.

- **Sectoral signs of stress**

Interest-sensitive sectors like **real estate, construction, and consumer durables** may be experiencing widening output gaps. Exports, especially **gems, jewellery, and leather** remain weak, impacting jobs and manufacturing growth. Corporate operating profits fell to **9.9% in FY25**, the lowest in four years, signaling weakening business margins outside the financial sector. There has been elevated defaults in the micro finance sector indicating strain in low-income borrower segments and declining rural credit absorption.

- **Rural demand fragility**
Concerns about rural consumption, linked to monsoon uncertainty, may also have influenced the RBI's dovish pivot.
- **A preemptive liquidity boost**
The cut could be aimed at shielding MSMEs and vulnerable borrowers from financial stress in a high interest rate environment, even as headline credit growth appears stable.

However, this move does have risk around it:

- If global food or oil prices rise unexpectedly, the **real interest rate buffer** may shrink, forcing a policy reversal, which can be harmful for RBI's credibility.
- A premature cut could also stimulate speculative activity, majorly in housing and equity markets.

Implications:

- **Short-term boost to investor optimism**, especially in NBFCs, housing finance, and consumption-related sectors.
- **Mild rupee weakening**, but global rate cycle moderation with the Fed leaving the interest rate unchanged should reduce capital flight risk.
- RBI will face pressure to **prove inflation control credibility** in subsequent quarters.

Conclusion:

The RBI's 50 bps rate cut signals a strategic shift to prioritize growth risks — possibly before they fully materialize in headline data. Yet, with global forecasts softening and fiscal space constrained, this easing cycle may need to be recalibrated quickly if inflation pressures resurface. In this balancing act, the RBI must continue to project confidence without appearing disconnected from external realities.

-Vaishnavi Varrier

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