DEAR ECO THINK
Issue No.94/ July 2025

1. State of the Indian Economy

RBI Monetary Policy Committee cuts repo rate by 50 bps and CRR by 1%: The Reserve Bank of India (RBI) Monetary Policy Committee (MPC) has cut Repo rate by 50 bps to 5.50% and changed its stance from 'Accommodative' to 'Neutral'. The rate cut has been undertaken with the objective to maintain growth momentum. With this decision RBI hopes to fulfil the objective of achieving the medium-term target for consumer price index (CPI) inflation of 4 per cent within a band of +/- 2 per cent, while stepping up growth momentum. RBI also announced a 100-bps reduction in the Cash reserve Ratio (CRR), from 4% to 3% of net demand and time liabilities (NDTL). This reduction will be implemented in four equal tranches of 25 bps each, beginning from the fortnights starting September 6, October 4, November 1, and November 29. The phased CRR cut is expected to release about Rs 2.5 lakh crore of primary liquidity into the banking system by the end of November 2025.

CII projects India's FY26 GDP growth at 6.4-6.7%: Confederation of Indian Industry forecasts India's GDP growth to grow at 6.4-6.7% in FY 26, driven by domestic demand. The industry body urges tax, land, and logistics reforms while warning of global headwinds and mineral shortages impacting key sectors like auto. It suggests that to be able to meet the developmental and infrastructure needs, while maintaining the fiscal balance, a focus on augmenting government revenues through calibrated disinvestment of public sector enterprises is required.

Core sector growth drops to a nine-month low: India's combined index of Eight Core Industries (ICI) increased by 0.7% (provisional) in May 2025 as compared to the Index in May 2024. This marks the slowest growth in nine months, following a tepid 1% increase in April and 4.5% in March. The subdued performance was largely due to a sharp contraction in electricity generation, which fell 5.8%, and continued weakness in fertiliser (-5.9 %) and natural gas (-3.6%) output. Crude oil production also declined by 1.8% in May 2025 over May 2024. The core sector accounts for nearly 41% of the index of industrial production (IIP), and the outcome of the sector has a bearing on the overall factory output numbers.

Agri yield could drop 25% due to climate change: India's agriculture sector could face up to 25% yield losses due to climate-related disruptions, according to a new report by Federation of All India Farmer Associations (FAIFA). It called for targeted policy action to improve adoption of climate-resilient technologies among small and marginal farmers, according to a report by a farmers' body. The study stressed on the urgent need for sustainable farming practices to counter climate change impacts and cited high initial costs, fragmented infrastructure, and low farmer awareness as key barriers of widespread adoption regarding sustainable farming practices. It called for targeted subsidies for renewable energy, micro-irrigation and organic inputs, while advocating for large-scale adoption of conservation agriculture and integrated farming systems.

PMI touches 14-month high to 61.0: The HSBC Flash India Composite Purchasing Managers' Index (PMI), compiled by S&P Global, jumped to a 14-month high of 61.0 in June month from 59.3 in May. India's private sector activity accelerated sharply in June as companies ramped up production to meet surging domestic and international demand. Services gained momentum with the activity index rising to 60.7 in June from May's 58.8 – the strongest since August last year—while manufacturing gained pace due to robust output and its PMI climbed to 58.4 in June from 57.6 in May.

Net direct tax collection dips 1.39%: Net direct tax collection for the current financial year slipped 1.39% to ₹4.59 lakh crore as of 19 June 2025. The dip is attributed to muted growth in advance tax payments and a surge in refund issuances. Advance tax collections, a key indicator of corporate profitability and individual income, rose by just 3.87% year-on-year to Rs 1.56 lakh crore. This is a sharp slowdown compared to the 27% growth recorded during the same period last year.

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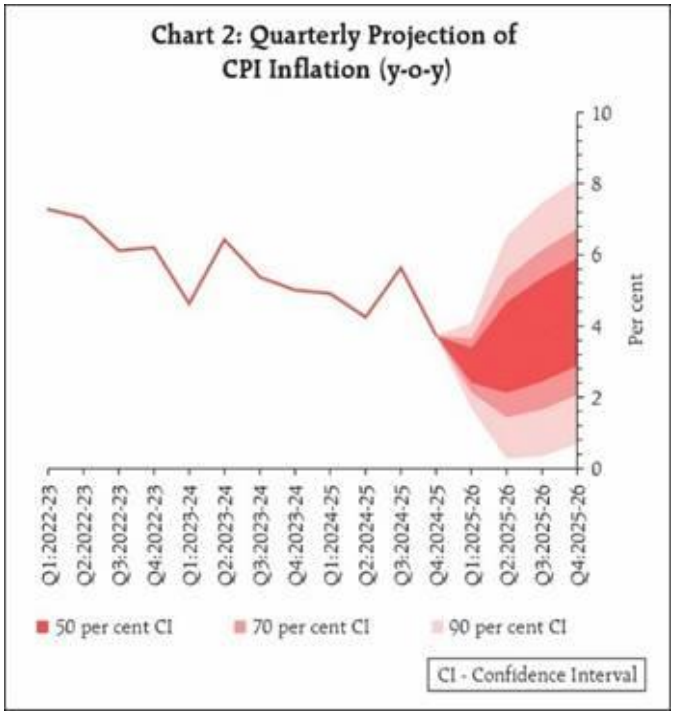
Published by Department of Economic Analysis and Research (DEAR), NABARD Head Office, Mumbai

June GST collection drops below ₹2 lakh crore mark: India's gross Goods and Services Tax (GST) collection went up by 6.2% on-year for the month of June to ₹1.84 lakh crore. However, on a month-on-month basis, GST collection during the month dipped as April 2025 recorded GST worth ₹2.37 lakh crore, followed by ₹2.01 lakh crore in May.

2. Inflation Outlook

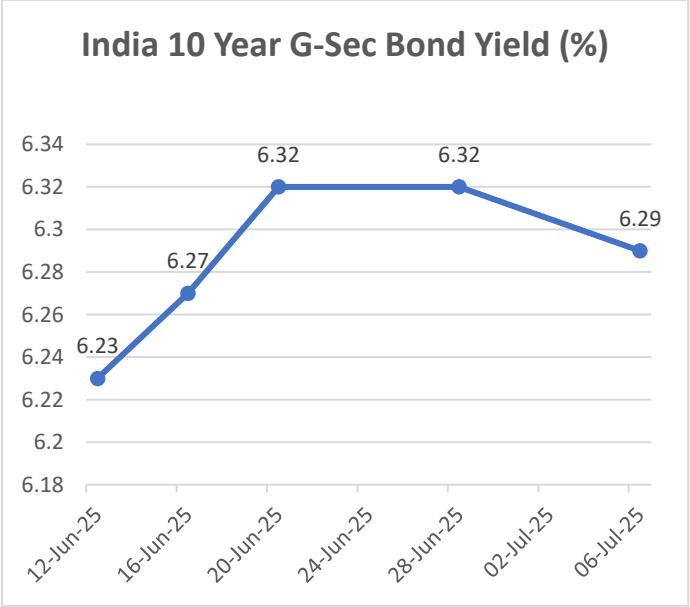
As per the RBI Monetary Policy Committee Report of June 2025, the CPI headline inflation continued its declining trajectory in March and April, with headline CPI inflation moderating to a nearly six-year low of 3.2% (year-on- year) in April 2025. Food inflation recorded the sixth consecutive monthly decline. Core inflation remained largely steady and contained during March-April. The muted core inflationary pressures likely reflect lower global commodity prices, India's increased reliance on Chinese imports, weak domestic growth, and muted second-round effects through lower household inflation expectations and wage growth.



Source: PIB

3. Interest Rate Outlook

India-US bond yield gap narrows to 1.88% points: The yield gap between India's 10-year government bond and the US 10-year Treasury note has narrowed significantly, falling to just around 1.88% points, a far cry from the 6.35% points spread seen in 2014. The development comes amid a steady drop in Indian bond yields driven by easing inflation, a dovish monetary policy stance from the Reserve Bank of India (RBI) and improving macroeconomic fundamentals. This narrowing is not merely a result of reduced risk premiums but highlights India's fiscal discipline, manageable debt levels, and inflation staying within the central bank's comfort range. India has consistently met its fiscal consolidation targets over the past three years, with a fiscal deficit goal of 4.4% set for FY26. The debt-to-GDP ratio stands at a more manageable ~82%, and inflation has remained stable in the 4–4.5% range.



Source: worldgovernmentbonds.com

Outlook: The narrowing yield gap makes Indian government securities less attractive to foreign institutional investors (FIIs), who will now seek higher risk-adjusted returns elsewhere. Lesser FII inflows, and potentially elevated outflows may be expected unless the yield gap widens again. Indian mutual funds and insurance companies are shifting towards an accrual strategy to capitalise on higher corporate bond yields, as government bond yields are expected to remain largely stable. Fund managers are increasingly favouring shorter-duration bonds when yields are near the upper end of the range.

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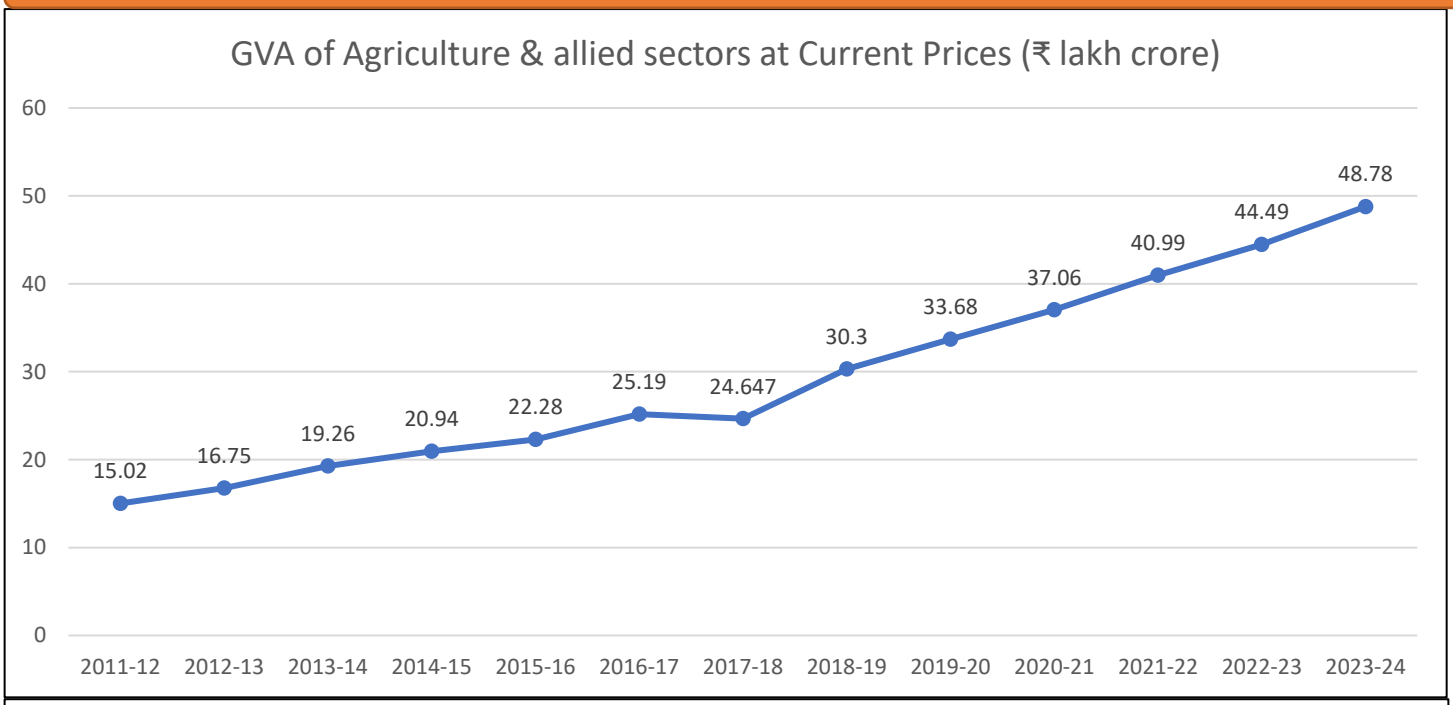
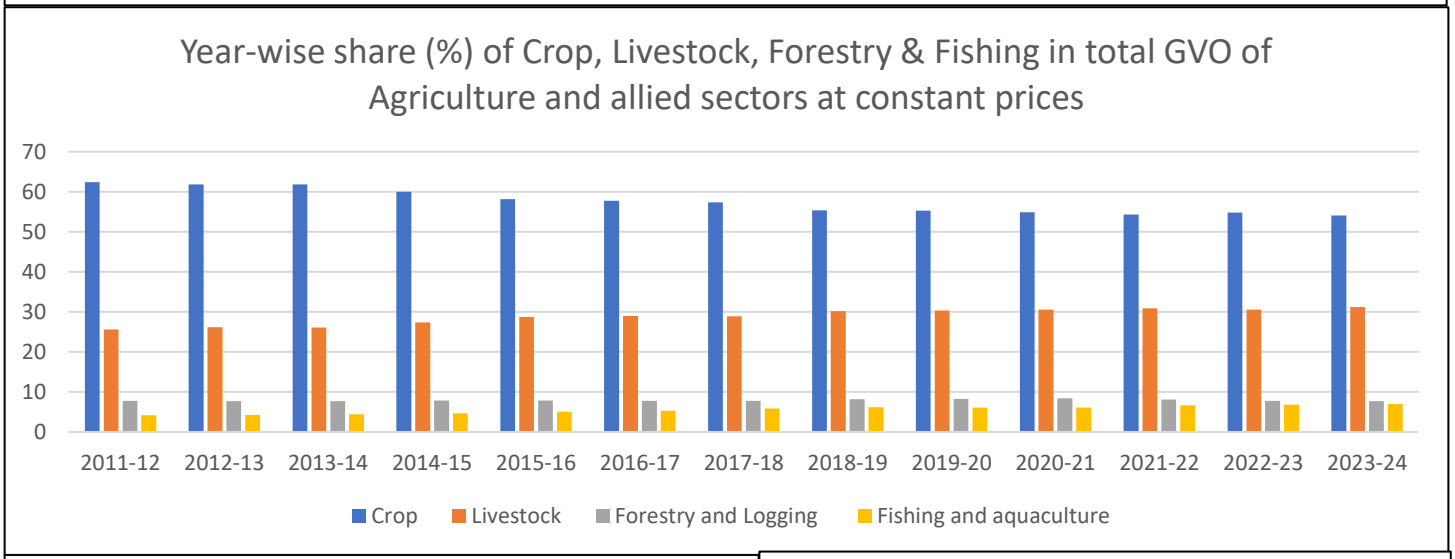
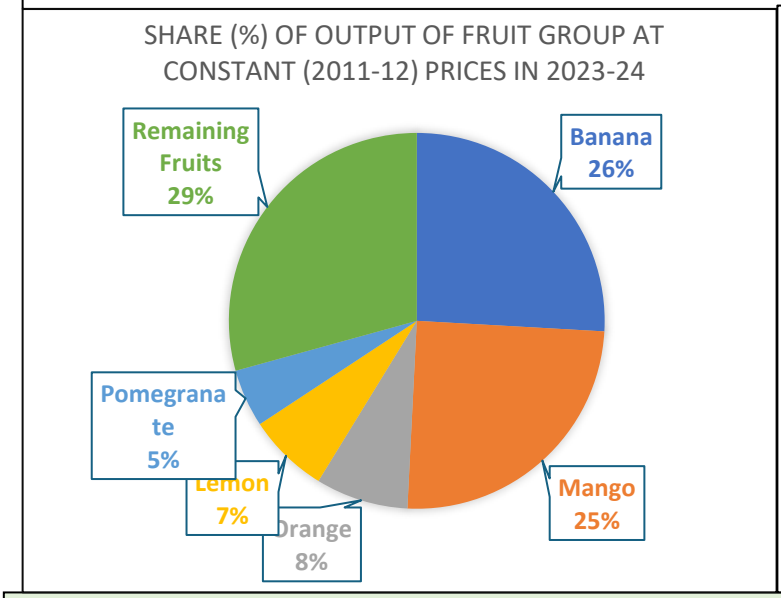
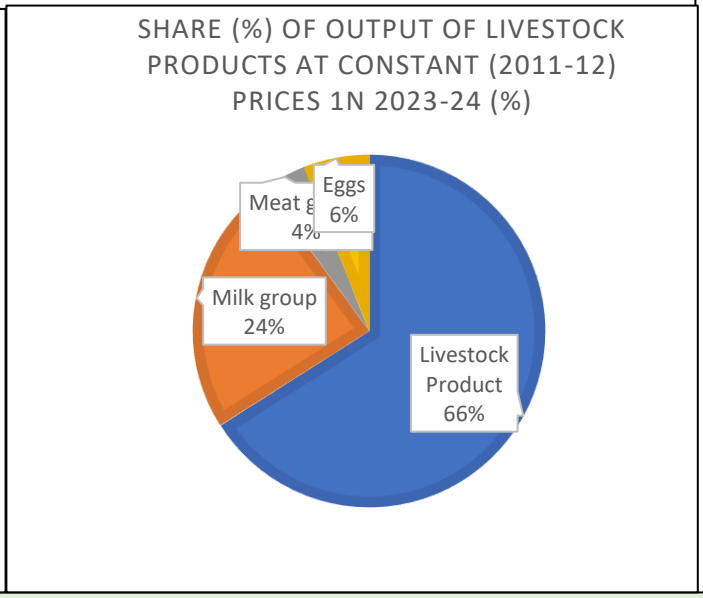
Dashboard on Value of Output from Agriculture and Allied Sectors









Source: Statistical Report on Value of Output from Agriculture and Allied Sectors, NSO, MOSPI

Report THINK

RBI Financial Stability Report- June 2025

The Financial Stability Report (FSR) is a half-yearly publication, with contributions from all financial sector regulators. It presents the collective assessment of the Sub Committee of the Financial Stability and Development Council on current and emerging risks to the stability of the Indian financial system. The report is intended to serve a vital purpose – identify systemic risks, assess the resilience of the financial system, and inform policy direction.

Key Findings from the Report

Global Macro financial Risk: Elevated economic and trade policy uncertainties are testing the resilience of the global economy and the financial system. Multilateral agencies have downgraded global growth forecasts largely reflecting trade disruptions and heightened volatility. Financial markets remain volatile, especially core government bond markets, driven by shifting policy and geopolitical environment. Alongside, existing vulnerabilities such as soaring public debt levels, excessive risk taking in the non-banking financial sector and elevated asset valuations have the potential to amplify fresh shocks. As countries confront varying trade-offs between growth and inflation, monetary authorities are charting divergent policy trajectory.

Domestic Macro financial Risks: The Indian economy continues to grow at a healthy pace, which coupled with steadily moderating inflation, is aiding macroeconomic and financial stability. The domestic financial system is exhibiting resilience fortified by healthy balance sheets of banks and non-banks. Financial conditions have eased supported by accommodative monetary policy and low volatility in financial markets. The strength of the corporate balance sheets also lends support to overall macroeconomic stability. The RBI has projected the real GDP to grow at 6.5 % in 2025-2612, same as in 2024-25, supported by buoyant rural demand, revival in urban demand, an uptick in investment activity on the back of above-average capacity utilisation, governments continued thrust on capex and congenial financial conditions

Financial Institutions: Soundness and Resilience: The soundness and resilience of scheduled commercial banks (SCBs) are bolstered by robust capital buffers, multi-decadal low non-performing loans and strong earnings. Furthermore, macro stress test results showed that SCBs' aggregate capital levels will continue to remain above the regulatory minimum even under adverse stress scenarios.

Regulatory Initiatives and Other Developments in the Financial Sector: Globally, financial sector regulators in most major economies have implemented measures to strengthen the financial system by bringing key reforms in liquidity management, credit risk regulation and securitisation practices. Domestic regulators are actively implementing a series of regulatory reforms aimed at enhancing the stability, transparency and inclusiveness of the financial system in line with global best practices. These initiatives focus on combating financial and digital fraud, promoting liquidity resilience, regulating digital lending and safeguarding retail investors.

Assessment of Systemic Risk: According to the latest round of the Reserve Bank's systemic risk survey (SRS) conducted in May 2025, all major risk groups remain in the 'medium risk' category. Respondents remained optimistic about the soundness of the domestic financial system, with 92 % expressing higher or similar level of confidence in the Indian financial system. Around two-thirds of the respondents expressed decreasing confidence in the stability of the global financial system. Geopolitical conflicts, capital outflows and reciprocal tariff/trade slowdown were identified as major near-term risks to domestic financial stability

About FSDC

Genesis: It is non-statutory body set up by the Government as the apex-level forum in 2010.

Chairman: Union Finance Minister.

Members: Heads of financial sector Regulators (RBI, SEBI, PFRDA, IRDA & FMC), Finance Secretary, etc. In 2018, FSDC was reconstituted to include more members.

Functions: The Council deals, inter-alia, with issues relating to financial stability, financial sector development, and inter–regulatory coordination, etc.

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