India

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India: Tensions, trade, and the technical

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- Geopolitical tensions with Pakistan escalated on 7 May, and tensions will unlikely abate in the near-term keeping sentiment on edge. This is notwithstanding progress on trade deals with the UK and reportedly US.
- The fundamentals remain skewed towards slowing growth momentum and cooling inflationary pressures.
- This justifies Reserve Bank of India's (RBI) dovish stance, and we expect RBI to cut its policy rate by 25bp at its 6 June meeting. We are also adding a cumulative 50bps in rate cuts through to end-March 2026.

Geopolitical tensions

Geo-political tensions between India and Pakistan remain a key focus. Tensions between the two countries have escalated and could remain elevated in the near-term considering minimal reconciliatory chatter. That said, the Government of India stated that its actions "have been focused, measured and non-escalatory in nature" suggesting targeted rather than widespread escalations. Civil society drills, the first since 1971, will take place across 244 districts across the country[1].

The subcontinent is no stranger to this type of brinksmanship. India has closed border crossings, removing diplomats, banned imports from Pakistan, closed its airspace and ports to Pakistan and Pakistan-flagged ships and held the Indus water treaty 'in abeyance'. Arguably, these are the lower hanging fruits compared to military escalation. The situation warrants close monitoring, and sentiment will likely remain pressured in the near-term.

Tariff updates

Against this backdrop of rising geo-political tensions, trade talks with the US have reportedly progressed. US President Donald Trump noted on 6 May that "India has one of the highest tariffs in the world. We are not going to put up with that, they have agreed already to drop it, drop it to nothing. They have already agreed. They wouldn't have done for anybody else, but me."[2]

[1] This drill will be held at 4pm IST in bigger states.
[2] India has dropped tariffs on US imports to 'nothing', says Trump amid trade deal talks with New Delhi, Money Control, 6 May 2025.

Meanwhile, India and UK have signed a trade deal – the result of three years of negotiations. UK noted that agreement will boost bilateral trade by £25.5bn a year from 2040. India will reduce levies on products from the UK and according to the UK government, based on current trade alone, India's tariff cuts amount to £400m in the first year, going up around £900m after 10 years[3].

This underscores our broader view for India and ASEAN-5 wherein the rise of US protectionism will catalyse regional authorities into diversifying trading and investment partners to bolster external engagement prospects.

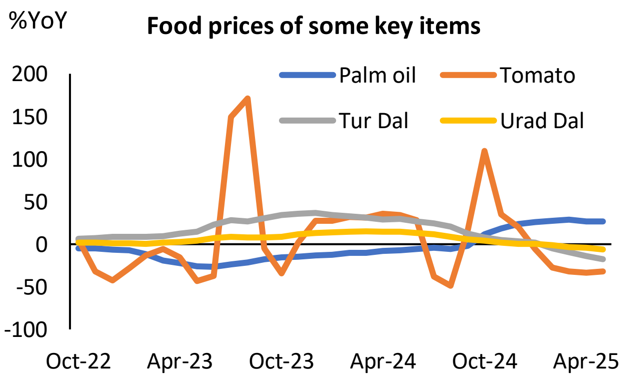
Growth momentum remains volatile

This will hold the economy in good stead over the medium-term, even as near-term growth momentum maybe losing traction. Based on monthly activity data, we estimate that 1Q25 GDP growth will slow to 5.9% YoY versus 6.2% in 4Q24. For FY25 (i.e., April 2024 until March 2025), we expect GDP growth will average 6.0% versus 9.2% in FY24.

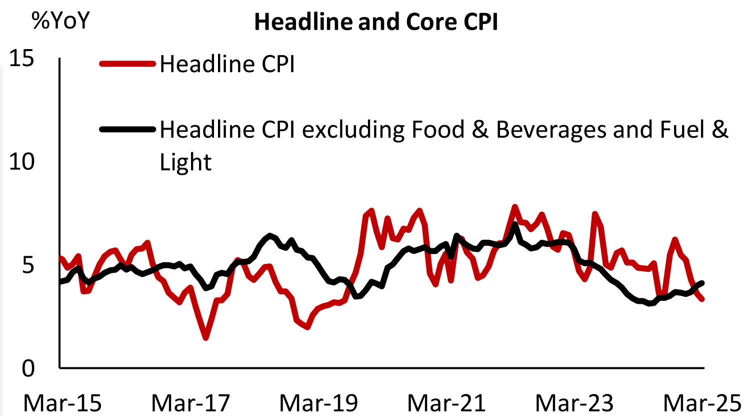
Although the Indian economy is more insulated than the other smaller, open ASEAN-5 economies, growth momentum is likely to remain under pressure for the remainder of the year. We forecast FY26 GDP growth to average 6.0% YoY, with the balance of risks skewed to downside. RBI has a higher FY26 growth forecast of 6.5%. First data indicators for FY26 such as April GST collections suggest a stabilisation in underlying demand momentum.

Inflation will likely ease further in April

Coinciding with slower GDP growth, we expect the disinflation momentum to continue. We see April CPI inflation coming in at 2.9% YoY versus 3.3% in March on the back of lower vegetable and pulses prices even as pal oil prices remain elevated. Simultaneously, easing retail petroleum prices (albeit at a slower rate compared to March) will also continue to support the disinflation trajectory.



Source: CEIC, OCBC.



Source: CEIC, OCBC.

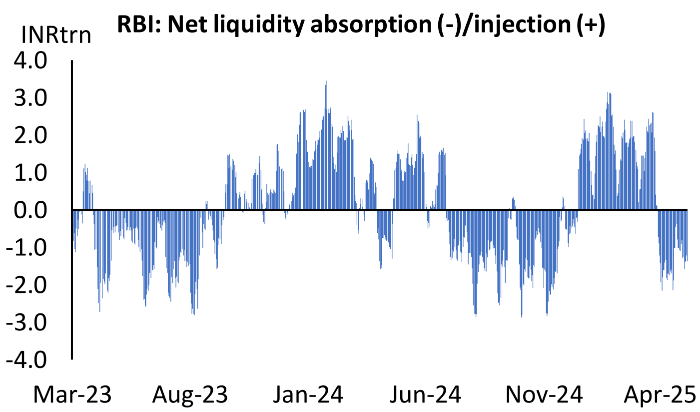
[3] UK-India Free Trade Deal: A Deal for Growth (GOV.UK, published 6 May 2025, accessed on 7 May 2025)

Notwithstanding, we expect headline inflation to inch higher through the rest of the fiscal year. For FY26, we expect headline CPI to average 4.3% YoY versus 4.6% in FY25, marginally higher than the RBI's forecast of 4.0% in FY26.

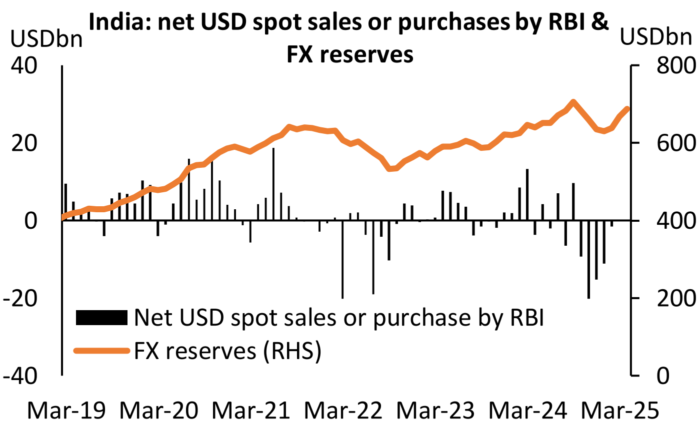
RBI: Adding to our rate cut expectations

The slowing growth and inflation outlook justified RBI's shift to a more dovish stance at its 9 April meeting. We expect the RBI will cut its policy rate again by 25bp at its 6 June meeting, taking the policy rate to 5.75%.

Following this, we are adding an additional 50bps in rate cuts to RBI, taking the policy rate to 5.25% by end FY26. The RBI will continue to maintain comfortable liquidity conditions. It continues to inject liquidity into the markets, even as it slows net USD purchases. FX reserves have risen in recent months to be USD688.13bn, as of 25 April.



Source: CEIC; OCBC.



Source: CEIC; OCBC.

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