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Economic Round-up: May 2025

After a brief respite, global trading system was once again hit with tariff driven uncertainty. At the start of the month, there were clear indications of a softer US tariff policy. US-UK trade deal was finalised, US and China agreed to start negotiations on a trade deal, and tariffs on EU were also paused for a 90-day period. Markets also cheered a US court ruling which quashed President Trump's Liberation Day tariffs as unconstitutional, which was subsequently appealed and reinstated. Reigniting fresh concerns on the tariff front, US President doubled the tariff on imports of aluminium and steel. Even as the world grapples with the continuously evolving US tariff policies, concerns have mounted over the debt burden in some countries. A rating downgrade in the US and a sharp sell-off in the Japanese long-term bond market, exacerbated these concerns. Global central banks are continuously navigating the changing tariff narrative, even though range-bound global commodity prices have provided some headroom for policy easing. In India, inflation is expected to ease further paving the way for RBI to cut rates further by 25bps in this meeting. The economy is expected to exhibit steady growth, underpinned by a favourable monsoon outlook and improvement in consumption and investment growth.

Global growth prospects: OECD downgraded its global growth estimate for 2025 to 2.9% from 3.1% estimated earlier and 3.3% in 2024. For 2026 as well, growth is now projected lower at 3% in 2026, lower by 10bps than its earlier estimates. Trade related uncertainty, increased protectionism, tighter financial conditions and worsening consumer and business confidence is likely to weigh on growth prospect. Inflation is also expected to moderate more slowly than expected. Major downward revisions were noted in growth in US, Canada, China and Mexico. India is expected to remain the fastest growing major economy with GDP growth of 6.3% in FY26 and 6.4% in FY27. Consumption and private investment growth is expected to pick up supported by tax incentives, rate cuts and government support. CPI inflation is expected to average around 4% in both FY25 and FY26.

Key macro data releases: GDP growth for Q4 FY25 surprised positively and rose by 7.4% from 6.4% in Q3FY25. For FY25, GDP growth rate of 6.5% was on expected lines. **CPI inflation** in India moderated further to 67-month low at 3.2% in Apr'25 versus 3.3% in Mar'25. The moderation in headline inflation was led by a broad-based deceleration in food prices. In particular, prices of vegetables and pulses noted the maximum decline. **Core CPI** remained largely sticky at 4.1%. Outlook on inflation is favourable supported by projection of a normal monsoon. This is likely to spur the RBI to cut the policy rate by another 25bps, when it meets this week. **INR** depreciated by 1.3% in May'25, as tariff uncertainty weighed. We expect INR to trade in the range of 85-86/$ in the near-term, as risk sentiment has once again taken a hit after US announced fresh tariffs. **India's 10Y yield** softened further by 7bps in May'25, supported by RBI's liquidity measures and expectations of further monetary policy easing. We expect domestic 10Y yield to trade in the range of 6.15-6.27% in Jun'25.

Macro developments

Global growth: Bumpy road ahead

High frequency data in the **US** continues to paint a sombre picture of the economy. Consumer spending eased to 0.2% in Apr'25 after increasing 0.7% in Mar'25. In particular, consumers reduced spending on discretionary goods such as motor vehicles, clothing and footwear etc,. Retail sales increased at a subdued pace of 0.1% in Apr'25, after increasing by 1.7% in Mar'25. Even so, Conference Board's consumer confidence index rose sharply to 98 in May'25 from 85.7 in Apr'25. Manufacturing sector, however continued to exhibit some stress. ISM manufacturing PMI slipped to a 6-month low of 48.5 in May'25 from 48.7 in Apr'25, despite tariff relaxations. Businesses reported a drop in both exports and imports. On the other hand, input prices remained elevated, and layoffs increased. ISM services PMI also dipped significantly to its lowest since Jun'24 at 49.9 in May'25 from 51.6 in Apr'25. Labour market indicators gave mixed signals. Weekly jobless claims rose by 14,000 to 240,000 for the week ended 24 May 2025. On the other hand, US JOLTS job openings increased by 191,000 to 7.39mn. At the same time, layoffs increased by 196,000 marking the highest pace of increase since Jul'24. ADP employment report also highlighted stress in the labour market with an addition of only 37,000 private sector jobs in May'25. On the positive side, inflationary pressures remained largely contained. Core PCE, Fed's preferred gauge of inflation, moderated to 2.5% in Apr'25 from 2.7% in Mar'25. PPI inflation declined by 0.5% in Apr'25, exacerbating the 0.4% drop in Mar'25 (MoM). Tariff related uncertainty returned, with legal disputes related to the imposition of Liberation Day tariffs keeping investors awry. More recently, US President once again raised tariffs on steel and aluminium to 50% from 25%. Trade related disruptions has led to a sharp downgrade in US growth forecasts by OECD to 1.6% in 2025 from 2.2% earlier.

In case of **Eurozone**, manufacturing PMI rose to a 33-month at 49.4 in May'25 from 49 in Apr'25. However, it continues to remain below the key 50-mark which separates expansion from contraction. On the positive side, a sub-index for manufacturing output remained steady at 51.5. Further, despite looming threats of US tariffs, businesses remained upbeat with respect to future rate cuts. Input costs eased further, and job losses also moderated. Amongst major economies, Spain and Greece noted solid improvements, while France and Italy reported stable growth. However, Germany continues to lag. Services PMI of the region slipped to 49.7 in May'25 from 50.1 in Apr'25. However, growth is expected to recover steadily in the coming months as reflected in business and consumer surveys. Ifo's business climate index picked up sharply from -25.8 in Mar'25 to -18.6 in Apr'25. Even ZEW investor sentiment index picked up to 25.2 in May'25 from -14 in Apr'25. CPI inflation in the Eurozone moderated to 1.9% in May'25, falling below the ECB's target for the first time since Sep'24. Core inflation also softened, boosting the case for an ECB rate cut this week (25bps).

China's official manufacturing PMI rose to 49.5 in May'25 from 49 in Apr'25, just shy of the crucial 50-mark. In contrast, Caixin manufacturing PMI declined sharply to 48.3 in May'25 from 50.4 in Apr'25. This was led by a precipitous fall in new orders, especially export orders. However, both input and output costs continued to slow down. On the other hand, non-manufacturing PMI remained broadly stable at 50.3 in May'25 compared with 50.4 in Apr'25. Industrial production growth slowed to 6.1% in Apr'25 from 7.7% in Mar'25. However, retail sales increased by 4.7% in Apr'25, following a 4.6% increase in Mar'25. China's GDP growth in Q1 2025 was recorded at a stellar 5.4%, unchanged from Q4 2024. However, OECD recently revised its growth forecast for China lower to 4.7% in 2025 and 4.3% in 2026. With both the US and China agreeing to pause escalated tariffs on imports for a period of 90-days, the outlook has improved. Successful completion of the trade negotiations between the World's largest economies will have a significant positive impact on global growth outlook.

India’s growth maintains momentum in Q4

GDP growth accelerated to 7.4% in Q4 FY25 from 6.4% in Q3 FY25. GVA growth also picked up pace to 6.8%. Industry growth improved to 6.5% in Q4 from 4.8% in Q3. Construction sector too expanded at an accelerated pace of 10.8% versus 7.9% in Q3. Growth in services sector was steady. For FY25, India’s GDP rose by 6.5% in compared with an increase of 9.2% in FY24. On expenditure side, PFCE growth was recorded in double digit at 12% compared with 9.7% in FY24. GVA growth for FY25 was 6.4% versus 8.6% in FY24. While agriculture growth rebounded sharply, mining and manufacturing were lower. For FY26, we expect GDP growth in the range of 6.4-6.6%, supported by a favourable monsoon, tax cuts, moderating inflation and lower rates.

In Q1FY26 so far (Apr/May’25), economic activity is signalling mixed trends. Indicators which are showing an improvement or are holding ground so far include: domestic air passenger traffic growth (4.8% versus 4.9% during the same period last year), GST collections (Rs 4.4 lakh crore versus Rs 3.8 lakh crore), diesel consumption (3.2% versus 1.9%), vehicle registrations (45.3 lakh units versus 43.4 lakh units), and toll collections (18.3% versus 5.6%). On the other hand, manufacturing (57.9 versus 58.2) and services (60.0 versus 60.5) PMIs are showing some signs of moderation in activity.

Central bank actions

Given that CPI has remained on the lower to middle end of **RBI's** band since Jan'25, we expect another back-to-back rate cut by the central bank in its upcoming policy. Since the start of CY25, RBI has cut policy rate by 50bps, in two consecutive meetings Feb'25 and Apr'25, bringing down the repo rate to 6%. We also expect RBI to revise its inflation projections for FY26 down by ~10bps, as the Q1 actual inflation is likely to undershoot the RBI's forecast by 30-40bps, supported by the broad-based moderation in food prices. Further, assuming normal monsoon and subdued oil and global commodity prices, we expect inflation to align closely to RBI's target. We maintain our inflation forecasts at ~3.8-3.9% for FY26. Growth forecasts on the other hand will likely remain unchanged as the central bank takes note of rising global trade uncertainties and its impact on growth. Our GDP forecast for FY26 at 6.4-6.6% also remains unchanged so far. RBI will continue with its "accommodative" stance as it aims to keep liquidity at comfortable levels to support credit growth. Cumulatively we expect 100 bps cut in the current cycle.

US Fed kept its policy rate steady for the third successive meeting in May'25 in the range of 4.25-4.50%, amidst increased risks to the growth and inflation outlook. Growth projections for both 2025 and 2026 were revised down. While both inflation and unemployment rate are expected to be higher than the levels estimated in the last policy. The decision to keep rates steady was based on the fact that there is increased uncertainty over tariff policies and its impact on growth, inflation and employment. Minutes of the Federal Reserve's meeting showed that MPC members noted that tariff driven uncertainty jeopardizes the Fed's twin objective of stable prices and maximum employment. Members agreed that the given the heightened uncertainty, it will be appropriate to adopt a cautious wait and watch approach. Fed officials continue to bat for a cautious approach to future rate cuts, with the MPC likely to face "difficult trade-offs" in coming days.

Bank of England (BoE), reduced its policy rate by 25bps in May'25 to 4.25%, after keeping rates on hold in Mar'25. The voting patter of the MPC showed growing discord amongst members on monetary policy. Out of the 9 MPC members, 5 voted for a 25bps rate cut, 2 voted for a 50bps cut, while the rest voted for status quo. Substantial progress on bringing inflation closer to the central bank's target drove the decision to cut rates. The BoE Governor also hinted that more rate cuts are likely, even as he welcomed the successful completion of a trade deal with the US. Analysts expect another 100bps of easing this year.

The ECB is widely expected to reduce its policy rate by 25bps today. Earlier in May'25, the ECB had reduced its policy rate by 25bps, taking the total easing in the current cycle to 175bps. With headline inflation easing below the ECB's target in May'25, and core inflation also showing a downward trajectory, inflation is likely to undershoot the central bank's target. However, given the uncertainty around the US tariffs, analysts expect ECB to keep rates on hold till late 2025, as it assesses the evolving tariff developments.

PBOC also lowered its key lending rates by 10bps to support the economy amidst tariff related challenges. This was the first rate cut since Oct'24 when the policy rates were reduced by 25bps. With this, the 1Y loan prime rate (LPR) was lowered to 3%, while the 5Y LPR now stands at 3.5%, the lowest level since the LPR mechanism was revised in 2019. The measures are expected to boost credit growth and consumption spending in the World's second largest economy.

Economic reports

Bonds Wrap

Global yields showed some stiffening in May'25 led by elevated debt concerns in the US which partly weighed on risk off sentiments. For India, however, the softening of yields continued across all parts of the curve. Significant moderation was visible in the very short end part which is more susceptible to evolution of system liquidity. Thus, it resulted in a steeper yield curve, which is likely to persist. RBI's orderly management has ensured that the system liquidity has remained in surplus averaging ~0.7% of NDTL in May'25. The elevated system liquidity also got mirrored in banking liquidity, with the gap between incremental deposits and borrowing net of incremental credit and investment going up. Going forward, we expect some pressure on account of the usual seasonal buildup of government cash balances. However, RBI's transfer of bountiful dividend coupled with continued fine tuning of daily liquidity will lend support. We expect more OMO announcements in the coming days to maintain liquidity surplus at ~1% of NDTL surplus level. RBI's upcoming policy will set the undertone of yields. A higher-than-expected reduction in policy rates (est. 25bps) might put further downward pressure on India's 10Y yield. We expect it to trade in the range of 6.15-6.27% in the current month, with risks tilted to the downside.

Currency update

In a turnaround of events, INR depreciated by 1.3% in May'25, after appreciating by 1.1% in Apr'25, and 2.4% in Mar'25. Less sharp decline in the US dollar (-0.1%) due to revival in global trade tensions and escalated geo-political tensions between India and Pakistan during early May'25, impacted INR's rally. INR fell by 1.2% in the first fortnight of May'25, before stabilizing in the second fortnight (0%). Weak economic data (consumption demand, impact of tariffs on growth, labour market slowdown) from the US in the second fortnight of May'25 led to US$ falling by 1.5% in that period, erasing gains (1.4%) made in the first fortnight. Losses in INR were contained by lower oil prices and FPI inflows. Going forward, as trade tension are expected to escalate in the coming weeks, pressure on INR will remain. However, strong domestic fundamentals (GDP growth, inflation, and monsoon), lower international oil prices will help limit the losses. We expect INR to trade with a depreciating bias in the near-term in the range of 85-86/$.

Fiscal position of central government in FY25

Centre's fiscal deficit was at 4.8% in FY25, in line with government's revised projections for FY25. Higher growth in nominal GDP (9.8% as per provisional estimate versus 7.6% as per FY25RE), and some trimming in expenditure helped government achieve this target. Revenue growth noted some moderation, led by revenue receipts. Within this, income tax and GST collections registered some shortfall. Corporate tax collections and non-tax revenue growth outperformed FY25RE targets. On spending, while capital expenditure surpassed its revised budgetary FY25 target, revenue expenditure witnessed some shortfall. This was not on account of subsidies, as both food and fertilizer subsidies fell in line with budgeted projections. Major ministries which registered higher than budgeted spending included: consumer and food affair, road & transport, rural development, home affairs and renewable energy. For FY26, given that both revenue collections and capital expenditure are off to a good start (Apr'25), we believe that government is likely to meet its revenue, expenditure and fiscal deficit (4.4%) target.

Industrial production

IIP growth was lower at 2.7% in Apr'25 from 5.2% in Apr'24, and 3.9% in Mar'25. Compared with previous year (Apr'24), slower growth was noted across the board. Manufacturing and electricity output slowed most notably, while mining sector output contracted. Within manufacturing, certain subsectors registered negative growth in Apr'25 compared with last year. For use-based industries, capital intermediate and FMCG goods registered improvement in Apr'25, while other industries registered slower growth. For the near term, there are downside risk emerging from volatility due to trade tariffs. However, tailwinds from lower inflation, commodity prices and easing monetary cycle will provide much needed support to industrial sector.

Inflation eases further

CPI inflation moderated to 3.2% in Apr'25 from 4.8% in Apr'24 driven by lower food inflation. At 1.8%, food inflation eased to a 43-month low. Within food, prices of vegetables and pulses declined sharply. Moderation was also visible in other categories of food, including in cereals and eggs and meat categories. In May'25 as well, daily price data suggests further moderation in underlying price pressures. Prices of edible oils have remained elevated but should see some softening momentum going ahead. Global commodity prices have remained soft, which should help keep a lid on core inflation. With domestic inflationary pressures in check, policy space for further monetary easing remains in place. This will be contingent on evolving monsoon conditions as well as external stimuli.

WPI inflation eases

WPI inflation eased to a 14-month low of 0.9% in Apr'25 compared with 1.2% in Apr'24. Food inflation moderated to 2.5% compared with 6.1% in Apr'24, led by a broad-based deceleration. Notably, sharp correction was seen in prices of vegetables, especially tomato, onion and potato, as well as pulses categories. Cereals inflation also moderated, led by lower rice prices. Fuel and power inflation eased, as crude oil prices remained downbeat. Within manufactured, incipient price pressure was visible for food products, reflecting higher edible oil prices. Further, despite lower global metal prices, domestic prices noted a marginal pickup on a YoY basis. Going ahead, food inflation is likely to get support from a favourable monsoon and prospects of higher production. On the other hand, global commodity prices are likely to remain contained despite a softer stance by the US on tariffs, amidst China's continued economic challenges. Global growth prospects too, appear to be in a jeopardy given the uncertainty over US tariffs. The above backdrop suggests that WPI inflation is likely to remain benign in FY26 as well.

RBI Annual Report

RBI's balance sheet expanded by 8.2% to Rs 76 lakh crore in FY25 compared to Rs 70 lakh crore in FY24. On the assets side, RBI gold holding has contributed to a significant increase, as safe-haven demand rose in a volatile global policy environment. The remaining increase was seen in the domestic investment portfolio of RBI led by conduct of OMO purchase for liquidity management. The income and expenditure statement showed that the record high dividend transfer to the government was possible on account of higher gains from foreign currency assets (FCA). The earnings from FCA as percent of average FCA rose to its decade high level. Going forward with normalization of domestic liquidity and notwithstanding any untoward pressure on DXY, we expect this stability on this front. Another interesting part of the RBI's balance sheet has been the higher ratio of Available Realized Equity as percentage of Balance sheet which went up to 7.5% in FY25 from 5.5% seen in FY21. This also is a buffer mechanism in line with the Bimal Jalan Committee recommendation to act in a prudent manner in a volatile financial landscape.

Which industries are investing?

To gauge investment being undertaken by corporates, a random sample of 1,393 companies has been selected that have announced their results and provided information on balance sheet items for FY25. An industry-wise analysis has been done rather than sector-wise as it provides a more disaggregated view. This sample has been classified into 122 industries. Gross fixed assets (defined as gross fixed assets plus capital work in progress) of the sample of companies was Rs 28.50 lakh crore as against Rs 26.49 lakh crore in FY24. Refineries had the highest share in fixed assets in FY25 at 31%. This was followed by telecom services (8.6%), iron and steel products (5.9%), cement (5.4%) and power (4.8%). The picture on growth in fixed assets in the corporate sector is encouraging for FY25 with growth of 7.6%. Most of the leading sectors in terms of being those that drive investment in the country are in the infra space and have registered impressive growth rates. The picture is diverse for consumer-oriented industries which should show more traction in the coming year when consumption shows a revival. Demand in some of these sectors has been mixed especially in urban areas and the measures announced by the government as well as declining inflation should help to reverse the same.

India-UK FTA

India and UK announced the successful conclusion of a mutually beneficial India – UK Free Trade Agreement (FTA). This forward-looking Agreement is aligned with India's vision of Viksit Bharat 2047 and complements the growth aspirations of both the countries. In FY24, India's exports were around US$ 13 bn, while imports from the UK were US$ 8.4 bn, thus yielding a surplus of US$ 4.6 bn. In FY25 exports were at US$ 14.5 bn. The chief exports are engineering, readymade garments, chemicals, petro and agro products among others. In case of imports, besides chemicals and engineering goods, gold was significant. The FTA with the UK is a modern, comprehensive and landmark agreement which seeks to achieve deep economic integration along with trade liberalisation and tariff concessions. India has ensured that non-tariff barriers are suitably addressed to ensure free flow of goods and services and that they do not create unjustified restrictions to India's exports. The FTA seeks to promote good regulatory practices and enhance transparency that are in sync with India's own focus on domestic reforms to enhance the ease of doing business. Overall, while UK per se is not a very significant trading partner for India, this paves the way for similar agreements with other countries like USA and EU and hence augurs well for India. The FTA will also ensure that momentum builds up in our bilateral trade with UK.

Current cycle favoring corporate bond yields

The current easing cycle has been conducive for corporate bond market. There has been considerable softening across yields of major rated paper, with higher rated paper showing a much steeper fall in yields. Interestingly, transmission has occurred in lower rated papers as well. This is positive and suggests that the depth of the corporate bond market has increased under the evolving financial landscape. Ample liquidity inducing measures adopted by the RBI, also supported lower yields. Apart from this, other measures such giving market clear signaling about the quantum of liquidity surplus to float around 1% of NDTL, announcing OMO calendar, have also led to better pricing and transmission of rate cuts to parallel market segments.Ceteris Paribus, a one-on-one comparison of yields under the current environment, reflects that for higher rated corporates, resorting to corporate bonds is cheaper compared to bank loans. For papers A and below, bank credit may be the preferred mode of finance.

Corporate performance in Q4 FY25

In Q4 FY25, aggregate net sales of a sample of 1,893 companies was recorded at 5.4%, while net profits rose by 7.6%. Expenditure and interest costs remained muted leading to an improvement in debt serviceability of companies. Some moderation in sales is observed in a few large sectors, such as oil and gas, textiles and iron and steel, which weighed on the aggregate sample. However, this appears to be a one-off phenomenon and not a structural issue. Similarly, the BFSI segment witnessed some slowdown after a strong run last year and can be associated with slowdown in growth in credit.

Overall, India Inc.'s performance in Q4 was satisfactory and there is scope for an upward movement once consumption picks up in FY26. There are sectors which are witnessing green shoots of recovery. Infrastructure linked sectors continue to witness steady growth notwithstanding a negative base effect. For consumer linked sectors, such as FMCG and consumer durables, strong rural demand and seasonal demand continues to aid a steady recovery. Industries in the services sector also continued to post steady growth amidst sustained demand momentum. Importantly, despite a challenging global environment, companies remain positive on future growth prospects. Stable commodity prices, low domestic inflation, favourable monsoon trajectory, trade deals, government capex, tax incentives are likely to be key drivers of growth and demand.

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