5 Feb 2025

Sonal Badhan
Economist

Economic Round-up: January 2025

As expected, US President Donald Trump has announced sweeping tariffs (25%) on goods imported from Mexico and Canada. Chinese goods will also face 10% tariffs in the US. Retaliatory measures have been announced by all three countries, leading to fears of higher inflationary pressures in the US. Annual growth estimates show that US GDP was up by 2.8% in CY24 versus 2.9% in CY23. For this year, Fed expects growth at 2.1% and inflation at 2.5%. At the start of the year, labour market is showing signs of slowdown, but inflation expectations in forward looking consumer survey remain elevated. As a result, analysts expect Fed to keep rates 'higher for longer'. This is in contrast to situation in the Eurozone. Sustained weakness in economic activity (stagnated GDP growth, contraction in manufacturing activity) has forced ECB to lower policy rates by 125bps so far. Another 75-100bps cuts are priced in for this year. Any tariff announcement by US on European goods poses further downside risk to growth and upside risk to inflation. Domestically, high frequency indicators for Q4 are sending mixed signals. Nonetheless, domestic consumption remains robust with GST collections coming in at 9-month high in Jan'25. Latest budget announcement will further propel demand in FY26.

Global Central Banks: In Jan'25, in line with market expectations, US Fed held rates steady, while ECB lowered it by 25bps. US Fed held rates unchanged in the view of steady labour market conditions. The central bank has also cautioned against build-up in price pressures and will note the impact of policy changes before announcing further rate cut. Analysts do not expect any rate cut by Fed before Jun'25. The ECB lowered its policy rate by 25bps—5th rate cut so far, given the ongoing steady disinflation process. Analysts expect continuous rate reduction by ECB till Jun'25. BoE is also expected to cut rates by 25bps this week. In case of BoJ, the central bank hiked rates by 25bps, taking short-term rate to 0.5% from 0.25% earlier. This was on account of sustained increase in wages and inflation. Given this momentum is still continuing, more rate hikes are expected by BoJ in the coming months. RBI will also announce its policy decision this week and we expect a 25bps rate cut.

Key macro data releases: Union Budget for 2025-26 was recently announced, which showed that government curtailed its fiscal deficit-GDP ratio to 4.8% in FY25 (RE) and aims to further lower it to 4.4% in FY26. Income and expenditure estimates for FY26 were announced in line with nominal GDP growth expected next year (10.1%). Capex, and expenditure on rural and agriculture has seen a significant push. Boosting consumption demand was also in focus with tax rebates announced. NSO has estimated that Indian economy is expected to clock a growth of 6.4% in FY25. For FY26, we expect the nominal GDP growth at 10.5% and real GDP growth at 6.8%. **CPI inflation** moderated to 5.2% in Dec'24 (BoB est.: 5%) compared to 5.5% in Nov'24. Food inflation went down by 65bps to 8.4% in Dec'24 from 9% in Nov'24. **Core inflation** moderated to 3.6% in Dec'24 from 3.7% in Nov'24. There had been a usual seasonal moderation in housing component of core. Apart from this, miscellaneous component edged down led by personal care and effects.

Macro developments

Global growth: Tariff war begins

Recently, US President Donald Trump announced 25% tariff on imported goods from Mexico and Canada and 10% tariff on Chinese goods. In case of China, the implementation has been with immediate effect, while a 30-day postponement period has been allowed for Canada and Mexico. This gives room for trade negotiations. All three countries have announced retaliatory tariffs on US goods, thus announcing the beginning of the much feared trade war, and raising the prospects of higher inflation in the US. Advance estimates of US GDP for Q4CY24 show that the economy ended the year on a sombre note, with growth easing to 2.3% from 3.1% in Q3. This was primarily due to (-) 5.6% decline in gross private domestic investment (+0.8% in Q3), led by (-) 7.8% decline in fixed investment as equipment (+10.8% in Q3). In contrast, residential investment improved (5.3% versus -4.3%). The main driver of growth remained private consumption, which was up by 4.2% from 3.7% in Q3. In CY24, GDP was up by 2.8%, broadly steady compared with 2.9% growth in CY23. This is also 30bps higher than what Fed had projected in Dec'24, thus implying that economy is not losing momentum as expected and there remains room for Fed to keep rates 'higher for longer'. However, at the start of 2025, some signs of slowdown are visible. Continuing claims (4-week moving average) rose by 6k from the previous week to come in at 1.87mn. JOLTS data showed that job openings rose by 7.6mn in Jan'25, down from 8.09mn in Dec'24. Even US conference board consumer confidence index retreated in Jan'25 to 104.1 points from 109.5. Inflation expectations have soared.

In case of **Europe**, tariff threat still looms as US President has signalled that next set of tariffs will focus on the Eurozone. Even without a trade war, economic conditions in EZ remain bleak. Eurozone's GDP in Q4CY24 stagnated (0% versus est.: 0.1%) following 0.4% increase in Q3. Germany's GDP fell by (-) 0.2% in Q4 versus est.: (-) 0.1% and +0.1% rise in Q3. France's GDP fell by (-) 0.1% (est.: 0%) in Q4 after expanding by 0.4% in Q3. These 2 biggest economies of Eurozone dragged the overall growth down. Latest manufacturing PMI data shows activity in Eurozone contracted at a slower pace of 46.6 in Jan'25 versus 45.1 in Dec'24, helped by softer decline in new orders and output. Country-wise Germany (45 versus 42.5) and France (45 versus 41.9) also reported softer pace of decline in Jan'25. Continued decline in policy rates by ECB has also helped improve business expectations. Germany's IFO business climate index also noted an improvement in Jan'25 to 85.1 (84.7 in Dec'24), helped by pickup in present situation index.

China's official manufacturing PMI index showed that activity contracted at the start of 2025. In Jan'25 index fell to 49.1 from 50.1 in Dec'24. This was led by steep decline in new orders, which could be a reflection of stalling demand from US, as companies had pre-ordered and stocked ahead of US-China tariff war. In CY24, China met is its official growth target of 5%, helped by 5.4% growth in Q4 (est.: 5.1%) versus 4.6% in Q3. FAI rose by 3.2%, missing estimate of 3.3%. Within this, real estate investment remains a major pain point with (-) 10.6% decline versus (-) 10.4% decline between Jan'24 and Nov'24 period. In contrast, both industrial production (6.2% versus est.: 5.4%) and retail sales (3.7% versus est.: 3.5%) picked up pace in Dec'24. Growth is expected to average around 5% in CY25 as well.

India's growth: Budget to boost growth

Latest union budget announcement, which included income tax rebates under the new regime, 10% increase in capex, higher pay-outs for rural and agriculture related sectors, enlarged coverage for MSMEs and PLI for manufacturing (automobile, batteries etc.), is expected to provide a significant boost to consumption and overall growth in FY26. Mospi has released advanced estimates for India's GDP growth in FY25. These estimates are based on data till Nov/Dec'24. Accordingly, growth in FY25 is expected to have moderated to 6.4% (BoB est.:

6.6-6.8%) from 8.2% in FY24. This is on account of slower pace of growth in investment demand at 6.4%, as against 9% in FY24. Moreover, contraction in import (-1.3% versus 10.9% in FY24) growth is also likely, given weakness in global economy. However, on the bright side, both private and government consumption is expected to register strong growth of 7.3% (4% in FY24) and 4.1% (2.5% in FY24) respectively in FY25. High frequency indicators show that activity rebounded in Q3FY25 versus Q2. In Q4, mixed signals of growth are visible. Indicators which are showing an improvement include: GST collections (Rs 2 lakh cr in Jan'25 versus average Rs 1.8 lakh cr in Q3), bank credit growth (11.5% at the start of Jan'25 versus 11.2% in Dec'24) and toll collections 16.9% in Jan'25 versus 14% in Q3). On the other hand, indicators like air passenger traffic, vehicle registrations, and diesel consumption cooled down in Jan'25. However, we see an upside bias to GDP growth in FY25 and expect numbers to be revised upward, on the back of robust domestic consumption.

Central bank actions

RBI, led by new Governor Sanjay Malhotra, is set to announce its monetary policy decision on 7 Feb 2025. A 25bps rate cut by the central bank is widely expected. Given that RBI has already announced liquidity easing measures (OMO purchase, VRR, currency swap), analysts are reading this is as a prelude to rate cut. We do not expect a CRR cut in this policy. Union budget announcement has also lent support. With government sticking to the path of fiscal consolidation and announcing non-inflationary measures to boost growth, we expect, in the current cycle, RBI may lower rates by 75-100bps. Monetary policy stance is expected to be retained at neutral to allow the MPC flexibility on future path of policy action.

US Fed in its Jan'25 meeting decided to keep policy rates on hold at 4.25-4.50%. This decision was driven by steadiness in labour market, overall strength of the economy and pressure build up on prices. Consumer confidence surveys have shown that inflation expectations for the near-term have gone up. Fed Chair Powell also clarified that the central bank will take into account policy announcements by the new administration before taking any rate cut call. Now, given that the Trump administration has announced tariffs on China, Canada and Mexico, risks to inflation have gone up. Markets are pricing in no rate cut before Jun'25.

Bank of England (BoE) in its Feb'25 meeting, is expected to cut rates by 25bps to 4.5% from 4.75% currently. This will take the cumulative cuts in the current cycle to 75bps. Slowing economic growth (0%) in quarter ending Sep'24 and in Nov'24 (0.1% on 3M basis) has raised the need for policy rates to come down. Further, slowing inflation in Dec'24 (2.5%) from the previous month (2.6%), is also supportive of the view that BoE has room to cut rates. However, this decision can be complicated if wage inflation is taken into account. Private sector pay-excluding bonuses rose by 6% in Nov'24, following 5.5% increase in Oct'24. Analyst expect upto 3 rate cuts by BoE in CY25.

ECB, in line with market expectations, lowered rates by another 25bps in its Jan'25 meeting, bringing the deposit rate to 2.75% from 3% earlier. This is in line with ECB President Lagarde's remarks that "the disinflation process is well on track". In addition, continued slowdown in economic activity has further added to the need for lower rates. Eurozone's GDP stagnated in Q4CY24 (0% versus est.: +0.1%). Cumulatively, in CY25 markets are expecting a 100bps cut in policy rates by ECB. However, major downside risk to this scenario is if US announces tariffs on imports from Eurozone.

BoJ raised its policy rate by 25bps, with a split 8-1 vote in Jan'25. The short-term policy rate now stands at 0.5% (highest in 17 years), up from 0.25%. The guidance remained unchanged, implying that the central bank stands ready to raise rates further in case its inflation forecasts are realised. As per its latest forecast, inflation is expected to rise to 2.4% this year versus previously estimated 1.9%. BoJ further cautioned that there remain upside risks to inflation-through imported inflation (due to weaker Yen), labour shortage and rising prices of rice. The central bank expects its neutral rate around 1-2.5%, signalling that there remains room for more rate hikes.

Data Releases

Union Budget 2025-26

In line with the fiscal glide path outlined in the Budget for 2021-22, fiscal deficit (as % of GDP) was lower in FY25 and will be brought down by another 40bps in FY26. Going forward, government will lower its debt-GDP ratio below 50%, as recommended by the 16th Finance Commission, by FY31. For FY26, budget outlined key areas where government will be focusing in the next five years. These include: employment, skilling, agriculture, MSMEs, women, infra, and space technology, etc. Government expects nominal GDP to rise by 10.1% in FY26, recovering from 9.7% growth in FY25. Overall tax revenue-GDP is estimated to remain steady at 12% in FY26BE versus 11.9% in FY25RE. Gross tax collections are estimated to register significant incremental improvement in FY26BE (Rs 4.2 lakh cr) compared with last year (Rs 3.9 lakh cr). This will be driven by increase in corporate tax receipts and indirect tax collections. Incremental increase in income tax collections will be lower, as government has decided to forego ~Rs 1 lakh cr as tax rebate. Non-tax revenue is estimated at Rs 5.8 lakh crore for next year, up from Rs 5.3 lakh crore in FY25. Centre's overall expenditure is estimated to increase from Rs 47.2 lakh crore in FY25RE to Rs 50.7 lakh crore in FY26BE. This will be led by both, revenue and capital spending. Revenue spending is set to increase to Rs 39.4 lakh crore in FY26BE, a Rs 2.5 lakh crore increase from last year, mainly on account of interest repayment and servicing of debt (Rs 1.4 lakh crore). Pensions, Rural development and agriculture will also be driving the growth in spending. In FY26, Centre's capex spending is expected to increase sharply to Rs 11.2 lakh crore from Rs 10.2 lakh crore as per FY25RE. As % of GDP, ratio of capex is retained at 3.1%. Increased focus in the Budget through PPP mode of project implementation will crowd in private investment.

BoB ECI: Inflation seen trending lower

BoB's Essential Commodity Index (ECI) exhibited a further downward momentum in Jan'25, dipping to 4% on YoY basis, moderating from 5.4% in Dec'24. On a sequential basis, the index declined sharply by 2.4%, after a fall of 0.5% in Dec'24. The decline was largely led by lower prices of vegetables, with tomato, onion and potato prices declining steeply. Edible oil prices were also lower. We thus expect a significant moderation in headline CPI in Jan'25. CPI inflation is expected in the range of 4.5-4.7%. The inflation outlook is evolving broadly in line with estimates, with significant support stemming from easing prices of vegetables. Global prices of edible oils too have softened, which is positive for domestic inflation trajectory. Prospects of higher production due to improvements in sowing of pulses (up by 2.3%) and wheat (up by 2.8%) in the ongoing rabi season, bodes well for domestic availability of these crops. Recent announcements in the Budget targeted at easing the supply-side issues related to oilseeds, pulses and vegetables and fruits should aid in preventing the sporadic food-price shocks which tend to unhinge the inflation outcome.

Rupee crosses 87? What next?

Just when the rupee was comfortably settled in the region of Rs 86.50/$, it has slipped past the Rs 87/$ mark. This may have been expected, though we believed that the global environment would probably improve. Donald Trump's decision to impose 25% tariffs on all imports from Canada and Mexico is now a reality. Canada and Mexico announced that they would be taking similar action against imports from USA. Canada and Mexico export around US$ 840bn of goods to USA. But USA exports close to US$ 630bn from these countries. Therefore, the trade war can get nasty. There is the 10% tariff hanging for China which exports around US$ 400bn to USA. The Yuan has weakened as the dollar has strengthened and the rupee is witnessing collateral effects.

We do believe that a repo rate cut is on the cards soon as the budget has done well to spur growth and with expectations of inflation to come down, this could be the right time. But the currency issue has popped up again which can lead to some serious discussion. The liquidity induction measures of RBI did improve the situation. The bond market has however been quite agnostic to these developments with the 10 year ending at ~6.68%. It would be hard to conjecture where the rupee is headed. We need to look at the dollar again for guidance. At this juncture, selling dollars may only slowdown the process. The 87.50/$ mark will now be tested. But left to the market, imported inflation can emanate. Hence, a tricky situation for sure.

Economic Survey

The Economic Survey is a prelude to the Budget. One of the core numbers that is judiciously looked at is the forecast for GDP in FY26. This is kept at 6.3-6.8%, which is bit conservation and in tune with NSO estimate of 6.4%. We assume GDP deflator of around 3.5%, which would translate nominal GDP growth to 9.8-10.3% in FY26. This nominal GDP number is crucial from a fiscal standpoint as any deviation might be reflected in the key deficit ratios. The key theme of the Survey has been one of achieving sustainable growth through reducing the cost of business by deregulation, augmenting internal capacities for growth and paving the new way of energy transition.

The Survey has spoken of faster reforms and more importantly easing of controls so that the private sectors can operate in a free manner. Three factors have been given for lower manufacturing output so far and these were: exports slowed significantly due to weak demand from destination countries, and aggressive trade and industrial policies in major trading nations; the above average monsoon had mixed effects disrupted sectors like mining, construction, and, to some extent, manufacturing; the variation in the timing of festivities between September and October in the previous and current years led to a modest growth slowdown. The survey was positive on the fiscal state of the government. Following an unprecedented expansion of capital expenditure in the last four years, it remained subdued during Q1 FY25, owing to general elections. However, it rebounded after July despite a reduction in non-debt receipts owing to an increase in the devolution of taxes to states. The survey noted that, the banking and financial sector remains stable and well-capitalised, and is catering to the financing needs of the economy. Area of concern within the banking system is the stress on unsecured credit, i.e., personal loans and credit cards. Going forward, there are many upsides to domestic investment, output growth and disinflation in FY26. There are equally strong, prominently extraneous, downsides too. Nonetheless, the fundamentals of the domestic economy remain robust, with a strong external account, calibrated fiscal consolidation and stable private consumption. On balance the Survey believes that the growth will be between 6.3% and 6.8%.

WPI inflation accelerates

WPI inflation rose to 2.4% in Dec'24 from to 1.9% in Nov'24, led by increase in manufactured product inflation and slower pace of deceleration in fuel and power inflation. Food inflation remained steady at 8.9% in Dec'24. With this, headline WPI averaged at 1.7% in CY24 (0.1% in CY23), with inflation for food items at 6.8% (2.8%), fuel at -1.7% (-1%) and manufactured at 0.7% (-1%). In Dec'24, within food, barring food grains and condiments and spices, all other sub-categories noted upward pressure. Amongst vegetable prices, onion and potato prices registered an increase. Within fuel, mineral oil and electricity indices decelerated at a slower pace. Mineral oil index mirrors the movement in international oil prices. Core inflation rose for the 4th consecutive month in Dec'24. Within manufactured products, food, textiles and electronics led inflation higher. Commodity prices broadly eased. Going forward, if Fed decides to keep to rates higher for longer, it will dent demand prospects and ease oil and other commodity prices. Imported inflation, due to stronger US$ also poses upside risk to domestic inflation.

Food pacifying CPI

CPI inflation moderated to 5.2% in Dec'24 (BoB est.: 5%) compared to 5.5% in Nov'24, on YoY basis. This comes in the wake of an elevated base and food inflation losing steam. Food inflation went down by 65bps to 8.4% in Dec'24 from 9% in Nov'24. Reversal in TOP (Tomato, Onion and Potato) trajectory has provided the desired comfort. Core (CPI excl. food and fuel) also softened led by range-bound global commodity prices. In Q4, albeit some unfavourable basis, we expect the downtrend in vegetable inflation will pull down headline CPI. Outlook of food inflation seems favourable as mandi arrivals statistics of perishables have improved in harvesting months. Rabi sowing data also remains promising for cereal inflation going forward. Key risks to overall inflation outlook stem from a depreciating INR which might escalate risks of imported inflation. Apart from this, any volatility in energy prices on account of ongoing sanctions might feed into higher intermediate input prices and hence to overall inflation print. On the policy front, RBI is likely to be watchful in its Feb'25 meeting.

Industrial production surges to 6-momth high

IIP growth registered a robust growth of 5.2% in Nov'24 against a growth of 3.7% in Oct'24. This was supported by improvement across all the sectors. Manufacturing sector expanded by 5.8%, with over 15 sub-sectors registering stronger growth than last year. Both mining and electricity sector registered strong growth in Nov'24. Within use-based classification, capital goods, infra good and consumer durable goods registered a healthy increase in Nov'24. A festival push during this period, supported the production. In the coming months, we expect a steady pick up in production level. This has been reflected by high frequency indicators. Moreover, given the expectation of higher government spending followed by improvement in investment in H2, the IIP growth is likely to be higher in H2FY25.

FY25 growth pegged at 6.4%

NSO has estimated that Indian economy is expected to clock a growth of 6.4% in FY25 growth compared with a growth of 8.2% in FY24. GVA growth is also estimated lower at 6.4% (previously 7.2%). Softer growth is expected across the industry sector in FY25 with manufacturing and mining sector to grow at 5.3% and 2.9% in FY25, much slower than last year. Agriculture sector is expected to record robust growth supported by recovery in rural demand and improvement in rabi sowing. Given the ongoing geopolitical conflict and threats of tariff war, the global headwinds signal weakness in global economy. On the other hand, India's economy is expected to perform much better in H2FY25. The attention will now shift towards Union Budget and corporate performance for Q3 and Q4. For FY26, we expect the nominal GDP growth at 10.5% and real GDP growth at 6.8%.

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For further details about this publication, please contact:

Economics Research Department
Bank of Baroda
chief.economist@bankofbaroda.com