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Economic Round-up: October 2024

US Presidential election results gave a clear mandate to Trump. President Trump has advocated for tax concession to companies and introducing tariffs on all imported goods. China and Europe will be impacted the most if these tariffs come into effect. Disinflation process in the US will also be at risk, as a loose fiscal policy is inflationary in nature. As a result, for now, markets are expecting a pause from Fed in Jan'25 meeting, after cutting rates for the third time in Dec'24. Fed has highlighted that economy is growing steadily, and inflation is slowing, but it still remains elevated. High frequency indicators for US signal that services sector continues to record improvement, supported by higher employment and new business. Consumer confidence is also up, on hopes of improved job prospects in the next 6 months. On the other hand, manufacturing sector continues to reel under pressure. Situation is similar in Eurozone. Germany recorded continued deterioration in manufacturing activity, albeit at a slower pace. Services activity gained momentum. In China, after noting slowdown in the previous 2 quarters, economy is beginning to show signs of rebound from Sep'24 onwards. Retail sales, industrial production, PMIs have picked up pace. Government is soon expected to announce fiscal measures to further propel growth and achieve 5% GDP target. India will also report Q2FY25 GDP numbers later this month, and we expect 6.9% growth, up from 6.7% in Q1.

Global Central Banks: In Oct/Nov'24, in line with market expectations, major central banks (US Fed, BoE, and ECB) lowered their policy rates. US Fed delivered a 25bps rate cut, keeping in view softening labour market conditions. However, Fed cautioned against elevated levels of inflation and unstainable fiscal policy. Markets are now pricing in another 25bps cut in Dec'24 meeting and a pause in Jan'25. BoE also lowered its policy rate by 25bps, 2nd rate cut in 4 years. Relatively loose labour market conditions and ongoing progress made in disinflation process helped the central take this call. Accounting for recent budget announcements, inflation projections for CY25 were raised to 2.7% from 2.5% in CY24 and growth is also estimated to be higher at 1.5% in CY25 (1% estimated earlier). No more cuts are expected this year, and next year as well, 2-3 cuts being priced in, compared with 4 rate cuts expected earlier. In contrast, BoJ maintained its policy rates unchanged and the statement appeared to be hawkish. New wage settlement deals are expected to push wage growth even higher. BoJ is confident of achieving 2% inflation target in the coming years. A rate hike in Dec'24 remains uncertain.

Key macro data releases: India's trade deficit narrowed down to US$ 20.8bn in Sep'24 compared to US$ 29.7bn deficit seen in Aug'24. This is attributable to faster pace of decline in imports. We expect **India's CAD** to be within a range of 1% to 1.2% of GDP in FY25. BoB Essential Commodity Index (BoB ECI) witnessed significant upswing both on a sequential and YoY basis in Oct'24. There is broad-based price pressure with a pronounced increase visible in tomatoes and edible oil. Core would also be on the upside due to frontloading of festive demand and higher gold prices. **We expect CPI to settle at 5.7% in Oct'24, with risks tilted to the upside**. CPI inflation inched up sharply to 5.5% in Sep'24 from 3.7% in Aug'24, as the favourable base effect waned. Further, food inflation inched up sharply to 9.2% from 5.7% in Aug'24. This can be attributed to higher prices of vegetables, particularly tomato and onion. We expect inflation to average ~4.5-5% in FY25. **The possibility of a rate cut is likely to open up only in Feb'25, as inflation is likely to peak in Q3 FY25**.

Macro developments

Global growth: World to prepare for Trump 2.0

US Presidential election results have given a clear mandate to re-electing President Trump for his second term. This is expected to have an impact on US' fiscal discipline and inflation trajectory and thus Fed's rate cuts. Up till now, advanced estimates for US GDP in Q3CY24 show that the economy expanded by 2.8%, slightly lower than 3% growth registered in Q2. Upward momentum was delivered by higher private consumption (3.7% versus 2.8% in Q2) and government consumption and investment (5% versus 3%). In contrast, private investment growth slowed sharply (0.3% versus 8.3%). At the start of Q4, mixed signals of growth are emerging, which is leading investors to believe that Fed may temper the pace of rate cuts. Labour market is softening, but this trend is considered to be temporary/seasonal. ISM index signals that manufacturing activity continues to remain under pressure, with index dropping to 46.5 in Oct'24 from 47.2. On the other hand, services sectors seems to be holding ground, with ISM index rising to 56 in Oct'24 from 54.9 in Sep'24, led by improvement in employment and supplier deliveries. Consumer confidence also jumped in Oct'24 to 108.7 in Oct '24 from 99.2 in Sep'24, driven by improved economic prospects, mainly on labour market front.

In case of Europe, the economic conditions remain on the weaker side. Further, with Trump returning to power and vowing tariffs on all countries, these conditions are unlikely to improve drastically in the coming months. Latest manufacturing PMI data shows activity in Eurozone contracted at a slower pace in Oct'24 (PMI at 46 versus 45 in Sep'24), mirroring the trend in Germany (43 versus 40.6). New orders fell at a slower pace and input price pressures also eased. In contrast, manufacturing conditions continue to remain weak in the 2nd largest Eurozone economy—France (44.5 versus 44.6). Services activity was also bleak (49.2 versus 49.6), due to drop in new business receipts. Germany's service sector on the other hand is holding ground with index improving to 51.6 from 50.6, supported by clearing of backlogs of work. Germany's IFO business climate index also rose in Oct '24 (86.5 versus 85.4), noting improvement in both current situation and expectations index.

China's Q3CY24 GDP growth was broadly stable (4.6% versus 4.7% in Q2), as economic activity began picking up towards the end of the quarter. Retail sales rose by 3.2% in Sep'24 (est.: 2.5%), up from 2.1% growth in Aug'24. Industrial production increased by 5.4% (est.: 4.5%) following 4.5% growth last month. FAI rose by 3.4% between Jan and Sep'24, unchanged from Jan-Aug'24 period. In Oct'24, conditions seem to be improving further, with official manufacturing PMI at 50.1 (1st since Apr'24) from 49.8 in Sep'24, supported by uptick in sub-index of production and new orders. Non-manufacturing activity is also gaining pace with index up at 50.2 in Oct'24 from 50 in Sep'24. China is soon expected to announce more fiscal stimulus measures to propel the economy, amidst increased risks of tariffs under the new Trump administration.

India's growth: Momentum maintained

India is set to announce the GDP numbers for Q2FY25 later this month. While overall we expect 7.3-7.4% growth in FY25, in Q2 (Jul-Sep) we estimate GDP to have recorded 6.9% growth, following 6.7% increase in Q1. This would be supported by domestic consumption and revival in private and government investment, following the conclusion of general elections in the country. At the start of Q3, momentum is being maintained as reflected in the high frequency indicators. GST collections have maintained a healthy run rate of Rs 1.82 lakh crore in FYTD25 (Apr-Oct) so far, compared with Rs 1.66 lakh crore last year during the same period, indicating sustained domestic demand. Apart from this, helped by festive demand, other indicators of urban consumption have also improved. Air passenger air traffic registered 10.7% growth in Oct'24, up from 7.8% growth seen in Q2. Vehicle registrations noted a steep jump as 28.4 lakh new units were registered in Oct’24 alone, compared with an average of 19 lakh units/month registered in Q2. Services PMI rose to 58.5 in Oct’24 from 57.7 in Sep’24. Bountiful Kharif harvest and a good Rabi season will imply boost to rural demand as well in the coming quarters.

Central bank actions

RBI’s newly constituted MPC decide to keep the repo rate unchanged at 6.5%, with a 5-1 vote. The dissenting vote was cast by Dr. Nagesh Kumar, who voted for a 25bps cut in policy rate. The stance of the monetary policy was changed to “neutral” from “withdrawal of accommodation” by a unanimous vote. The change in stance gives the MPC room to monitor the evolving risks to inflation and can be viewed as a prelude to monetary easing. RBI remained positive on the growth outlook and kept its projection for GDP growth unchanged at 7.2% for FY25. RBI’s estimates for Q3 and Q4 have been revised up by 10-20bps. The RBI also retained its FY25 inflation projections unchanged at 4.5%. Inflation forecast for the current quarter was revised lower by 30bps to 4.1%, to account for the sharp moderation in inflation in Jul and Aug’24. Inflation projection for Q3 FY25 has been revised to 4.8% (from 4.7%), on the back of a negative base as well as uptick in vegetable prices. As a result, we have pushed back the possibility of a rate cut in Dec’24. As of now we expect a rate cut in Feb’25.

US Fed decided to lower the policy rate by 25bps in its latest meeting in Nov’24, thus bringing the policy rate down to 4.5-4.75%. This is the second rate cut since CY20. The FOMC highlighted that “labour market conditions have generally eased, and the unemployment rate has moved up but remains low. Inflation has made progress toward the Committee's 2% objective but remains somewhat elevated”. This has led to investors believing that Fed may pause in Jan’25 meeting, after cutting rates once more by 25bps in Dec’24. While the Fed did not comment about inflation getting impacted under the new Trump Presidency, he cautioned that the current fiscal deficit and debt levels are unsustainable.

In line with market expectations, **Bank of England (BoE)** in its Nov’24 meeting, lowered the policy rate by 25bps to 4.75% with a vote of 8-1. This is the second rate cut, and it comes after first 25bps rate cut was announced in Aug’24. The policy statement continued to maintain a hawkish tone, as Governor Bailey stated that in order to lower inflation gradually, the central bank cannot cut rates too quickly or too steeply. Impact of budget announcements was also taken into account while presenting new forecasts for growth and inflation. BoE raised its growth forecast for CY25 to 1.5% from 1% earlier and expects inflation to also rise to 2.7% in CY25 from 2.5% in CY24. Analysts now expect 2-3 rate cuts in CY25, compared with 4 rate cuts expected earlier.

In line with expectations, **ECB** lowered its policy rates by 25bps in Oct’24, bringing the deposit rate to 3.25% from 3.5% earlier. This decision took into account faltering economic growth in the Euro Area and stabilizing inflation. As more signals appear of deepening economic downturn in the Euro Area, and risk of tariffs have increased following President Trump’s election victory, it is expected that ECB will fast track rate cuts going forward. There remains high chance of 50bps rate cut in Dec’24 meeting.

BoJ in Oct’24 kept its policy rates steady, in line with market expectations. Short-term rate was left unchanged at 0.25%. The central bank believes that inflation is following the projected path and will move towards its 2% target on a durable basis, in coming years. Largest wage hike by Japanese businesses in 31 years also confirms this view. With regard to future rate hikes, analysts had expected a hike in Dec’24 meeting. However, this was at the time of the last meeting, when BoJ Governor had also claimed that geo-political uncertainties have come down. Now post the results of US Presidential election, a rate hike call by BoJ still remains unclear.

Data Releases

Currency outlook

INR depreciated by 0.3% in Oct'24 (0.1% appreciation in Sep'24) and even fell to its lifetime low of 84.09/$. Currently, it is trading around a new low of 84.12/$. However, this decline was only marginal, when compared with bloodbath witnessed in other major currencies, as US$ strengthened sharply during the month (+3.2%). The factors that led to stronger US$ were: rising uncertainty around US Presidential race outcome, and trimmed US Fed rate cut outlook in view of mixed macro data points. Labour market is still perceived to be resilient, when accounted for temporary/seasonal shocks. Consumer confidence is on the rise, and input prices are noting a comeback (US ISM manufacturing sub-index). Domestically, sharp decline in equity indices have led to FPI outflows in this segment. In addition, narrowing spread between US10Y and India 10Y has impacted debt segment FPI outflows. As a result, INR traded in the range of 83.82-84.09/$. In the next fortnight, we expect pressure on INR to remain, but the movement will be range bound. Geo-political developments (US elections, tensions in the Middle East) and domestic inflation trajectory will be closely watched events. We thus expect INR to trade in the range of 83.9-84.2/$ in the current fortnight.

Bond Market Round-up

Upward rally in US 10Y steered other global yields. Resilience in US growth indicators coupled with stickiness in earnings report guided its movement of yield. The spill over was felt in yields across major AEs. In UK, concerns of a fiscal slippage added to further pressure in its yield. Going ahead, volatility in financial market would persist following US election results. Thus, rewinding of positions would continue to exert pressure on global yields till traders are pacified by actual outcome. On domestic front, India's 10Y yield also moved in tandem with other global yields. Geopolitical conflict, rising yield differential with the US and muted corporate results continued to be weighed down on FPI flows. System liquidity remained comfortable. However, some pressure cannot be discounted as credit growth is maintaining its momentum. We expect India's 10Y yield to trade in the range of 6.8-6.9% in the current month, with risks tilted to the upside.

Price picture: Inflation risks linger

BoB Essential Commodity Index (BoB ECI) witnessed significant upswing both on a sequential and YoY basis. There is broad-based price pressure with a pronounced increase visible in tomatoes and edible oil. For the former, lower arrivals were primarily due to a lagged impact of unseasonal rains observed in Sep'24 which impacted mandi arrivals statistics. For edible oils, a sharp increase is visible because of imported inflation as prices globally are heated up. Going forward, rising intensity of climate risks, weaker currency against a stronger dollar and geopolitical risks might pose further upside risks to inflation. Thus, what is required is a holistic policy response of the government in terms of addressing climate related shocks, logistical drawbacks and other supply side disruptions, might be beneficial in bringing down inflation. We expect CPI to settle around 5.7% in Oct'24, with risks tilted to the upside.

India’s Foreign Trade: H1FY25

India’s trade deficit narrowed down to US$ 20.8bn in Sep’24 compared to US$ 29.7bn deficit seen in Aug’24. This is attributable to faster pace of decline in imports. It fell to US$ 55.4bn in Sep’24 from US$ 64.4bn in Aug’24. Correction in gold imports post a sharp spike in Aug’24 has led to the same. Gold imports fell to US$ 4.4bn from US$ 10.1bn. Even non-oil non-gold imports moderated to US$ 36.5bn from US$ 43.3bn. Exports on the other hand, were broadly stable at US$ 34.6bn from US$ 34.7bn, attributable to seasonal fluctuations. On a seasonally adjusted MoM basis, exports growth rose at a higher pace of 4% while imports growth declined at a less sharp pace by 8%, thus supporting the trade deficit. In terms of commodity wise exports, Drugs and Pharma, engineering goods and chemicals gained pace. Higher inflationary pressure in cereals, pulses, edible oils has kept a lid on exports of agriculture and allied products. Textile exports also picked pace amid global shifts. Imports in H1FY25 have picked up at a faster pace than exports by 6.2% compared to a decline of 11.3%, seen during the same period of last year. The increase is attributable to increase in non-oil non-gold imports to US$ 222.7bn compared to US$ 211.3bn, signalling some headway in domestic consumption demand notwithstanding inflationary impact. Overall, we expect India’s CAD to be within a range of 1% to 1.2% of GDP in FY25.

WPI inflation scales up

WPI inflation climbed to 1.8% in Sep’24 compared with 1.3% in Aug’24, driven by food inflation. Our forecast for headline WPI inflation was at 2.2%. Uptick in both onion and tomato prices pushed vegetables inflation higher. Under food-grains, moderation in prices of paddy and pulses was noted. Fuel and power inflation remained in deflation at 4%, supported by dip in both domestic and global oil prices. Manufactured products inflation softened to 1% from 1.2% in Aug’24. The evolving geopolitical condition needs careful monitoring specially in terms of outlook on global commodity prices for oil and metals. With higher sowing better than last year, the arrivals of kharif crops is likely to be better this year. Against this back drop, we expect WPI to ease in Q4 in line with CPI provided oil and food shocks are not triggered. Any rate action by RBI is warranted only in Q4FY25.

CPI inflation

CPI inflation inched up sharply to 5.5% in Sep’24 from 3.7% in Aug’24, as the favourable base effect waned. Further, food inflation inched up sharply to 9.2% from 5.7% in Aug’24. This can be attributed to higher prices of vegetables, particularly tomato and onion. Significant price pressures were also visible in case of edible oils, in line with an uptick in global prices. Prices of cereals and pulses saw some much-needed correction, and are expected to ease further as fresh kharif harvest enter the market. Higher gold prices also fed into core inflation, which picked up to 3.5%. The outlook on inflation hinges on how food prices behave. High frequency price data shows that prices of key items such as tomato and onion have maintained an upward momentum even in Oct’24. Hence, we expect inflation to remain elevated in Oct’24 as well, barring any adverse weather shock. Unseasonal rains remain a key risk, especially since prices of perishables is highly sensitive to weather shocks. We expect inflation to average ~4.5-5% in FY25. The possibility of a rate cut is likely to open up only in Feb’25, as inflation is likely to peak in Q3 FY25.

Growth in Industrial Production

IIP growth fell by (-) 0.1% in Aug'24, from 4.7% in Jul'24, mainly driven by base effect. Mining and electricity output dropped in Aug'24, due to continued monsoon activity, while manufacturing production slowed. On FYTD basis as well, growth eased to 4.2% so far (Apr-Aug'24) from 6.2% last year. Within manufacturing, laggard growth was seen in case of vehicles, electronic/machinery/other transport equipment and basic/fabricated metal & products. In terms of use-based classification, primary and consumer non-durables registered a decline in output, while other sub-heads noted moderation. Going forward, as monsoon activity slowed in Sep'24, we expect some improvement in electricity output. Further, as government spending has seen picking up pace, we expect revival in construction activity and thus increase in output of related products. Also, as festive and harvest season begins, and base effect turns more favourable, we expect headline IIP growth to pick up in the coming months.

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