

## Economic Round-up: December 2024

The year 2025 has begun on a note of heightened global uncertainties. From anticipation of President-elect Trump's economic policies to snap election in Germany and impact of stimulus on China's economy, market participants are awaiting for more cues. To add to this, US economy is giving mixed signals regarding growth. While labour market appears to be softening and manufacturing activity is weak, but retail sales, pending home sales and service sector seems to be doing well. Input prices for manufacturing are already creeping back up and if Trump administration announces global tariffs, risks to inflation will further increase. Markets thus keenly await transfer of Presidency, due later this month. In Europe, manufacturing activity is unable to pick up pace so far, while service sector is regaining ground. Election results in Germany will determine future growth path. In China, while manufacturing sector is expanding slowly, lifting domestic consumption and reviving real estate sector is proving to be task for the administration. China announced stimulus measures towards the end of the year in CY24 and has vowed to announce more in CY25, to push growth beyond 5%. Domestically, India is in a much stronger position with high frequency indicators showing pick up in pace of growth in Q3FY25. GST collections, service PMI, air passenger growth, and vehicle registrations, all seeing notable improvement in Q3 versus Q2.

**Global Central Banks:** In Dec'24, in line with market expectations, major central banks (US Fed, ECB) lowered their policy rates. US Fed delivered a 25bps rate cut, but cautioned that rate cuts might be slower in CY25, depending upon evolving inflation conditions. Both GDP and inflation forecasts were revised upward by Fed for CY25. ECB also lowered its policy rate by 25bps—4<sup>th</sup> rate cut in CY24. This was in line with lower inflation projections and faltering growth scenario. Analysts expect continuous rate reduction by ECB till Jun'25. In contrast, BoE held policy rates unchanged, but the voting split widened, signalling more dovish stance of the central bank. However, given the sustained rise in wage inflation, sticky services inflation and risks to prices if US imposes tariffs, investors expect fewer rate cuts from BoE in CY25. In case of BoJ, while the central bank held policy rates unchanged, it signalled that stability in wage rise will be analysed by the central bank before it decided to hike rates again. As a result, next rate hike is not expected before Mar'25.

**Key macro data releases:** India's CAD narrowed to 1.2% of GDP in Q2FY25 from 1.3% of GDP in Q2 FY24. While the trade deficit was higher, buoyant services exports as well as continued strength in remittances underscored the lower CAD. Our **year-end market analysis** shows that both Sensex and Nifty 50 surged by 8.7% and 9% in CY24. Sensex touched an all-time high this year as it breached the mark of 85,500. Sectors including real estate, consumer durables and IT were amongst the best performing stocks in CY24. INR depreciated by 2.8% in CY24, but remained one of the better performing currencies amongst other its peers. India's 10Y bond yield moderated down by 44bps. The pressure on yields was lower and boosted demand flow as the market witnessed the bond inclusion in the JP Morgan emerging market index, Bloomberg and FTSE Russel. **CPI inflation** moderated to 5.5% in Nov'24 versus 6.2% in Oct'24, on YoY basis, led by favourable base. Apart from this, food inflation went down by 183bps to 9% in Nov'24 compared to 10.9% in Oct'24. Core inflation was at 3.7% in Nov'24. Slight momentum was seen in household goods and services component due to front-loading of festival demand.

## Macro developments

### Global growth: US economic momentum continues

Third estimates of **US** GDP for Q3CY24 showed that growth was revised higher to 3.1% (3% in Q2) from 2.8% estimated as per second estimates. This was primarily due to upward revisions to exports and government consumption. Part of its impact was offset by downward revisions to private inventory investments. As a result, US Fed has also revised its growth projections upwards. Further given steady demand conditions, inflation estimates have also been revised higher by the central bank. In addition, given mixed signals of growth in Q4, investors have priced in fewer rate cuts in CY25. Labour market is softening, with continuing jobless claims as of 14 Dec 2024 rising by 46k from the previous week to 1.91mn—highest since 13 Nov 2021 (1.97mn). Flash Markit manufacturing PMI suggests activity weakened further in Dec'24 to 3-month low of 48.3 (49.7 in Nov'24). Survey also showed that input cost pressures are rising. In contrast, price pressures in the services sector remain muted, and activity is also improving (58.5 in Dec'24—38 month high; 56.1 in Nov'24). US pending home sales index jumped to 21-month high of 79 (+2.2%) in Nov'24, up from 1.8% in Oct'24, despite elevated mortgage rates.

In case of **Europe**, economic conditions remain bleak. ECB has lowered its growth forecasts for both CY24 and CY25. BoE also expect flat growth (0%) in UK in Q4CY24, down from 0.3% estimated earlier. Further, with Trump returning to power and vowing tariffs on all countries, economic uncertainties have increased further for both Eurozone and UK. Latest flash manufacturing PMI data shows activity in Eurozone contracted at an unchanged pace of 45.2 in Dec'24, dragged by conditions in both France (41.9 versus 43.1) and Germany (42.5 versus 43). New orders fell at the sharpest pace in three months, driven by “client hesitancy, strong competition for new work and lower demand from abroad”. In the services sector, input inflation is making a comeback, implying that ECB might not have as much room to lower rates this year, as expected by market participants. Snap elections in Germany in Feb'25, may provide more political clarity and help growth prospects in the near-term.

China's official manufacturing PMI index showed that activity remained in expansion in Q4, even as its pace slowed to 50.1 in Dec'24 from 50.3 in Nov'24. Industrial production in Nov'24 had also picked up pace as it rose by 5.4% (est.: 5.3%) from 5.3% in Oct'24. In contrast, China continues to face significant challenges in lifting its domestic consumption as property sector remains under stress for the 4<sup>th</sup> consecutive year now. Retail sales growth eased to 3% (est.: 4.6%) in Nov'24 from 4.8% in Oct'24. Real estate investment fell further on CYTD basis in Nov'24 by (-) 10.4% compared with (-) 10.3% decline noted between Jan-Oct'24. Overall FAI growth also slowed to 3.3% (est.: 3.4%) as of Nov'24 (CYTD basis), compared with 3.4% as of Oct'24. In New Year's Day address, Chinese President has assured more policy support to boost growth in CY25. Growth is expected to average around 5% in CY25 as well, and fiscal deficit (% of GDP) is estimated to expand to a record high of 4%.

### India's growth: Momentum in Q3FY25 sustained

High frequency indicators have shown notable improvement in Oct-Dec'24 (Q3FY25) period. GST collections have jumped by 8.3% (YoY) in Q3 to Rs 5.5 lakh crore, and are also up from Rs 5.3 lakh crore in Q2, signalling further improvement in consumption pattern. Apart from this, helped by festive demand, other indicators of urban consumption have also improved. Air passenger air traffic registered 11.6% growth in Q3, compared with 7.8% growth registered in Q2. In CY24, passengers flown rose by 31.6mn from last year to 401.5mn. Vehicle registrations noted a steep jump with 11.3% (YoY) higher registrations in Q3 versus 3% higher in Q2. Services PMI averaged 59.2 in Q3 versus 58.1 in the same period last year. We expect quarterly corporate results to also show improved performance in Q3.

## Central bank actions

**RBI's MPC** with a 4-2 majority kept repo rate unchanged at 6.5%. The dissenting votes were cast by 2 of the 3 new members of the MPC. Stance was kept at neutral to allow the MPC flexibility on future path of policy action. This is important as the Governor's statement underlined the need for maintaining a favourable growth-inflation balance, as the two are highly interlinked. RBI now forecasts GDP growth lower at 6.6% in FY25, while inflation is projected higher at 4.8%. However, with growth expected to recover in H2 and inflation abating, we see a scope of 25bps rate cut in Feb'25. We expect a cumulative easing of 50-75bps in the current cycle.

**US Fed** decided to lower the policy rate by 25bps in its latest meeting in Dec'24, thus bringing the policy rate down to 4.25-4.5%. This is the third rate cut since CY20, taking the cumulative cuts to 100bps in CY24. However, more hawkish projections for next year spooked the markets. The dot plot indicates only 2 rate cuts in CY25. In the near-term, Fed expects GDP to have performed better than expected in CY24 (2.5% versus 2% estimated in Sep'24) and inflation will remain sticky (2.4% versus 2.3%). In CY25 as well, growth is expected to be higher (2.1% versus 2%), but worryingly, more significant jump is projected in inflation (2.5% versus 2.1%). Fed Chair has also cautioned that central bank will be monitoring evolution of government policies to gauge its impact on growth and inflation.

In line with market expectations, **Bank of England (BoE)** in its Dec'24 meeting, held the policy rates unchanged at 4.75% with a vote of 6-3. With this, BoE has made cumulative rate cut of 50bps in CY24. The split widened compared with 8-1 vote in the last policy meeting. Despite seemingly dovish voting pattern, BoE is unexpected to cut rates too steeply in CY25. Governor Bailey stated that "with the heightened uncertainty in the economy we can't commit to when or by how much we will cut rates in the coming year". With wage inflation exerting upward and services inflation sticky, BoE expects inflation "to rise slightly in the near term". Risks to growth also appear to be more significant than previously expected, leading to central bank reducing GDP forecast for Q4CY24 to 0% from 0.3% estimated earlier.

The **ECB**, in line with market expectations, lowered rates by another 25bps in its Dec'24 meeting, bringing the deposit rate to 3% from 3.25% earlier. This is in line with lower inflation projections. ECB now expects headline inflation at 2.4% in CY24 (2.5% estimated in Sep'24) and at 2.1% in CY25 (2.2% earlier). Growth however is expected to weaken further, with GDP now projected at 0.7% (0.8% earlier) in CY24 and at 1.1% (1.3% earlier) in CY25. As a result, analysts expect ECB to cut rates continuously till Jun'25 (4 cuts) and bring the policy rate to 1.75% by end CY25.

**BoJ** kept its policy rate unchanged (est.: 25bps hike), with a split 8-1 vote in Dec'24. Market expectations were split between a rate hike and pause. Uncertainty around price trajectory and global policy developments (President-elect Trump takes charge in Jan'25), led to this decision. Japan's CPI has remained above BoJ's target (2%) for 30 consecutive months so far, however, pressures appear to be easing now. Governor Ueda cautioned that the central bank will await "sustainability of wage increases" to gauge the timing of another rate hike. As a result, analysts now expect a rate hike by BoJ in Mar'25, when wage negotiations take place.

## Data Releases

### Markets: Year-end Round-up

Global equity indices performed stupendously ending CY24 on a high with a rally noted across the board. In the US, major indices including S&P 500 and Dow Jones continued to clock double digit gains on an annual basis. Within S&P 500, sectors such as technology, communication services along with consumer discretionary registered biggest gains for the year. Furthermore, both Hang Seng and Shanghai Comp rebounded sharply as they reversed their losing streak and advanced by 19.5% (-17% in CY23) and 13.1% (-5% in CY23) respectively in CY24. Notably, on the domestic front both Sensex and Nifty 50 surged by 8.7% and 9% for the same period. Sensex touched an all-time high this year as it breached the mark of 85,500. Sectors including real estate, consumer durables and IT were amongst the best performing stocks in CY24.

In CY24, the DXY index, which is used as a measure of dollar's strength against a basket of 6 major currencies gained by 7%. This was supported by the geopolitical conflict in Middle East, the ongoing Russia-Ukraine conflict which all contributed in strengthening dollar's demand. Yen was amongst the weakest performing currency as it weakened (4th time in a row) again as the interest rate differential between US and Japan widened. INR depreciated by 2.8% in CY24, but remained one of the better performing currencies amongst other its peers. RBI continued with the forex intervention in order to address the weakness in the currency. India's foreign exchange reserves dropped down by US\$ 8.5bn to US\$ 644.3bn for the week ending 20 Dec 2024. Stable CAD and lower oil prices also supported the rupee. In CY25, INR is expected to depreciate marginally as volatility in FPI flow might continue given the likelihood of stronger dollar.

Global yields ended mixed. The benchmark US treasury yields climbed up by 69bps in CY24 ending the year above 4.5%. Mixed economic signals through the data points resulted in the sideways movement of the yields through the year. In CY25, there is some uncertainty at play owing to the impact of the upcoming policies that will laid down by Donald Trump administration and these could be inflationary. Additionally, Fed shifting gears based on the inflation risk as it continues to remain above the target level along with the recent uptick in unemployment and close tracking of economic activity, signals some risks to rate cut expectation. India's 10Y bond yield moderated down by 44bps. The pressure on yields was lower and boosted demand flow as the market witnessed the bond inclusion in the JP Morgan emerging market index, Bloomberg and FTSE Russel. Expectation of rate cut by RBI are back on the table beginning with possibly Feb'25 after keeping rates on hold at 6.5% since Feb'23.

### Banking sector update-Oct'24

Overall growth in credit has slowed down by almost half in terms of growth rate to 10.6% in November. Within the 4 broad sectors, only industry witnessed higher growth compared with last year. The heartening part of growth to industry is that there have been double digit growth rates registered for MSME segment. In case of large industry, while it is at 6.1%, it is higher than last year when it was 2.9%. Growth in credit to services slowed down from 25.7% to 13%. The two large segments, NBFCs and trade witnessed major slowdown. For NBFCs it was down from 18.9% to 7.8% and for trade 20.6% to 14.5%. There was moderation for real estate which is the third largest component from 44.2% to 14.3%. In case of retail loans some features stand out. Unsecured lending slowed down to 11.6% from 24.9%. Credit card growth, though high at 18.1% was lower than 34.2% achieved last year. There was slowdown in growth of the two largest segments, partly due to the high base effect. Home loans were at 12.2% as against 36.7% last year while vehicle loans was at 10.3% (20.6%). At the aggregate level there has been some traction in credit growth to 11.5% for fortnight ending Dec 13 and this may be expected to increase in coming months based on the assumption that both investment and GDP growth pick up.

## **CAD narrows despite higher trade deficit**

India's current account deficit narrowed to 1.2% of GDP in Q2FY25 from 1.3% of GDP in Q2 FY24. While the trade deficit was higher, buoyant services exports as well as continued strength in remittances underscored the lower CAD. A surge in gold imports can explain the higher trade deficit, even though oil imports were largely in check. Capital account surplus expanded, led by FPI inflows, while FDI outflows were recorded higher. As a result, BoP surplus was recorded higher at US\$ 18.6bn compared with US\$ 2.5bn in Q2 FY24. Going ahead, a surge in gold imports is likely to push CAD for Q3 FY25 to above 2% of GDP. However, this is likely to be cushioned by services and remittances receipts. Overall, we expect CAD at 1.2-1.5% of GDP in FY25, with US trade policies being a key risk to the outlook. Sluggish FPI inflows along with a stronger dollar will continue to exert pressure on INR.

## **WPI inflation cools down**

WPI inflation eased to 1.9% in Nov'24 from 2.4% in Oct'24. This was due to significant moderation in food inflation. Core and manufactured product inflation on the other hand inched up. Food inflation slowed to 8.9%, on account of notable softening in vegetable and fruit prices. Within this, basic items like onions and tomatoes registered easing. Apart from this, food grain inflation also cooled down, helped by pulse inflation. In contrast, cereal inflation remains sticky, due to higher wheat inflation. Separately, slower pace of decline in international oil prices have had an impact on domestic fuel inflation. Mineral oil inflation index fell at a slower pace, leading to build up in price pressure for ATF, Kerosene, and furnace oil. Manufactured goods inflation was higher primarily due to jump seen in basic metals (mainly aluminium and Zinc). Domestically, revival in government investment activity seems to be pushing commodity prices higher. Globally, prices remain weak, owing to continued signs of strains in China's demand and prospects of higher inflation denting demand, if US imposes tariffs. Going forward, price trajectory will depend upon foreign trade policy of incoming President-elect Trump and stimulus measures announced by China to boost growth. These pose upside risks to inflation.

## **Food inflation: some silver lining**

CPI inflation moderated to 5.5% in Nov'24 (BoB est.: 5%) compared to 6.2% in Oct'24, on YoY basis. This comes in the wake of a favorable statistical base (5.6% in Nov'23 compared to 4.9% in Oct'23). Apart from this, food inflation went down by 183bps to 9% in Nov'24 compared to 10.9% in Oct'24. Going forward, the outlook of food inflation is expected to be benign. December witnessed further correction in major vegetable prices. Even Mandi arrival statistics of TOP vegetables (Tomato, Onion and Potato) are comfortably higher compared to same period of previous year. Expectation of good soil moisture along with adequate reservoir levels will bode well for Rabi harvest, as well. Core inflation was at 3.7% in Nov'24, on YoY basis. The sub-components of core gave a divergent picture. On one hand, slight momentum was seen in household goods and services component (2.8% in Nov'24 compared to 2.7% in Oct'24) due to some front-loading of festival demand. High frequency price data of Dec'24 is showing further correction with our in-house BoB ECI reading showing just 0.1% sequential increase in prices compared to 0.4% in Nov'24. The coming few inflation points remain crucial in veering RBI's policy compass towards an easier regime. Further, no demand side pressure is visible from core inflation reading, thus keeping it largely capped. We expect headline CPI to settle ~4.7-4.8% in FY25.

## **Industrial production strengthens**

Higher IIP growth at 3.5% was registered for Oct'24 compared with 3.1% growth in Sep'24. Across the board improvement was seen for the sectors. Electricity and mining growth advanced by 2% and 0.9% in Oct'24. Manufacturing growth rose by 4.1%. Within manufacturing, following sectors such as electrical equipment, fabricated metal and other transport equipment lifted growth. In terms of use-based classification, output of primary, infrastructure goods and consumer non-durables registered a steady increase. In the coming months, we expect further improvement in production. This has also been reflected by high frequency indicators. Furthermore, with the expectation of pick-up in government spending followed by improvement in both government and private investment in H2, the IIP growth will perform a lot better in H2FY25 from H1FY25.

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