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Economic Round-up: February 2025

Tariffs on Canada, Mexico and China, announced by US President Donald Trump, have come into effect from this month. These countries have also announced retaliatory tariffs on imports from the US, leading to start of a full-fledged trade war. Now US will soon announce more reciprocal tariffs on a wider set of economies, including India, from Apr'25 onwards. This escalation has raised concerns regarding a hit to global growth and has also revived fears of rising inflation. US economy is already showing signs of slowdown (existing home sales, consumer confidence, PMIs). Markets believe that if Fed delays rate cut action then the US economy may even enter a recession. So far investors are expecting 2-3 rate cuts by Fed this year. Businesses across the globe are now devising plans to manage their supply chains to avoid the impact of this trade war. Europe's major economy, Germany, is at most risk. Following the announcement of recent elections in Germany, hopes have increased that the new government may remove the debt ceiling clause to expand its fiscal deficit and provide much needed boost to infrastructure spending. Domestically, India's GDP growth softened to 6.2% in Q3FY25, following 9.5% growth in Q3FY24. Unfavourable base and lower sectoral growth in manufacturing and mining sector dragged the overall growth down. However, agriculture sector, private consumption and government spending remained bright spots. In Q4, economic prospects are improving with robust GST collections, toll collections and e-way bills generation. Kumbh mela will also provide a boost to economy in Q4.

Global Central Banks: In Jan/Feb'25, in line with market expectations, US Fed held rates steady, while ECB and BoE lowered rates by 25bps. Fed officials have repeatedly cautioned against sticky inflation. However, now with growth slowing, analysts expect 2-3 rate cuts this year. The ECB lowered its policy rate by 25bps, given the ongoing steady disinflation process and weak economic momentum. BoE after reducing its key policy rates by 25bps, may lower rates twice by Nov'25. However, in case inflation surges again (as projected by BoE for H2CY25), then these chances may dwindle. In case of BoJ, the central bank recently hiked rates by 25bps, taking short-term rate to 0.5% from 0.25% earlier. Now given that inflationary momentum is still continuing in Japan, analysts have raised their bets for another rate hike by BoJ soon. Markets are pricing in rate hike to 0.75% by Jul'25.

Key macro data releases: India's GDP growth softened to 6.2% in Q3FY25, following 9.5% growth in Q3FY24. Unfavourable base and lower sectoral growth in manufacturing and mining sector dragged the overall growth down. On the other hand, private consumption recorded a higher growth of 6.9% in Q3FY25 versus 5.7% in Q3FY24. GVA registered a growth 6.2% in Q3FY25 in line with our expectation compared with a growth of 8.0% in Q3FY24. Agriculture and public admin also turned out to be bright spots. **CPI inflation** softened to 4.3% in Jan'25 from 5.2% in Dec'24, helped by 237bps decline in food inflation which went down to 6% in Jan'25 from 8.4% in Dec'24. Core CPI (excl. food and fuel) remained sticky at 3.6%. The broad underlines of core have shown little or no momentum. Housing inched up a tad and the miscellaneous component of core was largely driven by personal care and effects. We expect **10Y yield** to trade in the range of 6.65%-6.75% in Mar'25, with certain upside risk including tightening liquidity conditions amidst tax outflows. For **INR**, we expect a range of 86.75-87.75/$ (and could also touch Rs 88/$ before reverting to this range) this month.

Macro developments

Global growth: Trade war escalating

US President Donald Trump has started a trade war with major global economies by announcing tariffs. US has levied 25% tariffs on imports from Canada and Mexico and 10% on Chinese goods. This has been met with reciprocal tariff (same magnitude) announcements by these countries. Now from Apr'25 onwards another round of tariffs will be levied on imports from these countries and some of the other major economies, including India. This has stocked fears of global growth uncertainties and inflation. US economy is already staring at risks of stagflation. Latest macro data shows that ISM manufacturing index slowed to 50.3 in Feb'25 from 50.9 in Jan'25, due to contraction in new orders and employment. Conference board consumer sentiment for Feb'25 fell to 98.3 from 105.3 in Jan'25, led by drop in both present situation and expectations index. Inflation expectation jumped sharply to 6% 5.2% in the previous month. Retail sales in Jan'25 fell (MoM basis) by (-) 0.9% following 0.7% increase in Dec'24. Existing home sales fell by (-) 4.9% in Jan'25 to 4.08mn units, lower than est.: 4.12mn units. Some analysts believe if Fed delays rate cuts for too long then US economy may even enter into a recession.

In case of **Europe**, economic conditions have begun to stabilize on some levels. For instance, manufacturing PMI for EZ rose to 47.6—24 month high in Feb'25 from 46.6 in Jan'25. In Germany and France too activity contracted at a slower pace in Feb'25. Services activity remained in expansionary zone (index unchanged a t 50.2 in Feb'25), but in Germany and France momentum seems to be weakening. While pace of growth slowed in Germany (51.1 in Feb'25 versus 52.5 in Jan'25), business activity contracted further in France (45.3 versus 48.2). Inflation so far continues to follow the disinflationary process with CPI at 2.4% in Jan'25 from 2.5% in Feb'25. As a result, ECB is expected to continue cutting rates aggressively this year to also deal with the impact of growth slowdown due to US tariffs. Further, in Germany, there is hope of revival in government spending to give economy a boost, as general elections last were broadly in line with market expectations. The new government may aim to remove the debt ceiling level clause in order to provide fiscal stimulus.

China's official manufacturing PMI index jumped to 50.2 in Feb'25 from 49.1 in Jan'25, supported by steep increase in new export orders. Importers are trying to place advance orders before US tariff rates on Chinese products rise even higher. Even the non-manufacturing PMI improved to 50.4 from 50.2. Private surveys (Markit/Caixin), covering smaller companies, also indicate a similar trend. For the current year (CY25), government has reaffirmed its GDP target of "around 5%"—same as last year, and despite threats to growth due to escalated trade war with the US. In the latest NPC meeting, government also raised its fiscal deficit target (% of GDP) to "around 4%"—highest since CY10 and "around 3%" last year. This signals that fiscal stimulus will be used to counter economic headwinds and boost growth.

India's growth to pick up in Q4

India's GDP growth softened to 6.2% in Q3FY25, following 9.5% growth in Q3FY24. Unfavourable base and lower sectoral growth in manufacturing and mining sector lowered growth rate. Weakness was noted in investment in Q3 with GFCF growth registering a growth of 5.7% against 9.3% last year. Imports growth contracted by (-) 1.1% in Q3FY25 compared with 11.3% increase in Q3FY24. On the other hand, private consumption recorded stupendous growth of 6.9% in Q3FY25 versus 5.7% in Q3FY24. GVA registered a growth 6.2% in Q3FY25 in line with our expectation compared with a growth of 8.0% in Q3FY24. Tepid growth was noted in manufacturing (3.5% from 14%) and mining (1.4% against 4.7%), which was expected given only gradual improvement in corporate profits. Growth in trade, hotels (6.7% from 8%) and financial sector (7.2% from 8.4% in Q3FY24) also softened in Q3FY25. However, agriculture sector turned out to be bright spot registering a robust growth of 5.6% in Q3

compared with 1.5% increase in the same quarter last year supported by improvement in Kharif output and higher Rabi sowing. Furthermore, in line with expectations, public admin registered a strong growth of 8.8% against a growth of 8.4% in Q3FY24. For full year, growth is estimated at 6.5% given robust growth in agriculture sector. Growth is expected to advance in Q4 further as has been evident form the high frequency indicators.

In Q4, mixed signals of growth are visible. Indicators which are showing an improvement include: GST collections (average Rs 3.8 lakh cr in Jan-Feb'25 versus Rs 3.4 lakh cr Jan-Feb'24), e-way bill generation (23.1% in Jan'25 versus 16.4% in Jan'24 and 16.9% in Q3FY25) and toll collections (average 16.7% growth in Jan-Feb'25 versus 11.2% in Jan-Feb'24 and 14% in Q3FY25). On the other hand, indicators like air passenger traffic, vehicle registrations, cooled down in Jan-Feb'25 period. However, we see an upside bias to GDP growth in Q4FY25 supported by Kumbh Mela boost to consumption, services and FMCG sector.

Central bank actions

RBI MPC unanimously lowered the repo rate by 25bps from 6.5% to 6.25%. Stance was kept at neutral. RBI Governor noted the need for "less restrictive" monetary policy to support growth as inflation remains within RBI's targeted band. The central bank expects growth to improve in FY26 to 6.7% from 6.4% in FY25. Inflation is projected to come down to 4.2% in FY26 from 4.8% in FY25. CPI will remain broadly sticky in Q4FY25 (4.4%) and Q1FY26 (4.5%). These projections also take into account rupee volatility. From Q2 onwards, inflationary pressures are expected to ease significantly, giving room to RBI to lower rates further. We expect up to 75bps (cumulative) reduction in rates in this calendar year. At the time of next rate cut, we also expect change in stance.

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. Latest PCE data shows cooling inflation, while consumer sentiment indices are showing firming up of inflation expectations. This along with slowing growth momentum has led investors to believe that 2-3 rate cuts may be forthcoming in this calendar year as US economy stares at the risk of stagflation.

Bank of England (BoE), in line with market expectations, reduced rates by 25bps in Feb'25 to 4.5% from 4.75%. This takes the cumulative cuts in the current cycle to 75bps. Slowing economic growth was a key driver of this decision. BoE revised its CY25 projection lower to 0.75% compared with 1% estimated in Nov'24. The central bank also expects 0.1% growth in the current quarter. On the inflation front, the room for rate cuts seems smaller towards the end of the year, as BoE expects higher energy and water bills in that period (peak inflation at 3.7%). Investors are now pricing in 2 rate cuts by Nov'25.

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. Now in the meeting this week, analysts expect another 25bps cut. Apart from this, another 2-3 rate cuts are expected this year, as inflation continues to slow and growth remains stagnant over the past 2 years. 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. The central bank expects its neutral rate around 1-2.5%, signalling that there remains room for more rate hikes. More traders are betting on BoJ to hike rates aggressively as inflation pressures mount. One of the BoJ official has even hinted that rates should be hiked to 1% level.

Data Releases

Bonds Wrap

Uncertainty around global economic growth and heightened market volatility amidst lingering geopolitical tensions, tightening financial conditions and escalated concerns around possible impact of tariff war, has kept the global investors on the edge. US 10Y yield moderated given the growing risk of slowing economy and the same has been reflected by weaker consumer sentiment and retail sales print. On the domestic front, given the moderation in inflation and evolving liquidity conditions, India's 10Y yield eased. Extensive efforts by RBI in managing liquidity through VRR auction supported bond yields. Going forward, the 10Y yield is expected to trade in the range of 6.65%-6.75% in Mar'25, with certain upside risk including tightening liquidity conditions amidst tax outflows. On policy rate, we anticipate RBI will wait and watch before taking any action in Apr'25 given the moderation in headline inflation.

Currency update

INR depreciated by 1% in Feb'25, marking its 5th straight monthly decline. Persistent FPI outflows and uncertainty over US tariffs have kept INR under stress. Since Oct'24, domestic markets have witnessed outflows of over US$ 22bn. An expected rebound in domestic GDP growth, range bound oil prices and strong external buffers are positive for INR. However, given the continued volatility in global financial system, the scope of INR appreciation looks limited. US tariff policies and hence the dollar, will play a greater role in where the INR goes from here. We expect a range of 86.75-87.75/$ (and could also touch Rs 88/$ before reverting to this range) in the coming month.

Sectoral bank credit growth in Jan'25

Growth in bank credit (non-food) moderated in Jan'25, dipping to 11.4% compared with 20.4% in Jan'24. However, on a sequential basis, there was a pickup in credit growth (11.1% in Dec'24). While credit growth to industry held steady at 8% in Jan'25 on a YoY basis, credit to all other sectors slowed down. Agriculture credit growth decelerated to 12.2% in Jan'25 compared with 20% in Jan'24. Within industry, credit growth to medium industry picked up sharply to 18.5% in Jan'25 compared with 10% growth in the same period last year. However, there was a slowdown in credit growth to the micro and small industry to 9.5% versus 16% in Jan'24. Credit growth in the services sector eased to 12.5% in Jan'25 from 24.2% in Jan'24. Except shipping and computer software, all sub-sectors noted a decline in credit growth vis-à-vis Jan'24. Credit growth to commercial real estate slowed down to 13.9% in Jan'25 versus 42.9% in Jan'24. Credit growth to NBFCs also continued to slow and dipped to 7.7% in Jan'25 versus 15.6% in the same period last year. With RBI restoring the risk weights on SCBs' exposure to NBFCs, this trend is likely to reverse. Retail credit growth rose at its slowest pace since Mar'21 at 11.8% in Jan'25, versus 28.6% in Jan'24. Within this segment, while the demand for unsecured lending through other personal loans/credit card outstanding moderated. Demand for gold loans continues to accelerate.

Health of central government finances

Centre's fiscal deficit has reached Rs 11.7 lakh crore as of Jan'25 (FYTD basis) which is 74.5% of the revised budget estimate, compared with 63.6% of the target achieved last year during the same period. As % of GDP (12MMA basis) it is currently running at 5.3% versus targeted 4.8%. The deficit ratio has remained higher than RE since Oct'24 as government aims to fulfil is expenditure targets, following a slow start at the beginning of the year due to general elections. In Jan'25 (FYTD basis), centre's expenditure growth improved notably, while receipt growth witnessed some easing compared with Dec'24. Amongst the receipts, corporate tax collections were the major drag, while income tax collections held ground and indirect tax collections improved (mainly customs and CGST). On the spending front, government has achieved 75.7% of its revised estimate, higher than 74.7% last year (as of Jan'24). Major ministries which have spent more than last year (as % of RE) include, ministries of railway, consumer affairs, rural development, defence, home affairs, education and health. We can expect the pace to moderate in the coming months as ministries have moved closer to their revised targets. As a result we continue to believe that centre will meet its fiscal deficit target of 4.8% in FY25.

WPI inflation softens

WPI inflation eased to 2.3% in Jan'25 from 2.4% in Dec'24, led by moderation in food inflation. On the other hand, manufactured product inflation inched up and slower pace of deceleration was noted in fuel and power inflation. As a result, core inflation rose to 0.9% from 0.7%. Food inflation softened to 7.5% in Jan'25. Within this, vegetables and protein based items noted moderation, while inflation for food grains, fruits and condiments and spices noted upward pressure. Amongst vegetables, tomato and potato prices registered a decline. Within fuel, mineral oil and electricity indices decelerated at a slower pace. Mineral oil index mirrors the movement in international oil prices. Within manufactured products, food, wearing apparels, basic metals (mainly aluminium) and electronic items led inflation higher. Going forward, as Fed decides to keep rates 'higher for longer', global demand prospects have been dented and are putting some downward pressure on oil and other commodity prices. However, based on retaliatory measures announced by countries with regard to tariffs imposed by the US, the global inflation situation will evolve. In India's case, imported inflation, due to stronger US$ remains a key risk, but lower oil and commodity prices may help ease upside risks.

Food putting a brake on CPI

CPI inflation softened to 4.3% in Jan'25 from 5.2% in Dec'24 (BoB est.: 4.7%), on YoY basis. The undershooting was supported by a significant correction in food inflation which went down by 237bps to 6% in Jan'25 from 8.4% in Dec'24. The major slump was noticed in the case of vegetable inflation (11.3% in Jan'25 compared to 26.6% in Dec'24). Bumper arrivals of TOP (Tomato, Onion and Potato) since Nov'24 has contributed to the same. Core CPI (excl. food and fuel) remained sticky at 3.6%, on YoY basis. However, core excluding pan, tobacco and intoxicants was slightly higher at 3.7%, on YoY basis. The broad underlines of core have shown little or no momentum. Housing inched up a tad by 2.8% from 2.7% in Dec'24. The miscellaneous component of core was largely driven by personal care and effects (10.6% from 9.8%). As during the same period gold prices went up by 33% on YoY basis. Going forward, if volatile items of CPI especially vegetable inflation continues to play in favour, alignment to the inflation target seems feasible. Our forecast also looks at progressive alignment to the 4% level. However, upside risks emanate from a depreciating rupee which poses risks of imported inflation and bottoming out of commodity price cycle from threats of tariff imposed by the US. We expect CPI to settle at ~4.9% in FY25 and 4.6% in FY26, with risks tilted to the upside.

Industrial production growth cools down

Tepid growth in manufacturing sector resulted in dragging down IIP growth lower at 3.2% in Dec'24 compared with a growth of 5.0% in Nov'24. Despite the moderation, both mining and electricity sector registered strong growth. Manufacturing sector had subdued performance, with over 15 sub-sectors registering weaker growth than last year. Within use-based classification, capital goods and primary goods registered a strong growth in Dec'24. Despite the moderation, we expect a rebound in the coming months which will be adequately supported by capex push, beginning with the easing cycle by RBI and lower inflation. However, the ongoing global tariff war remains a key risk to these projection amidst the concern around higher imported inflation and thereby, requires careful attention.

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