MONTHLY MACRO-INSIGHTS

DECEMBER 2024

Baroda BNP PARIBAS MUTUAL FUND

Together for more

Global Economy

Fed passes the cut, but still the markets jolted……Why?

- US FOMC reduced the federal fund rate by 25bps to 4.25-4.5%., marking a cumulative rate cut of 100bps in 2024.
- The key takeaway in the policy which swayed the markets globally was the summary of economic projections.
- The projections dictated the tone of the policy as hawkish.
- The dot plot indicating two more rate cuts of ~25 bps each in 2025 versus four rate cuts of ~25bps each in the September economic projections.
- This policy marks a shift towards a change in the forward guidance with the extent and timing of additional adjustments to depend on evolving labor and inflation dynamics.

US FOMC SEP in %		2024	2025	2026	
Change in real GDP	Dec-2024 Projections	2.5	2.1	2.0	↑
	Sep-2024 Projections	2.0	2.0	2.0	
Unemployment rate	Dec-2024 Projections	4.2	4.3	4.3	↓
	Sep-2024 Projections	4.4	4.4	4.3	
PCE Inflation	Dec-2024 Projections	2.4	2.5	2.1	↑
	Sep-2024 Projections	2.3	2.1	2.0	
Federal funds rate	Dec-2024 Projections	4.4	3.9	3.4	↑
	Sep-2024 Projections	4.4	3.4	2.9	

US benchmark rates %

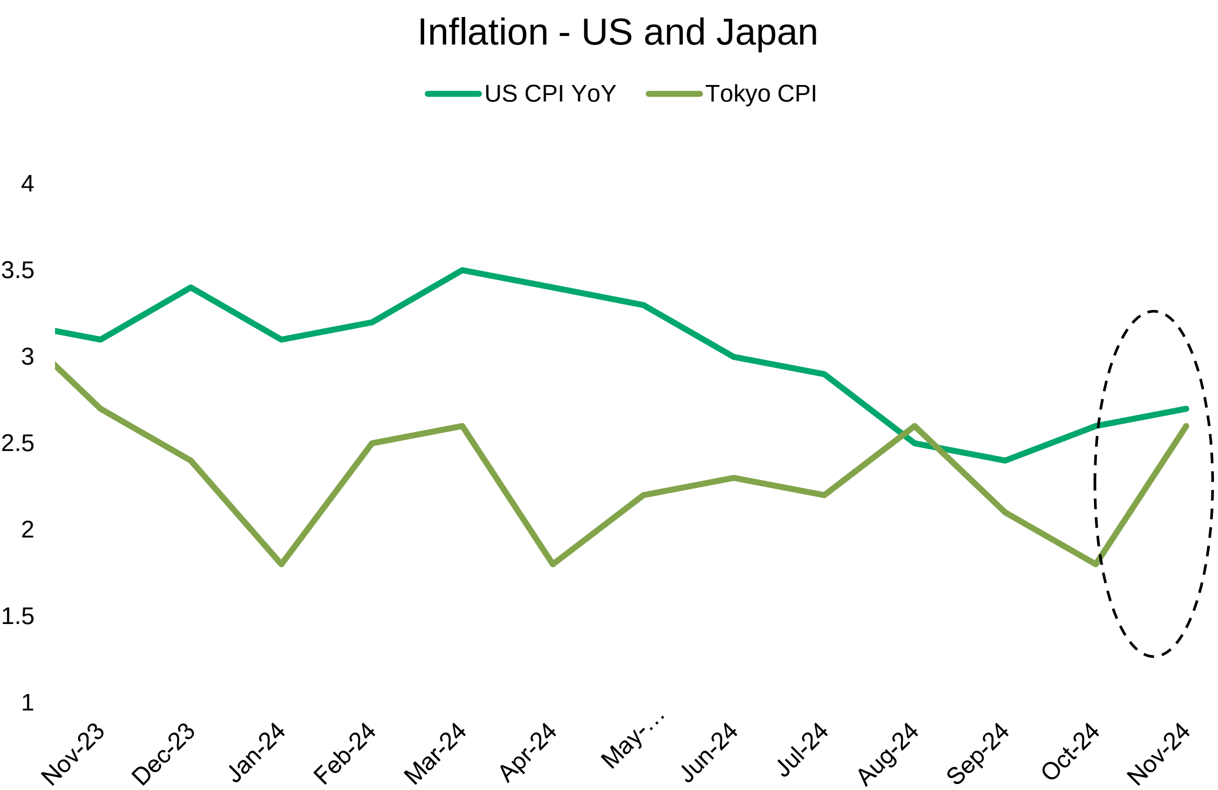
Market Reaction

- Dollar index (DXY)- Levels increased from 106 to 108 levels.
- US treasury yields rose above 4.5%, reaching its highest level in seven months.
- Global currency markets have also reacted with yen and yuan witnessing pressures..

Source: Bloomberg, Data as on 20.12.2024
FOMC- Federal open market committee

Recent pickup in US CPI, Persistent inflation in Japan….Implications on their monetary policies ?

- In major countries like US, Japan, inflation continues to remain sticky and driven by indigenous factors.
- Recent pickup in inflation in US and Japan is expected to drive the monetary policy expectations.

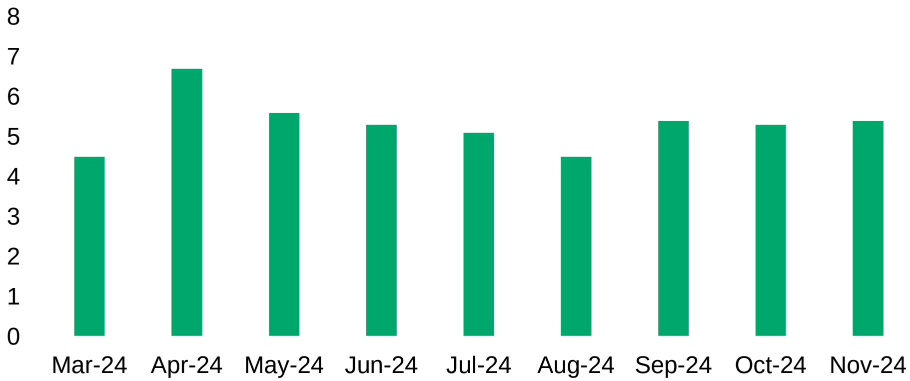


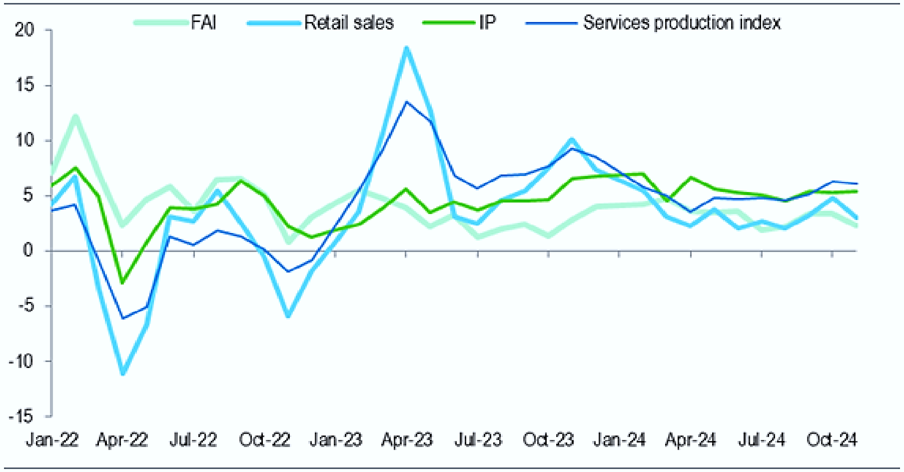
- In Nov-24, US inflation came at 2.7% higher than market expectations.
- The surprise was driven by core inflation.
- Japan’s core inflation has exhibited pressures from expanding economy and wage growth.
- The key question is the underlying spillovers on monetary policy of both countries.

Source: Bloomberg, Data as on 20.12.2024
CPI – Consumer Price Index

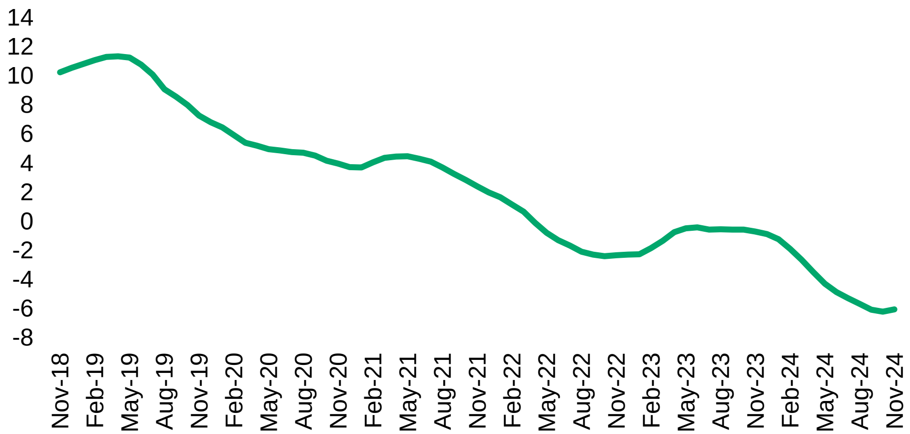
China The Wobbly Economy, Fiscal Package and Spillovers!

Industrial Production YoY





China 70 cities commerical home prices



- October and November data suggests that economic growth momentum saw signs of uptick in few of China's economic indicators.
- Recent increase in the fiscal deficit from 3% to 4% of GDP is expected to boost the recovery.
- The additional 1% of GDP is expected to have a fiscal cost of ~$179bn.
- This move is expected to keep pressure on Chinese yuan and other emerging market economies.

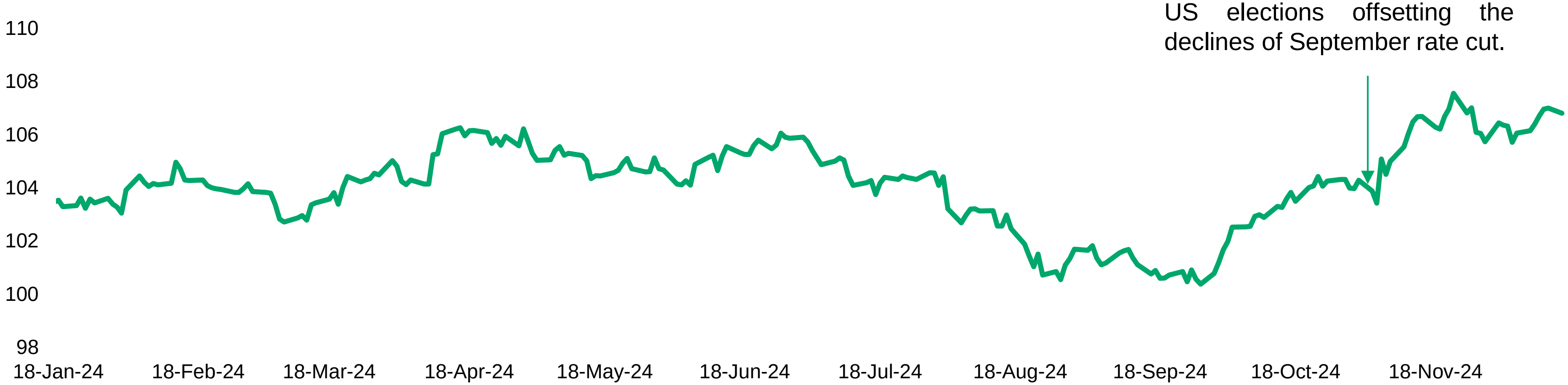
Source: Bloomberg, Lates data as end of Nov-2024

YoY- year on year
FAI- Fixed Asset Investment
GDP – Gross Domestic Product

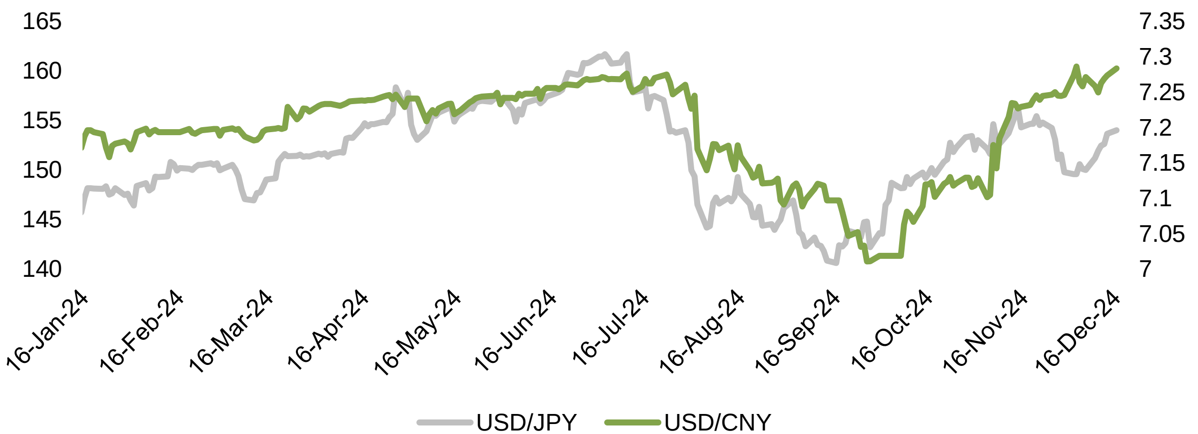
US economic strength, China's fiscal stimulus and Japan's inflation problem…

DXY Index

Dollar index strengthened post US elections offsetting the declines of September rate cut.



China and Japan's Currency movement



- Resilience of the US economy has been fueling the dollar index strength.
- This has been keeping the emerging market economies and other major Asian currencies under pressure.
- Looking at Japan and China both the economies are witnessing pressure on their currencies.

Source: Bloomberg, Data as on 20.12.2024

The uncertainty of Trump policy, FED's forward guidance and depreciating EM currencies?

	Thailand	India	Indonesia	China	Brazil	Japan	UK	Eurozone
Period	USD/THB	USD/INR	USD/IDR	USD/CNY	USD/BRL	USD/JPY	GBP/USD	EUR/USD
1 month	-2.23%	0.55%	0.81%	0.75%	4.29%	-0.19%	0.32%	-0.37%
3 month	2.41%	1.17%	3.90%	2.62%	9.69%	9.52%	-4.21%	-5.68%
CYTD	-0.93%	1.97%	3.92%	2.58%	24.58%	9.31%	-0.53%	-4.93%
1 year	-2.34%	2.25%	3.29%	2.27%	22.29%	8.34%	-0.17%	-3.62%

- Stands for appreciation
+Stand for depreciation

- A Trump presidential victory lent more strength to the DXY, increasing on expectations of high growth-high inflation and hence high-interest rate scenario for the US.
- Higher interest rates in the US has triggered risk of persistent flight of capital away from the emerging market economies.

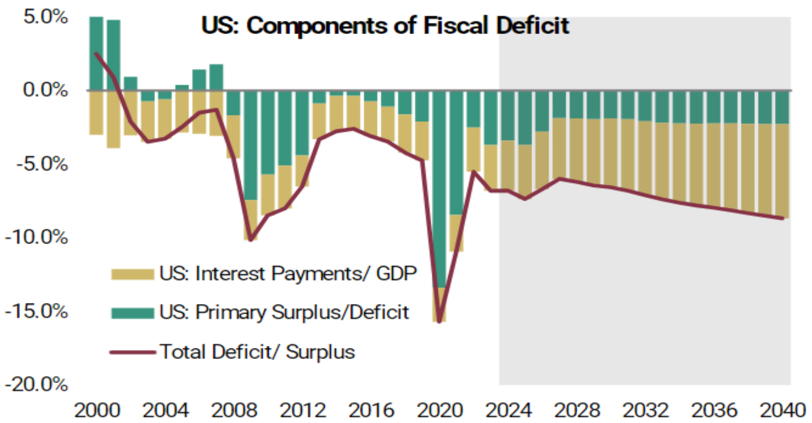
Source: Bloomberg, Internal Research data as on 16.12.2024

Trump wins the 2024 Presidential elections, the fear of unleashing of disrupting trade and fiscal policies……

Policy Action		Economic Impact					
		Headline PCE prices	Real Consumer Spending	Real Investment	Real Exports	Real Imports	Real GDP
Trump Trade Proposal	60% incremental tariff on Chinese imports and blanket 10% tariff on all other imports to the US	0.9%	-3.0%	-3.1%	-1.7%	-9.4%	-1.4%

- Above estimates reflect a faster response in prices and a drag in US real economic activity.
- Under such circumstance it becomes tricky for FED to continue with an interest rate cutting cycle.
- If implemented the fear of rising rates and additional fiscal burden through interest components adds to a dual problem for US.

- US interest costs are steadily rising as the cost of debt reprices to the current yield curve.
- Over time, the ratio of interest expense on the debt to GDP will continue to rise
- Therefore, the fiscal consolidation needed to stabilize the debt-to-GDP ratio increases, as well.
- Markets need to assess the credibility of fiscal policy, and the implied scrutiny is expected to increase the interest burden.



Source: Morgan Stanley Research, Data as on Nov-24

Key Global Triggers

US FOMC 2024 meetings

- FED's forward guidance in the Dec-2024 policy has been fueling volatility.
- The uncertainty regarding Trump's trade and fiscal policies is expected to keep even the FED watchful.

China's Growth Outlook

- China's growth outlook remains significant in two aspects. China's consumption power fuels growth outlook of neighboring economies.
- Secondly, slowdown in China has kept a deflationary phase and has contributed to moderating inflation pressures globally.
- Recent fiscal spend projections will keep the EM currencies market under pressure.

OPEC + Production cut

- In current scenario of falling crude prices, OPEC + decision on further production cuts could lead to upside risks to current crude prices.

Source: Internal Research
OPEC- Organization of the Petroleum Exporting Countries

What does it mean for India ?

US Monetary Policy pivot

- US monetary pivot is expected to trigger slowdown in flows to emerging market economies as interest differential narrows.
- Recent outflows from emerging markets (EM's) led by uncertainties US monetary and fiscal policy dynamics directly pressures INR.
- Domestic monetary policy is expected to follow the suite with a lag.

Commodity Prices

- Decline in brent prices remains favorable for India's trade deficit and second line effects on India's inflation.
- Decline in key metals prices is expected to keep the input cost inflation in control.

China and other EM's policy response

- China's deflationary phase and ultra loose monetary has kept the commodities under control. Whereas some pressure on INR remains due to depreciating yuan.
- Japan's monetary policy dynamics will be a significant variable for global flows. This could add some volatility on INR.

Source: Internal Research, Data as on 20.12.2024

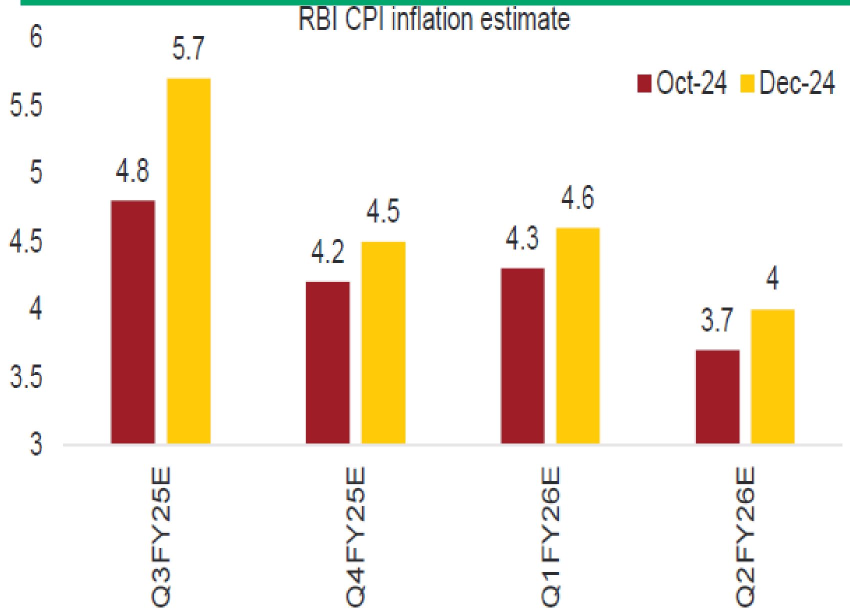
Domestic Economy

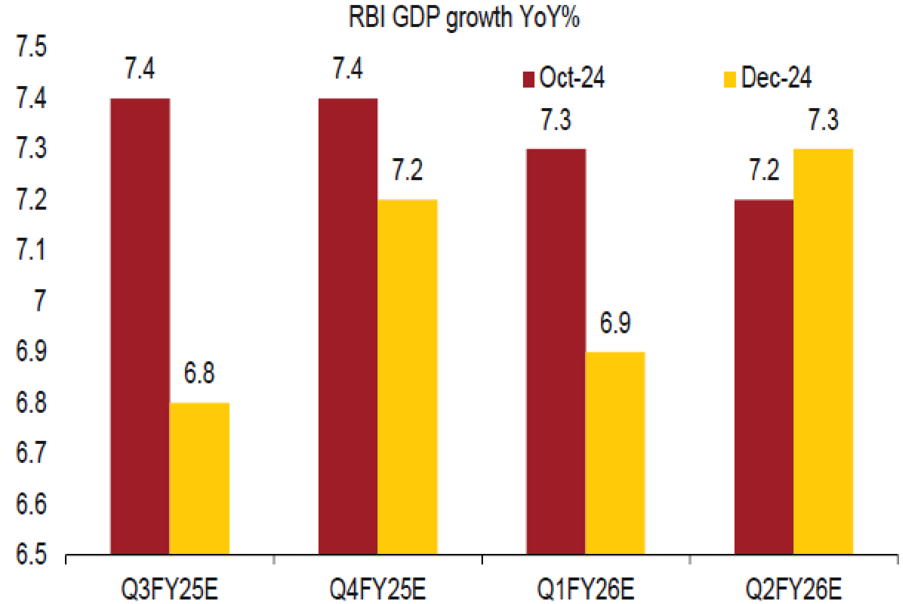
RBI MPC Dec-2024 – A Liquidity focused policy!

Key Decisions taken in December

- Repo rate kept unchanged at 6.5%
- Standing Deposit Facility (SDF) rate unchanged at 6.25% and MSF rate unchanged at 6.75%
- All six members voted to maintain the stance at “neutral” and to remain unambiguously focused on a durable alignment of inflation with the target, while supporting growth.
- **CRR reduced by 50 bps to 4% in two tranches of 25 bps each on December 14 and December 28.**

RBI’s estimates show the balance of risks to have tilted towards domestic indicators and in 2025 domestic indicators will be the key in determining the policy outlook





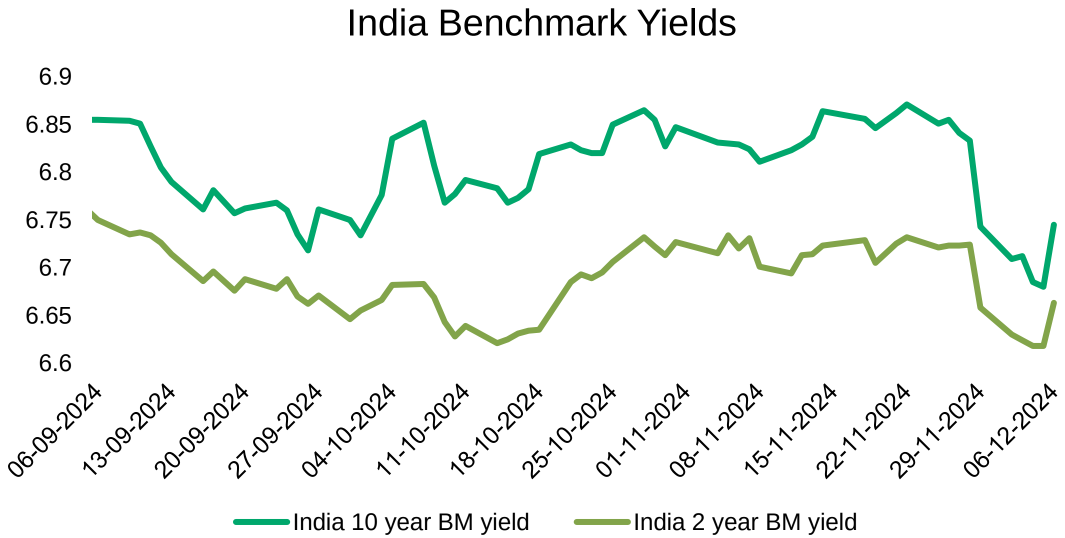
Source: RBI, Bloomberg, Data as on 08.12.2024

CRR cut and Post Policy Market Reactions

CRR cut of 50bps – What is the expected impact ?

- The recent liquidity pressures led by increase in currency in circulation, FPI outflows, advance tax outflows and GST outflows was visible in the end of Nov-2024 deficit liquidity.
- The CRR cut of 0.5% of NDTL will infuse INR1.16tn of liquidity, which will ease some of the pressure on liquidity mentioned above.
- The CRR cut will ease some of the pressure on system liquidity and keep overnight rates close to repo rate.

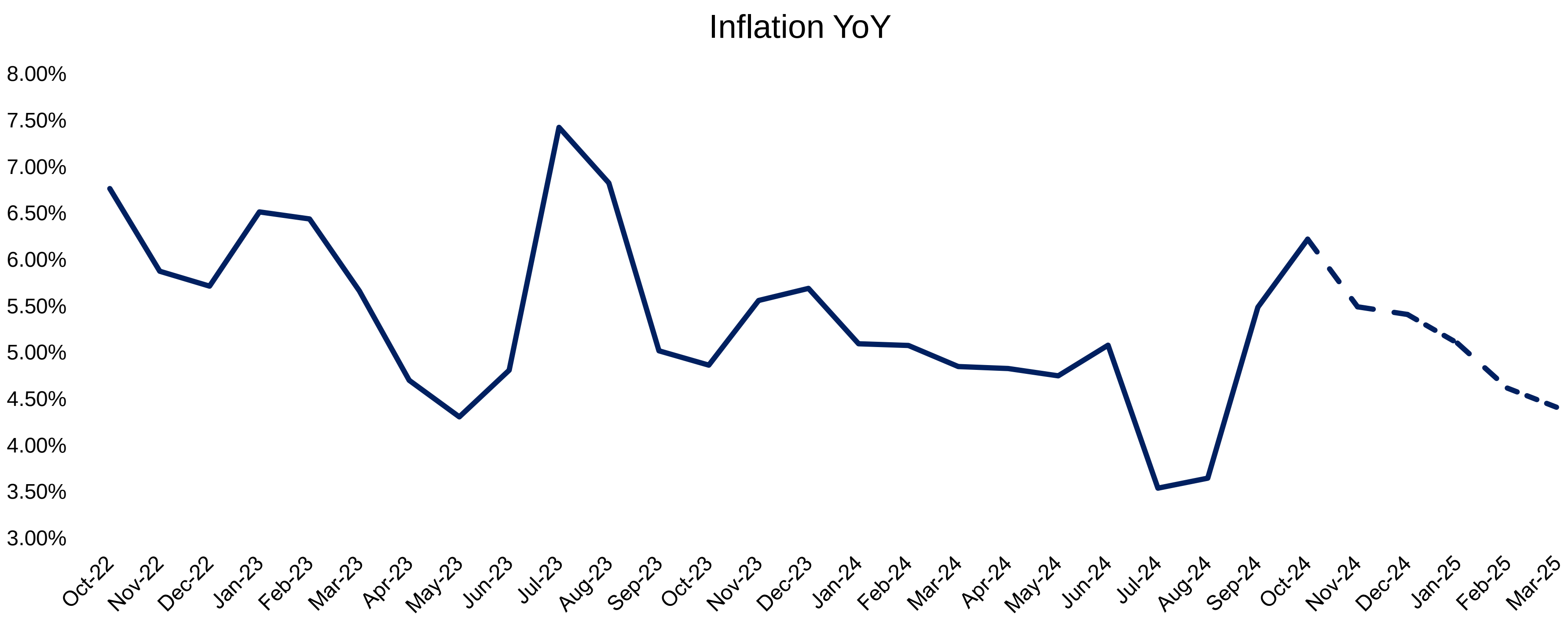
How did the market react ?



- Market reacted negatively with 10 yr benchmark rising by ~5bps immediately post announcement.
- Going ahead, we believe markets will be range bound to approximately 10-15 bps from current levels.

Source: Bloomberg, Data as on 06.12.2024

Domestic Inflation –November brings the respite



- Inflation moderated in Nov-24 at 5.48% from the high of above 6% in Oct-24 as vegetables inflation witness a M-o-M decline of 4.5%.
- A sequential decline of -0.15% M-o-M, after nine months brings a relief.
- Core inflation inched to 3.7% vs 3.5% last month with 0.5% M-o-M.
- We expect inflation to soften further in Q4 FY25 and slowly converse closer to 4.5% in Q4 FY25.

Source: Bloomberg, Data as on 12.12.2024

Domestic Inflation – Top Contributors

Components* of CPI Basket							
Date	All Items	Clothing and Footwear	Food and Beverages	Fuels And Lighting	Housing	Miscellaneous	Pan, Tobacco and Intoxicants
Nov-24	5.48	0.18	3.76	-0.13	0.29	1.21	0.06
Oct-24	6.21	0.18	4.44	-0.11	0.28	1.22	0.06
Sep-24	5.49	0.18	3.83	-0.09	0.27	1.15	0.06
Aug-24	3.65	0.18	2.43	-0.36	0.27	1.10	0.06
Jul-24	3.60	0.17	2.32	-0.38	0.27	1.09	0.07
Jun-24	5.08	0.18	3.83	-0.25	0.27	0.96	0.07
May-24	4.80	0.18	3.61	-0.25	0.26	0.97	0.07
Apr-24	4.83	0.19	3.61	-0.28	0.27	1.00	0.07
Mar-24	4.85	0.19	3.55	-0.23	0.27	0.99	0.07
Feb-24	5.09	0.21	3.56	-0.05	0.29	1.03	0.07
Jan-24	5.10	0.22	3.48	-0.04	0.32	1.08	0.08

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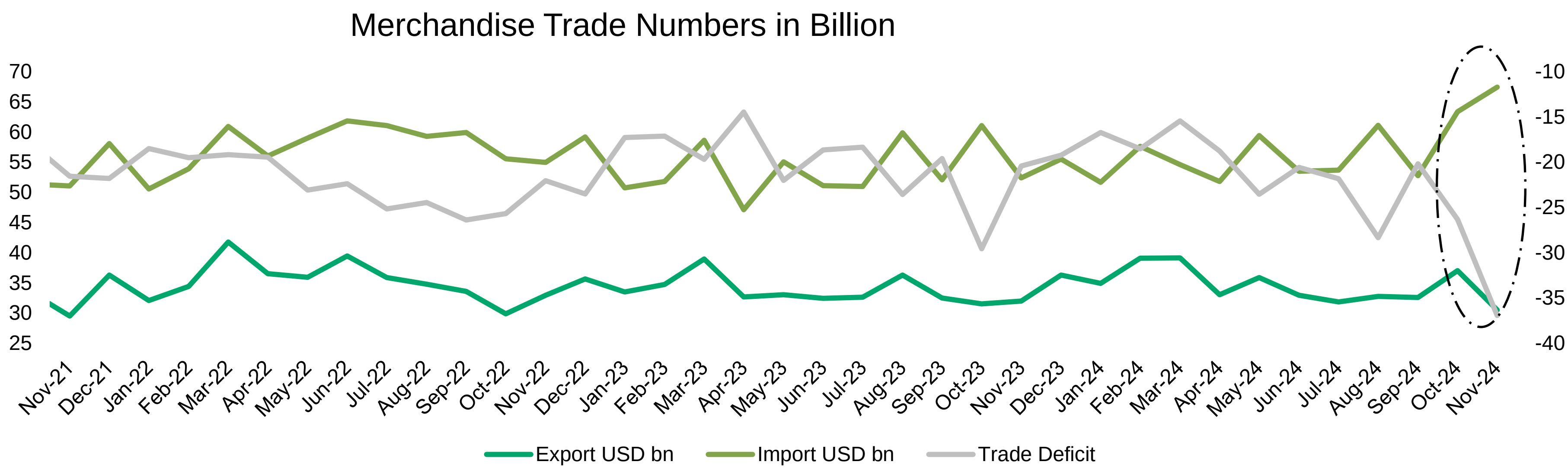
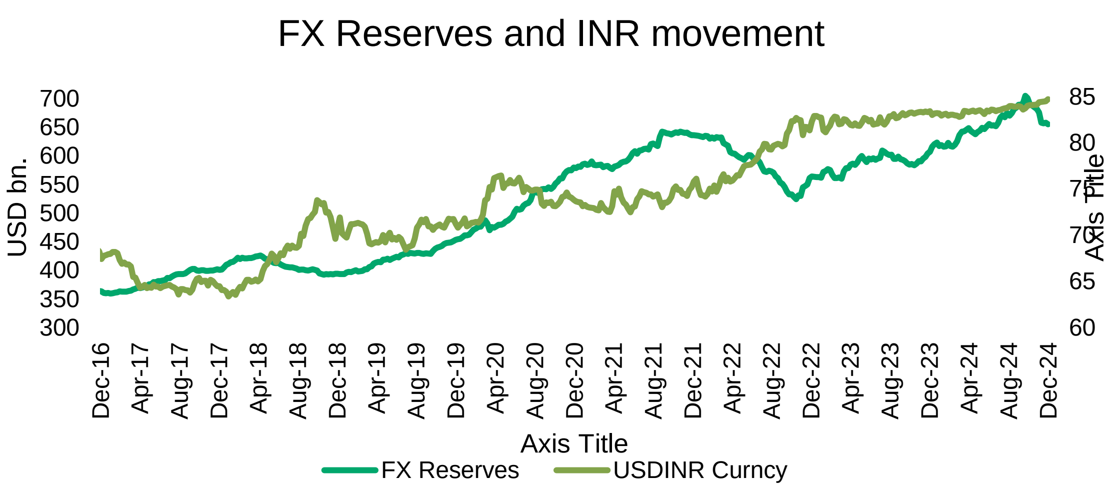
- As of Nov-24, food and beverage basket remained the key contributor to headline inflation.
- Fuel and lighting index remained in the deflationary zone.
- Miscellaneous basket which covers ~70% of core inflation has seen a pick up in inflationary pressures in the last two prints.

Source: Bloomberg, Data as on 12.12.2024

India's Trade Deficit widened further…..What could be the likely impact on Current Account Deficit?

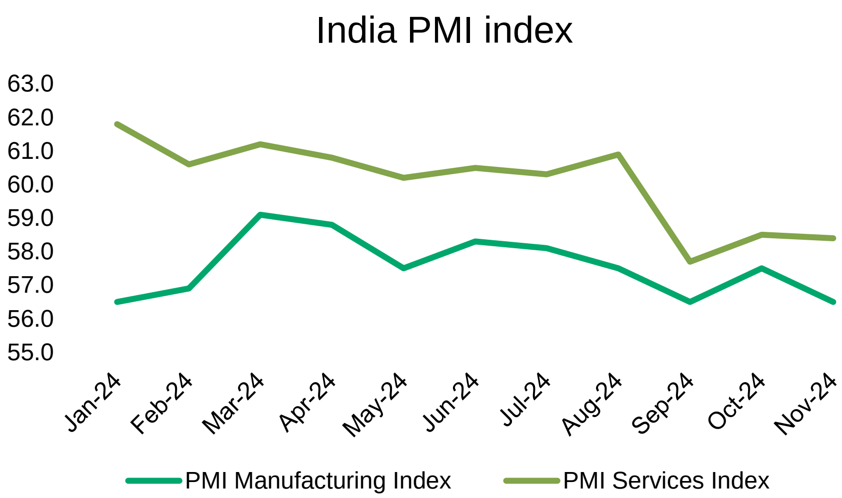


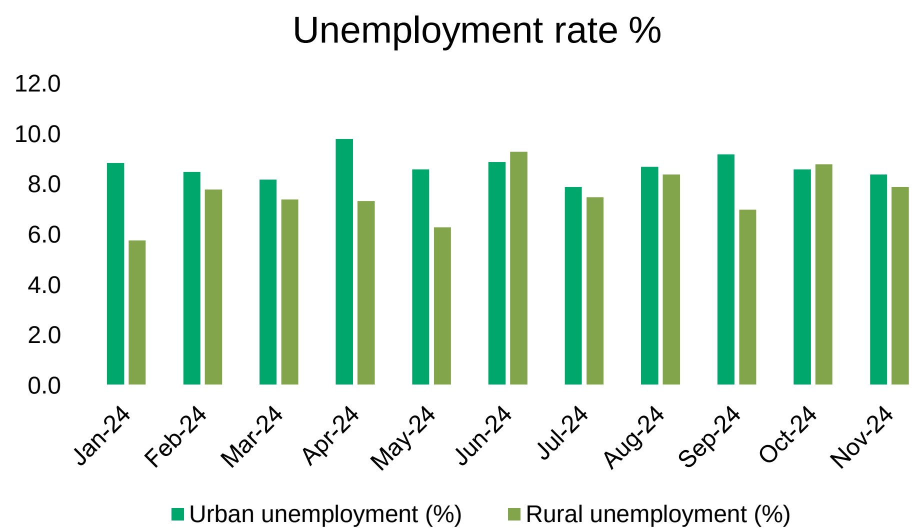


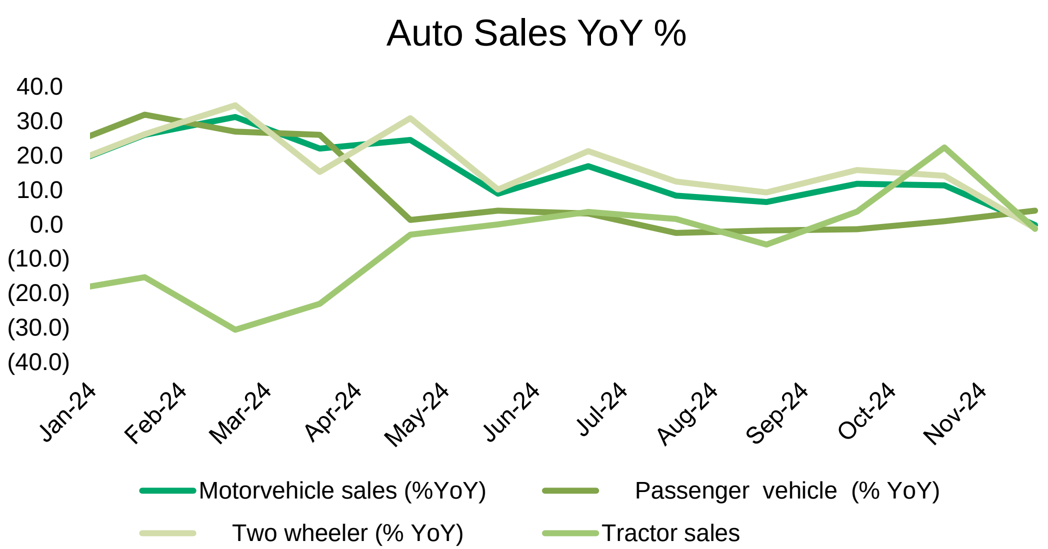
- India's trade deficit recorded a multi year high of USD 36bn in November-2024.
- This comes at a time where INR is already witnessing external headwinds as global monetary policies change winds.
- India's FX buffer are expected to keep the volatility in rupee limited.

Source: Bloomberg, Data as on 20.12.2024

India's growth concerns behind us?



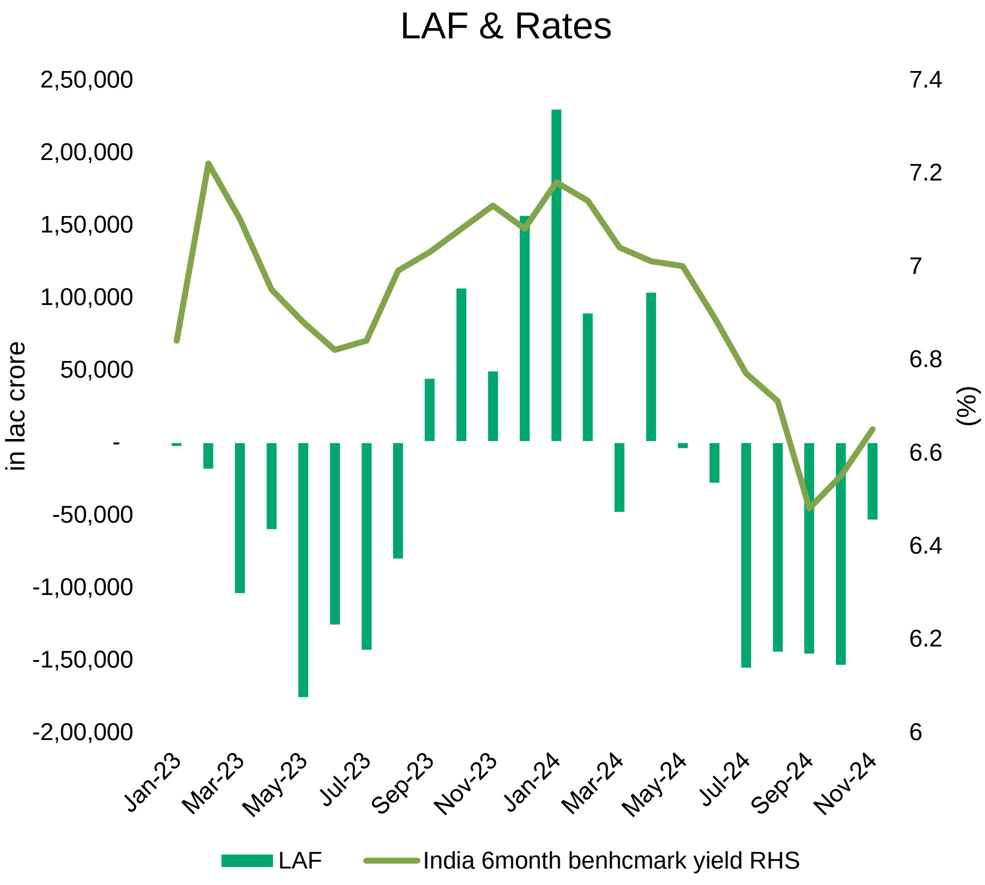




- India's growth indicators saw a pickup during the festive season.
- PMI indexes saw slower pace of expansion but remained in expansionary zone.
- Unemployment rate softened for rural areas with likely pickup in construction activity.

Source: Bloomberg, Data as on end of Nov-2024

Liquidity & Rates



LAF- Liquidity Adjustment Facility

Liquidity and Rates!

- Liquidity conditions tightened last week outflows related to excise and early advance tax payments even as CRR drawdown provided some relief.
- Given the liquidity movement last week, we expect the cash balances to have turned positive to Rs343 bn. For the current week, we expect cash balances to surge sharply to Rs3.4 tn, aided by advance tax and GST collections.
- Going forward, liquidity conditions will be attune to the extent of government spending and RBI's FX operation in an effort to support rupee.

WMA – Ways of means and advances
CRR- Cash Reserve Ratio
Source: Bloomberg, Data as on 30.11.2024

Decoding Yield Signals

Economic Variable	Our View	Impact on yields
Growth	Dent in the growth trajectory in Q2 FY25 economy remains a fragile spot in India's overall robust growth outlook.	↓
Inflation	Inflation trajectory looks optimistic with a few bumps, we expect inflation to average at 4.8% y/y in FY25.	↔
Domestic Liquidity	Liquidity conditions improved post election led by ongoing government spending. Recent pressure on INR has been negative for liquidty which is expected to be managed by RBI operations.	↔
Fiscal Health	Lower than expected government borrowing is positive for the bond markets.	↓
RBI Monetary Policy	RBI is expected to maintain pause tracking domestic inflation. Till then RBI is expected to be In a wait and watch mode.	↔
Global Commodities	Concerns on global economic outlook is visible in declining brent prices and softer commodity prices.	↔
Global Monetary Policy Stance	Global Monetary pivot has begun, tracking global inflation and growth dynamics.	↓

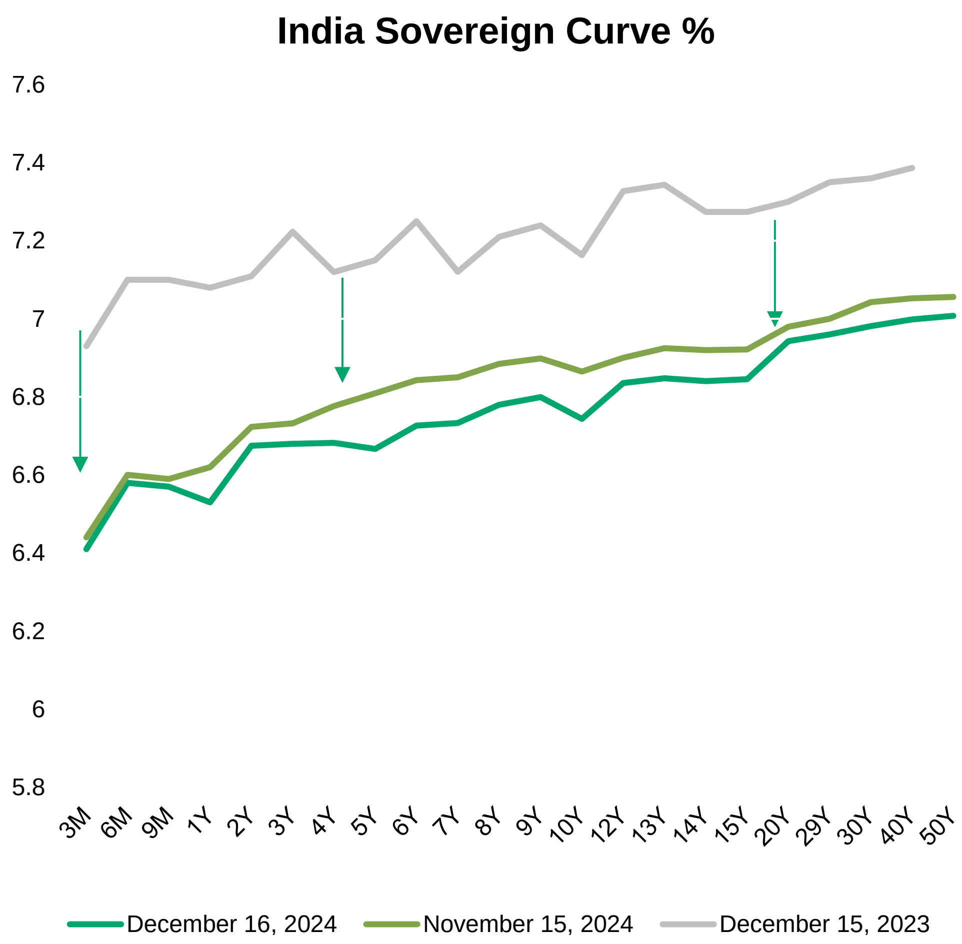
Source – Internal Research, Data as on 20.12.2024

Fixed Income Outlook

Outlook

- Global monetary policy dynamics have started witnessing bumps in their path to recalibrate the monetary rates.
- US FOMC's shift in the forward guidance and the recent pickup in inflation must be carefully monitored.
- Three things to watchout are
- US inflation and monetary dynamics, the movement of dollar index.
- Japan's inflation and currency movement.
- China's economic recovery and fiscal policies.

- On the domestic front, the dent of Q2 FY25 on domestic growth cannot be ignored.
- Inflation has seen significant relief in November-2024, and the forward trajectory also looks optimistic with projected inflation for Q1 FY26 converging to 4%.
- Global headwinds are expected to pressure INR which will have spillovers over domestic liquidity.
- Recent moves by RBI gives us the confidence that liquidity will be managed in spirit of the stance.
- We expect RBI to use different methods of liquidity management to offset any major set back from global headwinds.
- Having said that, the fundamentals of India's fiscal demand supply remain balanced and that is expected to maintain a downside bias on yield.



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Source – Bloomberg, RBI, Data as on 16.12.2024

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