MONTHLY MACRO-INSIGHTS

JANUARY 2025

Baroda BNP PARIBAS MUTUAL FUND

Together for more

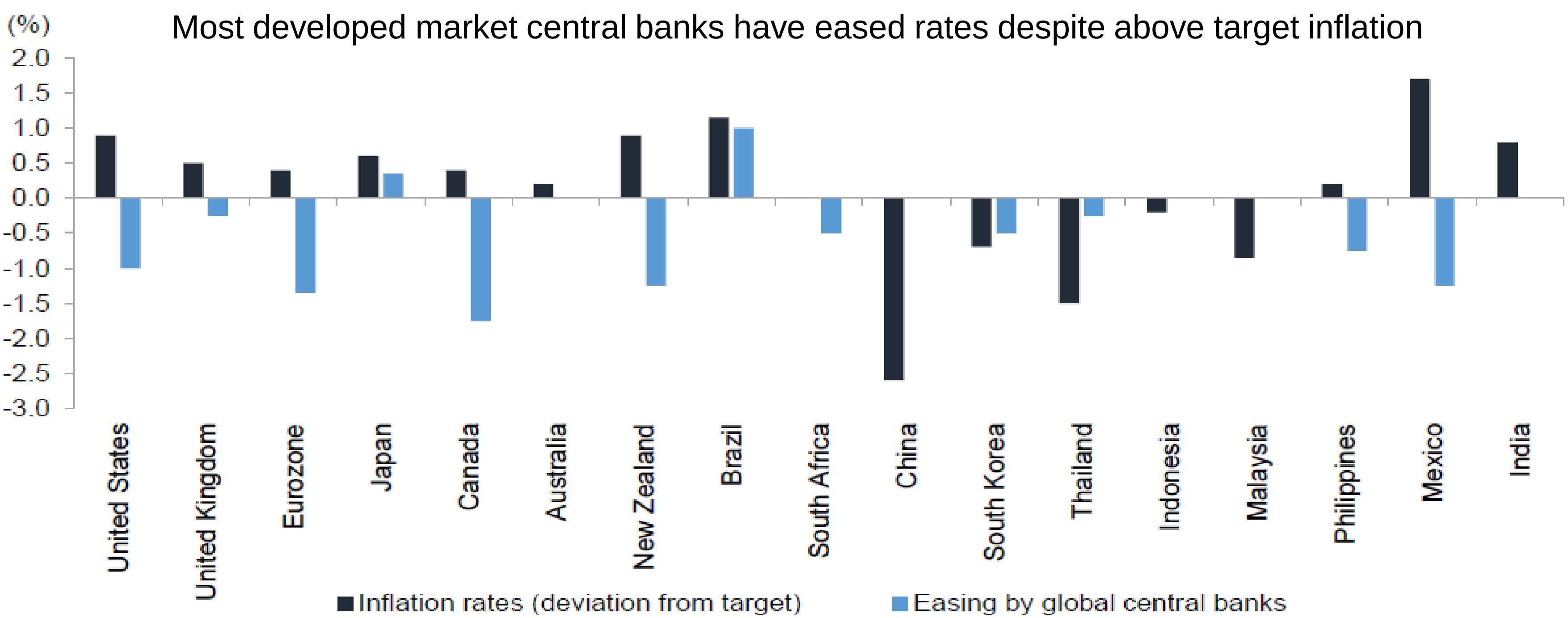
Global Economy

What we cover this month?

- ❑ Yields are rising globally! Why ?
- ❑ Japan – The inflation problem ?
- ❑ China – What is the economy trying to say ?
- ❑ It all boils down to currency!
- ❑ India – Liquidity, Growth and Inflation
- ❑ And of course, The Outlook!

Though central banks have cut interest rates, uncertainty about the future has sent yields sky-high! Why ?

- Global interest rates have started rising, we believe the core reason of rising interest rates is rising inflationary expectations.
- Having said that key global economies like US, UK, Japan etc. have their indigenous reasons driving their rates, currencies, and policies.
- In the below charts we can see the yields have risen, inflation is either sticky for some economies or have started rising for some.

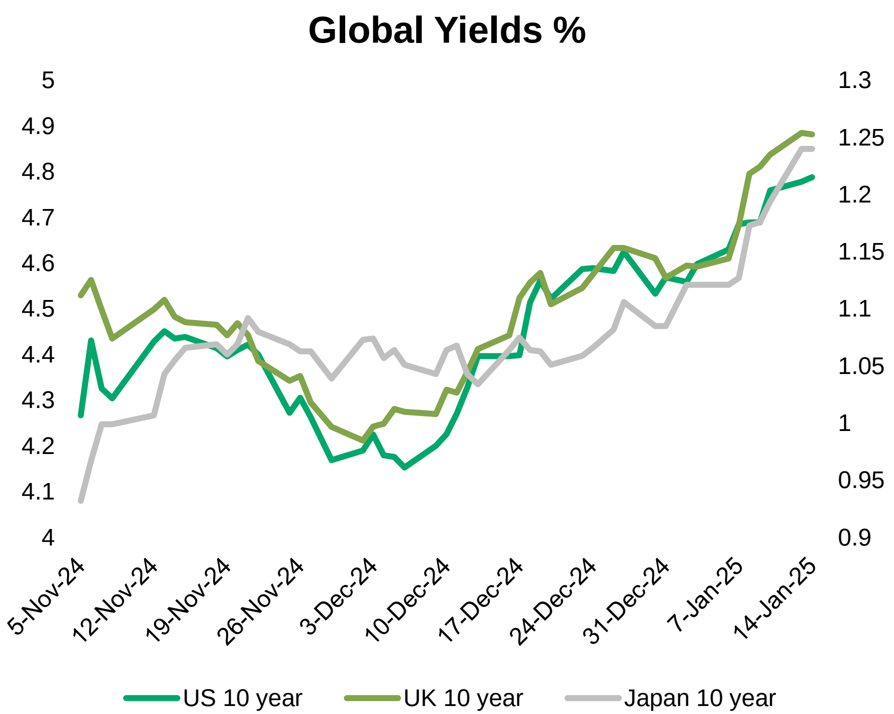


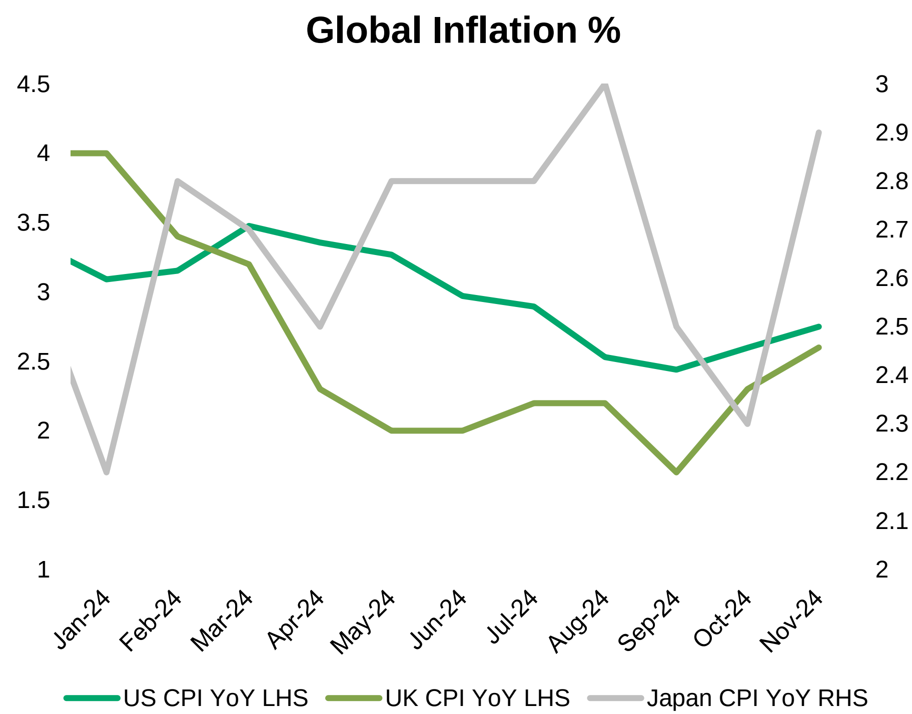
The table reflects rate data for 2024

Source: Nirmal Bang Institutional Equities, Data as on Dec-2024

The yields are rising, inflation is sticky!

US – High debt burdens, strong economy and sticky inflation.
UK- High debt burdens with an economy grappling with growth issues.
Japan – High wage growth, recovery in growth, both have led to inflationary pressures in Japan.





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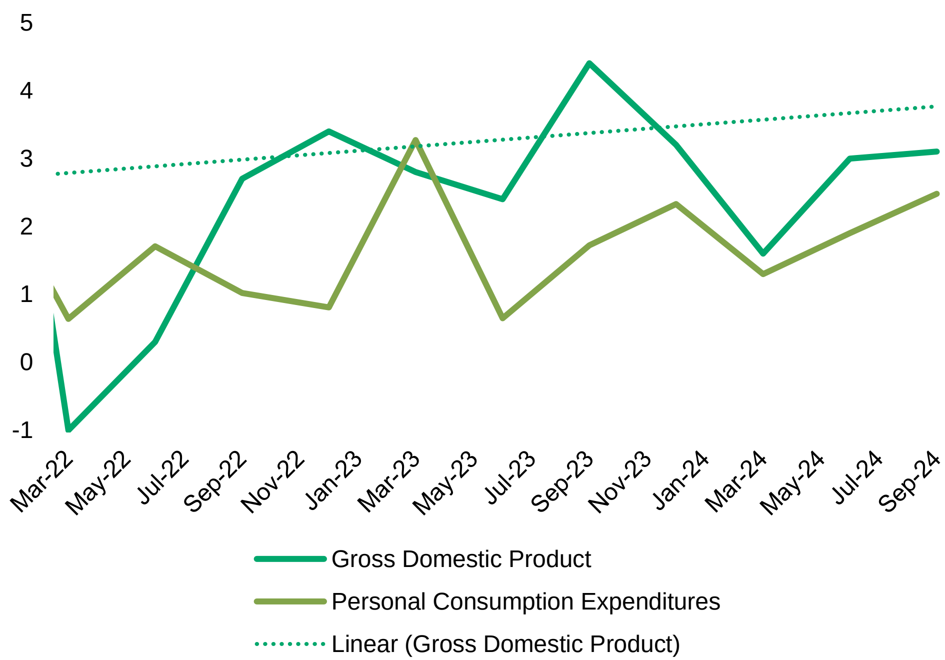
Source: Bloomberg, Latest available data as on 14-01-2025

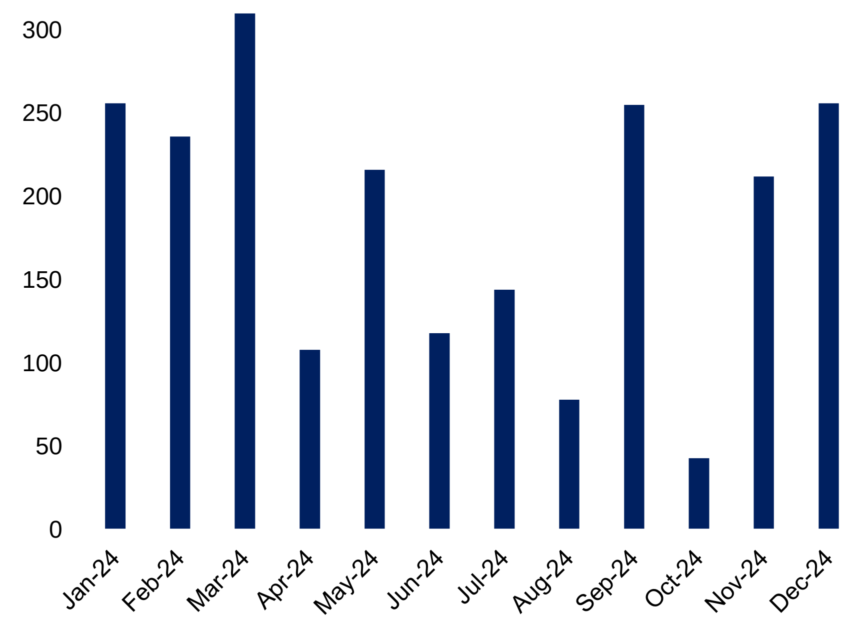
US – The rising duo – UST & USD (US Dollar)

- The spillovers of Trump policy is visible in USD, high borrowing and stronger economy is expected to keep inflationary expectations high which is visible in higher US treasury yield.

USD GDP- Stronger Consumption driving growth



Monthly Non farm payroll additions in thousands



Source: Bloomberg, Latest Available data as on 14-01-2025

Extension of tax cuts will likely help boost consumption and growth, What happens to US fiscal consolidation ?

Provision	Change in GDP	Change in GNP	Change in Capital Stock	Change in Wages	Change in Full-Time Equivalent Employment
Individual Tax Cut & Jobs Act (TCJA) Permanence	0.5%	0.8%	-0.1%	-0.1%	7,95,000
TCJA Estate Tax	Less than +0.05%	0.1%	0.1%	Less than +0.05%	8,000
TCJA Business	0.6%	0.5%	1.0%	0.5%	1,19,000
Restore Full Deduction for State & local tax	0.7%	0.6%	1.3%	0.2%	5,40,000
Exempt Social Security from Income Tax	0.1%	0.1%	0.1%	Less than +0.05%	55,000
Exempt Overtime from Income Tax	0.3%	0.3%	0.4%	Less than +0.05%	4,05,000
Exempt Tips from Income Tax	Less than +0.05%	Less than +0.05%	Less than +0.05%	Less than +0.05%	21,000
Create an Itemized Deduction for Auto Loan Interest	Less than +0.05%	0.1%	Less than +0.05%	Less than +0.05%	50,000
Lower Corporate Rate to 15% for Domestic Production Activities	0.2%	0.2%	0.3%	0.2%	38,000
Eliminate Green Energy Tax Credits	0.0%	0.0%	0.0%	0.0%	-
Impose a Universal 20% Tariff on All Imports Plus Additional 50% Tariff on Imports from China	-1.3%	-1.4%	-1.0%	0.0%	-10,73,000
Partial Foreign Retaliation to US Imposed Tariffs	-0.4%	-0.5%	-0.4%	0.0%	-3,62,000
Impact of Change in the Deficit	0.0%	-0.8%	0.0%	0.0%	-
Total	**0.8%**	**-0.1%**	**1.7%**	**0.8%**	**5,97,000**

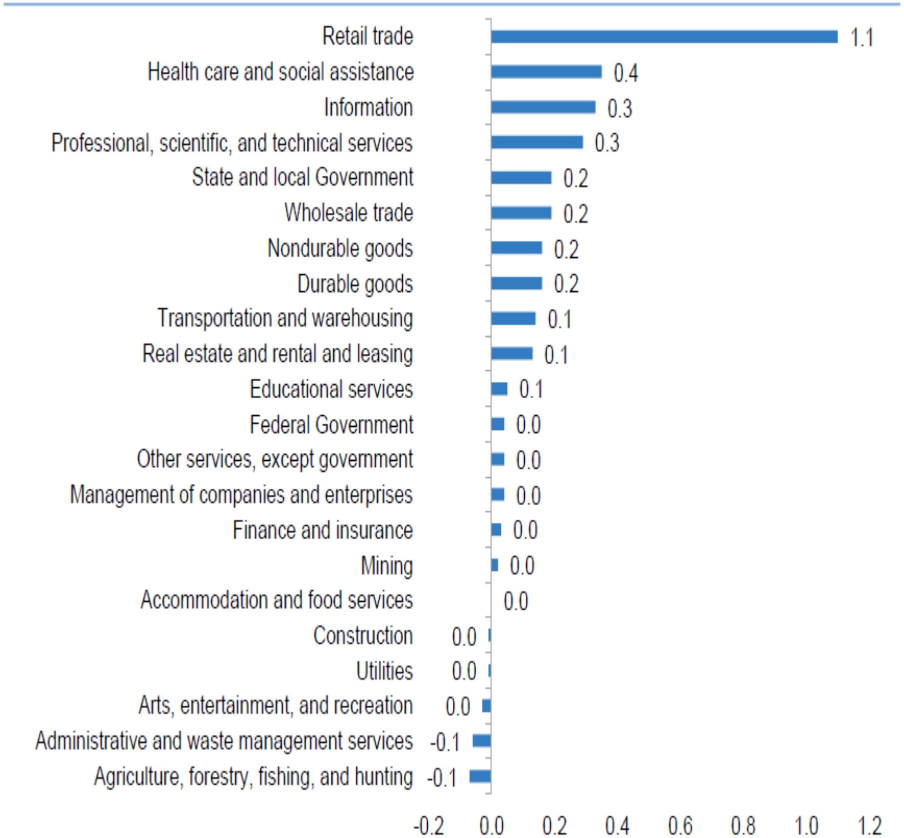
- Apart from supportive liquidity, fiscal policy has been by and large growth supportive in 2024 with no major fiscal consolidation in developed markets.
- Trump’s tax proposals primarily include extension of deductions under the Tax cuts and Jobs Act (TCJA) 2017.
- Extension of exemptions on income tax and proposals such as exempting tips from taxation will likely benefit consumption and provide the tailwinds for growth.

Source- Tax Foundation, Nirmal Bang Institutional, Data as on 14-01-2025

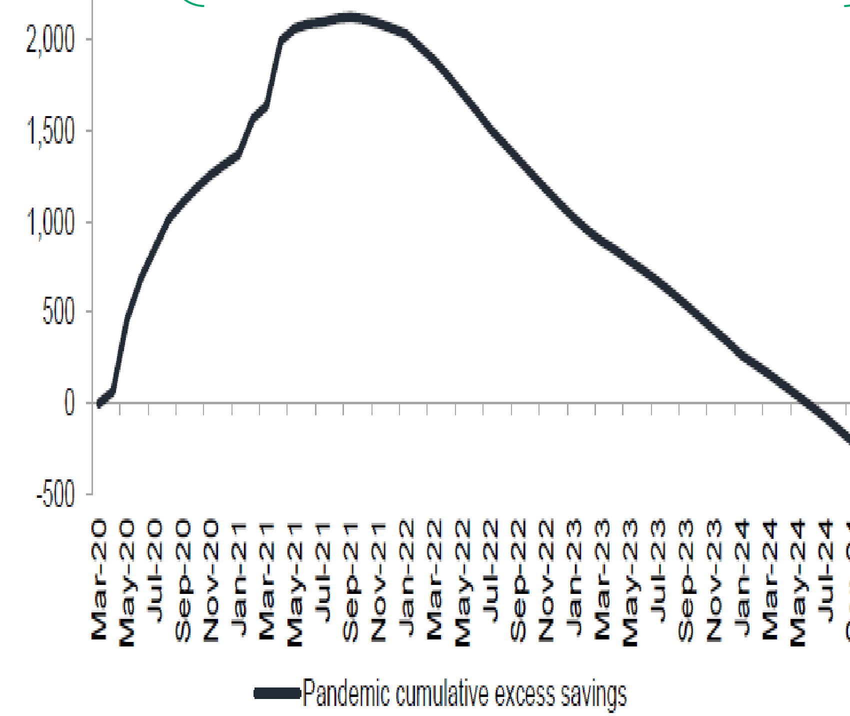
Is strong US Consumption a worry for the World?

- Consumption remained a key driver of US growth even in Q3 2024.
- Extension of exemptions on income tax and proposals such as exempting tips from taxation will likely benefit US consumption which can again have inflationary pressures.

Components of US GDP

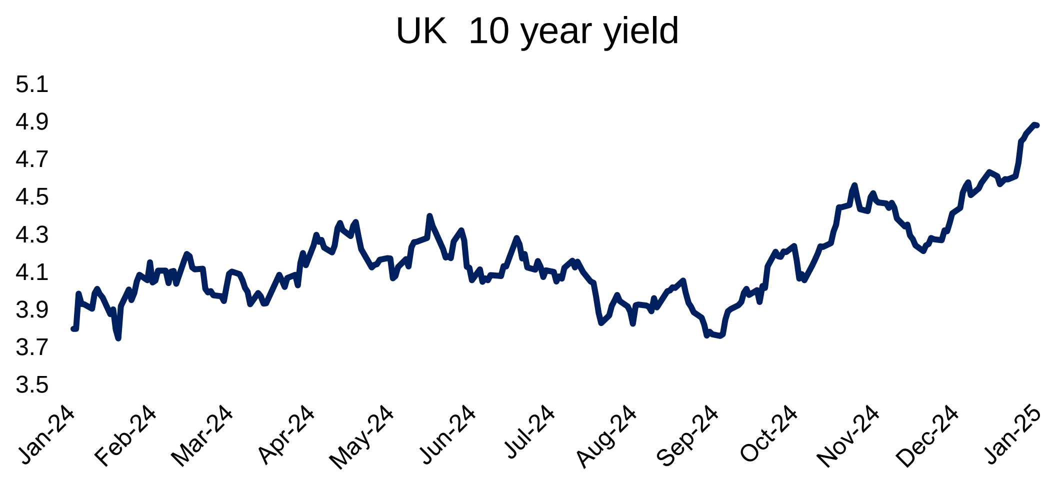


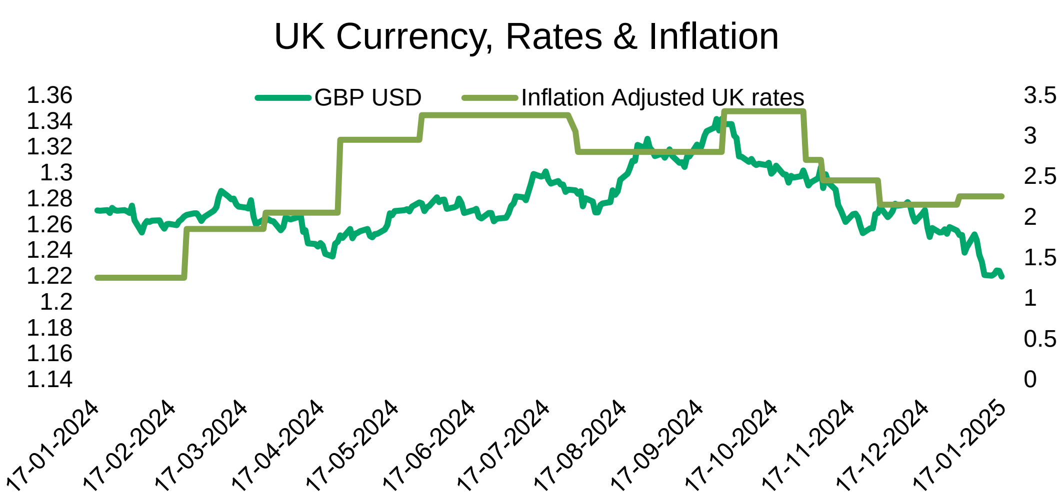
Despite, the drawdown of pandemic era excess savings, US consumption remains resilient.



Source: Bloomberg, Data as on Sep-2024

High Borrowing not only a US problem – UK yields have started to rise led by concerns over borrowing cost!





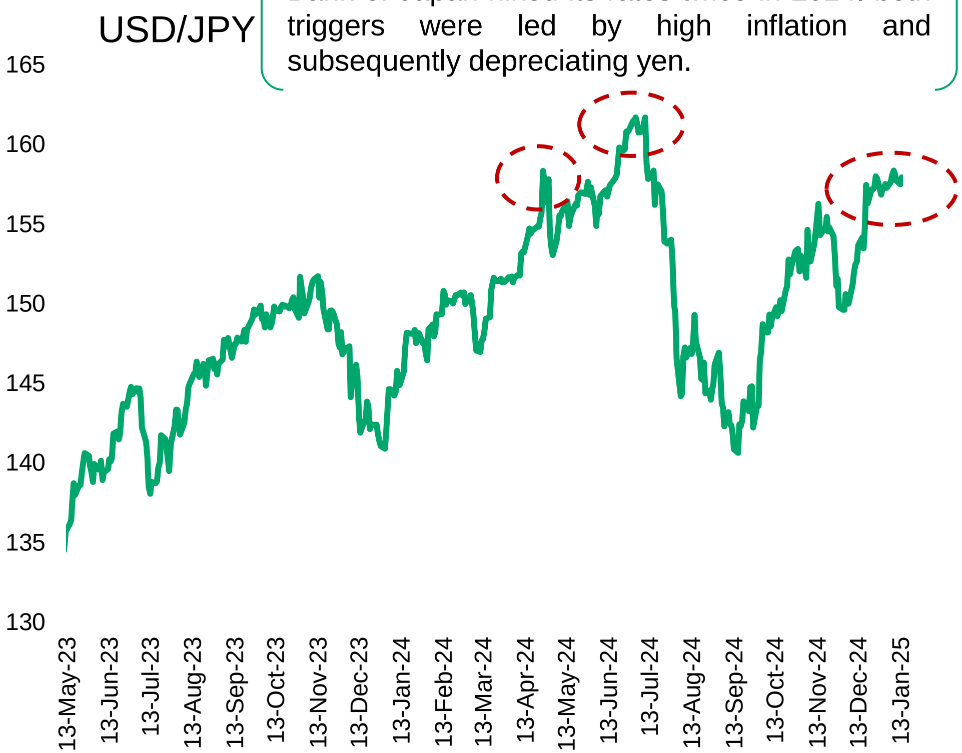
- The Bank of England is likely to pursue a more cautious pace of interest rate cuts owing to elevated inflation and rising uncertainty.
- The yields on the 10 year UK government treasury notes have inched higher.
- Given the concerns on growth and inflation dynamics, pound has seen a sharp depreciation since start of 2025.

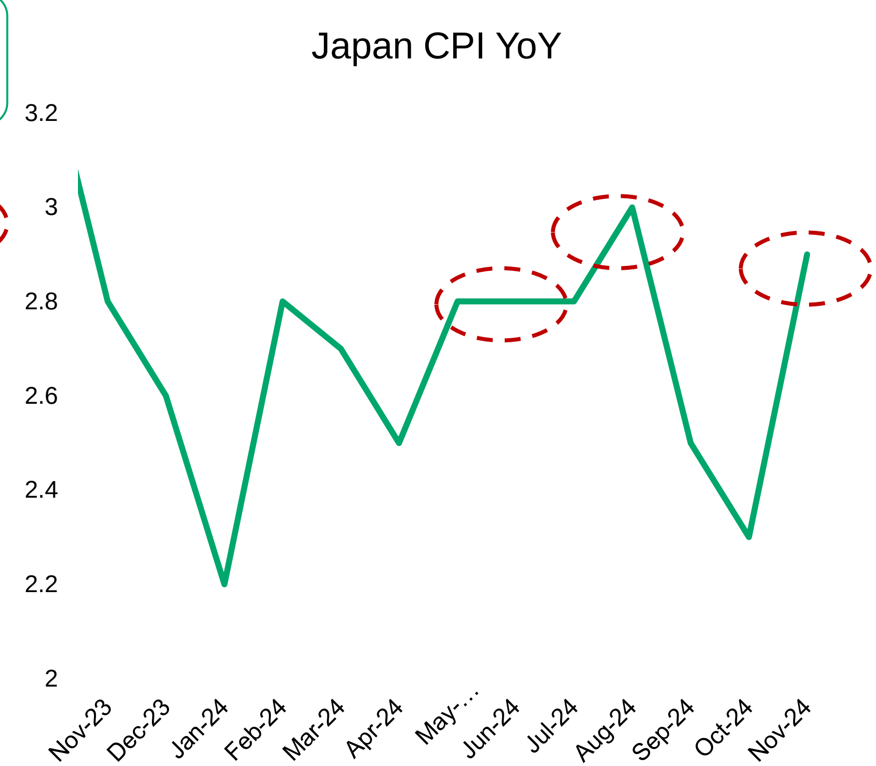
Source: Bloomberg, Latest Available data as on 17-01-2025

Japan – Turning a corner?

- 2024 was a pivotal year for Japan with Bank of Japan (BOJ) adopting a normalized policy stance, Japan moving out of decades of deflation and markets maintaining its strong momentum from 2023.
- We expect another rate hike by Japan in January 2025 policy as inflation is elevated and is at the previous trigger levels.

Bank of Japan hiked its rates twice in 2024. both triggers were led by high inflation and subsequently depreciating yen.

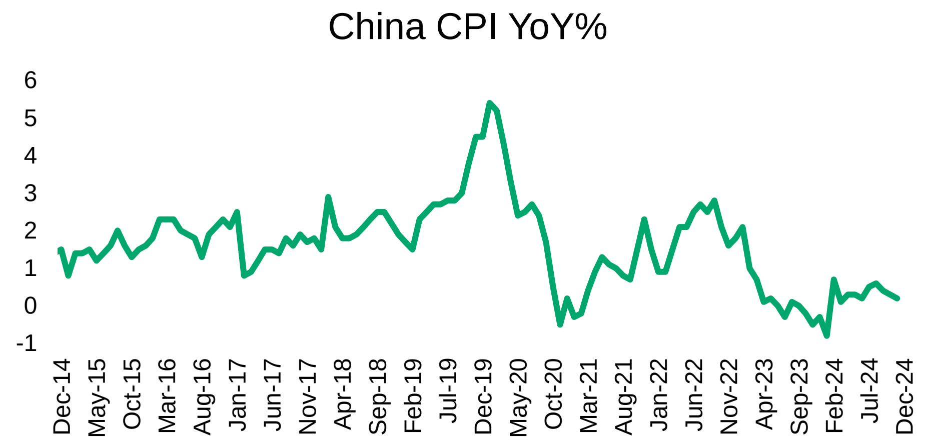


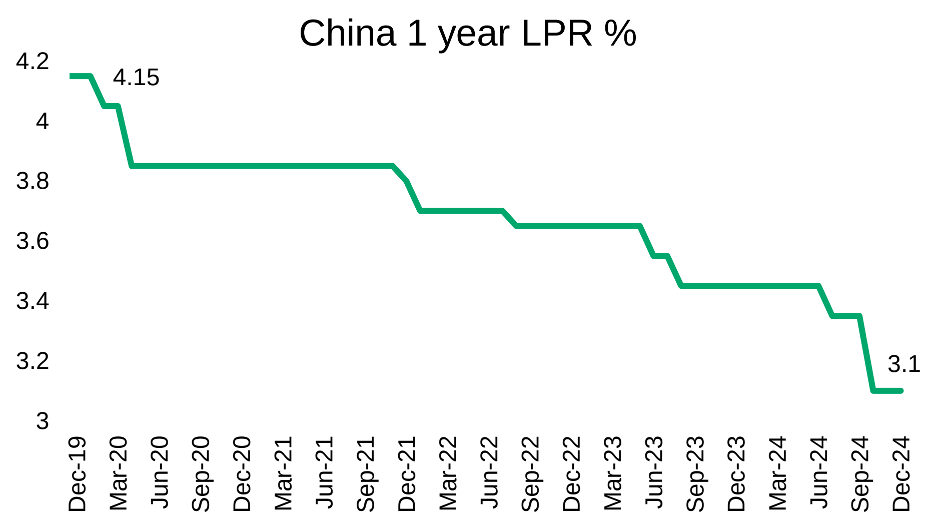


Source: Bloomberg, Latest Available data as on 13.01.2025

US, UK, Japan- the significant three has seen yields rising but China is on a contrarian move! Why ?

- China's economic growth has been erratic.
- The unbalanced growth raises concerns that structural problems may deepen further in 2025.
- Subsequently, loose fiscal and monetary policies have been in place to support growth.
- China's 10 year yield at historical lows is reflection of weak growth environment and inflation a reflection of deflation.





Source: Bloomberg, Latest Available data as on 16-01-2025

Key Global Triggers

Trump Policies and FOMC Projections

- 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

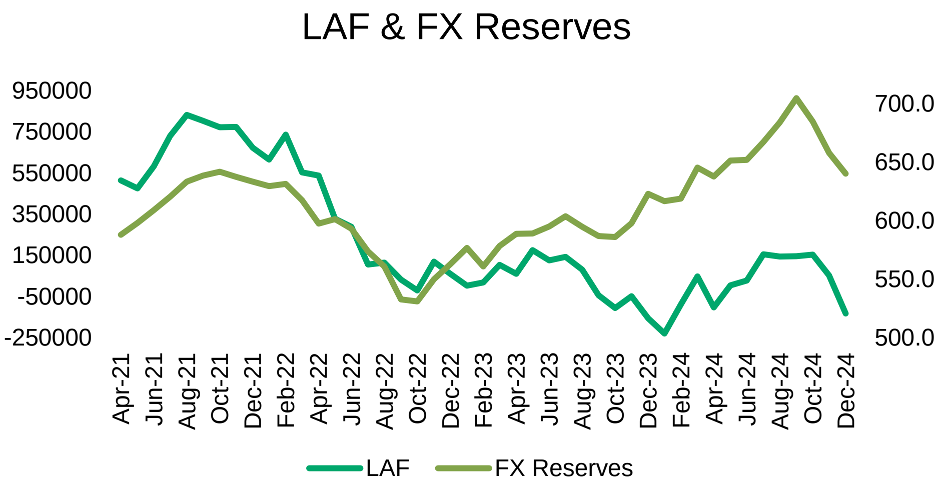
- In current scenario of rising crude prices, OPEC + decision on further production cuts could lead to upside risks to current crude prices.

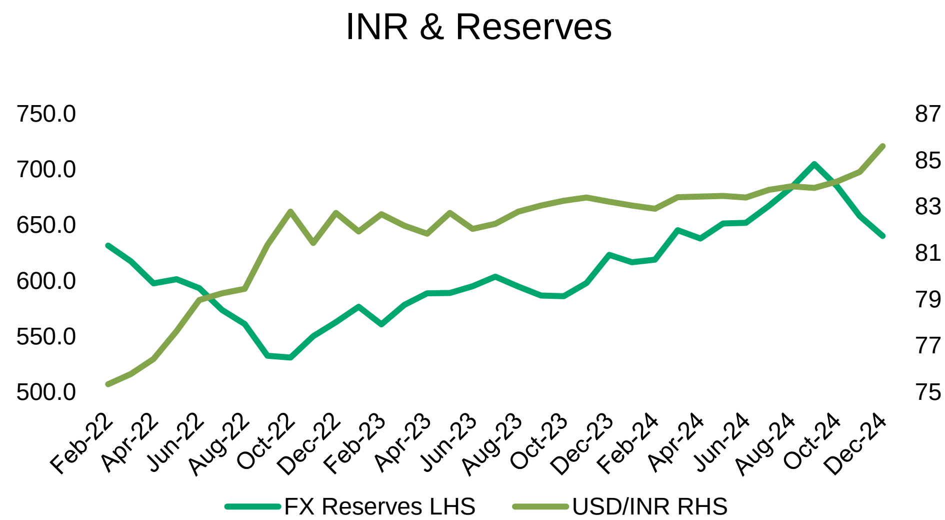
Source: Internal Research

Domestic Economy

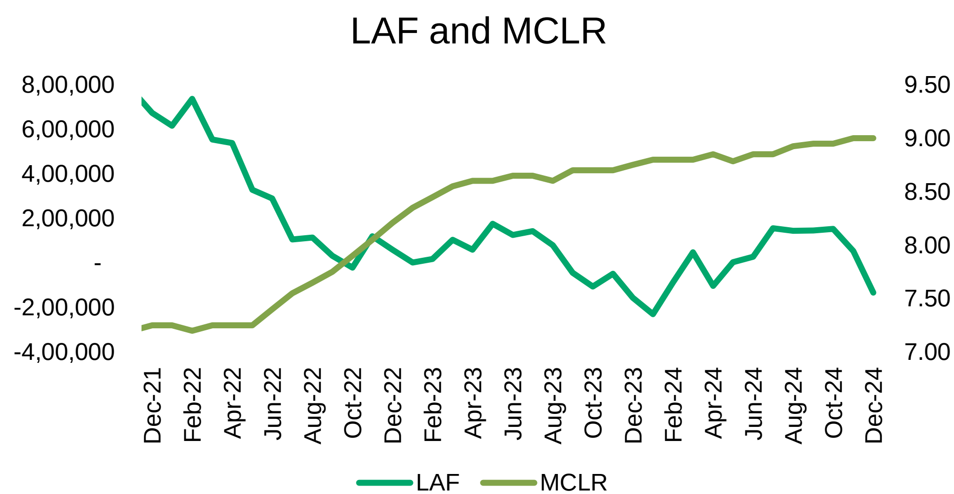
Liquidity, Growth and Inflation

Global Headwinds, INR, Reserves and Liquidity



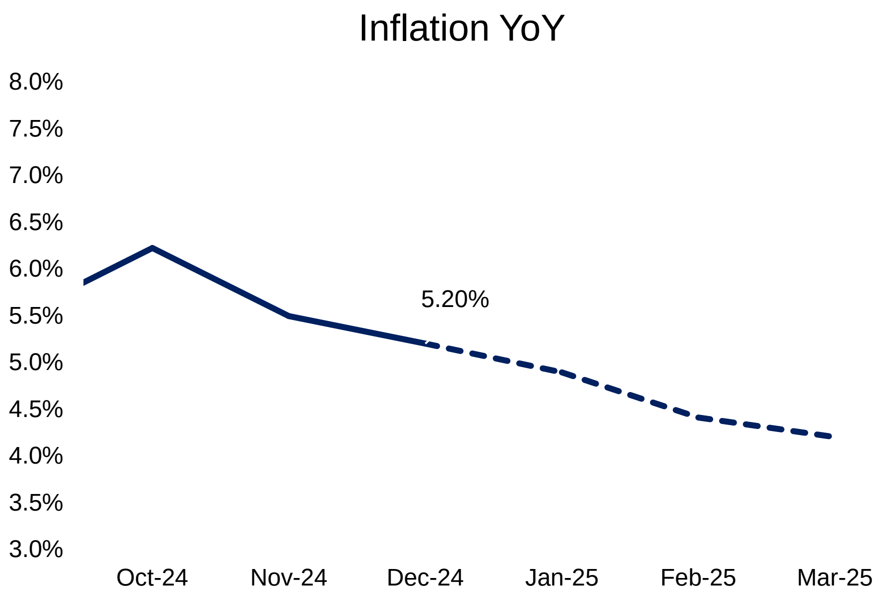


- Liquidity conditions remained in deficit zone.
- Possible FX intervention by RBI to support rupee and limited government expenditure has kept the liquidity under pressure.
- The start of daily VRR auctions is positive but insufficient to address pressure on durable liquidity.
- We expect RBI to be cognizant of the evolving liquidity conditions and expect measures like cash reserve ratio (CRR) cut, Open Market Operation (OMO) purchases and Forex (FX) swaps.



Source: Bloomberg, Latest Available data as on 31-12-2024
LAF- Liquidity Adjustment Facility
MCLR- Marginal Cost of lending rate
VRR- Variable reverse repo

Domestic Inflation –December brings the respite

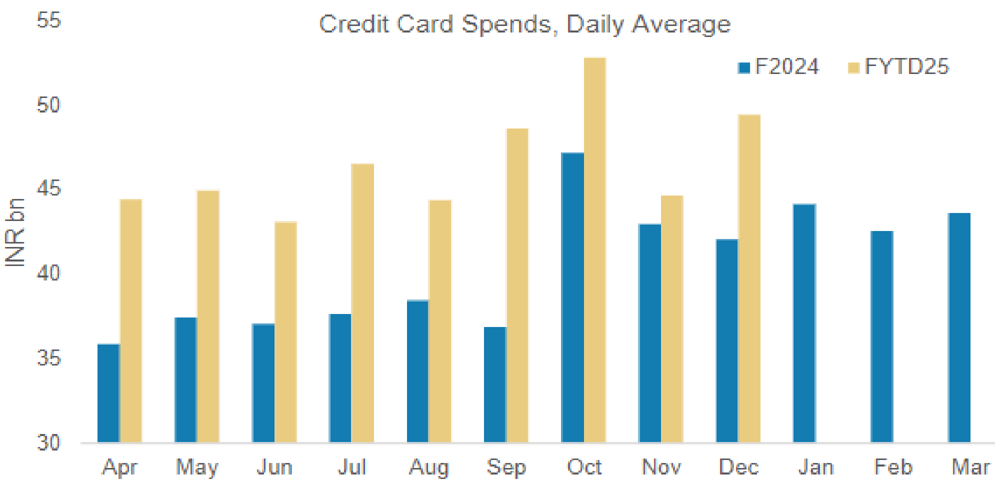


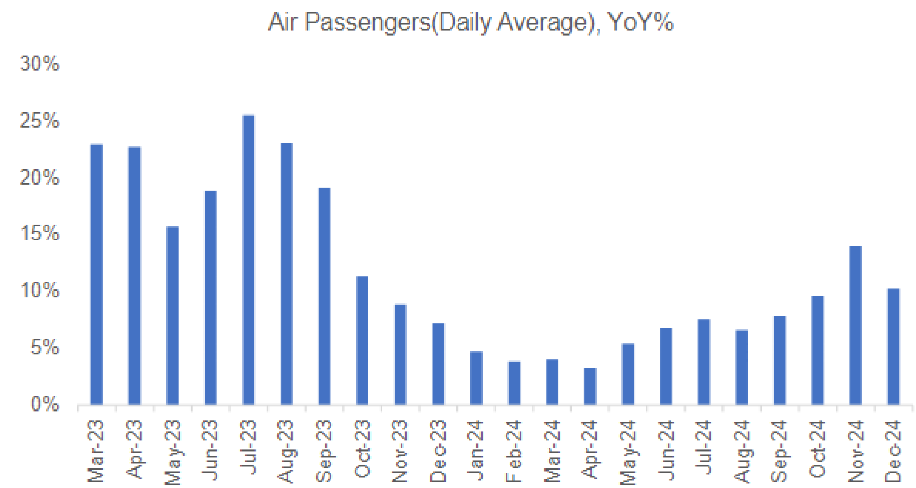
YoY%	Jul-24	Aug-24	Sep-24	Oct-24	Nov-24	Dec-24
CPI inflation	**3.6**	**3.7**	**5.5**	**6.2**	5.5	5.2
Food and Beverages	5.1	5.3	8.4	9.7	8.2	7.7
Pan, Tobacco and Intoxicants	3.0	2.7	2.5	2.5	2.3	2.5
Clothing and Footwear	2.7	2.7	2.7	2.7	2.7	2.7
Housing	2.7	2.7	2.7	2.8	2.9	2.7
Fuel and Light	-5.5	-5.3	-1.3	-1.7	-1.8	-1.4
Miscellaneous	3.8	3.9	4.0	4.3	4.3	4.2
Core	3.4	3.4	3.6	3.7	3.7	3.6

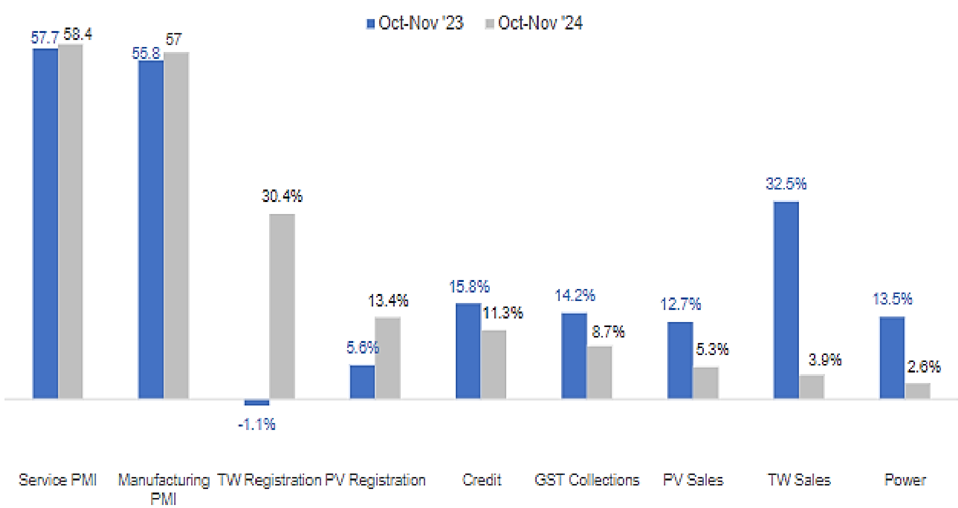
- CPI inflation in December softened to 5.2% slightly below November inflation of 5.5%, supported by a broad-based deceleration in prices.
- The softening was led by winter season disinflation in vegetable prices.
- Core inflation remained benign at 3.65% y/y in Dec-2024 vs 3.7% y/y in Nov-2024.
- Looking at the trajectory of inflation, Q4 FY25 monthly inflation is expected to track lower than 5% led by favorable base and continued decline in food prices led by winter crop arrival.

Source: Bloomberg, Data as on 13.12.2024

India Consumption – A dent only in Q2 FY25?







- India's consumption economy has shown moderation in FY25.
- One of the key read in the charts show that some part of the consumption is fueled by credit.
- Credit card spends in FYTD25 have remained significant, whereas other variables like GST collection, passenger vehicle sales, tractor sales and power generation have seen a relative moderation.
- The dent of Q2 FY25 cannot be ignored. Growth has started showing signs of moderation and some support from RBI has started gaining traction.

Source: Bloomberg, Latest Available data as on 14-01-2025

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	Recent pressure on INR has been negative for liquidity 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 14.01.2025

Source: BBNP Paribas Research

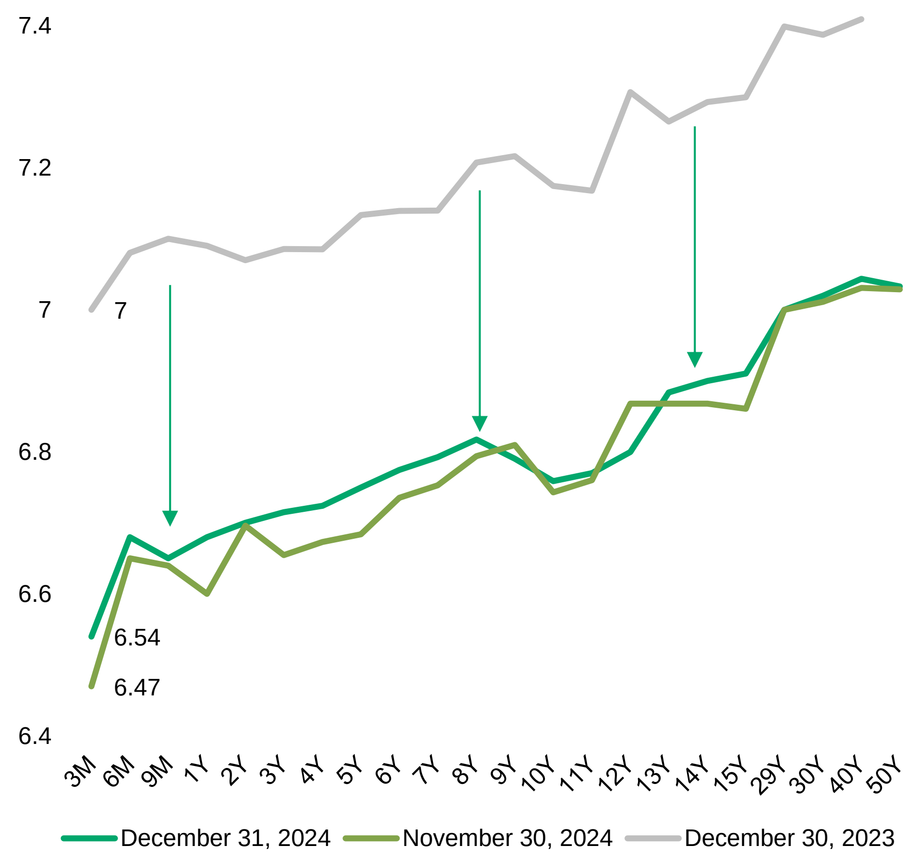
Fixed Income Outlook

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
- 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 Dec-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 on yield.

India Sovereign Yield Curve %



Past performance may or may not be sustained in future and is not a guarantee of any future return. Returns do not take into account the load, if any. Returns are for growth option. Different plans shall have a different expense structure. The performance details provided above for Hybrid Funds are for regular/distributor plan and the performance for Debt Funds are for direct plan.

Source – Bloomberg, RBI, Data as on 31.12.2024

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