MONTHLY MACRO-INSIGHTS

SEPTEMBER 2024

Baroda BNP PARIBAS MUTUAL FUND

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Global Economy

Global Macro and Key Events

Fed Pivot and the quantum of rate cut

Global commodity cycle

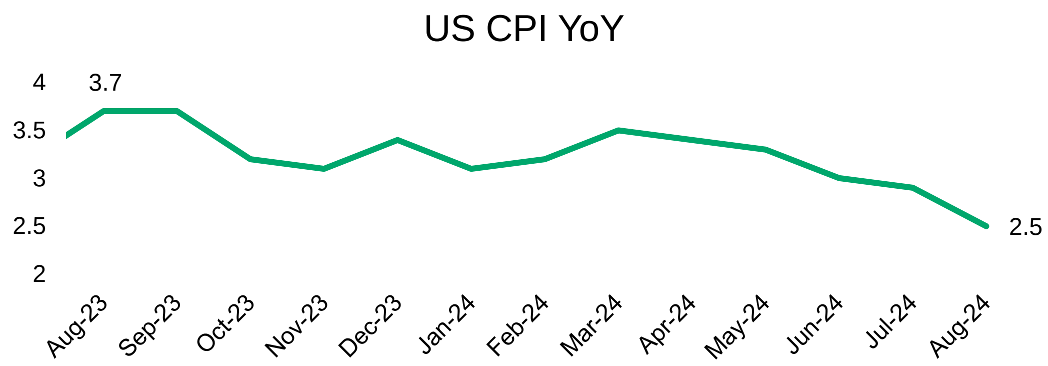
Global Bond Yield Movement

What does it mean for India?

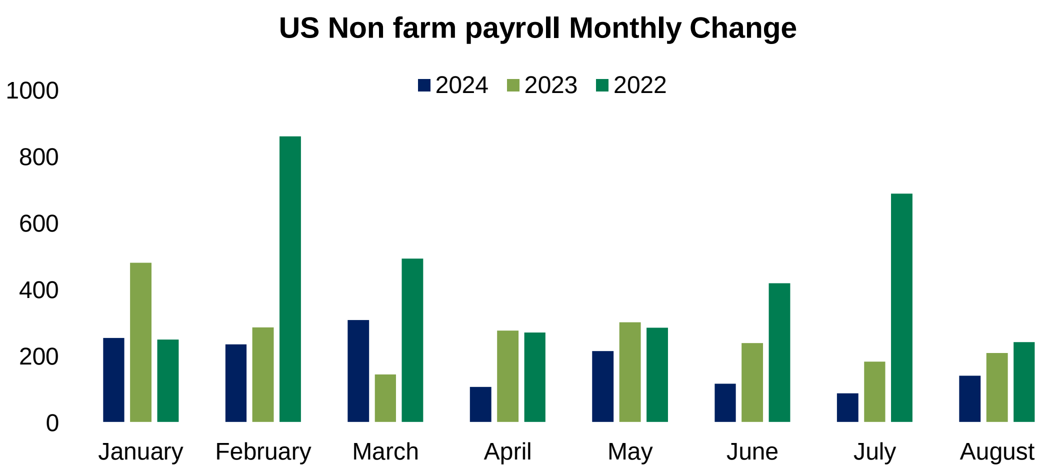
Fed Pivot – Quantum and Timing

- Recent data on US inflation and growth have been supportive of a fed pivot.
- Expectations of pivot lies between 25-50bps.
- Looking at the inflation and labour market data, we expect a 25bps rate cut in the Sep-2024 FED FOMC policy.

US Inflation continued a slow decay, Aug CPI declined to 2.5% y/y



US labour market continues the path to moderation, monthly additions to labour market has been lowest in last 3 years

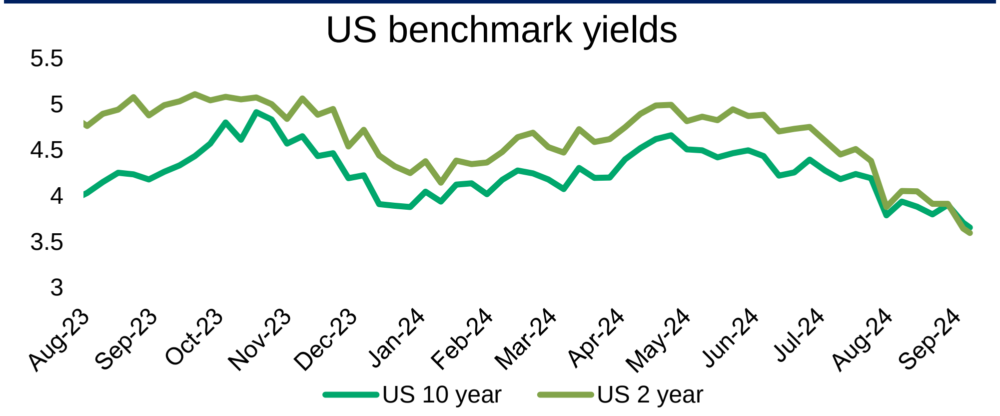


Source: Bloomberg, Data as on 15.09.2024

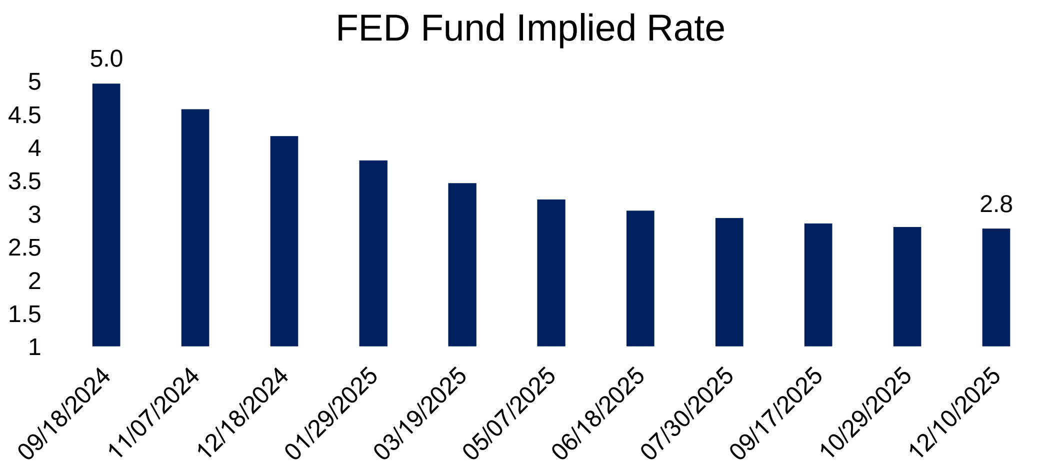
Fed Pivot – Movement of US Yields and Expectations

- US yields softened across the curve as the expectations of a FED pivot started pricing in.
- US 10-year yield softened to 3.65%, and the spread between US 2–10-year yields narrowed.
- US fed fund rate expectations foresee a 200-250bps rate cut by 2025.
- The key watch in the Sep-2024 FOMC will be the quantum of rate cut. Current probability surveys point towards a 50-50% probability of either a 25 or 50 bps rate cut.

US 2 year and 10 Year Benchmark rates softened

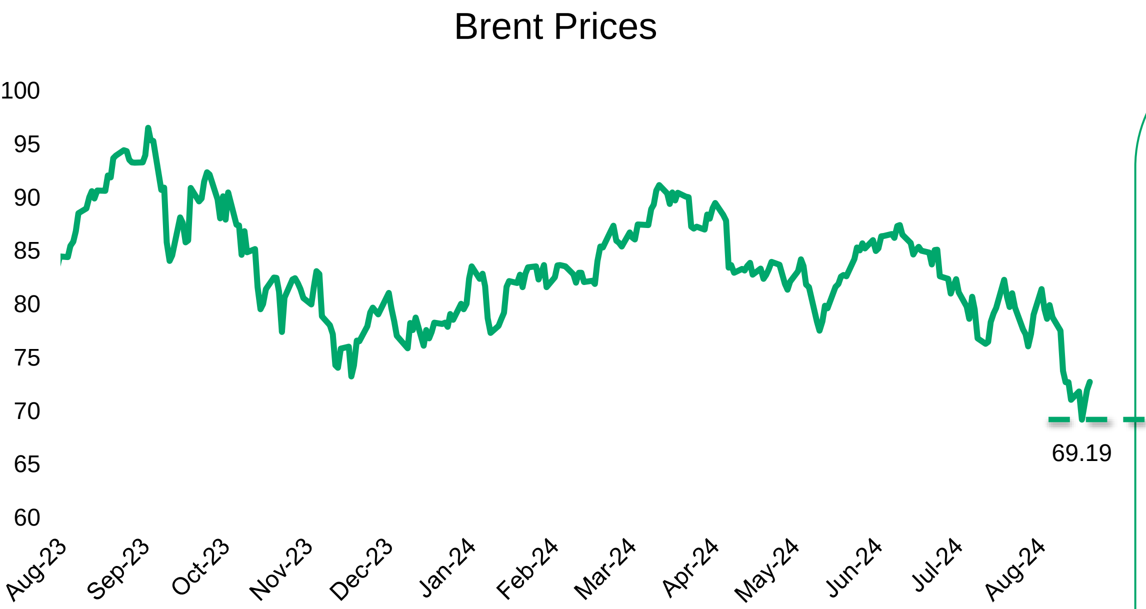


FED Fund rate projections implies a 200-250bps rate cut by 2025



Source: Bloomberg, Data as on 10.09.2024

Why is Brent Price falling?



MMBPD	2025 F	2024 F	2023	2022	2021	2020
Total World Supply	104.6	102.2	101.9	100.2	95.7	93.8
Total World Consumption	104.6	103.1	102.2	100.1	97.5	91.7
Change	0.01	0.91	0.28	-0.16	1.84	-2.14

- Brent prices were trading around 82$/bl in July-2024.
- In Sep-2024 the prices saw a steady decline to around 70$/bl and is currently around it.

The decline in brent prices is led by –

- Crude supply and demand forecast showcases lower demand in 2025. the demand and supply dynamics have started to price in the brent price.

What do we look forward to?

Although market concerns over economic and oil demand growth, particularly in China, have increased, causing oil prices to fall,
OPEC+ production cuts in Q4 FY24 will be a key watch.

OPEC - Organization of the Petroleum Exporting Countries
MMBPD- Million barrels of oil per day

Source: Bloomberg, Data as on 12.09.2024

Key Global Triggers

US FOMC 2024 meetings

- Widely anticipated event which is expected to be the key trigger for global flows.
- The key watch will be the quantum of rate cutting in September, Nov and December meetings.

US Elections

- US elections crucial for geopolitics. The risk from trade wars and import tariffs by US could weigh on China and other emerging market economies.
- Such tariffs are expected to lead to high inflation and could pressure US fiscal deficits.

China's Growth Outlook

- China's growth outlook remains significant in tow aspects. China's consumption power fuels growth outlook of neighboring economies.
- Secondly, slowdown in China has keep a deflationary phase and has contributed to moderating inflation pressures globally.

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

What does it mean for India ?

US Monetary Policy pivot

- US monetary pivot is expected to trigger flows to emerging market economies as interest differential narrows.
- India is favorably placed amongst this backdrop.
- 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 policy problem is witnessing a short-term fix where yen is under control and Japanese yields softened post expectations of US pivot.

Source: Internal Research

Domestic Economy

India GDP Q1 FY25- Positive Impulses

Components of GVA Growth YoY%	Weightage in GVA %	FY24	FY24				FY25
			Q1	Q2	Q3	Q4	Q1
Agriculture	15	1.4	3.7	1.7	0.4	0.6	2.0
Industry	30	9.7	5.9	13.7	10.7	8.8	8.4
Services	55	7.6	10.7	6.0	7.1	6.7	7.2
Real GVA	100	7.2	8.3	7.7	6.8	6.3	6.8
Real GDP	100	8.2	8.2	8.1	8.6	7.8	6.7

GVA growth remained strong at 6.8% y/y in Q1 FY25 led by a broad-based increased across sectors

Agriculture

- Agriculture sector showed softer signs of picking up and grew by 2% y/y.

Industry

- Manufacturing activity moderated in Q1 FY25 but was partly offset by strong mining and construction activity, thus supporting industry growth

Services

- The services sector remained the key driver of GVA growth. Services activity grew by 7.2% y/y in Q1 FY25 vs 6.7% in Q4 FY25

Source: Bloomberg, Data as on 1.09.2024

India Q1FY25 GDP – Positive Impulses

Major Components of GDP growth YoY%	FY24	FY24				FY25
		Q1	Q2	Q3	Q4	Q1
Private Consumption Expenditure (PFCE)	4.0	5.5	2.6	4.0	4.0	**7.4**
Government Consumption Expenditure (GFCE)	2.5	-0.1	14.0	-3.2	0.9	**-0.2**
Gross Fixed Capital Formation (GFCF)	9.0	8.5	11.6	9.7	6.5	**7.5**
Real GDP	**8.2**	**8.2**	**8.1**	**8.6**	**7.8**	**6.7**

Consumption –

- Pickup in private consumption expenditure is likely to have been supported by both urban and rural demand.
- In lieu of general elections government consumption expenditure remained subdued and declined by 0.2% y/y in Q1 FY25.

Investments –

- Gross fixed capital formation (GFCF) A proxy for investments in the economy remained strong irrespective of lower contribution by government.

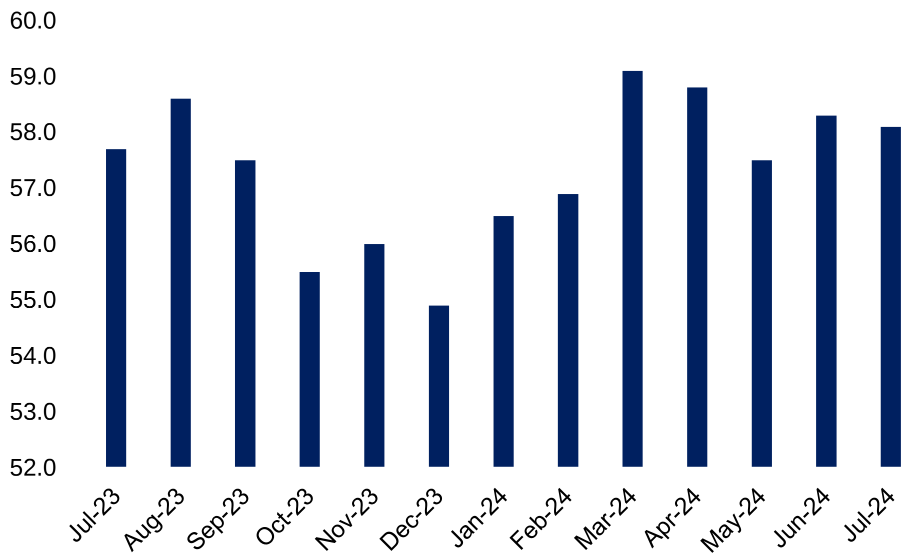
Source: Bloomberg, Data as on 1.09.2024

India Production Activity

Production YoY %	Mining	Manufacturing	Electricity	General IIP index
Average of last 10 years	**2.9%**	**3.0%**	**6.5%**	**3.3%**
July-24	**3.7%**	**4.6%**	**7.9%**	**4.8%**

- India's production activity remained strong.
- India's industrial production number for July 2024 was higher than its long run average of 10 years.

India Manufacturing PMI

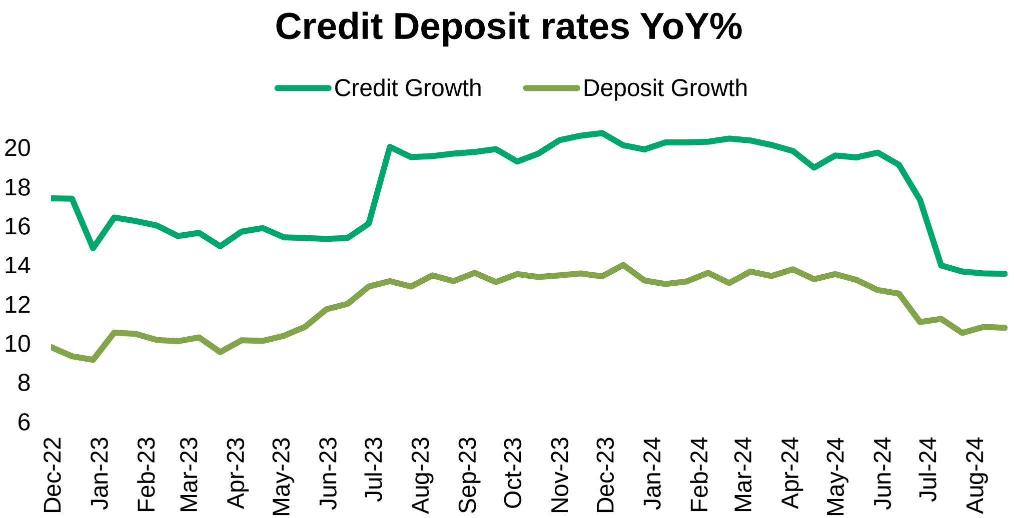


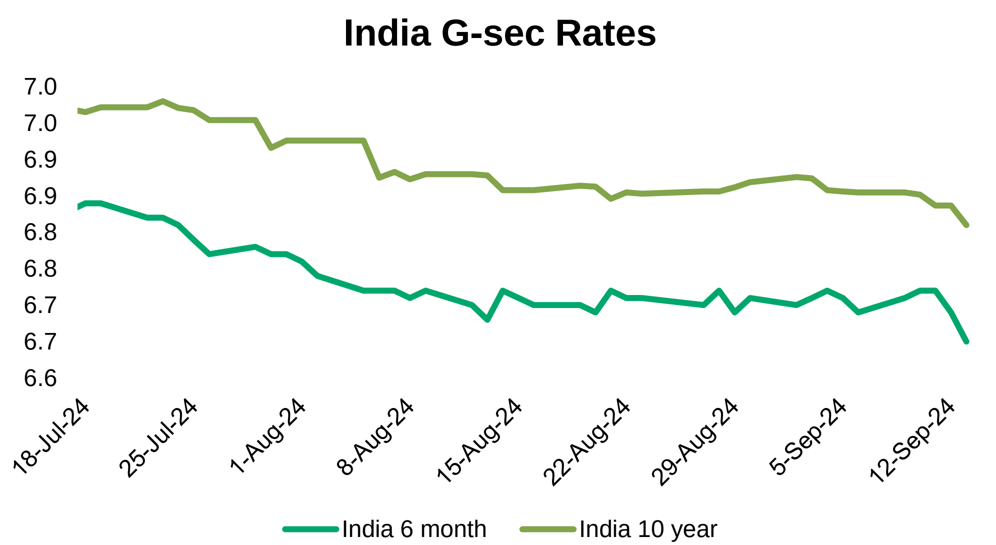
Key PMI Survey Highlights

- Output continued to rise at a historically sharp pace, the rate of expansion moderated to the slowest since January.
- On a positive note, the rise in input costs slowed
- sharply.
- Manufacturers increased their raw material buying activity in order to build safety stocks.
- In line with input costs, the pace of output price inflation also decelerated, but the deceleration was to a much smaller extent.
- Thereby increasing margins for manufacturers.

Source: Bloomberg, Data as on 15.09.2024

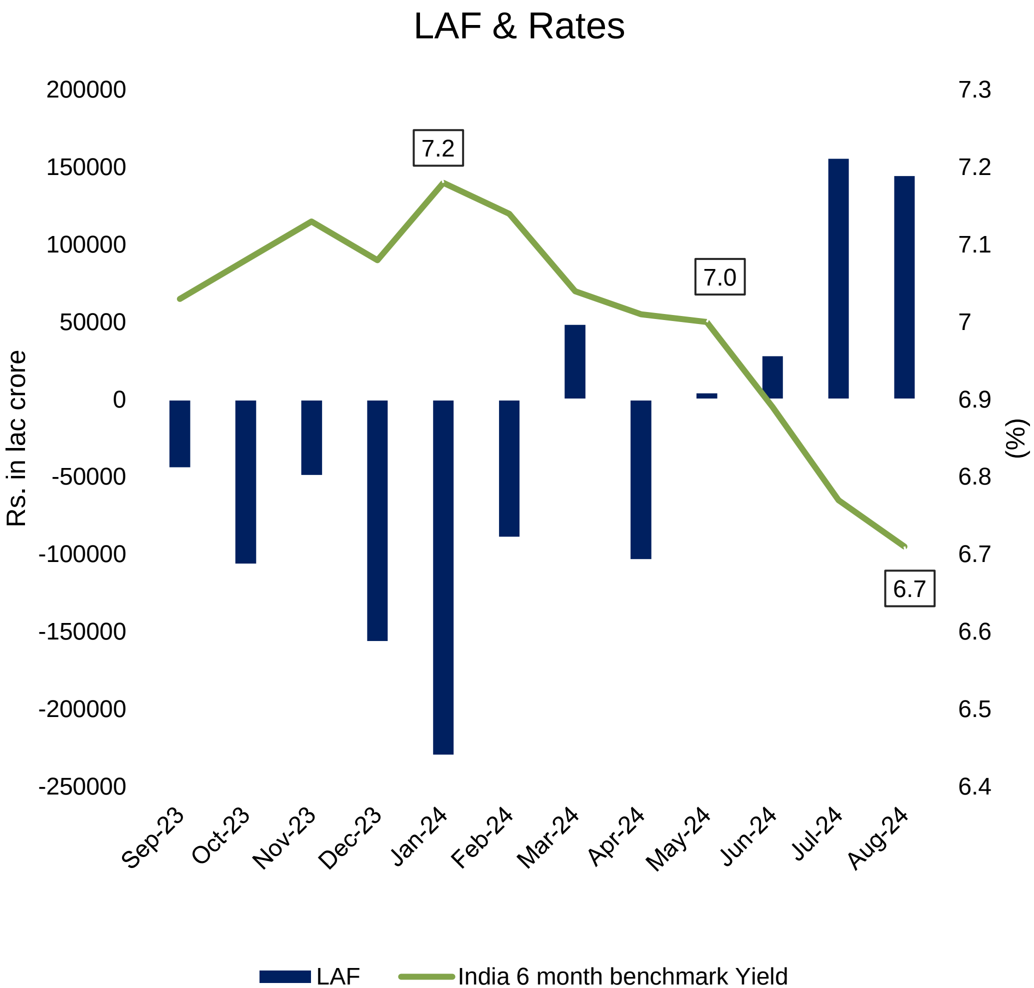
India Rates – Bond Yields and Credit Rates





- Credit growth has been above deposit growth for the past 29-months.
- Although credit growth has moderated to 13.3% in Sep-24 from a peak of 17.8% in Oct-22, the credit-deposit ratio remains elevated at 78.6%, having tracked above 77% since Nov-22.
- We expect seasonal factors such as increased incremental credit demand alongside currency in circulation driven by the festival / wedding season to create some pressure on liquidity in 2HF25.
- However, this will likely be offset by an improving trend in government spending.
- India government bond rates softened further in Sep-2024, driven by expectations of FED pivot.

Liquidity & Rates



LAF- Liquidity Adjustment Facility

What is driving the liquidity surplus?

- Continued government spending has managed to keep liquidity comfortably in surplus zone.
- India's 6-month g-sec rates have softened to 6.7% and overnight rates are tracking the liquidity conditions and have remained below repo rate.

Liquidity Outlook –

- Government cash balances is expected to have picked up to around Rs 2 trn due to indirect and direct tax collections.
- Hence, we can say that government's WMA balances are coming down and is visible in liquidity numbers.
- We remain positive on liquidity outlook given expectations of stance change in Q3 2024.

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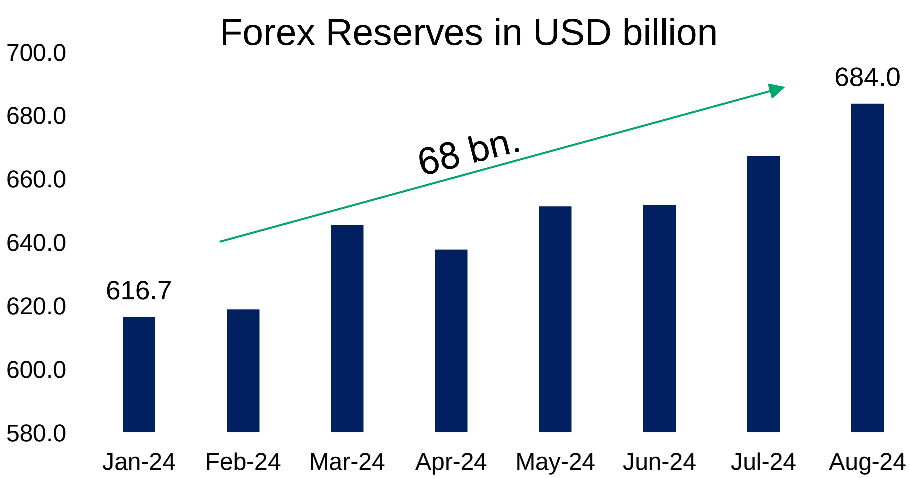
WMA – Ways of means and advances
Source: Bloomberg, Data as on 31.08.2024

Currency and Reserves

India FPI Flows in USD million			
Date	Equity	Debt-General Limit	Debt-FAR
Jan-24	-3,094	2,379	-
Feb-24	184	2,696	-
Mar-24	4,241	1,636	-
Apr-24	-1,034	-1,309	-
May-24	-3,058	1,048	-
Jun-24	3,180	1,786	-
Jul-24	3,870	2,667	-
Aug-24	873	2,131	-
Sep-24	3,315	6	1,762
Total	**8,477**	**13,040**	**1,762**



- **FPI flows** – FPI flows remained robust in CY2024.
- This remains supportive of India's capital account and currency.
- **Brent Prices** – Brent prices have fallen by~8% from RBI 's monetary policy estimate of 85$/bl. A positive development for India's current account deficit.
- Despite appreciating bias, INR has remained range bound at around 83.9 levels.

But why is INR still not appreciating ?

- **RBI intervention-** The most likely reason why rupee is range bound is RBI's fx intervention. RBI is likely absorbing the dollar inflows in the economy. This consistent dollar buying by the central bank has not allowed the rupee to appreciate.
- FX reserves for the week ending Sep 09, 2024, stood at USD 689 billion. Foreign currency assets holding out of total reserves stood at USD 604 bn., higher by $77bn from same time 2023.

Source – Bloomberg, RBI, Data as on 15.09.2024

Decoding Yield Signals

Economic Variable	Our View	Impact on yields
Growth	Rural 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 4.6% y/y in FY25.	↔
Domestic Liquidity	Liquidity conditions improved post election led by ongoing government spending.	↓
Fiscal Health	Lower than expected government borrowing is positive for the bond markets.	↓
RBI Monetary Policy	RBI is expected to maintain pause on repo until FED pivots. 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	US FOMC policy language has been dovish and our view is that the Fed is getting closer to a rate cut. The expectations arise from its incremental confidence in inflation.	↔

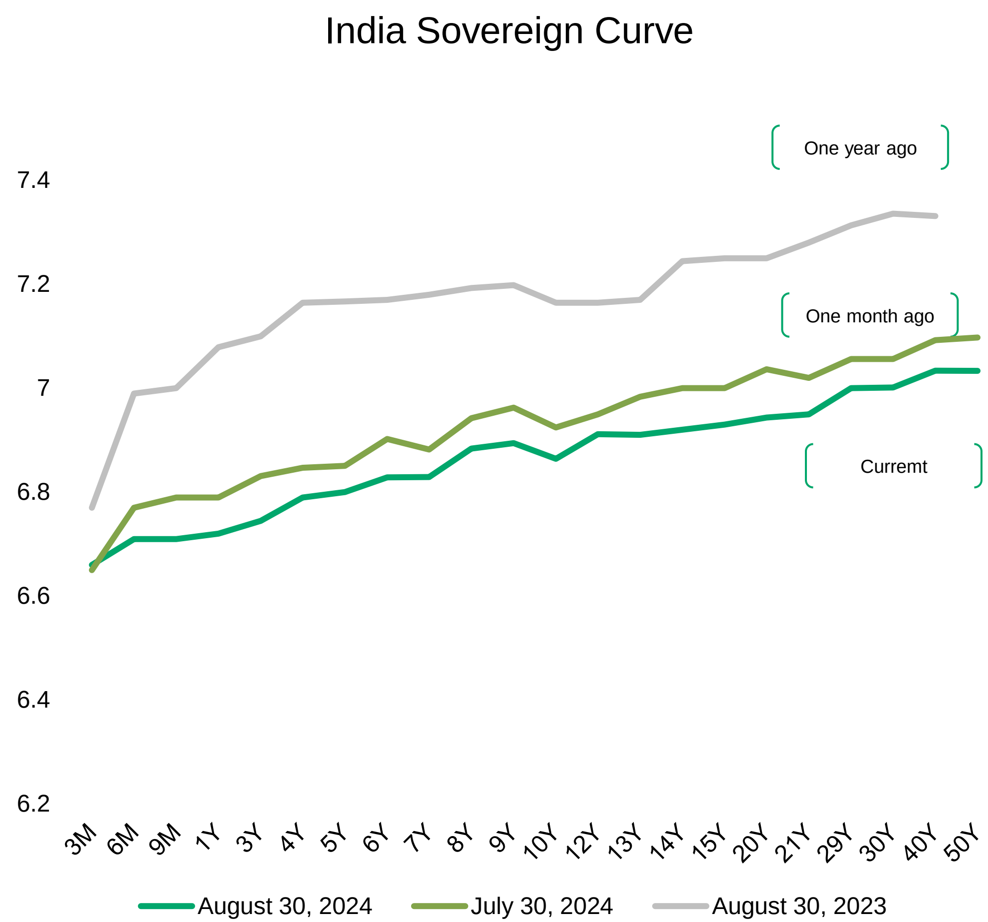
Source – Internal Research

Source: BBNP Paribas Research

Fixed Income Outlook

Outlook

- India Fixed Income outlook has been driven by two key fundamentals.
- Firstly, Global Monetary policy dynamics will be the key trigger for global liquidity and flows. India is placed as an favorable destination amongst other emerging market economies. Also, we have already started to witness robust flows in both equity and debt segments.
- Secondly, domestic inflation remains a key watch for RBI's monetary policy decision making.
- Headline inflation is expected to remain above 4% for entire fiscal FY25, with some headroom of inflation's closest call to 4% in Feb-2024.
- Therefore, we expect post FED's pivot, RBI's response will be attuned to first a stance change and followed by a lag in rate cut. The space to pivot is in Q4 FY25.
- Our view on rates remain optimistic with fundamentals aligning with fixed income outlook expectations of softening across the 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 01.09.2024