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06 February 2025

RESEARCH

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SUMMARY

INDIA ECONOMICS: MONTHLY ECONOMIC BUFFET

As expected, US President Donald Trump has announced sweeping tariffs (25%) on goods imported from Mexico and Canada. Chinese goods will also face 10% tariffs in the US. Retaliatory measures have been announced by all three countries, leading to fears of higher inflationary pressures in the US. Annual growth estimates show that US GDP was up by 2.8% in CY24 versus 2.9% in CY23. For this year, Fed expects growth at 2.1% and inflation at 2.5%. At the start of the year, labour market is showing signs of slowdown, but inflation expectations in forward looking consumer survey remain elevated.

Click here **for the full report.**

INDIA ECONOMICS: PRICE PICTURE

BoB's Essential Commodity Index (ECI) exhibited a further downward momentum in Jan'25, dipping to 4% on a YoY basis, moderating from 5.4% in Dec'24. On a sequential basis, the index declined sharply by 2.4%, after a fall of 0.5% in Dec'24. The decline was largely led by lower prices of vegetables, with tomato, onion and potato prices declining steeply. Edible oil prices were also lower. We thus expect a significant moderation in headline CPI in Jan'25. CPI inflation is expected in the range of 4.5-4.7%. The inflation outlook is evolving broadly in line with estimates, with significant support stemming from easing prices of vegetables.

Click here **for the full report.**

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INDIA ECONOMICS: MONETARY POLICY EXPECTATIONS

A lot has changed since the last monetary policy meeting of RBI. The most notable among them is the rising volatility visible in major asset classes, especially for INR. Most of it is attributable to rising geopolitical tensions emerging from anticipated tariff and counter tariff by US and major economies such as Canada, Mexico and China. This has propped up the dollar, thus impacting all currencies. The spillover effect was felt on domestic liquidity conditions as well where considerable tightening was noticed. Banking liquidity also witnessed strain as deposits growth showed moderation albeit normalisation in credit growth.

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MONTHLY ECONOMIC BUFFET

05 February 2025

Economic Round-up: January 2025

Sonal Badhan
Economist

As expected, US President Donald Trump has announced sweeping tariffs (25%) on goods imported from Mexico and Canada. Chinese goods will also face 10% tariffs in the US. Retaliatory measures have been announced by all three countries, leading to fears of higher inflationary pressures in the US. Annual growth estimates show that US GDP was up by 2.8% in CY24 versus 2.9% in CY23. For this year, Fed expects growth at 2.1% and inflation at 2.5%. At the start of the year, labour market is showing signs of slowdown, but inflation expectations in forward looking consumer survey remain elevated.

As a result, analysts expect Fed to keep rates 'higher for longer'. This is in contrast to situation in the Eurozone. Sustained weakness in economic activity (stagnated GDP growth, contraction in manufacturing activity) has forced ECB to lower policy rates by 125bps so far. Another 75-100bps cuts are priced in for this year. Any tariff announcement by US on European goods poses further downside risk to growth and upside risk to inflation. Domestically, high frequency indicators for Q4 are sending mixed signals. Nonetheless, domestic consumption remains robust with GST collections coming in at 9-month high in Jan'25. Latest budget announcement will further propel demand in FY26.

Global Central Banks: In Jan'25, in line with market expectations, US Fed held rates steady, while ECB lowered it by 25bps. US Fed held rates unchanged in the view of steady labour market conditions. The central bank has also cautioned against build-up in price pressures and will note the impact of policy changes before announcing further rate cut. Analysts do not expect any rate cut by Fed before Jun'25. The ECB lowered its policy rate by 25bps—5th rate cut so far, given the ongoing steady disinflation process. Analysts expect continuous rate reduction by ECB till Jun'25. BoE is also expected to cut rates by 25bps this week. In case of BoJ, the central bank hiked rates by 25bps, taking short-term rate to 0.5% from 0.25% earlier. This was on account of sustained increase in wages and inflation. Given this momentum is still continuing, more rate hikes are expected by BoJ in the coming months. RBI will also announce its policy decision this week and we expect a 25bps rate cut.

Key macro data releases: Union Budget for 2025-26 was recently announced, which showed that government curtailed its fiscal deficit-GDP ratio to 4.8% in FY25 (RE) and aims to further lower it to 4.4% in FY26. Income and expenditure estimates for FY26 were announced in line with nominal GDP growth expected next year (10.1%). Capex, and expenditure on rural and agriculture has seen a significant push. Boosting consumption demand was also in focus with tax rebates announced. NSO has estimated that Indian economy is expected to clock a growth of 6.4% in FY25.

PRICE PICTURE

05 February 2025

Inflation seen trending lower

Aditi Gupta
Economist

BoB's Essential Commodity Index (ECI) exhibited a further downward momentum in Jan'25, dipping to 4% on a YoY basis, moderating from 5.4% in Dec'24. On a sequential basis, the index declined sharply by 2.4%, after a fall of 0.5% in Dec'24. The decline was largely led by lower prices of vegetables, with tomato, onion and potato prices declining steeply. Edible oil prices were also lower. We thus expect a significant moderation in headline CPI in Jan'25. CPI inflation is expected in the range of 4.5-4.7%. The inflation outlook is evolving broadly in line with estimates, with significant support stemming from easing prices of vegetables.

Global prices of edible oils too have softened, which is positive for domestic inflation trajectory. Prospects of higher production due to improvements in sowing of pulses (up by 2.3%) and wheat (up by 2.8%) in the ongoing rabi season, bodes well for domestic availability of these crops. Recent announcements in the Budget targeted at easing the supply-side issues related to oilseeds, pulses and vegetables and fruits should aid in preventing the sporadic food-price shocks which tend to unhinge the inflation outcome.

For detailed methodology please refer to our ***previous edition*** of BoB ECI.

Price picture using BoB Essential Commodity Index:

- In Jan'25, BoB ECI showed a considerable moderation on both YoY and MoM basis. On a YoY basis, BoB ECI decelerated to a 6-month low of 4%, marking a significant correction from 5.4% in Dec'24. Out of the 20 commodities in the index, 14 commodities noted price increase of below 4%. Amongst major items, prices of vegetables continued to trend lower. Within the TOP (Tomato, Onion and Potato) vegetables, prices of tomato declined by 5.3%, compared with a 22.4% increase in Dec'24. Potato prices also eased to 34.8% in Jan'25 after increasing by an average rate of over 50% in the last 6 months. However, onion prices showed an uptick and rose by 3.2%, after declining in the last two-months. This can be explained by a negative base effect. Similarly, prices of edible oils also saw some upward momentum due to an adverse base effect.

- On a sequential basis, BoB ECI declined by 2.4%, marking the sharpest pace of decline in the index since Feb'18. This followed a drop of 0.5% in the index in Dec'24. On a sequential basis, prices of all TOP vegetables (tomato, onion and potato) have seen sizeable declines, led by tomato (-34.1%), onion (-21%) and potato (-15.9%).

MONETARY POLICY EXPECTATIONS

05 February 2025

Starting of a shallow rate cut cycle

Dipanwita Mazumdar
Economist

A lot has changed since the last monetary policy meeting of RBI. The most notable among them is the rising volatility visible in major asset classes, especially for INR. Most of it is attributable to rising geopolitical tensions emerging from anticipated tariff and counter tariff by US and major economies such as Canada, Mexico and China. This has propped up the dollar, thus impacting all currencies. The spillover effect was felt on domestic liquidity conditions as well where considerable tightening was noticed. Banking liquidity also witnessed strain as deposits growth showed moderation albeit normalisation in credit growth.

Domestic growth continued to show patchy recovery with premiumization continuing to take the front seat. Q3 financial results of corporates again mirrored the trend of moderation in sales. The same will be reflected in manufacturing GVA. Inflation the main monetary policy objective, however, is expected to provide the desired comfort. The Dec print showed moderation. Even Jan print is expected to be lower in the range of 4.5-4.7%. Considerable correction in TOP (Tomato, Onion and Potato) vegetables along with better arrivals have driven prices of these volatile items of CPI lower. Thus, it gives RBI the bandwidth to embark on its rate cut journey, albeit at a shallow data dependent pace in the future. Cumulatively we expect 50-75 bps cut in the current cycle.

What has changed since the last policy?

RBI in its upcoming policy is expected to encounter a trilemma encompassing 1) tighter liquidity conditions 2) depreciating INR and 3) heightened geopolitical uncertainty. The risks were not so profound in the last policy which expressed concerns about missing growth forecast and transient risks of inflation resulting in the misalignment of the 4% target. Let’s chart out the three risks in detail:

1) **Tighter liquidity:** The liquidity situation started getting tighter in Jan-25 when durable liquidity went into deficit. A plausible explanation could be tighter dollar and resulting drawdown of foreign exchange reserves. In Jan-25 itself, forex currency assets have fallen by US$ 14bn. Durable liquidity went into a deficit of Rs 40,000 crore as on 10 Jan 2025, which was not visibly present in the series since RBI started publishing the data of durable liquidity. Hence, the host of measures ranging from long term VRR and OMOs are targeted towards retaining the durable liquidity in surplus mode. On Banking liquidity front as well, incremental deposits and borrowings net of incremental investment and credit has fallen as deposits growth has shown loss of momentum albeit correction in credit growth.

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Note: Recommendation structure changed with effect from 21 June 2021

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