

By:  
 Kanika Pasricha  
 kanika.pasricha@unionbankofindia.bank  
 Shreyas Bidarkar  
 shreyas.bidarkar@unionbankofindia.bank

**Trade War Worries Lead to Caution and a period of elevated uncertainty**

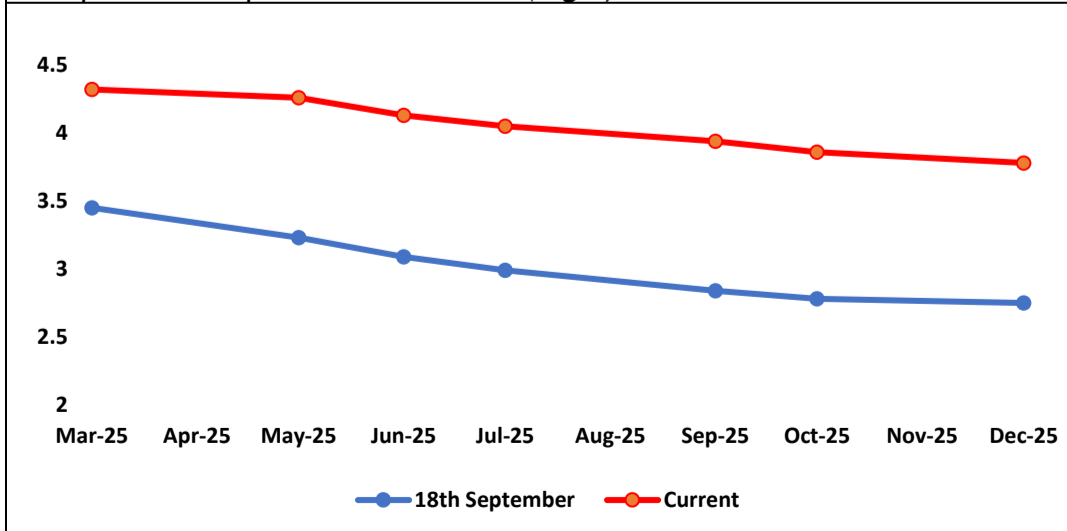
The market's attention has been focused on the wide array of new economic policies being rolled out from the US administration and their implications on the US economy. While the potential effects of tariffs, immigration, federal spending cuts and other high-priority policies remained key considerations. Trump's flip flops on trade tariffs are dimming the outlook for the global economy, leaving markets bracing for an extended period of uncertainty and positioning markets for new trade and political dynamics. This is playing out in reduced forecasts for economic growth in the US and countries targeted by Trump's policies. Tariffs are seen as likely to raise inflation, complicating the job for central banks that look to lower rates to support economic growth. While Trump's flip flops are creating uncertainty, spurring caution among investors facing an extremely difficult-to-predict economic outlook. Recently, Trump said he plans to impose reciprocal levies on every nation, but the rates would be lower than expected, and we're going to make it very lenient.

Trump's initial plan was to "Make America Great Again" while trade tariffs were supposed to boost US manufacturing, protect jobs and raise tax revenues supporting overall economic outlook. But the way Trump has handled the trade tariffs it has rather created uncertainty among the market participants which has led to lower growth forecast and weakness in US Dollar. The talks of recession have also been making rounds as was seen during mid-2024 when labour market data was deteriorating fast which triggered Sahm rule. But this time it's too early to call for recession if we assess economic indicators from the US even as Treasury Secretary Bessent has asserted that there's going to be a detox period with Trump also reiterating that this is a period of transition, because what we're doing is very big.

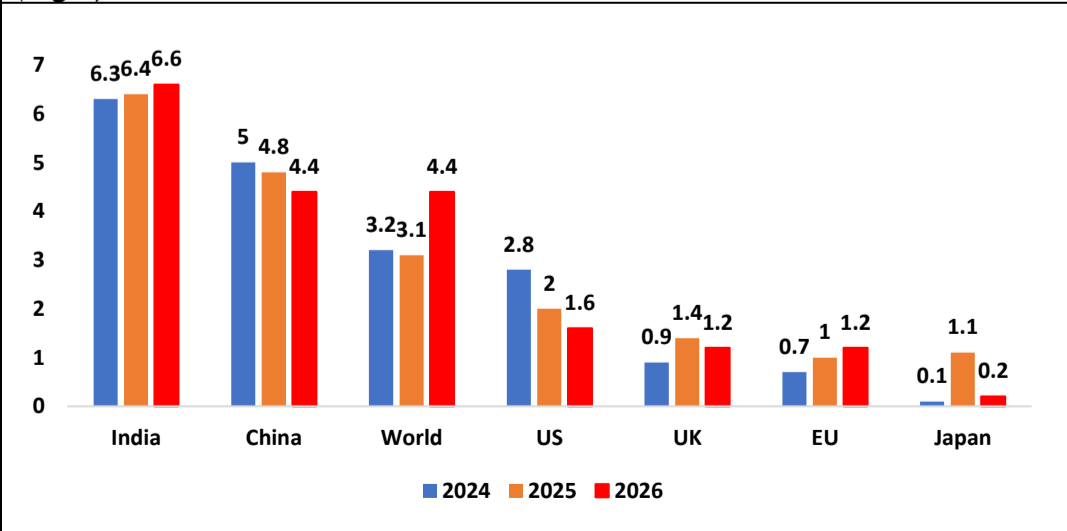
The next big trigger for markets is the reciprocal tariffs which are likely to be announced on 2nd April. The US dollar is gaining some strength as this deadline has led traders to trim risk positions and seek refuge in the USD. As per our [Trumponomics & its impact on India](#) report China/EU are likely to be worst affected while India may be relatively cushioned. While Trump has clearly identified India as a potential tariff target in his "Fair and Reciprocal Plan" on Trade with details scheduled for release on 2 Apr, noting the imbalance in the Most Favoured Nation (MFN) tariffs applied by India on goods such as agriculture in relation to the US. Every now and then, Trump has reaffirmed his tariff threats on India and while he noted that India is "probably going to be lowering those tariffs substantially", the US will be "charging them the same tariffs they charge us" on 2 Apr. This reciprocal tariff is likely to start trade war amongst the nations and its impact on global economy needs to be watched closely. Given the key countries on which tariffs are likely to be imposed like EU / India have already started trade talks with the US to avoid reciprocal tariffs, the final shape and form of the policy measure may not be as dramatic. The key themes for our Uni-Fx are outlined below.

- ♣ Market theme shift from US exceptionalism to un-exceptionalism has led U-turn in Dollar
- ♣ Euro rallied on back of German historic debt break reform
- ♣ BoJ holds rate steady, now focus turns towards reciprocal tariffs
- ♣ Threshold shift in Rupee led by positive seasonality, Dollar move & stalling of FPI outflows

Markets now expect Fed to cut rate twice this year by total of 50bps as against 100bps on 18<sup>th</sup> Sep'24 Jumbo rate cut (Fig 1)



Global growth forecast is projected to remain moderate in coming years (Fig 2)



Source: Bloomberg, Reuters, UBI research, OECD

**Market theme shift from US exceptionalism to un-exceptionalism has led U-turn in Dollar**

*Consumer confidence remains weak and economic policy uncertainty has spiked in various economies*

The global economy remained strong in 2024, growing at an annualized 3.3%. While the U.S. also saw solid domestic demand driven by consumption, the euro area remained weak amid contraction in Germany. Japan maintained resilience despite tighter policies. Emerging markets showed mixed performance, while Mexico's growth slowed, Brazil and India remained strong. But due to current flip flops from Trump administration over trade tariffs and uncertainty over economic policies has led to a macro environment where various economies have lowered their GDP forecast and elevated the inflation threshold level projection this year. The outlook for rest of the year currently looks uncertain amid US trade policies, while the effect of German debt break along with the trade tariffs on EU and China is yet to be seen which is likely to induce high market volatility going ahead. Interestingly, an academic research paper shows that the impact of tariff impositions would adversely affect the country imposing the tariffs rather than the country on which it is imposed. Consequently, the macro outlook for US, the country imposing tariffs, has come under pressure with growing stagflation concerns. This has raised questions over "US exceptionalism" theme with the shift seen towards "un-exceptionalism" driving market moves.

*Inflation continues to linger in many economies*

**Recent activity indicators suggest slower growth in Q1'25 amid rising uncertainty**

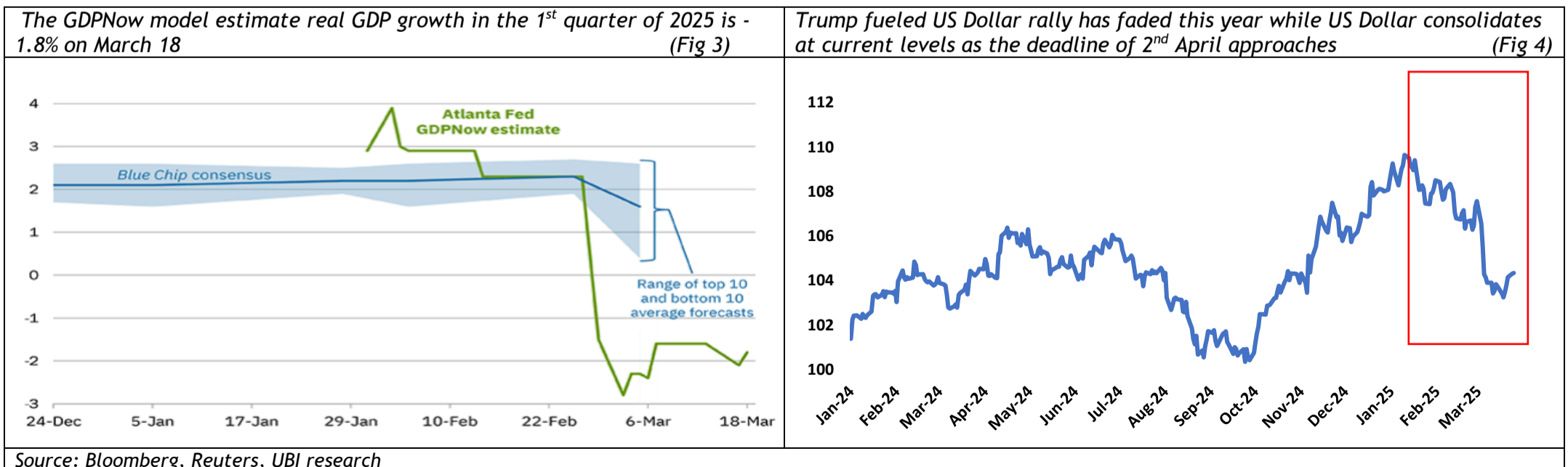
The outlook for the first half of the year is currently looking bleak as high-frequency indicators has started to illustrate some weakening of global growth in the Q1 of 2025. Consumer confidence has also dipped in early 2025 despite strong growth in real incomes in many economies. In the US, business expectations for the year ahead fell to their second lowest since October 2022 as companies grew increasingly cautious about the economic outlook, often citing worries over customer demand and the impact of aspects of the new administration's policies. Trade policy uncertainty has risen sharply due to new trade barriers imposed by several countries. This has led to a significant increase in economic policy uncertainty, particularly in Canada and Mexico, where higher U.S. tariffs have had a notable impact.

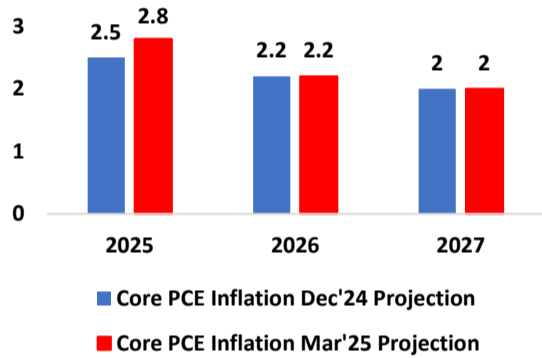
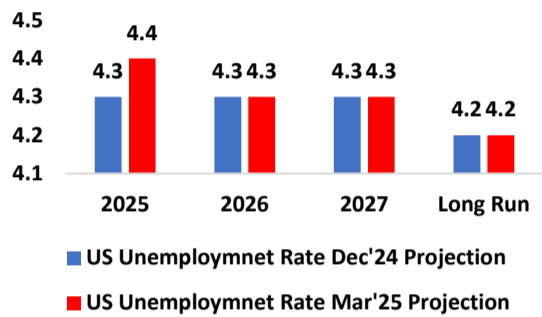
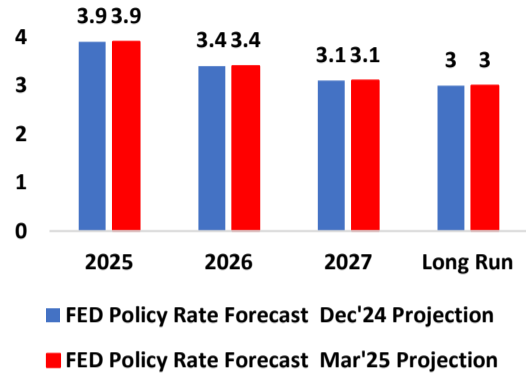
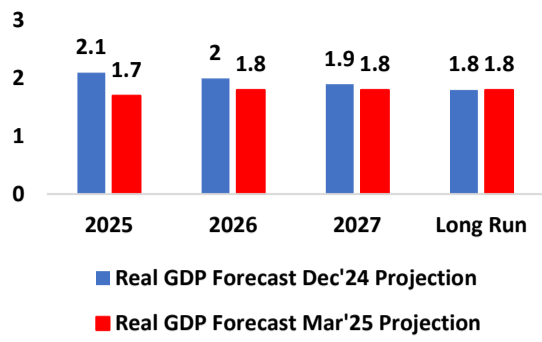
*Odds of recession in US are creeping higher*

**Some brown shoots in recent US economic data could it lead towards recession?**

The economic data continues to show some worrisome picture with some brown shoots, with consumer confidence at all-time lows although the labor market data continues to hold up despite DOGE engaged in mass layoffs.

- The Federal Reserve Bank of Atlanta's (Fed) GDPNow barometer for Q1-2025 growth remains in negative territory, with an estimate of -1.8% GDP growth as of March 18.
- US consumer sentiment continues to drop, the preliminary reading of University of Michigan consumer sentiment for March fell to 57.9. While consumer sentiment slid another 11%, with declines seen consistently across all groups by age, education, income, wealth, political affiliations, and geographic regions. Sentiment has now fallen for three consecutive months and is currently down 22% from December 2024. The expectations deteriorated across multiple facets of the economy, including personal finances, labor markets, inflation, business conditions, and stock market.





•US retail sales for February were lower than expected, and there was a substantial downward revision to US retail sales for January 4.

• US business activity growth picked up momentum in March as per flash PMI survey data as a marked upturn in the services sector offset a renewed fall in manufacturing output. However, business expectations for the year ahead fell to their second lowest since October 2022 as companies grew increasingly cautious about the economic outlook, often citing worries over customer demand and the impact of aspects of the new administration's policies.

**Rising probability of Trumpcession**

The above data points have increased the probability of a US recession and is rising as more brown shoots are appearing. Trump's import tariffs have shaken the consumer confidence and spooked the stock markets. Although its too early to call for recession as first quarter's weakness may be one off. The future also looks bright due to the promises of Artificial Intelligence, as well as recent public and private investments in infrastructure and technology. Will Trump's policies drive the US into recession (called as "Trumpcession") needs to be seen.

**Is Fed worried about stagflation?**

The Fed in its 18/19 Mar'25 FOMC meeting, unanimously decided to maintain the Fed Fund Target Rate at a range of 4.25%-4.50%, for the second straight meeting and in line with market expectation. One of the more eagerly awaited part of the Mar'25 FOMC was the Dotplot which showed that the FOMC members expect 50bps of rate cuts this year with the upper limit of the fed funds target range ending the year at 4% and another 50bps rate cut in 2026. While nine of 19 FOMC members expect 50bps of cuts this year, 4 expect only one 25bps cut, and four expect no cuts while two expect 75bps of cuts.

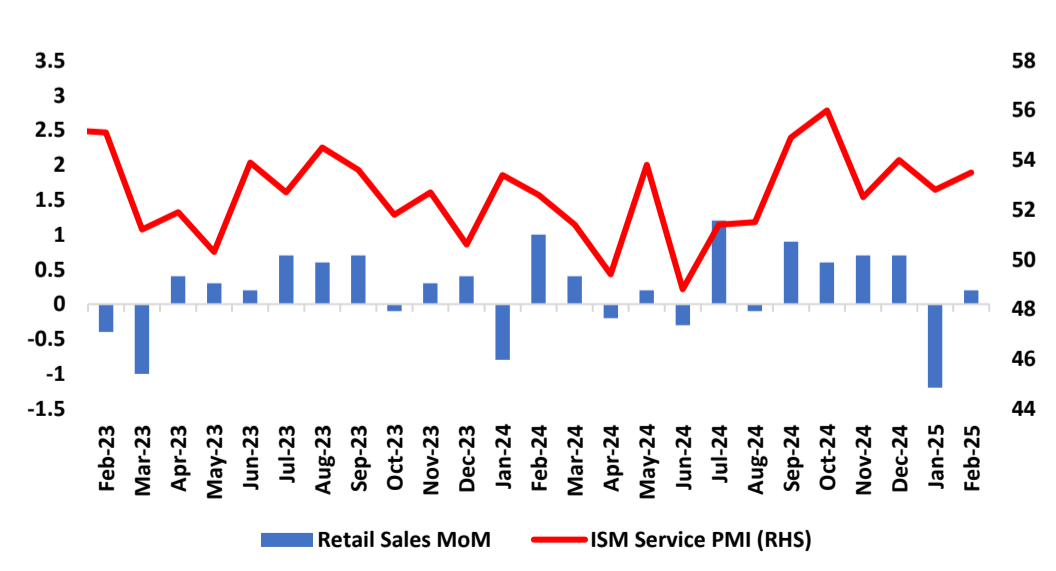
While in a non-unanimous decision to reduce the pace of quantitative tightening (QT) with Governor Waller dissenting as he preferred to keep the pace of QT unchanged. The Fed maintained its commitment to "continue reducing its holdings of Treasury securities and agency debt and agency mortgage-backed securities".

*The other major change in the text of the Mar'25 policy statement was that the Fed now warned that "uncertainty around the economic outlook has increased" while removing the mention that "the risks to achieving its employment and inflation goals are roughly in balance".*

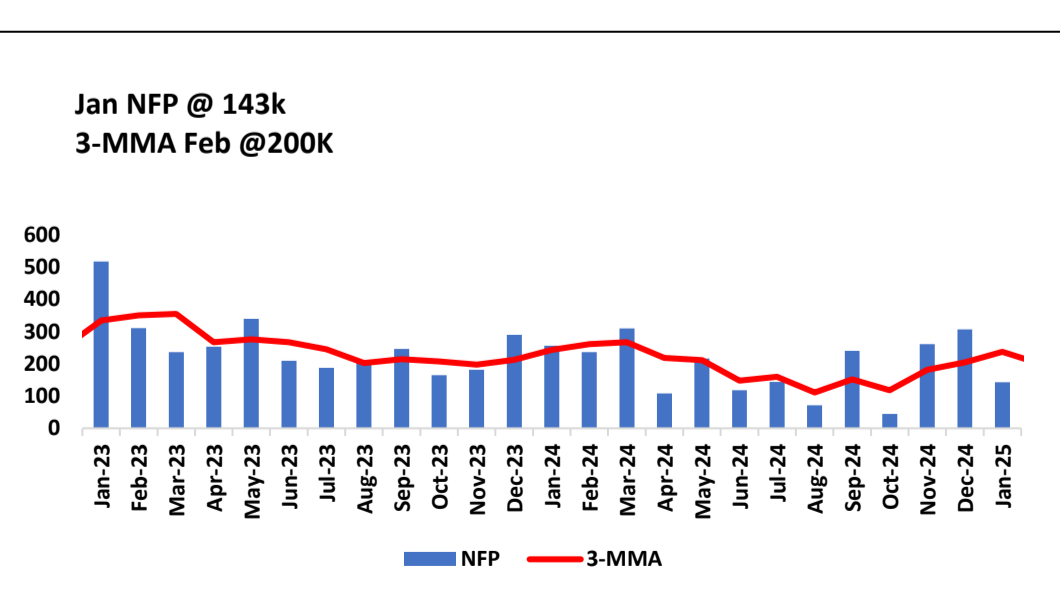
**Macro Forecast from Mar'25 FOMC meet**

The growth forecasts were reduced throughout the projection period. The FOMC now expects 1.7% growth this year as against 2.1% in Dec'24 forecast, 1.8% in 2026 which is down two-tenths, and 1.8% again in 2027 which is down one-tenth. The long-run potential growth rate is still estimated at 1.8%.

US retail sales rebounded marginally in Feb'25 although consumers pulled back on consumer discretionary spending (Fig 5)



US NFP data was stable in Mar'25 despite mass layoff by DOGE (Fig 6)



Source: Bloomberg, Reuters, UBI research



The German fiscal reform package is likely to rejuvenate its economy

Tariff risks continues to loom

**Germany agrees to change the debt brake a historic fiscal reform**

The German government approved plan this month to loosen government borrowing limit allowing it to spend heavily on defence and infrastructure to offset U.S. pivot away from Europe. This pushed, relaxes the “debt brake,” a limit on government borrowing and will exempt defence spending (in excess of 1% of GDP) from the constitutional borrowing restriction known as the “debt brake”—a federal spending law that currently allows for a maximum structural budget deficit of just 0.35% of GDP. With the policy change the federal government can borrow unrestricted to finance defence spending.

**What is a debt brake and why the need to break?**

Germany borrows money to help balance its annual federal budget. But unlike some peers like the US, Germany has a Constitution that limits its yearly borrowing to just 0.35% of the country’s GDP. The debt brake was added to German’s constitution after the country’s budget deficit grew during the 2008 financial crisis. While some believe that debt brake also handcuffed German’s ability to spur its economy, invest in its future and lead in European security affairs. This has led the country’s net public investment to be negative for the last 25 years, holding back its economic growth. Releasing the debt brake had become urgent as the German economy continues to shrink and US President Trump has threatened to scale back or remove U.S. security role in Europe.

**EURO (€ - EUR) view:**

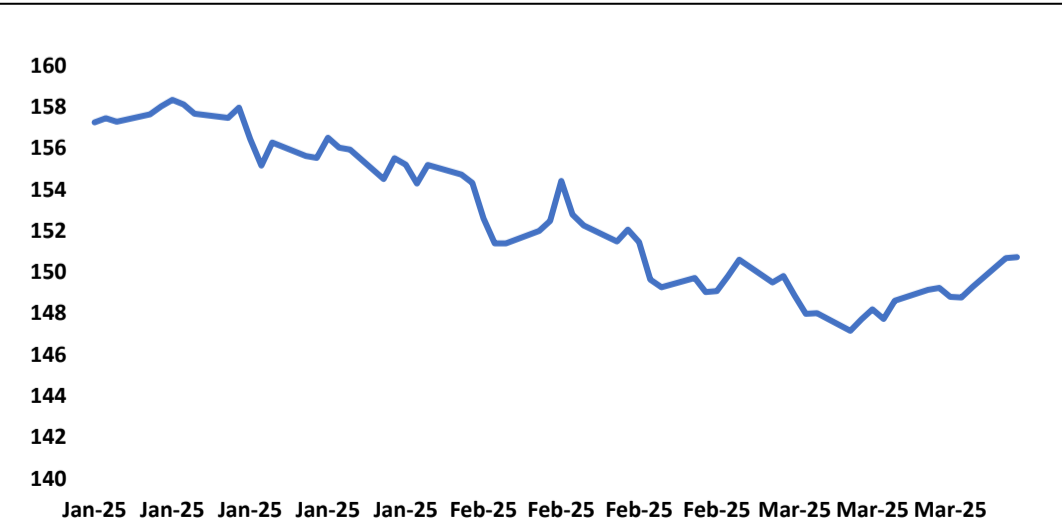
While fiscal spending efforts have already boosted the euro relative to the U.S. dollar. The stronger momentum could mean that the ECB can afford to shift towards a less dovish stance, although markets still expects the ECB to cut rates by 50bps this year, the probability of rate cut for 17th Apr’25 monetary policy stands at 66%. Tariffs, of course, remain a headwind to Europe and 2nd April is not far away, but the repositioning to domestic demand- and defence-driven growth as opposed to an export-driven model are changing the outlook. While on tariffs the European Union has been clear that in the event of US tariffs it would react “firmly and immediately.” While this tariff war is likely to weigh on the Euro. Technically the support for Euro/USD pair lies at 1.0510 and may face strong resistance at 1.1010.

**BoJ holds rate steady, now focus turns towards reciprocal tariffs**

The JPY continued to strengthen in the backdrop of weakness in US Dollar and has gained c.5% this year. This month it did manage to break below the crucial support of 150.00 on 11th Mar’25 just before the BoJ and FED policy meet but is again currently trading around the 150.0 mark. Another reason for yen to strengthen was the selling in US dollar continued after the Fed decided to slow the pace of balance sheet reduction and Fed Chair Powell suggested that recent inflation pressures were likely transitory along with trump’s announcement of peace deal between Russia and Ukraine.

In alignment with the technical range in our [Feb’25 Uni-FX](#) report, USDJPY pair took support at 146.50 levels the same was seen this month as the pair made low of 146.53 on 11th Mar’25 and bounced from those crucial levels.

JPY strengthened due to weakness on US Dollar and ceasefire between Russia and Ukraine (Fig 9)



Bank of Japan Governor Kazuo Ueda stated that the central bank will continue to raise interest rates if its underlying inflation target is likely to be achieved, despite potential losses on its government bond holdings

BoJ will continue raising interest rates if likelihood of achieving economic, price stability rises

Rupee rallied during this month focus shifts on reciprocal tariff announcement next week

The yen's rise has also been supported by shrinking yield gaps between Japan and other G10 economies along with this interest rate differentials between the US and Japan also remain one of the key driving forces for USD/JPY movements in 2025.

The highlight of this month was the monetary policy decision by BoJ which unanimously decided to keep its policy rate at 0.50% during the March 19 meeting. The BOJ emphasized that the virtuous cycle between wages and prices is strengthening. All the same, growing signs of sticky food inflation, which adds to prospects of sustained wage increases, will likely keep the BOJ on course to raise rates at a steady pace in contrast with more rate cuts signalled by its U.S. and European counterparts.

**Ueda concern over global uncertainty caused by US administration**

The BOJ Governor highlighted the high degree of uncertainty surrounding US trade policies, stressing the need to consider external factors when deciding on monetary policy. External uncertainties are likely to escalate in April, with the US government set to announce details regarding reciprocal tariffs.

The BOJ can incorporate to some extent the potential impact from Trump tariffs in its quarterly outlook report due at its next meeting on 1st May'25, while Ueda, signalling a rate hike at the meeting cannot be completely ruled out even though current consensus is for a tightening to occur around the third quarter.

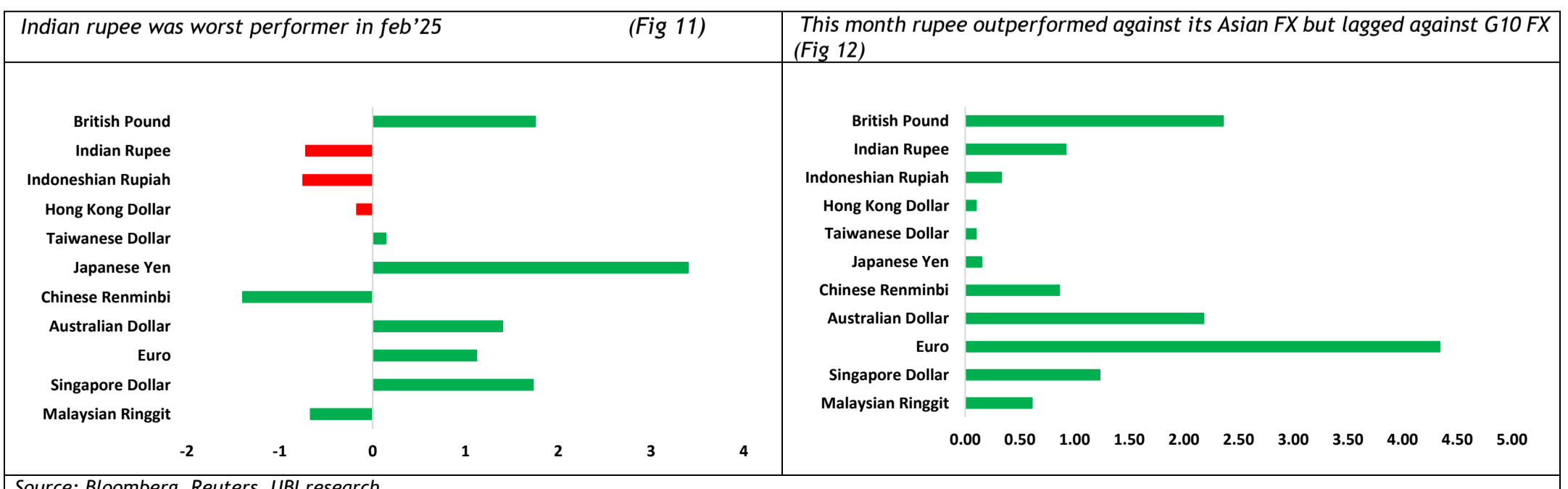
**JAPANESE YEN (¥ - JPY) view:**

With the conclusion of BOJ and FOMC meetings, market attention is pivoted toward U.S. trade policy in the coming week. Trump has reaffirmed his intention to implement reciprocal tariffs on April 2. To date, no exemptions have been announced for any countries, including Japan. Close monitoring of statements from Trump regarding these tariffs will be key things to watch out for. While currently markets are pricing in 33bps of rate hike this year while next policy meet on 1st May'25, the markets expect the BoJ to keep its policy rates unchanged the probability of which currently stands at 76%. Technically the next support level to watch out for is 146.00 a break of which and lead the pair to take support at 145.10 levels. On upside, 151.00 should provide a strong resistance followed by 152.50 level.

**Threshold shift in Rupee led by positive seasonality, Dollar move & stalling of FPI outflows**

This month is proving to be one of the best months for the rupee as it has recovered all its lost ground during the year and has positioned itself as one of the best performing currency amongst its Asian peers. The rupee started the year trading on a weaker note at 85.64 handle and made a low of 87.99 on 10th feb'25. It had to digest Trump's tariff threat, strength in US dollar, change of stance from RBI regarding the rupee, RBI rate cut, weak Q2'FY25 GDP data along with record FPI selling in equity segment.

But there has been dramatic shift this month, as rupee erased all of its losses for 2025. The key macro drivers were both global and domestic although the domestic factors did dominate over the global ones. Domestic factors such as lower trade deficit, lower inflation, stabilized FPI related inflows into equity and debt segment, RBI measures to ease banking liquidity and C/A deficit narrowed in Q3'FY25.



Source: Bloomberg, Reuters, UBI research

The flows into the equity markets have stabilized while FAR related flows are stronger this month

The rupee relative underperformance between Jan24 and Mar25 has helped to arrest its overvaluation on real effective exchange rate (REER) basis.

Reciprocal tariffs remain the threat any adverse tariff announcement could limit the room for rupee gain

While on globally front the weakness in U.S. dollar due to weak economic data, policy flip flops by Trump and strength in Euro over strong fiscal response from Germany has provided support to the rupee.

In equity segment flows turned negative this year to the tune of \$13bln but have stabilized significantly in the month of March'25 (Jan'25 -\$9.04bln, -\$3.978bln in Feb'25 and -\$0.41bln in March). While, the FAR related flows are strong this year to the tune of \$5.9bln where flows in Mar'25 was \$3.3bln compared to inflow of \$1.7bln in feb'25.

Trade deficit number for the month of Feb'25 was much better than market expectations at \$14bn from \$23bn the previous month. We have been mentioning in our reports that trade numbers show a positive seasonality in Jan'25 to Mar'25 quarter and hence we are likely to see some relief in net dollar demand. With the sharply positive surprise in trade data, we see a downside risk to our earlier FY25 C/A deficit projection of 1.2%. While goods deficit narrowed, services trade surplus also inched higher at \$18.48bn in Feb'25 vis-à-vis \$18.02bn a month ago and \$13.10bn in Feb'24. This is a positive trend in a slowing global economy and is likely to have a salutary effect on FY25 C/A dynamics.

The inflation prints in Feb'25 was also lower at 7-month low of 3.61% a sharp decline from 4.26% in Jan'25 and below RBI's target of 4%. The growth number for Q3'FY25 did improve the sentiment for the rupee which clocked 6.2% a significant improvement from 5.6% in Q2'FY25.

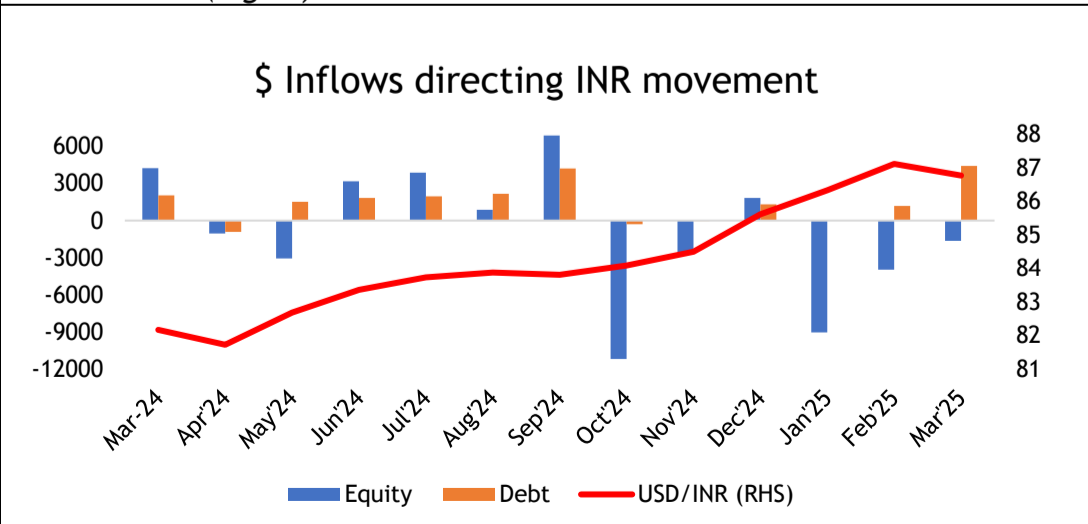
In Q3'FY25, C/A deficit narrowed to \$11.5 Bn (1.1% of GDP) from a \$16.7 Bn in Q2-FY25. Despite global volatility and restrictive tariff policies, we expect Current Account balance to report surplus in Q4'FY25 owing to support from strong service trade surplus and remittances.

The RBI continued its efforts to inject durable liquidity during Q4;24-25 like OMO purchase, term repo, USD/INR buy sell swaps for tenor of 6-months to 3-years and have injected Rs.6.9 lac cr. so far.

The rupee's real effective exchange rate against a basket of 40 currencies, in terms of trade-based weights, fell to 102.37 in February, its lowest level since May 2023, the rate was at 104.82 in January. While the rupee depreciated by 2.4% MoM in terms of the 40-currency REER in February 2025 due to depreciation of the INR in nominal effective terms and narrowing of India's inflation differential with its major trading partners. REER may have gone up in March as INR underperformed G10 FX like Euro and GBP. The RBI's dollar sales in the foreign exchange market were at \$60.28 billion in January, down from the record high of \$69.05 billion in December. India's foreign exchange reserves rose by \$305 million to \$654.27 billion in the week ended Mar. 14, likely owing to revaluation gains.

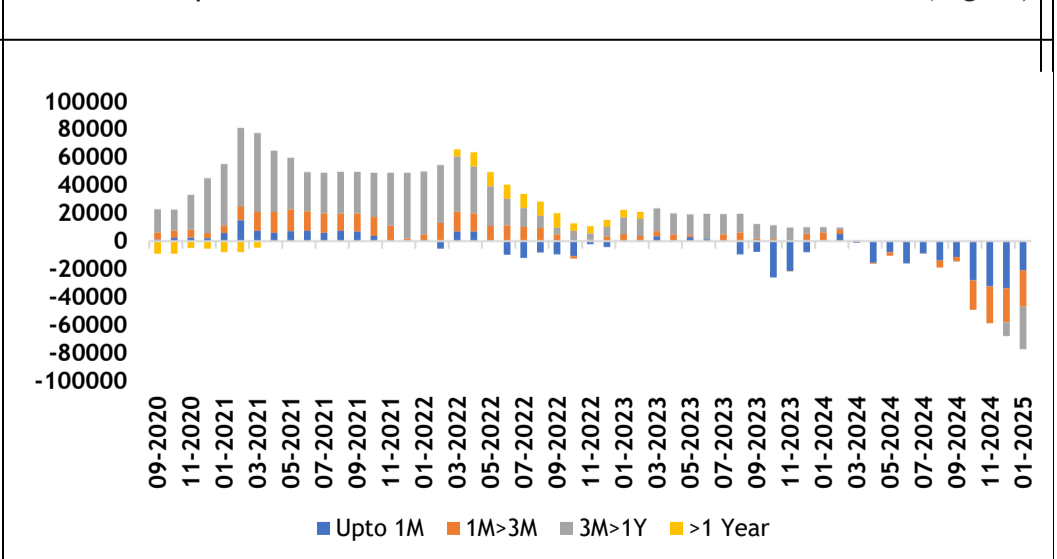
The rupee was one of the best performing currency among Asian peers but compared to other G10 FX it is still lagging behind. The larger risk to rupee in near term can arise if India is faced with higher reciprocal tariff from the US on 2<sup>nd</sup> April. Even though, we remain domestically driven economy and the Indian government is also trying to negotiate with US regarding tariffs and has also taken measures to lowered tariffs on some of its goods. The government has also been taking various steps to diversify its trading partners and has signed various agreements with EU, UK and New Zealand. Reciprocal tariffs remain the threat and any adverse tariff announcement could limit the room for rupee gain.

Rupee appreciated in March as flows in equity and debt market have stabilized (Fig 13)



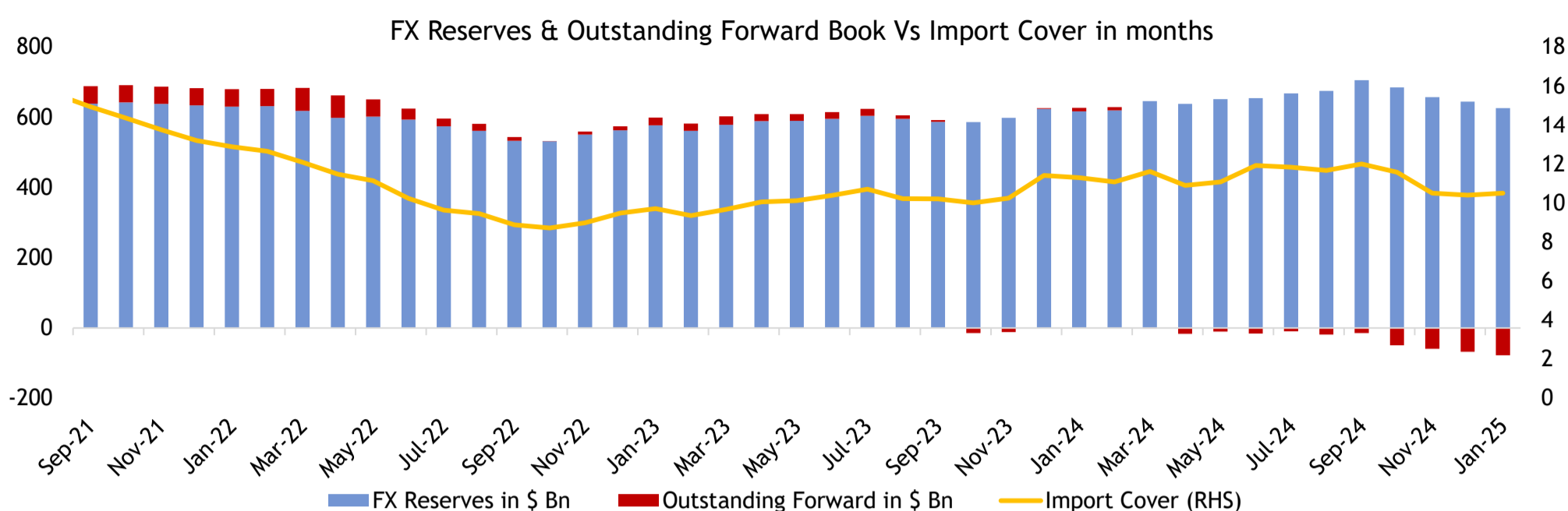
Source: Bloomberg, Reuters, UBI research

RBI forward position continues to rise at record levels (Fig 14)



FX Reserves continue to rise since last two months

(Fig 15)



Source: Bloomberg, Reuters, UBI Research

### Banking & Economic Research Team

Kanika Pasricha Chief Economic Advisor	kanika.pasricha@unionbankofindia.bank
Suneesh K	suneeshk@unionbankofindia.bank
R Gunaseelan	gunaseelan@unionbankofindia.bank
Nidhi Arora	nidhiarora@unionbankofindia.bank
Rajesh Ranjan	rajeshranjan@unionbankofindia.bank
Jovana Luke George	jovana.george@unionbankofindia.bank
Amit Srivastava	asrivastava@unionbankofindia.bank
Dhiraj Kumar	dhirajkumar@unionbankofindia.bank
Akash Deb	akash510@unionbankofindia.bank
Shreyas Bidarkar	shreyas.bidarkar@unionbankofindia.bank
Rohit Yarmal	rohitdigambar@unionbankofindia.bank
S. Jaya Laxmi	s.jayalakshmi@unionbankofindia.bank

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