August 5, 2025

Morning Briefing

Passage To India

Check out the accompanying chart collection.

Executive Summary: Trump's pivot on India from friend to foe, punctuated by a higher US tariff rate than expected, hit India watchers by surprise. Trump's dismissal of the country's importance to the West hurts Prime Minister Modi politically and India economically, William explains. A third of India's foreign investment comes from the US. But the world's fifth-largest economy is far from "dead," as Trump proclaimed. GDP growth has been outpacing China's, and the nation has big aspirations to position itself at the center of global supply chains and to become a developed nation by 2047.

Weekly Webcast. If you missed Monday's live webcast, you can view a replay *here*.

India's Tariff Shock I: Wake-Up Call. "What just happened?!," India watchers are wondering. In an abrupt pivot, US President Donald Trump wrote off the world's *fifth-largest economy* as "dead," lumping it in with the moribund economy of Russia, New Delhi's top oil supplier.

"I don't care what India does with Russia," Trump *posted* on social media Thursday. "They can take their dead economies down together, for all I care. We have done very little business with India, their Tariffs are too high, among the highest in the World."

But India is hardly resting in peace. India's Prime Minister Narendra Modi seems as shocked as anyone by Trump's sharp-tongued ending of their much celebrated bromance, culminating in a *25% tariff*. That's markedly higher than the *15% levy* Trump bestowed on Japan and South Korea, Washington's other top allies in Asia.

Suddenly, that triumphant 2019 50,000-person "*Howdy, Modi!*" rally in Texas seems a long time ago. Asia watchers are perplexed, too, by Trump's calling Modi's trade policies "*obnoxious*." India's tariffs have long served as a vital counterweight to China's regional ambitions.

With this sharp pivot, "Trump's causing *a lot of trouble for Modi*" and for India's economy. Modi now must explain to voters why he's not the ultimate Trump whisperer he had pitched himself to be. And for India Inc., this could be a break-glass moment.

Let's explore why a 25% tariff is so problematic:

(1) *Bromance interrupted*. Team Modi seemed to believe his rapport with Trump would enable India to score a tariff below the 19% that the White House assigned to *Indonesia* and *the Philippines*. Perhaps India might even get a *deal like Japan's*, with only minimal commitments to open its markets further. What a blunder on Modi's part those expectations turned out to be! They're especially farfetched now that Trump has turned on India's important partner in trade, Russia, even sending *nuclear submarines* into Moscow's orbit.

While the US relies on India for *just 2.3%* of its overall exports, Modi's economy gets one-third of its foreign investment from the US. The increasingly enthusiastic ways in which Amazon, Apple, Microsoft, and other household tech names are *investing in India* tell the story.

(2) *India shines economically*. Reports of India's economic death are wildly exaggerated. A recent report by research firm *Canalys finds* that Modi's economy has surpassed Xi Jinping's China as the globe's No. 1 smartphone exporter. In Q2, assembled-in-India smartphones accounted for 44% of US imports of such gadgets, a 13% y/y jump. The overall volume of India's smartphone business surged 240% over the last year.

The bull case for India is somewhat a product of Modi's early policies, including its vibrant startup scene. Excitement over India's *"unicorn"* boom in recent years has helped propel the BSE Sensex Index up *113%* since August 2020. The India MSCI stock price index (in local currency) is up 118% over the same time period (*Fig. 1*).

Tesla, for example, is veering India's way. As slumping sales in many markets test CEO Elon Musk's electric vehicle company, Tesla is pushing into the globe's most populous nation.

"We've been working on getting into India," Tesla CFO Vaibhav Taneja *told shareholders* in April. "It will be a great market to enter because India has a big middle class." Yet, he cautioned, the tariffs "create a little bit of tension, which we're trying to work around."

(3) *Outlook trumped*. Make that a whole lot of tension now that India may find itself on the

business end of Trump World's tariff bazooka. Modi's India is suddenly isolated at a moment when his Bharatiya Janata Party (BJP) thought it was creating a place for the economy at the center of global supply chains.

The good news is that India's Q1 GDP grew at a China-beating *7.4% y/y rate* (*Fig. 2*). The bad news is that higher-than-feared tariffs could make it difficult for New Delhi to generate growth anywhere near the *6.5% y/y* it had forecast for 2025. Even that optimistic forecast falls short of the 8% GDP growth needed annually to create enough jobs to meet Modi's goal of reaching developed-nation status *by 2047*.

India "has received a raw deal that could significantly hit its exports to the US," says Priyanka Kishore at *Asia Decoded*. "While further trade talks may bring down the 25% tariff rate and provide reprieve from a 'Russian penalty rate,' it appears unlikely that India will secure a significantly better outcome than its eastern neighbors, raising questions about its relative appeal as a China+1 destination."

India's Tariff Shock II: Self-Inflicted Wounds. While officials in New Delhi are probably directing much blame at the US, many of India's current troubles are products of the Modi era that began in 2014.

One mistake is attempting to straddle better ties with the US while also supporting Vladimir Putin's Russia via an estimated *$275 billion of oil purchases* per year, comparable to Peru's *annual GDP*. That balancing act is now blowing up on Modi, who so far hasn't moved to *turn off* the Russian spigot.

Similarly, India has an increasingly lopsided trade relationship with China. India's trade deficit with its northern neighbor hit a record *$99.2 billion* last fiscal year (ended March). Tensions over a disputed Himalayan border have both Modi and Xi averse to blink first. Only now are New Delhi and Beijing working to *resume flights* between the two countries that were grounded since the Covid-19 era.

Here's more on the challenges facing Team Modi:

(1) *Throwing BRICS*. New Delhi's BRICS association may now be thwarting Modi's hopes for closer US ties. Trump has long been suspicious of the Brazil, Russia, India, China, South Africa bloc, but its attempt at replacing the dollar as the reserve currency crosses a red line.

Individual BRICS members slapped with particularly sizable US tariffs include Brazil (50%) and South Africa (30%—the *highest* in all of sub-Saharan Africa).

(2) *Collateral damage zone*. The risk for India is that Trump will tighten the screws on the BRICS further for being “anti-the United States.” Catalysts could include a bigger falling out between Trump and Putin and China’s Xi walking away from the “grand bargain” US trade deal. If Trump announced a BRICS tariff on top of “reciprocal” levies, India Inc. would find itself in the middle of the collateral damage zone.

In 2024, India did more than *$129 billion of trade* with the US, its largest trading partner. Based largely on Washington’s desire to contain China’s global expansion ambitions, the US and India developed a strategic relationship in many sectors, especially in defense and technology.

Russian oil could be a particular flashpoint. Today, India buys more than *one-third of its oil* from Russia compared to 1% before Putin invaded Ukraine, according to commodities firm Kpler. This makes India the No. 2 buyer of Russian oil by value after China.

(3) *The Russian dilemma*. Another optics challenge for Russia hawks in Washington: Moscow has long been India’s main source for arms. Though New Delhi has diversified its military procurement to the US, France, and Israel, Russia remains a top supplier.

(4) *Modi’s Gujarat model.* Modi’s worse-than-advertised record as an economic reformer is catching up with Asia’s *third-largest economy*.

In 2014, Modi’s BJP won in an *electoral landslide* to retake power from Manmohan Singh’s Congress Party. Singh, an economist who led from 2004 to 2014, initially opened India to the business world in the 1990s when he was finance minister.

When Modi’s BJP returned to power in 2014, the plan was to kick the reform process into higher gear. Modi won on the strength of the folklore status he earned running the western state of Gujarat from *2001 to 2014*. He was widely credited with morphing the place into a free-market exemplar with fewer regulations, less corruption, stronger entrepreneurship, and faster GDP than the national average. Voters hired him to apply this “*Gujarat model*” to the broader Indian economy.

India’s Tariff Shock III: Time for Reform. Early on, Modi did just that. He had some big wins opening previously sacrosanct sectors like aviation, defense, and insurance to increased international investment. Moves to increase overseas access to pharmaceuticals, manufacturing, and retail even lured Walmart India's way.

A big driver of the appeal was Modi's "Make in India" push, which, along with Apple and Samsung, had Chinese smartphone *giants like Xiaomi* building plants in India. Yet Modi has been better at big, splashy deals and ribbon-cutting events than spreading the benefits of economic growth.

Here's more on how Modi's policies have set India up for the challenges it faces going forward:

(1) *Half measures*. A clear Modi pattern has been to grab low-hanging fruit reforms early and often and then pivot to other issues. These include silencing Indian media companies to limit criticism of his reform failures. Today, India *ranks 151st* in the annual Reporters Without Borders press freedom index (it was *140th in 2014*).

Too often, Modi has leaned on the Reserve Bank of India (RBI) to keep interest rates low to paper over government half measures. Financial markets are waiting with bated breath to see whether Trump's tariffs might prompt the RBI to *cut rates* on Wednesday (*Fig. 3*). But one former RBI governor in particular proved to be too independent for Modi's liking.

(2) *Thorn in Modi's side*. Raghuram Rajan was RBI governor from 2013 to 2016. The University of Chicago economist had an event-rich 2003-07 stint at the International Monetary Fund (IMF). He was among the first prominent economists to warn about the subprime crisis. In *August 2005*, he upset the crowd at the Federal Reserve's annual Jackson Hole gathering with talk of financial bedlam to come.

Modi opted not to give Rajan another term, shocking the financial markets. In September 2016, Modi replaced Rajan. Since then, Rajan, arguably India's most influential economic voice, has emerged as a thorn in Modi's side. At Davos in January, for example, Rajan warned that the economy needs fewer infrastructure-driven sugar highs and more job creation, especially among younger Indians.

"The problem is that [infrastructure] seems to be the primary engine of the growth," *Rajan said*. "Consumption, which was the other engine earlier, is faltering. Partly, because India needs many more jobs than what you are seeing. The biggest challenge for the government is to create those jobs across the board."

(3) *Time for reforms*. Rajan explained that “at the upper end, yes, jobs are plentiful. But at medium and lower levels, they are not. How do you get people out of agriculture? What do they go to? That is the big question."

The tariffs will make maximizing employment harder. They will, for example, complicate efforts to fight India’s next economic war: India’s biggest service-economy win over the last decade has been harnessing its huge English-speaking workforce to excel in business process outsourcing. These roughly *3 million jobs* in customer support, accounting, and software development could be at risk from artificial intelligence tools.

IMF Deputy Managing Director Gita Gopinath argues that “the *best thing* for India to do … is actually to focus on the domestic reforms.” Gopinath adds that “in terms of what prevents people from going into India, it is about still the ease of doing business, the infrastructure, the ability to buy land or sell land, and contract enforcement—those are the kinds of aspects that are more constraining factors. So, the more India does in terms of structural reforms at home … that will be what will change the story for India.”

(4) *Pre-existing conditions*. India needs more than pockets of success, economists agree. It needs a pivot toward creating tens of millions of jobs to ensure India’s young population—the so-called demographic dividend—doesn’t lead to mass discontent.

India’s pre-existing conditions are now coming to the fore just as extreme tariff pain awaits. Though the roughly 6.5% growth earmarked from 2025 sounds grand, it’s a long way from 8% needed to realize Modi’s 2047 ambitions as trade headwinds intensify.

Calendars

US: Tues: ISM NM-PMI 51.1; Trade Deficit $61.0b. **Wed:** MBA Mortgage Applications. (Source: FX Street)

Global: Tues: Eurozone, Germany & France C-PMIs 51.0, 50.3 & 49.6; Eurozone, Germany & France NM-PMIs 51.2, 50.1 & 49.7; France Industrial Production 0.2%; Spain Industrial Production; UK C-PMI & NM-PMI 51.0 & 51.2; China Caixin NM-PMI. **Wed:** Eurozone Retail Sales 0.3%m/m, 2.6%y/y; Germany Factory Orders 1.0%; Italy Industrial Output 0.1%. (Source: FX Street)

Strategy Indicators

S&P 500/400/600 Forward Earnings (*link*): During the August 1 week, forward earnings rose simultaneously for all three of these indexes for the ninth time in the 10 weeks since May 30. LargeCap's forward earnings rose for an 11th straight week in its longest winning streak since it did so for 12 weeks through late December, and has posted gains in 13 of the 15 weeks since it bottomed during the April 25 week. MidCap's rose for the tenth time in the 11 weeks since it bottomed during the May 16 week. SmallCap's has risen for ten straight weeks since it bottomed during the May 23 week, and is now on the longest winning streak since it did so nearly four years ago for 15 weeks through the December 17, 2021 week. LargeCap's forward earnings rose 0.3% w/w to its ninth straight record high. MidCap's rose 0.6% w/w to a 16-week high and is 0.8% below its record high during the April 4 week. SmallCap's rose 0.5% w/w to a 25-week high and is 11.6% below its June 2022 record. LargeCap's forward earnings has soared 26.9% from its 54-week low during the week of February 1, 2023; MidCap's is just 8.3% above its 55-week low during the week of March 10, 2023; but SmallCap's has lagged considerably and is up just 3.5% from a very recent 42-month low during the May 23 week. These three indexes' forward earnings downtrends from mid-2022 to early 2023 and again during Trump's Tarriff Turmoil were relatively modest compared to their deep double-digit percentage declines during the Great Virus Crisis and the Great Financial Crisis. Here are the latest consensus earnings growth rates for 2024, 2025, and 2026: LargeCap (9.7%, 9.1%, 13.8%), MidCap (0.4, 2.0, 17.9), and SmallCap (-10.2, 2.6, 19.4).

S&P 500/400/600 Valuation (*link*): Valuations were down w/w for all three of these indexes during the August 1 week. LargeCap's forward P/E fell 0.6pt w/w to a six-week low of 21.8 from a four-year high of 22.4. It's now 4.8pts above the seven-month low of 17.0 during the October 27, 2023 week. That compares to a 30-month low of 15.1 at the end of September 2022 and an 11-year low of 11.1 during March 2020. MidCap's forward P/E dropped 0.7pt w/w to a six-week low of 15.6 from a four-week high of 16.3. It's now 1.5pts below its 40-month high of 17.1 during the November 29 week and 3.4pts above the 12-month low of 12.2 in October 2023. That compares to a record high of 22.9 in June 2020 when forward earnings was depressed and an 11-year low of 10.7 in March 2020. SmallCap's forward P/E fell 0.7pt w/w to a nine-week low of 14.6 from 15.3, and is 1.0pt below its 20-week high of 15.6 during the July 4 week. It's 1.7pts above its 17-month low of 12.9 during the April 4 week and 4.0pts above its 14-year low of 10.6 in September 2022, but remains 1.8pts below its 41-month high of 17.1 during the November 29 week. That compares to a record high of 26.7 in early June 2020 when forward earnings was depressed, and a record low of

10.2 in November 2009 during the Great Financial Crisis. The forward P/Es for the SMidCaps have been mostly below LargeCap's since August 2018. MidCap's P/E is at a 28% discount to LargeCap's P/E, not much above its 25-year-low 29% discount during the July 5, 2024 week. That compares to a 19% discount during the March 2, 2023 week, which matched its best reading since October 14, 2021. SmallCap's P/E is at a 13-month-low 33% discount to LargeCap's P/E. That compares to a 23% discount during the November 29 week, which was its best reading since the March 2, 2023 week. It's now just 2ppts above its 24-year-low 34% discount during the July 5, 2024 week. SmallCap's P/E is also at a 13-month low 6% discount to MidCap's, up from a 20-year-low 10% discount in late 2021. Prior to that, from 2003 to 2018, SmallCap's P/E had been mostly above MidCap's, and both were above LargeCap's.

Contact us by *email* or call 480-664-1333.

Ed Yardeni, President & Chief Investment Strategist, 516-972-7683
Debbie Johnson, Chief Economist, 480-664-1333
Joe Abbott, Chief Quantitative Strategist, 732-241-6502
Melissa Tagg, Senior Global Investment Strategist, 516-782-9967
Mali Quintana, Senior Economist, 480-664-1333
Jackie Doherty, Contributing Editor, 917-328-6848
William Pesek, Contributing Editor, 516-277-2432
Valerie de la Rue, Director of Institutional Sales, 516-277-2432
Mary Fanslau, Manager of Client Services, 480-664-1333
Sandy Cohan, Senior Editor, 570-228-9102