Crisil Intelligence

RateView

CRISIL's outlook on near-term rates

February 2025

by S&P Global

Contents

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Crisil
Intelligence

January jostle

Yield on the 10-year benchmark government security (G-sec) opened at 6.78% and closed at 6.69%, down 7 basis points (bps) from its December close of 6.76% and within Crisil's forecast range of 6.69-6.79%.

The domestic bond market opened the month on a steady note, as traders covered short bets. Buying picked up following better-than-expected cut-off at the weekly G-sec auction, coupled with bullish market sentiment on hopes of a rate cut by the Reserve Bank of India Monetary Policy Committee (MPC) at its meeting in February 2025.Towards the closing session, a fall in the five-year overnight index swap (OIS) rates and news of change in United States (US) President Donald Trump's tariff plan aided gilt prices. Yield on the 10-year benchmark G-sec closed the first week at 6.75%.

At the start of the second week, bonds traded with a bearish sentiment due to a surge in US Treasury yields and rising OIS rates. A surge in US Treasury yields ahead of the non-farm payrolls data weighed on bond prices to some extent. A significant fall in the rupee to a record low against the dollar also weighed on the bond prices. In line with expectations, domestic Consumer Price Index (CPI) data did not lend any fresh direction. Gilts closed 5-10 bps weaker across the curve. The 10-year benchmark G-sec closed the week at 6.83%.

The third week started on a bullish note. The RBI's announcement of daily variable rate repo (VRR) auctions revived expectations of a policy rate cut in February 2025. Moreover, weaker-than-expected cut-off at the weekly auction weighed on bond prices. Traders also awaited clarity on tariffs under Trump 2.0. Consequently, trade volumes remained muted. The 10-year benchmark closed the week at 6.76%.

In the fourth week, domestic bonds traded with a positive bias, tracking an overnight decline in US-treasury yields. Moreover, expectations of lower gross borrowing for fiscal 2026 than 2025 kept market sentiment upbeat. With this, gilts closed 1-3 basis points stronger across the curve. RBI announced measures to infuse durable liquidity using open market operation (OMO) purchases and 56-day VRR auction. During the session, a rise in US treasury yields and profit booking by market participants weighed on the bond prices. Traders awaited the outcome of the US Federal Open Market Committee (FOMC) meeting outcome on January 29, 2025 and the Union Budget for fiscal 2026 on February 1, 2025, for further direction. The benchmark 10-year yield closed the week at 6.69%.

CRISIL's outlook

On interest rates

Benchmark	January 31, 2024 (A)	February 28, 2025 (P)	April 30, 2025 (P)
10-year G-sec yield*	6.69%	6.65%-6.75%	6.60%-6.70%
10-year SDL yield	7.09%	7.05%-7.15%	7.00%-7.10%
10-year corporate bond yield	7.18%	7.15-7.25%	7.15%-7.25%

A: Actual; P: Projected (6.79 GS 2034)
Source: CRISIL MI&A Research

One-month view

In February, domestic G-sec yields are likely to be influenced by various factors such as the Union Budget, foreign portfolio investor (FPI) inflows and outflows, MPC meeting, movement in crude oil prices and the impact of rupee-dollar moves on the debt market.

Gilt movement in the month of February till date –

Domestic bonds traded with a bullish bias, tracking an overnight decline in US treasury yields. Additionally, likely buying from foreign investors and some easing in banking system liquidity aided bond prices. Expectations of a rate cut by the MPC at its meeting this month supported short-term securities. After the MPC cut the repo rate by 25 bps but retained the policy stance at its meeting, domestic bond yields rose 3-4 bps as the committee did not announce any additional liquidity measures. The RBI announced it will double the size of its open market operation (OMO) purchase to Rs 40,000 crore in February, up from Rs 20,000 crore announced earlier. The move aims to ease the persistent liquidity deficit in the banking system.

Note: All yields are volume-weighted averages during the last trading hour of that day

Three-month view

Movement in the 10-year G-sec yield is expected to depend on FPI flows, crude oil prices, global interest rate environment, the CPI inflation print, FOMC's decisions, global cues and liquidity concerns.

Framework for the outlook

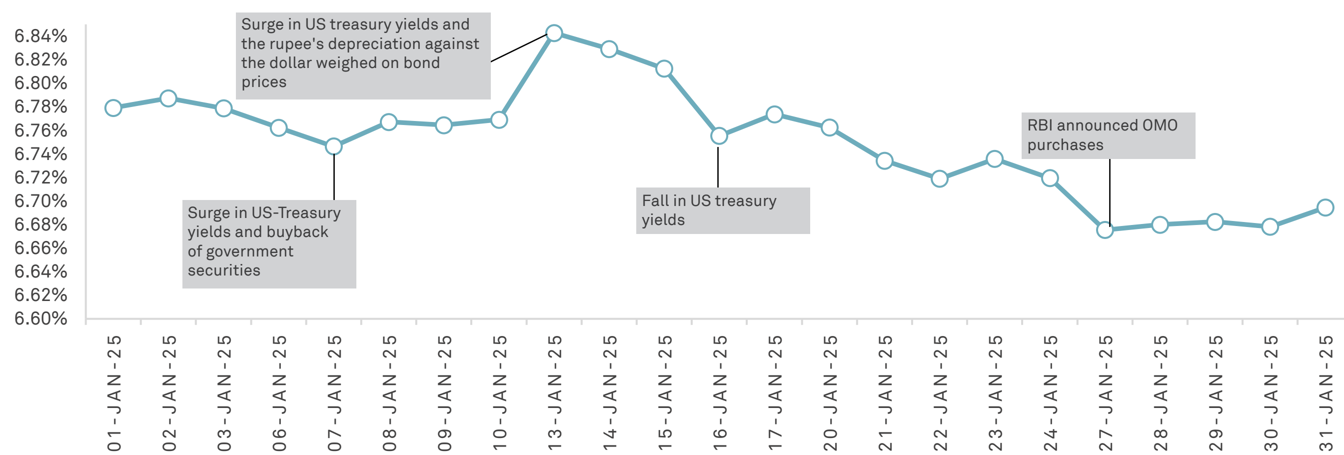
Crisil provides its outlook on key benchmark rates for different debt classes — 10-year G-secs, state development loans (SDLs) and corporate bonds (CBs) — based on statistical models and inputs from our in-house experts. We also incorporate our views on policy expectations, the macroeconomic outlook, key events (local and global) and market factors (liquidity and demand/supply).

Factors influencing the outlook

Economic parameter	Our view	Impact on yields
Gross domestic product (GDP) growth	• We expect GDP growth at 6.5% in fiscal 2026, mildly up from an estimated 6.4% this fiscal • Income tax cuts, softer inflation (assuming normal monsoon and lower crude oil prices) and the RBI's rate cuts are expected to lift growth next fiscal. The budget will be mildly supportive of growth, though overall fiscal impulse will moderate with fiscal consolidation. That said, exports face headwinds from tariff hikes initiated by the US • GDP grew 5.4% on-year in the second quarter of fiscal 2025, a sharp deceleration from the 6.7% in the first quarter	↓
Consumer price index (CPI) inflation	• We expect consumer price index (CPI)-linked inflation to soften to 4.4% in fiscal 2026 from our estimate of 4.7% in fiscal 2025 • Inflation is likely to move closer to the RBI's target of 4% in fiscal 2026 on expectations of a normal monsoon, high base effect in food inflation and softer global commodity prices. Some uptick is expected in non-food inflation due to an adverse base, but it is expected to remain in comfort zone • CPI inflation moderated to 5.2% in December from 5.5% the previous month.	↓
RBI's monetary policy	• We expect ~75-100 bps of rate cuts in the current easing cycle. However, US tariff hikes, moderating US Federal Reserve rate cuts and weather-related risks will have bearing on the rate cutting cycle. This rate cut cycle will be lesser than the previous rate cut of 225 bps during the pandemic. • Given the expected easing of inflation, the RBI has space to support growth. Continuing fiscal consolidation has further paved way for monetary easing. But geopolitical events and weather shocks remain risks • The Reserve Bank of India's (RBI) Monetary Policy Committee (MPC) cut policy rates by 25 bps in February, a first since May 2020. However, the MPC maintained its neutral stance, which gives it flexibility to remain data-dependent and respond to any global shock.	↓
Fiscal health	• The budget has targeted a reduction in centre's fiscal deficit to 4.4% of GDP in fiscal 2026 from 4.8% of GDP in fiscal 2025 • It aims to do this via a moderation in revenue expenditure (pensions, food and fertiliser expenditures have decreased as a share of GDP), even as the capex's share in GDP is maintained. On the receipts front, expectations on strong tax collections and a large dividend from the RBI will help • Gross market borrowing is estimated at Rs. 14.8 lakh crore for fiscal 2026, 5.8% higher on-year.	↓
Crude oil prices	• We expect crude prices average $70-$75 per barrel range in fiscal 2026 compared to an average of $79.8 per barrel in fiscal 2025 so far (Apr-Jan average). • Brent crude oil prices increased to $79.2 per barrel average in January, 7.3% higher on-month but 1.3% lower on-year.	↔

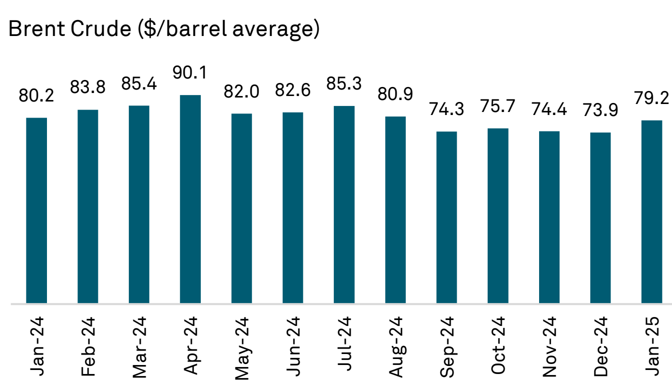
Economic parameter	Our view	Impact on yields
Current account balance	• We expect the current account deficit (CAD) to average ~1.3% of GDP in fiscal 2026 compared to an estimated 1.0% of GDP in fiscal 2025. • CAD is expected to increase owing to headwinds to exports from US tariff policies. Lower crude oil prices, healthy services trade balance and robust remittances growth will prevent CAD from widening too much • India's current account recorded a deficit of 1.2% of GDP in the second quarter of fiscal 2025 vs a deficit of 1.1% of GDP in the previous quarter.	↑
US Federal Reserve's stance	• S&P Global expects the Fed to cut rates more gradually than previously expected. They now expect only one rate cut in the first half of 2025 (calendar year), followed by a pause until the second half of 2026 compared to their previous forecast of 75 bps of rate cuts by the end of 2025 • The Fed kept its policy rate at 4.25-4.5% at its January meeting. The Fed has cut rates by a cumulative 100 bps in this easing cycle so far.	↓
Liquidity indicators **i) Demand & Supply**	**Supply:** • To finance the fiscal deficit, net market borrowing from dated securities is pegged at Rs 11.54 lakh crore. The balance financing is expected to come from small savings and other sources. Gross market borrowing is estimated at Rs 14.82 lakh crore • Additional borrowing of 0.5% of gross state domestic product (GSDP) will be allowed to states. • For January, the actual SDL borrowing was Rs 88,919 crore, compared with the budgeted borrowing of Rs 1,47,057 crore • An outlay of Rs 1.5 lakh crore is proposed for the 50-year interest free loans to states for capital expenditure and incentives for reforms **Demand:** • Continued demand from insurance companies and pension funds for the longer end curve in SDLs and corporate bonds	↑
ii) Call rates/LAF (liquidity adjustment facility)	• The Indian banking system encountered its worst liquidity crunch in more than a decade in January 2025. The liquidity deficit peaked at Rs 3.15 trillion on January 23, its lowest level in nearly 15 years. As was the case in the preceding month, tax outflows, GST payments and the RBI's forex interventions to stabilize the rupee and currency in circulation (CIC) outflows significantly impacted cash flows in the banking system. The deficit led to increased dependence by banks on market borrowing, thereby keeping interbank call money rates consistently above the policy repo rate of 6.50%. The WACR averaged at 6.61% during the month till January 31, 2025. • The central bank resorted to several measures during the course of the month to inject liquidity into the system, including several variable rate repo (VRR) auctions of varying tenors and a series of daily VRR auctions conducted between January 16 and January 23. As the month drew to a close, the RBI also announced additional measures, such as a $5 billion USD/INR buy/sell swap on January 31, as well as open market operations (OMO) purchase auctions of government securities aggregating Rs 60,000 crore and a 56-day VRR auction scheduled in February, to help overcome the tightness in liquidity.	↓

January at a glance



Source: Crisil Intelligence

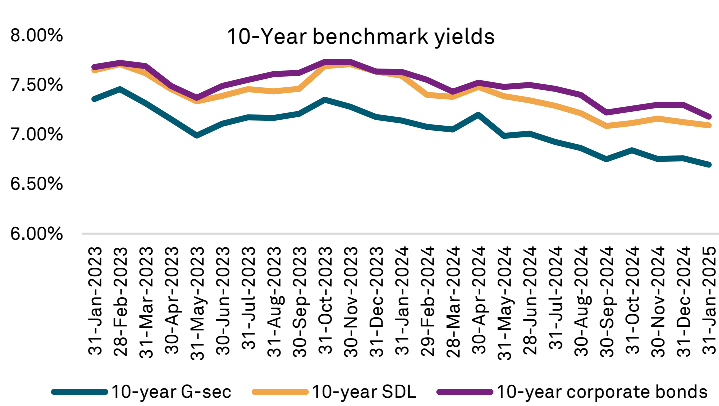
Crude oil prices increased in January



Brent crude oil prices rose to $79.2 per barrel on average in January, up 7.18% on-month. This increase was mostly driven by tougher US restrictions on Russian and Iranian oil exports, which reduced global supply.

Source: Crisil Intelligence

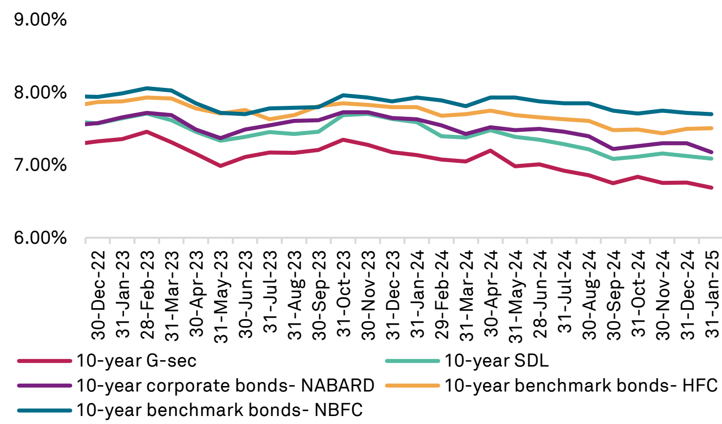
Benchmark SDL yield and corporate bond (PSU FI) yield eases



Yield on the 10-year benchmark G-sec closed at 6.69% in January, down 7 bps from the previous month's close. The yield on the 10-year SDL eased 3 bps to 7.09% and that on the 10-year corporate bond (10-year PSU FI) closed at 7.18%, down ~12 bps.

Source: Crisil Intelligence

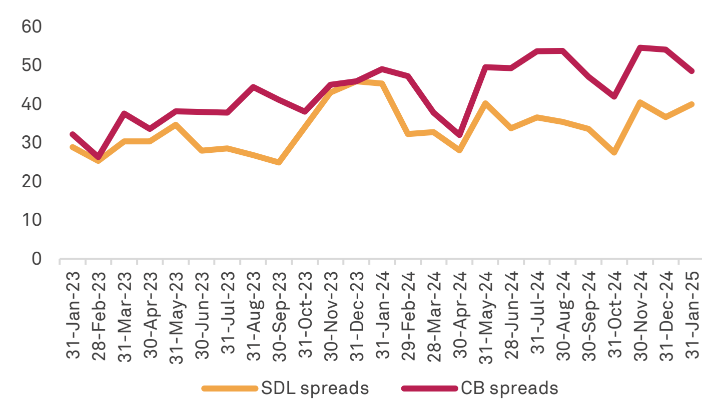
10-year G-sec/SDL/corporate bond benchmark yields



Source: Crisil Intelligence

Yield on a 10-year AAA-rated PSU bond fell to 7.18% from 7.30%. SDLs ended January at 7.09%, down from 7.13% in December. Yields on bonds issued by housing finance companies (HFCs) marginally inched up to 7.51% from 7.50% the previous month, while the same non- banking financial companies (NBFCs) closed at 7.70% down from 7.72% in December.

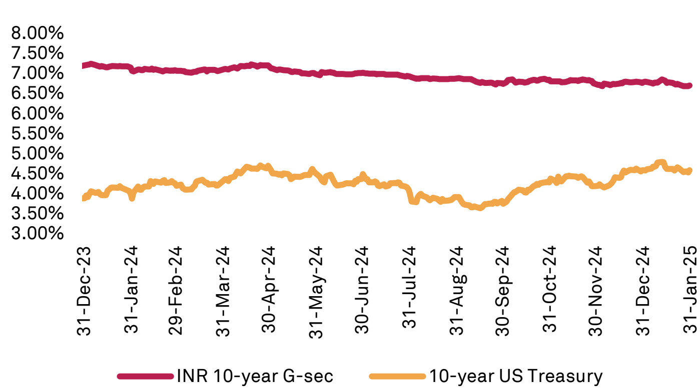
Corporate bonds and SDL yield spreads over 10-year benchmark G-sec yields



Source: Crisil Intelligence

The spread on the 10-year benchmark SDL over the 10-year benchmark G-sec closed at ~40 bps in January, up ~3 bps from the previous month's close. Meanwhile, the spread on the 10-year AAA-rated public sector corporate bonds (PSU FI) closed at ~49bps, down ~6 bps. The 12-month average spreads on the 10-year benchmark SDL and PSU FI over the 10-year benchmark G-sec were ~35 bps and ~47 bps, respectively.

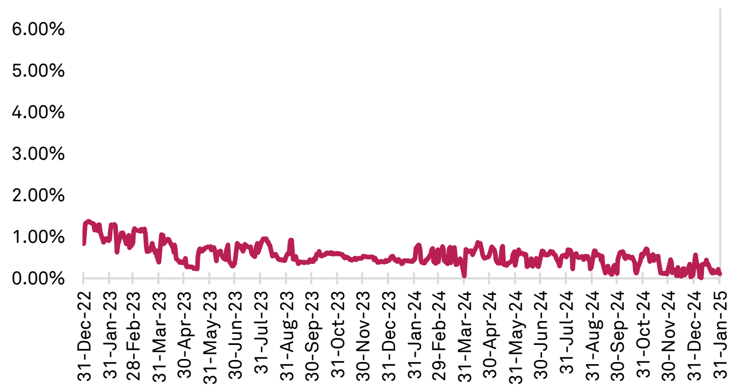
US Treasury and G-sec yield trajectory



Source: Crisil Intelligence

US Treasury yields ended at 4.58% in January, unchanged from December's close of 4.58%. The monthly spread between the domestic benchmark 10-year G-sec and the 10-year US Treasury yield narrowed to 211 bps in January 2025.

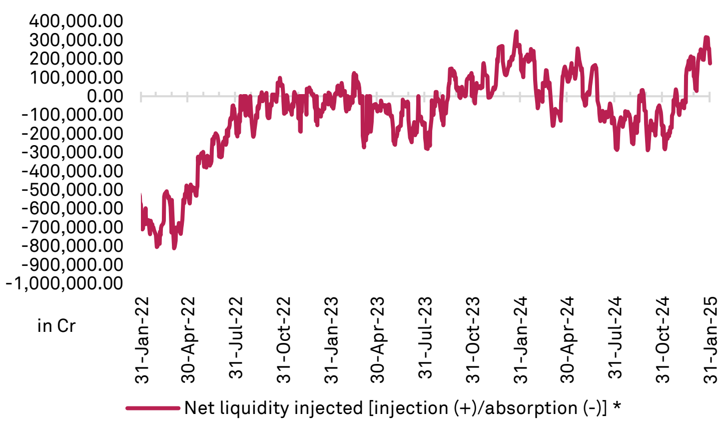
Term premium between 10-year benchmark G-sec and TREPS



Source: Crisil Intelligence

The average spread between the 10-year benchmark G-sec yield and the tri-party repo (TREPS) is ~24 bps in January 2025 as against ~19 bps in the previous month. The 12-month average spread was ~45 bps.

Systemic liquidity



**Spreads are for five-year securities over the annualised G-sec yield; selection of representative issuers has been re-evaluated as per the periodic review*
Source: Crisil Intelligence

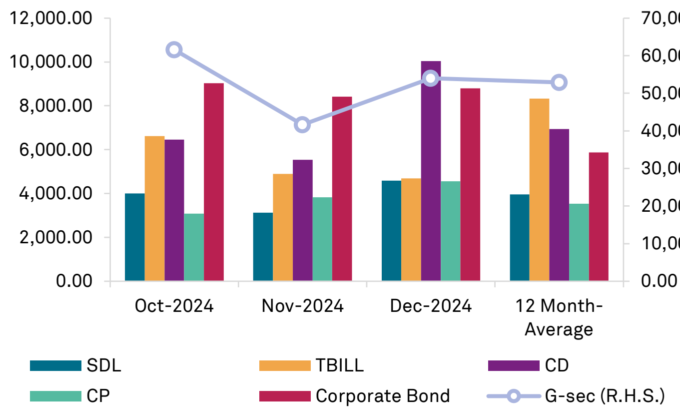
The average systemic liquidity deficit was ~Rs 2.03 lakh crore in January 2025, as against Rs 0.64 lakh crore in December. The average liquidity over the past 12 months was Rs 0.027 lakh crore. The liquidity in the month of January peaked at Rs 3.15 trillion lowest in nearly 15 years due to tax outflows, GST and RBI's forex interventions to stabilize the rupee. RBI to manage this deficit had announced daily VRR auctions totalling to Rs 1.65 lakh crore for the month of January.

Benchmark spreads over G-secs

Spreads over G-sec*				
Rating category	**Date**	**PSUs/ corporates**	**NBFCs**	**Housing finance companies**
AAA	31-Dec-24	0.64%	0.94%	0.86%
	31-Jan-25	0.61%	0.95%	0.84%
AA+	31-Dec-24	0.94%	1.41%	1.42%
	31-Jan-25	0.93%	1.43%	1.38%
AA	31-Dec-24	1.21%	2.35%	1.90%
	31-Jan-25	1.26%	2.30%	1.92%
AA-	31-Dec-24	2.07%	3.23%	2.68%
	31-Jan-25	2.03%	3.25%	2.71%

**Spreads are for five-year securities over the annualised G-sec yield; selection of representative issuers has been re-evaluated as per the periodic review*
Source: Crisil Intelligence

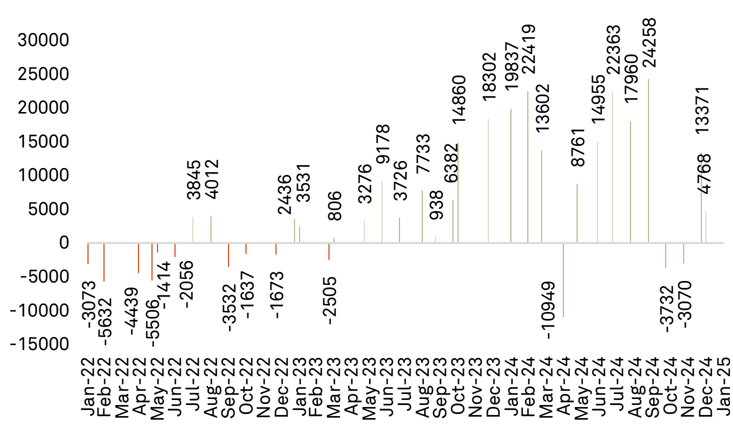
Trading volume decreased across securities except T-bills and G-sec



Source: Crisil Intelligence

In January, trading volume in G-secs increased 12.76% on-month, while that in SDLs declined 20.32%. Trading volume in commercial papers (CPs), certificates of deposit (CDs) and corporate bonds (CBs) decreased 45.74%, 29.24% and 29.28%, respectively. T-bill volumes increased 16.68%.

FPIs turn net buyers



Source: Crisil Intelligence

Net FPI inflow into the debt market was Rs 4,768 crore in January versus an inflow of Rs 13,371 crore in December. FPIs were net sellers in equity and net buyers in debt markets during the month.

Rating upgrades and downgrades in January 2025

Upgrades

Issuer name	Old rating	New rating
IKF Home Finance Ltd	CARE A-	CARE A
Precot Ltd	IND BBB	IND BBB+
TVS Holdings Ltd	CRISIL AA	CRISIL AA+
Karnataka Bank Ltd	[ICRA]A	[ICRA]A+
UCO Bank	CARE AA-	CARE AA
Indian Overseas Bank	IND AA-	IND AA
Dhruva	[ICRA]AA+(SO)	[ICRA]AAA(SO)
Central Bank of India	CRISIL AA-	CRISIL AA
Jana Capital Ltd	IND BB-	IND BB
Jana Small Finance Bank Ltd	IND A-	IND A

Downgrades

Issuer name	Old rating	New rating
Midland Microfin Ltd	ACUITE A-	ACUITE BBB+
Ananya Finance for Inclusive Growth Pvt Ltd	ACUITE BBB	ACUITE BBB-
Jodhpur Vidyut Vitran Nigam Ltd	CARE BBB+(CE)	CARE BBB(CE)
Jaipur Vidyut Vitran Nigam Ltd	CARE BBB+(CE)	CARE BBB(CE)
Ajmer Vidyut Vitran Nigam Ltd	CARE BBB+(CE)	CARE BBB(CE)

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