Market Intelligence
& Analytics

CRISIL
An S&P Global Company

RateView

CRISIL's outlook on near-term rates

September 2024

Research

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August affairs

The yield on the 10-year benchmark government security (G-sec; 7.10% GS 2034) closed August at 6.86%, down 6 basis points (bps) from the previous month's close of 6.92% and below CRISIL's forecast range of 6.88-6.98%.

Domestic bond prices started the month with a positive bias, tracking a sharp fall in US Treasury yields amid weaker-than-expected US non-farm payrolls data and fears about a US recession. However, US Treasury yields surged as the fears subsided, weighed on domestic bonds. The Reserve Bank of India's (RBI) Monetary Policy Committee (MPC) kept its policy rates unchanged for the ninth consecutive time in its August policy meeting. Further, liquidity in the system remained in surplus at Rs 1.46-2.86 lakh crore, prompting the central bank to conduct multiple variable-rate reverse repo (VRRR) auctions to manage the surplus. The yield on the 10-year benchmark government security (G-sec; 7.10% GS 2034) closed the week down 4 basis points (bps) at 6.88%.

During the second week, domestic bonds traded in a narrow range as traders avoided aggressive bets amid a raft of economic data releases from India and the US, including CPI, India WPI and US PPI. The 10-year US Treasury yield eased 5 bps to close the week at 3.89%, following softer-than-expected US producer price inflation data for July 2024. The cut-offs at the RBI's weekly gilt auction were as expected and failed to lend fresh direction. Yield on the 10-year benchmark G-sec (7.10% GS 2034) closed the week at 6.87%, down 1 bp from the previous week.

During the second half of the month, domestic bonds traded in a narrow price range amid lack of firm domestic as well as global cues. Liquidity surplus continued and the RBI conducted multiple VRRR auctions. The yield on the 10-year benchmark government security closed the month at 6.86%, 6 bps down from its previous close of 6.92%

In its third bi-monthly meet for this fiscal, as mentioned above, the MPC kept its policy rate unchanged at 6.50%. The RBI Minutes of the Monetary Policy Committee Meeting were broadly in line with market expectations, wherein RBI maintained status quo, flagging concerns over food inflation.

CRISIL's outlook

On interest rates

Benchmark	August 31, 2024 (A)	September 30, 2024 (P)	November 30, 2024 (P)
10-year G-sec yield*	6.86%	6.75% - 6.85%	6.73% - 6.83%
10-year SDL yield	7.22%	7.10% - 7.20%	7.10% - 7.20%
10-year corporate bond yield	7.40%	7.29% - 7.39%	7.31% - 7.41%

A: Actual; P: Projected; SDL: State development loan
Source: CRISIL MI&A Research

One-month view

In September, domestic G-sec yields are likely to be influenced by factors such as foreign portfolio investor (FPI) flows, crude oil price movements, the Federal Open Market Committee (FOMC) meeting and domestic inflows into the debt market.

Three-month view

The 10-year G-sec yield is expected to hinge on FPI flows, crude prices, global interest rates, the CPI inflation print, policy decisions of the RBI's MPC and the FOMC and the US presidential elections.

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 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).

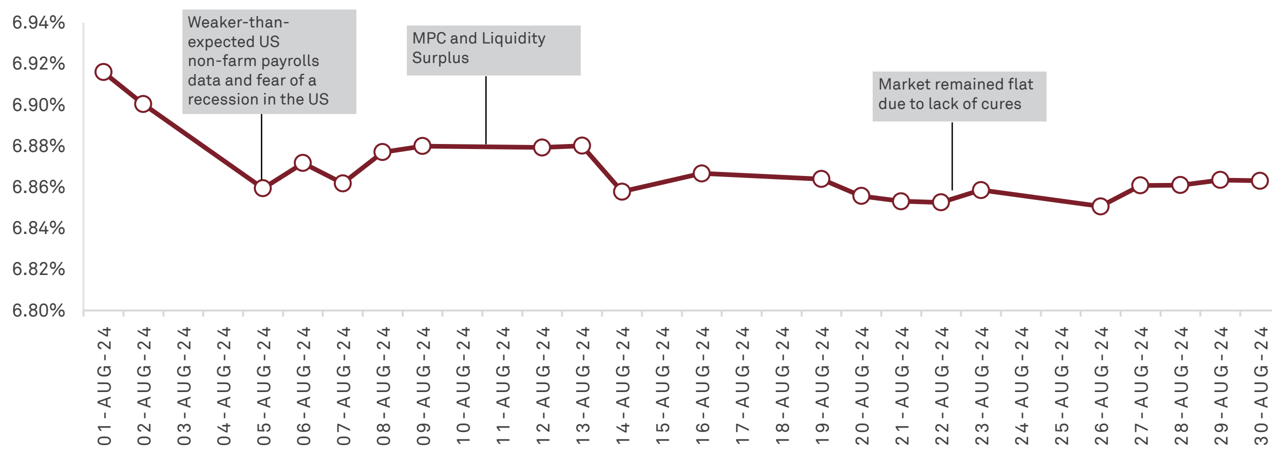
Note: All yields are volume-weighted averages during the last trading hour of that day

Factors influencing the outlook

Economic parameter	Our view	Impact on yields
Gross domestic product (GDP) growth	• We expect real GDP growth to moderate to 6.8% in fiscal 2025 from 8.2% in the previous fiscal. • High interest rates and lower fiscal impulse (from a reduction in the fiscal deficit) will weigh on growth. But growth will become more balanced as the last year's laggard segments — agriculture and private consumption — are poised to rise. Higher rural demand and easing food inflation are expected to lift consumption. • Real GDP growth moderated to 6.7% on-year in the first quarter of fiscal 2025, from 7.8% in the previous quarter.	↓
Consumer price index (CPI) inflation	• We expect consumer price index (CPI)-linked inflation to soften to 4.5% in fiscal 2025, from 5.4% in the previous fiscal. • Given the improved agricultural outlook for this year, we expect food inflation to soften. The monsoon has progressed well and kharif sowing is up 1.9% on-year as on September 2. Non-food inflation could see a statistical uptick but is expected to remain soft overall on the back of benign commodity prices. • CPI inflation eased sharply to 3.5% in July from 5.1% in June.	↓
RBI's monetary policy	• We expect two policy rate cuts by the RBI this fiscal, starting October 2024 at the earliest. • Inflation remains a key gauge for the MPC's decision, and rate cuts will mainly depend on durable easing of CPI inflation to the MPC's target of 4%. Inflation eased sharply in July, driven by a supportive base, but that support could fade soon. That said, better monsoon and higher kharif sowing versus last year are expected to ease food inflation this fiscal • The MPC kept its policy rates unchanged in its August meeting, while maintaining its stance of withdrawal of accommodation.	↓
Fiscal health	• The Budget has targeted a reduction in the central government's fiscal deficit to 4.9% of GDP in fiscal 2025 from 5.6% of GDP past fiscal. • In the first four months of this fiscal, the Centre's fiscal deficit was 17.2% of the Budget target, compared with 33.9% in the same period last year. Capital expenditure as a proportion of the Budget target has been lower relative to last year. • Gross market borrowing is estimated at Rs 14 lakh crore for fiscal 2025, 9.2% lower on year.	↓

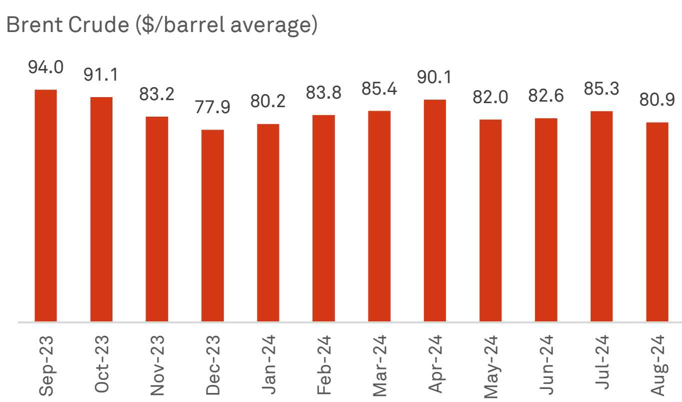
Economic parameter	Our view	Impact on yields
Crude oil prices	• We expect crude prices average $80-$85 per barrel range in fiscal 2025 compared to an average of $83 per barrel previous fiscal. • Brent crude oil prices reduced in August to $80.9 per barrel average, 5.2% lower on-month and 6.2% lower on-year.	↔
Current account balance	• We expect the current account deficit (CAD) to average 1.0% of GDP in fiscal 2025, compared with 0.7% of GDP in fiscal 2024. • Goods exports are expected to remain benign or rise moderately, given the uncertain and subdued global environment. At the same time, imports may continue to rise, given healthy domestic economic momentum, especially the uptick in consumption demand this fiscal. As a result, trade deficit is expected to widen and put some pressure on CAD. That said, healthy services trade surplus and remittances would keep a tab on CAD. • India's current account recorded a surplus of 0.6% of GDP in the fourth quarter of fiscal 2024 as against a deficit of 1.0% of GDP in the third quarter.	↑
US Federal Reserve's stance	• S&P Global expects the Fed to start cutting rates in September 2024, compared with their earlier forecast of December. • The Fed kept its policy rate unchanged at 5.25-5.50% for the eighth consecutive time at its July meeting.	↓
Liquidity indicators **i) Demand & Supply**	**Supply:** • For August, the actual SDL borrowing was Rs 89,190 crore, compared with the budgeted borrowing of Rs 88,740 crore. • Increase in CD issuances in the month of August, to meet the mismatch between assets and liabilities amidst falling deposits, additionally, sluggish deposit growth, and, shift in retail investments led to surge in CD issuances. **Demand:** • Increase in demand for longer tenure SDLs by insurance and pension players.	↔
ii) Call rates/LAF (liquidity adjustment facility)	• Liquidity in the Indian banking system remained in surplus for the second month in a row in August. Higher government spending pushed it towards a one-year high during the first half of the month. Accordingly, the weighted-average overnight money market rates briefly traded below the standing deposit facility (SDF) rate. Nonetheless, the RBI resorted to multiple VRRR auctions on almost all days of the month to mop up the excess liquidity. Eventually, August ended with the interbank weighted-average call rate (WACR) averaging at 6.52%, close to the RBI's repo rate of 6.50%.	↑

August at a glance



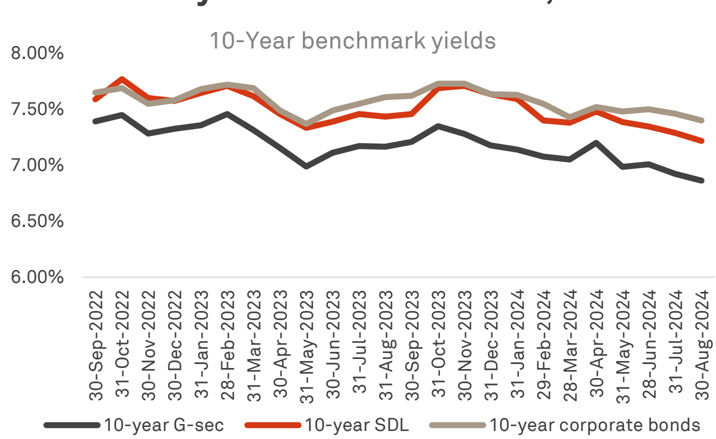
Source: CRISIL MI&A Research

Crude oil prices slip in August



Brent crude prices decreased 5.5% on-month to $80.9 per barrel on average in August.

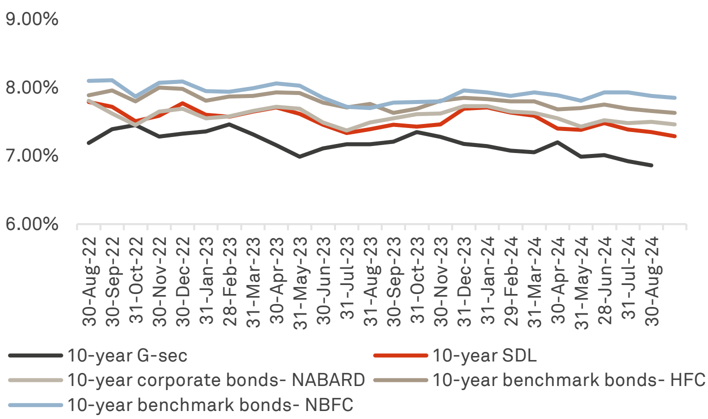
Benchmark yields ease for SDLs, G-secs and CBs



The yield on the 10-year benchmark G-sec closed at 6.86% in August, down 6 bps from the previous month's close. The yield on the 10-year SDL eased 7 bps to 7.22% and that on the 10-year CB (10-year PSU FI) eased 6 bps to 7.40%.

Source: CRISIL MI&A Research

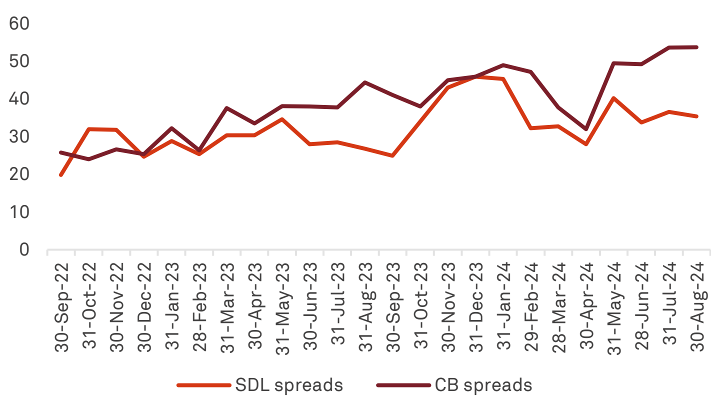
10-year G-sec/SDL/CB benchmark yields trend lower



Source: CRISIL MI&A Research

Yields on 10-year benchmark AAA-rated public sector undertaking (PSU) bonds decreased to 7.40% from 7.46% in July. Yields for housing finance companies also declined, closing at 7.61% against the previous month's close of 7.63%. Meanwhile, yields of AAA-rated non-bank financial companies (NBFC) remained flat at 7.85%.

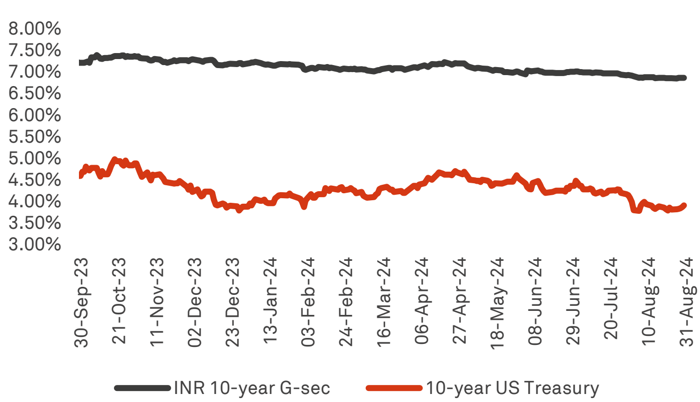
CB and SDL spreads over 10-year benchmark G-secs hold steady



Source: CRISIL MI&A Research

The spread on the 10-year benchmark SDL over the 10-year benchmark G-sec closed at 35 bps in August, down 1 bps from the previous month's close, while that on the 10-year AAA-rated public sector CB remained flat at 54. The 12-month average spreads on the 10-year benchmark SDL and CB over the 10-year benchmark G-sec were ~36 bps and ~45 bps, respectively.

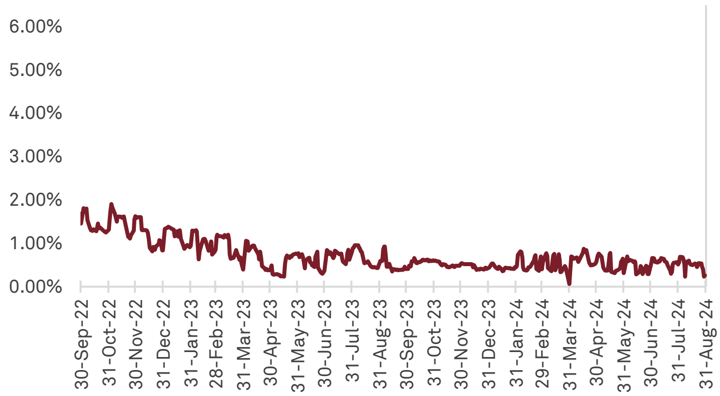
US Treasury yields dive



Source: CRISIL MI&A Research

The 10-year US Treasury yields dropped sharply after a weaker-than-expected jobs report heightened concerns over slowing economic growth. Yields ended at 3.91%, down 18 bps from the previous month's close. As a result, the monthly spread between the domestic benchmark 10-year G-sec and the 10-year US Treasury yields narrowed to 295 bps.

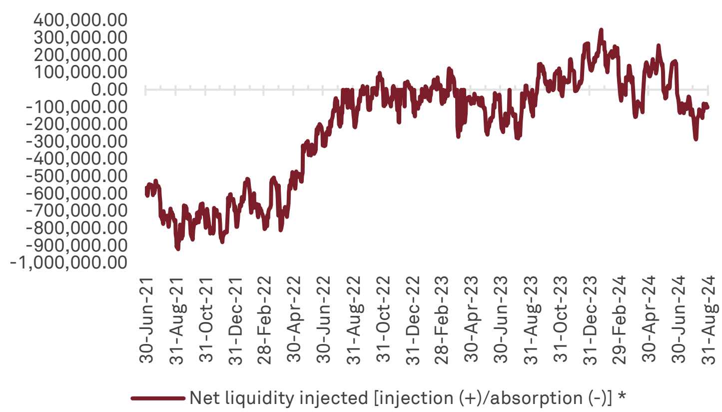
Term premium between 10-year benchmark G-sec and TREPS narrows



Source: CRISIL MI&A Research

The average spread between the 10-year benchmark G-sec yield and the tri-party repo (TREPS) decreased to ~50 bps in August from ~55 bps in the previous month. The 12-month average spread was ~52 bps.

Systemic liquidity improves



**Net liquidity is calculated as repo + marginal standing facility + standing liquidity facility - reverse repo*
Source: CRISIL MI&A Research

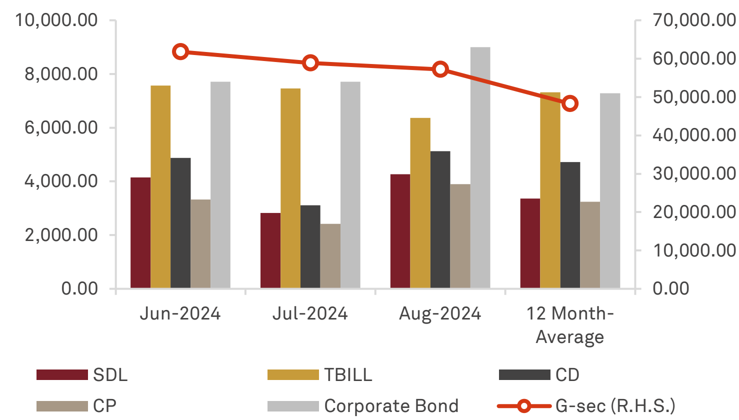
The average systemic liquidity surplus was ~Rs 1.49 lakh crore in August compared with ~Rs 1.02 lakh crore in July. The average liquidity over the past 12 months was Rs 0.49 lakh crore.

Benchmark spreads over G-secs

Spreads over G-sec*				
Rating category	**Date**	**PSUs/ corporates**	**NBFCs**	**Housing finance companies**
AAA	31-Jul-24	0.57%	1.02%	0.80%
	31-Aug-24	0.60%	1.04%	0.85%
AA+	31-Jul-24	0.97%	1.46%	1.35%
	31-Aug-24	0.98%	1.55%	1.44%
AA	31-Jul-24	1.13%	2.48%	1.93%
	31-Aug-24	1.16%	2.55%	2.02%
AA-	31-Jul-24	2.13%	3.51%	2.60%
	31-Aug-24	2.17%	3.51%	2.79%

**Spreads are for 5-year securities over the annualised G-sec yield; selection of representative issuers has been re-evaluated as per the periodic review*
Source: CRISIL MI&A Research

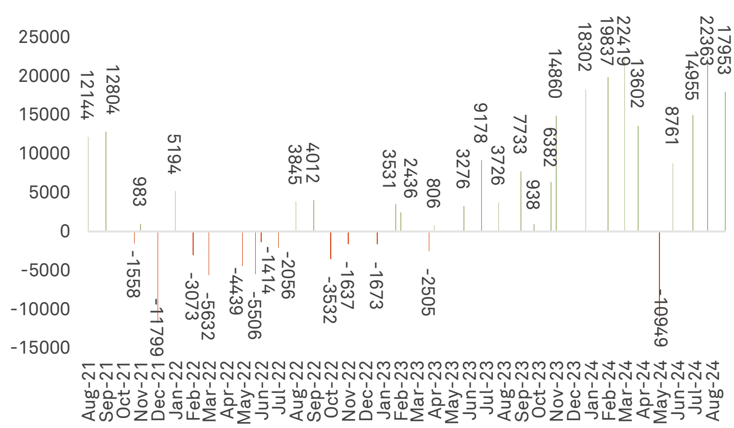
Trading volume increases across securities, except T-bills and G-secs



Source: CRISIL MI&A Research

In August, trading volume of G-secs declined 2.88% on-month, while that of SDLs increased 51.14%. Trading volume of T-bills declined 14.70%, while for Certificates of Deposit (CDs), Commercial Papers (CPs) and CBs it increased 64%, 61.25%, and 16.55%, respectively.

FPIs continue to be net buyers



Source: CRISIL MI&A Research

FPI inflows stayed positive for the month of August at Rs 17,953 crores. The positive outlook for Indian bonds was bolstered by the country's consistent economic performance. This was mainly due to the inclusion of Indian government bonds in the JP Morgan Government Bond Index-Emerging Markets and low US bond yields, which relieved pressure on Indian markets. Meanwhile, weaker-than-expected US employment data and hints of a potential economic slowdown have raised the possibility of rate cuts by the US Federal Reserve. Such developments have made Indian markets more lucrative to investors, resulting in FPIs being net buyers in August.

Rating upgrades and downgrades in August 2024

Upgrades

Issuer name	Old rating	New rating
IDBI Bank Ltd	[ICRA]AA-	[ICRA]AA
Indian Overseas Bank	CARE AA-	CARE AA
Aditya Birla Sun Life Insurance Co Ltd	CRISIL AA+	CRISIL AAA
Namra Finance Ltd	ACUITE A-	ACUITE A
Arman Financial Services Ltd	ACUITE A-	ACUITE A
Chaitanya India Fin Credit Pvt Ltd	IND A	IND AA-
GIC Housing Finance Ltd	[ICRA]AA	[ICRA]AA+
Yes Bank Ltd	CRISIL A	CRISIL A+
Karnataka Bank Ltd	CARE A	CARE A+
The Jammu & Kashmir Bank Ltd	IND A+	IND AA-
Aviom India Housing Finance Pvt Ltd	ACUITE BBB+	ACUITE A-
Bank of India	ACUITE AA	ACUITE AA+
Hindustan Construction Co Ltd	CARE BB	CARE BB+

Downgrades

Issuer name	Old rating	New rating
Finstars Capital Ltd	ACUITE BBB-	ACUITE BB+
SBM Bank (India) Ltd	CARE A+	CARE A
IREP Credit Capital Pvt Ltd	CARE BBB	CARE BBB-

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