

ECONOMY & GILT WATCH



(Subsidiary of Punjab National Bank)

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RBI Rate Cut Trajectory

RBI has started the rate cutting cycle with equal focus on keeping system awash with liquidity to support growth. The central bank remains cognizant of the risks abroad and has responded appropriately, it does seem that in an increasingly inward looking world the Central Bankers are keen on supporting growth. Downward trending inflation has helped RBI to decisively focus on domestic growth.

What remains to be seen is the quantum of future cuts and guidance by the central bank. Rates markets are currently pricing in two more cuts by the RBI, which takes the terminal rate to 5.50%. The growing uncertainty makes it increasingly difficult to gauge the timing of the incoming cuts than the quantum of cuts. Japanese and US bond markets have been shaken by weaker demand in auctions and growing fiscal concerns in these leveraged economies. Factors that are likely to determine the Rate Cut trajectory can be summed up below:

- **Inflation:** A good monsoon along with benign energy prices can spur RBI to cut rates faster. In addition, as and when growth picks up RBI may update the tolerance bank of inflation for the rate-cutting period.
- **Trump Tariffs:** The trade negotiations are still a work in progress but if the base tariffs materials then the impact on world growth and imported inflation remains to be seen.
- **Geopolitics:** Escalating war in Middle East and ongoing stalemate in Ukraine makes India prone to commodities price shock induced inflation shocks and that can affect the timing if not quantum of cuts.
- **Global Bonds :** If a selloff in Developed Market bonds especially USTs and JGBs is to happen that can put the rate cutting cycle on hold or stop the cut cycle in a scenario where world bond yields spike.

RBI Rate Cut Trajectory

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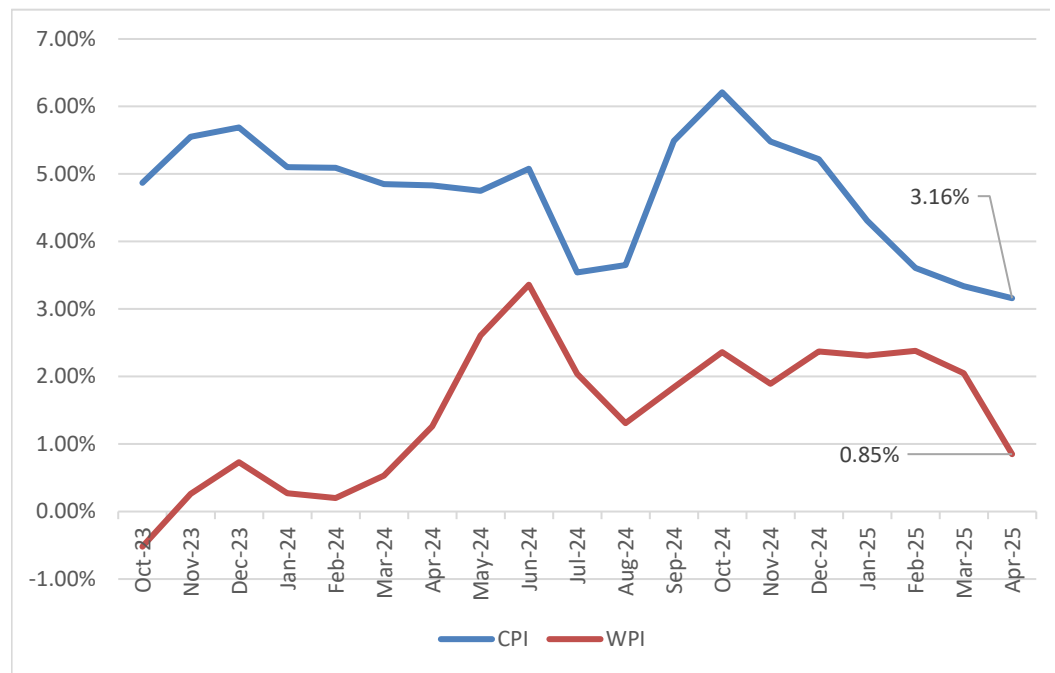
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RBI is expected to remain dovish/ cautious

Inflation update

India's retail inflation decreased to a six-year low of 3.16 percent in April 2025, down from 3.34 percent in March, as food price pressures eased, according to government data released on Wednesday. The inflation has been comfortably below the lower end of RBI targeted band of 4-6 percent for three consecutive months. Falling inflation can largely be attributed to the cooling in food prices.

Food inflation in April was 1.78 per cent, lower than 2.69 per cent in the preceding month and 8.7 per cent in the year-ago month. On the other hand, India's industrial activity slowed to an 8-month low figure of 2.7% in April against 3.9% in March. Meanwhile, India's WPI plummeted to 0.85% driven by a slowdown in the fuel prices.



Fixed Income Outlook

Fundamental View

Indian bonds are expected to trade with a bullish bias going forward with RBI in full control and actively managing liquidity. The 10Y paper is likely to trend higher finding a floor at 6-6.10% in yield terms. In case of RBI sounding cautious in its June policy, markets are likely to turn from bullish to sideways sentiment. Things look bright on the growth-inflation dynamic front but unease in Global Bond Markets pose serious challenges going forward. With Japan and UK trimming their long tenure borrowings and moving to short tenures, the panic can now spread across the curve considering weak fiscal positions.

Yields to trend down and settle later

On the global front, weak commodities prices continue to support the inflation at home and the deficit figure. Weakening of dollar has lifted sentiment for INR with RBI having replenished its reserves back to 680 Billion levels having faced a 10 percent drawdown. Going forward, both bonds and currency are likely to remain stable with risks arising out of aforementioned external risks to be managed proactively by RBI with increased buffer of currency reserves and an accommodative stance by the RBI.

SDL Overview

Last fortnight, CG benchmark 10 Yr traded in a range of 6.17% -6.31%, whereas, the 10Y SGS got dealt in the range of 6.60%-6.76% i.e. the sdl spreads vis-a-vis their CG counterpart remained in the range of 43-48 bps. The range has been wide despite the scenario of surplus liquidity and smaller issuances by states. States so far in this Q1, has borrowed a sum of Rs. 1,18,642 Crores against the notified sum of Rs. 1,86,550 Crores (~63.6% of calendar amount). We expect the spreads for coming fortnight to widen further and remain in the range of 45-50 bps as states are expected to increase their issuance size in June and investor demand is expected to be subdued.

SDL spreads can widen in June

Technical View

Technical Synopsis 6.79% GS 2034 Yield

6.79% G Sec 2034 paper settled at 6.2882% on Friday's session. Range- bound trade between 6.30% - 6.23% was witnessed in passing fortnight.

Momentum oscillator RSI is trading around 45 level. Also, it is showing Divergence to yield chart (as shown in the chart), indicating spike possible if it sustains the level of 6.30%, which also coincide with Middle Bollinger Band. Going forward 6.79%/34 may trade in range of 6.30% to 6.22%, However either side sustainability may trigger further 5-6 basis move on that side.

Bearish breakout possible



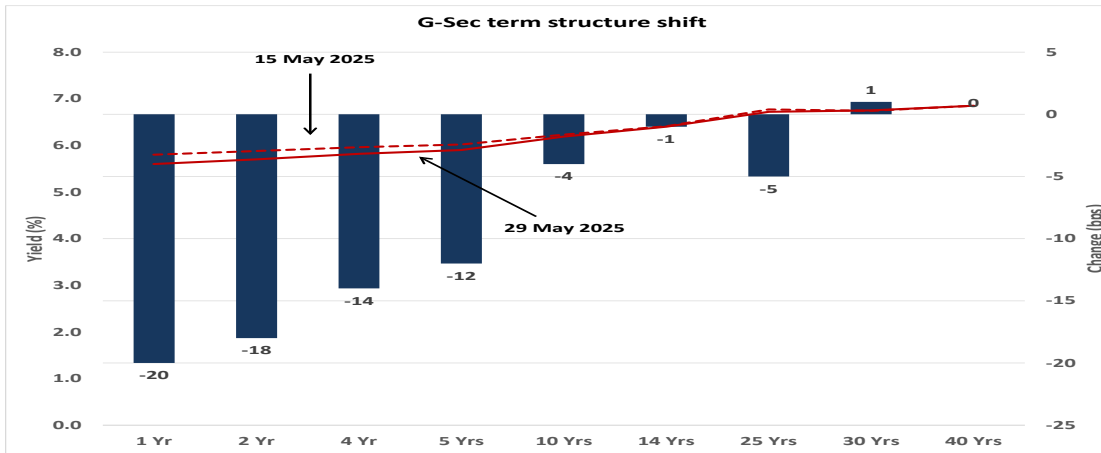
1D chart: 10 yr Source: Tickerplant

Liquidity

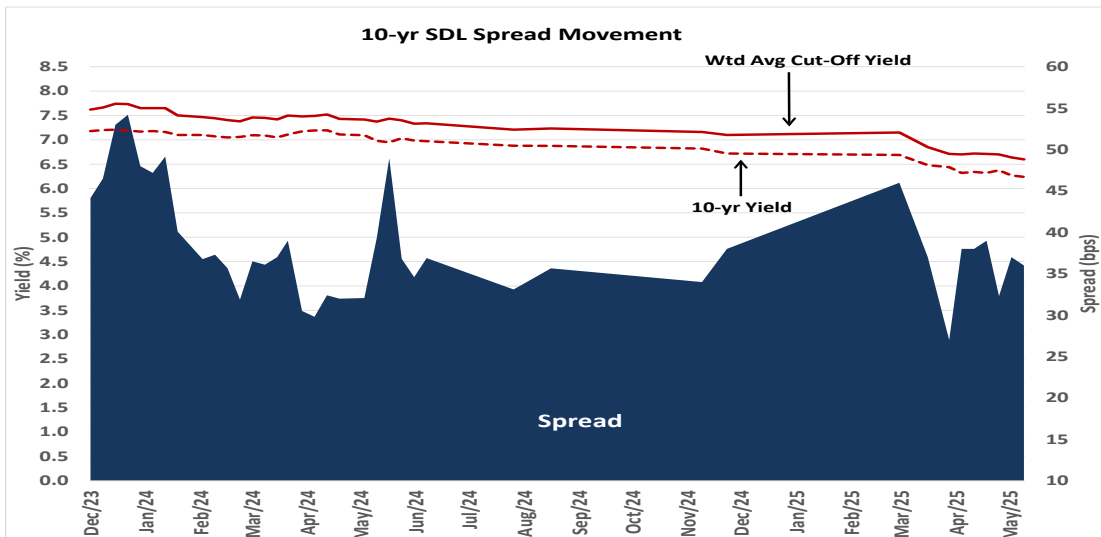
The System liquidity was in Surplus due to OMO Purchases and daily VRR auction by RBI, the weighted average call rate (WACR) exhibited a softening bias and has hovered near SDF rate, in tandem rates in the collateralized segment of the Repo and Treps market have also softened. Going forward the liquidity condition might ease more because of Government spending and Dividend inflow.

Liquidity conditions to ease

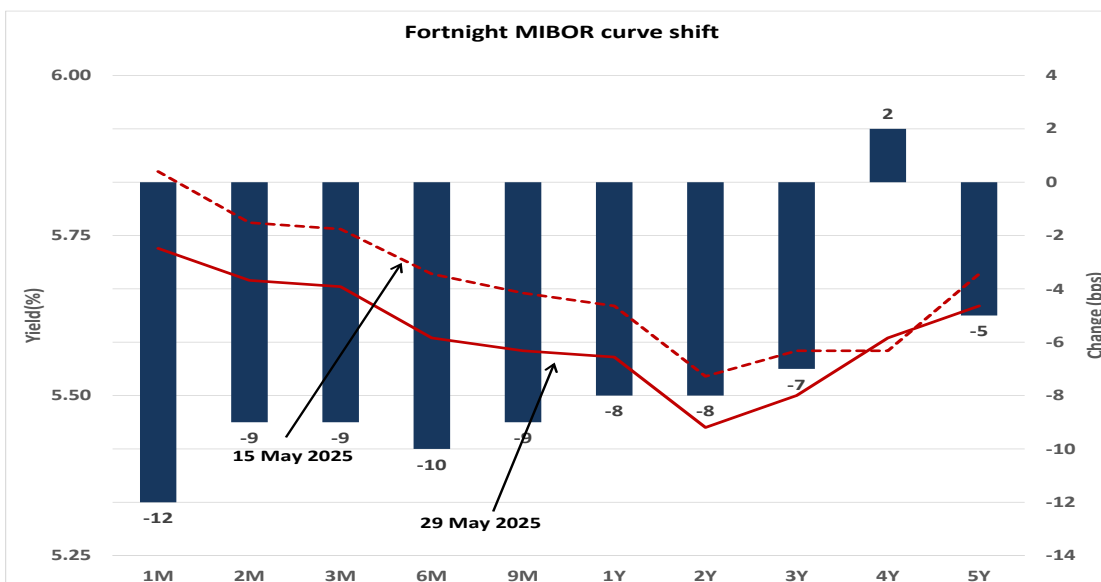
Spread Monitor



G-Sec yields indicating steepening



SDL Spreads have come down



OIS showing signs of stabilising



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