RateView

Crisil's outlook on near-term interest rates

January 2025

by S&P Global

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December drift

The yield on the 10-year benchmark government security (G-sec) opened at 6.71% and closed at 6.76%, up 1 basis point (bp) from its November close of 6.75% and within Crisil's forecast of 6.69-6.79%.

Domestic bond prices remained positive for most of the first week of December, driven by expectations of a potential policy rate cut. Additionally, foreign-investor participation supported gilt prices, with a decline in US Treasury yields providing further support. However, market sentiment took a hit on Friday after the RBI-MPC decided to maintain policy rates and slashed the cash reserve ratio (CRR) by 50 bps to 4% from 4.5% to boost liquidity in the financial system. Further, weak demand for 15-year securities at the weekly G-sec auction exerted additional pressure on bond yields. The 10-year benchmark G-sec closed the first week at 6.74%.

Bond prices remained bullish at the start of the second week, fuelled by hopes of a policy rate cut following the appointment of the new RBI governor. The CPI data for November 2024 printed lower at 5.5%, compared with the previous reading of 6.2%. Later during the week, a rise in the US Treasury yields due to a rise in inflation data exerted pressure on bond prices. Stronger-than-expected demand at the weekly G-sec auction lent support to the bond market. On average, liquidity in the system was ~Rs 38,746 crore surplus. The 10-year benchmark G-sec closed the week at 6.73%.

In the third week, bond prices declined slightly, driven by a higher US Treasury yield. On Thursday, the US Fed cut its policy rates by 25 bps, marking a third consecutive rate cut in 2024. However, the US Treasury yields rose further, following the US Fed's hawkish commentary during the FOMC meeting, which exerted pressure on bond prices. The interest-rate differential between India and the US narrowed to 240 bps because of higher US Treasury yields, leading to a sell-off in the market by foreign portfolio investors (FPIs). On average, liquidity in the system was ~Rs 1.49 lakh crore in deficit, which exerted pressure on bond prices. The 10-year benchmark yield closed for the week at 6.79%.

In the fourth week, bond prices traded in a narrow range and with muted volume amid the Christmas holiday season. A surge in US Treasury yields and the rupee's depreciation against the dollar weighed on the bond prices to some extent. The benchmark 10-year yield closed for the week at 6.76%.

Crisil's outlook

On interest rates

Benchmark	December 31, 2024 (A)	January 31, 2025 (P)	March 31, 2025 (P)
10-year G-sec yield*	6.76%	6.75% - 6.85%	6.65% - 6.75%
10-year SDL yield	7.13%	7.15% - 7.25%	7.08% - 7.18%
10-year corporate bond yield	7.30%	7.24% - 7.34%	7.17% - 7.27%

A: Actual; P: Projected (6.79 GS 2034)

One-month view

In January, domestic G-sec yields are likely to be influenced by various factors, such as liquidity management, FPI inflows and outflows, crude oil prices and the impact of rupee-dollar moves on the debt market.

Three-month view

The 10-year G-sec yield is expected to hinge on the FPI flows, Union Budget 2025-26, crude oil prices, global interest rates, CPI inflation print, FOMC decision, 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 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

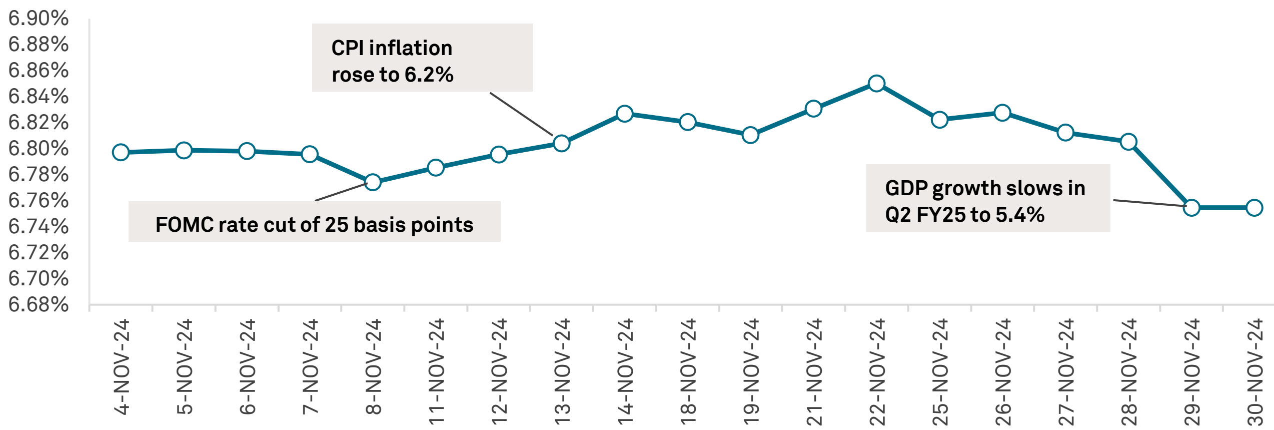
Economic parameter	Our view	Impact on yields
GDP growth	• The National Statistical Office's (NSO) first advance estimate (FAE) for this fiscal projects India's real gross domestic product (GDP) growth at 6.4%, significantly slower than the 8.2% last fiscal • Fiscal consolidation, elevated interest rates and prolonged high food inflation weighed down the economy this year. That said, the FAE indicates quicker growth at 6.8% in the second half compared with 6% in the first. • GDP grew 5.4% on-year in the second quarter of this fiscal, a sharp deceleration from the 6.7% in the first quarter of fiscal 2024	↓
CPI inflation	• We expect consumer price index (CPI)-linked inflation to soften to 4.6% in fiscal 2025 from 5.4% in the previous fiscal. • Food prices are expected to ease in the second half of this fiscal given healthy kharif output. Easing food inflation coupled with benign non-food inflation is expected to bring down headline CPI. • CPI inflation moderated to 5.5% in November from 6.2% the previous month.	↓
RBI's monetary policy	• We expect the first rate cut by the MPC in February • Overall, easing domestic inflation will be the main driver of RBI's rate cuts from February. That said, the cumulative reduction in the upcoming cutting cycle would be less than the 250-bps hiked since May 2022 as domestic growth momentum is projected to remain healthy and global rate cut cycle will also be shallower. • The MPC kept policy rates and stance unchanged in its December meeting. The RBI cut the cash reserve ratio (CRR) by 50 bps to 4% in December to address liquidity deficit	↓
Fiscal health	• The budget has targeted a reduction in centre's fiscal deficit to 4.9% of GDP in fiscal 2025 from 5.6% of GDP past fiscal. • In the first eight months of this fiscal, centre's fiscal deficit stood at 52.5% of the budget target, compared with 50.7% in same period last year. Capital expenditure has been lower this year compared to the same period last year. • Gross market borrowing is estimated at Rs 14 lakh crore for fiscal 2025, 9.2% lower on-year. The government plans to borrow 47.2% of the budgeted borrowings in the second half of the fiscal.	↓
Crude oil prices	• We expect crude prices average \$80-\$85 per barrel range in fiscal 2025 compared to an average of \$82.7 per barrel previous fiscal. • Brent crude oil prices decreased to \$73.8 per barrel average in November, 0.8% lower on-month and 5.2% lower on-year.	↔

[1]*Provisional estimate*

Economic parameter	Our view	Impact on yields
Current account balance	• We expect the current account deficit (CAD) to average ~1.0% of GDP in fiscal 2025 compared to 0.7% of GDP in fiscal 2024. • Even as merchandise trade deficit has come under some pressure, robust services exports and healthy remittances flow should help keep the CAD in the safe zone this fiscal. • 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 the expect the Federal funds rate to reach 3.5%-3.75% by the end of 2025 compared to the previous forecast of 3-3.25% • The Fed cut its policy rate by 25 bps in December to 4.25-4.5%. The Fed cut rates by a cumulative 100 bps in 2024.	↓
Liquidity indicators **i) Demand and supply**	**Supply:** • The SDL Q4-FY25 calendar was announced at Rs 1,53,356 crore, higher than the Q3-FY24 calendar. • The T-Bill Q4-FY25 calendar was announced at Rs 1,47,00 crore, higher than the Q3-FY24 calendar. **Demand:** • Continued demand from insurance companies and pension funds for the longer end of the curves in SDLs and corporate bonds	↔
ii) Call rates/ liquidity-adjustment facility	• GST and advance -tax payments exerted tremendous pressure on liquidity in the Indian banking system in December. This was further exacerbated by dollar sales by the RBI to curb volatility in the Indian rupee and festival season cash withdrawals. • Accordingly, the interbank weighted average call rate (WACR) hovered in the 6.60-6.70% range for most part of the month, well above the policy repo rate of 6.50%, averaging at 6.66% for the month of December	↑

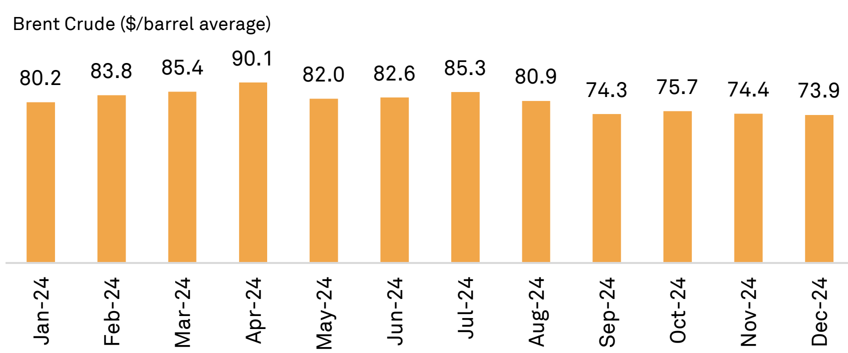
Crisil Intelligence

December at a glance



Source: Crisil Intelligence

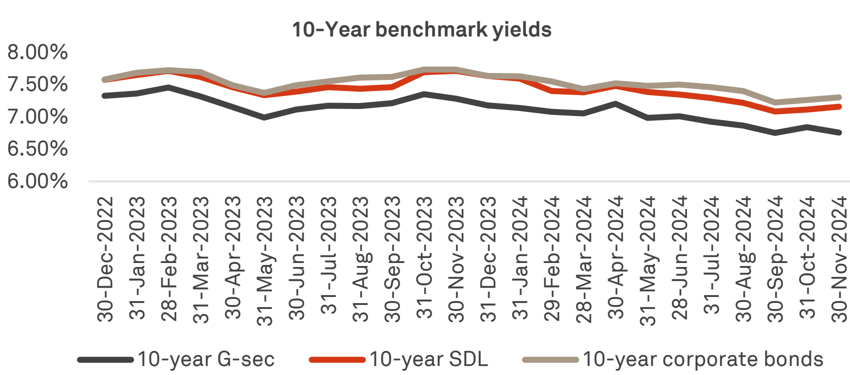
Crude oil prices declined in December



Source: Crisil Intelligence

Brent crude oil prices declined 0.67% on month to ~$73.9 per barrel on average in December.

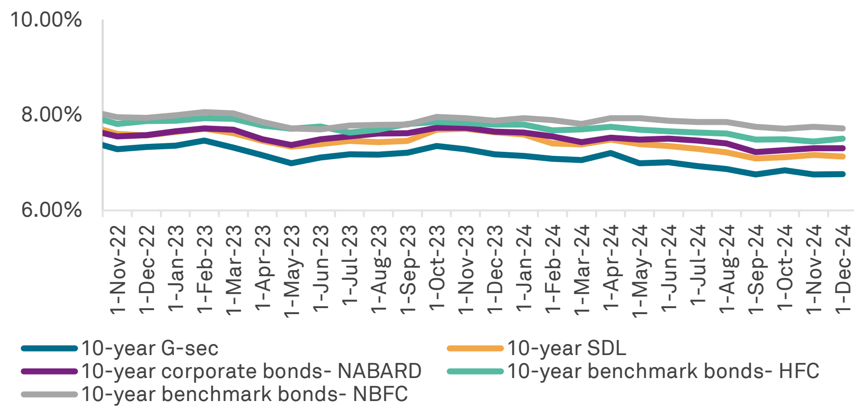
Benchmark SDL yield eases, while corporate bond (PSU FI) yield remains flattish



Source: Source: Crisil Intelligence

The yield on the 10-year benchmark G-sec closed at 6.76% in December, up 1 bp from the previous month's close. The yield on the 10-year SDL eased 3 bps to 7.13% and that on the 10-year corporate bond (10-year PSU FI) remained flattish at 7.30%.

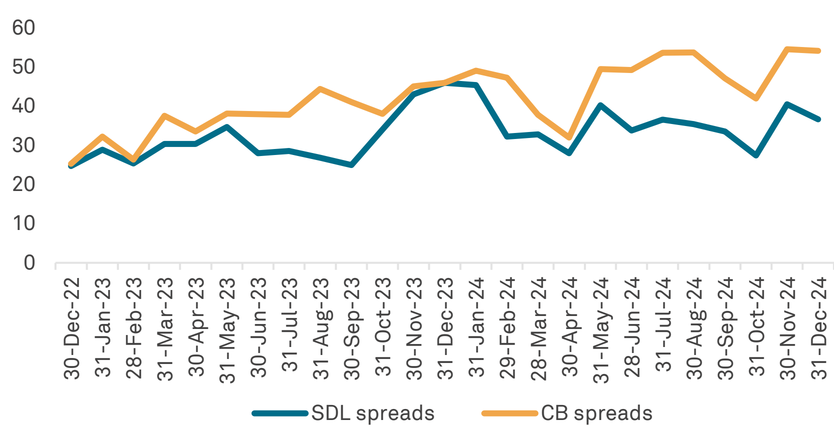
10-year G-sec/SDL/corporate bonds benchmark yields



Source: Crisil Intelligence

Yields remained largely stable. The yield on a 10-year AAA-rated PSU bond remained unchanged at 7.30% for both months. SDLs ended December at 7.13%, down from 7.16% in November. Yields on housing finance company (HFC) bonds rose to 7.50% from 7.44% in the previous month, while those on the bonds of non-banking financial companies (NBFCs) closed at 7.72%, down from 7.75% in November.

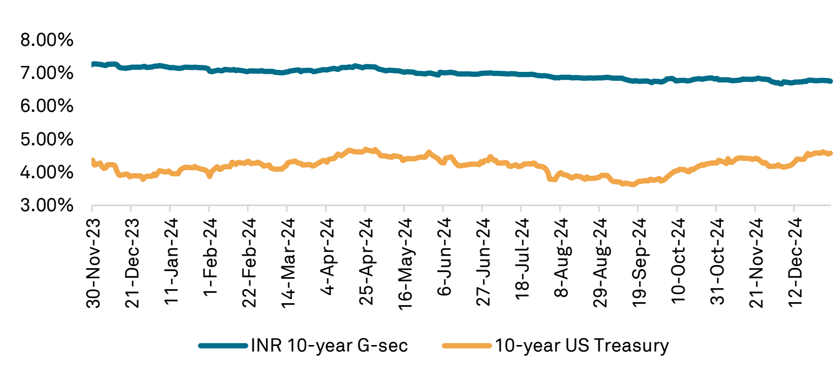
Corporate bonds and SDL yield spreads over 10-year benchmark G-sec yields



Source: Crisil Intelligence

The spread on the 10-year benchmark SDL over the 10-year benchmark G-sec closed at 36 bps in December, down ~4 bps from the previous month's close. Meanwhile, the spread on the 10-year AAA-rated public sector corporate bonds (PSU FI) remained unchanged at ~54 bps. The 12-month-average spreads on the 10-year benchmark SDL and corporate bond (PSU FI) over the 10-year benchmark G-sec were ~35 bps and ~47 bps, respectively.

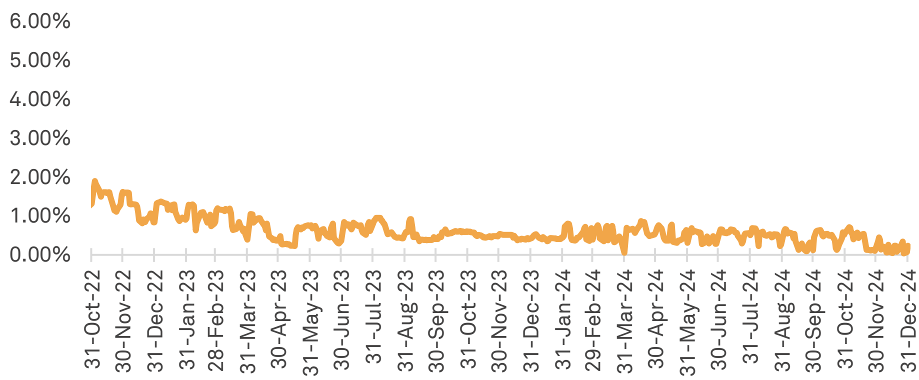
US Treasury and G-sec yield trajectory



US Treasury yields increased a significant 40 bps to 4.58% in December from 4.18% in November. The monthly spread between the domestic benchmark 10-year G-sec yield and the 10-year US Treasury yield narrowed to 218 bps in December.

Source: Crisil Intelligence

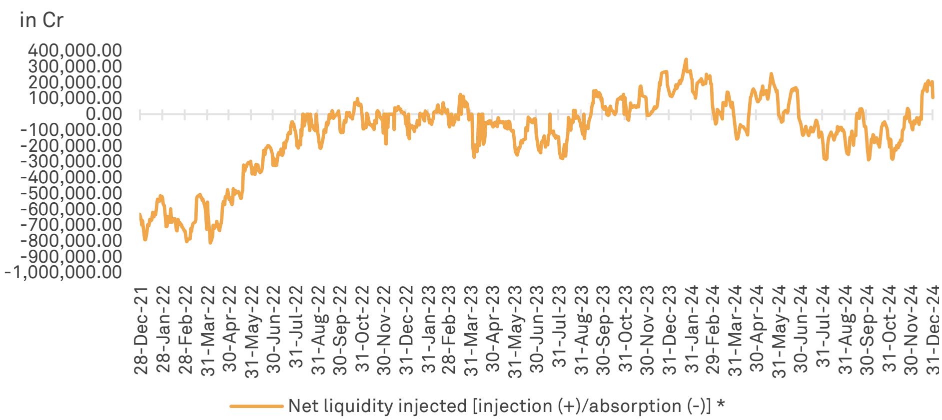
Term premium between 10-year benchmark G-sec and TREPS



Source: Crisil Intelligence

The average spread between the 10-year benchmark G-sec yield and the tri-party repo (TREPS) narrowed to ~19 bps in December from ~38 bps in the previous month. The 12-month average spread was ~47 bps.

Systemic liquidity



**Net liquidity is calculated as repo + marginal standing facility + standing liquidity facility - reverse repo*
Source: Crisil Intelligence

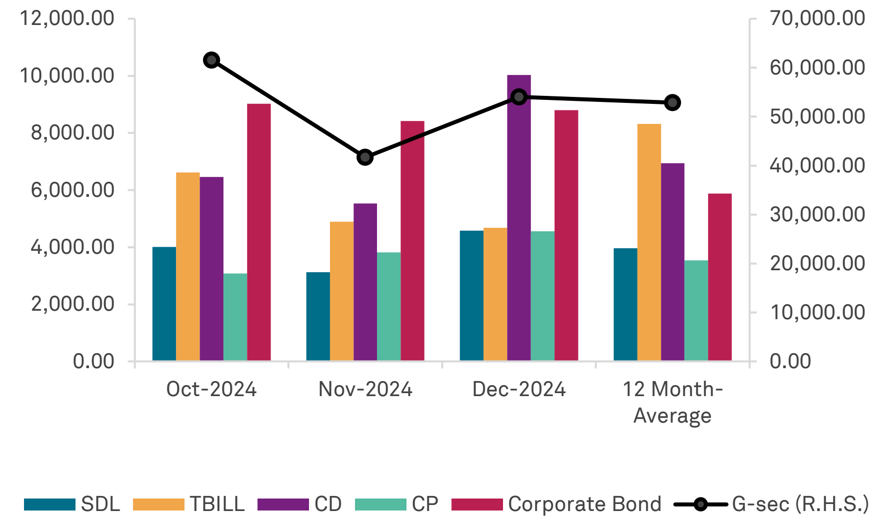
The average systemic liquidity deficit was ~Rs 0.64 lakh crore in December, compared with ~Rs 1.38 lakh crore surplus in November. The average liquidity over the past 12 months was Rs 0.048 lakh crore in surplus.

Benchmark spreads over G-secs

Spreads over G-sec*				
Rating category	**Date**	**PSUs / Corporates**	**NBFCs**	**Housing finance companies**
AAA	30-Nov-24	0.59%	0.93%	0.76%
	31-Dec-24	0.64%	0.94%	0.86%
AA+	30-Nov-24	0.85%	1.40%	1.42%
	31-Dec-24	0.94%	1.41%	1.42%
AA	30-Nov-24	1.14%	2.34%	1.92%
	31-Dec-24	1.21%	2.35%	1.90%
AA-	30-Nov-24	1.94%	3.22%	2.71%
	31-Dec-24	2.07%	3.23%	2.68%

**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 Intelligence

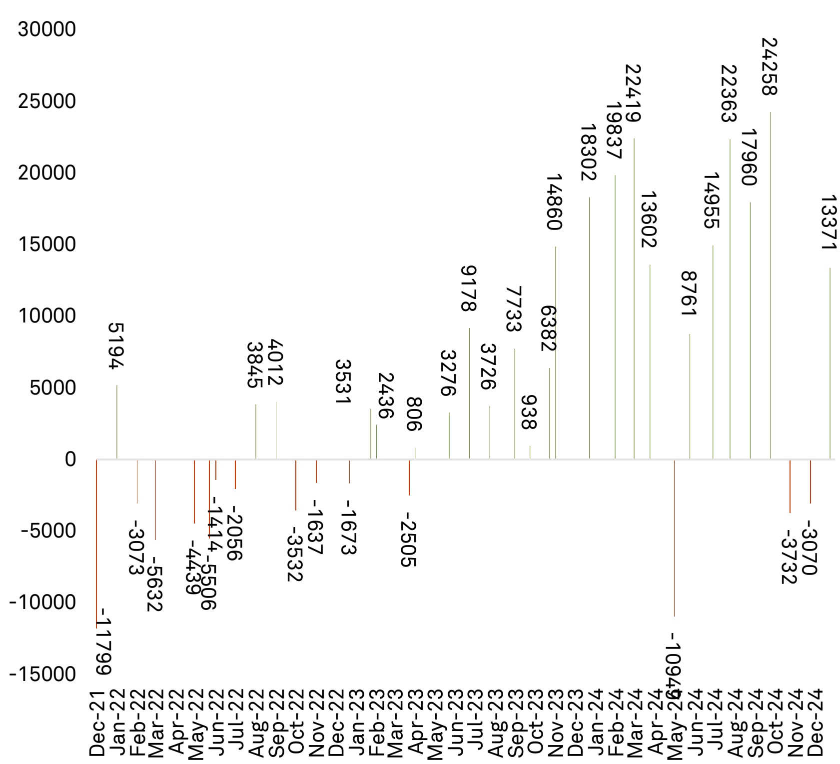
Trading volume increases across securities except T-bills



In December, trading volume in G-secs increased 29.63% on-month, while that of SDLs climbed 46.52%. Trading volume in commercial paper (CPs) and corporate bonds (CBs) rose 19.21% and 4.49%, respectively, while the certificates of deposit (CDs) recorded a significant increase in trading volume at 81.34%. T-bill volume declined 4.27%.

Source: Crisil Intelligence

FPIs turn net buyers



Net FPI inflow into the debt market was Rs 13,371 crore in December, as against an outflow of Rs 3,070 crore in November. FPIs were net buyers during the month, with inflows in both equity and debt markets.

Source: Crisil Intelligence

Rating upgrades and downgrades in December 2024

Upgrades

Issuer name	Old rating as per CRISIL	New rating
Vedanta Ltd.	CRISIL AA-	CRISIL AA
Heritage Max Realtech Pvt. Ltd.	CARE BB	CARE BB+
Raymond Lifestyle Ltd.	CARE AA-	CARE AA
Central Bank of India	IND AA-	IND AA
Mahanagar Telephone Nigam Ltd.	CARE AA+(CE)	CARE AAA(CE)
Varthana Finance Pvt. Ltd.	ACUITE BBB-	ACUITE BBB
Leon Realtors Pvt. Ltd.	CARE B+	CARE BB
IKF Finance Ltd.	CARE A	CARE A+
IKF Home Finance Ltd.	CARE A-	CARE A

Downgrades

Issuer name	Old rating	New rating
Reliance General Insurance Co. Ltd.	BWR A+	BWR A
Shriram Housing Finance Ltd.	CRISIL AA+	CRISIL AA
Save Microfinance Pvt. Ltd.	CARE BBB	CARE BBB-
Arohan Financial Services Ltd.	CARE A	CARE A-

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