

**CANARA ROBECO**

# **Macro Review & Fixed Income Market Outlook - June 2025**

- **Global Macro Review**
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- **Bond Yields & Spread Movements**
- **Fixed Income Fund Manager Outlook**

# Global Economy Update:

## Macro Backdrop:

- Fed officials found recent tariff increases much larger than expected and noted high uncertainty about trade policy and its economic effects. Policymakers agreed to stay patient with monetary policy due to solid economic growth, waiting for clearer trends on inflation and the economy.
- The Bank of England voted 5–4 to cut Bank Rate by 25bps to 4.25% in May as expected. Two members preferred a larger cut to 4%, while two opted to hold at 4.5%. The decision reflects continued disinflation progress as external shocks eased, and tight policy helped anchor inflation expectations.
- **Purchasing Managers' Index (PMI):**
  - **United States:** The S&P Global Flash US Manufacturing PMI increased to 52.3 in May 2025, the highest in three months, compared to 50.2 in April.
  - **Eurozone:** The HCOB Eurozone Manufacturing PMI rose to 49.4 in May 2025 from 49.0 in April.
  - **China:** The Caixin China General Manufacturing PMI unexpectedly declined to 48.3 in May 2025, down from April's 50.4
- **Unemployment Trends:**
  - **United States:** The U.S. unemployment rate held steady at 4.2% in April 2025, matching the March figure and aligning with market expectations.
  - **Eurozone:** Unemployment Rate In the Euro Area remained unchanged at 6.20 percent in March.
- **Monetary Policy:**
  - **European Central Bank (ECB):**
    - On April 17, 2025, the European Central Bank (ECB) reduced its key interest rates by 25 basis points, lowering the deposit facility rate from 2.50% to 2.25%.
    - This marked the ECB's seventh rate cut since June 2024, aiming to support the eurozone economy amid escalating global trade tensions and subdued inflation.
    - Looking ahead, markets anticipate additional rate cuts in 2025, with the next ECB policy meeting scheduled for June 5.
  - **U.S. Federal Reserve:**
    - The Federal Reserve kept the funds rate at 4.25%–4.50% for a third consecutive meeting in May 2025.
    - In discussing the outlook for monetary policy, participants agreed that, with economic growth and the labor market remaining solid and current policy stance moderately restrictive the Fed was well positioned to remain patient and await greater clarity on inflation and economic trends
    - Fed officials assessed that the announced tariff increases had been significantly larger and more extensive than anticipated and noted considerable uncertainty surrounding the direction of trade policy and the magnitude, scope, timing, and duration of its economic effects

## Inflation Trends:

### Global:

- The annual inflation rate in the US eased to 2.3% in April 2025, from 2.4% in March.
- The annual inflation rate in the Euro Area was confirmed at 2.2% in April 2025, hovering just above the European Central Bank's 2.0% target midpoint.
- The annual inflation rate in the UK jumped to 3.5% in April 2025, from 2.6% in March
- Japan's annual inflation rate stood at 3.6% in April 2025, unchanged from March.
- China's consumer prices dropped by 0.1% year-on-year in April 2025. It marked the third consecutive month of consumer deflation, weighed by the combined effects of ongoing trade tensions with the US, weak domestic demand, and persistent employment uncertainty.

# Indian Economy Update:

## Macro Backdrop:

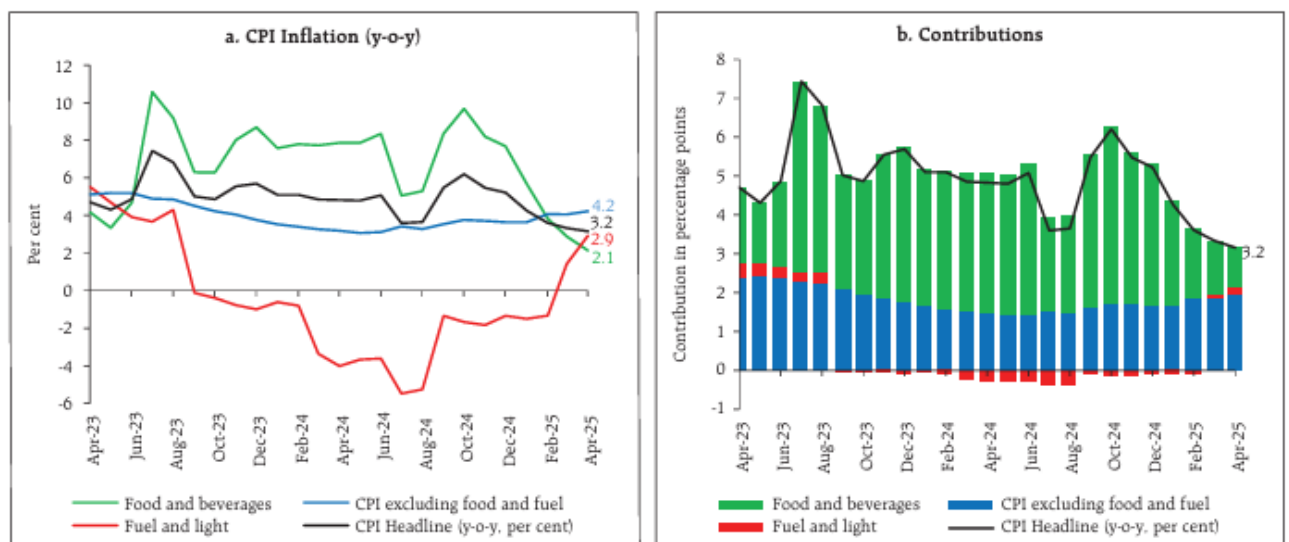
- The Indian GDP expanded 7.4% from the previous year in the March quarter of 2025, accelerating from the upwardly revised 6.4% growth in the earlier period.
- The recovery pointed to traction in Indian economic growth after a period of softening, as lower food and energy prices improved eased benchmark interest rates and spurred investment, while India's low dependence on exports made it robust to global tariff threats.
- **Purchasing Managers' Index (PMI):**
  - The HSBC India Manufacturing PMI was revised down to 57.6 in May 2025 from 58.2 in April. While this marks a three-month low, it still signals a solid improvement in business conditions.
  - The HSBC India Services PMI increased to 61.2 in May 2025, up from 58.7 in the previous month. Domestic new orders rose at the fastest pace in 11 months, while international demand also saw accelerated growth
- **Employment Trends:**
  - **Urban:** Urban employment remains strong, led by expansion in IT and financial services.
  - **Rural:** Rural employment benefited from higher agricultural output and government employment programs.

## Inflation Trends:

### Domestic:

- The annual inflation rate in India fell to 3.16% in April of 2025, the lowest since July of 2019, from 3.34% in the previous month.
- As a result, the inflation rate further below the Reserve Bank of India's 4% midpoint target, strengthening the case for additional rate cuts by the central bank.
- Food prices, which accounts for nearly half of the consumer price basket, rose only 1.78%, down from 2.69% in March.
- Significant decline in headline and food inflation in rural sector observed in April 2025. Also, a sharp decline is observed in food inflation from 2.48% in March 2025 to 1.64% in April 2025.
- Year-on-year Health inflation rate for the month of April 2025 is 4.25%. While Year-on-year Fuel & light inflation rate for the month of April 2025 is 2.92%.

### Trends and Drivers of Inflation:



Sources: National Statistical Office (NSO); and RBI staff estimates.

## Bond Yields & Spreads:

- Global rate markets remain volatile. Moody's recent decision to downgrade the credit rating of U.S. debt has ignited a wave of apprehension regarding the willingness of investors to continue purchasing U.S. government bonds, which may, in turn, may have led to an increase in US bond yields.
- The US tariff situation continues to remain fluid and uncertain, leading the US FED to remain in a pause mode. While inflation has come down, it still remains above US FED target of 2%.
- Indian yields continued to soften in May, albeit in early may, wherein the rates went higher on India-Pakistan skirmish. Overall, the policy direction is seen as dovish as RBI MPC shifted focus to growth as inflation remains below 4% in near term readings. Expectations of more rate cuts in coming MPC meetings continues to support positive market sentiment
- Following the announcement made by the Reserve Bank of India (RBI) regarding its decision to undertake the purchase of government securities valued at ₹1.25 lakh crore in the month of May, bond yields experienced a notable decline. This development significantly boosted market sentiment among investors and stakeholders, leading to a more optimistic outlook.
- The yield on the 10-year Indian G-Sec dropped near to ~6.25%, as the outlook of lower interest rates maintained the confidence in domestic debt. Also, a relatively stable rupee allowed foreign investors to reconsider buying Indian bonds, reigniting foreign inflows into domestic fixed-income securities.

## Outlook:

- Global markets are seeing impact of the tariff uncertainty, as well as geo-political concerns of continued Russia Ukraine conflict.
- Markets are gyrating between fear and hope as tariff situation remains uncertain.
- US fiscal concerns on a large expenditure bill being pushed through the US congress are keeping investors on the sidelines.
- Indian debt market continues to be driven by local factors, with global factors having sentimental impact on markets.
- Liquidity has eased considerably keeping the overnight rate near the standing deposit facility (SDF) rate. RBI continues to add liquidity through OMO purchases, showing intent to keep liquidity in surplus to enable transmission of rate cuts to ultimate borrowers.
- FII flows turned positive in May on strong economic fundamentals.
- RBI is likely to continue to maintain liquidity in a surplus mode and is likely to use OMO purchases as and when required.
- We expect RBI to reduce rates again in June policy as lower inflation creates room to support growth. Further, the ongoing tariff disruptions may lead to slower global growth in near term.
- We are structurally long on India as growth inflation dynamics are still favorable for yields to tick down as RBI may have to resort to further rate cut as growth slows and inflation remains near medium term target of 4%.

Source: RBI, MOSPI, PIB, CMIE, NSDL, S&P Global, Ministry of Commerce and Industry, Reuters, Bloomberg, Internal Research. Note: Data updated as available in the beginning of the month.

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