

Executive Summary

October 2025 opens with a sense of déjà-vu: the global macro picture is turning patchy: inflation hasn't collapsed, but growth signals (jobs, confidence, housing) are softening. US Fed have shifted emphasis toward the labour market, producing a deeply split Fed and a market that now prices an earlier cut.

At home, the big fiscal reform - "GST 2.0" - and an external shock of US tariffs have rearranged the landscape. Consumption tax relief supports domestic demand but tariff led uncertainty has pressured the rupee and equities. Foreign portfolio flows tell a mixed story: selective appetite for Indian debt persists even as equity flows remain volatile.

Global Outlook - Data and Policy take centre stage

A weakening patchwork of data

Across the US and advanced economies, several hard data points released or visible through September-25 showed weakening demand rather than a one-off wobble. Inflation remains sticky in recent prints but not accelerating sharply; at the same time labor market indicators and measures of consumer sentiment have softened - a signal that the economy is losing kinetic energy rather than overheating. Jobless claims have edged higher and payrolls growth has moderated, housing indicators remain fragile with existing and new sales under pressure - all pointing to a slow-motion deceleration in demand. These datapoints collectively explain why rate cut odds have risen in market pricing: the macro surprise is on the downside.

US Fed decision and internal dynamics - jobs over inflation

The September-25 FOMC minute (and related Fed commentary) reveals a US Fed pivot of emphasis: policymakers are increasingly focused on signs of labour market deterioration when weighing policy easing. The committee's late-September 2025 action (and minutes released in early October-25) show most participants supporting a modest easing path, chiefly due to rising unemployment risks. Even as some policymakers remain wary of putting inflation targets at risk. That tone explains the deep divisions markets are parsing: the Fed is signalling willingness to cut if jobs weaken further but not unanimously, and not blindly. The split is real and it leaves the Fed data reaction function asymmetric.

Domestic outlook — GST 2.0, tariffs and flows

GST 2.0 - what happened and why it matters

The government has pushed through a major GST rationalization - GST 2.0, that compresses the many slabs into a simplified structure (materially lowering rates on many essentials and bringing a two slab outcome for large swathes of consumption). The official press note highlights lower taxes on household essentials, medicines and lowered rates on many consumer durables.

The immediate effect: a possible discretionary boost to household purchasing power and a prospective lift to consumption-led demand into the festival season - which is supportive for domestic growth and should temper near-term disinflationary pressures in core goods by raising volume (even as tax rates fall). That combination can be mildly stimulative for growth while being neutral to mildly disinflationary on inflation once base effects pass.

Fiscal/funding angle: the rollout is phased, and the compensation architecture remains a live issue for states and the Centre. However, any delays or unplanned compensation burdens would be watched closely and might have negative impact.

Tariffs, FX and markets — a new source of volatility

Steps taken by US authorities (tariff actions) have lifted risk premia on certain Indian export sectors and added to rupee weakness and equity volatility. Currency moves have been decisive at times, amplifying mark-to-market losses in foreign investor portfolios and changing the calculus for rupee-hedged returns. Equity FPIs have been net sellers in recent months as tariff/headline risks and sector-specific policy worries pressured investor confidence yet debt markets have been a relative refuge.

FII and Indian debt — selective buying continues

The flows story is nuanced: while Foreign Portfolio Investors (FPIs) have been net sellers in equities in recent months, however foreign investors have continued to buy Indian debt selectively especially under the fully accessible route and in the corporate bond space where yields and relative value remain attractive. Weekly and monthly flow tallies showed FPIs as net buyers in debt in recent weeks (September-25 saw persistent, if uneven, debt purchases), reflecting the search for yield in an otherwise risk-off global backdrop.

Market implications

Rates in developed markets are expected to trend lower in the coming months (market-priced cuts), which could provide some tailwind for Emerging Market debt especially India. Domestically, state and central borrowing calendars, plus any compensation costs tied to GST 2.0 rollout, will be closely watched.

Fixed Income Funds that Could be looked at...

Given the risk/return mix, a preference for short-term, liquid and carry-oriented fixed income mutual fund categories could be prudent:

- Money Market Funds: primary allocation for liquidity, parking cash awaiting clearer signals, these provide capital preservation and modest roll-down.
- Ultra-Short Duration: a tactical take to capture better carry than money market while keeping interest-rate sensitivity low. Useful when supply fears raise front end volatility.
- Short Duration Funds: for investors seeking incremental yield with limited duration risk, suitable when the 1 to 3 year part of the curve offers attractive spread vs. cash.
- Income plus Arbitrage Active FOFs: especially attractive for investors seeking yield with limited directional equity risk. In a period of equity volatility, arbitrage structures that convert equity spreads into fixed income-like returns remain appealing.

Past Performance May or May not sustain in future All data as of 30th September 2025. Source: Internal, Trading Economics, Bloomberg

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