



Nippon **india** Mutual Fund

Wealth sets you free

# Fixed Income

## Market Outlook

August 2025



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# Fixed Income Market Update and Outlook

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## Market Update

### **Tariff Uncertainty, Improving Inflation outlook, Ample Liquidity and Front-loading of Spending**

July 2025 saw reduced tariff related to uncertainty globally, while it continued to remain elevated for India in absence of deal and in anticipation of higher reset of US tariff from August.

Back home, improving inflation outlook supported by good monsoon, ample liquidity and robust spending were key highlights of the month.

## **India**

### Monetary Policy:

In the early August'25 policy, the RBI left the policy rate unchanged at 5.5%. Benign inflation and resilient growth outlook were the key highlights of the policy. Despite mix signals from hi-frequency indicators and rising tariff related uncertainty, the RBI kept the FY26 growth projections unchanged at 6.5%, while it revised downward FY26 inflation projections by 60 bps to 3.1%/y. In the policy, the RBI provided neutral pause with data dependent as a forward guidance.

### Inflation:

June 2025 CPI inflation eased to record-low level of 2.1%/y (Better than consensus (2.25%/y) and Lowest since Jan 19). The lower print is supported by favourable base effect, lower than seasonal momentum in food and sequential contraction of fuel & housing prices. Core inflation rose to 4.43%/y in June, driven primarily by elevated gold prices. (Avg Prior three months: 4.15%/y). Food prices contracted marginally (-0.2%/y) – lowest since Jan 2019. 1Q FY26 (Apr-Jun) CPI inflation moderated to average 2.7%/y from 3.7%/y in Jan-Mar 2025 quarter.

## Fiscal:

1Q FY26 Fiscal deficit stood modest at 18% of BE FY26 (Previous yr: 8% of BE). This was aided by Robust receipts. Growth in revenue receipts was driven primarily by non-tax revenue, while net tax revenue contracted marginally on muted collections and higher devolution to the states. On other hand, expenditure growth was robust at higher double-digit (26%y/y), partially aided by the favourable base effect and front-loading of expenditure (especially Capex grew).

After picking up in April-May, GST growth moderated to 6.2%y/y in June & 7.5%y/y in July 2025. That said, YTD FY26 (Apr-Jul) growth was resilient at ~11%y/y.

## Liquidity:

Since April, system liquidity has eased substantially, with further improvement evident in July. Average monthly liquidity improved to Rs. 3.1 trillion in June (Apr: Rs. 1.4 trn; May: Rs. 1.7 trn; Jun: Rs. 2.8 trn) on Govt spending, buybacks and lower cash demand.

The core liquidity remained ample at ~Rs. 5.5 trn in July (Jun: Rs 5.7 trn) on higher Cash Reserve Ratio (CRR) requirement and RBI's FX actions.

## External Sector:

June Trade deficit moderated to ~US\$19 bn (May 25: US\$22 bn), on sharp decline in core imports. June 2025 net service exports grew robustly at ~20%y/y due to resilient services exports and tepid services imports.

Net FPI inflows continued to remain negative in July 2025 to US\$0.6 bn (Jun 2025: -ve US\$0.9 bn) driven down by equity outflows.

DEX continued to depreciate for sixth consecutive month, on rising tariff uncertainties and growth concerns. DEX depreciated by ~8% in the current calendar year till date.

INR continued to depreciate in July and stood on average 86.10 against dollar (Apr: 85.56; May 2025: 85.19; Jun: 85.90). In the calendar year 2025, the rupee has depreciated by ~2.3%.

## Yield Levels & Spreads:

July'25 saw fixed income market yields move in narrow range for most part of the month. G-sec yields eased initially on lower monthly inflation print and muted crude oil prices, but rose towards the end of the month on rising concern of delayed US tariff deal, higher crude prices and pressure on INR. 10-year G-sec yields started the month at 6.36% and moved in the narrow range of 6.30%-6.33% for most part of the month (Jun 2025: 6.32%-6.39%). 10 yr G-sec closed the month higher at 6.38% (Apr 2025: 6.36%; May 2025: 6.25%, Jun 2025: 6.36%).

Like G-sec, 10-year SDL moved in narrow range of 6.75%-6.80% for most part of the month (Jun 2025: 6.65%-6.74%;) and closed the month higher at 6.86% (Apr 2025: 6.67%; May 2025: 6.61%; Jun 2025: 6.73%). July SDL primary issuances stood at Rs. 96,769 cr (Jun 2025: Rs. 82,207 cr). The average spread between 10 yr SDL over G-sec stood at 47 bps during the month (Jun 2025: 35 bps).

10-year AAA bonds moved in the narrow range of 6.99%-7.04% (Jun 2025: 6.89%-7.02%). 10 yr AAA PSU closed the month higher at 7.04% (Apr 2025: 6.98%; May 2025: 6.85%; Jun 2025: 7.02%).



# **Global**

## Monetary Policy:

July 2025 saw major global central banks (US Federal Reserve, ECB, Bank of Japan) keeping the policy rates unchanged and preferring data dependent approach. Going forward, the central banks (CBs) are likely to prefer gradual rate cut cycle on back of global uncertainties.

## Financial Markets:

US 10 Yr Treasury bond (UST) yield harden a bit and moved in the range of 4.26%-4.50% and close the month higher at 4.37% (Apr 2025:4.17%; May 2025: 4.41%; Jun 2025: 4.24%). Yield movement was driven by better-than-expected 2Q GDP, higher reset of US reciprocal tariff than previously expected, higher inflation print, fiscal concerns and data-dependent US Federal Reserve.

Dollar index (DXY) continued to depreciate for sixth consecutive month by 0.5% (Apr 2025: -ve 3.3%<sub>m/m</sub>; May 2025: -ve 0.58%<sub>m/m</sub>; Jun 2025: -ve 1.7%).

After rising sharply in June'25, the average July'25 crude oil remained stood around June lvl at US\$71.04/barrel.

# Market View

- » US reciprocal tariff, and geopolitical uncertainties are likely to weight on India's growth and currency outlook.
- » Policy-makers decision-making is likely to be influenced by improving inflation outlook, mixed growth trends (Purchasing Managers Index {PMI}, industrial production, credit growth etc) and tariff implications on trade, currency and foreign flows.
- » In the early August'25 policy, the RBI has admitted that the average FY26 CPI to remain significantly below medium target. That said, RBI expect the headline CPI print to edge above 4% from 4Q onwards (driven primarily by adverse base effect) and core inflation to stay moderately above 4% in FY26.
- » RBI is likely to remain data dependent for future policy actions - tracking closely evolving trends in inflation, growth and external sector.
- » System Liquidity is likely to remain ample in August'25 on seasonally lower cash demand and lower activity months (due to monsoon). Further, with CRR cut to be implemented in September through November'25, the RBI continues to remain supportive and nimble on liquidity front.

## Common Source:

RBI, CSO, FAO, CEIC, NSO, US Federal Reserve, US Treasury department, Commerce Ministry of India, Finance Ministry of India, ECB, BoJ, NIMF Internal Research

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