



Nippon **india** Mutual Fund

Wealth sets you free

# Fixed Income

Market Outlook

September 2024



Good gets *better*

# Fixed Income Market Update and Outlook

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## Market Update

### **Robust Economic Growth, Guarded RBI and US Fed Pivot**

Better than expected 1Q FY25 economic growth (driven by broad-based improvement), good monsoon, guarded RBI (on volatility in food prices), improving system liquidity (seasonality), better fiscal and robust FPI inflows were key features of the month August 2024.

Globally, US Fed signalling rate cut cycle ahead and Bank of England (BoE) starting rate cut cycle were the highlight of the month.

## **India**

### Economic Growth:

1Q FY25 gross domestic product (GDP) growth moderated to 6.7%/y (4Q FY24: 7.8%/y; 1Q FY24: 8.24%/y). That said, private consumption grew robust at 7.45%/y (prior quarter: 4%/y; 1Q FY24: 5.55%/y) – Highest since Sep 2022 – indicating revival of private consumption. Also, capex and export growth were buoyant indicating resilience of the growth.

On the supply side, gross value added (GVA) growth was robust at 6.8%/y (prior qtr: 6.3%/y; 1Q FY24: 8.26%/y). Growth was broad-based driven by manufacturing, electricity, construction, mining and public spending. Core GVA (excludes agriculture and public spending) was buoyant at 7.3%/y (~ previous quarter level).

### Monetary Policy:

In August policy, the RBI maintained the status quo for ninth consecutive meeting. The policy statement and press conference that followed clearly indicated that it was guarded decision with options kept open. While RBI revise down the 1Q FY25 GDP estimate, it left FY25 growth projections unchanged. Similarly, while retaining FY25 inflation projections, RBI has revised upward 2Q & 3Q projections. That said, Policy focus was on growth while discussing about inflation. On the currency volatility concerns, RBI seems confident of meeting external financing requirements comfortably on backdrop of manageable current account deficit (CAD), robust capital flows and record high forex reserves.

## Fiscal:

April-July 2024 gross tax receipts grew robustly by ~23%/y - driven by buoyant direct tax collections and resilient indirect taxes. Record high RBI dividend resulted in sharp spike in non-tax receipts. Expenditure continued to register degrowth driven down primarily by degrowth in revenue expenditure and double-digit contraction in capex. As a result, Fiscal deficit stood at record low 17% of budget estimates (Previous year similar period: 34%). August GST data registered record third highest tax collections at Rs. 1.75 trn (Apr-Aug FY25: 10%/y).

## External Sector:

July'24 Trade deficit rose to ~US\$23 bn (Apr 24: US\$19 bn; May'24: US\$22 bn; Jun'24: US\$21 bn). Apr-July 2024 exports grew at muted 4%/y, while imports grew at 7.5%/y. Core imports growth (non-oil non gold) were muted. Apr-July 2024 Net services exports grew robustly at 16%/y.

FPI (debt and equity) continued to grow robustly at US\$3 bn in August despite volatility witnessed in global equity market in early part of the month. Apr-Aug FY25 FPI flows were buoyant at US\$10.4 bn (4Q FY24: US\$9 bn) aided by both equity and debt market inflows (especially related to bond inclusion index).

Rupee marginally continued to depreciate marginally in June through Aug and stood at 83.90 against dollar during Aug (July 2024: 83.59; June 2024: 83.47; May 2024: 83.39; Apr 2024: 83.41).

## Bond Inclusion:

India became part of JP Morgan Bond index since end June 2024. Total inflows since Sep 2023 announcement have been to the tune of ~Rs.1.5 trn, out of which FAR (Fully Accessible Route) securities got inflows to the tune of ~Rs.1.4 trn. Aug'24 saw ~Rs.24,000 cr in FAR securities (June 2024: ~Rs.17,000 cr; July 2024: ~Rs. 19,000 cr).

## Liquidity:

Banking system liquidity eased further to average Rs. 1.5 trn on seasonality, govt spending and FPI flows. (Jul 2024: Rs. 1.1 trn; Jun 2024: -ve Rs. 50,000 cr; May 2024 ~ -ve Rs.1.4 bn). Government balances continued to remain robust and stood on an average ~Rs. 2.6 trn (July 2024: Rs. 2.9 trn; June 2024: Rs. 4.2 trn; May 2024: Rs. 3.5 trn). Core liquidity (system liquidity + Government balances) stood at ~Rs.4.1 trn by Aug end (July end: Rs. 4.5 trn; June end: ~Rs. 3.5 trn; May end: ~Rs. 3.6 trn).

## Yield Levels & Spreads:

Fixed income market yields continued to remain range-bound during the month with easing bias on lower inflation and global cues (easing global policy rate, commodity prices etc). 10-year G-sec yield moved in the narrow range of 6.85%-6.92% (July 2024: 6.92%-7.01%; June 2024: 6.95%-7.03%). 10 yr G-sec closed the month lower at 6.86% (July 2024: 6.92%; June 2024: 7.02%). Average 10-year term premia increased to average~14 bps during the month (July 2024: 11 bps; June 2024: 2 bps) – on relatively faster easing of short-term rates aided by improved liquidity.

Taking cues from G-sec, 10-year SDL yields eased further and were range-bound during the month (range of 7.19-7.26% as against 7.28-7.36% in July) to close the month lower at 7.21% (July 2024: 7.28%; June 2024: 7.33%). August SDL primary issuances stood Rs.89,690 cr (July 2024: Rs. 68,400 cr; June 2024: Rs. 52,000 cr). The average spread between 10 yr SDL over G-sec stood at 35 bps during the month (June-July 2024: 36-37 bps).

Like G-sec and SDLs, AAA bonds were range-bound with easing bias, with 10 yr AAA PSU moving in the band of 7.40%-7.45% (Previous month: 7.45%-7.49%). It closed the month lower at 7.40% (July 2024: 7.46%, June 2024: 7.49%).



# **Global**

## Monetary Policy:

Aug'24 saw Bank of England joining the major Central bankers and begin the rate cut cycle. Backed by softer macro data, US Fed Chairman clearly indicated the rate cut action in Sep policy meeting.

## Financial Markets:

During the month of Aug'24, US treasury yields continued to ease further and rallied on rate cut expectations, easing inflation and dovish US Fed. US 10 Yr Treasury bond (UST) yield moved in the range of 3.78%-3.99% (as against 4.09-4.48% in Jun 2024) and closed the month lower 3.91% (Jul 2024: 4.09%; June 2024: 4.36%). Dollar Index continued to depreciate in Aug by ~2.3%<sub>m/m</sub> after depreciating by 1%<sub>m/m</sub> in Jul (CY2024 YTD: +ve 0.4%) on rate cut expectations.

# Market View

- » RBI's actions and other developments over the couple of months have been market supportive.
  - a). Regular FPI inflows; b). incremental LCRAR ratio (Liquidity Ratio- Conditional Redemption at Risk); c) RBI's aggressive forex intervention allowing liquidity to remain in the system; d). Faster fiscal consolidation.
- » Indian bonds are likely to be supported by easing global yield bias, good macro, lower core inflation and improved demand (bond inclusion).
- » Going forward, the market can be expected to perform well, unless RBI's specific action either on liquidity front or global financial market volatility.
- » Amidst the global central banker's easing bias and improving macros, we continue to expect rate cut in Oct/Dec'24 policy. The risk to projections is curve volatility.

**Common Source:**

RBI, CSO, FAO, CEIC, NSO, JP Morgan, US Federal Reserve, US Treasury department, Commerce Ministry of India, NIMF Internal Research.

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