Market Intelligence
& Analytics

RateView

CRISIL's outlook on near-term rates

November 2023

Research

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October heat

The yield on the new 10-year benchmark government security (G-sec; 7.18% GS 2033) opened October at 7.23% and closed at 7.35%, up 14 bps from its September closing of 7.21% and outside CRISIL's forecast range of 7.23-7.33%.

In the first week, bonds traded largely with a negative bias due to a surge in US-Treasury (UST) yields and crude oil prices. In addition, the Reserve Bank of India (RBI) hinted at open market operations (OMO) sales in future to manage liquidity in the market. This led the yield on the 10-year benchmark G-sec to harden by 14-15 bps. The domestic 10-year benchmark yield closed the week at 7.34%.

The second week started on a negative note, tracking a surge in crude oil prices amid geopolitical tensions in the Middle East and due to likely OMO sales. India's retail inflation printed at a three-month low of 5.02% in September on the back of softer vegetable prices. However, as the week progressed, the bond market witnessed a softening in yields due to a decline in UST yields. The 10-year benchmark yield slipped and closed the week at 7.32%.

In the third week, UST yields touched 5% for the first time since 2007 following strong economic data, which renewed fears that US interest rates may stay elevated for longer. Crude oil prices also remained high amid concerns that the Middle East conflict will spread through the region and cause supply disruptions. The domestic benchmark yield closed the week at 7.36%.

In the fourth week, a decline in UST yields supported domestic yields. In addition, bond yields softened further owing to better-than-expected cut-off prices at the weekly auction. The domestic 10-year benchmark yield closed the week at 7.35%

CRISIL's outlook

On interest rates

Benchmark	October 31, 2023 (A)	November 30, 2023 (P)	January 31, 2023 (P)
10-year G-sec yield*	7.35%	7.26%-7.36%	7.21%-7.31%
10-year SDL yield	7.69%	7.54%-7.64%	7.52%-7.62%
10-year corporate bond yield	7.73%	7.66%-7.76%	7.62%-7.72%

A: Actual; F: Forecast
Source: CRISIL MI&A Research

One-month view

In November, the 10-year benchmark G-sec yield is expected to stay range-bound. Oil prices, US Treasury yields and geopolitical tensions due to the Middle East conflict can put upward pressure on the yields. Moreover, RBI hinted at the possibility of OMO sales to drain out surplus liquidity from the money market.

Three-month view

Domestic factors such as inflation based on the consumer price index (CPI), Monetary Policy Committee (MPC) meeting and external factors such as global crude oil prices, further escalations in the Middle East conflict, capital flows, UST yields and geopolitical tensions are expected to exert upward pressure on yields for a couple of months.

Framework for 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 our in-house experts. We also incorporate our views on policy expectations, 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

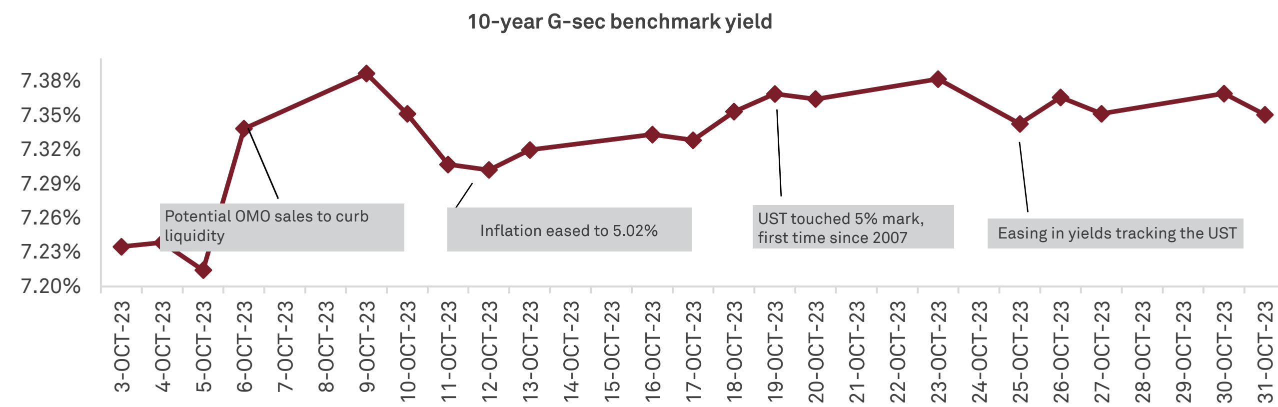
Economic parameter	Our view	Impact on yields
Gross domestic product (GDP) growth	• We expect India's real GDP growth to slow to 6.0% on-year in fiscal 2024 from 7.2 % the previous year • Slowing global growth in the second half of this fiscal is expected to hit the Indian economy through weaker exports. Domestic demand is expected to be mildly impacted by the lagged impact of RBI's past rate hikes • Real GDP growth accelerated to 7.8% on-year in the first quarter of fiscal 2024, from 6.1% the previous quarter	↓
Consumer price index (CPI) inflation	• We expect CPI-linked inflation to moderate to 5.5% in fiscal 2024 from 6.7% the previous year • Uneven rainfall distribution during the monsoon season, an uptick in crude oil prices, and tight global food supplies pose upside risks to inflation this fiscal. However, easing input cost pressures for manufacturers and moderating domestic demand are expected to ease core inflation • CPI inflation eased to 5% in September from 6.8% in August	↓
RBI's monetary policy	• We expect RBI to keep rates unchanged for the remainder of this fiscal • We expect a rate cut only in the first quarter of the next fiscal, assuming normalising inflation and slowing growth • MPC kept policy rates unchanged in its October meeting, while maintaining its stance of withdrawal of accommodation	↔
Fiscal health	• The budget has targeted a reduction in the centre's fiscal deficit to 5.9% of GDP this fiscal from 6.4% of GDP the previous fiscal • In the first six months of this fiscal, the centre's fiscal deficit stood at 39.3% of the budget target, compared with 37.3% in same period last year. Capital and revenue expenditure as a proportion of budget target have been higher than last year	↓
Crude oil prices	• We expect crude prices to average $80-$85 per barrel in fiscal 2024 compared with $95 per barrel the previous year • Brent crude oil prices decreased to $91.1 per barrel on average in October, lower 3.1% on-month and 2.2% on-year	↓

[1]Provisional estimate by National Statistics Office

Economic parameter	Our view	Impact on yields
Current account balance	• We expect current account deficit (CAD) to average 1.8% of GDP in fiscal 2024 compared with 2.0% of GDP in fiscal 2023 • Lower international commodity prices on-year and support from healthy services exports and remittances will help CAD narrow this fiscal. The recent uptick in crude oil prices poses an upside risk to our forecast for fiscal 2024 • CAD rose to 1.1% of GDP in the first quarter of fiscal 2024 from 0.2% of GDP the previous quarter.	↓
US Federal Reserve's stance	• S&P Global sees Fed keeping policy rates higher for longer and does not expect the first rate cut till June 2024 • Fed kept its policy rate unchanged at 5.25-5.50% for the second consecutive time at its November meeting	↔
Liquidity indicators i) Demand and supply	• Longer-duration G-secs have seen additional demand from long-term players as rates have stabilised • A new 50-year G-sec (7.46 GS 2073) has been issued in response to market demand for ultra-long papers • Bonds worth Rs 53,925.3 crore matured on November 2, and worth Rs 56,572.7 crore and Rs 32,500 crore are set to mature on November 25 and 29, respectively, infusing cash into the economy.	↔
ii) Call rates/ liquidity adjustment facility (LAF)	• The interbank call money rate averaged 6.51% in October, slightly higher than RBI's repo rate of 6.50%, due to a sizeable deficit in banking system liquidity through the month, which can be attributed to the impact of the implementation of the incremental cash reserve ratio (I-CRR) in August and tax outflows. • Although RBI eventually announced the withdrawal of I-CRR in the first week of October, tight liquidity conditions persisted through the month, as reflected in the deficit. • Liquidity stress being faced by banks is also reflected in RBI data, which revealed that banks borrowed Rs 3.2 trillion in the first week of October, compared with Rs 113.3 billion in the first week of August and Rs 220.6 billion in the first week of September. • Seeking to ease liquidity and interest rates in the call money market, RBI Governor Shaktikanta Das urged banks to lend in the overnight market rather than parking in the standing deposit facility. The central bank is also expected to conduct an open market sale of debt once government spending increases and liquidity surplus improves.	↔

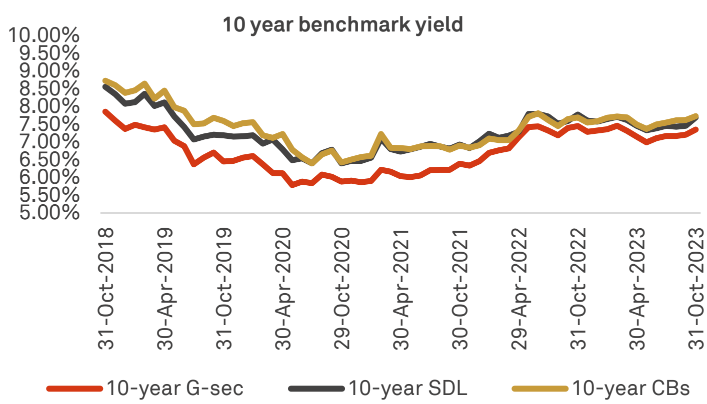
CRISIL's outlook on interest rates

October at a glance



Source: CRISIL MI&A Research

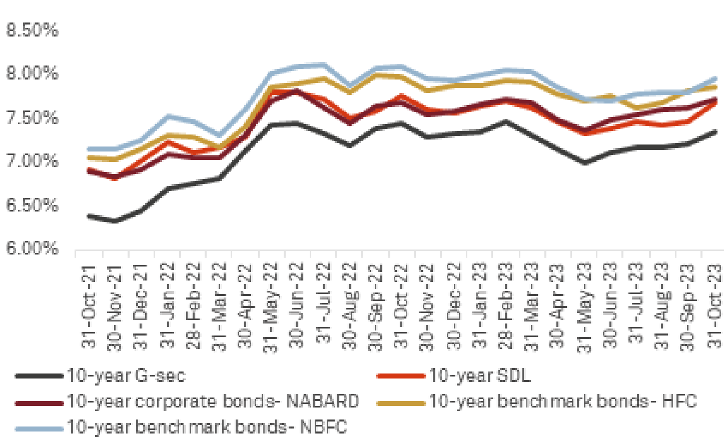
Benchmark yields



In August, the yield on the 10-year benchmark G-sec closed at 7.17%, at the same level as July close, while that on the 10-year SDL eased 3 bps to 7.43% from 7.46%. The yield on corporate bonds (CBs; 10-year PSU FI) closed at 7.61%, up 6 bps from 7.55% a month ago.

Source: CRISIL MI&A Research

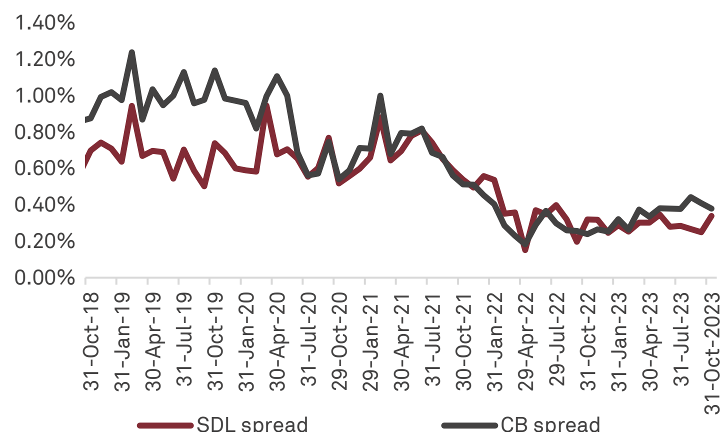
10-year G-sec/ SDL/ corporate bond benchmark yields



The yield on the 10-year benchmark bonds — Housing Finance Company (HFC) — hardened 4 bps on-month to 7.85% in October. Yields on the 10-year benchmark bonds for AAA-rated NBFCs and AAA-rated PSU bonds closed at 7.96% and 7.73%, respectively, up from 7.80% and 7.62% in September.

Source: CRISIL MI&A Research]

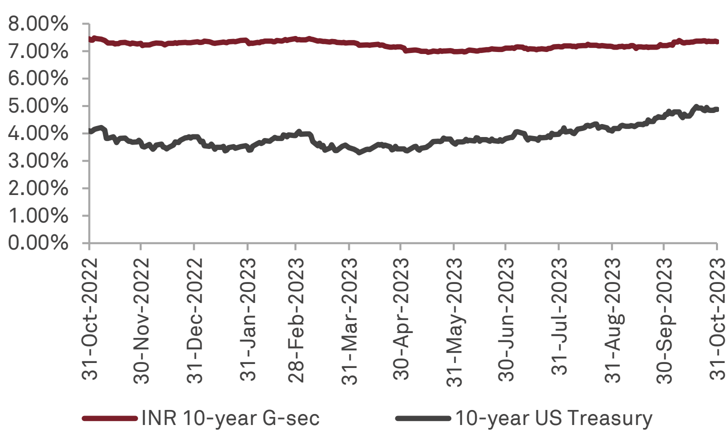
SDL spreads over 10-year benchmark G-sec hardens.



Source: CRISIL MI&A Research

The spread of the 10-year benchmark SDL over the 10-year benchmark G-sec closed at 34 bps in October, up from 25 bps in September. Meanwhile, the spread of the 10-year AAA-rated public sector CB contracted from 41 bps to 38 bps. The 12-month average spreads for the 10-year benchmark SDL and CB over the 10-year benchmark G-sec were 29 bps and 35 bps, respectively.

US Treasury yield hardens

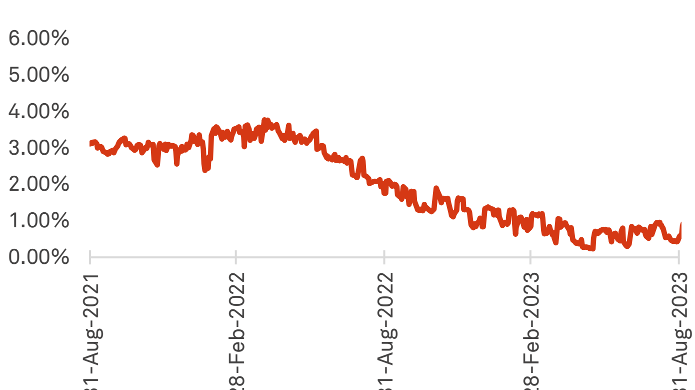


Source: CRISIL MI&A Research

The 10-year UST yield closed at 4.88% in October, 29 bps higher from its September close of 4.59%. The monthly average spread between the domestic 10-year benchmark G-sec yield and the 10-year UST yield eased to 247 bps from the previous month's 262 bps. The surge in UST yields reflected the rise in crude oil prices due to extended production cuts by Russia and Saudi Arabia. The ongoing Middle East conflict has added to global uncertainties, especially on energy prices.

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

Term premium (10-year G-sec benchmark and TREPS)

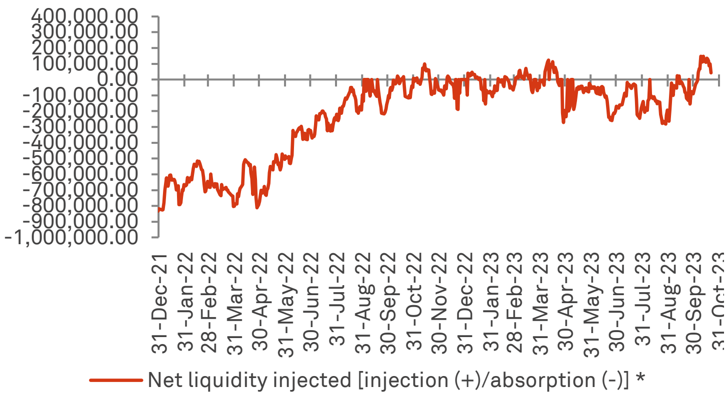


Source: CRISIL MI&A Research

The average spread between the 10-year benchmark G-sec yield and tri-party repos (TREPS) widened to ~57 bps in October from ~49 bps in September. The 12-month average spread was at ~81 bps.

Surplus systemic liquidity

Net liquidity injected in Rs crore [injection (+)/absorption (-)]*



** Net liquidity is calculated as repo + MSF + standing liquidity facility - reverse repo*
Source: CRISIL MI&A Research

In October, the average systemic-liquidity deficit was ~Rs 0.48 lakh crore, as against the previous month's deficit of ~Rs 0.24 lakh crore. The average surplus over the past 12 months was ~Rs 0.52 lakh crore. Systemic liquidity injected as of end-October was ~Rs 0.106 lakh crore. RBI's I-CRR was successful in draining out excess liquidity from the system for an extended period. In addition to tax spillovers, currency demand ahead of the festive season also seems to have impacted liquidity in the system.

Benchmark spreads over G-sec

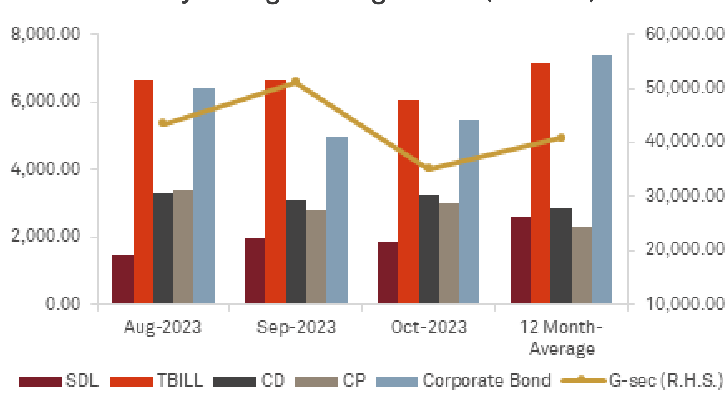
Spreads over G-sec*

Rating category	Date	PSUs/ corporates	NBFCs	Housing finance companies
AAA	30-Sep-23	0.32%	0.50%	0.43%
	31-Oct-23	0.39%	0.50%	0.44%
AA+	30-Sep-23	0.56%	0.97%	0.93%
	31-Oct-23	0.54%	1.07%	0.89%
AA	30-Sep-23	1.15%	1.72%	1.42%
	31-Oct-23	1.20%	1.74%	1.37%
AA-	30-Sep-23	1.89%	3.15%	2.30%
	31-Oct-23	1.89%	3.21%	2.32%

*Note: * Spreads are for five-year securities over annualised G-sec yield; selection of representative issuers has been re-evaluated as per periodic review*
Source: CRISIL MI&A Research

Trading volume across securities

Monthly average trading volume (Rs crore)

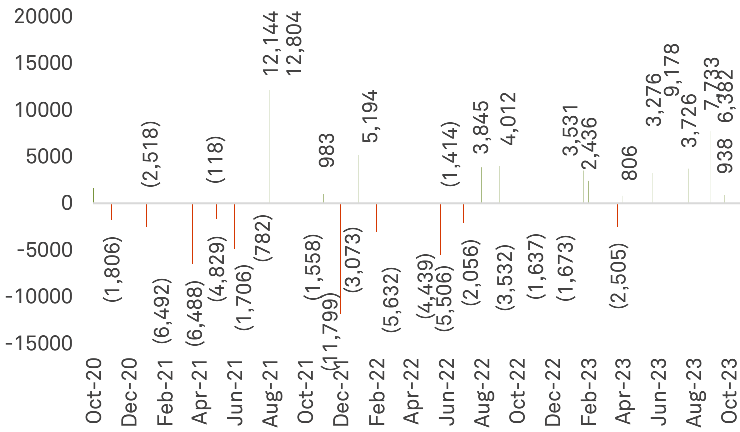


Source: CRISIL MI&A Research

While the trading volume in G-secs decreased by -31.43%%, SDLs decreased by -4.32%, volume in T-bills fell ~8.85%, the trading volume of commercial papers (CPs) and certificates of deposit (CDs) rose by ~7.20% and ~4.76%, respectively.

FPIs continued to be net buyers in debt.

FPI net investments in Debt (Rs crore)



Source: CRISIL M&IA Research

The net FPI inflow into debt was Rs 6,382 crore in October, compared with a net inflow of Rs 938 crore in September, making it the third-highest level this calendar year as investors rushed to lock in higher returns amid global uncertainties and geopolitical tensions. Equity witnessed an outflow of Rs 24,548 crore. Before this, FPIs incessantly bought Indian equities over March to August. However, in October, FPIs turned net sellers for the second consecutive month due to the surge in UST yields and geopolitical tensions arising from the Middle East conflict.

Key downgrades and upgrades

Upgrades

Issuer name	Old rating	New rating
Yes Bank Ltd.	CARE A-	CARE A
SK Finance Ltd.	CARE A+	CARE AA-
Federal Bank Ltd.	CARE AA	CARE AA+
Jindal Stainless Ltd.	CARE AA-	CARE AA
Bengal Aerotropolis Projects Ltd.	CRISIL BB+	CRISIL BBB-

Downgrades

Issuer name	Old rating	New rating
Rajasthan Rajya Vidyut Prasaran Nigam Ltd.	BWR BBB+(CE)	BWR BB+(CE)
Indiabulls Housing Finance Ltd.	CARE AA-	CARE A+
Indiabulls Commercial Credit Ltd.	CARE AA	CARE AA-
Vedanta Ltd.	IND AA	IND AA-
PTC India Financial Services Ltd.	CRISIL A+	CRISIL A

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