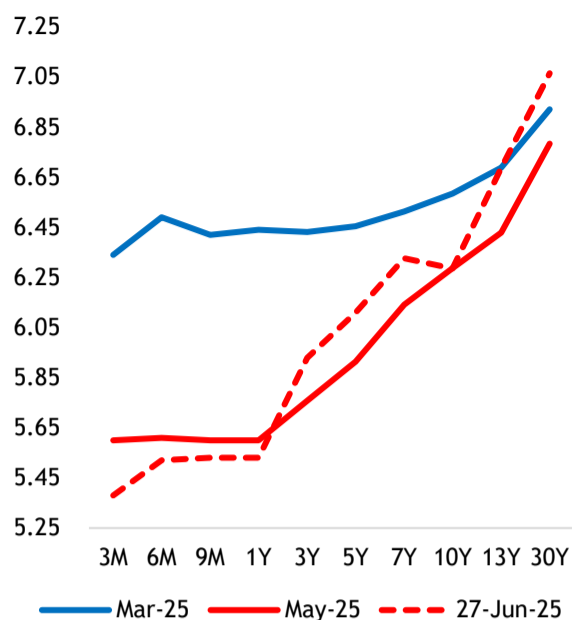


Fig.1: Surplus system liquidity and rate cut expectations keeping yield curve below 1 year flat



Source: Bloomberg, UBI Research

India led the global policy pivot, capitalizing on its disinflation advantage and domestic stability to deliver aggressive easing. The Reserve Bank of India (RBI) delivered a surprise 50 bps repo rate cut to 5.50% and a staggered 100 bps reduction in the Cash Reserve Ratio (CRR) to 3.0%, aimed at injecting Rs. 2.5 lakh crore in liquidity. This bold move, underpinned by cooling inflation (May CPI at 2.82%) and a downward revision in FY26 inflation forecast to 3.7%, marked a clear front-loading of policy support. Yet, bond markets remain cautious highlighting that policy support alone won't anchor yields unless transmission improves and liquidity is managed proactively. The 10-year G-Sec yield initially eased to 6.13% but firmed up post-policy, reflecting market reassessment of the RBI's simultaneous shift from an "accommodative" to a "neutral" stance, and expectations of limited policy space going forward. Liquidity remained in surplus, with money market rates trending below the repo rate, with RBI conducting a VRRR auction that lifted short-term yields indicating an evolving approach toward aligning WACR with policy stance (WACR moved to 5.38% on 27th Jun vs. 5.27% a day before). The curve steepened sharply at first, but hints of future liquidity management suggests a modest flattening ahead, led by the short end. Globally, six other central banks—the Federal Reserve, European Central Bank (ECB), Bank of England (BoE), Bank of Japan (BoJ), Swiss National Bank (SNB), and Norges Bank—set the tone for bond markets with mixed signals. The Fed held rates steady at 4.25%-4.50% amid soft macro data and rising geopolitical uncertainty, particularly in West Asia. US 10-year Treasury yields slipped 18 bps to 4.27% over the month, driven by weak retail sales, a sub-50 ISM Manufacturing print, and strong safe-haven demand. While the ECB cut rates by 25 bps as disinflation gained ground, the BoE and BoJ stayed on hold, citing sticky services inflation and uncertainty. SNB and Norges Bank surprised with 25 bps cuts amid easing price pressures. Meanwhile, tensions in the Middle East and uncertainty around US tariff policy (with the White House signaling flexibility on July deadlines) added a layer of risk premium—but markets found some relief as signs of de-escalation emerged by month-end.

Seven Central Banks announced their policy rates in Jun 2025:

- In June 2025, seven major central banks—including the Federal Reserve, European Central Bank (ECB), Bank of England (BoE), Bank of Japan (BoJ), Swiss National Bank (SNB), Norges Bank, and the Reserve Bank of India (RBI)—announced key policy decisions, setting the tone for global bond markets.
- Among the most impactful was the RBI's unexpected and front-loaded monetary easing, which included a 50 basis point repo rate cut to 5.50% and a 100 basis point phased reduction in the Cash Reserve Ratio (CRR) to 3%, aimed at injecting Rs.2.5 lakh crore in liquidity. This dovish pivot was accompanied by a shift in stance from "accommodative" to "neutral" and a downward revision in the FY26 inflation forecast to 3.7% from 4.0%. Meanwhile, the Federal Reserve held its policy rate steady at 4.25%-4.50% on June 18 but signaled the possibility of two cuts later in the year. Cooling US inflation data, weaker-than-expected economic indicators, and continued geopolitical uncertainty contributed to a decline in US 10-year Treasury yields—from around 4.45% at the start of the month to 4.27% by June-end.
- Across other major economies, the ECB cut rates by 25 basis points, bringing its deposit rate to 2.00%, as disinflation trends firmed across the Eurozone. This led to a modest softening in German Bund yields, which stabilized around 2.75%. The BoE maintained its policy rate at 4.25%, with markets continuing to price in a potential cut by August as UK inflation eased to 3.4%. In Switzerland, the SNB delivered a surprise 25 basis point cut to 0.25%, aiming to counter deflationary pressures and currency strength, which resulted in a brief spike in long-term bond yields due to repricing. Norges Bank also cut rates by 25 basis points, citing declining core inflation, while the BoJ kept its rate unchanged at 0.50%, prompting a slight uptick in Japanese yields. Heightened geopolitical risks, particularly in West Asia, led to short-lived increases in global yields due to oil-related inflation fears. However, persistent safe-haven demand and signs of de-escalation later in the month helped cap yields and stabilize broader market sentiment.

Fed kept the rates steady amid escalating geopolitical tensions in West Asia:

- The US 10-year Treasury yield declined from 4.45% on 01 Jun to 4.27% by 26 Jun, marking an 18 bps drop over the month. This easing reflected investor reaction to a series of weak macroeconomic prints. For instance, retail sales in May rose just 0.1% MoM, below the expected 0.3%, while the ISM Manufacturing Index for June came in at 48.2, remaining in contraction territory. These signs of economic deceleration lowered expectations for further monetary tightening and supported increased demand for Treasuries.
- The Federal Reserve kept the federal funds rate unchanged at 4.25-4.50% for the fourth straight meeting, aligning with market expectations. Policymakers emphasized a cautious approach as they continue assessing the broader economic impact of past policy decisions, particularly around tariffs, immigration, and taxation. While some uncertainty has eased, the Fed noted that risks to the outlook remain elevated. Despite this, it maintained projections for two rate cuts in 2025, with a more measured pace expected in 2026 and 2027—just one 25 bps cut in each of those years.
- The Fed revised its GDP growth forecast downward, projecting 1.4% for 2025 (down from 1.7%) and 1.6% in 2026 (vs 1.8%), while keeping the 2027 forecast unchanged at 1.8%. Inflation projections were revised upward, with the PCE inflation rate now seen at 3.0% in 2025 (vs 2.7%), moderating to 2.4% in 2026 (vs 2.2%) and 2.1% in 2027 (vs 2.0%). Chair Jerome Powell emphasized that the rate path is not fixed and reflects prevailing expectations amid considerable global and domestic uncertainty.
- Rising geopolitical tensions in West Asia, including U.S. military actions and threats to critical oil supply routes, introduced a significant risk premium into global markets. The resulting increase in oil prices intensified concerns over imported inflation and potential obstacles to global economic growth. These factors led to occasional spikes in U.S. Treasury yields as markets adjusted for higher inflation expectations. However, sustained geopolitical uncertainty also supported strong safe-haven demand, which helped contain the upward movement in yields. As the month progressed, signs of easing tensions—particularly related to Middle East developments and global trade—helped stabilize market sentiment and moderated yield volatility.
- The White House indicated that President Donald Trump may consider extending the upcoming deadlines for reinstating steep tariffs on imports from the majority of the world's countries. White House Press Secretary Karoline Leavitt told reporters that the July 8 and 9 deadlines for restarting these tariffs are "not critical." She added that while an extension is possible, the final decision rests with the president.

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India May'25 CPI cooled more than expected to 2.82% (Read our report - [May'25 CPI cools to sub 3% and validates front loading of rate cut](#)) :

- CPI inflation for the month of May'25 has fallen sharply to 2.82%, its lowest since Apr'19 vis-à-vis 3.16% in Apr'25. The key source of data surprise has come from sharper than expected cooling in food inflation especially cereals and pulses while vegetables inflation has seen a first uptick after six months of continued correction. Core CPI has however edged up to 4.18% in line with our projection from 4.10% in April'25.
- Uncertainty over global tariffs and geo-political tensions have contributed to the sharp rally in gold prices which has been instrumental in pulling up the core inflation in recent months: core inflation has gone up by almost 106 bps from 3.12% in May'24 to 4.18% in May'25. Interestingly, core-ex gold has continued to remain flat at 3.3%. Despite the slight uptick in core CPI, overall inflation dynamics stay comfortable.

MPC minutes re-confirms on providing certainty in times of uncertainty (Read our report - [India MPC Minutes](#)):

- RBI's June MPC minutes confirmed a bold, front-loaded monetary easing, with a 50 bps repo rate cut and a 100 bps CRR reduction, injecting around Rs. 2.5 lakh crore into the banking system. This policy move was anchored in a supportive inflation outlook—CPI fell to 3.2% in April and is projected at 3.7% for FY26, well below the 4% target, giving the central bank confidence to act decisively.
- While all six MPC members backed a rate cut, Saugata Bhattacharya advocated for a more cautious 25 bps cut, citing the limited remaining room for further easing. Governor Malhotra reinforced this caution, noting that after cumulative cuts totaling 100 bps since Feb, the policy space to support growth had become very limited. This remains aligned, in our view, with the Governor's latest media interview, asserting that policy space may open up if inflation is below the 3.7% projection for full year FY26.
- Prof. Ram Singh highlighted that real interest rates remain high (~1.65%) and, with inflation trending lower, justified the 50 bps front-loaded move. However, he also cautioned that, following earlier cuts, the scope for further easing is restricted to just 15-25 bps unless inflation undershoots.

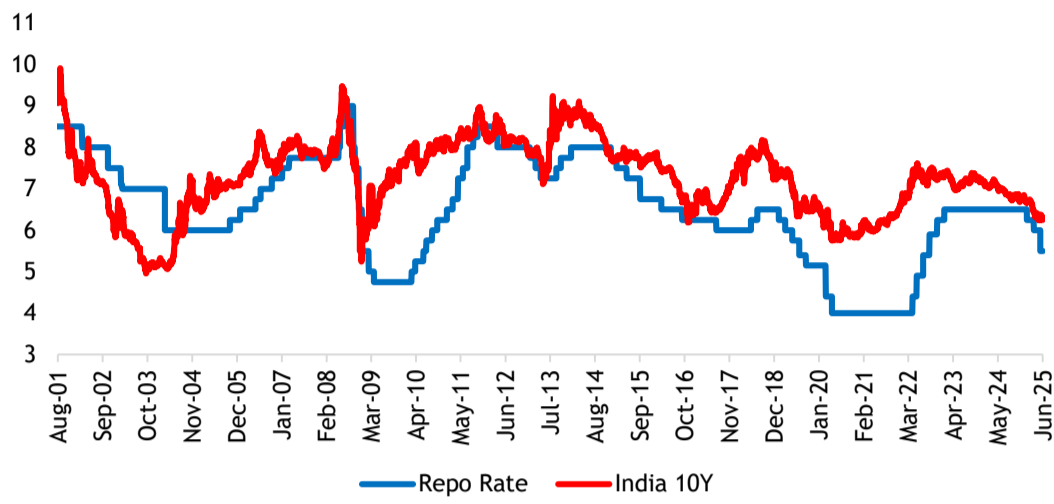
Liquidity, Money market and G-Sec yields:

- The banking system remained in surplus for the month of Jun'25 averaging Rs.2.74 lakh crore higher than previous month average of Rs.1.71 lakh core. The WACR was more aligned to SDF, below the repo rate, due to surplus fund in the system.
- As per RBI weekly data, the Govt. balance has lowered to Rs.2.0 lakh crore. With this the Core liquidity amounts to Rs.5.62 lakh crore. By end of Jun'25 we expect the liquidity to hover c.Rs.6.0 lakh crore on account of month end govt. spending.
- Credit growth trends reveal that the overall advances of the banking system have experienced a 9.0% growth, while deposits have seen a growth of 9.9% as of May 30, 2025. This expansion in the gap between credit and deposit growth (-92 basis points from -16 basis points in the last reported fortnight) indicates that banks are actively working to gather deposits.
- The 10-year benchmark yields moved to a low of 6.13% and shown a turn around on the day of MPC (06th Jun'25). The RBI, in its bi-monthly monetary policy on 06th Jun'25, announced a 50 bps repo rate cut to 5.50%, signaling a clear intent to frontload easing amid global uncertainties. In a more unexpected move, it also reduced the CRR by 100 bps to 3.0% of NDTL, last seen during the COVID period. The CRR cut will be implemented in four tranches starting September 6, 2025, releasing ~Rs 2.5 lakh crore of liquidity—aligned with the start of the busy credit season and the Governor's earlier liquidity assurance. The FY26 growth forecast was retained at 6.5%, while inflation was revised down to 3.7% (from 4.0%), with risks seen as balanced. Governor Sanjay Malhotra noted that while transmission of rate cuts is underway, it remains incomplete, even amid surplus banking system liquidity (Read our report - [Post RBI's policy gift to Banks; focus shifts towards transmission](#)).
- Despite the larger-than-expected 50 bps cut, 10-year bond yields firmed up, driven by:
 - **Frontloaded expectations:** Markets had largely priced in easing, with yields already down ~30 bps since April on anticipation of earlier cuts.
 - **CRR reduction impact:** Though liquidity supportive, the backloaded nature of the CRR cut reduced urgency for further OMOs unless short FX positions are unwound.
 - **Stance reversal:** The shift from "accommodative" (April 2025) back to "neutral" now suggests limited room for further cuts, reflecting a more cautious outlook.
 - **Governor's guidance:** With 100 bps already delivered since February and inflation easing, future actions will be data-dependent, with a balanced approach going forward.
- On 24th Jun'25, RBI announced VRRR auction to be conducted on 27th Jun'25 amounting to Rs.1.0 lakh crore. The VRRR announcement has led to spike in T-Bill cut offs with 6M & 12M to trade above repo rate of 5.50%. WACR has been trending at SDF levels since June MPC, despite the shift in policy stance to neutral. While it is not unusual for the WACR to slip below repo rate in times of surplus of surplus liquidity conditions, the guiding principle of liquidity management framework calls for WACR aligned with repo rate. We believe that the pace of uptick in WACR is likely to be gradual (given the [RBI Governor's views](#) on liquidity & transmission) and contingent follow up of VRRR announcements.
- The VRRR cutoff came in at 5.49%, as expected, close to repo rate with RBI accepting Rs.84,975 crore against auction of Rs.1 lakh crore. The WACR too jumped to trade at 5.39% on auction date as against 5.27% a day before.
- While some market participants expect the impact to be temporary, we see the use of VRRR as a trend shift, with likely use of the liquidity management tool to gradually align WACR (operating policy target) towards the repo rate even as average systemic liquidity is likely to stay comfortable at ~1% of NDTL range in coming months (assuming FX intervention related drag on liquidity, if any, is capped).
- The yield curve usually steepens at the end of the rate easing cycle(s), the recent trends reflect that (adequate) steepening has been clocked in the curve. However, as the RBI likely implements liquidity management steps to align call rate with repo rate, we expect slight flattening of the yield curve primarily led by the shorter end drifting higher.

Table 2: Market Snapshot		
	Yield (27 Jun)	Monthly Change
10 Year G-Sec (6.79% 2034)	6.40%	+12 bps
1 Year T-Bill	5.53%	-07 bps
US 10 year Yield	4.27%	-13 bps
Credit Growth (%) (as of 13 th Jun'25)	9.6%	-18 bps
Deposit Growth (%) (as of 13 th Jun'25)	10.4%	+41 bps
Credit Deposit Wedge (bps) (as of 13 th Jun'25)	(92)	-58 bps

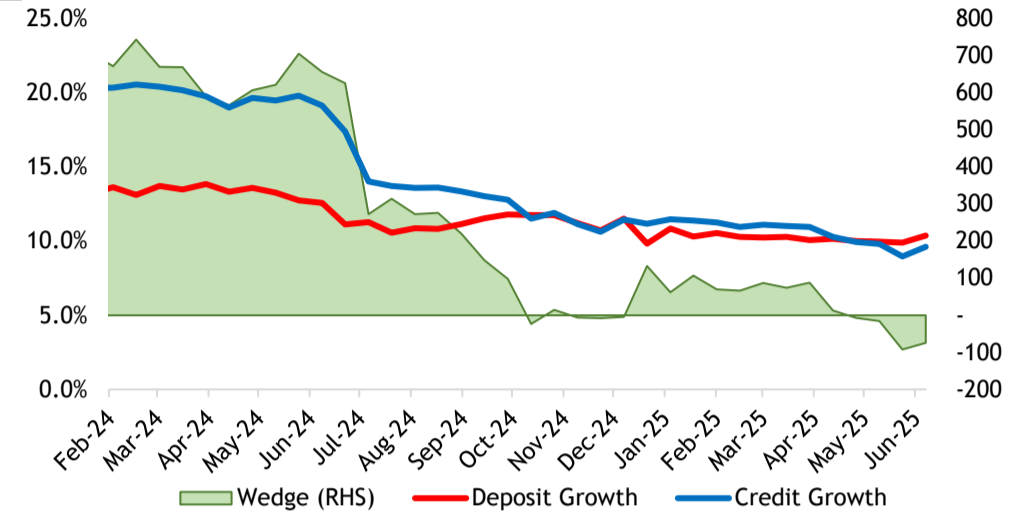
Source: RBI, CCIL, UBI Research

Fig.2: India 10 year Vs Repo Rate



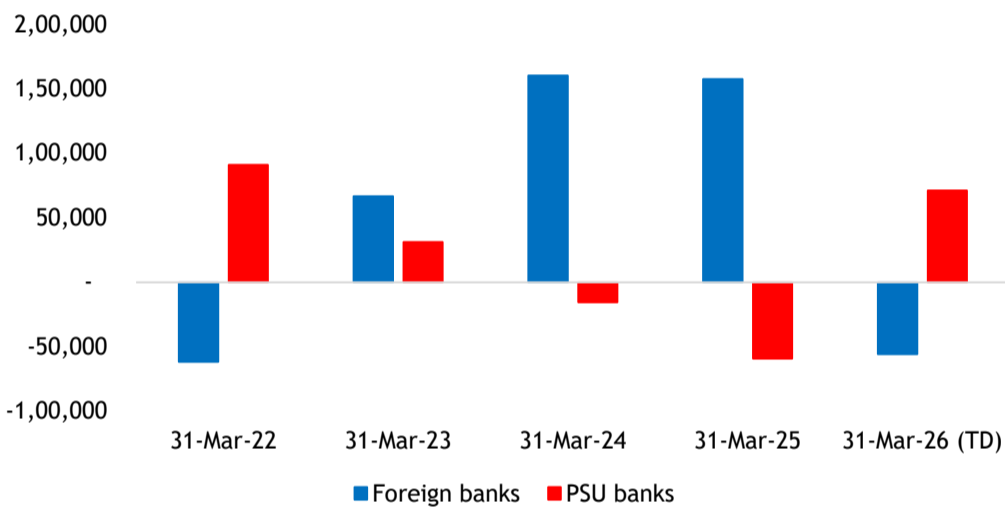
Source: RBI, UBI Research

Fig.3: Credit Deposit growth gap merged again showing banks' greater intent towards mobilising deposits



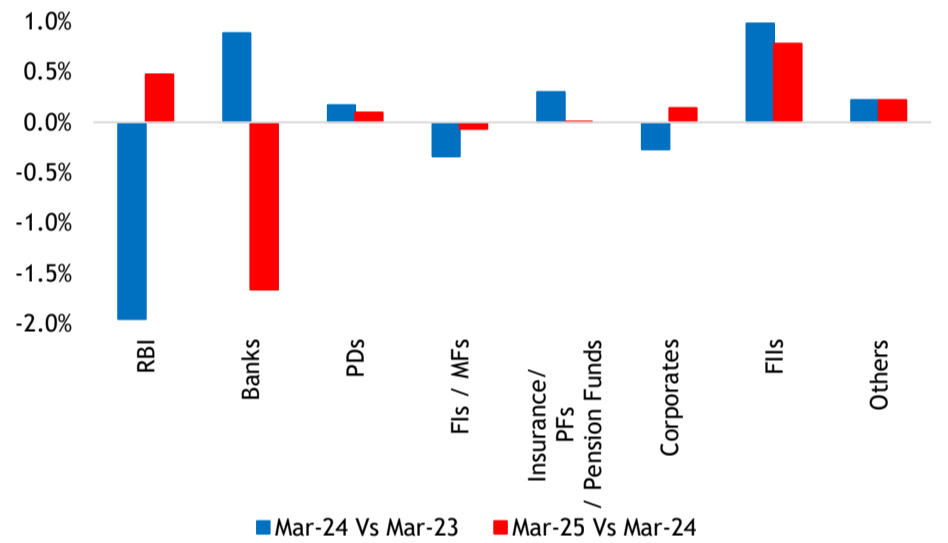
Source: RBI, CEIC, UBI Research

Fig.4: Foreign Banks were buyers and PSU Banks were sellers in past consecutive years, the trend has started to reverse in FY26



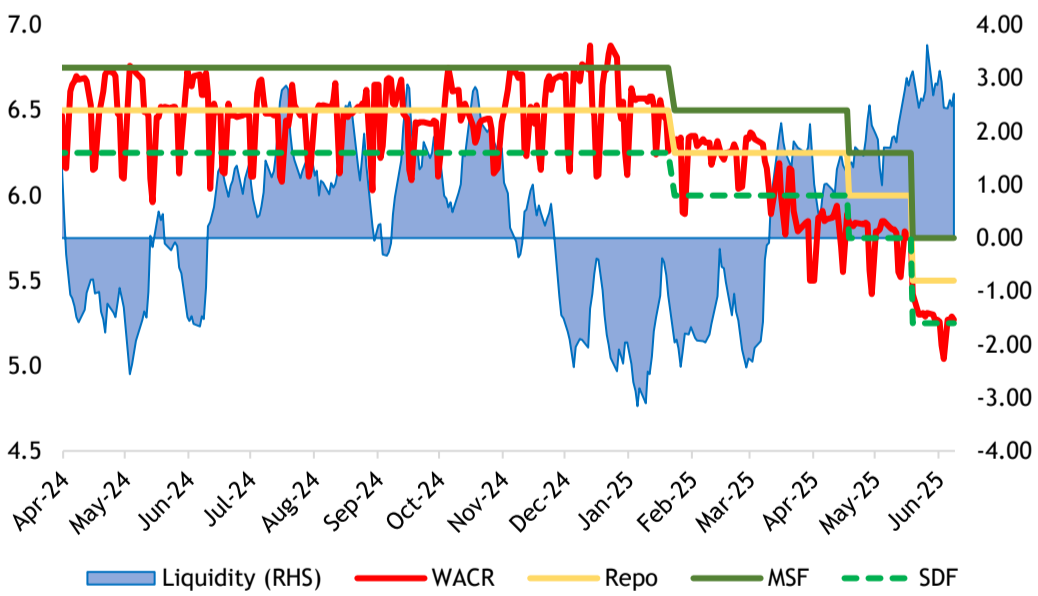
Source: Bloomberg, UBI Research

Fig.5: Ownership of Central Govt. Dated securities showing FIIs inclination



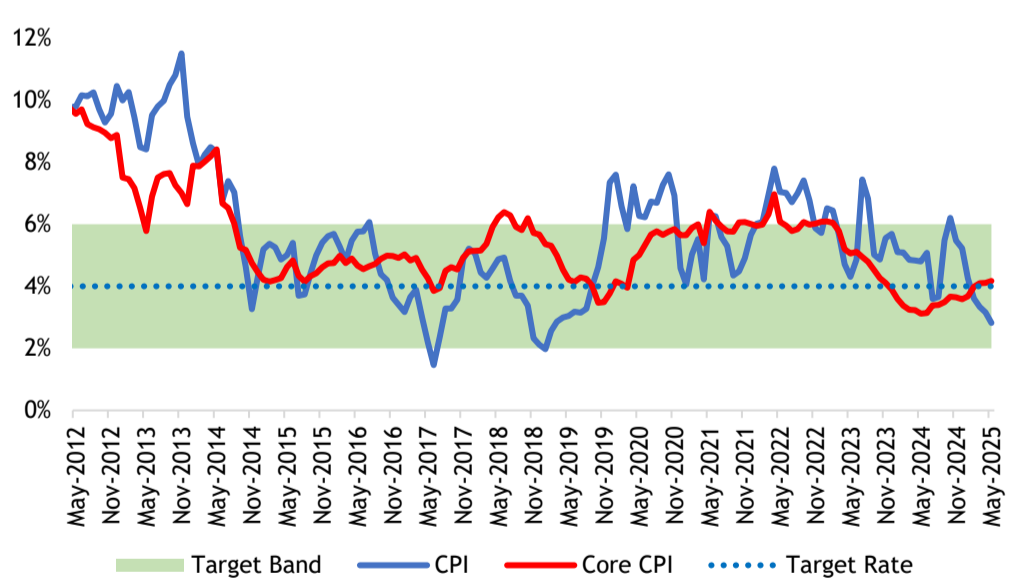
Source: CEIC, UBI Research

Fig.6: Surplus liquidity making its way back to SDF



Source: RBI, CEIC, UBI Research

Fig.7: Sequential uptick in Core CPI



Source: LSEG, UBI Research

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