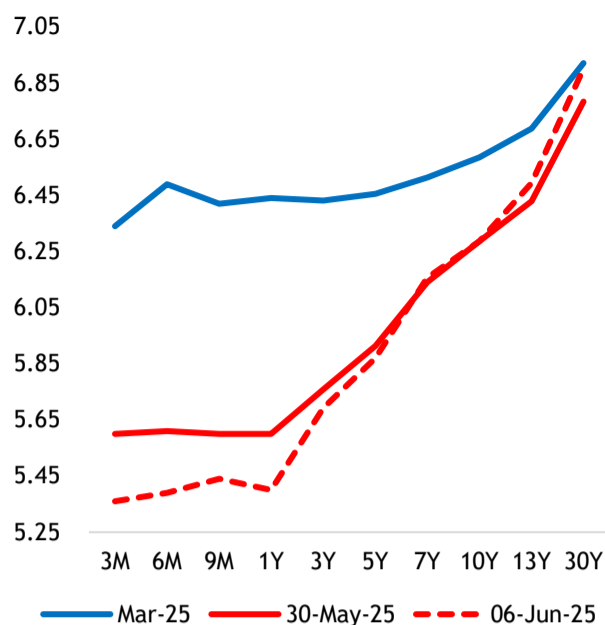
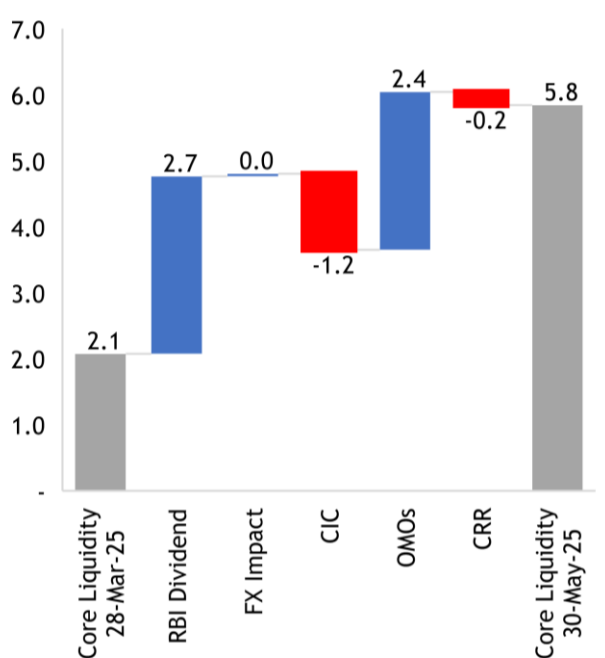


Fig.1: Surplus system liquidity kept yield curve steep



Source: Bloomberg, UBI Research

Fig.2: Drivers of liquidity showing impact of RBI steps



Fx Impact is net of LT Swap o/s of \$25Bn
Source: RBI, CEIC, UBI Research

The Fixed Income market saw a week of policy-driven action, with dovish central bank moves met by cautious market reactions. In India, the RBI surprised with a 50 bps repo rate cut and a staggered 100 bps CRR reduction starting September, aimed at frontloading support and injecting ₹2.5 lakh crore into the system. However, the quick shift in policy stance—from “accommodative” back to “neutral”—signaled a more cautious approach ahead, dampening expectations of further easing and triggering profit booking in government bonds. System liquidity remains in surplus, but with CRR cuts scheduled in H2 and rate cut hopes now moderated, the money market curve is likely to steepen. Globally, US Treasury yields edged higher as strong May jobs data pushed back Fed rate cut expectations, while President Trump’s new tariffs on steel and aluminium added to trade-related uncertainty. The ECB delivered a 25 bps rate cut but hinted at a pause, even as the OECD revised global growth forecasts lower.

US 10Y moved up after NFP data:

- US Treasury yields rose over the week, driven by robust May employment data and policy developments. The 10-year yield ended at 4.51%, up from 4.40% at the week’s start, while the 2-year yield closed at 4.04% and the 30-year at 4.97%.
- President Trump imposed new tariffs on steel and aluminium imports, escalating trade tensions. This move heightened concerns over global trade, contributing to market volatility and impacting risk sentiment.
- The US economy added 139,000 jobs in May, above expectations, with unemployment steady at 4.2%. This strong report reduced expectations for near-term Federal Reserve rate cuts. This robust jobs data reduced the likelihood of imminent Federal Reserve rate cuts, with futures markets pricing in a 97% probability that the Fed will keep rates unchanged at the June meeting.

ECB also nears end of rate cutting cycle

- The European Central Bank (ECB) lowered its deposit rate to 2% from 2.25%, its eighth cut and lowest since Dec’22 as the inflation has fallen below the 2% target. The ECB has projected the headline inflation to average in 2% in 2025 and 1.6% in 2026.
- The ECB signaled it may be nearing the end of its easing cycle, with President Christine Lagarde stating the central bank is now “in a good position.”
- According to OECD’s latest Economic Outlook, the global growth has slowed down from 3.3% in 2024 and 2.9% in 2025 and 2.26. GDP growth in US is projected to decline from 2.8% in 2024 to 1.6% in 2025 and 1.5% in 2026. In the Euro area, growth is projected to strengthen modestly from 0.8% in 2024 to 1.0% in 2025 and 1.2% in 2026.

RBI delivered more than what is asked for

- RBI in its bi-monthly monetary policy of FY’26 announced a 50bps repo rate cut to 5.50%, which shows a clear intent to frontload policy easing in an attempt to support the economy amid elevated global uncertainty.
- In a bigger surprise, the CRR was reduced by 100bps to 3.0% of NDTL (last seen during Covid), in a staggered manner. The CRR cut will be implemented in four tranches effective from fortnights beginning September 6, October 4, November 1 and November 29, 2025. It will align with the start of the busy credit season to provide liquidity boost of 1% of NDTL (Rs 2.5 lakh crore). It is also aligned with the Governor’s liquidity assurance of 1% of NDTL provided in April policy. The FY26 growth forecast was kept unchanged at 6.5%, while inflation projection was revised lower to 3.7% from 4.0% with risks evenly balanced.
- RBI Governor Sanjay Malhotra noted that credit transmission is yet to fully take effect despite ample banking system liquidity. He stated that the transmission usually occurs with a lag, though the liquidity surplus has aided the pass-through of repo rate cuts to short-term rates.
- Even with larger than expected rate cut of 50bps the 10 year bond yields hardened due to following key factors:
 - Anticipation priced in of rate cuts : The 25 bps rate cut was widely expected and had already been priced in by the bond market. With 50 bps of easing delivered earlier this year (25 bps each in Feb and Apr), the 10-year G-Sec yield had already dropped ~30 bps since April, factoring in expectations of further cuts. Alongside the rate action, the RBI also announced a phased CRR reduction—from 4% to 3%—to be implemented in four tranches of 25 bps each starting September through December. This move is expected to release around Rs.2.5 lakh crore into the system, improving liquidity conditions and supporting credit flow, particularly as system liquidity tends to tighten in the second half of the year. While CRR cut is backloaded our estimates show that possibility of OMOs has turned lower unless RBI provides delivery of a large amount of short dollar position due in next 12 months.
 - Quick shifting of stance from “Accommodative” to “Neutral” : It was only in the April 2025 MPC meeting that the policy stance was shifted to “accommodative” from “neutral,” which had buoyed market sentiment. However, the RBI’s swift move back to a “neutral” stance within such a short span signals a more cautious approach, indicating that the scope for further rate cuts may now be limited. This reversal has tempered market expectations of additional easing for the remainder of the year.
 - RBI Governor’s Comments: The RBI Governor highlighted that with inflation revised lower to 3.7% and growth still subdued, front loading rate cuts was necessary to support demand. However, with 100 bps already delivered since February 2025, policy space is now limited. Hence, the MPC shifted its stance back to neutral, indicating a more cautious approach ahead, with future actions to be guided by incoming data and evolving macro conditions.

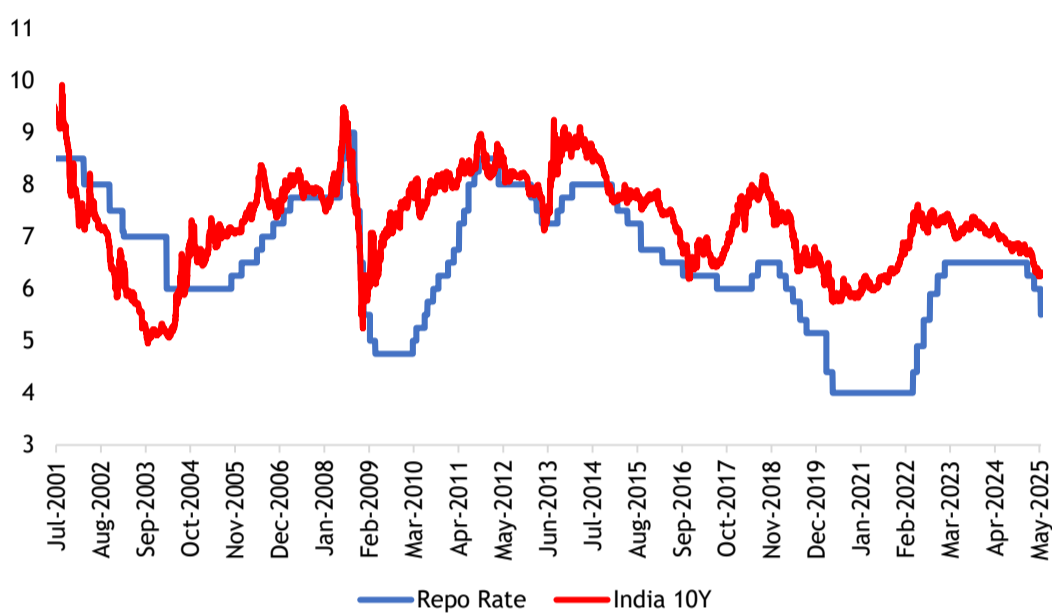
Liquidity dynamics may steepen money market curve

- As per latest weekly data by RBI, Core Liquidity as of 30th May’25 is Rs.5.84 lakh crore with a govt. balance of Rs.3.6 lakh crore as major contributor post RBI dividend bounty in the previous week. Government spending continues to boost banking system liquidity and with CRR cut becoming effective from Sep’25 we expect steepening of the money market curve.
- The spread between G-Sec 10Y yield and repo rate has moved to more than 75 bps (c.25bps in previous week) post 50bps cut in repo rate triggered by the sell off in domestic bond market.
- On the market activity front, during the previous week Mutual Fund and PSU banks were sellers led by Primary Dealers, whereas, Foreign Banks, Private banks along with others were on buying side. It is to note that PSU Banks and Mutual Funds were on buying side for the month of May.
- Going ahead, it will be interesting to watch for traction in 10 year and longer end G-Sec yield curve post market stabilizes around the new policy regime as it sold off even with a 50bps rate cut.

Table 1: Market Snapshot Instrument	Yield (Jun 06)	Weekly Change	Commentary
10 Year G-Sec (6.79% 2034)	6.29%	- bps	Yields jumped post MPC decision of 50bps rate cut with stance shifting to "Neutral"
1 Year T-Bill	5.40%	-20 bps	Surplus liquidity in system shifted T-Bills yield lower
US 10 year Yield	4.51%	+11 bps	NFP came better than expectations strengthening NIL rate cut in Jun meeting
Credit Growth (%) (as of 16 th May'25)	9.8%	-5 bps	Credit Deposit wedge closure continues with credit slow down
Deposit Growth (%) (as of 16 th May'25)	9.9%	-14 bps	
Credit Deposit Wedge (bps) (as of 16 th May'25)	(16)	-9 bps	

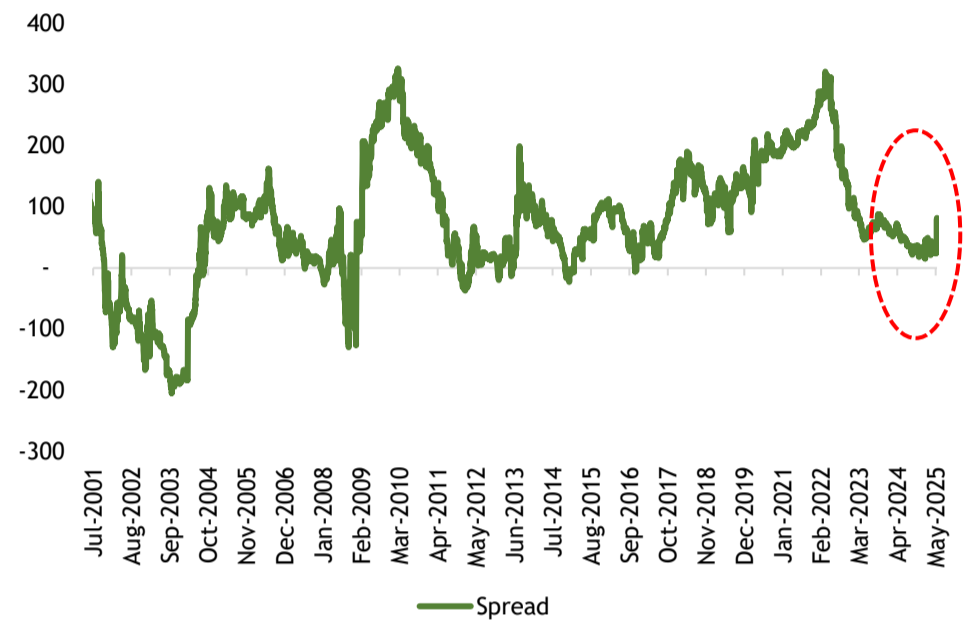
Source: RBI, CCIL, UBI Research

Fig.3: India 10Y and Repo rate over the years



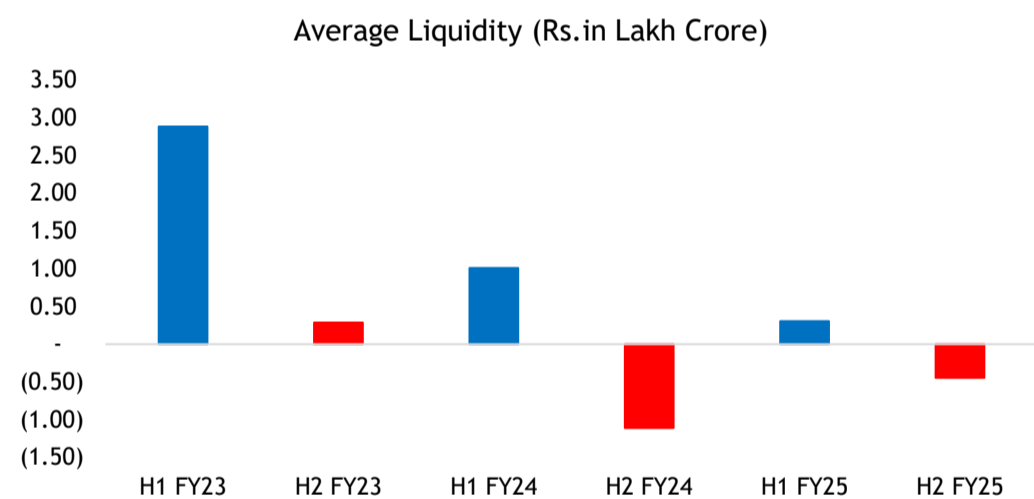
Source: Bloomberg,CEIC,UBI Research

Fig.4: The spread between India 10Y yield and repo rate bounced from lows



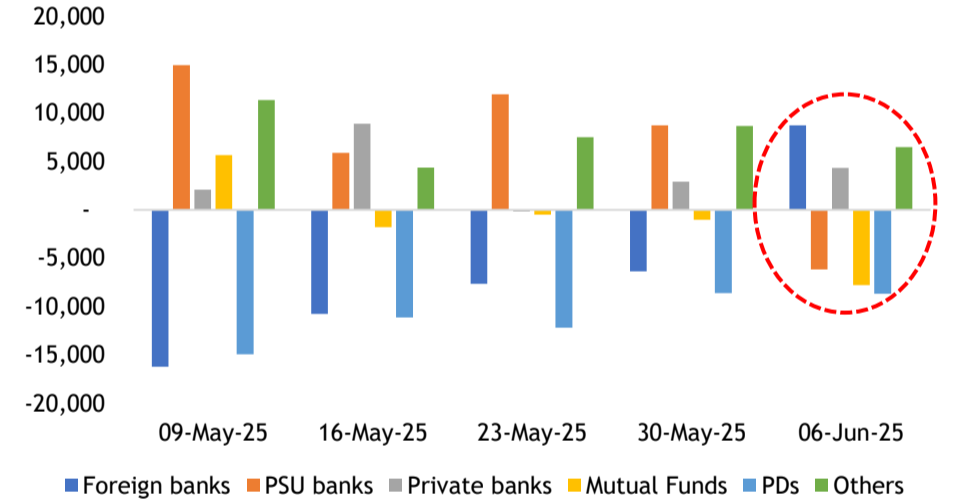
Source: Bloomberg,UBI Research

Fig.5: Average liquidity usually stays lower in H2 of the financial year, CRR cut in Sep'25 may support in current FY26



Source: Bloomberg, UBI Research

Fig.6: On weekly basis, Mutual Funds turned to be sellers in the last week ending 06th Jun'25



Source: Bloomberg, UBI Research

Table 2: Fixed Income tracking Heatmap

Fixed Income Heatmap	Apr-24	May-24	Jun-24	Jul-24	Aug-24	Sep-24	Oct-24	Nov-24	Dec-24	Jan-25	Feb-25	Mar-25	Apr-25	May-25
Growth														
PMI Manufacturing (YoY Gr%)	58.80	57.50	58.30	58.10	57.50	56.50	57.50	56.50	56.40	57.70	56.30	58.10	58.20	57.60
PMI Services (YoY Gr%)	60.80	60.20	60.50	60.30	60.90	57.70	58.50	58.40	59.30	56.50	59.00	58.50	58.70	61.20
GST Collection (YoY Gr%)	12.42	9.96	7.63	10.28	9.99	6.47	8.92	8.54	7.26	12.29	9.09	9.89	12.58	16.39
Govt Expenditure (YoY Gr%)	39.26	-37.87	-18.42	0.12	20.94	2.63	31.65	3.63	22.15	12.43	-17.66	9.65	9.95	
Vehicle registrations (% y/y)	26.90	3.51	1.64	14.10	3.50	-7.46	33.58	13.85	-11.46	7.69	-5.39	0.64	3.23	5.09
Exports (% y/y)	1.98	13.27	2.44	0.63	-9.93	-0.30	16.57	-5.30	-1.53	-2.62	-11.08	0.66	9.03	
Imports (% y/y)	11.07	7.30	4.64	11.19	9.97	7.77	1.89	16.10	2.32	10.31	-16.34	11.36	19.13	
Inflation														
CPI (Y-o-Y Gr%)	4.83	4.80	5.08	3.60	3.65	5.49	6.21	5.48	5.22	4.26	3.61	3.34	3.16	
Core CPI (Y-o-Y Gr%)	3.23	3.12	3.14	3.39	3.40	3.49	3.67	3.64	3.58	3.67	3.99	4.10	4.10	
Transmission														
Bank Credit (YoY Gr%)	19.21	20.72	17.40	13.71	14.03	12.34	11.80	11.16	11.16	12.53	12.26	11.03	9.93	
Bank Deposits (YoY Gr%)	12.56	14.02	11.12	10.57	12.72	10.38	11.50	11.25	9.83	12.12	12.01	10.28	9.89	
C-D Ratio (%)	79.90	79.90	79.70	79.70	78.80	79.60	79.80	79.90	80.80	80.60	80.80	81.10	79.90	
WALR O/s Rupee Loans (%)	9.81	9.81	9.89	9.89	9.89	9.88	9.88	9.87	9.86	9.85	9.78	9.75	9.68	
WALR Fresh Rupee Loans (%)	9.55	9.39	9.32	9.40	9.41	9.37	9.54	9.40	9.25	9.32	9.40	9.35	9.26	
WADR O/s (%)	6.91	6.92	6.91	6.92	6.93	6.95	6.96	6.98	7.00	7.02	7.02	7.04	7.01	
WADR Fresh (%)	6.48	6.47	6.46	6.48	6.46	6.54	6.44	6.47	6.58	6.57	6.49	6.65	6.30	
MCLR 1 Year - Median	8.85	8.79	8.85	8.85	8.93	8.95	8.95	9.00	9.00	9.00	9.05	9.00	9.00	

Source: CEIC, UBI Research

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