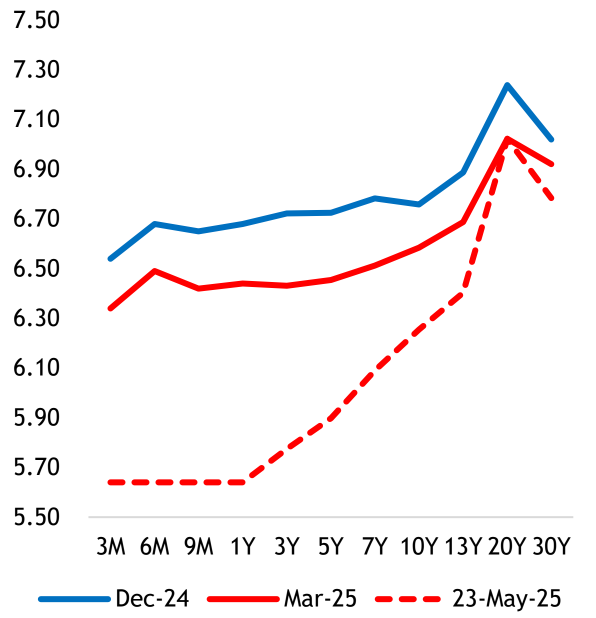
India FI Weekly: US India 10Y spreads at two decadal low

27th May 2025

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



Source: Bloomberg, UBI Research

The India-US 10 year benchmark spread has undergone a structural transformation over the past two decades reflecting India's emergence as a more stable investment destination. As of 23rd May 2025, the spread between India and US 10 year is 174 bps marking the lowest in history significantly narrowing when US yields rallied and India 10 year dipped. Historically, the spread has been much wider indicating higher risk perception associated with Indian G-Secs compared to US Treasuries. The current compressed spread highlights important shifts in relative risk perception for Indian currency & bonds and US fiscal deficit, inflation concerns coupled with weakening dollar. RBI dividend announcement post market hours last week was much awaited yet a lower than consensus number (UBI estimate of Rs 2.5-3.0 lakh crore proved right) was non-market moving. Over the weekend, US President Donald Trump plan to impose 50% tariff on the EU, which was subsequently delayed until 09th July.

Moody's downgrade coupling of 'big beautiful' tax bill sent yields on upswing:

- Moody's has downgraded the U.S. sovereign credit rating from AAA to Aa1, citing a sustained rise in debt and interest payment ratios. The agency also noted that growing borrowing needs are likely to place further strain on the US fiscal outlook.
- US house of representatives passed a sweeping tax and spending bill with a single vote margin. It will add about $3.8 trillion to the federal government's $36.2 trillion in debt over the next decade. The 1,100-page proposal intends to prolong the corporate and individual tax cuts that were approved in 2017 during Trump's first term, revoke many of the green-energy incentives that were established by former Democratic President Joe Biden, and impose stricter eligibility requirements for health and food assistance programs for those in poverty.
- The uncertainty surrounding fiscal policy due to tax legislation has disrupted global bond markets, worsening investor concerns that had already intensified in the wake of Moody's downgrade of the US credit rating. The US 30 year bond yield surged to its highest level since 2023, surpassing 5%, while 10 year benchmark yield climbed by 18bps as compared to previous week close of 4.44%. Global bond markets saw ripple effect as Japan and Germany bond market saw sell-off.
- The US dollar index fell under 99, reaching its lowest level in more than a month, as the euro strengthened following President Donald Trump's choice to postpone the application of 50% tariffs on the European Union until July 9. Trump made the announcement after a call with European Commission President Ursula von der Leyen, who described the discussion as "good" but pointed out that further time was needed to "achieve a satisfactory agreement."

India US yield spread narrowed to two decadal low

- As of May 23, 2025, the yield spread between India's 10-year government bond and the U.S. 10-year Treasury has narrowed to 174 basis points, marking the lowest level in over 20 years. This significant compression is the result of a rally in US Treasury yields alongside a decline in Indian 10-year bond yields.
- Historically, the spread has been much wider, reflecting a higher risk premium demanded by investors for holding Indian sovereign debt over US Treasuries. The current historically low differential signals a meaningful shift in market perceptions — with improved confidence in India's macroeconomic stability and fiscal discipline, contrasted against growing concerns over the US's fiscal trajectory, persistent inflation pressures, and a weakening dollar.
- The narrowing spread is attributed to :
    - Fiscal Policy: Aggressive fiscal measures including significant tax cuts have led to increased US yields
    - Debt to GDP ratio: Wide gap in Debt as GDP ratio, US with 121% and India at 83%
    - Monetary Policy: RBI has maintained a more cautious approach resulting in relatively stable Indian bond yields.

RBI dividend bounty curtailed on expanded CRB

- RBI announced its dividend payout to Centre on 23rd May'25 after market hours, amounting to Rs.2.69 lakh crore, in line with our estimate of Rs.2.5-3.0 lakh crore (Our Report: Drop in domestic yields amid global headwinds). However, it is still higher than the FY26 budgeted figures and last year's dividend of Rs.2.11 lakh crore.
- We believe that the revision in ECF with hike in buffers to 6 +/-1.5% is very prudent during times of global and domestic economic uncertainty. Despite the ECF revision and raising of contingency reserve buffer to upper end of threshold limit of 7.5% from 6.5% last year, with an absolute impact of ~Rs 75,000 crore, the RBI has been able to announce a strong dividend number. With the number higher versus budgeted by ~ Rs 60,000 crore (0.15% of GDP) the RBI has managed to provide fiscal leeway to the central government.

Liquidity and Money market

- The banking system remained in surplus for most of the week (19th to 25th May'25) averaging Rs.1.60 lakh crore lower than previous week of Rs.2.04 lakh core. The WACR averaged 5.81%, below the repo rate, signaling excess fund in the system.
- The T-bill cut off remained bullish at 5.71% down by 13bps from previous week showing comfort in lower tenures due to surplus liquidity.
- The 10-year benchmark yields moved to a low of 6.25% with anticipating RBI dividend of approx.Rs.2.5-3.0 lakh crore and easing inflation (CPI) numbers providing room for further rate cuts as real rates expands. Post announcement of RBI dividend, the 10-year benchmark yields moved slightly from 6.25% to 6.24% (on 26th May'25), as it looked already priced in.
- Markets currently looking forward to GDP data for FY25 due on 30th May'25. We are estimating a growth of 7.0% for Q4FY25 and our revised estimates for FY25 is lowered to 6.3%. Hence, the government's second advance estimate of 6.5% for FY25 faces downside risks as it implied 7.6% growth in Q4, which is very ambitious in our view (Our report: India's GDP growth likely clocked 7.0% in Q4FY25). MPC decision which due from 4th to 6th Jun is likely to be impacted by lower GDP, hence, markets look forward to factor in further rate cuts.

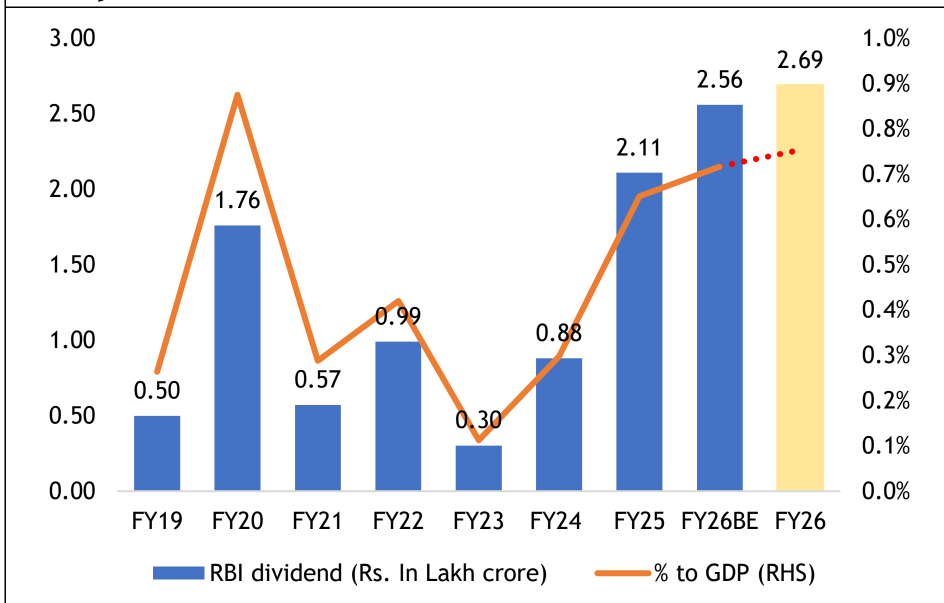
By:
Kanika Pasricha
kanika.pasricha@unionbankofindia.bank

Dhiraj Kumar
dhirajkumar@unionbankofindia.bank

Table 1: Market Snapshot Instrument	Yield (May 23)	Weekly Change	Commentary
10 Year G-Sec (6.79% 2034)	6.26%	-1 bps	Actual RBI dividend lower than anticipated by market & further room for rate cuts on easing CPI
1 Year T-Bill	5.66%	-11 bps	Lower cut-off signals strong demand amid surplus liquidity
WACR (avg.)	5.79%	+23 bps	Dipped below to repo on multiple days, reflecting surplus liquidity
US 10 year Yield	4.51%	+03 bps	Fear of fiscal expansion due to tax bill
Credit Growth (%)	9.9%	-34 bps	Credit Deposit wedge closed first time since Mid-December
Deposit Growth (%)	10.0%	-15 bps	
Credit Deposit Wedge (bps)	(6)	+19 bps	

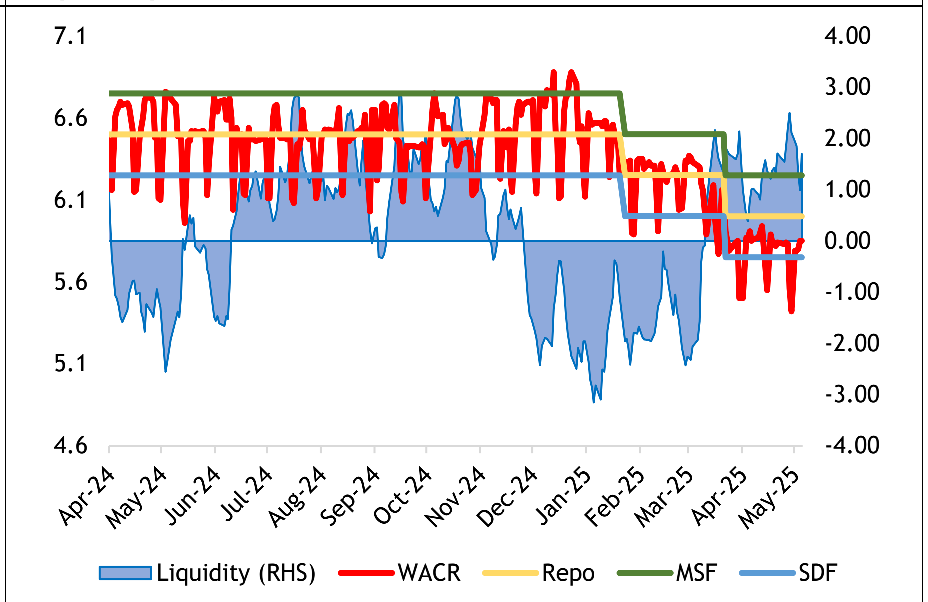
Source: RBI, CCIL, UBI Research

Fig.2: RBI dividend exceeded the FY26BE opening up scope for Fiscal leeway



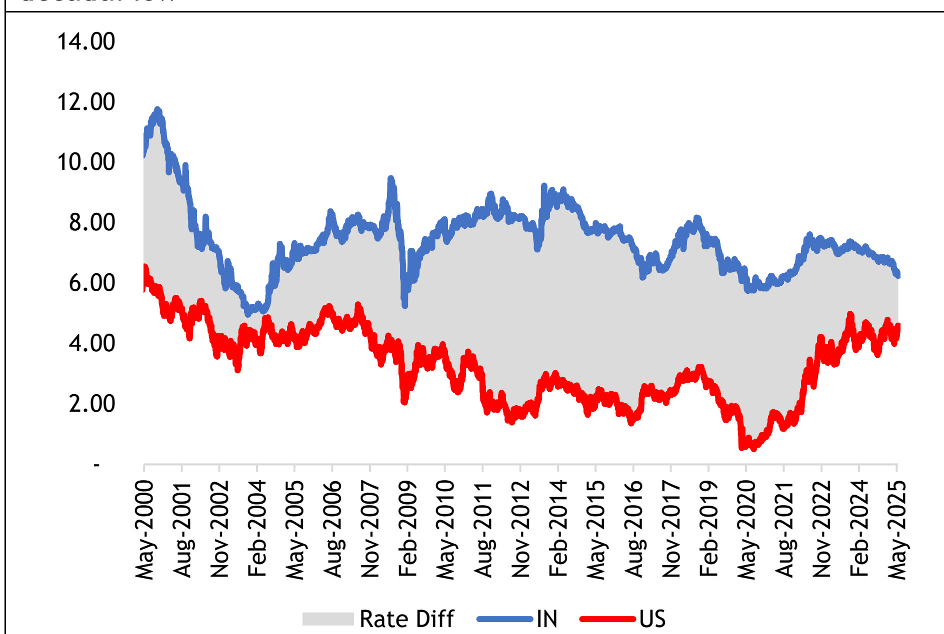
Source: RBI, UBI Research

Fig.3: WACR on the lower band of LAF as system is flushed with surplus liquidity



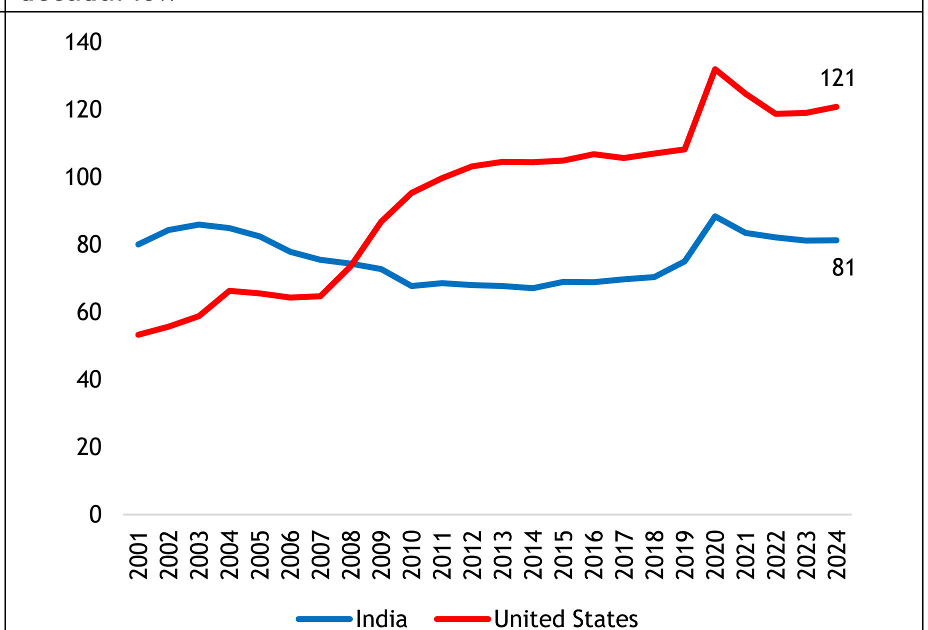
Source: RBI,CEIC, UBI Research

Fig.4: India US 10 year benchmark interest rate differential at two decadal low



Source: Bloomberg, UBI Research

Fig.5: India US 10 year benchmark interest rate differential at two decadal low



Source: IMF, UBI Research

Table 2: Fixed Income tracking Heatmap

Fixed Income tracking	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
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
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
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
Bank Credit (YoY Gr%)	18.82	20.72	17.40	13.71	14.03	12.34	11.80	11.16	11.16	12.53	12.26	11.03	10.28
Bank Deposits (YoY Gr%)	12.28	14.02	11.12	10.57	12.72	10.38	11.50	11.25	9.83	12.12	12.01	10.28	10.15
C-D Ratio (%)	79.80	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	
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	
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	
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	
MCLR 1Year - 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
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		

Source: CEIC, UBI Research

Banking Research Team	
Kanika Pasricha **Chief Economic Advisor**	**kanika.pasricha@unionbankofindia.bank**
Suneesh K	suneeshk@unionbankofindia.bank
R Gunaseelan	gunaseelan@unionbankofindia.bank
Nidhi Arora	nidhiarora@unionbankofindia.bank
Rajesh Ranjan	rajeshranjan@unionbankofindia.bank
Jovana Luke George	jovana.george@unionbankofindia.bank
Amit Srivastava	asrivastava@unionbankofindia.bank
Rohit Yarmal	rohitdigambar@unionbankofindia.bank
S. Jaya Laxmi	s.jayalakshmi@unionbankofindia.bank
Dhiraj Kumar	dhirajkumar@unionbankofindia.bank
Akash Deb	akash510@unionbankofindia.bank
Shreyas Bidarkar	shreyas.bidarkar@unionbankofindia.bank