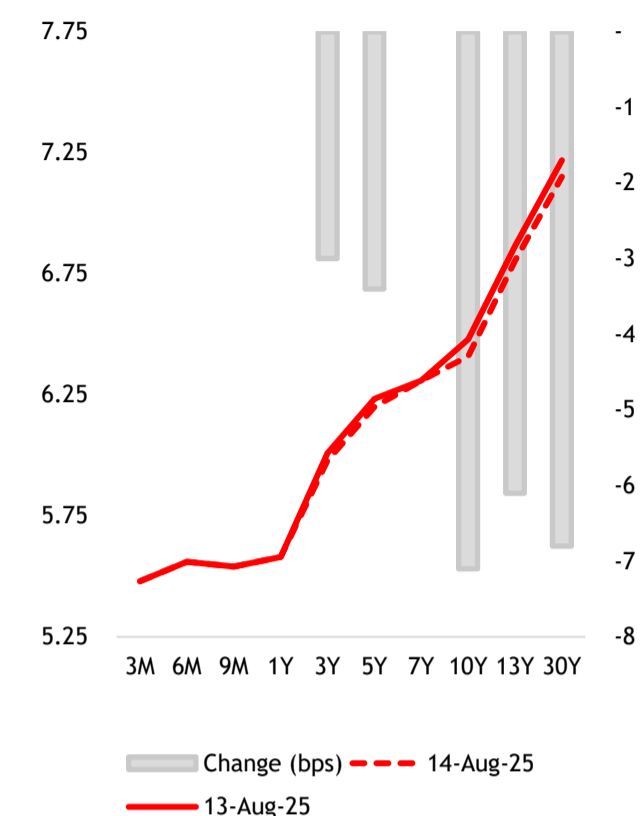


Fig.1: Higher duration yield softened on rating upgrade news; (% , bps)



Source: Bloomberg, UBI Research

Table 1: Tax Multipliers for GST rate cuts are higher than income tax rate cuts:

Variable	Impact Multipliers
Goods and Service Tax Multiplier	-1.08
Personal Income Tax Multiplier	-1.01
Corporate Tax Multiplier	-1.02

Source: NIPFP paper 'Fiscal Multipliers for India' By Sukanya Bose & N R Bhanumurthy; UBI Research

India received a long overdue S&P Global Ratings upgrade to 'BBB' after a gap of eighteen years. S&P cited strong macro fundamentals, sustained fiscal discipline, and policy continuity as drivers of the upgrade. The Finance Ministry noted this could reduce government borrowing costs, with yields already reflecting optimism: the 10-year benchmark fell 8 bps to 6.40%, supported by Rs.2,415 Crore in FPI inflows via the FAR route. The bond rally confirms the constructive stance outlined in our recent research, which highlighted stronger risk-reward in longer-duration G-Secs amid easing inflation and rate cut prospects. Meanwhile, Prime Minister Modi's Diwali-time GST overhaul focusing on rate rationalisation and simplified structures aims to lower inflation for general consumers. Together, these developments reinforce the long-term narrative of growth resilience and fiscal consolidation that underpinned the rating upgrade. Additionally, Fin Min officials post the upgrade also assured there will be no supply glut, with gross borrowing in FY26 capped at Rs.14.82 lakh crore.

S&P rating upgrade long overdue:

- S&P Global Ratings has upgraded India's long-term sovereign credit rating to 'BBB' from 'BBB-', and its short-term rating to 'A-2' from 'A-3', citing the country's robust economic fundamentals, institutional reforms, and sustained fiscal consolidation. This marks India's first rating upgrade by the global rating agency after a gap of 18 years, moving it one notch above the lowest investment grade. S&P attributed this decision to India's strong GDP trajectory, resilient monetary policy, and enhanced quality of public spending. The agency forecasts GDP growth at 6.5% for FY26 (April-March), aligning with the RBI's estimates, and an average 6.8% over the subsequent three years, supported by solid consumer demand and government-led capital investment. India's limited exposure to the US, exports to the US form only 2% of GDP, means the 50% US tariff on Indian goods is unlikely to materially impact growth. Similarly, any pivot away from Russian crude oil, which now constitutes 25% of India's oil imports (up from 2.7% in FY22), would have limited fiscal impact due to narrowing global price differentials.
- India's debt profile is improving steadily, while lower nominal GDP poses fiscal risks still on a statistical basis risk is low as nominal GDP level used in Budget was lower. General government debt is projected to decline from a pandemic-era high of 91% of GDP to 83% in FY25, reaching 78% by FY29, as per S&P estimates. The agency projects general government fiscal deficit to fall from 7.3% of GDP (looks comfortable to achieve, in our view) to 6.6% by FY29. S&P also highlighted the role of political stability in ensuring macroeconomic stability and policy predictability factors that support India's long-term creditworthiness.
- India's external and monetary metrics further strengthen its sovereign profile, with current account deficits expected to remain modest at 1.0% of GDP in FY26 and between 1.3 to 1.4% until FY29.
- S&P highlighted India's strong monetary framework, noting that inflation has remained within the 2-6% target range, averaging 5.5% over the past three years and falling to an eight-year low of 1.55% in July. However, further upgrades will depend on the government's ability to reduce fiscal deficits and manage debt sustainably.
- S&P rating upgrades, as per media reports signals a thaw in US-India relations and with Trump-Putin meeting ending on a peaceful note with next meeting also proposed in Moscow is a positive. Trump has also signalled that the additional 25% penalty will not be levied on India for import of Russian oil from 27th Aug'25.

PM's Diwali Gift of GST rate rationalisation likely to bode well for Inflation dynamics:

- The honourable Prime Minister in his 79th Independence Day speech announced a major overhaul of the Goods and Services Tax (GST) regime by Diwali. The reform is aimed at easing inflationary pressure on essential items in an attempt to boost consumption and supporting MSMEs.
- As per media reports, the GST overhaul would include removal of the 12% and 28% slabs while the 5%, 18% And 40% (sin tax) slabs would continue. Currently, if we map CPI basket weights with GST rates, c. 45% are in Nil slab (mostly food items), c.17-20% each are in 5% & 18% slab, while 12% and 28% slabs (due for rationalisation) map c.3-5% each of CPI basket with the 40% slab having c.10%. While it is too early to assess the inflation impact given details are awaited, media sources indicate a possible relief in terms of inflation for consumers, with: i/ taxes on discretionary consumption goods like air conditioners, TVs, refrigerators, washing machines etc may see GST rate cut from 28% to 18%, ii/ long awaited demand for cut in GST rate on cement from 28% to 18% may be accepted, and iii/ Items currently taxed at 12% like certain apparel (garments above Rs 1000, facing inverted duty structure), processed food, building materials, electronics, and some services are expected to move to 5% slab.
- From fiscal perspective, while there are concerns of a revenue loss, it needs to be clearly noted that the estimates of tax multiplier for GST rate cut is the highest at -1.08 while that of personal income tax is -1.01 (Table 1). GST rate cut will have a wider population impact while income tax cut only affects ~4% of population (taxpayer base). Hence, revenue loss, if any, is likely to be capped. More importantly, the items moved to 40% slab (sin tax and part of GST compensation cess) will be key to watch as well to determine the fiscal impact. In-fact, the outstanding amount in the compensation cess fund also provides fiscal buffers in the current year, given the government's estimate of a rise from Rs. 61,210 cr (FY25 RE) to Rs. 1.24 lakh cr in FY26 (BE).

We remain constructive on Long Duration bonds:

- Post announcement of rating upgrade, the benchmark 6.33%, 2035 bond ended the day at a yield of 6.40%, compared to 6.48% on Wednesday, an 8-bps drop, the largest single-day fall since April 2. The 15-year and the 5-year gilts also saw yields decline by over 8 bps and 3 bps, respectively. The new 7.24%, 2055 bond closed at 7.1585% yield of which auction cut-off was 7.24%. However, gains were capped as traders booked profits and remained cautious ahead of global events including the Trump-Putin meeting.
- The rating upgrade prompted a notable uptick in foreign portfolio activity, with FPIs purchasing Rs.2,415 Crore in government bonds via the Fully Accessible Route (FAR) on Thursday alone. Market participants see the S&P upgrade as a sentiment booster but remain cautious about its near-term impact on sustained inflows or bond performance.
- As highlighted in our research weekly dated 11th Jul'25, the rally in longer-dated G-Secs aligns with our constructive view that these bonds offer better risk-reward versus the shorter end under current conditions.
- With inflation easing, the RBI having already cut 100 bps in repo rate this year, and another 25-50 bps cut likely in the final leg of the easing cycle, long-duration bonds offer investors an opportunity to lock in yields in a relatively stable environment. The Centre's clear signal of no supply glut (media report dated 16th Aug'25) and continued focus on borrowing discipline further strengthens our conviction for a favourable duration bias.
- We will re-assess our trade post final announcement of GST reforms (close to Diwali) with greater clarity on possible inflation and fiscal impact.

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