CareEdge RATINGS

CareEdge

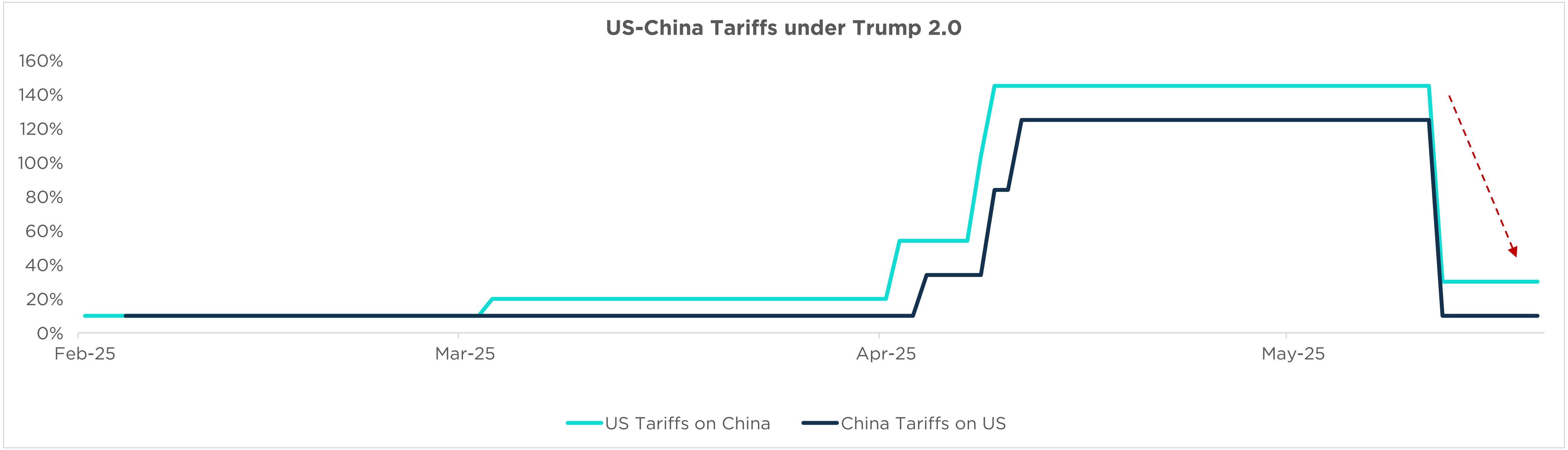
Debt & Forex Market Update

May 2025

Contents

Key Global Developments

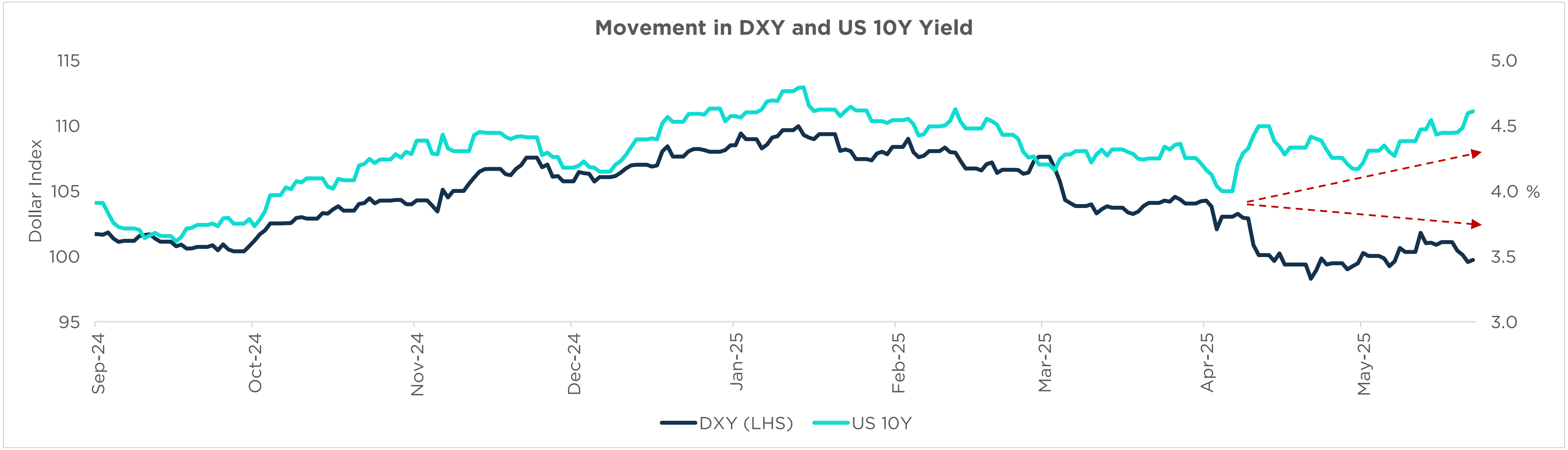
Trade Tensions De-escalate



Source: Official Sources

- The US and China agreed to a 90-day tariff truce, with deeper-than-expected tariff cuts.
- The US and UK announced a trade deal. The deal includes a 10% reciprocal tariff (as originally announced on 02 April), reduced tariffs on the first 100,000 vehicles imported into the US by UK car manufacturers each year, and the removal of US tariffs on UK steel and aluminum. The deal is also expected to expand US market access in the UK, creating a USD 5 billion opportunity for new exports for US farmers, ranchers, and producers.
- Trade negotiations between the US and other countries are underway. While US tariffs are expected to stay above pre-Trump 2.0 levels, they are likely to be lower than feared – easing global growth concerns.

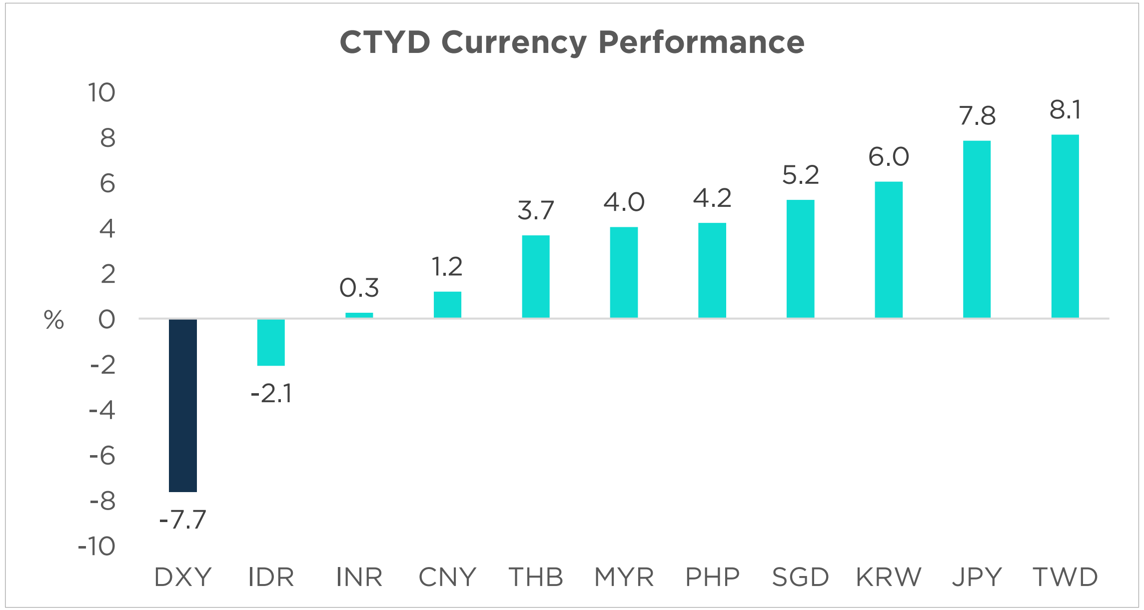
Markets Turn Focus to US Fiscal Risks



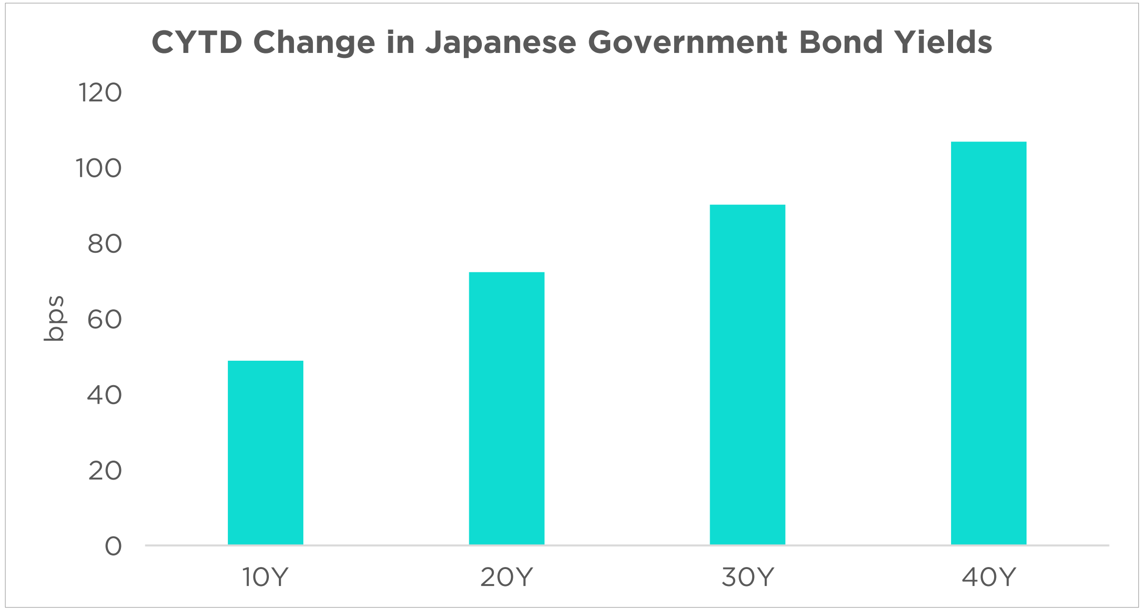
Source: Refinitiv. Data as of 21 May

- US fiscal concerns are in focus as a tax bill under consideration could increase the US deficit by USD 3.8 trillion over the next decade, according to the Congressional Budget Office.
- The US 10Y yield has surged by around 40bps in May to 4.6% (as of 21 May) amidst fiscal worries.
- Markets are now pricing in two Fed rate cuts in 2025 – down from four – due to easing recession risks.
- The dollar index remains weak near 100, well below its January peak of around 110.

Asian Currencies Strengthen & JGB Yields Rise



Source: Refinitiv. Note: Negative values imply currency has weakened. DXY measures the dollar's performance against a basket of currencies, while the performance of other currencies is measured against the USD.



Source: Refinitiv. Data as of 22 May

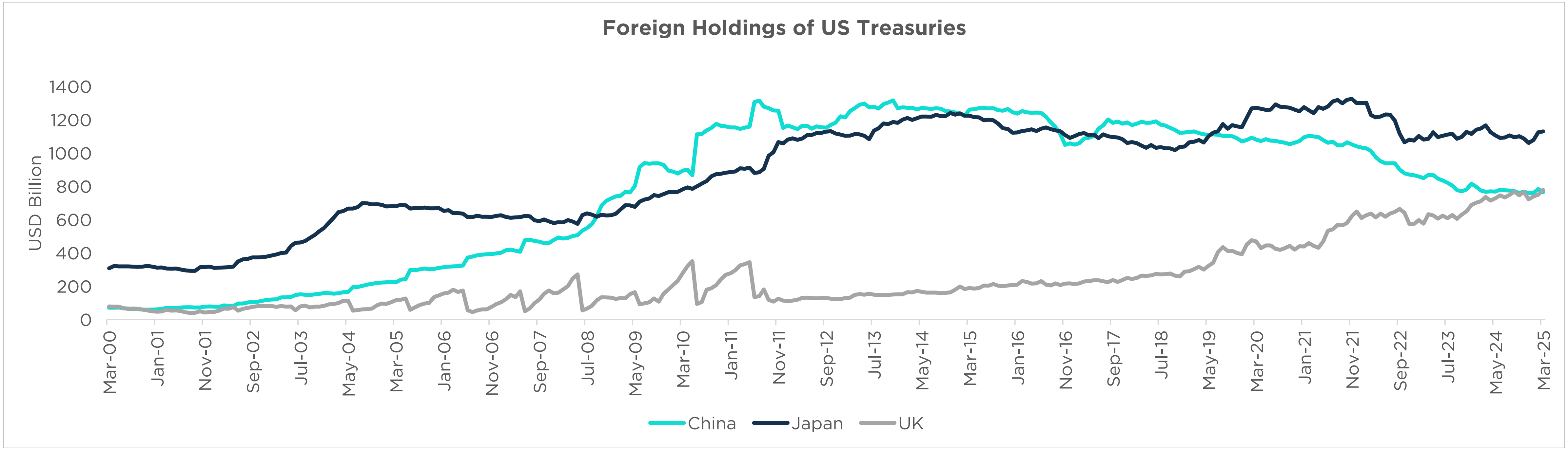
- Asian currencies have generally strengthened CYTD supported by a weaker dollar and the 90-day US-China tariff truce – with the exception of IDR.

- Notably, the Taiwan dollar has appreciated 8% CYTD, with most gains in early May. This was driven by a confluence of factors including:

a) Speculation that Taiwan may allow a stronger TWD to support trade negotiations with the US.
b) A weaker dollar environment, prompting exporters to convert their dollar earnings, while life insurers increased hedging demand.
c) Strong foreign capital inflows, following Taiwan's better-than-expected Q1 GDP growth.

- Japanese government bond (JGB) yields have risen CYTD amidst elevated inflation and as BoJ unwinds ultra-loose monetary policy. Weak demand at a recent auction has also put pressure on long term yields.

China's US Treasury Holdings Fall Below the UK's

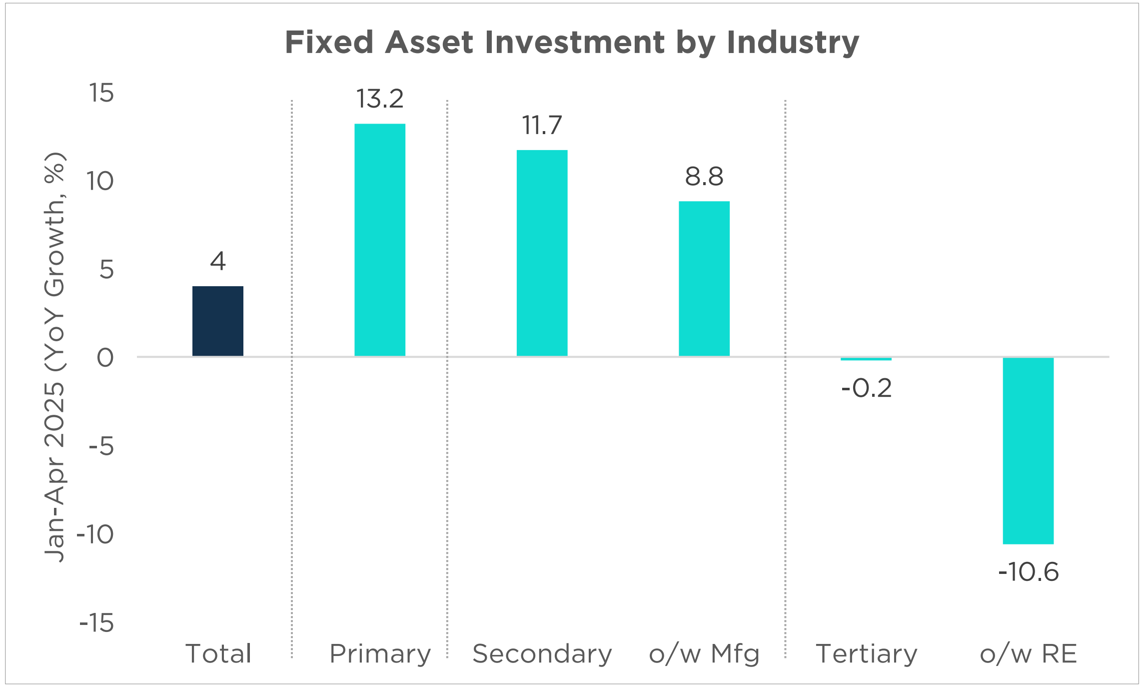


Source: CEIC, US Department of the Treasury

- In March, total foreign holdings of US Treasuries rose by USD 233 billion to around USD 9 trillion. While China's holdings fell by USD 19 billion to USD 765 billion, the UK's holdings rose by USD 29 billion to USD 779 billion, making it the second-largest foreign holder after Japan.
- The decline reflects China's ongoing diversification away from US assets since 2013.
- However, China is also believed to hold US Treasuries through third-party custodians, which may understate its official holdings. Additionally, the data is only available till March and does not capture any potential sell-off following Trump's Liberation Day announcement, which led to a sharp rise in US yields.

China: Strong Exports, Weak Property Sector

Source: CEIC, General Administration of Customs

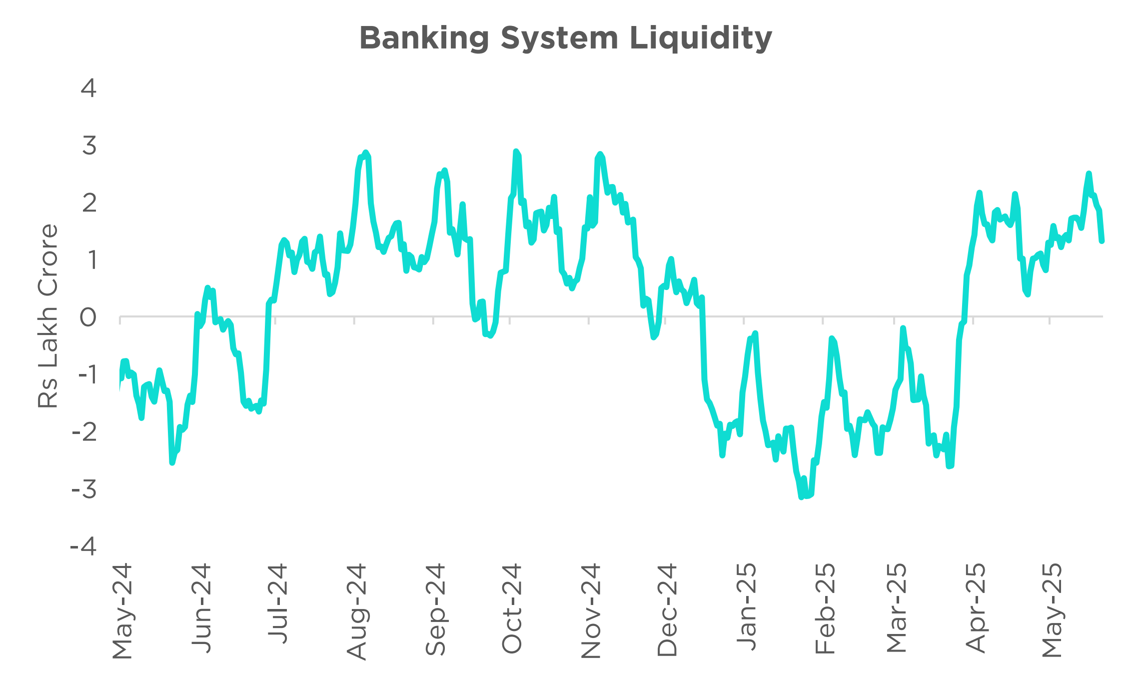


Source: CEIC, National Bureau of Statistics of China
Note- o/w: of which; Mfg: Manufacturing; RE: Real Estate

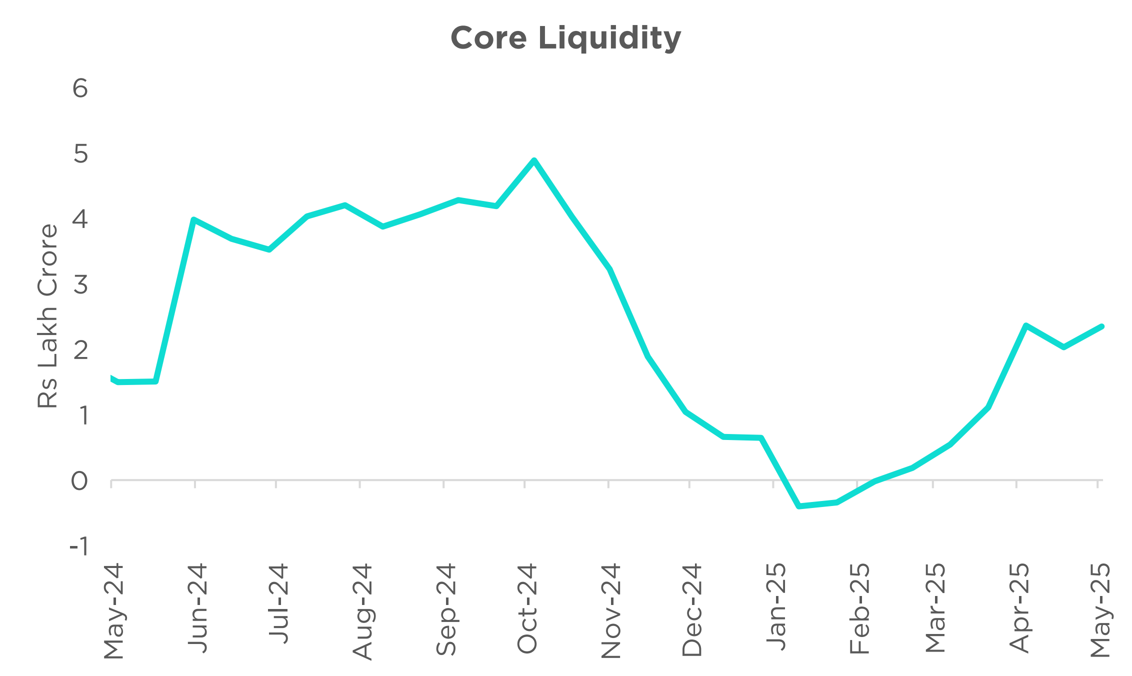
- China's exports rose 8.1% YoY in April, well above the 1.9% market estimate, though exports to the US fell by 21%. The 90-day US-China tariff truce may support near-term exports through front-loading of orders.
- Real estate investment fell 10.6% YoY in January-April period, highlighting continued weakness in the sector which is keeping domestic consumption subdued.
- In May, the PBoC cut key lending rates to record lows and reduced the reserve requirement ratio by 50bps. Further, monetary policy easing is expected to support growth.

India Debt & FX Market Trends

Liquidity Surplus Increases Further



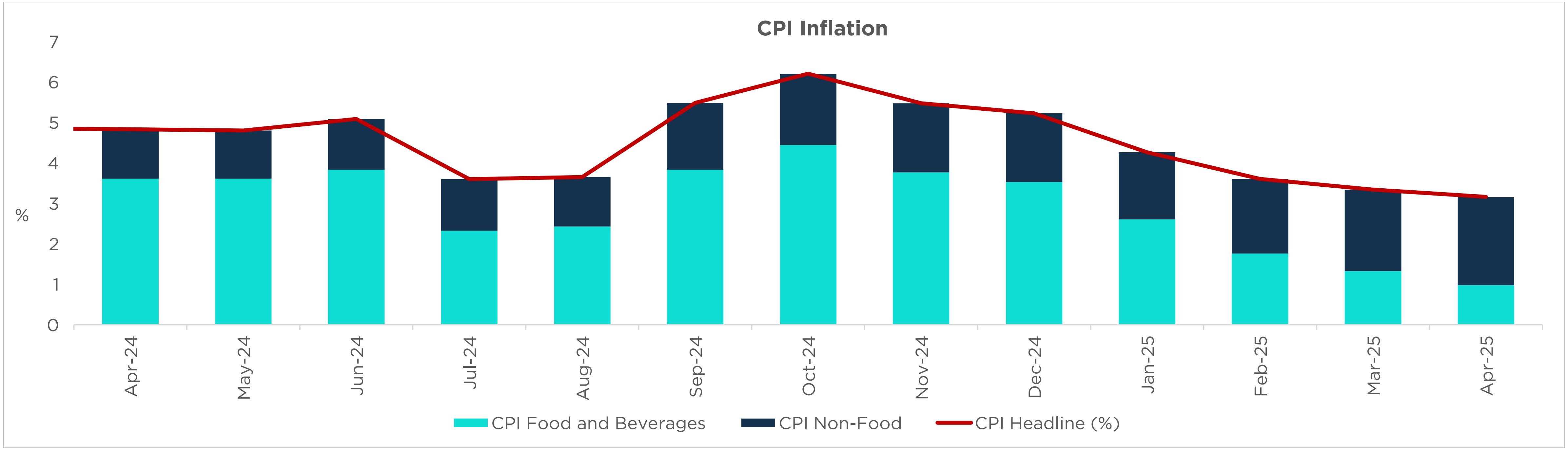
Sources: RBI, CEIC. Data as of 21 May
Negative values denote liquidity deficit.



Sources: RBI, CEIC. Data as of 02 May
Core liquidity includes government cash balances. Negative values denote liquidity deficit.

- Average banking system liquidity surplus stood at Rs 1.7 lakh crore in May (up to 21 May), equivalent to about 0.7% of NDTL.
- Core liquidity surplus rose to Rs 2.3 lakh crore as of 02 May. RBI conducted OMO purchases of around Rs 1.19 lakh crore in May (up to 20 May).
- On average, the WACR was 24bps below the policy rate in May (up to 21 May), due to surplus liquidity in the system.
- Looking ahead, liquidity is expected to remain comfortable, with likely RBI dividend of Rs 2.5- 3 lakh crore in Q1 FY26.

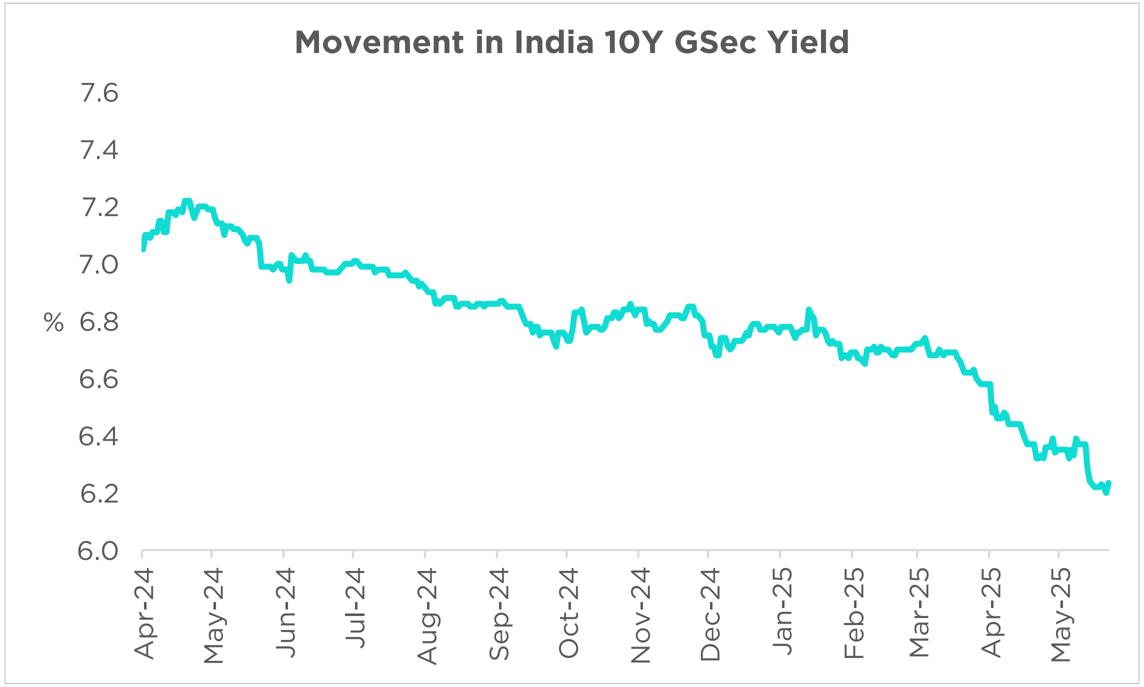
CPI Inflation Eases



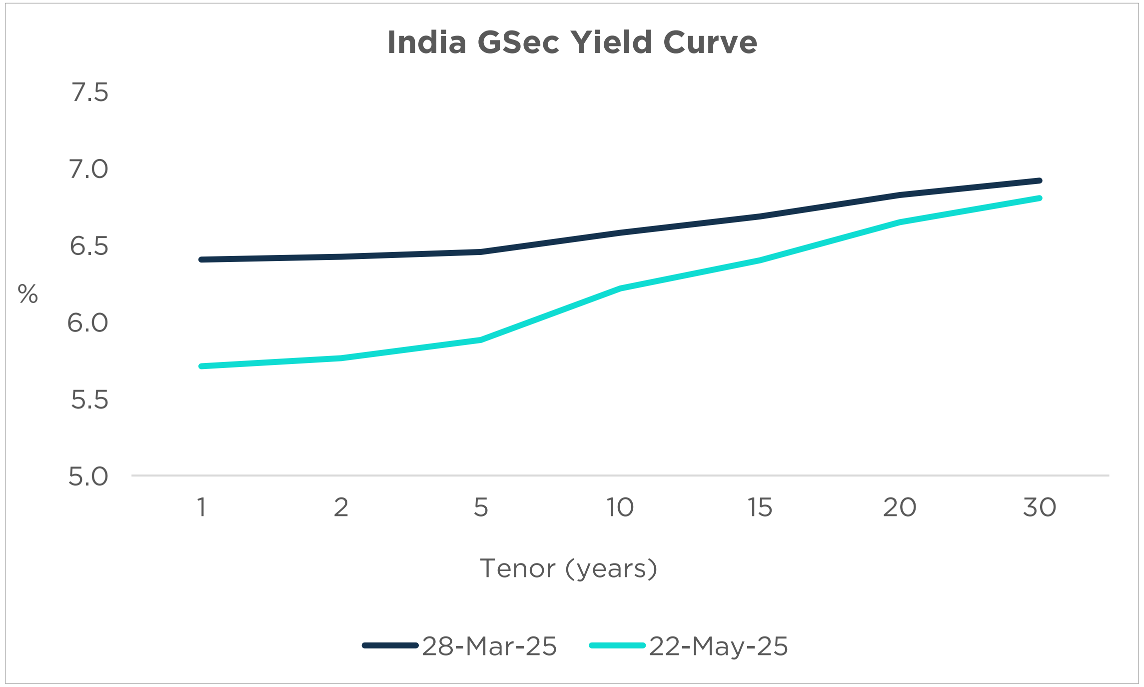
Sources: MOSPI, CareEdge

- Headline CPI inflation eased to 3.2% in April, the lowest since August 2019 and below 4% for the third straight month.
- Softening food and beverage inflation supported the moderating in CPI inflation.
- Core inflation remained unchanged at 4.1% in April.
- CPI inflation is expected to stay comfortable, averaging 4.2% in FY26. This opens room for further monetary policy easing. We expect the RBI MPC to cut the policy rate by another 50bps in FY26, with chances of a deeper rate cut cycle if growth falters.

India 10Y GSec Yield Declines



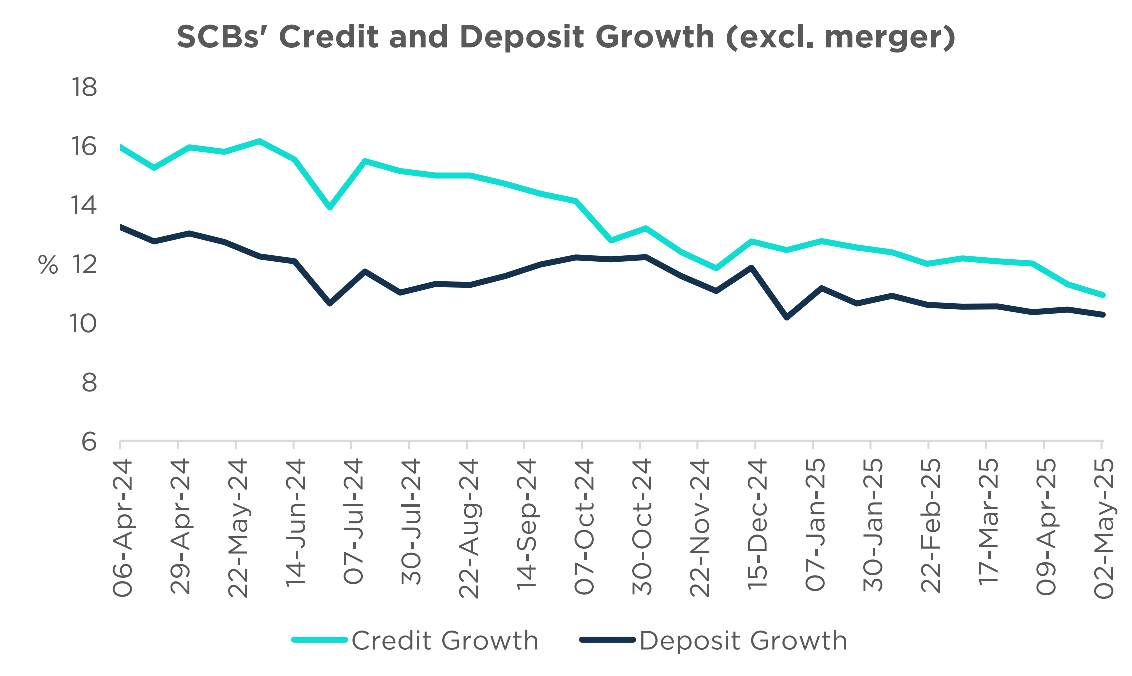
Source: Refinitiv. Data as of 22 May



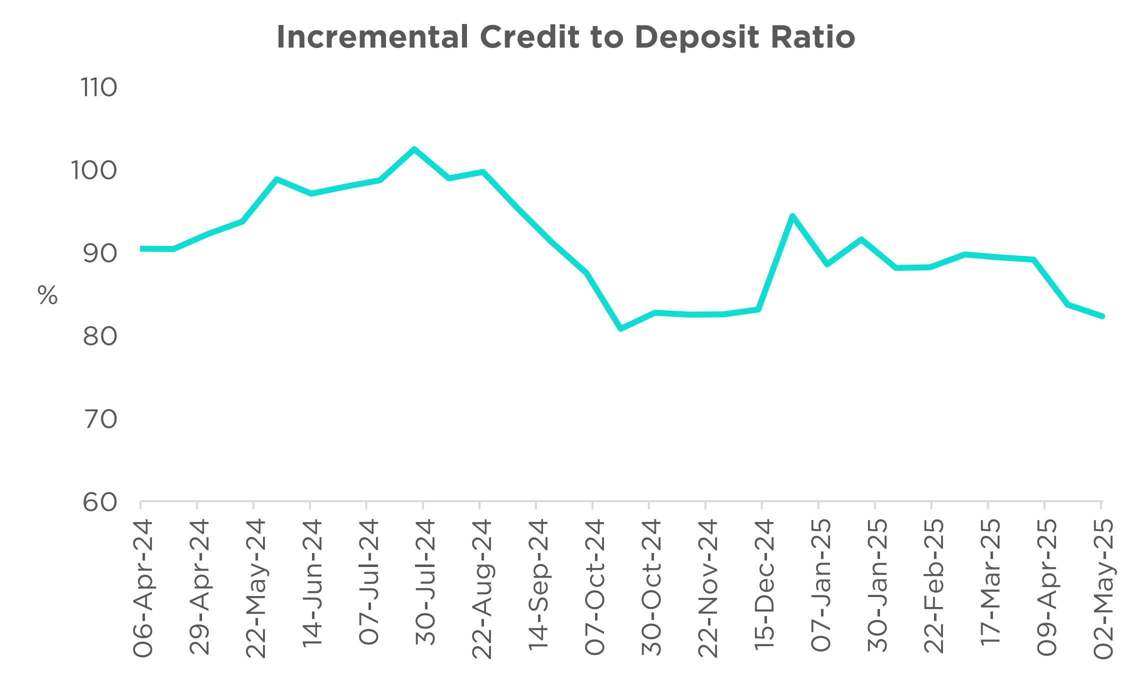
Source: Refinitiv

- India 10Y GSec yield eased by around 35bps since March to 6.23% as of 22 May - supported by RBI's OMO purchases, a dovish MPC, and easing inflation.
- Improving liquidity conditions have also softened yields across tenors, leading to a downward shift in the yield curve.
- Market focus is on the upcoming RBI dividend announcement, expected at Rs 2.5-3 lakh crore.
- Rising UST yields warrant monitoring, though their recent co-movement with Indian yields has weakened.
- We expect India 10Y GSec yield to trade in the 6.0-6.2% range by end-FY26.

Bank Credit & Deposit Growth Slows



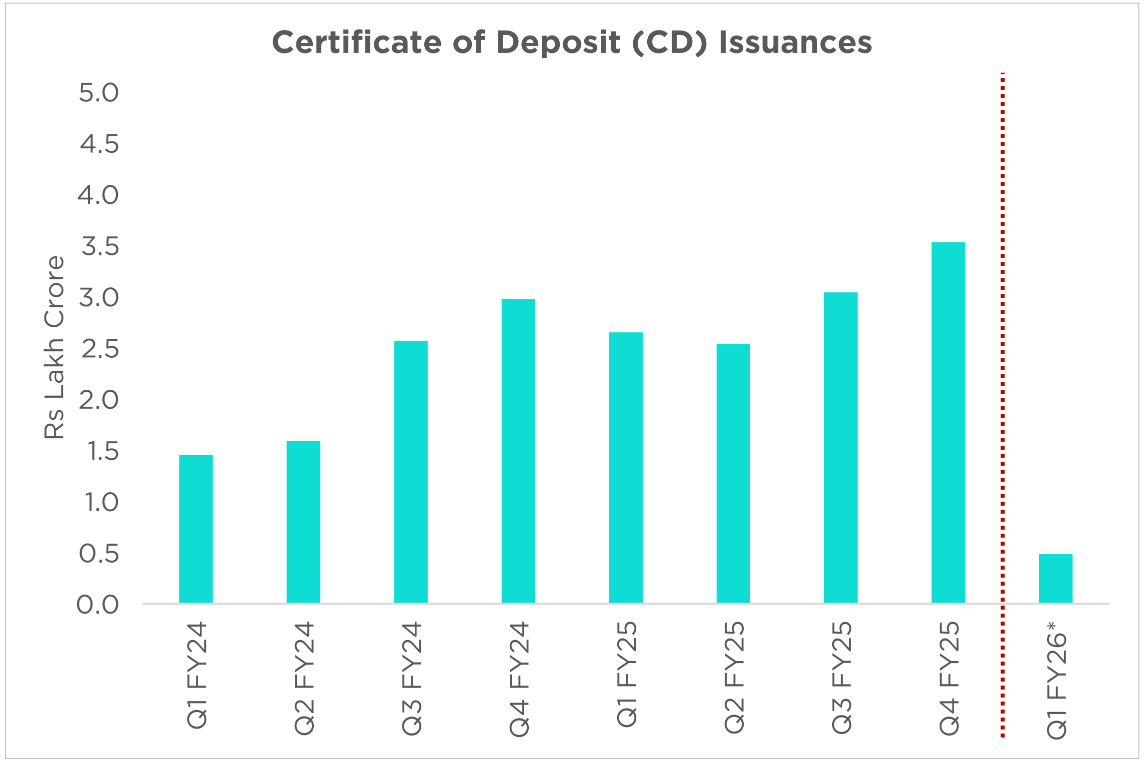
Source: CMIE. Data as of 02 May



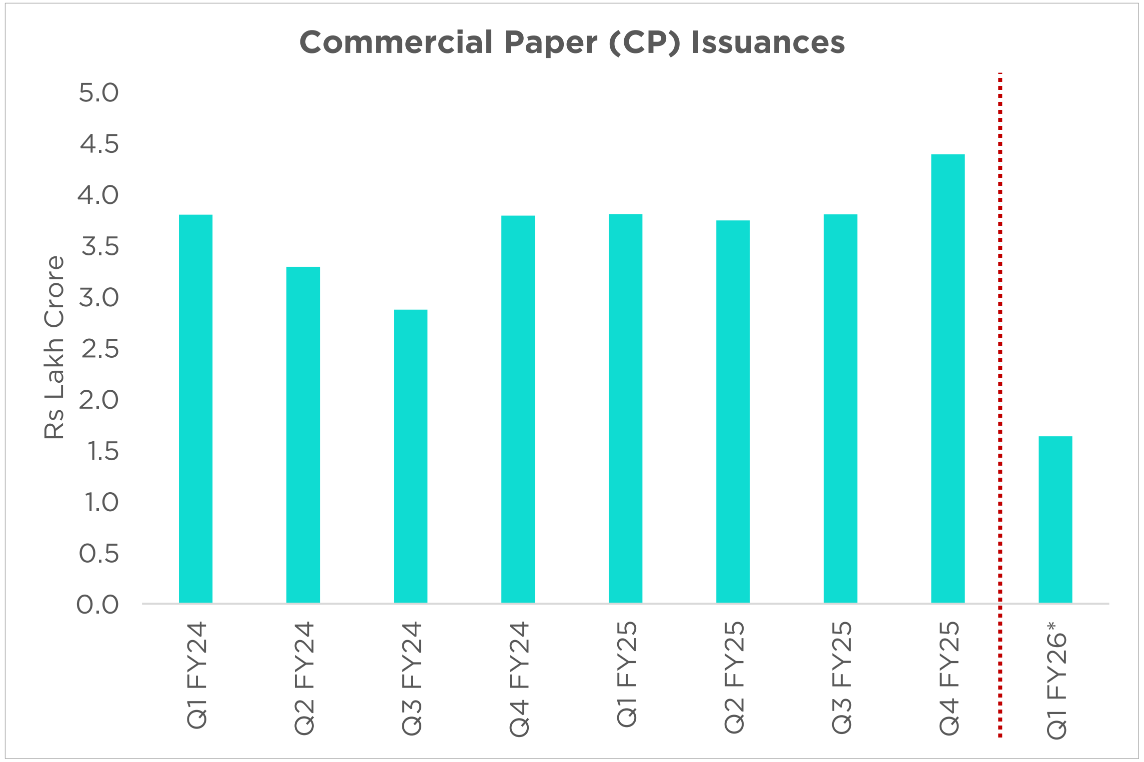
Source: CMIE. Data as of 02 May

- Credit growth slowed to 10.9% YoY as of 02 May from 15.9% a year ago amidst unfavorable base effect.
- Deposit growth eased to 10.3% YoY, compared to 13.3% in the same period last year.
- SCBs' incremental credit-deposit ratio declined for fourth straight week to 82.3% as of 02 May.
- In FY26, SCB credit offtake is likely to be supported by RBI rate cuts, the rollback of risk weights on bank lending to NBFCs, and the deferral of the LCR framework.

Higher Money Market Issuances



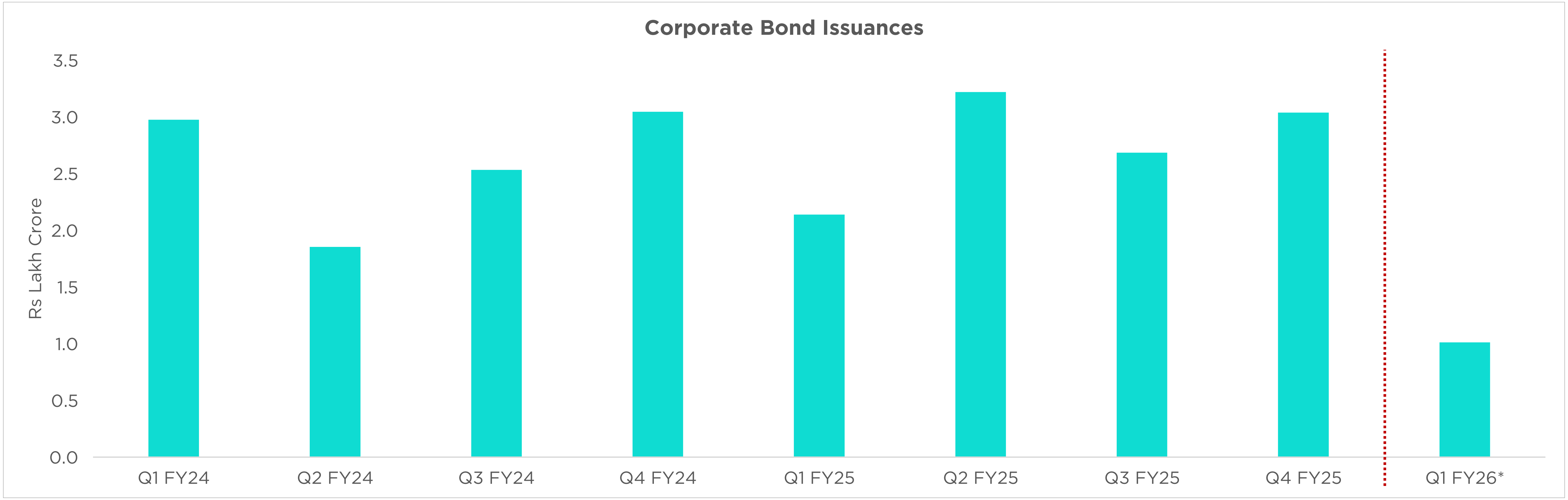
Source: CMIE. *Data as of 02 May



Source: CMIE. *Data as of 30 April

- CD issuances stood at Rs 0.39 lakh crore in April 2025, up 24% YoY. Banks continued to rely on CDs amidst subdued deposit growth.
- CP issuances rose to Rs 1.6 lakh crore in April 2025, up 94% YoY.

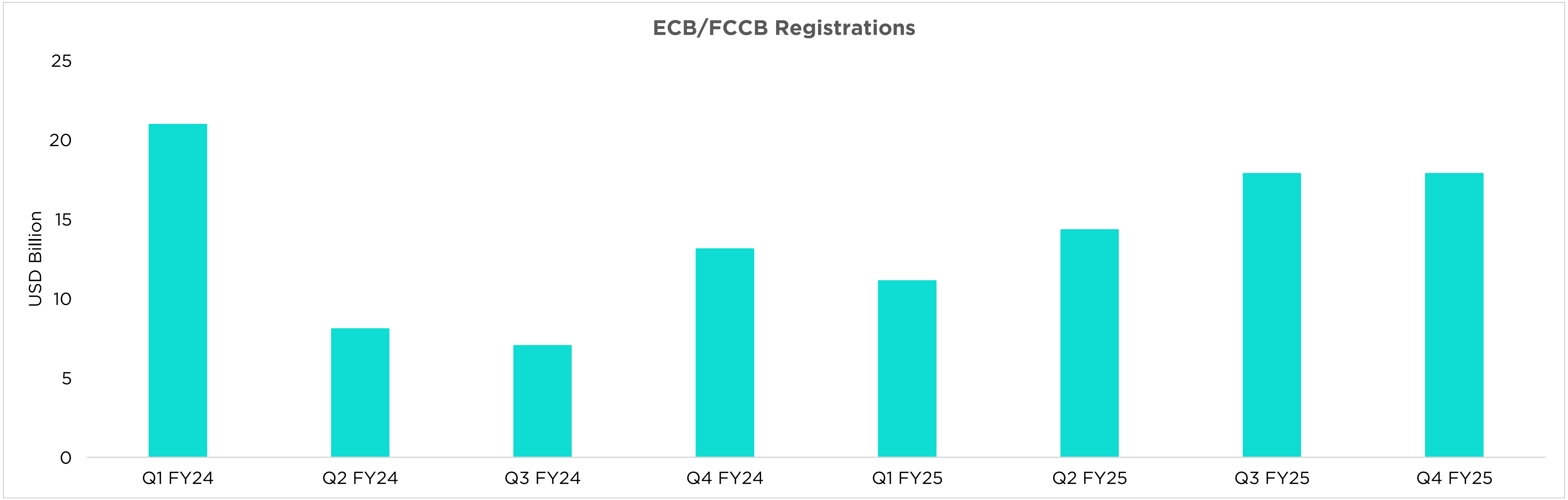
April Sees Sharp Uptick in Corporate Bond Issuances



Source: Prime Database. Data includes private placements and public issues. *Data as of April 2025

- Corporate bond issuances in April 2025 amounted to around Rs 1 lakh crore, up 76% YoY.
- Issuances in FY26 are likely to be supported by lower interest rates.

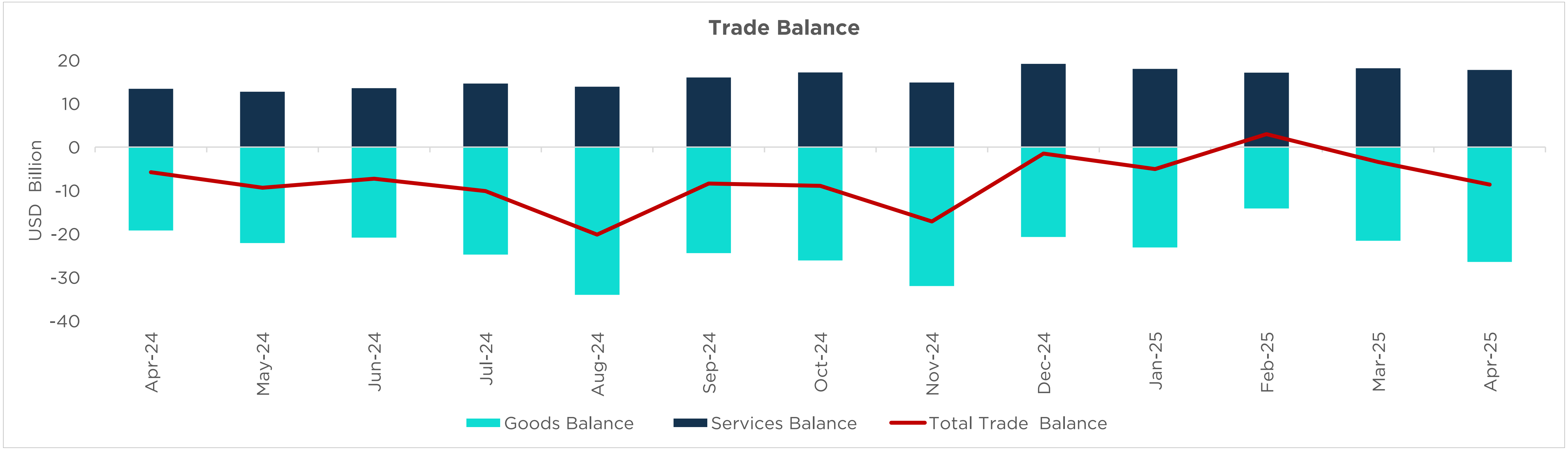
ECB Registrations Surge in FY25



Source: CMIE, RBI

- ECB/FCCB registrations reached around USD 11 billion in March 2025, the highest in over five years.
- FY25 registrations rose to USD 61 billion, up 24% YoY.
- Higher registrations should support USD/INR exchange rate.

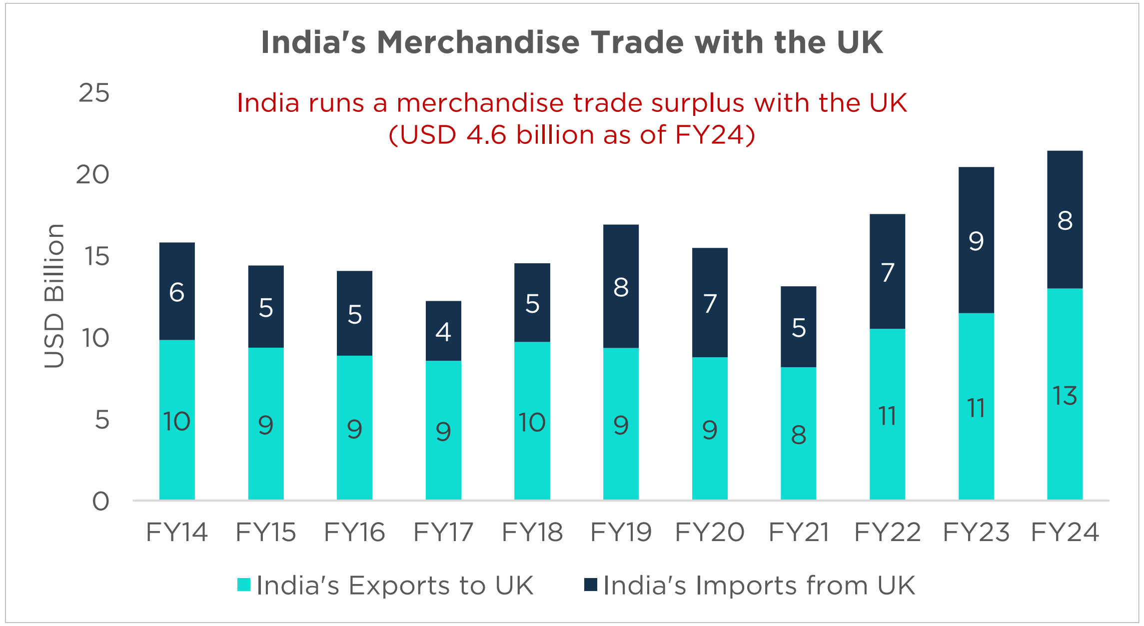
Goods Deficit Widens to 5-Month High; Services Surplus Holds Strong



Source: CMIE

- India's goods trade deficit widened to USD 26.4 billion in April.
- Goods exports rose 9% YoY to USD 38.5 billion, while imports surged 19% YoY to USD 64.9 billion, driven by a 26% rise in crude oil and petroleum imports.
- Net services exports remained strong at USD 17.8 billion in April, up 32% YoY.
- We expect India's CAD to stay manageable at 1.1% of GDP in FY26, supported by lower oil prices and resilient services exports — a positive for the rupee.

India & UK Reach a Historic Free Trade Agreement



Source: CMIE

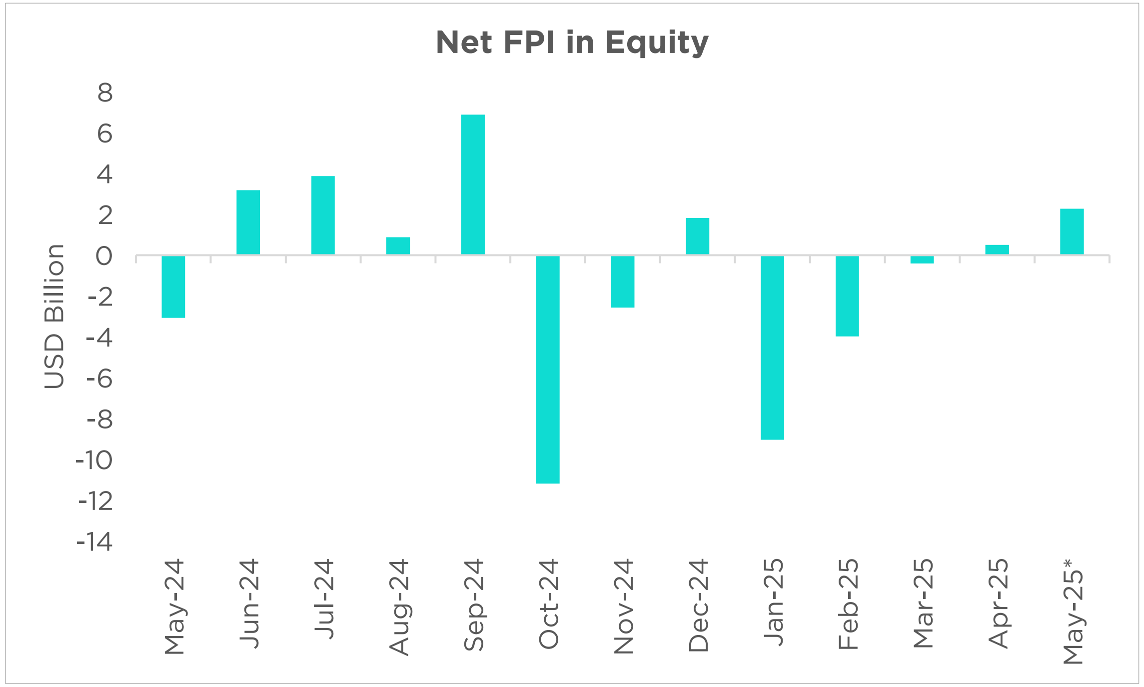
India's Top 5 Merchandise Exports to the UK (FY24)	Share
Electrical machinery & equipment	14%
Nuclear reactors, boilers, parts	12%
Mineral fuels and oils	10%
Apparels & clothing accessories	10%
Pharma products	5%

India's Top 5 Merchandise Imports from the UK (FY24)	Share
Pearls, precious stones & metals	28%
Nuclear reactors, boilers, parts	13%
Iron & steel	9%
Electrical machinery & equipment	6%
Essential oils & cosmetics	5%

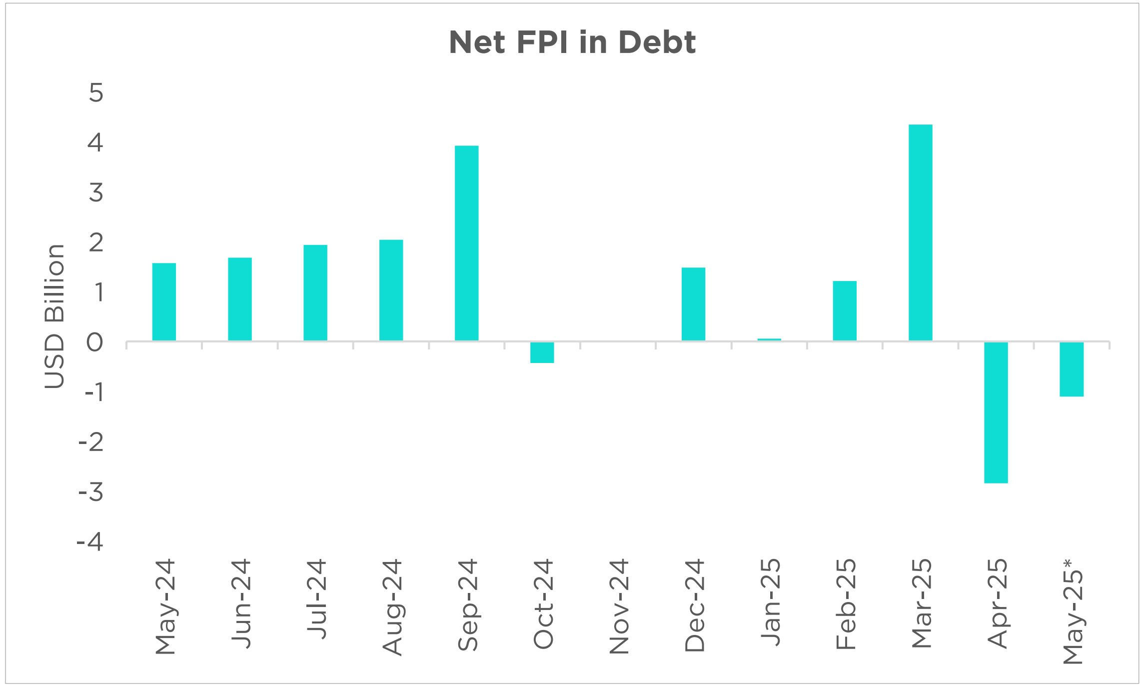
Source: Ministry of Commerce. Note: Export/Import categories are as per HS2 Code

- Under the FTA, 99% of Indian exports to the UK will enjoy zero duty, benefitting sectors like RMG, marine products, leather, toys, gems and jewellery, as well as engineering goods, auto parts and engines, and organic chemicals.
- India to reduce duties on whisky (from 150% to 40% over 10 years) and cars (from 100% to 10% under quota).
- Deal to boost services trade and talent mobility, supporting IT, financial, professional and educational services.
- As per the Government, India-UK bilateral trade of USD 60 billion is projected to double by 2030 with the help of FTA.
- Similarly, India's trade negotiations with other countries/regions like the US, EU, and New Zealand are a positive for its external sector outlook.

FPI Inflows Rebound in May



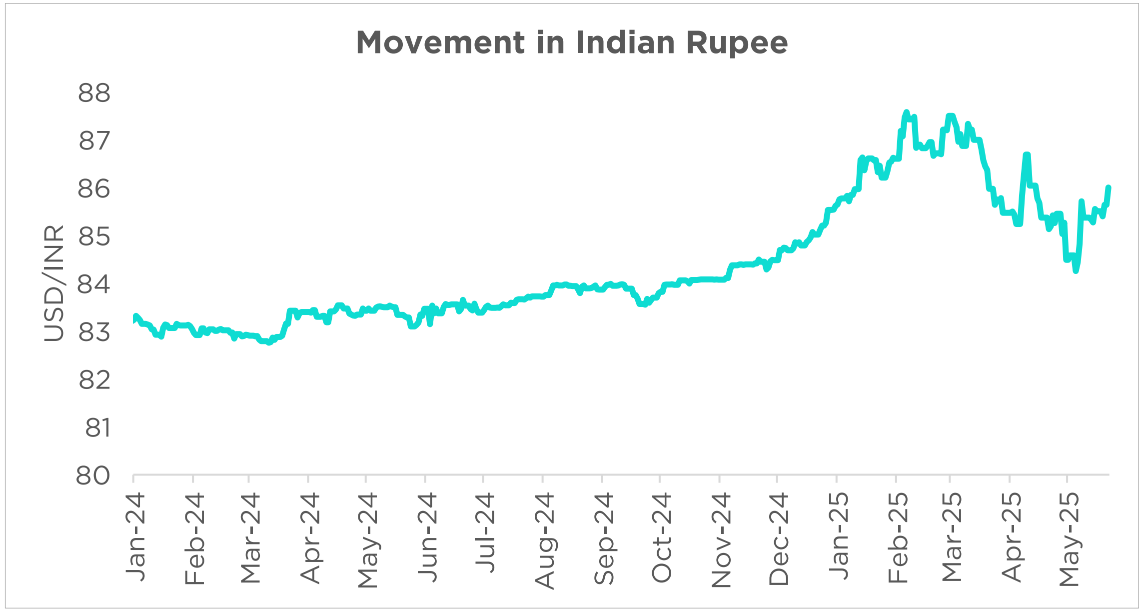
Source: NSDL. *Data as of 22 May



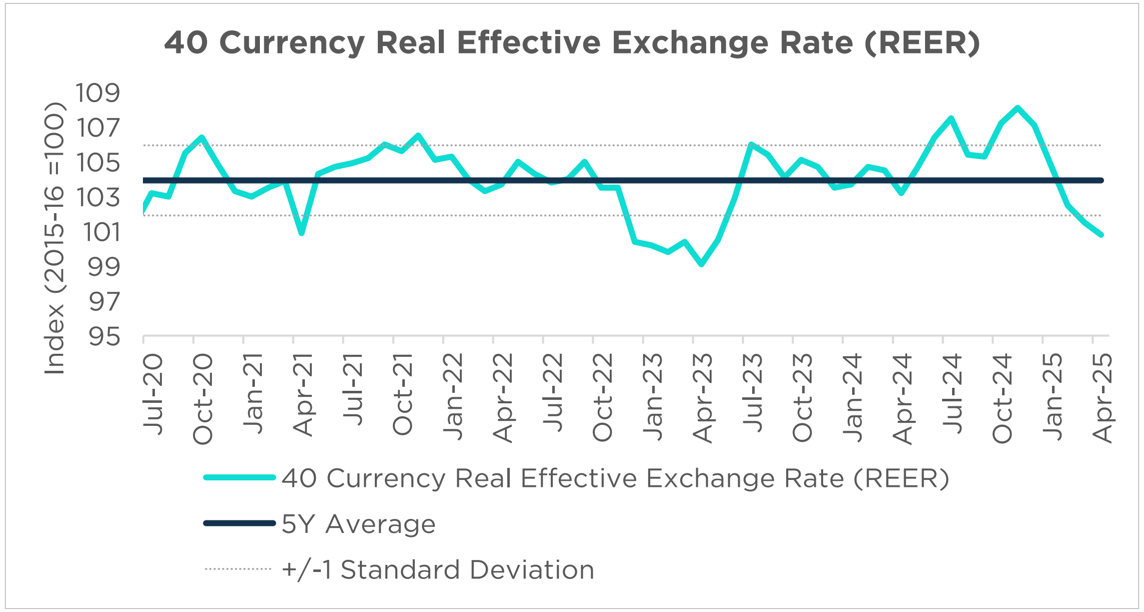
Source: NSDL. *Data as of 22 May

- Net FPI inflows (debt + equity) of USD 1.1 billion were recorded in May (up to 22 May), reversing USD 2.3 billion of outflows in April.
- Inflows were led by equities, while the debt segment saw outflows for a second consecutive month.
- Rotation away from US assets and RBI policy easing are supporting flows.
- FPI flows are expected to remain volatile with some rotation toward China likely amidst the US-China trade truce. US-India trade deal developments will be key to watch, with potential implications for market sentiment.

Rupee Supported by Easing Pressures



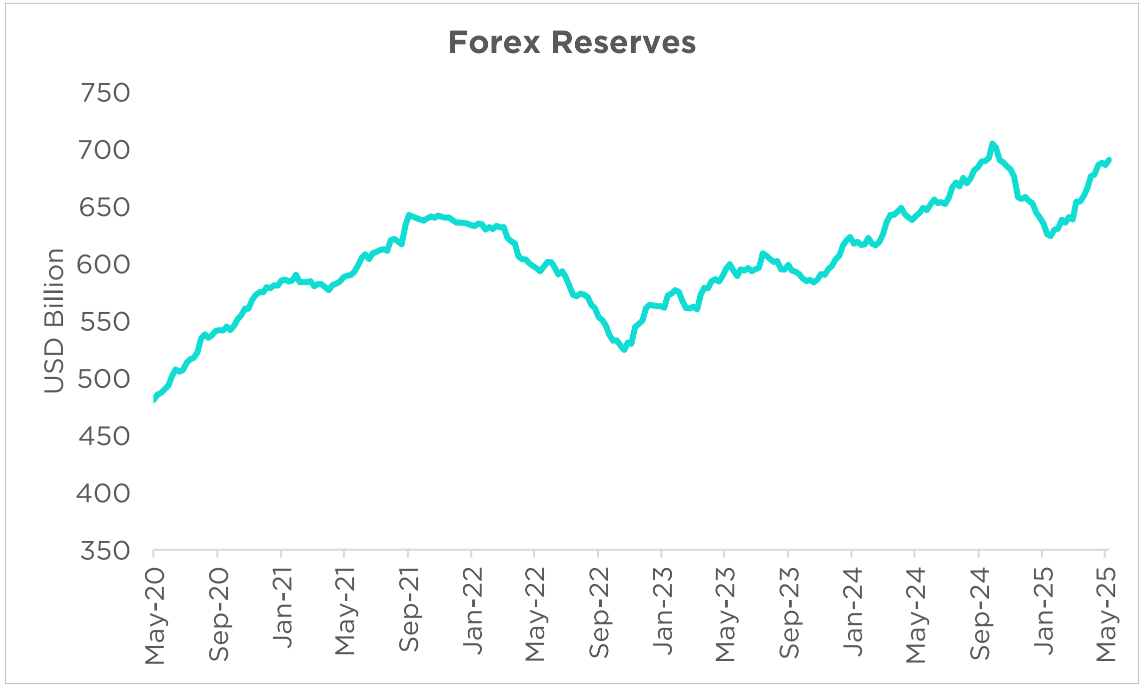
Source: Refinitiv. Data as of 22 May



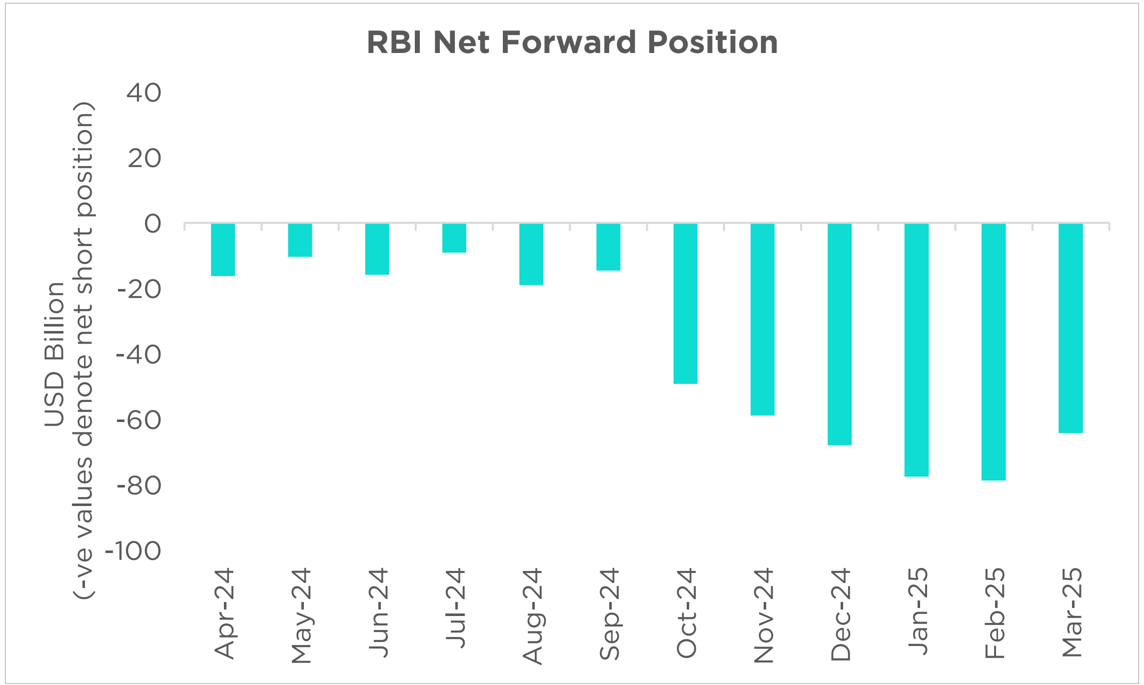
Source: CMIE

- The rupee has strengthened by around 2% against the dollar from its February lows; REER suggests valuation concerns have eased considerably.
- India's robust fundamentals - fastest growing major economy with low CPI and manageable CAD – support the rupee outlook.
- The dollar index is likely to stay weak - US recession fears have eased, but growth may slow as tariffs remain above pre-Trump levels; rising fiscal concerns and fading safe haven demand may also weigh on the dollar.
- Yuan appreciation may be limited, with the PBoC focused on currency stability and to support exports amid weak domestic demand.
- Likely rotation of FPI flows to China may weigh on the rupee in the short term, but overall pressures on the currency have eased.

Forex Reserves Healthy



Source: CEIC. Data as of 09 May



Source: CEIC

- Forex reserves rose by USD 50 billion CYTD, reaching USD 691 billion as of 09 May – providing a comfortable import cover of about 11 months.
- However, reserves remain below the September 2024 peak of USD 705 billion.
- RBI is likely to build its FX reserves, given it has a large net short forward book (USD 64 billion as of March 2025). This could limit rupee appreciation.
- However, RBI interventions may be more measured than in the past, suggesting some rupee volatility could persist.
- We expect USD/INR to trade around 87-88 by end FY26.

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