Bond Market in India – Rising Bond Yields Amid RBI Rate Cuts

September 2, 2025 • vajiramandravi.com

Bond Market in India Latest News

- India's 10-year benchmark **government bond yield has risen by about 26 basis points** in the past month, despite the Reserve Bank of India (RBI) cutting the repo rate by 100 basis points over seven months.
- This divergence signals **investor unease in the bond market in India** over inflation, fiscal risks, and government borrowing requirements.

Bond Market in India

- **Meaning**:
  - The bond market in India is a structured space where governments, companies, and public sector organisations **raise money by issuing bonds**.
  - The bond market is **not just a place for investors to park their money**—it plays a vital role in keeping the Indian economy running smoothly.

- **Importance:**
  - **Funding the nation's development:** Example, when the government needs money to build roads, schools, hospitals, or even invest in green energy projects, it issues bonds.
  - **Fueling business growth:** Corporate bonds allow businesses to raise money for expansion, new projects, or even to manage existing debt more efficiently.
  - **Shaping interest rates:** The bond market plays a key role in guiding interest rates. **Bond yields**—the returns investors expect—act as a benchmark for interest rates across the economy.
- **Types of bond markets in India:**
  - **Primary bond market:**
    - When a company or government needs funds, it **issues bonds for the first time** in this market.
    - Investors **purchase these fresh bonds directly from the issuer**, providing immediate capital for the issuer's projects.
  - **Secondary bond market:**
    - It allows investors to buy and sell previously issued bonds among themselves.
    - **Prices** in the secondary market **fluctuate** based on interest rates, issuer creditworthiness, and broader economic trends, offering both opportunities and risks for investors.
- **Key types of bonds one can invest in:**
  - **Government bond market**: The government issues various types of bonds, such as –
    - **Treasury Bills**: Short-term securities with maturities up to one year, ideal for those seeking safety and quick returns.
    - **G-Secs (Government Securities):** Long-term bonds with maturities from 2 to 30 years, often used to fund major infrastructure projects.
    - **State Development Loans (SDLs):** Bonds issued by state governments for regional development.
  - **Municipal bond market:** State and local authorities issue municipal bonds to finance public infrastructure like water supply systems or urban transport.
  - **Corporate bond market:** While these bonds carry higher risk compared to government bonds, they also offer higher coupon rates, providing an opportunity for greater returns.
- **Regulation**: Government bonds are regulated by Reserve Bank of India (**RBI**) and Corporate bonds are regulated by Securities and Exchange Board of India (**SEBI**).

Key Developments in Bond Market in India

- **Bond market dynamics:**
  - **10-year bond yield**: Rose from around 6.34% to 6.60% despite rate cuts.
  - **General expectation**: Bond yields fall when repo rate is cut; current rise shows investor concerns.
  - **Implication**: Rising yields leads to falling bond prices, reflecting selling pressure.
- **RBI's policy stance:**
  - RBI adopted a **hawkish** stance on inflation despite lowering rates.

- Monetary Policy Committee (MPC) kept key rates unchanged:
    - **Repo Rate:** 5.50%
    - **Standing Deposit Facility (SDF):** 5.25%
    - **Marginal Standing Facility (MSF):** 5.75%
- **Growth forecast**: 6.5% for 2025–26.
- **Inflation forecast**: Revised down to 3.1% for 2025–26, but projected to rise to 4.9% in Q1 of 2026–27.

Yield Curve and Market Interpretation

- **Steepening yield curve**: Long-term yields rose more sharply than short-term yields.
- **Investor expectation**: Higher future borrowing costs.
- **Mutual fund outlook:** RBI prioritising inflation control over growth revival.

GST Reform and Fiscal Concerns

- **Proposal**: Rationalisation of GST from 4 slabs (5%, 12%, 18%, 28%) to **2 slabs** (5%, 18%), plus 40% for sin goods.
- **Market concern:**
    - Possible revenue loss of ₹50,000–60,000 crore.
    - Risk of fiscal slippage and higher borrowing needs.
- **Effect**: Increased government borrowing would result in higher bond supply and rising yields.

Possible Corrective Measures

- **Government borrowing strategy**: Shift to short/medium-term borrowing.
- **RBI interventions:**
    - **Open Market Operations (OMOs)**: RBI buys long-term bonds to reduce supply and yields.
    - **Operation Twist**: Simultaneous buying of long-term bonds and selling of short-term ones.

Forward Outlook

- **No immediate rate cuts** likely due to inflation trajectory.
- If inflation eases further, RBI may adopt a **growth-supportive stance**.
- This could **revive long-duration bonds and ease yields** in the medium term.

Conclusion

- Going forward, the bond market in India will hinge on how effectively the RBI balances inflation management with the government’s fiscal consolidation efforts.

- **Prudent borrowing strategies** and timely policy interventions like OMOs or Operation Twist can stabilize yields and create space for growth-supportive measures once inflation risks ease.

Source: IE
