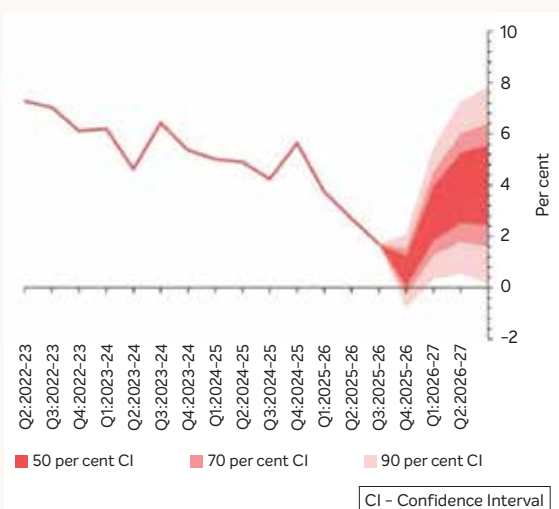


RBI Eases Rates – Aims to Strengthen Liquidity and Support Growth

The Monetary Policy Committee (MPC), in its December 2025 meeting, reduced the repo rate by 25 bps, taking the total rate cuts for the calendar year to 125 bps. Repo rate thus stands at 5.25% (unanimously voted).

Consequently, the standing deposit facility (SDF) rate under the liquidity adjustment facility (LAF) is adjusted to 5.00% and the marginal standing facility (MSF) rate and the Bank Rate at 5.50 %. The Cash Reserve Ratio (CRR) stands at 3%. Policy stance remains unchanged at “neutral”, reflecting a balanced approach in response to the evolving domestic growth-inflation dynamics and ongoing geopolitical uncertainties. The MPC noted that given the growth-inflation balance, especially the benign inflation outlook on both headline and core, continues to provide the policy space to support the growth momentum. Bond market yields touched intra-day lows of 6.46% as RBI announced OMO purchases this month, but some of it got reversed as the Governor clarified that OMOs were to be viewed as liquidity supporting measure and not meant for yield control.

Assessment & Outlook on Inflation:

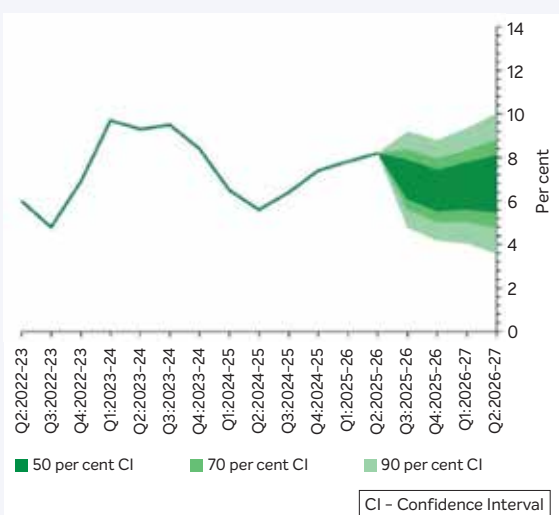


Headline CPI inflation declined to an all-time low in Oct-25. The faster than anticipated decline in inflation was led by correction in food prices, contrary to the usual trend witnessed during the months of Sept & Oct. Core inflation (CPI excl. food & fuel) remained largely contained in Sept-Oct, despite continued price pressures exerted by precious metals. Excluding gold, core inflation moderated to 2.6%.

Food Inflation outlook remains bright given higher kharif production & adequate reservoir levels. Barring some metals, international commodity prices are likely to moderate going forward. Overall, inflation is likely to be softer than what was projected in Oct, mainly on account of the fall in food prices.

Basis these factors, RBI expects CPI inflation for FY26 to now come in at 2.0% (revised down from 2.6%) with Q3 at 0.6% (down from 1.8%) and Q4 at 2.9% (down from 4.0%). CPI for Q1FY27 is estimated at 3.9% (down from 4.5%) and for Q2FY27 at 4.0%.

Assessment & Outlook on Growth:



Real GDP registered a six-quarter high growth at 8.2% in Q2FY26, underpinned by resilient domestic demand amidst global trade and policy uncertainties. Economic activity in H1FY26 was supported by income tax and GST rationalisation, softer crude prices, front-loaded government capex, and accommodative monetary and financial conditions amid low inflation.

High-frequency data indicates resilience in Q3 activity, though a few leading indicators show early signs of softening. Going forward, supportive domestic factors—better agri outlook, GST rationalisation, low inflation, and strong corporate and financial balance sheets—should help sustain growth.

On the external front, services exports are likely to remain strong, while merchandise exports face some headwinds. External uncertainties continue to pose downside risks to the outlook, while speedy conclusion of ongoing trade and investment negotiations present upside potential. Given this backdrop, real GDP growth has been revised to 7.3% (up from 6.8%) for FY26 with Q3 at 7.0% (up from 6.4%) and Q4 at 6.5% (up from 6.2%). GDP for Q1FY27 is projected at 6.7% (up from 6.4%) and Q2FY27 at 6.8%.

System liquidity, as measured by the net position under the liquidity adjustment facility (LAF) has been in surplus at an average of ₹1.5 lk cr since the last MPC in Oct'25. Money market rates have broadly tracked the policy repo rate. Following the cumulative 100 bps repo cut in the current easing cycle (till December 3), the WACR, 3-month T-bill, 3-month NBFC CP, and 3-month CD rates have fallen by 110 bps, 113 bps, 124 bps, and 140 bps, respectively. G-Sec yields have largely remained range-bound. The MPC reiterated its commitment to provide sufficient durable liquidity to the banking system. Post reviewing the current liquidity situation they have decided to conduct open market operation (OMO) purchases of government securities amounting to ₹1 lk cr and 3-year USD/INR Buy Sell swaps of \$5bn this month. These measures will ensure adequate durable liquidity in the system and further facilitate monetary transmission.

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Current Account Deficit (CAD) moderated to 1.3% of GDP in Q2FY26 from 2.2% of GDP in Q2FY25, on account of robust services exports and strong remittances. In Oct-25, merchandise exports contracted y-o-y, whereas merchandise imports continued to increase for the second consecutive month, resulting in a widening of the trade deficit. Healthy services exports coupled with strong remittance receipts are expected to keep CAD modest during 2025-26. On the external financing front, gross FDI posted strong growth in H1FY26, while net FDI rose sharply as repatriations declined despite higher outward FDI. FPI flows to India saw net outflows of \$0.7 bn in FY26 so far, driven by outflows in the equity segment. As of Nov-25, forex reserves stood at \$686.2bn, providing over 11 months of import cover.

System-level financial parameters related to capital adequacy, liquidity, asset quality and profitability of Scheduled Commercial Banks (SCBs) and NBFCs continue to remain robust. The outstanding credit and deposit for SCBs increased by 11.31% and 9.74% on a y-o-y basis Oct-24 and Oct-25. GNPA for SCBs (2.05% in Sept-25 v/s 2.54% in Sept-24) and NNPA (0.48% in Sept-25 v/s 0.57% in Sept-24) shows further improvement, while for NBFCs, GNPA ratio has improved from 2.57% Sept-24 to 2.21% in Sept-25, while NNPA ratio also improved from 1.04% in Sept-24 to 0.99% in Sept-25. Bank credit growth too has seen an uptick in recent months, registering a growth of 11.4% as on 14th Nov, compared to 11.2% a year ago. Growth was driven by steady lending to retail and services, while industrial credit strengthened on the back of robust MSME financing. Large industries, too, saw an improvement in credit demand.

The commitment shown by RBI to large-scale OMO purchases is particularly significant. It seems to be aimed at providing banks with greater and steadier liquidity assurance, supports smoother and accelerated rate transmission and also aims at lowering fund costs across banks and NBFCs. Rate cut, along with liquidity injection, should meaningfully improve access to cheaper credit and help revive momentum in segments where lending growth had slowed down.

The rate transmission of the recent policy actions is underway with weighted loan rates having come off by ~60bps. Reduction in cost of funds (better NIMs) could mean lowering of borrowing rates thus reducing EMIs and leaving more surpluses in the hands of consumers that could in part aid discretionary spends, now coupled with GST 2.0. Substantial downward revision to inflation forecasts suggests that RBI may have left itself with an option for one more rate cut in the Feb-26 policy. However, a robust Q3FY26 GDP expectation might act as a counterbalance to this view and limit the need/scope for more rate action. Additionally, external volatility will continue to reshape market expectations, and we prefer a dynamic and continuously reassessed approach to duration. The compelling opportunity that duration strategies have offered over the past 18m – 20m seems to have significantly played out. Incrementally, positioning majority of the fixed income portfolio into duration-driven funds may have marginal value addition in our view.

Deployment Strategy:

The curve has steepened and is expected to remain elevated given the government holding on to its H2FY26 borrowings calendar with ~70% and higher supply coming in bonds with 10yr and longer-term maturities. Tepid demand from traditional bond buyers in the duration space by Insurance and Pension funds, could lead to long-term yields being in range. Limited supply, and RBI's active liquidity management could mean the short to medium term yields could come off further (bull steepening). We thus remain overweight on strategies focusing on 2yr – 5yr segment of the yield curve. Investors should continue to allocate upto 45% of fixed income portfolio towards accrual-oriented strategies. Consequently, they should maintain allocation to dynamic / long duration strategies upto 20% of fixed income portfolio. Credit environment continues to remain stable, and credit spreads remain attractive. Thus, balance 35% allocation of fixed income portfolio is suggested towards high yielding assets (via bonds /funds).

Tenor	Rate Cut Cycle		Rate Hike Cycle				Rate unchanged				Rate Cut Cycle			Rate Unchanged		Rate Cut	Spread
	Feb 2020 (A)	May 2022 (B)	June 2022 (C)	Aug 2022 (D)	Sep-22 (E)	Dec-22 (F)	Feb-23 (G)	Oct-23 (H)	Feb-24 (I)	Oct-24 (J)	Feb-25 (K)	Apr-25 (L)	Jun-25 (M)	Aug-25 (N)	Oct-25 (O)	Dec-25 (P)	(P-G) (bps)
Repo	5.15%	4.40%	4.90%	5.40%	5.90%	6.25%	6.50%	6.50%	6.50%	6.50%	6.25%	6.00%	5.50%	5.50%	5.50%	5.25%	-125
3Y G-Sec	6.10%	6.31%	6.93%	6.67%	7.10%	7.11%	7.39%	7.34%	7.00%	6.75%	6.69%	6.23%	6.23%	5.97%	5.88%	5.75%	-164
10Y G-Sec	6.51%	7.38%	7.50%	7.30%	7.40%	7.27%	7.34%	7.35%	7.08%	6.87%	6.62%	6.45%	6.23%	6.39%	6.54%	6.48%	-86

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