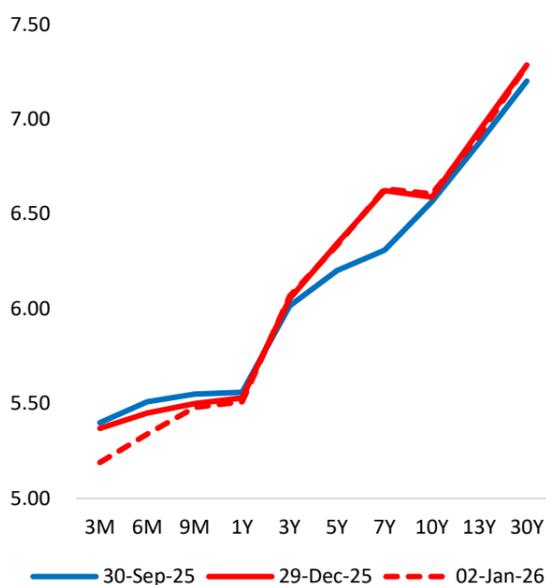


Fig.1: Yield curve movement during the week; (%)



Source: Bloomberg, UBI Research

The 10-year G-Sec began 2026 on a cautious footing, trading in a narrow 6.58-6.62% range and closing near 6.60%, as traders remained defensive ahead of fresh central government auctions and the release of the Jan-Mar state borrowing calendar. Supply concerns dominated sentiment, keeping yields elevated despite stable policy rate expectations. At the weekly gilt auction, PSU bank demand was muted, though mutual funds and short-covering ensured the Rs.320 billion supply cleared smoothly. Pricing undershot expectations, reflecting restrained risk appetite.

Market sentiment turned more cautious after states announced an indicative Rs.5 trillion SDL borrowing for Jan-Mar, exceeding expectations of ~Rs.4.5 trillion and triggering selling in gilts. Investors, particularly banks, are expected to pivot toward higher-yielding SDLs, limiting appetite for benchmark G-Secs. RBI's decision to buy bonds from banks' HTM portfolios in upcoming OMOs is also seen supporting spread assets over on-the-run benchmarks.

Despite the negative supply shock, losses were capped as state-owned banks stepped in near the key 6.65% yield level. The 6.48% 2035 gilt is expected to stabilise around this level, with markets confident of RBI intervention if yields approach 6.70%, the highest seen so far in FY26. Traders refrained from aggressive short positions, encouraged by data showing Rs.41.55 billion of RBI secondary market purchases on Dec. 23, when yields touched similar highs.

Looking ahead, the Jan-Mar 2026 supply pipeline remains the key driver, with T-Bills totalling Rs.3.84 lakh crore and SDL issuance at record levels. While this keeps near-term risks skewed towards modest yield hardening, RBI's active liquidity management and bond purchase operations are expected to prevent disorderly moves, keeping the market in a tactical, range-bound trading environment.

G-Sec Benchmark start 2026 on guard:

- The 10-year G-Sec benchmark opened the new year on a cautious note, trading in a narrow band around 6.58-6.62% and closing near 6.60%, reflecting restrained participation during the holiday-shortened week.
- Market positioning remained defensive, with traders reluctant to add duration ahead of fresh central government auctions and the release of a heavy state borrowing calendar.
- Supply expectations, rather than macro data, remained the dominant driver, keeping yields elevated despite stable policy rate expectations.
- At the weekly gilt auction, PSU bank demand was muted, with bids placed well below secondary market levels. Nevertheless, the Rs.320 bn supply cleared smoothly, aided by short-covering and mutual fund demand; PSU banks likely absorbed Rs.80-90 bn of the 6.48% 2035 gilt, while mutual funds bid for ~₹60 bn.
- Pricing reflected caution, as the cut-off price of Rs.99.03 and WAP of Rs.99.07 for the 6.48% 2035 bond both undershot market expectations, with only 225 of 395 bids accepted, highlighting restrained risk appetite.
- Yields are at multi-month highs as markets scale back expectations of further RBI rate cuts. Carry trades in short-dated bonds are gaining traction, while foreign outflows surged in December amid a weaker rupee. RBI interventions, though large, have only partially offset upward pressure as heavy central and state supply continues to dominate.
- Traders remain cautious ahead of the Jan-Mar SDL calendar, with some optimism that issuance may be below extreme consensus estimates. Speculation about India's inclusion in Bloomberg's Global Aggregate Index also provides a potential backstop, supporting prices even if supply surprises on the higher side.

Supply surge with T-Bills and SDLs take centre stage:

- The Jan-Mar 2026 T-Bill calendar totals ₹3.84 lakh crore, spread across weekly auctions of 91-day, 182-day, and 364-day bills. This provides a predictable short-term supply flow for market absorption.
- State Development Loans (SDLs) are set to reach a record ~₹5 trillion, far exceeding historical quarterly levels, particularly from large-borrowing states like Karnataka, Andhra Pradesh, Tamil Nadu, and Madhya Pradesh.
- The combined central and state issuance is expected to steepen the yield curve further, especially in the 5-15 year segment, and keep SDL-G-Sec spreads elevated.

Rate transmission check; WALR and deposit trend:

- The shift into the new reporting fortnight and year-end adjustments kept money markets tight yet stable, with overnight call rates trading at elevated levels. RBI's previous liquidity infusions via OMOs and FX swaps in 2025 helped contain sharp volatility during this transitional week.
- The weighted average lending rate (WALR) on fresh rupee loans rose to 8.71%, highlighting incomplete transmission of cumulative repo rate cuts during 2025. However, the RBI Governor clarified in the latest policy that this increase largely reflects a change in the composition of bank lending, with a higher share of unsecured retail and gold loans, which carry higher interest rates. The Governor reiterated that effective transmission stands at around 79 bps, and the rise in WALR does not indicate a reversal or stalling of monetary transmission.
- In contrast, weighted average term deposit rates (WATDR) on fresh deposits eased marginally to around 5.59%, reflecting selective repricing by banks. Elevated sovereign yields and competitive deposit mobilisation continue to slow lending rate pass-through, anchoring bond yields at higher levels.

SDL shock triggers G-Sec sell off, RBI seen as key backstop:

- Government bond prices fell after states announced an indicative ₹5 trillion borrowing for Jan-Mar, exceeding market expectations of ~₹4.5 trillion. The heavier supply reinforced concerns that demand for benchmark G-Secs could weaken as banks and other investors shift toward higher-yielding SDLs.
- Despite the negative trigger, losses were capped as state-owned banks stepped in near the key 6.65% level on the 10-year benchmark. The 6.48% 2035 gilt is expected to stabilise around this level, with strong expectations of RBI intervention if yields approach 6.70%, the highest seen so far in FY26.
- Traders also avoided fresh short positions, reassured by data showing the RBI bought ₹41.55 billion of gilts on Dec. 23, when yields touched 6.70%. Market participants expect further RBI purchases in early January, linked to the impending maturity of the 7.59% 2026 bond, reinforcing the central bank's role as a backstop.

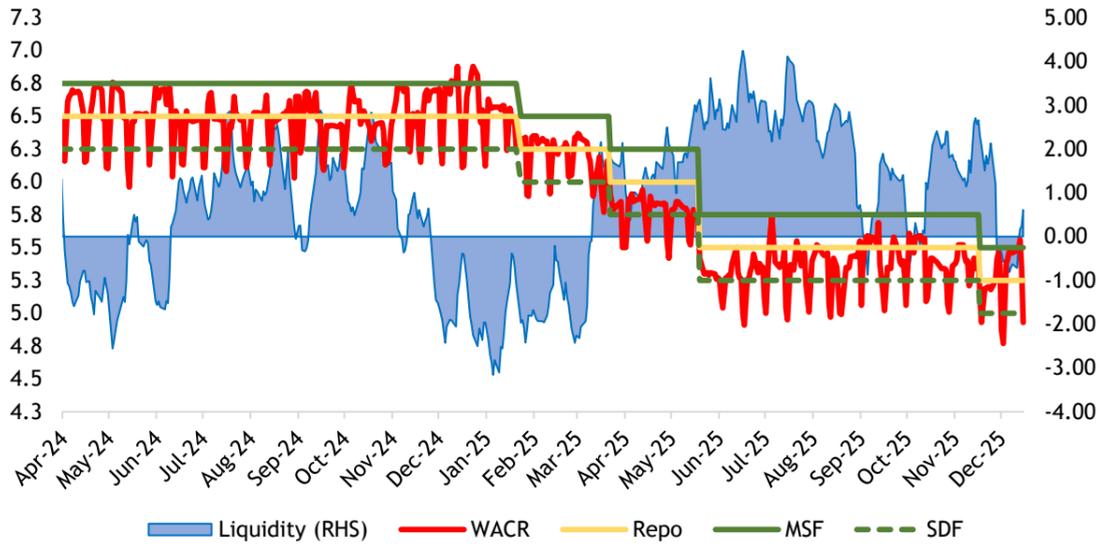
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Table 2: Market Snapshot Instrument	Yield (Jan 02)	Weekly Change	Commentary
10 Year G-Sec (6.33% GS 2035)	6.61%	+2 bps	Markets worried on higher SDL supply
1 Year T-Bill	5.51%	-2 Bps	Liquidity eased due to month end spending
US 10 year Yield	4.19%	+8 bps	Jobless claims data and Geopolitics pushed yields higher
Credit Growth (%) (as of 15 th Dec'25)	12.0%	+44 bps	Credit & Deposit growth increased on fortnight basis and the gap widened
Deposit Growth (%) (as of 15 th Dec'25)	9.4%	-46 bps	
Credit Deposit Wedge (bps) (as of 15 th Dec'25)	263	+65 bps	

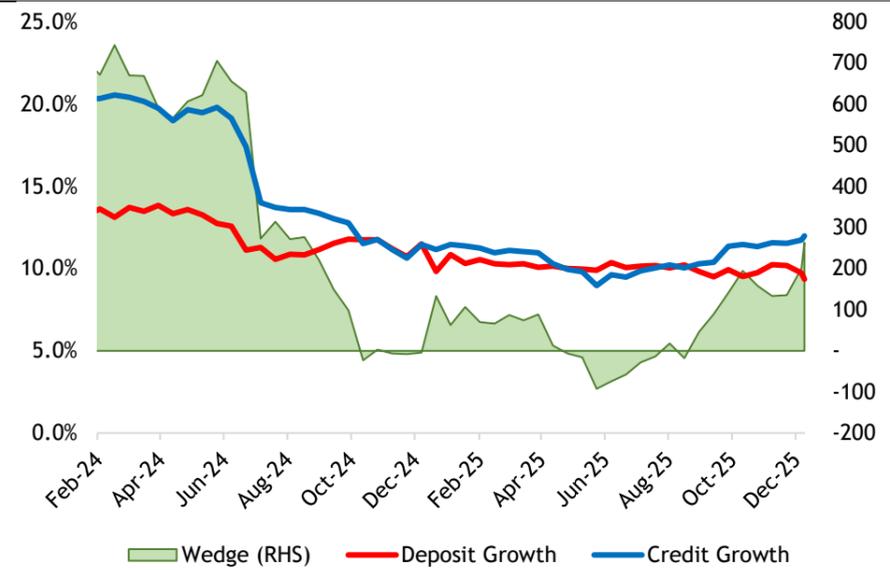
Source: RBI, CCIL, UBI Research

Fig.2: WACR moved up amid tight liquidity conditions; (%)



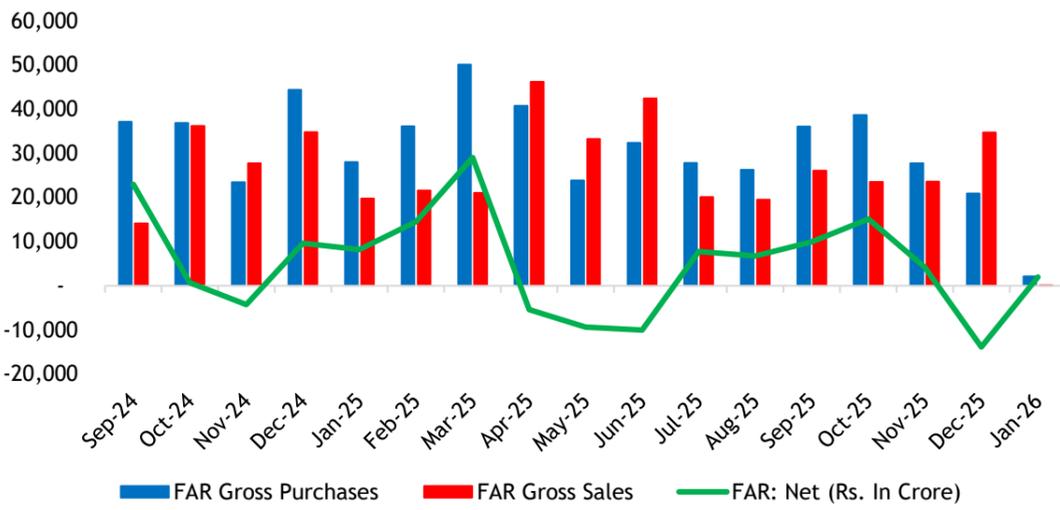
Source: Bloomberg, CEIC, UBI Research

Fig.3: Credit Deposit Gap widened at -263 bps in fortnight ending 15th Dec'25



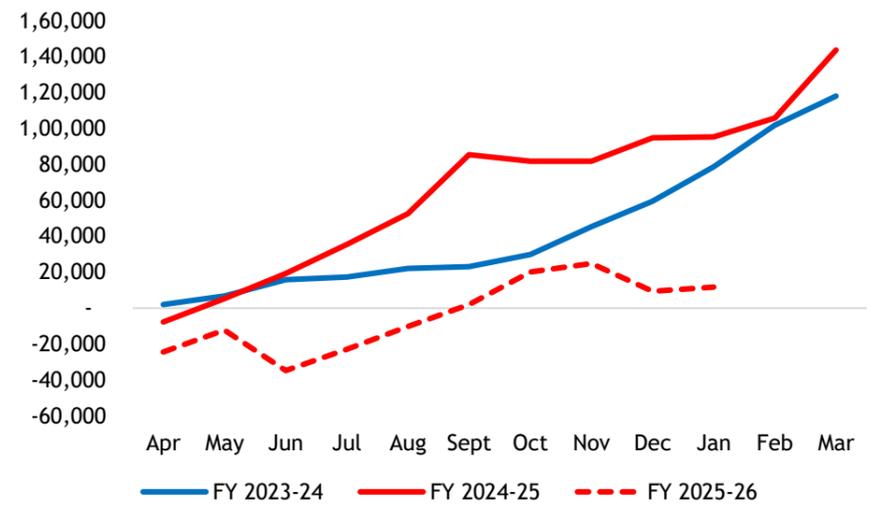
Source: CEIC, UBI Research

Fig.4: Negative Flows in FAR securities in Dec'25 Since Jun'25; (Rs. In Crore)



Source: CEIC, UBI Research

Fig.5: Cumulative FPI flows under Debt Segment; (Rs. In Crore)



Source: NSDL, UBI Research

Table 3: Fixed Income tracking Heatmap

Fixed Income Heatmap	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	May-25	Jun-25	Jul-25	Aug-25	Sep-25	Oct-25	Nov-25	Dec-25
Growth																					
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	57.60	58.40	59.10	59.30	57.70	59.20	56.60	55.00
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	58.80	60.40	60.50	62.90	60.90	58.90	59.80	59.10
GST Collection (YoY Gr%)	12.42	9.96	7.63	10.28	9.99	6.47	8.92	0.65	-0.20	12.29	9.09	9.89	12.58	16.39	6.20	7.50	6.49	9.11	4.59	3.56	6.07
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	9.65	9.95	40.26	37.39	3.35	-9.88	-7.99	-11.07	12.42	
Vehicle registrations (% y/y)	25.22	4.38	2.80	14.51	4.58	-5.29	33.50	10.54	-8.65	6.32	-4.91	1.17	2.61	6.13	5.70	-2.48	3.94	6.72	41.95	1.36	13.57
Exports (% y/y)	14.97	10.95	3.27	-5.25	-14.09	-0.96	16.60	-5.35	-1.53	-2.64	-10.86	0.85	-3.82	-1.23	-1.34	13.34	5.81	6.19	-11.87	19.38	
Imports (% y/y)	11.08	7.35	5.25	11.91	10.44	8.29	3.22	16.65	2.75	10.66	-14.81	12.13	20.00	-1.33	-3.41	9.10	-9.54	18.01	16.89	-1.89	
Inflation																					
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	2.82	2.10	1.61	2.07	1.44	0.25	0.71	
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	4.11	4.24	4.41	4.12	4.11	4.27	4.41	4.34	
Transmission																					
Bank Credit (YoY Gr%)	19.21	20.72	17.40	13.71	14.03	12.34	11.80	11.16	11.16	12.54	12.26	11.03	10.09	8.96	9.48	10.04	10.12	10.79	12.00	11.53	
Bank Deposits (YoY Gr%)	12.56	14.02	11.12	10.57	12.72	10.38	11.50	11.25	9.83	12.06	12.01	10.28	9.79	9.89	10.06	10.17	9.31	9.36	10.84	10.19	
C-D Ratio (%)	79.90	79.90	79.70	79.70	78.80	79.60	79.80	79.90	80.80	80.70	80.80	81.10	80.10	79.30	79.30	79.60	79.30	80.50	80.50	80.80	
WALR O/s Rupee Loans (%)	9.81	9.81	9.89	9.89	9.89	9.88	9.88	9.87	9.86	9.87	9.80	9.77	9.68	9.67	9.44	9.38	9.32	9.26	9.24	9.21	
WALR Fresh Rupee Loans (%)	9.55	9.39	9.32	9.40	9.41	9.37	9.54	9.40	9.25	9.33	9.40	9.35	9.26	9.20	8.62	8.81	8.72	8.39	8.61	8.71	
WADR O/s (%)	6.97	6.99	7.00	7.00	7.01	7.04	7.04	7.06	7.08	7.09	7.10	7.11	7.11	7.07	7.00	6.92	6.87	6.82	6.78	6.73	
WADR Fresh (%)	6.49	6.49	6.49	6.51	6.49	6.57	6.47	6.47	6.60	6.62	6.55	6.72	6.34	6.11	5.75	5.61	5.56	5.61	5.57	5.59	
MCLR 1 Year - Median	8.85	8.79	8.85	8.85	8.90	8.95	8.95	9.00	9.00	9.00	9.05	9.00	9.00	8.95	8.90	8.75	8.60	8.60	8.55	8.50	8.45

Source: CEIC, UBI Research

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