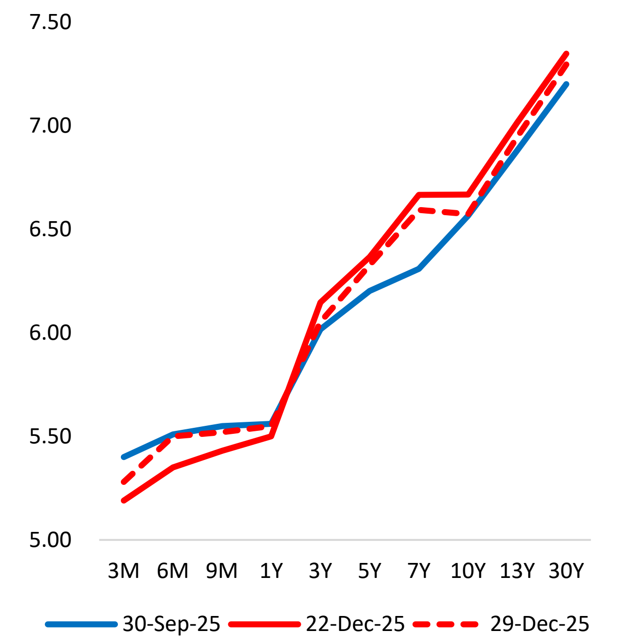
FI Weekly: Liquidity Relief from RBI Supports Bonds Despite Supply Headwinds

30th Dec 2025

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



Source: Bloomberg, UBI Research

The RBI has moved swiftly to ease liquidity stress, but the bond market remains wary rather than reassured. Frontloaded OMOs and a USD 10bn buy/sell swap have provided near-term liquidity comfort and helped yields retreat from recent highs, yet investor appetite remains subdued. Markets are already looking beyond the immediate relief, with heavy and front-loaded SDL supply estimated to exceed Rs.12 lakh crore dampening sentiment and limiting willingness to chase yields lower. While system liquidity is expected to remain manageable over the next few months, supported by RBI actions and seasonal improvement in government spending, concerns around persistent supply, and limited monetary easing keep the outlook cautious. As a result, any further decline in yields is likely to be tactical, with the market staying defensive amid looming supply pressures.

RBI Liquidity actions and market response:

- Liquidity conditions remained tight during the week, with the banking system in deficit of Rs.0.70 lakh crore (average for the week ending 29th Dec'25). Seasonal advance tax outflows, year-end balance sheet pressures and credit growth (11.7%) continuing to outpace deposit growth (9.7%) kept structural liquidity in deficit, as reflected in a persistent credit-deposit gap of ~200 bps.
- Indian Government Bonds (IGBs) recovered modestly after the RBI announced proactive measures to ease tight liquidity conditions, including Rs.2 lakh crore of OMO purchases and a USD 10bn 3-year buy/sell FX swap, together injecting ~Rs.2.9 lakh crore of liquidity. While the quantum of liquidity support broadly met market expectations, the RBI once again surprised by frontloading the easing, rather than staggering the measures.
- In response, bond yields declined by 5-10 bps, though the reaction has been muted. Recent auctions signal weak demand, with most bonds tailing by 2–3 bps, highlighting reluctance to chase yields lower. The announcement provided immediate relief to the fixed income market, with the 10-year G-Sec yield retreating from an intraday high of 6.70% to around 6.62%, after having risen sharply from 6.49% post the 5 Dec policy. While higher rupee liquidity is typically negative for the INR, the size of the OMO and FX swap provides the RBI greater flexibility to intervene in the Fx market without tightening liquidity.

Structural headwinds cap further yield declines:

- Despite RBI's liquidity support, a sharp and sustained rally in yields appears unlikely, as structural supply pressures remain intact. The heavy SDL issuance pipeline continues to overhang the market, with state borrowings expected to exceed Rs.12 lakh crore this year, following Rs.7.5 lakh crore issuance in the first three quarters. Historically, 35–40% of annual SDL supply is loaded in Q4 and based on this trend, the upcoming borrowing calendar could amount to Rs.4.3-4.8 lakh crore, keeping supply-related concerns elevated.
- MPC minutes reaffirm that the bar for further rate cuts is high, limiting the scope for additional monetary easing. With a significant portion of liquidity support already deployed, incremental OMOs beyond the current round are likely to be limited.
- On the fiscal front, the Indian government's upcoming Union Budget for FY 2026-27 (to be presented in February 2026) is projected to target a central government debt-to-GDP reduction in the range of approximately 1.1-1.6 percentage points. This would bring the ratio down to around 54.5-55% for FY27 from the budgeted 56.1% in FY26 (itself a decline from 57.1% in FY25). This continues the fiscal consolidation path outlined in prior budgets, with a long-term roadmap aiming for a debt-to-GDP ratio of around 50% (±1%) by FY31.
- This projected reduction implies a fiscal deficit target for FY27 down from 4.4% in FY26, based on nominal GDP growth assumptions of 10-11%. For context, the FY26 fiscal deficit is budgeted at Rs.15.7 lakh crore (4.4% of GDP). Assuming a similar composition of deficit financing (where net G-sec market borrowings typically account for ~70-75% of the fiscal deficit, with the rest from small savings, external aid, and other sources), this would translate to net G-sec supply of approximately Rs.11-12.5 lakh crore for FY27. The FY26 net market borrowings are budgeted at Rs.11.5 lakh crore (with gross at Rs.14.8 lakh crore), so the FY27 projection represents continuity amid ongoing consolidation, even as nominal GDP expands.

Liquidity outlook; near term relief measures, medium term risks:

- OMOs are scheduled on January 5, 12 and 22 for Rs.50,000 Crore each, alongside the USD 10bn Fx swap. These measures should be adequate to manage liquidity over the next six months. However, continued Fx impact remains a key drain in liquidity to possibly curb the Fx volatility has been ~$10Bn for the week ended 19th Dec'25, tightening conditions despite OMOs.
- Advance tax outflows and currency leakage have continued to weigh on liquidity, though core liquidity surplus is expected to stabilise around Rs.3–4 lakh crore as government spending gains momentum. While parts of the market are beginning to price in the possibility of an additional Rs.1 lakh crore of OMOs in February–March, given expectations of improving BoP dynamics in Q1 and the RBI's stated preference for FX swaps over outright OMO purchases. That said, should liquidity conditions tighten again, the probability of a repeat or extension of liquidity measures cannot be ruled out, keeping policy optionality intact.
- Based on our FY26 liquidity estimates, maintaining system liquidity at 1.0–1.5% appears achievable at this stage, with the RBI having front-loaded support through OMO purchases and Fx swap operations. However, the liquidity outlook will remain sensitive to evolving factors, including progress on the US-India trade deal, USD/INR volatility and forward cover maturities along with the scale and timing of Q4 FY26 and FY27 govt borrowings.

Table 1: Drivers of Core Liquidity

INR Lakh Crore	Systemic Liquidity Balance	Govt. Balance with RBI	LTRO	Core Liquidity	Fx Impact	OMOs	LTROs	RBI Dividend	CIC	CRR
FY26 YTD	0.19	2.43	-	2.62	-5.77	3.67	-1.83	2.69	1.89	-1.83
FY 26 Est.	2.41	0.75	-	3.16	-5.75	5.22	-1.83	2.69	2.75	-1.66

Source: RBI, UBI Research

FY 26YTD Data till 19th Dec'25

Assumptions for FY26 Est.:

Forward Cover o/s as of Oct'25 is $63.6Bn of which $19.7Bn matures during 1-3 Months, we have assumed $15Bn to be rolled over.

Redemptions during Jan'26 of ~Rs.0.45 lakh crore from Central Bank ownership shall reduce OMOs.

CIC may edge up in Q4FY26 due to seasonality effect.

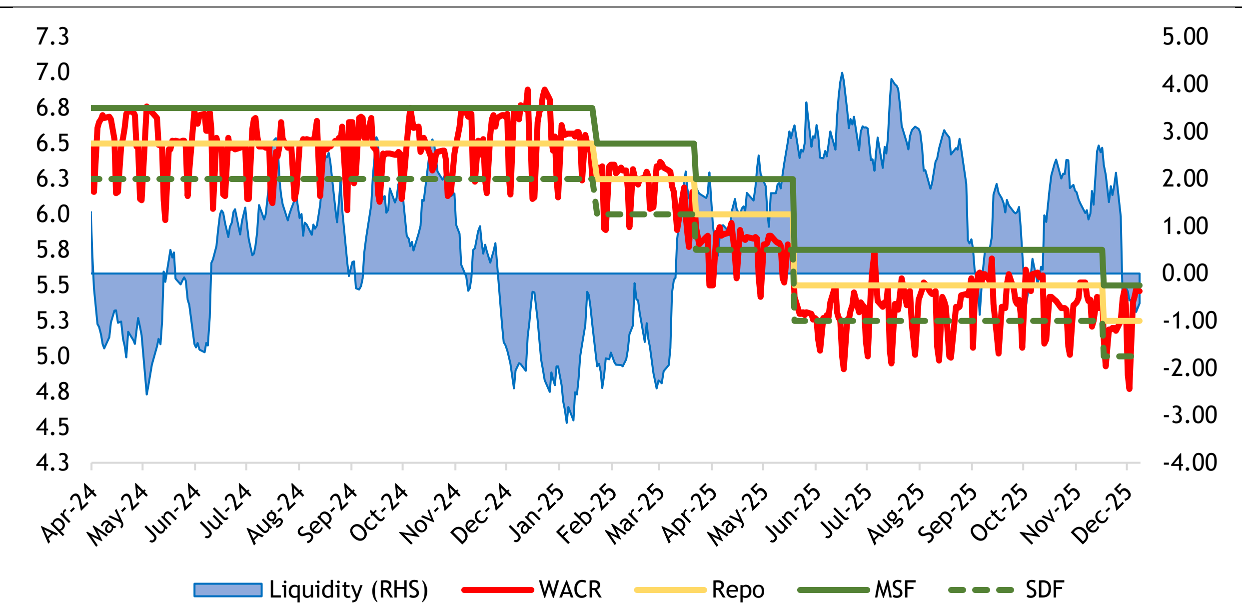
By:
Kanika Pasricha
kanika.pasricha@unionbankofindia.bank

Dhiraj Kumar
dhirajkumar@unionbankofindia.bank

Table 2: Market Snapshot Instrument	Yield (Dec 29)	Weekly Change	Commentary
10 Year G-Sec (6.33% GS 2035)	6.57%	-9 bps	Markets reacted on liquidity measures announced
1 Year T-Bill	5.55%	+5 Bps	Liquidity remained tight due to tax outflows
US 10 year Yield	4.11%	-5 bps	Taking cues from GDP & CPI data
Credit Growth (%) (as of 12th Dec'25)	11.7%	+19 bps	Credit & Deposit growth increased on fortnight basis and the gap widened
Deposit Growth (%) (as of 12th Dec'25)	9.7%	-46 bps	
Credit Deposit Wedge (bps) (as of 12th Dec'25)	200	+65 bps	

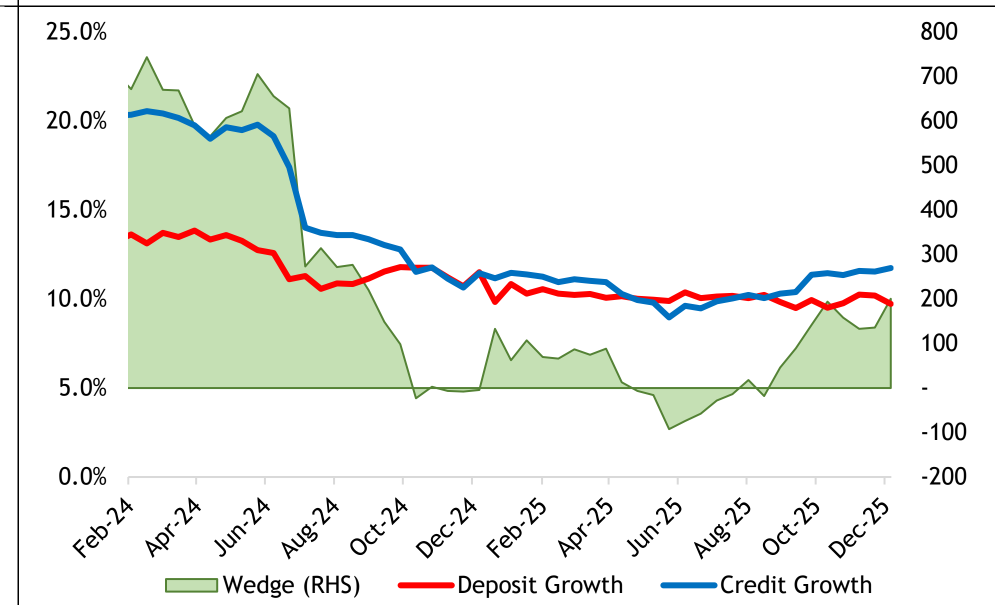
Source: RBI, CCIL, UBI Research

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



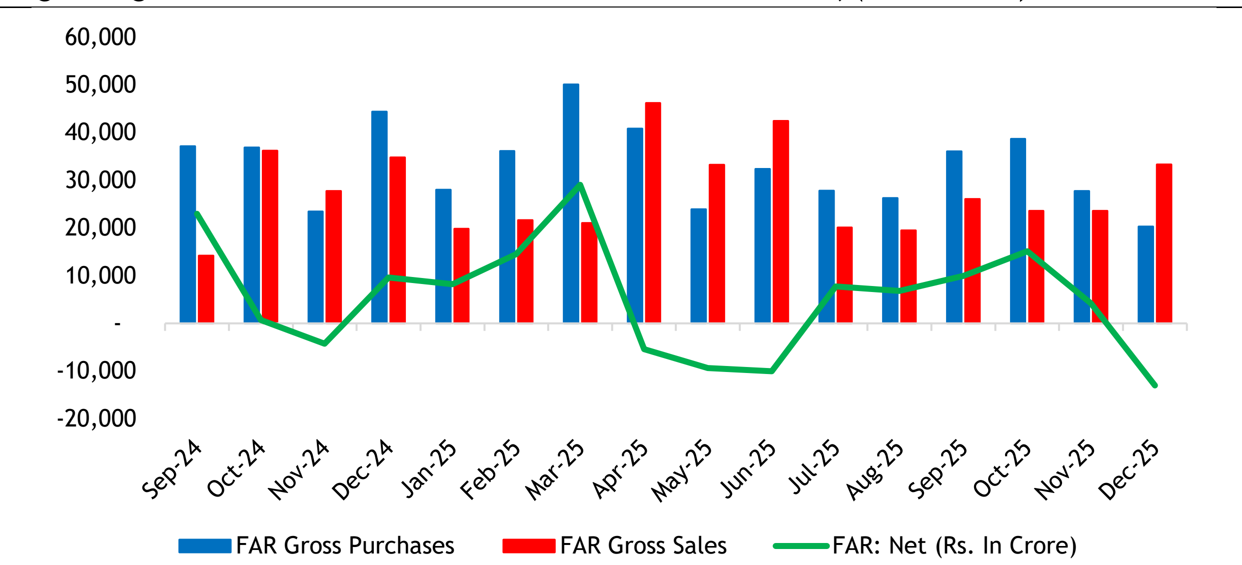
Source: Bloomberg, CEIC, UBI Research

Fig.3: Credit Deposit Gap widened at ~200 bps in fortnight ending 12th Dec'25



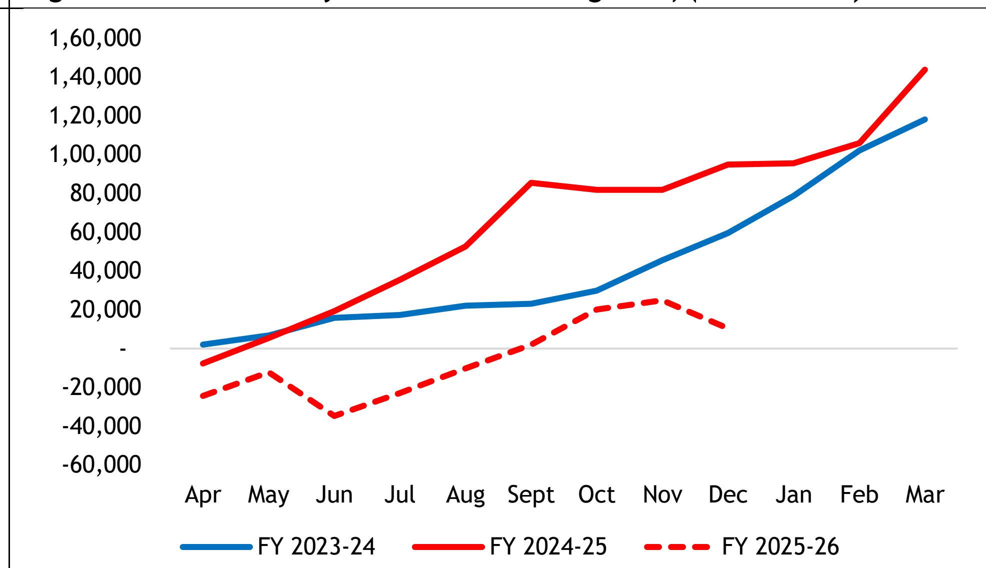
Source: CEIC, UBI Research

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	55.70
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	7.26	12.29	9.09	9.89	12.58	16.39	6.20	7.50	6.49	9.11	4.59	0.75	
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		
Vehicle registrations (% y/y)	25.28	4.37	2.78	14.53	4.58	-5.31	33.50	10.67	-8.82	6.34	-4.94	1.15	2.64	6.14	5.70	-2.49	3.95	6.70	41.80	1.08	
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		
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	8.74	8.50	8.64		
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		
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		
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	

Source: CEIC, UBI Research

Banking Research Team	
Kanika Pasricha **Chief Economic Advisor**	**kanika.pasricha@unionbankofindia.bank**
Suneesh K	suneeshk@unionbankofindia.bank
Nidhi Arora	nidhiarora@unionbankofindia.bank
Rajesh Ranjan	rajeshranjan@unionbankofindia.bank
Jovana Luke George	jovana.george@unionbankofindia.bank
Amit Srivastava	asrivastava@unionbankofindia.bank
Rohit Yarmal	rohitdigambar@unionbankofindia.bank
Dhiraj Kumar	dhirajkumar@unionbankofindia.bank
Akash Deb	akash510@unionbankofindia.bank
Shreyas Bidarkar	shreyas.bidarkar@unionbankofindia.bank