FI Weekly: Yields spike despite dovish MPC / FOMC policy

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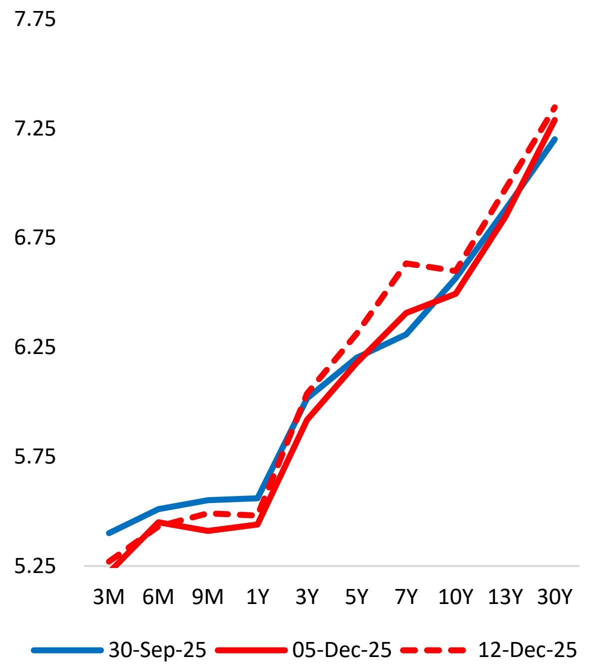
Fig.1: Yield curve movement during the week; (%)



Source: Bloomberg, UBI Research

Fixed income markets saw a reprieve today after last week's spike in yields, supported by easing inflation, proactive liquidity measures and clearer policy signaling. However, during the week gone by Indian government bond yields hardened despite softer-than-expected inflation, as markets continued to grapple with demand-supply dynamics. The RBI's decisive response through large OMO purchases, inclusion of the benchmark 10-year bond in the OMO basket, a USD-INR liquidity swap, and active fine-tuning operations has reinforced broad liquidity support and is likely to help anchor long-end yields and stabilize market conditions. Bond markets remained under pressure due to weakening demand-supply dynamics even as monetary policy stayed broadly dovish. The US Federal Reserve delivered a widely expected 25 bps rate cut but tempered dovish expectations through measured guidance, pushing US Treasury yields higher amid heavy issuance. Attention now shifts to diverging central bank paths, with the Bank of England preparing to ease while the Bank of Japan continues its gradual normalization.

Fed Cuts but yields push back on cautious easing:

- US Federal Reserve delivered a 25 bps cut at its December 9–10 meeting, lowering the fed funds target range to 3.50%–3.75%, marking the third rate cut in 2025. While the decision aligned with expectations, the accompanying communication was measured rather than dovish. Policymakers signaled a slower pace of easing in 2026, with one dissenting vote highlighting concerns around lingering inflation risks. Chair Powell emphasized that policy is now close to neutral and future actions will remain data-dependent.
- Despite the rate cut, US Treasury yields hardened over the week. The 10-year yield rose ~3-4 bps WoW to ~4.19%, driven by a combination of cautious Fed guidance and heavy Treasury supply, including a large 10-year auction. The move reflects market reassessment that the Fed has begun easing, but markets are no longer pricing aggressive follow-through in 2026.

Policy Divergence – BoE set to ease, BoJ moves to tighten:

Attention now turns to major central bank meetings scheduled for December 18–19, with policy divergence firmly in focus.

- Bank of England (BoE): Markets widely expect a 25 bps cut to 3.75%, reflecting cooling inflation and softening growth momentum. However, sticky services inflation and wage pressures may limit the scope for rapid follow-up easing in early 2026.
- Bank of Japan (BoJ): In contrast, the BoJ is expected to raise rates by 25 bps to 0.75%, continuing its gradual normalization. Rising wages, inflation near target, and a weak yen underpin the hawkish shift.

CPI Comfort and RBI liquidity measures likely to have salutary effect on yields:

- Indian government bond yield moved up by 10bps (benchmark 10-year yield) despite benign inflation data and proactive RBI liquidity measures.
- A key data was the November 2025 CPI print, which came in again below 1% (0.71%) for the second consecutive month. Softer food inflation and stable core (4.34% in Nov'25 Vs 4.41% in Oct'25) reinforced confidence in the disinflation trajectory. The data validated the RBI's recent dovish pivot and strengthened the case for maintaining a supportive policy stance.
- Following the 25 bps repo rate cut to 5.25% and the RBI reinforced its policy intent through decisive liquidity actions:
  - Rs.1 lakh crore of OMOs, split into two Rs.50,000 crore tranches on December 11 and December 18
  - Inclusion of the 6.33% GS 2035 (benchmark 10-year) in the OMO purchase basket
  - A $5 bn USD-INR buy/sell swap to inject durable liquidity
  - Continued fine-tuning operations to manage short-term rates
- The inclusion of the 6.33% GS 2035 marked a critical shift and signalled to move beyond generic liquidity infusion to active yield stabilization, improving transmission across the curve and signalling a willingness to cap long-end volatility and anchor benchmark yields.

Liquidity surplus holds, Market looks to Dec 18 OMOs for further direction:

- Liquidity has improved during Dec'25 with an average surplus of Rs.2.12 lakh crore vis-à-vis an average surplus of Rs.1.78 lakh crore during Nov'25. Since the effective date of CRR cut (06th Sep'25) the Fx impact (Rs.3.34 lakh crore) on liquidity has ousted the CRR cut infusion (Rs.2.23 lakh crore) with last tranche being effective from 29th Nov'25.

***Table 1: Drivers of* Change in Core Liquidity since CRR cut became effective** *(Rs. In Lakh Crore)*

Change in Core Liquidity (from 05th Sep'25 to 05th Dec'25)		**(1.60)**
Drivers of Core Liquidity (From 05th Sep'25 to 05th Dec'25)	***Fx Impact***	**(3.34)**
	OMOs	**0.27**
	CIC	**(0.77)**
	CRR	**2.23**

Source: RBI, UBI Research

- The credit growth of 11.5% (as of 28th Nov'25) has been above deposit growth of 10.2% (as of 28th Nov'25) created a Credit-Deposit gap of 134 bps which has remained unchanged over the previous fortnight of 133 basis. Hence, structural liquidity have continued to remain in deficit.
- System liquidity is in surplus of Rs.1.83 lakh crore and expected to be driven by advance tax & GST payments and Fx impact during the current week. Frictional liquidity challenges are being addressed by 11 day & 10 day VRRs adding to expectations of volatile money market in current month. The 11 day VRR auction conducted today was undersubscribed with banks bidding for Rs.24,969 Crore against the notified amount of Rs.75,000 Crore at a weighted average rate of 5.26% indicating muted demand because of cheaper option available for short term funding like TREPS (WAR of 5.09% on 15th Dec'25).
- The December 11 OMOs initially supported bonds, though gains moderated as the market assessed the bond mix. Sentiment improved meaningfully after confirmation that benchmark securities would be included, setting the stage for a stronger response to the December 18 OMOs.

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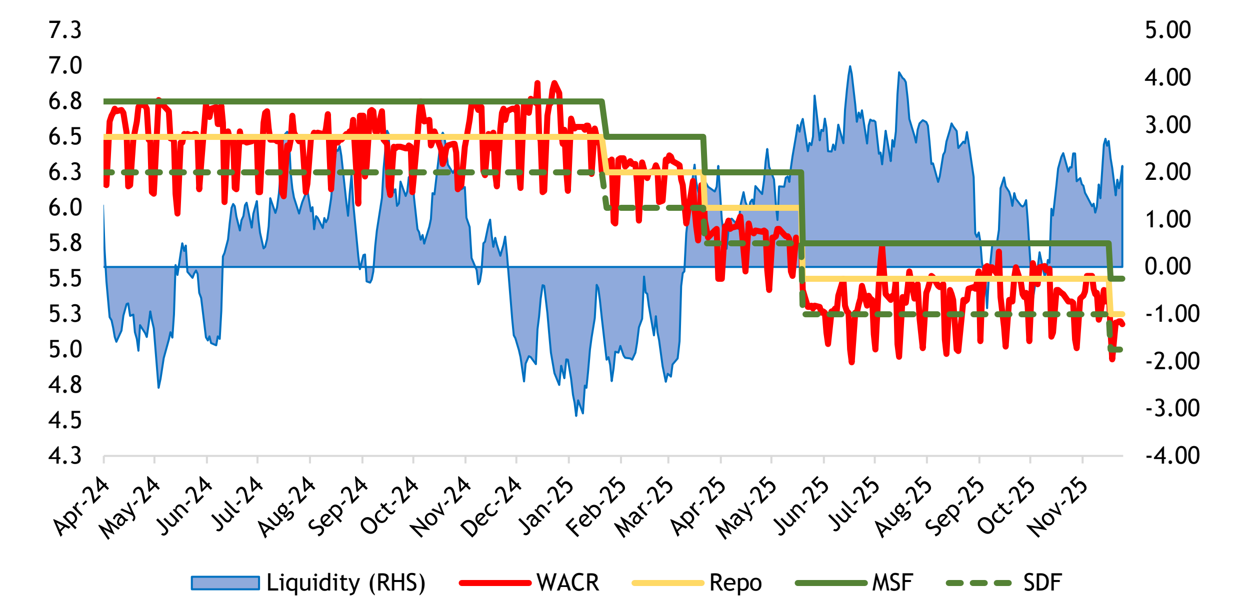
Table 1: Market Snapshot Instrument	Yield (Dec 12)	Weekly Change	Commentary
10 Year G-Sec (6.33% GS 2035)	6.61%	+10 bps	Post MPC rate cut
1 Year T-Bill	5.48%	+4 Bps	Worry on system liquidity with USDINR hitting record highs
US 10 year Yield	4.18%	+4 bps	Markets are not pricing aggressive rate cuts in CY26
Credit Growth (%) (as of 28th Nov'25)	11.5%	-5 bps	Credit & Deposit growth increased on fortnight basis and the gap narrowed
Deposit Growth (%) (as of 28th Nov'25)	10.2%	-4 bps	
Credit Deposit Wedge (bps) (as of 28th Nov'25)	134	+1 bps	

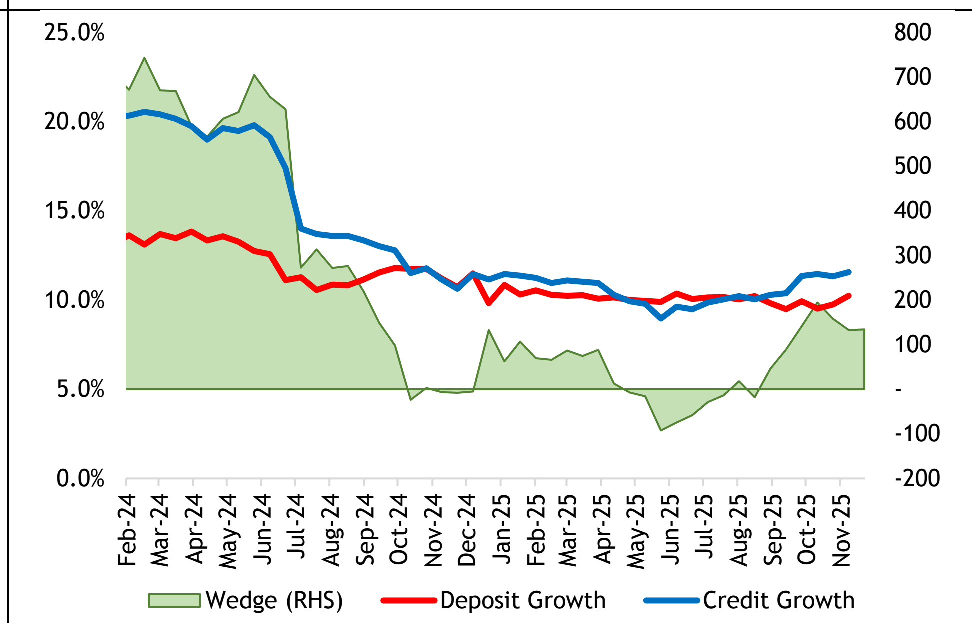
Source: RBI, CCIL, UBI Research

Fig.2: WACR moved up while managed to stay at lower end of corridor; (%)



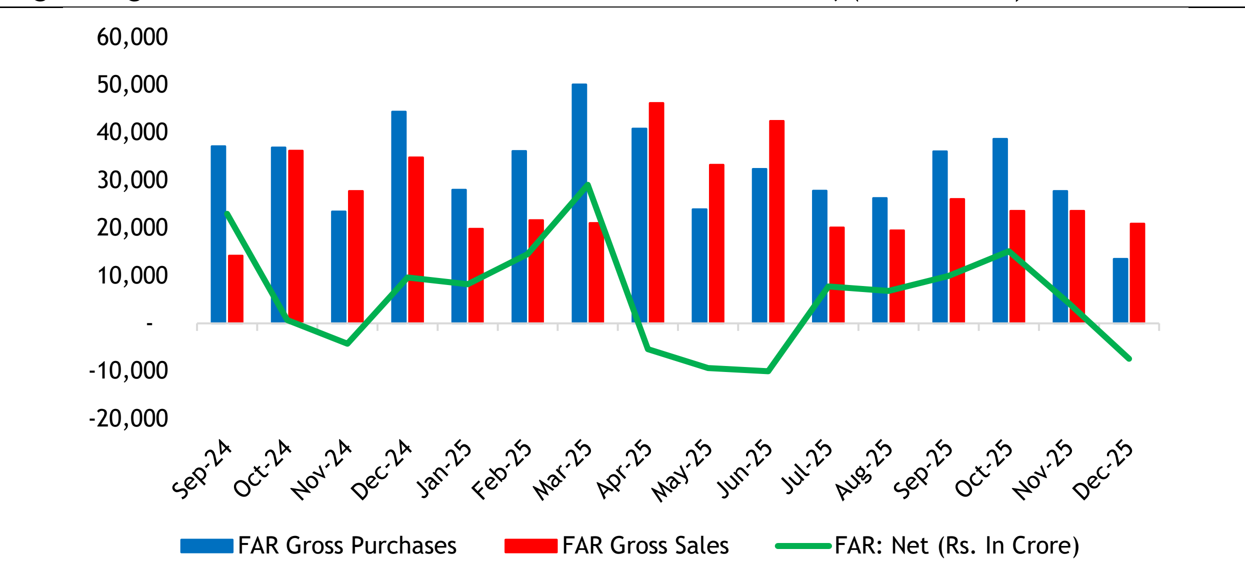
Source: Bloomberg, CEIC, UBI Research

Fig.3: Credit Deposit Gap narrowed at ~134 bps in fortnight ending 28th Nov'25



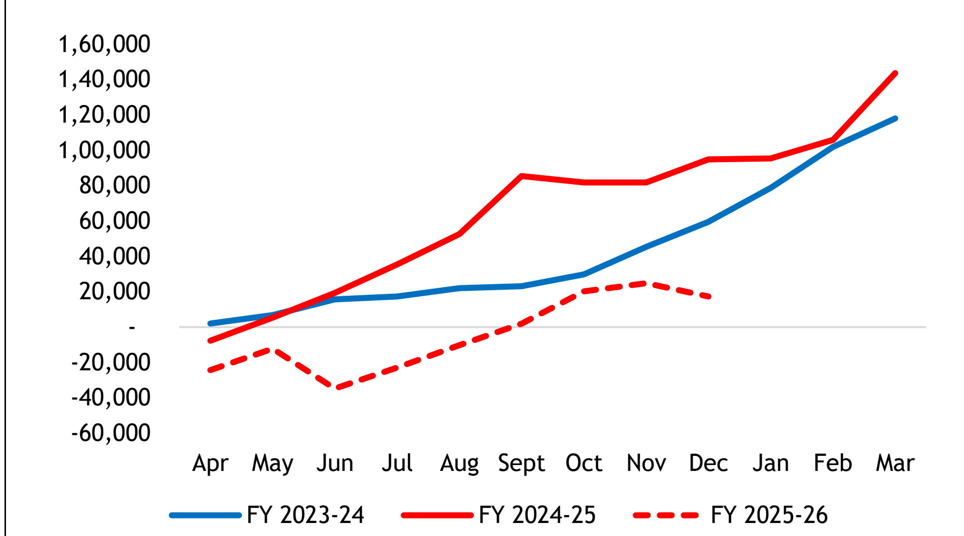
Source: CEIC, UBI Research

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



Source: Bloomberg, 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
	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
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
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	16.59	-5.34	-1.53	-2.64	-10.86	0.85	-3.82	-1.23	-1.34	13.34	5.81	6.19	-11.80	19.37
Imports (% y/y)	11.08	7.35	5.25	11.91	10.44	8.29	3.45	16.75	2.75	10.66	-14.81	12.13	20.00	-1.33	-3.41	9.10	-9.54	18.01	16.64	-1.98
	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	9.80	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	8.28	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	80.60	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

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