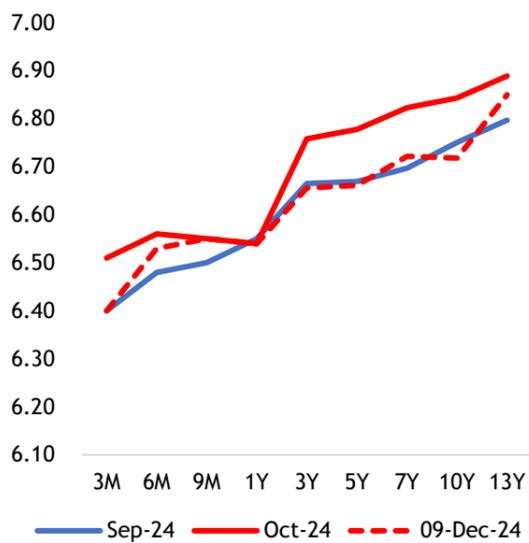
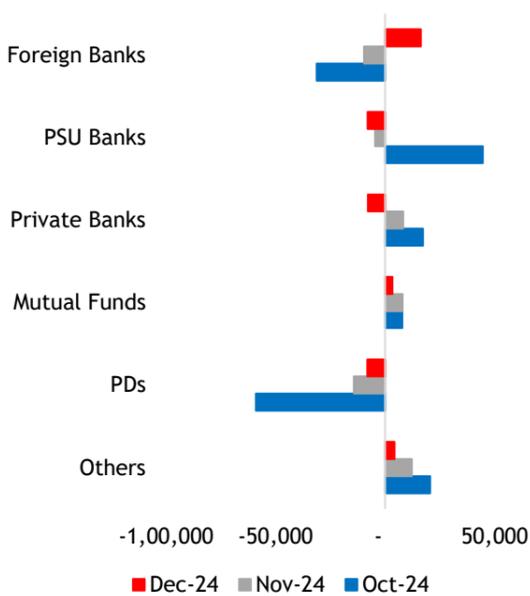


Fig.1: India yield curve movement ; (%)



Source: Bloomberg, UBI Research

Fig.2: Foreign Banks have turned buyers in December after two months of sell-off; (Rs.in Crore)



Source: Bloomberg, UBI Research

The December MPC gave relief to the market in terms of liquidity support, however, the long term yields spiked post decision as the governor clearly asserted inflation risks need policy focus as they have also played a role in curbing slowdown in consumption and growth. As per our estimates, Rs.2.95 lakh crore worth of liquidity was taken away during Oct-Nov-24 due to forex impact as Rupee hits record highs. A cut of 50bps in CRR shall infuse Rs.1.16 lakh crore over two fortnights commencing 25bps from 14th Dec and another 25bps starting 28th Dec. It is more likely a relief to the Banking system liquidity which lost durably in past 2 months. Another announcement of increasing spreads of FCNR(B) deposit with the likely intent to attract stable USD flows given the pressure on Rupee. We believe this measure to have limited impact on flows as FCNR rates are already prevailing way below the current ceiling which indicates that more policy levers to incentivize banks to attract more flows. Indian bond yields softened 2-3 bps on market buzz that cut may happen “sooner than later” post appointment of new RBI Governor Mr. Sanjay Malhotra in place of Mr. Shaktikanta Das.

US labor market not strong enough, rate cut most likely

- The US NFP for the month of November rose by 227k. The October reading was revised by 36k and came above market expectations of 200k.
- The NFP data beats the forecast, however, they were not strong enough to undermine the case for a final reduction this year. Meanwhile, the probability of rate cut pricing jumped to 86% from 72% last week as per CME FedWatch Tool.

MPC gave CRR cut, IGBs cheer new RBI Governor

- The Q2FY25 GDP print at 5.4% has pre-loaded expectations of rate cut in India. However, the MPC announcement of CRR cut spooked the yields which hardened to 6.75% (new benchmark), while softened by 2-3 bps post announcement of new RBI Governor.
- The MPC sharply revised lower the FY25 growth forecast to 6.6% from 7.2% previously, primarily led by drop in Q3 projection to 6.8% (from 7.4% despite festive season effects) while the Q4 forecast is reduced by 20bps to 7.2%. MPC revised higher the CPI inflation forecast to 4.8% for FY25 with Q3 and Q4 CPI now pegged at 5.7% and 4.5% respectively, from 4.8% and 4.2%. MPC was balanced in its guidance, and it emphasised that “strong foundations for high growth can be secured only with durable price stability”. The RBI Governor asserted that “at this critical juncture, prudence and practicality demand that we remain careful and sensitive to the dynamically evolving situation with all its complexities and ramifications”. (Refer our Report: [Dec'24 RBI MPC](#))
- Mr. Sanjay Malhotra to succeed Mr. Shaktikanta Das as the new RBI Governor. While the new RBI Governor’s views on economy / monetary policy are less known, we will watch out for his announcements in 3 areas i) Growth - Inflation Balance, ii) Macro prudential regulations (LCR, ECL etc.) iii) Fx in a world dealing with high volatility. Post announcement of new governor, the bond yield curve have shown buying momentum below 10 year segment as rate cut expectations shall lead to steepening of yield curve.
- Under FAR securities, the foreign buying has returned to the Indian Bonds markets. The below 10-year segment has witnessed major chunk of buying of Rs.7,063 Crore of the total FAR securities buying of Rs.9,343 during the month of December.

CRR cut to ease, GST outflows to tighten the liquidity

- The CRR cut of 50bps may not be enough to drive banks towards deposit cuts:
 - Liquidity of 0.5% of NDTL only partially offset the permanent loss on FX outflows
 - Profitability impact of CRR cut is relatively limited at -3-4bps
 - Banks may consider a shift in funding mix as well away from high-cost Bulk deposits
 - Outlook for FY25 if we assume deposit YoY growth remain in 11.0%-11.5.0% range & assuming the incremental CD ratio 80-85% credit YoY growth drops to 11.0 -11.5% in FY25 from 16% last year excluding merger effect.
- Currently, the system liquidity is in surplus of Rs.0.23 lakh crore whereas the fall in core liquidity is the cause for concern which is getting hit due to Fx impact (Fig.3). More importantly to note that the FY25 Core liquidity may slip to deficit unless Fx outflows reverse (Fig.5).
- After two months of consistent selling by FPIs in equity, they have turned buyers in December 2024. Till date they have bought Rs.23,668 Crore of equity and Rs.11,914 Crore of FAR securities.
- The fall in Fx Reserves stopped after consecutive 8 weeks, to \$658.09 Bn, as on the week ended 29th Nov-24.
- The government balance has moved from Rs.1.3 lakh crore to Rs.0.44 lakh crore during the week ended 29th Nov'24. Going forward, we expect advance tax flows to pop up government balance in the first fortnight of Dec-24.
- Bank’s borrowings through CDs rose sharply in November ahead of heavy debt maturities in December. Also, the liquidity deficit in last month has also resulted in increased demand for funds from the Banks. The sign of worry is the outstanding of CDs which is at all time high of Rs.4.92 lakh crore. On Gross issuance basis, the Q2FY25 Rs.2.53 lakh crore of CDs were issued, while, in Q3FY25 till 29th Nov-24 Rs.1.70 lakh crore of CDs were issued as demand for funds has weakened with Credit-Deposit wedge closing.

Fig.3: Drivers of Liquidity during Oct-Nov-24; (Rs.in lakh crore)

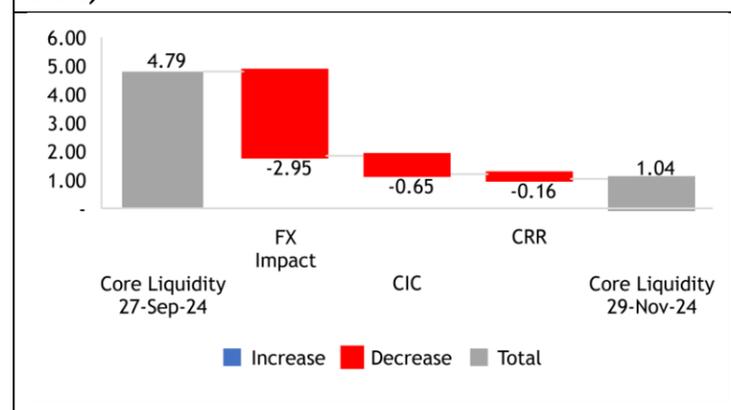
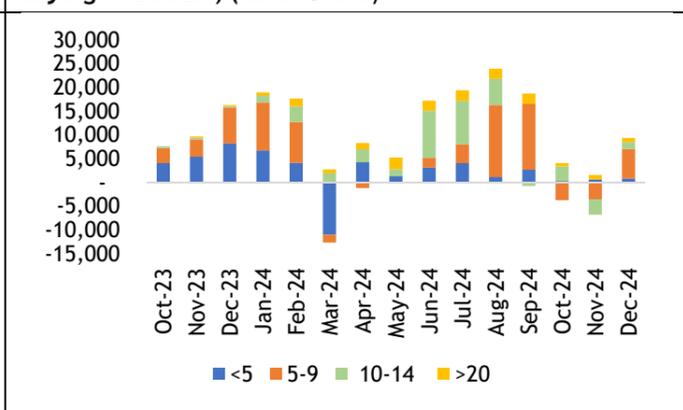


Fig.4: FAR securities below 10 year segment saw buying in Dec-24; (Rs.in Crore)



Source: CEIC, NSDL, RBI, UBI Research

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