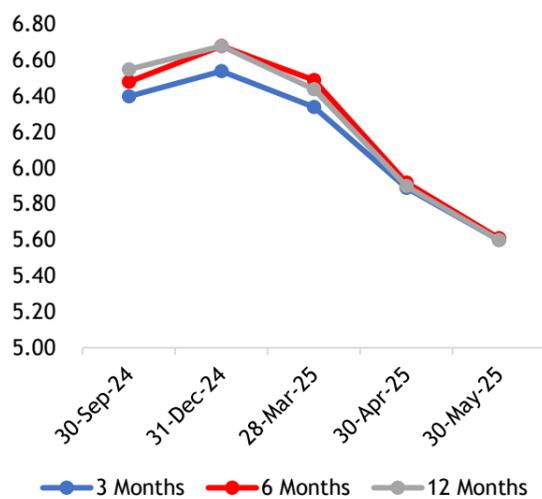
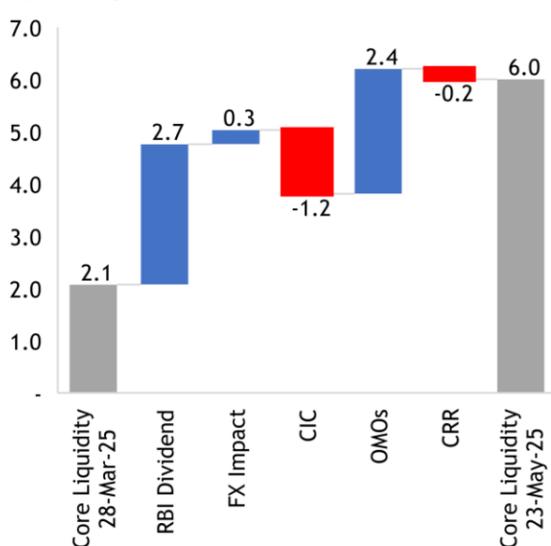


Fig.1: Surplus system liquidity and strong rate cut expectations squeezed spread below 1 year (T-bills)



Source: FBIL, UBI Research

Fig.2: Drivers of liquidity showing RBI dividend played its part



Fx Impact is net of LT Swap o/s of \$25Bn
Source: RBI, CEIC, UBI Research

US 10Y yield dropped 10 bps to 4.4% in the final week of May'25, as markets priced in softer PCE inflation (0.1% MoM) and slower personal spending (0.2%), while renewed US-China trade tensions and tariff rollbacks added to risk-off sentiment. Back home, RBI's Rs.2.69 lakh crore dividend payout on 23rd May pushed core liquidity to Rs.6.01 lakh crore (~2.7% of NDTL), with govt. balance swelling to Rs.4.3 lakh crore. RBI appears comfortable with WACR drifting below repo and nearing SDF, though the liquidity framework targets alignment of WACR with the repo rate. Surplus liquidity kept the 364D T-bill cut-off bullish at 5.62%, down 28 bps from end-Apr and 92 bps since Feb MPC, outpacing the 50 bps repo cut in the same period. CD-T-bill spread widened to 90 bps+, up from <80 bps at FY26 start, reflecting uneven liquidity distribution despite surplus; CP issuance also picked up, rising Rs.0.99 lakh crore to Rs.5.42 lakh crore by mid-May. G-Sec yields initially dipped to 6.24% on dividend and easing CPI, before rebounding to 6.29% post Q4FY25 GDP surprise at 7.4%. FY25 GDP came in at 6.5% vs 9.2% in FY24, while FY25 fiscal deficit stood at 4.77% of GDP (Rs.15.77 lakh crore), slightly above RE in value but below in ratio due to higher nominal GDP.

US 10Y fell on renewed US-China trade tensions & benign inflation expectations:

- The US 10Y yield declined from 4.5% to 4.4% in the final week of May'25, as softer PCE inflation at 0.1% MoM and a slowdown in personal spending to 0.2% reinforced expectations of a potential Fed rate cut later this year.
- Renewed US-China trade tensions and the temporary return of tariffs under the Trump administration added to market caution, driving a 10 bps fall in yields as investors shifted towards safe-haven assets.

How RBI dividend bounty came by

- The RBI's balance sheet grew by 8.2% to Rs.76.25 lakh crore in FY 2024-25, reflecting an increase in assets such as foreign currency reserves, gold, and government securities. Net income rose by 27%, primarily driven by higher global interest rates—which boosted returns on RBI's foreign investments—and gains from active foreign exchange operations amid rupee volatility.
- The interest income from foreign securities have increased from Rs.65,327 crore to Rs.97,006 crore during FY2024-25 recording a jump of 48%.
- The central bank recorded a substantial increase in income from foreign exchange transactions, earning Rs.1.11 lakh crore during the year compared to Rs.83,616 crore in the previous fiscal showing a jump of 33.73%. Markets were anticipating an average cost of below Rs.80/\$ for reserves as RBI nearly sold , which turned out to be -Rs.82/\$ pretty much above Rs.77.69/\$ last year.

Liquidity, Money market

- As per RBI weekly data, the Govt. balance has jumped to Rs.4.3 lakh crore on account of transfer of RBI dividend of Rs.2.69 lakh crore on 23rd May'25. This has led to a sharp increase in Core liquidity to Rs.6.01 lakh crore, which is c.2.7% of NDTL. The RBI dividend payout has played its part in making Core liquidity reach beyond this level. In Jun'25 we may witness further increase in banking system liquidity as high govt. balance spills over to banking system.
- RBI seems comfortable as WACR has moved below repo close to SDF rate. However, as per liquidity management framework objective is alignment of WACR with repo rate. The latest 364D T-bill cut off remained bullish at 5.62% down by 28bps from 30th Apr'25 showing comfort in lower tenures due to surplus liquidity.
- At the start of rate cutting cycle in Feb'25, the 364D T-Bill cut off as of 05th Feb'25 was 6.54% which has lowered to 5.62% as of 28th May'25. Even with MPC cutting down repo rate by 50bps since Feb'25 the 364D T-bill was down by 92 bps on the basis of surplus system liquidity.
- The 1 year CD-Tbill spread which squeezed to below 80bps at the start of FY 2026, has again expanded to 90bps & above in May'25 while it is still lower than Mar'25 of more than 100bps. Even with surplus banking system liquidity, the money going back to SDF due to weak credit demand. The Have-nots are currently commanding the pricing power thereby leading CD-T-bill spreads higher.
- There has been a noticeable increase in issuance of Commercial Papers (CPs). The CPs outstanding has shown an uptick of Rs.0.99 lakh crore from Rs.4.43 lakh crore as of 31st Mar'25 to Rs.5.42 lakh crore as of 15th May'25. This is to be closely watched as it has implications for bank credit growth since corporates may be shifting to CP market for their short term borrowings apart from weak credit demand which is reported below 10% for the 2nd consecutive fortnight.

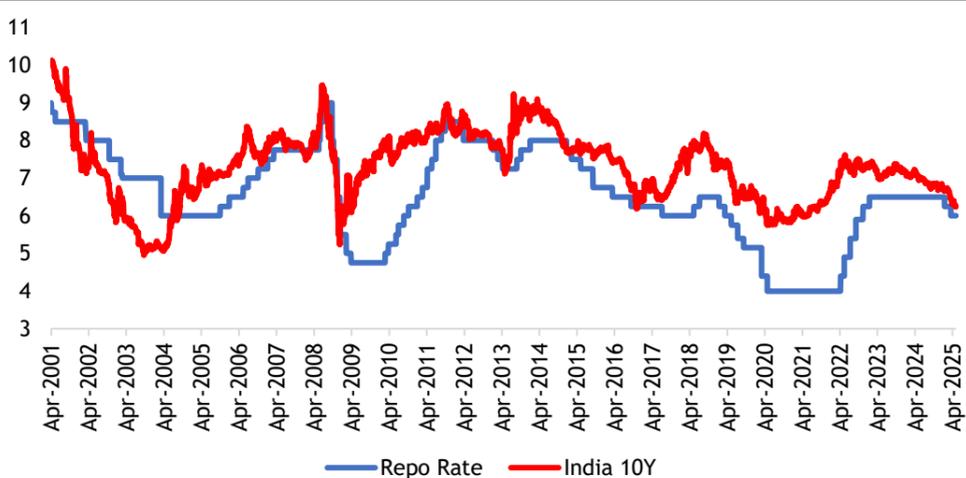
Short term rates slipped, while long term rose post GDP data

- The 10-year benchmark yields moved to a low of 6.24% on easing liquidity further with RBI dividend announcement of Rs.2.69 lakh crore and easing inflation (CPI) numbers providing room for further rate cuts. However, the better than expected Q4FY25 GDP data has spoiled the momentum of the G-Sec market and took the G-Sec to 6.29%.
- India's Q4 FY25 GDP recorded a growth rate of 7.4%, exceeding expectations and highlighting the strongest quarterly performance of the fiscal year. This growth was largely attributed to robust activity in the construction and manufacturing sectors, complemented by a significant rise in net indirect tax collections, which suggests increased economic activity and better compliance. For the full fiscal year, FY25 GDP growth moderated to 6.5%, down from 9.2% in FY24, reaching a four-year low. Despite this slowdown, India continued to be recognized as the world's fastest-growing major economy. In the future, analysts anticipate FY26 growth to fall within the range of 6.3% to 6.6%, driven by possible monetary easing and resilient domestic demand.
- Prices of G-Secs slumped after India's GDP growth of Q4FY25 was notified as 7.4%, higher than market consensus of 6.8%. Traders sold because the trajectory of rate cuts during 2025 has become uncertain, while 25bps cut remaining on table. Few market participants expectation of 50bps cut in June also diminished. However, in our view, we continue to expect 25bps cut in upcoming MPC meets of June and August. Market is divided on terminal repo rate in this cycle, we are at 5.5% while market is at 5%. For a terminal rate of 5.5%, WACR operating rate shall be 5.25% on surplus liquidity.
- Post market hours on 30th May'25, RBI announced a buyback auction of Rs.25,000 crore which was unforeseen. Also, no provision was made for such buybacks in FY26 budget. The buyback securities having maturity of 2026 & 2027, which shall impact short term rates slipping while long term rates rose post GDP data.
- India Fiscal deficit for FY 24-25 came in at 4.77% of GDP i.e. Rs. 15.77 Lakh Cr (100.5% of RE) vis-à-vis revised estimate (RE) of 4.84% of GDP i.e. Rs. 15.70 Lakh Cr. Even after exceeding the target by about Rs.7,700 Cr in absolute terms, the fiscal deficit was contained in terms of percentage target due to higher nominal GDP print for FY24-25. The fiscal consolidation was in place despite lower tax revenue and higher capital expenditure on revex rationalisation.
- On the market activity front, Foreign Banks were buyers and PSU Banks were sellers in past two consecutive years, the trend has started to reverse in FY26.
- Currently, the spread between G-Sec 10Y yield and repo rate has squeezed to 25bps and would like to wait for MPC decision due from 4th to 6th Jun before moving further.

Table 1: Market Snapshot Instrument	Yield (May 30)	Weekly Change	Commentary
10 Year G-Sec (6.79% 2034)	6.29%	+3 bps	Yields jumped as GDP numbers came in higher than market consensus
1 Year T-Bill	5.60%	-6 bps	Lower cut-off signals strong demand amid surplus liquidity
WACR (avg.)	5.78%	-7 bps	Dipped below to repo on multiple days, reflecting surplus liquidity
US 10 year Yield	4.40%	-11 bps	Benign inflation (PCE) along with geo-political concerns led to softening of yields
Credit Growth (%) (as of 16 th May'25)	9.8%	-5 bps	Credit Deposit wedge closure continues with credit slow down
Deposit Growth (%) (as of 16 th May'25)	9.9%	-14 bps	
Credit Deposit Wedge (bps) (as of 16 th May'25)	(16)	-9 bps	

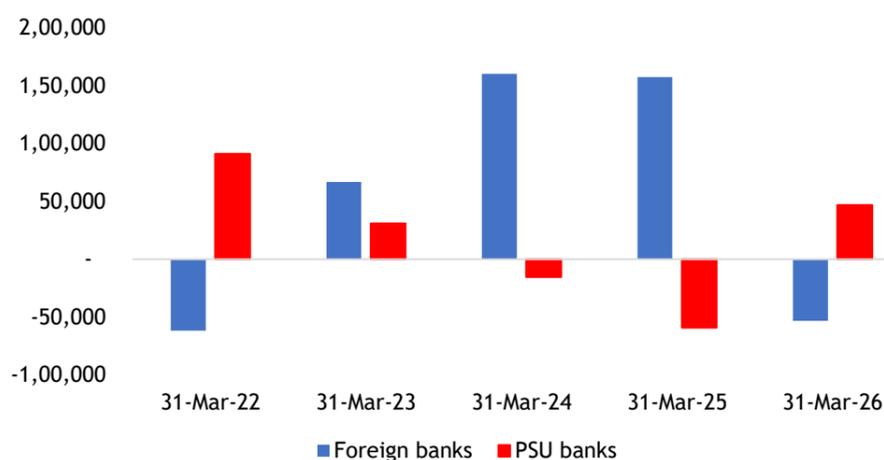
Source: RBI, CCIL, UBI Research

Fig.3: India 10Y approaching Repo rate



Source: Bloomberg, CEIC, UBI Research

Fig.4: Foreign Banks were buyers and PSU Banks were sellers in past consecutive years, the trend has started to reverse in FY26



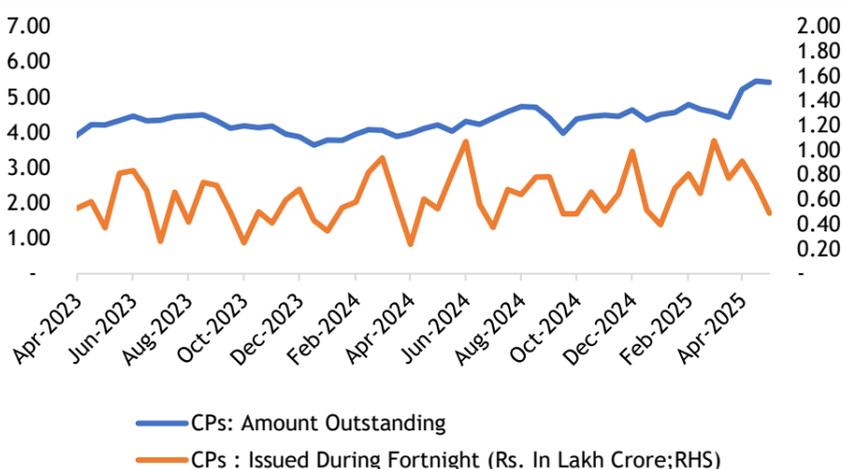
Source: Bloomberg, UBI Research

Fig.5: RBI's Exchange gain/loss from foreign exchange transactions moved higher with increased volumes & depreciation of Rupee

	O/s Reserves (\$ in Bn)	Avg. Cost of Reserves (Rs./\$)	Purchase (\$ in Bn)	Sale (\$ in Bn)	Exchange G/L (Rs.in Crore)
FY 20	476	60.46	72	27	300.00
FY 21	579	68.01	162	94	506.00
FY 22	618	67.80	114	97	690.00
FY 23	578	75.35	187	213	1,033.08
FY 24	646	77.69	194	153	836.15
FY 25	665	82.21	364	399	1,111.43

Source: Bloomberg, UBI Research

Fig.6: CPs issuance gained traction in Q1FY26



Source: RBI, CEIC, UBI Research

Table 2: 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
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
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	61.20
GST Collection (YoY Gr%)	12.42	9.96	7.63	10.28	9.99	6.47	8.92	8.54	7.26	12.29	9.09	9.89	12.58	16.39
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	
Vehicle registrations (% y/y)	26.93	3.53	1.65	14.08	3.49	-7.46	33.64	13.87	-11.45	7.72	-5.38	0.61	3.23	
Exports (% y/y)	1.98	13.27	2.44	0.63	-9.93	-0.30	16.57	-5.30	-1.53	-2.62	-11.08	0.66	9.03	
Imports (% y/y)	11.07	7.30	4.64	11.19	9.97	7.77	1.89	16.10	2.32	10.31	-16.34	11.36	19.13	
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	
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	4.10	
Transmission														
Bank Credit (YoY Gr%)	19.21	20.72	17.40	13.71	14.03	12.34	11.80	11.16	11.16	12.53	12.26	11.03	9.93	
Bank Deposits (YoY Gr%)	12.56	14.02	11.12	10.57	12.72	10.38	11.50	11.25	9.83	12.12	12.01	10.28	9.89	
C-D Ratio (%)	79.90	79.90	79.70	79.70	78.80	79.60	79.80	79.90	80.80	80.60	80.80	81.10	79.90	
WALR O/s Rupee Loans (%)	9.81	9.81	9.89	9.89	9.89	9.88	9.88	9.87	9.86	9.85	9.78	9.75	9.68	
WALR Fresh Rupee Loans (%)	9.55	9.39	9.32	9.40	9.41	9.37	9.54	9.40	9.25	9.32	9.40	9.35	9.26	
WADR O/s (%)	6.91	6.92	6.91	6.92	6.93	6.95	6.96	6.98	7.00	7.02	7.02	7.04	7.01	
WADR Fresh (%)	6.48	6.47	6.46	6.48	6.46	6.54	6.44	6.47	6.58	6.57	6.49	6.65	6.30	
MCLR 1 Year - Median	8.85	8.79	8.85	8.85	8.93	8.95	8.95	9.00	9.00	9.00	9.05	9.00	9.00	

Source: CEIC, UBI Research

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