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panorama

December 2025



## RBI's rate-cut cycle appears largely complete, with scope for at most one further 25 bps cut

- The RBI MPC cut the repo rate by 25 bps in December 2025 while maintaining a 'neutral' policy stance
- RBI projects inflation to bottom out in the Dec'25 quarter and remain anchored around the 4% target in H1FY27
- Upside risks to inflation, such as higher oil prices or adverse weather, could constrain further RBI easing
- We expect the RBI to be near the end of its rate-cut cycle, with scope for a final 25 bps cut if conditions allow
- RBI is expected to maintain banking system liquidity in a sufficiently large surplus to support credit growth
- Rate cuts late in the easing cycle have a limited impact on long-term yields as spreads widen
- Gross G-sec supply expected to be heavy due to limited fiscal consolidation and large redemptions
- Heavy supply will likely exert upward pressure on yields



## Capital expenditure growth expected to slow down

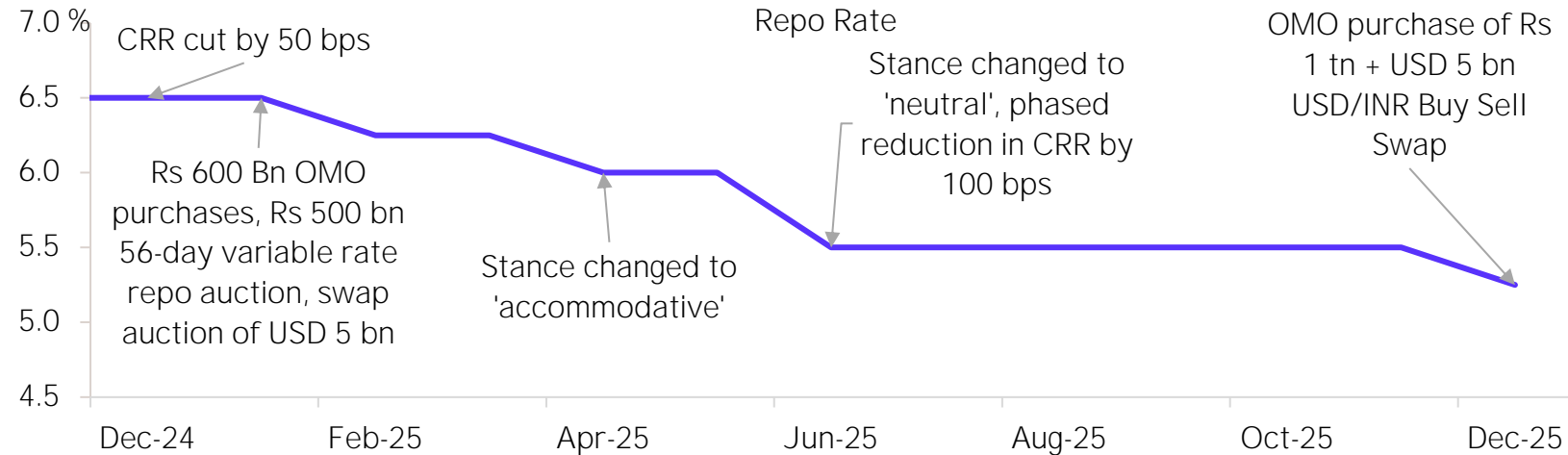
- Central Government's capex has witnessed a strong growth of 32% YoY in FYTD October 2025
- However, budgeted FY26 capex growth of 7% YoY implies a slowdown for the rest of the fiscal year
- Capex growth in FY27 may also remain muted, given the expected fiscal consolidation
- Higher social and welfare spending is likely to cap states' capex growth as well
- Private sector capex was muted in H1FY26, but the investment pipeline remains strong
- Contraction in residential sales points to a slowdown in household capex
- Weak employment is likely to be a structural drag on residential sales and household investment

# Monetary Policy and Debt Markets



# RBI is likely nearing the end of its rate-cut cycle

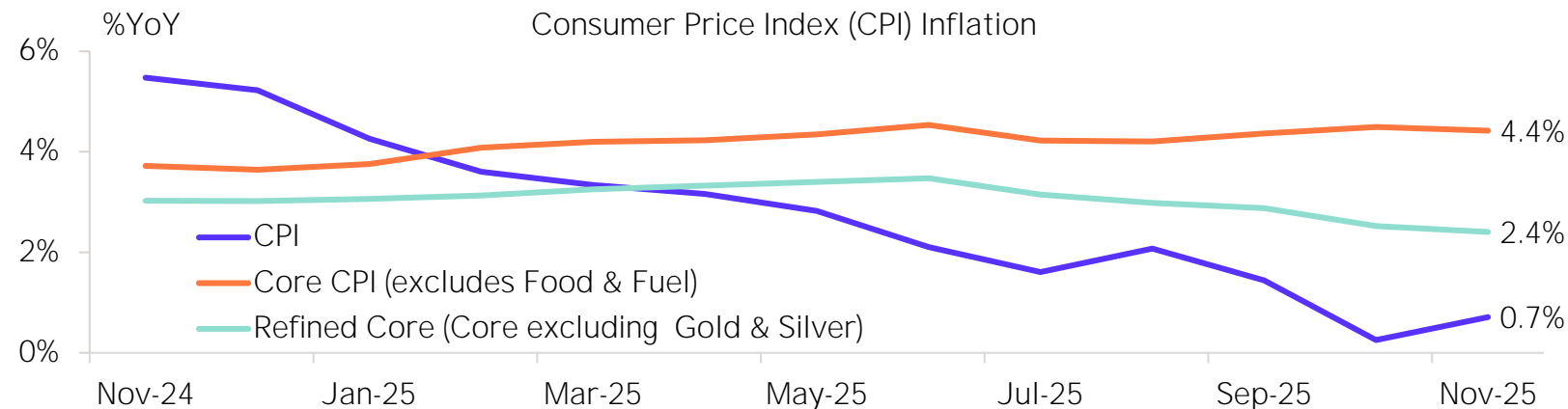
Favourable growth–inflation dynamics could create room for a final 25 bps rate cut in the current easing cycle



The RBI MPC reduced the repo rate by 25 bps in the December 2025 policy

The policy stance remained unchanged at 'neutral'

We believe the RBI is nearing the end of its rate-cut cycle, with a final 25 bps cut likely if growth–inflation dynamics permit

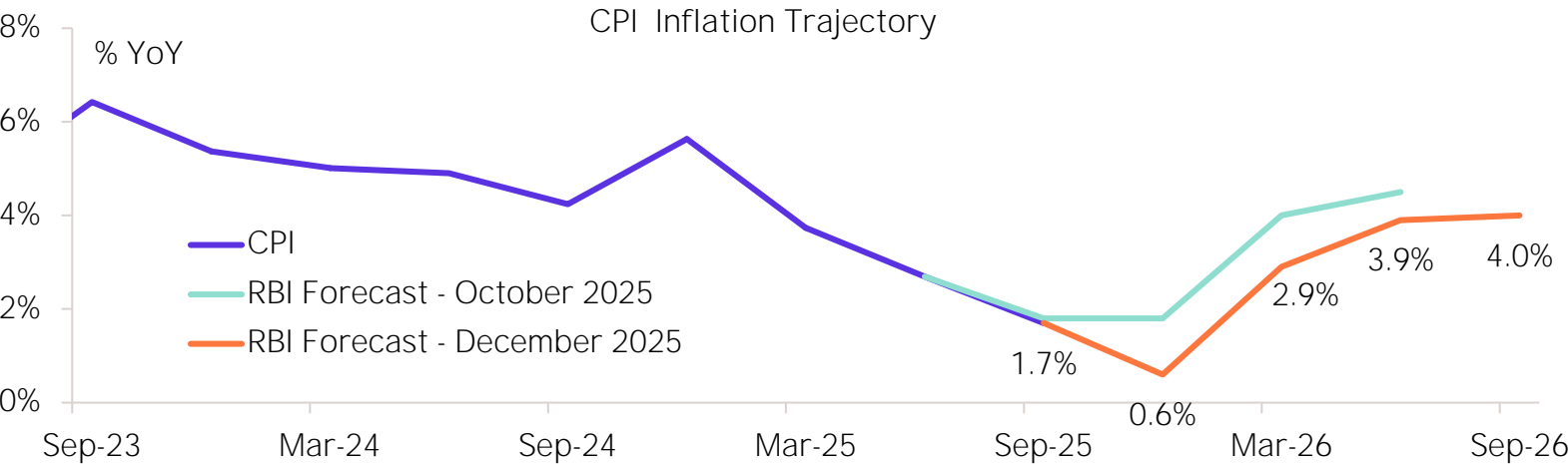


RBI highlighted in the December policy that underlying inflation pressures are even lower than suggested by the headline and core inflation prints, as these have been lifted by rising precious metal prices

If underlying inflation remains benign, there may be room for further easing

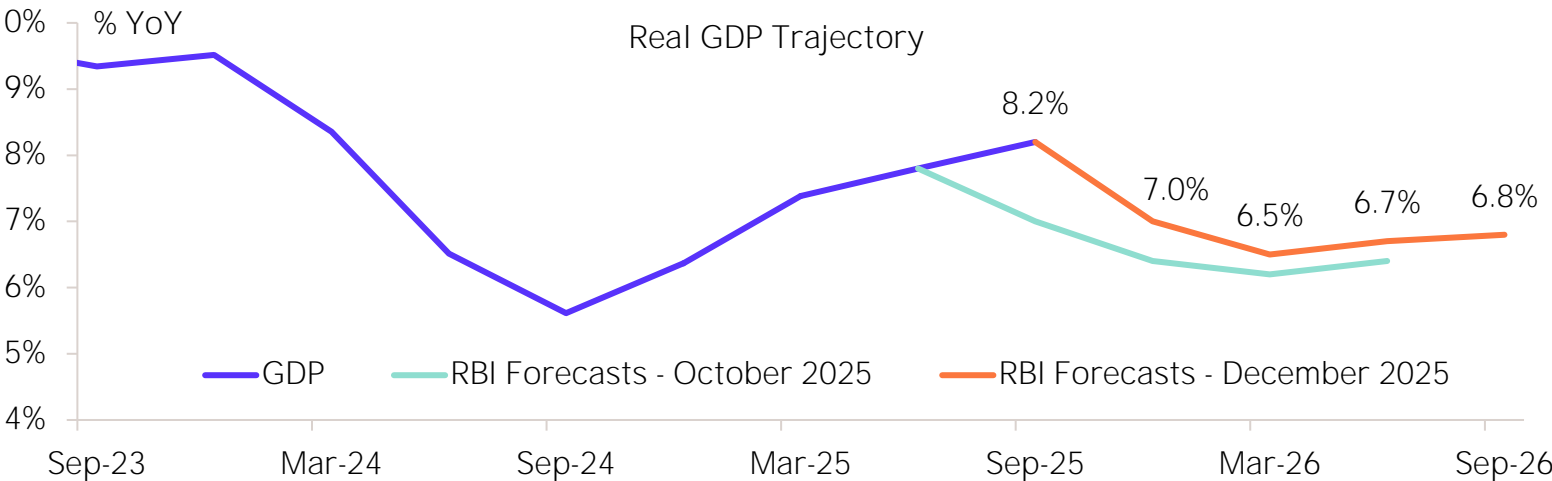
# RBI projects inflation to bottom out in the December quarter

GDP growth is expected to moderate to 6.5–7% YoY over the next few quarters



Inflation is expected to bottom out in the December 2025 quarter and remain anchored around the 4% target in H1FY27

However, there may be upside risks to this trajectory (such as higher oil prices or adverse weather conditions affecting agricultural output) that could limit the RBI's ability to pursue further easing

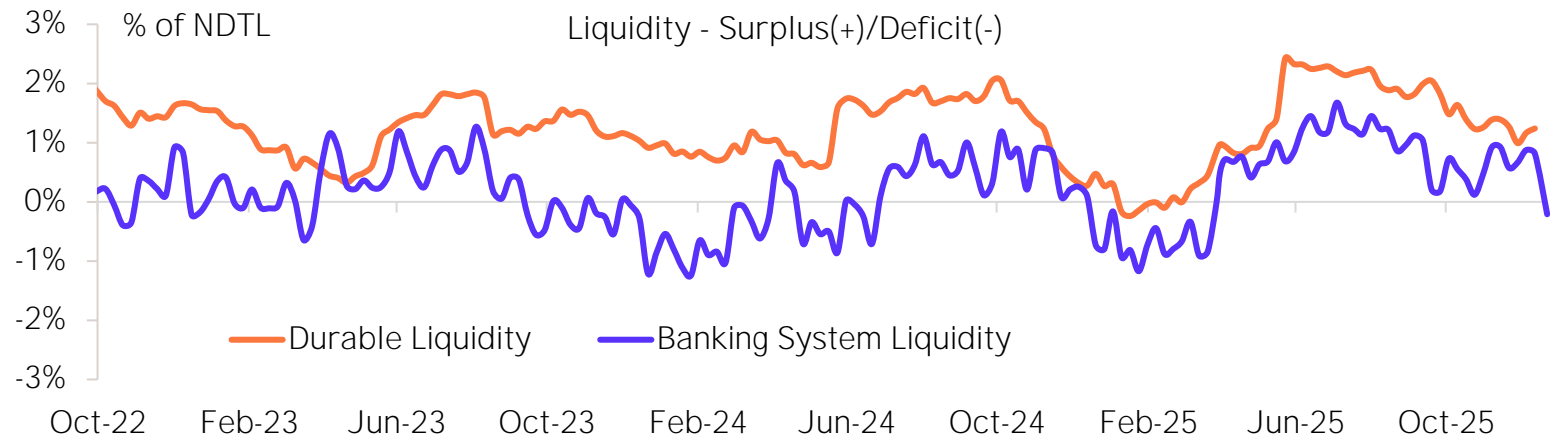


The RBI projects growth to moderate to a healthy 6.5–7% YoY over the next few quarters

Such growth would not, on its own, justify policy easing if there are upside risks to the inflation trajectory

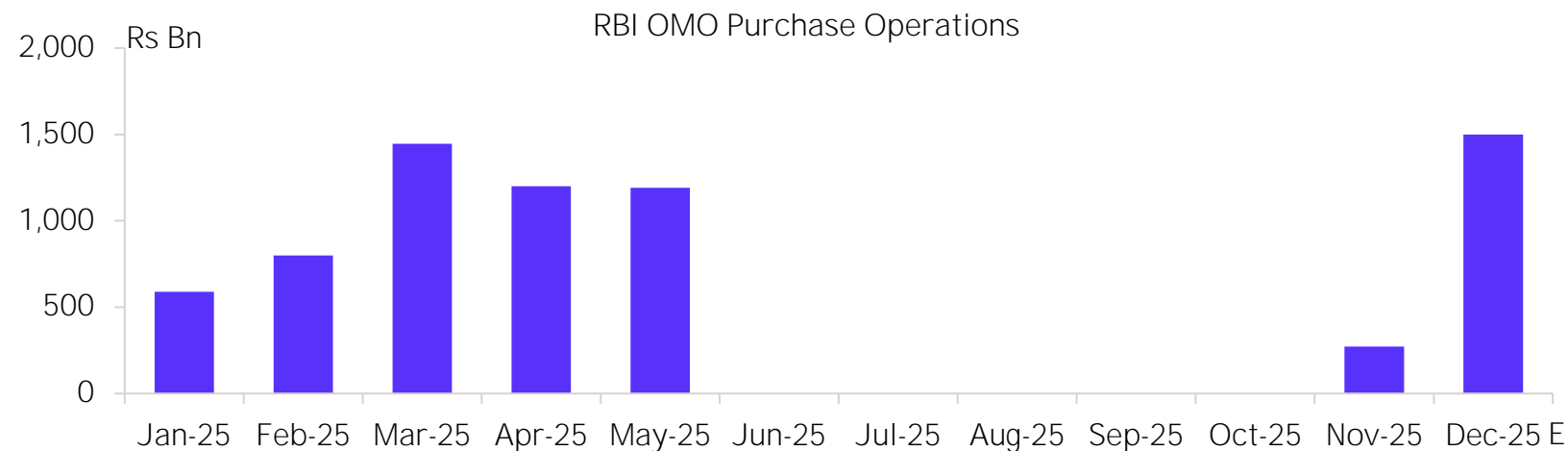
# We expect the RBI to maintain banking liquidity in sufficient surplus

The RBI may announce additional OMO purchases or FX swaps to infuse liquidity if conditions tighten



The RBI announced the infusion of Rs. 1.45 trillion of liquidity into the banking system in the December policy through Open Market Operations (OMOs) and FX swaps

The RBI is expected to maintain banking system liquidity in a sufficiently large surplus (likely above 1% of NDTL) to support credit growth



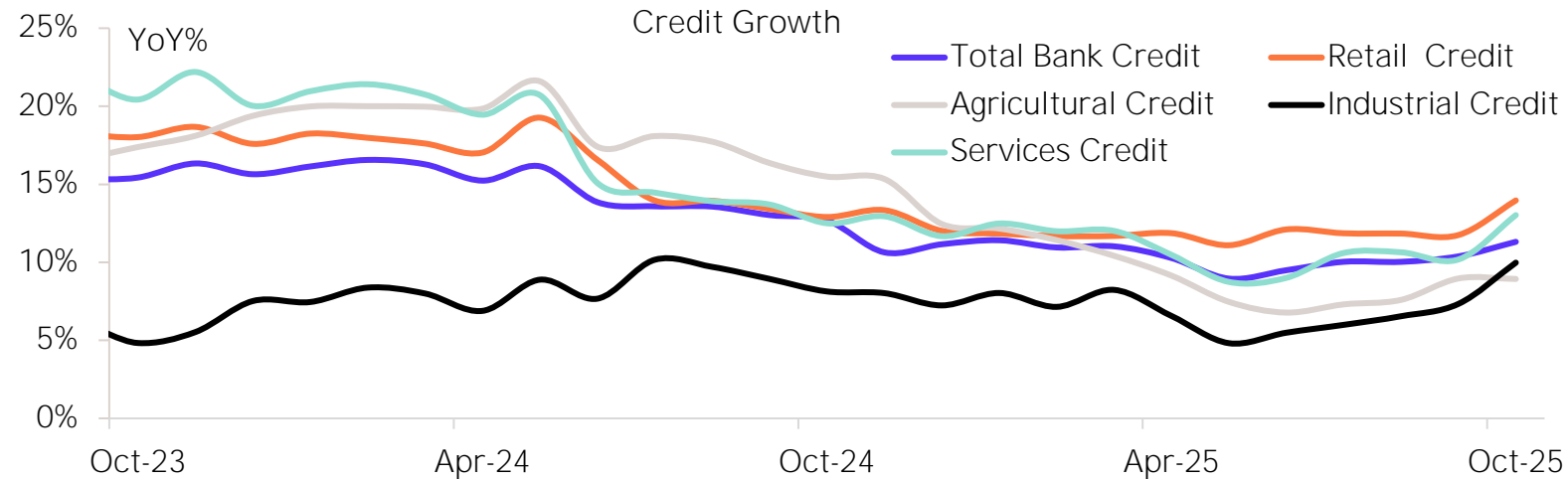
The RBI may announce additional OMO purchase auctions if the liquidity conditions tighten

While OMOs would be marginally supportive of G-sec yields, we do not foresee any significant downward move, as the economy is at the tail end of the rate-cut cycle (discussed later)



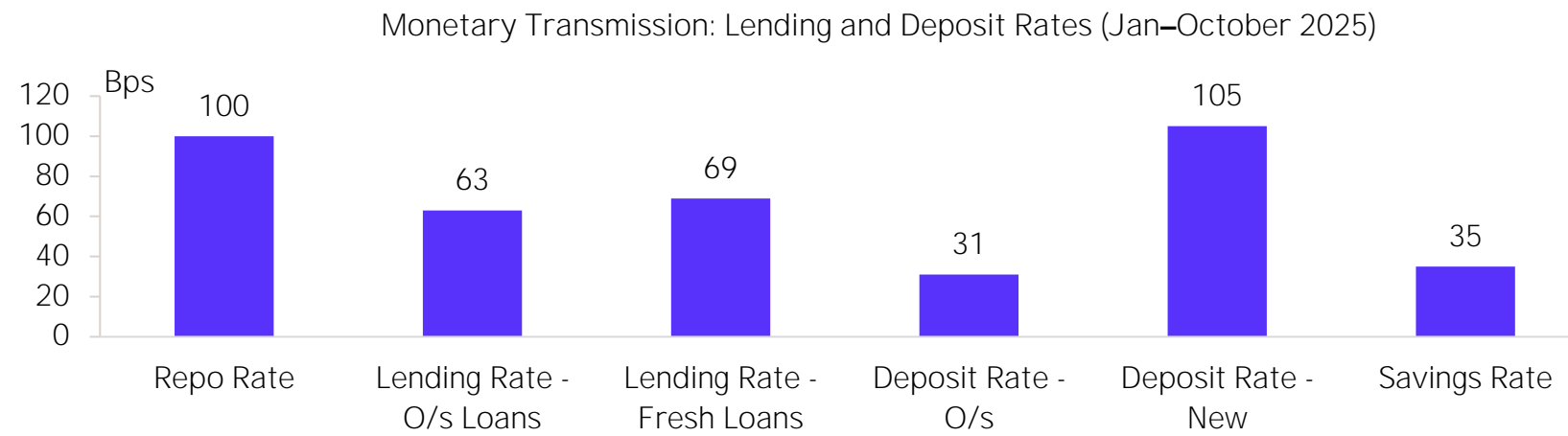
# Credit growth has picked up following regulatory and monetary easing

Transmission to lending and deposit rates has been swift so far, but further pass-through is expected to be gradual



Credit growth has bottomed out, with a broad-based recovery visible across sectors

There is scope for further pick-up in credit growth, supported by RBI regulatory easing, rate cuts, ample liquidity, and a healthy demand environment



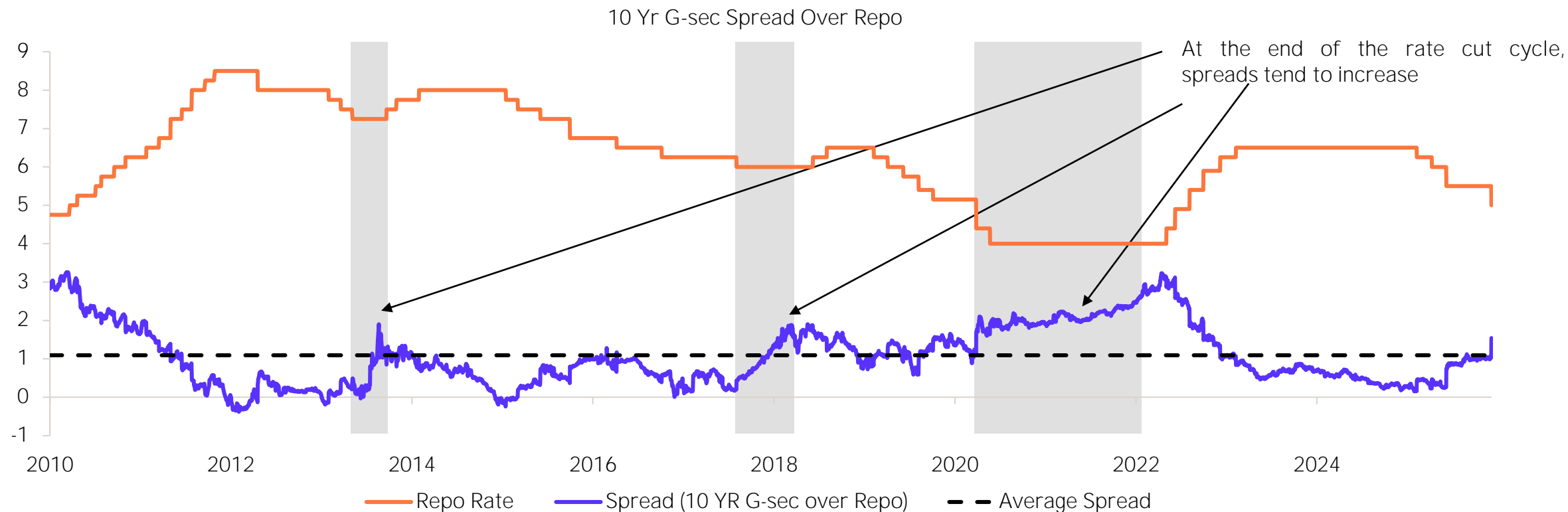
Transmission to lending rates has been swift, with 63% of floating-rate loans now linked to the External Benchmark Lending Rate, which resets quarterly

Similarly, transmission to new deposit rates has been rapid, aided by surplus liquidity conditions

However, further pass-through to lending and deposit rates is expected to be gradual, driven by a decline in MCLR rates and the maturity of existing deposits

# Long-term yields are expected to remain elevated

Rate cuts tend to have a limited impact on long-term yields as spreads widen toward the end of the easing cycle



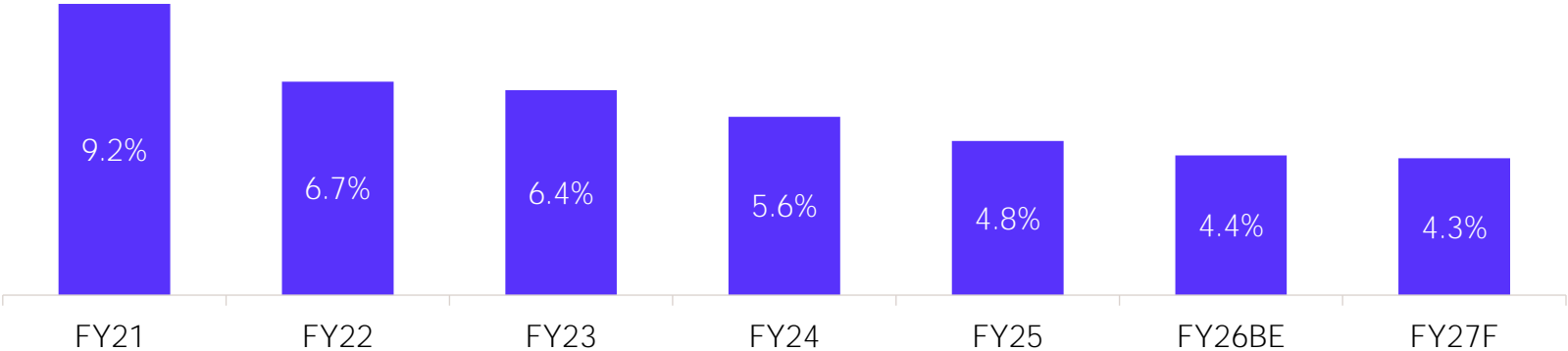
An additional 25 bps rate cut - if it materialises - is likely to have minimal impact on longer-dated bonds, as spreads would widen with no further cuts priced in, and the long end of the curve would be more influenced by heavy supply



# Gross g-sec supply likely to be heavy with limited fiscal consolidation

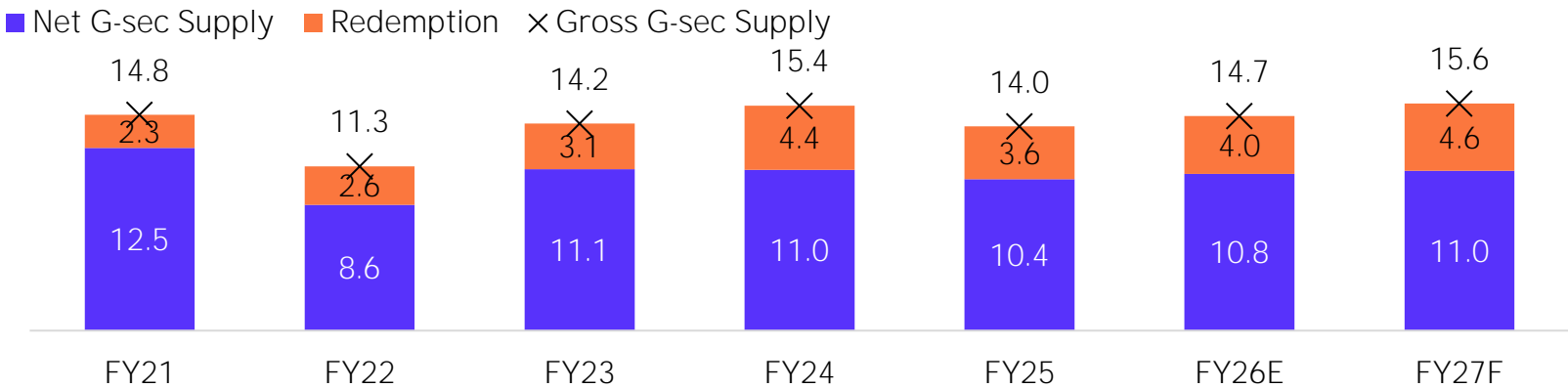
Heavy G-sec supply likely to exert upward pressure on yields

Fiscal Deficit (% of GDP)



The pace of fiscal consolidation has moderated, from 80 bps in FY25 to 40 bps in FY26, and is now expected to narrow further to just 10 bps in FY27

G-sec Supply (Rs Tn)



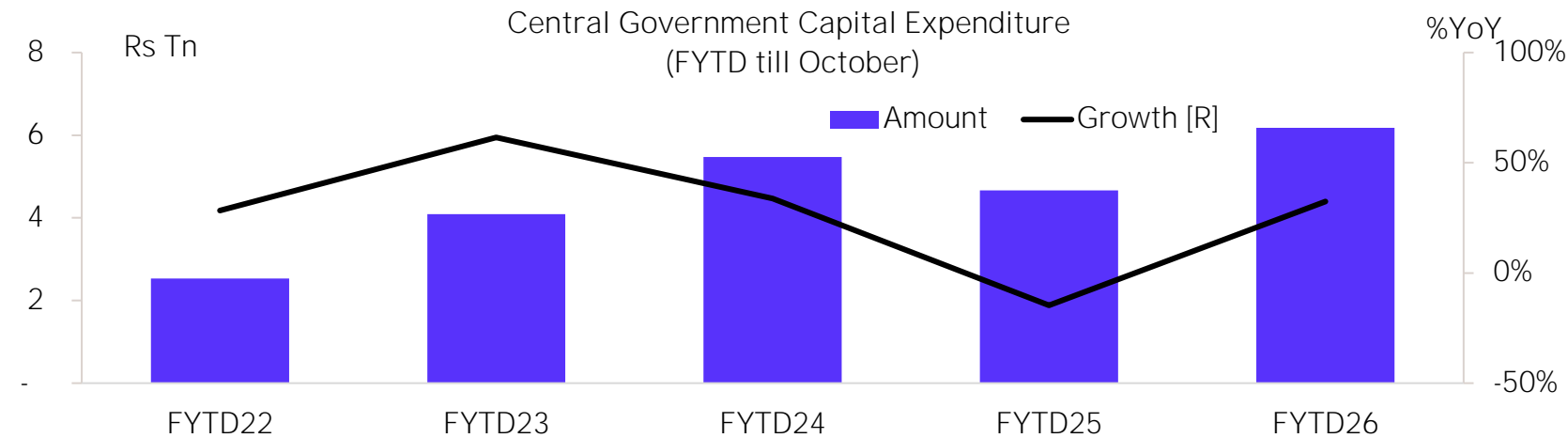
Heavy redemptions and limited fiscal consolidation could lead to higher gross supply in FY27, likely exerting upward pressure on yields

# Capex Outlook

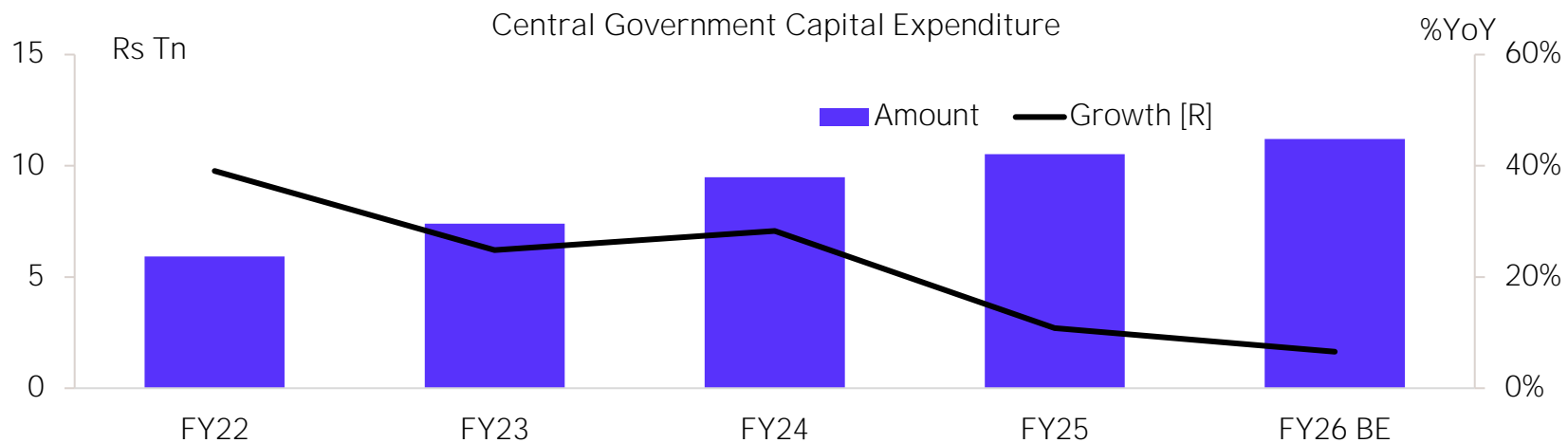


# Central government capex expected to slow down

Weak receipts and continued fiscal consolidation are likely to keep capex muted



The Central Government's capex has witnessed a strong growth of 32% YoY in FYTD October 2025



However, the government has budgeted for a 7% YoY growth in FY26

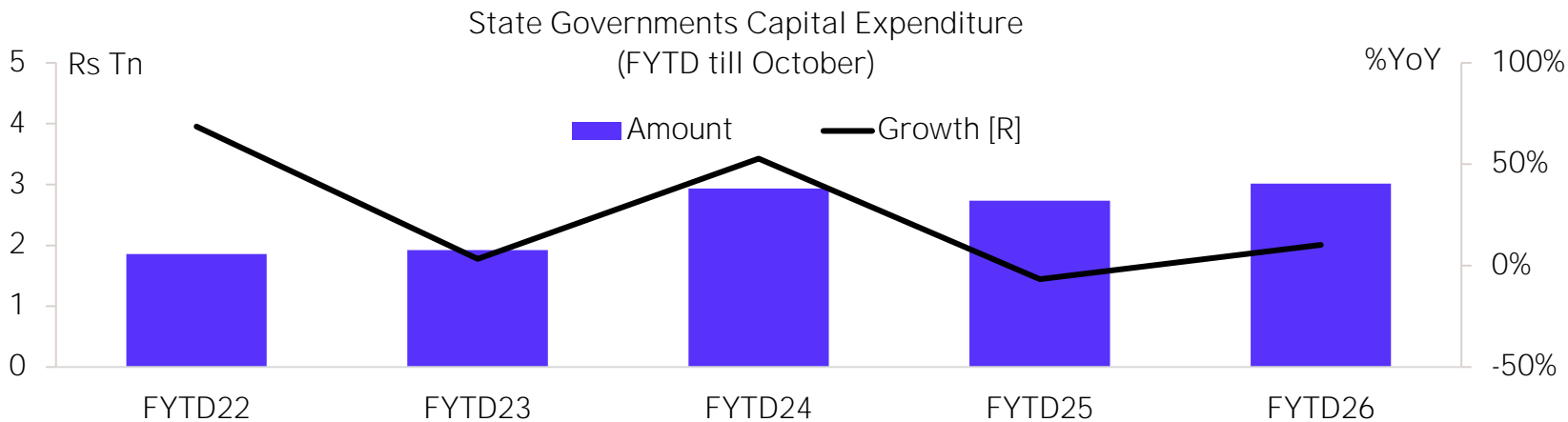
There is limited scope for the government to exceed the budgeted target, given the weak growth in receipts

Consequently, capital expenditure could contract by 14% YoY for the remainder of the financial year

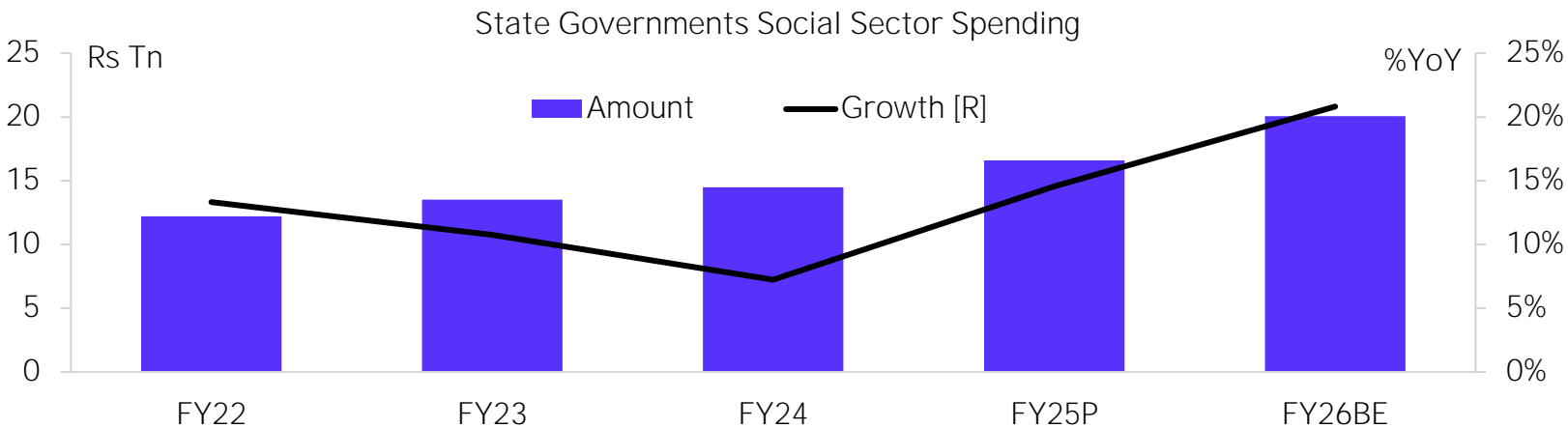
Capex growth in FY27 may also remain muted, given the expected fiscal consolidation

# Higher welfare spending is likely to cap states' capex growth

States have little room to expand fiscal space for capital expenditure due to strict fiscal deficit norms



States' capital expenditure has expanded by a decent 10% YoY in FYTD till October 2026



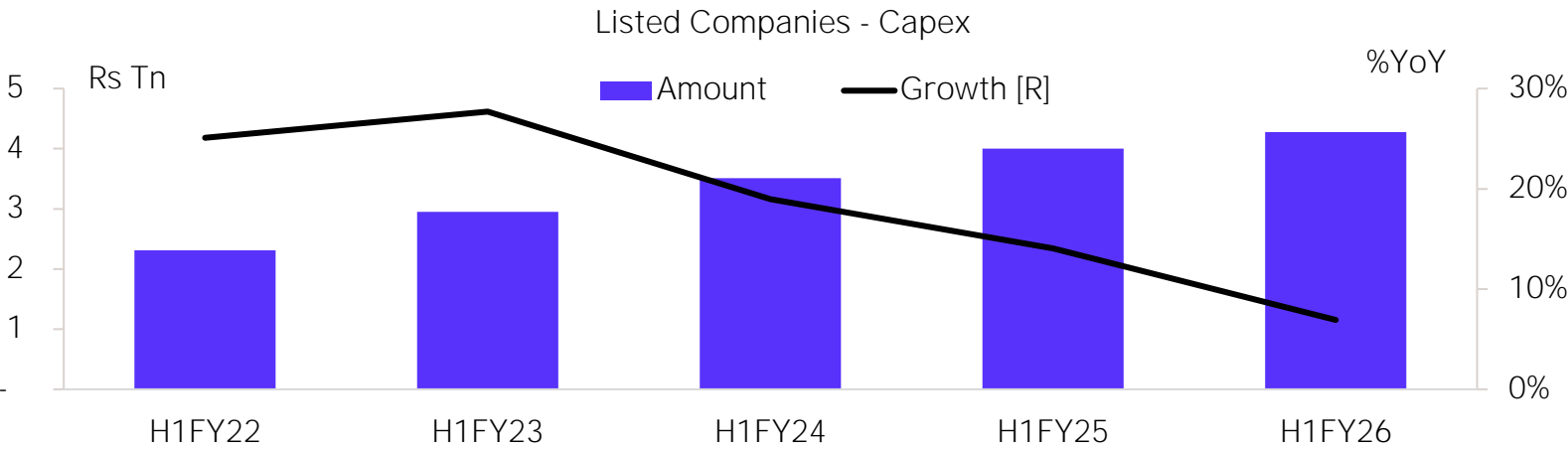
However, states' social sector spending is expected to increase by a steep 21% YoY in FY26

The rapid expansion in social and welfare spending is limiting state governments' capacity to allocate resources toward capital expenditure

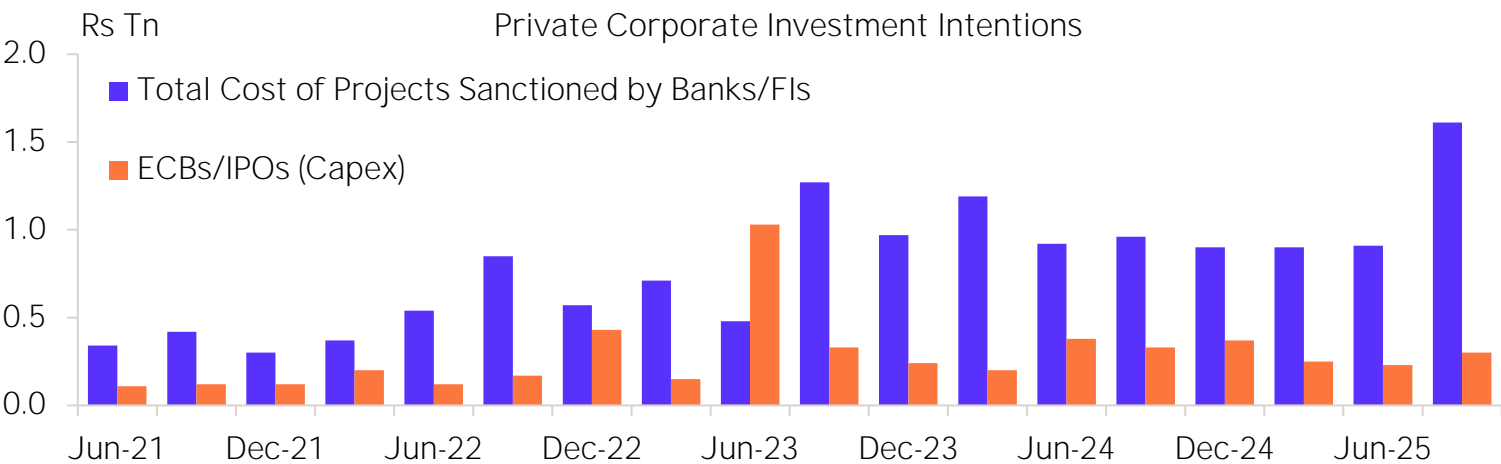
Stringent fiscal-deficit norms restrict states' ability to create additional fiscal space for higher capex

# Private sector capex has been muted in H1FY26

However, the investment pipeline remains strong, as reflected in the sharp increase in bank-sanctioned projects



Capital expenditure by listed firms, a proxy for private-sector capex, has decelerated to single-digit growth after multiple years of double-digit increases

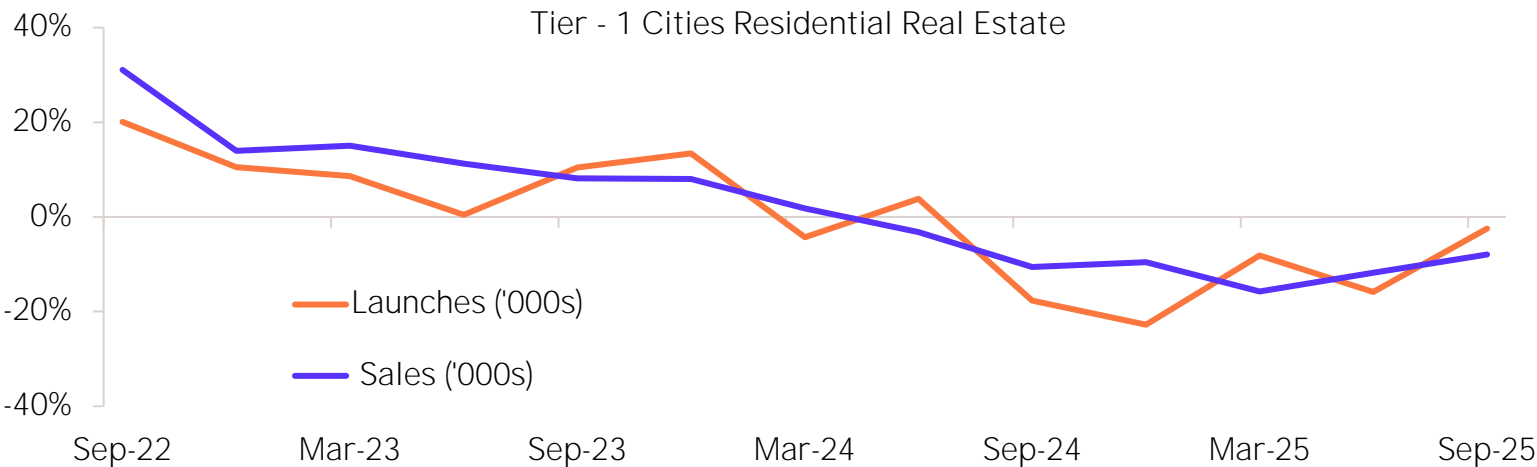


A sharp rise in bank-sanctioned projects indicates that the investment pipeline remains strong

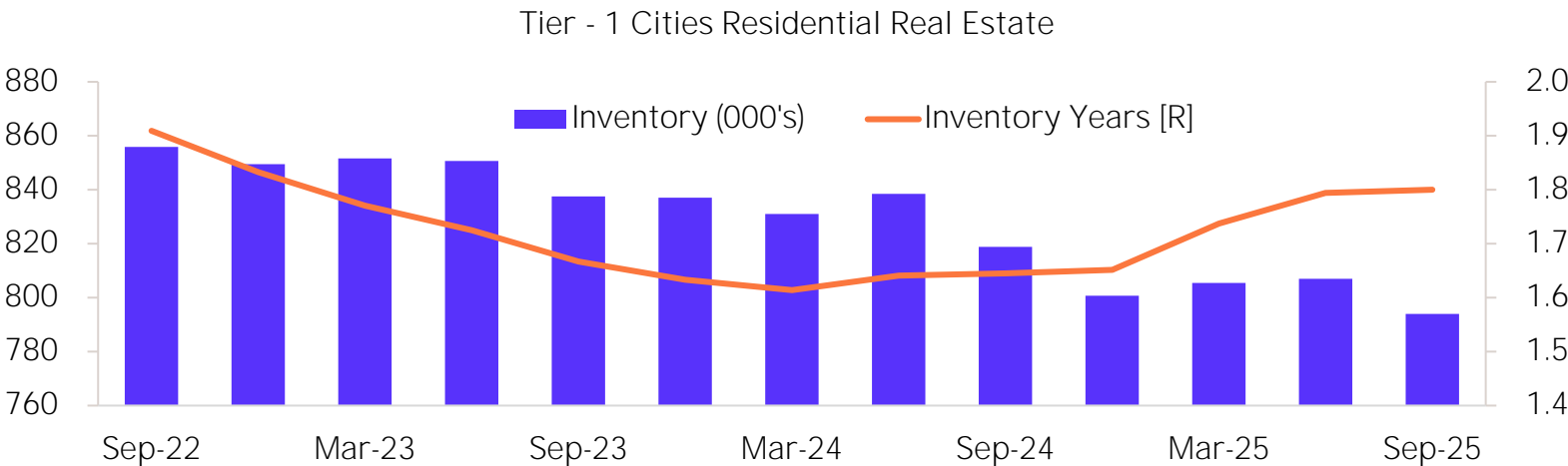
However, a sustained recovery in consumption may need to precede a broad-based rebound in private capex

# Weak home sales point to a slowdown in household capex

Residential inventory years have started inching up as sales have slowed down



A year-long contraction in residential sales and launches suggests persistent weakness in household capital expenditure

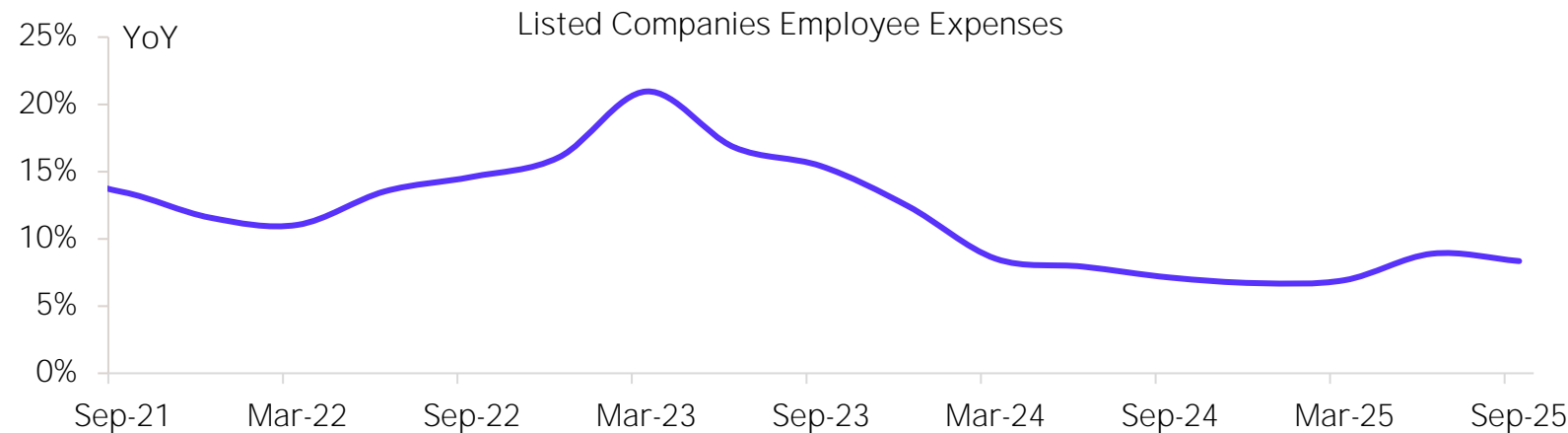


Even though residential inventory remains low, the slowdown in sales has led to an increase in inventory years - the number of years it would take to sell the existing stock of unsold residential homes



# Weak employment is likely to be a structural drag on residential sales

Hiring has also shifted toward more contractual employment rather than permanent positions



Employee expense growth has remained below 10% since March 2024

The weak growth reflects both subdued hiring activity and muted salary increments

In '000	Employees			Incremental Employees		Growth (% YoY)	
	FY23	FY24	FY25	FY24	FY25	FY24	FY25
Permanent Employees	8,101	8,346	8,494	245	148	3.0%	1.8%
Contractual Employees	3,448	4,100	4,535	652	435	18.9%	10.6%
Total Employees	11,550	12,446	13,029	896	583	7.8%	4.7%

The hiring mix has been shifting from permanent to contractual employment

Housing demand depends heavily on steady employment, permanent jobs, and wage growth

Hence, weak employment conditions are likely to remain a drag on household investment

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