FINANCIAL MARKETS & BANKING UPDATE VOL. 4: FY2025-FY2026

Bank credit growth picked up sharply, while high bond yields limited the rise in bond issuances in Q3 FY2026; trend remains monitorable in Q4 FY2026

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Abbreviations

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AUM: Assets under management	FY: Financial year	NBFC: Non-banking financial company
AIFI: All India Financial Instituitions	G-Sec: Government securities	NSDL: National Securities Depository Limited
CASA: Current account and savings account	GDP: Gross domestic product	NSO: National Statistical Office
CAD: Current account deficit	GFCE: Government final consumption expenditure	OMO: Open Market Operations
CD: Certificates of deposit	GFCF: Gross fixed capital consumption	PFCE: Private final consumption expenditure
CDSL: Central Depository Services (India) Limited	GoI: Government of India	PSB: Public sector bank
CEA: Central Electricity Authority	GST: Goods and Services Tax	PVB: Private sector bank
CIC: Currency in circulation	GVA: Gross value added	QoQ: Quarter on quarter
CP: Commercial paper	HFC: Housing finance company	RBI: Reserve Bank of India
CPI: Consumer Price Index	IDBI: IDBI Bank Limited	RDB: Rupee denominated borrowings
CMB: Cash management bills	IIP: Index of Industrial Production	SIAM: Society of Indian Automobile Manufacturers
CRR: Cash reserve ratio	IPO: Initial public offer	SIDBI: Small Industries Development Bank of India
CWP: Currency with public	IMD: India Meteorological Department	SCB: Scheduled commercial bank
CY: Calendar year	INR: Indian rupee	SDL: State development loans
DII: Domestic institutional investors	JV: Joint venture	SLR: Statutory liquidity ratio
DIPP: Department of Industrial Policy and Promotion	LAF: Liquidity Adjustment Facility	TLTRO: Targeted long-term repo operations
ECBs: External commercial borrowings	LIBOR: London Interbank Offered Rate	T-Bill: Treasury bill
EM: Emerging markets	LPA: Long period average	TTM: Trailing 12 months
FAR: Fully Accessible Route	LRS: Remittance Scheme	UAE: United Arab Emirates
FCCBs: Foreign currency convertible bonds	LTRO: Long-term repo operations	$: United States dollar
FCI: Food Corporation of India	MSME: Micro, small and medium enterprises	VRR: Variable Rate Repo
FDI: Foreign direct investment	MPC: Monetary Policy Committee	VRRR: Variable Rate Reverse Repo
FII: Foreign institutional investment	MSCI: Morgan Stanley Capital International	WoS: Wholly-owned subsidiary
FPI: Foreign portfolio investment	MSF: Marginal Standing Facility	WPI: Wholesale Price Index
FPO: Follow-on public offer	NABARD: National Bank for Agriculture & Rural Development	WACR: Weighted average call rates
FSB: Fully serviced bonds	NDTL: Net demand & time liabilities	YTD: Year to date

Agenda

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Highlights – I

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The 10-year G-Sec yield is likely to trend at 6.5-6.7% until the presentation of the Union Budget for FY2027.

FPIs remained net sellers in Q3 FY2026, albeit withdrawing a marginal $0.1 billion; the equity segment continued to record outflows amounting to $1.3 billion, while FPI inflows in the debt segment eased to $0.9 billion.

- **India's yield curve remained steep in Q3 FY2026:** The 10-year G-Sec yields were range-bound during October and November 2025, despite expectation of a potential rate cut in the ongoing quarter and US Fed's second rate cut. However, yields firmed up marginally in December 2025 driven by tight liquidity, rising US Treasury yields and global trade uncertainties. Nonetheless, the level of the 10-year G-sec yield remained broadly similar to March 2025 (6.58% as on March 31, 2025). The 91-day T-Bill softened in Q3 FY2026, declining to 5.26% as on December 31, 2025 from 5.47% as on September 30, 2025, and 5.41% as on June 30, 2025 (6.37% as on March 31, 2025). Although the banking system liquidity tightened in December 2025 owing to advance tax outflows and significant credit expansion, the RBI actively supported liquidity through OMO and FX swaps. ICRA expects the 10Y G-Sec yield to be guided by liquidity trends in the banking system as well as GoI's fiscal math and borrowing numbers for FY2027, and any news around the Bloomberg bond index inclusion. We expect it to trade at 6.6-6.75% until the presentation of the FY2027 Union Budget.
- **Bond issuances rose slightly in Q3 FY2026:** Bond issuances rose to Rs. 2.9 trillion in Q3 FY2026 from Rs. 2.7 trillion in Q2 FY2026, though they remained below the earlier quarterly high of Rs. 3.6 trillion in Q1 FY2026. Bond yields remained elevated throughout Q3 FY2026, while banks offered competitive rates, thereby leading to a demand shift from bonds to banks. Nevertheless, healthy pick up in economic activity in Q3 FY2026 driven by GST rationalisation and festive demand led to some uptick in bond issuances as well. Of the total issuance in Q3 FY2026, the share of NBFCs, corporates and banks (including AIFIs) stood at 41%, 42% and 18%, respectively, over 46%, 31% and 23%, respectively, in Q3 FY2025. Looking ahead, bond issuances are likely to be driven by NBFCs as they continue to tap capital markets to meet credit growth, while banks are also likely to increase some bond borrowings if the deposit growth continues to lag credit growth.
- **Net FPI outflows eased to $0.1 billion in Q3 FY2026:** India saw net FPI outflows (equity, debt and hybrid) of $0.1 billion in Q3 FY2026, albeit lower than that in Q2 FY2026 (-$4.5 billion). FPIs sold $1.3 billion from the equity market in Q3 FY2026 (-$8.7 billion in Q2), as the macroeconomic outlook remained uncertain after the imposition of US tariffs and penalties, leading to a slide in the USD/INR pair. In addition, net inflows in the debt segment eased to $0.9 billion in Q3 FY2026 from $4.2 billion in Q2, even as G-Sec spreads narrowed, particularly vis-à-vis the 10Y US treasury, UK and German bonds, along with sustained global uncertainty.

Highlights – II

Net FDI inflows increased to $5.6 billion in 8M FY2026 due to some big-ticket transactions for equity inflows in H1 FY2026 and slight decline in repatriation/divestment from India.

LRS remittances trended lower at $19.1 billion in 8M FY20206 over $20.0 billion in 8M FY2025, affected by the rupee depreciation and changes in taxation in the past fiscal.

Gross ECB approvals moderated in 8M FY2026 over 8M FY2025. This trend is expected to continue in rest of FY2026.

India's GDP growth is estimated to moderate in Q3 FY2026 from 8.2% in Q2 on an adverse base; nevertheless, the growth forecast for FY2026 is retained at a strong 7.4%, aided by sizeable monetary stimulus, direct and indirect tax cuts, and low inflation.

- **Net FDI inflows (including reinvested earnings) stay positive till YTD FY2026:** Net FDI inflows were positive at $5.6 billion during 8M FY2026 owing to some big-ticket transactions in H1 FY2026 driving up the equity inflows to India. Moreover, the repatriations and disinvestments from India declined marginally in 8M FY2026 after witnessing the record level in previous fiscal. The investment activity has been robust for India in 8M FY2026 with recent investment announcements by big tech giants for medium term, while the recently executed trade deals and many underway, provide an avenue for investment inflows over the long run. Nevertheless, the trade and tariff related concerns and geopolitical tension cast a shadow on how the trends culminate in the later end of the FY2026.
- **LRS outflows in FY2026 to likely settle below that in FY2025:** Total outflows under LRS rose to $7.9 billion in Q2 FY2026 from $6.9 billion in Q1 FY2026, while remaining 9% lower YoY compared to $8.7 billion in Q2 FY2025. The LRS remittances remained affected by adverse INR movement. Given the trend so far, the LRS remittances in FY2026 are likely to settle lower than FY2025 tally.
- **ICRA revises down estimate of ECB approvals in FY2026:** Gross ECB approvals moderated to $23.1 billion in 8M FY2026 from $33.8 billion during the corresponding period last year (net of refinancing, $18.7 billion in 8M FY2026 compared to $29.2 billion in corresponding period last year). With favourable borrowing rates from domestic lenders, the pace of ECB approvals and issuances is likely to dip in FY2026. Accordingly, ICRA has lowered its estimate for the gross ECB approvals to $40-45 billion in FY2026 from its earlier estimate of $50-55 billion in FY2026, trailing the record high $61.2 billion in FY2025.
- **India's GDP growth likely to have eased in Q3 FY2026**: India's GDP growth is expected to have eased in Q3 FY2026 from the elevated 8.2% in Q2 FY2026, while remaining healthy, given the slowdown in merchandise export growth, contraction in the GoI's capex, and an adverse base, even as domestic consumption is likely to have fared well aided by the GST rate cuts across a large set of items, which coincided with the festive season. Despite the tariff-related issues, ICRA expects the GDP growth to print at a strong 7.4% in FY2026, aided by sizeable monetary stimulus and liquidity support, direct and indirect tax cuts, and subdued inflation.

Highlights – III

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CPI inflation receded significantly to a series-low of 0.8% in Q3 FY2026, owing to sharper deflation in the F&B segment.

MPC likely to pause easing cycle in February 2026 to assess base year revision impact on growth-inflation mix.

Size of systemic liquidity surplus moderated in Q3 FY2026, amid increase in seasonal currency lekages, advance tax outflows, and forex intervention by the RBI.

- **CPI inflation cooled to a series-low of 0.8% in Q3 FY2026:** The headline CPI inflation eased from 1.7% in Q2 FY2026 to 0.8% in Q3 FY2026. This was mainly led by the food and beverage (F&B) segment (to a series low -2.8% in Q3 from -0.7% in Q2), followed by softer inflation prints for clothing and footwear, housing, and fuel and light, while miscellaneous items, and paan, tobacco and intoxicants saw an uptick during this period. With an expected turnaround in the F&B segment to an inflation in January 2026, we project the headline CPI inflation to cross the 2.0%-mark in the month. However, the December 2025 reading was the last print as per the current series (base year: CY2012) and the January 2026 print (to be released by mid-February), will be as per the new CPI series (base year: 2024); this would feed into our revised expectations for FY2026 as well as the upcoming fiscal.
- **ICRA expects a pause in February 2026 policy review:** While the December 2025 MPC minutes suggest a possibility of another rate cut in February 2026, ICRA believes that a pause is warranted at the current juncture to assess the upcoming CPI (for January 2026 on February 12; base: 2024) and GDP (FY2024-FY2026 on February 27; base: 2022-23) data as per the new base, which are due to be released at mid/end-February 2026. These data series will determine the current growth-inflation mix, and aid in forming a fresh outlook.
- **Liquidity pressure in Q4 to be partly offset by durable liquidity injection measures:** The monthly average size of the systemic liquidity surplus moderated to Rs. 1.1 trillion (+0.5% of NDTL) in Q3 FY2026 from Rs. 2.5 trillion (+1.0% of NDTL) in Q2 FY2026, owing to advance tax outflows, increase in seasonal currency leakages, as well as the RBI’s forex market intervention. Notably, the banking systemic liquidity temporarily transited into deficit during December 16-31, 2025, with a daily average deficit of Rs. 0.5 trillion, over the average surplus of Rs. 2.0 trillion of the first 15 days of the month. On the other hand, the durable liquidity surplus remains quite sizeable, although the extent of the same moderated to Rs. 3.4 trillion (1.4% of NDTL) as on December 31, 2025 from Rs. 5.2 trillion (2.2% of NDTL) as on September 19, 2025, despite CRR rate cuts, OMO purchases, and forex swaps. After injecting Rs. 2.4 trillion via OMOs and swap auction in January 2026 so far, the RBI has recently decided to conduct another buy/sell swap ($10 billion), long tenure VRR (Rs. 250 billion) and OMO purchases (Rs. 1.0 trillion) over the next few weeks, which are set to infuse liquidity of Rs. 2.2 trillion. These measures would partly offset the pressure of higher seasonal demand for cash in Q4, while also supporting monetary transmission.

Highlights – IV

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ICRA had projected deposit accretion at Rs. 23.8-25.5 trillion (10.5-11.3% growth) in FY2026. However, the recent reporting date change by the RBI will lead to higher reported deposit growth on year end.

ICRA's credit growth estimate of Rs. 19.0–20.5 trillion (10.4-11.3% YoY growth) for FY2026 is likely to hold on a like-to-like comparison of data (year-end FY2026 vs. year-end FY2025), though the credit growth rate on a reporting date basis is expected to be higher than ICRA's estimates.

- **Deposit growth inched up by end of Q3 FY2026*:** Deposit growth remained tepid and lagged the credit growth in most of Q3 FY2026; however, towards the end, YoY growth rate improved to 12.7% as on December 31, 2025 compared to 10.2% as on November 28, 2025. The incremental deposits accretion stood at Rs. 7.6 trillion in Q3 FY2026 (Rs. 6.7 trillion in Q2 FY2026, Rs. 1.4 trillion in Q3 FY2025). However, this is not directly comparable to the same period last year given the change in reporting dates to the 15th and end of every month from the earlier practice of alternate Fridays. The deposits outstanding of the banking system rose to Rs. 248.6 trillion (+12.7% YoY growth) as on December 31, 2025 from Rs. 220.6 trillion as on December 27, 2024 (+9.9% YoY growth). CD outstanding stood at Rs. 5.7 trillion as on December 31, 2025 (Rs. 5.0 trillion as on October 03, 2025, Rs. 4.9 trillion as on December 27, 2024). The CDs as a percentage of total deposits rose to 2.3% as on December 31, 2025, from 2.1% as on October 3, 2025 and 2.2% as on December 31, 2024; however, it was lower than 2.4% as on March 21, 2025. ICRA had projected deposit accretion at Rs. 23.8-25.5 trillion (10.5-11.3% growth) in FY2026 with outstanding deposit at Rs. 249.6-251.3 trillion by March 2026. However, the recent reporting date change by RBI will lead to higher reported deposit growth. The year-end figures are likely to differ from ICRA's estimates, though on a like-to-like basis (comparing with end-FY2025), the projections would hold.
- **Credit accretion picked up sharply in Q3 FY2026 :** Incremental non-food bank credit (NFBC) expansion stood at Rs. 10.1 trillion in Q3 FY2026 higher than Rs. 8.0 trillion in Q2 FY2026 (Rs. 4.6 trillion in Q3 FY2025). This was driven by banks' better competitive positioning given the sticky bond yields, growth in economic activity after the GST cut on September 22, 2025 spurring the demand for channel financing and growth in retail loans. In addition, the reporting date change to end of the month led to higher credit offtake towards the end of Q3 FY2026, with November 28, 2025 - December 31, 2025 period accounting for ~78% of incremental credit growth of Q3 FY2026. Consequently, the incremental credit growth in 9M FY2026 was healthy at Rs. 20.3 trillion compared to Rs. 11.6 trillion in 9M FY2025 (Rs. 18.0 trillion in FY2025). ICRA expects the credit demand to remain buoyant with retail and MSME being the primary growth drivers and the relief measures announced for tariff-hit sectors acting as stabilising factors. ICRA's credit growth estimate of Rs. 19.0–20.5 trillion (10.4-11.3% YoY) for FY2026 is likely to hold on a like-to-like comparison of data (year-end FY2026 vs. year-end FY2025), though on reporting date basis credit growth rate is expected to be higher than ICRA's estimates.

*Note: *Data for Q3 FY2026 is from October 3, 2025 to December 31, 2025; for Q2 FY2026 is from June 27, 2025 to October 3, 2025; for Q1 FY2026 is from March 21, 2025 to June 27, 2025; and for Q3 FY2025 is from October 04, 2024 to December 27, 2024*

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