

MARKET OUTLOOK

December 2025



Authored by

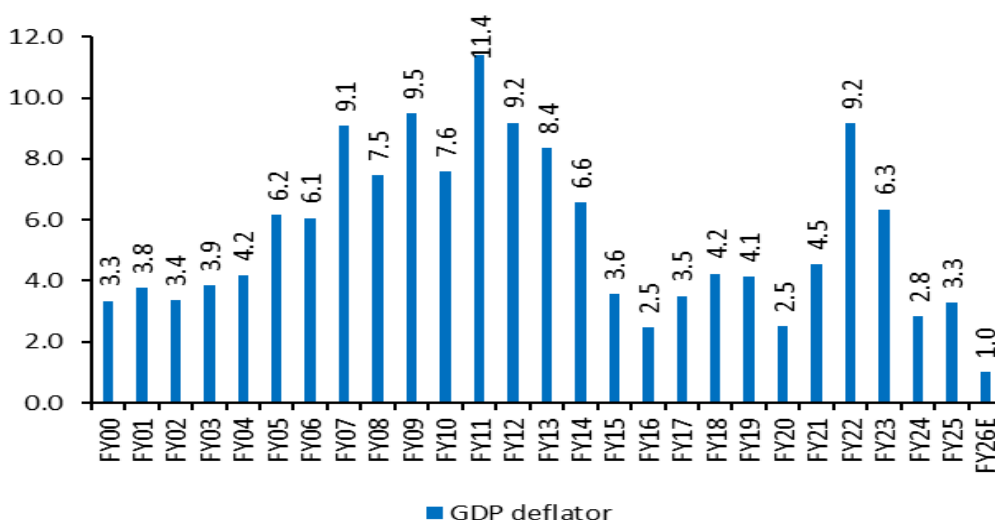


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Recent GDP data highlights the contrast between real growth, which remains materially above forecast with Q1 FY26 at 7.8%, Q2 FY26 at 8.2% and H1 nominal growth at below 8.7% y-o-y. While the transmission of policy rates, lower tax rates, potential easing of tariff pressures and regulatory easing should enable growth pick-up, near-term challenges on government revenues, corporate revenues and earnings could be evident going forward. The GDP deflator (a proxy for aggregate inflation in economy) currently at its historical low, also sits at odds with a more realistic measure of economy-wide prices.

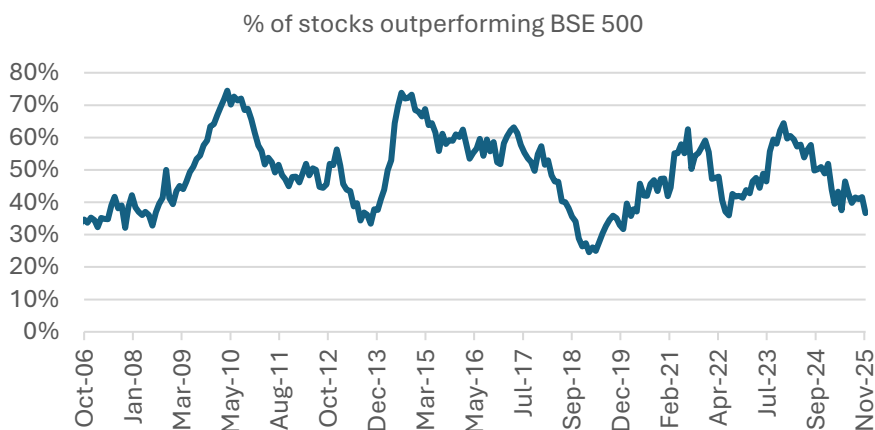


Source: Bloomberg, SBIFM Research

EQUITY

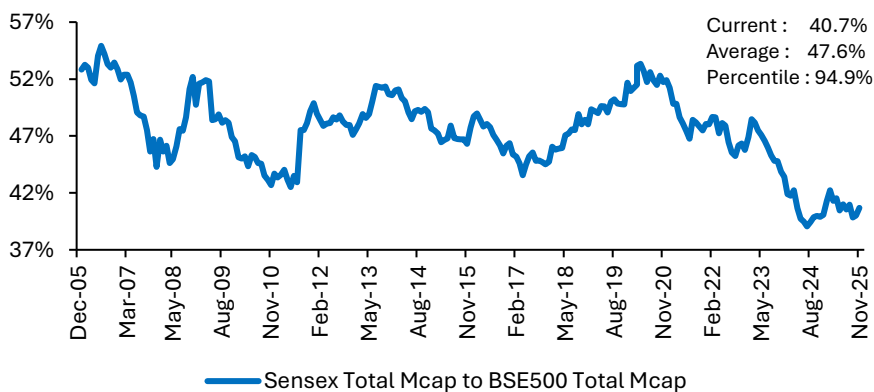
Indian equities did well for the month with the Nifty and the Sensex returning 2% and 2.2% respectively in November. The performance down the market capitalization curve was weaker with Nifty Midcap 150 and Nifty Smallcap 250 returning 1.7% and -3.3% respectively. On a YTD basis, Nifty and Sensex have returned 12.4% and 11.2% respectively as against 6.8% and -5% respectively for Nifty Midcap 150 and Nifty Smallcap 250 indices. Performance beneath the surface suggests a more pronounced deterioration in market breadth. In the BSE 500 universe, two-thirds of the stocks have underperformed the index on rolling 12-month returns. Given that large caps stay cheaper than broader markets on relative valuations, we believe polarization in equity markets may continue to increase.

Market breadth stays weak even as Nifty attempts fresh highs.



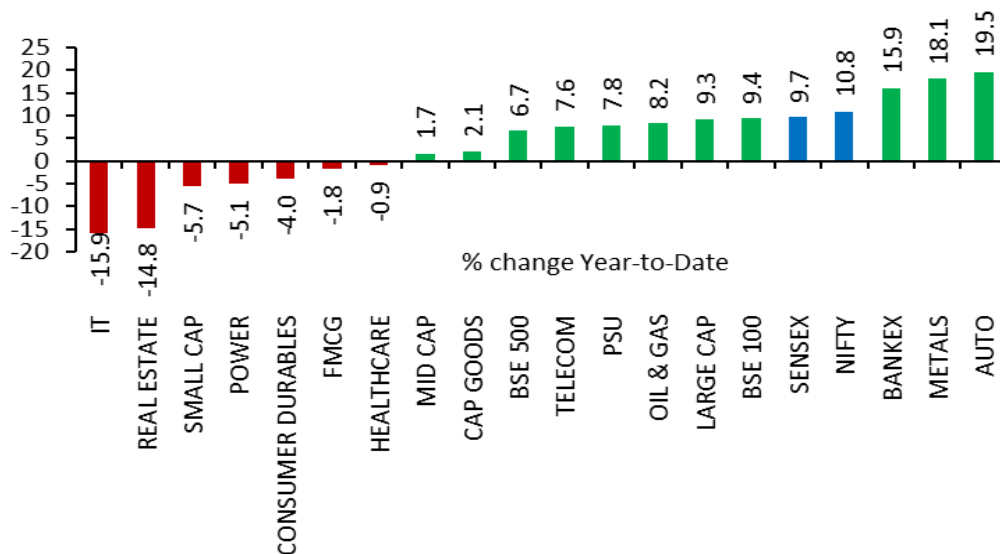
Source: FactSet, SBIFM Research

Polarization may continue to increase with large caps cheap on relative valuations.



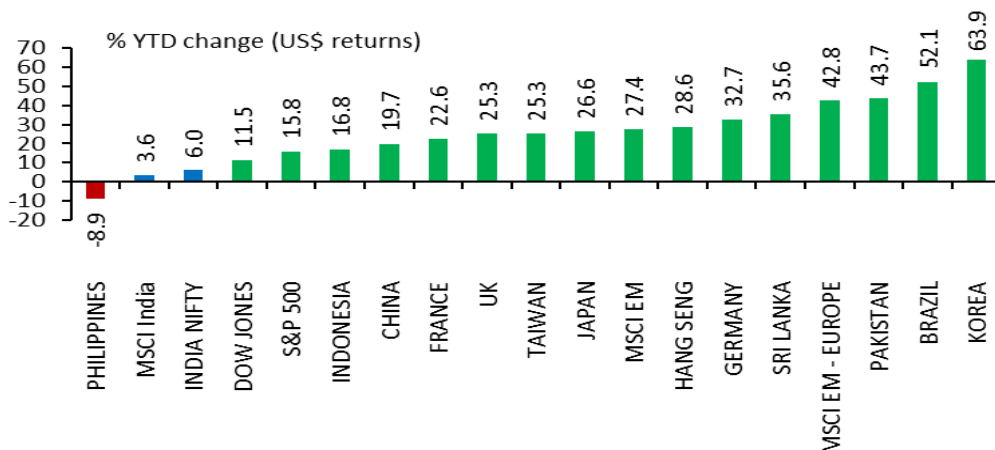
Source: Bloomberg, SBIFM Research

While Nifty has delivered double-digit gains this year, performance across sectors and market capitalizations has been mixed.



Source: Bloomberg, SBIFM Research

India has stayed an underperformer this year amidst expensive starting valuations and weak earnings.



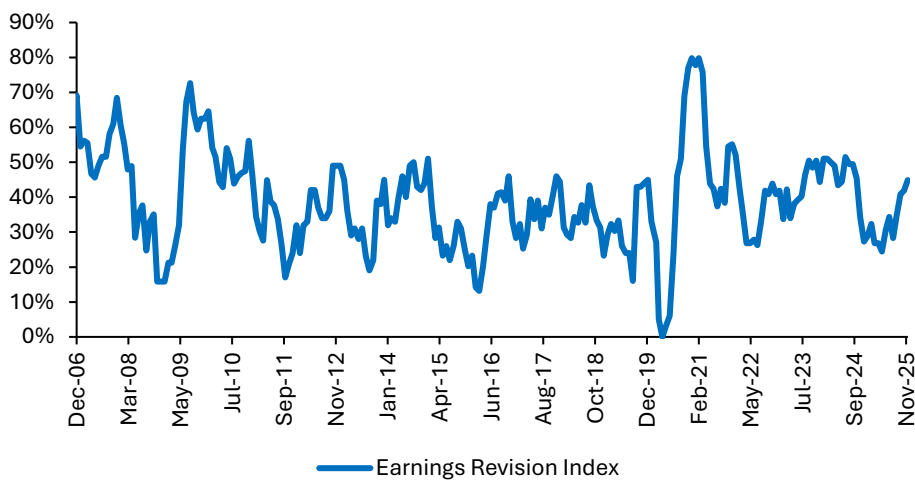
Source: Bloomberg, SBIFM Research

The recently concluded earnings season pointed to weak but in line corporate performance. Within Nifty companies, even as metals, NBFCs, capital goods, cement and telecom recorded healthy profits growth, weakness in private banks results coupled with a drag from Oil & Gas (ex OMCs), automobile, consumer, and insurance companies put pressure on profitability.

The interesting aspect is that earnings expectations have continued to improve with number of stocks being upgraded nearing the number being downgraded now versus a skew significantly in favour of downgrades over the past few months. Improving consumer sentiment on the back of Income Tax and Goods and Services Tax cuts as well as falling inflation, transmission of policy

rate cuts and government's willingness to push through structural reforms such as the recent labour codes augur well for economic and earnings outlook going forward. On the other hand, however, cyclical headwinds from trade uncertainties and the government's fiscal capacity constraints pose risks to growth. Overall, earnings and economic growth remain weak, but the worst appears to be behind, and we expect a gradual, directional improvement going forward.

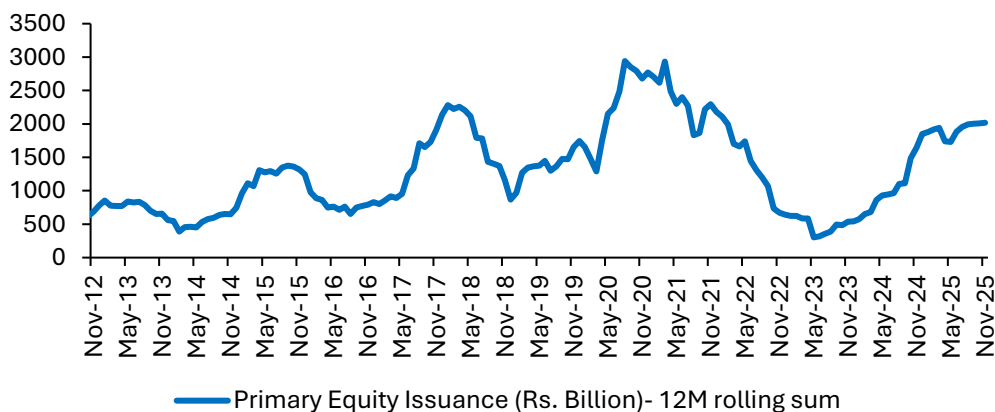
Breadth of earnings revisions have improved and now point to a balance between upgrades and downgrades.



Source: FactSet, SBIFM Research

Reflecting the expected improvement in economic and corporate fundamentals, market sentiment, as measured through our proprietary Equity Sentiment Index is improving as well. However, continued surge in equity supply through primary issuances and secondary stake sales has acted to put a ceiling on the market up move. In that context and with earnings improvement likely to be gradual, we expect market up moves to stay measured with opportunities at a micro, stock-specific level staying the focus.

Continued surge in primary market issuances have acted as lid on market up moves.



Source: FactSet, SBIFM Research

FIXED INCOME

The broader market direction over the last month was determined by RBI screen-based OMO purchases and the Governor's comments opening the possibility of a cut in the December review. Over the last few weeks, currency-related pressures have resurfaced, though the bond market reaction has been rather muted. Strong GDP prints led to market yields moving up post the data release.

Gsec	31-Oct-25	31NOV25	
3-year G Sec	5.88%	5.83%	-0.05%
5-year G Sec	6.17%	6.23%	0.06%
10-year G Sec	6.47%	6.51%	0.04%
15-year G Sec	6.84%	6.94%	0.10%
30-year G Sec	7.22%	7.31%	0.09%
slope 10x15y	0.37%	0.43%	0.06%
slope 10x30y	0.75%	0.80%	0.05%
SDL			
10-12Y	7.19%	7.20%	0.01%
SDL Spread	0.72%	0.69%	-0.03%
AAA- PFC/REC			
1Y AAA	6.51%	6.55%	0.04%
2Y AAA	6.60%	6.65%	0.05%
3Y AAA	6.70%	6.72%	0.02%
5Y AAA	6.81%	6.85%	0.04%
10Y AAA	7.11%	7.10%	-0.01%

Source: SBIFM Research

RBI Policy Review

A strong GDP print at 8.2% and worries with respect to the currency had reduced market expectations for a rate cut in the December review. However, RBI has reduced the Repo rate by 25 bps while simultaneously announcing Rs. 1.5 trillion of core liquidity infusion through OMO and FX swap for the month of December. The stance remains neutral with the central bank expressing confidence in a muted trajectory for forward inflation.

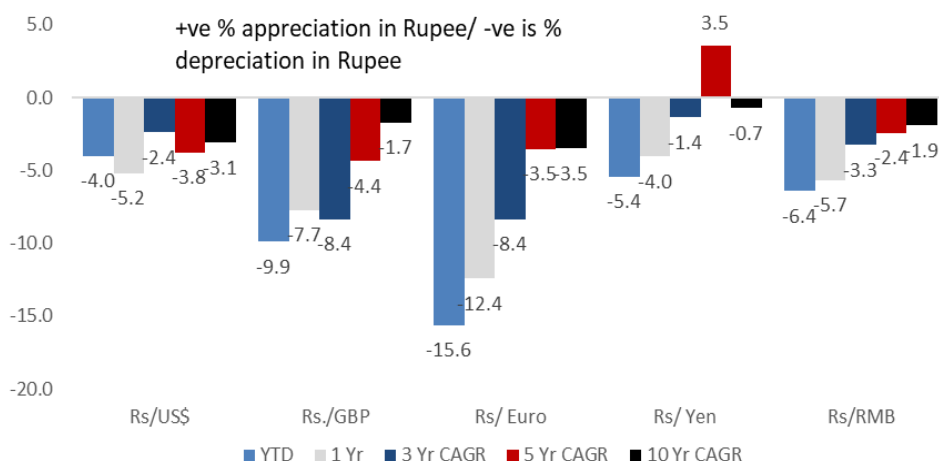
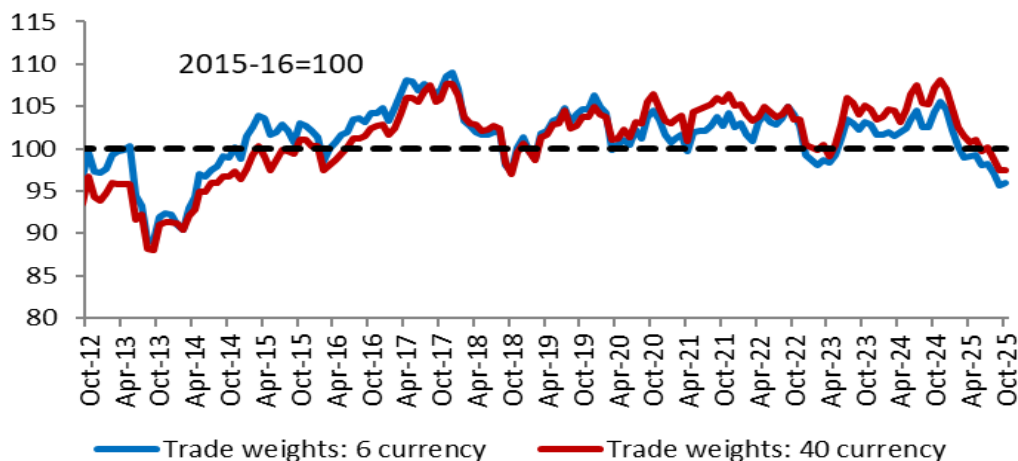
The RBI has utilized the available monetary space (with forward CPI estimates anchored around 4%) to ensure that the system receives adequate support for sustained growth. The conditions necessary for effective transmission have also been addressed through the announcement of durable liquidity measures, including OMOs and FX swaps. Going forward, while the guidance suggests some space, the focus would likely shift more toward liquidity management and policy transmission. Overall, the policy measures have appropriately responded to the domestic

growth–inflation matrix rather than being tied up with concerns over INR movements that are a logical adjustment to capital flows and tariff concerns in the short term.

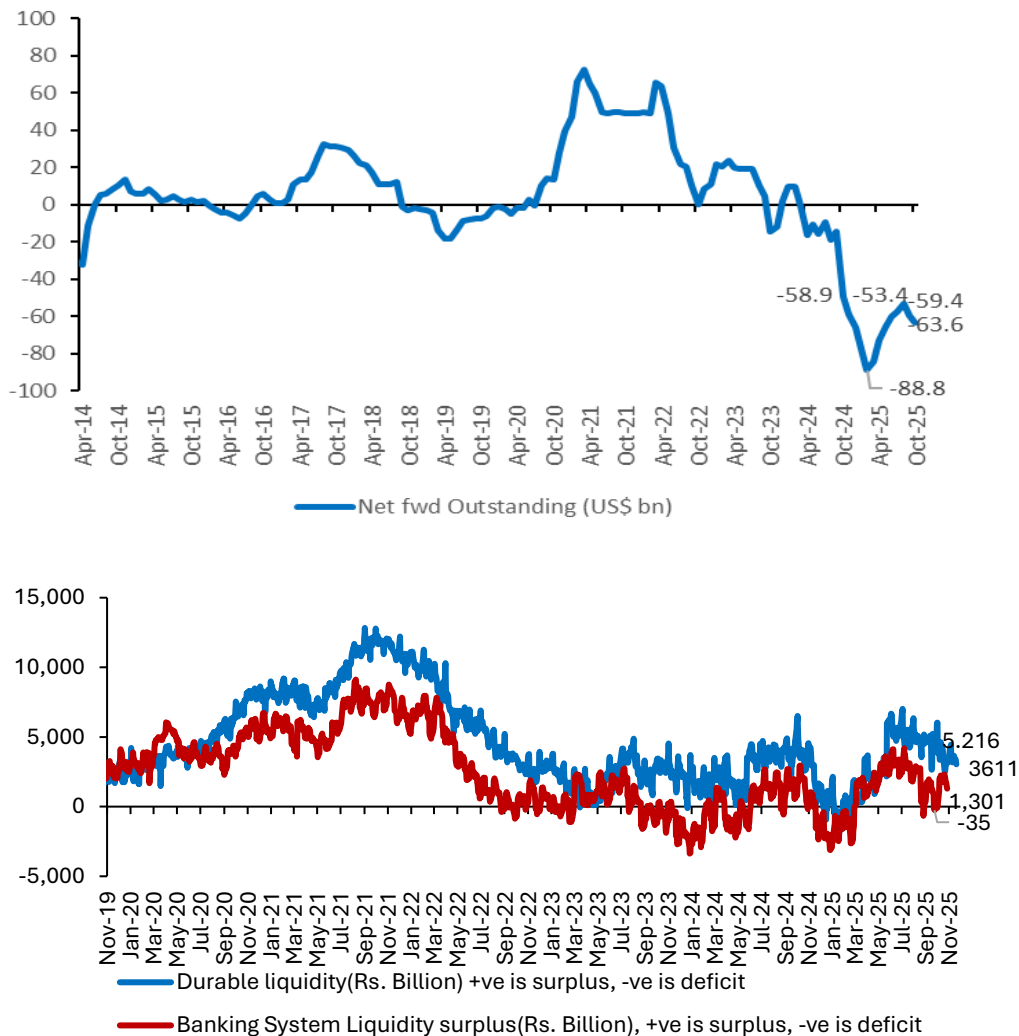
INR and Liquidity

The impact of previous liquidity infusion through CRR and OMO cuts have been largely neutralized through Forex interventions and currency leakage. The recent weakness in INR has been largely attributed to emerging worries on the trade account and delay in closing the trade deal with the US. At the same time, portfolio outflows, and muted Net FDI flows have kept the capital account under stress. Even as service sector and invisible surpluses have kept the overall Current account deficit within tolerable limits, near term market direction will be influenced by the vagaries of capital account.

Seen in the context of tariffs and trade uncertainty, a tolerance for a bit of currency weakness could also be seen as a necessary policy adjustment. Indices of REER seem to clearly suggest an overshoot with the currency being undervalued.



Liquidity dynamics have evolved with the interventions in the spot currency markets even as RBI forward book has enlarged over last few months. The outstanding short forwards have increased to around USD 64 bn based on reported October data. With core liquidity moving lower, basis estimates on incremental CIC, primary liquidity infusion measures would clearly be warranted going forward by the fiscal year end.



Source: RBI, CEIC, SBIFM Research.

Portfolio strategy

With the RBI having delivered a dovish cut, the market could possibly look forward to another cut in the February review. However, with the current set of measures alongside those taken earlier, expectations should be cautious. Monetary policy easing in the current cycle has possibly reached its end, with focus now likely to be on rates transmission. Fiscal policy support is likely to persist with the government incrementally not being bound by a numerical target on annual FD/GDP starting FY27. Apart from policy reforms, requirement of sustaining growth impulses would be best served through ensuring macro stability and adequate systemic liquidity.

The commitment to keep adequate liquidity should be seen in the context of a soft inflation outlook. This would imply that liquidity conditions do not tighten over the coming months, despite some frictional issues arising from seasonality. A turn in the cycle would be preceded by active liquidity absorption or RBI allowing the system liquidity to tighten naturally. Clearly, we are far away from such a macro context currently.

Market yields, on a forward-looking basis, are expected to remain in a tight range with no clear large directional downward momentum unless market interventions through OMOs are sustained beyond the current market expectations of around Rs. 2.0 trillion. While we continue to expect at least Rs. 2.0 trillion in OMO purchases incrementally, actual outcomes with respect to capital flows in CY26 would be an important determinant of the same. With economic growth remaining relatively better, a satisfactory resolution of tariff issue and necessary adjustment in expectations on equity market valuations and earnings improvement should help portfolio flows rotation back into India in CY26.

Overall, on a risk–reward basis, spreads on high grade bonds as well as selective credits at the shorter-end remain attractive. Given the anticipated external volatility and its likely resetting of market expectations, strategies on duration would continue to be nimble, with preference to remain relatively lighter on a directional basis. Curve steepness is expected to remain intact in the coming months. Short tenor high grade bond funds continue to provide higher accrual, wider spreads as well as an optimum risk/reward that provide opportunities over the coming months as well as into the coming year. State Development Loans are expected to have a larger net supply in Q4 FY26 and could provide a tactical opportunity with wider spreads over the last quarter.

**Mutual Fund investments are subject to market risks,
read all scheme related documents carefully.**