SBI RESEARCH

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CPI INFLATION SURPRISES ON DOWNSIDE…GLOBAL GEOPOLITICS HAS DECISIVELY SHIFTED TO GEOECONOMICS AND THIS WILL DETERMINE PRICE MOVEMENTS IN 2026, SPECIFICALLY COMMODITIES PRICES…RBI MAY HAVE TO NOW DO MORE OMOs TO KEEP BOND PRICES IN CHECK

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The November inflation data reveals that for the first time in the history of current series food inflation is in negative territory for consecutive seven months (in Aug'25 it was near to zero). Separately, the year 2025 has now unveiled the lowest level of yearly food inflation (0.4%) in the entire series (since 2012) and way below the 14-year average of 5.8%. Using a methodology similar to FRBSF Economic Letter, June 21, 2022, paper, we sliced the 299 items under CPI inflation to understand whether the drivers of inflation were demand or supply. Our analysis shows that out of 299 commodities in CPI, the drivers for 171 items could be categorised as factors that are supply driven (123 items being food), 99 as demand driven and 29 are neutral. **Our results thus show that supply side factors related to food have been one of the defining factors in ensuring that food inflation has stayed range bound for major part of 2025 and possibly might be in 2026 also.**

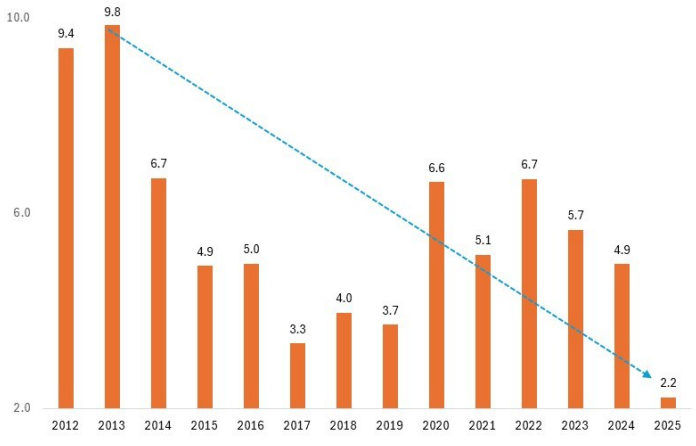
Meanwhile, after showing signs of considerable ebbing of frictions and fractures besieging the global geopolitical landscape towards later part of 2025, the year 2026 seems to have started on a rather tumultuous note. In particular, the circles of conflicts, gyrating from events in Venezuela to Iran are counter intuitive to energy and commodities most, that can show erratic price patterns going forward, in a clear departure from predicted outcomes touted much till a few days back. Greenland can be the Waterloo for world realpolitik. The looming threat over the Fed chair, revered and criticized at once as with any Public Office of high standing but always representative as vanguard of the cherished autonomy of an iconic institution since the chaotic days of the Great Depression is likely to fan out to broader contours of global markets. **The clouding outlook now reminds us of the spat and skirmishes between then Fed chair Paul Volcker and President Ronald Regan, and the moody turns of events across markets in June'1987 when a third term was refused for Volcker.** Whether or not markets react negatively, will perhaps be the defining point in terms of price volatility in 2026. The impact on prices of key imports can be disordering though deceptive in the beginning while exports may face more headwinds in its diversification strategy. Early signals from markets remain mixed though US treasury yields are headed northwards highest since Sep'25.

A direct fall out of such global uncertainty is that RBI may need to continue with record OMOs this fiscal in order to manage liquidity conditions properly. So far, OMOs net purchase worth Rs 5.16 lakh crore has already been done and given the current global uncertainties, we believe RBI may have to go upto 2 lakh crore further OMOs purchase in the remaining part of FY to support durable liquidity quest amidst credit growth. A similar trend awaits FY27 also.

CPI INFLATION INCREASED TO 1.33% IN DEC'25

- India's CPI inflation increased to 3-months high of 1.33% in Dec'2025, from 0.25% in Oct'25, with a rise in food & beverages inflation.
- As MOSPI will release CPI data of Jan'26 (on 12 Feb'26) with a new base year of 2024 and updated consumption basket, it is expected that inflation will go up marginally to 2.4-2.5% in March 2025.
- In the 2012 base, this is the last data point, and the CY average indicate a lowest average inflation of 2.2% in 2025.
- Fuel and light inflation declined to 1.97%, while miscellaneous items prices increased in Dec, with a rise in prices of personal care and effects, owing to higher gold prices. Inflation in gold remains high at 68.6% in December, compared 58.6% in Nov'2025. Silver inflation is at 97.1% in Dec, compared 65.6% in Nov'2025.

Overall CPI Inflation Reached at the lowest level of 2.2% (in 2012 Base



Source: SBI Research

GLOBAL UNCERTANITIES

- After showing signs of considerable ebbing of frictions and fractures besieging the global geopolitical landscape towards later part of 2025, the year 2026 seems to have started on a rather tumultuous note. In particular, the circles of conflicts, gyrating from events in Venezuela to Iran are counter intuitive to energy and commodities most, that can show erratic price patterns going forward, in a clear departure from predicted outcomes touted much till a few days back. Greenland can be the Waterloo for world realpolitik, as any coercive deal making can keep Europe on the tenterhooks and would be the catalyst of a phenomenal restructuring woven around national interests and security architectures, building blocks of NATO being the Guinea Pig of such misadventures first. **That may also necessitate new lines of thoughts along China-Taiwan-Japan trifecta, as also how the smoldering conflict in Europe progresses further against a largely futile truce talk in vogue.**
- The looming threat over the Fed chair, revered and criticized at once as with any Public Office of high standing but always representative as vanguard of the cherished autonomy of an iconic institution since the chaotic days of the Great Depression is likely to fan out to broader contours of global markets. **The clouding outlook now reminds us of the spat and skirmishes between then Fed chair Paul Volcker and President Ronald Regan, and the moody turns of events across markets in June'1987 when a third term was refused for Volcker. Bond prices suffered their worst pounding in years while equities dropped and gold had soared. A déjà vu seems to be in making perhaps. Whether or not markets react negatively, will perhaps be the defining point in terms of price volatility in 2026.**
- **With gold charting new highs from its demand from all core components; jewellery to industrial usage to investors' asset diversification and hedging strategies, there is a growing scepticism towards dollar dominance,** the pace of de-dollarization evident through holding of US treasury securities where BRICS nations have toned down their holdings significantly while DMs and conduit economies have gone up considerably.
- Contrary to many market 'experts', we don't think the quick gains of silver would warrant a tilt in its favour by the Central Banks, ostensibly for two reasons, First the panic signal it would send to broader markets as also the stakeholders and the very high (vis-à-vis gold) storage, holding, insurance and transportation/freight charges incurred that may dim the appeal. Also, the supply constraints in silver are much pronounced right now and silver may not be the object of desire for the Central Banks for now at least.
- **To cut a long story short, the impact on prices of key imports can be disordering though deceptive in the beginning while exports may face more headwinds in its diversification strategy. Also, the lines of capital and investments can be undergoing seismic currents in the aftermath of these events, the sum of the parts having a greater force than the arithmetic sum.**
- A direct fall out of such global uncertainty is that RBI may need to continue with record OMOs this fiscal in order to manage liquidity conditions properly. So far, OMOs net purchase worth Rs 5.16 lakh crore has already been done and given the current global uncertainties, we believe RBI may have to go upto 2 lakh crore further OMOs purchase in the remaining part of FY to support durable liquidity quest amidst credit growth.

RBI OMO including Secondary market(Rs lakh cr)

Fiscal	Purchase	Sale	Net purchase(+)/ net sale(-)
2016-17	1.11	0.00	1.10
2017-18	0.01	0.90	-0.89
2018-19	2.99	0.00	2.99
2019-20	1.46	0.32	1.14
2020-21	5.08	1.94	3.13
2021-22	2.78	0.64	2.14
2022-23	0.00	0.35	-0.35
2023-24	0.00	0.19	-0.19
2024-25	2.83	0.24	2.59
2025-26	5.16	0.00	5.16

Source: RBI; SBI Research

FOOD INFLATION

- First time in the history of current series that food inflation is in negative territory for consecutive seven months (in Aug'25 it was near to zero). Before this, the food disinflation exhibited for five months ranging from Oct'18 to Feb'19. Not only this, the year 2025 unveiled the lowest level of yearly food inflation (0.4%) in the entire series (since 2012) and way below the 14-year average of 5.8%.
- State wise food inflation shows that only 4 of the 22 major states have witnessed positive food inflation in Dec-25. Kerala witnessed maximum increase in food inflation 6.25% followed by Goa (4.0%) and Karnataka and TN slightly positive (0.4% and 0.2% respectively). Of these 4 states Kerala and Goa are the ones which have witnessed consistently higher food inflation this fiscal. Meanwhile, UP registered maximum deflation in food prices, followed by Odisha and MP.

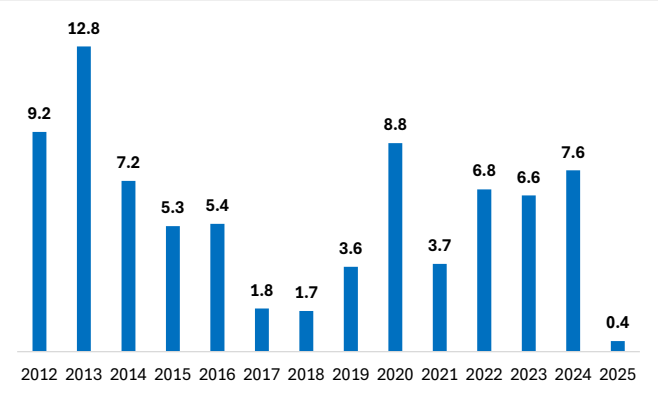
DEMAND & SUPPLY FACTORS

- Using the idea from the recent paper by Shapiro (How Much Do Supply and Demand Drive Inflation? FRBSF Economic Letter, June 21, 2022), we sliced the 299 items under CPI inflation to understand whether the drivers of inflation were demand or supply. Our analysis shows that out of 299 commodities in CPI, the drivers for 171 items could be categorised as factors that are supply driven (123 items being food), 99 as demand driven and 29 are neutral.
- Our results thus show that supply side factors related to food have been one of the defining factors in ensuring that food inflation has stayed range bound for major part of 2025.

FEDERAL RESERVE RATE OUTLOOK

- The Federal Reserve's first monetary policy meeting for 2026 is due at the end of January. The Federal reserve ended 2025 with 25 bps cut taking the federal funds rate to 3-1/2 to 3-3/4 percent.
- The internal median forecast for CPI and unemployment in December was positioned at 2.4% and 4.4% respectively. The latest unemployment reading at 4.4% is declining and CPI for December expected on January 13 is expected to be higher by around 3%, keeping issue of data quality in mind.
- Thus, with labor markets showing sideways movement, and CPI expected to rise, a rate pause in the near term looks the most likely scenario. The rate glide path in 2026 is expected to be slow and not dramatic.

Food Inflation (Yearly average, % YoY)



Source: SBI Research

State wise Food inflation (% yoy)

States	Apr-25	May-25	Jun-25	Jul-25	Aug-25	Sep-25	Oct-25	Nov-25	Dec-25
ALL India	2.1	1.5	-0.2	-0.8	0.0	-1.4	-3.7	-2.8	-1.8
Andhra Pradesh	0.7	-1.2	-4.8	-3.8	-1.2	-2.7	-5.2	-2.4	-0.4
Assam	2.9	1.8	1.1	-1.5	-1.5	-1.4	-2.6	-2.9	-2.4
Bihar	3.1	0.6	-0.6	-1.9	-0.6	-2.4	-4.7	-4.1	-3.5
Chhattisgarh	2.7	2.8	0.8	-0.5	0.4	-1.5	-5.2	-4.3	-2.5
Goa	9.3	9.9	6.7	8.8	5.1	4.8	3.9	3.6	4.0
Gujarat	1.0	1.5	-0.1	-0.5	-1.3	-2.8	-5.1	-2.9	-1.7
Haryana	2.1	2.5	1.5	-1.1	0.7	-1.6	-4.5	-3.9	-3.6
Himachal Pradesh	2.2	3.5	3.6	2.3	3.4	3.0	-0.4	-1.1	-1.0
Jammu and Kashmir	3.2	3.6	3.3	2.2	2.4	3.2	0.8	-0.3	-0.4
Jharkhand	2.6	1.1	-0.7	-0.3	1.3	-1.2	-4.7	-4.0	-2.0
Karnataka	2.3	1.3	-0.3	0.0	2.4	1.0	-0.9	-0.2	0.4
Kerala	6.4	6.8	6.4	11.5	10.7	8.9	6.2	5.7	6.2
Madhya Pradesh	1.3	1.7	-0.7	-2.3	-1.2	-3.3	-6.8	-5.5	-4.3
Maharashtra	2.7	2.3	0.5	0.2	0.4	-1.6	-3.0	-2.5	-1.1
Odisha	1.6	1.1	-2.0	-3.0	-3.4	-2.3	-5.4	-5.0	-4.5
Punjab	3.7	4.0	2.6	0.8	1.0	0.2	-2.1	-2.4	-2.3
Rajasthan	1.0	1.2	-0.2	-1.5	-1.5	-3.0	-5.5	-4.5	-3.6
Tamil Nadu	1.8	0.4	-1.0	-0.7	1.3	0.4	-2.2	-0.4	0.2
Telangana	-1.1	-2.6	-5.8	-4.5	-1.9	-4.3	-6.5	-4.0	-0.7
Uttar Pradesh	1.5	0.9	-0.5	-2.9	-2.5	-4.3	-6.4	-5.2	-4.6
Uttarakhand	2.2	1.7	1.8	-0.7	1.9	-0.3	-2.7	-2.9	-2.6
West Bengal	3.5	1.9	-0.3	-1.4	0.9	0.5	-2.3	-2.4	-1.7

Source: MOSPI, SBI Research

Bifurcation of CPI headline inflation into Demand led and Supply led Inflation

	# of Items	Wtd. contribution	Sep-25	Oct-25	Nov-25	Dec-25
Demand CPI	99	%	-0.4	-1.6	-1.2	-0.7
Supply CPI	171	%	1.8	1.8	1.8	2.0
Neutral	29		0.1	0.1	0.1	0.1
Overall CPI	299	%	1.44	0.25	0.71	1.33

Source: SBI Research

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