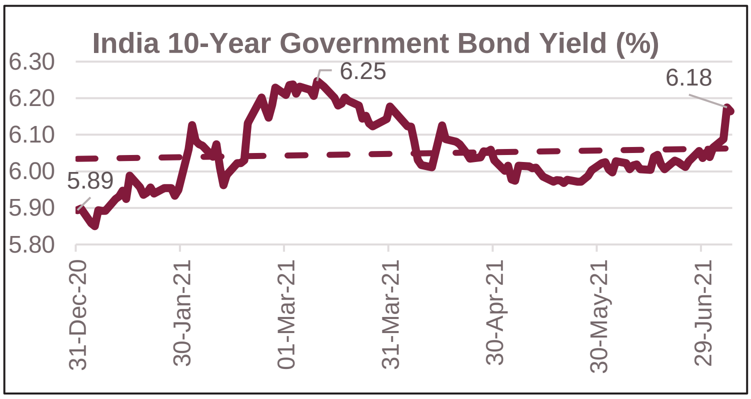
09 July 2021

The India 10 year benchmark yields spike

Key Highlights

- **India 10 year GSec yields climbed** about 9 bps on Tuesday 6 July 2021 to **6.18%** to the highest in more than 3 months.
- **Rising Global Crude Oil Prices** putting pressure on Inflation dynamics in the country.
- **New benchmark paper yielding higher** at 6.15% in the "when issued" market.
- **Exclusion of liquid papers from G-SAP.**

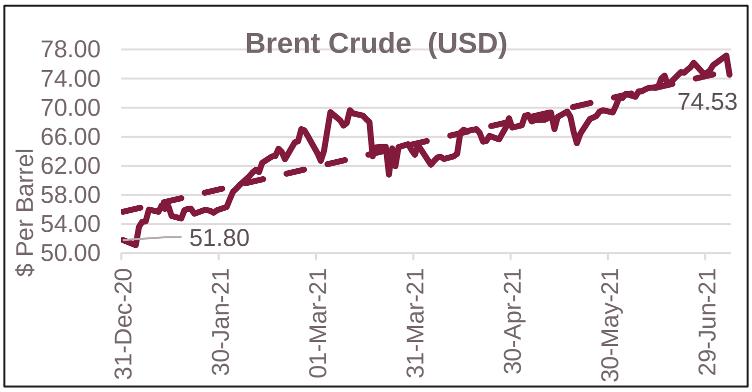
The **India 10 year GSec yields climbed about 9 bps on Tuesday 6 July 2021 to 6.18% to the highest in more than 3 months** on concerns over rising global crude oil prices and its cascading impact on logistics cost, thus leading to inflationary pressure in the economy. At the same time, the selection of papers for this week's bond buyback by the central bank also disappointed investors and the new benchmark yielded higher in the "when issued" market.



Source: Investing.com

Factors that led to the spike in the yields are stated below:

Rising Global Crude Oil Prices putting pressure on inflation dynamics in the country: Oil prices hit some of their highest levels since 2018 after OPEC+ discussions were called off, increasing expectations that supplies will tighten further just as global fuel demand recovers from a COVID-19-induced fall. India imports more than two-thirds of its oil requirements and higher prices usually translate to higher inflation; which has surpassed the RBI upper tolerance limit of 6% in May 2021.



Source: Investing.com

New benchmark paper yielding higher: The new benchmark paper is usually introduced by the RBI when the outstanding limit in the current GSec (Coupon of 5.85% maturing in 2030) reached about Rs. 1.20 lakh crore.

The outstanding limit of the current GSec has almost reached Rs. 1.20 lakh crore and furthermore, the RBI has mopped up about three-fourth of it via its G-Sec Acquisition Programme and special open market operations, and the trading volume in this paper has been gradually drying up. When traded in the "when issued" market it yielded higher at 6.15%. The "when issued" market, is a platform where a new benchmark paper is traded for price discovery before it is formally up for primary sale.

Exclusion of liquid papers from G-SAP: RBI announced a buyback of bonds worth Rs. 200 billion under the GSAP however it excluded certain liquid papers from it, thus most securities it proposed to buy were illiquid, which would not necessarily help tame yields and offset the impact of high global crude oil prices.

Outlook:

With economic activity increasing momentum once again after the second wave, leading to rise in demand and thus the prices of global crude oil, most **market participants are expecting** that the benchmark yields would touch the **6.25% mark by the end of the calendar year**.

Keeping these factors in mind and the fact that rates have bottomed-out we continue to maintain our stance of investing in shorter end of the curve through MF categories like **Low Duration / Floating Rate Funds.**

Good quality **Corporate Fixed Deposits** also appear to be an attractive option for **1-2 years horizon**.

For **longer term investments Short Term Funds / Corporate Bond Funds** continue to be our preferred categories.

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