

Dipanwita Mazumdar  
Economist

## **Bonds Wrap**

*Volatility in US 10Y yield steered movement in bond yields of major economies. Reverberation was primarily felt in major AEs such as Germany and UK. Even EMs were also not left out. The upward momentum in India's 10Y yield which was observed in Apr'24 was completely reversed in May'24, led by fall in US 10Y yield. Softer pace of outflow in the FPI debt segment (US\$ 88mn outflow, for 1-15 May) compared to US\$ 1.3bn outflow seen in Apr'24) also supported domestic 10Y yield in the current month. Going forward, we expect India's 10Y yield to remain in the range of 7.05-7.15% in the remaining days of May'24. Jun'24 is expected to see further downward correction in yield in anticipation of higher frontloading by FPI's ahead of inclusion in the JP Morgan global bond index.*

*System liquidity albeit being in deficit will get comfort from faster pace of growth of deposits compared to credit which is seen currently. Further, slower pace of accretion in CIC compared to same period of last year, is not expected to put any untoward pressure on liquidity, going forward.*

### **US 10Y yield guided movement of major global yields:**

- US 10Y yield exhibited considerable volatility in Apr'24 and May'24. It rose by 48bps in Apr'24. Factors which drove yield higher were stickier inflation print and tighter labour market data. This coupled with speeches of central bank officials which are forward signaling for the market, also hinted at wait and watch cautious approach going forward. However, the undertone completely changed in May'24 where US 10Y yield fell by 34bps. In the last trading session itself, it fell by 10bps. This was led by softer reading of current CPI and core print, which again fueled bets of rate cut to start this year. CMIE Fed watch tool is attaching the highest probability for 25bps rate cut by Fed in Sep'24.
- US 10Y yield has been the primary driver guiding the movement of other global yields. Other central banks such as BoE and ECB are also erring on the side of caution. BoE's Chief Economist also hinted at restrictive monetary policy approach. However, for ECB, traders are pricing in an earlier cut in Jun'24 as EU has cut its inflation forecast for CY24 to 2.5% from 2.7% earlier.
- 10Y yield in Japan reacted to reports of cut in bond purchase by BoJ by ~ ¥ 50bn of 5-10Year duration papers. Thus, 10Y yield will continue to exhibit upward momentum. China's 10Y yield is likely to get support from targeted government stimulus.

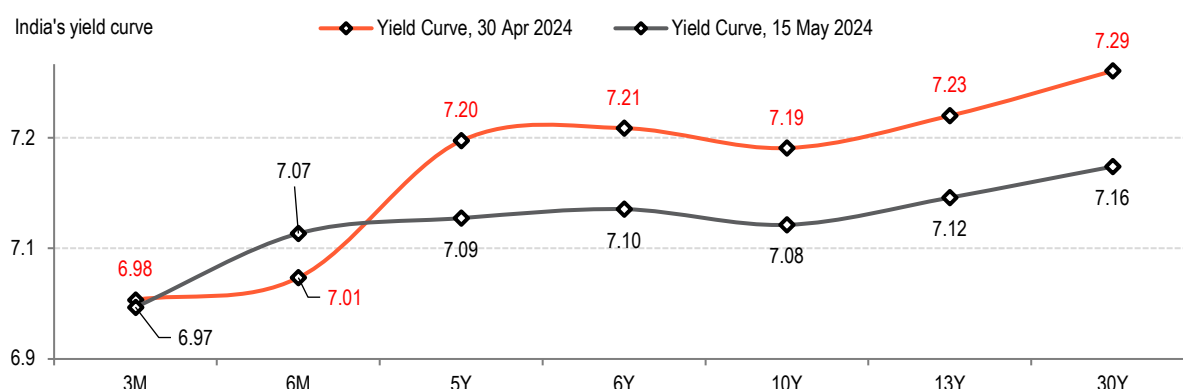
**Domestic 10Y yield** rose by 13bps in Apr'24. Much of it was attributable to higher debt outflow in FPI segment. In May'24, the upward momentum was arrested led by a fall in US 10Y yield. The pace of outflow of FPI debt has also been at a lower pace than observed in Apr'24.

**Table 1. 10Y Yields movement globally**

Countries	10Y sovereign yield, 30 Apr 2024	10Y sovereign yield, 15 May 2024	Change in 10Y yield, Apr/Mar	Change in 10Y yield, 15 May/Apr
Japan	0.88	0.96	15	8
China	2.31	2.30	2	-1
Thailand	2.76	2.74	26	-2
<b>India</b>	<b>7.19</b>	<b>7.08</b>	<b>13</b>	<b>-11</b>
Korea	3.65	3.55	25	-11
Germany	2.58	2.42	29	-16
Singapore	3.43	3.26	34	-18
Indonesia	7.25	6.98	55	-27
UK	4.35	4.07	41	-28
<b>US</b>	<b>4.68</b>	<b>4.34</b>	<b>48</b>	<b>-34</b>

Source: Bloomberg, Bank of Baroda Research, Note: Change in bps

**Figure 1: Evolution of India's yield curve**



Source: Bloomberg, Bank of Baroda Research

The 5Year and above part of the curve witnessed considerable downward movement. The short end part of the curve remained restrained supported by RBI nimble liquidity management approach. *The spread between 30Y and 3-month paper fell to 19bps currently compared to 31bps seen in Apr'24.*

**What auctions in the domestic market reflect?**

In May'24 (till 15 May), cut off yield for T-Bill slightly inched up.

**Table 2. Cost of borrowing**

Type of Papers	Cut off yield as on 30 Apr 2024	Cut off yield till 15 May 2024
Central Government Securities	7.23	7.21
SDL	7.48	7.44
Tbills	6.99	7.04

Source: Bank of Baroda Research, Note: Average cut off yield is taken to arrive at borrowing cost, Auction dates differ

### RBI's fine-tuning operations to support liquidity:

- Average system liquidity slipped into deficit of Rs 1.2 lakh crore for the first 15 days of May'24. This is against a surplus of Rs 20,240 crore seen in Apr'24. The results of VRR auction still reflect demand for funds. However, going forward some comfort on liquidity will be seen as incremental deposits have outpaced incremental credit by Rs 1.3 lakh crore (excl. merger).
- Durable liquidity also showed slight moderation. The accretion to currency in circulation in FYTD25 stands at Rs 0.75 lakh crore. However, the pace of accretion is lower than last year despite the ongoing election season. So, we do not expect any untoward pressure on liquidity going forward. Further, if the Fed cuts rate in Sep'24, it will further soften the dollar and will reduce leakage in terms of net forex purchase and provide comfort to durable liquidity.

### Outlook on 10Y yield for the next 30days:

- *India's 10Y yield is expected to remain in the range of 7.05-7.15% in the current month.* Jun'24 remains crucial as the narrative of RBI policy will set the tone for rate cuts. We expect that considering stickiness in food inflation, RBI might delay the rate cut cycle. OIS data also reflects no pricing of rate cut this year. Thus, primary driver of India's 10Y yield would be the trajectory of US 10Y yield. The current inflation and labour market data of US though led to some repricing; our view is that even Fed rate cut cycle might be slightly deferred as central bank officials have clearly signaled their objective of bringing down inflation sustainably to the targeted 2% level. In such a case, some upward pressure on domestic yield cannot be ruled out.
- However, what will counterbalance is that from Jun'24 onwards flows from inclusion to JP Morgan Global EM Bond Index will lead to higher frontloading by FPIs. Currently, the FAR holding for the benchmark security is at 11.55%, thus there is more scope to increase the holding percentage. Further, in Jun'24, Rs 1.08 lakh crore of securities are maturing, which will support liquidity and hence will be positive for yields.

**Table 3: OIS rates reflect no rate cut by RBI this year; corporate spreads remained stable**

	As on 30 Nov 2023	As on 29 Dec 2023	As on 30 Apr 2024	As on 15 May 2024
<b>OIS Rates</b>				
1M	6.87	6.79	6.73	6.7
2M	6.87	6.78	6.74	6.73
9M	6.86	6.66	6.85	6.77
<b>Corporate Spreads 10Y, bps</b>				
AAA	41	43	31	32
AA+	70	76	64	66
AA	106	111	101	101

Source: Bloomberg, Bank of Baroda Research

## **Disclaimer**

The views expressed in this research note are personal views of the author(s) and do not necessarily reflect the views of Bank of Baroda. Nothing contained in this publication shall constitute or be deemed to constitute an offer to sell/ purchase or as an invitation or solicitation to do so for any securities of any entity. Bank of Baroda and/ or its Affiliates and its subsidiaries make no representation as to the accuracy; completeness or reliability of any information contained herein or otherwise provided and hereby disclaim any liability with regard to the same. Bank of Baroda Group or its officers, employees, personnel, directors may be associated in a commercial or personal capacity or may have a commercial interest including as proprietary traders in or with the securities and/ or companies or issues or matters as contained in this publication and such commercial capacity or interest whether or not differing with or conflicting with this publication, shall not make or render Bank of Baroda Group liable in any manner whatsoever & Bank of Baroda Group or any of its officers, employees, personnel, directors shall not be liable for any loss, damage, liability whatsoever for any direct or indirect loss arising from the use or access of any information that may be displayed in this publication from time to time.

Visit us at [www.bankofbaroda.com](http://www.bankofbaroda.com)



---

**For further details about this publication, please contact:**

Economics Research Department

Bank of Baroda

[chief.economist@bankofbaroda.com](mailto:chief.economist@bankofbaroda.com)