

India bond yields rising slower than in US, but not for long

Analysts expect bond yields to go up faster in the new financial year amid inflationary pressure

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Interest rates and the benchmark bond yields are now rising in most economies across the world but the increase has been relatively muted in India than developed markets, such as the United States. The yield on the benchmark 10-year Government of India bond is up around 37 basis points year-to-date to 6.83 per cent (as on Wednesday), from 6.45 per cent at the end of December 2021.

In the same period, the benchmark bond yields in the United States are up 87 basis points. The gap widened further in March. Bond yields in the US are up

56 points since the beginning of the current month, against around 6-basis point rise in India.

This has led to a sharp fall in the spread on India's 10-year bond yield over the US' 10-year bond yield. The spread declined to a 10-month low of 445 basis points on Wednesday. For comparison, the spread was 494 basis points at the end of December 2021 and 495 basis points at the end of February.

Experts attribute this to the recent moves by the Reserve Bank of India (RBI). "The RBI calmed down the bond market after yields spiked after the Budget announcements. It also cancelled two bond auctions; there has been



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no fresh market borrowing by the Union government for nearly two months now," said Madan Sabnavis, chief economist at Bank of Baroda.

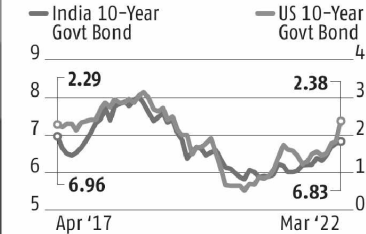
"The yields had cooled down slightly with support from the RBI's dovish monetary policy in early February and the cancellation of two successive weekly G-Sec auctions amounting to

₹48,000 crore, besides the cancellation of G-Sec switch auction," wrote Suman Chowdhury, chief analytical officer Acuité Ratings & Research.

Economists, however, are of the opinion that the relative pause in the bond yield in India may not last long. "In the long term, bond yields in most major economies move together. As

WIDENING GAP

The historical trend in the bond yield in the US and India



Note: Latest number if for March 23, 2022
Source: Bloomberg

such, the yields in India are expected to go up in coming months as they rise elsewhere in the world," said Devendra Pant, chief economist and head public finance at India Ratings & Research.

In the last 10 years, the yield on 10-year Government of India bond has been 522 basis points higher than a 10-year US government bond on average.

The spread has, however, ranged from a high of 681 basis points in May 2012 to a low of 385 basis points in November 2016.

Analysts now expect bond yields in India to start rising in the new financial year. "Going forward, we continue to expect 10Y G-Sec yield to move towards 7.25 per cent by March 2023 as supply pressures will dominate and the central bank may not be willing to deploy large scale OMO purchases as it did in FY21 and FY22 to infuse liquidity and support yields," said Chowdhury.

Bond yields may get a push from factors, such as an expected rise in inflation due to higher commodity prices, and further rate hikes by the US Fed Reserve and the European Central Bank. "Bond yields in India ultimately depend on a number of factors, such as inflation, banks credit to deposit ratio, changes in the RBI's forex reserves, and trajectory of interest rate globally," says Dhananjay Sinha, MD and chief strategist JM Financial Institutional Equity.