Benchmark 10-year yield closed almost flat at 6.02%, down by 01 bp from its previous close of 6.03%. The Reserve Bank of India's kept the benchmark interest rate unchanged. The repo rate will continue at 4% and the reverse repo rate at 3.35%. With this, the repo rate has remained unchanged for a sixth consecutive time.

Some of the key announcements of the policy are as follows:

- The MPC members unanimously voted for keeping the policy rates unchanged
- The MPC also unanimously decided to continue with an accommodative stance as long as necessary to revive and sustain growth on a durable basis and continue to mitigate the impact of COVID-19 on the economy, while ensuring that inflation remained within the target going forward
- Growth projections have been revised downwards, with real GDP growth expected to be at 9.5% in FY2022 (vs an earlier expectation of 10.5%)
- The projection for CPI inflation has been marginally revised upwards to 5.2% in Q1 FY2022, 5.4% in Q2 FY022, 4.7% in Q3 FY2022 and 5.3% in Q4 FY2022

READ THE FULL RBI REPORT WITH MARKET IMPACT

MARKET PERFORMANCE

The 10-year benchmark G-Sec yield closed at 6.02%, down by 01 bp from its previous close of 6.03% while that on the short-term 1-year bond ended 05 bps higher at 3.85%.

In the corporate bond segment, yields fell across the yield curve over the month.

The 10-year AAA bond yield ended 04 bps lower at 6.78%, while the short-term 1-year AAA bond yield ended flat at 4.17%.

The spread between 1-year and 10-year AAA bond narrowed. Within the short-term segment, the yield on 3-month commercial paper (CP) was up 15 bps to 3.60% while 1-year CP yield was flat at 4.20%.

10-Year G-Sec

Past performance may or may not be sustained in the future.

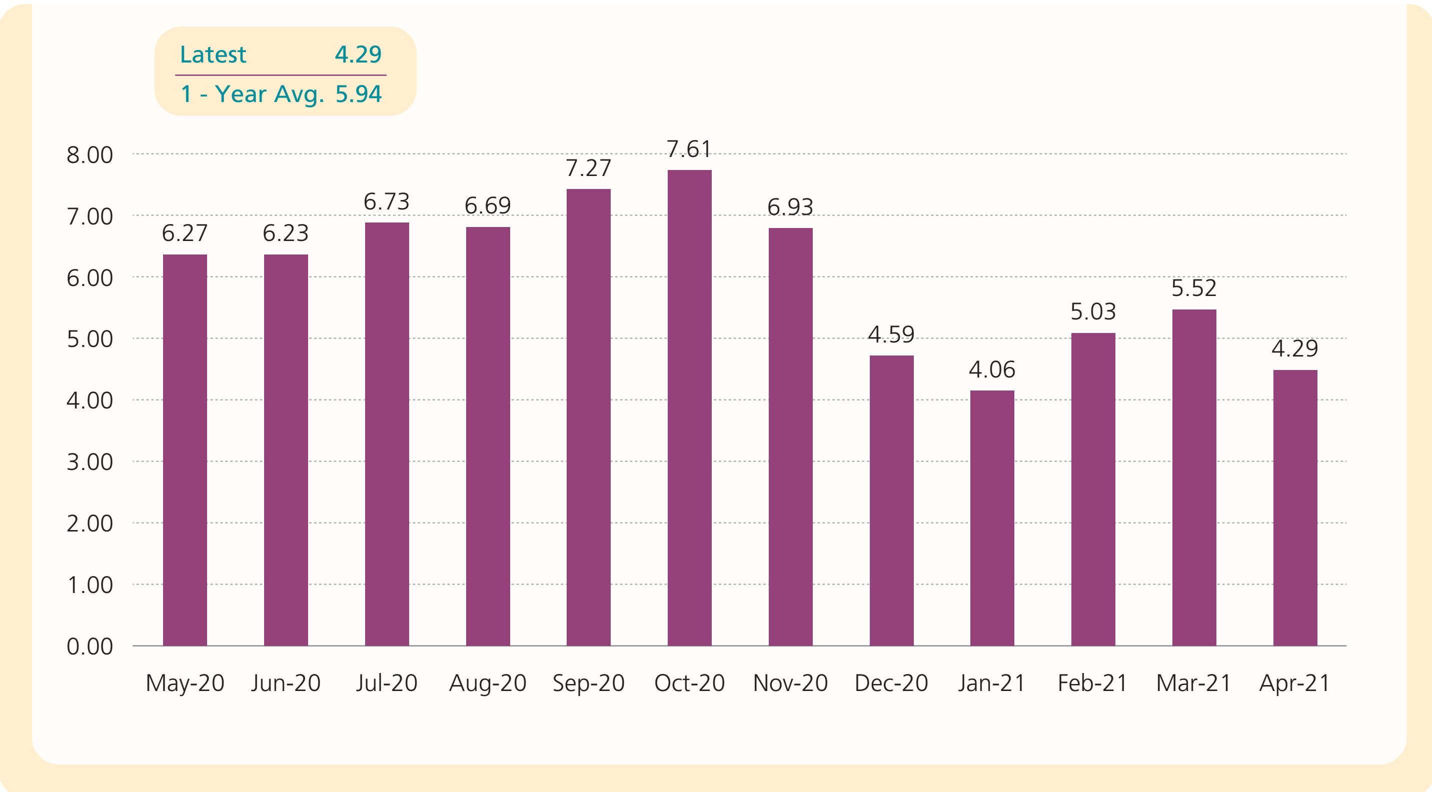
OUTLOOK

Bond markets have been broadly range-bound in May, both globally as well as here in India. Despite the noise and intense debate around the nature of inflationary forces in the US i.e. whether transitory or more sustainable, US Treasury yields have traded in a relatively narrow range of 1.55-1.70%. FOMC minutes for the April policy indicated that some of the members are hinting at a possible conversation around tapering of asset purchases at the upcoming meetings if the economy continues to show robust momentum and if inflation builds up above targeted levels. However, the broad-based guidance so far has been that the economy is short of where the Fed would expect it to be and markets should not price in a tapering in the near future.

With global growth continuing to pick up, OPEC members announced a net supply increase of 2.1 million barrels a day, however, demand is expected to outpace the increase in supply, which resulted in Crude prices moving above USD 70/bbl for the first time in a while. Crude prices remaining at these levels for a sustained period will remain a key monitorable for domestic rates.

Domestically – the focus has been entirely on the evolving second wave of the pandemic, the timing of its peak and the likely impact on growth. FY 22 growth estimates have been revised sharply lower by most research houses from the 11-13% earlier to 8-10% range. Against this backdrop, the April inflation data hardly caused any flutter in the bond markets. Headline CPI came in at 4.29% (vs 5.52% in March 2021) due to a favourable base effect and fall in food inflation. Core inflation also softened a bit to 5.43% after having been sticky over the past few months. WPI inflation spiked to an 11-year high of 10.49%, due to a rise in fuel and non-food inflation. The markets clearly believe that the focus of the RBI and the MPC over the next few quarters would be on supporting growth recovery, and any inflation worries are likely to be sidelined for now.

CPI Combined (YoY)



On the data front - Fiscal Deficit for FY2021 came in a tad lower at 9.2%. GDP for Q4 FY2021 came in at 1.6%, aided by a low base and higher Government spending. GDP for the full year FY2021 contracted by 7.3%. RBI announced a surplus transfer to the Government of INR 99,100 Crs for the period July 2020 to March 2021 (due to change in the financial year), higher than the budgeted amount of INR 53,500 Crs.

The Government of India indicated that there could be an additional borrowing to the tune of INR 1.58 Lakh Crs in FY2022 to fund the shortfall in cess collections required to compensate States. Even this news did not dent bond investor confidence too much and yields remained broadly range-bound – a testament to how effective RBI's control of the bond markets has been!

RBI continued to show discomfort with the 10-year benchmark trading above 6%. This is evident from the fact RBI did not accept any bids in the benchmark security in one of the auctions and devolved a substantial portion of the security on PDs in another. In order to keep yields below 6%, RBI accepted offers only in the 10-year security in the first OT auction of the financial year. With additional borrowing expected this year and SDL auction amounts still falling below the expected run-rate it will be important to see what measures RBI takes to keep yields at bay.

Source: MOSPI, Internal, Bloomberg