Bond Yields – Divergence across economies

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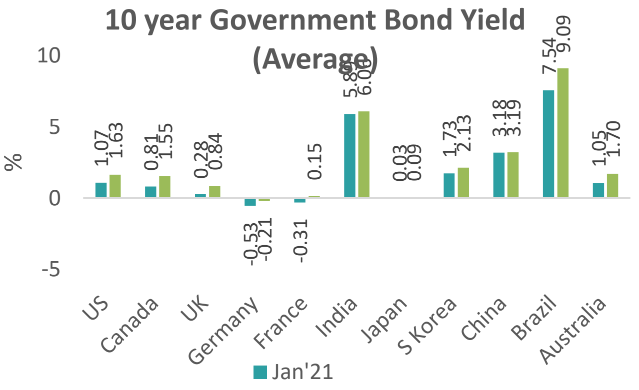
There has been a divergence in the global bond markets in April. While bond yields firmed up further across several major economies on indications of a strengthening economic recovery, it eased in case of some based on the economic outlook and policy support.

The pace of the rebound in economic activity in several economies viz. the advanced economies not only improved investor appetite for other riskier assets classes but has also raised the likelihood of a roll back of the extraordinary monetary policy viz. by way of the reduced bond purchases by the central banks which has been supporting yields at lower levels.

The analysis of the benchmark 10-year benchmark government bond yields of 11 major economies in April '21

- The benchmark sovereign bond yields across nearly all the major economies remained at elevated levels in April'21. The yields of these securities have witnessed a notable increase since the start of 2021.
    - Yields have climbed by an average 50 bps for all the major economies since January.
- There was a mixed trend in the movement of yields on a monthly basis in April. While seven of the major sovereign bonds saw an increase in average yields, the remaining four registered a decline.
    - USA (1bp), Canada (5 bps), UK (6 bps), France (22 bps), S Korea (8 bps), Germany (11 bps) and Brazil (46 bps) observed a rise in average yields from that in March'21.
    - Benchmark yields (average) fell in India (13 bps), Japan (1 bp), China (5 bps) and, Australia (5 bps) from month ago in April.
- Brazil witnessed the sharpest rise in (average) yields, taking the benchmark yields to 9.62%, the highest level in 28 months. The benchmark bond yields have increase by 155 bps year to date.
- The yields rose to a sixteen-month high in the US, Germany and Canada and to a near two year high in the UK and France. In case of South Korea, it increased to levels last seen November'18.
    - The average benchmark yields have hardened since January'21 by 56 bps each for the US and UK, 74 bps in case of Canada, by 46 bps for France, 33 bps for Germany and 40 bps in S Korea.
- Yields moderated to the lowest level in three months in India and China.
- Real, or inflation adjusted, benchmark sovereign bond yields were negative in the US, Canada, Germany, and France in April. It was in the range of 0.1% to 0.6% in the case of UK, Japan, S Korea, Australia, and India.



Source: CNN, Bloomberg, RBI and CARE Ratings

10 Year Government Bond Yield

	Mar'21	Apr'21	Range: April'21	Real Yields %: April'21
US	1.62	1.63	1.53 - 1.75	-1.0
Canada	1.50	1.55	1.44 - 1.62	-0.7
UK	0.78	0.84	0.71 - 0.87	0.1
Germany	-0.32	-0.21	(-0.35) - (-0.18)	-2.2
France	-0.07	0.15	(-0.10) - 0.17	-0.9
India	6.19	6.06	5.99 - 6.20	0.5
Japan	0.10	0.09	0.06 - 0.12	0.3
S Korea	2.04	2.13	1.97 - 2.14	0.6
China	3.24	3.19	3.16 - 3.25	2.8
Brazil	8.63	9.09	8.85 - 9.62	3.0
Australia	1.75	1.70	1.64 - 1.83	0.6

Factors driving bond yields across economies in April'21

US: Although Treasury yields continued to rise in April, the increase was marginal, indicating that the bond markets may be stabilizing. The sell -off in US bond eased during the month as investors pared down concerns over inflation and expectation of a faster tightening of the monetary policy. The reiteration by the Federal Reserve of maintaining low interest rates for a prolonged period along with its bond buying programme boosted sentiments. This along with the surplus liquidity in the system and the underlying pandemic led safe haven buying saw strong demand at the auction of Treasuries. At the same time, the concerns over the potential rise in Treasury bond issuances given the expansionary fiscal policy of the US government ($ 1.9 trn pandemic relief stimulus $ 2 trn infrastructure initiatives and $1.8 trn social spending) and the strengthening domestic economic recovery and encouraging corporate earnings that has boosted investor appetite for speculative investments kept bond yields at elevated levels

UK: Expectations of a lower pace of bond purchases and lesser stimulus amid indication pointing towards a strong economic recovery has pushed up bond yields.

Euro Zone: Germany and France saw a rise in bond yields on inflow of better-than-expected economic data that has raised expectations of a pull back of the extraordinary monetary policy measures. Rising equities also lowered demand for bonds.

Canada: Bond yields rose with the Bank of Canada signalling a rate hike in 2022 and announcing that it would taper bond purchases with the Canadian economic recovery seen to be on a strong footing.

South Korea: Optimistic outlook on the economy along with continued accommodative monetary policy raised bond yields.

Brazil: The rise in yields can be attributed to rising inflation that has raised the likelihood of an increase in interest rates amid higher government borrowings.

China: The decline in bond yields here has primarily been on account of the continued foreign inflows into the domestic bond markets. The higher interest rates of Chinese debt securities and the limited nature of pandemic stimulus programmes have been boosting inflows into the debt markets here.

India: The decline in the benchmark bond yields despite the underlying inflationary pressures and huge supply of government securities can primarily be credited to the RBI's announcement in early April to purchase sizeable quantities of government securities (Rs. 1 trillion in Q1 FY22) from the secondary market under the maiden G-sec acquisition or G-SAP 1.0 programme in conjunction with the regular open market operation, aimed at limiting the rise in bond yields. Concerns over the domestic economic outlook with the surge in the pandemic in the country also led to safe haven buying of government securities, cooling yields. Unfavourable global market conditions i.e., the rise in global bond yields, increase in commodity prices along with the weakening of the Indian Rupee, however weighed on investor sentiments and limited the fall in yields.

Outlook for the benchmark Indian Government Bonds

The RBI's secondary market purchases of government securities and other liquidity infusion measures are expected to anchor bond yields going forward. We expect the 10- year GSec yields to move in the range of 6.00 % - 6.05% in May'21.

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