

With IGB inclusion in JP Morgan Bond Index effective since 28th Jun'24, India has received an inflow of c. USD 0.6bn in FAR eligible securities. Impact of positive flows on Indian benchmark yields are yet to be seen as they remained near to 7% while with liquidity switching to surplus, the 3M T-Bill has fallen by 8bps. Whereas in US 10 year yields we have seen a drop of c.20bps last week to 4.27% as September rate cut probabilities rose post release of NFP data and downward revision of prior two months. In the current week, CPI data for Jun'24 and any cues on the Budget are key aspects to watch for continuity on being positive on both G-Secs and INR.

FPI debt flows of USD 0.6bn clocked post JP Morgan Bond Index inclusion:

- Average monthly inflow of ~\$2 Bn is expected due to IGBs being included in JP Morgan Bond Index, of which nearly ~1.82 Bn has been received during the month of Jun-24 in Debt Segment as per NSDL data.
- Starting Jul-24, from 01st to 05th, an inflow of USD 0.4bn (Rs.3,592 Crore) (Fig.1) was witnessed in FAR securities which is a little slower-than-expected pace. A cumulative of USD 0.6bn FPI flows have been received in FAR securities since 28th Jun'24.
- We expect inflows to continue over the coming months at the average monthly pace of ~\$2Bn across FAR securities. As the flows are trickling on daily basis instead of bulk trades, a one-off large impact on bond yields may not be witnessed.

Positive turnaround in systemic liquidity for the first time since mid-April:

- During the last week, liquidity surged to a surplus of Rs.1.3 lakh crore (on 5th Jul-24) from a surplus of Rs.0.3 lakh Crore (on 29th Jun-24).
- This is primarily led by a drop in government balance on spending post elections (Fig.2) and seasonal fall in currency leakage. Also, liquidity has been helped by FPI debt inflows last week.

US 10 Year softening amid jump in rate cut expectations:

- This was a holiday shortened week in the US, however, labour market economic data was on focus. The US 10-year Treasury note yield held its recent decline to around 4.3%, hovering near one-week lows as soft US economic data reinforced a dovish outlook on Federal Reserve monetary policy.
- As per Non-farm payrolls data, the US economy added 206K jobs in June 2024, slightly below a downwardly revised 218K in May and above forecasts of 190K. Data for May was revised sharply lower from an initial 272K and the April reading was also revised down by 57K to 108K. With these revisions, employment in April and May combined is 111K lower than previously reported. These revisions poked the investors spiking up the chances of rate cuts.
- Markets now see around a 76% chance of a Fed rate cut in September, with a second rate reduction in December also being priced in. Investors now look ahead to key US inflation data this week, as well as fresh commentary from Fed officials to guide the rates outlook further. Safe-haven demand for US bonds also pressured yields as investors prepare for the upcoming US presidential elections in November, while assessing the impact of recent elections in the UK and France.

Budget expectations brewing with CPI data due on 12th Jul:

- Now, India Budget for FY25 is to be presented on 23rd Jul'24. Going forward, Budget expectations shall drive the longer end of the yield curve in the near term. The focus of the Budget is how the Fiscal space created (0.6% of GDP) due to RBI dividend bounty (0.4%) and reduction in Fiscal Deficit (0.2%) from 5.8% to 5.6%, shall be allocated to Revenue & Capital expenditure or utilized in further lowering the fiscal deficit.
- CPI for Jun'24 is due on 12th July (post market hours) and is expected to jump above 5% with core CPI likely to stay flat at 3.1%. Due to sharp spike in vegetables prices along with cereals & pulses which kept food inflation at higher levels. Also, Jun-24 being the hottest Jun seen in 123 years further pushed the food prices up. Given that CPI data consensus range is wide (4.4-5.1%), in case the actual outcome is near the extreme ends of the range, we may see market impact next week.
- Monsoon deficit reported in Jun'24 has been witnessing a remarkable recovery to 2% surplus on 7th July vis-à-vis 11% deficit as of 30th June. Normalcy in monsoon could lead to softening of food inflation pressures over the course of the year helping to achieve MPC's headline inflation forecast of 4.5% for FY25.

Fig-1: FPI Flows in FAR Securities since 28th Jun-24 totaled c.USD 0.6 bn

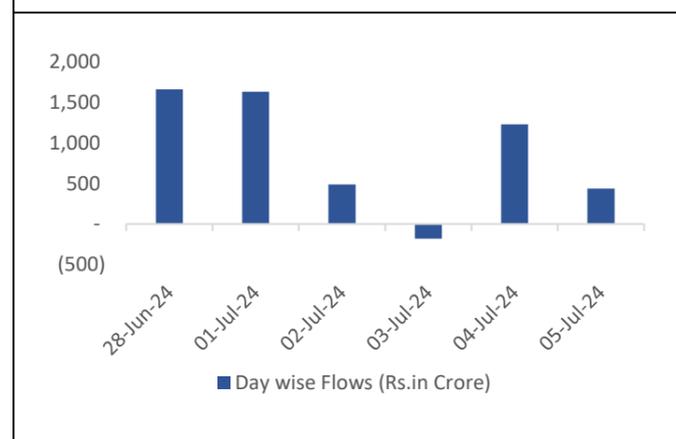
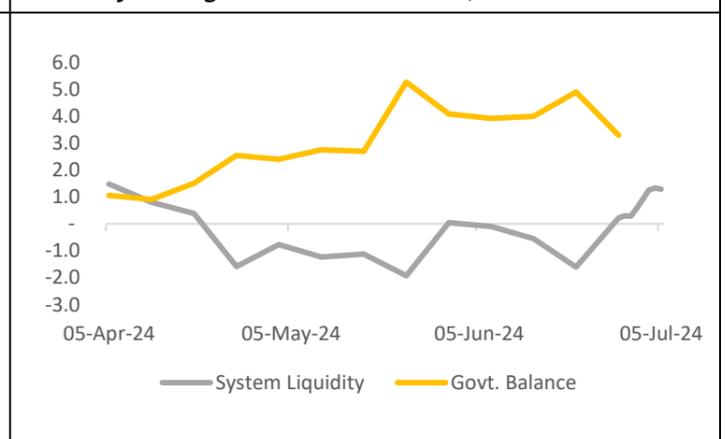


Fig-2: System Liquidity turned positive on fall in currency leakage and Govt. Balance; INR lakh cr



Source: CEIC, NSDL, CCIL, UBI Research

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