PNB GILTS LTD
HO: New Delhi

Debt Market Update
(For the week ended 14th June'10)

Money Market

Money market rates continued to remain firm on account of tight liquidity conditions. Robust 3-G auction outflows of nearly Rs. 68,000 crore led to significant decline in liquidity levels in the banking system. Both Call and CBLO rates traded near the upper bound of the LAF corridor during the week. In the coming weeks heavy outflow of advance taxes and BWA auction is likely to put further pressure on money market rates. RBI injected liquidity to the tune of Rs. 60,311 crore on a daily average basis, while reverse repo absorptions remained insignificant at Rs. 1,885 crore. Call rates ended the week at 5.15% vis-à-vis previous week's close of 4.89%, while CBLO rates ended the week at 5.24% vis-à-vis previous week's level of 4.46%.

G-sec Primary Market

During the week, GOI raised Rs. 11,000 crore through issue of new 5-yr paper (Rs. 4,000 crore), 10-yr paper 7.80% GOI 2020 (Rs. 5,000 crore) and 22-yr paper 8.32% GOI 2032 (Rs. 2,000 crore). 5-yr paper witnessed strong demand and bid to cover ratio of the same stood at 3.87. The cut off yield on the same was much below market expectations at 7.17%. On the other hand 7.80% GOI 2020 witnessed moderate demand and the same was sold at a yield of 7.57% (Price: Rs. 101.50). The 22 year paper was subscribed at 8.22% (Price: Rs. 101).

G-sec Secondary Market

During the week, bond yields traded with an upward bias as tight liquidity condition curbed demand for G-sec. Traders also remained wary ahead of release of monthly IIP and inflation data release. However the pace of rise in yields remained moderate given the bleak outlook of the global economy which may refrain RBI from raising interest rates rapidly. 10-yr yield rose to 7.60% levels on the last trading day as traders emptied position to accommodate fresh supplies. Stronger than anticipated IIP figure at 17.6% as against expected 14.3% in the month of April also pushed up yields higher. During the week, 10-yr yield rose by 9 bps to close at 7.61% as against 7.52% in the previous week.

Crude Oil

After trading subdued in the previous week, crude oil prices climbed up steadily from one week lows triggered by positive comments from the Fed chief on economic recovery. Significant pull back in dollar on speculation that US interest rates may remain at record lows also boosted demand for crude oil. Oil breached the psychological mark of USD 75 a barrel after a long gap as equities surged on back of strong economic data releases in China and Japan. Though an unexpected drop in US retail sales in the month of May took the market by surprise pushing oil prices lower by almost 3%, oil pared losses after a rise in US consumer confidence to the highest in two years was reported. Oil closed the week at USD 73.78 a barrel as against USD 71.51 a barrel in the previous week.

US Treasury Market

Treasuries made an positive start to the week with yield on 10-yr paper easing by 5-bps on emergence of buying after the sell off during the previous week. However, auction of securities during the week led to continuous rise in yields. While the amount of securities to be auctioned was lower in these auctions and demand as gauged by bid-to-cover ratio was also robust, still yields treaded upwards as market demanded higher yields given the amount of supply in market. Further, with Fed chairman stating that the impact of Europe's sovereign-debt crisis on the US is likely to be modest, yields shot up. Unexpected decline in US retail sales encouraging demand for the relative safety of government debt pulling down yields on the last trading day of the week. Yield on 10-yr benchmark paper ended the fortnight at 3.23% as against 3.20% during the previous week.

Forex Market

Rupee remained weak during most part of the week on speculation fund outflows from domestic stocks will accelerate as investors shun emerging-market assets amid concern the global economic recovery may stall. Rupee soon weakened above 47/Usd levels. However, rupee found buying support after release of higher-than-expected industrial production data. Rupee closed the week at 46.84/USD unchanged from previous week's level.

Outlook

Bond market is expected to open the week on a cautious note ahead of release of crucial monthly inflation number. Higher than anticipated IIP number for April had pushed up 10-yr yield to nearly 1 month highs at the end of previous week. Huge outflows of approximately Rs. 30,000 crore towards advance tax payments and Rs. 38,500 crore towards BWA auction are likely to keep upward pressure on yields in the coming week as well. However global cues will also be tracked closely as the global economic outlook continues to remain uncertain.

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