Government securities demand rises on short supply of SDL, AAA-rated corporate bonds

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The demand for government securities (G-Secs) has increased in the past few days, resulting in a sharp fall in yields on these instruments, due to the limited supply of state development loans (SDLs) and AAA-rated corporate bonds since the start of the current financial year.

Additionally, yields on government bonds also fell as traders covered their short positions. In the last two weeks, the yield on the benchmark bond 6.54%-2032 fell as much as 18 basis points, and is currently trading at 7.0422% level. “We have seen good demand in weekly G-Sec supply at the start of the financial year, largely due to the absence of any major supply in SDL and corporate bonds, coupled with G-Sec maturity worth Rs 27,000 crore,” said Sanjay Pawar, fund manager – fixed income, LIC Mutual Fund Asset Management.

Since the start of the financial year, states have raised just over 25% of the total budget amount to date worth Rs 8,000 crore, as against the budgeted amount of Rs 31,625 crore. Market participants said most states have remained on the sidelines because finance minister Nirmala Sitharaman, in the Union Budget, announced a 50-year interest-free loan of Rs 1 trillion to states to enable them to spend on capital investments, especially in infrastructure.

Further, issuance of corporate bonds having AAA ratings in the primary market has dried up, and only 3-4 issuers have tapped the market for fundraising because the higher coupon asked by investors are keeping most issuers on the sidelines. Usually, the first month of a financial year sees very less supply due to low capex. According to data compiled from market sources, companies to date have raised approximately Rs 4,000 crore as compared to around Rs 15,000 crore raised in the same period last year through AAA-rated corporate bonds.

Market participants said the sentiments of investors have improved after the release of MPC minutes, and the lack of supply into one segment is helping government bonds yields. “We think some segments of the market are finding the higher yields in the market (7% plus) attractive and also the fact that in general, the supply of bonds has been on the lower side over the last 2-3 months, meaning there is demand from real money players,” said Puneet Pal, head – fixed income, PGIM India Mutual Fund.

Traders believe yields on the government securities to trade in a very broad range going forward because the shift in demand from investors is transitory. The market will keenly watch the FOMC meeting and domestic CPI inflation numbers. Fund managers expect the yield on a 10-year bond to trade between 7.00% and 7.30%. However, going ahead, yields may inch upwards due to huge weekly bond supply in the first half of the financial year.