Bonds, ₹ strengthen as crude oil slides below $90 per barrel

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Government bonds and the rupee strengthened sharply on Thursday as crude oil prices declined to their lowest levels in seven months, easing concerns about elevated domestic inflation, dealers said.

Yield on the 10-year benchmark 7.26 per cent 2032 paper settled at 7.08 per cent as against 7.13 per cent at previous close. Bond prices and yields move inversely and a decline on 1 basis point in the 10-year yield corresponds to a rise in price of around 7 paise.

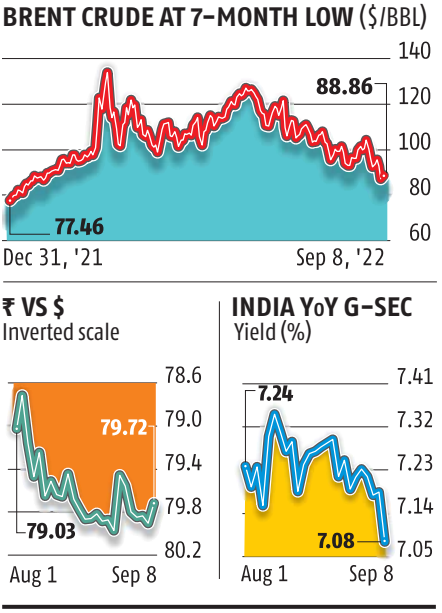
The rupee closed at 79.72 per US dollar as against 79.90 per dollar at the previous close. So far in 2022, the domestic currency has depreciated 6.7 per cent versus the US dollar.

International crude oil prices registered a steep decline on Wednesday, with Brent crude dropping below the prices that had prevailed prior to Russia's invasion of Ukraine as weak economic data from China stoked concerns of poor demand for the commodity.

The contract hit $87.40 per barrel on Wednesday, the lowest since January 25, but was marginally higher on Thursday, Reuters reported. Falling crude prices reduce upside risks to India's inflation and trade deficit, given that the country imports more than 80 per cent of oil needs. Last month, the Reserve Bank of India said it had assumed an average price of $105 per barrel for the domestic crude oil basket while providing inflation projections. India's CPI inflation was at 6.7 per cent in July, the first time in four months that the price gauge printed below 7 per cent. The RBI's target for CPI inflation is 4 per cent with a flexibility of 2 per cent on either side.

The fall in crude oil prices aside, a key factor that drove the buying in bonds was expectation of India's bonds being included on a global index in coming weeks.

Speculation of the event has been building up over the past few weeks as several global firms, including Morgan Stanley and Goldman Sachs, have said that they expect Indian sovereign bonds to be listed on international indices in 2023. Such a move could bring in inflows worth around $30 billion in a year. Two weeks ago, the *Financial Times* had reported that progress had made with regard to the inclusion of Indian government debt in the JP Morgan index. "There is a sustained positive momentum in the market because of the easing crude oil prices, US Treasury yields and a stronger expectation of global bond index inclusion," Naveen Singh, Head of Trading at ICICI Securities Primary Dealership said.



"In order for it to be operational by 2023, some sort of announcement would need to be made in September. Given the sort of momentum that we are seeing, I would not rule out the possibility of the 10-year yield falling below 7 per cent if there is good news on that front," he said. The rupee's strong showing on Thursday – the domestic currency fared better than several peer emerging market currencies – was also attributable to sustained inflows of foreign portfolio investment, dealers said.

Moreover, the RBI's firm defence of the rupee near the psychologically significant 80 per dollar mark, had also warded off speculation against the currency.