Yields on 10-year bonds could have neared their peak for now and should retrace if there be any positive trigger, sorely missing now.

The 10-year yields closed at 7.85 per cent on Friday. It is a rather sharp move up from the 6.5 per cent level in August, when the Reserve Bank of India (RBI) cut its policy repo rate. Since then, it has been an extended RBI pause but that didn't deter bond investors from pushing up the yields and demanding higher cut-off in the auctions.

There were certain triggers for that, the most obvious being the drying of liquidity at a time when US yields were nearing three per cent. The US 10-year yields have since fallen back to 2.8 per cent. That doesn't mean the foreign portfolio investors (FPIs) have slowed their pullout from Indian debt. In May, foreign investors have so far pulled out ~178 billion worth of their money from the debt segment.

Despite the pullout from FPIs, domestic investors say the bond market is only waiting for a clear signal from RBI on rates.

"The bond market can live with rates going up but cannot live with uncertainties," said Gaurav Kapur, chief economist at IndusInd Bank.

The present bond yields have already factored in a lot of negative news. If those developments don't materialise, there is no reason for bonds to remain elevated, say dealers.

"The present yields have factored in a lot of negative news already. At 7.8-8 per cent, it has factored in four rate hikes by RBI, US 10-year yields at 3.1-3.2 per cent and crude oil at $83-84 a barrel. The 30-40 year yields are attractive at an annualised 8.25 per cent," said Ramkamal Samanta, vice-president (investment), Star Union Dai-Ichi.

The attractiveness of long-term yields could be gauged from the fact that on Friday's auction, one bid took the entire ~10 billion offered on a bond maturing in 2033, and only two bids took the entire ~30 billion on a bond maturing in 2055.

"The yields look stable here because there is no trigger for softening, otherwise, the yields have room to fall. For example, if the monetary policy clears its stance on rates, on clarity with respect to OMO (open market operation) purchase of bonds to ensure the desired level of money supply growth, and on the government's likely fiscal outlook," said Samanta.

So far, RBI has conducted one OMO, or secondary market bond purchase. The market expects the central bank to conduct OMOs of up to Rs1 trillion to aid liquidity.

Strangely, if the RBI sounds hawkish in its June 4-6 policy review, it could sound music to the ears of bond investors. But if the central bank keeps its tone neutral and vague, expect yields to shoot up, bond dealers.