The 10-year gilt yield briefly crossed the 8 per cent mark in morning trades, but fell back below Thursday's close after news that Finance Minister Piyush Goyal had expressed concerns about high yields.

The rise in yields pushes up costs for everyone. Banks have been increasing their lending rates even before the Reserve Bank of India's (RBI's) rate hike this week. The cost of borrowing for corporates, as well as states and the Centre, goes up with every rise in yields.

As interest cost rises, investment activities take a hit. Goyal, according to sources, had discussed steps to bring down yields. Following this, the market started expecting that the RBI would bring out open market operations (OMO) announcements to buy bonds from the secondary markets, to provide liquidity in the banking system.

But OMOs are rarely done to manage yields.

"OMO purchases are done by the RBI for liquidity management. Post withdrawal of special banking notes, the system was flush with liquidity, therefore the RBI had refrained from OMO purchases, but as the economy grows the requirement of liquidity also grows," said Hemal Doshi, vice-president, treasury, at SBI DFHI Ltd.

The timing and the tools of liquidity infusion are decided by the RBI as and when its finds it appropriate, he added.

The 10-year gilt yield fell in the day to close at 7.95 per cent, lower than its previous close of 7.99 per cent. On Friday, the yield had for a brief period touched 8.03 per cent, but retraced soon on buying interest, said dealers. Complicating the matter is the rupee coming under pressure. The rupee closed at 67.51 to a dollar, down 0.56 per cent from its previous close of 67.13 to a dollar.

The rupee is tracking its Asian peers, according to Abhishek Goenka, managing director at IFA Global. He advised his importer clients to seek hedging at dips of till 67.30-67.35. India's foreign exchange reserves dipped $595 million to $412 billion for the week ended June 1. Reserves had peaked at $426 billion in April. "Exporters are advised to cover short-term exposure at current levels and wait for long-term forward bookings as the medium-term trend remains bullish," Goenka said.

Bond dealers say the Reserve Bank may have bought anonymously from the secondary market, but this is difficult to confirm because data is released with a lag. Gilt yields had touched 8 per cent back in December 2014.

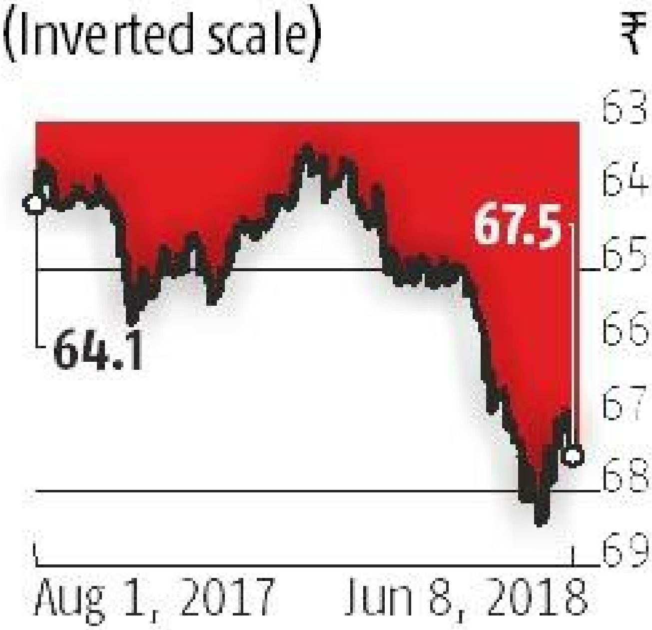
Nationalised banks, facing capital erosion due to their bad debt problem, are still not coming back in the bond market. And the government has met bankers earlier to convince them to return to the market. However, banks are sitting on excess bond holding of about 8-10 per cent and have no incentive to buy bonds in a rising interest rate scenario, according to a bank treasurer.

But bond dealers are not expecting a run-off in yields as of now. They expect bond yields to remain in the range of 7.80-8.10 per cent in the coming days. But a lot depends upon how crude oil prices behave and if global yields rise. The US 10-year bond yield has started rising and is around 2.93 per cent. Local yields are following the direction of US yields to a large extent, and had factored in a 25 basis points rate hike by the RBI.

RBI POLICY IMPACT

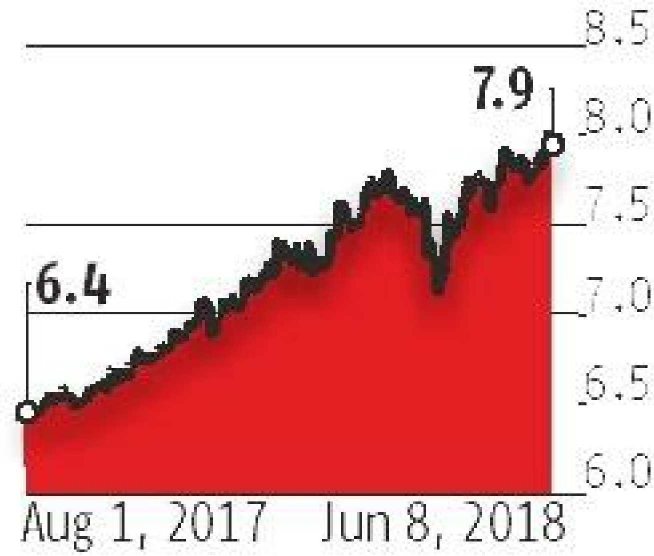
RUPEE VS DOLLAR

(Inverted scale)



INDIA G-SEC 10 YEAR

Yield (%)



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