India Bill Sale Fails as Money Rates Jump Most in a Year on RBI
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By Jeanette Rodrigues
July 17 (Bloomberg) -- India failed to sell treasury bills at a weekly auction after the central bank tightened policy for the first time since 2011, driving up interbank funding costs by the most in more than a year.

The Reserve Bank of India, which held the sale, rejected bids worth 293 billion rupees ($4.9 billion) received for a combined 120 billion rupees of 91- and 182-day notes offered, it said in an e-mailed statement. The overnight interbank borrowing rate in Mumbai surged 170 basis points to 8 percent today after the RBI increased on July 15 two of its interest rates by 2 percentage points each, while keeping the benchmark repurchase rate unchanged, to arrest a slide in the rupee.

The failure of the bill sale follows an offering of bonds yesterday by state governments, where the borrowers met only 26 percent of an 86 billion rupee target. With this week's rate increases, RBI Governor Duvvuri Subbarao joins policy makers from Brazil to China in reining in money-market liquidity to stem currency losses and ensure stability in the financial system. The rupee has lost 8.7 percent since March 31 in Asia's worst performance.

"Short-term rates are at an elevated level, so bids may have been at higher yields than what the government was comfortable with," said N.S. Venkatesh, the Mumbai-based head of treasury at IDBI Bank Ltd. "The market moves have been a knee-jerk reaction to the RBI's steps, and I think within a week or so things should settle down, when the market would have a clearer perspective of how liquidity will be."

India last sold 91-day bills at 7.48 percent on July 10 and 182-day notes at 7.60 percent on July 3.

'Shocked Market'

The yield on India's 10-year benchmark bond has jumped 50 basis points in the past two days to 8.07 percent, more than erasing declines since the start of the year. The rate, now up two basis basis points in 2013, will drop to about 7.90 percent in 10 days, and investors should buy now to gain from that, Venkatesh predicted, adding that the U.S. may not start paring stimulus before October.

The RBI increased the marginal standing facility rate and the bank rate to 10.25 percent from 8.25 percent, according to the July 15 statement. It also plans to sell 120 billion rupees of government debt at an open-market auction tomorrow to drain cash. In addition, the bank said it will cap its daily fund injections via repurchase contracts, meant to help lenders meet shortages, to about 750 billion rupees, compared with an average of 880 billion rupees availed by banks this year.

"The measures shocked the rates market," analysts at Standard Chartered Plc including Mumbai-based Samiran Chakraborty wrote in a research note yesterday. "The liquidity deficit will likely persist, implying elevated overnight rates and funding costs for government bond investors."

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