

VII

PUBLIC DEBT MANAGEMENT

The Reserve Bank successfully managed the large market borrowing requirements of the central government during 2015-16 in an orderly manner and at a lower cost despite multiple challenges such as reduction in Held to Maturity (HTM) category and Statutory Liquidity Ratio (SLR) impacting demand, tight domestic liquidity conditions and volatility in global financial markets. The maturity profile was elongated with a 40-year issuance. State government borrowings were managed at a lower cost, despite increase in supply mainly on account of issuance of UDAY bonds. The Ways and Means Advances (WMA) limits of the state governments were increased following the recommendations of the Advisory Committee on the same. During the year, the Medium Term Debt Management Strategy was formulated in consultation with the central government and placed in public domain. The agenda for 2016-17 includes formulating market making scheme for enhancing g-sec market liquidity, working towards better information sharing and daily cash flow forecasting through the Cash Coordination Committee (CCC), improving the design of Sovereign Gold Bond (SGB) to attract retail investors, imparting liquidity to State Development Loans (SDLs) and better liability management operations.

VII.1 The Reserve Bank has the obligation and the right to transact central government's business in India and manage its public debt in terms of Sections 20 and 21 of the Reserve Bank of India Act, 1934. As per the bilateral agreement signed under Section 21A, the Reserve Bank manages debt of all the 29 state governments and the Union Territory of Puducherry. It also acts as a banker to States, except Sikkim. Further, the Reserve Bank provides short-term credit to the central and state governments through Ways and Means Advances (WMA) to bridge temporary mismatch in their cash flows, in terms of Section 17(5) of the Reserve Bank of India Act, 1934. The Internal Debt Management Department of the Reserve Bank manages the operations relating to the central and state governments' market borrowings.

Agenda for 2015-16: Implementation Status

VII.2 During the year, the Reserve Bank successfully managed the large borrowing programme of the central government and the states in an orderly manner in the face of multiple challenges including reduction in HTM category

of banks' investments, reduction in SLR in an environment of tight liquidity, increased issuances by state governments and global uncertainties.

VII.3 The central government in consultation with the Reserve Bank designed a SGB scheme as an alternative to the purchase of metal gold. The Reserve Bank manages the scheme on behalf of the Government and issued three tranches of SGBs during the fiscal year 2015-16 (Box VII.1). Further, the Government of India (Ministry of Power) had formulated the Ujwal DISCOM Assurance Yojana (UDAY) scheme on November 20, 2015 with the objective to improve operational and financial efficiency of the state DISCOMs. The Reserve Bank during 2015-16 issued UDAY bonds for a total amount of ₹990 billion with a fixed spread of 75 bps over the FIMMDA g-sec yield. In 2016-17 so far, the issuance spread ranged between 63-74 bps for ₹495 billion. The response to the UDAY issuances has been robust and appears not to have had any adverse impact on the g-sec yields nor have the Uday issuances crowded out the SDL market. Price discovery for

Box VII.1 Sovereign Gold Bond Scheme

India is one of the largest consumers of gold in the world, accounting for around one-fourth of the total consumption. Gold imports accounted for 8.4 per cent of total merchandise imports in 2015-16. Thus, efforts to ease the pressure on the current account deficit (CAD) from gold imports have to incorporate a plausible strategy to moderate demand for gold by providing a safe alternative. Accordingly, three gold related schemes – the Gold Monetisation scheme, the Gold Coin Minted in India scheme and the Sovereign Gold Bond (SGB) scheme – were unveiled by the Government of India during 2015-16.

The SGB scheme is managed by the Reserve Bank on behalf of the Government of India. The scheme provides investors an assured nominal return besides savings in terms of storage costs for gold. There is no physical gold involved in the transactions. An investor pays the current price of gold and on maturity receives the price prevalent on that date. A coupon of 2.75 per cent per annum is paid

on a half-yearly basis. The bond is denominated in grams of gold with a cap of 500 grams per person per financial year. The tenor of the bond is for eight years, with the option of premature redemption after five years. Collection of SGBs is through banks, FIs, stock exchanges and post offices. SGBs can be used as collateral for loans. KYC norms for SGBs are similar to those for investments in physical gold.

The first tranche of SGBs was launched in November 2015. Subsequently, two tranches were floated in January and March 2016. Overall, subscriptions denominated in units of gold were at 4,904,130 grams amounting to ₹13 billion. Approximately, 0.4 million retail investors were successfully allotted SGBs, both in physical and dematerialised forms through the Reserve Bank's e-Kuber (CBS) platform. The fourth tranche, the first in 2016-17, which was floated in July 2016, witnessed increased investor demand with a total mobilization of ₹9.21 billion.

the UDAY issuances has also been efficient for the state governments.

Debt Management of the Central Government

VII.4 Gross market borrowings of ₹6,000 billion were proposed in the Union Budget 2015-16 through dated securities, of which ₹150 billion was allocated for issue of SGBs. The actual gross market borrowings through dated securities were ₹5850 billion and the net borrowings were ₹4406 billion which funded 82 per cent of the gross fiscal deficit (GFD) as against 89 per cent in the previous year. The net market borrowings of the central government, (*i.e.*, through dated securities and T-bills) declined to ₹4,530 billion in 2015-16 from ₹4,778 billion in 2014-15 (Table VII.1).

Debt Management Operations

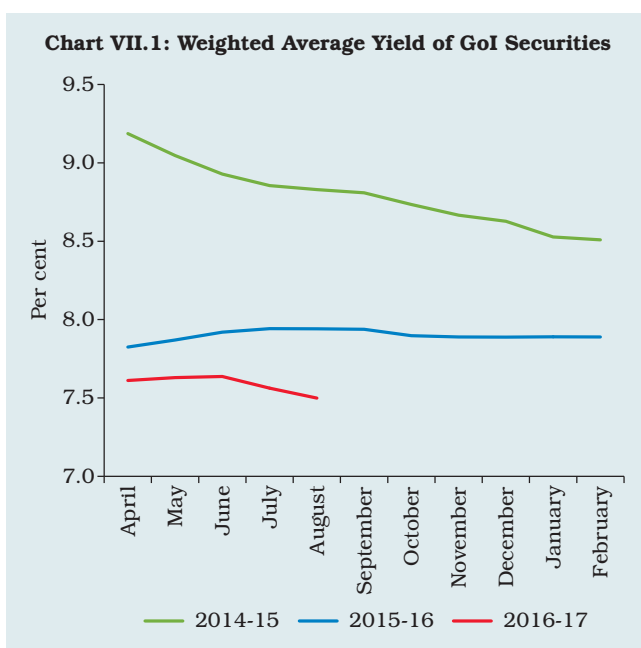
VII.5 The weighted average yield of dated securities issued during the year declined to 7.89 per cent from 8.51 per cent in 2014-15 (Chart VII.1). The yields which were stable for

Table VII.1: Net Market Borrowings of the Central Government

Item	(₹ billion)			
	2013-14	2014-15	2015-16	2016-17*
1	2	3	4	5
Net Borrowings	5,079	4,778	4,530	2,326
(i) Dated Securities	4,685	4,532	4,406	1,632
(ii) 91-day T-bills	207	114	63	640
(iii) 182-day T-bills	122	9	-40	48
(iv) 364-day T-bills	65	122	101	6

*: Up to August 16, 2016.

most part of the year, however, hardened during the second half. This was mainly on account of large and continuous supply of central and state governments securities, uncertainties over UDAY bonds and concerns over fiscal consolidation, in particular, on the implementation of One-Rank-One-Pension and the seventh pay commission's recommendations. There was, however, an overall softening in yields across tenors from end-February 2016 following the government's budget announcement adhering to the fiscal consolidation path; clarifications on the private



placement of UDAY bonds and their classification under the HTM category; reduction in the small savings rate; net open market purchases; expectations of better monsoon and rate cuts. A further decline in yield was driven by ample liquidity, expectations on passage of the GST Constitutional Amendment Bill and increased FPI activity amid increased global uncertainties, post Brexit.

VII.6 There was devolvement on primary dealers (PDs) in nine instances for an amount

of ₹110 billion in 2015-16 as compared to four instances for ₹53 billion in 2014-15. Devolvements were mostly in later half of the year on account of stressed market conditions arising out of concerns over UDAY bonds supply and global volatility. The share of PDs in subscriptions to primary auctions stood at 54.2 per cent in 2015-16 as compared to 51.8 per cent in 2014-15.

VII.7 The Reserve Bank continued with the policy of passive consolidation of g-secs by way of reissues. Out of 161 securities auctioned in 2015-16, 154 securities were reissues of the existing securities. In order to manage the maturity profile and reduce rollover risks of the government debt in a proactive manner, buybacks and switches were conducted in the fourth quarter of 2015-16 for an amount of ₹749 billion (₹579 billion in the previous year). This has modulated redemption pressures and reduced the quantum of gross borrowing requirement for 2016-17.

VII.8 Reflecting the strategy of maturity elongation, the weighted average maturity of borrowings increased to 16.0 years in 2015-16 from 14.7 years in 2014-15. Consequently, the weighted average maturity of outstanding debt increased to 10.5 years in 2015-16 from 10.2 years in 2014-15 (Table VII.2). The weighted average cost of outstanding market loans remained the

Table VII.2: Market Loans of Central Government – A Profile

(Yield in per cent/ Maturity in years)

Years	Range of YTM's at Primary Issues			Issued during the Year			Outstanding Stock	
	Under 5 years	5-10 years	Over 10 years	Weighted Average Yield	Range of Maturities	Weighted Average Maturity	Weighted Average Maturity	Weighted Average Coupon
1	2	3	4	5	6	7	8	9
2011-12	8.21-8.49	7.80-10.01	8.25-9.28	8.52	5-30	12.66	9.60	7.88
2012-13	8.82-8.21	7.86-8.76	7.91-8.06	8.36	5-30	13.50	9.66	7.97
2013-14*	7.22-9.00	7.16-9.40	7.36-9.40	8.41	6-30	14.23	10.00	7.98
2014-15*	-	7.66-9.28	7.65-9.42	8.51	6-30	14.66	10.23	8.08
2015-16*	-	7.54-8.10	7.59-8.27	7.89	6-40	16.03	10.50	8.08
2016-17@	-	7.05-7.61	7.20-7.87	7.52	5-40	14.37	10.53	8.05

Note: YTM: Yield to Maturity; -: No Issues; *: Excluding buyback/ switch in GoI securities. @ Upto August 16, 2016.

Table VII. 3: Issuance of Government of India Dated Securities - Maturity Pattern

(Amount in ₹ billion)

Residual Maturity	2013-14		2014-15		2015-16		2016-17*	
	Amount raised	Percentage to total	Amount raised	Percentage to total	Amount raised	Percentage to total	Amount raised	Percentage to total
1	2	3	4	5	6	7	8	9
Less than 5 years	110	2.0	-	-	-	-	150	5.9
5 - 9.99 years	2,305	40.9	2,350	39.7	2,000	34.2	840	32.9
10 - 15.99 years	1,340	23.8	1,510	25.5	1,600	27.4	870	34.1
16 - 19.99 years	930	16.5	960	16.2	1,120	19.1	340	13.3
20 years & above	950	16.9	1,100	18.6	1,130	19.3	350	13.7
Total	5,635	100.0	5,920	100.0	5,850	100.0	2,550	100.0

*: As on August 16, 2016.

same at 8.08 per cent during 2015-16. However, the cost has marginally declined to 8.05 per cent during 2016-17 (up to August 16, 2016).

VII.9 In view of limited space for issuance in maturities less than 10 years, about 66 per cent of the market borrowings were raised through issuance of dated securities with a residual maturity of 10 years and above in 2015-16 as compared to 60 per cent in 2014-15, leading to a decline in the share of maturities less than 10 years by the end of the year (Table VII.3). To cater to the demand from long-term investors like insurance companies and pension funds, a 40-year security was also issued in 2015-16.

VII.10 Commercial banks remained the largest holders of dated securities, accounting for around 40 per cent as at end-June 2016 (43 per cent as at end-March 2015) followed by insurance companies and provident funds. The share of the Reserve Bank's holdings increased to 14.9 per cent as on end-June 2016 as compared with 13.5 per cent as on end-March 2015, mainly on account of net outright OMOs purchases.

Medium Term Debt Management Strategy

VII.11 A Medium Term Debt Management Strategy (MTDS) was formulated by the Reserve Bank in consultation with the Government and

placed in the public domain on December 31, 2015. The MTDS has been articulated for a period of three years (2015-16 to 2017-18). It is premised on three broad pillars: low costs, risk mitigation and market development in line with the sound international practices while factoring in domestic economic and financial conditions. The low cost objective is pursued through measures such as planned and predictable issuances, suitability of instruments as per investor preferences and improved transparency through timely and appropriate communication to the market. The strategy adopted to contain rollover risks include switches/buybacks, elongation of maturity and placement of limits on issuances and annual maturities. Interest rate risks were dealt with by keeping the floating rate debt low; foreign currency risks were addressed by issuing debt in domestic currency, developing a stable domestic investor base and a calibrated opening of the g-secs market to foreign investors. The Reserve Bank will continue to develop the g-secs market by introducing new instruments, expanding the investor base and strengthening market infrastructure. Stress tests and scenario analyses in relation to costs, maturity and potential risks suggest that the Government of India's debt is stable and sustainable over the medium to long run.

Treasury Bills

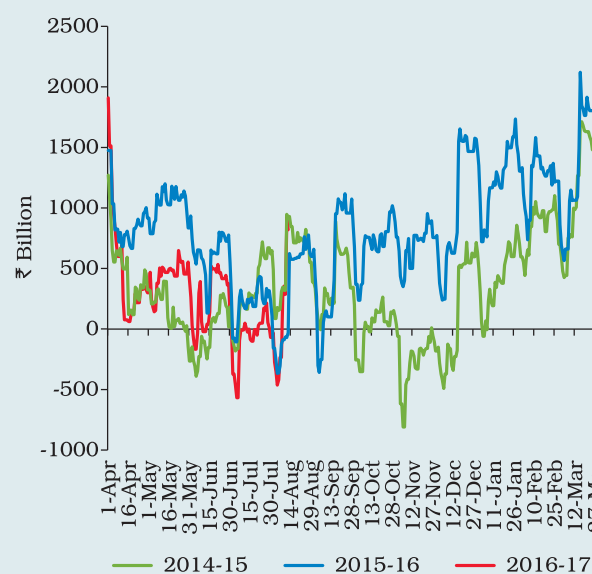
VII.12 T-Bills were issued essentially to smoothen the Government's temporary funding gaps. The net issuance of T-bills was lower during 2015-16 than in the previous year. The yields on T-bills softened during the year reflecting the easing interest rate regime. Primary Dealers (PDs) individually achieved the stipulated minimum success ratio and their aggregate share in T-bill auctions stood at 75.4 per cent in 2015-16, down from 77.2 per cent during 2014-15.

Cash Management of the Central Government

VII.13 The Government's WMA limits for the first and second halves of 2015-16 were fixed at ₹450 billion and ₹200 billion, respectively. The Government's cash position was largely comfortable as it started the year with a large cash balance of ₹1,573 billion. Recourse to WMA was limited to 16 days in 2015-16 *vis-à-vis* 61 days in the previous year (including 16 days of overdraft), reflecting relatively fewer gaps between receipts and expenditures. The average utilisation of WMA was lower at ₹187 billion as compared to ₹236 billion in 2014-15. The Government ended the fiscal year 2015-16 with a cash balance of ₹1,917 billion (Chart VII.2). The WMA limit for the first half of 2016-17 has been fixed higher at ₹500 billion.

VII.14 Effective December 16, 2014, the Government's surplus cash balance with the

Chart VII.2: The Government of India's Cash Balance



Reserve Bank is being reckoned for auction at variable rate repos.

Debt Management of State Governments

VII.15 Gross market borrowings of the states increased to ₹2,946 billion during 2015-16 through the issuance of 298 securities as compared to ₹2,408 billion mobilised through 282 securities in the previous year (Table VII.4). Despite increased supply, the weighted average yield of SDLs during 2015-16 was lower at 8.28 per cent as compared with 8.58 per cent in the previous year, reflecting the easing interest rate regime. However, the

Table VII.4: Market Borrowings of States through SDLs

Item	(₹ billion)			
	2013-14	2014-15	2015-16	2016-17 (up to August 16, 2016)
1	2	3	4	5
Maturities during the year	321	334	352	76
Gross sanctions under Article 293 (3)	2,174	2,435	3,060	1407
Gross amount raised during the year	1,967	2,408	2,946	900
Net amount raised during the year	1,646	2,075	2,594	823
Amount raised during the year to total sanctions (per cent)	92.0	99.0	96.0	64.0
SDLs outstanding (at the end period)	10,619	12,755	16,314	17,612

weighted average spread over the comparable central government securities increased to 50 bps from 38 bps during the previous year on concerns over increased supply due to UDAY bond issuances.

VII.16 An investors' meet was conducted during the year to increase awareness on SDLs with the objective of diversifying the investor base among market participants. Further, capacity building programmes were conducted in various states including North-Eastern states to sensitise them on better debt and cash management.

VII.17 State governments' borrowings were unevenly distributed during the year with bunching in the second half and more so in the fourth quarter. The Reserve Bank continuously engaged with the states to smoothen borrowings over the year, with the objective to lower costs. As part of this endeavour, state-wise quarterly borrowing calendar was introduced during 2015-16.

Cash Management of State Governments

VII.18 Investments by states in Intermediate Treasury Bills (ITBs) of the central government increased during the year. The daily average investments in ITBs increased marginally to ₹749 billion in 2015-16 from ₹731 billion in the previous year. Further, while the outstanding amount in Auction Treasury Bills (ATBs) continued to decline in 2015-16, the declining trend in investments in ITBs reversed over the same period (Table VII.5).

VII.19 During 2015-16, eleven states availed Special Drawing Facility (six states in 2014-15), eleven states availed WMA (10 states in 2014-15) and nine states availed Over Draft facility from the Reserve Bank in 2015-16 (10 states in 2014-15). The monthly average utilisation of WMA and OD by the states was higher during 2015-16 than that during 2014-15.

Table VII.5: Investments in ITBs and ATBs by State Governments/UT

(₹ billion)

Item	Outstanding as on March 31					
	2012	2013	2014	2015	2016	As on August 12, 2016
1	2	3	4	5	6	7
14-Day (ITB)	966	1,181	862	842	1,206	776
ATBs	220	286	463	394	383	814
Total	1,186	1,466	1,325	1,236	1,589	1,589

Advisory Committee on WMA to State Governments

VII.20 Pursuant to the recommendations of the Advisory Committee on WMA to state governments (Chairman: Shri Sumit Bose) which submitted its report in January 2016, the WMA scheme for States was revisited. The aggregate WMA limit for 28 States and the Union Territory of Puducherry was revised from ₹154 billion to ₹322 billion, effective February 01, 2016. The other recommendations of the committee are being examined and would be implemented in phases.

Investments in Consolidated Sinking Fund (CSF)/ Guarantee Redemption Fund (GRF)

VII.21 Outstanding investments in the CSF and the GRF maintained by state governments with the Reserve Bank stood at ₹781 billion and ₹44 billion, respectively, as at end-March 2016. Total investments in CSF/GRF during the year aggregated to ₹134 billion (₹141 billion in 2014-15).

Agenda for 2016-17

VII.22 The Union Budget 2016-17 projected gross market borrowings of ₹6,000 billion through dated securities, higher by 2.6 per cent than the actual amount mobilised during the previous year. Net funding through T-bills for 2016-17 has

been budgeted at ₹167 billion, higher by about ₹42 billion as compared to the previous year. Net market borrowings through dated securities have been estimated to fund 79.6 per cent of the budgeted GFD in 2016-17, which is lower than 82 per cent in 2015-16 (RE). Net market borrowings of States for 2016-17 are budgeted to finance 77.8 per cent of the states' consolidated GFD. The borrowing programme of the central and state governments is sought to be smoothly completed, while reducing costs and mitigating risks by adopting the following measures:

- i. Continuing the practice of frontloading of market borrowings through dated securities.
- ii. Switching of securities for effective liability management keeping in view the evolving market conditions.
- iii. Pursuing the objective of elongating the maturity to contain rollover risks.
- iv. MTDS articulated for three years will be reviewed and rolled over for the next three years (2016-17 to 2018-19).
- v. Cash Coordination Committee (CCC) comprising members from the Government of India and the Reserve Bank will work towards better information sharing, cash flow forecasting and management.
- vi. Features of the SGB scheme launched during 2015-16 will be improved upon for greater acceptability and expansion of the retail investor base.
- vii. With the objective of enhancing liquidity and giving a retail push to the secondary market for g-secs, a market making scheme will be formulated.
- viii. The Reserve Bank will continue to make efforts towards market development, providing greater predictability and ease of access to the g-sec auction process by market participants.
- ix. Market borrowings of the state governments will be spread more evenly across the year along with a more robust quarterly calendar.
- x. Reissuances of SDLs of different maturities will be continued to impart liquidity and better liability management operations.
- xi. The few remaining States which do not have CSF, will be encouraged to constitute it to strengthen their debt management operations.
- xii. The remaining issuances of special securities under the UDAY scheme will be completed with minimum market disruptions.