VII PUBLIC DEBT MANAGEMENT

The Reserve Bank conducted government's market borrowing programme smoothly during 2012-13 despite tight liquidity conditions. The weighted average yield of dated government securities declined and the weighted average maturity increased. To encourage savings by offering better menu choices to risk-averse investors, amidst high inflation in recent years, the Reserve Bank issued inflation indexed bonds.

DEBT MANAGEMENT OF CENTRAL GOVERNMENT

Market Borrowings

VII.1 The financial year 2012-13 was characterised by sustained inflationary pressure and tight liquidity conditions. The Reserve Bank, as the government's debt manager conducted the borrowing programme smoothly, guided by the twin objectives of minimisation of cost and pursuit of maturity profiles that are consistent with low rollover risk. Market borrowing to the tune of ₹5580 billion was successfully completed. Securities amounting ₹18 billion, however devolved on primary dealers as compared with ₹121 billion during the previous year. The gross and net amounts raised through dated securities in 2012-13 were higher by around 9 per cent and 7 per cent, respectively than those raised in the previous year (Table VII.1).

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

(₹ billion)

Item	2010-11	2011-12	2012-13
1	2	3	4
Net Borrowings	3,254 (3,450)	4,364 (3,430)	4,674 (4,790)
Gross Borrowings	4,370 (4,571)	5,100 (4,171)	5,580 (5,696)

#: Issuances through dated securities.
Note: Figures in brackets are budget estimates.

VII.2 The weighted average yield of dated securities declined to 8.36 per cent in 2012-13 compared to 8.52 per cent in 2011-12 due to easing of yield mainly for the long dated securities. The weighted average coupon on the outstanding stock of Government dated securities, however, increased to 7.97 per cent as on March 31, 2013 from 7.88 per cent as on March 31, 2012 (Table VII.2).

Table VII.2: Central Government's Market Loans - A Profile#

(Yield in per cent, Maturity in years)

Year	Range of YTMs at Primary Issues			Issues during the year			Outstanding Stock (As at end-March)	
	Under 5 years	5-10 years	Over 10 years	Weighted Average Yield	Tenor of securities	Weighted Average Maturity	Weighted Average Maturity	Weighted Average Coupon
1	2	3	4	5	6	7	8	9
2008-09	7.71-8.42	7.69-8.77	7.77-8.81	7.69	6-30	13.8	10.45	8.23
2009-10	6.09-7.25	6.07-7.77	6.85-8.43	7.23	5-15	11.16	9.82	7.89
2010-11	5.98-8.67	7.17-8.19	7.64-8.63	7.92	5-30	11.62	9.78	7.81
2011-12	8.21-8.49	7.80-10.01	8.25-9.28	8.52	7-30	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	9.67	7.97

#: Excludes issuances under MSS; YTM: Yield to Maturity.

VII.3 A large volume of long dated securities was issued during the year which resulted in the average maturity of debt issuances during 2012-13 to increase to 13.50 years from 12.66 years during the previous year.

VII.4 The weighted average maturity of the outstanding stock (based on residual maturity) increased to 9.67 years as on March 31, 2013 from 9.60 years as on March 31, 2012 (Table VII.2). During 2012-13 about 31 per cent of the market borrowings were raised through issuance of dated securities with maturity of 10-15 years as compared to 24 per cent in 2011-12 (Table VII.3).

VII.5 As per the Union Budget 2013-14, the gross market borrowings of the GoI through dated securities is estimated at ₹5,790 billion (net ₹4,840 billion) excluding ₹500 billion of buybacks/switches. The issuance calendar for dated securities for the first half of 2013-14 was issued in consultation with the GoI on March 18, 2013. An amount of ₹3,490 billion is scheduled to be raised in the first half as against ₹3,700 billion raised during the corresponding period of the previous year. Market borrowing of ₹2,400 billion in gross terms (and ₹2,272 billion in net terms) was completed by August 5, 2013. The weighted average maturity of the dated securities increased to 14.4 years from 13.62 years during the corresponding period of the previous year. The weighted average yield during the primary auctions (excluding IIBs) eased to 7.80 percent from 8.50 per cent during the corresponding period of the previous year.

VII.6 The yields on auction of Treasury Bills showed a declining trend till the middle of the quarter ending June 2013, but started hardening subsequent to the Fed Chairman's response in May 2013. Yields on Treasury Bills went up further significantly (by 273 bps and 209 bps for 91-day and 364-day treasury bills, respectively) subsequent to the liquidity tightening measures.

VII.7 The Union Budget 2013-14 had proposed to introduce instruments that will protect savings from inflation, especially the savings of the poor and middle classes. In the backdrop of the budget announcement, Inflation Indexed Bonds (IIBs) were issued through auction method on June 4 and 25, 2013 which is expected to provide benchmarks for the real yield and subsequently, IIBs exclusively for retail investors would be issued in the second half of 2013-14 (Box VII.1).

Cash Management

VII.8 The Government started the year 2012-13 with a surplus cash balance of ₹742 billion, but soon took recourse to WMA on April 12, 2012 due to its expenditure commitments (Chart VII.1).

Table VII.3: Issuance of GoI Dated Securities – Maturity Pattern

(₹ billion)

Residual Maturity	2010-11		2011-12		2012-13	
	Amount raised	Percentage to total	Amount raised	Percentage to total	Amount raised	Percentage to total
1	2	3	4	5	6	7
Less than 5 years	110	2.52	180	3.53	470	8.42
5 -9.99 years	1,520	34.78	2,340	45.88	1,910	34.23
10-14.99 years	1,640	37.53	1,230	24.12	1,730	31.00
15 -19.99 years	540	12.36	650	12.75	270	4.84
20 years & above	560	12.81	700	13.73	1,200	21.51
Total	**4,370**	**100.00**	**5,100**	**100.00**	**5,580**	**100.00**

Box VII.1
Issuance of Inflation Indexed Bonds

The debt management strategy should have a bouquet of instruments at its disposal for managing public debt in a cost-effective and non-disruptive manner. IIBs have emerged as a critical instrument for government market borrowing across the developed and emerging market economies (Table 1).

Although the debt management strategy shall be using variety of instruments for successful completion of market borrowing programme, it has largely relied on fixed rate nominal bonds. One variant of IIBs, 5 year Capital Index Bond (CIB) was issued on December 29, 1997 wherein only the principal repayment at the time of redemption was indexed to inflation. The response to the issue was, however, subdued as interest payment was not protected against inflation.

It is known fact that SLR requirement for banks and requirement of some minimum investment in G-Sec for insurance companies and provident funds provides significant captive demand for G-Sec. In view of market borrowing at elevated level, debt management strategy should continuously strive to broaden the investors' base, especially to tackle with the eventuality of decline in captive demand for G-Sec. Towards this end, based on the past experience, feedback from market participants and learning from international experiences, a new version of IIB has been designed with an inherent protection from inflation to both interest payment and principal repayment. The main features are:

i) Principal would be indexed to inflation (index ratio);

ii) Coupon will be paid on the indexed principal;

iii) Higher of the adjusted principal or the face value will be paid at redemption; and

iv) Wholesale Price Index (WPI) will be used for indexation of principal.

The Reserve Bank launched this product by the name of Inflation Indexed Government Stock and the first auction for ₹10 billion was conducted on June 4, 2013. Besides helping the government market borrowing, this product may also have host of other benefits. The issuance of IIBs may improve credibility of the public policy towards price stability. Long-term funding is always fraught with inflation risk that could be obviated by borrowing through inflation linked instruments. It would provide a benchmark for the private sector and banks, facilitating them to raise long-term resources through inflation linked instruments. Therefore, this product may be a great catalyst for infrastructure funding. It would also enable improved gauging of inflationary expectations that is critical for monetary policy formulation. The investment of financial savings in gold by people for inflation hedging may come down and help balance of payments of the country.

Non-competitive portion has been earmarked up to 20 per cent of the notified amount to encourage retail participation. Some demand from institutional investors such as insurance companies, pension funds, provident funds, *etc.* is also expected to the extent their payouts are linked to inflation. Banks may also like to invest in this product depending upon the tenor as it could facilitate them to raise long-term deposits.

Table 1: Composition of Domestic Bonds issued by Central Government: Cross Country
(as % of outstanding) (As at end 2011)

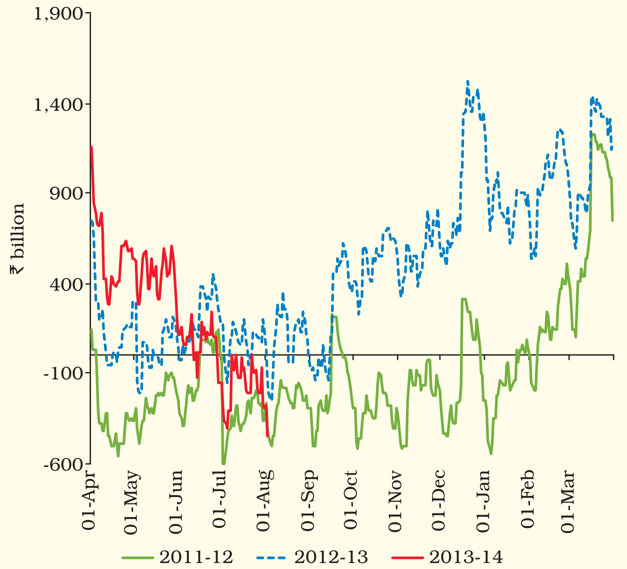
Country	Floating Rate	Fixed Rate	Inflation Indexed	Exchange Rate linked	Others
1	2	3	4	5	6
Argentina	14.8	0.8	49.2	34.6	0.7
Brazil	31.9	37.5	30.0	0.6	0.0
Chile	0.0	19.2	80.8	0.0	0.0
India	2.4	97.6	0.0	0.0	0.0
Indonesia	22.2	77.8	0.0	0.0	0.0
Canada	0.0	92.5	7.5	0.0	0.0
South Africa	11.6	70.8	17.6	0.0	0.0
Mexico	41.4	36.6	22.1	0.0	0.0
Germany	10.9	85.8	2.9	0.4	0.0
UK	0.0	77.6	22.4	0.0	0.0
USA	0.0	91.2	8.8	0.0	0.0

Source: Bank for International Settlements (BIS).

Thereafter GoI has availed WMA for 12 occasions before recording positive balance from September 15, 2012 till March 31, 2013. During the year, the Government of India was in WMA for 40 days and did not avail OD as compared with WMA for 263 days and OD on 70 days in the previous year.

VII.9 The limits for WMA for the first half of the financial year 2012-13 were set at ₹500 billion for first quarter and ₹450 billion for the second quarter. The limit for WMA for the second half was fixed at ₹200 billion. The same for the first half of the financial year 2013-14 has been fixed at ₹300 billion. During the current financial year (2013-14),

Chart VII.1: Cash Balance of the Central Government



GoI was in WMA for 27 days and availed OD for 4 days as on August 5, 2013.

DEBT MANAGEMENT OF STATE GOVERNMENTS

Market Borrowings

VII.10 The net allocation under the market borrowing programme for state governments for 2012-13 was placed at ₹1,881 billion. Taking into account the repayments of ₹306 billion, the gross allocation amounted to ₹2,187 billion, while gross sanctions under Article 293(3) amounted to ₹1,861 billion. The 28 state governments raised a gross amount of ₹1,773 billion (net ₹1,467 billion) in 2012-13 as against ₹1,586 billion (net ₹1,366 billion) raised by 26 states in the previous year (Table VII.4). Odisha Government did not participate in the market borrowing programme in 2012-13 as against Assam, Odisha and Chhattisgarh in 2011-12. Eleven States did not raise their full sanctions in 2012-13 as against 14 States in 2011-12.The outstanding stock of the SDLs and power bonds stood at ₹8874 billion at the end of March 2013 (Table VII.5).

Table VII.4: States' Market Borrowings

(₹ billion)

Item	2011-12	2012-13	2013-14 (till Aug 5, 2013)
1	2	3	4
Net Allocation	1,459	1,881	-
Additional Allocation	157	0	0
Maturities during the year	220	306	291.84
Gross Allocation	1,835	2,187	-
Gross Sanctions under Article 293 (3)	1,634	1,861	832.95
Gross Amount Raised during the Year	1,586	1,773	481.31
Net Amount Raised during the Year	1,366	1,467	189.47
Balance to be raised against GoI Sanctions	48	89	351.64
Amount Raised during the year as a % of Total Sanctions	97.09	95.22	-
SDLs outstanding (at the end period)	7,424	9,291	-

VII.11 The weighted average yield firmed up to 8.84 per cent (2012-13) from 8.79 per cent during the previous year (2011-12) as the weighted average spread for SDL issuances, over the corresponding GoI security, has increased to 71 bps compared to 44 bps over the previous year.

Table VII.5: Residual Maturity Profile of Outstanding State Development Loans and Power Bonds (as at end-March 2013)

(₹ billion)

Year of Maturity	State Development Loans	Power Bonds	Total
1	2	3	4
2013-14	321	29	350
2014-15	334	29	363
2015-16	352	29	381
2016-17	315	14	329
2017-18	678	0	678
2018-19	1,181	0	1,181
2019-20	1,306	0	1,306
2020-21	1,045	0	1,045
2021-22	1,586	0	1,586
2022-23	1,654	0	1,654
Total	**8,772**	**101**	**8,873**

Table VII.6: Utilisation of WMA/OD and Investment of State Governments@
(Average monthly outstanding)

(₹ billion)

Months	Special WMA			Normal WMA			Overdraft			Total		
	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14
1	2	3	4	5	6	7	8	9	10	11	12	13
April	10.0	5.0	0.8	7.0	4.0	3.0	9.0	3.0	2.0	26.0	12.0	5.8
May	6.0	1.0	0.6	1.0	0.3	1.3	0.4	0.0	0.2	7.4	1.4	2.1
June	2.0	0.6	5.8	3.0	2.0	5.3	0.1	0.2	2.1	5.1	2.8	13.2
July	1.0	2.0	1.9	1.0	2.0	2.9	0.0	0.8	0.6	2.0	4.8	5.4
August	2.0	0.6	4.0	3.0	1.0	0.4	0.0	0.3	0.0	5.0	1.9	4.5
Sept	1.0	4.0		2.0	4.0		0.1	2.0		3.1	10.0	
Oct	1.0	5.0		2.0	4.0		0.1	1.0		3.1	10.0	
Nov	5.0	5.0		2.0	4.0		0.0	1.0		7.0	10.0	
Dec	3.0	4.0		1.0	4.0		0.1	2.0		4.1	10.0	
Jan	3.0	0.6		1.0	1.0		0.0	0.1		4.0	1.7	
Feb	0.5	0.1		1.0	3.0		0.0	2.0		1.5	5.1	
Mar	0.2	0.9		1.0	1.6		0.3	4.9		1.5	0.0	

@ : Upto August 5, 2013.

Cash Management

VII.12 The aggregate Normal WMA limit for States, including the union territory of Puducherry, was placed at ₹102 billion for 2012-13, which was same as in the previous year. The rates of interest on Normal and Special WMA and OD continued to be linked to the repo rate. The monthly average utilisation of WMA and OD by all the States in 2012-13 was higher than 2011-12 for July, September-December and February (Table VII.6). During 2013-14 (thus far), 5 states have availed of overdrafts (Table VII.7).

VII.13 The surplus cash balances of state governments are automatically invested in 14-day Intermediate Treasury Bills (ITBs), the discount rate of which is presently fixed at 5 per cent. The average investment in 14-day ITBs increased from ₹722 billion during 2011-12 to ₹849 billion in 2012-13 (Table VII.8). The outstanding investments in ITBs stood at ₹1,181 billion as at end-March 2013 as

Table VII.7: No. of Days States Availed of Special/ Normal WMA and OD@

State	Special WMA			Normal WMA			Overdraft		
	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14
1	2	3	4	5	6	7	8	9	10
Haryana	23	13	2	22	12	1	6	5	0
Nagaland	41	193	76	20	139	56	0	34	35
Punjab	177	233	74	177	232	74	26	139	37
West Bengal	185	134	38	59	48	15	28	13	9
Maharashtra	0	7	0	0	0	0	0	0	0
Manipur	0	98	12	0	81	8	0	30	8
Mizoram	15	7	64	1	3	31	0	0	5
Uttarakhand	57	2	0	15	0	0	0	0	0
Jharkhand	5	14	8	4	14	8	0	0	0
Jammu & Kashmir	0	0	0	136	136	23	5	11	0
Meghalaya	-	-	5	-	-	1	-	-	0
Himachal Pradesh	-	-	0	-	-	12	-	-	0
Uttar Pradesh	-	-	1	-	-	-	-	-	0

@ : Upto August 5, 2013.

Table VII.8: Investments in ITBs and ATBs by State Governments/UTs@

(₹billion)

Month	Investment in ATBs			Investment in ITBs			Total		
	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14
1	2	3	4	5	6	7	8	9	10
April	108.6	231.6	317.40	864.1	863.1	1002.31	972.7	1094.7	1319.71
May	145.3	327.6	378.40	728.1	768.2	913.99	873.4	1095.8	1292.39
June	249.8	415.9	549.03	677.9	681.6	729.45	927.7	1097.5	1278.48
July	326.4	440.6	672.28	613.9	654.9	609.91	940.3	1095.5	1282.19
August	329.6	450.3	721.82	645.2	756.3	646.58	974.8	1206.6	1368.40
September	327.6	505.5		615.4	707.9		943.0	1213.4	
October	297.2	521.9		613.7	748.8		910.9	1270.7	
November	267.9	496.1		667.1	844.0		935.0	1340.1	
December	240.2	523.8		762.0	875.7		1002.2	1399.5	
January	326.3	546.6		717.1	912.2		1043.4	1458.8	
February	381.7	498.9		774.5	1088.8		1156.2	1587.7	
March	329.5	337.2		986.5	1295.5		1316.0	1632.7	
Average	276.5	441.0		722.1	848.9		998.6	1289.9	

@ : Upto August 5, 2013.

against ₹966 billion as at end-March 2012. The weekly average investment of the state governments in Auction Treasury Bills (ATBs) increased to ₹441 billion from ₹277 billion in the previous year. The outstanding investment in ATBs as at end-March 2013 stood at ₹286 billion was higher than ₹220 billion at end-March 2012.

VII.14 The Reserve Bank, on behalf of the state governments, maintains the consolidated sinking fund (CSF) that provides a cushion for amortisation of market borrowing/liabilities and the guarantee redemption fund (GRF), which provides for the servicing of contingent liability arising from invocation of guarantees issued in respect of borrowings by state level undertakings or other bodies (As on March 31, 2013, as many as 21 State Governments had subscribed to CSF and 11 States had subscribed to GRF). The outstanding investments under CSF and GRF amounted to ₹485 billion and ₹44 billion, respectively, as at end-March 2013.

VII.15 The report of the Committee to assess the feasibility of introducing more long-term fixed interest rate loan products by banks (Chairman: Shri K.K. Vohra) was placed on the Reserve Bank's website on January 22, 2013. Major recommendations included issuance of long-term bonds (minimum maturity of 5 years) to the extent of their exposure to the infrastructure sector by banks, popularising the fixed deposit schemes with tenors of above 5 years as the same are eligible for tax exemption and offering longer-tenor fixed rate loans by banks (say up to 30 years) which would help reduce the EMIs of the borrowers.