Government Securities

For Prelims: Government Securities, Reserve Bank of India (RBI)**,** Fiscal Deficit, Treasury Bills (T-bills), **Open Market Operations.**

For Mains: Government Securities, Indian Economy and issues relating to planning, mobilisation of resources, growth, development and employment.

Source: TH

Why in News?

The government has completed **Government Securities (G-Sec)** borrowing for the **current fiscal 2023-24** and it expects a dividend from the **Reserve Bank of India (RBI)** in Financial Year 25 (FR 25), similar to FY 24.

- The government's approach to borrowing remains cautious, focusing on prudent fiscal management and ensuring borrowing aligns with the actual needs.
- The completion of G-Sec borrowing, coupled with expectations for dividend income from the RBI, reflects efforts to maintain fiscal stability and meet expenditure targets.

What are the Rules Under Which RBI Transfers its Surplus to the Government?

- The RBI transfers its surplus to the government in accordance with **Section 47 (Allocation of Surplus Profits) of the Reserve Bank of India Act, 1934.**
    - A technical **committee** of the RBI Board **headed by Y H Malegam (2013),** which reviewed the adequacy of reserves and surplus distribution policy, recommended a higher transfer to the government.
- According to this section, after making provisions for **reserves and retained earnings**, the **RBI transfers the surplus to the government.**
- The amount transferred is determined based on various factors, **including the RBI's income from sources** such as interest on holdings of domestic and foreign securities, fees and commissions from its services, profits from foreign exchange transactions, and returns from subsidiaries and associates.
    - On the expenditure side, the R**BI incurs costs such as printing of currency notes,** payment of interest on deposits and borrowings, salaries and pensions of staff, operational expenses of offices and branches, as well as provisions for **contingencies and depreciation.**

What are Government Securities (G-Sec)?

- **About:**

    - A G-Sec is a tradable instrument issued by the **Central Government or the State Governments.**
    - A G-Sec is a type of **debt instrument** issued by the government to borrow money from the public to finance its **Fiscal Deficit**.
        - A debt instrument is a financial instrument that represents a **contractual obligation by the issuer to pay the holder a fixed amount of money,** known as principal or face value, on a specified date.
    - It acknowledges the **Government's debt obligation.**
        - Such securities are **short-term** (usually called treasury bills, with original maturities of less than one year- presently issued in three tenors, namely, 91-day, 182 days and 364 days) **or long-term** (usually called **Government bonds or dated securities** with original maturity of one year or more).
    - In India, the Central Government issues both, **treasury bills and bonds or dated securities** while the **State Governments issue only bonds** or dated securities, which are called the **State Development Loans (SDLs).**
    - **G-Secs carry practically no risk of default** and, hence, are called **risk-free gilt-edged instruments.**
        - Gilt-edged securities are **high-grade investment bonds offered by governments** and large corporations as a means of borrowing funds.
- **Types of G-Sec:**
    - **Treasury Bills (T-bills):**
        - Treasury bills are **zero coupon securities and pay no interest.** Instead, they are **issued at a discount and redeemed at the face value** at maturity.
    - **Cash Management Bills (CMBs):**
        - In 2010, the Government of India, in consultation with RBI introduced a **new short-term instrument, known as CMBs,** to meet the temporary mismatches in the cash flow of the Government of India.
            - The CMBs have the generic character of T-bills but are issued for maturities of less than 91 days.
    - **Dated G-Secs:**
        - Dated G-Secs are securities that **carry a fixed or floating coupon rate (interest rate)** which is paid on the face value, on a half-yearly basis. Generally, the tenor of dated securities ranges **from 5 years to 40 years.**
    - **State Development Loans (SDLs):**
        - State Governments also **raise loans from the market** which are called SDLs. SDLs are **dated securities issued through normal auctions** similar to the auctions conducted for dated securities issued by the Central Government.
- **Issue Mechanism:**
    - The RBI conducts **Open Market Operations (OMOs)** for sale or purchase of G-secs to adjust money supply conditions.
        - The RBI sells g-secs to remove liquidity from the market and buys back g-secs to infuse liquidity into the market.
    - These operations are **often conducted on a day-to-day basis** in a manner that balances inflation while helping banks continue to lend.
    - RBI carries out the OMO through commercial banks and does not directly deal with the public.
    - The RBI uses **OMO along with other monetary policy tools** such as **repo rate, cash reserve ratio and statutory liquidity ratio** to adjust the quantum and price of money in the system.

Retail Sale and Purchase of T Bills

- **Method of Purchase:** Retail investors can open an online Retail Direct Gilt (RDG) **Account with the Reserve Bank of India (RBI)** to directly purchase T-bills. Additionally, they can place bids via select banks and registered primary agents.
- **Portal for Purchase**: The **Retail Direct Gilt (RDG)** platform provided by RBI facilitates the purchase of T-bills for retail investors.
- **Rules Regarding Purchase and Sale:** Retail investors must adhere to certain rules and regulations when buying and selling T-bills. This includes meeting the minimum **investment**

amount requirement (INR 10,000 per lot for various durations)** and ensuring compliance with RBI guidelines.
- **Participation in Primary Market:** Retail investors can **participate in the primary market** by placing bids for T-bills through the designated channels mentioned earlier. This allows them to directly purchase newly issued T-bills from the RBI on behalf of the Government of India.
- **Participation in Secondary Market:** Retail investors can **also participate in the secondary market for T-bills through their demat accounts.** In the secondary market, investors can buy and sell T-bills before their maturity dates, providing liquidity and opportunities for trading.

UPSC Civil Services Examination, Previous Year Question (PYQ)

Q. In the context of Indian economy, 'Open Market Operations' refers to (2013)

(a) borrowing by scheduled banks from the RBI
(b) lending by commercial banks to industry and trade
(c) purchase and sale of government securities by the RBI
(d) None of the above

Ans: (c)

Q.2 In the context of the Indian economy, non-financial debt includes which of the following? (2020)

1. Housing loans owed by households
2. Amounts outstanding on credit cards
3. Treasury bills

Select the correct answer using the code given below:

(a) 1 only
(b) 1 and 2 only
(c) 3 only
(d) 1, 2 and 3

Ans: (d)

- Debts are contractual obligations to repay monetary loans, often with related interest expenses.
- Non-financial Debt
  - It consists of credit instruments issued by governmental entities, households and businesses that are not included in the financial sector.
  - It includes industrial or commercial loans, Treasury bills and credit card balances.
  - They share most of the same characteristics with financial debt, except the issuers are non-financial. Hence, statements 1, 2 and 3 are correct.
- Therefore, option (d) is the correct answer.

Q.3 Consider the following statements: (2018)

1. The Reserve Bank of India manages and services Government of India Securities but not any State Government Securities.
2. Treasury bills are issued by the Government of India and there are no treasury bills issued by the State Governments.
3. Treasury bills offer are issued at a discount from the par value.

Which of the statements given above is/are correct?

(a) 1 and 2 only
(b) 3 only
(c) 2 and 3 only
(d) 1, 2 and 3

Ans: (c)