

G-sec Acquisition Programme 2.0

Why in News

Recently, the <u>Reserve Bank of India (RBI)</u> has announced that it will conduct an <u>open market</u> <u>purchase</u> of government securities of Rs 25,000 crore under the G-sec Acquisition Programme (G-SAP 2.0).

■ Earlier, under **G-SAP 1.0,** the first purchase of government securities for an aggregate amount of Rs. 25,000 crore was made.

Key Points

- Government Securities Acquisition Programme (G-SAP):
 - About: The G-Sec Acquisition Programme (G-SAP) is basically an unconditional and a structured Open Market Operation (OMO), of a much larger scale and size.
 - RBI has called the G-SAP as an OMO with a 'distinct character'.
 - The word 'unconditional' here connotes that RBI has committed upfront that it will buy G-Secs irrespective of the market sentiment.
 - Objective: To achieve a stable and orderly evolution of the yield curve along with management of liquidity in the economy.
 - Significance: The government will mainly benefit from the G-SAP.
 - By purchasing G-secs, the RBI infuses money supply into the economy which inturn keeps the yield down and lower the borrowing cost of the Government.
 - The government of India, with its massive borrowing programme (for example, <u>National infrastructure pipeline project</u>), can now breathe a sigh of relief as long-term borrowing costs come down.
 - Issues: Critics of the G-SAP say that the rupee might get adversely affected.
 - They are of the view that the G-SAP announcement has already led to depreciation of the rupee (a fall in the value of currency).
 - So, critics are pointing to the fact that there is a trade-off between a tumbling rupee and lower borrowing costs/low yields.
 - Further, too much liquidity will **drive up** inflation.
- Open Market Operations:
 - Open Market Operations (OMO) is one of the <u>quantitative</u> (to regulate or control the <u>total volume of money</u>) monetary <u>policy tools</u> which is employed by the central bank of a country to control the money supply in the economy.
 - OMOs are conducted by the RBI by way of sale or purchase of government securities (g-secs) to adjust money supply conditions.
 - The central bank sells g-secs to remove liquidity from the system and buys back g-secs to infuse liquidity into the system.
 - 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.

Government Securities:

- A G-Sec is a **tradable instrument** issued by the Central Government or the State Governments.
- 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 day and 364 day) 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.

Yield Curve

- Bond yield is the return an investor realizes on a bond.
- The mathematical formula for calculating yield is the annual coupon rate (interest rate promised by the bond issuer) divided by the current market price of the bond.
- Movements in yields depend on trends in interest rates, it can result in capital gains or losses for investors.
 - A rise in bond yields in the market will bring the price of the bond down.
 - A drop in bond yield would benefit the investor as the price of the bond will rise, generating capital gains.
- A yield curve is a line that plots yields (interest rates) of bonds having equal credit quality but differing maturity dates.
- The slope of the yield curve gives an idea of future interest rate changes and economic activity.

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