Draft Norms Lending and Borrowing of G-secs

Prelims: Government Securities Lending Directions, 2023, Repo transactions, Fiscal Deficit, Open Market Operations.
Mains: Draft Norms Lending and Borrowing of G-secs.

Why in News?

Recently, the Reserve Bank of India released **Draft Reserve Bank of India (Government Securities Lending) Directions, 2023.**

- The RBI proposed introduction of securities lending and borrowing in Government Securities (G-sec) with an aim to **facilitate wider participation in the securities lending market** by providing investors an avenue to deploy idle securities and enhance portfolio returns.

What are the Draft Norms?

- **Government Securities Lending (GSL)** transactions **shall be undertaken for a minimum period of one day** and **a maximum of 90 days.**
- Government Securities issued by the central government **excluding Treasury Bills** would be eligible for lending/borrowing under a GSL transaction.
- Government securities issued by the Central government (including Treasury Bills) and the state governments would be **eligible for placing as collateral under a GSL transaction.**
- An entity eligible to undertake **repo transactions** in government securities, and any other entity approved by the Reserve Bank would be eligible to participate in GSL transactions as lender of securities.

What are Government Securities?

- **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 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.

What are the 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, 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 less than 91 days.
- **Dated G-Secs:**
    - Dated G-Secs are securities which carry a fixed or floating coupon (interest rate) which is paid on the face value, on 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 auction 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 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.

UPSC Civil Services Examination, Previous Year Question (PYQ)

Q. 1 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)

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