

## Chapter 7

### Government Securities Market

#### 7.1 Introduction

One of the objectives of Public Debt Management is to develop a liquid market. Developing a liquid and vibrant secondary market for government securities and broadening the investor base are the key factors to ensure that debt is raised in a cost effective manner. Further, the government securities market provides the benchmark yield and imparts liquidity to other financial markets and is considered an essential precursor, in particular, for development of the corporate debt market. Moreover, government securities market acts as a channel for integration of various segments of the domestic financial market and helps in establishing inter linkages between the domestic and external financial markets.

#### 7.2 RBI Holding of Government Securities

In terms of the FRBM Act, 2003, RBI was not allowed to subscribe to the primary issuance of the Government from April 2006 while they were allowed to buy and sell government securities in the secondary market. In practice, RBI purchases and sells government securities through Open Market Operations (OMOs) to infuse or absorb liquidity for monetary operations and to adjust the monetary base and/or the interest rate in line with their targets. The OMOs may also result in infusing liquidity to support the banking sector's purchases of government bonds. Audit observed that during the period 2009-10 to 2014-15, the holdings of Government securities by Commercial Banks, Life Insurance Companies and RBI together ranged between 77.65 to 82.09 *per cent* of the outstanding dated securities as shown in the **Table 7.1** below:

**Table 7.1: Major Holders of Government Securities**

*(In per cent)*

Category	2010 March	2011 March	2012 March	2013 March	2014 March	2015 March
<b>Commercial Banks (including Bank PDs)</b>	47.25	47.03	46.11	43.86	44.46	43.30
<b>Insurance companies</b>	22.16	22.22	21.08	18.56	19.54	20.87
<b>RBI</b>	11.76	12.84	14.41	16.99	16.05	13.48
<b>Total</b>	<b>81.17</b>	<b>82.09</b>	<b>81.6</b>	<b>79.41</b>	<b>80.05</b>	<b>77.65</b>

*(Source: Status Paper January 2016)*

From the above, it can also be seen that RBI's holding of Government securities had increased from 11.76 *per cent* of dated securities in March 2010 to 16.99 *per cent* in March 2013 before declining to 13.48 *per cent* in March 2015.

### **7.3 Concentrated Trading in a Few Securities**

The total annual trading (outright) in government securities had increased from ₹ 24,80,850 crore to ₹ 91,49,608 crore over the period from 2009-10 to 2014-15 indicating a 268.81 *per cent* increase. The details of the total dated government securities outstanding, total quarterly trade in dated Government securities, trade in top three and 10 dated Government securities has been presented in **Annexure-III**.

It was observed that though the trading volume of government securities had increased nearly threefold, trade in government securities in the secondary market was predominantly taking place in a few securities as can be seen from the **Annexure-III**. Thus, objective of developing a deep and liquid market did not appear to have been fully achieved.

RBI in their reply stated (August 2015) that they were committed to development of the government securities market and focused on market development along with cost minimisation and risk mitigation while adding that Indian government securities market was reasonably deep and liquid as evidenced by some measures of liquidity like average trading volumes, turnover ratio, bid-ask spread, impact cost etc. RBI further enumerated the steps taken by them for the development of the government securities markets in India and added that they would continue efforts to further develop liquidity in government securities market.

### **7.4 Retail Participation in Government Securities Market**

In order to encourage participation of medium and small investors in the primary market for government securities, a scheme of non-competitive bidding for allocation of upto 5 *per cent* of the notified amount in the specified auctions of dated securities at weighted average rate of accepted bids was introduced in January 2002. The participation of retail investors in the auction of dated securities during 2009-10 to 2014-15 is presented in **Annexure-IV**.

Audit observed that the total amount of bids received and accepted in respect of retail investors during 2009-10 to 2014-15, ranged from 0.30 *per cent* to 0.47 *per cent* of the notified amount as can be seen in **Annexure-IV**. From the above, it appeared that the steps taken by RBI and the Government for improving retail participation in government securities market were not producing the desired results.

RBI in their reply (August 2015) enumerated the steps taken to promote retail participation and stated that retail participation in government securities market, even though low, had been increasing gradually over the years. RBI added that they were continuously exploring possibility of making the system more investor friendly and that recent steps taken to enable seamless transfer of securities from de-mat to Subsidiary General Ledger may increase the retail participation.

In the Exit Conference, DEA accepted the audit observation and stated that steps would be taken to improve the position.

### **7.5 Participation of Foreign Institutional Investors (FIIs) in Government Security Market**

Foreign investment in rupee denominated government securities takes the form of foreign investors buying Government bonds in the Indian Government bond market, all of which are denominated in rupees. The percentage of foreign investment in outstanding government securities during the period 2009-10 to 2014-15 ranged from 0.59 *per cent* to 3.67 *per cent*. The limits on foreign investment in government debt and the minimum and maximum foreign investment in government debt during the years 2013-14 and 2014-15 are presented in **Table 7.2** below:

**Table 7.2: Minimum and Maximum Foreign Investment in Government Debt**

(₹ in crore)

	<b>2013 – 14 (upto 11 June 2013)</b>	<b>2013 – 14 (from 12 June 2013)</b>	<b>2014 - 15</b>
<b>Ceiling Limit</b>	1,24,432	1,53,569	1,53,569
<b>Minimum Investment</b>	79,906	53,491.95	81,795
<b>Maximum Investment</b>	96,392	88,078.5	1,53,387

As can be seen from the above, the holdings of the FIIs in government securities during 2013-14 were considerably less than the limits prescribed for them, while it seemed to have improved considerably during 2014-15.

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RBI in their reply stated (August 2015) that there was robust demand from FIIs for government securities and the limits were fully utilized. RBI added that there was a demand from various quarters to further open up the limits and that they had taken measures to improve the participation of FIIs in government securities market.

RBI may continue to take steps to ensure that the participation of FIIs in the Indian government securities market is maintained.