India's Gilt-edged Market

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Abstract

The term gilt-edged means of the best quality. It refers to the market of government securities as they do not suffer from the risk of default. Besides, government securities are highly liquid, as they can be easily sold in the market at their going market price. The open market operations of the RBI are also conducted in government securities. It is spelled out that India's Gild-edged market is monopoly of RBI and not like advanced countries namely USA, UK and Canada, but it is not the fact.
KEYWORDS: RBI, Gild-edged market, Government securities.

Introduction:

The marketable debt issued by the government and semi-government bodies which represents a claim on the government is called government securities. It is also called as gilt-edged security. Treasury bills and bonds are the example of government securities. The gilt-edged market is the market in government securities. Thus, government securities are a unique and important financial instruments in the financial market of any country.

Problem of the study:-

One special feature of India's gilt-edged market as distinguished from markets of USA, the UK and Canada is that in India, RBI is the sole dealer in government securities, in the above mention countries, this is not the case. And do the government securities ensure safety of both capital and Income?

Objectives of the study:-

1) To study how securities guaranteed by the government.
2) To examine a large statutory borrowing is from the RBI
3) To study how RBI provide finance to government to meet fiscal deficit.

Significance of the study:-

This study points out that the India's gilt-edged market in government securities is significant part of the stock market in India. The government securities also plays important role in the Indian debt market (both in terms of outstanding stock as well as turnover) RBI is in a position to advise the government about the appropriate timing of debt issue.

Scope of the study:-

The gilt-edged market is dominated by financial institutions. They constitute the 'Captive market' for government securities. As the total liabilities of these institution grow, the captive demand for government securities also grows, that generate employment.

The research study:-

Investopedia explains that 'Gilt-Edged Securities' are a high-grade investment with very low risk Typically, these are issued by blue chip companies that dependably meet dividend or interest payments because they are well- established and financially stable. Usually High-grade bonds that are issued by a government or firm. This type of security originally boasted gilded edges, thus the named as Gilt-edged security. In the case of a firm, a gilt-edged security is a stock or bond issued by a company that has a strong record of consistent earnings and can be relied on to cover dividends and interest.

The Government securities comprise dated securities issued by the Government of India and state governments as also, treasury bills issued by the Government of India. Reserve Bank of India manages and services these securities through its public debt offices located in various places as an agent of the Government.

The gilts-edged market is the market in government Securities or the securities guaranteed (as to both principal and interest) by the government. The former include securities of the Government of India and of the State Government. The latter are securities issued by local authorities (like City Corporations, Municipalities, and Port Trusts) and autonomous government undertaking like Development Banks, State Electricity Boards, etc.

Government securities have become a very important component of capital market in several countries. In India, they have gained importance since 1954-55 as the pressure for raising funds to finance public sector projects under five year plans built up. The total amount outstanding of the internal government debt in the form of market loans, special bonds and treasury bills was about Rs. 151,000 crores at the end of March 1991 and Rs. 275,000 crores at the end of March 1995. Dring 1990-91 alone, this debt had increased by about Rs. 18000 crores.

The gilt-edged market may be divided in two parts: The Treasury Bill Market and the Government Bond Market. On the borrower side, The RBI manages entirely the public debt operations of the central as well as state governments.

On the demand side, the gilt-edged market is dominated by financial institutions. Apart from the RBI, the major holders are commercial banks, insurance companies, provident fund, and trust funds. These financial intermediaries mobilize savings of the public and through their investment in government securities transfer these savings to government. They constitute what is called the 'captive market' for government securities, as they are required statutorily to hold certain minimum, proportions of their total liabilities (assets) in government securities. Therefore, as the total liabilities of these institutions grow, the 'captive' demand for government securities also grows. Besides these financial institutions, local authorities, semi-government securities from non-financial companies and individuals is negligible.

Due to the special features of India's gilt-edged market spelled out above, namely, the monopoly- dealer position of the RBI and the 'captive' nature of the demand for government securities, the prices of such securities are not formed freely in the market. Instead, they are very much under the direct control of the RBI. One main reason for the virtual absence of non-captive buyers from this market is that the rate of interest on government bonds has been kept artificially low-much lower than the rates of interest available on other financial assets such as fixed deposits with banks and post offices, with a much shorter maturity of five years and fiscal (income-tax) concessions, which have boosted up the effective rates of interest on them for income tax payers.

Some important points related to government securities market are as follows:

(i) Government securities are a unique and important financial instruments in the financial market.

(ii) Its issues are helpful in implementing the fiscal policy of the government.

(iii) As government security is a claim on the government, it is an absolutely secure financial instrument, which guarantees the certainly of both income and capital.

(vi) These securities are normally issued in the denomination of Rs. 100 or 1000. The face value, which used to be 100 till the middle of the 1980s was raised to 1000 in the recent past. The rate of interest on these securities is relatively lower because of their being liquid and safe.

(v) The most active participation in the government securities market is of the banking and corporate sector. They purchase and sell large quantities of government securities. Apart from these two sectors, government selling is extremely limited.

(vi) The role of brokers in marketing government securities is also limited.

(vii) The interest on government securities is payable half yearly. Interest in respect of Central and State government securities, along with income in the form of interest or dividends on other approved investments, is exempt from income tax subject to a limit. The value of investments in these securities and other investments specified in the Wealth Tax Act, 1957 is exempt from wealth tax up to a limit. As individuals do not normally invest in these securities, saving in tax liability does not seem to be an important motivation behind investment in them.

(viii) There are three forms of Central and State government securities (a) Inscribed Stock or Stock Certificate (SC), (b) Promissory Note (PN), (c) Bearer Bond. While these days, bearer bonds are not usually issued in India.

(ix) RBI deals in these securities only through a very limited number of brokers approved by it. As a result the role of brokers and dealers in marketing government securities in India is highly limited. Banks can directly approach RBI for these securities. The agency of dealer-bank is more active than individual dealers.

(x) The gilt-edged market is an ‘over the counter’ market and each sale and purchase has to be negotiated separately.

(xi) The gilt-edged market is basically limited to institutional investors.

A new development has taken place when the RBI announced in November 1995, the appointment of primary dealers in government securities to strengthen the securities market infrastructure and bring about an improvement is secondary market trading, liquidity and turnover and induce wider holding of government securities amongst a wider investor base.

Conclusion:

RBI holds a pivotal position in the gilt-edged market being always present in the market as seller of these securities and buying them generally in switch operations and sometimes for cash.

Issue of government securities is a convenient and flexible method of raising long term finance for the exchequer at very moderate interest costs. Since 1992, several important changes have come about in the gilt-edged market that the auction sale of treasury bills of 91 days and 164 days which has resulted in a substantial rise in the short term rate of interest.

Now Securities trading Corporation of India has been constituted in May, 1994 for developing and promoting secondary market for Government securities.

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