H2 FY2021 revised borrowing calendar: Putting uncertainty at bay

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- **The Finance ministry in a press release late last night announced that the borrowing under Option 1 (of the GST compensation cess fund) through a Special Window will be conducted by the Government of India (rather than individual state governments)**
- **This is expected to put the uncertainties around treatment of GST compensation cess fund and risk of higher central government borrowing announcements later in the year, to an end**
- **The fact that the weekly auction size would see reduction, along with lower weekly supply in duration (given the extension to mid-March), would be a positive. The 3-year, 5-year segment, would see higher supply and could lead to some bear flattening in the curve, though surplus liquidity could aid in putting a cap on yields**
- **The overall general government borrowing expectations do not change with this announcement as it is a transfer from state to central borrowings. Overall we expect gross general government borrowing of ~12% of GDP for the fiscal with H2 borrowing of ~INR 11 tn**
- **In terms of funding the fiscal deficit, while upside risks to further slippage remain (with our estimates for central government fiscal deficit at ~8-8.5% of GDP), this deficit could be funded by higher reliance on other sources of funding**

Settling the uncertainty around the GST compensation cess fund, the Finance ministry in a press release late last night announced that the borrowing under Option 1 of INR 1.1 tn (for the GST compensation cess fund), through a Special Window will be conducted by the Government of India (rather than individual state governments) in appropriate tranches. The borrowed amount will be passed on to "the States as a back-to-back loan in lieu of GST Compensation Cess releases" and is being done to ease administrative difficulties and differential interest rates through SDLs done by individual states.

While this communique is a reversal from the one announced earlier in the week in which the State Governments that had opted for Option 1 were being allowed to borrow an additional INR ~688 bn through SDLs, nevertheless it marks the end of the uncertainty that was being brought about through the ongoing embargo. This would lead the central government borrowing for the full fiscal at INR 13.1 tn vs. INR 12 tn earlier.

Internals of the new borrowing program which take central government H2 borrowing to INR 5.44 tn (from the earlier announced calendar of INR 4.34) could lead to a lower weekly supply of ~INR 240-250 bn vs. ~INR 270-280 bn, as the program is now being extended till mid-March vs. the earlier calendar ending in the last week of January.

Moreover, the distribution of the borrowing calendar across tenors indicates lower weekly supply of duration (given the extension to mid-March), with the incremental new borrowing of INR 1.1 tn being split equally between 3-year and 5-year paper. This could lead to some bear flattening, but the surplus liquidity in the system, could aid in capping the upside in yields in these segments.

Borrowing calendar for H2 FY 2021 (INR bn)

Tenors	Old borrowing	% share	Revised borrowing	Absolute change	Borrowing YTD*	% Share
2 years	240	5.5	240	0	30.0	0.6
3 years	-	-	550	550		0.0
5 years	640	14.7	1190	550	80.0	1.5
10 years	970	22.4	970	0	130.0	2.4
14 years	960	22.1	960	0	120.0	2.2
30 years	570	13.1	570	0	80.0	1.5
40 years	720	16.6	720	0	90.0	1.7
Floating rate bonds	240	5.5	240	0	30.0	0.6
Total Borrowing*	**4340**	**100**	**5440**	**1100**	**560**	**10.3**

* includes green shoe of INR 34 bn

Source: Ministry of finance, RBI, ICICI Bank Research

The other previously announced borrowing calendars of the state governments and t-bills calendar remain unchanged.

With this announcement we think that any risks of additional central borrowing announcements towards the end of the year, are at bay, which could also aid sentiment in the long end. In terms of funding the fiscal deficit, while upside risks to further slippage remain (with our estimates for central government fiscal deficit at ~8-8.5% of GDP), this deficit could be funded by higher reliance on other sources of funding – including external finances, cash drawdowns, short-term borrowing, and NSSF contributions. Accumulation in the NSSF fund is ~INR 950 bn (FYTD August 2020), which is slightly higher than the accumulation seen during the same time last fiscal. With higher differential interest rates in small savings instruments compared to other sources, as well as continued proclivity to save in safe haven instruments, this pace of accretion is expected to continue

Source of funding the deficit

(INR bn)	FY2021 (BE)	FYTD August 2020
Fiscal Deficit	7963	8703
Market borrowings (Dated + Short-term)	5359	9,744
External Assistance (Net)	46	401
Securities issued against Small Savings	2400	342
State Provident Fund (Net)	180	97
Other Receipts (Net)	508	(1,930)
Cash Balance	(530)	50

Source: CGA, ICICI Bank Research

With more clarity on the GST compensation fund issue, we expect state government borrowing of ~INR 9.3 tn which would lead to H2 borrowing of INR ~5.7 tn. We believe that the Q3 SDL borrowing calendar of INR 2.02 tn could see upside risks, with reliance on the green-shoe option, as states continue to remain severely resource constrained.

Overall, we expect gross general government borrowing of ~12% of GDP for the fiscal with H2 borrowing of ~INR 11 tn.

To summarise, the recent announcement would put the uncertainties around treatment of GST cess compensation fund and risk of higher central government borrowing announcements later in the year, to an end. The overall general government borrowing expectations do not change with this announcement as it is a transfer from state to central borrowings. The fact that the weekly auction size would see reduction, along with lower weekly supply in duration (given the extension to mid-March), would be a positive. The 3-year, 5-year segment, would see higher supply and could lead to some bear flattening in the curve, though surplus liquidity could aid in putting a cap on yields. Markets would expect higher OMOs in G-sec securities to absorb the supply, while continuing to expect announcements in SDL OMOs.

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