

RBI cautions states on fiscal discipline as bond yields rise

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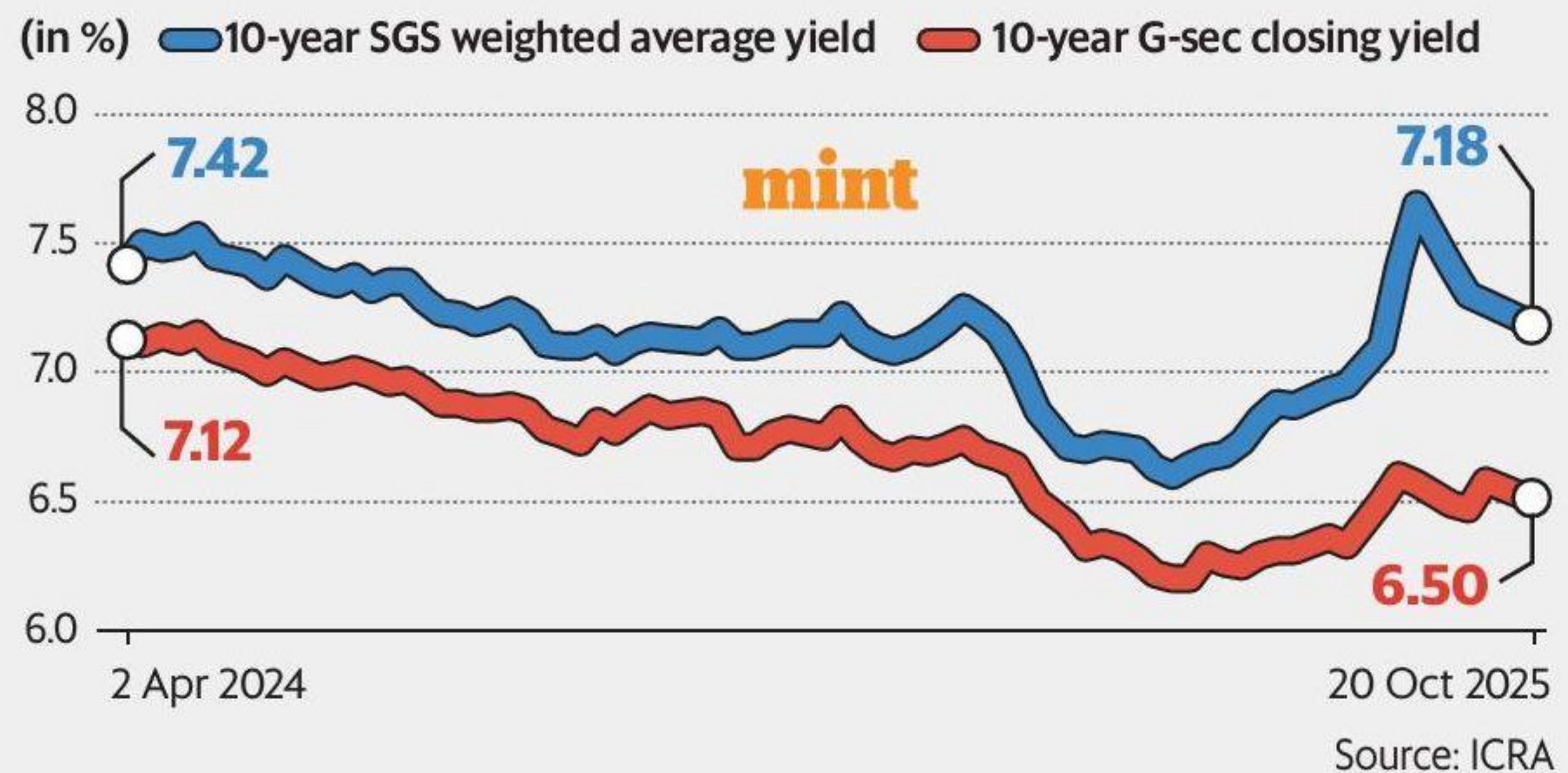
Flagging a sharp rise in state bond yields, the Reserve Bank of India (RBI) has cautioned states against pre-election populist spending and fiscal slippage, especially in Bihar and Maharashtra.

At a meeting with state finance secretaries last month, RBI governor Sanjay Malhotra urged states to keep borrowing in check and adhere to fiscal deficit targets under the Fiscal Responsibility and Budget Management (FRBM) framework, four people aware of the matter said.

A rise in market borrowings and an uncertain global environment widened the spreads between 10-year benchmark government bonds and state development securities (SDLs) to 106-112 basis points in early September, significantly higher than historical spreads

Caution signal

Rising market borrowings, global uncertainties widened the spread between 10-year govt bonds and state development securities



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of 30-40 bps.

The central bank's concerns were not reflected in a brief post-meeting statement, but have since gained urgency amid rising yields and expanding welfare commitments. The caution comes as market worries have deepened over the financial burden of populist schemes, the people cited above said on the condition of anonymity.

"Governor emphasised on the importance of fiscal disci-

pline for promoting economic growth and prosperity," the RBI statement on the 35th Conference of State Finance Secretaries had said on 18 September.

RBI is particularly worried about states that are simultaneously facing extended monsoon-related losses and pre-election spending pressures, according to two of the four people cited earlier.

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