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# State govts' borrowing costs surge as yields rise

TNN / Updated: Jan 19, 2022, 10:09 IST

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State governments

are paying a stiff price for their borrowings as yields move up in the money markets. The state governments have seen their borrowing costs move up by 9-14 basis points (100bps = 1 percentage point) from last month.

The RBI had announced an auction of state bonds (state development loans, or SDLs) to take place on Tuesday. These were issued by 12 state governments, totalling Rs 20,659 crore. The tenure on these bonds ranged from five years to 20 years.

The biggest borrower, the state of Uttar Pradesh (at Rs 3,000 crore) sold its 10-year bonds at a cut-off yield of 7.24%.

Among other states that opted for the issue of a 10-year paper, West Bengal priced its bonds at a cut-off yield of 7.23% compared to 7.14% last fortnight. Bihar's 10-year was at 7.24% and Goa & Manipur sold at 7.23%. On January 4, the 10-year yield was 7.10%. Therefore, the overall cost has gone up by 0.14%.

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"Bond yields are spiking upwards on inflation as well as budgetary concerns. The borrowing programme for next year is under focus. And, with redemptions being around Rs 4 lakh crore, there will once again be a large borrowing programme," said [Bank of Baroda](#) chief economist [Madan Sabnavis](#). He pointed out that oil prices were adding to inflationary pressures.

The cost is higher than what triple A-rated companies are paying for their borrowings. For banks, there is no credit risk in buying the state government loans auctioned by the RBI. Unlike borrowing by a state government undertaking, repayment of interest and principal on these loans is ensured by the central bank by dipping into the accounts of the states. All state governments have accounts with the RBI, where central government transfers are parked.

There is, however, a liquidity risk and a higher market risk. The market for these bonds is not as deep as central government bonds, because of which price movements are likely to be more volatile.

According to a Care Ratings report in December, with the size of the consolidated state budgets being higher than that of the centre, the development responsibility is almost equally distributed across the Centre and states. According to various budgets, expenditure for the Centre is Rs 34.8 lakh crore for FY22 as against Rs 42.9 lakh crore consolidated for the states. "In fact, with the finance commission mandating higher transfers to the states from the Centre's revenue collection (41%), the role of the states has increased," the report said.

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