3. Zero coupon bonds are the innovative financing tool used by Government of India to recapitalize Public sector banks in India. Explain.

Zero Coupon bonds are interest free bearing bonds, which are non-tradable instruments having a long maturity of 10-15 years and specifically issued to certain banks.

No market loss innovation :

1. Traditional coupon bonds vary with market fluctuations, creating certain risks to market subscribers.
2. But Zero Coupon bonds are usually held-to-maturity - HTM category, thus government use it as innovative tool to recapitalise market risked PSB.
3. (e.g) government recently gave ₹ 5000 crore Zero Coupon bonds HTM devoid of market fluctuations to recapitalise Punjab bank and Sindh bank.

Targeting banks - Innovative tool:

1. Traditionally, government securities can be bought by all banks, thus less targeting of specific distressed banks
2. Zero Coupon bonds are not tradeablle, specifically issued bonds only to certain banks to improve through recapitalisation
3. As a innovative tool, the balance sheet of NPA through targetisation of bank is done

No loss to bank at par - Innovative tool:

1. Usually Zero Coupon bonds are not issued at discount and issued par with face value
2. Thus end of 10-15 years maturity, the bonds are brought back only by the RBI guidelines, thereby no ~~fo~~ loss of banks financial sheet.

Concerns and challenges:

1. This is not a permanent solution as it can't target all stressed banks in nation
2. Short term bond availabilty absence cant absorb short-term bank risk fluctuations

The Zero Coupon bonds are innovative tool to address the twin balance sheet problem of Public sector banks to address 5 T economy by 2024.