

Section: Perspectives

Topic: Governance

Title: Municipal bonds in India: A 30 year story, still unfinished

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Teaser:

Municipal bonds – an instrument to finance urban infrastructure – have not quite taken off in India. In this post, Mehta and Mehta trace their history in the country over the past three decades and review global experiences. They recommend strengthening the fiscal base of Indian municipalities and promoting municipal bonds among the wider investor community.

Meta Description:

To develop municipal bond markets in India, there is a need to strengthen the fiscal base of municipalities, promote these instruments among the wider investor community.

Main Text:

The Union Budget 2026-27 has made a bold move to encourage cities to issue municipal bonds by proposing an incentive of Rs. 100 crore for municipal bond issuance above Rs. 1,000 crore by a municipal corporation. The AMRUT (Atal Mission for Rejuvenation and Urban Transformation) support for smaller bond issues also continues. These provisions suggest a recognition that municipal bonds have not generated any significant market capitalisation over the last 30 years.

Three decades ago, while working on the Financial Institution Reform and Expansion-Debt (FIRE-D) programme, we had organised the first workshop on municipal bonds in India. It had generated considerable interest among administrators and practitioners from both municipal and investment communities. In general, there was a consensus among the workshop participants that municipal bonds present a potential opportunity to finance urban infrastructure. In those early days, we worked with CRISIL (Credit Rating Information Services of India Limited) to develop a rating structure for municipal bonds, held meetings with potential merchant bankers, and conducted workshops for state and municipal officials. We supported discussions on the first Rs. 100 Crore public issue of Ahmedabad in 1998 without a State guarantee. Since then, references to municipal bonds have appeared in several major reports and programmes related to urban development of the Government of India (GoI).

However, 30 years hence, the story of municipal bonds remains unfinished. The total issuance of municipal bonds in India during 1997-2026 is Rs. 6,087 crore, a sum that is equal to the annual budget of a mid-sized city in India. More than two-thirds of this amount (Rs.

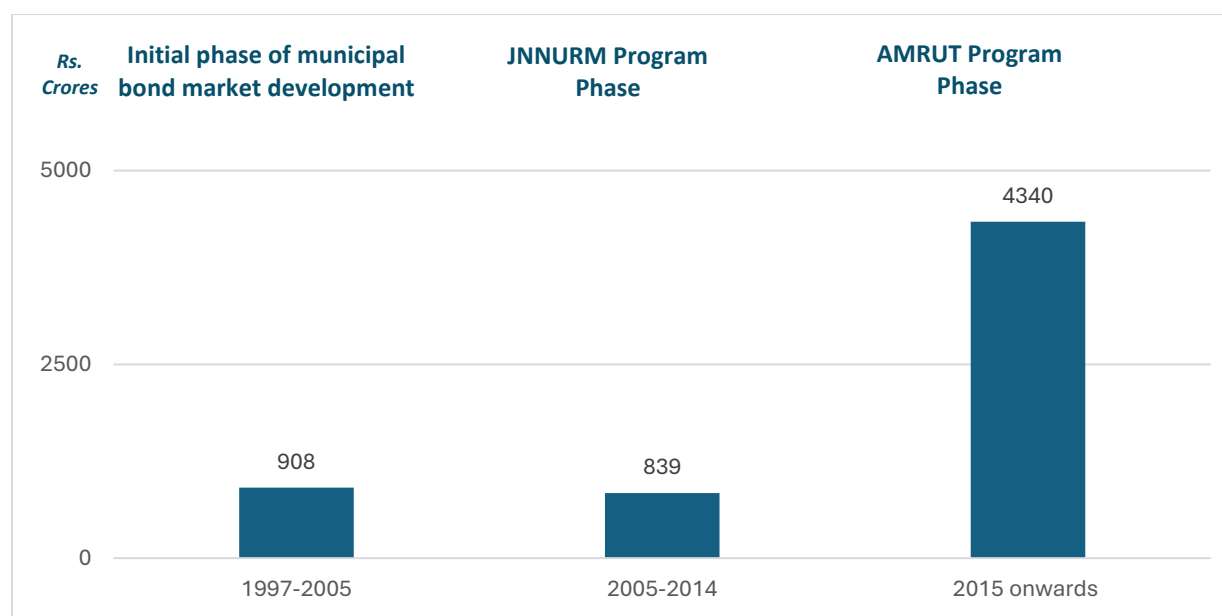
4,340 crore) was raised in the last decade, primarily as a result of the incentives offered by the Gol.

Why have municipal bonds not really taken off in India? Is there an unnecessary focus on an instrument that has no real demand from cities and no appetite from investors? In this context, it is worth looking at the experience of municipal bonds globally. What lessons can we draw from the global experience? In this post, we explore answers to these questions.

Municipal Bonds in India: No demand despite many efforts

There have been three distinct phases of municipal bonds in India. The first phase (1997-2005) was the developmental phase. “In 1995, a national workshop on municipal bonds for the first time brought together the urban and finance sectors to explore the possibility of using municipal bonds to access capital markets for urban infrastructure. In 1996, the Rakesh Mohan Committee advocated commercial finance as a way to meet the large shortfalls in urban infrastructure finance. Public-private partnerships (PPPs) in urban infrastructure were envisaged as a way both to mobilise resources and to improve efficiency in the delivery of services. In 1997, the Ninth Plan approach paper recommended issuance and trading of municipal bonds. In 1998, the Ahmedabad Municipal Corporation issued the first municipal bond in Asia without a sovereign or state government guarantee and with a domestic credit rating.” (Mehta and Mehta 2010). This was followed by the credit rating of several municipal bonds, which helped raise Rs. 900 crores during this period.

Figure 1. Issuance of municipal bonds in India over the years, in Rs crore (1997-2026)

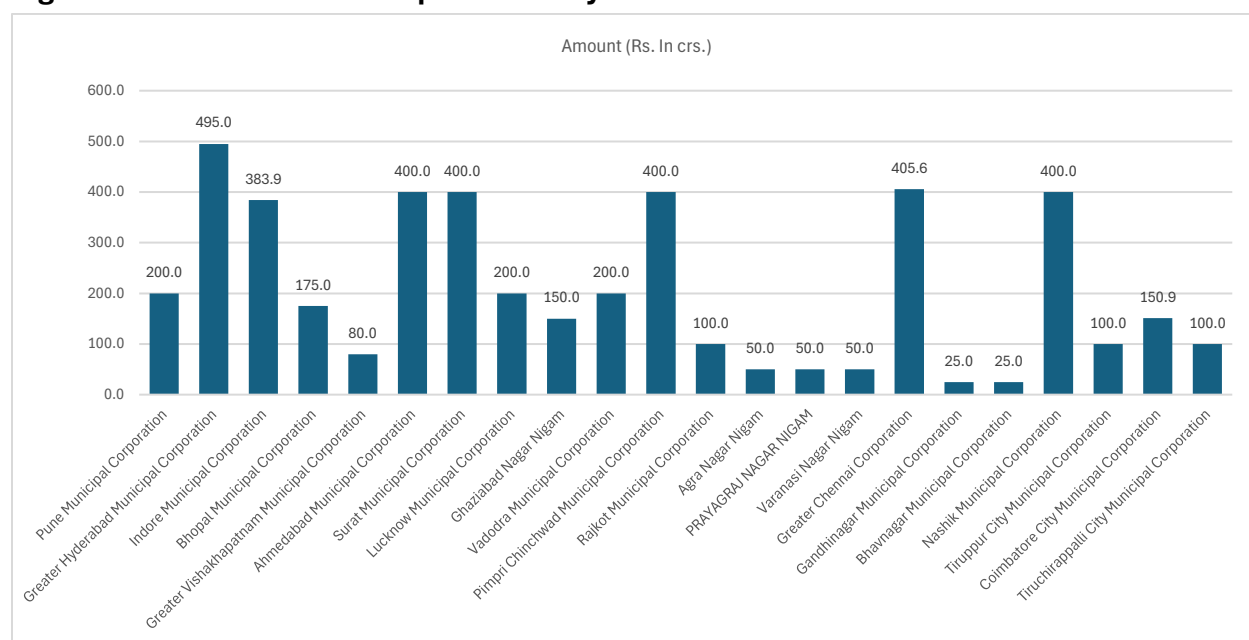


Source: Analysis by CWAS team, based on Securities and Exchange Board of India (SEBI) data, 2026 ([link](#)).

During the second phase (2005-2014), the JNNURM (Jawaharlal Nehru National Urban Renewal Mission) was launched with an envisaged outlay of Rs. 100,000 crore. This may have sounded a death knell for municipal bonds in India. The euphoria generated in the initial phase of development of municipal bonds died out as grant funds were plentiful. So, instead of preparing cities for raising capital from the market, the attention of cities and experts was drawn to the preparation of DPRs (detailed project reports) to mobilise public funds. The JNNURM grant funds probably 'crowded out' any market borrowings by cities. The only bond issues in this phase were by Tamil Nadu Water and Sanitation Pooled Fund and the Karnataka Water and Sanitation Pooled Fund – the entities that were not directly eligible for JNNURM grants. Cities that received a large share of JNNURM funds were those with a credit rating of A and above and had the potential to tap the capital market for funds. However, given the relative ease with which JNNURM funds were available, cities did not need to tap commercial finance sources (Mehta and Mehta 2020).

In 2015, the Securities and Exchange Board of India (SEBI) brought municipal bonds under the SEBI (Issue and Listing of Municipal Debt Securities) Regulations, 2015. These rules lay out the eligibility criteria, disclosure requirements, and listing standards that local governments must follow to raise capital for urban infrastructure development. The third phase (2017 onwards) can be referred to as the 'incentive-driven' phase. From 2018, an incentive of Rs. 13 crore for every Rs.100 crore of bonds issued was available under the AMRUT programme. It is capped at Rs. 26 crore per urban local body (ULB) and is available for the first bond issue. For the subsequent bond issues, the focus is on 'green bonds', and an incentive of Rs. 10 crore is provided per Rs. 100 crore raised, capped at Rs. 20 crore. The spate of municipal bond issues after 2017 is a result of these incentives and may have little to do with creating a municipal bond market. As of February 2026, a total of Rs. 4,340 crore has been raised, and an incentive amount of Rs. 330 crore was provided under the AMRUT programme.

Figure 2. Issuance of municipal bonds by cities in India



Source: Based on SEBI data, 2026 ([link](#)).

The recent issues of municipal bonds have been listed on the National Stock Exchange (NSE) and the Bombay Stock Exchange (BSE). However, this has not led to any trade of municipal bonds on these exchanges. This is largely due to the fact that, except for the Indore municipal bond, where a small amount was kept reserved for retail subscribers, all other bonds have been largely subscribed to by public financial institutions. For example, NaBFID, a GoI institution that is “focused on addressing the long-term financing needs of the infrastructure sector in India”, has acted as an anchor investor in several municipal bond issuances. It invested Rs. 30 crore in the Rs. 200 crore bond issue of Pimpri Chinchwad Municipal Corporation (PCMC). The Gujarat State Finance Company (GSFC), a Gujarat state-owned agency, invested Rs. 170 crore the Rs. 200 crore bond issue of Ahmedabad Municipal Corporation.

It appears that in the 30 years of efforts to promote municipal bonds in India, only Rs. 6,100 crore has been raised by 25 cities. Most of these bond issues have a tenor of five years, while such bonds are supposed to provide ‘long-term’ financing. A few bond issues of 10-year tenor in recent years are those that have implicit government backing, such as in Uttar Pradesh (UP) and Tamil Nadu. For instance, the Lucknow bond issue and subsequent bond issues in UP have support from the Infrastructure Development Fund of the state government of Uttar Pradesh, which may be utilised in case of any shortfall in meeting the debt obligation. In Tamil Nadu, under a World Bank-funded project, credit enhancement in

the form of cash collateral from the Project Sustainability Grant Fund was provided (Srikumar 2026).

Recognising that the incentives had largely limited the maximum issue size of municipal bonds to Rs. 200 crore, the Union Budget for 2026-27 introduced a specific Rs. 100 crore incentive for a single bond issuance over Rs. 1,000 crore, while continuing the standard AMRUT incentive for smaller bond sizes. It appears that without these incentives from AMRUT and the implicit government backing in some cases, the entire municipal bonds programme may come to a standstill.

Municipal debt: The global experience

While reviewing the municipal bond experience in India and its slow and limited development, it would be useful to look at the experience of other countries. Do cities in other countries get such 'lucrative' incentives to raise municipal bonds?

Municipal bond studies instinctively point to the established US municipal bond market, with an estimated market size of nearly US\$4 trillion. It should also be recognised that the US municipal bonds are often issued not only by municipal authorities, but also by many other service providers at the city, county, and state levels. Municipalities may issue bonds on behalf of private entities (known as "conduit issuers") to finance qualifying projects. These typically include non-profit hospitals, private universities, and multi-family housing developments (Fidelity Investments, 2025). The municipal bond market is estimated to be over US\$4 trillion, financing approximately 75% of US infrastructure, such as schools, hospitals, and transportation.

The US municipal bond market is probably the global outlier, not the benchmark. Municipal bonds thrive there because of several conditions. American municipalities are sovereign entities and can tax and borrow without state or federal government approval. Another key factor in the development of the US municipal bond market has also been its tax-free status. This tax-exempt incentive has created a large base of retail investors. While federal income tax is exempt, investors may still face federal tax on capital gains, and some bonds used for private projects can be subject to the Alternative Minimum Tax (AMT). Less than 10% of the municipal bonds issued in the US are taxable. Bonds are taxed if they do not provide significant benefits to the public, such as for building a stadium or replenishing a pension fund (Fidelity Investments, 2025).

The Indian approach to municipal bond market development has emulated the US experience, despite a dramatically different context in which cities in both countries operate. In India, despite being recognised as a third tier of the government in the constitution (the 74th amendment), municipalities remain under the administrative control

of state governments and need to seek their permission for raising debt. Moreover, infrastructure grants through national missions such as JNNURM and AMRUT and various state government grants have provided 'free' funds to municipalities. These funds, have crowded out market borrowing like bond financing (Mehta, Mehta and Bhavsar 2026) by focusing more on municipal entities.

Few studies, however, recognise that there are also other established municipal bond markets. For example, the size of municipal bond market in the People's Republic of China (PRC) has exceeded that of the US market in recent years, with an outstanding debt of US\$4.5 trillion (Asian Development Bank, 2026). It is also important to recognise that in the PRC, the municipal debt is often issued by the Local Government Financing Vehicles (LGFV). These are more akin to the city- and state-level SPVs in India. "Local government financing vehicles (LGFVs) are state-owned investment companies established by China's local governments. LGFVs have played a significant role in driving China's economic growth and investment by financing urban infrastructure development." (The Economist, 2021a and 2021b). However, the LGFVs in recent years have also run into problems and have even resulted in overall economic issues for the country (Mathews 2025 and The Economist 2021a and 2021b). Thus, such experienced need to be reviewed and emulated only with caution.

In Japan, the Local Autonomy Law authorises local governments – prefectures and municipalities (cities, towns and villages) – to borrow money. Their borrowing or debt, excluding those repaid within one fiscal year, is called *chihousai*, which is usually translated as 'local government bonds'. This includes not only publicly offered bonds and private placement bonds, but also loans in the form of deeds. The publicly offered bonds have retail investors, while the private placement bonds are subscribed to by financial institutions, like the Japan Finance Organisation for Municipal Enterprises (JFM). Japan has US\$1.7 trillion of municipal bonds outstanding.

The JFM is a primary public financial institution for providing long-term and low-cost financing to local governments, and it is a preferred lender to local governments for basic infrastructure-related funding. It was established with capital contributed by all prefectures, cities, special wards of Tokyo, government-designated cities, towns and villages, as well as some local government associations, to provide funds to local governments.

Table 1. Municipal bonds outstanding, selected countries

Country	Outstanding bonds (<i>in US\$ mn</i>)
People's Republic of China	4,451,000
United States of America	4,036,000
Japan	1,760,000
India	532
Vietnam	486

Source: Based on Asian Development Bank (2023).

While Vietnam has US\$486 million of municipal bonds outstanding, these were issued by only two local governments (Ho Chi Minh City Finance and Investment State-owned Company, and Hai Phong People's Committee). As in India, with multilayered controls on local government borrowings, the municipal bond market in Vietnam has not expanded.

Our brief review of the global municipal financing experience shows that municipal bonds are dominant only in a few countries.¹ It is also important to recognise that many countries in Europe and Asia rely entirely on different debt systems, with various forms of State entities. For example, the UK has the Public Works Loan Board, France has *Caisse des Dépôts*, the Netherlands has BNG Bank, and the DBSA in South Africa. These entities, supported by the government, can borrow at low costs (near-sovereign rates) and on-lend to municipalities. In the EU, National Promotional Banks and Institutions (NPBIs) support their national or regional governmental targets by investing in projects, funds, and companies. Their main goal is to increase the volume of investments and support certain policy areas or address identified market gaps. While NPBIs invest in financially viable projects, they do not always operate on strictly commercial terms, as they may also provide blended finance, subsidised interest rates, among others (Circular City Funding Guide, 2026).

These Municipal Development Funds (MDFs) are established at a level above individual local governments to pool resources for investing in urban infrastructure and services and thus help pool risk. They act as intermediaries, bridging the gap between national/international capital and local municipalities that may lack direct access to financial markets (Davey 1988, Mehta 2003).

¹ It must, however, be noted that there is a growing market in municipal green bonds in many European and Latin American countries.

What is needed to make municipal bonds really ‘take off’ in India?

It is recognised that constraints to municipal mobilisation of repayable finance exist along three dimensions – demand, supply, and the intermediating regulatory environment (World Bank, 2025). From the experience of recent municipal bond issues in India, there appears to be demand for these instruments. We also observed that municipal development funds play an important role in financing local governments in many countries. India has had limited success with national funds and institutions like the Urban Infrastructure Development Fund (UIDF), NaBFID, HUDCO etc.; these need to become more proactive in lending to urban local governments.

The share of municipal bonds in the overall debt of municipalities remains very low, and most current bond issues are subscribed to by institutions that would otherwise fund infrastructure projects. The municipal bond market in India can be broadened if tax exemption is made available to subscribers. This will open the bond market to a larger pool of retail investors and free up capital from financial institutions that are often required to subscribe to bond issues. Over time, the subsidy for bond issues can be reduced or eliminated. Such tax benefits may also attract institutions and banks to increase their investments in bonds.

Efforts are also needed to strengthen the fiscal base of municipalities in India. We recognise that cities will need to borrow for their infrastructure. However, this need not be only through municipal bonds. A range of financial institutions exists in India that can lend to municipalities. It is a misnomer that municipal bonds provide “long-term” funds. Most bond issues have a five-year term. Many financial institutions can also provide loans for this duration. They can also provide longer tenor loans if there are “viable” projects and adequate creditworthiness of the borrowing municipality. We have developed a tool to assess the creditworthiness of cities, which can be used by cities and lending agencies to evaluate debt repayment capacity. This user-friendly tool draws on publicly available data on finances and services to capture a city's ability to manage funds and deliver services. Initial analysis demonstrates that many more cities in India have the capacity to repay debt.

Indian cities have two primary sources of financing – own-source revenues and inter-governmental transfers and grants. Currently, these are insufficient to bridge the large infrastructure financing gap. The 16th Finance Commission has attempted to address this issue by increasing the allocation of untied grants to cities, which will also help improve their creditworthiness. With the introduction of GST (Goods and Services tax), several buoyant local taxes have been subsumed, and a strong case can be made for allocating a share of

GST revenues to ULBs to incentivise them to promote economic growth and strengthen their finances (Mehta and Mehta 2026).

In conclusion, while cities are recognised as engines of economic growth, the prevailing situation is one of "rich cities, poor city governments". Indian ULBs do not receive an adequate share of the economic prosperity of the country. It is likely that this also affects the development of municipal bond markets. There is also a need for greater awareness about municipal governments among the wider investor community. Thus, to really get municipal bonds to take off in the country, these wider issues of inter-governmental financing, as well as a focus on widening the potential investor base through tax benefits, will also need to be addressed.

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