Shedding more light on the debt dilemma

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The elevated levels of India's fiscal deficit and public debt have been a matter of concern for a long time in India. Even before the COVID-19 pandemic, debt levels were among the highest in the developing world and emerging market economies. The pandemic pushed the envelope further and relative to GDP, the fiscal deficit in 2020-21 increased to 13.3% and the aggregate public debt to 89.6%. As the economy recovered after the pandemic, the deficit and debt ratios have receded to 8.9% and 85.7%, respectively.

The projections show that even without any serious disruptions to the economy, the debt level is unlikely to return to the pre-pandemic trajectory in the medium term. With elections to a number of States scheduled in 2023 and with the general election for 2024, the electoral budget cycle could push the debt ratio further. And, there can be serious questions about its sustainability unless targeted interventions are made to reduce the debt burden, which may not be politically easy with elections on the horizon.

Financial repression

The debt-dynamics equation states that when there is no primary deficit (fiscal deficit in the year excluding the past legacy of interest payments), if the growth rate of GDP exceeds the effective interest rate paid on government bonds, the overall debt will decline. However, what is missed in these discussions are the distortions caused by financial repression to keep the interest rates on government borrowing low to reduce the cost. The statutory liquidity ratio (SLR) stipulated by the Reserve Bank of India (RBI) requires the banking system to hold 18% of their demand and time liabilities in government securities. Besides, the RBI intervenes in the market through open market operations around the time when government borrowing is taken up to keep the interest rates on government borrowing repressed. When the interest rate on government debt is lower than the growth of GDP, the debt may decline but the financial market gets distorted.

Thus, even when the sustainability of debt may not be threatened in the medium term, the costs of carrying high deficits and debt to the economy are heavy. First, on average, interest payments constitute over 5% of GDP and 25% of the revenue receipts, this is more than the government expenditure on education and health care put together. Large interest payments crowd out the much-needed expenditures on physical infrastructure and human development and emerging priorities to make the green transition. The issue is of concern in Punjab, Kerala, Rajasthan, and West Bengal. In Punjab, the Debt to GSDP ratio is 48.9%, in West Bengal, 37.6%, Rajasthan 35.4%, and in Kerala close to 33%.

Second, high levels of debt make it difficult to calibrate counter-cyclical fiscal policy and constrain the ability of the government to respond to shocks.

Third, the debt market in India is largely captive with mainly the commercial banks and insurance companies participating in it to meet SLR requirements. With a cash reserve ratio (CRR) of 4.5% and SLR of 18% of net demand and time liabilities, and 40% of the credit by the commercial banks earmarked for the priority sector, the resources available for lending to the manufacturing sector gets squeezed, driving up the cost of borrowing of the sector. Furthermore, the rating agencies keep the sovereign rating low when deficits and debt are higher, and this increases the cost of external commercial borrowing. Finally, 'today's borrowing is taxing tomorrow' and the burden of large deficits and debt will have to be borne by the next generation.

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On the debt burden

It is clear that in the present fiscal environment, even achieving a consolidated debt-to-GDP ratio of 58.2 recommended by the 14th Finance Commission for 2019-20 would be unfeasible in the medium term. The Finance Commission had recommended that the Union government bring down its deficit relative to GDP from 43.6% in 2015-16 to 36.3%, and the States maintain their deficit at about 22%. Even before the pandemic, the aggregate public debt had slipped to 74.3% in 2019-20, and the pandemic pushed it to 89.7% in 2020-21. With the nominal GDP recovering to grow at 18.5% in 2021-22 after the pandemic, the debt ratio declined only marginally to 85.7%. This implies that every individual in the country bears a debt burden of ₹1,64,000. With the high primary deficit of 3.7% of GDP in 2022-23 and budgeted at over 3% in 2023-24, we will have to contend with elevated debt levels in the medium term.

The issue is of critical importance; therefore, the fast pacing of fiscal consolidation is imperative. Fortunately, after six years, Goods and Services Tax (GST) has stabilised and has shown high growth potential. As the technology platform has stabilised, it is expected to maintain high buoyancy in the medium term. The technology has helped to improve tax administration and improved compliance. With the cross-matching of GST returns with income-tax returns, income-tax compliance too is expected to improve. In the medium term, the aggregate tax-GDP ratio is likely to increase by 1.5 percentage to 2 percentage points.

In terms of policy interventions, this is the time to rethink the role of the state and vacate activities that should really belong to the market rather than competing with it. At the central level, even after much talk about disinvestment, progress has been slow. Rather than dispensing with activities such as telecom to the private sector, the government continues to pour money into Bharat Sanchar Nigam Limited. Equally disturbing are the employment *melas* to fill so-called vacant posts which have been found to be redundant. At the State level, it is important to guard against the return to the old pension scheme and indulge in large-scale giveaways for electoral reasons. Of course, redistribution is a legitimate government activity, and that is best done through cash transfers rather than subsidising commodities and services. Giving subsidies alters relative prices, resulting in unintended resource distortions. Equally important is the need to impose hard budget constraints by enforcing Fiscal Responsibility and Budget Management rules in allowing States to borrow. Macroeconomic stabilisation is predominantly a Union government responsibility. Therefore, the Union government should follow the rules it makes, and enforce the rules on the States effectively.

The views expressed are personal

The SCO is a success story that can get better

On July 4, 2023, India successfully hosted the 23rd Meeting of the Council of Heads of State of the Shanghai Cooperation Organization (SCO). The world witnessed another "SCO moment". Leaders of the SCO member-states signed the New Delhi Declaration, and issued the statements on countering radicalisation and exploring cooperation in digital transformation. The summit granted Iran full SCO membership, signed the memorandum of obligations of Belarus to join the SCO as a member-state, and adopted the SCO's economic development strategy for the period until 2030. These significant outcomes have demonstrated the vitality of the "SCO family".

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A changing world

Our world, our times and history are changing in ways like never before. The world is grappling with geopolitical tensions, an economic slowdown, energy crises, food shortage and climate change. These challenges require the joint response of all countries. The major risks to world peace and development are power politics, economic coercion, technology decoupling and ideological contest. The central questions revolve around unity or split; peace or conflict; cooperation or confrontation. The international community must answer them.

Over the years, the SCO has been committed to becoming a community with a shared future for mankind, firmly supporting each other in upholding their core interests, and synergising their national development strategies and regional cooperation initiatives. Member-states have carried forward the spirit of good neighbourliness and friendship, and built partnerships featuring dialogue instead of confrontation, and cooperation instead of alliance. The SCO has been a guardian of and contributor to regional peace, stability and prosperity. These achievements manifest the common aspirations of all countries so that there is peace, development and win-win cooperation. The SCO's leading and exemplary role can help strengthen unity and cooperation, seize development opportunities, and address risks and challenges. Going forward in a new era, the SCO member-states should strengthen strategic communication, deepen practical cooperation, and support each other's development and rejuvenation. As we build a better homeland together, more certainty and positive energy will be brought to the world.

Shanghai Cooperation Organization member-states should strengthen strategic communication, deepen practical cooperation, and support each other's development

We should enhance solidarity and mutual trust for common security. There are some external elements that are orchestrating a new Cold War and bloc confrontation in our region. These developments must be addressed with high vigilance and firm rejection. SCO member-states need to upgrade security cooperation, and crack down in a decisive manner on terrorism, separatism and extremism, and transnational organised crimes. We need to pursue cooperation in digital, biological and outer space security, and facilitate political settlement when it comes to international and regional hot-spot issues.

We should embrace win-win cooperation to chart a path to shared prosperity. Protectionism, unilateral sanctions and decoupling undermine people's well-being all over the world. It is imperative for the SCO to generate stronger momentum for collaboration in trade, investment, technology, climate actions, infrastructure and people-to-people engagement. To contribute to high-quality and resilient economic growth of the region, there need to be collective efforts to scale up local currency settlement between SCO members, expand cooperation on sovereign digital currency, and promote the establishment of an SCO development bank.

Need for multilateralism

We should advocate multilateralism to shape our common destiny. The SCO needs more engagements with its observer states, dialogue partners and other regional and international organisations such as the United Nations, to uphold the UN-centered international system and the international order based on international law. Together, we are united in promoting world peace, driving global development and safeguarding the international order.

The SCO's success story is part of the broader global partnership of emerging economies and developing countries. As changes to the global landscape unfold, emerging economies and developing countries continue their collective rise with greater cohesion and global weight. We are increasingly acting as a progressive force for world fairness and justice. Over the next two months, South Africa and India will preside over the BRICS (Brazil, Russia, India, China and South Africa) and G-20 summits, respectively. These will be significant moments to shape a multi-polar world order, promote inclusive global development, and improve international governance architecture.

China's commitment

China is committed to working with India, South Africa and other partners from the South to put into action the Global Security Initiative, Global Development Initiative and Global Civilization Initiative, to contribute to world peace, security and prosperity. We need to pursue common, comprehensive, cooperative and sustainable security, respect each country's independent choice of the path to development and social system, and abide by the purpose and principles of the UN Charter. The reasonable security interests of all countries deserve consideration. Dialogue and diplomacy offer the best hope to address international disputes by peaceful means. And, security challenges in conventional and non-conventional domains should be dealt with in a holistic manner.

We need to forge a united, equal, balanced and inclusive global development partnership, promote humanity's common values of peace, development, equity, justice, democracy and freedom, and get global governance to evolve in a fairer and more reasonable direction. Our voice should be loud and clear against hegemony, unilateralism, a Cold War mentality and bloc confrontation. And, illegal unilateral sanctions and long-arm jurisdiction measures must be rejected. In doing so, we will lead by example in safeguarding the development rights and legitimate interests of the developing world.

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