Central government borrowing

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Source: *The Hindu*

Manifest pedagogy: The anticipation of a looming fiscal package combined with possible lower collection from taxes has prompted the government to revise its borrowing plan. This is a step in building resilience in the economy in the post covid-19 scenario.

In news: The central government recently has said that it would borrow an extra Rs 4.2 lakh crore during this fiscal.

Placing it in syllabus: Fiscal policy

Static dimensions:

- Borrowing roadmap
- FRBM

Current dimensions:

- **Increase in borrowing**
- Implications

Content:

Borrowing roadmap:

- The **Union finance ministry and the RBI** has finalised the Centre's borrowings at **Rs 12 lakh crore**, up **from the earlier budget estimate of Rs 7.8 lakh crore.**
- The steep increase is due to revenue shortfall because of the COVID-19 headwind.
- The government's borrowing calendar for the first half of the **previous financial year ended March 31, 2020** and **was Rs 4.42 lakh crore.**
- The weekly borrowing was Rs 17,000 crore in the first half of 2019-20.

- The new borrowing calendar has proposed that the government's **weekly borrowing will be around Rs 19,000 crore.**
- It is estimated that the **fiscal deficit would come at 5.8 percent of the GDP** in FY21 as against the budget target of 3.5 per cent.

FRBM Act:

- Fiscal Responsibility and Budget Management (FRBM) was **enacted in August 2003** to make the Central government responsible for ensuring inter-generational equity in fiscal management and long-term macro-economic stability.
- It **limited the fiscal deficit to 3%** of the GDP.
- It mandates the **conduct of fiscal policy in a medium-term framework.**
- The Budget of the Union government includes a **Medium Term Fiscal Policy Statement** that specifies the annual revenue and fiscal deficit goals over a three-year horizon.
- The **NK Singh committee** which was set up in 2016 recommended that the government should target a **fiscal deficit of 3% of the GDP in years up to March 31, 2020 cut it to 2.8% in 2020-21 and to 2.5% by 2023.**

Escape Clause provided: As per **Section 4(2) of the Act**, the Centre can exceed the annual fiscal deficit target citing **certain grounds** – *National security, war, Natural calamity, Collapse of agriculture and Structural reforms.*

Recently, the **State government of Kerala** has sought flexibility under the FRBM Act to ensure that fiscal stimulus in the wake of COVID-19 does not get deterred by FRBM considerations.

While the combined fiscal deficit of states in 2020 is seen higher than 2.6% of GDP estimated, **several states have asked**

Prime Minister Narendra Modi for forbearance in 2021, **for raising the deficit level to even 5%.**

However N K Singh has said that it would be easier to avail of the 0.5% cushion enshrined in their acts and higher relaxation would require amendment to the act.

Increase in borrowing:

- The government has announced that it would borrow an extra Rs 4.2 lakh crore during this fiscal, i.e. 12 lakh crore against initial borrowing target of Rs 7.8 lakh crore.
- According to the economists, the **shortfall in tax revenues this year for the government will be almost 1 percent of the GDP,** due to weak economic activity.
- The tax shortfall is estimated to be Rs 2 lakh crore.
- The government budgeted a divestment income of Rs 2 lakh crore.
- So the Rs 4.2 lakh crore excess borrowing is expected to just about meet revenue shortfall.

Implications:

Higher Fiscal Deficit: A higher borrowing amid falling revenues will push up the country's fiscal deficit which might breach the 5 percent mark.

High cost of borrowings: The yields on government securities are likely to shoot up as there is going to be a large supply of securities in the market.

Impact on state development bonds: The yield for state government is likely to spike. Though RBI has opened the overdraft window for states via increased limit under ways and means advances, the second half of the year would see bunching of all the securities.

Action by global rating agencies: The global rating agencies give a higher weightage to macro economic parameters like government debt and fiscal deficit. This would have implications for foreign investment in India both in terms of FDI and capital market.The cost of raising money for Indian corporates will move up.

Lesser funds for the private sector: There will be little money left for the private sector as the government mobilises all the money from the market. Banks will remain the only source for the private sector to get money.

Inflation: If RBI buys some of the bonds issued by the government, the economy will be benefitted as interest rates will not rise. But if the economy does not grow, the excess money sloshing around in the system can cause inflation.

Mould your thought: Why has the central government increased the borrowing limit recently? What are the implications?