REVENUE BUOYANCY, SUSTAINED CAPEX MAY BRING IT DOWN TO PRE-COVID LEVELS IN 4-5 YEARS

Another spike in debt-to-GDP ratio unlikely

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CHANCES OF INDIA'S public debt rising again after being off the pandemic-induced peak in FY21 are remote, experts said. Instead, over the next five years or so, the debt-GDP ratio could return to the pre-pandemic levels, most of them feel.

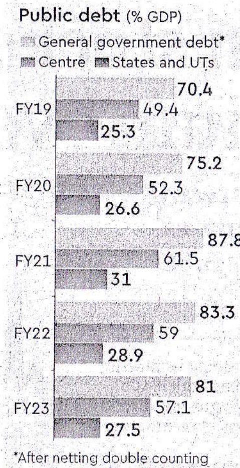
The optimism stems from the belief that the government is unlikely to materially digress from the fiscal glide path over the next few years. Also, the prospects of a steep fall in global commodity prices leading to very low inflation and nominal GDP expansion are slim in the near term.

Redemption pressures are unlikely to be too high to upset the calculations of the Reserve Bank of India, the manager of public debt.

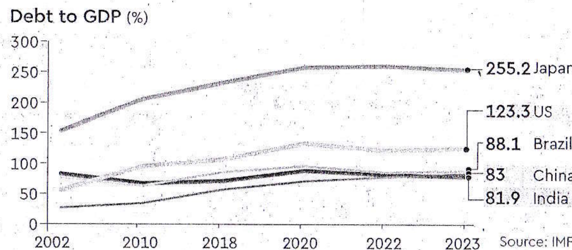
The buoyancy in tax collections is expected to stay, allowing the government to retain capex at somwhat elevated levels, and gradually lower the debt over the medium term.

Responding to the International Monetary Fund's recent forecast of India's general government debt overshooting 100% of the GDP under a worst-case scenario by FY28, the finance ministry has stated the Centre is "on track to achieve its stated fiscal consolidation target" of reducing fiscal deficit below 4.5% by FY26. What IMF referred to was not a

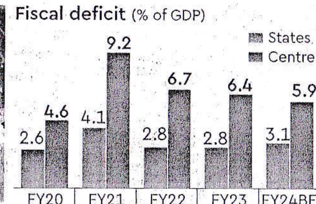
THE DEBT PICTURE



*After netting double counting



Source: IMF



baseline scenario, and any global shock would equally affect all countries, the ministry noted.

The ministry added that sticking to the glide path is necessary for India to curb general government debt, and prevent it from rising again.

India's general government debt, which comprises the debts of the Centre and states, had soared to 88% in FY21, the highest in at least four decades, as government expenditure rose during the pandemic, amid a revenue slump. It has moderated since to around 81% in FY23 with the Centre and states resorting to fiscal consolidation with a thrust on capex.

Large economies like China and Japan saw elevated debt-GDP levels after Covid also (see chart).

Of course, unlike India, these economies have a higher government revenue-to-GDP ratio than India. Government revenue of India was at 19.39% of GDP in 2022, compared with Japan's 37.24%, China's 25.88, Brazil's 43.28 and the US's 32.55%.

"We have been doing well for the past couple of years and if our economy grows by 7-8% for the next few years, this debt-to-GDP ratio has only to come down," said NR Bhanumurthy, vice-chancellor of Bengaluru's BASE University.

Going forward, a continuous push to capex will bring down the debt to GDP levels to the pre-Covid situation of around 70% by the end of 2030 as well as generate enough resources for revenue expenditure also to bring down the revenue deficit to closer to zero, Bhanumurthy said.

"The GoI's progress on fiscal consolidation is expected to augur well for the general government debt-to-GDP ratio. Additionally, the anticipated uptick in nominal GDP growth FY25, owing to the turnaround in WPI to inflation from the deflation expected in FY24, is also expected to help lower this ratio," Icra chief economist Aditi Nayar said. "Consequently, we expect continued progress towards the general government debt-to-GDP ratio reversing towards the pre-Covid levels of sub-80% over the next 1-2 years."

Nayar said the Centre would not materially deviate from the fiscal glide path over the next two years. "Hence, we do not expect a surge in the debt-to-GDP ratio during this period. However, exceptional circumstances, such as a sustained sharp fall in commodity prices could impact the nominal GDP numbers, could lead to a brief hiatus in the declining trend in (the debt-to-GDP ratio)."

While it may be difficult to target debt levels on an annual basis, the government should target interest payments by bringing down the revenue deficit closer to zero, she said.

Bhanumurthy said, "Even during difficult fiscal situations, the government should not compromise on capex as cutting back capex would lead to lower economic growth, which would put direct pressure on the debt-to-GDP ratio."

The Budget for 2023-24 provisioned for ₹10 trillion (3.3% of GDP) for capital expenditure, a sharp 36% annual increment from ₹7.36 trillion in 2022-23. This is almost three times the capital expenditure in 2019-20. With the assumption of a sharper expansion in revenue receipts of around 9.5% compared to revenue expenditure by about 3.9%, the revenue deficit is expected to entail a substantial correction to 2.4% of GDP in FY25 from 3% projected for FY24, Icra said.

High public debt means a substantial chunk of government resources are used annually to pay interest to bondholders.

The Centre's expenditure on interest payments rose to ₹9.28 trillion (27% of revenue expenditure) in FY23 from ₹5.83 trillion (29% of revenue expenditure) in FY19.