

Rethinking Fiscal Policy

IMF/PIIE Event

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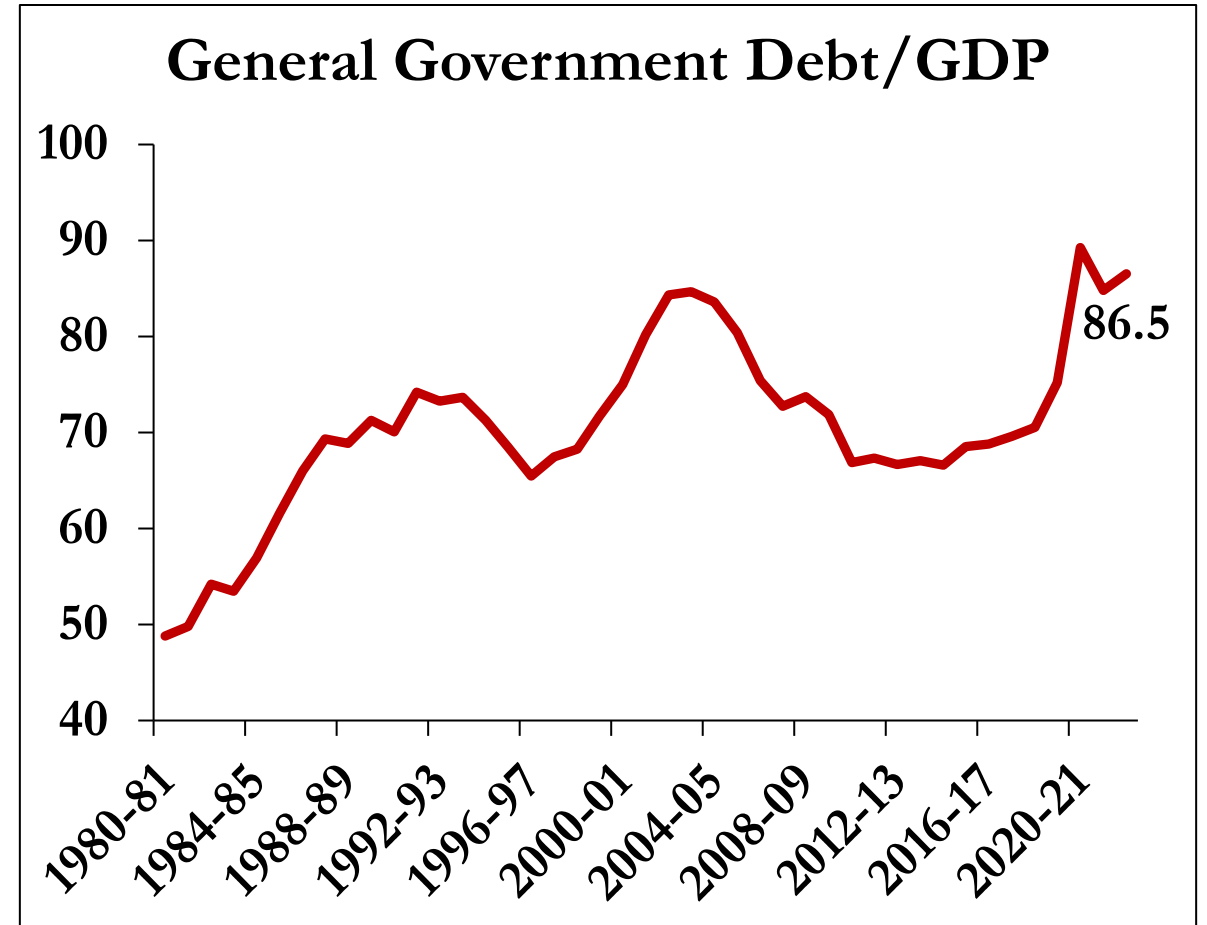
Relevant issues, for the rest of the world as well as for India

With elevated public debt and deficits:

- What will the debt trajectories look like?
- Which factors will play out: interest rates, growth, inflation, primary deficit, contingent liabilities, revenue buoyancy, better expenditure management, better expenditure allocation.
- How will the emerging priorities be financed, including on climate.
- What will the fiscal rules look like. Rules vs Institutions.

India's Public debt

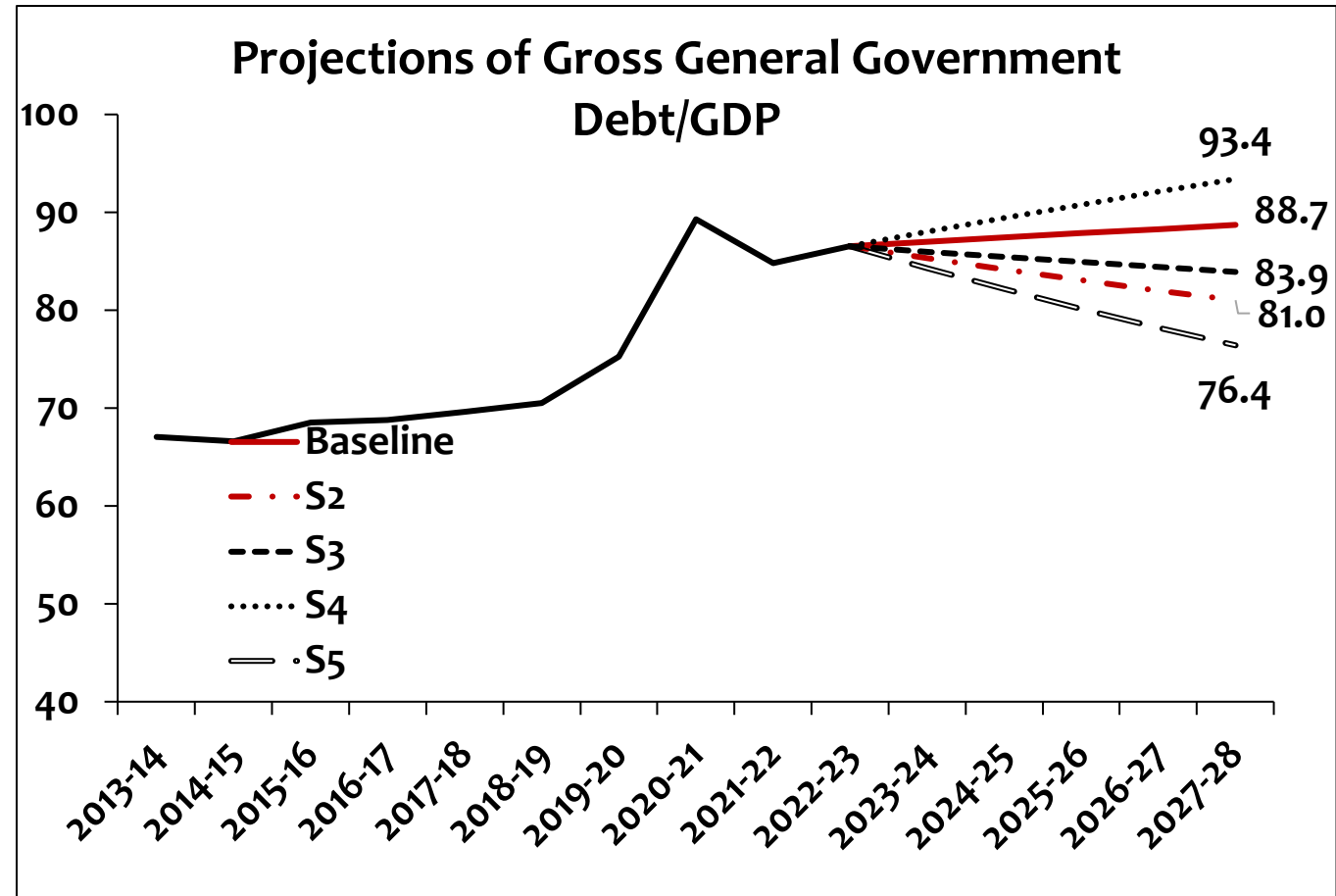
- India's public debt has been high
- Episodic consolidation of debt, to only reverse subsequently
- This is so despite favorable r-g. Due to:
 - Sizable primary deficit
 - Realization of Contingent Liabilities



India's Public debt will not decline significantly under Reasonable Scenarios

- (i) Growth, primary deficit, interest rates at past decadal average
- (ii) Growth accelerates
- (iii) Primary deficit declines
- (iv) Contingent liabilities materialize at past levels

Will need a combination of factors for debt to decline: e.g. faster growth plus lower primary deficit.



Yet no signs of debt distress. Low rollover risk.

- Bond yields have remained steady during the past decade
- Have not increased post covid either
- With slightly higher inflation, real yields have become negative

Why:

- Debt is held domestically
- By institutional investors and the central bank. Institutional investors partially owned by the government
- Debt raised on fixed rate; in local currency
- Longer average duration
- Adequate domestic savings for now

Other Relevant Developments and Issues

- Revenues (in percent of GDP) have lagged other countries. Rapid growth of revenue, but have not increased as percent of GDP.
- Better expenditure allocation—capital expenditure, and better targeted social spending.
- High household savings. Have not increased as percent of GDP, but seem sufficient to finance government borrowing for now
- Mixed success with fiscal rules. Fiscal rules in a federal set up require vertical and horizontal allocation of fiscal space.

Public Debt in India: Before, During and After Covid

- Public debt already high in India; has increased further during Covid.
- Tolerance for debt has increased. It will likely settle at elevated levels
- Conventional thresholds for sustainable level of debt deemed less relevant due to the composition of debt; high domestic savings rate; financial repression; and lack of safe assets

The way forward:

Somewhat higher inflation might be the least worst option

Increased revenue buoyancy, plus privatization (earmarked to pay back the debt or for climate)

Keeping the debt composition safe, continuing to finance it through domestic savings

Thanks!

Public debt to GDP: median and interquartile range

Figure A)

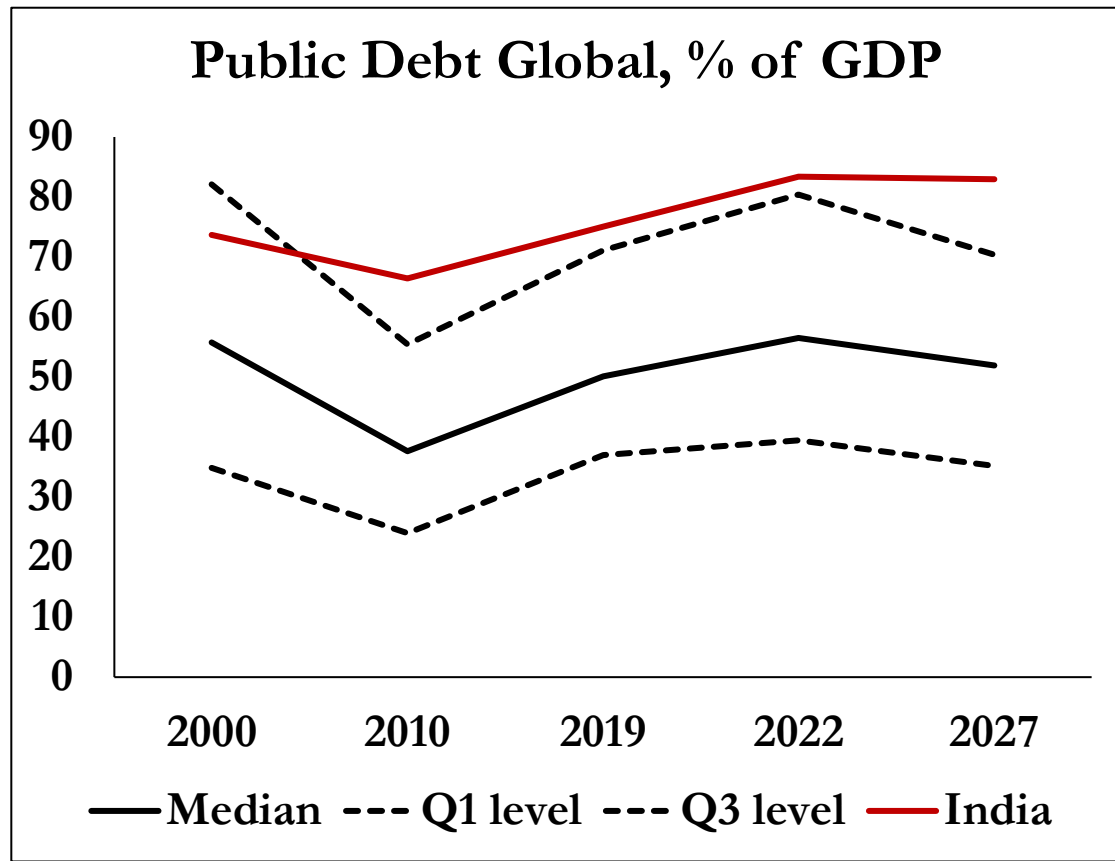
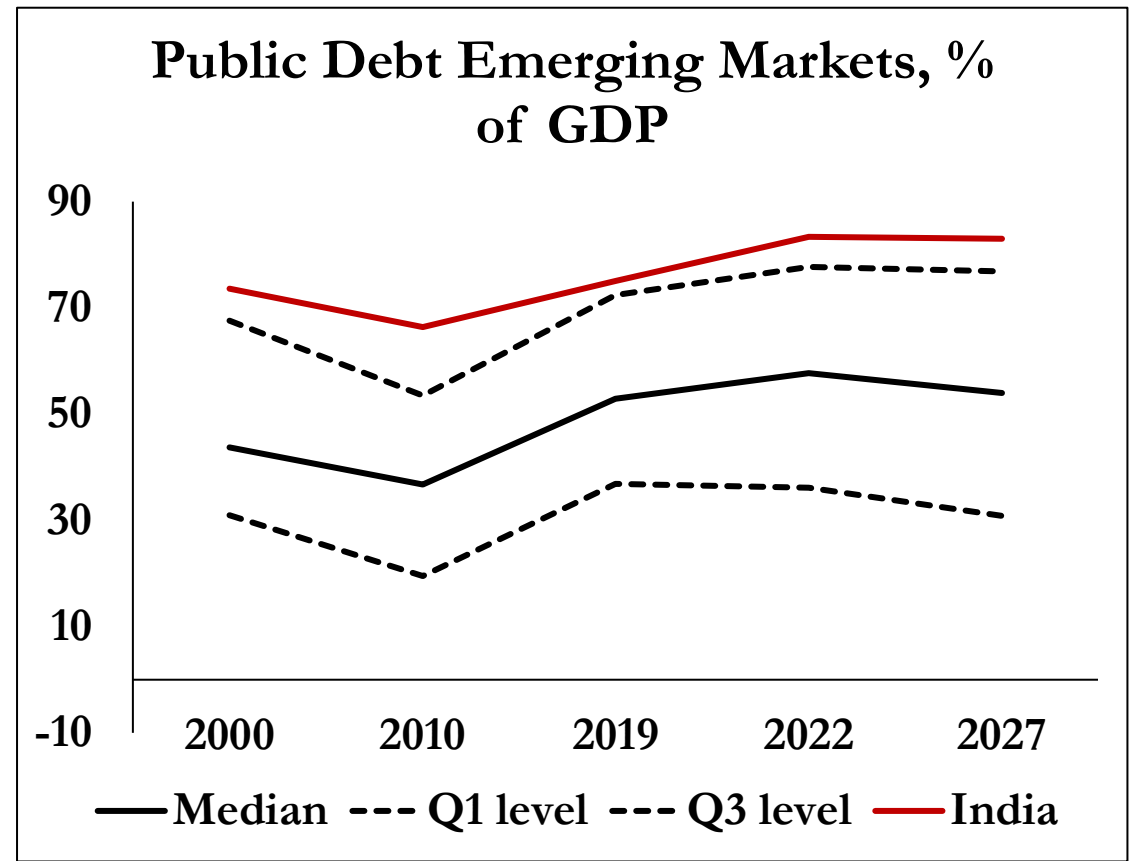


Figure B)



Interest Payments to GDP: median and interquartile range

Figure A)

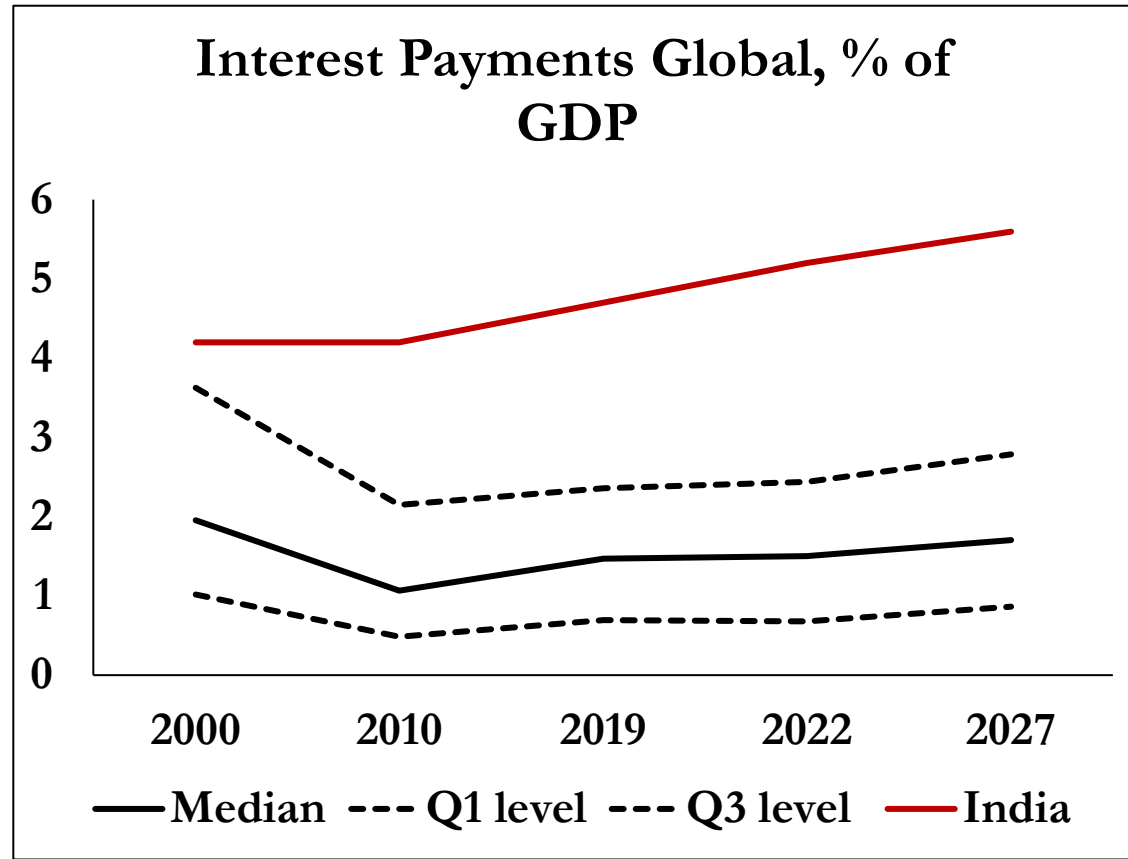
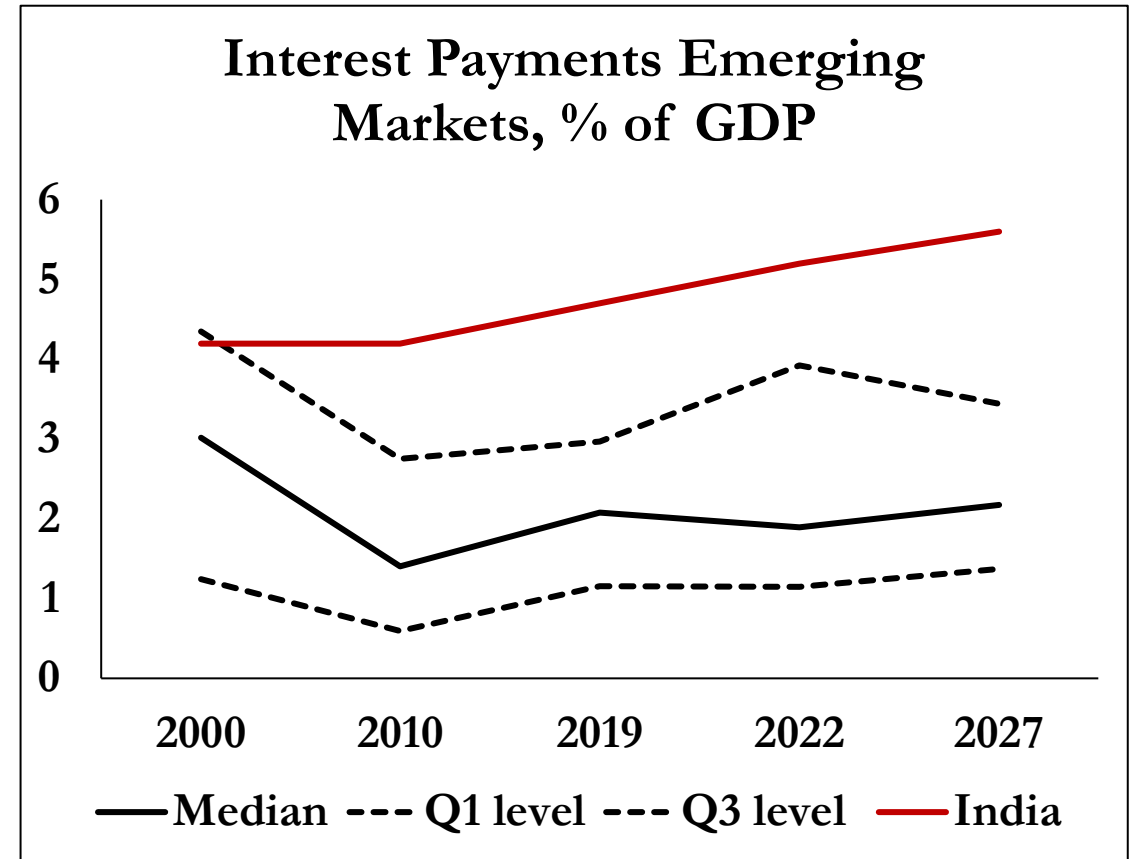


Figure B)



Fiscal deficit to GDP: median and interquartile range

Figure A)

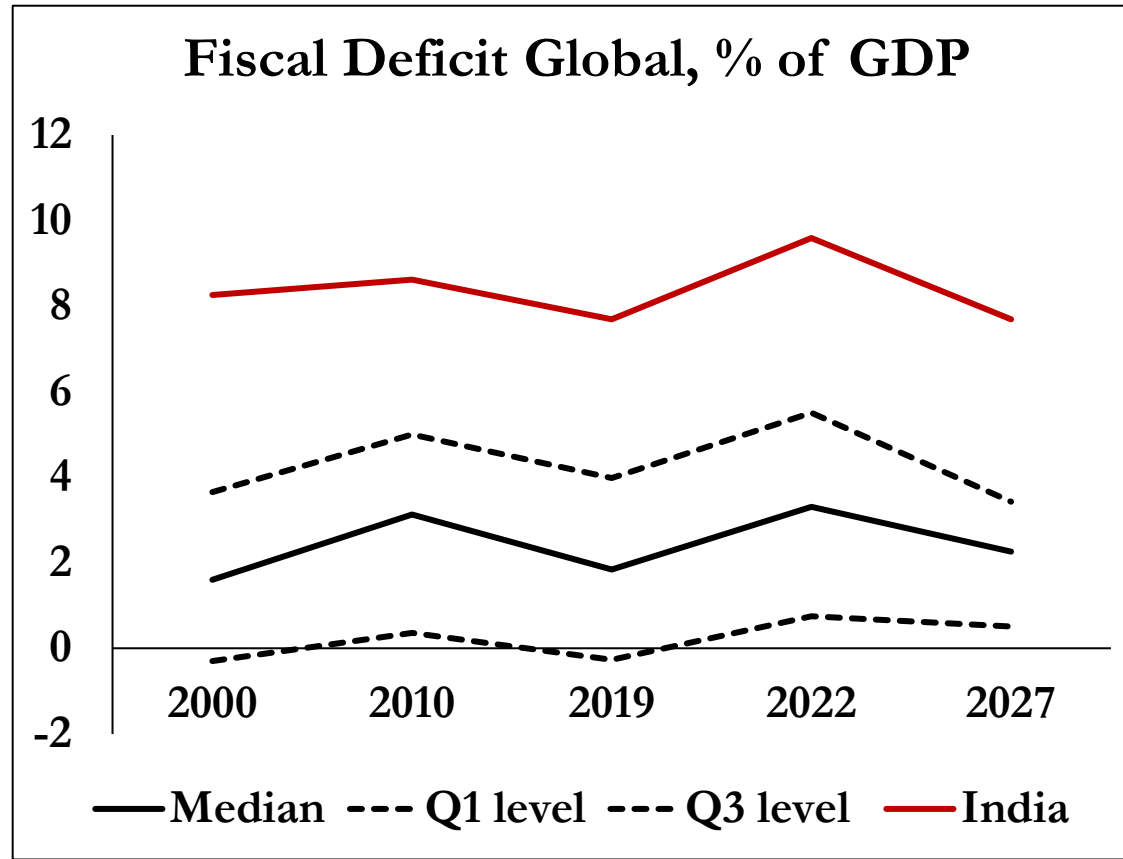
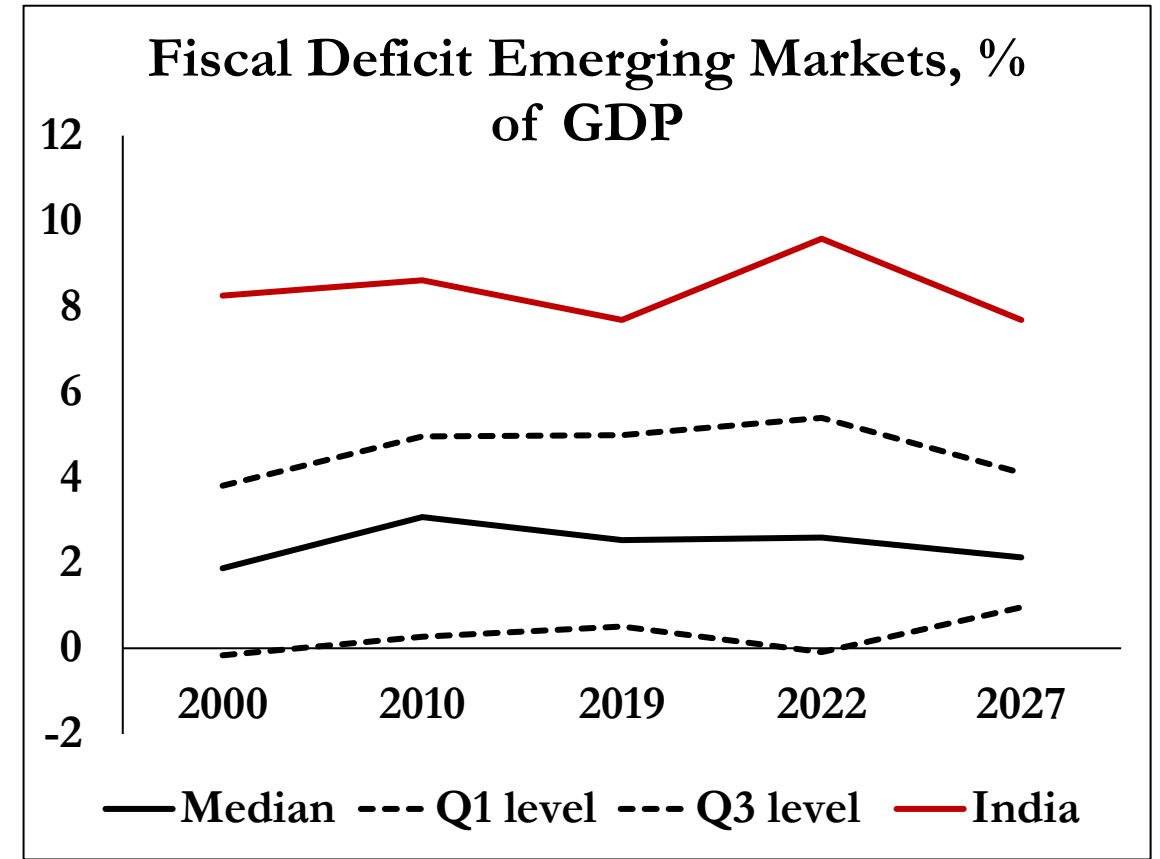


Figure B)



Primary deficits to GDP: median and interquartile range

Figure A)

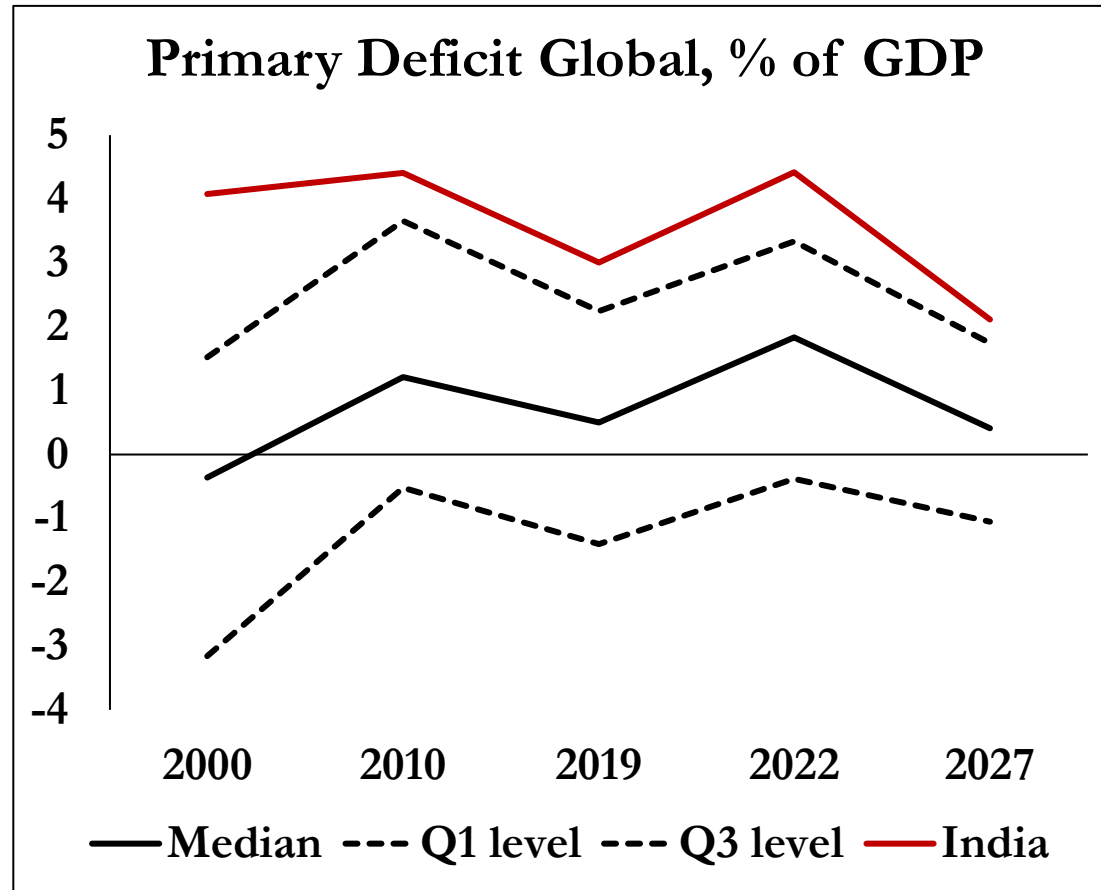
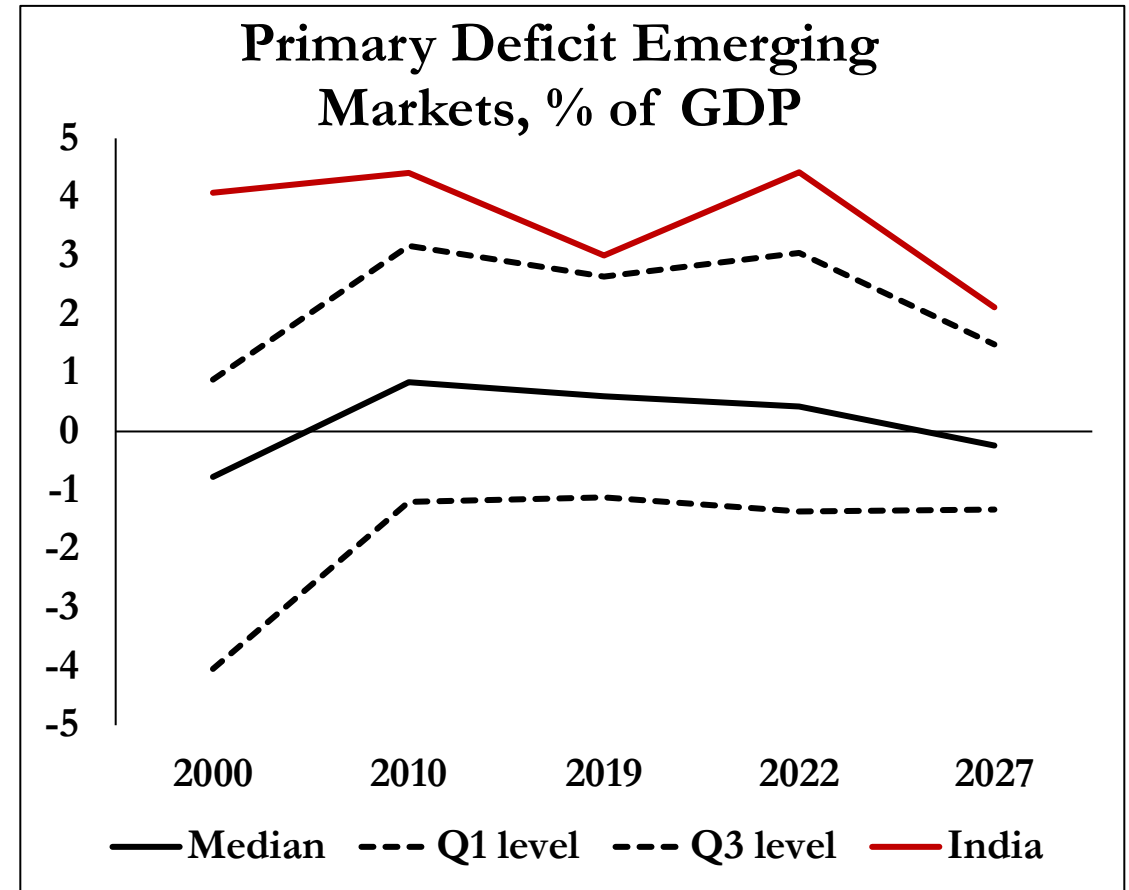
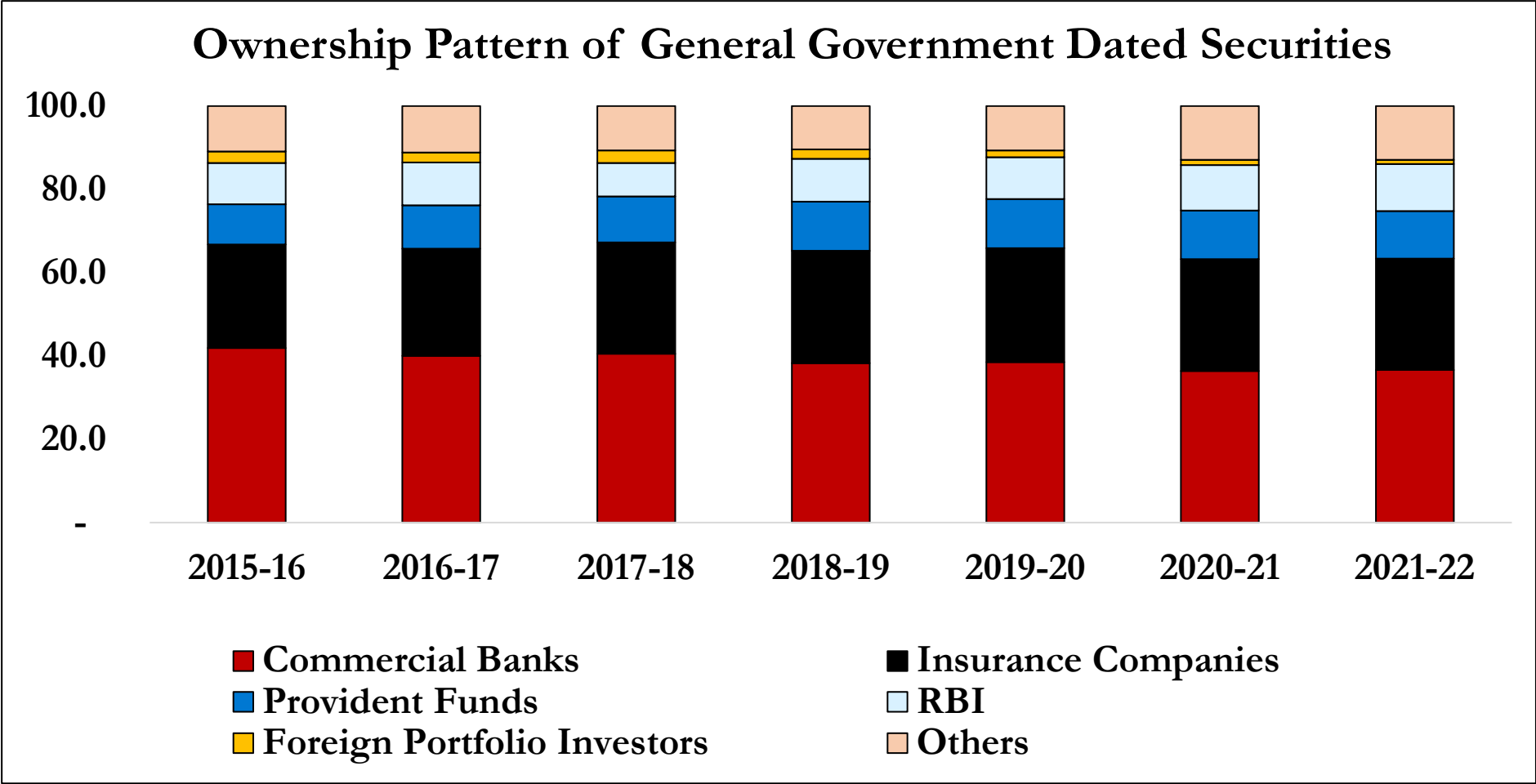


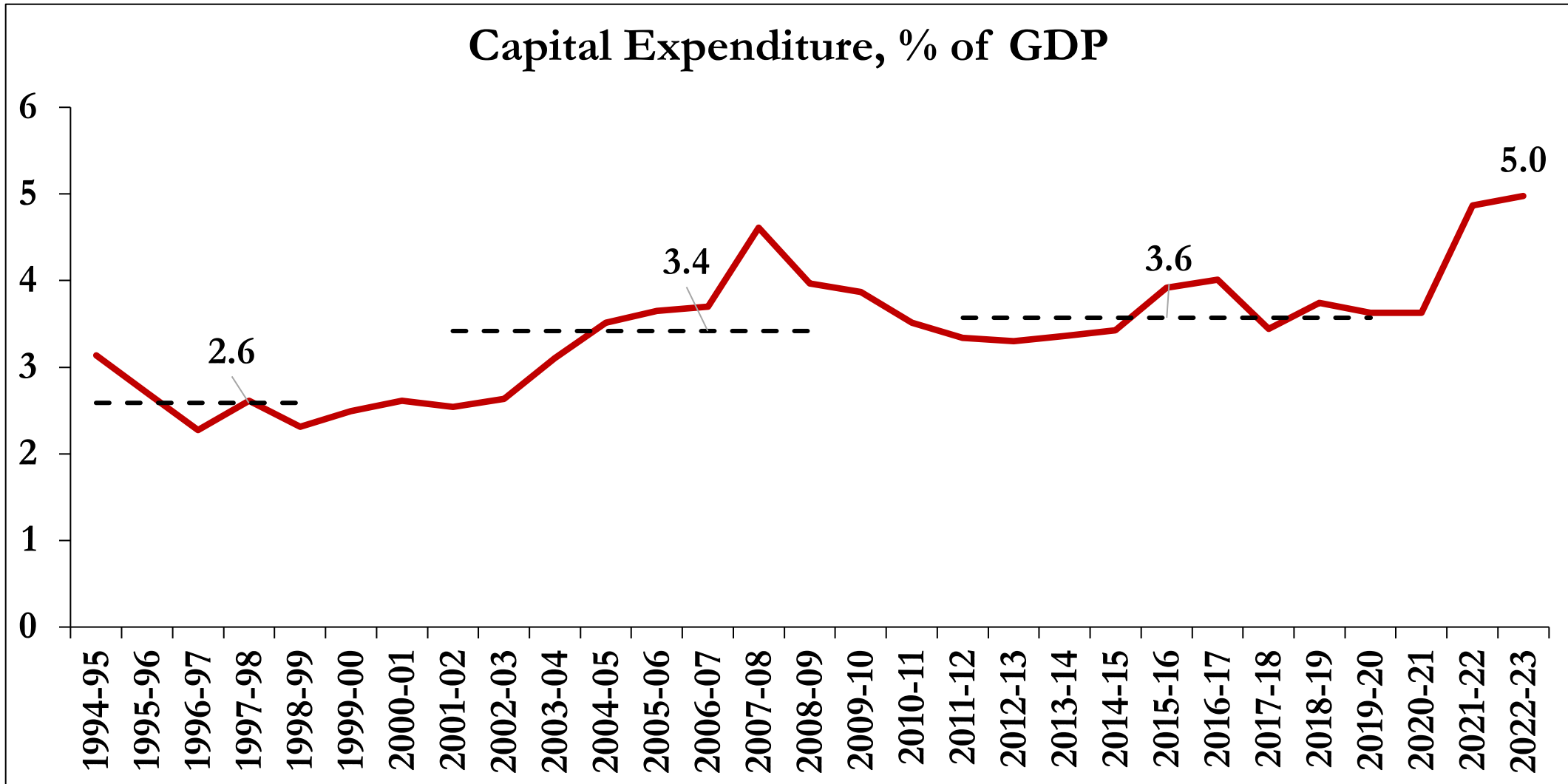
Figure B)



Ownership of debt



Capital Expenditure has increased during last two years



Cost of Debt (new issues in the year)

