Interest Payments in India's Expenditure

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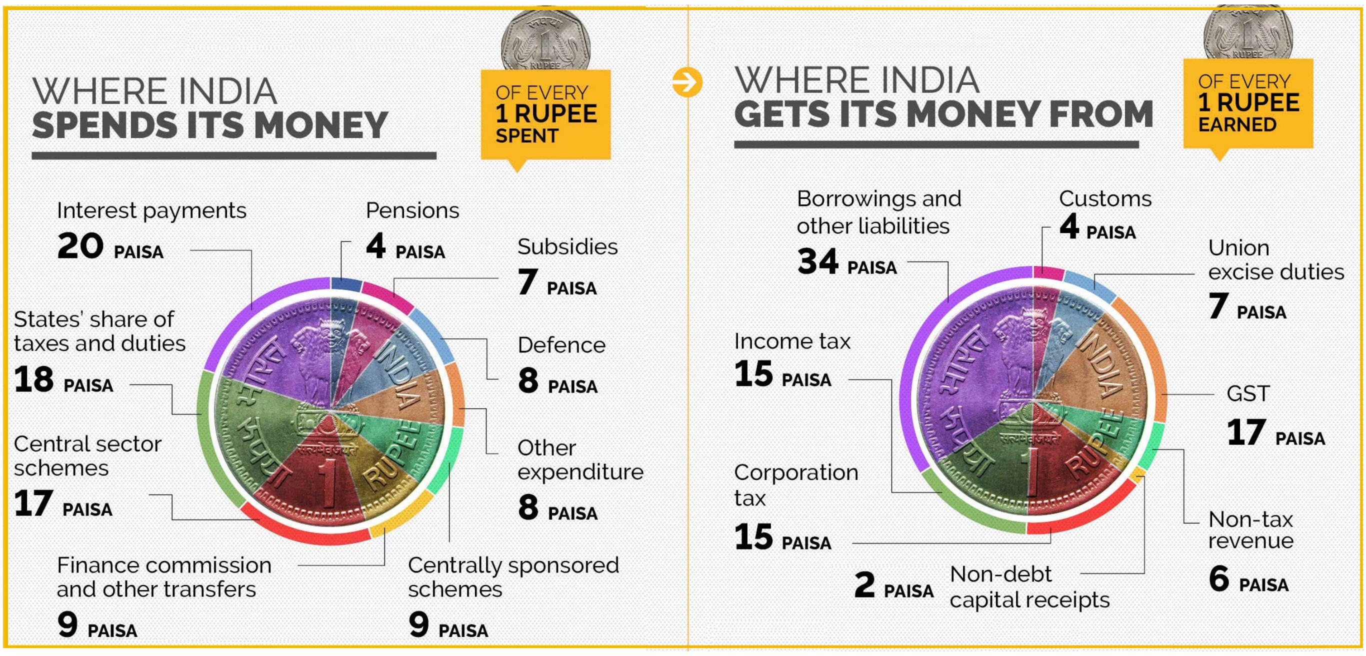
Why in news?

For the third year in a row, interest payments continue to be the single largest component of Centre’s total expenditure.

How is the picture of Centre’s expenditure?



- **Interest expense** is the cost incurred by an entity for borrowed funds it is a non-operating expense shown on the income statement.
- It represents interest payable on any borrowings—bonds, loans, convertible debt or lines of credit.
- When compared to 2018, the Centre’s interest expenditure went up by 52% to Rs 8.05-lakh crore as of FY22.
- Interest payment of the government has increased to **3.1% of the GDP** to Rs 7.31 lakh crore in 2021-22,
- **Interest payments** accounts for **20%,** the single largest component of the Centre’s total expenditure.
- **Market borrowings** through G-Secs & Treasury Bills accounts for 68% of the total sources of financing the fiscal deficit.

The Government has announced its commitment to reduce the fiscal deficit to a level below 4.5 % of GDP by FY 2025-26.

What are the factors that holding interest expenditures so high?

- **COVID led disruption** - With the pandemic-led fiscal disruption forcing the government to borrow more, the proportion of interest expenditure also went up proportionately.
- **Fiscal deficit** - Market borrowings through G-Secs & Treasury Bills accounts for 68 % of the total sources of financing the fiscal deficit.
- **Market borrowings** - Not the only source that adds to the interest burden but the small savings collections also carries higher interest burden for the government.
- **External debt** – It accounts for less than 2% of the government’s total source of funding.
- **Higher projections** - Higher projections of the Government's public finances, including a contraction in GDP/denominator.

What has the FRBM act mandated?

- **The Fiscal Responsibility and Budget Management (FRBM) Act**, 2003 requires the central government to progressively reduce its outstanding debt, revenue deficit and fiscal deficit.
- **Targets** - The central government gives three-year rolling targets for these indicators when it presents the Union Budget each year.
- The government was supposed to achieve fiscal deficit of 3.1% by 2022-23.
- In 2021-22, the government has not provided target for the next three years, and will amend the FRBM Act to accommodate the higher fiscal deficit.

Objectives

1. Reduction of fiscal deficit and revenue deficit
2. To achieve inter-generational equity in fiscal management by reducing the debt burden of the future generation
3. Achieving long-term macroeconomic stability
4. Better coordination between fiscal and monetary policy
5. Transparency in fiscal operations of the Government

References

1. The Hindu Businessline|Interest costs account for a fifth of Centre’s total expenditure
2. Business Standard|Interest payment by govt rises 3.1% of GDP