

RAA sounds alarm on debt, fiscal deficit and revenue

Tenzing Lamsang (20/11/2021)

The 2020-21 Annual Audit Report for the first time has given a lot of space to the issues of increasing national debt, rising fiscal deficits and the faster rise of current expenditure compared to revenue.

RAA has pointed to debt as one of the main issues in its executive summary itself.

Debt

The report says that a comparative analysis of outstanding debt with the GDP for the past three financial years of 2018-19 to 2020-2021 showed a constant increase in the debt to GDP ratio.

In FY 2018-19 debt was Nu 184.174 bn increasing to Nu 215.369 bn in FY 2019-20 and Nu 238.398 bn in FY 2020-21.

This means debt to GDP ratio increased from 100.57% in FY 2018-2019 to 129.06% in FY 2020-21.

A common explanation so far for debt is that most of it is hydro debt or that the increases are due to hydro debt.

However, while this explanation may have held true in the past, the composition of Bhutan's debt is increasingly tilting towards non hydro debt.

In FY 2018-19 hydro debt was Nu 142.038 bn increasing to Nu 159.359 bn in FY 2019-20 and 162.359 bn in FY 2020-21.

At the same time in FY 2018-19 non hydro debt was Nu 42.136 bn increasing to Nu 56.010 bn in FY 2019-20 and 76.039 bn in FY 2020-21.

This means that from FY 2018-19 to FY 2019-20 non hydro debt increased by 32.93% while from FY 2019-20 to FY 2020-21 it increased by 35.7%.

If this rate of increase is kept up FY 2021-2022 then Bhutan's non hydro debt will be doubling within 3 years.

This is a matter of concern as unlike hydro debt, non hydro debt is not self liquidating and it will have to be paid back from future internal revenue.

The issue in part is hydropower borrowing becoming stagnant due to the lack of new projects, P I being on hold, P II having borrowed most of its funds and Mangdechu starting to pay back its loan.

However, at the same time non hydro loan has taken on a life of its own and is even starting to match hydro loans in terms of sheer increase.

In between FY 2018-19 and FY 2019-20 the hydro debt increased Nu 31.195 bn while non hydro debt increased by 13.874 bn but from FY 2019-20 to FY 2020-21 while hydro debt only increased by Nu 23.09 bn non hydro debt increased by a whopping Nu 20.029 bn.

Of the Nu 238.398 bn debt in FY 2020-21 Nu 221.324 bn is external debt owed to foreign governments and institutions while Nu 17.074 bn debt is from the domestic market borrowed mainly from local Financial Institutions.

Fiscal Deficit

The fiscal deficit is the difference between the government's expenditure and its revenue, and the RAA report shows an increasing trend in the past few years.

To get an idea, fiscal deficit increased from Nu 545 mn in FY 2017-18 to 2.743 bn in FY 2018-19 to 3.385 bn in 2019-20 and a whopping Nu 11.139 bn in 2020-21.

RAA says this increase happened due to increasing public expenditure with unmatched revenue growth.

It says this gap between resources and spending has to be ultimately financed by government borrowings resulting in a huge public debt leading to a public debt burden due to a high finance cost.

RAA says such an imbalanced fiscal condition, if not corrected in time may impede the country's economic growth and fiscal sustainability.

The RAA advises the MoF to initiate measures such as rationalization of government expenditure, mobilizing additional resources through grants, raising of domestic revenues by increasing the tax base and practicing sustainable debt management to strengthen the country's fiscal sustainability.

A source said in the past it was the practice to keep the fiscal deficit at around 3% of the budget and at the end of the FY there usually would be no deficit as either revenue would be higher or the expenditure would not be as much, but this government increased it to 5% which would make it difficult to achieve the same result.

Increase in recurrent expenditure more than revenue

The RAA says that Article 14 of the Constitution says 'the government shall ensure that the cost of recurrent expenditure is met from the internal resources of the country.'

It also points to section 7(a) of the Public Finance Act 2007 which states, 'the recurrent expenditures shall be met from the internal resources of the country.'

The RAA says on analyzing the data of the last five years comparing internal revenue and expenditure while the above have been met, it found that the trend shows a faster increase in recurrent expenditure more than the increase in internal revenue.

In FY 2017-18 the internal revenue was Nu 36.871 bn with Nu 27.494 bn in recurrent expenditure. In FY 2019-20 the internal revenue was Nu 36.218 bn with Nu 33.023 bn in recurrent expenditure and in FY 2020-21 the internal revenue was Nu 35.855 bn with Nu 31.889 bn in recurrent expenditure.

In FY 2020-21 the portion of internal revenue consumed by recurrent expenditure was 88.94% leaving only a small portion for capital expenditure and loan repayment.

Even this 88.94% was achieved after a lot of government cut backs in the recurrent expenditure of the government.

RAA says more than 50% of the capital expenditure and loan repayments were covered by grants and borrowings in the last four years showing that internal revenue was not enough and the government even had to borrow and incur the additional cost of interest.

The RAA says such an imbalanced situation with rapid growth in recurrent expenditure compared to the internal revenue will widen the fiscal deficit leading to increasing debt and ultimately adversely impacting the national goal of achieving economic self-reliance.

The MoF in response says the ministry has been making efforts to maintain the increase in recurrent expenditure through adoption of numerous austerity measures. It says the increase in recurrent expenditure is mainly due to increase in salaries due to annual increments, annual inflation and revision in tariffs of utilities, expansion in human resources and new establishments.

It says in FY 2018-19 the substantial increase in recurrent expenditure by 18.92% was due to the pay hike then. Furthermore, since then allocation to pay and allowances accounted for 55% of total expenditure.

It says that recognizing the concern over the growing recurrent expenditure the MoF has introduced the allocation of the current budget in block grants which brings about flexibility in the judicious use of scarce resources.

The RAA said a high proportion of internal revenue being consumed by recurrent expenditure shows the syndrome of dependency on grant and borrowing. It said grant is driven by foreign donors with no certainty in terms of timing or cash flow while borrowing leads to a huge public debt with long term negative impact on economic sustainability.

It says it is imperative to make a more realistic revenue forecast and take appropriate steps to control increase in recurrent expenditure.

Finance Minister responds

The Finance Minister Namgay Tshering said, “We do not have to worry about non-hydro debt as whatever we have borrowed is as per the 12th FYP plan and without the resources being met it is very difficult to frame the plane. So whatever is the deficit we have borrowed internally and externally, but we have not borrowed beyond that.”

Lyonpo said that if they borrow now it will be a project based borrowing and not program based borrowing.

In a project based borrowing they want to invest in a productive economic sector where there is an assured return on investment which will help the economy to revive.

“If our economy is to revive we should not shy away from investing.”

“Being a Least Developed Country (LDC) as you graduate in 2023 the lending terms will change and it will become a little expensive and not affordable for an economy like Bhutan. I think it is better for us to capitalize on this current status,” said Lyonpo.

Lyonpo said the government is not borrowing to meet the recurrent expenditure but to make an investment.

“So if a country is to develop, and during such a time if we are to go back into recovery then a massive investment is required,” said Lyonpo.

The minister said non hydro borrowing has been taken in the past mainly to meet the budget deficit and for budgetary support under program borrowing.

He said such non hydro borrowing goes into farm roads, black topping roads etc.