

GST shortfall: Centre to borrow ₹1.1-lakh cr and on-lend to States

'Administratively' easier move to keep yields under control; many advantages for States, too

OUR BUREAU

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To meet the GST compensation cess shortfall, the Centre will borrow on behalf of all the States, and then on-lend to them. This will be done on the lines of funding of 'externally aided projects'.

The amount will be given to the States as back-to-back loans in lieu of GST compensation cess releases. This administratively easier borrowing arrangement will be done through a special window and has many benefits for the States, including better interest rates (rather than different rates) and will need to borrow lower amounts for funding the Atmanirbhar package.

Now, the Centre will borrow the estimated shortfall of ₹1.1-lakh crore (assuming all States sign up) through the special window in tranches and on-lend to States.

"It is just like what the Centre does for externally aided projects by borrowing from institutions like World Bank and ADB and then lend to States. It will not be on the books of the Central Government, which means there will be no impact on its fiscal deficit," a Finance Ministry official said.

Sweetening the deal

- Borrowing will be along the 'externally aided projects funding' model
- There will be no impact on the Centre's fiscal deficit
- Will avoid differential rates of interest that individual States may be charged for their respective SDLs
- Will be an easier arrangement from an administrative viewpoint



The official explained that if each State were to borrow separately, there would be too much of a fluctuation in the yield rates (on State Development Loans, or SDLs). But if the Centre does a consolidated borrowing, the rate will be much lower.

The official also said the borrowing will be for three-four years and the interest and principal will be repaid out of the compensation cess fund. The GST Council has already extended levying of the GST compensation cess beyond June 2022.

Also, the States that get the benefit of the special window are also likely to borrow considerably less via the additional facility of 2 per cent of GSDP (from 3 per cent to 5 per cent) under the Atmanirbhar package, the Finance Minister's office tweeted on Thursday.

An official release said this arrangement will not impact the Centre's fiscal deficit. The amounts will reflect as capital receipts of the State governments and as part of financing

of their fiscal deficits, the release said. The General Government (States+Centre) borrowings will not increase by this step, the release clarified.

It may be recalled that under Option 1, States could borrow ₹1.1-lakh crore for GST shortfall through a special window and, over and above that, raise from the open market 0.5 per cent of their GSDP. The increased OMB came as a relaxation of the reform conditions that were stipulated for eligibility. Additionally, under Option 1, the States are also eligible to carry forward their unutilised borrowing to the next financial year.

Experts' view

Divakar Vijayasathy, Founder and Managing Partner, DVS Advisors LLP, said the Centre borrowing ₹1.1-lakh crore should not be interpreted as the government yielding to the requests of the States. What is raised by the Centre "would be passed on to the States as back-to-back loans and would not have any impact on Central

Government's fiscal deficit. This would still stand as the liability of the States. The dissenting States wanted the Centre to absorb the liability without passing it on to States. The Centre has stuck to its ground and borrowing in its name is only for operational convenience and it should not be construed as the Centre yielding to the States. The dissenting States have indicated that they will knock at the doors of the judiciary and a legal battle is set to take place. The Attorney-General's opinion would be tested in the courts now," he said.

Jayanta Roy, Senior Vice-President and Group Head, Corporate Sector Ratings, ICRA, said: "This step will reduce the supply of State bonds in the second half of FY21, from the level that was earlier being anticipated. Moreover, the cost of such borrowings would go down. In conjunction with the plan to conduct open market operations in State Development Loans that has been announced by the RBI, such measures should help ease SDL spreads."

Congress welcomes move

"If the Centre has decided to borrow the ₹1.1-lakh crore and extend it to the States as a back-to-loans, I welcome the change of position. I thank all economists, academics and newspaper editors who supported our position," said senior spokesman for the Congress P Chidambaram, a former Finance Minister.