Chapter 1

Domestic Debt of the Central Government in India:
Introduction, Problem Identification and Research Objectives

1.0 Introduction

Fiscal imbalance continues to be the most intractable problem for both the central and the state governments in India. Correcting fiscal imbalances, while continuing to achieve growth objectives, has long been the foremost concern of policy makers and fiscal experts in the country. In this context, it is well recognised that control over and reduction in fiscal deficits is necessary to restrain build up of high level of national public debt in the country. The financial position of the central government, which the study specifically aims to address, is of particular concern as it has a greater potential of creating macroeconomic instability than the sub-national public debt. There is a widely held consensus that the fiscal stance of the central government in recent years has been unsustainable. Apart from the uncomfortably high level of central government total liability, the internal/domestic liability (of the two broad components of aggregate liabilities viz. internal/domestic liability and external liability) is accumulating rapidly.

Along with the rising level of fiscal deficit, the revenue deficit which determines the quality of fiscal adjustments is also deteriorating. The resource mobilisation through taxation and non-taxation has failed to match the size of government expenditure. The increasing proportion of revenue deficit in total deficit implies that the increase in total expenditure is more from the revenue account. This indicates a diversion of capital receipts to meet the revenue expenditure. The government borrowings, which form a major source of capital receipts, get absorbed in incurring revenue expenditure. With the revenue expenditure being less yielding and associated with interest liability have led to a rise in the financial burden of the central government. Further, not only the increase in domestic

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1The distinction between current expenditure and capital expenditure is usually made with reference to the creation of productive physical wealth. Capital expenditure consists of those government outlays that result in the enlargement of physical productive capacity of the economy either directly through government investment or indirectly through provision of investment grants to the private sector. Those outlays not directly productive are included in the current expenditure.
liability of the central government has implications for the monetary policy scenario of the country, but also the liberalised monetary policy regime of recent years has got implications for the fiscal scenario. The latter, in some years, has led to a rise in the cost of fiscal adjustments.

The "Fiscal Responsibility and Budget Management Bill (FRBMB, 2000)" was introduced at an appropriate time. The bill was perceived to be a desirable policy move on the part of the central government on the same line as proposed for the European countries in the Maastricht Treaty. In India the FRBMB was proposed for a prudential fiscal/financial management of the country and also as a policy measure to restrain the inefficient and ineffective use of resources. The bill was introduced with a view to complying with certain macro fiscal objectives of the country such as maintaining stabilisation (removing fiscal impediments in effecting the conduct of monetary policy and prudent debt management policy consistent with fiscal sustainability) and achieving higher rate of economic growth in keeping with intergenerational equity principle in perspective. In addition to many other measures for fiscal correction, the bill stipulated a set of fiscal rules which required the central government (a) to eliminate the revenue deficit (or rather build up of a revenue surplus) and to target an overall fiscal balance (subject to a fiscal deficit limit of 2 per cent of GDP) as of 2006; (b) to limit yearly issue of guarantees to half a percentage of GDP; to reduce the total liabilities to half a percentage of GDP by 2011; and (c) to abstain from borrowing from the Reserve Bank of India (RBI) effective from the year 2004 (GOI, 2000, Kopits, 2001; Mujumdar, 2002). Effective fulfilment of these conditionalities depends on how well the government implements its budgetary policies. Subsequently, it is observed that the government has continuously failed to keep up with the targets set in line with the proposed fiscal

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2 The treaty for European Monetary Union (EMU) was proposed in order to comply with certain fiscal convergence criteria for forming an integration of the European economies. This was with a view to enable the individual member countries and the union as a whole economically stronger and viable (Bougrine, 2000).

3 The vision of the FRBMB as stated by the Department of Ministry of Finance of India was to provide for the responsibility of the central government to ensure the inter-generational equity in fiscal management and long-term macro-economic stability by achieving sufficient revenue surplus, eliminating fiscal deficit and removing fiscal impediments in the effective conduct of monetary policy and prudent debt management consistent with fiscal sustainability through limits on the central government borrowings, debt, deficits, greater transparency in fiscal operations of the central government and conducting fiscal policy in a medium-term framework and for matters connected therewith or incidental thereto (GOI, 2000).
norms. This led the policy makers to revise the bill in 2004 by extending the time frame to March 2008 to meet the goals as set out earlier.

This gives an indication that despite several policy measures undertaken in the past by the central government, at times in co-ordination with the monetary authority of the country, the government has not been able to curb the rising level of deficits. The rapid build up of domestic debt of the central government has given rise to the emergence of several critical issues. Many authors opine that such a rise in public debt is a threat to the solvency of the treasury and viability of the economy (Rakshit, 2000). In this context, the emerging issues can broadly be outlined as follows, to bring out a consensus regarding the possible consequences of rising level of public debt.

1.1 Domestic Debt of the Central Government in India: Problem Identification

In the context of an increasing domestic debt and heavy reliance on domestic sources of borrowings by the central government, in recent years, many economists postulate that the country may be heading for an “Internal Debt Trap” i.e. a situation in which borrowing has to be resorted to often just to keep up with the servicing of debt. It is also feared that a situation may come, even without a rise in the interest rates on government securities and treasury bills, when the central government would have to borrow money just to pay for the amortisation and interest payments on past domestic borrowings (Seshan, 1987). Such perceptions necessitate a critical examination of the trends and composition of domestic debt of the central government. One of the objectives of the study is to make an extensive review of the existing scenario.

Along with the persistent rise in domestic debt of the central government in India, there is another component of domestic liability which is recently evolving and accelerating the financial pressure on the central government (Lahiri et.al, 2000). This arises on account of the central government’s guarantees, counter-

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4 In exercise of power conferred by the FRBM Act 2003, the central government framed FRBM rules effective July 2004. The government has made a commitment in the revised FRBM to wipe out the fiscal deficit in a phased manner over the period ending March 31, 2008 (as stated in Annual Report 2003-04, RBI).
guarantees and indemnities constituting contingent liabilities of the central
government in respect of the state governments and other private and public sector
undertakings. In many instances, the state governments, private and public sector
undertakings default in repaying the guaranteed loans. One of the reasons could be
due to their financial distress. Ultimately, the central government has to shoulder
the responsibility of clearing off these debts contracted in the past. Although these
liabilities are not accounted for as part of the total liability in the current accounting
practice, in actuality, they form a part of the liability of the central government and
thereby intensifying its total debt burden.

In the literature related to the debt trap consequence, usually addressed in
an environment of chronic fiscal deficits, is the issue of sustainability. Unsustainability of public debt is usually referred to as a long-run problem in fiscal
policy which forms a core issue in public finance. When the internal debt trap
continues for a longer period of time, it raises the possibility of unsustainability of
public debt. Then a situation comes when the individuals would be unwilling to lend
to the government. As we know that accumulated net fiscal deficits constitute total
debt of the government; the increase in deficit and in turn, debt, would call forth
not only the question of unsustainability of debt but also unsustainability of the
overall fiscal policy of the country. To make the term sustainability more explicit,
following Wilcox (1989) one may define it as a situation where the government is
able to borrow money as long as it is able to repay the debt. Technically, this is
possible if private sector savings grow faster than the growth rate of public debt. It
can be shown that this is possible as long as the growth rate of the economy exceeds the rates of interest. This is because private sector savings⁵ are related to
the growth rate of income/output (higher the level of income, higher would be the
savings) and growth rate of public debt is related to the interest rate on the
government borrowings (at a higher rate of interest, growth of debt would be
higher). Another important consideration to bear in mind is that sustainability
cannot merely be ensured only when the private sector savings grow faster than
the growth rate of debt, but how the private sector wants to put its surplus money
is also important. In particular, whether the private investors go in for buying

⁵ The surpluses out of current private income represent private sector savings in the present period.
government securities/financial assets or physical assets or investing in other assets? Thus, the decision of private savers acts as a binding constraint for the government to raise loans. A binding constraint may be avoided if the government is able to repay the debt on maturity and as per the market terms. As quoted by Sobhee (2000), the World Bank defines "a debt burden is sustainable when a country is able to meet its current and future debt obligations in full without recourse to relief or rescheduling debts of the accumulated arrears or without unduly compromising economic growth". But this does not happen in the context of developing countries. In a broader sense, sustainability is understood in terms of stability of the debt-to-GDP ratio in the short and medium term with the ratio tending towards zero in the long-run. In the Indian context, since there is a steady rise in the stock of domestic debt of the central government, it is worth examining the question of sustainability.

Three important concerns arise from high level of public debt. The first one relates to the amount of interest burden likely to arise on account of borrowings made by the government. The second concern relates to the problem of continuing deficits and the explosion of debt-to-GDP ratio which has implications on sustainability.\(^6\) Thirdly, whether debt-financing affects macro-economic indicators and if so, in what way?

**The Impact of Public Debt: Contrasting Views**

The last one is a serious concern. In India there have been debates pertaining to the implications of rise in domestic debt on the aggregate economic activities. This is to be examined by assessing the overall impact of domestic public debt on the economic activities. This would get reflected in *crowding out/in* of private investment and also other macro economic variables viz. prices (inflation), interest rates, private consumption and output. The impact of domestic debt is interrelated with the sustainability of debt issue. When public debt is unsustainable, it may have more adverse impact on the economic activities than when it is sustainable. Besides the direct impact of public debt on real economic activities,

\(^6\) The earlier studies have evaluated sustainability of public debt from the perspective of impact of public debt on economic activities. The recent studies evaluate sustainability from the government’s solvency position i.e. given the financial position whether it is feasible for the government to continue with its fiscal operations.
there are several indirect channels through which the impact of domestic public debt is felt on the real economic activities. For instance, given a fixed amount of supply of credit in the economy, high level government borrowings may crowd out private investment directly because of the unavailability of credit to the private sector and indirectly via raising the rate of interest in the economy. In India crowding out might not be taking place through the transmission channel of interest rates as the economy was operating under a repressed financial regime for a long period of time. The credit channel, i.e. availability of credit, might be a more relevant channel of crowding out in the context of India as emphasized by the exponents. Crowding out might be occurring directly through the preemption of resources (both financial as well as real resources) from the private sector. However, if the economy is operating under excess capacity, debt-financed government expenditure, particularly on infrastructure projects is likely to produce crowding-in rather than crowding-out effect. This would boost up aggregate demand and capacity utilisation. Capacity utilisation leading to an increase in income and profits of the private sector, would lead to a rise in real investment. This way of fiscal expansion would not only help increase current investment and output but also the long-term potential growth rate of the economy.

**New-Classicals’ Perspective**

In contrast to the above view, New-Classical economists who believe in Ricardian Equivalence Theorem (RET), assert that public debt does not produce any concrete economic impact. Consumers respond in exactly the same way to a change in government deficits as to the changes in taxes. Therefore, a tax reduction bond-financed increase in government expenditure wouldn’t have any net impact on the economy. In other words, a tax reduction bond-financed increase in deficit merely defers taxes into the future. Thereby, the overall level of private consumption, savings, investment and real interest rates remains unaltered. However, this theorem has later been challenged by several economists (refer Chapter 2 for a detailed review).

REFERENCE

AND ARCHIVAL SECTION
Monetarists' Perspective

In India, the Central Bank, known as the Reserve Bank of India (RBI) helps the government in the matters of exercising fiscal policy, however, the monetary policy has been used as part of fiscal policy. Given this scenario, economists view the consequence of an increase in government debt from a monetarists’ perspective as viewed by Sargent and Wallace (1981). In monetarists’ view, the bond-financed increase in expansionary fiscal policy is prone to more inflationary spiral than the money-financed expansionary fiscal policy (although money-financed is a consequence of bond-financed deficit). In monetarists’ analysis, the increase in bond-financed deficit at a certain point requires to be monetized. Monetisation of debt resulting in expansion of money supply (growth of high power money) leads to an increase in the price level. According to the monetarists, like Friedman (1968), monetary authority gives more priority to interest rate stability than price stability. In a situation of higher rate of interest in the economy (resulting from increase in bond-financed public expenditure), the monetary authority tries to accommodate the fiscal policy through printing of notes in order to stabilize the interest rates resulting in an increase in money supply and a consequent upward pressure on price level resulting in price instability. Even if the monetary authority does not accommodate the fiscal policy, given a level of savings in the economy, an increase in government demand for credit, leads to an increase in domestic interest rate. Hence, there is a possibility of crowding out of private investment.

Another striking outcome following from the rise in interest effect of bond-financed government deficit is that the increase in interest rate leads to the appreciation of exchange rates of foreign currencies. The exchange rate appreciation dampens the export performance of domestically produced goods and services, which in turn leads to increase in deficit in the current account of the balance of payments by way of discouraging exports. Therefore, the rise in domestic public debt affects external balance of the economy. Mounting Public debt also influences income levels of individuals across generations, thereby affecting the intergenerational redistribution of resources in the economy (Buchanan, 1958).
Emerging Issues:
Thus, on the basis of above discussion, some of the emerging issues can briefly be outlined as follows:

(1) The growth of domestic debt of the central government and its changing pattern of financing in India has a bearing on the financial burden of the central government.
   (i) The growth of government debt in favour of costly forms of domestic debt results in increase in interest burden. The rising debt service burden reflects an ever-widening fiscal deficit.
   (ii) This raises the possibility of the central government getting into an internal debt trap situation and debt becoming unsustainable.

(2) The system may react to a severe squeeze on government finances in future through a collapse in expenditure on essential public services including maintenance of infrastructure, which is bound to an adverse impact on growth.

(3) The government may be forced to monetize the deficits to avoid higher interest rates, but this has implications on inflation rate, exchange rate and the resultant external imbalance and distortions in the economy.

(4) There are implications of rising domestic public debt for the aggregate economic activities - for instance, crowding out/in impact of public debt on private consumption and investment. The accentuation of crowding-out phenomenon, again has implication for decelerating growth.

(5) The government may be forced to impose higher taxes in the future to service the expanding size of debt burden, in which case the expectation of higher taxation can discourage investment and encourage capital flights from the economy.

1.1 Researchable Issues and Research Gaps
With a persistent rise in government of India’s level of deficits and domestic debt, the following important issues emerge in this context.

- The first one relates to whether such a continuous rise in debt is sustainable. In other words, whether this rise in debt would be
consistent with the macrofiscal policy objectives of stabilization and higher growth rate of the economy.

- The second issue, given the trends and pattern of growth of domestic public debt, concerns the possible impact it can produce on the major macroeconomic variables (in a closed economy as well as in an open economy context). A higher debt-to-GDP ratio may be sustainable but it may have adverse impact on investment, and economic growth rate.

- Third, whether anything went wrong with the past policy prescriptions which have led to such proportion of fiscal imbalance in the country and what needs to be done keeping in mind longer term fiscal policy perspective.

- Another important issue addressed several times at the theoretical level by many economists like Auerbach et al. (1991), Kotlikoff (1992) and Blanchard and Fischer (1989) is the intergenerational debt burden. Whether the burden is equally distributed across generations? At the empirical level, few studies have examined this issue. However, focusing on the distribution of debt burden is not the concern of the present study as it is a complex issue which needs to be addressed separately.

These are some of the important researchable issues which attracted a lot of research and policy attention among the economists and the policy makers, in developed as well as in less developed countries over the past few decades. There are many studies looking at the trends and causes of growth of public debt in the Indian context but there are limited studies at the empirical level specifically looking into the sustainability aspect of domestic debt of the central government from a long-term fiscal perspective (a detailed empirical review of literature is presented in Chapter 2). The studies by Gupta (1992), Buiter and Patel (1992), Rajaraman and Mukhopadhaya (2000) and Moorthy and Singh (2000) considering short period time series have evaluated the question of sustainability of fiscal policy in the Indian context. Gupta (1992) and Buiter and Patel (1992) have examined sustainability by various time series techniques such as Dickey-Fuller, Augmented Dickey-Fuller and Phillips-Perron unit root tests. Rajaraman and Mukhopadhaya (2000) have applied autoregressive integrated moving average (ARIMA) model for forecasting the level of debt. Moorthy et al. (2000) in order to examine the issue of sustainability, have
examined Domar's (1944) growth rate cross over formula. But by definition, sustainability is a long run issue. For assessing sustainability the length of time period should also be reasonably long. Further, if one could broadly divide the domestic debt into various components such as market borrowings arising on consolidated fund of India and other liabilities arising on public account, then it would be more relevant for policy purpose to examine which components of domestic debt have got more potential for making the fiscal policy more vulnerable. In this direction, hardly any study has made an attempt. The time coverage period considered for the study is longer than what had been considered in the previous studies. By considering a longer time period the present study tries to take care of the definitional aspects of sustainability for assessing the sustainability of domestic public debt in the Indian context. Although there are studies by Gopalakrishnan (1991), Mohanty (1995) and Singh (1998) which have specifically looked into the impact of public debt on private consumption and savings at the macro level, hardly one would find any comprehensive study undertaken with respect to private consumption and private investment (later measured in terms of gross domestic capital formation) as dependent variables in tandem with all other relevant macro-economic determinants. This is expected to give a broad idea about the impact of public debt on the economy. In accordance with the implications, policy actions could produce desirable results in terms of sustainable growth of the economy, if implemented.

1.3 Objectives

Given this background, the study focuses on the sustainability of domestic debt of the centre and its macro-economic impact on private sector activities. The study has the following set of specific objectives.

1. To examine the growth and composition of central government domestic debt inclusive of its contingent liabilities.
2. To critically evaluate the domestic debt and interest rate policy- before and after the financial liberalisation of the economy.
3. To assess the sustainability of domestic public debt.
4. To examine the impact of domestic public debt on the key macro-economic variables viz. private consumption and private investment.
5. To draw policy implications.
1.4 Database and Methodology

For collecting and compiling the required data, the study primarily relies on reports of the Reserve Bank of India (RBI), Central Statistical Organization (CSO), Ministry of Finance and National Institute of Public Finance and Policy (NIPFP). The specific data collected from a particular source and the way it is computed are mentioned in respective chapters.

The study uses both descriptive statistics and econometric techniques to analyse the above objectives. In order to examine the first objective, a time series analysis of trend and composition of government domestic debt in India is attempted. The measure of debt burden and the factors that influence the rise in domestic debt of the central government are discussed with the help of simple ratios and percentages.

For evaluating the second objective, a critical analysis of public debt policies and interest rate policies followed in India is undertaken. In order to empirically examine the third objective i.e. an assessment of sustainability of central government domestic debt along with relevant indicators, unit root test of time series analysis is applied.

For examining the fourth objective i.e. regarding the macro-economic impact of domestic public debt, the study assesses the impact of public debt on the key macroeconomic variables such as private consumption and investment. The relationship between public debt and private consumption is investigated keeping in mind the net wealth impact against no net wealth impact of public debt. The relationship between public debt and private investment is examined aiming at establishing the complementarity/competitive relationship between government borrowings and private investment in the economy. The relationship in many previous studies is analysed either under the neo-classical or standard Keynesian framework. Under the Keynesian framework, the influence of government borrowings on private investment is examined via rate of interest. If government borrowings positively influence the rate of interest, studies conclude that there is crowding out impact of government borrowings on private investment. But this may not give a concrete picture about the relationship between government borrowings
and private investment. Even if there is an adverse impact of rate of interest on private investment as a result of increase in government borrowings, the adverse impact may get nullified due to other incentives to invest. Therefore, the study tries to directly examine the relationship between government borrowings and private investment along with other relevant factors in the model. This would help us determine, if any, impact of government borrowings on private investment.

For the empirical analysis of the fourth objective, an appropriate time series econometric technique is employed. The study relies on the autoregressive distributed lag (ARDL) approach to cointegration. The ARDL model is used for the reason that this is suitable to establish the dynamic impact of domestic government borrowings on aggregate economic activities. The government borrowings may not have immediate impact on the economy. The economic activities may respond to the change in government borrowings with certain time lags. By considering appropriate time lags, the model incorporates the role of expectation of different economic agents viz. consumers and investors. Modeling through ARDL approach to cointegration, inter alia, the study contributes to the existing literature. The fifth objective is to draw policy implications on the basis of empirical results and the analysis of past fiscal policies followed in India.

1.5 Scope of the Study
Debt of a government refers to the financial obligation on the part of the government contracted and discharged in accordance with certain terms and conditions attached with its incurrence. In a broader sense, government of a country should refer to general government and all the public sector undertakings. But the study confines only to the debt of the central government of India which excludes debt of the state and union territory (UT) governments, central public

\footnote{Later the ARDL approach to cointegration results is verified with Johansen's cointegration and vector error correction results for private consumption model. The same is not verified for private investment model because Johansen's cointegration and vector error correction model does not fit well with the data for private investment model giving rise to inconsistent estimates, which is not in accordance with the theory. For instance, income adversely affecting private investment, is surprising and is not in accordance with major economic theories.}

\footnote{There is a conceptual difference between public debt and government debt. Public debt refers to government debt from domestic private sector and abroad or non-residents (Bhattacharya, 1990; Rajaraman, 1999). But in general, government debt refers to interest bearing government borrowings irrespective of the sources from which it is raised be it private, quasi-private or public sector.}
sector undertakings and public financial institutions. This is for the reason that the central government is a major borrower among all the government entities in the country and also that the measurement of borrowings and lendings of the central public sector undertakings is very difficult due to unavailability of data from the published sources. Debt of the government includes both the interest bearing as well as non-interest bearing/concessional debt obligations. It is the sum of all borrowings and liabilities of a government (owed to other entities) on which the government has to incur interest liabilities (unless it happens to be concessional debt, where the government need not pay interest liability) along with repayment of the principal amount on maturity.

Under a federal fiscal set up, national public debt of the country broadly refers to the debt of the central government, sub-central governments as well as local governments along with debt of the public enterprises. In a country like India with a federal fiscal set up where most of the state governments owe a larger sum of funds to the central government and the local governments owe to the state governments, these inter public sector financial transactions should be netted out from the aggregate national public debt in order to arrive at the actual aggregate national public debt of the country; and in the same way, the borrowings of the state and UTs governments should be netted out from the total central government debt in order to arrive at only the debt burden of the central government.

The government of a country borrows from within the country as well as outside. The government debt of a country comprises aggregate internal and external liabilities. Since there is a drastic compositional shift in the central government borrowings from external sources to domestic sources, the study particularly addresses the issue arising due to domestic debt of the central government in India.

Further, the total internal liabilities or domestic debt of the central government in India broadly comprise(s) (i) internal debt and (ii) other liabilities. The (i) internal debt includes loans raised from the open market, special securities issued to RBI, compensation and other bonds and also includes borrowing through issue of Treasury Bills (TBs) issued to the RBI, State Governments, Commercial...
Banks and other institutions, and (ii) other liabilities comprise small savings and public provident funds, and reserve funds etc. According to the Union Budget Document of India (1998) internal debt also includes non-negotiable, non-interest bearing rupee securities issued to the international financial institutions like IMF, IBRD, IDA along with other components defined above. Since the government owes the sum to the domestic market and from other internal sources, especially, public accounts in the form of small savings and provident funds, it is obliged to pay back these liabilities along with the interest payments. External government liabilities include borrowings from multilateral financial institutions and different countries of the world, which are bilateral in nature. Thus, Government of India’s debt is the sum of all outstanding domestic liabilities including external liabilities.

As mentioned earlier, the coverage of the study is confined to the central government domestic debt. The problems arising out of state government debt and external public debt and their implications fall outside the scope of the study. Any mention of state government debt and external public debt would be incidental in the course of the study. One important point which needs to be mentioned here is that since a sizeable portion of state and UTs governments’ domestic debt is owed to the central government, domestic debt of state and UTs governments and debt of public sector enterprises owed to the centre should be completely eliminated from the total domestic debt of the centre to arrive at the net domestic debt of the central government (domestic borrowings in actual possession of the centre). However, due to the fact that most of the states and UTs are under financial strain, they continue to roll over their debt and ultimately it shall become centre’s responsibility to settle, and hence the study emphasises on the gross domestic debt of the centre. On the other hand, there are public enterprises, that borrow from the central government and return profits to the government; and there are public enterprises which borrow from the government and incur losses and are unable to pay off their debt. Therefore, in an uncertain world where there is no guarantee that the central government would get back the principal with interest payments thereon, computation of net domestic debt of the central government loses its significance. On account of these practical problems associated with net domestic debt of the centre, the study takes into account the gross domestic debt of the central government in India. As per the definition of the budget document of India,
the issue of non-interest and non-negotiable bearing rupee securities issued to the international financial institutions viz., International Monetary Fund (IMF), International Bank for Reconstruction and Development (IBRD), International Development Agency (IDA) etc. are included in the estimation of domestic debt of the centre. Although debt is external in nature, is being denominated in domestic currencies. Contingent liabilities arising due to central government guarantees to the state governments, private and public sector undertakings are separately shown to highlight the financial risks of the central government. However, an important consideration in measuring the interest payment burden of the central government is that since the state governments do repay the interest liabilities on their past borrowings, they have been netted out from the total interest liabilities of the central government to arrive at the net interest liability, which makes measuring and realising the actual interest burden of the central government more meaningful.

The study covers the period from 1960-61 to 1999-2000. The starting period 1960 has been chosen bearing in mind the fact that in the first two decades, the fiscal health of the country was sound as reflected in the surpluses generated in the revenue account until the end of 1970s; and borrowing was mainly incurred for capital expenditure. In 1980's the fiscal health of the country started deteriorating and the country found itself in a macroeconomic crisis in early 1990s. Subsequently, several policy measures were undertaken to overcome the fiscal problems of the country. The study period extends up to 2000, for the reason that the official reports still give estimated figures on GDP as well as fiscal policy variables. As a result, it is difficult to consider the latest data for a comparative perspective of debt position of the central government in relation to GDP of the country. By taking account all these three phases, the study tries to assess the policy implications with regard to the domestic public debt of the centre.

1.6 Chapter Organisation of the Study

The entire study comprises eight chapters. Chapter 1 presents a brief introduction about the study in terms of emerging issues in the context of rising domestic debt of the central government. In this respect, the study tries to find out research gaps in the existing literature in the Indian context, and then tries to fill up the gaps by
setting up clearly defined objectives. Chapter 2 outlines the theoretical and empirical review of literature, concerning sustainability of domestic public debt and the impact/effect of domestic public debt on the key macroeconomic variables (viz. private consumption and investment). Chapter 3 analyses the trend pattern and compositional character of domestic debt of the central government. This chapter also discusses the genesis of fiscal imbalances along with addressing the fiscal risks arising out of contingent liabilities of the central government.

Chapter 4 critically analyses the central government domestic debt policy and interest rate policy in connection with domestic debt of the central government, with a view to suggesting certain concrete policy measures for maintaining fiscal stability in the economy. Chapter 5 assesses the issue of domestic debt sustainability of the central government. This chapter compares two approaches to sustainability - the accounting approach vs. the present value budget constraint approach.

Chapter 6 empirically evaluates the macroeconomic impact of domestic public debt on private consumption. This chapter specifies a general private consumption model and later augments the structural variables in the model to take care of the influence of specific structural characteristics of the economy on private consumption. Then, it applies a suitable time series technique for examining the impact of domestic public debt on private consumption in India.

Chapter 7 evaluates the macroeconomic impact of domestic public debt on private investment. Similar to private consumption model, this chapter brings out a model of private investment and applies similar econometric technique for examining the impact of government borrowing on private investment in India. Finally, Chapter 8 provides summary results and policy suggestions.