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RECONSIDER SOVEREIGN EXTERNAL BORROWING

Relevant for: Indian Economy | Topic: Issues relating to Growth & Development - Public Finance, Taxation & Black Money incl. Government Budgeting

According to a *Bloomberg* report, the Government of India is planning to raise $10 billion in its first overseas bond sale by October. The decision to resort to this route for raising capital was announced in the budget earlier this month. While the initial offerings might be for euro or yen-denominated bonds, dollar offerings have not been ruled out. There are both pros and cons of using this route to raise capital.

The biggest benefit of such bonds is that interest rates in international markets are much lower than domestic markets. Such borrowing also does not lead to the government crowding out the private sector from a finite, and decelerating, pool of domestic savings. The biggest risk is that such borrowings have an in-built unpredictability because of foreign exchange movements. Because the debt has to be repaid in foreign currency out of domestic resources, a depreciation in the Indian rupee vis-à-vis the currency in which the debt is denominated can lead to a spike in domestic debt burden. Given the sovereign guarantee, it will have to be repaid at all costs, unlike a corporate loan, which need not be paid in case of bankruptcy. An unforeseen disruption in global markets in the future can derail the calculations which form the basis of taking any such debt in the present.

It is because of these downside risks that a wide gamut of economists and policy makers, including three former governors of the Reserve Bank of India, have advised against this route to raise investible resources. The cautionary voices also include economists who are a part of the Prime Minister’s Economic Advisory Council. These are people whose service and allegiance to the best interests of the Indian economy are beyond doubt. Even the Swadeshi Jagran Manch has spoken against this plan. Therefore, it is necessary that the government engages with these voices and tweaks its policy decision to allay their concerns. Any such decision will not be seen as a sign of political weakness, but a rational decision to heed to wise counsel within the country. It is in our best interests to continue avoiding riskier forms of engagement with the global economy.

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