Off Budget Borrowing, Meaning, Mechanism, Issues, Way forward

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Off-budget borrowing is a method of financing government expenditure through public institutions or PSUs instead of direct borrowing by the Centre. The loans are used for government schemes but are not shown in the official fiscal deficit, even though the government ultimately bears the repayment burden. It is mainly used to manage fiscal deficit targets and fund subsidies, but it raises concerns about hidden debt, lack of transparency, and weak fiscal discipline.

Off Budget Borrowing Meaning

Off-budget borrowings are **loans that are taken not by the Centre directly, but by another public institution which borrows on the directions of the central government**.

- Such borrowings are used to fulfil the government's expenditure needs.
- But since the **liability of the loan is not formally on the Centre**, the **loan is not included in the national fiscal deficit.**
- This helps keep the country's fiscal deficit within acceptable limits.

Mechanism of Off-Budget Borrowing

The government can ask an implementing agency to raise the required funds from the market through loans or by issuing bonds.

- For example, in the Budget presentation for 2020-21, the government paid only half the amount budgeted for the food subsidy bill to the **Food Corporation of India**. The shortfall was met through a loan from the National Small Savings Fund.
- Public sector oil marketing companies were asked to pay for subsidised gas cylinders for **Pradhan Mantri Ujjwala Yojana** beneficiaries in the past.

Public sector banks are also used to fund off-budget expenses.

- For example, loans from PSU banks were used to make up for the shortfall in the release of fertiliser subsidies.

Reasons for Off-Budget Borrowing

The primary reasons for resorting to off-budget borrowing include:

- **Meeting fiscal deficit targets**: Governments use off-budget borrowing to keep the reported fiscal deficit within **FRBM**-mandated limits while still financing required expenditure.
- **Managing subsidy burden**: Large and recurring subsidies such as food, fertiliser, and LPG are often financed through entities like FCI and PSUs to avoid immediate strain on the central Budget.
- **Bridging budgetary under-provisioning**: When actual expenditure exceeds allocated Budget estimates, off-budget channels are used to meet the shortfall without revising fiscal numbers.
- **Financing capital and infrastructure projects**: Special Purpose Vehicles (SPVs) and extra-budgetary resources are used for long-gestation infrastructure projects like railways, roads, and irrigation.
- **Avoiding fiscal pressure visibility**: It helps present lower official borrowing and deficit figures, maintaining macroeconomic stability perception and investor confidence.
- **Handling economic shocks and emergencies**: During crises such as economic downturns or the COVID-19 period, it enables faster mobilisation of resources without immediate budget restructuring.
- **Maintaining policy flexibility**: It allows governments to continue welfare and development spending despite constraints in formal budgetary allocations.

Issues with Off-Budget Borrowing

Off-budget borrowing raises serious concerns regarding fiscal transparency, accountability, and long-term debt sustainability. The **Comptroller and Auditor General (CAG)** in its 2019 report highlighted that such financing mechanisms shift major sources of funds outside the direct control of Parliament, despite having clear fiscal implications.

- **Undermines parliamentary oversight**: A significant portion of public expenditure is financed outside the Budget, reducing effective scrutiny by Parliament over government finances.

- **Crowding Out**: When PSUs borrow heavily from the market to fund government projects, it leaves less credit available for private companies, potentially raising interest rates for everyone.
- **Distorts fiscal indicators**: Since these borrowings are excluded from fiscal deficit calculations, they present an incomplete and potentially misleading picture of the government's fiscal position.
- **Weakens fiscal transparency**: Off-budget financing reduces clarity in public accounts, making it difficult to assess the true level of government liabilities and expenditure.
- **Creates hidden debt burden**: Although not immediately visible in official statistics, these borrowings eventually become government liabilities, increasing long-term public debt.
- **Undermines FRBM framework**: It dilutes the effectiveness of fiscal discipline mechanisms under the FRBM Act by bypassing mandated borrowing limits.
- **Reduces accountability in public finance**: Since expenditure is routed through PSUs or agencies, responsibility becomes diffused and less directly accountable to legislative oversight.
- **Risk of fiscal mismanagement**: Over time, accumulation of off-budget liabilities can create fiscal stress and reduce policy flexibility for future governments.

Way Forward

Ensuring fiscal transparency and long-term debt sustainability requires a structured reduction and better regulation of off-budget borrowing practices in India.

- **Complete transparency in fiscal reporting**: All off-budget liabilities should be clearly disclosed in Union and State Budget documents to reflect the true fiscal position.
- **Gradual inclusion in fiscal deficit**: Extra-budgetary resources should be progressively incorporated into fiscal deficit calculations to avoid hidden liabilities.
- **Strengthening FRBM framework**: The FRBM Act should be strictly enforced with clear limits on indirect borrowings and improved compliance mechanisms.
- **Rationalisation of subsidies**: Structural reforms in food, fertiliser, and energy subsidies can reduce dependence on off-budget financing.
- **Improved budgetary planning**: Better estimation and allocation of expenditures can minimise the need for last-minute off-budget funding.
- **Stronger parliamentary oversight**: Enhanced scrutiny by Parliament and its financial committees over PSU and SPV borrowings.
- **CAG monitoring and audit strengthening**: Regular audit and disclosure of off-budget liabilities to ensure accountability.
- **Reducing reliance on PSUs for borrowing**: Limiting the practice of using public sector entities as financing intermediaries for government expenditure.
- **Fiscal consolidation focus**: Medium-term strategy should aim at reducing overall debt and improving quality of public expenditure.
