

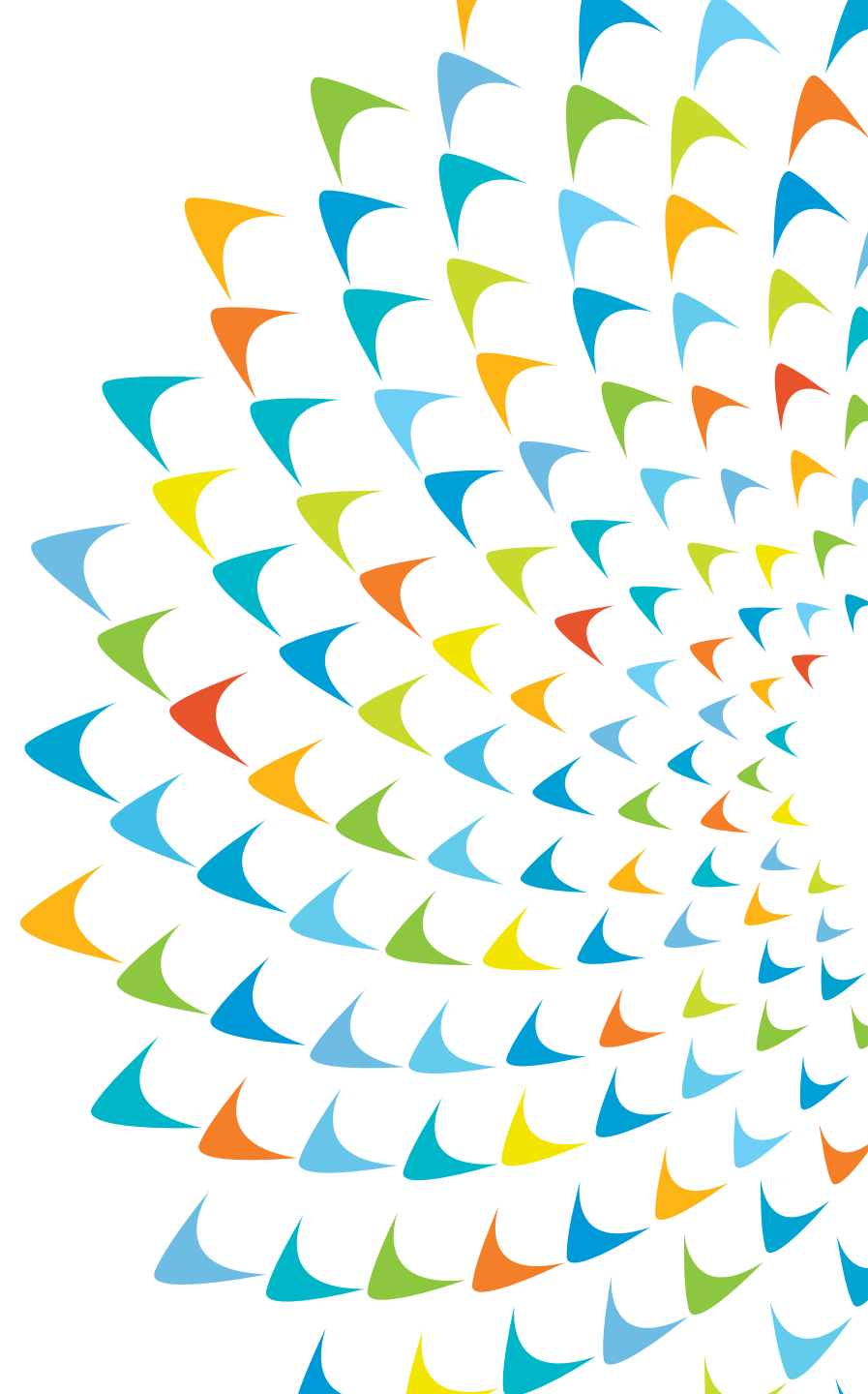


Fiscal and Debt Sustainability Issues and Challenges

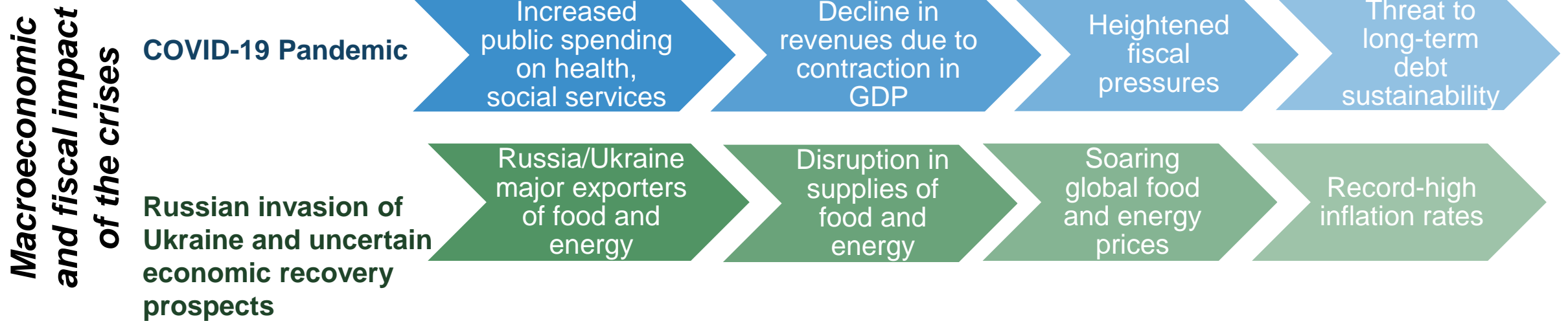
ADB Developing Member Countries-
Post-COVID-19 Period

Asian Development Bank (ADB)

21 September 2022



Objective of the presentation

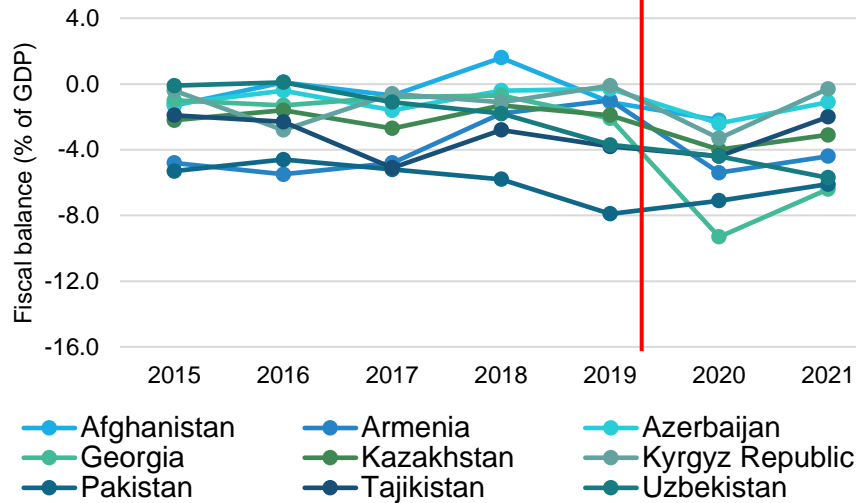


The objective is to analyse the fiscal and debt sustainability of ADB DMCs in the post-covid period and provide some recommendations.

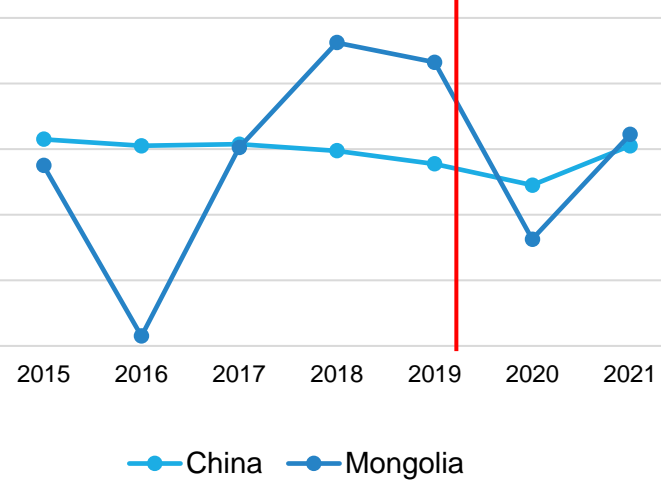
- **Country groups:** 30 ADB DMCs
- **Sub-regions covered:** Central and West Asia, South Asia, East Asia, South-east Asia, the Pacific
- **Time period:** 2015 – 2019 (pre-covid) and 2020-2022 (post-Covid)
- **Indicators:** GDP growth, inflation, unemployment, debt, fiscal balance, revenue and expenditure

Analysis of Fiscal Deficit

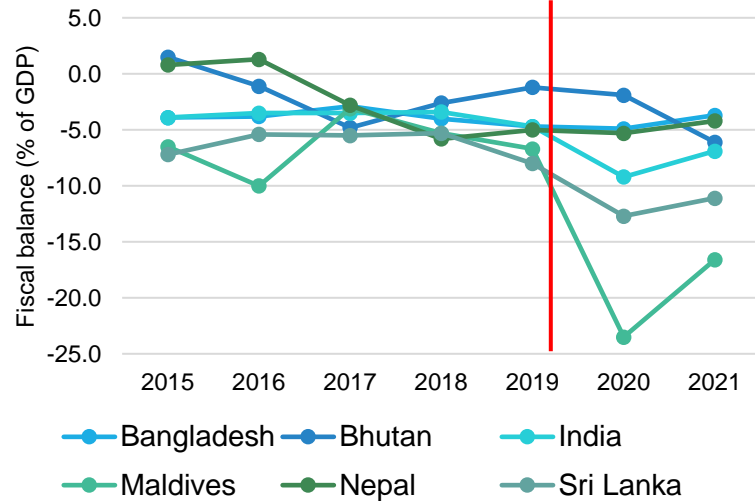
Central and West Asia



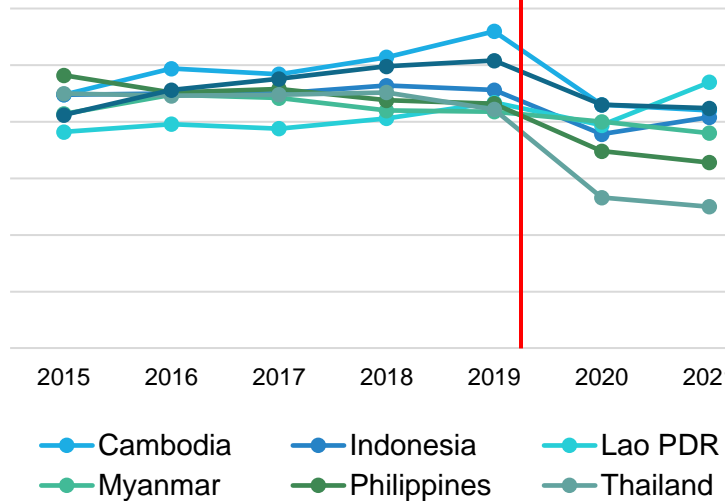
East Asia



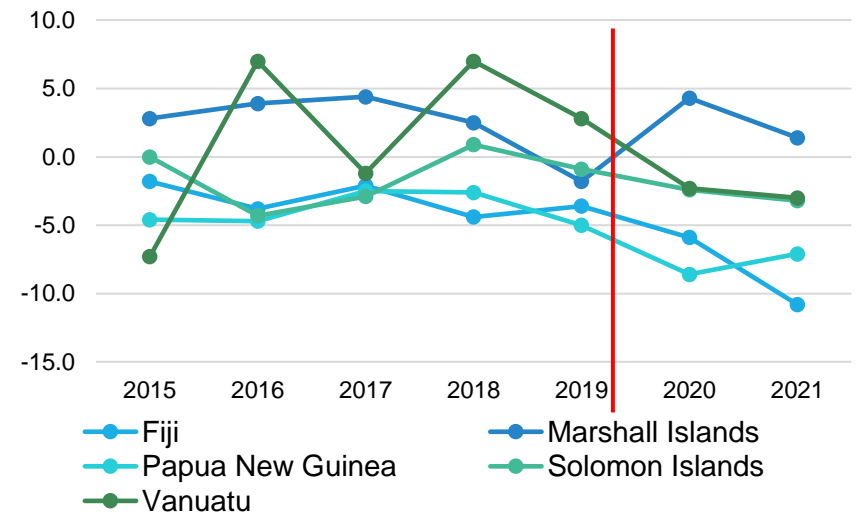
South Asia



Southeast Asia



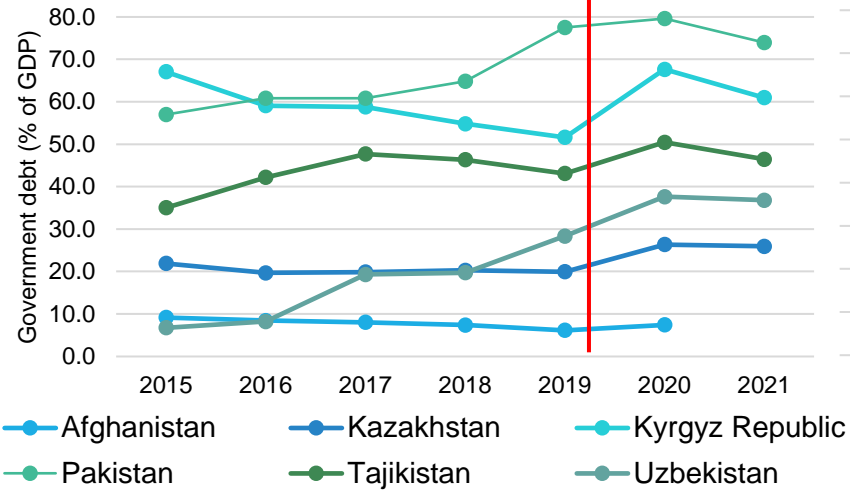
The Pacific



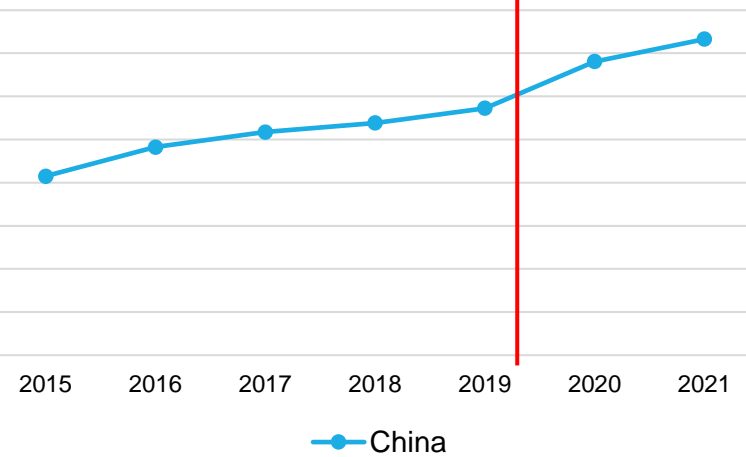
- Fiscal balances of all ADB DMCs deteriorated in 2020 (versus 2019) except for Pakistan and Marshall islands. Most DMCs recorded fiscal deficits in the post-covid period apart from Marshall Islands (fiscal surplus of 1.40% in 2021).
- While several countries such as Azerbaijan, India improved their fiscal balance in 2021 relative to 2020, countries such as Uzbekistan, Thailand, Philippines, Myanmar, Vietnam, Bhutan, Fiji, etc. saw a further deterioration.

Analysis of General Government Gross Debt

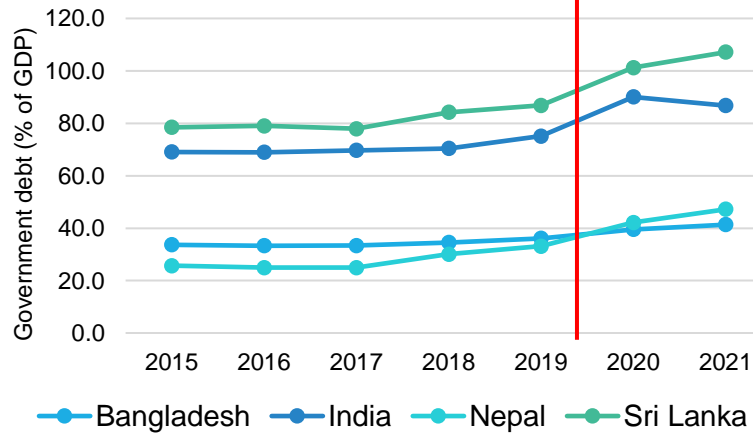
Central and West Asia



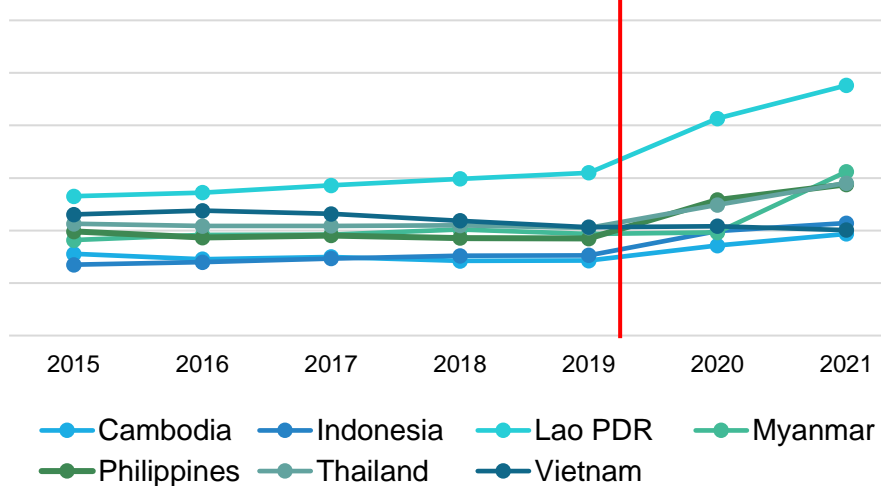
East Asia



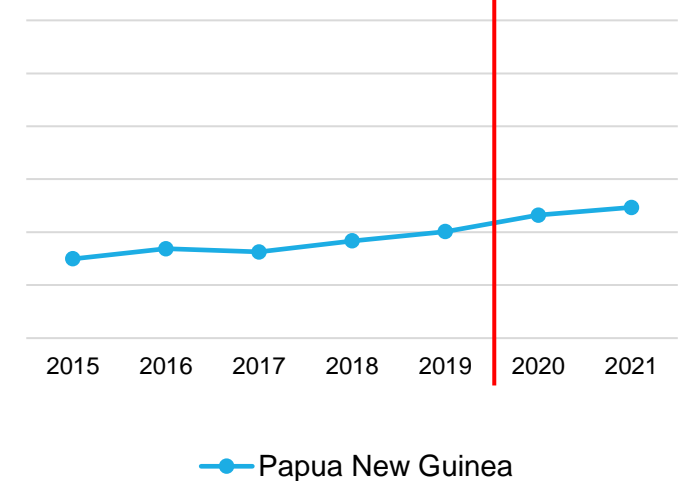
South Asia



Southeast Asia



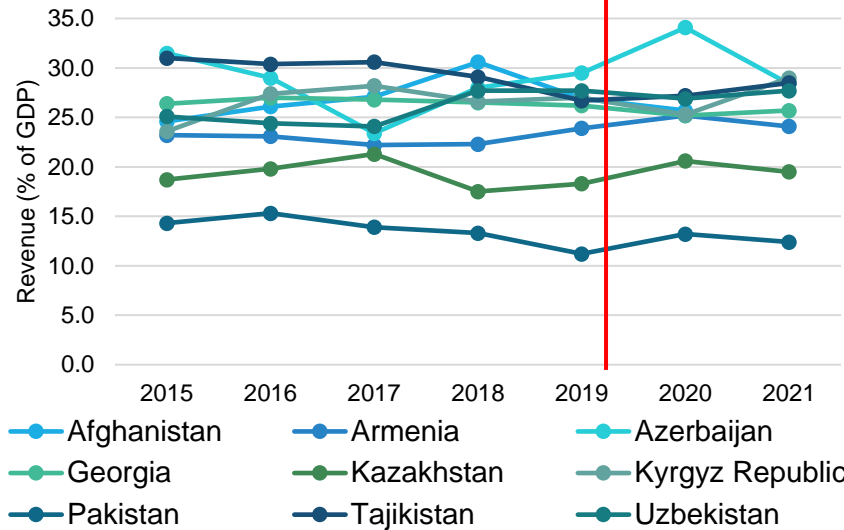
The Pacific



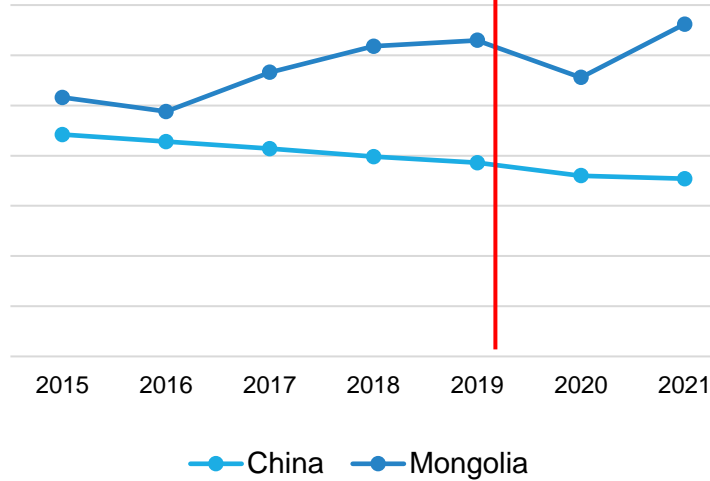
- DMCs such as Sri Lanka and India had high debt-GDP ratios in the pre-covid period (above 70%), relative to 37.4% for other DMCs on an average.
- In the post covid period, most countries saw a spike in 2020 but several managed to curtail debt levels in 2021. Some countries like Sri Lanka, PRC, Lao PDR, Philippines, Thailand saw a worsening of debt levels in 2021.

Analysis of Total Revenue

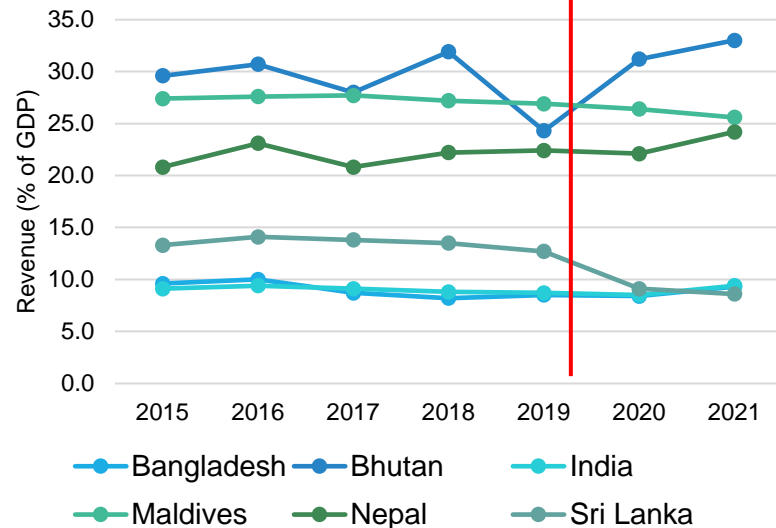
Central and West Asia



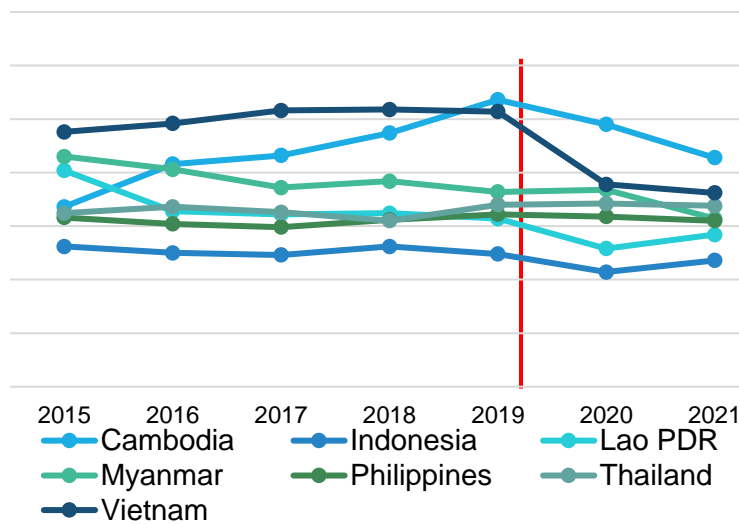
East Asia



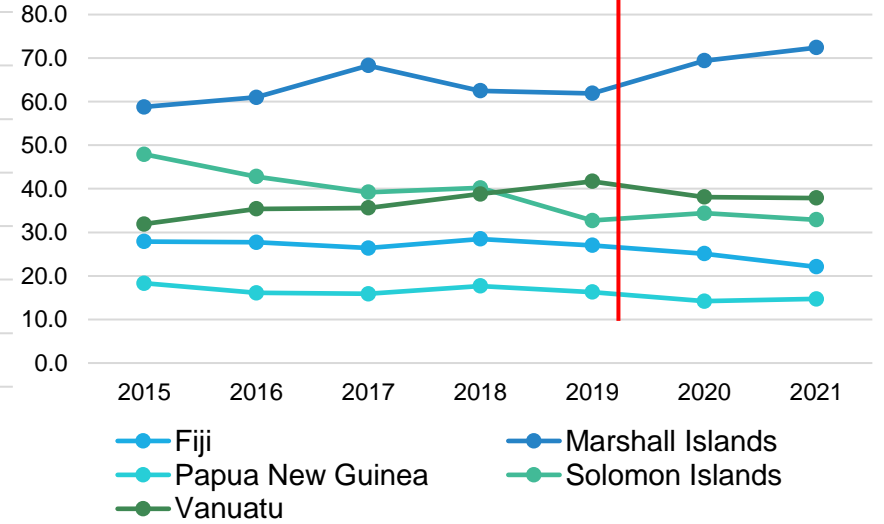
South Asia



Southeast Asia



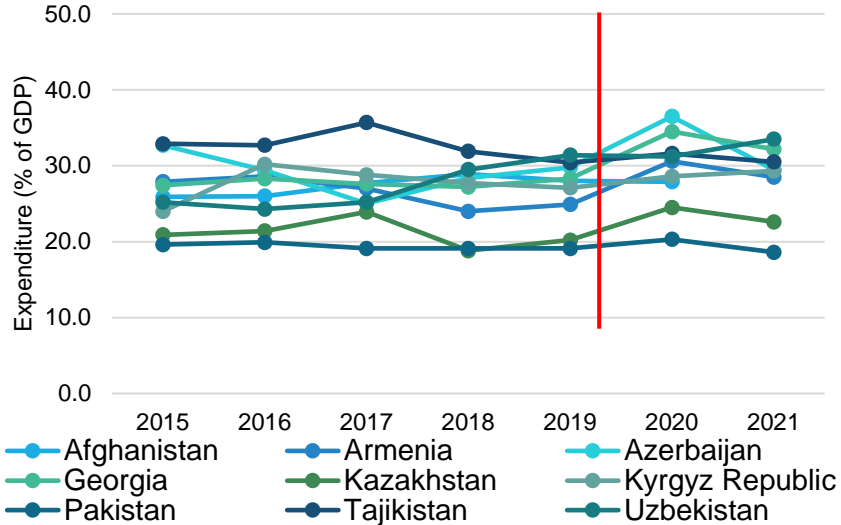
The Pacific



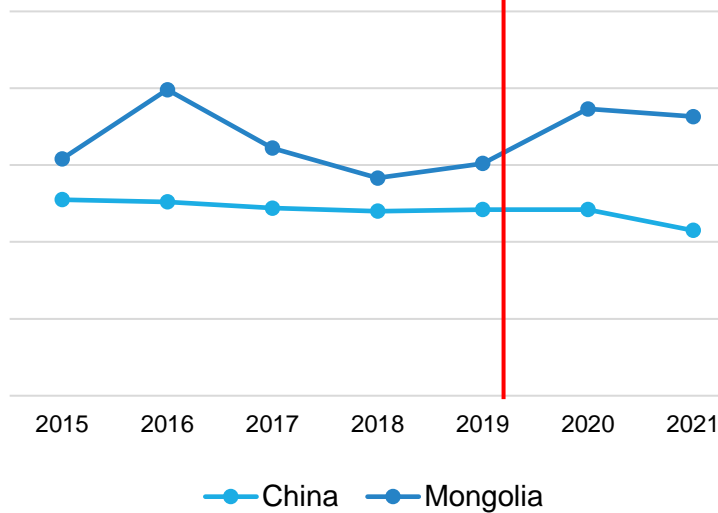
- Higher revenue as a share of GDP is observed for DMCs in the Pacific region (36.8% on average), compared to DMCs in the other regions (21.1%), primarily on account of Marshall Islands (62.5%)
- 19 DMCs witnessed a decline in revenue in 2020. Revenues continued to decline in 2021 for DMCs such as Armenia, Cambodia and Sri Lanka and improved for DMCs such as Bangladesh, India, and Nepal.

Analysis of Expenditure

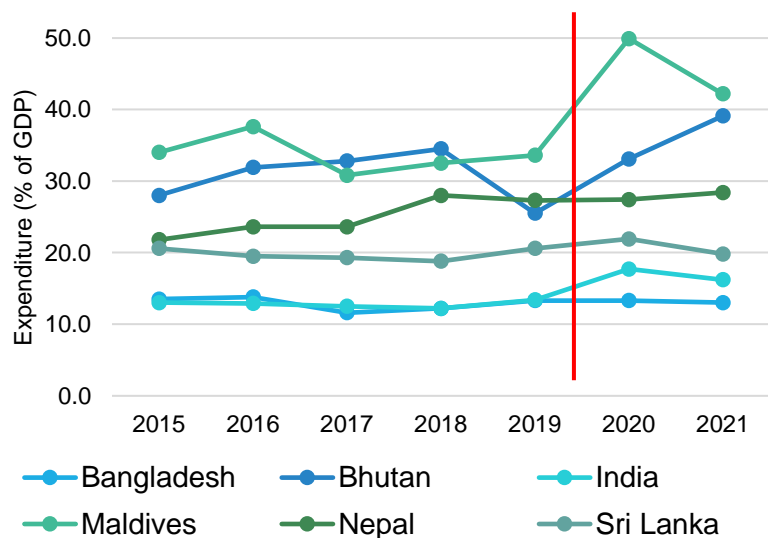
Central and West Asia



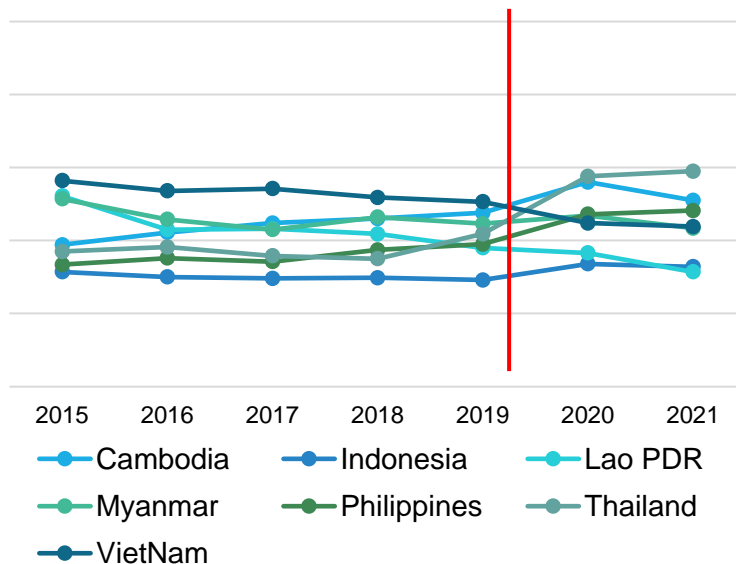
East Asia



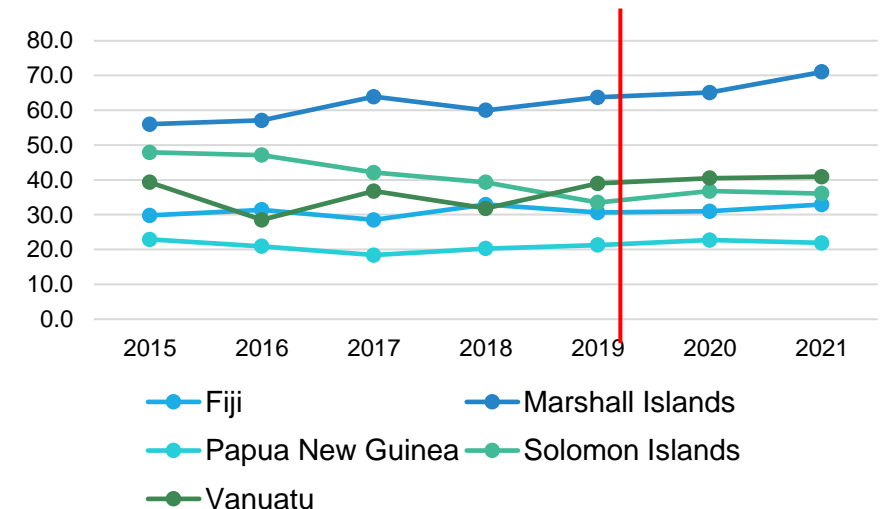
South Asia



Southeast Asia



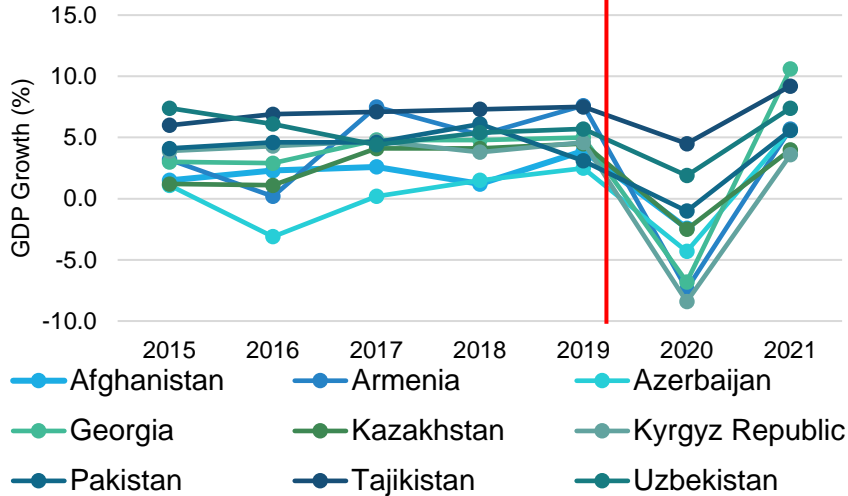
The Pacific



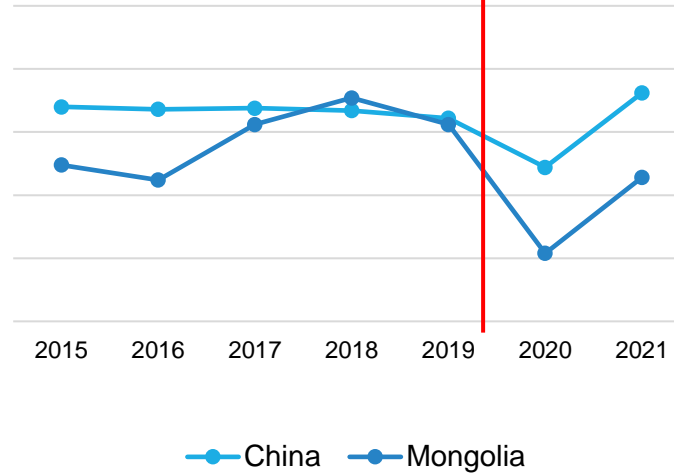
- Relatively stable expenditure levels were observed for most DMCs in the pre-covid period. Expenditure as a share of GDP increased in 2020 for 23 DMCs and declined for a few DMCs such as PRC and Vietnam.
- In 2021, expenditures as a share of GDP declined relative to 2020 for 20 DMCs apart from a few DMCs such as Bhutan, Philippines and Fiji for which expenditure as a share of GDP continued to increase.

Analysis of GDP Growth

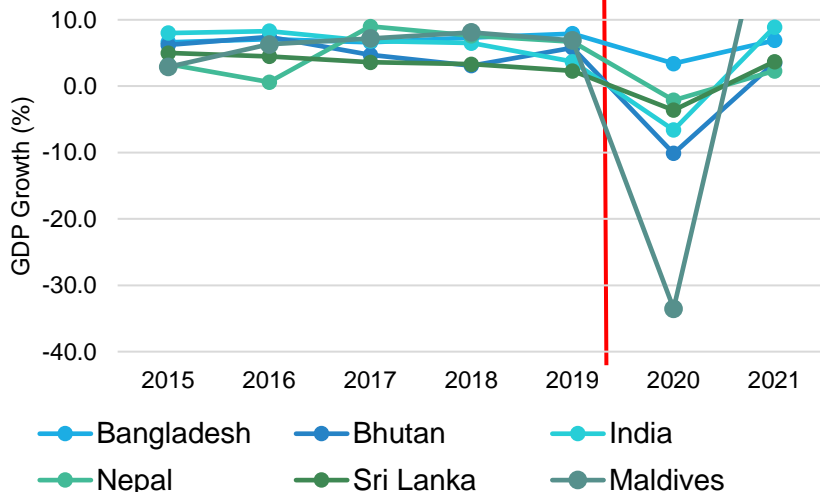
Central and West Asia



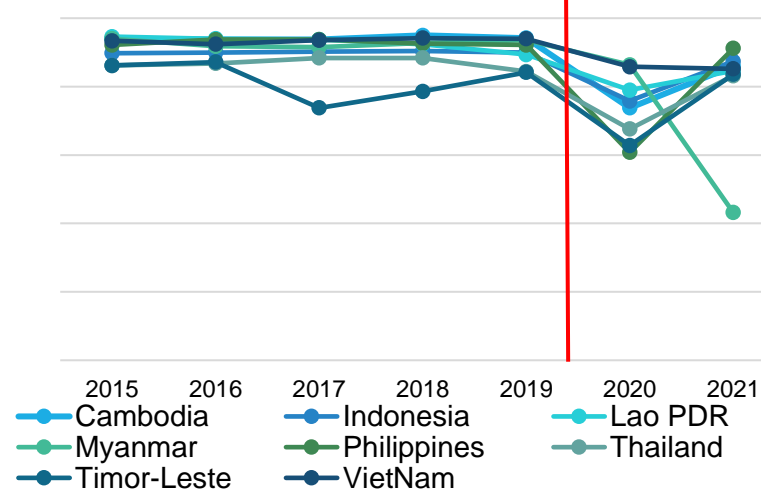
East Asia



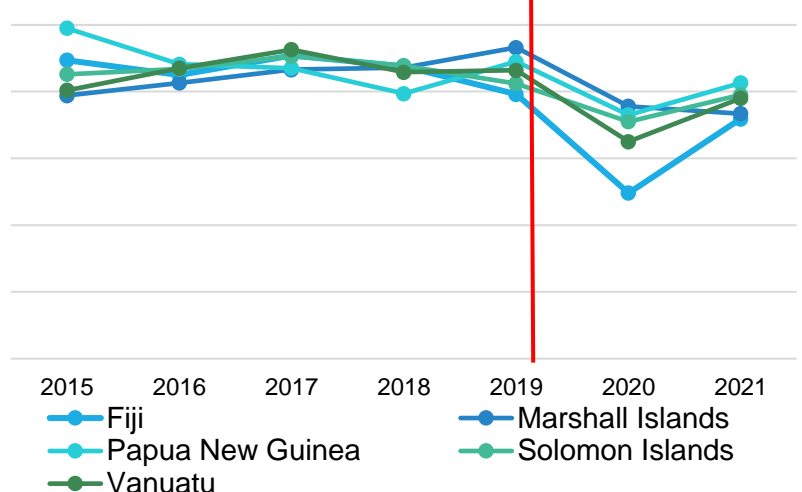
South Asia



Southeast Asia



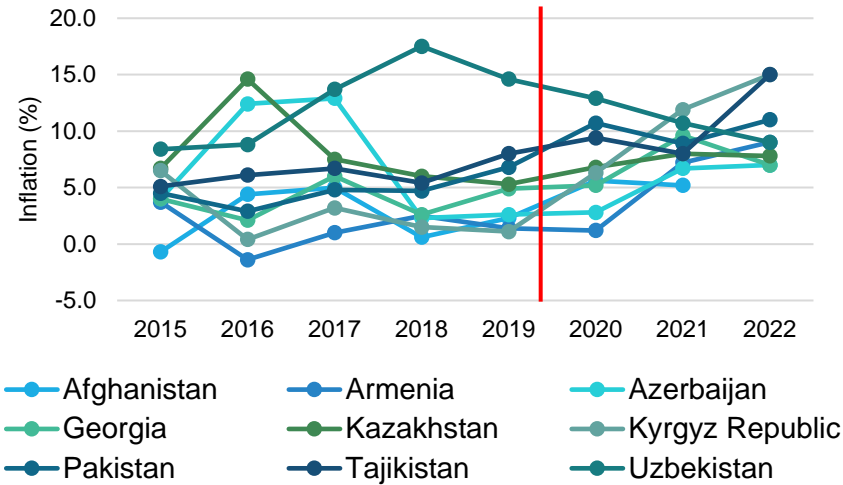
The Pacific



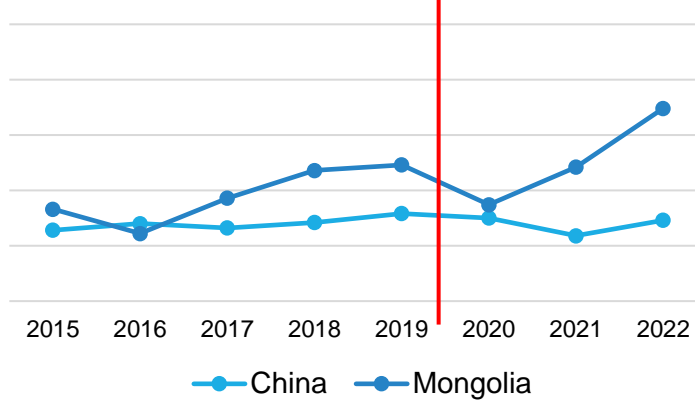
- In the pre-covid period, a 4.7% average GDP growth was witnessed in the DMCs and Bangladesh and Cambodia recorded high average GDP growth (more than 7%).
- While the GDP growth rate declined for all DMCs in 2020, most were able to recover the GDP growth in 2021 from the 2020 levels, except countries such as Myanmar, Vietnam and Marshall Islands.

Analysis of Inflation

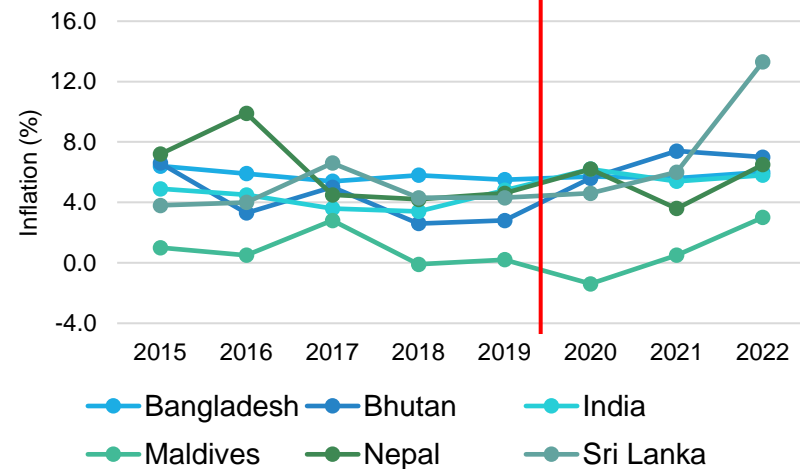
Central and West Asia



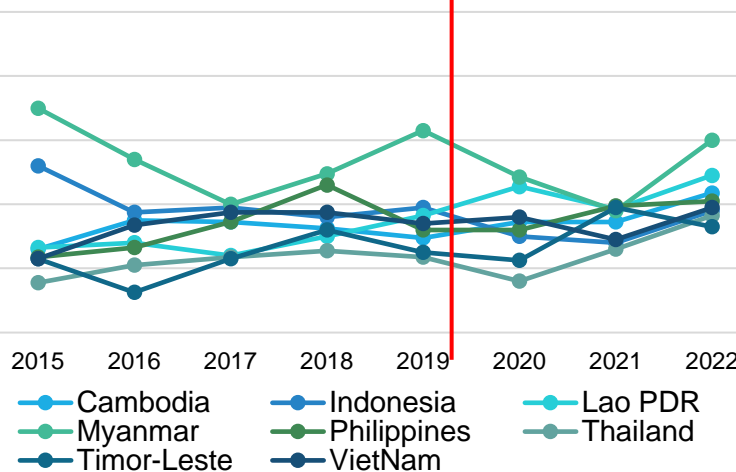
East Asia



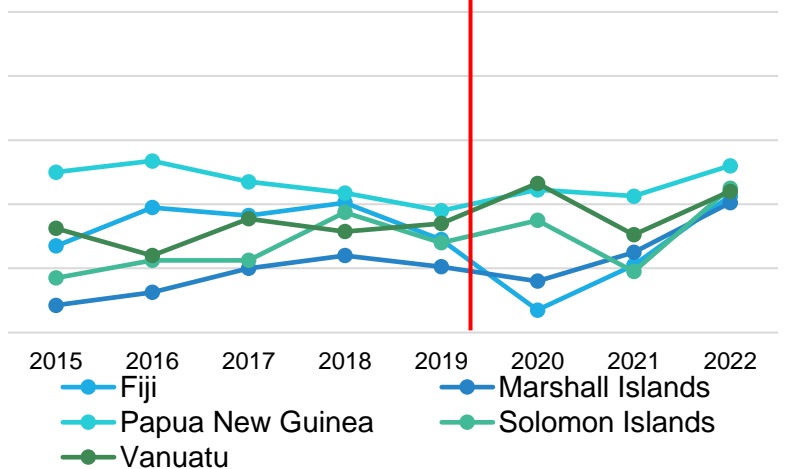
South Asia



Southeast Asia



The Pacific



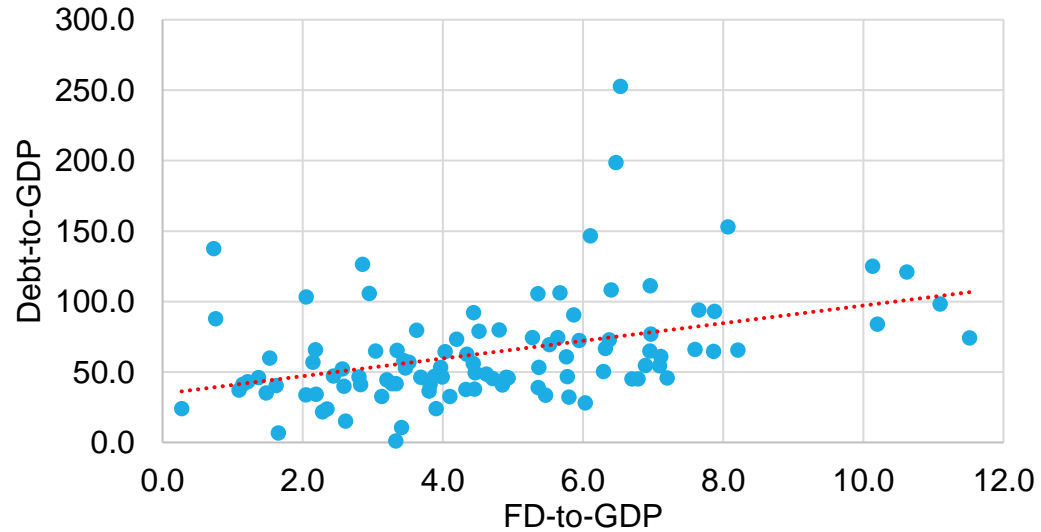
While varying inflation trends were observed in the DMCs in the pre-covid period, relatively higher inflation (5.4% on an average) was observed in the Central and West Asia region compared to the other regions (3.1%).

Several DMCs managed to reduce the inflation rate in 2021 from the 2020 levels except for countries such as Azerbaijan, Bhutan and Sri Lanka. Inflation rate is expected to rise in 2022 from 2021 levels for most DMCs apart from countries such as Georgia and Uzbekistan.

Debt- Deficit Dynamics

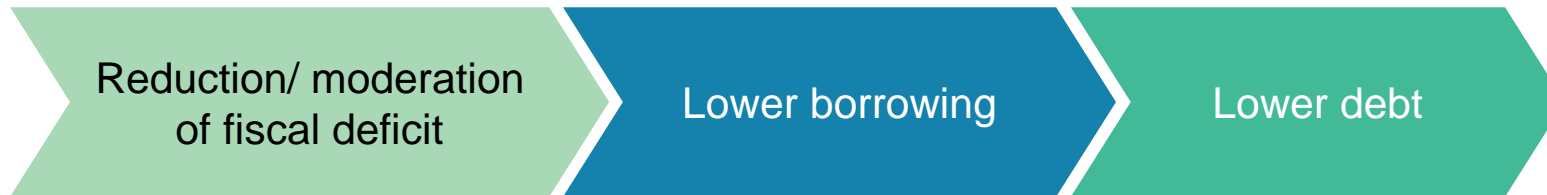
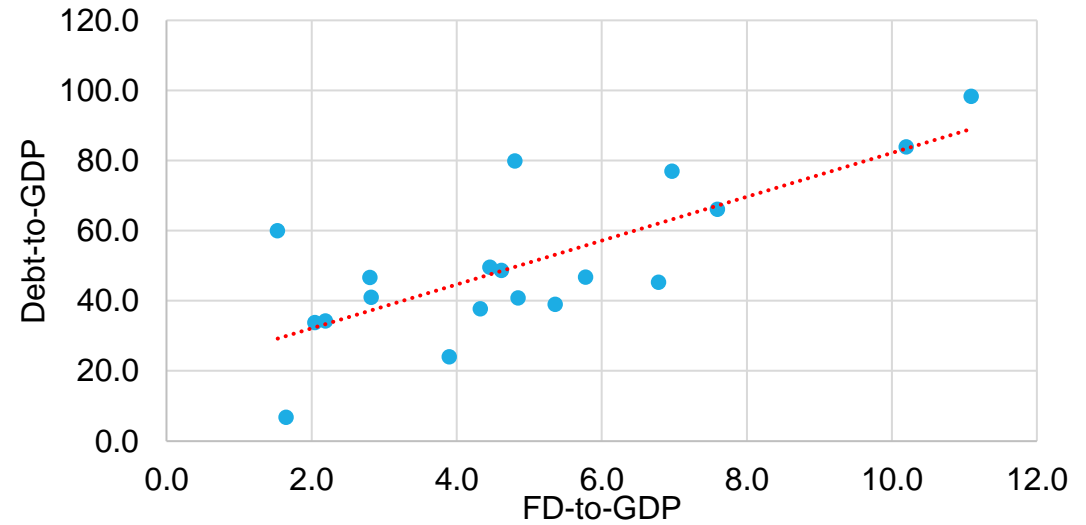
All countries

$$y = 6.2678x + 34.484$$
$$R^2 = 0.1548$$
$$t\text{-stat} = 4.2790$$



ADB DMCs

$$y = 6.2517x + 19.683$$
$$R^2 = 0.5647$$
$$t\text{-stat} = 4.6963$$



Key Recommendations



Recommendations for Revenue

Mobilisation of domestic tax revenues

- ❖ Analysis of tax effort and capacity: *Countries in developing Asia can increase tax-to-GDP ratio by ~3%-4% on an average.*
- ❖ Tax expenditures in the form of tax holidays, subsidies etc. can constitute significant leakage from the system due to lack of transparency. There is a need to improve transparency and ensure a strong legal and governance framework.
- ❖ Tax stimulus packages need to be carefully designed to ensure that the benefits outweigh the costs
- ❖ Need to incorporate sustainability in taxation through measures such as **green tax and health tax. Carbon pricing** via carbon tax and Emissions Trading Systems (ETS) is one such measure with great potential.
- ❖ Revenues from VAT / GST can be strengthened further by reducing exemptions and subsidies and effective taxation of the rapidly expanding digital economy.

ETS in Republic of Korea

Republic of Korea launched the first ETS in Asia in 2015. In RoK, \$257.7 million total revenues was generated by the K-ETS in 2021.

Carbon Tax in Singapore

Singapore introduced a carbon tax through the Carbon Pricing Act. The carbon tax revenue was \$150 million and \$143.5 million in 2020 and 2021, respectively, in Singapore.

Role of MDBs

- ❖ Supporting TAs for detailed assessment of tax expenditures and customizing and aligning local tax policies and administration systems with international standards and best practices
- ❖ Assisting in reforms (such as development of comprehensive VAT strategy for e-commerce) that address the challenges of taxing the digital economy, including imports

Recommendations for Revenue

Mobilisation of non-tax revenues through asset monetization

- ❖ Asset monetization can provide an alternative to disinvestments in PSE and restructuring of enterprises and it does not necessarily entail change in the ownership structure of various asset classes. So, **government can retain the ownership** and take help of private investment to reduce the strain on public finances.

Asset management in Singapore

Temasek was responsible for managing all commercial public assets in Singapore. It manages assets that are more than 1.7 times the GDP of Singapore.

NLMC set up by India

India is setting up a National Land Monetization Corporation (NLMC) as a wholly owned GoI company which will be responsible for monetization of surplus land and building assets of public sector enterprises and other government agencies.

NIP undertaken by GoI

The Government of India undertook the National Investment Pipeline (NIP) plan on 31st December 2019 to meet the challenges of infrastructure deficit.

Recommendations to improve asset monetization

- ❖ Identify assets that can be monetized and create a registry of public assets across sectors
- ❖ Create right governance and ensure having a strong legal, regulatory and governance framework in place
- ❖ Create a professional asset manager
- ❖ Co-sharing of assets can create mechanisms of knowledge transfer and spillover effects

Recommendations for Revenue

Base Erosion and Profit Shifting (BEPS)

- ❖ MNEs often exploit gaps and mismatches in tax rules to avoid or pay less taxes referred to as Base Erosion and Profit Shifting (BEPS). This leads to lower collection of tax revenues.
- ❖ BEPS Pillar I and II outlined by the OECD/G20 Inclusive Framework on BEPS is aimed at reducing the incentives of the MNEs to shift profits to low or no tax jurisdictions.

The two-pillar approach to BEPS - Pillar I and II - to address the tax challenges was approved by 137 BEPS Inclusive Framework members on 8 October 2021

- ❖ Pillar I is focused on setting up a new taxing right that allows reallocating profits to market jurisdictions of multinational enterprises (MNEs) with a global turnover of more than 20 billion euros and profitability above 10% (profit before tax). 25% of the residual profit (profit in excess of 10% of revenue) of the relevant MNEs is intended to be allocated to market jurisdictions using the revenue-based allocation approach.
- ❖ Pillar II emphasizes on the payment of a minimum level of taxation by the MNEs in each jurisdiction. It depends on two rules: the global anti-base erosion (GloBE) rules and the subject to tax rule (STTR).
 - The GloBE rules apply to the MNEs meeting the 750 million euros threshold under BEPS Action 13 and provide for a minimum taxation of 15% in each jurisdiction.
 - The STTR rule allows an additional taxation of upto 9% at source by developing countries.

Recommendations for Expenditure

Improving Public expenditure management

- ❖ **Medium Term Frameworks:** Can help governments allocate budgetary resources to programs, activities, and projects that promote the strategic priorities of national/ sub-national governments in the medium-term.
- ❖ **Scheme rationalization:** Ensure efficient utilisation of limited budgetary resources available with national and sub-national governments
- ❖ **Diagnostic Assessments:** Can help identify issues/ inefficiencies in public spending and inform policy-making for improving the efficiency and effectiveness of public spending
 - ❖ PERs analyses the quality & quantity of public expenditure against policy goals
 - ❖ PETS can serve as a vital tool to inform PFM practices by tracking flow of public resources

Role of MDBs

MDBs can assist governments in undertaking assessments, such as **PERs and PETS** to keep the governments informed about the allocation and utilization of their public expenditure.

They can also support in establishment and preparation of medium-term frameworks for better expenditure allocation

MTFF

- It represents first step towards MTEF and establishes fiscal policy objectives.
- It can be useful as it provides medium-term macro-fiscal framework for budget preparation.

MTBF

- It includes bottom-up projection of medium-term expenditure estimates for individual administrative units and reconciles expenditure

MTEF

- MTEF helps add elements of performance-based budgeting to MTBF
- It represents a complete transition from input-oriented budgeting

Scheme Rationalisation in India

Government of India's 15th Finance Commission has asked for discontinuation of schemes that have negligible impact or are no longer necessary and putting in place a minimum budget threshold allocation for Centrally Sponsored Schemes (CSSs). When the budget allocation falls below this threshold, the concerned department will have to specify the rationale for continuing the scheme.

Recommendations for Expenditure

Infrastructure Investment

- ❖ Quality infrastructure investment (QII) can help countries in creating jobs, attracting further investment, driving economic prosperity, while ensuring sound finances.
- ❖ Some of the key recommendations of improving infrastructure governance are as follows:
 - ❖ Development of a good infrastructure governance framework is mainly dependent on having the right enabling environment including the regulations and the ability to select and implement the right projects based on cost-benefit analysis, cost-effectiveness etc.
 - ❖ Identifying the effective procurement method – PPP or traditional – is key to understanding on which will deliver VfM for specific projects.
 - ❖ Infrastructure governance should also connect the project appraisal process with the budget cycle and investment plans should be formulated in MTEFs.

Role of MDBs: MDBs can play an important role by **strengthening, extending knowledge sharing tools**, focusing on upstream and midstream technical assistance (TA) to support the key drivers of quality infrastructure such as economic efficiency, life-cycle costs, and value for money (VfM).

Guiding principles adopted by G-20 at the 2019 Osaka Summit

- 01 Maximizing infrastructure's positive impact
- 02 Improving economic efficiency
- 03 Integrating environmental and social considerations
- 04 Building resilience against natural disasters
- 05 Strengthening infrastructure governance



Thank you

Click to edit Master title style

