3. Rising Debt Burden of Indian States - Economy

1. Why in News

1. Analysis highlighted rising debt burden of major Indian states: Tamil Nadu, West Bengal, Kerala, Assam
2. Debt-to-GDP ratios and interest payments increasing sharply
3. State finances increasingly unsustainable
4. RBI State Finances Report (2025-26) shows most states exceed FRBM recommended debt limit of 20% of GSDP
5. High debt servicing constraining capital expenditure, development spending
6. Post-election governance challenges balancing welfare promises with fiscal reality

2. About Rising State Debt

Definition

1. Continuous increase in government borrowings and outstanding liabilities over time
2. Includes loans from central government, financial institutions, market borrowings through state bonds
3. Accumulated fiscal deficits creating debt stock

3. Rising Debt Burden: State-wise Snapshot

Tamil Nadu

1. Outstanding debt nearly quadrupled: ₹2.8 lakh crore (2016-17) to ₹10.6 lakh crore (2026-27)
2. Debt stock rose from 21.8% to 26.1% of GDP
3. Interest payments increased from 15.3% to 22.8% of total revenues over ten years
4. Significant fiscal stress evident

West Bengal

1. Persistent high debt-to-GDP ratio: around 30-38% over last decade
2. Large revenue portion (~20%) spent on interest payments
3. Limiting funds for development and welfare schemes
4. Fiscal flexibility severely constrained

Kerala

1. Debt-to-GDP ratio increased further reflecting growing fiscal stress
2. Around 20% of state revenue for interest servicing
3. Reduced fiscal space for public investment and social spending
4. Despite development model, facing debt sustainability concerns

Assam

1. Debt-to-GDP ratio increased from 17.1% to 25.2% showing rapid liability accumulation
2. Interest burden relatively low (below 10%) due to special category state benefits and higher central grants
3. Better positioned despite rising debt

4. Impact on Governance and Economy

Reduced Infrastructure Spending

1. High debt servicing constrained capital expenditure growth (RBI State Finances Report)
2. Tamil Nadu, Kerala allocates large share to revenue spending rather than capital creation
3. Infrastructure expansion limited

Pressure on Social Sectors

1. Development expenditure (social + economic services) below fiscal needs due to rising committed expenditure
2. Kerala's committed expenditure (salaries, pensions, interest) accounts for over 65% of revenue spending

3. Health and education budgets squeezed

Declining Fiscal Autonomy

1. West Bengal (~39% GSDP) and Kerala (~35-37%) face reduced flexibility
2. Heavy borrowing dependence limits independent development policy design
3. Reliance on central support or market borrowing increases

Rising Debt Servicing Burden

1. Tamil Nadu interest payments reached ₹78,677 crore (2026-27 estimate)
2. Reduces fiscal space for productive spending
3. Increases dependence on fresh borrowings creating vicious cycle

Long-term Fiscal Instability

1. Most states exceed FRBM recommended 20% GSDP debt limit
2. Structural fiscal stress evident
3. Vulnerability to interest rate shocks increases

Development Inefficiency

1. Despite high expenditure, lower capital outlay efficiency
2. Spending diverted to salaries, pensions, subsidies
3. Infrastructure and welfare delivery delays

Inter-generational Burden

1. Tamil Nadu projected over ₹10 lakh crore debt by 2027
2. Repayment pressure shifted to future taxpayers
3. Reduces future fiscal space and development choices

5. Why Fiscal Stress Rising?

1. Rising loan dependency reflecting weak internal revenue mobilization
2. Persistent fiscal deficits with spending exceeding revenues
3. Increasing interest burden reducing productive expenditure funds
4. Reduced fiscal space for development (infrastructure, health, education)
5. Revenue-expenditure mismatch with widening gap
6. Rising borrowing costs due to hardening interest rates
7. Structural revenue weakness with heavy central transfer dependence, limited tax base expansion
8. Long-term sustainability risk threatening debt trap without corrective measures

Post-Election Governance Relevance

1. Electoral promises vs fiscal reality: Balancing welfare promises (freebies, subsidies, loan waivers) with revenue constraints
2. Immediate budget pressure: Inherited high debt stocks and interest burdens limiting new schemes
3. Policy shift toward fiscal consolidation: Revising subsidies, rationalizing welfare, improving revenue mobilization
4. Freebies vs development spending debate intensifies
5. Centre-State fiscal relations focus on loan restructuring, borrowing limits
6. Pressure for fiscal reforms: FRBM compliance, asset monetization, subsidy rationalization
7. Investor confidence impact through credit ratings
8. Governance priorities shift from populist politics to fiscal consolidation

Centre's Role

1. Fiscal transfers and revenue support through tax devolution, grants-in-aid (Finance Commission recommendations)
2. Regulation of state borrowings under Article 293 preventing unsustainable debt accumulation
3. Finance Commission suggestions on debt management, fiscal consolidation, performance-based incentives
4. Centrally Sponsored Schemes sharing financial responsibility reducing state fiscal pressure

5. FRBM norms enforcement for prudent fiscal management
6. Special financial assistance during crises: GST compensation, disaster relief, special packages
7. Cooperative federalism through GST Council, NITI Aayog
8. Incentivizing capital expenditure through interest-free loans, reform-linked incentives

6. Way Forward

1. Debt restructuring and conditional relief: Centre restructure/waive interest or write off loans conditional on reforms (electricity tariff rationalization, user charges on water/sanitation)
2. Asset monetization: Leasing, selling, commercializing government land and non-core assets
3. Strategic divestment of profitable PSUs providing one-time capital inflow
4. Strengthening tax administration: Improving GST compliance, widening tax base
5. Expanding non-tax revenues: User charges, fees, fines, service pricing
6. Rationalizing subsidies and welfare schemes through better targeting
7. Outcome-based budgeting linked to measurable outcomes ensuring efficient resource allocation

7. Conclusion

Rising state debt burden threatens fiscal sustainability with Tamil Nadu, West Bengal, Kerala, Assam facing severe stress. Centre plays dual role as financial supporter and fiscal regulator. Strengthening cooperative federalism, balanced fiscal transfers, promoting fiscal discipline, debt restructuring, asset monetization, tax administration strengthening, and subsidy rationalization essential for sustainable state finances preventing inter-generational burden.

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