

CHINA: EXPLAINING “AUGMENTED” GOVERNMENT DEBT AND DEFICIT

Rationale. Infrastructure investment has become local governments' main strategy to foster growth and a preferred countercyclical tool, especially during the global crisis. However, local infrastructure spending has mainly been financed off-budget, either through land sales or Local Government Financing Vehicle (LGFV) borrowings. This raises the questions of (1) the actual level of fiscal vulnerabilities (in particular the government debt stock), and (2) the actual size of fiscal stimulus that has contributed to supporting growth in recent years.

Approach. Therefore, IMF staff have developed a new ‘augmented’ concept in an attempt to capture these off-budget fiscal activities, which expands the perimeter of the government to include off-budget and LGFV activity. LGFVs are different from other state-owned enterprises (SOEs) as LGFVs are largely set up, owned, and operated by the local governments; they engage in economic activities that are fiscal in nature; and the government directly or indirectly shares the debt servicing responsibilities, and sometimes subsidizes their losses. LGFVs may also generate revenue and some may be operated on a commercial basis, which underscores that the augmented fiscal data should be viewed as a complement, not a substitute, to the traditional government data.¹

- *Augmented government debt* captures borrowing by LGFVs through market financing channels. As in other countries, it excludes liabilities of regular SOEs and other state entities as well as contingent liabilities, such as NPLs in the banking sector, policy bank loans, and pension liabilities. At the same time, it measures gross debt only, and so excludes government assets.
- *Augmented net borrowing* adds to government net lending/borrowing the market financing of LGFVs (through banks, bonds, and trusts), data on which are incomplete and filled in using IMF staff estimates. This measure captures transactions in financial liabilities—that is, debt creating flows, and thus closely corresponds to the change in augmented debt.
- *Augmented fiscal deficit* adds both market financing of LGFVs and financing from selling land usage rights (net of costs such as resettlement and compensation). Land sales are treated as a financing item akin to privatization, but do not contribute to debt accumulation. This is an analytical concept justified by the IMF’s Government Finance Statistics (GFS), and well-suited to capturing the overall impact of fiscal policy on aggregate demand.

Bottom-line. On this basis, IMF staff estimate the *augmented government debt* has risen to nearly 50 percent of GDP in 2012, having increased sharply through the global crisis but still at a well-manageable level. For 2012, staff estimate that the *augmented net borrowing* was around 8 percent of GDP and the *augmented fiscal deficit* was on the order of 10 percent of GDP. These estimates are preliminary and will be refined as more information becomes available.

¹ Government is defined as general government, which is the consolidated central and local government.