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Original Paper

Effect Measurement and System Optimization of Special Debt in Promoting High-Quality Development of Local Economy

Xinyuan Wang[1]

[1] Anhui University of Finance and Economics, Bengbu, 233030, China

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Abstract

The rapid expansion of the scale of special bonds stems from the mode transformation of local finances under continuous pressure. As land finance is unsustainable and hidden debts need to be resolved urgently, special bonds will inevitably bear the important responsibility of maintaining the sustainable development of local finances and stimulating the high-quality development of local economies. It is recommended to re-sort out the development responsibilities of local governments under the framework of fiscal decentralization, give full play to the financing role of special bonds in high-quality development areas such as infrastructure, industry, environmental protection, and people's livelihood, and establish corresponding incentive compatibility and risk control mechanisms to enhance the efficiency of fund utilization and avoid the accumulation of debt risks again.

Keywords

special bonds, economic growth, local finance, debt risk

1. Introduction

1.1 The Origin of Special Bonds

Under the tax-sharing system, fiscal power among governments has been transferred upwards, while administrative power has been transferred downwards. Especially after the 2008 financial crisis, local governments responded to the impact of the financial crisis by investing heavily in infrastructure through debt, and debt risks have accumulated accordingly (Gan, Yu, & Zheng, 2011). In response, the state adopted the measure of “opening the front door and blocking the back door”. The Budget Law of the People's Republic of China promulgated in 2014 formally granted local governments the right to raise debt financing, and issued the Opinions of the State Council on Strengthening the Management of Local Government Debt (Guofa, 2014, No. 43) in the same year, which divided local debts into two types: general debt and special debt according to the purpose of funds and the source of debt repayment funds, and formed general debt and special debt respectively.

Comparing general bonds and special bonds, we can find that both are issued by provincial governments, endorsed and guaranteed by local finances, and included in the local fiscal budget system, but there are also many differences between the two. First, from the perspective of function, the issuance of general bonds is mainly to improve fiscal deficits and alleviate temporary funding difficulties of local governments. Special bonds are mainly issued to support the construction of special projects, and the funds are generally used for public welfare projects with certain returns (Sun & Yang, 2014). As a financing tool with both fiscal and financial attributes, the support areas of special bonds have gradually expanded, from the initial replacement special bonds and land reserve special bonds to 11 important areas including new infrastructure, new energy, and ecological and environmental protection. Secondly, there are also differences in the sources of funds for repayment of principal and interest between the two (Tao & Xu, 2021). General bonds are mainly repaid with general public budget revenue, while special bonds are repaid with government fund revenue or special revenue corresponding to public welfare projects. It should be noted that the "Notice on Piloting the Development of Local Government Special Bonds with Self-Balanced Project Income and Financing" (Caiyu, 2017, 89) requires that the project income of special bonds should be balanced with self-financing.

1.2 Characteristics of Special Bonds

my country's special bonds have three major characteristics. First, the proportion of special bonds in local government bonds is on the rise. According to the issuance of special bonds in local government bonds, new bonds and refinancing bonds2, since my country's local governments began to issue special bonds in 2015, their proportion in local government bonds has increased from 25.41% in 2015 to 69.65% in 2022, their proportion in new bonds has increased from 16.22% in 2015 to 84.90% in 2022, and their proportion in refinancing bonds has increased from 19.92% in 2018 to 41.87% in 2022 (no refinancing bonds were issued from 2015 to 2017). bonds), indicating that special bonds are increasingly important to local government financing. As of early October 2023, the cumulative amount of special bonds issued nationwide this year has reached 4,795.589 billion yuan, accounting for 68.11% of the local government bonds issued that year[4]. Among them, the issuance of new special bonds was 3,448.651 billion yuan, accounting for 84.19% of the new bond issuance; the issuance of refinancing special bonds was 1,345.077 billion yuan, accounting for 45.76% of the issuance of refinancing bonds.

Second, the issuance of special bonds shows significant regional differences in my country. The provinces at the forefront of special bond issuance are mostly provinces with good economic development in my country. Taking the issuance of special bonds in various regions across the country in 2022 as an example, the provinces with the largest issuance scale are all provinces with relatively good economic development in my country. As of early October 2023, the regions with the largest issuance of special bonds this year are Guangdong, Shandong, and Anhui. Among them, Guangdong ranked first with an issuance scale of 494.259 billion yuan; Tibet, Qinghai, Ningxia and other regions had smaller special bond issuance scales in the first nine months. In the current context of increasing fiscal pressure on local governments, the difference in issuance scale reflects the demand and adaptability of local governments for bond financing tools.

Third, medium- and long-term special bonds are gradually increasing. In the early days of issuance, the issuance period was mainly 3 or 5 years. In 2019, the Ministry of Finance lifted restrictions on the term ratio structure of local bonds and increased the issuance ratio of long-term bonds for reasons such as easing the refinancing pressure of local governments and improving the matching degree of project funds and terms[5]. Since then, the average issuance period of local bonds has risen rapidly, and the average term of special bonds has increased significantly. The issuance period has also been extended from 6.1 years in 2018 to 15.5 years in 2022. Special bonds are transforming from short-term bonds to medium- and long-term bonds. The short-term risks of local finances have been reduced, and long-term risks have accumulated to a certain extent.

1.3 The Impact of Special Bonds on Local Finances

Since 2015, the issuance of local government special bonds has been increasing year by year. From 2015 to 2022, the annual issuance of new special bonds was 95.9 billion yuan, 403.7 billion yuan, 793.7 billion yuan, 1352.7 billion yuan, 2148.7 billion yuan, 3601.9 billion yuan, 3584.4 billion yuan, and 4038.4 billion yuan, respectively. The growth rate of issuance scale was faster than the growth rate of Gross Domestic Product (GDP), fiscal revenue, and land transfer fees. As an important tool for local government financing, special bonds have a certain role in promoting local economic growth (Wei & Ren, 2012). Local governments can meet fiscal needs by issuing new special bonds, thereby alleviating local government fiscal pressure to a certain extent. At the same time, the decline in the growth rate of land transfer fees and the increase in the scale of special bonds indicate that there has been a significant change in the source of local government fiscal revenue.

2. Discussion on the Relationship between Special Bonds and High-Quality Development of Local Economy

2.1 The Connotation of High-Quality Development of Local Economy

At present, my country's economy has entered a stage of high-quality development from high-speed development. As an important tool for the effectiveness of proactive fiscal policies, special bonds have an important impact on improving the quality and efficiency of local economic development. Therefore, it is necessary to analyze from the perspective of special bonds, combine the policy requirements of stabilizing growth and preventing risks, and explore the new connotation of high-quality development of local economy from multiple dimensions and indicators.

Debt ratio shows government's ability to resist risks

This article uses the government debt ratio as an indicator to measure the government's ability to resist risks. First, the total government debt (the sum of the central government's treasury debt balance and the national local government debt balance) is calculated as the proportion of GDP, and the government debt ratios from 2015 to 2022 are 37.67%, 36.66%, 36.04%, 36.36%, 38.63%, 45.93%, 46.76%, and 50.35%, respectively. Although the overall trend is upward, it is still below the EU's 60% red line, which shows that my country's government debt indicators are still stable. The balance of local government debt accounts for more than 50% of the total government debt each year, which may mean that local governments have assumed the main responsibilities in local economic development and infrastructure construction, but the financial power cannot match the responsibilities.

Special bonds account for about 60% of the balance of local government debt and 17.08% of GDP, which shows that local governments prefer to raise funds through special bonds. The issuance of special bonds will help promote the development of specific projects and fields such as infrastructure construction and environmental protection, but we also need to be vigilant about debt management and risk control issues. Therefore, we need to pay more attention to the use and benefits of special bond funds, as well as the ability of local governments to manage debt scale and risks, and do a good job of risk prevention while stabilizing growth.

2.2 Regional Economic Development Level and Special Bond Issuance Scale

To measure the high-quality development of the local economy, it is necessary to evaluate the level of regional economic development, and the scale of special bond issuance can reflect this to a certain extent. On the one hand, the original intention of issuing special bonds is mainly to support local infrastructure construction. Infrastructure construction is an important foundation for the high-quality development of the regional economy. Therefore, the scale of special bond issuance can indirectly reflect the investment intensity and attention of a region in infrastructure construction-related projects. Generally speaking, if the scale of special bond issuance in a certain region is large, the infrastructure conditions in that area are relatively good, which is conducive to improving the quality of economic development.

On the other hand, the scale of special bond issuance is also closely related to the fiscal situation of local governments. Generally speaking, the larger the actual issuance scale of special bonds, the stronger the fiscal bearing capacity and debt repayment capacity of local governments are likely to be. On the contrary, regions with poor fiscal conditions have relatively weak debt repayment capacity, which may limit the application of special bonds when applying for quotas, and the final scale of bond issuance will also be small. Observing the scale of special bond issuance in various parts of my country, it can be found that the scale of special bond issuance in the eastern region or economically developed regions is often higher than that in the western region or economically underdeveloped regions.

2.3 Regional Market Operation Status and the Marketization Level of Special Bonds

The combination of "effective market" and "effective government" is a necessary prerequisite for the high-quality development of local economy. Special bonds, as a financing tool with both fiscal and financial attributes, play a vital role in both. The full combination has far-reaching impact. Improving the marketization level of special bonds can increase market liquidity and investment options, and can also promote the improvement of market standardization and transparency. Therefore, by measuring the marketization level of the special bond market, it is possible to provide a basis for analyzing the effectiveness of regional bond market operations.

2.4 Special Bonds Pose Challenges to the Sustainability of Local Finances

Although special bonds can fill the gap between fiscal revenue and expenditure and help the local economy continue to grow, my country is currently facing an objective environment where tax cuts and fee reductions reduce fiscal revenue, land fiscal risks increase, and fiscal expenditures are rigid. Special bonds will also increase the government's debt repayment pressure, making the sustainability of local finances face certain challenges. First, the continued prosperity of the real estate market for many years has enabled local governments to obtain a large amount of income through real estate-related taxes and land transfer fees, and has provided a stable source of funds for fiscal expenditures and debt repayments.

As the real estate market goes down, related taxes and land transfer revenues will be affected, increasing local finances. political pressure. The amount of special bond issuance available to local governments will also be limited due to worsening financial conditions. Secondly, taking into account the limited land resources and the need for healthy development of the real estate market, the growth rate of land transfer revenue has declined significantly in recent years, and the future growth space is also relatively limited. This may increase the risk of local government debt repayment and affect the local fiscal situation. Stable operation.

3. Related Suggestions

3.1 Building a New Framework for Fiscal Decentralization

First, adjust the tax sharing ratio and improve the local tax system. When local governments bear the main responsibility for fiscal expenditure and debt repayment, consider increasing the local tax sharing ratio and cultivating local tax sources, thereby giving local governments more financial power and ensuring the effective realization of government functions. For example, the collection of consumption tax can be moved back and gradually adjusted from a central tax to a local tax; the local share ratio of shared tax can also be appropriately increased. Second, consider moderately relaxing the authority of local governments to raise debt financing. Through the calculation of the government debt ratio in the previous article, it can be found that my country's local government debt indicators are currently in a reasonable range, so the restrictions on local government bond issuance can be moderately relaxed.

Of course, while empowering, it is also necessary to strengthen supervision of local debt management to prevent excessive government debt and affect local fiscal sustainability. Third, strengthen budget management and standardize revenue and expenditure behavior. When building a new framework for fiscal decentralization, in addition to giving local governments financial resources, relevant fiscal systems should be improved, budget constraints should be strengthened, and the transparency of local fiscal operations should be improved to ensure the stability of economic growth.

3.2 Further Improve the Marketization Level of Special Bonds

First, we need to increase the diversification of the special bond investor structure. According to my country's current local bond investor structure, although its diversification has increased compared to 2015, commercial banks still account for 82.51% of investors. Therefore, in the future, we can attract other types of investors through tax incentives and other means, and provide more opportunities for individual investors. Open up more convenient investment channels to improve the market liquidity of special bonds and provide more sources for special bond financing. Second, improve the transparency of special bond information disclosure. Information disclosure can improve information asymmetry, help investors better understand the operation of the special bond market, and make more scientific investment choices based on their own circumstances.

At present, the information disclosure of special bonds is insufficient, and some information can only be inferred through the overall data of local bonds. More detailed and comprehensive information disclosure should be one of the directions for optimizing the special bond system in the future. Third, it is necessary to improve the credit rating system for special bonds. First, since special bonds are issued by provincial governments, and the bond users may be municipal and county governments, the issuer as the rating object cannot truly reflect the use of special bonds. If the rating agency is single, the report issued will lack verification, and there may be rent-seeking, which will affect the marketization level of special bonds. Therefore, in the future, information disclosure should be made on the bond users and the bond use situation, and a more scientific and comprehensive credit rating indicator system should be established based on this. At the same time, it should also be considered to select different institutions in the initial credit rating, subsequent tracking rating, and irregular rating of special bonds, so that the reports can be mutually verified and the authenticity and reliability of the rating results can be increased.

3.3 Promote Industrial Upgrading through Multiple Financing Tools

At present, in addition to special bonds, non-public debt means such as the government-private partnership model (PPP) and infrastructure real estate investment trusts (REITs) can also help the government carry out various types of investment and financing. In comparison, special bonds have a strong financing function and help to form physical workload, but they are limited by debt limits and cannot solve all the funding needs of local governments, and the review procedures are relatively complicated. PPP has the advantage of high investment efficiency due to its characteristics of sharing benefits and sharing risks, but at the same time, due to the low credit of social capital, its financing cost is higher than that of special bonds. REITs have the advantages of stable returns and reduced debt risks, but my country will not officially start the REITs pilot until 2020, and the relevant system still needs to be improved. In summary, in the future, we can try to effectively integrate special bonds with PPP or REITs to achieve the purpose of reducing project financing costs, improving investment efficiency, and alleviating debt risks.

3.4 Establishing an Incentive-Compatible Risk Prevention and Control Mechanism

Establishing an incentive-compatible special bond risk prevention and control mechanism means that local governments should not only use special bonds to stimulate local economic development, but also do a good job in debt risk prevention. First, it is necessary to build a special bond performance evaluation mechanism for the entire life cycle. my country's current performance evaluation system is mainly based on general public budget expenditure projects, while special bond projects are both public welfare and profitable, and have a long project cycle and great uncertainty. It is difficult to perfectly adapt to the current performance evaluation management mechanism. In the future, it is urgent to adjust the special bond performance evaluation mechanism. In this process, attention should be paid to the entire life cycle of the project, and performance evaluation should be carried out throughout the entire process of special bond issuance, fund use, debt repayment, and project income generation, so as to achieve supervision and risk control in the entire process before, during, and after the event.

At the same time, it is also necessary to trace the cause from the result, timely analyze the causes of related problems and optimize them, and promote more efficient use of funds. Second, it is necessary to strengthen risk prevention and control from both vertical and horizontal directions. From a vertical perspective, if the main users of special bonds are city and county governments, there may be a problem of weakening debt repayment awareness and shifting the pressure of debt repayment upward; from a horizontal perspective, due to the prevalence of the "GDP-only" performance evaluation method in some regions in the past, coupled with government term limits, local governments may "borrow but not repay", bringing greater debt repayment pressure to the new government. Therefore, while appropriately granting local governments financial power incentives, provincial governments should also strengthen risk supervision of city and county governments, implement debt repayment responsibilities, strengthen risk assessment and early warning mechanisms, and establish accountability mechanisms and emergency measures to deal with unexpected risk events.

Conflicts of Interest

The author declare that there is no conflict of interest regarding the publication of this article.

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