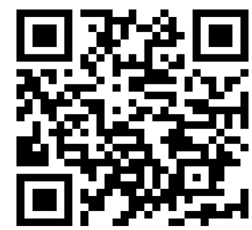
International Journal of Language Learning and Applied Linguistics

ISSN: 2835-1924
Volume 2 | No 4 | April -2023



Public Debit: An Overview

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Public debt refers to the borrowing of capital by the government from citizens or other entities within a country or from foreign sources. In most cases, the government utilizes the borrowed funds for capital expenditures like infrastructure development, military equipment acquisition, and social programs. Public debt is a common practice in almost all countries globally, with varying levels of debt incurred by the respective governments.

Public debt is a two-way street with its advantages and disadvantages. Proponents of public debt argue that it is essential since it provides the government with the necessary capital to run and develop crucial projects, much of which benefit the public at large. On the other hand, critics argue that the government's current public debt levels put the future of its citizens in jeopardy through increased interest rates, inflation, and heavy taxation.

The scale of a country's debt is usually measured in terms of its debt-to-GDP ratio. The debt-to-GDP refers to the percentage of the government's debt over the country's gross domestic product (GDP). A country's debt-to-GDP ratio is used as a metric for measuring the time it would take for the government to pay off its entire debt. It also helps creditors evaluate a country's ability to repay its loans. A lower debt-to-GDP ratio implies that the government is generating ample revenue to pay off its current debt and is unlikely to default on future loans.

How do governments incur public debt?

Governments can borrow funds from the public in various ways, including:

A. Treasury bonds: A country's Treasury issues bonds to the public to raise public debt. Treasury bonds are long-term securities issued to the public in fixed denominations and pay interest regularly.

B. Development bonds: These are long-term bonds issued to fund critical national infrastructural and developmental projects.

C. Short-term Treasury bills: These are short-term securities issued by the government, usually with a duration of less than one year. They are issued to finance short-term projects and government expenditures.

D. Loans from foreign countries and international financial organizations: Countries can secure loans from foreign countries and international organizations like the World Bank, IMF, and African Development Bank to fund developmental projects and other government expenditures.

Advantages of Public Debt

A. Funding for critical projects: Governments borrow funds in public debt to finance government programs, social welfare services, and infrastructure development. These are vital developmental projects that help to improve the quality of citizens' lives, especially in developing countries.

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B. Economic stimulation: Sometimes, borrowing money can help stimulate a country's economic growth. For example, the government can borrow money to construct new roads, thus creating job opportunities and stimulating growth within the construction industry. The government can also use debt to finance social programs such as education, leading to a more educated workforce.

C. Debt financing has lower costs: Public debt financing is often considered to have lower costs compared to other forms of finance, making it an attractive alternative. Interest rates on government bonds tend to be lower because they are considered less risky, and there is less likelihood of default.

Disadvantages of Public Debt

A. Burdens the economy: Public debt poses a great danger to a country's economy, especially when the government's borrowing levels are too high. High debt levels typically lead to increased taxation to service the debt, reducing disposable income and private investment.

B. Impact on future generations: Public debt is often considered an intergenerational issue since it impacts future generations who must pay off the debt. When a government borrows heavily, it means that future citizens of the country will have to pay for current borrowing levels. This can cause resentment and tensions between the current and future generations.

C. Increases interest rates: When governments borrow heavily, it often leads to the creation of money by central banks leading to higher interest rates as well as a decrease in the purchasing power of currency. This leads to decreased private investment due to higher borrowing costs, discouraging growth.

Conclusion

Public debt is an important tool for governments to finance critical projects and development initiatives. However, borrowing without a comprehensive plan can lead to significant levels of debt, which can burden an economy for years. Governments must carefully weigh the advantages and disadvantages of public debt before deciding to borrow. The debt-to-GDP metric is an important indicator of a country's ability to pay back its debt with a lower debt to GDP ratio implying a stronger economy. Therefore, governments must implement sound macroeconomic policies to ensure the country's debt levels remain sustainable.