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Public Finances of India: Are You Surprised?

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ABSTRACT

Public finances in India are at a turning point. Analysis of the past data shows that no major improvement in any of the major fiscal indicators. Restructure of debt, reforms in power sector and implementation of other issues under MTFRP hold promise for future. The Centre is carefully treading the path of fiscal prudence but State finances are slipping. The main objective of this paper is to suggest restructuring of public finances of the Centre and state governments to provide macroeconomic stability, equitable growth in the country and improve efficiency of resources. The paper also suggests ways to augment revenue resources and contraction in expenditure On the contrary, other fiscal indicators have shown significant deterioration. Thus the claims about fiscal adjustment are illusory. Fiscal consolidation in India perhaps need more attention and commitment. A comparison of deficits of Centre and state are made from period 1991-92 to 2016-17.

Keywords: Public Finance, India, Revenue, Expenditure, Deficits
JEL Classifications: H1, H2, H5, H7

1. INTRODUCTION

The financial condition of Indian government has been a cause for concern for some time now. In some of their main deficit measures, the combined financial situation of the Center and state governments has shown a noticeable deterioration over the years. Previous data analysis shows no significant changes in any of the fiscal initiatives. Debt restructuring, reforms in the power sector and other issues brought under Meduim term fiscal reform programme have commitment for the future. The Center walks the road of fiscal prudence cautiously, but government finances are sliding. The main aim of this paper is to propose reforming the Centre's and state governments' public finances to provide macroeconomic stability, equitable development in the region, and enhance resource performance. The paper also proposes ways of rising revenue opportunities and reducing expenditure.

The Covid-19 crisis is likely to give government financial management a tough time as it may affect its divestment plans, a reduction in tax collections in the midst of sluggish growth, and pressure on fiscal deficit goals. The Covid-19 pandemic will have a major effect on the finances of both the centre and state (Mannu Arora and Shivani Phaugat, 2020).

Fiscal deficits are likely to worsen and the burden on GST collections may be felt. India needs to maintain reasonably sound public finances to stave off a possible second wave of financial sector risks once the coronavirus crisis has diminished.

"Coronavirus-lockdown-and-the-state-of-state-finances", 2020, The national shutdown to avoid Covid-19 from spreading has left state government budgets in a challenging situation. The Centre has its own revenue problems and increasing investment demand, but at least it's its own boss. Not so for states that may depend on the Center to assign funds under different headings. This reliance became especially acute after the implementation of GST, in which the Center had to compensate for the 5-year loss of revenue ending in 2022.

"Public-finances-stretched-to-mitigate-the-impact-of-covid", 2020 The Reserve Bank of India (RBI) has warned that public finances

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have been stretched by the imperative to mitigate the impact of the pandemic, and headroom for continuing support to aggregate demand may be severely diminished.

According to a RBI report on state finances, own tax revenue accounts for just under half (45 percent) of total state revenue; 47.5 percent of central transfers. 90 per cent of own tax revenue comes from liquor taxes, electricity supply, stamp duties and vehicle registration. All these are below pressure now. There have been no new vehicle and property registrations since the lockout began, and no liquor sales, either. As economic activity is at a halt and cars and planes are not moving oil prices have fallen by almost half. As a result, states' own tax receipts decreased by 80-90 per cent, leaving their budgets unchecked.

The great Lockout's recession is putting tremendous pressure on government finances. Fiscal pressure is still high in India, since the country is going through a time of economic slowdown. In that context, the cost associated with the distribution of Covid-19 brings more strain to government finances. According to the collective budget of the central government, tax revenue accounts for about 80 per cent of the total revenue receipts. The government has set a Rs 16.3 lakh crore tax revenue target for FY21, with a growth rate of 8 per cent from the previous fiscal year. Development of tax revenues in each country depends on how well the economy performs and how well the economic activities take place. In the current scenario, the economic activity in the country is highly affected in the midst of the lockdown and an uncertain climate

The service sector has a share of Gross Value Added (GVA) about 55 per cent. Within the service sector, travel, hotels, transportation, networking and broadcasting-related services account for 18 percent of total GVA. The travel and tourism industry is badly affected by the current crisis, and doubt exists as to when those industries will resume their normal operations. The situation is no different for the manufacturing sector which has multiple factories in shutdown. The agricultural sector also faces crisis because it is inaccessible to the laborers.

GST has the largest percentage of corporate tax and income tax-led tax revenues. GST collection represents the state of the country's economic activity and declined in March against Rs 1,05 lakh crore collected in February to Rs 97,597 crores. GST collection will be much lower for April, the opening month of FY21, as the domestic economy is in complete lockdown until 3 May. In the coming months, even, the downward trend will continue. A similar trend will become apparent in the case of corporate taxation and income taxes. Corporate tax and income tax depend on corporate and individual profit/earnings rise, which in turn is linked to economic activity.

The target for tax revenue was set at Rs 16.3 lakh crore, considering a nominal GDP growth rate of 10 per cent. The IMF has, however, downgraded India's GDP growth rate to 1.9%, and bringing the inflation rate to 4%, India's nominal GDP growth rate will drop to 6%. In such a situation, growth in tax revenues will be substantially lower than the target being budgeted.

For non-tax income the target for FY21 is set at Rs 3.8 lakh crore. Dividends and dividends are the main component of non-tax revenues. Considering the Open Market Operations (OMO) carried out by the RBI in FY20, the government is expected to benefit from the central bank 's transfer of dividends. In the last fiscal year, RBI transferred Rs 1.23 lakh crore as an annual dividend to the government following a significant number of RBI-led OMOs in FY19.

Similarly, the disinvestment goal, which is the major component of the capital receipts set at Rs 2.1 lakh crore, would also be difficult to achieve. The poor state of the stock market makes it difficult to grasp the government's disinvestment receipts. Similarly, in the present scenario, given the poor health of the aviation industry, it would be difficult to get a potential buyer for Air India. In short, the Government will face severe revenue crunch in the current fiscal year. The state condition is similar to, or even worse, too.

But India should safeguard public finances, a previous data review shows no change in any of the fiscal parameters. Power sector reforms, Debt restructuring and other issues put in place under MTFRP are promising for the future development. While the deterioration in fiscal parameters over the last decade can be attributed to close causes such as employee compensation revision or sluggish growth in revenues due to economic downturn, the state budget imbalances stem from systemic factors (Anand et al., 2001). Like most other areas of change, Indian fiscal adjustment story was the one of a symbolic exercise.

The effort has been to take the least resistance in carrying out changes. The manner in which the government has identified fiscal indicators as targets for correction and its numerous attempts to mask and window-dress the numbers on different fiscal indicators accurately illustrates this proposal (Rao, 2000).

2. REVIEW OF LITERATURE

India has several reports on fiscal reforms and related problems at the State level. This segment deals with the research while similar studies are being conducted. Rao (1981) makes a study to examine and classify the determinant of the tax revenue and unplanned government spending by the States against their medium-term estimates. For the purpose of studying the deciding time series the researcher chose the following states Kerala Karnataka West Bengal and Orissa. This study looked at the determinants of both politics and economics.

It also studies the influence of political and economic powers on the fiscal decision making of the four States. The study summarizes the determinants of unplanned revenue expenditure by summing up the growth expenditure on various services provides this for all four states except Orissa. Orissa is single state where the rise in unplanned tax expenditure is attributable to the increased amount of public services.

Lahiri (2000) discuss the reforms at the Indian state level in their paper. The factors that led to the spread of state-level reforms in India are also listed. According to these authors, India cannot reform and reinvigorate the governments of the states.

In his paper (1999), Kurian attempts to highlight the deteriorating trend of state finances over recent years. "Failure on the part of

States to curtail wasteful spending and inability to raise extra revenue" are key problems facing most state budgets. In the aftermath of economic reforms, tax wars between states to attract private investment, as well as extreme populism and revision of employee pay led to demand for state funding. There will be no break in State finances if they turn to drastic measures.

Rao (Jan, 2002) they discuss the rational ways in which central and state governments in India can increase their tax revenues. According to them, no effort was made to modernise tax administration. All States administration is manual based. The two important steps to be taken in order to raise revenue are Computerization and major tax administration modernization reform, as well as successful dissuasive action against tax evaders and fraudulent taxpayers.

Kurian (2003) some investment success in the Center has been achieved in his work but the finances of the state have declined drastically. Any downward trend in the Union's government's finances and corresponding decline in the country's devolution would further reduce the country's regional imbalances. Anand et al. (Jan, 2002) have addressed the causes of fiscal mismanagement at the state level, citing deficiencies in the system of intergovernmental fiscal ties as the primary causes of fiscal indiscipline among states requiring corrective action.

Anand et al. (2002) saw the consolidated fiscal deficit (Center plus states) of the government at about the same amount at the end of the decade as it is even after a decade of correction at the beginning of 10 percent of GDP. State-financial crises are rooted in some deep-seated fiscal instability which demands structural reforms. The weakness lies in the system of revenue, budgeting, and financial intergovernmental ties. To the weakness of the above-mentioned fiscal system the fiscal deficit must be handled frontally.

The Research led by Bhargava (2002) dealt with structural reforms at State level. The State should play a complementary role and outcomes complementing the efforts made by the Center to support and revive the fiscal situation. It is now correct time that the constitution introduced income tax on agriculture to raise State revenue.

Rao (Jan, 2002) they discuss the rational ways in which central and state governments in India can increase their tax revenues. No big effort has been made to modernise the tax administration according to them. Analysis shows that the decline in the fiscal deficit was comparably negligible. On the opposite, other fiscal policies have been showing considerable deterioration. And the claims around tax-adjustment are illusory. In India, fiscal consolidation may involve yet another crisis (Rao, 2000). Hajra and Rakhe, 2008 in their paper analyses the pattern and composition of tax transfers in India, and presents some options/proposals that Thirteen Finance Commission may consider. In his article, Rao (2017), analyse major issues in India's public finances in the context of India's economic growth. Based on the average conduct of the 98 countries, the paper shows that the tax-GDP ratio for the country is 2-3 percentage points lower for its per capita GDP level. The reasons for the low tax ratio must be found in the exemption from farm income, widespread tax preferences due to different tax policy goals, global tax manipulation and weak tax management. Weak tax collections are also the reasons for keeping the deficits and debts high. Acharya (2001) provides a comprehensive review of India's macroeconomic performance and policies during the last 10 years. The nineties have ended but macroeconomic challenges continue.

Ahluwalia (2000) talks about liberalisation has reduced the degree of control exercised by the centre in many areas, leaving much greater scope for state level initiatives. This is particularly true as far as attracting investment, both domestic and foreign, is concerned. State level performance and policies therefore deserve much closer attention than they receive.

Joshi and Little (1996) focuses on the economic reforms introduced after the financial crisis of 1991. The authors examine the different areas of the economy and outline the successes and effects of reform measures.

Purohit (2001) talks about roadmap for national and sub national VAT in India.

Raju and Amar Nath (2000) talks about the story of fiscal adjustment in India is one of missed opportunities. The crisis did initiate reforms in right earnest, but once the immediate problems were overcome, rather than achieving fiscal consolidation, the attempt in successive budgets has been to create the illusion of achieving fiscal correction rather than really achieving it.

Rastogi (2004) says public finances in India are at a turning point. Analysis of the past data, however, shows no improvement in any of the major fiscal indicators. Restructure of debt, reforms in power sector and implementation of other issues under MTFRP hold promise for future.

Vadra (2012; 2012 a; 2012 b; 2012 c) talks about the era of frequent elections and competitive populism practiced by different political parties aspiring for power, the regime of responsible public finance has become extremely difficult. As we look ahead there are many unfinished agenda awaits us. At the top of this agenda is reforms and in that of fiscal reforms.

Vadra (2013; 2013 a) says that the States is facing a severe financial crisis. The mounting revenue deficits accompanied by rapid increase in revenue expenditure and slow growth of revenue receipts, inadequate own revenues, declining Central assistance and negative contribution by public enterprises have kept the developmental expenditure of the State at low level.This paper studies the structure and trends in public finances of fiscal scenario of the southern states of Karnataka, Kerala, Andhra Pradesh and Tamil Nadu and make a comparison of their finances these states from1999 to 2008-10. The study examines the key indicators in four categories deficit management, financing fiscal deficit, revenue and expenditure management and debt management and dependence of funds on center.

3. EMERGENCE OF FISCAL CRISIS IN INDIA

Over the years, in the face of insufficient sales buoyancy, the Center has seen a swelling of non-plan expenditures. They

responded by using higher and higher borrowing amounts to fund programme spending, which is decreasing as a percentage of GDP. This led to a steady accumulation of debt, which in turn created a growing interest burden the unsustainable discrepancy between government revenues and expenditure was one of India's crises of 1990-1991.

The tax shortfall was offset by running surpluses on the Government's capital account. Such budget capital surpluses would prove counterproductive to long-term economic growth prospects. The steady fall in the tax account has brought an increase in the gross fiscal deficit.

The tax deficit has been offset by running surpluses on the capital account of the Government. Such surpluses in budget resources will prove detrimental to expectations for long-term economic development. The gradual decrease in the tax account has caused the gross fiscal deficit to grow.

The fiscal reform process that began in India after 1991 clearly underpins the objectives of macroeconomic stability and development. Efforts to regain control of the macroeconomic situation by fiscal reform have been a global phenomenon since the early 1980s, this time unfolding domestic and external debt events, high inflation rates and strong announcements of growth potential for many developing countries.

The two most important reasons were India's global context, and the expediency of the 1991 situation, which contributed to a thorough series of reform measures being introduced in the Indian economy. The fiscal adjustment mechanism initiated in 1991 as part of the Centre's structural reform programme was strongly focused on reducing the Centre's fiscal deficit. The Central Government's budget deficit became a matter of serious concern to Indian policy-makers.

The precarious fiscal situation of the Center required bold and decisive policy measures to reduce the fiscal deficit of the Centre. Since 1991 the Center has carried out a number of tax reform proposals as part of ongoing economic reforms. The overall effect of these changes has not been seen positive on Central Government finances. The Centre's tax GDP ratio, which in the late 80's hit a level of over 11 percent, has fallen below 10 percent in recent years. But the attempt by the Center to control its deficit has resulted in fiscal deficit staying below 6 per cent. Subsidies were eliminated, and deficit monetized was practically reduced.

Center is concerned about the deterioration of state finances for states and offers a helping hand for states to resolve their fiscal deficit. The deterioration of state finances has become a major problem in recent years as it has prompted a drastic reduction in development budget funding and has led to considerable borrowing even to fund current expenses, primarily wages for workers and interest payments. Indeed, the situation for the reform agenda at the state level is not grim without which government finances won't improve. States cannot even retain existing public properties, they are alone creating new facilities and expanding infrastructure on the required scale.

Despite central government attempts to reduce the substantial tax adjustment burden on states, the unwelcome fiscal condition continued to exist even after 10 years of fiscal reform. Clearly the Center cannot bail out any state because it borrows heavily to cover the wide gaps in tax expenditure that resulted in lower capital status.

States borrow from the market as previously agreed with the Reserve Bank of India and, with increased borrowing and higher interest payments, the fiscal position of the States cannot be improved without bold and drastic measures, such as charging user fees for all utilities such as electricity, irrigation, transportation water, etc.

The buildup of public debt and the debt interest burden, which is now the largest and fastest-growing component of spending, fueled further growth in revenue spending. These have resulted in a downward spiral of rising deficits, growing debt, increasing interest rates and widening the deficit described as a debt trap by some analysts.

4. CENTRAL GOVERNMENT FINANCES

The Centre's fiscal deficit, and in particular its revenue deficit, remains a matter of serious concern. Since 1997-98 the fiscal situation has deteriorated especially. (This is largely due to a tax fall: GDP ratio and a further increase in non-interest income spending, which, combined with the continuing rise in interest payments, has resulted in a substantial decrease in the capital expenditure ratio to GDP.

Table 1: Key Deficit Indicators of the Central Government (Rupees Crore), 1991-1992 to 2016-2017

Year	Gross fiscal deficit	Gross primary deficit	Revenue deficit
1991-1992	36,325	9729	16,261
1992-1993	40,173	9098	18,574
1993-1994	60,257	23516	32,716
1994-1995	57,703	13644	31,029
1995-1996	60,243	10198	29,731
1996-1997	66,733	7255	32,654
1997-1998	88,937	23300	46,449
1998-1999	113,349	35466	66,976
1999-2000	104,716	14467	67,596
2000-2001	118,816	19502	85,234
2001-2002	140,955	33495	100,162
2002-2003	145,072	27268	107,879
2003-2004	123,273	–815	98,261
2004-2005	125,794	–1140	78,338
2005-2006	146,435	13805	92,299
2006-2007	142,573	–7699	80,222
2007-2008	126,912	–44118	52,569
2008-2009	326,515	133821	241,273
2009-2010	400,996	175485	282,735
2010-2011	13,735.91	1395.69	2522.52
2011-2012	5159.90	2428.40	3943.48
2012-2013	490.190	1770.20	3642.82
2013-2014	5028.58	1286.04	3570.48
2014-2015	5108.17	1083.04	3656.11
2015-2016	5350.90	924.99	3415.09
2016-2017	5339.04	412.34	3540.15

Source: Budget documents of the State Governments

This decline in capital spending occurred across the board across both the social and infrastructure sectors. Declines in the tax-to - GDP ratio are also due to shifts in the economy's sectoral composition. During the 1990s, the industrial sector remained relatively stagnant, while agriculture remained largely untaxed and its share of GDP is decreased.

The service sector, on the other hand, has grown rapidly but service taxes account for just a small fraction of revenue. On the expenditure side, the sharp rise in current spending consists mainly of spending on pledged interest payments, guided by the rapid growth in public debt, and large rises in the wage bill following adoption of the Sixth Pay Commission recommendations. The problem has been further compounded by downward rigidities in military spending and subsidies because of security issues and political economic constraints.

Central government's gross fiscal deficit was Rs 36325 crores (5.5 per cent of GDP) in 1991-92 which increased to Rs 360243 in 1995-1996 and then to Rs 118816 crores in 2000-2001. It increased further to Rs 400996 crores in 2009-2010. It increased further to Rs 5339.04 in 2016-2017.

In terms of revenue deficit, it was Rs 16261 in 1991-92 which increased further to Rs 107879 in 2002-2003 and then to Rs 282735 crores in 2009-2010 which increased further to Rs 3540.15 crores in 2016-2017. The primary deficit also showed a growing pattern over the period (Table 1).

Deficits are a systematic Government fiscal health measure. Fiscal deficits (total receipts with the exception of borrowings minus total expenditure expressed as a share of GDP) for state governments to imply stability in state GDP finances. It is the main computed factor in the fiscal deficit which has been a growing trend.

Table 2: Key deficit indicators of Central Government (As Percentage to GDP)

Year	Gross Fiscal Deficit	Gross Primary Deficit	Revenue Deficit
1991-1992	5.55	1.49	2.48
1992-1993	5.34	1.21	2.47
1993-1994	6.96	2.72	3.78
1994-1995	5.68	1.34	3.05
1995-1996	5.05	0.86	2.49
1996-1997	4.84	0.53	2.37
1997-1998	5.82	1.53	3.04
1998-1999	6.47	2.03	3.82
1999-2000	5.36	0.74	3.46
2000-2001	5.65	0.93	4.05
2001-2002	6.19	1.47	4.40
2002-2003	5.91	1.11	4.40
2003-2004	4.48	-0.03	3.57
2004-2005	3.99	-0.04	2.49
2005-2006	4.08	0.38	2.57
2006-2007	3.45	-0.19	1.94
2007-2008	2.69	-0.93	1.11
2008-2009	6.14	2.51	4.53
2009-2010	6.85	3.00	4.83

Source: Budget documents of the State Governments

It is useful to start recounting the centre finance crisis by analysing the Central Government's deficit patterns over the period 1990-1991-2016-2017. In Table 1 concerning the status of the centre's fiscal deficit as a percentage of GDP, in 1991-1992 it was 5.5 percent, which in 1999-1999 further rose to 6.47 percent of GDP. After that it showed a decreasing trend due to some fiscal steps taken by the government and declined to 3.99 percent in 2004-05 and then began to raise 6.85 percent of GDP in 2009-10(B.E) (Table 2).

If we see the position of revenue deficit in 1991-1992 was 2.48 percent of GDP, which increased to 3.82 percent in 1998-1999 and then increased to 4.40 percent of GDP in 2002-2003, and then amounted to 4.83 percent of GDP in 2009-2010. The primary deficit in 1991-1992 was 1.49 percent of GDP, decreased further to –0.03 percent of GDP in 2003-2004, but increased further to 2.5 percent of GDP in 2008-2009 and then to 3 percent in 2009-2010. In summary, it may be noted that in the coming years the Central Government witnessed a noticeable reduction in the deficit indicators due to strict steps taken by the government but now due to relaxation attitude and financial crisis it has begun to increase.

As the year 2008-2009 progressed, the Indian economy was severely affected by the twin global shocks – unprecedented rise in global commodity prices in the first half of the year and the ripple effects of the global financial crisis escalating in the second half. This has resulted in a deliberate fiscal expansion, made up of both tax cuts and higher spending.

Owing to the farm loan waiver, the introduction of the Sixth Pay Commission award, and funding for the projects prioritised in

Table 3: Measures of deficit of state governments of India (1990-1991 to 2016-2017)

Year	Gross Fiscal Deficit	Gross Primary Deficit	Revenue Deficit
1991-1992	18,900	7956	5651
1992-1993	20,892	7681	5114
1993-1994	20,364	4564	3872
1994-1995	27,308	7895	6706
1995-1996	30,870	9031	8620
1996-1997	36,561	11,175	16,878
1997-1998	43,474	13,675	17,492
1998-1999	73,295	37,854	44,462
1999-2000	90,098	45,458	54,549
2000-2001	87,922	36,937	55,316
2001-2002	94,261	32,665	60,398
2002-2003	99,727	30,699	57,179
2003-2004	120,631	40,235	63,407
2004-2005	107,774	21,353	39,158
2005-2006	90,084	6060	7013
2006-2007	77,509	–15,672	–24,857
2007-2008	75,455	–24,376	–42,943
2008-2009	146,349	40,128	–10,701
2009-2010	199.510	760.1	322.95
2010-2011	1614.6	366.4	–30.5
2011-2012	1683.19	315.4	–239.6
2012-2013	2478.5	450.0	–203.2
2013-2014	3271.9	789.5	105.6
2014-2015	3333,3	1367.8	457
2015-2016	49336	1141.8	–537.2
2016-2017	4495.2	1952.8	–208.5

Source: Budget documents of the State Governments

the Eleventh Five Year Plan, the slippage in the terminal year fiscal goals has also been accentuated by the Supplementary Grant Demands. Also due to the issue of oil, fertiliser and food bonds, there was a marked increase in liabilities even after further accommodation of fertiliser subsidies as above the line expenditure in 2008-2009.

From Table 1 we see that deficits are still there and improvement in fiscal balance in the recent years should be undertaken fastly. The trend in major deficit measures as illustrated in Table 2 shows substantial improvement in recent years following the history of rapid deterioration from the second half of the 1990's.

As the effects of the recession continued through 2009-2010, the 2009-2010 Budget maintained its expansionary fiscal stance. Given the relative levels of private final consumption expenditure and government consumption expenditure shares, such expansion could only be a short-term step and introduced in the Medium Term Fiscal Policy Statement along with the 2009-2010 Budget.

The fiscal deficit target of 3.3 per cent of GDP for 2018-2019, to meet higher spending demand compared to the previous 3% target. The more troubling factor, however, is that the government's revenue deficit shot up to 2.6 per cent of GDP in 2017-2018 from the budget estimate of 1.9 per cent of GDP, indicating signs of fiscal consolidation worsening efficiency. This is also attributed to a rise in revenue expenditure of Rs1.1 trillion during the year.

Table 4: Key deficit indicators of the State Government (As Percentage to GDP),1990-1991-2016-2017

Year	Gross fiscal defict	Gross primary deficit	Revenue deficit
1990-1991	3.3	1.8	0.9
1991-1992	2.9	1.2	0.9
1992-1993	2.8	1	0.7
1993-1994	2.4	0.6	0.4
1994-1995	2.7	0.8	0.6
1995-1996	2.6	0.8	0.7
1996-1997	2.7	0.9	1.2
1997-1998	2.9	0.9	1.1
1998-1999	4.3	2.2	2.5
1999-2000	4.7	2.4	2.8
2000-2001	4.1	0.2	2.7
2001-2002	4.2	1.5	2.6
2002-2003	4.1	1.3	2.2
2003-2004	4.4	1.5	2.3
2004-2005	3.3	0.7	1.2
2005-2006	2.4	0.2	0.2
2006-2007	1.8	–0.8	–0.8
2007-2008	1.5	-0.5	-0.9
2008-2009	2.0	0.1	-0.5
2009-2010	2.9	1.2	0.5
2010-2011	2.1	0.5	-
2011-2012	1.9	0.4	-0.3
2012-2013	2.0	0.5	-0.2
2013-2014	2.2	0.7	0.1
2014-2015	2.6	1.1	0.4
2015-2016	3.6	0.8	-0.4
2016-2017	3.0	1.3	-0.1

Source: Budget documents of the State Governments

5. FINANCES OF THE STATES

If we look at the larger picture, it's about half of India's fiscal deficit aggregates that the state governments account for. Tables 3 and 4 represent the deficit between 1990-1991 and 20016-17 of the Indian State governments. Table 3 indicates the Rs Crore state deficits and Table 4 explains the deficits as a percentage of GDP. Complete structural deficit, main deficit, and revenue deficits are key state budget indicators. The total fiscal deficit of the state government in 1991-1992 was Rs 18900 crores (3.3% of GDP), which rose to Rs 30,870 in 1995-1996 and Rs 87,922 crores in 2000-2001. It grew further to Rs 107,774 crores in 2004-2005 and then to Rs 199,510 in 2009-2010. It further accelerated to Rs 4495.2 crores in 2016-2017.

Given that we see GFD as a percentage of GDP, it was around 3.3 percent in 1991-1992 and rised to a high level of 4.7 percent in 1999-2000 and then declined to 1.8 percent in 2006-2007, but then rose to 2.9 percent in 2009-2010 and still stands at 3 percent in 2016-2017. State fiscal deficit grew from 3.2 percent of GDP to 4.7 percent between 1990-1991 and 1999-2000.This rise in the fiscal deficit reflects a 2.8 per cent improvement in the 1999-2000 budget deficit. The close position of wealth and the manipulation of capital investment by raising the burden of interest payments and wages on the income statement are therefore obvious.

Social service expenditure during years 1998 and 1999 is largely attributable to an increase in the wage bill as a result of rising wages due to salary increases and does not represent any dramatic

Table 5: Combined deficits of central and state governments (Rs Billion)

Year	Gross fiscal deficit	Gross primary deficit	Revenue deficit
1991-1992	458.5	148.58	219.12
1992-1993	524.04	159.36	236.88
1993-1994	709.52	279.38	365.29
1994-1995	716.39	193.13	371.85
1995-1996	776.71	185.98	379.32
1996-1997	872.44	171.56	487.68
1997-1998	1107.43	324.66	627.82
1998-1999	1570.53	639.56	1106.18
1999-2000	1848.26	743.75	1213.93
2000-2001	1998.52	750.35	1388.03
2001-2002	2264.25	840.39	1593.5
2002-2003	2349.87	759.27	1629.9
2003-2004	2345.01	569.28	1594.08
2004-2005	2347.21	424.09	1147.61
2005-2006	2395.6	355.83	993.12
2006-2007	2191.28	–117.03	553.66
2007-2008	1991.1	–596.75	96.26
2008-2009	4671.35	1836.81	2408.65
2009-2010	6046.68	2900.98	3700.15
2010-2011	5340.32	1854.71	2492
2011-2012	6849.66	2849.63	3703.88
2012-2013	6843.95	2300.9	3439.6
2013-2014	7497.11	2154.8	3676.11
2014-2015	8365.63	2520.2	4112.24
2015-2016	10245.93	3724.39	3726.96
2016-2017	9799.45	2407.71	3331.67

Source: Budget documents of the Government of India and the State Governments

improvement in social service provision. States' Gross Fiscal Deficit (GFD) is mainly the product of bilateral agreements between states and the Permissible Net Borrowing Centre, i.e. the GFD is a vector of exogenously defined instruments.

If we see the revenue deficit of the states rose as a proportion of GDP from Rs 5651 crores in 1991-1992 to Rs 55316 crores in 2000-2001. The proportion declined to 2.2 per cent and of GDP in each of the two years 2002-2003 and 2005-2006. The tax deficit, which was 0.9 per cent of GDP in 1991-1992, then increased to 2.5 per cent in 1998-1999 to 2.7 per cent in 2000-2001, fell to 0.5 per cent in 2009-2010 and currently to 0.1 per cent in 2016-2017 as a proportion of GDP.

It can be seen that in 1991-1992 the state primary deficit was Rs 7956 crores, which rose to Rs 13,675 crores in 1997-98 and then further rose to Rs45,458 crores in 1999-00, then declined to -Rs 24,376 crores in 2007-2008. After 2008-2009, it again began to grow. As a percentage of GDP, the primary deficit in 1991-1992 was 1.8 percent, which in 1999-2000 rose to 2.4 percent and then fell to –0.5 percent in 2007-2008. The latest primary deficit projection in 2016-2017 was 1.3 per cent (Table 4).

The states' combined budgets which had shown a very intractable negative function. Earlier in 2005-2006, a dramatic turnaround was observed, with a fiscal deficit rule sum expected three years later far below the 3.0 percent of GDP goal. Three main factors that led to this included the Twelfth Finance Commission's granting of grants and the debt reduction and waiver incentive scheme linked to fiscal consolidation under fiscal law, the revenue buoyancy of the Center, and the introduction of state-level VAT, which has proven to be a highly buoyant source for governments.

6. CONSOLIDATED GENERAL GOVERNMENT

It is possible to examine the full picture of public finances and their effect on the macroeconomy through the deficit rate in the integrated General Government. From Table 5 we can see that in 1990-91 the combined fiscal deficits of central and state governments amounted to 7 % of GDP, which increased to 10% of GDP in 2000-01. With reform initiatives and budget control, it decreased to 5.57% in 2008-2009. In 1991-1992, the budget deficit was 3.3 per cent, rising to 6.9 per cent in 2001-2002. The overall expansion to improve production, fiscal and revenue deficits for 2009-2010 (BE) is set at 9.7% and 5.2% of GDP.

As the Indian economy expanded at a rapid rate of 8 percent in the mid-2000s, state government finances were way ahead of the Center in fiscal management terms. Many states have registered a surplus in revenues. The Center's combined fiscal deficit as well as state governments stood at 6 percent. The general government fiscal deficit fell to 8 percent levels in 2008-2009 and 2009-2010. The central and state governments' combined deficit reached 7 percent in 2015-2016. The number reached the 8 per cent mark in 2009 and 2010. At the combined level, the general government deficit for FY16 was 7.1 per cent, higher than the tolerance level of 6 per cent. Main reason for this is a fall in States' own tax revenues and lower net transfers from the government did the damage for the States in 2015-2016.

7. CONCLUSION

As the effort was only to establish an illusion of fiscal reform, fiscal consolidation remained an elusive task. It created the illusion of progress by stressing an insufficient measure of fiscal balance. While adequate steps have not been taken in reducing the fiscal deficit. Instead of achieving fiscal adjustment, the effort in successive budgets has been to create the illusion that fiscal changes are being accomplished rather than actually being accomplished.

The government has hidden deterioration of the fiscal balance by stressing the fiscal deficit rather than more concrete summary indicators, and also changing its concept and calculation system. Analysis shows that the decline in the fiscal deficit was comparably negligible. On the opposite, other fiscal policies have been showing considerable deterioration. And the claims around tax-adjustment are illusory.

The Center walks the road of fiscal prudence cautiously, but government finances are sliding. Much of the debates in India's public finances revolve around the finances of the Center and its fiscal status, but how does the picture look when we take an aggregate figure after comparing the Center's numbers with all the States? This is not very good if we have the combined picture.

After the introduction of the Fiscal Responsibility and Budget Management Act (FRBM) in India, state governments have been predominantly prudent spenders, reducing their expenditures much more efficiently than the Union government. This pattern appears to be reversing in recent years, with states' aggregate fiscal deficit increasing at a time when the Union government's aggregate fiscal deficit was decreasing.

State finances are expected to deteriorate much more in the future. There are two key reasons why the fiscal deficit is getting bigger. One is implementing the recommendations of the Seventh Pay Commission, and the second is the consequence of "UDAY" (Ujwal DISCOM Assurance Yojana). With a workforce of 12 million, the seventh Pay Commission recommendations are projected to have a significant impact on India's state finances as against 8 million Central Government employees. The Seventh Pay Commission, according to the RBI, will have an effect of 0.9 per cent of GDP on the general government's revenue and fiscal deficit (over a 3-4-year period).

The sharp decline in state finances over the past few years is partly due to the restructuring of state-run power utilities under the Yojana (UDAY) Ujwal Discom Assurance scheme. The that concerns about the increasing state deficits are expressed in the widening gap between government development loans (SDLs) and central government bonds. As market borrowings from state governments have risen much faster than borrowings from Centre in recent years. Second, the power revival package known as UDAY (Ujwal DISCOM Guarantee Yojana), where states take over 75 per cent of

their power distribution companies' outstanding debt in a phased manner, is expected to raise interest payments;

Over the last year substantial changes have been implemented. GST is one of India's most important autonomous fiscal reforms. The Goods and Services Tax Transition (GST) started at midnight stroke on July 1, 2017. On the other hand, though higher tax devolution recommended by fourteen finance commissions from 32% to 42% resulted in higher income transfers from the Centre. The coming years will say the effect of these reforms on Center and State Finance The health of Indian public finances will depend to a large extent on the fiscal rectitude of state governments.

In view of the cyclical position and the structural challenges facing the Indian economy at this stage, we suggest that policies focus on managing domestic demand slowdown and boosting productivity growth and promoting job creation in the medium term should set a number of main priorities. 'Politically, the time — is right for a drive for structural change.' India needs to keep public finances reasonably stable to stave off a potential second wave of financial-sector risks once the coronavirus crisis ends.

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