This chapter explains fiscal developments in India during the year 2019-20. MTFP Statement presented with the Budget 2019-20, pegged the fiscal deficit target for 2019-20 at 3.3 per cent of GDP as against 3.4 per cent of GDP in 2018-19 Provisional Actuals (PA)

**Fiscal Developments: Centre**

***Revenues Trends in Receipts***

Central government receipts can broadly be divided into Non-debt and debt receipts. The Budget 2019-20 targeted a high growth in Non-debt receipts of the Central Government, which was driven by high expected growth in Net Tax revenue and Non-Tax revenue.

***Tax Revenue***

Budget 2019-20 estimated the Gross Tax Revenue (GTR) to be 11.7 per cent of GDP. This is an improvement of 18.3 per cent over 2018-19 PA. The direct taxes, comprising mainly of corporate and personal income tax, constitute around 54 per cent of GTR. The receipts from corporate and personal income tax have improved over the last few years. Better tax administration, widening of TDS carried over the years, anti-tax evasion measures and increase in effective tax payers base have contributed to direct tax buoyancy. Widening of tax base due to increase in the number of indirect tax filers in the GST regime has also led to improved tax buoyancy.

*Non-Tax Revenue*

 Non-Tax revenue comprises mainly of interest receipts on loans to States and external grants. The Budget 2019-20 aimed to raise Non-Tax revenue amounting to 1.5 per cent of the GDP, 0.3 percentage points more than that in 2018-19 PA. Most of it came from dividends and profits especially surplus transferred by RBI.

***Non-debt Capital receipts***

Non-debt Capital receipts mainly consist of recovery of loans and advances, and disinvestment receipts. Over the last few years, the contribution of *Non-debt Capital receipts* have improved in the total pool of Non-debt receipts. They have been estimated to around 0.6 per cent of GDP, in 2019-20 BE owing to an envisaged growth on account of disinvestment receipts that accrue to the government on sale of public sector enterprises owned by the government (including sale of strategic assets). Given the significant pipeline of deals that are in process, realizations are likely to accelerate.

**Trends in Expenditure**

It is imperative for any developing economy to optimally allocate the available resources without compromising on the crucial developmental and macroeconomic goals. As India’s tax to GDP ratio is low, Government faces the challenge of providing sufficient funds for investment and infrastructure expansion while staying within the bounds of fiscal prudence. Therefore, improving the composition and quality of expenditure becomes significant.

The composition of government expenditure in the last few years reveals that expenditure on defence services, salaries, pensions, interest payments and major subsidies account for more than 60 per cent of total expenditure. Several initiatives have been undertaken by the Ministry of Defence to improve efficiency and utilization of defence expenditure, promote self-reliance, and encourage private sector participation in the defence sector.

Budgetary expenditure on subsidies has seen significant moderation through improved targeting. There is still headroom available for further rationalization of subsidies especially food subsidy. The expenditure on major subsidies, which is a significant component of non-committed revenue expenditure was pegged at 1.4 per cent of GDP in 2019-20 BE. The budgetary expenditure on major subsidies including food, fertilizer and petroleum subsidies has shown a declining trend over the past years.

Also there here has been considerable restructuring and reclassification of Central sector and Centrally Sponsored Schemes in the recent years. Expenditures on salaries, pensions and interest payments are committed in nature and therefore have limited headroom for creation of additional fiscal space.

The quality of expenditure is captured by the share of capital expenditure in total expenditure. In the current scenario share of capital expenditure in total expenditure is envisaged to decline roughly by a percentage point in 2019-20 BE over 2018-19 PA. However, capital spending in 2019-20 BE is estimated to grow by 10 per cent over that of 2018-19.

Major sectors apart from defence services that account for bulk of capital expenditure allocation include internal security, investments in Financial Institutions, assistance for metro projects, space technology and construction of Roads and Railways.

Apart from budgetary spending, Extra Budgetary Resources (EBR) have also been mobilized to finance infrastructure investment since 2016-17. EBRs are those financial liabilities that are raised by public sector undertakings for which repayment of entire principal and interest is done from the Central Government Budget. Government proposes to raise EBR to the tune of 0.27 per cent of GDP. These EBRs are not taken into account while calculating the Fiscal Deficit. However, they are considered in the calculations of Government Debt.

**Transfer to States**

The Fourteenth Finance Commission (FFC) for the award period 2015-20 had made far-reaching changes to strengthen fiscal federalism in the country. Consequently, States have obtained larger fund transfers as well as greater autonomy to utilise funds as per their needs. Transfer of funds to States comprises essentially of three components: *share of States in Central taxes devolved to the States, Finance Commission Grants, and Centrally Sponsored Schemes (CSS), and other transfers.* Till 2013-14, funds for CSS were routed through two channels, the Consolidated Funds of the States and directly to the State implementing agencies. **In 2014- 15, direct transfers to State implementing agencies were discontinued and all transfers to States including for the CSS were routed through the Consolidated Funds of the States.**

The Budget 2019-20 envisages an increase in expected grants and loan to States on account of higher requirements under compensation to States for revenue losses on roll out of GST, grants to rural and urban bodies and releases under Samagra Shiksha.

**Fiscal outcome in 2019-20 (up to November 2019) vis-à-vis 2019-20 BE**

Indian economy registered a sluggish growth during first half of 2019-20. A series of measures were introduced by the Government during the financial year to boost the economy, which are expected to have a substantial direct and indirect impact on the fiscal performance of the economy.

Revenue receipts have grown at a much higher pace during the current financial over the corresponding period last year. Considerable growth in Non-Tax revenue, especially dividends and profits, which offset the low growth in Net Tax revenue, underlie it. Dividends and profits led by transfer from RBI grew at roughly three times over the same period last year.

Centre’s tax collection is likely to fall short of its estimate by 1.2 per cent of GDP in 2019-20.This is primarily owing to low growth in GTR as compared to the previous financial year. Within direct taxes, personal income tax has grown at 7 per cent while corporate tax has registered a negative growth during 2019-20. This compares poorly with growth recorded by these taxes over the last year. The indirect tax receipts have registered a negative growth in the first eight months of this fiscal year. Gross GST collections, Centre and States taken together registered an increase of 3.7 per cent over the last year.

Notably, so far, during 2019-20, despite the rationalisation of GST rates, the gross GST monthly collections has crossed the mark of ` one lakh crore, for a total of five times. The increase in GST collections may be a result of concerted efforts taken by the government to improve tax compliance and Tax revenue collection. These include extensive automation of business processes, application of e-way bill mechanism, targeted action on compliance verification, enforcement based on risk assessment and proposed introduction of electronic invoice system. Amongst the reforms undertaken for increasing GST compliance, the GSTN has taken several initiatives to incorporate behavioural parameters to induce voluntary compliance by taxpayers.

The Non-debt Capital receipts includes recovery of loans and disinvestment receipts. Government has targeted to mobilise `1.05 lakh crore from disinvestment proceeds. So far, it has been able to raise `0.18 lakh crore which is 17.2 per cent of 2019-20 BE.

On the expenditure side, the capital expenditure during 2019-20 has grown at roughly three times vis-à-vis the same period in 2018-19. Also revenue expenditure has grown at a higher rate in 2019-20, compared to the same period previous year.

Among the major subsidies, the growth in expenditure on Urea and Petroleum subsidies has been higher during this period as compared to 2018-19. Based on the above analysis there is an apprehension that the Tax revenue for the current fiscal year would be muted relative to the target envisaged in 2019-20 BE.

The gap due to lower tax receipts could be to some extent compensated by higher mobilisation of Non-Tax revenue and disinvestment proceeds for 2019-20. However, high growth in Non-Tax revenue may not be sustainable year after year. The realization from Non-Tax revenue and disinvestment being uncertain adds to the volatility in revenue projection.

 Thus in order to be on track with the fiscal path outlined by the Medium Term Fiscal Policy Statement, it would be imperative to rationalize expenditure. However, given the sluggish demand and decline in growth of private consumption expenditure reported in first half of the fiscal year, any cut in expenditure especially capital expenditure would have adverse implications for growth. Moreover, since a considerable proportion of revenue expenditure like interest payments, wages and salaries and pensions is committed in nature, this leaves a little fiscal headroom for manoeuvre. Therefore, the focus of the Government should lie on rationalization of non-committed revenue expenditure like subsidies. Further, to boost the domestic demand which is crucial for revival of growth, fiscal deficit target may have to be relaxed for the current year.

**Central Government Debt**

 Total liabilities of the Central Government include debt contracted against the Consolidated Fund of India, technically defined as Public Debt, as well as liabilities in the Public Account. These liabilities include1 external debt (end-of-the financial year) at current exchange rate but exclude part of NSSF liabilities to the extent of States’ borrowings from the NSSF and investments in public agencies out of the NSSF, which do not finance Central Government deficit. Total liabilities of the Central Government at end March 2019 stood at `84.7 lakh crore and 90 per cent of which was public debt.

Total liabilities of the Central Government, as a ratio of GDP, has been consistently declining, particularly after the enactment of the FRBM Act, 2003. This is an outcome of both fiscal consolidation efforts as well as relatively high GDP growth.

Central Government debt is characterised by low currency and interest rate risks. This is owing to low share of external debt in the debt portfolio and almost entire external borrowings being from official sources. Further, most of the public debt has been contracted at fixed interest rate making India’s debt stock virtually insulated from interest rate volatility. This lends certainty and stability to budget in terms of interest payments.

The other salient feature is the gradual elongation of the maturity profile of the Central Government’s debt leading to reduced rollover risks. The proportion of dated securities maturing in less than five years has seen consistent decline in recent years. The weighted average maturity of outstanding stock of dated securities of the Government of India has increased from 9.7 years at end March 2010 to 10.4 years at end March 2019.

**STATE FINANCES**

As per 2019-20 budget estimates of the State Governments, the States’ combined own Tax revenue and own Non-Tax revenue is anticipated to grow at 11.1 per cent and 9.9 per cent respectively, which is low relative to the robust growth displayed in the previous year. The envisaged growth of 8.4 per cent in total expenditure in 2019-20 w.r.t. 2018- 19 is largely led by growth in revenue expenditure, whereas the capital expenditure is placed to grow at a lower rate.

The rising trend in revenue expenditure is driven by rise in committed expenditure including pension and interest. In fact, the RBI Study on State Finances attributes the fiscal consolidation of the States in the last four to five years to the ***steep decline in expenditure, mainly capital, which may have adverse implications for the pace and quality of economic development****.*

The States have thus continued on the path of fiscal consolidation and contained the fiscal deficit within the targets set out by the FRBM Act. For the year 2019-20, the States have budgeted for gross fiscal deficit of 2.6 per cent of GDP as against an estimate of 2.9 per cent in 2018-19 RE and 2.4 per cent in 2017-18. The financing pattern of Gross Fiscal Deficit for States has also changed over the years. Financing via market borrowings has increased from 61.6 per cent in 2015-16 to 73.7 per cent in 2018- 19 RE and is further expected to rise to 87.9 per cent in 2019-20 BE.

On the other hand, the debt to GDP ratio for States has risen since 2014-15 owing to the issuance of UDAY bonds in 2015-16 and 2016-17, farm loan waivers, and the implementation of Pay Commission awards. The Debt to GDP for States is likely to remain around 25 per cent of GDP in 2019-20, clearly making the sustainability of debt the main medium term fiscal challenge for State.