WHITE PAPER

ON

FINANCIAL AND ECONOMIC CONDITION

OF MADHYA PRADESH

DEPARTMENT OF FINANCE
GOVERNMENT OF MADHYA PRADESH
BHOPAL
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Introduction

After the Assembly elections, a new government has taken over the reigns of administration of the State. It has promised people a White Paper on the state of finances. The Financial position of a State would determine the pace of the development and level of the development the government could achieve. Thus, a White Paper provides an opportunity to assess the fiscal position and also enables people to access the knowledge about the finances of the State. The White Paper would help in understanding the efforts of the government in raising resources for the development purposes.

The White Paper is divided mainly into three chapters. The first chapter delineates the economic structure of the State, in terms of its composition, rate of growth and level of the development. The second chapter portrays the financial position in terms of its source of revenue, its composition, the usage of revenue, borrowings and debt position. The third chapter describes emerging contours of the fiscal policy.

The analysis covers a period of eleven years between 1993-94 to 2003-2004. For the purpose of analysis of the macroeconomic key indicators, a new series was started in 1993 94 and is continuing till date and hence this White Paper presents data from 1993-94. The composite State of Madhya Pradesh has been bifurcated into Madhya Pradesh and Chhattisgarh and the present State of Madhya Pradesh was formed on 1st of November 2000. This creates problems of comparison of absolute quantities of any parameter before and after bifurcation of the State. Enough care is taken not to compare the incomparable, while drawing the conclusion.

The White Paper also poses the bifurcated data in bold relief for a comparative analysis along with the absolute data of erstwhile Madhya Pradesh. The adjusted data has been depicted in **blue colour** just below the absolute data of erstwhile Madhya Pradesh. The data has been adjusted in the population proportion (Madhya Pradesh: Chattisgarh 485.7: 176.2). Thus the present Madhya Pradesh constitutes approximately 73.3797% of the erstwhile Madhya Pradesh. .

The main sources of data set in the White Paper are the budget documents of the Government of Madhya Pradesh, Finance Accounts, Plan Document of the Planning Commission of India, Reserve Bank of India data etc. The data for 2003 - 04 is assumed data and may marginally differ from the final account. The budget documents too can differ marginally from the Finance Accounts of that year since the Finance Accounts are later adjusted by the Accountant General. For the purpose of maintaining transparency in data each table shows its sources.

Chapter 1
Economy of the State

1.1 Sectoral Composition

1.1.1 The fiscal position of the government and the economy are closely related while the contribution of finances of the state is a sub-set of the economy. The level of the development of the economy primarily determines the size of the budget. The more developed the state, the greater would be the tax base and the higher the tax revenues in the government treasury. This would enable the Government to invest more in physical and social infrastructure, which would accelerate the growth of the economy. Appropriate economic policies would rejuvenate the growth process.

1.1.2 To study and analyse the structure of the economy, it is divided into three sectors. They are primary, secondary and tertiary or service sectors. The primary constitutes of agriculture and allied activities, mining and forestry. The secondary sector consists of manufacturing (formal and informal), electricity, gas, water supply, construction, and the tertiary sector consists of all types of services including transport and communications. In the initial stages of development, the primary sector dominates the economy. As the economy progresses the secondary sector overtakes the primary sector and necessitates the growth of service sector. Since the taxes of the State are borne out of secondary sector, any increase or decrease has its own bearing on the financial situation of the State and yet they are not be sole factor for it since the rate of taxes are equally important.

Table 1.1

Sectoral Composition of Economy

(in %)

Sectors	1993-94		2002-03	
	Madhya Pradesh	All India	Madhya Pradesh	All India
Primary	45.70	33.54	30.74	23.30
Secondary	18.60	23.69	25.99	21.90
Tertiary	35.70	42.77	43.27	54.80
	100.00	**100.00**	**100.00**	**100.00**

Source: Central Stastical Organization, Govt. of India / Directorate of Economic & Statistics, Madhya Pradesh.

1.1.3 Table 1.1 compares the new State of Madhya Pradesh with that of all India the economic structure as depicted in the percentage share of different sectors in the Gross domestic Product at constant prices (1993-94 prices). As seen from the table, during 1993-94 the economy of MP was predominantly agrarian followed by service sector. By 2002-03, the proportion of primary sector in the GSDP has decreased by

14.96% points, the proportion of secondary sector has increased by 7.39% points and that of the service sector increased by 7.57% points.

1.2 Development of Economy

1.2.1 The growth of the economy has a positive effect on the revenue collections. The relationship between the growth of economy and revenue collections is called revenue buoyancy. If the revenue buoyancy were 1.2 then a 5% rate of growth of the GSDP would ensure a six percent (1.2 * 5) rate of growth of revenue. The growth of the economy is generally shown by Net State Domestic Product (NSDP) at constant prices. The growth of value of output has two components: the growth of output and the increase in price of the output. In order to isolate the price component of growth constant prices are used. The annual growth rates of Net State Domestic Product (NSDP) at constant prices (1993-94 prices) of MP and Net National Product (NNP) at constant prices (1993-94 prices) of India are presented in the table1.2.

Table 1.2
Net Domestic Product (93-94 Constant Prices)

(Rs. in Crores)

Year	Bifurcated MP	Annual Growth Rate	All India	Annual Growth Rate
1993-94	33937	------	697992	------
1994-95	34529	1.74	747573	7.10
1995-96	36601	6.00	800411	7.07
1996-97	39057	6.71	862808	7.80
1997-98	41101	5.23	901734	4.51
1998-99	43815	6.60	960555	6.52
1999-2000	48415	10.50	1019298	6.12
2000-01	42773	-11.65	1062492	4.24
2001-02 (P)	47037	9.97	1125286	5.91
2002-03 (Q)	43923	-6.62	1168224	3.82

Source: Central Stastical Organization, Govt. of India / Directorate of Economic & Statistics, Madhya Pradesh.
(P) Provisional estimates (Q) Quick estimates.

1.2.2 The growth of the economy of MP during 1993-94 to 2002-03 has been less than that of India. During this period the MP was growing at average annual growth rate 3.69 % and the Indian economy was growing at 6.57 %. The economy of MP suffered a set back in 2000-01 due to severe drought. The Ten Five-Year Plan of MP has projected an annual growth of 7% per annum. In order to achieve the targeted growth rate of the plan, huge investments both in public and private sector are required.

1.3 Levels of Poverty

1.3.1 The per capita income is another indicator that reflects the level of development of the State. The per capita income is also affected by the increase in population along with the rate of growth in economic development. The rate of growth of population in Madhya Pradesh has been much higher as compared to other states while the growth of the per capita income lower in MP compared to most of other States. Not only the growth rate of domestic economy of MP lower than other States but the Per capita income is also much lower.

Table 1.3
Per Capita Income of States at constant (1993-94) prices
(in Rupees)

State	*1993-94*	*2001-02 (Q)*	*Annual Average Compound Growth Rate*
West Bengal	6756	10376	5.51
Karnataka	7838	11936	5.4
Tamil Nadu	8943	13055	4.84
Gujarat	9796	14102	4.66
All-India	7690	10754	4.28
Andhra Pradesh	7447	10313	4.15
Rajashthan	6182	8536	4.12
Kerala	7938	10832	3.96
Haryana	11079	14075	3.04
Orissa	4896	6105	2.8
Maharashtra	12183	15070	2.69
Punjab	12710	15255	2.31
Chattissgarh	6539	7647	1.98
Madhya Pradesh	6584	7635	1.87
Bihar	3037	3399	1.42

Source: Economic Survey of India. (various years)

1.3.2 The growth of the NSDP and per capita income has an impact on the poverty levels in the State. There is enough empirical evidence to show that high growth rate of the economy would bring down the poverty levels sharply. The slow growth of the MP economy had an adverse affect on the reduction of the poverty levels. In the year 1999-00, more than one third of the population (37.43%) in the State lives below the poverty line. The level of poverty of MP is not only above the national average of 26.1 %, but also just below only to Orissa and Bihar. The percentage of population living below poverty line is only 31% in the Uttar Pradesh while the same in Rajasthan is 15%. During the period 1993-94 to 2000-01, the poverty reduction in MP was only 5.09 percentage points whereas at the all India level the reduction was 9.87 percentage points. The rural poverty, during this period, was reduced by only 3.58 percentage points, while in urban areas the poverty was reduced by 9.94 percentage points. Rajasthan (12 percent) and Uttar Pradesh (10%) that too form part of BIMARU states, have left Madhya Pradesh behind in poverty elimination.

Table 1.4
Percentage of Population below Poverty Line

Sl. No.	State	1993-94			1999-2000		
		Rural	Urban	**Total**	Rural	Urban	**Total**
1	Andhra Pradesh	15.92	38.33	**22.19**	11.05	26.63	**15.77**
2	Assam	45.01	7.73	**40.86**	40.04	7.47	**36.09**
3	Bihar	58.21	34.5	**54.96**	44.3	32.91	**42.6**
4	Gujarat	22.81	27.03	**24.21**	13.17	15.59	**14.07**
5	Haryana	28.02	16.38	**25.05**	8.27	9.99	**8.74**
6	Karnataka	29.88	40.14	**33.16**	17.38	25.25	**20.04**
7	Kerala	25.76	24.55	**25.43**	9.38	20.27	**12.72**
8	Madhya Pradesh	40.64	48.38	**42.52**	37.06	38.44	**37.43**
9	Maharashtra	37.93	35.15	**36.86**	23.72	26.81	**25.02**
10	Orissa	49.72	41.64	**48.56**	48.01	42.83	**47.15**
11	Punjab	11.95	11.35	**11.77**	6.35	5.75	**6.16**
12	Rajasthan	26.46	30.49	**27.41**	13.74	19.85	**15.28**
13	Tami Nadu	32.48	39.77	**35.03**	20.55	22.11	**21.12**
14	Uttar pradesh	42.28	35.39	**40.85**	31.22	30.89	**31.15**
15	West Bengal	40.8	22.41	**35.66**	31.85	14.86	**27.02**
16	All India	37.27	32.36	**35.97**	27.09	23.62	**26.1**

Source: Plan Document : Planning Commission of India. (various years)

1.3.3 The economic condition and the human development index depicts a sorry state of picture of Madhya Pradesh that despite after 48 years of independence, the State remains in the category of the most backward states. (See Annexure I)

Chapter 2
Analysis of Fiscal Situation

2.0 The State Government has a constitutional obligation (Article 202) to present at the beginning of the every financial year, an annual financial to the Legislature for its approval. This annual financial statement is popularly known as the Budget of the Government. This statement contains all the receipts and expenditure, loans and advances, public account and transactions in contingency funds of the current year and the estimates for the coming year. The financial statement describes the result of the transactions in the consolidated fund and public account as per the Heads of Account laid down by the President on the aid and advise of the CAG under Article 150 of the Constitution. The transactions in consolidated fund comprise of state total revenue receipts and revenue expenditure on the revenue account and capital expenditure, public debt (both receipts and disbursements) and recoveries from loans and advances on the capital account. All other receipts and disbursements, which are not part of the consolidated fund, like employees provident fund, employees' insurance funds etc are shown in the public account. The budget estimates (BE) approved by the Assembly may undergo changes during year due to supplementary demand voted during the year and any other unforeseen transactions in the Contingency Fund. These changes both in the expenditure and receipts are laid before the House in the Revised Estimates (RE). The annual statement of income and expenditure of the government is prepared by the Comptroller and auditor General of India and is laid before the House in Vidhan Sabha

2.1 Receipts:

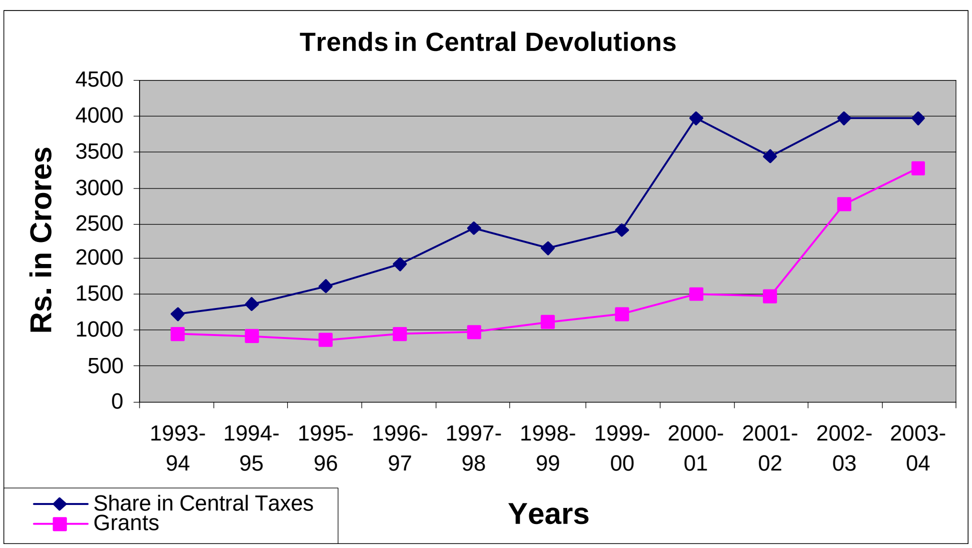
2.1.1 The revenue receipts are main component of the total receipts. This ratio was 81.94% in 1993-94 and has come down to 65.67% by 2003-04. This implies that the State has been increasingly dependent on debt rather than the revenues during this period since it is the only other source of receipts.

Table 2.1
Receipts of Government

Year	Revenue Receipts	Public Debt	Recovery loans	Consolidated Fund	Public Acc(Net)	Total	% Revenue Receipts of the Total
1993-94	7069.79	680.25	496.71	8246.75	381.42	8628.17	81.94
1993-94 **(Adj)**	5187.79	499.17	364.48	6051.44	279.88	6331.32	81.94
1997-98	11257.1	1740.13	794.08	13791.3	367.97	14159.3	79.5
1997-98 **(Adj)**	8260.43	1276.9	582.69	10120	270.01	10390.05	79.5
1999-00	13203.7	2912.77	313.8	16430.3	1062.86	17493.11	75.48
1999-00 **(Adj)**	9688.81	2137.38	230.26	12056.5	779.92	12836.39	75.48
2000-01	13667.1	2282.17	13.45	15962.7	438.92	16401.61	83.33
2001-02	11201	2759.32	1590.61	15550.9	1770.66	17321.57	64.66
2002-03	13390.4	3455.68	42.71	16888.8	155.4	17044.19	78.56
2003-04	14758.2	7799.69	71.53	22629.39	-146.25	22483.14	65.64

Source: Budget Documents – Government of MP (various years)
Note : (Adj) Data adjusted in Bifurcation ratio of MP : Chattisgarh

2.1.2 The revenue receipts comprise State own revenues and Central devolutions. The State own revenues are tax and non-tax revenues. The central devolutions are share in Central taxes as per the Finance Commission award, revenue component of State plan assistance as per modified Gadgil formula and Central plan transfers. The tax devolutions did increase sharply till 1996-97 and then were fluctuating. The Central plan grants were almost stagnant till 2000-01 (see graph).



2.1.3 It is observed from the table 2.2 that the share of State own resources has decreased from 57.72% in 1993-94 to 55.46% in the year 2003-04, while the share of Central taxes increased from 23.78% in 1992-93 to 28.81% in 2003-04. The share in Central taxes depends on the buoyancy of these taxes, given the Finance Commission award. The major contributing factor to this decrease is the non-tax revenues.

Table 2.2
Composition of Revenue Receipts (%)

Year / Item	State Own Revenue			Central share		
	Tax Revenue	Non-tax Revenue	Total	Share in Taxes	Grants	Total
1993-94	37.87	19.86	57.73	23.78	18.5	42.28
1994-95	37.68	21.2	58.88	24.62	16.5	41.12
1995-96	40.66	20.55	61.21	25.36	13.44	38.8
1996-97	40.98	19.72	60.7	26.32	12.98	39.3
1997-98	40.55	17.93	58.48	29.55	11.97	41.52
1998-99	45.03	15.71	60.74	25.84	13.43	39.27
1999-00	43.89	18.7	62.59	24.7	12.71	37.41
2000-01	47.32	12.62	59.94	28.94	11.12	40.06
2001-02	41.68	14.3	55.98	30.71	13.31	44.02
2002-03	46.22	12.21	58.43	27.66	13.9	41.56
2003-04	44.94	10.52	55.46	28.81	15.73	44.54

Source: Budget Documents – Government of MP (various years)

2.1.4 There is an adverse effect on the finances of the States by any decrease in the central tax devolution since it reduces the resources of the States suddenly, while at the same time their daily expenditure remains at the anticipated level and hence adversely affects the expenditure to devolution ratio.

Projections of the Eleventh Finance Commission and Central Devolutions

(Rs. In Crore)

Parameter/Year	2000-01	2001-02	2002-03	2003-04	2004-05
EFC projection	4840.53	4067.00	4742.63	5531.77	6453.90
Devolution	3955.51	3439.30	3981.36	4502.09	5272.25
Difference	885.02	627.70	761.27	1011.68	1181.65
Revenue Deficit	**1319.34**	**3167.8**	**1513.48**	**5243.67 (Expected)**	**3046.85**
Had the devolutions been as per the EFC projections, the RD would be much lesser and as below					
Revenue Deficit	434.32	2540.1	752.21	4231.99	1856.17

Deterioration in the Tax Devolution

The Central tax devolutions in the current quinquennium have been less than the projections made by the EFC and also less than its own Budget estimates. The Tenth Plan document has clearly brought out that the Central tax revenues as a proportion of GDP has come down. “Tax revenue (net) decreased by more than 1 percentage point from 6.85 per cent in the 1996-97 to 5.80 per cent in 2001-02” (Tenth Five-Year Plan. Vol. I p. 76). The States’ share of taxes in the 2002-03 BE were Rs.61235 crore and were reduced to Rs. 56141 crore in the RE. Similarly the assistance for Central and Centrally sponsored schemes has been reduced from Rs. 10105 crore in BE to Rs. 8918 crore in RE.

Source: Report of the Eleventh Finance Commission

2.1.5 The State tax revenues mainly comprise of sales tax, excise tax, stamps & duties, electricity duties, taxes on vehicles, taxes on goods and passengers, professional tax etc. Sales tax and excise tax 60 % of the State tax revenues. Sales tax has reached 50 % of the tax revenues in 2001-02 and then started a slide. The proportion of State excise in the taxes was 18.73 in 1993 - 94 and has been gradually declining.

Table 2.3
Composition of State Taxes

(in%)

DESCRIPTION	1993-94	1997-98	99-2000	2000-01	2001-02	2002-03	2003-04
Sales Tax	45.35	45.05	44.09	49.06	50.45	47.25	48.56
State Excise	18.73	18.52	18.52	17.29	15.06	14.48	16
Taxes on goods and passenger	8.14	6.98	7.39	5.92	5.61	5.71	6.25
Taxes and Duties on Electricity	10.69	10.48	10.55	7.94	5.73	13.03	8.82
Stamps & Registration	7.06	7.91	8.11	8.46	9.51	8.7	8.3
Taxes on Vehicles	7.85	8.14	6.94	7.2	8.41	6.97	7.51
Professional tax	0.09	1.69	3.1	2.97	3.7	3.14	3.34
Other Taxes	2.09	1.23	1.3	1.17	1.53	0.72	1.22
Total	100	100	100	100.01	100	100	100

Source: Budget Documents – Government of MP (various years)

2.1.6 The revenues from non-tax revenue are basically user charges for the services provided by the government. These are categorised into fiscal services, general services, social services and economic services. The fiscal services include interest and dividends, general services include police, general administration etc, the social serves include education, art, culture, health, water supply etc.,, and economic serves include crop and animal husbandry, forestry, fisheries, mining, irrigation, tourism etc,. The major revenue yielding components of the non-tax revenue are forestry and mining. As seen from the table 2.4, these two components contributed 71.5 % of the revenues from economic services in 1997-98 and dropped to 66.5 % in 2002-03. The policies of the GoI are responsible for this. There is also a need to take stock of the other user charges on the principles of ability to pay.

Table 2.4
Composition of Non-Tax Revenue

Descreption	1993-94	1997-98	99-2000	2000-01	20001-02	2002-03	2003-04
Interest Receipts, Dividends & Profits etc	15.44	11.14	10.49	10.73	15.5	2.21	7.16
General Services	5.98	6.64	8.59	10.71	14.39	13.82	15.91
Social Services	3.67	3.86	3.79	4.34	4.59	5.48	2.96
Economic Services of which	74.91	78.36	77.13	74.22	65.52	78.49	73.97
(I) Forestry & Wild Life	35.06	31	20.56	21.61	19.13	30.41	25.02
(ii) Non-ferrous Mining & Metallurgical Industries	33.85	40.47	35.15	41.82	32.99	36.12	41.16
Total Non-Tax Revenue	100	100	100	100	100	100	100

Source: Budget Documents – Government of MP (various years)

2.2 Expenditure:

2.2.1 The most fundamental classification of the expenditure is revenue and capital. There is a constitutional requirement (Article 202 (2) (b)) of Budget to be classified into revenue and capital. All the expenditure that goes into consumption and does not create any asset is called revenue expenditure and all the expenditure that creates assets is called capital expenditure.

2.2.2 As can be seen from the table 2.5 that government spends most of its receipts on consumption. The percentage of revenue and capital do not add up to 100 as a small proportion of total is given as loans and advances. In order to maintain the quality of expenditure and development of infrastructure, it is most necessary to contain the revenue expenditure to increase the capital expenditure.

Table 2.5
Composition Expenditure - Revenue & Capital

Year/Item	% Revenue Exp.	% Capital Exp.
1993-94	93.36	10.03
1994-95	86.43	9.67
1995-96	88.76	8.36
1996-97	95.99	8.55
1997-98	89.67	12.83
1998-99	91.89	6.53
1999-00	94.28	5.55
2000-01	91.5	6.78
2001-02	96.78	9.91
2002-03	83.42	14.03
2003-04	85.78	12.39

Source: Budget Documents – Government of MP (various years)

2.2.3 The composition of revenue expenditure is shown in the table 2.6. The salaries and pensions constitute the major component of the revenue expenditure. The other category is mainly comprised grants to various bodies including local bodies. As per Article 202 (3) (c) the interest payments on debt are charged expenditure (expenditure that need not be voted in the house). In a declining interest rate regime, appropriate change in the debt portfolio can bring down the interest payments.

2.2.4 From the national economy point of view, India has entered into a lower interest regime where there is a reduction in interest rates. Interest rates have been traveling south. It would be prudent for the government to pay of high cost debt by swapping it with low cost of borrowings. This would not only reduce the interest burden on the state, but would also reduce the average cost of borrowing for the government.

Table 2.6
Composition of Revenue Expenditure

(Rs. in Crores)

Year / Item	*Revenue Exp*	*Pay & Pensions*	*% of RE*	*Interest*	*% of RE*	*Others*	*% of RE*
1993/94	7517.93	3382.47	44.99	867.9	11.54	3267.56	43.46
1993/94	5516.63	2482.04	44.99	636.86	11.54	2397.73	43.46
1994/95	7808.77	3697.75	47.35	1094.3	14.01	3016.69	38.63
1994/95	5730.04	2713.39	47.35	803.01	14.01	2213.63	38.63
1995/96	9130.87	4347.82	47.62	1158.3	12.68	3624.8	39.7
1995/96	6700.2	3190.41	47.62	849.91	12.68	2659.66	39.7
1996/97	11462.06	4950.77	43.19	1376.2	12.01	5135.07	44.8
1996/97	8410.82	3632.8	43.19	1009.9	12.01	3768.09	44.8
1997/98	11726.44	5497.25	46.88	1659.9	14.16	4569.27	38.97
1997/98	8604.82	4033.86	46.88	1218	14.16	3352.91	38.97
1998/99	14217.65	7104.89	49.97	1834.8	12.9	5278.01	37.12
1998/99	10432.86	5213.54	49.97	1346.3	12.9	3872.98	37.12
1999/00	16135.94	7861.45	48.72	2138.7	13.25	6135.83	38.03
1999/00	11840.5	5768.7	48.72	1569.3	13.25	4502.45	38.03
2000/01	14986.41	6684.55	44.60	2410.8	16.09	5891.08	39.31
2001/02	14368.78	5678.49	39.52	2253.7	15.68	6436.62	44.8
2002/03	14556.8	6188.28	42.51	2492.4	17.12	5876.08	40.37
2003/04	19962.34	6816.03	34.14	3416.52	17.11	9729.79	48.74

Source: Budget Documents – Government of MP (various years)

2.2.5 One of the disturbing aspects of the revenue expenditure is grants. Grants include subsidies. The rationality of subsidies is to bring in economic and social equity. Some of these recipients are deserving and some of the not so deserving. In most of the cases, once a subsidy is given it continues ad infinitem since there is no review of the same and any reduction in subsidies call for agitation. There is a strong need to review these grants.

Table 2.7
Distribution of Grants (2001-02)

Department	***Rs. in crore***	***% to total***
Revenue	68.53	1.84
Energy	2025.44	54.35
Agriculture	121.21	3.25
Urban Administration	439.68	11.80
School Education	67.66	1.82
Panchayat	307.59	8.25
SC & ST welfare	97.49	2.62
social welfare	128.25	3.44
Higher education	69.37	1.86
Others	401.57	10.78
Total	3726.79	100.00

Source: Budget Documents – Government of MP (various years)

2.2.6 During the year 2001 – 2002 nearly 26% of the revenue expenditure was on these grants. As seen from the table 2.7, more than 50% of the grants were for the Energy department including subsidies for supplementing the power charges for the purpose of Agricultural pumps, single point connection. The financial condition of the State and also MP SEB is being adversely affected by such heavy subsidy.

2.2.7 Assigning grants to the local bodies so as to supplement the resources for developmental purposes is also a constitutional requirement. A decentralised democratic form of local bodies government is as important as is to provide them with financial resources in order to meet of their social liabilities

2.2.8 Another dimension of expenditure composition is plan and non-plan. Nearly two-third of expenditure goes into the non-plan expenditure. All most all of capital expenditure takes place in plan.

Table 2.8
Composition Expenditure-Plan & Non-Plan

Year / Head	Plan	Non Plan	Total
1993-94	31.38	68.62	100
1994-95	32.8	67.2	100
1995-96	31.51	68.49	100
1996-97	29.17	70.83	100
1997-98	31.51	68.49	100
1998-99	24.15	75.85	100
1999-00	22.92	77.08	100
2000-01	24.8	75.2	100
2001-02	26.23	73.77	100
2002-03	36.77	63.23	100
2003-04	27.19	72.81	100

Source: Budget Documents – Government of MP (various years)

2.2.9 However all non-plan expenditure is not unproductive. Generally the social sectors like education and health, which are necessary to increase the human capital, have large non-plan budgets. Wherever there is a greater demand for investment from the government sector, there is a higher budgetary allocation in the non plan. This essentially has to be earmarked as the development expenditure. In the state of Madhya Pradesh, the school education is mostly fed and paid by the state government. Thus the development expenditure in MP is much higher in relation to other States, but this has adversely affected the capital investment in infrastructure. Table 2.9 shows the level of development and not development expenditure in various States

Table 2.9
Composition of Development and Non-Development Expenditure – Major States

States	% of Development Expenditure		% Non-Development Expenditure	
	00-01	**01-02 (RE)**	**00-01**	**01-02(RE)**
Andhra Pradesh	68.03	67.55	31.97	32.45
Bihar	61.77	55.37	38.23	44.63
Chhattisgarh	71.78	68.41	28.22	31.59
Gujarat	75.83	73.97	24.17	26.03
Haryana	64.1	64.55	35.9	35.45
Karnataka	69.43	67.85	30.57	32.15
Kerala	56.49	57.23	43.51	42.77
Madhya Pradesh	66.28	69.57	33.72	30.43
Maharashtra	66.93	58.25	33.07	41.75
Orissa	59.69	53.52	40.31	46.48
Punjab	50.48	49.45	49.52	50.55
Rajasthan	60.71	59.77	39.29	40.23
Tamil Nadu	62.43	61.54	37.57	38.46
Uttar Pradesh	55.27	56.98	44.73	43.02
West Bengal	61.45	58.99	38.55	41.01
All States	63.91	62.2	36.09	37.8

Source: State Finances: A Study of Budgets, Reserve Bank of India (various years)

2.3 Financial Management

2.3.1 The Annual Financial Statement, besides budget estimates of the coming financial year, provides previous year's actual, budget estimates of the current year and revised estimates (RE) of the current year. Some States present their Budgets before Central budget while others thereafter. If the state budget is presented after the central budget, it can incorporate the information on central assistance. As opposed to which, presenting a budget by the state in the end of the financial year prevents new words being taken up at the field level as the appropriation accounts are finalised only at the year-end

2.3.2 The state of Madhya Pradesh traditionally presents its budget before the Centre does. In such a situation, one does not know the likely Central transfers and thus they are kept at the previous year's level. This necessitates supplementary demands for Central schemes. Thus, in case of MP the BE of both the receipts and expenditure are underestimates. While, the RE should be fairly close to the actuals as they prepared at the end of the financial year. The accuracy with which the RE is prepared reflects the fiscal transparency and marksmanship.

2.3.3 The table 2.10 shows the fiscal transparency and marksmanship. The revised estimates on the plan side were much higher than the actual. This is mainly because the Departments are reluctant to relinquish control over appropriations. There has been a marked difference between the budget estimates, revised estimates and the account (actual) in the last few years. The actual plan expenditure for the year 2001-02 was only 70.5% of the revised estimates. Similarly, in non plan head expenditure was down by Rs 950 crore (7.3%) in the same year. The Central Government appears to be doing much better than MP as can be seen in the last row of the table.

Fiscal Transparency and Marksmanship

Fiscal transparency is generally defined as openness toward the public about government structure and functions, fiscal policy intentions, public sector accounts and fiscal projections. It involves ready access to reliable, timely, comprehensive, understandable and internationally comparable information on government activities undertaken inside or outside the government sector. Fiscal transparency strengthens accountability. Non-transparent fiscal management can be destabilising, create inefficiency, and foster inequity.

Transparency in government operations has several dimensions. First at an aggregate level, transparency involves the provision of reliable information on the government's fiscal policy intentions and forecasts. Thus, fiscal transparency presupposes a high degree of fiscal marksmanship. Second, detailed data and information are required on government operations, including the publication of comprehensive budget documents that contain properly classified accounts for the general government and quasi-fiscal activities conducted outside the government. The third dimension consists of mainly behavioural aspects including a transparent regulatory framework, open public procurement and employment practices, a code of conduct for tax officials and published performance audits.

Source: State Finances: - Reserve Bank of India

Table 2.10
Fiscal Marksmanship

(Rs. in Crores)

Year / Rs. Cr	***Plan Expenditure*** RE	Actuals	***Difference***	***Non-Plan Expenditure*** RE	Actuals	***Difference***
1993-94	1730	1710.6	19.4	5638.3	5807.4	-169.1
1993-94 (Adj.)	1269.5	1255.2	14.3	4137.3	4261.4	-124.1
1997-98	2439.5	2283	156.5	9022.5	9443.5	420.9
1997-98 (Adj.)	1790.1	1675.2	114.9	6620.7	6929.6	-308.9
1999-00	4672.2	3995.2	677	13320	13433.7	113.8
1999-00 (Adj.)	3428.4	2931.6	496.8	9774.1	9857.6	-83.5
2000-01	4946.1	4064.6	881.5	12613	12328	-284.6
2001-02	6112.7	4311.4	1801.3	13081	12126.7	-954.6
2002-03	7456.98	6433.2	1023.78	11527	11062.2	-468.2
2001-02 (Centre)	99154	101194	-2040	265282	261259	-4023

Source: Budget Document – Government of MP, Government of India.

2.3.4 During any financial year the flow the receipts do not match with the expenditure requirements as it depends on the priorities of those who pay and remit the same. This mismatch between receipts and expenditure necessitates a balancing mechanism. Such balancing mechanism is called Ways and Means Advances (WMA) provided by the Reserve Bank of India (RBI). There is a limit on the WMA provided by the RBI. At present the WMA limit for MP (general and special) is Rs. 345.oo + 21.37 = Rs. 366.37 crore. Sometimes, the gap between receipts and expenditure is so large that the limit of WMA is not sufficient. In such cases, there is another facility called Overdraft (OD). The State has to clear the OD within a limited period beyond which the State Government's cheques are not honored.

2.3.5 It appears from the Table 2.11 that the overdraft (OD) is a rule than an exception. In the year 2003 -- 2004, the state government had to depend on the reserve bank for ways and means for 183 days and an overdraft for 61 days. The reappropriation is being more than the financial resources of the state and hence an imbalance is created for the year.

Table 2.11
Fiscal Imbalances during the Year

Year / Rs.cr	Closing Balance	No.Of days on WMA	No.Of days on OD	Interest paid
1992-93	-21.83	135	130	6.07
1997-98	312.27	142	48	5.21
1999-00	184.13	165	101	12.53
2000-01	186.84	165	47	11.01
2001-02	309.07	117	172	15.62
2002-03	-444.66	106	175	18.24
2003-04	-559.91	183	61	9

Source: Department of Finance, Government of MP.

2.3.6 If the greater amount of estimated expenditure than the income is deposited into the public account receipts in order to maintain a financial balance, the same fiscal imbalance carries on with the next year and in due course of time, the situation becomes alarming. Thus the Comptroller and auditor General of India does not advocate such system as a prudent public fiscal management.

2.3.7 It is also observed that after being on negative with RBI almost all through the year 2002-03, the closing balance has been positive. This is partly because of the Central transfers taking place at the fag end of March. However, there is a need to balance the revenue (both from State and Centre) and expenditure streams.

2.4 Plan Resources

2.4.1 Another important indicator of the financial position of State is the resources available for the plan. A plan is important public policy instrument for initiating and accelerating the growth impulses in the economy.

2.4.2 The resources available for the plan are the residual of all revenue receipts excluding the plan grants from Centre after meeting the non-plan expenditure of the State. The residual of all revenue receipts excluding the plan grants from Centre after meeting the non-plan expenditure of the State is called Balance from Current Revenue (BCR). Ideally, BCR should be positive. Higher the BCR higher would be the size of the plan. As seen from the table 2.12 the BCR has been negative for last five years implying that we have been spending plan resources on non-plan consumption.

Table 2.12
Contribution of State Resources to the Plan

(Rs. in crores)

Year / Rs. cr	Tax Revenues	Non-Tax Revenues	Non-Plan Grants from Centre	Total	Non-Plan Expenditure	Balance from Current Revenues
1993-94	3314.2	1403.73	1764.98	6482.91	5807.36	675.6
1993-94 (Adj.)	2431.95	1030.05	1295.14	4757.14	4261.42	495.7
1997-98	4564.32	2018.54	3592.33	10175.2	9443.48	731.7
1997-98 (Adj.)	3349.28	1481.2	2636.04	7466.52	6929.59	536.9
1999-00	5795.22	2468.97	3873.26	12137.5	13433.7	-1296.2
1999-00 (Adj.)	4252.51	1811.72	2842.19	8906.42	9857.6	-951.2
2000-01	6467.35	1724.33	3309.31	11501	12328	-827
2001-02	4668.88	1601.68	3998.14	10268.7	12126.7	-1858
2002-03	5983.29	1439.31	4463.03	11885.6	11045.9	839.7
2003-04	6633.2	1560.64	5175.43	13369.3	16932.75	-3563.5

Source: Budget Document – Government of MP. (various years)

2.5 Public Debt:

2.5.1 There has been an ever increasing importance of the Public Debt in financial system of the state. One of the major concerns of the State finances is burgeoning public debt. The debt has been growing very rapidly since mid nineties. The financing of public expenditure through debt involves the principles of intergenerational equity. The net public debt was only Rs. 6927.63 crore in 1993-91. It has grown by more than four and half times and estimated to cross Rs.33,737 crore by the end of March 2004. The per capita debt in 1994 was Rs.647.88 and now has become Rs. 5183.66. During this period the consumer price index has doubled. The ratio of public debt to the GSDP of MP for the year 2003-04 is estimated to be 36.41 % The problem is very serious and more so keeping in view that the State requires to make huge investments in physical infrastructure.

Table 2.13
Growth of Public Debt

(Rs. in Crores)

S. No.	As on 31 March	Debt of MP Gross	Debt of MP Net	% Growth of Net Debt	GSDP	% to GSDP
1	1994	9718.85	6927.63	24.76	52752	13.13
2	1994 **(Adj.)**	7131.66	5083.47	24.76	38709	13.13
3	1995	10797.7	7654.03	10.49	58611	13.06
4	1995 **(Adj.)**	7923.28	5616.5	10.49	43009	13.06
5	1996	12545.2	9105.9	18.97	65800	13.84
6	1996 **(Adj.)**	9205.65	6681.88	18.97	48284	13.84
7	1997	14198.2	11301.17	24.11	75345	15
8	1997 **(Adj.)**	10418.6	8292.76	24.11	55288	15
9	1998	16272.6	13705.09	21.27	86255	15.89
10	1998 **(Adj.)**	11940.8	10056.75	21.27	63294	15.89
11	1999	19510.9	16695.28	21.82	94516	17.66
12	1999 **(Adj.)**	14317	12250.94	21.82	69356	17.66
13	2000	23343.5	20498.86	22.78	102144	20.07
14	2000 **(Adj.)**	17129.4	15041.99	22.78	74953	20.07
15	2001	26807.4	17134.41	-16.41	88951	19.26
16	2001	26807.4	17134.41	-16.41	88951	19.26
17	2002 (P)	23883.6	21875.91	27.67	81286	26.91
18	2003 (Q)	27478.6	25038.74	14.46	84087	29.78
19	2004 **(A)**	35555.9	32761.59	26.02	89973	36.41

Source: Budget Document – Government of MP. (various years) / Director of Economics and Statistics, Govt. of MP.

Note: (P) Provisional estimates, (Q) Quick estimates and (A) Assumed estimates.

The data for the GSDP of the state is for the present Madhya Pradesh only. The same has been constructed notionally by the Directoraite of Economics and Statistics Government of Madhya Pradesh. Hence no bifurcation effect is given what the GSDP, while at the same time the net debt has been bifurcated. Growth in GDP of the year 2003 for as being resumed at 7% per annum as per the plan estimates

2.5.2 Another important dimension of public debt is its composition. In technical terms it is also called debt portfolio. The main sources of borrowings of the State are Centre (32%) (70% being part of the plan assistance), Market Loans (25%) also called Development Bonds raised from public through RBI, Institutions like NABARD, HUDCO, LIC. etc, Small Savings (16%) and Public Account (19.2%) (provident Fund, employees insurance and other deposits). As is clear from table 2.14 that almost one-third of the debt is from the Centre. Open market borrowings are on increase in recent times and hence this ratio is gradually reducing. Since the governments pay the old debt by creating a new debt it is only the interest component that is paid out of annual receipts. The ease of getting debt from the Centre, small savings, market borrowings and sanctions off provident fund have also contributed to an unprecedented rise in the public debt.

The Artcle 293(3) of the Constitution governs the borrowings of the States. The permission of GOI has to be obtained to borrow as long as any State owes any money to the Centre. Concern with the mounting interest payments on high cost debt, the GoI recently introduced a debt swap scheme. As per the scheme the State can surrender 30 % of the small savings collections to retire old high cost debt of GoI.

Table 2.14
Composition of Public Debt

S.No	Item/Year	2002	% of Gross Debt	2003	% of Gross Debt	2004	% of Gross Debt
1	Market Loans	4476.36	18.74	5161.51	18.76	8450.1	24.75
2	Centre	9043.18	37.86	10010.55	36.38	10927.8	32.01
3	Institutions	845.84	3.54	1108.61	4.03	1754.9	5.14
4	Small Savings	2326.23	9.74	3926.23	14.27	5526.23	16.19
5	Public Account	7192	30.11	7309.48	26.56	7484.35	21.92
6	Gross Debt	23883.61	100	27516.38	100	34143.4	100
7	Net Debt	21875.91		25997.19		33737.07	

Source: Budget Document – Government of MP. (various years)

2.5.3 It is seen from the table that during the current year almost one third of gross debt is from Centre. This proportion is coming down in recent year due to increased market borrowings. The debt to the Centre is mainly because of the plan assistance given to the States, which contain 70% loan and thirty percent grant. The rate interest on these loans, though coming down, is higher than the market rate. For instance, the present interest rate on the Central loans is 10.5 % as against the market rate of 6%.

2.5.4 In the past market borrowing and small savings did not form a significant part in the debt portfolio. It is only in the recent years, the market borrowings and small savings have increased substantially. Borrowing by the Government is not bad economics per se. It is almost a truism that no Government can survive without borrowing. What the Government does with these borrowing is important both in terms of sustainability of the debt and also intergenerational equity. If the debt is for public investment like irrigation, water supply, power, roads etc., and not for present consumption, then it is justified. It is true that most of these public investments are not financially viable due to low user charges. But they are economically viable as these investments create large externalities, both in terms of inducing private investment and also enlarging the tax base.

Table 2.15
Uses of Debt

(Rs. in Crores)

Year / item Rs.in cr	Net Debt	CE	% of CE in debt
1993-94	1061.67	807.39	76.05
1993-94 **(Adj.)**	779.04	592.46	76.05
1997-98	2108.1	1677.8	79.59
1997-98 **(Adj.)**	1546.91	1231.16	79.59
1999-00	3975.63	950.07	23.9
1999-00 **(Adj.)**	2917.3	697.15	23.9
2000-01	2721.09	1110.51	40.81
2001-02	4529.98	1470.64	32.46
2002-03	3611.08	2448.47	67.8
2003-04	7799.69	2930.16	37.57

Source: Budget Document – Government of MP. (various years)

2.5.5 Unfortunately, as seen from the table 2.15, a majority of the public debt went into financing current consumption (to bridge the revenue deficit) and loans & advances, most of which are never serviced. (The net debt does not include the closing balance of accounts).

2.5.6 An analysis of the White Paper would depict that the loan taken for the purpose of development have not been spent on development. On the contrary, it has been spent on non developmental purposes. For instance, only 24 percent of the net debt taken in the year 1999 2000 was spent on developmental capital expenditure while the balance was spent on revenue expenditure. Loans are usually taken for asset creation of the purpose of development like road construction, power generation, irrigation, etc. but the study proves that the purposes of raising loans have been unclear and objectives unfulfilled. The description of public debt also indicates that the project based loans form only 5% of the overall debt portfolio. Non utilisation of the loans from financial institutions like NABARD have precipitated the cost and time overruns as can be seen from Annexure II. The condition of public sector undertakings of the state, various corporations & boards also do not pose a rosy picture and have been reporting continues losses in last few years. The accumulated losses of such public sector undertakings have mounted to 52040.87 lakhs (Annexure III)

2.6 Debt Burden

2.6.1 The interest burden of the State has increased unprecedentedly in the last decade. An interest burden of Rs 868 crores in 1993-94 that used to the 12 percent of revenues is likely to go up to Rs 3500 crores that is 23 percent of revenues in the year 2003-04. A decrease in the own revenues of the government as a proportion of the overall revenues has necessitated the dependence on public debt.

2.7 Debt Sustainability

2.7.1 Another important dimension of the public debt is its sustainability. After examining the debt position of all the States and the Centre the Eleventh Finance Commission has prescribed that the proportion of the interest payments to the revenue receipts including devolutions and grants should be about 18 percent. The table below presents proportion of interest payments in the total revenue receipts. It can be seen from the table that we crossed the Lakshman Rekha prescribed the Eleventh Finance Commission.

Fiscal Objectives set by the EFC

- Gross Fiscal Deficit of the States as an aggregate, fall to 2.5% GSDP Revenue deficit of all States, in an aggregate, falling to zero.
- Interest payments as percentage of revenue receipts of the State Sector as a whole to be between 18-20%
- In the supplementary Report the EFC has also suggested the following objectives:-

1. Increases in wages and salaries should not exceed 5% or increase in the consumer price index whichever is higher.
2. Increase in interest payments (in absolute terms) may be limited to 14.3% per year
3. Explicit subsidies to be brought down to 50% over the next five-year period with a view to eliminate subsidies altogether by 2009-2010.

Source: Report of Eleventh Finance Commission

Table 2.16
Problems of Public Debt?

(Rs. in Crores)

Year/Item	*Revenue Receipts*	*Interest*	*% of Interest payments in RR*	*Debt to Revenue Receipts ratio*
1993/94	7069.78	867.9	12.28	97.99
1993/94 (Adj.)	5187.78	636.86	12.28	97.99
1994/95	7618.29	1094.33	14.36	100.47
1994/95 (Adj)	5590.28	803.02	14.36	100.47
1995/96	8653.47	1158.25	13.38	105.23
1995/96 (Adj)	6349.89	849.92	13.38	105.23
1996/97	10014.23	1376.22	13.74	112.85
1996/97 (Adj)	7348.41	1009.87	13.74	112.85
1997/98	11257.12	1659.92	14.75	121.85
1997/98 (Adj.)	8260.44	1218.04	14.75	121.85
1998/99	11345.85	1834.75	16.17	147.15
1998/99 (Adj.)	8325.55	1346.33	16.17	147.15
1999/00	13203.68	2138.66	16.2	155.25
1999/00 (Adj.)	9688.82	1569.34	16.2	155.25
2000/01	13667.07	2410.78	17.64	125.37
2001/02	11200.98	2253.67	20.12	195.3
2002/03	13390.4	2502.31	18.68	187.94
2003-04	14758.17	3416.52	23.15	221.99

Source: Budget Document – Government of MP. (various years)

2.7.2 The government of India does not favour those States whose debt burden is more than 30% of their GSDP. The government of India has also indicated that the debt to total revenue received ratio for the year 2003-04 should not exceed and 166.40% and the same for the year 2004-05 should be 166.75%. Only those States that are complying with these ratios are eligible for multilateral assistance.

2.8 The Fiscal Parameter

2.8.1 The Revenue Deficit (RD), Fiscal Deficit (FD) and the Primary Deficit (PD) are the summary indicators that reflect the financial position of the Government. The RD is the difference between the revenue receipts and revenue expenditure. If Revenue Expenditure is more than the Revenue Receipts, then the government has to borrow for meeting out the deficit. Since these are deficit indicators, a positive number indicates deficit and a negative number indicates surplus. If the revenue expenditure is more than the revenue receipts, it means the Government is not able meet its current consumption requirements and is borrowing to meet these demand. The borrowings for consumption requirements and for the capital investment are indicated by the FD. The interest payments are current consumption for past borrowings. The PD is derived by excluding the interest payments from the FD.

All these indicators are expressed as a ratio of GSDP at current prices for the purpose of comparability across time and space.

2.8.2 The table 2.17 depicts these deficit parameters. Except for the year 1992-93, the State has been in deficit. Annexure V shows the revenue deficit and fiscal deficit of the main States of the country for the year 2000 -- 01 (actual) and 2001 -- 02 (revised) The annexure would also depict that in the year 2001 -- 02 the state of Madhya Pradesh has failed to perform its fiscal parameter as compared to the other States.

Table 2.17
Deficit Parameters[1]

Year / Parameters	Revenue Deficit	Fiscal Deficit	Primary Deficit
1993-94	0.85	1.86	0.22
1997-98	0.58	2.47	0.42
1999-00	2.87	3.83	1.74
2000-01	1.48	3.05	0.34
2001-02	3.9	4.49	1.71
2002-03	1.41	4.89	1.88
2003-04	5.78	9.43	5.64

Source: Budget Document – Government of MP. (various years)

2.8.3 In pursuance of the recommendation of the Eleventh Finance Commission, the Ministry of Finance, Government of India issued certain guidelines regarding formulation of a Fiscal Reforms Programme (FRP). As per the FRP, the States are supposed to prepare a Medium Term Fiscal Restructuring Policy (MTFRP). This Policy includes fiscal reforms, power structure reforms, public structure reforms and budgetary reforms. The releases from the incentive fund are based on a single monitorable fiscal objective. Each State is expected to achieve a minimum improvement of 5 percent in the revenue deficit as proportion of their revenue receipt each year till 2004-05. The base year is financial year 1999-00. Keeping these guidelines in view, the Government of Madhya Pradesh drew up on its own a medium term fiscal reforms Programme with basic objective of reducing the revenue deficit as a percentage of revenue receipt by 5 percent in each year from 2000-01 onwards with reference to its level for the year 1999-2000. The revenue deficit as a percentage of revenue receipts, which was 22.21 percent in the year 1999-2000, fell to 9.65 percent in the year 2000-01. It however, rose to 28.28 percent in the year 2001-02, but has fallen to 8.55 percent in the year 2002-03.

[1] Growth Rate for the year 2003-04 has been assumed at 7% for GSDP, based on the Plan.

2.9 Contingent Liabilities on Revenue

2.9.1 Guarantees

have been given by the government for the discharge of certain liabilities like loans raised by statutory corporations, government companies, joint stock companies, cooperative institutions, local bodies etc. These guarantees constitute the contingent liabilities of the state revenue. Unfortunately, most of the organisations to which these guarantees are given, are not able to service their debt obligations diligently. As a result in many an occasion, the lending organisations had revoked the guarantee against Government. The total guarantees at the end of year 1993-94 were 6838.84 crores which mounted to Rs 9709.6 crores on 31st October 2000 at the time of bifurcation. The total guarantees of the present Madhya Pradesh outstanding as on 2002-03 are to the tune of 11572.38 crores. Most of the balances in of the above figures are still from the erstwhile Madhya Pradesh because the same has not been divided between the present Madhya Pradesh and Chhattisgarh. The loans and advances given by the government are shown at Annexure VII. These loans and advances are given for general services, social services and economic services. The Annexure would also depict that most of the loans and advances have been given to economic services. The indiscriminate guarantees provided by the government has created the contingent liability on the state.

Policy Measures on guarantees

The State Governments' guarantees is another area where the Bank has taken a number of initiatives. The Technical Committee on State Government Guarantees constituted by the Bank in its report (1999) had recommended: (i) imposition of ceiling on guarantees, (ii) selectivity in calling for and providing of guarantees, (iii) greater transparency in the reporting of guarantees and standardisation of documentation, (iv) guarantee fee and contingency fund for guarantees and (v) monitoring and honouring of guarantees. Following this, many States have initiated measures such as placing ceiling on guarantee, setting up guarantee redemption fund, *etc.* The Reserve Bank had constituted a Group to assess the fiscal risks of State Governments guarantees. The major recommendations of the Group are as under:

(i) segregation of guarantees which are effectively in the nature of direct liabilities and assess the risk of such guarantees as 100 per cent and treating the same as equivalent to debt, (ii) publication of data regarding guarantees regularly, in a standard format, (iii) classification of projects/ activities as high risk, medium risk, low risk and very low risk and assigning appropriate risk weights; once the guarantees have been categorised, the finance departments of States will have to use their judgment to assign devolvement probability to each risk category, (iv) creation of a Tracking Unit for guarantees (in the Ministry of Finance) at the State level, (v) transferring one per cent of outstanding guarantees to the Guarantee Redemption Fund each year, (vi) the total obligation of interest payments and likely devolvement should not exceed 20 per cent of revenue receipts and (vii) State Governments should take administrative measures to discipline the State level undertakings whose borrowings are guaranteed and set up arrangements like escrow accounts with contributions from project earnings or rationalising user charges.

Source: State Finances :A Study of Budgets of 2002-03- RBI

Chapter 3
Emerging Fiscal scenario

3.0 The State Governments have been experiencing fiscal stress in recent years as evident from large and increasing fiscal and revenue deficits. The rise in the fiscal deficit (FD) was pronounced in the second half of the 1990s, with an increasing high proportion being accounted for by the rising revenue deficit. In recent years, on an average, more than one half of the FD has been on account of revenue deficit. This implies that a significant proportion of the borrowed funds has been utilised for meeting revenue expenditure. The consequential accumulation of debt and debt service obligations has put constraints on the States' ability to undertake developmental activities, *viz.*, provision of economic and social infrastructure.

3.1 Fiscal Responsibility

3.1.1 In order to address this problem, the States have been undertaking a number of policy measures relating to revenue augmentation, containment of expenditure, and public sector reforms. The States' initiatives towards fiscal reforms have also been supplemented by the Central Government. Recognising the fact that significant improvement in States' fiscal health is feasible only in the medium term, a number of States have, in consultation with the Centre, embarked upon medium term strategies towards fiscal consolidation.

3.1.2 The institutional reforms proposed in the State budgets aim at fiscal stability and sustainability. As per the Reserve bank Report on, "State Finances :A Study of Budgets of 2002-03", four States *viz.* Karnataka, Kerala, Maharashtra and Punjab have initiated/proposed measures to provide statutory backing to the fiscal reform process through enabling legislation. The State of Karnataka enacted the Fiscal Responsibility Bill in August 2002, while States of Maharashtra and Punjab have introduced fiscal responsibility bills in their Legislatures. The Kerala Government has proposed to introduce a Fiscal Accountability Bill. On the expenditure front, a number of States have proposed containment of revenue expenditure through a set of economy measures such as restrictions on fresh recruitment/creation of new posts and curbing the growth in administrative expenditure. Some States have proposed introduction of a new contributory pension scheme for newly recruited staff as is the case in Rajasthan.

3.1.3 Government of Karnataka had prepared a Fiscal Responsibility Bill. Subsequently, this has been notified as the Fiscal Responsibility Act in the Karnataka Gazette dated August 30, 2002.

The key features of the Karnataka Fiscal Responsibility Act are as under:

- Reduction in the revenue deficit to 'nil' within four financial years beginning April 2002 and ending March 31, 2006.

- Reduction in the fiscal deficit to not more than three per cent of the estimated gross state domestic product (GSDP) within four financial years beginning April 2002 and ending March 31, 2006.

- Reduce revenue and fiscal deficits as a percentage of GSDP in each of the financial year.

- Limiting the guarantees within the prescribed limits under the Guarantees Act.

Ensure that by end-March 2015, the total liabilities do not exceed 25 per cent of the estimated GSDP for that year.

3.2 Conclusion

3.2.1 A strong financial condition is the foundation of self-reliance state of economy. A fiscal consolidation is most necessary in high cost debt regime. While granting assistance the government of India, reserve bank of India and other financial institutions have been emphasizing on fiscal consolidation of state. An attempt in this direction is most necessary for the future development state