WMA Borrowings of States

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Why in News

Recently, states like Kerala, Punjab and Bihar have said that the **Reserve Bank of India's (RBI)** decision to allow 60% higher borrowing under Ways and Means Advances (WMA) compared March 30, 2020 limit, is inadequate given the mounting expenses of states to counter the **Covid-19 pandemic**.

Key Points

- The states welcomed the **RBI move to allow 60% higher borrowing under Ways and Means Advances (WMA)**, but said it is a temporary relief and will have only a marginal impact upon the fiscal crisis the states are facing.
- They are saying that they **can not go long for ways and means and have to slash their expenditure** to a large extent because they do not have many avenues left for revenue augmentation.
    - They said banks are not willing to lend for the long term large amounts of money because of their **liquidity preference.**
- They demanded from the Central government to **raise the fiscal borrowing** limits of states currently capped at 3% of the GSDP (Gross State Domestic Product) under the **Fiscal Responsibility and Budget Management (FRBM) Act.**
- The Centre can invoke **Section 5(3)** of Fiscal Responsibility and Budget Management Act, 2003 which allows the RBI to **"subscribe to the primary issues of Central Government securities"** under very specific grounds.
- Those cover, among other things, **"act of war" and "national calamity".**
- The RBI can also undertake increased **secondary market purchases** and **sales of Central as well as state government securities.**

Ways and Means Advances (WMA)

- The WMA are **short-term loan facilities** which allow the **Centre and states** to borrow funds from the **RBI** to bridge their **temporary mismatch** between expenditure and receipts.
- The interest rate on WMA is the **RBI's repo rate.**
    - Repo rate is basically the rate at which RBI lends short-term money to banks.
- The WMA loans have a **three-month tenure.**
- States are allowed an **overdraft facility** (to borrow in excess of WMA limit) **of 21 days.**

Fiscal Responsibility and Budget Management (FRBM) Act, 2003

- The FRBM Act was enacted by the Parliament in 2003 to institutionalize fiscal discipline, reduce fiscal deficit, and improve macroeconomic management.
- The government was supposed to wipe out revenue deficit and cut fiscal deficit to 3% of GDP by 2008-09, thus bringing much needed fiscal discipline.
    - **Fiscal deficit** is the total expenditure excluding revenue receipts, loan recoveries and receipts from disinvestment etc. It is a measure of the government borrowing in a year.
- The Act applies only to the central government and the **States have to enact suitable legislation to adopt the rules under the FRBM Act.**
- The implementation of the Act was **put on hold in 2007-08** due to the global financial crisis and the need for fiscal stimulus.
- In 2012, the FRBM Act was amended and it was decided that the FRBM Act would target an effective revenue deficit in place of revenue deficit.
    - **Effective revenue deficit** excludes capital expenditure from revenue deficit and thus provides space to the government to spend on formation of capital assets.
- In 2017, the **FRBM Review Committee** headed by former Revenue Secretary, **NK Singh** submitted its report to the Central Government. Few important recommendations being-
    - A debt to GDP ratio of 60% should be targeted with a 40% limit for the centre and 20% limit for the states;
    - Creation of an autonomous Fiscal Council;
    - An "escape clause", i.e. the government can deviate from the targets in case of a national calamity, national security, etc.
        - The government **used an escape route** in its Budget for FY20, by taking a deviation of 0.5 percentage points from the fiscal deficit targets set out earlier.
- During the presentation of the Budget 2020-21, the government fixed the fiscal deficit target for the year 2020-21 at 3.5% of the GDP.

Source: IE