State Finances: A Study of Budgets of 2022-23

For Prelims: Reserve Bank of India (RBI), Gross Fiscal Deficit (GFD), Informal sector, State Finances: A Study of Budgets of 2022-23, Fiscal Responsibility and Budget Management (FRBM).

For Mains: Significance of the State Finances: A Study of Budgets of 2022-23 in Debt improvement of the states.

Why in News?

Recently, the **Reserve Bank of India (RBI)** has released a report stating that the **Gross Fiscal Deficit (GFD)** of states is expected to **decrease to 3.4%** of **Gross Domestic Product (GDP)** in **2022-23**, from **4.1%** in **2020-21.**

- This is due to a **broad-based economic recovery** and an increase in **revenue collections.**

What is the Report "State Finances: A Study of Budgets of 2022-23"?

- **About:**
  - The report titled **"State Finances: A Study of Budgets of 2022-23"** is a **comprehensive analysis of the financial position of the Indian states,** including the **trends and challenges** in their **revenue and expenditure.**
- **Finding of the Report:**
  - According to the **RBI** report, **states' debt** is expected to **decrease to 29.5% of GDP in 2022-23**, compared to **31.1% in 2020-21.**
  - However, the report also highlights that this is still higher than the **20%** recommended by the **Fiscal Responsibility and Budget Management (FRBM) Review Committee in 2018.**
  - States are anticipating an increase in **non-tax revenue**, which is generated from sources such as **fees, fines, and royalties**. This increase is likely to be driven by **revenue** from industries and general services.
  - The report notes that states are expecting to see **an increase in revenue** from various sources such as State GST**, excise taxes**, and **sales taxes** in the **2022-2023** fiscal year.
- **Measures Suggested in the Report:**
  - This suggests that **debt consolidation should be a priority for state governments.**
    - **Debt consolidation** refers to the **process of combining multiple debts into a single, more manageable debt.** This can help to **lower overall interest costs,** simplify **payments,** and make it **easier to pay off the debt.**
  - Allocating **more resources to key sectors** such as **healthcare**, **education**, **infrastructure**, **and** green energy, the states can promote **economic growth** and **development.**
  - The report is proposing that it would be beneficial to establish a fund that would be used to **buffer capital expenditure** during periods of **strong revenue growth.**
    - The purpose of this fund would be to **maintain a consistent level of spending on capital projects**, and to ensure that spending on these projects is not

drastically reduced during **economic downturns.**
- In order to attract **private investment, state governments** should focus on creating a **favorable environment** for the private sector to operate and grow.
    - This can be achieved by **implementing policies and regulations** that make it easy for private companies to do business, as well as **providing incentives and support for private investment.**
- States also need to encourage and facilitate **higher inter-state trade and commerce** to realize the full benefit of spillover effects of state capex across the country.

What is Gross Fiscal Deficit (GFD)?

- **GFD** measures the **overall financial health** of the **state government** and is **calculated by subtracting total revenue** from **total expenditure.**
- A decrease in **GFD** is generally considered a **positive sign** as it indicates that the **state government is able to balance** its revenue and expenditure more effectively.

What are the Measures of Government Deficit?

- **Revenue Deficit:** It refers to the excess of government's revenue expenditure over revenue receipts.
    - **Revenue Deficit = Revenue expenditure – Revenue receipts**
- **Fiscal Deficit:** It is the gap between the government's expenditure requirements and its receipts. This equals the money the government needs to borrow during the year. A surplus arises if receipts are more than expenditure.
    - **Fiscal Deficit = Total expenditure – (Revenue receipts + non-debt creating capital receipts).**
- **Primary Deficit:** Primary deficit equals fiscal deficit minus interest payments. This indicates the gap between the government's expenditure requirements and its receipts, not taking into account the expenditure incurred on interest payments on loans taken during the previous years.
    - **Primary deficit = Fiscal deficit – Interest payments**
- **Effective Revenue Deficit:** It is the difference between **revenue deficit** and **grants** for **creation of capital assets.**
    - The concept of **effective revenue deficit** has been suggested by the **Rangarajan Committee** on Public Expenditure.

UPSC Civil Services Examination Previous Year Question

Q1. Which one of the following is likely to be the most inflationary in its effect? (2021)

(a) Repayment of public debt
(b) Borrowing from the public to finance a budget deficit
(c) Borrowing from the banks to finance a budget deficit
(d) Creation of new money to finance a budget deficit

Ans: (d)

Q2. Consider the following statements: (2018)

1. The Fiscal Responsibility and Budget Management (FRBM) Review Committee Report has recommended a debt to GDP ratio of 60% for the general (combined) government by 2023, comprising 40% for the Central Government and 20% for the State Governments.
2. The Central Government has domestic liabilities of 21% of GDP as compared to that of 49% of GDP of the State Governments.
3. As per the Constitution of India, it is mandatory for a State to take the Central Government's consent for raising any loan if the former owes any outstanding liabilities to the latter.

Which of the statements given above is/are correct?

(a) 1 only
(b) 2 and 3 only
(c) 1 and 3 only
(d) 1, 2 and 3

Ans: (c)

Q3. Which of the following is/are included in the capital budget of the Government of India? (2016)

1. Expenditure on acquisition of assets like roads, buildings, machinery, etc.
2. Loans received from foreign governments
3. Loans and advances granted to the States and Union Territories

Select the correct answer using the code given below:

(a) 1 only
(b) 2 and 3 only
(c) 1 and 3 only
(d) 1, 2 and 3

Ans: (d)

Source: IE

PDF Refernece URL: https://www.drishtiias.com/printpdf/state-finances-a-study-of-budgets-of-2022-23