

Chapter 4

DEFICITS: MANAGEMENT OF FISCAL IMBALANCES

4.1 The budget deficit is an instrument of fiscal management. The different facets of the budget deficit indicate the different nature of fiscal imbalances. The annual budget indicates three types of deficits, viz. revenue, fiscal, and primary. This chapter discusses the nature and magnitude of these deficits, their trend over time and the manner of financing these deficits.

4.2 Table 4.1 presents the break-up of the deficit during 2000-01. There was a deficit in the CFI amounting to Rs 23925 crore and a surplus in the Public Account amounting to Rs 25123 crore. The excess of this surplus amounting to Rs 1,198 crore represented addition to the closing cash balances.

Table 4.1: Deficits in Government Account

<i>(Rs in crore)</i>					
CONSOLIDATED FUND					
Receipt	Amount			Disbursement	Amount
Revenue	256,036	Revenue deficit	86,611	Revenue	342,647
Non-debt Capital Receipts	2,125			Capital	25,426
Recovery of loans & advances	16,799			Loans & advances disbursement	27,761
Sub total CFI (other than public debt)	274,960			Sub total CFI (other than Public Debt)	395,834
Public debt	366,461	Fiscal deficit	120,874	Public debt repayment	269,512
Total (CFI)	641,421	A: Deficit in CFI	23,925		665,346
PUBLIC ACCOUNT					
Small savings, provident funds etc.	140,856			Small savings, provident funds etc.	126,464
Deposits and advances ¹	70,400			Deposits and advances	59,873
Reserve funds [□]	21,742			Reserve funds	21,378
Suspense & miscellaneous	13,344			Suspense & miscellaneous	16,735
Remittances [□]	3,534			Remittances	303
Total Public Account	249,876	B: Surplus in Public Account: 25,123			224,753
Increase in cash balance {B-A} = 1,198					
<ol style="list-style-type: none"> 1. Includes Security Deposits of Railways Telephone Application Deposits, Postal Deposits, Forest Advances, Departmental Advances etc. 2. Includes Depreciation Reserve Funds – Railways, Revenue Reserve Funds - Railways, Sugar Development Funds, Mines Welfare Funds, National Renewal Funds etc. 3. Includes amounts awaiting final adjustments in the accounts like Pay and Accounts Office Suspense, Suspense Account P&T, Defence, Railways and Tele-communication, Coinage Accounts, Cheques and Bills etc. 4. Includes money in transit like Money Orders. RBI Remittances, Small Coin Depot remittances, Mint remittances etc 					

Fiscal deficit was not only unduly high during 2000-01; it was used predominantly for meeting revenue expenditure.

4.3 The surpluses and deficits in Consolidated Fund or Public Account only indicate the excess of receipts or disbursements in these accounts and these do not constitute fiscal deficits or surpluses. Fiscal deficit of the Union Government indicates the excess of its total expenditure consisting of revenue and capital expenditures and loans and advances over its non-debt receipts. In the year 2000-01, total expenditure of the Union government at Rs 395,834 crore exceeded its non-debt receipts by Rs 120,874 crore. The fiscal deficit, at this level, was 5.58 *per cent* of GDP. The Union government resorted to borrowings from internal and external sources as also from the Public Account to meet this deficit.

4.4 There was also a revenue deficit as revenue receipts fell short of the revenue expenditure by Rs 86,611 crore. Revenue deficit accounted for nearly 72 *per cent* of the fiscal deficit.

Deficits: Trends

4.5 Fiscal imbalances are both transient and structural. Transient imbalances result from temporary mismatches in revenue and expenditures of the Union Government, management of which requires accommodation in the nature of ways and means advances. These transient mismatches, largely of a cyclical nature, may at times go beyond an accounting time frame of a year, but there could be an automatic correction. However, persisting imbalances are structural and more difficult to address. These may arise from the inability to raise revenues or contain expenditure or a combination of both. As was indicated in the previous two chapters, fiscal imbalances is largely due to poor tax compliance.

4.6 Fiscal deficit represents the draft of the Union Government from the economy and a net transfer of resources in its favour. This transfer, however, results in creation of fiscal liabilities for the Union government. This makes the issue of debt sustainability critically dependent on the fiscal deficit and the application of resources so arranged. Fiscal deficit and current account deficit are also inter-linked and existence of the former essentially spills over to the later.

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4.7 Table 4.2 indicates the trend in various facets of fiscal imbalances together with the trends of revenue and expenditure. Appendix-IV presents deficit for the last 25 years. Revenue deficit of the Union government increased from Rs 5564 crore in 1985-86 to Rs 86,611 crore in 2000-01, nearly sixteen times in sixteen years (1985-2001), at an annual trend rate of 18.73 *per cent*. Revenue deficit was not only a permanent feature of the Union government finances, it has risen faster compared to both revenue receipts and revenue expenditure.

Table 4.2: Magnitude of Deficits

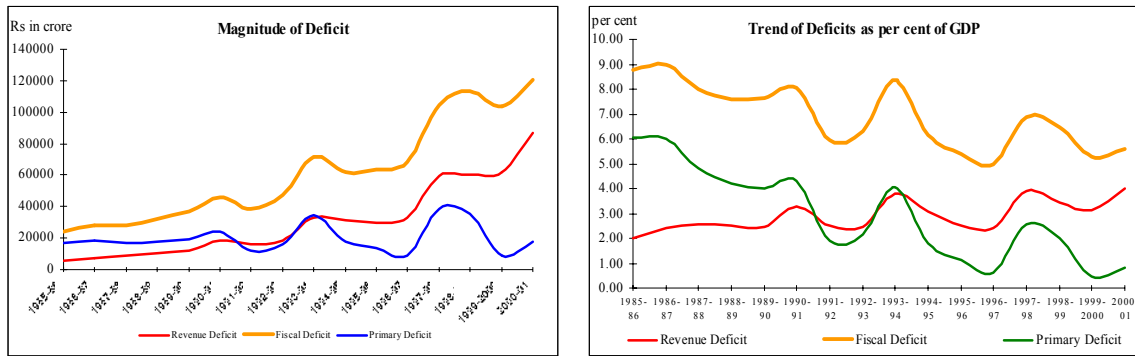
(Rs in crore)

	Revenue Receipts	Non-Debt Receipts	Revenue Expenditure	Total Expenditure	Interest Payments	Revenue Deficit	Fiscal Deficit	Primary Deficit
1985-86	37843	41708	43407	66112	7512	5564	24404	16892
1995-96	150560	158956	180291	222645	50045	29731	63689	13644
1997-98	195853	206361	255286	310982	65637	59433	104621	38984
1998-99	215224	234287	275791	347585	77882	60567	113298	35416
1999-2000	254595	268869	316237	372619	94593	61642	103750	9157
2000-01	256036	274960	342647	395834	103224	86611	120874	17650
Average Annual Trend Rate of Growth (<i>per cent</i>)								
1985-2001	14.11	13.83	14.94	13.10	19.11	18.73	11.61	0.00
1985-90	15.88	15.33	16.49	13.55	24.05	20.33	10.33	2.37
1992-97	15.61	14.51	14.64	11.87	17.44	10.88	6.42	19.36
1997-2001	10.21	10.50	10.74	8.26	16.80	12.16	3.51	31.13
Annual Rate of Growth (<i>per cent</i>)								
1998-99	9.89	13.53	8.03	11.77	18.66	1.91	8.31	-9.15
1999-2000	18.29	14.76	14.67	7.20	21.46	1.77	-8.43	-74.14
2000-01	0.57	2.27	8.35	6.23	9.12	40.51	16.51	92.75

Negative signs have been omitted for all deficits.

4.8 Fiscal deficit recorded a comparatively lower growth of 11.62 *per cent* during 1985-2001. But this lower growth offers no comfort as in absolute terms it increased nearly five fold from Rs 24,404 crore in 1985-86 to Rs 120,874 crore in 2000-01. The comparatively lower growth in fiscal deficit was due to a relatively lower growth of capital expenditure, which moderated

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the growth in total expenditure of the Union government. Primary deficit, which indicates fiscal deficit net of the interest payments, show a negative trend growth. But this was due to a much faster increase in interest payments, which averaged 19.11 *per cent* per annum during 1985-2001. Appendix-V presents the fiscal deficit and interest payment for the last 25 years.

4.9 The comparative picture of the three deficits over the Five Year plans indicates a mixed trend. Revenue deficit witnessed a deceleration in the average annual growth rates during the VIII Plan (1992-97) compared to the earlier plan. However, during the IX Plan, growth further accelerated. In case of the fiscal deficit, average annual rate of growth continued to decelerate over the plans. Average annual growth of fiscal deficit declined to 3.51 *per cent* during 1997-2001, compared to a growth of 10.33 *per cent* during 1985-90 and 6.42 *per cent* during 1992-97.

4.10 In 2000-01, all the three variants of deficit accelerated. In case of revenue deficit, the increase was of the order of 40.51 *per cent*, as against a modest growth of 1.77 *per cent* a year earlier in 1999-2000. The fiscal deficit, which had recorded a negative growth of 8.43 *per cent* in 1999-2000, grew by 16.51 *per cent*. In the primary deficit, the rate of growth at 92.75 *per cent* was even higher. This indicates a further deterioration in the fiscal situation in 2000-01.

Revenue Deficit

4.11 Revenue deficit represents government's dis-saving and inter-temporally, a shift to present consumption. Of the three variants of deficit,

persistent revenue deficit is considered most undesirable in view of its adverse impact on capital formation by the government.

4.12 Table 4.3 summarises the magnitude of the revenue deficit relative to revenue receipts, revenue expenditure and GDP over the plans and during the last three years.

Table 4.3: Revenue Deficit Relative to GDP, Revenue Receipts & Expenditure

	<i>(per cent)</i>		
	GDP	Revenue Receipts	Revenue Expenditure
1985-2001	2.90	22.38	18.12
VII Plan (1985-90)	2.39	17.14	14.62
VIII Plan (1992-97)	2.85	22.45	18.22
IX Plan (1997-01)	3.62	29.13	22.50
Annual Relative Share (per cent)			
1998-99	3.44	28.14	21.96
1999-2000	3.15	24.21	19.49
2000-01	4.00	33.83	25.28

4.13 Revenue deficit increased from an average of 2.39 *per cent* of GDP during the Seventh Five Year Plan (1985-90) to an average of 3.62 *per cent* during the Ninth Plan (1997-2001). It was around 17 *per cent* of the revenue receipts and around 15 *per cent* of revenue expenditure during 1985-90. The ratio of revenue deficit to revenue receipts/expenditure indicates the increase/decrease in revenue receipts/expenditure that was needed to completely eliminate the deficit. These ratios show a continuous increase over the two successive plans. During 1997-2001, revenue deficit was 29 *per cent* of revenue receipts and around 22 *per cent* of revenue expenditure, indicating that nearly a quarter of revenue expenditure was financed by additional fiscal liabilities. All these ratios were on the rise indicating continuing deterioration in the revenue deficit situation and increasing fiscal imbalances.

4.14 There was a further deterioration of the revenue deficit situation in 2000-01. It reached a level of 4 *per cent* of GDP and accounted for 25.28 *per cent* of revenue expenditure. The growing revenue deficit indicated increasing dependence on debt for meeting even the current expenses.

Fiscal Deficit

4.15 Table 4.4 indicates the ratio of fiscal deficit to GDP, non-debt receipts and total expenditure over the plans and during the last three years.

Table 4.4: Ratio of Fiscal deficit to GDP, Non-debt Receipts and Total Expenditure

	<i>(per cent)</i>		
	GDP	Non-Debt Receipts	Aggregate Expenditure
1985-2001	6.89	48.43	32.45
VII Plan (1985-90)	8.19	53.74	34.92
VIII Plan (1992-97)	6.22	45.59	31.06
IX Plan (1997-01)	6.05	45.40	31.16
Annual Relative Share <i>(per cent)</i>			
1998-99	6.44	48.37	32.60
1999-2000	5.30	38.59	27.84
2000-01	5.58	43.96	30.54

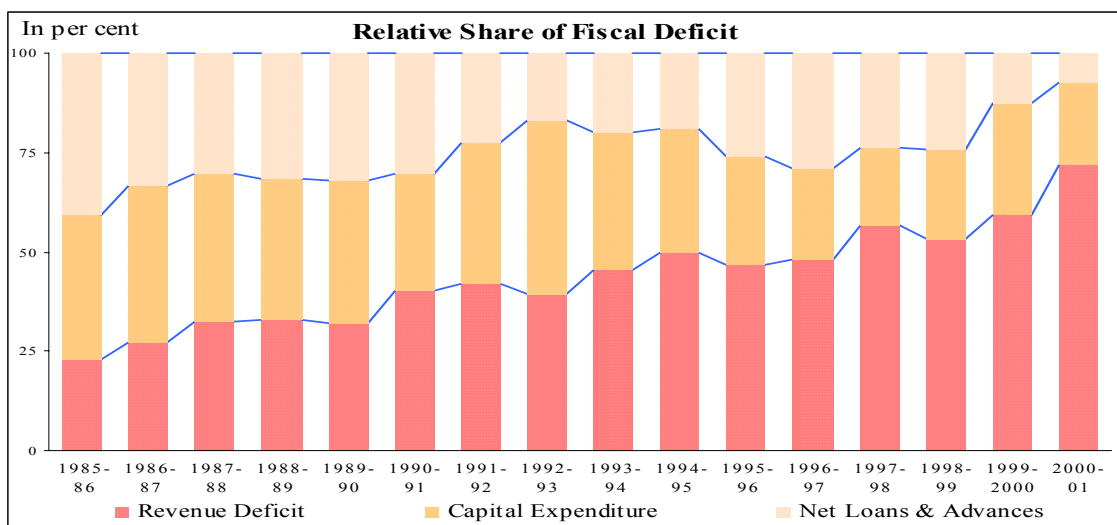
4.16 The ratio of fiscal deficit to GDP shows a continuous decline, when compared over the three Plans. It declined from an average of 8.19 *per cent* of GDP during 1985-90 to an average of 6.05 *per cent* during 1997-2001. Fiscal deficit financed nearly 35 *per cent* of total expenditure during 1985-90. This ratio marginally declined to 31.16 *per cent* during 1997-2001. As a percentage to non-debt receipts, fiscal deficit declined from an average of 53.74 *per cent* during 1985-90 to an average of 45.40 during 1997-2001. This ratio indicates the increase in non-debt receipts that would have been needed to meet the expenditure levels.

4.17 In 2000-01, though the fiscal deficit/GDP ratio at 5.58 *per cent* remained lower compared to the trend value, it worsened compared to a level of 5.30 *per cent* reached in 1999-2000. Fiscal deficit financed 30.54 *per cent* of total expenditure, as against 27.84 *per cent* in 1999-2000.

4.18 It is necessary to study the components of fiscal deficit and their movement over the plan periods.

Table 4.5: Components of Fiscal Deficit- Relative Share

	<i>(per cent)</i>		
	Revenue Deficit	Capital Expenditure	Net Loans & Advances
1985-2001	43.77	31.24	24.99
VII Plan (1985-90)	29.43	36.91	33.66
VIII Plan (1992-97)	45.91	31.93	22.16
IX Plan (1997-01)	60.33	22.64	17.02
Annual Relative Share (per cent)			
1998-99	53.45	22.24	24.31
1999-2000	59.41	27.97	12.61
2000-01	71.65	21.04	7.31



4.19 Revenue deficit accounted for 43.77 *per cent* of the fiscal deficit over 1985-2001. This ratio witnessed a continuous increase over the plans. From an average of 29.43 *per cent* during 1985-90, it increased to 60.33 *per cent* during 1997-2001. Ideally, even capital expenditure of the Government should be financed from revenue surpluses. If such surplus is not available, fiscal deficit should be used to finance the capital expenditures so that income-generating assets are created to match the increasing liabilities. These assets could be serviced from the income/revenue generated by them. But continuous recourse to fiscal deficit for meeting the current expenses is not desirable.

4.20 In 2000-01, revenue deficit accounted for 71.65 *per cent* of the fiscal deficit. Capital expenditure accounted for 21.04 *per cent* and the balance 7.31 *per cent* was utilized for making loans and advances. Expenditure financed by borrowings during the last 25 years is given in **Appendix-VI**.

4.21 Adequate financial accommodation is required to meet the fiscal deficit. Raising debt and use of Public Account funds are two options in meeting the deficit, and have been resorted to in varying degrees over the years for this purpose. Table 4.6 indicates the manner of financing the fiscal deficit.

Table 4.6: Financing of Fiscal deficit- Components and relative Share

(Rs in crore)

Period	Fiscal deficit	Financing of Fiscal Deficit			Relative Share (<i>per cent</i>)		
		Internal Debt	External Debt	Public Account Receipts	Internal Debt	External Debt	Public Account Receipts
1985-2001	61869	46572	3082	12426	75.30	5.00	20.10
1985-1990	29957	14931	2341	12881	49.80	7.80	43.00
1992-1997	62565	34345	3458	24855	54.90	5.50	39.70
1997-2001	110636	114805	2927	-6724	103.80	2.60	-6.10
Annual Values							
1998-99	113298	70699	1920	40942	62.40	1.70	36.10
1999-2000	103749	254554	1180	-152876	245.40	1.10	-147.40
2000-01	120874	89444	7505	25123	74.00	6.20	20.80

Relative share may not add up to 100 as the excess/shortfalls were adjusted in increase/decrease of the cash balances.

4.22 The Union Government's dependence on the three sources of financial accommodation for meeting the deficit has varied over the years. On a long term basis, about a fifth of the accommodation has come from public account. Internal debt accounted for 75 *per cent* of the overall accommodation for bridging the gap between revenue and expenditure of the Union government. External debt financed only 5 *per cent* of fiscal deficit. The comparison of the sources over the plans indicates that while the share of internal debt has increased; the dependence on Public Account funds has reduced. However, the year 1999-2000 was exceptional since accommodation from Public Account was negative, owing to creation of the NSSF. The accommodation further reached a level of 20.8 *per cent* in 2000-01.

Impact of NSSF on Fiscal Deficit

4.23 In 1999-2000, Union government constituted National Small Saving Fund (NSSF) for bringing in greater transparency in transactions relating to the small savings and public provident fund. With the constitution of this Fund, part of the net collections, which hitherto was passed through CFI, was routed through NSSF. This reduced the Union government's loans and advances. Further, interest on small savings and management costs were also a part of the revenue expenditure of the Union government. Though the Union government continues to pay the interest on the special securities issued in lieu of the net balances, the difference between the interest paid to the individual subscribers and the current interest liability represents under provision in this regard. This results in under estimation of the fiscal deficit of the Union government as indicated in Table 4.7:

Table 4.7: Impact of NSSF on Fiscal Deficit

		<i>(Rs in crore)</i>	
		1999-2000	2000-01
1	Opening Balance	176,221	973
2	Collections	75,435	88,468
3	Interest Receipt	20,265	24,877
4	Total additions	95,700	113,345
5	Repayment	36,864	43,111
6	Investment	212,137	41,581
	(a) Union Government Securities	<i>185,200</i>	<i>8,316</i>
	(b) State Government securities	<i>26,937</i>	<i>33,265</i>
7	Interest Paid	20,198	26,347
8	Management Cost	1,749	2,430
9	Total Outflow	270,948	113,469
10	Closing Balance	973	849
11	Impact on Fiscal Deficit (7-3)+6b+8	28,619	37,165
12	Fiscal deficit with NSSF	103749	120874
13	Total Fiscal Deficit would have been without NSSF (11 + 12)	132,368	158,039
14	Fiscal deficit as percentage to GDP	7.29	7.09

4.24 Reassessed fiscal deficit in 1999-2000 would climb up to 7.29 per cent of GDP. The revised fiscal deficit in 2000-01 would become 7.09 per cent of

GDP as against the earlier figure of 5.58 *per cent*. The under estimation of fiscal deficit in 2000-01 works out to be around 1.5 *per cent* of GDP. This would also impact on primary deficit by the same magnitude in absolute terms and also relative to GDP.

Primary Deficit

4.25 Table 4.8 indicates the ratio of primary deficit to GDP, non-debt receipts of the Union Government and revenue expenditure. Primary deficit/GDP ratio declined from an average of 5.02 *per cent* during 1985-90 to a level of 0.81 *per cent* in 2000-01. After an improvement in the primary deficit/GDP ratio in 1999-2000, there was a slippage in the current year.

Table 4.8: Primary deficit- Selected Ratios

(per cent)

Period/Year	GDP	Non-Debt Receipts	Revenue Expenditure
1985-2001	2.93	20.17	18.13
VII Plan (1985-90)	5.02	32.90	30.78
VIII Plan (1992-97)	1.96	14.35	12.39
IX Plan (1997-01)	1.46	10.96	9.04
Annual Values			
1998-99	2.02	15.13	12.85
1999-2000	0.47	3.41	2.90
2000-01	0.81	6.42	5.15

Non- Debt Receipts of the Union Government include – Revenue Receipts (net of the share of the States’ in Union taxes and the non-debt capital receipts.

4.26 Improvement in primary deficit would indicate a better outlook for the future, as the revenue receipts and non-debt capital receipts would cover current operations. However, in 2000-01, the primary deficit increased together with a decline in non-interest payments, which was a disturbing situation.