The Fuss around Fiscal Deficit

What is the issue?

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- The fragile nature of the Centre’s finances and its level of control over interest, pension and subsidy expenses are a cause of concern.
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- This article discusses the multiple facets and consequences felt due to budget deficits and burden of mounting government debt.
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How does the estimated deficits for FY-18 fare?

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- The estimated income for the FY18 fiscal from tax, non-tax revenues and capital items is Rs. 16.23 lakh crores.
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- But the expected expenditure is Rs. 22.17 lakh crores, which overshoots income by as much as 36.5%, and leaves a shortfall of Rs.5.94 lakh crores.
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- This shortfall when expressed as a percentage of GDP (which is around 167 lakh crores) is called fiscal deficit, which only displays a modest number.
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- Further, fiscal deficit counts both recurring revenue income and capital receipts (which are a one-time thing) as part of the government’s income.
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- Even if revenue items alone are counted, the Centre is still spending more than it earns, with revenue deficit of Rs. 4.39 lakh crore (FY18 estimate).
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Why are deficits bad?

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- When the Centre ends up spending more than it earns, it takes recourse to market borrowings to bridge the gap.
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- The borrowing target is closely watched by the bond market because the government's appetite for money might crowd out other borrowers.
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- Hence, companies, small businesses, and individuals would find it difficult to raise funds from India's relatively shallow financial/bond market.
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- Many years of such extravagant spending has resulted in the mounting of government's debt, which currently hit 82.32 lakh crores (49.3% of GDP).
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- Notably, this has grown form Rs. 57 lakh crore five years ago.
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- The only positive is that the bulk of those loans are from domestic sources, with just Rs. 2.4 lakh crore owed to foreign lenders.
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What is worrying about the budget allocation patterns?

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- While various schemes are highlighted in the budget speech, the bulk of the expenditure each year goes to - interest payments, pensions and subsidies.
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- In the FY18, interest payments (largest header) was expected to absorb Rs. 5.3 lakh crore, pensions Rs. 1.5 lakh crore and subsidies Rs. 2.3 lakh crore.
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- In short, servicing interest payouts alone will take up 32% of the Centre's earnings this year, while pensions and subsidies absorb another 23%.
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- With 23% allocated to State grants and 16% to defence expenditure, these repetitive expenses will effectively mop up 95% of the total Budget receipts.
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- These trends holds good across years and for all long-standing fiscal issues, leaving little room in the annual Budget for new schemes.
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- Another long-time issue is that the bulk of the Budget spending goes into maintenance expenses, and little remains for creation of new assets.
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- In FY18, just 12% of the budget was defrayed in capital spending.
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What is desired?

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- Fiscal Responsibility and Budget Management (FRBM) Act mandates the government to steadily tighten its fiscal and revenue deficits over the years.
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- It also envisions reining in its debt-GDP ratio by establishing a targeted outlay.
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- For the government to be really able to launch bold new schemes, it needs to clean up its finances first — pare down debt, save on interest payouts.
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- Reducing pensions and subsidies and raising asset creation are also important.
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- It is also important to ensure that receipts grow at a far faster pace than expenses in future, so that the debt can be paid down.
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- Therefore, the success or failure of the annual Budget exercise really has to be measured on the progress in these parameters over the years.
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How has the fiscal consolidation progressed since the NDA takeover?

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- Since 2o14, Centre's receipts have grown at a faster pace than its expenditure, which has helped the centre avoid a big bloat in the fiscal deficit.
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- While total receipts (excluding borrowings) have shot up by 50% in the last 4 years, the expenditure in the same period registered a slower 39% increase.
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- Further, spending on interest, pensions and subsidies rose by a much lower 30%, thus freeing up room for other expenditure.
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- Over the years, fiscal deficit as a percentage of GDP has come down from 4.5% to 3.5% in the current fiscal.
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- But all this thrift has made only a mild dent in the Centre's stockpile of debt, which has dipped merely from 50.4% to 49.3% of GDP over four years.
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- The progress achieved so far is hence miniscule and the government needs to persist ahead with fiscal prudence and resist populist temptations.
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Source: The Hindu

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