PUBLIC FINANCE

The fiscal year 1997-98 saw a major deterioration of the fiscal deficit of the central government from 4.5 per cent of gross domestic product (GDP) as per the budget estimates to an estimated 6.1 per cent of GDP as per the revised estimates. The slippage on the fiscal front was largely on account of major shortfalls in tax revenues and non-debt capital receipts from disinvestment. In particular, net tax revenues to the centre at Rs.99158 crore as per the revised estimates in 1997-98 were lower by 12.6 per cent (Rs.14236 crore) over the budget estimates. The shortfall in tax collections is mainly attributed to revenues from excise and customs, which were adversely affected by a slower growth in both industrial output and imports.

2. The 1997-98 budget reduced personal and corporate tax rates to internationally comparable levels. The budget slashed the top marginal personal income tax rate to 30 per cent (from 40 per cent); reduced corporate tax rates for domestic companies to 35 per cent (from 40 per cent) and on foreign firms to 48 per cent (from 55 per cent) along with the abolition of surcharge on corporate tax; lowered to 20 per cent (from 30 per cent) the tax rate on royalty and technical service fees payable to foreign companies; exempted export profits from the minimum alternate tax (MAT) and converted payment of MAT into a tax credit carried forward for five assessment years; and abolished tax on dividends. A modest beginning was also made to widen the tax base by stipulating that residents of large metropolitan cities who satisfy certain specified economic criteria must file their tax return. Another proposal with the same objective was the introduction of an estimated income scheme for retail traders. With a view to harness “black money” for productive purposes a new Voluntary Disclosure of Income Scheme (VDIS) was introduced, which netted tax collections estimated at Rs. 10050 crore.

3. On the import duty side, the budget signalled the Government’s resolve to achieve the average level of tariffs prevalent in ASEAN countries by the turn of the century. To this end, peak level of customs duties was lowered from 50 per cent to 40 per cent. Simultaneously customs duties were brought down to much lower levels on a large number of inputs, raw materials and intermediates to make domestic production more competitive in power, chemicals, textiles and information technology. Besides, duty on capital goods was further reduced from 25 per cent to 20 per cent. On the excise front, duty changes were effected with a view to reduce dispersion in rates. Also the scheme of excise duty concession for the small-scale units was radically simplified. The ambit of service tax was widened to cover a number of services like transportation of goods by road, consulting engineers, steamer/ shipping agents, air travel agents etc.

Fiscal and Budgetary Developments in 1997-98

4. The process of fiscal correction received a serious setback during 1997-98 when fiscal deficit as a proportion of GDP increased to 6.1 per cent as per the revised estimates from 4.5 per cent as per the budget estimates (Table 2.1). Concomitantly, the primary deficit defined as gross fiscal deficit minus interest payments also worsened. Primary deficit for 1997-98 as a proportion of GDP (as per the revised estimates) is placed at 1.5 per cent as against a marginal budgeted surplus of (-) 0.2 per cent. Primary deficit essentially reflects the gap in resources on account of current policies of the government both on the revenue and expenditure side. For the year 1996-97, the actual fiscal deficit as a proportion of GDP has turned out to be 5.2 per cent as against 5 per cent envisaged in the budget and revised estimates respectively. Table 2.2 provides a snap view of the trajectory of various components of gross fiscal deficit of the central government in recent years.

5. The revised estimates for 1997-98 reflect serious deterioration on the fiscal front. On the revenue side, the most important cause of deterioration is major shortfalls in tax collections and disinvestment receipts. Net tax revenues for the centre are estimated at only Rs.99158 crore, showing a drop of Rs.14236 crore (12.6 per cent) primarily due to serious shortfalls in customs revenue by 22 per cent (Rs11550 crore) vis-à-vis budget estimates on account of

both lower volume and lower unit price of imports. The decline in revenue from union excise resulted from unusually low industrial growth. Receipts from PSU disinvestment are estimated to fall short of the budget estimates of Rs.4800 crore by Rs.3893 crore. However, the revised estimates for total expenditure are expected to exceed the budget estimates by only Rs. 3069 crore. This is less than the additional expenditure of Rs.4432 crore incurred on account of the single item of loans to states and union territories against small savings collections, which have been exceptionally buoyant during 1997-98. The net result of these factors has been a sharp deterioration of the gross fiscal deficit from the budget target of 4.5 per cent of GDP to 6.1 per cent during 1997-98 (RE). However, if the increase in expenditure

TABLE 2.1

Receipts and Expenditure of the Central Government

		1980-81	1990-91	1991-92	1994-95	1995-96	1996-97	1997-98 (BE)	1997-98 (RE)
					(Rs. crore)				
1.	**Revenue Receipts (2+3)**	**12419**	**54954**	**66031**	**91083**	**110130**	**126279**	**153143**	**138514**
2.	**Tax Revenue**	**9358**	**42978**	**50069**	**67454**	**81939**	**93701**	**113394**	**99158**
	(net of State's share)								
3.	**Non-Tax Revenue**	**3061**	**11976**	**15962**	**23629**	**28191**	**32578**	**39749**	**39356**
4.	**Revenue Expenditure**	**14455**	**73516**	**82292**	**122112**	**139861**	**158934**	**183408**	**182200**
	of which								
	(a) Interest Payments	2604	21498	26596	44060	50045	59478	68000	65700
	(b) Subsidies	1851	12158	12253	12932	13372	16125	18251	19644
	(c) Defence Expenditure	3604	10874	11442	16426	18841	20997	26713	26802
5.	**Revenue Deficit**	**2037**	**18562**	**16261**	**31029**	**29731**	**32655**	**30265**	**43686**
6.	**Capital Receipts**	**7261**	**38997**	**38528**	**68695**	**58338**	**61544**	**79033**	**96731**
	of which								
	(a) Recovery of Loans	2104	5712	6021	6345	6505	7540	8779	9479
	(b) Other Receipts			3038	5607	1397	455	4800	907
	(mainly PSU disinvestment)								
7.	**Capital Expenditure**	**7801**	**31782**	**29123**	**38627**	**38414**	**42073**	**48768**	**53045**
8.	**Total Expenditure**	**22256**	**105298**	**111415**	**160739**	**178275**	**201007**	**232176**	**235245**
	of which								
	(a) Plan Expenditure	8994	28365	30961	47378	46374	53534	62852	60630
	(b) Non-plan Expenditure	13262	76933	80454	113361	131901	147473	169324	174615
9.	**Fiscal Deficit**	**7733**	**44632**	**36325**	**57704**	**60243**	**66733**	**65454**	**86345**
					(As per cent of GDP)				
1.	**Revenue Receipts (2+3)**	**9.1**	**10.3**	**10.7**	**9.5**	**9.8**	**9.9**	**10.6**	**9.8**
2.	**Tax Revenue**	**6.9**	**8.0**	**8.1**	**7.0**	**7.3**	**7.3**	**7.9**	**7.0**
	(net of State's share)								
3.	**Non-Tax Revenue**	**2.3**	**2.2**	**2.6**	**2.5**	**2.5**	**2.6**	**2.8**	**2.8**
4.	**Revenue Expenditure**	**10.6**	**13.7**	**13.3**	**12.7**	**12.5**	**12.4**	**12.7**	**12.9**
	of which								
	(a) Interest Payments	1.9	4.0	4.3	4.6	4.5	4.7	4.7	4.6
	(b) Subsidies	1.4	2.3	2.0	1.3	1.2	1.3	1.3	1.4
	(c) Defence Expenditure	2.6	2.0	1.9	1.7	1.7	1.6	1.9	1.9
5.	**Revenue Deficit**	**1.5**	**3.5**	**2.6**	**3.2**	**2.7**	**2.6**	**2.1**	**3.1**
6.	**Capital Receipts**	**5.3**	**7.3**	**6.2**	**7.1**	**5.2**	**4.8**	**5.5**	**6.8**
	of which								
	(a) Recovery of Loans	1.5	1.1	1.0	0.7	0.6	0.6	0.6	0.7
	(b) Other Receipts	0.0	0.0	0.5	0.6	0.1	0.0	0.3	0.1
	(mainly PSU disinvestment)								
7.	**Capital Expenditure**	**5.7**	**5.9**	**4.7**	**4.0**	**3.4**	**3.3**	**3.4**	**3.7**
8.	**Total Expenditure**	**16.4**	**19.7**	**18.1**	**16.7**	**15.9**	**15.7**	**16.1**	**16.6**
	of which								
	(a) Plan Expenditure	6.6	5.3	5.0	4.9	4.1	4.2	4.4	4.3
	(b) Non-plan Expenditure	9.8	14.4	13.0	11.8	11.8	11.5	11.8	12.3
9.	**Fiscal Deficit**	**5.7**	**8.3**	**5.9**	**6.0**	**5.4**	**5.2**	**4.5**	**6.1**

Note: The figures may not add up to the total because of rounding approximations.

TABLE 2.2

Components of Gross Fiscal Deficit of the Central Government

	1980-81	1990-91	1991-92	1994-95	1995-96	1996-97	1997-98 (B.E.)	1997-98 (R.E.)
				(Rs. crore)				
1. Fiscal Deficit	**7733**	**44632**	**36325**	**57704**	**60243**	**66733**	**65454**	**86345**
1.1. Interest Payments	2604	21498	26596	44060	50045	59478	68000	65700
1.2. Primary Deficit	**5129**	**23134**	**9729**	**13644**	**10198**	**7255**	**-2546**	**20645**
1.21 Primary Deficit Consumption	1310	6358	1306	3982	-147	-2363	-10130	6675
1.22 Primary Deficit Investment	3819	16776	8423	9662	10345	9618	7584	13970
				(As per cent of GDP)				
1. Fiscal Deficit	**5.7**	**8.3**	**5.9**	**6.0**	**5.4**	**5.2**	**4.5**	**6.1**
1.1. Interest Payments	1.9	4.0	4.3	4.6	4.5	4.7	4.7	4.6
1.2. Primary Deficit	**3.8**	**4.3**	**1.6**	**1.4**	**0.9**	**0.6**	**-0.2**	**1.5**
1.21 Primary Deficit Consumption	1.0	1.2	0.2	0.4	-0.0	-0.2	-0.7	0.5
1.22 Primary Deficit Investment	2.8	3.1	1.4	1.0	0.9	0.8	0.5	1.0
Memorandum Items								
(a) Interest Receipts	1795	8730	10933	15797	18419	22106	24092	25327
(b) Dividend and Profit	82	564	708	1216	1748	2354	3513	3362

Note: 1. Primary deficit consumption =Revenue Deficit-interest payments+interest receipts+dividend & profits
2. Primary deficit investment =Capital expenditure-interest receipts -Dividend & profit-recovery of loans-other receipts

attributable to small savings loans were excluded, the fiscal deficit would be lower at 5.8 per cent of GDP in 1997-98(RE).

6. The interim budget for 1998-99 has devolved to the States 77.5 per cent of the revenue from VDIS collections estimated at Rs.10050 crore for the full year 1997-98 as against the earlier decision to devolve 77.5 per cent of the collections upto the end of December 1997. As a consequence, the States will receive an additional Rs.3215 crore, thus taking the total devolution on this account to Rs.7594 crore during 1997-98. Besides the interim budget has provided for an additional sum of Rs.1000 crore by way of additional central assistance to States on account of externally aided projects in order to settle all pending claims in the financial year 1997-98. Taken together, these two decisions have given to the States an additional sum of Rs. 8594 crore in 1997-98.

7. In contrast to a cutback in central plan outlay in 1996-97, the 1997-98 (RE) outlay at Rs.81034 crore, although lower compared with 1997-98 (BE) at Rs.91838 crore was 5.7 per cent of GDP and reflected an increase of 4.5 per cent over the 1996-97 (RE) level. This modest expansion in the plan outlay has been solely contributed by an increase of 11.7 per cent in the budget support.

Performance of fiscal parameters in 1997-98

8. The gross fiscal deficit is defined as the difference between, the revenue receipts (net) plus non-debt capital receipts and the total expenditure including loans net of repayments. This is a measure, which captures the entire shortfall in the non-debt resources for financing the plan and non-plan activities/schemes of the central government. As per the revised estimates for 1997-98, the size of the gross fiscal deficit at Rs.86345 crore exceeded the budgeted amount by about 32 per cent. Primary deficit, which was budgeted to show a surplus of Rs.2546

TABLE 2.3
Central Government Finances

(Rs. crore)

	April-March			Percentage Change	
	1996-97	1997-98(BE)	1997-98(RE)	Col. 4/3	Col. 4/2
1	2	3	4	5	6
1. Revenue Receipts	**126279**	**153143**	**138514**	**-9.6**	**9.7**
2. Tax (net to Centre)	**93701**	**113394**	**99158***	**-12.6**	**5.8**
of which					
(a) CIT	18567	21860	21360	-2.3	15.0
(b) PIT	4715	6009	5178	-13.8	9.8
(c) Customs	42851	52550	41000	-22.0	-4.3
(d) Excise	23463	27637	25254	-8.6	7.6
3. Non Tax	**32578**	**39749**	**39356**	**-1.0**	**20.8**
4. Capital Receipts	**7995**	**13579**	**10386**	**-23.5**	**29.9**
of which					
(a) Recovery of loans	7540	8779	9479	8.0	25.7
(b) Other Receipts	455	4800	907	-81.1	99.3
5. Total Receipts	**134274**	**166722**	**148900**	**-10.7**	**10.9**
6. Non Plan Expenditure	**147473**	**169324**	**174615**	**3.1**	**18.4**
7. Revenue Account	**127299**	**145854**	**146080**	**0.2**	**14.8**
of which					
(a) Interest payments	59478	68000	65700	-3.4	10.5
(b) Subsidies	16125	18251	19644	7.6	21.8
(c) Defence	20997	26713	26802	0.3	27.6
(d) Pensions	5077	5251	6883	31.1	35.6
8. Capital Account	**20174**	**23470**	**28535**	**21.6**	**41.4**
9. Plan Expenditure	**53534**	**62852**	**60630**	**-3.5**	**13.3**
(a) Revenue Account	31635	37554	36120	-3.8	14.2
(b) Capital Account	21899	25298	24510	-3.1	11.9
10. Total Expenditure	**201007**	**232176**	**235245**	**1.3**	**17.0**
(a) Revenue Expenditure	158934	183408	182200	-0.7	14.6
(b) Capital Expenditure	42073	48768	53045	8.8	26.1
11. Revenue Deficit	**32654**	**30265**	**43686**	**44.3**	**33.8**
12. Fiscal Deficit	**66733**	**65454**	**86345**	**31.9**	**29.4**
13. Primary Deficit	**7255**	**-2546**	**20645**	**-**	**184.6**

1. Fiscal deficit: Total expenditure + Suspense & Remittances-Revenue Receipts - Non debt creating capital Receipts
*** Includes VDIS collections of Rs. 2456 crore.**

crore, has posted a huge deficit of the order Rs. 20645 crore in 1997-98(RE).

9. Table 2.3 provides a snap view of major fiscal parameters pertaining to the central government finances for 1996-97 and revised and budget estimates for 1997-98. As is evident from this table the fiscal deficit got exacerbated on account of substantial slippage on the receipts side.

Measure for Cash Management: Ways and Means Advances

10. The system of ad-hoc treasury bills as a means of financing the budget deficit was discontinued. With effect from April 1,1997, this system has been replaced by a system of ways and means advances (WMA). Under the new arrangement, the temporary accommodation by way of WMA for meeting temporary mismatches between expenditure and receipts will be outside the Reserve Bank's support to the government's borrowing programme during the year. The size and cost of WMA would be determined on the basis of mutual agreement between the Reserve Bank and the Government of India. Amounts drawn beyond the WMA limit would be treated as overdraft. The limit of WMA for the first six months (April-September) of the fiscal year 1997-98 was fixed at Rs. 12000 crore and for the subsequent six months (October-March) of the year at Rs. 8000 crore. The above development imparts a new dimension to the concept of deficit in that the conventional budget deficit which comprised changes in ad-hoc treasury bills net of changes in cash balances has been rendered redundant. Therefore, the concept of gross fiscal deficit becomes the key measure of deficit. On the other hand, the monetised deficit, which mainly captures changes in the Reserve Bank's holding of dated securities and auctioned treasury bills, would reflect monetary impact of the government's fiscal operations in a transparent way. Although the budget has estimated a monetised deficit of Rs. 16000 crore during 1997-98, representing the *exante* level

of Reserve Bank's support to central government market borrowings, the actual out-turn at the close of the year could be different on account of the open market operations that the Reserve Bank would undertake during the course of the year depending on the evolving monetary situation.

11. The WMA is intended to strengthen fiscal discipline, while providing greater autonomy to the RBI in its conduct of monetary policy. This would make monetary impact of fiscal operations transparent and facilitate the process of fiscal consolidation. A clear cut WMA limit during the course of the year would put a cap on the automatic monetisation of the fiscal deficit and create conducive macro economic environment for setting a "monetary target". Besides, dismantling of ad-hoc treasury bills also entails a shift in the composition of financing of fiscal deficit towards market borrowing. However, from the operational point of view, the new arrangement of WMA would necessitate improvement in cash management by the central government as well as debt management by the Reserve bank, so as to keep the cash deficit within the limits of WMA for the year.

Government Debt

12. The process of fiscal correction over the last few years has had a moderating influence on the accumulation of aggregate internal liabilities of the central government. These are budgeted to increase to Rs.718299 crore in 1997-98 (RE) from Rs.621438 crore in 1996-97 (Table 2.4). This shows an increase in the growth of internal liabilities from 12 per cent in 1996-97 to 15.6 per cent in 1997-98 (RE). Reflecting this trend, aggregate internal liabilities as a proportion of GDP increased from 48.7 per cent in 1996-97 to 50.8 per cent in 1997-98(RE). This increase is mainly contributed both by market borrowings and "other internal liabilities".

13. External liabilities estimated in the budget are at the historical rates of exchange. External liabilities at book value increased from Rs.54238 crore in 1996-97 to Rs.55242 crore in 1997-98(RE). At historical rates, the ratio of external debt stock to GDP has been on downward slide for many years. The repayment burden of the debt stock is better reflected by valuing the debt stock at exchange rates at the end of the relevant fiscal year. When this is done, external liabilities as a proportion of GDP turns out to be much higher, although the ratio has shown a declining trend since 1991-92.

14. In the context of increasing government liabilities over time and the need to strengthen fiscal prudence, the issue of fixing limits on public debt had come up for consideration on several occasions in the past. Some of the important issues are summarised in Box 2.1.

Interest Payments

15. Interest payment is the largest single item of government expenditure (Table 2.5). Gross interest payments in 1997-98, which were budgeted at Rs.68000 crore are now placed at Rs.65700 crore as per the revised estimate for 1997-98. These payments are estimated to absorb 47.4 per cent of total revenue receipts in 1997-98 (RE) compared with a similar ratio of 47.1 per cent in 1996-97. As a proportion of GDP, interest payments have hovered between 4.5 to 4.7 per cent of GDP between the years 1995-96 and 1997-98 (RE). Strategy to restrain the growth of borrowing and subsequent interest outgo will have significant impact on total expenditure.

Subsidies

16. Aggregate explicit subsidies provided in the central government budget are estimated to grow by 21.8 per cent from Rs.16125 crore in 1996-97 to Rs.19644 crore in 1997-98(RE). Subsidy on food and fertiliser accounted for an overwhelming share of more than three-fourths of the total expenditure on subsidies in 1997-98 (RE). The relative importance of different explicit subsidies provided in the budget has changed over the years. For example, food subsidies accounted for about 70 per cent of total subsidies in 1974-75. The relative share of export subsidies has been on the decline except for a spurt in the late eighties and early nineties. Since 1983-84, fertiliser subsidies have been the largest among the explicit subsidies except in 1986-87, 1993-94, 1996-97 and 1997-98. The total explicit subsidies of the central government have galloped from Rs.140 crore in 1971-72 to Rs.19644 crore in 1997-98 (RE). This represents an annual growth of around 19 per cent.

17. Although the aggregate size of explicit subsidies provided in the budget have increased during the nineties, its relative size measured in

TABLE 2.4

Outstanding Liabilities of the Central Government

At the end of :

		1980-81	1990-91	1991-92	1994-95	1995-96	1996-97	1997-98 (BE)	1997-98 (RE)
					(Rs.crore)				
1.	**Internal liabilities**	**48451**	**283033**	**317714**	**487682**	**554984**	**621438**	**677615**	**718299**
	a) Internal Debt	30864	154004	172750	266467	307869	344476	368077	385694
	i) Market borrowings	15676	70565	78075	131007	164094	184101	217904	217626
	ii) Others	15188	83439	94675	135460	143775	160375	150173	168068
	b) Other Internal liabilities	17587	129029	144964	221215	247115	276962	309538	332605
2.	**External debt(outstanding)***	**11298**	**31525**	**36948**	**50929**	**51249**	**54238**	**56001**	**55242**
3.	**Total outstanding liabilities (1+2)**	**59749**	**314558**	**354662**	**538611**	**606233**	**675676**	**733616**	**773541**
4.	Amount due from Pakistan on account of share of pre-partition debt	300	300	300	300	300	300	300	300
5.	**Net liabilities (3-4)**	**59449**	**314258**	**354362**	**538311**	**605933**	**675376**	**733316**	**773241**
					(As per cent of GDP)				
1.	**Internal liabilities**	**35.6**	**52.9**	**51.5**	**50.6**	**49.6**	**48.7**	**47.0**	**50.8**
	a) Internal Debt	22.7	28.8	28.0	27.7	27.5	27.0	25.6	27.3
	i) Market borrowings	11.5	13.2	12.7	13.6	14.7	14.4	15.1	15.4
	ii) Others	11.2	15.6	15.3	14.1	12.8	12.6	10.4	11.9
	b) Other Internal liabilities	12.9	24.1	23.5	23.0	22.1	21.7	21.5	23.5
2.	**External debt(outstanding)***	**8.3**	**5.9**	**6.0**	**5.3**	**4.6**	**4.2**	**3.9**	**3.9**
3.	**Total outstanding liabilities**	**43.9**	**58.7**	**57.5**	**55.9**	**54.2**	**52.9**	**50.9**	**54.7**
	Memorandum items								
	External Debt (Rs.crore)@	13479	66320	109685	142514	148398	149564	151999	150765
	(as per cent of GDP)	9.9	12.4	17.8	14.8	13.3	11.7	10.6	10.7
	Total outstanding liabilities(adjusted)	61930	349353	427399	630196	703382	771002	829614	869064
	(as per cent of GDP)	45.5	65.2	69.3	65.4	62.9	60.4	57.6	61.4
	Outstanding liabilities (Non-RBI)# (Rs.crore)	48495	275298	346512	525823	592532	651228	709840	749290
	Outstanding liabilities (Non-RBI) (as per cent of GDP)	35.7	51.4	56.2	54.6	53.0	51.0	49.3	53.0

*** External debt figures represent borrowings by Central Government from external sources and are based upon historical rates of exchange.**

@ Converted at current year end exchange rates. For 1980-81, the rates prevailing at the end of March, 1981. For 1993-94, the rates prevailing at the end of March, 1994 and so on.

 # This includes marketable dated securties held by the RBI

TABLE 2.5

Interest on the Outstanding Liabilities of Central Government

		1980-81	1990-91	1991-92	1994-95	1995-96	1996-97	1997-98 (BE)	1997-98 (RE)
						(Rs.crore)			
1.	**Interest on internal liabilities**	**2373**	**19664**	**23892**	**40034**	**45631**	**55255**	**63254**	**61550**
	a) Internal debt	1369	9814	11317	19168	22179	27233	31585	31459
	i) Market borrowings	808	6366	7355	13205	15400	19125	22824	22189
	ii) Others	561	3448	3962	5963	6779	8108	8761	9270
	b) Other internal liabilities	1004	9850	12575	20866	23452	28022	31669	30091
2.	**Interest on external debt**	**231**	**1834**	**2704**	**4026**	**4414**	**4223**	**4746**	**4150**
3.	**Gross interest payments**	**2604**	**21498**	**26596**	**44060**	**50045**	**59478**	**68000**	**65700**
4.	**Net interest payments**	**809**	**12768**	**15663**	**28263**	**31625**	**37372**	**43908**	**40373**
					(Average rate of interest)				
1.	**Internal liabilities**	**N.A.**	**8.2**	**8.4**	**9.3**	**9.4**	**10.0**	**10.2**	**9.9**
	a) Internal debt	N.A.	7.4	7.3	7.8	8.3	8.8	9.2	9.1
	i) Market borrowings	N.A.	10.2	10.4	11.9	11.8	11.7	12.4	12.1
	ii) Others	N.A.	4.9	4.7	4.4	5.0	5.6	5.5	5.8
	b) Other Internal liabilities	N.A.	9.2	9.7	11.3	10.6	11.3	11.4	10.9
2.	**External debt**	**N.A.**	**6.5**	**8.6**	**8.5**	**8.7**	**8.2**	**8.8**	**7.7**
3.	**Total liabilities**	**N.A.**	**8.0**	**8.5**	**9.2**	**9.3**	**9.8**	**10.1**	**9.7**
	Memorandum items								
	(a) Interest on External Debt	252	1863	2763	4035	4414	4223	4746	4150
	(b) Average rate of interest	N.A.	3.4	4.2	3.2	3.1	2.8	3.2	2.8
	(c) Gross interest payments (as per cent of Revenue Receipts)	21.0	39.1	40.3	48.4	45.4	47.1	44.4	47.4

Note : The interest liabilities indicated above are on cash basis and not on accrual basis.

BOX 2.1

Public Debt

- As per the current Indian budgetary practice there are three sets of liabilities which constitute central government public debt viz. (a) internal debt, (b) external debt, and (c) "other liabilities". Internal debt and external debt constitute public debt of India and are secured under the Consolidated Fund of India. The Indian Constitution under Article 292 provides for placing a limit on public debt secured under the Consolidated Fund of India but precludes "other liabilities" under Public Account. There is also a similar provision under Article 293 of the Indian Constitution in respect of borrowings by States, wherein the State legislature has powers to fix limits on State borrowings upon the security of the Consolidated Fund of the State. However, a State's power to borrow is limited to internal debt and a State is required to obtain prior consent of the government of India, as long as the State has outstanding loans made by the government of India.

- Internal debt includes market loans, special securities issued to Reserve Bank of India (RBI), compensation and other bonds, treasury bills issued to RBI, State governments, commercial banks and other parties, as well as non-negotiable and non-interest bearing rupee securities issued to international financial institutions. The internal debt is classified into market loans, other long and medium term borrowing and short term borrowing and shown in the receipts budget of union government. External debt represents loans received from foreign governments and bodies. The liabilities other than internal and external debts includes other interest bearing obligations of the government such as post office savings deposits, deposits under small savings schemes, loans raised through post office cash certificates etc., provident funds, interest bearing reserve funds of departments like railways and telecommunications and certain other deposits.

- The "other liabilities" of government arise in government's accounts more in its capacity as a banker rather than as a borrower. Hence, such borrowings, not secured under the Consolidated Fund of India, are shown as part of public account. Furthermore, some of the items of "other liabilities" like small savings are more in the nature of autonomous flows, which to a large extent are determined by public preference, and relative attractiveness of these instruments. Nevertheless, it should be emphasised that all liabilities are obligations of the government.

- Total internal liabilities of the central government as proportion of GDP has been in the range of about 51 per cent in 1997-98 (RE) to around 53 per cent in 1990-91 during the nineties (Table 2.4). There are some important questions, which need to be addressed before fixing a limit on public debt: Should this limit be fixed in terms of a legislative ceiling on public debt? What should be the ambit of public debt? Should the limit be confined to "public debt" or include "other liabilities" of the Government also? Should the limit be fixed in absolute terms or as a proportion of GDP? What is the sustainable level of public debt and what is the rationale for choosing a particular limit for the Indian economy? Whether the limit on public debt should be fixed on a year-on-year or for a medium term/long term or permanent basis ?

relation to GDP, revenue expenditure and total revenue receipts have declined over the same period. Total explicit budgetary subsidies absorbed 22.1 per cent of revenue receipts (tax plus non tax) in 1990-91. However, this ratio declined to 12.8 per cent in 1996-97 and has edged up to 14.2 per cent as per the revised estimates for 1997-98. Concomitantly, the share of subsidies in the total revenue expenditure fell from 16.5 per cent in 1990-91 to 10.8 per cent in 1997-98(RE). Also explicit budgetary subsidies as a proportion of GDP has fallen from 2.3 per cent in 1990-91 to around 1.4 per cent in 1997-98(RE).

Savings and Capital Formation

18. As per the economic and functional classification of the union budget, the total expenditure of the central government in 1997-98 (BE) is budgeted to increase to Rs.243195 crore from Rs.213931 crore in 1996-97 (RE) (Table 2.6). This reveals moderation in the growth of total central government expenditure from 15.5 per cent posted in 1996-97(RE) to 13.7 per cent in 1997-98(BE). This has also led to a marginal increase in total expenditure to GDP ratio to 16.9 per cent in 1997-98 (BE) from 16.8 per cent in 1996-97 (RE).

19. Gross dis-savings of the central government shrank to Rs.7380 crore in 1996-97(RE) from Rs.9835 crore recorded in 1995-96. However, gross dis-savings are budgeted to expand to Rs.8572 crore in 1997-98 after showing a decline in the previous year. This

BOX 2.2

Government Subsidies in India

- The Government of India released the discussion paper entitled "Government Subsidies in India" with the intent to generate an informed debate and initiate a more open approach to subsidies. This paper is based on a detailed research study by the National Institute of Public Finance and Policy. The paper has provided a comprehensive estimate of budget based subsidies in which both explicit and implicit subsidies are covered. In this paper subsidies are computed as the excess of costs over receipts. The study quantifies aggregate government subsidies, their distribution across services (economic and social), merit and non-merit categories, and service wise recovery rates for the year 1994-95. The study excludes from its purview certain services like defence, administration, etc. These services are treated as "public goods". These are the goods whose benefits are individually spread among the entire community, whether or not the individuals desire to purchase the public good. The entitlement to these services is common to all citizens.

- The study estimates subsidies as follows. First, estimation of subsidies for the central government was done for the year 1994-95. Second, fifteen major states were considered for estimation of state government subsidies based on the data for the year 1993-94. These estimates were then "blown up" for all the states and projected forward for 1994-95. Finally, central and state subsidies for the same year were brought together.

- In this paper a distinction is made between "merit" and "non-merit" subsidies based on the perceived significant externalities associated with merit goods/services. This also provides a rationale for providing the appropriate degree of subsidisation to a Good/Service falling in the merit category. It may also be noted that in a very few cases, such as food, subsidies may be justified on grounds other than "externalities", such as on grounds of income distribution or meeting minimum needs.

- The study brings to the fore the massive magnitude of subsidies (un-recovered costs) in the provision of economic and social services by the government. The aggregate level of subsidy in 1994-95 for all services provided by the central and state governments is placed at Rs. 137338 crore and constituted 14.4 per cent of GDP. This includes central and state subsidy amounting to Rs.43048 crore and Rs.94290 crore respectively. Further central subsidy on social and economic services excluding those on identified merit goods were Rs.36125 crore, which is 3.8 per cent of GDP. Subsidies by the central government on "merit" goods account for Rs.6923 crore and formed less than 1 per cent of GDP. Even if "merit" subsidies are set aside, the remaining ("non-merit") subsidies alone amount to 10.7 per cent of GDP, comprising 3.8 per cent and 6.9 per cent of GDP, pertaining to central and state subsidies, respectively. The average all-India recovery rate for these non-merit subsidies is just 10.3 per cent, implying a subsidy rate of almost 90 per cent.

- The key to reducing the scale of subsidies is through phased increases in user charges. The current recovery rates, even for non-merit services, are extremely low, just over 10 per cent for all-India, with a slightly higher rate of 12.1 per cent for the central government and only 9.3 per cent for states. Another way of putting this is that the subsidy rate for non-merit services for centre and states combined is nearly 90 per cent. If this rate of subsidy could be brought down to 50 per cent, then subsidies on non-merit goods/services would drop from 10.7 per cent of GDP to about 6.0 per cent of GDP, that is a decline of 4.7 per cent points of GDP. This shows the enormous scope for fiscal correction through a more effective strategy of cost recovery through user charges for non-merit goods/services.

- The discussion paper points out that there exists considerable scope for improving our present regime of subsidies by focusing on : reducing the overall scale of subsidies; making subsidies as transparent as possible; using subsidies for well-defined economic objectives; focusing subsidies to final goods and services with a view to maximising their impact on the target population at minimum cost; instituting systems for periodic review of subsidies and; setting clear limits on duration of any new subsidy schemes.

TABLE 2.6

Total Expenditure and Capital Formation by the Central Government and its Financing

		1980-81	1990-91	1991-92	1993-94	1994-95	1995-96	1996-97 (RE)	1997-98 (BE)
						(Rs.Crore)			
I,	**Total expenditure**	**22495**	**104973**	**112731**	**145788**	**166998**	**185233**	**213931**	**243195**
II.	Gross capital formation out of budgetary resources of Central Government :	9012	35058	35165	45051	54200	55276	62012	69208
	(i) Gross capital formation by the Central Government	1907	8602	9259	12765	14328	16685	18822	21951
	(ii) Financial assistance for capital formation in the rest of the economy	7105	26456	25906	32286	39872	38591	43190	47257
III.	Gross saving of the Central Government	3	-10502	-7802	-20335	-13882	-9835	-7380	-8572
IV.	**Gap(II-III)**	**9009**	**45560**	**42967**	**65386**	**68082**	**65111**	**69392**	**77780**
	Financed by :								
a.	Draft on other sectors of domestic economy	7339	41794	36599	59319	63463	63655	65604	74246
	(i) Domestic capital receipts	4762	30447	29744	48359	62502	53848	58704	74246
	(ii) Budgetary deficit	2577	11347	6855	10960	961	9807	6900	0
b.	Draft on foreign savings	1670	3766	6368	6067	4619	1456	3788	3534
						(As per cent of GDP)			
I.	**Total Expenditure**	**16.5**	**19.6**	**18.3**	**18.0**	**17.3**	**16.6**	**16.8**	**16.9**
II.	Gross capital formation out of budgetary resources of Central Government :	6.6	6.5	5.7	5.6	5.6	4.9	4.9	4.8
	(i) Gross capital formation by the Central Government	1.4	1.6	1.5	1.6	1.5	1.5	1.5	1.5
	(ii) Financial assistance for capital formation in the rest of the economy	5.2	4.9	4.2	4.0	4.1	3.4	3.4	3.3
III.	Gross saving of the Central Government	0.0	-2.0	-1.3	-2.5	-1.4	-0.9	-0.6	-0.6
IV.	**Gap(II-III)**	**6.6**	**8.5**	**7.0**	**8.1**	**7.1**	**5.8**	**5.4**	**5.4**
	Financed by :								
a	Draft on other sectors of domestic economy	5.4	7.8	5.9	7.3	6.6	5.7	5.1	5.2
	(i) Domestic capital receipts	3.5	5.7	4.8	6.0	6.5	4.8	4.6	5.2
	(ii) Budgetary deficit	1.9	2.1	1.1	1.4	0.1	0.9	0.5	0.0
b.	Draft on foreign savings	1.2	0.7	1.0	0.7	0.5	0.1	0.3	0.2
II.	Gross capital formation out of budgetary resources of Central Government (increase over previous year)	24.7	6.2	0.3	19.7	20.3	2.0	12.2	11.6

Notes: **(i) Gross capital formation in this table includes loans given for capital formation on a gross basis. Consequently domestic capital receipts include loan repayments to the Central Government.**
(ii) Because of the revision in the series of GDP ,the ratios given here may differ from those given in the earlier issues of Economic Survey.
(iii)Total expenditure as per Economic and Functional classification of Central Government Budget.

estimated deterioration in dis-savings by Rs.1192 crore in 1997-98 (BE) has been largely contributed by dis-savings on account of government administration.

20. Gross capital formation out of budgetary resources (physical plus financial investment of centre) after remaining stagnant at 4.9 per cent of GDP during 1995-96 and 1996-97 (RE) is estimated to decline marginally to 4.8 per cent of GDP in 1997-98 (BE). This erosion is mainly the result of a lower growth in financial assets. Gross capital formation in physical assets is estimated to grow by 16.6 per cent compared to a lower growth of 9.4 per cent in financial assets during 1997-98.