HIGHLIGHTS OF THE
UNION GOVERNMENT FINANCES AND ACCOUNTS: 1999-00

Union Finances: Overall Assessment

- Union finances have become less adequate, less autonomous, and more vulnerable during the nineties. Voted expenditure as proportion of total disbursement has fallen from 44.51 percent in 1992-93 to 31.94 percent in 1997-98. Therefore, there is less autonomy for applying available resources for current applications. Although by 1999-00, this ratio recovered to 35.68 percent, it still shows that the degree for autonomy in the application of resources is low, and has fallen over the ten-year period in the nineties. This view is further supported by the fact that repayment as percentage of borrowing has increased from 72.73 percent in 1990-91 to 86.74 percent in 1999-00 indicating that only about 13 percent of current borrowing is usable for current services. The interest ratio has also increased from 25.47 to 33.60 percent, showing increasing loss of autonomy in using current resources for current applications. Central finances are also more vulnerable now than before. Revenue deficit as percentage of fiscal deficit has increased from 40.40 in 1990-91 to 59.43 in 1999-00, exhibiting an increase of about 20 percentage points. To the extent fiscal deficit is not used for creating assets, finances become vulnerable because liabilities are being added without addition to the capacity for repayments.

Union Government Accounts: New Arrangements

- The 1999-00 summarised accounts of the Union government show a reversal of the relative position of the Consolidated Fund of India (CFI) and the public account. The CFI, which until 1998-99 used to end with a deficit, emerged with a surplus of Rs. 151986 crore at the end of 1999-00; and, the public account, which used to remain in surplus, ended with a deficit of Rs.152876 crore. The establishment of National Small Savings Fund (NSSF), with effect from 01 April 1999, led to this change. It occurred because beginning 1999-00, the government has begun to formally borrow small savings from the NSSF, by issuing securities. As internal debt, this borrowing went into the CFI, unlike the past when the government used net surplus in public account to meet its deficit as a matter of course. In the new arrangement, the government has started the management of small savings and the mechanics of their transfers to the states through the NSSF.

The Macro Economy in 1999-00: Salient Features

- At the macroeconomic level, 1999-00 offered little comfort. The growth of the GDP was lower than its peak in mid nineties. The public sector savings remained negative for the second year running. There was a fall in the growth of money supply that was coincident with lower inflation.

- The economy has been undergoing significant structural change. The services sector has not only shown the highest trend growth rate (TGR) but also less fluctuation in the growth rates as compared to the other sectors. As a result of differential growth rates between the three major sectors, the services sector now constitutes about 53 percent of the GDP. The agriculture sector has a share of about 25 percent, and the industrial sector, only about 22 percent.

Fiscal Imbalance

- In 1990-91, the revenue and fiscal deficits were 3.26 and 8.07 percent of the GDP. In 1999-00, the revenue deficit was 3.15 percent of the GDP, and the fiscal deficit, 5.3 percent. However, the fiscal deficit figure is not comparable with the corresponding figures upto 1998-99 because of the changeover to the NSSF. The revenue imbalance indicates that the decade of fiscal reforms closed with almost as bad a profile of imbalance as at the beginning. In one sense, it was worse. In 1990-91, the ratio of revenue deficit to fiscal deficit was about 40 percent. This ratio, indicating the quality of fiscal deficit, degenerated to 60 percent in 1999-00.

Central Taxes: Aggregate Performance

- The tax-GDP ratio improved marginally in 1999-00, rising from 8.18 percent in 1998-99 to 8.78 percent. But this still was well below the 10.12 percent level in 1990-91. The course that different Union taxes took during the nineties largely determined why the deficits defied correction. The central failure was persistent erosion of the Union excise duties relative to the GDP. While income and corporation taxes rose relative to the GDP, the Union excise and customs duties fell. The fall in the customs duties may have explanations in external liberalisation and the WTO considerations. For the customs duties, there were perhaps the WTO compulsions that brought the tax rates and revenues down. Reforms, on the other hand, that recast the Union excise duties under the value added tax principle into MODVAT and later CENVAT, proved to be revenue depleting relative to the GDP. The fall in the indirect taxes could not be overcome by a rise in revenues from the direct taxes, and a small increase in the non-tax revenues. Consequently, the overall revenue receipts of the centre fell relative to the GDP. The tax base remained focussed on a narrow portion of the GDP. The industrial sector which constitutes the core of the tax base of important central taxes like the corporation tax and the Union excise duties accounted for only 21-22 percent of output throughout the nineties. There is enough potential for widening the direct taxes revenue base. The service sector potential for tax revenue still remains largely untapped.

Non Tax Revenues: Near Stagnant Growth

- Non-tax revenues as a percent to the GDP have remained near stagnant during the nineties. There is an increase of 0.52 percent points if three years averages are compared in the beginning and the end of the decade. An important contributing factor of this increase is the higher contributions of the RBI's surpluses, which were in effect only endogenous resource transfers.

Government Expenditure: Fall in Capital Expenditure

- The erosion of the tax-GDP ratio, even while maintaining almost as much borrowing relative to the GDP as at the beginning of the nineties, led to a fall in government expenditure, both revenue and capital. It was 17.54 percent of the GDP in 1999-00 down from18.10 percent in 1990-91. This small fall hides two major casualties. One, the ratio of non-interest, non-pension expenditure, i.e. expenditure directly relevant for the provision of services, fell. Secondly, asset-forming expenditures also fell: capital expenditure from 2.35 percent of the GDP in 1990-91 to 1.48 percent in 1999-00, and loans and advances, from 3.64 percent to 1.40 percent. Interest payments and pensions, on the other hand, mounted. Further, while plan revenue expenditure has grown at a trend growth rate of 14.43 percent per annum over the nineties, plan capital expenditure has grown at a dismally low TGR of 2.86 percent during this period. In 1999-00, the share of non-plan expenditure in total expenditure was the highest for the decade.

Subsidies: Non Transparent Design

- The quality and efficacy of expenditures are further beset by a non-transparent subsidy regime. Many subsidies are administered through inputs like power, irrigation, transport, fertilizers and diesel. Input based subsidies dissipate resources and the incidence of their benefits cannot be controlled. As such, these input subsidies remain ill targeted. Even those subsidies that are administered through final outputs like the food subsidy remain inappropriately targeted. Food and fertilizers subsidies hide inefficiencies and have defied correction in spite of budgetary promises. Some of the central subsidies show high TGR during the nineties like food at 16.34 percent and interest subsidies at 17.62 percent. Subsidies pertaining to the sale of decontrolled fertilizer have grown at the TGR of 63.61 percent over 1994-95 to 1999-00. Implicit subsidies are more difficult to control because these remain hidden in general expenditures. Roughly estimated, implicit subsidy to the nationalized banks amounted to Rs.1429 crore; to PSUs, amounted to Rs.2404 crore; and to postal services, these amounted to Rs. 991 crore during 1999-00.

Rising Interest Rates: Adverse Cycle

- The deteriorating trends in the Union government finances are partly due to a self- sustaining adverse cycle linking higher fiscal deficit to higher cost of borrowing. The pressure on the interest rates builds up because of rising repayment obligations as also rising interest payments. Since the government has to lift up this large amount of money from the system, it has to bear a high cost. Resultantly, there is steady depletion of the ratio of net receipts to government relative to gross receipts, which has fallen from 53.41 in 1990-91 to 38.17 in 1999-00. Thus, the government has been getting less and less resources, for current applications for the services that it provides, at higher and higher interest costs. The effective interest rate has gone up from 8.02 percent per annum in 1990-91 to 10.61 percent in 1999-00.

Debt: Compositional change and Sustainability Issues

- The government reckons its external debt in the budget at historical exchange rates. It would be, however, more appropriate to evaluate it at the current exchange rates. Total liabilities at current exchange rates stood at 57.23 percent of the GDP at the end of 1999-00. This is nearly 7 percentage points higher than its level evaluated at historical exchange rates.

- The debt GDP ratio has fallen during the nineties. The share of internal debt in total liabilities has increased substantially, rising from 40.43 percent in 1991-92 to 63.77 percent in 1999-00 of the total liabilities, evaluated at current exchange rates. The other component of liabilities that has risen over the nineties comprises small savings and provident funds. Together internal debt and small savings and provident funds accounted for 79 percent of the total liabilities, rising from 68.86 percent in 1991-92.

- The conversion of the treasury bills to government securities during the nineties hiked the RBI interest costs to the government. However, payment of higher interest by the government to the RBI and transfer of surplus by the RBI to the government amounted to little else than completion of a fruitless accounting circuit. Likewise, the endogenous resource transfers of the RBI's surplus to the government inhibit the effectiveness of Ways and Means Advances, introduced in 1997, as an instrument of fiscal discipline.

- Sustainability of debt remains a key issue. The trends in the nineties indicate that interest payments rose relative to the GDP, even though the debt-GDP ratio fell. For sustainability, the debt-GDP ratio needs to be reduced further. The trend of the fall in the debt –GDP ratio weakened towards the end of the nineties. The average yearly fall between 1991-92 to 1995-96 was 0.8 percentage points, which slowed down to an average of 0.15 percentage points between 1996-97 to 1999-00. Achievement of speedier reduction in the debt–GDP ratio would require additional remedial measures in the medium term.

Fiscal Marksmanship

- The government has persistently underestimated revenue and fiscal deficits. It has also generally overestimated the receipts, although 1999-00 was a notable exception in recent years. On the other hand, the government has generally underestimated revenue expenditures and has overestimated the capital expenditures. The budget estimates of discharge of public liabilities have fallen short of actuals in all the years in the nineties without exception. Receipts from small savings and provident funds have also been consistently under budgeted. Repeated estimation errors indicate that the government needs to focus on the systemic factors, improve its understanding of the past errors, and rework the estimation methodologies significantly for improving fiscal marksmanship.

Efficacy of Expenditures

- As resources available for application for current services have depleted relative to the GDP, it is critical that these are used with optimum efficiency. Inefficiencies in government expenditure lead to either higher costs for the same service or poorer service for the same cost. A more macro level of inefficiency relates to inadequate provision for essential services that need to be provided by the government, such as public goods and high merit goods. Inefficiencies result from rigidities like lapse of funds at the close of the financial year, opacities in the budget process, such as large implicit subsidies, limited parliamentary debates on demands for grants, and routine delays in decision processes. Many of these inefficiencies are visible after the examination of finance and appropriation accounts and the emergent pattern of the finances. In sum, the following sources of inefficiencies may be underlined:

  a. ***March rush***: a large proportion of expenditure is crowded in the month of March leading to hasty decisions, involving avoidable inefficiencies.

b. ***Implicit subsidies***: there is a large volume of hidden subsidies making the budget process opaque. The implication of these subsidies is not fully realized or debated because these are not mentioned in the budgets as subsidies.

c. ***Procedural inefficiencies***: major deficiencies in the process of incurring expenditures, relate to incurring expenditure without sanction, excess disbursements over sanctioned grants, which remain non-regularized, and unspent amounts against provisions.

d. ***Unauthorised reappropriations***: considerable amounts are reappropriated between different primary units of appropriation defeating the original purpose or activity which is authorized by the Parliament; often these reappropriations are found to be injudicious and without prior approval.

e. ***Poor fiscal marksmanship***: a major cause of inefficiency is unrealistic budgeting. Budget estimates are based on such assumptions as often turn out to be unrealistic; demands are habitually overstated. Similar errors are repeated year after year.