State of finances

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Introduction:

The COVID-19 pandemic adversely impacted the fiscal position of both central and state governments.

Impact of Covid-19 pandemic on states' finances:

1. The states saw their combined fiscal deficit rise to 4.1 percent of GDP in 2020-21, their debt-to-GDP ratio also went up, as their revenues came under stress, while the pressure to spend rose during this period.
2. However, their fiscal position has since then witnessed considerable improvement, as outlined in a study by the Reserve Bank of India on state budgets.
3. Alongside, states have, aided by the Centre, also tried to maintain a healthy momentum in their capital spending to provide the much-needed fillip to investment activity in the economy.

RBI study on state budgets:

1. As per the study, the consolidated fiscal deficit of states fell from 4.1 percent of GDP in 2020-21 to 2.8 percent in 2022-23.
2. The deficit in 2022-23 was, in fact, lower than what states had pegged in their budgets as well as the revised estimates.
3. For 2023-24, states have projected their deficits at 3.1 percent.
4. This, however, is lower than the limit of 3.5 percent for the year, implying that states are not utilising the entire fiscal space available to them.
5. For the current financial year, states had projected a healthy rise in their revenue receipts. However, data available for the first half of the year shows that their revenue growth has been slightly lower than what they had budgeted for.
6. However, the study notes that while states' revenue expenditure has decelerated (committed expenditure which includes interest payments, pensions etc have been pegged at the same level as last year), capital spending continues to grow at a robust pace.
7. Their capital outlay has risen by a staggering 52.6 per cent, aided by the Centre's assistance for investments.
8. In the Union budget, the central government had provided for a 50-year interest-free loan to states for investments with an outlay of Rs 1.3 lakh crore.

Challenges to states' finances:

1. For one, the decision of some to shift back to the old pension scheme will impose a fiscal burden.
2. This will have implications for the space available to them to allocate more for capital spending.

3. While overall, the fiscal position of states has improved, not all of them have seen such healthy improvements.
4. In fact, some states continue to have significantly higher debt and deficit levels.

How states can improve their fiscal condition?

Revenue Enhancement:

1. Tax reforms: Implement broader tax bases and simplify tax structures to improve efficiency and compliance.
2. Rationalization of subsidies: Review and revise existing subsidies to ensure they are targeted and effective, minimizing waste and leakages.
3. User charges: Implement user charges for public services where feasible, ensuring equitable distribution of the burden.
4. Improved tax administration: Invest in technology and human resources to strengthen tax collection and minimize evasion.
5. Public-private partnerships: Explore public-private partnerships for infrastructure development and other projects, attracting private investment and boosting revenue.
6. Disinvestment: Consider strategic disinvestment of non-core assets to generate revenue.

Expenditure Management:

1. Rationalization of government schemes: Evaluate and consolidate existing government schemes to ensure cost-effectiveness and avoid overlap.
2. Zero-based budgeting: Implement zero-based budgeting, reviewing all expenditures annually and justifying them based on current needs.
3. E-governance: Leverage technology to improve efficiency and transparency in government spending, reducing administrative costs.
4. Review of public sector enterprises: Assess the performance of public sector enterprises and consider restructuring or privatization where appropriate.
5. Payroll reforms: Implement rationalization of government salaries and pensions, considering long-term sustainability.

Additional Strategies:

1. Financial discipline: Maintain strict financial discipline with clear spending limits and a focus on fiscal responsibility.
2. Intergovernmental transfers: Work collaboratively with the central government to ensure equitable distribution of resources and financial support.
3. Capacity building: Invest in capacity building for state officials in areas like financial management, public policy, and project implementation.
4. Transparency and accountability: Implement measures to improve transparency and accountability in government spending, fostering public trust and participation.

Creative Approaches:

1. Crowdfunding: Explore innovative financing mechanisms like crowdfunding for specific development projects.
2. Social impact bonds: Consider using social impact bonds to address social challenges and attract private investment.
3. Green bonds: Issue green bonds to finance environmentally friendly projects and attract investors seeking sustainable investments.

Conclusion:

In conclusion, we can say that the Fiscal position of states has improved. However, they must guard against imprudent schemes.