Restructuring Public Finances[1] (DRAFT)

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Executive Summary

Public finances in India are at a turning point. Analysis of the past data, however, shows no improvement in any of the major fiscal indicators. Implementation of VAT, a review of the role of inter-governmental agencies such as the Planning Commission and realignment of transfers to states for capital expenditure will provide the foundation for stronger public finances.

Revenue and fiscal deficit are far from the targets proposed by the Eleventh Finance Commission for 2004-05. In the recent past, the brunt of sustained level of fiscal deficit has been borne by social infrastructure which received smaller and smaller resources. In spite of reforms in power sector, tangible results have not materialised as yet. Reforms in irrigation sector and state road transportation have not progressed much. The stock of debt is still far too high by any standard. The Fiscal Responsibility and Budget Management Act, 2003 of the Central government and the Medium Term Fiscal Reforms Programme (MTFRP) of states are positive steps to deal with twin deficits. Restructure of debt, reforms in power sector and implementation of other issues under MTFRP hold promise for future, deficit and debt targets may be achieved by 2010 only. In the last decade, India has substituted domestic debt for foreign debt. To be credible, the domestic debt as a proportion of GDP needs to be pared in an aggressive manner.

One initiative which would have had significant impact is the introduction of VAT. The aborted launch of VAT at states level was aimed at eliminating the fiscal drag and strengthening the reform process at sub-national level. It could have enlarged the tax base without raising overall tax rate. Assignment of taxation power is one area, especially through VAT on services, which will help in filling the vertical gap partly. An urgent need is there to make sustained efforts for an early introduction of VAT.

Although, central government expenditure seems to be counter-cyclical, it has not helped states. In fact, lower revenue transfers to states have exacerbated their revenue deficits and capacity to spend on social infrastructure. Transfer to states partly as fixed sum and the rest linked to specific programme/project – with or without incentive payment – can ameliorate the cascading effect of lower than anticipated revenue collection. The performance based sector-specific transfers could set an example for state finance commissions. Performance could be related to recoverable user charges also. Such transfers would be progressive and would improve efficiency of resources.

In the coming years, as states are expected to raise part of the resources from the capital market, the market should be allowed to assess viability of economic infrastructure projects. Rethinking on role of state plans and of the central planning commission needs to be reconsidered when allocation of resources is being guided by the markets. Capital expenditure under plan and non-plan has given rise to step-motherly treatment to the maintenance of physical assets created under plan heads. Social infrastructure and maintenance which bears the burden of cuts in revenue expenditure may benefit from abolition of artificial distinction between plan and non-plan expenditure.

1. Introduction

The structural imbalance in India's public finance system exists right from the beginning. While the deterioration in fiscal turning points in the last decade can be related to some proximate causes like pay revision of employees or sluggish revenue growth because of a slowdown in the economy, the imbalances in the state budgets have their origin in factors that are structural in character (Anand, Bagchi and Sen, 2001). The main objective of this paper is to suggest restructuring of public finances of the Centre and State governments to provide macro-economic stability, equitable growth in the country and improve efficiency of resources. The paper also suggests ways to augment revenue resources and contraction in expenditure.

Public finances in India are at inflection point. If past data is analysed and projected in future there would be little hope of seeing any improvement in any of the major macroeconomic indicators. The Eleventh Finance Commission (EFC), which was entrusted with the responsibility of suggesting restructuring of the central and state governments public finances, had envisaged trend path for level of revenue and fiscal deficit, the level of debt and expenditure on social infrastructure. None of the indicators seem to be on the trend-path and gap between the suggested path and actual turnout has stubbornly remained.

Given the objective of this paper, section 2 analyses suggestions made by the EFC. Section 3 compares the EFC projections with the most recent data available. Section 4 describes the restructuring process at the national and sub-national level. Section 5 examines whether the gradual restructuring process and institutional changes are going to have favourable impact on the macroeconomic indicators in medium term. Based on assumptions on GDP growth rate, inflation and interest rates, three scenarios have been outlined in section 6 to estimate the economic outcome in the coming decade. Finally, in section 7 suggestions are made to restructure public finances to meet development objectives of the economy.

2. Restructuring suggested by the Eleventh Finance Commission

For the first time the terms of reference of a finance commission was enlarged to suggest the restructuring of public finances. Clause 4 of the TOR required the Eleventh Finance Commission (EFC) '*to review the state of finances of the Union and the States and suggest ways and means by which the governments, collectively and severally, may bring about a restructuring of the public finances so as to restore budgetary balance and maintain macroeconomic stability*'. The Commission considered and spelt out the relevant parameters of macroeconomic stability, specified a restructuring path and gave an outline by which such restructuring can be brought about by the Central and State governments (GOI, 2000).

This changed the scope of the finance commission work and it recommended fiscal transfers which shall bring about macroeconomic stability over the medium term. Probably it was in response to the shift in emphasis from planned allocation to market based allocation of resources. Central as well as state governments used (misused !!) all the financing measures which could soften the budget constraint in 1990s. Resources were raised using state guarantees without due diligence process. Temporary financial instruments such as 'Ways and Means' advances and overdraft from RBI, which are essentially bridge loans, were used to finance projects which require long-term funds. The misuse of such facilities gave rise to liquidity mismatch and forced the central bank to tighten the norms for providing 'Ways and Means' facility as well as for guarantees (RBI, 2002 and 2003c).

The EFC recognised upfront that general government fiscal deficit is too high and it needs to be controlled and government should go all out to reduce the fiscal deficit. It underlined the importance of having surpluses on revenue account to finance capital expenditure but the growing demand of servicing of past debt has meant that the revenue deficit could not be reined in. Failing to raise revenue receipt resulted in self-perpetuating spiral of debt and deficit, and threatened the macroeconomic stability.

The term 'macroeconomic stability' was defined as stability of prices at full employment of available resources generally referred to as non-accelerating inflation rate of unemployment (NAIRU) in economic literature. However, this would provide only internal balance and for the external balance it was suggested that the current account deficit should be within limits which can be serviced in the long run out of export earnings and factor incomes from abroad. The Commission also suggested that fiscal policy should be counter cyclical to economic fluctuations in order to maintain stability in short-term. To achieve long-run stability the composition of government expenditure, debt and fiscal deficit should be in line with potential full employment output. The report acknowledged the limit placed on monetised deficit through the MOU between the GOI and the RBI; however, it suggested that the limit should be linked to GDP. While considering sustainability of domestic debt, it was emphasised that budget constraint rule – the rate of interest should not exceed the rate of GDP growth – should be followed. The report emphasised that this rule is violated in the budgets of the centre, in the combined accounts of the Centre and states and individually in many states (Para 3.14).

Fiscal deficit also came under scrutiny and a view was taken that fiscal deficit as a proportion of (full employment) GDP depends on how the borrowed funds are used. Nevertheless, revenue budget should generate surpluses for government investment. While discussing normative level of fiscal deficit, the report suggested the same norm prevalent in the EU countries under the Maastricht treaty for fiscal deficit and inflation. The fiscal deficit of 3% of GDP and the debt-GDP ratio of less than 60 per cent are the EU norms. For a growing economy like that of India, the EFC recommended that debt-gdp ratio should be stabilised around 55% and a combined fiscal deficit of the Centre and States at 6.5% of GDP.

While emphasis remained to control the fiscal deficit, the report was emphatic that tax base must be expanded to increase tax revenue so that fiscal compression does not hurt expenditure on social and infrastructure sectors. While recognising vertical imbalance of Indian federal structure, the commission was emphatic to devolve taxation power to state and local bodies so that expenditure and revenue collection gap narrows down to some extent (Para 3.74). In order to achieve fiscal consolidation the commission recommended the following important institutional changes at the Central and state level:

Central government

a. Widening of the tax base and listing of services in the concurrent list
b. Rightsizing of the government at all levels
c. Prescribe limits on borrowings as proportion of GDP
d. Revise the present system of determining and providing assistance for state plans
e. Introduce a multi-year budgeting process

State government

a. Use profession tax and tax farm incomes to augment tax revenues of states
b. Rely on user charges reflective of input costs to augment non-tax revenue
c. Rightsizing of the government at all levels
d. Prescribe limits on borrowings as proportion of GSDP
e. Introduce a multi-year budgeting process

3. Review of EFC recommendations

3.1. Central government

On the basis of point estimates projected by the EFC one can safely conclude that except inflation rate and current account balance all other indicators are too far from the EFC projection for 2004-05 and it is unlikely that these targets can be achieved (Table 1). One can even argue that had the economy been operating near its full potential, not only the twin deficits could have been reined in, the turnout would have been very near the EFC projections without affecting inflation and current account balance adversely[2].

Table 1: Macro Scenario Over the period 1999-04 and the EFC's Projection for 2004-05 (per cent of GDP)

	1999-2000	2000-01	2001-02	2002-03 (RE)	2003-04 (BE)/(F)	2004-05 (EFC Proj.)
Growth Rate (% per annum)	6.1	4.4	5.6	4.3	6.5	7.0-7.5
Inflation Rate (% per annum)	3.3	7.2	3.6	3.4	3.5	5.5-5.0
Current Account Balance (% of GDP)	-1.1	-0.8	0.2	0.7	1.0	-1.5
Revenue Deficit (% of GDP)	6.4	6.8	7.2	7.0	6.1	1.0
Fiscal Deficit (% of GDP)	9.9	9.9	9.8	9.4	9.5	6.5
Tax Revenue (% of GDP)	14.1	14.6	13.7	14.9	15.2	16.7
Non-Tax Revenue (% of GDP)*	3.8 (2.5)	3.5	4.1	4.7	4.4	3.2
Capital Expenditure (% of GDP)	3.3(4.2)	3.1	3.2	3.9	4.4	6.6

*excludes interest payment from states to Centre. F - Forecast

Source : RBI (2003a), RBI(2003b), Budget Papers

Note: Figures in brackets are the EFC's base figures where there is a significant change from the actual data.

Table 2 shows that barring custom duties and states' own tax revenues, other major tax sources are nearly in line with the set target[3]. Reduction in custom duties is in line with opening up of manufacturing sector to international competition by lowering tax barriers.

Combined finances of the centre and states show sizeable divergence from the EFC projections of revenue deficit, fiscal deficit and capital expenditure. Revenue expenditure could not be controlled and, hence, weight of adjustment fell on capital expenditure. Tax revenue, non-tax revenue and revenue receipts suggest some improvement over the years and yet are short of the EFC target (Table 3).

[2] One needs a small macroeconomic model to carry out these counter-factual scenarios to spell out the impact of economic growth on investment and consumption. Such an exercise was carried out for the UK economy when it underwent structural changes in 1970s and 1980s. For evaluation of UK's economic policies - Medium Term Fiscal Strategy (1979-84) and debate on entry of UK in the European Monetary System in 1970's and 1980's - see Minford and Rastogi (1989) and Hughes Hallett, Minford and Rastogi (1993).

[3] Final comparison (2003-04) is with budget estimates and these are generally revised downwards, especially, when economic growth is below expectations. However, a higher GDP growth expected in 2003-04 may see the 2003-04 targets being met.

Table 2: Tax Revenues 1999-04 and the EFC's Projection for 2004-05 (per cent of GDP)

Taxes	1999-00	2000-01	2001-02	2002-03	2003-04 (BE)	2004-05 (EFC Proj.)
Income Tax	1.5	1.8	1.6	1.7	1.8	1.8
Corporation Tax	1.7	2.0	1.9	2.0	2.1	2.2
Union Excise Duties	3.5	3.7	3.6	3.9	3.9	3.7
Custom Duties	2.7	2.6	2.1	2.0	2.0	2.6
Central Taxes (Gross)	9.6	10.3	9.4	9.8	10.1	10.3
States Own Tax Revenues	5.2	5.6	5.6	5.9	6.0	6.4

Source : RBI (2003b), Budget Papers

Table 3:Fiscal Parameters Centre and States: 1999-04 and the EFC's Projection for 2004-05 (per cent of GDP)

	1999-00	2000-01	2001-02	2002-03	2003-04 (BE)	2004-05 (EFC Proj.)
Combined Finances						
Tax Revenues	14.1	14.6	13.7	14.9	15.2	16.7
Non-Tax Revenues	3.8 (2.5)	3.5	4.1	4.7	4.4	3.2
Revenue Receipts	19.4(16.6)	19.4	19.1	20.9	21.0	20.0
Revenue Expenditure	26.3(23.3)	26.6	26.7	28.3	27.5	21.0
Capital Expenditure	3.3(4.2)	3.1	3.2	3.9	4.4	6.6
Revenue Deficit	6.4(6.8)	6.8	7.2	7.0	6.1	1.0
Fiscal Deficit	9.9	9.9	9.8	9.4	9.5	6.5
Centre						
Tax Revenues	8.8	9.0	8.1	9.0	9.2	10.3
Non-Tax Revenues	2.8	2.7	3.0	2.9	2.5	3.0
Revenue Receipts	9.4(11.5)	9.2	8.8	9.6	9.3	13.3
Revenue Expenditure	12.9(13.1)	13.2	13.1	13.8	13.4	11.5
Capital Expenditure	2.5(2.6)	2.3	2.7	2.5	2.7	4.0
Revenue Deficit	3.5(3.8)	4.1	4.4	4.2	4.1	1.0
Fiscal Deficit	5.4(3.6)	5.7	6.1	5.9	5.6	4.5
States						
Tax Revenues (own)	5.3	5.6	5.6	5.9	6.0	6.4
Non-Tax Revenues (own)	1.5(1.0)	1.5	1.4	1.5	1.4	1.5
Revenue Receipts	10.4	8.8	8.6	9.0	9.2	13.0
Revenue Expenditure	13.3	11.6	11.4	11.7	11.1	13.0
Capital Expenditure	2.1	3.1**	3.2**	3.9**	4.4**	2.9
Revenue Deficit	3.0	2.8	2.8	2.7	2.0	0.0
Fiscal Deficit (gross)	4.7	4.3	4.2	4.7	4.0	2.5

*does not include interest payments from the States to the Centre
** The increase is due to compensation and assignments to local bodies and Panchayti Raj Institutions
Note : Figures in brackets are the EFC's base figures where there is a significant change from the actual data.

Source : RBI (2003a), RBI(2003b), Budget Papers

At the centre, revenue expenditure has remained almost at the same level as it was in the base year 1999-2000. As a result, revenue deficits could not be reduced sufficiently. With revenue deficit remaining intractable, there is no reduction in fiscal deficits. Consequently, capital expenditure which was expected to show a growth of one and a half percentage points of GDP has remained stagnant at the 1999-2000 level as proportion of GDP (Table 4).

3.2. State governments

That the states' own tax revenues potential has not been fully exploited is evident from the economic data. However, the gap is narrow enough which can be easily filled[4]. Revenue deficit of the combined state finances has been gradually declining but fiscal deficit remained stubbornly above 4% of GDP (Table 3). Capital expenditure of the states since 2000-01 has shown an unusual spurt due to compensation and assignments to local bodies and Panchayti Raj Institutions as suggested by their respective State Finance Commissions (RBI, 2003b). But, revenue receipts have fallen short significantly from the EFC's target of 2004-05 which is closely related to the revenue deficit of the states (Table 3).

Table 4: Main Components of Expenditure 1999-04 and the EFC's Projection for 2004-05 (per cent of GDP)

	1999-00	2000-01	2001-02	2002-03	2003-04 (BE)	2004-05 (EFC Proj.)
Revenue Expenditure						
Centre						
Interest Payments	5.2 (4.7)	5.2	5.1	5.1	5.0	4.3
Pensions	0.8	0.8	0.7	0.6	0.6	0.7
Other General Services	0.3 (2.5)	0.4	0.4	0.4	0.3	2.1
Social Services	0.4	0.3	0.3	0.3	0.3	0.3
Economic Services	0.4	0.5	0.4	0.5	0.5	0.3
States						
Interest Payment	2.6 (2.3)	2.8	3.2	3.3	n.a.	2.6
Pension	1.3 (1.2)	1.3	1.3	1.3	n.a.	1.0
Other General Services	0.1 (1.6)	0.2	0.2	0.4	n.a.	1.7
Social Services of which	5.8 (5.1)	5.4	5.6	5.4	n.a.	5.8
Education, sports etc	3.2	3.1	3.1	2.9	n.a.	1.8
Primary Health etc	0.9	0.8	0.8	0.8	n.a.	0.5
Water Supply and Sanitation	0.4	0.3	0.3	0.3	n.a.	0.5
Economic Services of which	4.3 (2.9)	3.3	3.3	3.1	n.a.	2.3
Energy		0.7	0.8	0.6	n.a.	
Capital Expenditure						
Centre	2.5 (2.6)	2.3	2.7	2.5	2.7	4.0
States	2.1	3.1	3.2	3.9	4.4	2.9

Source : RBI (2003a), RBI(2003b), Budget papers
Note : 2002-03 figures of States are BE

Interest payments on debt have been rising rather than declining as expected by the EFC. Expenditure on economic services remained high though declining in the last couple of years. Interestingly, expenditure under energy head is expected to decline in 2002-03(BE) (Table 4).

[4] The example of Maharashtra is well documented in WB(2002).

In brief, at the Centre, interest payments could not be reined in and it remained a major component of revenue expenditure. At states level, interest payments have been growing. Expenditure on social services which was envisioned to grow by 0.7% of GDP has shrunk by 0.4% of GDP over by 2002-03.

4. Emerging pattern of restructuring process

Table 1 shows that the decline in tax collection as well as the economic growth were in the region of 0.5-0.6 and 2-2.5 percentage points respectively (Table -1). Nevertheless, restructuring on various fronts, in line with the EFC recommendations, continued, albeit slowly, and many of them have reached fruition in the current year. We outline the monetary and structural changes and their implications on fiscal health of the government finances in the coming years.

4.1. Central government

The weak links – a narrow tax base and overwhelming dependence on manufacturing sector for tax revenues – in the Central government finances continue to persist, despite various measures taken to strengthen the process of fiscal consolidation. The Union budget for 2003-04, in particular, has attempted to address the issues of structural weaknesses in the Central government finances. The budget has projected a modest growth in revenue collection and larger non-debt capital mobilisation through disinvestment. The rationalisation of expenditure and improved cash management suggested in the budget would consolidate public expenditure and enhance productive use of financial resources. Investments in infrastructure sectors are envisaged through public-private partnership. The initiatives such as prepayment of external debt, buy-back of past high cost loans from the banking system, and debt-swapping with State governments are expected to strengthen the fiscal consolidation process.

4.1.1. The Fiscal Responsibility and Budget Management (FRBM) Act, 2003

Bringing fiscal responsibility on statute books is a landmark legislation and its implementation over the next few years will have some impact on public finances. In particular, bringing revenue deficit to zero by 31st March, 2008 is a stiff target. Compliance with the Act has already started in earnest (Article 7) and one can hope that medium term fiscal targets advocated in the Act are kept in mind during budget making process in the next fiscal year which would be the first FY under the FRBM Act. The Centre armed with this Act can now fend off unreasonable pressure from states for assistance. The Act has bestowed total responsibility to RBI in matters related to monetary affairs of the government.

4.1.2. Restructuring of debt

Following a softening interest rate regime the Government has initiated debt restructuring process on three fronts, viz., pre-payment of external debt, buy-back of loans from banks contracted under high interest rate regime and debt-swapping scheme with the State governments[5].

With regard to external debt repayment, the Government has effected premature repayment of 'high-cost' currency pool loans of the World Bank and of the Asian Development Bank, totalling around $ 3 billion, taking advantage of comfortable foreign exchange reserves and lower domestic interest rates. The latest budget has reaffirmed the intention to continue with the policy

[5] The average interest rate on Government of India's outstanding debt has come down from 11.8 per cent in 1999-2000 to 5.9 per cent in 2003-04 (Table A1).

of prudently managing the external liabilities and of proactively liquidating relatively higher cost component of external debt portfolio.

As regards domestic debt, the measures are initiated in the context of large proportion of Central government domestic debt contracted under the high interest rate regime, which is thinly traded and largely owned by public sector banks and institutions. With the softening of interest rates, such loans commanded a premium over their face value. Under the debt buy-back scheme, the Central government offered to buy-back high interest loans from banks on 'voluntary' basis. The scheme enabled the banks to improve their liquidity position by encashing the premium for making provisions for their NPAs. Furthermore, in case the banks declare the premium received as business income, for income tax purpose, they will be allowed additional deduction to the extent such income is used for provisioning of their NPAs for improving their balance sheet.

The process of debt restructuring is being carried out in full earnest. The RBI has been able to raise money at interest rates which are historically low. For instance, 10-year money has been raised at 5.7 per cent for the Centre and 6.2 per cent for the States[6]. In the first quarter of FY 2003-04 the central government had a freak result where its fiscal deficit has been lower than the revenue deficit due to states repaying Rs 24,268 crore of their debt[7].

4.1.3. Utilisation of divestment windfall

The EFC had recommended that proceeds from disinvestment process should be used to retire debt. Since 1999-2000, proceeds from divestment including control premium, dividend and dividend tax etc. have not been substantial as percentage of GDP (Table A4). But, there is a distinct change in disinvestment process and government policy. Unlike previous disinvestment of PSUs, now the emphasis is on selling government equity to a strategic buyer with management control in a transparent manner using market intermediaries for pricing of assets, marketing of the strategic stake etc.

During the disinvestment of BALCO, the Supreme Court gave the landmark judgement that disinvestment could be effected by an executive order which would have made the future disinvestment of the rest of the PSUs simpler and faster. The policy of disinvestment specifically aims at modernization and upgradation of Public Sector Enterprises, creation of new assets, generation of employment, and retiring of public debt. Further, the Finance Minister in his Budget Speech for 2003-04 announced that '*the pace of disinvestment will accelerate in the coming year. I wish to also state that details about the already announced Disinvestment Fund and Asset Management Company, to hold residual shares post disinvestment, shall be finalized early in 2003-04……., disinvestment is not merely for mobilizing revenues for the Government, it is mainly for unlocking the productive potential of these undertakings, and for reorienting the Government, away from business and towards the business of governance'*. This suggests that government is serious about getting out of managing business. Strategic sale of many PSUs since January 2000 corroborates government intent (Table A5).

Disinvestment process and schedule is now on a slippery ground as the Supreme Court's judgement on the sale of HPCL and BPCL requires that disinvestment of PSUs created by a legislative act or paid from consolidated fund of the government require approval from the respective legislature. This would add to the traditional problems related to valuation and labour policy[8].

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[6] RBI Press Release : 2003-2004/157, August 3, 2003

[7] Data released by Controller General of Accounts on August 29, 2003

[8] Pension liabilities, land policy, subsidies and regulatory uncertainty affect the valuation of a PSU.

4.2. State governments

4.2.1. Medium-Term Fiscal Reforms Programme

The EFC had recommended the establishment of an incentive fund to encourage speedier fiscal reforms in the states which can be easily monitored and the span of the programme should be over the EFC time frame. In response to this, the central government created the 'States' Fiscal Reforms Facility (2000-01 to 2004-05)'. An incentive fund of Rs 10,607 crore over the EFC's life-time was allocated. To be eligible to draw from the fund, states having revenue deficit were to reduce it by five percentage points as a proportion of the State's total revenue receipts in each year till 2004-05[9]. States were also allowed to raise resources from the market to meet their structural adjustment requirement arising from VRS, downsizing of PSEs and centre-state debt swap for bringing down interest liabilities (GOI, 2002).

In response to this 16 states drew up a Medium-Term Fiscal Reforms Programme (MTFRP) and signed a MOU with the MOF, GOI. The objective of the MTFRP is to eliminate revenue deficit, to reduce fiscal deficit to sustainable levels and to reduce debt-GDP ratio including contingent liabilities to sustainable levels. The MTFRP includes a whole gamut of fiscal consolidation measures, PSUs restructuring, power sector reforms etc. In line with the EFC's recommendations, the Planning Commission is ensuring that the Annual Plan framework is consistent with the MTFRP.

4.2.2. Reforms in power sector[10]

Fiscal reforms of the States are inextricably intertwined with power sector reforms. Commercial losses of the SEBs amounted to 1.2 percent of GDP in 2000-01 (Rao, 2002). In comparison to this fiscal deficit of states was 4.3 percent of GDP in 2000-01 and it is expected to be 4 percent in 2003-04 (Table 3) The Electricity Act 2003 consolidates laws relating to transmission, distribution, trading and use of electricity. The Act is the most important legislative change for the power sector but the other two equally important reports, namely, *Expert Committee Reports - Settlement of SEB Dues* chaired by Montek Singh Ahluwalia (GOI, 2001) and *Structuring of Accelerated Power Development & Reform Project (APDRP): Reform Framework and Principles of Financial Restructuring of SEBs* chaired by Deepak Parekh (GOI 2002a) are more important in the near future for State finances.

It was in the year 2000 that central and state governments realised the debilitating effect of SEBs on power sector development. The GOI proposed a scheme to restructure finances of the SEBs (GOI, 2001). The crux of the scheme is that past dues of the SEBs cease to be a financial burden on the SEBs and have to be serviced by the respective state governments at concessional terms. The future revenue generation of SEBs is therefore no longer hostage to past liabilities and hence, the path to reform is smoother. Additionally, in the debt forgiveness that the "One Time Settlement of Dues" entailed MoUs which were signed by the state governments, committed them to reform including tariff convergence. This will nudge state governments to reform their power sector.

[9] Revenue surplus states were to increase their balance in the current revenue by three percentage points only.
[10] For a detailed description of reforms in power sector see Rastogi (Forthcoming) and Rastogi (2003)

Implementation of the One Time Settlement of SEB Dues

Under this scheme the Government of India, Reserve Bank of India and state governments signed tripartite agreements. RBI notified in July, 2003 that the state-wise dues of around Rs 12,000 crore is to be paid by Andhra Pradesh, Assam, Goa, Gujarat, Himachal Pradesh, Haryana, Karnataka, Kerala, Meghalaya, Nagaland, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh, Uttaranchal, West Bengal to NTPC and other Central public sector undertakings (CPSUs). The states which did not figure in the RBI's notification were Maharashtra, Madhya Pradesh, Chhattisgarh, Bihar, Jharkhand, Orissa, Sikkim and Jammu & Kashmir. Since then, the Maharashtra government has signed a tripartite agreement with the Ministry of Power and Reserve Bank of India (RBI) for one-time settlement of dues of around Rs 600 crore owed by Maharashtra State Electricity Board (MSEB) to various CPSUs (RBI, 2003b).

Under the one-time settlement of SEB dues, the debt burden of SEBs has been further reduced as the central sector power utilities have waived Rs 10,000-crore delayed payment surcharge component payable by defaulting state electricity boards. Accordingly, total SEB dues to be securitised through the issue of tax-free bonds by the concerned state governments has reduced to Rs 31,000 crore from Rs 41,000 crore[11].

Further, the Central Government-owned Power Finance Corporation (PFC) has restructured debts of around Rs 800 crore of 18 state-owned utilities. The state utilities are expected to take advantage of the debt restructuring because PFC reduced its base lending rate to nine per cent in June 2003. The debt restructuring would reduce the interest burden on the states taking up power sector reforms. Past loans were given @12-15 per cent per annum. Restructuring the debts would therefore mean a substantial savings in expenditure, since the utilities continue to suffer revenue shortfalls. PFC could offer this restructuring package to the states as it took advantage of the soft interest rate regime by effecting prepayments and exercising early exit options on some of its high cost borrowings, particularly bonds[12].

Accelerated Power Development and Restructuring Programme (APDRP)

The Parekh Committee report outlined a reform framework and principles of financial restructuring of SEBs that could form the basis for devising state-specific reform programmes. The report is aimed at helping the states to devise strategies that are credible – and, hence, "bankable" – for raising transition financing support as recommended by the Ahluwalia Committee (GOI, 2001). The Parekh Committee decided to address its task in two stages. In the first stage the Committee reviewed the Accelerated Power Development Programme and suggested measures for improvement to be incorporated in the APDRP as part of a consolidated reform approach; and evolved a reform framework and broad principles for the financial restructuring of SEBs, based on a review of reform experiences in India and abroad. The reform framework has four critical components: market structure, distribution zoning, regulatory approach and ownership. The report has not suggested any specific way to reorganise a SEB. A reform template is given in the report which will be the starting point for devising the state-specific reforms – the second stage of the Committee's work.

Implementation of APDRP

All states had been requested last year to draw up their five-year programme for the power sector. The allocation under the APDRP depends on the states' performance for both components of the programme — incentives and investment. It is interesting to note that almost all states have drawn up plans to invest money in power projects. Though investment component of APDRP has

[11] Economic Times (July 29, 2003)
[12] Business Line (July 24, 2003)

achieved its budget target, states have not been able to tie up their counter part funds. Only 4% of target investment could be utilised[13] (Table A11).

Most state governments have now realised that power reforms have to be implemented to save the bleeding SEBs. For example, in 2003-04, Rajasthan and Delhi have accepted the tariff orders of the state electricity regulatory commission and implemented tariff hikes. In 2002-03, Madhya Pradesh effected steep tariff hikes while Tamil Nadu and Punjab introduced tariff on agricultural power consumption.

Nevertheless, there is still a wide gap between cost of supply and the average tariff. The gap widened from 0.23/kwh in 1992-93 to Rs 1.10/kwh in 2001-02. But, it is showing some signs of reversal with a decrease in the gap to Rs 0.91/kwh in 2002-03. Apart from setting up of SERCs the states' power reform measures include reducing T&D losses by 5% annually, unbundling, 100% consumer metering and achieving parity between cost of power and tariffs. In consumer metering, Delhi, Haryana, Himachal Pradesh, Karnataka, Kerala and Tamil Nadu have achieved 100% metering. There are only three states which have below 50% metering — Sikkim, Mizoram and J&K. Majority of the states managed to achieve over 80% metering by December 2002. Nearly 22 states have set up power regulatory commissions and many have proposed unbundling and corporatisation of SEBs.

The Finance Ministry's review of MTFRP indicates that growth in gross subsidy and commercial losses have been marginally arrested with a corresponding increase in revenue mobilisation in the power sector. Gross power subsidy has come down from Rs 34,587 crore in 2001-02 to Rs 33,280 crore in 2002-03 and is further expected to go down to Rs 32,429 crore in the current fiscal. The reducing trend in subsidy has been attributed to increase in tariffs to agricultural consumer and implementation of state electricity regulatory commissions' tariff awards[14].

4.2.3. Accelerated Irrigation Benefits Programme (AIBP)

A large number of river valley projects, both multipurpose and irrigation have spilled over from Plan to Plan mainly because of financial constraints being faced by the State Governments. As a result of this, despite a huge investment having already been made on these projects, the desired benefits have not accrued to the economy. There were 171 Major, 259 Medium and 72 Extension/ Renovation/ Modernisation (ERM) of on-going Irrigation projects in the country at various stages of construction at the end of the VIII Plan (i.e. end of March, 1997) with a spill over cost of Rs. 75,690 crore. Under the AIBP, the Union Government took remedial measures for expeditious completion of some of the projects which were in the advanced stage of completion.

Irrigation subsidies are a substantial part of state budgets and, therefore, wide ranging organizational reforms are on the agenda of several states: AP, Orissa and Tamil Nadu have enacted legislation envisaging major changes in the organization for water development. Some – notably Andhra Pradesh and Maharashtra – have taken significant and bold steps to raise water rates. Andhra Pradesh has legislated water user participation at all levels of each major and medium irrigation system. Maharashtra also has water user associations. Entrusting maintenance and repair to the local water user associations rather than contractors has given a strong sense of involvement on the part of users resulting in speedier completion of works, at lower cost and better quality than under the earlier dispensation (Vaidyanathan, 2003 and WB, 2002).

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[13] Incentive based funds were released to Gujarat (Rs 236.37 crore), Maharashtra (Rs 137.89 crore) and Haryana (Rs 5.01 crore) [Source : Ministry of Power (Conference of State Power Ministers, June 12th, 2003)].

[14] Economic Times (September 12, 2003)

4.2.4. Non-recurring revenue avenues (Divestment of state PSUs)

Recommendations of the EFC apply to State Level Public Enterprises (SLPE) as much as to Central Public Sector Undertakings. Divestment process at state level has not been encouraging, though some states are gearing up to disinvest/ close loss making enterprises in an accelerated manner (Table A6). Andhra Pradesh, Gujarat, Karnataka and Maharashtra account for more than 50% of total investment in SLPEs and except Maharashtra the other three states are pursuing restructuring/ disinvestment of SLPE earnestly (Table A7). It is disheartening to note that Punjab, Rajasthan, UP and West Bengal which account for approximately 25% of total investment in SLPEs, the process of disinvestment is moving at a snail's speed. Disinvestment process in Punjab has gathered pace recently and may gain momentum in the coming years.

The restructuring of SLPEs is part of the states MTFRP. It is worth noting that SLPEs run with periodical infusion of capital in the form of fresh share capital from the state governments or additional loans from them. This is mainly due to the running down of net worth through regular losses. In this situation, when states have to finance their deficit, they often force repayment of loans or payment of accumulated interest due to them. Consequently, it leaves the SLPEs with little productive capital, further worsening their financial health (Sen, 2000). Therefore, disinvestment of SLPEs should be seen as reduction in recurring cost (staff cost, establishment cost etc.) due to perennial losses being made by these SLPEs rather than as avenues to raise resources.

4.2.5. Restructuring of debt

Many states have passed fiscal responsibility act and are restructuring debt in co-ordination with the central government. In states, revenue expenditure accounts for a large proportion of the aggregate expenditure and interest payment accounts for roughly 25 percent of the revenue receipts. In some states interest payments have exceeded 30 percent of the revenue receipts[15]. To meet redemption of market loans of states the RBI set up a Consolidated Sinking Fund in 1999-2000[16] and also allowed states to directly access the market for resources ranging from 5% to 35% of gross borrowings, with the states deciding on the method, timing and maturities of the borrowings. These facilities have enabled the states to reduce their loan and advances requirements from the Centre. States have also reduced their loans and advances extended for non-development purposes. The weighted average of interest rate on market borrowings of states has declined continuously in the recent years from 14% percent in 1995-96 to 7.49 percent in 2002-03 (GOI, 2002). Outstanding guarantees of state governments have reduced from 8% of GDP in 2001 to 7.2% in 2002[17] (RBI, 2003a).

The net market borrowing of states has been declining and growth has been arrested after a spurt in growth in 2001-02 (Table A8) but long-end of the market loans is building up rapidly and repayment after 2007-08 is growing at an unsustainable rate (Table A9). Under MTFRP states will extinguish their central government loans bearing interest rate greater than 13% by 2005-06 but loans with 12%-13% coupon rates amount to almost one-quarter of their total loans, though overwhelmingly these are central government loans to states (Table A10).

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[15] These states are West Bengal, Orissa, Punjab and UP (RBI, 2003a).

[16] We reckon that this fund is too small to take care of borrowings of irrigation development corporations and financial engineering is required to take advantage of present low interest rate regime.

[17] In absolute term change has been marginal from Rs 1,68,712 crore in 2001 to Rs 1,66,116 crore in 2002.

Recent Developments

Under the debt-swap scheme between the Central government and the States, all state loans to the Government of India bearing coupons in excess of 13 per cent would be swapped (of the total stock of debt of Rs.2,44,000 crore owed by the states to the Government of India as on March 31, 2002, a little over Rs.1,00,000 crore bear coupon rates in excess of 13 per cent per annum) over a three-year period ending in 2005-06. It is envisaged that 20%, 30% and 40% of small saving funds will be used to retire high cost debt bearing more than 13% rate of interest and by 2005-06 all high cost debt will get swapped. The states are expected to save an estimated Rs 81,000 crore in interest, and deferred loan repayments, over the residual maturity period of the loans (RBI, 2003b). To provide extra resources to states the Central government is going to transfer the entire proceeds of small savings to the states. The scheme would also help to restrain the debt build-up in states through the small savings scheme. Further, interest rates on small savings as well as on States Plan loans were reduced by 50 basis points.

At the same time, the RBI has raised the maximum tenor of state government loans to 12 years from 10 years. All state governments have been offered to sell 'on-tap' 6.2% state development loan maturing on August 25, 2015. It makes good economic sense to lengthen the average maturity of loans when interest rates are low.

4.3. Reforms at local government level

Local bodies are responsible for drinking water, street lighting and local roads. 73rd and 74th Amendments have expanded their expenditure responsibilities without providing for commensurate power to raise resources. Local bodies in turn have looked for concessional loans from state governments or have abdicated responsibilities to departmental agencies operated by state governments. Most of the states constituted second finance commission to suggest funds transfer to local government bodies. Some states are in the process of constituting third finance commission. Accounting reforms and property tax reforms are important developments in local government sector[18].

5. Assessment of restructuring process

Analysis of public finances trend of recent past makes a bleak reading and on the face of hard evidence of past data there is no confirmation of restructuring of public finances. It seems that none of the recommendations of the EFC were implemented and governments, both at the Centre and States, are carrying on their business as usual. A generous critique could say that present governments are victim of their predecessors' misdeeds. Nothing could be further from the truth. One of the factors which prevented hard evidence of structural changes to be noticeable was that the economy operated below its full capacity.

In restructuring public finances, the EFC emphasised that the level of debt is unsustainable and fiscal deficit should be pared to 6.5 of GDP by 2004-05 (Para 3.18); the government expenditure should be counter-cyclical to economic growth and expenditure on social infrastructure should be raised from 2.1% of GDP in 1999-2000 to 2.9% of GDP by 2004-05 (Table 4). We assess the impact of the restructuring process on these three critical areas.

[18] As finances of local bodies are going to be dealt in detail, we shall not dwell on this. For details on property reforms see Mathur (Forthcoming), on municipal accounting reforms see Joshi (Forthcoming) and on recent developments on urban local bodies see Vaidya et. Al. (Forthcoming).

5.1. The level of debt and twin deficits

Analysis of public finances carried out by academics and international rating agencies and recent data on public finances provide no comfort on the progress of controlling twin deficits – revenue and fiscal – as suggested in the EFC report. In particular, the government has failed miserably in controlling revenue and fiscal deficits. But, considering that the economy was operating far below its potential between fiscal year 1999-2000 to FY 2002-03, the twin deficit may have provided counter-cyclical weight to the economy which may have resulted in gradual increase of deficits. Revenue targets as percentage of GDP were met but expenditure did not, mainly because interest outgo as percentage of GDP could not be reduced. The losses in power sector alone constitute well over 25% of total revenue deficits. These losses may reduce to 0.15% of GDP by 2006-07, if states are able to implement their respective Financial Turnaround Plan submitted to the Ministry of Power under our business as usual scenario.

A detailed analysis of institutional changes, restructuring of domestic and foreign debts, favourable macroeconomic conditions – low rate of inflation and interest rate – suggest that public finances are on the turning point. Conversion of ad-hoc treasury bills into dated securities illustrate that monetisation is under control as envisaged in the MOU between the RBI and the Central Government to eliminate the use of ad-hoc treasury bills to finance budget deficits. Repayment schedule for market loans and interest profile of outstanding central government securities reveal that interest burden would peak in 2010-11 in nominal terms, but the debt (% of GDP) is going to reduce substantially as debt on shorter-end is getting extinguished rather than growing (Table A2 and A3).

Whereas the EFC included only direct government liabilities in fiscal deficit, Kapur and Patel (2003) included all public sector liabilities including contingent liabilities[19]. It is the centre's revenue deficit which is at the centre of growing fiscal deficit and to macro-manage the economy to ensure stability, adequate fiscal corrections must take place. Burden of adjustment must be shared by the centre and states for sustained growth. A sustainable fiscal-financial-monetary plan will be a painful one and despite fiscal adjustment undertaken in mid-nineties solvency is not assured[20]. A primary surplus of four and half percentage points is required to stabilise the debt-GDP ratio and long term real growth rate must exceed long term real interest rate by one percentage point to succeed in closing more than half of the primary deficit (Buiter and Patel, 1997).

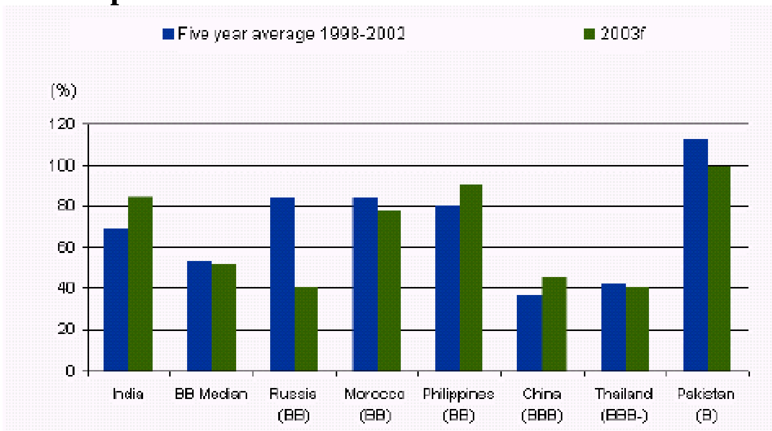
According to Standards and Poor rating agency fiscal deficits and the debt burden of India are worse than the similarly rated countries[21]. It is the gross general government debt/GDP excluding guarantees which have climbed to 84% of GDP from the five year average (1998-2002) of approximately 67% which is worrisome to the rating agency (Graph 1).

[19] In the S&P study general government fiscal deficit is taken. Inclusion of public sector liabilities provides a broad measure of fiscal deficit. Level of states deficit are not dealt with separately.

[20] Solvency is defined in terms of ability to meet debt service obligations.

[21] India's rating on long-term local as well as foreign currency is BB+ and outlook is negative. Outlook was revised from positive to negative in September 2002.

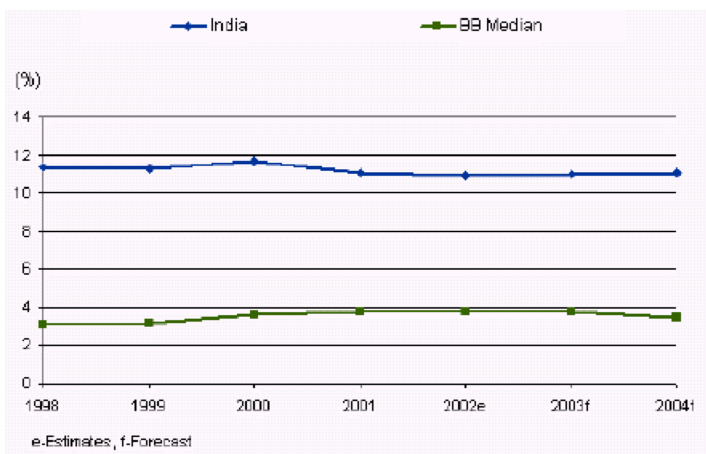
Graph 1 – Gross General Government Debt/GDP



Source: S&p (2003)

Domestic debt in the BB+ rated countries is 45% of GDP and fiscal deficit is below 2.5% of GDP (Graph 1 and 2). In India, in contrast the general government deficits have persistently remained in the range 9%-10% of GDP in the past few years leading to an erosion of fiscal flexibility (Graph 2).

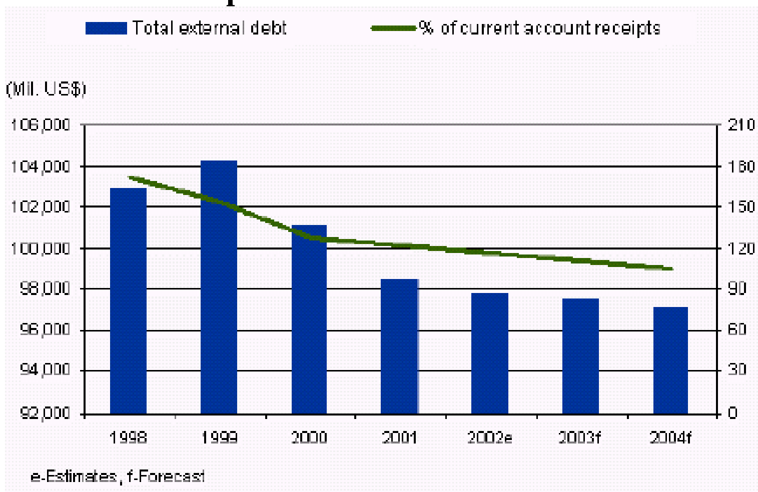
Graph 2 – General Government Fiscal Deficit/GDP



Source: S&p (2003)

General government guarantees still account for about 11% of GDP in March 2002, of which guarantees by state governments alone were 8.1% of GDP (S&P, 2003).

Graph 3 – Total External Debt



Source: S&p (2003)

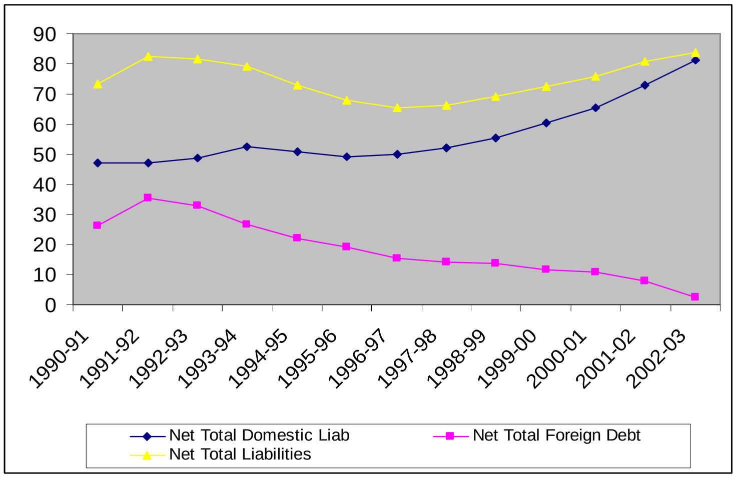
The size of the external debt burden in India has been falling since fiscal year 2001 because of better access to the credit and lower interest rates in the domestic markets. Total external debt is estimated to fall to US$98.7 billion or 117% of current account receipts, at the end of fiscal year 2002, from a peak of 338% in fiscal 1992. All but 3% of external debt is medium- and long-term debt, making India's external debt payments less vulnerable to the volatility of short-term interest rate (Graph 3). The government used reserves to repay expensive multilateral debt. Various private sector firms have also raised domestic debt recently to retire expensive external debt. The general government has become a net external creditor from the end of fiscal year 2001.

Nevertheless, the high foreign exchange reserves do not make it easier for the government to pay its debt as payment comes from government revenues ultimately. The reserves make it easier for the government to buy dollars using its rupee revenues in order to service external debt. In the absence of rupee revenues, the government borrowed dollars from the RBI and substituted domestic for external debt. The outstanding liabilities of the public sector – the broadest measure of debt – is growing since 1996-97 (Kapur and Patel, 2003). Their calculations show that net total foreign debt has reduced from 35.6% of GDP in 1991-92 to 2.5% of GDP in 2002-03 whereas net total domestic liabilities over the corresponding period have increased from 46.9% to 81.4%. Net total liabilities of the public sector which had shrunk to 82.5% in 1991-92 to 65.4% in 1996-97 have again ballooned to 83.9% in 2002-03!! (Graph 4).

It is the growing net total domestic liabilities at a rapid pace which is worrisome to rating agencies. It is worth noting that countries have defaulted on their internal debt even when they had sufficient foreign exchange reserves because debt service was taking up too much of government spending and the government decided (as in Russia) to reschedule its debt. Hence, there is little doubt that stock of debt is quite high and retiring of debt gradually is an option which must be explored vigorously.

To provide legislative backing to deficit control, the FRBM Act 2003 is an honest attempt to bring transparency to fiscal governance at the Central government level. However, the government is absolved of all its responsibilities if it fails to achieve the pre-announced targets. Thus, the Act which could have teeth to gnaw fiscal deficits, has been reduced to a mere statement of intent.

Graph 4 - Outstanding Liabilities of the Public Sector (% of GDP)



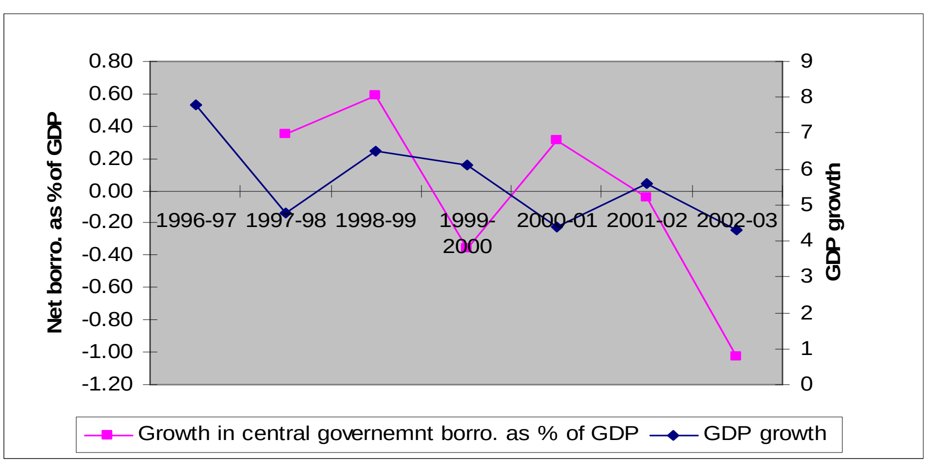
Source: Kapur and Patel (2003)

Apart from restructuring of debt to reduce outgo on interest, expenditure needs to be reduced. The Expenditure Review Commission reports on almost all the central government departments to cut wasteful expenditure, however, have not been implemented in spirit. Similarly at the state level, notwithstanding the central government's attempts to revive irrigation schemes, experience has shown that the present system, whereby the government assumes the responsibility of design, evaluation, financing and construction of irrigation systems as well as their continuing management wholly through its bureaucracy, is incapable of completing the projects in time. The entire process at every stage is far too opaque, open to interference and manipulation, without any effective incentive or mechanism to ensure economical use of resources in construction and management or to ensure that costs are fully recovered.

5.2. Counter-cyclical government expenditure

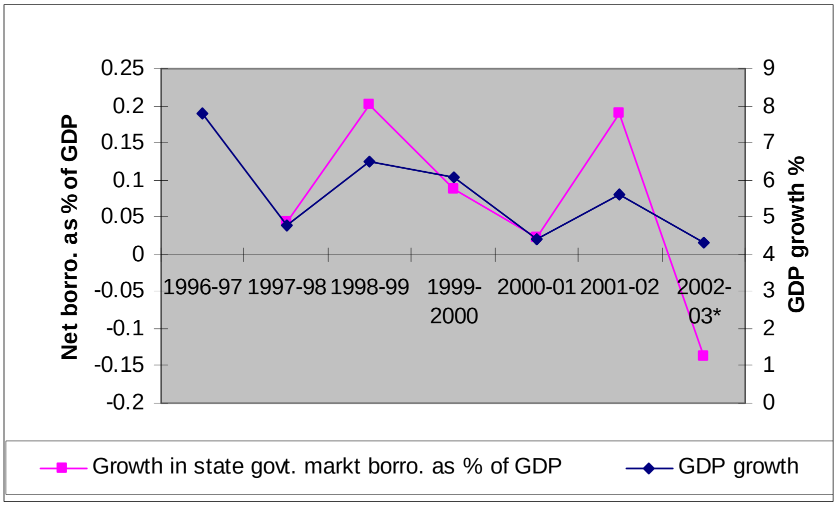
The rationale behind counter cyclical government expenditure is that when economic growth is not at its full employment level and there is demand compression at macroeconomic level, the government should be expansive and lean against the wind to decompress demand. The growth in central government market borrowing is taken to measure the central government stance to analyse if the government expenditure has been counter-cyclical (Graph 5).

Graph 5 – Growth of Central government market borrowing and GDP



The analysis of market borrowing of 1996-97 to 2002-03 shows that the fiscal policy has been countercyclical in the last few years (Table A1 and Graph 5). Prior to 1999-2000, it moved in tandem with GDP growth and since 1998-99 it is counter- cyclical[22].

Graph 6 – Growth of State governments market borrowing and GDP



State government net market borrowing has been waxing and waning in tandem with GDP growth rate (Graph 6). A large part of state governments' expenditure being pre-committed in interest payments, salary, pension etc. they have little room to alter its expenditure. Thus, state governments are obliged to meet their expenditure commitments. They tighten their belt on social and infrastructure expenditure which continues during the expansion phase of the economy as well. It may be noted that states market borrowing in the recent past may have been affected by restructuring of their debt by the RBI.

5.3. Social expenditure and reforms at local government level

The main impact of high fiscal deficit has been short of resources to spend on social infrastructure such as education, health, water supply and sanitation. Revenue and fiscal deficit remained high and the impact of expenditure compression fell on social infrastructure (Table 4).

The ad-hoc support provided by state governments to local government has increased over the 1980s the 1990s. State finance commissions which derive their authority from the 73rd and 74th amendments recommended devolution of funds to local government. The finance commission (FC) based transfers have been robust to change in government, and to different parties existing at different levels of the government. This has provided some relief to social expenditure, however, there is a wide gap between their expenditure and their own resource base. The FC based transfers have opened possibility of securitisation of grants from states to pay for social infrastructure and not depend on the whims and fancies of state administration.

[22] It is worth noting that the European Union's stability pact which mandates a fiscal deficit of 3 per cent for member states has been widely criticised for its ineffectiveness in boosting domestic demand. In fact, Stiglitz has commented that to insist on an arbitrary budgetary position in an economic downturn is to ignore all what we have learnt about economic stabilisation in the past seventy years [*Don't trust the bankers' homilies : The EU stability pact destabilises by cutting spending in a downturn* by Joseph Stiglitz (The Guardian, May 9, 2003)].

6. Three scenarios

In the next few years the debt restructuring of the economy is going to have a favourable impact on government budget constraint as well as fiscal deficit. A small macroeconomic model with government budget constraint built into it will be useful to predict main fiscal variables. The model can be used to forecast macroeconomic variables of the economy in short- and long-term as well. A model which takes into account impact of taxes, subsidies and other government interventions which influence the productive capacity of the economy can be effective in understanding likely unfolding scenario. A model which can predict government spending for a given target of fiscal deficit and tax rate can be useful in determining capital spending of the government[23].

We have used a static model to develop three scenarios – Business-as-usual, Medium growth and High growth scenario based on assumptions relating to GDP growth, inflation and bank rate. Combined government receipt, expenditure and plan outlay are projected using three year moving average rate of growth. Similarly, central government fiscal variables – revenue receipts, tax receipts, direct and indirect taxes etc. have been projected. However, in government expenditure and outstanding internal debt, increase/decrease in interest outgo has been factored in.

6.1. Business-as-usual

Main assumptions in this scenario relate to GDP growth of 5.5%, inflation growing at 4.5% and bank rate continues to be 5% p.a. Maintaining inflation rate constant satisfies the criterion of the macroeconomic stability.

Table 5: Macroeconomic Growth under Business-as-usual Scenario

		2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Assumptions								
GDP at factor cost	% change	6.5	5.5	5.5	5.5	5.5	5.5	5.5
WPI all commodities	% change	4.5	4.5	4.5	4.5	4.5	4.5	4.5
Bank rate (March-end)	%	5.8	5	5	5	5	5	5
Main fiscal variables (Combined government)								
Government receipts	% of GDP	33.2	33.8	34.4	35.0	35.7	36.3	37.0
Government expdt	% of GDP	34.0	34.7	35.6	36.5	37.4	38.3	39.3
Plan outlay	% of GDP	10.2	10.6	11.0	11.5	12.0	12.4	12.9
Central Govt								
Interest	% of GDP	4.5	4.3	4.1	3.9	3.7	3.6	3.4
Revenue deficit	% of GDP	4.1	4.1	4.0	3.9	3.8	3.8	3.7
Gross fiscal deficit	% of GDP	5.6	5.6	5.3	5.2	5.1	4.9	4.8
Outstanding internal debt	% of GDP	48.6	49.4	50.2	51.1	49.2	46.6	43.2

Growth of combined government tax revenues which lagged behind that of government expenditure by about 0.8 percentage point will widen to 2.3 percentage point of GDP. At the

[23] A model developed on these lines is Rastogi (1994). A Monte Carlo simulation can be used to estimate the range of economic variable outcome rather than point estimates. To be used productively to carry-out counter-factual and as-if scenario, it needs re-estimation to take advantage of recent information.

combined government level, expenditure is growing steadily because of increase in plan expenditure even though there is a gradual reduction in interest outgo. Outstanding internal debt peaks at 51.1% of GDP before reducing step by step as interest burden eases progressively.

6.2. Medium growth scenario

Main assumptions in this scenario relate to GDP growth of 7% per annum, inflation rate growth at the rate of 4.5% per annum – same as that of the Business-as-usual scenario. Bank rate is assumed to be 5.5% per annum – fifty basis point more than the Business-as-usual scenario.

Table 6: Macroeconomic Growth under Medium Growth Scenario

		2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Assumptions								
GDP at factor cost	% change	6.5	7	7	7	7	7	7
WPI all commodities	% change	4.5	4.5	4.5	4.5	4.5	4.5	4.5
Bank rate (March-end)	%	5.8	5.5	5.5	5.5	5.5	5.5	5.5
Main fiscal variables (Combined government)								
Government receipts	% of GDP	33.2	33.3	33.5	33.6	33.8	34.0	34.1
Government expdt	% of GDP	34.0	34.3	34.7	35.1	35.4	35.8	36.2
Plan outlay	% of GDP	10.2	10.5	10.7	11.0	11.3	11.6	11.9
Central Govt								
Interest	% of GDP	4.5	4.2	4.0	3.8	3.6	3.4	3.2
Revenue deficit	% of GDP	4.1	4.0	3.9	3.7	3.6	3.5	3.4
Gross fiscal deficit	% of GDP	5.6	5.5	5.2	5.0	4.8	4.6	4.4
Outstanding internal debt	% of GDP	48.6	48.2	47.7	47.0	43.6	39.7	35.2

Combined government receipt and expenditure as percentage of GDP is lower even though in absolute money terms both are same as that of the earlier scenario. At the central government level outstanding internal debt in money terms reduce marginally but as a proportion of GDP is eight percentage points[24]. Even though gross fiscal deficit targets suggested by the EFC are not met, the outstanding internal debt is just met by 2009-10.

6.3. High growth scenario

Main assumptions in this scenario are average growth rate of 8% per annum, inflation of 5% per annum – 50 basis points more than the earlier scenario and bank rate of 6% per annum – 100 basis points more than the Business-as-usual scenario. Rationale for slightly higher rate of inflation and bank rate is that the economy may hit capacity constraint, if it grows at 8% per annum on sustained basis. Hence, certain amount of inflationary pressure is likely to build up and there will be some squeeze on credit availability as well.

Although there is no change in combined government receipts and expenditure in absolute terms but as percentage of GDP there is approximately 5.5 percentage point change compared to the

[24] A non-econometric model projection has an inherent problem. A different projection is available from rating agency Crisil. Their report on state finances has estimated that debt of all the states is expected to double to Rs 12,00,000 crore by 2007 from Rs 5,89,000 crore on March 31, 2002. Crisil predicts that the indebtedness (debt plus guarantees) of states in relation to their revenue receipts will increase from 2.8 times in 2002 to 3.6 times in 2007 (Business Standard, July 16, 2003).

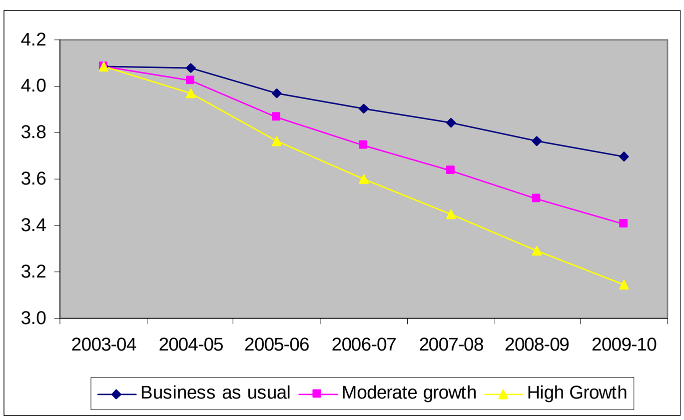
Business-as-usual scenario. Only under this scenario government receipts and expenditure as percentage of GDP are lower than the base year (2003-4). There is a direct impact on interest outgo as percentage of GDP and outstanding internal debt as percentage of GDP reduce by more than fourteen percentage points by 2009-10. Under this scenario the internal debt norms envisaged in the EFC report (Para 3.20) are met by 2008-09, but revenue deficit norms envisaged under FRMB act for the central government are far from the target.

Table 7: Macroeconomic Growth under High Growth Scenario

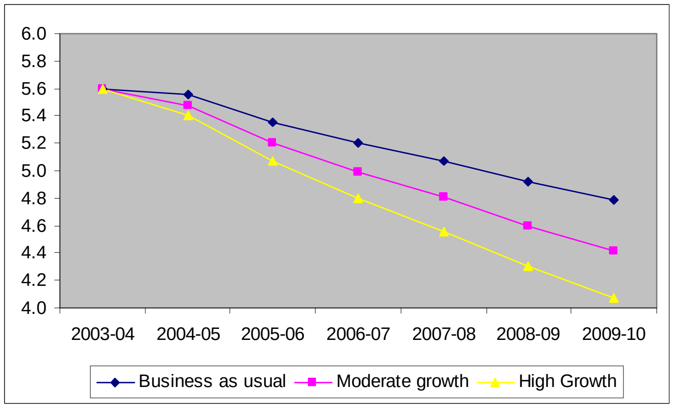
		2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Assumptions								
GDP at factor cost	% change	6.5	8	8	8	8	8	8
WPI all commodities	% change	4.5	5	5	5	5	5	5
Bank rate (March-end)	%	5.8	6	6	6	6	6	6
Main fiscal variables (Combined government)								
Government receipts	% of GDP	33.2	32.9	32.6	32.3	32.0	31.8	31.5
Government expdt	% of GDP	34.0	33.8	33.8	33.7	33.6	33.5	33.4
Plan outlay	% of GDP	10.2	10.4	10.5	10.6	10.7	10.9	11.0
Central Govt								
Interest	% of GDP	4.5	4.2	3.9	3.7	3.5	3.3	3.1
Revenue deficit	% of GDP	4.1	4.0	3.8	3.6	3.4	3.3	3.1
Gross fiscal deficit	% of GDP	5.6	5.4	5.1	4.8	4.6	4.3	4.1
Outstanding internal debt	% of GDP	48.6	47.1	45.3	43.3	38.8	33.9	28.8

Reduction in non-plan expenditure as percentage of GDP, but not in nominal terms, is in agreement with the observation that increased provision to social sectors and physical infrastructure can be made only when the slide in the revenue-GDP ratio is reversed (Rao, 2002).

Graph 7 – Revenue Deficit as percentage of GDP



Graph 8 – Fiscal Deficit as percentage of GDP



Source : Tables 5, 6 and 7

A comparative presentation (Graph 7 and 8) of revenue and fiscal deficit as percentage of GDP shows that the two deficits decline faster as economy grows at a faster pace. Fiscal deficit under this static model mimics changes in revenue deficit.

7. Proposals for restructuring of public finances

It has been argued that the institutions of intergovernmental relations have generated perverse incentives and fiscal indiscipline among states (Anand, Bagchi and Sen, 2001). The vertical imbalance which exists in Indian federal structure got further exacerbated as Indian economy opened up and increasingly depended on market based rules administered by the central bank. Before the economic reforms, the statutory institution of finance commission attempted to reduce the vertical imbalance and the horizontal disparities. It functioned well in the past as transfers were rule based and transparent. Another institution – the Planning Commission - the allocative machinery to direct savings of the economy into productive resources, also allocated resources largely based on well understood formula. The two inter-governmental institutions have continued to function in the same fashion with some minor variations, but their allocations have been questioned recently as states have to attract private investment based on economic and social infrastructure available in the state. The 73rd and 74th Amendments to the Constitution have exacerbated the vertical imbalance and fiscal health of public finances. A few developments in local government finances are noteworthy and need to be highlighted as they hold promises in the future.

7.1. Reforms in transfers to states

In India, transfer from the Centre to States constitutes a large proportion of Planning Commission transfers. Plan/non-plan distinction is non-operational. Linkage between loan disbursement from the Planning Commission for capital projects and actual spending on capital projects is weak.

Capital expenditure under plan and non-plan has given rise to step-motherly treatment to the maintenance of physical assets created under plan heads. In the coming years as states are expected to raise part of the resources from the capital market, it should be left to the market to assess viability of economic infrastructure projects. Social infrastructure and maintenance which bears the burden of cuts in revenue expenditure may benefit from abolition of artificial distinction between plan and non-plan expenditure. Rethinking on institutional role of the state planning bodies and the central Planning Commission needs to be undertaken when allocations of resources are guided by markets.

Prior to the implementation of MTFRP, states had an incentive to launch new programmes to qualify for loan and grant financing under their respective state plans for the first few years, after that they get transferred to non-plan account and, thus, required to be supported by general purpose grants from the Centre or their own resources (McCarten, 2003). The co-ordination between state plans and finance commission transfers has begun since 2002-03.

Traditionally, projects and schemes meant for states were used to be location specific or project specific. To finance planned projects, financial resources were available to states from state owned/controlled financial institutions and the institutions assumed that the due diligence has been done by the Planning Commission. This method suited nationwide plan allocations carried out by the Central Planning Commission. The fall-out of this methodology under a market based allocation system produced structural infirmities which have been addressed by the RBI and the Central government (RBI, 2002 and 2003c). The new trend in transfers from Centre to states is that they are becoming increasingly sector-specific and are based on reform conditionalities (output performance)[25]. As a result total transfer to states may be able to balance redistributive demand of states without being regressive[26]. For example, APDRP and Urban Reform Incentive Fund are sectoral initiatives and outside the Gadgil formula. Hence, the role of the Planning Commission and State Plans needs to be considered carefully in the emerging scenario. Reform conditionalities must be crafted carefully. For example, under the States' Fiscal Reform Facility, now part of MTFRP of most of the states, targets are same for all states having revenue deficits. These targets for fiscally better off states is stiffer than worse off states. The Finance Commission should recommend a trajectory for reduction in revenue deficit so that efforts made by states commensurate with the incentive provided to them from the facility.

7.2. Devolution as a proportion of tax receipts or fixed-sum

In order to raise accountability and to contain fiscal imbalances, the intergovernmental transfers could be broadly divided into specific-purpose and general-purpose grants. General purpose grants have been allocated as proportion of revenue collected by the centre using a pre-determined formula suggested by the Finance Commission.

When the economy has not been functioning at full employment level, revenue collections fall and these transfers in absolute terms shrink and result in higher revenue deficit of state governments. Further, the management of cash-flows at state level becomes difficult, given the nature of transfers. The State Finance Secretaries generally agree that two of the major factors contributing to liquidity problems, even after discounting the adverse impact of the deficit are, (i) the abrupt shortfalls in actual monthly transfers from the Central government to the states as compared to the budget estimates and, (ii) the bunching of releases of Plan funds for the Central Sector and Centrally-sponsored schemes, especially in the last quarter of the financial year. The

[25] Needless to say that wherever conditionalities and performance criteria are not well thought of, the central government budget announcements remain on paper. Consequently, there are no projects and no transfers.

[26] Table A11 and A12 – APDRP funds utilization 2002-03 and progress of Pradhan Mantri Gram Sadak Yojana – both sector-specific and incentive based schemes – support this argument.

latter, generally released in the last quarter, exacerbate liquidity problem as expenditure is incurred uniformly throughout the year (RBI, 2003c).

Moving from general purpose grants to specific purpose grants is going to worsen this further as 'tied' grants strap hands of the recipient states. The states have also complained that a larger share of plan finances is given as earmarked funds on Centrally-sponsored schemes, that too outside the Consolidated Fund of the State, and that only a smaller share is being received as untied Plan loans (RBI, 2003c). This view is in line with the observations that states have often expressed a preference for tax devolution because of in-built buoyancy in tax receipts (Sen, 2000). This is true when economy is growing at a higher clip, but reverse happens during economic downturn.

The method of transfer is an issue which needs to be addressed. Given the similarities in fiscal structure of India and Australia, we should take a leaf from their book. Enforcing a hard budget constraint is probably not a feasible solution for India at this stage of economic development and of bond market (Box 1 – Best Practices in Fiscal Federalism). A middle way is that transfers are divided into two parts. First is a fixed part which is in line with the committed revenue expenditure of the state i.e. expenditure on social infrastructure and interest. And second part of transfer is project specific which is disbursed in line with the conditionalities placed on these transfers with or without incentives[27].

The sector specific transfers based on output-based rather than input based measures can be best illustrated from the AIBP and APDRP. The AIBP which is project specific but without any output-based performance measure has shown no visible result. Irrigation subsidies are unlikely to show any improvement in the near future. The unholy nexus between co-operative banks and irrigation development corporations needs high level political commitment to crack this problem. A debt restructuring programme on the lines of 'one time settlement of SEB dues' at individual state level is required to ease burden on state government budgets without having unfavourable fall out from co-operative bank depositors[28].

Box 1 - Best practices in fiscal federalism

One of the main issues at sub-national government level is the absence of hard budget constraint. Federal governments do not allow sub-national governments to go bankrupt which give rise to time-inconsistency problem and the budget constraint becomes flexible. It has been argued and widely acknowledged that fiscal discipline at the sub-national government level can be brought about by the 'market' or market-like mechanisms supported by bond rating agencies. Pre-requisite for this is a well developed and well regulated capital market. However, most federal countries do not rely on market mechanism to restrain sub-national debt. Among all federal countries, sub-national governments of USA and Canada only depend entirely on the market for their resources. These two countries also had to go through a painful process to acquire credibility and judge the resolve of federal government on no-bailout commitment (Ma, 1997). A lesson here for India is that if it is to rely entirely on market mechanism, a painful process to show the central government resolve will be necessary.

Australia is another federal country whose system of transfer to states is much admired. Out of total government revenue approximately two-third goes to federal government and one-third goes to states. Federal government needs only 50% of its revenue and hence 50% of federal government revenue is distributed through various forms of transfers to states and local governments. In 1999-2000, about 50 per cent of the total federal transfer was general purpose grants and the rest were specific purpose grants (Searle, 2002). The Commonwealth Grants Commission – a permanent statutory body – distributes general purpose grants using a formula that measures states' fiscal capacity and its fiscal need.

[27] See para 3.58 b of the EFC for a different view.
[28] Raising resources for irrigation development corporations in Maharashtra is a typical example of this type of borrowing resorted to by states (WB, 2002).

On the other hand, APDRP which is sector specific with output based performance measures has started showing reduction in cash losses (Section 4.2.2). Moreover, the performance based fiscal transfers recommended by the finance commission could set an example for state finance commissions for transfers to local government bodies. Such targeting would ensure that wherever user charges have to be levied, they must be levied and must be monitored. The Finance Commission decision in this regard can help targeting of social expenditure. Under this method, a certain proportion of transfers will be progressive and improve efficiency of resources.

7.3. Implementation of VAT

Apart from reforming the transfer system, it is important to plug the vertical gap by assignment of tax powers to states. This would reduce the burden placed on the transfer system. It is generally accepted that the competition among states to give incentives for industrialisation has only resulted in a ‘race to the bottom’. To attract industries, states provided multi-year sales tax exemptions to industries. One of the reasons for states’ inability to improve their own tax collections as percentage of GDP is that they have mortgaged future tax revenues already. With the 89th Amendment to the Constitution, the revenue from the central tax on services is also becoming available for sharing of taxes and services have been allowed to be taxed by states as well. With the production and consumption of services coming within the tax net, the buoyancy in states’ taxes as well as expansion of tax base will get improved as states will be able to levy VAT on services.

The introduction of destination based VAT in all the states is an important reform. Compared to present indirect tax system at the Centre and states, VAT is comparatively a simple, transparent and rule based tax system. In addition to changing the overall structure of commodity taxes in the country, the implementation will have a direct impact on widening the tax base for the Centre as well as states. The management information system required to implement the VAT successfully in the country would make tax avoidance difficult and there is an in built incentive for tax compliance. It will be beneficial for the government as well as for honest tax payers. India, like other federal governments, would face difficulty in harmonising tax on inter-state trade while implementing VAT but these complexities are not insurmountable (Purohit, 2002). The transition to a VAT system in India has not come about due to expected loss in revenues, administrative difficulties without much computerisation, resistance from tax payers and the problem of border adjustment in place of the central sales tax (Purohit, 2001). Nevertheless, VAT is growing in importance as a national tax around the world and at the sub national level. Main reason is that user charges and property tax usually preferred for financing local governments are difficult to implement and are not able to fill the fiscal gap where major spending responsibilities of local governments are in social areas such as drinking water, health and education (Bird, 2000).

It is disheartening that broad-based tax reforms have not kept pace with liberalisation in financial markets, banking sector and goods market. Restructuring of indirect finances, especially, implementation of VAT in the country can expand the tax base further. An expanding tax base in the medium term at the state and local government level would lessen the burden placed on federal transfer to provide resources to meet expenditure needs of the social as well as economic sectors.

8. Conclusion

The Eleventh Finance Commission (EFC) had recommended restructuring of government finances which would usher into macroeconomic stability by 2004-5. The Commission emphasised that revenue deficit must be reduced at an accelerated pace to reduce fiscal deficit and to make resources available for social infrastructure. At full employment level there should be surplus on revenue account and stock of debt should be around 55% of GDP. In the past few years restructuring of debt – domestic as well as foreign – has gained momentum. There is a distinct shift in refinancing of high cost debt which is going to reduce revenue deficit as proportion of GDP in the coming years. Inflation is under control and the central bank has taken advantage of the development to reduce bank rates signalling reduction in interest rates on savings – contractual as well as voluntary one – which underpinned market interest rates.

Liberalization of economic markets and strengthening of federal structure of India has made the environment ripe for more institutional reforms including strengthening of 'hard budget' constraints, especially, for states. Implementation of FRBM and MTFRP, restructuring of debt, introduction of user pays principle for power and sector specific conditional loans and grants to states would show results in medium term. Subsidies related to irrigation development schemes still remain a knotty problem in some states. However, the debt obligations for most states under MTFRP are manageable in medium term and should help states in controlling their fiscal deficits.

Revenue and fiscal deficits have remained stubbornly high. Our analysis shows that the high level of debt would continue to plague revenue deficit and would only ease gradually by 2010 unless there is a spurt in economic growth on a sustained basis. Consistent economic growth rate of 8% per year – which would make the economy grow at its full employment level – would see the deficit targets as well as expenditure level being met in medium term.

With the production and consumption of services coming within the tax net, the buoyancy in states' taxes as well as enhancement of tax base will get improved as they will be able to levy VAT on services. The in-built fiscal gap between centre and states has placed enormous pressure on federal transfers. Assignment of taxation power is one area, especially through VAT on services, that will help in filling the gap partly.

Capital expenditure under plan and non-plan has given rise to the neglect of maintenance of physical assets created under plan heads. Although, central government expenditure seems to be counter-cyclical, it has not helped states. So far, during economic downturn lower revenue transfers to states have exacerbated their revenue deficits and capacity to spend on social infrastructure. Social infrastructure and maintenance which bear the burden of cuts in revenue expenditure may benefit from abolition of artificial distinction between plan and non-plan expenditure. Rethinking on institutional role of the state planning bodies and the central Planning Commission needs to be undertaken when allocations of resources are guided by markets. Transfer to states partly as fixed sum and the rest linked to specific programme/project – with or without incentive payment – can ameliorate the cascading effect of lower than anticipated revenue collection. There is a need to break the nexus between state governments revenue deficit with that of the Central government by making 'committed' expenditure on social infrastructure free from economic growth cycle. Incentive based transfer to sector-specific and project specific is required to improve productivity of capital expenditure.

Legislative and administrative changes required to contain revenue and fiscal deficits are in place. Its implementation in medium term, assuming continuation of favourable macroeconomic scenario – moderate interest and inflation rates – will reduce the deficits. Now, the main issues in restructuring of public finances are implementation of VAT, rethinking on the role of intergovernmental institutions responsible for allocation of resources and mechanism of transfer to states for their capital expenditure.

Appendix

Table A1 - Market Borrowings and Coupon Rates on Central Government Dated Securities

Fiscal Year	Outstanding dated securities (Rs Cr)	Conversion of Ad-hoc Treasury Bills (Rs cr)	Total Outstanding (Rs Cr)	Weighted Average Yield (%)	Growth of central government debt as % of GDP	GDP growth	GDP (Rs Cr)
1996-97	6666	121818	128484	13.69		7.8	1368200
1997-98	31977	101818	133795	12.01	0.35	4.8	1522500
1998-99	42212	101818	144030	11.86	0.59	6.5	1740900
1999-2000	35190	101818	137008	11.77	-0.36	6.1	1933700
2000-01	41732	101818	143550	10.95	0.31	4.4	2104300
2001-02	40927	101818	142745	9.44	-0.04	5.6	2296000
2002-03	55438	61818	117256	7.34	-1.03	4.3	2472800
2003-04*	83574	41818	125392	5.94			

Source : RBI (2003b)   * As on August 1, 2003

Table A2 – Repayment Schedule for Market loans of Central Governments as of August 2003

Fiscal Year	Amount of Repayment (Rs. Crore)	GDP in line with Business as usual scenario	% of GDP
2003-04	32910	2744800	1.20
2004-05	34316	3019279	1.14
2005-06	35631	3321207	1.07
2006-07	36894	3653328	1.01
2007-08	41151	4018660	1.02
2008-09	40223	4420526	0.91
2009-10	45195	4862579	0.93
2010-11	53109		
2011-12	45610		
2012-13	46255		
2013-14	40191		
2014-15	27588		
2015-16	36857		
2016-17	36130		
2017-18	37000		
2018-19	16632		
2019-20	11000		
2020-21	11000		
2021-22	13213		
2022-23	13000		
2026-27	15000		
2032-33	5000		

Source : RBI (2003b) & Table 5

Table A3 - Interest Rate Profile of Outstanding Central Government Securities as of March 31, 2003

Range of Interest Rate (%)	Outstanding (Rs Cr)	% to Total
5.73 - 5.99	12378	1.84
6.00 - 6.99	44684	6.63
7.00 - 7.99	79654	11.82
8.00 - 8.99	29643	4.40
9.00 - 9.99	51992	7.72
10.00 – 10.99	84572	12.55
11.00 – 11.99	212243	31.49
12.00 - 12.99	125047	18.56
13.00 - 14.00	33692	5.00
Total	673905	

Source : RBI (2003b)

Table A4 - Actual Disinvestment from April 1991 onwards and Methodologies Adopted

Year	No. of Companies in which equity sold	Target receipt for the year (Rs In Crore)	Actual receipts (Rs In Crore)	Methodology
1999-00	4	10000	1829	GDR—GAIL VSNL-domestic issue, BALCO restructuring, MFIL's strategic sale and others
2000-01	4	10000	1870	Strategic sale of BALCO, LJMC; Takeover - KRL (CRL), CPCL (MRL), BRPL
2001-02	9	12,000	5632 #	Strategic sale of CMC – 51%, HTL –74%, VSNL – 25%, IBP – 33.58%, PPL-- 74%, and sale by other modes: ITDC & HCI; surplus reserves: STC and MMTC
2002-03	5	12,000	3348 #	Strategic sale of JESSOP-72%, HZL – 26%, MFIL-26%, IPCL – 25% and other modes : HCI, Maruti
2003-04	3	13,200	993#	
Total	**49 ***	**91,500**	**30484 #**	

* Total number of companies in which disinvestment has taken place so far.

\# Figures (inclusive of amount expected to be realised, control premium, dividend/dividend tax and transfer of surplus cash reserves prior to disinvestment etc.)

Source : www.disinvest.nic.in

Table A5 - Strategic Sale of PSEs Year 2000 Onwards

Sr.No	Name of PSE	Date	Ratio of paid up Equity Sold %	Face Value of Equity Sold (Rs. in Crore)	Realisation (Rs. Crores)
1	Modern Foods	Jan-00	(i) 74	9.63	105
			(ii) 26	3.38	44
2	LJMC	Jul-00	74	0.7	2.53
3	BALCO ^	Mar-01	51	112.52	826.5
4	CMC	Oct-01	51	7.73	152
5	HTL	Oct-01	74	11.1	55
6	VSNL ^	Feb-02	25	71.2	3,689
7	IBP	Feb-02	33.6	7.4	1,153.70
8	PPL	Feb-02	74	320.1	151.7
9	Jessop*	Feb-02	74	68.1	18.2
10	HZL	Apr-02	26	109.8	445
11	IPCL	May-02	26	64.5	1,490.80
12	Maruti Udyog	May-02	27.5	39.73	1,993
13	ICVL**	Apr-03	51	6.21	16
14.-16	HCI (3 Hotels)	2001-02 various dates	100	14.7	242.5
17. -35	ITDC (19 Hotels)	2001-02 various dates	100	27.1	444.1
	Total			900.17	11,260.23

^ Including dividend & Divi. Tax/withdrawal of surplus cash prior to disinvestment.

* Subject to court order. ** Subject to BIFR approval.

Source : www.disinvest.nic.in

Table A6 - Status of investment in State Level Public Enterprises as on 31.03.2001

Sr. No.	Name of the State	Approximate number of State Level Public Enterprises (SLPEs)	Estimated total investment in SLPEs (Rs in crore)	Net Accumulated Loss * (Rs. in crore)	Approximate number of loss making SLPEs	Approximate number of non-working SLPEs
1	Andhra Pradesh	128	48794	2919	62	9
2	Assam	42	3649	2792	28	10
3	Delhi	N/A	N/A	N/A	N/A	N/A
4	Goa	12	4869	730	N/A	N/A
5	Gujarat	54	23438	965	N/A	N/A
6	Haryana	45	443	384	10	4
7	Himachal Pradesh	21	3143	369	12	2
8	Jammu & Kashmir	N/A	N/A	N/A	N/A	N/A
9	Karnataka	76	19295	811	37	13
10	Kerala	109	9805	1124	52	13
11	Madhya Pradesh	26	7923	600	8	15
12	Maharashtra	65	22477	N/A	28	17
13	Manipur	14	N/A	N/A	10	N/A
14	Orissa	68	9796	1180	18	34
15	Punjab	53	12425	847	25	23
16	Rajasthan	24	11576	261	6	3
17	Tamil Nadu	59	6192	N/A	33	12
18	Uttar Pradesh	41	17773	5327	21	19
19	West Bengal	82	18241	5068	59	6
		919	219839	23377	409	180

N/A - Not available

Source: State Government, IPE, Hyderabad and other sources (www.disinvest.nic.in)

Table A7 – Disinvestment in states

Sl. No	Name of the State	Approximate number of State Level Public Enterprises (SLPEs)	SLPEs identified for disinvestment / winding up / restructuring	No. of SLPEs in which process initiated	No. of SLPEs privatised	No. of SLPEs closed down
1	Andhra Pradesh	128	87	79	12	12
2	Assam	42	N/A	N/A	-	-
3.	Delhi	N/A	N/A	1	1 *	-
4	Goa	12	2	2	2 ^	-
5	Gujarat	54	24	24	1	6
6	Haryana	45	22	13	1	12
7	Himachal Pradesh	21	15	5	3	2
8	Jammu & Kashmir	N/A	7	2	-	2
9	Karnataka	76	20	20	2	11
10	Kerala	109	12	-	-	-
11	Madhya Pradesh	26	14	14	1	-
12	Maharashtra	65	6	4	-	-
13	Manipur	14	10	N/A	-	-
14	Orissa	68	27	27	8	11
15	Punjab	53	10	10		5
16	Rajasthan	24	10	6	1	1
17	Tamil Nadu	59	13	3	-	12
18	Uttar Pradesh	41	9	9	-	-
19	West Bengal	82	2	2	1 #	-
	TOTAL	919	290	221	33	69

Source : www.disinvest.nic.in

Table A8 - Market Borrowings and Coupon Rates on State Government Dated Securities

Fiscal Year	Net Market Borrowing (Rs Crore)	Weighted Coupon/Cut-off Yield (%)	Growth in state governments debt as % of GDP	GDP growth
1996-97	6536	13.83		7.8
1997-98	7193	12.82	0.043	4.8
1998-99	10700	12.35	0.201	6.5
1999-2000	12405	11.89	0.088	6.1
2000-01	12880	10.99	0.023	4.4
2001-02	17261	9.2	0.191	5.6
2002-03*	13874	7.49	-0.137	4.3

* Upto January 31, 2003
Source : RBI (2003a)

Table A9 - Repayment Schedule for Market loans of State Governments as of end-March 2003

Fiscal Year	Amount of Repayment (Rs. Crore)	GDP in line with Business as usual scenario	% of GDP
2003-04	4145	2744800	0.15
2004-05	5123	3019279	0.17
2005-06	6274	3321207	0.19
2006-07	6551	3653328	0.18
2007-08	11554	4018660	0.29
2008-09	14400	4420526	0.33
2009-10	16511	4862579	0.34
2010-11	15870		
2011-12	22032		
2012-13	30065		

Source : RBI (2003b) and Table 5

Note : Outstanding are likely to increase on account of issue of power bonds by State Governments with retrospective effect from October 1, 2001

Table A10 - Interest Rate Profile of Outstanding State Government Loans as of March 31, 2003

Range of Interest Rate (%)	Outstanding (Rs Cr)	% to Total
<7	19585	14.72
7.00 - 7.99	11030	8.29
8.00 - 8.99	8004	6.02
9.00 - 9.99	5411	4.07
10.00 - 10.99	14563	10.94
11.00 - 11.99	17062	12.82
12.00 - 12.99	31269	23.50
13.00 and >	26142	19.65
Total	133066	

Source : RBI (2003b)

Table A11 –APDRP Funds Utilisation 2002-03 (Investment component) (in Rs crores)

S.No.	State	Project Cost	contribution from APDRP	APDRP Disbursement in 2002-3						Counter part fund tied up by the state	Utilisation of funds
				1st (4/4/2002)	2nd (28/1/2003)	3rd (31/3/03)	Investment	Incentive	Total		
1	Andhra Pradesh	1476.50	738.25	39.07	72.75	52.00	163.82		163.82	738.25	69.48
2	Bihar	717.57	358.79	16.11		50.00	66.11		66.11	76.95	0.48
3	Chattisgarh	424.58	212.29	10.00			10.00		10.00	10.00	23.90
4	Delhi	946.46	473.23			105.51	105.51		105.51	473.23	25.20
5	Goa	176.34	88.17	9.00	6.52	6.52	22.04		22.04	4.45	12.53
6	Gujarat	1035.80	517.90	21.35	54.07	30.00	105.42	236.37	341.79	291.96	27.44
7	Haryana	450.66	225.33	18.23	19.05	19.05	56.33	5.01	61.34	163.38	35.93
8	Jharkhand	444.85	222.43	12.00			12.00		12.00	137.25	9.32
9	Karnataka	1161.19	580.60	29.77	57.69	57.69	145.15		145.15	580.60	69.00
10	Kerala	350.35	175.18	17.07	13.36		30.43		30.43	173.18	17.19
11	Madhya Pradesh	598.98	299.49	27.83	23.52	23.52	74.87		74.87	62.00	11.96
12	Maharashtra	1107.85	553.93	45.00	46.74	46.74	138.48	137.89	276.37	345.42	65.09
13	Orissa	592.22	296.11	14.72		39.63	54.35		54.35		
14	Punjab	667.46	333.73		41.72	12.26	53.98		53.98	333.73	
15	Rajasthan	1255.05	627.53	28.40	62.24	35.00	125.64		125.64	308.02	71.68
16	Tamil Nadu	968.17	484.09	32.12	44.45	35.00	111.57		111.57	484.09	77.14
17	Uttar Pradesh	718.19	359.10	30.12		50.00	80.12		80.12	301.77	
18	West Bengal	132.71	66.36	19.02			19.02		19.02	66.36	
19	Assam	365.98	365.98	10.95	86.02		96.97		96.97		0.05
20	Arunachal Pradesh	67.29	67.29				0.00		0.00		
21	Himachal Pradesh	105.51	105.51	13.33	19.71	10.00	43.04		43.04		4.69
22	Jammu & Kashmir	453.48	453.48			20.00	20.00		20.00		
23	Manipur	10.13	10.13	2.67			2.67		2.67		
24	Meghalaya	26.29	26.29		6.57		6.57		6.57		
25	Mizoram	9.77	9.77	2.67	1.11		3.78		3.78		3.78
26	Nagaland	47.22	47.22	2.67	10.47		13.14		13.14		2.67
27	Sikkim	63.48	63.48	2.67	14.53		17.20		17.20		2.67
28	Tripura	13.27	13.27	2.67			2.67		2.67		
29	Uttaranchal	361.51	361.51	18.50	81.13	75.00	174.63		174.63		56.60
	Total	14748.86	8136.40	425.94	661.65	667.92	1755.51	379.27	2134.78	4550.64	586.80

Source : Ministry of Power (Conference of State Power Ministers, June 12th, 2003)

Table A12 - Progress of PMGSY Scheme (August, 2003)

Sr.No.	State	Value of Proposals [Rs. Crore]	Amount Released [Rs. Crore]	No. of road works	No. of roadworks completed [upto Aug2003]	Percent road works completed[%]
1	Andhra Pradesh	924.7	380	3815	1705	44.7
2	Arunachal Pradesh	120.5	70	359	147	41.0
3	Assam	423.4	150	1845	217	11.8
4	Bihar	451.6	300	967	0	0.00
5	Chhattisgarh	349.6	174	434	89	20.5
6	Goa	22.4	10	127	71	55.9
7	Gujarat	235.7	100	972	445	45.8
8	Himachal Pradesh	188.9	120	372	196	52.7
9	Haryana	130.2	40	64	1	1.6
10	Jharkhand	377.4	220	370	20	5.4
11	Jammu & Kashmir	83.3	40	112	0	0.0
12	Karnataka	435.8	190	1692	541	32.0
13	Kerala	61.4	40	217	53	24.4
14	Meghalaya	103.2	70	307	208	67.8
15	Maharashtra	699.4	260	2226	860	38.6
16	Manipur	141.2	80	572	0	0.0
17	Madhya Pradesh	1370.0	426	1756	244	13.9
18	Mizoram	85.4	40	45	24	53.3
19	Nagaland	84.1	40	175	130	74.3
20	Orissa	716.4	350	1559	663	42.5

Source :

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