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# Is the level of government spending enough to revive growth? : A study of Union Government and Southern States

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The government of India adopted a counter-cyclical fiscal policy which included tax cuts and increases in expenditures during the global financial crisis of 2008 (De, 2012; 14th FC Report). The government undertook such policy to revive the economy from a downturn. The impact of global financial crisis was almost negligible on the economic growth in India but it deteriorated the fiscal parameters of the Union government as a result of expansionary policies. The fiscal deficit of the Union government which met the fiscal targets of Fiscal Responsibility and Budget Management (FRBM) during 2007-08 (2.5 %), exceeded the 3 per cent limit of GDP and reached 6 per cent in 2008-09 which further increased to 6.5 per cent in 2009-10. The fiscal path of the Union government shows that the FRBM target was achieved only in 2007-08 and it remained above the target level since then. On the other hand, the state finances were not much affected by the crisis and the states continued to follow the fiscal discipline path set by fiscal responsibility legislation (FRL).

A recent study by RBI (2020) shows that the general tendency of the fiscal policy of the state governments is dependent on the actual output and the debt level of the states. The fiscal rules compel the state fiscal policies to be pro-cyclical. A pro-cyclical fiscal policy means an expansionary policy during upturn and a contractionary policy during downturn. When the States' revenue falls due to a fall in output, they need to cut back their expenditure to follow the FRL, which indicates a pro-cyclical policy. In short, pro-cyclical fiscal policy reflects the co-movement of government's revenues and expenditures in the same direction as the output and vice-a versa for a counter-cyclical policy. However, the economic recovery policies are generally based on counter-cyclical policies, which demands for an expansionary fiscal policy.

The unprecedented COVID-19 pandemic has affected the pre-existing declining growth path of the country, further leading to a negative growth. The Gross Domestic Product (GDP) growth has been declining since 2017-18. It declined from 8.3 per cent in 2016-17 to 7 per cent in 2017-18 to 6.1 per cent in 2018-19 to 4.2 per cent during 2019-20 Provisional Estimate (PE) and to -7.8 per cent in 2020-21 Advance Estimate (AE) (MOSPI). The first advance estimates of Gross Value Added (GVA) at basic prices during 2020-21 by economic activity shows a positive growth only in agriculture, forestry, fishing (3.4 %) and electricity, gas and other utility services (2.7%) with negative growth being observed in rest of the economic activities[1] vis-à-vis 2019-20(PE).

COVID-19 has been affecting the financial resources of both Union and State government. Following the affected revenue and the demand of the state government, the borrowing limit of the state government was increased from 3 per cent to 5 per cent of GSDP for 2020-21 (MoF, 2020) . Although the borrowing limit has been extended beyond 3 per cent of GSDP, it is conditional upon various factors like, state governments need to implement one nation one ration card system, ease of doing business reform, urban local body/utility reforms and power sector reforms. The weightage for carrying out these reforms are 0.25 per cent of GSDP for each component, totalling to 1 per cent of GSDP. "The remaining borrowing limit of 1 percent will be released in two installments of 0.50 percent each - first immediately to all the States as untied, and the second on undertaking at least 3 out of the above named reforms"(MoF, 2020).

Given the revenue loss faced by the states due to COVID-19 pandemic and the conditional borrowing of the states, this article review the fiscal stance of southern states and union government during Apr- Oct 2020 and compares it with the previous period.

**Revenue receipts**

The pre-dominant feature of Union and state finances during the pandemic has been a continuous negative growth in both tax and non-tax revenue. The figures up to October 2020 shows the persistent negative growth in tax revenue for all the southern states as well as for Union government with Kerala (26.7%), Karnataka(22.3 %) and Tamil Nadu (19.6 %) having a higher negative growth compared to that of Union government (15.8 %). The share in central taxes has been showing an alarming negative growth for all the states with highest decline in Karnataka (40.9 %), Telangana (33.1 %), Kerala (31.3 %), Tamil Nadu (15.7 %)

and Andhra Pradesh (13.2 %). Even the positive growth in grants-in-aids in the states is not allowing the states to have a positive growth in the revenue receipts [2] except for Andhra Pradesh (Table 1).

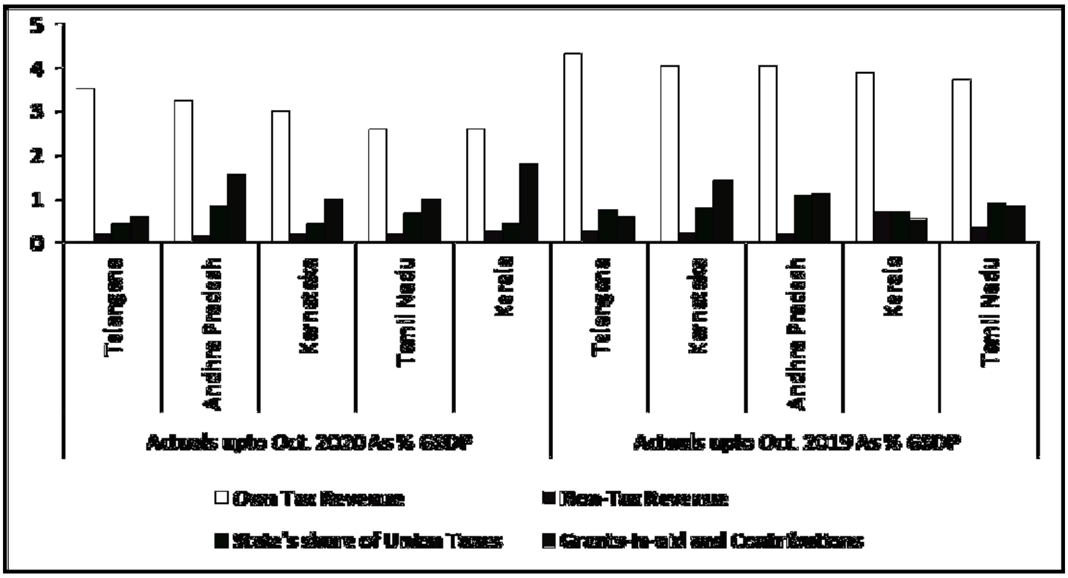
**Table 1.** Growth in revenue receipts (%)

| Description | Revenue Receipts | Tax Revenue | Own Tax Revenue | Non-Tax Revenue | State's share of Union Taxes | Grants-in-aid and Contributions |
|---|---|---|---|---|---|---|
| Telangana | -9.8 | -12 | -8.4 | -27 | -33.1 | 16.9 |
| Andhra Pradesh | 1.8 | -9.9 | -9 | 1.7 | -13.2 | 55 |
| Karnataka | -22.5 | -22.3 | -18.6 | -12.2 | -40.9 | -25.2 |
| Tamil Nadu | -12.1 | -19.6 | -20.6 | -31.1 | -15.7 | 38 |
| Kerala | -4.1 | -26.7 | -25.8 | -60.5 | -31.3 | 254 |
| Union Government | -23.8 | -15.8 | | -48.2 | | |

Source: Computed from monthly indicators, C&AG and Monthly Accounts, CGA

Kerala registered the highest negative growth in own tax revenue of 25.8 per cent, followed by Tamil Nadu (20.6%), Karnataka (18.6%), Andhra Pradesh (9 %) and Telangana (8.4%). The components of revenue receipts show almost a similar picture when analysed as per cent of GSDP (Fig.1). The loss in own tax revenue as per cent of GSDP has been highest in Kerala (-1.31 %) followed by Tamil Nadu (1.11 %), Karnataka (1.05 %), Telangana (0.81%) and Andhra Pradesh (0.78%) during 2020 vis-à-vis 2019 (Fig.1).

**Fig 1.** Comparison of the revenue receipts components % GSDP between 2019 and 2020




Source: Computed from monthly indicators, C&AG

### Government expenditure

The growth in total expenditure of the union government of 0.4 per cent shows a growth less than the southern states like, Andhra Pradesh (54.4%), Telangana (7.4%) and Kerala (6.8%). This gets reflected in the growth rate of revenue expenditure of the Union government which amounts to 0.7 per cent, is less than that in Andhra Pradesh (45.6 %), Telangana (10.1%) and Kerala (6.1%). Rest of the southern states, Karnataka and Tamil Nadu, experienced a negative growth in both total as well as in revenue expenditure of the state government (Table 2).

**Table 2.** Growth in expenditure (%)

| Description | Andhra Pradesh | Karnataka | Kerala | Tamil Nadu | Telangana | Union Government |
|---|---|---|---|---|---|---|
| Revenue Expenditure of which | 45.6 | -6.7 | 6.1 | -6.4 | 10.1 | 0.7 |
| i) Expenditure on Interest payment | 36.3 | 19.8 | 9.4 | -5.2 | 38.5 | 15.2 |
| ii) Expenditure on Subsidy | 14 | NA | 217.5 | NA | 49 | -18.2 |
| Capital Expenditure | 214.1 | 4.5 | 15 | -2.4 | -9.4 | -1.9 |
| Total Expenditure | 54.4 | -5.1 | 6.8 | -6.1 | 7.4 | 0.4 |

Source: Computed from monthly indicators, C&AG and Monthly Accounts, CGA
Note: NA represents not available

The data up to October 2020 vis-à-vis 2019 shows that the growth in subsidy expenditure of Kerala has been remarkable (217.5%) and unparalled to other southern states including the Central government's spending on subsidies which is observed to be negative (-18.2%) when it should have been the highest. The highest spending on subsidies in Kerala shows its timely response on addressing the distressing effects of the pandemic by providing required social security benefits for protecting the livelihood of the people. The growth in interest payment expenditure shows a lowest growth in Tamil Nadu (-5.2%) and Kerala (9.4%) compared to the highest growth in Telangana (38.5%) and Andhra Pradesh (36.3%).

The fall in government final consumption expenditure in India can also be observed from table A1 given in the appendix. It decreased from 11.8 per cent in 2019-20 to 5.8 per cent in 2020-21. This is a matter of serious concern and needs special attention. The exports, imports which were previously following a negative growth during 2019-20 have deteriorated further during 2020-21 (Table A1).

## Appendix

**TableA1.** First advance estimates of GDP, 2020-21 and growth rates (at 2011- 12 Prices)

| Item | | | (Rs. Crore) | | (%) | |
|---|---|---|---|---|---|---|
| | | | | | Percentage Change Over Previous Year | |
| SL. No | Domestic Product | 2018-19 (A/C)Actuals | 2019-20 PE | 2020-21 AE | 2019-20 | 2020-21 |
| 1 | GVA at Basic Prices | 12803128 | 13301120 | 12339175 | 3.9 | -7.2 |
| 2 | Net Taxes on Products | 1178298 | 1264831 | 1100487 | 7.3 | -13 |
| 3 | GDP (1+2) | 13981426 | 14565951 | 13439662 | 4.2 | -7.7 |
| 4 | NDP | 12372051 | 12893977 | 11888607 | 4.2 | -7.8 |
| | **Final Expenditures** | | | | | |
| 5 | Private Final Consumption Expenditure (PFCE) | 7908057 | 8325907 | 7537315 | 5.3 | -9.5 |
| 6 | Government Final Consumption Expenditure (GFCE) | 1478565 | 1652367 | 1747876 | 11.8 | 5.8 |
| 7 | Gross Fixed Capital Formation(GFCF) | 4460967 | 4334091 | 3707516 | -2.8 | -14.5 |
| 8 | Change in Stocks (CIS) | 264415 | 269489 | 258023 | 1.9 | -4.3 |
| 9 | Valuables | 169734 | 192629 | 99082 | 13.5 | -48.6 |
| 10 | Discrepancies | 119923 | 89196 | -18195 | -25.6 | 120.4 |
| 11 | Exports | 2922543 | 2817660 | 2584918 | -3.6 | -8.3 |
| 12 | Imports | 3342777 | 3115388 | 2476873 | -6.8 | -20.5 |
| 13 | GDP | 13981426 | 14565951 | 13439662 | 4.2 | -7.7 |
| | **Rates to GDP** | | | | | |
| 14 | Private Final Consumption Expenditure (PFCE) | 56.6 | 57.2 | 56.1 | | |
| 15 | Government Final Consumption Expenditure (GFCE) | 10.6 | 11.3 | 13 | | |
| 16 | Gross Fixed Capital Formation(GFCF) | 31.9 | 29.8 | 27.6 | | |
| 17 | Change in Stocks (CIS) | 1.9 | 1.9 | 1.9 | | |
| 18 | Valuables | 1.2 | 1.3 | 0.7 | | |
| 19 | Discrepancies | 20.9 | 19.3 | 19.2 | | |
| 20 | Exports | 23.9 | 21.4 | 18.4 | | |
| 21 | Imports | 0.9 | 0.6 | -0.1 | | |
| 22 | GDP | 100 | 100 | 100 | | |
| | **Per capita income** | | | | | |
| 23 | Per Capita GDP (Rs ) | 105361 | 108620 | 99155 | 3.1 | -8.7 |

Source: MOSPI, 2021

## The deficit and borrowing positions

Fiscal deficit shows an alarming increase in Karnataka (24291.08%) followed by Andhra Pradesh (140.2 %) during April-Oct 2020 over 2019. The growth rate of fiscal deficit is 57.8 per cent in Telangana , 34 .4 per cent in Kerala and it is 18.8 per cent in Tamil Nadu during 2020 over 2019. It is observed that the rate of growth of fiscal deficit is relatively low in Tamil Nadu and Kerala. (Table 3)

**Table 3.** Growth rate of deficits in southern states in 2020 from 2019 (Apr-Oct) (%)

| Description | Andhra Pradesh | Karnataka | Kerala | Tamil Nadu | Telangana |
|---|---|---|---|---|---|
| Revenue Deficit | 194.6 | -111.1 | 35.4 | 20.7 | 230.3 |
| Fiscal Deficit | 140.2 | 24291.1 | 34.4 | 18.8 | 57.2 |
| Primary Deficit | 187.1 | -174.6 | 52.7 | 43.6 | 69.5 |

Source: Computed from C&AG

Revenue deficit shows a positive growth during April to October 2020 in all the southern states. Kerala (34.5%) and Tamil Nadu (20.7%) registered a lowest growth in revenue deficit. In Andhra Pradesh and Telangana, the revenue deficit growth are 194.6 per cent and 230.1 per cent, respectively (Table 3). During 2019, Karnataka registered a revenue surplus of Rs 15336.9 crores, which transformed to a revenue deficit of Rs 1704.1 crores in 2020 (April to October).

Prior the pandemic, the fiscal deficit of all the southern states were meeting the FRL target of 3% of GSDP (Table 4 and Figure2). Kerala and Andhra Pradesh were having the fiscal deficit as per cent of GSDP closely nearing the targets of 2.8 and 2.9 per cent respectively. Other southern states were having deficits much below the target. States, like Karnataka, Tamil Nadu and Telangana did not even exhaust the available fiscal space.

**Table 4.** Deficit and borrowing as percentage of GSDP

| As %GSDP | Actuals upto Oct. 2020 | | | | | Actuals upto Oct. 2019 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Description | Andhra Pradesh | Karnataka | Kerala | Tamil Nadu | Telangana | Andhra Pradesh | Karnataka | Kerala | Tamil Nadu | Telangana |
| Borrowings & Other Liabilities | 6.3 | 1 | 3.4 | 1.9 | 2.8 | 2.9 | 0 | 2.8 | 1.8 | 2 |
| Revenue Deficit | -5 | -0.1 | -2.5 | -1.3 | -1.6 | -1.9 | 1 | -2.1 | -1.2 | -0.5 |
| Fiscal Deficit | -6.3 | -1 | -3.4 | -1.9 | -2.8 | -2.9 | 0 | -2.8 | -1.8 | -2 |
| Primary Deficit | -5.1 | -0.4 | -2.2 | -1.1 | -1.9 | -2 | 0.6 | -1.6 | -0.9 | -1.3 |

Source: Computed from C&AG and RBI, State Finances: A Study of Budget, 2020

**Figure 2.** Comparison of fiscal deficits and fiscal targets


Source: Computed from monthly indicators, C&AG

The recent scenario from April-October 2020 shows a similar picture as April-October 2019. Even if the borrowing limits are increased to 5 per cent of GSDP, it does not get reflected in the current borrowing positions of the southern states except for Andhra Pradesh (6.3%). This probably is the effect of conditionality being put in the borrowing limits of the state governments. Also it may be noted that Tamil Nadu and Karnataka is reflecting upon a pro-cyclical policy, fall in state government expenditure is accompanied with a fall in own tax revenue of the states. Nonetheless, the central government finances reflect not a different fiscal policy. A fall in central government final consumption expenditure from 11.8 per cent in 2019-20 to 5.8 per cent in 2020-21 along with a fall in tax revenue calls for an immediate counter-cyclical policy to revive the economy.

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