CHAPTER – II

REVIEW OF LITERATURE

In this section, an attempt has been made to present a brief review of the important earlier studies on revenues, expenditures and the deficits of the union budgets in India. In this chapter an attempt has been made to review some important works related to the present study. The available literatures reveal the fact that studies undertaken in this area are limited in number. Some important research works undertaken in recent years which are very closely with the present study are reviewed in this chapter. The budgetary positions of some foreign countries have also been given in this chapter.

The collected literatures have been given into three categories such as literature on revenue side of the budgets of the Union Government, literature on expenditure side of the budgets of the Union Government and literature on fiscal imbalance of the Union Government. They have been given in chronological order.

A.LITERATURE ON REVENUE SIDE OF THE UNION BUDGETS

Jha (1990) in his analysis on “Taxation and the Indian Economy” had stated that taxation is a compulsory form of savings because which is used to finance socially desirable and productive projects of development in the public
sector. It contributes substantially to the expenditure of the government. Substantial tax revenue is more useful to Indian government to manage its plan and non-plan expenditure.¹

**Stotsley and Wolde Meriam (1997)** in his article entitled “Tax Efforts in Sub-Saharan Africa” had studied important determinants of tax-GDP ratio of Sub-Saharan Africa and they concluded that factors such as political system, attitudes towards the government, the quality of tax, customs, other institutions of the government and commodity price shocks were important determinants of tax-GDP ratio.²

**Parthasarathi Shome (1997)** in his article entitled “The 1990s Revolution in Tax Policy” had stated that one broadly compares the current rate structures of the main central taxes in India with those prevailing at the beginning of the decade, it would be hard to deny that the 1990s had witnessed far-reaching changes in the Indian tax system. Indeed recent budgets had speeded up the process of tax reform to a revolutionary pace. This paper also attempted to assess the impact of the major changes on the efficiency, equity and revenue productivity of the tax system.³

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Jonathan Haughton (1998) in his study entitled “Estimating tax buoyancy, elasticity and stability” had analysed that the revenue from different taxes varies from year to year. Taxes whose revenue was relatively stable or whose revenue was negatively correlated with the revenue from other taxes were likely to be particularly helpful in giving stability to the overall stream of revenue. Revenue stability is desirable, at least from the government perspective, in that it makes it easier to put together plausible spending and borrowing for plans for the year ahead.4

Andreoni, Erard and Feinstein (1998) in their article on “Tax Compliance” they had studied tax evasion. They used the term shadow variable for denoting tax evasion in their econometric equations. If the shadow variable is negative, it implies large hidden economy and vice-versa. It is negative for countries with a larger hidden economy to be characterized by lower tax revenue. It reduces both tax revenue and GDP.5

M.Govinda Rao (2000) in his article on “Tax Reform in India: Achievements and Challenges” had analysed the evolution of the tax system in India since the early 1990s. There had been major changes in the tax system in

several countries over the last two decades for a variety of reasons. This analysis described and assessed the introduction of new forms of direct and indirect taxes, their revenue and equity implications and the success achieved in their implementations. It was concluded that after eight years of reform, improving the tax system remains a major challenge in India.6

Sharma and Chaiti Sharma Biswas (2001) in their article “Restructuring the Present Tax structure: Some Theoretical and Practical Aspects” had addressed to two government perspective, in that it makes it easier to put together plausible spending and basic objectives to reduce the dependence on foreign trade taxes and orient the tax structure towards an open and competitive economy by removing its inefficiencies and to improve the buoyancy of the tax revenues on a sustainable basis so that the budgets of the government could be balanced and eventually yield some surplus to finance public investments. The reforms of 1991-93 brought about extensive changes in the central government’s major taxes-customs, union excises and income tax. These have yielded some positive results. But, the system still requires being more vibrant, amenable and need-based particularly to the deficit states.7


Balachandran (2002) had opined that the indirect tax system in India comprised a system of customs and excise duties at the centre and sales tax at the state level. The constitution gives the Union Government the power to levy custom duties and excise duty on all commodities except alcoholic liquor and advertisements therein. However, it has long been felt the present indirect tax system was not conducive to good tax administration mainly on account of multiplicity of indirect tax laws, ambiguity of interpretation of the various provisions of indirect tax laws and classification disputes which were a natural outcome of a multiple tax rate system.\(^8\)

Venkitaramana (2004) had analysed the recommendations of Kelkar task force on indirect taxes concluded that tax reform is a different challenge at the best of times. Many states have to argue to the grand bargain proposed by Kelkar is all the more of a problem, in that the proposal may appeal to dilute state powers.\(^9\)

Fox, Wiliam and Lethun Luna (2006) in their article “State Corporate tax revenue trends: Causes and Possible solutions” had noted that the value of tax revenue in any given year is the product of the tax rate and the tax base. The

changes in the tax base, the growth of non-corporate entities, changes occurred at the state level and the growth in tax planning activities were the more important factors affecting corporate income tax revenue.\footnote{10}

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\textbf{Farooq Rasheed, (2006)} in his article entitled” An analysis of the Tax buoyancy rates in Pakistan” had estimated tax buoyancy by using econometric technique for estimating tax elasticity and found that the significant but low tax buoyancy rates for GDP, high powered money and volume of trade. There was no significant association between tax revenue growth and investment, credit, public debt and inflation. This illustrated weakness of the tax regime in Pakistan.\footnote{11}
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\textbf{Nayak (2007)} in his article entitled “A Macro Economic View of the Union Budget 2007” had stated that the Central Government tax to GDP ratio had risen from 9.2 per cent in 2003-04 to 11.4 per cent in 2006-07. There was a fairly moderate and modern direct tax schedule, informed by the huge body of theoretical and empirical work on direct taxation in the past three decades. The idea of not tampering with the direct tax schedule too frequently was
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essentially sound. Growth of income and an environment conducive to voluntarily going to yield higher revenue. It is a matter of some satisfaction that the tax to GDP ratio for the centre had moved up from 9.2 per cent in 2003-04 to 11.4 per cent in 2006-07. This would bring the tax to GDP ratio in the country at large to around 16.5 per cent, which was the percentage at the beginning of the reform process in 1991. On the eve of the initiation of economic reform in 1990-91 direct taxes were a mere 19 per cent of GDP. By 2006-07 direct tax collection stood at 51 per cent of GDP. As regard indirect taxes, there had been wide ranging reductions in tariffs.\textsuperscript{12}

Chidambaram (2007) the former finance minister in his speech had stated that the buoyancy in tax revenues is directly contributable to high growth. In the three years since 2003-04, gross tax revenue of the Central Government had increased by 19.9 per cent, 20.1 per cent and 29.3 per cent respectively. The tax revenues were growing at a brisk rate so far. High growth accelerated the movement towards fiscal stability. The higher growth rate improved tax buoyancy and there was positive relationship between tax buoyancy and tax revenue.\textsuperscript{13}

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Abhijit Sen Gupta (2007) in his study entitled “Determinants of Tax Revenue Efforts in Developing countries” had studied the determinants of tax buoyancy in the developing countries and he found that in developing countries the factors such as agriculture sector, industrial sector, foreign trade, budget deficit, service sector and per capita income are the major determinants of tax buoyancy. Agricultural sector and grants in aid were negatively correlated with the tax buoyancy and budget deficit, manufacturing and service sectors played a crucial role in determining the tax buoyancy.14

Venkatesh (2008) had stated that the spectacular rise in the collection of income tax both at the corporate and non-corporate levels, as well as service tax was a pointer to the significant buoyancy witnessed within the national economy. However, it did not hide some services issues confronting the government and its revenues. The buoyancy in revenues was not witnessed in the case of indirect taxes. This is because of variety of reasons. He suggested that as an incentive to regular and honest tax payers, the government must ensure that the income tax act is suitably amended.15


Seth and Ankur Bhatnagar (2008) had attempted in their article on “Influence of demographic variables on Indirect Tax setting for selected Indian states” to provide conclusive evidence in favour of sensitivity of optimal commodity taxes to demographic variables. This involved estimating optimal commodity taxes for the chosen 16 Indian states, incorporating demographic profiles for each state using National Sample Survey (NSS) data. Such calculations are further done under alternative welfare weights for each household. The results revealed that the introduction of demographic variables in the demand system makes the tax rates more non-uniform across commodities and across states and significantly alters their response to changes in the social planner’s perception of a household’s welfare. These effects were more pronounced for certain commodities that are basic and essential in a household’s basket. Differences in welfare weights also had a similar effect on tax rates, though to a lesser degree.  

Pandi (2008) had revealed that recent government data on tax collections paint a flattering picture of the economy. If the trend continues, as expected, collections from income tax and corporate taxes would definitely breach the target. If the finance minister wants that this trend would continue in the years to come, a comprehensive review and reduction of tax rates are the need of the hour. All the proposals of the previous budget lacked measures to control inflation and did not provide any major thrust to the economy.

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As result, the working class had been forced to intensify the struggle in order to
tight the pro-rich, anti-pro policies of the government.\textsuperscript{17}

\textbf{In the Hindu (2009)} an article had showed that for the first time in recent
history, the actual collection in direct and indirect taxes exceeded both the
budget estimates and the revised estimates for the fiscal 2006-07. The data also
validated the shift away from indirect taxes to direct taxes in the post-reform
period, with the share of direct taxes in gross tax revenues of the centre touching
48.8 per cent in 206-07. In 1990-91, less than a fifth of center’s gross tax
revenues came from direct taxes.\textsuperscript{18}

\textbf{Yuthika,Indraratna (2009)} in her study entitled “The measurement of
tax elasticity in Sri Lanka: A time series approach” had analysed factors that
affect the tax to base elasticity such as tax rates, exemptions and improvements
in the tax administration were within the control of the fiscal authorities, thereby
making this measure important for related purposes. The base to income
elasticity was determined largely by the way in which the economic structure
responds to growth.\textsuperscript{19}

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\textbf{References}
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\textsuperscript{17} Dr.Pandi, R., “Taxation needs a Pragmatic Approach”, Southern Economist, Volume 46,
No.20, February 15, 2008, PP 41-42.

\textsuperscript{18} The Hindu Business Line, dated 29th April, 2009,P3

\textsuperscript{19} Yuthika,Indraratna, “The measurement of tax elasticity in Sri Lanka: A time series
approach, World Bank staff studies,P3.
Qazi Mosood Ahmed (2010) in his article entitled “The determinant of tax buoyancy: evidence from the developing countries”, had concluded that the insignificant impact of service sector in determination of tax buoyancy was because of underdeveloped financial sector. After 1990s, financial reforms and better tax administration caused improved tax collection through service sector in developing economy.20

B.LITERATURE ON EXPENDITURE SIDE OF THE UNION BUDGETS

Nagarajan and Spears”(1990) in their study on” An Econometric test of Wagner’s law for Mexico: A Reexaminations” stated that a country had to perform many activities such as social services, economic services and community services. It is common that a country increases its public expenditure when its national income increases. They had econometrically tested the Wagner’s law for Mexico and they concluded that the Wagner’s law supported for the country.21

Afxentiou and Serletis (1991) in their study entitled “A time series analysis of the Relationship between Government expenditure and GDP in


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Canada” had analysed the relationship between the government expenditure and GDP in Canada and they had arrived at conclusion that there had been continuous association between Canada’s government expenditure and its GDP and Canada’s expenditure increased in association with the increase in its gross national product over the periods.22

Courakis (1993) in his article on “Public expenditure growth in Greece and Portugal: Wagner’s law and Beyond” had tested the Wagner’s law of increasing state activities for the countries Greece and Portugal and he found that the Wagner’s law of public expenditure supported for both Greece and Portugal. He had also found that both the government raised their expenditure when they earn public revenue.23

Alexander Morozov and Mark Sundberg (2000) had studied that the overall reduction of recorded public expenditure in relation to GDP had been accompanied by fairly substantial shifts in the structure of spending. Extra budgetary funds, which accounted in 1992 for almost half of total spending, accounted for about one third – largely as a result of an elimination of off-budget import subsidies and incorporation in the budget of remaining hard currency operations; federal spending, which in 1992 accounted for over 65 percent of consolidated federal-regional government spending, today accounts


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for less than one-third of the total; expenditures for National Economy (which primarily reflect subsidy outlays), declined from 11.4 percent of GDP in 1992 to roughly 6 percent, with the federal share declining from more than 50 percent to less than 15 percent; reported defense expenditures declined from about 5 percent of GDP to 2-3 percent range.  

**Mahendra Dev and Jos Mooji (2002)** had pointed out that since 1990-91 the government had been attempting to check the growth of public expenditure. The ratio of public expenditure to GDP declined to 27.1 per cent in 1996-97. Since than the trend of declining public expenditure – GDP ratio had been reversed and as a result in 2002-03 public expenditure – GDP ratio was once again as high as 31.3 per cent. Now the ratio of public expenditure to GDP in India is one of the highest in developing countries and very much comparable to the ratio in the USA, Canada, the U.K, France and Germany. However the share of social services in total public expenditure is significantly lower in India than in all developing countries taken together.  

**Jha and Sharma (2004)** in their study on “Structural Breaks, Unit Roots and Co-Integration: A further test of the sustainability of the Indian Fiscal deficit” had studied co integration of government expenditure and revenues in India on the basis of time series data. They found that there was existence of co

integration of government expenditure and revenues during their study period. For which they studied this integration at different structural breaks. There had been adjustment between the government revenues and expenditure over the period of time.\textsuperscript{26}

**Bimal Jalan (2004)**, the ex-governor of Reserve Bank of India in his article “Economics, Politics and Governance” had viewed that high fiscal deficit over time had not resulted in increasing the government’s ability to spend where higher expenditure was required. Most of the government expenditure was committed to servicing past debt or meeting salary and other past commitments. There was high fiscal deficit without fiscal empowerment.\textsuperscript{27}

**Misra and Puri (2005)** had noted that increasing expenditure on subsidies is the main factor to be considered in development of expenditure of the central government in India. Based on the study of the National Institute of Public Finance and Policy (NIPFP) the government placed a report on central government subsidies in 2004. According to the report, subsidies amounted to Rs.104113 crore in 2002-03 and Rs.115825 crore in 2003-04.

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central government subsidies thus constituted 4.25 percent of GDP in 2002-03 and 4.18 percent of GDP in 2003-04. Subsidies and social services constituted 12.8 percent and 14.1 percent of social subsidies in 2002-03 and 2003-04 respectively with the rest accounted for by economic services.\(^{28}\)

**Misra and Puri (2005)** had also noted that the capital expenditure-GDP ratio was 5.6 percent in 1990-91. It declined steadily throughout the decade and stood at 2.7 percent in 2002-03. It is thus clear that the burden of fiscal imbalance correction during the 1990s has been primarily on capital expenditure and social sector expenditures. The approach of the central government is questionable. Reducing expenditure on transport and infrastructure development both in urban and rural areas disrupted the growth process. Reduced capital expenditure in real terms over the years has become such a constraint that it unreservedly dampens investment activity in the private sector. This has caused a set back to overall growth process particularly at a time when the state has dramatically withdrawn from productive activities.\(^{29}\)

**Anand Gupta (2005)** in his article entitled “Reforming management of the Government of India’s expenditures: Some thoughts” had stated that setting up of district-wise targets for spending, Public expenditure and surveys have to be organized to check the expenditure. On the basis of this survey,

\(^{28}\) Misra, S.K., Puri, V.K., “Public Expenditure in India”, Indian Economy, Himalaya Publishing House, New Delhi, 2005, PP. 784-790

\(^{29}\) Ibid, PP. 785-793
he suggested to develop a strategic action plan. He had also suggested that the plan and non-plan expenditure distinction does not sound rational, distorts allocation of resources and therefore must be abolished.\(^{30}\)

**Sajikumar (2006)** had pointed out that higher economic growth was invariably accompanied by an increase in the government expenditure. This is well supported by the trend observed in India from 1950-51 to 2000. The ratio of public expenditure to the GNP rose considerably in response to the rise in per capita GNP. Once an economy is in early stages of development, the public expenditure rises at an increasing in response to a rise in per capital income. Only after reaching a fairly developed stage a stable ratio between the public expenditure and the national income will be obtained.\(^{31}\)

**Kausik Chaudhuri and Sugato Dasgupta (2006)** had investigated whether state governments’ fiscal policy choices were tempered by political consideration by using data from the 12 major states of India. Their principal findings were twofold. First, they showed that certain fiscal policies experience electoral cycles: state governments raised less commodity tax revenue, spent less


on the current account and incur larger capital account developmental expenditures in election years than in all other years. Second they showed that the coalition state governments raised less own non-tax revenues and spent less on the current account that state governments were more cohesive in composition. In sum, the dispersion of political power affects government size.\textsuperscript{32}

\textbf{Chidambaram (2006)} had addressed that India was marching ahead on the path of glory and success. In 2004-2005 the growth rate was 7.5 per cent while manufacturing sector grew at a speed of 8.1 per cent. National calamities in 2005-06 took a heavy toll on human lives besides causing extensive damage to crops, roads, houses and the infrastructure. Finance minister provided funds in the budget and planning commission would draw a programme for rebuilding infrastructure. The budget gave a good emphasis for infrastructure and rural growth. An ambitious plan of Bharat Nirman would provide results next four years. Flagship programs of UPA government liker Sarva Siksha Abiyan, Mid-Day Meal scheme had been given good amount of budgetary allocation. In this budget the finance minister had not imposed taxes on individuals or corporate at the same time not many deductions and benefits had been provided.\textsuperscript{33}

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Anderson and Minarik (2006) had opined that debt sustainability can be achieved by completing the medium term debt target with a consistent nominal expenditure growth rule. Given the target debt path and a projected revenue path based on conservative trend GDP growth, a nominal expenditure path and implied nominal expenditure growth ceiling consistent which can be computed. Expenditure rules had better cyclical properties since they let automatic stabilizers operate in down turn and induce savings of windfall gains during an upturn without requiring any specific cyclical adjustment method to do so.\(^{34}\)

Stella Karagianni, Maria Pempetzoglou and Soultana Strikou (2008) in their article entitled “Testing Wagner’s law for the European Union Economics” had examined the validity of Wagner’s law, the proposition that there was a long-run tendency for the public sector to grow relative to national income in the European economies. They concluded that Wagner’s law existed in the vast majority of the European union countries.\(^{35}\)

Nalraj (2008) had stated that there was relatively higher positive correlation between fiscal deficit and revenue expenditure than fiscal deficit and total expenditure. He pointed out that there was drastic change in fiscal deficit

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mainly because of revenue expenditure. Revenue expenditure is one of the two major parts of total expenditure and also has a lion’s share in India’s union budget. Two-third of total expenditure is spent on revenue expenditure and only one-third is spent on capital expenditure. The revenue expenditure to GDP was 14.4 per cent in 1990-91 and continues to reduce and come down to 12.9 per cent in the fiscal, year 1996-97. After 1996-97, revenue expenditure started rising till 2004-05 and touches a higher percentage of 158.4 to GDP.\textsuperscript{36}

**Amos Peter (2010)** in his study on “An Application of Wagner’s law of expanding state activity to totally diverse countries” had examined the validity of Wagner’s law for four countries. They are the United States, Thailand, Barbados and Haiti. For the United States, both real per capita income and government share in economic activity increased over the years. For Thailand and Barbados, the same appears to be true. Haiti was the exception because income rose and then started to decline rapidly. He found empirical support for Wagner’s hypothesis in four diverse countries.\textsuperscript{37}

\begin{itemize}
\item[37.] Amos Peter, “An Application of Wagner’s law of expanding state activity to totally diverse countries”, Monetary Policy Unit, Eastern Caribbean Central Bank, P².
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C. LITERATURE ON FISCAL IMBALANCES OF THE UNION BUDGETS

**Gupta (1993)** in his article entitled “Redefine Budget deficit” had noted that India’s economic health was in a very bad shape in 1991. In response, the government of India, put in place a programme of economic reforms for promoting growth. But later on, India’s economic health was substantially better. But all was not well. Public sector deficit was a substantially better measure of the current state of India’s public finance than the combined fiscal deficit of the central and states in the country.  

**Bohn and Inmem (1996)** had reported that several studies that have looked at the effectiveness of sub national government rules in the context of the U.S. states. The general results were that the rules did enforce some budget discipline on U.S. states, in terms of lower deficits and quicker reaction to negative shocks.  

**Srinivas Gowda (1998)** had analysed that heavy dependence on indirect tax is an unhealthy feelings of fiscal policy in India. Notwithstanding the fiscal reforms affected in India since 1991, the fiscal system is still far from efficient. Tax collection efforts must become more efficient and government expenditure

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must be curbed. Government must stop expenditure in areas where the private sector can work more efficiently. This not only reduce fiscal deficit but would improve the overall efficiency of resource allocation in the economy, besides, releasing resources for productive uses in the private sector.40

Aiyagari Rao and Ellen McGrattan(1998) had stated that the fiscal responsibility and budget management act should aim at to focus medium term fiscal policy on debt sustainability, consider using debt and expenditure growth targets. This approach would tackle the deficit bias at its core and allow room for macro economic stabilization through automatic stabilizers. This could be achieved by setting a medium debt target and debt reduction path to achieve it. A direct rule on gross public debt should be a logical part of the fiscal responsibility and budget management act successor. Setting the exact debt level target requires judgment about sustainable debt levels and India’s debt tolerance. As India continues its gradual integration with global financial markets, the judgement should also be informed by the debt levels observed in other emerging markets following sound fiscal policies.41

Gouda (1998) had noted that budget have been presented by more than twenty finance ministers from R.K Shanmugam Chettiyar to Dr.Yashwant Sinha. These comprised businessmen, bureaucrats, politicians and economists as well

within certain budget framework. Each one of them looked at the economy differently and hence has toyed with different ideas and policies regarding taxation and public expenditure. Further there had also been different epochs in this fifty years budget history in which fiscal rectitude, fiscal robin, subsydism and reformism. As far as public finance is concerned, India was almost back to where it was in 1991.\textsuperscript{42}

The Twelfth Finance Commission (2004) had recommended that the fiscal distress can be alleviated by raising the amount of revenue by tapping new sources of revenues, restructuring of debt and a strict borrowing ceiling \textsuperscript{43}

Prasad Abha, Rajan Goyal and Anupam Prakash (2004) had viewed that in view of the increasing debt sustainability of states, a global cap on all borrowings could be considered. States required permission from the centre to raise loans if they are indebted to the central government or have taken generous from the centre in respect of loans raised by states. This means that the centre has to assess the debt sustainability of the state and its ability to repay the loans, prior to giving states the permission to undertake fresh borrowings. States have financed their fiscal deficits though components such as market borrowings and

\textsuperscript{42} Gouda, M.V., “India’s Budget –The Fifty Years Saga”, Southern Economist, Volume.37, 1 July 1998, P\textsuperscript{13}.
\textsuperscript{43} Report of Twelfth Finance Commission, 2004, Government of India,P \textsuperscript{125-128}
loan from the centre. This has now changed, with bulk of states financing coming from securities to the NSS a controlled component.\textsuperscript{44}

\textbf{Goyal, Rajan (2004)} in his article entitled “Does higher fiscal deficit leads to rise in interest rates?, “An Empirical Investigation” had analysed the relationship between fiscal deficit and interest payment. He used monthly data for his analysis and he found that there was two-way causality relationship prevailed between the fiscal deficit and the amount of interest payment. He also concluded that the growing interest payment was not mainly because of growing fiscal deficit. Because there was larger liquidity available to the fiscal system in India.\textsuperscript{45}

\textbf{Rajmal (2006)} had analysed a phase-wise analytical view of the fiscal situation of the Indian major states over the previous two and half decades and examined the effectiveness of the policy measures to strengthen the states finances. The analysis revealed that the states’ fiscal position showed imbalances, albeit in a varied degree, since the mid-1980s which depended in the second half of the 1990s. The effectiveness of policy measures had remained largely inadequate. Most of the policy measures were exigency-driven rather

\textsuperscript{44}Prasad Abha, rajan Goyal and Anupam Prakash, “ States Debt and Debt Relief”,Economic and Political Weekly,Volume.XXXIX,No.26,June 26,2004,PP 2726-2736
than being structured. As the states face large resource gap, they required effective and time-bound policy measures to enhance revenues particularly non-taxes and shift in expenditure pattern towards economic infrastructure and social sectors to facilitate acceleration in growth.\footnote{Rajmal, “State Finances and Effectiveness of Policy Measures: An Analysis of Indian States”, Reserve Bank of India Occasional Papers, Summer-Monsoon 2006, Volume 27, Issue 1-2, PP. 141-175}

Govinda Rao and Pinaki Chakraborty (2006) had stated that the widening fiscal deficit of sub-national governments has made the task of macro economic stabilization much more difficult and complex. In many countries, including India, multilateral lending institutions provide assistance for sub national fiscal reforms through structural adjustment loans (SAL) with conditionality heavily loaded with fiscal correction measures. This paper examined the fiscal impact of SAL in Indian states by analyzing the quantitative and qualitative aspects of SAL-induced fiscal reforms. There was evidence of softening of the budget constraints in some states, but there was also evidence of greater reduction in fiscal imbalances of SAL states than non-SAL states. It was also seen that much of the fiscal gains had occurred through improved revenue productivity of the tax system and not through expenditure restructuring.

It was also seen that the poorer states have preferred to reduce their developmental expenditures to deal with fiscal stress and to comply with fiscal correction targets. This in turn, had adverse growth implications. They
concluded that the benefits and the acceptability of SAL at the sub-national level in India would critically depend on factors such as the qualitative change in government expenditure in meting deficient delivery of public services at state level and the removal of state level social and infrastructural bottlenecks for promotion of growth by releasing government resources through expenditure restructuring and reform.\textsuperscript{47}

\textbf{Nikhil Saket (2007)} in his article entitled “Public debt and Economic development in India” had found the following findings: Rather complacent attitude to government budget deficit which resulted in unplanned growth in public debt was on the assumptions that borrowed funds would be used only for capital purposes and the resultant investment would yield adequate direct or indirect returns. These assumptions were not often fulfilled in practice. The fiscal crisis and the attunement exponential growth of public debt had risen not merely because of revenue expenditure running ahead of current revenue but also capital expenditure financed by borrowing have not yielded adequate returns.\textsuperscript{48}

\textbf{Khemani, Suti (2007)} had stated that the introduction of fiscal rules by the states needed to be accompanied by complementary reforms to strengthen incentives for sub national fiscal discipline. A large body of literature has


examined both theoretically and empirically the reasons for fiscal profligacy by sub national governments in a federal setting, such as the common mandates, irregional competition and short electoral cycles. The intergovernmental fiscal relations system in India was not immune to such weakness. 49

Joydeep Mukherji (2007) in his article “India: Asia’s Next Productivity Success Story” had told that India’s large fiscal deficits would constraint India from reaching even faster growth. India had created the basic rules of modern economic and political life. While the country’s institutional framework needs strengthening, it would allow India to prosper without drastic change. Gradual economic reform has transformed India, putting it on a much faster growth path. Economic growth in the next ten years may not equal China’s current double-digit growth rate. But India is a nevertheless very likely to become one of the fastest growing economies in the world, growing at a pace similar to that of Malaysia, Thailand, Taiwan and Korea during their period of sustained rapid economic growth. The recent acceleration in real GDP growth reflects both faster input growth as well as rising total factor productivity.

However, India has weaker social pillars to support economic growth than other East Asian countries had at the time of their miracles growth years, mainly due to its poor education system. Huge fiscal deficits is the major constraint to India in this regard.\textsuperscript{50}

\textbf{Bimal Mohanty and Trilochan Tripathy (2007)} had analysed Orissa state’s finance. In their analysis it was found that among the non-special category major states of India, Orissa is one of the high-spending less developed states. Its precarious fiscal situation has been a cause of worry. Its failure to satisfy the expectations of its citizens particularly in respect of social sector development has further aggravated the problem of underdevelopment. The government of Orissa published the white paper on Orissa state finance in 2001 with a view to presenting the facts for its continuing fiscal crisis for public consumption. Among others, unrestrained fiscal deficits, unbridled public debt and unusual spurt in non-developmental expenditure have been held as the major causes of its unsound finance. This state of affairs continues even after the measures of reforms are introduced and thereby confirms the insensitiveness of its fiscal crisis to the measures of reforms.\textsuperscript{51}

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Murali and Vaithianathan (2009) had studied the budgetary performance of four southern states Tamilnadu, Anthra, Kerala and Karnataka. In their analysis they found that the states are slowly moving away from the path of fiscal discipline forsaking earlier efforts to control deficits. The positive trend in the budgets figures of the southern states seen in the last few financial years are being revised due to the slow down of the economy. The mainstay of state finances namely, indirect tax revenues started declining and mounting welfare and relief expenditure in the backdrop of unemployment and poverty is contributing to widening deficits. Fiscal deficit is still less than three per cent of GSDP in all the four states. They have given priority for agriculture and allied sectors along with social welfare.52

Ammannaya (2008) in his study on “Good and Sensible Budget” pointed out that the budget had given adequate attention to fiscal consolidation and fiscal deficit are sought to be restricted to reasonable levels. The micro economic figures reported and projected in the budget in terms of fiscal and revenue deficit.It is heartening to note that the government has been able to achieve a higher tax-GDP ratio.53


Sethuraman (2009) had stated that it is time India brings out the full impact of all its liabilities on the budget document to give a true measure of the revenue and fiscal deficits. With the fiscal deficit at 6.6 per cent of GDP, it is unthinkable for government to reduce the tax revenues, especially during an economic slowdown. The budget may include some further rationalization of taxes and duties to assist the affected sectors, manufacturing and services. Additional revenue mobilization through the budget would be deferred until the economy resumes sustainable growth. Major emphasis in the budget would be expanded social sector programmes, increased similar focus would be on infrastructure which would call for more public expenditure without waiting too long for private participation.54

Ravindra Dholakia (2009) had noted that the FRBM Act targets were comprehensively missed. For the first time in the last 40m years, it is reported a primary revenue account deficit and that too, of one per cent of GDP, which implies that our revenues are insufficient not only to meet our capital outlays and interest obligations but also a part of our current consumption expenditure. Fiscally, this is a grange situation and must be immediately addressed. It is agreed by several economists and policy makers that once in a while such a

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situation would not be unacceptable particularly when the government was required to pump-prime the economy to sustain growth and employment. However a closer examination would reveal that global meltdown and its adverse impact on the Indian economy was hardly one per cent to three per cent points of GDP, whereas the fiscal slippage was almost three times the amount.  

In his article Neelakant Patri (2009) had stated that it was interesting to note that the OECD has joined the IMF in demanding that the new government in India should restore fiscal discipline while a push for further growth needs massive public expenditure that surely would send fiscal deficit to further heights. The OECD has further called on the Indian government to speed up structural reform increase sales of public-sector assets. The IMF in its report on India has made it clear that fiscal consolidation should be a priority for India and that a new law should replace the FRBM Act, which has run out of its 5 years validity. The FRBM Act was passed by Parliament in 2004 had set the target of reducing the fiscal deficit to 3 per cent by 2008-09and the revenue deficit to nil. Those targets have remained elusive because of political compulsion of running of government. The objective social and economic conditions too played a part in the government postponing measures to cut subsidies and sell of government assets to reduce deficit.  

56. Neelakant Patri, “ If wishes were Horses”, Southern Economist, Volume 48, No.5, July 1, 2009, P 3-4