How credible is the path of improving fiscal deficit quality

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The Budget has not only tried to improve fiscal consolidation next fiscal year but has also refined the way it is done.

While the Centre's fiscal deficit is projected to come down to 5.9 per cent of GDP next fiscal year from 6.4 per cent in the current one, its revenue deficit is expected to fall to 2.9 per cent of GDP from 4.2 per cent over this period.

Expenditure on the revenue account does not lead to asset creation. The revenue deficit means the government borrows from the market to finance its current consumption while the burden of servicing that debt will fall on future generations.

But if a higher portion of the fiscal deficit is due to the deficit on the capital account, it would still make sense because capital expenditure leads to asset creation even if future generations service the debt.

However, a larger portion of the fiscal deficit used to be on the revenue account since much of the expenditure there, such as salaries and pensions, is committed. For instance, the revenue deficit was 65 per cent of the fiscal deficit during 2021-22. This proportion is projected to come down to a bit over 63.3 per cent this fiscal year.

This trend would change now since the revenue deficit would account for 48.7 per cent of the fiscal deficit next fiscal year because the government is focusing on its own capital expenditure as well as those of the states.

However, one could doubt the credibility of this path since the numbers relating to 2023-24 are projections and in the past there have been huge deviations from estimates. For instance, the revenue deficit was supposed to come down to 3.8 per cent of GDP this fiscal year from 4.4 per cent in the previous one. However, now it is projected to be 4.1 per cent of GDP, according to Revised Estimates.

Similarly, the revenue deficit was projected to come down to 2.7 per cent of GDP in 2020-21, but it widened to 7.5 per cent in Revised Estimates and came in at 7.3 per cent of GDP as the government became transparent on its various subsidies.

However, experts said the path this time seemed credible.

"The fiscal numbers look credible because the step taken this time is a modest 0.5 per cent reduction in the fiscal deficit ratio. They will have to be more aggressive in the next two years," said Bank of Baroda Chief Economist Madan Sabnavis.

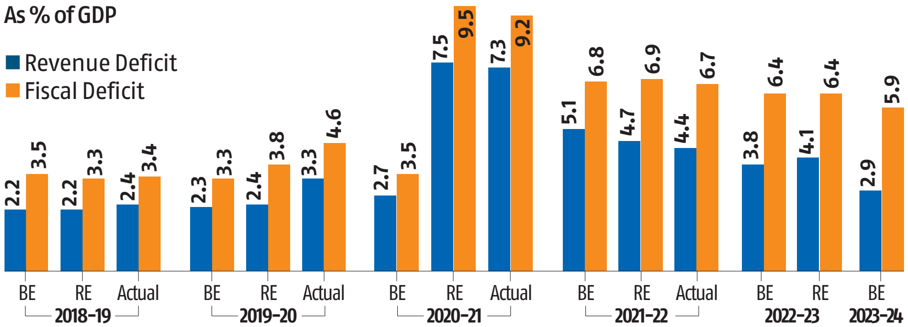
The government used to give fiscal-deficit projections for the next two years in its guide path in the Budget. But now it is not doing so because the Fiscal Responsibility and Budget Management (FRBM) Act is yet to be amended. However, it said it would try to bring down the deficit below 4.5 per cent of GDP by 2025-26.

ICRA Chief Economist Aditi Nayar said a factor determining the quality of expenditure was the states' take-up on capex loans.

Pranab Mukherjee as finance minister came up with the concept of an effective revenue deficit in the Budget for 2011-12.

FISCAL DEFICIT OVER THE YEARS

As % of GDP



BE: Budget Estimates, RE: Revised Estimates

Source: Budget documents