MEDIUM TERM FISCAL POLICY STATEMENT

A. FISCAL INDICATORS – ROLLING TARGETS AS PERCENTAGE OF GDP

(at current market prices)

		Revised Estimates 2014-15	Budget Estimates 2015-16	Targets for 2016-17	Targets for 2017-18
1.	Effective Revenue Deficit	1.8	2.0	1.5	0.0
2.	Revenue Deficit	2.9	2.8	2.4	2.0
3.	Fiscal Deficit	4.1	3.9	3.5	3.0
4.	Gross Tax Revenue	9.9	10.3	10.5	10.7
5.	Total Outstanding Liabilities[2] at the end of the year	46.8	46.1	44.7	42.8

Notes:—

1. *"GDP" is the Gross Domestic Product at current market prices as per new series from 2004-05.*
2. *"Total outstanding liabilities" include external public debt at current exchange rates. For projections, constant exchange rates have been assumed. Liabilities do not include part of NSSF and total MSS liabilities which are not used for Central Government deficit.*

1. The performance on select fiscal indicators for the current financial year and rolling targets over the next financial years are presented above. As explained in this chapter and the next, the changes were necessitated due to emerging Government priorities and compositional shift in the fiscal relations between the Centre and States, following the recommendations of the Fourteenth Finance Commission.

2. Performance in current fiscal year established the robustness of the fiscal correction process. Several macro-economic developments assisted in Government's efforts to remain steadfast in the pursuit of consolidation. While, tax revenues remained sluggish growth revival, fall in international crude oil prices, gains on the current account deficit etc. eased pressure on subsidies and provided scope for expenditure management to meet the fiscal targets.

3. The General Budget 2015-16 is a step further in the direction of fiscal consolidation albeit with revised roadmap. As the first year of the 14th Finance Commission Award period, with higher devolution of taxes to States, Budget 2015-16 is presented with lower tax resources at the disposal of the Centre. Thus, the budget size contracted marginally as compared to BE 2014-15, though it marks an increase of 5.7 per cent over RE. However, Government has maintained its stance on the deficit, adopting 3.9 per cent fiscal deficit target in FY 2015-16 as compared to 4.1 per cent in FY 2014-15. Though, it represents a deviation from 3.6 per cent adopted in the fiscal roadmap; the recalibration was necessitated to maintain fine balance between the need to continue with policy of fiscal rectitude to provide sufficient space for monetary policy easing on one hand and the need to adequately provide for social and welfare programmes and increase public spending in core sectors to give fillip to growth, on the other hand. Thus, the budget 2015-16 opted for keeping the deficit target range bound i.e. under the 4 per cent level, while shifting the target of 3 per cent by one year viz. from 2016-17 to 2017-18. Accordingly, deficit targets of 3.9, 3.5 and 3.0 per cent have been adopted in next three years 2015-16, 2016-17 & 2017-18 respectively. It is noteworthy that the fiscal deficit target has been kept range bound, between to 3 to 4 per cent levels; attaining the 3 per cent over the Medium term framework. The approach of progressively bringing down the deficit has been retained in the Budget 2015-16 despite resource crunch following changes in the revenue sharing. Similarly, revenue targets will be recalibrated and revision to the FRBM Act / Rules is being introduced in the Parliament along with the budget.

4. 14th Finance Commission (FFC) Award has been one of the themes of the budget 2015-16. As discussed in the fiscal policy statement, Government had set in motion the institutional changes necessary for implementing co-operative federalism by way of replacing Planning Commission with National Institute for Transforming India (NITI), re-designing many of the centrally sponsored schemes etc. By providing a quantum jump in the States' share of taxes, FFC has enlarged the scope of development programme by sharing the onus between Centre and States. It is contextual that the Finance Commission has mandated in letter what government had already initiated in spirit in the FY 2014-15.

5. In the emerging scenario, Centre will continue to provide enabling platform, it is for the States to take lead in various developmental programmes based on local needs and aspirations. Thus, budget 2015-16 provides modest increase in Non-Plan spending, basic minimum jump in the Central sector programmes. None-the-less, Government has protected the welfare programmes under social sectors, including outlays for minorities, disability, social justice, health, education etc. In other sectors the share of centre has been reduced with greater contribution coming from States in view of higher devolution. Similarly, in some other State subjects, schemes have not been provided allocation from Centre, as States may like to decide on the efficacy and need for such schemes. The shift is monumental, in terms of changes in the mode of implementation and will undoubtedly require a transition phase. Therefore, certain minimum provision has been made to meet the requirement in the first quarter, with a proviso to re-examine the need for continuation in the initial part of the financial year. Going forward, there is need to change the design of many schemes as also the implementing mechanism in line with the changes set in motion in this budget. The details are given in the later section on Plan expenditure.

6. In terms of trends, the gross tax revenue estimates in FY 2015-16 have been estimated with growth of 15.8 per cent over RE 2014-15, which implies tax to GDP ratio at 10.3 per cent. Total expenditure in FY 2015-16 is estimated to grow marginally by 5.7 per cent over RE and is pegged at 12.6 per cent of GDP. As compared to BE 2014-15, total expenditure shrinks by 1 per cent due to shrinking resource base and fiscal consolidation following FFC, as explained above. Non-tax revenue has shown growing trends in last couple of years. It has been revised upwards, despite high base in FY 2014-15. However, on an increased base the growth in 2015-16 over the RE is about 1.8 per cent, but it is slated at 1.6 per cent of the GDP. On the expenditure side, government has provided realistic allocations for subsidies based on the assessment of exchange rate and lower crude oil prices in the international market. In FY 2014-15, there was scope for some saving in the subsidy bill for petroleum and fertilizer, while additional allocation had to be made for Food. Easing of international prices of crude oil provided the much needed opportunity to introduce some reforms in fuel prices as also clear some of the financial burden. Additional allocation has been made to fill cavern for building up reserves in RE 2014-15. As ratio of GDP, it is expected that major subsidies would come down from 2.0 per cent in RE 2014-15 to 1.6 per cent in BE 2015-16. With deregulation of diesel prices and rationalization of LPG subsidy, it is expected that the provision for fuel subsidy kept in the budget should suffice. However, increased allocation for food subsidy has been retained in view of additional requirements to meet the demand from National Food Security Act. While limiting the Non-plan expenditure to 9.3 per cent of the GDP in 2015-16, an increase of 8.2 per cent over the RE 2014-15 has been provided to meet the commitments of the government.

7. Non-debt capital receipts have been revised down ward at ₹42,236 crore in RE 2014-15. In B.E. 2015-16, to meet the additional resources requirement following shrinking of tax revenues for the centre due to higher devolution to States, the non-debt capital receipts has been revised upwards and targeted at'80,253 crores. Significantly net taxes to Centre, as ratio of GDP, has declined from 7.2 per cent in RE 2014-15 to 6.5 per cent in B.E. 2015-16. As a result, a total revenue receipt of the centre has declined from 8.9 per cent in RE 2014-15 to 8.1 per cent in B.E. 2015-16, as ratio of GDP. Debt receipts have increased in nominal terms, while reducing the fiscal deficit target to 3.9 per cent. Thus, the total resources of centre after absorbing the impact of FFC and continuing on the path of consolidation, albeit with revised roadmap, has declined marginally from BE 2014-15.

8. The fiscal rules required elimination of effective revenue deficit and limiting revenue deficit to 2 per cent by 31st March, 2015. As pointed out in the MTEF statement presented along with the Budget 2014-15, this stipulation required removing imbalances on the revenue account. While, fiscal deficit could be steered as per the roadmap adopted in 2012-13, the targets on revenue account required compositional shift in the designing of Plan schemes with greater emphasis in transfer of funds for creation of capital assets. Re-designing of centrally sponsored schemes was initiated in FY 2014-15, the scope was however limited

as the changes have to be balanced keeping in view the spending in social and welfare sectors for the protection of vulnerable sections. Revenue deficit in budget 2015-16 has been retained at 2.8 per cent to meet the commitment under various welfare programmes. It is proposed to re-align the targets on revenue account, with the fiscal deficit target. Thus, it is proposed to set the target for elimination of effective revenue deficit and confining the revenue deficit at two per cent of GDP by 31st March, 2018; co-terminus with the fiscal deficit target. Necessary amendment in the FRBM Act and Rules are being introduced accordingly.

Fiscal Outlook for 2016-17 to 2017-18

9. The General Budget 2015-16 re-affirms Government's commitment to carry the process of fiscal consolidation. Accordingly, the fiscal deficit target of 3.9 per cent has been retained in this year's fiscal policy. Going forward, in the medium term fiscal deficit target will be progressively reduced to 3.5 and 3.0per cent in FY 2016-17 and 2017-18 respectively. This implies limited fiscal space over the medium term period. The process of fiscal rectitude which has so far been largely on the expenditure side will have to be matched by greater resource mobilization in coming years.

10. Fiscal parameters on the revenue account, revenue deficit and effective revenue deficit, presented in the general budget 2015-16 remain out of bounds set forth in the fiscal rules. While revenue deficit in 2015-16 at 2.8 per cent shows a marginal improvement from 2.9 per cent in RE 2014-15, Effective Revenue Deficit climbs up from 1.8 per cent in RE 2014-15 to 2.0 per cent in BE 2015-16. This is mainly due to changes in the nature of transfer of resources to States. It is interesting to note that following the recommendations of FFC, the untied transfers to States (devolution of taxes and duties) which was about 49 per cent of total transfers in 2014-15 marks a steep rise to 63 per cent in 2015-16.

11. In order to protect the interests or poor and needy, Government has decided to continue welfare programmes while giving greater space to States in development schemes. Thus, much of the funds that were hitherto considred as grant-in-aid for capital expenditure are subsumed within untied funds that are now to be transferred to States directly. It has been decided, accordingly, to relax some of the fiscal rules with regard to revenue account imbalances, while continuing with the fiscal consolidation stance, by couple of years. It is expected that the transition phase can be spanned out in FY 2015-16, whereupon the correction on the revenue account can be effectively implemented. Accordingly, necessary amendment to the FRBM Act is being proposed in the Budget 2015-16. The amendment will be followed by notifying new Rules.

12. However, it is pertinent to note that the resource base of the Centre will be constrained following the implementation of the FFC. With steep jump in the sharing pattern of tax revenues, the revenues of the States, which is surplus in most of the cases, will be further augmented on one side and the Centre will face resource crunch in one of the difficult phases of consolidation underway. While, the revenues are constrained in the FY 2015-16, it would continue over the medium term framework in FY 2016-17 and 2017-18. Moreover, the 7th Pay Commission impact may have to be absorbed in 2016-17. The phase of consolidation, extended by one year, will be also be spanning out in the period. Thus, in the medium term framework the fiscal position will continue to be stressed. However, with necessary corrections on the Plan side under the new paradigm of Centre-State fiscal relationship and reforms on the subsidies, with better targeting and policy initiatives, it is expected that over the medium framework much of the fiscal correction would have taken shape, leaving room for building up better fiscal management thereupon. The change is monumental; and needs dextrous manoeuvring in this initial phase.

13. Gross tax revenue is estimated to increase from 9.9 per cent of GDP in RE 2014-15 to 10.3 per cent in BE 2015-16 (reflecting growth of 15.8 per cent over RE 2014-15), which is however lower than peak of 11.9 per cent of GDP achieved during 2007-08. With economy poised for economic turnaround, it would be possible to get back to the achieved level of tax to GDP ratio. In the medium term targets, gross tax collection as percentage of GDP is projected at 10.5 per cent in 2016-17 and 10.7 per cent in 2017-18.

14. Despite the resource crunch in FY 2015-16, government has remained steadfast in its commitment to reduce the fiscal deficit from 4.1 per cent of GDP in RE 2014-15 to 3.9 per cent in B.E. 2015-16. Total expenditure as per cent of GDP is reducedfrom 13.3 per cent in RE 2014-15 to 12.6 per cent in B.E. 2015-16. Going forward, it is estimated that the expenditure of the government will be progressively reduced to 12.1 and 11.6 per cent of the GDP in the financial years 2016-17 and 2017-18 respectively. On the other hand the tax revenues of the Centre are estimated to reduce sharply from 7.2 per cent of GDP in RE 2014-15 to 6.5 percent in BE 2015-16, with the change in

devolution. Over the period of next two years it is expected to increase marginally to 6.7 and 6.8 per cent respectively. With improvement in the macro-economic conditions and revival of growth, it is expected that tax reforms including implementation of GST on the indirect taxes side and rationalization of tax structure in the direct taxes will restore the total tax revenues of the government to the higher levels.

15. Non-tax revenue has emerged as one of the important components of government resources, in the present phase of fiscal consolidation. With tax revenues under pressure due to slowdown in the economic growth, the rise in non-tax revenues has played key role in the fiscal rectitude in recent years. Non-tax revenues grew by 45 per cent in 2013-14 over the previous year, 2012-13. In the general budget 2014-15 it was estimated to grow by 6.7 per cent over the last year's actuals, to reach level of 1.7 per cent of GDP. In RE 2014-15, it has been estimated at 1.7 per cent of GDP, which is 2.5 per cent higher than BE 2014-15. In General Budget 2015-16, Non-tax revenue receipts are estimated to grow by 1.8 per cent over RE 2014-15.However, the growth in this component of revenue is limited and it is expected that in next two years it will register modest growth. It is estimated that as ratio of GDP, non-tax revenue will be at 1.5 and 1.4 per cent in the financial year 2016-17 and 2017-18 respectively.

16. Despite extension of target for fiscal consolidation by one year, Budget 2015-16 continues on the path or progressively reducing the gap between Government resources and spending. Thus, total liabilities of the Central Government, as a percentage of GDP, will also see a decline continuing with the trend in the recent past. At end of 2014-15, total liability of the Government was estimated at 46.8 per cent of GDP which will reduce to 46.1 per cent by the end of 2015-16. Continuing the declining trend it is likely to reduce to 44.7 per cent in 2016-17 and 42.8 per cent in 2017-18. A progressive reduction in debt-GDP ratio of the Government will ease the interest burden and allow more space for the government to spend particularly on infrastructure development without taking recourse to additional borrowings.

B. Assumptions underlying the fiscal indictors

1. Revenue receipts.

(a) Tax-Revenue

17. Tax revenues as a percentage of GDP, riding on high economic growth and aided by rich menu of tax reform measures, reached its peak by 2007-08 and touched a level of 11.9%. Average annual tax growth rate during the five year period in 2003-08 was 21.3%, where annual tax growth was highest at 28.9% in 2006-07. These reforms were mainly driven by direct tax whose average annual growth rate during this period was about 28%. The buoyancy of tax revenue with respect to GDP was almost 1.5 during this period. This trend of high tax growth was moderated due to global economic crisis and the tax-GDP ratio slid to 10.8% in 2008-09 and further to 9.6% in 2009-10.

18. In years, following global crisis, the tax revenues declined due to reduction in custom duties and central excise as part of the stimulus package. Subsequent slowdown in the economy also impacted the revenues. From 2012-13 onwards, fiscal consolidation phase has been marked by taxes performing lesser than the estimates. Consequently, the fiscal correction has been largely an exercise in expenditure management. The tax to GDP ratio has remained around 10 per cent with tax buoyancy less than one.

19. The need for realistic projection in tax growth was much needed. This base correction has been made in the Budget 2015-16. Despite revival of growth in the current year, the tax revenues remained under stress. Easing of inflationary pressure ensured that the nominal growth remained stagnant despite higher real growth in the economy. Thus, indirect taxes remained sluggish, though direct taxes did register growth on the expected lines. Overall, the Gross taxes were revised downwards by 8.3 per cent in the RE 2014-15, implying tax to GDP ratio of 9.9 per cent as opposed to 10.6 per cent at the B.E. stage. Accordingly, the Gross tax revenue has been estimated at 10.3 per cent of GDP in Budget 2015-16, with a growth of 15.8 per cent over RE 2014-15. Projections for 2015-16 have been made taking into account a realistic economic recovery and continuation of set of tax measures announced in the budget for 2014-15. It is also expected that reforms in the administrative machinery oriented towards strict implementation will yield result.

Details of Tax Measures

20. With above measures, tax revenues in BE 2015-16 are targeted to grow at 15.8 per cent over the RE of 2014-15. The tax to GDP ratio estimated in the Budget 2015-16 is 10.3 per cent. With revival of the growth, and stabilization of various macro-economic parameters, favourable international prices for crude oil etc. afford an opportunity to attain the revenue targets in FY 2015-16.

21. Tax reforms and tax efforts are the most critical elements for the overall process of fiscal consolidation. Without a robust and ambitious tax growth it is not possible to achieve the fiscal roadmap which the Government has embarked upon. While the tax projections need to be realistic, at the same time they need to be ambitious to enable Government in achieving the fiscal roadmap without resorting to more than required expenditure compression. Overall, while tax should increase as percentage of GDP, expenditure should progressively reduce as percentage of GDP till the fiscal consolidation goals are fully met. While the ultimate objective should be to bring back the tax to GDP ratio to the pre-crisis levels, it should be calibrated gradually in consonance with the prevailing macro-economic situation. As the tax to GDP ratio increases, incremental improvements would be more gradual and difficult to achieve. The outlook for tax revenues for the years 2016-17 and 2017-18 have been designed keeping this in mind. As shown in table above the tax to GDP ratio is projected to reach 10.5 per cent in 2016-17 and 10.7 per cent in 2017-18. This implies an average buoyancy of 1.25 in next three years which is a realistic target. This will require an average tax growth of 15.0 per cent during this period which would be possible through a combination of better tax effort. It may be contextual that a much higher tax growth has been achieved in the previous decade.

(b) Devolution to States

22. As mentioned earlier, FY 2015-16 is the first year of the Award period of the 14th Finance Commission. FFC has mandated major jump in the sharing of taxes between the centre and the States, thereby re-defining the fiscal relationship. The paradigm shift is none-the-less in consonance with Government's drive towards co-operative federalism. At 42 per cent devolution, it is expected that the States' share will increase from ₹ 3.38 lakh crores in FY 2014-15 to about ₹ 5.24 lakh crores in FY 2015-16, a quantum jump. Interestingly, tax revenues to centre as ratio of GDP will decline from 7.2 per cent in RE 2014-15 to 6.5 per cent in B.E. 2015-16. It will marginally improve to 6.7 per cent and 6.8 per cent in the FY 2016-17 and 2017-18 respectively.

(c) Non Tax Revenues

23. Non Tax Revenues of the Centre mainly comprise of interest and dividend receipts of the Government, receipts from the services provided by Central Ministries and Departments like supply of central police force to various agencies, issue of passport and visa, registration of companies, patents and license fees, royalty from off-shore oil fields, profit petroleum and various receipts from telecom sector. In FY 2013-14 ₹ 1,98,870 crore was realized, recording a growth of 45 per cent over the previous year, at 1.8 per cent of GDP. In the general budget 2014-15, non-tax revenues were estimated at ₹ 2,12,505 crore marking a growth of 6.9 per cent over actuals of 2013-14. In RE 2014-15, it has been revised upwards to ₹ 2,17,832 crores, at 1.7 per cent of GDP it marks an increase of 2.5 per cent over BE 2014-15. This component of revenue has shown marked increase in last years and has grown to be comparable with one of the Indirect taxes in nominal terms. However, on an increased base there is little scope to increase this item of revenues. In BE 2015-16, Non-tax revenue receipts are estimated at 1.6 per cent of GDP which marks 1.8 per cent increase over RE 2014-15.

24. Interest receipts of Government that are mainly from Railways, State Governments and loans extended by central ministries and departments to Central PSUs.Interest receipts from States will be declining overall as net lending from states has considerably reduced after disintermediation as per the recommendations of 12th Finance Commission. Dividends receipts of the Centre may be split into two parts, one from RBI and banks and the other is from various PSUs. While dividends from PSUs should grow as their profit grows, they would be moderate due to disinvestment of Government stake in PSUs. On the contrary, since the Government would be infusing equity into banks to meet the CRAR requirement of BASEL III, the dividend from banks would increase relatively faster due to the coupled effect of increase in profit and increase in GoI stake in public sector banks. Another important component under the Non-tax revenue has been the Telecom receipts. It has grown to be significant component since the turn of this century, with the boom in telecommunication sector. The expected revenues have not been forthcoming due to litigations in some of the auctions, but it is expected to continue to be major source of revenue over the medium term framework.

25. Mostly following the assumptions above, the outlook for non-tax revenues for 2016-17 and 2017-18 have been put in place. Certain one-time receipts budgeted in earlier financial year will not be available as these were due to unlocking of resources. With regard to dividends from PSUs, the policy of the Government would be to enable them in investing their retained earnings in their capital projects. However, in the absence of any concrete capital investment plan PSUs should pay their cash surpluses as dividend to

Government and other shareholders. From telecom sector it has been assumed that renewal of licenses issued for 20 years earlier will come up for renewal during the projection period. The success of Spectrum auctions scheduled in near future will translate into higher revenues on regular basis over the term of allocation. This will entail stable stream of income to the government. Based on the assumptions, the non-tax revenue for 2016-17 and 2017-18 has been projected at 1.5 per cent and 1.4 per cent of GDP respectively.

2. Capital receipts

(a) Recovery of loans and advances

26. Net recovery of loans from the States have declined during the 12th FC award period on account of gradual disintermediation by Central Government and the debt consolidation and debt waiver scheme. Since further loans are not given to State governments, except eternally aided projects which are passed through on back-to-back basis, this receipt will decline over years as old loans get liquidated. The repayment of loans from Central PSEs is also impacted on account of defaults from PSEs that are either sick or under revival through BIFR. The waiver of interest or write off of loans of sick PSUs has reduced the potential future receipts. Recovery of loans and advances was estimated at ₹ 10,527 crore in B.E.2014-15. However, it was revised to ₹ 10,886 crore in RE 2014-15. In BE 2015-16 it is estimated at ₹ 10,753 crores. For 2016-17 and 2017-18, this component of receipt is estimated to be flat at ₹ 10,500 crore as the government would not encourage net lending (except for the back to back arrangement made for external loans to States).

(b) Other non-debt capital receipts

27. Disinvestments in Government PSUs are main source of receipts under this head. From FY 2013-14 government decided to create a separate fund, NIF under Public Account, with the intent that proceeds from disinvestment will only be deployed for specific authorized purposes. With this major step forward, the proceeds will not be available to fund regular government spending. As per actuals for FY 2013-14, receipts from disinvestment proceeds accounted at ₹29,368 crore.

28. In R.E. 2014-15, disinvestment receipts have been pegged at ₹ 31,350 crores, including ₹ 5,000 crores from sale of SDRs to RBI. For General budget 2015-16, receipts from disinvestment have been estimated at ₹ 41,000 crore. However, as additional resource mobilization to meet the revenue shortfall following 14th Finance Commission, ₹ 28,500 crores have been estimated to flow from strategic disinvestments. These include sale of government holdings in non-government commercial entities, SUUTI, BALCO, HZL etc. Over the medium term frame work, an amount of ₹ 55,000 crore and ₹ 50,000 crores has been estimated for the years 2016-17 and 2017-18 respectively.

(c) Borrowings – Public Debt and other Liabilities

29. Of the overall Central Government liabilities (net of inter-government borrowings), about 92.7 per cent is domestic and only 8.3 per cent is external as at end-March 2014. It may be observed that, in India's context, despite India's high gross fiscal deficit (GFD) during 2008-2013 on account of government's efforts to safeguard India against slowdown being caused by global financial crisis, debt position in India is practically stable (or better) at a time when public debt position has been deteriorating globally. In RE 2014-15, net market borrowings through dated securities is estimated at ₹ 4,46,922 crore (after the netting ₹ 6283 crore of buyback). to finance 87.2 percent of gross fiscal deficit (GFD). Other sources of the GFD financing such as short term treasury bills, small savings collections, state provident funds, net external assistance and cash draw down were budgeted to finance the remaining 12.8 per cent of the GFD. The realization from external assistance was higher than budgeted at ₹ 9,705 crore. There was negative outflow from other debts due to higher disbursements than estimated initially. Similarly, the realization from State Provident funds had to be revised downwards. Treasury bill realization also increased due to higher investment by State governments in the non-competitive auction T-bills. This was mainly on account of comfortable cash position of the State Governments and higher interest rates in auction T-bills as compared to Intermediate T-bills. Better fiscal management resulted in reduction of market borrowings by ₹14,283 crore to ₹4,46,922 (adjusted for repurchases of G-secs maturing in 2015-16) crore for fiscal year 2014-15. Borrowings programme for the year was conducted smoothly broadly in line with pre-announced calendar for borrowings. Auction for borrowings were reduced by '16,000 during August 14, 2014 to September 30, 2014, from the auction calendar for first half of financial year 2014-15, announced in March 2014, after review of Central Government's cash position. The weighted average maturity of primary issuances of dated securities in fiscal year 2014-15 increased to 14.66 years from

14.28 years in the previous year, reflecting the continued efforts by the Government to elongate the maturity profile of its debt. The weighted average yields of issuance in fiscal year 2014-15 went marginally up to 8.51 per cent from 8.48 per cent in the previous year.

30. In line with Government's commitment to fiscal consolidation measures under the revised roadmap discussed above, the fiscal deficit for 2015-16 is budgeted to decline to 3.9 per cent of GDP. Accordingly, total borrowings requirement for 2015-16 has been budgeted at ₹ 5,55,649 crore. However, in nominal terms net borrowing projections at ₹ 4,56,405 crores shows an increase of 2.1 per cent over the previous year. In terms of GDP, net market borrowing is budgeted to decline to 3.2 per cent as compared with 3.5 per cent in FY 2014-15. Borrowings through external debt are budgeted at ₹ 11,173 crores during 2015-16, increase of 15.1 per cent over RE 2014-15. In nominal terms, on a lower base, the increase is not substantial. In FY 2015-16, the share of external debt in the net Central Government debt is declining to 7.6 per cent from 8.3 per cent in FY 2014-15.

31. Commercial banks are major investor category which currently holds about 45.7 per cent of outstanding dated securities (at end-Sep 2014). The deposits of commercial banks during 2014-15 saw a y-o-y growth of 11.6 per cent (as on January 23, 2015), which is lower than 15.3 per cent growth seen in the same period of previous year. Insurance companies are another major investor category in the government securities, which traditionally has demand from longer tenor securities. As at end of September 2014 the share of insurance companies holding in the central government dated securities increased to 20.6 per cent from 19.5 per cent at end of previous financial year. Provident funds are another stable source of demand for government securities whose share is stable at around 7.2 per cent. A significantly higher growth in deposits of commercial banks vis-a-vis the budgeted growth in net market borrowings of Government implies that the government borrowings programmes for 2015-16 will completed comfortably without exerting any pressure on availability of financial resources for the private sector. Furthermore, improved share of insurance companies and stability in the share of provident funds in holding of government securities provide space for further increasing the maturity profile of the Government debt without increasing the cost.

32. Total liabilities of the Government, as a percentage of GDP, will also see a decline continuing with the trend in the recent past. At end of 2014-15, a total net liability of the Central Government is estimated at 46.8 per cent of GDP which will reduce to 46.1 per cent by the end of 2015-16. With gains of fiscal consolidation setting in and deficit being contained, the declining trend will continue. It is likely to reduce to 44.7 per cent in 2016-17 and 42.8 per cent in 2017-18. A progressive reduction in debt-GDP ratio of the Government will ease the interest burden and allow more space for the government to spend on other/developmental expenditure without taking recourse to additional borrowings. Gross fiscal deficit is projected to decline progressively to 3.9 per cent of GDP in 2015-16. The MTFP statement projects a further decline in GFD to 3.5 per cent by 2016-17 and to 3.0 per cent by 2017-18. Assuming market borrowings financing at about 86.5 per cent of the GFD, the net market borrowings are likely to decline significantly in next three years to 3.2 per cent of GDP in 2015-16, 3.1 per cent in 2016-17 and 2.6 per cent in 2017-18. With contraction of government deficit there will be more room for private investment and capital inflows. This will also ease inflationary pressure providing comfort to RBI for easing monetary policy.

3. Total Expenditure

(I) Revenue account.

(i) Plan Revenue Expenditure.

33. The Plan size in last several years has been ambitious, though aspirational. It is noteworthy that during the 12th plan period starting from 2012-13, the budget estimates have been higher than the achievement in successive years. In fact, to finance such ambitious Plan, higher revenue growth had to be targeted, to be revised at lower levels subsequently. Thus, the exercise became idealism, divorced from the implementation capacity. With the change in the institutional arrangement from Planning Commission to NITI Ayog, an attempt has been made to rectify the problems in approach to Plan. The top-down, one-size-fit-all approach has been abandoned in favour of co-operative federalism that encourages States to play more active role in designing and implementing the development agenda based on local conditions. With higher devolution, the Finance Commission has laid down the roadmap for this new paradigm. Thus, Finance Commission has proposed in letter what Government had already started implementing in spirit.

34. During 2013-14, government efforts for fiscal consolidation resulted in containing total plan expenditure at 4.0 per cent of GDP, lower than the RE 2013-14. The Plan Expenditure for 2014-15 was budgeted at ₹ 5,75,000 crore with growth of 26.9 per

cent over the performance in last financial year. In RE 2014-15, Plan expenditure is revised at ₹ 4,67,934 crore, which shows reduction of 18.6 per cent over BE 2014-15. The downward revision was necessitated due to lower revenues and lower pace of utilization following scheme revision in few cases.

35. With higher devolution, Finance Commission as also States have called for greater flexibility in the design and implementation of schemes. With higher resources at their disposal, States are in position to share the responsibility of development programmes. Under the new paradigm, the Plan spending will be altered. However, there will be transitional issues that need to be managed smoothly to avoid any disruptions in the field. For F.Y. 2015-16, Plan expenditure is budgeted at ₹ 4,65,277 crore, which is 3.3 per cent of GDP and 0.6 per cent lower than RE 2014-15. In view of higher devolution, Centre's resource base has shrunk. However, in order to meet the spending on social and welfare programmes, and also to provide sufficiently to on-going schemes and programmes during the transition phase, additional resources mobilization has been planned to provide adequately to the development needs. Going forward, with fiscal consolidation and limited revenue share, it is projected that as ratio of GDP the total expenditure budget of the centre will contract, with lesser Non-Plan and Plan size. Accordingly, it is projected that resources for plan expenditure will be at 2.9 per cent and 2.7 per cent of GDP in FY 2015-16 and FY 2016-17 respectively.

36. It is important to note that while giving its recommendation for higher devolution to States, FFC has taken into account the transfer of central funds to States through various developmental programmes and subsumed this item in general transfer. Thus, with greater sharing of resources with States, it is assumed that Centre would withdraw from welfare programmes. However, Budget 2015-16 continues with central allocation for the needy and vulnerable, as sudden withdrawal from these programmes may lead to hardship. Schemes that are in nature of providing helping hand to the needy and poor need to be continued at national level; to ensure uniformity and continuity. Accordingly, different components under the Plan have been categorized under three sections as depicted in Statement 16 and 16-A of expenditure budget volume 1. Significantly, over 30 Centrally Sponsored Schemes that have been identified which ought to have been transferred to the States because expenditure on them has already been taken into account as State expenditure, in arriving at the greater devolution of 42% to the States. However, keeping in mind that many of these schemes are national priorities, and some are legal obligations (such as MGNREGA) and in order to underline the Central Government's continued support to national priorities, especially with regard to schemes meant for the poor, most of these are proposed to be continued. It is proposed that only 8 Centrally Sponsored Schemes be delinked from support from the Centre.

37. Certain programmes of the Government will have to continue unaltered as they are either legal/ Constitutional obligations, or are privileges available to the elected representatives for welfare of their constituents. Further, and more importantly it is proposed that the Union Government may continue to support certain programmes which are for the benefit of socially disadvantaged in an unaltered manner from its own resources. In respect of various other centrally sponsored schemes, the sharing pattern will have to undergo a change with States sharing a higher fiscal responsibility in terms of scheme implementation. Details of changes in sharing pattern will have to be worked out by the administrative Ministry / Department on the basis of available resources from Union Finances. In addition, Budget 2015-16 provides additional allocation of ₹ 20,000 crores to NITI for interventions as special assistance.

(ii) Non Plan Revenue Expenditure

38. Non Plan Revenue Expenditure of government mainly consists of its establishment expenditure, interest payments, defence expenditure, subsidies, statutory grants to States and other residual items. The Non Plan Revenue Expenditure jumped from 8.4 per cent of GDP in 2007-08 to 10.2 per cent of GDP in 2009-10 mainly due to implementation of Sixth Pay Commission's recommendations. Since then it has come down to 8.7 per cent in 2014-15 BE due to various expenditure reform measures undertaken by the Government. In RE 2014-15 Non-plan revenue expenditure is revised downward marginally at ₹ 12,13,224 crore which is 9.3 per cent of GDP and shows reduction of 0.5 per cent over BE 2014-15. For FY 2015-16, Non-plan expenditure is estimated at ₹ 13,12,200 crore with the growth of 7.6 per cent over BE 2014-15 and 8.2 per cent over RE 2014-15. Over the projection period, it is expected at 9.2 per cent and 8.9 per cent of GDP during FY 2015-16 and FY 2016-17 respectively. Various components of Non Plan Revenue Expenditure are detailed below.

(a) Interest Payments

39. Due to fiscal expansion undertaken by the Government, interest payments increased sharply

post global economic crisis. As a percentage of net tax revenue of the Centre, interest payments jumped from 38.9 per cent in 2007-08 to 43.4 per cent in 2008-09 and further to 46.7 per cent in 2009-10. In BE 2014-15 expenditure under this component was estimated at 43.7 per cent of net tax to centre which has been revised at 45.3 per cent in RE. The increase in the revised estimate is essentially due to lower tax realization. The factors that have impacted interest payment during the recent period are the increased debt stock due to stimulus measures along with the fiscal slippage during 2011-12 and relatively tougher interest rate regime that has been in existence for quite some time now.

40. In BE 2015-16, interest payment is projected at 49.6 per cent of net tax to Centre, which is marked increase over the last year despite fiscal consolidation underway. The increase is again due to the shrinking revenue base of the centre following higher devolution recommended by FFC. In fact interest payments of the centre as a ratio of gross tax revenue shows the secular trend of decline from 32.9 per cent in RE 2014-15 to 31.5 per cent in BE 2015-16. With the fiscal deficit coming down and easing of inflationary pressure, it is expected that interest rates would be falling in the years to come. Deficit reduction and fall in interest rates would create positive space for the private sector to raise resources at lower cost. With policy of fiscal reforms gaining ground, over the medium term it is expected that ratio of interest payment to net tax revenue of the Centre will come down to 47.5 per cent in FY 2016-17 and 45.1 per cent in FY 2017-18.

(b) Defence Services

41. Defence Expenditure on the revenue account mainly comprises of salary expenditure of defence forces and their operational expenses. Defence Revenue Expenditure was estimated at ₹ 1.34 lakh crore in BE 2014-15. In RE 2014-15 it has been revised upwards marginally at ₹ 1,40,405 crore. For FY 2015-16 Defence Revenue Expenditure is estimated at ₹ 1,52,139 crore i.e. growth of 13.2 per cent and 8.4 per cent over BE 2014-15 and RE 2014-15 respectively. During projection period i.e. FY 2016-17 and 2017-18, it expected to grow by 15 per cent, average. Additional provision has been assumed in the financial year FY 2016-17 and 2017-18 to accommodate the likely impact of VII Pay Commission. Total Defence expenditure as ratio of GDP is projected to remain at 1.8 per cent of GDP in FY 2016-17 and 2017-18 respectively.

(c) Pensions

42. The expenditure on pension payments of the Central Government includes both defence as well as civil pensions. Pension payment, in nominal terms was estimated at ₹ 74,076 crore in RE 2013-14 and at the year-end it was accounted at ₹ 74,896 crore. In BE 2014-15, pension payment in nominal terms was estimated at ₹ 81,983 crore. In RE 2014-15, it has been revised at ₹ 81,705 crore. The pension payment of Central Government for the past few years has been growing faster than the salary expenditure. The main reason for this is that there is an increase in number of pensioners due to higher retirements and increased life expectancy. In view of the likely impact of VII Pay Commission, Pension payment of the Government likely to be about 0.7 per cent of GDP in FY 2016-17 and FY 2017-18 respectively.

(d) Non Plan Grants to States

43. Non Plan Grants to States mainly comprises of the grants recommended by the Finance Commission. In BE 2014-15 Non-plan Grants were estimated at ₹ 69,084 crore. In RE 2014-15, Non-plan Grants to States were revised at ₹ 79,166 crore. In the view of recommendations of XIV Finance Commission, for BE 2015-16, non-plan Grants to States are estimated at ₹ 1,07,559 crore. Normally most of the grants recommended by Finance Commission are recommended to flow from second year of the award period to ensure a convenient preparatory period for the State Governments. Based on these assumptions Non Plan Grants have been projected at 0.6 per cent and 0.5 per cent of GDP in 2016-17 and 2017-18 respectively.

(e) Major Subsidies

44. As per actuals for 2013-14 expenditure on major subsidies was accounted at ₹ 2,44,717 crore. This had been constituted by food, petroleum and fertilizer at ₹ 92,000 crore, ₹ 85,378 crore and ₹ 67,339 crore respectively. In BE 2014-15, Major subsidies were budgeted at ₹ 2,51,397 crore which have been revised at₹. 2,54,913 crore in RE 2014-15. Major subsidies have been budgeted in 2015-16 at 1.6 per cent of GDP as against 2.0 per cent in BE 2014-15. Over the projection period, major subsidies are estimated at 1.6 per cent of GDP. In order to achieve the fiscal targets of fiscal consolidation it is essential that government follows the policy of progressively reducing the expenditure on subsidy through improved targeting of beneficiary.

45. Major subsidies are extremely critical from the viewpoint of fiscal consolidation and are the most important factor in determining the success of Government in meeting its fiscal targets. The effort of Government would be to address this issue with a two pronged strategy. Government is committed to progressively pursuing subsidy reforms in a manner that will ensure efficient targeting of subsidies to the poor and needy, while also saving scarce financial resources for investment in infrastructure and pursuit of new development programmed announced by the Government. It is pertinent to mention that both petroleum and diesel are now fully decontrolled. The Government has launched a new universal Direct Benefit Transfer Scheme for LPG from 1st January, 2015 onwards. The new scheme will cover both Aadhaar card and non-Aadhaar card holders. The subsidy will be transferred directly into the bank accounts of cash-transfer-compliant customers in a manner that will avoid duplication and prevent leakages.

46. On fertilizers, Nutrient based subsidy regime has been working well in the P&K sector. What is now urgently required are certain pricing reforms in the urea sector with an immediate price correction for urea, new Nutrient based Urea Policy. This is not only essential from viewpoint of the size of the subsidy bill but also from the viewpoint of balanced use of N, P & K nutrients. Government had notified the New Investment Policy (NIP)-2012 on 2nd January, 2012 to encourage investments in urea sector leading to increase in indigenous capacities and reduction in import dependence. The policy will also lead to savings in subsidy due to import substitution at prices below IPP. Over long term, there is need to increase indigenous production of fertilizers which will help reducing dependence on imports and make prices much more stable.

47. Government has also launched a dedicated scheme for end-to-end computerization of Public Distribution System throughout the country. 11 States have already joined the National Food Security Act Framework and as the required systems are put into place the other States will follow suit. Simultaneously drive has been launched to ensure universal coverage of Aadhaar throughout the country. Decentralised Procurement and distribution of foodgrains, end-to-end computerization, combined with universal Aadghaar coverage, improving the operational efficiency of the FCI are some of the measures that will set the stage for the next generation food subsidy reforms. Government will actively pursue this during the course of this financial year. As already explained without focused subsidy reforms, the process of fiscal consolidation will be difficult. The expenditure of Government on major subsidies is projected to come down from 2.2 per cent of GDP in 2013-14 to 2.0 per cent of GDP in 2014-15. It is expected that with active policy reforms the incidence will progressively reduce. Over the projection period it has been proposed to contain at 1.6 per cent in 2016-17 and 2017-18 respectively.

(II) Capital Outlay

48. As per the acctuals 2013-14, total capital expenditure of Government was ₹ 1,87,675 crore and it was estimated grow up to ₹ 2,26,781 crore in BE 2014-15. However, in RE 2014-15, it has been revised at ₹ 1,92,378 crore. In BE 2015-16, total capital expenditure of Government is estimated at Rs. 2,41,431 crore which is 6.5 per cent higher than BE 2014-15 and 25.5 per cent higher than RE 2014-15. On the non-plan side, the major portion of Capital Expenditure consists of the Defence Capital Expenditure. In BE 2014-15, the Defence Capital Expenditure was estimated at ₹ 94,588 crore. For FY 2015-16, it has been retained at ₹ 94,588 crore, a growth of 15.4 per cent over RE 2014-15. On an increased based, it has been assumed at nominal growth of 15.9 per cent in FY 2016-17. However, growth of 9.1 per cent has been projected for FY 2017-18, which is consistent with the overall resource availability and other demands of Centre's resources.

49. The Plan Expenditure of GoI mainly consists of gross budgetary support to gross Railway Expenditure, of national highways investments in government companies and banks and loans to State Govt. and PSUs. Since the overall effort has to be to reduce the revenue deficit of the Government, it is essential that within the overall Plan Expenditure, the expenditure on capital components grows faster than the revenue component. Plan Capital Expenditure is budgeted at 29.1 per cent of total Plan Expenditure in 2015-16 and is projected to be 25.6 per cent of total Plan Expenditure in 2016-17; and further increase to 25.7 per cent in FY 2017-18.

4. GDP Growth

50. Central Statistics Office (CSO) has recently undertaken a revision in National Accounts aggregates by shifting to the new base of 2011-12 from the earlier base of 2004-05. Under the revised base, the CSO has furnished estimates for three years from 2011-12 to 2013-14 and the Advance Estimates for 2014-15. The estimates of GDP (both at current and constant market prices) and growth rates released by the CSO under the new 2011-12 series are different from the

figures released earlier under the 2004-05 series. Economic growth, measured by growth in GDP at constant market prices, estimated at 5.1 per cent and 6.9 per cent respectively during 2012-13 and 2013-14 under the new series, was higher than the corresponding figures of 4.7 per cent and 5.0 per cent released under the 2004-05 series in May 2014. GDP at current market prices for the year 2013-14 was estimated (under the new series) at ₹ 11345056 crore. The Advance Estimates for 2014-15 has estimated the GDP at current market prices to attain a level of ₹ 12653762 crore, with a growth of 11.5 per cent, which can be decomposed into a real growth of 7.4 per cent and an implied inflation of 3.8 per cent. Assuming that the economy picks up growth momentum, under stable prices and with the reform measures of the Government making further impact, the GDP at current market prices can be expected to achieve a growth of 11.5 per cent in 2015-16 (real growth of 8.5 per cent and an implied inflation of 2.8 per cent) to attain a level of ₹ 14108945 crore. With gradual growth acceleration and under assumptions of continuing price stability, the growth rate of the GDP at current market prices during 2016-17 and 2017-18 can be expected to be around 12.2 per cent and 12.4 per cent respectively.

C. Assessment of Sustainability relating to

(i) The balance between Revenue Receipts and Revenue Expenditure

51. In the revised estimate for 2014-15 the Non-Plan expenditure is set at 107.7 per cent of total revenue receipts of the Government. Ratio of Non-plan expenditure to revenue receipts of more than one implies use of borrowed resources for consumptive expenditure. This imbalance needs to be corrected to ensure greater fiscal space for undertaking developmental works. However, with revenue receipts of the centre shrinking due to higher devolution in 2015-16, it is estimated that Non-plan expenditure will rise to 114.9 per cent. Growing interest payments, rising establishment costs including impact of VII Pay commission, subsidies and defence allocations makes this item of spending more rigid. Fiscal consolidation and higher devolution add to the increase in this ration. However, going forward it is expected that with growing revenues and containing the rise under Non-plan spending will provide the opportunity to reverse this trend and bring this item of spending within sustainable limits. Thus, the ratio of Non-plan expenditure to revenue receipts would progressively reduce to 112.4 per cent and 108 per cent over the medium term period. The revenue deficit has progressively declined from high of 4.5 per cent in 2011-12 to 3.1 in 2013-14 and is projected at 2.9 per cent in RE 2014-15; it is still some distance away from the milestone of 2 per cent set for 31st March, 2015. Further, under prevailing conditions, the fiscal framework assumptions yield a revenue deficit of 2.4 per cent which is above the two per cent limit prescribed by the new FRBM regime. It is noteworthy that the revenue deficit projections work out to 2.0 per cent in FY 2016-17, achieving the target set under the FRBM.

52. Similarly, effective revenue deficit has come down from 3.0 per cent in 2011-12 to 2.5 per cent in 2012-13 and stands at 2.0 per cent in 2013-14. It is estimated at 1.8 per cent in RE 2014-15, while it was required to be eliminated by closure of the financial year. Following the FFC, there are major changes in the nature of funds transfers to States, as explained in earlier sections. In order to protect the interests of poor and needy, Government has decided to continue welfare programmes while giving greater space to States in development schemes, with higher resources at their disposal. Thus, grant-in-aid for capital expenditure is subsumed within untied funds transferred to States. In the backdrop of such changes, the efficacy of 'effective revenue deficit' as measure to capture end-use of resources needs critical examination. It is pertinent to mention that FFC also recommends for abolition of this parameter. As per the Action Taken Report, Government has informed the Parliament that the recommendation will be examined.

53. The targets on revenue account are proposed to be re-set along with fiscal deficit, following the recalibration of fiscal rules in the aftermath of finance commission impact, as explained in earlier section. It is expected that with re-structuring of fiscal relations between the Centre and the States in the 14^{th} FC period, necessary correction on the imbalances in public finance on the revenue side will be carried out. Government has re-affirmed its commitment for fiscal reforms and acknowledged the need for restructuring the Plan schemes. However, review and restructuring of on-going schemes will have to be phased out, to protect the interest of poor and vulnerable sections of the society. Committed liabilities have to be met before affecting such changes. Thus any fundamental change in respect of the mix of expenditure may be implemented over a period of time.

(ii) The use of capital receipts including market borrowings for generating Productive Assets

54. Another important parameter to assess the quality of government spending is the ratio of Plan expenditure to fiscal deficit, which a pointer towards deployment of borrowed resources. In B.E. 2015-16, the total Plan expenditure of ₹ 4,65,277 crores is 83.7 per cent of the estimated fiscal deficit. With pressure on tax revenues continuing and Non-plan expenditure remaining higher, it is expected that the ratio will decrease marginally to 83.2 per cent in FY 2016-17 and improve in FY 2017-18 to about 89.5 per cent, pointing towards marked improvement in deployment of public resources towards development. Part of fiscal reforms is targeted to bring down debt to GDP ratio and interest payment to net tax revenue of Centre gradually to a sustainable level so as to make available precious public resources for developmental purposes. The Interest payment to net tax revenue of the Centre has progressively come down to 45.9 per cent in FY 2013-14. However, with lower revenue base in FY 2015-16, this ratio is likely to increase to 49.6 per cent. None-the-less with improvement in public finances further, it is estimated to reduce to 47.5 per cent in FY 2016-17 and 45.1 per cent in FY 2017-18.

55. Capital expenditure which has witnessed declining trend in last several years. As ratio of total expenditure, the capital expenditure has reduced from a high of 23.2 per cent in FY 2003-04 to around 12 per cent in recent years. There is need to improve the capital spending to provide trigger investment and give impetus to growth. Despite revenue crunch and pressure on the Plan, capital spending in FY 2015-16 has been provided significant jump of 25.5 per cent over RE 2014-15. It is projected at 13.6 per cent of total expenditure, improvement over 11.4 per cent in RE 2014-15. The allocations in core infrastructure such as Railways, Roads etc. have been adequately provisioned.