# TARGET PRELIMS 2024
# BOOKLET-20; ECONOMY-1
# BUDGET 2024-25; OTHER UPDATES RELATED TO FISCAL DEVELOPMENT

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## 2. KEY HIGHLIGHTS FROM THE SPEECH

### 1) SOCIAL JUSTICE:

- As our PM firmly believes, we need to focus on **four major castes**. They are, 'Garib' (Poor), 'Mahilayen' (women), 'Yuva' (Youth) and 'Annadata' (farmer). There needs, their aspirations, and their welfare are our highest priority.

- **Garib Kalyan, Desk Ka Kalyan**:
    - Government has assisted 25 crore people to get freedom from **multi-dimensional poverty**.
    - '**Direct Benefit Transfer'** of 34 lakh crore from the government using PM-Jan Dhan accounts has led to savings of Rs 2.7 lakh crores for the government. The savings have helped in providing more funds for Garib Kalyan.
    - '**PM SVANidhi'** has provided credit assistance to 78 lakh street vendors. From that a total of 2.3 lakh have received credit for the third time.
    - **'PM JANMAN'** Yojana reaches out to the PVTG groups.
    - '**PM Vishvakarma Yojna**' provides end to end support to artisan and craftspeople engaged in 18 trades.

- **Momentum to Nari Shakti**:
    - 30 crore Mudra Yojna loans have been given to women entrepreneurs.
    - Making Triple Talaq illegal.
    - Reservation of 1/3rd of the seats for women in the Lok Sabha and State legislative assembly.
    - Giving over 70% houses under PMAY in rural areas to women.

- **Welfare of Annadata**:
    - **PM-KISAN SAMMAN Yojna**: It provides direct financial assistance to **11.8 crore farmers** including marginal and small farmers.
    - **PM Fasal Bima Yojna** provides crop insurance for 4 crore farmers.
    - **E-NAM** mandis have integrated 1361 mandis and is providing services to 1.8 crore farmers with trading volume of Rs 3 lakh crores.

- **Empowering Amrit Peedhi, the Yuva**:
    - **PM ScHools for Rising India (PM SHRI)** are delivering quality teaching and nurturing holistic and well-rounded individuals.
    - **The Skill India Mission** has trained 1.4 crore youth, upskilled and reskilled 54 lakh youth, and established 3,000 new ITIs.
    - A large number of new Institutions of Higher Learning, namely 7 IITs, 16 IIITs, 7 IIMs, 15 AIIMs, and 390 universities have been set up.
    - **PM MUDRA Yojna** has sanctioned 43 crore loans aggregating 22.5 lakh crores for entrepreneurial aspiration of youth.

### 2) ECONOMIC MANAGEMENT

The multipronged economic management over the past ten years has complemented people-centric inclusive development. Following are some of the **major elements**.

(1) All forms of **infrastructure,** physical, digital or social, are being built in record time.

(2) All parts of the country are becoming active participants in economic growth.

(3) **Digital Public Infrastructure**, a new 'factor of production' in the 21st century, is instrumental in formalization of the economy.

(4) **GST** has enabled ***'One Nation, One Market, One Tax'***. Tax reforms have led to deepening and widening of tax base.

(5) **GIFT IFSC and the unified regulatory authority, IFSCA** are creating a robust gateway for global capital and financial services for the economy.

(6) **Proactive inflation management** has helped keep inflation within the policy band.

## 3) GLOBAL CONTEXT

- **Several achievements during G20 President of India**. The country showed the way forward and built consensus on solutions for those global problems.
- **India-Middle East Europe Economic Corridor** announced recently, is a strategic economic game changer for India and others.

## 4) VISION FOR VIKASIT BHARAT

- Our vision for Vikasit Bharat is that of "Prosperous Bharat in harmony with nature, with modern infrastructure, and providing opportunities for all citizens and all regions to reach their potential".
- The trinity of Democracy, Demography and Diversity backed by 'Sabka Prayas' has the potential to fulfill aspirations of every Indian.

## 5) STRATEGY FOR 'AMRIT KAAL'

- Government will adopt measures to foster and sustain growth, facilitate inclusive and sustainable development, improve productivity, create opportunities for all, help them enhance their capabilities, and contribute to generation of resources to power investments and fulfill aspirations.

- Government is guided by '**Reform, Perform and Transform**', the government will take up next generation reforms, and build consensus with the states and stakeholders for effective implementation.

- Government will facilitate sustaining high and more resource-efficient economic growth in line with '**Panchamrita' goals**. This will work towards energy security in terms of availability, accessibility, and affordability.

- **To facilitate** investment, government will prepare financial sector with size, capacity, skills and regulatory framework.

## 6) IMPORTANT INITIATIVES DISCUSSED IN THE BUDGET (WILL BE DISCUSSED IN DETAIL LATER IN THE CLASSES)

- **Aspirational District Program**

- **PMAY (Grameen):** Government is close to achieving the target of 3 crore houses. **Two crores more houses will be taken up in next five years** to meet the requirements arising from increase in the number of families.

- **Rooftop Solarization and Muft Bijli**: Through this program 1 crore households will be enabled to obtain upto 300 units free electricity every month. The scheme is expected to have following benefits:
  1) Financial saving of 15k-18K per year for households from free electricity and selling of surplus to the distribution companies.
  2) Charging of electric vehicles.
  3) Entrepreneurship opportunities for large number of vendors for supply and installation.
  4) Employment opportunities for the youth with technical skills in manufacturing, installation, and maintenance.

- **Housing for Middle Class**: Government will launch **a scheme to help deserving sections of middle class** "living in rented houses, of slums, or chawls, and unauthorized colonies" to buy or build their own houses.

- **Medical Colleges**: Government plans to set up more medical colleges by utilizing the existing hospital infrastructure under various department. A committee for this purpose will be set-up to examine the issues and make relevant recommendations.

- **Cervical Cancer vaccination**: Government will encourage vaccination for girls in age group of 9 to 14 years for prevention of cervical cancer.

- **Maternal and Child healthcare**:
  1) Various schemes for maternal and child health care will be **brought under one comprehensive program** for synergy in implementation.
  2) Upgradation of anganwadi centres under **"Saksham Anganwadi and Poshan 2.0"** will be expedited for improved nutrition delivery, early childhood care and development.
  3) The newly designed **U-WIN Platform** for managing immunization and intensified efforts of mission Indradhanush will be rolled out expeditiously throughout the country.

- **Ayushman Bharat**: Healthcare cover under AB Scheme will be extended to all ASHA workers, Anganwadi Workers and Helpers.

- **Agriculture and Food Processing**:
  1) **Pradhan Mantri Kisan Sampada Yojna** has already benefitted 38 lakh farmers and generated 10 lakh employment.

  2) **Pradhan Mantri Formalization of Micro Food Processing Enterprise Yojana** has assisted 2.4 lakh SHGs and 60,000 individuals with credit linkages.

  3) **NANO DAP**: After the successful adoption of Nano-UREA, application of Nano DAP on various crops will be expanded in all agro-climatic zones.

  4) **Atmanirbhar Soil Seeds Abhiyan**: Building on the initiative announced in 2022, a **strategy will be formulated to achieve *'atmanirbharta'* for oil seeds** such as mustard, groundnut, sesame, soybean, and sunflower. This will cover **research for high-yielding varieties**, widespread adoption of modern farming techniques, market linkages, procurement, value addition, and crop insurance.

  5) **Dairy Development**:
     - **Efforts to control foot and mouth disease (**a highly contagious viral disease**)** are on.
     - **India** is the world's largest milk producer, but Indian milch-animal has low productivity.
     - **A program will be built on the successes of existing schemes**, such as Rashtriya Gokul Mission, National Livestock Mission, and Infrastructure Development Funds, for daily processing and animal husbandry.

  6) **Matsya Sampada**:
     - Government has taken several steps like setting up of separate fishery department etc. for the fishery sector. All this has contributed to doubling of both inland and aquaculture production and exports since 2013-14.

     - **Implementation of Pradhan Mantri Matsya Sampada Yojna (PMMSY)** will be stepped up to:
       **a)** Enhance **aquaculture productivity** from existing 3 to 5 tons per hectare.
       **b)** Double exports to 1 lakh crore
       **c)** Generate 55 lakh employment opportunity.

     - **Five integrated aquaparks** will be set up.

- **Lakhpati Didi**:
  1) **What is Lakhpati Didi Initiative**: This initiative was announced in PM's Independence Day Speech in which he said that it was his dream to make 2 crores 'Lakhpati Didis' in the country's villages. In the Budget speech the **target has been enhanced to 3 crores**. The target is a 3-year timeline under the scheme that is being executed by Deendayal Antyodaya Yojna – National Rural Livelihood Mission.

  2) **83 lakh SHGs** with nine crore women are transforming rural socio-economic landscape with empowerment and self-reliance. Their success has assisted around 1 crore women to become Lakhpati Didi already. Their achievements will be recognized by honoring them.

- **Research and Innovation for Catalyzing growth, employment and development.**
  - PM Shashtri gave the slogan of "*Jai Jawan, Jai Kisan*". PM Vajpayee made that "*Jai Jawan, Jai Kisan, Jai Vigyan*". PM Modi has furthered that to "*Jai Jawan, Jai Kisan, Jai Vigyan, Jai Anusandhan*".
  - A corpus of **Rs 1 lakh crore** will be established with fifty-year interest free loan. This corpus will provide **long term financing or refinancing with long tenors and low or nil interest rates**. This will encourage private sector to scale up research and innovation significantly in sunrise domain.
  - A new scheme will be launched for strengthening deep-tech technologies for defence purposes and **expediting Atmanirbharta**.

## 7) INFRASTRUCTURE DEVELOPMENT RELATED INITIATIVES

- **Capital expenditure outlay** for FY25 is being increased by 11.1% to elevent lakh, eleven thousand, one hundred, eleven crore rupees (11,11,111 crores). This will be **3.4% of the GDP**.

- **Railways**:
  1) **Three major economic railway corridor programs** will be implemented. These are:
     - Energy, mineral and cement corridor
     - Port Connectivity corridors, and
     - High traffic density corridors

     The projects have been identified under PM Gatishakti for enabling multi-modal connectivity. This will improve logistics efficiency and reduce cost.
     **Significance**: Improved operation of passenger trains; accelerate logistic efficiency; promote GDP growth.

  2) Fourty thousand normal rail bogies will be converted to the Vande Bharat standards to enhance safety, convenience and comfort of passengers.

- **Aviation Sector**: In the past 10 years, number of airports have doubled to 149. Roll out of regional connectivity under UDAN scheme has been widespread. 570 new routes are carrying 1.3 crore passengers. Indian carriers have also placed orders for over 1,000 new aircrafts. This expansion of new airports and development of new airports will continue expeditiously.

- **Metro and NaMo Bharat:** India is seeing an expansion of middle class and increased urbanization. Metro Rail and Namo Bharat can be the catalyst for required urban transformation. Expansion of these systems will be supported in large cities focusing on transit-oriented development.
  1) **Note**: NaMo Bharat is an electric multiple unit (EMU) train built for RapidX (Regional Rapid Transit Services). The train was designed by the French rolling stock manufacturer **Alstom** at its engineering centre in Hyderabad, and was manufactured in Savli, Gujarat. The train has an aerodynamic design which reduces the drag when it travels. The train has a design speed of **180 km/h** and is operated at a speed of 160 km/h. Currently, it is operational on **Delhi Meerut RRTS** system.

- **Green Energy**: To meet the commitment of **Net Zero** by 2070 following steps will be taken:
    1) **Viability Gap Funding (VGF)** will be provided for harnessing offshore wind energy potential for initial capacity of one giga-watt.
    2) **Coal Gasification and Liquefaction capacity** of 100 MT will be set up by 2030. This will help in reducing the import of natural gas, methanol and ammonia.
    3) **Phased Mandatory Blending** of Compressed Biogas (CBG) in Compressed Natural Gas (CNG) for transport and Piped Natural Gas (PNG) for domestic purpose will be mandated.
    4) **Financial Assistance** will be provided for procurement of biomass aggregation machinery to support collection.

- **Electric Vehicle Ecosystem**: Government will expand and strengthen the E-vehicle ecosystem by supporting manufacturing and charging infrastructure. Greater adoption of e-buses for public transport networks will be encouraged through payment security mechanism.

- **Biomanufacturing and Bio-foundary**: A new scheme of biomanufacturing and bio-foundary will be launched to promote green growth. It will provide **environment friendly alternatives such as biodegradable polymers, bioplastics, biopharmaceuticals and bio-agri-input**s. This scheme will also help in transforming today's consumptive manufacturing paradigm to the one based on regenerative principles.

- **Blue Economy 2.0**: For promoting climate resilient activities for blue economy 2.0, a scheme for restoration and adaptation measures, and coastal aquaculture and mariculture with integrated and multi-sectoral approach will be included.

    1) **Note**: Mariculture has been defined as the cultivation, management, and harvesting of marine organisms in their natural environment (including estuarine, brackish, coastal, and offshore waters) or in enclosures such as pens, tanks, or channels.

- **Comprehensive Development of Tourism Sector**:
    1) **States will be encouraged** to take up comprehensive development of iconic tourist centres, branding and marketing them at global scale. A **framework for rating of the centres** based on quality of facilities and services will be established. **Long-term interest free loans will be provided to States** for financing such development on matching basis.
    2) To address the **emerging fervour for domestic tourism**, projects for port connectivity, tourism infrastructure, and amenities will be taken up on **our islands, including Lakshadweep**.

## 8) OTHER INITIATIVES DISCUSSED IN THE BUDGET

### A) PROMOTING INVESTMENT

- During 2014-2023, FDI inflow in country was $596 billion (double of previous 10 years.
- For further promoting investments, government is negotiating **bilateral investment treaties** with foreign partners, in the spirit of '**First develop India**'.

### B) REFORM IN THE STATE FOR VIKASIT BHARAT

- A provision of 75,000 crore rupees as fifty year interest free loan is proposed this year to support those milestone-linked reforms by the state governments.

## C) DEALING WITH FAST POPULATION GROWTH AND DEMOGRAPHIC CHANGES

- Government will from a **high powered committee** for an extensive consideration of the challenges arising from fast population growth and demographic changes. The committee will be mandated to make recommendations for addressing these challenges comprehensively in relation to the goal of '**Vikasit Bharat'**.

## 3. VOTE ON ACCOUNT

Government sought a **'vote on account'** approval of the Parliament through appropriation Bill for a part of the financial year 2024-25.

**Details about Vote on Account**:

- **Article 116 of the Indian Constitution** defines Vote on Account as an advanced grant to the government from the Consolidated Fund of India to cover short-term expenditure requirement until the new financial year begins.

- A VOTE ON ACCOUNT, is the process of withdrawing money from CFI (for the period when the final appropriation bill is not passed), usually 2 months. A vote on account doesn't require debate. When elections are scheduled in the same year, government seeks a vote on account for four months. Vote on account is essentially Parliament's **interim approval of spending** by the government.
- Thus, in an election year, the government doesn't present a full-fledged budget for the whole year, instead the government prepares an interim budget or vote on account.

- **Reasons**:
    - It would be prerogative of the new government to signal its policy direction, which is often reflected in the budget.
    - There is little time to get approval from Parliament for various grants to ministries and departments, and to debate these as well as any provisions for changes in taxes.

- **Because of the above reasons**, starting 1948, when Finance Minister R K Shanmukham Chetty presented a vote on account and followed it up with Independent India's regular budget, **most governments have followed this convention**.
    - **Note**: Some governments have made policy announcements or tweaked tax rates in the vote on account.

- **Difference between Vote on Account and Interim Budget**:
    - **A vote on account** only includes government's expenditure, whereas the **interim budget** deals with both receipt and expenditure.
    - Vote on account is passed by LS without discussion. An interim budget is passed after discussion with LS.
    - Vote on account can't change the direct taxes, whereas interim budget may change the tax regime.

- Vote on account can be used by both regular and caretaker government, whereas interim budget is only used by caretaker (outgoing) government.

## 4. IMPORTANT DATA FROM BUDGET

**i. Fiscal Deficit**

**= Total Expenditure - Total Receipts other than borrowings**

= Revenue Expenditure + Capital Expenditure - (Revenue Receipt + Non-Debt Creating Capital Receipt)

- Targeted Fiscal Deficit to be below **4.5%** by 2025-26.

- **CURRENT SCENARIO**: **FISCAL DEFICIT**
  1. **FY23: (ACTUAL)**: 6.32%
  2. **FY24: (BE):** 5.9%
  3. **FY24**: (RE): 5.8%
  4. FY25: (BE): 5.1%

- **Implications of High fiscal deficit**:
  - **Inflationary Spiral**
  - **Increased national debt**: This will impact future economic growth as a large part of the expenditure will go in paying interest for the debt rather than for capital investment.
  - **Vicious Cycle of high Fiscal Deficit and Low GDP Growth**
  - **Crowding out Effect**: This is the situation when high borrowing by the government (due to high fiscal deficit) leads to reduction in availability of funds for private investors. Accordingly overall investment in the economy reduces.
  - **Erosion of government credibility** and credit ratings

  - **Therefore**, fiscal deficit shouldn't be allowed to go beyond manageable limits (about 3% of the GDP is considered manageable).
    - **High deficit** also signifies fiscal indiscipline. It points to a situation when GDP growth is low, and unemployment is high. The economy slips into stagnation and revival becomes difficult with FDI.

**ii. Revenue Deficit**: It refers to excess of revenue expenditure over revenue deficit.
- **FY24(RE): 2.8%**
- **FY25(BE): 2.0%**

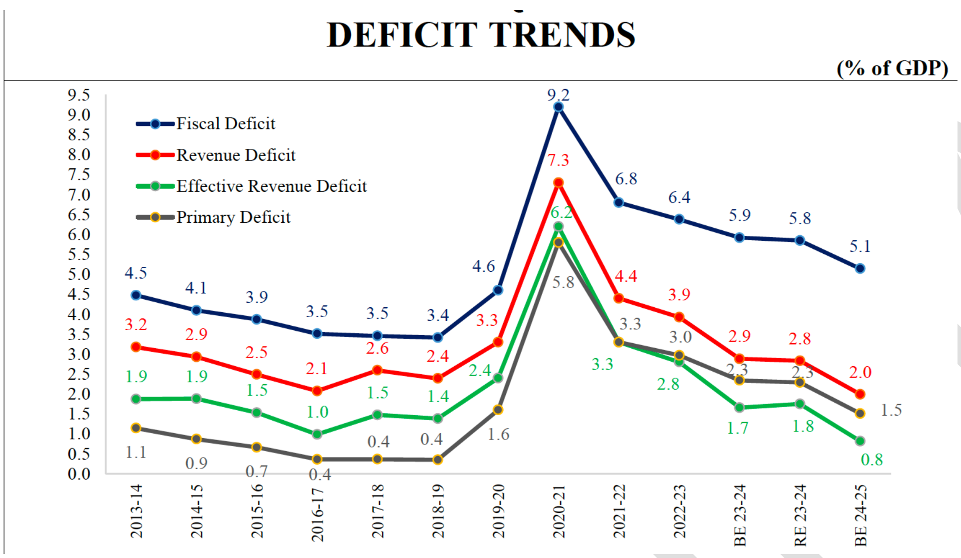
**iii. Effective Revenue Deficit** is the difference between Revenue Deficit and Grants for Creation of Capital Assets.
- **The calculation of effective revenue deficit was introduced from 2010-11 budget.**
- **FY24(RE): 1.8**
- **FY25(BE): 0.8**

**iv. Primary Deficit** is measured as Fiscal Deficit less interest payments.
- **Primary Deficit** = Fiscal Deficit - Interest Payment
- **FY24** (RE): 2.3%

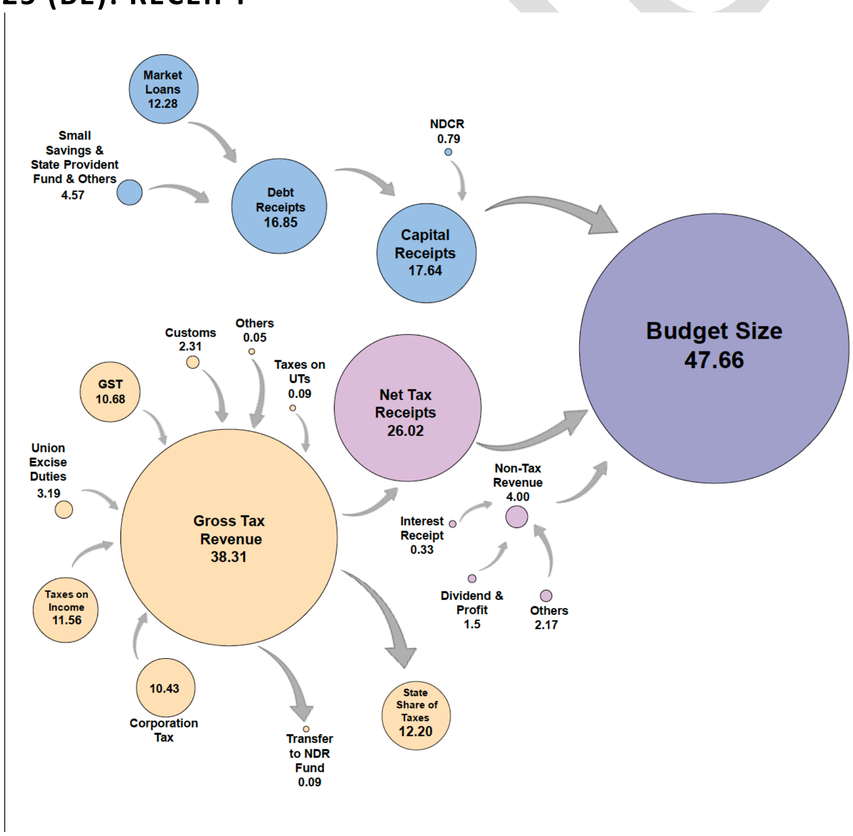
- **FY25 (BE):** 1.5%

v. **Monetized Deficit**: It goes beyond the government's budgetary operations. It represents increase in the net RBI credit to the Union government which is the sum of increase in RBI's holding of government debt and any draw down by the government of its cash balance with RBI.

vi. **Fiscal Slippage**: If the actual fiscal deficit is more than what was expected it is called fiscal slippage.

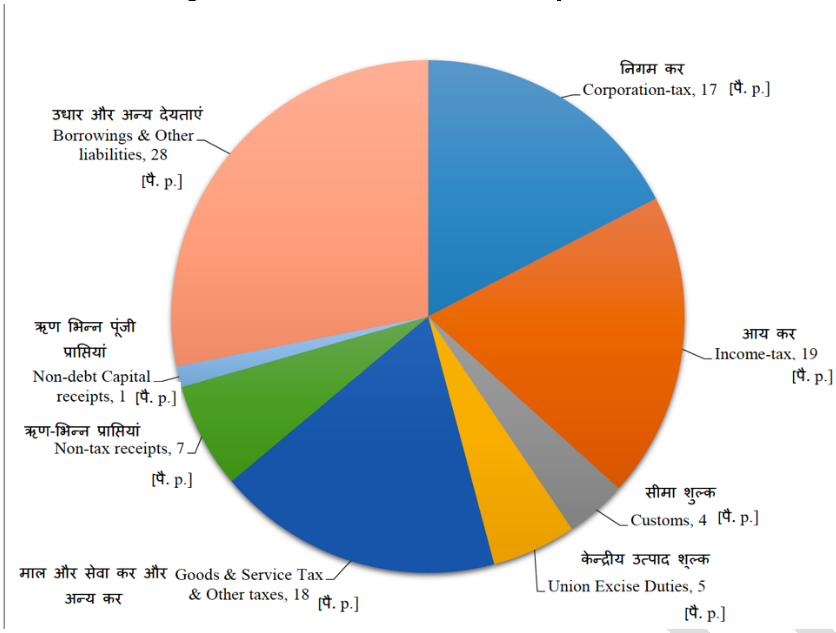



## D) FY25 (BE): RECEIPT

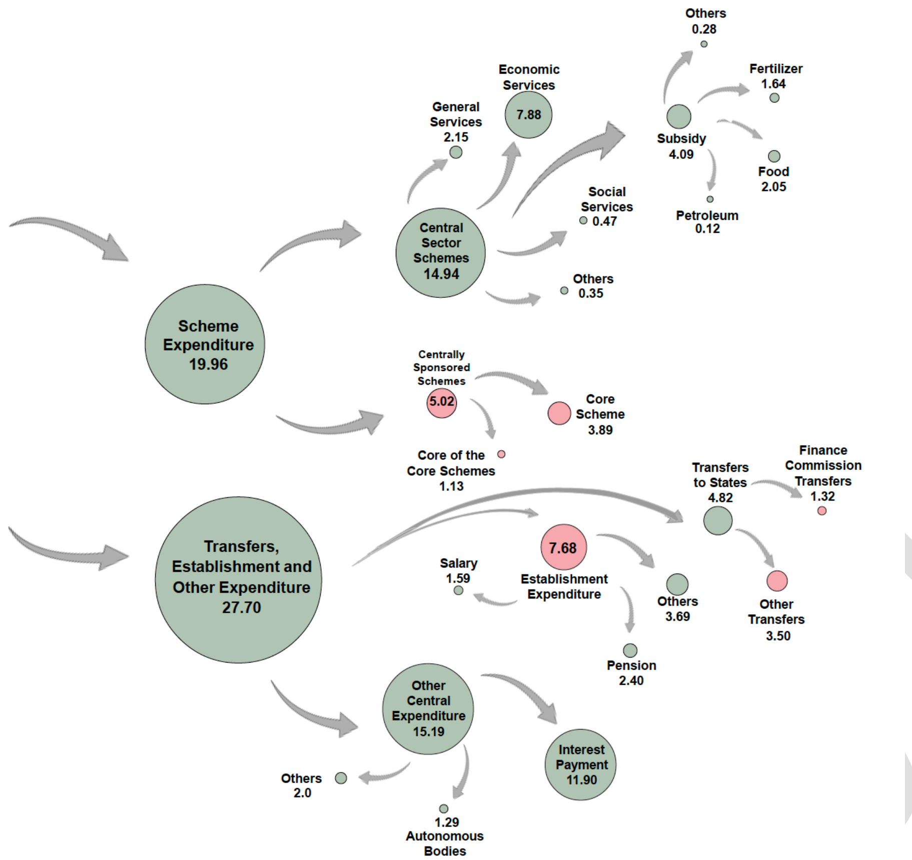


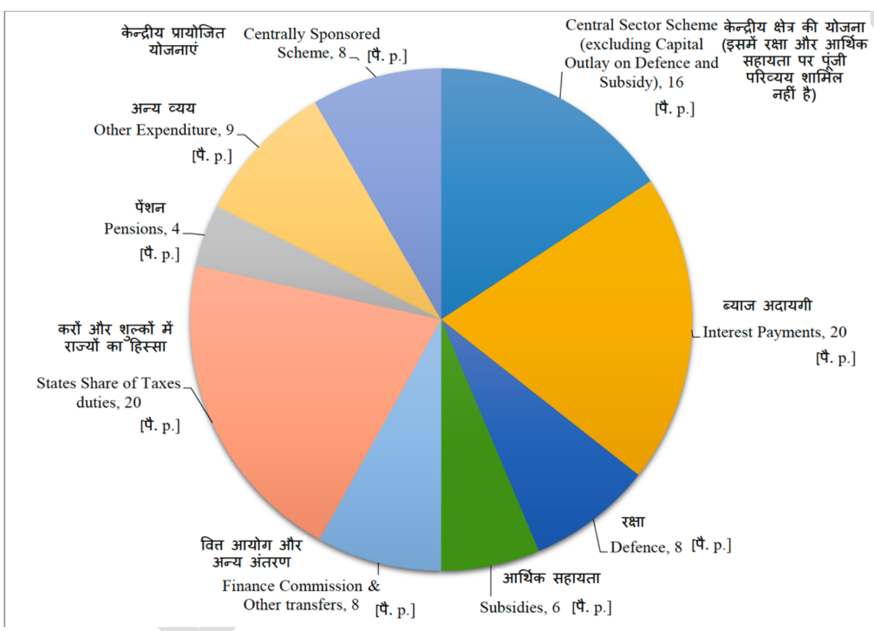
**Total Receipt** (other than borrowing) is estimated at 30.80 lakh crores. **Total Expenditure:** 47.66 lakh crores.

### Understanding different sources of Money:

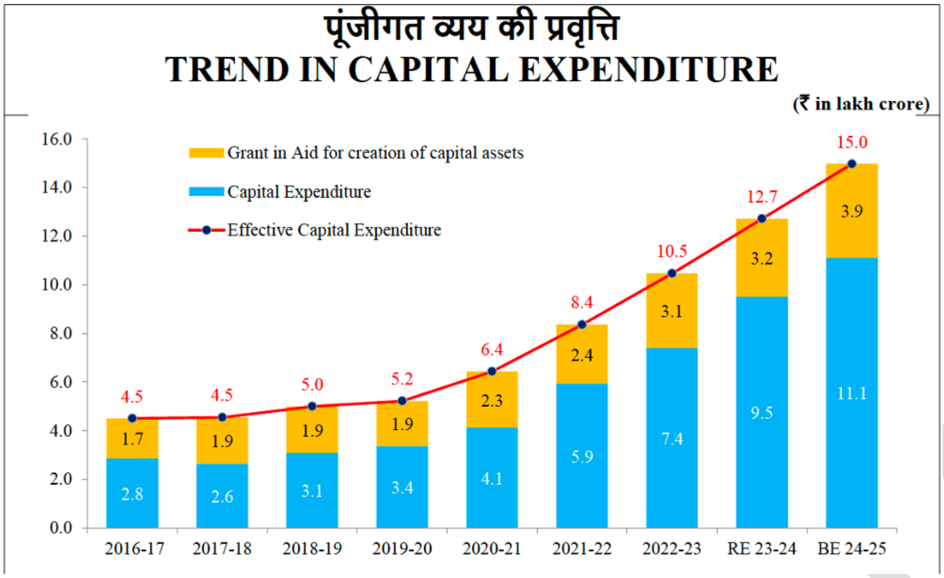



## E) EXPENDITURE:




## 5. TREND IN CAPITAL EXPENDITURE

- 


- Capital Expenditure has <u>rose substantially in last **5 years**</u>.
  - The government's <u>thrust on capital expenditure</u>, particularly in the <u>infrastructure intensive sectors</u> like roads and highways, railways, and housing and urban affairs, has <u>longer term implications for growth</u>.
  - **Advantages of Higher Capital Expenditure:**
    - Strengthens aggregate demand.
    - Crowds in private spending
    - Enhances longer term supply chain productivity.
  - Centre has also worked towards <u>enhancing capex from state governments</u> by providing <u>long-term interest free loans</u> and <u>capex-linked additional borrowings</u>.

- In the **Budget FY25**, government has announced that the <u>scheme of fifty-year interest free loan for capital expenditure to states</u> will be continued this year with total outlay of 1.3 lakh crores.

## 6. ANY CHANGES IN THE TAX REGIME IN THE INTERIM BUDGET (NO)

- **Direct Taxes**:
  - FM proposes to retain **<u>same tax rates for direct taxes</u>**
  - <u>Direct tax collection tripled, return filers increased to 2.4 times, in the last 10 years</u>
  - Government to improve tax payer services
    - Outstanding direct tax demands upto Rs 25000 pertaining to the period upto FY 2009-10 withdrawn
    - Outstanding direct tax demands upto Rs 10000 for financial years 2010-11 to 2014-15 withdrawn
    - This will benefit one crore tax payers
  - **<u>Tax benefits to Start-Ups, investments made by Sovereign wealth funds or pension fund</u>**s extended to 31.03.2025
  - **Tax exemption on certain income of IFSC units** extended by a year to 31.03.2025 from 31.03.2024

- **Indirect Taxes**

- FM proposes to **retain same tax rates for indirect taxes and import duties**
- **GST unified the highly fragmented indirect tax regime in India**
  - Average monthly gross GST collection doubled to Rs 1.66 lakh crore.
  - GST tax base has doubled
  - State SGST revenue buoyancy (including compensation released to states) increased to 1.22 in post-GST period(2017-18 to 2022-23) from 0.72 in the pre-GST period (2012-13 to 2015-16)
  - 94% of industry leaders view transition to GST as largely positive
  - GST led to supply chain optimization
  - GST reduced the compliance burden on trade and industry
  - Lower logistics cost and taxes helped reduce prices of goods and services, benefiting the consumers

## 7. FISCAL CONSOLIDATION

- **Fiscal consolidation** refers to long term permanent strategies to reduce deficit by increase the revenue and reducing expenditure.

- **Why is Fiscal Consolidation** (i.e. reduction of fiscal deficit) **needed / Negative Impacts of High Fiscal Deficit**:
  - **Inflationary Spiral**: Borrowing from RBI leads to increased money supply in economy which leads to higher inflation.
  - **Increased national debt**: This will impact future economic growth as a large part of the expenditure will go in paying interest for the debt rather than for capital investment.
  - **Vicious Cycle of high Fiscal Deficit and Low GDP Growth**
  - **Crowding out Effect**: This is the situation when high borrowing by the government (due to high fiscal deficit) leads to reduction in availability of funds for private investors. Accordingly overall investment in the economy reduces.
  - **Erosion of government credibility**: High fiscal deficit (thus high debt of government) erodes credibility of the government in domestic as well as international money market. It may also lead to reduction in the 'Credit Rating' of the government (and the economy). Lower credit rating may lead to global investors withdrawing their investment from the domestic economy.
  - **High Burden on Future Generation** as they are the ones who have to bear the brunt of higher interest rates.

- **Therefore**, fiscal deficit shouldn't be allowed to go beyond manageable limits (about 3% of the GDP is considered manageable).

- **However**, some amount of fiscal deficit may be crucial for developing economies like India.
  - Promote capital expenditure (fiscal deficit with high capex)
  - Revitalize the business cycle (Counter-cycle fiscal policies)
  - Promote crowding in investment (if better infrastructure is created -> fall in cost of production)
  - Spending has higher fiscal multipliers during slowdown.

- **Thus, fiscal deficit may be ok, if following things are kept in mind:**
  - Loan interest shouldn't become very high. Rate of growth of interest shouldn't be higher than the rate of growth of the GDP.
  - Loans shouldn't be used to fund revenue deficit. It should go on **capital expenditure**.

- **Current Situation of India**:
    - Structural reforms in FY20 (reduction in corporate taxes) and COVID-19 lockdowns in FY21 and FY22, diverted India from the track of fiscal consolidation.
    - But currently India is back on track with target of fiscal deficit to be **4.5% by FY26**. In FY 25 (BE) fiscal deficit will reduce **to 5.1% of the GDP**.

## 8. MONETIZATION OF DEFICIT

- **What is Monetization of Deficit?**
    - In simple terms, monetization of deficit means **printing more money i.e. RBI buys government securities from the primary market to fund the government's expenses**. It thus means increase in RBI credit to government.
    - **Note:** Monetization of deficit doesn't mean that government is getting free money, rather it is highly subsidized money.

- **Monetization of Deficit in India**
    - Till 1997, monetization of deficit was a **common practice in India** and RBI used to automatically monetize government's deficit through the issue of ad-hoc treasury bills.
        - But, through **agreements in 1994 and 1997 t**he funding through ad-hoc treasury bills was completely phased out. Later, **FRBM act** completely prohibited RBI from subscribing to the primary issuance of the government from 1st April 2006.
        - **Now**, RBI only buys government bonds in secondary market through open market operations. Here RBI is indirectly monetizing the deficit.
        - **Note:** FRBM Act has an escape clause which permits monetization of the deficit under special circumstances.

- **Advantages of the above decision to prohibit/phase out monetization of deficit** i.e. of prohibiting RBI from subscribing to the primary issuance of the government.
    - Since the government started borrowing in the open market, **interest rates went up** which **incentivised saving and thereby spurred investment** and growth
    - Also, the **interest rate that the government commanded** in the open market acted as a critical **market signal of fiscal sustainability**.
    - Importantly, the agreement shifted **control over money supply, and hence over inflation, from the government's fiscal policy to the RBI's monetary policy.**
    - The **India growth story** that unfolded in the years before the global financial crisis in 2008 when the economy clocked growth rates in the range of 9 per cent was at least in part a consequence of the high savings rate and low inflation which in turn were a consequence of this agreement

- **Advantages/ Need of Monetization during recessionary face**
    - **Fiscal Stimulus**
    - **Reducing cost of borrowing**

- **Limitations**

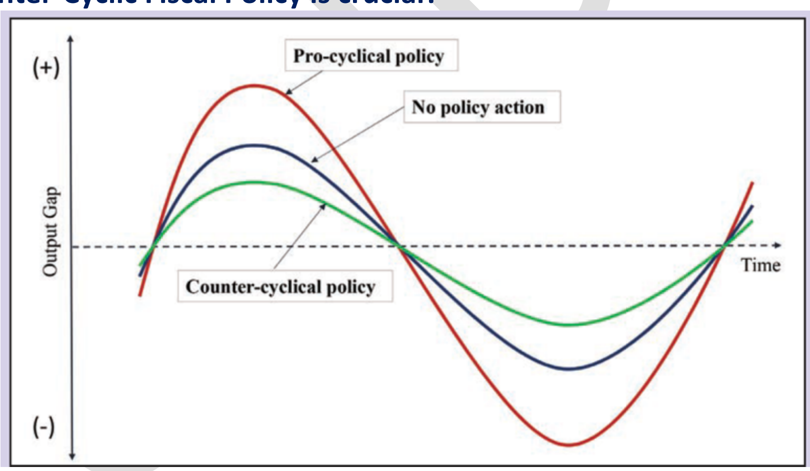
» It triggers **inflation**. In long run, the increased money supply would definitely add to the inflationary pressure.
» **Increased supply of Rupee** may also lead to **depreciation of the value of Rupee**. This makes imports expensive and exports cheap.
» It gives rise to **unproductive spending**.
» **Impacts credibility of government ->** portrays government as unable to meet its own financial needs.
» Finally, it also **erodes RBI's control over monetary policy** (and thus its independence). If RBI agrees to monetize the deficit, it is effectively agreeing to subordinate monetary policy to the financing policy of the government.

## 9. COUNTERCYCLICAL FISCAL POLICY

- **What is Countercyclical Fiscal Policy?**
  » **During slow-down or recession**, government should allow slippage of fiscal target and reduce taxes and increase expenditure. This creates more demand and brings economic upswing.
  » **During Boom Period**, government should perform fiscal discipline, increase taxes and reduce government expenses. Otherwise, the growth would not be sustainable, high inflation may result and the amplification of boom can be disastrous in long run.

- **Pro Cyclic Fiscal Policy**
  » It is opposite of counter cyclic policy. During Boom, government may further increase the expenditure to allow further growth of the boom.

- **Why counter-Cyclic Fiscal Policy is crucial?**




- At the time of recession, **private consumption (C) reduces, and private investment (I) also go down.** In such scenario, **increasing government expenditure** – both consumption and expenditure – **will support GDP and minimize the output gap**. This happens primarily through the **following mechanism**:
  i. Increased government expenditure **cushions the contraction in output by contributing to the GDP growth** and offsetting the decline in consumption and investment.
  ii. During recession **spending multiplier is higher** which leads to boosting of private investment and consumption.
  iii. Higher spending by government **compensates for 'risk aversion' by private sector** and brings back 'animal spirits'.

iv. It also **enhances expectation multiplier** by building confidence in tough times. Since government is able to exhibit their commitment to sound fiscal management, the *rational players in the economy would not expect the economy* to fluctuate as much and therefore private players will further increase the investments and reinforce this expectation multiplier.

## 10. FRBM ACT

- **Background: Need to institutionalize a new fiscal discipline framework:**
  - In 1980s, India saw a sharp deterioration in fiscal situation, which ultimately culminated in the balance of payment crisis of 1991. Within a decade of economic liberalization, the fiscal deficit and debt situation again seemed to head towards unsustainable level around 2000. At that time, a need to **institutionalize a new fiscal discipline framework**.

- **FRBM Act** was passed in 2003 and became effective from July 5, 2004. It enjoins government to conform to a pre-set fiscal target, and in the event of failure to do so, to explain the reasons for deviation.
  - The **aims** of the act are to:
    - Introduce **transparency in India's fiscal management** systems.
    - Achieve **inter-generational equity** by ensuring equitable distribution of debt over the years.
    - Ensure **long term macro-economic stability** through fiscal stability

  - **To promote transparency** in fiscal management, **section 3 of the act** provides that Union government will place **three more documents on fiscal policy** along with the budget:
    1. Macroeconomic framework Statement
    2. Medium Term Fiscal Policy Statement
    3. Fiscal Policy Strategy Statement

  - Later, through an amendment a fourth statement, **Medium Term Expenditure Framework (MTEF)** needs to be presented.

  - At the end of the second quarter, the finance minister would make a statement on the trend of fiscal indicators and corrective measures taken thereof.

  - The Act requires the central government to progressively reduce outstanding debt, revenue deficit, and fiscal deficit.
    - The central government gives three year rolling targets for these indicators when it presents the Union Budget each year.

  - It says that the **Central Government shall not borrow from the RBI** except by way of advances to meet temporary excess of cash disbursements over cash receipts.
    - Further, **RBI shall not subscribe to the primary issue of the Central government securities** from the year 2006-2007.

- **Originally, the following targets were set under the act and FRBM rules.**
  - Revenue Deficit -> 0 by 2007-08; Fiscal Deficit -> 3% by 2007-08.

- **Total liabilities of** central government should **not rise by more than 9% a year**.
- Union government will not give guarantee to loans raised by PSUs and state governments for more than **0.5%** of the GDP aggregate.

- **2008 Financial crisis and its aftermath**
  - Deadlines for the implementation of the targets in the act was initially postponed and subsequently suspended in 2009. In the next few years, the act was largely neglected.

- **NK Singh Committee to review FRBM Act (Report submitted in 2017): Key Recommendations:**
  - The committee said that **debt should be considered primary targe**t. It suggests Public Debt to GDP ratio as a medium-term anchor for fiscal policy in India.
  - It also gave targets of (Fiscal Deficit, Revenue Deficit and debt) to be achieved by 2022-23.
  - Creation of a **Fiscal Council**: It is a proposed 3 member body which will have functions like preparing multi-year fiscal forecast; preparing fiscal sustainability analysis; providing independent assessment of the central government's fiscal performance; and improving quality of data.
  - **Escape Clause and Buoyance Clause**

- **In 2018, the FRBM Act was amended to specify three conditions upon which the escape clause can be invoked**.
  - **First**, over-riding considerations of **national security, acts of war, and calamities of national proportion** and **collapse of agriculture severely affecting farm output and incomes**.
  - Second, far-reaching **structural reforms in the economy** with unanticipated fiscal implications.
  - Three, a **sharp decline in real output growth of at least 3 percentage points** below the average for the previous four quarters.
  - The FRBM amendments also mentioned that the **deviation from the stipulated fiscal deficit target must not exceed 0.5 percentage** points in a year.

  - **Note:** the term "escape clause" hasn't been used in the act. It was used by the FRBM review committee chaired by NK Singh.

  - In Budget 2020-21, the finance minister Nirmala Sitharaman has used the escape clause provided under the act to relax the fiscal deficit target. It was done on the grounds of reduction in corporate tax (structural reform)
    - The fiscal deficit of FY19-20 was 3.8% (BE was 3.3%, therefore the 0.5% relaxation)

- **Recommendations of the 15th Finance Commission**
  - The 15th Finance Commission for 2021-26 suggested a path for fiscal consolidation for the centre by reducing **fiscal deficit to 4%** of GDP and **outstanding debt liabilities** to 56.6% of the GDP by 2025-26**.**

- **Current Scenario:**
  » Due to **COVID-19 scenarios**, the **targets were against missed**. Therefore, FRBM Act should have been amended to set new targets.

- But the revisions to the FRBM Act Medium Term Fiscal Policy Statement for 2021-22 and 2022-23 omitted the rolling targets for budget deficits.
    - **Government wants a fiscal flexibility to respond to emerging contingencies** till the pandemic induced uncertainties ease.

- However, government has said that it would pursue **a broad path of fiscal consolidation** reaching the target **of 4.5% of Fiscal Deficit by 2025-26**.

**In Aug 2023**, the Finance Ministry conveyed its inability to release **Medium Term Expenditure Framework (MTEF)**, mandated by FRBM Act, 2003. It said that since the presentation of Union Budget for FY24 in Feb, there hasn't been any significant and favourable change in global headwinds and associated risks. Therefore, the **medium-term projections are not feasible**. Further, effective management of exogenous shocks and global uncertainties **necessitated additional flexibility** for the Government in terms of expenditure management and fiscal consolidation.