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Overview

1.1 At the time when this Report is being released, three quarters of 2020 have gone by and yet the COVID-19 continues to scar economies across the globe. Output retrenchments have been unprecedented as have been policy responses. Fiscal stimuli have, however, become circumscribed by the growth contractions themselves as they, in turn, have translated into sharp falls in government revenues. Meanwhile, income and health support measures have distended expenditures, substantially out of alignment with budgetary targets. Even as fiscal space gets exhausted the second wave of infection has either arrived or may be imminent in several economies, forcing lockdowns again. Overall, uncertainty remains high, and even as the quest for vaccine intensifies with no immediate relief in sight yet, the prospects for the green shoots that appeared in the third quarter of 2020 is fraught with downside risks.

1.2 The Indian economy has been hit hard, with the second largest caseload in the world and the COVID-19 curve yet to flatten on a sustained basis. With about a quarter of GDP already lost in Q1: 2020-21 (April-March) and the contraction estimated at close to 10 per cent in Q2, public finances have been subjected to severe strains. States have been at the forefront in the fight against the pandemic and the public health crisis it has spawned, besides the biggest migration in the world. The debilitating combination of compression in tax receipts and ramped-up expenditures has generated unprecedented pressures on fiscal positions at sub-national levels. These spatial and structural dimensions of the pandemic and the differential nature of

responses of sub-national policy authorities are the defining features of the evolution of state finances in India in 2020-21, and the theme of this year's Report: "COVID -19 and its Spatial Dimensions in India".

1.3 First, some states have been impacted quicker and harder than others, depending upon indigenous demographics and epidemiological features as well as availability and accessibility of health care resources. Supply chain disruptions have also been different depending on nature of businesses and other activities that various states specialise.

1.4 Second, with health care, social services and other critical aspects of containment being the responsibilities of state governments, testing, monitoring, and enforcing confinement and ensuring the continuity of provision of essential services has turned out to be a function of the digitisation base of states.

1.5 Third, a wave of de-coupling was unleashed by the pandemic across regions, states and cities with highly asymmetric effects spatially. As against the conventional push/pull factors which work towards influencing the migrants' movement, a different kind of push/pull worked during the pandemic, associated with high levels of informal unemployment. Indian states had to contend with reverse migration from abroad as well as across states, with large-scale implications for underlying activity, conditional upon the extent of dependence of states on migrants for factor income, employment and performance of micro, small and medium enterprises (MSMEs). This had implications for state finances as well.

1.6 Fourth, the pandemic produced varied direct effects on fiscal conditions across states. On the one hand, fiscal pressures were intensified by the operation of 'scissor effects'-expenditures surging and revenues collapsing. On the other hand, fiscal sustainability risks were heightened by off-budget loans and guarantees. The overall impact on state finances would be conditional upon the exposure to COVID-19, the availability of initial fiscal space and access to rainy day funds, or other reserve funds, if any. State governments' responses by delaying or cutting down expenditures, even wages and salaries, also need to be taken into account in the assessment of the pandemic's direct effects on state finances.

1.7 In line with the usual practice, Chapter II undertakes an in-depth analysis of the fiscal position of states as reflected in their budgets for 2020-21, profiled against actual outcomes for 2018-19 and revised estimates/provisional accounts for 2019-20. With COVID-19 changing the fiscal landscape for states post their budgets, a quick analysis of its likely impact on state finances for 2020-21 is also added.

1.8 Chapter III dwells on the regional dimensions of the pandemic with regard to two structural health parameters – demography and epidemiology; and healthcare infrastructure and implications for the fisc, particularly in the context

of regional dimensions of migration, employment and role of MSMEs. This chapter also examines the digitisation architecture and the opportunities going forward for investing in digitisation. The role of empowered third tier local governments in influencing the effectiveness of policy responses is also featured in this chapter. The implications of the pandemic for states' output during 2020-21 is also presented, drawing on relevant state-level data, relating to important structural parameters to emphasise successes and good practices/strategies worthy of mutual emulation and learning in the spirit of cooperative federalism.

1.9 Chapter IV concludes with setting out the way forward in rebuilding the socio-economic ethos and a robust public health and pandemic response infrastructure, boosting investment in digital infrastructure, enhancing/upgrading the urban infrastructure so as to improve the resilience of our cities to future pandemics, strengthening and empowering local governance institutions for effective interventions at the grass-root level, aligning fiscal incentives with reforms in labour laws for skilling and gainful employment of migrant workers, public-private partnership strategies in all these vistas.

1.10 Data on fiscal indicators for all states and union territories with legislatures, including on various budgetary components, are presented in appendices and statements to the Report¹.

¹ An additional Statement 36 providing information on subsidies given by states, which is not readily available from state budgets, has been added with the support of state governments.