

FOREWORD

The Reserve Bank of India brings out a publication 'State Finances: A Study of Budgets' every year that provides an analytical presentation of developments in State finances. This annual publication has been a regular feature since 1950-51. Till 1998-99, this study was a part of the RBI Monthly Bulletin. However, from 1999-2000 onwards, it is being brought out as a stand-alone publication. It provides a comprehensive picture of State finances at the consolidated level as well as at the individual State level. The analysis, orientation, coverage and format of the Report have been restructured from time to time to make it more contemporary. However, the overall purpose has been to present a detailed and critical assessment of various developments and issues having a significant bearing on the finances of State governments. Since 2005-06, the analytical content of the Study has been improved further through incorporation of a separate Section on 'theme-based' analysis covering specific aspects of State finances in the medium-term perspective. In the past five years, the special theme based chapters covered developments relating to 'Outstanding Liabilities of State Governments', 'Social Sector Expenditure', 'Fiscal Transfers to State governments', 'Revenue Receipts of State Governments: Trend and Composition' and 'Expenditure of State Governments: Trend and Composition'. This practice has been continued in the present study, which covers 'Finance Commissions in India: An Assessment' in its special theme chapter.

An analysis of State finances in this Study reveals the following:

- The developments in State finances during 2008-09 to 2009-10 reflected the impact of a moderate slowdown in the Indian economy. Despite some deterioration in State finances during 2008-09, the consolidated revenue account of States showed surplus position, *albeit* lower than that in 2007-08. However, the impact of the macroeconomic slowdown was sharper in 2009-10 (RE), when revenue deficit re-emerged at a consolidated level after a gap of three years and the gross fiscal deficit shot up above 3 per cent of GDP. With an improvement in growth prospects coupled with fiscal consolidation initiatives, both revenue deficit and gross fiscal deficit are estimated to fall in 2010-11 (BE).
- Improvement in State finances in 2010-11 (BE) is expected to be broad-based as most States are likely to improve their revenue accounts in 2010-11. States seem to have shown their inclination to revert to the path of fiscal consolidation suggested by the Thirteenth Finance Commission.
- Correction in revenue account in 2010-11 is expected to come mainly through compression in revenue expenditure (as a ratio to GDP).
- Even with slippages in 2008-09 and 2009-10 on fiscal deficit targets and consequent higher market borrowings, the overall debt position of States at 25.0 per cent of GDP in 2009-10 has remained within the recommended target of the Twelfth FC. The debt-GDP ratio is expected to further decline in 2010-11 (BE).

In addition to the presentation of developments in State finances, the Study discusses various contemporary issues such as the fiscal roadmap for States, implications of recommendations of the Thirteenth FC, the proposed introduction of GST, quality of expenditure, the cash balance position of States, disclosure and dissemination in State budgets and strengthening of State Finance Commissions.

The theme chapter on an assessment of Finance Commissions (FCs) points out that the scope of FCs has extended beyond the constitutional tasks of deciding the proportion of tax revenue to be shared with the States and determining the principles governing the grants-in-aid. The FCs have also been assigned the task of analysing and providing recommendations on several other issues impinging on State government finances. Of late, the issues relating to augmentation of State Consolidation Funds to supplement the resources of local bodies and the States' debt position have also been examined by the FCs. Based on a comparative analysis of recommended and benchmark (using the equalisation principle) transfers, it is observed that the equalisation component was the highest in the case of the Eleventh FC as the gap between recommended and benchmark transfers was minimum.

The Study has been prepared in the Fiscal Analysis Division (FAD) of the Department of Economic and Policy Research (DEPR) under the overall direction of Shri Deepak Mohanty, Executive Director and under the guidance and supervision of Smt. Balbir Kaur, Adviser, by a team comprising Shri Dhritidyuti Bose (Director), Shri Rajeev Jain (Assistant Adviser), and Shri Dirghau Keshao Raut and Shri Prabat Kumar (Research Officers). The team also received valuable guidance from Shri B.M. Misra (Adviser) in the initial phase of the Study with the work being initiated by Smt. R Kausaliya (Director). Shri P.P. Joshi, Shri B.A. Rankhambe, Shri A.K. Dharampal, Shri T.R. Muralidharan, and Smt. E. Fernandes provided support in compilation of data.

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Starting with 2001-02, the Study is also available on the RBI website (www.rbi.org.in). The earlier issues of the above Study (from 1950-51) are available in the Central Library of the Reserve Bank at Mumbai. In order to improve the quality of the Study, feedback/comments are solicited. These may be sent to Director, Fiscal Analysis Division, Department of Economic and Policy Research, Reserve Bank of India, Shahid Bhagat Singh Road, Mumbai 400 001 or through email at deprfad@rbi.org.in.

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