

FOREWORD

The Reserve Bank of India has been publishing an annual report entitled “State Finances: A Study of Budgets”, which provides an analytical discussion on fiscal position at the sub-national level and also serves as primary source of disaggregated state-wise fiscal data. The report, which was historically a part of the Reserve Bank’s Monthly Bulletin since 1950-51, is being brought out as a stand-alone publication since 1999-2000 in order to improve its visibility to the public. With a view to improve access of historical data on fiscal position of the States, the Reserve Bank brought together all the articles/studies on State Finances from 1950-51 to 2010-11 in a Compendium CD, which was released in July 2011. The analysis, orientation, coverage and format of the report have been restructured periodically to make it more contemporary. Since 2005-06, the analytical content of the report has been enhanced by incorporating in each issue, a special theme based on a specific issue of relevance. The special themes, which have been covered so far in past studies, include ‘Outstanding Liabilities of State Governments’, ‘Social Sector Expenditure’, ‘Fiscal Transfers to State governments’, ‘Revenue Receipts of State Governments: Trend and Composition’, ‘Expenditure of State Governments: Trend and Composition’ and ‘Finance Commissions in India: An Assessment’. Continuing this practice, the present report has taken up ‘Role of the Reserve Bank in State Finances’ as its special theme.

The salient features that emerge from this report are as follows:

- The consolidated fiscal position of the States, after witnessing a deterioration in 2009-10, showed a broad-based improvement in 2010-11(RE), as States benefitted from growth-induced boost in tax revenues as well as enhanced share in Central transfers in accordance with the Thirteenth Finance Commission (ThFC) recommendations. This was reflected in an improvement in the fiscal position of the States in terms of key deficit-GDP ratios. Development and social sector expenditures also increased, indicating that the States resumed fiscal consolidation efforts without undermining the quality of expenditure.
- The budgetary data for 2011-12 indicates the commitment of States to carry forward fiscal correction, as evident from the emergence of revenue surplus after a gap of two years and consequent reduction in fiscal deficit-GDP ratio. Notwithstanding the improvement in the revenue account, the budgeted fiscal deficit-GDP ratio for 2011-12 is higher than the recommended benchmark by the ThFC, mainly on account of higher capital outlay during 2011-12.
- Notwithstanding the large crisis-driven market borrowings in 2009-10, consolidated debt-GDP ratio of the States continued its declining trend, which was further reinforced in 2010-11 following the revival of the fiscal consolidation process. During 2011-12, consolidated debt-GDP ratio of the States is expected to be much below the ThFC recommended benchmarks, both for the individual years as also for the medium-term.

- The report highlights several other issues of concern such as structural factors hampering rule-based fiscal correction for few States; fiscal transparency in the context of amended FRBM Acts; classification of expenditure; central transfers and improving efficacy of centrally sponsored schemes; prudent management of external borrowing of States; mounting losses in state power utilities; and the need for greater disclosures of public private partnership at the State level for transparent assessment of liabilities of the States.

The theme chapter 'Role of the Reserve Bank in State Finances', traces the growing responsibilities of the Reserve Bank beyond its mandated roles of serving as a banker and debt manager of the State governments. Besides extending banking services to all the States, the Reserve Bank has been effectively balancing the short-term financing requirements of States consistent with its objective of maintaining monetary stability. As a debt manager, the Reserve Bank has, over the years, created the enabling conditions for States to switch over to a full-fledged auction system for market borrowings. The Reserve Bank also played a pivotal role in facilitating rule-based medium-term fiscal consolidation of the States and advising them on policy issues emerging from time to time to ensure fiscal sustainability.

The report 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); Smt. Deepa S.Raj and Shri. Neeraj Kumar (Asst. Advisers); and Shri Dirghau Keshao Raut and Shri Prabhat Kumar (Research Officers). Shri P.P. Joshi, Shri A.K. Dharampal, Shri B.A. Rankhambe and Smt. E. Fernandes provided support in the compilation of data.

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This report is also available on the RBI website (www.rbi.org.in). In order to improve the analytical or information content of the report, 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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