

## AN OVERVIEW OF GROWTH AND FISCAL DEFICIT (1991-2017)

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### Abstract:

India is the sixth-largest economy in the world in terms of nominal GDP and third largest in terms of purchasing power parity, second in population ranking, and has 130<sup>th</sup> rank in the human development index with HDI 0.609 in 2015. India having features like low poverty rate, unemployment, low capital formation, high level of the national debt, slow growth rate, high inflation, fiscal deficit, etc represents itself as a developing economy. In this paper, we try to study some macroeconomic variables and their reactions toward each other. This paper focuses on fiscal deficit and economic growth covering the period from 1990-91 to 2016-17. Fiscal deficit getting more importance in recent times, especially after the IMF's restrictions and monitoring. Almost all IMF members are adopting the fiscal consolidation methods after making it mandatory for all members by the IMF. Since 2003-04 Government of India is more proactive in adopting different policy measures to control fiscal deficit and smooth running of the Indian economy. Time series and trend analysis has been adopted to examine the objectives of the study. The results of the study show that fiscal deficit does affect economic growth but there is no direct relationship between the two variables in the context of the Indian economy, rather there are other factors too that affect the growth of the economy. In the end, we suggested that our economy must focus on HDI and other developmental activities and should try to do more and more productive expenditures which will help in increasing the per capita income and growth of the economy.

**Keywords:** Budget deficit, fiscal deficit, growth, revenue expenditure, time series analysis.

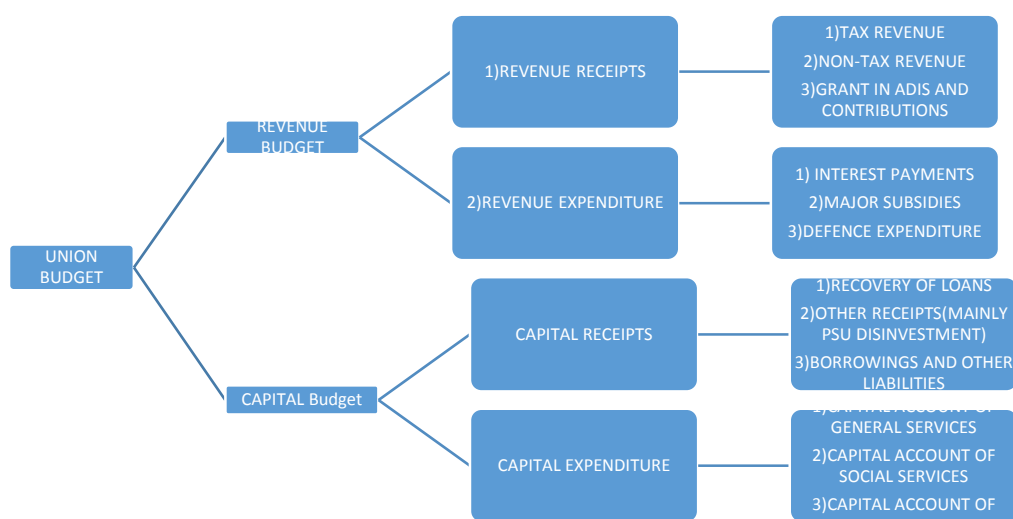
### Introduction

Indian economy is facing some critical macroeconomic problems like economic debt, the balance of Payment deficit, inflation, low investment rate, and high expenditure leads to a low rate of economic growth. The concept of fiscal deficit was missing before the 1990s in the economic survey and budgets, it was only a budget deficit and revenue deficit that were present (D'souza). Fiscal deficit became the focal point of economic policy only after the economic crisis of the early 1990s. There is a highly debatable issue in the Indian economy that is the relationship between Growth and fiscal deficit. But still, we don't have any clear conclusion regarding this relationship. We have different theoretical views in this regard. Neo-classical says fiscal deficit adversely affects economic growth whereas Keynes thought that deficit expenditure is essential to optimally utilize the existing services. While Ricardian equivalence denies the existence of a relationship between fiscal deficit and growth. Even the recent literature has different opinions on this. Different studies by the reserve bank of India show that fiscal deficit plays a major role in a persistent and high rate of inflation (RBI, 2012,

Kundrapam ET, 2010). While on the other hand central Government is of the opinion that higher government spending leads to higher economic growth.

The paper tries to show the trends of fiscal deficit and economic growth from 1990 to 2017.

Generally, people have misconceptions about the term fiscal deficit as the simple difference between Government's expenditure and revenue. To better understand the concept of fiscal deficit first we need to know the structure of the union budget. The below family chart depicts the structure of the union budget.



**Budgetary deficit** = total expenditure (revenue + capital) - total receipts (revenue + capital)

**Revenue deficit** = Total revenue expenditure – Total revenue receipts.

**Capital deficit** = Total capital expenditure – Total revenue receipts.

**Fiscal deficit** = Total expenditure – Total receipts excluding borrowings. (Net borrowings of the government).

**Primary deficit** = Fiscal Deficit-Interest payments.

When government spends more than its income, then there is a gap, and to fill that gap the Government has to borrow from different sources. Those net borrowings represent the fiscal deficit. More of the borrowings will be the fiscal deficit.

According to Dasgupta and De, 2011, "The gross fiscal deficit (GFD) of Government is the excess of its total expenditure, current, and capital, including loans net of recovery, over revenue receipts (including external grants) and non-debt capital receipts."

## Review of literature

The economists differ in their opinion regarding fiscal deficit by financing government expenditure is neutral, good or bad, specifically on growth rate and investment (Mohanthy, 2011). We can explain the effects of budgetary deficit in Ricardian, Keynesian and Neoclassical terms. According to classical economists, there is no need for Government intervention and the market plays its best role on its own. According to Keynes, more Government expenditure leads to more output and growth, contrary to this Neoclassical were with the view that fiscal policy does not have any major impact on economic growth and national output (Tajudeen Mehta Olatunji, 2012). While some have a strong opinion regarding the role of fiscal policy or Government intervention in the situation when the market fails (Abu and Abdullah, 2010). While Yuyyuri and Sessaiah (2004) have concluded in their study that there is no direct relationship between budget deficit and growth of the economy. In a study of Maharashtra state, it has been proved that budget deficit hurt the growth of state domestic product by Karnik (2002). Thus, the empirical evidence shows the mixed result of the relationship between fiscal deficit and economic growth.

## Objectives of the paper

- To study and analyze the relationship between fiscal deficit and economic growth from the 1990s till 2016-to and 2017.
- To be aware of trends of the budget deficit, economic growth, and composition of revenue expenditure.

## Methodology

Secondary data has been used for the study. The data was mainly collected from RBI reports, textbooks, economic surveys, periodicals, and the internet. The data from the 1990s have been collected for fiscal deficit and growth. The time series method has been used to show the trends.

## Fiscal deficit and Growth Trends from 1990-91 to 2002-03

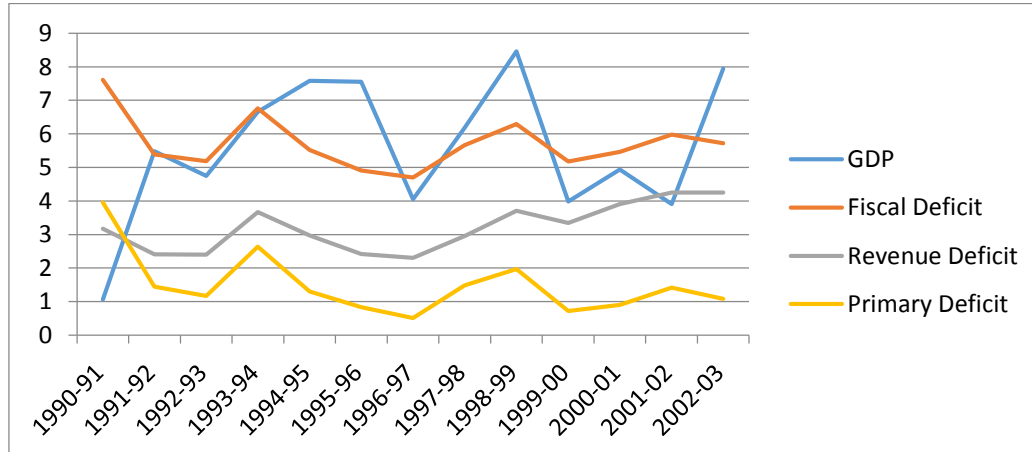
Table 1 & Figure 1 show the trends of budget deficits and economic growth from 1990-91 to 2002-03. The time series method shows that growth was spread between 1% to 12%. Fiscal deficit was 5.39 and GDP was 5.48 percent in 1991-92 and reaches its height to 6.76 and GDP to 6.66 percent in 1993-94 and again fiscal deficit goes down to 5.66 but GDP keeps itself at 6.18 percent in 1997-98. After 1999-2000 government slows down its deficit from 5.18 to 5.72 in 2002-03 and GDP from 3.98 per cent to 7.94 percent. After three new economic policies, the government liberalized its licensing and disinvestment policy because of which capital expenditure decreased and capital receipts increased. That's why there was a decline in primary deficit after 1990-91, it declines from 3.95 percent in 1990-91 to 1.08 percent in 2002-03.

**Table: 1 shows the deficit as a percentage of Gross Domestic Products (1990-2002-03)**

year	GDP	Fiscal Deficit	Revenue Deficit	Primary Deficit
1990-91	1.06	7.61	3.17	3.95
1991-92	5.48	5.39	2.41	1.44
1992-93	4.75	5.19	2.4	1.17
1993-94	6.66	6.76	3.67	2.64
1994-95	7.58	5.52	2.97	1.3
1995-96	7.55	4.91	2.42	0.83
1996-97	4.05	4.7	2.3	0.51
1997-98	6.18	5.66	2.95	1.48
1998-99	8.46	6.29	3.71	1.97
1999-00	3.98	5.18	3.34	0.72
2000-01	4.94	5.46	3.91	0.9
2001-02	3.91	5.98	4.25	1.42
2002-03	7.94	5.72	4.25	1.08

**Source:** Handbook of statistics on Indian Economy 2015-2016, RBI

**Figure 1**



**Source:** Author's Compilation based on table 1

Summarizing the fiscal deficit from 1990 till 2003; a large amount of fiscal deficit was faced by the Indian economy. The government took a large amount of borrowing and was not able to pay even for three weeks of imports which lead to the economic crisis of 1991. Economic reforms and fiscal consolidation were introduced but fiscal consolidation faltered after 1997 and the fiscal deficit started rising after 1997, so the government introduced the FRBM act, of 2003 to control the fiscal situation.

**Table: 2 shows the composition of revenue expenditure**

Year	Defense expenditure	Interest Payments	Subsidies	Other revenue expenditure	Total Revenue expenditure
1990-91	108.74	214.98	121.58	289.86	735.16
1991-92	114.42	265.96	122.53	320.01	822.92
1992-93	121.09	310.75	108.24	386.94	927.02
1993-94	149.78	367.41	116.05	448.45	1081.69
1994-95	164.26	440.60	118.54	497.72	1221.12
1995-96	188.41	500.45	126.66	583.09	1398.61
1996-97	209.97	594.78	154.99	629.59	1589.33
1997-98	261.74	656.37	185.40	699.84	1803.35
1998-99	298.61	778.82	235.93	851.25	2164.61
1999-00	352.16	902.49	244.87	991.26	2490.78
2000-01	372.38	993.14	268.38	1144.49	2778.39
2001-02	380.59	1074.60	312.10	1247.39	3014.68
2002-03	407.09	1178.04	435.33	1366.67	3387.13

**Source:** Handbook of statistics on Indian Economy 2015-2016, RBI

**Figure 2**

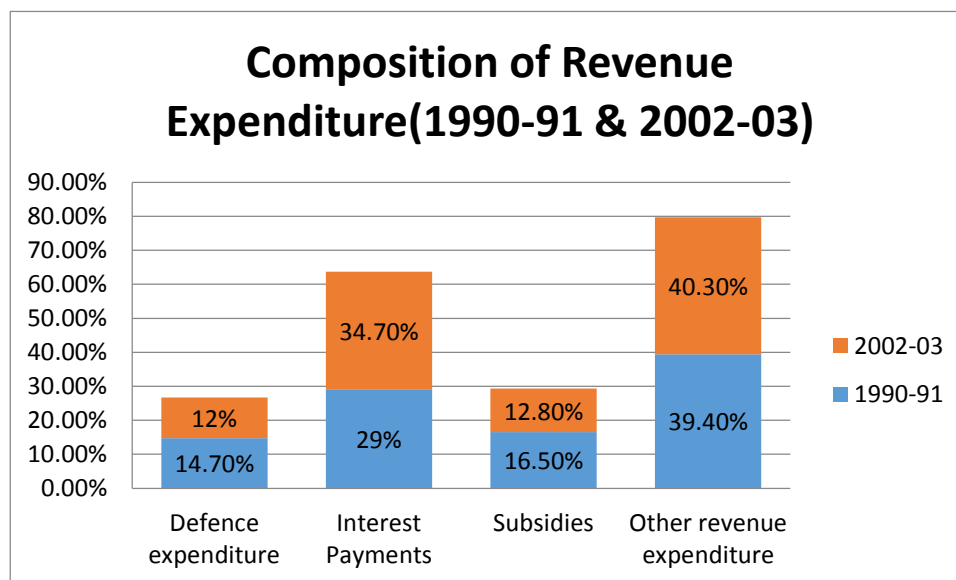


Table 2 & Figure 2 depict the trends of the composition of revenue expenditure. In 1990-91 the share of defence, interest payments, and subsidies in total revenue expenditure were 14.7, 29, and 16.50 percent while in 2002-03 it changed to 12, 34.70, and 12.80 percent. Because of the increased expenditure of the central government, its borrowings go up and

consequently the interest payments which again increases the fiscal deficit, while defence expenditure and expenditure on subsidies are reduced by 2 percent.

### Fiscal deficit and Growth Trends from (2003-04 to 2016-17)

**Table: 3 Shows the deficit as a percentage of Gross Domestic Product (2003-04 to 2016-17)**

year	GDP	Fiscal Deficit	Revenue Deficit	Primary Deficit
2003-04	7.85	4.34	3.46	-0.03
2004-05	9.29	3.88	2.42	-0.04
2005-06	9.26	3.96	2.5	0.37
2006-07	9.80	3.32	1.87	-0.18
2007-08	3.89	2.54	1.05	-0.88
2008-09	8.48	5.99	4.5	2.57
2009-10	10.26	6.46	5.23	3.17
2010-11	6.64	4.79	3.24	1.79
2011-12	5.62	5.84	4.46	2.75
2012-13	6.64	4.91	3.65	1.77
2013-14	7.24	4.43	3.15	1.13
2014-15	7.34	4.09	2.89	0.81
2015-16	7.45	3.94	2.8	0.71
2016-2017	7.49	3.5	2.3	0.27

**Source:** Handbook of statistics on Indian Economy 2015-2016, RBI

**Figure 3**

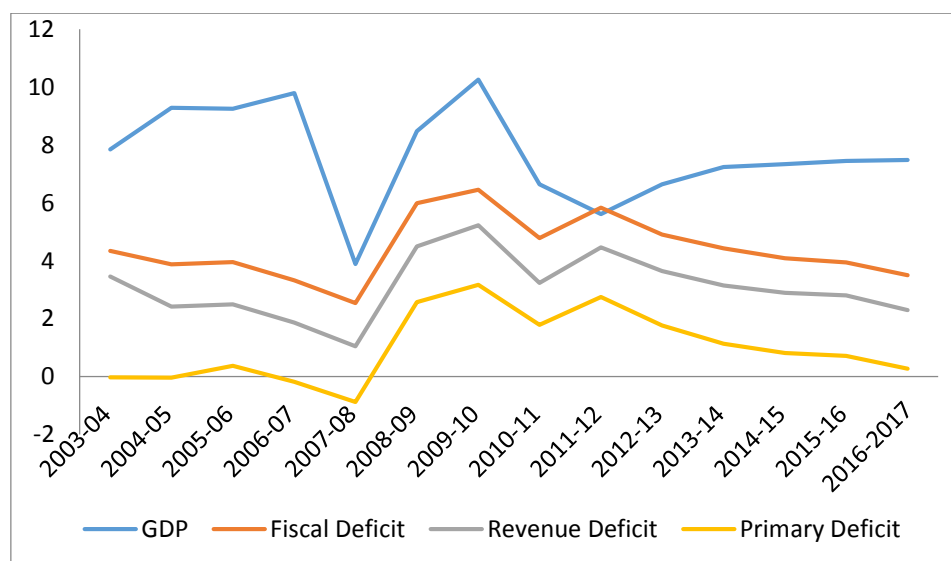


Table 3 & Figure 3 shows that in 2003-4 fiscal deficit reaches 4.34 and GDP to 7.85 percent and the fiscal deficit decreased to 4percentcent and GDP to 7.34 percent in 2014-15. The fiscal deficit continued to decrease up to 3.5 percent in 2016-17 but GDP shows a steady growth of 7.49 percent. The figure shows the trends of deficits and growth which depicts that there is no such direct relationship between the two rather there are other factors too which affect growth. But yes, a higher fiscal deficit is always dangerous for economic growth because a higher fiscal deficit means higher borrowings which result in higher interest payments.

**Table: 4 shows the composition of revenue expenditure**

Year	Defense expenditure	Interest Payments	Subsidies	Other revenue expenditure	Total Revenue expenditure
2003-04	432.03	1240.88	443.23	1504.60	3620.74
2004-05	438.62	1269.34	459.57	1675.76	3843.29
2005-06	482.11	1326.30	475.22	2110.13	4393.76
2006-07	516.82	1502.72	571.25	2555.30	5146.09
2007-08	542.19	1710.30	709.26	2982.58	5944.33
2008-09	733.05	1922.04	1297.08	3985.81	7937.98
2009-10	906.69	2130.93	1413.51	4666.96	9118.09
2010-11	920.61	2340.22	1734.20	5412.20	10407.23
2011-12	1030.11	2731.50	2179.41	5516.83	11457.85
2012-13	1112.77	3131.70	2570.79	5619.88	12435.14
2013-14	1243.74	3742.54	2546.32	6185.12	13717.72
2014-15	1404.05	4113.54	2666.92	6703.29	14887.80
2015-16	1521.39	4561.45	2438.11	6839.52	15360.47
2016-2017	1627.59	4926.70	2504.33	8251.75	17310.37

Source: Handbook of statistics on Indian Economy 2015-2016, RBI

**Figure 4**

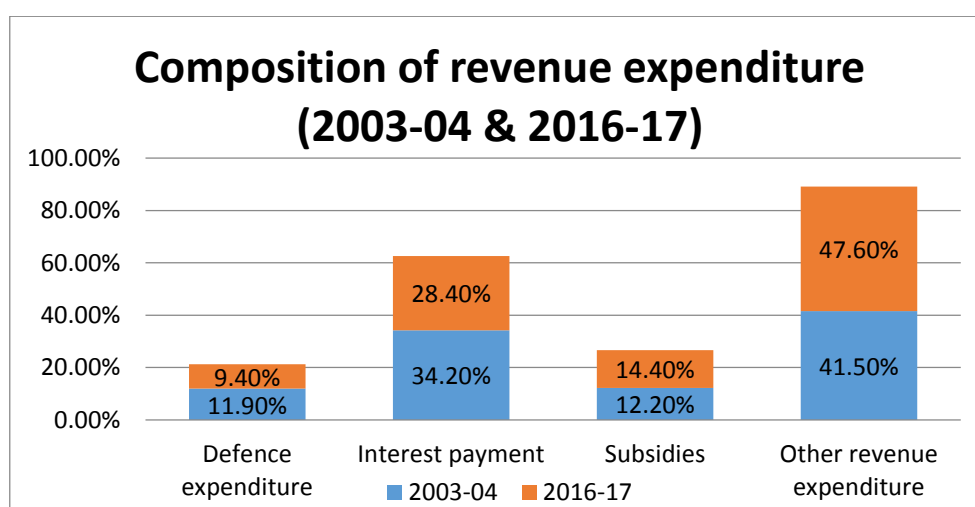


Table 4 & Figure 4 show the effect of government fiscal measures and the FRBM Act too. The objective of the central government to bring down the rate of interest payment was achieved. Interest payment decreased from 34 percent in 2003-04 to 29 percent 2007-08 and continued reducing to 28 percent in 2016-17. The increase in other revenue expenses in 2010-11 was the result of the subprime crisis which reduced the contribution of interest payments in the revenue composition which again reduced the fiscal deficit.

## Conclusion

The paper attempts to show the trends of fiscal deficit and economic growth from 1990 to 2017. It has been found that there is no such direct relationship between the two variables but the role of fiscal deficit is very important as it is directly related to government spending and borrowings. Being a developing economy, our expenditure is always greater than its revenue and to fill this gap government has to borrow, so the net borrowing of the government increase which in turn leads to a fiscal deficit. So our major focus should be on curtailment of non-productive expenditure. Government spending should be used for more capital formation and not for consumption only. The more capital formation the more will be the level of output and growth in the long term.

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