# EVALUATION OF FISCAL PACKAGE BY GOI WITH SPECIAL REFERENCE TO FEDERALISM

DR. MANASI PHADKE, 18TH JULY 2020

# CENTRE- STATE RELATIONS IN INDIA: QUICK BACKGROUND OF THE POWER BALANCE

- "Quasi- federal" Constitution of India: Powerful Centre
- Reflection of this power balance in fiscal federalism design
- Tax revenues are concentrated in the hands of the Centre (pre-GST)
- Income tax, Wealth tax, Excise, Customs
- However, expenditures are carried out by the State Governments
- 58% of total Government expenditures in India undertaken by States
- Clearly, there is a case of "transfers" from the Centre to the States
- Covid has sharpened the need for transfers!
- What is the nature of the transfers? Route of transfers? Adequacy of transfers? Symmetry in transfers?

# TRANSFERS TO THE STATE GOVERNMENTS: 2 USUAL ROUTES, 1 COVID ROUTE

Transfers from Central Government to the State Governments

Finance Commission transfers

1. Recommended by the FC
2. One-way flow
3. Untied / unconditional

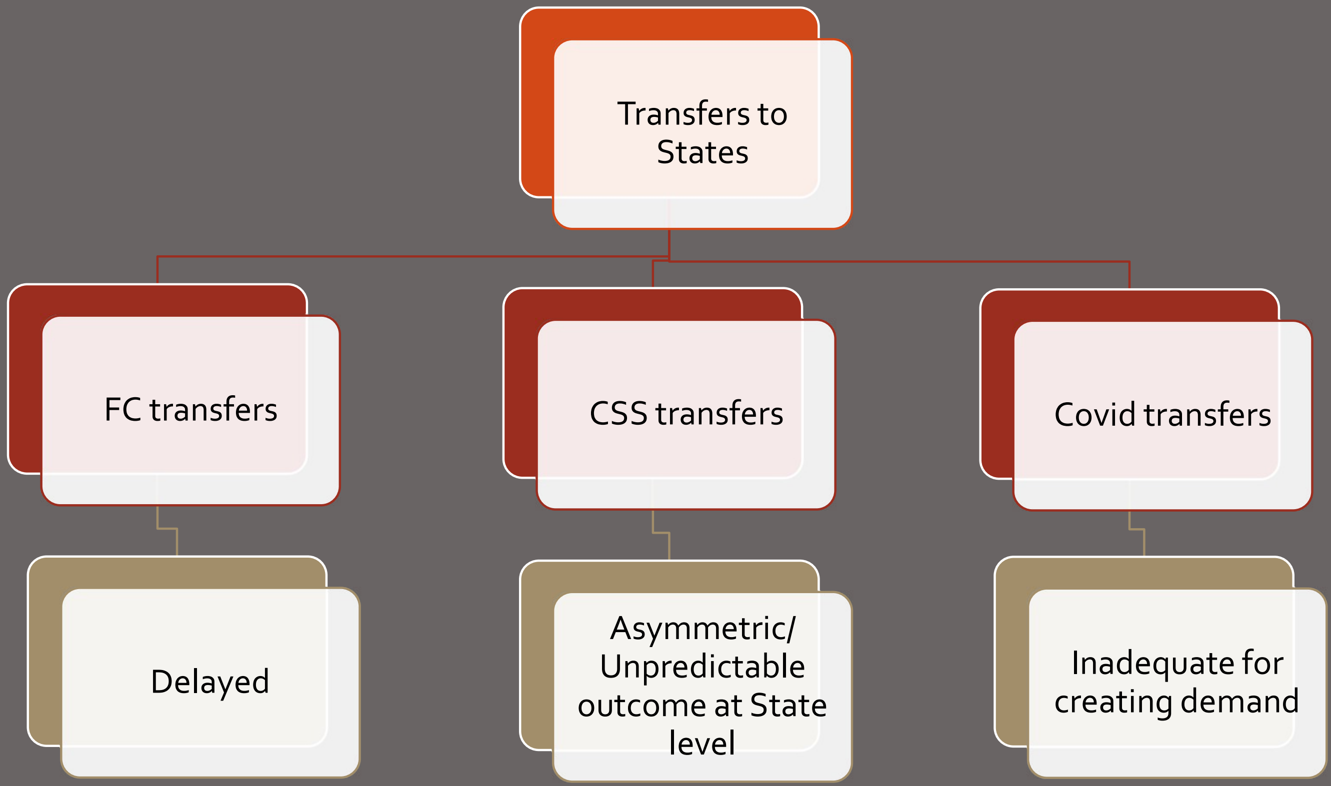
Transfers under existing Central Sector and Centrally Sponsored Schemes (CSS): MNREGA

1. Centre makes a provision for the transfers
2. Partially funded by States themselves
3. States have to “demand” the funds

Specific “Covid” transfers

These, together with some other elements form the Atmanirbhar Package (Rs.20 lakh crores)

# HOW THE TRANSFERS FARE



# PART I

# TAX TRANSFERS FROM CENTRE TO STATES

# FC TRANSFERS

- The FC defines a “divisible pool” of taxes
- 41% of the divisible pool is shared with the States
- In pre-GST era, States charged VAT, octroi, advertisement tax etc.
- These have been subsumed into GST
- So, Centre agreed to compensate States if there was a revenue shortfall after switching to GST regime for 5 years after adoption
- State tax revenue in FY2016 is calculated. 14% growth is assumed in the tax
- If actual < calculated, then compensation paid through “Compensation Cess”

सत्यमेव जयते

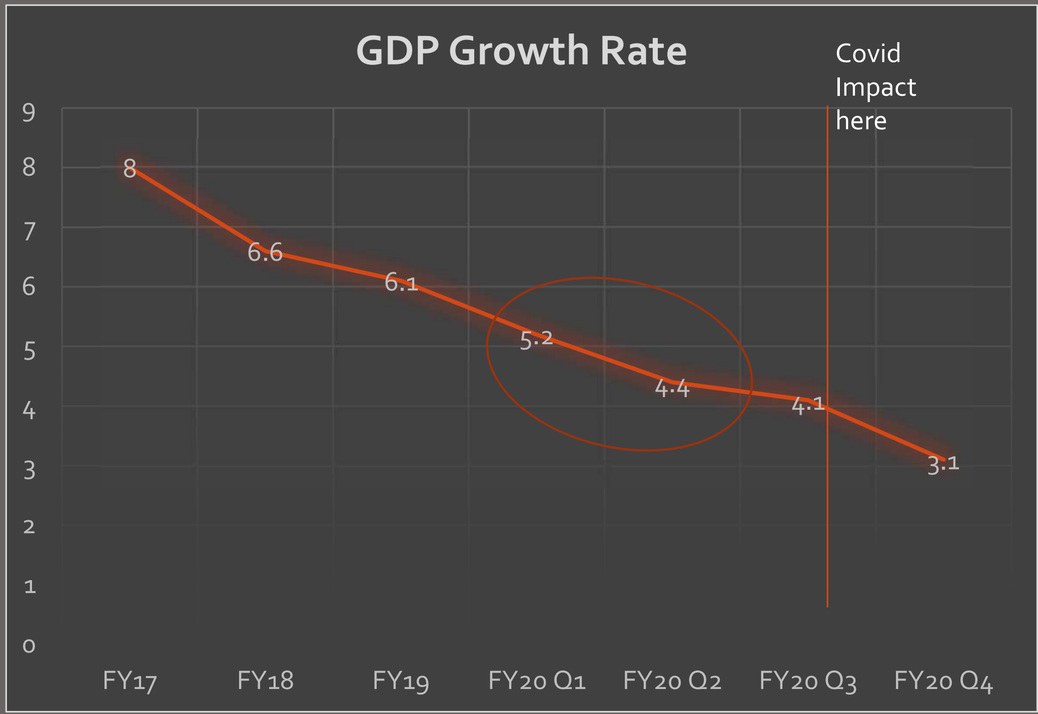
Finance Commission
Of India

# COMPENSATION CESS: HOW IT WORKS

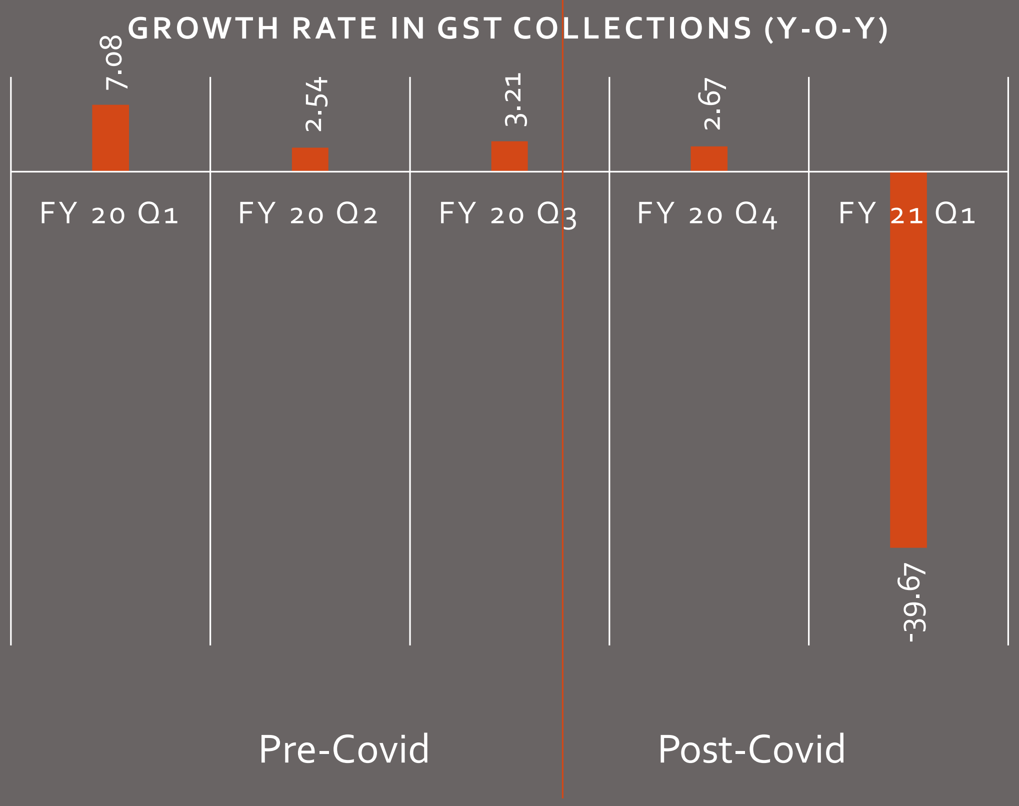
- Cess levied on luxury goods: High end SUVs have a 50% GST (28% GST tax rate +22% Cess)
- States are compensated through such cess collections
- If cess paid to States < cess collected, the remaining amount is part of divisible pool
- For FY2018 and FY2019, the compensation paid < cess collected

# FY20: SLOWDOWN OBVIOUS EVEN BEFORE COVID

- In 2017-18, ₹41,146 crore was released to States as compensation
- In 2018-19, ₹69,275 crore was released to States as compensation
- Growth slowed in Q1 and Q2 of FY20
- SGST fell drastically in the period April 2019 to Dec 2019
- States were falling short of 14% growth rate!



# GROWTH RATE (Y-O-Y) IN GST COLLECTIONS ARRANGED BY QUARTERS

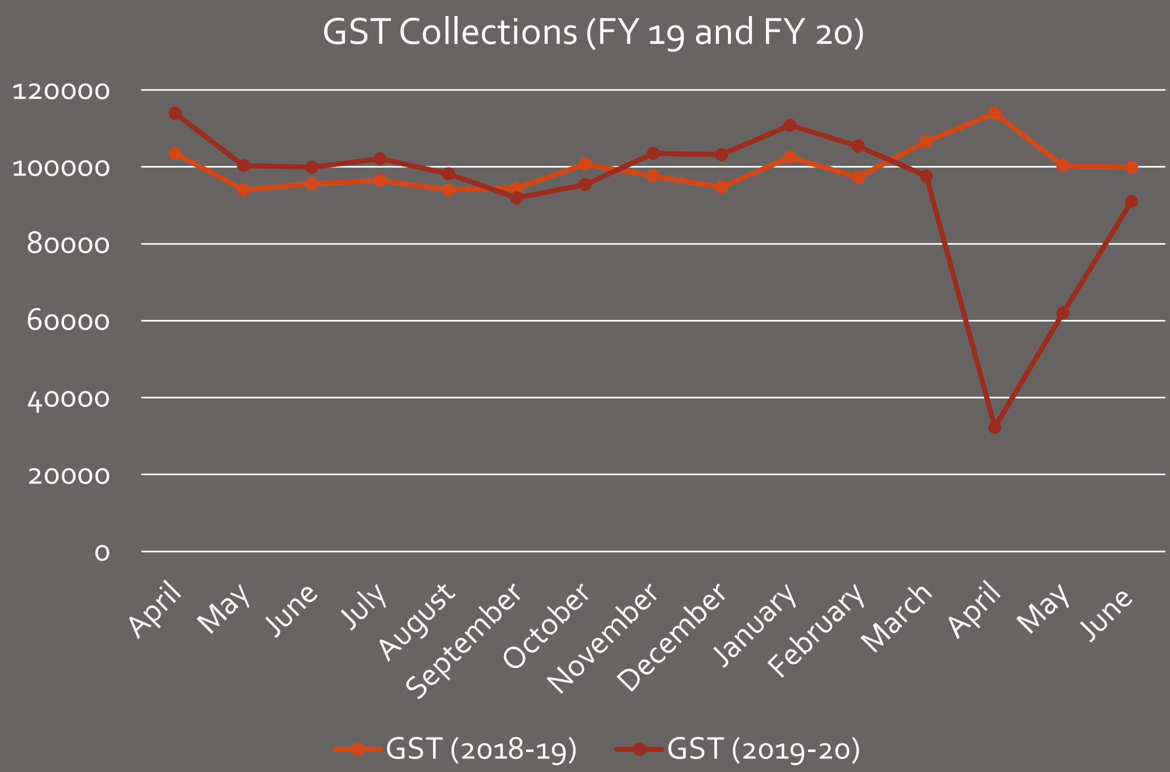



As per GST Council data, the growth rate in GST collections shows a decline across the quarters

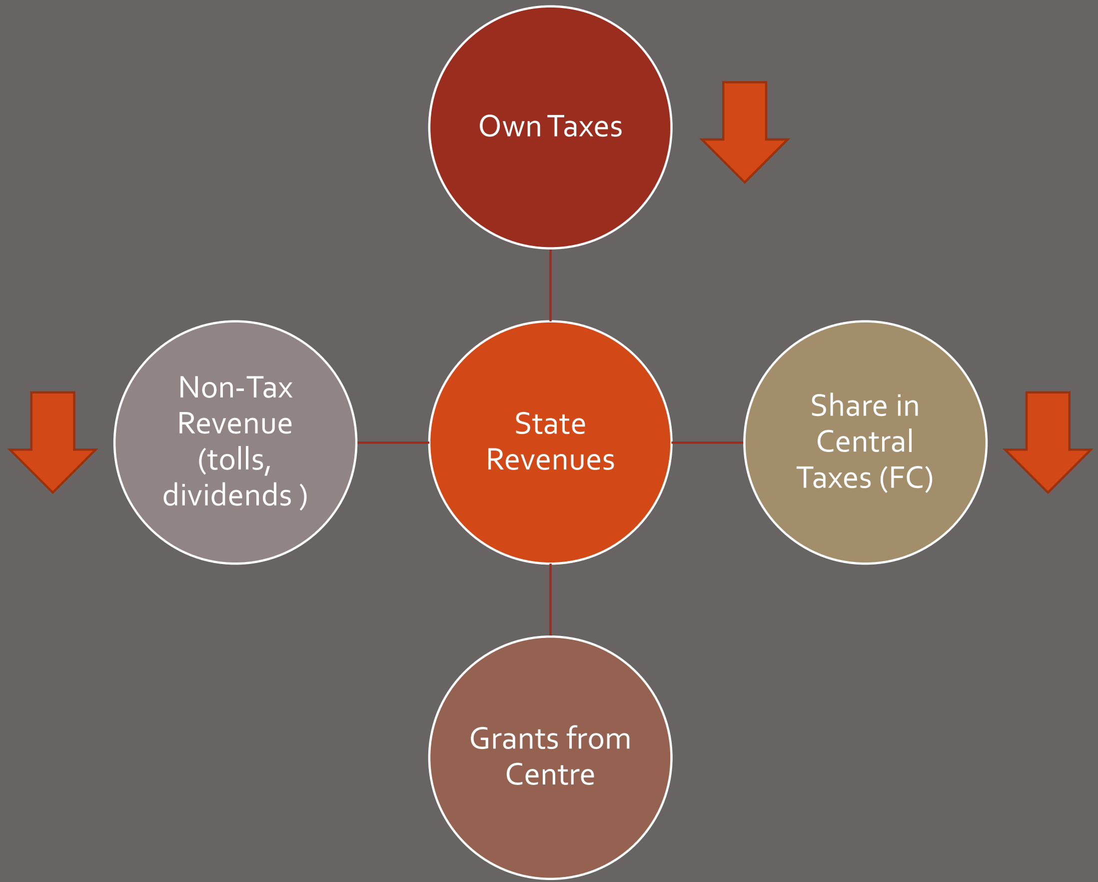
For Q1 in FY21, the GST collections have actually been only about 60% of the collections in Q1 for FY20

# GST COMPENSATION AND COVID

- As the year progressed, States started demanding compensation
- But the Centre did not have funds to compensate them!
- In December 2019, Rs. 115096 was released as compensation for April to Nov 2019
- By then, compensation released > cess collected!
- States were continuously asking for further compensation
- Covid struck in March 2020; SGST went into nosedive and State expenses increased further
- Finally, Rs.36400 for compensation from Dec 2019 to Feb 2020 was released on 4th June 2020
- With the pandemic spreading and lockdown woes, the demand for compensation has risen!



# FROM WHERE DO STATES GET REVENUES?




Each State has different weights for components of revenue

State revenues are drying up fast and furious: But the pace of drying up is different

SGST compensations are delayed: Dependence on SGST Is different for different States

In the meanwhile, expenditures on health have increased sharply

Delhi, Maharashtra, TN are epicentres

How are the States coping? Borrow!

# BORROWING LIMITS ENHANCED

- In the meanwhile, for FY21, Centre has allowed States to borrow more than what is allowed under the FRBM limits
- Normally, States are allowed to borrow upto 3% of their GSDP
- This limit has been raised to 5% of GSDP
- Additional 50 bps: Unconditional
- Additional 100 bps are conditional: 25 bps each for One Nation One Ration Card, ease of doing business, power distribution and urban local body revenues
- Additional 50 bps for meeting 3 out of 4 criteria
- Again, difficult to predict how States will respond to this helpline

# PART II + III

# SCHEME-BASED TRANSFERS FROM CENTRE TO STATES

# CENTRAL PACKAGE TIMELINE

| S. No. | Package (lakh crore) | % of GDP | Announcement date | Major Feature |
|---|---|---|---|---|
| -4 | 1.7 | 0.85 | 26th March 2020 | PM Garib Kalyan Yojana |
| -3 | 3.74 | 1.8 | 27th March 2020 | Liquidity Injection by RBI |
| -2 | 1 | 0.5 | 17th April 2020 | Liquidity Injection by RBI |
| -1 | 0.5 | 0.25 | 27th April 2020 | Special Liquidity Facility for MFs |
| Tranche 1 | 5.94 | 2.97 | 13th May 2020 | Focus MSME |
| Tranche 2 | 3.1 | 0.55 | 14th May 2020 | Free foodgrain supply to migrants |
| Tranche 3 | 1.5 | 0.75 | 15th May 2020 | Agriculture: Agri Infrastructure |
| Tranche 4 | 0.081 | 0.04 | 16th May 2020 | Viability Gap funding |
| Tranche 5 | 0.4 | 0.2 | 17th May 2020 | MNREGA |

1. Insurance scheme for health workers fighting COVID-19

2. PM Garib Kalyan Anna Yojana: 5 kgs cereal per month for 3 months, 1 kg free dal for 3 months. Covers 80 crore Individuals. Extended till Diwali (+ Rs.90000 crores)

3. Benefit to farmers: Upload PM Kisan transfers for 8.7 crore farmers

4. Cash transfers for the vulnerable:

   i. 20 crores women PMJDY account holders to get Rs.500 pm
   ii. 3 crore widows and disabled to get Rs.1000 over 3 months
   iii. Free LPG for Ujwala beneficiaries for 3 months
   iv. 24% of wages as PF payments for workers earning < Rs.15000 to be paid by Government (factories < 100 workers only)
   v. Increment in MNREGA wages from Rs.182 to Rs.202 per manday: 13.6 crore families to be covered

5. SHGs to get collateral free loans

# LIQUIDITY INJECTIONS + CREDIT SUPPORT

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CRR slashed by 100 bps to 3% (1.37 lakh crore); banks may borrow additional 1% from investments in SLR, 3 yr borrowing through targeted long-term repos

100% credit guarantee for Rs 3 lakh crore collateral-free loans to MSMEs that were doing fine earlier: To Impact 45 lakh MSMEs

'Subordinate debt scheme' worth Rs 20,000 crore and is mainly for MSMEs who are already struggling with debt : Liquidity support for those who are not very credit-worthy

# MNREGA/ PDS

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MNREGA expenditure was budgeted at Rs.61500 cr in the Budget 2020-21

Additional Rs.40000 crores have been provided

14.17 crore job cards were issued, of which 50% were Active

Most of these in UP, Bihar and WB: These are also the States that have witnessed high influx of migrants

Fortune at the bottom of the pyramid!

Differential impact: IT systems, MIS, UC culture, design issues (33% job card holders as women, admin expense < 6%)

Same issues with PDS

# WHERE IS KEYNES?

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Main issue: This is not a demand-side package at all! Relies more on the credit policy rather than fiscal Policy

Credit policies are known to “stabilize”, not to “kickstart”

GDP = C + I + G + NX

Should have been more emphasis on immediate demand boosters: Infrastructure, exports

“Rs.20 lakh crore” is misleading: Actual fiscal support in terms of “G” only Rs.2.17 lakh crores

The Union Budget size was Rs.30.42 lakh crore

Numbers needed on how the expenditure will be prioritized

# IN A NUTSHELL

- The package has been more about liquidity and not direct demand creation
- Misleading to talk of a Rs.20 lakh crore package; the fiscal support is only about Rs. 2 lakh crore
- More data needed on status of the existing budgeted expenditure – which expenditures will be carried out as per schedule, which are being deferred, which are being substituted with other expenditures within the Atmanirbhar package
- More data also needed on health expenditure
- The package will affect States differently: Their dependence on SGST, compensation and borrowing is different. Their health expenditure needs are different. The status of schemes such as MNREGA, PMGSY, PDS is different.
- Obviously, the Central package will have differential impact on States – Care needed to make sure that the poorer States do not lose out in the bargain

# SOME SUGGESTIONS FOR THE NEXT 2 QUARTERS..

- Direct spending by the Government is crucial in the months ahead of us: Creates quick and broad-based multipliers: Infrastructure, health and education, technology, exports
- Reduce the State share in funding schemes so that poorer States can also quickly avail of the scheme provisions
- Allow deviations in some of the scheme rules: 33% beneficiaries under MNREGA should be women
- It is not only about GST compensation given, it is also about the timing: Quicker cashflow management to be undertaken by the Centre
- Frontload release of grants from the Centre to the States
- Allow decentralized agencies to play a role: Kerala/ Rajasthan delegated powers to local bodies to manage contact tracing, community kitchens
- Devolution of power and funds please!

Thank you!

Dr. Manasi Phadke

manasi.phadke@gmail.com

www.manasiecon.wordpress.com