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An Analysis of Fiscal Performance and Debt Sustainability of Jharkhand Since its Inception

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Abstract

There has been a marked increase in the debt and liabilities in India at the Union as well as States level mainly on account of the fiscal deterioration observed in the late 1990s and early 2000s.Since then consistent efforts have been made to bring down the debt to GDP/GSDP ratios and ensure prudent fiscal management by the central government as well as the state governments. During the above mentioned reference period, Jharkhand was a part of Bihar whose fiscal performance indicators were consistently showing a negative sign. But after separation from Bihar in 2000, Jharkhand continued the same trend, particularly in the initial years of its inception. But, later on, the state enacted its FRBMA in 2007 and managed to reap the benefits of Debt Relief and Debt Swapping Schemes. The state followed a tight fiscal policy to reduce its Debt Burden and turned the Debt Sustainability Indicators positive. The present paper analyses the current position of the state on the path of prudent fiscal management with Debt Sustainability and Fiscal Performance as a central theme.

Keywords : Fiscal Performance, Debt Sustainability, Debt Relief, DSS, FRBM Act.

Introduction

India, including many other countries of the world, witnessed a serious deterioration in government fiscal finances in the late 1990s and early 2000s which asked for a prudent fiscal management. During the same period, it was also realized that the management of sub-national government (SNG) finance is equally important for a smooth and balanced growth of the country as it is a part of federal financing structure. Canuto and Liu (2010)[1] stated three main factors for this escalating importance of SNG finance and debt sustainability. First, in the process of decentralization, sub-national governments are increasingly entrusted with large expenditure responsibilities with limited freedom to raise revenue through user charges or market borrowings. Secondly, state governments are in immense pressure of supplying quality social and economic infrastructure elevated from rapid urbanization and catching up by the states in overall development. This has compelled the sub-national governments to undertake large borrowings. As debt servicing cost as well as benefits derived from using infrastructure is spread across the generations, the inter-generational equity issue comes into the picture. Lastly, they stated that private capital has become an important source of sub-national finances and often compete with bank loans.Hence, the central government encouraged the state governments to focus on the state finances and many states found that they are in trouble and need to address this issue.

Although, at that time, Jharkhand was not present but its ancestor Bihar was facing this problem. At the time of separation in the year 2000, with assets Jharkhand also inherited the debt burden of Rs. 5961.94 Crores[2]. Initially, the state could not manage its finance well.The 13th Finance commission (2008)[3] *cautioned that the State's outstanding debt which had more than tripled between fiscal years 2001-02 and 2006-07 would need to be controlled*.A detailed study on Jharkhand Public Financial Management and Accountability has been done by Financial Management Unit, South Asia Region for the World Bank (2007)[4].The study addressed the various issues of financial management in the state and expressed its concern about poor management and accountability. "The study's overall findings are that both fiduciary and development risks are high. The state government urgently needs to enforce the existing rules and regulations to achieve financial discipline and augment its capacity for the development and implementation of its budget proposals. It is crucial that a time bound action plan is prepared for capacity building at all levels of the government- at the legislature, at the line departments including spending units located across the state and the independent agencies involved with service delivery".A similar type of article was published by The Telegraph (2005)[5], based on the studies and conclusions of economist Dr. Ramesh Sharan. It states that- "The last few years have witnessed deterioration in the state of public finance marked by ad-hocism and non-planning and very little concern for the future".

So, it is true that some points of concern are there on the issue of fiscal management and burden of public debt. Here, this paper attempts to investigate and analyze the current position of the state on the issue of Fiscal Performance and Debt Sustainability based on the trend analysis of fiscal ratios.

Theoretical Framework for Assessing Fiscal Performance and Debt Sustainability

The issue of fiscal performance and debt sustainability are usually addressed by analyzing the variables such as growth rate of GSDP, average interest rate on public debt, growth rate of public debt, etc. A number of mathematical models, containing such variables, are available for this purpose. But here, some popular fiscal indicators have been used to assess the fiscal performance and sustainability of debt of Jharkhand. Following indicators are used for this purpose:

1. State Debt to GSDP
2. Fiscal Deficit to GSDP
3. Primary Deficit to GSDP
4. Interest Payments to Revenue Receipts
5. Interest Payments to State's Own Revenues
6. Interest Payments to Total Expenditures
7. State's Own Revenues to Revenue Receipts
8. Revenue Deficit to Gross Fiscal Deficit

Although, there is a scope for using some other measures also, but many have believed that the above ratios are an adequate representation of fiscal situation in its totality. The first ratio, the debt to GSDP, is the outcome of the behaviour of all ratios and is considered, in some sense, the ultimate measure of fiscal health. The second ratio, the fiscal deficit to GSDP, captures the overall underlying cause for the deterioration in the first. The other ratios contribute in varying degrees to the behaviour of fiscal deficit to GSDP ratio. Primary deficit is central to debt sustainability. State's own revenues (SOR) indicate the degree of State's autonomy and independence (see, kannan et al, 2004)[6] while the proportion of revenue deficit in fiscal deficit reflects the quality of fiscal deficit (see, 11th FC; 2000, ch.3)[7]

Trends of Debts and Deficits in Jharkhand

The state inherited outstanding liabilities of Rs. 5961.94 Crores from Bihar and its fiscal indicators remained at undesirable levels over the years, leading to higher borrowings. Initially its fiscal situation deteriorated very significantly. Just by 2005-06 the fiscal deficit of the state reached at 9.2% of GSDP and outstanding debt at 28.5% of GSDP. A normal look on the Audit Report (State Finances) for the year ended 31 March 2009[8], reveals the fact that the public debt of the state has shown a continuous increasing trend as it was Rs 16354.69 Crores in 2005-06, Rs 17843.34 Crores in 2006-07, Rs 19280.51 Crores in 2007-08, Rs 20823.27 Crores in 2008-09, and Rs 22645.30 Crores in 2009-10, BE. 13th Finance commission on its visit to the state cautioned that the State's outstanding debt which had more than tripled between fiscal years 2001-02 and 2006-07 would need to be controlled. All these citations raise doubts about the prudent fiscal management in Jharkhand which can be cleared only by examining the facts and analyzing the observed trends.

Fiscal Performance and Debt Sustainability Indicators of Jharkhand

The Fiscal Performance and Debt Sustainability Indicators of Jharkhand, as defined above in terms of ratios, have been computed and presented in a tabular format as follows:

Table- Fiscal Performance and Debt Sustainability Indicators of Jharkhand (in %)

Year	D/GSDP	FD/GSDP	PD/GSDP	I/RR	I/SOR	I/TE	SOR/RR	RD/FD
2001-02	21.4425	-4.331147	2.712025	12.63198	23.29611	9.437704	54.22356	20.08704
2002-03	22.6433	-5.1515	1.414175	28.74242	51.66205	20.57678	55.63545	29.28058
2003-04	23.8816	-5.13892	2.353648	20.97141	38.24088	15.11313	54.8403	-10.6279
2004-05	22.61068	-3.711737	1.801817	17.13565	33.22398	11.78074	51.57616	14.22008
2005-06	28.50539	-9.200177	6.86928	16.77188	33.92352	9.886981	49.44027	0.480992
2006-07	29.00929	-1.360305	-1.05006	16.11797	36.34639	13.70501	44.34545	-103.883
2007-08	25.74697	-2.314008	0.219869	14.61815	34.64269	11.91033	42.19693	-61.4833
2008-09	27.43238	-3.555573	1.40636	14.28818	33.11484	10.96401	43.14737	-10.5389
2009-10	26.99737	-2.992427	0.699218	15.26247	34.16288	11.93007	44.67558	0.324808
2010-11	22.51323	-1.658818	-0.09128	11.86053	26.14631	10.02672	45.36215	-39.6138
2011-12	21.31042	-1.390344	-0.18521	10.11211	22.6887	8.691968	44.56893	-71.3723
2012-13	20.77925	-2.126713	0.676381	9.65399	20.41044	7.839606	47.29928	-39.0618
2013-14*	20.57524	-2.16216	0.854266	7.365241	17.28157	6.257165	42.61904	-77.3367

Table Computed by the Author Based on Information Collected from Following Sources

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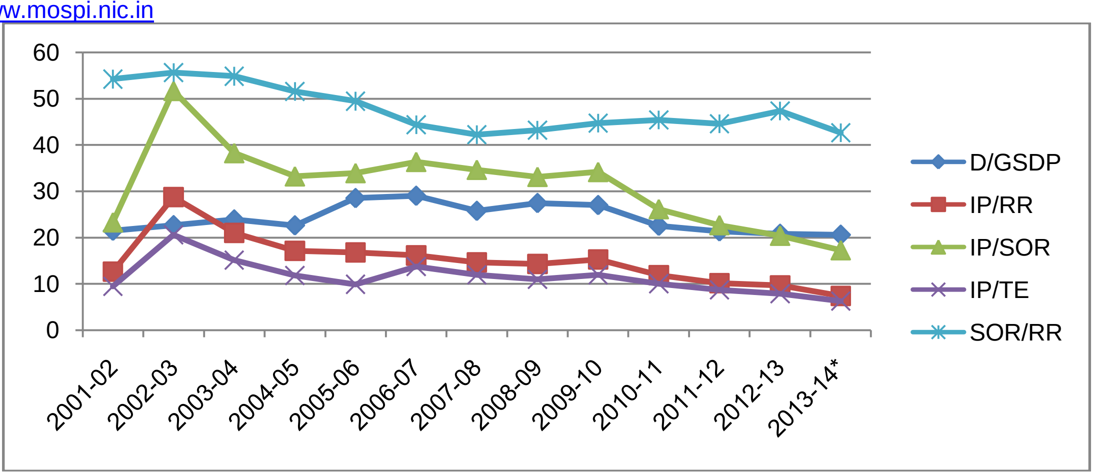
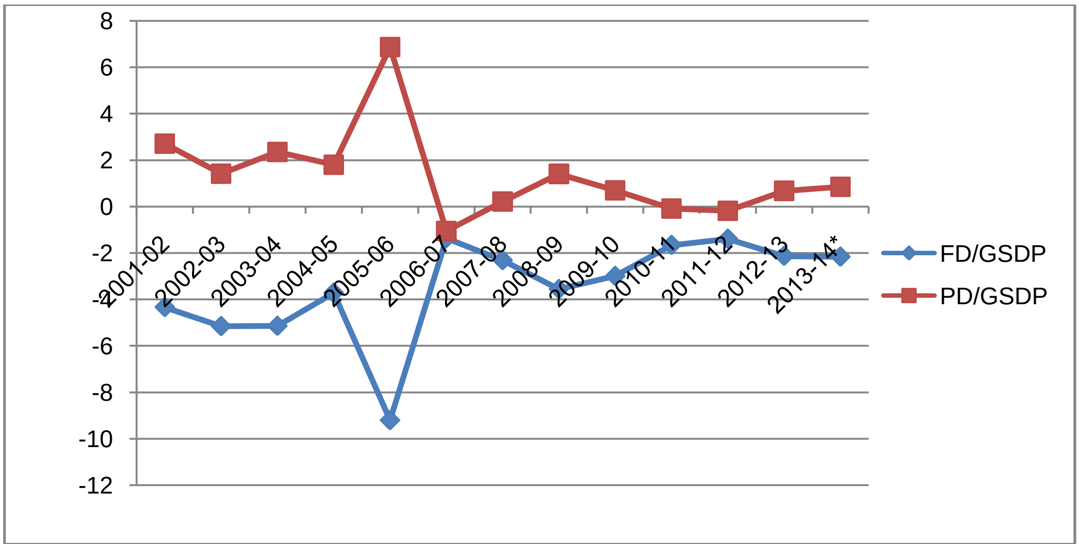
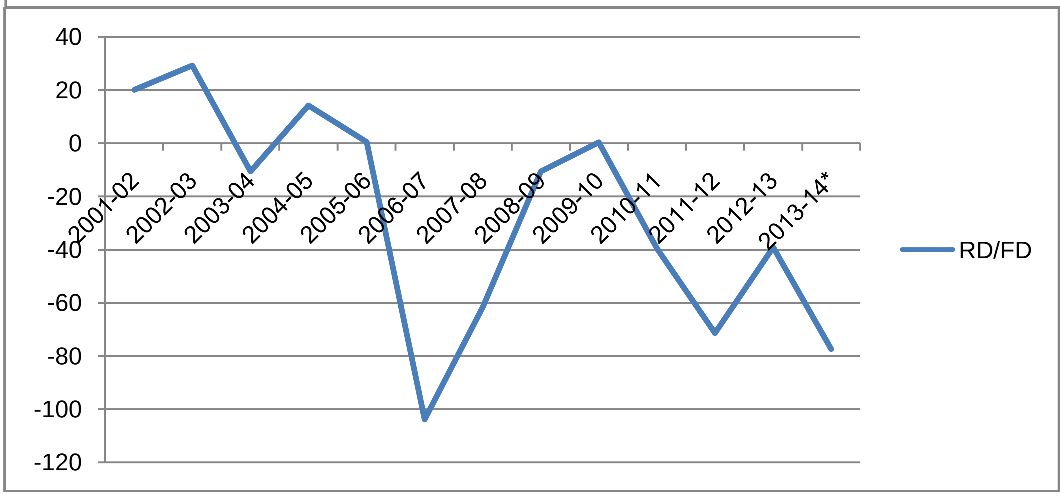
1. Figures of Debt, Deficits, Revenue collection and Interest payments have been collected from Economic Survey of Jharkhand- 2007-08, 2011-12& 2013-14, * refers BE.
2. Figures of nominal GSDP (base year 2004-05) of is based on the table published by CSO and can be downloaded from the website- www.mospi.nic.in

Analysis of Trends

A pictorial description of the above table in terms of a line chart gives us a clear idea about the overall trends of the variables and thus helps in a quick analysis.







Debt to GSDP (D/GSDP) Ratio

Debt to GSDP ratio has a declining trend, which is good and ensures that the rate of growth of GSDP has exceeded that of the debt. The current level of debt to GSDP ratio, i.e. 20% is excellent in terms of fiscal management as up to 35% is considered sustainable[9].However, this raises another question- is the government of Jharkhand lazy in undertaking developmental projects? But for now, debt sustainability will remain the core issue of focus. It is clear from the table as well as the chart that the highest ever debt to GSDP ratio, which it has faced was 29% in 2004-05. And since then the conditions have improved. One of the significant contributors to this is the *Debt Swapping Scheme (DSS) and Debt Reliefs(DR).*From 2007-10, Jharkhand enjoyed a Debt Relief of 314.88 Crores and Interest Relief of Rs. 213.64 Crores[10,] But these can only help in the short run and for sustainability structural strength is required. So, the future course of this trend can be guessed on the basis of the course of other ratios.

Fiscal Deficit to GSDP (FD/GSDP) Ratio

There is a direct relationship between Fiscal Deficit to GSDP and Debt to GSDP ratio. So, a state who is maintaining a tolerable level of Debt to GSDP ratio needs to worry if its Fiscal Deficit to GSDP ratio has a rising trend and is persistent. In Jharkhand's case the trend lack consistency, this is quite evident from the chart above. In 2005-06, it was the highest, i.e. more than 9% of GSDP and immediately in the next year, i.e. in 2006-07, it was less than 2% of GSDP and again it increased to 3.5% of GSDP in 2008-09. But after that it has shown a declining trend.

Primary Deficit to GSDP (PD/GSDP) Ratio

This is perhaps the most important ratio in terms of assessing the current and future trends in the fiscal position of a government, as it reveals the real fiscal pressure experienced by a state on account of either special factors like natural calamities or political will and processes. In general, an improvement in the PD/GSDP ratio is a precondition for improvement in FD/GSDP ratio. Here in Jharkhand, after 2005-06, there has been improvement in this ratio. However, in the early days, the movement in this ratio was inconsistent. And it was a clear indication of the need to build a robust fiscal structure which can easily release the pressure of special factors. It seems that enactment of FRBM in 2007 has proved helpful for the state in this direction.

Interest to Revenue Receipts (I/RR) Ratio

If debt obligations devour revenues, productive investments suffer. And Governments need scarce revenues for social and physical infrastructures. A rise in I/RR ratio would indicate that revenues of the State Governments are not adequate either because of its inability to raise more revenues by tax or non-tax measures or because transfers from the centre to the states are not sufficiently large. The table as well as the chart reveals that somehow Jharkhand has responded well to this problem in recent years as the ratio was having an increasing trend in early years. It was more than 28% of GSDP in 2002-03, but now it is around 7% of GSDP.

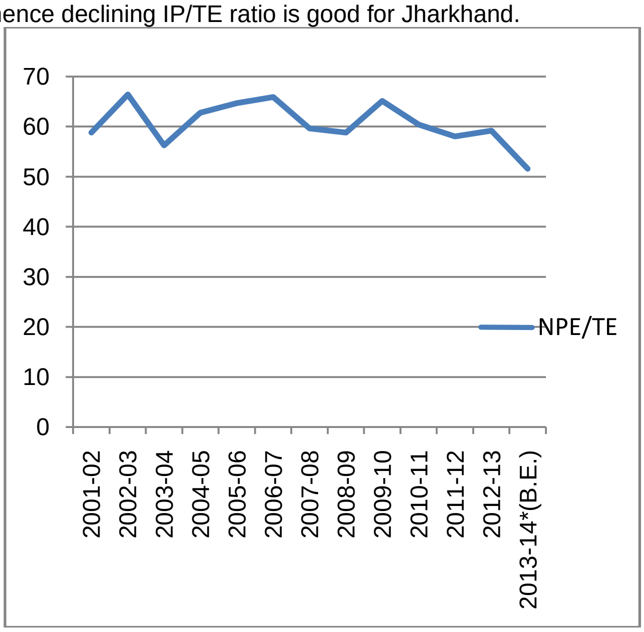
Interest to State's Own Revenues (I/SOR) Ratio

Interest as a ratio of SOR reflects the ability of a state to discharge its obligations out of its own resources. The higher this ratio, the greater would be the dependence of a state on central transfers or on borrowings to meet its other current expenditures. And so, a state with high I/SOR ratio would have a relatively high debt to GSDP ratio or would be experiencing lack of financial autonomy through substantial transfers from the centre to the state. In Jharkhand, during 2002-03, this ratio was more than 50% which was quite alarming. And the table confirms this fact that because of this the state has experienced the higher PD/GSDP, GFD/GSDP and D/GSDP ratios in the next few successive years. However, the recent good performance of the state has helped in improving all the crucial ratios. In 2013-14, it is expected to be around 17% only.

Interest to Total Expenditure (I/TT) Ratio

A rise in interest to total expenditure ratio could indicate either a relative rise in interest payments or a relative decline in total expenditure. If it is due to the first reason then it is quite detrimental to the state, but if its reason is the second logic then it could be welcomed if and only if it comes from a decline in other non-productive expenses. Similarly, if a decline in this ratio is largely due to a rise in non-productive expenditures then it would not be desirable. This ratio is having declining trends in Jharkhand; hence there is a need to examine the ratio of non-productive expenditure (NPE) to total expenditure. It is clear from the chart below that in 2002-03, it was more than 66%, but has come down to around 51% in 2013-14.However it is quite high.

But, this ratio has a declining trend and hence declining IP/TE ratio is good for Jharkhand.



State's Own Revenues to Revenue Receipts (SOR/RR) Ratio

SOR/RR ratio shows the extent to which a state enjoys financial autonomy and independence. A high SOR/RR ratio implies effective control of the state on financial resources and hence less dependence on the centre. In Jharkhand, this ratio has an overall declining trend which means that the state has problems in generating revenues from own sources. In 2002-03, it was more than 55%, but has declined continuously to reach to 42.6% in 2013-14. This is a serious issue as the state is lacking buoyancy in revenue generation. And if it is not corrected soon, then it may pose problems in achieving debt sustainability for the state in future.

Revenue Deficit to Fiscal Deficit (RD/FD) Ratio

RD/FD ratio reflects the quality of fiscal deficit in a state. If a state is running revenue deficit, it uses its costly borrowing to finance its current or consumption expenditures. And to that extent, the state is unable to use its borrowed funds for productive investment. So, the higher is the RD/FD ratio, the greater are the chances of the state getting into the debt-trap (see, 11th F.C., 2000, ch.3)[11]. In 2002-03, it was around 30% which declined to 0.32% in 2009-10 and then after it continued to have a negative trend. So, in the near future Jharkhand does not have a threat to adebt-trap.

Conclusion

The trend analysis based on Fiscal Performance and Debt Sustainability indicators have not raised any major doubts towards the current policy and practices of the state in prudent fiscal management. The enactment of FRBM Act and its successful implementation has helped the state in realizing the financial benefits provided to the state by the 13th Finance Commission. Since 2010-11, the state is maintaining a surplus in its Revenue Account and has also maintained the level of Fiscal Deficit at less than 3% of GSDP. So, it is clear that Jharkhand needs not to worry much about its fiscal performance and sustainability of debt. However, the discussions on some indicators like SOR/RR ratio and I/TE ratio have raised some issues which need to be addressed to continue the current trend of the indicators and ensure long lasting sustainability of public debt.

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