6. State of State Finances 2025 Report - Polity

Rising committed expenditure squeezing states' development spending - PRS. The 'State of State Finances 2025' report by PRS highlights that states' fiscal health is strained, with 62% of revenue consumed by committed spending (salaries, pensions, subsidies), leading to revenue deficits. States' debt remains high at 27.5% of GSDP (far above the 20% FRBM target), while revenue from GST-subsumed taxes has declined compared to the pre-GST era.

'State of State Finances 2025' Report (PRS Legislative Research)

This report, released by PRS Legislative Research, provides an in-depth analysis of the financial health of all Indian states by examining their budgets, audit reports, and economic data for the financial years (FY) 2023–24 and 2024–25.

Key Findings of the Report

1. Rising Committed Expenditure

A significant portion of state revenue is consumed by fixed, non-developmental expenses. In 2023-24, states spent 62% of their total revenue receipts on committed items, which include -

1. Salaries
2. Pensions
3. Interest payments
4. Subsidies

This high level of fixed spending leaves very little room for developmental expenditure (e.g., building schools, hospitals, or roads). The states' combined revenue deficit stood at 0.4% of GSDP (Gross State Domestic Product), implying that states were borrowing money to finance their day-to-day expenses.

2. Reduction in GST Revenues

Revenue collection from the taxes that were subsumed under the GST has declined as a percentage of the economy. This revenue fell from 6.5% of GDP in 2015-16 (pre-GST) to 5.5% in 2023-24. The states' average SGST-to-GDP ratio (State GST) during the GST years has been 2.6%. This is lower than the 2.8% average that states used to collect from equivalent taxes in the pre-GST era. The report also notes that 19% of state capital outlay (investment in infrastructure) in 2024-25 was funded by SASCI loans (Special Assistance to States for Capital Investment).

3. Widening Inequality Among States

A significant financial gap is growing between richer and poorer states. Richer States (e.g., Maharashtra, Karnataka, Tamil Nadu) -

1. They are able to raise more of their own revenue.
2. This allows them to spend more per capita on development and services.
3. This creates a "virtuous cycle" of growth, attracting more investment and generating more revenue.

Poorer States (e.g., Bihar, UP, Jharkhand) - They have limited fiscal space and are more dependent on central transfers. This limitation is widening the income and development gap compared to richer states.

4. Unconditional Cash Transfer Schemes for Women

As of 2025-26, 12 states have implemented unconditional cash transfer schemes for women. The total annual cost of these schemes is estimated at ₹1.68 lakh crore, which is 0.5% of India's GDP.

Budgetary Strain - These schemes are putting significant pressure on state budgets. In several states, such as Karnataka and Madhya Pradesh, these schemes have caused budget surpluses to turn into revenue deficits.

Economic Trade-off - While recognized as socially beneficial, there is a concern that these schemes may "crowd out" (i.e., displace funding from) essential capital expenditure and other long-term development spending.

5. Persistent High Debt Levels - States' combined debt-to-GDP ratio is at 27.5%. This level remains higher than pre-pandemic levels. Only three states—Gujarat, Maharashtra, and Odisha—are currently meeting the FRBM Act's recommended target of 20% debt-to-GSDP.

6. Rising Interest Payments - Between 2016 and 2025, states' interest payments grew at an annual rate of 10%. This growth in interest payments has outpaced the annual revenue growth of 9.2% during the same period. This mismatch is progressively tightening the fiscal space for states, as more money must be allocated just to service existing debt.

7. High Subsidy Burden - In 2023-24, subsidies accounted for 9% of states' total revenue receipts. A majority of this burden (53% of all subsidies) is spent on power subsidies. The top subsidy-spending states are identified as -

1. Punjab
2. Tamil Nadu
3. Rajasthan
4. Karnataka
5. Gujarat

8. Fiscal Deficit Trends - For the 2025-26 budget, the combined fiscal deficit of all states is budgeted at 3.2% of GSDP. If the SASCI loans from the Centre are excluded, this deficit figure drops to 2.8% of GSDP.

Fiscal Framework for States - The report's findings are contextualized by the following key financial rules

FRBM Act (2003) (Fiscal Responsibility and Budget Management) - This Act sets fiscal targets for states. States are expected to maintain their total debt below 20% of their GSDP. States are expected to keep their fiscal deficit at or below 3% of their GSDP.

Article 293 of the Constitution - This article restricts the borrowing powers of states. It specifies that a state cannot raise a new loan without the consent of the Central Government if it has any outstanding loans to the Centre.

Source - https - //www.business-standard.com/economy/news/states-committed-expenditure-squeezing-development-spending-prs-report-2025-125110501565_1.html