4.RBI Reports On State Budget- Economy

States' consolidated fiscal deficit widens 0.3 pc to 3.3 per cent in FY25- RBI.The RBI's "State Finances" report warns that while states are pushing for capital expenditure supported by central loans, their fiscal health is strained by rising deficits (3.3% of GDP) and high debt levels (29.2%). The report emphasizes that demographic shifts—ageing populations in the south versus young populations in the north—require tailored fiscal strategies, alongside an urgent need to curb non-merit subsidies and off-budget borrowings.The Reserve Bank of India (RBI) has released its annual report titled “State Finances- A Study of Budgets of 2025-26”. The report assesses the fiscal health, budgetary priorities, and challenges faced by Indian states in the upcoming fiscal year.

Findings- Fiscal Performance of States

1. Fiscal Deficit Trends

Rising Deficit- The consolidated Gross Fiscal Deficit (GFD) of states is budgeted at 3.3% of GDP for FY25.
Comparison- This marks an increase from the 3% level maintained over the previous three fiscal years, indicating a slight loosening of fiscal purse strings.

2. Capital Spending and Central Support

Capex Projection- State capital expenditure is projected to be 3.2% of GDP.
Focus Area- The spending is primarily targeted towards long-term public asset creation (infrastructure, roads, bridges).
Catalyst- A significant driver for this growth is the Centre's SASCI scheme (Scheme for Special Assistance to States for Capital Investment), which provides 50-year interest-free loans to states.

3. Debt Sustainability

Current Level- Total outstanding state liabilities stand at 29.2% of GDP.
Breach of Targets- This level significantly exceeds the fiscal prudence target of 20% recommended by the FRBM Review Committee (2017), signaling a need for caution.
4. Tax and Revenue Structure
SGST Dominance- State Goods and Services Tax (SGST) has cemented its position as the primary tax source for states.
Performance Lag- However, its growth rate has slowed, and its share in State Gross Domestic Product (SGDP) remains below pre-GST levels.
Non-Tax Revenue- There has been a steady decline in non-tax revenue sources (like user charges, dividends from PSUs) over the past decade.

Demographic Transition and Fiscal Implications

The report categorizes states based on their demographic profiles, highlighting distinct fiscal challenges for each group.

Category	Examples	Fiscal Imperatives & Challenges
Young States	Bihar, Uttar Pradesh	• Priority- Must drastically increase spending on education and skilling. • Goal- To effectively utilize their massive working-age population (Demographic Dividend).
Ageing States	Kerala, Tamil Nadu	• Pressure- Facing rising fiscal pressure due to increasing pension bills and geriatric healthcare demands. • Challenge- Balancing welfare for the elderly with development needs.
Transition States	West Bengal, Maharashtra	• Strategy- Need to adjust fiscal strategies now to ensure long-term revenue sustainability before their populations age further.

Major Concerns Highlighted

1. Expenditure Rigidity

Committed Expenditure- A large chunk of state budgets is locked into "committed expenditure"specifically salaries, pensions, and interest payments.
Impact- This leaves very little fiscal space for discretionary spending on new development projects.

2. Quality of Subsidies

Non-Merit Subsidies- The expansion of freebies and non-merit subsidies (those not delivering clear social or economic benefits) is a major concern.

Crowding Out- These expenditures risk crowding out productive investments in critical social sectors like health and education.

3. Power Sector Stress (Discoms)

Financial Losses- The persistent financial losses of state-owned Power Distribution Companies (Discoms) remain a structural weakness.

Contingent Liabilities- These losses create large contingent liabilities (potential debts) for state finances, which can crystallize suddenly.

4. Transparency Gaps

Off-Budget Borrowings- There is inconsistent disclosure regarding off-budget borrowings (loans taken by state entities but guaranteed by the state).

Hidden Risks- This practice obscures the true extent of state indebtedness and hides potential fiscal risks from public scrutiny.

Policy Recommendations

Fiscal Consolidation Roadmap- States must adopt a strict, time-bound roadmap to reduce their debt-to-GDP ratios back to sustainable levels.

Strengthening Revenue Base- It is essential to boost non-tax revenue sources (e.g., revising user charges for utilities) to reduce over-reliance on central transfers and market borrowings.

Climate-Sensitive Budgeting- States should integrate climate budgeting to prepare for and mitigate fiscal shocks caused by increasingly frequent natural disasters.

Digital PFM Systems- Implementing robust Digital Public Financial Management systems can drastically improve the efficiency of tax collection and ensure subsidies reach the intended beneficiaries (better targeting).

Source- https-//economictimes.indiatimes.com/news/economy/indicators/states-consolidated-fiscal-deficit-widens-0-3-pc-to-3-3-per-cent-in-fy25-rbi/articleshow/127307037.cms