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The union budget 2022-23: The COVID-19, fiscal challenges and normalization

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The Union Budget 2022-23 is the first post-pandemic budget that captures the full fiscal effect of it for the year 2020-21(accounts); gives a comprehensive idea about the emerging implications of the pandemic on government finances for the year 2021-22 (RE); and as the country recovers from Covid, the budget provides policy intents of the Union Government for the fiscal year 2022-23 (BE). How the unfolding global macroeconomic uncertainties will play out during the year, in terms of India's fiscal balance, is not easy to predict. There are difficult questions around macroeconomic uncertainties, be it covid, the emerging post-covid world, or the Russia-Ukraine war. However, there is optimism around key macro numbers, namely, economic growth, tax collections and fiscal consolidation. There has been significant fiscal consolidation at the Union and State levels in the year 2022-23. The post-covid stabilisation of debt and deficit in India also conforms to the global trend.

On the macroeconomic front, the economic shock in terms of GDP contraction due to the COVID-19 pandemic though reversed in the fiscal year 2020-21, a stable and sustained recovery is needed. The Medium-Term Fiscal Policy cum Fiscal Policy Strategy Statement presented as a part of the Union Budget 2022-23 mentioned that "in line with the commitment made in the budget for FY 201-22, the Government would pursue a broad path of fiscal consolidation to attain a level of fiscal deficit lower than 4.5 per cent of GDP by FY 2025-26. The Government would continue with its efforts to attain sustained, broad based economic growth, and take such measures as may be necessary to protect the lives/livelihoods of the people, while adhering to the path of fiscal rectitude."

As I write this article, questions are also being asked about the global fiscal situation and financial stability, rising inequality, federalism, the role of government, and long-run macro, fiscal and financial stability. On the role of government, quantifying the optimal size of Government during a catastrophic event like Covid-pandemic is almost an impossible task. However, there is near unanimity that it is the sovereign government's responsibility to bring the economy back on track, provide livelihood support and make necessary increases in health expenditure to contain the pandemic. As of June 5 2023, globally, there were 532 million cases of Covid infection and more than 6.3 million covid related death. In India, the number of Covid cases as of 5 June 2022 was 40.31 million and the number of people who died due to Covid was 0.53 million.

The multidimensional response to deal with the Covid by India's federal system consisted of supporting life, livelihood and economic recovery. Within the overall resource envelope, to deal with the pandemic, the combined health expenditure of the Union and State governments, as per cent of GDP increased. The health expenditure of most of the major states as per cent of GSDP increased from 0.70 per cent in 2019-20 to 0.83 per cent in 2020-21 and is expected to increase to more than 1 per cent in the year 2021-22 (RE) and 2022-23 (BE). India's federal system also delivered well on vaccination. As of 5th June, the number of people vaccinated fully was 64.7 per cent of the total population and more than 74 per cent of the population have been vaccinated with a single dose.

Due to the contraction in revenues and fiscal stimulus for the Covid response, both debt and deficits increased sharply (See Table 1). India's general government debt to GDP ratio is now hovering around 90 per cent of GDP. The debt ratio of the Union government increased from 48 per cent of GDP to 61 per cent in 2020-21. Though it is stabilizing, as evident from 2021-22 (RE) and 2022-23 (BE), the debt servicing cost is on the rise. The interest payment as per cent of GDP increased from 3.1 to 3.6 per cent, between 2012-13 and 2022-23 (BE). During the same period, as per cent of revenue expenditure, it increased from 23.8 to 29.4 per cent.

Table 1: Central Government, Deficits and Liabilities (% of GDP)

Year	Fiscal Deficit	Revenue Deficit	Primary Deficit	Total Liabilities
2011-12	5.9	4.5	2.8	51.7
2012-13	4.9	3.7	1.8	51.0
2013-14	4.5	3.2	1.1	50.5
2014-15	4.1	2.9	0.9	50.1
2015-16	3.9	2.5	0.7	50.1
2016-17	3.5	2.1	0.4	48.3
2017-18	3.5	2.6	0.4	48.2
2018-19	3.4	2.4	0.4	48.1
2019-20	4.7	3.3	1.6	50.9
2020-21	9.2	7.3	5.7	61.0
2021-22 RE	6.7	4.6	3.3	57.5
2022-23 BE	6.3	3.8	2.7	57.9

Source: Union Budget Documents (various issues)

Increasing debt servicing costs reduces the fiscal space for development spending. In this context, the large increase in debt and deficit calls for fiscal normalization. Also, the fiscal deficit for the year 2022-23 is higher than what was recommended by the Fifteenth Finance Commission after factoring in the Covid impact while assessing Union finances. However, the direction of fiscal consolidation is towards the reduction of fiscal deficit. As evident from Table 1, the estimated liability to GDP ratio of the Union government for the year 2020-21 (RE) and 2022-23 (BE) are 57.5 and 57.9 per cent respectively. This is significantly lower than the recommended debt/liability to GDP ratio (61 Percent of GDP) proposed by the Fifteenth Finance Commission. Due to higher nominal GDP growth compared to what was proposed by the Commission, the debt ratio is lower. At the same time, higher growth could not translate into a corresponding reduction in fiscal imbalance (as proposed by the Commission). The fiscal deficit to GDP ratio for the year 2022-23 (BE) is 6.3 per cent as against the 5.5 per cent proposed by the Fifteenth Finance Commission. Thus, in light of the improved GDP growth rate compared to what was assumed by the Finance Commission, better tax collection and increasing capital expenditure, there is a need to rework the path of fiscal correction to set the debt to GDP ratio to a level much lower than what was recommended by the Fifteenth Finance Commission. Probably, the Budget 2023-24 may have to focus on providing a medium-term fiscal framework with a quantified path of fiscal deficit and debt to GDP ratio. A credible MTFP for the Union Government is critical for fiscal stability and debt sustainability. An annual fixed target of deficit and debt reduction is now necessary for a steady and sustained economic recovery. Finally, the post-Covid fiscal consolidation framework is evolving globally and there is pressure on governments to calibrate the deficit and debt in a way that responds to the crisis. Though in the medium-term, the fiscal story is about supporting recovery, it is also true that there is no "one-size fits all" solution to fiscal consolidation and debt sustainability. This remains the most complex part of fiscal management when one focuses on the budget of a single year.

Reference

Department of Economic Affairs (2022): *Economic Survey 2021-22,* Ministry of Finance, Government of India, New Delhi.

As on February 4, 2023

Does not include data related to health expenditure of Odisha, Punjab, Tamil Nadu and Uttar Pradesh.

Ministry of Finance. (2022). Budget 2022-23. Government of India.