

1. Introduction: Meaning of the Government Budget

In a mixed economy like India, the government plays a significant role alongside the private sector.

The **Government Budget** is a constitutional requirement under **Article 112**, which mandates the central government to present an '**Annual Financial Statement**' before the Parliament for every financial year (running from **1 April to 31 March**).

It is a detailed statement of estimated receipts and expenditures of the government for that specific period.

The budget is more than a simple accounting document; it is a vital policy statement that reflects and shapes the country's economic life, setting priorities for growth, equity, and stability.

2. Objectives of the Government Budget

The government intervenes in the economy through the budget to achieve specific social and economic goals. These are categorised into three primary functions:

- **Allocation Function:** The government provides **public goods** (such as national defence, roads, and administration) which cannot be efficiently provided through the market mechanism. Public goods are characterised as being **non-rivalrous** (one person's use doesn't reduce availability for others) and **non-excludable** (it is impossible to bar people from using them), making it difficult to charge fees. The government ensures their provision through **public provision** (financing via the budget) or **public production** (producing them directly).
- **Redistribution Function:** The government aims to bring about a 'fair' distribution of income by affecting the **Personal Disposable Income** of households. It does this by

collecting taxes from the wealthy and providing **transfer payments** (like pensions and scholarships) or subsidies to the poor.

- **Stabilisation Function:** To correct fluctuations in income and employment, the government uses fiscal policy to manage **Aggregate Demand**. During periods of low demand and unemployment, the government may increase its own spending to stimulate the economy; conversely, it may reduce spending or increase taxes to curb inflation when demand exceeds available output.

3. Components and Classification of the Budget

The budget is divided into two main accounts to distinguish between current operations and those affecting assets and liabilities:

1. **Revenue Budget:** Deals with the current financial year's receipts and expenditures.
2. **Capital Budget:** Concerns the assets and liabilities of the government.

4. Classification of Government Receipts

Receipts are the money flowing into the government treasury and are classified based on whether they create a liability or reduce assets.

A. Revenue Receipts

These are receipts that **do not lead to a claim** on the government (non-redeemable). They are subdivided into:

- **Tax Revenue:** The most important component, divided into:
 - **Direct Taxes:** Levied directly on the income of individuals (**Personal**

Income Tax) and firms (**Corporation Tax**).

- **Indirect Taxes:** Levied on goods and services, such as customs duties and the **Goods and Services Tax (GST)**. GST is a single, destination-based consumption tax that replaced a multitude of older taxes.

- **Non-Tax Revenue:** Includes interest receipts on loans given by the government, dividends and profits from government investments (like PSUs), fees, and cash grants-in-aid from foreign countries.



B. Capital Receipts

These receipts either **create a liability** or **reduce financial assets**. They include:

- **Borrowings:** Money raised from the public (small savings), commercial banks (via SLR), the RBI, or foreign bodies. These are **debt-creating** capital receipts.
- **Recovery of Loans:** Money returned to the central government from states or other parties.

- **Disinvestment:** Proceeds from the sale of government assets, such as shares in Public Sector Undertakings (PSUs). These are **non-debt creating** capital receipts.

5. Classification of Government Expenditure

Expenditure is categorised by its impact on assets and the nature of the government's service.

A. Revenue Expenditure

This is expenditure incurred for purposes **other than the creation of physical or financial assets**. It covers:

- Normal functioning of government departments and services.
- **Interest payments** on government debt (the largest component of non-plan revenue expenditure).
- **Subsidies** on food, fertilisers, and exports to increase welfare.
- Grants given to state governments.
- Salaries, pensions, and defence services.

B. Capital Expenditure

These expenditures result in the **creation of physical or financial assets** or the **reduction of financial liabilities**. Examples include:

- Acquisition of land, buildings, machinery, and equipment.
- Investment in shares.

- Loans and advances granted by the central government to state governments and PSUs.

*Note: Traditionally, expenditures were also classified as **Plan** (related to five-year plans) and **Non-Plan** (general and committed services), though this distinction has been debated regarding its impact on maintenance and resource allocation.*



6. Balanced, Surplus, and Deficit Budgets

The relationship between total revenue and total expenditure defines the budget's state:

- **Balanced Budget:** When the government spends an amount exactly equal to the revenue it collects.
- **Surplus Budget:** When tax and other revenue collections exceed required expenditure.
- **Deficit Budget:** When government expenditure exceeds its revenue.

7. Measures of Government Deficit

Economists use various measures to capture the nature of the government's financial imbalance:

I. Revenue Deficit

- **Definition:** The excess of the government's **revenue expenditure** over **revenue receipts**.
- **Formula:** $Revenue\ Deficit = Revenue\ Expenditure - Revenue\ Receipts$.
- **Implication:** It signifies that the government is **dissaving**—using the savings of other sectors to finance its own consumption expenditure. This leads to a build-up of debt and interest liabilities, often forcing the government to cut productive capital or welfare spending.

II. Fiscal Deficit

- **Definition:** The difference between total expenditure and total receipts, **excluding borrowings**. It is the key indicator of the total borrowing requirements of the government from all sources.
- **Formula:** $Gross\ Fiscal\ Deficit = Total\ Expenditure - (Revenue\ Receipts + Non-debt\ Creating\ Capital\ Receipts)$.
- **Financing:** It must be met through net domestic borrowing, borrowing from the RBI, or borrowing from abroad.
- **Implication:** A large fiscal deficit indicates heavy reliance on debt to meet expenses. If the revenue deficit forms a large share of the fiscal deficit, it suggests that borrowed funds

are being used for consumption rather than investment.

III. Primary Deficit

- **Definition:** Measures the borrowing requirements of the government, **excluding interest payments** on accumulated debt. It focuses on present fiscal imbalances.
- **Formula:** *Gross Primary Deficit = Gross Fiscal Deficit – Net Interest Liabilities.*
- **Implication:** It helps policy-makers understand how much of the current year's deficit is due to current policy rather than past obligations.

8. Key Policy Frameworks

- **Fiscal Responsibility and Budget Management Act, 2003 (FRBMA):** This legislation was enacted to institutionalise fiscal prudence and ensure long-term stability. It mandated reducing the fiscal deficit to **3% of GDP** and eliminating the revenue deficit, though targets are occasionally adjusted for national security or natural calamities.
- **Debt as a Burden:** Government debt is considered a burden if it reduces the savings available to the private sector, thereby hindering capital formation. However, if the government invests in infrastructure that generates returns higher than the interest rate, the debt may not be burdensome as it is paid off by future output growth.
- **Ricardian Equivalence:** A theory suggesting that forward-looking consumers anticipate future tax increases to pay off current government debt and may reduce their current consumption accordingly, matching the effect of an immediate tax increase.

9. Quick Summary Table: Budget Receipts and Expenditure

Category	Type	Definition	Key Examples
Receipts	Revenue	No liability created; non-redeemable.	Income Tax, GST, Interest Receipts.
	Capital	Creates liability or reduces assets.	Market Loans, PSU Disinvestment.
Expenditure	Revenue	No asset creation; operational.	Interest Payments, Subsidies, Salaries.
	Capital	Asset creation or liability reduction.	Building Roads, Buying Machinery.

