P£ÁðIP ¸PÁðg

Government of Karnataka

**DyðP E¯ÁS**

Finance Department

# gÁdå º tPÁ¹£

# ªÄzåªÁ¶ðP ¥j²Ã®£

# 2017-18

# MID YEAR REVIEW OF STATE FINANCES 2017-18

(2017£Ä ವಷðz £ªA§gï wAU½£° «zÁ£ ªÄAq®z ªÄÄAz ªÄAr¹zAv)

(As Presented to the State Legislature in November 2017)

# MID YEAR REVIEW

# OF

# STATE FINANCES

# 2017-18

**Government of Karnataka**

**Finance Department**

# MID YEAR REVIEW
# OF
# STATE FINANCES
# 2017-18

Outcome of the review of the trends in receipts and expenditure in relation to the budget at the end of the second quarter of the financial year 2017-18

and

Remedial measures proposed to be taken to ensure adherence to the fiscal parameters stipulated in the Karnataka Fiscal Responsibility Act, 2002

***(Presented as per the Section 6(2A) of the Karnataka Fiscal Responsibility Act, 2002)***

## TABLE OF CONTENTS


| Chapter No | Chapters | Page No |
|---|---|---|
| 1 | Introduction | 1 |
| 2 | Overview of Economy and Trends in State Government Finances | 2-5 |
| 3 | Budget Estimates 2017-18 | 6-7 |
| 4 | Review of Trends in Receipts and Expenditures | 8-16 |
| 5 | Fiscal & Debt Management | 17-18 |
| 6 | Deficit Management | 19-22 |
| 7 | Supplementary Estimates | 23 |
| 8 | Mid Year Assessment of MTFP 17-21 benchmarks | 24-25 |
| 9 | FMRC Recommendations and the Road Ahead | 26-28 |

# 1

## Introduction

1. The Mid Year Review (MYR) is presented to the State Legislature as required under Section 6 (2A) of the Karnataka Fiscal Responsibility Act (KFRA), 2002; wherein it is mandated that the Minister in charge of Finance shall review every half year, the trends in receipt and expenditure in relation to the Budget and the remedial measures to be taken to achieve budget targets as recommended by the Fiscal Management Review Committee (FMRC) headed by the Chief Secretary to Government. The outcome of this review i.e. the MYR is to be placed before the Legislature along with measures proposed to ensure adherence to the parameters stipulated in KFRA.

2. The MYR would amongst others include the following:

   - any deviation or likely deviation in meeting the obligations cast on the State Government under KFRA;

   - whether such deviation is substantial and relates to the actual or the potential budgetary outcomes and how much of the deviation can be attributed to general economic environment and to policy changes by the State Government; and

   - Remedial measures the State Government proposes to take.

## 2

## Overview of the Economy

### National Economic Scenario[1,2,3]

3. The growth rate of GDP in Q1 of 2017-18 was 5.7 per cent as compared to 7.9 per cent in the corresponding period of previous year. The growth in Gross Value Added (GVA) at constant (2011-12) basic prices in Q1 of 2017-18 was 5.6 per cent, as compared to the growth rate of 7.6 per cent in Q1 of 2016-17. Agriculture, industry and services sectors grew at the rate of 2.3 per cent, 1.6 per cent and 8.7 per cent respectively in Q1 of 2017-18. The WPI headline inflation declined to 2.6 per cent in September 2017 from 3.2 per cent in August 2017. CPI inflation remained unchanged at 3.3 per cent in September 2017 as in August 2017. On the revenue front, Gross tax revenue in April-August 2017 recorded a growth of 20 per cent over April-August 2016. Tax revenue (net to Centre) increased by 21.5 per cent during April-August 2017. The budget estimate of the fiscal deficit for 2017-18 has been set at 3.2 per cent of GDP, as compared to 3.5 per cent in 2016-17 (RE).

4. The bimonthly policy of RBI states that inflation is expected to pick up from its recent lows as favourable base effects reverse. Economic activity is expected to recover, with an improvement in the services sector, even with a slowdown in the investment activity. The slowdown of economic activity that became pronounced in the second half of 2016-17 appears to have extended into the first half of 2017-18. However, some improvement in services may counterbalance the persisting weakness in industrial production. The foreign exchange reserves were around 11.5 months of imports in September 2017 and over 4 times short-term external debt showing improvement in external viability.

[1] Ministry of Finance, Department of Economic Affairs, Economic Division's Monthly Economic Report Sep 2017

5. Recent structural reforms are seen to have a slight impact on growth in the short run. However, they are expected to boost medium- to long-term growth prospects. To improve immediate growth prospects, teething troubles relating to GST need to be addressed expeditiously. Concerted efforts also need to be made to encourage investment activity by removing various constraints. Resolution of stressed balance sheets of banks remains important for supporting a revival in the investment cycle[2].

6. The RBI expects real GVA growth at 6.7 per cent in 2017-18 and 7.4% in 2018-19. In the September round of the RBI's survey, professional forecasters expected real GVA growth to pick up from 5.6 per cent in Q1:2017-18 to 7.2 per cent in Q4:2017-18 and to 7.5 per cent in Q2:2018-19, led by improvement in industry and services sector activity.[3]

7. As per the IMF's World Economic Outlook, World growth is projected to increase from 3.2 percent in 2016 to 3.6 percent in 2017 and 3.7 percent in 2018—an upward revision of 0.1 percentage point for both 2017 and 2018 relative to April. Economic activity is projected to pick up speed in all country groups except for the Middle East. India is expected to grow at 6.7% in 2017-18 and at 7.4% in 2018-19 as per the report, thus showing signs of recovery in the future.

**State's Economic scenario**

8. State's economic growth (GSDP) was 7.2% per cent during FY 16-17 as per the figures released by the DES. State's economy, being closely integrated with the national economy, is expected to be reflective of the overall national mood during the current year too.

[2] Minutes of MPC Oct 2017
[3] RBI bimonthly policy of Oct 2017

## Trends in State Government Finances

9. The Budget Estimates of Government of Karnataka for the year 2017-18 was presented to the Legislature during March 2017 for a total budget size of Rs. 1,86,561 crore. With GSDP at current prices indicated at Rs.13,10,879 crore, the Budget Estimates for the financial year 2017-18 projected fiscal deficit of 2.54 per cent of GSDP and a revenue surplus of 0.01 per cent of GSDP.

10. The Receipts and Expenditure at a Glance for 2017-18 at **Table 1** below shows a summary of receipts and expenditures along with the fiscal indicators for the year as set out in the Budget vis-à-vis that of the previous two years.

**Table 1: Receipts / Expenditures at a Glance**

(in `Crores )

| Sl No | Item | 2015-16 A/c | 2016-17 BE | 2016-17 RE | 2017-18 BE |
|---|---|---|---|---|---|
| 1 | Revenue Receipts | 118817 | 130758 | 132867 | 144892 |
| 1a | Own Tax Revenues | 75550 | 83864 | 82211 | 89957 |
| 1b | Own Non Tax Revenues | 5355 | 6220 | 7099 | 6945 |
| 1c | Devolution from GOI | 23983 | 26979 | 28760 | 31908 |
| 1d | GIA & Contributions | 13929 | 13694 | 14798 | 16082 |
| 2 | Capital Receipts (Non-debt) | 412 | 162 | 201 | 135 |
| 2a | Recovery of Loans and Advances | 60 | 87 | 104 | 60 |
| 2b | Other Non-debt Capital receipts | 352 | 75 | 97 | 75 |
| 3 | Total Receipts | 119229 | 130920 | 133068 | 145027 |
| | E Public Debt | 21072 | 31036 | 31036 | 37092 |
| | Total Receipts including Public Debt | 140302 | 161956 | 164104 | 182119 |
| 4 | Revenue Expenditure | 117029 | 130236 | 131805 | 144755 |
| 4a | Interest Payments out of 4 | 10746 | 12672 | 12291 | 14159 |
| 5 | Capital Expenditure | 21369 | 26341 | 25418 | 33630 |
| 5a | Loans and Advances disbursed out of 5 | 656 | 625 | 644 | 1597 |
| 6 | Total Expenditure (4+5) | 138398 | 156577 | 157222 | 178385 |
| | E Public Debt | 4110 | 6841 | 7256 | 8176 |
| | Total Expenditure including Public | 142508 | 163419 | 164479 | 186561 |

## Table 1: Receipts / Expenditures at a Glance

(in `Crores )

| Sl No | Item | 2015-16 A/c | 2016-17 BE | 2016-17 RE | 2017-18 BE |
|---|---|---|---|---|---|
| | Debt | | | | |
| 7 | Fiscal Deficit (6-3) | 19169 | 25657 | 24154 | 33359 |
| 8 | Revenue Deficit (4-1) | -1789 | -522 | -1062 | -137 |
| 9 | Primary Deficit (7-4a) | 8422 | 12986 | 11863 | 19200 |
| | GSDP at Current Prices | 735975 | 1117334 | 1117334 | 1310879 |
| | Fiscal Deficit | 2.60% | 2.30% | 2.16% | 2.54% |
| | Revenue Deficit | -0.24% | -0.05% | -0.10% | -0.01% |
| | Primary Deficit | 1.14% | 1.16% | 1.06% | 1.46% |

## Budget Estimates 2017-18

11. There is an increase of 14.16 per cent over the Budget estimate of FY 16-17. The Total Expenditure is estimated at Rs.1,78,385 Crore including Revenue Expenditure of Rs.1,44,755 Crore and Capital Expenditure of Rs. 33,630 Crore. The Total Receipts is estimated at Rs. 1,45,027 Crore which includes Revenue Receipts of Rs. 1,44,892 Crore and non-debt Capital Receipts of Rs. 135 Crore.

## Adherence to Karnataka Fiscal Responsibility Act, 2002

12. Revenue surplus of Rs.137 crores and fiscal deficit of Rs. 33,359 crore at 2.54 per cent of GSDP, have been estimated, both under limits prescribed by KFRA. Fiscal deficit for BE 2017-18 is higher than the Fiscal Deficit of 2.30 per cent estimated in BE 16-17. The Total Outstanding Liabilities (TOL) is estimated to reach a figure of Rs.2,42,420 Crore during FY 17-18. This is 18.49 per cent of GSDP as compared to BE 16-17 estimates of 18.67 per cent, and it is within the mandate prescribed by KFRA. Hence all the requirements under KFRA have been conformed to.

## Approval of full budget for 2017-18

13. To meet the expenditure of the Government in the first three months of the financial year i.e. April to June 2017, the State Legislature approved the Vote on Account (VoA) for incurring expenditure of Rs.48729.30 crore. Thereafter in June 2017, State passed the Appropriation Bill for the entire financial year (Apr 2017 to March 2018) for incurring expenditure of Rs.1,86,561 Crore.

## Public Disclosure of Fiscal Situation on monthly basis

14. The State is committed to being transparent in its fiscal operations. Information on the fiscal scenario of the State is being hosted on the official website of the State's Finance Department at ***www.finance.kar.nic.in*** on a monthly basis. For the

financial year 2017-18, the accounts for the first six months (April to September 2017) as compiled by the Accountant General have been hosted.

**Supplementary Estimates**

15. Under Article 205(1)(a) of Constitution of India, State Legislature can approve Supplementary Estimates during the course of the year to meet additional expenditure. During the first two quarters of FY 17-18, State has sought additional funds through Supplementary Estimates I instalment for an amount of Rs.1733.95 Crore (Gross) with a net cash out flow of Rs. 451.58 Crore. Further sanction for additional expenditure during the current session of Legislature will be sought. The details of the requirement are brought out in later part of this report.

## Review of trends in receipts and expenditure

## (April to September 2017)

16. This Report analyses the fiscal situation during the first half of the current financial year (H1) i.e. fiscal position as at the end of September 2017. The overview of the State's financial performance during H1 as compared to Budget Estimates 17-18 and that during the corresponding period in the previous year (2016-17) is summarized in **Table-2** shown below. Subsequently in the review, various components of receipts and expenditures have been compared.

### Table-2: Mid Year Comparison of Receipts, Expenditure and Fiscal Indicators

(` in Crores)

| Sl No | Item | 2017-18 BE | April to September (H1) 2017-18 | Percentage Achievement during H1 of 2017-18 to BE17-18 | Percentage Achievement during H1 of 2016-17 to BE16-17 | Increase over previous year |
|---|---|---|---|---|---|---|
| 1 | Revenue Receipts | 144892 | 67894 | 46.86% | 48.47% | 7.13% |
| 1a | Own Tax Revenues | 89957 | 43258 | 48.09% | 47.41% | 8.79% |
| 1b | Own Non Tax Revenues | 6945 | 2601 | 37.46% | 51.16% | -18.25% |
| 1c | Devolution from GOI | 31908 | 13666 | 42.83% | 42.86% | 18.20% |
| 1d | GIA & Contributions | 16082 | 8368 | 52.03% | 64.74% | -5.62% |
| 2 | Capital Receipts (Non-debt) | 135 | 83 | 61.69% | 32.00% | 60.92% |
| 2a | Recovery of Loans and Advances | 60 | 82 | 136.89% | 56.00% | 69.17% |
| 2b | Other Non-debt Capital receipts | 75 | 1 | 1.33% | 4.16% | -67.95% |
| 3 | Total Receipts | 145027 | 67978 | 46.87% | 48.45% | 7.18% |
|  | E Public Debt | 37092 | 2925 | 7.88% | 3.82% | 146.70% |
|  | Total Receipts including Public Debt | 182119 | 70902 | 38.93% | 39.89% | 9.74% |
| 4 | Revenue Expenditure | 144755 | 66976 | 46.27% | 41.94% | 22.62% |
| 4a | Interest Payments out of 4 | 14159 | 5866 | 41.43% | 40.80% | 13.46% |

(` in Crores)

| Sl No | Item | 2017-18 BE | April to September (H1) 2017-18 | Percentage Achievement during H1 of 2017-18 to BE17-18 | Percentage Achievement during H1 of 2016-17 to BE16-17 | Increase over previous year |
|---|---|---|---|---|---|---|
| 5 | Capital Expenditure | 33630 | 7892 | 23.47% | 21.46% | 39.60% |
| 5a | Loans and Advances disbursed out of 5 | 1597 | 181 | 11.33% | 8.45% | 242.37% |
| 6 | Total Expenditure (4+5) | 178385 | 74868 | 41.97% | 38.50% | 24.21% |
| | E Public Debt | 8176 | 3314 | 40.54% | 46.04% | 5.23% |
| | Total Expenditure including Public Debt | 186561 | 78182 | 41.91% | 38.81% | 23.27% |
| 7 | Fiscal Deficit (6-3) | 33359 | 6891 | | | |
| 8 | Revenue Deficit (4-1) | -137 | -918 | | | |
| 9 | Primary Deficit (7-4(a)) | 19200 | 1025 | | | |
| | **GSDP at Current Prices** | **1310879** | **1310879** | | | |
| | **Fiscal Deficit** | **2.54%** | **0.53%** | | | |
| | **Revenue Deficit** | **-0.01%** | **-0.07%** | | | |
| | **Primary Deficit** | **1.46%** | **0.08%** | | | |

**Resource Position (Non Debt)**

17. The non debt resources of the State include Own Tax and Non Tax resources, Devolution from GOI, GIA and Contributions from GOI and Non Debt Capital Receipts.

**Own Tax and Non Tax Receipts (Own Revenue Receipts)**

18. The collection of own revenue receipts have shown a healthy increase in the first half of 2017. The total revenue receipts of the state during the first six months of financial year 2017-18 ending September 2017 is Rs. 67,894 crore including the States' Own Tax Revenue (SOTR) of Rs. 43,258 crore and State's Own Non Tax Revenue (SONTR) of Rs. 2601 crore. Thus the total Own Revenue Receipts (ORR) during the first half (H1) of financial year 2017-18 is 47 per cent of that budgeted for the full year, which is on par with the moving average of 47 per cent

during H1 of the previous five years (**Table 3**). Total receipts (excluding borrowings) for the State during H1 of this year is around 7.1 per cent above that during the corresponding period in 2016-17.

**Table 3: Five year trend in State's Own Tax and Non Tax Receipts (ORR) – April to September**

(` in Crores)

| Particulars | 2012-13 | 2013-14 | 2014-15 | 2015-16 | 2016-17 | 2017-18 |
|---|---|---|---|---|---|---|
| SOTR | 25590 | 28744 | 32671 | 35671 | 39762 | 43258 |
| SONTR | 1645 | 1669 | 1978 | 2213 | 3182 | 2601 |
| Total ORR | 27235 | 30413 | 34649 | 37884 | 42944 | 45860 |
| BE | 55014 | 66502 | 74343 | 81652 | 90085 | 96901 |
| **% to BE** | **50%** | **46%** | **47%** | **46%** | **48%** | **47%** |

### State's Own Tax Revenue (SOTR)

19. State's Own Tax Revenue (SOTR) includes amongst others, the four major State taxes viz. Commercial Taxes, Excise, Motor Vehicle Taxes and Taxes on Stamps & Registration. All the major SOTR have shown reasonable achievement during the first six months of 2017-18, in terms of percentage achievement to BE with 48 per cent of the budget estimate of SOTR already been achieved in first six months of 2017-18, which is a notch higher than that achieved in 2016-17 during the same period. **Table 4** provides the SOTR breakup.

## Table 4: State's Own Tax Revenues (SOTR)

(` in Crores)

| Particulars | 2017-18 BE | Actual upto Sept 2017 | Actual upto Sept 2016 | % to BE 17-18 | % to BE 2016-17 | Growth over Previous Year |
|---|---|---|---|---|---|---|
| Commercial Taxes | 55000 | 26753 | 24792 | 49% | 48% | 7.9% |
| State Excise | 18050 | 8539 | 8063 | 47% | 49% | 5.9% |
| MV Taxes | 6006 | 2870 | 2584 | 48% | 50% | 11.1% |
| Stamps & Reg Fees | 9000 | 4127 | 4006 | 46% | 44% | 3.0% |
| Others | 1901 | 969 | 316 | 51% | 18% | 206.2% |
| **Total** | **89957** | **43258** | **39762** | **48%** | **47%** | **8.8%** |

- **Commercial Taxes**

20. Commercial taxes witnessed a growth of 8 per cent over the collections during the first half of 2017-18 which is less than the 13.3% growth achieved during the corresponding time of the previous year. While 48 per cent of the budget estimate was collected during H1 of FY 16-17, the collection as percentage of budget estimate during H1 of the current year is higher at 49 per cent .It is expected that the budget estimates would be met.

**Goods and Services Tax**

21. GST has been implemented in the country with effect from 1st July, 2017 and the tax pertaining to July and August has been collected by the Government (in the months of August and September). For these two months, the total SGST collection has been Rs. 4100 crore and the State has received net settlement of Rs. 1470 crore from the IGST account. In the same period, Rs. 140 crore has been collected from VAT and other subsumed taxes pertaining to periods before introduction of GST. Taking into account all these revenues, an amount of

Rs.5710 crore has been collected for this period. The revenue collected during these two months (August and September) in 2016-17 was Rs. 6190 crore. As per the Compensation Act, the revenue to be compensated for this period with a 14% per annum growth over the 2015-16 collection is Rs. 6640 crore. The gap will be compensated by the Central Government as compensation to the State.

- **Excise**

22. State Excise collections have fared well. As against the budgeted estimate of Rs.18,050 crore, collections in first six months of 2017-18 is 47 per cent i.e. Rs.8,539 crore with a growth rate of 6 per cent over corresponding period of 2016-17. It is expected that the budgetary targets would be achieved.

- **Motor Vehicles Tax**

23. In first half of 2017-18, Motor Vehicle Tax grew at 11.1 per cent over that of the same period during 2016-17. With 48% collection against the budget estimate of Rs.6,006 crore mid year, it is expected that the budget estimates would be fully met.

- **Stamps and Registration Tax**

24. The receipts under Stamps and Registration are at 46% to budget estimates and is growing at 3% over that of the corresponding period in 2016-17. With sustained efforts, it is expected that the budgetary targets would be achieved.

- **State’s Own Non Tax Revenue (SONTR)**

25. The non-tax revenues majorly consists of receipts from mining, Interest receipts and others .Under own non-tax revenues, the realization this year as at the end of September 2017 was Rs.2,601crore, which is around 37.46 per cent of the budget estimates of Rs.6,945 crore for the year.

**Devolution of Central Taxes and Grant-in-Aid (GIA) & Contributions from Government of India**

26. Devolution from Government of India has continued to flow at 1/14th of the budgetary estimates. The receipt during the first six months of 2017-18 is Rs.13,666 crore at 43 per cent of budget estimate of Rs. 31,908 crore. The devolution as a proportion of actuals of 16-17 was also 43% in the first half of last year. Meanwhile, devolution which was being received on the 1st of every month till August 2017 has been changed to the 15th of every month for FY 17-18. From FY 18-19, devolution part comprising of Income Tax and corporation taxes is going to be released only quarterly. This implies that amount would flow in only from June of that year for these components. The other components viz, Basic custom duty would be released on 15th of every month and Service Tax and Excise duty on the 20th of every month. Significant amount of money gets devolved to the states which help in cash flow management on a monthly basis. Shifting of the date of release of this amount affects the State financially. Receipts of grants in aid and contributions from Government of India is Rs.8,368 crore during the first half of FY 17-18 as against the budget estimate of Rs.16,082 crore for the full year. This corresponds to 52% to BE when compared to 64.7% to BE received during the FY 16-17. It is expected that all the administrative departments will put in efforts to receive the full budgeted central assistance.

**Non Debt Capital Receipts (NDCR)**

27. Non debt capital receipts are primarily receipts from recovery of loans and advances and also receipts from sale of assets. For the current year 2017-18, the total receipts during first six months under this head has been Rs.83 crore which translates to around 62 percent of the budget estimate of Rs.135 crore.

## Overall Resource Position (Non Debt)

28. Major taxes and non-tax receipts are likely to meet the budgeted targets. Moreover, State expects that the shortfall in GST collections would be made good by GoI.

## Public Debt (Gross Borrowings)

29. Public Debt constitutes internal debt and loans and advances from GoI. Internal debt mainly comprises of gross open market borrowings of the State, National small savings Fund (NSSF) loans and negotiated loans. In FY 17-18, the State has tried to improve efficiency in open market borrowings by scheduling it based on the cash flow requirement as per the receipt and expenditure profile. Because of uncertainty in GST an amount of Rs.1500 Crore has been borrowed in the last week of September. No borrowings were resorted to during the first half of the year taking into account cash position during FY 2016-17.

## Total Expenditure (including Public Debt) or Budget Size

30. Total Expenditure including public debt during April-September 2017 stood at Rs.78,182 crore which is 41.91% per cent of total budgeted expenditure in 2017-18. While revenue expenditure in first six months of 2017-18 has grown by 22.62% per cent, capital expenditure is increased by 39.6 per cent over the corresponding period in 2016-17. Public Debt expenditure is 40.50% of the budgeted expenditure. The overall increase in Total Expenditure including public debt is about 23.27% per cent as compared to same period in 2016-17. **Table 5** shows the overall trends in expenditure.

**Table 5: Trends in Budget Size - April to September**

(Rs. in Crores)

| Particulars | 2012-13 | 2013-14 | 2014-15 | 2015-16 | 2016-17 | 2017-18 | Growth over previous year |
|---|---|---|---|---|---|---|---|
| Revenue Expenditure | 31176 | 37030 | 46544 | 49811 | 54622 | 66976 | 22.6% |
| Capital Expenditure | 5258 | 5526 | 6340 | 5985 | 5654 | 7892 | 39.6% |
| Total Expenditure | 36434 | 42556 | 52884 | 55796 | 60275 | 74868 | 24.2% |
| Public Debt | 1639 | 2671 | 2107 | 1878 | 3150 | 3314 | 5.2% |
| Budget Size | 38073 | 45227 | 54990 | 57675 | 63425 | 78182 | 23.3% |
| BE for full Year | 102742 | 121611 | 138008 | 142534 | 163419 | 186561 | 14.2% |
| % to BE | **37%** | **37%** | **40%** | **40%** | **39%** | **42%** | - |

**Scheme Expenditure**

31. With a view to improve the pace of implementation of schemes and thereby improve expenditure, it has been endeavored to facilitate timely release of funds through delegation of powers. Finance Department has delegated powers of fund releases to the concerned Administrative Secretaries for the first three quarters of FY 17-18 for almost all the major schemes of departments.

32. With the powers to release the budgeted amount being delegated to administrative departments, the scheme expenditure is expected to increase further in the last two quarters of the current year and reach the budget estimate. However, consistent efforts from all the administrative departments are required to minimize the rush of expenditure in the month of March.

33. The growth rate of committed expenditure has been lower than the scheme expenditure. This has become possible by enforcing economy orders. More accurate budgeting of major committed components like salary and pensions by using the HRMS database have helped to rationalize the allocations.

**Resources Transferred to Local Bodies**

34. As per recommendations of the Third State Finance Commission (TSFC) which was accepted by the State with certain modifications, total funds to be devolved on to local bodies was increased from 40 per cent to 42 per cent of the Non Loan Net Own Revenue Receipts (NLNORR) of the State. Out of this, 32 per cent of NLNORR was to be assigned to Panchayat Raj Institutions (PRIs) and 10 per cent to Urban Local Bodies (ULBs), inclusive of their salary expenditure. For the year 2017-18, the corresponding devolution figure for ULBs is 10 percent of NLNORR and for PRIs it is 32 per cent of NLNORR. The $4^{th}$ SFC has been constituted and is expected to submit the report by this year.

35. The releases for PRIs and ULBs during the period April to September 2017 as against the budget estimate by Finance Department is shown in the following **Table 6.**

**Table 6: Resources transferred to PRIs and ULBs**

(Rs. in crores)

| Particulars | 2017-18 BE | Actual upto Sep 2017 | % to BE |
|---|---|---|---|
| PRIs | 32794 | 23675 | 72.19% |
| ULBs | 7187 | 2847 | 39.61% |
| **Total** | **39982** | **26522** | **66.33%** |

## Fiscal and Debt Management

36. State is known for the prudent management of its finances. Being the first State in the country to lay out a fiscal consolidation roadmap to improve its finances, it went on to achieve the fiscal and debt consolidation targets laid out therein well ahead of the timeline prescribed.

### Cash Management

37. The State has not availed of any Special Ways and Means Advances (SWMA) or Normal Ways and Means Advances (NWMA) from RBI since 2008-09. Even during the first half of FY 17-18, due to the reasonably comfortable cash position, there wasn't any necessity to operate SWMA / NWMA. As advised by RBI, additional cash balance available over and above anticipated requirement is being invested in GOI's 91 day Auction Treasury Bills. Such investment enables State to earn additional interest income.

### Market borrowings

38. Of the budgeted gross borrowings of Rs. 34,717 crore from Open Market in the current fiscal year, up to end of September 2017, State has got Government of India's consent to borrow Rs. 30,358 crore for the first nine months of the FY 2017-18 under Article 293(3) of Constitution. GOI will also be requested to provide concurrence for balance requirement. An amount of Rs.1500 crore has been borrowed till September and remaining borrowings will be undertaken in the last two quarters only on necessity basis and within the permissible limit.

### Contingent liabilities

39. Contingent Liabilities are those commitments given by the State which could become actual liabilities in the books of the State Government in future. Government guarantees are contingent liabilities which the State has to take onto its books in case of default in repayment by the guaranteed borrower and where the guarantee is invoked by the lender.

40. The Karnataka Ceiling of Government Guarantee Act (KCGGA), 1999 provides for a cap on outstanding guarantees extended by the Government as at the end of any year at 80 per cent of the State's revenue receipts of the second preceding year. Since the enactment of KCGGA, the outstanding guarantees at the end of the financial year have all been well within the prescribed limit.

41. At the end of FY 16-17, the 'outstanding guarantees as a percentage of State's revenue receipts of the second preceding year' was around 14.78 per cent. Even by the end of FY 17-18, it would be ensured that the statutory ceiling of guarantees would not be breached.

**Off Budget Borrowings**

42. Off Budget Borrowings are borrowings availed by State public sector enterprises or agencies whose principal and interest repayment is however, made through the budget. For estimation of Total Outstanding Liabilities (TOL), State has been taking into account the liabilities under Off Budget Borrowings also.

43. During February 2014, KFRA 2002 was amended to provide legal framework to formalize the system. During FY 17-18, fresh Off Budget Borrowing of Rs. 3528 crore has been allowed for the special purpose vehicles of Water Resource Departments i.e. KBJNL, KNNL, CNNL and KRDCL. They will be raising the funds based on both the requirement and prevailing market conditions.

## 6

### Deficit Management

44. The KFRA 2002 lays out the roadmap for fiscal discipline to be followed by the State. The State is bound by the provisions under KFRA of maintaining adequate revenue surplus and ensuring that fiscal deficit is kept below 3 per cent of GSDP. The following Table-7 table provides the trends available for first six months of financial year 2017-18 for various deficit parameters as compared with previous five half yearly figures.

**Table 7: Deficit Trends – April to September**

(` in Crores)

| Item | 2012-13 | 2013-14 | 2014-15 | 2015-16 | 2016-17 | 2017-18 |
|---|---|---|---|---|---|---|
| Revenue Deficit April to September | -5351.50 | -2987.49 | -2130.01 | -4381.15 | -8751.11 | -918.49 |
| Revenue Deficit full year (BE) | -930.77 | -595.84 | -281.28 | -910.63 | -522.00 | -136.53 |
| % of BE | 574.95% | 501.39% | 757.26% | 481.11% | 1676.46% | 672.74% |
| % of GSDP | -1.03% | -0.50% | -0.31% | -0.60% | -0.78% | -0.07% |
| Fiscal Deficit April to September | -138.84 | 2463.10 | 4159.59 | 1255.61 | -3149.28 | 6890.51 |
| Fiscal Deficit full year (BE) | 15312.31 | 17449.50 | 20041.43 | 20220.01 | 25657.10 | 33358.71 |
| % of BE | -0.91% | 14.12% | 20.75% | 6.21% | -12.27% | 20.66% |
| % of GSDP | -0.03% | 0.41% | 0.61% | 0.17% | -0.28% | 0.53% |
| Primary Deficit April to September | -2737.54 | 733.21 | 446.77 | -3212.70 | -8319.01 | 1024.93 |
| Primary Deficit full year (BE) | 7812.31 | 8949.50 | 10341.43 | 9552.34 | 12985.56 | 19199.83 |
| % of BE | -35.04% | 8.19% | 4.32% | -33.63% | -64.06% | 5.34% |
| % of GSDP | -0.53% | 0.12% | 0.07% | -0.44% | -0.74% | 0.08% |

## Revenue Surplus

45. Revenue Surplus is the excess of revenue receipts over revenue expenditure. KFRA mandates that the State should maintain revenue surplus. Karnataka has been maintaining revenue surplus since 2004-05. Up to September 2017, the revenue surplus is Rs. 918 crore as compared to the budget estimate of Rs. 137 crore, reflecting a comfortable mid-year revenue position for the State. Revenue Surplus would also be maintained at the end of FY 17-18.

## Fiscal Deficit to GSDP

46. Fiscal Deficit is the difference between total expenditure (excluding debt repayment) and non-debt receipts. It reflects the expenditure met out of borrowed/debt funds. As KFRA requires that Fiscal Deficit should be kept within 3 per cent of GSDP, fiscal deficit was estimated at 2.54 per cent of GSDP i.e. Rs.33,359 crore. As compared to this, the State had a fiscal deficit of Rs. 6891 crore as at the end of September 2017.

47. With prudent fiscal management, continuing revenue mobilization efforts, pruning down non-essential expenditure and identification of savings to partly finance new expenditure commitments included in the Supplementary Estimates, it should be possible to remain within the fiscal deficit limit prescribed under the KFRA Act.

## Financing of Fiscal Deficit

48. Fiscal Deficit is financed from Net Receipts from internal debt, loans and advances from GOI, contingency fund, public account and cash balance. **Table 8** shows the snapshot of financing of deficit.

## Table 8 : Financing of Fiscal Deficit (Upto Sep 2017)

(` in Crores)

| Sl No. | Item | BE 2017-18 | Apr - Sep 2017 |
|---|---|---|---|
| 1 | Internal Debt (Net) | 28329 | -858 |
| 2 | Loans & Advances from GOI (Net) | 588 | 469 |
| 3 | Contingency Fund (Net) | 0 | 0 |
| 4 | *I Provident Fund (Net)* | 2484 | 638 |
| 5 | *J Reserve Funds (Net)* | 763 | 310 |
| 6 | *K Deposits (Net)* | -4029 | 10790 |
| 7 | *L Suspense A/c (net)* | 5029 | -4893 |
| 8 | *M Remittances (Net)* | 0 | -57 |
| 9 | Increase/Decrease in Cash Balance(OB-CB) | 196 | 492 |
| **10** | **Total Deficit Financing** | **33359** | **6891** |
| 11 | Net from Public Account | **4246** | **6788** |

### Primary Deficit to GSDP

49. Primary Deficit is the Fiscal Deficit less interest payments. This constitutes the core deficit for the year as it excludes earlier year interest payments. BE 17-18 for Primary Deficit has been estimated at Rs. 19,200 crores which is 1.46 per cent of GSDP. During the first six months of FY 17-18, there is primary deficit of Rs.1,025 crores. The primary deficit of the full year is expected to remain well within the budgeted estimate.

**Total Outstanding Liabilities to GSDP**

50. The Total Outstanding Liabilities (TOL) is worked out by including under it all outstanding liabilities under public debt, public account and off-budget borrowings. This covers the entire ambit of liabilities. TOL to GSDP as at the end of the financial year 2016-17[4] was 19.81 per cent as against the KFRA ceiling limit of 25 per cent for that year. While the TOL of the State in absolute numbers is expected to increase from Rs.2,08,557 crore in FY 16-17 to Rs.2,42,420 crore in FY 17-18, the GSDP of the State is projected to increase from Rs.11,17,334 crore to Rs.13,10,879 crore during the same period (as estimated by MoF, GOI). Thus TOL to GSDP ratio will remain within 25%.

[4] As per Accounts Pre actual 2016-17

## Supplementary Estimates

### Supplementary Estimates – 1st Instalment

51. In accordance with Article 205(1)(a) of Constitution of India, State Legislature approved the Supplementary Estimates – I installment for an expenditure amounting to Rs.1734 crore, with a net cash outflow of Rs.452 crore in June 2017. The net cash outflow is proposed to be funded out of the overall savings in expenditure.

### Supplementary Estimates – IInd Instalment

52. Total gross outlay of Rs.7476.86 crore has been proposed in the Supplementary Estimates II Instalment to be presented before the Legislature in November 2017. After adjusting for expenditure met out of reserve funds and deposits and taking into account the central receipts and adjustments, net additional expenditure out of Consolidated Fund is Rs.5662.23 crore. Keeping the overall fiscal position of the State in mind, only the most essential requirements have been included in Supplementary Estimates.

53. Major items of expenditure included in the Supplementary Estimates II Instalment are loan waiver scheme, state highway development programme, district and other roads.

### Financing of net additional expenditure out of Consolidation Fund

54. As per Section 6(5) of KFRA, a statement of financing the additional expenditure under Supplementary Estimates needs to be provided. The net additional expenditure out of the Consolidated Fund amounting to Rs.5662.23 crore would be met out of expenditure re- prioritisation.

55. With the above measures, all the KFRA mandated revenue, fiscal and debt indicators would be kept within prescribed limits at the end of FY 17-18.

## 8

### Mid Year Assessment of Medium Term Fiscal Plan (MTFP) benchmarks

56. Section (3) of KFRA 2002 mandated that in particular MTFP shall assess sustainability of State finances relating to

    - Balance between revenue receipt and revenue expenditure
    - Use of capital receipts for generating productive assets.

57. MTFP 2017-21 projected revenue surplus of Rs.137 crores for the year 2017-18 with revenue receipt and revenue expenditure being estimated at Rs.1,44,892 crore and Rs.1,44,755 crore respectively. During H1 of FY 17-18, revenue surplus is at Rs. 918 crore with the revenue receipts at Rs. 67,894 crore and revenue expenditure at Rs. 66,976 crores. Thus there is a favourable mid-year balance.

58. However revenue balance has to be carefully managed with additional revenue expenditure requirement of Supplementary Estimates. To offset the impact, the strategy of expenditure reprioritisation within budget estimates 2017-18 and use of accumulated reserves in the public account would be adopted.

59. On the capital side, State has incurred expenditure of Rs.7,892 crore during H1 of FY 17-18 and is in line to achieve target of Rs.33,630 crore to be spent on generating productive assets. The additional capex requirement in supplementary estimates would have to be met out of expenditure savings within budget estimates 2017-18.

60. State in general, would need to be cautious while expanding its expenditure, as this would be in the backdrop of continued slower growth of national and State economy, albeit visible signs of recovery, high inflation and weakening industrial production. All these factors would have long term impact on the State's own revenue mobilisation efforts and devolution anticipated from Government of India.

Thus, the mid-year review suggests a balanced approach while deciding on enhancing outlays. This is imperative if the State has to conform to its statutory fiscal obligations under KFRA 2002.

## 9

## FMRC Recommendations and the Road Ahead

### Outlook for 17-18 and the way forward

61. To balance the requirement of providing adequate funds to critical sectors of the economy and that of adherence to fiscal prudence norms, the strategy for the remaining part of the financial year will include the following:

    - Complying with the Karnataka Fiscal Responsibility Act, 2002 commitments;
    - Ensuring attainment of budgetary tax targets to ensure availability of sufficient resources.
    - Full utilization of the central assistance available including the Centrally Sponsored Schemes.
    - Providing adequately for the capital expenditure as envisaged in the budget.

### FMRC Mid Year Review

62. During November 2017, the Fiscal Management Review Committee (FMRC) headed by the Chief Secretary to Government reviewed the fiscal and debt position of the State and its progress on fiscal correction path as required under the KFRA. The Committee deliberated in detail on the mid-year fiscal and debt parameters and thereafter advised the Finance Minister on the remedial measures to be adopted to ensure adherence to the parameters stipulated in KFRA on the following:-

    a. Change in the release dates for the devolution from FY 17-18 and proposed quarterly release from FY 18-19 was discussed. Since significant amount of money gets devolved to the states which help in cash flow management on a monthly basis and shifting of the date of release of this amount affects the cash position of the State, the committee advised Finance Department to do necessary follow up with GoI with a request to revert to the previous methodology employed for releases.

b. Budget estimates of this financial year has seen an increase of 14.16% over the previous year. This would require equivalent increase in the revenue collection front also. Else, there would be strain on expenditure front. Added to this, marginal revenue surplus estimated in BE 17-18 is also a cause of concern. Since additional demands have already been included through SE-I and SE-II, including the package of loan waiver which was not budgeted, re-prioritization of expenditure was impressed upon.

c. The model of using cash reserves as in the case of MML to help fund the loan waiver scheme was discussed. The committee suggested to Finance Department to find out other means of meeting the huge requirement of loan waiver.

d. The Committee advised Finance Department to closely study the impact of shortfall in GST collection and to follow up with GoI to receive the complete compensation due. The committee also advised the Commercial Taxes department to put in concerted efforts to increase the collections under GST and to improve registrations under GST.

e. The committee advised that steps need to be taken to improve the capital receipts.

f. The committee observed that the sale of IML in the State has reduced when compared to the neighbouring States and recommended proactive measures from the Excise department. In the case of registration of motor vehicles too, a dip was observed when compared to the registrations last year. The committee recommended to the department to examine and rationalize the tax structure and to resolve issues which have arisen like that of lifetime tax so as to improve the registrations and thereby tax collections in future.

g. The committee discussed on the reduced non tax collections till mid year. Since majority of non taxes are on account of mining receipts, the committee recommended immediate action towards auctioning of the remaining mines to meet the targets. During the discussion, the FMRC committee also noted the efforts taken by the committee headed by the Additional Chief Secretary and Development Commissioner on the revision of non tax revenues and advised all departments to take necessary action to revise rates which are due for a long time.

h. Over the past few years, the State has had to bear the additional funds out of its own resources to meet the commitments under the Centrally Sponsored schemes. The mid year receipts from Central Government towards the central schemes has shown a decline. The committee recommended a close watch on the receipts from Central Government for the rest of the year and advised Administrative Departments to follow up with the respective Ministries.

i. The committee advised that more number of schemes need to be brought under the DBT so as to improve efficiency.

j. Preventing idle parking of funds in bank accounts was stressed upon by the committee.

k. With expected additional burden on account of recommendations of the Pay Commission which has been set up, steps to augment resources was discussed. The committee advised suitable reprioritization of expenditure and augmentation of own resources to help make the additional requirements.

***