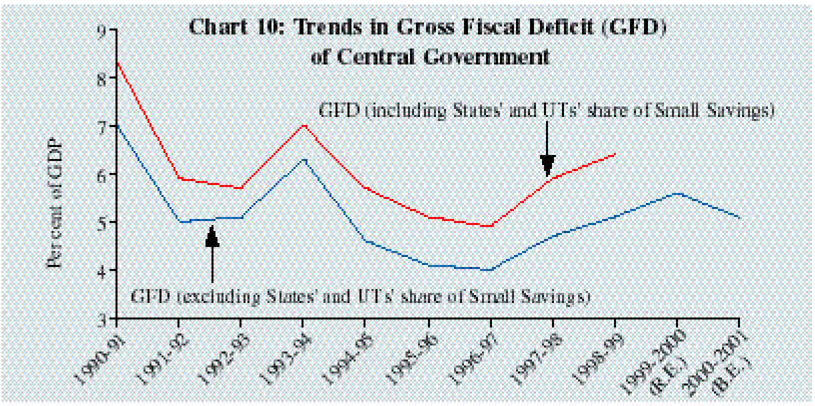
II. Fiscal Situation

Centre's Fiscal Deficit

The fiscal situation in 1999-2000 proved to be difficult partly because of cyclical, unforeseen and security related factors. Net revenue collection of the Central government fell short of the budgeted target by Rs.3,336 crore while proceeds from disinvestment declined from the budgeted level of Rs.10,000 crore to Rs.2,600 crore in the revised estimates. The revenue shortfall was exacerbated by pressures from the unanticipated increase in defence expenditure, additional relief expenditure due to a super cyclone in Orissa, elections, the residual impact of the Fifth Pay Commission and higher level of fiscal assistance to States. Added to this were the higher level of support to plan expenditure and increases on account of interest payments. Total expenditure of the Central government, as a result, overshot the budgeted target by Rs.19,856 crore as per the revised estimates. The pressure was felt on the gross fiscal deficit[3] (excluding the States' and Union Territories' (UTs') share of small savings), which increased from the budgeted Rs.79,955 crore to Rs.1,08,898 crore in the revised estimates. As proportion to GDP, the Centre's gross fiscal deficit (excluding the States' and UTs' share of small savings) increased from 4.0 per cent in the budget estimates to 5.6 per cent in the revised estimates. the Compared to the actual of 1998-99, Centre's gross fiscal deficit (excluding States' and UTs' share of small savings) increased by 0.5 percentage point in 1999-2000 (Chart 10). Almost all key fiscal indicators such as the primary deficit, revenue deficit, debt to GDP ratio and interest payments to GDP ratio witnessed a deterioration in 1999-2000 (Chart 11).



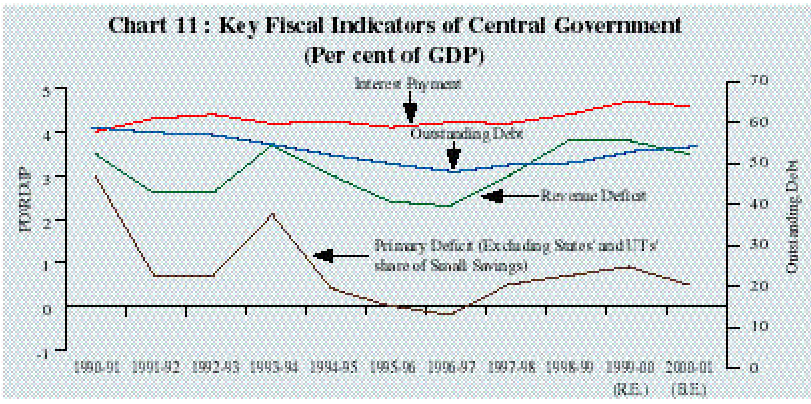


Chart 11 : Key Fiscal Indicators of Central Government (Per cent of GDP)

Market Borrowing

The Central government's borrowing requirement showed a substantial rise in 1999-2000. The net market borrowing of the Central government increased from Rs.57,461 crore in the budget estimates to Rs.73,077 crore (including 364-day Treasury Bills) according to the Reserve Bank's records. At this level, the gross market borrowing through dated securities amounted to Rs.86,630 crore in 1999-2000, as against Rs.83,753 crore in 1998-99. Including the fresh issue of 364-day Treasury Bills, the gross market borrowing of the Central government rose to Rs.99,630 crore from Rs.93,953 crore in 1998-99. During the past three years, market borrowings of both the Central and State governments have gone up sharply, with the steepness being prominent in 1998-99 (Chart 12).

During 1999-2000, the Reserve Bank's initial subscription to the Central government's borrowing programme by way of private placement of dated securities (Rs.27,000 crore) and devolvement of 364-day Treasury Bills amounted to Rs.29,267 crore as against Rs.39,777 crore in 1998-99, which included Rs.30,000 crore of private placement. In 1999-2000, the need for initial subscription from the Reserve Bank through private placement and devolvement was relatively low due to a strong increase in the demand for government securities by banks, financial institutions and mutual funds. The market sentiment during 1999-2000 remained positive in absence of major domestic and international uncertainties. Scheduled commercial banks' investment in government securities increased by Rs.54,612 crore in 1999-2000 as against Rs.36,261 crore during the previous year. Currently, scheduled commercial banks are holding above Rs.80,000 crore of government and other approved securities in excess of the minimum statutory liquidity requirement.

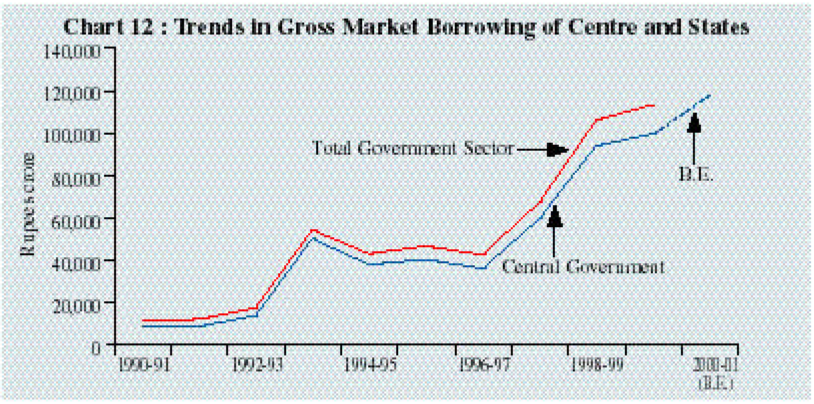


Chart 12 : Trends in Gross Market Borrowing of Centre and States

While the debt management strategy through the private placement mechanism helped to stabilise the cost of borrowing to the government, the Reserve Bank used the open market window to release the securities from its portfolio to mop up the excess liquidity from the system. During 1999-2000, net open market sale of securities (net) amounted to Rs.30,861 crore as against Rs.29,669 crore in 1998-99. The cut-off yield on medium and long-term securities showed a substantial decline during 1999-2000. The cut-off yield on Central government 10-year bond declined steadily from 12.25 per cent in December 1998 to 11.99 per cent in April 1999 and to 11.59 per cent in August 1999. The yield on the longest maturity bond of 20 years declined from 12.60 per cent in January 1999 to 12.42 per cent in May 1999 (19 years and 5 months) and to 12.05 per cent in October 1999 (19 years and one month).

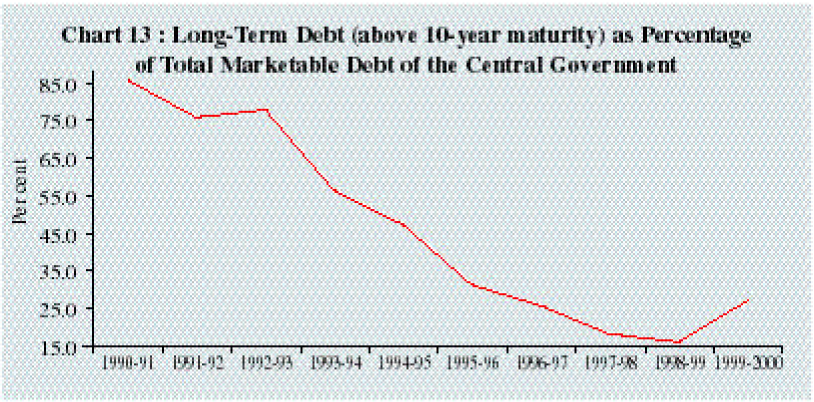


Chart 13 : Long-Term Debt (above 10-year maturity) as Percentage of Total Marketable Debt of the Central Government

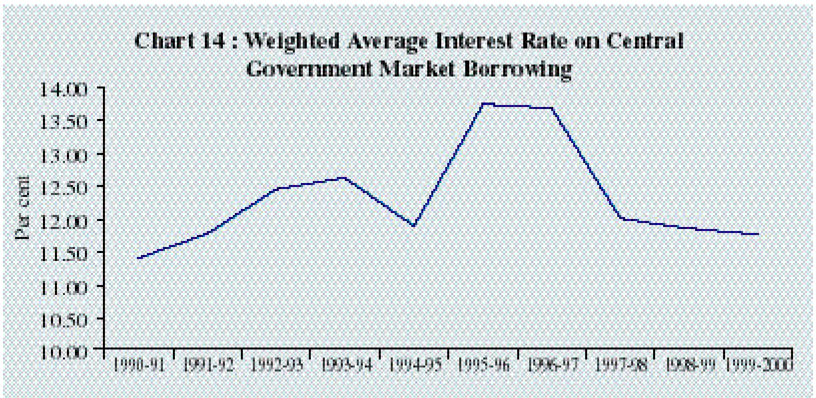
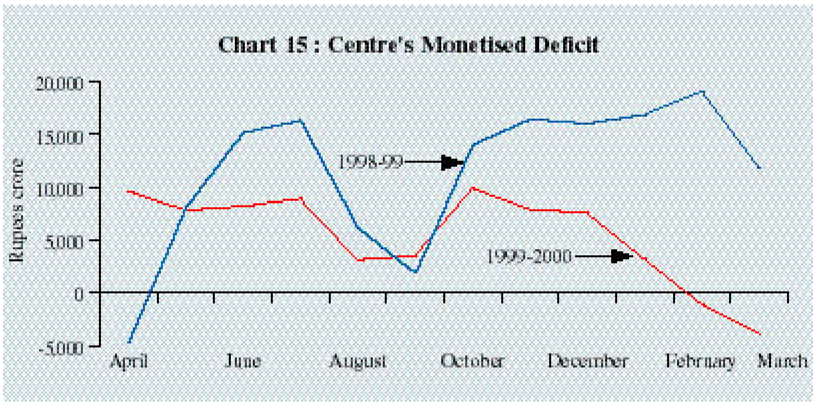


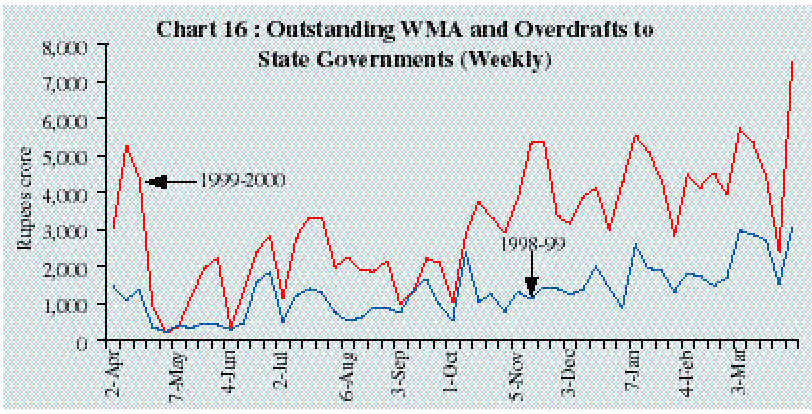
Chart 14 : Weighted Average Interest Rate on Central Government Market Borrowing

As a part of the debt management strategy to elongate the maturity profile of marketable debt, a substantial part of the government borrowing (65.0 per cent) was raised through bonds with maturity over 10 years. In fact, all borrowings in 1999-2000 were above 5-year maturity, ranging between 6 to 20 years. As could be seen from Chart 13, there has been a turn around in the falling trend of the share of long-term bonds in the total marketable debt of the Central government in 1999-2000. Thus, the weighted average maturity of Central government market borrowing increased from 7.7 years in 1998-99 to 12.64 years in 1999-2000. Notwithstanding that there was concentration of borrowing at the longer-end of maturity, the overall borrowing cost to the government declined during 1999-2000. The weighted average cut-off yield on the Central government market borrowing declined to 11.77 per cent in 1999-2000 from 11.86 per cent in 1998-99. The weighted average cut-off yield has shown a substantial decline in recent years as revealed by Chart 14, and was only slightly above the level of coupon rates in 1990-91, *i.e.*, before the introduction of the system of auctioning of Government securities. In the first auction of dated securities during 2000-01, held on April 13, 2000, the cut-off yield of 10 year security declined to 10.26 per cent from 11.59 per cent in August 1999.



The liquidity management operation put in place during the year (see Section 3 for details) also ensured a lower order of monetised deficit of the Central government, despite a higher level of fiscal deficit. In fact, before the closure of government accounts, the net Reserve Bank credit to the Central government during 1999-2000 declined by Rs.3,865 crore, recording a monetised surplus for the first time since 1977-78. The net Reserve Bank credit to the Central government had increased by Rs.11,800 crore during 1998-99. Throughout 1999-2000, the Centre’s monetised deficit remained below that of 1998-99, except in April and September 1999 (Chart 15).

Several States faced financial difficulties and frequently resorted to the Ways and Means Advances (WMA) and overdrafts from the Reserve Bank despite the recent enhancement of the WMA limits of State governments to Rs.3,685 crore from Rs.2,234.4 crore. The outstanding level of WMA and overdrafts of States from the Reserve Bank increased from Rs. 4,818 crore as on March 31, 1999 to Rs. 7,519 crore as on March 31,2000, which included an overdraft of Rs. 4,092 crore (Chart 16).



The gross fiscal deficit of the Central government for 2000-2001 has been budgeted lower at 5.1 per cent of GDP than 5.6 per cent in 1999-2000. The Union budget has placed the net market borrowing programme at

Rs.76,383 crore in 2000-2001 as against Rs.73,077 crore in 1999-2000. Together with repayment of maturing loans and 364-day Treasury Bills, the gross borrowing requirement works out to Rs.1,17,704 crore as against Rs.99,630 crore in 1999-2000. Raising this order of gross market borrowing would pose a challenge. It is, however, necessary to ensure that the interest rate conditions remain favourable to industrial recovery and that liquidity conditions do not give rise to adverse inflationary expectations. Monetary policy has to play a balancing role in this context.

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[3] The gross fiscal deficit is the excess of total expenditure including revenue and capital expenditure and net disbursement of loans by the Central government (excluding the States' and UTs' share of small savings) over the revenue receipts and proceeds from disinvestment.