MANY INDIAN STATES ARE STRUGGLING TO MAKE ENDS MEET

Last month, global ratings agency Moody’s cut its outlook for India’s credit ratings to “negative” from “stable”. Pressure on revenues in the face of a sharp slowdown and the corporate tax cut means the Centre will be stretched to meet its spending needs. This in turn, Moody's said, will see the budget deficit climb to 3.7% of GDP in FY 2019, breaching the Centre’s 3.3% target. In a recent report, the ratings agency analyzed how the state of the states’ finances also causes a drag for the Centre’s fiscal targets. The states, it said, do not generate sufficient own source revenue for their spending needs and remain dependent on central grants. State-level deficits will continue to “create headwinds” for the Centre and that narrows the Centre's window to roll out stimulus packages in times of slowdown, like now, when the quarterly GDP growth rate has hit 4.5%, falling for the seventh straight quarter.

STATE'S OWN-SOURCE REVENUE SHARE HAS DECLINED

<table>
<thead>
<tr>
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<th>FY 2013</th>
<th>FY 2020</th>
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</thead>
<tbody>
<tr>
<td>Own tax revenue</td>
<td>52</td>
<td>44</td>
</tr>
<tr>
<td>Own non-tax revenue</td>
<td>23</td>
<td>27</td>
</tr>
<tr>
<td>Shared taxes</td>
<td>15</td>
<td>10</td>
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<tr>
<td>Inter governmental transfer</td>
<td>10</td>
<td>8</td>
</tr>
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6.7% of GDP is estimated to be the general government deficit in FY 2019. The deficit at the central level is expected to be 3.7% with the proportion for the states at around 3%.

GST NOT HELPING YET

- Introduction of GST replaced many indirect taxes that were levied by the states. That reduced states' share of own source revenue in their total revenue
- As a result, states now rely on the Centre, or the GST Council, for a majority of their revenue. But below-expectation GST collections are not helping matters with the Centre promising to compensate states for any revenue shortfalls due to the GST for five years.

STATE REVENUE COLLECTIONS ARE SET TO SLOW DOWN...

- Estimates for fiscal 2020 suggest that states’ aggregate operating revenue growth is projected to slow to 10% year-on-year from 24% (revised estimates, fiscal 2019)
- The slowdown can be attributed to the mix of weaker growth in tax revenue, non-tax revenue and central transfers amid overall economic slowdown and below-expectation GST revenues

States’ revenue growth projected to weaken in fiscal 2020

AND THEIR BORROWINGS SET TO RISE

- Rs 7.5L Crore Expected borrowing by Indian states in fiscal 2020, a 28% increase over FY 2019 levels. It also represents 3.4% of national GDP
- Slowing revenue growth in fiscal 2020 will increase states’ needs for borrowing, especially to target infrastructure needs
- States’ debt continues to increase

Debt levels of states jumped to 180% of operating revenue in FY2017 from 168% in FY2016. While strong projected growth in revenue in FY2019 is set to lower the projected debt level to about 162% of operating revenue, this decline may be overestimated as revenue growth may be lower due to slowing economic growth

Source: Moody’s Investors Service