

STATE GOVERNMENT FINANCES

States' fiscal balances remain weaker than pre-Covid levels in Q1 FY2022, with milder recovery in revenues relative to rise in spending

September 2021





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19 state governments' revenue receipts in Q1 FY2022 were a mild 2.0% higher than Q1 FY2020

Their revenue expenditure in Q1 FY2022 increased by 14.1% relative to the pre-Covid level, whereas capital spending rose by a modest 2.6%

Combined fiscal deficit doubled in Q1 FY2022 from the pre-pandemic levels

SDL issuance increased, as did some states' usage of liquidity facilities

With a varied recovery in the revenues and expenditures of 19 state governments in Q1 FY2022, their combined fiscal balances have reported a deterioration relative to the pre-Covid level. While the revenue receipts rose by a mild 2.0% in Q1 FY2022 relative to Q1 FY2020, the revenue expenditure expanded by a sharper 14.1%. As a result, the combined revenue account position of the 19 states worsened to a deficit of Rs. 462 billion in Q1 FY2022 from a modest surplus of Rs. 57 billion in the pre-Covid period of Q1 FY2020. Moreover, the capital outlay exceeded the pre-Covid level by 2.6% in Q1 FY2022. With this, the fiscal deficit of the 19 states nearly doubled to Rs. 1.1 trillion in that period.

- **Revenues in Q1 FY2022 were a mild 2.0% higher than pre-Covid level, dampened by contraction in tax revenues:** The own tax revenues of 19 states in Q1 FY2022 (Rs. 2.3 trillion) remained 2.5% lower than the pre-pandemic level of Q1 FY2020 (Rs. 2.4 trillion). This was led by a sharp ~21% contraction in stamps and registration (S&R) collections in Q1 FY2022 relative to Q1 FY2020, despite attractive home loan rates, while excise duty collections were lower by a relatively muted 3.6%. Moreover, the devolution of taxes from the Government of India (GoI) to the states was a sharp ~20% lower in Q1 FY2022 relative to the pre-Covid level. The latter was offset by the front loading of the higher Finance Commission (FC) recommended grants by the GoI to the states in Q1 FY2022 relative to Q1 FY2020. Moreover, states' own non-tax revenues recorded a healthy 17.0% expansion in that period.
- **Expenditure in Q1 FY2022 was 12.8% higher than pre-Covid levels:** The combined revenue expenditure of the 19 state governments in Q1 FY2022 was ~14% higher than the pre pandemic level in Q1 FY2020 reflecting higher social sector spending in Q1 FY2022, amid the second wave of Covid-19. Moreover, with the permission to continue construction activities with some restrictions, their capital spending stood at Rs. 0.6 trillion in Q1 FY2022, modestly exceeding the pre-pandemic level of Q1 FY2020.
- **Fiscal balances in Q1 FY2022 were weaker than pre-Covid levels:** The combined revenue account balance of the 19 states slipped into a deficit of Rs. 0.5 trillion in Q1 FY2022, in contrast to the small surplus of Rs. 0.1 trillion in Q1 FY2020. Moreover, their fiscal deficit nearly doubled to Rs. 1.1 trillion in Q1 FY2022 from Rs. 0.6 trillion in Q1 FY2020. With this, the issuance of state development loans (SDLs) increased sharply to Rs. 1.4 trillion in Q1 FY2022 from Rs. 0.8 trillion in Q1 FY2020. Moreover, some states' usage of the Reserve Bank of India's (RBI's) liquidity facilities recorded a rise in the just-concluded quarter, relative to the pre-Covid period.

Revenue receipts expanded by 30.2% YoY in Q1 FY2022, but exceeded pre-Covid levels by mild 2.0%

Exhibit: Revenue receipts in Q1 during FY2020-22

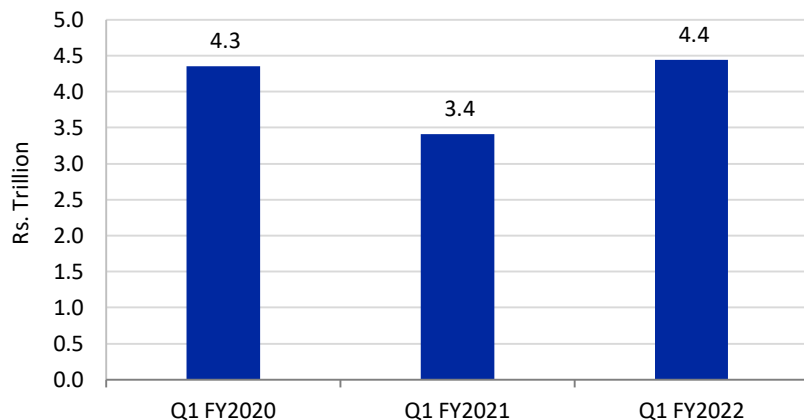
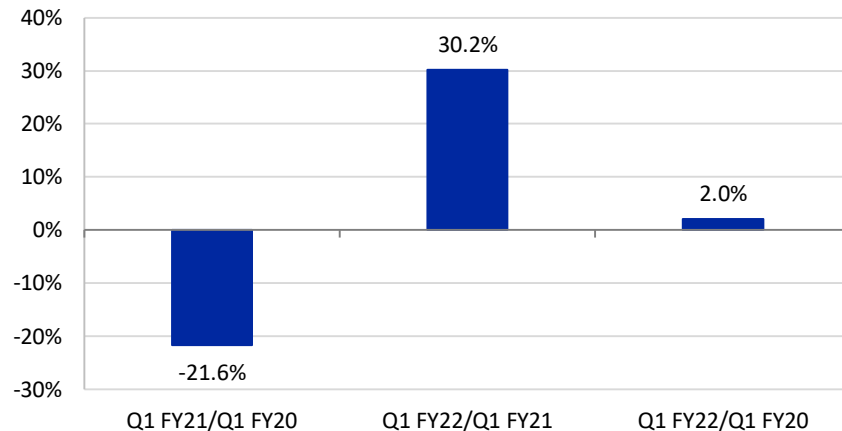


Exhibit: Growth performance of revenue receipts in Q1 during FY2021-22



- Despite the onset of the second wave of Covid-19, the combined revenue receipts of the 19 states* increased by a sharp 30.2% in Q1 FY2022 on a YoY basis to Rs. 4.4 trillion.
- This benefitted from the low base of Q1 FY2021 (-21.6%; Rs. 3.4 trillion), when the country was in a restrictive nation-wide lockdown for much of the quarter.
- However, the states' combined revenue receipts in Q1 FY2022 were only 2.0% higher than the pre-Covid level of Rs. 4.3 trillion in Q1 FY2020, led by non-tax revenues.

Note: * Unaudited provisional actuals for Q1 FY2022 is available for 19 Indian states, except Andhra Pradesh, Arunachal Pradesh, Assam, Bihar, Goa, Manipur, Meghalaya, Mizoram and West Bengal, from the Comptroller and Auditor General (CAG).

Source: CAG; ICRA research

Components of revenues displayed a divergent trend; tax revenues trailed while non-tax revenues exceeded pre-Covid levels

Exhibit: Trends of sub-components of revenue receipts during Q1 FY2020-22

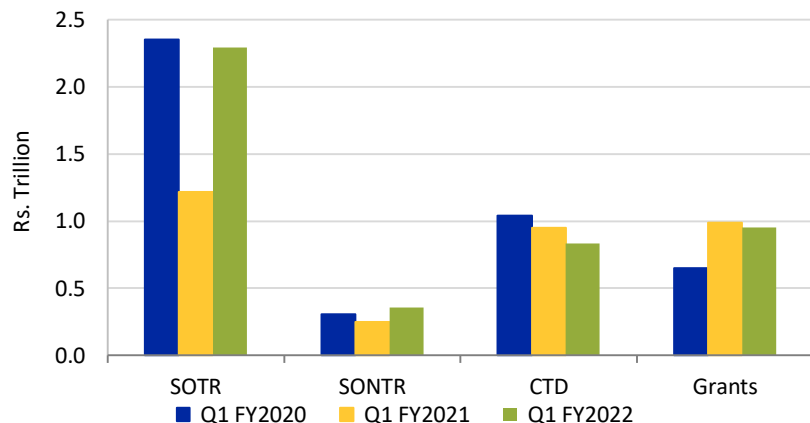
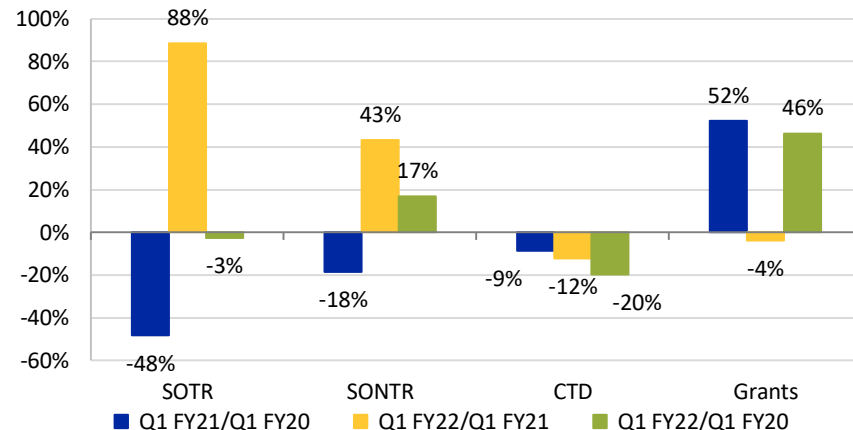


Exhibit: Growth performance of sub-components of revenue receipts during Q1 FY21-22



- State own tax revenues (SOTR) expanded sharply in Q1 FY2022 on a low base, while trailing the pre-Covid levels by ~3%, on account of the impact of the second wave of Covid-19 on stamps and registrations, and excise duty collections.
- Central tax devolution (CTD) declined from Rs. 1,042 billion in Q1 FY2020 to Rs. 952 billion in Q1 FY2021, and further to Rs. 836 billion in Q1 FY2022 (~20% lower than pre-Covid level).
- On a positive note, state own non-tax revenues (SONTR) in Q1 FY2022 were ~43% higher than Q1 FY2021, and ~17% higher than Q1 FY2020.
- Grants in Q1 FY2022 were 4% lower than Q1 FY2021 on a high base, while exceeding the pre-Covid level by a sharp ~46%.

S&R collections in Q1 FY2022 were a sharp ~21% lower than the pre-Covid level despite attractive home-loan rates

Exhibit: S&R collections during Q1 FY2020-22

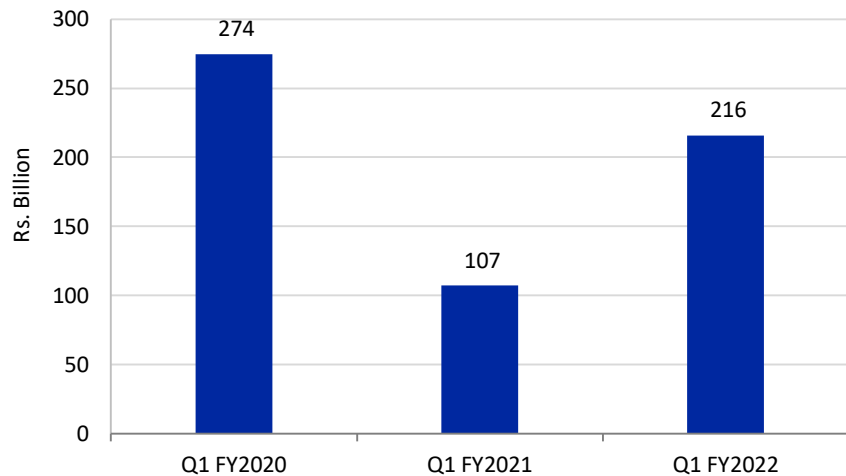
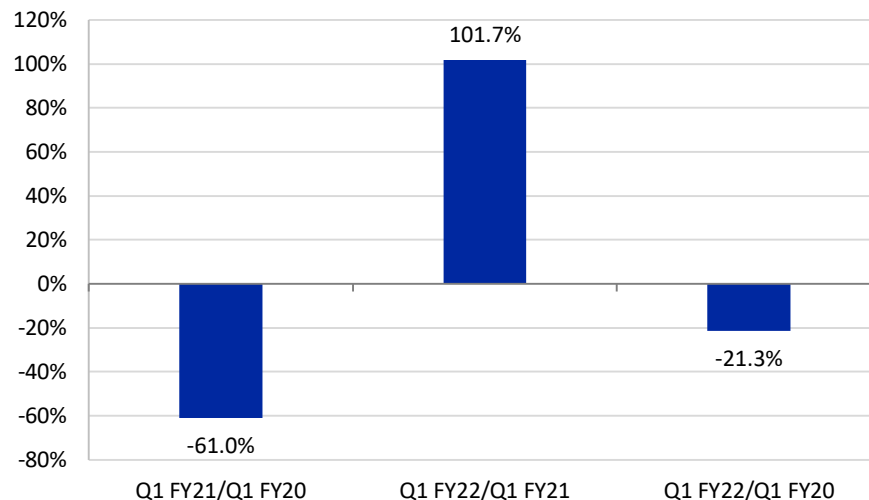


Exhibit: Growth performance of S&R collections during Q1 FY2021-22



- Reflecting the stringent nation-wide lockdown, the combined S&R collections of the 19 state governments had contracted by 61.0% in Q1 FY2021.
- Led by the low base, and benefitting from attractive home loan rates and cut in stamp duty rates by some of the states in the sample, S&R collections expanded by a sharp 101.7% to Rs. 216 billion in Q1 FY2022 from Rs. 107 billion in Q1 FY2021.
- However, the combined S&R collections of the 19 states remained a substantial 21.3% lower than the pre-Covid level of Rs. 274 billion in Q1 FY2020.

Despite higher tax rates/prices, excise duty collections in Q1 FY2022 trailed pre-Covid level by ~4% reflecting lower consumption amid localised restrictions

Exhibit: Excise duty collections during Q1 FY2020-22

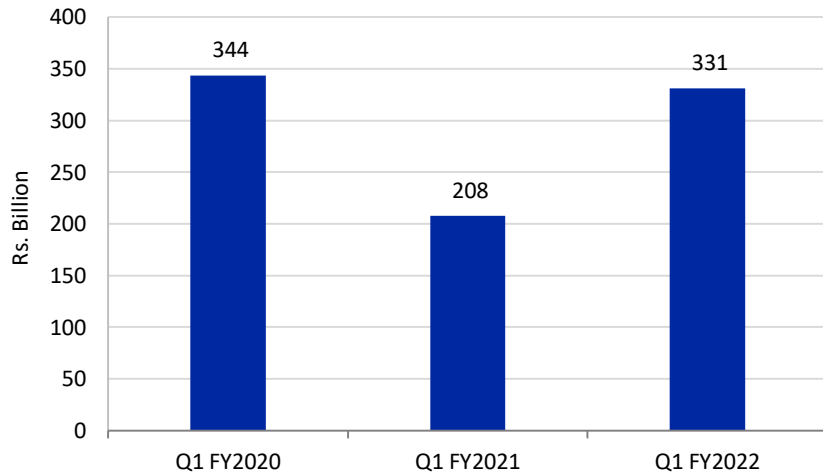
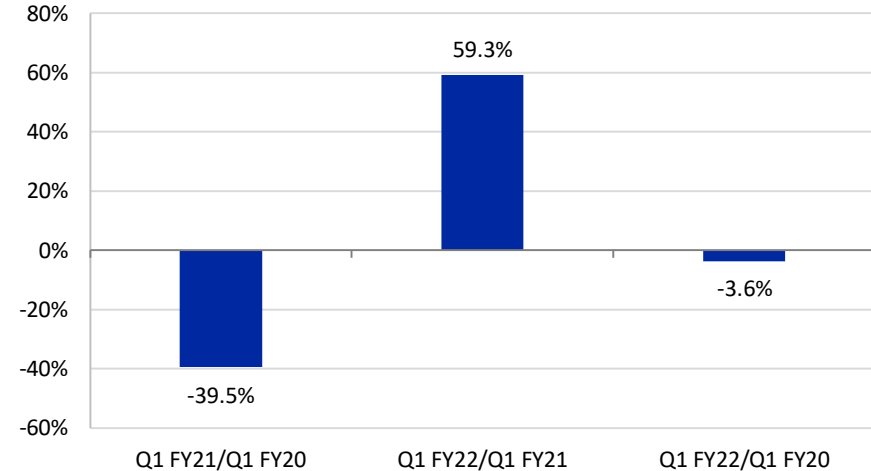


Exhibit: Growth performance of excise duty collections during Q1 FY2021-22



- Excise duty collections had recorded a ~40% contraction in Q1 FY2021, amid the nation-wide lockdown.
- 14 of the 19 state governments in our sample had increased the rate of excise duty on liquor consumed in their state from June FY2021 onward.
- Benefitting from this, the combined excise duty collections rose by 59.3% to Rs. 331 billion in Q1 FY2022 from Rs. 208 billion in Q1 FY2021.
- However, excise duty collections in Q1 FY2022 were a mild 3.6% lower than the Rs. 344 billion collected in Q1 FY2020, with the localised restrictions dampening consumption in the first quarter of the ongoing fiscal.

SGST collections in Q1 FY2022 recovered to pre-Covid level

Exhibit: SGST collections during Q1 FY2020-22

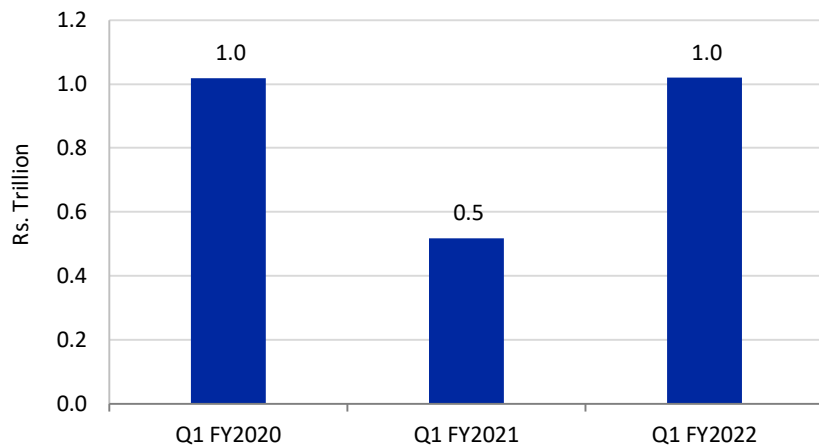
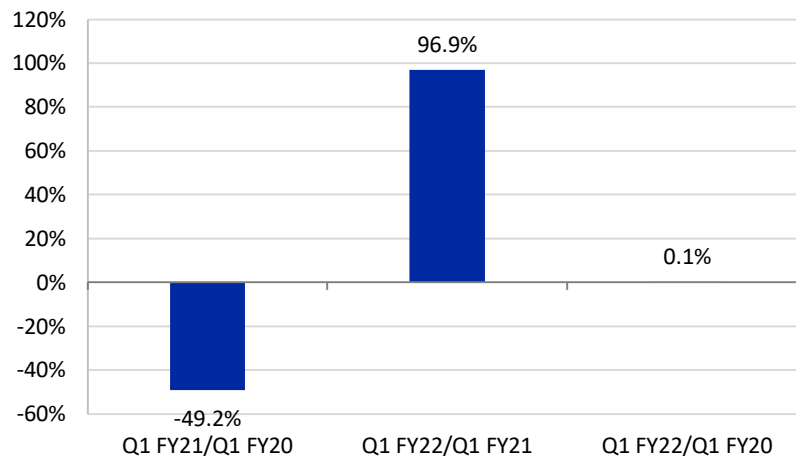


Exhibit: Growth performance of SGST collections during Q1 FY2021-22



- Following the contraction in Q1 FY2020 and Q1 FY2021, SGST collections nearly doubled in Q1 FY2022 on a YoY basis, and recovered to the level recorded in Q1 FY2020.
- With a deepening economic recovery, ICRA expects state goods and tax (SGST) collections in the remaining portion of the ongoing fiscal to display a moderate growth relative to FY2020, provided a third wave of Covid-19 does not hit the country.
- Assuming monthly headline GST collections at Rs. 1.2 trillion for Sept-Feb FY2022 and Rs. 1.3 trillion for March FY2022, ICRA estimates the total GST collections at Rs. 14.2 trillion, nearly 25% higher than the level in FY2021 (Rs. 11.4 trillion) and ~16% higher than FY2020 (Rs. 12.2 trillion).

Headline GST collections during Apr-Aug FY2022 surpassed pre-Covid levels by ~10%

Exhibit: Monthly headline GST collections during Apr-Aug FY2020-22

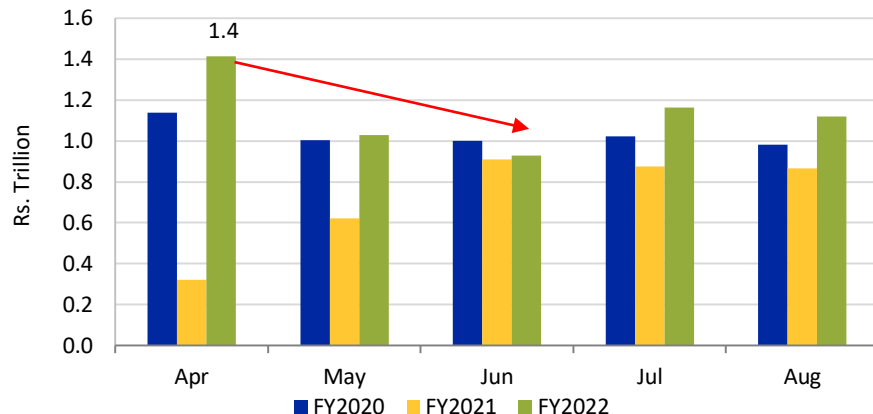
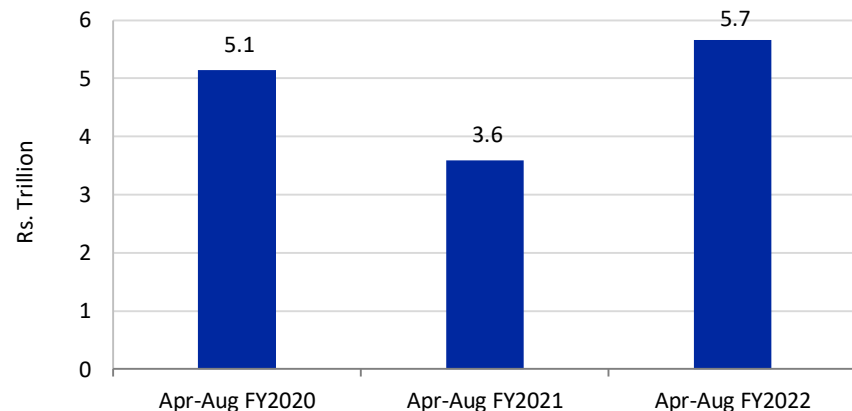


Exhibit: Headline GST collections during Apr-Aug FY2020-22



- The headline GST collections had contracted by 41.0% in Q1 FY2021, reflecting the adverse impact of the nationwide lockdown on consumption as well as the relaxation for filing GST returns in that quarter.
- GST collections related to a particular month become a part of the state governments' revenues in the subsequent month. Accordingly, the record-high headline GST collections of Rs. 1.4 trillion reported in April 2021, which reflected healthy economic activity in March 2021, boosted the SGST collections in the current year.
- The spread of the Covid-19 infections in several parts of the country during April-May 2021, led to localised restrictions in those months. Accordingly, the May 2021 and June 2021 GST collections declined sharply on a sequential basis to Rs. 1.0 trillion and Rs. 0.9 trillion, respectively, from Rs. 1.4 trillion in April 2021.
- However, with the gradual unlocking and improved mobility, GST collections for July and August 2021 stood at a healthy Rs. 1.2 trillion and Rs. 1.1 trillion, respectively, higher than the collections in July-Aug in the previous two years.
- Overall, the headline GST collections for the first five months of this fiscal stand at Rs. 5.7 trillion, exceeding the pre-Covid level by nearly 10% (Rs. 5.1 trillion)

Sales tax collections in Q1 FY2022 were nearly twice as high as Q1 FY2021, and ~11% higher than pre-Covid level

Exhibit: Sales tax collections during Q1 FY2020-22

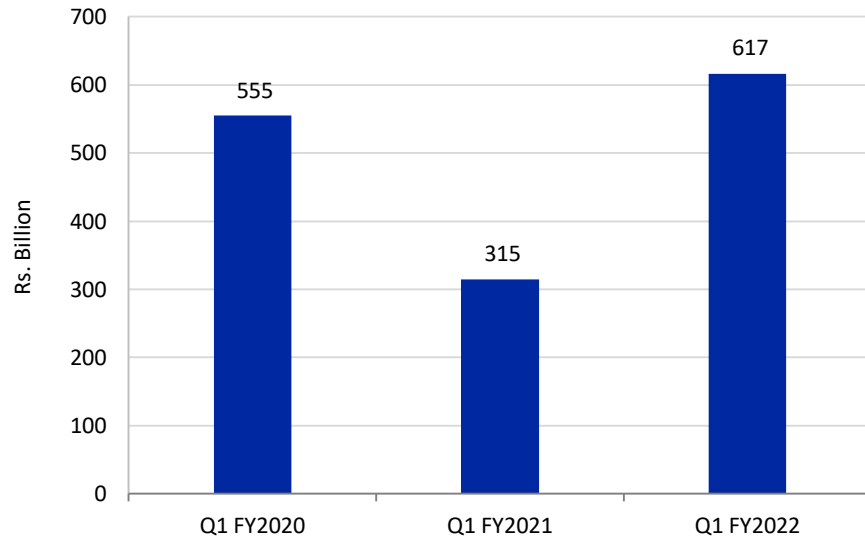
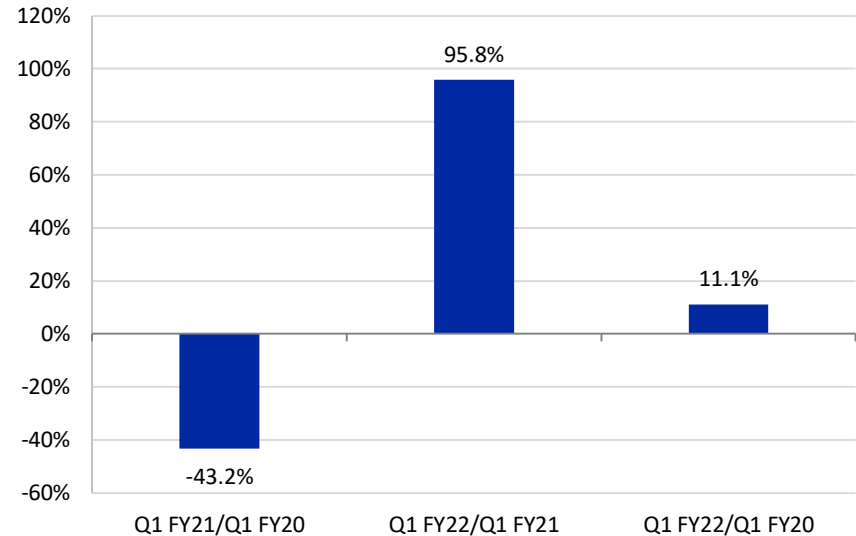


Exhibit: Growth performance of sales tax collections during Q1 FY2021-22



- The combined sales tax collections of the 19 states nearly doubled to Rs. 617 billion in Q1 FY2022 from Rs. 315 billion in Q1 FY2021 and were ~11% higher than the pre-Covid level of Rs. 555 billion in Q1 FY2020.
- Sales tax collections had contracted by a sharp 43.2% in Q1 FY2021, on account of a substantial dip in consumption of fuels as a result of the nation-wide lockdown implemented in that quarter.
- Reflecting higher prices and consumption of fuels in Q1 FY2022 relative to Q1 FY2021, the combined sales tax collections of the 19 state governments expanded by 95.8% in the just-concluded quarter.

Sales tax collections in Q1 FY2022 benefitted from higher retail prices of fuels

Exhibit: Average retail selling price (RSP) of petrol and diesel during Q1 FY20-22

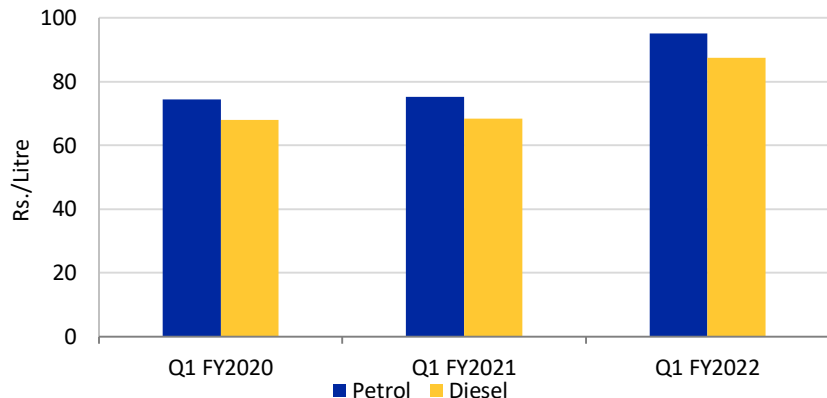
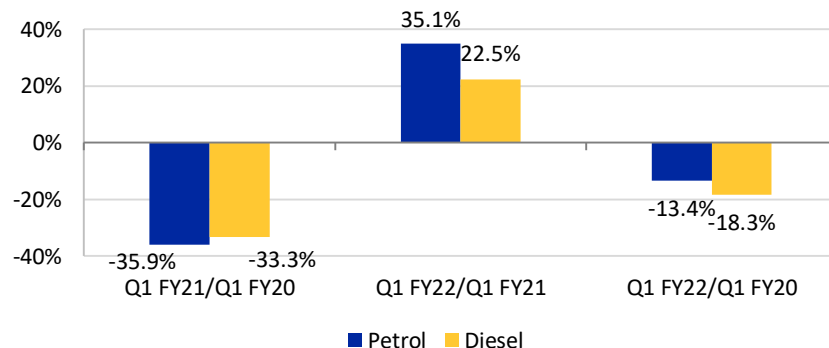


Exhibit: Growth performance of consumption of petrol and diesel during Q1 FY2021-22



- A rise in crude oil prices since mid-2020 has boosted retail prices of fuels in India. Moreover, 14 of the 19 state governments had increased the rate of sales tax/value added tax (VAT) levied on petroleum products in FY2021. Accordingly, the average RSP of petrol and diesel in metro cities during Q1 FY2022 exceeded the level in Q1 FY2021 by Rs. 19.8/litre and Rs. 19.1/litre, respectively.
- While the pan-India consumption of petrol and diesel in Q1 FY2022 increased by 35.1% and 22.5%, respectively, on the low base of Q1 FY2021, it was 13.4% and 18.3% lower than the consumption in Q1 FY2020, respectively.
- Subsequently, petrol and diesel consumption increased by 16.4% and 11.5% respectively, on a YoY basis in July 2021; diesel consumption remained 10.2% lower than the pre-Covid level of July 2019 and petrol consumption exceeded the pre-Covid level by 4.2%. Monthly RSP for petrol surpassed Rs. 100/litre in July-Aug 2021, whereas that for diesel averaged Rs. 93.4/litre in the same period.
- ICRA expects the increase in RSPs of these fuels (Indian basket of crude oil expected to average US\$72/barrel in FY2022 compared to US\$44.5/barrel in FY2021) and improved mobility and fuel consumption to boost the sales tax collections for the states during FY2022.

CTD to 19 states contracted by ~12% in Q1 FY2022, despite budgeted growth in tax devolution

Exhibit: CTD to 19 states during Q1 FY2020-22

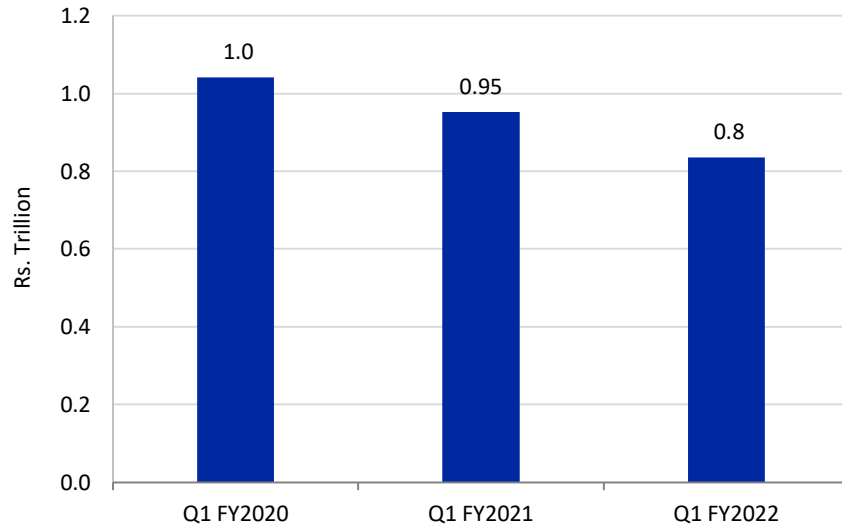
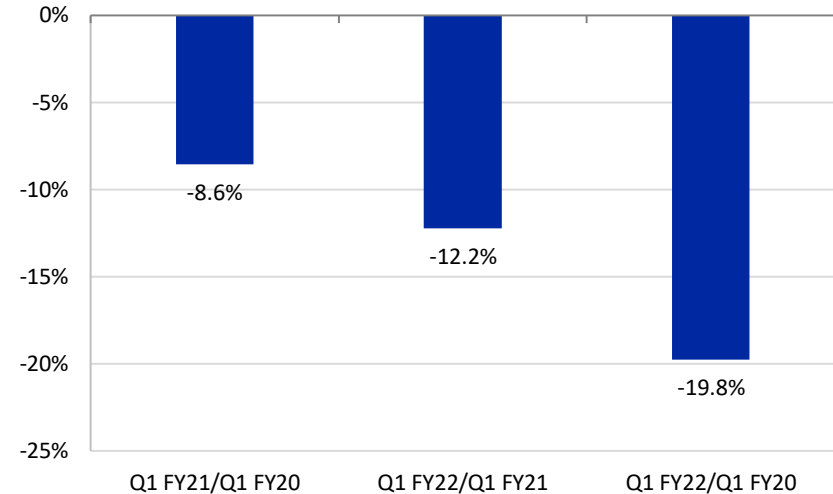


Exhibit: Growth performance of CTD to 19 states during Q1 FY2021-22



- Based on the inter-se of the 19 state governments, ICRA estimates the share of these states in the aggregate CTD of Q1 FY2021 at Rs. 0.8 trillion, 12.2% lower than ~Rs. 952 billion in Q1 FY2021 and nearly 20% lower than Rs. 1.0 trillion in Q1 FY2020.
- The CTD to all states included in the Gol's BE for FY2022 (Rs. 6.7 trillion) is 15.1% lower than that was budgeted for FY2021 (Rs. 7.8 trillion), although it exceeds the FY2021 Provisional Estimates of Rs. 6.0 trillion by 11.9%.

Step up in devolution amount in July 2021 augurs well for state cash flows

Exhibit: Tax devolution to all states

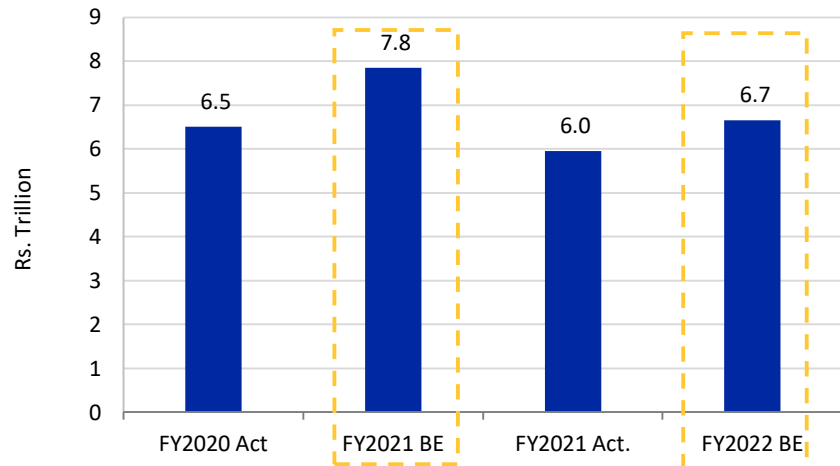
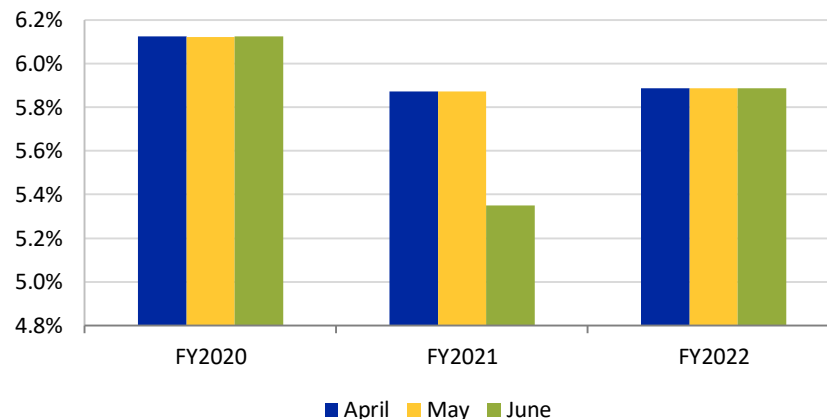


Exhibit: Monthly tax devolution as a proportion of BE of that year



- The GoI released 5.9% of the budgeted tax devolution each month to the state governments in April-May FY2021 and Q1 FY2022, which contributed to the contraction in devolution of taxes to all states by ~12% in Q1 FY2022 on a YoY basis.
- ICRA estimates that the budgeted gross tax revenues (Rs. 22.2 trillion) for FY2022 can be achieved even with a 7.5% contraction during August –March FY2022, which appears unlikely with a deepening of the economic recovery in the ongoing quarter. Accordingly, the budgeted tax devolution of Rs. 6.7 trillion to all states for FY2022, appears to be realistic.
- **The GoI subsequently stepped-up the devolution to states to Rs. 475 billion (7.1% of FY2022 BE) in July 2021 from Rs. 392 billion (5.9% of FY2022 BE) each in the previous three months. If the monthly devolution continues at Rs. 475 billion until February 2022, it will reduce the back-ending of such transfers.**

Grants from the Centre in Q1 FY2022 were sharply higher than the pre-Covid level led by front loading of Finance Commission grants

Exhibit: Grants from the Centre to 19 states during Q1 FY2020-22

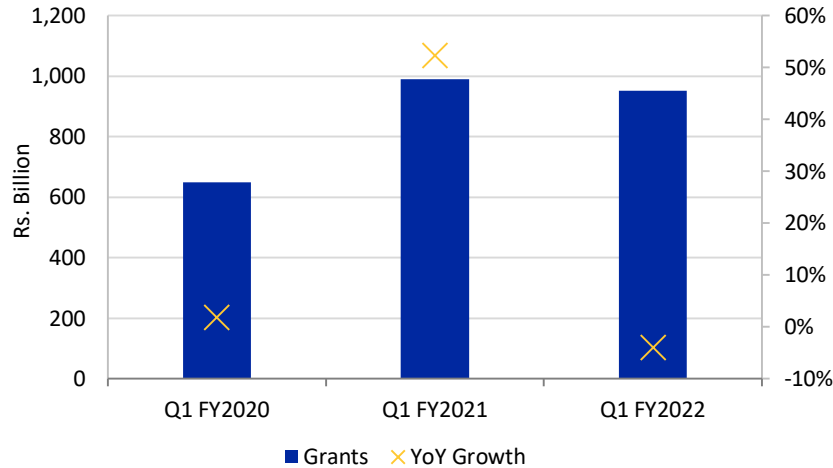
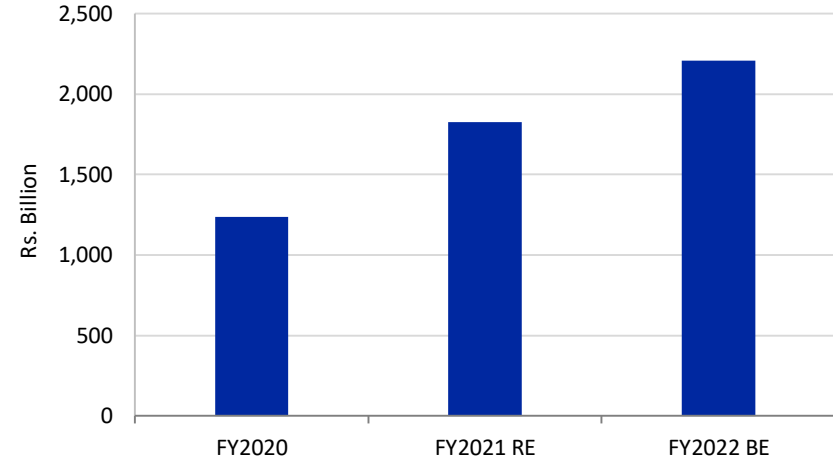


Exhibit: FC grants from the Centre to all states during FY2020-22 BE



- Grants from the Centre to the states include scheme related grants (centrally sponsored plan schemes), FC-recommended grants (grants to local bodies, revenue deficit grants and grants for state disaster response funds) and other transfers including GST compensation.
- Grants from the Centre to the 19 state governments eased to Rs. 951 billion in Q1 FY2022 from Rs. 990 billion in Q1 FY2021.
- However, they were a substantial 46.3% higher than the pre-Covid level of Rs. 650 billion in Q1 FY2020, on account of front-loading of the FC-recommended grants in Q1 FY2022, which includes a higher monthly quantum of revenue deficit grants compared to FY2020.**

Revenue expenditure in Q1 FY2022 increased by ~11% on a YoY basis and ~14% relative to the pre-Covid level

Exhibit: Revenue expenditure during Q1 FY2020-22

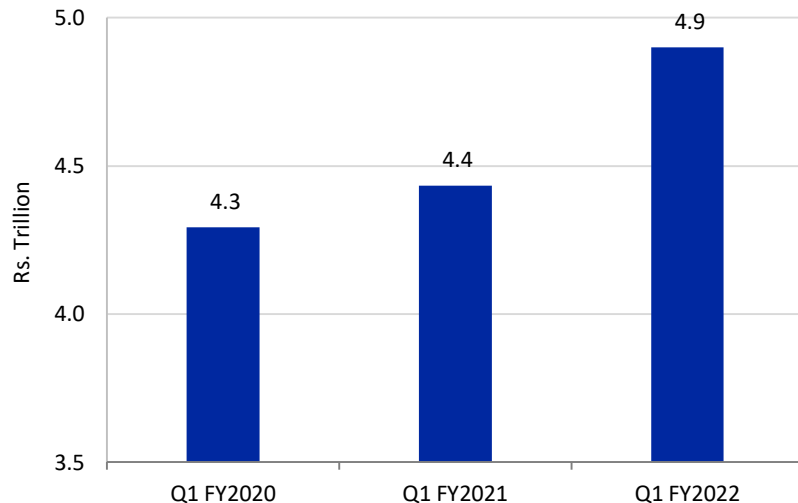
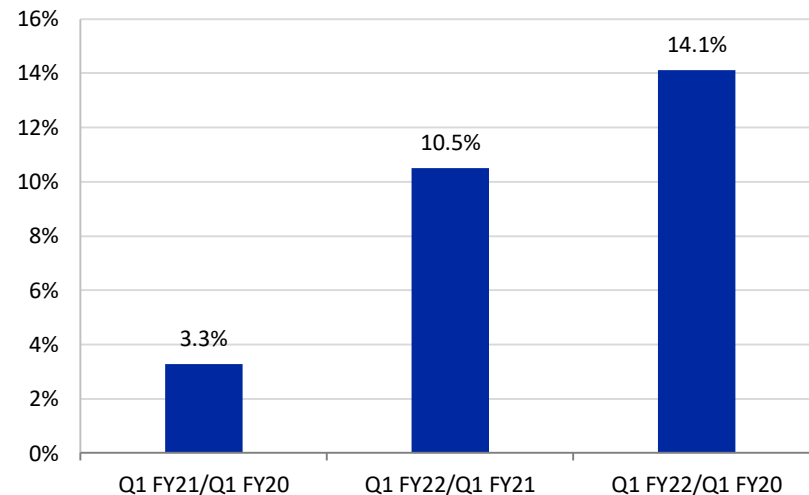


Exhibit: Growth performance of revenue expenditure in Q1 during FY2021-22



- Pace of growth of revenue spending rose to a moderate 10.5% in Q1 FY2022 from 3.3% in Q1 FY2021.
- Revenue spending of the 19 state governments increased to Rs. 4.9 trillion in Q1 FY2022 from Rs. 4.4 trillion in Q1 FY2021, with the latter having been somewhat constrained by lower demand for Government services during the nation-wide lockdown.
- Moreover, the revenue spending of the sample was nearly 14% higher than the pre-Covid level of Rs. 4.3 trillion in Q1 FY2020, possibly reflecting higher social sector spending in Q1 FY2022, amid the second wave of Covid-19.

Capital spending in Q1 FY2022 recovered and mildly exceeded pre-Covid level

Exhibit: Capital outlay during Q1 FY2020-22

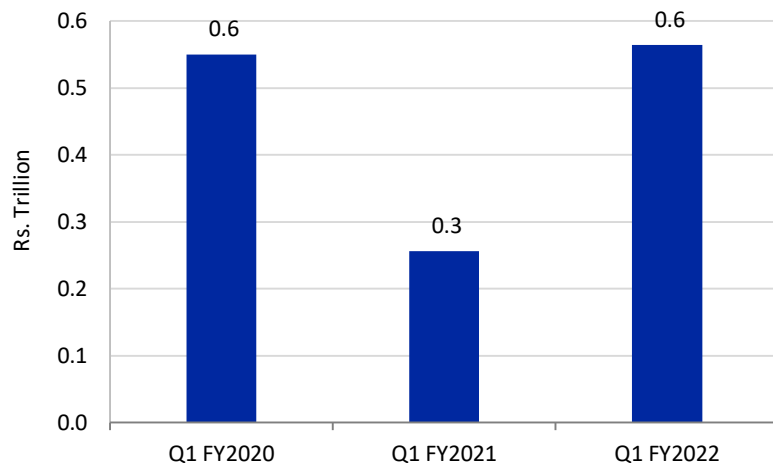
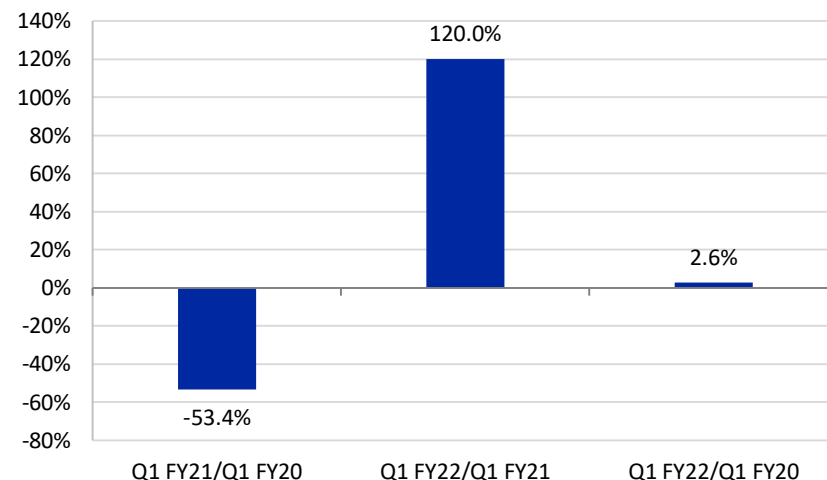


Exhibit: Growth performance of capital outlay in Q1 during FY2021-22



- On account of the adverse impact of the nationwide lockdown on revenue collections as well as the ongoing restrictions, capital spending by the 19 state governments had contracted by 53.4% to Rs. 0.3 trillion in Q1 FY2021 from Rs. 0.6 trillion in Q1 FY2020.
- However, given the relatively healthy revenue position as well as permission to continue construction activities with some restrictions, the capital spending by the 19 state governments doubled to Rs. 0.6 trillion in Q1 FY2022, exceeding the pre-pandemic level of Q1 FY2020 by 2.6%.

Notwithstanding the YoY improvement, fiscal balances in Q1 FY2022 were weaker than the pre-Covid level

Exhibit: Revenue balance during Q1 FY2020-22

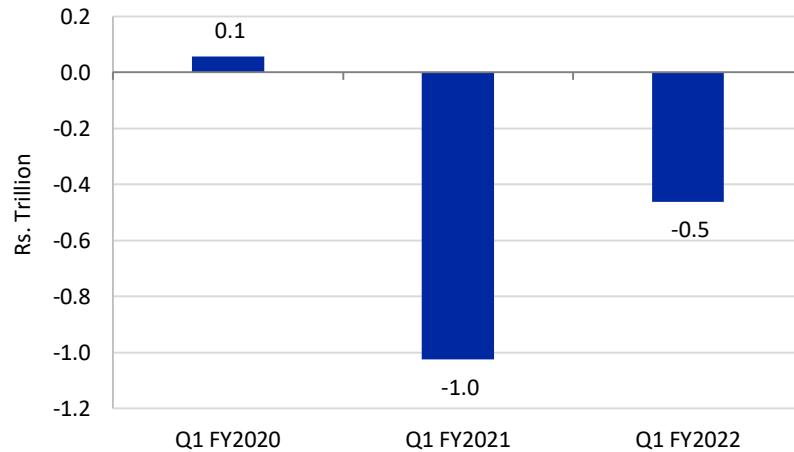
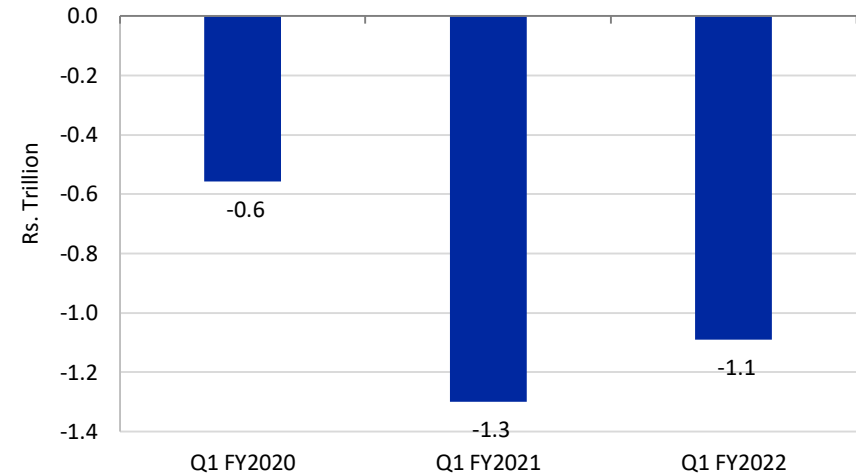


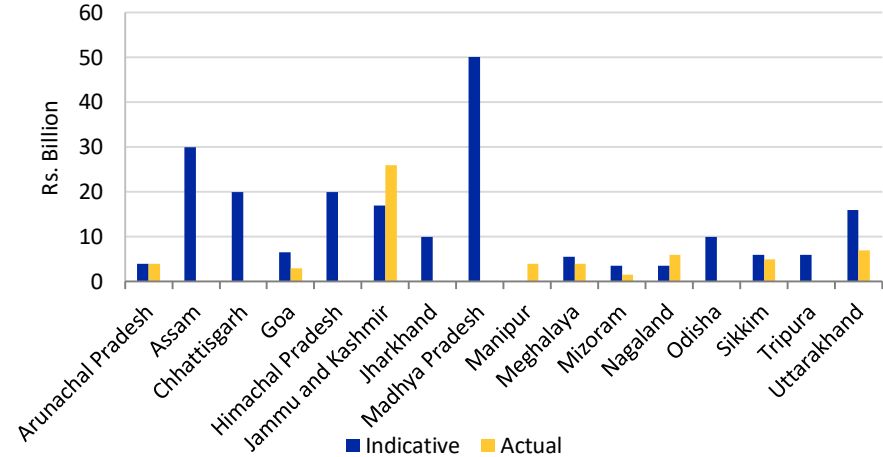
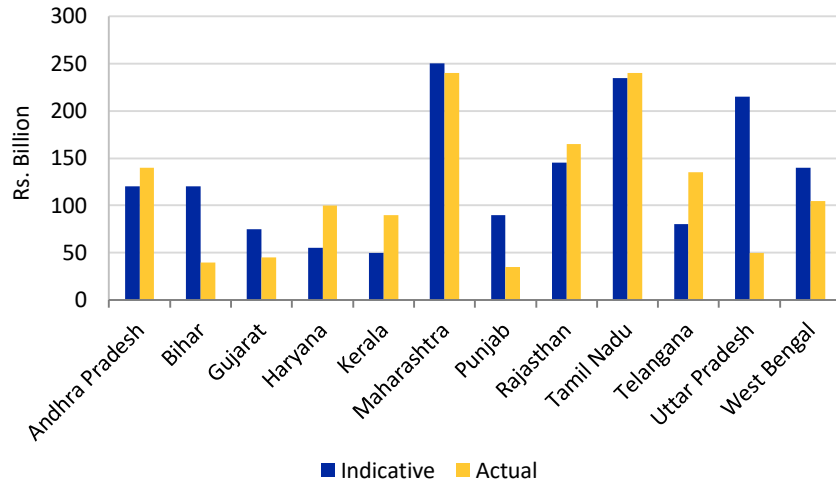
Exhibit: Fiscal balance during Q1 FY2020-22



- With a relatively higher incremental increase in revenue receipts (by Rs. 1.0 trillion) compared to revenue expenditure (by Rs. 0.5 trillion) in Q1 FY2022 relative to Q1 FY2021, the combined revenue deficit of the 19 states halved to Rs. 0.5 trillion in that quarter from Rs. 1.0 trillion in Q1 FY2021. Moreover, their combined fiscal deficit declined modestly to Rs. 1.1 trillion in Q1 FY2022 from Rs. 1.3 trillion in Q1 FY2021, while remaining large.
- However, their revenue balance has slipped into a deficit in Q1 FY2022, in contrast to the small surplus in Q1 FY2020, partly on account of the increase in pandemic-related spending. Moreover, the fiscal deficit of the 19 states has nearly doubled in Q1 FY2022 compared to the pre-Covid level of Rs. 0.6 trillion in Q1 FY2020.

SDL issuance in Q1 FY2022 was lower than indicated as well as year-ago level, while sharply exceeding Q1 FY2020

Exhibit: Indicative and actual SDL issuance in Q1 FY2022



- 21 state governments/UT raised Rs. 1.4 trillion SDLs in Q1 FY2022, nearly 19% lower than the indicated level of Rs. 1.8 trillion for that period. However, a few states, such as Andhra Pradesh (by Rs. 20 billion), Haryana (by Rs. 45 billion), Kerala (by Rs. 40 billion), Rajasthan (by Rs. 20 billion) and Telangana (by Rs. 55 billion) borrowed a larger amount than what they had originally indicated for Q1 FY2022.
- Moreover, the issuance declined by 13.6% on a YoY basis (Rs. 1.7 trillion). This benefitted from the YoY decline in the fiscal deficit, as well as improved cash flow situation following the unexpected devolution of Rs. 450 billion at end-March 2021.
- However, the issuance of SDLs increased by a sharp 77.3% to Rs. 1.4 trillion in Q1 FY2022 from Rs. 0.8 trillion in Q1 FY2020.**

Some states stepped up their usage of financial accommodation from the RBI in Q1 FY2022

Exhibit: Number of states/Union Territories (UTs) availing financial accommodation from RBI

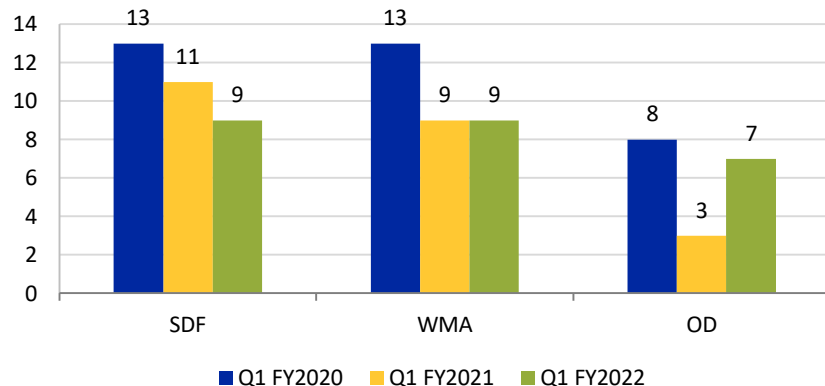
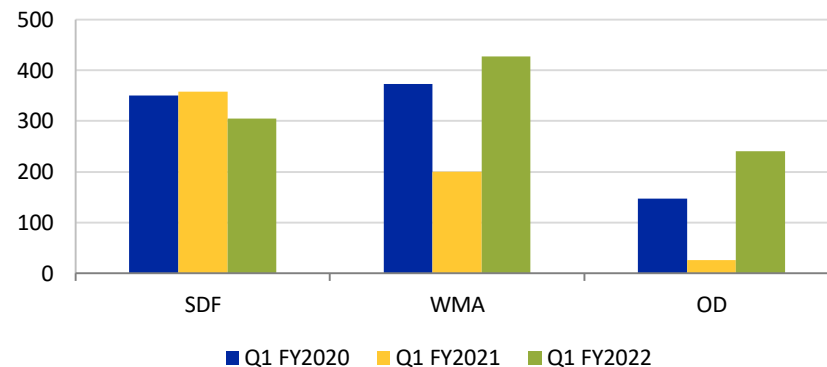


Exhibit: Number of days financial accommodation was availed from RBI by state governments/UTs



- The RBI provides financial accommodation to the states/UTs in the form of special drawing facility (SDF), ways and means advances (WMA) and overdraft (OD) for overcoming temporary mismatches in their receipts and payments.
- Usage of WMA and OD facilities had reduced in Q1 FY2021 from Q1 FY2020, possibly reflecting the lower spending and near doubling of SDL issuance in the first quarter of the last fiscal.
- Although the number of states/UT availing WMA remained stable at nine, the combined number of days for which these states availed WMA more than doubled to 427 in Q1 FY2022 from 200 in Q1 FY2021. Moreover, the number of days the states/UT availed WMA also increased from 373 in Q1 FY2020.
- In addition, the number of states/UT availing OD rose to seven in Q1 FY2022 from three in Q1 FY2021, and the number of days for which these states were in OD also increased sharply to 240 from 26 during the same period. The number of days the states/UT were in OD was also higher compared to the pre-Covid level of FY2020 (147 days).
- Andhra Pradesh, Telangana, Manipur, Mizoram and Nagaland were some of the states, which substantially increased their frequency of availing WMA and OD in Q1 FY2022.



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