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## An Examination of the Fiscal Policy's Impact on India's Economic Growth: A Quantitative Analysis from 2014 to 2023

ORIGINAL ARTICLE



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### Abstract

*This paper undertakes a quantitative analysis to examine the impact of fiscal policy on India's economic growth from 2014 to 2023. The study employs econometric techniques to investigate the relationship between Government expenditures and revenues, and their subsequent effects on key macroeconomic variables such as GDP, inflation, and employment.*

### Key Words

*Fiscal Policy, Economic Growth, India Economy, GDP Growth.*

### Introduction

Fiscal policy has long been recognized as a crucial tool for Governments worldwide in shaping their economies. In recent years, India has implemented various fiscal policies aimed at stimulating its sluggish economy. In contemporary times, Government

expenditures serve as a crucial tool for regulating the flow of finances within an economy, shaping demand and supply patterns, implementing various developmental initiatives, and executing social, economic, and political policies. This fundamental component is akin to fuel, without which the engine of economic growth would stall.

The systematic examination of Government expenditures at the national, provincial, or municipal levels constitutes the discipline known as Government expenditure analysis. By definition, "expenditure" refers to the measurable allocation of resources, whether in monetary or non-monetary forms. Consequently, Government expenditure encompasses the pecuniary outlays made by central, state, or local Governments.

As a subfield of public finance, Government expenditure research focuses on optimizing the utilization of both cash and in-kind resources to facilitate the effective execution of Governmental objectives.

The overall prosperity of a nation is significantly impacted by the magnitude of Government expenditures. As a key aspect of a Government's budget, Government expenditure plays a pivotal role in evaluating the well-being of citizens and serves as a vital instrument for maximizing public satisfaction.

### Literature Review

According to empirical evidence presented by Md.Rahman et al. (2023), Government expenditures have a significant and positive effect on Gross Domestic Product (GDP) within the South Asian Association for Regional Cooperation (SAARC) region. Furthermore, the study reveals a lasting correlation between Government expenditures and economic growth in these nations. The analysis indicates a one-way

causal link between GDP and Government expenditures within the SAARC region, suggesting that augmenting Government expenditures would lead to a corresponding increase in GDP, while reductions in Government expenditures would result in a decrease in GDP. Consequently, it is recommended that increased Government expenditures could potentially stimulate economic growth in the selected SAARC countries.

**According to Smitha Nayak et al.'s 2021** publication, Government expenditures have a direct correlation with economic growth and serve as the primary catalyst for national development worldwide. Following India's post-liberalization period, the country has become increasingly integrated into the global economy, resulting in a substantial influence of Governmental outlays on its economic expansion. Notably, sustained economic growth assumes paramount importance for a nation's long-term prosperity, particularly in the context of emerging economies.

**In contrast, Srivastava's research (2015)** focuses on the influence of educational expenditures on the economic development of the northern Indian states during the three-year period from 2008 to 2011. The investigation considers several variables, including the number of employed primary teachers, funding allocations for school activities, and the dependent variable, GDP. Employing co-integration modelling and error correction models, the findings indicate that the effects of education sector expenditures on economic growth vary across the northern states.

**A recent research endeavour by Srinivasan (2013)** investigates the correlation between public expenditures and economic growth in India. The analysis focuses on two primary variables: public expenditures and Gross Domestic Product (GDP), which serves as a proxy for economic growth. To examine these relationships, the researcher employs a combination of methodologies, including Johansen's integration approach, the Vector Error Correction Model, and the Augmented Dickey-Fuller test to determine stationarity. The findings indicate a unidirectional causal link from economic growth to public expenditures, thereby substantiating Wagner's Law and establishing a long-term association between public expenditures and economic growth in India.

**A recent study by Gangal and Gupta (2013)** examines the correlation between public expenditures and economic growth in India over the period from 1998 to 2012. The researchers aim to demonstrate that these two factors are independent entities. To achieve this goal, they employ two key indicators: Total Public Expenditure (TPE) and Gross Domestic Product (GDP). Analysis of the Impulse Response Function (IRF) reveals a positive association between GDP and TPE, while the Granger Causality Test suggests that public expenditures have a stimulatory effect on economic growth.

A subsequent paper published by **Wu et al. in 2010** analysed a broader sample size and longer timeframe, reassessing the causal link between public spending and economic development. Notwithstanding variations in how Government spending and economic growth were quantified, the outcomes consistently substantiated Wagner's Law and the theoretical notion that Government expenditures contribute positively to economic growth.

## **The Fiscal Framework of the Government of India: A Comprehensive Overview**

The Government of India, being one of the largest economies in the world, relies heavily on a diverse range of sources to generate its revenue. Simultaneously, it also incurs significant expenditures to fulfil its constitutional obligations, provide public goods and services, and promote economic growth. In this article, we will delve into the various sources of revenue and expenditure of the Government of India, shedding light on the fiscal framework that underpins its financial operations.

### **A. Sources of Revenue**

The Government of India derives its revenue from multiple sources, which can be broadly categorized into three main segments:

- i. Taxation:** The Indian Government's primary source of revenue is taxation, which accounts for

approximately 80% of its total receipts. This includes income tax, corporate tax, wealth tax, and other taxes levied on individuals and corporations.

- ii. **Non-Tax Revenue:** Non-tax revenues comprise a significant portion of the Government's overall revenue. These include dividends received from public sector undertakings (PSUs), interest earned on deposits with RBI, and proceeds from disinvestment of PSUs.
- iii. **Grants-in-Aid:** Grants-in-aid refer to transfers made by the Central Government to State Governments, local bodies, and autonomous institutions. These grants are used to support specific programs and schemes aimed at promoting social welfare, infrastructure development, and rural upliftment.

## **B. Expenditure Patterns**

Public expenditures, alternatively referred to as Government outlays, encompass the financial contributions made by the central Government, local authorities, and state Governments towards various national endeavours. Notably, the central Government bears the primary responsibility for these disbursements. As of 2019, the Indian Government's total spending exceeded 59 trillion rupees, projected to rise to over 95 trillion rupees by 2025. A significant portion of this allocation, exceeding one-quarter, pertains to interest payments, while approximately one-tenth is dedicated to defence expenditures.

Indian Government Expenditures can be categorized into four distinct segments:

- i. **Development Services:** These expenditures focus on enhancing the nation's socioeconomic infrastructure, human capital, and economic development through investments in education, healthcare, transportation, and other vital sectors.
- ii. **Debt Services:** A substantial proportion of Government expenses involves servicing debt obligations incurred to finance specific initiatives or projects. This encompasses interest payments on borrowed funds.
- iii. **Administrative Services:** This category comprises expenditures related to maintaining essential civic functions, including law enforcement, taxation, and pension schemes.
- iv. **Defence Services:** Defence-related expenditures constitute around 10% of the central Government's overall revenue expenditure.

The primary sources of revenue for the Indian Government comprise Goods and Services Tax (GST) and income tax, collectively accounting for nearly 90% of the Government's overall revenue. Specifically, GST contributed approximately 57% of total tax revenue during the fiscal year 2021-22. Public expenditures refer to the Government's allocations aimed at ensuring the upkeep and welfare of the broader society. In 2019, the Indian Government disbursed more than 59 trillion rupees. This overview provides insight into the key revenue streams and expenditures of the Indian Government.

## **The Crucial Role of Government Spending in Fostering Economic Growth**

In today's complex and interconnected global economy, Governments play a vital role in promoting economic growth through strategic spending decisions. Effective Government spending can stimulate economic activity, create jobs, and drive innovation, ultimately leading to increased prosperity for citizens. This article will explore key areas where Government spending fosters economic growth.

- i. **Infrastructure Development:** Investment in infrastructure is a cornerstone of Government spending that has a direct impact on economic growth. Roads, bridges, airports, and seaports are essential components of a nation's transportation network, facilitating the movement of goods and services. By investing in these critical assets, Governments enable businesses to operate efficiently, reducing costs and increasing productivity. Moreover, improved infrastructure attracts foreign investment, creating new opportunities for job creation and economic expansion.
- ii. **Education and Research:** Government spending on education and research is another crucial area that drives economic growth. A skilled and educated workforce is essential for attracting businesses

and industries, which in turn generates revenue and creates employment opportunities. Governments can also invest in cutting-edge research initiatives, fostering innovation and entrepreneurship. This not only enhances the country's competitiveness but also contributes to the development of new technologies and industries.

- iii. **Healthcare and Social Services:** Adequate healthcare and social services are indispensable for maintaining a healthy and productive population. Government spending on healthcare ensures access to quality medical care, reducing absenteeism and improving overall well-being. Additionally, investments in social services, such as childcare and eldercare, support vulnerable populations and promote social cohesion. These expenditures contribute to a more stable and resilient society, allowing individuals to focus on their work and personal lives without worrying about basic needs being met.
- iv. **Environmental Sustainability:** Governments must prioritize environmental sustainability to ensure long-term economic viability. Investing in renewable energy sources, conservation efforts, and sustainable practices reduces carbon emissions, mitigates climate change risks, and promotes eco-friendly industries. This not only protects natural resources for future generations but also creates new business opportunities and job prospects in emerging sectors like green technology.
- v. **Public Safety and Security:** Robust public safety and security measures are fundamental to fostering economic growth. Law enforcement agencies and emergency responders protect citizens from harm, ensuring a sense of stability and trust in the system. This confidence boost encourages entrepreneurs to start new ventures, investors to take calculated risks, and consumers to spend with confidence. Furthermore, effective crime prevention and response reduce the financial burden associated with criminal activities, freeing up resources for more productive pursuits.
- vi. **Agriculture and Rural Development:** The administration dedicates significant resources towards supporting agriculture through investments in cutting-edge research initiatives, irrigation projects, rural infrastructure development, and subsidies aimed at bolstering the livelihoods of farmers.
- vii. **Social Welfare and Poverty Reduction Initiatives:** Furthermore, the Government allocates substantial funds towards various social welfare programs designed to mitigate poverty and improve the socio-economic standing of marginalized segments of society. These initiatives include pension schemes, affordable housing programs, food subsidy allocations, and job creation endeavours intended to elevate the overall standard of living among vulnerable populations.

## **The Interconnectedness of Government Expansion, Economic Growth, and National Prosperity**

In today's fast-paced global economy, Governments and policymakers face numerous challenges in fostering economic growth and development. One crucial aspect to consider is the relationship between Government expansion and economic growth. This article will delve into the intricacies of this connection, exploring how Government intervention can either hinder or facilitate national prosperity.

- **The Concept of Government Expansion:** Government expansion refers to the increase in the size and scope of public sector activities, often resulting from increased taxation, regulation, and bureaucracy. This phenomenon has been observed in various forms throughout history, with examples ranging from ancient civilizations to modern-day nation-states. In recent times, Government expansion has become a ubiquitous feature of many economies worldwide.
- **The Impact of Government Expansion on Economic Growth:** Proponents of limited Government argue that excessive state involvement stifles innovation, entrepreneurship, and productivity, ultimately leading to reduced economic growth. Conversely, advocates for expanded Government roles contend that targeted interventions can stimulate economic activity by addressing market failures, providing essential public goods, and promoting social welfare.

Research suggests that moderate levels of Government expansion can have positive effects on economic growth, particularly during periods of economic downturn. For instance, fiscal stimulus packages aimed at shoring up aggregate demand can help mitigate recessionary pressures. However, over-reliance on Government spending can lead to inefficiencies, misallocation of resources, and crowding out private investment.

## Case Studies and Implications

Several notable case studies illustrate the complex interplay between Government expansion and economic growth:

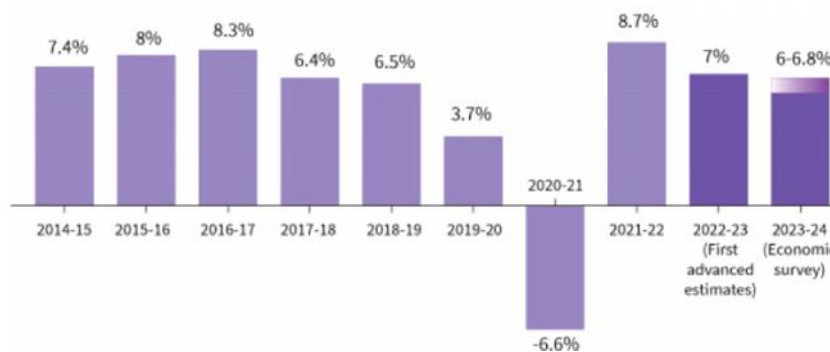
- 1. Japan's Post-War Reconstruction:** Following World War II, Japan's Government played a significant role in rebuilding the country's infrastructure, education system, and industries. This strategic combination of Government support and private initiative enabled Japan to achieve remarkable post-war economic growth.
- 2. South Korea's Miracle Economy:** South Korea's rapid industrialization was facilitated by a series of Government-led initiatives, including investments in human capital, technology transfer, and export-oriented manufacturing. These efforts helped transform South Korea into one of Asia's Four Tigers.
- 3. China's State-Led Development Model:** China's unique blend of central planning and market-based reforms has driven impressive economic growth since the late 1970s. While critics argue that this approach relies too heavily on state control, proponents point to the success in lifting hundreds of millions of people out of poverty.

The relationship between Government expansion and economic growth is multifaceted and context-dependent. Moderate levels of Government involvement can be beneficial in stimulating economic activity, while excessive state intervention can stifle innovation and efficiency. Policymakers must strike a balance between these competing forces to foster sustainable national prosperity.

As nations navigate the complexities of globalization, it becomes increasingly important to understand the intricate dynamics governing the intersection of Government expansion and economic growth. By acknowledging both the benefits and limitations of Government intervention, we can better design policies that promote long-term economic stability and progress.

## Data Analysis and Interpretation

**Figure 1:** The Indian economy is expected to grow in the range of 6-6.8% in 2023-24, according to the economic survey, compared to the estimated growth rate of 7% in 2022-23.



According to recent projections, India's economic growth rate for the fiscal year 2023/2024 is anticipated to surpass the International Monetary Fund's estimate of 6.1%. This optimistic outlook is attributed to the expectation that the global economic downturn will be mitigated by robust domestic demand.

A report compiled by Chief Economic Adviser V Anantha Nageswaran suggests that the country's baseline scenario envisions a growth rate of 6.5% for the upcoming fiscal year, making India one of the

fastest-growing economies worldwide. However, the actual outcome may fall within the range of 6.0% to 6.8%, contingent upon the trajectory of global economic and political developments.

Nageswaran emphasized that a moderate decline in global growth would have a net positive impact on India, leading to reduced commodity prices and alleviated inflation concerns. Notably, India's economy has recovered significantly since the COVID-19 pandemic, but the ongoing Russia-Ukraine conflict has introduced inflationary pressures, prompting central banks, including the Reserve Bank of India, to reassess their monetary policies.

The report indicates that inflation levels are neither sufficiently elevated to deter private consumption nor insufficiently low to undermine investments, despite remaining above the central bank's targeted range of 2% to 6% throughout most of 2022/2023. Consumer price indices registered a 5.72% increase compared to the same period last year.

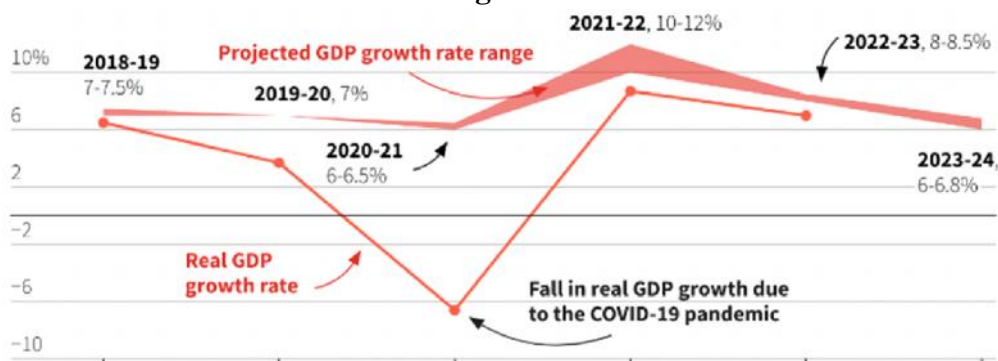
The survey predicts that demand in the economy will persist at a brisk pace in 2023/2024, driven by a vigorous credit disbursement and capital investment cycle, facilitated by strengthened balance sheets among corporations and banking institutions. Nevertheless, this development may lead to a persistent current account deficit, as a thriving domestic economy would likely sustain imports, whereas exports are expected to experience a decline due to weakening foreign market conditions.

India's current account deficit stood at 4.4% of GDP during the July-September quarter, representing a significant increase from 2.2% in the preceding quarter.

## Overestimating Growth

In the last five Year, the real GDP growth rate has been lower than the economic projection:

**Figure 2**



**Note:** Real GDP growth rate for 2022-23 are according to the first advanced estimates.

In response to the significant increase in India's general Government debt resulting from the pandemic era, the Government has initiated measures aimed at achieving fiscal consolidation.

According to recent reports, the Government remains on course to achieve its fiscal deficit targets for the current financial year (2022-2023), which includes meeting its medium-term fiscal objectives. Notably, the Government had previously outlined plans to reduce the fiscal deficit to 4.5% by the end of the next financial year (2025-2026) through its budgetary allocations for 2022-2023.

Furthermore, the report suggests that sustained economic growth driven by increased capital expenditures will enable India to maintain a positive growth-interest rate differential, thereby ensuring the sustainability of Government debt.

## Conclusion

This research investigation has demonstrated that Governmental expenditures have a statistically significant positive influence on economic expansion. Consequently, it is recommended that Governments prioritize

investments in public projects to stimulate long-term economic development. Notably, the effects of Government disbursements on economic growth may fluctuate over time and differ depending on various macroeconomic conditions. Furthermore, the efficacy of Government spending hinges upon the quality of governance, the institutional framework, and the prevailing policy environment. To achieve sustainable economic growth, policymakers must carefully craft and execute fiscal policies to guarantee that Government expenditures yield a net positive effect.

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