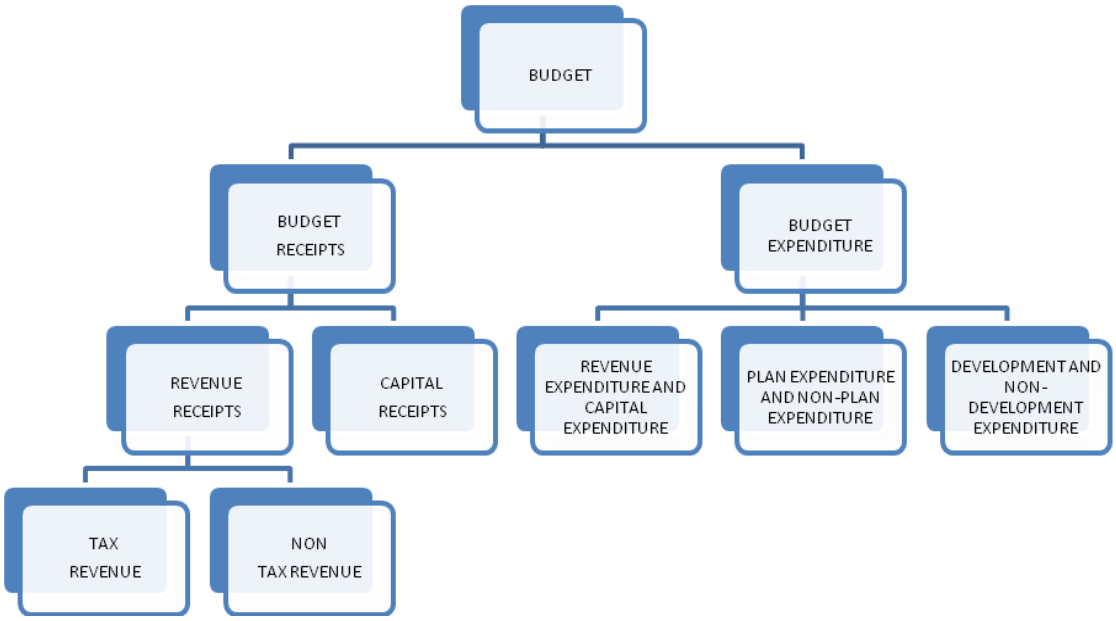
UNIT 9

GOVERNMENT BUDGET AND THE ECONOMY

KEY CONCEPTS:

- Meaning of the Budget
- Objectives of the Budget
- Components of the Budget
- Budget Receipts
- Budget Expenditure
- Balanced, Surplus and Deficit Budgets
- Types of Deficits

GOVERNMENT BUDGET – A FLOW CHART



01 MARK QUESTIONS AND ANSWERS

1. Define a Budget.
   Ans: It is an annual statement of the estimated Receipts and Expenditures of the Government over the fiscal year which runs from April –I to March 31.

2. Name the two broad divisions of the Budget.
   Ans: i) Revenue Budget
   ii) Capital Budget
3. What are the two Budget Receipts?
   Ans: i) Revenue Receipts
   ii) Capital Receipts
4. Name the two types of Revenue Receipts.
   Ans: i) Tax Revenue
   ii) Non-tax Revenue.

5. What are the two types of taxes?
   Ans: a) Direct Taxes: i) Income Tax, ii) Interest Tax, iii) Wealth Tax
   b) Indirect Taxes: i) Customs duties, ii) Excise duties, iii) Sales Tax
6. What are the main items of Capital Receipts?

   Ans: a) Market Loans (loans raised by the government from the public)

   b) Borrowings by the Government

   c) Loans received from foreign governments and International financial Institutions.

7. Give two examples of Developmental Expenditure.

   Ans: Plan expenditure of Railways and Posts

8. Give two examples of Non-Developmental expenditures.

   Ans: i) Expenditure on defence

   ii) Interest payments

9. Define Surplus Budget.

   Ans: A Surplus Budget is one where the estimated revenues are greater than the

   Estimated expenditures.

10. What are the four different concepts of Budget Deficits?

   Ans: a) Budget Deficit

   b) Revenue Deficit

   c) Primary Deficit and

   d) Fiscal Deficit

<u>03 AND 04 MARK QUESTIONS AND ANSWERS</u>

1. Explain the objectives of the Government Budget.
   Ans: These below are the main objectives of the Government Budget.
   a) <u>Activities to secure reallocation of resources:</u> - The Government has to reallocate resources with social and economic considerations.
   b) <u>Redistributive Activities</u>: - The Government redistributes income and wealth to reduce inequalities.
   c) <u>Stabilizing Activities</u>: - The Government tries to prevent business fluctuations and maintain economic stability.

d) **<u>Management of Public Enterprises</u>: - Government undertakes commercial activities that are of the nature of natural Monopolies, heavy manufacturing etc., through its public enterprises.**

2. **What are the components of the Budget?**

Ans: These below are the main components of the Government Budget. They are---

a) **Budget Receipts**
b) **Budget Expenditure**

Budget receipts may be classified as----

i) **Revenue Receipts and**
ii) **Capital Receipts**

Revenue Receipts may be classified as____

i) **Tax Revenue and**
ii) **Non-tax Revenue**

Budget Expenditure may be classified as -------

a) **Revenue Expenditure and Capital Expenditure**
b) **Plan Expenditure and Non-Plan Expenditure**
c) **Developmental and Non-Developmental Expenditure**

3. **Define Direct Taxes and Indirect taxes and give two examples each.**

i) **Direct Tax: - These are those taxes levied immediately on the property and Income of persons, and those that are paid directly by the consumers to the state.**
Examples: Income Tax, Wealth Tax, Corporation Tax etc.

ii) **Indirect Taxes*:* These are those taxes that affect the income and property of persons through their consumption expenditure. Indirect taxes are those taxes levied on one person but paid by another person.**
Examples: Customs duties, excise duties, sales tax, service tax etc.,

4. **What are the Non-Tax Revenue receipts?**

Ans: These below are the Non-tax revenue receipts:

a) **Commercial Revenue: Examples-Payments for postage, tools, interest on funds borrowed from government credit corporations, electricity, Railway services.**
b) **Interest and dividends**
c) **Administrative revenue, Examples: Fees, fines, penalties etc.,**

5. **What are the three major ways of Public Expenditure?**

Ans: These below are the three ways of Public Expenditure----

a) **Revenue Expenditure and Capital Expenditure**
b) **Plan Expenditure and Non-Plan Expenditure**
c) **Development and Non-developmental Expenditure.**

6. **What do you mean by Revenue Expenditure and Capital Expenditure?**

Ans: i) Revenue *Expenditure*:- It is the expenditure incurred for the normal running of government departments and provision of various services like interest charges on debt, subsidies etc.,

iii) *Capital Expenditure*:- It consists mainly of expenditure on acquisition of assets like land, building, machinery, equipment etc., and loans and advances granted by the Central Government to States & Union Territories.

7. **Define Balanced, Surplus and Deficit Budgets.**

Ans: a) *Balanced Budget*:- It is one where the estimated revenue *EQUALS* the estimated expenditure.

b) *Surplus Budget*:- It is one where the estimated revenue is *GREATER THAN* the estimated expenditures.

c) *Deficit Budget*:- It is one where the estimated revenue is *LESS THAN* the estimated expenditure.

8. **Explain the four different concepts of Budget deficit.**

Ans: These are the four different concepts of Budget Deficit.

a) ***Budget Deficit*:- It is the difference between the total expenditure, current revenue and net internal and external capital receipts of the government.**
Formulae: B.D = B.E > B.R (B.D= Budget Deficit, B.E. Budget Expenditure B.R= Budget Revenue

b) ***Fiscal Deficit*:- It is the difference between the total expenditure of the government, the revenue receipts PLUS those capital receipts which finally accrue to the government.**
***Formulae*: F.D = B.E - B.R (B.E > B.R. other than borrowings) F.D=Fiscal Deficit,**
B.E= Budget Expenditure, B.R. = Budget Receipts.

c) ***Revenue Deficit*: - It is the excess of governments revenue expenditures over revenue receipts.**
***Formulae*: R.D= R.E – R.R., When R.E > R.R., R.D= Revenue Deficit, R.E= Revenue Expenditure, R.R. = Revenue Receipts.**

d) ***Primary Deficit*: - It is the fiscal deficit MINUS Interest payments.**
***Formulae*: P.D= F.D – I.P, P.D= Primary Deficit, F.D= Fiscal Deficit, I.P= Interest Payment.**

06 MARK QUESATIONS AND ANSWERS

1. **How is tax revenue different from administrative revenue?**

Ans:

a) ***Tax Revenue*:-**
***i)* It is the main source of revenue of the government**
***ii)* It is the revenue that arises on account of taxes levied by the government.**
***iii)* Taxes of two types i.e., Direct and Indirect.**

iv) **Direct taxes are those taxes levied immediately on the property and income of persons. Examples: Income Tax, Corporate Tax, Wealth Tax etc.,**

v) **Indirect taxes are those taxes levied on the production and sale of the goods. Examples: Sales Tax, Excise Duty etc.,**

b) *Administrative Revenue*:-

i) It is the revenue that arises on account of the administrative function of the Government.

ii) It includes-------

a) Fees

b) License fees

c) Fines and penalties

d) Forfeitures of surety by courts

e) Escheat – means claim of the government on the property of a person who dies without having any legal heirs.

2. What is a balanced government budget? Explain the multiplier effect of a balanced budget.

Ans:

a) *Balanced Budget*: - It is one where the estimated revenue of the government equals the estimated expenditure.

b) *Effect of Multiplier on the Balanced Budget*:-

i) If only source of revenue is a lump sum tax, a balanced budget will then mean that the amount of tax equals the amount of expenditure (T=E)

ii) A balanced budget has an expansionary effect on the economy.

iii) Under balanced budget, the increase in income is equalent to the amount of government expenditure financed by tax revenue (i.e., $\Delta Y = \Delta G/\Delta T$)

iv) The multiplier effect of a balanced budget is ONE (Unitary)

v) A balanced budget is a good policy to bring the economy, which is under employment to a full employment equilibrium.

HIGHER ORDER THINKING SKILLS (HOTS)

1. What are the three levels at which the budget impacts the economy?

Ans: These below are the three levels at which the budget impacts the economy.

a) *Aggregate fiscal discipline*:- This means having control over expenditures, given the quantum of revenues. This is necessary for proper macro-economic performance.

b) *Allocation of resources*: - The allocation of resources based on social priorities.

c) *Effective and efficient provision of programmes:-* Effectiveness measures the extent to which goods and services the government provides its goals.

NUMERICALS

1. The following figures are based on budget estimates of Government of India for the year
   2001 – 2002. Calculate i) Fiscal Deficit ii) Revenue Deficit and iii) Primary deficit.

ITEMS	RS. BILLIONS
A) Revenue receipts	2,31,745
i) Tax Revenue	1,63,031
ii) Non-tax Revenue	68,714
B) Capital receipts	1,43,478
i) Recoveries of loans	15,164
ii) Other receipts	12,000
iii) Borrowings and other liabilities	1,16,314
C) Revenue expenditure	3,10,566
i) Interest payments	1,12,300
ii) Major subsidies	27,845
iii) Defence Expenditure	1,70,421
D) Capital Expenditure	64,657
E) Total Expenditure	3,75,223
i) Plan expenditure	1,00,100
ii) Non-plan expenditure	2,75,123

i) Ans: Fiscal Deficit = Total expenditure – Revenue receipts – Non-debt capital receipts = 3,75,223 – 2,31,745 – 15,164 – 12,000 = Rs. 1,16,314 billion.

ii) Revenue Deficit = Revenue expenditure – Revenue receipts
= 3, 10,566 – 2, 31,745 = Rs. 78,821 billion.

iii) Primary deficit = Fiscal deficit – Interest payments
= 1, 16,314 – 1, 12,300 = Rs. 4,014 billion.

2. From the following data about a government budget find
   a) Revenue Deficit b) Fiscal Deficit and c) Primary Deficit.

S.No.	Items	Rs. (cr.)
01	Tax revenue	47
02	Capital receipts	34
03	Non-tax revenue	10
04	Borrowings	32
05	Revenue expenditure	80
06	Interest payments	20

Ans: a) Revenue Deficit = Revenue expenditure – (Tax revenue + Non-tax revenue)
= 80 – (47+10) = 80 – 57 = 23 (cr.)
Fiscal Deficit = Borrowings = 32 (cr.)
Primary Deficit = Borrowings – Interest Payments 32 - 20 = 12 (cr.)