Press Release

Second Session of CSEP-World Bank Seminar Series on India's Public Financial Management System, September 20, 2021

Taking Stock of PFM reforms – the road ahead

International evidence has shown that a strong system of Public Financial Management (PFM) is critical for operational and allocative efficiency and sustainability of public expenditure. In this context, and given the Covid-19 shock to the PFM systems across countries, the Centre for Social and Economic Progress (CSEP), in coordination with the World Bank, has organized a three-part seminar series on "India's Public Financial Management (PFM) System – Post-COVID-19 need and opportunities for reform".

In the second session on "Taking Stock of PFM reforms- The road ahead", Hisham Waly, Practice Manager, World Bank, in his opening remarks, shared international examples of PFM reforms where fiscal transfers from the federal government to states have been used to incentivize PFM reforms and performance; and how, in developed economies, PFM has transitioned from a control function to a tool for improving public service delivery. Waly emphasised that it was critical to build stakeholder consensus across all levels of government, since that was where most reforms faltered.

Hisham Waly was in conversation with Pinaki Chakraborty, Director, National Institute of Public Finance and Policy, Ashutosh Vajpeyi, Joint Secretary (Economic Affairs), Government of Rajasthan and Project Director, Rajasthan PFMS Project, Prabodh Saxena, Additional Chief Secretary (Finance), Government of Himachal Pradesh and Mridul Saggar, Executive Director, Reserve Bank of India, all of whom spoke in their personal capacity. The session was moderated by Manoj Jain, Lead Governance Specialist, World Bank.

In the context of Covid-19, Pinaki Chakraborty pointed out three relevant issues: asymmetric fiscal shocks across levels of governments depending on revenue and expenditure assignment; borrowing power of different governments; and reprioritisation of expenditure depending on what is needed most in times of crises. He added that the 2021-22 state budgets are significant as they capture the impact of the pandemic on state government finances. He further pointed out that for PFM assessment during Covid, there is a need to arrive at an indicator framework that better reflects the resource constraints as well as expenditure priorities of both the centre and states.

According to state-level fiscal data, tax revenue aggregates in the revised estimates for 2020-21 across 28 states were 15% lower than the budget estimates for 2020-21, and 16% lower than the actuals for 2019-20, even as health expenditure and aggregate expenses increased. “There is a need to arrive at an indicator framework to evaluate and incorporate these shocks during the COVID and post-COVID eras, at least in the medium term, and develop a framework that better reflects the resource constraints as well as expenditure priorities,” he said.

Prabodh Saxena said that, in keeping with the Fifteenth Finance Commission’s recommendations, Himachal Pradesh has been attempting to rationalize its schemes. However, he highlighted the need to understand these attempts in the context of the political reality that Himachal Pradesh has seen new political parties coming to power in every election since 1990. “This is a major reason why schemes have multiplied manifold”, he observed. To deal with this constraint, he explained how Himachal Pradesh has been rationalising certain schemes through gradually reducing their funding, in a way to better manage the multiplicity of schemes. He added that “in the latest budget, we have a clear statement on how the Himachal Pradesh Government is committed to the rationalization of schemes.”

Elaborating on the experiences of states, Ashutosh Vajpeyi said that first step was to ensure fiscal discipline. He shared how Rajasthan has addressed this challenge with a state-of-the-art, fully transparent Integrated Financial Management System (IFMS) that enables real-time transactions, analysis, and projections.

“Use of Information Technology has strengthened the efforts made in this direction at the sub-national level,” he said. “Evidence–based-policy making has been attempted by the State Government in various sectors with the help of data analytics

Focusing on the fiscal challenges faced in the context of current pandemic and how RBI has effectively used debt management to help in mitigating the fiscal stress, Mridul Saggar said that, considering the macroeconomic conditions, RBI announced liquidity enhancing measures worth ₹17.2 lakh crore (8.7 per cent of nominal GDP of 2020-21) since February 6, 2020. This helped limit private sector scarring, while also keeping the fiscal borrowing costs at a 17-year low in 2020-21. The costs, though higher this year, remain low by historic standards.

He added that debt ratios for advanced economies will cross 122% of GDP this year and that for emerging markets is set on a rising path till 2026. In contrast, India’s debt ratio, having risen to 90% in the backdrop of pandemic, will be on a declining path from next year, provided we stick to the broad path laid out by the Fifteenth Finance Commission’s report. However, it will be important to lower primary deficits in the coming years so that any changes in interest rate cycles do not impact macro-economic and debt sustainability. He also said that the Covid crisis should not be wasted and those recommendations of the Fifteenth Finance Commission on which there was a broad consensus should be straight away implemented.

In terms of debt management for States, Saggar emphasised that capacity building on debt management must be a forerunner before States can consider moving to independent debt management cells. At the current juncture, RBI is helping them improve their cash flows management. They also need to focus on transparency in their budgets, especially in terms of off-balance sheet items and contingent liabilities.

Moderating the session, Manoj Jain summarised its key takeaways, observing that, “We need to see PFM as not only a tool from a transparency and accountability perspective, but as a means to an end, that can help improve public service delivery in sectors such as health, education, infrastructure, and even climate change, thus contributing to growth and poverty reduction in India.”

Elaborating further, he noted that “in order to develop a concerted, well-coordinated, and sequenced PFM reform strategy, it is necessary to get all stakeholders together.” He concluded that, for these reforms to get traction across all levels of government, they “would need to be contextualised to local ground realities and demonstrate a path of rapid results, concentrating on low-hanging fruits first”.

Closing the session, Anoop Singh, Distinguished Fellow, CSEP concluded that, “The fundamental issue is to bridge the gap between the high level public financial management framework in the Constitution and all the other guidelines, rules, and regulations.” Anoop Singh pointed out that this was a well-recognised problem, and it remains to be assessed what can be done to develop a “more resilient and unified framework” that ensures transparency, accountability, and the effective utilization of funds, especially in times of shocks.

The final session in this seminar series is scheduled for September 27 and will be on “The need for an overarching PFM Law and other practical steps”.

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