Economics Notes PDF

On

Government Budget and the Economy

(Class – 12)

BUDGET

A budget is a year-long financial report that explains how future revenue and expenditure will be calculated item-wise. The budget details a country's revenue and expenditures.

Main objectives of budget are:

(i) Reallocation of resources.
(ii) Redistribution of income and wealth
(iii) Economic Stability
(iv) Management of public enterprises.
(v) Economic Growth
(vi) Generation of employment

Importance of a budget:

(a) Today every country aims at its economic growth to improve the living standard of its people. Besides, there are many other problems such as poverty, unemployment, inequalities in incomes and wealth etc. Government strives hard to solve these problems through budgetary measures.
(b) The budget shows the fiscal policy. Item wise estimates of expenditure disclose how much and on what items, the government is going to spend. Similarly, item wise details of government receipts indicate the sources from where the government intends to get money to finance the expenditure.
In this way the budget is the most important instrument in the hands of governments to achieve their objectives and there lies the importance of the government budget. Note: Fiscal year is the year in which a country's budgets are prepared. Its duration is from 1st April to 31st March.

Two Components of Budget:

1. Revenue budget: The revenue budget is made up of the government of India's revenue receipts and the expenditures that are met with that revenue.
2. Capital budget: Capital receipts and payments are included in the capital budget. It also includes transactions from the Public Account.

BUDGET RECEIPTS

1. Revenue Receipts: Revenue receipts are those that do not result in a liability or a decrease in assets. The revenue is then split into two categories.

A. Receipt from tax:

a. Direct Tax:
i. Income Tax
ii. Corporate Tax
iii. Wealth and Property Tax

b. Indirect Tax:
i. Value added Tax
ii. Service Tax
iii. Excise Duty
iv. Custom Duty
v. Entertainment Tax

Commerce Classes

B. Receipt from non-Tax:

a. Commercial Revenue
b. Interest
c. Dividend, Profits
d. External Grants
e. Administrative Revenues
f. Fees
g. License Fee
h. Fines, Penalties
i. Cash grants-in-aid from foreign countries and international org.

2. Capital Receipts: Capital receipts are government receipts that create liability or deplete financial assets. The main sources of capital receipts are loans from the public, also known as market borrowings, as well as borrowings from the Reserve Bank, commercial banks, and some other financial institutions through the sale of treasury bills, borrowings from foreign governments and international organizations, and loan recoveries. Small savings, provident funds, and net receipts from the sale of shares in Public Sector Undertakings are among the other items (PSUs).

BUDGET EXPENDITURE

1. Revenue Expenditure:
(i) Neither creates assets.
(ii) Nor reduces liabilities.
e.g., Interest Payment, subsidies etc.

2. Capital Expenditure:
(i) It creates assets.
(ii) It reduces liabilities.
e.g., Construction of school building Repayment of loans etc.

Budget Deficit: The amount by which a budget's expenditures exceed its revenue is referred to as a budget deficit. This deficit is a good indicator of the economy's financial health.

Revenue deficit: Revenue deficit is defined as the difference between total revenue collected and total revenue expenditure. Only current income and current expenses are included in this deficit. A large deficit figure implies that the government should reduce its spending. The government may be able to boost revenue by raising tax revenue.
Revenue deficit = Total revenue expenditure – Total revenue receipts

Implications of Revenue Deficit are:

(i) A high revenue deficit shows fiscal indiscipline.
(ii) It shows wasteful expenditures of Govt. on administration.
(iii) It implies that the government is dissolving, i.e. the government is using up the savings of other sectors of the economy to finance its consumption expenditure.
(iv) It reduces the assets of the government. due to disinvestment.
(v) A high revenue deficit gives a warning signal to the government to either curtail its expenditure or increase its revenue.

Commerce Classes

Fiscal Deficit: When total expenditure exceeds total receipts excluding borrowing.
Fiscal Deficit: Total expenditures > Total Receipts excluding borrowing.

of Fiscal Deficits are:

- A significant drawback or consequence of fiscal deficit is that it may result in a debt trap.
- It causes inflationary pressures.
- It stifles future advancement.
- It increases reliance on foreign resources.
- It raises the government's obligation.

Primary Deficit: It is derived by subtracting interest payments from the fiscal deficit.
Primary deficit: Fiscal deficit – Interest payments on previous loans

Implications of Primary Deficits are:
It indicates how much of the government borrowings are going to meet expenses other than the interest payments.

Measures to correct different deficits:-
(i) Monetary expansion or deficit financing.
(ii) Borrowing from the public.
(iii) Disinvestment.
(iv) Borrowing from international monetary institutions and other countries.
(v) Lowering the government. expenditure.
(vi) Increasing govt. revenue.

Fiscal Policy: Keynesian economics, a theory developed by economist John Maynard Keynes, serves as the foundation for fiscal policy. It is the system by which a government makes changes to its planned expenditure and tax rates in order to monitor and influence the performance of a country's economy. It is implemented in tandem with monetary policy, by which the central bank of the country impacts the country's money supply. This policy influence aids in containing inflation, increasing employment, and, most significantly, maintaining a healthy currency value.

Debt: A quantity of the money borrowed by one entity, the borrower, from another entity, the lenders, is referred to as debt. Governments borrow money to cover their deficits, which allows them to fund regular operations as well as large capital expenditures. This debt might be in the form of a loan or bond issuance.

Commerce Classes