Fiscal Stress in India an Investigation into Budget Deficit and Reformoriented Solutions

Nethra C.[1]; Sahayaraj Antony Michael[2]; Santhanalakshmi V.[3]; Dr. D. P. Sivaskthi Balan[4]

[1,2,3,4]KAM Public School Channel

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Abstract: India's budget deficit has been a recurring economic challenge over the past few years, reflecting the imbalance between government revenue and expenditure. This research analyzes the primary reasons behind India's fiscal deficit from 2021 to 2025, focusing on factors such as rising government spending on welfare schemes, subsidies, and infrastructure, alongside limited growth in tax and non-tax revenues. The study also explores India's key income sources, including direct and indirect taxes, public sector enterprises, and non-debt capital receipts. Furthermore, it evaluates strategies to enhance national income and reduce the deficit through improved tax compliance, promotion of exports, privatization of loss-making enterprises, diversification of income sources, and digitalization of financial systems. By examining data from the Union Budget, Economic Survey, and reports from financial institutions, this research provides insights into sustainable fiscal management and policy measures required for long-term economic stability in India.

Keywords: *Economy, India, Policies.*

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I. INTRODUCTION

The fiscal budget of any nation serves as a blueprint for its economic priorities, development strategies, and financial discipline. In recent years, India has consistently recorded a fiscal deficit, where the government's total expenditure surpasses its total revenue, excluding borrowings. This recurring shortfall in the national budget has raised concerns about the sustainability of public finances, the efficiency of resource allocation, and the long-term impact on economic growth.

From the unprecedented challenges posed by the COVID-19 pandemic to structural issues such as a narrow tax base, rising subsidy burdens, and high interest payments, multiple factors have contributed to the widening fiscal deficit. Furthermore, global disruptions, inflationary pressures, and efforts to stimulate economic recovery through increased capital expenditure have also played significant roles.

This research aims to explore the key causes behind India's budgetary deficits over the past four years, analyse their implications on the broader economy, and propose practical strategies for fiscal consolidation. By examining both the short-term drivers and long-term structural issues, this study seeks to offer informed recommendations for reducing the fiscal deficit while maintaining economic growth and social welfare.

➢ *Hypothesis*

This research is based on the hypothesis that India's persistent budget deficit from 2021 to 2025 is primarily caused by a significant gap between increasing public expenditure and slower revenue growth. It is assumed that while tax collections and non-tax revenues have improved gradually, they have not kept pace with rising government spending on welfare schemes, subsidies, infrastructure, and interest payments. The study also hypothesizes that external factors such as the COVID-19 pandemic, global inflation, fluctuating oil prices, and geopolitical tensions have intensified fiscal pressure. Furthermore, the research proposes that effective fiscal reforms—such as broadening the tax base, promoting disinvestment, increasing foreign investment, and improving the efficiency of public spending—can play a crucial role in reducing the deficit. By analysing income sources, spending patterns, and policy interventions, the paper aims to validate whether these factors are the key drivers of India's fiscal imbalance and identify which corrective measures may yield the best outcomes.

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II. REVIEW OF LITERATURE

- *Analyzing India's Rising Fiscal Deficits Over the Past Four Years:*

- *Increased Public Spending Post-Pandemic*

In the aftermath of the COVID-19 pandemic, the Indian government significantly ramped up public expenditure to manage both the health crisis and its economic consequences. Large-scale spending was directed toward healthcare infrastructure, vaccine procurement, emergency relief, and welfare schemes such as the PM Garib Kalyan Yojana and MGNREGA. These initiatives, while crucial for safeguarding public welfare, substantially increased the fiscal burden on the government. This surge in spending, unmatched by proportional revenue growth, was a major contributor to the fiscal deficit during this period.

- *Slower Revenue Growth*

Government revenues, particularly from taxes, were adversely affected in the early post-COVID years. Direct taxes like income and corporate tax witnessed slow recovery as many sectors struggled to regain stability. Although GST collections improved in later years, they remained inconsistent and fell short of bridging the widening fiscal gap. Additionally, sectors such as tourism, hospitality, and informal trade—important contributors to indirect tax revenue—remained sluggish, leading to a subdued revenue base.

- *Rising Subsidy Burden*

India's subsidy expenditure surged, especially in response to global disruptions. The Russia-Ukraine war triggered sharp increases in global crude oil, fertilizer, and food prices. To shield its population from inflation, the Indian government chose to absorb much of these costs by increasing subsidies. Excise duties on fuel were slashed to keep prices in check, which significantly reduced government revenue. Simultaneously, food and fertilizer subsidies rose dramatically to support food security and agricultural needs, placing further strain on the budget.

- *Growing Borrowing and Debt Servicing Costs*

To fund the rising gap between income and expenditure, the government turned to increased borrowing. While this allowed the continuation of essential public programs, it also led to a rise in public debt. Consequently, a larger portion of the annual budget has been directed toward interest payments and debt servicing, reducing fiscal space for development and capital expenditure. This debt cycle adds to the ongoing deficit, making it more difficult to achieve fiscal consolidation in the short term.

- *Impact of Global Economic Pressures*

External economic factors have further exacerbated India's budgetary stress. Global supply chain disruptions, currency depreciation, and international interest rate hikes have impacted trade balances and capital inflows. Inflationary pressures and geopolitical uncertainties have made imports costlier and reduced the flow of investments. These global trends have complicated India's efforts to maintain a balanced budget despite relatively stable foreign exchange reserves.

Table 1 India's Income and Expenditure Trends Over the *Last ~4 Years*

FY 2021-22 / FY 2022-23	After Covid-19 disruptions, receipts recovered. Tax collections rose, non-tax revenues improved. The government also used stimulus and relief measures. Expenditure remained elevated; large spending under health, social welfare, subsidies due to pandemic. Capital outlay started picking up. Fiscal deficits remained high; strong pressure on revenue deficit. Debt and interest payments increased.
FY 2023-24	Revenue receipts rose significantly. Estimates and revised estimates show growth in both tax revenues (direct & indirect) and non-tax sources. ([PRS Legislative Research] Expenditure continued upward. There was an increasing focus on capital expenditure (CapEx) — infrastructure, asset creation etc. Revenue expenditure also increased (committed liabilities, subsidies, interest payments). ([Drishti IAS]) The fiscal deficit remained elevated (~5-6% of GDP in earlier years), but there is a gradual movement toward consolidation. Revenue deficits persisted though some improvement. ([PRS Legislative Research]
FY 2024-25	The budget documents estimate further growth in receipts. Tax revenue growth projected in double digits. Gross tax revenue, non-tax revenue, states' share, etc all rising. ([Business Standard][3]) | Expenditure projections continue to grow. Capital expenditure is a priority. The government is increasing effective capital expenditure (which includes grants for capital asset creation to states etc.).

➢ *Trend of India Fiscal Deficit for Last Years*

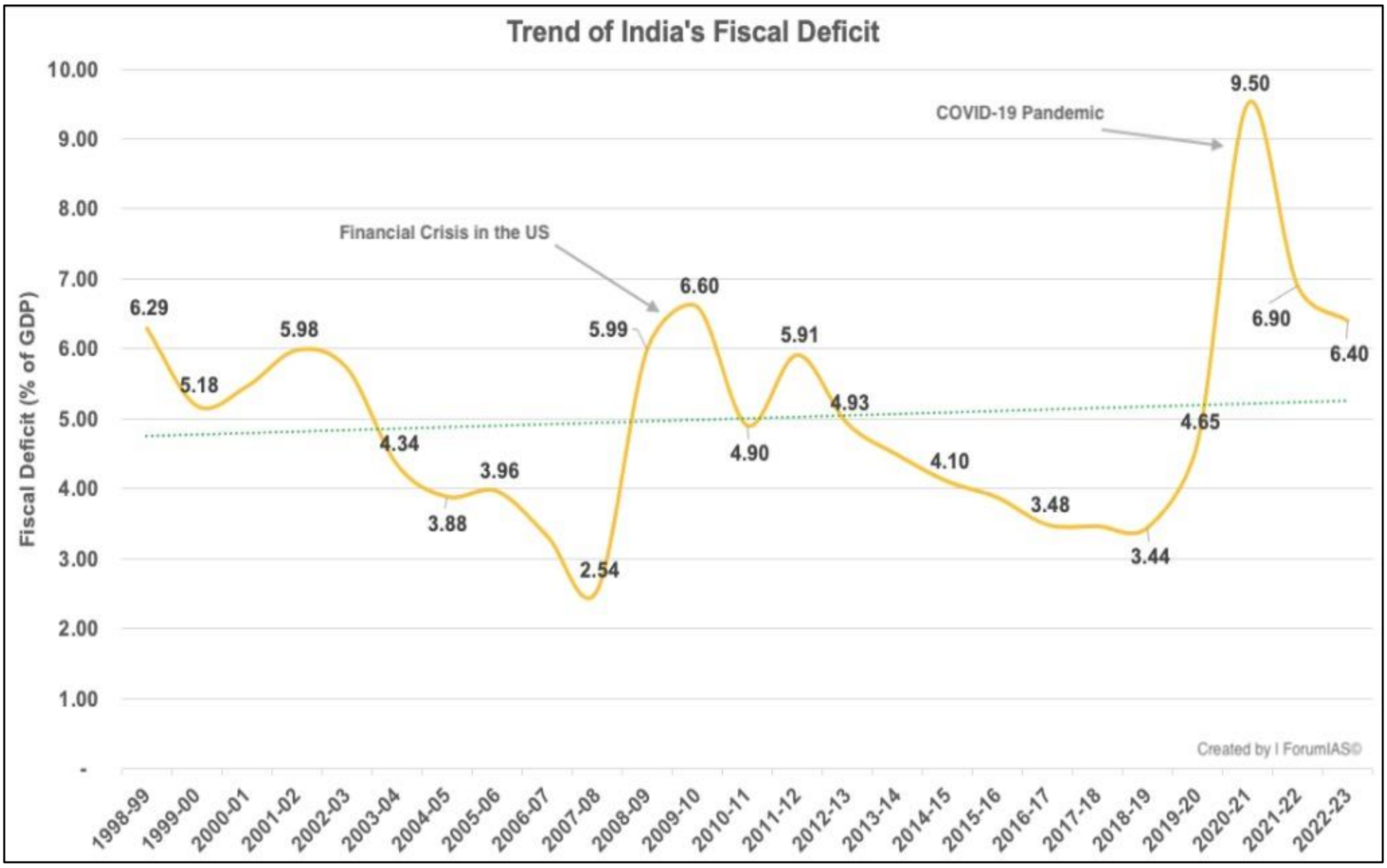

Fig 1 Trend of India Fiscal Deficit for Last Years

➢ *Tracking India's Budget Spending: A Sectoral Review of 2021 to 2025:*

- *Welfare and Subsidy Programs*

A large portion of India's expenditure goes toward subsidies and social welfare schemes aimed at supporting its vast population, especially the economically weaker sections. Key among these is the food subsidy program managed through the Public Distribution System (PDS), which provides free or subsidized grains to over 800 million people under schemes like the PM Garib Kalyan Anna Yojana. The fertilizer subsidy ensures affordable prices for farmers, while fuel subsidies—though reduced in recent years—continue to offer price protection for LPG and kerosene users. Additionally, the government runs several direct benefit transfer (DBT) programs, such as PM-KISAN, Ujjwala Yojana, and old age pensions, which require steady funding despite low returns. These welfare expenses have increased particularly after the pandemic, putting further pressure on public finances.

- *Infrastructure Development*

Infrastructure development has remained a central pillar of the government's budget strategy to stimulate long-term growth and job creation. Capital expenditure has steadily increased, reaching record highs year after year. The government has invested heavily in building and expanding national highways, modernizing railways, developing metro projects in major cities, and upgrading urban infrastructure under the Smart Cities Mission. Programs like PM Awas Yojana, which provides affordable housing to urban and rural poor, have also received sustained funding. Despite fiscal stress, infrastructure spending has been prioritized because it has high multiplier effects on employment and economic activity.

- *Defence and National Security*

India's defence expenditure is among the highest in the world, driven by the need to modernize its armed forces and maintain strong border security. Over the last four years, defence spending has consistently remained one of the top three allocations in the Union Budget. Funds have been used for procurement of advanced equipment, indigenization under the "Make in India" defence initiative, and strategic infrastructure near India's borders. A significant amount also goes toward pensions for retired defence personnel, further increasing the total burden. In a time of geopolitical tensions—especially with neighbouring countries—India continues to invest heavily in national security despite financial constraints.

- *Health and Education*

Post-COVID, public spending on healthcare increased substantially to strengthen India's fragile health infrastructure. Funds were directed toward upgrading primary healthcare centers, expanding medical college networks, and

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implementing national health insurance schemes like Ayushman Bharat. Vaccination drives and pandemic management also demanded large-scale investments between 2021 and 2023. On the education front, the government has been working on implementing the National Education Policy (NEP), expanding digital learning through programs like PM eVIDYA, and upgrading school infrastructure under schemes such as Samagra Shiksha and PM SHRI Schools. Though spending on health and education is still below the global average, it has seen noticeable increases during this period.

- *Interest Payments on Borrowings*

One of the largest non-productive expenditures in India's budget is interest payments on previously borrowed funds. As the government borrows more to meet its fiscal needs, the debt burden rises—leading to higher interest liabilities. In recent years, interest payments have taken up nearly 25% of total budget expenditure. This means a large portion of government income is used just to service debt, rather than fund new programs. This growing financial obligation limits the government's flexibility and adds to long-term fiscal challenges.

- *Transfers to States and Centrally Sponsored Schemes*

The central government allocates a substantial part of its budget as transfers to states for implementing central schemes and sharing tax revenue. States receive funds for programs like PMGSY (rural roads), Jal Jeevan Mission (rural water supply), Swachh Bharat (sanitation), and National Health Mission. While the center designs and partially funds these schemes, the states are responsible for executing them on the ground. These transfers are crucial for achieving national development goals but also add to the budget's overall weight.

- *Agriculture and Rural Development*

India continues to invest heavily in agriculture and rural development to support the livelihoods of a large part of its population. Schemes like PM-KISAN (₹6,000 annual support to farmers), crop insurance programs (PMFBY), irrigation schemes, and MGNREGA (rural job guarantee) are some of the key areas of focus. These programs are essential for ensuring food security, reducing rural poverty, and stabilizing.

➢ *Study if India's Budgetary Revenue Sources (2021–2025)*

- *Government Revenue Sources*

A large portion of India's income comes from tax collections, which form the backbone of the central and state governments' finances. These tax revenues are broadly divided into direct and indirect taxes. Direct taxes include income tax paid by individuals and corporate tax paid by businesses. Over the past few years, direct tax collections have grown steadily due to increased digitalization, tighter tax compliance, and better income reporting—especially after linking PAN cards with Aadhaar and streamlining the e-filing system. In the financial year 2023–24, direct tax collections crossed ₹19 lakh crore, showing strong economic activity and compliance.

Indirect taxes, on the other hand, include the Goods and Services Tax (GST), customs duties, and excise duties. GST has been India's most significant indirect tax since its implementation in 2017. It is collected on the supply of goods and services and is shared between the center and the states. Monthly GST collections consistently crossed ₹1.8 lakh crore by 2024, thanks to improved compliance and technology-enabled tracking systems. Excise duty, particularly on fuel and tobacco, and customs duties on imported goods have also been significant, though they fluctuate based on global prices and trade volumes.

In addition to tax revenue, the government earns non-tax revenue through various channels. This includes dividends from public sector enterprises (PSUs), such as ONGC, LIC, and NTPC, which pay a portion of their profits to the government. The Reserve Bank of India (RBI) also transfers surplus income annually to the government. Interest earned on loans given to states and public entities, fees from government services (like passport applications, vehicle registrations), and telecom spectrum auctions also add significantly to non-tax revenue. For instance, spectrum auctions in 2022–23 generated substantial income when telecom companies bid for 5G airwaves.

The government also raises funds through disinvestment and asset monetization. This involves selling stakes in public enterprises (such as the IPO of LIC in 2022) or leasing infrastructure assets like highways, railways, and airports to private entities for revenue generation under the National Monetization Pipeline. These initiatives, although politically sensitive, have been crucial in supplementing government income during fiscal deficits.

- *Sectoral Contributions to National Income*

India's economic structure is divided into three main sectors—services, industry, and agriculture—each contributing differently to the nation's income.

The services sector is the largest contributor to India's Gross Domestic Product (GDP), accounting for approximately 53% to 58% during these years. Key services include information technology (IT), financial services, communications, tourism, and logistics. India's IT and software exports, led by companies like TCS, Infosys, and Wipro, have remained robust and globally competitive, generating over $200 billion in export revenue in 2023. Banking and fintech services have also expanded, especially with the rise of digital payments and UPI transactions, adding to GDP growth and tax contributions.

The industrial sector, including manufacturing, mining, construction, and electricity, contributes around 25% to 28% of GDP. The government has promoted schemes like "Make in India" and the Production Linked Incentive (PLI) program to boost domestic manufacturing in electronics, automobiles, pharmaceuticals, and textiles. Despite global supply chain disruptions and the energy crisis in 2022, sectors such as cement, steel, and construction have shown signs of recovery. However, industrial growth still faces challenges due to high input costs and regulatory hurdles.

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The agriculture sector, while contributing only about 15% to 18% of GDP, remains vital as it employs nearly 40% of India's population. This sector includes crops, livestock, fisheries, and forestry. Over the years, agricultural income has been volatile due to irregular monsoons, rising input costs, and climate-related risks. Government schemes like PM-KISAN (direct income support to farmers) and increased procurement under Minimum Support Prices (MSPs) have provided some financial relief. Yet, the sector continues to contribute less to overall income relative to the workforce it sustains.

- *External Sources of Income*

India also earns substantial income from external sources, especially in foreign currency. A major component is remittances—money sent home by Indians working abroad. India has consistently ranked as the world's top recipient of remittances, with inflows exceeding $100 billion annually by 2023. These funds support household consumption, investment in property, and rural development.

Export of goods and services is another crucial income source. India exports petroleum products, gems and jewellery, pharmaceuticals, textiles, and machinery, among others. Services exports, particularly in IT and business process outsourcing (BPO), have grown rapidly. However, external trade has also faced pressure due to global uncertainties like the Russia-Ukraine war, tightening U.S. monetary policy, and supply chain disruptions.

Foreign investments—both Foreign Direct Investment (FDI) and Foreign Institutional Investment (FII)—also contribute to India's economic inflows. FDI, in particular, has shown strong performance, with sectors like electronics, renewable energy, and real estate attracting significant interest. By 2022–23, India received over $100 billion in FDI inflows, which not only support economic growth but also generate tax revenue through employment and business expansion.

➢ *Strategies to Reduce India's Fiscal Deficit: A Policy Perspective*

- *Strengthening Tax Revenue*

One of the most effective ways to reduce the budget deficit is by expanding and improving tax collection. This can be done by broadening the tax base—bringing more people and businesses into the tax net—and ensuring better compliance through digital tools, stricter enforcement, and simplified procedures. Encouraging formalization of the economy and reducing tax evasion will enhance both direct (income, corporate tax) and indirect (GST) revenues.

- *Rationalizing Subsidies and Public Expenditure*

India spends a large portion of its budget on subsidies—especially for food, fuel, and fertilizers. While these are necessary for social welfare, targeting them more efficiently using digital platforms (like Aadhaar-linked DBT) can reduce leakage and waste. Rationalizing such subsidies and cutting non-essential expenditures (such as excessive administrative costs or underperforming schemes) can significantly lower the fiscal burden.

- *Boosting Disinvestment and Asset Monetization*

The government can raise substantial revenue by selling or leasing public sector assets through disinvestment and monetization. Privatizing non-strategic PSUs, listing more state-owned enterprises, and leasing public infrastructure (like roads, railways, airports) can generate funds without raising taxes. A consistent and transparent disinvestment policy will also attract private and foreign investment.

- *Promoting Economic Growth*

A growing economy naturally improves revenue through higher tax collections, job creation, and industrial expansion. By investing in infrastructure, manufacturing, and digital innovation, India can boost GDP, which in turn improves the government's income without raising tax rates. Programs like "Make in India" and Production Linked Incentives (PLI) help in this direction.

- *Efficient Debt and Fiscal Management*

Improving how the government manages borrowing is also critical. Reducing reliance on short-term or high-interest debt, prioritizing capital expenditure over revenue expenditure, and maintaining fiscal discipline in both central and state budgets will ensure sustainable deficit levels.

III. METHODODLGY

This research paper employs a qualitative and descriptive approach to investigate the reasons behind India's recurring budget deficits from 2021 to 2025. The study is based entirely on secondary data, gathered from credible and publicly available sources. Key documents analysed include the Union Budget reports of the Government of India, Economic Surveys, Reserve Bank of India publications, and reports from institutions such as the Ministry of Finance, NITI Aayog, and the Comptroller and Auditor General (CAG). International sources such as the World Bank and the International Monetary Fund (IMF) have also been referenced to provide context and comparison with global fiscal trends.

The analysis focuses on identifying patterns in revenue generation and government expenditure over the last four years. Special attention has been paid to trends in direct and indirect tax collections, non-tax revenues, fiscal deficit-to-GDP ratios, and government borrowings. Factors such as the economic impact of the COVID-19 pandemic, inflation, rising oil prices, increased subsidies, and welfare spending have been critically examined to understand their effect on the budget balance. Policy decisions related to disinvestment, monetization, and taxation have also been considered to assess their effectiveness in addressing the fiscal deficit.

While the central objective of this study is to examine the causes of the budget deficit at the national level, the research does not delve into the fiscal conditions of individual states. In addition, the study is limited to analysis based on existing government and financial reports; no primary data

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collection, such as surveys or interviews, has been conducted. Despite these limitations, the methodology provides a comprehensive understanding of India's fiscal challenges during this period.

IV. ANALYSIS

Over the past four years (2021–2025), India has faced persistent fiscal deficits, primarily due to a combination of high public expenditure and relatively slower revenue growth. The economic impact of the COVID-19 pandemic created a substantial initial shock to government finances, leading to increased spending on healthcare, vaccination drives, relief packages, and social welfare schemes. At the same time, economic activity slowed, resulting in reduced tax collections and weaker private sector earnings. This imbalance widened the fiscal deficit significantly in the financial year 2020–21 and had lingering effects in the subsequent years.

India's income sources during this period were heavily reliant on direct taxes such as income tax and corporate tax, and indirect taxes such as Goods and Services Tax (GST), customs duties, and excise duties. While tax collections did improve in later years, especially with increased compliance and digitization, they were not sufficient to cover the rising costs of subsidies, interest payments on debt, and infrastructure investments. Non-tax revenue, such as dividends from public sector undertakings and surplus transfers from the Reserve Bank of India (RBI), added to government income but remained inconsistent. Disinvestment efforts and asset monetization through schemes like the National Monetization Pipeline were undertaken, but they faced delays and political challenges, resulting in shortfalls from expected revenue targets.

The government's expenditure has been particularly high in sectors such as food and fertilizer subsidies, defence, rural employment schemes (like MGNREGA), and infrastructure development. The ambitious capital expenditure push in the Union Budgets aimed to stimulate economic growth and job creation, but it also increased fiscal pressure. Additionally, rising global oil prices, inflation, and import costs due to a weak rupee contributed to higher fiscal outflows.

To address the deficit, the government needs to adopt both short-term and long-term measures. In the short term, improving tax compliance, widening the tax base, and curbing unproductive expenditures can help balance the books. Long-term measures include promoting privatization, strengthening public sector efficiency, reducing subsidies gradually, and boosting economic growth through reforms in manufacturing, agriculture, and digital infrastructure. Encouraging foreign investment, expanding exports, and investing in skill development can also lead to higher national income and improved fiscal health.

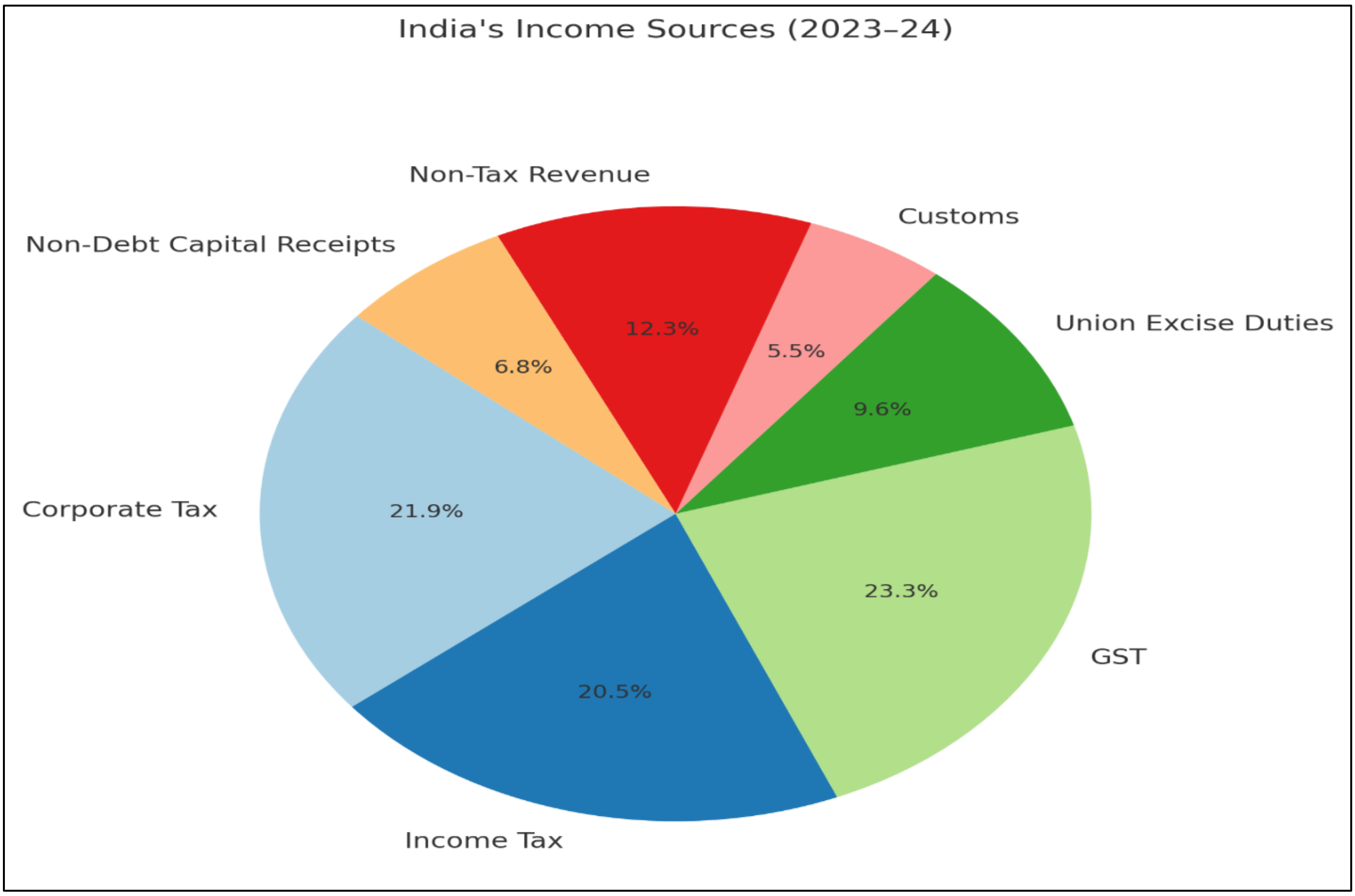

Fig 2 India's Income Sources (2023-24)

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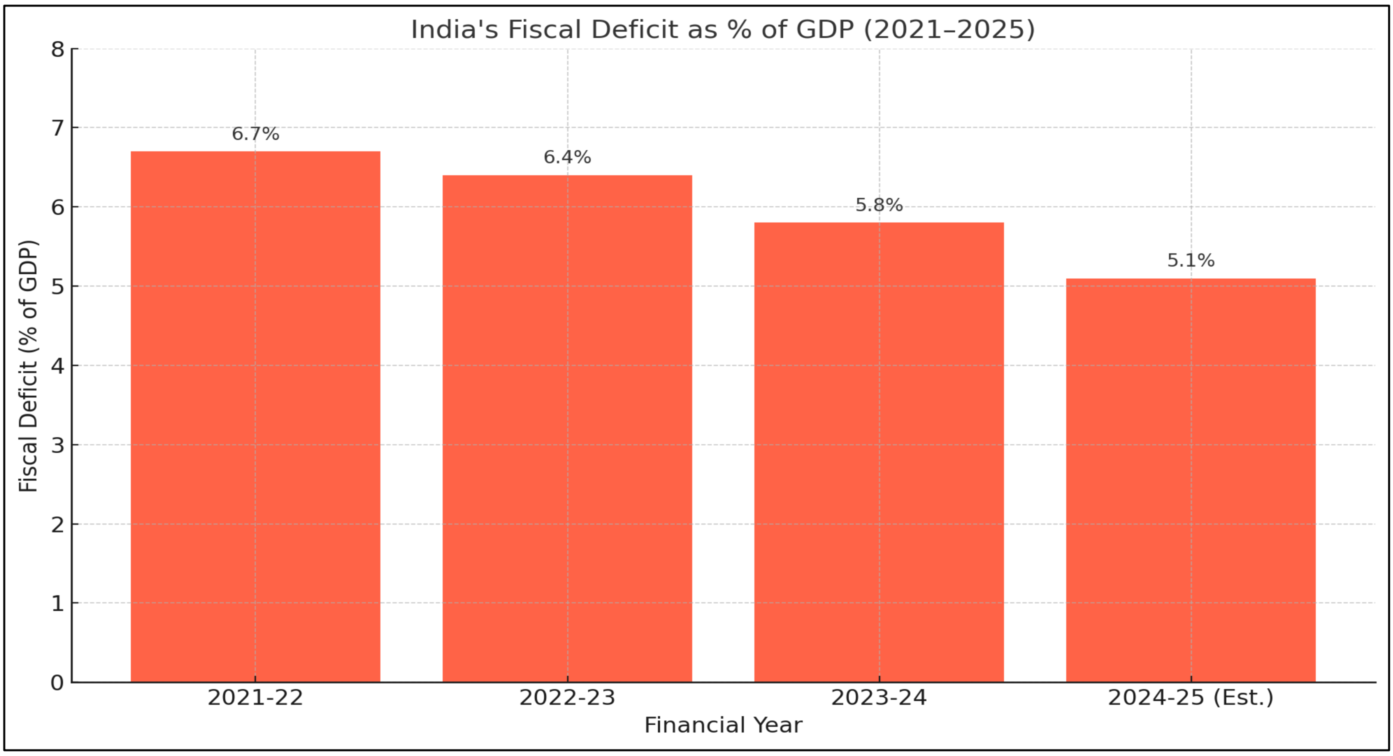

Fig 3 India’s Fiscal Deficit as % of GDP (2021-2025)

V. CONCLUSION

India’s budgetary deficit over the past four years (2021–2025) reflects a complex interplay of internal economic policies and external global challenges. The fiscal imbalance has primarily arisen from rising public expenditure, including subsidies, infrastructure investment, and welfare schemes, coupled with only moderate growth in revenue generation. Although India has made progress in increasing tax collections, improving compliance through digitization, and tapping non-tax revenues like disinvestment and RBI transfers, these efforts have not yet fully bridged the fiscal gap.

The analysis shows that while income from direct taxes, GST, and public sector contributions forms a significant part of the government’s revenue, it is often outweighed by expenses such as interest payments, defence, and social programs. External shocks—like the COVID-19 pandemic, global inflation, and fluctuating fuel prices—have further stressed India’s finances. These factors have collectively contributed to the consistent budgetary deficit.

To reduce the deficit, a multi-pronged strategy is essential. This includes broadening the tax base, increasing non-tax revenues through efficient asset monetization, curbing unnecessary expenditures, and boosting economic growth through structural reforms. Strengthening domestic industries, encouraging exports, and enhancing private sector participation can also lead to sustained revenue generation.

In conclusion, while fiscal deficits are a common feature of growing economies like India, careful financial planning, transparency, and policy discipline are crucial to ensure long-term economic stability. Addressing the root causes of revenue-expenditure mismatches will be key to building a more resilient and balanced fiscal future for the country.

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