

Riyasat IAS Mentorship

Riyasat IAS
Mentorship

Secure Prelims Program 2026

English - हिंदी माध्यम

AN INITIATIVE UNDER **RIYASAT IAS MENTORSHIP**

*Shaping Potential
Into Performance*



Riyasat Ali Sir

IAS Mentor Since 2011

INTENSIVE & INTERATED

Prelims GS & CSAT PROGRAM

to Crack CSE 2026

Secure Prelims ECONOMY Sample Notes

More Information: 8090528260, 9319612575, 9266989092

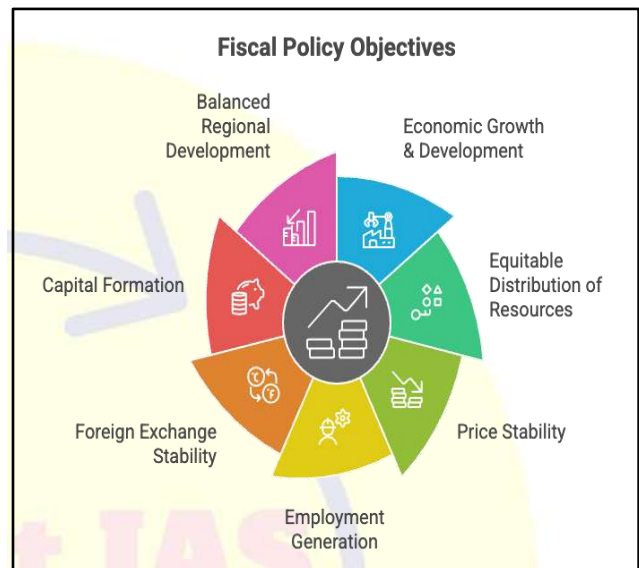
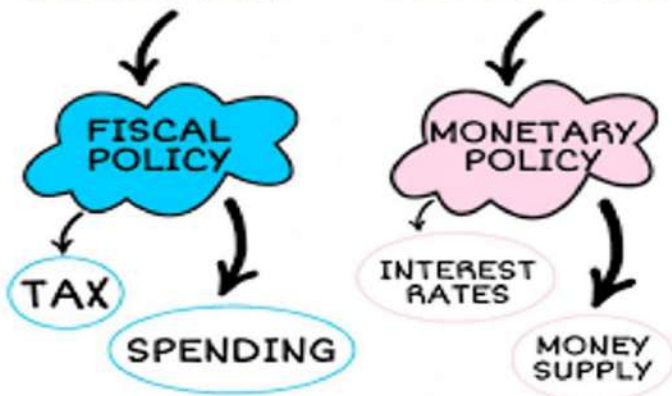
FISCAL POLICY

Fiscal Policy: It is a part of government policy that deals with **raising revenue** through **taxation and spending** for **socio-economic development**, to influence a nation's economy. Its main goal is to manage aggregate demand to achieve macroeconomic objectives, such as price stability, full employment, and economic growth.

ECONOMIC POLICY

GOVERNMENT

CENTRAL BANK



Types of Fiscal Policy

EXPANSIONARY FISCAL POLICY

$$G > T$$

NEUTRAL FISCAL POLICY

$$G = T$$

CONTRACTIONARY FISCAL POLICY

$$G < T$$

*G - GOVT. SPENDING; T - TAX REVENUE

Expansionary Fiscal Policy

Definition: A policy used by the government to **stimulate economic growth** during periods of **recession or slowdown**. It is a fiscal Policy that involves an increase in government expenditure or a reduction in government taxation (or combination of both).

Tools:

- **Lower Taxes** → Increases disposable income and consumption.

Riyasat IAS Mentorship

	<ul style="list-style-type: none">• Increase Government Spending → Boosts demand and job creation. <p>Effects:</p> <ul style="list-style-type: none">• Higher demand for goods and services• Increased employment opportunities• Higher inflation risk (if overused) <p>When Used: During economic recession, high unemployment, or low GDP growth.</p> <p>Example: India's fiscal stimulus packages during the COVID-19 pandemic.</p> <p>Negative effect of Expansionary Fiscal Policy:</p> <ul style="list-style-type: none">• Crowding out private investment: Excessive borrowing by government may increase interest rates and increase cost of borrowing by private sector, resulting in crowding out private investment.• Increase in Public debt: Excessive borrowing by the government may result in unsustainable Public debt levels.
Contractionary Fiscal Policy	<p>Definition: A policy aimed at reducing inflation and controlling excessive demand in the economy. It refers to deliberate policy of decreasing government spending or an increase in government taxation (or combination of both).</p> <p>Tools:</p> <ul style="list-style-type: none">• Higher Taxes → Reduces disposable income.• Reduced Government Spending → Limits public expenditure and demand. <p>Effects:</p> <ul style="list-style-type: none">• Decreased demand and inflation• Lower budget deficit• May slow economic growth <p>When Used: During high inflation, overheating of the economy, or to reduce fiscal deficit.</p> <p>Example: Reduction in subsidies and tax hikes during post-2008 fiscal consolidation</p>
Neutral Fiscal Policy	<ul style="list-style-type: none">• It refers to a policy where government expenditure is fully funded by tax collected by the government.• It is usually undertaken when the economy is in equilibrium (aggregate demand = aggregate supply).

Budget/Annual Financial Statement (AFS): Fiscal Policy Tool

- According to **Article 112** of Indian Constitution, **Union Budget** is referred to as **Annual Financial Statement (AFS)**.
- It is a **statement of estimated receipts and expenditure** of the Government in a **financial year**.
- The **Department of Economic affairs** is responsible for the **preparation of the Union Budget** that is presented to the Parliament.

Types of Budget: The types of budgets are defined based on the relationship between the government's revenue collections and expenditures:

- **Balanced Budget:** Revenue = Expenditure. A balanced budget indicates a neutral fiscal stance.
- **Surplus Budget:** Revenue > Expenditure. A surplus budget suggests a contractionary fiscal stance.
- **Deficit Budget:** Revenue < Expenditure. A deficit budget indicates an expansionary fiscal stance, which might be a response to stimulate economic growth during downturns, though it leads to an accumulation of government debt. Reducing revenue expenditure and Rationalising subsidies by the Government can reduce the deficit.

Components of Budget:

1. **Annual Financial Statement [Article 112]:** Contains **receipts and expenditures** of:
 - **Current year**
 - **Previous year**
 - **Upcoming year**
- Divided into:
 - **Consolidated Fund of India**
 - **Contingency Fund of India**
 - **Public Account of India**
2. **Demands for Grants [Article 113]:** Ministry-wise **expenditure estimates** presented to **Lok Sabha**
3. **Appropriation Bill [Article 114(3)]:** No expenditure can be made from the **Consolidated Fund** without passing this bill.
4. **Finance Bill [Article 110(a)]:** A bill to **impose, abolish, remit, alter, or regulate taxes** as proposed in the Budget.

1. Allocation Function

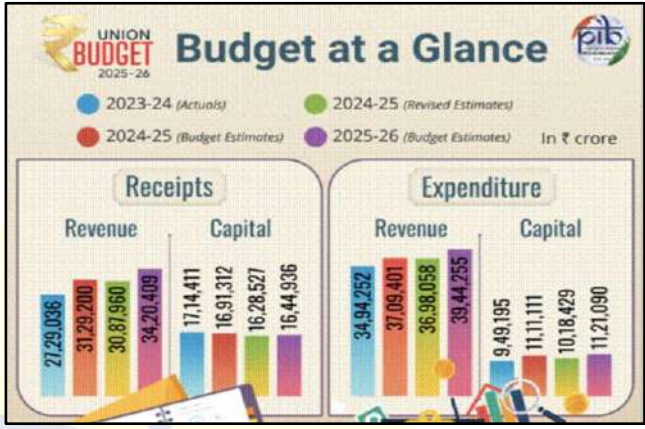
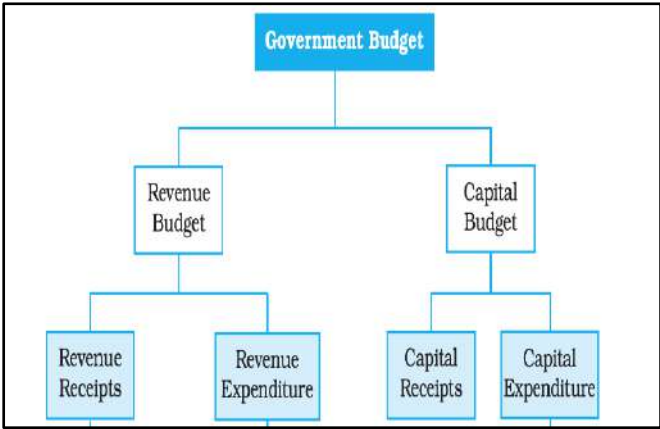
- **Provision of Public Goods:** Government provides goods/services which the market **cannot provide efficiently** like **defence, roads, administration**.
- **Difference from Private Goods:**
 - **Private goods (clothes, food, cars):** Rivalrous consumption & excludable (non-payers excluded).
 - **Public goods (parks, pollution control):** Non-rivalrous & non-excludable; benefits available to all, free-riders issue.
- **Free-Rider Problem:** Users consume benefits without paying → market fails → government steps in.

	<ul style="list-style-type: none"> ● Public Provision vs Production: <ul style="list-style-type: none"> ○ Public Provision: Financed through budget, no direct payment. ○ Public Production: Goods produced directly by government (can also be by private sector).
2.Redistribution Function	<ul style="list-style-type: none"> ● National Income Distribution: <ul style="list-style-type: none"> ○ National income → Private income (firms, households) + Public income (government). ○ Private income → Personal income → Personal disposable income. ● Government Role: <ul style="list-style-type: none"> ○ Taxes collected and transfer payments made. ○ Alters distribution of income → aims at fair distribution in society. ● Objective: Achieve equity and social justice through redistribution.
3.Stabilisation Function	<ul style="list-style-type: none"> ● Need for Intervention: <ul style="list-style-type: none"> ○ Aggregate demand fluctuations → impact on employment & prices. ○ Private decisions depend on income, credit availability, etc. ● Low Demand Situation: <ul style="list-style-type: none"> ○ Demand < Output capacity → unemployment persists (since wages & prices are rigid). ○ The government intervenes to increase demand (expansionary policies). ● High Demand Situation: <ul style="list-style-type: none"> ○ Demand > Output capacity → inflation rises. ○ The government uses restrictive policies to reduce demand. ● Objective: Ensure price stability, full employment, economic stability.

BUDGETARY REFORMS

1. **Merger of Railway Budget with General Budget**
 - From **FY 2017-18**, a separate Railway Budget was abolished and consolidated into the Union Budget as a single document. The merger was based on recommendations of the **Bibek Debroy Committee.**
 - This move ended a colonial-era convention (rooted in **Acworth Committee, 1920s**).
2. **Removal of Plan / Non-Plan Distinction**
 - From Budget 2016-17 onwards, classification between “Plan Expenditure” and “Non-Plan Expenditure” was removed.
3. **Advancement of Budget Presentation Date:**
 - The budget presentation was shifted earlier from the **last day of February** to **1st February.**
 - Objective: Get Parliamentary approval and Presidential assent before April 1 so that all allocations are available from Day 1.
 - This reform eliminated the need for a “**Vote on Account**” to provide interim funding (for the first 2 or 3 months) which constrained new scheme launches in April–May.

Key Fiscal Budget Components

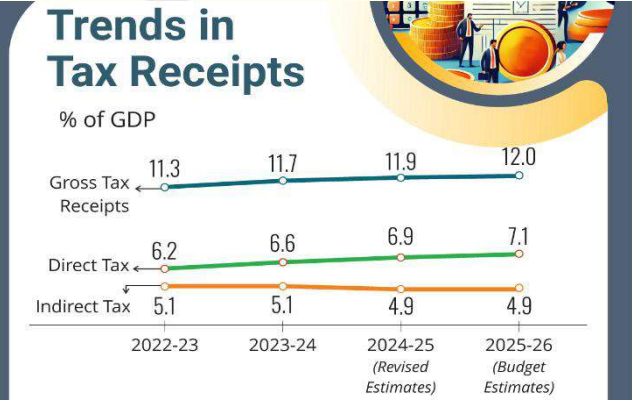
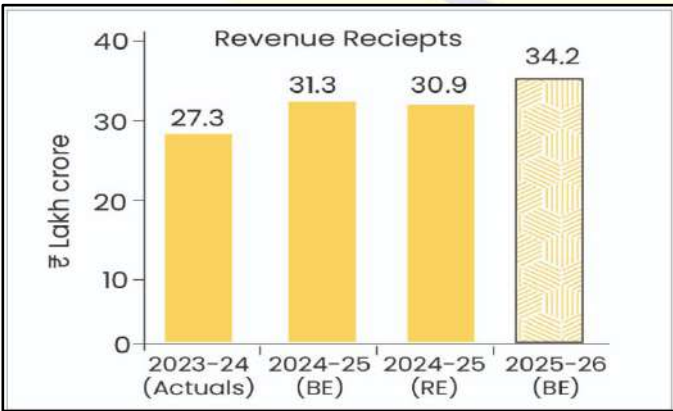


Revenue Budget: It consists of the **revenue receipts and revenue expenditures** of the Government. It is a detailed statement outlining a government's or organization's projected income (revenue receipts) and expenditures for a current fiscal year, focusing on recurring and day-to-day operational items rather than those affecting long-term assets or liabilities.

- For governments, it includes sources like taxes, duties, fees, and interest on investments, and covers routine expenses such as salaries, subsidies, and debt interest payments.
- Deals with **income and expenditure** that is **recurring** in nature + Regular operational expenses.
- **Examples:** Sales, purchase, salaries, wages, rent

Revenue Receipts:

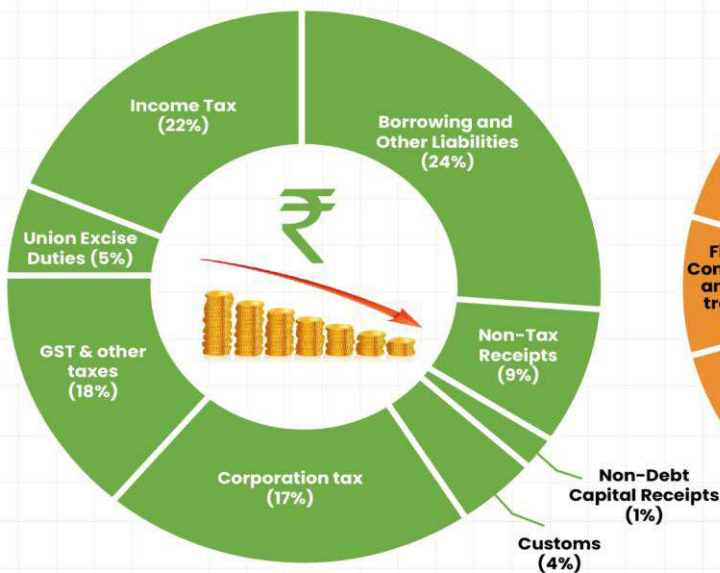
- Revenue receipts are current income receipts from all sources such as taxes, profits of public enterprises, grants, etc. Revenue receipts consist of **Tax revenues** and **Non-Tax revenues**.
- Revenue receipts are **non redeemable government receipts** that neither create any liability nor cause any reduction in the assets of the government.



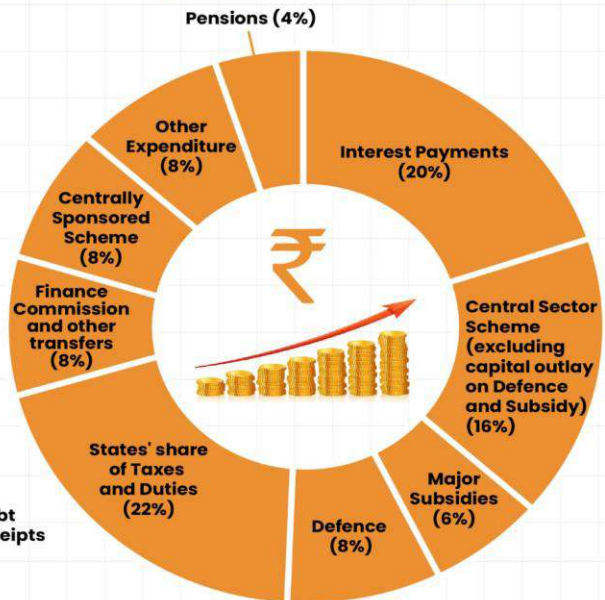
Riyasat IAS Mentorship

Tax Revenue	Non Tax Revenue
<ul style="list-style-type: none"> • Direct Taxes: Personal Income Tax, Corporation Tax. • Other Direct Taxes (Paper Taxes): Wealth tax, Gift tax, Estate duty (abolished). • Indirect Taxes: <ul style="list-style-type: none"> ○ Excise duties: Goods produced within the country. ○ Customs duties: Imports & exports. ○ Service tax: Now merged into GST (since 1 July 2017). • Progressive Taxation: Higher income → higher tax rates. • Corporate Tax: Proportional basis on profits. • Excise Policy: <ul style="list-style-type: none"> ○ Necessities exempted/low taxed. ○ Comforts moderately taxed. ○ Luxuries, tobacco, petroleum → heavily taxed. 	<ul style="list-style-type: none"> • Interest receipts on loans given by the government. • Dividends & profits from investments/PSUs • Fees and Charges from government services e.g. licences, passports. • Cash grants-in-aid from foreign countries/international organisations • Sales of Goods and Services: Income from government-provided goods/services. • Property Income: Revenue from the rent, lease, or sale of government assets.

RUPEE COMES FROM



RUPEE GOES TO

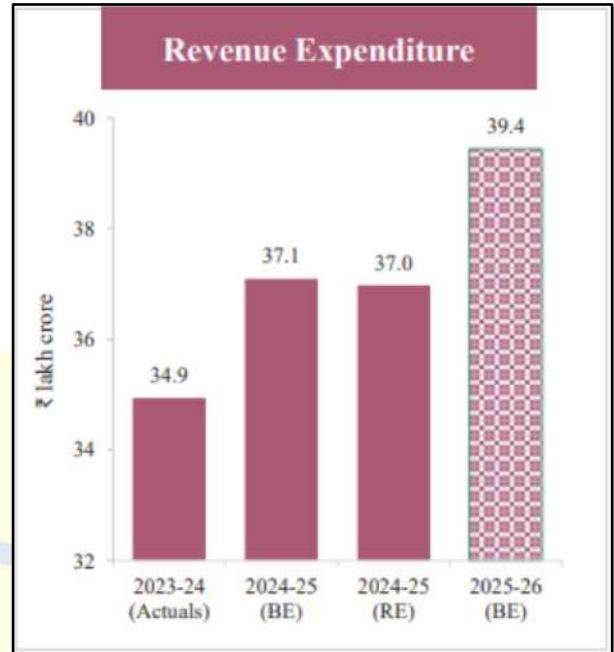


Revenue Expenditure: Government spending that does not create assets or reduce liabilities but is crucial for day-to-day operations and public services, including salaries, pensions, interest payments, and subsidies

- Does **not** create assets
- Spent on **maintenance and consumption**

Components of Non-Plan Revenue Expenditure

- **Interest Payments** → On market loans, external loans, reserve funds; largest component.
- **Defence Services** → Committed expenditure due to national security concerns.
- **Subsidies** → Key policy instrument for welfare enhancement.
 - **Implicit subsidies:** Through under-pricing of public goods/services (e.g., education, health).
 - **Explicit subsidies:** On exports, loan interest, food, fertilisers.
- **Salaries and Pensions** → For govt. employees.



Capital Budget: Capital receipts and capital expenditure together constitute the Capital Budget. It is a plan for receipts and expenditures related to long-term assets and liabilities.

- It includes capital receipts, such as borrowings and disinvestments, and capital expenditures, which are outlays for assets like infrastructure (roads, hospitals), machinery, and equipment.
- Estimates **inflows and outflows** on capital expenses.
- Capital expenses lead to **asset creation**.
- **Examples:** Plant & machinery, shares, furniture.

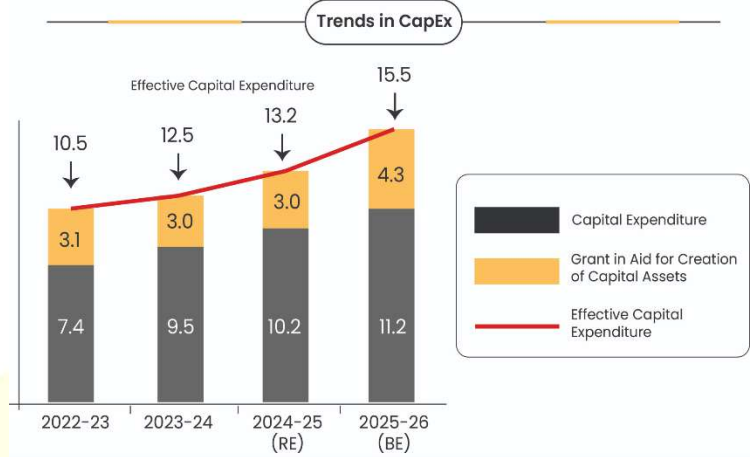
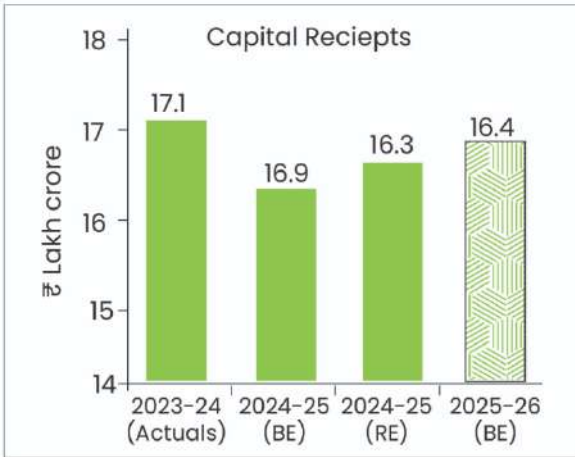
Capital Receipts: Capital receipts, are receipts of government which either create liability or cause any reduction in the assets of the government. e.g., borrowings, recovery of loan and disinvestment etc.

- Money raised through **borrowing (debt)** or **sale of assets (non-debt)**
- **Examples:** Loan recoveries, borrowings (domestic & foreign), disinvestment

Capital Expenditure: It is defined as government spending on assets like roads, buildings, and machinery, or to reduce liabilities, which provides benefits over a long period and enhances long-term growth potential

- Spent for **asset creation**
- Examples: Infrastructure, social sector, loan repayments

Riyasat IAS Mentorship



3 CENTRE'S CAPEX RISES AS REVENUE SHARE FALLS

Share of capital expenditure and revenue expenditure in total expenditure (in %)

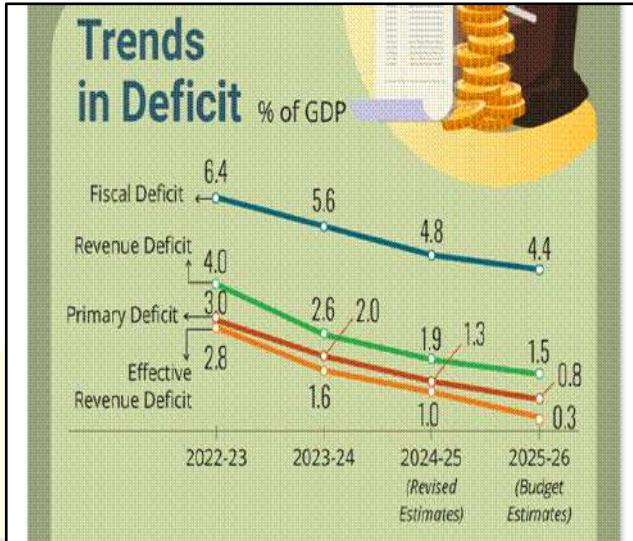


Source: RBI, Budget documents, BS calculations

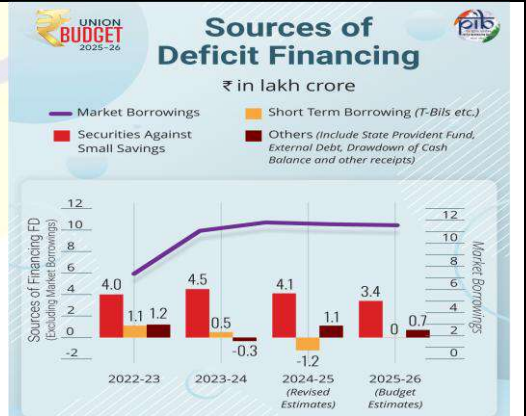
Key Fiscal Budget Components

Deficit:	<ul style="list-style-type: none"> Occurs when expenses exceed revenues, imports exceed exports or liabilities exceed assets.
Revenue Deficit (RD):	<ul style="list-style-type: none"> It occurs when a government's Revenue Expenditure exceeds its Revenue Receipts. It indicates the government is spending more on day-to-day operations and maintenance than it earns in revenue, requiring it to borrow to cover these operational expenses. Formula: RD = RR – RE = Difference between Revenue Receipts (RR) and Revenue Expenditure (RE)
Effective Revenue Deficit (ERD)	<ul style="list-style-type: none"> It is the difference between the Revenue Deficit and Grants-in-Aid for the Creation of Capital Assets, reflecting revenue expenditure that actually leads to productive, asset-creating investments Effective Revenue Deficit = Revenue Deficit – Net Grants for Capital Creation

Fiscal Deficit (FD)	<ul style="list-style-type: none"> • A fiscal deficit (FD) situation occurs when the government's expenditure exceeds its income. <ul style="list-style-type: none"> ○ It is the difference between total expenditure of the government and its total revenue (excluding borrowings). ○ Fiscal deficit is the gap between total expenditure and total income of the government. • Fiscal deficit = Total budget expenditure – Total budget receipts excluding borrowings OR Fiscal Deficit • FD = (Revenue Receipts + Non-debt capital receipts) – Total Expenditure • Represents total borrowing requirement of government.
Budget Deficit (BD)	<ul style="list-style-type: none"> • Formula: BD = Budgetary Receipt – Budgetary Expenditure • Difference between total budgeted receipts and expenditure
Primary Deficit (PD)	<ul style="list-style-type: none"> • It is a fiscal deficit minus interest payments on the government's previous borrowings. • It indicates the government's borrowing requirement for the current fiscal year's expenditure, excluding the burden of past debts • Formula: PD = Fiscal Deficit – Interest Payments • Indicates government borrowing excluding interest liability

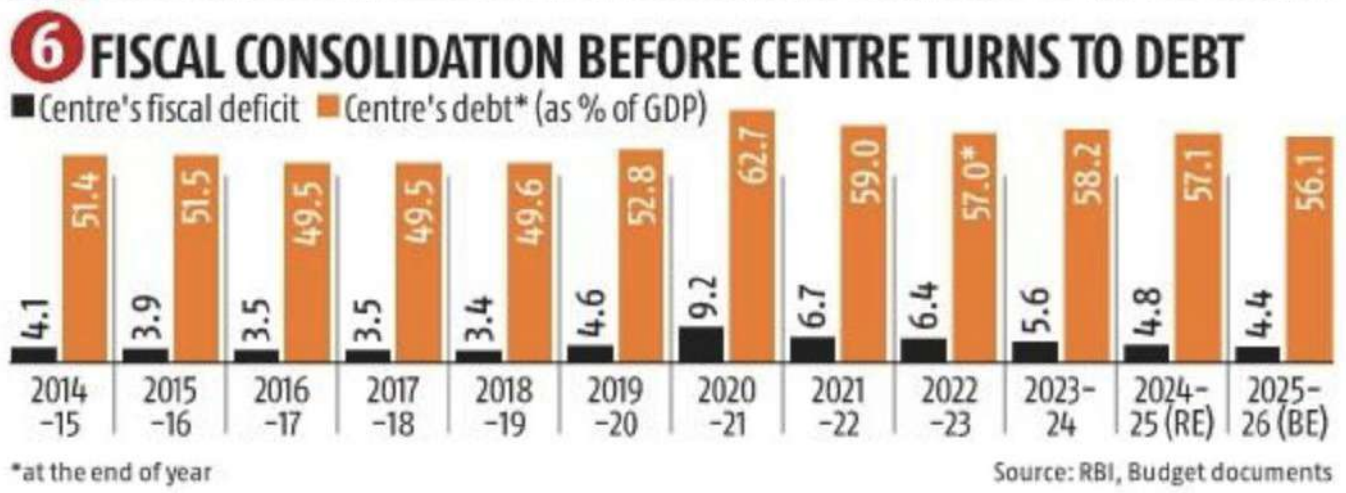


Deficit Financing: It is a fiscal strategy where a government funds its budget deficit, the gap between its total expenditure and total revenue, by borrowing or printing new money.	<p>How does the government manage its deficits?</p> <ol style="list-style-type: none"> 1. Monetized deficit – Borrowings made from RBI through printing fresh currency. The printed money is called high power money. FRBM act disallow RBI to do this under normal conditions 2. Ways and Means Advances (WMA): The Reserve Bank of India gives temporary loan facilities to the centre as a banker to government against adhoc treasury bill. There is no collateral but penal interest rate is charged.
---	---



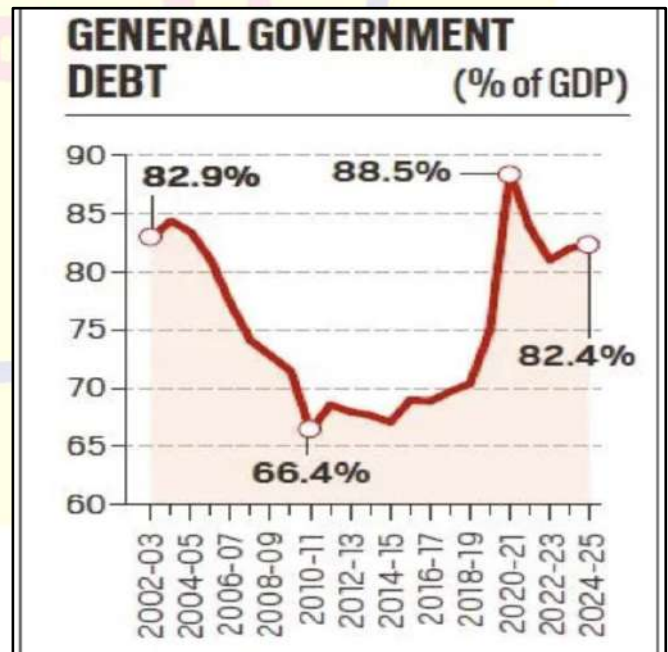
Fiscal Responsibility and Budget Management Act (FRBMA), 2003: Mandates **3 policy statements** along with the Budget

1. **Medium-term Fiscal Policy Statement:** Sets **3-year rolling targets** for fiscal indicators.
 - Examines if **revenue expenditure** can be met by **revenue receipts** sustainably.
 - Reviews utilisation of **capital receipts (incl. market borrowings)**.
2. **Fiscal Policy Strategy Statement:** Lays down **government fiscal priorities**.
 - Examines current policies & **justifies deviations** in fiscal measures.
3. **Macroeconomic Framework Statement:** Assesses economy's prospects re: **GDP growth, fiscal balance of Centre, external balance**.



Government Debt:

- **Government liabilities** are classified as:
 - **Public Debt:** Contracted against **Consolidated Fund of India**
 - **Other Liabilities:** Liabilities in **Public Account**
- **Public debt** is classified into:
 - **Internal debt:** Borrowed within country via **Treasury bills, market loans**
 - **External debt:** Loans from foreign countries, **international financial institutions, external commercial borrowings (largest borrowing), NRI deposits, bilateral and multilateral debt, trade credit**
- **Rupee debt:** Part of external debt denominated in Rupees
- **Other Liabilities:** Include **Provident Funds, Reserve Funds Deposits, Other Accounts**
- **Government debt as a percent of GDP:** Indicator used by investors to assess a country's **debt sustainability**.



Various Budgeting Techniques

Type	Description
Incremental Budgeting	<ul style="list-style-type: none"> Adds or subtracts a % to last year's actuals to obtain current year's budget. Simple and widely used.
Activity Based Budgeting	<ul style="list-style-type: none"> A top-down approach based on the number of inputs required to meet outputs or targets.
Value Proposition Budgeting	<ul style="list-style-type: none"> Focuses on ensuring that all budgeted items deliver value for the business.
Zero-Based Budgeting	<ul style="list-style-type: none"> Assumes all departmental budgets are zero initially and must be justified from scratch. Avoids unnecessary expenditures.
Gender Budgeting	<ul style="list-style-type: none"> Involves estimating and prioritizing expenditure for women empowerment.
Outcome-Performance Budgeting	<ul style="list-style-type: none"> Refers to suggesting and listing estimated outcomes of each government programme or scheme.

Finance Commission:

- It is a **quasi-judicial body** under **Article 280** of Indian Constitution, constituted **by the President** every five years, to review **tax devolution**.
- It consists of a chairman and four members appointed by the President, with qualifications defined by Parliament.
- 15th Finance Commission:**
 - Term: **2020–2026** (extended by 1 year)

Major Recommendations of 15th Finance Commission:

Vertical Devolution:

- Recommended share: **41%** (1% less than 14th FC)
- The 1% cut is due to allocation for **Jammu & Kashmir and Ladakh** (Transformed into UTs from states under Reorganisation of J&K Act 2019).

Horizontal Devolution Criteria:

Criteria	Weight
Population	15%
Area	15%
Forest & Ecology	10%
Income Distance	45%
Tax and Fiscal Efforts	2.5%
Demographic Performance	12.5%

- **Other Recommendation:** Creation of a non-lapsable defence and internal security fund under Public Accounts of India

HOW THE BOOTY IS DIVIDED

FORMULA THAT DECIDES A STATE'S SHARE

Weight in 15th FC

Weight in 14th FC

*17.5% according to 1971 population, 19% by 2011 population

STATES' SHARE IN DIVISIBLE POOL (%)

*Effective share does not change due to change in J&K status

Resources Transferred to States and UTs

₹ in lakh crore

	Monetary Policy	Fiscal Policy
Tool	Interest rates	Tax and government spending
Effect	Cost of borrowing/mortgages	Budget deficit
Distribution	Higher interest rates hit homeowners but benefit savers	Depends which taxes you raise.
Exchange rate	Higher interest rates cause appreciation	No effect on exchange rate
Supply-side	Limited impact	Higher taxes may affect incentives to work
Politics	Monetary policy set by independent Central Bank	Changing tax and government spending highly political.
Liquidity trap	Cuts in interest rates may not work in liquidity trap	Fiscal policy advised in very deep recessions