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Impact of FRBM Act 2003 on Public Expenditure in India

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Abstract

India is a developing nation experiencing lower socio-economic indicators, and widespread poverty and inequality exist in the economy. So, the development of the nation requires huge public expenditure in the social and infrastructure sectors. The contribution of taxes to the GDP ratio is very low in India, and the government could not meet the various public works with limited resources. In India, interest payments, defence, pensions, salaries, and subsidies are the major components of public expenditure and collectively occupy more than 60 percent of total public expenditure. The government plays a vital role in establishing a welfare society, and it has spent a huge amount on the development of the economy in various ways. Insufficient funds from the government require better utilisation of available sources of public expenditure and better management of the fiscal deficit. In 2003, the Fiscal Responsibility and Budget Management (FRBM) Act was enacted to maintain the fiscal deficit at 3 percent, establish financial discipline in the economy, reduce the fiscal deficit, and improve the administration of public resources. This act came into force in 2004. This study aims at understanding the trends and growth rate of public expenditure in India. The study found that after implementing the FRBM Act 2003 in India, the ACGR of subsidies, loans, advances, and capital outlays has increased, which is conducive to enhancing economic development.

Keywords: Public Expenditure, Revenue Expenditure, Capital Expenditure, Subsidies, etc.

Introduction

The government participated in all economic activities, directly or indirectly, in every type of economy, whether it was socialist, capitalist, or mixed. The government plays a vital role in establishing a welfare society, and it has spent a huge amount on the development of the economy in various ways. Insufficient funds from the government require better utilisation of available sources of public expenditure and better management of the fiscal deficit. The main aim of the government is to establish a welfare state in a country. So, the government has spent a huge amount of money on developmental activities. The main features of developing countries are lower socio-economic indicators and widespread poverty and inequality in the economy. Thus, developing countries need a huge amount of public expenditure to maintain the smooth functioning of the economy. After independence, the Indian government has been continuously active in creating a welfare state. This study aims at understanding the trends and growth rate of public expenditure in India.

Review of Literature

Seshaiah et al, (2018) examined the Central and State Government expenditure and Economic Growth in India during 1980-81 to 2015-2016. They found that the GDP growth rate except FDI growth rate was affected by all the explanatory variables positively and significantly.

Mohanty and Mishra (2017) have examined the Co-integration of Government Expenditure and Revenue of India. They concluded that this study shows one-way causality running from tax revenue to expenditure both in short run as well as in the long run by using the vector error correction model.

Objectives

- To examine the trends in public expenditure in India before and after the FRBM Act 2003.
- To find out the growth rate of public expenditure in India before and after the FRBM Act 2003.

Research Methodology

The data collected for this study is secondary.

The data has been collected from the Handbook of Statistics on the Indian Economy, the RBI, and the Department of Economic Affairs. The regression analysis is used to determine the compound growth rate of public expenditure in India. In 2003, the Fiscal Responsibility and Budget Management (FRBM) Act was enacted to establish financial discipline in the economy, reduce fiscal deficits, and improve the administration of public resources. This act came into force in 2004. Based on the FRBM Act, the study period from 1985–86 to 2022–23 has been bifurcated into a period of pre-reform from 1985–86 to 2003–04 and a period of post-reform from 2004–05 to 2022–23.

Table 1 Share of Revenue and Capital Expenditure in Total Expenditure before FRBM Act 2003

Year	Revenue Expenditure (Rs. in crore)	% of Revenue Expenditure to Total	Capital Expenditure (Rs. in crore)	% of Capital Expenditure to Total	Total Expenditure
1985-86	33924	64.41	18742	35.58	52666
1986-87	40860	64.94	22056	35.05	62916
1987-88	46174	67.64	22087	32.35	68261
1988-89	54106	68.39	25005	31.60	79111
1989-90	64210	69.11	28698	30.88	92908
1990-91	73516	69.81	31782	30.18	105298
1991-92	82292	73.86	29122	26.13	111414
1992-93	92702	75.60	29916	24.39	122618
1993-94	108169	76.25	33684	23.74	141853
1994-95	122112	75.96	38627	24.03	160739
1995-96	139861	78.45	38414	21.54	178275
1996-97	158933	79.06	42074	20.93	201007
1997-98	180335	77.71	51718	22.28	232053
1998-99	216461	77.49	62879	22.50	279340
1999-00	249078	83.56	48975	16.43	298053
2000-01	277839	85.33	47753	14.66	325592
2001-02	301468	83.20	60842	16.79	362310
2002-03	338713	81.96	74535	18.03	413248
2003-04	362074	76.84	109129	23.15	471203

Source: Handbook of statistics on Indian Economy, RBI 2022-23

The total public expenditure is classified into revenue expenditure and capital expenditure. The revenue expenditure is less productive. Expenditure on pensions, salaries, subsidies, interest payments, etc. comes under revenue expenditure incurred for creating financial assets. The above table clearly

indicates that revenue expenditure is greater than capital expenditure and also explores the fact that the share of revenue expenditure in total expenditure is dribbled with that of capital expenditure. The gap between revenue expenditure and capital expenditure widened before the FRBM Act of 2003.

The revenue expenditure and capital expenditure of the central government before the FRBM Act 2003 and its share in total expenditure are shown in Table 1. The revenue expenditure of the government has increased from Rs. 33924 crores in 1985–86 to Rs. 362074 crores in 2003–04, registering a 10-fold increase over the reference period. The share of revenue expenditure in the total expenditure was 85.33 percent in 2000–01. But their share has increased to 76.84 percent in 2003–04.

The capital expenditure of the government has increased from Rs. 18742 crores in 1985–86 to Rs. 109129 crores in 2003–04, registering 5-fold increases over the reference period. The share of capital expenditure in the total expenditure was 35.58 percent in 2000–01. But their share has

been reduced to 18.03 percent in 2003–04. It was inferred that the government has increased its expenditure more on revenue expenditure than on capital expenditure. The government has taken a number of policy measures to develop the rural area, create employment opportunities, and increase their expenditure on defence expenditures, interest payments, and subsidies.

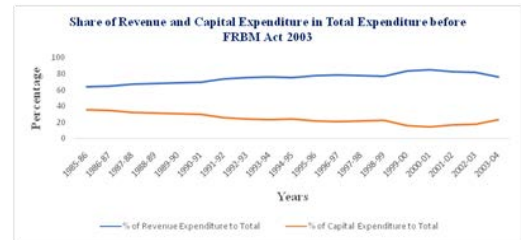


Table 2 Share of Revenue and Capital Expenditure in Total Expenditure after FRBM Act 2003

Year	Revenue Expenditure (Rs. in crore)	% of Revenue Expenditure to Total	Capital Expenditure (Rs. in crore)	% of Capital Expenditure to Total	Total Expenditure
2004-05	384329	77.22	113331	22.77	497660
2005-06	439376	86.87	66362	13.12	505738
2006-07	514609	88.21	68778	11.78	583387
2007-08	594433	83.40	118238	16.59	712671
2008-09	793798	89.80	90158	10.19	883956
2009-10	911809	89.00	112678	10.99	1024487
2010-11	1040723	86.92	156605	13.07	1197328
2011-12	1145785	87.84	158580	12.15	1304365
2012-13	1243514	88.16	166858	11.83	1410372
2013-14	1371772	87.96	187675	12.03	1559447
2014-15	1466992	88.17	196681	11.82	1663673
2015-16	1537761	85.87	253022	14.12	1790783
2016-17	1690584	85.59	284610	14.40	1975194
2017-18	1878833	87.71	263140	12.28	2141973
2018-19	2007399	86.70	307714	13.29	2315113
2019-20	2350604	87.50	335726	12.49	2686330
2020-21	3083519	87.85	426317	12.14	3509836
2021-22	3167289	84.01	602711	15.98	3770000
2022-23	3194663	80.98	750246	19.01	3944909

Source: Handbook of statistics on Indian Economy, RBI 2022-23

The above table shows the revenue expenditure and capital expenditure of the central government after the FRBM Act 2003 and its share in total expenditure. The revenue expenditure of the government has increased from Rs. 384329 crores

in 2004–05 to Rs. 3194663 crores in 2022–23, registering eight-fold increases over the reference period. The share of revenue expenditure in total expenditure was the highest at 89.80 percent in 2008–09. But its share has been reduced to 80.98

percent, and the share of capital expenditure has been increased to 19.01 percent in 2022–23.

The capital expenditure of the government has increased from Rs. 66362 crores in 2005–06 to Rs. 750246 crores in 2022–23, registering an 11-fold increase over the reference period. The share of capital expenditure in total expenditure was 13.12 percent in 2005–06. But their share has increased to 19.01 percent in 2022–23. It is clearly observed

that, compared to before implementing the FRBM Act, the government has reduced its share of capital expenditure to total expenditure.

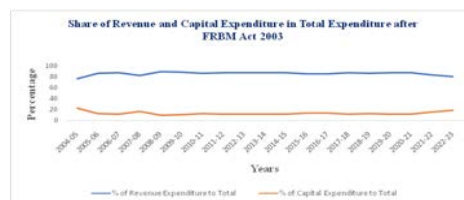


Table 3 Distribution of Revenue Expenditure before FRBM Act 2003

Year	Defence Expenditure (Rs. in Crore)	% of Defence Expenditure to Total	Interest payments (Rs. in Crore)	% of Interest payments to Total	Subsidies (Rs. in Crore)	% of Subsidies to Total	Total
1985-86	7021	36.32	7512	38.86	4796	24.81	19329
1986-87	9179	38.44	9246	38.72	5451	22.83	23876
1987-88	8861	33.96	11251	43.12	5980	22.91	26092
1988-89	9558	30.27	14278	45.22	7732	24.49	31568
1989-90	10194	26.52	17757	46.21	10474	27.25	38425
1990-91	10874	24.41	21498	48.27	12158	27.30	44530
1991-92	11442	22.75	26596	52.88	12253	24.36	50291
1992-93	12109	22.42	31075	57.53	10824	20.04	54008
1993-94	14978	23.65	36741	58.02	11605	18.32	63324
1994-95	16426	22.70	44060	60.90	11854	16.38	72340
1995-96	18841	23.10	50045	61.36	12666	15.53	81552
1996-97	20997	21.87	59478	61.97	15499	16.14	95974
1997-98	26174	23.71	65637	59.48	18540	16.80	110351
1998-99	29861	22.73	77882	59.29	23593	17.96	131336
1999-00	35216	23.48	90249	60.18	24487	16.32	149952
2000-01	37238	22.79	99314	60.78	26838	16.42	163390
2001-02	38059	21.53	107460	60.80	31210	17.65	176729
2002-03	40709	20.14	117804	58.30	43533	21.54	202046
2003-04	43203	20.41	124088	58.63	44323	20.94	211614

Source: Handbook of statistics on Indian Economy, RBI 2022-23

Table 3 exhibits the distribution of revenue expenditures before the FRBM Act of 2003. The major share of revenue expenditure is used to finance mainly three components: defence expenditure, interest payments for internal and external debt, and providing subsidies. Among these three components, the share of interest payments played a major role in the total revenue expenditure before the implementation of the RFBM Act 2003. Defence expenditures on administrative and defence services are considered

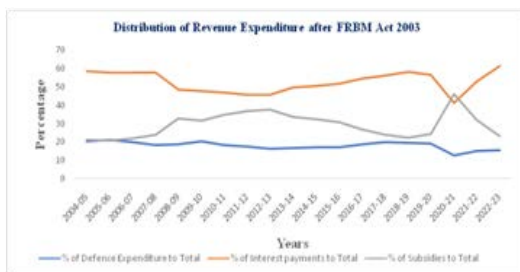
revenue expenditures. The government has spent a huge amount on interest payments; it has increased from Rs.7512 crore in 1985–86 to Rs. 124088 crore in 2003–04.



Table 4 Distribution of Revenue Expenditure after FRBM Act 2003

Year	Defence Expenditure (Rs. in Crore)	% of Defence Expenditure to Total	Interest payments (Rs. in Crore)	% of Interest payments to Total	Subsidies (Rs. in Crore)	% of Subsidies to Total	Total
2004-05	43862	20.23	126934	58.56	45957	21.20	216753
2005-06	48211	21.11	132630	58.07	47522	20.80	228363
2006-07	51682	19.94	150272	58.00	57125	22.04	259079
2007-08	54219	18.30	171030	57.74	70926	23.94	296175
2008-09	73305	18.54	192204	48.63	129708	32.81	395217
2009-10	90669	20.36	213093	47.87	141351	31.75	445113
2010-11	92061	18.43	234022	46.85	173420	34.71	499503
2011-12	103011	17.33	273150	45.97	217941	36.68	594102
2012-13	111277	16.32	313170	45.95	257079	37.72	681526
2013-14	124374	16.51	374254	49.68	254632	33.80	753260
2014-15	136807	17.15	402444	50.46	258258	32.38	797509
2015-16	145937	17.13	441659	51.85	264106	31.00	851702
2016-17	165410	18.77	480714	54.56	234809	26.65	880933
2017-18	186127	19.81	528952	56.29	224455	23.89	939534
2018-19	195572	19.53	582648	58.19	222954	22.26	1001174
2019-20	207572	19.18	612070	56.57	262304	24.24	1081946
2020-21	205789	12.51	679869	41.35	758165	46.12	1643823
2021-22	229567	14.99	813791	53.14	487872	31.86	1531230
2022-23	233001	15.23	940651	61.50	355639	23.25	1529291

Source: Handbook of statistics on Indian Economy, RBI 2022-23



The distribution of revenue expenditure after the FRBM Act 2003 is shown in the above table 4. It reflects that the share of defence expenditure in the total revenue expenditure was declined, but it has

been increased to Rs. 233001 crore in 2022–23, and at the same time, the share of subsidies in the total revenue expenditure has been increased. So, the implementation of the FRBM Act 2003 helps the government change its expenditure pattern to spend more on granting subsidies to encourage production levels in energy, agriculture, and transportation. The share of subsidies in total expenditure has increased from 20.80 percent in 2005–06 to 46.12 percent in 2020–21 due to the COVID-19 pandemic situation in India. It is also noted that the largest item of interest payment was tremendously increased to Rs. 940651 crore, which is 61.50 percent of total revenue expenditure in 2022–23.

Table 5 Distribution of Capital Expenditure before FRBM Act 2003

Year	Loans and advances (Rs. in crore)	% of Loans & advances to Total	Capital outlay (Rs. in crore)	% of Capital outlay to Total	Defence Expenditure (Rs. in crore)	% of Defence Expenditure to Total	Total
1985-86	11087	56.25	7655	38.84	967	4.90	19709
1986-87	12797	54.79	9259	39.64	1298	5.55	23354
1987-88	12793	50.77	9294	36.88	3107	12.33	25194
1988-89	14750	51.23	10255	35.62	3783	13.14	28788
1989-90	16890	51.30	11808	35.86	4222	12.82	32920
1990-91	19652	54.08	12130	33.38	4552	12.52	36334
1991-92	17723	52.63	11043	32.79	4905	14.56	33671
1992-93	16297	46.35	13385	38.07	5473	15.56	35155
1993-94	20454	50.61	13089	32.39	6867	16.99	40410
1994-95	23736	52.22	14891	32.76	6819	15.00	45446
1995-96	24316	52.37	14099	30.36	8015	17.26	46430
1996-97	27878	55.11	14196	28.06	8508	16.82	50582
1997-98	34193	56.21	17526	28.81	9104	14.96	60823
1998-99	44037	60.39	18841	25.84	10036	13.76	72914
1999-00	24938	40.99	24037	39.51	11855	19.48	60830
2000-01	23008	38.25	24745	41.14	12384	20.59	60137
2001-02	34284	44.49	26558	34.46	16207	21.03	77049
2002-03	31668	41.82	29101	38.43	14953	19.74	75722
2003-04	28768	36.05	34150	42.80	16863	21.13	79781

Source: Handbook of statistics on Indian Economy, RBI 2022-23

The distribution of capital expenditure before the FRBM Act 2003 is depicted in the above table. The government's expenditure on loans and advances has increased from Rs. 11087 crores in 1985–86 to Rs. 44037 crores in 1998–99, whereas it has sharply declined to Rs. 28768 crores in 2003–04. Among loans and advances, capital outlay, and defence expenditure, the share of capital outlay was the highest, i.e., 42.80 percent of the total capital expenditure in the study period. The defence expenditure also comes under revenue expenditure because the government has spent huge long-term

expenditures on purchasing new weapons, aircraft, warships, and other military hardware. It has increased from Rs.967 crore in 1985–86 to Rs. 16863 crore in 2003–04.

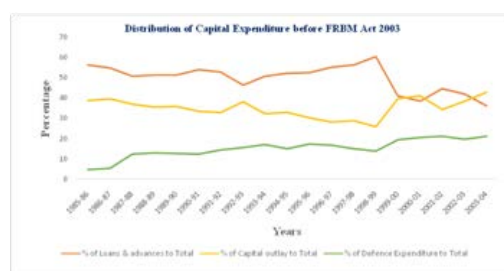
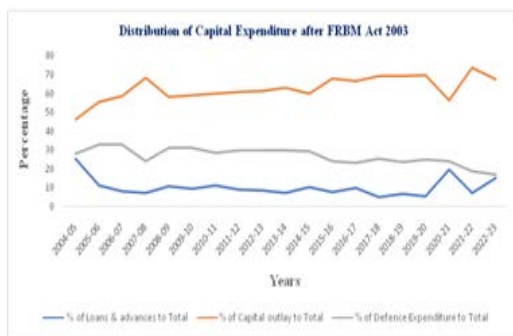


Table 6 Distribution of Capital Expenditure after FRBM Act 2003

Year	Loans and advances (Rs. in crore)	% of Loans & advances to Total	Capital outlay (Rs. in crore)	% of Capital outlay to Total	Defence Expenditure (Rs. in crore)	% of Defence Expenditure to Total	Total
2004-05	28910	25.52	52338	46.21	31994	28.25	113242
2005-06	11337	11.48	55025	55.74	32338	32.76	98700
2006-07	8524	8.30	60254	58.72	33828	32.96	102606
2007-08	11298	7.25	106940	68.68	37462	24.06	155700
2008-09	14107	10.76	76051	58.02	40918	31.21	131076
2009-10	15647	9.55	97031	59.24	51112	31.20	163790
2010-11	24985	11.42	131619	60.19	62056	28.38	218660
2011-12	20737	9.15	137843	60.86	67902	29.98	226482
2012-13	20800	8.76	146058	61.53	70499	29.70	237357
2013-14	19198	7.19	168478	63.14	79125	29.65	266801
2014-15	29218	10.48	167463	60.11	81887	29.39	278568
2015-16	26337	7.90	226685	68.07	79958	24.01	332980
2016-17	36810	9.92	247800	66.79	86371	23.28	370981
2017-18	18027	5.09	245113	69.32	90445	25.57	353585
2018-19	28221	7.00	279492	69.36	95231	23.63	402944
2019-20	24414	5.46	311312	69.67	111092	24.86	446818
2020-21	110491	19.70	315826	56.33	134305	23.95	560622
2021-22	55255	7.45	547457	73.82	138851	18.72	741563
2022-23	140057	15.51	610189	67.60	152370	16.88	902616

Source: Handbook of statistics on Indian Economy, RBI 2022-23



The below table 6 shows the government's capital expenditure on loans and advances, capital outlay, and defence expenditure. Defence expenditure also comes under capital expenditure when the government has spent a huge amount on purchasing new weapons, aircraft, warships, and other military hardware, whereas these are long-term expenditures. After the FRBM Act 2003, there was a fluctuation in the expenditure on loans and advances. Currently, the government has spent more on loans and advances; it reaches Rs.140057crore.

Table 7 Distribution of Developmental Expenditure before FRBM Act 2003

Year	Economic services (Rs. in crore)	% of Economic services to Total	Social services (Rs. in crore)	% of Economic services to Total	Total
1993-94	27571	85.09	4830	14.90	32401
1994-95	33897	85.23	5873	14.76	39770
1995-96	35029	82.06	7655	17.93	42684
1996-97	37253	79.38	9672	20.61	46925
1997-98	44246	78.88	11845	21.11	56091
1998-99	54375	78.76	14656	21.23	69031
1999-00	60956	77.97	17221	22.02	78177
2000-01	71731	80.22	17679	19.77	89410
2001-02	80868	84.23	15130	15.76	95998
2002-03	103820	82.51	22007	17.48	125827
2003-04	108071	81.91	23859	18.08	131930

Source: Handbook of statistics on Indian Economy, RBI 2022-23

Table 7 explains the distribution of developmental expenditure before the FRBM Act of 2003. Developmental expenditure refers to the expenditure incurred by the government to develop the economy. It has been discussed under two headings, namely expenditure on economic services and social services.

The amount spent by the government on economic services has been increasing steadily, but there have been fluctuations in its share of total expenditure. The government has spent more of Rs. 108071 crore on economic services than social services, which is four fold of the amount spent on social services.

Table 8 Distribution of Developmental Expenditure after FRBM Act 2003

Year	Economic Services (Rs. in crore)	% of Economic Services to Total	Social Services (Rs. in crore)	% of Economic Services to Total	Total
2004-05	115030	79.36	29906	20.63	144936
2005-06	133053	77.66	38264	22.33	171317
2006-07	142772	76.53	43762	23.46	186534
2007-08	172955	73.72	61648	26.27	234603
2008-09	273222	75.26	89797	24.73	363019
2009-10	304440	74.78	102628	25.21	407068
2010-11	404312	76.38	124990	23.61	529302
2011-12	436943	79.36	113612	20.63	550555
2012-13	458222	79.33	119346	20.66	577568
2013-14	478376	78.01	134840	21.98	613216
2014-15	459786	88.11	62038	11.88	521824
2015-16	495234	84.41	91462	15.58	586696
2016-17	569910	84.40	105303	15.59	675213
2017-18	623730	84.61	113382	15.38	737112
2018-19	631826	83.71	122949	16.28	754775
2019-20	719731	82.46	153058	17.53	872789
2020-21	1323898	88.34	174640	11.65	1498538
2021-22	1251202	83.61	245141	16.38	1496343
2022-23	1207408	83.40	240197	16.59	1447605

Source: Handbook of statistics on Indian Economy, RBI 2022-23

The above table shows that after the FRBM Act 2003, the government has increased the amount spent on social services from Rs. 29906 crores in 2004–05 to Rs. 240197 crores in 2022–23. But its share of total

expenditure has been reduced from 20.63 percent in 2004–05 to 16.59 percent in 2022–23. The share of economic services in total expenditure has increased from 79.36 percent to 83.40 percent in 2022–23.

Table 9 Growth Rate of Public Expenditure in India before and after FRBM Act 2003

Variables		Regression Coefficients Before		Regression Coefficients After		R2 before	R2 after	AGR (%) before	AGR (%) after
		a	b	a	b				
Revenue Expenditure		10.36961* (529.3007)	0.133274* (77.56352)	9.787101* (134.1453)	0.077674* (12.46865)	0.99	0.91	14.26	8.08
Capital Expenditure		12.93965* (244.6617)	0.11676* (24.7301)	2.5627 (627.3086)	0.00795* (22.79023)	0.97	0.97	11.82	0.79
Major distribution of Revenue Expenditure	Defence Expenditure	8.713524* (166.6117)	10.6977* (197.6612)	(197.6612) (197.6612)	(20.78256) (20.78256)				
	Interest Payments	9.015886* (143.9276)	11.61443* (464.517)	11.61443 (464.517)	0.111471* (52.21431)	0.98	0.99	16.78	11.79
	Subsidies	8.457654* (102.2479)	0.99538* (59.29913)	0.99538 (59.29913)	0.114871* (7.255611)	0.94	0.76	11.84	12.17
Major distribution of Capital Expenditure	Loans and Advances	9.422959* (93.25471)	8.898745* (41.80188)	8.898745 (41.80188)	0.117102* (6.442505)	0.72	0.72	5.83	12.42
	Capital Outlay	8.895902* (164.9818)	10.75613* (136.0104)	10.75613 (136.0104)	0.125597* (18.6002)	0.94	0.96	7.63	13.38
	Defence Expenditure	7.599464* (73.34073)	10.27124* (203.3531)	10.27124 (203.3531)	0.087689* (20.3327)	0.92	0.96	12.5	9.16
Major distribution of Developmental Expenditure	Economic Services	10.04122* (209.7525)	11.75229* (113.9345)	11.75229 (113.9345)	0.122078* (13.86099)	0.98	0.92	15.29	12.98
	Social Services	8.570782* (75.61419)	10.75337* (68.32011)	10.75337 (68.32011)	0.07788* (5.795036)	0.91	0.68	15.38	8.09

Source: Computed from collected data

Note: 1. (Table value = 4.1) * Significant at one per cent level

2. Figures in parentheses indicates 't' value

The growth rate of public expenditure in India before and after the FRBM Act 2003 has been positive for the type of expenditure during the study period. The growth rate of interest payments showed a significant growth rate of 16.78 percent per annum before implementing the FRBM Act 2003. There has been a varying trend in public expenditure during the study period. After implementing the FRBM Act 2003, the annual growth rate of capital expenditure was tremendously reduced from 11.82 to 0.79, followed by revenue expenditure, which decreased from 14.26 to 8.08. The growth rate of revenue expenditure on interest payments was also reduced from 16.78 to 11.79, followed by developmental

expenditure on social services, which decreased from 15.38 to 8.09. The growth rate of capital expenditure on loans and advances increased from 5.83 to 12.42, followed by capital outlay, which increased from 7.63 to 13.38. The growth rate of revenue expenditure on subsidies was also increased from 11.84 to 12.17. The AGR is computed for the different categories of government expenditure, which are significant at the 1 percent level.

Conclusion

This study is undertaken mainly to examine the growth rate of public expenditure before and after the FRBM Act 2003 in India during the period from

1984–85 to 2022–23. The present study observed that public expenditure in India is showing an increasing tendency in the long term, but its share in the rate of total expenditure is showing a decreasing trend. The government has spent more on revenue expenditure than capital expenditure. When the government places more concentration on revenue expenditure, it adversely affects the development of the nation. It should be observed that the government has shifted its expenditure from development to non-developmental activities. After implementing the FRBM Act 2003 in India, the AGR of subsidies, loans, advances, and capital outlays has increased, which is conducive to enhancing economic development. So, the government would take policy measures to give equal importance to all public expenditures and consider all macro-economic variables seriously while preparing the union budget in the future.

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