A STUDY ON IMPACT OF FISCAL DEFICIT AND INFLATION IN INDIA

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This study co-relates between consumer price index, fiscal deficit inflation, and government expenditure in India. The main objective of this study is to analyse the factors that influences increase in fiscal deficit in India, by considering all factors that can affect fiscal deficit. This study finds that inflation is not at all cause of fiscal deficit. However, government expenditure is an important determinant to calculate fiscal deficit.

Key words: Consumer Price Index, Fiscal deficit, inflation, government expenditure.

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- **Introduction:**

The relationship between Consumer Price Index /fiscal deficit, government expenditure and inflation has acquired a prominent place in literature on monetary economics. This study has made an attempt to examine the direction of causality among the fiscal deficit, government expenditure, money supply, and inflation. However, we have found conflicting results for India. Inflation is generally associated with rapid monetary expansion. Hence, these two problems of fiscal deficit and inflation have been given a lot of importance in budget of Central government in India.

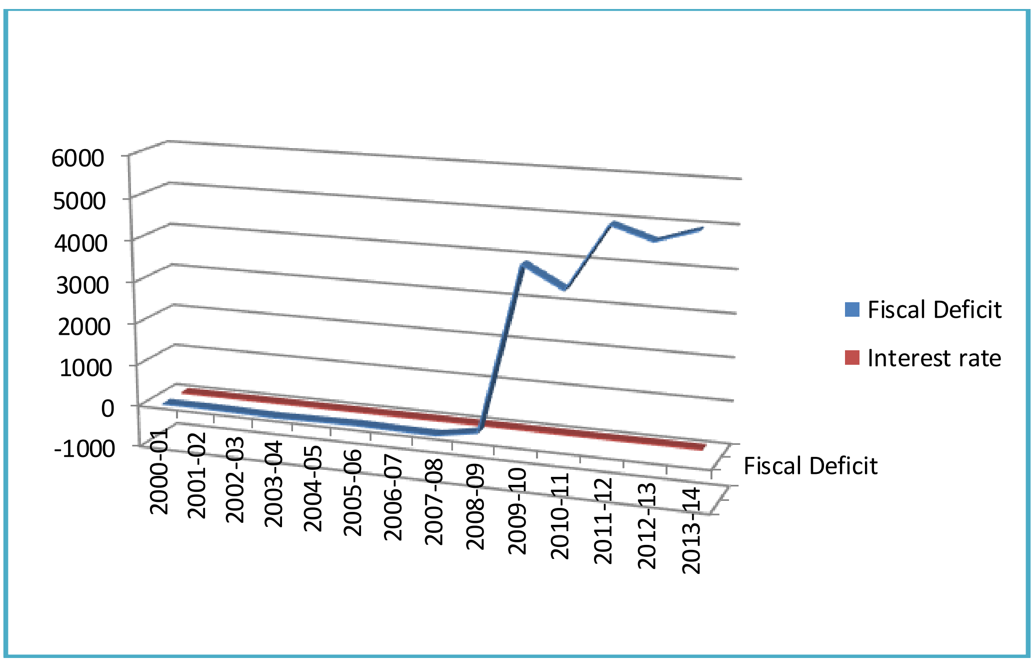
- **Methodology**

This study has used time series data sourced from Handbook of statistics of Reserve Bank of India (RBI) and also other references of journals and magazines. In this study inflation has been measured through consumer price index of all level. Government expenditure has been measured by total expenditure of central government. The period 2000 to 2015 has been taken for analysis in this study. The study is basically analytical whereby the statistics of various economic indicators have been analysed with their inter relationships and inferences are drawn.

CPI and Fiscal Deficit:

Year	CPI	Fiscal Deficit
2000-01	4	13.46
2001-02	3.7	18.63
2002-03	4.4	2.92
2003-04	3.8	-15.03
2004-05	3.8	2.05
2005-06	4.2	16.41
2006-07	6.1	-2.64
2007-08	6.4	-10.98
2008-09	8.4	157.28
2009-10	10.9	4114.48
2010-11	12	3610.26
2011-12	8.9	5141.03
2012-13	9.3	4844.5
2013-14	10.9	5160.42
Total Avg. annual growth rate	96.8	23052.79

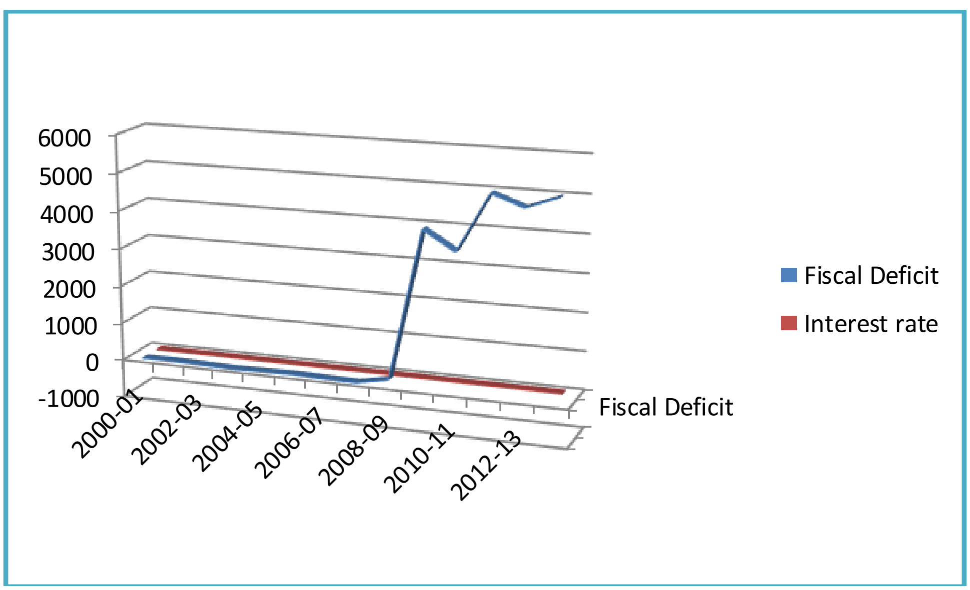
Analysis of relationship between consumer price index ad fiscal deficit indicate a high degree of positive relationship indicating more the fiscal deficit higher is the inflation and vice versa. Any controlling measure for inflation should be by reducing fiscal deficit.



Fiscal Deficit and Government Expenditure:

Year	Fiscal Deficit	Government expenditure
2000-01	13.46	59.84
2001-02	18.63	61.05
2002-03	2.92	62.3
2003-04	-15.03	70.68
2004-05	2.05	78.9
2005-06	16.41	90.71
2006-07	-2.64	98.01
2007-08	-10.98	127.42
2008-09	157.28	133.79
2009-10	4114.48	162.54
2010-11	3610.26	195.37
2011-12	5141.03	206.01
2012-13	4844.5	200.91
2013-14	5160.42	211.14
Total Avg. annual growth rate	23052.79	1758.67

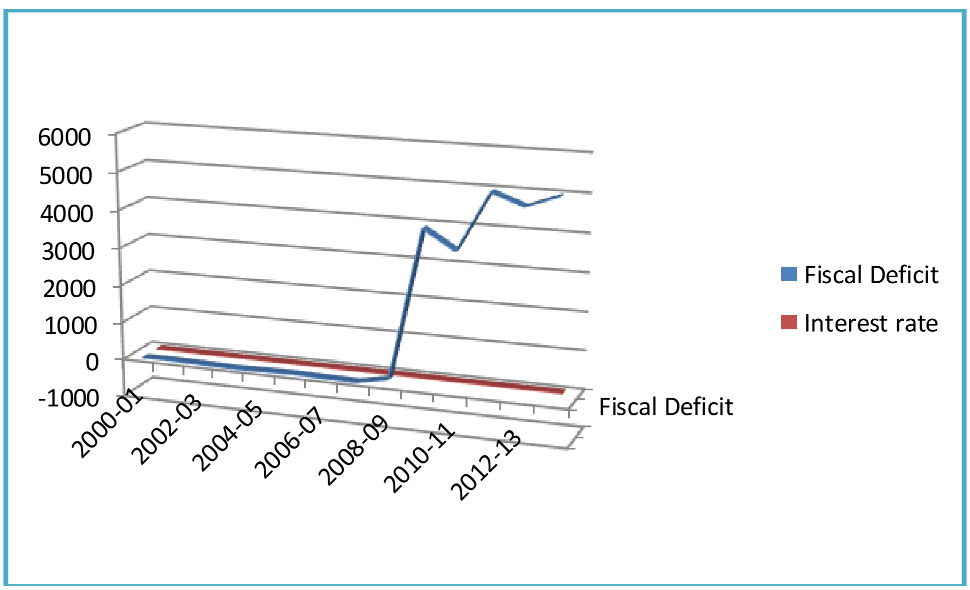
The relationship between the fiscal deficit and government expenditure shows a high positive nearly perfect correlation. In other words, every one rupee extra expenditure, by the government more or less proportionately increases fiscal deficit.



Fiscal Deficit and Interest Rate:

Year	Fiscal Deficit	Interest rate
2000-01	13.46	12
2001-02	18.63	12
2002-03	2.92	12
2003-04	-15.03	11
2004-05	2.05	11
2005-06	16.41	11
2006-07	-2.64	11
2007-08	-10.98	13
2008-09	157.28	13
2009-10	4114.48	12
2010-11	3610.26	8
2011-12	5141.03	10
2012-13	4844.5	11
2013-14	5160.42	10
Total Avg. annual growth rate	23052.79	157

The analysis of the relationship between the Fiscal Deficit and Interest Rate indicates a negative correlation it means that government expenditure does not significantly influence the prevailing interest rates.



- **<u>Conclusion</u>**

It has been witnessed that over the years particularly in the last decade not only burden of fiscal deficit has increased but also mounting inflation rate. Government expenditure has also increased the pressure of the burden on Central government. As for as money supply is concerned, annual growth rate of money supply has remained more or less constant. However, money supply in absolute terms has increased. Result obtained from the analysis shows that the important variables which are affecting fiscal deficit are money supply and mounting government expenditure, while inflation does not count for fiscal deficit significantly. This implies that as money supply increases fiscal deficit will decrease and as government expenditure increases fiscal deficit will increase. This implies that while on one hand financing of deficit through the banking system from printing of new money and creating interest-bearing decreases fiscal deficit, on the other hand increasing government expenditure is the main cause of mounting fiscal deficit.

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