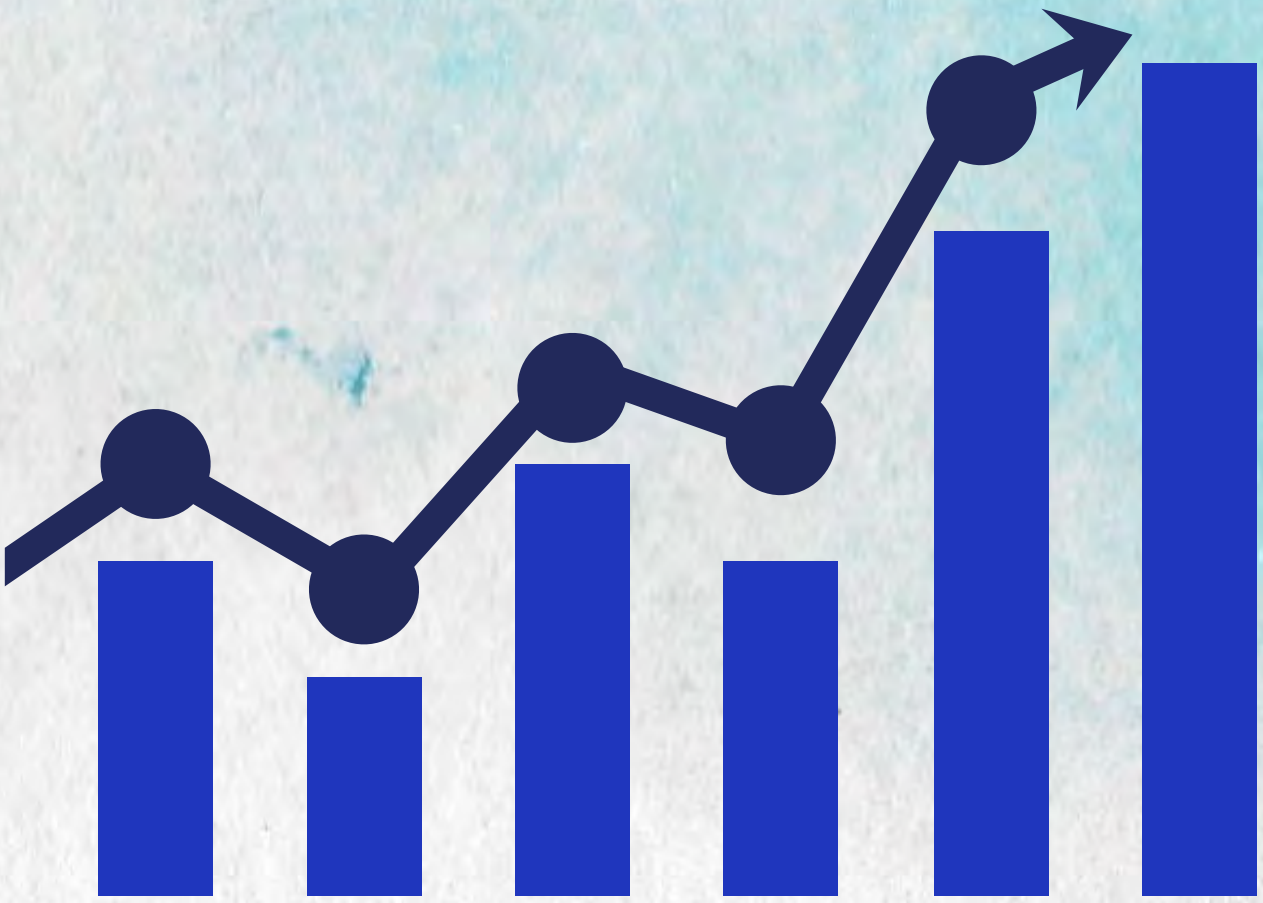
Government Of Odisha

Fiscal Risk Statement



July 2022

Finance Department

FISCAL RISK STATEMENT

July 2022

FISCAL RISK & DEBT MANAGEMENT UNIT
FINANCE DEPARTMENT
ODISHA

CONTENT

GLOSSARY

BE	Budget Estimates
CAG	Comptroller and Auditor General
CAMPA	Compensatory Afforestation Fund Management and Planning Authority
CL	Contingent Liability
CSS	Centrally Sponsored Scheme
ECI	Empowered Committee on Infrastructure
FD	Finance Department
FR&DU	Fiscal Risk and Debt Management Unit
FRBM	Fiscal Responsibility and Budget Management
FRU	Fiscal Risk Unit
FSR	Fiscal Strategy Report
FY	Fiscal Year
GDP	Gross Domestic Product
GFS	Government Financial Statistics
GridCo	Grid Corporation
GSDP	Gross State Domestic Product
GST	Goods and Services Tax
HLCA	High Level Clearance Authority
ICRA	Investment Information and Credit Rating Agency
IPRR	Interest Payment to Revenue Receipt
IPSAS	International Public Sector Accounting Standards
IT	Information Technology
OM	Office Memorandum
OMBADC	Odisha Mineral Bearing Areas Development Corporation
PED	Public Enterprises Department
PEFA	Public Expenditure and Financial Accountability
PFRAM	Public Private Partnership Fiscal Risk Assessment Model
PPPs	Public Private Partnerships
PSUs	Public Sector Undertakings

PREFACE

In an endeavour to enhance fiscal transparency and the tradition of Odisha's continued efforts of reforms in public finance management in the state, the Fiscal Risks & Debt Management Unit of Finance Department has brought out the Fiscal Risk Statement for FY 2022-23. This is the second edition of this document. It was published for the first time in FY 2021-22 along with the annual budget.

Analysing fiscal risks is critical for devising appropriate risk mitigation measures. Identification of individual fiscal risk, qualitative and quantitative analysis of the identified fiscal risk, disclosure of the risk and finally devising suitable risk mitigation measure are the important aspects of the fiscal risk management.

The Fiscal Risk Register and Fiscal Risk Matrix have been updated taking into account the recent developments and emerging fiscal risks. This edition of the Fiscal Risks Statement is a continuity of the first edition.

The identified fiscal risks have been categorized broadly into (i) macroeconomic risks, (ii) public debt, and (iii) specific risks that include Public Private Partnerships (PPP), Public Sector Undertakings (PSU), Government guarantees, natural disasters, and other risks.

The objective of this document is to disclose various possible financial risks to the State Government and the risk mitigation measures undertaken or planned to be taken by the State Government. Identifying risks, quantifying them and taking suitable risk mitigation measures are the basic objectives of the Financial Risk Management practice in the public finance management domain.

We sincerely hope that this document will enhance the fiscal transparency of the State Government and will be useful tool for the policy makers to recognize and to devise appropriate policy for risk mitigation.

(Vishal Dev)
Principal Secretary

EXECUTIVE SUMMARY

1. **Fiscal Risks are factors that may cause fiscal outcomes (government revenues, expenditures, and the value of assets and liabilities) to deviate from expectations or forecasts.** The fiscal risks have been categorized into different types such as Macroeconomic Risks due to various macroeconomic factors, risks from Public Private Partnership Projects, contingent liabilities in the form of guaranteed and non-guaranteed loans extended to the State PSUs and economic loss and damage of critical assets and infrastructure due to natural disasters like cyclones.

2. **Fiscal Risk Analysis** includes risk identification and quantification, risk classification, risk reporting in the form of disclosure statement and finally putting in place suitable risk mitigation measures. In the fiscal risk analysis, we have identified all possible sources of risk such as macroeconomic, institutional, risks emanating from SOEs, PPP, Natural Disasters, Government Guarantees etc. The fiscal risks have also been quantified as percentage of State GDP.

3. Revenues of the State Government are sensitive to various factors. These include economic growth at the global, national and state level, iron ore prices, revenue from mining sector, central transfers to the State, GST Compensation etc. Similarly, expenditures of the government may also deviate from budget estimates if specific financial risks materialize. Besides, contingent liabilities from guaranteed and non-guaranteed debt of State Public Sector Enterprises and Public Private Partnerships can also pose fiscal risk to the State Government.

4. **Fiscal Risk Register,** a top-down tool to identify different fiscal risks, has been developed. It lists fiscal risks with both qualitative and quantitative analysis. Each identified fiscal risk has been categorized based on the potential fiscal impact and the likelihood of materialization.

5. Fiscal Risk Assessment has been done based on quantitative financial impact and likelihood of realization of any fiscal risk. Based on the assessment, various financial risks have been classified and put into a risk matrix. The **Fiscal Risk Matrix** has been updated taking into account the recent developments.

6. Our analysis suggests that historically, natural disasters, volatile revenues from mining, GST, Odisha's share in central taxes, and electricity sector are the sources of the largest fiscal risks. During the FY 2021-22, revenue collection from mining sector has come as a positive fiscal shock. The mining revenue has been substantially higher than the budgeted amount. The higher mining revenue has created a large fiscal space and thus the committed expenditure will be higher in the coming financial years. Since volatility in metal price directly affects the mining revenue, the risk associated on this account will substantially increase in future due to higher exposure.

7. The **State PSUs** receive budgetary support in the form of equity capital, loans and subsidies. It is critical for the State Government to undertake strategic oversight, monitoring and fiscal analysis of high-risk PSUs. Majority of government guarantees are in power sector PSUs. Using the **PSUs Risk Analysis tool**, financial health check of around 33 major operating PSUs has been done.

8. The State Government has a growing portfolio of Public Private Partnership projects (PPPs). Majority of the projects under implementation are in transport and urban development sector. Depending on their mode of design and implementation, the PPP projects can create fiscal commitments as well as explicit and implicit contingent liabilities. Mostly the PPP projects are executed through viability gap funding (VGF). The State Government also supplements the VGF of Central Government where the State Government contribute up to 20 percent of the total project costs and commit to a stream of annual payments depending upon the design mode of the project. The **PPP Directorate** in Finance Department compiles all information related to total fiscal commitments, contingent liabilities concerning all PPP projects under implementation and in pipeline. The **PPP Fiscal Risk Assessment Model (PFRAM)** is being used to assess fiscal risk associated with the PPP project.

9. Adopting appropriate risk mitigation measure is the ultimate goal of the fiscal risk analysis exercise. Odisha has already put in place a number of risk mitigation measures such as setting up of dedicated funds such as **Guarantee Redemption Fund**, **Consolidated Sinking Fund** and **Disaster Risk Management Funds**. With the identification of newer risks, suitable risk mitigation measures are being adopted. For example, recently State Government in Finance Department has decided to put in place a **Budget Stabilisation Fund** to cushion the State Budget against both positive and negative shocks stemming from mining revenue.

10. **Fiscal Risk Assessment Tool (FRAT)** developed by the IMF has been piloted in Odisha. The FRAT gives a high-level perspective on various financial risks faced by the government and helps in identification and quantification of risks.

11. **Fiscal Risk Reporting** is a critical aspect of Fiscal Risk Management. It helps in ensuring transparency and accountability in public financial management. Public disclosure about various risks and the risk mitigation measures adopted by the State Government will enhance the credibility of the Government. In fact, RBI in its '**State Finances: A Study of Budgets of 2020-21**' report (page-34) has recognized the Fiscal Risk Management practice in Odisha as a best practice in financial management in India. Odisha's Fiscal Risk Management practice has been presented as a case study in the IMF Spring meeting, 2022 in the session on "**CD Talk: Building Capacity on Fiscal Risks**" on 19th April, 2022.

12. The fiscal risk statement not only increases financial transparency but also facilitates the State Government to take critical policy decisions in the area of public finance management.

I: INTRODUCTION

At times, fiscal parameters like revenue, expenditure, GDP growth rate etc. experience significant deviations from projected value in the budget or any forecast document. The deviations occur from shocks arising from sources as varied as natural disasters, financial crisis, economic downturn, cost-overrun of big projects, realization of government guarantees, or an unprecedented situation like Covid-19 health emergency. These shocks pose enough challenge to disrupt government finances and in turn, smooth functioning of the economic activity of the government gets severely affected. Broadly speaking, these kinds of risks to government finances are called fiscal risks.

Fiscal Risks need not be negative always. There can be positive risks as well, such as higher than budgeted collection of mining revenue during FY 2021-22. The mining revenue during the year has been more than 3 times of the budgeted amount. This has come as a positive shock for the State Government. Obviously, there is a larger fiscal space now to go for higher capital spending, but appropriate risk mitigation measure needs to be put in place to absorb the shock arising from the mining sector so that the State Government is able to meet the committed expenditure in future.

Over the past few decades, fiscal risk management by the governments worldwide has been an emerging trend precisely because there are countless sources of fiscal risks that can materialize and the degree of uncertainty that is associated with them. This implies forecasts and plans are always at risks of being proven wrong or be far off the mark. In a responsible democracy like ours, government has the ultimate responsibility to ensure that economic system operates smoothly in the country and in the state. This makes fiscal risk identification, analysis, disclosure and management ever so necessary for any government.

Traditional understanding of the government finances puts macroeconomic management as the sole responsibility of the central government. This in turn limits the fiscal risk exposure to the central government and its budget only. However, in recent times fiscal risk exposure at sub-national level is getting considerable attention and thus fiscal risk management at the sub-national level is getting traction. In India, the Fiscal Responsibility and Budget Management (FRBM) Act, 2003 puts both the central and state governments under a legally sanctioned limited fiscal space. In addition to the fiscal limits set by the FRBM Act, successive Finance Commissions have recommended sustainable debt level and fiscal deficit level for the Union Government and State Governments as a whole. There are different tools for managing fiscal risks that also include legislative intervention. The Fiscal Responsibility Legislation is one such intervention.

The 15th Finance Commission has recommended that the normal limit for net borrowing by State Governments may be fixed at 4 per cent of GSDP in 2021-22, 3.5 per cent in 2022-23 and be maintained at 3 per cent of GSDP from 2023-24 to 2025-26.

1.1. ODISHA ON THE PATH OF FISCAL SUSTAINABILITY

Government of Odisha has undertaken a number of fiscal reform measures in last two decades, which aimed at expenditure rationalization and revenue generation. It has succeeded in bringing about a turnaround in the State's finances. It is important that all committed expenditures and developmental expenditures are met from the borrowing space, without resorting to off-budget or any non-transparent means of financing for any expenditures.

The State has been able to reduce the debt stock from 50.7% of GSDP in 2002-03 to below the prudential level of 25% as recommended by the 13th Finance Commission and prescribed in Odisha Fiscal Responsibility and Budget Management (FRBM) Act, 2005. The ratio of interest payment to revenue receipt (IP/RR) ratio, which should be within the prudential level of 15%, has also been achieved and consistently maintained. Strong fiscal performance of the state by fulfilling these criteria gives the state an additional fiscal space over the prescribed fiscal deficit 3% of GSDP.

1.2. SOURCES OF FISCAL RISK IN ODISHA

The major sources of fiscal risk in Odisha, which are subsequently dealt with in this document, are as follows:

1.3. FISCAL RISK IDENTIFICATION AND MEASUREMENT

All possible identified sources of fiscal risk were measured and the impact of each fiscal risk worked out as ratio to GSDP and classified as high, medium and low based on the level and possibility of occurrence using a framework. For instance, if a particular risk factor (say reduction in central transfer) has potential to have a fiscal impact more than 0.5 per cent of GSDP and the possibility of occurrence is more than 50 per cent, that factor is regarded as high-risk. Similarly, all other identified fiscal risks are classified as low or high based upon the fiscal impact and likelihood of realization as presented in the chart below where green represents low fiscal risk, yellow corresponds to medium risk, and red to high risk.

Chart-1.1: Fiscal Risk Matrix

Fiscal impact[1]				
	High (>0.5% of GSDP)	• Growth slowdown	• Central Transfer	• Natural disasters • Mining-related revenues • Electricity sector – Energy Sector PSUs • GST Compensation
	Medium (0.1% - 0.5% of GSDP)	• Risks from Public sector undertakings	• Social security programs • Food Supply Department • Government Institutions • Investment scams of small-scale investors	• Inflation • Non-performing assets of public financial institutions
	Low (<0.1% of GSDP)	• PPPs • Tax refunds under litigation • Pension schemes • Foreign-currency debt	• Line departments	
		Low (<10%)	Medium (10%-50%)	High (>50%)
		Likelihood of realization[2]		

1.4. FISCAL RISK REGISTER

Fiscal risk reporting, critical for transparency and public disclosure, is envisaged through a two-stage approach. First, a Fiscal Risk Register as a continuous exercise of identifying the sources of fiscal risks, risk exposure and likelihood and severity of risk materialization is put in place in the form of a register. The State Government is maintaining separate Risk Registers for PPPs, PSUs etc., which contain details of the individual projects and PSUs which provide inputs to the consolidated Fiscal Risk Register. These Registers are updated every month. At the second stage, a Fiscal Risk Statement is released along with Annual Budget documents as a disclosure document. The snapshot of the Fiscal Risk Register is shown in the table below.

Table-1.1: Fiscal Risk Register

Category	Type/Name of the Risk	Fiscal Impact	Comments on Fiscal Impact	Likelihood	Comments on Likelihood
Macro-economic Risk	Growth Slowdown	High	Revenues of the State are linked to GSDP growth. A decline in the latter will adversely affect the deficit.	Low	There is possibility of high economic growth in FY 2022-23 due to recovery from the pandemic-hit 2021-22 and base effect. Positive economic growth will have positive impact on the State Revenue.
Macro-economic Risk	Central Transfers	High	Central Transfers account for a significant share of the State's Revenues.	Medium	The likelihood of realization of risk from the central transfer is going to be medium in the FY 2022-23 due to the fact that there is positive economic growth at the national level. Further, the uncertainty surrounding recommendation of 15th Finance Commission is over now. Odisha's share of the central taxes has been defined at 4.53% of the divisible pool.

[1] Defined as marginal impact of risk realization on fiscal deficit.

[2] Over a three-year period, consistent with the timeframe of the Medium-Term Fiscal Framework.

Category	Type/Name of the Risk	Fiscal Impact	Comments on Fiscal Impact	Likelihood	Comments on Likelihood
Macro-economic Risk	GST Revenues	High	Major source of State's Own-Tax Revenues.	High	GST Compensation from the Centre will be over by June, 2022. There is demand from the States for continuance of GST compensation for some years so that risk will further go down.
Macro-economic Risk	Mining Revenues	High	Major source of State's Non-Tax Revenues.	High	Mining revenues includes mining royalty and premium. This year it grows substantially mainly because of collection of premium from the auction of mineral blocks. There will be positive financial risk due to more than expected revenue from the mining sector

II: MACROECONOMIC RISKS

Macroeconomic Risks may be broadly classified into two types; first, risks due to ***Economic Volatility*** and second, risks due to ***Institutional Uncertainty***. The State receipts and thus expenditures are extremely sensitive to the macroeconomic risks. Materialization of any of the macroeconomic risks could put budgetary constraint on the State Government to spend on critical areas such as education, health, infrastructure etc. Macroeconomic risks such as *slower than projected GSDP growth*, *volatility in mining revenue collection*, *variation in inflation and interest rate* are generally classified under the **Economic Volatility Risks.** The fiscal risks due to *uncertainty in GST compensation to the State*, *uncertainty in share in central taxes to the State Government*, *Finance Commission Devolution Criteria* could be classified under the **Institutional Uncertainty Risks.**

2.1. FISCAL RISKS FROM ECONOMIC VOLATILITY

2.1.1. SLOWER THAN PROJECTED GROWTH IN GSDP

The geopolitical war between Russia and Ukrain has pushed the world economy into uncertainty, especially when the economy was showing signs of recovery after the pandemic induced contraction. As per the IMF's World Economic Outlook (April 2022), the global economy is projected to to slowdown from estimated 6.1 percent in 2021 to 3.6 percent in 2022 and 2023. The Reserve Bank of India has lowered the real GDP growth rate of India from initial 7.8 percent to 7.2 percent for FY 2022-23. The real GDP growth rate is estimated to be about 7.3 percent for FY 2022-23. Similarly, Economic growth (real GSDP) of Odisha is estimated to be between 8 to 8.5 percent in FY 2022-23. However, due to higher commodity prices, volatility in global crude oil prices and evolving geopolitical tensions in between the West and Russia could potentially impede the economic recovery. Although Odisha's direct exposure to such geopolitical risks is minimal, nevertheless there remains uncertainty in projected GSDP growth rate.

The variation in rate of GSDP growth from the estimated growth rate is a critical macroeconomic risk which could destabilise the fiscal state. The estimated revenue and expenditure are based on the estimated GSDP growth. Being the base of economic projection, in case any variation in it, the output such as revenue and expenditure estimation will also be different. The economic projection is not always cent percent accurate. However, if the gap between the estimation and actual is large, it may have visible effect on receipt and expenditure position of the government.

The chart-2.1 below shows the downward revision of growth forecast from budget estimate to actual estimate. GSDP growth forecasts have been revised downwards in successive years. The reason for such downward revision in growth forecasts is mainly due to change in underlining macroeconomic assumptions and downward revision of growth forecast of national GDP. Due to revision in GSDP growth forecasts, tax revenue projection is also affected by virtue of the relationship between tax and the tax base (GSDP).

Chart-2.1: Variation between Budget Estimates and Revised Estimates

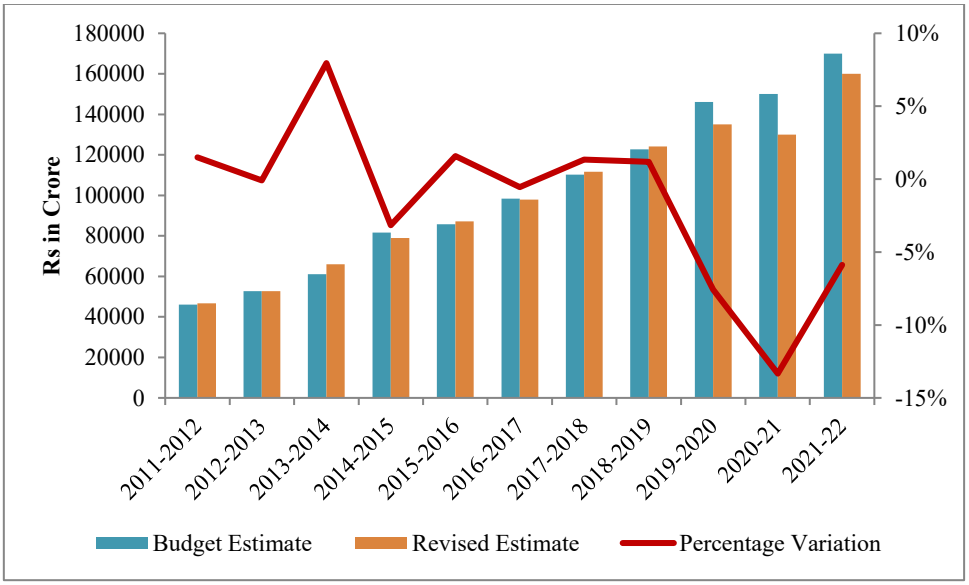
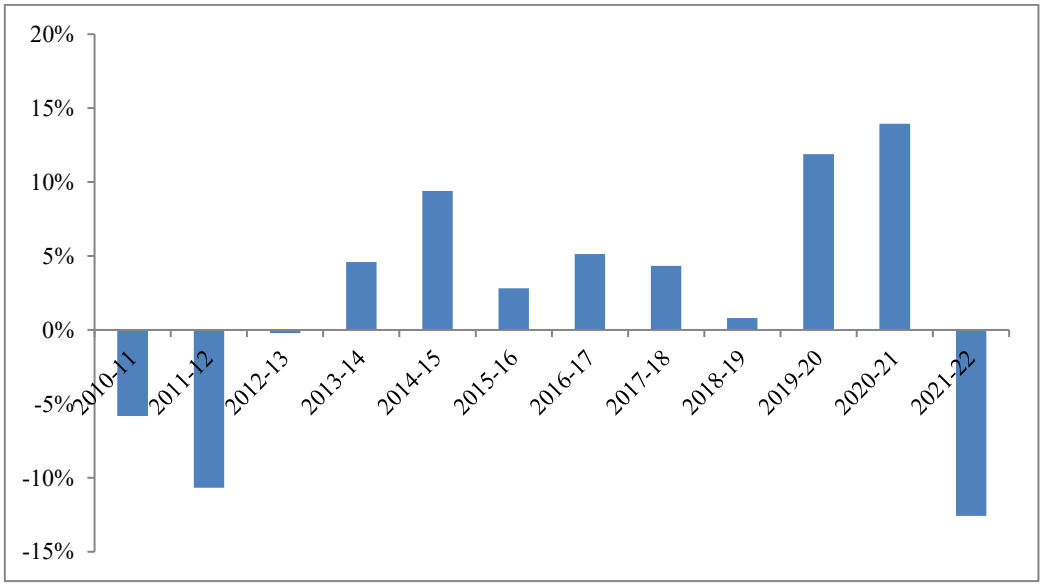


Chart-2.2 below shows the forecast error analysis of total revenue receipts (budget estimates for total revenue receipts minus actual revenue receipts) as a percentage of GSDP. A negative value indicates a pessimistic forecast (the actual receipt is higher than the budgeted estimate) whilst a positive value indicates an optimistic forecast (the actual receipt is lower than the budgeted estimate). A higher value indicates the uncertainty in revenue estimation due to uncertain economic conditions.

Chart-2.2: Forecast Error of Revenue Receipts, percent of GSDP



* For FY 2021-22, revised estimate value has been considered.

2.1.2. VOLATILITY IN MINING REVENUE

Mining revenue constitutes about 6 percent of State GDP, 26 percent of total revenue receipts, 90 percent of State Own Non-Tax Revenue and 46 percent of State Own Revenue. Major industries of the State are largely concentrated in the metals and minerals sector.

Historically, mining industry has driven the economic growth of the State. Since mining revenue is sensitive to demand and price of metal in national and international market, there is risk associated with the mining revenue. It was estimated in the budget for FY 2021-22 that mining revenue would be around Rs.13,700 crore. However, as per the revised estimate for FY 2021-22, mining revenue is expected to exceed Rs.44,000 crore.

Mining revenue is directly dependent on the price of metals in international market. A 20 percent variation in commodity prices can impact the State revenue by about Rs.10,000 crore, which is substantial compared to the size of the State budget. Hence, there is need for building up a strategic reserve to offset any fluctuation in mining revenue.

2.1.3. VARIATION IN INFLATION, INTEREST RATE & EXCHANGE RATE

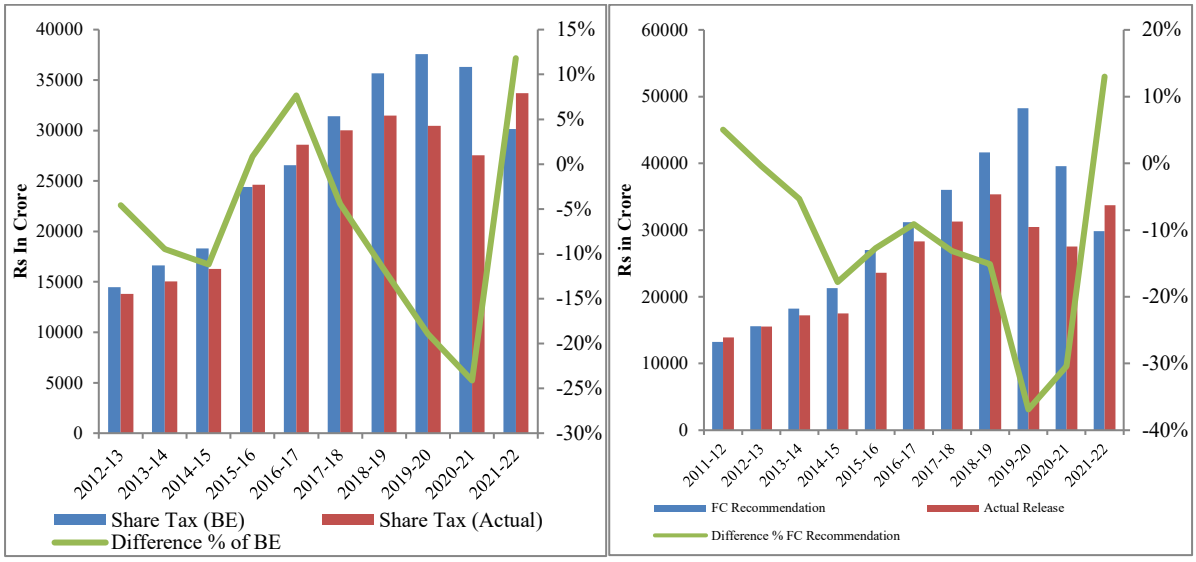
Although majority of the State government's public debt is in Indian Rupees, around 7% of total borrowing is from external agencies in foreign currency. Due to change in currency exchange rate and interest rate, debt-serving cost is affected. Some of external debts are LIBOR linked and their interest costs vary according to changes in the LIBOR rate. The loans are borrowed mostly in US dollar and Japanese yen. The Indian rupee has been fluctuating against these foreign currencies. Depreciation in the Indian currency alongside variable interest rates raises the cost of servicing this debt. Variation in inflation has a direct bearing on debt servicing cost. Inflation in Odisha mostly follows national trends. The Reserve Bank of India (RBI) has projected that the inflation of to be at 5.7 percent in FY 2022-23 for India. The Consumer Price Index (CPI) surged to 7.79 percent in April 2022 as per the recent data released by the National Statistical Office (NSO), Ministry of Statistics and Programme Implementation, Government of India. The CPI for Odisha in April 2022 is 8.8 percent as per the NSO.

2.2. INSTITUTIONAL UNCERTAINTY

2.2.1. UNCERTAINTY AROUND SHARE IN CENTRAL TAXES

A fall in economic activity reduces national tax collections which results in lower central transfers to the State. The State share in central taxes is based upon the recommendation of the Finance Commission. The Finance Commission recommendation is for a period of five years. The current 15th Finance Commission has recommended reduction in State Share (all states) from earlier 42 percent to 41 percent owing to bifurcation of Jammu & Kashmir into two Union Territories. The share of Odisha has reduced from 4.64 percent to 4.53 percent for the 15th FC award period (2021-22 to 2025-26). The 15th FC had recommended share of Odisha for 2020-21(pandemic year) at 4.63 percent as per its interim report. Due to less collection of taxes during the pandemic, the actual release of share tax by the union Government to Odisha in 2020-21 was substantially lower than the FC recommendation. The difference was almost 30 percent. However, there was higher release in 2021-22 due to higher GST collection.

Chart-2.3: Difference in Share Tax (BE) and Actual Share Tax & FC Recommendation and Actual Release



**For FY 2021-22, revised estimated value of share tax has been taken.*

2.2.2. UNCERTAINTY AROUND GST COMPENSATION

The State was assured for compensation for the losses incurred on account of GST implementation till June 2022. But due to pandemic the cess collection in the GST Compensation Fund has been low. The recent initiative of the GST Council to compensate a portion of the pandemic related GST loss through a special borrowing window will give partial relief to the State. Government of India has decided to extend loan to the States whose service cost will be borne by the Union Government by extending the period of collection of compensation cess. There is substantial gap between the actual GST collection by the States and protected revenue during 2020-21 and 2021-22. If the GST compensation regime is closed in June, 2022, there will be a fiscal shock to the extent of about 1% of GSDP for the State.

2.2.3. CHANGE IN DEVOLUTION CRITERIA OF THE FINANCE COMMISSION:

The revenue receipt in coming years is likely to be affected by changes in the devolution structure recommended by Fifteenth Finance Commission. This change is mainly due to updated population data being used as a basis for determining the share of central taxes that each State receives. Odisha's share of total population has declined, which has resulted in decline in State's horizontal share of central taxes proportionately from 4.64 percent to 4.53 percent as per recommendations of 15th Finance Commission. The State will continue to receive share in central taxes at this reduced rate during next five years, i.e., from FY 2021-22 to FY 2025-26.

III: DEBT MANAGEMENT

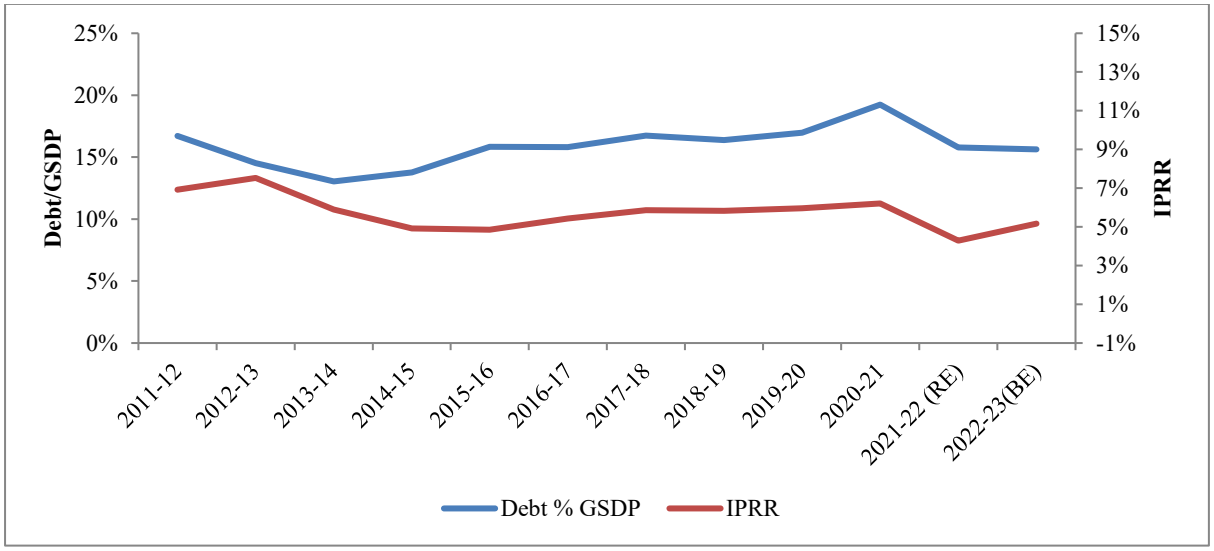
The total outstanding public debt of Odisha as per 2021-22 (RE) stands at Rs. 100813 crore which is 15.8 percent of the State Gross Domestic Product (GSDP). The borrowing undertaken by the Government of Odisha is fully used to finance capital investment. Whilst the total stock of debt is increasing over time, the public debt of Odisha is sustainable, meaning that the Government of Odisha can service its debts without difficulty. Strong revenue growth is helping to keep interest payments manageable, and within the limits of the Fiscal Responsibility and Budget Management (FRBM) Act.

3.1. FISCAL RISK DUE TO PUBLIC DEBT

The long maturity profile of Odisha's debts reduces the risk from an economic shock and the low percentage of foreign currency debts has lowered Odisha's vulnerability to any exchange rate depreciation. As on 31st March 2022, the total outstanding loan from external agencies is Rs 6652 crore which is 6.98% of total outstanding loan.

Majority of the State Government borrowing is from low cost sources. During FY 2021-22, State Government did not go for market borrowing because of availability of low-cost sources such as OMBADC, CAMPA. This is reducing the average cost of borrowing for the State. Through these short-term loans, the State is exposed to rollover risk. However, the rollover risk is not likely to have a significant impact on the State finances in view of the comfortable liquidity position.

Chart 3.1- Debt to GSDP and Debt servicing as a percentage of Total Revenue Receipts

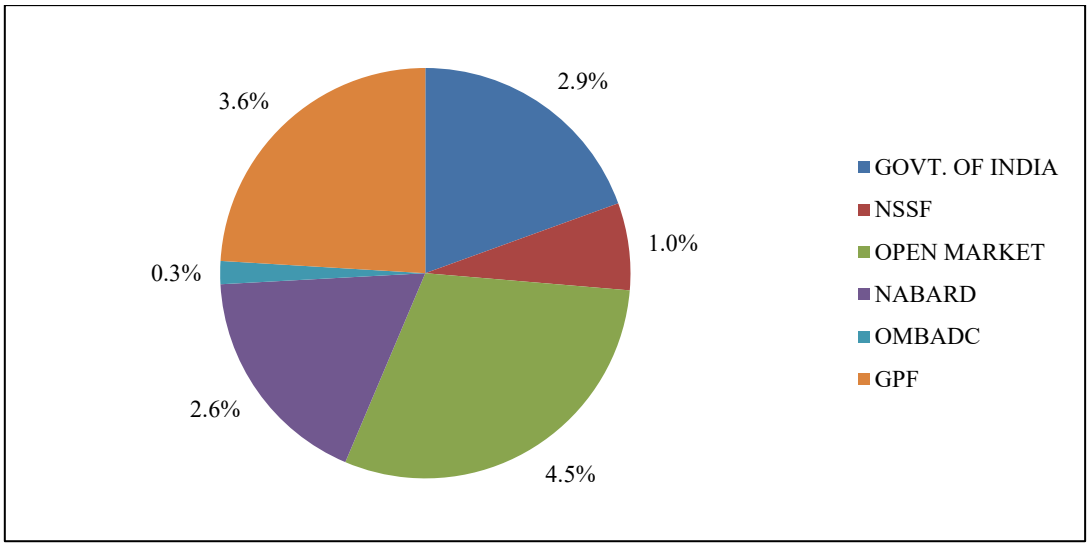


3.2. DEBT PORTFOLIO OF THE STATE

The composition of debt stock in the State (Chart-3.2) has also witnessed a transition from some of the high cost borrowing sources such as National Small Saving Fund (NSSF) to low cost borrowing sources. The State is availing short-term loans at cheaper interest rate from funds setup for dedicated purposes such as OMBADC and CAMPA. The State Government can borrow up to 60 percent of the surplus fund available in these funds. These loans

substitute some of the high cost borrowings of the State Government. The share of market borrowing has come down also. Therefore, overall the cost of borrowing and thus debt servicing cost will come down in coming years. Broadly the five largest sources of borrowing are shown in the chart below.

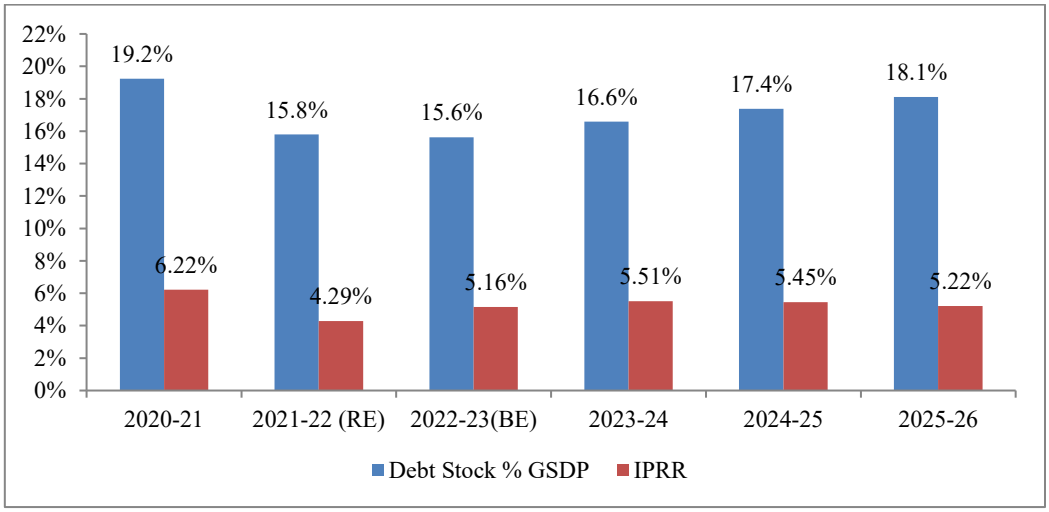
Chart 3.2- Composition of Public Debt as on 31-03-2022



3.3. DEBT OUTLOOK

The debt outlook of the State Government in the medium term appears to be within the FRBM Act prescribed ceiling and sustainable level. In the last three years, total public debt was less than 20% of GSDP and within the FRBM defined limits. Interest payment to revenue receipts has significantly declined from 40.2% in FY 2001-02 to 6.2% in 2020-21. It is estimated that IPRR will be 4.3% in 2021-22 and 5.2% in FY 2022-23. Over the next three years, total public debt is expected to increase from 15.3% of GSDP in FY 2022-23 to approximately 18.1% of GSDP in FY 2025-26.

Chart 3.3- Debt Outlook



IV: SPECIFIC RISKS

The specific risks include risks emerging out of the various factors like risks associated with Public Private Partnerships, Public Sector Undertakings, risks due to natural disasters, risks out of Government Guarantee and others which have been discussed as under.

4.1. PUBLIC PRIVATE PARTNERSHIPS

Public Private Partnership (PPP) is a nascent concept related to development of infrastructure especially meant for public use. PPPs have brought in the investment, managerial & technical competencies of the private sector and enabled the public sector to achieve social, economic, financial and environmental sustainability. The Government of Odisha has been instrumental in identifying the scope of PPP and has undertaken several projects in this regard. Odisha State PPP Policy, 2007 was formulated to popularise the use of PPP for development of public infrastructure in the State.

4.1.1. ODISHA PPP POLICY, 2007

The Odisha PPP Policy - 2007 envisages following objectives to guide the State Government initiatives on PPP:

(i) To leverage State and Central Government funds, support private investment and to create a conducive environment to utilize the efficiencies, innovativeness & flexibility of the private sector to provide better infrastructure & service at an optimal cost.

(ii) To set up a transparent, consistent, efficient administrative mechanism to create a level playing field for all participants and protect interest of all stakeholders.

(iii) To prepare a shelf of projects to be offered for PPP and take them forward with assistance of the owner departments through a transparent selection process.

(iv) To put in place an effective and efficient institutional mechanism for speedy clearance of the projects.

(v) To provide necessary risk sharing framework in the project structure so as to assign risks to the entity most suited to manage them.

(vi) To create a robust dispute redressal mechanism / regulatory framework for PPP projects.

(vii) To provide the required Viability Gap Funding (VGF) where the essential projects are intrinsically unviable.

(viii) To create Odisha Infrastructure Development Fund (OIDF) to facilitate implementation of the objectives of the Policy.

4.1.3. Overall PPP Scenario in Odisha:

The PPP Projects in Odisha have been categorised into *completed*, *under implementation* and *pipeline* projects. *Completed* projects account for Rs.8,365 Crore, the projects in the *under-implementation* category account for Rs.7,481 Crore whereas those in pipeline account for Rs.7,136 Crore.

Table 4.1- Summary of sector-wise PPP Projects (As on 31-03-2022)

Sector	Number	Cost
Urban Development	35	3161
Health	14	2981
Finance & Revenue Related	1	87
Transport	7	12422
Industrial Infrastructure	5	885
Roads	2	1480
Tourism	2	51
Education	16	85
Energy Related	4	1774
Food Supplies & Consumer Welfare	3	57
Total **Percent of GSDP**	**89**	**22983** **(3.6% of GSDP)**

Source: Directorate of PPP

4.1.4. RISKS ASSOCIATED WITH PPPs

Though PPPs bring in several advantages including on-time, on-budget asset delivery, they can also pose serious risks in form of hidden fiscal costs. Therefore, a thorough understanding of the fiscal costs and risks involved in each project is necessary. The major risks comprise risks related to construction and design, operation and maintenance, financial markets, environment, etc. The risks involved in PPP projects may give rise to Contingent Liabilities, which can have a serious impact on the state's fiscal resources.

Depending on the design, PPPs can create fiscal commitments as well as explicit and implicit contingent liabilities. In Odisha, some of the PPP projects like Road, Bulk Water supply Projects are injected with Viability Gap Funding (VGF) by Government of India as well as the State Government. Similarly, rice storage godowns created through PPP are partially funded through VGF. Under Government of India (GoI) VGF funding, a one-time grant of up to 20 percent of total project costs is paid to the operator to construct and operate a facility. The State Government also contributes VGF funding up to a maximum of a further 20 percent if required.

Government of India has recently extended the VGF to social sectors like wastewater treatment, water supply, solid waste management where VGF can be up to 60 percent of the capital cost of the project with 30 percent share from Government of India and balance from State. For pilot projects in social sectors like healthcare & education, VGF amount shall be up to 80 percent of the capital cost (40 percent by Central Government) and provision of funding support to cover 50 percent of operational expenses for 5 years.

The VGF mode avoids annual payment commitments by government but depending on the details of the contract, it may involve the government to bear any explicit or implicit risk. There are also projects based on a revenue sharing model concession in Odisha, especially in

port sector projects that generate a stream of annual revenues for government from a share of the concessioner's revenue stream. However, there are very few annuity model PPPs in Odisha, under which government is committed to a stream of annual payments to a PPP operator to finance services in a long-term contract.

4.1.5. PPP RISK ANALYSIS:

In Odisha, investment in PPP projects as a percentage of GSDP is very low thereby the risk associated with PPP projects is not that significant. Odisha has replicated projects having a success history thus is exposed to lower risk. The land alienation process experiences a risk to housing, road and port projects. In renewable energy sector, the cost of production is higher making them unviable. Odisha is in the process of maturity of PPP projects and handles risks by learning from own experiences and from others as well, by way of risk avoidance, mitigation, intermittent modification of contract agreement by incorporation of suitable clause. Hence, fiscal risk associated with the PPP projects has been estimated as low.

A **PPP Risk Register** has been developed with the help of IMF SARTTAC experts to record, monitor and assess the risk components of PPP projects. It is updated on a regular basis and records relevant data and information of specific PPP projects received from line departments and other Government stakeholders. It captures all relevant data and necessary information relating to any specific PPP project. This will enable in assessing and quantifying any potential risk that may arise from a project. This in turn will help policymakers in timely and well-informed decision making to minimise the risks.

4.2. PUBLIC SECTOR UNDERTAKINGS

At present there are 45 working PSUs in the State in various sectors such as power, agriculture, finance, infrastructure, manufacturing etc. Majority of the working PSUs are profit making. As per the Comptroller and Auditor General of India (CAG) report on functioning of State PSUs in 2020-21, out of 45 PSUs, only 10 PSUs have incurred losses in that financial year. The State PSUs receive budgetary support in the form of equity capital, loans and subsidies from the State Government. The total investment of the State Government in PSUs is about Rs.21,750 crore which includes both equity investment as well as long term loans extended to the PSUs. Therefore it is critical to monitor the fiscal position of the PSUs and asses contingent liabilities so that appropriate risk mitigation measures could be adopted.

Table 4.2: Equity and Loans in Government Companies and Corporations

(₹ in crore)

Sources of investment	As on 31.03.2021			As on 31.03.2020		
	Equity	Long Term Loans	Total	Equity	Long Term Loans	Total
State Government	4116.06	1245.22	5361.28	3998.06	1272.30	5270.36
State Government Companies/ Corporations/ Autonomous Bodies	614.84	595.34	1210.18	528.84	791.76	1320.60

Sources of investment	As on 31.03.2021			As on 31.03.2020		
	Equity	Long Term Loans	Total	Equity	Long Term Loans	Total
Central Governments/ Central Government Companies/ Corporations	46.75	7214.53	7261.28	46.75	6882.83	6929.58
Financial Institutions and Others	969.04	6947.77	7916.81	969.03	4223.55	5192.58
Total	**5746.69**	**16002.86**	**21749.60**	**5542.68**	**13170.44**	**18713.12**

4.2.1. FISCAL PERFORMANCE OF PSUs:

Some of the profit-making PSUs of the State are Odisha Mining Corporation (OMC), Odisha Hydro Power Corporation (OHPC) and Odisha Construction Corporation Limited (OCCL). On the other hand, GridCo, Odisha Power Transmission Corporation Limited (OPTCL) and IDCOL Ferro Chrome and Alloys Limited (IFCAL) are some of the loss incurring PSUs of the State. The State Government is most vulnerable to risks from the power sector PSUs, especially GridCo. The power sector PSUs represent about 70 percent of State Government investment in PSUs, about 94 percent of outstanding government guarantees and 86 percent of loans extended to PSUs.

Financial stress is mostly concentrated in the power sector. The architecture of the power sector is that there are multiple electricity generators, an electricity company and multiple distribution companies. The GridCo purchases power from multiple power generating companies at a price higher than the regulated sale price of electricity. The DISCOMs are operating at loss too. The reasons for poor financial health of the DISCOMs are unscientific tariff schemes, high AT&C losses and operational inefficiencies. GridCo is incurring consistent losses because of unrealized receivables from the DISCOMs over the years.

Although the State PSUs are subject to oversight by their respective Administrative Departments and Public Enterprises Department, but no consolidated report on the financial health of all the PSUs is being produced. It is critical for the State Government to closely monitor the performance and financial condition of each PSU because they can pose significant fiscal risks to the State Government. It is on this backdrop, Finance Department in consultation with *IMF SARTTAC* has undertaken fiscal risk assessment of major PSUs of the State. A sample of 30 important PSUs of the State is taken for conducting the risk analysis.

4.2.2. RISK ASSESSMENT OF STATE PSUs

The *IMF Risk Assessment Tool* is used to assess the fiscal health of the PSUs. The PSUs have been segregated into Non-financial and Financial sector PSUs following the best practices for financial health analysis of the PSUs. The qualitative assessment of the PSUs has been supplemented with quantitative analysis through analysis of annual reports of PSUs. The quantitative analysis constitutes both balance sheet and profit-loss statements analysis of PSUs.

Risk assessment of PSUs has been done based on four risk indicators such as liquidity, solvency, profitability and financial performance of the PSU. Each of the indicators has been assessed based on certain ratio calculation such as *Current Ratio, Quick Ratio, Debt to Equity Ratio, Debt to Assets Ratio, ROA, ROE, Cost Recovery Ratio* etc.

The risk assessment of PSUs indicates that the likelihood of risk materialization from PSUs of the State is low to moderate. The power sector PSUs especially Grid Corporation of Odisha (GridCo) and Odisha Power Grid Corporation (OPGC) are currently operating at relatively higher risk level vis-à-vis other power sector PSUs. The financial sector PSUs such as Odisha State Financial Corporation (OSFC) and Utkal Grameen Bank (UGB) are too operating at moderate to high risk level. The overall fiscal risk associated with the State PSUs would be moderate. The financial position and functioning of these PSUs will be monitored actively. The measures taken to improve fiscal condition of PSUs is explained in Chapter-V.

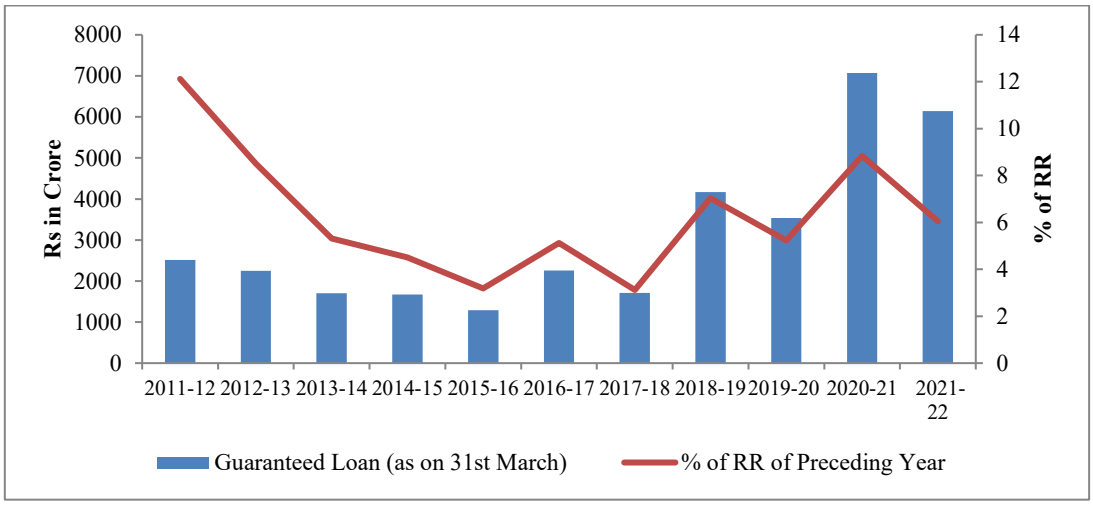
4.3. GOVERNMENT GUARANTEES

The total outstanding government guarantee as on 31st March 2022 is Rs.6140.91 crore which is 0.96 percent of GSDP. The guarantees do not form a part of the State government's loans, but it becomes incumbent on the State Government to discharge the guaranteed loan liability in case of failure on part of the borrowing organisations to service their debt covered under such guarantee. The guaranteed loan as a percentage of revenue receipts (Total Revenue Receipts of the second preceding year) has been reduced drastically from 123.37% in 2001-2002 to 7.93 percent during 2021-22. Major part of the guaranteed loan is availed by power sector PSUs.

Table 4.3- Sector-wise Outstanding State Guaranteed Loan (Rs. in Crore) as on 31st March 2022

SECTOR	GURANTEED LOAN AVAILED	OUTSTANDING LOAN
ENERGY	14835	6062.57
HOUSING & URBAN DEVELOPMENT	719.13	0.85
AGRICULTURE	18.41	11.29
HANDLOOMS	69.63	0.08
CO-OPERATIVES	1277.35	54.11
WOMEN & CHILD DEVELOPMENT	17.13	0.0
MSMEs	595.23	11.49
OTHERS	NA	.51
TOTAL		**6140.9 (0.96% of GSDP)**

Chart 4.1 - Outstanding State Guaranteed loan



As per the ceiling policy of the State Government, the outstanding government guarantees in a financial year should not exceed 80 percent of revenue receipts of the second preceding financial year. The outstanding government guarantee as a percentage of revenue receipts has been consistently reduced from a high of 80 percent in 2002-03 to about 6 percent in 2021-22. The overall fiscal risk exposure of the State Government due to guaranteed loan is low (below 1 percent of State GDP). In addition, the Government has a Guarantee Redemption Fund with a balance equivalent to approximately 20 percent of the outstanding stock of guarantees (see section 5.2.2) and an Escrow Account requirement for the repayment of guaranteed loans (section 5.2.3). Nevertheless, the total guarantee exposure is monitored closely to avoid materialization of any risk in future.

4.4. NATURAL DISASTERS

The geographical position of Odisha makes it prone to various natural disasters. Tropical cyclones ravage the coastal districts of the State almost every year. Besides the tropical cyclone, the State faces frequent floods due to heavy rain. Agriculture being an important economic activity of the State is heavily affected due to flood and drought because of unpredictable rainfall pattern across the State. The economic loss due to such frequent natural disasters put heavy burden on the State Finances. A lot of State resources go in management and mitigation of such frequent natural disasters. The State Government has to deploy resources immediately towards rescue, relief, rehabilitation, resettlement and restoration of critical infrastructure.

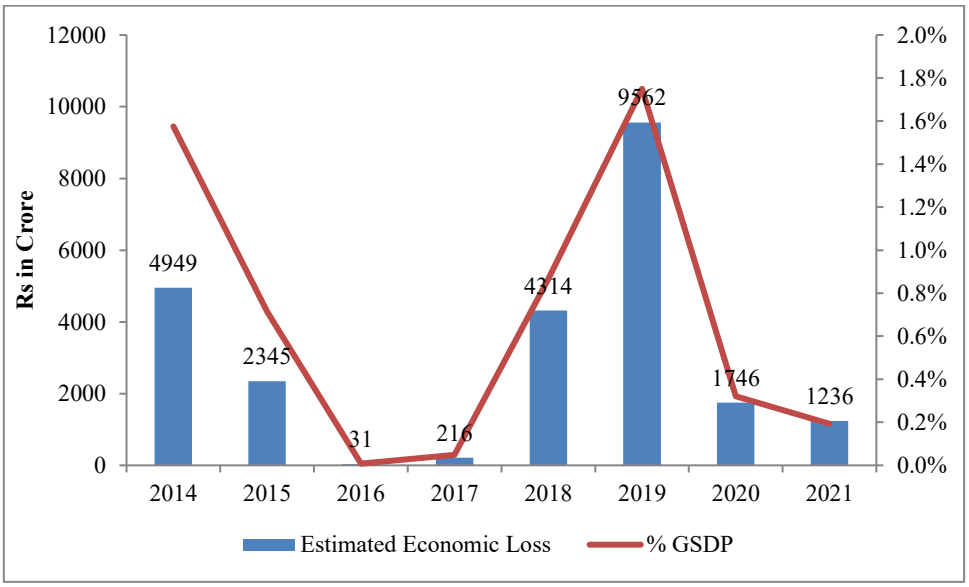
4.4.1. ECONOMIC LOSS DUE TO NATURAL DISASTERS

Apart from losses to life and property, natural disasters also lead to crop failure, decline in surface and groundwater level, increasing unemployment and under-employment, migration, and indebtedness. The natural disasters dent economic growth of the State. In addition to frequent tropical cyclones, the frequency of drought and flood is increasing every year. Since the year 2014, Odisha has faced eight tropical cyclones. The estimated economic loss due to natural disasters from 2014 to 2021 is about Rs. 24400 crore which is around 3.82 percent of GSDP (as per 2021-22 AE). The table below shows the estimated economic loss since 2014.

Table 4.4- Natural Calamities and Estimated Loss since 2014(Rs. in Crores)

Year	Calamity	Estimated Loss (Rs in Crore)	Total Loss(Rs in Crore)
2014	Cyclone-Hudhud	4949.39	4949
2015	Drought	2344.99	2345
2016	Flood	31.25	31
2017	Flood	216.23	216
2018	Cyclone-Titli & Flood	2779.32	4314
	Drought	1534.82	
2019	Cyclone-FANI	9337.27	9562
	Cyclone-Bulbul	224.43	
2020	Cyclone-Amphan	236.68	1746
	Flood	1509.33	
2021	Cyclone-Yash	823.49	1236
	Cyclone-Gulab	35.69	
	Cyclone-Jawad	376.65	
		Total	**24399.54**

Chart 4.2 – Estimated Economic Losses in Odisha due to natural disasters 2000-2020



*Source: Revenue & Disaster Management Department, Odisha Government
* Economic Losses include crop loss, infrastructure damage, livestock loss, private property

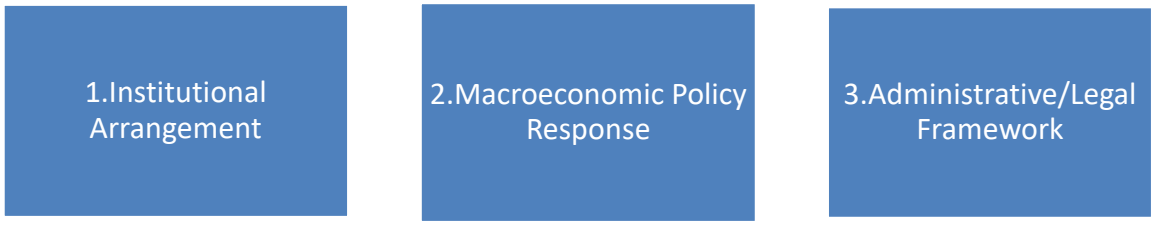
4.4.2. OVERALL RISK LEVEL DUE TO NATURAL DISASTERS:

The fiscal risk analysis shows that the financial risk to the State due to various natural disasters is very high. Therefore, recognition of fiscal risks due to Natural Disaster is critical for devising risk mitigation strategy effectively and efficiently. Besides the dedicated constituted funds to finance disaster response and management (section 5.2.6), it is critical to frame appropriate fiscal policy because the frequency of extreme climatic events will be higher in future due to climate change.

V: FISCAL RISK MITIGATION

Fiscal risk mitigation framework consists of mechanisms to handle the wide array of fiscal risks that the State is exposed to while carrying out social and economic developments. There are number of State public sector enterprises carrying out many critical works which are extremely important for overall development of the State. The State Government has to undertake Public Private Partnerships projects in areas like infrastructure development where the private sector is non-existent. Natural disaster is yet another risk that shatters the social and economic fabric every now and then.

This creates a huge opportunity to put in place a robust fiscal risk mitigation framework so as to ensure that fiscal shocks don't dent the socio-economic development of the State. The three broad pillars of the fiscal risk mitigation framework are:



5.1. INSTITUTIONAL ARRANGEMENT

5.1.1. FISCAL RISK COMMITTEE

The biggest institutional arrangement for oversight of fiscal risk is the creation of Fiscal Risk Committee in Finance Department under the chairmanship of Principal Secretary Finance.

The broad functions of the committee are

(i) To monitor the framework for fiscal risk management, quantifying risks and developing risk mitigation measures in priority areas.

(ii) To evaluate Fiscal Risk Statements, drawing on inputs from Strategic Macro Fiscal Planning Unit and other parts of Finance Department and Government.

(iii) Reviewing fiscal flows and transaction between government and PSUs; Financial performance and the position of PSU sector and individual PSUs.

5.1.2. DEPARTMENT OF PUBLIC ENTERPRISES

To regulate the functioning of State Public Sector Enterprises, Public Enterprises Department was created as the "Nodal Department of State Enterprises" on 4th January 1991. Since then it is rendering service in all functional areas of control and management in State Public Sector Enterprises.

5.1.3. DIRECTORATE OF PUBLIC PRIVATE PARTNERSHIP

The Directorate of PPP evaluates different aspects of risks and financial viability of the projects. All the PPP projects are also appraised to the ECI or HLCA where a panel of senior officers examined the projects in details including financial implications. Again the basic documents like RfPs, DPRs are also evaluated by PPP Directorate in terms of fiscal prudence. Project monitoring is also made by the PPP Directorate as the projects are evaluated at different stages starting from commencement of projects till the implementation and concession period. Some of the projects are modified in terms of fiscal prudence when it is replicated after taking the feedback from the implemented projects of similar types.

5.2. MACROECONOMIC POLICY RESPONSE

5.2.1. BUDGET STABILISATION FUND

The contribution of non-tax revenue from mining sector has substantially gone up from 25% of own revenue in 2020-21 to 51% in 2021-22. Revenue from this sector is sensitive to price fluctuation in international market and demand for metals in national and international markets. Also, it is subjected to variation in exchange rate between Indian Rupee and benchmarked currencies of the world. Considering the financial risks associated with mining revenue, the State Government has decided to put in place a "Budget Stabilisation Fund" which will act as a buffer fund to ensure financial stability during the period of negative shocks from the mining sector. A strategic reserve would be maintained in the fund to offset any decline in mining revenue in coming financial years. The size of the corpus and procedure to drawdown from the fund is being worked out.

5.2.2. CEILING ON GUARANTEES

The State Government has fixed the ceiling on guarantees during 2002-03 to regulate the guarantees as follows: "The total outstanding Government guarantees as on 1st day of April every year shall not exceed 100 per cent of the State Revenue Receipts of the second preceding year as reflected in the books of accounts maintained by the Accountant General. Attempts should be made to bring this gradually to the level of 80 per cent over next five years."

The guaranteed loan outstanding as percentage of the Revenue Receipts of the 2nd preceding year has been reduced drastically in the last seventeen years and the same has come down from 123.37% in 2001-2002 to 7.93 percent during 2021-22.

5.2.3. GUARANTEE REDEMPTION FUND

The Fund has been set up by the State Government during FY 2002-03 with an initial contribution of Rs.4.96 crore available under the erstwhile Guarantee Reserve Fund Scheme. The Fund is operated outside the State Government account and is administered by Reserve Bank of India. The proceeds of the fund are being invested and re-invested in Government of India Securities. The accumulation in the Guarantee Redemption Fund along with the interest

accrued thereon stands at Rs.1646.41 crore as on 31st March 2022 and would be utilised for meeting the payment obligations arising out of guarantees.

5.2.4. ESCROW ACCOUNT

In order to enforce financial discipline in the Public Sector Undertakings/Urban Local Bodies/ Co-operative Institutions and State owned companies etc., and to minimize the risk of default on payment of Government Guaranteed Loans, the State Government (Finance Department) in their resolution No. 11311/F., dt.19.03.2004 have issued instructions that the Public Sector Undertakings/Urban Local Bodies/Co-operatives institutions who have borrowed or intend to borrow against Govt. Guarantee will open an "Escrow Account" in a Nationalized Bank for timely repayment of Guaranteed Loans. The proceeds of this account shall first be utilized for payment of dues of the Financial Institutions and it is only after meeting such payments, the surplus amount shall be diverted for other payments including salaries.

5.2.5. GUARANTEE COVER ONLY FOR THE PRINCIPAL AMOUNT

With a view to limiting the guarantee exposure of the State, the Government took a decision during Nov, 2006. (Finance Department Resolution No.46546/F., dt.14.11.2006) that hence forth, the government guarantee shall be confined only to Principal Amount borrowed by the Public Sector Undertakings/ Urban Local Bodies/ Co-operative Institutions/ Companies etc.

5.2.6. CONSOLIDATED SINKING FUND

Government of Odisha created a Consolidated Sinking Fund (CSF) in 2002-03 with objective to utilize the corpus of the fund for amortization of debt in crisis years. The State had been making annual contribution equivalent to 0.5 percent of outstanding liability to the fund till the corpus reached 5 percent of outstanding liability. The scope of the fund has been expanded now to cover the foreign currency exchange risk related to external borrowing. The present corpus of the CSF is about 10 percent of the outstanding liability of the State Government.

5.2.7. DISASTER RESPONSE AND MITIGATION FUND

The State Government maintains a State Disaster Response and Mitigation Fund (SDRMF) with annual contribution of about 0.3 percent of GSDP as determined by successive Finance Commissions. The corpus of the fund takes care of the immediate response and restoration from the natural calamities. If the corpus of the fund becomes inadequate to meet the requirement in case of severe calamities, there is a mechanism of transfer of resources from the National Response and Mitigation Fund (NDRMF).

5.2.8. CORPORATE GOVERNANCE MANUAL FOR THE STATE PSUS

The State Government has adopted the "Corporate Governance Manual for the State PSUs" in 2010 as a policy to institute a system of good corporate Governance practices for Public

Enterprises so as to enhance transparency, accountability & certain measure of autonomy in their operations and improving their performance.

5.3. ADMINISTRATIVE/LEGAL FRAMEWORK

5.3.1. INDUCTION OF INDEPENDENT DIRECTORS IN THE BOARD OF PSUs

As part of Corporate Governance measure, Department of Public enterprises has created a panel of eminent persons of various fields/ professionals as Independent Directors and hoisted the same in the Department website and intimated the same to the PSUs out of which PSUs can select Independent Directors to be in their Boards. The main responsibility of the Independent Directors is to provide independent and broader perspective suggestions to their respective Board as well as the company.

5.3.2. AUDIT OF PSUs

Department of Public Enterprises, Odisha in the presence of the Administrative Department of the State PSUs and A.G., Odisha have reviewed the audit positions of the PSUs with regular interval and advised the defaulting PSUs to complete the annual audit and compilation of accounts in time.