

OPINION

# A Budget few can quarrel over



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## **elections**

Some said it was a 'make or break' Budget, one that would use the potential gains from demonetisation to give a decisive push to economic growth. Others said it would be a populist budget aimed at the upcoming elections in Uttar Pradesh and elsewhere.

It has turned out to be neither. Finance Minister Arun Jaitley has presented a 'don't rock the boat' Budget that is intended to reassure international investors that India will continue to be a bright spot in the world economy. In the climate of uncertainty that shrouds the world economy and the Indian economy alike, that seems sensible.

Foreign investors will be impressed with the stability of the Centre's finances. Mr. Jaitley has met the fiscal deficit target of 3.5% for 2016-17 in spite of exceeding the expenditure targets on both the revenue and capital accounts. This is in refreshing contrast to the past when the fiscal deficit target was met through cuts in capital expenditure.

Mr. Jaitley has managed his feat thanks to buoyant tax revenues for the second year in succession. Tax revenues have been boosted by buoyancy in both direct and indirect tax revenues. These have offset the shortfalls on account of spectrum sale and disinvestment. Customs duty has disappointed but excise duty and personal and corporate tax have contributed significantly. The government has taken advantage of low international oil prices to raise the excise duty on petroleum products.

The tax-to-GDP ratio has risen to 11.3% of GDP, compared to the Budget estimate of 10.8%. This is the first time since 2007-08 that the tax-to-GDP ratio has crossed the 11% mark; it had stagnated at around 10% since 2008-09. At the same time, the expenditure-to-GDP ratio has declined over the years. These are structural changes that will boost confidence in the Indian economy.

### **Meeting revenue targets**

For 2017-18, the fiscal deficit and revenue deficit are projected to decline to 3.2% and 1.9% respectively, compared to the targets laid out earlier of 3% and 1.8% laid out in last year's budget. Investors will not mind these slippages, given that the government is using the extra fiscal space to enhance capital expenditure by 25.4% over 2016-17.

The big question is whether Mr. Jaitley can meet the revenue targets for the coming year. He does not have the benefit of falling oil prices and higher excise duties any more. And the

target of Rs. 72,500 crore for disinvestment looks challenging when compared with receipts of Rs. 45,500 crore in 2016-17.

This is where the potential bonanza from the demonetisation comes in. The bonanza may be realised in several ways: extinguishing of some of the liabilities of the Reserve Bank of India as some of the demonetised currency does not come back into the system, the extra taxes payable under the Income Disclosure Scheme, and tax that could be recovered from income not declared in some of the deposits that have come into the banking system.

Prime Minister Narendra Modi's instinct about the demonetisation may thus turn out to have been spot on. It's not just the long-term gains that will be material. At a time when growth is faltering, the demonetisation could hold the key to realising more taxes and maintaining fiscal stability in the immediate future.

Contrary to what many had forecast, Mr. Jaitley has steered clear of populist giveaways in the run-up to Assembly elections. There are no farm loan waivers, no transfer of demonetisation gains to Jan-Dhan accounts, no announcement of a universal basic income. He has, however, made bold to increase the allocation for the MGNREGA by nearly 25%. The Congress party won't be amused.

The Finance Minister has cut the personal tax rate from 10% to 5% for individuals in the income slab of Rs. 2.5-5 lakh. He has also offered a uniform rebate of Rs. 12,500 to those in the higher tax slabs. A surcharge of 10% is proposed on those earning between Rs. 50 lakh and 1 crore. The net loss to the exchequer on account of these proposals is Rs. 12,800 crore. This might have been avoided given the focus on increasing tax collections but is, perhaps, excusable given the improvement in the tax-to-GDP ratio.

Mr. Jaitley has disappointed those who had expected a 'big bang' reduction in the corporate tax rate to 25%. Instead, he proposes such a reduction for only companies with an annual turnover of up to Rs. 50 crore. He has also not yielded to the clamour to abolish the Minimum Alternate Tax – he has only allowed companies to carry forward MAT credit for 15 years instead of the 10 years allowed at present. At the same time, he has cheered the markets by steering clear of any change to the tax on capital gains.

The Budget has the predictable schemes and initiatives aimed at particular segments: farmers, the rural poor, youth. There are measures to promote digitisation and affordable housing. Following up on the Prime Minister's pledge to battle corruption and black money, the Budget limits to Rs. 2,000 the maximum amount of cash donation that any political party can receive. Whether this will materially change illicit donations can be debated.

### **The growth picture**

This is a Budget that few can quarrel over. But is that good enough for a government that rode to power on a promise of accelerating growth to over 8% and creating jobs? The Budget assumes nominal GDP growth of 11.75% for 2017-18 which, according to the Economic

Survey, translates into real growth of 6.75-7.25%. This will come on the heels of growth of under 7% in 2016-17. Voters are unlikely to be impressed.

As the latest Economic Survey points out, for India to grow at 8% in the next decade, exports would have to grow at 15%. Until a couple of years ago, we could hope that export growth would revive once the global economy gathered steam. Now, we are faced with a more fundamental constraint: the world, led by the U.S., seems to be turning its back on globalisation.

Taking growth up to 8% in the changed global scenario will now require relying more on internal sources of growth. There is only so much fiscal space for increasing public investment. Private investment is not picking up because leading corporates are saddled with too much debt.

Public sector banks (PSBs) can't lend to those who are creditworthy because they have a huge load of non-performing assets and not enough capital. The Budget does little about the paralysis in banking. The proposed infusion of capital of Rs. 10,000 crore for PSBs means nothing. There is no initiative for resolving the non-performing assets issue either.

It does appear that the government is reconciled to growth in the region of 7-7.5% in the medium term. Perhaps, it hopes to manage the political fallout through a greater focus on redistribution. At a time of global uncertainty, there is merit in this approach, but achieving efficiency in redistribution remains a challenge.

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