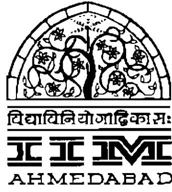

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Macroeconomic Analysis of the Union Budget 1998-99

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Abstract

Union Budget 1998-99 was the maiden budget of the newly elected coalition government led by the BJP. There were apprehensions about the economic philosophy of the new government indicating the possibility of a reversal of tax reforms introduced in the earlier budgets. The Finance Minister sought to achieve a wide ranging array of highly ambitious objectives and in the process ended up presenting a budget that lacked focus. An attempt has been made in this paper to present a broad macroeconomic analysis of the main proposals of the Union Budget 1998-99 and examine the likely impact of the budget proposals on Indian economy. An attempt has also been made to present the post-budget macroeconomic scenario for Indian economy for the year 1998-99.

MACROECONOMIC ANALYSIS OF THE UNION BUDGET 1998-99

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1. The Background

Union Budget 1998-99 was the maiden budget of the newly elected coalition government led by the BJP. There were many expectations as well as apprehensions about what the budget would contain or not contain. The main problems that the Finance Minister had to tackle while formulating the Union Budget for 1998-99 were declining growth rate of GDP, the industrial slow down, the slow down in the growth of exports, rising rate of inflation, failure of infrastructural investment to pick up, relatively depressed sentiments of the stock market and growing fiscal indiscipline. Given the seriousness of these problems, the Finance Minister was expected to aggressively pursue the long unfinished agenda of economic reforms and take some hard but essentially unavoidable economic decisions without any further delay. However, while the economic agenda was quite clear, there were apprehensions about the economic philosophy of the new government and it was widely feared that the Finance Minister might actually reverse the tax reforms introduced in the previous Budget. The Union Budget for 1998-99 needs to be viewed in this context.

2. Objectives of the Budget

The main objectives of the Union Budget for 1998-99, as stated explicitly by the Finance Minister in the first part of his Budget Speech, are as follows :

- Strengthen the foundations of the Indian economy to deal effectively with an inherently uncertain external environment.

- Reverse the decline in agriculture and strengthen the rural economy.
- Restore the momentum of industrial growth, especially of small scale enterprises, and revive the capital market.
- Accelerate the development of infrastructure.
- By these and other means, rapidly expand productive job opportunities.
- Give special impetus to social sector development.
- Calibrate the pace and character of integration with the world economy, while strengthening India's international economic position through revival of exports and reduced reliance on borrowed funds.
- Ensure macro-economic stability and control over inflation.
- Raise the rate of domestic savings to achieve higher national investment and thus lay the basis for faster medium-term growth. Supplement this effort through foreign investment.
- Free the productive energies of our people from unnecessary bureaucratic hurdles and undertake reforms to raise the productivity of our land, labour and capital.

It is evident that a comprehensive and fairly intensive effort on a large scale is required to achieve such a wide-ranging array of highly ambitious objectives. It is indeed very difficult for any single Budget to simultaneously take care of so many different objectives. An attempt to do so would lead to a lack of necessary focus in the Budget. It would have been much better if the Finance Minister had focused on acceleration of industrial growth, revival of exports and revival of capital market as the main objectives of the Budget.

It would be interesting to carry out a broad macroeconomic analysis of the budget proposals and their likely impact on the economy especially in the short run. In what follows, we have made an attempt to analyse the main proposals and provisions of the Union Budget 1998-99 aimed at achieving the above-mentioned objectives and the impact that these measures are likely to have on Indian economy during 1998-99. It may be noted that the Union Budget for 1998-99 presented on June 1, 1998 has undergone an unprecedented number of modifications and roll back of original proposals. The Finance Bill incorporating a series of amendments

announced from time to time since June 2, was finally passed by the Parliament on July 17, 1998. The main proposals and provisions of the budget (incorporating the relevant amendments) are summarised in *Exhibit 1*, while a summary of the budget estimates of aggregate revenue, expenditure and deficit is given in *Exhibit 2*. Details regarding various components of revenue receipts & expenditure are given in *Exhibits 3 & 4*.

3. Direct Tax Proposals

The major saving grace of the Union Budget for 1998-99 has been the continuation of the liberalised regime of direct taxes introduced in the previous budget by Mr. P. Chidambaram. It was widely speculated that Mr. Yashwant Sinha would impose a surcharge on both personal income tax as well as corporate tax and thereby effectively raise the tax rates and actually reverse the process of direct tax reforms initiated by his predecessors. That he has avoided the temptation of doing so despite the major shortfall in direct tax revenue witnessed during 1997-98 should in fact be viewed as a major relief. There is considerable merit in operating a stable tax regime over a reasonable period of time before arriving at any definite conclusion about the impact of liberalised tax rates on tax revenues.

The post-1991 period has witnessed a significant buoyancy in the direct tax revenue, which has been attributed to (a) the relatively much faster nominal growth of non-agricultural incomes (around 17% p.a.); (b) the estimated income elasticity of 1.2 for the personal income-tax revenue (computed on the basis of time-series data for the period 1985-86 to 1996-97); and (c) tax-payers' response to liberalised tax rates. During 1997-98, however, the growth of non-agricultural income has slowed down considerably and is likely to remain depressed during 1998-99 also. While there was a shortfall of about Rs.2000 crores in the personal income-tax collection target during the year 1997-98, its impact was more than offset by the spectacular success of VDIS 1997 which effectively mobilised additional revenue of Rs. 9050 crores by end of March 1998. Based on the experience of the preceding year, the Finance Minister seems to have moderated the personal income-tax collection target for 1998-99, which indicates an effective rate of increase of around

14% if we take into account the loss of revenue of Rs.1200 crores resulting from an increase in the income-tax exemption limit from Rs. 40,000 to Rs.50,000.

The previous budget presented by Mr. Chidambaram had introduced a special scheme for widening the income-tax net to cover non-tax paying residents of 12 metropolitan cities who satisfy any two of the four economic criteria, viz., ownership of four-wheelers, telephones, immovable property and foreign travel in the preceding year. In the budget for 1998-99, Mr. Yashwant Sinha has focused special attention on this scheme by extending its coverage to 35 cities and adding two more criteria, viz., club membership and possession of credit cards. Moreover, he has also tightened the qualifying condition by making it mandatory for any individual who falls within the purview of any one of the six criteria, instead of two out of four proposed earlier, to file income-tax return.

It may be noted that there is a substantial scope for ambiguity and discretion in the identification and assessment of the likely new assessees who may be covered under this scheme and whose number could be anywhere between 5 to 8 million. In fact, given the present structure and system of functioning of the income-tax department, this task would indeed be a Herculean task. The increase in the workload of the Income Tax Department would be enormous and it would require proper computerised information systems and a significant increase in the efficiency of income tax personnel to achieve this ambitious target of increasing the number of assessees for mobilising additional tax revenue. It should be noted in this context that any movement towards world class tax rates by itself cannot succeed in mobilising higher resources, if it is not backed up by world class tax administration. It would have been more appropriate for the Finance Minister to give some indication in his budget speech about the success of the earlier scheme based on four criteria implemented in 12 cities during 1997-98. The chances are that the scheme did not achieve the desired success and it would not be surprising if the new enlarged scheme also fails to achieve the ambitious target set by the Finance Ministry during 1998-99.

The revenue from corporate tax is projected to increase by Rs.5,200 crores, which implies an annual growth rate of 24%. Since the estimate of income elasticity of corporate tax revenue derived from the time-series data for 1985-86 to 1996-97 is only 1.1, the expected increase in the corporate tax revenue of such a high order is unlikely to materialise, especially in view of the prolonged recession in the industrial sector witnessed during the whole of last year and the first quarter of the current year. The experience of 1997-98 shows that there was a shortfall of Rs. 500 crores in corporate tax collections, the actual growth rate being only 12% as against the targeted growth rate of 15%. There is a distinct possibility, therefore, of a shortfall of at least around Rs.2,000 crores in the budget estimates for corporate tax revenue during 1998-99.

4. Indirect Tax Proposals

The Budget contains several proposals relating to the customs and excise duties primarily aimed at increasing the overall duty rates to mobilise additional resources.

4.1 Customs Duties

Mr. P. Chidambaram had aggressively pursued the tariff reform agenda in his Union Budget for 1997-98. With the overall objective of "bringing India's tariffs in accord with world levels", the then Finance Minister had reduced the peak rate of customs duties from 50% to 40% and also significantly reduced the duty rates on a large number of specified groups of items such as capital goods, project imports, inputs for several industries including steel, chemicals & textile machinery, steel products, telecom & computer equipment, etc. As against this, the budget presented by Mr. Yashwant Sinha for the year 1998-99 originally proposed an across-the-board increase of 8% in customs duties, which was subsequently brought down to 4%. Moreover, the basic rates of customs duty on several items have been increased in this budget. As a result, the weighted average rate of tariff in Indian economy is likely to increase from 29% in 1996 to more than 35% in 1998, which is

almost the same level as in 1993, implying that our customs reform clock has been effectively back-tracked by five years.

The Budget Estimates for 1998-99 indicate an increase in the customs revenue from Rs.41 thousand crores in 1997-98 (RE) to Rs. 48.1 thousand crores, indicating an increase of 18%. The projected increase in customs revenue needs to be viewed in the context of the experience of 1997-98. The budget estimates for 1997-98 projected an increase of 19% in customs revenue, whereas the revised estimates showed a decline of 7%. In effect the decline would have been much greater (more than 11%) if the exchange rate had remained unchanged during 1997-98. However, notwithstanding the experience of 1997-98, the Finance Minister has projected the customs revenue to increase by Rs.7.1 thousand crores during 1998-99, which, after providing for the upward revision of rates, implies an overall volume growth of more than 15% in aggregate imports. The preconditions for achieving such an ambitious growth target for customs revenue are significant buoyancy of the industrial sector during 1998-99 with an overall growth rate of industrial production of around 10% and the consequent rapid acceleration in the import growth, which has actually been quite sluggish during 1996-97 and 1997-98. Given the past experience and the recent trends observed during the first quarter of 1998, there is a distinct possibility of a significant shortfall in the customs revenue target during 1998-99.

4.2 Excise Duties

The basic purpose of the proposals relating to excise duties is to attempt further rationalisation of the existing excise duty structure so as to reduce the multiplicity of rates and ensure convergence towards a mean rate of 18% *ad valorem*. The ultimate objective of excise reform, as clearly spelled out by the Finance Minister, is to evolve an ideal tax structure where, barring the mean rate, there is one lower rate for items deserving concession and a higher rate for what may be described as demerit goods, i.e., to have a three-rate structure, which would "minimise the oscillation in rates". However, the specific proposals relating to the excise duty fall significantly short of these objectives and in effect imply widening of

the excise net and simultaneously increasing the average rate of excise duty as reflected in an overall revenue gain of more than Rs.5 thousand crores through the so called measures of rationalisation of excise structure.

The excise structure for the small scale sector has been revamped with an increase in the exemption limit for excise purpose from Rs. 30 lakhs to Rs. 50 lakhs of aggregate turnover and a flat nominal rate of 5% for the clearances between Rs. 50 lakhs and Rs. 1 crore. These measures, which are expected to result in a revenue loss of Rs.300 crores, essentially represent continuation of the excise reform for the small scale sector introduction in the previous Budget. The basic purpose of the revised excise scheme for the small scale units, introduced earlier and strengthened in this Budget, is to relieve them from the requirement of maintaining complicated records for availing MODVAT and also avoid the complexities involved in determining the exact classification of goods for computing the tax liability.

Total revenue from excise duties is targeted to increase by 21% during 1998-99. This is a highly ambitious target considering the fact that the revenue from excise duties increased by only 3% during 1997-98 as against the targeted increase of 13% provided in the budget estimates for 1997-98. Thus, in all probability there would be a significant shortfall in the excise revenue target during 1998-99.

The overall impact of indirect tax proposals (taking into account both customs as well as excise duties) on specific industries is indicated in *Exhibit 5.* On the whole, the indirect tax proposals will be inflationary in nature. It needs to be noted in this context that the across the board increase of 4% in customs duty finally proposed in the Budget is non-MODVATable and to that extent it would have a significant cascading effect, which would enhance the inflationary potential of the upward revision of customs duties.

5. Fiscal Deficit

The Finance Minister has claimed a major success in his endeavour to control the fiscal deficit in this budget, as the magnitude of fiscal deficit during 1998-99 is expected to be Rs. 91 thousand crores which represents 5.6% of GDP indicating a significant decline from the level of 6.1% observed in 1997-98. It would be interesting to examine the validity of this claim.

If the fiscal deficit can actually be restricted to the budgeted level, it should indeed be regarded as a major achievement under the prevailing socio-political and economic environment. However, the chances of the fiscal deficit being contained within its budgeted level do not appear to be very bright, especially in the light of the analysis of indirect tax proposals presented above coupled with information on the relevant components of public expenditure given in *Table 1*.

An important aspect of the control of fiscal deficit is the control of public expenditure. Some relevant information regarding the trends in selected components of public expenditure is presented in *Table 1*.

Table 1

Trends in Selected Components of Public Expenditure

(Rs. 000 crores)

Component of Public Expenditure	1996-97 (RE)	1997-98 (BE)	1997-98 (RE)	1998-99 (BE)
Aggregate of Interest Payments, defence expenditure & subsidies	102.2	120.7 (18.1%)	121.4 (18.8%)	138.2 (13.8%)
Other Non-Plan Expenditure	45.2	48.6 (7.5%)	53.2 (17.7%)	57.7 (8.5%)
Central Assistance to States and Union Territories	24.8	26.7 (7.7%)	27.0 (8.9%)	29.5 (9.3%)
Other Plan Expenditure	30.1	36.2 (20.3%)	33.6 (11.6%)	42.5 (26.5%)
Total Expenditure	202.3	232.2 (14.8%)	235.2 (16.3%)	267.9 (13.9%)

Note : Figures in parentheses indicate annual growth rates.

BE indicates Budget Estimates; and RE indicates Revised Estimates

It is evident from our analysis of direct & indirect tax proposals that there is a sizeable over-estimation of the expected revenue from each of the major tax categories. On the expenditure side, there appears to be a considerable under-estimation, especially in the case of the major component relating to non-Plan expenditure other than interest payments, defence expenditures and subsidies. As shown in *Table 1*, this major component, which accounts for almost one-fourth of total public expenditure, is budgeted to increase in nominal terms by only 8.5% during 1998-99. However, in the year 1997-98 this major component of public expenditure was budgeted to increase by only 7.5%, whereas it actually increased by almost 18%. A detailed comparison of the Budgeted and actual growth rates of various items of revenue and expenditure is presented in *Exhibit 6*.

Given the nature of coalition government at the Centre, Finance Ministry's assumption regarding their ability to exercise such a tight control on what essentially represents a politically sensitive & crucial item of Central Government's expenditure can only be considered as highly optimistic and far-fetched. In fact, a story similar to the last year is likely to be repeated during 1998-99, and as a result, we expect the actual level of total expenditure to significantly exceed the budgeted level. Thus, according to our estimates, the likely level of fiscal deficit during 1998-99 will be around Rs.108 thousand crores rather than Rs.91 thousand crores indicated in the budget estimates. The fiscal deficit-GDP ratio is, therefore, more likely to be 6.7% rather than 5.6%, as indicated by the Finance Minister. Thus, for all practical purposes no further fiscal correction has been achieved during the post-1993 period and the situation in 1998-99 on the fiscal front could actually turn out to be worse than what prevailed in 1993-94, which amounts to putting the clock of fiscal reform backwards by five years.

Another aspect that deserves special consideration while assessing the overall fiscal situation is the distinct possibility that the Central Government's fiscal problem is now actually being pushed to the State Governments resulting in a significant increase in the State-level fiscal deficit. With the regional parties dominating the current political scene and the growing competition among different political parties in various states to

introduce populist schemes effectively costing huge amounts to the state exchequers, there is already a clearly emerging trend for the state level fiscal deficit to increase, especially after 1994. The information on the state level fiscal deficit is provided in *Exhibit 7*.

The consolidated fiscal deficit of the State Governments is budgeted at Rs. 45.5 thousand crores in 1997-98, which represents a sharp increase of 64% from the corresponding amount of Rs.27.7 thousand crores in 1994-95. The experience of 1996-97 shows that the revised estimates of the gross fiscal deficit of State Governments turned out to be significantly higher (Rs.41.8 thousand crores) than the corresponding budget estimates (Rs. 36.5 thousand crores). It is, therefore, most likely that the actual magnitude of gross fiscal deficit of the States in 1997-98 would turn out to be significantly greater than the budgeted amount of Rs. 45.5 thousand crores. This experience of last four years represents a sharp contrast in relation to the period 1990-91 to 1993-94 during which the consolidated gross fiscal deficit of State Governments increased by less than Rs.2,000 crores (i.e., only around 10%). Moreover, during the last four years, there is a significant increase in the number of State Governments showing a revenue deficit. As many as 17 State Governments have budgeted revenue deficits during the financial year 1997-98, and this number is likely to increase further during 1998-99. Thus, even if the Finance Ministry achieves a moderate success in controlling the Central Government's fiscal deficit (which is unlikely as we have argued above), the country's fiscal problem would continue to remain unsolved because of the growing fiscal indiscipline at the state level. It is evident that such a large scale and rapidly growing fiscal deficit would turn out to be highly inflationary in the ultimate analysis.

6. Impact on the Capital Market

Viewed from the angle of Indian capital market, the Budget for 1998-99 can be regarded as the most unfriendly Budget presented since 1991. In fact, the overall macroeconomic impact of the Budget would lead to the commencement of the bearish phase, which could result in a significant downward shift of the lower

support level for Sensex. The sustainable Sensex bottom attracting spontaneous support is most likely to decline from the level of around 3700 witnessed during 1997 to 3100 during 1998 indicating a downward shift of more than 16%. Moreover, there could be at least a couple of reasonably durable but essentially short spells when the Sensex would actually fall below 3000 mark during the second half of 1998.

A depressed stock market would create serious obstacles for even the well managed companies to raise the much needed resources from the capital market. Moreover, it would also effectively block the way for a smooth and satisfactory implementation of the disinvestment programme for raising Rs.5000 crores as envisaged in the Budget and the actual realisation from the divestment programme is unlikely to exceed Rs.1000 crores as it happened during 1995, 1996 and even 1997.

The post-budget behaviour of the Stock Market has been quite discouraging and the market seems to be clearly heading towards a prolonged bearish phase as indicated by the performance indicators of the Bombay Stock Exchange and the National Stock Exchange shown in *Table 2*.

Table 2

Post-Budget Behaviour of BSE & NSE Indices

Period	BSE Sensex	NSE-50 Index
Pre-Budget Closing (June 1, 1998)	3794	1063
One Week after the Budget (June 8)	3417	969
Four Weeks after the Budget (June 26)	3290	949
Eight weeks after the Budget (July 24)	3085	899
Post-Budget Bottom level (Aug. 18)	2868	832
Twelve weeks after the Budget (Aug. 21)	2923	855

Thus, over a period of twelve weeks after the Budget, the stock market has already witnessed a steep decline. The market dropped to its post-budget bottom

on August 18 indicating 24% decline in the Sensex and 22% decline in NSE Index. Such a sharp decline in the country's leading stock markets has resulted in a large scale erosion of market capitalisation. Thus, during the six-month period from March to August 1998, the aggregate market capitalisation of securities listed on BSE has declined by more than 30%. The net foreign institutional investment in Indian stock markets has been negative during the three month period from June to August 1998 indicating the adverse impact of the budget on the sentiments of FIIs.

7. Post-Budget Macroeconomic Scenario

During the conventional post-budget briefing by the senior officials of the Finance Ministry, it was indicated that the Budget envisaged an overall GDP growth rate of 7% and an inflation rate of around 6.5% during 1998-99. In fact, the Budget estimates for 1998-99 are based on the assumption of 14.5% to 15% projected growth rate of nominal GDP at market prices. In the light of the above analysis of the Budget proposals, it is evident that the overall inflation rate during 1998-99 is likely to be around 9% and it might even turn out to be 10%. Thus, this Budget is most likely to fuel inflationary expectations in the economy. The other major negative aspect of this Budget is its failure to include any direct measures to boost the stagnating level of manufactured exports. This is particularly unfortunate as the last two years have witnessed a sharp deceleration in the growth of exports. Information on recent trends in India's foreign trade and related macroeconomic parameters is given in *Table 3.*

The latest available information on India's foreign trade reveals an alarming decline in aggregate exports during the first quarter of 1998-99, the observed growth rate being (-)8%. The industrial growth rate has also been slow during the first quarter of 1998-99, the index of industrial production indicating an overall growth rate of only around 5%. Food products, cotton textiles, wood products and machinery & equipment manufacturing industries were the major industry groups which actually experienced a decline in output during the first quarter of 1998-99. Moreover, during this period the FDI flows have also declined and several large projects involving an investment of more than Rs. 10,000 crores have actually been shelved.

Table 3 **Trends in Selected Macroeconomic Growth Parameters** (Annual Growth Rates)				
Macroeconomic Variable	1994-95	1995-96	1996-97	1997-98
Real GDP	7.8%	7.2%	7.5%	5.0%
Industrial Production	9.4%	12.1%	7.1%	4.2%
Exports	18.4%	20.7%	5.3%	2.6%
Imports	22.9%	28.0%	6.7%	5.8%
Foreign Currency Assets	38.1%	(-) 18.1%	31.2%	16.1%
Exchange Rate	(-) 0.1%	(-) 6.1%	(-) 5.8%	(-) 4.5%
Money Supply	22.3%	13.7%	16.0%	17.0%
Rate of Inflation :				
WPI	10.4%	5.0%	6.9%	5.0%
CPI	9.7%	8.9%	10.0%	8.3%

Given the strong evidence available now about the further slow-down in the growth of industrial production during 1997-98 with no clear signs of a significant revival during the first quarter of 1998-99, it is doubtful whether the Finance Ministry's optimistic projections of a double-digit industrial growth rate during 1998-99 would materialse at all. The latest available information on the corporate performance is also not very encouraging. The first set of quarterly results available for a sample of 944 manufacturing companies for 1998-99 clearly indicates that most of the smaller and mid-cap companies have been severely affected by the prolonged recession. Many of the large companies have also reported a significant slow down in the growth of sales as well as PAT and majority of the sample companies have experienced a substantial erosion in margins on sales during the first quarter of 1998-99. Thus, it seems that the Indian corporate sector is now slowly but surely entering a new phase of shake-outs and the famous principle of the survival of the fittest in a competitive environment is now beginning to play an important role in Indian economy. An assessment of the emerging post-budget macroeconomic scenario assumes special significance in this context.

Our forecast of the overall post-budget macroeconomic scenario for 1998-99 is presented in *Table 4*. Given the present state of uncertainties regarding both the global economic environment as well as the domestic political environment, we have presented our forecast in the form of a narrow range for each of the relevant macroeconomic variables.

Table 4

Post-Budget Macroeconomic Forecast for 1998-99

Macroeconomic Variable	Finance Ministry's Forecast	Our Forecast
GDP Growth	7.5%	4.5% to 5.5%
Industrial Growth	10.0%	5.0% to 6.0%
Inflation Rate	6.5%	9.0% to 10.0%
Fiscal Deficit (% of GDP)	5.6%	6.7% to 7.2%
Export Growth	NA	4.0% to 6.0%
Import Growth	NA	6.0% to 9.0%
Exchange Rate (Rs. per $) (March 1999)	NA	Around 45

It is evident from our post-budget macroeconomic forecast presented in *Table 4* that the high degree of optimism implicit in the Finance Ministry's projections of economic growth, inflation and fiscal deficit during 1998-99 is most unlikely to materialise. In fact, our macroeconomic forecast indicates an advance warning of the rough weather that the Indian economy will have to face during the course of its attempt to take off into the long lasting high growth phase. A strong and decisive corporate response to economic reforms and the emerging competitive pressures should actually represent the ideal instrument to deal with such rough weather. That is indeed the main reason why this budget should have focused more on the corporate sector than any of the earlier budgets presented during the post-reform period.

8. Conclusion

The above analysis of the Union Budget shows that the chances of a significant revival of industrial growth during 1998-99 are bleak and even if the agricultural growth rate improves significantly from negative growth of 2% in 1997-98 to a positive growth rate in 1998-99, the overall economic slow down is likely to continue. Thus, the golden opportunity provided by three consecutive years of high GDP growth coupled with a fairly comfortable balance of payments position has been badly squandered. As a result, the overall growth rate of Indian economy is unlikely to exceed 5% and the growth rate of exports is also likely to remain depressed during 1998-99.

The Budget in effect appears to be a gamble on the agricultural performance. The information available on the progress of monsoon till the end of July 1998 indicates that the proportion of gross cropped area which received normal or excess rains during 1998 is significantly lower than the preceding two years. Given our past experience in this regard, the most likely situation on the agricultural front will be a marginal decline in foodgrains production and only a marginal growth in non-foodgrain production during 1998-99. Besides agricultural performance, we also need to consider other major uncertainties facing Indian economy. In fact, the possibility of economic sanctions imposed by the developed countries along with international financial institutions, the possibility of a sharp increase in the international price of oil and the possibility of a drought are the three basic uncertainties that would seriously influence the overall impact of the Budget on Indian economy. If unfortunately any two of these three unfavourable conditions materialise during 1998-99, the growth rate of Indian economy might well fall below 5%, which coupled with an inflation rate of more than 9%, does not augur well for the economy. In such a scenario, the interest rates will rise and the Rupee will depreciate. Under these conditions, with foreign investment flows including the foreign portfolio investment drying up and with export growth not picking up, the Indian economy might well be on the brink of another economic crisis by the year 2000. Given this kind of a highly protectionist and inflationary Budget, we can only pray to God for a record bumper harvest and hope for

some sort of a miracle to pull the Indian industry out of the recessionery trend. Perhaps through this Budget, the Finance Minister wants to tell us that we should hope for the best and be prepared for the worst. While the success of Resurgent India Bonds floated in August 1998 in mobilising US $ 4.2 billion does represent a silverlining in the dark clouds haunting Indian economy, it remains to be seen whether this could be regarded as a matter of luck or a clear signal of turn-around in the international investor community's outlook on Indian economy. At this juncture, we feel that it is luck rather than Government's decisive action which would ultimately determine the prospects for Indian economy during 1998-99. It is indeed unfortunate that this Budget has shattered our dreams of witnessing the emergence of Indian economy as a new Asian tiger by the turn of the century.

Exhibit 1

Main Provisions of the Union Budget 1998-99

- Fiscal deficit to be reduced from 6.1% of GDP in 1997-98 to 5.6% in 1998-99.
- Significant additional resource mobilisation of Rs. 8300 crores (subsequently rolled back to Rs. 5300 crores) through several indirect tax proposals.
- No changes in personal income-tax and corporate tax rates.
- Personal income-tax exemption limit raised to Rs.50,000 and standard deduction on salaries exceeding Rs.500,000 withdrawn.
- Gift tax abolished altogether.
- Persons fulfilling any one of six specified conditions including possession of credit card and specified club memberships, compulsorily required to file returns of income. The scheme extended to 23 more cities taking the total coverage to 35 cities.
- Proposal to introduce a simple one page taxpayer-friendly return form to be called `*SARAL*', which will be applicable to all non-corporate tax payers.
- Tax evasion attempts to be curbed by making it obligatory for assessees to quote their PAN or GIR number mandatorily in respect of specified high value transactions
- Interest income of foreign lenders now taxable in certain cases.
- Increased deductions and carry forward of losses available to income from house property.
- Depreciation allowed on intangible assets; consequently, expenditure on acquisition of patents/copy rights/technical know-how no longer eligible for tax deduction.
- Special provisions introduced for expense deductions and capital receipts on transfer of businesses engaged in prospecting or extraction or production of petroleum or natural gas.
- Conversion of a firm/proprietory concern to a company not to attract capital gains tax.
- Industrial undertakings allowed additional deductions equal to 30% of wages paid to new workmen.
- Residents executing World Bank aided construction projects allowed deductions equal to 50% of the profits from such projects.
- Tax holiday extended to radio paging and domestic satellite service operators, inland waterways, ports, housing projects and refineries set up in the North East.
- Special additional customs duty at the rate of 4% levied on all imports with the exception of some specified items.
- A scheme to be called `*Samadhan*' to be introduced for resolution of cases under litigation, with abatement along with waiver of interest, penalty and immunity from prosecution.

- Duty rates on select commodities reduced in compliance with WTO norms.
- Increase in duty announced on specified steel products; spark ignition, compression ignition engines and their parts used for motor vehicles; motor spirit; paper and paper-boards.
- Reduction in duty announced on newsprint, including glazed newsprint; leather machinery; jumbo rolls of films; computer hardware and their parts; telecommunication software; specified textile intermediaries; specified drugs; crude petroleum.
- Duty free baggage allowance doubled.
- Efforts to rationalise rates towards a mean rate of 18% and shift towards a Central Value Added Tax System continued.
- Excise duty to be levied on Maximum Retail Price basis for several additional products.
- Excise duty exemption to Small Scale Industries (SSIs) enhanced.
- Excise duty rate on multi-utility vehicles, unrecorded audio cassettes, motor spirit, etc. increased.
- Excise duty rate on alcohol based toiletries, pagers, etc. reduced and exemption granted to recorded audio cassettes; video cassettes intended for television broadcasting; software, etc.
- Levy of service tax extended to include 12 new specified services and Service tax on goods transport operators, outdoor caterers, etc. withdrawn.
- Coal, lignite and petroleum products to be delicensed.
- Farm tools and implements to be dereserved from the SSI sector.
- Time-bound clearance and monitoring for foreign direct investments proposed.
- The Foreign Exchange Regulation Act, 1973 to be replaced by the Foreign Exchange Management Act and an Anti-Money Laundering Bill.
- Investment schemes in the nature of increased portfolio investment limits, special schemes of the Unit Trust of India and SBI bonds and other benefits proposed for NRIs.
- 10% of the new accretions to provident funds permitted to be invested in rated infrastructure projects.
- Stock index futures to be brought within the purview of `securities' by amending the Securities Contracts (Regulation) Act, 1956.
- Software companies will now be permitted to introduce dollar denominated options on shares issued under the ADR/GDR regime.
- Private sector participation mooted in the insurance sector.
- Foreign Institutional Investors permitted to invest in unlisted debt securities.

***Exhibit 2* : Union Budget 1998-99 at a Glance**

(Rs. crores)

		1992-93 Actuals	1993-94 Actuals	1994-95 Actuals	1995-96 Actuals	1996-97 Actuals	1997-98 BE	1997-98 RE	1998-99 BE
1	Tax Revenue	54044	53449	67454	81939	93701	113394	99158	116857
2	Non Tax Revenue	20084	22004	23629	28191	32578	39749	39356	45137
3	Revenue Receipts	74128	75453	91083	110130	126279	153143	138514	161994
4	Loan Recoveries	6356	6191	6345	6505	7540	8779	9479	9908
5	Other Receipts	1961	-48	5607	1397	455	4800	907	5000
6	Borrowing	27861	49297	56743	50436	66733	65454	86345	91025
7	Capital Receipts	36178	55440	68695	58338	74728	79033	96731	105983
8	Total Receipts	110306	130893	159778	168468	201007	232176	235245	267927
9	Interest Payments	31035	36695	44049	50031	59478	68000	65700	75000
10	Revenue Exp.	92702	108169	122112	139860	158933	183408	182200	210062
11	Capital Expenditure	29916	33684	38627	38415	42074	48768	53045	57855
12	Total Expenditure	122618	141853	160739	178275	201007	232176	235245	267927
13	Revenue Deficit	18574	32716	31029	29730	32654	30265	43686	48058
14	Capital Surplus	6262	21756	30068	19843	32650	30265	43686	48128
15	Fiscal Deficit (3+4+5-12)	40173	60257	57704	60243	66733	65454	86345	91025
16	Primary Deficit (15-9)	9138	23562	13655	10212	7255	(-) 2546	20645	16025

Exhibit 3

Union Budget 1998-99 : Summary of Receipts

(Rs. Crores)

	Item	1996-97 RE	1997-98 BE	1997-98 RE	1998-99 BE
I	Tax Revenue				
	1. Corporation Tax	19010	21860	21360	26550
	2. Income Tax	18843	21700	28750	20930
	3. Interest Tax	2000	1800	800	920
	4. Expenditure Tax	190	210	210	300
	5. Wealth Tax	110	130	130	145
	6. Customs Duties	44135	52550	41000	48148
	7. Excise Duties	46190	52200	47700	57690
	8. Service Tax	970	2150	1500	1867
	9. Other Taxes & Duties	871	1047	1270	1161
	10. Gross Tax Revenue	132319	153647	142720	157711
	11. Share of States & UTs	35107	40254	43562	40854
	12. Net Tax Revenue	97212	113393	99158	116857
II	Non-tax Revenue				
	1. Interest Receipts	21945	24092	25327	27954
	2. Dividends & Profits	4077	6013	5862	7373
	3. External Grants	1199	1100	1170	1054
	4. Other Non-tax Revenue	6350	8545	6997	8756
	5. Total Non-tax Revenue	33571	39750	39356	45137
III	Capital Receipts				
	1. Recoveries of Loans	7809	8779	9479	9908
	2. Market Borrowings	4025	4070	4070	NA
	3. Other Short, Medium & Long Term Loans (including Treasury Bills & Zero Coupon Bonds)	21473	29750	38414	48326
	4. External Assistance	2589	2435	1201	2337
	5. Disinvestment of Equity in Public Enterprises	500	4800	906	5000
	6. Small Savings, PPF & Staff PF	17450	16550	28678	26990
	7. Special Deposits & Other Receipts	10694	12649	11658	13372
	8. Total Capital Receipts	64615	79033	96731	105933

Exhibit 4

Union Budget 1998-99 : Summary of Expenditure

(Rs. Crores)

	Item	1996-97 RE	1997-98 BE	1997-98 RE	1998-99 BE
1	Non-Plan Expenditure				
	a) Interest Payments	58500	68000	65700	75000
	b) Food & Fertilizer Subsidies	14233	17130	18366	19883
	c) Other Subsidies	2461	1121	1278	2142
	d) Write-off of Loans to States	301	212	790	1013
	e) Defence Expenditure	29498	35620	36099	41200
	f) Pensions	5095	5251	6883	7342
	g) Social Services	3401	3461	4358	4865
	h) Economic Services	5275	4001	4524	5003
	i) Grants & Loans to States	17088	16366	20442	21046
	j) Grants & Loans to Foreign States	363	516	499	594
	k) Other items	11189	17646	15676	17837
	Total Non-plan Expenditure	147404	169324	174615	195925
2	Plan Expenditure (4+5)	54894	62852	60630	72002
3	Total Expenditure	202298	232176	235245	267927
4	Central Assistance to State & UT Plans	24790	26722	27001	29538
5	Budgetary Support for Central Plan	30104	36130	33629	42464
6	Internal & Extra Budgetary Resources of Public Enterprises	47414	55709	47404	62723
7	Total Central Plan Outlay (5+6)	77518	91839	81033	105187

Exhibit 5

Sectoral Impact of Indirect Tax Proposals

Sector	Effect	Nature of Impact
Air-conditioning & Refrigeration	Negative	Increase in input costs due to additional import tariff.
Aluminium	Positive	Additional Import duty to raise the cost of imported metals and improve margins.
Automobiles - 2/3 wheelers	Negative	Increase in input costs. Negative impact of petrol price hike.
Automobiles - 4 wheelers	Neutral	Higher input costs expected to be passed on.
Auto Ancillaries	Neutral	Increase in steel prices to be passed on.
Banks	Neutral	Budget not expected to facilitate credit offtake.
Cement	Neutral	Impetus to housing and road sectors should spur demand, but input cost will increase
Chemical - Inorganic	Positive	Realisations to increase as prices are bench-marked to landed cost of imported materials.
Cigarettes	Negative	Excise duty hike will have an adverse impact on volume growth.
Consumer durables	Neutral	Increase in input costs due to additional import tariff but the competition from MNCs may actually decline.
Electrical Equipment	Negative	Higher import duty on inputs will adversely affect profits as imports represent a major proportion of current inputs.
Fertilizers	Positive	Increase in subsidy on fertilizers will increase demand resulting in off-take.
Housing Financing Companies	Positive	Concession to housing sector to boost demand for housing loans
Oil & Gas	Positive	Higher import duties on petroleum products and lower import duties on crude oil will increase profits.
Packaging	Neutral	PET/BOPP fill manufacturers to benefit from price rise. Laminate manufacturers adversely affected.
Paints	Neutral	Major players expected to pass on cost increases to final consumers.
Paper & Paper Products	Positive	Higher duty on imports to boost demand for domestic paper. Lower import duty on newsprint will be off-set by higher international prices and rupee depreciation.
Personal Care & Detergents	Negative	Lower excise duties on alcohol based toiletries, but overall input costs will increase significantly.

Petrochemicals	Positive	Increase in product prices will benefit manufacturers.
Pharmaceuticals	Neutral	Domestic bulk drug manufacturers will benefit but import intensive manufacturers will be adversely affected.
Power Cables	Negative	Import duty increase on copper and polyethylene will adversely affect the margins.
Steel	Positive	Rise in import duties likely to increase pricing flexibility and improve the margins.
Tea & Coffee	Negative	Higher excise duty on packaged tea to adversely affect the margins.
Textiles	Negative	Increase in man-made fibre prices to adversely affect overall profitability.
Telecom Cables	Negative	Import duty increase on copper and polyethylene will lead to a fall in the margins.
Telecom Equipment	Neutral	Marginal decrease in duty on imported parts.
Tractors	Neutral	Excise hike may temporarily effect demand. Steel cost increase is likely to be passed on to the buyers.

Exhibit 6 **Budgeted V/s. Actual Growth Rates of Revenue & Expenditure**			
Item	97-98 BE	97-98 RE	98-99 BE
Corporate Tax	15%	12%	24%
Personal Income-tax (excl. VDIS)	15%	(-) 9%	6%
Customs Duties	19%	(-) 7%	18%
Excise Duties	13%	3%	21%
Total Tax Revenue (incl. VDIS)	16%	0%	19%
Non-tax Revenue	18%	17%	15%
Revenue Receipts (Net)	21%	10%	17%
Capital Receipts	22%	50%	10%
Market Borrowings & Loans	33%	67%	26%
Total Receipts (Net)	16%	17%	14%
Revenue Expenditure	15%	15%	15%
Capital Expenditure	16%	26%	9%
Total Expenditure	15%	17%	14%
Plan Expenditure	15%	10%	19%
Non-plan expenditure	15%	18%	12%
Non-plan Expenditure excl. subsidies, Interest & Defence expenditure	11%	25%	9%
Subsidies	9%	18%	12%
Allocation to Agri. & Rural Dev.	15%	4%	25%
Allocation to Infrastructure	25%	8%	35%
Budgetary support for Central Grant	20%	12%	26%
IEBR of PEs	17%	0%	32%
Central Plan Outlay	18%	4%	30%

Exhibit 7

Trends in the Gross Fiscal Deficit of State Governments

(Rs. Crores)

Sl. No.	States	1994-95 (Actuals)	1997-98 (BE)
1.	Andhra Pradesh	2348.5	3,178.8
2.	Assam	710.6	741.2
3.	Bihar	1342.1	1551.4
4.	Goa	44.5	176.7
5.	Gujarat	1292.4	2456.5
6.	Haryana	534.6	1690.3
7.	Himachal Pradesh	620.4	638.0
8.	Jammu & Kashmir	(-) 23.4	214.6
9.	Karnataka	1512.8	1510.4
10.	Kerala	1108.7	1977.3
11.	Madhya Pradesh	1416.9	1848.2
12.	Maharashtra	2861.3	3735.7
13.	Manipur	62.1	225.1
14.	Orissa	1158.8	1,912.8
15.	Punjab	1785.3	2145.4
16.	Rajasthan	1762.7	2185.3
17.	Tamil Nadu	1496.4	3067.9
18.	Uttar Pradesh	4766.5	11023.9
19.	West Bengal	1965.3	4098.6
20.	Other States	907.0	1151.5
21.	Total (All States)	27696.9	45529.6

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