Budget well meaning, but may miss deficit target

BY INVITATION
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Expectations from the Budget for 2020-21 were running high because of the background against which the Budget had to be prepared. There were three disturbing trends in the economy — a perceptible slowdown in growth, a steep fall in investment rate and a stressed financial system. The Budget was expected to address all these issues and also lay the foundation for a significantly faster economic growth. Otherwise, the $2 trillion economy will be only a distant reality.

Overall, the Budget is well intentioned, even though it does not use the word ‘slowdown’ even once. It outlines at length the multiple objectives it seeks to achieve. While the expenditure programmes may show how demand will be revived, the revenue projections along with the fiscal deficit will indicate whether these expenditure programmes are sustainable. It is to this scrutiny we turn our attention.

While the fiscal deficit in the current fiscal year is 3.8%, the projected fiscal deficit for 2020-21 is 3.5%. While these levels are above the implicit mandate of 3% of GDP, they are nevertheless at reasonable levels considering the overall commotion to raise government revenues to stimulate demand. However, the question is whether the 3.5% fiscal deficit will stick.

The nominal GDP in 2010-11 is assumed to grow by 10%. This is realistic. The gross tax revenue is assumed to grow by 12%. Thus the buoyancy is greater than one which did not materialise in the current year. The reliance on disinvestment is high while there may be special circumstances such as LIC disinvestment which may be helpful. However, the disinvestment target has in the past not been fulfilled in any year.

The Finance Ministry has to monitor the revenue growth so that expenditure must be adjusted such that the fiscal deficit can be maintained. In fact, taking the expenditures as given, the possibility of the government exceeding the budget’s fiscal deficit is very much there. The escape clause should be seen as permitting the government to exceed the implicit mandate of 3% rather than over and above what is budgeted. It is hoped that the government would not invoke the escape clause to ask the RBI to enter the market.

Some of the changes in the tax regime are significant. A major effort was made some months ago to cut the corporate tax rate. In this budget, some steps have been taken in the direction of simplifying personal income tax. The impact of this may be very limited. In fact, the broad principle of reducing the tax rate along with withdrawing exemptions must be taken to the logical end and must cover entire gamut of personal income tax. We should move towards a single regime rather than piecemeal.

Several of the measures proposed may help to accelerate the inflow of funds from abroad. The withdrawal of Distribution Dividend Tax is welcome, particularly on equity grounds. While relaxation in investment by non-residents in government paper in rupee terms is acceptable, caution must be exercised. Easy access should not pave the way for larger borrowing.

Rangarajan is the former chairman of the Economic Advisory Council to the Prime Minister and former governor of Reserve Bank of India.