

Public Finance

Background

Union Budget 2007, the UPA government's fourth, was a reiteration of the regime's commitment to the provisions of the Fiscal Responsibility and Budget Management (FRBM) Rules, 2004. It projected a revenue deficit of 1.5 per cent and gross fiscal deficit of 3.3 per cent of GDP for the present financial year, which was lower than even FRBM projections - of 1.98 per cent and 4.32 per cent respectively. In fact it bettered the revised esti-

mates of 2 per cent and 3.7 per cent respectively. The Budget-making process envisaged revenue-led correction along with reprioritisation of expenditure to augment allocations for agriculture and the social sector.

Gross tax revenue is projected to grow from Rs 5,48,122 crore in 2007-08(BE), compared to Rs 4,42,153 crore in 2006-07(BE). The growth in tax revenue is expected to be higher by 23.4 per cent in 2007-08 (BE) compared to 21.1 per cent

Table PF.1: Budget at a glance in Rs Crore (growth rate per annum)

Budget Heads	2005-06 (BE)	2006-07 (BE)	2007-08 BE
Revenue Receipts	13.54	14.88	20.56
- Tax Revenue	16.91	19.65	23.43
- Non-tax Revenue	3.07	-1.90	8.25
Capital Receipts	-3.18	-1.60	20.91
- Recoveries of Loans	-55.72	-33.33	-81.25
Total Receipts	7.64	9.65	20.66
Non-Plan Expenditure	11.62	5.51	21.51
- On Revenue Account	12.56	4.21	11.36
- Interest Payments	3.43	4.39	13.71
- On Capital Account	4.48	16.16	96.18
Plan Expenditure	-1.44	20.37	18.74
- Revenue Expenditure	26.28	23.95	21.28
- Capital Expenditure	-48.81	5.27	6.15
Total Expenditure	7.64	9.65	20.66
- Revenue Expenditure	15.83	9.33	14.28
- Capital Expenditure	-26.54	11.75	61.77
Revenue Deficit	25.13	-11.11	-15.64
Fiscal Deficit	10.00	-1.63	1.52
Primary Deficit	117.52	-48.47	-190.79

in 2006-07 (BE). The continued growth in the share of gross tax revenue to GDP is expected to be driven by direct tax collection. Non-tax revenue is proposed to grow by 8.3 per cent, from a decline of 1.22 per cent in 2006-07.

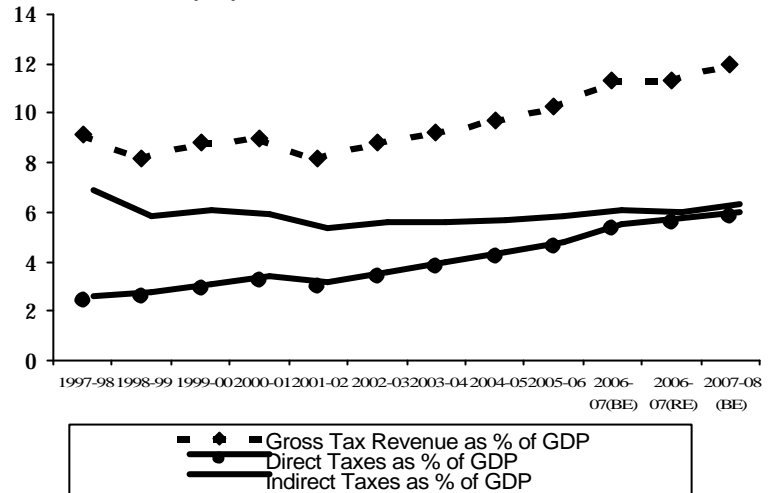
As revenue projections grow, expenditure proposals rise - albeit at a marginally higher rate in this instance. The total expenditure of the central government is projected to grow by 13.6 per cent in 2007-08 (BE) compared to 11.4 per cent projected in 2006-07(BE) - that is, from Rs. 5, 63,991 crore to Rs. 6, 40,521 crore respectively. This moderation in the growth of the expenditure is driven by the need to reduce revenue and fiscal deficit. The government has also achieved a primary surplus.

In terms of broad composition of tax revenues of the Centre, the revenue from direct taxes is improving in comparison to indirect taxes.

Trends in central government revenues

The growth picture is currently buoyant. In June 2007, the Central Statisti-

Fig PF.1: Tax revenue of the union government as a proportion of GDP at Market Prices



cal Organisation (CSO) upped its GDP growth estimates to 9.4 per cent for 2006-07, over its advance (February) estimate of 9.2 per cent. The drivers of high growth have been industrial and service sectors, both of which grew by 11 per cent. The GDP in Q4 (January-March 2007) grew year over year by 9.1 per cent, compared to 10 per cent in the corresponding quarter of 2006.

Table PF.2: Quarterly growth rate for major items of revenue

Year	Quarter	Net Tax Revenue	Gross Tax Revenue (Total)	Gross Tax Revenue (Corporation Tax)	Gross Tax Revenue (Income Tax)	Gross Tax Revenue (Customs)	Gross Tax Revenue (Excise Duties)	Gross Tax Revenue (Other Taxes)	Surcharge for Financing NCCF	Tax Revenue Assigned to States	Non-Tax Revenue
2004-05	Q1	26.78	21.58	25.28	74.38	-3.92	12.84	56.65	-21.63	15.72	7.77
	Q2	16.71	18.48	2.93	72.68	20.35	6.30	30.60	-43.35	26.66	-3.25
	Q3	17.95	16.57	53.37	-43.30	21.77	10.62	40.85	58.80	11.21	-18.45
	Q4	22.71	22.69	33.38	8.81	33.76	8.91	107.17	-9.97	23.61	36.03
2005-06	Q1	30.29	25.95	182.20	-21.67	38.57	4.03	43.66	-27.60	20.52	0.16
	Q2	20.59	19.52	39.01	-12.39	13.45	14.15	148.15	13.27	16.36	-9.23
	Q3	14.32	14.63	-9.64	130.85	3.44	6.30	94.53	-5.79	16.20	15.24
	Q4	21.45	22.18	20.52	18.26	4.81	17.92	105.97	4.60	24.85	-11.84
2006-07	Q1	40.40	32.13	50.00	29.34	31.98	6.63	81.07	34.81	19.28	25.00
	Q2	32.43	29.49	48.83	21.02	33.42	7.78	54.00	69.67	19.49	15.99
	Q3	41.01	36.18	62.93	30.82	33.27	6.03	65.28	-5.88	19.83	-19.18
	Q4	17.50	23.27	21.36	51.06	31.99	4.27	39.39	-44.79	42.18	14.78
2007-08	Apr-May*	44.00	34.96	231.80	22.14	23.14	13.54	37.09	63.11	26.32	-1.63

* Data so far is available only for April-May 2007

With such high growth, it is natural to expect higher revenue collection during this period. However, available information on government finances during April-May 2006-07 indicates need for caution. In April-May 2007, tax revenue (net to Centre) growth was higher by 44 per cent in comparison to 74.2 per cent growth recorded exactly a year ago.

However, on the other hand, Total Expenditure actually declined during this period by 1.3 per cent, compared to a rise of 53.9 per cent in the corresponding period of 2006-07. As a result, revenue deficit declined by 13.5 per cent during April-May, whereas there was an actual rise of 55.4 per cent in the corresponding period in the last fiscal. Similarly, fiscal deficit has

also declined by 13.8 per cent during the first two months of 2007-08, compared to a growth of 51.4 per cent in April-May 2006-07. This reflects the government's cautious fiscal approach.

Trends in Central Government Expenditures

It is now recognised that growth alone would not suffice. It would not guarantee the flow of benefits across the diverse resource owners. In the words of Dr Manmohan Singh, there is need for a growth process that is "more inclusive" -- one that "ensures access to essential services such as health and education for all sections of the community".

Table PF.3: Trends in central government expenditure: selected items

Selected Expenditure Items	Averages			2006-07 (BE)	2007-08 (BE)
	1997-98 to 1999-00	2000-01 to 2002-03	2003-04 to 2005-06		
Ratio to GDP %					
Education, Arts & Culture	0.24	0.26	0.35	0.51	0.59
Health and Family Welfare	0.19	0.22	0.23	0.30	0.28
Social Welfare and Nutrition	0.11	0.11	0.09	0.12	0.12
All Other Social Services	0.27	0.31	0.40	0.56	0.64
Total Social Services	0.81	0.90	1.07	1.49	1.63
Total Subsidies	1.27	1.48	1.46	1.18	1.19
Plan expenditure	3.86	4.32	4.18	4.41	4.48
Non-Plan expenditure	11.61	11.78	11.42	10.00	10.39
Total expenditure	15.48	16.10	15.60	14.41	14.88
Share in expenditure %					
Education, Arts & Culture	1.54	1.64	2.22	3.51	3.98
Health and Family Welfare	1.22	1.34	1.46	2.07	1.90
Social Welfare and Nutrition	0.72	0.67	0.58	0.83	0.82
All Other Social Services	1.76	1.92	2.60	3.91	4.27
Total Social Services	5.24	5.57	6.86	10.32	10.98
Total Subsidies	8.23	9.22	9.34	8.19	7.98
Plan expenditure	24.96	26.82	26.78	30.63	30.14
Non-Plan expenditure	75.04	73.18	73.22	69.37	69.86

The FRBM Act was enacted by Parliament in 2003 and received the President's assent in August the same year. The UPA government had notified the FRBM Rules in July 2004. Under this Act, and amended later, the government is required to bring down revenue deficit to zero by 2008-09. The logic behind the FRBM is that if the government spends more than what it earns, and relies on borrowings, which it pays back with interest. If the money collected by the government could be spent on important sectors such as education, social services and necessities that people expect in the form of public provisioning, it would be possible to have a better-equipped and productive future generation. However, the general trend so far reveals that after making interest payouts and meeting other necessary overheads, what is left with the government for spending on the social sector is hardly adequate.

The share of education, arts and culture in GDP is 0.59 per cent in 2007-

08(BE) compared to 0.51 per cent in 2006-07 (BE) (Table 3). The average share during 2003-04 to 2005-06 was 0.35 per cent. So, there is a slow but steady increase in expenditure under this head. However, there is a need to examine education expenditure per se to fully understand the growth in expenses on education. While examining the expenditure under 'Health and Family Welfare', we find that this vital sector's growth as well as share of total expenditure has actually fallen in comparison to 2006-07 (BE). Subsidies have been reined in marginally, and, overall, there has been a tightening of expenditure. Naturally, this has led to the articulation of concerns about the social sector.

Therefore, in a line with the recognised need to have inclusive growth, there is scope for a more well designed mechanism for revenue and expenditure management to further improve growth and productivity, thereby improving the fiscal strength of the economy.