

# Budget 2010-2011: Fiscal Adjustment and Tax Policy

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# Scheme of Presentation

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- Finance Minister's Dilemmas.
- A Stocktaking – Fiscal Situation in 2009-10.
- Initiating Fiscal Consolidation: Sources of Adjustment.
- Fiscal Adjustment and Infrastructure Spending.
- Major Tax Reform Initiatives: Roadmap to GST?
- Concluding Remarks.

## Finance Minister's Dilemmas

- ❑ Keeping the stimulus while making fiscal consolidation: How much fiscal consolidation is appropriate?
- ❑ Need for greater allocation to social sector, infrastructure and devolution to States (4.8 to 5% of GDP) while compressing fiscal and revenue deficits.
- ❑ Need to increase taxes and administered prices – but they may add to inflation
- ❑ Prepare the ground for Direct Taxes Code and Goods and Services Tax while dealing with the clamour for selective tax exemptions and preferences.

# Fiscal Situation in India – A Stocktaking

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- Fiscal deficit retained as a per cent of GDP in RE; Partly due to GDP revision; In absolute terms, the deficit increased by Rs. 13000 crore.
- Revenue deficit however increased by Rs. 46226 crore or by 0.7 percentage points to GDP (4.6 to 5.3).
- This is due to:
  - Non-realization of spectrum : Rs. 32000 crore;
  - Shortfall in tax revenue : Rs. 9000 crore.
  - Increase in non-plan expenditure : Rs. 23110 crore
  - (Subsidies on food and fertilizers) : Rs. 19747 crore
  - Reduction in capital Expenditure : Rs. 8414 crore.
  - Disinvestment money : Rs. 24838 crore.

## The Nature of Fiscal Correction

- Marginal Stimulus withdrawal: Total expenditure increase – 8.5%. Rev. Exp – 5.8%. Total Tax increase- 17.9%; Additional revenue mobilized: Rs. 20500 crore (0.3% of GDP).
- Fiscal deficit reduced from 6.7% to 5.5% of GDP; Rev. def. from 5.3% to 4.0%.
- Roadmap for fiscal consolidation: 4.8% and 4.1% in the next two years.
- Sources of adjustment:
  - Pay and pension arrears : Rs. 20000 crore.
  - Loan waiver : Rs. 15000 crore.
  - Spectrum 3G Auction : Rs. 35000 crore.
  - Additional Disinvestment : Rs. 15000 crore
- Partial withdrawal of stimulus from pay revision: Pay and Allowances as a ratio of GDP increased from 0.9% in 2007-08 to 1.6 % in 2009-10 and is budgeted at 1.3% in 2010-11.
- Are the targets realistic? No provision for oil subsidies. Very low provision for fertilizer and food subsidies.
- Fertilizer subsidy – Will it deliver? Nutrient based subsidy without dismantling administered price mechanism is meaningless.



## Budget Analysis (Per Cent of GDP)

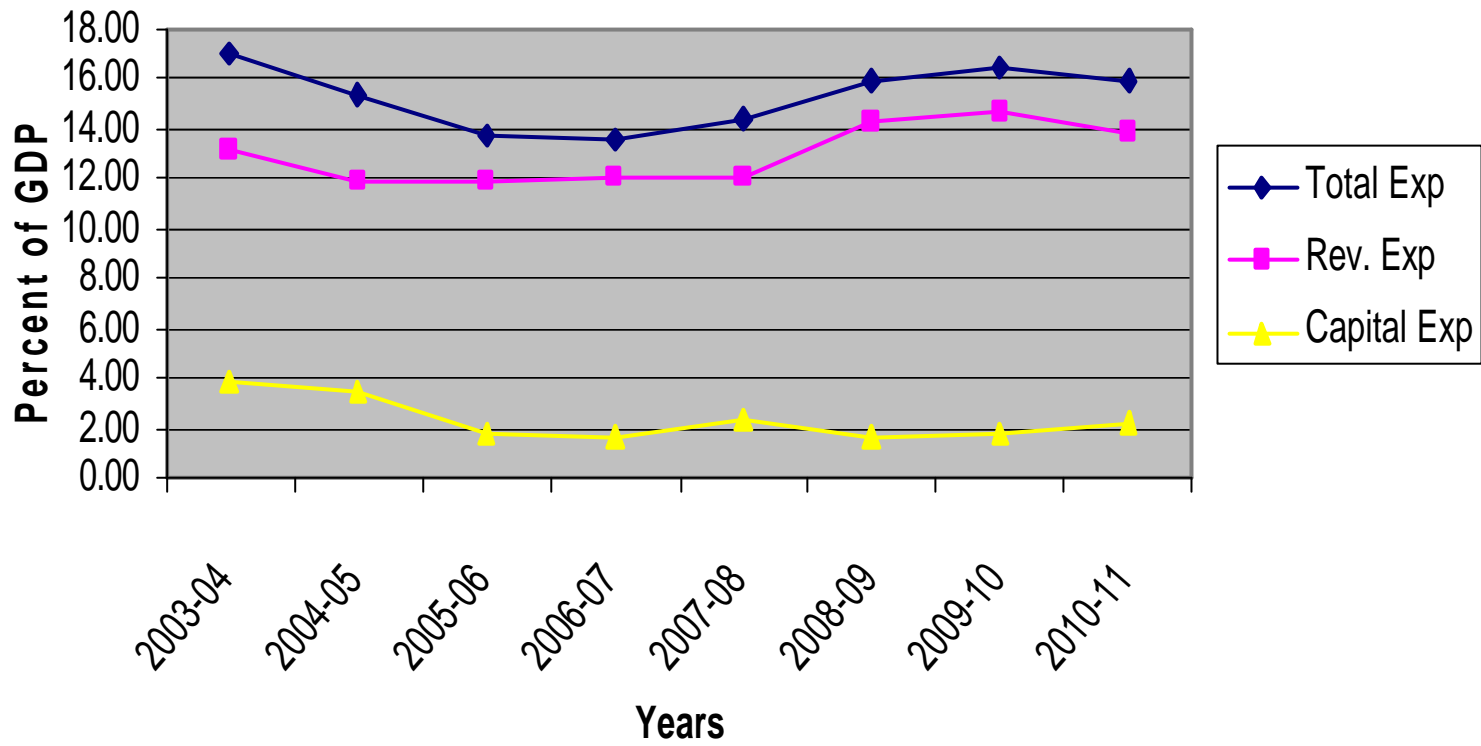
	2007-08	2008-09	2009-10 BE	2009-10 RE	2010-11 BE
Fiscal Deficit	2.56	5.86	6.05	6.70	5.50
Primary Deficit	-0.89	2.40	2.60	3.15	1.91
Revenue Deficit	1.06	4.33	4.55	5.32	3.99
Gross Tax Revenue	11.99	11.26	10.86	10.24	10.77
Net Tax Revenue	8.88	8.36	7.95	7.53	7.70
Non-tax Revenue	2.07	1.73	1.74	1.82	2.14
Total Revenue (Net)	10.95	10.08	9.69	9.34	9.84
Revenue Expenditure	12.01	14.41	14.24	14.67	13.83
Plan	3.51	4.34	4.21	4.28	4.54
Non-Plan	8.51	10.08	10.03	10.39	9.28
Capital Expenditure	2.39	1.75	1.62	1.86	2.16
Plan	4.14	5.08	4.94	5.10	5.38
Non-Plan	1.75	1.01	0.89	1.04	1.33

# Fiscal Adjustment and Infrastructure Spending

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- The Budget 2010-11 proposes to increase spending on infrastructure.
- Capital Expenditure is Budgeted to increase, marginally as a ratio of GDP. The fiscal adjustment since 2003-04 entailed sharp reduction in capital expenditures from 4 per cent of GDP in 2003-04 to 1.6 in 2008-09 before increasing to 1.9 per cent in 2009-10 and budgeted at 2.2 per cent in 2010-11.
- Central plan outlay to increase by 23.2% . Much of the increase in plan expenditure for various schemes. Budget Support to plan to increase by 22.5% and Internal and Extra-budgetary Resources of Public Enterprises (IEBR) to increase by 24%.
- The IEBR in seven infrastructure sectors (coal, mines, power, highways, shipping, urban development and railways) 69.3 per cent. Budget support to these sectors to decline from 36% in 2009-10 to 30.7 per cent in 2010-11.

### Trends in Revenue and Capital Expenditures



# Tax Reforms

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- DTC and GST in April 2011.
- Increase in Cenvat rate to 10 per cent to facilitate GST.
- Budget missed an opportunity to take transitional steps towards GST:
  - Service tax continues to be selective. But some services added.
  - No attempt to converge the rates of central excise, convert specific duties into ad valorem and simplify the tax system (Why should cement continue to be taxed in specific form and not ad valorem?). There are several tax rates (2, 4, 8, 12, 24, 37.5, 42). There are 283 exemptions. Small scale industry exemption could have been done away with. Sunset clause for area based exemption needs to be applied.

# Tax Reforms

- Policy perspective lacking in tax changes. Excise duty increased on large cars, multi utility vehicles, cigarettes, tobacco, air-conditioners, gold and silver.
- Micro changes in the excise and customs continues.
  - LED lights – reduction in central excise from 8 to 4%.
  - Specified exemptions, concessional rates for infrastructure, medical sector and infotainment.
  - Exemption from customs for specified inputs used in sports goods, toy balloons, reduction in customs duty on magnetrons to 5 %.
  - Customs duty reduction on long pepper, asafoetida.
  - Reduction in central excise on replaceable kits for household water filters, corrugated boxes etc., latex rubber from 8 to 4%.
- End-use exemptions are bad in principle; the budget proposes to extend them.
  - (i) Concessional import Mechanized handling systems and pallet racking systems in ‘mandis’.
  - (ii) Project status at concessional import duty (5%) and exemption from service tax for preservation and storage of agricultural products.
  - (iii) Extension of 5% duty on agricultural machinery for use in the plantation sector for one year.
  - (iv) Service tax exemption for transportation of cereals and pulses by road and railways.
  - (v) Concessional duty for equipment for solar and wind energy.

# Concluding Remarks

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- ❑ Broad thrust of the budget is on expected lines.
  - ❑ Compression of revenue and Fiscal deficit will provide borrowing space to the private sector.
  - ❑ Low infrastructure investment is a matter of concern. Maintaining high growth rate of the economy depends increasing the volume and productivity of infrastructure investment.
  - ❑ The budget missed an opportunity to advance reform towards GST in a meaningful manner.
  - ❑ Micro tax proposals need to be avoided to provide stability in the policy regime.