Bucks for the banks

The Union Budget is hoping to spur the economy by revitalising the financial sector

The maiden budget of Nirmala Sitharaman has many interesting features, but it does not have a defining central theme. There were expectations of a big growth push through either tax cuts or large expenditure programmes even if it meant a rise in the fiscal deficit. But the Finance Minister has chosen to be fiscally conservative, opting to play the long-term game, though it could lead to pain in the short term. The only indulgence she has permitted herself is a big ₹70,000 crore capital infusion in banks that will, it is hoped, spur lending to growth sectors in the economy. Also, quite notably, the budget has sought to address the problems that have plagued the non-banking finance companies space over the last few months and the consequent credit freeze and loss of confidence in the market. Ms. Sitharaman has comprehensively addressed the important issues of liquidity, solvency and poor governance in the NBFC sector. She has made available a liquidity window of ₹1 lakh crore to public sector banks through the Reserve Bank of India to buy pooled assets of NBFCs and offered a one-time credit guarantee for first loss of up to 10%. To enable better supervision of the sector, housing finance companies, which have been the main villains of the piece, will come under the RBI's regulatory ambit. A long-standing demand of NBFCs for equitable treatment with banks in the matter of taxing interest receivable on bad loans has been conceded. They will not need to maintain a Debenture Redemption Reserve on public placements that was leading to locking-up of funds, which is their raw material for business. These are important reform measures for NBFCs. More interesting is the move towards reviving development financial institutions. The big problem faced by NBFC financing infrastructure is the lack of long-term funding sources to match their lending tenure. This pushed them into borrowing short-term funds to lend to long-term projects, leading to asset-liability mismatches. The proposal to set up a committee to study the issue, including the experience with development finance institutions, is welcome.

There are several reform measures that have been announced, but the most interesting is the reiteration of the government's commitment to strategic disinvestment and the declaration that it is willing to allow its stake to fall below 51% in non-financial PSUs. Start-ups can heave a sigh of relief as the angel tax is practically off the table. The government seems to be moving towards a single identity card for citizens in the form of Aadhaar, which will now be interchangeable with the PAN card. Taxpayers who do not have a PAN card can file returns quoting their Aadhaar number, which effectively can be a substitute for PAN in all transactions. Another reform measure is the introduction of faceless e-assessment of tax returns taken up for scrutiny. This will eliminate the scope for rent-seeking by officers as there will be no interface between assessee and official. In fact, the assessee will not even know the identity of the officer scrutinising the return. This is an absolutely welcome measure but needs to be closely watched for implementation. The corporate sector has got a minor sop with the turnover limit for the 25% tax bracket being raised to ₹400 crore per annum from ₹250 crore. The expectation was that this would be extended to all companies irrespective of size. It appears that the government wants to wait for the finalisation of the Direct Taxes Code, which is being examined by a committee. Real estate companies may have reason to cheer as the generous tax concession for affordable housing may create demand, especially in the smaller metros.

The 'nudge theory' of economist Richard Thaler, mentioned extensively in the Economic Survey 2018-19 presented in Parliament on Thursday, has been put to use by the Finance Minister to push forward two of this government's pet themes – increasing digitalisation of money and promoting electric mobility. On the first, there will now be a 2% tax deducted at source when withdrawals from bank accounts exceed ₹1 crore in a year. This is a commendable measure, but it could lead to genuine problems for businesses such as construction and real estate that are forced to deal in cash for wage payments. Of course, the TDS can be set off against their overall tax liability. The second, and more interesting 'nudge', is towards electric vehicles where those taking loans to buy one will get a tax deduction of up to ₹1.5 lakh on the interest paid by them. But the fact is that there are not too many electric vehicles in the market now. And even for those that are there, the waiting period to deliver one is long. Besides, there is no ecosystem, such as charging points, even in the major cities. The government's hope seems to be that this incentive will create a market for e-vehicles that will then lead to the development of the ecosystem.

The budget documents show that the government has stuck to the glide path for fiscal deficit, which will be at 3.3% this fiscal. This is, however, based on exaggerated growth projections in tax revenues. The estimated total revenue receipts this fiscal is ₹19.62 lakh crore, which implies a 25.56% growth compared to the actual receipts of ₹15.63 lakh crore (as presented in the Economic Survey) in 2018-19. This is an extremely ambitious projection, especially given the ongoing slowdown in the economy. Of course, the Finance Minister could get a comfortable buffer if the Bimal Jalan committee that is going into the sharing of RBI's reserves with the government comes up with favourable recommendations. The government also appears to be sliding into a protectionist mode, going by the increase in customs duty on everything from cashew kernels to PVC, newsprint and even auto parts. While some of it may be well-intentioned to promote domestic manufacturing, this sends out a retrograde signal on the reforms front.

Falling far short of the goal

The rhetoric in the Budget of accelerated, inclusive and sustainable development receives only limited financial backing

C.P. CHANDRASEKHAR

R.V. MOORTHY

The general election is over and a new government has been formed. But the campaign does not seem to end. More than an hour of Finance Minister Nirmala Sitharaman's maiden Budget speech was largely devoted to underlining what she claimed were the remarkable economic achievements of the previous government. Given that legacy, she presented her role as one of expanding and strengthening the many achievements of Prime Minister Narendra Modi's first government. To underline that, she flagged the 10 points earlier presented as a vision for the decade in the interim Budget speech.

This raises two questions. First, how far has Ms. Sitharaman gone in actually extending and strengthening the initiatives that make it possible to realise the goals deriving from that vision? And, second, how does she intend to finance that effort to build on and take forward a legacy she claimed has laid out the agenda?

Ambition is not lacking. India, which was an approximately $1.85 trillion economy when the previous government took over (2014), and has grown to become a $2.7 trillion economy today will, the Prime Minister promises, grow to be a $5 trillion economy by 2024. Allowing for an inflation rate of 5%, that requires a real growth rate of 8% or more per annum. If GDP has to grow at that rate, investment must rise sharply. The Budget is clear on the government's role in this process. It cannot invest too much, but it must ensure huge investments in infrastructure and elsewhere by attracting and incentivising private investors. Optimistically leaving this to the private sector, the government focusses on taking the benefits of growth to the rural areas, the Micro, Small and Medium Enterprises and the marginalised.

A shortfall

However, one striking feature of the figures that make up the Budget is that the allocations to match this ambition are significantly short of requirement. Going by the nominal GDP figures implicit in the fiscal deficit ratios provided, total expenditure of the Central government which rose from 12.7% of GDP in 2017-18 to 13.2% of GDP in 2018-19, would remain at 13.1% of GDP in 2019-20. Spending to "kick-start" growth is absent.

Math for welfare programmes

This is true of allocations for the government's social welfare schemes as well. If we take the six major schemes labelled "core of the core schemes" (including the National Social Assistance Programme and the Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA), nominal allocations, which amounted to ₹84,361 crore in 2018-19 as per the revised estimates are projected to fall to ₹81,863 crore in 2019-20. Allow for inflation and that 3% fall would imply a significant real cut. In the case of the MGNREGA, the budgetary allocation for 2019-20 at ₹60,000 crore is lower than even the inadequate ₹61,084 crore spent in 2018-19. Elsewhere, in the case of some flagship schemes extolled in the Budget speech, budgetary allocations for the Pradhan Mantri Gram Sadak Yojana is the same in 2019-20 as it was in 2018-19 and that for the Pradhan Mantri Awas Yojana are lower for 2018-19 than it was in the Budget for the previous year. It is principally the farmer income support scheme of ₹6,000 per identified household that receives a significantly large and enhanced allocation of ₹75,000 crore. But even this has to an extent been financed by cutting allocations for other schemes. In effect, the rhetoric of accelerated, inclusive and sustainable development receives only limited financial backing.

The difficulty is that to finance even this curtailed thrust, the Finance Minister is hard put to find the resources, especially because the government wants to show it is committed to fiscal deficit reduction, with the deficit projected at 3.3% in 2019-20. It does make one effort at squeezing surpluses out of the system with increased taxes on the super-rich. Surcharges on those with taxable incomes in the ₹2-5 crore and above ₹5 crore ranges are to be increased so as to raise the effective tax rate applicable by 3 and 7 percentage points respectively.

Though in 2017-18 almost 99% of returns filed were of those with taxable incomes less than ₹2 crore, the tax makes a small difference, inasmuch as the 0.05% of returns filed that fell in the above ₹5 crore taxable income group accounted for close to 32% of taxable income declared. But this gain has been partly neutralised by reducing tax rates for corporations with a turnover in the ₹250 crore to ₹400 crore range from 30% to 25%. The government has also resorted to some regressive taxation. At a time when oil prices are on the rise because of American sanctions on Iran, the Finance Minister has decided to raise the duty on petrol and diesel by ₹1 per litre each.

Public sector sale

The other major source of non-debt receipts is disinvestment and privatisation which is to be accelerated. Strategic sales will continue and equity even in public sector enterprises where government shareholding has reached the 51% floor is to be sold. That is expected to yield ₹1,05,000 crore in 2019-20, compared with the ₹80,000 crore last year. But, as noted, all this has not been enough to deliver resources that match the ambition reflected in the rhetoric of the new government.

Which leads naturally to dependence on welfare hype and the strategy of hopelessly depending on private initiative to drive growth.

C.P. Chandrasekhar is Professor at the Centre for Economic Studies and Planning, Jawaharlal Nehru University, New Delhi

Choosing the long view

The Budget is part of the longer-term creation of a new India, and continues with the vision of the previous tenure

ASHIMA GOYAL

The first Budget of the new government in the 17th Lok Sabha powerfully recommits to the vision guiding the last term emphasising continuity, individual empowerment and infrastructure for nation building, fiscal consolidation, discipline, and process improvements. The rural sector comes in for special attention, but even there the focus is on value addition and transformation rather than income transfers as the means to double farmer incomes.

Jarring note

But in choosing the long view, there is hardly any discussion of the current growth slowdown, and how the Budget can contribute to alleviating it. This is a pity, because this is expected of the major macroeconomic policy statement of the government. Markets are looking for a big spending boost from the government to revive growth. But there are many aspects of the Budget that will contribute to reviving growth but unfortunately they are not brought out explicitly. The Budget is presented as part of the longer-term creation of a new India.

The standard idea of macroeconomic stimulus is to announce a large increase in government spending without raising taxes. This raises deficits. There has been an active debate in the run-up to the Budget that given the slowdown some rise in deficits is acceptable in order to provide a boost to the economy. But the government is committed to a long-term macroeconomic framework and a path of deficit reduction. A deviation will hurt its credibility. As we see below, there are other ways of stimulating the economy. Moreover forward-looking agents know short-term indulgence comes at the expense of long-term pain. They are likely to become more confident and spend more with a government that is able to keep its word. India has had a long battle to escape from macroeconomic fragility and high inflation due to over spending and over stimulus by past governments.

Macroeconomic stimulus

The Budget gives many examples of this government's faster speed of delivery in infrastructure, such as road building or construction of low-income housing. Since the same government is back, it will be able to front-load expenditure on ready projects. The spending comes before taxes are raised and, therefore, is stimulatory. Apart from creating incomes it boosts demand for the cement and steel industries. Moreover, although the fiscal deficit ratio has come down from 3.4 in the interim Budget to 3.3, a larger share of resources are to be raised by privatisation. Since this does not reduce private demand as taxation does, there is a larger net expenditure stimulus which supports demand and growth. Completed schemes are being built upon, as some funds from Swachh Bharat are being reallocated to piped water and to obtaining energy from solid waste management. The substitution of LED bulbs under the Unnat Jyoti by Affordable LEDs for All (UJALA) Yojana for earlier energy guzzlers led to an estimated cost saving of ₹18,341 crore per year. Now solar stoves and battery chargers will be promoted.

Faster privatisation as well as monetisation of other assets such as brown field projects and government land banks will encourage private activity. The ₹70,000 crore to be pumped into public sector banks coming after the asset clean-up has started yielding results, together with a series of measures for non banking financial companies (NBFC) will help credit growth.

REUTERS

A climate of pessimism and fear was responsible for falling credit growth, which fed into a slowdown in private investment and consumption. The Government's role is to bolster confidence. As a confident state steps in, begins to spend, and turns around the financial sector, private spending will also revive. Private investment projects had started in end-2017 as some sectors were running into capacity constraints, and then dried up because of the NBFC credit slowdown and election-related political uncertainty. It should revive again, especially since interest rates are coming down. G-Secs rates have fallen after the Budget. Spreads for corporate bonds and NBFC funds should also come down. Many NBFCs continue to have viable business models. The fear of credit risk will fade as costs come down and activity revives. The moribund real estate market that is responsible for much destruction of asset value will get a fillip from tax exemptions and lower interest rates.

Help is promised for industry in many other ways. Land availability, labour law simplification, reduction in legal costs, delays and tax harassment. The focus on public-private partnerships and support for entrepreneurship will create many opportunities for industry. Private firms generally do much better in last mile delivery of public services. Cuts in corporate taxes, other sops and tweaks in tariffs are well-thought-out to attract foreign firms to produce at scale in India. This is the right time for such initiatives in the context of foreign direct investment re-locating from China.

One of the strengths of the last government was in process improvements. These continue in this Budget. A new initiative of faceless e-assessment with no human interface, and cases assigned in random manner will reduce tax payer harassment. Integrated information will be used to auto fill tax forms making compliance easier even as tax evasion becomes more difficult. There is more simplification in Goods and Services Tax and other taxes while information will be used more intensively to increase the tax base.

The improvement in processes reflects in better delivery of Budget promises, and the quality of fiscal consolidation. The revenue deficit has fallen as well as the fiscal deficit even as expenditure promises were largely kept, although much more was spent for agriculture. Capital expenditure was supported by market borrowing of public sector enterprises (PSEs) – as they become commercially viable, they must borrow based on future income streams. The growth slowdown would have been worse last year without this borrowing. PSEs do not suffer from credit risk. The food subsidy from the Food Corporation of India – which last year was supported by borrowing from small savings – is now brought back to the Budget as it should be.

Apart from reforms in budget processes there is support for larger reform processes. The emphasis on technology cannot deliver alone without improvement in governance. But there is evidence of complementary action on both. For example, a major handicap for small businesses is an absence of timely payments from government. A payment platform has been announced for cutting time and improving processes. Ministries dealing with water have been merged.

A major constraint India has been facing is the absence of long-term funding for infrastructure. There is evidence of innovative thinking on this with sops announced for alternate investment funds; thinking about setting up a development bank as well for making more foreign savings available. Retail investors are also to be encouraged to buy government securities. Stock exchanges are building platforms, which are to be supported by inter-operability between the Securities and Exchange Board of India and the Reserve Bank of India depositories. To the extent there are large diversified domestic investors in government securities the proposal to also raise funds abroad becomes less risky.

As these reforms improve the supply-side, cost and time delays reduce for business as well as for the average citizen.

Long-term framework

As argued above, some stimulus is possible without raising deficits. In the long run, however, the macroeconomic framework constraining the Budget needs to be revisited to allow policy to counter growth slowdowns and booms. The present framework gives very little space for this. The Fiscal Responsibility and Budget Management adjustment path should be in terms of a cyclically adjusted fiscal deficit, with incentives to protect the quality of expenditure. A target for revenue deficit is also required since it is easiest to cut public investment, which also hurts growth. The 15th Finance Commission should consider this reset.

Reducing the level of debt and interest payments is a desirable objective, since it would release much more government funds for productive expenditure. But growth raises tax revenues and a rise in GDP increases the denominator reducing deficit ratios. Therefore maintaining growth is one of the best ways to reduce debt and deficit ratios.

Ashima Goyal is on the Prime Minister's Economic Advisory Council

LETTERS TO THE EDITOR

Letters emailed to letters@thehindu.co.in must carry the full postal address and the full name or the name with initials.

Budget talk

Finance Minister Nirmala Sitharaman's maiden Budget, coming with an ambitious call for a $5 trillion economy, is a lacklustre exercise filled with slogans and devoid of solutions. It aims to create wealth without giving any scope for creating employment. There is no proposal to reduce the rich-poor gap and bring about more equitable distribution of resources. The call for Public-Private Partnership in Railways is a move to bring the sector into the fold of private entities in due course. A streamlining of labour laws will enthuse the investors but do nothing to satisfy the working class. A disinvestment target of ₹1,05,000 crore will hasten the extinction of Public Sector Undertakings, which are the people's asset. This is a budget for the rich and offers nothing to the common man

A.G. RAJMOHAN,
Anantapur, Andhra Pradesh

This year's Budget steered clear of awarding too many sops and instead focussed on the need of the hour for the common man. There was emphasis on construction of houses and electrification. Raising the tax threshold from ₹2.50 lakh to ₹5 lakh would be welcomed by a section of the salaried class. Giving incentives to start-ups is a step towards increasing employment. Further, relaxation in corporate tax slab will be welcomed by companies. There is considerable additional tax deduction available for home-buyers as well. To sum up, the Budget has given every sector a pie in the cake.

ASHOK JAYARAM,
Bengaluru

Investment slump

I am unable to share the Chief Economic Adviser's confidence that the slump in investment has "bottomed out" (Editorial, "Blue-sky visions," July 5). The banking system and its functioning is the weakest link here. Domestic savings, a vital source of investment, are channelled through banks. The framework under which they operate is anachronistic and not in line with the present-day requirements of the real economy, causing high level of Non-Performing Assets. Further, due to a steady deterioration in their operational profitability, a deep patron-client relationship with the government has developed and independent decision making by senior bankers has all but disappeared. Since their conceptual lending framework itself is flawed, which leads to wrong credit decisions being made and then a periodic monitoring of their functioning, bankers have developed a lot of expertise on how not to take decisions.

SUSHIL PRASAD,
Hyderabad

Rahul's resignation

The Congress Party can revamp its strength only through a democratic election of its leaders. The nomination system currently followed acts as a conduit for unpopular leaders to rise to top levels. Rahul Gandhi can give a concept note party workers providing them direction.

V.R. AJITH KUMAR,
Thiruvananthapuram

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CORRECTIONS & CLARIFICATIONS:

"U.S. lawmakers slam detention centres" (July 3, 2019, World page) refers to *Joaquin* Castro as the Democratic presidential hopeful from Texas. The correct name is *Julián* Castro.

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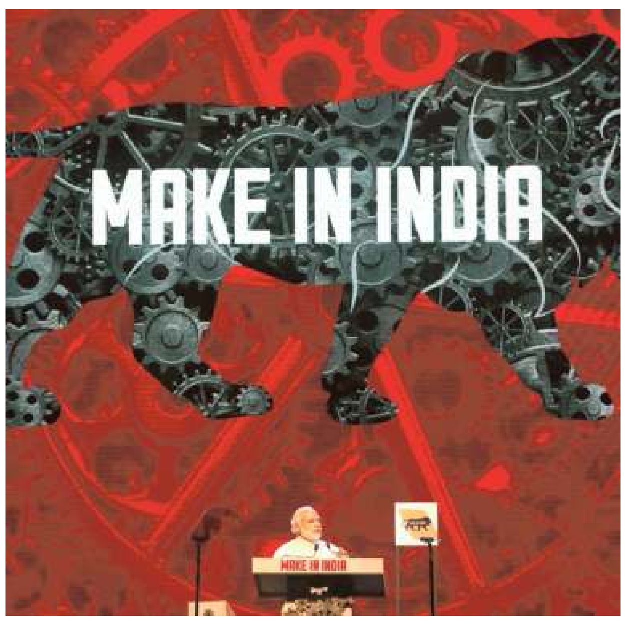
Searching for reform signals

While the Budget shows commitment to fiscal consolidation, there are very few measures that can steer the economy to acceleration

M. GOVINDA RAO

There were high expectations from the Budget to provide a clear road map for much-needed reforms, given that the government received an unprecedented electoral mandate. The GDP growth in the last quarter of 2018-19 was the slowest in the last five years, and considering that the capacity utilisation in manufacturing has already peaked, reviving the investment climate is critical to accelerate economic growth. The unemployment rate, which is 6.1%, is the highest in four decades. With the Economic Survey making a pitch for creating a virtuous cycle of saving and investment, there was hope that there would be far-reaching announcements in the Budget.



Balancing the books

To be fair, Finance Minister Nirmala Sitharaman has a difficult job of balancing the books, particularly when the revenues are not buoyant and demands for expenditure are high. From that perspective, it is noteworthy that she has tried to show her commitment to the process of fiscal consolidation by keeping the fiscal deficit budgeted at 3.3%. The difference between the 3.4% budgeted in the interim Budget and this is mainly due to higher GDP estimates (₹93,168 crore) used in the denominator. The revenue is lower by ₹55,463 crore compared to the interim Budget estimate but this is offset by non-tax revenue estimated to be higher by ₹40,532 crore. Thus, there are not many significant departures from the estimates of revenue and expenditure presented in the interim Budget. The gross income tax revenue is estimated to be lower than the interim Budget by ₹90,000 crore, mainly on account of lower GST (₹97,857 crore) and individual income tax (₹51,000 crore). Despite taking lower estimates, the revenue estimates look far too optimistic in comparison with the pre-actuals given by the Controller General of Accounts. To realise the Budget estimates, the increase over the actual tax collected in 2018-19 in gross tax revenue will have to be 21.2%, net tax revenue must rise by 25.3%, and the non-tax revenue will have to increase by 27.2%.

A major source of additional revenue projected in the Budget is by having an active disinvestment policy. Disinvestment is expected to generate ₹1,05,000 crore, which is almost ₹15,000 crore higher than what was taken in the interim Budget. The Budget speech also speaks about an active disinvestment policy beginning with Air India. Hopefully, the environment will help to implement this. Another source of revenue which is expected to increase is the dividend. This amounts to ₹1,63,528 crore, which is ₹21,457 crore more than what was estimated in the interim Budget. Much of this will be from the Reserve Bank of India (RBI).

The most important reform measure in the Budget is the proposal to streamline multiple labour laws into a set of four labour codes. Although the details are not yet available, it is hoped that the government will embark on the much-needed reforms in this area. This is a contentious issue that has been long debated. The Economic Survey too has referred to the need to make the factor markets less distorting and the disincentives these laws create in ensuring optimal sizes. Hopefully, the government will address this in the interest of increasing employment and exports of labour-intensive goods.

The reform front

On the reform front, while much was expected, the Budget has been clearly disappointing. There are very few measures that can steer the economy to acceleration, leave alone changing gear to achieve the aspirational goal of achieving 8% growth to reach a $5 trillion economy by 2024. On the contrary, some of the measures take us back to the pre-reform era. Over the last three years, there has been a steady increase in import tariff in the name of ‘Make in India’, and with the U.S. coming hard on India by terminating India’s designation as a beneficiary developing nation under the key Generalised System of Preferences programme, it was hoped that there would be an attempt at lowering and reducing the expansion of the protectionist wall. The objective of ‘Make in India’ should be to make the economy competitive and not to dish out higher cost, inferior products to domestic consumers. By selective increases in customs duty and by varying the rates based on whether the item is an intermediate good, capital good and final consumer good, the Budget has caused the effective rate of protection on many items to be much higher than the nominal rates. This can create unintended distortions. This is clearly retrograde.

The Budget allocates ₹70,000 crore for the recapitalisation of public sector banks, but is silent on structural reforms including governance reforms.

One of the major initiatives needed at the present juncture is to reform the banking system. The Budget allocates ₹70,000 crore for the recapitalisation of public sector banks, but is silent on the urgently needed structural reforms including governance reforms. Nor are there any concrete measures to deal with the Non-Banking Financial Companies crisis apart from empowering the RBI to undertake the regulatory function. Not that everything has to be done in the Budget, but events have shown that there is a need to improve both the legal framework and governance system. Consolidation of public sector banks cannot serve the purpose of changing the structure of incentives and accountability.

Revive the investment climate

The revival of the economy requires the revival of the investment climate. A recent OECD study has shown that corporate taxes in India are very high amounting to almost 48% when the dividend distribution tax and surcharges are taken account of. The Budget in 2015-16 promised to bring the basic rate down to 25%. This was implemented for companies with a ₹250 crore turnover in the 2018 Budget; the present Budget increases it to ₹400 crore. Although these companies cover 90% of the number of companies, their tax payment is less than 10-15%. If large investments have to be attracted, then the reduction should have been general and the scaffolding approach can only disincentivise the companies to grow bigger and better. This only discourages the companies from becoming larger. While the Economic Survey is eloquent about the need to transform the ‘dwarfs into giants’, the various measures taken in the Budget to incentivise the MSMEs amount to reiterating that ‘small is beautiful’.

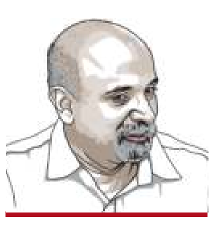
Cooperative federalism

The Finance Minister speaks about the rejuvenated Centre-State dynamic and commitment to cooperative federalism shown by the government during the last five years. At the same time, most of the measures taken to raise additional revenues are by way of cesses and surcharges. The increase in income tax for people with more than ₹2 crore and ₹5 crore is by way of additional surcharge. Similar is the case with additional tax on petrol and diesel. This is clearly to exclude the additional revenue raised from the divisible pool and deny the share of the tax to the States. Hopefully, the Finance Commission which is deliberating on the devolution will take note of the issue. On any case, such measures do not promote cooperative federalism.

M. Govinda Rao is Member, Fourteenth Finance Commission, and former Director, NIPFP. Views are personal

A Budget that goes nowhere

It would seem that since the government is unable to catalyse domestic investment or fund public investment, it is now turning abroad to fuel growth



C. RAMMANOHAR REDDY

Union Finance Minister Nirmala Sitharaman is mistaken if she thinks her first Budget is going to revive a slowing economy.

The economy grew by just 5.8% in real terms in the last quarter of 2018-19. Yet, the Union Budget for 2019-20 assumes that the economy will grow this year by 12% in nominal terms, or by 7-8% in real terms. How can that dramatic a turnaround take place? Only if there is a sharp pick-up in investment – private and/or public.

There is little in the Budget that is likely to boost domestic private investment. There are neither any incentives for private investment nor support for public investment. To make matters worse, the Budget has actually projected a decline in central government capital expenditure (public investment) in 2019-20 by 6% in nominal terms. This is perhaps the first ever decline in public investment in the past half century, which, once adjusted for inflation, could measure over 10%. It is no wonder that the Finance Minister, shedding the convention of decades, did not mention any allocations for schemes in her speech and pushed all the numbers to the fine print.

Same direction as before

It would seem that since the government is unable to catalyse domestic investment or fund public investment, it is now turning abroad to fuel growth. Some of the norms for foreign institutional investment (FII) are to be liberalised, so too for foreign portfolio investment (FPI) and ceilings on foreign direct investment (FDI) are to be raised in some sectors. More ominously, the government has now decided to go in for external commercial borrowings to meet part of its borrowing requirements, claiming that India’s external debt to GDP ratio is very small. This is very much like what the governments of the 1980s did, which eventually led to the balance of payments crisis of the early 1990s. Why are we again heading in that direction?

Prime Minister Narendra Modi’s slogan of a $5 trillion economy by 2024-25 has taken over the discourse on the economy. The Economic Survey gave it considerable importance and now the Union Budget has too. We have forgotten that a larger economy does not necessarily translate into improved well being for all. A larger economy is of value only if in the process it delivers more jobs and better services. It is significant that the word “jobs” found no mention in the Finance Minister’s speech.

The approach of the Narendra Modi government in its second term seems much like in the first – focus on a select group of welfare schemes like Ujjwala Yojana, Swachh Bharat, Sowbhagya and Jan Dhan (all of which are believed to have served it well in the 2019 elections) and now Jal Shakti, while leaving it to private investment or private consumption to deliver economic growth.

If private investment does not deliver, then the assumption is that private consumption will. Indeed, consumption with the help of household debt has been driving growth in recent years. The dangers of consumption loaded by private debt are obvious.

Numbers from interim Budget

Since the numbers in the Budget papers have steadily lost their integrity, it seems pointless to examine them in much detail. Last month, the Controller General of Accounts had made public the provisional numbers for 2018-19. These showed that central tax revenues were lower than the revised (yes, revised and not Budget) estimates by as much as ₹1.67 trillion. In order to hold down the fiscal deficit, the government cut its expenditure by ₹1.33 trillion. Though these updated figures are available (with the Finance Secretary himself saying in the post Budget press conference that the actuals for 2018-19 are now with the government), why on earth do the Budget papers reproduce the numbers from the interim Budget of February 2019? Obviously because presenting the final numbers for 2018-19 now would have shown the Modi government in a poor light: unable to fulfil its promises on tax collection and spending commitments in its last year of its first five-year term.

To be fair to the Finance Minister, the revenue projections, especially in income tax, are more modest and therefore perhaps more realistic than that of her predecessor. They are modest enough to project a decline in gross tax receipts from 11.9% of GDP (2018-19) to 11.7% of GDP (2019-20), arising from a slump in both direct and indirect taxes. It is interesting that the last time there was a fall in tax revenue was in 2014-15, the first year of the first Modi government.

A larger economy is of value only if in the process it delivers more jobs and better services. It is significant that the word “jobs” found no mention in the Budget speech.

How then is the government planning to marginally lower its fiscal deficit in 2019-20 to 3.3% of GDP (assuming that this is indeed a reliable estimate)? It turns out a boost in non-tax revenue will make the difference. The biggest jump is of dividends from the Reserve Bank of India and the nationalised banks: ₹1.06 trillion, a 43% jump over 2018-19. Since few public sector banks are making money, most of this must be expected from the RBI. These dividends have more than doubled from 2017-18. We now know why the government-RBI tussle was so bitter last year.

Cooperative federalism?

True to form, the government swears by cooperative federalism in words but does actually the opposite in practice. A major source of revenue mobilisation is to come from a higher cess and special additional excise duty on petrol/diesel. That is good for the Centre because cesses are not to be shared with the States!

With the year ahead already threatening to be a difficult one because of a monsoon that increasingly looks likely to be less than normal, we have to buckle up. We will not get any support from the second Modi government’s first Budget.

A feel good spirit from an impressive electoral victory and slogans about a $5 trillion economy are by themselves not going to give any buoyancy to the economy.

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The macro does not gel with the micro

The Budget describes with admirable practicality what we would like to see in India, but it is not convincing on how we can have the growth to afford the same

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The maiden Budget presented by Finance Minister Nirmala Sitharaman was much looked forward to partly because she is the first woman to hold this post full time, an achievement for our democracy.

Attention to detail

Though her speech was perhaps a little combative, as she kept asserting the achievements of the first Narendra Modi government, it was nevertheless marked by an even-handedness and attention to detail that is rare. The first was seen in the methodical way in which she ranged over the areas – manufacturing, Gramin India, Shahari India, women, and the youth. One of the many instances in which the second was evident is in the elaboration of the proposed elimination of human interface in the conduct of scrutiny for taxpayers.

However, there was a disconnect in the speech. At the outset, Ms. Sitharaman appeared to assert that India is headed towards becoming a $5 trillion economy by 2024. However, much of the rest of her speech was concerned with what this economy would look like – there would be widely dispersed social and physical infrastructure; a low-carbon footprint; and housing for all, among other desirable things. We were not told how the country will get there. And getting there is important, for the things that have been promised need to be paid for and there has to be the income for this.

Improving ease of living

If only five points in the Budget are to be highlighted, I would choose bank capitalisation; rural electrification to be completed by 2022; a final push for water and sanitation, making India open defecation free by October 2 this year; encouraging solar power usage; and tax-related changes. Of these, electrification, water and solar power may not require large outlays but they make a big difference to people’s lives, a reality ably grasped by the Bharatiya Janata Party (BJP), which portrays its actions in these areas as aimed at improving ‘the ease of living’.

The infusion of ₹70,000 crore into public sector banks would be a significant contribution to easing the liquidity situation caused by non-performing assets. It is mentioned that this will be accompanied by governance reforms, though we do not know as yet what form they will take, which alone will determine how significant they will be.

There is no mention in the Budget of public investment, stepping up of which would be essential even to stimulate private investment right now.

The package for the financial sector also includes a time-bound public guarantee to commercial banks that acquire assets of the presently troubled Non-Banking Financial Companies (NBFCs). This should bring some stability to the NBFC sector, instability in which would ruin the lives of hundreds of investors and choke lines of credit outside the banking sector.

In case it is found that the capital infusion is inadequate, the government can always increase it later in the financial year, but to have intervened at this stage of liquidity shortage is statesmanly. The proposals on taxation include changes in both tax liability and administration. The exemption limit on the income tax has been raised but the surcharge has now been increased on those in the highest two tax brackets. There is a balancing act here. Similarly, the upper limit for eligibility for the lowest slab of the corporate tax has been raised from ₹250 crore to ₹400 crore.

This in in line with the demands of India’s corporate sector but it may not be what is best for the economy at a time when the government needs as much revenue as it can garner to quicken it.

New era of tax administration

However, the Budget may have initiated a new era with respect to the tax administration. Compliance is to be made easier for the taxpayer. There are to be pre-filled tax returns and less human interaction in the event of tax scrutiny. There will be ‘faceless assessment’ through the use of an electronic mode. Face-to-face encounters between inspectors and the assesses will be eliminated, with notices sent from a central Income Tax cell. Some similar simplification is to be done in the sphere of the Goods and Services Tax too. The Minister is right to speak of all this as a “paradigm shift” in the functioning of the tax department.

While it is surprising that she equated the ease of paying taxes with the ease of living in India, which must take far more into account, it is the case that individuals have experienced powerlessness when dealing with the tax department.

Where the Budget fails

This Budget’s failing is in not setting out the means by which the government is to take the economy to the aspirational $5 trillion level. Barring unforeseen productivity surges, we must assume that investment holds the key. At least the Economic Survey tabled earlier spoke of the importance of investment, even though it somewhat ideologically confined validity to private investment.

The Budget has nothing to say on the matter. Perhaps it is believed that the very return of this government is sufficient to release the ‘animal spirits’ of private investors. However, this would amount to overlooking the history since 2014. In this period, though there has been macroeconomic stability and much attention has been paid to the ease of doing business, private investment has declined. This points to the limits to confining yourself to the supply side when you are interested in growth, which this government is doing.

Moving to a $5 trillion economy by 2024 would require growing at a rate faster than the average that has been achieved since 2014. There is no mention in the Budget of public investment, stepping up of which would be essential even to stimulate private investment right now. Capital expenditure has been raised by much less than the actual increase in the past year.

One way of seeing this Budget is that it is something good in parts. It describes with admirable practicality what we would like to see in India, from water connections to roads. But it is not convincing on how we can have the growth to afford them. We might say then that the macroeconomics does not gel with the microeconomics.

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