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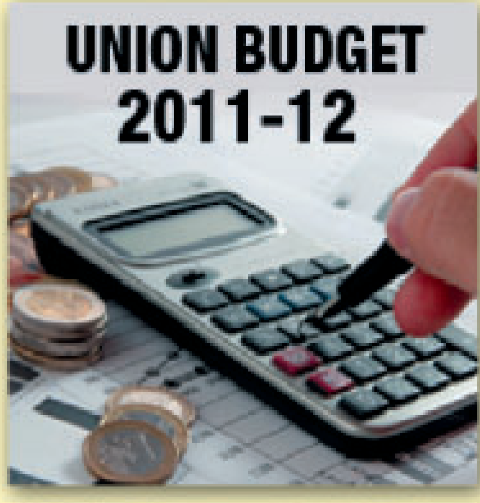

March 2011

Theme 232

UNION BUDGET 2011-12 - Growth with Fiscal Correction

A monthly publication from South Indian Bank

19th Year of Publication

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The South Indian Bank Ltd., H.O. : 'S.I.B. House', Thrissur, Kerala

SIB STUDENTS' ECONOMIC FORUM

MARCH 2011

THEME 232: UNION BUDGET 2011-12–GROWTH WITH FISCAL CORRECTION

The budget presentation is an annual exercise of projecting revenues and expenditures of the government for the ensuing year. Raising and expending resources should match with various economic objectives and priorities. This is also an occasion to make announcements or provide indications on major policy reforms on taxes, economic growth, and development schemes. In developing economies, the general expectation is that the budget should address major macroeconomic issues and also propose measures to tackle them.

Explain the economic context in which the budget is presented?

There are often conflicting macroeconomic objectives to be pursued with a balanced trade-off. Economic growth and price stability are two ideal objectives of economic policy, but these are often difficult to achieve simultaneously. India recorded a positive but subdued economic growth during the period of global economic crisis. The growth momentum slowly picked up, and it has reached slowly the pre-crisis growth trajectory. But, the benefits of high growth rate are slowly getting dissipated by inflationary tendencies which first started from the food basket and then became broad-based to cover manufactured goods. The persistent inflation will create social tensions. Thus tackling inflation without impairing economic growth is very significant. The budget expects economy to grow at 9 percent and average inflation level to be lower in 2011-12. The fiscal deficit and current account deficit (CAD) will be brought to lower levels. At a time when social and financial inclusion is given emphasis, government expenditure is likely to go up; but this will conflict with the objective of fiscal consolidation. Economic stimulus packages have caused increase in purchasing power of the people and thus demand pull inflation. The fiscal deficit has to be brought under control as a means of taming inflation.

What are the major expenditure and revenue estimates of the budget 2010-11?

The total expenditure proposed in the budget estimates is Rs.12, 57,729 crore, an increase of 13.43 percent over last year. The Plan and non-Plan expenditures estimated at Rs.4, 41,547 crore and Rs.8, 16,182 crore respectively record an increase of 18.3 percent in Plan expenditure and 10.9 percent in non-Plan expenditure over the previous year. Total receipts by way of taxes, non-taxes, recoveries of loans and disinvestment amount to Rs, 8,44,912 crore. The fiscal deficit, the difference between total expenditures and total receipts, works out to be Rs.4, 12,817 crore, which is 4.6 percent of the gross domestic product. Taking into account the various other financing items for fiscal deficit, the actual net market borrowing of the government in 2011-12 would be of the order of Rs.3,43,000 crore.

What are the measures proposed in the budget to control inflationary pressures?

A coordinated monetary and fiscal action is required to tackle a persistent inflation. The RBI has already taken monetary measures such as increase in reserve ratios – CRR, SLR - and increase in policy interest rates – repo rate, reverse repo rate. Now the government has to reciprocate to remove supply bottlenecks and improve agricultural production. In an attempt to address the structural nature of inflation, the major focus for 2011-12 will be to remove production and distribution bottlenecks for items like fruits and vegetables, milk, meat, poultry and fish, which has kept inflation as high as 9.4 percent. In India, 40 percent of total food produce is wasted due to lack of adequate infrastructure such as warehouses, cold storage and transportation. Thus, measures to build infrastructure for the agriculture sector by approving 15 Mega Food Parks, 24 new cold storage facilities and to increase storage capacity by 40 lakh tones are announced in the budget.

What is the roadmap for further fiscal consolidation in 2011-12?

The fiscal deficit for the coming fiscal year is projected at 4.6 percent of GDP. Apparently, the extent of fiscal correction envisaged is modest. The fiscal deficit has improved to 5.10 percent of GDP in 2010-11 from 6.40 percent of GDP in 2009-10. But the actual fiscal correction required to be undertaken in 2011-12 is substantial. This is because the government benefitted considerably from the one-time inflow of more than Rs. 100,000 crore from the telecom auctions in 2010-11.

In 2011-12, tax revenues are estimated to grow by 18 percent on the expectation that real economic growth would be as high as 9 percent. The indirect taxes by way of customs duty, excise collections and service tax collections are estimated to expand by 15, 19, and 18 percentages respectively. The coverage of service tax, with the rate remaining at 10 percent, has been increased. It is estimated that income tax collections would expand by 15 percent, despite increase in exemption limit for tax payers. The corporate taxes are expected to increase by 21 percent in 2011-12.

The revenue expenditure is budgeted to increase by 4 percent owing to lower allocation to debt waiver for farmers and to major subsidies in fuel, food and fertilizers. However, capital expenditure is expected to increase by 24 percent. But, confining subsidies within budget estimates will be a difficult proposition.

What are the reforms proposed in the taxation front?

The government has reiterated commitment to implement Direct Taxes Code (DTC) by April 1, 2012. It is also assured that Constitution Amendment Bill would be introduced for facilitating implementation of Goods and Services Tax (GST) legislation. In the personal taxation, exemption limit has been increased for individuals and senior citizens. The central excise duty will be maintained at a standard rate of 10 percent. The broad themes of indirect taxes relate to revenue augmentation, widening the tax base, alignment to GST principles and simplifying compliance. The service tax net has been widened and alignment with VAT has been done. It is proposed to introduce a negative list of services exempt from tax.

How is it proposed to strengthen financial inclusion initiatives?

It is stated that National Food Security Bill will be introduced in the course of this year. This will be a landmark legislation akin to rural employment guarantee act. These schemes will definitely help improve standard of living in the rural areas. Total budget allocation to the social sector has been increased by 17 percent over the last year figure. This amounts to 36 percent of the total plan allocation. Increased allocation to Bharat Nirman programme, plan to provide rural broadband connectivity to all 2,50,000 panchayats in the country in three years, and indexing wage rates under MGNREGA to the Consumer Price Index for Agricultural Labour are measures to promote inclusive growth. Also, the target for farm credit has been increased from Rs. 375,000 crore in the previous year to Rs. 475,000 crore in the coming year.

Infrastructure is the key to economic growth. How is it underlined in the budget?

Investment in infrastructure has been given major focus in the budget. An allocation of Rs. 214,000 crore is provided and this amounts to 48.5 percent of the total plan expenditure. Other measures include increase in FII limits for investment in corporate bonds and provision of tax free status to infrastructure bonds issued by government undertakings for development of ports, railways and highways. Overseas borrowing for infrastructure will attract only 5 percent withholding tax rate instead of the 20 percent in other cases. The private infrastructure firms will be given incentives to invest in urban transport and low cost housing.

What are the implications of the budget on the financial and banking sector?

It is announced that FDI policy will be further liberalized to attract foreign investment. SEBI registered mutual funds are allowed to accept subscription from foreign investors for equity schemes. Amendments are proposed in the Banking Regulation Act in the context of new banking licenses to private sector players. Final guidelines on new banking licenses will be issued by the RBI in this year. Public sector banks and Regional Rural Banks will be recapitalized to improve capital ratio. It is envisaged to put in place appropriate regulatory framework to protect the interests of small borrowers in microfinance lending. More resources will be provided to SIDBI to refinance incremental lending by banks to MSME enterprises. Interest subvention to farm credit and to housing loans will be further liberalized. It is proposed to set up Central Electronic Registry to prevent frauds involving multiple lending on the same immovable property. Financial Sector Legislative Reforms Commission will be set up to rewrite and streamline financial sector laws, rules and regulations.

The budget 2011-12 is viewed by some analysts as a budget without any ‘big bang’ announcements. But, the budget provides many indications and roadmaps for a high sustainable economic growth with adherence to fiscal consolidation.

Budget 2011-12 at a Glance

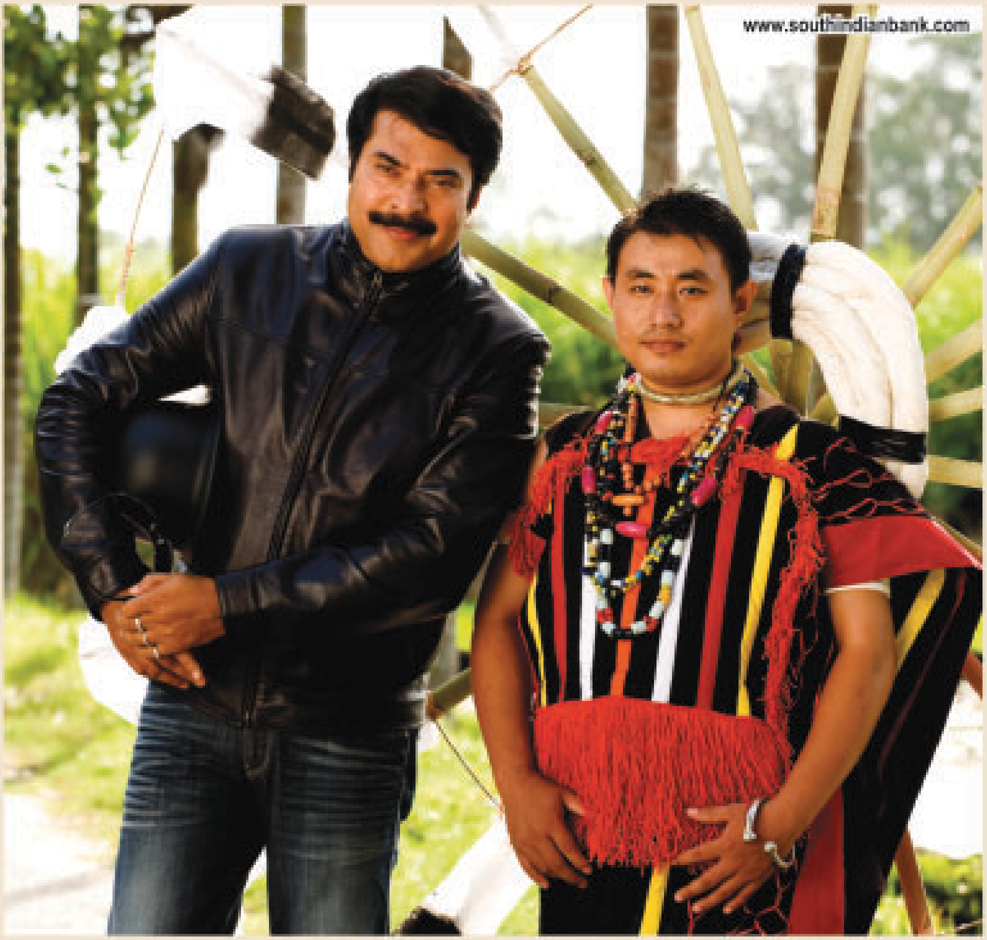
(In Rupee Crore)

	2010-11 Revised Estimates	2011-12 Budget Estimates
1. Revenue receipts (2+3)	7,83,833	7,89,892
2. Tax revenue (net to Centre)	5,63,685	6,64,457
3. Non-tax revenue	2,20,148	1,25,435
4. Capital receipts (5+6+7)	4,32,743	4,67,837
5. Recoveries of loans	9,001	15,020
6. Other receipts	22,744	40,000
7. Borrowings & other liabilities	4,00,998	4,12,817
8.Total receipts (1 + 4)	12,16,576	12,57,729
9. Non-plan expenditure (10+12)	8,21,552	8,16,182
10. On revenue account of which,	7,26,749	7,33,558
11. Interest payments	2,40,757	2,67,986
12. On capital account	94,803	82,624
13. Plan expenditure (14+15)	3,95,024	4,41,547
14. On revenue account	3,26,928	3,63,604
15. On capital account	68,096	77,943
16. Total expenditure (9+13)	12,16,576	12,57,729
17. Revenue expenditure (10+14)	10,53,677	10,97,162
18. Capital expenditure (12+15)	1,62,899	1,60,567
19. Revenue deficit (17-1)	2,69,844	3,07,270
20. Fiscal deficit (16-(1+5+6))	4,00,998	4,12,817
21. Primary Deficit (20-11)	1,60,241	1,44,831

Personal Income Taxes – Budget 2011-12

Individuals other than women & senior citizens	Women below 60 years of age	Senior citizens in the age group of 60 years or more but less than 80 years	Tax rates
0 -1,80,000	0-1,90,000	0 - 2,50,000	Nil
1,80,000-5,00,000	1,90,000-5,00,000	2,50,000-5,00,000	10%
5,00,001-8,00,000	5,00,001-8,00,000	5,00,001-8,00,000	20%
8,00,001 & above	8,00,001 & above	8,00,001 & above	30%

Your comments and feedback on this publication may be sent to Staff Training College, The South Indian Bank Ltd., Thrissur 680 001 or by E.mail: ho2099@sib.co.in



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