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Theme 220

UNION BUDGET 2010 -11 - THE PATH OF FISCAL PRUDENCE

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SIB STUDENTS' ECONOMIC FORUM

MARCH 2010

Theme No. 220 : UNION BUDGET 2010-11 - THE PATH OF FISCAL PRUDENCE

The Union Budget 2010-11 is presented at a time when apparently competing and conflicting economic objectives are required to be reconciled. The rollback of economic stimulus measures was mooted to control the inflationary situation in the economy, but economic recovery and high growth had to be achieved. The public expenditure on infrastructure and rural sector had to be continued for a high growth trajectory, but then fiscal deficit needed to be checked for a long-term growth. Double digit economic growth should be aimed at, but then growth should be socially equitable and inclusive. Tax reforms are required to make tax laws modern and more transparent, but tax burden should not be increased for the common people. The budget document 2010-11 balances all these objectives in an optimal manner in the same manner as it balances the revenues and expenditures of the government for the coming financial year.

In the aftermath of the global economic crisis and the remarkable global management of the economic recovery, all the governments and the central banks are now planning an 'exit strategy' from easy monetary and expansionary fiscal policies. Ample liquidity is already pumped into the economies, and there should be a limit to the existence of surplus liquidity lest another cycle of boom-bust should arise engendering new set of crises. Therefore, there should be at least a partial rollback of the stimulus measures adopted by the government.

Overspending by the government was required in recession/slowdown times to make good the shortage of private investment. Now that clear signals of economic recovery and growth are evident, it is time to follow the path of fiscal prudence and control of public debt in the economy. In short, there should be a roadmap for fiscal consolidation.

What are the major economic challenges that the Budget proposes to address to?

The Finance Minister clarifies that there are three major challenges that the budget seeks to find a solution. The first challenge is to quickly revert to the high GDP growth path of 9 percent and then find the means to cross the ‘double digit growth barrier’. The second challenge is to harness economic growth so as to make development more inclusive. This requires continuance of the development of rural infrastructure. The third challenge relates to the weaknesses in government systems, structures and institutions at different levels of governance. This requires addressing the bottleneck of the public delivery mechanism. ‘Thus the budget cannot be a mere statement of government accounts. It has to reflect the government’s vision and signal the policies to come in future’.

What are the major estimates of receipts and expenditures in the Budget?
The total expenditure proposed in the budget estimates is Rs.11, 08,749 crore, an increase of 8.6 percent over last year. The Plan and non-Plan expenditures estimated at Rs.3, 73, 092 crore and Rs.7, 35,657 crore respectively record an increase of 15 percent in Plan expenditure and 6 percent in non-Plan expenditure over the previous year. Total receipts from taxes and non-taxes amount to Rs.727, 341 crore of which direct taxes form Rs.422, 500 crore and indirect taxes Rs.315, 000 crore. The fiscal deficit, the difference between total expenditures and total receipts, works out to be Rs.381, 408 crore, which is 5.5 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 2010-11 would be of the order of Rs.345,010 crore.

What are the major proposals on the taxation front?
In the direct taxes, personal income tax slabs are widened, thus leaving more disposable income with the people. There will be tax exemption for income up to Rs.1.6 lakh. The 10 percent rate will now extend up to Rs.5 lakh. The 20 percent rate will apply to income slabs beyond Rs.5 lakh to Rs.8 lakh. The maximum marginal rate of 30 percent will now apply on income slab of above Rs.8 lakh. In corporate taxes, the surcharge on domestic companies has been slashed from 10 percent to 7.5 percent. The Minimum Alternate Tax (MAT) has been raised from 15 percent to 18 percent. In indirect taxes, the standard ‘Cenvat’ excise duty, applicable on most non-petroleum products has been raised from 8 percent to 10 percent. This can be seen as partial rollback of the rate reduction granted as part of the various fiscal stimulus packages. The budget effected excise hike of Rs.1 a litre on petrol and diesel along with raising the customs duty from 2.5 percent to 7.5 percent. Though service tax rate has been kept unchanged at 10 percent, the ambit has been widened to cover rail freight and air travel. The budget included a statement of commitment to introduce the Goods and Services Tax (GST) regime and

the Direct Taxes Code (DTC) from April 2011. While the DTC seeks to replace the Income Tax Act, 1961, the GST will subsume various indirect taxes like excise, VAT, and Service tax.

What is the roadmap for fiscal consolidation in the budget?

The fiscal deficit should be in control for balanced non-inflationary economic growth path and for containing debt service burden in the future. The fiscal deficit is reduced to 5.5 percent of the gross domestic product (GDP) in the new budget, down from 6.9 percent in the current fiscal. This is achieved by increase in tax revenues, proceeds of disinvestment and auction of telecom license and curtailment of non-plan expenditure and subsidies. The deficit will be met by market borrowings. The market borrowings are lower than the last year actual figures. Thus there will be less hardening of the interest rates and less 'crowding out' of the private investment in the coming fiscal year. The government would endeavour to reduce fiscal deficit further to 4.8 percent in 2011-12 and to 4.4 percent in 2012-13. In accordance with the recommendation of the 13th Finance Commission, the combined debt of the central government and the states should be limited to 68 percent of GDP by the year 2014-15. The government would soon prepare a roadmap for curtailment of the overall public debt.

How does the budget blend the ideals of high economic growth and inclusive development?

Infrastructure development remains at the forefront of the expenditure agenda, with an outlay of Rs.1.73 lakh crore, about 46 percent of the total Plan allocation. The budget has continued with liberal allocations for rural credit, employment, and rural infrastructure development schemes. The spending on social sector will be to the extent of Rs.1.38 lakh crore, around 37 percent of the total Plan outlay. The plan expenditure is hiked by 15 percent and non-plan expenditure by 6 percent over the previous financial year. Thus it is attempted to rein in government revenue expenditure. Many programmes are announced in the budget to help the marginalized sections of the population with more allocations for health, education, insurance scheme for unorganized workers, another green revolution for the eastern states etc. To spur growth in agriculture sector, a four-pronged strategy covering agricultural production, reduction in wastage of produce, credit support to farmers and a thrust to the food processing sector is envisaged. Thus high growth and inclusive development are integrated in the budget.

Why do the critics state that the budget is inflationary?

There was immediate political reaction that the budget instead of addressing the problem of inflation will aggravate it. It is pointed out that the duty hikes in petroleum products and crude oil would lead to immediate rise in wholesale price index. Also rollback of Cenvat duty by 2 percent will lead to increase in prices of most durable commodities. The government admits that there will be a small impact on prices, but then fiscal deficit needed to be urgently curtailed and for this duty hikes were required, and a prolonged deficit has more implications on long-term inflationary pressures.

What are the Budget announcements having implications on the financial sector?

It is announced that an apex-level Financial Stability and Development Council (FSDC) will be set up to institutionalize the mechanism for maintaining financial stability. The proposed Council has to co-ordinate the functions of various regulators such as RBI, SEBI, IRDA and PFRDA. The need for such a supervisory body is felt in all major economies after the financial crisis. This Council would monitor macro prudential supervision of the economy, including functioning of large financial conglomerates to take care of macro systemic risks. It is decided to open up further private sector banking space. The RBI will give some additional banking licenses to private sector players, including non-banking finance companies, if they meet the RBI's eligibility criteria. Thus competition in the banking sector, especially in private sector segment will intensify. The budget plans to set aside Rs.16,500 crore towards recapitalization of public sector banks. Thus the banks will be able to maintain 8 percent Tier-I capital. Regional Rural Banks also will be recapitalized. The government would extend banking facilities including insurance and other services to habitations having population in excess of 2000 by March 2012. The banking correspondent and other models with appropriate technology back-up would be extended to around 60000 habitations. It has been decided to accord an official symbol to Indian currency – Rupee and the rupee with distinct identity would join the select club of leading global currencies.

The budget has performed a well-balancing act by targeting high economic growth combined with inclusive social development. It has set a roadmap for fiscal consolidation by way of gradual fiscal reduction. It has proposed to raise resources for capital expenditure by disinvestment and partial rollback of duty stimulus. Of course, annual budgets can not be revolutionary in reforms but only evolutionary.

Budget at a Glance

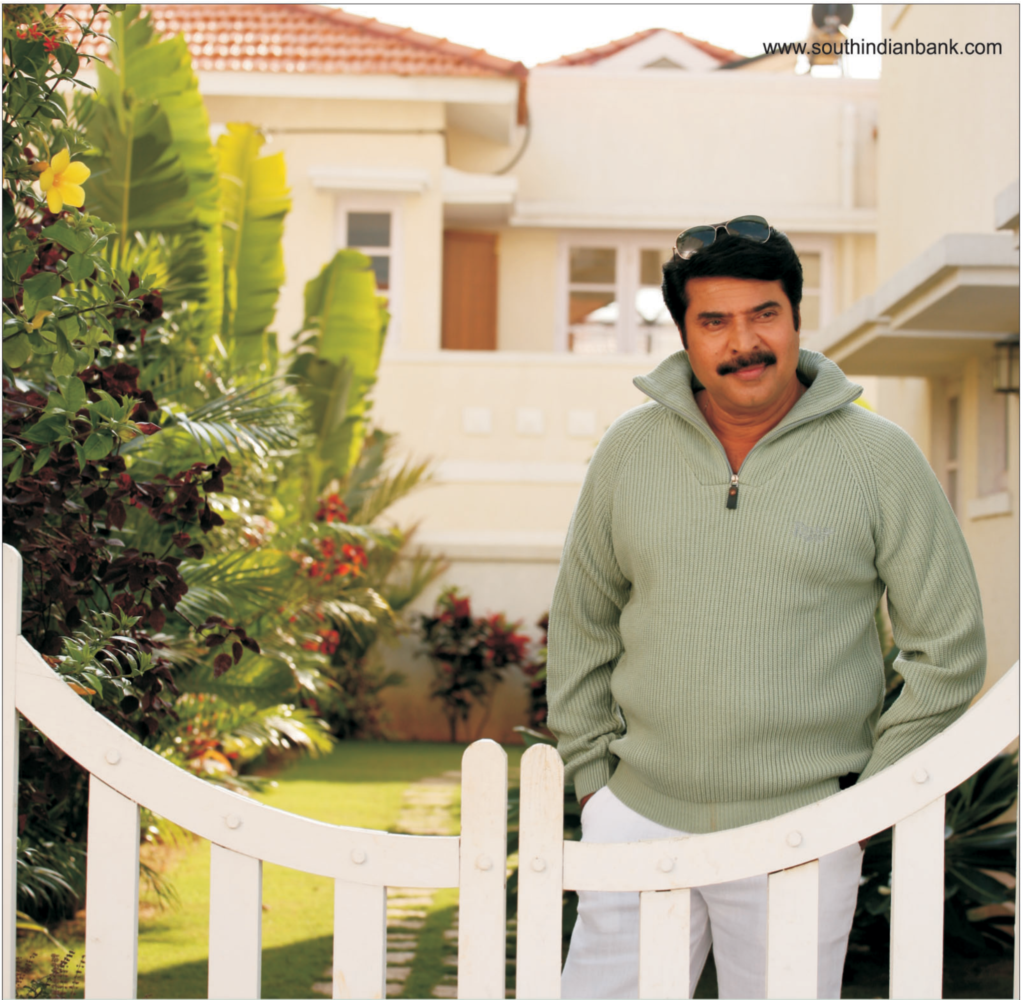
(In Rupee Crore)

	2008-2009 ACTUALS	2009-2010 BUDGET ESTIMATES	2009-2010 REVISED ESTIMATES	2010-2011 BUDGET ESTIMATES
1. Revenue Receipts	5,40,259	6,14,497	5,77,294	6,82,212
2. Tax revenue (net Centre)	4,43,319	4,74,218	4,65,103	5,34,094
3. Non-tax revenue	96,940	1,40,279	1,12,191	1,48,118
4. Capital receipts (5+6+7)	3,43,697	4,06,341	4,44,253	4,26,537
5. Recoveries of loans	6,139	4,225	4,254	5,129
6. Other receipts	566	1,120	25,958	40,000
7. Borrowings and other liabilities	3,36,992	4,00,996	4,14,041	3,81,408
8. Total receipts (1+4)	8,83,956	10,20,838	10,21,547	11,08,749
9. Non-Plan expenditure	6,08,721	6,95,689	7,06,371	7,35,657
10. On revenue account of which,	5,59,024	6,18,834	6,41,944	6,43,599
11. Interest payments	1,92,204	2,25,511	2,19,500	2,48,664
12. On capital account	49,697	76855	64,427	92,508
13. Plan expenditure	2,75,235	3,25,149	3,15,176	3,73,092
14. On revenue account	2,34,774	2,78,398	2,64,411	3,15,125
15. On capital account	40,461	46,751	50,765	57,967
16. Total expenditure (9+13)	8,83,956	10,20,838	10,21,547	11,08,749
17. Revenue expenditure (10+14)	7,93,798	8,97,232	9,06,355	9,58,724
18. Capital expenditure (12+15)	90,158	1,23,606	1,15,192	1,50,025
19. Revenue deficit (17-1) (as percent of GDP)	2,53,539 (4.5)	2,82,735 (4.8)	3,29,061 (5.3)	2,76,512 (4.0)
20. Fiscal deficit {16-(1+5+6)} (as percent of GDP)	3,36,992 (6.0)	4,00,996 (6.8)	4,14,041 (6.7)	3,81,408 (5.5)
21. Primary deficit (20-11) (as percent of GDP)	1,44,788 (2.6)	1,75,485 (3.0)	1,94,541 (3.2)	1,32,744 (1.9)

Personal Income Taxes – Budget 2010-11

INDIVIDUALS OTHER THAN WOMEN & SENIOR CITIZENS	WOMEN BELOW 65 YEARS OF AGE	SENIOR CITIZENS IN THE AGE GROUP OF 65 YEARS OR MORE	TAX RATES
Up to Rs.1.60 lakh	Up to Rs.1.90 lakh	Up to Rs. 2.40 lakh	**Nil**
Above Rs. 1.60 lakh to Rs.5 lakh	Above Rs.1.90 lakh to Rs.5 lakh	Above Rs.2.40 lakh to Rs.5 lakh	**10 %**
Above Rs.5 lakh to Rs. 8 lakh	Above Rs.5 lakh to Rs.8 lakh	Above Rs.5 lakh to Rs. 8 lakh	**20 %**
Above Rs.8 lakh	Above Rs.8 lakh	Above Rs.8 lakh	**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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