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A reasonably good performance: Budget focus is on expenditure to accelerate growth. Deficit will be exceeded

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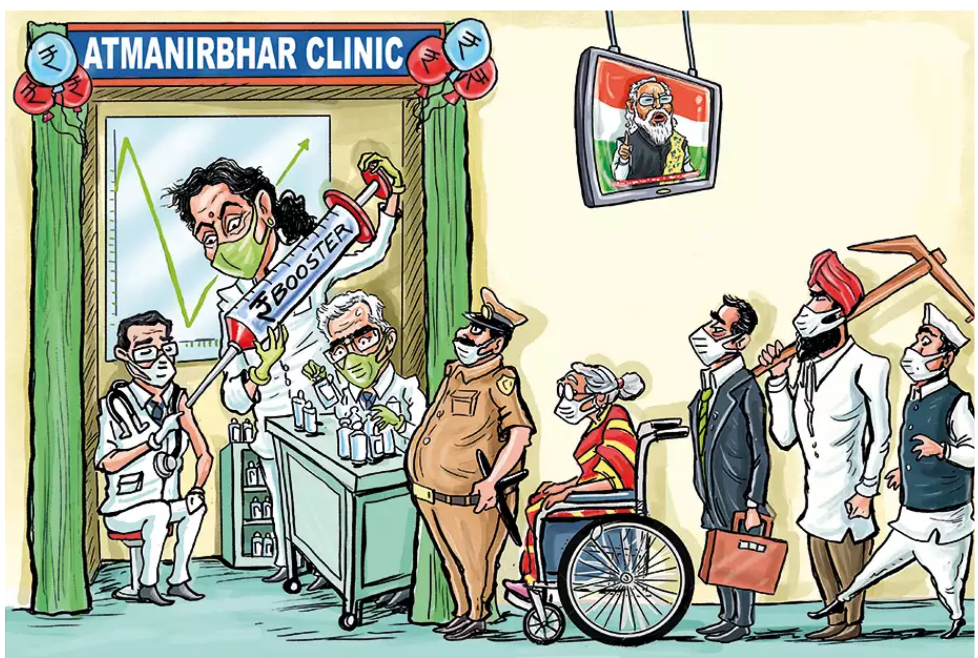
The expectations from the Budget were many. Fiscal 2020-21 is the worst year Ind has seen on economic performance since Independence. CSO had estimated that the economy would shrink by 7.7%. Other forecasts are even more grim. The Budget was expected to address two problems: To provide a strong stimulus to growth and to cast itself in a framework both credible and acceptable. On both thes counts, it has performed reasonably well.

On the revenue side, the Budget has not levied any new tax, direct or indirect whic itself has given great relief to taxpayers. There are however certain other tax changes which have been welcomed. Centre's tax revenue for 2021-22 is budgete to increase by 14.9%. The implied tax buoyancy is a little over 1 because GDP is expected to increase by 14.4%. The key question is, will GDP increase by this percentage? Earlier, it was put out by the government that real GDP will grow by 11%. These projections appear optimistic. This has a direct bearing on fiscal deficit



We'd commissioned two of our illustrators to draw on the same theme. We liked both illustrations equally. We felt this one, by Chad Crowe, was stylistically more suited to the opinion page, and the other to a news page.

The Budget has made a sincere attempt to pull up the economy. The emphasis on capital expenditures is well taken. There's a substantial increase as a proportion of GDP. The shift is more in the composition than the total of expenditures. It's unlikel that the fiscal deficit will hold. We shouldn't be surprised if it exceeds.

The strength of the Budget depends on a number of initiatives announced by the finance minister. Setting up a long term lending financial institution to promote investment is a good move. It in fact revives an earlier practice. Setting up an institution to provide liquidity in the bond market is again an extremely good idea. I fact, in the late 1980s when it was decided to promote initially the Treasury Bill market and later government bond market, two institutions were set up.

There are many other welcome ideas, such as increase in the foreign holding in private insurance companies and setting up asset reconstruction companies to tak care of bad debts of public sector banks. Privatisation of one or two public sector banks is also a good decision. All of these may improve investment climate.

This year's Budget incorporates the recommendations of the 15th Finance Commission (FC). Normally, in the year in which FC recommendations are incorporated, there's a jump in the allocation of funds for states out of gross tax revenue. That hasn't happened this year as FC has retained the share of states of 41% as the previous FC had raised the share sharply.

However, distribution among states may change because of the change in the horizontal formula of distribution. Fiscal effort has come back as a criterion. FC wa fully conscious of the impact of Covid-19 on the economy as they were putting together the recommendations. It has suggested a new road map for fiscal consolidation to be prepared by an Inter-ministerial Group. Even though the NK Singh Committee earlier fixed the target to be achieved in terms of debt/ GDP ratio the operating variable which was to be monitored was only fiscal deficit.

The argument that the path of fiscal deficit must be counter cyclical is well taken. B if we look at the behaviour of fiscal deficit in the past, even in the very good years when growth rate had exceeded 9%, the deficit was not below the mandated level. Fiscal federalism is passing through a critical phase. Fixing tax devolution at 41% i a good move. But this shouldn't be defeated by increasing the cesses which aren't shared with states. The cesses are also not temporary but permanent. Centre, in a true spirit of cooperative federalism, must desist from levying cesses. Even some legal cap can be brought in.

FC has recommended sectoral grants for health, school and higher education and agricultural reforms. Sectoral grants should be distributed in such a way as to resul in additionality. FC hasn't rocked the boat and maintained a reasonable balance between the needs of Centre and states.

In a difficult year like the current one, fiscal deficit consideration recedes back. The fiscal deficit of 9.5% of GDP in 2020-21 is truly high. The main reason is fall in revenue. As compared to budgeted estimates, revised estimates of tax revenue show a decline by 23.04%. For all we know, the fiscal deficit of 2021-22 will also exceed the budgeted level for several reasons.

First of all, tax revenue is perhaps overestimated for reasons already mentioned. Second, non-tax revenues are always overestimated. For example in 2020-21, disinvestment receipts were put at Rs 2,10,000 crore in the Budget and the actual according to revised estimates was Rs 32,000 crore. The time has come to redraw the road map for fiscal consolidation. It's difficult to see how the government could achieve a fiscal deficit of 4.5% of GDP by 2025-26. In fact even a level of 4.5% is high. We need to spell out when we can reach 3% of GDP.

To sum up, Nirmala Sitharaman has done her best in a difficult situation to revive tl economy. The most significant change on the expenditure side is the rise in capital expenditures. The total however remains the same. Fiscal deficit is likely to be exceeded. Once Covid problems are out of the way, a new road map must be drav up to take the deficit to the previously mandated level.