Publication: The Economic Times	
Page no: 20	Date: Mar 23, 2016

BUDGET 2016

Spending, Quality Time

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The dust has settled on Budget 2016. More than just centimetres have been used up in column space to analyse various aspects of the Budget. It might be useful, therefore, to think of the recent Budget slightly differently and to compare and contrast this year's exercise with those we have seen in the last decade. In effect, to examine what's changed and what's not.

As the Indian economy has grown from $1.3 trillion in 2007 to $2.1 trillion in 2015, the fiscal deficit as a percentage of GDP has actually come off from around 6% in 2008-09 to 3.5% budgeted in 2016-17. This suggests that, by and large, the role of the state in economic activity has reduced and fiscal consolidation has become much more apparent as a theme.

If one takes a look at the drivers of this deficit — namely, the expenditure and receipts over time — against an average expenditure growth rate of 15.5% over the last 10 years, total expenditure in 2016-17 is budgeted to grow at 10.8% over 2015-16. Yes, it is true that the base of expenditure is now much larger and one should expect the percentage growth to slow down.

But the fact is that the growth in total expenditure is marginally higher than last year as required by the economy, but significantly less than what it was in the early part of this decade. Fiscal prudence has clearly been the driver of the growth of expenses.

During the same time, the composition of expenditure has also changed. Revenue expenditure as a percentage of GDP has declined from 14.1% in 2008-09 to 10.9% in 2015-16. However, the growth of revenue expenditure is forecast to grow from 5.5% year-on-year to 11.8% year-on-year between 2015-16 and 2016-17 mainly on account of the one rank-one pension (Orop) and Seventh Pay Commission recommendations. This growth would position revenue expenditure as a percentage of GDP for 2016-17 at 11.5%, higher than 10.3% of GDP in 2015-16.

Capital expenditure, on the other hand, has been growing more or less in line with GDP growth, improving marginally from 1.6% of GDP in 2008-09 to 1.7% in 2015-16. It is important to see the capital expenditure not just for the Centre but also for states, especially after the 14th Finance Commission.

The theme of fiscal consolidation is also visible in the fact that the subsidy burden has come down from 2.3% of GDP in 2008-09 to 1.7% of GDP in 2015-16. Unfortunately, though, the elevated interest rate environment in the country has kept interest expenditure as a percentage of GDP broadly unchanged during this time span.

Funding this expenditure has revealed some other trends. The reliance on direct tax revenues has reduced over time, and indirect tax revenues have grown in terms of contribution to total receipts. The share of direct taxes in total receipts has fallen from 29.5% in 2008-09 to 28% in 2015-16, while that of indirect tax has gone up from 18% in 2009-10 to 24.5% in 2016-17.

The share of tax revenue in total receipts has gone down from 61% to 54% between 2006-07 and 2014-15. During the same time, the share of capital receipts has grown from 25% to 34% of total receipts. This suggests that divestment and strategic stake sales, along with telecom spectrum auctions, have funded a bigger part of the government's revenue over the years.

Fiscal capacity creation is important for long-run economic development, especially in developing economies. Simple tax-GDP and spending-GDP ratios suggest that India under-taxes and underspends relative to other comparable countries. But, adjusting for the level of economic development, India probably neither under-taxes nor underspends.

India, however, does stand out in terms of the low number of individual income-tax payers, currently only about 4%, far from the desirable estimate of about 20%. Building long-run fiscal capacity could mean not raising exemption thresholds for personal income tax, allowing natural growth in income to increase the number of taxpayers. Looking to widen the tax net so that more people pay direct taxes is also important.

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Of course you will spend, Uncle. But aapka deficit?