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Union Budget: Macrobatics?

By N.S. Viswanath* Bangalore, April 6, 2012

Union budget 2012-13 is over with the Finance Minister presenting a well articulated budget. The minister has mixed rationality with facts and irrationality with his personal beliefs (He claims that his lucky number is 3). The economy is expected to grow at 6.9% in 2011-12 which had grown at 8.4% in the two preceding years. Agriculture is growing at 2.5% and is expected to grow at around 3.8% or 4.0%. Industry is shows a marginal improvement at 3.9% from 2.0% growth,on an average. Services sector is accelerating its growth at 9.1%. Interestingly, services, industry and agriculture are contributing 59%, 27.0% and 13.9% of GDP respectively. Inflation rate is at 8% suggesting that it has crossed over 6% fixed as threshold level for India.

The savings rate is estimated at 32.3% and the rate of capital formation is at 35.1% in 2010-11 respectively. The share of India is 2.22% with rates of growth of exports and imports being 23.5% and 29.4% respectively. Foreign exchange reserves stood at Rs.4292.8 bn and the average exchange rate was at Rs.47.70 per US dollar in 2010-11. Against this back drop, the budget 2011-12 is analysed for deriving implications.

Priorities

The priorities before the government is to sustain growth rate, peg inflation and ensure buoyancy amongst economic agents. Political compulsions confound with economic priorities to make decisions complex. The finance minister has made financial acrobatics to ensure good feel amongst all sections of people. This budget, like any other, had created expectations amongst business, industry and consumers. These have been attended to by enhancing tax exemption limits, reduction in age for tax benefits, investment ,equity measures and health care insurance preventive checkup expenses. There are exemptions in service tax on branded dwelling and reduction in tax for branded garments. Tax free investments are followed by reduction in security transaction tax by 1%. Industry has gained from reduction in withholding tax on interest and exemptions.

The finance minister has increased service tax to 12% and has added more services into the net. The prices of food products and common man's good been allowed to increase because of higher exercise duty. Bicycles and gold will cost more because of tax increase and import duties respectively.

Macrobatics

With so many tax proposals the finance minister intends to reduce fiscal deficit to 5.1% of the GDP in 2012,while the realization of fiscal deficit was at 5.1% of the GDP in 2012. The realization of fiscal deficit was at 5.9% for 2011-12 as against 4.6% targeted.An effort has been made to keep subsidies under 2% of GDP in addition to a disinvestment of target of Rs.30,000 crores. The projected growth rate of GDP for 2012-13 is 7.6% which has had an inflation rate at 9.1%. How can anyone achieve 7.6% growth rate without fiscal and financial efforts to contain inflation?

The finance minister proposes tax reforms with FRBM Act- 2003 in vogue. He has announced public debt management agency bill 2012-13 to be introduced in the parliament. Direct Tax Code (DTC) and Goods and Services Tax (GST) are to be enacted to expand tax base for augmentation of revenues. He intends to revisit public expenditure management. These macrobatics are unlikely to help in reaching set growth and development targets as the country is now poised with governance problems.

Governance – The Critical Issue

The finance minister must be congratulated for admitting the factors and forces that are bent upon impending growth efforts. Corruption is the main determinant for blocking any concerted efforts towards real growth prospects. Corruption is creating easy money. This unaccounted money is damaging the fabric of developmental efforts. This is accentuating inequality which leads to disaster. Corruption is

* Dr. N. S. Viswanath is Director, Bhavan's Management Research Centre (BMRC) and Dean, M.P. Birla Institute of Management, Associate Bharatiya Vidya Bhavan Race Course Road, Bangalore-1.

weakening the governance quality. Where to cut out corruption when polity is strong enough to destroy any seminal effort? We should have a dilated discussion on corruption at the policy level, while action from the top is essentially critical.

Tax evasion is as worst as money laundering. Businesses and functional activities evade taxes to preserve and maintain liquidity. Developmental efforts are thwarted by tax evasion which would leave little money for productive activities. Tax laws per se many not help unless governance mechanism is geared up for targeted realization. Many tax reforms envisaged by the finance minister may not help in blocking evasion. Proactive measures such as rewards, recognition and special status of citizenship may accentuate money inflow.

Antimony laundering measures are yet to acquire legal status. Our parlimentations are busy legislating on other priority issues. Market activating measures by Reserve Bank of India may help regulate laundering of money in the development efforts. The government is not optimistic of concrete measures on antimony laundering.

The government is seized of matter on the illicit money alleged to be deposited in Swiss bank by many Indians. Efforts to bring back the deposited money are being attempted. The money deposited in Swiss bank is the strength of many leaders. As such the government is slow in action. This means no sincere action is attempted to acquire illegal money. Will this help realize targeted growth rate? No, not at all. Some steps, however, have been initiated on drug trafficking prevention. Domestic and international efforts are being worked out. Governance as measured by its quality is delivering leading to reflect a pessimistic out look. Leadership of impeccable quality may solve the issue. Where can we find quality leadership to sail through economic transformation? High inflation rate coupled with high interest rate have led Reserve Bank of India to adjust CRR at thirteen times during last one year.

Agriculture – The Primary Sector

Agricultural sector is growing at 2.5% against a target of 4.0% per annum. The food grain production is estimated at 250.4 million tones with a per capita availability of 193 grams per day. This accounts for production of non edible industrial products. Prices of agricultural products have thrown continuous increases during the last two years. Supply induced inflation caused serious concern to the government and people suffered due to value deceleration of their earnings. Food, vegetables and fruit prices sky rocketed making aam admi feel the heat of rising prices. The government has expressed interest to support agricultural sector in all possible ways. Subsidies for agricultural products continue in spite of low capital formation in agriculture at 20.1% of GDP. Distribution mechanism at subsidized prices for BPL families continues to exist. Nutrient based subsidies (NBS) are a part of governmental efforts to make available the nutrition rich products to the end user. The government is actively considering direct transfer of subsidies to the end user. Agriculture sector lacks institutional support although institutions have proliferated. Sustainable growth orientation measures such as water management, organic farming, marketing institutions and extension institutions for post harvest practices are not reflected in the budget proposals in a formulated way.

Manufacturing Sector – Backyard?

Domestic value addition is crux of the finance minister's proposal to the manufacturing sector. A service of duty reduction measures for low risk, inputs, technical fibre and steel have been initiated. Expert duty increase on iron ore and import duty reduction measures are welcome step to derive productions from the manufacturing sector. Infrastructure is gaining importance in the budget proposals. This should get more importance than what is at present. Investment in infrastructure would yield long term and duration returns.

Services sector – The Growth

Services sector with its share of 59.0% of the GDP is the sector leading growth of the economy. Services sector led growth must continue with a positive slope. Broadening the base of the sector by forming a negative list and introduction of Goods and Services Tax (GST) are critical for holding on to the growth trajectory. Tax proposals for direct and indirect taxes are appropriate steps to put the sector on contributing path. Indirect taxes at Rs.11,300 crores revenue may prop up the sector for better results.

Conclusion

This budget may be characterized as low tax heavy, development sustainable and a well crafted macrobatics exercised by the finance minister. The government has made a cautions move towards capturing business sentiments and feelings of aam admi. The realization short term growth rate is achievable. However, the long term of targets of growth with equity is a mirage. ❑