THE UNION BUDGET 2018-19

H. P. Ranina
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FORUM
OF FREE ENTERPRISE

"Free Enterprise was born with man and shall survive as long as man survives".

- A. D. Shroff
Founder-President
Forum of Free Enterprise

SHAILESH KAPADIA

(24-12-1949 – 19-10-1988)

Late Mr. Shailesh Kapadia, FCA, was a Chartered Accountant by profession and was a partner of M/s G.M. Kapadia & Co. and M/s Kapadia Associates, Chartered Accountants, Mumbai.

Shailesh qualified as a Chartered Accountant in 1974 after completing his Articles with M/s Dalal & Shah and M/s G.M. Kapadia & Co., Chartered Accountants, Mumbai. Shailesh had done his schooling at Scindia School, Gwalior and he graduated in Commerce from the Sydenham College of Commerce & Economics, Mumbai, in 1970.

Shailesh enjoyed the confidence of clients, colleagues and friends. He had a charming personality and was able to achieve almost every task allotted to him. In his short but dynamic professional career, spanning over fourteen years, Shailesh held important positions in various professional and public institutions.

Shailesh's leadership qualities came to the fore when he was the President of the Bombay Chartered Accountants' Society in the year 1982-83. During his tenure he successfully organized the Third Regional Conference at Mumbai.

Shailesh was member, Institute of Fiscal Studies, U.K.; member of the Law Committee and Vice-Chairman of the Direct Taxation Committee, Indian Merchants' Chamber. He was also a Director of several public companies in India and Trustee of various public Charitable Trusts.

He regularly contributed papers on diverse subjects of professional interest at refresher courses, seminars and conferences organised by professional bodies.

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THE UNION BUDGET 2018-19

I

A Vision Document for Inclusive Growth

H. P. Ranina*

The last Budget before the next general elections does a tightrope walk by reconciling fiscal consolidation with the need to keep up the growth momentum for the economy. A nominal growth rate of 11.5% is built into the budget's revenue estimates, with the underlying assumption of a 5% inflation rate in view of rising oil prices. Large outlays have been earmarked for agriculture, social security and infrastructure development.

Despite structural changes made in terms of introduction of the Goods & Services Tax law

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and the initial teething problems of this landmark legislation, there has been a marked tax buoyancy for the year ending 31st March, 2018, which is expected to increase in the financial year 2018-19. Most of the teething problems should be smoothened out in the coming days and the GST regime will contribute substantial revenues in the full financial year.

The big bang announcement has been in respect of the National Health Protection Scheme which will cover more than 100 million indigent and vulnerable families, providing for upto Rs.5 lakh cover per family every year for secondary and tertiary care, including hospitalization. This marks a welcome shift towards universalization of welfare schemes.

During the financial year 2017-18, there has been a healthy increase in tax revenue of Rs.42,440 crore beyond what was budgeted for. Capital receipt from disinvestment of Rs.1 lakh crore is higher than the amount of Rs.72,500 crore which was estimated to be recovered in 2017-18. However, during this financial year, expenditure of the Government has increased largely on account of general services which include administration, pension and defence.

The slippage in fiscal deficit for this financial year is primarily due to the fact that March figures of the Goods and Services Tax will be accounted for in April and not in the fiscal year 2017-18. This has resulted in a slippage in the fiscal deficit for the current financial year which will now be 3.5% of GDP.

For the financial year 2018-19, the deficit is estimated to be Rs.6,24,276 crore which is 3.3% of GDP. However, the implementation of the National Health Protection Scheme will cast a substantial burden on the Exchequer. The farmers' demand for calculation of the Minimum Support Price as per the Swaminathan Committee recommendation may cast a long shadow on revenue expenditure, together with an increase in global oil prices and funds required for re-capitalization of public sector banks. Hence, the projected deficit target of 3.3% of GDP may be difficult to adhere to.

Revenue and Expenditure for Fiscal Year 2018-19

The Finance Minister has highlighted the startling facts that, for the assessment year 2016-17, 1.88 crore individual businessmen and professionals who filed their tax returns paid an aggregate tax of just Rs.48,000 crore. As against this, 1.89 crore salaried individuals filed their tax returns and paid total tax of Rs.1.44 lakh crore. These figures clearly show that the self-employed class of tax payers are notoriously non tax compliant and seem to have got away with impunity over the past seventy years. Hopefully, with effective implementation of the GST regime, tax compliance will increase leading to improved tax collections.

The collection of taxes from individuals and other non-corporate assessees during the financial year 2018-19 is estimated to be Rs.5,29,000 crore, and the collection from corporation tax is estimated to be Rs.6,21,000 crore, aggregating to Rs.11.5 lakh crore. Indirect tax collection by way of customs duties, excise duties and the Goods & Services Tax along with other indirect taxes is estimated to be Rs.11,21,242 crore. After transferring around 35% of the gross tax revenue of Rs.22,71,242 crore to State Governments as per Finance Commission's recommendations, the Central Government will retain Rs.14,08,649 crore to be spent for plan and non-plan expenditure.

The non-plan expenditure would primarily be in respect of establishment expenditure of Rs.5,08,400 crore, pension Rs.1,68,466 crore, defence Rs.2,82,733 crore, and interest on monies borrowed amounting to Rs.5,75,795 crore. Thus, the entire net tax revenue would go towards expenditure on the aforesaid four items. The expenditure on developmental schemes of the Central Government will, therefore, be met partly out of the non-tax revenue of Rs.2,45,089 crore and substantially out of borrowings of Rs.6,24,276 crore which is the fiscal deficit budgeted for the financial year 2018-19. This deficit is estimated at

3.3% of the GDP for this financial year which has been projected at Rs.187,22,302 crore, roughly USD 2.925 trillion.

Incentives for Agriculture and Rural Development

During the financial year 2016-17, for which final figures are available, the country achieved a record food grain production of around 275 million tonnes, and in respect of fruits and vegetables of around 300 million tonnes. Farmers are now being incentivized by assuring them of minimum support price which would be fifty percent more than the cost of production. This will cover all crops produced by farmers throughout India.

The development of the Gramin Agricultural Markets will provide farmers facility to make direct sale of their produce to consumers and bulk purchasers. All these measures will ensure that the farmer's income is doubled in the next five years. This will give a tremendous boost to industrial growth as 47% of the population is dependent on agriculture and, with more purchasing power in their hands, demand for goods and services will increase.

The most important announcement in this year's budget for the rural sector is that institutional credit for agriculture will be in the region of Rs.11 lakh crore during the financial year 2018-19. Lessee and tenant cultivators will also be entitled to avail of the loans, which will reduce their dependence on usurious moneylenders. Agricultural commodities exported out of India touched a figure of USD 30 billion. To realize the target of USD 100 billion, 42 mega food parks have been set up with state-of-the-art testing facilities.

To promote ease of living, steps are being taken to alleviate the common problems of the poor. Free LPG connections will be provided to five crore families which, in the next few years, would be increased to eight crore. Currently, four crore families are being provided with electricity connection free of charge entailing an outlay of Rs.16,000 crore. In the rural areas, more than one crore residential units are to be constructed, and in the urban areas 37 lakh such units.

Education and Tourism

In the field of education, technology will be the biggest driver in improving the quality of education. This would be done through increasing the digital intensity in education by gradually moving from the blackboard to the digital board. Substantial efforts need to be made to upgrade the skills of teachers. Investment in research is being given high priority with a budgetary allocation of Rs.1 lakh crore to be spent over the next four years. Under a proposed scheme, one thousand B.Tech students will be selected every year and given fellowships to pursue the Ph.D. course in IITs and the Indian Institute of Social Science.

The tourism sector is considered to be the major job provider not only in India but in all countries of the world. India has not realized its full potential considering its rich cultural and historical heritage. The Government has, therefore, decided to transform ten prominent tourist hotspots into iconic destinations through intensive marketing and branding.

The Government plans to increase the number of airports by five times the present number of 124. Under the UDAN scheme, 64 unconnected airports in India are being revived. This will not only give a boost to the travel industry, but will generate more employment opportunities in different facets of tourism, including the hotel and hospitality sectors.

The tourism sector will also get a boost on account of modernization of railways, redevelopment of major railway stations and providing greater facilities and enhanced quality of food. The doubling of railway tracks in certain areas will help speed up trains and increase capacity for transportation of goods on dedicated rail tracks which will leave the existing tracks free for passenger traffic.

MSMEs and Job Creation

The medium, small and micro enterprises have been the major engine of growth and employment.

Formalization of the business of these enterprises is taking place after demonetization and introduction of the Goods & Services Tax. This is generating enormous financial information and will be used for providing sufficient capital for the growth of this sector. The budget proposals have provided emphasis for the small and medium enterprises by allocation of Rs.3 lakh crore to be given as loans to entrepreneurs who invest in start-ups. Programmes of entrepreneurship and skill development would ensure that the young become job creators rather than job seekers.

To encourage creation of additional jobs, the deduction under section 80-JJAA of the Income-Tax Act, 1961 (the Act), has been liberalized which will permit deduction of 130% of the wages paid to additional employees who are employed for a minimum period of 150 days in the case of the apparel, footwear and leather industries. In these sectors, the Government will contribute 12% of the salary to the Employees' Provident Fund for new employees for a period of three years. Introducing the system of fixed term employment is a major step towards labour reform.

Incentives for Start-ups

To promote start-ups, the tax holiday provision under section 80-IAC of the Act is currently available for three consecutive assessment years out of seven years at the option of the assessee. This benefit will be available if the entity is incorporated after 1st April, 2016, but before 1st April, 2019, and the total turnover of the business does not exceed Rs.25 crore in any of the financial years beginning from 2016-17 up to 2020-21. Such start-up must be engaged in the eligible business which involves innovation, development, deployment or commercialization of new products, processes or services driven by technology or intellectual property.

In order to improve and enhance the effectiveness of this tax holiday provision, the Finance Bill, 2018, has extended the benefit even to start-ups which are incorporated before 1st April, 2021. The requirement of the turnover not exceeding Rs.25 crore would apply to seven financial years commencing from the date of incorporation. Further, the definition of eligible business has been expanded to provide that the benefit would also be available if the entity is engaged in a scalable business model with a high potential of employment generation or wealth creation.

Rationalization for Business Transactions

Section 145 of the Act empowers the Central Government to notify Income Computation & Disclosure Standards (ICDS). The Central Government has notified ten such standards which are effective from the financial year 2017-18 for computation of business or professional income or income from other sources. To give effect to certain judicial pronouncements on the issue of applicability of ICDS, it is proposed to provide that marked to market loss or other expected loss computed in the manner provided in the ICDS would be allowed as a deduction under section 36 of the Act. Any foreign exchange gain or loss in respect of specified foreign currency transactions would be treated as income or loss computed in the manner provided in ICDS.

In respect of a construction contract, the profits would be determined on the basis of percentage of completion method. For this purpose, contract revenue would include retention money. Contract costs would not be reduced by incidental interest, dividends and capital gains.

Amendments are also proposed to provide that for determining the taxable profits of a business, valuation of inventory would be made at lower of actual cost on net realizable value computed in the manner provided in the ICDS. Valuation of purchase and sale of goods or services and of inventory would be adjusted to include the amount of any tax, duty, cess or fee actually paid or incurred by the tax payer to bring the goods or services to the place of its location.

Unlisted securities or securities which are listed but not quoted on a recognized stock exchange would be valued at the actual cost in the manner provided in the ICDS. Listed securities would be valued at lower of actual cost on net realizable value as provided in the ICDS. Finally, the ICDS provisions are sought to be streamlined by providing that interest received by an assessee or enhanced compensation would be deemed to be the income of the year in which it is received. The claim for escalation of price in a contract or the claim for export incentives would be treated as income of the financial year in which reasonable certainty of its realization is achieved. Some of these amendments may lead to further litigation and would require clarifications in future.

The Government has discontinued the earlier 8% Savings (Taxable) Bonds, 2003. New bonds under the 7.75% GOI Savings (Taxable) Bonds have been issued this year. Interest on these bonds would also be liable to tax. No tax would be deducted at source if the interest earned is less than Rs.10,000 in a financial year. Where higher interest is paid, the tax would be deducted at source at the time of making payment of interest to residents.

International Taxation

Under section 9 of the Act, 'business connection' includes business activities carried on by a non-resident through dependent agents. The scope of business connection is similar to the provisions relating to Dependent Agent Permanent Establishment (DAPE) which is referred to in

Double Tax Avoidance Agreements which India has entered into. In terms of the DAPE rules in tax treaties, if any person acting on behalf of the non-resident is habitually authorized to conclude contracts for the non-resident, then such agent would constitute a permanent establishment (PE) in the source country. However, with a view to avoid establishing a PE, the person acting on behalf of the non-resident negotiates the contract but does not conclude the contract.

It is now proposed to amend section 9 of the Act to provide that business connection would also include any business activities carried on through a person who habitually concludes contracts or plays a principal role leading to conclusion of contracts by the non-resident. This amendment has been made to bring it in line with the provisions of the Double Tax Avoidance Agreement as modified by Article 12 of Multilateral Convention to Implement Tax Treaty Related Measures.

At present, emerging business models such as digitized businesses which do not require physical presence in India or an agent in India do not fall within the scope of business connection in India. In order to widen the scope of business connection, it is proposed to amend section 9 to provide that 'significant economic presence' in India would also constitute a business connection. For this purpose, significant economic presence would mean systematic and continuous soliciting of business activities or engaging in interaction with such number of users, as may be prescribed, in India through digital means. Further, significant economic presence would include transaction in goods, services or property carried out by a non-resident in India.

Transactions of downloading of data or software in India would also result in significant economic presence if the aggregate of payments arising from such transactions during the financial year exceeds the amount as may be prescribed. So much of the income as is attributable to such transactions or activities would be deemed to accrue or arise in India, whether or not the non-resident has a residence or place of business in India, or renders services in India.

Sops for Salaried Employees

Salaried employees will now be eligible for a standard deduction of Rs.40,000 per annum. While the transport allowance of Rs.19,200 and reimbursement of medical expenses of Rs.15,000 are done away with, a large number of employees will benefit from the standard deduction where they do not receive from their existing employers these two benefits. Further, pensioners who do not receive these allowances will substantially benefit as a result of the standard deduction being given to them.

Senior citizens will now enjoy tax-free interest on deposits with banks up to Rs.50,000 per annum instead of Rs.10,000 under section 80-TTA. Further, deduction for health insurance premium has been increased from Rs.30,000 to Rs.50,000. The limit of deduction for medical expenditure in respect of certain critical illnesses has been increased to Rs.1 lakh from Rs.60,000 under section 80-DDB. Under the scheme for senior citizens whereby 8% interest is given by Life Insurance Corporation of India, the limit on investment which is currently Rs.7.5 lakhs has been doubled to Rs.15 lakhs.

Capital Gains Tax Regime

Long-term capital gains on sale of shares are currently exempt if the shares are sold through the stock market and securities transaction tax is paid. For the assessment year 2017-18, the total amount of exempted capital gains from listed shares was Rs.3,67,000 crore. It is now proposed to levy 10% tax on long-term capital gains in excess of Rs.1 lakh, without giving the benefit of indexation. However, this provision will only apply where shares are sold on or after 1st April, 2018. This has been clarified by the Central Board of Direct Taxes as the new provision will apply only from Assessment Year 2019-20, relevant to the financial year ending on 31st March, 2019.

Further, long term capital gains made up to 31st January, 2018 will not be liable to tax. There will be no deduction of tax at source from payment of long-term capital gains to a resident tax payer. However, in the case of non-resident tax payers, except foreign institutional investors, there will be a withholding tax of 10%.

Cost indexation benefit has been granted for shares which were unlisted on 31st January, 2018, but which are listed subsequently. Further, indexation benefits will be available for unlisted shares which are exchanged for listed shares at the time of mergers or amalgamations, or at the time of corporate restructuring.

Corporate Taxation

All companies having a turnover of less than Rs.250 crore will now have to pay tax only at the rate of 25%. This new tax will, therefore, cover more than ninety percent of the companies in India, leaving only 7,000 companies which will have to pay tax under the present regime. However, these companies, after claiming various deductions and exemptions under the income-tax law, are in any case paying tax of around 24%.

Hence, the corporate tax rate structure has been rationalized to permit enough retention of profits for investing in additional capacities. Foreign companies which are engaged in shipping, air transport, oil exploration and turnkey construction projects have been exempted from the minimum alternate tax under section 115-JB with retrospective effect from 1st April, 2001. This will give a tremendous boost to foreign direct investment.

Further, where an application under the Insolvency & Bankruptcy Code, 2016 has been admitted by the National Company Law Tribunal, the company will be entitled to reduce the unabsorbed depreciation and brought forward losses from its book profits while computing the minimum alternate tax. The past losses of such companies which are closely held can be carried forward and set off in subsequent years though there may be a change in the majority shareholding. Hence, section 79 of the Act will not apply in such cases.

Where a wholly-owned Indian subsidiary receives any property from its holding company and vice versa, no income will be deemed to arise under the provisions of section 56(2)(x) of the Act. Where stock-in-trade is converted into capital asset, the fair market value of the same on the date of conversion would be taken into account for computing business income. Deemed dividend under section 2(22)(e) of the Act will now be subject to the dividend distribution tax at the rate of 30% without grossing up.

Empowerment and Inclusive Growth

To conclude, this budget sends a clear signal of working towards empowerment and active inclusion.

Inclusion is essential for sustainable growth. Active inclusion is that which increases capabilities and allows more people to contribute and participate in the benefits of growth. Expenditure on agricultural productivity, education, health, employment and empowerment of the small and medium scale industries will all help active inclusion.

The budget proposals deal with future challenges and opportunities by providing for institutional responses. The Government's commitment towards economic empowerment is coupled with its desire for maintaining fiscal prudence.

In short, the budget has achieved multiple objectives within a prudent fiscal framework by ensuring that the public debt of India will not exceed 40% of its Gross Domestic Product. The budget reflects the Government's consistent and pragmatic endeavour to spur economic growth. Growth is never by chance. It is a result of forces working together. This year's budget proposals will undoubtedly lay the foundation for a double digit rate of growth from 2020.

The GDP of India for the financial year 2017-18 will touch USD 2.6 trillion, and for the next financial year ending 31st March, 2019, it will be around USD 2.9 trillion. This makes India the seventh largest economy but in terms of purchasing power parity, the Indian economy is considered to be the third largest in the world.

THE UNION BUDGET 2018-19

II

Reflections on the Budget 2018-19

Sunil S. Bhandare*

Setting the Perspective

No other public policy issue evokes so much of attention and assessment as the Central Budget. That perhaps is not unusual. After all, the budget happens to be the most pervasive and powerful instrument of economic policy. It reflects the Government's vision, strategies and action plans. And all those need to conform to aspirations and expectations of stakeholders at large. Of course, this time, there have been several more engaging reasons, both political and economic, which provoked intense curiosity about what the Finance Minister was likely to unfold. On the political front,

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the setting was influenced by the outcome of some crucial state assembly elections, especially a visible setback encountered by the BJP in Gujarat. Thus, there were imperatives of shoring up its political constituency before several upcoming major state assembly elections scheduled during 2018-19, such as Karnataka and MP, etc. and more importantly, the next crucial Loksabha election sometime in May 2019. Indeed, this happened to be the last full-fledged budget of the present NDA government.

Not surprisingly, the keen observers of the political economy were anxious to see how the budgetary strategy would navigate the government's natural instinct towards becoming overtly populist in the midst of formidable challenges of strengthening fiscal governance and economic revival. On the economic front, there have also been far too many dominant factors at play. Illustratively, the teething troubles in the implementation of GST since 2017; the lingering adverse impact of demonetization; the consequences of surging crude oil prices on fiscal consolidation and inflation; a prolonged phase of agricultural stagnation; the severity of rural distress; the urgency of stimulating industrial and investment revival; the progress in a spate of key policy initiatives to resolve mounting tide of banks' NPAs; the issues of insolvency and bankruptcy of businesses; imperatives of building up investors' confidence; and so on.

Fortunately, a sequence of encouraging trends and events has preceded the presentation of the budget 2018-19. The latest Economic Survey points out that "in the second half of the year, the economy witnessed robust signs of revival. Economic growth improved as the shocks began to fade, corrective actions were taken, and the synchronous global economic recovery boosted exports. Reflecting the cumulative actions to improve the business climate, India jumped 30 spots on the World Bank's Ease of Doing Business rankings, while similar actions to liberalize FDI regime helped increase flows by 20 percent. And the cumulative policy record combined with brightening medium-term growth prospects received validation ...... in the form of a sovereign ratings upgrade, the first in 14 years". The Survey has in fact scaled up the projected real GDP growth rate in 2017-18 to 6.75% [versus CSO's estimates of 6.5%], based on its expectations of a substantial rebound to 7.5% growth rate in the second half of the current financial year. It further expects the real GDP growth rate to rise to 7-7.5% in 2018-19, "thereby reinstating India as the world's fastest growing major economy".

This reassuring assessment of the Survey about improved growth profile of the economy has since been ratified by the latest CSO data, which has estimated a sharp improvement in real GDP growth rate at 7.2% in Q3 [Oct-Dec] 2017-18 as against 5.7% and 6.5%, respectively in Q1 [Apr-June] and Q2 [Jul-Sept] of 2017-18. Several "green shoots" are also visible over the past several months – prominently in improved performance of major manufacturing industries be it automobiles, aluminium, steel, cement, consumer durables or pharmaceuticals. Like-wise, corporate earnings have regained a slice of their lost steam and an up-tick, *albeit* hesitant, is being observed in investment activities – witness, the hectic developments in fund raising through IPOs; credit growth and capital inflows. On the eve of the budget, stock markets had also expressed their vote of confidence about the emerging economic outlook. All the major market indices had scored significant gains – scaling new heights. Unnervingly, during the post-budget trading sessions so far, there has been a sharp retreat in stock markets partly in response to wayward behaviour of global financial markets; protectionist policy stance of the USA and a few other countires; and near home, the break-out of banking scams, especially the confidence-shaking PNB scam.

Underpinnings of Budgetary Strategy

Be that as it may, this article seeks to focus on the underpinnings of budget's strategic framework.

Doubtless, the Finance Minister must have been overburdened with a huge lot of expectations from across various sectors and sections of the economy. Consequently, when the actual budgetary proposals were laid out, there have been quite a few inevitable disappointments. Thus, many keen observers and reformists are vehemently critical about several features of the budget, especially–

First, the fiscal slippage and soft-pedaling of fiscal consolidation path for second year in succession: Two key justifications given by the official spokespersons are: [i] that thanks to the implementation of GST, the treasury could receive revenues from this sources only for 11 months, instead of 12 months; and [b] that there has been shortfall in non-tax revenues on account of various developments, including deferment of spectrum auction. We would be looking at the overall budgetary performance little later;

Second, some irritants in tax proposals – the reintroduction of long-term capital gains at 10% after a gap of fourteen years has received the maximum flak – contributing in no small measure to a sharp setback in stock market sentiments;

Third, a visible shift towards protectionist stance as evident from steep hikes in customs duties on as many as 46 tariff items with a view to providing adequate protection to domestic industry. Such tariff related protection now includes several consumer goods from fruit and vegetable juices to perfumes to watches to toys and games. Similarly, increased protection would now also be available to automobile and automobile parts as well as electronics/ hardware. While critics have argued that this measure is anti-globalization and retrograde, two key points made by the official spokesperson in support of these measures are: [a] that new higher customs duties on concerned goods are well within India's bound tariff commitments to the WTO; and [b] that the mission Manufacturing India calls for protecting the sectors wherein India can legitimately build its competitiveness, increase export potential and generate employment opportunities for her growing class of skilled and semi-skilled manpower;

Fourth, there is considerable skepticism about the scope and effectiveness as well as likely fiscal dimensions of series of social sector initiatives. Illustratively, the much talked about ambitious flagship National Health Protection Scheme, which proposes to cover 100 mn. poor, and vulnerable families [or 500 mn beneficiaries] being entitled to health insurance coverage of up to Rs.5 lakhs per family per year for secondary and tertiary hospitalization. While the initiation of a comprehensive universal health protection scheme is laudable, issues are being raised concerning [a] "inadequate" budgetary allocations; [b] lack of detailing of the scheme as well as its explicit reasonable timeframe for implementation.

Nevertheless, the budget per se has been welcomed as positive and well balanced, offering comprehensive strategy towards stronger and sustainable economic revival. In this context, the Finance Minister himself sounds very confident when he observes in his budget speech "while making the proposal in this year's Budget, we have been guided by our mission to especially strengthen agriculture, rural development, health, education, employment, MSME and Infrastructure sectors of the economy. ***I am sure the New India which we aspire to create now will emerge".***

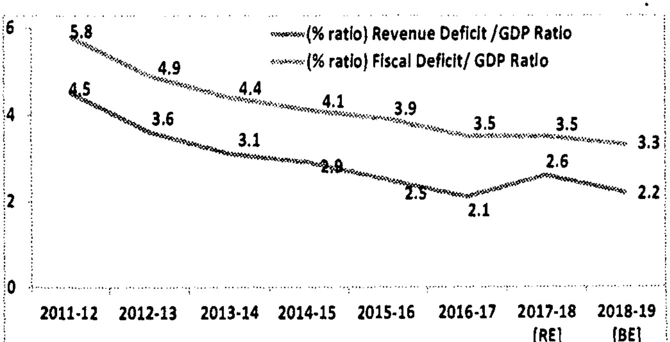
Thus, what is discernible are ***the four key pillars*** of the budgetary strategy: first, a special thrust on agriculture and rural economy; second, a concerted package for the MSME sector and alongside the focus on employment generation; third, a continuing drive towards broad-based infrastructure development; and last, efforts towards improvement in investment climate. Each one of these areas has been embellished with separate package of measures and significant incremental budgetary allocations. It, however, needs to be emphasized that for bringing about balanced and sustainable economic resurgence, the budget is not going to be everything. So much more is required to done to bring about Center-States coordination; strengthening the stability of financial system; labor reforms; revamping of the prevailing format of public private partnership [PPP] models for infrastructure developments, *et al.* In this article, we reflect principally on issues concerning the fiscal consolidation and agriculture and rural economy.

The Budgetary Arithmetic – Some Serious Concerns

The success of the budgetary strategy is inextricably linked with how effective –quantitatively and qualitatively – is the management of fiscal consolidation. In the previous budget, the FM had promised to implement the key recommendations of the FRBM Review Committee, which, among other things, recommended the target of fiscal deficit to GDP ratio at 3% for the next three years. Given the urgency of stimulating investment revival during 2017-18, FM justified the imperatives of creating some fiscal space for increased capital expenditure. Hence, he chose to calibrate the reduction in fiscal deficit for 2017-18 at 3.2% of GDP, while remaining committed to achieve 3% target for the following year. It was pointed out that, this would ensure "adherence to fiscal consolidation, without compromising the requirement of public investment". However, this little leeway has in fact led to sizable overstepping of the fiscal deficit from the budgeted figure of Rs.5466 billion to Rs.5948 billion in the revised estimate for 2017-18 or from 3.2% to 3.5% of GDP. As mentioned earlier, shortfall in tax revenues [GST mobilization] and non-tax revenues made the budgetary arithmetic vulnerable.

But what has been even more worrisome is the sharp increase in revenue deficit, which increased from Rs.3212 billion or 1.9% of GDP to Rs.4389 billion or 2.6% of GDP. In effect, it was the revenue expenditure which overshot the budgeted estimates – the adverse variance being as much as 5.8% from Rs.18,369 billion to Rs.19,443 billion. Indeed, capital expenditure contracted from budget estimates of Rs.3098 billion to revised estimates of Rs.2734 billion or by 11.7%. In effect, while requirement of public investment received a cutback, there has been an overwhelming additional burden of revenue expenditure. Thus, not just quantitatively, but even qualitatively budgetary management has been adversely impacted during 2017-18. Nothing of the larger fiscal deficit contributed in anyway to public spending driven capital formation.

Would the budgetary performance improve in 2018-19, as envisaged by the FM in his arithmetic? Evidently, there is no drastic reduction projected in fiscal deficit and revenue deficit ratios as shown the in the following graph. Indeed, we perceive that the fiscal management is now stumbling – and there is some sort of resistance or "ratchet" effect on the process of further fiscal consolidation. The overall key budgetary parameters are set out in the Appendix Table 1. What is obvious therefrom is the promised effort to reverse the trend in both fiscal and revenue deficit ratios and the FM expects this to be achieved through [a] an incremental buoyancy in tax revenues with normalization of GST implementation – the Center's net tax revenues are slated to increase by 16.6% in 2018-19 as against 15.3% in the previous year; [b] a recovery in non-tax revenue collection to 3% from negative 13.5% in the previous year; and [c] a sharp reduction in the growth rate of revenue expenditure to 10.1% from 15% in the previous year. At the same time, the budget proposes to reverse the trend of contraction in capital expenditure – from a fall of 3.9% in 2017-18 to an increase of as much as 9.9% in 2018-19.



Prima facie, the budgetary arithmetic for 2018-19 looks reasonably sound and realistic. It seems that the fiscal slippage caused by GST can be mitigated, if there is further rationalization and streamlining of its implementation going forward. Growth recovery would also help in improving the tax buoyancy, and would be mainly driven by private consumption expenditure and investments. There may not be further significant surge in international crude oil prices upsetting the provisions for some petroleum product subsidies. However, more concerted efforts would be required in curbing the growth of revenue expenditure – and that requires huge administrative and governance reforms. The major worry will invariably be with respect to the proposed step up in capital expenditure. Can this be accomplished? Will an axe fall, as hitherto, on such perceived "discretionary" spending in the absence of tougher alternatives of controlling "pre-emptive and compulsive" revenue expenditure? Also, since the budget has envisaged earnest implementation of several flagship programs – as mentioned before, the National Health Protection Scheme – would it become imperative to make sizeable additional budgetary allocations through supplementary budget during latter part of the financial year? All such issues would make the fiscal scenario remain delicately poised even in the 2018-19!

Equally importantly, given the elevated level of fiscal deficit in 2018-19, there would be inevitable pressures of high market borrowings impinging upon the current market liquidity. As the year progresses, it would also be realistic to expect increased demand for bank credit, especially from the corporate sector and the MSME sector in response to revival of industrial and investment growth, apart from continuing rising credit demand from retail borrowers. The dynamics of "higher fiscal deficit-growth revival-liquidity pressures-inflation" would have implications on RBI's stance on key policy rates, and the overall interest rates scenario. Besides, the key policy rates in the global context are expected to be on a rising curve during 2018, especially in advanced countries like USA and the EU. There are implications too for the exchange rate behaviour of the Indian rupee *vis-à-vis* global currencies. Evidently, there is a stronger probability of the rupee's depreciation, say, with respect to the US$ as compared to its relative stability over the last couple of years. [Please see Appendix Table 2 for our projections for 2018-19] In substance, issues of fiscal governance, as highlighted above, would have considerable relevance when one evaluates budgetary strategy for accelerating economic revival with macro stability.

Agriculture and Rural Economy

As mentioned earlier, from amongst the four pillars of the budgetary strategy, we would prefer to restrict our reflections only on the importance to agriculture and rural economy. Based on the recent experience of India's development process, it is evident that the agricultural GVA [in real terms or at 2011-12 prices] has risen at a modest annual average rate of 2.5% over the five year period ended 2016-17. Indeed, a predominant part of the gains of accelerated overall GDP growth rate in the post-reforms period have eluded this vital sector of the economy – and for variety of reasons, including the failure of agricultural reforms. Consequently, rural distress has been manifest in a variety of ways – unemployment or underemployment; disillusionment about government's commitment to ensuring remunerative minimum support prices [MSP] for farm produce; rising rural indebtedness; and so on.

For decades, Indian planners and policy makers have waxed eloquent that this sector must grow at a long-term annual average rate of at least 4% in real terms to afford fuller employment opportunities and decent living standards for about 50% people directly engaged in farm activities and overall 65% people living in rural areas of our country. It has, therefore, become necessary for the FM to give primacy of focus to agriculture and rural economy in his budgetary strategy. Recalling the NDA government's election manifesto that "farmers should realize at least 50 per cent more than the cost of their produce", the budget promises raising the MSP for agricultural crops accordingly. Further, to strengthen the system of better price realization, several other measures are proposed to be taken, which include creating institutional mechanism to develop appropriate policies and practices for price and demand forecast, use of future and options market, expansion of warehouse depository, etc.

The package of initiatives also cover many other well-meaning measures such as developing avenues for gainful on-farm and non-farm employment for the farmers and landless families; strengthening agricultural marketing infrastructure; evaluating and developing cluster based model for identified agriculture produces, promoting organic farming in big way through Farmer Producer Organizations and Village Producer's Organizations in large clusters; boosting food processing sector through increased budgetary allocations; boosting agri-commodities exports by setting up large number of Mega Food Parks; progressive expansion of agricultural credit through the banking system, etc.

We believe that all such measures *per se* if implemented with "the holistic approach" and fuller commitment of budgetary allocations would have the potential of transforming the rural economy. But what is also urgently called for is the participation of the farming community, especially of their various representative organizations and agricultural experts from across the country. In fact, most of them have been wary about the most crucial part of the budgetary strategy, namely, that budgetary proposal of MSP fails to adhere to the well articulated, and long-pending M S Swaminathan formula. This formula is popularly known as "Cost C2", which means comprehensive cost, including imputed cost of family labor, imputed rent of owned land and imputed interest on owned capital. The government has virtually rejected this formula and instead of Cost C2 plus 50% it has been apparently recalibrated it to exclude imputed rent of owned land and imputed interest on owned capital.

Hence, considerable dismay from the farming community! Of course, one needs to recognize inflationary and budgetary implications of Cost C2 formula, but for all that the government has to create confidence making dialogue mechanism with concerned legitimate interest groups/ organization in coordination with the State governments. Also, there are issues about how effective would be the procurement, storage and distributional operations of agricultural produce at the proposed MSP without honest participation of State governments and concerned departmental undertakings. In this context, we believe that the time is most opportune that on all policy and program matters concerning agriculture and the rural economy, the Central Government should initiate the National Rural Economy Policy Council [NREP Council] on lines of GST Council for bringing about participative and transformational change in the vital aspects of reforms in this sector. Given the fact that agriculture is predominantly a State subject, this becomes eminently desirable and doable proposition within our federal polity.

Concluding Observations

In summing up, the budget 2018-19 cannot be looked at in isolation. Indeed, it is an integral part of vision-mission objectives of the NDA Government as well as of the reforms agenda traversed so far by it, ever since assuming the reins of power in May 2014. Just to recall: the economy has witnessed genuinely powerful – and some game-changing policy reforms – be it demonetization, GST implementation, financial inclusion *a la* Jan Dhan Yojana, comprehensive Direct Benefit Transfer program, Manufacturing India or Insolvency and Bankruptcy Code. Most of these truly mark structural breaks from the past. The latest budget carries this process forward with yet another ambitious flagship program of National

Health Protection Scheme – now popularly called Modicare Policy. The cumulative and composite positive impact of these policy changes cannot be seen in the short-term, but in the framework of medium-term to longer-term perspective, provided of course their committed implementations within a reasonable time-frame.

This budget in a sense is an effort towards consolidation of gains of reforms and removing many of the imbalances in the economic system. One of the major shortcomings hitherto happens to be in agriculture and rural economy, which could be dealt with given the meaningful policy package already announced. Like-wise, promotion of employment generating activities could be stimulated through thrust on MSME sector or more aggressive infrastructure development programs. What, however, is the most worrisome area is strong probability of a failure to rein in fiscal deficit and making a decisive qualitative change in the budgetary management – trimming and fine-tuning of public expenditure, especially the revenue expenditure.

Despite several fault-lines, the economic outlook is going to be more promising, and growth revival would be gaining further momentum in 2018-19. However, areas to watch out are: First, on the international economic front, the winds of global trade wars under the impetus of growing protectionism; international crude oil prices; key interest rates policy stance of advanced countries; and currency rates behavior. Second, on the domestic front, the economic outlook can be vitiated principally by fiscal slippages; pressures on the exchange rate in event of capital flight driven by the hikes in global interest rates; the failure of monsoon; social unrest associated with growing dismay about lack of adequate employment opportunities for new entrants to workforce and rising income and wealth inequalities; etc. All in all, quite promising, but challenging times post the presentation of the Budget 2018-19...

Appendix

Table 1: Key Components of Budgetary Arithmetic

[Rs. Billion]	2016-17 [Actuals]	2017-18 [RE]	2018-19 [BE]	% increase (+)/ decline (-) in	
				2017-18	2018-19
A. Revenue Receipts	13,742	15,054	17,257	+ 9.5	+ 14.6
[i] Tax Revenue	11,014	12,695	14,806	+ 15.3	+ 16.6
[ii] Non-Tax Revenue	2,728	2,360	2,451	- 13.5	+ 3.9
B. Capital Receipts	6,010	7,123	7,165	+ 18.5	+ 0.6
Total Receipts [A+B] = Total Expenditure [C+D]	19,752	22,178	24,422	+ 12.3	+ 10.1
C. Revenue Expenditure	16,906	19,443	21,418	+ 15.0	+ 10.2
D. Capital Expenditure	2,846	2,734	3,004	- 3.9	+ 9. 9
Revenue Deficit [C-A]	3,164	4,389	4,160	+ 38.8	- 5.2
Fiscal Deficit*	5,356	5,948	6,243	+ 11.1	+ 5.0

* Fiscal deficit represents excess of total expenditure over total revenue receipts *plus recoveries of loans & other capital receipts.*

BE = Budget Estimate. RE = Revised Estimate.

Table 2: Key Macro Economic Indicators				
Year-on-Year Growth Rate [%]	2015-16	2016-17	2017-18	2018-19*
1. Real GDP	8.2	7.1	6.6	7.2 – 7.5
2. Real GVA	8.1	7.1	6.4	7.0 – 7.3
3. Agriculture & Allied GVA	2.2	6.3	3.0	4.0 – 4.5
4. Manufacturing GVA	8.6	7.9	5.1	6.8 – 7.5
5. Index of Industrial Production [IIP]	3.3	4.6	4.8	5.5 – 6.0
6. CPI Inflation Rate	4.9	4.5	3.9	4.5 – 4.8
7. WPI Inflation Rate	- 3.7	1.7	2.5	2.5 – 3.0
8. Fiscal Deficit to GDP Ratio	3.9	3.5	3.5	3.3
9. CAD to GDP Ratio	- 1.1	- 0.7	- 1.8	-1.8 to - 2.2
10. Forex Reserves [US$ Bn.]@	360	370	420	410 – 440**
12. Exchange Rate [US$ = Rs.]@	66.86	64.84	65.05	65 – 67@@

Note: All GDP/ GVA growth rates are in real terms – figures are measured at 2011-12 prices. GVA = Gross Value Added; GDP = GVA *plus* Net Taxes on Products; CAD = Current Account Deficit * Most of these are our range bound estimates. @ End-March figures - March 2018 & 2019 are our estimates. *** Lower of the range suggests strong possibility of some flight of capital, while the upper range suggests equally strong prospects of the pull factors driven by the economy's higher growth potential. @@ There is a stronger possibility of rupee depreciation, but an outside chance of moderate appreciation from its current level.

"People must come to accept private enterprise not as a necessary evil, but as an affirmative good".

- Eugene Black
Former President,
World Bank

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