The 2015-2016 Budget: Business as Usual?

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INTRODUCTION
A popular quip goes, "a politician is that person who, when he comes to a fork in the road goes both ways." This contains a significant truth about political decision-making. In an electoral democracy like India moneyed interests wield a large influence on policy. But the vast majority of votes lie with the poor. The former exert great pressures to steer government policy in an anti-people direction. But the latter ensures that extreme steps cannot easily be taken. Government must be at least seen to be taking both forks in the road.

The 2015-2016 budget presented by Finance Minister Mr. Arun Jaitley on February 28 is of this nature. One way of looking at the budget that has been widely reflected in its corporate media coverage is that this is not a "bold," or "courageous" budget. It has not met expectations of "big-bang reforms." Another way of looking at it is that the Narendra Modi government has not been able to move as decisively in the anti-people direction as the corporate sector wished it to. This has surprised some observers given that general elections are several years away. As one pundit observed on TV, every subsequent budget takes the government closer to the next general election and hence pulls it further in the "populist" direction (incidentally, a whole article could be written on how the word "populist" has been skillfully used to cast aspersions and suspicions on any pro-people actions).

But the 2015 budget also negotiates another tension, that between domestic and international capital. In the build up to the budget there was a noticeable tension between what the domestic capitalist class wants and what international finance would have liked to see. Taking into account the sluggish rate of economic growth over the past few years and continued anemic domestic demand, there were corporate voices asking for government to stimulate demand ("not just show us the money, but show us the market" as one put it). There were also domestic capitalists calling for larger investments in infrastructure. On the other hand, the pressure for "fiscal consolidation" continues unabated and international finance would like to see the fiscal deficit reduced as per plan since its financial returns are potentially placed in jeopardy otherwise.

For example, the fiscal deficit target of 3% of GDP has been postponed by one year to be achieved by 2017-18 instead of 2016-2017 (the fiscal deficit targets are 3.9%, 3.5% and 3.0% in FY 2015-16, 2016-17 and 2017-18 respectively). The space created for spending is supposed to go to infrastructure and welfare spending. In the words of the budget documents, "Despite pressure on Union Finances, Government has decided to run welfare

programmes for poor and socially disadvantaged in an unchanged manner." In this respect it is worth nothing that the MGNREGA budget has increased by around 4% from what was actually spent (as opposed to budgeted) on its last year from 32456 crore rupees revised estimate in 2014 to 33700 crore rupees. Of course accounting for inflation this is not necessarily an increase in real terms. Also in continuation with last year's budget, money for Centrally Sponsored Schemes such as MGNREGA will be given to the States to spend.

The budget that has been presented could thus be seen as the product of these three sets of class forces: the working masses, the domestic corporate class (including its middle-class hangers on), and the international financiers. In addition there is the institutional inertia that comes with a large economy like India's. Seen in this context, it is not surprising that the budget is more a continuation of medium-run trends than a radical departure from them.

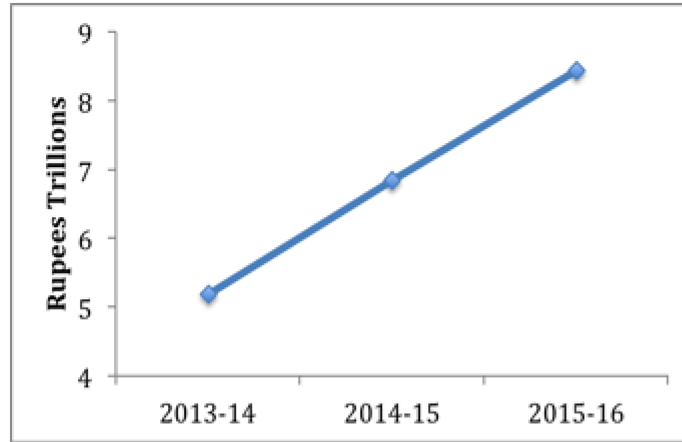
EXPENDITURES

One way in which the budget is substantially different is a result of the implementation of the recommendations of the fourteenth Finance Commission (FFC). This involves the transfer of a much larger proportion of certain revenues to the states. A much-noted feature is thus the jump in States' share of taxes from 32% to 42% of the gross tax revenue. Figure 1 shows that net resources transferred from central revenues to State and UT governments have been increasing steadily. While the spin that the Modi government has been putting on this goes by the name of cooperative federalism, it remains to be seen what the actual impacts will be on the ground. In principle of course, decentralization of finance is to be desired. However, a real danger is that under the guise of decentralization of decision-making states will be forced to compete for domestic and foreign investment. And they obviously have lesser resources to withstand the threat of capital flight than does the Centre. Further, what has occurred is a compositional change. Together with the substantial increase in tax revenues going to the states there has been a big decline in plan assistance to states, and some increase in non-plan assistance. As a result while total transfers to States have grown in absolute terms they remain the same in proportion to total government spending.

A little bit of terminology is useful here. For historical reasons expenditures are categorized in two main categories: plan and non-plan. Plan expenditures, as the name suggests are developed as part of the planning process while non-plan expenditures cover all spending not included in the Plan, such as expenditure that is obligatory in nature (e.g. interest payments, statutory transfers to States) and expenditures on essential functions (e.g. defence, internal security, external affairs). This distinction has lost meaning with the scrapping of the Planning Commission. And may soon disappear.

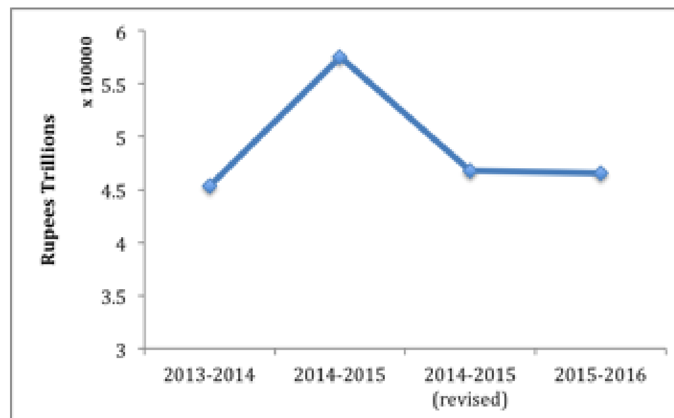
In keeping with the anti-planning view of the present regime, several critical analysts have noted the general reduction in plan spending over the proposed amount last year. In fact the actual amount of spending in this category fell far short of the proposed amount, as Figure 2 shows. When one sees the actual amount of plan spending over the past few years, it seems that it has been stagnant rather than falling, at least in nominal terms.

Figure 1: Net Resources Transferred to State and UT Governments



Source: Resources transferred to State and U.T. Governments (Union Budget 2015-16)

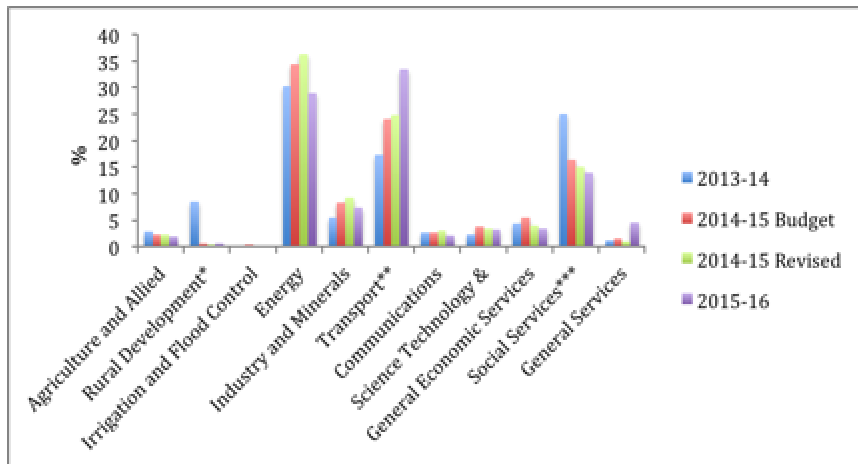
Figure 2: Plan spending (revenue and capital)



Source: Expenditures (Union Budget 2015-16)

However, within the stagnant or slightly declining plan spending, there are big differences in how different sectors have been prioritized. But these differences have largely been inherited from the previous regime, though the present government has put its own stamp on it also. For example, agriculture and rural development were very small parts of plan spending even in last the UPA budget, but the steep decline in social services and increase in transport is a feature of the NDA government (Figure 3). That social sector spending under different heads has been cut sharply can be seen here.

Figure 3: Breakdown of plan spending by sector



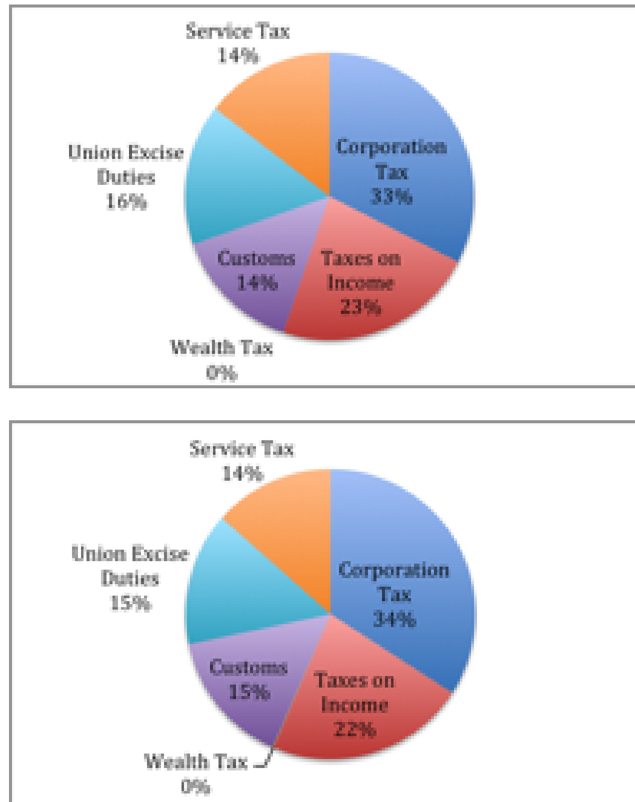
Source: Central Plan Outlay (Union Budget 2015-16)

TAXES

The Indian fisc continues to be plagued with the problem of a narrow tax base further narrowed by tax write-off and evasion at the top of the income distribution. The tax-to-GDP ratio has not grown in the past year. In 2013-14 it stood at 10% of GDP. The target for 2014-15 was 10.6% but the revised estimates show it to be 9.9%. As an article in the Wall Street Journal noted, even today, only about 3% of Indians are subject to an income tax, compared to 20% of Chinese. Total tax revenue as a percentage of GDP is only 10% in India, among the lowest in emerging economies.

But the tax regime is being made more regressive via a proposed cut in corporate taxes and a rise in indirect taxes. The proposed reduction in the corporate tax rate from 30% to 25% over the next four years has had a mixed reception. The fiercely pro-corporate ex-Finance Minister Mr. P. Chidambaram, now in the role of the opposition and hence suddenly concerned about the present government's "pro-corporate tilt," noted in a post-budget press conference that India already has a "competitive" corporate tax rate and that the effective rate is 23% right now. And this is the average effective rate. Breaking down the numbers by firm size shows that smaller firms pay close to the official 30% rate while larger the company the lower the tax rate it ends of paying (see Figure 5). Since one percentage point in corporate taxes represents Rs. 4,000 crore, the government has effectively promised a relief of this amount every year for the next four years to the corporate sector. This combined with the "tax expenditures" (projected revenue foregone due to exemptions) which amounts to Rs. 62398 crore, together this corporate subsidy comes to Rs. 78,398 crore or 32% of the entire subsidy budget for the upcoming year. As before, P. Sainath has analyzed the "Statement of Revenues Foregone" document that lists corporate write-off in detail (link). See point 7 in this Hindu article which has other useful charts and data.

Figure 4: Tax Shares for the upcoming year (top) and revised estimates for 2014-2015 (bottom)



Source: Receipts (Union Budget 2015-16)

Of course, the news media coverage of this is accompanied by Mr. Jaitley's provisio that tax exemptions will be reduced to maintain revenue constant while simplifying the code. On the face of it this may appear reasonable. But really, what else was Mr. Jaitley expected to say? That we are reducing the tax burden of corporations, full stop? Obviously this would be politically difficult given India's already low tax-GDP ratio. So the reduced exemptions sop is to be expected. Whether it will be realized in practice remains to be seen.

Figure 5: Effective corporate tax rates across firm size

Table 1: Profile of sample companies across range of profits before taxes

(Financial Year 2013-14) (Sample size – 564787)

Sl. No.	Profit Before Taxes	Number of Companies	Share in Profits Before Taxes (in %)	Share in Total Income (in %)	Share in Total Corporate Income Tax Payable (in %)	Ratio of Total Income to Profits Before Taxes (in %)	Effective Tax Rate (in %) [Profit to tax ratio]
1.	Less than Zero	228447	0.00	0.48	0.50	-	-
2.	Zero	25624	0.00	2.61	3.98	-	-
3.	₹ 0-1 Crore	278515	2.94	3.76	3.41	88.07	26.89
4.	₹ 1-10 Crore	25613	6.94	8.02	7.72	79.72	25.84
5.	₹ 10-50 Crore	4664	8.99	9.73	9.67	74.63	24.99
6.	₹ 50-100 Crore	853	5.39	5.62	5.63	72.13	24.29
7.	₹ 100-500 Crore	808	15.45	15.60	15.38	69.60	23.11
8.	Greater than ₹ 500 Crore	263	60.29	54.18	53.71	61.96	20.68
9.	**All Companies**	**564787**	**100.00**	**100.00**	**100.00**	**66.83**	**23.22**

1 *The sample size for financial year 2012-13 was 618806.*
2 *The term "total income", in income-tax returns, represents taxable income as would be implied in common parlance.*
3 *Effective tax rate in case of companies is the ratio of total taxes paid [including surcharge and education cess but excluding Dividend Distribution Tax] to the total profits before taxes [PBT] and expressed as a percentage.*
4 *Effective tax rate including dividend distribution tax was 25.47 percent.*
5 *Average statutory tax rate has been worked out taking an average of the tax rate of 32.445% in the case of companies having total income upto ₹ 10 crore and 33.99% in the case of companies having total income exceeding ₹10 crore.*

Source: Statement of Revenues Foregone

BACK TO CONSOLIDATION

Finally, the government has continued the tradition of slashing expenditures to meet fiscal targets. Gross Tax receipts are estimated to be 14,49,490 crore. Devolution to the States is estimated to be 5,23,958 crore. Share of Central Government will be 9,19,842 crore. Non Tax Revenues for the next fiscal year are estimated to be 2,21,733 crore. With the above estimates, fiscal deficit will be 3.9 per cent of GDP. As has happened over the last few years, once again the tax receipts were overestimated (13.6 trillion estimated, 12.5 trillion realized). Hence the fiscal deficit target of 4.1% announced last year is being achieved by spending less than announced in last year's budget (16.8 trillion instead of 17.9 trillion proposed).

Bulk of the reductions (94%) are to plan spending as expected. But slashing spending obviously has limits. So the Fiscal Policy Strategy Document notes that "Given the resource constraint explained above on the revenue side, only option to raise additional resources remains through borrowing…"

As if it were not enough that an insistence on fiscal deficit reduction (itself a symptom of the class interests of international finance as noted above) and corporate giveaways (class interest of domestic and international capital) create a situation where expenditures that would be in the class interest of the working majority have to be cut or kept stagnant, the government also continues to subscribe to the much-criticized "crowding out" theory of public spending. Thus the budget document notes:

> …attempt to raise higher resources from the market [via borrowing] has to be viewed in the larger monetary policy context. Higher Government borrowing will adversely impact private investment and make it difficult for reduction of interest rates. This would adversely affect the revival of growth, which has just started to show positive signs. Therefore, government has decided to continue with the fiscal consolidation phase…

Never mind that investment depends much more on the state of expectations about the future than interest rates in the present. And never mind that there is ample evidence to show that government spending can create conditions for "crowding in" private spending rather than crowding it out.

This is not to suggest that borrowing to bridge the deficit is a class-neutral strategy. Far from it.
At 6 trillion rupees, debt servicing remains a large part of the budget as always (38%). Most of this is domestic debt that the government owes to Indian citizens (external debt now represents only 8.3 percent of total government debt). But this does not change the fact, as we have noted in last year's article on the budget, that in class terms debt servicing represents a transfer of income from tax-payers to bond-holders.

In summary, the best that can be said for the budget is that the pace of anti-people "reforms" has not picked up to the extent that the corporate media was clamouring for. Though in conclusion, going beyond the budget, it is worth pointing out that various executive decisions of the government that have been taken already have been anti-people. For example, the decision to restrict NREGA to only the poorest districts, the decision to cap NREGA fund remittances to the state, the land acquisition ordinance were all take outside the budget. Needless to say these have important consequences on peoples' lives and livelihoods.

I thank Deepankar Basu, Debarshi Das, and Partho Ray for comments.

No Comments »

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