



## ICRA's Comment on Interim Budget for 2009–10

Traditionally, a Vote-On-Account is a sanction of Parliament for withdrawal of money from the Consolidated Fund of India to meet the government's expenses, typically for 2-4 months before a full Budget is presented. Apart from this, the revised estimates of revenue and expenditure during the ongoing financial year are also presented. While there was an expectation that this year's interim budget may go beyond the convention and announce some definitive measures for reviving the economy, given the extraordinary situation that the economy is confronted with, the Finance Minister stuck to convention and did not introduce any of the expected policy measures.

Given the current economic situation, the fiscal deficit was expected to be significantly higher than what had been suggested by the budget estimates for 2008-09 because of the impact of factors such as lower tax collection as a result of the economic slowdown and cuts in tax rates, as well as big-ticket expenditure items including a) the recommendations of the Sixth Central Pay Commission b) impact of the loan waiver for farmers c) subsidy bill on petroleum, food and fertilisers and d) the fiscal stimulus measures announced earlier this year. In light of the economic slowdown, Government of India (GoI) has deviated from its fiscal reform path and the FRBM targets have been relaxed to allow for higher spending as well as to absorb the impact of lower revenue growth in 2008-09 and 2009-10. In addition, the FRBM targets for the States, which were to curtail the overall fiscal deficit to 3.0% of GSDP in 2008-09, have been relaxed to 3.5% of GSDP as a temporary measure.

While non-tax revenues for the Centre for 2008-09 are largely on track, tax revenues are estimated to be nearly 9% lower than budget estimates, clearly reflecting the impact of the economic slowdown. The impact of the cuts in tax rates, including the central excise duties announced in December 2008, is estimated to be nearly Rs. 400 billion, which accounts for two-thirds of the total shortfall in tax revenues.

The revised estimates for 2008-09 also suggest that expenditure has exceeded budget estimates for the current fiscal year by 20%, on account of a 16% increase in plan expenditure and 22% in non plan expenditure. Nearly 40% of the increase in plan expenditure was on account of increased assistance to the States through increased outlays in sectors such as irrigation, roads and bridges etc., which should provide a boost to economic growth. The increase in non plan expenditure through higher salaries and pensions of Government employees after the announcement of the Sixth Central Pay Commission's recommendation as well as the higher releases under the National Rural Employment Guarantee Scheme, which have increased rural incomes, are also expected to provide a boost to domestic demand.

Government of India's Fiscal Deficit			
As a percentage of GDP	2008-09 Budget Estimates	2008-09 Revised Estimates	2009-10 Interim Budget
Revenue Deficit	1.0%	4.4%	4.0%
Fiscal Deficit	2.5%	6.0%	5.5%

As a result of the above factors, the Centre's fiscal deficit is estimated to be around 6% of GDP in 2008-09, significantly higher than the erstwhile targets of 3% as per the FRBM and 2.5% as per the budget estimates. With the States' fiscal deficit expected to be around 3.5% of GSDP in 2008-09, the consolidated deficit for the States and the Centre is likely to be over 9% of GDP. In addition, with the inclusion of off-budget items, the overall deficit figure could well exceed 11% of GDP.

As a direct effect of the global economic meltdown, the growth rate of the Indian economy is expected to decelerate sharply from 9.75% in 2006-07, to 9.0% in 2007-08 and further to 7% as per the Advanced Estimates for 2008-09 released by the Central Statistical Organisation. These growth rate figures do not, however, reveal the extent of demand destruction that has taken place in certain sectors like auto, auto components, housing and real estate, construction and a host of export oriented sectors like Gems and Jewellery and textiles. However, as stated earlier, the Government has largely stuck to the convention and not made any fresh announcements regarding further stimulus apart from an interest subvention scheme for certain export oriented sectors.

While the full budget to be presented later in the year is now expected to announce fiscal measures to boost demand through additional spending, especially plan expenditure, as well as tax cuts, given the current estimate for fiscal deficit for the Centre at 5.5% of GDP, the high deficit level could seriously restrict the ability of the Government to provide further fiscal stimuli through the full budget for 2009-10. With the economic uncertainty and pressing need to pump prime the economy, the new Government will have to grapple with creating a medium term fiscal path that is both sustainable and credible.

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