FISCAL POLICY STRATEGY STATEMENT

A. Fiscal Policy Review

1. In 2015-16 the macroeconomic policy of the Government was aimed at building up on the reforms initiated in the previous year. The policy thrust was aimed at promoting growth revival as well as to foster a stable macroeconomic environment. The reforms initiated in 2014-15 included measures taken towards de-bottlenecking the economy, removing structural constraints, promoting industry and enterprise and enhancing foreign investment inflows. A host of attendant measures were also taken to improve the ease of doing business, improve programme delivery performance including through expansion of direct benefit transfers coverage and deepening the financial inclusion initiatives. These reform initiatives were taken forward during 2015-16.

2. The Indian economy as a consequence of the above mentioned series of measures, has emerged as the fastest growing one amongst the large economies of the world. According to the advanced estimates of the Central Statistics Office, the growth in the GDP at constant market prices in 2015-16 is estimated at 7.6 per cent, which is higher than that of any country of comparable size. The broader macroeconomic conditions have also improved substantially with the continuance of fiscal prudence, lower inflation, lower current account deficit, and robust foreign exchange reserves.

3. Fiscal policy of 2015-16 was designed in the challenging circumstances. The Government needed to complement the macroeconomic objectives of promoting growth and stability even with the reduced fiscal space. This was sought to be achieved by increasing the outlays on infrastructure investments within the available fiscal space, while continuing on the path of fiscal consolidation. In order to achieve this, the Government revised its expenditure policy to consolidate and focus on core developmental schemes. Simultaneously, measures were also taken to enhance the tax and non-tax revenues. The impact of twin measures both on macroeconomic and fiscal fronts, aided by the fall in international crude prices have shown positive results. This is reflected by the higher trends of economic growth and stability along with an improved performance on all fiscal parameters.

4. As observed by the Fourteenth Finance Commission, the Government has taken proactive measures to reduce the existing structural imbalances both on the expenditure and the revenue fronts. On the expenditure side, measures were taken to enhance capital investments and control the growth in non-plan consumptive expenditure. On the receipts side also, measures were taken to enhance both the tax and non-tax revenues so as to counter balance the reduced share in the divisible pool of taxes. The seemingly divergent objectives of continuing on the path of fiscal consolidation alongside reduced fiscal space and need for higher investment expenditures, required a fine balancing act. The fiscal policy of the Government as it turns out, has shown encouraging results.

5. The expenditure policy of the Government in 2015-16 reflects a continuance of the process of expenditure rationalization carried out with substantial correction on the revenue-capital expenditure imbalance. In BE 2015-16, the total expenditure was estimated at 12.6 per cent of GDP compared to 13.3 per cent of GDP in 2014-15. In absolute terms this was a moderate 6.8 per cent increase over the total expenditure in 2014-15. Based on Advanced estimates of GDP the total expenditure has however been revised to 13.2 per cent of GDP in RE 2015-16, attributable largely to revision in the GDP estimates. The actual increase in total expenditure over the budgeted estimates is only Rs.7,914 crore in nominal terms and 0.06 per cent as a ratio of GDP.

6. In the revised estimates for 2015-16, the component of plan expenditure has been marginally enhanced with an increase of 2.6 per cent. The provision for non-plan expenditure is though showing a marginal reduction of 0.3 per cent in the revised estimates against BE 2015-16 provisions. The overall expenditure control has been achieved while accommodating some substantial increase provided during the course of the year provided towards Food Subsidies (₹15,000 crore) and Bank Re-Capitalization (₹19,000 crore). The revenue-capital ratio has also substantially improved in comparison to the previous year. The capital expenditure of the Government has increased from 11.8 per cent of total expenditure in 2014-15 to 13.3 per cent in RE 2015-16, which is the highest since 2007-08.

7. On the tax side, the gross tax revenues of the Centre had been stagnating in the range of 10 per cent of GDP since the last few years. In FY 2014-15,
the gross tax to GDP ratio registered at 9.9 per cent, while in BE 2015-16 it was estimated at 10.3 per cent. The tax policy of 2015-16 was based on a more realistic growth estimation keeping in view the lower tax buoyancy in the previous years. The policy on direct taxes continued to focus on broadening the tax base while maintaining the regime of moderate tax rates. On the Indirect taxes, the underlying theme was to give a boost to domestic manufacture, bring about greater clarity in tax laws, maintaining stable rates and rationalizing the tax structure.

8. In RE 2015-16, the gross tax -GDP ratio is estimated to increase further to 10.8 per cent of GDP. In nominal terms this would mark an increase of 17.2 per cent over 2014-15. This is against the increase of 9.3 per cent achieved in the previous financial year. A substantial increase on the indirect taxes through excise duty helped in not only compensating for the lower direct taxes collections, but also a marginal over achievement on gross tax revenues. However, the significant improvement in gross tax to GDP ratio in RE 2015-16 against the budgeted estimates, is attributable largely to the revised estimates of the GDP for the year. Following marginal increase in gross tax revenues and the enhanced Cess component within that, the net tax revenue to Centre has increased in RE 2015-16.

9. In the context of the lower share of taxes from the divisible pool, the non-tax revenues have become an important source of financing for the Centre. The share of the non-tax revenues now compares with the level of any of the three major indirect taxes. Budget 2015-16 provided for an increase of 12.1 per cent in the non-tax revenues over the actuals of 2014-15. In RE 2015-16, aided with certain policy actions like enhancement of dividend rates to 30 per cent for all public sector enterprises and higher than estimated receipts under the Economic services, it is estimated to register a further increase over the budgeted estimates. The non-tax revenues are estimated to increase by 16.6 per cent over the budgeted estimates in RE 2015-16.

10. Due to higher growths in both tax and non-tax receipts, total revenue receipts of the Centre has been revised upward in RE 2015-16 showing an increase of 5.7 per cent over BE 2015-16. Receipts from disinvestment (including strategic disinvestment) of Government stake in PSUs however continued to be lower than the budgeted estimates. It was budgeted at ₹69,500 crore in 2015-16. However, due to highly uncertain market conditions prevalent for most part of the year, the Government decided to take a more cautious approach and go slow on disinvestments. In RE 2015-16, this target has been revised downwards to ₹25,000 crore.

11. At the end of third quarter of 2015-16 (April-December, 2015) gross tax revenues were 66.5 per cent of budgeted estimates against 58.3 per cent in the corresponding period in the previous year. Similarly, tax revenue (net to the Centre) was 67.6 per cent of budgeted estimates against 55.8 per cent in the corresponding period in the previous year. Realization from non-tax revenues have been much higher during the first three quarters at 81.9 per cent of the budgeted estimates against 69.7 per cent in the previous year. In the light of above performances on revenue side and measures taken for fiscal prudence and expenditure management including subsidy reforms and direct transfer of benefits (DBT) etc. which are underway, it is estimated that the year-end results will show substantial improvements in fiscal peformance over the budgeted targets.

12. To summarize, the fiscal policy of the Government in 2015-16 has shown visible positive results. The trends of fiscal outcomes during the year are showing improvements over the projections made at the BE stage. The capital expenditure of the Government as a percentage of total expenditure and the tax-GDP ratio is likely to be the highest since 2007-08. The non-tax revenues have also increased substantially over the budgeted estimates. The enhanced fiscal space thus created has enabled the Government to adhere to the fiscal deficit target as a ratio of GDP, without the need for resorting to large expenditure cuts. The fiscal policy of the Government has also contributed to support the macroeconomic objectives of promoting growth and stability in the economy. This policy was crucial especially at a time when the private sector investments were slow to come by.

B. Fiscal Policy for 2016-17

13. Fiscal policy of 2016-17 is aimed at continuing the momentum of aiding the growth revival of the economy and institutionalizing the co-operative federal fiscal relations while at the same time continuing on the path of fiscal consolidation. Budget 2016-17 has tried to achieve a fine balance to meet these objectives.

14. The fiscal policy of the Government needs to be guided by the larger macroeconomic needs of higher investments for higher growth. The investment focus is primarily in the agricultural and rural sectors, having substantial potential for higher growth. Higher levels of infrastructural investments particularly in the
During the initial phase of the fiscal year, the government had to face challenges impacting the growth in direct tax collections. On the indirect taxes, excise duty collections are already on a higher base while customs duty collections continue to be impacted by the uncertain global conditions. The higher growth reliance on indirect taxes in 2016-17, will therefore, be primarily on the excise duty and service tax. In the longer term, however, effort will be to augment the gross tax to GDP ratio for sustainability purposes. The likely implementation of GST in the near future will also give a boost to indirect tax collections. Keeping these in view the gross tax to GDP ratio is estimated at 10.8 per cent of GDP in 2016-17 which is the same level as RE 2015-16. The growth in the gross tax revenues is also estimated to come down to 11.7 per cent in 2016-17 as against 17.2 per cent growth estimated in RE 2015-16 over the previous year.

15. On the deficits front, the fiscal policy of the Government in 2016-17 will continue to be guided by the principles of gradual adjustments to achieve the fiscal consolidation targets as laid down in the FRBM Act and Rules. The targeted adjustment on fiscal deficit by 0.4 per cent of GDP in 2016-17, is far steeper than the correction of 0.2 per cent achieved during the current year. It may be seen that fiscal deficit is estimated at 3.5 per cent of GDP in 2016-17 against 3.9 per cent estimated in the current year. The accelerated adjustment on fiscal deficit will help the Government in reducing the debt to GDP ratio at a faster pace. This in turn will help free up more resources out of the Government revenues for developmental programmes and bring down the existing levels of interest payments as a ratio of net revenues of the Centre.

16. In order to achieve the indicated fiscal consolidation and to correct the revenue-expenditure imbalance, the Government focus in 2016-17 is on revenue corrections. However, Government will continue with the process of rationalization in areas having further scope. The focus on DBT including for subsidies has already shown positive results and will be expanded further. More areas of potential savings are being examined and required action will be taken in due course. There is however, limited scope for further expenditure rationalization in view of higher committed components and persistent expenditure rationalization exercise carried out over last few years. The details of the expenditure policy have been brought out subsequently in a separate section.

17. The structural nature of fiscal imbalance requires the focus to be shifted to revenue side corrections. The Government policy on direct taxes has been to achieve growth in direct taxes by broadening the tax base including minimising exemptions, ewhile maintaining a regime of moderate tax rates. The corporate side however continues to face challenges impacting the growth in direct tax collections. On the indirect taxes, excise duty collections are already on a higher base while customs duty collections continue to be impacted by the uncertain global conditions. The higher growth reliance on indirect taxes in 2016-17, will therefore, be primarily on the excise duty and service tax. In the longer term, however, effort will be to augment the gross tax to GDP ratio for sustainability purposes. The likely implementation of GST in the near future will also give a boost to indirect tax collections. Keeping these in view the gross tax to GDP ratio is estimated at 10.8 per cent of GDP in 2016-17 which is the same level as RE 2015-16. The growth in the gross tax revenues is also estimated to come down to 11.7 per cent in 2016-17 as against 17.2 per cent growth estimated in RE 2015-16 over the previous year.

18. Keeping in view the limitations on higher growth on tax side, reliance on revenue side correction in 2016-17 and in the medium term rests primarily on non-tax revenues and non-debt capital receipts, primarily disinvestment and strategic disinvestment receipts. The details are discussed in Part C of this Statement.

(1) Tax Policy

19. Fiscal consolidation strategy rests on two important pillars of gradual increase in tax-GDP ratio and rationalization of expenditure as a percentage of GDP by curtailing non-developmental expenditure. Tax policy of the Government therefore, remains an important tool in achieving the projected goals of fiscal consolidation in the medium term.

20. During the initial phase of the fiscal consolidation period, the tax- GDP ratio had improved significantly from 9.2 per cent in 2003-04 to 11.9 per cent in 2007-08. These gains were substantially lost due to the counter-cyclical stimulus provided largely on the tax side during the global economic crisis. The tax to GDP ratio was stagnating in the range of 10 per cent ever since. In RE 2015-16, the ratio is estimated to improve substantially to 10.8 per cent of GDP. However, keeping in view the already higher base particularly on excise duty, a moderate growth in tax revenues have been projected for 2016-17. The tax to GDP ratio is estimated at the same level of 10.8 per cent. The tax policy of 2016-17 have been brought out in the following paras.

Indirect Taxes

21. The indirect tax collections has shown a turnaround in the current fiscal and are likely to exceed
the 2015-16 Budget Estimate by a healthy margin. Indirect tax collections, during the period April to January of financial year 2015-16 have shown a growth of about 34 per cent over the corresponding period in previous year, partly on account of additional resource mobilization measures taken during 2014 and 2015, and partly on the back of underlying growth in overall economy.

22. With growth in indirect tax collections, the Indirect Tax to GDP ratio for 2015-16 would be about 5.2 per cent, as compared to about 4.4 per cent for 2014-15. This is largely on account of widening of the tax base by comprehensive taxation of all services (except those in the Negative List or otherwise exempt), increase in excise duty on petrol and diesel and pruning of exemptions in Customs, Central Excise and Service Tax. In addition to the above, use of information technology, audits, speedier adjudications, liquidation of arrears, speedy disposal of confiscated/ seized goods etc. has also contributed to the indirect tax revenue collection growth.

23. **Service Tax**

23.1 In the Union Budget, 2015-16 the proposals have been made to increase the indirect tax-GDP ratio by pruning the negative list and withdrawal of certain exemptions with regard to service tax.

23.2 The Service Tax rate was increased from 12 per cent plus Education Cesses to 14 per cent. The ‘Education Cess’ and ‘Secondary and Higher Education Cess’ were subsumed in the revised rate of Service Tax. Thus, effective increase in Service Tax rate was from 12.36 per cent (inclusive of cesses) to 14 per cent. The new Service Tax rate came into effect from 1st June, 2015.

23.3 An enabling provision was made to empower the Central Government to impose a Swachh Bharat Cess on all or any of the taxable services at a rate of 2 per cent of the value of such taxable services with the objective of financing and promoting Swachh Bharat initiatives. This Cess was levied from 15th November, 2015 at the rate of 0.5 per cent on taxable value of all taxable services which were not covered in negative list or were not otherwise exempt.

23.4 Service Tax was levied on the service provided by way of access to amusement facility providing fun or recreation by means of rides, gaming devices or bowling alleys in amusement parks, amusement arcades, water parks, theme parks or such other places.

23.5 Service Tax was levied on service by way of admission to entertainment event of concerts, non-recognized sporting events (commercial sporting events), pageants, music concerts, award functions, if the amount charged is more than ₹500 for right to admission to such an event.

23.6 The entry in the Negative List that covers service by way of any process amounting to manufacture or production of goods was pruned to exclude any service by way of carrying out any processes for production or manufacture of alcoholic liquor for human consumption. Consequently, Service Tax was levied on contract manufacturing/job work for production of potable liquor for a consideration with effect from 1st June, 2015.

23.7 Presently, services provided by the Government or a local authority, excluding certain specified services, are in the Negative List. Service tax was applicable on the “support service” provided by the Government or local authority to a business entity. An enabling provision was made in Finance Act, 2015, to exclude all services provided by the Government or local authority to a business entity from the Negative List. These amendments have been notified and shall come into effect from 01.04.2016. Thus, all services provided by the Government or local authority to a business entity, except the services that are specifically exempted, or covered by any other entry in the Negative List, shall be liable to Service Tax.

23.8 Exemption to construction, erection, commissioning or installation of original works pertaining to an airport or port has been withdrawn. The other exemptions covered under S.No.14 of notification No. 25/12-ST shall continue unchanged.

23.9 Exemptions has been withdrawn on the following services:

- (a) services provided by a mutual fund agent to a mutual fund or assets management company,
- (b) distributor to a mutual fund or AMC,
- (c) selling or marketing agent of lottery ticket to a distributor.

Service tax on these services has been levied on reverse charge basis.

23.10 In Budget 2016-17, some of the measures taken for resource mobilization on the service tax side include:-

- (a) An enabling provision has been made in the Finance Bill, 2016 to levy Cess on all taxable services to finance and promote initiatives to improve agriculture. This cess shall come into force on 1st June, 2016 after enactment of the Finance Bill, 2016.
(b) Exemption on services provided by,-

(i) a senior advocate or a partnership firm of advocates to an advocate or partnership firm of advocates providing legal service; and

(ii) a person represented on an arbitral tribunal to an arbitral tribunal, is being withdrawn; and levy service tax under forward charge

(c) Exemption to construction, erection, commissioning or installation of original works pertaining to monorail or metro, in respect of contracts entered into after 1\textsuperscript{st} March 2016 is being withdrawn.

(d) Exemption to the services of transport of passengers, with or without accompanied belongings, by ropeway, cable car or aerial tramway is being withdrawn.

(e) The Negative List entry that covers ‘service of transportation of passengers, with or without accompanied belongings, by a stage carriage’ is being omitted to levy Service Tax on the services provided by way of transportation of passengers by air conditioned stage carriage only, at the same level of abatement as applicable to the transportation of passengers by a contract carriage i.e. 60 per cent without credit of inputs, input services and capital goods.

23.11 Measures are being taken to boost construction sector, promote affordable housing, promote social security and moving towards a pensioned society. Efforts are also being made to reduce litigation and provide certainty in taxation, ease of doing business, skill development and promote make in India. A number of rationalization measures have also been taken.

24. Customs and Central Excise:

24.1 In order to achieve fiscal consolidation, the following measures are proposed in the Budget 2016-17:

- Clean Energy Cess [being renamed as Clean Environment Cess] levied on coal, lignite and peat is being increased from ₹200 per tonne to ₹400 per tonne.

- Infrastructure Cess @ 4 per cent is being levied on certain specified motor vehicles.

- Excise duty on Aerated waters, lemonade and other waters, containing added sugar or other sweetening matter or flavoured is being increased from 18 per cent to 21 per cent.

- Additional Excise Duty on cigarettes is being increased on non-filter and filter cigarettes of various lengths so that the aggregate of duties of excise on such cigarettes increases by about 10 per cent.

- Specific rates of Excise duty on Cigar and cheroots, Cigarillos, Cigarettes of tobacco substitutes, Cigarillos of tobacco substitutes and other forms of tobacco substitutes is being increased by about 10 per cent.

- Excise duty on Gutkha, chewing tobacco (including filter khaini) and jarda scented tobacco is being increased from 70 per cent to 81 per cent, Excise duty on Unmanufactured tobacco is being increased from 55 per cent to 64 per cent and Excise duty on pan masala is being increased from 16 per cent to 19 per cent. Accordingly, the deemed production and the duty payable per machine per month for each of these tobacco products is being notified.

- Excise duty on Aviation turbine fuel [ATF], other than for supply to aircraft under the Regional Connectivity Scheme, is being increased from 8 per cent to 14 per cent.

- Excise duty of 2 per cent (without CENVAT credit) and 12.5 per cent (with CENVAT credit) is being imposed on branded readymade garments and made up articles of retail sale price of Rs.1000 or more. Also, the tariff value is being increased from 30 per cent of the retail sale price to 60 per cent of the retail sale price.

- Excise duty of 1 per cent (without CENVAT credit) and 12.5 per cent (with CENVAT credit) is being imposed on Articles of Jewellery [excluding silver jewellery, other than studded with diamonds/other precious stones].

- Basic Customs Duty on Cashew nuts in shell is being increased from Nil to 5 per cent.

Direct Taxes

25. The Government policy on direct taxes has been to achieve growth in direct taxes by broadening the tax base while maintaining a regime of moderate tax rates. Tax collection is the product of two factors – tax rates and tax base. There will be no change in; the rate of personal income – tax and the rate of tax for foreign companies in respect of income earned in the financial year 2016-17. However, it is proposed that in the case of domestic companies having total
turnover or gross receipts not exceeding ₹ 5 crore in the financial year 2014-15, the income-tax shall be charged @ 29 per cent. Besides, the domestic companies incorporated on or after 1st March, 2016 and engaged solely in manufacture and production of articles and things, may, at their option, pay tax @ 25 per cent if they do not claim any accelerated depreciation, investment allowance, profit linked deductions and investment linked deductions. All other domestic companies shall be liable to tax @ 30 per cent in respect of income earned in the financial year 2016-17, assessable in the assessment year 2017-18.

26. It is further proposed that surcharge in the case of individuals, HUF, association of persons, body of individuals and artificial persons, shall be increased from 12 per cent to 15 per cent if their total income exceeds ₹1 crore. In all other cases the rate of surcharge shall continue to be the same as in the financial year 2015-16.

27. The widening of tax base to achieve growth in tax collection is a continuous process which involves both legislative as well as administrative measures. The major policy proposals in the Union Budget 2016-17, intended to broaden the tax base and augment revenue, are as under:

- It is proposed to provide for additional chargeability of income exceeding ₹ ten lakh by way of dividend @ 10 per cent in the hands of shareholders being individuals/ HUFs/ firms.

- In order to bring High Value Transactions in tax net & check cash economy, it is proposed to levy Tax Collection at Source (TCS) on purchase of motor vehicles of value exceeding ₹10 lakh and purchase in cash of any goods and services exceeding two lakh rupees.

- To provide equalization levy @ 6 per cent of the amount of consideration for specified services received or receivable by a non-resident not having Permanent Establishment (PE) in India, from a resident in India who carries out business and profession or from a Non-Resident having PE in India.

- To provide that additional tax at maximum marginal rate shall be levied on the accreted income represented by net assets on the date of conversion of a trust or institution from charitable organization to a non-charitable one.

28. The administrative and technological initiatives to augment revenue are as under:

- A non-adversarial and non-intrusive tax regime to enhance ease of doing business is being promoted through modernization of the business processes of tax administration. Extensive use of information technology is being made for e-enablement of tax payer services. Filing of income tax returns, various forms, audit reports, statements of tax deduction at source have been made compatible with electronic filing and computerized processing. Concept of paperless assessment has been introduced on pilot basis in order to minimize human interface of Income-tax department with taxpayer in select Metros. Further, ‘e-sahyog’ initiative has been launched to provide an online mechanism to resolve mismatch without requiring taxpayers to attend the income tax office.

- The e-filing portal of the Department has been very successful where the number of registered users on the portal have gone upto 4.95 crore on 31st December, 2015. Electronic Verification of Returns (EVC) as an alternative to verification by physical submission of signed ITR-V by the taxpayers has been provided where the taxpayer can verify his return through internet banking or AADHAAR based authentication process.

- The non-filers Monitoring System (NMS) is a project undertaken by Income Tax Department to prioritize action on non-filers with potential tax liabilities. Based on specific information available in AIR, CIB data and TDS/ TCS returns, NMS cycle 1(2013), Cycle 2(2014) and Cycle 3(2015) identified 12.19 lakh, 22.09 lakh and 44.07 lakh non-filers, respectively, with potential tax liabilities. The project led to collection of total tax amounting to ₹10,439.11 crore till date.

29. There has been increase in the direct tax collection during the year 2014-15 though at a lower rate compared to 2013-14. The personal income-tax has shown a higher growth as compared to the corporate income-tax. The personal income-tax increased by 9.16 per cent, whereas the corporate income-tax showed a growth of 8.67 per cent.

(2) Expenditure Policy

30. There has been a wide debate within and outside the Government on whether the Government should stick to the fiscal consolidation roadmap or
allow for a relaxation keeping in view the needs of higher levels of public expenditure. However, any attempt to raise fiscal deficit has to be viewed in the larger monetary policy context of impact on policy rates. Keeping in view the negative fallouts of higher Government borrowings on private investments and growth, the Government has decided to stick with the existing fiscal consolidation roadmap.

31. While continuing on the path of fiscal consolidation, the expenditure policy of the Government in 2016-17, reflects a continuance of the policy of expenditure rationalization. The Government has also tried to maintain an optimum balance between the revenue and capital and developmental plan and non-plan components of expenditure. Total expenditure in BE 2016-17 is estimated to grow by 10.8 per cent over RE 2015-16. The plan expenditure within this has been given a higher growth of 15.3 per cent. The details on the revenue-capital correction has already been discussed in the Medium-term Fiscal Policy (MTFP) Statement. Growth in the non-plan revenue component has been controlled despite additional provisions made for implementation of VII Central Pay Commission recommendations and One Rank One Pension (OROP) in Defence Services.

32. On the non-plan side, rationalization of expenditure on major subsidies continues to be critical to achieve the goal of fiscal consolidation. Expenditure on major subsidies with various initiatives in the pipeline, is estimated to reduce to about 1.5 per cent of GDP in 2016-17 compared to 1.7 per cent of GDP in RE 2015-16. Various initiatives of the Government to rationalize expenditure on Major subsidies such as Direct Benefit Transfer (DBT), reforms in LPG subsidies as well as in the fertilizer sector are also underway. It is expected that expenditure on major subsidies as a percentage of GDP will further come down in future.

33. The exercise of rationalization of plan schemes was carried out during the year in consultation with the Ministries/Departments for reducing the number of schemes to a fewer and outcome based umbrella schemes. Further, in the backdrop of the implementation of the recommendations of the 14th Finance Commission, a Sub-Group of Chief Ministers on rationalization of Centrally Sponsored Schemes was constituted by NITI Aayog. Based on its recommendations, the Government has decided that the funding pattern of core of the core schemes will be retained on the existing sharing pattern. The sharing pattern of the core schemes which form part of the National Development Agenda, will be at 60:40 except for 8 North-Eastern and 3 Himalayan States for whom it has been kept at 90:10. All other schemes have been kept in the Optional category with a sharing pattern of 50:50. For the Union Territories, the Centrally Sponsored Schemes will be funded 100 per cent by the Central Government. The Government has also decided that from 2016-17 onwards, the schemes/projects of national importance such as National Aids and STD Control Programme, Pradhan Mantri Kaushal Vikas Yojana, programme with network externalities like Crime and Criminal Control Network will be run as a Central Sector Scheme.

34. In 2015-16, net market borrowings through dated securities at ₹4,56,405 crore were budgeted to finance 82.1 per cent of Gross Fiscal Deficit (GFD). Other sources of financing were treasury bills, external assistance, state provident funds, National Small Savings Fund (NSSF), etc. Total borrowing requirement for 2016-17 has been budgeted at ₹6,00,000 crore. Net market borrowings of ₹4,26,670 crore through dated securities has been budgeted to finance nearly 80 per cent of GFD. A provision of ₹16,649 crore is also made to be realised through treasury bills. Thus, in terms of both the short-term and medium term debt financing, the borrowings strategy during 2016-17 will continue to rely on market oriented domestic sources with external sources financing only ***per cent of the fiscal deficit.

35. Prudent debt management is corner stone of good economic policy. Experience in other part of the world has shown that vulnerability of debt profile to international shocks needs to be closely monitored in emerging global economic order. In India, debt policy is driven by the principle of gradual reduction of public debt to GDP ratio so as to further reduce debt servicing risk and create fiscal space for other/developmental expenditure. The debt policy emphasizes maintaining stable, low cost and prudent debt structure. Further, GoI in consultation with RBI have used market-oriented active debt management since 2013-14 in the form of buyback and switching of shorter tenor G-securities with longer tenors G-securities, with an objective to smoothen redemption pressure, reduce rollover risk as well as utilizing the cash surplus.

36. One of the key features on country’s debt profile is diminishing proportion of external debt as percentage of total liabilities of Central Government, which stands at 6.2 per cent as on March 31, 2015. Further, external borrowing is limited to multilateral/ bilateral loans from select development partners and, thus, not exposed to reversal of capital flows and
insulates the debt portfolio of the Government from volatilities in international capital markets. However, low interest rates in the international financial markets has provided the Government with an option to explore other sources of external debt. The decision to issue foreign currency denominated sovereign bonds cannot be based on cost considerations alone and will need to be assessed in the context of overall savings and investment requirements of the economy.

37. The rollover risk in the Government debt portfolio continues to be low with weighted average maturity of outstanding dated securities remaining close to 10.38 years as on February 29, 2016. This is high compared to international standards. The weighted average yield of dated securities issued during 2015-16 stood at 7.89 per cent as compared to 8.51 per cent during 2014-15, indicating lower yield environment with falling inflation rates. The increased maturity of primary issuances without a substantial increase in borrowings costs also reflects the greater demand for longer tenor securities (by insurance companies and provident funds), which will continue to support the Government efforts to elongate its maturity profile in the medium term.

38. Developing a liquid and vibrant secondary market for Government securities and broadening the investor base are the key factors to ensure that debt is raised in a cost effective manner. Primary issuance strategy of the Government remains focused on issuing new securities under benchmark maturities and building volumes under existing securities to improve liquidity in the secondary market. Broadening of investor base is another key factor in the stability of demand for Government securities. With an objective of having a more predictable regime for investment by the foreign portfolio investors (FPI), RBI, in consultation with the Government, has set out the medium term framework (MTF) for FPI limits in Government securities. Accordingly, FPI investment is expected to increase to 5 per cent of outstanding stock of Government securities by March 2018. Gold Schemes launched by Government of India in November, 2015 has further broadened investment choice and diversified investor base through increased participation of retail investors.

39. The Government is also moving toward alignment of administered interest rates with the market rates. Interest rates on small savings are now linked with yields in secondary market for dated securities.

(4) Contingent liabilities

40. In terms of Article 292 of the Constitution, Central Government gives guarantee for the repayment of borrowings upon the security of the Consolidated Fund of India. The FRBM Rules prescribe a ceiling of 0.5 per cent of GDP for incremental guarantees that the Government can assume in a particular financial year. The Central Government extends guarantees primarily for the purpose of improving viability of projects or activities undertaken by the Government entities with significant social and economic benefits, as well as to fulfill the requirement in cases where sovereign guarantee is a precondition for bilateral/multilateral assistance.

41. FRBM ceiling on guarantees which can be assumed by Government during a financial year has resulted in reduced contingent liability to GDP ratio. The Ratio which stood at 3.3 per cent in 2004-05 is now reduced to 2.73 per cent in 2014-15. The disclosure statement on outstanding Guarantees as prescribed in FRBM Rules, 2004 is appended in the Receipt Budget at Annex 5(iii). During the year 2014-15, net accretion to the stock of guarantees was Rs.41,456.13 crore, amounting to 0.33 per cent of GDP, which is within the limit of 0.5 per cent set under the FRBM Rules.

C. Strategic priorities for ensuing year

42. The fiscal policy strategy on the receipts side in 2016-17, and in the medium term projection period, rests primarily on augmentation of the Centre’s non-tax revenues and non-debt capital receipts. On the non-tax revenues, Budget 2016-17 provides for an increase of 25 per cent over RE 2015-16. As a result, the share of non-tax revenues as a percentage to GDP, is estimated to increase from 1.9 per cent in RE 2015-16 to 2.1 per cent in BE 2016-17. To achieve these targets of NTR, Government has already initiated some measures and others are expected to be implemented during the course of next year.

43. To enhance revenues from dividends, Government has already taken action by making the rate of dividend at 30 per cent applicable for all public sector enterprises. A majority of PSEs which were paying dividend at 20 per cent will now pay 33 per cent higher dividends. Higher dividends can also be taken if they do not have any significant capex plans. Further, with the huge shelf of spectrums due for auction in 2016-17, substantially higher collections from telecom receipts are estimated next year as well as in the medium term. There is also, substantial scope to enhance non-tax revenues through increase in user fees/charges etc. The Government will take measures for optimal rate revisions on products and services provided by the Government and its agencies. The rate revisions will be carried out in consultation with concerned Ministries/Departments, while keeping in consideration the social obligation
needs of the Government. In the medium term therefore, the growth in net revenues of the Centre relies substantially on the enhancement of the non-tax revenues, in particular, through receipts from spectrum auctions. This will provide a cushion till the tax to GDP ratio achieves a higher growth trajectory.

44. ‘Receipts from disinvestment of Government stake in PSUs have been estimated at Rs.56,500 crore in BE 2016-17. This includes Rs.20,500 from strategic sale of assets. It is expected that with likely recovery in the market conditions and new policy to be unveiled soon in this regard, the Government will be able to carry out the targeted disinvestments/sale of assets in 2016-17.

(2) Broad principles underlying expenditure management

45. While Government has managed to control the expenditure through rationalization in the fiscal consolidation phase, quality of expenditure remains an area that needs to be addressed. The ongoing fiscal consolidation has been successful in taming the fiscal deficit; however the public finance on the revenue side requires attention in the view of accomplishment of target set for the revenue deficit and effective revenue deficit under the FRBM regime. This entails structural changes in the Plan spending and definitive measures to contain Non-Plan spending within sustainable limits.

46. The Government has already started the process of outcome based budgeting by creation of two separate verticals of capital expenditure and admin expenditure in every proposed scheme/project so that tangible outcomes and physical progress can be measured. As already explained, a Sub-Group of Chief Ministers on rationalisation of Centrally Sponsored Schemes was constituted by NITI Aayog. Based on its recommendations, the Government has decided that the funding pattern of core schemes viz., Krishi Vikas Yojana, Pradhan Manti Krishi Sinchai Yojana, National Health Mission, ICDS, etc., which form part of National Development Agenda, will be shared 90:10 for 8 North-Eastern and 3 Himalayan States and 60:40 between the Centre and the States. The Government has also decided that from 2016-17 onwards, the schemes/projects of national importance like National Aids and STD Control Programme, Pradhan Mantri Kaushal VikasYojana, programme with network externalities like Crime and Criminal Control Network will be run as a Central Sector Scheme.

47. Widening and deepening of Direct Benefit Transfer (DBT) is another major reform area where cash/benefits are transferred directly in the bank accounts of beneficiaries, cutting several layers in the delivery process. It makes a strategic shift in the subsidy delivery to the citizens of India. DBT envisages achieving accurate targeting of beneficiaries, de-duplication and reduction of fraud, efficiency in delivery process, ensuring greater inclusion, elimination of waste, curbing leakage; and thereby controlling expenditure with greater accountability and transparency. Thus, it intends to reduce subsidy burden on exchequer and improve fiscal management.

48. Direct Benefit Transfers was rolled out in 121 districts for 27 selected Central Sector (CS) and Centrally Sponsored Schemes (CSS) w.e.f. 1.1.2013 in phased manner. DBT in LPG (DBTL) was launched on 1.6.2013. In December, 2014 DBT was extended across the country of 27 schemes and 8 new schemes including MGNREGA (for 300 selected districts) were brought on DBT platform. In February, 2015 DBT was universalized to include all Central Sector/Centrally Sponsored Schemes of all Ministries/Departments, where cash is transferred to individual beneficiaries. In the financial year 2015-16 (upto 31.12.2015), approximately 29.59 crore beneficiaries in various Government schemes were paid Rs.44,035.21 crore through 103.43 crore transactions on DBT platform.

49. ‘PAHAL’ a scheme for direct transfer of LPG subsidy to consumers has also been highly successful in terms of de-duplication, accurate targeting and savings in administrative expenditure. In MGNREGS about 96 per cent of scheme payment is on DBT mode. Cash transfer of Food subsidy is being implemented on pilot basis in Union Territories of Chandigarh and Puducherry. Nine State Governments have come forward to implement DBT in Kerosene in selected districts. With a view to incentivize States/UTs to implement DBT in Kerosene, it has been decided that the States will be given cash incentives of 75 per cent of subsidy savings during the first two years, 50 per cent in the third year and 25 per cent in the fourth year. Implementation of DBT has resulted in streamlining the subsidy regime by simplifying the process, transferring benefits directly in the bank accounts of the beneficiaries, del-duplication and elimination of fake/ghost beneficiaries thus bringing transparency in the system. These initiatives will be further expanded during 2016-17.

Railway Budget

50. Railways Budget is presented separately from the General Budget. However, the earnings and expenditure and all other major financial figures are also incorporated in the General Budget. Government support is provided to Railways in the form of Gross Budgetary Support (GBS) on which dividend is paid every year. The rate of dividend is determined by the
Railways Convention Committee and is presently at 4 per cent. Railway revenues are primarily earned through two major traffic streams, passenger and freight. Some earnings are also contributed by luggage/parcels, commercial utilization of land, siding charges, advertisement and dividend paid by Railways’ PSUs under two categories called ‘other coaching and sundries’. The earnings are utilized to meet the operating expenses called Ordinary Working Expenses (OWE), Depreciation and pensionary charges. The remaining surplus is used to pay dividend and balance is ploughed back as plan investment for meeting safety and development needs of the system.

51. After stabilization of the impact of 6th Central Pay Commission (CPC) and also due to various measures taken including additional resources mobilization through rationalizing the fare and freight tariffs, the financial position of the Railways had started showing signs of improvement. The prime earning segments of Railways i.e., passenger and goods have however not performed on expected lines in 2015-16. While the negative growth in originating passengers witnessed since 2013-14 continues in 2015-16 also, Indian Railways is likely to witness one of the lowest incremental loading in several years. The Operating Ratio in RE 2015-16 is likely to be at 90 per cent. Traditionally the passenger services of railways have been loss making and the under recovery this year is likely to exceed ₹26,000 crore. In the backdrop of the current traffic performance, Indian Railways will also have to bear an additional burden of about ₹30,000 crore towards salary, allowances and pension on account of 7th CPC impact, once implemented.

52. The plan investment in railways is funded through GBS, internal resources and extra budgetary resources (EBR). A Plan outlay of ₹1.21 lakh crore has been envisaged in BE 2016-17 as against investment of ₹1 lakh crore in RE 2015-16 and ₹58,008 crore in Actuals 2014-15. Railways have proposed a five year (2015-2019) investment plan of ₹8.56 lakh crore with special emphasis on network decongestion, network expansion and safety. The plan resources are targeted to be invested judiciously and operationally important projects are being provided assured funding. This will help the railways in not only removing the infrastructure bottlenecks but also augment the revenue earning capacity of the system.

D. Policy Evaluation

53. In 2015-16, the fiscal performance of the Government has been better than estimated on all parameters. This has reinforced the belief in the fiscal policy strategy adopted by the Government, which entailed fiscal consolidation along with corrections on revenue-capital imbalance. Government successfully managed to contain itself within the lower fiscal deficit in nominal terms. In the bargain, the FRBM targets on revenue/effective revenue deficit which appeared insurmountable till recently, now appears to be within the striking range. It is estimated that with the continuance of the policy in 2016-17, the Government will be finally able to achieve all the FRBM targets within the stipulated timeframe of 2017-18.

54. The real GDP growth of 7.6 per cent in 2015-16 despite weak global demand and private investments is indicative of the robustness of the macroeconomic fundamentals. Fiscal policy of the Government in 2016-17, will continue to remain supportive. The enhanced level of public investments targeted in 2016-17 in the major infrastructure sectors of power, railways, highways, rural roads, waterways as well as in other focus areas of drinking water and sanitation, will continue to create a more conducive environment for higher economic growth next year. With a more conducive global economic environment and restoration of the domestic private sector confidence, investments and growth in the Indian economy has the potential to scale new heights.

55. In conclusion, the fiscal outlook for 2016-17, seeks to achieve a much larger consolidation even while providing for substantially higher revenue expenditure requirements on salaries and pensions. However, there are some downside risks. To alleviate these risks, the Government will need to deliver on the initiatives rolled out on non-tax revenues, carry out disinvestments/strategic sale of assets as per the estimated targets and above all, ensure going through with the spectrum auctions, at least in a phased manner.