

PUBLIC FINANCE

The Budget for 1996-97 continued the process of fiscal adjustment within the framework of the Common Minimum Programme (CMP). The budget has envisaged fiscal correction of 0.8 percent point through a reduction in the gross fiscal deficit (GFD) as a proportion of GDP from 5.8 per cent in 1995-96(RE) to 5 per cent in 1996-97 (BE). Also the primary deficit as a proportion of GDP is budgeted to fall to 0.2 per cent of GDP. The other dimension of the gross fiscal adjustment is its quality as reflected in the composition of fiscal adjustment. The compression in the fiscal deficit during the current year has been attempted through a combination of an increase in revenues coupled with reduction in expenditure. Revenue receipts as a proportion of GDP are budgeted to edge upwards from 10.0 per cent in 1995-96 (RE) to 10.4 per cent in 1996-97. On the other hand, revenue expenditure as a proportion of GDP is expected to decline from 13.1 per cent in 1995-96 (RE) to 12.9 per cent in 1996-97 (BE). This is largely on account of containment of non-interest non-plan expenditure.

2. A number of initiatives were taken, to signal government's resolve towards strengthening the infrastructure and social sectors. To provide long term finance for infrastructure sector, the budget announced establishment of an Infrastructure Development Finance Company (IDFC). A budgetary provision of Rs.500 crore has been made for IDFC in the current year. In addition an infusion of Rs.200 crore to strengthen the capital base of the National Highway Authority was also made in the budget. With a view to improve living standards of the rural poor, the budget has provided an additional outlay of Rs.2466 crore as Central assistance for State and UT Plans for certain basic minimum services. This assistance would cover a wide array of social programmes aimed at increasing the provision of safe drinking water, primary education, primary health centres, public housing, mid-day meals, and rural roads. To promote capital formation in the

agricultural sector, the budget has made a provision for additional central assistance, available by way of matching loans to the States for the timely completion of selected irrigation projects.

3. The 1996-97 budget carried tax reforms forward, with a move towards a tax structure which is simple, relies on moderate rates and fewer exemptions. On the import duty side, the basic duty rate on a number of items was reduced to 30 or 40 per cent. Progress was also made in unifying import duty rates on similar items, in order to avoid disputes arising out of mis-classification and multiplicity of rates. On the excise front, the ambit of MODVAT was extended to cover textiles. This would help rationalisation of rate structure and benefit textile industry in general. Excise duty has been reduced on a number of items of daily consumption and many mass consumption goods were added to the exemption list. A mandatory penalty for evasion of excise duty or misuse of MODVAT credit scheme on account of fraud, collusion etc. was also introduced.

4. On the direct taxation front, some significant measures were taken. The effective corporation tax came down further from 46 per cent to 43 per cent as a result of reduction in the rate of surcharge from 15 per cent to 7.5 per cent. A Minimum Alternate Tax has been introduced to bring into the tax net corporations that avoid paying taxes on corporate income or benefit from excessive exemptions. Companies engaged in the power and infrastructure sectors are outside its ambit. The scope of five year tax holiday provision was extended to include investment in irrigation, water supply, sanitation and sewerage system. The long-term capital gains tax for domestic companies was reduced to 20 per cent in line with that for foreign companies so as to provide a level playing field. Furthermore, the scope of long term capital gains tax exemption has been widened to include investment in shares issued by public companies in the priority sectors.

Fiscal and Budgetary Developments in 1995-96

5. The process of fiscal correction, continued more gradually into 1995-96 as is reflected in Table 2.1. The modest compression in the fiscal deficit to 5.8 per cent of GDP in 1995-96 (RE) from 6.1 per cent during 1994-95 was mainly brought about by a significant increase in receipts.

Consumption, Savings and Capital Formation

6. As per the economic classification of the budget (Table 2.3), total expenditure of the Central Government in 1995-96 (RE) rose by 14.7 per cent to Rs.191618 crore from Rs.166998 crore in 1994-95. However, as a ratio of GDP, the total expenditure declined from 17.5 per cent in 1994-95 to 17.4 per cent in 1995-96 (RE). Consumption expenditure in 1995-96(RE) formed 3.8 per cent of GDP and was

TABLE 2.1
Receipts and Expenditure of the Central Government

	1980-81	1990-91	1992-93	1993-94	1994-95	1995-96 (RE)	1996-97 (BE)
	(Rs. crore)						
1. Revenue receipts (2+3)	12419	54954	74128	75453	91082	110191	130345
2. Tax Revenue (net of State's share)	9358	42978	54044	53449	67454	81088	97310
3. Non-Tax Revenue	3061	11976	20084	22004	23628	29103	33035
4. Revenue Expenditure of which	14455	73516	92702	108169	122112	143522	161820
(a) Interest Payments	2604	21498	31075	36741	44060	52000	60000
(b) Subsidies	1851	12158	11995	12864	12982	13726	16320
(c) Defence Expenditure	3604	10874	12109	14978	16426	18835	18854
5. Revenue deficit	2037	18562	18574	32716	31029	33331	31475
6. Capital Receipts of which	7261	38997	36178	55440	68696	65213	67737
(a) Recovery of loans	2104	5712	6356	6191	6345	7411	7048
(b) Other receipts (mainly PSU disinvestment)			1961	-48	5607	1392	5001
7. Capital expenditure	7801	31782	29916	33684	38627	39482	42840
8. Total expenditure of which	22256	105298	122618	141853	160739	183004	204660
(a) Plan expenditure	8994	28365	36660	43662	47378	48684	54685
(b) Non-plan expenditure	13262	76933	85958	98191	113361	134320	149975
9. Fiscal Deficit	7733	44632	40173	60257	57705	64010	62266
	(As per cent of GDP)						
1. Revenue receipts (2+3)	9.1	10.3	10.5	9.3	9.6	10.0	10.4
2. Tax Revenue (net of State's share)	6.9	8.0	7.7	6.6	7.1	7.4	7.8
3. Non-Tax Revenue	2.3	2.2	2.8	2.7	2.5	2.6	2.6
4. Revenue Expenditure of which	10.6	13.7	13.1	13.4	12.8	13.1	12.9
(a) Interest payments	1.9	4.0	4.4	4.5	4.6	4.7	4.8
(b) Subsidies	1.4	2.3	1.7	1.6	1.4	1.2	1.3
(c) Defence expenditure	2.6	2.0	1.7	1.8	1.7	1.7	1.5
5. Revenue deficit	1.5	3.5	2.6	4.0	3.3	3.0	2.5
6. Capital Receipts of which	5.3	7.3	5.1	6.8	7.2	5.9	5.4
(a) Recovery of loans	1.5	1.1	0.9	0.8	0.7	0.7	0.6
(b) Other receipts (mainly PSU disinvestment)			0.3	neg.	0.6	0.1	0.4
7. Capital expenditure	5.7	5.9	4.2	4.2	4.1	3.6	3.4
8. Total expenditure of which	16.4	19.7	17.4	17.5	16.9	16.7	16.3
(a) Plan expenditure	6.6	5.3	5.2	5.4	5.0	4.4	4.4
(b) Non-plan expenditure	9.8	14.4	12.2	12.1	11.9	12.2	12.0
9. Fiscal Deficit	5.7	8.3	5.7	7.4	6.1	5.8	5.0

Note: The figures may not add up to the total because of rounding approximations.

TABLE 2.2
Components of Gross Fiscal Deficit of the Central Government

	1980-81	1990-91	1992-93	1993-94	1994-95	1995-96 (R.E.)	1996-97 (B.E.)
(Rs. crore)							
1. Fiscal Deficit	7733	44632	40173	60257	57705	64010	62266
1.1. Interest Payments	2604	21498	31075	36741	44060	52000	60000
1.2. Primary Deficit	5129	23134	9098	23516	13645	12010	2266
1.21 Primary deficit Consumption	1310	6358	979	12004	3983	1429	-4581
1.22 Primary deficit Investment	3819	16776	8119	11512	9662	10581	6847
(As per cent of GDP)							
1. Fiscal Deficit	5.7	8.3	5.7	7.4	6.1	5.8	5.0
1.1. Interest Payments	1.9	4.0	4.4	4.5	4.6	4.7	4.8
1.2. Primary Deficit	3.8	4.3	1.3	2.9	1.4	1.1	0.2
1.21 Primary deficit Consumption	1.0	1.2	0.1	1.5	0.4	0.1	-0.4
1.22 Primary deficit Investment	2.8	3.1	1.2	1.4	1.0	1.0	0.5
Memorandum Items							
(a) Interest Receipts	1795	8730	12487	15078	15797	18369	21393
(b) Dividend and Profit	82	564	993	951	1216	1729	2551
Note: 1. Primary deficit consumption = Revenue Deficit - Interest payments + Interest receipts + dividend & profits 2. Primary deficit investment = Capital expenditure - Interest receipts - Dividend & profit - recovery of loans - other receipts							

marginally higher by 0.1 percent point over the preceding year. Current transfer payments as a ratio of GDP were also higher by 0.1 percent point in 1995-96 (RE). The Economic and Functional Classification of the Central Budget shows improvement in gross savings (Table 2.4). Gross dissavings of the Central Government as a proportion of GDP fell to 1.2 per cent in 1995-96 (RE) from 1.5 per cent in 1994-95. Gross capital formation out of budgetary resources, as a proportion of GDP, declined significantly to 5.3 per cent in 1995-96 (RE) from 5.7 per cent in 1994-95. This erosion was the result of a sharp decline in financial assets in 1995-96 (RE). These fell by 0.5 percent point of GDP over the previous year's level. In contrast, gross capital formation in physical assets constituted 1.6 per cent of GDP in 1995-96 (RE), and was up by 0.1 percent point over the same ratio recorded for 1994-95.

7. Gross capital formation financed by budgetary resources increased from Rs.54200 crore in 1994-95 to Rs.58314 crore in 1995-96 (RE). This increase of Rs.4114 crore (as per revised estimates) in 1995-96 represents an increase of 7.6 per cent over the

preceding year. Physical assets grew by about 26.1 per cent compared to a mere growth of 0.9 per cent in financial assets. As a result, the expenditure on physical assets increased from 26.4 per cent of gross capital formation in 1994-95 to 31.0 per cent in 1995-96 (RE).

Government Debt

8. Aggregate internal liabilities of the Central Government increased from Rs. 487682 crore in 1994-95 to Rs. 553276 crore in 1995-96 (RE). However, as a proportion of GDP internal liabilities declined by 0.7 percent point from 51.1 per cent to 50.4 per cent over the same period. The fall in internal liabilities as a proportion of GDP was the result of fall in both the components, viz, internal debt and "other liabilities" as evident in Table 2.5.

9. External liabilities shown in the budget are at the historical rates of exchange. External liabilities at book value increased from Rs. 50929 crore in 1994-95 to Rs 52666 crore in 1995-96 (RE). At historical rates, the ratio of external debt stock to GDP has been on the decline for many years (Table 2.5). The repayment burden of the debt stock is,

TABLE 2.3
Economic Classification of Total Expenditure of Central Government

	1980-81	1990-91	1992-93	1993-94	1994-95	1995-96 (R.E.)	1996-97 (S.E.)
	(Rs. Crore)						
1. Consumption expenditure	5174	22359	26865	31815	34878	41957	48103
2. Transfer payments(Current)	6912	45134	58518	66750	76368	88719	102128
3. Gross capital formation out of budgetary resources	9012	35058	37649	45051	54200	58314	61227
a) Physical assets	1907	8602	11875	12765	14328	18070	18063
b) Financial assets	7105	26456	25774	32286	39872	40244	43164
4. Others	1397	2422	2895	2172	1552	2628	5860
5. Total expenditure	22495	104973	125927	145788	166998	191618	217318
	(As per cent of GDP)						
1. Consumption expenditure	3.8	4.2	3.8	3.9	3.7	3.8	3.8
2. Transfer payments(Current)	5.1	8.4	8.3	8.2	8.0	8.1	8.2
3. Gross capital formation out of budgetary resources	6.6	6.5	5.3	5.6	5.7	5.3	4.9
a) Physical assets	1.4	1.6	1.7	1.6	1.5	1.6	1.4
b) Financial assets	5.2	4.9	3.7	4.0	4.2	3.7	3.4
4. Others	1.0	0.5	0.4	0.3	0.2	0.2	0.5
5. Total expenditure	16.5	19.6	17.8	18.0	17.5	17.4	17.4
	(As per cent of total expenditure)						
1. Consumption expenditure	23.0	21.3	21.3	21.8	20.9	21.9	22.1
2. Transfer payments(Current)	30.7	43.0	46.5	45.8	45.7	46.3	47.0
3. Gross capital formation out of budgetary resources	40.1	33.4	29.9	30.9	32.5	30.4	28.2
a) Physical assets	8.5	8.2	9.4	8.8	8.6	9.4	8.3
b) Financial assets	31.6	25.2	20.5	22.1	23.9	21.0	19.9
4. Others	6.2	2.3	2.3	1.5	0.9	1.4	2.7

however, better measured by valuing the debt stock at exchange rates at the end of the relevant fiscal year. When this is done, external liabilities as a proportion of GDP were much higher. Even these ratios exhibit a fall from 14.9 per cent in 1994-95 to 13.5 per cent in 1995-96(RE). Total liabilities have also declined from 69.0 per cent in end-March, 1994 to 63.9 per cent in end-March, 1996.

Assets

10. The assets of the Central Government essentially consist of physical assets and financial assets. The former are heterogeneous and reflect acquisition of such assets over time at historical prices. Therefore assets do not reflect their current market value. As a percentage of GDP, total assets at 36.0 per cent at end 1995-96 (RE) were lower by 1.9 percent points over the same ratio in 1994-95 (Table 2.7). This erosion in assets, measured as a proportion of GDP, was mainly contributed by economic services which fell by 1.3 percentage points in the capital outlay category in 1995-96 (RE). Another 0.3 percent point each was contributed by loans advanced by the Central Government to

States/UTs and public enterprises. The comparison of assets and liabilities does not reflect current picture since assets are shown at book value. The assets need to be converted into current value, which should be much higher, in order to make the comparison economically valid.

11. Despite the limitation of "book value" approach, it is useful to look at the distribution of assets. At the end of 1995-96 (RE), capital outlay formed 55 per cent of total assets (Table: 2.7). The remaining 45 per cent of Central Government assets were in the form of loans advanced by the Central Government to State governments, public sector enterprises and others. The distribution of loans given by the Central Government reveals that about 73 per cent were accounted by States and UTs Governments and about 26 per cent by public sector enterprises. In recent years there has been a steady increase in the loans to the former at the cost of the latter.

12. Within the capital outlay at book value, the distribution of assets across major functional categories during 1995-96 (RE) reveals that about

TABLE 2.4
Capital Formation by the Central Government and Its Financing

	1980-81	1980-91	1982-93	1993-94	1994-95	1995-96 (RE)	1996-97 (BE)
(Rs.Crore)							
I. Gross capital formation out of budgetary resources of Central Government	9012	35058	37649	45051	54200	58314	61227
(i) Gross capital formation by the Central Government	1907	8602	11875	12765	14328	18070	18063
(ii) Financial assistance for capital formation in the rest of the economy	7105	26456	25774	32286	39872	40244	43164
II. Gross saving of the Central Government	3	-10502	-8401	-20335	-13882	-13638	-10138
III. Gap(I-II)	9009	45560	46050	65386	68082	71952	71365
IV. Draft on other sectors of domestic economy	7339	41794	39812	59319	63463	68776	68095
(i) Domestic capital receipts	4762	30447	27500	48359	62502	61176	61517
(ii) Budgetary deficit	2577	11347	12312	10960	961	7600	6578
V. Draft on foreign savings	1670	3766	6238	6067	4619	3176	3270
(As per cent of GDP)							
I. Gross capital formation out of budgetary resources of Central Government	6.6	6.5	5.3	5.6	5.7	5.3	4.9
(i) Gross capital formation by the Central Government	1.4	1.6	1.7	1.6	1.5	1.6	1.4
(ii) Financial assistance for capital formation in the rest of the economy	5.2	4.9	3.7	4.0	4.2	3.7	3.4
II. Gross saving of the Central Government	0.0	-2.0	-1.2	-2.5	-1.5	-1.2	-0.8
III. Gap(I-II)	6.6	8.5	6.5	8.1	7.1	6.5	5.7
IV. Draft on other sectors of domestic economy	5.4	7.8	5.6	7.4	6.7	6.3	5.4
(i) Domestic capital receipts	3.5	5.7	3.9	6.0	6.6	5.6	4.9
(ii) Budgetary deficit	1.9	2.1	1.7	1.4	0.1	0.7	0.5
V. Draft on foreign savings	1.2	0.7	0.9	0.7	0.5	0.3	0.3
(per cent increase over the previous year)							
I. Gross capital formation out of budgetary resources of Central Government	24.7	6.2	7.1	19.7	20.3	7.6	5.0
Notes: (a) Gross capital formation includes loans given for capital formation on a gross basis. Consequently, domestic capital receipts include loan repayments to the Central Government. (b) Because of the revision in GDP estimates, the ratios given here may differ from those given in the earlier issues of Economic Survey.							

69.3 per cent of the assets were in the economic services, 28.1 per cent in general services and 2.7 per cent in social services. The miniscule share of social services reflects the limited role of the Central Government and the larger role of State Governments in the provision of such services. Economic assets at the end of 1995-96 (RE) were 25.6 per cent of the total marketable liabilities arrived at after netting out the borrowings from the RBI.

Borrowings from RBI need to be excluded since, due to their monetisation, the general public has already incurred the cost in the form of higher inflation. Therefore, it may be stated that at least 25 per cent of the outstanding marketable debt could be retired by selling these assets. However, in reality, the sale of such assets could retire more of the total liabilities depending upon the mode and timings of such sale.

TABLE 2.5
Outstanding Liabilities of the Central Government
At the end of :

	1980-81	1990-91	1992-93	1993-94	1994-95	1995-96 (RE)	1996-97 (BE)
(Rs.Crore)							
1. Internal liabilities	48451	283033	359654	430623	487682	553276	613208
a) Internal Debt	30864	154004	199100	245712	266467	303359	332883
i) Market borrowings	15676	70565	81752	110680	131007	158507	184005
ii) Others	15188	83439	117348	135032	135460	144852	148878
b) Other Internal liabilities	17587	129029	160554	184911	221215	249917	280325
2. External debt(outstanding) ¹	11298	31525	42269	47345	50929	52666	54902
3. Total outstanding liabilities (1+2)	59749	314558	401923	477968	538611	605942	668110
4. Amount due from Pakistan on account of share of pre-partition debt	300	300	300	300	300	300	300
5. Net liabilities (3-4)	59449	314258	401624	477668	538311	605642	667810
(As per cent of GDP)							
1. Internal liabilities	35.6	52.9	50.9	53.2	51.1	50.4	49.1
a) Internal Debt	22.7	28.8	28.2	30.3	27.9	27.6	26.6
i) Market borrowings	11.5	13.2	11.6	13.7	13.7	14.4	14.7
ii) Others	11.2	15.6	16.6	16.7	14.2	13.2	11.9
b) Other Internal liabilities	12.9	24.1	22.7	22.8	23.2	22.7	22.4
2. External debt(outstanding) ¹	8.3	5.4	6.0	5.8	5.3	4.8	4.4
3. Total outstanding liabilities	43.9	58.7	56.9	59.0	56.5	55.2	53.4
Memorandum Items							
External Debt (Rs.crore) ²	13479	66314	120979	127798	142514	148387	
(as per cent of GDP)	9.9	12.4	17.1	15.8	14.9	13.5	
Total outstanding liabilities(adjusted) (as per cent of GDP)	61930	349347	480633	558421	630196	701663	
Outstanding liabilities (Non-RBI) ³ (Rs.crore)	48495	275292	387973	453780	525823	590813	
Outstanding liabilities (Non-RBI) (as per cent of GDP)	35.7	51.4	55.0	56.0	55.1	53.8	
¹ External debt figures represent borrowings by Central Government from external sources and are based on historical rates of exchange. ² Converted at exchange rates at the end of the year. ³ This includes marketable dated securities held by the RBI.							

TABLE 2.6
Interest on the Outstanding liabilities of Central Government

	1980-81	1990-91	1992-93	1993-94	1994-95	1995-96 (RE)	1996-97 (BE)
(Rs.Crore)							
1. Interest on internal liabilities	2373	19664	27546	33017	40034	47101	54726
a) Internal debt	1369	9814	13542	15587	19168	22267	26730
i) Market borrowings	808	6366	8147	9258	13205	15770	19154
ii) Others	561	3448	5395	6329	5963	6497	7576
b) Other Internal liabilities	1004	9850	14004	17430	20866	24834	27996
2. Interest on external debt	231	1834	3529	3724	4026	4899	5274
3. Gross interest payments	2604	21498	31075	36741	44060	52000	60000
4. Net interest payments	809	12768	18587	21679	28252	33631	38607
(Average rate of interest)							
1. Internal liabilities	N.A.	8.2	8.7	9.2	9.3	9.7	9.9
a) Internal debt	N.A.	7.4	7.8	7.8	7.8	8.4	8.8
i) Market borrowings	N.A.	10.2	10.4	11.3	11.9	12.0	12.1
ii) Others	N.A.	4.9	5.7	5.4	4.4	4.8	5.2
b) Other Internal liabilities	N.A.	9.2	9.7	10.9	11.3	11.2	11.2
2. External debt	N.A.	6.5	9.6	8.8	8.5	9.6	10.0
3. Total liabilities	N.A.	8.0	8.8	9.1	9.2	9.7	9.9
Memorandum Items							
(a) Interest on External Debt	231	1863	3578	3794	4026	4899	
(b) Average rate of interest	N.A.	3.4	3.3	3.1	3.1	3.4	

Note : The interest liabilities indicated above are on cash basis and not on accrual basis.

TABLE 2.7
Assets of the Central Government
At the end of :

	1980-81	1990-91	1992-93	1993-94	1994-95	1995-96 (RE)	1996-97 (BE)
(Rs.Crore)							
1. Capital outlay	29162	122016	155291	182410	201499	218164	228865
(a) General services	5951	31023	37607	45024	52168	61202	71289
(b) Social services	1062	3749	4484	4881	5254	5811	6452
(c) Economic services	22149	87244	113200	132505	144077	151151	151124
2. Loans advanced by the Central Government	29837	114724	135672	147466	160329	177789	198528
(a) States and Union Territory Governments	17335	74111	91554	101627	115940	130206	147288
(b) Foreign Governments	261	2103	687	471	466	557	696
(c) Public Sector Enterprises	12040	37877	42639	44517	43046	45987	49350
(d) Government Servants	201	633	792	851	877	1039	1200
3. Total Assets	58999	236740	290963	329876	361828	395953	427393
(As per cent of GDP)							
1. Capital outlay	21.4	22.8	22.0	22.5	21.1	19.9	18.3
(a) General services	4.4	5.8	5.3	5.6	5.5	5.6	5.7
(b) Social services	0.8	0.7	0.6	0.6	0.6	0.5	0.5
(c) Economic services	16.3	16.3	16.0	16.4	15.1	13.8	12.1
2. Loans advanced by the Central Government	21.9	21.4	19.2	18.2	16.8	16.2	15.9
(a) States and Union Territory Govts. Governments	12.7	13.8	13.0	12.6	12.2	11.9	11.8
(b) Foreign Governments	0.2	0.4	0.1	0.1	0.0	0.1	0.1
(c) Public Sector Enterprises	8.9	7.1	6.0	5.5	4.5	4.2	3.9
(d) Government Servants	0.1	0.1	0.1	0.1	0.1	0.1	0.1
3. Total Assets	43.4	44.2	41.2	40.7	37.9	36.0	34.1
(As per cent of total)							
1. Capital outlay	100.00	100.00	100.00	100.00	100.00	100.00	100.00
(a) General services	20.41	25.43	24.22	24.68	25.89	28.05	31.15
(b) Social services	3.64	3.07	2.89	2.68	2.61	2.66	2.82
(c) Economic services	75.95	71.50	72.90	72.64	71.50	69.28	66.03
2. Loans advanced by the Central Government	100.00	100.00	100.00	100.00	100.00	100.00	100.00
(a) States and Union Territory Governments	58.10	64.60	67.48	68.92	72.31	73.24	74.19
(b) Foreign Governments	0.87	1.83	0.51	0.32	0.29	0.31	0.35
(c) Public Sector Enterprises	40.35	33.02	31.43	30.19	26.85	25.87	24.86
(d) Government Servants	0.67	0.55	0.58	0.58	0.55	0.58	0.60

Fiscal and Budgetary Developments in 1996-97

13. The Budget for 1996-97 continued the process of fiscal adjustment within the framework of the Common Minimum Programme (CMP). The budget has envisaged fiscal correction of 0.8 percent point through a reduction in the fiscal deficit as a proportion of GDP from 5.8 per cent in 1995-96 (RE) to 5 per cent in 1996-97 (BE). A number of initiatives have been taken, which signal government's strong commitment towards fulfilling basic minimum needs and rural development, and strengthening of the

infrastructure sector. With a view to improve living standards of the rural poor, the budget has provided an additional outlay of Rs.2466 crore as Central assistance for State and UT Plans for certain basic minimum services. This assistance would cover a wide array of social programmes. They include the provision of safe drinking water, primary education, primary health centres, public housing, mid-day meals, and rural roads. To promote capital formation in the agricultural sector, the budget has enhanced the subsidy limit on small tractors, power tillers, sprinklers and drip irrigation equipment. A provision has been made for additional central

assistance, by way of matching loans to the states for the timely completion of selected irrigation projects. To provide long term finance for infrastructure sector, the budget announced establishment of an Infrastructure Development Finance Company (IDFC) in the current year. A budgetary provision of Rs.500 crore has also been made for IDFC. The budget also made a provision of Rs.200 crore to strengthen the capital base of the National Highway Authority.

14. The key deficit measures viz. gross fiscal deficit (GFD) and primary deficit are budgeted lower, compared not only with the preceding year's level but also to their average levels during the past five years (1991-96) (Table 2.1). The GFD is estimated to decline to 5.0 per cent of GDP in 1996-97, from 5.8 per cent in 1995-96 (RE). Similarly, the revenue deficit as a proportion of GDP is budgeted at 2.5 per cent as against 3.0 per cent in 1995-96 (RE) and 3.1 per cent on an average, during 1991-96. The proposed reduction is quite conspicuous in the case of primary deficit, which is budgeted at 0.2 per cent of GDP as against a 1.1 per cent in 1995-96 (RE) and 1.7 per cent on an average during 1991-96 (Table 2.2).

15. The quality of fiscal adjustment is also important, as it draws attention to the composition of fiscal adjustment. The compression in the fiscal deficit during the current year has been attempted through a combination of an increase in revenues coupled with a reduction in expenditure. Revenue receipts (net) are budgeted to increase by 18.3 per cent during 1996-97. These receipts, as a proportion of GDP, are budgeted to edge upwards from 10.0 per cent in 1995-96 (RE) to 10.4 per cent in 1996-97. Outgo on account of interest payments (Rs 60000 crore), subsidies (Rs 16320 crore) and provision for revision of salaries and pensionary benefits (Rs.4000 crore), has increased. Despite this total revenue expenditure is budgeted to grow at a lower rate of 12.7 per cent compared with 17.5 per cent in 1995-96 (RE). This deceleration in the growth of revenue expenditure has led to a decline in revenue expenditure to GDP ratio from 13.1 per cent in 1995-96 (RE) to 12.9 per cent in 1996-97 (BE) (Table 2.1). This favourable outturn on the expenditure side is largely on account of containment of non-interest non-plan expenditure. The growth of non-interest non-plan expenditure is budgeted at 9.3 per cent during 1996-97, and is less than half of the growth (18.8 per cent) posted during 1995-96 (RE). Consequently, non-interest revenue expenditure as a proportion of GDP is budgeted at a lower level of 8.1 per cent compared to 8.3 per cent in 1995-96 (RE).

Interest Payments

16. The rising interest payments reflect both rising debt and higher interest rates due to financial liberalisation. Interest payments as a proportion of GDP edged upwards from 4.6 per cent in 1994-95 to 4.7 per cent in 1995-96 (RE) (Table 2.1). However, as a proportion of non-plan expenditure, these have recorded a marginal decline of 0.2 percent point from 38.9 per cent in 1994-95 to 38.7 per cent in 1995-96 (RE). Interest payments entail a large claim on public resources, and reduces the government's capacity to spend on social sectors and developmental activities. Interest payments can be reduced either by retiring debt, particularly higher interest bearing debt, or by curbing the growth of new debt.

Budget Deficit

17. The budget deficit, defined as total receipts (revenue and capital) minus total expenditure, both revenue and capital, is estimated to decline from Rs.7600 crore for 1995-96 (RE) to Rs.6578 crore in 1996-97 (BE). In the past, the actual budget deficit has tended to overshoot the budgeted estimate. With a view to constrain the enlargement of the budget deficit, Central Government entered into a formal agreement with the Reserve Bank of India in 1994 to limit its borrowing through ad-hoc treasury bills to a predetermined amount. Past experience in this regard has shown the difficulty of staying below the within-year limit. However, before the system of ad-hoc treasury bills is phased out it is necessary to put in place a better expenditure control mechanism. This would also need a more transparent method of defining and reporting the true budget deficit, including all forms of monetisation. The weekly movements of the budget deficit during the course of 1996-97 are shown in Fig.2.3.

18. The fiscal deficit is defined as the difference between, the revenue receipts (net) plus non-debt capital receipts, and the total expenditure including loans net of repayments. This has also been at higher levels during the course of 1996-97. At the end of June, 1996, the fiscal deficit was Rs. 24718 crore as against Rs. 21157 crore at the end of June, 1995. At the end of September, 1996 it stood at Rs.30908 crore compared with Rs. 28298 crore at the end of same period last year. It increased to Rs. 41347 crore at the end of December, 1996 as against Rs. 37112 crore at the end of December, 1995.

Financing of Gross Fiscal Deficit

19. While fiscal adjustment has sought to limit the quantity of bank borrowing, financial sector reforms have begun to alter the manner in which the Government finances its deficit. There has been a

Figure 2.1

CENTRE'S BUDGETARY DEFICIT

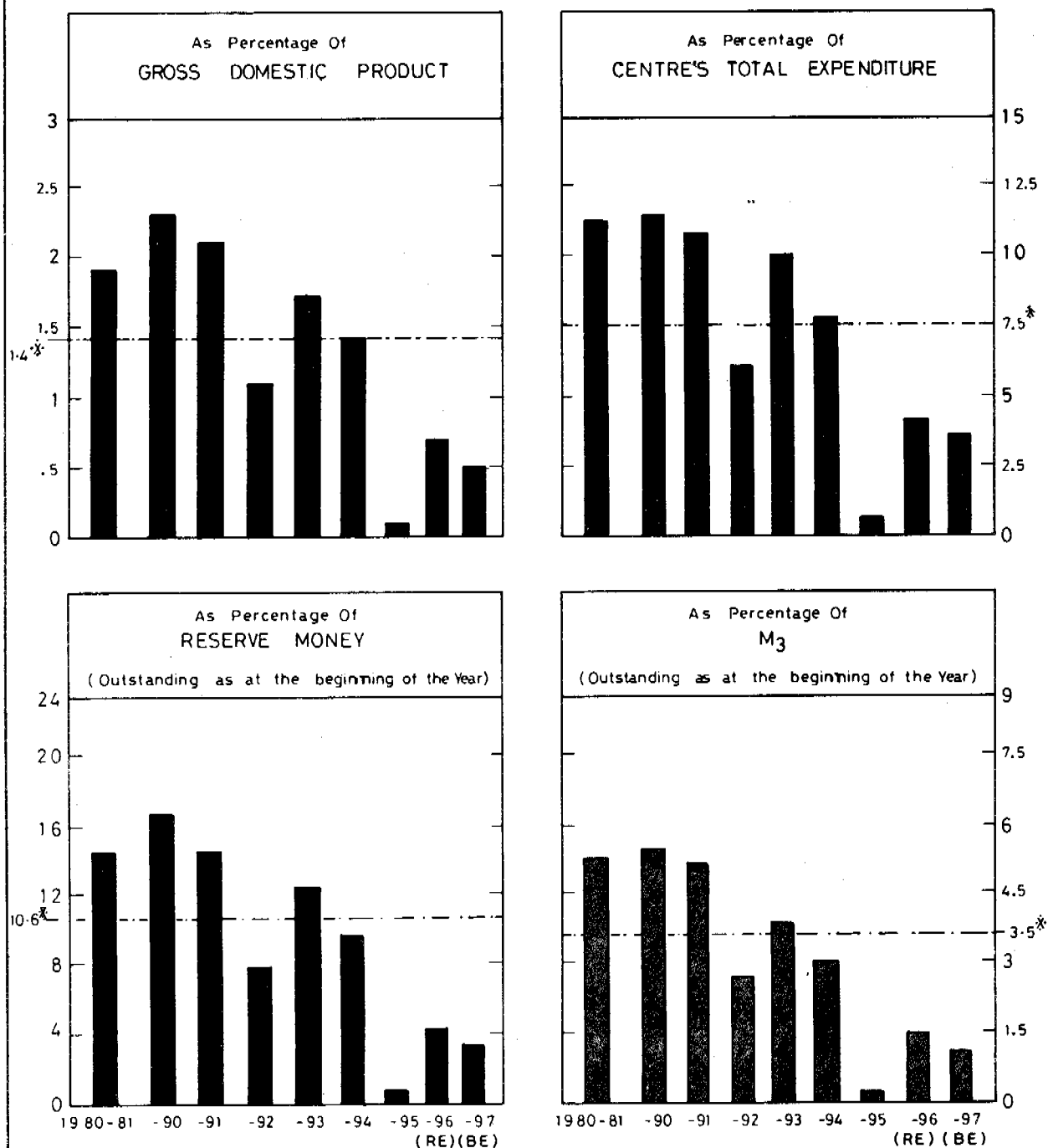


Figure 2.2

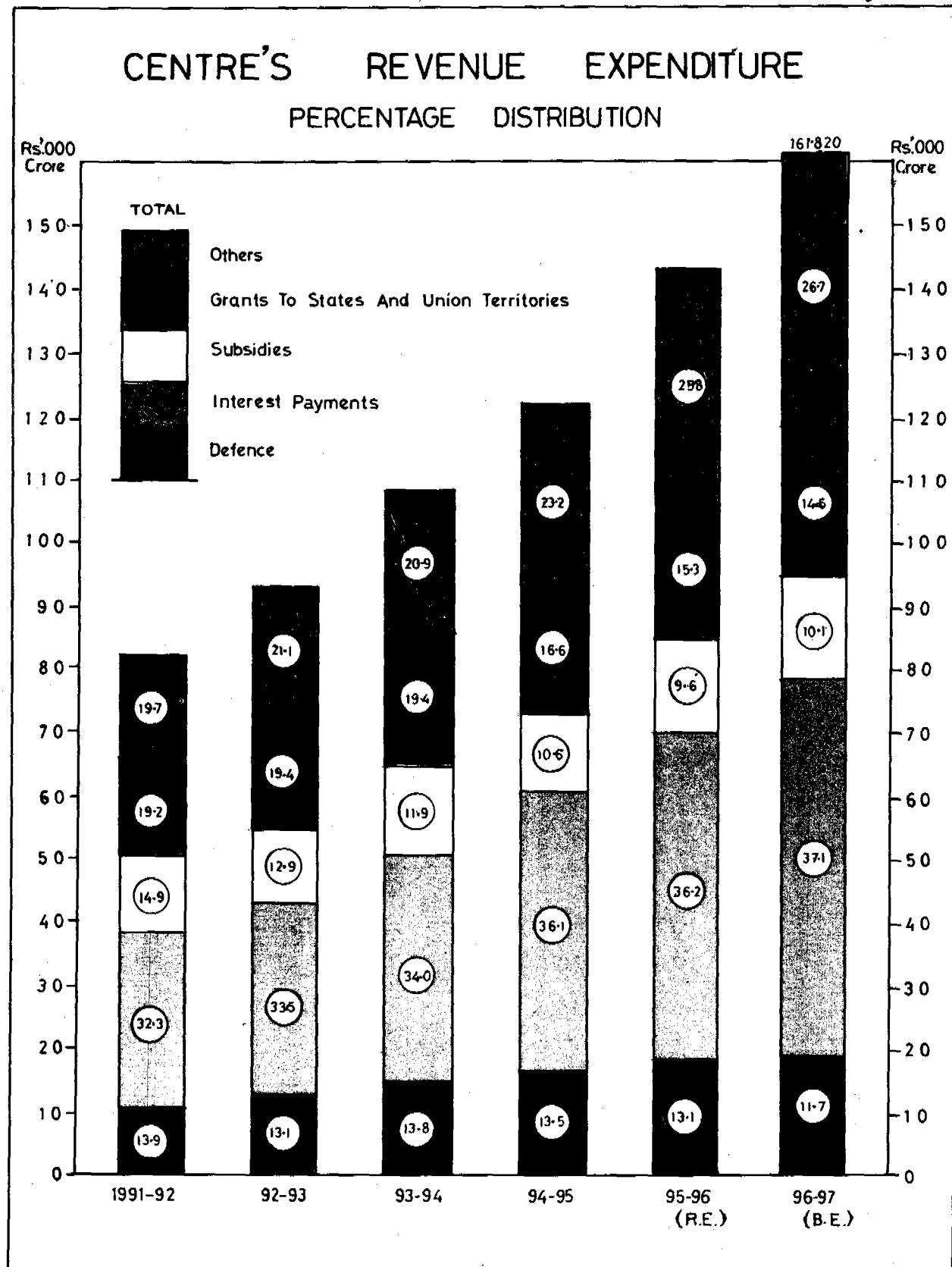


Fig. 2.3

Budgetary Deficit

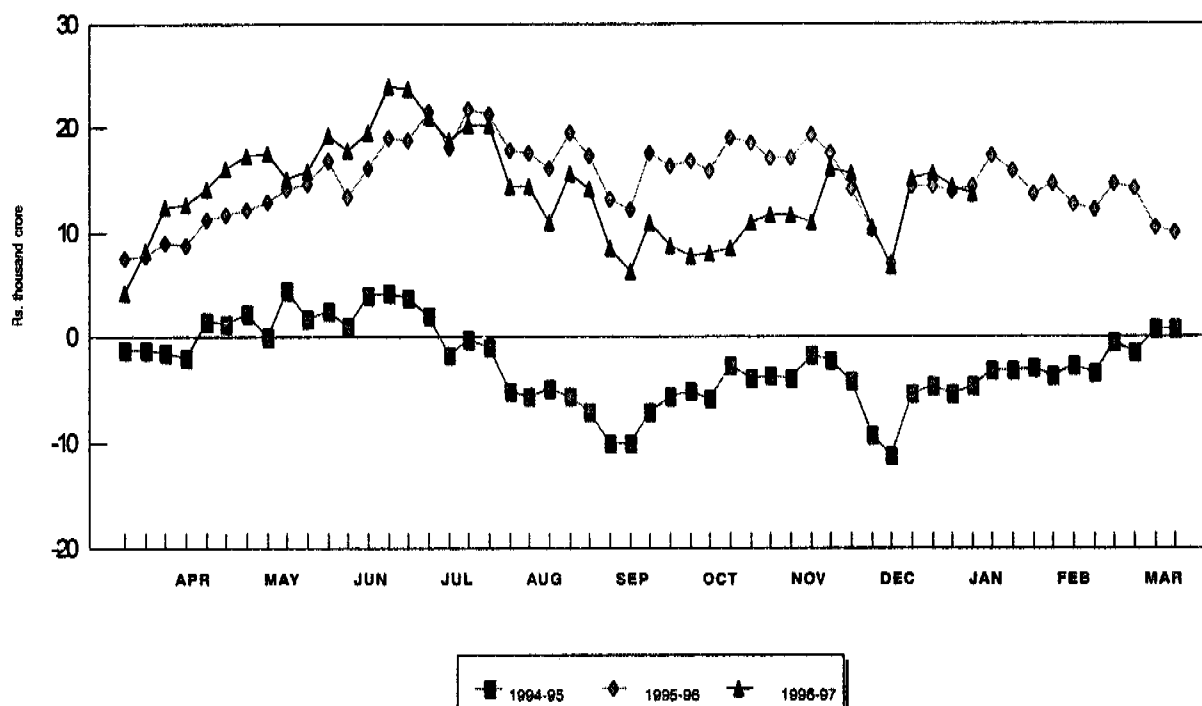


TABLE 2.8

Financing of the Gross Fiscal Deficit

Year	External Finance	Internal Finance			Total	Total Finance/ Gross Fiscal Deficit
		Market Borrowings	Other Liabilities	Budget Deficit		
(Rs. Crore)						
1980-81	1281	2679	1862	2477	7018	8299
1985-86	1449	4884	10209	5315	20408	21857
1989-90	2595	7404	14941	10592	32937	35532
1990-91	3181	8001	22103	11347	41451	44632
1991-92	5421	7510	16538	6855	30903	36324
1992-93	5319	3676	18867	12312	34855	40174
1993-94	5074	28928	15295	10960	55183	60257
1994-95	5146	20326	31271	961	52558	57704
1995-96(RE)	1969	27500	26941	7600	62041	64010
1996-97(BE)	2461	25498	27729	6578	59805	62286
(Percent share in the total)						
1980-81	15.4	32.3	22.4	29.8	84.6	100.0
1985-86	6.6	22.3	46.7	24.3	93.4	100.0
1989-90	7.3	20.8	42.0	29.8	92.7	100.0
1990-91	7.1	17.9	49.5	25.4	92.9	100.0
1991-92	14.9	20.7	45.5	18.9	85.1	100.0
1992-93	13.2	10.5	54.1	35.3	86.8	100.0
1993-94	8.4	52.4	27.7	19.9	91.6	100.0
1994-95	8.9	38.7	59.5	1.8	91.1	100.0
1995-96(RE)	3.1	43.0	42.1	11.9	96.9	100.0
1996-97(BE)	4.0	41.0	44.5	10.6	96.0	100.0

perceptible shift, from captive sources of borrowing at below market rates, towards market related borrowings. The financing pattern of gross fiscal deficit has undergone a compositional shift. The share of market borrowings has increased. It is budgeted to finance 41.0 per cent of Central Government's fiscal deficit in 1996-97 (BE), as against 20.7 per cent in 1991-92. In contrast, the share of the budget deficit has come down from 18.9 per cent in 1991-92 to 10.6 per cent in 1996-97(BE). Similarly the share of external finance in the financing of gross fiscal deficit, is budgeted at 4.0 per cent in 1996-97(BE) down significantly from 14.9 per cent in 1991-92. The share of other liabilities has marginally declined from 45.5 per cent to 44.5 per cent over the same period (Table 2.8).

Savings and Capital Formation

20. Gross dissavings of the Central Government are budgeted to shrink to Rs. 10138 crore in 1996-97 (BE) from Rs.13638 crore in 1995-96 (RE) (Table 2.4). This expected contraction in dissavings by Rs.3500 crore has been contributed by improvement in net profits of the departmental commercial undertakings and a reduction in dissavings on current account. Net profits of departmental undertakings budgeted at Rs.8743 crore in 1996-97(BE) are higher by Rs.1625 crore over 1995-96 (RE) levels. The dissavings on current account budgeted at Rs. 21526 crore are lower by Rs. 1806 crore over 1995-96 (RE) levels. Growth in total expenditure, after being 14.7 per cent in 1995-96 (RE) is expected to moderate to 13.4 per cent during 1996-97. Consequently, total expenditure as a proportion of GDP is budgeted to remain unchanged at 17.4 per cent in 1996-97(BE). However, transfer payments (current) as a proportion of GDP are budgeted to marginally edge upwards to 8.2 per cent in 1996-97 (Table 2.3).

21. Gross capital formation out of budgetary resources (physical plus financial investment of centre) is estimated to decline to 4.9 per cent of GDP in 1996-97 (BE) from 5.3 per cent in 1995-96(RE). This decline in investment seems to be the result of a decline in financial assistance for capital formation as a proportion of GDP from 3.7 per cent in 1995-96 (RE) to 3.4 per cent 1996-97(BE). Similarly, the formation of physical assets as a proportion of GDP, is expected to decline from 1.6 per cent in 1995-96 (RE) to 1.4 per cent in 1996-97 (BE) (Table 2.3).

Government Debt

22. The declining trend in the fiscal deficit have had a salutary impact in the accumulation of aggregate internal liabilities of the Central Government. These are budgeted to increase to Rs. 613208 crore in 1996-97 (BE) from Rs. 553276 crore in 1995-96 (RE) (Table 2.5). This shows moderation in the growth of

aggregate internal liabilities from 13.5 per cent in 1995-96 (RE) to 10.8 per cent for 1996-97(BE). Reflecting this trend, aggregate internal liabilities as a proportion of GDP are budgeted to decline from 50.4 per cent in 1995-96 (RE) to 49.1 per cent in 1996-97(BE). This decline has been brought about by a fall in both internal debt and "other liabilities". As a proportion of GDP, internal debt component is budgeted to fall by 1.0 percentage point from 27.6 per cent in 1995-96(RE) to 26.6 per cent in 1996-97 (BE). Similarly, "other liabilities" as a percentage of GDP are expected to show a modest fall of 0.3 percentage points from 22.7 per cent in 1995-96(RE) to 22.4 per cent in 1996-97(BE).

23. The high level of debt to GDP ratio has entailed significant debt servicing costs. During 1996-97 total debt servicing obligation is budgeted at Rs. 128558 crore comprising Rs. 60000 crore of interest outgo and Rs. 68558 crore towards repayments. The interest payment as a ratio of revenue receipts is budgeted to decline from 47.2 per cent in 1995-96(RE) to 46.0 per cent in 1996-97(BE). Furthermore, in 1996-97 interest outgo absorbed about 37 per cent of total revenue expenditure. Servicing the country's debt puts a large claim on public resources, which reduces the Government's capacity to spend on key infrastructure sectors and social sectors in particular.

Interest Rates

24. The average rate of interest on internal liabilities rose from 9.3 per cent in 1994-95 to 9.7 per cent in 1995-96 (RE). It is budgeted to edge upwards to 9.9 per cent in 1996-97(BE), largely on account of substitution of old lower interest debt by new higher interest bearing debt. Since a large chunk of the outstanding internal liabilities were contracted at very low interest rates, the overall interest rates may firm up in coming years, as these obligations mature and have to be rolled over at current market rates. This may also ultimately lead to convergence of the average rate to the marginal rate. The average rate of interest on external liabilities also hardened from 8.5 per cent in 1994-95 to 9.6 per cent in 1995-96 (RE), and to 10.0 per cent in 1996-97(BE) (Table 2.6). This reflects continued reduction in proportion of soft loans and hardening of international rates in the past.

Supplementary Demand for Grants

25. Supplementary demand for grants for a total amount of Rs.3065 crore was presented in December,1996. The gross expenditure was matched by savings or increased additional receipts of the order Rs.1065 crore. Thus, supplementary demands, entailed a net cash outflow of Rs. 2000 crore. Some of the significant items of expenditure are non-plan defence expenditure of Rs.1200 crore and Rs.650

crore Central plan assistance to the Government of Jammu & Kashmir (towards financing of its plan). Besides, Rs.150 crore is budgeted for additional plan expenditure on the space programme.

Tax Measures

Direct Taxes

Personal Income Tax

26. In budget 1996-97, the Government's objective has been to remain steadfast on the course of economic reforms and liberalisation aimed at accelerating economic growth with social justice. During the past several years the endeavour of the Government has been to increase the revenue without levy of fresh taxes. This has been possible by moderation of the tax rates and rationalisation of the tax system. No new taxes were levied in the 1996-97 budget also, save one.

Rates and Exemptions

27. The trend towards tax rate reduction continued with lowering of the tax rate on the first slab from 20 per cent to 15 per cent. The standard deduction was raised from Rs.15,000 to Rs.18,000 in respect of an employee having a salary income of Rs. 60,000. This has the effect of raising the exemption limit to almost Rs.60,000 in the case of a salaried employee. A salaried employee with an income of Rs.60,000 per annum, making the minimum contribution to his provident fund, will pay no tax at all. In order to simplify and rationalise the tax structure, the distinction between specified HUF and unspecified HUF has been abolished. The rates applicable to individuals will also be now applicable to all Hindu undivided families. Section 80 R, Section 80 RR and Section 80 RRA of the Income Tax Act, provided deduction from total income in respect of foreign exchange earnings from export of services. The admissible deduction was equal to 50 per cent of such income or remuneration or 75 per cent of such remuneration as is brought into India. The deductions under these sections have now been linked to repatriation of foreign exchange. The deduction under sections 80R, 80RR and 80RRA shall now be equal to 75 per cent of the foreign exchange earnings which are brought into India, within a period of six months from the end of the previous year.

Welfare Measures

28. A number of welfare measures were included in the 1996-97 Budget. These can be summarised as follows:

(a) To facilitate charitable contribution, deduction of hundred per cent of donations to the following

funds have been allowed from the taxable income of the donor.

- (i) Funds established by State Governments to provide medical care to the poor.
- (ii) State and National Council of Blood transfusion set up by Ministry of Health and Family welfare.
- (iii) Army Central Welfare Fund, Indian Naval Benevolent Fund and Air Force Central Welfare Fund.
- (iv) The Andhra Pradesh Chief Minister's cyclone Relief Fund, 1996.
- (v) National Illness Assistance Fund.

These provisions will go a long way in ameliorating the condition of the poor and the armed personnel.

(b) As a special consideration for the Senior citizens, the present special tax rebate of 40 per cent which was allowable upto the income level of Rs.100,000 has been extended to the income level of Rs.120,000.

(c) There are certain chronic and protracted diseases such as cancer or AIDS which are not permanently curable, or they take a long time to cure. To help such individuals, a separate deduction of Rs.15000 has been allowed from the income of individuals suffering from such disease. This will also be allowed to any individual or HUF on whom such individuals are dependent.

Saving Incentives

29. The Life Insurance Corporation of India's new personal cum family pension scheme combines welfare with incentives for savings. The scheme is designed to offer attractive terms to its contributors. It particularly envisages life time widow's pension in the unfortunate event of the death of the contributor during the contribution period. The income of any such fund set up by LIC has been exempted from Income Tax. In addition, a deduction upto ten thousand rupees shall be allowed from the income of the contributor to such fund. The limit under Sec.80 D of the Income Tax Act for deduction in respect of any sum paid towards an insurance policy on health of the individual or his family members has been raised from Rs.6000 to Rs.10000.

30. In order to encourage savings and to channelise savings into investment in the priority sector of the economy, long term capital gains have been exempted from tax, if, (a) the net consideration received or accruing from the transfer of the capital asset is invested in specified assets for a period of three years or, (b) if the entire capital gains are

invested in specified assets for a period of seven years. The Income Tax (Second Amendment) Ordinance, 1996 has extended exemptions from long term capital gains tax to cases where the net consideration or amount of capital gains received or accruing from the transfer of the capital asset is reinvested in specified shares of a public company.

31. In the case of self occupied house property, exemption of interest paid on borrowed capital has been enhanced from Rs.10,000/- to Rs.15,000/-. The Act has also extended deduction on account of interest payable on borrowed capital to such persons who are unable to occupy the property by reason of their employment etc., at a place other than where the property is situated.

Corporate Tax

32. Corporate Tax rates have been reduced and simplified over the past few years and the result has been very encouraging. There has been a significant increase in corporate tax collection as a percentage of GDP. The policy of moderation of tax rates has been continued in 1996 by reducing the rate of surcharge on corporate tax from 15 per cent to 7.5 per cent.

33. At the same time, an effort has been made to tackle the phenomenon of zero tax companies having substantial book profits by bringing such companies under "Minimum Alternate Tax" (MAT). This applies where the total income of a company as computed under the Income Tax Act, after availing all eligible deductions, is less than 30 per cent of the book profit. The total income of such companies shall be deemed to be 30 per cent of the book profit (subject to certain adjustments) and shall be charged to tax accordingly. However, the companies in power and infrastructure sector or a sick industrial company or companies located in backward areas entitled to exemption under Section 80 I A, have been kept out of the purview of MAT. The tax under MAT would in reality work out to about 12 per cent only.

34. As a step towards achieving a level playing field, the rate of tax on long term capital gains in the case of domestic companies as well as other resident assesses has been reduced from 30 per cent to 20 per cent.

Strengthening Infrastructure

35. The availability of adequate infrastructure facility is vital for accelerating the economic development of the country. The provisions of 5 years tax holiday available under Sec.80 IA of the Income Tax Act to enterprises engaged in developing, maintaining and operating infrastructure facilities such as roads, highways, bridges, new airports, ports

and rail system have been extended to investment in irrigation, water supply, sanitation and sewerage systems. In order to attract further investment in infrastructure sector, some more tax incentives to investors were provided in the budget for 1996. These incentives are:-

- (a) tax exemption to any income by way of dividends, interest or long-term capital gains of infrastructure capital fund or infrastructure capital company, from investments made by way of shares or long-term finance in any enterprise carrying on the business of developing, maintaining and operating any infrastructure facility.
- (b) tax rebate under section 88 of the Income tax at the rate of 20 per cent of investment made by way of subscription to issue of approved debentures or equity shares of public companies engaged in infrastructure including power sector.
- (c) Tax rebate under section 88 of the Income Tax at the rate of 20 per cent of investment made by way of subscription to units of approved Mutual Funds if the amount of subscription to such units is invested in approved debentures or equity shares of public companies engaged in infrastructure including power sector.
- (d) The eligible amount for tax rebate has been increased from Rs.60,000 to Rs.70,000 for encouraging savings in the sectors specified in (b) and (c) above.

Research and Development

36. Firms in developed countries spend substantial money on scientific research and development activities. The Finance (No. 2) Act 1996 has enacted provisions to boost such activities. To promote research and development activities, the companies engaged in scientific and industrial research have been provided five years tax holiday. The procedure for granting approval to the research projects for claiming the benefit of weighted deduction, equal to one and one fourth times of the amount paid for such projects, has also been simplified.

37. A number of big projects particularly in infrastructure are likely to be undertaken in which assets are financed by a number of assessee and, therefore, each of the participating assessee owns a fraction of the asset. The Finance (No. 2) Act, 1996 has made provision to allow depreciation in respect of fractional ownership of an asset, which was not allowed so far in view of a Supreme Court judgement.

Wealth Tax

38. Wealth tax is leviable on any guest house and any residential house (including a farm house situated within 25 kms of the local limits of any municipality). Commercial properties, other than those used by the assessee wholly and exclusively in their business or profession, were earlier not taken as assets for the purpose of levying wealth tax. Henceforth, only commercial buildings, which are used by the assessee in his business or profession, other than the business of letting out of properties, shall not be subjected to Wealth-tax.

Foreign Investment

39. Concessional treatment is given to non-resident tax payers on income by way of interest, dividend or capital gains from specified bonds and shares. These have to be issued in accordance with a scheme notified by the Central Government and be purchased in foreign currency. Such income is charged to tax at a rate of 10 per cent only. The concessional treatment, has been extended to income by way of interest, dividends or capital gains, on such bonds or shares of a public sector company, which are sold either by the Central Government or by a State Government, to a non-resident assessee in foreign currency.

Rationalisation and Simplification

40. The Government is keen on further simplification of the Income Tax Act. A committee of experts has, therefore, been constituted to rewrite a simpler Act which is easily comprehensible by the tax paying public.

41. The Finance Act has provided that unabsorbed depreciation will be carried forward for a period of eight years only, in the same manner as business losses.

42. Deduction of any sum payable by the assessee as interest on any loan or borrowing from any public financial institution, or a State Financial Corporation or a State Industrial Investment Corporation is allowed in the year in which such interest is actually paid, irrespective of the year in which the liability to pay such sum was incurred. These provisions were enacted, as some assesseees did not pay interest, but claimed the liability on due basis, thus lowering their tax liability also. It has now been provided that deduction of interest on any term loan from a scheduled bank would also be allowed on actual payment.

43. The instrument of Sale and Lease Back (SLB) transactions was used by some tax payers as a tax planning device to reduce their tax liability. There

TABLE 2.9
Sources of Tax Revenue

	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97
Tax Revenue as Percentage of Gross Tax Revenue						
Direct Taxes(a)	22.6	24.3	26.8	29.2	29.5	29.5
Personal tax	10.0	10.6	12.0	13.0	13.7	13.5
Corporation tax	11.7	11.9	13.3	15.0	14.7	14.8
Indirect Taxes(b)	75.5	73.7	71.6	70.6	70.3	70.3
Customs	33.0	31.9	29.3	29.0	32.0	33.6
Excise	41.7	41.3	41.8	40.5	37.2	35.5
Tax Revenue as Percentage of Gross Domestic Product*						
Direct Taxes(a)	2.5	2.6	2.5	2.8	3.0	3.1
Personal tax	1.1	1.1	1.1	1.3	1.4	1.4
Corporation tax	1.3	1.3	1.2	1.4	1.5	1.6
Indirect Taxes(b)	8.3	7.8	6.7	6.8	7.1	7.4
Customs	3.6	3.4	2.7	2.8	3.2	3.5
Excise	4.6	4.4	3.9	3.9	3.7	3.7
Gross tax revenue(c)	10.9	10.6	9.4	9.7	10.0	10.6

* Refers to Gross Domestic product at current market prices. For the year 1996-97, the ratio has been arrived at by estimating the GDP figure. Tax revenue figures for the years 1995-96 and 1996-97 are revised and budget estimates, respectively, and for earlier years these are accounts.

(a): Includes expenditure, interest, wealth, gift taxes & estate duty.

(b): Includes other taxes and duties and service tax; (c): Includes taxes referred in (a) & (b) and taxes of Union Territories.

have also been cases where such SLB transactions have been effected at values much higher than the fair market value of the assets. These loopholes have been plugged by providing that the written down value of the asset in the hands of the lessee, who was the previous owner, will be treated as cost in the hands of the lessor.

44. A number of organisations had been using the "keyman insurance scheme" as a tax planning device, to pass on large sums to their directors and employees etc, apparently without incurring any tax liability. At the same time, the insurance premium is claimed as business expenditure. To plug this loophole, the Income Tax Act has been amended to tax the sum received under such a policy, or in place of the surrender value of such a policy, in the hands of recipient.

45. The tax reforms have resulted in substantial growth in tax revenue. The direct tax revenue, which constituted only 2.1 per cent of GDP in 1990-91, rose to 3.0 per cent in 1995-96. It is further budgeted to rise to 3.1 per cent of GDP in 1996-97. Direct taxes are considered to be the most equitable and efficient form of raising revenue. Also the direct taxes which constituted only 19.1 per cent of the gross tax revenue in 1990-91 rose to 29.5 in 1995-96 and may remain at that level in 1996-97.

Revenue Impact of Reforms

46. The recent trends in direct tax collection show that the decision to reduce rates, simplify and rationalise tax procedures, and thereby encourage compliance, has yielded good results. The reduction in personal and corporate tax rates over the past years have brought a substantial increase in tax collections. Average buoyancy, as measured by the ratio of change in tax revenue to the change in GDP at current prices, has shown substantial improvement. The reduction in personal income tax rates over the assessment years 1991-92 to 1995-96, from the maximum marginal tax rate of 56 per cent on income above Rs.1 lakh, to 40 per cent of income above Rs. 1.2 lakh has not resulted in a reduction in revenue collections. The buoyancy of personal income tax revenues rose from an average of about 1.1 during 1986-87 to 1990-91 to around 1.5 during 1991-92 to 1995-96, and is expected to remain well above unity for the current year as well. Effective corporate tax rates have similarly been reduced, from a peak of 57.5 per cent for certain domestic companies to 43 per cent for all domestic companies having income above Rs. 75,000. Surcharge which was reduced from 15 per cent to 7.5 per cent is not leviable in the case of companies having income below Rs. 75,000 and these are thus taxed at the rate of 40 per cent only. Despite this, the buoyancy has risen from an average of 0.8 during 1986-87 to

1990-91 to 1.6 in 1991-92 to 1995-96. The buoyancy is expected to decline, but may remain well above unity for the current year as well.

Indirect Taxes

Import Duties

47. Government has taken several measures in the last few years to reform the indirect tax structure by reducing the number of rates, removing exemptions and by switching over to ad-valorem rates. On the custom duties side, the objective was to reduce the high rates of import duty gradually, so as to lower the cost of production, improve the competitiveness of domestic industry to face international competition, and benefit domestic consumers through better quality and lower cost goods. This involved reduction in the import duty rate and simplification of the tariff schedule. The unification of rates of similar items has resulted in avoiding anomalies relating to parts and components, reducing classification disputes and promoting investment by reducing its cost.

48. The thrust of import tariff reforms in the budget for 1996-97 was to reduce import duty on raw materials and components used in the employment oriented sectors such as textiles, electronics, and metals. The process of reduction in peak duty rates continued in organic and inorganic chemicals. The rate of duty on similar items have been unified in order to make them effective and to reduce disputes on classification and rates.

Metals

49. Metals, ferrous and non-ferrous, are key inputs in the capital goods industry. In recent years, reduction in import duties on capital goods has been accompanied by duty reduction on metals as well. The magnitude of the import duty reduction in metals has been staggered to provide domestic producers of metals a reasonable transition period to adjust. The duty rate on metals, excepting nickel and aluminium, was reduced from 35 per cent or 40 per cent to 30 per cent. On wrought aluminium and wrought nickel, the duty was reduced from 25 per cent and 30 per cent to a uniform rate of 20 per cent. The duty on stainless steel slabs was brought down from 40 per cent to 20 per cent and on primary forms of stainless steel, other than stainless steel slabs, from 40 per cent to 30 per cent. In addition, duty on stainless steel scrap was reduced from 20 per cent to 10 per cent.

Electronics

50. The electronic industry, which has a substantial potential for exports, employment and development in the small scale sector, has witnessed rapid growth

as a result of sharp reduction in customs duty. The customs duty on specified raw material was reduced from 15 per cent to 10 per cent, on specified components from 25 to 20 per cent, on glass shells for colour TVs from 30 per cent to 25 per cent, on colour picture tubes from 40 per cent to 35 per cent and on computers and computer peripherals from 40 per cent to 20 per cent. Further, the import duty on HDD, FDD and CD-ROM drive was brought down to 10 per cent. These changes in duty for electronics are expected to impart dynamism to the computer industry.

Capital Goods

51. In the 1996-97 budget the import duty on parts and sub-assemblies of telecommunication equipment was reduced from 35 per cent to 30 per cent, and on finished equipment from 50 per cent to 40 per cent. To check the menace of smuggling of cellular phones, pagers and trunking handsets, the duty rates were reduced from 50 per cent to 30 per cent.

52. The import duty regime for medical equipment for the last few years has been gradually simplified. In the 1996-97 budget, import duty on specified medical equipment not generally made in India and parts therefore, was reduced from 15 per cent to 10 per cent, and on other medical equipment from 40 per cent to 30 per cent.

53. Import duty structure on ball or roller bearings of bore diameters of over 60 mm and parts thereof, was revised. They now attract duty at the rate of 10 per cent plus Rs. 80 per kg. Ball or roller bearings of bore diameter up to 60 mm and parts thereof, attract duty at the rate of 10 per cent plus Rs. 150 per kg.

54. The duty rate on signalling and safety equipment for railways, airports etc. was reduced from 50 per cent to 25 per cent. Duty on specified textiles and garment machinery was reduced from 25 to 10 per cent.

Chemicals and Fibres

55. India has become a major producer and exporter of chemicals in the world. Chemicals industry has shown healthy growth in the last two years, partly due to scaling down of import duty on chemicals widely used in the industry. In the budget for 1996-97 import duty on crude oil was reduced from 35 per cent to 25 per cent, and on natural bitumen from 30 per cent to 10 per cent. Besides the peak rate of duty on organic and inorganic chemicals was reduced from 50 per cent to 40 per cent. The duty on certain inorganic chemicals such as caustic soda and soda ash was reduced from 40 per cent to 30 per cent; on iodine from 25 per cent to 10 per cent; on acetic-acid and adipic acid from 40 per cent to 25 per cent; phenol and vinyl pyridine

monomer from 40 per cent to 30 per cent and on methanol from 40 per cent to 30 per cent. The import duty levels on petro-chemicals building blocks like cumene, toluene and cyclo hexane was reduced to a uniform level of 10 per cent.

56. Import duty on artificial and synthetic fibres was brought down to 30 per cent from 40 per cent. Import duties on raw materials and inputs used in the manufacture of synthetic yarns and fibres and fabrics, such as DMT, PTA and MEG was reduced from 35 per cent to 25 per cent, and on nylon filament yarn, polyester filament yarn and viscose filament yarn from existing levels of 45 per cent and 40 per cent to 30 per cent. On certain other chemical intermediates like acrylonitrile, the duty rate was reduced from 20 per cent to 10 per cent, on caprolactum, a basic ingredient for nylon, reduced from 45 to 30 per cent and on rayon grade pulp reduced from 25 per cent to 10 per cent. These changes and rationalisation will improve the competitiveness of the domestic fibre and yarn industry.

57. Import duty on plastic polymers was reduced from 40 to 30 per cent, and on articles of plastic from 50 to 40 per cent.

Other Sectors

58. Customs duty on non-coking coal was reduced from 35 to 20 per cent, and on coke from 25 to 20 per cent. Import duty on specified edible oils was reduced from 30 to 20 per cent.

59. For building infrastructure in the country, special customs duty at the rate of 2 per cent ad-valorem was levied on all imports except those that carry nil rate of duty or are imported at nil rate of customs duty for export production under duty free licences. This levy does not apply to gold and silver imported by eligible passengers or under special import licences.

60. The duty rate on the commonly used veterinary drugs was reduced from 15 per cent to 10 per cent, and peak rate of duty on the alleopathic medicines was reduced from 50 per cent to 40 per cent.

Baggage

61. The import duty rate on baggage beyond threshold limit of Rs.6000 was reduced from 80 per cent to 60 per cent. The restriction on maximum duty free limit of Rs.3,000 for import of VCR/VCP as baggage was removed.

Post Budget Changes

62. In order to give reasonable level of protection to the domestic industry, customs duty of 10 per cent has been imposed on standard newsprint with effect from 29th October, 1996.

TABLE 2.10
Collection Rates for Selected Import Groups

S. No.	COMMODITY GROUP						(In per cent)
		1990-91	1991-92	1992-93	1993-94	1994-95	1995-96 (Prov)
1.	Food products	47	27	12	19	22	23
2.	POL	34	31	31	36	31	30
3.	Chemicals	92	82	71	52	44	44
4.	Man-made fibres	83	63	45	18	18	36
5.	paper & newsprint	24	23	18	13	11	8
6.	Natural fibres	20	21	20	14	9	12
7.	Metals	95	110	97	69	53	52
8.	Capital goods	60	64	53	31	38	33
9.	Others	20	14	13	10	11	13
10.	Non POL	51	49	39	28	29	28
11.	Total	47	44	37	30	29	29
S.No. 1 Includes cereals, pulses, milk and cream, fruits, vegetable and animal fats.							
S.No. 3 Includes chemical elements, compounds, pharmaceuticals, dyeing and colouring materials, plastics and rubber.							
S.No. 5 Includes pulp and waste paper, newsprint, paperboards and manufactures and printed books, newspaper, journals, etc.							
S.No. 6 Includes raw wool and silk.							
S.No. 7 Includes iron and steel and non-ferrous metals.							
S.No. 8 Includes non-electrical machinery and project imports, electrical machinery and transport equipment.							

Collection Rates

63. Collection rates are better indicators of nominal tariff protection than the declared tariff rates. The collection rate is defined as the ratio of realised import revenue (including additional customs duty) to the value of imports of a commodity. Because of numerous exemptions, the declared tariff rate does not reflect the nominal level of protection. The actual incidence of duty is lower than that notified in the tariff schedule.

64. Table 2.10 shows customs duty collection rates during the period 1990-91 through 1995-96. The average collection rate fell when peak rates were reduced from internationally unheard levels of more than 150 per cent. The fall in average collection rates was, however, much less than in the peak rate. Since 1993-94, collection rates have by and large remained unchanged despite further reductions in peak rates. While peak rates have fallen from 80 per cent in 1993-94 to 50 per cent in 1995-96, collection rates fell marginally from 30 per cent to 29 per cent. The drop in the collection rate between the years 1993-94 and 1995-96 encompassed major product groups like petroleum products, metals, paper and news-print and chemicals. The collection rate in case of man-made fibres has doubled, whereas there was only a marginal increase in case of food products, capital goods and other items. The dispersion of rates, as measured by the range between the maximum and the minimum collection rates, though reduced considerably, is still too wide.

This distorts incentives and leads to misallocation of resources.

65. All major product groups barring natural and man-made fibres and food products showed decline in their collection rates during 1995-96 compared with 1994-95. The collection rate for man-made fibres rose from 18 per cent in 1994-95 to 36 per cent in 1995-96. Metals, chemicals and capital goods continue to have high collection rates of the order of 52 per cent, 44 per cent, and 33 per cent respectively. The collection rate for metals at 52 per cent is the highest and 19 percent points higher than the capital goods. This puts capital goods sector at a dis-advantage and possibly bestows negative protection. Paper and newsprint, natural fibres and other category had collection rates ranging between 8 to 13 per cent.

66. In the past few years duty rates have been brought down and a large number of end use exemptions have been removed. With considerable rationalisation in the tariff structure, there is still a need to compress tariff rates further. This would greatly reduce the risk of certain product group sectors suffering from negative protection.

Excise

67. The MODVAT scheme was introduced in 1986 mainly for reducing industrial costs and prices by relieving taxes on inputs, thereby mitigating the cascading effect on the final products. Since 1986, the MODVAT scheme has undergone many changes.

In the 1996-97 budget, the scheme has been extended to the textiles sector by rationalisation of rate structure to help modernisation and revival of the textile industry. Further, invoices issued only by the first and the second stage dealers will be valid documents for availing MODVAT. Mandatory penalty has been introduced for evasion of excise duty or misuse of MODVAT credit scheme on account of fraud, collusion etc.

68. Besides the above changes, duty rates have been reduced on a number of items of daily consumption and more mass consumption items were exempted from excise duty.

Rate reduction and rationalisations

69. The heavy incidence of excise duty on yarn intermediates was brought down to provide relief to the consumers. The excise duty on polyester filament yarn was reduced from 50 per cent to 40 per cent and the rates on other yarns excepting nylon filament yarn and cotton yarn were unified at 20 per cent. For extending MODVAT scheme to the textile sector, basic excise duty of 5 per cent was imposed on cotton fabrics (not containing any other textile material) of value up to Rs.30 per sq.mt. and basic excise duty of 12 per cent was imposed on specified fabrics. The duty rates in case of motor vehicles were significantly rationalised.

70. To make up for the loss on account of reduction in customs duty on crude oil from 35 per cent to 25 per cent, excise duty on all petroleum products excepting LPG and kerosene was revised upward from 10 per cent to 15 per cent.

Duty exemptions and concessions

71. The budget for 1996-97 effected duty reduction on many items of mass and daily consumption: tooth paste from 20 per cent to 10 per cent, detergents from 30 per cent to 25 per cent, glassware made by semi-automatic process from 20 per cent to 10 per cent, on glassware used for table, kitchen etc. from 15 per cent to 10 per cent, instant coffee from 30 per cent to 25 per cent, pan masala from 50 per cent to 40 per cent, ceramic articles other than glazed tiles from 20 per cent to 15 per cent and articles of asbestos cement from 25 per cent to 20 per cent. Further, the duty rate on cartons, boxes and bags made of paper and paperboard was reduced from 20 per cent to 10 per cent. These wide ranging reductions have been carried out to provide relief to the consumers and bring down higher end duty rates in particular.

72. The excise duty on paper and paperboard made from pulp, in which at least 75 per cent of non-conventional raw materials are used was fixed at 5 per cent for initial clearances upto 10000 tonnes in a financial year and 10 per cent for clearances exceeding 10000 tonnes.

73. The benefit of complete exemption from the excise duty was further extended to items of mass consumption such as vanaspati and margarine, vermicelli, tapioca products, animal fats and oils, writing and printing paper supplied to all State Text Book Corporations and spoons, forks, ladles etc. The exemption limit for footwear was raised from Rs.50 to Rs.75 per pair.

Duty Changes/Increases

74. Modest increase in specific duties on cigarettes excepting non-filter cigarettes upto 60 mm in length (called mini cigarettes), ranging from about 5 per cent to 7.5 per cent, was effected. The effective increase in the case of mini cigarettes was 25 per cent. In addition, the scope of service tax has been expanded by bringing advertising services, courier services, and radio paging services under the Service Tax net.

Small scale sector

75. The small scale sector exemption scheme was extended to include copper powder, potassium chlorate and cigarette lighters.

Revenue Performance

76. The data available for principal sources of direct and indirect taxes for the first eight months (April-December, 1996) of the current year show trends which are not as robust as in the corresponding period of the last year. In case of direct taxes, collections from personal income tax and corporation tax at Rs.23827 crore were higher by 11.7 per cent over the same period of 1995. Collections from excise and customs were at Rs.62727 crore during April-December, 1996 and posted a growth of 16.3 per cent.

Tariff Commission

77. Following on the commitment made in the Budget speech of the Finance Minister, Government has decided to constitute an Independent Tariff Commission.

Alternative Scheme of Devolution

78. The Tenth Finance Commission (TFC) had recommended an alternative scheme of devolution for sharing of resources between the Centre and the States. It envisages that 26 per cent of the gross proceeds of all Central taxes (excluding stamp duty, excise duty on medicinal and toilet preparations, central sales tax, consignment tax and surcharge) is to be assigned to the States. This is in lieu of existing share in income tax and basic/special excise duties and grants in lieu of tax on railway passenger fares. In addition, 3 per cent of the gross proceeds of all Central taxes is to be assigned to the States in lieu of existing share in additional excise duties in lieu of sales tax on tobacco, cotton and sugar. The

TFC has proposed that tobacco, cotton, and sugar may continue to be exempt from sales tax and the additional excise duties in lieu of sales tax on these items may be merged with the basic excise duties.

79. These percentages (26 per cent and 3 per cent) are recommended by the TFC to be built into the Constitution of India and frozen for fifteen years. During this fifteen year period, the Finance Commissions will merely recommend the shares of different States devolution and grants-in-aid. Under this dispensation, while all the taxes listed in the Union List will remain Union taxes and the proceeds of no particular tax shall be deemed "divisible", the States will be entitled to a prescribed percentage of tax receipts of the Union. Therefore, while implementing the TFC scheme, the Centre's authority to administer Central taxes will not be affected in any manner.

80. The advantages of the proposed system of vertical resource sharing, in which central taxes are pooled with a proportion of gross receipts devolving to States' are many, and include:

- (1) States will be able to share the aggregate buoyancy of Central taxes.
- (2) The Central Government can pursue tax reforms without the need to consider whether a tax is shareable with the States or not.
- (3) The impact of fluctuations in Central tax revenues would be felt alike by the Central and the State Governments.
- (4) Should the taxes mentioned in Articles 268 and /or 269 form part of this arrangement, there will be a greater likelihood of their being tapped. The net proceeds of the taxes mentioned in Article 269 are assignable to the States, but most of these taxes are not being levied at present. Thus, giving a share in these taxes to the Centre will be an incentive to the Centre to mobilise resources which may benefit States as well.
- (5) A constitutional guarantee of a fixed share in central taxes would be more reassuring for the States than quinquennial pronouncements by the Finance Commission. It will also make for greater stability and certainty of resource flows to the States.
- (6) The divisible pool proposed under the TFC scheme does not include surcharges for the purpose of the Union. Hence it provides some resources for exclusive use by the Centre to meet exigencies and leaves some flexibility with the Union.

81. However, the alternate scheme of devolution is not revenue neutral as it would have entailed additional burden of Rs. 2091 crore on the Centre if it had been put in place as per the budget estimates for 1996-97.

82. In order to achieve revenue neutrality, the percentage share of the States would have to be reduced from the recommended level of 26 per cent and 3 per cent so as to maintain the level of transfers at the existing level in absolute terms. Alternatively, the TFC scheme should be accepted with some modifications. The percentage share of the States should be increased from the recommended level of 26 per cent and 3 per cent, but the increased share should not be merely in lieu of the existing shares in Central taxes, but should be in lieu of all existing transfers on Revenue account. In other words, the fixed percentage of the pooled Central taxes should be frozen for next fifteen years in lieu of all revenue transfers from the Centre to the States. The Plan transfers would then be only on capital account. Both horizontal and vertical distribution amongst the States may be reviewed once in five years.

83. Although TFC scheme appears *prima facie* reasonable and feasible, there can be genuine differences of opinion regarding its overall desirability and its implications for the Centre - State fiscal relations. The TFC scheme does not claim to be a panacea for the problems in Centre-State fiscal relations, but is a distinct improvement over the existing arrangements. It leaves sufficient flexibility to the Centre to mobilise resources for its exclusive use and will facilitate tax reform by removing incentive to favour a particular tax as a means of raising revenue.

Performance of Departmental Enterprises

Railways

84. Railways in recent years has been spurred to augment internal generation of resources through economy in working expenses and enhancing its earnings. The share of its internally generated resources has risen from a mere 25 per cent during the Fifth Plan to 58 per cent during the Eighth Plan. Railways is an important infrastructure sector and a provider of vital non-traded service which has a bearing on the overall competitiveness of the economy. It is, therefore, necessary that a distinction between the network of railway lines, and the railway rolling stock which uses this network to provide transport services is maintained. The high capital intensity and long gestation lags act as disincentives to investment in line networks. This is not, however, applicable to railway service, which can be viable

and competitive. Conventional market borrowing is, therefore, restricted to funding rolling stock which is essential to sustain railway services. This has resulted in raising its liabilities on account of market borrowings through the Indian Railway Finance Corporation (IRFC). The lease charges being payable to IRFC as per budget estimates have already exceeded Rs.1650 crore during 1996-97 and constitutes about 10 per cent of the ordinary working expenses. The resource requirements of Railways are huge and therefore cannot be adequately met through internal generation of resources and conventional market borrowings alone. This calls for greater innovations in management and in funding of assets and services provided by the Railways. A start has been made by allowing private sector participation in selected Railway projects/activities. These include Build-Own-Lease-Transfer (BOLT) and Own-Your-Wagon(OYW) Schemes. These initiatives can inject limited amount of competition in selected areas, and also ease the strain on railway finances.

85. The gross traffic receipts of the Indian Railways increased from Rs.20101 crore in 1994-95 to Rs.22418 crore in 1995-96, representing a growth of 11.5 per cent. In 1995-96, the total working expenses (including appropriations to the Depreciation Reserve Fund and Pension Fund) were Rs.18525 crore as against Rs.16590 crore in the previous year. The working expenses thus showed an increase of 11.7 per cent. Consequently, the net traffic receipts of the Railways have shown an increase from Rs.3511 crore in 1994-95 to Rs.3893 crore in 1995-96. The net railway revenue comprising the net traffic receipts and net miscellaneous receipts, amounted to Rs.4135 crore in 1995-96. The ratio of net revenue to capital-at-charge and investment from capital fund, works out to 15.2 per cent in 1995-96 as compared to 13.7 per cent in 1993-94 and 15.3 per cent in 1994-95. The ordinary working expenses, forming a major part of the total working expenses, registered a higher increase of 13.2 per cent in 1995-96 on account of interim relief, increased PLB cost, and hike in energy charges etc. After making payment of Rs.1264 crore as dividend to general revenues, the excess amounted to Rs.2871 crore, which partly contributed to the investment requirements of the Railways.

86. In 1995-96 Railways contributed Rs.2246 crore to the general exchequer, consisting of payment of dividend of Rs.1264 crore and net accretion of Rs.982 crore to Railway funds kept with the general exchequer. Railways dues of Rs.895 crore remained outstanding against certain State Electricity Boards and power houses as on 31st March, 1996. The inability to settle outstanding financial dues with Railways, bestowed on the recipient of railway services, financial accommodation without payment

of interest. Railways transaction with RBI also closed with a net deposit of Rs.908 crore in 1995-96.

87. The railway budget for 1996-97 envisages a surplus of Rs.1916 crore, after providing for payment of dividend to general revenues in full. The fare and freight rate increases in the railway budget for 1996-97 consisted of the following. Freight rates of all commodities increased by 10 per cent excepting certain essential commodities. Minimum distance for charge raised from 75 kms to 100 kms; no increase in second class fares; upper class and AC 3 tier/ chair car fares raised by 10 per cent; fares of Rajdhani, August Kranti and Shatabdi Express trains also increased by 10 per cent; sleeper class fares increased by 5 per cent for distance beyond 200 kms; parcel and luggage rates rationalised by replacing the existing GPA, CP1 and CP2 by new general parcel scale (GPS), concessional parcel scale (CPS) and modified luggage/motor car scales; and no increase in first and second class monthly season ticket and quarterly season ticket. They are expected to fetch an additional revenue of Rs.927 crore. The plan outlay for railways for 1996-97, the terminal year of the Eighth Five Year Plan, has been budgeted at Rs.8280 crore, including budgetary support of Rs.1419 crore. Market borrowings, BOLT and OYW schemes are expected to fetch an additional Rs.2750 crore. The rest of the plan outlay of Rs.4111 crore is to come from internal resources. In the plan, priority has been accorded to rolling stock, track renewals, safety works and electrification.

Post

88. The gross receipts of the Department of Post during the year 1995-96 were Rs.1150 crore. Gross working expenses were Rs.2472 crore and net working expenses Rs.1810 crore. There was, therefore, a deficit of Rs.660 crore. During the year 1996-97, as per budget estimates, the gross receipts are expected at Rs.1350 crore and gross working expenses at Rs.2616 crore. With net working expenses at Rs.1962 crore the deficit is estimated at Rs.612 crore for 1996-97 (BE).

89. The Budget of the Department of Post has been in deficit continuously over the years, and no dividend is being paid to the general revenue. Modernisation activities, through induction of new technology, has been initiated on a modest scale during the current plan. Its further expansion and spread during the next plan, are likely to improve the service efficiency. A modernised postal system should also be able to provide new value added services to yield revenue. Low tariff on most of the postal services for many years, and inadequate agency charges for agency functions, are the main factors for the deficit. However, a moderate increase in some of the services i.e., printed postcard from

TABLE 2.11
Cost and Revenue of Main Services of the Department of Post

Service	1994-95		1995-96		Subsidy during 1993-94	Subsidy as per cent of cost
	Cost	Revenue	Cost	Revenue		
1. Postcard	1.73	0.15	1.83	0.15	1.68	92
2. Printed card	1.62	0.60	1.74	0.60	1.14	66
3. Letter card	1.78	0.75	1.88	0.75	1.13	60
Registered Newspapers						
4. Single	2.23	0.26	2.39	0.30	2.09	87
5. Bundle	2.83	0.50	3.93	0.54	3.39	86
6. Parcel	20.67	17.01	20.79	20.09	0.70	3
7. Registration	10.62	6.00	11.91	6.00	5.91	50
8. Value pbls.	7.23	2.99	9.33	3.23	6.10	65
9. Acknowledgement	1.54	1.00	1.68	1.00	0.68	40
10. Money orders	15.08	13.61	16.78	16.56	0.22	1
11. Tele. money order	17.86	15.83	19.92	18.66	1.26	6
12. I.P. orders	8.73	1.17	9.26	1.06	8.20	89
Book Post						
13. Book pattern and sample packet	2.40	2.15	2.78	2.35	0.43	15
14. Printed books	3.01	1.70	3.97	1.89	2.08	52
15. Other periodicals	3.28	1.55	3.97	1.66	2.31	58

60 paise to 100 paise and registration fee from Rs.6.00 to Rs.8.00 and introduction of competition postcard at Rs.2.00 each is expected to yield additional revenue to the tune of Rs.76 crore in a full financial year. The degree of subsidy, as indicated in Table 2.11 ranges from about 1 per cent in respect of money orders to 92 per cent on postcard.

Telecommunications

90. The network owned and operated by the Department of Telecommunications (DOT) has been generating surpluses, which is utilised for further expansion of the net work. Net receipts increased to Rs.4951 crore in 1995-96 (RE) from Rs.3936 crore in 1994-95 reflecting an increase of 25.8 per cent. Net receipts are estimated at Rs.5213 crore in 1996-97 (BE). The dividend contribution to the general revenues increased to Rs.279 crore in 1995-96(RE) from Rs.270 crore in 1994-95. The operating ratio, which is a percentage of net operating expenses (excluding the provision for redemption of bonds) to operating revenue earned (excluding registration fee) has come down to 48.7 in 1995-96 (RE) from 48.8 in 1994-95. The Plan outlay for Telecommunication Services (including all PSUs) for the year 1996-97 (BE) is marginally higher at Rs.9874 crore from Rs.9830 crore in 1995-96(RE). The entire outlay (except Rs.5.00 crore pertaining to WMO etc. which is by way of budgetary support) is to be financed

from the internal accruals and extra budgetary resources of the Telecommunication sector. Internal accruals amounting to Rs.7491 crore account for 75.9 per cent of total resources against 79.6 per cent in 1995-96 (RE).

91. Though the telecom network in India is fairly large in absolute terms, (in 1994 it was ranked fourteenth in the world) yet the tele density was 1.4 per cent in March, 1996. An advanced and efficient telecommunications system can enhance international competitiveness of the economy. The DOT has been increasing the quantum of resources deployed for the development of the telecom infrastructure, although the pattern of financing has undergone a sea change. During the first plan DOT received budgetary support which accounted for around 79 per cent of the total resources deployed by it. In the Eighth Plan, 78.7 per cent is expected from internal accruals, 21 per cent from borrowings and other sources, and only 0.3 per cent from budgetary support. In the coming years, substantial investment would be required to upgrade and expand the existing telecom network. The aggregate resource requirements for the provision of basic and cellular mobile telecom services as estimated by the Expert Group on Commercialisation of Infrastructure Projects is placed at Rs. 1,91,500 crore by 2006. These estimates are at today's prices and duty structure.

92. Of late, DOT has primarily relied on internal accruals. However, to meet its targets of network expansion, DOT will have to look to a larger resource pool. It will have to devise a tariff structure which largely reflects the cost oriented approach, subject to country's social obligations and thrusts.

93. A corporate structure for the DOT will enable it to leverage its substantial assets and raise adequate funds to meet all its investment needs. Corporate structure would make DOT into an autonomous entity owned by the Government. In the short and medium term, the government will remain the dominant operator and provider of telecom services in the country. However, with the advent of private operators, the present tariff regime should orient as quickly as possible towards a cost-based structure. It is imperative to have the tariffs reviewed to allocate costs for various services and identify the need, if any, of subsidies.

Broadcasting

94. As per the revised estimates for 1995-96, the total expenditure on Broadcasting was Rs.974 crore as against total receipts of Rs.549 crore. This shows an increase of 19 per cent and 20.4 per cent in total expenditure and receipts, respectively. As a result, the ratio of total receipts to total expenditure improved from 55.8 per cent in 1994-95 to 56.4 per cent in 1995-96. The rising trend in commercial receipts in broadcasting activity over the past few years is indicative of efforts being made in this direction. Commercial receipts were Rs.426 crore in 1993-94, Rs.450 crore in 1994-95, and Rs.540 crore in 1995-96(RE). Further break up of commercial receipts brings to the fore the overwhelming contribution of Doordarshan towards revenue generation. The commercial receipts in case of Doordarshan were Rs.363 crore in 1993-94, Rs.384 crore in 1994-95 and Rs.460 crore in 1995-96.

Outlook

95. It is widely accepted that the fiscal deficit is one of the most important macro-economic policy instruments in the hands of the government and that it plays a major role in maintaining macro-economic balance. The precise effect it has on the economy depends, among other things, on the nature and degree of openness of the economy, the extent of excess capacity and the efficiency and productivity of the economy. It is quite clear, however, that rising fiscal deficits magnify other weaknesses in the economy. High and/or rising fiscal deficits have been associated with an overwhelming majority of the balance of payments crisis. Further, a reduction in the fiscal deficit has been an element of virtually every successful response to meet such a crisis.

The Indian BOP crisis of 1991-92 is a clear example of these facts which illustrate the nexus between the fiscal and current account deficits. A falling trend in the fiscal deficit as a proportion of GDP is therefore one indicator of fiscal health.

96. Though it is relatively easy to see whether the trend in fiscal deficit is up or down, it is much more difficult to define what is the "appropriate" level for each country at any given point in its economic development. For this purpose, the primary surplus or deficit provides a much more precise indication. The critical dividing line is the point of zero primary deficit. As long as there is a primary deficit in the fiscal accounts, both government interest payments and government debt are likely to constitute an increasing proportion of GDP. A primary fiscal surplus can therefore be taken as a second indicator of fiscal health.

97. The combined fiscal deficit of the Central and State governments was budgeted to be around 6.5 per cent of GDP in 1996-97. Of this the primary deficit constitutes only around 0.8 per cent of GDP, with the rest being interest paid by the Central and State Governments to the rest of the economy. Accordingly, reduction of the primary deficit of Central and State Governments to zero is important for achieving fiscal health. If all this adjustment is undertaken by the Central Government, the Centre would need to generate a primary surplus of about 1.0 per cent of GDP.

98. A third factor in determining fiscal health is the quality of the tax and expenditure systems underlying this deficit. This is best illustrated by examples. For instance a primary deficit of 1.0 per cent of GDP when coupled with an extensively reformed tax system would clearly be preferable to a primary deficit of 0.5 per cent with an unreformed system. Similarly, a primary deficit of 1.0 per cent with most unproductive expenditures eliminated from the system would be healthier than a primary deficit of 0.5 per cent of GDP based on an unreformed expenditure system. This is because the more efficient systems of taxation and expenditures would be more sustainable, giving confidence about the sustainability of the related fiscal deficit; inefficient systems would conversely lead to a lack of confidence in the ability to maintain lower fiscal deficits.

99. In the short run, the most critical issue is that of crowding out of private borrowing by government borrowing (both viewed in net terms). Government borrowing is by definition equal to the fiscal deficit of the Central and State Governments taken together. It is considered essential to reduce the fiscal deficit to make room for higher investment and contain inflationary potential.