THE NEW
INDIAN
EXPRESS

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HIGH FISCAL DEFICIT CAN BE GROWTH MANTRA

IN the budget, Union Finance Minister Nirmala Sitharaman has announced a fiscal deficit of 6.9% of gross domestic product (GDP) in revised estimates of 2021-22, against the pegged deficit of 6.8% in budget estimates of 2020–21. Simultaneously, she has not deviated from the medium-term fiscal consolidation path to bring down the high fiscal deficit to 4.5% of the GDP by FY26.

The minister has presented a very high fiscal deficit of 9.2% of GDP last year in 2021-22 from a position of strength, substantiating that it is for strengthening public investment, which in turn can "crowd-in" private investment. High fiscal deficit is perceived as growth-enhancing in the times of pandemic.

Against the backdrop of pandemic, there is a refreshing perspective about the "fiscal rules"— whether to adhere to numeric threshold ratios of deficit. The quality of fiscal consolidation suffers if the path to fiscal consolidation is through expenditure compression rather than increased tax buoyancy.

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In 2022-23, the fiscal deficit to GDP ratio is brought to 6.9% primarily through tax buoyancy, though expenditure cuts in a few schemes – including the food security and employment guarantee schemes – cannot be denied. This also gives insights into how we have reduced the revenue deficit from 7.3% of GDP in 2020-21 (RE) to 4.7% in 2021-22 (RE).

Though there was no "formal announcement on normalisation", such expenditure compression measures give sufficient cues on governments' intention to curb revenue deficits.

If the underlying assumption that "revenue expenditure is bad", it can be detrimental in the time of pandemic as social infrastructure related policies especially in health, education, food security and employment guarantee need budgetary support. The reduction in budgetary allocations, including MNREGA and food subsidies, is a matter of concern.

High capital expenditure is welcome as it can support sustained growth recovery. The outlay for capital expenditure in 2022-23 has been increased sharply by 35.4% in the Union Budget 2022-23.

It is a no brainer that high public debt has no fiscal costs if real rate of interest is not greater than the real rate of growth of economy. This narrative is very close to the dynamics of public finance in Kerala. The state has explored innovative sources of financing the public infrastructure projects. The sources of financing the fiscal deficit in the budget show that gross market borrowing is the dominant financing mode. If the cut-off yield rate of long term government securities go high, it will increase the cost of borrowing of the government. However, the volatility in global financial markets and the impending taper tantrums give pressures to RBI to increase the policy rates, to avoid a capital flight.

The Economic Survey FY22 tabled in the Parliament on Monday highlighted that the government supported the pandemic-ridden economy through simultaneous short term (safety nets) and long term (structural) packages for a sustained recovery – termed as "Bayesian". But, there is conspicuous absence of announcements in budget 2022-23 for small business firms and poor income households who are suffering from pandemic and fighting for survival.

Indeed, RBI has done heavy lifting through massive liquidity infusion programmes. However, the uneven recovery in India tells us that the multiplier effects from credit-related economic stimulus are limited. The uneven recovery in India is a matter of urgent concern and I hope economic stimulus packages will be announced to address that, outside the purview of budget. Another interesting aspect is that even against the backdrop of elections, the government has not announced any political packages for the states that are going for elections -- like a few capital infrastructure projects announced in last year's budget for Kerala and Bengal -- to incentivise the "calculus of (voting) consent" of people.

The term "state" was in the Budget 2022-23 approximately 20 times, which clearly shows the intent of the minister towards co-operative federalism.