

Economic Policy Goals, Ideology and Governance

(Commemorative Lecture)

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I am happy to be here this morning on this occasion to commemorate the 20th anniversary of the National Institute of Public Finance and Policy. Twenty years is a short period in the life of an institution but long enough to make a mark and indicate the kind of contribution that an institution can make to sensible policy making in the public domain.

I have come here to listen. I shall not, therefore, deliver a long lecture. I can also take refuge on the fact that since Parliament is in session, I cannot even utter the word 'policy'. In recent years, there has been a greater degree of convergence among economists and administrators that we require a set of policies which will impart stability to the economy and which will impart a certain dynamism that is required for growth. The central concern of economic policy making, in my humble view, should be the fiscal deficit. This requires paying attention to both augmenting resources as well as controlling expenditure. Many scholars have told me that the effort to control expenditure will yield only marginal results; that unless various institutions and organs of the state are thoroughly overhauled, control of expenditure may not yield results adequate to contain fiscal deficit. They have also told me that the burden, therefore, has to fall on augmentation of resources.

It is tempting to make radical suggestions but one has to remember that we are working under a written Constitution and there are clear divisions of taxation power between the Centre and the states. One, therefore, has to work within the limits laid down by the Constitution. Every now and then I turn to the Seventh Schedule of the Constitution to see if there is any tax that we have missed or any source that we could tap. Frankly, there are very few. Noted politicians easily say that we should tax agricultural incomes. The entry in the Constitution says that you can tax income other than agricultural income. The power to tax agricultural income is with the states. I give that just as an example. It is, therefore, increasingly clear to me, that while we can look at new and innovative taxes and also try to sustain them, under the residuary power of taxation which

is vested in Parliament, the only effective way to augment resources is to widen the tax base.

There is enormous tax evasion in this country. Sometimes it is disguised as tax avoidance but, from the collectors' point of view whether it is evasion or avoidance, the result is the same: the tax does not come to the state. Take the Minimum Alternate Tax (MAT) which has been severely criticised in some quarters. The incidence of MAT will be felt only in the assessment year beginning 1st April 1997! Surely it cannot account for poor corporate performance last year. MAT is a tax which corporates who have large profits and declare such profits to the shareholders and declare dividends, yet who do not pay any tax to the state, have to pay. Firstly, MAT falls on a corporate; secondly, he must have large profits; thirdly, he must declare those profits by adopting a pattern of depreciation which allows him to declare such large profits. And he must have a chartered accountant who is able to disclose that he has made a loss, to the tax collector. Such a company, according to me, is a very successful company and if we extract 12.9 per cent from that company, it should wear it as a badge of success. Why should that company hide the fact that it is a successful profit making company which declares large dividends to its shareholders when the government is asking it to pay 12.9 per cent of its profits as tax?

Why I give MAT as an example is that, while we can innovate with taxation, the real way to augment tax resources is by widening the tax base. Here we run into enormous difficulties. There is very little data base in this country; whatever there is, it is totally fragmented. There is no way in which we can integrate these data bases. I have asked my people a simple question: if a person owns a house and a car and a telephone, or possesses two of these three characteristics, is it not fair to assume that he must have an income which should be subject to income tax? At a meeting of the Chief Commissioners I gave out these figures—the number of telephones in Delhi, the number of houses in Delhi. They run into lakhs. Yet there are only 5 lakh people who are assessed to income tax in Delhi. I think on any Sunday if you walk through Karol Bagh or South Extension you will find hundreds of shoppers who obviously have to pay tax. But they do not pay tax. How do we augment the tax base? This is the real issue.

I would urge all of you to bestow some attention on widening the tax base. The wider the tax base, I can assure you, the quicker it will be and the easier it will be for the government to bring down tax rates. If we

can double the number of income tax assessees in this country we can move much more rapidly towards reducing income tax rates. The two are closely linked. The demand for reduction of tax rates will depend only upon how quickly we are able to widen the tax base.

The same is true of excise and customs—less so in customs but more in excise. A couple of days ago, a Commissioner of Excise who has done good analytical work gave me some very interesting data. In his Zone, 44 per cent of companies contribute 80 per cent of excise revenues—a little over 80 per cent in fact; 56 per cent of companies contribute only less than 20 per cent of excise revenues. The small scale industry (SSI) exemption has become a tax shelter. SSIs must have some exemption. But that has become a device by which one can avoid paying even a certain minimum amount of tax. It has also resulted in fragmentation of production and of productive capacities. How do we widen the tax base in excise which is a major source of revenue for the government? These are questions which we must be concerned with.

It seems to me that we have not yet drilled into the consciousness of policy makers and administrators that the availability of resources at any point of time is finite. People assume that resources are infinite; the capacity of government to borrow is infinite; and the capacity of government to monetise its deficit is infinite. It is not. There are severe limits. If you yield somewhere, you have to pay a price somewhere else. If you yield on the question of, say, borrowing or on the question of monetisation, it shows up somewhere else. It shows up either as high interest rates or it shows up as high inflation and then it hurts everyone.

Today as far as containing inflation is concerned, at least in 1995-96, and to some extent in 1996-97, the entire burden is falling on monetary policy. We are not able to do enough on the fiscal side to contain inflation because the demands are so great. We are now in the middle of an exercise of drawing up the next Five Year Plan. Some snatches of the discussions have appeared in the newspapers. I think the Member-Secretary, Planning Commission, very aptly described it: as it is a dharma of the planner to ask for more, it is a dharma of the Finance Ministry to plead for less. The point I wish to make is, even for planners, the fiscal deficit must be the central concern, and planning must recognise that government does not have an infinite capacity to borrow, either domestically or externally.

The country can grow only to the extent it has savings, can attract foreign savings, and has an efficient capital output ratio. We must raise savings; we must keep India attractive for foreign savings; and we must become more efficient. These appear to be old-fashioned virtues, but it is old-fashioned virtues which have made new "Tigers". We need to imbibe these old-fashioned virtues. I think it is possible to raise domestic savings. It is possible to raise savings particularly in the public sector and in the government sector. The Common Minimum Programme of our Government says that the public sector cannot be allowed to dissave. That is a very pregnant statement. One must have the courage to follow up and take the steps by which that can be translated into policy. The public sector cannot be allowed to dissave. Similarly, we must keep India attractive for foreign savings to come here as foreign direct investment.

A single minded drive towards certain measurable goals is what is missing in India. The Chinese have such a goal. Malaysians have such a goal that they want to make their country a developed country by 2020 and drop the tag of a developing country. Indonesia has such a goal. We *must* keep for ourselves some measurable goal. And we must become more efficient. Unless we improve efficiency, even if our savings go up or we attract more foreign savings, it will not translate into real growth. I would urge, therefore, NIPFP and others to work on a set of measurable goals which we can achieve, say, by the year 2000 and, again, goals which we can achieve by 2010, and goals which we can achieve before 2020. For good reasons I do not think beyond 2020.

I would suggest that by the year 2000, a measurable goal that we must achieve is a 7.5 per cent real GDP growth rate on a sustainable basis. We must, therefore, have in place policies and instruments which will ensure that we have a 7.5 per cent GDP growth rate every year. An economist friend of mine three or four days ago left a very sobering thought with me. She told me that I could no longer take credit for a 6.5 per cent growth rate because that is already there now. To achieve 6.5 or 6.6 per cent is no big achievement because the economy seems to have matured into a 6.3–6.4 per cent rate of growth. So at the end of the year if you turn up and say that you have achieved 6.3 or 6.4 per cent, that is no big success. I think that is very sobering but, by 2000, we must be able to say that we can achieve, on a sustainable basis, a 7.5 per cent growth rate. By 2010 we should be able to say that we have a per capita income of at least US\$ 750 and, by the year 2020, we should set for ourselves a goal of a per capita income of at least US\$ 1200. We must also set for ourselves a goal of a

fiscal deficit of less than 4 per cent of GDP by the year 2000 and then bring it sharply down to, say, 3 per cent by the year 2005. May be that is too long a time table. But we *must* set for ourselves some measurable goals because I think we allow year after year to pass by without goals against which we can measure our success. We seem to be happy with good monsoon and we rue when there are bad monsoons, but we must set for ourselves measurable goals.

I think governance will become easier if we can make these goals widely accepted and widely looked forward to. Governance is becoming more complex because the polity is fragmented. For every reformer, you will find an anti-reformer. For every measure of reform, you will find some opposition. The task is difficult enough to put together a government which commands majority, because the people seem to elect, for a variety of reasons, parties and individuals who do not share a basic ideology or basic philosophy. In fact it is sometimes more comfortable to go back to the age of ideology when at least you knew that 350 individuals of one ideology could get elected—even if it was an imperfect ideology, atleast some ideology linked them. Today one can never say what will happen to a bill or what will happen to a measure. It is quite possible that someone in your own constituency will stand up and say that we don't agree. So, given the fragmented polity, it is even more necessary to find *some* convergence on a few economic issues, particularly issues concerning fiscal policy and public policy.

I think that is enough for the commemorative speech. I think commemorative is too high sounding a title. I have made a few introductory remarks just to show that we support the work you do, and that we will continue to support the work you do. We are respectful listeners of your advice, even if we don't follow them always, and we want you to continue to work for the government. We want independent institutions like NIPFP to continue to be a guide, critic, and counsellor of government, and I wish you many many more years of useful work. Thank you.