Will Investor Sentiment Change?

Budget may help at the margins, but has no real measure to boost private investment

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The first Budget of a new government is always looked forward to with great expectations. This is true even if the old government is re-elected to power as is the case in the current situation. Added to this, we have a new finance minister who presents her first Budget. A budget is something more than a statement of government's revenues and expenditures. It spells out the new government's aspirations and what it seeks to achieve in the next few years. But the expenditure programmes have to be seen in the context of revenue expectations and the programme for fiscal consolidation. It is to this scrutiny that we turn.

As in the case of past two budgets, the Budget for 2019-20 has to be presented against a background of several concerns which include a slowdown in economic growth, inadequate private investment, agrarian distress and problems in the financial sector. The Budget reflects these concerns and provides a host of measures to address them. But much will depend on how these programmes will be implemented.

What stands out prominently in the Budget is the commitment to stick to fiscal consolidation. The fiscal deficit is now pegged at 3.3% of GDP, which is a shade lower than what was indicated in the interim Budget. But much will depend upon how revenues will move. In fact, the Economic Survey expected the real GDP to grow at 7% in 2019-20. But there are doubts about whether this will happen or not.

The nominal GDP in 2019-20 is assumed to grow by 12%. According to the Budget Estimates, the gross tax revenue is assumed to grow at 9.5% which certainly is not high. In fact gross tax revenue as a percentage of GDP is expected to come down from 11.9% in 2018-19 to 11.7% in 2019-20. However, non-tax revenue is expected to grow at 27.7%. Within it, dividends and profits are budgeted to grow at 37%. Reliance on the non-tax revenues is certainly high. The finance ministry will have to keep a constant watch on the revenues and should be willing to adjust expenditures, if revenues do not grow at the desired rate.

The tax changes are minimal. But some of them are significant. The lower corporate tax rate covers most of the companies. It has not been extended to all, presumably because the companies left out are the ones which contribute significantly to the tax revenue. It is not clear whether the change will contribute to a change in investment sentiment.

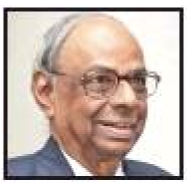
The surcharge on income earners above Rs 2 crore will be really biting. The imposition of surcharge will also antagonise state governments because this revenue will not be shared with them. The tax concession given to affordable house owners is welcome and this can have a direct impact on investment. Tax concession on purchase of electrical vehicles is also welcome. Government must rethink the imposition of customs duties on certain products as this is a reversal of the trend since liberalisation. It will create unnecessary controversies globally.

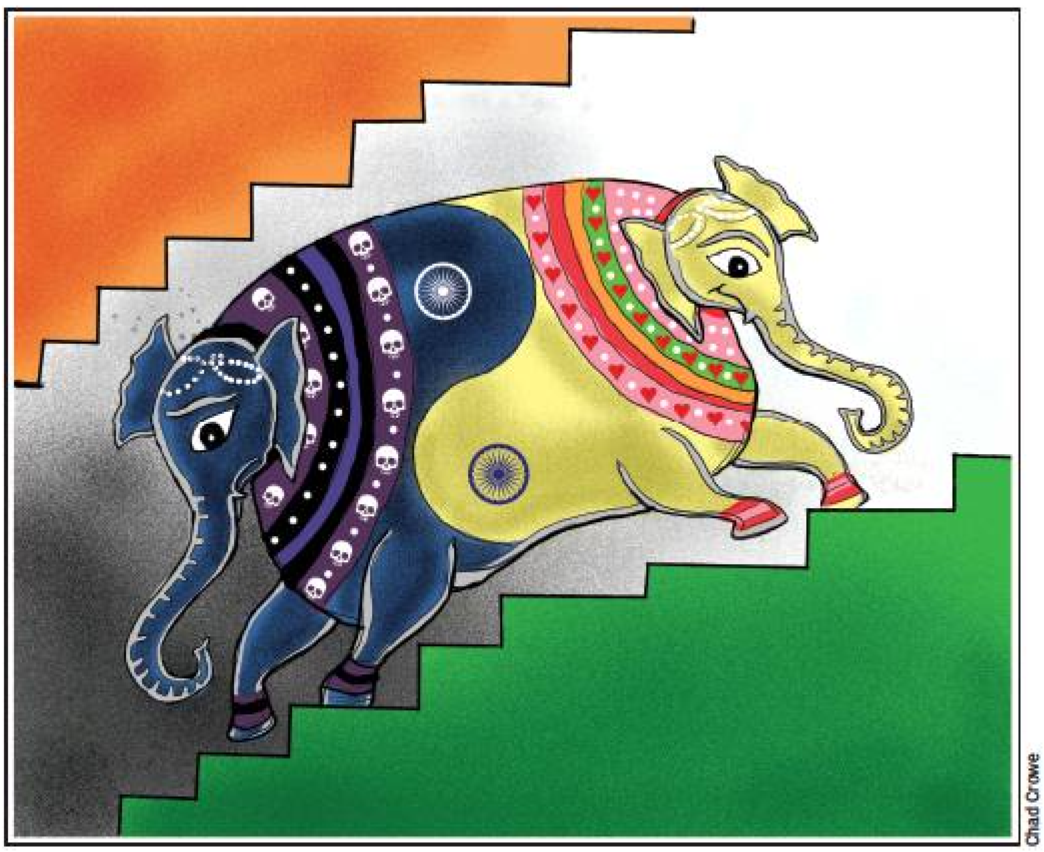
The FM spent the bulk of her time dealing with several programmes in different areas. These are obviously in the right direction. But the concern with all expenditures is how well they are implemented and what impact they have. While total expenditures are expected to rise by 13.4%, capital expenditures are to rise by 9.4%. The ratio of capital expenditures to GDP remains at 1.6%. Thus in the contribution of government directly to investment, there is no change.

The Budget has several proposals relating to reform of several sectors. Prominent among them are those relating to the financial sector. The proposal for government to borrow in foreign currency does not appear to be correct. This essentially means the exchange risk is borne by government, unlike the situation in which foreign investors are allowed to invest in government bonds in rupees. Second, there is certainly no need for government to borrow as the foreign inflows are adequate. There are a number of other issues relating to NBFCs and house finance on which there can be differences of opinion. The tax on cash withdrawals is not incorrect in principle. But clever people can get around it in a number of ways.

To conclude, both the Economic Survey and the FM talked of private investment driven growth. Will the totality of the measures introduced in the Budget help in accelerating investment? As mentioned earlier capital expenditures of government as a proportion of GDP remain the same. The other programmes such as those relating to highways are financed by non-budgetary resources. There is however no measure in the Budget which will result in an increase in private investment. If however the Budget as a whole helps to create a favourable investment sentiment, it will help.

The writer is former Chairman of the PM Economic Advisory Council and former Governor, RBI





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