Economy Insight:
Union Budget Outlook

FICCI Research ***January 27, 2017***

Introduction

It is that time of the year again when everyone awaits with anxiety the Budget speech of Union Finance Minister and looks out for specific announcements that will influence economic performance of various sectors, have a bearing on social development and most likely affect the pockets of consumers.

This year's budget is different from previous years' budget on several counts. It is for the first time in the long history of budgetary exercise that the Union Budget will be announced a month in advance. This will help in timely disbursements of capital outlays from the beginning of next financial year instead of later in the second quarter. The other big change is going to be the merger of Rail Budget with the General Budget. This will help in better policy planning and better allocation of resources. The Budget document will also do away with the classification of 'plan and non-plan expenditure' and replace it with 'capital and revenue expenditure'. This will provide a clear distinction between productive and general recurring expenditure.

Most importantly, the budget comes soon after the '50 days' of demonetisation move that was unprecedented and jolted the cash economy of the nation. The immediate fallout of the move has been slowing of demand and consumption, which is expected to affect the GDP growth for a few quarters. The Budget is also going to be laid out keeping in view the implementation of GST in 2017-18. Given the backdrop of such developments, this year's budget is expected to deliver a fiscal stimulus for enhancing consumption and boosting investment, while simultaneously preparing the economy for greater formalisation and widening of tax net.

There is a lot of speculation with respect to the exact impact of demonetisation on various macro indicators including inflation, growth, as well as tax revenues. It is highly difficult to predict the outcomes since the move has been unprecedented with no empirical evidences from the past. Nevertheless, we have made an attempt in this paper, to assess the fiscal math that is likely to play post demonetization and help in achievement of the fiscal deficit target of 3.5% for the year 2016-17. Additionally, we have tried to assess whether the fiscal deficit target of 3.0% as provided in the fiscal consolidation roadmap, is achievable for the year 2017-18, especially in light of factors such as rise in global oil prices, and greater formalization of the economy due to digitization push as well as implementation of GST.

Part A: Outlook on Achievement of Budget Estimates for 2016-17

The foremost factor that will influence the outcome of budget 2016-17 will be the GDP growth in third and fourth quarters of the fiscal. While there are unequivocal views on the slowdown of growth in these quarters owing to demonetisation, the extent of slowdown however is highly debated amongst experts as well as economists. As per the Advance Estimates of GDP growth recently released by the CSO, GDP growth for 2016-17 will be lower at 7.1%, as against 7.6% in 2015-16. The GDP growth in the first two quarters of 2016-17 is already estimated lower at 7.1% and 7.3%, as against the corresponding figures of 7.5% and 7.6% in 2015-16, respectively. In light of these statistics, it is quite possible that the GDP growth estimate of 7.1% for 2016-17 does not take into account the demonetisation effect. In-fact, CSO's press release also states that the advance estimates are based on extrapolation of key indicators for first 7/8 months of the financial year[1].

Traditionally, the first Advance Estimates are used as a basis for fiscal calculations in the Budget. ***As per the Advance Estimates, nominal GDP growth for 2016-17 is estimated at 11.9%, higher than last year's Union Budget projection of 11%.*** This may give a sense that there will be higher fiscal space available to the government, but since this does not fully take into account the impact of demonetisation, the Finance Minister could revise the estimates downwards while preparing the fiscal account.

Assessment of Expenditure

The Government has budgeted total expenditure for 2016-17 at Rs 19.78 lakh crore, which is 10.8% higher than the revised estimates of previous year (Rs 17.65 lakh crore). During the eight months of the current fiscal (Apr-Nov 2016), the government has spent 65% of the budgeted amount. Out of the total expenditure during Apr-Nov 2016, the government has incurred Rs 1.42 lakh crore on capital expenditure, which is equivalent of 57.6% of the budgeted amount under this category. On a y-o-y basis, this is 10% lower than the corresponding period in previous fiscal. On the other hand, the growth of revenue expenditure has increased by 16% y-o-y during the first eight months, which is primarily due to the higher salaries and pensions under the seventh pay commission and OROP. The fall in the share of capex in total expenditure is worrisome, especially since public capex is crucial to spur the investment cycle. ***We hope that the outstanding 42.4% of the budgeted capex will be fully utilized over the remaining period of the fiscal.***

Central Government's Expenditure (Apr-Nov 2016)

	Budget Estimates FY17 (Rs crore)	Actuals upto Nov 2016 (Rs crore)	% of Actuals (upto Nov 2016) over BE FY17	% change over Apr-Nov 2015
Non-Plan Expenditure	14,28,050	9,22,492	64.6%	-64%
Plan Expenditure	5,50,010	3,64,189	66.2%	-64%
Total Expenditure	**19,78,060**	**12,86,681**	**65.0%**	**-64%**
of which				
Capital Expenditure	*2,47,024*	*1,42,347*	*57.6%*	*-10%*
(% of total expenditure)	*12.5%*	*11.1%*		
Revenue Expenditure	*17,31,036*	*11,44,334*	*66.1%*	*16%*
(% of total expenditure)	*87.5%*	*88.9%*		

Note: As per RE 2015-16, share of revenue expenditure in total expenditure is 86.7% and that of capital expenditure is 13.3%
Source: Controller General of Accounts, Medium Term Expenditure Framework, Ministry of Finance, FICCI Calculations

In terms of the revenue expenditure, three key components need to be specifically analysed to assess any possible deviations from the budget estimates. These are salaries, subsidies and interest payments.

As regards the ***salaries*** component, which accounts for 5.7% of total budget expenditure, there has been an additional payout due to the seventh pay commission and pension payments. While the last year's budget had made an additional provision in this regard, the medium term expenditure framework presented in August 2016 states that complete absorption of the pay revision will require some enhancement in revised estimates of 2016-17. Alternatively, the Finance Minister would have to keep higher salary provisions in the 2017-18 budget.

[1] *http://pib.nic.in/newsite/PrintRelease.aspx?relid=156182*

Subsidies component of expenditure requires close assessment as India has been spending almost 2-2.4% of GDP on subsidies alone. Over the last few years, fuel, food and fertilizer subsidies have roughly accounted for 14 – 18% of total budgetary expenditure.

Stressing on rationalization of subsidies, the Union Budget for 2016-17 lowered the subsidy spend to 12.7% of total expenditure (roughly 1.65% of GDP). In absolute terms, total subsidy expenditure for 2016-17 is estimated at Rs 2.50 lakh crore, about Rs 7,368 crores less than the subsidy spend in 2015-16. To find out, whether there could be any slippage on the subsidy targets, we have analysed the trend in major subsidies i.e. food, fuel and fertilizer subsidies in the current fiscal.

		RE 2015-16	BE (2016-17)	Change (FY17 over FY16)
1	**Major subsidies (Rs. crore)**	241856.58	231781.61	-10074.97
	(as a % of GDP)	1.8%	1.5%	
1.1	Food subsidy **(Rs. crore)**	139419	134834.61	-4584.39
	(as % of GDP)	1.0%	0.9%	
1.2	Fertilizer subsidy **(Rs. crore)**	72437.58	70000	-2437.58
	(as % of GDP)	0.53%	0.46%	
1.3	Petroleum subsidy **(Rs. crore)**	30,000	26,947	-3053
	(as % of GDP)	0.22%	0.18%	
2	**Interest (Rs. crore)**	13808.27	15523.29	1715.02
		0.10%	0.10%	
3	**Others (Rs. crore)**	2136.32	3128.03	991.71
		0.02%	0.02%	
	Total subsidy (Rs. crore)	**257801.17**	**250432.93**	-7368.24
	(as a % of GDP)	**1.90%**	**1.65%**	
	Percentage of Total Expenditure		**12.66%**	

Source: Budget Documents

a) **Food subsidy**: Food subsidy forms the major chuck of India's subsidies, accounting for nearly 1% of the GDP. The Government had budgeted food subsidy bill at Rs 1.35 lakh crore for 2016-17, about Rs 4,584 crore less than the revised estimates for 2015-16, owing to targeted distribution of food subsidy under PDS. As per a recent report by Financial Express, food subsidy bill for 2016-17 is, however, expected to be about Rs 10,000 crore more than the budgeted Rs 1.35 lakh crore (i.e. at RS 1.45 lakh crore). It has been reported that Food Corporation of India (FCI) has requested for an additional Rs 7,000 crore in the current fiscal against the budget allocation of Rs 1.03 lakh crore, and state-level agencies have also asked for additional Rs 2,000-3,000 crore[2].

The increase in food subsidy bill can be attributed to the implementation of National Food Security Act (NFSA) across all the States from April 2016. The Central Government is now providing subsidised foodgrains to about 80 crore beneficiaries in the country. However, efforts are on to extend Direct Cash Transfer of food subsidy to the beneficiaries to plug the leakages. As of now, the cash transfer under the DBT scheme has been implemented in 3 Union Territories namely Chandigarh, Puducherry and in Dadra & Nagar Haveli, covering 9.14 lakh beneficiaries. In-fact, the government saved Rs 10,191 crore in 2015-16 through DBT implementation of food subsidy[3]. A higher savings is expected from DBT implementation in 2016-17.

[2] http://www.financialexpress.com/india-news/no-subsidy-shock-for-narendra-modi-govt-despite-food-security-act-roll-out/506221/

[3] https://dbtbharat.gov.in/page/frontcontentview/?id=ODM=

b) **Fertiliser subsidy:** Fertilizer subsidies too constitute a significant portion of our subsidies (almost 0.5% of GDP). In the Union Budget 2016-17, the government had allocated Rs 70,000 crore for fertiliser subsidies, which is about Rs 2,437 crore lesser than the actual fertiliser subsidy in 2015-16. However, as per a recent report by Business Standard, the Fertiliser Ministry has already placed a demand for an extra Rs 25,000 crore above the budget allocation, in order to pay dues which had been exhausted by August itself. It has been estimated that unpaid dues might touch Rs 40,000 crore[4].

c) **Fuel/ Petroleum subsidy**: India has significantly rationalised upon its fuel subsidies in the last few years, owing to deregulation of petrol and diesel prices and lately through GiveUp campaign and DBT implementation of LPG subsidies (under PAHAL). Nearly 10 million LPG consumers have given up their subsidies under the GiveUp campaign. The DBT implementation of LPG under PAHAL enabled the government to save Rs 6,912 crore in 2015-16 and even higher savings are expected for the year 2016-17. The other component of fuel subsidy is kerosene, which has come down over the years and is expected to fall sharply as rural supply of cooking gas and electricity goes up. In-fact, sale of subsidised kerosene fell by 4.2% to 6.8 million metric tonnes in 2015-16. In the current fiscal, the Centre has planned reduction of kerosene supply by 5% every quarter and there have been small increase in retail prices besides the roll out of direct cash transfer for beneficiaries. All these measures are expected to reduce kerosene subsidy by 25% by the end of this fiscal year to about Rs 8,600 crore[5].

Year	Kerosene Consumption		Kerosene Under Recovery/ Subsidy	
	(million metric tonnes)	y-o-y change (%)	(Rs. Crore)	y-o-y change (%)
2007-08	9.4		19,102	
2008-09	9.3	-1.1%	28,225	47.8%
2009-10	9.3	0.0%	17,364	-38.5%
2010-11	8.9	-4.3%	19,484	12.2%
2011-12	8.2	-7.9%	27,352	40.4%
2012-13	7.5	-8.5%	29,410	7.5%
2013-14	7.2	-4.0%	30,574	4.0%
2014-15	7.1	-1.4%	24,799	-18.9%
2015-16	6.8	-4.2%	11,496	-53.6%

Source: Economic Times, FICCI calculations

Recently, the Organization of the Petroleum Exporting Countries (OPEC) decided to cut crude oil production by 1.2 mbpd from 1st January 2017, which is expected to raise the oil price. The average crude price during Apr-Nov 2016 was $45 a barrel, and the latest data shows the crude oil price at around $53 a barrel (as on Jan 17, 2017). However, it is expected that this will not have a significant incremental impact on the subsidy bills as prices of petrol and diesel stand deregulated. On the whole, it is expected that the fuel subsidy bill may not exceed the budgeted amount of Rs 26,947 crore for 2016-17.

[4] http://www.business-standard.com/article/economy-policy/here-s-why-flat-advance-tax-will-not-derail-govt-s-fiscal-deficit-target-116121900004_1.html

[5] http://economictimes.indiatimes.com/news/economy/policy/kerosene-subsidy-likely-to-decline-by-25-per-cent-this-fiscal-year/articleshow/54819717.cms

As regards the other major expenditure component - **Interest payment -** that constitutes almost 25% of total expenditure, some deviation is expected owing to reduction in yields post demonetisation.

	BE 2016-17	2016-17 (Actuals) (Apr-Nov)	2015-16 (April to November)	Percentage to budget estimate (2015-16)	Percentage to budget estimate (2016-17)
Interest payment (Rs. billion)	4,926	2,668	2,526	55.40%	54.16%
Interest as % of total expenditure	24.90%	20.74%	22.11%		

Source: https://rbidocs.rbi.org.in/rdocs/Bulletin/PDFs/23T336C38CD059B4114895954F18AAA33EF.PDF

For the full fiscal year 2016-17, government had budgeted Rs 4.9 lakh crore for interest payments, 54% of which has been incurred upto Nov 2016. Post demonetisation in November 2016, most of the banks have parked excess liquid funds in government bonds and this has led to a dip in the government bond yield. Already the average monthly yield for 10-year Government Securities in 2016-17 has been significantly lower in comparison with that of 2015-16 (Refer table below). Hence, government's interest payments from Nov 2016 onwards are expected to be lower than the previous year.

Average monthly yield of 10 year G-sec (%)

Month	2015	2016
April	7.78	7.44
May	7.90	7.45
June	7.98	7.48
July	7.99	7.30
August	7.79	7.13
September	7.72	7.02
October	7.56	6.85
November	7.68	6.53
December	7.75	6.52

Source: Economic Outlook, CMIE, RBI

Assessment of Revenues

Tax Revenue

Hon'ble Finance Minister recently said that the government is likely to exceed the budget estimates for Tax Revenues for 2016-17. As per the data released by the Ministry of Finance for the nine month period Apr-Dec 2016, **Direct Tax collections** stand at Rs 5.53 lakh crore, which is 12% more than the net collections for corresponding period previous year, and account for 65.3% of the Budget Estimates for 2016-17. While the personal income tax collections (after refunds) during this period are 24.6% higher over the corresponding period of last year, corporate tax collections (after refunds) have seen a rise of only 4.4%. The robust growth in personal income tax can be attributed to the change in time schedule of payment of advance tax[6] and partly to better compliance post demonetisation. Further, old currency notes were allowed to be used for making tax payments during the demonetisation period, and hence there was no negative impact of same on the direct tax collections.

[6] *An individual needs to pay advance tax of 75% by December 15 for the current fiscal, as against the requirement of 60% till previous year*

Additionally, the government has received Rs 67,382 crore under the **Income Declaration Scheme** and huge sum of undisclosed income has been detected as a part of the nation-wide operations against black-money hoarders till January 8, 2017. The second leg of income disclosure scheme under the Pradhan Mantri Garib Kalyan Yojana (PMGKY) was introduced from December 17 and will remain in force until March 31, 2017. It has been reported that the government expects around Rs 30,000 crore tax collections from the IDS scheme that ended on Sep 30, 2016[7]. Additionally, according to BofA Merrill Lynch Global Research report, the government could raise about one lakh crore rupees of additional taxes under the IDS-II (PMGKY)[8].

Tax Revenue Collections in 2016-17 (Upto December 2016)

	Apr-Dec 2016 (Rs Lakh cr)	Apr-Dec 2015 (Rs Lakh cr)	y-o-y %	% of Budget Estimate
Direct tax	**5.53**	**4.93**	**12.0%**	**65.3%**
Personal Income Tax	2.32	1.86	24.6%	
Corporate Tax	3.19	3.06	4.4%	
Indirect tax	**6.30**	**5.03**	**25.0%**	**81.0%**
Excise Duty	2.79	1.95	43.0%	
Service Tax	1.83	1.48	23.9%	
Customs Duty	1.67	1.60	4.1%	
Tax Revenue	**11.83**	**9.96**	**13.5%**	**69.3%**

Source: PIB, Ministry of Finance, FICCI Calculations

On the **indirect tax** front, the data for the nine month period shows that net revenue collections from excise, customs and service tax stand at Rs 6.30 lakh crore, which is 25% higher than the corresponding period previous year. This significant rise can be attributed to the increase in service tax rates and increase in excise duty on petrol and diesel. Demonetisation move that led to slow demand post November 8, 2016 could have some adverse impact on indirect tax collections. However as per the data, government has already mopped 81% of the budgeted indirect tax collections upto December 2016. Hence, outstanding target should be achievable in the last quarter of the fiscal year.

Given the robustness in direct tax collections and indirect tax collections too expected to reach the budgeted levels, we could very well exceed the tax revenue estimates for 2016-17, as stated by the Finance Minister.

Non-Tax revenue

Over the past few years, non-tax revenue has emerged as one of the important component of government resources. These non-tax revenues mainly comprise of interest and dividend receipts of the Government, as well as revenue from telecom spectrum auctions. For the year 2016-17, the government has budgeted Rs 322,921 crore from the non-tax revenue, which is about 25% higher over the 2015-16 revised estimates.

As regards the **disinvestment proceeds** from state-owned enterprises, the Government had budgeted Rs 56,500 crore during 2016-17, of which Rs 36,000 crore was to be raised from minority stake sales and Rs 20,500 crore from strategic stake sales.

[7] http://indianexpress.com/article/business/black-money-65250-rs-crore-income-tax-arun-jaitley-narendra-modi-3059673/

[8] http://www.newindianexpress.com/business/2016/dec/29/ids-to-raise-rs-100000-crore-in-tax-to-contain-fiscal-deficit-report-1554183.html

Disinvestment proceeds in 2016-17 (Rs crore upto Nov 2016)

Budget Estimates (2016-17)	Receipts from sale of Minority Shareholding in CPSE	Receipts through Strategic Sale	Receipts from other related transactions	Total Receipts (Apr-Nov 2016)
56,500	20,903.2	2,096.4	529.2	23,528.7

Source: Ministry of Finance

As of November 2016, the receipts from minority stake sales has been Rs 20,903 crore (58% of budgeted amount), while strategic stake sales have fetched only Rs 2,096 crore (10% of budgeted amount). As per recent reports, the government is considering strategic stake sale of PSUs in the next two months to achieve the disinvestment target for the year. In fact, on January 18, 2016 the Cabinet has approved listing of five general insurance companies; the government shareholding in these companies will be reduced from 100% to 75% in one or more tranches over a period of time.[9]

A slippage is expected on the **spectrum** target. The spectrum sale target was Rs 64,000 crore and the government has realized only about half of this amount (Rs 32,434 crore) from the Spectrum auctions in October 2016.[10] With respect to **dividend** receipts, the government had budgeted Rs 123,780 crore in 2016-17, of which 70% has been realized during Apr-Nov 2016.[11] It has been reported that some PSU banks are likely to skip dividend payment in the current financial year, owing to lower profits on the back of lower credit offtake and increased NPAs[12]. However, RBI could shell out special dividend to the government in wake of the cash that does not return to the banking system post demonetisation. As per the analysis of Bank of America – Merill Lynch, the dividend payout from RBI could be of Rs 50,000 crore.[13]

Will Fiscal Deficit Target of 3.5% for 2016-17 be achieved?

In the eight month period, Apr-Nov 2016, the fiscal deficit of the Central Government has touched Rs 4.58 lakh crore, which is almost 86% of the budget estimates. This implies that there is a space to spend only Rs 76,000 crore above the receipts in next four months, if 3.5% fiscal deficit target is to be met.

Central Government Finances: April - November (2016-17)

Indicator	Budget Estimates 2016-17 (Rs crore)	Actuals in Rs crore (Apr-Nov 2016)	% of Actuals to Budget Estimate
Total Expenditure	19,78,060	12,86,681	65.0%
Total Receipts*	14,44,956	8,28,685	57.4%
Fiscal Deficit	5,33,904	4,57,996	85.8%

** Total receipts include revenue receipts and non-debt capital receipts*

Source: Ministry of Finance, Controller General of Accounts.

9 http://www.financialexpress.com/market/cabinet-oks-listing-general-insurance-companies-in-a-boost-to-divestment-plan/512739/

10 http://www.livemint.com/Industry/xt5r4Zs5RmzjdwuLUdwJMI/Spectrum-auction-ends-after-lukewarm-response-from-telcos.html

11 http://164.100.158.190/writereaddata/MonthAccount/112016/Nontax1611.HTM

12 http://indianexpress.com/article/business/banking-and-finance/most-psu-banks-to-skip-dividend-payout-this-fiscal-4478652/

13 http://www.livemint.com/Industry/I97HL5tCsAvI9SHpUHbPtM/RBI-surplus-payout-from-note-ban-seen-Rs50000-crore-BofAM.html

Based on our above analysis of expected expenditure in 2016-17, spend on salaries, food subsidy and fertilizer subsidy are likely to exceed the budget estimates while interest payments could be marginally revised downwards. There would also be some additional expenditure in the last quarter owing to sops announced by Hon'ble Prime Minister on the New Year Eve with respect to interest subvention for affordable housing, 60-days interest relief to farmers and financial assistance to pregnant women, etc. The capital expenditure, on the other hand, has been way below mark during the first eight months, but we hope that the government will fully utilize the budgeted amount in the remaining period of the fiscal as it is critical to spur the investment activity and push growth. The overall expenditure could thus exceed budgetary estimates.

Above analysis of revenue collections shows that tax revenue is likely to exceed the budgetary estimate and while there could be a shortfall with respect to receipts from disinvestment and spectrum sale, the special dividend payout from RBI could be a bonus. Under such a scenario, the government would have adequate fiscal space to fund additional expenditure.

The achievement of fiscal deficit target would also depend upon the revised estimates of nominal GDP growth, taking into account the advance estimates of CSO as well as the impact of demonetisation. Different organizations have given varying estimates of decline in GDP growth ranging from a low of 0.3 percentage points to a significantly high figure of 2 percentage points.

If the Finance Minister takes nominal GDP growth estimates of 11.9% as put out by CSO (as against 11% projected in last year's Budget), the revised fiscal deficit target would stand at about Rs 5.78 lakh crore, thereby providing additional fiscal space of almost Rs 1.2 lakh crore as against Rs 76,000 crore. The fiscal deficit target would be very much achievable in such a scenario, and could also be lower than 3.5%. However, if the Finance Minister revises GDP growth estimates downwards of 11% assuming deeper impact of demonetisation, there could be a slippage on the fiscal deficit target.

Part B: Outlook and Suggestions for Union Budget 2017-18

The medium term fiscal consolidation roadmap sets the rolling target for fiscal deficit at 3% of GDP in 2017-18. To predict whether Finance Minister will stick to the said target or not, we need to assess various factors that are likely to influence the fiscal management and could have both positive and negative implications. In this section, we have assessed the likely implication of demonetisation, GST, oil prices, interest rates, tax policies and DBT implementation on the budgetary expenditure and revenue of 2017-18.

Foremost, a realistic estimate of GDP growth for the next fiscal year is essential. Several experts believe that demonetisation move will have minimal impact in 2017-18 as it was a temporary measure. Post demonetisation, while various international organisations have cut GDP growth forecast for the current fiscal, they remain optimistic for the next fiscal year. World Bank projects India's GDP growth for 2017-18 at 7.6% while IMF puts it at 7.2%. Further, there could be inflationary pressure owing to rise in crude oil prices and this could push the nominal GDP growth upwards. As per RBI's inflation projections (Oct 2016), if crude oil prices increase to $70 per barrel by the end of 2017-18, inflation could be higher by about 40-60 bps.[14] The medium-term policy framework of the government has assumed GDP growth at current market prices in 2017-18 at 12%, which seems to be a reasonable estimate.

[14] https://rbi.org.in/Scripts/PublicationsView.aspx?id=17385#ti2

Snapshot: Factors likely to influence fiscal maths in 2017-18

	Positive Impact	Negative Impact
Demonetisation	+ Greater tax compliance	
GST	+ Increase in tax revenue	
Lower tax rates		− Lower tax revenue if no/ limited rise in taxpayers
Lower interest rates	+ Reduced interest expenditure	
Rise in oil prices		− Loss of excise revenue + slight rise in subsidy
DBT implementation	+ Savings on subsides and CSS	

Outlook on expenditure in 2017-18

The total expenditure for 2017-18 is projected at about Rs 21 lakh crore according to the medium term expenditure framework of the government. Keeping in view the fiscal deficit target of 3% in 2017-18, the medium term projections have estimated total expenditure to be brought down to 12.3% of GDP as against 13% of GDP in BE 2016-17.

As per these projections, capital expenditure is expected to grow at a higher rate of 8.8% y-o-y while revenue expenditure is expected to increase by 5.7%. However, in terms of GDP share, the capex projections for 2017-18 are at the same levels as in BE 2016-17 at 1.6%. It is desired that the capex is enhanced further. ***We hope that the forthcoming budget allocates adequate funds on the capex, which should be at least 1.8%-2% of GDP***.

To maintain appropriate fiscal balance, higher expenditure on capex and social sector needs to be supplemented with rationalization of unproductive expenditure, such as that on subsidies and interest payments. The medium term expenditure projections of the government estimate interest payments in 2017-18 to be 10.4% higher over that of 2016-17. There could be slight downward deviation from this owing to a progressive reduction in debt-GDP ratio of the Centre and downtrend in the rate of borrowings.

With respect to subsidies, food subsidy bill for 2017-18 is likely to be in line with the actual bill for 2016-17, since NFSA has been implemented nationwide from April 2016 itself. As discussed in the previous section, the food subsidy bill for 2016-17 is expected to be around Rs 1.45 lakh crore. The expected rise in oil prices could raise the oil subsidy component, however this will be limited as petrol and diesel have already been deregulated and kerosene consumption has been on a downtrend. However, LPG subsidy bill could shoot up as subscription for LPG cylinders has been on a rise, especially since the launch of Pradhan Mantri Ujjwala Yojana (PMUY) in May 2016.

As per the medium term expenditure projections of the government, the expenditure on major subsidies (food, fertilizer and petroleum subsidies) is estimated to be brought down to 1.4% of GDP in 2017-18. However, as the above analysis shows, cost of major subsidies could be higher than projected. Thus, ***to arrest the rise of subsidy bill, the government should implement DBT for all subsidies at the earliest***. It has been reported that DBT could be made applicable to another 500 central schemes[15]. The plan is to expand the coverage of DBT significantly. The list includes subsidy payments for fertilizer, interest on home loans up to Rs 1 lakh from public sector banks and those for transport and freight, among many others.

Medium Term Expenditure Projections (2017-18)

Amount in Rs crore	RE 2015-16	BE 2016-17	2017-18				Likely deviation
			(MTE Projections)	*% chg over 2016-17*	*% sh of total expenditure*	*% sh GDP*	
Revenue Expenditure	*15,47,673*	*17,31,037*	*18,29,317*	*5.7%*	*87.2%*	*10.7%*	
Salary	93,740	1,12,133	1,22,284	*9.1%*	*5.8%*	*0.7%*	
Interest	442,620	4,92,670	5,44,000	*10.4%*	*25.9%*	*3.2%*	↓
Pension	95,731	1,23,368	1,36,026	*10.3%*	*6.5%*	*0.8%*	
Subsidy-							
a. Fertiliser	72,438	70,000	70,000	*0.0%*	*3.3%*	*0.4%*	
b. Food	1,39,419	1,34,835	1,40,000	*3.8%*	*6.7%*	*0.8%*	↑
c. Petroleum	30,000	26,947	21,000	*-22.1%*	*1.0%*	*0.1%*	↑
Defence	1,48,228	1,68,380	1,83,355	*8.9%*	*8.7%*	*1.1%*	
Centralised provision for grants to states	106,679	112,996	115,451	*2.2%*	*5.5%*	*0.7%*	
Education	56,495	57,454	60,554	*5.4%*	*2.9%*	*0.4%*	
Health	29,190	30,597	33,615	*9.9%*	*1.6%*	*0.2%*	
Capital Expenditure	*2,37,718*	*2,47,024*	*2,68,866*	*8.8%*	*12.8%*	*1.6%*	
Total Expenditure	**17,85,391**	**19,78,061**	**20,98,183**	*6.1%*	*100.0%*	*12.3%*	

Note: The table provides only select segments of the revenue expenditure

Source: Ministry of Finance, FICCI analysis

With respect to other major recurring expenditure, the salary component is expected to be somewhat higher, owing to impact of pay commission rewards. In its medium term expenditure framework, the government expects the impact of pay commission increase to decline gradually in the medium-term rolling period.

Outlook on revenue collection in 2017-18

It is anticipated that Finance Minister could lower direct tax rates in the Union Budget 2017-18, with a view to boost consumption and investment demand in the economy. This would have a bearing on total direct tax revenue, unless lower rates induce better compliance and widen the tax base. The number of taxpayers is already expected to rise following the demonetisation move, owing to aggressive drive of authorities against tax evaders and insights from data on cash deposits. Lower tax rates but increase in taxpayers is likely to have a positive impact on the direct tax revenue in 2017-18.

It is expected that indirect tax revenue will drive the tax revenue growth in next fiscal. The likely implementation of GST from July 2018 should help in enhancing the indirect tax revenue. However, a downside risk emanates from the likely rise in oil prices, which could trigger fuel duty cuts and significantly lower the tax collections from petrol and diesel.

In the BE 2016-17, direct tax revenues are estimated at 5.6% of GDP and indirect tax collections at 5.2% of GDP, implying gross tax revenues at 10.8% of GDP. The medium term fiscal policy statement has projected a slight increase in this ratio for 2017-18 at 10.9%. As discussed in the earlier section, the tax collections for 2016-17 are expected to exceed the budget estimates. Given better growth prospects, improved compliance and

[15] *http://timesofindia.indiatimes.com/india/500-central-schemes-to-go-DBT-way-next-fiscal-year/articleshow/54928603.cms*

implementation of GST, it is thus expected that tax revenue collections for 2017-18 should also be significantly higher than the projected levels in the medium-term fiscal policy statement. Non-tax revenue receipts for 2017-18, according to the medium term fiscal policy statement, are expected at 2% of GDP as against 2.1% of GDP under BE 2016-17. The projection takes into account the available shelf of spectrum due for auction in next fiscal and assumes disinvestment receipts of Rs 40,000 crore, lower than the BE 2016-17.

Outlook on fiscal deficit target in 2017-18

The fiscal deficit target of 3% could be revised in light of the recently submitted report of the Fiscal Responsibility and Budget Management (FRBM) panel, chaired by Mr N K Singh. It is widely anticipated that the report could recommend relaxation of fiscal deficit target. Alternatively, the FRBM panel could propose a shift from a point to a range of target (say 3.0% - 3.3%). The Finance Minister, in the latest budget, could consider some of the recommendations of the report and accordingly arrive at the fiscal deficit target for 2017-18.

In light of the expected expenditure and need for greater push to productive and social expenditure (especially on construction, health, education and social security schemes), the fiscal deficit target of 3% could be challenging. It is thus recommended that while the Finance minister should continue to focus on fiscal consolidation with a downwards direction in fiscal deficit, the target of 3% could be slightly relaxed.