Seminar Report

BUDGET 2017-18 WITH SPECIAL REFERENCE TO DEFENCE ALLOCATION

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The Centre for Land Warfare Studies (CLAWS), New Delhi, is an autonomous think tank dealing with contemporary issues of national security and conceptual aspects of land warfare, including conventional and sub-conventional conflicts and terrorism. CLAWS conducts research that is futuristic in outlook and policy-oriented in approach.

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EXECUTIVE SUMMARY

The Indian economy has emerged as a bright spot in the world economy, becoming one of the fastest growing large economies in the world. The 7.6 per cent growth in the Gross Domestic Product (GDP) at constant market prices in 2015-16, according to the advanced estimates of the Central Statistics Office, compares favorably with growth in the previous three years; 7.2 per cent in 2014-15, 6.6 per cent in 2013-14, and 5.6 per cent in 2012-13. It is noteworthy that this growth is estimated to be achieved despite subdued global demand that dampened India's exports significantly, and two consecutive below-normal monsoons that impacted farm output and productivity.

The most important issue that faces the defence ministry is the fact that whether the latest allocation is adequate to meet the security needs of the country? The noticeable fact is the further decline in the defence budget's share in both central government expenditure and the GDP. With a share of 1.56 per cent of the estimated GDP of 2017-18, the defence budget is the lowest since 1956-57. Another worrying aspect is the further increase in the share of the revenue expenditure in the total defence budget. The increase is primarily due to the hike in the manpower cost of the armed forces, which accounts for over 83 per cent (or Rs 11,071 crore) of the overall growth of Rs 13,291 crore in the defence budget. The result is a debilitating effect on two vital elements of the defence budget: revenue stores and capital modernization which together play a vital role in the operational preparedness of the armed forces. This does not augur well, especially when there exists a huge void in India's defence preparedness, and the armed forces have grave shortages in many areas ranging from ammunition, assault rifles, bullet-proof jackets, night fighting-devices to howitzers, missiles, helicopters, fighters, and warships. Thus, for the forces to be adequately prepared, the present ratio needs to change for the better, for which allocation under revenue stores and capital modernization needs to be augmented substantially.

DETAILED REPORT

Introduction

The Union Budget of India, also referred to as the *Annual Financial Statement* in Article 112 of the Constitution of India, is the annual budget of the country. Till date it used to be presented each year on the last working day of February by the Finance Minister of India in Parliament. Departing from the colonial era tradition of passing the budget on the last working day of February was part of the British administration in India that the Indian government inherited post independence. In November 2016, Prime Minister Narendra Modi announced a shift in the date of budget. In 2017 therefore, the budget got presented on 1 February. The year 2016 has seen two major economic decisions taken by the government, one being the Goods and Services Tax and the second being the demonetization move announced on 8 November. While people are still uncertain about the impact of both these decisions, it is the budget of 2017 that was most awaited in determining the government's way of dealing with the current financial situation in the country. The other major change which the Union Budget 2017 witnessed, was the merger of the Railway Budget with the Union Budget, marking a dramatic move away from the 92-year-old practice of presenting a separate Railway Budget ahead of the Union Budget.

Objectives of the Seminar

The seminar discussed issues related to the current year's budget and the defence budget in particular. It attempted to assess the current environment and debate the requirements of the future.

The objectives were as follows:

- Understand the Budget from the macro-economic perspective.
- Key changes from the previous year's budget and current priorities.
- Adequacy of allocation and possible implications.

- Evolving security environment as a signal for budget priorities in the medium-term.
- Comparison of budget with general standard practices in other countries.
- Whether there are sufficient allocations to meet the requirements of modernization.
- Implications of digitization.

Speakers (In order of Presentation)

- **Macro-economic Impact of the Union Budget** – Professor Rajeev Kumar, CPR and Pahle India Foundation
- **Key Changes from Previous Years and Priorities** – Dr Ashok Lahiri, Ex CEA, Government of India
- **Analysis of Defence Budget** – Major General Anil Puri, VSM, DDG FP
- **Impact of Demonetization and Digitization** – Deviprasad

Macro-economic Impact of the Union Budget

The 2017 Union Budget, presented by the current Finance Minister Arun Jaitley on 1 February 2017 focused on certain key areas—the farming sector, the rural population, the youth, the poor and under-privileged health care, infrastructure, the financial sector for stronger institutions, speedy accountability, public services, prudent fiscal management, and tax administration for the honest. The first objective of the Budget seemed to be signalling intent of continued fiscal consolidation. It is quite an achievement that financial year (FY) 2018 would be the sixth consecutive year of continuous decline in central fiscal deficit despite different phases of political and economic cycles.

The ability of the Budget to kick-start the private investment cycle was another major consideration. It is a welcome development that the Budget proposes a higher growth in capex spend of 11 per cent compared to the lower growth in revenue spends. In particular, allocation of funds to infra ministers are up 14 per cent from the revised estimates of the FY 2017. However, one has to keep in mind that some of the ministries, like roads, were unable to spend their allocated funds in the FY 2017. So, the implementation ability and the absorptive capacity need to be enhanced for the higher capex spend to have its desirable impact.

The Union Budget achieved the right balance between providing a growth impetus and maintaining fiscal prudence. It comprehensively addressed all areas of socio-economic priority: farmers, poor and under-privileged sections of the society, infrastructure development and strengthening of the financial sector. The Union Budget rightly prioritized investment in infrastructure and the rural economy. The increase in capital spending and the proposals for investment in a range of areas from affordable housing to roads and railways would not only have a multiplier impact on other sectors of the economy but also enhance employment generation and make the growth inclusive. The thrust on digital transactions will increase the size of the formal economy and also make the payment systems more convenient and efficient. The tax measures are aimed at improving direct tax mobilization by broadening the tax base and improving tax administration. Giving infrastructure status to affordable housing, can improve resource allocation to the sector, thereby reducing cost of capital for developers. Moreover, the changes under Section 80 IB of the Income Tax Act with respect to size of units (built up area to carpet area), timeframes for project completion (3 years to 5 years) and geography (up to 60 square metre beyond the 4 metros) will encourage greater participation by organized developers in the affordable housing segment, thereby catalyzing development and reducing the supply gap. One of the biggest announcements is the withdrawal of service charge on rail tickets booked through the Indian Railway Catering and Tourism Corporation (IRCTC). This will not only lead to more bookings but will enable the consolidation of a digital economy. It is also encouraging to note the measures that will be incorporated to make the railways friendlier for the disabled. With emphasis on a digital economy, by introducing measures like elimination of service charge while booking rail tickets on IRCTC, launching DigiGaons to facilitate employment and skilling.

Key Changes in the Budget of 2017-18 from Previous Years and Priorities

Union Budget 2017 proposed to offer many benefits to small and medium enterprises (SME) in the country. Income tax on companies with annual turnover of less than Rs 50 crore per year has been reduced to 25 per cent from the earlier 30 per cent. The lending target for Pradhan Mantri Mudra Yojana (MUDRA) has been doubled to Rs 2.44 crore for the FY 2017-18. The Finance Minister Arun Jaitley also decided to continue the preferential taxation announced last year. Under the scheme of presumptive taxation, 8 per cent of the turnover is counted as income in case if the taxpayers' turnover is less than Rs 2 crore. According to the new proposal this is brought down to 6 per cent. Budget 2017 triggered a relief rally on the bourse as investors rejoiced the government's decision to retain the existing provision on long-term capital gains tax exemption on stocks. During the run up to the Budget there were talks that the government was considering increasing the holding period for Long Term Capital Gains for tax exemption from 12 months to 36 months. On another front, the Finance Minister Arun Jaitley reduced the time period required to qualify for the long-term capital gains on property from 36 months to 24 months. The Finance Minister has also announced the abolition of Foreign Investment Promotion Board (FIPB). This is seen as a big positive step in the form of reduced bureaucracy. This is certainly a sentiment booster. The Budget's focus on infrastructure spending and limited populism also worked as big positive for the investors. A clear focus on Fiscal Responsibility Budget Management framework and low interest rates should further bolster the corporate profitability and the reward investors in return. The old demands such as reduction or removal of Securities Transaction Tax and Commodities Transaction Tax however, did not materialize. There was also expectation that the Finance Minister will raise the investment limit under Section 80C of the Income Tax Act. However, this too remained unchanged.

The Budget provided a boost to small businessmen by offering lower income tax rates. Budget 2017 proposed to continue with the scheme of presumptive taxation. Instead of presumptive tax at 8 per cent of the turnover it will be 6 per cent for the turnover received by non-cash means, if the turnover is less than Rs 2 crore. Due to slow economic recovery in India and demonetization in the last quarter of the current year (CY) 2016, the businessmen community was under pressure. On the individual front, small businessmen may benefit with lower tax for income up to Rs 3.5 lakh, the bigger ones with income more than Rs 50 lakh will see higher income tax due to additional surcharge of 10 per cent. As the MUDRA lending target is doubled to Rs 2.44 crore for the FY 2017-18, the businessmen will find it easy to raise loans for their business. Fiscal prudence by the government will further ensure that the interest rates in the economy will remain low which will help the profitability of the business. There was also hope that there would be an increase in service tax exemption limit to Rs 25 lakh. However it did not happen.

Analysis of Defence Budget

	Revenue Expenditure (Rs. in crore)	*Capital Expenditure (Rs. in crore)*	*Total (Rs in crore)*
1915-16	145937	79958	225895
1916-17 (BE)	162759	86340	249099
2016-17 (RE)	168635	79370	248005
2017-18 (BE)	175861	86529	262390

The Table above shows the breakup of the defence budget for the last 3 years. The noticeable aspect in the table is the underutilization of the capital budget of 2016-17. The surrendered amount is largely absorbed in the revenue expenditure. Among the defence services, the Indian Army with a budget of Rs 1,49,369 crore got the largest share in defence budget, followed by the Air Force, Navy, Defence Research and Development Organisation (DRDO) and Ordinance Factories (OFs). This kind of share for the Army is mainly because of its overwhelmingly numerical superiority over the sister services. Army has more 85 per cent of the uniformed personnel; as a result bulk of the Army's Budget goes into meeting the pay and allowances of the personnel. In 2017-18, only 17 per cent of Army's total allocation has been earmarked for capital expenditure. The comparative figures for the Air Force and Navy are 58 per cent and 51 per cent, respectively. As far as modernization is concerned the overall allocation in the 2017-18 Budget has declined, although slightly, over the previous allocation.

The small increment of 5 per cent in the official Defence Budget is grossly inadequate particularly in view of the huge voids existing in military capability and the diminished and incremental effect on modernization and operational preparedness. There is a need to enhance resources substantially, particularly under two important heads of the Defence Budget – stores and capital procurement – which are under a lot of pressure in the last several years with a huge negative consequence on India's defence preparedness.

Impact of Demonetization and Digitization

The government's decision to ban Rs 500 and Rs 1,000 notes on 8 November 2016, to curb black money and terrorism financing through counterfeit notes has evoked mixed reactions. One of the prime targets of this action was Black Money and was supposed to be one of the solutions. Demonetization has affected the daily lives of millions, especially those in what is called the informal sector—domestic workers, small traders, and farmers—but what its impact will be in the long-term remains to be seen. In the short-term, demonetization has led to the rapid adoption of e-wallets, and credit and debit cards as a means of payment. Such digital payments have in a large way replaced cash transactions at least in urban areas. The other impact of demonetization has been the fact that a majority of borrowers have returned their borrowed money along with the fact that a huge number of Jan Dhan accounts have seen large deposits. Many municipalities have seen huge tax collections. Many economists and socio-political researchers also believe that the country's path to digitization was smoothened and the time to achieve a cashless society has been compressed. While the jury may be out on whether the Government of India will achieve its initial objectives of the demonetization exercise, as the programme progresses it has become increasingly clear that the entire exercise has clearly fast forwarded the programme of 'digitization of the Indian economy'. We can see all around us, hitherto small traders and businesses which were primarily operating in cash, opening bank accounts and now have started operating with POS machines acquired in a hurry as well as e-wallet payments. The labour force working in the informal sector has also realized that the way forward is to open bank accounts and carry on with their lives. The banks have also started taking steps for rapid digitization by adopting villages as well as using the payment infrastructure provided by the National Payments Corporation of India (NPCI) for including using the infrastructure for USSD technology including micro auto teller machines (ATMs) for payments to be made using an ordinary non-featured phone apart from smart phones.

Conclusion

While recognizing the fact that economic growth is faltering, the Budget has used the lone engine at its disposal (government spending) to spur economic growth by focusing on manufacturing, particularly in labour-intensive sectors. To sustain this growth story the focus needs to shift to the agriculture sector. With an effort to revive the agriculture sector, the total allocation for rural, agricultural, and allied sectors has been increased by 24 per cent. As far as Public Sector Undertakings (PSUs) were concerned, the government has estimated that it will receive an amount of Rs 72,500 crore from selling stakes in PSUs. However, a successful disinvestment programme needs rising stock markets, which is a big assumption. In conclusion the Budget had done a balancing act between upping government spending while at the same time keeping in mind the need to not deviate from the path of fiscal consolidation.

PROGRAMME

0930–1000h	**Registration and Tea**
1000–1005h	**Welcome Remarks:** Lt Gen BS Nagal, PVSM, AVSM, SM (Retd), Director CLAWS
1005–1035h	**Union Budget – Macro Economic Perspective, Main Features and Developmental Spending –** Prof Rajeev Kumar, CPR & Pahle India Foundation
1035–1105h	**Implications of Allocations –** Dr Ashok Lahiri, Ex CEA, GoI
1105–1115h	Q&A
1115–1145h	**Tea**
1145–1245h	**Analysis of Defence Budget – Maj Gen Anil Puri, VSM, DDG FP**
1245–1310h	**Impact of Demonetisation and Digitisation – Mr Deviprasad**
1310–1330h	Q&A and Closing Remarks
1330–1430h	**Lunch**