Addressing the Economic Slowdown

What is the issue?

- India is at a critical stage in terms of its economy with increasing fiscal deficit and growth not happening at required levels.
- In this backdrop, here is a look at the various recourses that the government could take.

What should the government do on the investment side?

- The private sector, in its reaction to the economic slowdown, has lost confidence and is investing less.
- This is only aggravating the economic crisis.
- An RBI report suggests that business confidence, consumer confidence and capacity utilisation are down.
- The government thus has to garner resources and give a boost to the economy by increasing its investments.
- But, the slowdown has adversely impacted growth of tax revenues.

What is required on the tax revenues side?

- The government calculated tax revenues on the assumption of a 12% nominal growth.
- But, it has been around only 9%, both in 2018 and 2019.
- So, in 2018-19, tax revenue was short by about Rs. 1.5 lakh crore.
- However, this was not reflected in the planning for the 2019-20 Budget.
- So, certainly, the revenue shortfall for the Centre will be even larger than last year when it was around Rs. 2 lakh crore.

How does this affect the states?

- The States get 42% of the tax revenue, and so they will get Rs. 84,000 crore less this year.
- Further, the concessions in corporate taxation of Rs. 1.45 lakh crore will also mean Rs. 58,000 crore less revenue for the States.
- While the Centre has obtained Rs. 1.76 lakh crore from the RBI's reserves, no such assistance is available to the States.
- The Centre will also get the proceeds of disinvestment but that is not shared with the States.

- In essence, the States will have a larger shortfall in resources than the Centre.

How can the states manage this?

- With the current GST structure, revenue from indirect taxes cannot fill the resource gap of the states.
- The States have also been complaining that they are not getting the funds that are due to them from the Centre.
- The Centre has partly responded to this by transferring more, but that raises its deficit.
- The Centre is required to give the States their share of Integrated Goods and Services Tax (IGST).
- It should also compensate the states if the revenue growth of State Goods and Services Tax is less than 14%.
- This could come from the cess collected on sin goods and luxury goods.
- One of the big contributors to GST has been the auto sector.
- But, with sales falling in the recent period, collections have declined.
- The Centre is apparently holding back the States' share of IGST and arguing that the cess collection is inadequate to compensate the States for their shortfall.

What are the challenges in addressing this?

- The dilemma is that if the GST rates are increased, prices would rise and demand would further slump.
- This would further aggravate the economic slowdown and shortfall in revenues.
- One of the suggestions has been to raise the 5% slab to 6% or 10%.
- It has also been suggested that taxes on petro goods and liquor for human consumption are under the purview of the States.
- They can raise tax rates on these items as per the demands of the situation.
- But, these will be inflationary moves and demand would fall.
- The problem is compounded by the shortfall in direct tax collections.
- This is both the result of corporate tax concessions and the slowing economy.
- Income-tax rates cannot be raised now since that would be seen as inequitable.

- There are demands to reduce income-tax (I-T) rates to boost demand in the economy.
- However, a cut in I-T rates will largely benefit less than 2% of the citizens who pay a significant amount of income-tax.
- They are well-to-do and unlikely to increase consumption.

- Similarly, the cut in corporate tax rates will not boost demand since neither investment nor consumption will rise.
- The concessions to the corporate sector have narrowed the fiscal space available without raising demand.

What lies ahead?

- The government has to garner resources and give a boost to the economy by increasing its investments.
- Clearly, investment will rise only when capacity utilisation improves.
- So, the government should cater to the needs of the unorganised sector where the problem actually originated from.
- If the unorganised sector is separately accounted for, the economy is in a recession and not just a slowdown.
- The fiscal deficit at all levels of government is already high, so a policy decision is needed on how much more it can be.
- If the fiscal deficit is allowed to rise further, the extra resources can be used to boost incomes in the unorganised sectors through greater public investments.

Source: The Hindu

SHANKAR IAS PARLIAMENT
Information is Empowering