Reforming Subsidies

How consumption will get affected due to the pandemic?

- India’s growth forecasts are now 1-2 percentage points lower due to the second wave of coronavirus.
- But the actual economic toll may be higher and consumption demand may remain subdued longer than currently foreseen and there are sufficient reasons to justify this fact.
- One, lethality of virus and its spread, severe human and economic scarring, fear-persistence due to the anticipated third wave, and lack of guaranteed vaccination will affect the consumption.
- This is in addition to the drained financial strength from health expenses and income losses, increased indebtedness.
- Two, the supply-side stress are also affecting the consumption pattern.
- MSMEs are affected by shutdowns which affect their sales, raw material procurements and supply chain linkages.
- Large firms are impacted by labour shortages due to migration, infections, lowered sales and future demand uncertainties.
- As a result there is feeble demand for credit and loan restructuring in the banking sector.
- Three, it is expected that reopening the economy will be accompanied with more infections in forthcoming months which will reduce demand.

What are the steps to be taken?

- It is advocated that budgeted expenditures should be reoriented to meet the emergency health and income requirements.
- The government should act along the structural lines and prepare a fiscal space for this emergency of unknown magnitude and longevity.
- It must follow the efforts of deepening the revenue-expenditure reforms as it did last year.
- This involves reforms to agriculture marketing and institutional structures, accounting transparency by bringing subsidy arrears (food, fertilisers) on the balance sheet, raising LPG prices.

What is the issue in this?

- Recently, there has been regression with the increase in fertiliser subsidies instead of revising issue prices.
- This can derail the reform momentum and diminish the credibility of effort and commitment to improve finances.
- Therefore any reform should aim to reduce subsidies over the medium-term in a modest fashion.
- For example, it can choose between different ways to moderate the food subsidy, i.e. streamlining the beneficiary eligibility and numbers or revising the issue prices or a mix of both.
- Other welfare and often populist expenditures, at both state and central levels should also be reviewed.

What is the inference?

- This stretching pandemic of unknown duration and spread will worsen the employment-income situation of the people.
- RBI cannot alone lead with its monetary measures and fiscal policy measures needs to be taken.
- With general government debt touching 90% of GDP, debt sustainability and macroeconomic stability are now a binding restriction.
- The government should revise the fiscal rules (the FRBM Act) or present a detailed medium-term fiscal adjustment plan.
- So any action which is taken should impart strength and confidence to overcome revenue shortfalls, reduce the exceeding expenditure limits without raising the debt sustainability concerns.

Source: Financial Express

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