**GE.4: INDIAN ECONOMY-II**

**UNIT-I**

**MACROECONOMIC POLICIES AND THEIR IMPACT**

**FISCAL REFORM MEASURES:**

Fiscal Policy refers to the taxation and expenditure decision of government. It includes various policies like export policy, investment policy, disinvestment policy, expenditure policy etc. to achieve the development of nation. Broadly, during the first 30 years of independence, between 1950 and 1980, the fiscal deficits of both the Central and the State Governments were not excessive. There was a significant deterioration in the fiscal situation in the 1980s, accompanied by large and automatic monetisation of government deficits. The fiscal reforms in India address both revenue as well as expenditure related policies.

**Goals of Fiscal Policy:** The major goals of fiscal policy are:

* [Economic Growth and Development](http://www.papertyari.com/general-awareness/economics/economic-growth-economic-development/)
* Price stability and [inflation](http://www.papertyari.com/general-awareness/economics/inflation-types-effects-causes-inflation/) control
* Social stability

**Fiscal Reforms in India**

The government of India has initiated fiscal reforms in India from time to time to achieve the above stated goals but major fiscal reforms were started aftermath of 1991 economic crisis. The focus is on to raise revenue through taxation and improving the quality of public expenditure.

**Revenue Reforms**

Until 1980’s the direct tax rate was very high which induced people to evade taxes and create Black economy. Tax rate of income tax and corporate tax have been lowered to moderate level so that tax buoyancy is achieved through better compliance and minimum exemptions.

* Excise duties and custom duties have been progressively reduced to make Indian Exports competitive in international market.
* Service tax was introduced
* GST
* Fringe Benefit Tax
* Minimum Alternate Tax (MAT)

**Expenditure Reforms**

* [FRBM Act](http://www.papertyari.com/general-awareness/finance/frbm-act-explained/)
* Chelliah committee
* TRC 1991

**Fiscal Reforms 1950’s**

The objective of economic policy during the 1950s and 1960s was mainly to increase the growth rate of the economy through increasing public investment and overall economic planning. Taxation was used as an instrument for reducing private consumption and for transferring resources to the Government to enable it to undertake large-scale public investment in an effort to spur economic growth. Furthermore, taxation policy was geared towards achieving the economic objectives of:

* promoting employment through grant of tax incentives to new investment
* reducing inequality through progressive taxes on income and wealth
* reducing pressure on balance of payments through increase of import duties
* stabilizing prices through tax rebate in excise duties on consumption goods

The fiscal deficits of both the central and the state governments were not excessive. This was a period of revenue surplus in general.

### Fiscal Reforms 1970’s

Fiscal policy during the 1970s consciously focused on achieving greater equity and social justice and both taxation and expenditure policies were employed towards this end. Accordingly, income tax rates were raised to very high levels, with the maximum marginal rate of income tax moving up to 97 per cent and, together with the incidence of wealth tax, it even crossed 100 per cent

### Fiscal Reforms 1980’s

During the 1980s, Indian public finances were in a state of disarray with the fiscal pattern destabilising the relationship between the economy and the budget. This resulted in persistently large deficits which were seemingly intractable. Considerable fiscal deterioration took place during the 1980s and eventually became unsustainable, though the growth rate did rise significantly with enhancement in public investment in infrastructure. During this phase, expenditure of the Government was seen as an instrument having a bearing upon aggregate demand, resource allocation and income distribution. The Government sought to reduce its deficit through tax increases. Customs duties were hiked to augment revenue and to protect domestic industry. There was a structural change in the government budgets during the 1980s. The emergence of revenue deficit in 1979-80 in the Centre’s Budget continued to enlarge during the 1980s, raising concerns over the rising public debt and interest payments and the consequent constraint on the availability of resources for meeting developmental needs. The 1980s witnessed a steady increase in market borrowings along with an increase in Reserve Bank’s support to such borrowing, thus compromising monetary policy

**Fiscal Reforms since 1990’s**

India’s reform program included wide-ranging reforms. These reforms can be classified as:

* **Banking Sector Reform**: It includes measures like:
  1. Liberalization, like dismantling the complex system of interest rate controls, eliminating prior approval of the Reserve Bank of India for large loans, and reducing the statutory requirements to invest in government securities;
  2. to increase financial soundness, like introducing capital adequacy requirements and other prudential norms for banks and strengthening banking supervision
  3. To increase competition like more liberal licensing of private banks and freer expansion by foreign banks
  4. Reduced CRR, SLR
  5. Introduction of prudential norms
  6. The Board for Financial Supervision was The Board for Financial Financial Supervision Supervision was set up within the RBI to attend exclusively to supervisory functions
  7. Removed barriers for entry of private sector banks
  8. Opening of payments bank and small finance banks
* **Capital Market Reforms**: several steps have been taken after 1980’s to attract investments from foreign investors. This resulted in significant expansion of capital market in the 1980s. the market capitalization of companies registered in BSE rose from 5% of GDP in 1980s to 13% in 1990s. The financial market was further liberalized after Narasimham Committee were accepted by government. [SEBI](http://www.papertyari.com/general-awareness/functions-sebi/), which was originally established as a non-statutory body in 1988, was established as full-fledged market regulator. Based on Chandrashekhar Committee recommendations, Sebi, in June 2014, merged different classes of investors such as  FIIs, their sub-accounts and qualified foreign investors (QFIs) into a  new category called foreign portfolio investors (FPIs) and simplified the registration rules for FIIs’ entry into the capital market.

**FISCAL RESPONSIBILITY AND BUDGET MANAGEMENT ACT (FRBM ACT)**

(FRBM Act) was introduced in Parliament as the FRBM Bill in December 2000. It seeks to foster fiscal discipline on the Central Government and achieving a balanced budget with effective revenue management. The Act was passed on August 26, 2003, therefore it is also called Fiscal Responsibility and Budget Management Act (FRBMA), 2003. FRBMA was brought into effect from July 5, 2004.

**Revenue Deficit, Primary Deficit, Effective Revenue Deficit**

Before we start the discussion of FRBM Act, you need to understand following terms:

* **Revenue Deficit (RD)**: It is the difference between revenue expenditure and revenue receipts.
* **Effective Revenue Deficit (ERD)**: It is the difference between revenue deficit and grants to states for creation of capital assets.
* **Fiscal Deficit (FD)**: It is the difference of total expenditure of government and total receipts excluding borrowings.
* **Gross Fiscal Deficit (GFD):** It is the excess of total expenditure including loans net of recovery over revenue receipts (including external grants) and non-debt capital receipts
* **Primary Deficit (PD)**: It is the fiscal deficit minus the interest payments.

**FRBM Act Targets**

The targets that were set in original version of act were:

* Reduction and Elimination of revenue deficit by 2008-09
* Thereafter build up adequate revenue surplus
* Reduction of fiscal deficit to no more than 3 per cent of GDP at the end of 2008-09
* Reduce the Gross Fiscal Deficit (GFD) by March 31, 2008

**Latest Changes in FRBM Act with Union Budget 2021**

1. The target of Fiscal deficit at 6.8% of GDP in 2021-22.
2. In 2021-22, the total expenditure proposed by the government is Rs 34,83,236 crore.
3. 123 percent change is seen in the expenditure allocated for [Jal Jeevan Mission](https://byjus.com/free-ias-prep/national-water-mission/).
4. The budget allocation for the welfare of women has seen a drop of 26 percent in comparison to revised estimates 2020-21.
5. 52.7 percent increase in allocation for welfare of SCs and 50 percent for STs.
6. The allocation for the North Eastern region has been increased by 32.7 percent.

***(to be continued)***