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Union Budget 2015 – Prospects for Big Bang Reform

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India's Union Budget has become a vehicle for policy direction and reform statement since 1992, when the economic reform package of liberalisation, privatisation and globalisation became the mantra of good governance. Going beyond a dry statement of receipts and expenditures of government, the Budget signals the specific intent of the government with regard to funding of major initiatives and raising of resources for them. Policy directions in the Union Budget focus on tax reform and duty structure rationalisation, expenditure management and incentives for savings and investment, for households, firms and industry sectors.

The expectations from the Modi Government continue to be high for investors and households alike. The projected spike in economic growth to 7 per cent plus (prior to the recent revision of GDP methodology) will depend a lot on the content and intent of the Union Budget 2015. As the first full budget of the NDA-II, the 2015 Budget is an opportunity for credible reform signals – reducing the centre's fiscal deficit to 4.1 per cent, improving the tax collection so as the bring the central tax to GDP ratio above 10 per cent in the medium term, greater incentives for investment in core sectors – energy (including renewables), infrastructure, manufacturing and new ventures in the services sector and the IT economy.

The Railway Budget is the first of the three major policy statements by the Government. The Debroy Committee findings on organisational reform and steps to attract private investment (without privatising) in the expansion and up-gradation of railway infrastructure would be reflected in the Railway Minister's speech. The challenge for the railway budget would be to continue to bridge the revenue deficit by rationalising the fare structure and curtailing the extent of the cross-subsidy of passenger fares by freight fare.

The Annual Economic Survey will not only address issues of GDP estimation (new series) but also provide an assessment of the exact state of the economy in the past year (FY 2014-15) on key indicators such as inflation, forex reserves, trade deficit and the baselines and goals for new initiatives such as Swachchh Bharat, Jan Dhan, Digital India and Smart Cities. It would be an opportunity to set monitorable outcomes on which progress in years ahead can be tracked. Given the new direction and impetus of the NITI Aayog, one can expect cross-fertilisation of input between Chief Economic Advisor Arvind Subramaniam and Vice-Chairman Arvind Panagariya. The meeting of minds between the two Arvinds' will also decide the feasibility of the populist agenda of the third "Arvind"–Kejriwal?

Humour aside, the Union Budget policy signals would also be relevant for the states' budgets insofar as funds' allocation under the national flagship programmes are now expected to flow through state governments. This would not happen immediately, but the discourse in the Budget statement is expected to be strong on "cooperative federalism" and direction for reform at the state level. It is to be noted that the feasibility of critical steps such as the Goods & Services Tax (GST) depends upon the states (especially Tamil Nadu, Maharashtra and Karnataka which would take a haircut with regard to their current tax revenues). Therefore, the Union Budget 2015 is an opportunity to reach out and expand the federal constituency – and the Finance Ministry meetings with State Governments, bankers and other key stakeholders should be seen in this light.

Finally, we come to the question of political feasibility of a reform budget. It is widely argued that 2015 being a year where no major states are going for elections, it is imperative to push through bold reform measures this year. It is easy to agree with the view for urgency, but not with haste. “Big Bang reform” would of course accelerate the flow of investment – foreign and domestic. However, there should be considerable thought and abundant caution with regard to the fine print. “Make in India” should also include practical steps for greater ease of business – including measures to be taken by State Governments to facilitate entry, operation and exit of firms.

As far the point about “election year” is concerned, there is a case for a revisionist view. Evidence at national and state levels indicates that, in grosso modo, there is insufficient correlation between election year, reform statement and electoral outcomes. While it is true that the electoral reverses suffered by incumbent governments can always be laid at the door of “reform”, it also true that the electoral reverses happen in non-reform years and governments in non-reforming states do get voted in and out almost cyclically. Between 1991 and now, no national government lost the election because of a reform budget. 1996, 1998, 2004, 2009 and 2014 - none of these years (and the year preceding in “vote on account” cases when elections were held in April-May-June) witnessed major reform signals. In “reforming states” such as Andhra Pradesh, Gujarat, Chhattisgarh and Madhya Pradesh, the reforming regimes were invariably re-elected for a minimum second term, during the period 1993-2014.

In sum, the electoral experience of India and its states shows that “good economics is indeed good politics”. We must therefore moderate expectations from the Union Budget only on technical grounds of resource availability and feasibility of implementation. If a reform measure meets the above two criteria, it certainly merits consideration by the Finance Minister and his team!

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