Budgetary developments in 2003-04

2.6 The macroeconomic situation that preceded the presentation of Budget 2003-04 remained uncertain, with global recovery remaining sluggish, threat of terrorism looming large and the effect of drought spilling over. Budget 2003-04 enunciated five core priorities, viz., poverty reduction, infrastructure development, fiscal consolidation, development of agriculture and enhancing manufacturing sector efficiency. Fiscal deficit of the Central Government was budgeted at 5.6 per cent of GDP (Rs.1,53,637 crore). Revenue deficit was budgeted at 4.1 per cent of GDP as compared with 4.4 per cent of GDP in the previous year. The reduction in revenue deficit was budgeted to be achieved from higher growth in revenue receipts and lower growth of revenue expenditure. Proposals contained in the Union Budget 2003-04 are discussed below under different heads.

Revenue receipts

2.7 Revenue receipts (net to the Centre) in 2003-04 were budgeted to increase by 9.6 per cent to Rs. 2,53,935 crore compared with Rs.2,31,748 crore in 2002-03 (Table 2.2). The budgeted increase in revenue receipts was sought to be achieved through growth in net tax revenue by 15.5 per cent. Non-tax revenue was budgeted to decline by 3.5 per cent on account of lower interest receipts from States. With tax reforms, the share of direct taxes in total tax revenue of the Centre has been increasing. The share of direct taxes in gross tax revenue increased from 19.1 per cent in 1990-91 to 38.4 per cent in 2002-03. In keeping with the tax reforms underway, the share was budgeted to remain at 38.1 per cent in 2003-04 (BE). The share of indirect taxes was budgeted at 61.3 per cent compared with 60.7 per cent in the previous year (Table 2.3).

2.8 With expenditure-GDP ratio already low in India by international standards and rigidities in compressing expenditure, improvement in tax collections is crucial for fiscal consolidation. The tax-GDP ratio continues to remain low. What is a matter of grave concern is that the ratio has declined and remains at a lower level even as compared with the pre-reform year of 1990-91. The ratio for the Central Government declined from 10.1 per cent in 1990-91 to 8.8 per cent in 2002-03, which was sought to be improved to 9.1 per cent in 2003-04 (BE). The decline in the tax-GDP ratio was entirely on account of the decline in the ratio of indirect taxes to GDP. The indirect tax-GDP ratio witnessed a sharp decline from 7.9 per cent in 1990-91 to 5.3 per cent in 2002-03. Among the indirect taxes, the ratio of customs duty to GDP halved from 3.6 per cent in 1990-91 to 1.8 per cent in 2002-03. The reduction in the ratio of customs duty as a proportion of GDP was on account of a phased reduction in the peak rates as part of tax reforms to improve resource allocation, improve efficiency and make Indian manufacturing globally competitive. There was also a decline in the ratio of excise duty collections to GDP by about one percentage point on account of duty rationalisation. The uncompensated loss of customs and excise revenue by other sources resulted in a lower tax-GDP ratio. The introduction of tax on services in 1994 and its gradual extension to 58 services and increase in the rate of tax from 5 per cent to 8 per cent along with on-going reforms in direct and indirect taxes was expected to result in an improvement in the tax-GDP ratio in 2003-04.

Tax measures

2.9 One of the important commitments made in the Budget was to move away from a suspicion-ridden, harassment generating and coercive regime to a more trust-based regime with a firm belief in voluntary compliance. The guiding philosophy in the tax measures was a harmonious mix of stability and continuity. Rates of income tax and corporation tax were left unchanged.

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Table 2.3 : Sources of tax revenue								
	1990-91	1998-99	1999-2000	2000-01	2001-02	2002-03	2003-04 (BE)	2003-04@ (Prov.)
				(Rs. crore)				
Direct	**11024**	**46600**	**57958**	**68306**	**69197**	**83080**	**95714**	**105236**
PIT	5371	20240	25654	31764	32004	36858	44070	41441
CIT	5335	24529	30692	35696	36609	46172	51499	63608
Indirect	**45158**	**95871**	**112450**	**118681**	**116125**	**131284**	**154141**	**147279**
Customs	20644	40668	48420	47542	40268	44852	49350	48625
Excise	24514	53246	61902	68526	72555	82310	96791	90764
Service tax	0	1957	2128	2613	3302	4122	8000	7890
Gross tax revenue #	**57576**	**143797**	**171752**	**188603**	**187060**	**216266**	**251527**	**254438**
			Tax revenue as a percentage of gross tax revenue					
Direct	**19.1**	**32.4**	**33.7**	**36.2**	**37.0**	**38.4**	**38.1**	**41.4**
PIT	9.3	14.1	14.9	16.8	17.1	17.0	17.5	16.3
CIT	9.3	17.1	17.9	18.9	19.6	21.3	20.5	25.0
Indirect	**78.4**	**66.7**	**65.5**	**62.9**	**62.1**	**60.7**	**61.3**	**57.9**
Customs	35.9	28.3	28.2	25.2	21.5	20.7	19.6	19.1
Excise	42.6	37.0	36.0	36.3	38.8	38.1	38.5	35.7
Service tax	0.0	1.4	1.2	1.4	1.8	1.9	3.2	3.1
			Tax revenue as a percentage of gross domestic product*					
Direct	**1.9**	**2.7**	**3.0**	**3.3**	**3.0**	**3.4**	**3.5**	**3.8**
PIT	0.9	1.2	1.3	1.5	1.4	1.5	1.6	1.5
CIT	0.9	1.4	1.6	1.7	1.6	1.9	1.9	2.3
Indirect	**7.9**	**5.5**	**5.8**	**5.7**	**5.1**	**5.3**	**5.6**	**5.3**
Customs	3.6	2.3	2.5	2.3	1.8	1.8	1.8	1.8
Excise	4.3	3.1	3.2	3.3	3.2	3.3	3.5	3.3
Service tax	0.0	0.1	0.1	0.1	0.1	0.2	0.3	0.3
Total#	**10.1**	**8.3**	**8.9**	**9.0**	**8.2**	**8.8**	**9.1**	**9.2**

@ Figures for 2003-04 are provisional accounts (unaudited) as released by the Controller General of Accounts.

PIT : Personal income tax CIT : Corporation tax

Note (1) Direct taxes also include taxes pertaining to expenditure, interest, wealth, gift, estate duty and for 1998-99 also VDIS;

(2) The ratios to GDP for 2003-04 (provisional) are based on CSO's Advance Estimates released in February 2004.

 # : Includes taxes referred to in footnote 1 and taxes of Union Territories and "other" taxes.

*** : Refers to gross domestic product at current market prices.**

Source: Budget documents

Surcharge on income tax was withdrawn for individuals and Hindu undivided families (HUF), except for those with an annual income of Rs.8.5 lakh and above. For corporate assessees and certain other categories of institutions, the rate of surcharge was halved from 5 per cent to 2.5 per cent. Other important direct tax measures included incentives for housing and infrastructure and rationalisation of provisions relating to amalgamations and demergers. A number of measures aimed at reforming tax administration were announced. These included outsourcing non-core activities, abolition of discretion based selection of returns for scrutiny, simplification of tax returns, abolition of tax clearance certificates for persons leaving India and simplification of procedures to be followed during search and seizure. Details of various direct tax measures are given in Box 2.1.

2.10 In the case of indirect taxes, emphasis was on rationalisation and simplification of tax rates, procedures, rules and regulations. The peak rate of customs duty was reduced to 25 per cent, excluding agriculture and dairy products. Excise duties were rationalised with the introduction of a three-tier duty structure of 8 per cent, 16 per cent and 24 per cent (except for petroleum products, tobacco products, pan masala, textiles and specific rated products). Other measures in respect of customs duty included reduction in the customs duty on project imports with a

Box 2.1 : Tax proposals — Budget 2003-04

Direct taxes

- No change in personal income tax rates to maintain stability in tax rates. Surcharge on income tax in the case of individuals, Hindu undivided families abolished except for those earning annual income above Rs.8.5 lakh. For those earning above Rs. 8.5 lakh, surcharge of 10 per cent applied. In the case of corporate assessees, firms, foreign companies, cooperatives, and local authorities, surcharge reduced from 5 per cent to 2.5 per cent.
- Standard deduction for salaried employees, whose salary income does not exceed Rs.5 lakh increased to 40 per cent or Rs.30,000, whichever is less. For salaried taxpayers, whose income from salary exceeds Rs.5 lakh, the standard deduction is Rs.20,000.
- VRS payments upto Rs.5 lakh, whether paid in lumpsum or in instalments exempted from income tax.
- Interest deductible under income tax upto Rs.1,50,000 for construction or purchase of self-occupied house property to continue.
- Education expenses up to Rs.12,000 per child for two children made eligible for rebate under Section 88.
- Deduction of interest income under Section 80-L for individual tax payers increased to Rs.12,000. Additional deduction of Rs.3,000 for interest on Government securities continued.
- Tax rebate in case of senior citizens (65 years and above) increased to Rs.20,000.
- Tax rebate in a year in respect of certain life insurance policies restricted to 20 per cent of the sum assured.
- Physically handicapped or persons with such dependants entitled to a deduction of Rs.50,000 for permanent physical disability and an enhanced deduction of Rs.75,000 in case of severe disability.
- Income tax at 12.5 per cent levied on dividend distributed by domestic companies. Dividends made tax free in the hands of the shareholders.
- Income from units of UTI exempted from tax in the hands of unit holders.
- Expenditure tax abolished effective from June 1, 2003.
- Interest payable to assessees on refunds reduced to 6 per cent and that chargeable from the assessees reduced to 12 per cent.
- To promote equity culture, income arising from transfer of eligible equity shares in a company listed on any recognised stock exchange and purchased between March 1, 2003 and March 1, 2004 and held for a period of more than one year exempted from tax.
- Rate of depreciation increased from 25 per cent to 40 per cent in respect of life saving medical equipment.
- Capital gains arising from the transfer of units of Unit Scheme 1964 of UTI exempted from tax effective from the assessment year 2003-04.
- Units in Special Economic Zones (SEZs) and 100 per cent Export Oriented Units (EOUs) allowed the benefit of carry forward of business losses and unabsorbed depreciation.
- Deduction under Sections 10A and 10B of the Income Tax Act allowed to the resulting entity in the case of amalgamation or demerger.
- The existing deduction to units in SEZs and 100 per cent EOUs extended to the business of cutting and polishing of precious and semi-precious stones.
- An additional deduction on account of reinvestment allowance allowed to units in Special Economic Zones, equal to 50 per cent of the profits, credited to a reserve account to be utilised for the purposes of business, for a period of three consecutive years.
- Tax incentive of deduction of 40 per cent of the profits to coffee and rubber industry.
- Premium receivable by banks under the debt buy back offer of the Government eligible for additional deduction, if such premium is declared as business income and used for provisioning of their non-performing assets.
- Sales from the Domestic Tariff Area (DTA) units to units in SEZs made eligible for deduction under Section 80HHC for a period of one year.
- A new provision allowing a ten-year tax holiday for new undertakings as well as existing undertakings on their substantial expansion, located in certain notified areas or engaged in certain thrust sector activities, in Himachal Pradesh, Sikkim, Uttaranchal and the North-Eastern States.
- The benefit of carried forward losses and unabsorbed depreciation in a scheme of amalgamation under section 72A extended to hotels and specified banks.
- Threshold limit for deduction of tax at source enhanced from Rs.1,000 to Rs.2,500 for dividends and income from units.
- Section 197A amended to provide for filing of self-declarations by senior citizens for the purpose of no deduction of tax at source in case of certain payments.
- Section 206 amended to provide for compulsory filing of TDS returns on magnetic media by corporate assessees.
- Section 230 relating to tax clearance certificates rationalised. Persons not domiciled in India, who have come to India as foreign tourists or for any other purpose other than business or employment are not required to furnish ITCC.

certain threshold investment and reduction in customs duty on specified items for promoting the information technology sector. In the case of excise duties, other important measures included an incentive package for the textile industry and extension of maximum retail price (MRP) based levy to chewing tobacco and insecticides. Details of various indirect tax measures are given in Box 2.2.

Service tax

2.11 The need for revenue augmentation for financing enhanced public sector outlays on physical and social infrastructure – such

Box 2.2 : Indirect tax proposals — Budget 2003-04

Customs

- Peak rate of customs duty reduced from 30 per cent to 25 per cent, excluding agriculture and dairy products.
- Custom duty on specified life saving drugs and life saving equipment reduced from 25 per cent to 5 per cent with exemption from countervailing duty (CVD). To encourage indigenous manufacturing, excise duty exempted on life saving equipment already enjoying CVD exemption.
- Customs duty on rough ophthalmic blanks reduced from 25 per cent to 5 per cent.
- CVD on 88 specified life saving drugs and life saving medical equipments reduced from 5 per cent to nil.
- Customs duty on specified equipment for high-voltage transmission projects reduced from 25 per cent to 5 per cent.
- Customs duty on Liquefied Natural Gas (LNG) regassification plants reduced from 25 per cent to 5 per cent.
- To encourage modernisation, customs duty on a large number of textile machinery and parts reduced from 25 per cent to 5 per cent.
- Customs duty on capital goods for telecom and information technology reduced from 25 per cent to 15 per cent.
- Customs duty on optical fibre cables reduced from 25 per cent to 20 per cent.
- Customs duty on specified raw materials for manufacture of e-glass roving used for making optical fibres reduced from 30 per cent to 15 per cent.
- Customs duty on cut and polished diamonds and gem stones reduced from 15 per cent to 5 per cent.
- Customs duty on gold reduced from Rs.250 to Rs.100 per 10 grams.
- Duty on crutches, wheel chairs, walking frames and tricycles reduced to 5 per cent without SAD. These items are also exempted from CVD. Domestic manufacturers exempted from excise duty.
- Customs duty on specified veterinary drugs reduced from 15 per cent to 10 per cent.
- Customs duty on shrimp larvae feed reduced from 15 per cent to 5 per cent, with exemption from CVD to promote marine food industry.
- Customs duty on apparel grade raw wool reduced from 15 per cent to 5 per cent.
- Customs duty on passenger baggage reduced from 60 per cent to 50 per cent.
- Drugs and materials for clinical trial exempted from customs duty.
- Customs duty on braillers, artificial limbs, hearing aids and their parts reduced to 5 per cent and also exempted from SAD.
- Customs duty on glucometers and glucometer test strips reduced from 10 per cent to 5 per cent.
- Customs duty on nickel unified at 10 per cent from 5 per cent and 15 per cent, irrespective of the class of importer.

Box 2.2 : Indirect tax proposals — Budget 2003-04 (cont.)

- Customs duty on lead reduced from 25 per cent to 20 per cent.
- Customs duty on routers, modems and fixed wireless terminals reduced from 15 per cent to 10 per cent.
- Customs duty on paraxylene reduced from 10 per cent to 5 per cent.
- Rough coloured gemstones and semi-processed half cut or broken diamonds exempted from customs duty.
- Customs duty on refrigerated trucks reduced from 25 per cent to 20 per cent.
- Customs duty on loco simulators reduced from 25 per cent to 5 per cent.
- Customs duty on spares for diesel locomotives, parts for conversion of DC locos to AC locos reduced from 25 per cent to 15 per cent.

Excise

- Rationalisation of excise rates by a three-tier duty structure of 8 per cent, 16 per cent and 24 per cent, except on petroleum and tobacco products, pan masala, textiles and items attracting specific duty rates.
- Special excise duty (SED) on tyres, aerated soft drinks, polyester filament yarn, air-conditioners and motor cars reduced from 16 per cent to 8 per cent.
- Excise duty reduced from 4 per cent to nil on unbranded surgical bandages, registers & account books, umbrellas, kerosene pressure lanterns, articles of wood, imitation zari, adhesive tapes, tubular knitted gas mantle fabrics, walking sticks, articles of mica, bicycles & parts, toys, mosaic tiles, utensils & kitchen articles, knives, spoons and similar kitchenware, tableware and glasses for corrective spectacles.
- Excise duty on pressure cookers, ophthalmic blanks, biscuits, boiled sweets and dental chairs reduced from 16 per cent to 8 per cent.
- Matches made by non-mechanised sector exempted from excise duty. Matches manufactured in the mechanised and semi-mechanised sector to attract an ad-valorem duty of 8 per cent without CENVAT credit.
- Duty on medicinal and toilet preparations containing alcohol reduced from a range of 20 to 50 per cent to a uniform rate of 16 per cent.
- Duty on electric vehicles reduced from 16 per cent to 8 per cent.
- Excise duty of 8 per cent with CENVAT credit imposed on refined edible oils, vanaspati and other similar edible oil preparations (branded and packed for retail sale).
- Specific rates on cement and clinker increased by Rs.50 per tonne.
- Additional duties of excise on motor spirit and high- speed diesel oil increased from Re. 1 per litre to Rs.1.50 per litre.
- A one per cent duty imposed on polyester filament yarn, motor cars, multi-utility vehicles and two wheelers towards contribution to National Calamity Contingency Fund. Domestic and imported crude subjected to a specific duty of Rs.50 per metric tonne.
- A cess of Re.1 per kg of tea for creating a separate fund for development, modernisation and rehabilitation of plantation sector to replace the excise duty of Re.1 per kg.
- A package of incentives announced for the textile sector. The incentives include, *inter-alia*, reduction in duty on polyester filament yarn from 32 per cent to 24 per cent, on all spun and other filament yarns from 16 per cent to 12 per cent, on woven garments from 12 per cent to 10 per cent, uniform duty of 12 per cent on polyester cotton, cotton viscose and all other spun yarns and excise duty on all knitted cotton fabrics and garments reduced from 12 per cent to 8 per cent.

as roads, water supply, education and basic health – is well recognised. The Tax Reforms Committee headed by Dr.Raja Chelliah made some far reaching recommendations, of which, levying a tax on services was an important one. The Committee felt that the indirect taxes at the Central level should be broadly neutral in relation to production and consumption of goods and should, in course of time cover commodities and services. The Committee emphasised the importance of moving towards a full fledged Value Added Tax (VAT) system to realise the above objective. The tax on services is relatively non-regressive. Keeping in view the fact that the services sector is the fastest growing sector and accounts for about 51 per cent of GDP, Government after introducing the service tax for the first time in 1994, has been extending the scope of the tax. The Budget for 2003-04 extended the service tax to ten new services taking the number of services subjected to tax to 58 and also proposed an increase in the rate of service tax from 5 per cent to 8 per cent. The new services subjected to the levy of the service tax were life insurance including insurance auxiliary services relating to life insurance, inland cargo handling, storage and warehousing services, light agricultural products and cold storage, event management, rail travel agents, health clubs and fitness centres, beauty parlours, fashion designers, cable operators and dry cleaning services. Subsequently, life insurance was exempted and service tax was extended to specialised services provided by banks and non-banking financial companies and corporate bodies. The credit of service tax on input services was extended for payment of service tax in 2002-03, provided the input and the final services were within the same category. Budget for 2003-04 had proposed extension of this to all services even if the input and the final services fell under different categories. The Budget also proposed a Constitutional amendment and enabling legislation that would give the Central Government power to levy the tax and empower the Centre and the States to collect the proceeds. The amendment to the Constitution is in progress.

2.12 Revenue collected from service tax increased from Rs.407 crore in 1994-95 to Rs.4,122 crore in 2002-03 and was budgeted to increase to Rs.8,000 crore in 2003-04. Service tax has a very large base of tax payers per unit of tax collected who are mostly non-corporate in nature, and whose standards of maintenance of accounts are rudimentary. This presents a major challenge to the revenue authorities to design and operationalise a system of tax collection that not only enables the collection of revenues due, but also avoids harassment to tax payers. Keeping this in mind, the Central Excise Department has made the procedure for registration, filing and assessment simple, with the guiding philosophy of voluntary tax compliance. To facilitate the filing of returns and to reduce the compliance cost, certain procedural changes were introduced from January, 2004. These include, simple verification for grant of registration under service tax, single registration and single return for assessees providing more than one taxable service and automation of service tax by extending e-filing of returns and electronic scrutiny from 10 services to all the 58 taxable services.

Expenditure trends

2.13 Total expenditure of the Central Government after witnessing compression in the first half of the nineties started rising in 1997-98. Total expenditure as proportion of GDP declined from 17.3 per cent in 1990-91 to 13.9 per cent in 1996-97. Thereafter, it has been rising to reach a level of 16.2 per cent of GDP in 2002-03. The quality of expenditure has also been witnessing a deterioration over the years. Capital expenditure has declined from 4.4 per cent of GDP in 1990-91 to 2.5 per cent of GDP in 2002-03, indicating that such expenditure has borne the major burden of fiscal adjustment. More than the level of expenditure, which by international standards is not very high, it is the deterioration in the quality of expenditure that is a matter of serious concern. Total

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expenditure of the Central Government was budgeted to grow by 9.6 per cent in 2003-04 over the actual expenditure in the previous year. Within the total expenditure, revenue expenditure was budgeted to grow at lower rate of 7.8 per cent compared with 12.7 per cent in 2002-03, mainly on account of lower budgeted growth in interest payments and subsidies. Capital expenditure was budgeted to grow by 19.4 per cent compared with the negative growth of 0.1 per cent in the previous year.

2.14 Interest payments, subsidies, pay and allowances and revenue expenditure on defence accounted for 99.2 per cent of net revenue receipts, 68.8 per cent of revenue expenditure and 57.4 per cent of the total expenditure of the Central Government in 2003-04 (BE). These percentages reveal the committed nature of Government expenditure and difficulties in compressing such expenditure. Details of major components of expenditure are discussed below.

Interest payments

2.15 Interest payments account for about 30 per cent of total expenditure and 35 per cent of revenue expenditure. Interest payments pre-empt nearly 50 per cent of revenue receipts. Following the deregulation of interest rates on market borrowings, as part of economic reforms undertaken in the early nineties, the average cost of market borrowings had increased from 11.4 per cent in 1990-91 to 13.7 per cent in 1996-97, despite reduction in the weighted average maturity from 18.4 years to 5.5 years in this period. With the softening of interest rates in recent years, the average cost of market borrowings witnessed a declining trend, particularly in 2003-04. The average cost of market borrowings had come down by 160 basis points from 7.3 per cent in 2002-03 to 5.7 per cent in 2003-04. The excess liquidity with the banking system and lower off take of credit, also contributed to keeping the cost of market borrowing low. Banks' holdings of Government securities were over 40 per cent of their net demand and time liabilities, as compared with the statutory minimum of 25 per cent. However, credit off take has started picking up from the third quarter of 2003-04 and the trend is likely to continue on account of revival of industrial growth. This may exert pressure on interest rates on fresh borrowings, unless the Government reduces its borrowing. Alongwith the softening of interest rates, there has also been an elongation in the maturity of dated securities. The weighted average maturity of dated securities issued during 2003-04 was 14.9 years compared with 10.6 years in 2001-02. The average cost of total internal liabilities has been witnessing a declining trend since 2000-01, reflecting the general softening of interest rates (Table 2.4).

2.16 The effect of lower interest rates on the total interest burden of the Central Government is not distinctly visible because of the growth in outstanding debt. Interest payments were budgeted to increase by 4.6 per cent in 2003-04 to Rs. 1,23,223 crore as

Table 2.4 : Interest on outstanding internal liabilities of Central Government

	Outstanding Internal liabilities	Interest on internal liabilities	Average cost of borrowings (percent per annum)
	(Rs. crore)		
1990-91	283033	19664	8.2
1991-92	317714	23892	8.4
1992-93	359654	27546	8.7
1993-94	430623	33017	9.2
1994-95	487682	40034	9.3
1995-96	554984	45631	9.4
1996-97	621438	55255	10.0
1997-98	722962	61527	9.9
1998-99	834551	73519	10.2
1999-00	962592	85741	10.3
2000-01	1102596	94900	9.9
2001-02	1294862	103175	9.4
2002-03	1499589	113238	8.7
2003-04 (RE)	1677092	121412*	9.4

Note : Average cost of borrowing is the percentage of interest payment in year 't' to outstanding liabilities in year 't-1'.

*** Includes an amount of Rs. 4079.62 crore towards premium on account of domestic debt buyback scheme and prepayment of external debt.**

Source : Budget documents.

compared with an increase of 9.6 per cent witnessed in 2002-03. Interest payments budgeted in 2003-04 constituted 33.6 per cent of revenue expenditure and 48.5 per cent of the net revenue receipts of the Central Government.

2.17 In pursuance of the announcement made in the Budget for 2003-04, Government of India in consultation with the Reserve Bank of India formulated a scheme for the buyback of high coupon Government securities held by banks and financial institutions. The scheme was structured as a switch, with the Government of India offering to buy back pre announced high coupon securities at a minimum discount of 7.5 per cent to the market value and reissuing securities of an equivalent face value at a pre announced fixed price. In the first ever buyback auction conducted online on July 19, 2003, Government accepted all the 131 offers in respect of 19 high coupon securities with face value of Rs.14,434 crore. Government had reissued four securities for an equivalent face value of securities bought back. Interest saving on bought back securities amounted to Rs.1,307 crore and with the interest outgo on reissued securities amounting to Rs.790 crore, there was a saving of Rs.517 crore in 2003-04. The estimated saving in interest payments in 2004-05 is Rs. 751 crore.

Subsidies

2.18 Expenditure on major subsidies has increased in nominal terms from Rs. 9,581 crore in 1990-91 to Rs.40,416 crore in 2002-03. It was budgeted to increase by 20.3 per cent to Rs.48,636 crore in 2003-04. Expenditure on major subsidies as per cent of revenue expenditure after declining from 13.0 per cent in 1990-91 to 8.7 per cent in 1995-96 started rising to reach a level of 9.6 per cent in 1998-99. In 2002-03, expenditure on major subsidises increased to 11.9 per cent from 10.0 per cent in 2001-02. With the dismantling of the administered price mechanism for petroleum products from April 1, 2002, subsidies in respect of LPG and kerosene distributed through the public distribution system are now explicity reflected in the budget. This partially explains the spurt of 35.3 per cent in the expenditure on major subsidies in 2002-03. The spurt in major subsidies in 2002-03 was also on account of an increase in food subsidy by Rs. 6,677 crore necessitated by the widespread drought in the country. Some of the major initiatives taken so far to rationalise the budgetary subsidies include targeted approach to food subsidy (BPL families) under Public Distribution System, allowing Food Corporation of India (FCI) to access market loans carrying lower interest rates, encouraging private trade in food grains, liquidating excess food grain stocks, replacing unit based retention price scheme with a group based scheme in the case of fertiliser subsidies and proposed phasing out of subsidies on PDS kerosene and LPG.

Central plan outlay

2.19 The Revised Estimates for 2002-03, the first year of the Tenth Five Year Plan, indicate a shortfall in the Centre's plan outlay to the extent of 5 per cent as compared with the Annual Plan/Budget Estimates. Budgetary support to the Centre's Plan was higher by 2 per cent in 2002-03 (RE) as compared with the budget estimates. There was a shortfall in the internal and extra-budgetary resources (IEBR) of the Central Public Sector Enterprises (CPSEs) by 11 per cent over budget estimates.

2.20 In the Budget for 2003-04, a provision of Rs.1,47,893 crore was made towards the annual plan outlay representing an increase of 8 per cent over the revised estimates of the previous year. This outlay was proposed to be financed by budgetary support amounting to Rs.72,152 crore (48.8 per cent) and internal and extra budgetary resources of public enterprises to the extent of Rs.75,741 crore (51.2 per cent). Energy (29.3 per cent), transport (19.5 per cent), communications (10.1 per cent) and social services (21.4 per cent) accounted for bulk of the Central plan outlay. There was a significant step-up in the outlays, as compared to 2002-03(RE), for agriculture (20 per cent) and general economic services

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(148 per cent). A lower outlay of Rs.8,181 crore was budgeted for rural development as compared with Rs.12,834 crore in 2002-03 (RE).

2.21 Central assistance to State and Union Territories (UTs) Plans was budgeted to increase by 6.4 per cent to Rs.48,822 crore in 2003-04 over the revised estimates for 2002-03. There was a substantial step-up in Central assistance to State plans under Accelerated Power Development Programme (APDP) and Rashtriya Sam Vikas Yojana (previously known as Development and Reform Facility). While the assistance for APDP was increased from Rs.1,089 crore in 2002-03 (RE) to Rs. 3,500 crore in 2003-04 (BE), assistance under Rashtriya Sam Vikas Yojana was increased from Rs.775 crore to Rs.1,450 crore over the same period.

Government debt

2.22 There is growing concern about the level of indebtedness of the Government and its sustainability. Outstanding liabilities of the Central Government, after declining from 55.3 per cent of GDP in 1990-91 to 51.2 per cent in 1998-99, started rising to reach 63.1 per cent of GDP in 2002-03. These were budgeted to increase to Rs.17,80,064 crore in 2003-04 (64.6 per cent of GDP). While internal liabilities increased from 49.8 per cent of GDP to 60.7 per cent of GDP between 1990-91 and 2002-03, there was a decline in the external liabilities from 5.5 per cent to 2.4 per cent of GDP in the same period. External liabilities valued at year-end exchange rates declined from 11.7 per cent of GDP to 7.9 per cent of GDP between 1990-91 and 2002-03. The increase in the debt-GDP ratio witnessed since 1999-2000 was mainly on account of increase in the internal liabilities of the Central Government. Within internal liabilities, the share of market borrowings has been steadily increasing. The share increased from 24.9 per cent in 1990-91 to 41.3 per cent in 2002-03. It was budgeted to increase to 42.4 per cent in the budget estimates for 2003-04 (Table 2.5).

2.23 The increasing trend in government debt has been a matter of serious concern because of the associated preemption of resources from the private sector. With over three-fourths of the fiscal deficit being accounted for by revenue deficit, there is limited room to deploy the borrowings in a productive manner. Any increase in debt puts pressure on interest payments, which in turn necessitates a further build up of debt. Increase in Government debt by drawing on private savings deprives the private sector of required resources. The indirect cost of debt is the incremental growth foregone by the economy as a result of the diversion of resources from the private to the Government sector. Gross market borrowings of the Central Government (excluding 364-day treasury bills) were budgeted at Rs.1,39,887 crore and the net market borrowings at Rs.1,07,194 crore in 2003-04. A notable development in 2003-04 was that actual net market borrowings of the Central Government at Rs.88,860 crore were considerably lower than the budget estimate, despite additional borrowing to fund pre payment of external debt. This was facilitated by large receipt on account of debt swap scheme. With a view to reducing the debt burden, Government prepaid external debt of US $3753.56 million in 2003-04.

Supplementary demands for grants

2.24 Three supplementary demands for grants were presented in 2003-04. In the first batch of supplementary demands, approval of Parliament was sought for gross additional expenditure of Rs.8,519 crore in respect of 29 grants. These demands involved net cash outgo of Rs.5,580 crore and gross additional expenditure, matched by savings of the Ministries concerned, amounting to Rs.2,939 crore. Major items of additional expenditure involving cash outgo included Rs.607 crore for providing loans to States for making payment to sugarcane growers against dues, Rs.200 crore for implementing the scheme of Price Stabilisation Fund for tea, rubber, coffee and tobacco, Rs.3,650 crore for meeting additional requirement under special

Table 2.5 : Outstanding liabilities of the Central Government

(end-March)

		1990-91	1999-00	2000-01	2001-02	2002-03	2003-04$ (BE)	2003-04$ (RE)
					(Rs. crore)			
1.	**Internal liabilities**	**283033**	**962592**	**1102596**	**1294862**	**1499589**	**1719133**	**1677092**
	a) Internal debt	154004	714254	803698	913061	1020688	1158639	1134020
	i) Market borrowings	70520	355862	428793	516517	619105	728664	704902
	ii) Others	83484	358392	374905	396544	401583	429975	429118
	b) Other Internal liabilities	129029	248338	298898	381801	478901	560494	543072
2.	**External debt(outstanding)***	**31525**	**58437**	**65945**	**71546**	**59612**	**60931**	**47407**
3.	**Total outstanding liabilities (1+2)**	**314558**	**1021029**	**1168541**	**1366408**	**1559201**	**1780064**	**1724499**
4.	**Amount due from Pakistan on account** of share of pre-partition debt	**300**	**300**	**300**	**300**	**300**	**300**	**300**
5.	**Net liabilities (3-4)**	**314258**	**1020729**	**1168241**	**1366108**	**1558901**	**1779764**	**1724199**
					(As percent of GDP)			
1.	**Internal liabilities**	**49.8**	**49.7**	**52.8**	**56.7**	**60.7**	**62.4**	**60.9**
	a) Internal debt	27.1	36.9	38.5	40.0	41.3	42.1	41.2
	i) Market borrowings	12.4	18.4	20.5	22.6	25.1	26.4	25.6
	ii) Others	14.7	18.5	17.9	17.4	16.3	15.6	15.6
	b) Other Internal liabilities	22.7	12.8	14.3	16.7	19.4	20.3	19.7
2.	**External debt(outstanding)***	**5.5**	**3.0**	**3.2**	**3.1**	**2.4**	**2.2**	**1.7**
3.	**Total outstanding liabilities**	**55.3**	**52.7**	**55.9**	**59.9**	**63.1**	**64.6**	**62.6**
	Memorandum items							
	(a) External debt (Rs.crore)@	66314	186791	189990	199639	196067	236604	184088
	(as per cent of GDP)	11.7	9.6	9.1	8.7	7.9	8.6	6.7
	(b) Total outstanding liabilities	349347	1149383	1292586	1494501	1695656	1955737	1861180
	(adjusted) (as per cent of GDP)	61.4	59.3	61.9	65.5	68.7	71.0	67.6
	(c) Internal liabilities(Non-RBI)#	208978	820967	956478	1142698	1337752	1557970	1518040
	(as per cent of GDP)	36.7	42.4	45.8	50.1	54.2	56.5	55.1
	(d) Outstanding liabilities (Non-RBI)# (Rs.crore)	275292	1007758	1146468	1342337	1533819	1794574	1702128
	Outstanding liabilities (Non-RBI) (as per cent of GDP)	48.4	52.0	54.9	58.8	62.1	65.1	61.8
	(e) Contingent liabilities of Central Government (Rs.crore)	n.a.	83954	86862	95859	90617	n.a.	n.a.
	Contingent liabilities of Central Government (as per cent of GDP)	n.a.	4.3	4.2	4.2	3.7	n.a.	n.a.
	(f) Total assets (Rs crore)	236740	607705	676581	760592	840768	956444	892123
	Total assets (as per cent of GDP)	41.6	31.4	32.4	33.3	34.0	34.7	32.4

n.a. : not available

* **External debt figures represent borrowings by Central Government from external sources and are based upon historical rates of exchange.**

@ **Converted at year end exchange rates. For 1990-91,the rates prevailing at the end of March, 1991; For 1999-2000, the rates prevailing at the end of March,2000 and so on.**

\# **This includes marketable dated securties held by the RBI.**

$ **The ratios to GDP at current market prices for 2003-04 are based on CSO's Advance Estimates released in February, 2004.**

Source: 1. Budget documents. 2. Controller of Aid Accounts and Audit. 3. Reserve Bank of India.

component of Sampoorna Gramin Rozgar Yojana and Rs.500 crore for meeting additional expenditure of Delhi Metro Rail. The second batch of supplementary demands for grants involving 42 grants sought the approval of Parliament for additional expenditure of Rs.7,660 crore. These proposal involved a net cash outgo of Rs.4,888 crore and gross additional expenditure, matched by savings of the Ministries concerned amounting to Rs.2,772 crore. Major items of additional expenditure involving cash outgo were Rs.2,300 crore for providing compensation to Bharat Sanchar Nigam Ltd. for meeting operational losses on rural telephony, Rs.550 crore for meeting additional expenditure under national programme for nutritional support to primary education and another Rs.1,580 crore for meeting additional expenditure under Sampoorana Gramin Rozgar Yojana. The third and final batch of supplementary demands included 63 grants and 5 appropriations involving an additional expenditure Rs.31,105 crore. Out of this, net cash outgo amounted to Rs.2,592 crore and gross additional expenditure matched by savings of the Ministries concerned amounted to Rs.28,513 crore. Major items of additional expenditure involving cash outgo included Rs.682 crore towards pre-payment premium for reduction of external and internal debt, Rs.650 crore towards interest on market loans, Rs.394 crore for establishment related expenditure of para-military forces and Rs.251 crore towards fencing of border etc. In the third supplementary demands for grants, major items of expenditure, not involving cash outgo included Rs.3,398 crore towards payment of premium for reduction of external debt and Rs.15,673 crore towards pre-payment of external debt.

Savings and capital formation

2.25 The economic and functional classification of the Central Government Budget 2003-04 puts total Government expenditure at Rs.4,38,187 crore, an increase of 9.0 per cent over the revised estimates of the previous year. Of this, provision towards gross capital formation amounted to Rs. 87,138 crore or 19.9 per cent of the total expenditure. Gross capital formation of the Central Government has exhibited a secular declining trend. Another disturbing development relates to the growing dis-savings of the Central Government. The dis-savings of the Central Government increased from 1.8 per cent of GDP in 1990-91 to 3.3 per cent of GDP in 2002-03 (RE). The dis-saving was estimated at 3.4 per cent of GDP in 2003-04 (Table 2.6). Expenditure on wages, salaries and pensions of the Central Government as a proportion of its total expenditure was budgeted at 11.9 per cent in 2003-04 as compared with 12.4 per cent in 2002-03 (RE).

Collection rates

2.26 In a tax system, where there is lack of convergence between statutory and effective rates of duty on account of numerous exemptions, nominal rates of duty do not fully reflect the incidence. The collection rate, which is the ratio of realised import revenue to the value of a commodity, broadly indicates the incidence of customs duty and other levies, which are not in the nature of protective tariffs such as special additional duty and countervailing duty on imports. Thus, the collection rate not only captures the element of protection due to customs duties but also the incidence of other duties, which are in the nature of off-sets to mitigate the impact of domestic levies for which producers cannot avail of any credit. Generally, the collection rate is higher than the basic customs duty as the latter excludes other duties and levies. Recent trends in collection rates indicate a sharp decline. The total incidence of duty for all commodity groups has come down to 15 per cent in 2002-03 from a level of 47 per cent noticed in 1990-91. A sharp decline was noticed in the case of petroleum products, chemicals, paper and metals.

Website: http://indiabudget.nic.in

Table 2.6 : Total expenditure and capital formation by the Central Government and its financing

(As per economic and functional classification of the Central Government budget)

		1990-91	1998-99	1999-00	2000-01	2001-02	2002-03 (RE)	2003-04$ (BE)
					(Rs. crore)			
I.	**Total expenditure**	**97947**	**263755**	**307509**	**328265**	**360616**	**401996**	**438187**
II.	**Gross capital formation out of budgetary resources of Central Government**	**28032**	**57807**	**67602**	**66960**	**76888**	**75632**	**87138**
	(i) Gross capital formation by the Central Government	8602	20647	26075	22258	12634	20074	22960
	(ii) Financial assistance for capital formation in the rest of the economy	19430	37160	41527	44702	64254	55558	64178
III.	**Gross saving of the Central Government**	**-10502**	**-41893**	**-41169**	**-56920**	**-76306**	**-81435**	**-92692**
IV.	**Gap(II-III)**	**38534**	**99700**	**108771**	**123880**	**153194**	**157067**	**179830**
	Financed by							
	a. Draft on other sectors of domestic economy	34768	96793	106483	115561	145841	169581	174788
	(i) Domestic capital receipts	23421	97029	105619	116758	147337	164283	174788
	(ii) Budgetary deficit/draw down of cash balance	11347	-236	864	-1197	-1496	5298	0
	b. Draft on foreign savings	3766	2907	2288	8319	7353	-12514	5042
					(As per cent of GDP)			
I.	**Total expenditure**	**17.2**	**15.1**	**15.9**	**15.7**	**15.8**	**16.3**	**15.9**
II.	**Gross capital formation out of budgetary resources of Central Government**	**4.9**	**3.3**	**3.5**	**3.2**	**3.4**	**3.1**	**3.2**
	(i) Gross capital formation by the Central Government	1.5	1.2	1.3	1.1	0.6	0.8	0.8
	(ii) Financial assistance for capital formation in the rest of the economy	3.4	2.1	2.1	2.1	2.8	2.2	2.3
III.	**Gross saving of the Central Government**	**-1.8**	**-2.4**	**-2.1**	**-2.7**	**-3.3**	**-3.3**	**-3.4**
IV.	**Gap (II-III)**	**6.8**	**5.7**	**5.6**	**5.9**	**6.7**	**6.4**	**6.5**
	Financed by							
	a. Draft on other sectors of domestic economy	6.1	5.6	5.5	5.5	6.4	6.9	6.3
	(i) Domestic capital receipts	4.1	5.6	5.5	5.6	6.5	6.7	6.3
	(ii) Budgetary deficit/draw down of cash balance	2.0	0.0	0.0	-0.1	-0.1	0.2	0.0
	b. Draft on foreign savings	0.7	0.2	0.1	0.4	0.3	-0.5	0.2
					(increase over previous year)			
II.	**Gross capital formation out of budgetary resources of Central Government**	**2.8**	**5.5**	**16.9**	**-0.9**	**14.8**	**-1.6**	**15.2**
	Memorandum items							
					(Rs.Crore)			
1	Consumption expenditure	22359	59920	68831	71977	77324	85259	97773
2	Current transfers	45134	137611	161549	183696	201188	233251	248326
					(As per cent of GDP)			
1	Consumption expenditure	3.9	3.4	3.6	3.4	3.4	3.5	3.5
2	Current transfers	7.9	7.9	8.3	8.8	8.8	9.4	9.0

$: The ratios to GDP at current market prices for 2003-2004 are based on CSO's Advance Estimates released in February, 2004.

Notes:
- **(i) Gross capital formation in this table includes loans given for Capital formation on a gross basis. Consequently domestic capital receipts include loan repayments to the Central Government.**
- **(ii) Consumption expenditure is the expenditure on wages & salaries and commodities & services for current use.**
- **(iii) Interest payments, subsidies, pension etc. are treated as current transfers.**
- **(iv) Gross capital formation & total expenditure are exclusive of loans to States'/Uts against States'/Uts share in the small savings collection.**
- **(v) The figures of total expenditure of the Central Government as per economic and functional classification do not tally with figures given in the Budget documents. In the economic and functional classification, interest transfered to DCUs, loans written off etc, are excluded from the current account. In the capital account, expenditure financed out of Railways Posts &Telecommunications own funds etc, are included.**

Source : Economic and Functional Classification of the Central Government Budgets.

Table 2.7 : Collection rates* for selected import groups

(in per cent)

Sl. No.	Commodity Groups	1990-91	1997-98	1998-99	1999-00	2000-01	2001-02	2002-03 (Prov.)
1	Food products	47	16	15	15	31	40	30
2	POL	34	29	29	23	16	10	11
3	Chemicals	92	37	34	36	38	29	29
4	Man-made fibres	83	36	49	64	49	31	32
5	Paper & newsprint	24	13	11	9	8	6	7
6	Natural fibres	20	17	22	24	18	8	10
7	Metals	95	44	51	55	48	36	36
8	Capital goods	60	41	42	36	36	28	24
9	Others	20	15	11	12	12	9	9
10	Non POL	51	27	23	22	23	19	17
11	Total	47	27	23	22	21	16	15

* Collection rate is defined as the ratio of realised import revenue (including additional customs duty/ countervailing duty (CVD), and special additional duty) to the value of imports of a commodity.

S.No.1 includes cereals, pulses, tea, milk and cream, fruits, vegetables, animal fats and sugar.

S.No 3 includes chemical elements, compounds, pharmaceuticals, dyeing and colouring materials, plastic and rubber.

S.No.5 includes pulp and waste paper, newsprint, paperboards and manufactures and printed books.

S.No 6 includes raw wool and silk.

S.No. 7 includes iron and steel and non-ferrous metals.

S.No. 8 includes non-electronic machinery and project imports, electrical machinery.

Source : Budget documents.