

## Outlook

2.65 Fiscal consolidation continues to remain a major challenge in the process of on-going economic reforms in the country. Measures taken so far to address the problem of growing fiscal imbalances have not been adequate and commensurate with the magnitude of the problem. Over the years, the revenue deficit has emerged as the main source of fiscal imbalances with serious implications for public investment and growth of the economy. The Tenth Five Year Plan (2002-07) has thrown up a new challenge in terms of raising public and private investment levels to realise the average growth target of 8 percent per annum. The growth envisaged in the Plan requires an average annual investment of 28.4 percent of GDP involving acceleration in the investment rate from 24.4 percent of GDP in the base year (2001-02) to 32.3 percent of GDP in the terminal year of the Plan. The step up envisaged in the public sector investment is nearly 3 percentage points of GDP. Without fiscal consolidation, it would not be possible to achieve any improvement in the current levels of public investment.

2.66 The total government expenditure of the Central government at 16.7 percent of GDP in 2002-03(BE) is not higher by international comparison. It is not the level of government expenditure that is a matter of concern but its composition. Wages and salaries, interest payments and subsidies account for a predominant share of government expenditure. Therefore, fiscal consolidation is not a question of expenditure reduction, but the manner in which such reduction is brought about, while at the same time promoting growth enhancing expenditure. In fact, public investment needs to be stepped up to realise the Tenth Plan growth target of 8 percent per annum.

Restructuring expenditure in favour of public investment in infrastructure, both physical and social, assumes significance in this context. Expenditure needs to be prioritised by pruning untargeted subsidies and exercising utmost economy in wages and salaries. Besides, emphasis needs to be laid on the completion of on-going projects before committing expenditure on new projects.

2.67 Flexibility in restructuring expenditure will have to come mainly from an improvement in revenue collections. Revenue from recovery of user charges remains largely untapped. The main focus of reforms in the area of direct and indirect taxes so far has been on the rationalisation of tax rates. The existence of a fairly large unorganised sector, exemptions and evasions have affected buoyancy of tax collections. Modernisation of tax administration, broadening the base and restricting the exemptions to the bare minimum may improve revenue collections. The appointment of two Task Forces on direct and indirect taxes under the chairmanship of Dr. Vijay L Kelkar indicates the importance attached to these aspects by the Government. The follow up on the recommendations of these Task Forces is expected to result in improved tax collections in the medium term. Tax reforms so far remained confined to the Central government. This position has changed with State Governments deciding to introduce VAT from April 1, 2003. This has further strengthened the hopes of fiscal consolidation. The shift in the emphasis on disinvestment in public enterprises from sale of minority share holding to strategic sale and emerging consensus on the need to speed up privatisation are also likely to contribute to fiscal consolidation.