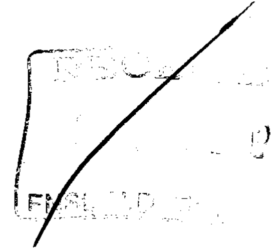

INDIAN LIBERAL GROUP

March 27, 2002

Ms. Rebon Banerjee
New Delhi

Dear Rebon:

Herewith 14 packets totalling 107 covers for delivery to MPs and party offices as follows:

At Parliament House (102 covers)

- BJP	: 20 covers
- BSP	: 2 covers
- Indian National Congress	: 37 covers
- Trinamul Congress	: 6 covers
- Nationalist Congress Party	: 3 covers
- TDP	: 8 covers
- Socialist Party	: 4 covers
- AIADMK	: 4 covers
- PMK	: 2 covers
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- RJD	: 1 cover
- BBM	: 1 cover
- DMK	: 1 cover
- MDMK	: 1 cover
- JD(U)	: 1 cover
- SJP(R)	: 1 cover
- SAD (M)	: 1 cover
- BJD	: 4 covers
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2. BJP Central Office : 3 covers

3. Individual addresses : 2 covers

Many thanks for your assistance in having these delivered. Enclosed are two copies for Mr. Welck and you.

National Headquarters: Sassoon Building, 1st Floor, 143 Mahatma Gandhi Road, Mumbai 400 001.
Phones: 0091 (22) 2843416 / 2674453 • *Telefax*: 0091 (22) 2843416
email: freedom@vsnl.com • *Website*: www.liberalsindia.com

INDIAN LIBERAL GROUP

March 26, 2002

To,

Dear Friend

Re: Union Budget: **2002- 2003 – The** Liberal View

The Indian Liberal Group (ILG), founded by the late Minoo Masani, author and parliamentarian, to promote the Liberal philosophy, and to place before the country an alternative to Socialist policies, supports the ongoing economic reforms.

The ILG has issued a statement presenting the Liberal view on the Union Budget 2002-03 for the consideration of Members of Parliament, politicians and decision-makers outside the political spectrum. This statement has been prepared from inputs provided by over 15 members of the Indian Liberal Group belonging to various vocations and disciplines and located in various parts of the country.

This is the first of many statements we shall be making on current issues and developments, from the Liberal point of view. If you would like to receive such statements kindly let us have your mailing address (where you would prefer to receive mail from us) and your email address.

We do hope you will give serious consideration to our views, which are based on reason and careful thought, even if they swim against populist currents and are politically not correct. We base our thinking on the belief that what is popular may not necessarily be in the long term interests of our people.

If you wish to know more about the Indian Liberal Group please visit our website www.liberalsindia.com. You can also write to us at the address given below.

With greetings,

Yours truly,

S. V. Raju
President

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UNION BUDGET 2002 –2003
THE LIBERAL POINT OF VIEW
Statement of the Indian Liberal Group

With GDP growth at **5.4** per cent in 2000-01 and industrial growth at around less than 3 per cent it is very obvious that the economy has slowed down considerably and is in very poor shape. This, despite the fact that agricultural production grew 6 per cent, inflation has been around one per cent and foreign exchange reserves stand at around $ 50 billion.

The economy needs a strong demand push. At the same time the path of deficit financing is fraught with risk. The government has attempted a very Keynesian approach by increasing public investment (plan expenditure is up 14 per cent), especially in the infrastructure sector. Even in a situation of extremely low inflation, given the extent of fiscal mismanagement by successive governments, it is doubtful if any kind of fiscal relaxation can really revive the economy. On the other hand, if past experience is any guide, it is only likely to spin out of control. So, given that government spending is never very efficient, there are limitations to the Keynesian approach. What needs to be noted - and supported - is government's attempt to encourage private investment in various sectors, especially the infrastructure, by easing restrictions.

Demand has to be generated by leaving more money in the hands of the people for them to spend. Unfortunately, the new guidelines on 'exemptions and perquisites, the replacement of the two per cent surcharge on income tax with a five per cent one and making dividend subject to 10 per cent tax in the hands of the recipients has only increased the tax burden on the middle classes, leaving them with little disposable income. This will mean people will spend less, depriving industry of demand.

Increased public expenditure will only increase the fiscal deficit and, hence, government borrowings. The fiscal deficit, at 5.7 per cent of GDP, is unsustainable and even next year, the deficit is targeted at a high 5.3 per cent, which is certain to be exceeded, given the government's record. The revenue deficit - the excess of revenue or non-productive expenditure over revenue receipts - is the main culprit and eats up 65 per cent of government borrowings. The government will, therefore, have to be ruthless in cutting non-productive expenditure like interest payments (which account for 50 per cent of revenue receipts in 2001-02), subsidies -14 per cent of revenue receipts in 2001-02) and its own salary and pension bills.

The problem of interest payments can be solved only by reducing borrowings and this, in turn, requires better fiscal management. For this, some tough decisions will have to be taken by the government and supported by all political parties.

The Budget talks about reducing central government staff strength by 12,200 by March 2002 and must be encouraged to show boldness in pursuing this intention. The surplus manpower has been estimated at 42,200 posts and 12,200 is a minuscule percentage

of this. At the same time, retrenchment should be accompanied by adequate compensation.

The subsidy burden has gone up because of the increased food subsidy bill and the fact that, with the dismantling of the administered price mechanism, the subsidy on LPG and kerosene (Rs 6495 crore) has come on to the general budget. The Budget took the bold step of increasing the prices of LPG and kerosene. This step was in the right direction and was absolutely necessary. It is regrettable that political parties, for populist reasons, are opposing this sound economic decision and, worse, the government has succumbed to pressure and rolled back, albeit partially, the increase in LPG prices. This has increased the subsidy burden in 2002-03 by Rs 700 crores, something that the economy cannot afford. What needs to be realised is that while the common man may save Rs.20 on one LPG cylinder, he will have to pay far more in other ways if the economy suffers.

The food subsidy bill, which amounted to Rs.17, 612 crore in 2001-02 and is budgeted at Rs.21,200 crore in 2002-03, can be contained by reforming the foodgrains procurement system and toning up the public distribution system. The subsidy has soared because of high carrying costs (comprising freight, storage and interest charges). The high minimum support price (MSP), which governments are arm twisted into paying, leads to excess procurement that, together with reduced offtake because of shortcomings in the public distribution system, result in a much larger buffer stock and, consequently, higher carrying costs. The Budget, regrettably, does nothing at all in this respect.

The fiscal deficit can be reduced if increased expenditure is matched by increased revenues. The tax-GDP ratio needs to be increased from its present level of 9 per cent to at least 14 per cent. This has to be done by a combination of widening the tax base and toning up the tax collection machinery and plugging leakages. It is good that the finance minister has tried to widen the tax base by bringing more services under the tax net. Services constitute almost 50 per cent of the GDP and yet contribute only around 2 per cent to tax revenue. People will pay taxes if they get something in return. This return is nothing less sensible economic management and good governance which implies *inter alia* less corruption!

The Budget has rationalised customs and excise duties. All this will reduce the element of discretion and, therefore, reduce the scope for corruption. The finance minister needs to be lauded for carrying forward the tax rationalisation effort. In his endeavour to bring down the customs duties to ASEAN levels in three years, the finance minister has reduced the peak rate from 35 per cent to 30 per cent. Sections of domestic industry may protest, but this is a move towards making our economy more globalised. The increased competition that this will expose domestic industry to will only force it to improve efficiencies and, in the long run make it globally competitive.

The Budget has done nothing to improve consumer sentiment towards the equity market. Small investors have been hit particularly hard, with interest rates on small savings reduced and dividends taxed in the' hands of the recipient. While reducing the interest

rate on small savings may be an economically sound step, given the record low inflation, it is difficult to accept the logic that reducing the interest on these savings will move more money into the debt and equity markets. Earlier reductions in the administered interest rates have not resulted in this. Investment in equity will come only when there are viable opportunities and when the markets become scam free. For the market to be scam-free, the Securities and Exchange Board of India needs to be strengthened and political interference stopped. The control of finance ministry bureaucrats over SEBI needs to be drastically reduced, enabling it to function as a truly independent regulator.

However, the finance minister needs to be commended for initiating a system where the revisions in the interest rates on contractual savings will be made annually on a non-discretionary automatic basis. Political considerations will no longer prevail when deciding the rates. The logic must be purely economic.

The agriculture sector accounts for 33 per cent of GDP and employs, directly and indirectly, over 70 per cent of the population. But the sector has been stagnating, because public investment has been going down over the years. For every rupee spent on investment, an equal amount is spent on subsidies. Private investment is not coming in because the necessary reforms have not taken place.

Rural demand constitutes 50 per cent of overall demand. While farm productivity has improved because of better technologies, farm profitability and prosperity of the farmers are hampered by the large number of controls on movement of foodgrains, restrictions on exports, and the lack of encouragement to contract farming.

The Finance Ministers needs to be complimented for attempting some reform of the agriculture sector. The move to amend the highly restrictive Milk and Milk Products Control Order (MMPO) is a step in the right direction. India is the largest producer of milk in the world, yet only 14 per cent of the 81 million tonnes produced annually is processed.

Equally important is the announcement of the setting up of a group of ministers to prepare a modern, integrated food law and converging the multiplicity of regulations relating to food. This will come as a boost to the food processing sector. Farmers need to diversify their produce from cereal crops to non-cereal crops like vegetables and fruits, horticulture etc. India is the world's second largest producer of fruits and vegetables, but less than 2 per cent of production is processed. The development of a modern food processing industry will provide an assured market to farmers.

However, the finance minister has avoided the most important issue in agricultural reform by deferring the reform of the foodgrain procurement system, which has resulted in huge stocks piling up in government godowns even as there are starvation deaths.

Also, the increased allocation of Rs.91 crores for agricultural research and extension is inadequate to meet the new challenges under the WTO which will require considerable research in new seeds and trans-genics. The WTO gives huge opportunities to boost

agri-business and farmers must be enabled to reduce production costs, improve the quality of their produce and raise income via exports.

While the Budget proposes to step up funding for the Accelerated Irrigation Benefit Programme to complete the ongoing major and medium irrigation projects, there is no mention of minor irrigation schemes and watershed development programmes. The Budget should have paid attention to this.

On the other hand the Budget, very creditably, has paid a great deal of attention to the infrastructure sector, increasing outlays and taking significant steps towards deregulation and increasing private sector involvement in the power, ports and airports sectors.

The increase in the outlay on energy and enhanced allocation for the Accelerated Power Development and Reform Programme needs to be welcomed. Reforming the power sector is crucial to getting private sector investment. The emphasis on transmission and distribution is commendable since new generation schemes (barring those already being implemented) are not necessary. By reducing system losses, more power can be released. Proper metering, increasing user charges and ending all free power schemes will go a long way to making the state electricity boards viable and improving their service. People will not mind paying more if the quality of power supplied improves.

The initiatives in urban development in the form of an Urban Reform Initiative Fund and a City Challenge Fund are progressive measures. It is good that the finance minister has linked these to amendments to rent control laws,' repeal of the Urban Land Ceiling Act, rationalisation of high stamp duty regimes, revision of bye-laws relating to construction and municipal laws and simplification of formalities for conversion of agricultural land for non-agricultural purposes. All this will provide a tremendous boost to the housing and construction sectors, which have great job-generation potential. The construction sector is the second largest employer after agriculture.

The finance minister has announced that some more industries will be de-reserved, another good step. The policy of reserving sectors of production for SSI units is peculiar to India and has affected the competitiveness of Indian industry, especially in areas where it has maximum export potential. The Rs.1 crore ceiling on investment has ensured that industries are unable to take advantage of economies of scale or improved technology.

Though the Indian Liberal Group is concerned at the lack of growth impulses in the Budget, something that was sorely needed at this point of time, it commends the various proposals that take significant steps towards freeing the economy.

The ILG hopes the government will follow these announcements with implementation and hopes that all political parties, particularly those in the opposition, will shed the mentality of opposition for opposition's sake and offer constructive and informed support to these measures.

Even though this statement is the ILG's view of the more crucial aspects of Budget 2002-2003 it will be incomplete without drawing attention to the fact that there are a number of economic Bills awaiting clearance and which can determine whether the objectives that the finance minister has set for the country are fulfilled or not. These include the Electricity Bill (which will revitalise the sector), the Banking Companies (Acquisition and Transfer of Undertaking) Bill - to reduce government holding in public sector banks to 33 per cent - and amendments to the Industrial Disputes Act and the Contract Labour Act.

The economy is in dire need of structural reform and these bills will help that process. The Opposition parties ire seem to be directed at the amendments to the labour laws. It is difficult to understand why. The proposed amendments to the Industrial Disputes Act will allow factories with upto 1000 workers to retrench employees without seeking government permission. At the same time, it also enhances the compensation to be paid to the workers. The amendments to the Contract Labour Act make it easier for companies to hire temporary labour. Both these amendments are sound in principle and are needed to give industry operational flexibility.

Ensuring the passage of these Bills will only help protect the workers' interests. The parties in the opposition must give up their obstructionist approach if they wish tobe taken seriously. Political expediency cannot be above the national interest.

Budgets of the Union and, for that matter, of the states cannot stand alone. They need to be supported by legislation and decisions that help ensure that the taxpayer's rupee yields the maximum returns. Hence this interpolation about the need for these bills to be passed. They are far more urgent than the question of putting up a temple in Ayodhya.

Mumbai, March 21,2002