

<http://in.rediff.com/money/2009/feb/17bud-how-a-spendthrift-government-hurts-growth.htm>

## How a spendthrift government hurts growth

Kunal Kumar Kundu

February 17, 2009

**T**he **Interim Budget** presented in Parliament on Monday was, as expected, shorn of any heroics. Not that the interim finance minister can be blamed. Announcing populist measures and the inability to carry through the same (which is very much likely given the soon to be imposed code of conduct by the Election Commission) would not have served any purpose.

More importantly, from the point of view of the market and its sentiment, another round of booster dose was also not announced. That, though, may have been caused both by the precarious fiscal health and the desire to stick to propriety.

While in keeping with the trend of making Budget exercises lacklustre, since many measures are nowadays announced in between, the Budget speech, at one point in time, seemed like an election rally with encomiums being showered on the current government.

Of course, this Budget will be debated and discussed by various economists and analysts. However, the aim of this article is not to go into too much of analysis but to leave behind a few thoughts which needs to be pondered over.

The finance minister has mentioned that the Indian economy grew by nearly 9 per cent on an average during the first four years of their tenure. While that indeed is commendable, it is not very clear as to how much credit the current government can take since it is quite obvious that while part of the growth can be termed as structural (euphemism for successful reform) a part is indeed cyclical as India got the benefit of ultra cheap capital that was sloshing around all over the world pouring into India leading to a virtuous cycle.

We are now paying the price (along with the world) given our excessive dependence on capital flows as the tap closed. Few good years of growth blinded us from reality, making us believe that we will continue to grow at 9 per cent plus in the coming years. Hence, rather than embarking in ways to conserve resources when the going was good, it was frittered away. The freshest action in memory is the farm loan waiver (to the extent of almost Rs 72,000 crore -- Rs 720 billion) announced last year.

That apart, the euphoria of high growth seemed to have blinded us from the actual objective -- that of ensuring continued real economic reform. Come to think of it, we are now paying the price for not doing enough on the reforms front. As a result, the constraints that remained hidden during good growth years are coming to back to haunt us when the going has got tough.

As mentioned earlier, we have failed to make judicious use of resources when the going was good. Indeed, we continued on our profligate ways and embarked on the route of accounting jugglery just to show the world that our deficit is under control.

Reducing deficit by shifting deficit-causing items below the line (in the name of issuing bonds which will only burden our future generations) does not hide the reality. Continuous and imprudent use of resources in the name of populism can only defer the problems, not solve those.

And now, in these tough times, despite the creative accounting process, our fiscal deficit is expected to shoot up to 6 per cent. If we add to this the state deficits and if we bring the below-the-line items on board, we are staring at a fiscal deficit of over 10 per cent, maybe closer to 12 per cent!

Make no mistake, even a 6 per cent fiscal deficit is huge. While we are talking of a much desired pump priming (a la Keynesianism) to fight the current slowdown, our ability to use the fiscal deficit appropriately is much limited. This will be clear if we dig deeper into the actual deficit figure.

Our revenue deficit at Rs 2,41,273 crore (Rs 2,412.73 billion) is close to 74 per cent of our fiscal deficit, which is at Rs 3,26,515 crore (Rs 3,265.15 billion).

For a capital-scarce country like India, it is criminal if the government fails to manage its own expenses. But this is exactly what has been happening, resulting in high revenue deficit. And the government is currently using nearly 75 per cent of its borrowings just to meet housekeeping expenses.

Clearly, one can imagine the positive impact our fiscal policy would have had in the current phase of slowdown in the absence of such uncontrolled wastage. Any takers?

**The author is COH, Global Market Research, Infosys [Get Quote] BPO Ltd. The views expressed here are solely those of the author.**