Fiscal Correction versus Democracy in India*

Jayati Ghosh

There is a reason why budgets have to be passed in parliament (in India certainly, but also in most other countries). There is a reason why, as per the Indian Constitution, the Finance Bill that details the revenues and expenditure plans of the central government for the coming fiscal year is the single most important bill that must be passed for a government to stay in power. The underlying presumption is that these fiscal strategies, in terms of how resources are raised and the level and direction of spending, must be subject to democratic accountability. This matters because these decisions are not simply "technocratic" – they are fundamentally about distribution of resources and incomes, and therefore they are deeply political. Therefore attempts to make budgetary decisions without public scrutiny and discussion are deeply anti-democratic.

Consider: if the government promises, and Parliament accepts, that a certain stated amount will be spent on rural housing or public health or nutrition programmes or the Integrated Child Development Scheme that is directed to for mothers and infants, then by what right does the central government on its own decide that this amount will be reduced? Surely, just as the initial plans for fiscal allocation are considered and discussed extensively by elected representatives before being passed, and various amendments are made, any subsequent reductions should also be subject to similar scrutiny and debate in full public view. Making such cuts that reduce the level of spending that was approved without such accountability runs completely counter to the very spirit of the functioning of Indian democracy.

Unfortunately, the closing years of the UPA-2 government were marked by just such an unacceptable tendency. As December approached, with just one quarter of the fiscal year remaining, the former Finance Minister P. Chidambaram would decide that the fiscal targets (in terms of fiscal deficit to GDP ratios) were in danger of being overshot, and would arbitrarily announce cuts to allocations of different Ministries – sometimes even blanket cuts of 20 per cent that the Ministries would then have to cajole and beg to reduce even partially. These cuts also fell on some important areas of public social spending, including the UPA's "flagship schemes", which would thereby be squeezed of resources.

This was bad enough and extremely reprehensible. But the current Modi government appears to have gone one step ahead of this, by not just imposing sweeping cuts to important areas of public spending, but trying to do so by stealth without allowing any kind of public knowledge, much less scrutiny. Instead of open declaration of such cuts, which would no doubt be controversial – and far from seeking Parliament's approval for such spending cuts – there are reports that the Finance Ministry has informed various Ministries that there would be significant reductions in any further allocations they would receive in the remainder of the financial year until March 2015.

The purported reason for this is the need to contain the fiscal deficit to the proposed 4.1 per cent of GDP that was announced as the goal in the Budget speech. But this number depends on not just the revenues raised and the expenditure made, but on the rate of GDP growth, which forms the denominator. The Finance Minister had assumed nominal GDP growth of 13.4 per cent, but both real GDP growth and inflation have been lower than anticipated so the nominal GDP growth this year is likely to be around 11 per cent. This would obviously cause the ratio to rise, also because tax revenues are lower than expected as GDP growth slows. But the Finance Bill does not talk about this ratio: it refers to actual numbers for spending, and it is these numbers (approved by parliament) that Finance Minister Arun Jaitley now seeks to slash.

The proposed cuts in social expenditure are all the more alarming, and likely to be really severe in their impact, because Mr Jaitley's budget had already reduced proposed spending in these areas by around 15 per cent compared to the previous year. Even in areas where the nominal amount remained unchanged, this implied a cut in real terms because of inflation. But now on top of that, apparently the Ministry is seeking further cuts in areas that are critical for public well-being. If the media reports are to be believed, health sector plan expenditure is to be cut by much as Rs 7,000 crore. The hugely important spending of Departments like those of Rural Development, Panchayati Raj and Drinking Water and Sanitation are to face cuts of around 25 per cent. (The last is particularly ironic given the Prime Minister's much publicised brouhaha around the Swachch Bharat Campaign.)

One of the most egregious of proposed cuts relates to the employment programme of the MNREGA, which this government has already sought to undermine in myriad ways. Reliable sources that have been quoted in the media note that the proposed cut is Rs 3,000 crore to the already low budget estimate. There are several reasons why this is not just wrong but illegal. To start with, the law (that was unanimously passed in parliament, with the consent of all MPs including those belonging to the BJP and other NDA constituents) envisages the MNREGA as providing demand-driven employment. In other words, the only cap is the 100 days per household (which is incidentally nowhere near being met except in the remarkable state of Tripura).

As long as there is demand for employment, the state governments – and therefore the central government – are duty bound to provide works, and therefore there should be no question of a budget cap on this scheme. Yet the central government (unfortunately even in UPA-2 after 2011-12) has effectively exercised such a cap by keeping the budgetary allocation on this scheme nearly constant at between Rs 30,000 and Rs 33,000 crore. This obviously implies a decline in real terms. But what is worse is that this was not because of low demand for the scheme. On the contrary, the central government simply delayed payment to states, which were therefore unable to pay wages to workers who had already worked for the scheme.

As a result, even in the current budget year, there was an amount of Rs 9,000 crore worth of unpaid wages that was left over from the previous year. Obviously, this would have to be the first call on the resources for this programme. But that means the actual budgetary outlay on this scheme this year was only Rs 24,000 crore, because Rs 9,000 would have to go to pay the previous year's wages. This is a huge nominal decline – on which a further cut of Rs 3,000 is now sought to be imposed.

It is hard to think of a more effective way of killing the scheme. It is certainly not the case that there is no demand for work – in fact around ten Chief Ministers (including some in BJP-ruled states) have already written to the Centre demanding more funds which have thus far been denied. If the state governments are unable to make the wage payments, workers will again not be paid for work they have already done. Indeed, there are reports of some workers having to wait for their wage arrears for more than a year. Obviously state governments will try to avoid setting up new works in such a context. And this will become easier because the workers themselves will get disheartened and not seek work form a programme that does not ensure timely wage payment. There are already reports from many parts of the country that workers are once again migrating in search of short-term work because of this failure. And then the government will find it easy to declare that the programme is not really working, so it may as well be reduced (to the poorest districts) or simply closed down.

Another shocking cut that is being talked about is that which has purportedly been proposed on the National Aids Control Programme. Spending on this actually is a life and death question for poor people who are afflicted with HIV-AIDS, who rely crucially on the medicines and other support made available through this programme. Yet this is to be cut by around Rs 450 crore, a decline of nearly a quarter in nominal terms. Similarly, the project to create “one stop crisis centres” for women, which was one of the official responses in the wake of the public outcry over the ghastly “Nirbhaya case” gang rape and murder of a young woman in Delhi, had been given a budget of Rs 200 crore. That project is apparently now to be abandoned completely.

It is worth noting that even for budgetary savings, such cuts should not be necessary because of other price movements that have benefited the public fisc. This government is the (apparently undeserved) beneficiary of the sharp drop in global oil prices, which should certainly reduce the subsidy burden for oil and thereby lead to significant savings. So with appropriate fiscal management, there should really be no need to cut down on these essential items of public spending.

The deep cynicism of this approach is shocking, but what is possibly even more shocking is the comparative ease with which these strategies have been utilised so far. Much more public outcry is required to force the government to implement what is now a law of the land. And much more outcry and protest is also needed to ensure that the government releases funds for spending on the other programmes that matter for ensuring the basic needs of the people. There is an obvious contradiction that must be highlighted: if real GDP is growing by more than 5 per cent in the current year, why should spending on health, nutrition and education, etc. be cut at all? At the very least it should grow by a minimum of 5 per cent and in fact it should increase by more to ensure that the people at large benefit from this growth, rather than just some favoured cronies of the government.

The sad part is that this strategy of imposing fiscal austerity will not even work in terms of its stated aim of delivering higher growth. The idea is that restraining fiscal deficit to GDP ratio is crucial for attracting foreign investors, who are supposed to be the main force driving future economic expansion. But if the spending cuts operate to reduce people’s real incomes, they will have negative multiplier effects that will further cause aggregate economic activity to decelerate. And if the denominator falls, the fiscal deficit to GDP ratio will also not improve as desired.

*** This article was originally published in the Frontline, Print edition: December 26, 2014.**