सत्यमेव जयते

GOVERNMENT OF INDIA

Medium-term Expenditure Framework Statement laid before Parliament as required under the Fiscal Responsibility and Budget Management Act, 2003

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PREFACE

Section 3 of the Fiscal Responsibility and Budget Management (FRBM) Act, 2003 require the Government to place three Statements of fiscal policy namely the Medium-term Fiscal Policy Statement, the Fiscal Policy Strategy Statement and the Macro-economic Framework Statement in both Houses of Parliament. This section has been amended to require the Government to lay a fourth statement viz. the Medium Term Expenditure Framework (MTEF) in both Houses of Parliament, immediately following the session of the Parliament in which the budget has been presented.

The MTEF is to set forth a three-year rolling target for the expenditure indicators with specification of underlying assumptions and risks involved. The MTEF is essentially expected to be a vertical expansion of the expenditure projections in the MTEF Statement. The objecive of the MTEF is to provide closer integration between budget and the FRBM Statements. It also furthers the Governmentôs comitment towards fiscal consolidation.

MEDIUM-TERM EXPENDITURE FRAMEWORK

A. MEDIUM-TERM EXPENDITURE PROJECTIONS

(₹ crore)

	Revised Estimates 2013-14	Budget Estimates 2014-15	Projection for next two years 2015-16	2016-17
Revenue Expenditure				
1. Salary	82025	90636	99625	119550
2. Interest	380066	427011	468431	515275
3. Pension	74076	81983	90154	108182
4. Subsidy-				
a. Fertiliser	67972	72970	76000	85000
b. Food	92000	115000	120000	130000
c. Petroleum	85480	63427	50000	40000
5. Centralised provision for Grants to States	138038	125332	127926	129524
6. Defence	124800	134412	147853	177424
7. Postal Deficit	5880	6908	6908	6908
8. External Affairs	8665	9977	10041	10084
9. Home Affairs	13989	16542	16809	17039
10. Tax Administration	4505	2988	12988	12988
11. Finance	20133	22277	22546	22730
12. Education	64867	71996	76762	79958
13. Health	24224	31624	34259	35484
14. Social Welfare	30406	35347	38671	40109
15. Agriculture and Allied	23869	28815	30416	31335
16. Commerce and Industry	12478	16444	16178	16543
17. Urban Development	2823	15172	15588	15874
18. Rural Development	77302	106031	115334	119573
19. Development of North East	1662	2134	2348	2583
20. Planning and Statistics	5894	6164	6419	6577
21. Scientific Departments	7601	10096	10393	10590
22. Energy	7021	11197	12011	12369
23. Transport	15554	17765	18125	18407
24. IT and Telecom	4632	7194	8060	8471
25. UT	5884	6167	6277	6352
26. Others	17693	32504	34237	34972
Total-Revenue Expenditure	**1399540**	**1568111**	**1674359**	**1813899**
of which **Grants for Creation of Capital Assets**	**138228**	**168104**	**301598**	**253496**

(₹ crore)

	Revised Estimates 2013-14	Budget Estimates 2014-15	Projection for next two years 2015-16	2016-17
Capital Expenditure				
1. Defence	78872	94588	108776	116390
2. Home Affairs	6805	10159	14275	15608
3. Finance	19071	16130	21912	22769
4. Health	1590	2068	3483	3830
5. Commerce and Industry	2437	1233	1637	1760
6. Urban Development	6937	9767	11853	12378
7. Planning and Statistics	365	797	1113	1224
8. Scientific Departments	2587	3898	5273	5600
9. Energy	4682	7124	9904	10880
10. Transport	49911	54759	69767	73863
11. IT and Telecom	503	3993	5352	5690
12. Loans to States	11000	12000	13200	13992
13. UT	1328	1727	2244	2378
14. Others	4805	8539	10948	11776
Total-Capital Expenditure	**190894**	**226781**	**279738**	**298139**
Total Expenditure	**1590434**	**1794892**	**1954096**	**2112038**

B. ASSUMPTIONS UNDERLYING THE MEDIUM-TERM EXPENDITURE PROJECTIONS:

Growth of gross domestic product (GDP) at factor cost at constant 2004-05 prices declined from 8.9 per cent in 2010-11 to 6.7 per cent in 2011-12 and further to 4.5 per cent in 2012-13. Among the factors that contributed to the slowdown included structural constraints viz. delays in projects, bottlenecks in environmental approvals and land acquisition, elevated inflation and external imbalances, in addition to uncertain global economic situation. There was a marginal improvement in 2013-14 with GDP growing at 4.7 per cent. The phase of sub 5 percent growth in the last two years is characterized by a moderation in services growth and a protracted slowdown in industry. Higher growth in agriculture on the back of a steady monsoon and robust growth in financial and business services helped the modest uptick in growth in 2013-14.

During the first quarter of 2014-15, early signs of recovery could be seen with growth rate at 5.7 per cent as against 4.7 per cent in the corresponding quarter of 2013-14. Based on the wholesale Price Index, the average inflation during 2013-14 was 6.0 per cent. During the first quarter of 2014-15, it was 5.8 per cent as compared to 4.8 per cent during the corresponding quarter of 2013-14. The trade deficit for 2013-14 was US$ 135.8 billion. During the first quarter of 2014-15 (April-June 2014), exports, imports and trade deficit were US$ 80.1 billion, US$ 113.1 billion and US$ 33.1 billion respectively, as compared to US$ 73.4 billion, US$ 120.9 billion and US$ 47.4 billion respectively in the first quarter of 2013-14.

The net invisibles balance (invisibles receipts minus invisibles payments) was US$ 115.2 billion during 2013-14 as compared to US$ 107.5 billion during 2012-13. Reflecting the changes in trade balance and invisibles balance, the current account deficit decreased sharply to US$ 32.4 billion in

2013-14, as compared to US$ 88.2 billion during 2012-13. The current account deficit decreased to US$ 7.9 billion in the first quarter of 2014-15, as compared to US$ 21.8 billion in the corresponding quarter of 2013-14.

Indiaôs foreign exchange reserves increased to US$ 304.2 billion at end-March 2014 from US$ 292.0 billion at end-March 2013 and they were further increased to US$ 316.1 billion at end-June 2014. The annual average exchange rate of the Rupee was ₹ 60.50 per US$ in 2013-14 as compared to ₹ 54.41 per US$ in 2012-13.The monthly average exchange rate of the Rupee (RBIôs reference rate) appreciated from ₹ 61.01 per US$ in March 2014 to ₹ 59.73 per US$ in June 2014.

The Budget 2014-15 was presented against the backdrop of some positive developments that auger well for macroeconomic stabilization, the most significant was the dramatic improvement in the external economic situation with the current account deficit declining to 1.7 per cent of GDP and the economy firmly on the trajectory of fiscal prudence. On the expectation of modest global recovery, modest recovery in manufacturing and absence of large upshots in the international energy prices, the economy was expected to register real GDP growth in the range of 5.4 to 5.9 per cent in 2014-15.

Headline WPI inflation has moderated in recent months. While steps are being taken by the Government to improve investor sentiments and to address the slowdown in growth as well as the fiscal situation, the global economic scenario is yet to witness decisive improvement.

According to October, 2014 update of World Economic Outlook published by International Monetary Fund, due to weaker-than-expected global activity in the first half of 2014, the growth forecast for the world economy has been revised downward to 3.3 percent for this year, 0.4 percentage point lower than in the April 2014 World Economic Outlook (WEO). The global growth projection for 2015 was lowered to 3.8 percent. Largely Downside risks have increased since the spring. Given these increased risks, raising actual and potential growth must remain a priority. In advanced economies as well as emerging market and developing economies, there is a general, urgent need for structural reforms to strengthen growth potential or make growth more sustainable.

Assessment of the fiscal position and consequent expenditure projection for the Government has to be made in this macroeconomic backdrop. As committed by Government there was a marked improvement in fiscal situation in 2013-14. As per the fiscal roadmap, Government committed to progressively reduce the fiscal deficit to 3.0 per cent of GDP by the end of F.Y. 2016-17. Budgetary estimates of 4.8 per cent for fiscal deficit in 2013-14 were revised to 4.6 per cent in R.E. 2013-14, against which actual (provisional) achievement was 4.5 per cent of GDP. Measures undertaken by Government to rationalize expenditure and mobilize resources have thus created necessary fiscal space.

The General Budget 2014-15 re-affirms Governmentôs commitment to carry the process of fiscal consolidation to its logical end. Accordingly, the fiscal deficit target of 4.1 per cent has been adopted in this yearôs fiscal policy. The target is commensurate with the fiscal target laid down in the amended FRBM Rules notified in 2013. In the medium term, this is to be reduced to 3.6 per cent in 2015-16 and 3.0 per cent in 2016-17. Similarly target for Revenue deficit is 2.9 per cent of GDP in 2014-15 is to be reduced to 2.2 per cent in 2015-16 and 1.6 per cent in 2016-17. Effective Revenue deficit of 1.6 per cent in B.E. 2014-15 is to be reduced to ñnilò by 2015-16. The above mentioned fiscal targets have been informed in the Medium Term Fiscal Policy statement presented along with General Budget 2014-15 in the Parliament.

In the process of achieving these fiscal targets it has been estimated that outstanding liabilities as Percentage of GDP will be reduced to 41.5 per cent in 2016-17 from the level of 45.4 per cent estimated for 2014-15. Further Gross Tax revenue (before devolution of State share) as a percentage of GDP will progressively rise to 11.2 per cent by 2016-17 from the level of 10.6 per cent estimated in Budget 2014-15.

Increase from Tax to GDP ratio of 10.6 per cent to 11.2 per cent requires an average annual tax growth of 17.7 per cent and an average tax buoyancy of 1.32. In pre-crisis period, growth in gross tax revenue for 2006-07 and 2007-08 was 28.9 per cent and 25.3 per cent respectively. These reforms were driven mainly by direct taxes, whose average annual growth rate during 2003-08 was about 28 per cent. The buoyancy of tax revenue with respect to GDP was nearly 1.5 during this period. Therefore, fiscal consolidation strategy of Government primarily hinges on reclaiming high growth in gross tax revenue achieved in the past. This is also essential for creating space for financing programmes of Government.

One of the risks to the assumption on resources side is the award of XIV Finance Commission. The projection period crosses the time horizon of XIII Finance Commission and spills over to first two fiscal years of the award period of the newly constituted XIV Finance Commission. The fiscal plan outlined in this document may have to be redesigned if the XIV Finance Commission changes the State share significantly.

Non-tax revenues of Centre mainly comprises interest and dividend receipts of the Government, receipts from services provided by Central Ministries and Departments like supply of Central Police Force to various agencies, issue of passport and visa, registration of companies, patent and license fees, royalty from off-shore oil fields, various receipts from telecom sector etc. Budget 2014-15 has been presented with non-tax revenue as 1.7 per cent of GDP. It has further been assumed that certain one-time receipts budgeted in 2014-15 will not be available in 2015-16 and 2016-17. With these assumptions the ratio of Non-Tax revenue to GDP has been estimated to decline to 1.4 per cent of GDP in 2015-16 and to 1.2 per cent in 2016-17.

In F.Y. 2013-14, government decided to create a separate fund, National Investment Fund (NIF) under Public Account, with the intent that proceeds from disinvestment will only be deployed for specific authorized purposes. With this major step forward, the proceeds will not be available to fund regular government spending. In B.E. 2014-15, other non-debt capital receipts (including disinvestment receipts) have been estimated to ₹ 63,425 crore. Over the medium term frame work, an amount of ₹ 55,000 crore has been estimated for the years 2015-16 and 2016-17.With the resources outlined above and underlying assumptions, a projection for various items for expenditure over a medium term framework has been made.

1. REVENUE EXPENDITURE:

Major items of Revenue expenditure include:

(a) Salaries: -

An important requirement for projections of salaries is to adequately provide for the increase in Dearness Allowance and normal annual increments. However, the projection period spills over to beginning of the award period of the newly constituted VII Central Pay Commission (CPC). In the view of this, a normative growth of 10 per cent over the salary outlay of 2014-15 (B.E.) has been provided for first year of projection period. Whereas, a higher than normative growth has been made for the F.Y. 2016-17. Salaries shown in the Medium term expenditure framework also includes ñGrants-in-aid for salariesò.

One of the risks to the projection on salaries is the award of VII CPC. Since, the award of VII CPC is not known; it is difficult to anticipate the change in remuneration structure. Therefore, projections on salaries as outlined in this document have to be redesigned to align with the changes suggested by VII CPC.

(b) Pensions: -

Expenditure on Pension payment includes both Defence and Civil pensions. In nominal terms a provision of ₹ 81,983 crore has been made in B.E. 2014-15 for Pensions. As like in salaries, a normative growth of 10 per cent has been assumed for the projections of F.Y. 2015-16 and higher than normative growth has been made for the projection of outlay on Pensions during F.Y. 2016-17. As mentioned under salaries, one of the risks to the projection on pensions is the award of VII CPC. Therefore, the projections on pensions as outlined in this document have to be redesigned to align with the changes suggested by VII CPC.

(c) Interest payment: -

One of the largest items of revenue expenditure is the Interest payment commitment of the Government. As per the Constitutional provisions this is a charged item of expenditure. Fiscal expansionary measures undertaken by Government post crisis have resulted in sharp increase in the Interest payment commitments. Due to accumulation in the debt stock of the Government, as a percentage of net tax revenue of the Centre, interest payments jumped from 38.9 per cent in 2007-08 to 43.4 per cent in 2008-09 and further to 46.7 per cent in 2009-10. In B.E. 2014-15, interest payment is projected at 43.7 per cent of net tax to Centre, showing a decline following fiscal consolidation. It has been assumed that with Government deficit coming down in the medium term and softening of interest rate regime, commitment on this count will decline.

(d) Major Subsidies: -

National Food Security law provides food as a legal entitlement for nearly 2/3rd of Indian population. Separately, there are enabling provisions in the Law to provide for nutrition requirements of pregnant and lactating women. Major subsidies have been budgeted at ₹ 2, 51,397 crore in B.E. 2014-15. Total subsidies were at 2.3 per cent of GDP in 2013-14 and are budgeted to be at 2.0 per cent of GDP in 2014-15. In the medium term adequate provisions have been kept in the view of above law. Constrained by the fiscal roadmap, Government faces the challenge of containing outlay on the other Subsidies viz. Petroleum and Fertilizer within the sustainable limits. Key to meeting these challenges lies in achieving greater efficiency in the systems delivering these subsidies. To improve targeting of subsidies, Government has embarked upon an ambitious programme to directly transfer government benefits into Aadhar linked bank accounts of beneficiaries. Issues of eligibility and duplicate transfers can be handled much better using the Aadhar platform. With decontrol of Petrol and Diesel prices and better targeting of Kerosene and LPG subsidies, fuel subsidies are likely to be kept in check over projection period. On the pricing issue, there is a need to undertake pricing reforms in the urea sector. This is not only essential for reducing the subsidy bill, but is also necessary for a more balanced usage pattern of N, P and K Fertilizers

(e) Defence Services: -

Defence expenditure on Revenue account mainly comprises of salary expenditure of armed forces and their operational expenses. Defence Revenue expenditure is estimated to grow at approximately 10 per cent over the base of ₹ 1.34 lakh crore (BE 2014-15) in F.Y.2015-16. For F.Y. 2016-17, likely impact of VII CPC award has been taken into account.

(f) Other revenue expenditure: -

Projection for budgetary allocation in the medium term in respect of health and education, agriculture and allied activities, rural development, social welfare programmes, external affairs, home affairs etc. has been done keeping in view the availability of resources and financing requirement for various programmes of Government in line with various decisions and commitments. In BE 2014-15 a provision of ₹ 6,908 crore has been made for Postal deficit. In the medium term it has been kept at the same level. Additional provision has been kept in the projection years 2015-16 & 2016-17 on account of Central Sales Tax (CST) compensation to States.

2. GRANTS-IN-AID FOR CAPITAL ASSETS:

In B.E. 2014-15, a provision of ₹ 1, 68,104 crore is made for Grants-in-Aid for creation of capital assets. Amended FRBM Act mandates to eliminate the effective revenue deficit (revenue deficit *less* Grants-in-aid for creation of capital assets) by 31st March 2015. Targets for effective revenue deficit at 1.6 per cent of GDP in B.E. 2014-15 shows progressive improvement over previous year. However, while adhering to the path of fiscal consolidation, the imbalances on revenue account on this count could not corrected to the extent mandated under the new FRBM regime. In view of this, provision has been made during projection period to eliminate effective revenue deficit by 31st March, 2016.

3. CAPITAL EXPENDITURE:-

(a) Plan: -

Plan Capital expenditure of Government mainly consists of gross budgetary support to Indian Railways, investment in National Highways and various Urban Metro construction and recapitalization of Public Sector Banks, external assistance backed loans to Public sector banks and equity infusion in PSUs. Since the overall effort would be to reduce the revenue deficit of the Government, it is essential that within the overall Plan expenditure, the expenditure on Capital components grows faster than the revenue component. Plan capital expenditure is budgeted at 21.2 per cent of total plan expenditure in 2014-15 and is projected to increase at a faster pace in the first year of projection period and then grow at nominal rate on the elevated base. It may be relevant to mention here that more items of Plan capital expenditure will be financed from National Investment Fund. This is being funded through disinvestment proceeds.

(b) Non-Plan:

On the Non-Plan side, the major portion of Capital expenditure consists of outlay on Defence Capital expenditure. In BE 2014-15 a provision of ₹ 94,588 crore has been made for capital outlay on the Defence Services for modernization of Defence Forces. Over the projection period this is estimated to grow at 15 per cent in the first year and then at 7 per cent on the elevated base in the second year of projection period. Other items of expenditure include expenditure for production of Heavy Water, investment in International Financial Institutions and for construction of certain strategic roads in border areas.