

The Central Budget: A Review

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The economic significance of the budget can hardly be over-emphasised. Presenting as it does estimates of revenue receipts and expenditures as well as the schedule of activities to be undertaken and the mode of financing them, the budget is, so to speak, the master plan of the Government.

With the continued growth of the role of the State in economic life, fiscal policy has greatly gained in importance in recent years.

There has been a growing recognition that the fiscal operations of the Government affect not only the pattern of production and the distribution of the total product but also the level of production, demand and employment in the economy.

I

In 1959, recognising that the root cause of inflation lay in the deficit financing operations of the past governments, the present Government decided upon a policy of living within its means and to put a stop to deficit financing.

To avoid slowing down the tempo of development on account of the abandonment of deficit financing, the Government attempted to restrain the rising trend in non-development expenditure on the one hand and sought to mobilise additional resources through non-inflationary means on the other.

The budget for 1960-61 seeks to carry forward this policy. For the second year in succession, the budget makes no provision for borrowing from the country's central bank. Non-development expenditure will be strictly controlled while resources for a somewhat enlarged outlay on development will be found mainly through external sources and higher taxation.

<i>Expenditure</i>	<i>(In crores of Rupees)</i>		
	1959-60 (Budget)	1959-60 (Revised)	1960-61 (Budget)
1. Revenue Expenditure ..	151.46	162.66	169.86
2. Development Outlay ..	149.66	162.90	172.19
3. Non-Development Outlay ..	30.08	30.80	7.00
4. Total Expenditure ..	<u>331.20</u>	<u>356.36</u>	<u>349.05</u>
<i>Financed by</i>			
1. Revenue Receipts ..	158.46	175.84	171.37
2. Permanent Debt (Internal) ..	7.00	18.59	10.00
3. Floating Debt ..	17.62	13.44	-0.29

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4. Recoveries of Loans and Advances	..	4.33	4.37	4.42
5. Foreign Aid and Loans	..	101.03	87.30	108.47
6. Other Capital Receipts	..	3.72	4.54	4.65
7. Unfunded Debt	..	11.80	11.86	10.24
8. Accretions to Reserve Funds	..	15.43	15.40	23.75
9. Deposit and Remittance Heads	..	4.97	3.62	2.50
10. Drawal of Cash Balances	..	6.84	21.40	13.94
Total Financing	..	<u>331.20</u>	<u>356.36</u>	<u>349.05</u>

Before analysing the budget it may be useful to summarise the estimates:

The revised estimates for 1959-60 clearly reflect the success of the new fiscal policy. The surplus on revenue account is placed at Rs. 13.18 crores in the revised estimates as against Rs. 7 crores in the budget estimates.

This is because according to revised estimates, revenue receipts for 1959-60 are expected to be higher by Rs. 17.38 crores at Rs. 175.84 crores which improvement is only partly offset by the rise of Rs. 11.20 crores in revenue expenditure to Rs. 162.66 crores.

The rise in revenue receipts and expenditure is attributable in part to the inclusion in the revenue budget, both on the receipt and expenditure sides, of an amount of Rs. 12 crores of defence expenditure financed from US defence support which was previously shown as a reduction in defence expenditure.

Isolating the effect of this new method of showing defence budgetary support received from the United States, the increase in revenue receipts was of the order of Rs. 5.38 crores while revenue expenditure was actually lower by Rs. 0.80 crore.

This shows that while the revenue receipts exceeded the expectation, the Government was able to exercise proper control on its current expenditures with a result that a large surplus was available for financing a part of the capital outlay.

The revised estimates for 1959-60 show a rise of Rs. 13.96 crores in the capital expenditure of the Government as compared to budget estimates but the bulk of the rise (Rs. 13.24 crores) is accounted for by the increase in development expenditure.

It is noteworthy that despite the increase in the capital expenditure of the Central Government, there was no net borrowing from the State Bank of Pakistan during the year. However, there was a larger utilisation of cash balances, necessitated mainly by the shortfall in receipts under foreign loans and grants.

The financial discipline imposed by the present Government has had a favourable effect on the monetary situation. For the first time in the post-Korean period the Government sector did not add to money supply during 1959-60.

In fact, Government financial operations exercised a net contractionary influence of Rs. 3.38 crores as the table below will show:

Fiscal Years

		(Crores of Rs.)		
		1957-58	1958-59	1959-60 (provisional)
Increase/Decrease in Money Supply	..	+35.14	+19.79	+29.76
Causative Factors:				
Expansion (+)				
Contraction (-)				
1. Domestic Private Sector	..	+ 4.15	— 0.42	+35.74
Adjustment for Shift to Time Deposits	..	—13.16	—5.32	—19.26
		— 9.01	— 5.74	+16.48
2. Government Sector	..	+71.51	+21.73	+12.41
Adjustment for Accumulation of Counterpart Deposits	..	— 3.58	— 2.68	—15.79
		+67.93	+19.05	— 3.38
3. Foreign Sector	..	—28.23	+12.17	+21.04
4. Other Factors	..	+ 4.45	— 5.69	— 4.38
5. Total Causative Factors	..	+35.14	+19.79	+29.76

Within eight months of the assumption of office the new Government was able to effect a notable improvement in Government finances so that during the year 1958-59 as a whole the quantum of money creating deficit in Government transactions was brought down to Rs. 19.05 crores as compared to Rs. 67.93 crores in the previous year.

The metamorphosis was completed in 1959-60, when in sharp contrast to past years, Government operations actually served to partially offset the expansionary influences emanating from other sectors.

The achievement of an overall surplus in Government financial transactions within such a short period is truly remarkable, for large-scale deficit financing and inflationary pressures built up in the economy over the past years had rendered the task of balancing the budget a most difficult one.

The principles underlying the new fiscal policy of the Government find fuller expression in the latest budget for 1960-61. The revenue receipts for the fiscal year 1960-61 are estimated at Rs. 171.37 crores at the previous level of taxation as compared to Rs. 175.84 crores in the revised estimates for 1959-60.

The decline is due largely to lower anticipated receipts from the two commercial departments viz; the Railways and the Posts and Telegraphs on account of the decision to earmark larger sums from their earnings to depreciation and renewal reserve funds.

Receipts from customs duties are expected to fall by Rs. 1.03 crores to Rs. 44.75 crores, but this will be partly offset by the anticipated increase of Rs. 0.48 crore in receipts from central excise.

Receipts under debt services, civil administration and currency and mint are expected to show increases of Rs. 1.00 crore, Rs. 0.37 crore and Rs. 0.19 crore respectively. Revenue expenditure in 1960-61 is expected to go up by Rs. 7.20 crores to Rs. 169.85 crores compared with the revised estimates of 1959-60.

By far the largest increase will take place under Beneficent Departments (Rs. 4.53 crores) followed by defence services (Rs. 1.43 crores) and debt services (Rs. 1.03 crores). The revenue account was thus expected to show a small surplus of Rs. 1.51 crores at the previous level of taxation.

However, the revenue surplus will go up to Rs. 11.41 crores taking into account the effect of the new tax measures in the 1960-61 budget.

On capital account, the total expenditure is estimated at Rs. 179.19 crores, representing a decline of Rs. 14.51 crores compared to the revised estimates for 1959-60.

However, the decline is due entirely to reduction in non-development expenditure as compared to last year when the Government had to make a provision of Rs. 23.81 crores for payment of Pakistan's increased subscription to the International Monetary Fund.

Development expenditure in 1960-61 is actually expected to increase by Rs. 9.29 crores to Rs. 172.19 crores.

It is expected that foreign aid and loans will be forthcoming in a much larger measure during 1960-61 to finance the capital expenditure of the Central Government. At the budgeted level of Rs. 108.47 crores, these items represent roughly 60 per cent of the total capital budget.

II

Notwithstanding the larger foreign aid component in the budget, the Government intends to intensify its efforts at the mobilisation of domestic resources. Apart from higher taxation, the Government have announced the introduction of a Prize Bond Scheme to tap larger savings.

The stepping up of the limit of Investment Allowance from Rs. 8,000 to Rs. 12,000 may also be expected to mobilise additional savings for development in the public sector.

In conformity with the declared policy of the Government to afford maximum incentives to the private sector, the budget incorporates several tax measures to encourage private enterprise and risk bearing. The rates of corporate taxation have been reduced by 5 to 10 per cent.

In the case of industrial companies established after Independence and declaring dividends in Pakistan the rate has been reduced from 55 per cent to 45 per cent. Foreign industrial companies would now pay tax at 55 per cent instead of 60 per cent previously.

Similarly, the tax rate of commercial companies declaring dividends in Pakistan and of industrial companies established before Independence has been reduced from 60 to 50 per cent. Tax rate for companies in this group not declaring dividends in Pakistan has been brought down from 65 per cent to 60 per cent.

The period of "Tax Holiday" has been extended from two to four years for industries set up in the comparatively developed areas of West Pakistan and six years for industries set up in East Pakistan and relatively underdeveloped

areas of West Pakistan. Both these measures are intended to stimulate productive activity in the domestic private sector as well as to attract foreign capital.

As a further incentive to the investment of foreign capital in Pakistan, it has been decided to exempt from income tax interest payable by industrial undertakings in Pakistan on approved loans received from abroad either in cash or in the shape of plant or machinery provided the country from which loans have emanated either grants total exemption from its own tax to the interest income in question or agrees to give credit in the home assessment of the lender for tax payable or such income in Pakistan but not actually charged.

Simultaneously with the reduction in tax rates on companies, the system of "grossing up" of dividends has been abolished making the net dividends received taxable like other income but in order to give relief to small investors it has been decided to exempt from tax the first Rs. 1,000 of dividend income.

In the field of indirect taxation, the most important measure is the increase in the basic rate of sales tax from 10 to 12-1/2 p.c. The increase has been dictated by the urgent necessity of raising the tax revenues of the Government for stepping up development activity without taking recourse to inflationary methods of finance. It would also serve to restrain consumption expenditures.

With the same object in view, excise duties on certain items have been increased while new duties have been imposed on cement, mild steel bars and betel-nuts.

The customs tariff has been thoroughly revised; under revised schedule, rates of duties on luxury goods and non-essential items have been maintained or occasionally enhanced, but duties on essential items, especially raw materials, have been reduced. The measures for increased indirect taxation in the budget have to be viewed in the context of the needs of our developing economy.

III

The only alternatives to adequate taxation are a slower rate of development or resort to inflationary methods of finance. An adequate rate of development is the only answer to the crushing poverty with which our masses are afflicted.

Development through inflation is highly inequitable for it imposes a relatively greater burden on the economically weaker sections of the population and also tends to be self-defeating. An increase in the tax burden is therefore irresistible if development is to be pushed forward without endangering monetary stability.

As it is administratively difficult to tax the majority of the population belonging to low-income groups directly, resort to indirect taxation is the only means through which they can be made to contribute their share towards the development effort.

However, the budget makes every attempt to avoid imposing undue hardships on the community by totally exempting from sales tax certain articles of daily use and confining increases in import duty to articles which are generally consumed by the well-to-do classes.

While pursuing a policy of sound finance, the Government are most anxious to step up the rate of development in the country. The direct capital outlay of the Central Government on development will be smaller by Rs. 9.84 crores during 1960-61 but allocations to the provinces will be substantially greater that is, Rs. 99.87 crores as compared to Rs. 66.92 crores in 1959-60.

The Central and Provincial Governments have combinedly budgeted a total development expenditure of Rs. 222 crores in 1960-61 as compared to about Rs. 185 crores in 1959-60. This clearly demonstrates that Government are determined to implement the largest development programme that is consistent with the availability of real resources.

This can be achieved over the long run only by ensuring that short-term programmes do not overstrain the economy by inflicting on it the mounting tensions of a continuously rising price level and recurrent foreign exchange crisis.

By relating the size of the development programme to the availability of real resources, including those which are generated as development proceeds, Government appear to be anxious to avoid a false sense of complacency about the size and the intensity of the effort required for putting the programme through.

This so-called "banking approach" will help the Government to avoid the pitfalls inherent in a policy of "easy finance" which inveigles a Government into undertaking commitments which turn out to be insupportable by real resources, thereby forcing the Government to try to cover up the short-fall through resort to inflationary methods of finance in order to keep up a predetermined rate of spending. Needless to say, such a course can only be self-defeating for it frustrates the development effort which it professes to foster.

