RNI No. DELENG/2020/79244
ISSN 2347-1522
■ Vol. IV ■ Issue No. 2
MARCH-APRIL 2023

INDIA FOUNDATION JOURNAL

Editorial Board

Table of Contents

India Foundation Journal

Vol. IV
Issue No. 2

March-April 2023

Editor
Maj Gen (Dr) Dhruv C Katoch

Assistant Editor
Siddharth Singh

Printed on behalf of India Foundation

Printed at Pearl Printers, C-105, Okhla Industrial Area, Phase-1, New Delhi-110020

Published at India Foundation, J-1 and H-1, Ground Floor, Upasana Building, 1 Hailey Road, Near K.G Marg, New Delhi - 110001

RNI No.- DELENG/2020/79244
ISSN 2347-1522

Annual Subscription - Rs.3000/-
Single copy - Rs.500/-

*For advertising details contact
Phone: 011- 41654836 / 43012351,
journal@indiafoundation.in
www.indiafoundation.in*

About India Foundation

India Foundation is an independent research centre focussed on the issues, challenges, and opportunities of the Indian polity. The Foundation believes in understanding contemporary India and its global context through the civilizational lens of a society on the forward move. Based on the principles of independence, objectivity and academic rigour, the Foundation aims at increasing awareness and advocating its views on issues of both national and international importance.

With a team of dedicated professionals based at its office in New Delhi, the Foundation works with partners and associates both in India and overseas to further its stated objectives.

About India Foundation Journal

The India Foundation Journal is led by an Editorial Board of eminent scholars and leaders from various spheres of Indian public life. The bi-monthly journal covers a wide range of issues pertinent to the national interest, mainly focusing on international relations, national security, legal and constitutional issues and other issues of social, religious and political significance. The journal seeks articles from scholars with the intent of creating a significant body of knowledge with a nationalist perspective and establish a recognised forum for debates involving academicians and policymakers.

A Vision for Bharat

Dhruv C. Katoch*

The Union Budget 2023-24 has been characterised as the first budget for "Amrit Kaal"— A vision to see a transformed Bharat by the time the nation celebrates its Independence centenary on 15 August 2047. For the first time, we have a long-term road map of what Bharat should be in terms of its human and developmental index, with clear markers for reaching the desired end state over the course of the next quarter century.

This, by itself is a quantum leap forward from the incremental development policies followed for the most part since 1947. There was a hesitancy in envisioning a great and prosperous Bharat, which perhaps was a result of a socialist mind-set, mired in a philosophy that pedalled poverty as virtue and derided wealth as being sinful and corrupting. For decades since independence, the state set about controlling the means of production and telling the people what, how and how much they could produce and at what cost. The bureaucracy became all powerful as the arbiters of the nation's destiny and this soon morphed into a political-bureaucratic-criminal nexus.

This was a recipe for disaster and by 1990, the nation was on the verge of bankruptcy. Then came the era of reforms, which since the last decade, have taken on a more focussed approach with major initiatives like the rolling out of the GST and the JAM trinity (Jan Dhan Yojana which has provided access to India's poor to the banking sector, Aadhar—a unique biometric identifier and the Mobile penetration). This has enabled targeted provision of benefits to millions below the poverty line with near zero pilferage and brought about a sense of inclusivity to an unparalleled extent. Rural housing, electricity access, toilets for all, are but a few of the myriad schemes which has seen wide penetration across the length and breadth of Bharat in a truly transformative manner.

Budget 2023-24 builds on the India story which saw a rejuvenation in 2014 after a decade of stalled economic reforms. There is renewed focus on digitisation, indigenous defence manufacture, green energy, transparency in government, skilling of the work force, education sector reforms and the like. A host of initiatives have been announced to unleash the full potential of all citizens. In this new Bharat, there is little doubt that every citizen will stand up to be counted. But a slew of challenges remain.

It would be naive to think that the major powers will look on benignly as India moves ahead. A strong and economically powerful Bharat poses a threat to the economic interests of other powers. An Atmanirbhar Bharat would be an economic challenger, and with defence indigenisation taking place at a rapid rate, a rival to the worlds military industrial complex as an arms exporter. So, there will be attempts made by both India's enemies as well as those with whom India has friendly relations, but who may view India as a serious competitor in future, to sabotage the Bharat growth story. An inkling of what the coming year holds can be seen

*Maj. Gen. Dhruv C. Katoch is Editor, India Foundation Journal and Director, India Foundation.

in attempts being made to create rift in society by inciting the public. The ham-handed manner in which the BBC tried to inflame passions by making a documentary on the post-Godhra riots of 2002, is a case in point. Another is the hit job done by a US based short-seller on the Adani business group. We are now seeing fringe Khalistani elements raising their ugly heads in a clear bid at destabilising the country. We are likely to see radical Muslim elements within the country creating discord over inane issues. There will be others with perceived grievances, who will be funded by external actors like the George Soros Open Society Foundation, the Ford Foundation and the Rockefeller Foundation, all of whom, through a network of NGOs, will attempt to spread a divisive agenda. And in all this they will receive support from both China and Pakistan, who have their own axe to grind. Unfortunately, there will be elements of certain political parties who have their own agenda, who will also lend political support to such groups.

But these challenges are an intrinsic part of trying to create a strong and vibrant Bharat. While the Government can provide the vision and the policy support, it is also up to each and every citizen to rise to the occasion, to achieve the objectives of Atmanirbharta. The nations public and private sectors too will have to play their role. The same goes for the nation’s bureaucracy. Can they measure up to the Prime Minister’s vision and play an enabling and supportive role? Therein lies the challenge.

◆◆◆

Positioning India for the Future: The Amrit Kaal Budget

Jayant Sinha*

On February 1, the Hon'ble Finance Minister Srimati Nirmala Sitharaman, presented her FY 2024 Budget to Parliament. The Hon'ble Prime Minister termed this the Amrit Kaal Budget—the budget for a golden age for India. It proved to be so. Unlike most other budgets, which are almost always criticised on multiple counts, this budget has been hailed by all stakeholders. The people of India appreciated the continued support for key welfare programs and infrastructure investment. Taxpayers loved the judicious tax cuts. Businesspeople expressed their happiness for policies supporting green growth and robust job creation. The capital markets praised the stability and continuity in policymaking. And economists were gratified to see that all the key macroeconomic parameters ranging from growth to the fiscal deficit to open market borrowings were deftly managed.

The Amrit Kaal budget was prepared under daunting circumstances. The last three years have drastically disrupted the world. The global economy has suffered from high inflationary pressures and interest rates, low investments and, more recently, a wave of layoffs in technology-based companies. Through the economic slowdown of the last three years, India has emerged as the shining star of the global economy. According to a United Nations study[1], growth prospects in the developed world have taken a sharp downturn – with the United States and the European Union growing by a low 0.4% and 0.1% in 2023, respectively. On the other hand, India is expected to grow at close to 6% in 2023, while the average growth rate in South Asia is projected to remain at 4.4%.

From being a Fragile Five country in 2013-14, India is now among the Top Five economies in the world! The Indian government's strong and stable fiscal policies have allowed the country's economy to not only emerge relatively unscathed from the pandemic, but also aid the developing world. To put the Union Budget of 2023-24 in context, it is important to understand how the major events of the past three years have impacted the world economy.

- **Covid-19 Pandemic:** Following the once-in-a-century pandemic, the World Bank projected the growth of the developing world, much like Covid-19 vaccine accessibility, to be quite uneven. As a result, Low-Income Countries (LICs) have fallen into extreme poverty due to rising food and energy insecurity. As per the Bank's projections[2], LICs with extreme poverty over 50% will rise to a positive figure by 2024, as opposed to the pre-pandemic expectation of poverty reduction. The strict, yet poorly managed, lockdowns in China have also impacted supply chains and global trade even as the world starts to recover from the pandemic.

**Jayant Sinha is the Chairman of the Standing Committee on Finance in Parliament and a Lok Sabha MP from Hazaribagh, Jharkhand. Views are personal.*

- **Russia-Ukraine War**: The conflict has had significant spill over effects on both the South Asian and global economy due to disrupted supply chains and increased food and energy prices. The impact was further magnified due to increased energy requirements, owing to climate change and disrupted energy supply following the war. As median inflation[3] reached a new high of 9% in the second half of 2022, central banks around the world tightened monetary policy, reducing inflation but temporarily slowing down growth as well.
- **Climate Change and Natural Disasters:** Even as the world was reeling from the post-Covid impact on local, regional, and global economies, it was further shaken up by grave climate change-induced disasters in the form of hurricanes, cyclones and floods. The 'State of the Global Climate 2021'[4], published by the World Meteorological Organization, reported loss and damages worth USD 100 billion in 2021. In 2022, the floods in neighbouring Pakistan devastated the country's economy[5] – with total damages at USD 15 billion, total economic losses at USD 15.2 billion, and the cost of rehabilitation and reconstruction at USD 16.3 billion, Over 33 million people were affected and almost 9 million were pushed below the poverty line. India also witnessed more frequent extreme weather events, as storms and flooding alone cost the country over USD 7.5 billion in 2021. Once the loss and damage from weather events in agriculture and other sectors are quantified, the figure will be much larger.

This year's budget is historic for two major reasons: first, it seeks to lay the foundation for the next 25 years to ensure continuity and stability in development decisions and, second, it divides policy priorities into seven interdependent, yet holistic 'saptarishis' (seven sages). Together, they make the budget people- and development-friendly. They are:

1. Inclusive Development:

Equal benefit to all sections of society through investments in agriculture and farmers' welfare, as well as medical infrastructure.

- Agriculture (BE 2023-24 = Rs 1,25,036 crore or a 5% increase over last FY RE): The proposed additions under the Budget will cater to the entire agricultural supply chain. Enhanced agriculture credit to the tune of Rs 20 lakh crore for animal husbandry, dairy, and fisheries aims to improve the quality and care of farm resources. The proposed Digital Public Infrastructure will revolutionise agricultural practices in India by providing open-source access to solutions, inputs, credit, and insurance to farmers. Decentralised storage capacity for farmers will help them realise competitive prices, and additional cooperative dairy and fishery societies will further organise the sector and bring in more formal agricultural employment. Finally, in line with the Atma Nirbhar Bharat vision of the Hon'ble Prime Minister, the Agriculture Accelerator Fund will reach young entrepreneurs in rural areas and give them an opportunity to innovate and revolutionise agricultural practices.

  Health (BE 2023-24 = Rs 89,155 crore or a 12% increase over last FY RE): Post the

Covid-19 pandemic, the focus of the health sector has shifted to infrastructure development. The Budget speech announced the establishment of 157 new nursing colleges, introducing multidisciplinary courses at medical colleges on technology, allowing private players to access the Indian Council for Medical Research (ICMR) facilities, and pushing R&D in the pharmaceutical sector. In addition, health infrastructure via the old and new All India Institute for Medical Sciences (AIIMS) has received an increased outlay, and additional expenditure under Ayushman Bharat shall further the mission of achieving universal healthcare.

2. Reaching the Last Mile:

To ensure inclusivity of tribal groups, the Budget lays special emphasis on schemes for their benefit, specifically through the new Pradhan Mantri PVTG (particularly vulnerable tribal groups) Development Mission, and by increasing the number of teachers in the Eklavya Residential Model Schools for tribal children in remote areas. Education has received a significant boost this year of 8.3% as compared to last year.

3. Unleashing the Potential:

Micro, Small and Medium Enterprises (MSMEs) form a core part of the Indian economy. India has over 63 million MSMEs, contributing 30% to its GDP, 40% to its manufacturing output, and 48% to its exports. One of the biggest challenges of the sector has been the provision of safe credit opportunities. The Standing Committee on Finance[6], in our 'Strengthening Credit Flows to the MSME Sector', had noted that more than 60% of the MSMEs currently avail credit from informal sources, depending on costly and unreliable credit. The Budget provides additional support to MSMEs through the infusion of Rs 9000 crore under the revamped Credit Guarantee Scheme. This will potentially lower the cost of capital and allow MSMEs to avail collateral-free credit guarantee of Rs 2 lakh crore. Access to reliable credit will significantly boost their output, accelerate formalisation, and increase creditworthiness.

Additionally, the Standing Committee also recommended bringing MSMEs into the digital ecosystem both for credit access and formalisation, especially given India's UPI success story. The Government further establishes an enterprise DigiLocker for MSMEs, other businesses and trusts as a one-stop solution for foundational identification and digital safe-keeping of documents.

4. Youth Power:

With a strong belief in the power of the youth and their ability to take our nation forward through the Amrit Kaal, the Budget aims to enhance the layout for skilling. The PM Kaushal Vikas Yojana 4.0 (PMKVY 4.0) will focus on technical skills like robotics, artificial intelligence, and coding to provide a stimulus to India's already booming start-up industry. Previous editions of PMKVY have provided over 10 million certifications, out of which a quarter have materialised into meaningful employment. The increased outlay for school and higher education, coupled with the National Education Policy, will provide an impetus to infrastructure-oriented, multidisciplinary, and skill-based education. The power of India's youth will be unleashed by providing them with high-quality modern education with a special focus on skill development and entrepreneurship.

5. Green Growth:

The Hon'ble Prime Minister's commitment to net zero by 2070 at COP26 laid the foundation for India's green growth. With the announcement of the target, India also committed to utilising renewable power for 50% of its energy requirements, reaching 500 GW of non-fossil energy capacity by 2030, reducing the total projected carbon emissions by one billion tonnes by 2030, and reducing the carbon intensity of the economy by 45% by 2030. The announcement came at a crucial juncture for the world, as the United Nations Environment Programme[7] projects a 2.8 degrees Celsius rise in temperature by the end of the century, as opposed to the target of capping it at 2.0 degrees Celsius by 2100. It is estimated that by 2070, over 75% of greenhouse gas (GHG) emissions will come from countries from the Global South (developing countries).

India is one of the few Global South countries that has declared a net zero target for itself. The 2023-24 Budget takes this vision forward with Rs 35,000 crore allocated for capital investments into the green transition and net zero. Additionally, support shall be provided to set up battery storage systems with a capacity of 4000 MWh. The Green Credit Programme, along with the additional outlay to the National Green Hydrogen Mission, will provide further momentum to the green transition in India. The Government is also planning to introduce an Emissions Trading System unique to India, based on buying and selling of credits earned from reducing emissions intensity, as opposed to absolute emissions reductions.

At COP26, the Hon. Prime Minister announced a requirement of $1 trillion from developed countries for climate finance.[8] India's Budget proves that it is on track to achieve its Nationally Determined Contribution (NDCs) and achieve net zero, which shall also require mobilisation of finance from the developed world, in line with the principle of common but differentiated responsibilities (CBDR).

6. Infrastructure Investment:

The last nine years have been extremely positive for India's infrastructure story. For example, the Government doubled the number of airports to 146, added close to 43,000 kilometres to the national highways, and tripled the capital expenditure on higher education institutions like AIIMS and IITs. The budget streamlines the investment pipeline for the country across sectors. Firstly, it simplifies the administrative structure for investments. It creates an Infrastructure Finance Secretariat for more private investment in public-dominated sectors like urban infrastructure, power, and others. It creates a 'Harmonised Master List of Infrastructure', with recommendations from experts on classification and financing requirements for the Amrit Kaal.

Secondly, the Budget lays great emphasis on city and urban planning through the 'Sustainable Cities of Tomorrow' mission, focusing on resource efficiency and enhanced availability and affordability. It creates the foundation for significant investment opportunities in urban infrastructure through the introduction of municipal bonds. Urban investments also get a renewed push through the Urban Infrastructure Development Fund worth Rs 10,000 crores.

Lastly, regional connectivity, railways, and logistics have been given a boost via enhanced allocation of Rs 2.4 lakh crore to the railways.

7. Financial Sector:

To reduce the cost of compliance, regulators shall be expected to review regulations through public and private consultation. Further, in order to enhance the governance of public sector banks, the Government shall propose amendments to the Banking Regulation Act, the Reserve Bank of India Act, and the Banking Companies Act. Additionally, the focus will be on setting up better digital infrastructure for payment security by using PAN as the common identifier on platforms and providing subsidies to banks on UPI payments.

Conclusion

In summary, the Amrit Kaal Budget is a visionary, well-balanced budget as it provides fresh stimulus through two key measures. Firstly, enhanced capital expenditure (capex) to boost employment, help crowd in private investments, and improve operational efficiency. This year, capex has been increased to Rs 10 lakh crore (3.3% of GDP), and effective capital expenditure, inclusive of grants-in-aid to states, to Rs 13.7 lakh crore (4.5% of GDP). Secondly, a significant middle-class tax cut to put money in the hands of consumers, generate demand, as well as increase spending and consumption. Together, both sources of stimuli will stabilise macroeconomic parameters, increase growth rate to 6-7%, and make India a shining star in the global economy by driving digitisation and decarbonisation.

References:

1 *https://www.un.org/development/desa/dpad/publication/world-economic-situation-and-prospects-february-2023-briefing-no-169/#:~:text=Average%20GDP%20growth%20is%20projected,weigh%20on%20investment%20and%20exports.*

2 *https://openknowledge.worldbank.org/bitstream/handle/10986/38030/GEP-January-2023.pdf?sequence=34&isAllowed=y page 25*

3 *https://openknowledge.worldbank.org/bitstream/handle/10986/38030/GEP-January-2023.pdf?sequence=34&isAllowed=y page 11*

4 *https://library.wmo.int/doc_num.php?explnum_id=11178*

5 *https://www.worldbank.org/en/news/press-release/2022/10/28/pakistan-flood-damages-and-economic-losses-over-usd-30-billion-and-reconstruction-needs-over-usd-16-billion-new-assessme*

6 *https://eparlib.nic.in/bitstream/123456789/994373/1/17_Finance_46.pdf*

7 *https://www.unep.org/resources/emissions-gap-report-2022*

8 *https://pib.gov.in/PressReleasePage.aspx?PRID=1768712*

◆◆◆

FOCUS

Navigating the Precarious Balancing Act: A Critical Analysis of the Union Budget

Bibek Debroy & Aditya Sinha*

Introduction

The Union Budget, which is an annual report on the government's revenue and expenditure, is often perceived as a platform for major policy announcements. However, it actually accounts for a decreasing share of public expenditure, with much more spending happening at the state level. As a result, State Budgets deserve more attention and scrutiny. The hype around the Union Budget stems from a bygone era when taxes changed frequently, and people were eager to know how prices would be affected. However, stability and predictability are essential for tax reform. While there may be a need to simplify the GST and reduce the number of tax rates, this is the responsibility of the GST Council, not the Union Budget.

The current budget is a stark contrast to N.D. Tiwari's "sindoor budget" of 1988-89 made headlines for its symbolic tax exemptions on items like sindoor and kajal. Instead, this budget is all about empowering women, youth and progress. The government is gearing up for the 'Amritkaal', charting a path towards a developed India by 2047. It's a budget focused on real change and investment in the future, leaving the quaint symbols of the past behind. This is a budget for a new India, ready to embrace its destiny and unleash its full potential.

The Finance Minister encountered a nuanced predicament in navigating the current economic terrain. Mindful of the importance of upholding macroeconomic stability, the budget strikes a delicate equilibrium between tackling inflationary constraints and promoting economic growth hindered by external factors. This conundrum entailed a precarious balancing act, which necessitated the Finance Minister to display unwavering composure.

The art of budgeting is a crucial component in fulfilling the commitment to proficient and impactful governance. Substantial deviations in the projection of revenue and expenses can impede the execution of government initiatives and policies, ultimately jeopardising social welfare results. Against this background, we highlight four areas where the budget has done exceptionally well.

Fiscal Discipline

Democratic political systems often face choices between present and future welfare. According to Nordhaus' influential work published in 1975 on the political business cycle, a democracy that evaluates political parties solely based on their past performance is likely to make decisions that are unfair to future generations. This is because politicians may prioritise short-term gains over long-term benefits in order to secure immediate political

**Bibek Debroy is the Chairman, Economic Advisory Council to the Prime Minister & Aditya Sinha is Additional Private Secretary (Policy & Research), Economic Advisory Council to the Prime Minister.*

success. Nordhaus (1975) further goes on to say, *"within an incumbent's term in office, there is a predictable pattern of policy, starting with relative austerity in early years and ending with the potlatch right before elections" (pp.187)*[1].

Hence, the political business cycle theories posit that incumbent political parties engage in opportunistic behaviour, manipulating economic instruments before elections to enhance their chances of being re-elected. In other words, Governments are known to employ a strategic approach by exploiting the short-term Phillips curve to further their objectives[2]. In addition, governments may also take advantage of the limited knowledge and simplistic expectations of voters in order to attain their goals. This reveals a complex interplay between political manipulation and the economic implications of short-term policies.

At the same time, the work of Rogoff (1990) and Rogoff and Sibert (1988) suggests that in situations where information about the competence of an incumbent is limited, expansionary policy measures implemented prior to an election are often viewed as an indicator of high competence[3&4]. As per their analysis, a potential outcome of the political business cycle could be an increase in the budget deficit, as well as an increase in the money supply via the monetisation of the deficit. In addition, there may also be an increase in inflation during the electoral period, as politicians prioritise short-term economic gains in order to increase their chances of re-election. In the case of India, too, some studies have found clear evidence of an increase in revenue deficit in the years leading to an election[5].

However, under the incumbent government in India, things have changed. What Narendra Modi's government is doing is completely opposite to the basic tenets of the political business cycle theories. The Prime Minister has proved Nordhaus and other PBC theorists wrong.

With the upcoming elections, many expected the government to unleash a spree of spending, showering voters with loan waivers and other financial goodies. But the Finance Minister and the government have taken a different approach, choosing to prioritise long-term stability over short-term gains. By resisting the temptation to indulge in vote-winning measures, the government has demonstrated a commitment to responsible financial management, even in the face of political pressure. This budget stands as a testament to the government's determination to put the country's future first.

The government has demonstrated exceptional fiscal discipline in recent years, consistently meeting or exceeding its deficit target. India's fiscal deficit shot up to a record 9.3% in 2020/21, from 4.6% the previous year due to pandemic-related spending. This year, despite formidable fiscal challenges owing to the ongoing Russia-Ukraine conflict and global economic uncertainties, the government deserves accolades for reinforcing its resolve to stick to the fiscal deficit target of 6.4%.

For the next year, the government has committed to bringing down the fiscal deficit to 5.9%. This reduction is in line with the government's earlier commitment towards the fiscal deficit target of 4.5% of GDP by the end of 2025/26. Obviously, this doesn't have to be linear. Even if the reduction is by 0.5% next, there may be more opportunities for substantial consolidation and growth as the global recession and headwinds would be behind us in the first year of the next government. Thus, there will be more room for fiscal consolidation in the next two years.

The endeavour to simultaneously achieve rapid economic growth and social welfare improvement while maintaining responsible fiscal management is a multifaceted challenge. Nevertheless, recent studies indicate that the fundamental means of accomplishing these goals is not merely through the reduction of fiscal deficits but rather by diminishing expenditures of inferior quality. This necessitates abstaining from the temptation to artificially generate capital account surpluses that come at the cost of enlarging gross fiscal deficits.

Capital Expenditure

In the midst of the Great Depression in 1933, economist John Maynard Keynes penned a passionate letter[6] to President Roosevelt urging him to take bold actions to jumpstart the economy. Keynes argued that the government should borrow money and use it to increase spending rather than raise taxes, as a way to boost national purchasing power and ignite growth. While it’s unclear if Roosevelt actually read the letter, he did ultimately turn to government spending to revitalise the economy through his New Deal.

A lot has already been written about the union government setting aside 10 lakh crore (~3.3% of the country’s GDP) for Capital Expenditure in this budget, a 37.4% increase from last year’s Revised Estimates. Economists talk about the multiplier effect. The multiplier effect is a concept that highlights the exponential impact of changes in government spending on a nation’s output. When the fiscal multiplier is greater than one, an increase in government spending leads to a corresponding increase in output that is greater than the original investment. In simpler terms, a single rupee increase in government spending could result in a return that is worth much more than one rupee.

The economic survey may have shed light on the resurgence of private investment, but with global challenges and monetary constraints, it alone may not be enough to drive growth. This is where the government steps in, with their unwavering commitment to revive the economy demonstrated by allocating a record-high 10 trillion for long-term capital expenditure in 2023-2024, surpassing the previous year’s budget of 7.5 trillion, thus providing a cushion from global headwinds. A 33% increase year-on-year shows that the government is putting their money where its mouth is and that growth is within reach. This, in turn, will also help in crowding in private investments.

But what is the extent of the fiscal multiplier in the case of capital expenditure in India? There is a dearth of studies on the subject. However, the most influential study out of these is that by Bose & Bhanumurthy, which first came out as a NIPFP Working Paper in 2013 and later got published in the Journal of Applied Economic Research[7]. According to their calculations, the multipliers for capital expenditures, transfer payments, and other revenue expenditures are 2.45, 0.98, and 0.99, respectively. However, the multipliers for taxes are approximately -1. Goyal & Sharma (2018) find that capital expenditure exhibits the greatest cumulative multiplier, with a size ranging from 2.4 to 6.5 times that of revenue expenditure.

Furthermore, capital expenditure has a more pronounced impact on long-term inflation reduction. Nonetheless, capital expenditure is susceptible to greater volatility due to its vulnerability to discretionary spending cuts[8]. However, the multipliers of public capital expenditure would not be as high as they used to be in 2013. The explanation for this phenomenon is straightforward. During the past nine years, the government has made significant expenditures on infrastructure development, including roads, railways and logistics. Infrastructure no longer poses as significant an obstacle for private capital influx as it did during the UPA era. Thus, the government is not just focusing on capital expenditure but also on addressing institutional weaknesses.

At the same time, the capital expenditure multipliers of the states are much higher the that of the union government's capital expenditure. Thus, it is crucial to encourage states to prioritise capital expenditure as a means to revitalise the economy, especially after the shocks[9].

Incentivising States for Capital Expenditure

In pursuit of fostering cooperative fiscal federalism, the Union Government has extended a program of financial assistance program for capital expenditure for the upcoming fiscal year of 2023-24. This initiative has received a significant boost in allocation, with an increased budget of 1.30 lakh crore, representing a 30% escalation from the previous year. In terms of the current fiscal year, this amounts to approximately 0.4% of the nation's GDP. The importance of empowering the states to undertake capital projects cannot be overstated, and this expanded allocation represents a progressive step forward.

The FM has decided to continue a 50-year interest-free loan to the state governments for one year. The states have been given autonomy to spend this at their discretion, with a catch - a portion of it is contingent upon increasing their actual capital expenditure. But what will they spend it on? The Union Government has tied parts of the outlay to either reforms or allocation to priority areas. This includes urban planning reforms, financing reforms in ULBs to make them creditworthy, the State share of capital expenditure of central schemes etc. Thus, there will be an inherent incentive for the state governments to also ensure the quality of public expenditure.

However, states should focus on the quality of the capital expenditure. There is a significant variation in capital expenditure by different states. Delving into the granular details, the states of Uttar Pradesh, Maharashtra, Madhya Pradesh, Karnataka, and Tamil Nadu collectively contribute over 40% towards the consolidated capital outlay carried out by all states. In a particularly fascinating trend, states such as Uttar Pradesh, Odisha, Assam and Jharkhand exhibit a relatively larger proportion of capital outlays in relation to the size of their respective economies.[10]

Similarly, the RBI's State Finances report has also pointed out that fiscal marksmanship relating to capital outlay also varies across the state. During 2017-18 to 2019-20, states & union territories like Andhra Pradesh, Delhi, Jammu & Kashmir, Goa, Tripura and Punjab have cut their budgeted capital expenditure by more than 40%.

Himachal Pradesh, Haryana, and Nagaland were the sole outliers in exceeding their budgeted targets for capital expenditure.

The RBI report has also flagged the issue of a residual approach to spending. Over the past five years, a substantial portion, amounting to one-fourth, of total expenditures occurred solely during the month of March. This presents a grave matter as the primary objective of spending by the year's end results in a compromise in the quality of expenditures. The Union budget can only nudge the states to improve their quality of public expenditure. But under a federal structure, states will have to do more if they want to ensure higher growth rates for a prolonged period.

Transparency

In the past two budgets, the government has taken bold steps to bring off-budget borrowings, like those of the Food Corporation of India (FCI) previously, in its own light. By doing so, they aim to offer a clear picture of the government's financial obligations, enabling informed decisions and assessments. Previous finance ministers acknowledged the issue with off-budget borrowings and made hollow announcements which were never fructified. P. Chidambaram, in his budget speech (2008-09), stated - "I acknowledge that significant liabilities of the government on account of oil, food and fertilizer bonds are currently below the line. This accounting arrangement is consistent with past practice. Nevertheless, our fiscal and revenue deficits are understated to that extent. There is a need to bring these liabilities into our fiscal accounting." However, it was Nirmala Sitharaman who made it a reality. The finance minister has continued with this tradition again this year.

Social Sector

Some have argued that the union government's outlay on the social sector, as a percentage of its overall expenditure, has displayed a persistent stasis. In FY 2009-10, the government allocated 21% of its total expenditure towards social sector expenditures, which subsequently saw a slight decrease to 20% by FY 2019-20. Over the past fourteen years, the average proportion of social sector spending by the government, amounting to nearly one-third (30%), was dedicated to the provision of subsidised food to the country's poorest two-thirds. However, the percentage of such spending exceeded 50% in FY 2020-21 amidst the global health crisis caused by the COVID-19 pandemic.

While the percentage of overall expenditure on the social sector would have remained same in the last few years, there is an incremental improvement on quality of expenditure in the social sector. Notably, today, intended beneficiaries get 100% of funds which they are supposed to get. During a visit to the drought-stricken Kalahandi district in Odisha in 1985, Rajiv Gandhi made a statement indicating that only 15 paise out of every rupee spent by the government actually reached the intended recipient. One should quote Justice A. K. Sikri's majority opinion on the constitutionality of the Aadhar Act: *"Resultantly, lots of ghosts and duplicate beneficiaries are able to take undue and impermissible benefits… It cannot be doubted that with UID/Aadhaar much of the malaise in this field can be taken care of."*[11]

The digital public infrastructure has not only enhanced accessibility of public services to the most disadvantaged and susceptible sections of the nation, but it has also facilitated the detection and elimination of fraudulent beneficiaries from various government schemes. The system has effectively curbed leaks caused by non-existent and duplicate beneficiaries who use fake identities to obtain benefits. While one should acknowledge that there are some exclusion errors, but the government is ensuring that there are enough safeguards against exclusion in the cases of authentication failure. The digital public infrastructure and Aadhaar based biometric authentication (ABBA) also makes it easier to ensure portability of benefits.

More importantly, use of Aadhaar to identify and authenticate beneficiaries in government scheme has led to considerable fiscal savings. Thus, even if the social sector spending has remained stagnant, the use of DPI and ABBA, has ensured that more people, especially the one who are marginalised and vulnerable are able to get intended benefits.

Moreover, criticism has been raised regarding the allocation of funds for the Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA) scheme in the 2023-24 budget. The budget for MGNREGA in 2023 is 18% lower than the budget estimates of Rs. 73,000 crore for the current year of 2022-23, and approximately 33% lower than the revised estimates of Rs. 89,000 crore for the current year.

MGNREGA operates on a demand-driven model where households seeking employment are entitled to a minimum of 100 days of unskilled manual labor during a given financial year. In the ongoing fiscal year of 2022-23, nearly all rural households, or 99.81%, have been offered wage employment according to their demand. If a job seeker does not receive employment within 15 days of application, they are eligible for a daily unemployment allowance as per the provisions of the Scheme.

As there is reduced demand of MGNREGA, the number of person days generated by MGNREGA has also been going down. While the person days generated under MGNREGA was 389.09 crore in FY20-21 due to the migration to rural areas owing to pandemic, it has been going down subsequently.

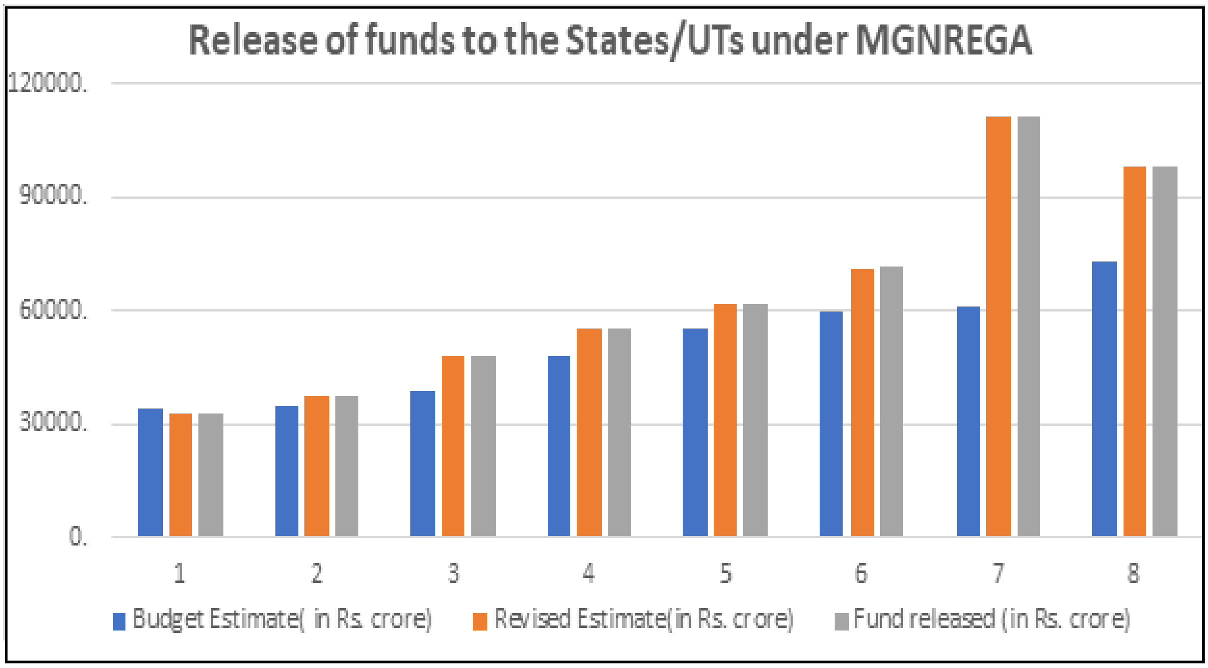
It should also be highlighted that the budget estimates are revised once there is more demand for work under MGNREGA. Over the past seven years, actual funds released to states under MGNREGA have consistently exceeded budget estimates. For example, in the fiscal year 2019-20, the budget estimate for MGNREGA was Rs.60,000 crore, but due to increased demand, it

	FY2022-2023	FY 2021-22	FY2020-21	FY 2019-20
Person days generated (in crores)	248.08	363.33	389.09	265.35

Source: Ministry of Rural Development[12] was revised to Rs.71,001 crore. Similarly, the COVID-19 pandemic and the sudden influx of population into rural areas led to a revised estimate of Rs.1,11,500 crore in 2020-21, compared to the original budget estimate of Rs.61,500 crore. In the fiscal year 2021-22, the budget estimate of Rs.73,000 crore was revised to Rs.98,000 crore. These figures demonstrate that the government is willing to allocate additional funds to MGNREGA in response to demand.

Conclusion

The Union Budget is no longer the sole platform for major policy announcements, as much more spending happens at the state level. The hype surrounding the budget is a remnant of a bygone era, and stability and predictability are essential for tax reform. The current budget is focused on empowering women, youth, and progress, leaving symbolic tax exemptions of the past behind. The Finance Minister has done an exceptional job of balancing tackling inflationary constraints and promoting economic growth. The government's commitment to responsible financial management is commendable, even in the face of political pressure, and this budget stands as a testament to putting the country's future first. The government has demonstrated exceptional fiscal discipline in recent years and deserves accolades for reinforcing its resolve to stick to the fiscal deficit target of 6.4%. The endeavour to simultaneously achieve rapid economic growth and social welfare improvement while maintaining responsible fiscal management is a long-term goal that requires prudent budgeting, and this budget is a step in the right direction.



Source: Ministry of Rural Development

References:

1 *Nordhaus, W. D. (1975). The Political Business Cycle. The Review of Economic Studies, 42(2), 169-190.*

2 *Dubois, E. (2016). Political Business Cycles 40 Years after Nordhaus. Public Choice, 166(1-2), 235-259.*

3 *Rogoff, K. (1990). Equilibrium Political Budget Cycles. The American Economic Review, 80(1), 21-36.*

4 *Rogoff, K., & Sibert, A. (1988). Elections and Macroeconomic Policy Cycles. The Review of Economic Studies,, 55(1), 1-16.*

5 *Sen, K., & Vaidya, R. R. (1996). Political Budget Cycles in India. Economic and Political Weekly, 31(30), 2023-2027.*

6 *Keynes, J. M. (1933). An Open Letter to President Roosevelt. Retrieved from University of Texas: https://bit.ly/3ScJVa2*

7 *Bose, S., & Bhanumurthy, N. R. (2015). Fiscal Multipliers for India. The Journal of Applied Economic Research, 9(4), 379–401.*

8 *Goyal, A., & Sharma, B. (2018). Government Expenditure in India: Composition and Multipliers. Journal of Quantitative Economics volume, 16, 47-85.*

9 *Swaroop, E. (2022). Estimation of Expenditure Multiplier for India. Retrieved from IES: https://bit.ly/3YSly44*

10 *RBI. (2023). State Finances: A Study of Budgets of 2022-23. Mumbai: Reserve Bank of India.*

11 *Justice K S Puttaswamy (Retd.) and Another versus Union of India and others, 494 of 2012 (Supreme Court of India September 26, 2018). https://bit.ly/3XNTsph*

12 *Ministry of Rural Development. (2023, February 3). Clarifications of Union Rural Development Ministry on budget cut to MGNREGA. Retrieved from Press Information Bureau: https://bit.ly/3SdCmzP*

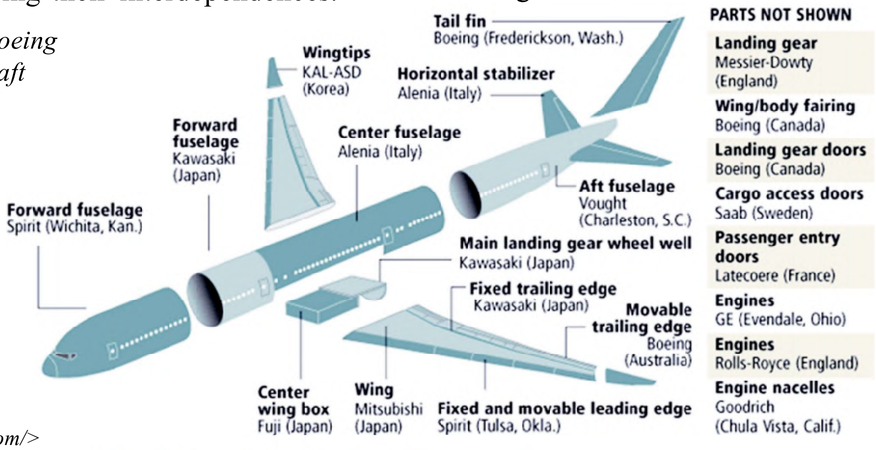
◆◆◆

Foreign Direct Investment, Trade and the Union Budget: Understanding the Issues

Manoj Pant and Sugandha Huria*

The global economy has been experiencing severe economic downturns since 2008. Much before the sub-prime crisis triggered the collapse of global trade, the world economy started experiencing recessionary trends. The European debt crises, the US-China war, the Covid-19 pandemic, and the Russian-Ukraine war, among others, have significantly influenced the world economic outlook in the last decade. Amid such a crises prone period, even though the growth of trade has also been sluggish, the world trading platform has experienced a structural transformation creating several new opportunities for emerging and developing market economies. More than ever, international trade and commerce are now considered as critical weapons to ensure world peace and harmony, as these escalate the cost of future conflicts. This ideology *though* is not new. Mill (1848) also emphasised how international trade renders inter-country wars obsolete by enhancing their interdependences. However, today, the definition of trade has changed drastically. Unlike the traditional concept where production processes used to happen domestically and countries were engaged in the export and import of only final goods and services, in today's world, there is no product which is made in a single country. The new trade reality is now demonstrated by the so-called Global Value Chains [or, GVCs], which are guided by fragmented production structures spread across different countries in the world. For example, as explained in a recent study by Xing and Huang (2021), a smartphone finally assembled in China contains components from several countries, such as visual design and power management module from the USA, computer codes from France, printed circuit board from Taiwan, silicon chips from Singapore, memory chips from Korea, and precious metals from Bolivia.[1] Another example is that of a Boeing 787 Dreamliner (originally an American product), the fragmented value chain of which, is shown in Figure 1 below.

Figure 1: *GVC of a Boeing 787 Dreamliner Aircraft*



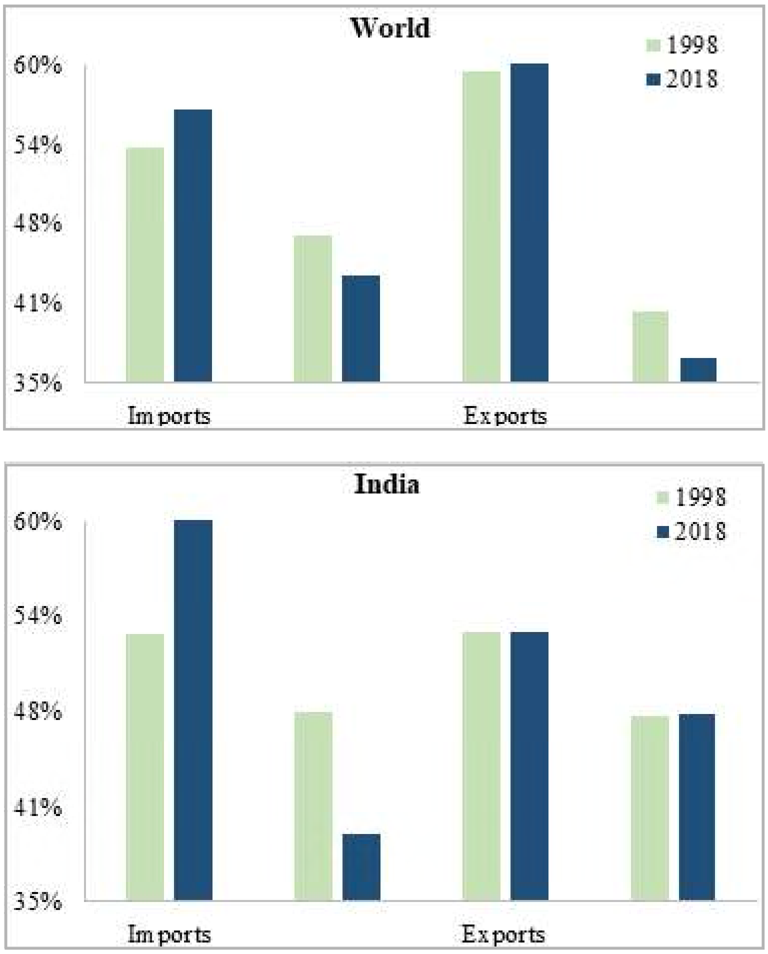
Source: Adapted from <https://modernairliners.com/>

Source: Adapted from <https://modernairliners.com/>

**Prof. Manoj Pant is former Director/VC of IIFT and Sugandha Huria is a faculty member, IIFT.*

Thus, Figure 1 clearly demonstrates how in the new world of highly complex international production chains, goods cross several borders multiple times before reaching their end customers. To put it another way, this suggests that what we see happening in the world today isn't really trade in final goods or services, but rather trade in intermediate inputs, materials, components, activities, or tasks. Rapid technological development, a steady decline in tariffs, lower costs for shipping and logistics, organisational innovations, etc. are just a few of the factors that remarkably decreased the cost of coordination between nations and enabled this process of global production sharing. The upper panel of Figure 2, based on OECD'S TIVA database, shows how, in the past few decades, this type of trade has dominated global exports and imports, and today, contributes to more than 60 per cent of the world trade.

Figure 2: Gross Trade in (Final and Intermediate) Goods and Services, 1998 - 2018



Source: OECD TIVA (2021 Ed.); Authors' Calculations.

In addition, it is crucial to understand that the network of trade is expanding not between countries or industries but rather between businesses/firms, the majority of which are overseas affiliates or subsidiaries of various multinational corporations (i.e., the carriers of *Foreign Direct Investment*).[2] This is what is referred to as *intra-firm* trade in the literature, which is distinct from international trade carried out between *unrelated* parties. In a recent interaction with Financial Express, Pant and Bimal (2020) noted that

"Estimates suggest that about a third of global trade occurs in the form of intra-firm trade among MNEs;[3] the remaining two-thirds occur either as exports by MNEs to non-affiliates or trade among non-MNE national firms."

In fact, the value of these intra-firm trade flows has increased as a result of MNCs' expanding operations and rapidly emerging GVCs in the past decade or so. Based on the OECD's database on Activities of Multinational Enterprises [AMNE], it has been estimated that these companies contribute to approximately 36 per cent of the global output, which accounts for about two-thirds of the world exports and more than 50 per cent of world imports. The UNCTAD [United Nations Conference on Trade and Development] estimates also suggest that around 80 per cent of global trade takes place under the purview of MNCs. However, this type of trade occurs only when MNs make investments abroad, referred to as Foreign Direct Investment [or, FDI]. Thus, in today's GVC-driven era, FDI is serving as a conduit for the growth of trade flows. The main argument is that, in the present-day world, it is impossible to examine trade policy in isolation or to disentangle it from FDI policies.

To discuss the linkages between international trade and FDI, let us first understand the *definition of Foreign Direct Investment, and how it differs from Foreign Portfolio Investments (FPI) or what we call Foreign Institutional Investors (FII) in India*.

Until about the early 1960s, FDI, like other forms of international investment used to be considered as a part of international capital theory. It was actually seen as a response to interest rate differentials between countries around the globe. Thus, it was recognised that, similar to trade in goods, a capital-scarce country (the one which offers higher return) imports capital and this continues up to the point where the return to capital gets equalised internationally. This explanation is analogous to the predictions of the standard Heckscher-Ohlin (H-O) theory of trade.[4] Hence, it was thought that trade in goods could substitute for the international movement of factors of production, including FDI. But, with the failure of this capital theory in explaining most of the rise in *international production* (in contrast to just capital movement) during the late 1950s, efforts were made to analyse them from the trade theorist's point of view. Only then, it was realised that trade and FDI are actually two different sides of the same coin (Pant and Srivastava 2015) and hence, they cannot be studied or analysed in isolation.

It was John Dunning who, in his 1980 seminal work, defined foreign direct investment based on what is popularly referred to as the 'OLI' paradigm, where O stands for Ownership, L for Location, and I stands for Internalisation. According to him, these three are potential sources of advantage that underlie a firm's decision to become a multinational corporation. The first component 'O' addresses the question that why some firms go abroad, and suggests that a successful MNC has some *firm-specific advantages*, which allow it to overcome the costs of operating in a foreign country. Location advantages, on the other hand, deal with the question of where an MNC chooses to locate and suggest why it sometimes becomes profitable for a firm to locate itself in different countries, rather than producing and exporting from its parent country. Lastly, internalisation advantages influence how a firm chooses to operate in a foreign country, trading off the savings in transactions, hold-up and monitoring costs of a wholly-owned subsidiary, against the advantages of other entry modes such as exports, licensing, or joint venture. This implies that Foreign Direct Investment, as distinct from FPI or FII, does not just include the transfer of foreign capital from an enterprise in the source to another *related* entity in the host country, but also the transfer of know-how in the form of advanced technology, managerial expertise, or any other firm-specific factor.[5] Put differently, FDI combines three elements, viz. trade in commodities, services (for example, managerial services) and international technology flows. Secondly, most direct tax treaties between nations provide favourable treatment in the withholding tax rates applied on dividends/ royalty payments among related enterprises, acknowledging the relationship between FDI flows and the production capacities of firms (Pant 2014).

In fact, as explained in Pant and Srivastava (2015), an investor in the parent country decides to switch to domestic production in the other country (i.e., it opts for FDI), when either entry barriers like tariffs make its exports uncompetitive, the other location gives it access to critical inputs at comparatively lower costs (vis-à-vis, the parent country), or when such a move becomes necessary to internalise the firm-specific advantages. With the establishment of the World Trade Organisation [WTO], the world has already experienced a gradual decline in tariff rates imposed by different countries. Hence, as argued in Huria and Pant (*op. cit.*), it is the latter reason that presently explains the expansion in the flows of FDI. This is because even if trade is free but FDI flows are restricted, it will be difficult for an economy to deepen its integration with the world market via GVCs. For one, restrictions on FDI inhibit the flow of technology and hence, the country's technology-based trade. Secondly, no or lower levels of integration with global value chains (due to restrictions on intra-firm trade) may limit trade in intermediate inputs, which, in turn, could render a nation less competitive in the manufacture of a good (or goods) in which it had previously enjoyed a comparative advantage. Nevertheless, it is equally important to recognise that this association between FDI and trade could be complex and vary across countries, industries, production stages, and types of investment, etc. For example, while liberalised trade and FDI policies may foster a favourable correlation between the two, higher regulatory interventions in an industry in the form of tariff or non-tariff barriers, tax-based subsidies, etc. could potentially offer substantial incentives to the MNC to replace trade with FDI.

Tables 1 and 2 encapsulate Pearson's pairwise correlation coefficients (measuring the strength and direction of the linear relationship) between different FDI and trade indicators (at the aggregate and sectoral level) for the world economy.

Table 1: Pearson's Pairwise Correlation Coefficients – Trade and FDI, World (1970-2021)

Percentage Shares in GDP	Total Exports	Total Imports	Total Trade
Net FDI Inflows	0.714*	0.731*	0.821*
Net FDI Outflows	0.654*	0.676*	0.780*
Total FDI Flows	0.701*	0.719*	0.817*

*Source: World Bank's World Development Indicators (WDI) Database; Authors' calculations. Note: * represents significance at 1 per cent level, Total trade represents the total of goods and services trade, Green highlights represent the top three correlations. Interestingly, all the correlations are above 50 per cent, and the majority of the correlations are above 70 per cent (i.e., closer to perfect correlation).*

Table 2: Pearson's Pairwise Correlation Coefficients – Goods, Services Trade and FDI, World (1970-2021)

Percentage Shares in GDP	Goods Exports	Goods Imports	Goods Trade	Services Exports	Services Imports	Services Trade
Net FDI Inflows	0.717*	0.745*	0.721*	0.729*	0.662*	0.704*
Net FDI Outflows	0.665*	0.699*	0.669*	0.660*	0.581*	0.635*
Total FDI Flows	0.707*	0.736*	0.711*	0.711*	0.638*	0.686*

*Source: WDI; Authors' calculations. Note: * represents significance at 1 per cent level, Green highlights represent the top three correlations.*

At the aggregate level for the world economy, Table 1 shows that trade and FDI are significantly and positively correlated with each other – be it the association between inward FDI and exports/imports, or the outward FDI or total FDI with exports/imports. Further, Table 2 replicates the analysis by incorporating information separately, on goods and services trade. Once again, we find that there exists a direct positive association between the two, indicating their complementarity.

Though our analysis is indicative, it clearly makes a strong case for examining trade and FDI policies in a comprehensive and coherent framework.[6]

But, *is this link well established in India's trade and FDI-related policies*? – Below we discuss some of the evidence in this regard, and suggest a possible way forward.

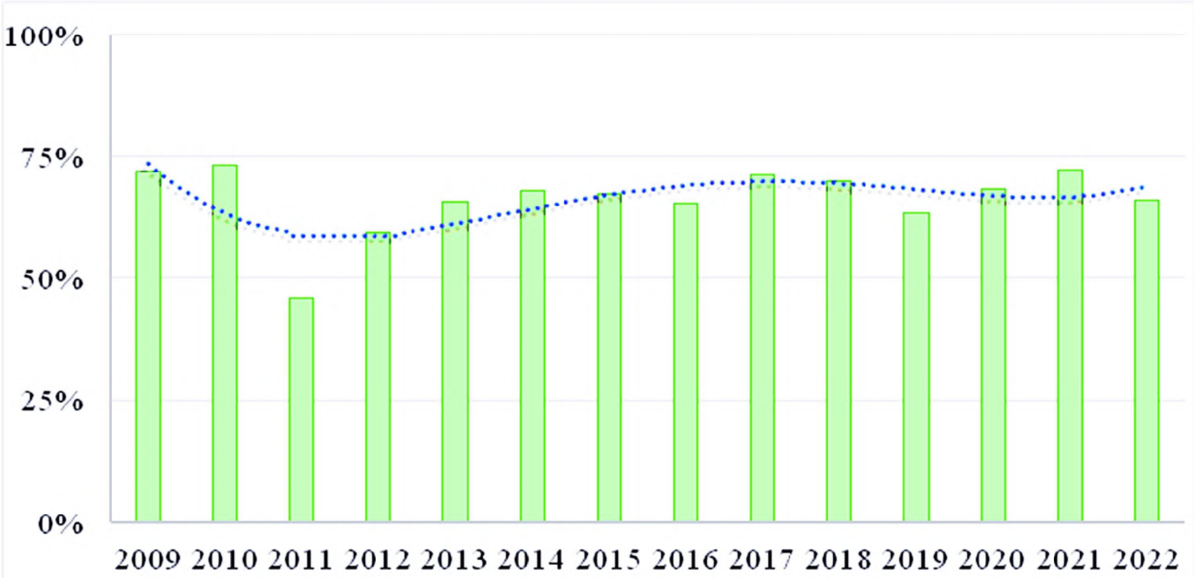
The Case of India

The lower panel of Figure 2 and Tables A.1, A.2 in the appendix to this article, show that India's trade composition and the trade-FDI link are in line with our observations for the global economy. In fact, the correlation coefficients, on average, are higher in the case of India, than in the world, indicating the strength of the positive association between international trade and foreign direct investment. The last decade has witnessed several initiatives on the part of the country's government to improve the ease of doing business, and make the country one of the most attractive FDI destinations in the world. In 2011, the Department for Promotion of Industry and Internal Trade (*erstwhile* Department of Industrial Policy and Promotion [DIPP]) introduced the National Manufacturing Policy [NMP] to increase the share of the manufacturing sector in India's GDP. National Investment and Manufacturing Zones have been established as an instrument to implement NMP, with an overall objective to facilitate the access to a requisite ecosystem for promoting world-class manufacturing activity (Press Information Bureau [PIB] 2018).

In September 2014, the government launched the Make In India [MII] programme with an endeavour to create and encourage domestic and multinational firms to develop, design, manufacture, and assemble products in India (PIB 2022b). As an initiative to simplify the process of approvals of inward FDI flows under government approval, the Union Cabinet abolished the Foreign Investment Promotion Board [FIPB] in May 2017. Henceforth, all the FDI proposals are required to be submitted through the DPIIT-managed Foreign Investment Facilitation [FIF] Portal, and respective applications are then screened by the concerned administrative ministries/department (PIB 2022a). Further, the government has also opened up several sectors for which FDI up to 100 per cent is permitted through the automatic route. A few examples are – ports and shipping, railway infrastructure, renewable energy, agriculture and animal husbandry, automobiles and auto components, single-brand product retail trading, and insurance intermediaries, among others.

While several other policy initiatives have also been undertaken to position India as the most attractive location for investment and conducting businesses (such as the Production Linked Incentive Schemes, PM Gati Shakti, India Industrial Landbank, the National Logistics Policy, Remission of Duties and Taxes on Exported Products, and the National Single Window System), however, at the same time, the country's trade policy has been found to be highly restrictive in nature in the past one decade. Figure 3, based on the Global Trade Alert Database, shows the share of harmful trade interventions defined as those that restrict trade practices, as a percentage of total trade interventions for India for the period 2009-2022.

Figure 3: Harmful Interventions (% of total trade interventions), India (2009-2022)



Source: Global Trade Alert Database; Authors' Calculations.

Except for the year 2011, as shown in Figure 3, the number of harmful trade interventions has always exceeded the number of liberalised trade interventions by the country. In fact, very recently, India was also flagged as highly restrictive in its trade practices by the industry associations of the United States of America, who pointed out that "although Prime Minister Narendra Modi has taken steps aimed at improving India's business environment, India's high tariff rates and restrictive border measures continue to limit manufacturers' ability to invest in and export to India."[7] This is a concern in itself as trade and FDI go hand in hand, and the rapidly expanding international production networks have only strengthened their association in the recent past.

The recent Budget announcements, however, seem to take a positive step in this direction. While the country's long-due Foreign Trade Policy is still in the making, in this year's Union Budget 2023-24, the country's finance minister has reduced custom duties on a selected set of intermediate inputs to enhance domestic value addition, promote export competitiveness, and correct duty inversion. This is in contrast to the Union Budget 2021-22, where duties on imports of inputs were raised to ensure higher value addition within the country (even though the majority of India's imports are of the intermediate category (see Figure 2, Lower panel)). Examples include some components used in TV manufacturing, electric heat coils, capital equipment for electrically operated vehicles and lithium battery production, parts of mobile phones, denatured ethyl alcohol for manufacturing of industrial chemicals, lab-grown diamonds, etc. Certain tariffs have been raised though for competing imports that may impact the local industry, such as rubber, toys and parts of toys.[8]

Other initiatives include skill training programmes, the development of data processing centres, etc.

Despite these initiatives, one issue that still remains pertains to the bureaucratic separation of trade and FDI in India. While the definitional aspects of FDI are looked after by the country's Ministry of Finance, the policies and control of FDI is with DPIIT. On the contrary, India's international trade and trade-related policy matters are governed by the relevant trade policy division in the commerce ministry. More so, no chapter in its Foreign Trade Policy (FTP 2015-2020) thus far deals with investment-related provisions/norms (except for the section on Special Economic Zones/ Export Oriented Units). This demands immediate attention especially when today, trade is determined more by technology and FDI, than by access to cheaper and abundant factors of production, and the emerging dynamics make it imperative for India to become a part of international production networks. The latter, as discussed above, are guided by MNCs to a great extent. The recent restructuring in the department of commerce may take this into account and create a separate wing to deal with trade and FDI policies simultaneously. Similarly, the government should consider the trade-FDI interlinkages while drafting India's new FTP.

Lastly, akin to India's policy framework, even at the multilateral level, there is no such comprehensive agreement that guides the trade in goods-services-investment nexus. However, acknowledging the link between the three, it seems that countries around the world are trying to bridge this gap by signing more and more regional trade agreements – now that these agreements also contain a specific chapter on investment-related provisions.[9] On the contrary, in India, the majority of the trade agreements still focus only on trade liberalisation, and exclude substantive provisions for foreign direct investment. Our recent work shows that this will not create significant gains for India, especially when it is now willing to conclude such deals with countries which are amongst its top FDI source economies.

Appendix

Table A.1: Pearson's Pairwise Correlation Coefficients – Trade and FDI, India (1970-2021)

Percentage Shares in GDP	Total Exports	Total Imports	Total Trade
Net FDI Inflows	0.898*	0.883*	0.892*
Net FDI Outflows	0.721*	0.733*	0.745*
Total FDI Flows	0.876*	0.867*	0.876*

*Source: WDI; Authors' calculations. Note: * represents significance at 1 per cent level, Green shaded cells represent correlation above 0.8.*

Table A.2: Pearson's Pairwise Correlation Coefficients – Goods, Services Trade and FDI, India (1970-2021)

Percentage Shares in GDP	Goods Exports	Goods Imports	Goods Trade	Services Exports	Services Imports	Services Trade
Net FDI Inflows	0.863*	0.867*	0.871*	0.916*	0.800*	0.903*
Net FDI Outflows	0.686*	0.705*	0.703*	0.741*	0.711*	0.755*
Total FDI Flows	0.840*	0.849*	0.851*	0.895*	0.799*	0.888*

*Source: WDI; Authors' calculations. Note: * represents significance at 1 per cent level, Pink highlights represent the top three correlations while green and pink shaded cells together represent correlation above 0.8.*

References:

1 *The Organisation for Economic Co-operation and Development [OECD] has also demonstrated several such cases with the help of it Trade In Value Added [TIVA] Database.*

2 *Gereffi and Lee (2012)*

3 *Multinational Enterprises (MNEs) and Multinational Companies (MNCs) are used synonymously in the trade-FDI literature.*

4 *In a 2-country, 2-sector, 2-factor world, Hecksher-Ohlin Theorem states that a country should export the good which utilises its abundant factor of production intensively, and import the commodity which is intensive in the use of its scarce factor of production. For example, if the world market comprises of only India and the United States of America, with India having comparatively higher access to labour relative to that of Capital, while the US is relatively richly endowed with capital, then as per the H-O theory, India should export the labour-intensive good (say, textiles) to the USA. On the contrary, the USA should export machinery (i.e., the capital-intensive good) to India (See any textbook on trade theory such as Krugman, Obstfeld, and Melitz (2017) or Batra (1973) for details).*

5 *Huria and Pant (2018)*

6 *The literature now consists of a plethora of empirical studies examining the link between trade and FDI at various levels of analyses. For a detailed review, refer to Pant and Srivastava (*op. cit.*).*

7 *Mishra (2022)*

8 *Government of India [GOI] Budget Speech (2021, 2023)*

9 *Huria and Pant (op. cit.)*

References:

- *Batra, R. N. (1973).* Studies in the pure theory of international trade. *Springer.*
- *Dunning, J. H. (1980). Toward an eclectic theory of international production: Some empirical tests.* Journal of international business studies, 11*(1), 9-31.*
- *Gereffi, G., & Lee, J. (2012). Why the world suddenly cares about global supply chains.* Journal of supply chain management, 48*(3), 24-32.*
- *GOI. (2021).* Union Budget 2021-2022: Speech of Nirmala Sitharaman. *New Delhi: Government of India. Retrieved from <https://www.indiabudget.gov.in/doc/bspeech/bs202122.pdf>*
- *GOI. (2023).* Union Budget 2023-2024: Speech of Nirmala Sitharaman. *New Delhi: Government of India. Retrieved from <https://www.indiabudget.gov.in/>*
- *Huria, S., & Pant, M. (2018). Foreign direct investment, welfare and wage inequality in a small open economy: theory and empirics.* Indian Economic Review, 53*, 131-166.*
- *Huria, S., & Pant, M. (2019). Trade, Investment, and the Multilateral Trading System. In* 20 Years of G20 *(pp. 93-111). Springer, Singapore.*
- *Krugman, P., Obstfeld, M., & Melitz, M. (2017).* International Economics: Theory and Policy. *Pearson Education.*
- *Mill, J. S. (1848). Principles of political economy with some of their applications to social philosophy. 1857.* George Routledge and Sons, Manchester*, 467-474.*
- *Mishra, A.R. (2022, November 27). US industry associations red-flag India's 'restrictive' trade barriers.* Business Standard. *Retrieved from <https://www.business-standard.com/article/economy-policy/us-industry-associations-raise-concern-over-india-s-trade-measures-122112700668_1.html>*
- *Pant, M. (2014, June 16). FDI or trade: end the confusion.* The Mint. *Retrieved from <https://www.livemint.com/Opinion/d35M6kulhSuMF4H5Bamc3N/FDI-or-trade-end-the-confusion.html>*
- *Pant, M., & Bimal, S. (2020, May 28). Combating economic downturn post Covid-19 pandemic: Sync trade and FDI policies.* Financial Express. *Retrieved from <https://www.financialexpress.com/opinion/combating-economic-downturn-post-covid-19-pandemic-sync-trade-and-fdi-policies/1972883/>*
- *Pant, M., & Srivastava, D. (2015).* FDI in India: history, policy and the Asian perspective*, New Delhi: Orient BlackSwan.*
- *Press Information Bureau (2018, December 27). Establishment of NIMZs. Retrieved from <https://pib.gov.in/PressReleaseIframePage.aspx?PRID=1557424>*
- *Press Information Bureau (2022a, May 24). Foreign Investment Facilitation Portal (FIF) completes 5 years since Union Cabinet decision to abolish FIPB. Retrieved from <https://pib.gov.in/PressReleasePage.aspx?PRID=1827889>*
- *Press Information Bureau (2022b, December 16). Make in India facilitates investment, fosters innovation, helps build best in class infrastructure. Retrieved from <https://pib.gov.in/PressReleaseIframe Page.aspx?PRID=1884260#:~:text='Make%20in%20India'%20is%20an,manufacturing%2C%20 design%2C%20and%20innovation.>*
- *Xing, Y., & Huang, S. (2021). Value captured by China in the smartphone GVC–A tale of three smartphone handsets.* Structural Change and Economic Dynamics, 58*, 256-266.*
- *[Data] Global Trade Alert Database: https://www.globaltradealert.org/*
- *[Data] OECD Activities of Multinational Enterprises Database: https://www.oecd.org/sti/ind/amne.htm*
- *[Data] OECD Trade In Value Added Database: https://www.oecd.org/sti/ind/measuring-trade-in-value-added.htm*
- *[Data] World Bank's World Development Indicators Database: https://databank.worldbank.org/source/world-development-indicators*
- *[Website] Organisation for Economic Co-operation and Development <https://www.oecd.org/>*

◆◆◆

FOCUS

Union Budget 2023 – 24: A View from the Private Sector

Vikas Khitha*

The FY 24 Union Budget, formulated amidst global headwinds and a bleak economic outlook in much of the developed world also had the conflicting domestic demands of growth and fiscal consolidation as challenges. With India ranking amongst the top 5 global economies, the Union Budget was awaited with bated breath not only by India, but by several friendly nations. The Hon'ble Finance Minister did not disappoint, with the vast majority of Indians at home and abroad, cheering a path breaking set of announcements!

While the economic growth in FY 23 is estimated to be at 7%, FY 24 growth is expected to range between 6 and 6.8%, in stark contrast to other large economies. This while continuing the downward trend of fiscal deficit from 6.4% of GDP in FY 23 to a targeted 5.9% in FY 24, and a target of 4.5% fiscal deficit by FY 25 – a challenging ask by any yardstick.

The FY24 Budget aims to propel economic growth via a record capital outlay of Rs 10 lakh crore, and rekindle animal spirits in the private sector, with the thrust areas being infrastructure development and green energy while keeping an eye on food security for the world's largest population, and indirectly providing an impetus to manufacturing activity associated with these sectors.

Construction and Manufacturing being the largest employment generators, this budget lays the foundation for a developed and modern economy, catalyse job creation and aid demand generation, especially in rural and semi-urban clusters. The increased demand for skilled labour, would bring into sharp focus the various skilling initiatives kick-started in previous years and supported by the corporate sector.

India's manufacturing sector of which MSMEs are the back-bone, has often been characterised by low returns on investment due to the high cost of logistics, high energy costs, low productivity, high working capital requirements coupled by meagre credit facilities, multiple labour laws, under- utilisation of capacity, and the absence of entire industrial eco-systems such as semi-conductor manufacturing, the last aspect resulting in supply chain vulnerability in testing times.

The Government's relentless push to lower the cost of logistics and connect Tier 2 towns via construction of expressways, freight corridors, the Gati Shakti programme and the National Logistics Policy carries its unmistakable stamp on the FY 24 budget too, via a capex outlay of Rs 75,000 crore towards 100 critical projects including airports and Rs 2.4 lakh crores for Railways.

The PLI scheme launched two years ago including in areas such as mobile manufacturing, along with the very large scale of digital financial transactions via UPI, resulted in a large demand being created for smartphones, which are now manufactured in the country. An eco-system of

*Vikas Khitha is the Vice President & Head of L&T Defence at Corporate Office in Delhi

semi-conductor manufacturing thus received due impetus, with large investments already committed.

Ease of Doing Business also received due focus, with a reduction in the number of compliances and de-criminalisation of several offences, and the PAN card being notified as the single identifier for businesses in FY24 budget. This should be of relief to firms with input tax credits in one state being able to offset tax dues in another state, as private sector working capital is presently blocked on this count. Green initiatives in the Power sector received a capex outlay of Rs 19,700 crore towards the Green Hydrogen Mission, with an additional Rs 35,000 crore being earmarked for transition to green energy and a further Rs 20,700 crore to connect renewable energy from Ladakh via a 13 GW transmission line. In addition to a significant reduction in carbon footprint with a target of net zero by 2070, large scale generation of renewable energy would help in lowering the cost of industrial power as well, to aid competitiveness in manufacturing.

The private sector has been making significant investments in defence manufacturing facilities and in R&D over the last few years. The sector received a further thrust over the last two years with the notification of four positive lists for indigenisation to substitute imports. While defence exports did make their presence felt in recent times with a stellar performance, the Hon'ble Prime Minister's target to the sector of USD 5 billion in defence exports by 2025 at the recently concluded Aero India event, has far reaching implications for growth and transformation of the defence sector.

The budget features a capex outlay of Rs 1,62,600 crore for defence manufacturing in FY24—a 7% increase over the previous fiscal. Although a higher increase in the Defence capex would have been desirable, for now much shorter evaluation and ordering cycles and superlative execution are clearly the need of the hour, in light of both domestic imperatives and the exports target. The private sector defence industry which is now beginning to take the lead in order generation and execution, does require certain measures by way of enabling policies; hopefully they will be heard once again.

The Space sector has also been churning out a spectacular performance and has received a budgetary allocation of Rs 12, 543.91 crore, for FY 24, up 19% from the previous fiscal, including a capital outlay of Rs 6356.8 crore for space research for the forthcoming year, bringing cheer to the Space start-up and research eco-system.

The Space economy will be a game changer in times to come for the nation, by way of enhanced connectivity via 5G with the remote regions, ushering in a wave of education, financial inclusion, tele-medicine, tourism opportunities as more locations are discovered by both domestic and foreign tourists, growth and development – all key enablers to Ek Bharat Shrestha Bharat!

An examination of how key parameters in the attached table published by CII (with data sourced from CSO, RBI, Ministry of Commerce & Industry and CGA) have moved since 2018, will reveal the rationale behind many of the recent initiatives undertaken by the present Government. While per capita income has been steadily rising, inflation held in check, a rising trend in current account balance as a percentage of GDP underscores the urgent need to further enhance manufacturing activity and exports from India, as opposed to outright imports.

In order to increase exports especially in high tech areas, cost competitiveness and quality would be of paramount importance. Since a large part of the cost of the product is built into the design itself, once again, Indian industry's famed frugal engineering skills—amply demonstrated by the Auto, Defence and Space sectors, would once again come into play! Adoption of industry 4.0 practices in manufacturing has already met with success at several plants in the country and the numbers are only expected to grow.

With execution being key, the Budget indirectly also places the onus onto laggard States to get their act together in dramatically improving on ease of doing business parameters and in creating a business-friendly environment in order to attract serious investors. With several steps now in place for a transition from a developing country to an emerging super-power, it's all hands-on deck!

Table: Key Parameters of the Economy

Sno	Category	Unit	2018-19	2019-20	2020-21	2021-22	2022-23
1	**Population**	Million	1327	1341	1355	1369	1383 (AE)
2	**GDP & related indicators**						
2.1	GDP (2011-12 prices)	Rs Lakh Cr	140.0	145.2	135.6	147.4	157.6 (AE)
2.2	Growth Rate	%	6.5	3.7	-6.6	8.7	7.0 (AE)
2.3	GVA at Basic Prices (2011-12 prices)	Rs Lakh Cr	127.4	132.2	125.9	136.1	145.2 (AE)
2.4	Growth Rate	%	5.9	3.8	-4.8	8.1	6.7 (AE)
2.5	Gross Savings Rate	% of GNDI	30.6	29.4	27.8	N.A.	N.A.
2.6	Gross Capital Formation Rate	% of GDP	33.8	30.7	27.3	31.2	31.7 (AE)
2.7	Per Capita Net National Income (at Current Prices)	Rs.	1,25,883	1,32,115	1,26,855	1,50,007	1,70,620
3	**Production**						
3.1	Food Grains	Million Tonnes	285.2	297.5	310.7	315.7	149.9 (AE)
3.2	Index of Industrial Production (Growth)	%	3.8	-0.8	-8.4	11.4	5.5 (Apr-Nov)
3.3	Electricity Generation (Growth)	%	5.2	0.9	-0.5	8.0	9.8 (Apr-Dec)

4	**Prices**						
4.1	WPI Inflation (average)	%	4.3	1.7	1.3	12.8	11.6 (Apr-Dec)
4.2	CPI (Combined) inflation (average)	%	3.4	4.8	6.2	5.5	6.8 (Apr-Dec)
5	**External Sector**						
5.1	Merchandise Export Growth	%	8.7	-5.1	-6.9	43.8	9.1 (Apr-Dec)
5.2	Merchandise Import Growth	%	10.4	-7.7	-16.9	55.1	25.0 (Apr -Dec)
5.3	Current Account Balance	% of GDP	-2.1	-0.9	0.9	-1.2	-3.3 (H1 FY23)
5.4	Foreign Exchange Reserves (end of year)	USD Bn	411.9	475.6	577.0	617.6	573.7 (as on 20 Jan 23)
5.5	Average Exchange Rate	Rs / USD	69.9	70.5	74.2	74.5	79.9 (Apr-Jan)
6	**Money & Credit**						
6.1	Broad Money (M3) Growth (Annual)	%	10.5	8.9	12.2	8.7	9.7 (as on 13 Jan 23)
6.2	Scheduled Commercial Bank Credit Growth	%	13.2	6.1	5.6	9.6	16.5 (as on 13 Jan 23)
7	**Fiscal Indicators (Centre)**						
7.1	Gross Fiscal Deficit	% of GDP	3.4	4.6	9.2	6.7	6.4 (RE)
7.2	Revenue Deficit	% of GDP	2.4	3.3	7.3	4.4	4.1 (RE)
7.3	Primary Deficit	% of GDP	0.4	1.6	5.7	3.3	3.0 (RE)

Source : as published by CII with data sourced from CSO, RBI, Ministry of Commerce & Industry and CGA
Legends : AE : Advance Estimates : RE : Revised Estimates; H1 refers to first half of fiscal year (Apr – Sep); NA indicates Not Available.

◆◆◆

FOCUS

Analysis of Allocations for Defence: Union Budget 2023-24

Kapil Aggarwal*

Smt Nirmala Sitharaman, the Hon'ble Finance Minister, presented her fifth successive Union Budget on 01 February 2023. By all accounts, it appears a growth-oriented budget and was hailed by eminent economists and captains of industry. No election freebies are visible in the budget in this pre-election year, which was a relief. The budgetary numbers at the macro level are summarised below.

GDP: The government has estimated a nominal GDP growth rate of 10.5% in 2023-24 (i.e. real growth plus inflation). The real GDP growth is estimated in the band of 6.1% to 6.8% with 6.5% as the base case.

Fiscal Deficit: The Fiscal Deficit is estimated to be 5.9% of GDP with the three year rolling target given as 4.5% of GDP (by 2025-26).

Expenditure: The government proposes to spend Rs 45,03,097 crore in 2023-24, which is an increase of 7.5% over the Revised Estimate (RE) of 2022-23. Out of the total expenditure, Revenue Expenditure is estimated to be Rs 35,02,136 crore (1.2% increase) and Capital Expenditure is estimated to be Rs 10,00,961 crore (37.4% increase). Excluding loans and advances, the Capital Outlay has increased by 35% over the RE 2022-23.

Receipts: The receipts (other than borrowings) in 2023-24 are expected to be to the order of Rs 27,16,281 crore, an increase of 11.7% over RE of 2022-23.

Source: Note on Demand of Grants 2023-2024.

Defence Budget

Unlike previous budgets, the specifics of Defence Budget were conspicuous by their absence in the budget speech. There were no big-ticket announcements made. Allocations at the macro level are summarised below.

Total Allocation: Rs 5.94 lakh crore, an increase of 13% over Budget Estimate (BE) of previous year (Rs 5.25 lakh crore).

Capital Outlay: Increased by 6.7% to Rs 1.63 lakh crore. Distribution amongst the three Services is as follows:

Army	:	Rs 37241 crore (increase of 14.25%)
Navy	:	Rs 52804 crore (increase of 10.64%)
Air Force	:	Rs 57137 crore (increase of 6.3%)
DRDO	:	Rs 23,264 crore (increase of 9%)
BRO	:	Rs 5000 Crore (increase of 35%)
iDEX & DTIS	:	Rs 116 Crore (increase of 93%) and Rs 45 Crore (increase of 95%).
Revenue Expenditure	:	An increase of 8.8% to Rs 2.7 lakh crore
Defence Pensions	:	Rs 1.38 lakh crore (increase of 15.5%).
MSMEs	:	Credit Guarantee Scheme with a corpus of Rs 9000 crore
MoD (Civil)	:	Rs 8775 crore (Capital) and Rs 13838 crore (revenue)

Source : Note on Demand of Grants 19,20,21,22 for 2023-24

**Lt Gen Kapil Kumar Aggarwal, AVSM, SM, VSM retired as the Director General, Electronics and Mechanical Engineering. Earlier, he was the Chairman, Army Pay Commission Cell. He is a Post Graduate Engineer from IIT Kharagpur and also an alumnus of Defence Services Staff College, Wellington.*

Comparison of Defence Budget with RE 2022-23

The present budget allocation of Rs 5.94 lakh crore, although 13% higher than BE 2022-23, yet it is just 1.5% higher as compared to the Revised Estimate (RE) 2022-23 of Rs 5.85 Crore (on an overall basis). This is evident from the interesting table below, which reveals that at the RE stage 2022-23, revenue budget had to be increased by more than Rs 26,000 crore, which as per the PIB release of 01.02.2023, was to ensure liquidation of the entire carry over liabilities during the current year thereby ensuring that there is no dent in the next year's operational outlay of the Services. Clearly the major factors were the operational exigencies obtaining in Ladakh and North East as also the OROP arrears.

Defence Budget Composition (in Rs Crore)

Major Head	**BE 2022-23**	**RE 2022-23**	**BE 2023-24**	**% Change 2022-23 RE to 2023-24 BE**
MoD (Civil)*	43675	45183	45919	1.6%
Defence Services (Revenue)	239743	266984	277033	3.76%
Capital Outlay (Defence)	152369	150000	162600	8.4%
Defence Pensions	***119696***	***153414***	***138205***	***-10% (15.4% BE FY 23***

Extracted from Page 9 Serial 19-22, Demand For Grants 2023-24

*Excluding revenue receipts

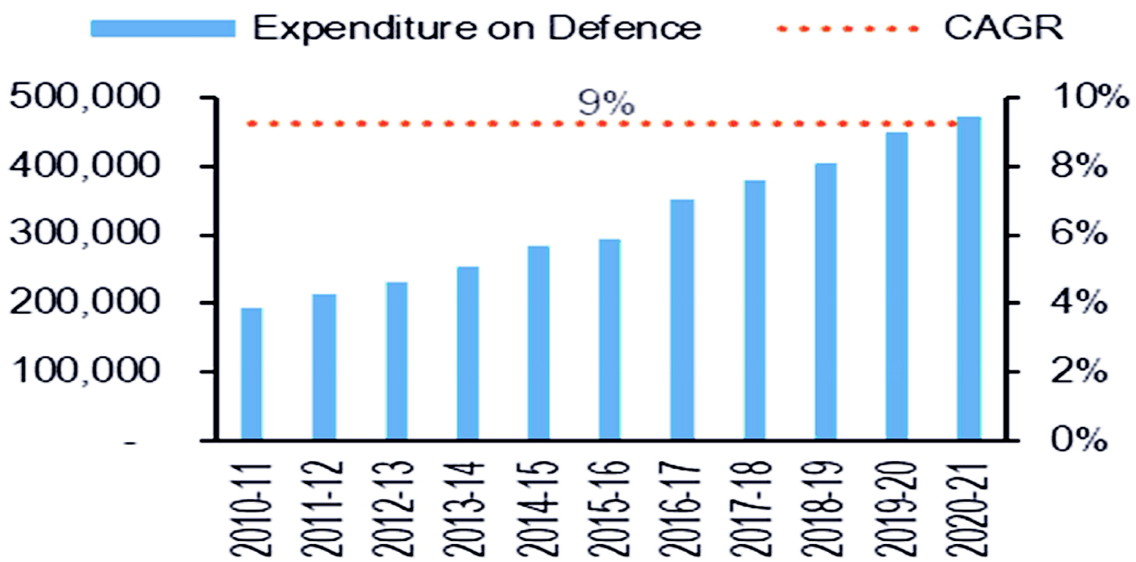
As far as Pensions are concerned, there was a huge increase of about Rs 33,000 crore (28%) at the RE stage, which as per the PIB release included an amount of Rs 28,138 Crore to meet the requirement on account of revision of Armed Forces Pensioners/ Family Pensioners under One Rank One Pension (OROP). Thus, the BE 2023-24 reflects a decrease of about 10% in the Pension outlay vis a vis RE 2022-23.

Analysis of Overall Defence Budget

As outlined earlier, Defence Budget 2023-24 has an allocation of Rs 5.94 lakh crore including approximately Rs 1.38 lakh crore in pensions. There is a perception of Defence Budget being large and the need to cap it, especially the need for reducing the ever-burgeoning Pension bill. Every year sees an increased allocation to Defence; every year it is called the highest ever defence budget allocation. True, in terms of absolute figures but the whole gamut of figures associated with the defence budget need a nuanced scrutiny and ratio analysis with standard yardsticks along with their progression over the years to arrive at a meaningful inference. Accordingly, the official statistics for the last decade need to be examined under the following parts:-

- Growth Rate of Defence Budget Allocation
- Defence Expenditure as a ratio of GDP
- Defence Expenditure as a ratio of Central Govt Expenditure (CGE)
- Comparison with Major Countries/Countries of Interest

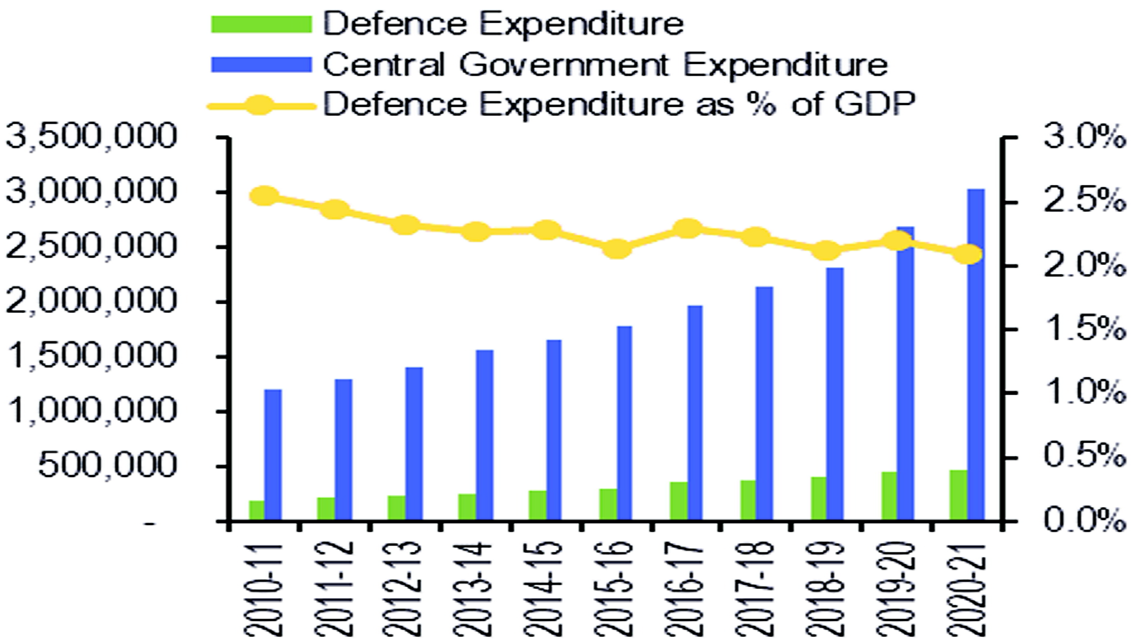
Budget of Ministry of Defence (in Rs Crore)



Source : Union Budget Documents 2010-2020; PRS.

The Defence Budget, as seen from the above figure, between Financial Years 2011 and 2021 has grown at a CAGR of 9%. During the same period, India's GDP has grown from approximately USD 1676 billion to USD 2667 billion (source IMF, Statista 2022). Adjusted for the USD-Rupee exchange rate (45.03 on 01.01 2011 and 73.05 on 01.01.2021), the GDP has grown at a CAGR of 9.94%, higher than the growth of Defence Budget, even when the defence budget includes expenditure on numerous civilian establishments like PSUs and ordnance factories with total strength of serving civilians being approximately four lakh.

Defence Expenditure as a Percentage of GDP (in Rs Crore)

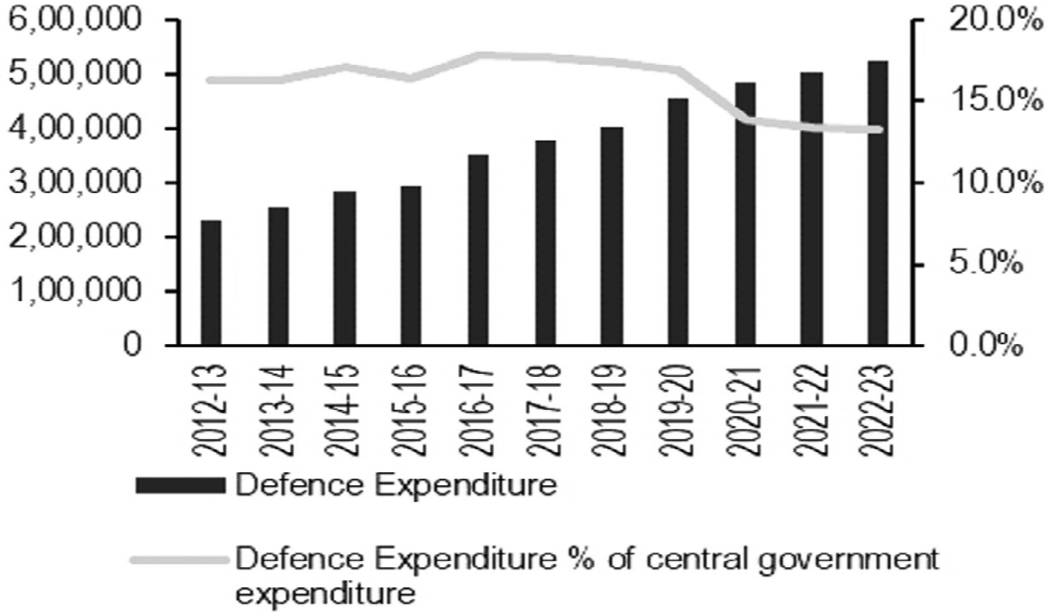


Source: Union Budget 2010-20, Central Statistics Office; PRS

The above Figure shows the Defence expenditure reducing as a % of GDP, a secular decline. To put things in perspective, throughout the decade of eighties, defence budget as a percentage of GDP was upwards of 3.5% while now the defence budget (including pensions) may barely exceed 2% of GDP. The inference is that while their is an annual increase in the Defence Budget, the same is declining in terms of percentage share as part of the GDP. If GDP is visualised as a piece of national cake, then defence is getting a smaller and smaller, ever reducing slice of this cake! A former Prime Minister had spoken of the necessity of maintaining the defence budget at 3% of GDP. The same was reiterated by the Standing Committee on Defence (2018) which had recommended that the Ministry of Defence should be allocated a fixed budget of about 3% of GDP to ensure adequate preparedness of the armed forces.[1] As per official figures[2], the defence expenditure as a percentage of GDP has declined from 2.3% in 2012-13 to 2% in 2022-23. Just as a matter of reference, agricultural subsidies alone in India are usually about 2.25% of GDP, while distortions in power sector require another 4% of GDP.

As per the latest analysis, Defence expenditure has grown at an annual average rate of 8.6%, while total government expenditure has grown at 10.8%. The defence expenditure, thus, as a proportion of Central Government Expenditure, over the period 2012-13 to 2022-23 has decreased from 16.4% to 13.3%. As per the BE of 2023-24, it is still lower at 13.18%.

Defence Expenditure As a % of CGE (2012-13 to 2022-23) (in Rs Crore)



Sources: Union Budget documents (various years); PRS.

As per the latest Stockholm International Peace Research Institute(SIPRI) report, India is the third largest military spender in the world. It will also be of interest to compare the defence spending of our neighbouring and developed countries, the budgets as a percentage of GDP and overall Govt expenditure. According to the data submitted by the Ministry of Defence to the Standing Parliamentary Committee on Defence, relevant to year 2018[3], the Defence Expenditure comparison is as follows:-

Country	As % of GDP	As % of Govt Expdr
China	1.9	5.5
Pakistan	4	18.5
US	3.2	9
Russia	3.9	11.4
UK	1.8	4.6

It is evident that India's Defence Expenditure as a % of GDP pales in comparison to expenditure of Pakistan, US and Russia. China's defence budget as a % of GDP appears lower; However, as per the SIPRI report, India has a defence budget at USD 71.1 billion, while China's defence budget is more than three times that of India at USD 261 billion.

Modernisation of Forces (Capital Expenditure)

It is evident that India can afford higher defence expenditure (from the perspective of GDP progression), yet the defence allocation is reducing in comparative terms vis a vis the overall Govt expenditure. Budget allocation to defence every year falls short of the resource projection by the Forces. For the current Financial Year 2023-24, out of the defence budget allocation of Rs 5.94 lakh crore, revenue expenditure on salaries, Operational Maintenance of Forces (stores, spares and repairs) along with pensions is Rs 4.08 lakh crore, which is 68.7% of the defence budget. Capital outlay of Rs 1,62600 crore forms just 27.4% of the defence budget. The remaining allocation is towards border roads, research, and administrative expenses. It is the Capital outlay which is relevant for modernisation of Forces and a cause of concern as evident from the figure below[4].

Expenditure on Capital Outlay (2012-13 to 2022-23) (in Rs Crore)

Source: Union Budget documents (various years); PRS

It is evident that there is only a marginal increase in % share of Capital Outlay during last ten years. In fact, in absolute terms, between 2012-13 and 2018-19 the average annual growth rate of Capital Outlay was just 5% while between 2019-20 and 2022-23 it has increased to approximately 11%. The overall impact of a largely stagnant defence budget (adjusted for inflation) and within the budget, higher increase of revenue component (mainly pay and pensions) vis a vis Capital Outlay is that there is not enough capital allocation for modernisation of forces.

The Standing Committee on Defence (2018) had noted that modern armed forces should have one-third of its equipment in the vintage category, one-third in the current category, and one-third in the state-of-the-art category. However, Indian Army had 68% of its equipment in the vintage category, 24% in the current category, and 8% in the state-of-the-art category. The Committee also noted that over the years, the Army has accumulated a substantial deficiency of weapons, stores and ammunition. It found that adequate attention has been lacking with respect to both policy and budget for modernising the aging armoury[5].

Of late, the Govt has aptly prioritised Capital Expenditure at the national level as well as in Defence; the Capital outlay in national budget 2023-24 has increased by 35% over last year. However, the defence budget 2023-24 has only a modest increase of 8.4% in Capital outlay (vis a vis RE 2022-23), allocating Rs 1,62,600 crore vis a vis 1,50,000 crore at RE 2022-23, which itself was a reduction from BE figure of Rs 1,52,369 crore. The inference is that while Govt wants to alter the Capital to Revenue expenditure ratio in favour of Capital so that Forces are modernised at a faster pace, yet it has realised that after excluding committed and contractual liabilities, there are limitations in absorption of Capital allocated on an annual basis.

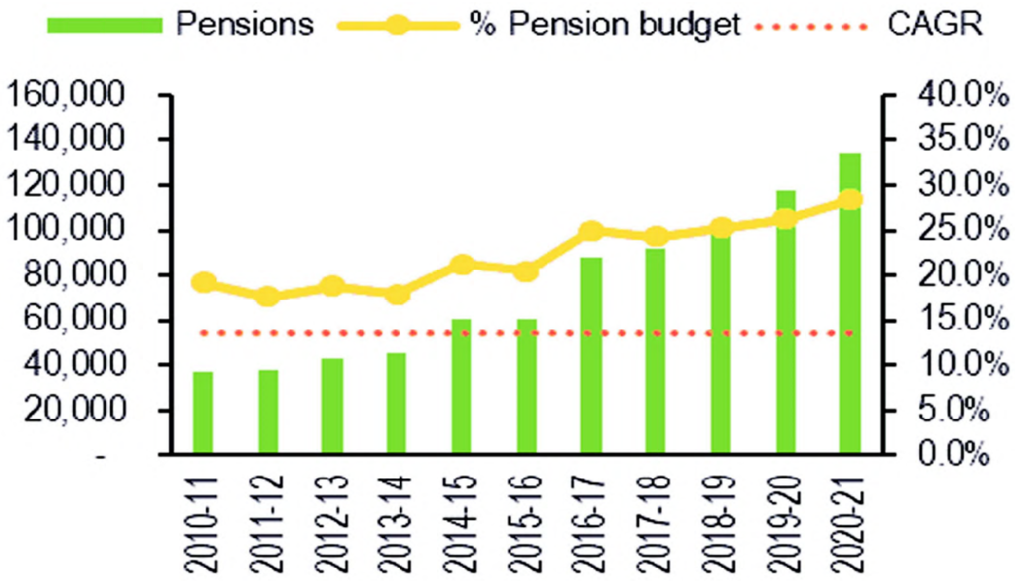
In order to tackle the limitations in annual absorption of allocated modernisation funds, the 15th Finance Commission recommendation of constituting a non lapsable, dedicated Modernisation Fund for Defence and Internal Security has to be implemented. This will also be a reassurance for industry and encourage them to enhance their production capacities. It is also to be noted that higher Capital Expenditure as part of defence spending has a multiplier effect on industrial productivity and thus the national GDP, not to emphasise the strengthening of defensive capability itself. Overall, it gives a fillip to the Comprehensive National Power of which military strength is an important component.

Defence Pensions (Revenue Expenditure)

The next perception to be addressed is the inordinate burgeoning of the pension bill. As seen from the Figure on Defence Pensions, the same have increased at a CAGR of approx. 13.5%. This pension bill increase is again lower than the nominal GDP growth, despite grant of OROP and arrears during the period. However, there is no denying the fact that the defence pensions are increasing at a faster pace (13.5%) than the defence budget itself (9%), ie pace of increase is 50% higher.

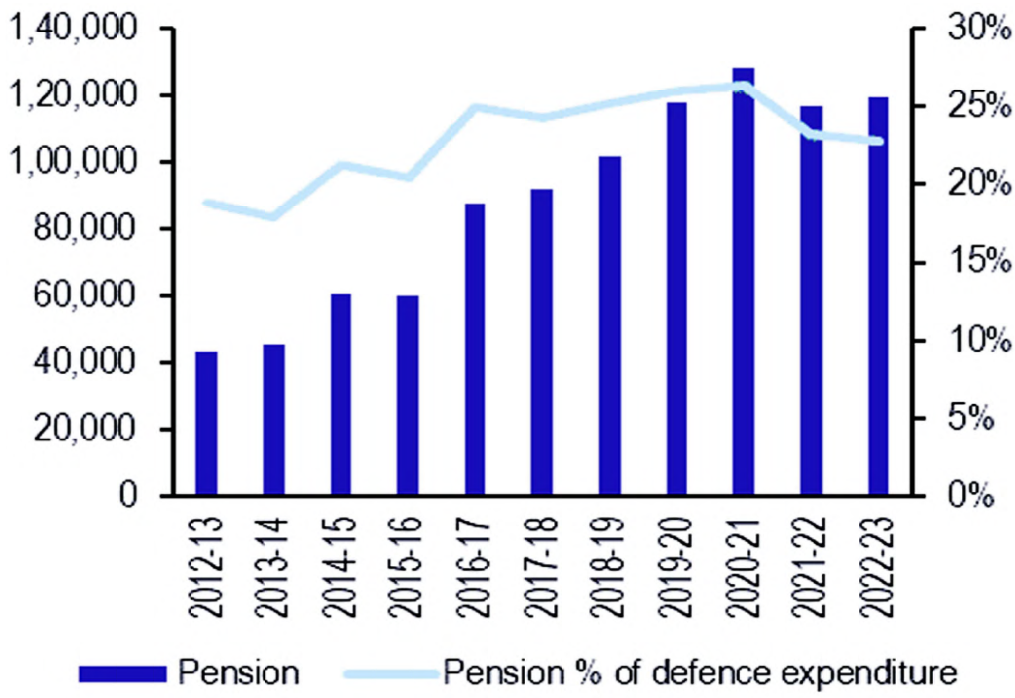
If we take the 10 year window as 2012-13 to 2022-23, Expenditure on defence pension has grown at an annual average rate of 10.7%. This is again higher than the average annual growth of the defence budget at 8.6%. In the budget for 2023-24, the expenditure on defence pension is estimated to be Rs 1,38,205 crore which is 15.5% higher than the BE of Rs 1,19,696 crore in 2022-23. This is ostensibly due to payment of arrears of OROP, due since July 2019.

Expenditure on Defence Pensions (2010-11 to 2020-21) (in Rs Crore)[6]



Source: Union Budget 2010-20; PRS.

Expenditure on Pensions as % of Defence Budget (in Rs Crore)[6]



As far as the share of pension in the defence budget is concerned, it increased from 19% in 2012-13 to 26% in 2019-20. It has since fallen to about 23% as per the budget estimates of 2023-24. In the budget for 2023-24, the expenditure on defence pension is estimated to be Rs 1,38,205 crore which is 15.5% higher than the BE 2022-23 of Rs 1,19,696 crore, but 11% lower than the 2022-23 RE figure of Rs 1,53,414 crore. This is ostensibly due to payment of arrears of OROP, due since July 2019. It is likely that there would be additional allocation at RE stage.

It is also worthwhile to mention that average per capita pension of defence personnel is much lower than a Central Govt civil employee. For 11,28,441 civilian pensioners, the Govt paid Rs 64,684.44 crore as pension in year 2021-22 while for 36,03,609 defence pensioners, the outgo was Rs 1,21,983.9 crores[7]. The Defence Pension Budget, however, is big in absolute numbers due to large number of retired personnel which itself is a function of soldiers being compulsorily retired early from 36 years age onwards owing to the requirement of maintaining a young and physically fit military. The total number of defence pensioners stands at 34,10,567 while the total number of all Govt pensioners is 68,62,465[8]. The inference is startling, ie today, half of the total Central Govt pensioners today are defence personnel and it only corroborates the analysis above. It also indicates that that India has 2.4 defence pensioners for every serving soldier while the ratio for civilians is approximately one pensioner for each serving employee. The reason for high pension bill of the Services, is now evident; it is this problem which would have made a real dent in the pension bill, if tackled.

Various proposals have been made over the years to check the pension budget, ie lateral absorption in Govt jobs on retirement or re-calibration of retirement ages. However, they have not been implemented. Last year, in June 2022, the Agnipath scheme of recruitment of soldiers has been introduced. Although, reduction of pension budget was not been listed as one of the objectives of the Agnipath scheme in the Govt website, yet it is likely to result in reduction of revenue expenditure, depending upon the annual recruitment intake.

Revenue Expenditure (Excluding Pensions)

Revenue expenditure (excluding pensions) for the year 2023-24 as per the budget estimates is Rs 2.7 lakh crore, which is approximately 45.5% of the total defence outlay, a major chunk. It caters for salaries, operational maintenance of Forces, stores, spares and repair expenditure. Since the limelight at the national level is invariably on the requirement of speeding up defence modernisation and limiting the defence pensions, the less glamorous revenue component of defence expenditure does not get enough attention of analysts. In any case, salaries is a rather inelastic component of Revenue Expenditure, based on Central Govt Pay Commission awards, while the variable factor of Revenue Expenditure happens to be the Operational Maintenance of Forces.

The Revenue allocation of Rs 277033 crore for 2023-24 is a significant increase of 15.5% from BE 2022-23 (Rs 2,39,743 crore) but just a 3.8% increase from RE 2022-23 (Rs 266984 crore). This needs to be seen in the backdrop of salary budget which is expected to increase 6-8% annually due to inflation based DA increases alone. The inference is clear, either the Revenue allocation will have to be enhanced again at RE 2023-24 or there will be a severe squeeze on operational maintenance of Forces, including stores, spares and repairs.

Indigenisation and Atma Nirbhar Policy

Make In India initiative was launched on 25 Sep 2014 with the primary goal of making India a global manufacturing hub by encouraging both domestic as well as foreign companies to manufacture their products within the country. Since then, Make In India has introduced many new initiatives viz promoting FDI, implementing IPR and developing the manufacturing sector, thereby facilitating job creation and fostering innovation and skill development. The major focus of Make In India in Defence Sector has been on Indigenisation in manufacturing of weapon systems and Govt's commitment to transform India into a Defence Industrial Hub for both import substitution as well as to export Indian made defence products to other countries. During the recent Air Power Show in Bengaluru on 13.02.2023, the Hon'ble PM, Shri Narendra Modi stipulated the Export target of USD 5 billion for defence systems by 2025.

The Govt has taken a number of initiatives to promote indigenous manufacture of defence equipment. In 2017, a Make II - a time bound, fast track procedure - was introduced in Defence Acquisition Procedure to encourage private sector to design and manufacture prototype of equipment which meet the requirements/voids of defence and field them with the three Services. It is felt that a similar procedure for revenue acquisitions also needs to be introduced as part of Defence Procurement Manual; can be termed as a Make III procedure or any other suitable nomenclature. This will also give a huge fillip to the MSMEs, manufacturing assemblies/modules/spare parts for defence.

In September 2020, the Central Govt increased the limit for foreign direct investment (FDI) in defence sector from 49% to 74% under the automatic route[9]. FDI beyond 74% is permitted with government approval which may be given where FDI is likely to result in access to modern technology. Since the increase in limit, an FDI inflow of Rs 186 crore has been reported in the defence sector in the very next year[10].

This year's budget 2023-24 was silent on Indigenisation; last year, budget speech 2022-23, the Hon'ble Finance Minister had announced that 68% of defence procurement will henceforth be from indigenous manufacturers. Hon'ble Defence Minister has now stated in Bengaluru on 15 February that the Govt will earmark 75% of defence procurement budget for the domestic industry. The move will throw open Rs 1 lakh crore in defence contracts for Indian private and public sector defence companies in the new fiscal year[11]. However, for this to happen, the production capacity of domestic Industry (DPSUs and private Sector) has to increase significantly.

In order to deeply entrench the indigenisation drive of weapon systems/ equipment, the focus on R & D in defence also has to improve. In the last six years, the expenditure on R&D by DRDO, the primary research agency for defence, has remained between 0.08% to 0.09% of GDP. This is too low as noted by the Standing Committee on Defence (2021), much lower than what developed countries spend. The total national spend on R&D has to go up to at least 1% of GDP, for the success of indigenisation policy in defence. Innovation in the defence domain has to be given a further boost through start-ups eco system, IDEX and DTIS schemes and collaboration with academia.

References:

1 *40th Report: Demands for Grants (2018-19) General Defence Budget*

2 *https://prsindia.org/budgets/parliament/demand-for-grants-2022-23-analysis-defence#*

3 *P13, Demand for Grants 2020-21, Standing Committee for Defence (2019-20)*

4 *https://prsindia.org/budgets/parliament/demand-for-grants-2022-23-analysis-defence*

5 *41st Report, Demands for Grants (2018-19) Army, Navy and Air Force, Standing Committee on Defence, Lok Sabha, March 2018, http://164.100.47.193/lsscommittee/Defence/16_Defence_41.pdf.*

6 *https://prsindia.org/budgets/parliament/demand-for-grants-2022-23-analysis-defence*

7 *Lok Sabha Unstarred Question No 2961 of 03.08.2022*

8 *Lok Sabha Unstarred Question No 2324 of 16.03.2022*

9 *"Press Note No. 4 (2020 Series), reviewing Foreign Direct Investment (FDI) Policy in Defence Sector", Press Information Bureau, Ministry of Commerce & Industry, September 18, 2020.*

10 *Starred Question No. 161, Rajya Sabha, December 13, 2021, https://pqars.nic.in/annex/255/AS161.pdf.*

11 *Economic Times, New Delhi, 16 February 2023*

Inferences:

- *Indian Defence spending, whether as a percentage of GDP or on pro rata basis is decreasing gradually and continuously.*
- *The spending is lower in comparison to most countries of interest, even though India has higher security concerns.*
- *Apparently, while security concerns get adequate attention, priority is development, ie infrastructure and poverty alleviation.*
- *However, there is evidence of commendable flexibility in additional funding of defence requirements at RE stage, based on operational requirements.*
- *Within the Defence Budget, focus is on modernisation and infrastructure; however, procedural constraints seem to hamper absorption of allocated funds. The recommendations of 15th Finance recommendation on non lapsable modernisation fund have to be implemented. It is also evident that Capital Outlay for procuring modern Weapon Systems/Platforms can increase significantly only if higher funds are allotted to defence, ie a higher % of GDP or Central Govt Expenditure.*
- *Pension Budget is large due to sheer number of retired personnel, even though per capita pension of defence personnel is lower than national average, despite OROP granted by the present Govt.*
- *Higher ab-initio allocation is required for operational maintenance of Forces to avoid adhoc additional funding at RE stage.*
- *Salary and Pension bills being rather inelastic (based on Central Pay Scales and norms), the funding squeeze will either be on Capital Expenditure or on Operational Maintenance of Forces.*
- *The initiatives on Indigenisation of Defence Manufacturing are a potent way to conserve Capital and need to gather further pace. Atma Nirbhar is the way to go, but will require increase in domestic production capacity and higher R&D expenditure.*
- *Overall, a way has to be found in the ensuing decade to reverse the decline in defence spending as a percentage of GDP, accelerate the modernisation of Forces and have higher defence contribution in Comprehensive National Power of India.*

◆◆◆

Empowering the Digital Economy through Budgetary Provisions and Policy Signalling

Jaijit Bhattacharya*

Introduction

This Union Budget 2024 continued on the path to enabling increased allocation to digital infrastructure, including Digital Platform Infrastructure, thus ensuring that the Indian economy accelerates towards a lower cost, higher efficiency, competitive economy.

Let us analyse the budget from an overall perspective, before we deep dive into the digital aspects. The announcement of significant tax reductions for the middle class made it a "feel great" budget for the masses, while avoiding populist measures and avoiding unnecessary freebies. It was thus another mature budget presented, with budgetary support being extended to only the vulnerable sections of the society such as those who require food grain support or for MSMEs that are the backbone of the economy and not resorting to mass populisms that lead to fiscal pressures and ultimately to inflation. Hence, in this context, a budgetary support of Rs 2 trillion for food grains is most welcome. In the same spirit, targeting a spend of 2.5% of GSP on healthcare by 2024 is a very desirable step.

The budget appeared to focus on enabling people and small businesses to earn their own living, that is to be economically self-sustaining. In other words, it was a budget that enabled people to be 'Atmanirbhar'. How does the budget achieve such an objective? The massive capital outlay of Rs 10 lac crore or 3.3% of the GDP ensures that the public sector spend creates the demand for cement, steel, labour, transportation, logistics and so on that would give an opportunity for people to provide the goods and labour. This is further amplified by proposed increase in budgetary support for PM Awas Yojna (housing for all) to the extent of 66%, making it a Rs 79,000 crore outlay. There is also INR 2.4 trillion of additional investments for the Indian Railways, which is the highest in a decade and four times last year's budget. This outlay is double of what was generally expected. In addition, there are multiple other infrastructure outlays such as 50 new airports and heliports, coastal shipping etc. The multiplier effect of such an unprecedented capital expenditure will ensure that all sectors of the economy grow in an economically sustainable manner.

Along with economic sustainability, there is very significant focus on environmental sustainability, both in terms of moving the economy away from polluting industries and energy sources to promoting production of green capital goods such as batteries, solar power, hydel power etc.

**Dr Jaijit Bhattacharya is a noted expert in technology policies and technology-led societal transformation. A recipient of the prestigious APJ Abdul Kalam Award for innovation in Governance, he is currently President of Centre for Digital Economy Policy Research. He is also CEO of Zerone Microsystems Pvt Ltd, a deep-tech startup in the fintech sector.*

To this goal, committing Rs 20,700 crore to generation of 13 GW from Ladakh has repercussions in not only making our energy sources green, but also making Ladakh a green energy hub and increasing local job opportunities in a future industry. There is also a very significant commitment of Rs 19,700 crore to accelerate the green hydrogen industry and a humungous target of having capacity for battery storage of 4 GWH.

As with all Indian budgets, this budget continues to provide significant support to agriculture. Agriculture has grown by a sustained average annual rate of 4.6% in the last six years. However, what is different in this budget is that it aims to steer the agriculture industry towards more sustainable practices such as growing of millets that are natural, indigenous crops for India that require less water, and thus making India the global hub for millets, to moving away from chemical pesticides and fertilisers through 10,000 support centres. I am assuming such a change would be effected responsibly and in a graded manner such that we do not fall into the trap that Sri Lanka fell into by adopting natural agricultural practices in a knee-jerk manner without scientifically sanctified practices for the same.

The budget also continued this government's quest for enhancing ease of doing business by creating centralised KYC infrastructure and having PAN as single identifier. It also aims to build a Digilocker for companies so that they can have the same benefits as individuals. It also provides significant relief to MSMEs.

The Nudge to Digital

The above steps help in increasing the demand for digital from both consumers and the industry. With extra money in their hands, taxpayers would spend some of it on digital such as access devices (smartphones or laptops), broadband connection, intelligent machines such as smart washing machines etc. The industry too will consume more optical fibre as the large scale housing projects are built-out. In addition, with the push to ensure that fibre optic is laid out with all linear infrastructure, there would be a significant uptick in consumption of fibre optic.

The budget also brought in sharp focus on future industries, be it industry 4.0, with considerable focus on Artificial Intelligence (AI) to the next generation of diamond industry that is driven by lab grown diamonds (LBG) which is environmentally responsible and can feed the massive diamond cutting and polishing industry of India that sustains an army of skilled labour. The budget proposed to leverage digital for multiple sectors, including what caught people's attention was digitisation of one lac ancient inscriptions, thus democratising the quest for discovering more about our rich cultural and scientific heritage. There is also push for drone adoption, thus incentivising to create future industries.

Specific Provisions for Digital

Besides the nudges to Digital, the budget has specific provisions for supporting Digital. It has allocated INR 16,549 crore to the Ministry of Electronics and Information Technology, which is a 40% higher allocation than that of last year. This allocation includes INR 3,000 crore for the Indian Semiconductor Mission. Semiconductors are the heart of digital and are extremely strategic, as has been made amply clear during the COVID induced semiconductor shortages, which were exacerbated by the Ukraine war. Without semiconductors, most modern manufactured products can come to a grinding halt, as most modern gadgets and white goods are run using semiconductors. This includes automobiles, washing machines, air conditioners, displays, televisions etc. Even solar panels are based on semiconductors. With a giant push towards switching to carbon-neutral energy generation, solar panels have become critical for India and therefore, semiconductors have become even more of a strategic requirement for India. Thus, India having a negligible semiconductor manufacturing capacity requires urgent attention to kickstarting the manufacturing of semiconductors in India. The budget does well in ensuring that we finally get around to pushing for semiconductor manufacturing in India. In December 2021, the government had announced a corpus of Rs 76,000 crore to promote the semiconductor and display manufacturing ecosystem in India. The budget this year signals the seriousness of the government to promote an atmanirbhar semiconductor industry.

The allocated INR 3000 crore corpus includes INR 1,799 crore that has been allocated for the modified scheme for setting up compound semiconductors, silicon photonics, sensors fab, discrete semiconductors fab and semiconductor assembly, testing, marking and packaging (ATMP), outsourced semiconductor assembly and test (OSAT) facilities in India. These are critical for establishing the semiconductor ecosystem in India.

In addition, the budget has allocated Rs 1,000 crore for the modified scheme for setting up of semiconductor fabs in India, while Rs 4 lakh has been allocated for the scheme to set up display fabrication units in India. Such units are required in televisions, mobile phones and other such devices. To back the semiconductor wafer fab proposals by various corporate entities, the scheme involves the central government making a large, upfront investment which would possibly be to the tune of 50% fiscal support as per recent modifications. The budget also allocated INR 200 crore for design-linked incentive scheme to incentivise companies to design semiconductor chips and wafers in India.

The budget also supported the Digital Platform Infrastructure that India has created and is a pioneer in the world. To augment the digital payment capacities, the budget has allocated INR 1,500 crore for promotion of digital payments. This scheme will push banks to develop robust digital payment ecosystem, and to promote RuPay debit card and BHIM-UPI digital transactions across all sectors. Such a move will make the Indian economy significantly more efficient. UPI has grown by leaps and bounds in the past couple of years as it facilitated transactions worth Rs 125.94 trillion in the calendar year 2022, jumping 4X from Rs 33.88 trillion in 2020.

To promote more of electronics manufacturing in India, with more indigenisation of components, the budget has also allocated INR 4,499 crore for the production-linked incentive (PLI) scheme for large-scale electronics manufacturing. The scheme envisages incentives between 3% and 6% on incremental sales of goods manufactured in India.

The PLI scheme for IT hardware, which offers incentives between 2% and 4% on incremental sales for goods such as laptops, servers, tablets, and all-in-one PCs manufactured in India, has been allocated Rs 146 crore. These allocations will significantly strengthen electronics manufacturing in India. Such measures have helped India pull back from a situation where it was predicted that by 2016, India's import bill for electronics will be more than our oil import bill. Instead, we have shot from having almost no production of mobile phones to becoming the second largest producer of mobile phones in the last few years. Such scale up has been unprecedented globally, and the budgetary incentives and PLI schemes have played a significant role. In addition, the budget has allocated significant funds for the modernisation of the semiconductor laboratory at Mohali, while Rs 533 crore has been allocated for other expenditures of SCL.

The budget has also announced support for an open-source, digital public agriculture infrastructure that will facilitate the agricultural sector in the country. A digital agricultural stack, a data repository of the farm sector, is already being built and the new open-source initiative, which will be accessible to the private sector, is expected to be based on it. It is expected that such an initiative will enable inclusive, farmer-centric solutions through relevant information services for crop planning and health, improved access to farm inputs, credit, and insurance, help for crop estimation, market intelligence, and support for growth of agri-tech industry and start-ups.

So clearly, the budget has given a significant push to greater digitalisation of the Indian economy and has also built in sufficient signalling of the path that the nation will take. However, it is important to also understand issues that are not necessarily solvable through budgetary provisions.

What did the industry want?

To understand the impediments to an accelerated digitalisation of the economy, it is important to understand some of the key asks of the digital economy.

The foremost is that we still have large parts of the country that are not connected through broadband. As has been oft repeated, the Wuhan Covid pandemic has made it amply clear that broadband is a necessity for survival. Under such circumstances, accelerating the rollout of BharatNet III Saturation Project, which aims to connect every village with a broadband, is critical. The more time we lose, the more we lose the chance of educating the youth, providing services to the old and connecting the workers to opportunities. Each of these lost opportunities will quickly come back to bite India, as India propels to greater levels of growth and prosperity. We would be staring at problems of not finding appropriately trained workers while having the largest population in the world. We may need to import skilled workers to fill the gap, while not being able to offer jobs to our citizens, as they did not get trained. Therefore, it is imperative that we execute the Bharat Saturation Project on an urgent basis.

In the above context, it needs to be noted that given the criticality of universal broadband connectivity, the government has gone on a war footing on the 4G saturation project, which aims to cover every village in the country with 4G connectivity. However, for such an infrastructure to operate effectively, the towers would need to be connected by optical fibre, which brings us back to the issue of rapid implementation of BharatNet Saturation Project.

In addition, given that the Indian environment takes a toll on the optical fibres been rolled out, it is important that we roll out bend-resilient optical fibres, which do not degrade when bent. Fortunately, India manufactures such fibres domestically, while the poorer quality fibres are imported. It would be beneficial for an atmanirbhar optical fibre industry that India adopts bend-resilient fibre for government initiated projects, which will not only ensure that higher quality infrastructure is created, but will also ensure a future-proof infrastructure, supported by the local industry.

As part of atmanirbhar, the government has taken proactive steps to mandate use of Atmanirbhar products for any component that is a significant percentage of a project. This was part of the Public Procurement Preference to Make in India (PPP-MII) order. However, what we observe is that a project has many components and could include large amount of cement and steel and the digital component such as switches etc, become a minuscule portion of the project. It would be important to fine tune the atmanirbhar policy and use percentage of the product as a key metric to enforce atmanirbhar product, rather than using percentage of project as a metric.

And as dwell on the topic of atmanirbhar digital ecosystem, we see a strange phenomenon happening. While the government has pioneered the much-needed policy of "Atmanirbhar", we observe that where the industry is getting marauded by dumping from foreign players, with poor quality fibre, there seems to be a laxity in providing the trade remedies required in such cases. In fact, the industry is observing a strange situation where anti-dumping duty cases are being approved and recommended by the DGTR, but the same appear to be rejected by Ministry of Finance. The budget was an excellent opportunity to provide clarity on the issue and on the larger vision of the government, before we again see our industry getting decimated, rather than becoming the capital of digital production globally.

There are also more proactive steps that can potentially be taken to promote digitalisation of the nation. This may include making it mandatory to provide in-building connectivity, especially for multi-storied buildings and low-cost housing, so that it becomes cheaper to access broadband, as it would be cheaper to layout the connectivity while the buildings are being constructed.

Conclusion

The question at the end is always on how the budget will get funded, with the lofty and desirable goals of getting back to the fiscal responsibility targets, gliding back to 5.9% fiscal deficit in the coming year and to less than 4.5% in the year after? Such a fiscal deficit target also makes the inflation target of sub 6% more believable. But where would the Government get the funds to fund this budget? The budget speech was silent on the disinvestment targets. Perhaps the actual budget documents will have the details. Going by previous track record, there is reason to believe that the budget numbers will add up, especially on the back of higher formalisation of the economy which is also reflected in record GST collections.

If we are able to implement this budget in the way it has been presented, it would be a great start to the 'Amrit Kaal', supporting sustainable agriculture, next generation industries, massive infrastructure rollout and supporting the vulnerable sections of the society, that will further accelerate the growth of per capita income from the current USD 2,500, bringing more prosperity to the common people.

A great budget will have considerable positive impact on India's journey towards accelerated digitalisation. So, while the government has made stunning progress in steering India towards a path of rapid digitalisation, with initiatives that are path-breaking and first of its kind globally, there is more to be done, given the size and complexity of India. There is also a need to ensure that we continue to keep a hawk-eye on our still young digital manufacturing industry and protect them from unfair trade practices of foreign players.

◆◆◆

Macroeconomics of Union Budget 2023-24

Haseeb A Drabu*

Introduction

The macro-economics of the Union Budget 2023/24 is simple, but not simple minded. A classical budget, it seeks to pump-prime the economy through autonomous investment and engender dependent consumption demand thereby increasing incomes, both aggregate and disposable.

Be it the underwriting of food consumption of the poor with a Rs 2 lakh crore allocation for free grain for the poorest, or to increasing public capital expenditure for "crowding in" capital formation by the private sector or the increasing disposable incomes of the high consuming segment of middle class through direct tax relief.

Key Takeaways

This budget makes a break from past in two ways; first, from the time-honoured tradition of being populist ahead of elections. Nirmala Sitharaman has been practical, not populist. Second, a move away from current expenditures and transfer payments, a hallmark of the earlier NDA budgets. The focus of this year's Union Budget is on capital expenditure. The Capex allocation is, unlike in the recent past, likely to "crowd in" capital formation by the private sector because the gross market borrowing program in relation to the nominal growth of the economy is lower. This will ensure that the much-needed private corporate investment is not crowded out from the financing side. Till now, because of the massive pre-emption of financial resources for financing investments, an increase in public investment has resulted in a decrease in private investment, especially private corporate investment.

While the public expenditure policy is decidedly expansionary, the fiscal policy can't be called that. It is, at best, accommodative in its stance and substance. While the size of the gross fiscal deficit is budgeted at fifty basis points lower than the previous year, the cyclically adjusted fiscal deficit is almost 100 basis points lower at 5.5 per cent. This reduction in the overall fiscal deficit comes along with an increase in capital expenditure. Not only is this the key highlight of the budget but it also underlies the real gains in fiscal management over the years.

Given the overall increase of 7.5 per cent in total expenditure, the substantial increase in the capital expenditure that has been budgeted implies a significant change in the structure of expenditure away from revenue expenditure which is budgeted to grow by 1.3 per cent. Notwithstanding the sharp reduction of one third in food subsidy and by a quarter of the fertiliser subsidy bill, revenue expenditure is still 11.6 per cent of GDP; more than three times of capital expenditure which is budgeted to rise to 3.3 per cent of GDP. This points towards the emergence of serious macro-economic anomaly of interest payments overtaking capital expenditures. In other words, the amount of money that the Union will spend to defray past borrowings will be more than that earmarked for creating new capacities. Obviously, this anomaly is a consequence of the national debt having gone up nearly four times from Rs 32.3 lakh crore to Rs 115 lakh crore in FY22. The increasing debt burden has resulted in interest payment shooting up from 2.2% of GDP to 3.1%.

But for now, key takeaway from the underlying fiscal policy is that the revenue deficit, which used

*Mr. Haseeb A Drabu is former Finance Minister of J&K.

to account for more than two thirds of the fiscal deficit and pre-empted as well as raised the cost of finance for productive private investment is beginning to show a decline. It is still not quite at the level of being one-third that it was earlier. This change in fiscal consolidation can free up productive resources for the private sector and contribute to lowering the cost of capital, thereby raising the growth rate of the economy in 2023-24.

An interesting and important initiative in the Union Budget has been to try and delink the Capex in the states from their fiscal deficit. Even as the Centre has fixed States' gross fiscal deficit at 3.5 per cent of the gross state domestic product for 2023-24, it has decided to continue with the 50-year interest-free loan to States for one more year with an enhanced allocation of 1.3 lakh crore. The loan amount will have to be spent in 2023-24. While most of the loan will be at the discretion of the States, a part of it will be contingent on States increasing their actual capital expenditure.

A part of the outlay will also be linked to, or allocated for, scrapping old government vehicles, urban planning reforms and actions, financing reforms in urban local bodies (to make them creditworthy for municipal bonds), housing for police personnel above or as part of police stations, constructing Unity Malls, children and adolescents' libraries and digital infrastructure, and States' share of capital expenditure of central schemes. The Union Budget also proposes to incentivise cities to improve their creditworthiness for municipal bonds through property tax governance reforms and ring-fencing user charges on urban infrastructure. Additionally, an Urban Infrastructure Development Fund (UIDF) is proposed to be established. It will be managed by the National Housing Bank and used by public agencies to create urban infrastructure in Tier 2 and Tier 3 cities.

Despite this, the transfer to states is becoming an area of concern. While the gross transfer to the States is budgeted to increase in 2023-24 (BE) because of an increase in allocation for special assistance to States for capital expenditure, the Finance Commission Grants are budgeted to decline in 2023-24, due to a lower amount of the fixed Revenue Deficit Grants. While a lower post-devolution deficit grant, reflecting a reduced need on account of revenue deficit is a good fiscal trend, the overall transfer to states are lower.

The total transfers to the states are projected to decrease in the upcoming fiscal year, with the states' share of tax revenues reduced to 30.4% from the previous year's 33.2 per cent. Furthermore, the states' share of tax revenues is much lower than the promised 42 per cent share by the 14th Finance Commission. These reductions in transfers may negatively affect the states' ability to fund critical infrastructure and social welfare programs.

At the same time, the transfer to the local bodies shows an increase. While the increased resource flow and the associated financial empowerment of the third tier of governance is desirable, kt is debatable whether this should come at the expense of the state governments. Given that the budget has an accommodative fiscal stance, more so in the structure of expenditure than the level of fiscal deficit, the attention should now shift from Raisina Hill in New Delhi to the Mint Street in Mumbai. Whether or not the growth targets set out in the budget will be met, will now depend on how the RBI, Indian Inc and banking sector responds to the challenge.

The RBI is already set on a path of hiking interest rates and is far from done yet. With the global uncertainties, especially the impact of the Russia-Ukraine war, RBI will keep a watch on how world energy prices behave and what would be the impact of these on inflation and indeed growth. In such a situation, there is a real risk of the RBI looking to follow a conservative monetary policy. A contractionary monetary policy in the face of an expansionary public expenditure policy will cause the same kind of policy schizophrenia that was the hall mark of the economic policy making in the late 80s which eventually resulted in a macroeconomic imbalance and a balance of payment problem.

The starting point for the RBI must be the gross market borrowing program implicit in the Budget. While the nominal rate of growth is assumed to be 15 per cent, the gross market borrowing program is budgeted to increase at around 8 per cent. Clearly, the pre-emption of resources by the government will be lower. Indeed, the moment the FM announced the borrowing number, it led to a rally in government bond prices with a drop in the yield to 7.28 per cent from the levels of 7.35 per cent that it had reached consequent upon the tightening cycle of the RBI. The prime focus of the credit policy will have to be on ensuring adequate liquidity in the market for the credit cycle to gain momentum and engender growth.

The budget has made significant changes to personal income taxation by reducing tax slabs from seven to five and lowering the top slab tax rate from 42% to 39%. The rebate has been raised from Rs 5 lakh to Rs 7 lakh at the lower end, and the exemption limit has been raised to Rs 3 lakh with an enhancement of standard deduction. These changes could be seen as a pre-election sop to the middle class, but they are likely to incentivise taxpayers to switch to the new tax regime.

The growth strategy underlying the budget, which is one of decisive reliance on the home market, must be seen to insulate the Indian economy from the impending global recession. Yet, the budget is not insular, and in its underlying themes, is global. There are three clear themes in the budget. First, of course is **Decarbonisation;** be it Rs 35,000 crore for energy transition, or the 5 MMT of hydrogen, or concession for green mobility, this is pretty much a green budget. In the long run, the focus on decarbonisation is perhaps second only to poverty alleviation in terms of ensuring sustainability of growth. For in the short term, fossil fuel-based energy prices are the single biggest risk to this Budget panning out as planned.

Second is **Digitalisation**, across the board, and not sector or industry specific. Indeed, the budget has been used creatively to push even the artisanal sector and seek to link it to the digital global supply chain network. Third is **Decentralisation** in infrastructure, agriculture and MSME in terms of creation of new production and transactional platforms. More importantly, along with new concessions and tariffs, these will improve the operational efficiency of transmission and distribution networks, thereby responding adequately to the growing challenges of energy in India.

Challenges

The ten Union Budgets presented by the BJP led NDA government over the last decade have, in a sense, laid the foundation of a structural transformation. But while the scaffolding has been erected, subsequent budgetary policies have not leveraged the initiatives of the preceding budget to erect the complete structure. As an example, major policy initiatives have been made to formalise the Indian economy through initiatives such as the GST, but this has not found adequate resonance in subsequent budgets to the degree required. This is perhaps, still a work in progress.

The current Union Budget also could have focussed more on addressing the "transitional" decline in the unorganised sector, resulting in lower growth than what the official statistics indicate. This can have long term adverse implication of a widening income inequality as the unorganised sector suffered a substantial loss of income in the last three years, primarily due to the pandemic and the war in Ukraine. The short-term transitional troubles could have been addressed in the budget by providing more focussed and structured credit to the unorganised sector en-route to its formalisation. This can prove to be the Achilles heel, not just in terms of meeting the budgetary growth arithmetic but of the larger political economy, at a time when the elections are just around the corner.

Budgetary Naam-Karan: Seeking a Civilisational Connect

There is a distinct shift in the earlier inherited lexicon, which in a sense, perpetuated the colonial legacy. We see now a 'vernacularisation' of the Union Budget, through terms such as 'Amrit Kaal', the phrase being used for the first time by Prime Minister Modi on Independence Day, 2021. 'Amrit' literally translates to "nectar of immortality" in Sanskrit while "Kaal" refers to a specific time period. The Finance Minister has characterised this budget as "the first budget of Amrit Kaal"—setting the stage for India to be a developed country by 2047.

So, we see terms such as **Shree Anna** being used by the Finance Minister, while announcing the goal of positioning India as a global hub for millets. Or **GOBARdhan** being announced as a scheme under which 500 new 'waste to wealth' plants would be established. The seven priorities of the Union Government in the Budget—inclusive development, reaching the last mile, infrastructure and investment, unleashing the potential, green growth, youth power, and financial sector, were described as **Saptarishi**, a reference to the wise sages, who would guide the country through to **Amrit Kaal**. The youth of India were referred to as **Amrit Peedhi**; **Panchamrit,** a Sanskrit word used for the five nectar elements, was used to refer to PM Modi's push for net-zero carbon emission by 2070 and the budgets focus on green growth.

Other terms which found resonance were **MISHTI** which means sweetmeats in Bengali, while referring to a scheme for the 'Mangrove Initiative for Shoreline Habitats & Tangible Incomes'. Then we had **Vishwakarma** for the Artisans, the acronym **UDAN** for a scheme to make air travel affordable, another acronym, **SHAKTI** for harnessing coal power, **SAGAR,** reflecting India's vision for the Indian Ocean Region and **USTADD** for upgrading skills training. Other acronyms /phrases which found their way into the budget were **GIAN** for a global academic network and **PRASAD**—Pilgrimage Rejuvenation and Spiritual, Heritage Augmentation Drive— a scheme to facilitate religious tourism through provision of appropriate infrastructure.

Conclusion

The Budget, despite having assiduously shunned populism has still found great resonance because of its focus on an investment led consumption oriented growth strategy. By associating the Budget with our civilisational ethos, there is an attempt to connect with history and heritage to re-define the future.

◆◆◆

The Dangerous Life-Cycle of Currency & the Concept of Money

Ankit Shah*

We are witnessing a moment where humanity has reached a juncture to again question the concept of What is Money and Who can use it. There is a visible clash between three different formats of currencies. The Private Cryptocurrencies backed by blockchain technology, claiming to be a de-centralised version of modernity, current Fiat currencies which began with 1971 unhooking from the Gold Standard, backed by the Central Banks, and a new, multi-polar pegged currency which is in the making process by the BRICS+ nations.

I am forthright ruling out the private cryptocurrencies for the role of legal tender of money usage, as no central bank or polity would allow it. Neither does it makes sense for rational citizens to use it as a store of value or as a stable medium of exchange as there is lack of jurisdiction; what would happen if tomorrow the screen shows zero as its value? A good store of value does not fluctuate so wildly with the words of mouth or news. The Central Bank Digital currencies are being brought in a way to counter private cryptocurrency popularity of modernness.

That leaves my research to confining the analysis between the current fiat currency format, the pegged currency format and the CBDC. It is important to lay some background as to why did we arrive at this stage where a currency needs a reset. Let us begin.

Barter System

Humanity began a peaceful, sustainable living with a simplistic barter system. A barter is a simple exchange of goods and services between two or more person or entities.

Benefits of the Barter System (most of which do not exist today)

A. Only if your product is ready for end-user consumption, you could conduct the barter for another finished product or service in exchange. There was no sense or visibility of unemployment virtually because entire value-addition was done by the individual, family or the community jointly. Entire society was equally empowered. Since the value-chain involved the entire family and community circle, there was never a concentration of huge chunks of wealth in a few hands. In the

*Dr. Ankit Shah is a Fellow Chartered Accountant & a Qualified Company Secretary, and a keen observer of foreign policy & security for the Indian subcontinent. His predictions include many major geo-political events like Doklam, 370-35 A removal, LAC standoff, Balakot, Ukraine & Taiwan conflicts, the De-dollarization process, and so on. He introduces US hegemony as a Two Buckets Theory in his book – GEOPOLITICS - DECODING INTENTS, LIES, NARRATIVES AND FUTURE. He laid out a Chakravartin Bharat 2047 & its Sphere of Influence as a concluding chapter in another recently launched marvel. As a Geo-Economics observer, he is currently working on a Sanatan Economics Model to plug the gaps of Adam Smith's Capitalism and Karl Marx's Communism theories. He has served in IIM-Ahmedabad as an Academic & Research Associate.

contemporary world, the final product or service is built after running through several de-centralised processes amongst unknown entities and individuals, totally disconnected from family or community.

B. There was no massive storage of production to the extent of creating the ability of artificial price manipulation. Most commodities or goods were perishable in nature. There was no over or under production. The society auto-adjusted the output based on their requirements for the barter. In this sense, the region or village was inherently self-sufficient and content. Optimum utilisation of resources meant that the nature's gift of resources was used with the wisdom of minimalism. In the contemporary world, there are widespread manipulations by all actors by weaponisation of over-production and by hoarding. The natural resources stand ruthlessly exploited. The height of extreme capitalism has resulted into speculative trade (derivatives) in the commodities determining the price of the underlying asset (commodity) instead of the physical asset determining the prices of the derivative. The output or production is altered to fix a maximum profitability scenario, irrespective of nature's capacity or human needs.

C. There was complete price stability & almost zero inflation. The barter trade wasn't re-negotiated for over years. The understanding of what many hours of hard work should measure the exchange between the buyer and seller was inherently understood and largely remained non-disputed. There was no requirement of the idea of socialist welfare in an inflation-free society. In the contemporary world, the exploitation of extreme capitalism for profits causes income inequality between the rich and poor. As the by-product of the exploits of 18th century Adam Smith Capitalist-industrialisation, we had Karl Marx communism born, making a fit case for a huge Government format launching communist freebies politics.

D. The national and international trade was smooth. It did not require maintenance of foreign reserves or facing deficits like in the current world. Strong society meant strong governments and hence zero outside interference in the policies of the state. Individual and national sovereignty, both were equally maintained. In the contemporary world, globalisation has entered like a Trojan horse removing the physical security of the borders. It's an open invitation to enemies for all kinds of internal sabotage without requiring a war at the border.

E. There was a very negligible credit-based sales and hence almost zero chance of bad debts. This massively contributed to the social harmony further. In the contemporary world, the West is enabled to pass on their socialist freebies bills with the reserve currency format on the rest of the World. While the East is totally unaware of that fact that these government offerings in the West are actually from their pockets and hence, they admire the western lifestyle out of ignorance. The East does not have a reserve currency endless printing privilege for their Governments to take care of their aged parents or issue entitlement benefits, social benefits, income security, food stamps, low interest loans and so on.

What was the World promised to jump out of the Barter system? We are going to make your life easy & super convenient, and how!

- Bringing a unit of account as your goods are not divisible into units for conducting transaction any point of time.
- Bringing a stable store of value as your goods are perishable in nature.
- Bringing a common measure of value as a tool for trading and universally accepted medium of exchange you can easily carry with you.
- Bringing a standard for deferred payment in case you don't have your goods ready to exchange with something you want to consume right away. It will serve as a basis of credit. You can't grow rich without debts.
- Bringing a fairer payment for your produce as you are not getting good exchange deals beyond a geographical or practical limit.

So, the question now was – **how to shift to coins and paper currencies? How to make people trust these?**

Gold and Silver as precious metals is the real purchasing power accepted worldwide. So, minting the coins made a lot of sense. Faces of Gods, Kings & Queens as an addition made people trust it for usage as currency.

De-monetisation by Monarch: The Kings or the State de-monetised by calling back all the gold and silver coins, and issued cheaper metal coins in return to accumulate wealth. Then, again, they could re-introduce and de-monetise when needed. Today, benefits of physical gold as currency has been lost.

Civilisational wisdom of Gold as the real Purchasing Power

A. Physical Gold is the best store of value for passing wealth over generations and life-cycles as emergency/insurance fund, seed fund for enterprising, for Streedhan and ornamental usage. It is Sanatan wisdom which is why all Indian Bhagwans are laden with gold.

B. Physical gold is the best absorber of inflationary pressures and de-centralised from day-to-day state policy fluctuations.

C. Physical gold has zero political risk, zero geo-political risk, zero default risk, zero counter-party risk, zero liquidity risk and zero convertibility risk.

Conclusion: A Currency Reset only happens by accumulation of gold or silver (De-monetisation from whoever has it physically with them)

Now, if we want a seamless and fair credit system, a middleman will be required, which would save the people from exploitative, unorganised lenders. That gave birth to the formal banking sector. **Welcome to the World of printed notes as currency across the state.**

Interest started being offered on deposits to divert family's enterprising savings and corpus to corporates via banks. This broke the entire entrepreneurship, perpetually rich economy worldwide. The entire chunk of family savings went to companies via banks and the entire society got converted to jobbers. The formation of joint stock company with the support of the state rights to specific trade and business became the norm. Now, these companies wanted to pay lesser to their employees, knowing well that their family savings are all diverted and that they cannot do enterprise. These companies also wanted cheaper loans from the banks. The powerful private banking groups did not listen to the State. Politicians wanted to declare socialist freebies for vote bank as well. This gave birth to the Central Banking system for regulating the banking services nationwide.

There are only two ways to recover the cost of socialist freebies and massive government expenditure: taxes or printing more currency notes to fund that expense. The printing of more notes drives the purchasing power down automatically. This way, without more taxes, the cost of freebies can be recovered without masses knowing about it. More supply by printing of currency notes also means that corporates can continue paying the same amount of salary (with lesser purchasing power which the employees won't understand is a reduction in pay). The Corporates also enjoyed lower interest rate loans from the banks compared to the loans offered in the unorganised banking.

Now you reach the printed paper currency world driven by the Capitalists where printed notes are several times more than the actual physical gold backing it. An era of debt-based lifestyle began.

What was the World promised to jump out of the Precious and Cheap metal coins? We are going to make your life easy & super convenient, and how!

- Bringing a printed note backed by the central bank as a legal tender of money.
- Bringing an easy to carry currency compared to coins in terms of weight.
- Bringing a common measure of value throughout the nation which won't require a third party to convert the precious metal or coins into a different local measure of value.
- Bringing a note which is printed, based on a fixed Gold Standard (pegged currency) and easily convertible to gold as and when you want. If at all you lose faith in the government or our financial systems, walk in with your notes and take back the gold in exchange. We guarantee these notes are safe and backed by the State for a promise to pay the denomination worth mentioned. Please understand that physical gold is very limited in stock and in order to grow the economy, we need to print notes in some proportion to Gold, not equal to the actual physical gold that we hold.

Britain as the global power, imposed the British Pound as the Reserve currency worldwide.

Demonetisation by Capitalism

US started collecting physical gold in exchange of war supplies from the EU allies during the World War. In the Bretton Woods agreement, with the strength of physical gold accumulated, it imposed the US dollar as the new reserve currency replacing the pound. In this formula, the US dollar maintained the Gold Standard, while the rest of the World's currencies were pegged to the US dollar for referencing, valuations and invoicing of all bilateral and multilateral trade. The International busybodies like the UN, World Bank, IMF, WTO and so on, sold the idea of Unipolar dollar (police) World of trade by packaging it as "Globalization".

To counter the anti-religion communist USSR during the Cold War, the words "In God we Trust" were added to the printed dollar. The deep state companies started forming strength in the US by the legacy funding for the few aristocrat families and support from the UK. President JF Kennedy was the first casualty within the US. The military industrial complex was gradually able to take over the polity as the retired army generals took plum postings in deep state companies. These post-retirement temptations lure the currently serving generals to follow the diktats of the deep state companies. While the deep state companies covered several sectors, the top military appointments taking plum postings post retirement in them was the turning point which made it very lethal. For example, you can make out Donald Rumsfeld talking Iraq attack even before being appointed in the government. By the stretching of the Vietnam war, the economy of the US started weakening. Upon losing faith many nations started demanding physical gold in exchange of the US dollar. President Nixon banned the Gold convertibility and the Gold standard on 15th August, 1971. This move made all the currencies of the world fiat, meaning backed by nothing. The concept of Fiat currency was born.

The 1973 Oil for security program with Saudi Arabia and OPEC gave birth to the petrodollar. Both petrodollar recycling air and reserve currency bubble started accumulating in the Dot com by late 1990s. In order to cover up the wall street manipulations from the masses, REG D and the Gramm Leach Bliley Act was introduced to mix commercial and investment banking, so that public deposits are mixed with the reserve currency bubble. EU launched Euro currency in the first ever fiat de-dollarisation attempt (without accumulating or pegging the EURO with physical Gold). Furious with this move, US brought China in WTO and started passing on all the manufacturing from the West. EU retaliated by refusing to park excess in US treasury and pin-pricked the reserve currency balloon accumulated. This collapsed the IT sector valuations by 78% in what came to be known as the Dot Com crash in 2002. The Euro currency eventually managed to win 20% of reserve currency status in the world.

The Services sector was born out of 1971 fiat currency format & the IT sector was born out of the reserve currency status bubble. Both caused artificial suppression of valuations of farming, precious metals and manufacturing sectors worldwide. For example, paper gold floating around today is several times higher than the real physical Gold in the market. Specific few financial entities are playing the manipulation game in the West to curb the value of gold and silver worldwide for 5 decades now, to ensure central banks don't get attracted to accumulate it, just to avoid them from de-dollarization temptations. This is how the West artificially suppresses value of all what Asia and Gulf produces. This artificial suppression of valuations of enterprising MSMEs, SMEs, farming and manufacturing sectors causes inequality of revenues in all countries making a use case for issuing massive socialist freebies by the state.

(Note: What do you expect if Fiat currency formula is killed and de-dollarization is done?

a. Services sector and specifically the IT sector to take a big hit worldwide.
b. Farming, manufacturing & precious metals to zoom in valuations.
c. Too much paper will chase too less physical and cause massive chaos in the West.)

Nothing surprising; Karl Marx's communist theory was born out of 18^{th} century industrial capitalism exploitations. The destruction of farming, precious metals and manufacturing sectors worldwide presented a tempting use case of exploiting the reserve currency status with endlessly printing huge socialist freebies. Politicians were also happy as they got their vote bank served, Capitalists were happy that these socialist freebies broke families, which meant more selling, cheap labor and lesser competition from family-based entrepreneurship.

Where does this cost of socialist freebies go? It takes the form of increased taxes or inflation by printing more notes, as too many notes chase too less goods. The reserve currency status of dollar and EURO passed on the chunk of these costs to the rest of the world as all other nations have to compulsorily do bilateral and multi-lateral trade in consistently sliding purchasing power of both the currencies.

(Note: Humanity was made to jump from the barter system because you were told goods are perishable and not a good store of value. Turns out, you could buy a good suit for 20$ in 1970 and today you hardly buy a good pair of socks with 20$. Whoever heard of this kind of a store of value. You were told it will be a fairer payment for your work. Turns out, salaries increase in absolute numbers, the purchasing power goes down every day. You were told you may not want to buy what the seller produces for a barter to happen. Turns out, you land up paying premium and even taking loans for buying basic things you want.)

For the EU & the US, the debt-based lifestyle accumulated huge mountain of debts. After the 2008 crisis, the US started pushing private cryptocurrencies like Bitcoin aiming to give a back door entry to the dollar in nations if they de-dollarise. The printing of dollars to solve the 2008 crisis at home caused massive inflation worldwide and the food inflation brought down the middle-east governments in the form of Arab spring. This was the time the Middle-East realised the heavy cost of continuing with the reserve currency status of the dollar.

Asia started serious de-dollarization moves with India taking the lead by launching a gold monetisation scheme to channelise domestic gold to coffers by 2015. Russia and China were totally unaware of how fast India was moving. We started cancelling out multilateral trade pacts which are by default dollar based, so that in future we can flip individual Free Trade Agreements when we want to move to any other currency. The RUPAY and UPI will certainly have a first mover advantage in the new world order based on a de-dollarised economy. The US printed trillions of dollars during Covid era and that bounced back as inflation to Americans instead of the world this time. This occurred partly because most nations including allies have stopped parking their excess funds in the US treasuries. The extreme capitalism of the West is now at a juncture of a global currency reset to solve the mountain of debts they have accumulated. US alone sits on a 31 trillion plus debt and has reached the stage where all erstwhile global powers lost their status—the point when debt servicing (interest expense) crosses defence spending. Extreme capitalism is now looking at extreme communism as a solution. The only way out now is to give in to **full-scale**

communism to conduct a regulated collapse with a completely controlled currency regime.

Welcome to the World of Fully-Controlled Central Bank Digital Currency (CBDCs)!

What is being promised to jump out of the Paper currency? We are going to make your life easy & super convenient, and how!

- Bringing an electronic token-based currency to reduce the cost of transactions.
- Bringing an electronic token-based currency to speed up your transactions worldwide.
- Bringing an electronic token-based currency that will increase liquidity in a click. This will let us shut down needless costs of ATM services, Banks' front desk operations clogging, credit-debit cards, private crypto manipulations and other payment methods.
- Bringing an electronic token-based currency which aligns the end user directly with the Central bank and reduces maintenance.

My Concerns about what this Communist money can actually turn out to be -

- Least Safe payment system of all: No country is dynamic and sophisticated enough to handle external cyber sabotages like say data theft or transaction theft.
- Least Inclusive of all: Very doubtful in terms of who could be sanctioned, who could be bailed out and what if the criminal history of someone causes problems to the account, transactions, money or reputation of an innocent user who transacted with him?
- Most prone to manipulations and governmental interventions: What is the future of the masses with a fully controlled currency usage that is tracked 24x7? Can some draconian actions be taken by some future government weaponising this format? Do note that Trudeau administration recently froze some bank accounts of protestors.
- How does it address transactions in areas with lack of electricity and internet?
- While zero interest rates are clarified already on these tokens. What if some government in the future does negative interest rates? Say for example, the salary deposited of Rs. 20,000 in the account is tweaked to Rs. 19,000 applying negative interest rates. At least in the paper currency, people weren't losing the principal amount denominated on the note.
- Least Transparent of all: What if the currency is used to discriminate citizens or community?

Conclusion: The Path Forward for India

Sanatan Economics

An evolved Barter system with full Privacy and Control with the retail end users. This will make Corporate modest and cut the size of the State. It empowers the family and the individual.

- **Retail Users:** Paper currency pegged with commodities like gold and others. Individual citizens need to be made aware of the dangers of completely shifting to a digital currency and legislation should explicitly prohibit cancellation of paper currency at any time in the future.
- **Wholesale and Inter-country Users:** (sections of trade which need scrutiny and does not involve individuals or families or specific communities). Digital currency pegged with commodities like gold and silver.

Extreme Capitalism

It attacks family, community corpus and enterprises, while perpetrating toxic individualism and hyper consumerism. The control of the policy lies with the state, but users still have decent privacy in dealings with the physical possession of the currency notes.

Extreme Communism

It thrives on a bigger State concept to enforce forced equality of outcomes as an excuse for freebies. It attacks the wealth creators, family and the individual. The control lies with the state and the user has no privacy of his dealings.

Demonetisation by Communism

If the physical currency notes are completely removed, this currency format itself will become a tool to establish a communist government. Entry, exit, movement, access, supply and payment can be scrutinised and tampered for each individual. This can become the case of losing all individual sovereignty, human rights of the citizens and even national sovereignty in the worst-case scenario. Historically, extreme Capitalism has always managed to create scenarios for extreme Communism to thrive. The danger is real!

◆◆◆

INTERVIEW

The Union Budget 2023-24:
An Interview with Shri V. Anantha Nageswaran*

Gaurie Dwivedi*

Gaurie Dwivedi: The Economic Survey survey projects a very positive outlook for the Indian economy, especially when viewed in the context of the headwinds which the global economy is facing. In one of your interviews you had stated that the economic survey is actually an annual economic story, so I begin by asking you: In your assessment, what is the India economic story for the next 12 months, 24 months or even beyond?

V. Anantha Nageswaran: The next 12 months story is one of continued economic growth. The momentum set in 2021-22, will continue this financial year. Soon after the Union Budget 2022-23 was presented last year, within a few weeks the conflict in Ukraine broke out and then over the next 4 to 5 months we witnessed commodity prices and oil prices shooting through the roof. But we navigated the impact of the war through government's proactive supply measures, central bank hiking interest rates and by ensuring adequate supply of food and fuel inside the country. The estimate today is that we will grow at about 7% in real terms for the current financial year. That's a very creditable achievement. The only country within G-20 that is going to grow faster than India is Saudi Arabia, which is largely the result of the oil boom. Over the next year, even though the international agencies project a slightly lower growth for India, it will still probably be the fastest growing economy.

India's growth story, I think is about a steady recovery. We have got through the impact of the pandemic and the economy is steadily marching on. We did have a difficult second decade because the financial system, the banking system, overextended itself in the first decade of the millennium. We therefore had to do an adjustment and what I call digestion of the excess credit which the government and the corporate sector had created. The corporate sector had to reduce their balance sheet, sell assets, pay off debt, etc. All that is now behind us. Therefore, I expect the financial cycle and the capital investment cycle to be in our favour. What were headwinds in the last decade is going to turn into tailwinds in this decade. The second reason for my hope and optimism about the Indian economy is the digital transformation of the economy. This took place not just because of the pandemic, but because fortuitously, the building blocks had been put in place well before the pandemic struck. This is also going to propel growth in the country, drawing segments of the population which we had not hitherto included in the formal economy. So, it is the formalisation, financial inclusion facilitated by digitisation and the resumption of the credit and capital investment

**Dr. V. Anantha Nageswaran the Chief Economic Advisor (CEA) in the Ministry of Finance, Govt. of India.*
**Gaurie Dwivedi is a Senior Editor at Economic Times.*

cycle, that is what will drive India's growth not only in the next 12 months but 24 months and beyond as well.

Gaurie Dwivedi: On growth projections, you have spoken off variations of course that typically happen between the finance ministry projections, the economic survey and projections by international agencies. You have also stated that these numbers give us a false sense of precision. But how far off could we be from these numbers and are there any reasons to worry for us to be off this track?

V. Anantha Nageswaran: How far could we be from the numbers that we are projecting for 2023-24? That itself is a question which is difficult to forecast. So, forecasting how far off your forecast will be from reality is also as challenging as making the initial forecast. So, I would not venture into that, but I do give some clues as to where I see the balance of risks lies. When I picked the number of 6.5 % as real GDP growth for 2023-24, deliberately, I gave the range as 6 to 6.8. I could have given the range as 6 to 7 on my baseline of 6.5, but I picked the range of 6 to 6.8, to indicate that the downside risk is higher than the number being exceeded. So, while 6.5 is my base case scenario, it could go all the way down to 6 on the lower side, but on the upper side it could only go up to 6.8. So, I'm adding only 0.3% to the upper end, but adding 0.5% on the lower end of the range, which kind of tells you that I still see challenges and those challenges stem primarily from the global environment. We have no idea of what will happen to the conflict in Ukraine and how that may impact on the price and supply of crude oil. Just last week we saw Russia deciding to cut the oil supply by 500,000 barrels per day! Also, we do not know the speed with which or the smoothness with which Chinese economy will reopen and what kind of demand it will create for commodities. Should the US and European economies avoid a complete economic recession, then it will also add to the demand for fuel, etcetera. Then we need to see how that will impact oil supply and oil prices. So much of the risk that India faces stems from external factors, and those uncertainties are still quite big. So, there are large number of unknown unknowns and that is why I feel while the baseline number is 6.5, I do see downside risk dominating the upside.

Gaurie Dwivedi: Global factors do impact on the level of risks to the economy. Now, if China opens up faster, it grows faster. There will be, accordingly, major spike in commodity prices and so on and so forth. On the other hand, we are looking at probably the global economy reaching its lowest level in terms of growth rates, especially when we view the European market. This will have a direct bearing on our exports and our economy. How do you see that panning out?

V. Anantha Nageswaran: It's a fair question. Obviously, whatever happens in the global economy, whether it is performing better than expected 3-4 months ago or performing worse than expected 3-4 months ago, both will have their own implications for India and those implications will be a mix of good and bad. Ultimately, we have to come to a judgment on balance, whether the good effects dominate the negative effects or vice versa. So, with that framework in mind, I can say that a global economic slowdown will, on balance, be more beneficial to India than a global economy that does better than what we expected a few months ago. And the reasons are yes, you are absolutely right, export growth will be impacted. But remember, India's services sector growth in the developed world is mostly recession proof. Recently, a major IT company executive told me, based on empirical record over the last couple of decades that when the global advanced economies slow down, the demand for IT services from India comes from their need to tighten back-end operations and control costs. When their economies are doing well the need for India's IT enabled services come from their front end wanting to expand their markets and so on. So, whichever way their economies are going, one or the other side of the company's operations seem to be having the need to use Indian IT enabled services. That's a good thing. So, services are reasonably recession proof. And we can verify that with the data as well. Exports of course will be hurt, but set against this, what are the benefits? Global oil demand will come down, imports will be lower, oil price will come down, the central banks in the developed world will stop raising interest rates and may even drop them. So the pressure on the US dollar to appreciate will be less intense, which will provide relief to many emerging economies and currencies, including India. Therefore, investors from developed countries whose economies are slowing will be looking for investment opportunities in countries like India which have a current account deficit. India's need for external financing thus becomes easier to obtain. So, you have these multiple benefits and against that there is a little bit of impact on goods exports. So, I would consider the positives outweighing the negatives of a global slowdown. That is why I will be somewhat relieved to see a world economy doing somewhat less better or somewhat worse than expected.

However, I must say that since the beginning of the year, the feeling is that the European economies have dodged the recession because the winter has been much warmer than expected and gas prices haven't gone up to that extent. Also, the US economy, even with the most recent employment data, seems to be pretty strong. So, at the moment I would say the indications are that the global economy would be performing better than what we thought, let's say in October 2022 when the IMF brought out its World Economic Outlook, but in January the World Economic Update that they provided was a tad better in terms of sentiments and China's reopening and the speed with which the reopening happened was also completely unanticipated. So, we have to wait and see.

Gaurie Dwivedi: So, China is like the X Factor in the equation right now, you know because how far it will grow, how fast it will grow, and also how much will there be, will impact globalisation sentiment. There may or may not be, alternate supply chains, and all of which, of course, will have a direct bearing on the India story and the manufacturing side of it. How do you foresee India's presence in these supply chains that are getting realigned? India's manufacturing has been stuck at about 15 to 16 percent for decades. As the chief economic adviser how do you see these global scenarios pushing that upwards?

V. Anantha Nageswaran: I think this global scenario does provide us an opportunity. I would say India's industrialisation story is not a story of missed opportunities, but it is a story that is still waiting to unfold because I think we never really had the kind of infrastructure that facilitates this manufacturing growth. Now we have that. There is a certain critical mass, whether it is roads, railways, ports, telecom network, digitisation, I think we do have the building blocks that can facilitate a rapid growth in manufacturing. And also, the geopolitical environment is making many companies, even though they may not spell it out very clearly for various reasons, look for opportunities that India provides, both in scale and capacity. Foreign companies are definitely also going to countries like Vietnam, Bangladesh, Mexico etc. but all those countries, being relatively smaller compared to India, will have at some point, limitations in capacity creation, etc. India provides not just a large domestic market for these companies, but also the ability to set up manufacturing at scale. What India is therefore aiming to do is to create local manufacturing capacity at scale to be able to cater to domestic and overseas markets. And that, I think, is a story that can happen and will happen. The entire Production Linked Incentive (PLI) is geared towards making that happen and it is too premature to talk about its success or failure because many of those sectors under the PLI were opened up only in 2021. Therefore, you receive applications in 2022, take time to evaluate, and then you grant them the license approvals and then they go about setting up the capacity and then they start producing and then they start exporting. So, this is not something that's going to happen at the speed with which one can write out a tweet. So, I think the PLI scheme, the national logistics policy and the PM Gatishakti program are all elements of India's manufacturing becoming a force to reckon with in the economy, and I think it's an important policy goal. I am confident that global conditions are also getting aligned with India's goal for its own manufacturing.

Gaurie Dwivedi: And how soon do you see this panning out? Today, some of the building blocks are in place, so infrastructure costs are now going down for companies and power supply too is more stable. What kind of an outlook do you foresee over the next 3 to 5 years.

V. Anantha Nageswaran: I think in the next 3 to 5 years we will see the results of all these policy initiatives. Unfortunately, even as these policy initiatives were being rolled out, we faced shocks caused by the pandemic, followed by the commodity price shock and then the synchronised monetary policy tightening. So naturally, what happens is investors tend to become cautious. They want to re-evaluate in the light of higher cost of capital for them and then in the light of higher commodity prices. They have to factor in the risk element. Say, for example, a ship is blocked in the Suez Canal for two weeks! So, there are many risk elements that have to be factored in. So many of these exogenous factors are external developments of the last 12 to 24 or even longer months, which naturally makes investors cautious and a little bit slower in responding. That is why we sometimes feel a little bit frustrated and concerned that the results are not showing, but once these one off shocks slowly go out of the system, we will begin to see the results of the various policy initiatives meant to push India's manufacturing share higher.

Gaurie Dwivedi: As a policymaker, do you now think that the policy framework is nimble footed, and responding as fast as it can? It's not cast in stone; it wants to attract investments and is responding to markets.

V. Anantha Nageswaran: I think I would say yes to all of those questions, because the intent is very clear whether it is in public pronouncements or actual policy decisions. We have taken decisions to supplement and complement the PLI with the logistics policy 'Gatishakti', which enables government projects to be timely implemented without cost overruns and then a tax policy that allows lower tax rate for new manufacturing established within the country, which has now been extended to cooperatives as well. We had the reduction in the corporate tax rate in September 2019, that allowed the corporates to rebuild their financial health. These are all part of the policy package and they're acting in sync. So, there is quite a bit of clarity and sure footedness in terms of doing our best to achieve these aspirational goals and the creation of public infrastructure by the government when the private sector was still repairing its balance sheet and sort of getting back to good health. All of these things are quite clearly focused on the idea and aspiration of bringing India's manufacturing onto the global stage and plugging India into the global supply chain networks.

Gaurie Dwivedi: When we talk about aspiration, we talk about a 10 trillion-dollar economy. We understand that this cannot be achieved overnight, but those are aspirations that most of India has. Do you share them and do you see us realising the same? Is there a path that you see for that?

V. Anantha Nageswaran: At a personal level, I do not subscribe to this idea of these number-based GDP targets. They are placeholders, but media and several commentators are very focused on these numbers and they try to pin the government to the same. But we know that to achieve a particular level of GDP, it is not just the government policies or efforts or project implementation. It is a whole lot of factors well beyond our control, happening outside our borders that also matter. So, in fact, it is not just a philosophical statement in line with what the Lord said in Bhagavad Gita- "What is in your control is your efforts." So, whatever we must do with the government sector, with the private sector, with households, we will do. But whether they result in a particular GDP outcome this year or next year, depends also on other factors which are beyond our control. But we must keep doing what we have to do. So that is my personal philosophy. But having said that, I think right now in March 2023, we are going to have a GDP level of about USD 3.5 trillion. And just to give you a sense of where we came from - In 1993, our GDP was only around 300 billion dollars and we're talking about 3 .5 trillion dollars now—a tenfold increase in 30 years, in dollar terms. This indicates a growth rate of about 9.1-9.2% per annum in dollar terms, despite the depreciation of the rupee from Rs 30 or 32 to the dollar in 1993 to about Rs 83 to the dollar as at present. So, we have achieved a 9 % annual growth rate in dollar terms. I, in fact, said in my post economic survey press conference interviews or even before that from a 3.5 trillion dollar economy in March 2023, to get to 7 trillion by 2030 March, a 7-year period, is possible because the rule of 72 tells you we need to grow at 10% per annum in dollar terms to get to that number. We have achieved 9% growth in the last 30 years on average and over the next seven years, we could actually see the dollar depreciating against the rupee, because interest rates in the developed world may not go up so much and their inflation rates are not going to be as low as before. So, in real terms their interest rates could be quite low or even negative. And that doesn't make the case for a stronger dollar. So, in fact, if the Indian rupee rather than depreciating, if it were to appreciate, it will happen even faster. So, to talk about 7 trillion dollars by the end of the decade isn't particularly outlandish.

Gaurie Dwivedi: Yes. That's very positive and very good to hear. We have today, the largest population of young people. They need jobs, they need skills and we have to see that the demographic dividend materialises. This can only happen when we have growth engines. As we sort of wrap this conversation, Dr. Nageswaran, what are your concluding thoughts in terms of some of the important initiatives that the government is taking, whether it is in terms of free trade agreements that it is looking to ink, or coming up with newer ideas to look at fresh growth avenues? What do you see as areas as potential and growth inflection points?

V. Anantha Nageswaran: The growth inflection, as I mentioned earlier to your first question I think is going to come from the resumption of the credit and capital investment cycle and the other inflection point for us has been the advancement in digital technology and digitisation of the Indian economy. But the free trade agreements that we are signing are going to help us with our energy security and energy transition and opening up markets for exporters, even though initially some of these free trade agreements may actually result in a widening of the trade deficit because we are going to lower our duties more than they do because we start from a high level of duties. And if you are a country with a trade deficit with the other country with whom you are signing an agreement, the country with the trade deficit will be the one that will give in more and therefore you will initially see imports coming in. But that should not discourage us because eventually you are creating a market, opening a market for India's exporters. So, one of the important things I want to leave for you and your readers is, that we often think in terms of what the government should be doing when it comes to economic growth. But there is plenty that the private sector and households also have to do. I mean skilling and educating our youth is not just the government's responsibility, it is also their own responsibility.

And similarly, the private sector always looks for ease of living, lower taxes, infrastructure, etc. But they also have to invest in R&D and realise the importance of social stability for their own business stability and viability, and therefore they have to strike the right balance between labour and technology on their part, etc. And they have to pay micro and small and medium enterprises on time for the goods that they purchase. So, I think all three segments—the public sector, the private-corporate business sector and the households have to do their part to realise the economic dreams of every Indian.

Gaurie Dwivedi:

Absolutely. And that's how we get to that Atmanirbhar and Amrit Kaal phase that everybody's been the government has been talking about and is pushing. But thank you so much for this conversation, Dr. Nageswaran. It was important to highlight some of those aspects where the Indian economy is growing and we look forward to the next phase, as you said, 7 trillion and more, sooner than probably at the end of the decade.

◆◆◆

The Strategic Culture of China and the Era of Xi Jinping

Priyadarsi Mukherji*

India and China had been having cultural exchanges since several centuries in a relatively peaceful manner simply because Tibet stood in between these two civilisations as a buffer zone. Tibet played the role of a catalyst in bringing about a synergy between the two ancient Asian societies. Despite its geographic proximity with China, Tibet had evolved its distinct identity even before its coming in contact with Buddhism. The Tibetan empire built under King Songtsen Gampo (604-650) brought about geostrategic transformations in terms of its equation with China. The king sent a scholar named Thonmi Sambhota to India in the 7th century CE in order to create a distinct script for the Tibetan language. The written language of Tibetan was constructed on the basis of Gupta script and the Sharda letterings (which is based on Brahmi script), that originated in India. With the advent of Buddhism in Tibet, its physical and spiritual contacts with India increased across the Himalayas. Historically speaking, since time immemorial, Tibet has been the immediate neighbour of India, maintaining an independent entity for centuries. In ancient times, China never ruled over Tibet. In fact, in 763 CE, the Tibetan army under King Tri Songdetsen captured Chang'an (present-day Xi'an), the then capital of the Tang dynasty. Under the influence of Buddhism, Tibet transformed into a peaceful country, eventually becoming the purest repository of the Tantric Buddhist traditions. India maintained its contiguous borders with Tibet. China never shared its borders with India till Tibet stood obliterated from the world-map following the Chinese occupation of Tibet. Yet, India maintains its Indo-Tibetan Border Police (ITBP) force along the northern borders.

In the light of the recent developments in the sphere of India-China relations, one might ponder why the bilateral ties have suddenly reached the nadir. However, as a Sinologist and a pragmatist, I have never been surprised to witness such a deterioration since there has never been an ideal neighbourliness between India and China ever since the Chinese Communist Party (CPC) came to usurp the seat of power in mainland China. Negating history and wilfully seeking to extend its so-called imperial legacy is what the CPC pursued all around its neighbourhood. Its outright dictatorial domestic conduct, no doubt, has been extended to the domain of international relations as well, right from 1949. On the contrary, any move to extend imperial legacy has never been initiated by India unlike China despite India's deep cultural influence—both tangible and intangible heritage—having extended up to Central Asia including the present-day Xinjiang in China, and significantly throughout South-East Asia. The antithesis in myriads of facets, philosophies, worldview etc. between the two countries of India and China have created an impasse in terms of good neighbourliness.

*Prof. Priyadarśī Mukherji is Professor in Chinese & Sinological Studies, JNU, New Delhi.

India under Nehru was overzealous in setting up an "Asian solidarity" with the People's Republic of China (PRC). Thus, India happened to be the first non-socialist country to establish diplomatic relations with the PRC on 01 April 1950. By the end of that year, China invaded Tibet. Nehru meekly accepted China's domination over Tibet. The grand strategy of the CPC followed the age-old Han-Chinese stratagem of annexing the neighbouring regions of non-Chinese ethnicities. China has expanded its territories through centuries with mainly two objectives: One, to capture more resource-rich lands for their profit-oriented ventures towards generating wealth for China, and two, to build a buffer zone around the predominantly Han-Chinese habitats with non-Chinese territories in order to safeguard the Chinese population against any foreign aggression.

The CPC quite conveniently used its army, the so-called People's Liberation Army (PLA) to dislodge the Tibetans from their own land and lay claim over all the regions that were considered having Tibetan cultural influence even along the Indo-Tibetan border. As the PLA had done in East Turkestan (renamed as Xinjiang), similarly, they moved this time to capture the world's highest plateau—the Tibetan plateau— the source of all major rivers and water resources in Asia. Thus, the PLA swiftly turned into a Perfidious Land-grab Army.

India, on the contrary, in its futile effort, repeatedly made mistakes by relying on China over myriads of agreements. The Indian consulates in Lhasa and Kashgar were closed down in early 1950s under hostile circumstances created by China. Yet, Nehru struck conciliatory posture and signed non-aggression pacts, including the *Panchsheel*, which China never followed in words or deeds. Indeed, it was India's failure to secure for Tibet an honourable settlement in terms of sovereignty. Once the Indo-Tibetan border evaporated to become an illegal frontier between India and China, all the peaceful atmosphere across the Himalayas too vanished amidst an unending onslaught from China. Whether physical or cartographic aggression, China brandished brute force in order to extract maximum concessions from a submissive Indian side.

The CPC's disdain for other countries was amply revealed in the daily propaganda of its mouthpiece, '*People's Daily'*, since the very first day of its capturing power in China. The media focus was fully geared to portray China as the most ideal nation on earth while deliberately conducting a smearing campaign against all other countries. It would be relevant to highlight in this context how historically China considered other ethnicities other than the Han-Chinese as barbarians. The non-Han Chinese ethnicities dwelling in the east of China were called *Yi*. They were often referred to as Eastern Barbarians, the non-Chinese tribe living around 2200 BCE. The northern ethnic groups or the Northern Barbarians were called *Di* [pron. Tee]. The Southern Barbarians or savage tribes who lived along the southern fringes of China were called *Man* [pron. Maan]. Ethnic groups in the northwestern regions of China, who were mainly from the Turkic culture, or from the Central Asian regions, were called *Hu*. These were known as nomadic barbarians. Among the barbarians, an ethnic group of northeastern frontier of China, or those inhabiting the southeastern part of southern Mongolia were called

Eastern Barbarians, or *Donghu* [pron. Tung-hu]. The non-Chinese 'man-eating barbarians', called by the Chinese as aboriginal savage tribes, were named as *Shengfan*. One can fathom the degree of self-superiority complex of the Han-Chinese with their ostensible display of civilisational greatness. That complex is being carried on by the Chinese xenophobes and Sino-centric elements to this day even in their academic discourses. The ethnic minorities were time and again sought to be Sinicized and their culture and traditions were eventually assimilated by the Han-Chinese majority. The demographic composition of the non-Chinese regions have been deliberately altered by settling Han-Chinese and thus virtually obliterating the ethnic minorities in their own homeland, all in the name of ushering economic development but actually committing cultural genocide.

Winding the relations fast forward, we arrive at the doorstep of 1980s where we witness the economic reform drive in China under Deng Xiaoping. China embarked on becoming the factory of the world with its labor-intensive growth trajectory in order to capture the centre-stage of the global economy. It was quite evident as my personal observation during my higher studies in China would suggest, that China, through its cheap labor or, in many cases, unpaid labor enforced on prisoners in jail-cum-production units, captured the world market in an unprecedented manner. Then came the era of dumping China-manufactured products in various countries, especially in the Third World. Clearly, such mass dumping by the Chinese practically sought to destroy indigenous products and industry in many parts of the world. The deceitful practices of the Chinese were manifested through their proclaimed adherence to socialism but, on contrary, in their actual pursuance of hardcore capitalism, both internally and externally. Material aggrandisement was adopted to subvert regimes in other countries, and thereafter install dictators with allegiance to Beijing. Such modus operandi was implemented with a certain degree of subtlety at least till 2012.

Mao Zedong, the founder of the People's Republic, was excessively obsessive with an ultra-communist ideological brand, combining Marx, Lenin and Stalin. After his death in 1976, his successor Deng Xiaoping brought an end to the Maoist ideological obsession and advocated a theory, namely "Socialism with Chinese Characteristics" under which the CPC remained a Communist Party solely in name. Deng had literally discarded the Marxist theory in public life, and had rapidly expanded the role of the market in the Chinese domestic economy and embraced a foreign policy that maximised China's participation in a global economic order led by the USA. The CPC, in fact, reinvented itself in the mould of capitalism in order to stay relevant for the sake of remaining in power, and also for abiding with time to extract all the benefits from the liberal world but strike back at an opportune moment. However, practically, CPC could never abandon its genetically feudal mindset embedded in its "civilisational baggage of sanctimonious hypocrisy". Despite being an ideological opponent, the US-led western world, in its penchant for building an anti-Soviet bloc in the East, kept nurturing and pampering the CPC in its vain hope of turning China into a free society like the West.

Then came the era of Xi Jinping as the

president of the PRC. The era of pragmatism, non-ideological governance came to a crashing halt as Xi echoed his diktats that the country might be steering back to its Maoist ideological moorings. Today, Xi controls the party as its General Secretary, the state as its President, and the armed forces as the Chairman of the Central Military Commission. The military strategic culture of China started showing its ugly face under Xi Jinping's wild ambition of establishing himself as the new Hegemonic Emperor of the world through his pet projects of "One Belt, One Road", "Belt and Road Initiative", or even the illegal "China-Pakistan Economic Corridor". China continued resorting to its hidden agenda of enticement and creating debt-traps in the greater part of the world. Sinister designs were invented to internally weaken the countries that did not fall into its trap. China's ever-increasing hunger in terms of exploiting natural resources in every part of the world has enhanced the danger of catastrophes not only on Earth but also in the outer space.

Xi Jinping uses his covert scheme of "Chinese victimhood" and claims avenging Western injustice and prejudices down the line in history. His using the 'victim card' arose from his own experiences as a son of a Communist apparatchik, especially during the 'Cultural Revolution'. In fact, within the CPC, after having ascended the highest echelons of power, Xi is actually playing the victimhood card by developing a negative view of life — both internally and externally. Xi used his "anti-corruption" drive against top leaders, both within the government hierarchy and also outside the public sector, in order to capture the imagination of the common Chinese. He abolished the presidential term limits and incorporated a powerful new agency called the National Supervisory Commission into the Chinese constitution, and used this tool to persecute all those whom he perceived as his political adversaries. He appointed himself as the life-time emperor of China, virtually setting the clock of history upside down. One would recall how Yuan Shikai had become the self-proclaimed emperor of China, though briefly, after the foundation of the Republic in 1912. Sun Yat-sen might have repented having trusted Yuan.

Probably Hu Jintao too might have regretted about why he had chosen Xi Jinping as his successor. At the closing ceremony of the 20th Party Congress of the CPC held in October 2022, Hu Jintao was unceremoniously dragged out of the hall. Xi was apprehensive that Hu might abstain from voting for Xi's continuation in power before the media. Premier Li Keqiang, being the protégé of Hu Jintao, was ousted from the Politburo. The announcement about the new Politburo came just after Hu was taken out of the hall. Xi took no probable risk of facing an agitated Hu who could have expressed annoyance at Li's exclusion. Instead of promoting greater balance and openness within the party, Xi completely undermined the past conventions. He instilled distrust within the party, the state and even within the officers of the armed forces. The whole country is under surveillance through highly sophisticated systems of monitoring each and every person's movements and whereabouts by intruding into one's private life.

Following more or less in the footsteps of Mao Zedong, Xi enshrined "Xi Jinping Thoughts" in the Constitution, in the school curriculum, and even in other walks of life with impunity by virtue of his unbridled power. Deng Xiaoping worked to a great extent in order to tune China up with the pace of the world in the post-Mao era. But Xi scrapped those positive factors and brought China once again, and probably more virulently, in a mode of direct confrontation with the rest of the world. One might be interested to know about Xi's zodiac sign. He was born in 1953, the year of the Snake. It is believed that men of Snake Year combine lofty ideals and inherent strength of action, enabling them to reach the pinnacle of their careers. Their shortcomings lie in their character. They are stubborn, not listening to people's persuasion, suspicious in character, keeping words in heart and not confiding to others, and are complete hedonists.

By the end of 2019, Xi Jinping unleashed a clandestine biological war across the globe. Of course, the initial connivance came from the USA but later it turned out to be a game changer against the western world. All the theories going around the Wuhan virus laboratory leakage, or the accidental spilling of virus in a wet-market in Wuhan, would eventually be proven deliberate fabrications. The actual blueprint of the global pandemic was drawn several years ago after Xi's coming to power. The preliminary ploy was to liquidate the old-age population within China and thereby save financial resources that could have otherwise been expended in pension. Thus, Wuhan became the 'Experimentation Lab'. Later, the lethal viruses of the bio-war was deliberately planted far beyond the borders of China, thus bringing death in almost every part of the world. The secret document referred by me in my earlier article indicates that the export of virus was primarily aimed at annihilating the Whites in the West. Around the same time, when the pandemic raged across the globe, Xi unleashed an entire bunch of Wolf Warriors all over the world to deal with other countries. Wolf Warrior Diplomacy is a style of coercive diplomacy adopted by Chinese diplomats under the Xi Jinping administration. It is an assertive diplomatic tactic that goes as far as insulting or threatening those deemed to violate "China's interests". Xi made use of this tactic in asserting China's unjustified claims over the entire South China Sea or the Indo-Pacific region. Creating and militarising artificial islands, and capturing of shoals, or even naming the illegally occupied isles in the ocean, have been a part of Xi's coercive methods of fabricating a Chinese narrative of supremacy and an "ancestral inheritance" of the high seas.

Amidst the Covid pandemic, Xi Jinping preferred to destroy the India-China relations completely with his aggressively expansionist manoeuvres along the border. Starting right from the communist takeover of China, through various developments of events across seven decades, it is quite apparent that Communist China has never been a friend of India at any point of time in history. China's increasing adherence to the abhorred policy of "Might is Right" has brought disrepute to China and its self-proclaimed 'civilisational superiority'. China's stubborn imposition of its decisions on other countries in the name of preserving its national interests has been witnessed in its usurping the liberal policies in other countries but never conceding anything in return to others within its own jurisdiction. Ludicrously, this is what China terms as "win-win" policy. Nibbling at the borders of India, and initiating the salami-slicing tactics even at the height of pandemic displays the viciously malicious intents of Xi's China.

The Galwan Valley incident with bloodshed on 15 June 2020 was preplanned by the perfidious land-grab Army of China. It was a blood sacrifice offered by the PLA on the birthday of Xi Jinping. The official rhetoric from China kept blaring against India ever since the PLA had unilaterally changed the status quo of exercising control over the areas of domination along the India-China frontier. As a China-watcher, I had already foreseen the violent clashes a week prior to the incident. Greater crudity by ordinary citizens of China was manifested after the unfortunate assassination of the former Japanese premier Shinzo Abe in July 2022, when they celebrated his death. The Chinese, in multifarious ways, also ridiculed India when, during the first few waves of the pandemic, several funeral pyres were seen burning on the ghats of Varanasi. But Indians never derided China for the recent cataclysm brought about due to the sudden relaxation of lockdown in China. This is the civilisational difference between India and China.

Xi Jinping's weakness was reflected through his excessive lockdown policy imposed upon the ordinary citizens across the country in the name of reaching a Zero-Covid level for entire China. He wanted to root out any challenge to his absolute power and authority. China's hardline Covid-19 strategy stoked public frustration, with growing pain around snap lockdowns, lengthy quarantines and mass testing campaigns. Exercising Zero-Covid excesses restricted the public movement outside their home, and thus neutralised any possibility of a popular uprising. Xi made the system completely opaque, and thus inaccessible to both his countrymen and the world beyond. The excessive measures adopted against the commoners in China gave rise to public resentment against China's authoritarianism, and steered the protests ultimately against Xi. Right in the heart of the capital city of Beijing, big banners were displayed with slogans — (1) Say no to Covid test, yes to food. (2) No to lockdown, yes to freedom. (3) No to lies, yes to dignity. (4) No to Cultural Revolution, yes to reform. (5) No to great leader, yes to vote. (6) Don't be a slave, be a citizen. (7) Remove dictator and national traitor Xi Jinping. Lastly, it was inscribed—"Our generation loves freedom.

Similar situation arose in Shanghai and Beijing in 1986 during my student days in China. That was the precursor of the students' protest which culminated with the Tiananmen Square Massacre on 4 June 1989. In those days, the common citizens and even a portion of the press were in support of the students' movement. Their demand for democracy and greater freedom was dubbed as a foreign interference. Then, Deng Xiaoping was the paramount leader. Tanks were brought onto the streets of Beijing. The exact figure of casualty still remains a state secret. Quite analogous to the rolling of battle tanks against its own citizens, this time around July 2022, during the height of pandemic, large-scale protests erupted in many parts of China. Amid a massive bank scam, bank depositors protested against the official decision that impeded them from withdrawing their own money. They demanded the release of frozen funds. Displaying its utter insensitivity, the government rolled out battle tanks to scare the people. Millions of people were summarily terminated from their posts during the pandemic, thus giving rise to unemployment in China.

Communist China has been brutal in handling dissidence across the globe. Very recently, countries woke up to the unpleasant fact that China has been blatantly violating international law by secretly sending their police to at least twenty-five cities in twenty-one countries—setting up more than fifty illegal police stations across five continents to monitor, threaten and terrorise Chinese nationals living overseas. China's illegal deployment of police with covert global network has been operating on foreign soil, primarily in Europe. The clandestine operation by the Chinese police involves physical and mental torture of dissidents outside China, and even forcing them to return to China to face criminal proceedings through a well-coordinated surreptitious network of locating, pressurising, blackmailing, and silencing by making reference of bringing harm to their relatives back in China. This is China's underground overseas police force conducting "long-arm policing and transnational repression." The Chinese government seeks to control its diaspora through illegal methods such as intimidation, harassment, detention or imprisonment of suspects and their families back in China. Their children are even deprived of education as part of a "guilt by association" campaign. The handling of the Uighurs, Kazaks, and other ethnic minorities in East Turkestan (Xinjiang) has been equally ruthless.

Massive violations of human rights, including clandestine business in human organs, have been reported. Yet the western world as well as the Islamic world remain mute spectators just because the Chinese state overtly fills their coffers. Hypocrisy of the recipient countries is glaring.

The diabolic features of Xi Jinping's regime have been manifested in multifarious forms. China's unrelenting ambition of becoming a global superpower by dislodging the USA and turning the world into a unipolar one has pushed humanity to the brink of an impending Yellow Peril that also underlines rampant exploitation of natural resources globally for the sake of China's embellishment. Xi Jinping's malignant and malevolent approach towards relationship with the world, based on sheer muscle and money power is being loathed by most people the world over except some corrupt power-hungry politicians and dictators. Taiwan, which has never been a territory under the CPC, is being threatened with forcible occupation by the communist warmongers of the mainland China.

An unprecedented scale of weaponisation of various countries is taking place, following China's hegemonic expansionism and the consequential response from countries far and near. The USA that nourished and armed the Chinese dictators since the 1970s, is suddenly finding itself vulnerable in the face of China's ever-increasing military might and giant leaps in technological innovations. Unprecedented changes in the global climate pattern has resulted from excessive exploitation of natural resources and wanton denudation of forests, thereby bringing ecological destruction and an overall imbalance in the weather-changing patterns. All such occurrences underscore selfish policies, protectionism and rampant corruption. Fast depletion of energy and subterranean water resources, and exhaustion of financial resources, coupled with rapid draining of human patience are dangerous indicators for a catastrophic future of our global village. Untimely occurrence of torrential rain-causing flash floods, melting of glacier at an alarming rate, resulting in the rise in sea level, endanger the entire biosphere. Due to global interdependence, no nation can thrive for long at the cost of the rest of the world.

A series of antithesis characterises a rather unpleasant coexistence of India and China as neighbours. Across the Himalayan heights, lie the diametrically opposite worldviews or antithetical philosophies of India and China. The Indic philosophy believes in inclusivity, and thus professes the values embedded in *Vasudhaiva Kutumbakam* (the World is one Family). On the contrary, the Chinese philosophy is all about exclusivity, and thus advocates the concept of Middle Kingdom that is "ordained to receive tributes" from the world far and wide, and is "mandated by Heaven" to establish Chinese supremacy in the global arena. Hence the coinage of the Chinese phrase which means "Number One in the World" — thereby reflecting the Chinese aspiration for a worldwide domination. Unlike the Indic worldview of a peaceful coexistence of cultures, the Sinocentric view of the world aggressively seeks to project China's civilizational superiority and Sino-supremacist outlook that is potentially destructive. To my analysis, the Indic faith is *sāttvik* (सात्त्विक), whereas the Chinese faith is *tāmasik* (तामसिक). Correspondingly, India epitomizes *Yang* and China symbolizes *Yin*. With such realities, howsoever unpleasant and with everlasting contradictions, we must learn to live like incompatible neighbours.

◆◆◆

The Sino-Japanese Territorial Dispute

Hossein Ebrahim Khani*

At the southernmost corner of the Japanese archipelago in the East China Sea, a cluster of uninhabited small **islands** is currently a frontline of what might turn into a new hotbed of potential conflict. This group of islands, named "Senkaku" in Japanese and called "Diaoyu" by China consists of five islets and three rock formations with a total cover area of 7 square kilometres located at about equal distance of 170 km from Taiwan and the closest Japanese island in Okinawa Prefecture, and 330 km. from the mainland China. The Islands are currently under Japanese administration, though their sovereignty is contested by both China and Taiwan. This tiny string of islands lies close to significant oil and gas deposits, strategic shipping lanes and rich fishing grounds.

On the issue of sovereignty, Japan holds that the Senkaku Islands are under its valid control and in light of historical facts and based on international law are clearly an integral part of its territory. From 1885, the Government of Japan initiated the surveys of the Senkaku Islands and on 14 January 1895 installed a sovereignty marker and formally incorporated the islands into Japanese territory. In 1932, the Japanese Government revised the status of four islands from state-owned to privately-owned land and sold them to a Japanese family. After World War II and under the 1951 San Francisco Treaty, Japan renounced all its claims to Korea, Formosa (Taiwan), the Pescadores, and the Spratly Islands in the South China Sea. In 1953 the United States was granted formal administrative rights on Okinawa in accordance with Article 3 of the San Francisco Treaty. An important feature of that arrangement was that the United States recognised Japanese "residual sovereignty" over the islands, meaning that at a future date all sovereign powers obtained by the United States were to be returned to Japan. The Senkaku Islands are not explicitly mentioned in the treaty, though there was a tacit understanding that Japan will administer them as a part of Okinawa Prefecture. The Senkaku islands under U.S. trusteeship were returned to Japan in 1971 in compliance with the Okinawa reversion deal. In 1968 Japan began enforcing its Air Defense Identification Zone (ADIZ) on the area covering the Senkuku islands. An ADIZ is a defined area extending beyond national territory in which unidentified aircrafts are liable to be interrogated and, if necessary, intercepted for identification before they cross into sovereign airspace.

In contrast to China's claims to the South China Sea (the so called 'nine-dash line') that was formalised back in 1947, the first official statement of the Chinese Ministry of Foreign Affairs disputing the title over the Senkuku/Diaoyu islands in the East China Sea was issued on 30 December 1971. China claims that the islands have been part of its

*Hossein Ebrahim Khani is Senior Fellow at the Institute of Political and International Studies (IPIS), Tehran, Iran.

territory since ancient times, serving as important fishing grounds administered by the province of Taiwan. According to Beijing, ancient Chinese records dating back to the Ming Dynasty era (1368-1644) mention the islands, while more recent documentation indicates that the islands were incorporated into the Ming and Qing dynasties (1644-1911) maritime defence. Beijing further argues that Taiwan was ceded to Japan vide the Treaty of Shimonoseki in 1895 after the Sino-Japanese war and with Taiwan's return as of implementation of the Treaty of San Francisco, all islands associated with it should have been returned too.

The other claimant, Taiwan (officially Republic of China or R.O.C.) maintains that the islands it refers to as "Diaoyutai" form an inherent territory of Taiwan based on the islands' geographical location, geological structure, historical evidence, usage, and international law. However, Taiwan's position is complicated by the fact that the R.O.C. retreated to Taiwan in 1949 and the People's Republic of China (P.R.C.) was established in the mainland in the same year and has maintained a strict "one China" policy asserting that Taiwan is a part of China, and by the fact that neither the R.O.C. nor the P.R.C. were parties to the 1951 San Francisco Peace Treaty. Although Taiwan and China have made similar claims owing to their shared history, Taiwan has chosen to make its own claims and to pursue a different diplomatic initiative in the face of geopolitical realities as well as the overall interactions with Japan in view of the fact that Tokyo does not officially recognise Taiwan as a sovereign state.

Japan and China normalised their relations in 1972 and concluded their "Peace and Friendship Treaty" in 1978. In the course of the related negotiations, Japan raised the issue of the Senkaku Islands but in the end both parties decided to unofficially shelve the issue so as to avoid negative effect on the otherwise successful outcome of their talks. The Chinese side apparently was keen to avoid raising issues that might have hindered or otherwise put at risk the outcome of bilateral negotiations. China's policy under Deng Xiaoping (1978-1992), was said to be aimed at deferring the dispute and to seek joint exploitation of the area's natural resources with Japan.

China and Japan also disagree on application of the 1982 United Nations Convention on the Law of the Sea (UNCLOS), which both nations have ratified. Article 57 of the convention defines the limitation of exclusive economic zones (EEZs), which are permissible up to 200 nautical miles from the baseline, or to the median line if claims from opposing coasts overlap. Meanwhile, UNCLOS's Article 76 defines the extended continental shelf, permissible to the shorter of the end of the continental shelf or 350 nautical miles from the baseline. Japan, based on UNCLOS proposes the Median line division of the EEZ. China instead insists on the application of UNCLOS, considering the natural prolongation of its continental shelf and its extension as far as the "Okinawa Trough" and beyond 200 nautical miles from the baselines from which the breadth of the territorial sea of China is measured. Thus, the conflicting claims overlap in approximately 81,000 square miles of water.

The dispute between China and Japan reignited into open in September 2012 when the Japanese government announced it was finalising the purchase of three of the contested islands from the private Japanese owner. The move sparked widespread protests in China and counter protests in Japan. The Chinese foreign ministry issued a statement criticising the Japanese Government's decision to nationalise the islands, on the grounds that this has "altered the status quo" and affected China's "inalienable rights" over the islands. Since then, Beijing has taken legal and operational measures to strengthen its own hand, and Chinese maritime surveillance vessels, trawlers and investigation boats have regularly sailed in and out of what Japan considers to be its territorial waters around the islands while the Japanese coast guard is used to escorting Chinese ships inside the island's territorial waters. China's increased naval presence around the Senkaku Islands appears to be a further attempt to demonstrate that Beijing has a degree of 'administrative control' over the islets challenging Japan's de facto administration. Beijing is taking similar steps to bolster additional sovereignty claims in the South China Sea, as it clearly desires to rise as a greater maritime power.

On 23 November 2013, China announced the creation of a new ADIZ in the East China Sea waters facing its coastline overlapping the already enforced Japanese ADIZ. Japan demanded the revocation of the Chinese ADIZ, while the United States declared that it would ignore the zone and refused to comply with any Chinese regulations involving it. Most third countries criticised the Chinese move and expressed their concern about any potential restrictive reading of customary international laws. Noteworthy was that Washington has also refrained from taking a clear position on Chinese legal claims to the Islands, but has stressed on a number of occasions over the years that since the Senkaku Islands are under the administration of Japan, they are ipso facto covered by the 1960 US-Japan Treaty of Mutual Cooperation and Security. The European Union has so far preferred to take a cautious approach and has not expressed its explicit views on the sovereignty of the contested islands. On 25 September 2012 the then E.U. High Representative Catherine Ashton called on all parties to calm the situation in East Asia's maritime areas, using the UN Convention on the Law of the Sea (UNCLOS) and other international rules to resolve disputes.

The island issue highlights the more assertive conduct China has undertaken to eventuate its territorial claims in both the East China Sea and the South China Sea. The issue raises serious questions about sustainable regional security as the Chinese military is fast modernising amid the Obama administration's 2012 "Pivot to East Asia" regional strategy and the increasingly unresilient American posture vis-à-vis Beijing further cemented by President Joe Biden's first phone call to Prime Minister Suga of Japan reiterating Washington's stance of "unwavering commitment to the defence of Japan" that covers the Senkaku islands too.

While the dispute has turned into the most significant geopolitical boiling point and locus of security competition between China and Japan, forcing both sides to lodge regular diplomatic protests, the two countries have so far preferred to handle the situation with utmost care and to avoid measures that could turn the dispute into a hot conflict. Tokyo, with better standing in legal and logical arguments, does not seem to be eager to stir up differences with its biggest trading partner while China, in the face of the many other territorial disputes at its immediate and extended neighbourhood, and also the current tough diplomatic and trade battle with the U.S., does not wish to pick an extra challenge with another power, at least, for the time being. The stalled Ukraine war and Russia's unexpected poor performance in military, diplomatic, economic and public opinion fronts that has compromised Moscow's superpower status, alongside the evident unified resolve of the west to counter major adversaries might have left their impact on the mindset of Chinese leaders with the result of a more cautious Chinese pursuit of risky territorial claims in a transforming global environment.

◆◆◆