

Modi Govt's Economic & Social Reforms?

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INTRODUCTION

- Make two points about reforms:
- 1) Put reforms of last two years in historical perspective
 - From perspective of personal involvement in reforms within govt over 20 yrs from 1988 to 2009
- 2) Highlight some areas of concern, and how to address them- **tax reform**

Two years of reforms

- Most significant set of reforms since the 1990s.
 - If the commitment to & spirit of reforms is maintained, could be more significant than 1990 reforms
- Three things stand out
 - Change in philosophy
 - Change in approach (policy & institutions),
 - Change in Openness to information/knowledge/expertise

1. Change in philosophy

- Change from Communist-Socialist => Market economy & modern welfare democracy
- Key elements are, the
 - Creation of a competitive market economy
 - Govt provision of higher quality Public goods
 - Physical, digital
 - Better, more modern regulations & regulatory system
 - for externalities & information asymmetries: **Incomplete**
 - Efficient well targeted welfare transfers to & focus on improving the Ease of living(EOL) of lower 2/3rd

2. Change In Approach

- Change in **Policy** approach : Director to Facilitator
- Comprehensive, Systematic effort to reform/liberalize
 - Production & services sectors; e.g. Agriculture, Space, AE, BPO-WFH, drones, geo-mapping , infrastructure.
 - Factor markets: IBC, labor codes, Bad Bank,
 - Public sector (PSE privatization, monetization, PPP)
- **Institutional** reform to complement policy change
 - Access to & quality of, Public Services
 - EORC/EODB, CODB (eg logistics-Gati shakti)
 - Legal, judicial reform

3. Openness to info

- Openness to information & accumulated knowledge of stake holders;
- Consultation with producers, job creators, wealth creators, in every sector/industry
- Openness to advise for faster, inclusive, sustained growth
- Macro-economic knowledge gap, remains to be filled

Underlying Vision

- Entrepreneurship as Wealth/Job creator
 - Key role for Tech Startups
- Science & technology: Driver of Productivity
- Digital Economy
 - Critical for inclusive growth
- Classic Public Health issues
 - Swach Bharat (Water, sanitation & sewage)
- Green Economy
 - Future

Areas of concern

- Epidemic: Negative impact on informal sector
 - Sharp decline in contact services due to infection fears
 - MSMEs in retail trade, street food
 - Income/wages, Jobs, affected
 - Pvt Consumption not-recovered, Cons expectation down
- Much is temporary, & will reverse
- Some may persist if not countered.
- Would accentuate earlier decline in informal sector share, due to purge of black money from system

Economy: MSMEs

- Need to ensure that modern, productive MSMEs have full opportunity to compete with corporate sector
 - => Must level playing field with corporate sector
- MSMEs are critical to inclusive growth, jobs & income distribution
 - => Ensure MSMEs do not suffer from policy related disadvantage
 - => Reduce regulatory burden & cost of doing business
- Best way to is through tax reform: GST, DTC, Customs

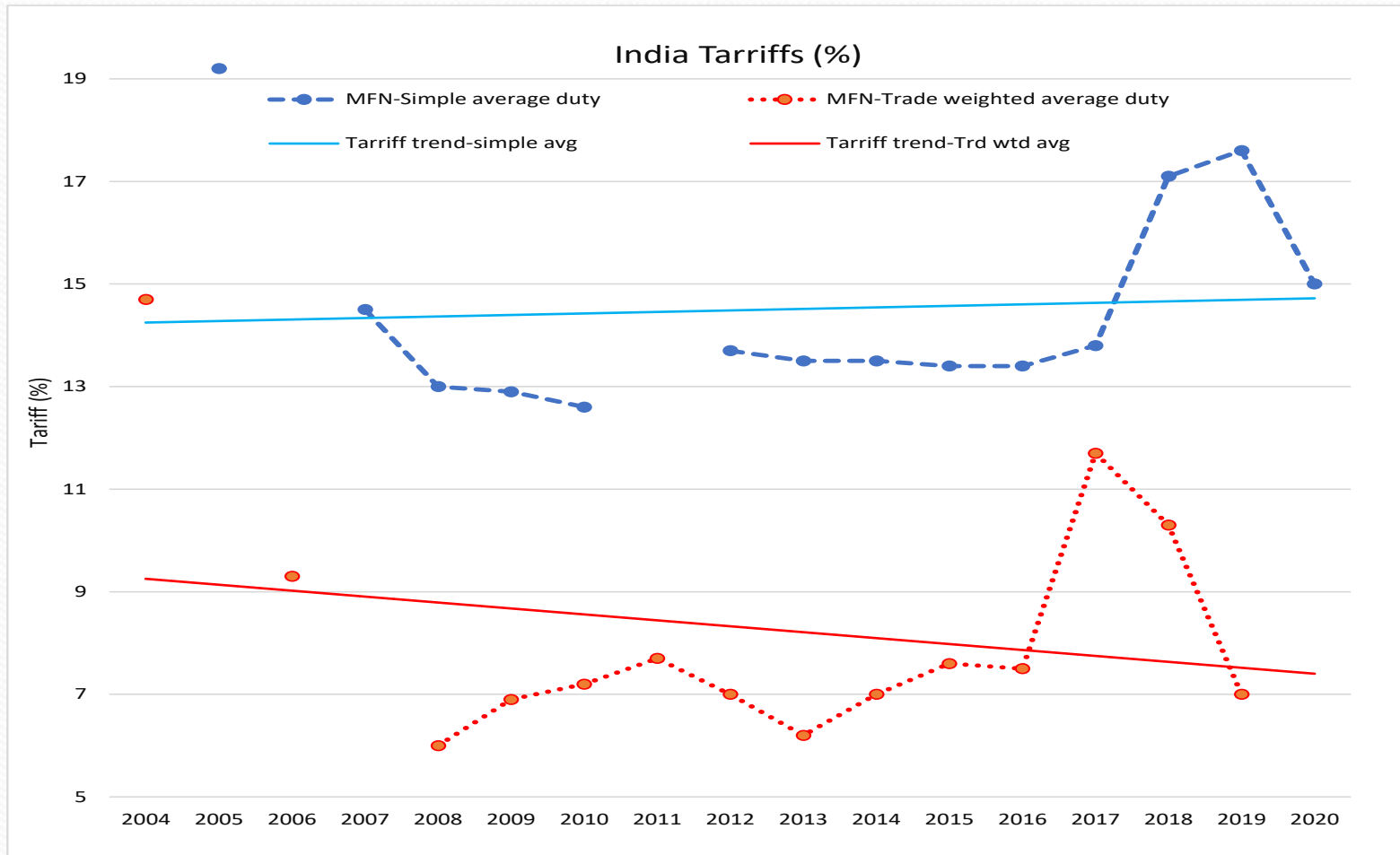
GST: Revenues vs Reform

- GST council seems focused on short term revenue maximization: Insufficient attention
 1. Long term efficiency & revenue buoyancy.
 2. Current macro conditions: Decline in Pvt Cons
- Revenue negative GST simplification, needed to
 - Provide Consumption stimulus to economy,
 - Quickly restore lost Jobs and wages
- Rate structure & cess
 - 15% on $\frac{3}{4}$ of G&S; No cesses
 - Exemption ($\frac{1}{8}$): Basic Food, health services, Schooling
 - 25% on $\frac{1}{8}$ G&S, cess on autos, tobacco prds only

Pending Tax reform: Customs

- Too many tariff rates
 - Textile sector has 10-15 specific rates
- Dispersion of rates is too high
- Average simple tariffs have risen by 2% pts from low of 13% in 2008 to 15% in 2020 (WTO data - fig below)
- Reduce number & dispersion of tariff rates
- Lower average rate by to 14%(2021) & to 13%(2022)
- This will Increase Job creation & wage growth
 - Labor intensive manufactured exports

India's Average tariffs: 2004-20



Direct Tax Reform (DTC)

- Outdated act with Ad-Hoc amendments over 50 yrs
 - Riddled with sections, sub-sections & provisos
- DTC reform: Simplify with
 - Economically rational definitions
 - Global best practice (pragmatic)
- Enhance MSME competitiveness
 - By reducing Cost of Doing business (CODB)
 - Leveling playing field wrt Corporates
 - Post-corporate tax reform (sept 2019)
- Use 2009 printed version of new DTC

Other tax reform

- National Carbon Tax
 - Internationally agreed minimum level
 - Replace cesses and higher taxes(>25%) on petrol, diesel with carbon tax
- Market for carbon credits: Create national, global
 - Link water & energy conservation, product recycling, low carbon product subsidies, to this market

Conclusion: Reforms & Growth

- Primary Goal: Re-accelerating GDP growth
- Major (“Big bang”) reforms in process
- Must complete remaining reforms
 - Maximize geo-economic opportunity (supply chains)
 - Minimize risk from slower world Gdp gr (from 2023)
- Projected GDP growth
 - FY22: 10% +/-1%;
 - FY21-FY30(avg): 7.5% +/-0.5%

Appendix: Corporate Tax

- Excellent CIT reform, has NOT been followed by equally radical GST, DTC & import tariff reform!
- Corporate tax reform of September 2019, which initiated big bang reforms.
 - World data shows a Laffer curve effect at ~22-23%.
 - Revenue neutral reform: Eliminating all exemptions & deductions & reducing rate to 25%
 - 15% - small temp incentive for manf. (NICs experience)
 - Reduction of CIT revenue during Pandemic does NOT prove revenue negativity!

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- Papers on growth in India & lessons from others: <https://sites.google.com/site/drarvindvirmani/growth>