

## **Budget 2012: Excise, service tax rates headed up as RBI makes it precondition for monetary easing**

Policymakers have begun talks on raising indirect taxes and withdrawing the last remnants of the 2008 stimulus, as the government comes under fire for not tackling the rising fiscal deficit.

"There is a thinking within some sections in the finance ministry as well as other senior policymakers that the budget needs to send strong signals on fiscal prudence; hikes in excise duty and service tax rates are under consideration," said a government official.

The official said a two percentage point increase in both excise duty and service tax, which would take the Cenvat and service tax rates to 12%, was being considered though a final decision would be taken at the highest political level.

The government had cut excise duties and service tax rates in 2008 as part of a stimulus package to tackle the global economic slowdown. While some of these cuts were partially rolled back in last year's budget, the ballooning subsidy bill and lower-than-expected revenue collections have resulted in government overshooting its deficit target for 2011-12 by a wide margin.

The Reserve Bank of India has made fiscal consolidation a pre-condition for monetary easing and the head of the Prime minister's economic advisory panel has also called for indirect taxes to be restored to their 2008 levels. "In the wake of international financial crisis, we brought down the indirect tax rates to provide a stimulus. We don't have that space anymore. Therefore, we should go back to the rates that prevailed before the financial crisis," said C Rangarajan, chairman of the Prime Minister's Economic Advisory Council, in an interview with ET in December.

But some experts question the wisdom of hiking excise and services tax rates at a time when growth has slowed down again, and say the government should focus on reducing its expenditure. "Signal is required on expenditure side as industry is only beginning to recover...What they need is a credible fiscal consolidation plan," said D K Joshi, chief economist, Crisil.

The fiscal stimulus measures had pushed the deficit to a 16-year high of 6.8% in 2009-10. The government managed to bring it down to 4.7% in 2010-11, following the over Rs 1 lakh crore bonanza from 3G and broadband auctions. But the government will miss its 4.6% fiscal deficit target in 2011-12, and with the food security bill and large social sector schemes on the anvil, the next financial year, too, will pose challenges for the government's fiscal managers.

The government had cut the Cenvat rate, or the median excise duty rate levied on nearly 90% of goods manufactured, to 10% from 14% in December 2008 and by another 2 percentage points to 8% in the interim budget in February 2009. The service tax rate was cut to 10% from 12%. In the 2010-11, the Cenvat rate was raised to 10%, but the rates were left unchanged in last year's budget.

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