

## ● THROUGH THE LOOKING GLASS

THE NOTIONAL 'SAVING' OF ~₹1 LAKH CRORE ON THE FISCAL DEFICIT FRONT OFFERS THE GOVT AN OPPORTUNITY TO, AMONG OTHER THINGS, CREATE A FUND TO DEAL WITH CLIMATE CHANGE

# Sequestering the fiscal bounty

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**F**Y22 HAS BEEN volatile, to say the least. Budget FY22 was presented on February 1, 2021, at a time when the first wave of Covid-19 was firmly behind us. However, soon thereafter, in March and April, India saw another wave leading to another round of lockdowns and dip in economic activity. This also led to increasing the tenure of support for people on many dimensions, including food, etc. With the fantastic roll-out of vaccinations over the last few months, more than three-in-five people in the country have been fully vaccinated leading to a steady pick-up in economic activity. We now have the Omicron variant which many fear could lead to a third wave. All these gyrations have left a mark on public finances.

### A rare, large fiscal space

In a significant act, by pushing the limits of the Fiscal Responsibility and Budget Management (FRBM) Act, the government dramatically eased the fiscal constraints. In an article in March 2021 ([bit.ly/33mVwxG](https://bit.ly/33mVwxG)), we had noted that the relaxation could amount to a cumulative stimulus, over five years, of \$550 billion (or ₹40 lakh crore). A large part of that stimulus was front-loaded: almost ₹11 lakh crore of fiscal stimulus was earmarked for FY22.

The budget estimated that the central government could have a fiscal deficit of ₹15.1 lakh crore on a GDP base of ₹222.9 lakh crore, or 6.8% of the estimated GDP. As things stand now, the expectation that analysts are baking in for FY2022 is that the fiscal deficit may end up in the ₹13.5 lakh crore to ₹14 lakh crore range. There could possibly be some upside in the estimate of GDP

itself allowing the government a higher fiscal space. The "consensus" numbers are now closer to 6-6.2% of fiscal deficit-to-GDP ratio.

Most credit rating agencies and analysts focus on the fiscal deficit-to-GDP ratio and not the absolute amounts. Every year around the Budget, even a decimal point of miss on the expected fiscal deficit-to-GDP ratio generates significant commentary and excitement. It

is rare that India ends up with as large a fiscal space as this.

The notional 'saving' for the government is the gap between (a) the commitment made in the Budget (₹15.1 lakh crore) and (b) where the fiscal deficit ends up (conservatively, ₹14 lakh crore). This is a gap of, say, ₹1 lakh crore, even after accounting for buffers and last-minute surprises, not the least of which could be

contingency planning in case there is a third wave.

### How to use ₹1 lakh crore?

There are many ways in which the fiscal space can be used. The easiest options will be (a) reduction in accumulating debt, (b) lowering taxes, or (c) increasing revenue expenditure. Given that the pandemic meant a large increase in the government's debt-to-GDP ratio over the last couple of years, having a lower

fiscal deficit this year can ease the pressure on this ratio. The fiscal space can be used on the revenue side—for example, taxes on fuels were slashed substantially. This amount can be used to relax taxes further, say on the direct taxes side for individuals or corporate. Alternatively, this amount can be used for enhancing revenue expenditure, say for key government projects like Namami Gange or PM Awas Yojana or for schemes like MGNREGA or food subsidy—this will be continuation of the fiscal stimulus/support that started with the pandemic.

An alternative is to sequester away the fiscal space for long-term investment: use ₹1 lakh crore to create a fund specifically to deal with matters relating to climate change.

### Use greenbacks for green

India has made deep commitments to climate change at COP26. With the ambitious goal of 500 GW of renewable energy and the 2070 target of Net-Zero, India needs to channelise investments in green. There are various estimates of the amounts of investment that India needs to do for its transition: the IFC estimates that India will need to invest \$3.1 trillion (~₹230 lakh crore) between 2018 to 2030 in climate-smart investments.

The developed world has been

unable to agree on the \$100 billion per year mobilisation for climate mitigation and adaptation. It is possible that this will fall in place over the next few years. In any case, a large part of such mobilisation is expected to be commercial debt and equity commitments. Ideally, a significant portion of such mobilisation should have been grants and technology transfer.

Since the global route on creating 'impact capital' appears distant, India can create a significant pool of such capital on its own using the fiscal space currently available. Such a pool of capital can help crowdsource private investments into newer (and currently more costly technologies) like offshore wind, green hydrogen, battery or pumped storage, smart grids, etc.

Impact capital can be of various types:

- (1) 'first-loss' capital which absorbs losses on a portfolio of (risky) investments,
- (2) guarantees for performance for an underlying portfolio,
- (3) 'confidence capital' which can help source more funding bilaterally from other governments or multilateral development banks, or (4) creation of certainty on raw material supply (say, lithium for the battery industry), or (5) pay-out under schemes like Production Linked Incentives (PLIs), etc.

The creation of 'impact capital' can boost India's transition to green. By definition, only a small amount of impact capital can crowdsource very large multiples of private capital. Backing up the impact capital with appropriate policy and regulatory changes can create a (climate) green revolution in India! India must use the funds now available from the pandemic to fight another humanitarian crisis.

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