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# IMPORTANCE AND ROLE OF FISCAL POLICY IN ECONOMIC DEVELOPMENT IN INDIA- ITS ADVANTAGES AND DISADVANTAGES

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**ABSTRACT :**


*The economy does not always work smoothly. There often occurs fluctuations in the level of economic activities. At times the economy finds itself in the grip of recession when levels of national income, output and employment are far below their full potential levels. During recession, there is a lot of idle or unutilized productive capacity, that is, available machines and factories are not working to their full capacities. As a result, unemployment of labour increases along with the existence of excess capital stock. On the other hand, at times the economy is 'over heated' which means inflation (i.e. rising prices) occurs in the economy. Thus, in a free market economy there is a lot of economic instability. The classical economists believed that an automatic mechanism works to restore stability in the economy, recession would cure itself and inflation will be automatically controlled.*

**KEYWORDS :** *output and employment , automatic mechanism.*

## INTRODUCTION:

Macro economic policy refers to the instrument by which a government tries to regulate or modify the economic affairs of the country in keeping with certain objectives. In other words, it "attempts to assess the behaviour of the economy as a whole and to seek ways in which its aggregate performance might be improved". These are achieved through certain tools of macro economic policy. According to Keynes, Monetary policy was ineffective to lift the economy out of depression. He underscored the job of monetary strategy as a viable instrument of settling the economy. Notwithstanding, in perspective on the cutting edge market analysts both financial and money related approaches assume a helpful job in balancing out the economy.

Monetary policy is conducted by the central bank of a country. Fiscal policy is conducted by the Executive and legislative branches of the government and deals with managing a nation's budget. Monetary and fiscal policies are generally thought of as demand management policies. The purpose of monetary and fiscal policy, taken together is to maintain demand roughly equal to supply in the economy and to maintain the existing price level. The appearance of excess demand will probably cause inflation, while an insufficiency of demand will bring at least temporary unemployment and deflation.

### *Fiscal Policy*

The most important instrument of government intervention in the economy today is that of fiscal or budgetary policy. Fiscal policy refers to the taxation, expenditure and borrowing by the government. The economists now hold the government intervention through fiscal policy is essential in the matter of overcoming recession or inflation as well as of promoting and accelerating economic growth.

***Meaning:-***

The fiscal policy is concerned with the raising of government revenue and incurring of government expenditure. The government frames a policy called budgetary policy or fiscal policy. So, the fiscal policy is concerned with government expenditure and government revenue. Fiscal policy has to decide on the size and pattern of flow of expenditure from the government to the economy and from the economy back to the government.

***Definitions:-***

According to ***J.M. Culbertson,*** "By fiscal policy we refer to government actions affecting its receipts and expenditures which we ordinarily takes as measured by the government's net receipts, its surplus or deficit." The Government may offset undesirable variations in private consumption and investment by anti-cyclical variations of public expenditures and taxes.

***Arthur smithies*** defines fiscal policy as "a policy under which the government uses its expenditure and revenue programmes to produce desirable effects and avoid undesirable effects on the national income, production and employment." Though the ultimate aim of fiscal policy is the long run stabilisation of the economy, yet it can only be achieved by moderating short run economic fluctuations.

***Otto Eckstein*** defines fiscal policy as "Changes in taxes and expenditures which aim at short run goals of full employment and price -level stability."

***Objectives of Fiscal Policy***

The importance of fiscal policy is high in underdeveloped countries. The state has to play active and important role. In a democratic society direct methods are not approved. So, the government has to depend on indirect methods of regulations. In this way, fiscal policy is a powerful weapon in the hands of government by means of which it can achieve the objectives of development. The principle objectives of fiscal policy are given below :-

***1. Development by Effective Mobilisation of Resources:-***

The principal objective of fiscal policy is to ensure rapid economic growth and development. This objective of economic growth and development can be achieved by Mobilisation of Financial Resources.

***2. Efficient Allocation of Financial Resources :-***

The central and state governments have tried to make efficient allocation of financial resources. These resources are allocated for development activities which includes expenditure on railways, infrastructure, etc. While non-development activities includes expenditure on defence, interest payments, subsidies, etc.

***3. Reduction in Inequalities of Income and Wealth:-***

Fiscal policy aims at achieving equity or social justice by reducing income inequalities among different sections of the society. The direct taxes such as income tax are charged more on the rich people as compared to lower income groups. Indirect taxes are also more in the case of semi-luxury and luxury items, which are mostly consumed by the upper middle class and the upper class.

***4. Price Stability and Control of Inflation:-***

One of the main objective of fiscal policy is to control inflation and stabilize price. Therefore, the government always aims to control the inflation by reducing fiscal deficits, introducing tax savings schemes, productive use of financial resources, etc.

***5. Employment Generation:-***

The government is making every possible effort to increase employment in the country through effective fiscal measure. Investment in infrastructure has resulted in direct and indirect employment. Lower taxes and duties on small-scale industrial (SSI) units encourage more investment and consequently generates more employment.

***6. Balanced Regional Development :-***

Another main objective of the fiscal policy is to bring about a balanced regional development. There are various incentives from the government for setting up projects in backward areas such as cash subsidy, concession in taxes and duties in the form of tax holidays, finance at concessional interest rates, etc.

***7. Capital Formation***

The objective of fiscal policy is to increase the rate of capital formation so as to accelerate the rate of economic growth. An underdeveloped country is trapped in vicious circle of poverty mainly on account of capital deficiency. In order to increase the rate of capital formation, the fiscal policy must be efficiently designed to encourage savings and discourage and reduce spending.

***8. Increasing National Income***

The fiscal policy aims to increase the national income of a country. This is because fiscal policy facilitates the capital formation. This results in economic growth, which in turn increases the GDP, per capita income and national income of the country.

***9. Development of Infrastructure***

Government has placed emphasis on the infrastructure development for the purpose of achieving economic growth. The fiscal policy measure such as taxation generates revenue to the government. A part of the government's revenue is invested in the infrastructure development. Due to this, all sectors of the economy get a boost.

***Role of Fiscal Policy in Economic Development:-***

One of the important goals of fiscal policy formulated by the Government of India is to attain rapid economic development of the country.

**To attain such economic development in the country, the fiscal policy of the country has adopted following two objectives:-**

1. To raise the rate of productive investment of both public and private sector of the country.
2. To enhance the marginal and average rates of savings for mobilising adequate financial resources for making .investment in public and private sectors of the economy.

The fiscal policy of the country is trying to attain both these two objectives during the plan periods.

***Merits or Advantages of Fiscal Policy of India:***

Following are some of the important merits or advantages of fiscal policy of Government of India:-

***(i) Capital Formation:-***

Financial approach of the nation has been assuming an essential job in raising the rate of capital development in the nation both in its open and private divisions. The gross local capital development as percent of GDP in India expanded from 8.4 percent in 1950-51 to 19.9 percent in 1980-81 and after that to 39.1 percent in 2007-08. Hence, it has made a positive effect on people in general and private division speculation of the nation.

***(ii) Mobilisation of Resources:-***

Financial strategy of the nation has been assembling significant measure of assets through tax collection, open obligation and so forth to back its different formative activities. The degree of interior asset assembly to fund plan expanded significantly from 70 percent in 1965-66 to around 90 percent in 1997-98.

***(iii) Incentives to Savings:-***

The financial strategy of the nation has been giving different motivating forces to raise the reserve funds rate both in family unit and corporate segment through different budgetary approach changes, viz., charge exception, charge concession and so forth. The sparing rate expanded from a negligible 8.6 percent in 1950-51 to 37.7 percent in 2007-08.

***(iv) Inducement to Private Sector:-***

Private part of the nation has been getting important affectation from the financial strategy .of the nation to grow its exercises. Duty concessions, charge exceptions, sponsorships and so forth joined in the financial plans have been giving sufficient impetuses to the private segment units occupied with industry, framework and fare segment of the nation.

***(v) Reduction of Inequality:-***

Monetary strategy of the nation has been making steady undertaking to decrease the disparity in the appropriation of pay and riches. Dynamic duties on salary and riches charge exception, appropriations, concede and so forth are attempting to diminish such disparity. Besides, the monetary strategy is additionally endeavoring to decrease the local abberations through its different budgetary strategies.

***(vi) Export Promotion:-***

The Fiscal approach of the Government has been making steady undertaking to advance fare through its different budgetary strategy as concessions, appropriations and so forth. Subsequently, the development rate of fare has expanded from an insignificant 4.6 percent in 1960-61 to 10.4 percent in 1996-97.

***(vii) Alleviation of Poverty and Unemployment:-***

Another critical value of Indian financial strategy is that it is trying to lighten destitution and joblessness issue through its different neediness destruction and business age programs, as, IRDP, JRY, PMRY, SJSRY, EAS, NREGA and so on.

***Shortcomings of Fiscal Policy in India:-***

***(i) Instability:-***

Monetary arrangement of the nation has neglected to achieve soundness on different fronts. Developing volume of deficiency financing has made the issue of inflationary ascent in value level. Disequilibrium in its parity of installments has additionally influenced the outside soundness of the nation.

***(ii) Defective Tax Structure:-***

Financial approach has additionally neglected to give a reasonable assessment structure to the nation. Assessment structure has neglected to raise the profitability of direct charges and the nation has been depending much on backhanded expenses. In this way, the duty structure has turned out to be troublesome to poor people.

***(iii) Inflation:-***

Monetary approach of the nation has neglected to contain the inflationary ascent in value level. Expanding volume of open consumption on non-formative heads and shortfall financing has brought about interest pull swelling. Higher rate of backhanded tax assessment has likewise brought about cost-push swelling.

***(iv) Negative Return of the Public Sector:-***

The negative profit for capital put resources into the open division units has turned into a major issue for the Government of India. Regardless of having a tremendous absolute speculation to the degree of Rs 4,21,089 crore in 2007 on PSUs the arrival on venture has remained for the most part negative or lower.

***(v) Growing Inequality:-***

Financial arrangement of the nation has neglected to contain the developing disparity in the appropriation of pay and riches all through the nation. Developing pattern of tax avoidance has made the expense hardware inadequate for the reason. Developing dependence on circuitous charges has made the expense structure backward.

***Techniques of Fiscal Policy:-***

***(i) Policy of Taxation of Government of India:-***

One of the important sources of revenue of the Government of India is the tax revenue. Both the direct and indirect taxes are being levied by the Government of India. Direct taxes are progressive by nature and most of indirect taxes are regressive in nature. Taxation plays an important role in mobilising resources for plan.

***(ii) Public Expenditure Policy of Government of India:-***

Public expenditure is playing an important role in the economic development of a country like India. With increase in responsibilities of the government and with the increasing participation of government in economic activities of the country, the volume of public expenditure in a highly populated country like India is increasing at a galloping rate. In 1992-93, the public expenditure as percentage of GDP was around 30 per cent.

***(iii) Policy of Deficit Financing of Government of India:-***

Following the policy of deficit financing as introduced by J.M. Keynes, the Government of India has been adopting the policy for financing its developmental plans since its inception. The deficit financing in India indicates taking loan by the Government from the Reserve Bank of India in the form of issuing fresh dose of currency.

Considering the low level of income, low rate of savings and capital formation, the Government is taking recourse to deficit financing in increasing proportion. Deficit financing is a kind of forced savings.

***(iv) Public Debt Policy of the Government of India:-***

As the taxation has got its limit in a poor country like India due to poor taxable capacity of the people, thus the Government is taking recourse to public debt for financing its developmental expenditure. In the post-independence period, the Central Government has been raising a good amount of public debt regularly in order to mobilise a huge amount of resources for meeting its developmental expenditure. Total public debt of the Central Government includes internal debt and external debt.

***Measures of Fiscal Policy Reforms:-***

The Government of India has presented a few financial strategy changes which comprise the principle premise of the adjustment arrangement of the nation. Following are a portion of the critical proportions of financial arrangement changes embraced by the Government of India lately:

***(i) Reduction of Rates of Direct Taxes:-***

The pinnacle rate of pay charge was diminished to 30 percent in 1997-98 spending plan. This has brought about an expansion in the offer of direct charges in all out income of the nation from 19 percent in 1990-91 to around 61 percent in 2008-09.

***(ii) Fall in the volume of Government Expenditure:-***

A few measures were embraced as of late by the legislature. In like manner, all out consumption of the Government under different heads has been decreased. Thus, all out open consumption as percent of GDP has declined from 19.7 percent of GDP in 1990-91 to 16.9 percent in 2008-09.

***(iii) Reduction in the Volume of Subsidies:-***

Focal Government has been making tremendous installments as appropriations, i.e., nourishment sponsorships, manure endowments, send out sponsorships and so on. Steps have been taken to diminish these sponsorships in a staged way.

***(iv) Reduction in Fiscal Deficit:-***

The Central Government has been attempting truly to contain the financial deficiency in its yearly spending plan. In like manner, it has decreased the degree of monetary deficiency from 7.7 percent of GDP in 1990-91 to 6.1 percent in 2008-09. Be that as it may, monetary adjustment requires containing the financial shortage at any rate to 3 percent of GDP.

***(v) Reduction in Public Debt:-***

As of late, the Central Government has been endeavoring to diminish the weight of open obligation. Likewise, the outside obligation as percent of GDP which was 5.4 percent in 1990-91 step by step declined to 4.9 percent in 2008-09. The inward obligation as percent of GDP has declined from 48.6 percent in 1990-91 to 37.9 percent in 2008-09.

So also, the all out extraordinary credit or liabilities as percent of GDP additionally declined from 63.0 percent in 2003-04 to 58.9 percent in 2008-09.

***Suggestions for Necessary Reforms in Fiscal Policy:-***

***(i) Progressive Taxes:-***

The assessment structure of the nation should endeavor to imbue increasingly dynamic components with the goal that it can put overwhelming weight on the rich and less weight on poor people. Important changes ought to be made in regard of water system charge, deals charge, extract obligation, land income, property charges and so forth.

***(ii) Agricultural Taxation:-***

The assessment net of the nation ought to be reached out to the farming part to rap a gigantic measure of income from the rich agriculturists.

***(iii) Broad-based Tax Net:-***

Duty net of the nation ought to be expansive based with the goal that it can cover expanding number of populace having the assessable limit.

### *(iv) Checking Tax Evasion:-*

Satisfactory measures be taken to check the issue of tax avoidance in the nation. Assessment laws ought to be made stricter for indicting the duty dodgers. Duty apparatus ought to be made progressively effective and legitimate to outfit its activities. Assessment rate ought to be decreased to empower the developing pattern of expense consistence.

### *(v) Increasing Reliance on Direct Taxes:-*

Duty apparatus of the nation ought to connect considerably more dependence on direct expenses rather than aberrant charges. As needs be, the assessment hardware should attempt to present riches charge, bequest obligation, blessing charge, use charge and so on.

### *(vi) Simplified Tax Structure:-*

Expense structure and standards of the nation ought to be improved with the goal that it can empower charge consistence among the general population and it can evacuate the superfluous badgering of the citizens.

## CONCLUSION

The objectives of fiscal policy such as economic development stability, Social Justice, etc. can be achieved only if the tool of policy life public expenditure, taxation, borrowing and deficit financing are effectively used.

Though there are gaps in Indian fiscal policy, there is also an urgent need for making Indian fiscal policy rationalized and growth oriented one.

The success of fiscal policy depend upon taking timely measure and their effective administration during implementation.

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