Defence Budgeting: Trends and Issues

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The defence budget for the financial year 2009-2010, even though in terms of percentage increase appears large, yet it is not actually so. There has generally been a mismatch between the funds asked by the MOD and those allotted by the MOF. The absence of indication of likely availability of funds impacts adversely the defence planning process. Of late, there has been improvement in the ratio of revenue to capital expenditure, but for a healthy ratio there is a need to increase the defence budget as a percentage of the GDP. While the capital budget allotment to the Navy and Air Force has seen a shift towards the positive, there is also a need to allot additional budget to the DRDO for R&D. Indigenisation efforts also need a boost. There is also a need to enhance coordination between the MOF and MOD for force modernization to meet the challenges from potential adversaries.

The final defence budget presented by the finance minister did not depart materially from the interim budget which allotted Rs 1, 41,703 Crore for the financial year 2009-10: an uncharacteristic increase of 34 percent over the previous year's budgeted estimates. The Plan expenditure will be to the tune of Rs.86, 879 crore against Rs.73, 600 crore and will include Rs. 54,824 crore for capital expenditure as against Rs.41, 000 crore in the RE for 2008-09. Parnab Mukherjee had stated that the raise has been made "*to strengthen the security in view of the recent terror attacks*."

One would tend to think that such a large increase was in the wake of Mumbai massacre and steady deterioration of security and strategic environment around India with China becoming increasingly assertive. However, on closer scrutiny it becomes quite clear that if the figure of defence expenditure is compared with Revised Estimates for financial year 2008-09 of Rs 1,14,600 Crore the increase is 23 percent and if the effect of Sixth Pay Commission on salaries and perks is taken into account the increase could even be less than ten percent. And generally the financial babudom tells the defence forces to plan for an annual increase of ten percent which may only cater for inflation. Further, despite many observations by Parliament's Standing Committee on Defence; the Finance Ministry has been reluctant to give a long term commitment of funds to support the Five Year Defence Plans (FYPD).

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For instance, the 10th FYPD (2002-2007) completed its period without the same having been approved by the Cabinet Committee and the Finance Ministry allotted funds during the plan period which were much less than the projections put forward by the Ministry of Defence. Apparently, the 11th FYPD (2007-2012) also appears to be heading for the same fate; the plan has entered its third year without having been approved so far. When the defence forces are not sure of long term commitment of funds for their integrated perspective plans then it has adverse impact on their capability building. So far the trend has been an incremental addition to their arsenals which may not be in congruence with developing of integrated capabilities.

The Parliament's Standing Committee on Defence in its 16th Report (released in April 2007) felt constrained to remark that “the Ministry of Finance and Ministry of Defence should not shift the responsibility to each other; rather together they must approve the Eleventh Plan at the earliest, so that it does not face the same fate of Tenth Plan. This will further facilitate both the Ministry of Defence to plan their finance, equipment acquisition and utilise the allocated amount to the fullest extent in a time- bound manner”. The Committee was also perturbed because of the mismatch between the projection and budgetary allocation for the first year (2007-08) of the plan.

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But on another level the armed forces have been regularly surrendering some of the capital budget meant for force modernization. The armed forces had returned Rs.7, 000 crore of the Rs.48, 007 crore allocated for the purchase of military hardware during 2008-09. An average of 14% of budgeted amount varying between Rs 5,000 and Rs 9,000 crores remained unspent each year from 1999-2000 till this was arrested in 2004-05. However, the trend of surrendering the budget especially the one earmarked for capital expenditure has continued since then. The inability to spend has been attributed to the difficult nature of procurement and acquisition process which has been revised frequently over the years with the new Defence Procurement Procedure-2008 having been put into place in August last year. The proposal for creating a non-lapsable fund proposed by the last BJP government and also recommended by the Parliament's Standing Committee on Defence has not found much acceptance in the current policy making quarters however so appropriate it might be to address this recurring phenomenon of surrender of capital funds.

According to the logic given by the government to Standing Committee, the creation of non-lapsable Defence Modernisation Fund (DMF) has a limited utility in as much as the funds available in the DMF would not automatically be available to the Ministry of Defence for utilization in the subsequent financial year. The Ministry would be required to seek approval of the Ministry of Finance and the Parliament for its utilization.

Another goal of the services has been to reduce the revenue expenditure and increase the capital expenditure with the ultimate aim of achieving an optimal ratio of 50: 50 between both types of budget heads. There has been a general trend of increase in the capital expenditure and a marked reduction in the revenue expenditure which reflects the rapid pace of modernization in the Indian armed forces. Further, the percentage of funds allotted to Navy and the Air Force has been increasing over the years, which indicates a trend towards added emphasis on modernizing these two services.

The ratio of Revenue Expenditure to Capital Expenditure, during the last decade and many years before has been in the region of 70:30. Due to the steep rise in the Capital budget in the recent years, the decadal average ratio between 1998-99 and 2007-08 is 67:33. There is a huge variation amongst the services on this account due to nature of their missions, requirements of man power and technology intensive equipment and weapon platforms and systems. For the Army, in the last decade, this ratio has been 82:18 bringing out its manpower intensive nature without much effort to cut manpower and manpower costs. For the Air Force it is 52:48. It is least for the Navy at 46:54. Capital budget share for Army in the last decade, 1997-2007/08 has been 30 %, followed by 27 % for Navy and 36 % to Air Force.

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But in the current financial year even though the capital expenditure has been increased in actual terms the ration between revenue and capital is not favourable due to the impact of Sixth Pay Commission. However, it is hoped that with a larger percentage of GDP, perhaps up to 3 percent of GDP being spent on the defence, as once articulated by Prime Minister Manmohan Singh, it would be possible to achieve a harmonious ratio of 50:50 in the coming years.

A healthy Capital to Revenue ratio of 50:50 has several long-term implications on for example on sustenance of current force levels as also additional revenue needed for maintaining the additional capital expenditure structures in future. Revolution in military affairs can be ushered in at a faster pace compared to the glacial pace at which it has been progressing since the last one decade. Force planning, force development, force modernization and capacity building can also be achieved during the current Long Term Integrated Perspective Plan (2007-2022) if this optimal ratio is maintained. Defence procurements, import substitution and self-reliance are some of the other areas which would be positively impacted upon.

Further, the revised LTIPP (2007-22) is being prepared following a deliberate and integrated 'Top Down' approach by articulating National Security Strategy (NSS), National Military Strategy, and National Military Objectives/Capabilities. The document is expected to be ready by December 2009. Presently, draft NSS is doing the rounds of various ministries for suggestions and amendments; many are skeptical whether it will see the light of the day any time soon, others are questioning even the need for such a document. Strategic discourse in India being what it is it would be too optimistic to expect such a time bound articulation of NSS and evolving subsequent documents based on NSS which would be essential precursors to our long term defence budgeting and planning.

Another important endeavour of our government has been to increase the level of indigenization of defence. Despite several initiatives taken in the recent past for promoting indigenisation and achieving self-reliance in the defence sector, there is still heavy dependence on foreign suppliers and the goal of achieving self-reliance remains elusive. The government had set a target of achieving an indigenization ratio of 70:30 by 2005 but we are very far from reaching that goal. The Standing Committee on Defence (SCD) has desired that a formal mechanism for sharing information on the futuristic requirements and the perspective plans of the users should be put in place in accordance with the practices adopted by certain advanced countries so as to inspire the confidence of the private industries and enable them to gear up their infrastructure well in advance. Such mechanisms and structures have been formed but apparently they have been remiss in performing their functions efficiently.

The SCD has now recommended that the steps should be taken to reverse current import/indigenization ratio of 70:30 in the next 10 to 15 years. This would require changes in policies and allotment of additional budgeted funds for DRDO and Department of Defence Production. For instance, Ordnance Factories do not have their own R&D and they cannot decide on their vendors, hence, they are not efficient. It has also recommended that a fund called 'Defence Technology Development Fund' with the Department of Defence Production (DDP) be created which should be used for providing funds to Small and Medium Enterprises (SMEs) to carry out design and development work either directly or through industry champions/Defence PSUs/OFs. Another suggestion is to create a Strategic Defence Industry Fund (SDIF) on the lines of North-East Development Fund where non-lapsable pool of resources should be utilized exclusively for the 'Make' category of products of Indian Industry.

Thus there is also a good case for R&D budget to be progressively increased to over 10% with accompanying drive to recruit better talent, commensurate organizational changes and more accountability. The R& D budget has been languishing at an average 6 percent of the defence budget since 2000. Earlier it was much less; surprisingly the budgetary support to Defense R&D activities in the first 25 years of Independence, was around 1% of the Defense budget. Recently, the Parliament's Standing Committee on Defence has recommended that R&D budget should be at least 14 to 15 percent of the total defence budget of the country as more and more research and product development opportunities are likely to come India's way due to changed international scenario. Needless to say, our neglect of the vital aspect of R & D has cost the nation very dear. We can not have pretensions of being a major or regional power unless we have adequate indigenous defence production capabilities for production of the state-of-art weapons and systems and allied equipment.

And lastly, the annual defence budget is treated by the Ministry of Finance as merely an exercise in accountancy with rarely an element of either vision or long term planning. MOD's long term projections are usually ignored and any criticism of the same is sought to be met by the Finance Minister offering a regular caveat that if more funds are needed during the year they would be allotted. Mercifully, this year the Finance minister has not repeated that meaningless statement. But that does not mean that disjunction between the MOF and MOD has been removed; the lack of coherence between defence budgeting and planning continues to bedevil the process affecting the force modernization of our armed forces leading to delays in acquiring comprehensive national power. Such a situation emboldens our adversaries in many ways.