Press Release
The wean, lean, sheen and green Budget

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The FY24 Union Budget is going to be presented in the backdrop of a gradual normalization of the economic shocks in the near past and the continuing global headwinds. Covid has turned endemic amidst comfortable level of inoculation (more than 67% of population has received double dose of vaccination). Global supply chain pressures and international commodity prices are back to levels existing before the start of Russia-Ukraine war despite simmering of unresolved issues. While that's a welcome development, the outlook for FY24 would still be shaped by the anticipation of a sharp slowdown in global economic growth - a fallout of the aggressive monetary policy tightening across the world and lingering of geopolitical uncertainty over the last one year. **Acuité AMEP**[1] index up to Dec-22 confirms the resilience of the Indian economy to these headwinds with a satisfactory level of post pandemic reset at the headline level although it also highlights that the recovery has not been uniform with the rural sector continuing to be a relative drag on the overall growth momentum.

With this backdrop, the Finance Minister would need to redraw fiscal priorities while doubling down on fiscal levers that have performed well. We believe the FY24 Union Budget could be a good mix of what we call "wean, lean, sheen, and green".

The importance of a wean off

There is consensus expectation with respect to the central government being able to largely meet its FY23 fiscal deficit target of 6.4% of GDP. However, there is likely to be a slippage of 20-40 bps in case of revenue deficit and primary deficit for the year, which highlights underlying fiscal pressures, some of which have persisted on account of continuation of the Covid era relief programs.

With size of the economy in FY23 projected to be 8.6% higher than its pre pandemic (FY20) levels and the visible domestic recovery, there is little merit in extension of the Covid era relief programs. After providing multiple extensions earlier, the government has now made its intent clear by discontinuing the Pradhan Mantri Gareeb Kalyan Anna Yojana (PMGKAY) in its earlier avatar post Dec-22 although electoral considerations have led to the absorption of the scheme under the existing programs under National Food Security Act (NFSA) and the waiver of the modest PDS charges in CY23. While the latter will involve some costs, we estimate that a net fiscal saving of Rs 1 Lakh Cr is feasible in FY24 against food subsidy.

The expenditure on fertiliser subsidies is expected to drop to Rs 1.4 Lakh Cr as against nearly Rs 2.3 Lakh Cr in FY23 (RE) driven by expectations of lower crude oil prices and the government's revised gas procurement policy for fertilizer companies. All Covid era schemes should be allowed to have a sunset post Mar-23 but given the upcoming state and the central elections, this is not going to be an easy task for the government.

[1] Please refer to the latest update on AMEP index here: https://www.acuite.in/pdf/PR_AMEP_Dec-2022.pdf

Be lean but preserve sheen

While India's post Covid fiscal expansion was lower in comparison to developed countries (as per IMF data, general government net borrowing jumped by 6.4% of GDP in case of India in the year after COVID began, compared to a jump of 8.0% of GDP in case of advanced economies), the economy does face elevated debt levels vis-à-vis its peers. The IMF estimates India's general government's gross debt ratio at 83.4% of GDP in 2022, considerably higher than 64.5% average for emerging and developing economies.

Being fiscally overweight impinges upon the degrees of freedom for policymakers. In case of India, we estimate central government to set aside around 42% of revenue receipts just to meet interest expenses in FY24. Debt repayment imparts a sense of rigidity and hence an elevated obligation on this count would constrain government's ability for developmental expenditure. Hence, the merits of fiscal consolidation cannot be underemphasized. The central government has managed to retrace 48% of the post Covid fiscal expansion (comparison of fiscal deficit in FY23 (RE) over FY19) with the support of the revenue buoyancy seen over the last two years. It is important to normalize fiscal policy further to (i) regain fiscal space for future economic contingencies (ii) ensure overall fiscal policy works in tandem with monetary policy (which has been nearly normalized) for a stable inflation regime (iii) adequately rebalance the available credit space for private sector borrowers and (iv) enable India's entry into global bond indices for expansion of the investor base and attract higher foreign savings.

Overall, we expect FY24 Union Budget to present a fiscal deficit target between 5.5%-5.8% of GDP vs. 6.4% in FY23. This needs to be accompanied by reiteration of the medium term path of fiscal consolidation – a clarity on revised FRBM glidepath can boost market sentiments.

Notwithstanding the virtues of being fiscally lean, the Union Budget will have to do a tightrope walk to preserve the fiscal sheen, which the current administration has displayed by almost doubling the share of capital expenditure in last five years, from 1.5% of GDP in FY18 to an estimated level of 2.9% in FY23. With the momentum in private capex still uncertain (amidst a highly uncertain global demand backdrop) in the near term, we hope the FY24 Union Budget to scale up capex allocation further to a two decade high of 3.0% of GDP, almost touching Rs 10 Lakh Cr in absolute terms. This will ensure that the quality of fiscal adjustment remains healthy while government's focus on infrastructure related programs like "PM Gati Shakti" and "National Infrastructure Pipeline" receives a further push. We expect to see a higher outlay on both urban and rural infrastructure projects in the upcoming budget.

Embrace green

Taking into account India's commitment at COP27, the government has been taking gradual steps to achieve the long-term climate goals. The FY24 Union Budget could make a further effort to reduce the carbon footprint by (i) increasing allocation for Ministry of New and Renewable Energy and Ministry of Environment, Forests and

Climate Change, (ii) extend PLI coverage for wind energy and green hydrogen projects (iii) introduce a platform for trading carbon credits, etc.

While FY23 Union Budget made a seminal contribution by the introduction of Sovereign Green Bonds (which has got priced at 5-6 bps below comparable g-secs at its maiden auction in Jan-23), the upcoming budget is expected to extend the size of these SGB issuances and facilitate the development of a domestic green finance market. The state governments may also be allowed to allocate a small portion of their issuances under the green channel – after all, on a 12-month trailing basis, states put together have accounted for around 42% of general government capex.

Overall, we expect FY24 Union Budget to lay down the necessary policy framework for a sustainable growth path of the Indian economy over the medium term while also keeping an eye on fiscal prudence and consolidation.

About Acuité Ratings & Research Limited:

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Media Contact:

Sahban Kohari
Ph: + 91-9890318722
sahban@eminenceonline.in

Analytical Contacts:

Suman Chowdhury Chief Analytical Officer Ph: + 91-9930831560 suman.chowdhury@acuite.in	Prosenjit Ghosh Chief Operating Officer – Subsidiaries Ph: +91-9920656299 prosenjit.ghosh@acuite.in