2020-21 Union Budget: Fiscal slippage but little stimulus

HDFC Bank, February 2020

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Summary

- *The budget delivered credible numbers in terms of its fiscal deficit estimates, raising the deficit by 50bps this year and the next. The fiscal deficit was raised to 3.8% for 2019-20 and to 3.5% for 2020-21. The budget used up the 0.5% GDP leeway provided by the FRBM instead of sticking to the fiscal consolidation path that laid out a target of 3% for FY20-21.*

- *For 2020-21, the government plans to increase expenditure by 13% with the bulk of the increased expenditure in agriculture and infrastructure. While this is likely to improve productivity and raise the growth potential in the medium term, the budget falls short of providing the much needed counter-cyclical stimulus that the current economic environment warrants in the short term. On the tax side, while the personal income tax cut is a welcome step, it is unlikely to boost consumption demand significantly given the low tax base in the economy.*

- *On the expenditure side, while allocations for certain agricultural and rural schemes has been increased, the real challenge is the utilisation of funds. The lower than budgeted spending for FY20 for some of these schemes signals that absorption of funds remains an issue.*

- *Revenue collections: In this muted growth environment the assumptions on tax collections for next year look somewhat stretched. The budget assumes a tax buoyancy of 1.2 for 2020-21 compared to 0.5 and 0.8 over the last two years. To bridge the gap on the receipts side, the government relies on a significantly higher disinvestment target (Rs. 2.1 trn) with the LIC and IDBI stake sale, higher telecom receipts and Rs. 1.5 trn as dividends and profits from the RBI and PSUs.*

- *The financing of the fiscal deficit: In line with our expectations, the government kept its gross market borrowings unchanged at INR 7.1 trn in FY20 and financed its higher fiscal deficit through other sources (particularly the NSSF). For next year, the government has budgeted to borrow INR 7.8 trn which is broadly in line with our and market expectations (HDFC Bank estimate of INR 7.7- 7.8 trn). The reliance on the small savings fund is likely to continue (estimate of INR 2.4 trn) and could imply that small savings rate undergo little or no revision in FY21 as well. We expect the 10 year G-Sec to trade between 6.50%-6.60% in the short run as market are likely to get some relief in terms of no additional borrowings this year and in line with expectations borrowing target for next year*

- *The Positives: The abolishment of the Dividend Distribution tax, 100% exemptions for the flows coming in through the sovereign wealth funds, raising the limit for FPI in corporate bonds to 15% (from 9%), focus on infrastructure push (through the National Infrastructure pipeline) are likely to help garner foreign flows when domestic savings continue to decline.*

- *The disappointments: No significant reforms for the power sector (expectations of UDAY 2.0) after a mixed performance of UDAY 1.0, lack of a bad bank (TARP style) solution for NBFCs to reduce the risk aversion in the system, no major reforms for the real estate sector, lack of any major counter-cyclical measures to boost consumption.*

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No additional borrowings for FY20 as government leans on the small savings fund

- In line with our expectations, the government kept its gross market borrowings unchanged at INR 7.1 trn in FY20 and financed its higher fiscal deficit through other sources (particularly the NSSF).
- For next year, the government has budgeted to borrow INR 7.8 trn which is broadly in line with our and market expectations (HDFC Bank estimate of INR 7.7 trn). The reliance on the small savings fund is likely to continue (estimate of INR 2.4 trn). The government plans to do buybacks of INR 300bn next year compared to no buybacks this year and is expected to do switches of INR 2.7 bn in FY21 from INR1.65 trn this year.
- We expect the 10 year G-Sec to trade between 6.50-6.60% in the short run as market are likely to get some relief in terms of no additional borrowings this year.

INR bn	FY20 BE	FY20 Actual	FY21
Fiscal Deficit	7038	7668	7963
Gross borrowings	7100	7100	7800
Repayments	2369	2360	2351
Net Market Borrowings	4731	4740	5449
Switches	500	1650	2700
Buybacks	500	0	300
Short term borrowings	250	250	250
Net Market Borrowings (excluding buybacks)	4231	4740	5149
Other Financing			
External Debt	-30	49	46
NSSF	1300	2400	2400
State Provident Funds	180	180	180
Other receipts	595	49	508
Drawdown of cash balance	511	0	-530

Source: Budget Documents, HDFC Bank

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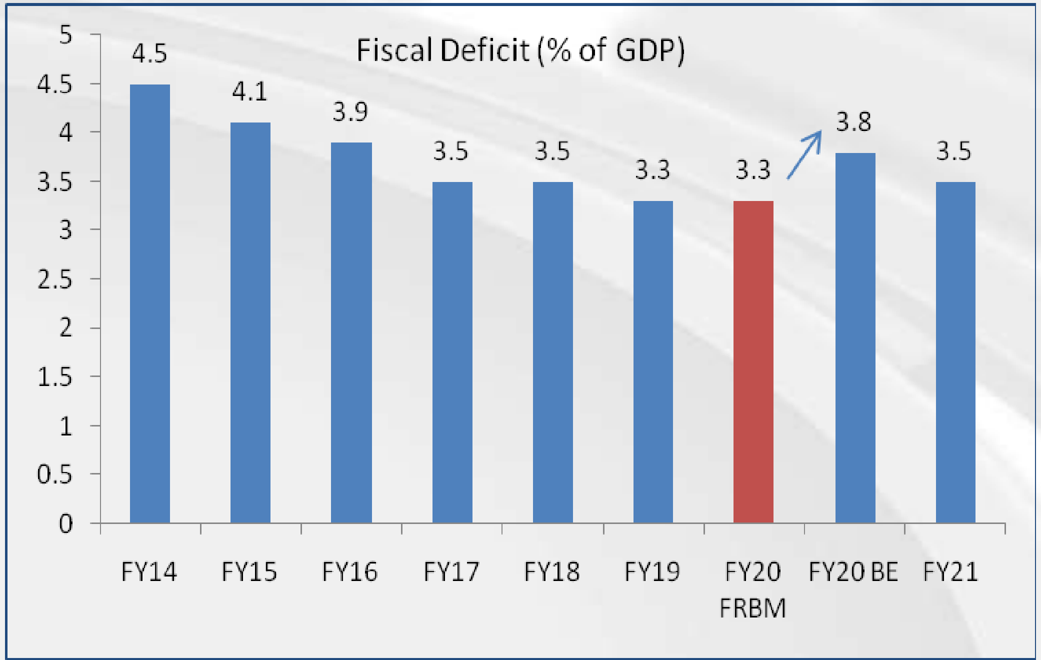
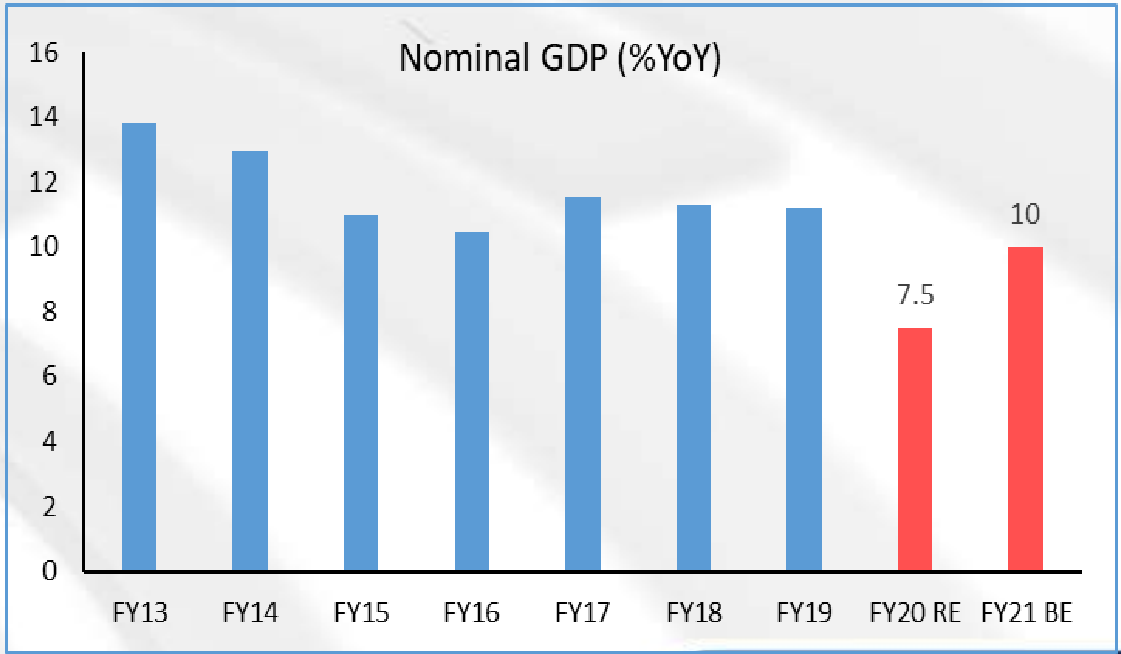
Government deviates from its fiscal consolidation path

- *The government deviated from its path of fiscal consolidation, lowering the fiscal deficit target to 3.5% of GDP for FY21 compared to 3.8% in FY20. It invoked the 0.5% leeway given under the FRBM act to make up for revenue shortfall recorded.*

- *The Budget assumes Nominal GDP growth to rise by 10% in FY21 (effective assumption of 6% real growth and 4% inflation) from 7.8% in FY20. This growth number seems to be a bit on the optimistic side, given the real GDP growth continue to moderate and inflation is expected to cool-off below 4% in the second half of 2020-21 as food inflation spikes moderate and a high base effect kicks-in.*

- *The budget is likely to be only mildly positive for growth in FY21 and we do not expect any discernible impact on inflation given the output gap (actual growth is much lower than the potential growth rate).*





Source: Budget Documents, HDFC Bank

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FY2020-21: How the government plans to balance the fiscal scales

The fiscal math: Revenue targets continue to seem aggressive for FY21

				%YoY	
(INR trn)	FY19A	FY20RE	FY21BE	FY20 RE	FY21
Revenue receipts	15.53	18.50	20.21	19.14	9.2
Tax revenue(net to centre)	13.17	15.05	16.36	14.23	8.7
Gross tax revenue	20.80	21.63	24.23	3.99	12.0
Direct tax	11.25	11.70	13.19	3.98	12.7
Income tax	4.73	5.60	6.38	18.29	14.0
Corporate tax	6.64	6.11	6.81	-8.00	11.5
Indirect Tax collections excluding GST	3.57	3.74	4.06	4.91	8.5
Customs	1.18	1.25	1.38	6.10	10.4
Excise	2.32	2.48	2.67	6.91	7.7
GST collections	5.82	6.12	6.91	5.29	12.8
Non- tax revenue	2.36	3.46	3.85	46.59	11.4
Dividends and profits	1.13	2.00	1.55	76.24	-22.3
Misc. capital Receipts including disinvestments	1.13	0.82	2.25	-27.64	175.7
Disinvestments	0.95	0.65	2.10	-31.38	223.1
Total receipts (ex borrowings)	16.66	20.83	19.32	25.03	-7.2
Total Expenditure	23.15	26.99	30.42	16.56	12.7
Revenue Expenditure	20.07	23.50	26.30	17.05	11.9
(Subsidies)	2.20	2.64	2.62	19.82	-0.6
Capital Expenditure	3.08	3.49	4.12	13.39	18.1
Fiscal Deficit	6.49	7.67	7.96		
Fiscal Deficit % of GDP	**3.42**	**3.75**	**3.54**		
Nominal GDP	190.10	204.42	224.89	**7.53**	**10.0**
Tax Buoyancy (Gross)	0.80	0.50	1.20		

Source: Budget Documents, HDFC Bank

Gross tax assumptions seem optimistic given the slowdown in growth:

- Direct collections are budgeted to grow by 12.0% in FY21 compared to 4.0% in FY20 RE. This is despite INR 40 bn loss in revenue expected from the reduction in income tax cuts.
- **Tax Buoyancy (Gross) expected to rise above 1.0 after coming in 0.5 and 0.8 over the last two years (expected to increase to 1.2 in FY21 from 0.5 in FY20 RE and 0.8 in FY19).**

- GST collections target set at INR 6.9 trn. **Our calculations show that a monthly run rate of INR 1.06 trn is required to meet the target.**
- Indirect tax collections excluding GST are expected to rise (by 8.5% in FY21, coming in at INR 4.1 trn) **on account of increase in collection from custom and excise duties.**

The cushion: Aggressive disinvestment target

- Higher disinvestments expected to provide cushion to the fiscal math.
- The budget also accounts for INR 1.6 trn in dividends and profits from the RBI and PSUs.

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Higher growth budgeted for direct tax collections despite the personal income tax cut

Income tax cuts unlikely to be a game changer for boosting consumption

Revenue foregone on account of reduction in income tax cut will account to INR 400 bn/year (~0.18% of GDP in FY21). The income tax cuts are unlikely to significantly push overall consumption given the low tax base – only 7% of India's working age population pays tax and more than 75% of the tax collections are paid by the Top 5% of the tax payers (who have a high propensity to save).

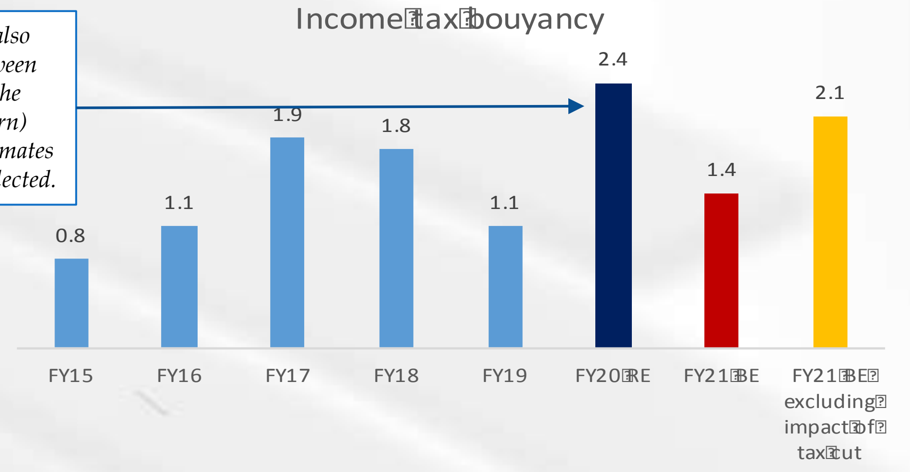
INR lakh	New Tax Rates	Existing Tax Rates
0-2.5	Exempt	Exempt
2.5-5.0	5%	5%
5-7.5	10%	20%
7.5-10	15%	20%
10-12.5	20%	30%
12.5-15	25%	30%
>15 lakh	30%	30%

Budgeted Direct Tax collections for FY21

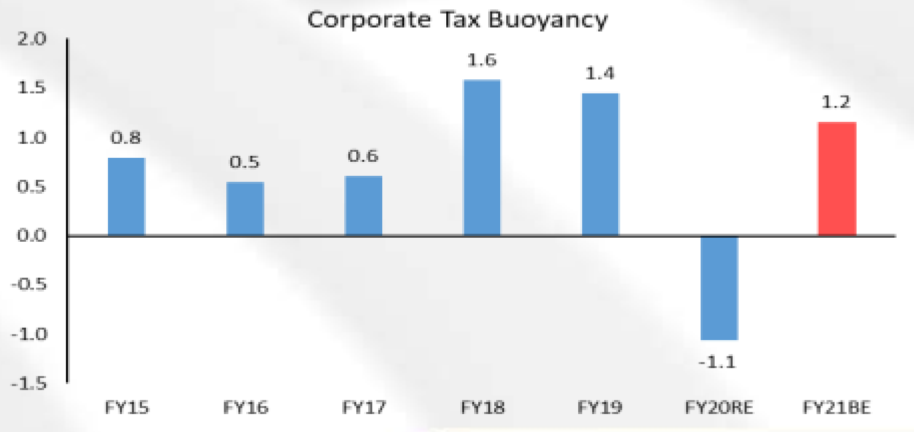
INR bn	FY20RE	FY21BE
Corporate Tax (%YoY)	6105 (-8.0)	6810 (11.5)
Income Tax (%YoY)	5595 (18.3)	6380 (14.0)

Tax buoyancy excluding income tax cut expected to be high

Actual Tax buoyancy for FY20 also likely to be lower given that between Apr-Nov 2019 less than half of the income tax revenues (INR 2.7 trn) accounted for in the Revised estimates for FY20 (INR 5.6 trn) were collected.



Corporate tax buoyancy is budgeted to pickup in FY21



Source: Budget Documents, HDFC Bank

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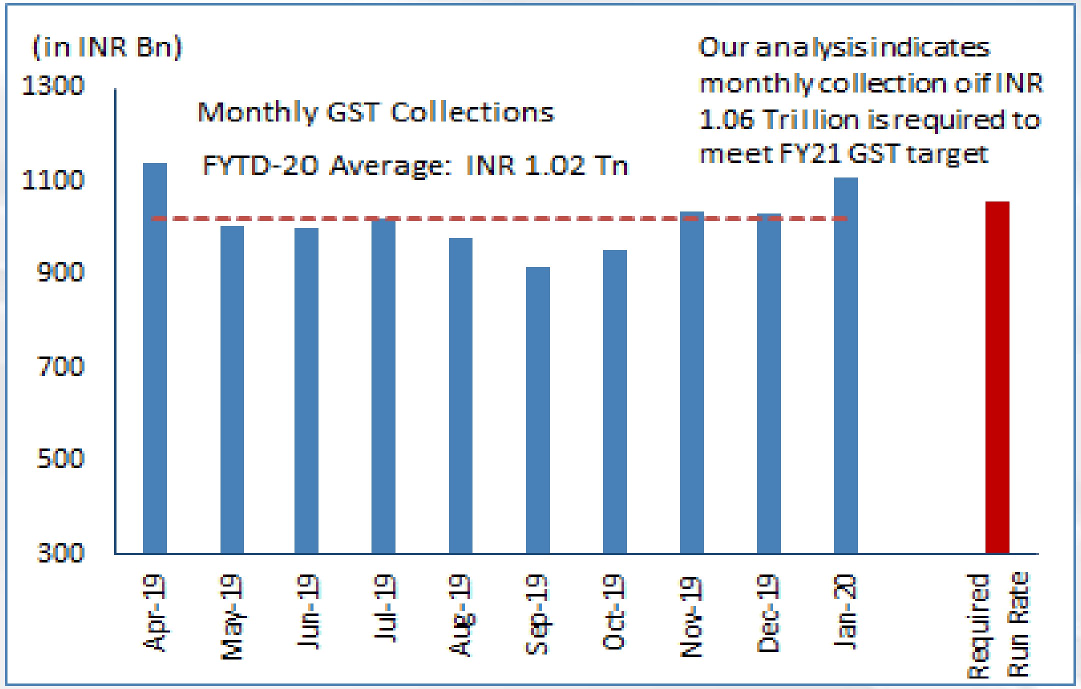
Indirect tax collections: Banking on higher custom duties and GST collections



Custom and excise duty constitute ~35% of indirect tax collection

Excise Duty on Cigarettes & Tobacco Products
Depending upon the size of cigarette, excise duty is increased in the range of INR 200-735.

Custom duty revision: both up and down

Increase

Decrease

- Custom duty on newsprint and light weighted coated paper from 10% to 5%
- Custom duty is removed from raw material used for fuels, chemicals and plastics.

Source: Budget Documents, Media Article, HDFC Bank

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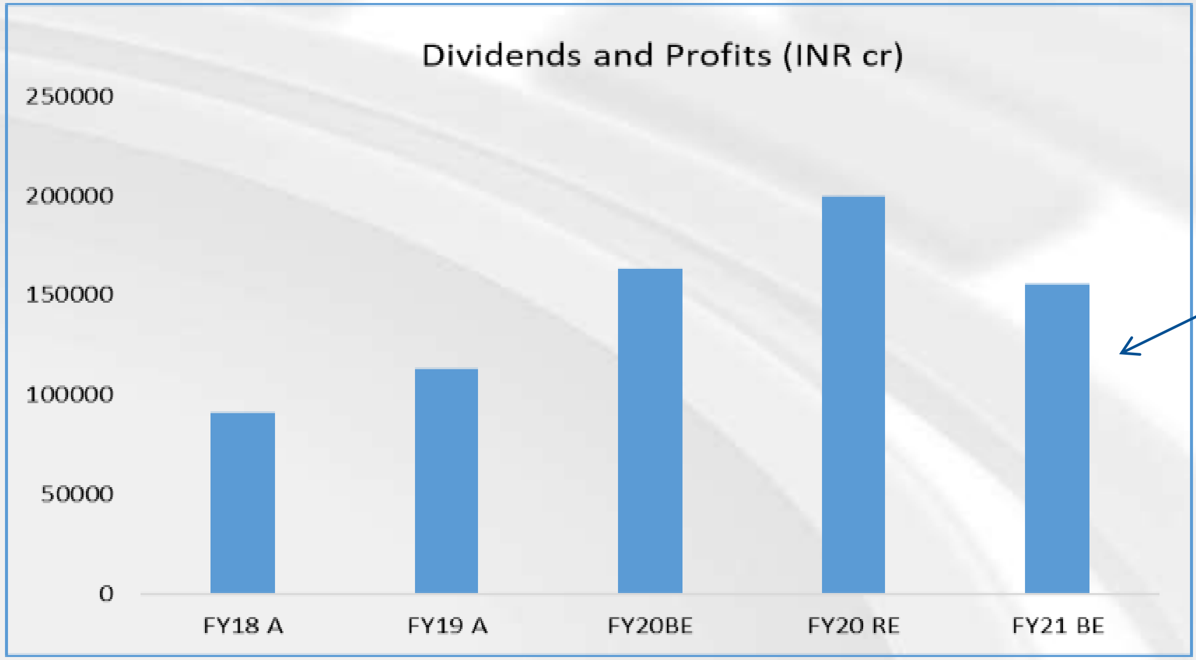
Non-Tax Revenue: Lower proceeds Dividends and Profits to weigh; higher communication receipts to provide relief.

- Non-Tax revenue growth is budgeted to moderate to 11.4% in FY21 vs. 46.6% in FY20 RE due to reduced receipt from dividends and profits from PSUs and the RBI.

- Dividends and Profits from PSUs and the RBI are expected to decline by 22.3% to INR 1.55 trn in FY21 vs. INR 2.0 trn in FY20RE.

- **The cushion for Non-tax revenue growth is expected to come from higher telecom receipts.** Government has budgeted INR 1330 bn from licence fees and spectrum usage charges for FY21, 125% growth from FY20 RE (INR 590 bn). The additional amount is mainly on account of adjusted gross revenue dues. The budget documents do not specify accounting of any proceeds from spectrum auction. Airtel owes ₹35,586 crore to DoT, Vodafone Idea ₹50,000 crore, and Tata Teleservices, which has sold its mobile services business to Airtel, owes ₹14,000 crore – which in total accounts for INR 1 trn in dues.

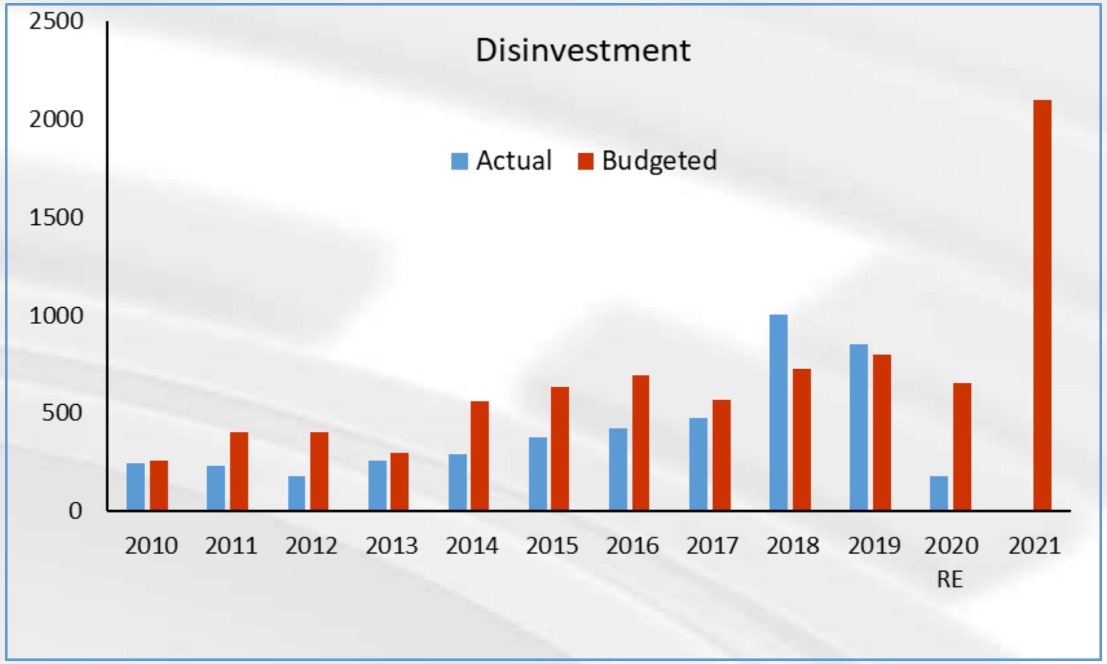


Transfer from the RBI pegged at INR 896 billion for FY21 vs INR 1516 bn in FY20

Source: Budget Documents, HDFC Bank

Disinvestment: An ambitious target?

Disinvestment target at an all-time high



Proposed strategic stake sale for (%)

- •Air India (100% stake)
- •BPCL
- •IDBI (46.5% stake)
- •Tehri Hydro Development Corporation of India
- •North Eastern Electric Power Corp

- Disinvestment target was revised lower to INR 650 bn from INR 1050 bn in FY20. For FY21, government has set at an ambitious target of INR 2100 bn.
- Government expects to garner INR 900 bn proceeds from stake sale in IDBI (amounts to only INR 170bn at current market cap) and LIC (10%). The valuation to be decided at the time of listing.
- INR 1200 bn in disinvestment proceeds expected from CPSE stake sales in FY21.

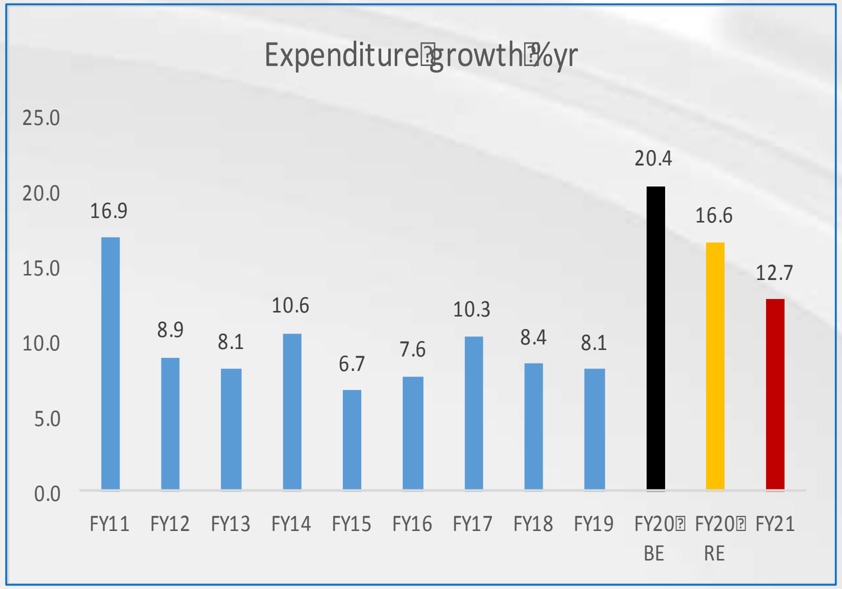
Source: Budget Documents, HDFC Bank

Government expenditure to rise in FY21 without compromising on the quality of expenditure

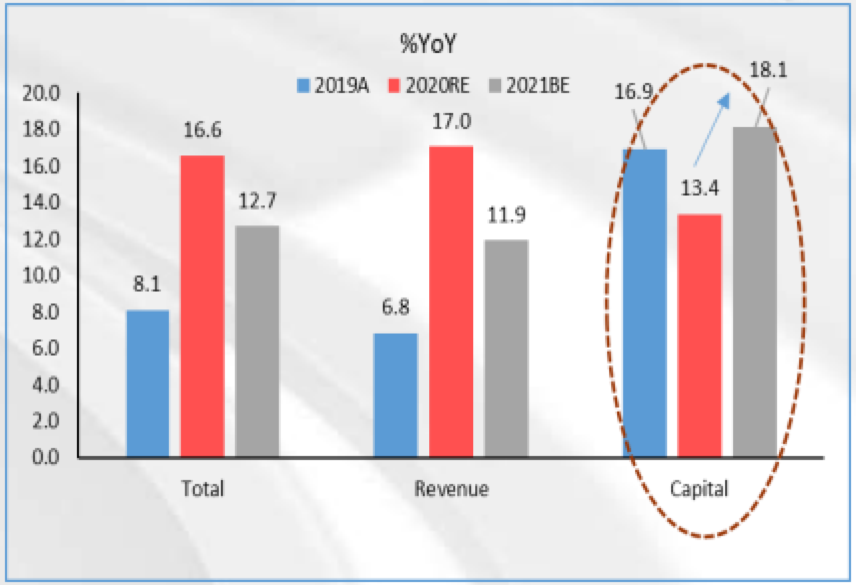
- *Expenditure expected to grow by 13% in FY21 from 16% in FY20 but higher than 8% in FY19.*
- *As a share of total expenditure, revenue expenditure accounts for 86% while capital expenditure is at 14%.*
- *Quality of expenditure expected to improve in FY21. For FY21, Capital expenditure growth of 18% - Highest since FY17. Revenue expenditure growth of 12% - lower than last year*
- *Revenue to Capital Expenditure ratio is expected to be at 6.4 in FY21 vs. 6.7 in FY20RE, implying improvement in the quality of spending.*
- *However, if growth fails to pick up in FY21 and tax revenues fall short of expectations, the expenditure targets could come under pressure in FY21 yet again.*

- *To recall, in FY20 as well the government has cut back on expenditure by 3% (INR 87,000 crore) as per the revised estimates, which in itself also seem optimistic. Between Apr-Nov 2019, the government had spent INR 18.2 trn out of the INR 27.9 trn target. As per the revised estimates, it seems that the government plans to spend 31% of its BE in the last four months of FY20 (although the government in January 2020 had said that it would restrict Q4 spending to 25% of BE from an earlier limit of 33% of BE).*

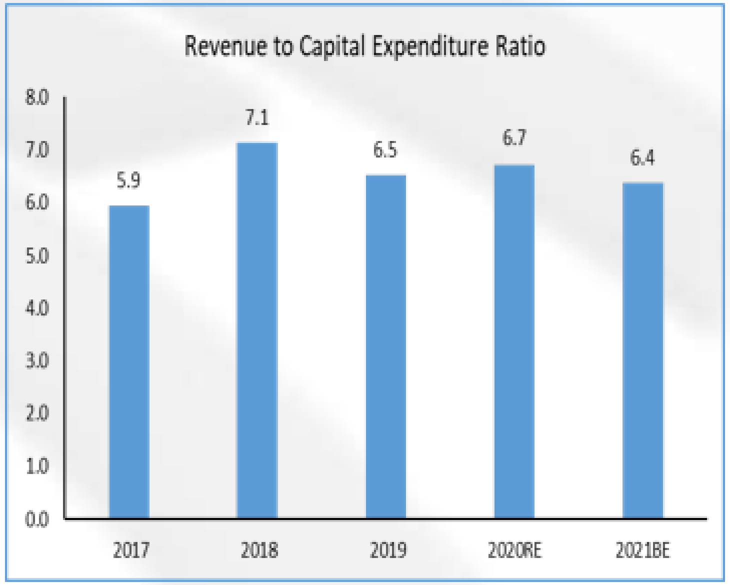
Expenditure growth higher than historical trend



Revenue expenditure growth lower while capex spending growth rises



Quality of expenditure seen improving



Source: Budget Documents, HDFC Bank

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So where is the government actually spending?

- The major heads where there has been an increase in expenditure in FY21 compared to FY20 include Agriculture, Roads, IT& Telecom, Pensions.
- Interest payments and transfer to states are also budgeted to grow at a strong pace with INR7.08 trn budgeted for interest payments and INR 2.0 trn for transfer to states.

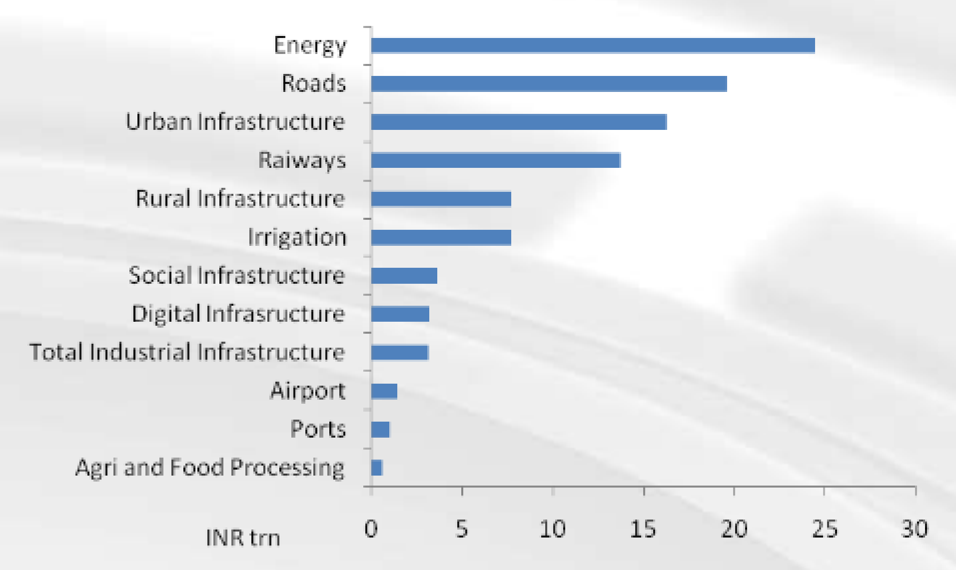
Growth

Amount change

Budget Allocation (in INR, Bn)					Change in Allocation			
	FY19	FY20BE	FY20RE	FY21 BE	FY20 %yr	FY21 %yr	FY20 (INR bn)	FY20 (INR bn)
Agri & Allied	**633**	**1515**	**1208**	**1548**	**91**	**28**	**576**	339
Roads	**773**	**830**	**830**	**918**	**7**	**11**	**57**	88
Rails	549	680	700	722	27	3	151	22
Health	545	650	638	675	17	6	94	37
Education	803	949	949	993	18	5	145	45
Rural Development	1328	1408	1434	1448	8	1	106	14
Defence	2908	3053	3163	3231	9	2	255	68
New and Renewable Energy	44	-	37	56	-15	51	-7	19
IT &Telecom	149	218	160	593	8	271	11	433
Pension	1602	1743	1841	2107	15	14	239	265
Interest Payments	5826	6605	6251	7082	7	13	425	831
Transfer to States	1191	-	1554	2004	30	29	363	450
GST Compensation Fund	543	1012	1212	1354	123	12	669	142

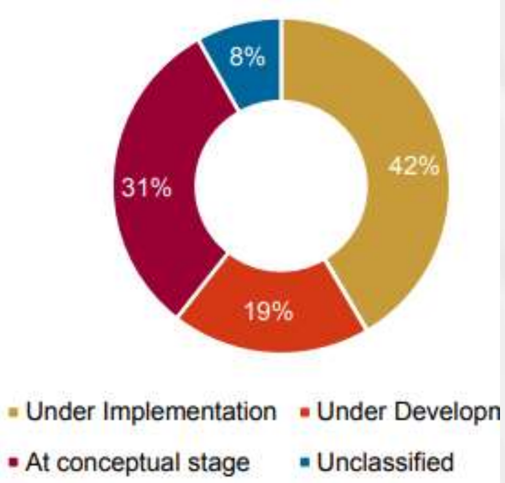
Source: Budget Documents, HDFC Bank

National Infrastructure Pipeline



Roads, urban and housing, railways, power and irrigation to comprise ~80% of the NIP

Status of Projects



- **INR 103 lakh crore to be invested on infrastructure over the next 5 years.** INR 22000 cr has been already provided to Infrastructure Pipeline and the rest from non-budget financing.
- 6500 projects across sectors including housing, safe drinking water, airports, warehousing, etc under NIP.
- **In addition, INR 1.7 trn was allocated for transport infrastructure.**

- **Roads:** Accelerated development of highways will be undertaken. This will include developments of:
    - 2500 km access control highways, 9000 kms of economic corridors, 2000 km of coastal and land port roads and 2000 km of strategic highways
    - Delhi-Mumbai Expressway to be completed by 2023
- **Ports:** Corporatizing at least one major port
- **Airport:** 100 more airports to be developed by 2024 to support Udaan scheme

Source: Budget Documents, HDFC Bank

…and Rural India

Focus on Solar Energy

PM Kusum: The scheme was introduced last year with an aim to reduce farmer's reliance on fuel and kerosene and link pump sets to solar power.

What has changed: -Scope of the scheme has been increased to support ~2 Mn farmers in setting up solar pumps.

- 1.5 Mn will be provided aid to solarise grid connected pump sets.

Budget Allocation: INR 100 Bn.

Other schemes: To strengthen food supply chain of perishable products, a railway service ("Kisan Rail") and air service "Krishi Udaan" will be set up.

Outlay on Major Schemes	(in INR Bn)				YoY,%		
Schemes	FY19	FY20BE	FY20RE	FY21BE	FY20BE	FY20RE	FY21BE
Income Support Scheme/PM Kisan	12	750	544	750			37.9%
Crop Insurance Scheme	119	140	136	157	17.6%	14.3%	15.4%
Ayushmaan Bharat	26	66	33	64	153.8%	26.9%	93.9%
National Health Mission	315	337	343	341	7.0%	8.9%	-0.6%
MGNREGA	618	600	710	615	-2.9%	14.9%	-13.4%
PM Krishi Sichai Yojana	81	97	79	111	19.8%	-2.5%	40.5%
PM Grm Sadak Yojana	154	190	141	195	23.4%	-8.4%	38.3%
PM Awas Yojana	254	259	253	275	2.0%	-0.4%	8.7%
National Rural Drinking Water Mission	55	100	100	115	81.8%	81.8%	15.0%
National Education Mission	308	385	377	392	25.0%	22.4%	4.0%
National Livelihood Mission- Ajeevika	63	98	98	100	55.6%	55.6%	2.0%
Job & Skill Development	61	73	57	54	19.7%	-6.6%	-5.3%
Swachh Bharat Mission	154	126	96	123	-18.2%	-37.7%	28.1%
AMRUT & Smart Cities Mission	121	138	98	138	14.0%	-19.0%	40.8%
DBT- LPG & Kerosene	166	297	298	356	78.9%	79.5%	19.5%
Deen Dayal Upadhyay Gram Jyoti Yojana	38	41	41	45	7.9%	7.9%	9.8%

PM Kisan's allocation is revised downwards in F2020, indicating operational inefficiencies. Going forward, dealing with operational inefficiencies will remain a key challenge

While FY20 allocation under MGNREGA is increased, FY21 allocation is decreased

Rural schemes allocation is increased for FY21

DBT budgetary allocation has increased

For sectors with higher allocations, the real challenge is the utilisation of funds. The lower than budgeted spending for FY20 signals that absorption of funds remains an issue.

ource: Budget Documents, HDFC Bank

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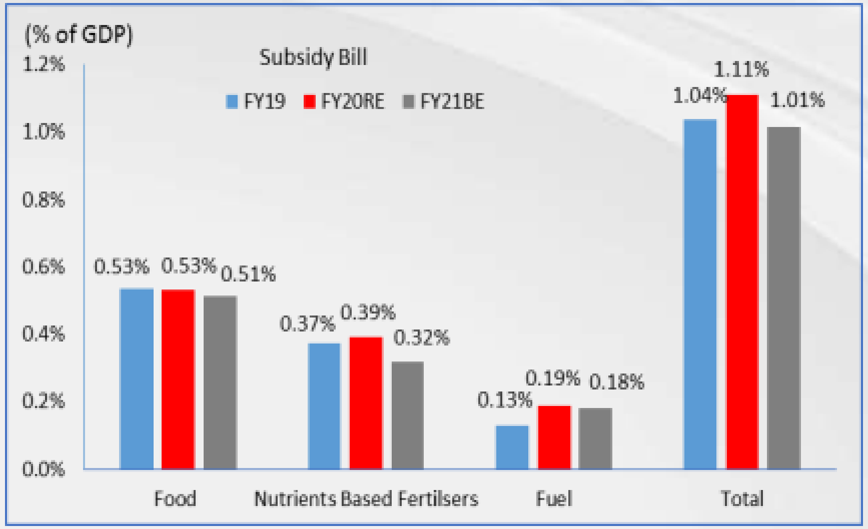
Lower subsidy bill for FY21 as FCI funds greater share of food subsidy through NSSF

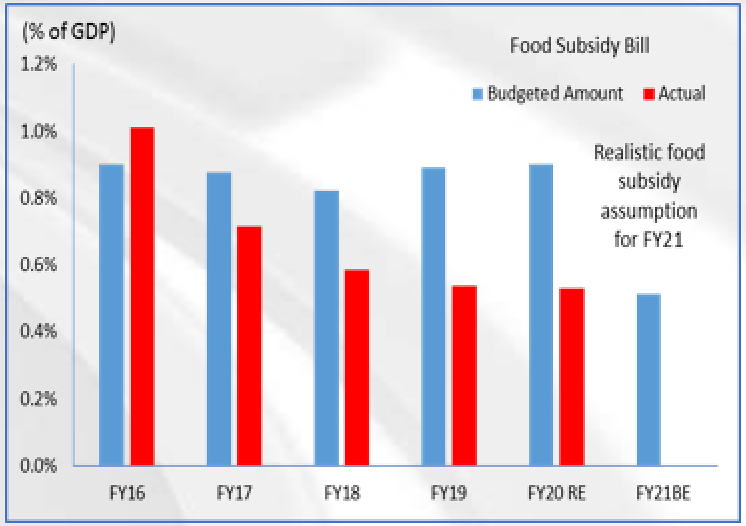
- For FY21, total subsidies are budgeted to decline by 0.6% on account of reduction in food, fertilizer and other subsidies.
- The food subsidy assumption is more realistic as the financing through the budget is in line with the trend and off budget support to FCI through NSSF has increased to INR 1.4 Trillion vs INR 1.1 Trillion for FY20.

	INR bn			% YoY	
	FY19A	FY20RE	FY21BE	FY20 RE	FY21 BE
Food	1013.3	1086.9	1155.7	7.3	6.3
Fertilizers	706.1	800.0	713.1	13.3	-10.9
Petroleum	248.4	385.7	409.2	55.3	6.1
Interest	200.0	259.0	282.0	29.5	8.9
Others	62.0	104.0	61.0	67.7	-41.3
Total Subsidies	2229.7	2635.6	2620.9	18.2	-0.6

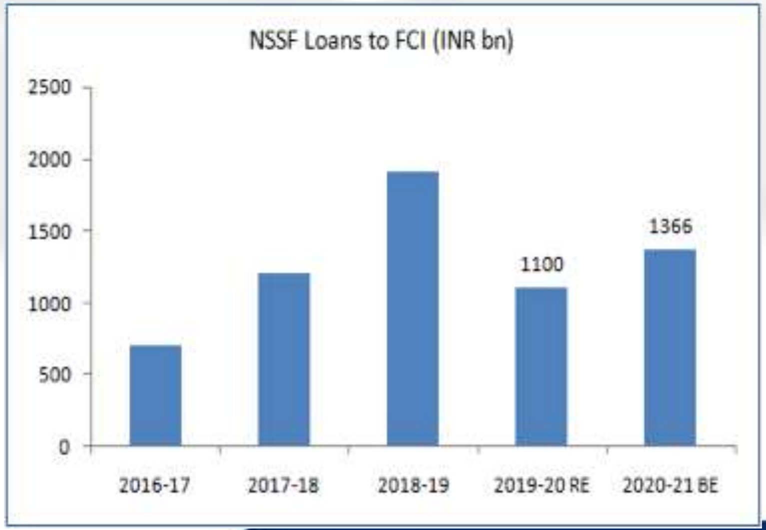
Subsidy bill set to decline in FY21



Due to a lower food subsidy bill



As the GoI leans on the NSSF to fund food subsidy



Source: Budget Documents, HDFC Bank

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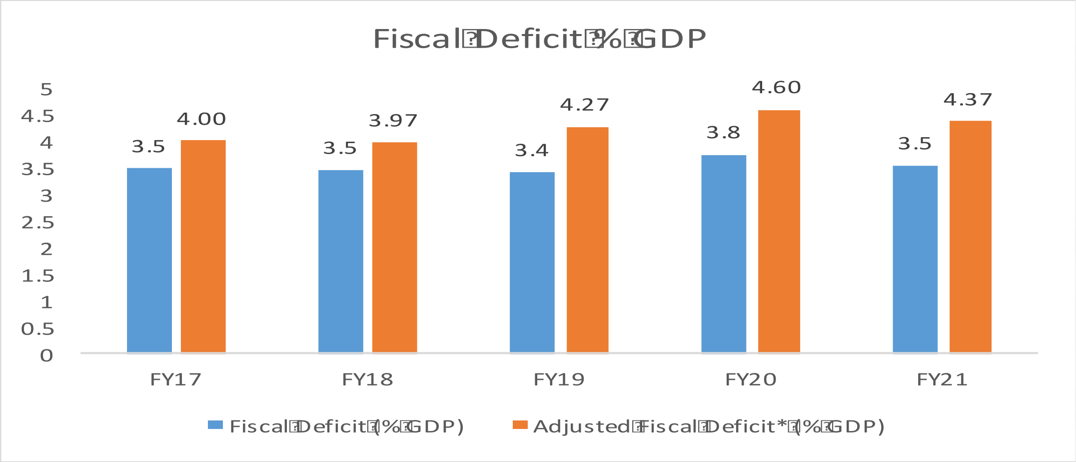
Off balance sheet spending continues to provide support

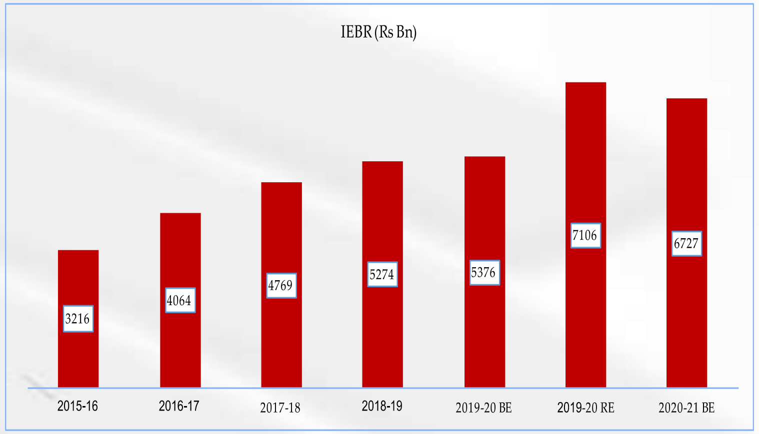
Adjusted Fiscal deficit for the year is at 4.37% (this includes GOI serviced bonds and FCI borrowings)



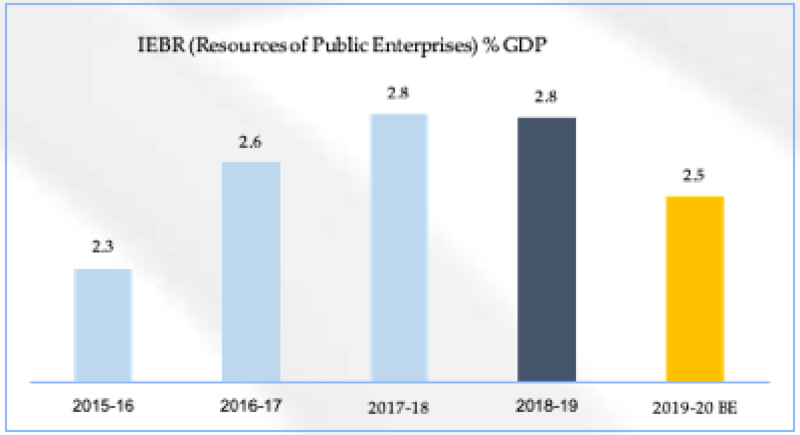
Spending through EBR expected to rise by 11% in FY21

(in INR, Bn)	FY20BE	FY20RE	FY21 BE
Health			
PM Swasthya Suraksha Yojana	50	27	30
Housing			
PM-Awas Yojana (Urban)	200	100	100
Education			
Revitalising Infra & Systems in higher education	50	10	30
Water			
Ploavaram Irrigation Project	-	18.5	-
PM Krishi Sinchai Yojana	48.8	30.3	50
Drinking Water & Sanitation			
Swachh Bharta Mission (Rural)	50	50	-
National Rural Drinking Water Programme	63	20	120
Energy			
PM Kusum	8.22	5	10
Power			
Saubhagya	90	85	55
Rural Developemnt			
PM-Awas Yojana(Rural)	-	100	100
Shipping			
Inland Waterways Authority of India Projects	10		
Total EBR (GoI Serviced Bonds)	570	446	495

IEBR budgeted to be lower in FY21 compared to FY20, but remains high compared to past trends



The total IEBR is expected to be at 2.5% of GDP compared to 2.8% in FY20



Source: Budget Documents, HDFC Bank

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The Positives: The budget attempts to attract foreign flows as domestic savings remain under stress

The abolishment of the Dividend Distribution tax, 100% exemptions for the flows coming in through the sovereign wealth funds, raising the limit for FPI in corporate bonds to 15% (from 9%), focus on infrastructure push (through the National Infrastructure pipeline) are likely to help garner foreign flows when domestic savings continue to decline.

- Government securities (G-Sec) to open for Non-Resident Investors
- Non-Debt ETF consisting of government securities to be launched
- Deposit insurance coverage to be increased to INR 5 lakh vs. INR 1 lakh at present
- Limit for NBFCs to be eligible for debt recovery under SARFAESI to be reduced to an asset size of INR 100 crs from INR 500 crs
- A partial credit guarantee scheme to address liquidity constraints of non-banking financial companies (NBFCs) and hosing finance companies (HFCs)

- Dividend Distribution tax removed. Dividends to be taxed only in the hands of investors
- Tax concession for sovereign wealth funds of foreign government
- Benefit of corporate tax cut of 15% extended to new domestic companies engaged in power generation
- Concessional withholding tax rate of 5% extended till June 2023 .
  Concessional withholding tax rate of 5% on interest paid on municipal bonds
- FPI limits in corporate bonds to be raised to 15% from 9%
- Reduction in withholding tax rate to 4% from 5% on interest paid on listed bonds

Source: Budget Documents, HDFC Bank

UDAY

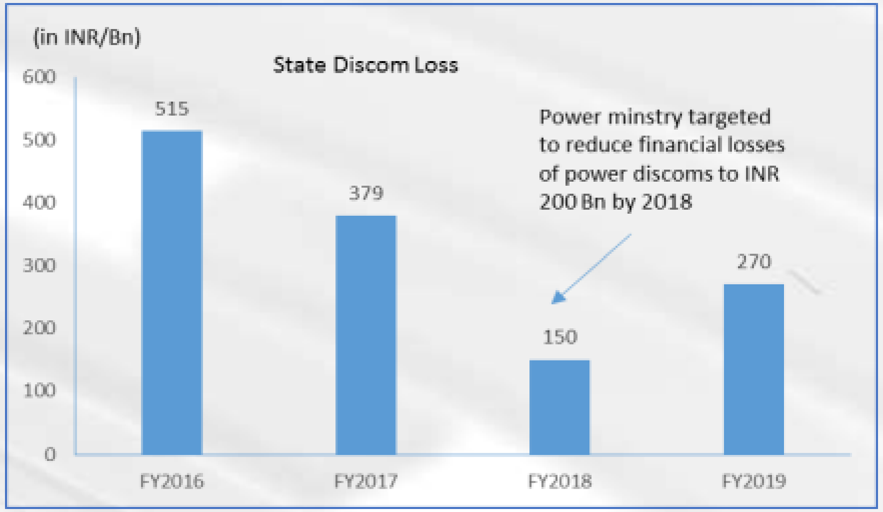
Launch Date: 15th December 2015

Central Budgetary Support- Nil

Objective- To reduce losses of power distribution companies and make them financially viable with an aim to provide 24*7 power supply. Under this scheme, state governments took over 75% of discom debt and agreed to fund future losses in a progressive manner.

Target- **To reduce AT&C (aggregate technical &commercial) losses to 15% and eliminate gap between ARR (average revenue realized) & ACS (average cost of supply) by F2019.**

*In addition to UDAY, **Deen Dayal Upadhayay Gram Jyoti Yojana** which focuses on **rural electrification** and **Integrated Power Supply Scheme** aimed at providing **capex related assistance to discoms** are also in place.*



Progress so far

- **Discom losses after reducing between FY16 and FY18 are again rising.** In FY2019, losses rose to INR 270 Bn, indicating the need to revamp existing scheme.
- **Scheme was able to reduce AT&C losses to 18.79% in F2019 from 21% in F2016. However, losses are rising again, currently AT&C losses are tracking at 21.3%, close to pre-UDAY level.**
- In line with AT &C losses, gap between ACS and ARR reduced to INR 0.33/kwh by Dec-18. However, it is again on upward trend. Currently, the gap is tracking at INR 0.38/kwh.
- Furthermore, there remains a wide difference between the state performances.

EXPECTATION

Power Minster highlighted that a revamped integrated scheme subsuming all power related schemes aimed at reducing power sector losses is under consideration. New scheme "ADITYA" was expected to be announced in FY21 budget.

OUTCOME

FM highlighted that the government intends to promote usage of "smart metering". It envisages to replace conventional energy meters by smart meters across country in next three years. She also mentioned that further measures to reform DISCOMs will be taken.

Budget allocation for power sector is INR 220 Bn for FY21 vs INR 198 Bn in FY20 (RE)

Source: Budget Documents, HDFC Bank

Treasury Economics Research Team

Abheek Barua
Chief Economist
Phone number: +91 (0) 124-4664305
Email ID: abheek.barua@hdfcbank.com

Sakshi Gupta
Senior Economist
Phone number: +91 (0) 124-4664338
Email ID: sakshi.gupta3@hdfcbank.com

Avni Jain
Economist
Phone number: +91 (0) 124-4664354
Email ID: avni.jain@hdfcbank.com

Swati Arora
Economist
Phone number: +91 (0) 124-4664354
Email ID: swati.arora1@hdfcbank.com