

## Budget 2025 Preview: Spending growth likely to be increased in FY25

Fiscal deficit target could be reduced to 5% of GDP in FY25

- The Bharatiya Janata Party (BJP)-led National Democratic Alliance (NDA) has retained power for the third consecutive term, albeit with a narrower majority (293 seats) than expected (Exit Poll predictions of ~370 seats and BJP's own ambitious target of 400+ seats). The BJP fell short of a single-party majority (won 240 seats) in the 543-seat lower house of parliament for the first time since its government came to power in 2014, leading to the formation of a coalition government in 2024. The return of BJP-led coalition government makes NDA-I during FY00 and FY04 a relevant episode.
- Accordingly, this note serves two purposes – 1) it provides a comprehensive comparison of the fiscal performance of different Union governments during the past 25 years, starting from NDA-I (FY00-04), led by Mr. Atal Bihari Vajpayee, till BJP-II (FY20-24), and 2) it also shares our key expectations from the Budget 2025 to be presented next month.

### 1. Fiscal performance during the past 25 years<sup>1</sup>:

Fiscal deficit:

- It would not be unfair to state that the bottom line, or the fiscal deficit, has been on the minds of almost all finance ministers in the past many decades. Although the Fiscal Responsibility and Budget Management (FRBM) Act came into force only in 2003, various governments, even in the 1970s and 1980s, were well aware of the adverse consequences of a high fiscal deficit. During the past two decades (since FRBM Act), while the Union Government has never been able to bring down its fiscal deficit to 3% of GDP (3.4% of GDP in FY07-08 and 3.5% of GDP in FY17-19), the government has seen it rise only during the two global events, namely the Great Financial Crisis of 2008 and the Covid pandemic in 2020 (*Exhibit 1*). *We continue to believe that the new coalition government will narrow its fiscal deficit target of 4.5% of GDP by FY26 (and hopefully, further down to 3.5% by FY30).*

Total receipts:

- Like others, this government's ability to meet targets would be determined by buoyancy in receipts. The only way to achieve deficit targets with weak receipts is by suppressing spending disproportionately, which is a risky proposition. *India's aggregate tax receipts hit an all-time high in FY22 (beating the previous high of FY08), and surpassed it further in the last two years.* However, the share of states has increased during the past 15 years, leaving only ~45% of total taxes with the Center. Therefore, the Center's net taxes in FY24 were still much lower than in FY08 (*Exhibit 2*). Further, the share of taxes in the Center's total receipts has also increased to 85% in recent years from as low as 60% during NDA-I and ~75% during the UPA-I (FY05-09).
- There are two more interesting facts about receipts: 1) direct taxes grew faster than indirect taxes during all periods, except in BJP-I, and 2) corporate income taxes grew faster than non-corporate (or personal) income taxes during the first decade of the century, after which the latter took over the former – from UPA-II (FY10-14) to BJP-II (*Exhibits 3 and 4*).

Total spending:

- Interestingly, a look at the last five five-year period averages reveals that the average growth in total spending lagged that of total receipts during NDA-I (FY00-04), UPA-II (FY10-14) and BJP-I (FY15-19) periods. While spending growth averages ranged from 8.2% (during BJP-I period) to 14.5% (during BJP-II period), receipts growth averages ranged between 9.6% (BJP-I) and 15.9% (NDA-I). Consequently, the fiscal deficit narrowed during NDA-I and BJP-I periods and widened during BJP-II. Since the 2008 GFC was at the fag end of UPA-I, the deficit during UPA-II was higher than the former, despite the fact that spending growth was slower than receipt growth in the latter period (*Exhibits 5 and 6*).
- As expected, average spending growth during UPA-I (led by 2008 GFC) and BJP-II (led by the pandemic) was the highest at 13.8% and 14.5%, respectively, while it was only 8.2% during BJP-I. Details suggest that: a) the average growth in non-discretionary revenue spending (interest payments, salaries & pensions) was slower than discretionary spending during NDA-I, UPA-I and BJP-II periods, while capital spending growth was the highest in all periods, except in UPA-I (*Exhibit 7*); b) rural spending (including Ministry of Agriculture and Farmers' Welfare, department of fertilizers, Department of Drinking Water and Sanitation, Ministry of Panchayati Raj and Ministry of Rural development) grew faster than total spending during UPA-I and the two episodes of BJP-majority, while it was almost stagnant during UPA-II (*Exhibit 8*).

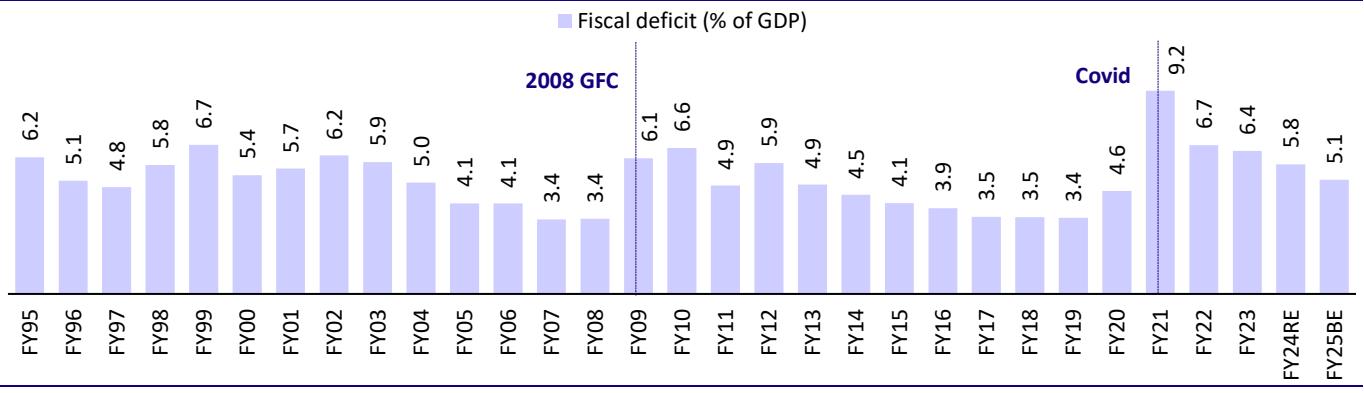
### Total capex (Center + CPSEs):

- Lastly, we must remember that budgeted capex is only one part of the planned capex by the central government. Central public sector enterprises (CPSEs) also account for a significant portion of total capex by the central government. A huge change has happened in this area, due to which analyzing only budgeted capex is misleading. CPSEs' capex (excluding Food Corporation of India, FCI) has declined for the fourth consecutive year in FY24RE, due to which it shrank by an average 7.1% during BJP-II (*Exhibit 9*). What is more important, however, is the fact that the combined total capex grew 9.4% (simple annual average) during BJP-II, the slowest in the five episodes and compared to a very stable 11-13% during the previous three episodes and as high as 17% during NDA-I (*Exhibit 10*).
- The combined capex, therefore, averaged 3.7% of GDP each in the last two periods (of BJP-majority), compared to 4.6%/3.9% of GDP during UPA-I/UPA-II and 4.4% during NDA-I (*Exhibit 11*). It was 3.7% of GDP in FY24RE vs. its three-decade peak of 5.3% of GDP in FY04.

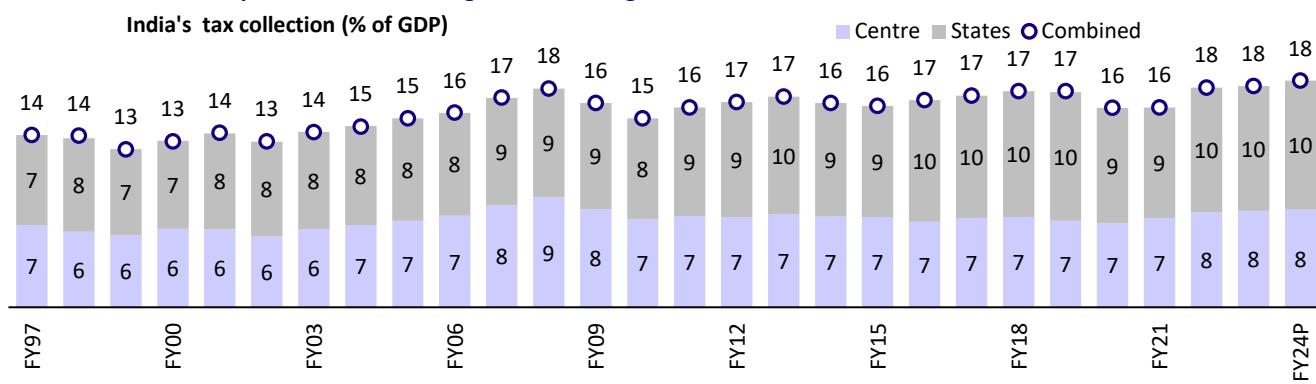
### 2. Budget 2025 Preview:

- From the Budget 2025 perspective, we believe that the new government will largely retain its tax and non-debt capital receipt (including disinvestment) projections as presented during the Interim Budget in Feb'24. If so, a transfer of INR2.11t by the RBI implies excess receipts of about INR1.5t in FY25. *A large part of these additional receipts, we believe, would be spent under various heads, while a small portion could be used to reduce the fiscal deficit (Exhibit 12)*.
- INR300-400b could be utilized to reduce the fiscal deficit to 5% of GDP, from the 5.1% of GDP announced in the Interim Budget.
  - One of the ways to spend additional resources could be to provide more capex-related loans to states, which would also make the Center's total capital spending (including loans & advances) look better. The Center budgeted INR1.4t to states and UTs as loans & advances in FY25 in the Interim Budget, which could be increased by INR300-400b.
  - Similarly, if the government decides to revise the installments under PM-KISAN by 50% to INR9,000 per annum, it would entail the cost of another INR300b to the exchequer.
  - The remaining INR500b could be used by the Union Government to provide some more incentives to the taxpayers to shift to the new tax regime and to expand on housing schemes or various other schemes.
  - Overall, we do not expect the government to divert from its fiscal deficit consolidation path while improving the quality of fiscal spending. It is, however, very likely that fiscal spending could be increased (vs. Feb'24 budget), due to higher receipts led by the RBI dividend.
- *Can upcoming state assembly elections in Maharashtra, Haryana and Jharkhand influence the upcoming budget allocations?* We see a low probability of this and there are several reasons behind it. *First*, it is now amply clear that the voting patterns in state and general elections tend to be very different. *Second*, while the supporters of a rural economy package point to the poor performance of the BJP in Uttar Pradesh and Maharashtra, it does not gel with its exceptional win in Bihar and Madhya Pradesh. *Third*, it is highly unlikely that tax incentives for the middle-class and poor Indians would be seen by voters in the election-bound states as exclusive policies for them. More importantly, a list of a large package of freebies, which was included in the Congress manifesto but was largely absent in the BJP manifesto, reflects the maturity of voters in the country. *Lastly*, we believe the results of Maharashtra assembly elections would be largely driven by the state politics, rather than national policies.
- The mandate of the BJP in NDA-II (starting FY25) is much stronger than during NDA-I. This was quite visible in the Cabinet allocation, wherein the BJP retained most of the high-profile departments with their ministers (such as home, defence, finance, external affairs, road transport and highways, among others). During the past decade, the BJP has very carefully created an image of a clean government, minimizing wasteful spending and corruption, making the Budget more transparent by reducing off-budget expenditure/borrowings leading to higher capex allocation, resisting calls for large rural support, and maintaining fiscal prudence. We strongly believe (and hope) that there will not be substantial changes in its mindset/philosophy, creating policy continuity. Coalition politics, however, could make it more challenging to pass legislation on the more ambitious parts of the government reform agenda in areas like agriculture, land, labor and judicial, which are usually out of Budgets.

<sup>1</sup>We have used FY24 revised estimates (FY24REs) for the center and CPSEs for this entire section, as provisional estimates (FY24P) are not available in some areas. It does not change any broad conclusions

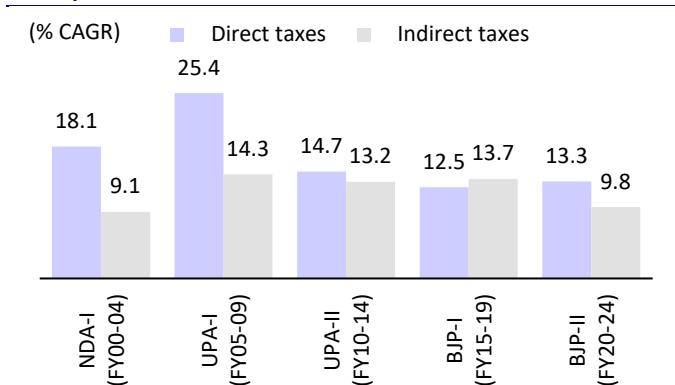
**Exhibit 1: Long-term trends of the Union government's fiscal deficit**

Source: Union Budget documents, CSO, MOFSL

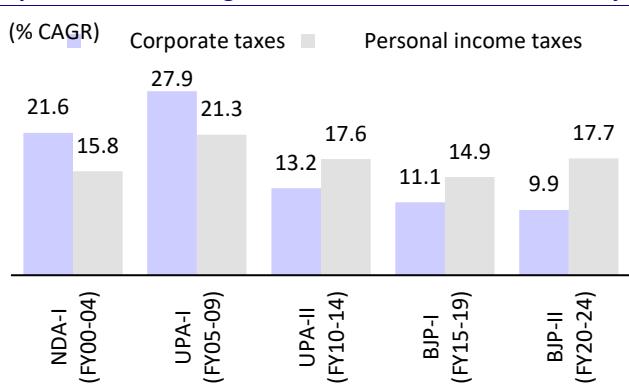
**Exhibit 2: India's tax receipts are at all-time high, but with higher share of states**

Gross taxes (excluding cesses and surcharges) are distributed between the center and state based on finance commission's recommendations  
FY24P for center; our estimates for states

Source: Union/State Budget documents, CSO, RBI, MOFSL

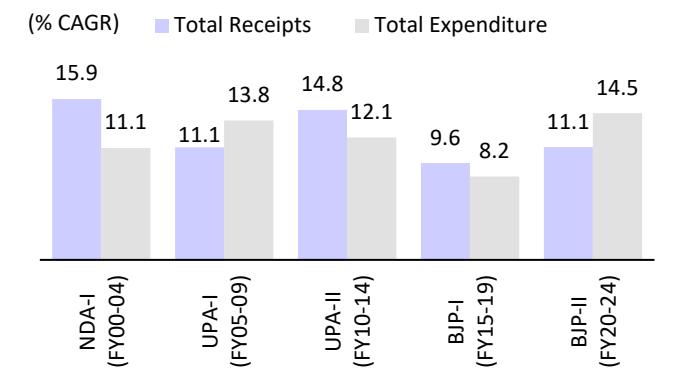
**Exhibit 3: Direct taxes grew faster than indirect taxes during most periods**

Direct taxes include corporation income taxes and non-corporate (also called personal) income taxes

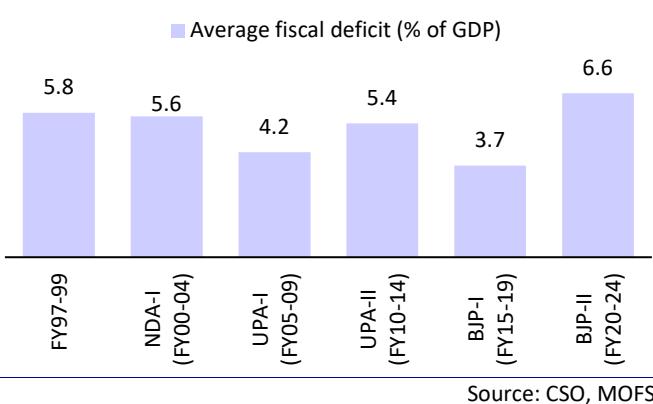
**Exhibit 4: Corporate income taxes grew faster than non-corporate taxes during the first decade of the 21<sup>st</sup> century**

Source: Union Budget documents, CGA, MOFSL

**Exhibit 5: Fiscal spending grew slower than fiscal receipts during three periods...**

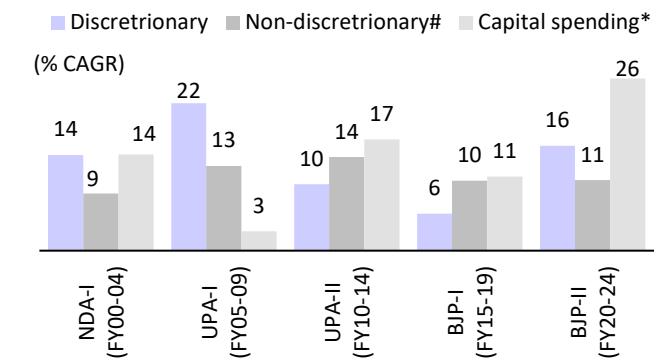


**Exhibit 6: ...and thus, fiscal deficit narrowed during NDA-I and BJP-I periods**



Source: CSO, MOFSL

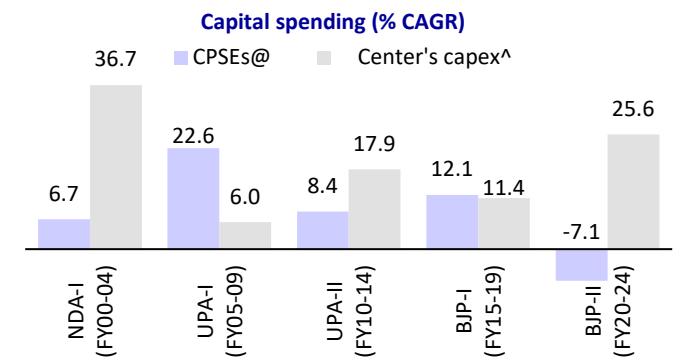
**Exhibit 7: Capex\* spending has increased at fastest pace in all periods except UPA-I**



# Interest, salaries & pension

\*Including loans & advances (L&As)

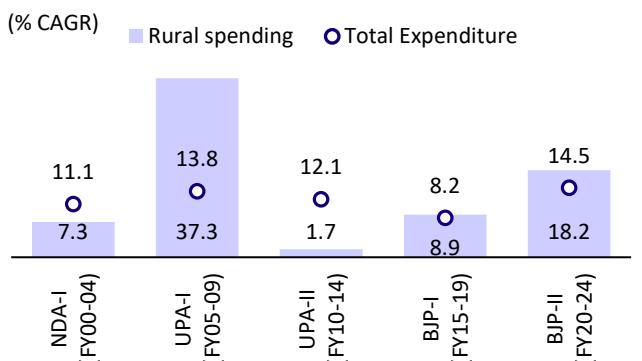
**Exhibit 9: CPSEs' capex declined for the first time during BJP-II period...**



@ CPSEs capex (EX-FCI) is REs prior to FY10

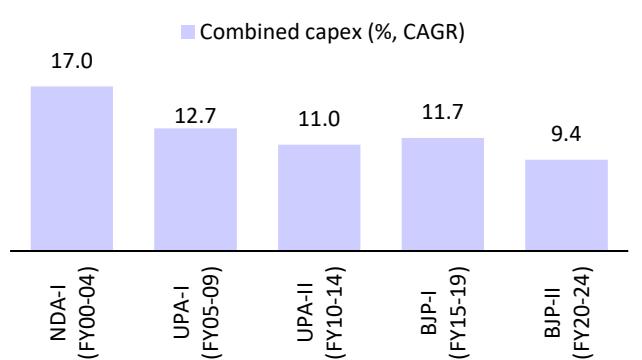
^Excluding L&As

**Exhibit 8: Rural spending growth grew faster than total expenditure during the past decade**



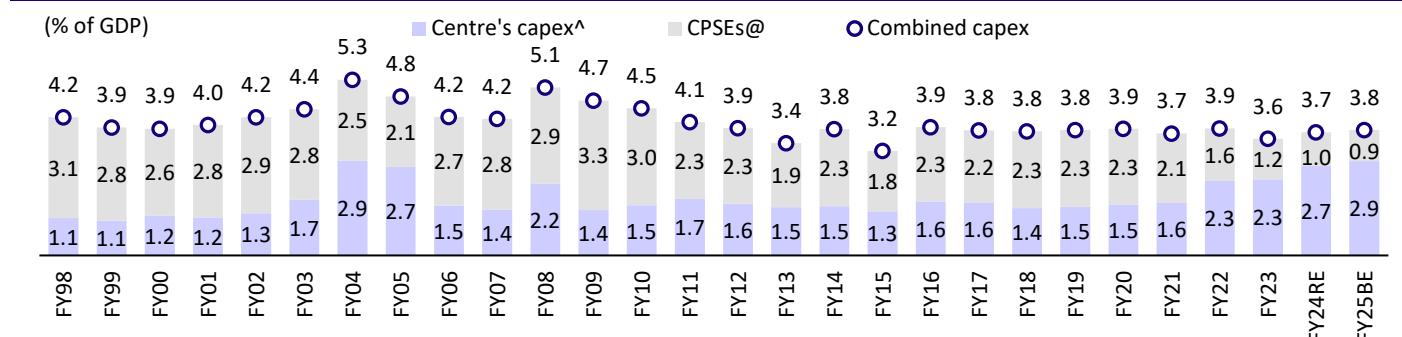
Source: CSO, MOFSL

**Exhibit 10: ...which dragged down the average growth of the combined capex**



Source: Union Budget documents, MOFSL

**Exhibit 11: Combined capex of the central government has been unchanged in the last five years**



^ Excluding loans and advances

@CPSEs capex (ex-FCI) data is revised estimates prior to FY10  
Source: Union/State Budget documents, CSO, RBI, MOFSL

## Exhibit 12: What could the fiscal math look like?

	FY23	FY24P	YoY (%)	FY25BE\$		FY25BE^	
	INRb	INRb		INRb	YoY (%)	INRb	YoY (%)
<b>Total receipts</b>	<b>24,554</b>	<b>27,889</b>	<b>13.6</b>	<b>30,803</b>	<b>10.4</b>	<b>32,303</b>	<b>15.8</b>
Revenue receipts	23,832	27,284	14.5	30,013	10.0	31,513	15.5
Gross taxes	30,542	34,648	13.4	38,308	10.6	38,308	10.6
Net taxes	20,978	23,265	10.9	26,016	11.8	26,016	11.8
Direct taxes	16,591	19,220	15.8	21,988	14.4	21,988	14.4
Corporation taxes	8,258	9,111	10.3	10,428	14.5	10,428	14.5
Income taxes	8,333	10,109	21.3	11,560	14.3	11,560	14.3
Indirect taxes	14,951	15,428	10.6	16,320	5.8	16,320	5.8
Goods & Services Tax (GST)	8,491	9,621	13.3	10,677	11.0	10,677	11.0
Customs	2,134	2,331	9.2	2,313	-0.8	2,313	-0.8
Excise Duties	3,190	3,053	-4.3	3,188	4.4	3,188	4.4
Less: Devolution to states	9,484	11,295	19.0	12,198	8.0	12,198	8.0
Non-tax revenue receipts	2,854	4,019	40.8	3,997	-0.5	5,497	36.8
Non-debt capital receipts	722	605	-16.3	790	30.7	790	30.7
Divestment	460	331	-28.0	500	51.0	500	51.0
<b>Total expenditure</b>	<b>41,932</b>	<b>44,425</b>	<b>5.9</b>	<b>47,658</b>	<b>7.3</b>	<b>48,797</b>	<b>9.8</b>
Primary expenditure*	27,337	29,651	10.4	31,942	7.7	33,081	11.6
Revenue expenditure	34,531	34,940	1.2	36,547	4.6	37,297	6.7
Interest payments	9,285	10,639	14.6	11,904	11.9	11,904	11.9
Subsidies#	5,310	4,135	-28.4	3,812	-7.8	3,812	-7.8
Defense	2,562	2,904	13.4	2,828	-2.6	2,828	-2.6
Pensions	2,416	2,380	-1.5	2,396	0.7	2,396	0.7
Other	14,958	14,881	-0.5	15,607	4.9	16,357	9.9
Capital spending	7,400	9,485	28.2	11,111	17.1	11,500	21.2
Defense	1,429	1,543	7.9	1,720	11.5	1,720	11.5
Railways	1,593	2,426	52.3	2,520	3.9	2,520	3.9
Roads & Highways	2,060	2,639	28.1	2,722	3.2	2,722	3.1
Others	2,318	2,877	24.1	4,149	44.2	4,538	57.7
<b>Fiscal deficit</b>	<b>17,378</b>	<b>16,537</b>		<b>16,855</b>		<b>16,493</b>	
<b>Fiscal deficit (as a percentage of GDP)</b>	<b>6.4</b>	<b>5.6</b>		<b>5.1</b>		<b>5.0</b>	
<b>Nominal GDP</b>	<b>2,69,496</b>	<b>2,95,357</b>	<b>9.6</b>	<b>3,27,718</b>	<b>11.0</b>	<b>3,27,253</b>	<b>10.8</b>
<b>Memo:</b>							
Capex@ (Capital outlays)	6,248	7,874	26.0	9,396	19.3	9,396	19.3
Net market borrowings~	12,178	12,676	4.1	12,252	-7.3	12,000	-5.3
Net market borrowings (% of GDP)	4.5	4.3		3.7		3.7	

\$As per the Interim Budget presented in Feb'24 (% YoY over FY24P)

^Our expectations for the Budget to be presented in Jul'24

\* Total expenditure excluding interest and subsidies

# For major subsidies only

@ Excluding loans & advances

~Including market loans, switching, POLIFs and short-term borrowings

Red data highlights the expected changes vis-à-vis interim Budget

Source: Union Budget documents, CGA, CSO, MOFSL

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Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	> - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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