Spending to get back growth impulses

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By focussing on infra spending, divestment and financial sector reforms, Finance Minister has laid the ground for growth revival

The Finance Minister did the unthinkable by front-loading spending in FY21 itself to ₹34.5-lakh crore, a steep increase of 28.4 per cent over last year's level. While spending has seen a significant lift, the Centre's revenue collections are estimated to fall by 7.7 per cent to ₹15.6-lakh crore.

Disinvestment receipts are also estimated at only ₹32,000 crore this year. As a result, the fiscal deficit for FY21 (RE) is now estimated at ₹18.5-lakh crore, or 9.5 per cent of GDP.

Sector-wise, the Centre has allocated ₹4.2-lakh crore to food procurement and distribution, a steep jump of more than ₹3.1 lakh crore (1.6 per cent of GDP) from ₹1.08-lakh crore in FY20. Even the fertiliser subsidy has seen a sharp increase of more than ₹52,000 crore to ₹1.3-lakh crore. The Finance Minister has also allocated ₹1.1-lakh crore for MNREGA this year which is ₹40,000 crore higher than last year.

Spending on roads and railways has also seen a sharp jump of ₹65,000 crore at ₹2.18-lakh crore. Similarly, the Centre will transfer additional ₹94,000 crore this year to States and UTs for spending on key schemes and projects. Given that the spending is being financed through higher borrowing, the Centre's interest outgo is estimated to increase by ₹80,000 crore this year itself.

Such a large fiscal impulse this year is positive for growth. Direct tax collections — both corporate and income tax — have seen a substantial jump in Q3 compared to H1. The Finance Minister has budgeted for a 22 per cent increase in direct tax collections next year, which seems achievable.

Disinvestment push

The Budget has targeted ₹1.75-lakh crore from disinvestments next year, which include IPO of LIC and disinvestment/strategic sale of Air India, BPCL, BEML and now two public sector banks and one insurance company.

After such a big splurge in FY21 itself, the Finance Minister has pegged the overall expenditure higher by only 1 per cent in FY22 (BE) at ₹34.8-lakh crore. While revenues (including disinvestment) are estimated to increase by 24 per cent to ₹19.9-lakh crore, much of it would go to pay the short-term borrowing and funds raised from small savings. This will bring fiscal deficit to 6.8 per cent of GDP in FY22 (BE). The Centre will still have to borrow ₹12.05-lakh crore next year to meet its targeted spend. No wonder long-end yields have increased by more than 20bps since the announcement of the Budget.

More than the numbers, the essence of the Budget lies in its intent. The government has been carrying out structural reforms to kick-start the investment cycle. First, it reduced corporate taxes. Second, it introduced production linked incentive scheme for 13 sectors. Third, it introduced four labour codes to replace a number of labour laws. Now, the government is

looking at monetising assets such as transmission lines, gas distribution networks and even privatising public sector banks and an insurance company to fund growth.

Infrastructure thrust

Infrastructure and capital spending in the Budget has been raised to 2.5 per cent of GDP. An infrastructure bank is being set up to fund infra projects with an initial capital of ₹20,000 crore to create assets of ₹5-lakh crore in three years.

To clean up the books of public sector banks, an asset reconstruction and management company will be set up, which will enable quicker resolution of stressed assets and recovery, opening up room for lending by PSBs.

Equity markets were taken by surprise with the government's move to finance expenditure through borrowing rather than raising taxes. A buoyant capital market will ensure availability of adequate resources to fund government's privatisation agenda and provide financing to private sector to fund growth. Foreign Portfolio Investors invested $23 billion in Indian equity markets in the last calendar year. However, fixed income investors have been reducing their India exposure. Despite this, yields have been falling as banks and the RBI have turned large buyers in the current financial year. The fiscal glide path given in the Budget envisages reduction in fiscal deficit to 4.5 per cent of GDP in FY26 from 6.5 per cent in FY22.

This implies gradual fiscal consolidation. This also implies elevated level of Centre and States' borrowing. While banks have had limited opportunity to lend this year and thus have been deploying deposits in government bonds, an economic recovery will lead to higher demand for credit. This is likely to put upward pressure on interest rates next year. The rate cycle in India seems to have bottomed out.

The Finance Minister has created an environment of growth by stepping up on spending when most required. The commitment to spend by monetising assets will create a positive feedback loop. India's medium-term growth prospects look lot better now.

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