24 Jan 2024

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FY25 Budget Preview

With 2024-25 budget being an interim one, government will focus on maintaining continuity of policies, while committing itself to the path of fiscal consolidation. We expect centre to achieve its fiscal deficit target of 5.9% in FY24, with risks titled to the upside. These risks emerge from: lower than anticipated nominal GDP growth, and higher than budgeted expenditure. From these levels, government is expected to reduce deficit target by ~50bps in FY25BE, thus targeting 5.4-5.5% range in our base case scenario. In the wake of weak monsoon, and subdued Rabi sowing, budget will focus on steering rural growth. For this, enhanced spending on MGNREGA, PM KISAN, and PMAY can be expected. Driving investment growth will be another focus area for the government. We thus expect Rs 1.5-2 lakh crore incremental increase in capex for the next year. Markets will also keep a watchful eye on government's borrowing program, which is anticipated to increase only marginally next year.

Expectations from FY25 Budget

Focus to remain on consolidation

Since the latest budget presentation for 2024-25 (FY25) will be an interim budget before the General Elections of 2024, no significant announcements are expected to be made. Government will try maintaining continuity of policies and schemes already announced, while sticking to its path of fiscal consolidation. For the central government to reach its target of 4.5% fiscal deficit target by FY26, it is likely to announce ~50bps reduction in fiscal deficit target for FY25. Challenges that may emerge include: normalisation of nominal GDP and hence receipt growth. On the other hand, quality of expenditure is unlikely to be compromised upon for two reasons—one, to crowd in private investments by boosting government capex (RBI monthly bulletin reaffirms this trend), two, to support growth and maintain continuity of key social schemes. We give here our expectations, which have been placed forth keeping in mind the practical side of fiscal space that will be available.

Key themes: Steering rural growth and investment

Given a weaker than expected monsoon in FY24 and muted Rabi sowing (+0.2% as of 19 Jan 2024), government through its budget will aim to give rural growth a boost. Government capex is also expected to maintain a healthy pace of growth to give nudge to private investment. To support these agendas, government may:

- Increase the budget allocation for PM Kisan Samman Nidhi (PM-KISAN) scheme from Rs 60,000 crore in FY24BE to ~Rs 70-75,000 crore in FY25.
- Increase the budget allocation for MG-NREGA scheme from Rs 60,000 crore in FY24BE to ~Rs 80-85,000 crore in FY25.
- Provisions under affordable housing (rural and urban) are expected to touch ~Rs 1 lakh crore from ~Rs 80,000 crore as FY24BE.
- Announce measures to incentivise homes to switch to solar power.
- May also announce next set of FAME subsidies.
- Retain focus on capex and increase it to ~Rs 11.5-12 lakh crore.

On the **taxes side** no major changes are expected, as this is an interim budget. However, certain proposals may get importance:

- To help sustain consumption growth, and lighten the burden of consumers due to elevated prices in recent years, government may increase limit under standard deductions.
- In order to attract more tax payers to adopt the new tax regime, some incentives may be announced.
- To boost sustainable tourism, tax incentives for hotels/home stays adopting environment friendly practices can also be expected.
- Custom duties on finished products of certain items may again be raised to correct the inverted duty structure (such as palm oil, refined glycerine).
- Savings under section 80C can be relooked and increased to encourage savings.

Fiscal consolidation: FD 5.4-5.5% of GDP in FY25

Fiscal deficit (FD) in FY25 will get support from a normalization in domestic conditions. In the year ahead, even as global growth is expected to slow down, domestic growth is expected remain broadly stable. This will impact both real and nominal GDP, thus giving more room for the government to push fiscal deficit ratio to a lower level. Further, as the economic activity remains steady and is driven by domestic factors (consumption and investment), revenue growth of the government will also improve. Lower rate of inflation will help boost consumption and government's infra spending will provide support to investments. Assuming this, nominal GDP is estimated to register ~10-11% growth in FY25 (slightly up from 8.9% in FY24), fiscal deficit is expected to come in at ~Rs 17.5-18 lakh crore, implying a deficit of ~5.4-5.5% (~50bps less than FY24's target of 5.9%).

Gross borrowing programme

In FY24, government is expected to meet its gross borrowing target of Rs 15.4 lakh crore and net borrowing target of Rs 11.8 lakh crore. Despite better than expected revenue collections, government will maintain the target, on account of higher than anticipated spending and due to shortfall on part of disinvestment receipts.

In FY25, even as revenue collections are expected to come off a high base, net borrowing is estimated to increase only marginally to ~Rs 12-12.5 lakh crore. Along with repayments of Rs 3.7 lakh crore, this implies a gross borrowing of around Rs 15.7-16.2 lakh crore.

It must be pointed out here that next year the government will also have access to more FPI due to the inclusion of Indian bonds in JP Morgan Global Bonds Index. It has been announced that from Jun'24 onwards, 23 sovereign Indian bonds will be included in the index. Till Mar'25, this is expected to bring additional inflows to the tune of Rs 1.7-2.6 lakh crore. In case inflows are towards the higher end of the bracket then overall gross and net borrowing targets may be reduced for FY25.

Subsidy levels

Following sharper than estimated jump in subsidies in FY24, they are expected to be rationalised in FY25. In FY24, government had budgeted Rs 3.7 lakh crore for major subsidies (food, fertilizer and petroleum). However, with the extension of PM-Garib Kalyan Anna Yojna (PMGKAY) for the next five years, food subsidy bill is expected to go up by ~Rs 35-40k crore in FY24. As no cuts are expected in case of other subsidies, this will push the overall subsidy burden to ~Rs 4-4.2 lakh crore in FY24. From that level, the burden is expected to come down to ~Rs 3.9-4 lakh crore in the next financial year. Trimming will be visible across segments, with food subsidy expected to be contained in the range of Rs 2-2.5 lakh crore, and fertilizer subsidy at ~Rs 1-1.5 lakh crore. Subdued international commodity prices (LNG and Brent), will help keeping both fertilizer and petroleum subsidies in check in FY25.

Fig 1 – Subsidy breakdown

(Rs lakh crore)	FY23PA	FY24BE	FY24E	FY25E
Food	2.73	1.97	2.36	2.40
Fertilizer	2.51	1.75	1.75	1.50
Fuel	0.07	0.02	0.04	0.03
Total	5.31	3.75	4.15	3.93

Source: CEIC, Union Budget Documents, Bank of Baroda Research | Note: PA- Provisional Actuals, BE-Budget Estimates, E-Bank of Baroda estimates

Interest payments

With interest rates remaining elevated in recent period, interest cost burden is estimated to increase at a steady pace in FY25. Following estimated 16% increase in FY24 (Rs 10.8 lakh crore), interest payment is expected to increase to Rs 12.4 lakh crore (+15%) in the next fiscal year.

Fig 2 – Interest burden

(Rs lakh crore)	FY23PA	FY24BE	FY24E	FY25E
Interest payments	9.28	10.80	10.80	12.42

Source: CEIC, Union Budget Documents, Bank of Baroda Research | Note: PA- Provisional Actuals, BE-Budget Estimates, E-Bank of Baroda estimates

Focus on capital expenditure to continue

To support growth and remain as the fastest growing major economy even next year, Union Government will continue to prioritize capex in order to push investments and improve the quality of expenditure. Even RBI's monthly bulletin highlights that this has helped crowd in more private investments. The report highlighted that high corporate profitability has led to increased creation of fixed assets. Home sales have also picked up pace, and the rate of real fixed investment in FY24 was at record high. We thus estimate ~20% jump (Rs 10.1 lakh crore estimated in FY24) in capex to Rs 11.5-12 lakh crore in FY25. Revenue expenditure on the other hand is estimated to increase less substantially to Rs 37.3 lakh crore from estimated Rs 35.2 lakh crore in FY24.

Fig 3 – Capex

(Rs lakh crore)	FY23PA	FY24BE	FY24E	FY25E
Capital spending	7.4	10.0	10.1	11.5-12

Source: CEIC, Union Budget Documents, Bank of Baroda Research | Note: PA- Provisional Actuals, BE-Budget Estimates, E-Bank of Baroda estimates

Size of the budget

Size of the budget is likely to range between Rs 49-50 lakh crore in FY25.

Fig 4 – Budget size

(Rs lakh crore)	FY23PA	FY24BE	FY24E	FY25E
Size	41.9	45.0	45.3	49.3

Source: CEIC, Union Budget Documents, Bank of Baroda Research | Note: PA- Provisional Actuals, BE-Budget Estimates, E-Bank of Baroda estimates

Disinvestment

Disinvestment for FY24 was targeted for Rs 61,000 crore and with current run-rate at ~Rs 10,000 crore, we do not expect this target will be met. Statement by officials suggest that sale of IDBI is not expected to be completed in the current fiscal year. In the coming months focus will be on small ticket size receipts. We thus expect a shortfall of around Rs 20,000-30,000 crore this year. In FY25, as market conditions are expected to be slightly more supportive, this may in turn enhance government's ability to attract buyers and allow receipts in the range of Rs 50-55,000 crore bracket.

Tax receipts to ease

Tax receipts

On the revenue side, tax receipts would be critical in determining the extent to which fiscal consolidation can be achieved next year. Receipts move broadly in sync with the state of the economy. This implies that as nominal GDP is expected to remain broadly steady next year, revenue growth will also stabilize.

In FY24, centre's net revenue collections are expected to register 13.6% growth (+Rs 75,000 crore) over FY23PA versus 12.1% estimated in the budget. This is owing to better than expected corporate and income tax receipts so far. Buoyancy in GST collections has also helped. On the other hand, customs and excise duty collections are expected to miss budgeted targets. In FY25, centre's net revenue is estimated to clock in at 13.4% at ~Rs 31 lakh crore. This will be led by 16.2% growth in centre's tax revenues and 20% increase in non-tax revenues.

Fig 5 – Tax receipts

(Rs lakh crore)	FY23PA	FY24BE	FY24E	FY25E
Centre's net tax revenue	21.0	23.3	23.9	27.1
Growth (%YoY)	*16.2*	*11.7*	*13.8*	*16.2*
Centre's net revenue	23.8	26.3	27.1	30.7
Growth (%YoY)	*9.8*	*12.1*	*13.6*	*13.4*

Source: CEIC, Union Budget Documents, Bank of Baroda Research | Note: PA- Provisional Actuals, BE-Budget Estimates, E-Bank of Baroda estimates

In conclusion:

As the budget presented on 1 Feb 2024 will be an interim budget, no significant announcements are expected. We expect government to stick to its path of fiscal consolidation, without compromising on quality of expenditure. In the wake of weaker monsoon and pressure seen in Rabi sowing season, focus will be on providing support to rural growth. Important schemes such as PM-KISAN, MGNAREGA, Housing for all, free food grains, will continue to hold significant importance. In addition, focus on infra spending will also remain. On the receipt front, growth is expected to stabilize, in line with nominal GDP growth. For the government to achieve fiscal consolidation, while maintaining spending momentum at the same time, we do not foresee room for any tax cuts. Borrowing program will also remain relatively unchanged. Inflows from inclusion into the JP Morgan EM index will provide additional avenue for borrowing.

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