INTERIM BUDGET 2019-20

01 February 2019

A budget for rural, middle class India

The government presented a farm and middle class focused budget as it heads towards elections. At the same time, allocation for capital formation has also been increased. Given the spending constraints, fiscal deficit has been kept at 3.4% of GDP in FY19/ 20 which led to 12% increase in net borrowings. Gross borrowings increased by 24% due to higher repayments in FY20. Lower gross borrowing with higher switches/ alternate sources will be positive for yields.

Sameer Narang
+91 22 6698 5713
chief.economist@bankofbaroda.com

Dipanwita Mazumdar
dipanwita.mazumdar@bankofbaroda.com

Jahnavi
jahnavi@bankofbaroda.com

Aditi Gupta
aditi.gupta3@bankofbaroda.com

Sonal Badhan
sonal.badhan@bankofbaroda.com

Farm focused Budget: Farm sector has benefitted the most from the Budget with Rs 200bn (0.1% of GDP) and Rs 750bn (0.36% of GDP) allocation towards a new income support scheme, PM-KISAN in FY19 and FY20 respectively. Along with an estimated Rs 2.6tn of farm loan waivers by state governments, this should push rural consumption higher.

Digital India and vision for 2030: The Finance Minister articulated his vision for modern, digital, healthy and clean India. As a first step, the allocation to Digital India was increased by 32.3% led by IT & Telecom. Health, education and Northeast too got significant increase in allocation.

Middle class to benefit: The Middle class households got a significant boost to their income with tax sops of Rs 232bn in FY20. Any individual with a taxable income of upto Rs 0.5mn will have to pay no tax. Real estate sector got a boost with exemption on capital gains and notional rent for two self-occupied houses.

Fiscal deficit at 3.4% in FY19/20: Given the spending commitment to farm sector while ensuring a boost to capital formation, the fiscal deficit for FY19 was increased to 3.4% of GDP from glide path of 3.3%. For FY20 also the fiscal deficit has been kept at 3.4% of GDP instead of glide path of 3.1% of GDP. The deviation is a result of farm distress due to low food prices.

Bond yields rise: While net market borrowings have increased only by Rs 500bn in FY20, the gross borrowing has seen a sharper increase at Rs 1.4tn (an increase of 24.3%). This is due to much higher repayments in FY20 at Rs 2.37tn compared with Rs 1.48tn in FY19. While the fiscal impulse is only marginally positive, the impact on yields may be much higher unless the gross borrowing is reduced through higher switches/ alternative sources.

KEY HIGHLIGHTS

- Farm sector and middle class remained key focus
- Fiscal deficit for FY19/FY20 estimated at 3.4% of GDP
- Net borrowing estimated at Rs 4.73tn in FY20 (Rs 4.23tn in FY19)

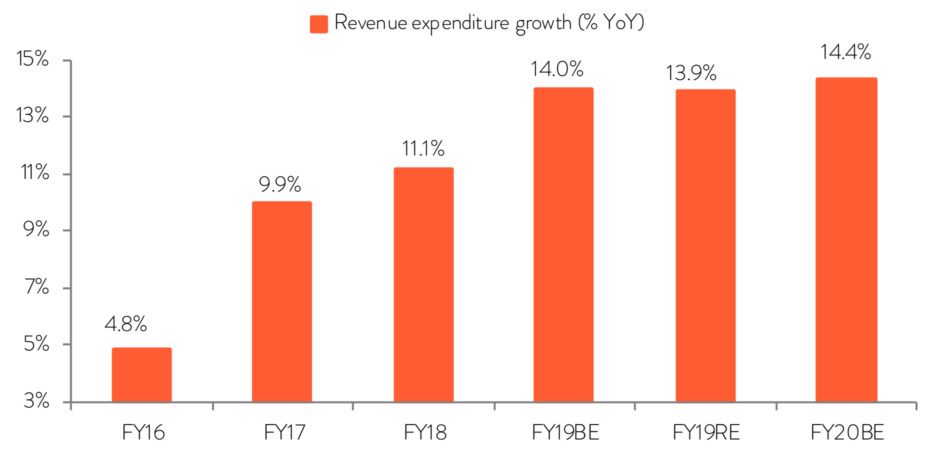
Pro-consumption budget

Farm, Digital India and pro middle class: key theme

The government's interim budget is pro-farm and middle class with both the sections of the economy getting specific benefits. While middle class will benefit through tax exemption, farmers will see direct income in their hands. For this, the government has introduced PM-KISAN program which encapsulates Rs 6,000 annual payment to each farmer with a land holding less than 2 hectares. This entails an allocation of Rs 750bn (0.36% of GDP). In addition, the government has kept the allocation for National Employment Guarantee Fund (MNREGA) at Rs 600bn.

With election on the horizon, the government has presented a pro-consumption budget with 14.4% increase in revenue expenditure compared with 13.9% increase pegged in FY19RE. The increase in revenue spending is driven by 73.2% increase in allocation to agriculture and allied activities. This is primarily driven by Rs 750bn allocation to PM-KISAN, a direct income support scheme for small farmers.

FIG 1 – REVENUE EXPENDITURE TO PICK UP



Source: Budget Documents, Bank of Baroda Research

Apart from this, subsidies have been increased by 11.4% (1.4% of GDP) compared with 39.2% increase seen in FY19RE. Food subsidy in FY20BE is now pegged at Rs 1.84tn from Rs 1.71tn in FY19RE (up by 8% compared with 71% increase in FY19) when the government implemented its scheme of ensuring gross income of 150% for farmers. However, petroleum subsidy is expected to shoot up significantly by 51% in FY20BE because of the extensive coverage of the Ujjwala Yojana.

Apart from the farm economy, digital economy has also got a large push with increase of 32.3% on IT and telecom sector. Allocation of Ministry of Communication has been raised by 27%. Even health and education sectors have seen a larger than usual increase in spending at 13.6% (5.6% in FY19RE) and 12.2% (4.3% in FY19RE).

With higher interest rates and elevated borrowing program, government's interest payments are budgeted to increase by 13.2% to Rs 6.7tn (3.2% of GDP). Defence spending is budgeted to increase by 7% to Rs 3.05tn (1.5% of GDP).

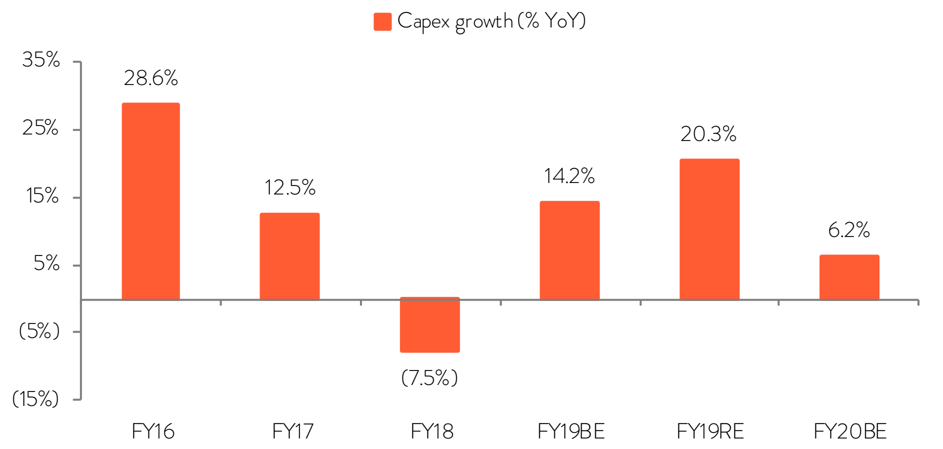
FIG 2 – EXPENDITURE PROFILE BY MINISTRY

	FY18	FY19BE	FY19RE	FY20BE
Agriculture and Allied Activities	526	638	866	1,500
YoY (%)	4.9	21.3	64.6	73.2
Development of North East	25	30	26	30
YoY (%)	0.7	19.3	4.6	14.1
Education	802	850	836	938
YoY (%)	11.4	6.0	4.3	12.2
Health	530	547	559	635
YoY (%)	35.9	3.2	5.6	13.6
Interest	5,290	5,758	5,876	6,651
YoY (%)	10.0	8.9	11.1	13.2
IT and Telecom	169	224	163	215
YoY (%)	(6.0)	32.4	(3.7)	32.3
Rural Development	1,350	1,381	1,351	1,390
YoY (%)	18.5	2.3	0.1	2.9
Urban Development	401	418	430	480
YoY (%)	8.4	4.3	7.2	11.8

Source: Budget Documents, Bank of Baroda Research

Capital spending is estimated to increase by 6.2% in FY20BE compared with an estimated 20.3% increase in FY19RE. Notably, centre's capital spending has been muted during Apr-Nov 2018 at 4%. Spending on transport sector is estimated to increase by 7.4% to Rs 1.56tn with budgetary support for roads ministry increasing by 5.5% to Rs 830bn. However, IEBR spending by NHAI is now budgeted at Rs 750bn in FY20 compared with Rs 620bn in FY19RE. On an overall basis (Centre+IEBR+Railways), capital spending is budgeted at Rs 9.5tn in FY20 compared with Rs 9.6tn (4.5% of GDP) in FY19RE (5.1% of GDP.

FIG 3 – CAPEX SPENDING TO MODERATE

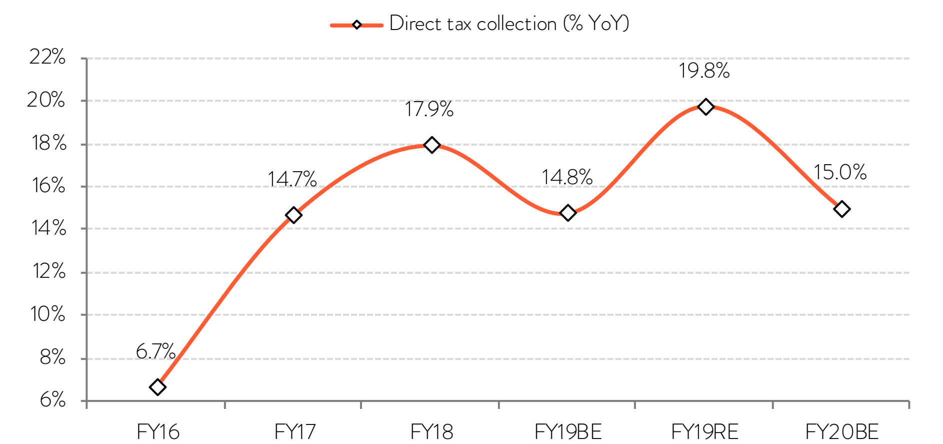


Source: Budget Documents, Bank of Baroda Research

Direct taxes to remain buoyant in FY20

Over the last three years, direct taxes have increased at an average of 17.5% led by 22.6% increase in income tax collections. Corporate tax collections have picked up in FY18 at 17.8% and FY19RE at 17.5%. The same are now budgeted to increase by 13.3% in FY20. There seems to be a room for positive surprise here. At the same time, direct tax collections are estimated to increase by 15% in FY20 as government has announced tax sops for middle income households aggregating to Rs 232bn (4.4% of Income tax collections).

FIG 4 – DIRECT TAX COLLECTIONS EXPECTED TO MODERATE



Source: Budget Documents, CEIC, Bank of Baroda Research

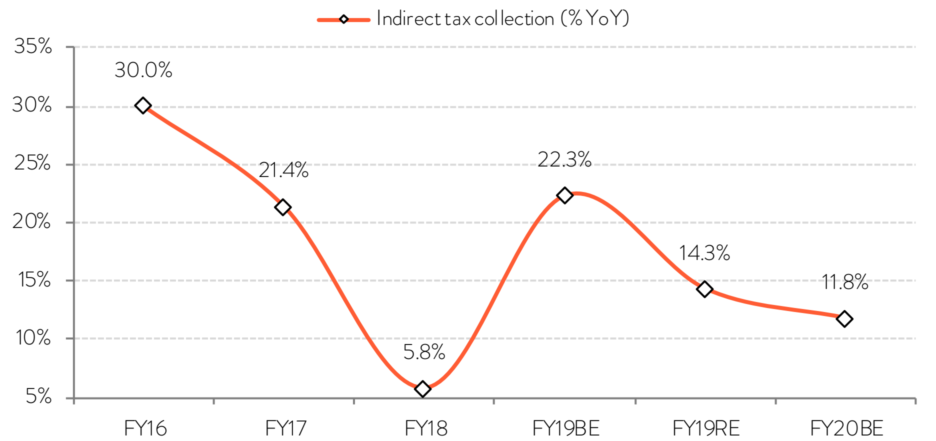
Indirect taxes have been increasing at a far lower pace. During FY19, indirect taxes are likely to increase by 14.3% compared with BE of 19.2%. The underperformance was led by CGST collections which are estimated to increase to Rs 5.03tn versus BE of Rs 6.03tn. The government has estimated a 21.1% increase in CGST collections driven by higher compliance. Notably, the current run-rate for CGST collections is Rs 372bn (Apr-Nov'18). Hence, the overall revenue collections are budgeted to increase by 13.5% with centre's tax collections increasing by 14.9% in FY20.

FIG 5 – GST COLLECTIONS

(Rs bn)	Apr-18	May-18	Jun-18	Jul-18	Aug-18	Sep-18	Oct-18	Nov-18	FY19RE	FY20BE
CGST	321	281	309	579	360	299	480	344	5,039	6,100
Change (%)	-	-	-	-	-	97.3	53.8	44.3	147.9	21.1
IGST	200	169	102	(399)	52	148	(142)	90	500	500
Change (%)	-	-	-	-	-	(51.5)	(177.4)	(51.5)	(71.7)	0
SGST*	333	433	473	678	455	481	561	433	-	-
Change (%)	-	-	-	-	-	15.8	97.9	27.0	-	-
Cess	85	72	80	80	74	79	77	79	900	1,012
Change (%)	-	-	-	-	-	(2.2)	(3.8)	11.7	43.7	12.4
Total GST	**940**	**956**	**965**	**940**	**944**	**1,007**	**976**	**947**	**6,439**	**7,612**
Change (%)	-	-	-	-	-	5.9	13.6	13.2	45.5	18.2

Source: CEIC, PIB, Bank of Baroda Research | Note: BE-Budget Estimates | *Computed from PIB and CGA data

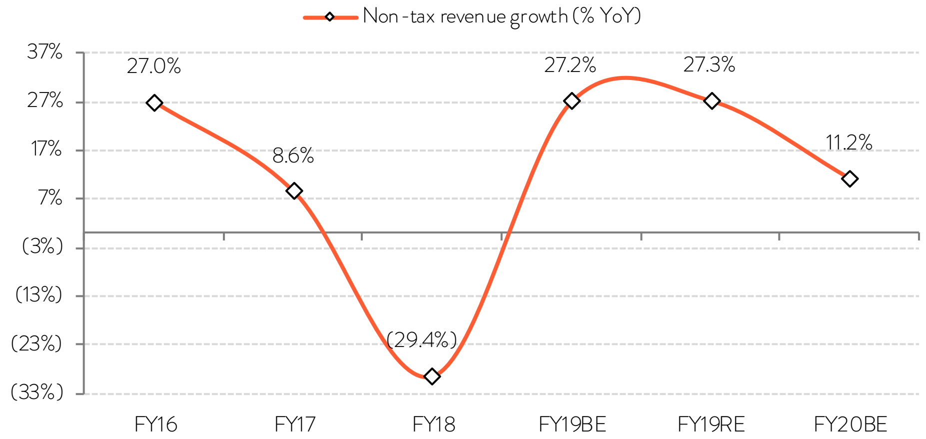
FIG 6 – INDIRECT TAX COLLECTIONS TO REMAIN LOW



Source: Budget Documents, CEIC, Bank of Baroda Research

Interestingly, non-tax revenue has also been buoyant on the back of higher dividend from RBI and other public sector institutions. This year the government has already received Rs 500bn in transfer from RBI and an interim transfer is due in Mar'18. Even next year, the government will be receiving a hefty dividend depending upon the recommendation of Bimal Jalan committee report.

FIG 7 – NON-TAX REVENUE GROWTH TO SLIP

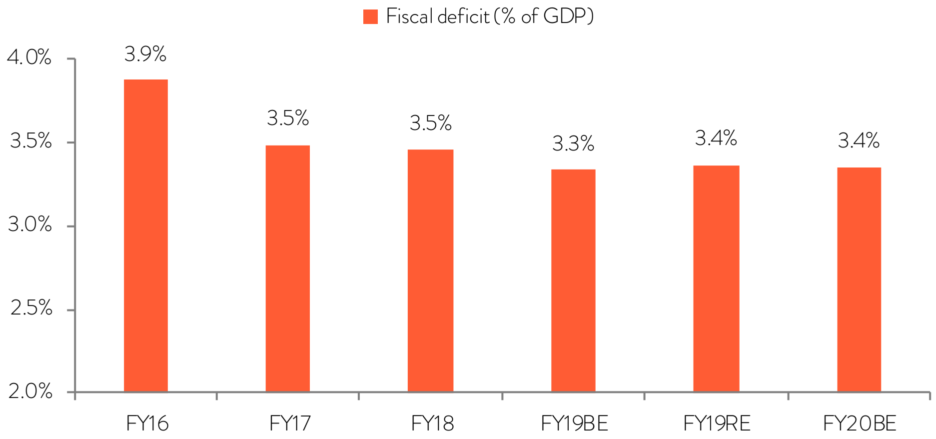


Source: Budget Documents, CEIC, Bank of Baroda Research

Fiscal deficit at 3.4% of GDP in FY20BE: Even with a 14.3% increase in centre's revenue (tax + non-tax) to Rs 19.8tn (Rs 17.3tn in FY19RE), the expenditure increase has been budgeted at 13.3% to Rs 27.8tn (Rs 24.6tn in FY19RE). In order to meet its spending commitment to farmers and ensure benefit for middle class, the fiscal deficit has been budgeted at 3.4% of GDP in FY20. Even for FY19 the fiscal deficit has been increased to 3.4% of GDP from 3.3% of GDP. The increase is directly attributable to Rs 200bn (0.1% of GDP) increase in income support scheme in FY19 and Rs 750bn (0.36% of GDP) in FY20.

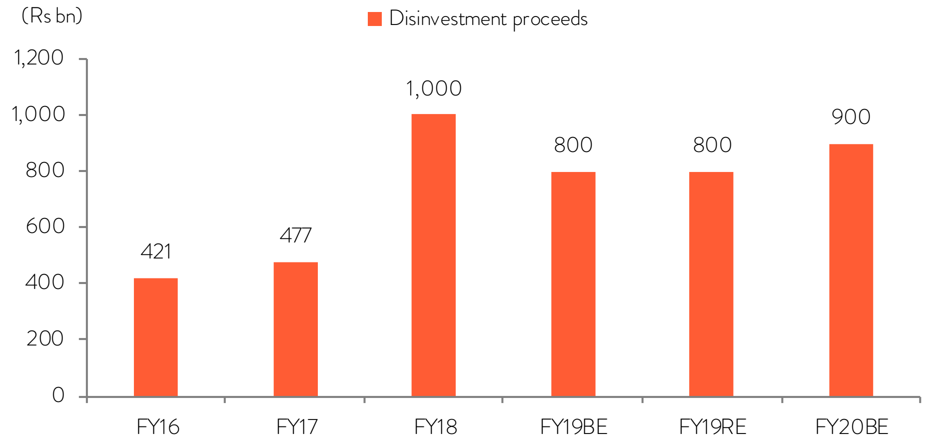
While disinvestment receipts are estimated to remain buoyant at Rs 800bn in FY19 and Rs 900bn in FY20, the gap between centre's net revenue and expenditure has increased to Rs 8.1tn in FY20BE from Rs 7.3tn in FY19RE. While a part of this gap will be funded by higher drawdown of cash balances, the majority of the gap will be met through higher net market borrowing at Rs 4.73tn in FY20 compared with Rs 4.23tn in FY19RE (an increase of 11.9%). However, with repayments of Rs 2.37tn in FY20 compared with Rs 1.48tn in FY19RE, the gross borrowing will increase to Rs 7.1tn in FY20 compared with Rs 5.71tn in FY19RE (an increase 24.3%).

FIG 8 – FISCAL DEFICIT AT 3.4% OF GDP



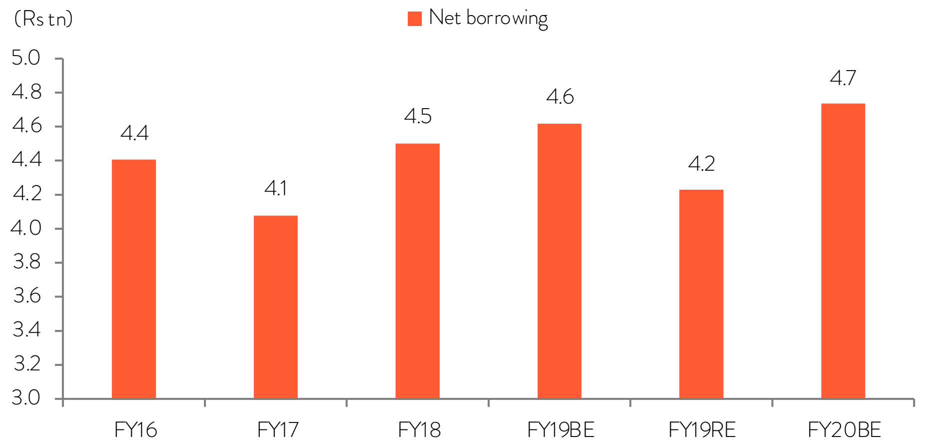
Source: Budget Documents, CEIC, Bank of Baroda Research

FIG 9 – DISINVESTMENT PROCEEDS TO RISE



Source: Budget Documents, CEIC, Bank of Baroda Research

FIG 10 – NET BORROWING JUMPS IN FY20



Source: Budget Documents, Bank of Baroda Research

Key Highlights of Budget 2019-20

Farm Sector:

- With the objective of boosting farm income, government has announced the Pradhan Mantri Kisan Samman Nidhi (PM-KISAN) wherein Rs 6,000 per year will be provided to small farmers with landholding of less than 2hectares. This income will be provide in three equal instalments of Rs 2,000 each. The scheme will be implemented retrospectively from 1st of Dec 2018 and will enable farmers much needed ease in purchasing equipment and other materials.

- The government has introduced an Income Support Scheme (ISS) for farmers under Pradhan Mantri Kisan Samman Nidhi (PM-KISAN) with an outlay of Rs 750bn (0.36% of GDP). The scheme will be implemented retrospectively from 1 December 2018 with an outlay of Rs 200bn for FY19. It is likely to benefit over 120mn farmers.

- With fisheries sector growing at a steady pace of 7% per year and providing livelihood to around 1.45cr people, the government has proposed to establish a separate Department of Fisheries.

- A benefit of 2% interest subvention to farmers engaged in activities of animal husbandry and fisheries sector will be provided. Also an additional 3% will be provided if loans are paid back in requisite time.

- Government has proposed to provide 3% prompt repayment incentive in case of natural calamity over and above 2% interest subvention benefit.

Unorganised sector

- As part of its focus to provide financial security to unorganised workers, government has launched a mega pension drive called Pradhan Mantri Shram-Yogi Maandhan Yojana. The scheme will provide assured monthly pension of Rs 3,000 to workers with monthly income of Rs 15,000. A corpus of Rs 5bn has been allocated under this scheme

MSME sector

- In order to improve the availability of credit to the sector, government had earlier announced a scheme for sanctioning loans upto Rs 10mn in 59 minutes. On incremental loans above Rs 10mn, GST registered SMEs will get a 2% rebate on interest rates.

- To further promote the MSME sector, the government has increased the sourcing requirement from SMEs by government enterprises to 25%, with at least 3% of the material sourced from women owned SMEs.
- The GeM platform has been extended to all CPSEs.

Infrastructure Spending

- Capex for railway has been increased to Rs 1.6tn in FY20BE from Rs 1.4tn in FY20RE. Capital support from the budget for railways is proposed at Rs 646bn in FY20BE compared with Rs 531bn in FY19RE.
- Ministry of roads transport and highway has received an allocation of Rs 830bn for FY20 (BE), of which, 55% is for road works (Rs 459bn) and 44% is for NHAI (Rs 367bn). Within roads, allocation to Pradhan Mantri Gram Sadak Yojna (PMGSY) has jumped by 23% from Rs 155bn in FY19RE to Rs 190bn in FY20BE.
- The government has also increased the allocation for the North Eastern areas to Rs 582bn in FY20BE. Apart from strengthening the roads, railways and air infrastructure, the government also plans to set up a container cargo facility in the region to boost trade.

Taxation

- Individual taxpayers with taxable annual income up to Rs 0.5mn will get full tax rebate and thus will not be required to pay any income tax. Apart from this, to benefit the middle-income tax payers, the government has also increased the standard deduction limit from Rs 40,000 to Rs 50,000 per year.
- Income tax on notional rent on a second self-occupied house has been exempted. Further, the period of exemption from levy of tax on notional rent on unsold properties has been increased from one year to two years.
- With respect to TDS on interest income, the limit has been raised from Rs 10,000 to Rs 40,000. TDS limit for income tax on rent has also been raised to Rs 2,40,000 from Rs 1,80,000 presently.
- The real estate sector received a big boost from the Budget. For capital gains upto Rs 20mn, the benefit of rollover under Section 54 of the IT Act has been increased to two residential houses from one.

Fiscal Highlights of Budget 2019-20

- Revenue expenditure of the government to increase by 14.4% in FY20BE versus 13.9% in FY19RE. Capital spending to increase by 6.2% in FY20BE compared with 20.3% in FY19RE.
- Direct tax collections are estimated to rise by 15.0% versus 19.8% in FY19RE. Indirect tax collections expected to increase by 11.8% versus 14.3% in FY19RE.
- Non-tax revenues estimated to rise by 11.2% to Rs 2.7tn compared with Rs 2.45tn in FY19RE.
- Capital receipts to grow by 10.9% in FY20BE versus 2.9% in FY19RE.
- Gross borrowings expected to increase by 24.3% to Rs 7.1tn in FY20 compared with Rs 5.71tn in FY19RE.
- Net market borrowing to rise to Rs 4.73tn in FY20 compared with Rs 4.23tn in FY19RE (an increase of 11.9%).
- Fiscal deficit at Rs 7,040bn in FY20 (3.4% of GDP) versus Rs 6,344bn in FY19 (3.4% of GDP).
- Glide path towards target of 3% fiscal deficit to be achieved by 2020-21. Debt to GDP ratio to be reduced from 46.5% in year 2017-18 to 40% by 2024-25.

FIG 11 – FISCAL ESTIMATES

					Increase (%)	
(Rs bn)	**FY17**	**FY18**	**FY19RE**	**FY20BE**	**FY9RE**	**FY20BE**
Tax Revenue						
Corporation Tax	4,849	5,712	6,710	7,600	17.5	13.3
Taxes on Income	3,646	4,308	5,290	6,200	22.8	17.2
Indirect Taxes	8,620	9,123	10,428	11,662	14.3	11.8
Total - Tax Revenue	17,158	19,189	22,482	25,521	17.2	13.5
Less: State's Share	6,080	6,730	7,615	8,446	13.1	10.9
Centre's Tax Revenue	11,014	12,425	14,844	17,050	19.5	14.9
Total Non-Tax Revenue	2,728	1,927	2,453	2,726	27.3	11.2
Centre's Revenue (net)	13,742	14,352	17,297	19,777	20.5	14.3
Capital Receipts						
Internal Debt Market Borrowing	4,082	4,507	4,227	4,731	(6.2)	11.9
Disinvestment	477	1,000	800	900	(20.0)	12.5
Others	1,450	1,560	2,248	2,434	44.1	8.3
Total Capital Receipts	**6,010**	**7,067**	**7,276**	**8,065**	**2.9**	**10.9**
Draw-down of Cash Balances	**(89)**	**41**	**412**	**513**	**-**	**-**
Total Receipts	**19,752**	**21,420**	**24,572**	**27,842**	**14.7**	**14.0**
Expenditure						
Interest Payments	4,807	5,290	5,876	6,651	11.1	13.2
Defence Expenditure	2,518	2,766	2,854	3,053	3.2	7.0
Subsidies	2,040	1,912	2,662	2,967	39.2	11.4
Transfer to States	1,327	1,075	1,414	1,669	31.5	18.1
Rural Development	1,139	1,350	1,351	1,390	0.1	2.9
Transport	1,022	1,104	1,454	1,562	31.7	7.4
Home Affairs	784	875	990	1,039	13.1	4.9
Education	720	802	836	938	4.3	12.2
Agriculture	502	526	866	1,500	64.6	73.2
Others	4,893	5,720	6,269	7,074	9.6	12.8
Total Expenditure	**19,752**	**21,420**	**24,572**	**27,842**	**14.7**	**13.3**
Revenue	16,906	18,788	21,406	24,479	13.9	14.4
Capital	2,846	2,631	3,166	3,363	20.3	6.2
Revenue Deficit	3,164	4,436	4,109	4,702	(7.4)	14.4
Fiscal Deficit	**5,356**	**5,911**	**6,344**	**7,040**	**7.3**	**11.0**
% of GDP	3.5	3.5	3.4	3.4	-	-

Source: Union Budget Documents, CEIC, Bank of Baroda Research; BE- Budget Estimates; RE- Revised Estimate

Disclaimer

The views expressed in this research note are personal views of the author(s) and do not necessarily reflect the views of Bank of Baroda. Nothing contained in this publication shall constitute or be deemed to constitute an offer to sell/ purchase or as an invitation or solicitation to do so for any securities of any entity. Bank of Baroda and/ or its Affiliates and its subsidiaries make no representation as to the accuracy; completeness or reliability of any information contained herein or otherwise provided and hereby disclaim any liability with regard to the same. Bank of Baroda Group or its officers, employees, personnel, directors may be associated in a commercial or personal capacity or may have a commercial interest including as proprietary traders in or with the securities and/ or companies or issues or matters as contained in this publication and such commercial capacity or interest whether or not differing with or conflicting with this publication, shall not make or render Bank of Baroda Group liable in any manner whatsoever & Bank of Baroda Group or any of its officers, employees, personnel, directors shall not be liable for any loss, damage, liability whatsoever for any direct or indirect loss arising from the use or access of any information that may be displayed in this publication from time to time.

Visit us at **www.bankofbaroda.com**

For further details about this publication, please contact:

Economics Research Department

Bank of Baroda

+91 22 6698 5713

chief.economist@bankofbaroda.com