India's Populist Budget – A Gift for the Masses

India's Union Budget was released on Friday, February 1st by Finance Minister, Piyush Goyal. This was supposed to be an interim Budget, given the upcoming National Elections in April-May 2019. An interim Budget generally means significant initiatives are not announced given the potential for change of Government. However, that was not the case in this Budget, with major incentives and tax cuts announced by the Modi Government to win over voters at the polls. It's important to remember that's 2/3 of India's population lives rurally and is largely classified as low to middle class.

We list the key changes announced below:

- Income support of Rs. 6,000 per annum to farmers owning <2 hectares of land (87% of farmer community base). This assistance will commence immediately, with A$3.8bn allocated. 120 million of India's 250 million households will benefit from this[1].
- A full tax rebate has been given for individual taxpayers with a taxable income of less than A$9,615. Additional investment in pension funds and insurance have also been upped. This provides an overall boost of A$3.6bn to the economy. This will have an impact on 30 million middle class in India[2].

The Budget is populist given farmers are significant in numbers at the polls. Additionally, it's also populist given its positive impact on the poor and middle class in terms of tax cuts. This should support greater consumption and increasing potential for GDP growth in FY20 than that currently forecast by the IMF (7.5%).

The impact of these initiatives is to put a small dent in the fiscal prudence of the Government. A Budget Deficit which was targeted to be 3.3% for FY20 is now shifted to 3.4%. This Government was supposed to achieve a deficit of 3.0% by the end of their term. However, tax collections are increasing as a result of the GST and post-election the deficit may be reduced towards the target of 3% in FY21/22. Moody's who recently upgraded India, views fiscal slippage as credit negative and will continue to monitor this situation given there were no new policies announced to increase tax revenue.

Rising bond yields on the back of this announcement, with more 10-year bonds to be issued to fund the deficit, led to a yield of 7.38% on Friday (up 9bp). However, this may be neutralized by low inflation which may call for a rate cut this week at the RBI Monetary Policy Committee meeting and a weaker global growth environment.

In order to fund this, the Government had to squeeze some spending for Highways and Defence and change the glidepath for the fiscal deficit forecast. Another issue is the disinvestment program of the Government, which so far has been underwhelming, with barely half of the FY19 A$15.4bn target being achieved. The target for FY20 is A$17bn and needs to be achieved to helps ends meet fiscally.

[1] Elara Capital Research

[2] The Finance Minister also hinted that the next slab of income earners would be considered next for tax cuts

	Budget at a Glance (INR bn)				Growth (% YoY)				
	FY18 (A)	FY19 (BE)	FY19(RE)	FY20(BE)	FY17(RE)	FY18(A)	FY19(BE)	FY19(RE)	FY20 (BE)
Total Receipts (ex-borrowings)	**15,510**	**18,179**	**18,228**	**20,802**	**14.4**	**7.7**	**17.2**	**17.5**	**14.1**
Revenue Receipts	14,352	17,257	17,297	19,776	15.0	4.4	20.2	20.5	14.3
Net Tax Revenue	12424	14,806	14,844	17,050	16.7	12.8	19.2	19.5	14.9
GST (Gross)	4425	7,439	6,439	7,612			68.1	45.5	18.2
Non-Tax Revenue	1927	2,451	2,452	2,726	8.6	(29.4)	27.2	27.2	11.2
Non-Debt Capital Receipts	1156	922	932	1,025	3.8	76.8	(20.2)	(19.4)	10.0
o/w Disinvestments	1,000	800	800	900	13.3	109.5	(20.0)	(20.0)	12.5
Total Expenditure	**21,419**	**24,422**	**24,572**	**27,842**	**10.3**	**8.4**	**14.0**	**14.7**	**13.3**
Total Revenue expenditure	**18,788**	**21,418**	**21,406**	**24,479**	**9.9**	**11.1**	**14.0**	**13.9**	**14.4**
o/w interest payments	5289	5,758	5,875	6,650	8.8	10.0	8.9	11.1	13.2
o/w pensions	1457	1,685	1,666	1,743	35.8	10.9	15.6	14.4	4.6
o/w subsidies	2,244	2,955	2,992	3,342	(11.1)	(4.4)	31.7	33.3	11.7
Food	1002.81	1,693	1,712	1,842	(21.0)	(9.0)	68.8	70.7	7.6
Fertilizer	664	701	700	749	(8.4)	0.1	5.5	5.4	7.0
Petroleum	244.6	249	248	374	(8.2)	(11.2)	1.9	1.4	50.8
Total Capital expenditure	**2,631**	**3,004**	**3,166**	**3,363**	**12.5**	**(7.6)**	**14.2**	**20.3**	**6.2**
Fiscal Deficit	**5,910**	**6,243**	**6,344**	**7,040**					
Fiscal Deficit: GDP ratio	3.5	3.3	3.4	3.4					
Subsidies (% of GDP)	*1.3*	1.6	1.6	1.6					
Revenue deficit/GDP	*2.6*	*2.2*	*2.2*	*2.2*					
Primary deficit/GDP	*0.4*	*0.3*	*0.2*	*0.2*					

Source: Ministry of Finance, Elara Securities Research

The Finance Minister also highlighted the following achievements by the Government in its term:

- Stage of recovering funds which were lent out under poor lending practices of the past. Bank mergers to provide economies of scale
- Increasing transparency in business, attracting US$240bn over the last five years
- 98% rural sanitation coverage which is critical to improve lives, increase productivity
- Construction of rural roads have tripled (A$3.6bn to be spent on rural roads in FY20)
- Launched healthcare program for 500m people (India has a low allocation to health)
- Low cost housing building program underway
- 60m homes now have a gas connection, improving livelihoods of women and reducing cost
- India is the second largest start up hub in the world. Critical because 420m workers are from the unorganized sector, which is a massive employer of youth (50% of India's GDP)
- 340m bank accounts opened since 2015, individual identity cards (Aadhaar), increasing smart phone penetration creates digital transparency
- 100 digital villages will be targeted over the next 5 years
- Railway capex increasing, with safety being monitored closely in rural locations
- India is becoming a hub for automobile construction, smartphone and component assembly, renewable energy, medical drug manufacturing and information technology. This will beneficial for private investment and exports.

Our View

The Interim Budget is seen as a populist measure to address the upcoming National Election. In recent State Elections (December 2018), the BJP Government lost three states based on anti-incumbency and growing farmer dissent. Whilst State Election results are not necessarily a proxy for the National Election, the Modi-led BJP Government understood the need of the hour in this budget. Reducing oil prices is a gift for the Government as it takes the pressure off the current account and allows the Rupee to recover. Additionally, benign inflation allows scope for rate cuts in the next RBI policy meetings. We are of the view that GDP growth could surprise on the upside given handouts and easing of policy. We expect that foreign investors are keeping a keen eye on markets for an entry point in the lead up to or post-election.