February 3, 2020

India's Union Budget 2020–2021 Highlights

- **The Budget 2020–21 focuses on rural demand and infrastructure investment, yet fiscal measures seem inadequate to address the economy's weakness.**
- **The administration aims to return to fiscal consolidation in Fiscal Year 2020–21 (FY21) following fiscal slippage in the current fiscal year. The central government deficit is expected to narrow to 3.5% of GDP in FY21 from 3.8% in the current fiscal year.**

India's Union Budget for Fiscal Year 2020–21 (April–March) was presented by Finance Minister Nirmala Sitharaman on February 1. Despite the economy's ongoing struggles with weak domestic demand, the Budget's stimulative impact will be limited, leaving most of growth-revival efforts to the Reserve Bank of India.

The estimate for the central government's fiscal deficit in the current fiscal year was revised to 3.8% of GDP vs. the targeted 3.3% as economic softness has lead to muted tax revenue. Following the fiscal slippage this year, the government aims to resume fiscal consolidation efforts and narrow the shortfall to 3.5% of GDP in the FY21 (chart1). This highlights the administration's challenge in balancing between stimulating the economy and promoting investor confidence on India's fiscal sustainability; we assess that the administration prioritized the latter with the Budget's overall impact on economic growth being fairly neutral.

According to Finance Minister Sitharaman, public outlays in FY21 will be directed at:

- infrastructure projects with focus on transport infrastructure, such as roads, railways and airports;
- reviving rural demand with programs that lift farmers' incomes, support rural development, and boost the agricultural sector's productivity;
- sector-specific programs in such areas as electronics manufacturing, textiles, power and renewables, and affordable housing;
- inclusive growth-related programs, encompassing employment generation, skill development, as well as health and sanitation.

Other key proposals include:

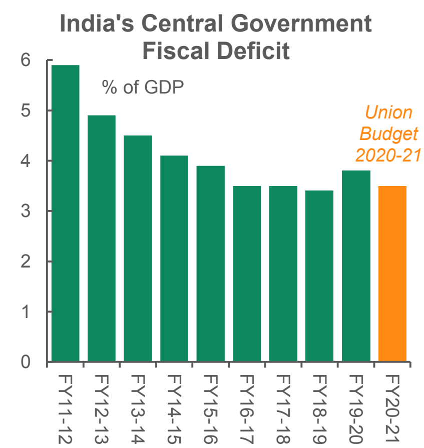
- Lower income tax rates; the new structure is optional and available to those taxpayers that are willing to forgo certain exemptions and deductions.
- The dividend distribution tax for companies will be abolished.
- The disinvestment target for FY21 is set at a record-high, and includes selling of stakes in public sector financial institutions and enterprises.
- Certain government securities will be opened for foreign investors while the limit on foreign portfolio investment in corporate bonds will be raised.

The government expects India's real GDP growth to rebound to 6–6.5% y/y in FY21 from around 5% in the current fiscal year; the growth forecast is in line with our expectation. Nevertheless, we are somewhat sceptical about the administration's ability to execute the ambitious divestment program swiftly. Moreover, we note that the expectation for a notable pickup in tax revenue may be too optimistic given the weak economy. Accordingly, we assess that the government's deficit target for FY21 will be at risk.

CONTACTS

Tuuli McCully, Head of Asia-Pacific Economics
65.6305.8313 (Singapore)
Scotiabank Economics
tuuli.mccully@scotiabank.com

Chart 1



Sources: Scotiabank Economics, IMF, India Ministry of Finance.