Budget math appears relatively credible

Assumptions on revenue and expenditure targets as well as nominal GDP growth seem reasonable

ADITI NAYAR

The Budget for FY27 has stuck to its fiscal deficit target of 4.4 per cent of GDP for FY26 and has pegged the same at a marginally lower 4.3 per cent for FY27, in line with our expectations. Importantly, it has pencilled in mostly reasonable assumptions across revenue and expenditure targets, thereby lending credibility to the overall Budget math.

The tax revenue assumptions for FY26 were somewhat optimistic to begin with, particularly on the personal income tax front after the sizeable tax relief in the FY26 Budget, the GST rate cuts and termination of the compensation cess in September 2025 impacted such collections. Consequently, the revised estimate (RE) for gross tax revenue (GTR) has been pared by a considerable ₹1.9 trillion relative to the budget estimate (BE).

While a part of this shortfall has been offset by additional non-tax revenues, the government has pencilled in expenditure cuts to the tune of ₹1 trillion to avoid a fiscal slippage. This includes an unwelcome curtailment of capex modestly below the budgeted figure. Importantly, the headroom left after the actual spending in the first nine months implies an unpalatable 16 per cent year-on-year (YoY) contraction in the the government's capex in Q4 FY26, which would weigh on GDP growth in the quarter.

GROWTH IN TAX REVENUE

For FY27, the government has assumed a nominal GDP growth of 10 per cent, only marginally higher than our forecast of around 9.8 per cent. While GTR is budgeted to rise by a moderate 8 per cent, lower than the rise in nominal GDP, this is largely on account of the termination of GST compensation cess collections.

OPTIMISTIC. The growth assumptions for excise and STT collections ISTOCKPHOTO

Excluding this, GTR is expected to grow by 10.4 per cent in FY27, particularly aided by a healthy growth in direct taxes. Among other taxes, the growth assumptions for excise and security transaction tax (STT) collections seem somewhat optimistic, even though the latter may be supported by duty hikes on options and futures trades.

With the 16th Finance Commission retaining the vertical share of devolution at 41 per cent of Centre's divisible pool of taxes for the award period (FY27-31), there is no material impact of the government's net tax revenues, that are budgeted to grow by 7.2 per cent in FY27 amidst some prior period adjustments in FY26.

Additionally, the government has pencilled in flattish non-tax revenues, on a high base, which seems reasonable. However, it has pegged the miscellaneous capital receipts at ₹0.8 trillion, which appears on the higher side given the repeated undershooting seen every year on this account, unless there are sizeable inflows related to asset monetisation.

With the fiscal deficit pegged at 4.3 per cent of GDP, the reasonable revenue assumptions have limited the expansion in total expenditure to 7.7 per cent in FY27, dampened by a growth of just 6.6 per cent in revenue spending. However, in line with the trends observed in the recent past, the government has prioritised expanding its capex at a much faster 11.5 per cent, leading to a continued improvement in the spending mix. In fact, after accounting for grants for creation of capital assets, which are typically included under revenue expenditure, the government's effective capex is up by a robust 22.1 per cent in FY27. This is a favourable move, given that committed expenditure is likely to surge in FY28, with the implementation of the 8th Central Pay Commission, which would limit the space for boosting capex in that fiscal.

The government has stuck to reducing the debt-to-GDP ratio in FY27 to 55.6 per cent from 56.1 per cent in FY26, in pursuit of its goal to align it to 50 +/-1 per cent by FY31. We had anticipated a slightly faster reduction in this metric in the current year. However, the upcoming release of GDP on the new series may well result in a larger absolute GDP, which could result in the government's debt to GDP looking smaller than 55.6 per cent, and bringing it closer to the goal post of 50 +/-1 per cent by FY31. Having said that, compressing the debt-to-GDP ratio further in FY28 amidst the pay revision may prove to be a daunting task.

The writer is Chief Economist, Head – Research & Outreach, ICRA