India Pre Budget FY23: Focusing on capex revival

We expect Government to meet its fiscal deficit target of 6.8% in FY22 despite an increase in nominal fiscal deficit to INR 15.7tn (INR 15.1tn in FY22BE) on the back of higher nominal GDP. Tax buoyancy has been the highlight for FY22 with tax to GDP ratio increasing to 11.3% of GDP compared with 5-year average of 10.7%. For FY23, we expect fiscal deficit to moderate to 6.3% of GDP (INR 16.2tn). Overall spending is estimated to increase by 3.6%. However, we expect capital spending led by roads and railways to inch up by 20% in FY23. At the same time, food subsidy will be lower while fertilizer and MGNREGA spending will be at current levels to support rural incomes. Strategic sales to finance the deficit will remain a thrust area as also digitization of the economy to give a boost to start-ups. Inclusion in bond index will also be a positive to finance gross and net issuances of INR 13tn and INR 9.75tn respectively.

Buoyant Tax Revenue: India's tax buoyancy is visible in sharp increase in gross tax collections, which are estimated to increase to 11.3% of GDP in FY22 as against 5-year average (FY17-21) of 10.5% of GDP. Within this, direct tax collections are estimated to increase to 6.1% of GDP in FY22 (5.4% during FY17-21). We expect direct tax collections to increase by 10% YoY in FY23. In FY22, indirect tax collections are estimated to increase to INR 12.2tn (5.1% of GDP) led by customs, up by 38% YoY and GST collections by 32% YoY. In FY23, we expect indirect tax collections to increase by more moderate 2.4% on the back of dip in excise duty collections. Even customs and GST collections are likely to show a deceleration in pace of growth.

Non-tax revenues: We expect non-tax revenues to be higher than FY22BE on the back of INR 991bn transfer by RBI to Government. Communication receipts will get a boost from pre-payment of arrears by a few telecom operators. In FY23, we expect buoyancy in non-tax revenues on the back of 5G auctions, RBI dividend and higher profitability of Public Sector Banks and other CPSEs. At the same time, disinvestment revenues are likely to miss the FY22BE as BPCL strategic sale will be rolled over to FY23. There are a number of transactions that can be completed in FY23. Thus, we see disinvestment revenues at INR 1tn in FY23.

Spending boost in FY22, capex boost in FY23: Spending in FY22 will be higher than FY22BE by 11%. Large increase in allocation is seen in food subsidy to INR 3.7tn (INR 2.4tn in FY22BE), fertilizer subsidy at INR 1.4tn (INR 0.8tn in FY22BE) and MGNREGA at INR 950bn (INR 0.7tn in FY22BE). According to supplementary demand for grants, higher cash outgo is also allocated for writing off Air India debt and export arrears. On the other hand, capital spending during April-November is up by 13% as against FY22BE estimate of 26% YoY. We expect capex to increase by 24% YoY over FY21PA. We expect capex spending to get a boost in FY23 as well with an increase of 20% YoY led by higher allocation for roads, railways and housing. However, food subsidy is likely to be lower than FY22. Fertiliser subsidy will remain elevated to cushion the impact of higher international prices. MGNREGA spending too will remain at current levels to provide for rural jobs.

Fiscal deficit: Given the revenue and spending outlook for FY22, we see fiscal deficit at INR 15.7tn (6.8% of GDP) as against INR 15.1tn in FY22BE. The boost to nominal GDP will help fiscal deficit remain at 6.8% of GDP as envisaged in FY22BE. This raises risk of additional borrowing in FY22. During FY23, we see fiscal deficit to expand to INR 16.2tn. This implies a fiscal deficit of 6.3% of GDP in FY23. This will entail gross and net borrowing of INR 13tn and INR 9.75tn respectively compared with INR 12.1tn and INR 9.2tn in FY22BE. The gap between fiscal deficit and market borrowings will be filled up by small saving borrowings. Even during April-November 2021, Centre has borrowed INR 2.8tn through small savings as against only INR 0.8tn in the same period last year. Going ahead, we continue to see this as important element in financing elevated fiscal deficit. India's inclusion in global bond indices will also be an important segment for financing India's bond issuances.

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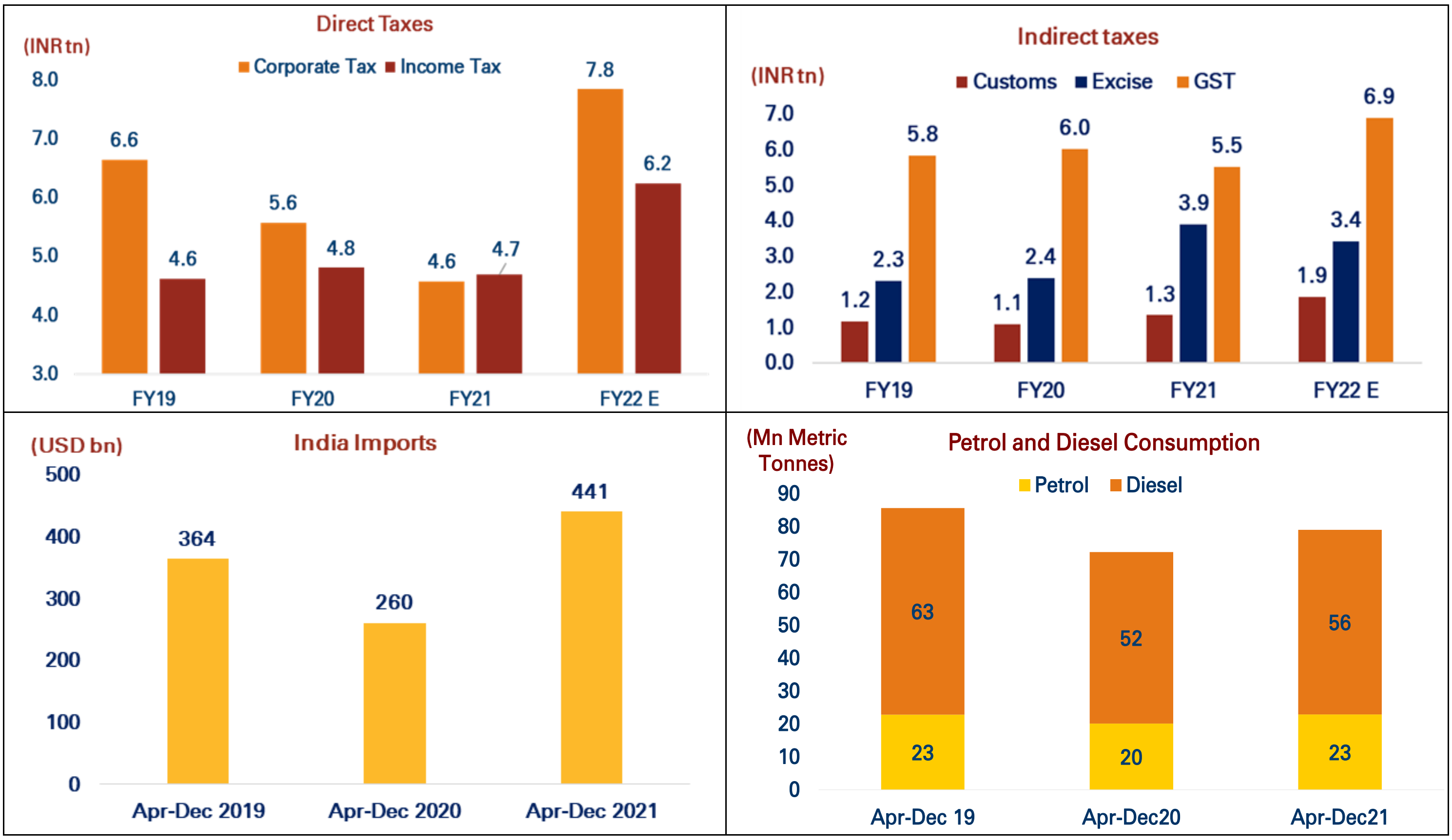
Detailed analysis of fiscal performance in FY22 and our expectations on FY23

Revenue and Total receipts: FY22 performance

Tax revenue: Gross tax revenues in Apr-Nov2021 stood at INR 15.4tn (69.5% of the Budget Estimate) for FY22. This implies an increase of 50% over the same period last year. Notably, gross tax collections have increased by 15% over a 2-year CAGR. The increase is led by direct tax collections, which have increased by 66% YoY to INR 7tn. Over a 2-year CAGR, direct tax collections are up by 12%. Within this, corporate tax collections have increased by 11% (2-year CAGR, 90% YoY) and income tax collections are higher by 14% (2-year CAGR, 47% YoY). This goes to show the buoyancy in direct tax collections.

During the same period, indirect taxes have also been buoyant at 39% YoY (2-year CAGR of 16%) led by 99% YoY (2-year CAGR at 29%) increase in customs duties. It is a direct result of rising imports, which are up by 69.3% YoY to USD 443.7bn during April-December 2021. Even excise duty collections have been buoyant which is a result of higher excise duties (before the excise duty reduction in November) as well as higher volume throughout. While GST collections have been buoyant at 26% YoY, over a 2-year CAGR basis, GST collections are up by only 7%.



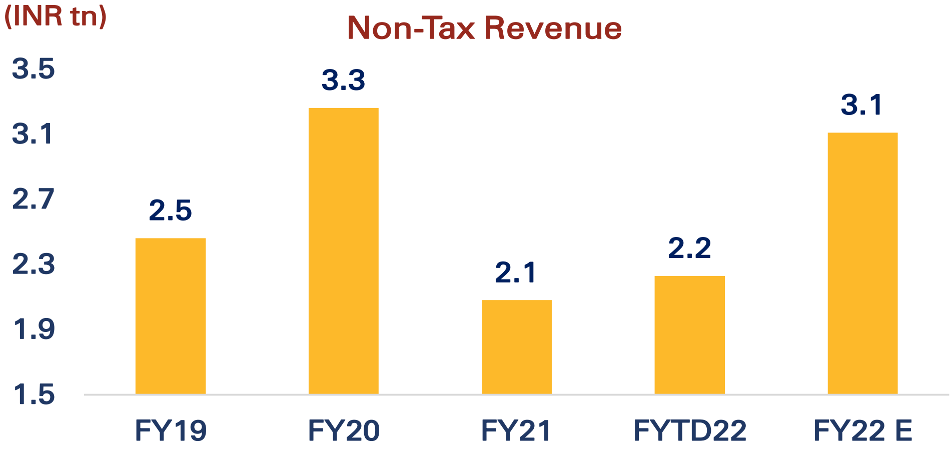
Source: CGA, DGCA, PPAC, ICICI Bank Research

What does it mean for tax revenues in FY22 and FY23?

Given the current run-rate and estimates of advance tax collections (INR 4.6tn as of Dec16, 2021), we expect direct tax collections to reach INR 14.1tn (6.1% of GDP). Indirect tax collections are estimated to increase to INR 12.2tn (5.2% of GDP). After the increase seen in FY22, we believe direct and indirect taxes are estimated to increase by 10% YoY and 2.4% YoY to INR 15.5tn and INR 12.5tn, respectively, in FY23. On the direct tax front, corporate taxes are estimated to increase by 10% YoY. This is on the back of an elevated base and underlying margin pressure on corporate sector because of higher input costs.

Income tax collections will continue a steady increase of 10% YoY, in-line with long-term CAGR, albeit lower than last year. The possibility of increase in standard deduction also implies Government may forego some revenue. On the indirect tax front, we expect both custom duties and GST collections to increase at 8% YoY. Excise duty collections are expected to be lower since excise duties have been reduced in November and this will impact revenue collections for a large part of the next financial year. Given the above backdrop, we have estimated gross tax collections to increase by 6.5% YoY in FY23 to INR 28tn.

Non-tax revenues: have increased by 79% YoY during April-November 2021. This is led by higher surplus transferred by Reserve Bank of India (RBI) at INR 991bn in May 2021. Compared with this, RBI had transferred a surplus of INR 618.3bn in FY21. During FY22, we expect dividends and profits at INR 1.7tn (Budget estimate of INR 1.0tn). At the same time, telecom receipts are expected to reach the budgeted target of INR 539bn, after accounting for annual license fee and spectrum usage charges and pre-payment of some deferred spectrum liabilities by telecom operators. We expect dividends and profits in FY23 to be in-line with current year on the back of 5G auctions and improved profitability of Public Sector Enterprises, in particular Public Sector Banks.



FYTD=Apr-Nov FY22; E=Estimate
Source: Union Budget Documents, CGA, ICICI Bank Research

Disinvestment: So far in the year, the disinvestment receipts of the government stand at INR 93.2bn (only 5.3% of the BE). Air India at an enterprise value of INR 180bn (INR 27bn is the cash paid to the government). Other significant disinvestment receipt is estimated from LIC. Together, these stake sales expected to contribute INR 1105bn, taking overall disinvestment proceeds to INR 1198bn (68% of the targeted 1.75tn).

Key stake sales so far in FY22	Receipts (INR bn)
NMDC	36.5
HUDCO	7.2
HCL	7.4
IPCL(now RIL)	2.2
Others (SUTTI Axis Bank)	40.0
Total	93.3

Source: DIPAM

We have assumed that the BPCL stake sale will be rolled over to FY23. There is a long list of undertakings that may be available for stake sale next year. Thus, we have assumed disinvestment receipts at INR 1tn in FY23.

CPSEs likely to undergo stake sale	Govt shareholding
Bharat Petroleum Corp. Ltd.	53
Container Corp. Of India Ltd.	55
Pawan Hans Ltd	51
Neelachal ISPAT	65
Alliance Air	100
Indian Overseas Bank	96
Central Bank of India	93
Industrial Development Bank of India	45
General Insurance Corporation of India	86

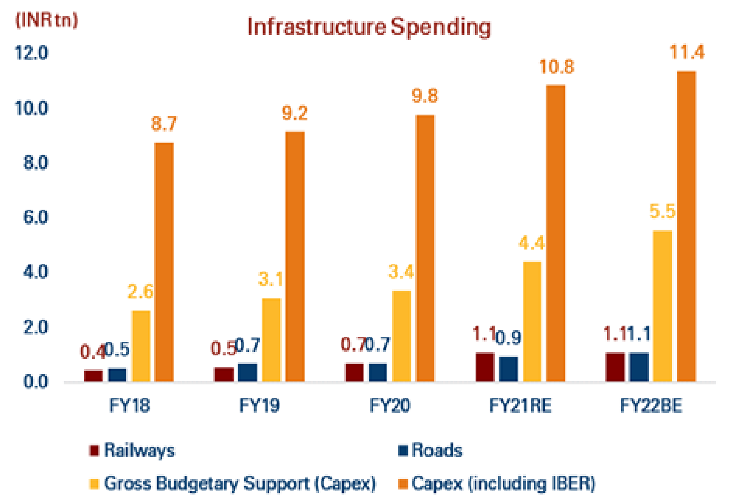
Source: ICICI Bank Research

Expenditure: During April-November 2021, expenditure of Centre has increased by 9% YoY to INR 20.7tn. Within this, revenue expenditure has increased by 8.2% YoY to INR 18tn.

Capital expenditure has increased by 13.5% YoY to INR 2.7tn. Compared with this, Centre has budgeted a 26% YoY increase in capital spending. In the last financial year, Centre spent INR 1.9tn in the last four months. Even if there is a higher amount of spending this year, Centre is likely to miss its capital-spending target of INR 5.5tn.

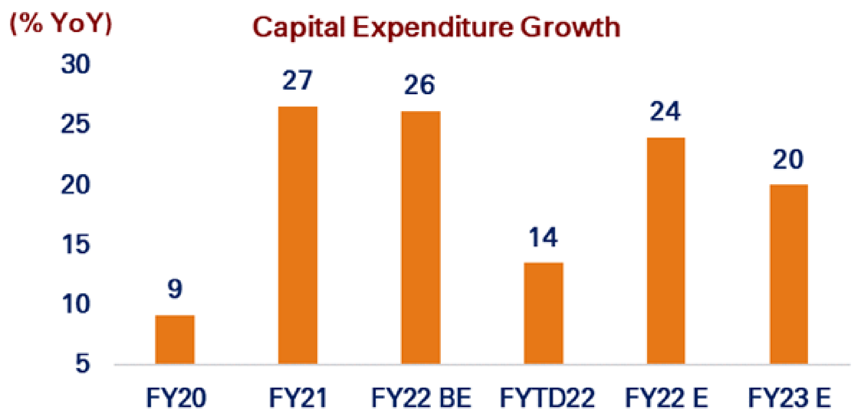
Budget allocation (towards capex) FY22

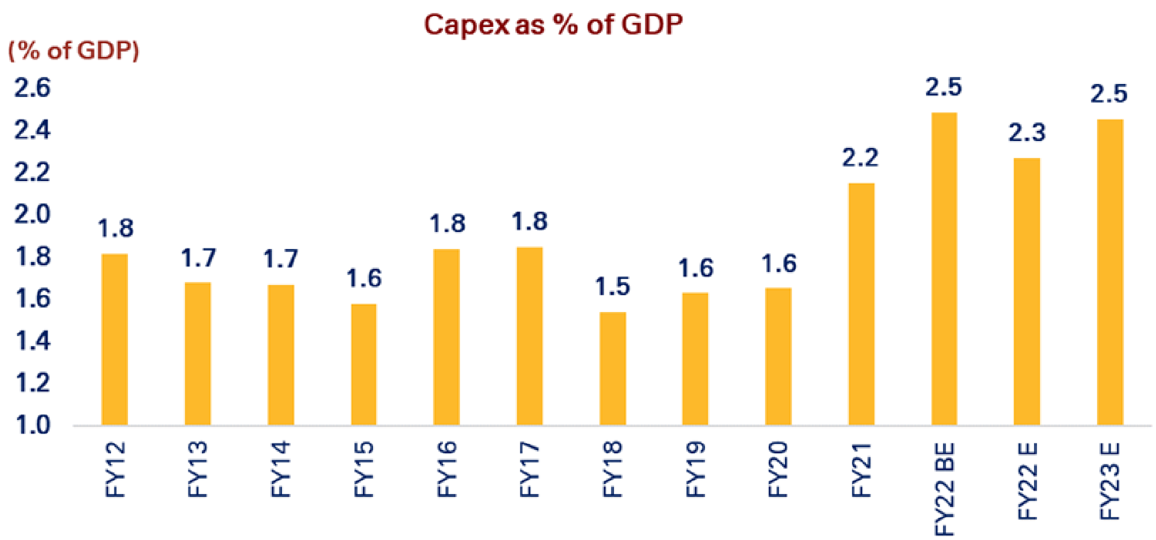
Ministry	Budgeted amount FY22 (INR bn)	Share of total allocation (%)
Ministry of Road Transport and Highways	1082	20
Ministry of Housing and Urban Affairs	258	5
Ministry of Communications	268	5
Ministry of Defence	1402	25
Ministry of Railways	1071	19
Others	1461	26
All ministries	5542	



RE: Revised Estimate , BE : Budget Estimate
Source: Union Budget Documents, ICICI Bank Research

We expect roads, housing, defence and railways to remain thrust areas in FY23 as well. In fact, we have seen an 11% (CAGR) increase in government spending on capex between FY16 and FY21. Government had budgeted capex at 2.5% of GDP in FY22. We expect capex to increase by 20% in FY23.





FYTD=Apr-Nov FY22 ; E=Estimate
Source: Union Budget Documents, CGA, ICICI Bank Research

Revenue spending is estimated to be much higher than what was estimated at the beginning of the year. Government has laid out additional cash spending of INR 3.2tn in FY22.

Among the areas of higher expenditure, food subsidy component is estimated at INR 3.7tn which is INR 1.3tn more than budgeted amount of INR 2.4tn. Fertiliser subsidy also is likely to be higher than budgeted amount by INR 584bn. This implies overall subsidy outlay at INR 5.2tn (INR 1.9tn higher than BE). Other areas of increase in expenditure are MGNREGA at INR 220bn, export subsidies at INR 531bn and write-off of Air India debt at INR 621bn. Given the higher revenue spending and slight dip in capital expenditure from Budget Estimates, we expect overall expenditure to increase to INR 38.7tn, 10% higher than actual expenditure (provisional accounts) of INR 35.1tn in FY21.

Additional Revenue Expenditure	
Cash outgo on first supplementary grant	237
Cash outgo on second supplementary grant (major components below)	2990
Fertiliser Subsidy	584
Food subsidy	498
Export subsidy arrears	531
Air India Debt	621
MGNREGA	220
Others	536

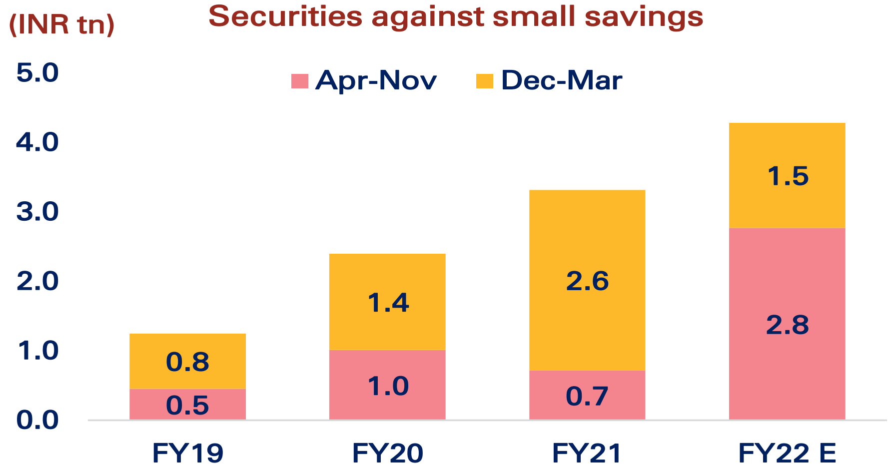
Source: Supplementary Demand for Grants (1 and 2)

Fiscal deficit:

The revenue and expenditure estimates for this year imply fiscal deficit for FY22 will be at INR 15.7tn compared with Budgeted amount of INR 15.1tn. However, nominal GDP is also estimated to be much higher at INR 232tn compared with Budget estimate of INR 223tn. Hence, our fiscal deficit estimate is in-line with Budget estimate at 6.8% of GDP. For FY23, we have estimated Centre's revenue (tax and non-tax revenue) at INR 22.4tn. Disinvestment is estimated at another INR 1 tn. Expenditure is estimated at INR 39.8tn.This leaves a fiscal gap of INR 16.25tn, which is 6.3% of GDP.

Financing the fiscal deficit:

This will entail gross market loans of INR 13tn in FY23 and net market loans of INR 9.75tn. This is higher than gross and net market borrowing of INR 12.1tn and INR 9.2tn in FY22. Small savings instruments will continue to be an important source of funding government's fiscal deficit as has been the case this year when government has raised INR 2.8tn from small saving scheme upto November 2021 compared with INR 716 bn in the same period last year. In the current financial year, overall amount of borrowing from small savings is estimated at INR 4.3tn.



Source: CGA , ICICI Bank Research

Detailed fiscal estimates are given below:

INR trn	FY19	FY20	FY2021 PA	FY22 BE	FY22 ICICI Exp	FY23 ICICI Exp	%YoY (FY23)
Gross Tax Revenue	20.8	20.1	20.2	22.2	26.3	28.0	6.5
Direct Tax	11.4	10.5	9.3	11.1	14.1	15.5	10.0
Corporate Tax	6.6	5.6	4.6	5.5	7.8	8.6	10.0
Income Tax	4.7	4.9	4.7	5.6	6.2	6.9	10.0
Indirect Tax	9.4	9.5	10.5	11.0	12.2	12.5	2.4
Customs	1.2	1.1	1.3	1.4	1.9	2.0	8.0
Excise	2.3	2.4	3.9	3.4	3.4	3.1	-9.3
GST	5.8	6.0	5.2	6.3	6.9	7.4	6.7
Taxes of Union Territories	0.1	0.1	0.0	0.1	0.1	0.1	10.0
Transfer to states	7.6	6.5	5.9	6.7	7.8	8.3	6.5
NCCD transferred to the NCCF/NDRF	0.0	0.0	0.1	0.1	0.1	0.1	
Net tax revenue	13.2	13.6	14.2	15.5	18.5	19.7	6.5
Non-tax revenue	2.4	3.3	2.1	2.4	3.1	3.0	-5.0
Revenue receipts	15.5	16.8	16.3	17.9	21.6	22.7	4.8
Non-debt capital receipts	1.1	0.7	0.6	1.9	1.3	1.2	
Disinvestments	0.9	0.5	0.4	1.8	1.2	1.0	
Debt Capital Receipts	6.5	9.3	18.2	15.1	15.7	16.2	
Total receipts (excluding debt capital receipts)	16.6	17.5	16.9	19.8	22.9	23.8	3.8
Total receipts	23.2	26.9	35.1	34.8	38.7	40.0	
Revenue expenditure	20.1	23.5	30.9	29.3	33.1	33.7	1.8
Food subsidy	1.0	1.1	5.3	2.4	3.7	3.2	-13.4
Fertiliser subsidy	0.7	0.8	1.3	0.8	1.4	1.4	5.0
Capital expenditure	3.1	3.4	4.2	5.5	5.3	6.3	20.0
Total expenditure	23.2	26.9	35.1	34.8	38.7	40.0	3.6
Gross fiscal deficit (GFD)	6.5	9.3	18.2	15.1	15.7	16.2	
GFD % of GDP	3.4	4.6	9.2	6.8	6.8	6.3	

PA :Provisional Accounts

Source: Union Budget Documents, CGA, ICICI Bank Research

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