

Union Budget FY 2020-21

Decoded



View from the Fixed Income Desk

Kumaresh Ramakrishnan,
CIO – Fixed Income

Union Budget – Return to consolidation; focus on execution

No big bang stimulus

The Government stuck to the fiscal glide path for FY 2020 by resorting to the deviation clause of 50 bps in the FRBM act. Fiscal deficit for FY20 is thus estimated higher by 50 bps at 3.8%. This slippage has prompted the Government to opt in favour of consolidation for FY 21 and refrain from providing any big bang fiscal stimulus. The fiscal consolidation is expected to help pull deficit back down to 3.5% in FY 21 and should also help avert any rating action from agencies.

Growth in gross tax collections at 12% for FY 21 appears consistent with the 10% nominal growth target (versus a nominal growth of 7.5% in FY20). However, in aiming to balance the budget, the Govt is relying heavily on non-tax revenues for the year.

Heavy reliance on non-tax revenues

Asset sales are targeted to generate 1% of GDP, comprising strategic sale of assets (BPCL, Concor, Shipping Corp) and proceeds from disinvestment (including an IPO of LIC). In addition, the budget factors in receipts from telecom at INR 1.3 trillion (INR 0.59 trillion in FY 20) covering AGR dues, 5G auction proceeds and spectrum charges.

Another positive is a tax amnesty that is proposed for all ongoing direct tax litigations which could now be settled without paying any penalties or interest if paid by March 31, 2020. Given the huge backlog of close to 1 trillion in outstanding disputes, this is significant and could potentially lead to inflows of anywhere between INR 30,000-40,000 cr and could alleviate the stress.

GDP to be powered through capex and consumption

On the investment front, the budget focused on continuing the capex momentum despite a strain in revenues. Capex outlay for FY 21 rose by 10 bps to 1.8% of GDP and should help fill up the slack arising from the inability of the private sector to invest adequately.

The consumption lever was addressed by attempting to push INR 450 bio into the hands of the middle class by rejigging IT rates provided no deductions are availed. Overall the net tax revenues are estimated to rise by 9.2% while expenditures are projected to rise by 12.7%, leading to a fiscal deficit of INR 7.96 trillion (3.5% of GDP).

Implication for bond markets

Net borrowing of G-secs (including a buyback of INR 300 bio) for FY 21 is estimated at INR5.15 trillion, while the gross is higher at INR 7.86 trillion (INR 7.1 trillion in FY 20). Besides, switches of INR 2.7 lakh cr are planned for FY 21. In our view, RBI is likely to keep up Operation twist, to prevent any curve steepening.

Other positives for the fixed income market include a probable listing of separate bonds for FIIs as a first step towards inclusion in some of the bonds indices.

Lack of incremental borrowing in FY 20 and only a marginal increase projected for FY 21 is a positive for the bond markets. The Govt's decision to put prudence first should please RBI and let it stay the course on an accommodative phase and a medium term pause in the upcoming policy.

Risks that we foresee

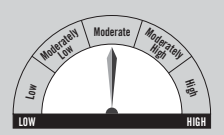
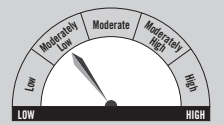
Despite opting for prudence over a big bang stimulus and realistic forecasts, downside risks exist. Delayed recovery to a 10% nominal rate is the biggest risk given the continuing local headwinds to growth. For the first time in 10 years, there was no capital allocation to banks in the budget, which together with sub par credit conditions could impede credit and GDP growth.

Also, capital markets locally need to stay adequately buoyant to help see through the rather ambitious disinvestment drive. In FY 20 for instance, the disinvestment target has been scaled down from INR 1.05 trillion to INR 0.65 trillion, while the realised figure stands at INR 0.18 trillion.

Besides the world is preparing to face fresh risks arising from the effects of the health epidemic in China which could seriously slow down its GDP and pull down global growth in the near term.

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<p>PGIM India Dynamic Bond Fund</p> <ul style="list-style-type: none"> Regular income for short term To generate returns through active management of a portfolio of debt and money market instruments Degree of risk – MODERATE 		<p>PGIM India Dynamic Bond Fund</p> <ul style="list-style-type: none"> Regular income for short term To generate returns through active management of a portfolio of debt and money market instruments Degree of risk – MODERATE 	

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