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FY21 BUDGET MIGHT END WITH A FISCAL DEFICIT AT 7.4%: FY22 FISCAL DEFICIT AT 5.2%, NOMINAL GDP GROWTH AT 15%

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As per the first advanced estimate of the GDP, real GDP will contract by -7.7% in FY21, and nominal GDP growth is expected at –4.2% . Accordingly, we project **for FY22, nominal GDP would grow by 15% to Rs 224.04 lakh crore**. Current trends in the GDP for FY21 will translate into Rs 3.2 lakh crore net revenue shortfall for the Centre this fiscal and at the same time expenditure is higher by around Rs 3.3 lakh crore, **thus taking the fiscal deficit to Rs 14.46 lakh crore and with new revised nominal GDP estimate for FY21 it will be around 7.4% of GDP.** For FY22, assuming the Government keeps the expenditure growth at 6% over FY21 estimates and overall receipts (excluding borrowing and other liabilities) expected at 25%, it would result in **fiscal deficit of around Rs 11.67 lakh crore or 5.2% of GDP**. The net market borrowing of the Centre will be around Rs 8.8 lakh crore and with repayments of Rs 2.7 lakh crore gross borrowing are expected at Rs 11.5 lakh crore. With states' gross borrowing around Rs 9.4 lakh crore **total gross market borrowing would be around Rs 20.9 lakh crore, but could have a clear downward bias.**

The fiscal situation of the states is equally stretched but tad better than what was being anticipated. The combined amount of SGST, Allocated IGST and Cess stands at Rs 3.73 lakh crore, which is 13% lower than last year's collection in the same period and it is equal to 58% of the states' budgeted SGST which is Rs 6.49 lakh crore. As per our projections, if 50% of the IGST collected is disbursed to sates by Mar'21, then state GST shortfall can narrow down to around Rs 25,000 crore after taking into account the full compensation cess. **Taking all the assumptions given the current data, it appears that states will end with an overall shortage of around Rs 3.00 lakh crore in tax revenue. Overall for FY21 states had budgeted a gross fiscal deficit of Rs 6.26 lakh crore or 2.8% of GDP. However COVID-19 related slowdown in state revenues and decline in SGDP numbers can push the state fiscal deficit to 4.7%.** Overall the combined fiscal deficit for states and Centre for FY21 will be at 12.1% of GDP. With the focus on health expenditure and vaccine delivery states will also have to spare more money for the same in the next fiscal. With the FY21 Budget expenditure on health and family welfare at just about 1% of GDP, even if we assume that the states' spend around 2% of GDP on health, it entails an extra expenditure of around Rs 2.5 lakh crore from the FY21 Budget estimates. With the gains from oil getting limited as oil slowly gains $50/bbl level and taxes already high, governments will have to figure out other avenues for revenue generation.

The revival strategy will have to carefully factor in the resource crunch and yet be imaginative to finance growth. Push to infrastructure such as roads, civil aviation and agriculture will be a well advised strategy. Specifically, now that Government is creating a DFI and given the abundance of financial savings, there should be a clear plan to mobilize such savings for financing infrastructure. The power transmission assets of various state TRANSCOs may be monetized to release capital for other productive purposes. Other suggestions should focus on the rural sector by improving the credit delivery mechanisms for small and marginal farmers for loan upto Rs 3 lakh crore. Simplification and rationalisation of means for availing the KCC loan facility should be thus a major reform for the benefit of small and marginal farmers. We also need to have both a price and income support for the farmers. MSMEs with 70% turnover from exports could be awarded special status. For the banking sector uniformity in rules in recognising bad assets of CBDT must be aligned with RBI norms to unlock banking capital. For Senior Citizens, some tax incentive for savings is a necessary sine qua non and that has minimal fiscal implications. There is a need for phased reduction in Government share holding to 51% in PSBs.
One suggestion. There must not be any new taxes in the budget! Let us have a tax holiday budget, with carefully crafted policies for immediate fiscal lubrication. This could include an honest attempt by the Government to settle the tax litigation cases once and for all and also ensure all pending payments to parastatal entities are made in a time bound manner! This could be the biggest game changer.

BUDGET 2021-22: FISCAL ARITHMETIC

- As per the first advanced estimates, real GDP will contract by -7.7% in FY21, and nominal GDP growth is expected at Rs 194.8 lakh crore (-4.2%). For FY22, real GDP growth is likely to be 11% and with deflator expected at 4%, nominal GDP would grow by 15% to Rs 224.04 lakh crore in FY22 budget.
- For FY21, we believe Rs 3.2 lakh crore is the net revenue shortfall for the Centre this fiscal and at the same time expenditure is higher by around Rs 3.3 lakh crore, thus taking the fiscal deficit to Rs 14.46 lakh crore and with new revised nominal GDP estimate it will be around 7.4% of GDP.
- If we look at receipts post the 2008 crisis, they grew by more than 20%. And since inflation was more during that time and real growth was lower so in FY22 we can safely assume receipts to grow by around 25%. We expect revenue receipts to grow around 20% to Rs 21.8 lakh crore with tax revenue growth of 13% to Rs 17.1 lakh crore. Within tax revenue corporate tax will grow around 9.8% and personal income tax by around 8.6%. Meanwhile, non-tax revenue is expected to grow by 54.8% to Rs 4.72 lakh crore. Disinvestment receipts are expected at Rs 2.0 lakh crore.
- Meanwhile, the Government has stated it would vaccinate 30 crore (22% of population) prioritized individuals by August 2021 and another 50 crore (rest of the adult population) by the end of 2022. So the expenditure on vaccination drive at 0.5% of GDP should be taken into account.

Fiscal Estimates

Rs lakh crore	FY21 BE	FY21 (SBI)	FY22 (SBI)	% yoy
GDP	224.9	194.8	224.0	15.0
Receipts (Rev+Cap-Borrowing)	22.5	19.3	24.1	25.0
Tax Revenue	16.4	15.2	17.1	13.0
Non-tax Revenue	3.9	3.1	4.7	54.8
Capital Receipts - Borrowing & other liabilities	2.3	0.6	2.2	242.1
Expenditure	30.4	33.7	35.7	6
Fiscal deficit	7.96	14.46	11.67	-
Fiscal Deficit (% of GDP)	**3.5**	**7.4**	**5.2**	

Source: SBI Research

Amount under dispute at reporting year FY19 (Rs Crore)	
Taxes on Income & Expenditure	**802621**
Corporation Tax	405564
Taxes on Income other than Corp. Tax	397057
Taxes on Commodities & Services	**153982**
Customs	10903
Union Excise	55221
Service Tax	87858
Total	**956603**

- However we believe even if the Government levies additional cess to cover for vaccine drive, it should be levied only for a year or so and must not be a perpetual burden for tax payers. Our recommendation is there should not be any new taxes. Assuming that the Government keeps the expenditure growth at 6% over FY21 estimates (of Rs 33.7 lakh crore) at Rs 35.7 lakh crore in FY22 and receipts (minus borrowing and other liabilities) would grow by 25%, it would lead to fiscal deficit of around Rs 11.67 lakh crore or 5.2% of GDP in FY21.
- A game changer in the budget could be an honest attempt by the Government to settle the cases under tax litigation once and for all. This could provide the immediate fiscal lubrication. A significant amount of tax revenue is under dispute. As per the latest data available, at the end of FY19 the total amount under dispute was around Rs 9.5 lakh crore with Rs 4.05 lakh crore under corporation tax, Rs. 3.97 lakh crore stuck under income tax other than corp. tax, and another Rs 1.54 lakh crore under taxes on commodities and services.
- We believe net market borrowing of the Centre will be around Rs 8.8 lakh crore and with repayments of Rs 2.7 lakh crore gross borrowing are expected at Rs 11.5 lakh crore. With states' gross borrowing around Rs 9.4 lakh crore, total gross market borrowing would be around Rs 20.9 lakh crore, though it could have a downward bias.

STATES' FISCAL ARITHMETIC

- Dec'20 GST revenue was 12% higher than the GST revenues in the same month last year. The positive trend which started from Sep'20 has sustained and has gained momentum. The SGST collection for states is 12% lower at Rs 1.87 lakh crore in Apr-Dec'20 vis-à-vis Apr-Dec'19 and the allocated IGST is 13% lower at Rs 1.26 lakh crore. Meanwhile the cess collection is Rs 60,312 crore which is again 17% lower than last year The combined amount of SGST, Allocated IGST and Cess stands at Rs 3.73 lakh crore, which is 13% lower than last year's collection in the same period and it is equal to 58% of the states' budgeted SGST which is Rs 6.49 lakh crore. The gap between last year and this year's cumulative revenue is narrowing as GST collections have improved. As per our projections, if 50% of the IGST collected is disbursed to sates by Mar'21, then state GST shortfall can narrow down to around Rs 25,000 crore after taking into account the full compensation cess. However, the Apr-Dec'20 average allocation shows that states have got only 31% of the allocated IGST. If the Centre keeps 60% of the IGST revenue, then the states could be staring at a shortfall of around Rs 79,000 crore.
- When we look at the state VAT data till H1 FY21 the contribution of this to state exchequer was Rs 84,057 crore and the states had budgeted Rs 3.10 lakh crore for the entire year. If we assume that states garner Rs 2.5 lakh crore which is still on the higher side, there will a shortfall of Rs 60,000 crore on this head.
- Another major component the state excise, which was budgeted at Rs 1.92 lakh crore and the available data for some sates shows that they have collected around Rs 89000 crore till Nov'20. We are assuming states' revenue shortfall under this head at Rs 16,000 crore, as the entire data set is not available as of now.
- For stamp and registration fess again, the available data shows collection of around Rs 53000 crore, vis-à-vis budgeted Rs 1.56 lakh crore. Overall states can see shortfall of around Rs 60,000 crore in this head.

Market Borrowings (Rs lakh crore)			
Centre	FY20 (RE)	FY21 (Estimates)	FY22 (Estimates)
Gross Borrowing	7.1	13.1	11.5
Repayments	2.4	2.3	2.7
Net Borrowing	4.7	10.8	8.8
State			
Gross Borrowing	6.3	8.7	9.4
Repayments	1.5	1.5	2.1
Net Borrowing	4.9	7.2	7.3
Source: SBI Research			

- Taking all the assumptions given the current data, it appears that states will an overall shortage of around Rs 3 lakh crore in tax revenue.
- Overall for FY21 states had budgeted a gross fiscal deficit of Rs 6.26 lakh crore or 2.8% of GDP. However, COVID has impacted their finances, as well as, the overall GDP projections. If we take into account the GST shortfall and loss of revenue from other tax components as well as non-tax revenue the states can add Rs 3.7 lakh crore in the fiscal deficit. If we see some expenditure reduction, then also the states will add around Rs 3 lakh crore in the budgeted Rs 6.26 lakh crore, which pushes the states' fiscal deficit to 4.7% of GDP.
- **Overall the combined fiscal deficit for states and Centre for FY21 will be 12.1% of GDP. However, the pandemic has thrown government finances in a tizzy worldwide and India is no exception.**
- The states had budgeted Rs 1.86 lakh crore expenditure in medical and public health and family welfare in FY21. Meanwhile the outlay of the Centre through the Department of Health and Family Welfare was Rs 65,011.8 crore and this includes outlay to states for central schemes. With health expenditure gaining prominence and vaccine disbursement commencing this year, states will have to spend more. The expenditure of Rs 1.86 lakh crore is just about 1% of FY21 GDP. Even if we assume that states increase their health expenditure outlay to 2% of FY22 GDP it entails an extra expenditure of around Rs 2.5 lakh crore from their side.
- However, the gains from oil duties are limited as EIA forecasts Brent prices will average $47/b in the first quarter of 2021 and rise to an average of $50/b by the fourth quarter, much higher than what was witnessed in 2020. Thus the states and Centre have limited option to finance its expenditure through increasing duties which are already very high.

15TH FINANCE COMMISSION & BUDGET

- The report of 15th Finance Commission, which will be released along with the Budget this year, will pave way for tax revenue sharing in coming years.
- It is expected that there can be rationalisation of centrally sponsored schemes and the constitution of a panel to re-examine classification of legislative subjects between the Centre and states. The total public outlays on centrally sponsored schemes were close to Rs 6-7 lakh crore per annum and that the central government spends over Rs 3.5 lakh crore, or around 1.2% of GDP.
- The division of power between the Centre and the State in Schedule VII of the Constitution need to be revisited.

Sector-wise Budget Recommendations	

Agriculture	• Nearly 60% of Agri credit is by way of KCCs. So, simplification and rationalisation of means for availing of the KCC loan facility should be a major reform for the benefit of small and marginal farmers. We propose:
	  ◦ Renewal of KCC loans of small and marginal farmers for amounts up to Rs 3 lakh, the payment of interest be an enough condition for renewal.
	  ◦ Additionally, the interest subvention benefit which at present accrues only for crop cultivation and working capital loans for allied agricultural activities can be extended to cover term loans for investment credit purposes availed by small and marginal farmers without increasing the overall loan limit of Rs 3 lakhs for eligibility.
	• Currently there are 11.5 crore farmers who are getting PM KISAN and 6.5 crore farmers have KCC. Thus, the remaining 4-5 crore could be land owning cultivators and at least 3-4 crore of such could be tenants/lessees/ landless. Currently, such tenant farmers are not formalised into the credit delivery mechanism. We propose, that to enable lending to tenant farmers/lessee farmers/landless farmers, formation of a SHG model under Deen Dayal Antodoya Yojana under National Rural Livelihood Mission that is being run by the Centre can be used for lending by banks for agri and allied activities. The Government can incentivise such with a bare minimum fiscal support of Rs 27 crore that could support 2.7 lakh SHGs.
	• We need to have both a price and income support for the farmers. This is akin to what the RBI is currently providing both a price and quantity support in terms of liquidity management for financial markets.
	  ◦ Price support: Examine the feasibility of converting Minimum Support Price for select commodities to Floor Price of Auction on National Agriculture Market (eNAM).
	  ◦ Quantity support: A quantity guarantee clause for a specified period that procurement to production percentage of procured crops every year should at least be equal to previous year percentage (with safeguards in exceptional events like droughts, etc. when farmers selling outside APMC to benefit from higher prices)
	• Setting up a Contract Farming regulator in India with adequate oversight as small and marginal farmers should have the necessary wherewithal to deal with large buyers. Global experience shows successes in contract farming is often not sustained as large firms initially attract small growers with favourable conditions, but later tightens them.
	• Banks are investing more than Rs 1 lakh crore in RIDF as shortfall in PSL. There is a new Credit Guarantee Fund Trust for Agriculture created under the auspices of NABARD for which the corpus is set as Rs 500 crore. Even though RIDF is a repayable source of funds, since it is likely to remain on tap for a long time, a small percentage, say 3%, of RIDF could be used as additional contribution for the Agri Credit Guarantee Fund Corpus purely for the use of small and marginal farmers. This has the potential to add Rs 4000 crore to the Fund Trust without causing much of problems and these funds are often unutilised and are callable.

MSMEs	• 2% interest subvention for all GST registered MSMEs, on fresh or incremental loans may be continue. All the Loans up to Rs 2 crore to MSME should be mandatory to be sanctioned with CGTMSE coverage. • Investment in Plant and Machinery needs to be incentivized and MSMEs be provided subsidy on the investment made in plant and machinery. • MSMEs with 70% turnover from exports could be awarded special status, entitling them to various incentives such as subsidized land in an export promotion zone, faster clearances, cheaper finance, etc. ECGC Premium to export oriented unit may be waived.
Senior Citizens	• Government has an excellent scheme for senior citizens. Under Senior Citizens Savings Scheme (SCSS), a senior citizen can deposit Rs 15 lakh. However, the interest on SCSS is fully taxable which is a major drawback of this scheme. We propose full tax rebate of this interest income • Under 80TTB interest income from deposits by senior citizen (Savings bank accounts, fixed deposits, recurring deposit accounts) up to Rs 50,000 is exempted from income tax. This threshold may be increased to Rs 1 lakh.
Health	• Medical Savings account wherein a part of the advance tax goes to Mediclaim policy – thus enabling customers to take advantage of EMIs. A scheme to deduct Interest from Savings Account and pay towards Mediclaim policy can be thought of. Size of the health insurance is Rs 32,000 crore and savings bank interest is Rs1.15 lakh crore. • The government should consider exempting all health insurance products from GST, if not for full range of products, at least for all retail and health focused products. At a time when Governments are grappling with pandemic scenarios, they can look at making Health insurance more affordable

Sector-wise Budget Suggestions	
Banking Services	• All the Loans up to Rs 2 crore to MSME should be mandatory to be sanctioned with CGTMSE coverage. The lock in period should be reduced to six months from the present 18 months. • CGTMSE Annual Premium Fees should be waived. iii) Enhance the credit guarantee scheme for companies in the identified 26 sectors having credit outstanding of up to Rs 1000 crore as at 29-Feb-2020 into the 1+4 year loan scheme. • Income-tax Act rules provide for recognition of income on Bad and Doubtful debts in accordance with the rules framed by CBDT which provide for 6-months overdue delinquency norms. The rules issued by CBDT for recognition of income on Bad and Doubtful debts need to be amended to be in line with the RBI guidelines in this regard. • Phased reduction in Government share holding to 51% in PSBs
Payment services	• Access to Central Repository of Information on Large Credits (CLIRC) portal should be provided to non-bank entities as well to enable them to view the SMA status of its borrowers as reported by other lenders. • Government may prohibit levying of any convenience fee, services charges and other charges on use of online payment, credit card or any other mode of digital payment for making payment to a merchant. • Approval may be granted for enabling credit cards as a payment option on UPI platform for customers making payment to merchants (Peer to Merchant).
Fiscal Policy	• Withdraw all tax appeals where the Government has lost at the Tribunal level . Accept all domestic arbitration decisions against government departments/agencies. Withdraw judicial appeals. Make the payments. • There should be no insistence in Bank Guarantees from assesses and contractors as this defeats the purpose. This simply means that the State gracefully accepts its defeat when an impartial Tribunal has ruled against. All these payments need to be made eventually anyway as the state loses 70% of appeals at every level. • The advantages of such will be immediate fiscal lubrication. In that sense, these do not constitute Fiscal Deficit target excesses. One can even think of them as a one-time balance sheet entry recognizing liabilities and paying them off.
Infrastructure	• The power transmission assets of various state TRANSCOs may be monetized to release capital for other productive purposes. The monetization may be carried out through privatisation (as a TOT model in road sector) or through InvIT structure. The government shall provide a roadmap for such monetisation which will help the state finances to some extent • Change the mix of Public Vs. Private in NIP: Private share to raise to 30% • Allowing retail participation in infrastructure monetization through issue of tax Free Bonds- Banks and Institutions should be allowed to raise tax free infrastructure bonds (preferred tenor 15-20 years) and the exclusive purpose of such resources should be for Infrastructure project finance. • Aviation Turbine Fuel (ATF) to be brought under the GST framework to provide for full input tax credit • Full digitization of port infrastructure for faster good mobility

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