UNION BUDGET - FY22

Not a Dream, Not a Nightmare – Sun Shines through

ASK WEALTH ADVISORS

Key takeaways

No tinkering: Union Budget for FY22 spared any major tinkering on the tax rates, either direct or indirect. This outdid the market expectations of some form of Covid/Wealth tax and therefore is a big positive for equity markets.

Our take: This is the key reason for the relief rally in the equity market. Raising the limits for tax scrutiny is a significant positive doing business measure.

Union Budget for FY22 – Key figures

	INR bn		YoY%		% of GDP	
	FY21RE	FY22BE	FY21RE	FY22BE	FY21RE	FY22BE
I. Total Receipts (non-debt)	**1,602**	**1,976**	**-8.6**	**23.4**	**8.2**	**8.9**
Of which						
Net tax revenue	1,345	1,545	-0.9	14.9	6.9	6.9
Non-Tax revenue	211	243	-35.6	15.4	1.1	1.1
Non-debt capital receipts	46	188	-32.2	304.3	0.2	0.8
Debt capital receipts	1,866	1,435	116.9	-23.1	9.6	6.4
II. Total Expenditure	**4,096**	**4,066**	**23.1**	**-0.7**	**21.0**	**18.2**
Of which						
Capital expenditure	1,085	1,137	11.0	4.8	5.6	5.1
Revenue expenditure	3,011	2,929	28.2	-2.7	15.5	13.1
Of which Subsidies	595	335	160.7	-43.7	3.1	1.5
III. Fiscal Deficit	**1,849**	**1,507**	**98.0**	**-18.5**	**9.5**	**6.8**
Revenue Deficit	1,456	1,141	118.4	-21.7	7.5	5.1
IV. Net Borrowing	**1,053**	**925**	**122.1**	**-12.2**	**5.4**	**4.1**
Gross borrowing	1,280	1,206	80.3	-5.8	6.6	5.4
Repayments	-227	-281	-3.7	23.6	-1.2	-1.3

Note: YoY% for FY21RE has been computed over FY20 Actuals while FY21BE over FY20RE.

Source: Government, CMIE, ASKWA Research.

Stimulus: It wasn't "We spent, We spent, We spent", but there was a fiscal stimulus in FY21 after all. The expenditure increased to 17.7% of GDP from 13.2% during FY20. This translates into 28.4% YoY growth on FY20 actual expenditure. While at the headline numbers show ~4% of GDP stimulus, a chunk of it was merely clearing up of Union Budget accounts – subsidy arrears from previous years and bringing Food Corporation of India (FCI) borrowing brought inside the budget. Excluding the drop in nominal GDP (-4%) and clearing of arrears, etc. it would still amount to a stimulus of around 2.5% of GDP. FY22 expenditure is planned to stay high at 15.7% of GDP. However, this is only 1% increase over FY21RE. Thus, FY22 would be a more of a maintaining level of expenditure rather than growth.

Our take: There was a stimulus in FY21, more than what was earlier thought, but less than what it appears. FY22, though, is an year of normalisation rather than fiscal boost.

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Fiscal Credibility: There are a lot of elements suggesting improved credibility of fiscal nos and point to potential upside.

i) Taking FCI borrowing out of small savings to on balance sheet (partially in FY21 and completely in FY22). However, this also poses challenge of comparability of expenditure figures FY21 onwards.
ii) Nominal GDP growth rate projected conservatively at 14.4% as compared with 15.4% in recently released Economic Survey.
iii) Tax buoyancy assumed at just 1.1 in FY22 pointing towards upside potential. Tax to GDP ratio for FY22 assumed same as FY21 at 6.9% of GDP.
iv) Disinvestment figure have been pegged at INR1,750 bn is being considered realistic provided the buoyant market conditions remains and privatization plan could be given shape in time.
v) Reduction in Extra Budgetary and Other Resources to just INR300 bn during FY22 from INR1,261 bn in FY21.
vi) However, no year-wise medium term fiscal deficit reduction plan announced apart from an FY25 target of 4.5% of GDP.
vii) The practice of cherry-picking certain expenditure head clouds overall actual spend under major expenditure heads/Ministries.

Our take: The gentler glide-path of FRBM proposed now is good news for growth, even though the government hasn't really busted any charts on expenditure for FY22.

Deficit and Borrowing:

i) **Deficit**: Headline fiscal deficit is at 9.5% for FY21. However, chunk of it is merely the one-time clean-up of Budget accounts (as described earlier). FY22 deficit has been pegged at 6.8%. This however has some clack built-in, given a modest 1% expenditure growth and very realistic estimates of nominal GDP growth and tax buoyancy.
ii) **Borrowing**: As the headline deficit figures are higher than market expectations so are the market borrowing figures too. Net (gross) market borrowing at INR9.2 tn (INR13.9 tn) is expected to reduce only by INR1.3 tn (INR545 bn). However, once again these figures need to be adjusted by the reduction in other modes of financing which are of higher dimension (INR1.8 tn), especially small savings (INR886 bn) for a like to like comparison.

Our take: In our assessment RBI would need to be in continued accommodative stance to fund the borrowing calendar comfortably. However, a better expenditure quality (capex has gone up faster than overall expenditure) and a comfortable external account would give enough levers for RBI to continue to provide monetary support to the fisc.

The reforms measures:

i) Time limit for re-opening direct tax assessments reduced
ii) Dispute resolution committee for small tax payers
iii) Ambitious privatization plan announced, including 2 banks, one insurance company and Air India.
iv) New institutions like a Development Finance Institution and an ARC for tackling NPAs.
v) Proposal to launch National Asset Monetisation Pipeline
vi) FDI limit in insurance hiked to 74%

Our take: While these are all positive, they are dependent on significant legislative work and prone to execution challenges – hence need higher timeframe than one year.

Market Reaction – Equities overbought Bonds oversold

i) The equity market gained +4.7% while 10-year GSec yields in bond market increased by 11 bps (to 6.06%) on the day of announcement of the Budget.

ii) As outlined earlier, there is no medium-term fiscal boost emerging from the FY22 deficit or from the expenditure plan. Government spend is not a sustainable driver for market. The policy announcements – privatization, asset monetization etc. – are all positive but immediate market impact may be upfronting the effects too quickly.

iii) Bond markets were spooked by the higher-than-expected deficit (for both FY21 and FY22) as well as increased borrowing for the current year i.e., Q4FY21. However, given the incipient nature of economic recovery (widely recognized to be K-shaped, with disproportionate negative impact on the bottom half of population and enterprises), there are very few arguments for monetary tightening. The yield curve is already quite steep, we would expect a bear-flattening of the curve, i.e., shorter-term yields inching up gradually even as longer rates are supported by RBI.

iv) In a nutshell, the market is discounting too much of the positives on Equities and too much of negatives on Bonds. Both are likely misreading the fundamentals of the Budget.

v) The sun though shines through – sans any negative surprises on taxes, the ongoing cyclical recovery and global liquidity provide tailwinds to markets. Investors continue to have room to invest rather than sit out – in a range of assets.

vi) We remain neutral on both Equities and Bonds. Our overweight call on REITs received a small shot-in-the-arm from the Budget.

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