Fine balance in the fiscal calculus

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IN THE FIRST full year Budget of the third term of the present government, the finance minister was tasked with presenting a roadmap for short term fire-fighting to deal with slowdown in the economy and potential turbulence in the global economy on one hand and to provide policy direction for aspirations of *Viksit Bharat*. The Budget speech provided direction by focusing on agriculture, MSMEs, Investment and exports. Further, significant reduction in income tax rates is expected to stimulate demand and provide a growth momentum in the short term.

The Budget has successfully navigated the course in a tough context and reiterated the commitment to fiscal consolidation. The finance minister has presented a Budget which adheres to the fiscal consolidation path set out by the 15th Finance Commission. Fiscal deficit for 2024-25 is forecast to be 4.8% of GDP, marginally lower than the Budget Estimates. For FY26, the finance minister has proposed a fiscal deficit of 4.4% of GDP. Further, she has reiterated commitment to fiscal consolidation in the medium term as well. This is very commendable since it suggests continuity and consistency in policy stance of the government.

Consistent reduction in debt and the moderation in the interest rates have meant moderation in the resources cornered by interest payment. The ratio of interest payment to revenue receipts has declined from a high of 39% in FY24 to 37%, marginally higher than the levels reported for Revised Estimates of FY25.

However, some stress points are evident in the revised estimates of FY25. The current fiscal year represents a departure from fiscal performance in last few years. In earlier years, tax revenues exceeded budgeted numbers and the additional fiscal space was used to accommodate higher spending by the government. In FY25, tax revenues fell short of the budgeted levels. To accommodate for the shortfall, expenditure was compressed. While revenue receipts are lower by about ₹41,000 crore, expenditures are lower by about ₹1 lakh crore, largely accounted for by lower levels of capital outlay. The result is lower fiscal deficit. Whether this is prudent fiscal management or the particular context remains unclear.

Turning to budget numbers for FY26, against a projected growth of 10.1% of GDP, the revenue forecast is more modest. Customs and Union excise duty are forecast to grow at rates between 2-3%. Personal Income Tax and CGST are forecast to grow faster than the assumed growth in GDP—at 11% and 14% respectively. Together, gross revenue receipts are expected to grow at 10.8%. Customs revenues reflect policy changes through rate rationalisation. They perhaps also reflect on global uncertainties. It should be noted that even with a significant reduction in tax rates, with a suggested impact of ₹1 lakh crore, PIT is expected to grow by 14%.

Sustained growth of personal income tax and GST are critical for supporting the proposed budget.

On the expenditure side, forecasts for revenue and capital expenditure indicate growth of 6.7% and 10.1% respectively, over RE numbers for FY25. These numbers seem reasonable and are similar to those for recent years. However, there are two elements of detail that might be useful to look at. Interest payment, a sizeable component of revenue expenditure, is expected to grow at over 12%. Establishment expenditure is forecasted to grow at around 6%. Net of these components, revenue expenditure is to grow at 4%, suggesting limited room for maneuverability.

The careful balancing act of the Budget is a commendable exercise in managing expectations and providing direction. Uncertainties can be managed through nimble adjustments.