HSBC Mutual Fund

# The Macro Sphere
# India Budget FY27

CapEx Thrust with slower consolidation, higher market borrowing

# Key takeaways from the Union Budget



- Budget focused on three C's = Consistency, CapEx and Consolidation –
  - **Consistency** in tax policy, spending allocations, sectoral push – MSMEs, Semiconductors 2.0, Textiles; Streamlined customs/import duties. A 20-year tax holiday for data centre in hi-tech sector space while for labor-intensive manufacturing the focus was more on infra connectivity and smoothening of processes/operational ease
  - **CapEx** thrust continued despite the headwinds to revenue mobilization and sticky recurring expenditure
  - **Consolidation** commitment adhered to; With the new avatar and anchor, the pace of fiscal consolidation for FY27 continues but is rather slow-paced in nature. Rightly so, given the income tax rate changes and the Goods & Services Tax (GST) rate changes of FY26.
- Rationalization of customs/import duties, TCS rate reduced, Minimum Alternate Tax (MAT) for certain sections were announced. Given the headwinds to tax mobilization, the govt. has hiked Securities Transaction Tax (STT) wherein –
  - **STT** on Futures to 0.05% from present 0.02% and that on options premium is raised to 0.15% from 0.1% and on exercise of options it is raised to 0.125%.
- Fiscal Deficit numbers for FY26 and FY27 are broadly in-line with our expectations; For FY27, debt-to-GDP is to fall to 55.6% vs 56.1% in FY26; implying a deficit of 4.3% of GDP. The new fiscal anchor of debt-to-GDP ratio is to be brought down to 50% +/- 1% by FY31
- The 16th Finance Commission (SFC) Report recommendations have been accepted with the devolution of transfers from the Centre's pool retained at 41% with focus on grants for rural & urban local bodies, and disaster management. Compared to the previous report, the horizontal devolution is likely to change, and wary across States following the change in definitions for criteria, weights in the SFC.

**The Three C's = Consistency, CapEx and Consolidation**

Source: India Union Budget Documents, CMIE, RBI Database, Bloomberg, HSBC AMC, FI, Economic Research Desk

# The Fiscal Math: The rise in market borrowing to bridge the deficit gap

- For FY26, the govt. is set to meet its fiscal deficit target of 4.4% of GDP without sharply cutting back on CapEx and despite a shortfall of ~INR 1.6 tn on Net tax revenue. Increased Non-tax revenue and decline in RevEx to the tune of ~INR 800bn offset the fiscal impact.
- For FY27, Revenue projections appear conservative with Revenue Receipts estimated to increase by 5.7% YoY; with nominal GDP growth of 10% YoY. Overall, the tax buoyancy has moderated and dipped below unity, to 0.8, mainly arising from weaker indirect tax growth for FY27.
- While Non-tax revenue is flat-to-modestly negative, the Dividend/surplus of RBI, nationalised banks & financial institutions will be key to watch. In FY26, a higher than budgeted surplus transfer cushioned from lower tax revenue mobilization.
- Having said that, another trend to look out for is the collection under Non-debt capital receipts; It is budgeted to rise 85% YoY, mainly due to the Disinvestment (asset-monetization) target of INR 800bn, the highest seen in last ~6-years.
- On the headline deficit and debt to GDP ratios, and consequently, market borrowing (dated and short-term) was expected to rise marginally. However, even with dated securities to fund ~69% of fiscal deficit, the reliance on short-term borrowing at ~8% of fiscal deficit is likely to be sentiment dampener. Moreover, the absence of buybacks and the Redemption of INR 5.5 tn, the Gross Borrowing is at a whopping INR 17.2 tn, higher than the street expectations of INR 16.0-16.5 tn.
- While the SFC retaining devolution, there is increased allocation to States CapEx loans, transfer to States is higher, and the report recommends the continuation of 3% of fiscal deficit at the State level could keep the borrowing in check. Nevertheless, the horizontal devolution impact at State level needs to be monitored. Meanwhile, the supply overhang is likely to keep market participants on tenterhooks.
- The RBI MPC meet on 6-Feb is expected to maintain a dovish hold with focus on liquidity guidance and additional liquidity measures.
- We retain our view on staying nimble footed with accrual strategy while taking any tactical duration calls.

**Supply overhang likely to keep yields under pressure; We retain our accrual strategy and tactical duration calls**

Source: India Union Budget Documents, CMIE, RBI Database, Bloomberg, HSBC AMC, FI, Economic Research Desk

# Budget at a glance – Conservative estimates; Disinvestment target higher



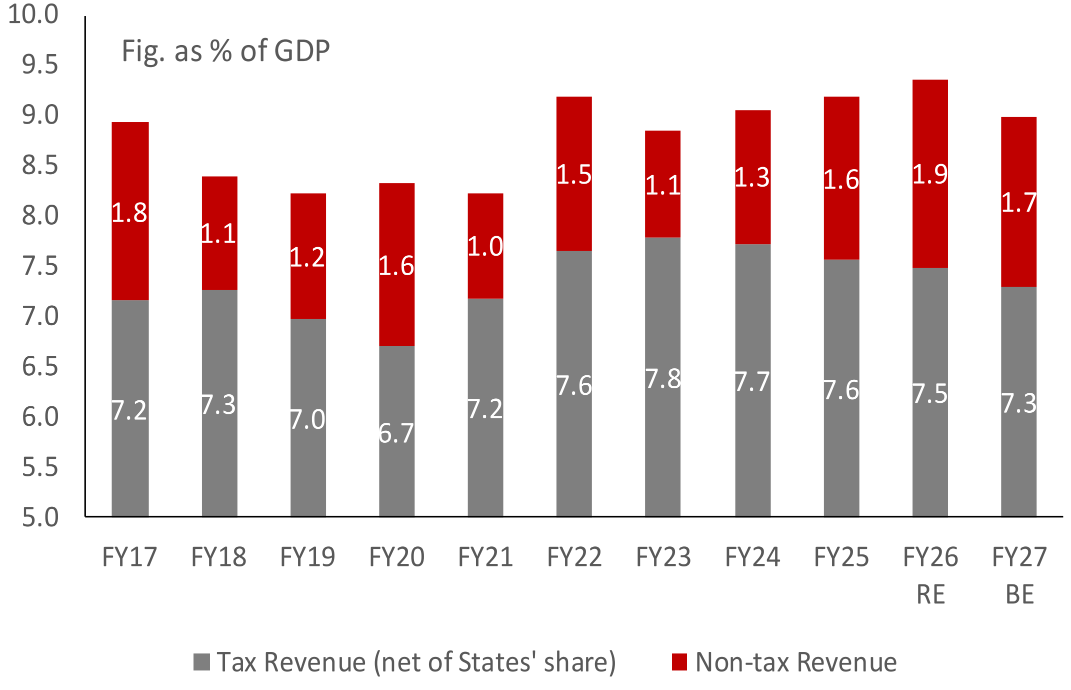
| | INR Trillion | | | | | % YoY | | | % of GDP | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Budget at a glance | FY24 | FY25 | FY26 BE | FY26 RE | FY27 BE | FY25 vs FY24 | FY26 RE vs FY25 | FY27 BE vs FY26 RE | FY25 RE | FY26 RE | FY27 BE |
| Revenue Receipts | 27.3 | 30.4 | 34.2 | 33.4 | 35.3 | 11.3% | 10.1% | 5.7% | 9.2% | 9.4% | 9.0% |
| Gross Tax Revenue | 34.7 | 38.0 | 42.7 | 40.8 | 44.0 | 9.5% | 7.4% | 8.0% | 11.5% | 11.4% | 11.2% |
| Net Tax Revenue | 23.3 | 25.0 | 28.4 | 26.7 | 28.7 | 7.4% | 7.0% | 7.2% | 7.6% | 7.5% | 7.3% |
| Income Tax | 10.6 | 12.5 | 14.5 | 13.3 | 14.9 | 18.0% | 6.3% | 12.5% | 3.8% | 3.7% | 3.8% |
| STT* | 0.3 | 0.5 | 0.8 | 0.6 | 0.7 | 54.5% | 22.0% | 15.8% | 0.2% | 0.2% | 0.2% |
| Corporate Tax | 9.1 | 9.9 | 10.8 | 11.1 | 12.3 | 8.3% | 12.4% | 11.0% | 3.0% | 3.1% | 3.1% |
| Customs | 2.3 | 2.3 | 2.4 | 2.6 | 2.7 | 0.0% | 10.8% | 5.0% | 0.7% | 0.7% | 0.7% |
| Excise | 3.1 | 3.0 | 3.2 | 3.4 | 3.9 | -1.7% | 12.1% | 15.6% | 0.9% | 0.9% | 1.0% |
| GST | 9.6 | 10.3 | 11.8 | 10.5 | 10.2 | 7.3% | 1.9% | -2.6% | 3.1% | 2.9% | 2.6% |
| Transfer to States | 11.4 | 13.0 | 14.3 | 14.0 | 15.4 | 13.9% | 8.2% | 9.6% | | | |
| Non-Tax revenue | 4.0 | 5.4 | 5.8 | 6.7 | 6.7 | 33.5% | 24.4% | -0.2% | 1.6% | 1.9% | 1.7% |
| Non Debt Capital Receipts | 0.6 | 0.4 | 0.8 | 0.6 | 1.2 | -30.0% | 53.1% | 84.9% | 0.1% | 0.2% | 0.3% |
| Misc. Receipts (incl.Divestment) | 0.3 | 0.2 | 0.5 | 0.3 | 0.8 | -48.1% | 96.7% | 136.4% | 0.1% | 0.1% | 0.2% |
| Total Receipts | 27.9 | 30.8 | 35.0 | 34.1 | 36.5 | 10.4% | 10.7% | 7.2% | 9.3% | 9.5% | 9.3% |
| Total Expenditure | 44.4 | 46.5 | 50.7 | 49.6 | 53.5 | 4.7% | 6.7% | 7.7% | 14.1% | 13.9% | 13.6% |
| Revenue Expenditure | 34.9 | 36.0 | 39.4 | 38.7 | 41.3 | 3.1% | 7.4% | 6.6% | 10.9% | 10.8% | 10.5% |
| Interest Payments | 10.6 | 11.2 | 12.8 | 12.7 | 14.0 | 4.9% | 14.2% | 10.2% | 3.4% | 3.6% | 3.6% |
| Subsidies | 4.1 | 3.9 | 3.8 | 4.3 | 4.1 | -6.6% | 11.6% | -4.5% | 1.2% | 1.2% | 1.0% |
| Capital Expenditure | 9.5 | 10.5 | 11.2 | 11.0 | 12.2 | 10.8% | 4.2% | 11.5% | 3.2% | 3.1% | 3.1% |
| Fiscal Deficit | 16.5 | 15.7 | 15.7 | 15.6 | 17.0 | -4.8% | -1.0% | 8.8% | 4.8% | 4.4% | 4.3% |
| Nominal GDP | 301.2 | 330.7 | 357.0 | 357.1 | 393.0 | 9.8% | 8.0% | 10.0% | | | |
| **Fiscal Deficit-to-GDP** | **5.5%** | **4.8%** | **4.4%** | **4.4%** | **4.3%** | | | | -0.74% | -0.36% | -0.10% |
| **Debt-to-GDP** | **57.6%** | **56.2%** | **56.1%** | **56.1%** | **55.6%** | | | | **-1.43%** | **-0.01%** | **-0.54%** |

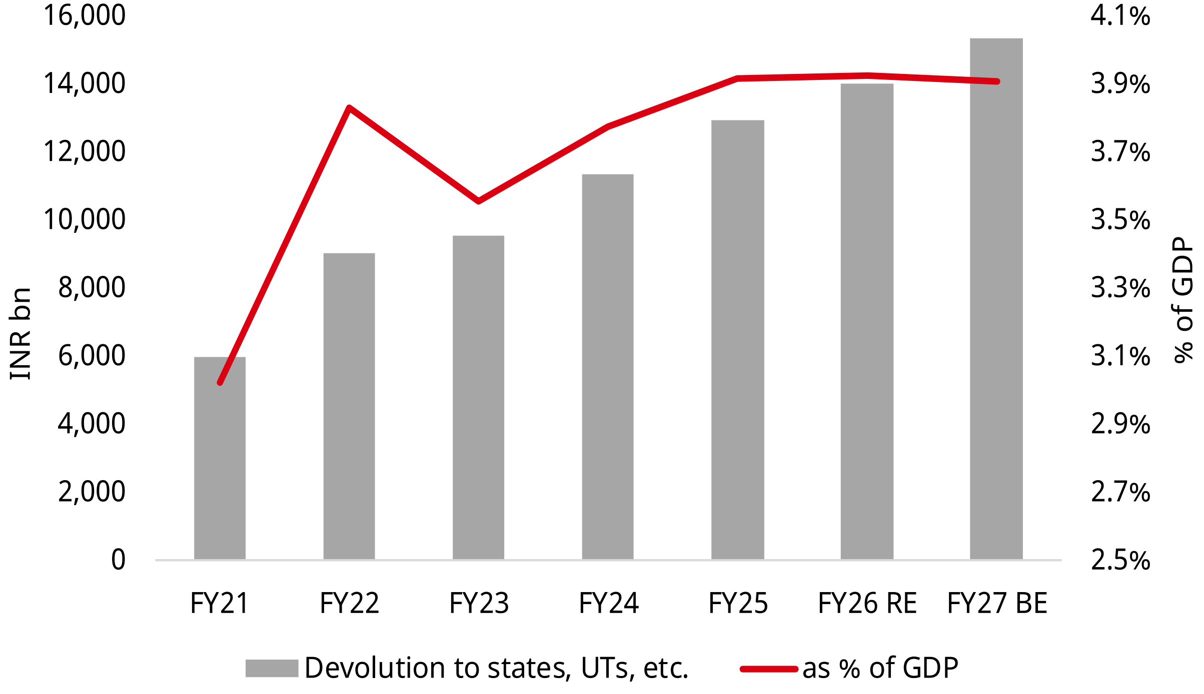
Note: Total receipts is non-debt receipts;* STT = Securities Transaction Tax

Source: India Union Budget Documents, CMIE, RBI Database, Bloomberg, HSBC AMC, FI, Economic Research Desk

# Revenue Receipts and Devolution to States



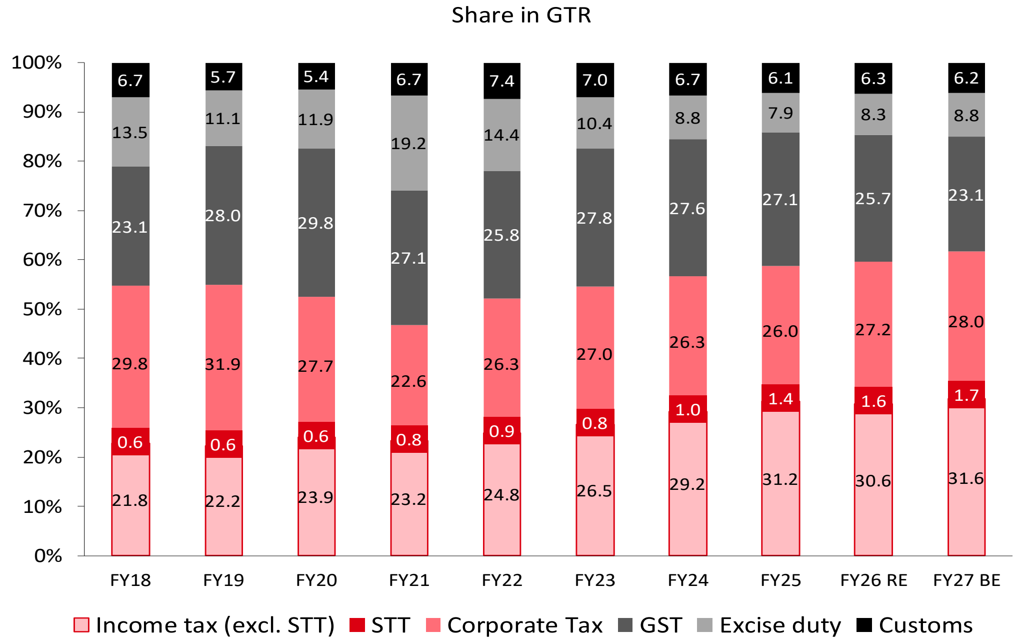



**Weaker Revenue Receipts in FY27; Devolution to States by Centre retained at 41%**

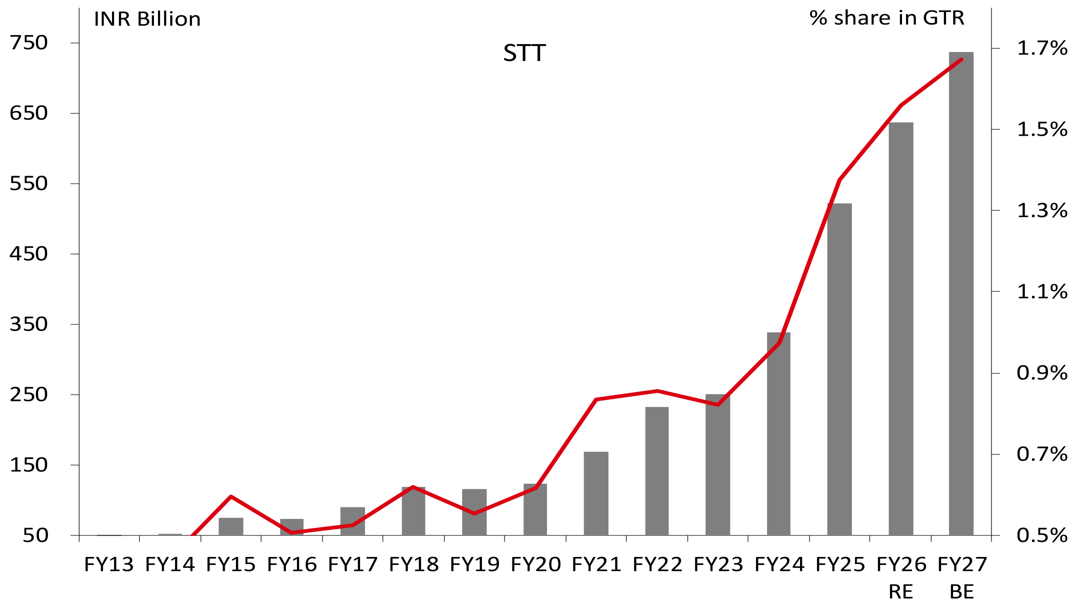
Source: India Union Budget Documents, CMIE, RBI Database, Bloomberg, HSBC AMC, FI, Economic Research Desk Any views expressed were held at the time of preparation is based on the information available in the public and are subject to change without notice. While any forecast, projection or target where provided is indicative only and not guaranteed in any way. HSBC Asset Management India Pvt. Ltd. accepts no liability for any failure to meet such forecast, projection or target. Past performance may or may not be sustained in future and is not a guarantee of any future returns.

# Direct & Indirect Tax – the changing contours of each in last decade




| | FY18 | FY19 | FY20 | FY21 | FY22 | FY23 | FY24 | FY25 | FY26 RE | FY27 BE |
|---|---|---|---|---|---|---|---|---|---|---|
| Customs | 6.7 | 5.7 | 5.4 | 6.7 | 7.4 | 7.0 | 6.7 | 6.1 | 6.3 | 6.2 |
| Excise duty | 13.5 | 11.1 | 11.9 | 19.2 | 14.4 | 10.4 | 8.8 | 7.9 | 8.3 | 8.8 |
| GST | 23.1 | 28.0 | 29.8 | 27.1 | 25.8 | 27.8 | 27.6 | 27.1 | 25.7 | 23.1 |
| Corporate Tax | 29.8 | 31.9 | 27.7 | 22.6 | 26.3 | 27.0 | 26.3 | 26.0 | 27.2 | 28.0 |
| STT | 0.6 | 0.6 | 0.6 | 0.8 | 0.9 | 0.8 | 1.0 | 1.4 | 1.6 | 1.7 |
| Income tax (excl. STT) | 21.8 | 22.2 | 23.9 | 23.2 | 24.8 | 26.5 | 29.2 | 31.2 | 30.6 | 31.6 |

Source: CMIE; Note: GTR = Gross Tax Revenue, STT = Securities Transaction Tax (STT)




- Share of Income tax in Gross Tax Revenue (GTR) has steadily increased ; Corporate tax rate has dropped compared to the pre-Covid years
- Following the GST rate rationalization, GST share estimated to fall
- ..to offset the revenue impact as well as deter activity in the F&O segment, the govt. has raised STT
- …STT composition has increased from 0.6% to 1.7% as per FY27 BE. STT Revenue has increased from ~INR 50bn to INR 700-odd billion
- …STT as % of GDP now makes up 0.2% of GDP

**Income tax mop-up is higher with GST share now budgeted to fall**

Source: India Union Budget Documents, CMIE, RBI Database, Bloomberg, HSBC AMC, FI, Economic Research Desk

# Walking the tightrope



- **CapEx Thrust**
  - Budget allocates INR 12.2 tn with a modest miss in FY25 budgeted levels; a 11.5% growth YoY
  - Capital spending has been maintained at 3.1% of GDP in FY27BE
  - The top-5 focus areas are – Defence, Roads & Highways, Railways, CapEx loans to States
  - While the allocation as % of GDP is flat-sih to modestly higher, Defence outlay increases 17% YoY & vs 15% in FY26, Roads & highways up 8% YoY
  - Capex loans to States outlay increased 33% YoY to INR 2 tn vs INR 1.5 trn in FY26 RE

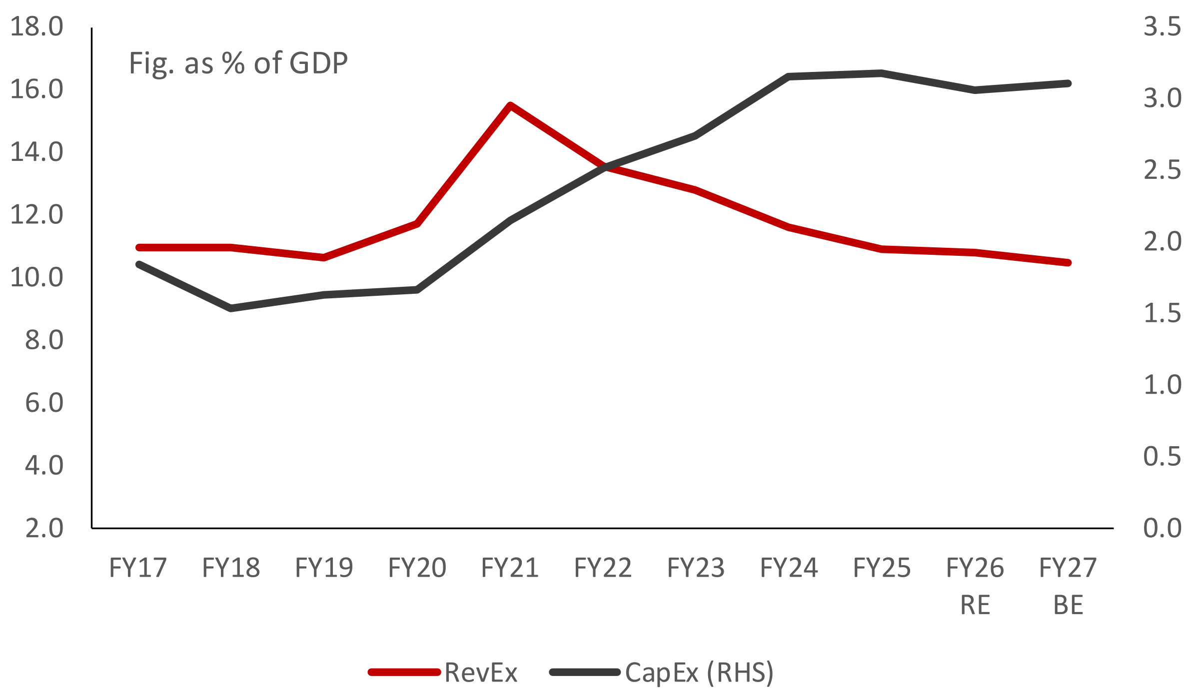
- **Total expenditure to increase to INR 53.5 tn in FY27 from INR 49.6 tn in FY26 with an improved ReCo**
  - The total revenue expenditure for FY27 is budgeted to rise by 7.7% YoY at INR 41.3 tn;
  - Higher allocation witnessed for Ministry of Jal Shakti, Education, Health and Urban Development
  - Interest payments (IP) and Subsidies make up for ~45% of RevEx; but subsidy outgo has fallen to 1% of GDP, whereas IP is at ~3.6% of GDP
  - Revenue expenditure has increased at slower rate of 6.6% YoY and as a % of GDP it has dropped to 10.5% of GDP from 10.8% in FY26RE
  - The growth in CapEx is higher than that of RevEx; further bettering the ReCo
  - Revenue and Primary Deficits to GDP reflect the improving trends in spending
  - Total Expenditure as % of GDP is modestly squeezed to 13.6% as CapEx continued to rise

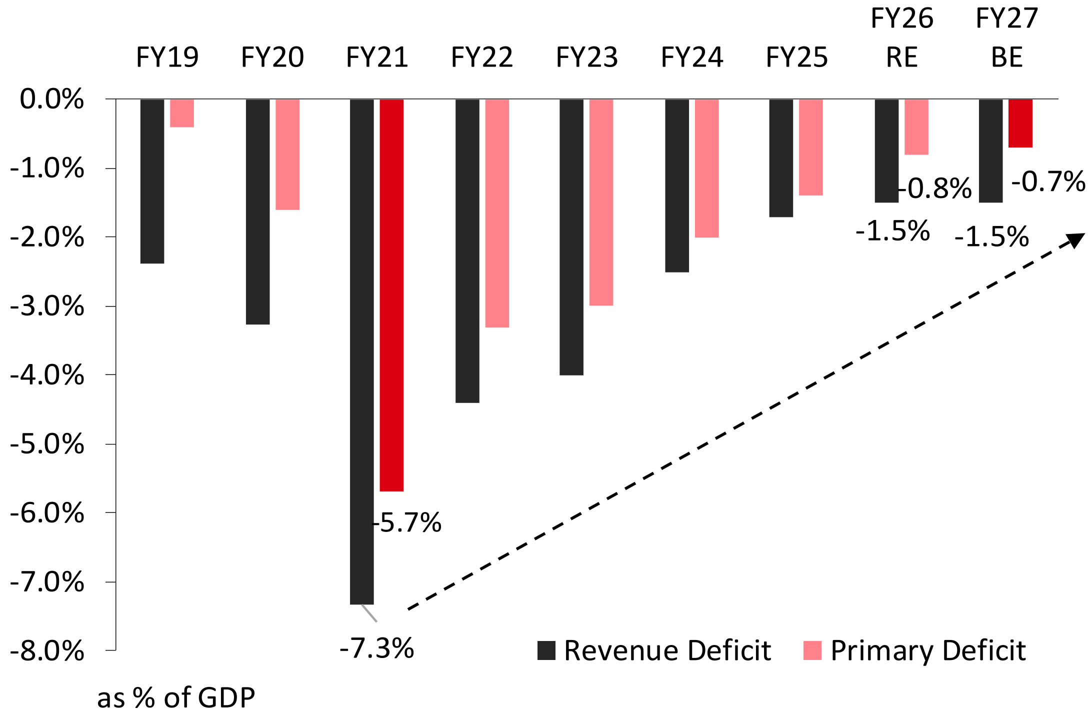
- **Subsidy expenditure projected to decline, but interest payments outgo elevated**
  - Total subsidies to ease to be modestly lower at INR 4.1 tn; falling marginally to 1% of GDP
  - Interest payments are expected to rise 10% YoY to INR 14.0 tn or 3.6% of GDP – while lower than CapEx growth rate of 11.5%, it is higher than 3.1% of GDP!
  - A debt-to-GDP glide path laid out in the budget under the FRBM is likely to improve the expenditure mix
  - The current higher than expected borrowing figures delay the quick consolidation; the short-term borrowing increase limits the spillover to next year

**CapEx fares better than RevEx; State-level spending mix watched**

Source: India Union Budget Documents, CMIE, RBI Database, Bloomberg, HSBC AMC, FI, Economic Research Desk

# The Fish Tail: Improving ReCo*



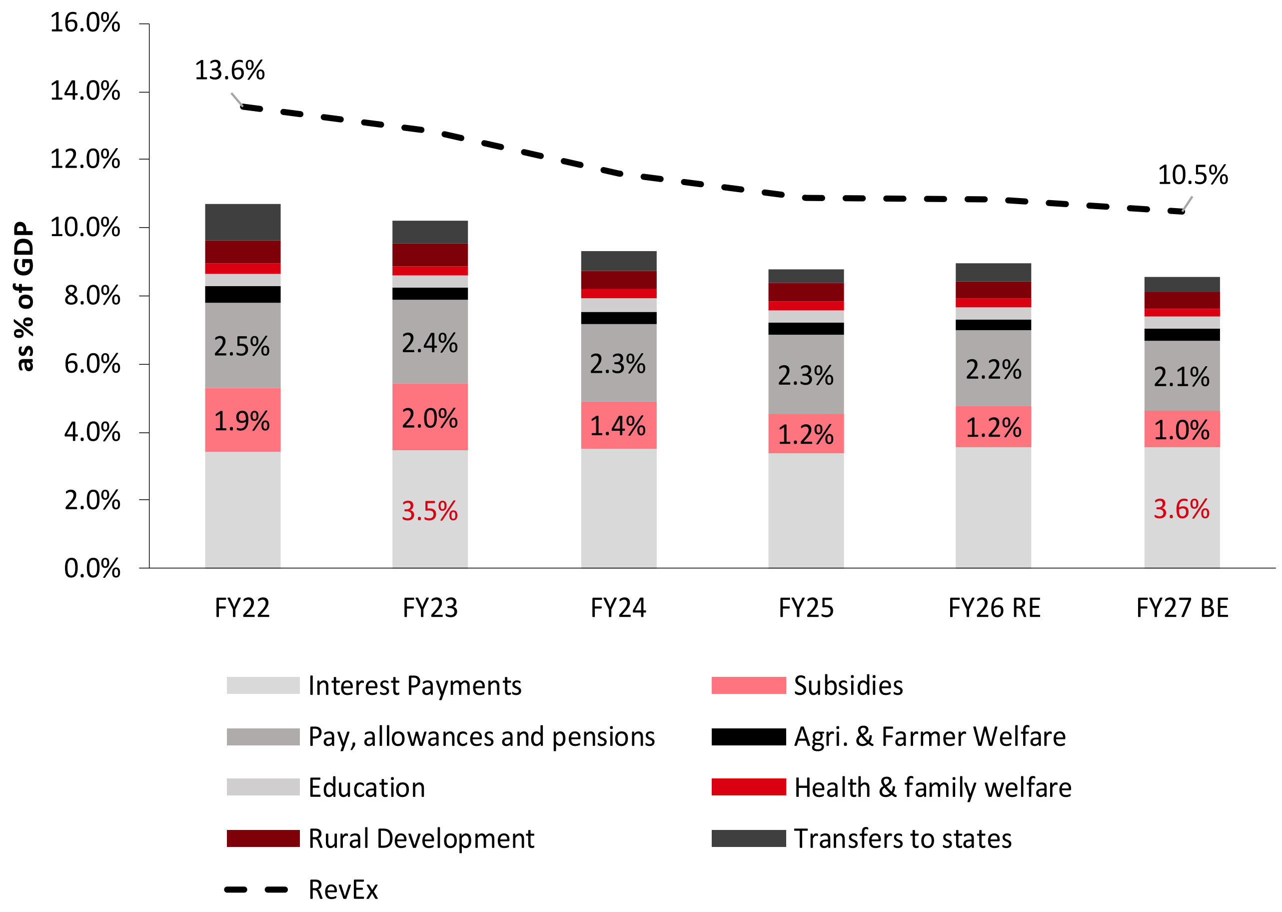




**The improved expenditure mix is reflected in lower Revenue and Primary Deficits**

Note: ReCo is referred to Revenue Expenditure-to-Capital Outlay;
Source: India Union Budget Documents, CMIE, RBI Database, Bloomberg, HSBC AMC, FI, Economic Research Desk

# Recurring Expenses dominate RevEx



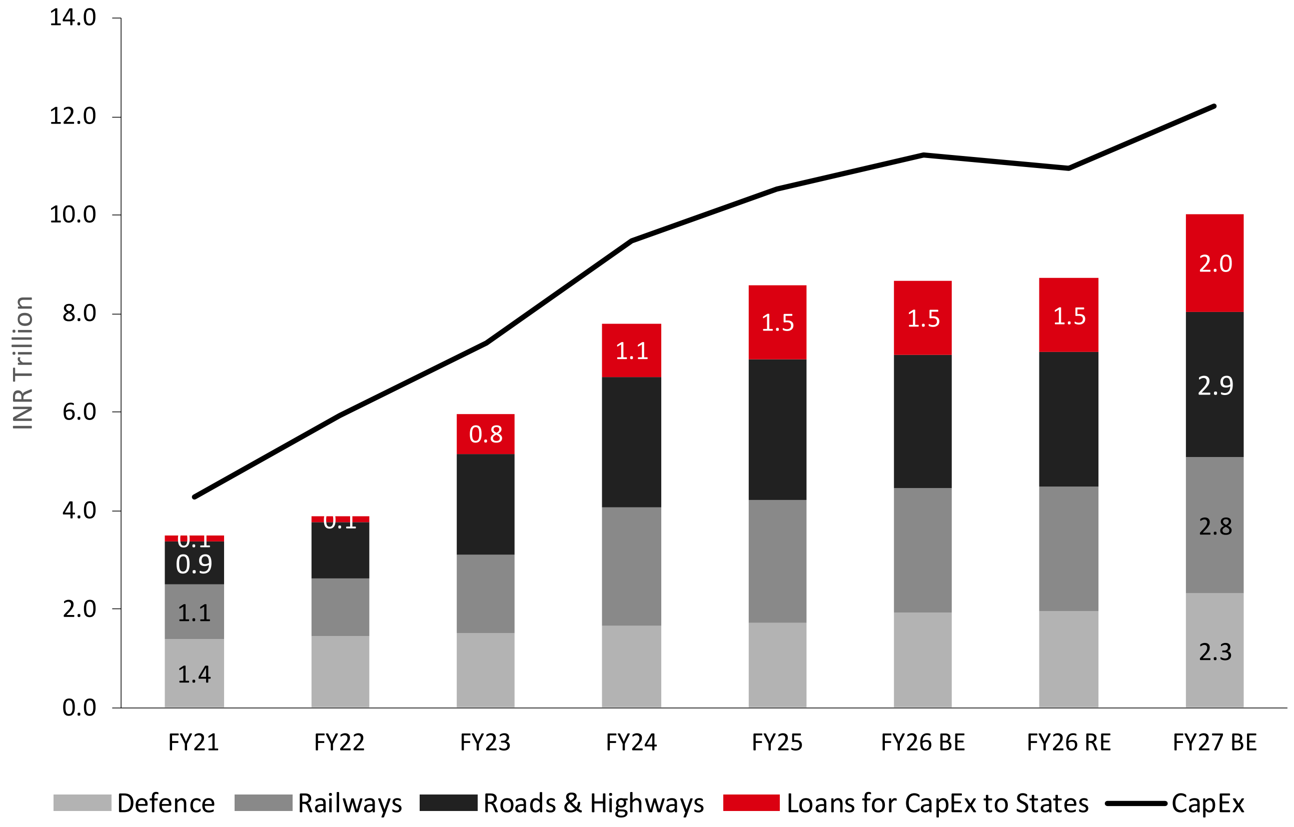



- We have taken the figures as % of GDP across key Revenue spending categories for the last five years
- RevEx to GDP moderates to 10.5% for FY27 from 13.6% five years ago
- While at the headline level, the RevEx consolidation is commendable…
- …at the category level, recurring expenses remain sticky with interest payments and subsidies making up for ~45% of Total RevEx
- Recurring expenses leave less wiggle room to accommodate other developmental expenses that are not necessarily CapEx

**Interest Payments & Subsidy continue to take up ~45% of RevEx**

Source: India Union Budget Documents, CMIE, RBI Database, Bloomberg, HSBC AMC, FI, Economic Research Desk

# Consistency in Capital spending



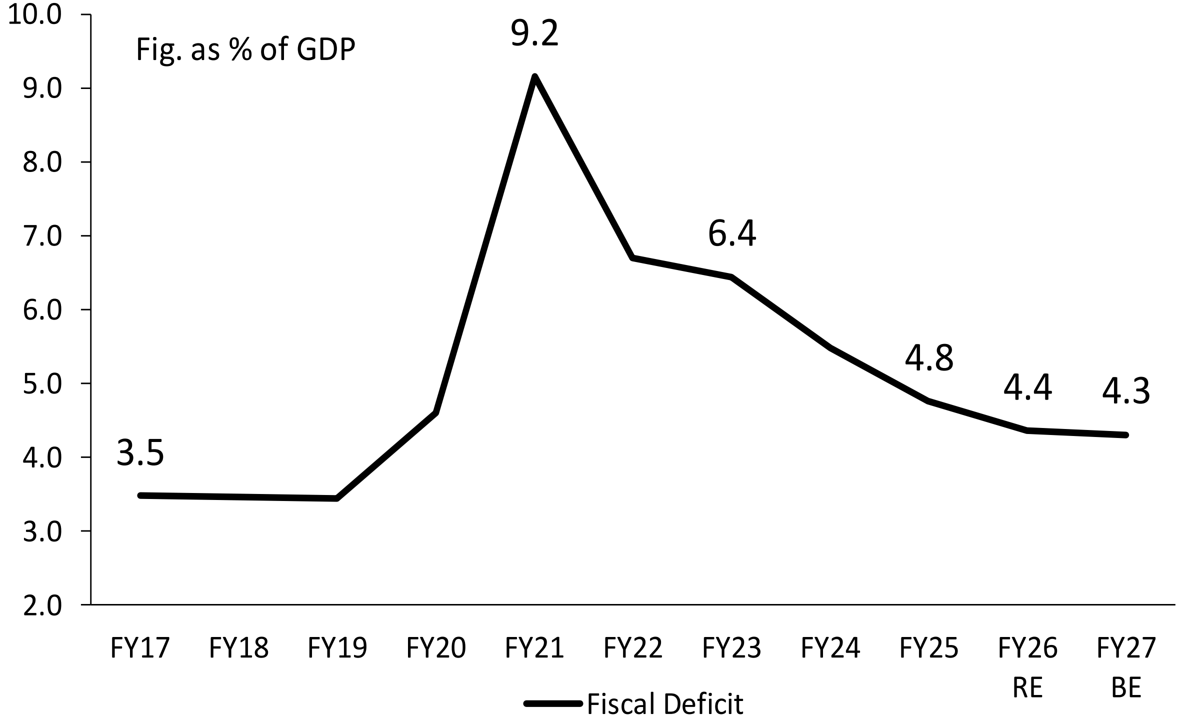

- CapEx is projected to rise 11.5% YoY, outpacing the Nominal GDP growth forecast of 10% for FY27
- For FY26, the CapEx spend was lower at 4.2% YoY vs the budgeted level of 6.6% YoY. But, it is still tracking 3.1% of GDP
- For FY27, too the CapEx target remains in consistency with that of 3.1% of GDP – the Top-5 ministry/department allocation too remain pretty much the same (chart alongside)
- Higher budgetary outlays are to Defence and Loans to States.
- If we were to look at 'Effective CapEx' which also includes Grant-in aid for asset creation, the fiscal thrust is higher at INR 17 tn

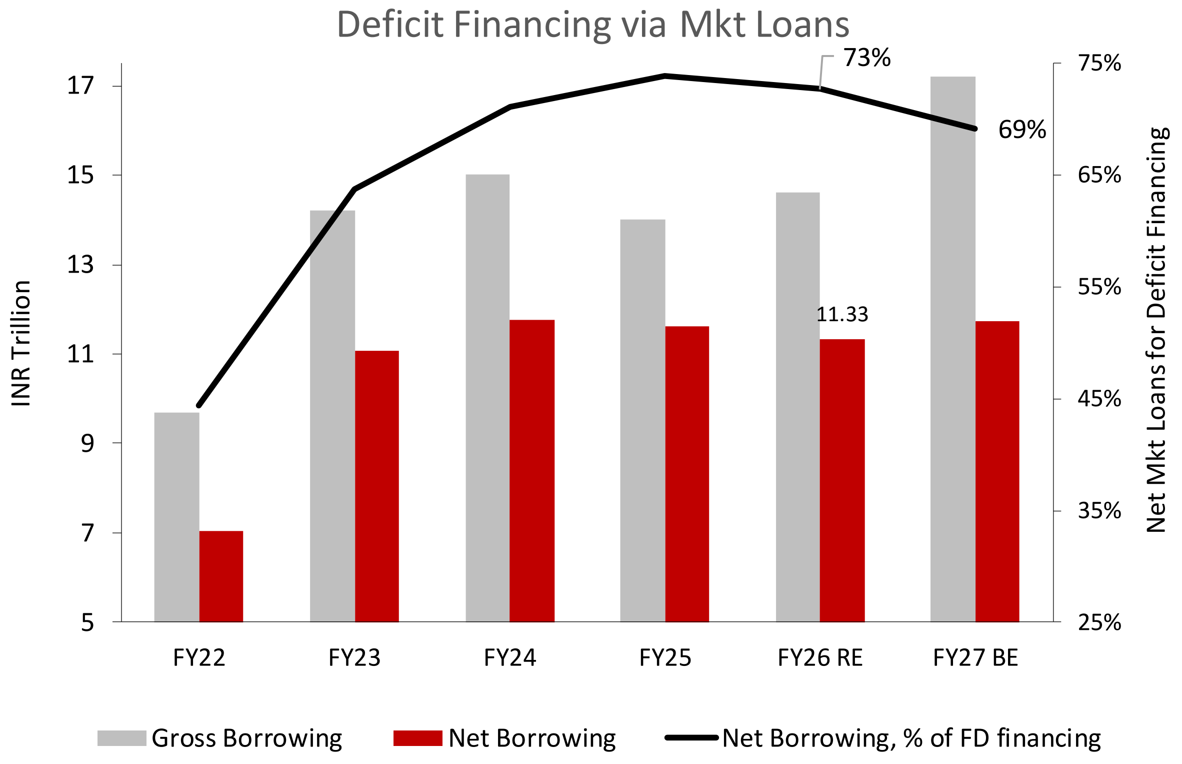
**Despite weaker tax buoyancy, CapEx thrust sustains**

Source: India Union Budget Documents, CMIE, RBI Database, Bloomberg, HSBC AMC, FI, Economic Research Desk

# Deficit a shade lower, but its financing (via markets) edges higher






Note: Net Market Loans is unadjusted for switches/buybacks

**Optically flat? – Deficit funding via Gsecs at 69%, but incl. short-term borrowings at 77%, highest since FY18**

Source: India Union Budget Documents, CMIE, RBI Database, Bloomberg, HSBC AMC, FI, Economic Research Desk Any views expressed were held at the time of preparation is based on the information available in the public and are subject to change without notice. While any forecast, projection or target where provided is indicative only and not guaranteed in any way. HSBC Asset Management India Pvt. Ltd. accepts no liability for any failure to meet such forecast, projection or target. Past performance may or may not be sustained in future and is not a guarantee of any future returns.

# The Supply Overhang



## A modest fiscal consolidation unlikely to add cheer to bonds market

- **Budgeted Fiscal Deficit in-line with market expectations**
  - Fiscal Deficit target for FY27 in absolute numbers is higher at ~INR 17 tn
  - As % of GDP it is a shade lower at 4.3% vs 4.4% in FY26 RE
  - Weak tax collections have increased the burden of financing as the govt. retains CapEx thrust

- **Borrowing numbers belying street expectations**
  - Govt. has budgeted for Switches of INR 2.5 tn; However, there is no budgeted level for Buybacks
  - The Revenue Secretary at a presser indicated that the Buybacks could be come through at a later stage, the markets might react to the current figures
  - The redemption figure is at INR 5.5 tn and the Gross Borrowing figure is at INR 17.2 tn
  - Net market borrowing translates to INR 11.7 tn via market loans; however, the govt. would also tap markets for short-term borrowing, raising INR 1.3 tn
  - Together, market borrowing is budgeted to finance ~77% of the fiscal deficit , highest observed since FY18
  - Small savings will continue to finance ~23% of the deficit, Higher disbursements under 'Other Receipts', the sources have dried-up, adding to supply overhang

**Fiscal numbers look conservative & achievable; Net borrowing numbers higher**

Source: India Union Budget Documents, CMIE, RBI Database, Bloomberg, HSBC AMC, FI, Economic Research Desk

# Deficit Financing: Tapping the markets (Gsecs & short-term) to fund the deficit



| | Financing via (INR bn) | | | | | Pre-Covid |
|---|---|---|---|---|---|---|
| ***INR bn*** | ***FY27 Est.*** | ***FY26 RE*** | ***FY26 BE*** | ***FY25*** | ***FY24*** | **FY19** |
| Gross Market Borrowings | 17,200 | 14,610 | 14,820 | 14,007 | 15,430 | 5,710 |
| *- Redemptions** | 5,468 | 3,282 | 3,282 | 2,378 | 3,625 | 1,483 |
| ***- Net Market Loans (G-Sec)*** | ***11,732*** | ***11,328*** | ***11,538*** | ***11,629*** | ***11,778*** | ***4,227*** |
| *Short term borrowings (T-Bills)* | 1,300 | - | - | (1,602) | 532 | **69** |
| External Assistance (Net) | 154 | 205 | 235 | 473 | 551 | -49 |
| Securities issued against Small Savings | **3,868** | **3,722** | **3,434** | **4,295** | **4,514** | **1,250** |
| State Provident Fund (Net) | 35 | 38 | 50 | 40 | 51 | 161 |
| Other Receipts (Net) | (458) | 759 | 407 | 1,787 | (887) | 740 |
| Drawdown of Cash Balance | 327 | 457 | 25 | 6 | 8 | -13 |
| **Fiscal Deficit** | **16,958** | **15,585** | **15,689** | **15,744** | **16,546** | **7,040** |
| **FD/GDP** | **-4.3%** | **-4.4%** | **-4.4%** | **-4.8%** | **-5.5%** | **3.4%** |
| **Debt/GDP** | **55.6%** | **56.1%** | **56.1%** | **56.2%** | **57.6%** | **49.6%** |

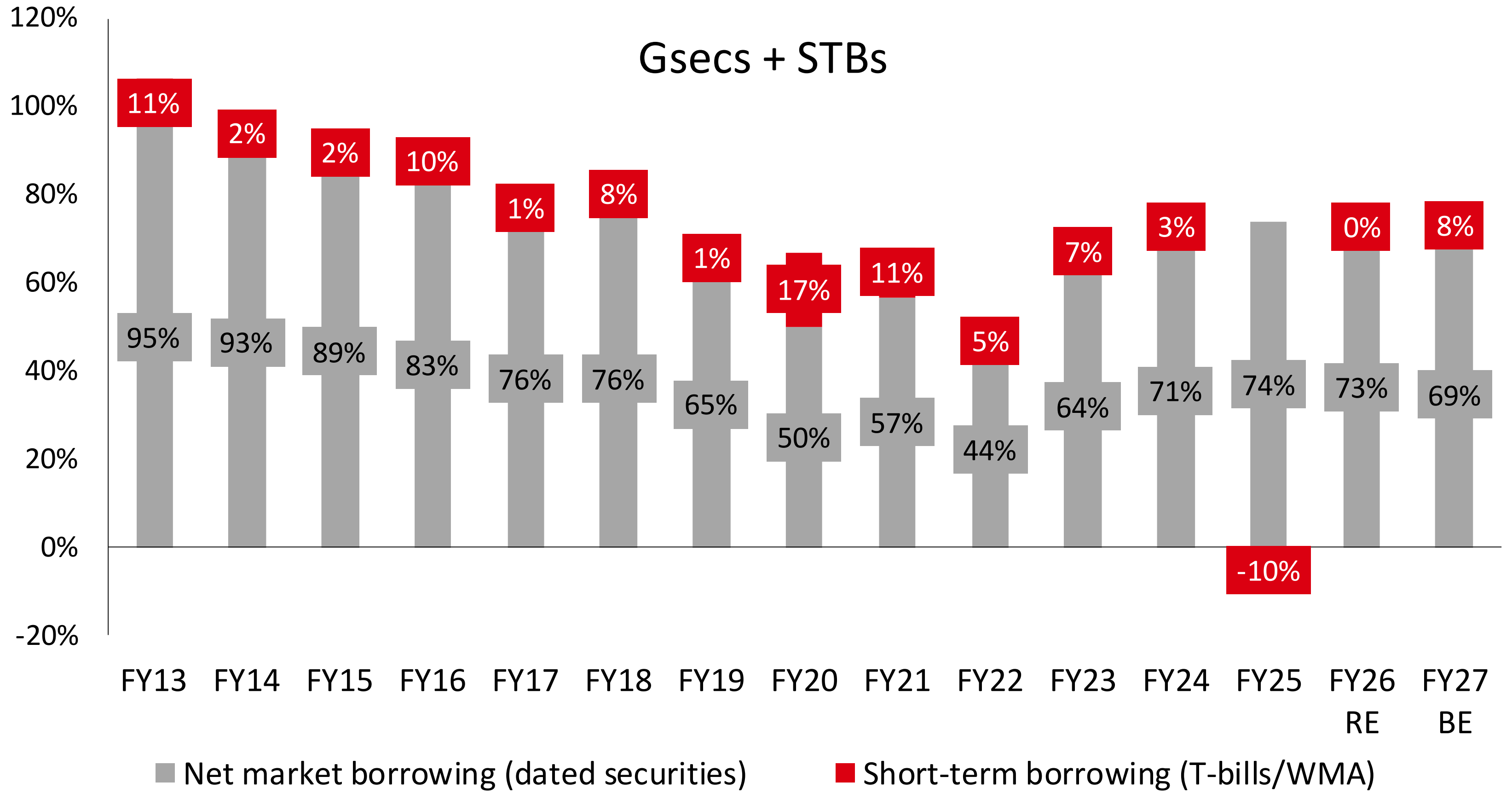
| | Net figures, INR bn | FY25 | FY26BE | FY26 RE | FY27 BE |
|---|---|---|---|---|---|
| 1 | Relief Bonds | 0 | 0 | 0 | 0 |
| 2 | Saving Bonds | 41 | 22 | 75 | 59 |
| 3 | Net-Sovereign Gold Bond Scheme | -81 | -55 | -71 | -43 |
| 4 | Net-Gold Monetization Scheme | 73 | 19 | -11 | -4 |
| 5 | Net-Other Receipts (Public Account Other than State Provident Funds) | 1,742 | 500 | 843 | -391 |
| 6 | Net-International Financial Institutions | 12 | -78 | -77 | -78 |
| Total (1+6) | Net-Other Receipts (Internal Debts and Public Account) | 1,787 | 407 | 759 | -458 |

**Consolidation on track, but reliance on markets increases; Net borrowing somewhat higher, T-bills to rise too**

Source: India Union Budget Documents, CMIE, RBI Database, Bloomberg, HSBC AMC, FI, Economic Research Desk

# Deficit Funding via Market loans and STBs






**Gsecs + STBs to finance ~77% of the fiscal deficit , highest observed since FY18**

Source: India Union Budget Documents, CMIE, RBI Database, Bloomberg, HSBC AMC, FI, Economic Research Desk

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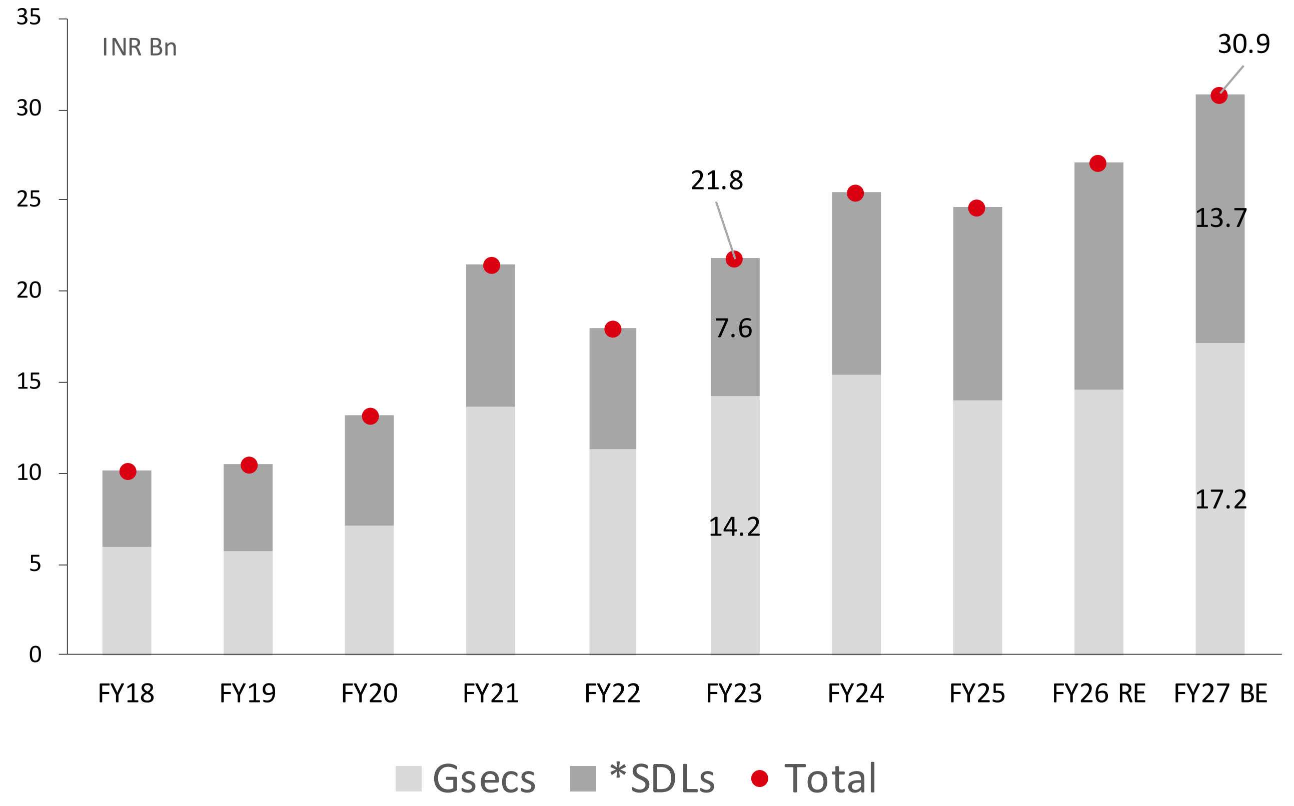
# Higher Gross supply likely to weighs on bond yields



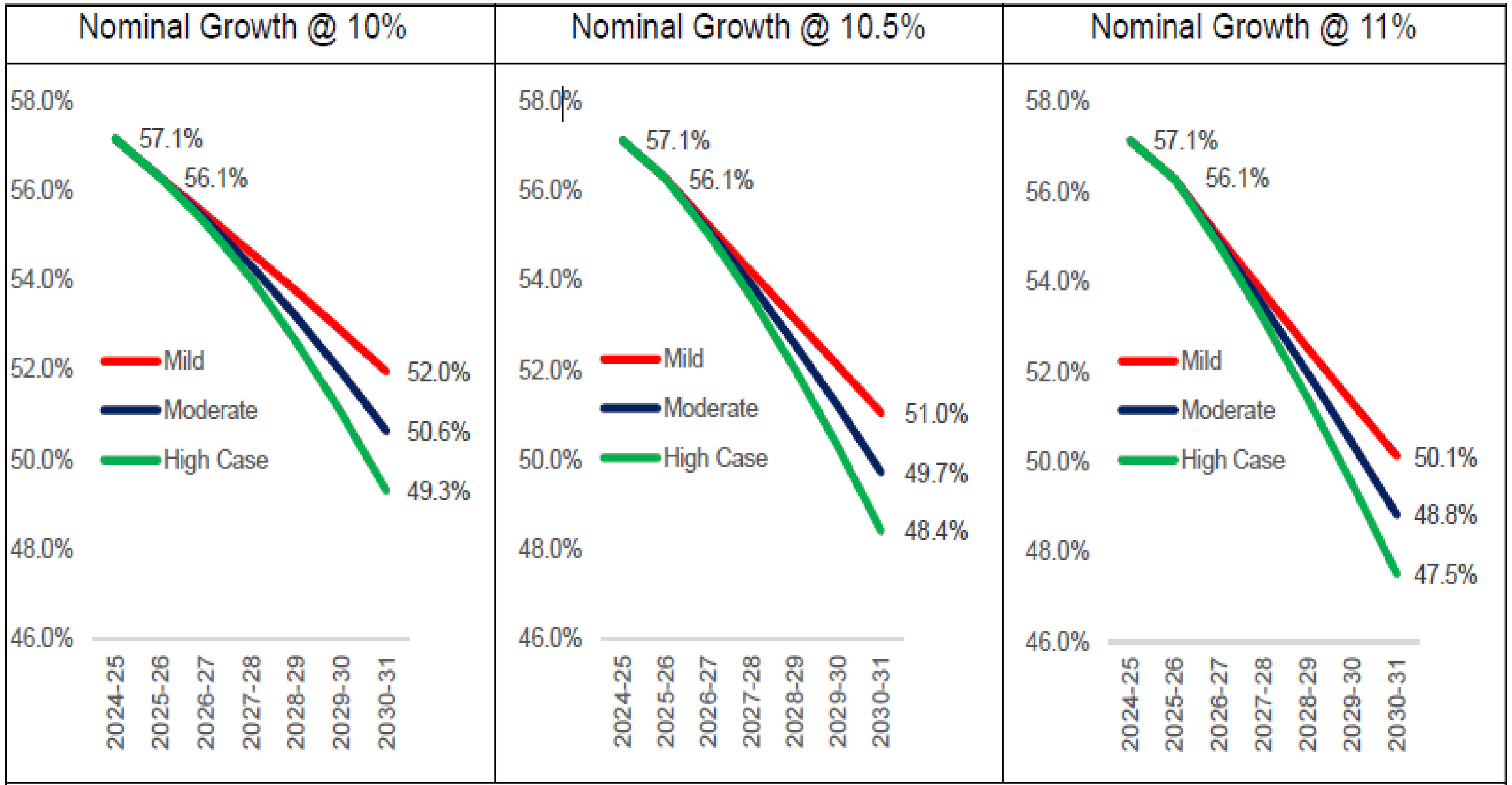



Note: *SDLs: assumed gross borrowing increases, 10% YoYFY27; Gross Gsecs is FY27 budgeted figures

**Supply of ~INR 30 lakh crore likely to weigh on yields, market sentiments**

Source: India Union Budget Documents, CMIE, RBI Database, Bloomberg, HSBC AMC, FI, Economic Research Desk

# Medium-term glide path under FRBM




Note: Mild/Moderate/High case refer to degrees of fiscal consolidaton.

**A shift in anchor to debt-to-GDP as stated in July 2024 Budget seen give the fiscal headroom spend and consolidate by FY2031**

Source: Indian Union Budget Document, Bloomberg, July 2024

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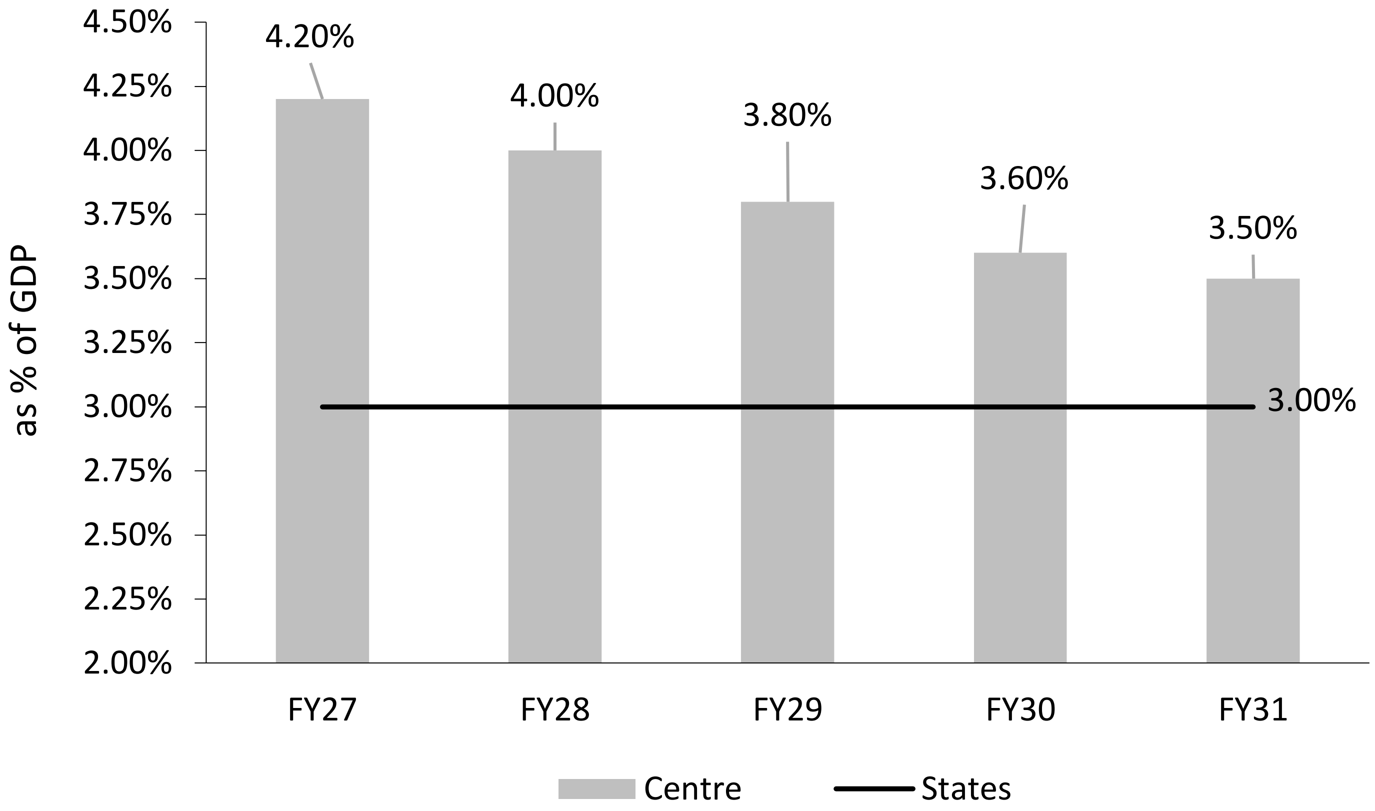
# Glide Path: The 16th Finance Commission Recommendation




**While fiscal deficit roadmap is laid out, a drop at the State level debt-to-GDP ratio is critical to lower General Govt. debt**

Source: India Union Budget Documents, CMIE, RBI Database, Bloomberg, HSBC AMC, FI, Economic Research Desk

# Conclusion: Focus on Fiscal prudence



| | |
|---|---|
| **Fiscal prudence** | • Budget focuses on fiscal prudence; fiscal deficit to GDP pegged at 4.3%, however, the new anchor of debt-to-GDP is budgeted to be brought down by 0.5% of GDP |
| **Capex thrust** | • CapEx thrust sustained despite the modest mobilization via revenue receipts; Govt. sets an aggressive disinvestment target for FY27 |
| **Deficit funding** | • Deficit funding relies heavily on market borrowing (dated and short-term borrowing); weighing on bond yields and dampening market sentiment coupled with the fears around increased States supply |
| **Supply-demand** | • The drying up of debt foreign flows and concerns around incremental demand from RBI by way of OMOs further adds to the supply-demand imbalance |
| **Strategy** | • In this backdrop, we reiterate our view of staying nimble footed with an accrual-based strategy and taking tactical duration calls |

Source: India Union Budget Documents, CMIE, RBI Database, Bloomberg, HSBC AMC, FI, Economic Research Desk

# Disclaimer



Source: Indian Union Budget Document, Data as on 1 February 2026

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