Budget 2022-23: A Capex Bonanza

The 2022-23 Budget has somewhat successfully managed to balance fiscal retreat and support for economic recovery. The budget deserves a somewhat favourable verdict. It has a gameplan premised on credible numbers. The fiscal deficit target of 6.4 per cent, prima facie, suggests that the FM has grabbed some much-needed fiscal space to nurture the nascent recovery and not been tempted to "over-consolidate".

- **Pump-Prime Keynesian style:** The underlying macro-economic strategy behind this budget is one of pump priming the economy through public investments, hoping that economic buoyancy would crowd-in private sector capex. The aim is to kick-start the investment cycle with multiplier effects on employment and income in turn addressing fragile consumption growth and uneven recovery. Thus, instead of redistributive direct fiscal support, an investment-led growth remains the government's economic management mantra. This is reflected in a 35 per cent increase in capital expenditure outlay (at INR 7.5 lakh cr) and a large increase in financial support to states for investment plans in the coming fiscal (INR 1 lakh cr).

- **Support for covid hit sectors:** There are also some direct measures to address the worst affected sectors by the pandemic. The extension of the credit guarantee scheme (ECLGS-- that gives a government back-stop to bank loans to the medium and small-scale sector) by a year and an increase in the guaranteed amount earmarked for the hospitality sector (INR 50,000 cr) is a welcome move.

- **Atmanirbhar Bharat amidst global supply chain disruptions:** The budget tilts further in the direction of self-reliance, offering tariff protection to capital goods that feed a range of sectors from coal mining to power to footwear, textiles, and food processing. This is accompanied by commitments of higher government procurement from local producers in areas like defence. This is important as inter-regional trade has been shrinking (apart from trade with China) since the Great Financial Crisis. Differences in the incidence of Covid and in containment strategies has further exposed the fragility of globalized supply chains. Increased localization (or self-reliance) might just emerge as a new paradigm for production. In this scenario, the case of unharnessed free trade and its presumed benefits perhaps need to be re-examined.

- **Digital currency on its way:** The introduction of a Central Bank Digital Currency, an electronic fiat currency (not to be confused with the box-standard "Crypto") was widely anticipated. However, it could have a significant impact on banks – on their deposit base for instance – and needs careful attention both from bankers and policy makers.

- **Credibility of fiscal math:** The budget is surprisingly conservative on the GDP growth assumptions, factoring in 11.1 per cent nominal (at current market prices) growth for 2022-2023 compared to 17.2 per cent in 2021-22. The disinvestment target too is subdued at Rs 65000 and hence more credible that previous budgets that saw large shortfalls. The big punt is on increasing tax buoyancy with the tax-to-GDP ratio estimated at 10.7 per cent instead of 9.9 per cent previously in FY22 BE. This increase is primarily due to an assumed increase in GST collections that is projected to yield INR 1.3 lakh crores a month compared to an average of INR 1.13 lakh cr assumed for the current year. This might well be achieved. There are reports that the technical glitches in the GST backbone have been fixed leading to better compliance and coupled with a sustained momentum in the economy should do the trick.

- **Concerns – Will the capex punt work?** There are some concerns around the current capex led strategy. For one thing, absorption of funds allocated to projects has been a long-standing problem in India. The big question then is --does the government have enough shovel-ready projects to absorb the allocated funds to make a difference in the near term? Also, by focussing primarily on capex the budget has perhaps overlooked some key revenue expenditures. For instance, the allocation to MNREGA been reduced by a good Rs 25000 crores when demand for these jobs still exceeds supply and indeed there were suggestions of an urban employment guarantee.

Financing of the deficit and Bond View

For the bond market, a significantly higher than expected borrowing of INR 14.95 lakh crore in FY23 is likely to put further pressure on yields at a time when both global and domestic interest rate cycles are at the cusp of turning this year. The absence of any announcement around a tax relief for foreign bond investors was a disappointment and led to further pressure on yields. The 10-year yield rose by 14bps post the budget announcement to 6.83%.

- **Bond View:** For the coming fiscal year, we expect the 10-year bond yield to rise to 6.9-7% by H1 FY23 with a breach of the 7% level now likely. Although, we expect the RBI to continue with operation twists and signals through auctions to try and keep a cap on yields, with liquidity tightening the room for plain vanilla OMOs is likely to reduce. We expect policy normalisation and interest rate hike expectations to get priced in well before hand and we could see some moderation in yields in the second half of the year, despite the RBI delivering rate hikes by that time (expect 25bps hike in August 22 and 25bps in Dec 22). This relief we think is also likely to be driven by lower inflation prints in H2 (expect average of 4.5-5%), some cool-off in commodity prices as supply capacities catch up with demand, and the announcement of an inclusion in the global bond index. We see the 10-year between 6.7-6.8% by H2 FY23.

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- **Market Borrowing:** The government revised down its gross market borrowings to INR 10.5 lakh cr in FY22 from 12.06 lakh cr budgeted. The government borrowed an additional INR 1.59 lakh cr for the GST compensation shortfall transferred to states in FY22. For the next fiscal, the government plans to borrow INR 14.95 lakh cr in gross borrowings and INR 11.2 lakh cr in net borrowings. These calculations exclude the recent switch by RBI of INR 64,000 cr done for securities maturing in FY23 and is likely to be lowered by the same amount.

- **Financing Mix:** As a % of total financing, gross market borrowings are 90% of the fiscal deficit compared to 66% in FY22 and 69% in FY21. In other sources of financing, dependence on small savings funds continues in FY23 (26% of FD, INR 4.25 trn) and that on other receipts and cash balances is expected to rise. It is noted that for FY22, the government's draw down on cash balances rose to INR 1.74 lakh cr (compared to BE of INR 70,000) as was expected due to the rise in surplus cash balances with the RBI over the last few months.

Financing of the Fiscal Deficit

(in INR, Tn)	FY20	FY21	FY22 RE	FY23BE
Fiscal Deficit	**7.7**	**18.5**	**15.9**	**16.6**
Gross Market Borrowing	**7.1**	**12.8**	**10.5**	**15.0**
- Repayments	2.4	2.3	2.7	3.8
Net Borrowings	**4.7**	**10.5**	**7.8**	**11.2**
ST Borrowings	0.3	2.3	1.0	0.5
-Switches	1.7	1.6	1.2	1.0
Other				
External Debt Net	0.05	0.55	0.02	0.02
NSSF	2.40	4.80	5.92	4.25
State PF	0.18	0.18	0.20	0.20
Other Receipts	0.05	0.40	-0.09	0.37
Draw down CB		-0.20	1.74	0.07

Source: Budget Documents, HDFC Bank

Fiscal Math FY23

	INR lakh crore			%YoY	
	FY21A	FY22 RE	FY23 BE	FY22	FY23 BE over FY22 RE
Revenue Receipts	16.3	20.8	22.0	27.4	6.0
Net Tax revenue	14.2	17.7	19.3	23.9	9.6
Gross Tax revenue	20.2	25.2	27.6	24.3	9.6
Direct Tax	9.4	12.5	14.2	32.4	13.6
Income Tax	4.9	6.2	7.0	26.3	13.8
Corporate Tax	4.6	6.4	7.2	38.9	13.4
Indirect Tax ex GST	5.2	5.8	5.5	11.2	-6.0
Customs	1.3	1.9	2.1	40.3	12.7
Excise	3.9	3.9	3.4	1.1	-15.0
GST	5.5	6.8	7.8	22.7	15.6
Non tax revenue	2.1	3.1	2.7	50.4	-14.1
Non Debt Capital Receipts	0.6	1.0	0.8	73.5	-20.7
Divestment	0.3	0.8	0.7	137.2	-16.7
Total Receipts	16.9	21.8	22.8	29.0	4.8
Total Expenditure	35.1	37.7	39.5	7.4	4.8
Revenue	30.8	31.7	31.9	2.7	0.9
Subsidy	7.6	4.9	3.6	-35.6	-27.0
Capex	4.3	6.0	7.5	41.4	24.5
Fiscal Deficit	18.2	15.9	16.6	-	-
% of GDP	**9.2%**	**6.9%**	**6.4%**	-	-
Nominal GDP (INR trn)	198	232	258	17.2	11.1
Gross tax/GDP	10.2	10.8	10.7	-	-

Source: Budget Documents, HDFC bank

The Revenue Side: GST collection to support revenue receipts

The budget has set the revenue receipts target at INR 22 lakh crore for FY23, an increase of 6% from FY22 RE. We reckon that the revenue targets set for FY23 seem achievable given a pickup in economic recovery. Gross Tax-to-GDP ratio has been kept broadly unchanged at 10.7% in FY23 from 10.8% in FY22 RE (and as compared to 9.9% of FY22BE). The support from the revenue side is likely to come largely from robust GST collections, which are budgeted to rise to INR 7.8 lakh crore in FY23 (implying a monthly run rate of INR 1.3 lakh cr vs. INR 1.13 lakh cr in FY22 RE).

- **Direct tax collections – realistic target:** Direct tax collections growth is budgeted to increase by 13.6% in FY23 led by both income tax and corporate tax collections. Income tax and corporate tax buoyancy budgeted at 1.24 and 1.2, respectively for FY23 seems achievable.

- **Indirect tax (excluding GST):** Collections are budgeted at INR 5.5 lakh crore in FY23, lower than INR 5.9 lakh crore in FY22. Looking at the internals, proceeds from custom duties are likely to increase while those from excise duties are estimated to decline in FY23 compared to the FY22 RE figures, reflecting a cut in excise duties on petrol and diesel.
    - **Custom Duties:** Custom duties budgeted at INR 2.1 lakh crore, 12.1% higher as compared to FY22 RE. Government has slashed custom duties on a host of products including cut and polished diamonds and gemstones, chemicals. On the other hand, duty is being raised on other chemicals such as sodium cyanide, etc.
    - **Excise Duties:** Additional differential excise duty of INR 2/ltr will be levied on unblended fuel from 1st October 2022. The target of INR 3.35 lakh cr for FY23 seems achievable although does not leave space to reduce duties on petrol and diesel any further in FY23.

- **An achievable GST collection target: GST collection** target is set at INR 7.8 lakh crore in FY23. Our calculations show that a monthly run rate of INR 1.3 lakh crore/month is required to meet the target vs. the current run rate (average) of INR 1.2 lakh crore (Apr 2021-Jan 2022). Given recovery in growth and improvement in economic activity GST target seems achievable. GST collections have been hovering ~INR 1.3 lakh crore mark since Oct-21, hitting an all-time high of INR ~1.40 trn in Jan 2022, indicating a steady pace of economic recovery post the pandemic.

- **Disinvestment – a modest target**: Disinvestment target is set at INR 65,000 crore for FY23. For FY22, the government drastically reduced the target to INR 78,000 crore from the budgeted INR 1.75 lakh crore. In FY22, due to the second and third wave of covid, big ticket privatisation proposals such as BPCL, Shipping Corporation of India are not likely to be completed due to procedural delays. The intent is to complete these plans in FY23. It seems likely that the government has accounted for the LIC IPO proceeds in FY22 numbers.

So far (Apr-Dec 2021), the Government has garnered INR 12,030 crore (as per DIPAM)

Disinvestment in FY22 (until Dec 2021)	Amount (INR cr)
NMDC	3654
Others (SUTTI Axis Bank)	3994.33
HUDCO	720.45
HCL	742
IPCL	219.34
Air india	2700
Total	**12030.12**

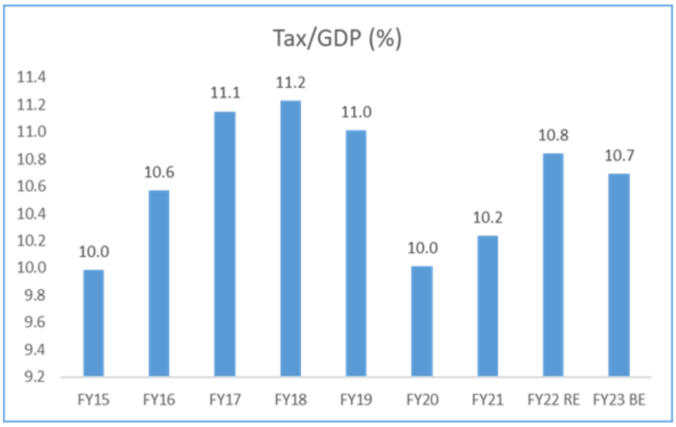
Source: DIPAM, HDFC Bank

Budget direct tax collections for FY23

INR lakh crore	FY22RE	FY23BE
Corporate Tax	6.4	7.2
(%YoY)	*38.9*	*13.4*
Income Tax	6.2	7
(%YoY)	*26.3*	*13.8*

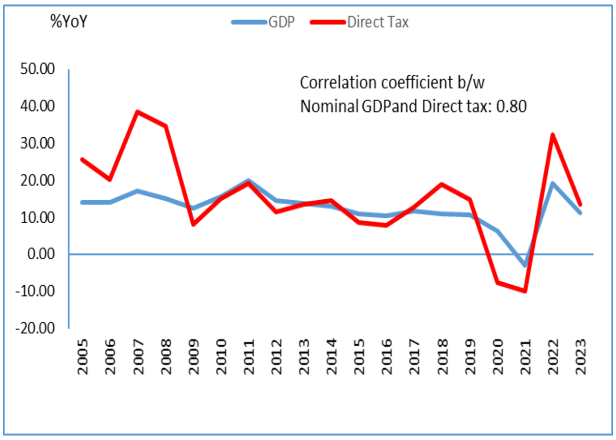
Source: Budget Documents, HDFC Bank

Tax to GDP ratio at 10.7% in FY23



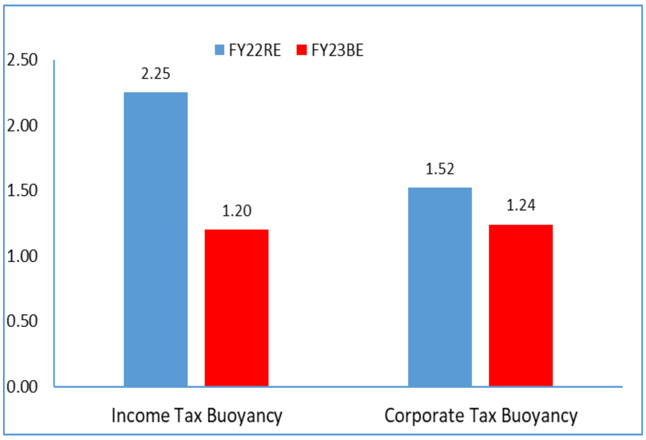
Source: Budget Documents, HDFC Bank

Direct tax collection growth is budgeted to increase by 13.6% in FY23. The target seems achievable given an upbeat nominal growth



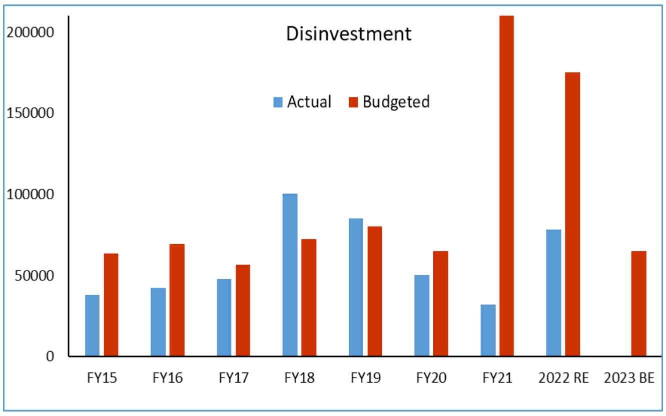
Source: Budget Documents, HDFC Bank

Tax Buoyancy estimates seem achievable



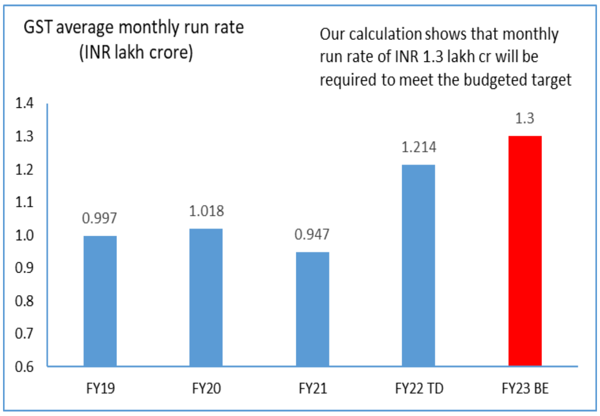
Source: Budget Documents, HDFC Bank

A modest disinvestment target for FY23



Source: Budget documents, HDFC Bank

Government pinning hopes on robust GST collection



Source: Budget documents, PIB, HDFC Bank

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Custom duty changes: Sectors	Announcement
Steel	• *Custom duty exemption for steel scraps given last year is being extended for another year to provide relief to MSME secondary steel producer.* • *Certain anti-dumping duty of stainless and coated steel products, bars of alloy steel and high speed steel are being revoked*
Chemicals	• *Duty on certain chemicals (such as methanol acetic acid) reduced while duty on other chemicals sodium cyanide*
Gems and Jewellery	• *Custom duty reduced on cut and polished diamonds and gemstones (to 5%)* • *Duty on sawn diamond cut to 0%*
Electronics	• *Duty concessions given to parts of transformer of mobile phone chargers and camera lens of mobile camera module*
Exports (textiles, furniture, handicrafts, leather garments)	• *Exemptions provided on items such as fasteners, buttons, zipper, lining materials, specified leather, furniture fittings and packaging boxes*

Source: Budget Document, HDFC Bank

Sector specific measures

MSME

- ECGLS scheme extended till March 2023 and its guarantee cover extended by INR 50,000 crore to total cover of INR 5 lakh crore.
- Raising and Accelerating MSME Performance program with outlay of INR 6000 crore over 5 years will be rolled out

Affordable Hosuing

- 80 lakh households will be completed under the affordable housing scheme (both rural and urban).
- INR 48,000 crore allocated for the same

Agriculture

- Funds to be facilitated through NABARD to finance starttups in agriculture and rural enterprises for farm produce value chain will be set up
- Scheme to increase domestic production of oilseeds
- Kisan drones to promote crop assessment, digitalization of land records, spraying of insectides

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The Expenditure Story: Capex, Capex, Capex!

FY23: *Total expenditure for FY23 stood at INR 39.5 lakh cr, almost INR 2 lakh cr higher than FY22 RE. Majority of this increase comes from higher capital expenditure. FY23 capital spending is pegged at a historic high of INR 7.5 lakh Cr, a 24.5% increase over FY22 RE and a 35% increase over FY22BE numbers. To put things in perspective, capital spending target for FY23 is more than double as compared to pre-pandemic levels (FY20). While the government managed to over-deliver on its FY22 capex target (at INR 6 lakh cr vs. BE of INR 5.5 lakh cr) due to the inclusion of equity infusion into Air India, allocating such a large capex program in FY23 remains challenging and requires effective implementation. Segment wise, roads, railways, defence, and telecom saw the highest allocation in terms of capex. On the revenue expenditure side, the target remained broadly unchanged at INR 32 lakh cr (compared to INR 31.7 lakh cr in FY22 RE).*

FY22 RE: *In line with expectations, the Government has revised up its FY22 total spending to INR 37.7 Lakh Cr (vs. 34.8 lakh Cr-BE). Most of this increase was on account of an extension of the free food program and fertiliser subsidy payments.*

Digging in FY23 spending:

- **No change in revenue expenditure:** Revenue expenditure at INR 32.0 lakh Cr is almost flat when compared to FY22-RE. On the similar lines, revenue expenditure ex interest payments ex subsidy is budgeted to increase by a mere 1.8% (vs. FY22-RE).
    - Among major revenue expenditure items, interest payments are expected to rise by 15.6% (vs. FY22-RE) to INR 9.4 lakh Cr. This reflects an increase in cost of borrowings. Taking cues from Government's liabilities and interest payments, our back of envelope calculation suggests implicit yield at 6.5% for FY23.
    - **Lower subsidy bill:** However, the Government plans to bring down its subsidy bill to INR 3.6 lakh Cr from INR 4.9 lakh Cr in FY22 (RE). As a % of GDP, subsidy bill is budgeted at 1.4% of GDP vs. 2.1% of GDP in FY22 (RE).

- **Revenue to Capex ratio improves:** On the flip side, capex is budgeted to increase to a record high of INR 7.5 lakh Cr, which is a 24.5% increase over FY22-RE. The improvement in quality of spending is reaffirmed by revenue expenditure to capex ratio which is estimated at 4.3 in FY23 vs. 5.3 in FY22-RE.

- **Major schemes:** Among major schemes, PM Sadak Yojana, National Livelihood Mission, National Education Mission, Rural Drinking water mission got higher allocation (vs. FY22 RE). Discouragingly, allocation to MGNREGA is reduced to INR 73,000 Cr from INR 98,000 Cr (FY22-RE).

- In our view, budgeted expenditure estimates (specifically for capex) look credible and can be achieved. However, implementation will be the key.

What lies in Revised estimates for FY22?

- Out of INR 2.9 lakh Cr extra spending in FY22, INR 2.4 lakh Cr is attributed to revenue expenditure.

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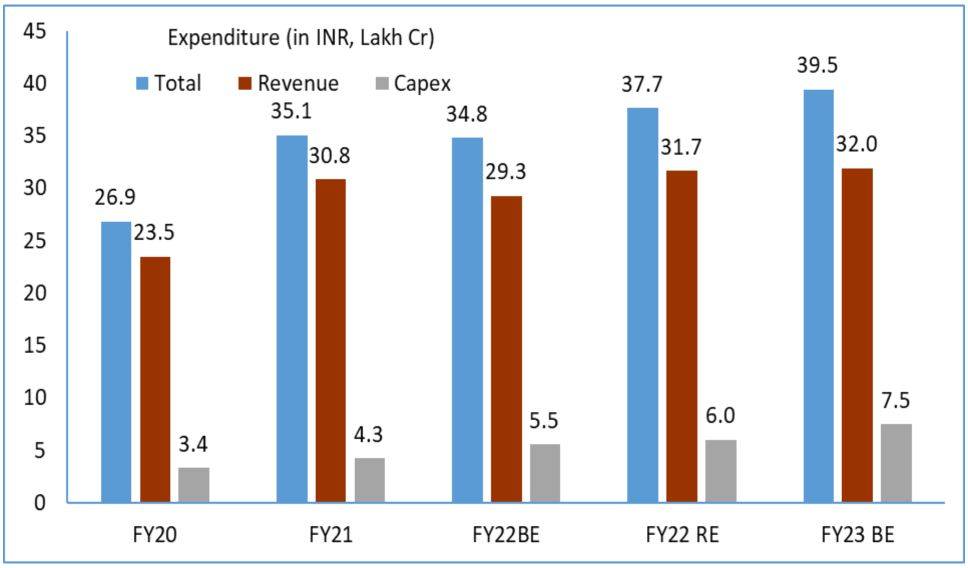
- Subsidy bill accounts for ~50% of increase in revenue expenditure: Food subsidy at INR 2.86 lakh Cr (vs. 2.4 lakh Cr- BE), fertiliser subsidy is being revised to INR 1.4 lakh Cr from INR 0.8 lakh Cr earlier.

- FY22 revised capex includes equity infusion and loans to Air India worth INR 51,971 Cr. Excluding these items capex stands at INR 5.51 lakh Cr.

- Ministry wise, (FY22) allocation to transport, housing & urban development and rural development are also revised up. Encouragingly, spending on Rural Job Guarantee Scheme (MGNREGA) is also increased to INR 98,000 Cr from INR 73,000 Cr BE.

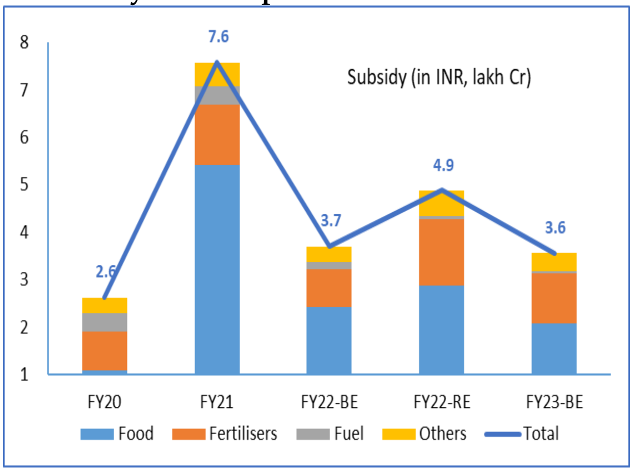
More than two-fold in capex as compared to pre-pandemic levels



Roads, railways and telecom capex in focus

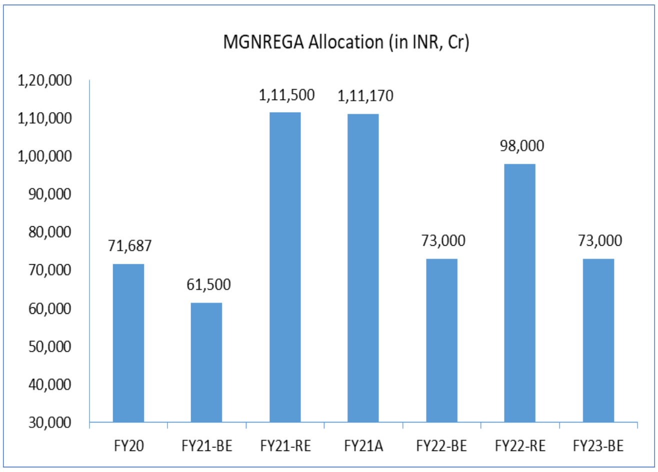
Capex Spending	FY22-BE	FY22-RE	FY23-BE	FY21	FY22-RE	FY23 BE (vs. FY22 RE)
	(in INR, lakh Cr)			YoY,%		
Housing	0.26	0.26	0.27	-46.6%	151.9%	5.3%
Telecom	0.26	0.05	0.54	-11.6%	25.6%	889.9%
Railways	1.07	1.17	1.37	61.1%	7.1%	17.1%
Roads	1.08	1.21	1.88	30.5%	35.9%	54.8%
Defence	1.35	1.39	1.52	20.9%	3.4%	9.7%
Others	1.52	1.94	1.92	22.8%	146.2%	-1.3%
Total	5.54	6.03	7.50	27.0%	41.4%	24.5%

Subsidy bill is expected to decrease in FY23



Source: Budget Documents, HDFC Bank

MGNREGA allocation reduced for FY23



Source: Budget Documents, HDFC Bank

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