Fiscal Policy Stance is Clearer: On to the Monetary Policy*

By Dr M Govinda Rao, Chief Economic Adviser, Brickwork Ratings

There were considerable apprehensions about how the Finance Minister would balance the fiscal consolidation objective with the objective of reviving growth by increasing infrastructure spending. The budget proposes to compress the fiscal deficit by half a percentage point to GDP to 5.9% while increasing the capital expenditure from 2.7% of GDP to 3.3%. In nominal terms, this is 37% higher than the revised estimate of the previous year and comes on the back of 23% higher outlay than the revised estimate of the previous year and 39% increase in the year before. In many ways, it is an ambitious budget and is crafted at a time when the global economic environment is challenging and domestically the engines of growth except private consumption were stuttering.

Although the fiscal deficit projections show the reduction by 0.5%, the next two years are going to be challenging. Reducing the fiscal deficit to 4.5% by 2025-26 requires compression of deficit by 1.4 percentage points in the next two years. This is the last full year budget before elections and as there will be general elections next year, feasibility of large compression of fiscal deficit next year is questionable. Given that interest payments at the central level constitute 40% of the revenue receipts, further addition to the debt will only add to the problem and in some ways, it would have been better to front load fiscal adjustment.

The global economic environment poses serious uncertainties. The IMF, in its latest revision, has estimated global GDP growth at 2.9% as against 3.2% in the previous year and 6.1%, the year before. More than a third of the economies are facing recessionary conditions. The excess liquidity released during the pandemic and the sharp increase in food and energy prices due to the Russia-Ukraine war and the sanctions have not only resulted in both inflationary conditions but also supply chain disruptions causing significant economic slowdowns in most parts of the world. Besides, there has been a secular decline in saving and investment rates in India and most projections show the economy decelerating from 7% growth this year to 6- 6.5% in the next with an upward bias. The slowing world economy does not leave much scope for reviving exports and the only way the growth can be maintained and accelerated is by increasing public investment. Considering the fact infrastructure spending has a crowding-in effect, the sharp increase in capital expenditure could help to revive private investment as well.

Of course, the actual increase in public investment will depend upon how well the budget is implemented. The increase in capital expenditures was done mainly by compressing revenue expenditures and the budgeted revenue expenditure in nominal terms is just 1.2% higher than the revised estimate of the previous year. While interest payment itself takes claims 40% of revenues,

there is very little scope for compressing revenue expenditures. Much of the compression has come from reducing food subsidies, the fertilizer subsidy, and reduced allocations to the MGNREGA. The food subsidy has been cut by Rs 90,000 crore and mainly due to the discontinuation of foodgrain distribution under PMGKAY. The fertilizer subsidy was reduced by Rs 50,000 crore due to lower prices. MGNREGA funds allocation has been reduced by Rs 29,000 crore (from Rs 89,400 crore in 2022-23 RE to Rs 60,000 crore in 2023-24 BE).

There are a number of other budget announcements which basically are intended to appeal to virtually every section of population. The seven focus areas stated in the budget are intended to appease across a wide section of people and most of them are in the State or concurrent list. The direct tax policy announcement is mainly aimed nudging the taxpayers to opt for the new tax regime. Of course, a tax policy without tax preferences is simple and desirable but providing options will add to the confusion.

After the budget, the focus was shifted to the monetary policy stance. In line with the market opinions, the monetary policy committee increased the repo rate marginally by 25 basis points. But the MPC continued with the accommodating stance. With the inflation rate crossing again the upper target of 6% in January 2023, and the core inflation continues to be sticky leaving little room for any easing in the near term. Besides, the better employment data in the US and the possibility of a further increase in the rate by the Fed could lead to the outflow of FII widening the current account and exchange rate depreciation putting pressure on prices. Therefore, the dilemma of supporting growth on the one hand and controlling inflation on the other will continue for some more time.

**** Views are personal.***

Contacts:

Investors & Media Contact
+91 95133 99706
1-860-425-2742
investordesk@brickworkratings.com
media@brickworkratings.com

ABOUT BRICKWORK RATINGS

Brickwork Ratings (BWR) is India's home-grown credit rating agency built with the superior analytical prowess of the industry's most experienced credit analysts, bankers and regulators. Established in 2007, BWR aims to provide reliable credit ratings by creating new standards for assessing risk and by offering accurate and transparent ratings. BWR provides investors and lenders timely and in-depth research across the structured finance, public finance, financial institutions, project finance and corporate sectors. BWR has employed over 350 working professionals including credit analysts and credit market professionals across 8 offices in India. Our experienced analysts have published over 12,000 ratings across asset classes. BWR is committed to providing the investment community with products and services needed to make informed investment decisions. BWR is a registered credit rating agency by Securities and Exchange Board of India (SEBI) and a recognised External Credit Assessment Agency (ECAI) by the Reserve Bank of India (RBI) to carry out credit ratings in India. BWR is promoted by Canara Bank, India's leading public sector bank. More information on Canara Bank is available for reference at www.canarabank.com

BWR Rating Criteria are available at https://www.brickworkratings.com/ratingscriteria.aspx

Brickwork Ratings, a SEBI-registered credit rating agency, has also been accredited by the RBI, and it offers rating services for bank loan, NCD, commercial paper, bonds, securitised paper etc. BWR has Canara Bank, a nationalised bank, as its promoter and strategic partner.
BWR has its corporate office in Bengaluru and a country-wide presence, with offices in Ahmedabad, Chandigarh, Chennai, Hyderabad, Kolkata, Mumbai and New Delhi, along with representatives in 150+ locations. BWR has rated debt instruments/bonds/bank loans, securitised paper of over ₹ 10,00,000 Cr. Additionally, fixed deposits and commercial papers, among others, worth over ₹24,440 Cr have been rated.

DISCLAIMER

Copyright © 2023 by Brickwork Ratings India Pvt Ltd., 3rd Floor, Raj Alkaa Park, 29/3 & 32/2, Bannerghatta Main Rd, Kalena Agrahara, Bengaluru, Karnataka 560076.Telephone: +91 80 4040 9940. Fax: +91 80 4040 9941. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. In issuing and maintaining its ratings, Brickwork Ratings relies on factual information it receives from issuers and underwriters and from other sources Brickwork Ratings believes to be credible. Brickwork Ratings conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Brickwork Ratings' factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Brickwork Ratings' ratings should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Brickwork Ratings relies on in connection with a rating will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Brickwork Ratings and to the market in offering documents and other reports. In issuing its ratings Brickwork Ratings must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings can be affected by future events or conditions that were not anticipated at the time a rating was issued or affirmed. THE INFORMATION IN THIS REPORT IS PROVIDED "AS IS" WITHOUT ANY REPRESENTATION OR WARRANTY OF ANY KIND. A Brickwork Ratings rating is an opinion as to the creditworthiness of a security. This opinion is based on established criteria and methodologies that Brickwork Ratings is continuously evaluating and updating. Therefore, ratings are the collective work product of Brickwork Ratings and no individual, or group of individuals, is solely responsible for a rating. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Brickwork Ratings is not engaged in the offer or sale of any security. All Brickwork Ratings reports have shared authorship. Individuals identified in a Brickwork Ratings report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Brickwork Ratings rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time, for any reason in the sole discretion of Brickwork Ratings. Brickwork Ratings does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Neither Brickwork Ratings nor its affiliates, third party providers, as well as their directors, officers, shareholders, employees or agents (collectively, "BWR Reps") guarantee the accuracy, completeness or adequacy of the Report, and no BWR Reps shall have any liability for any errors, omissions, or interruptions therein, regardless of the cause, or for the results obtained from the use of any part of this publication. In no event shall any BWR Reps be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs) in connection with any use of any part of the Report even if advised of the possibility of such damages. Brickwork Ratings receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities.