India's Union Budget 2018–19 Highlights

- **The Budget 2018 focuses on India's rural economy and infrastructure.**
- **The government's commitment to fiscal prudence has eased somewhat.**
- **The central government deficit will be narrowed to 3.3% of GDP in FY2018–19 from 3.5% in the ongoing fiscal year.**

India's Union Budget for Fiscal Year 2018–19 (April-March) was presented by Finance Minister Arun Jaitley today. The budget is a careful balancing act between stimulating domestic demand, particularly the rural economy, and maintaining investor confidence on India's fiscal sustainability. We assess that the government gave priority to the former, which may reflect the fact that this is the last full budget of Prime Minister Narendra Modi's government before the general elections in 2019. Even though the government remains committed to gradual fiscal consolidation, the central government deficit targets were relaxed somewhat. Given that a similar step was taken last year, India's pledge to reach fiscal sustainability is questionable.

According to Finance Minister Jaitley, public outlays in FY2018–19 will be directed at:

- strengthening the agricultural and rural economy;
- developing the country's infrastructure; and
- improving education, health and social protection.

Beyond various social development measures related to the aforementioned areas, other key highlights include:

- The corporate tax rate for medium-sized enterprises was cut to 25% from 30%; previously only small firms had benefitted from a lower rate.
- A 10% long-term capital gains tax on listed equities was introduced.
- Personal income tax brackets were left unchanged, yet some deductions and exemptions were introduced.

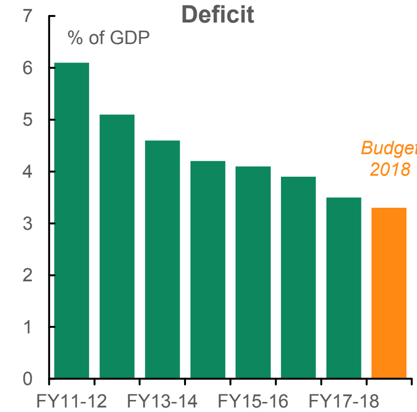
The budget's supporting documents that lay out detailed expenditure and revenue estimates are not yet publically available at the time of writing; nevertheless, Finance Minster Jaitley indicated that India's central government deficit will average 3.5% of GDP this fiscal year, thereby missing the Budget 2017 target of 3.2%. The shortfall in FY2018–19 is projected to narrow to 3.3% of GDP. Nevertheless, it is worth highlighting that India's public deficit remains substantially larger at the general government level, likely averaging 6¼% of GDP in 2018–19. Accordingly, we assess that the Indian economy's main fundamental weaknesses and risks continue to lie on the fiscal front as the government's ability to respond to potential adverse shocks is somewhat limited.

In our view, the Indian economy is on the mend following disruptive reform implementations over the past year. Accordingly, a pick-up in real GDP gains will support the government's revenue growth. Nevertheless, Finance Minister Jaitley's estimate that economic growth will soon reach 8% y/y is somewhat optimistic in our opinion. We expect the Indian economy to expand by 7½% y/y over the next two years after an estimated 6.3% advance in 2017.

CONTACTS

Tuuli McCully
65.6305.8313 (Singapore)
Scotiabank Economics
tuuli.mccully@scotiabank.com

India's Central Government Fiscal Deficit



Sources: Scotiabank Economics, IMF, India Ministry of Finance.