Union Budget 2025-26 - Paradigm Shift

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"Budgets are not merely affairs of arithmetic, but in a thousand ways go to the root of the prosperity of individuals, the relation of classes and the strength of kingdoms." – William E. Gladstone

In terms of Article 112 of the Indian Constitution, a statement of estimated receipts and expenditures of the Government of India must be laid before Parliament every financial year from 1st April to 31st March. Hence, in this sense the Budget is routine. The Budget indicates the state of the economy, the priorities of the Government, and the use of instruments to realize identified objectives and influence the direction and pace of the economy. Hence, the Budget, which is a document of estimates based on assumptions and strategies to achieve those estimates, transcends a public statement of expected government revenues and scheme expenditures over one year and becomes a socio-economic and political document.

Global Perspective

The International Monetary Fund's (IMF's) World Economic Outlook (WEO) (January 17, 2025), makes a sober reading. While the IMF maintained its global growth forecast unchanged at 3.3 per cent both in 2025 and 2026, global headline inflation is likely to decline to 4.2 per cent in 2025 and to 3.5 per cent in 2026. In this tumultuous time, adroit risk management *"requires a keen policy focus on balancing trade-offs between inflation and real activity, rebuilding buffers, and lifting medium-term growth prospects through stepped-up structural reforms as well as stronger multilateral rules and cooperation"*. This is quite a tall order given President Donald Trump's accent on tariffs, a throwback to protectionism, currency volatility, and checking inflationary impulses while raising growth.

The WEO's assessment *"growth in India also slowed more than expected, led by a sharper-than-expected deceleration in industrial activity"* causes a gnawing feeling. But given the global setting of *"divergent and uncertain"* growth and India's consistent outperformance, there is no cause for alarm.

The Union Budget on February 1, 2025, provided an impetus to the transformative growth process of the Indian economy and revived the "animal spirits".

Domestic Backdrop

India's GDP is expected to decline markedly to 6.4 per cent in FY 25 and over 8.2 per cent in FY 24 because of flagging manufacturing and investment growth. The Ministry of Statistics and Programme Implementation (MoSPI) said *"Real GDP has been estimated to grow by 6.4 per cent in FY 2024-25 as compared to the growth rate of 8.2 per cent in Provisional Estimate (PE) of GDP for FY 2023-24. Nominal GDP has witnessed a growth rate of 9.7 per cent in FY 2024-25 over the growth rate of 9.6 per cent in FY 2023-24"*.

This slowest growth rate since the pandemic manifests moderation across key sectors occurred because of higher interest rates amid elevated inflation, particularly of food commodities, slack urban consumption, and capital expenditure.

Incidentally, the RBI had lowered its growth projection for the current financial year to 6.6 per cent from 7.2 per cent in its December 2024 Policy.

The RBI had kept the Repo rate steady since April 2023 (i.e., the last 11 consecutive meetings) after raising it by 250 basis points to 6.5 per cent between May 2022 and February 2023 to check inflation and bring inflation to the medium-term target of 4 per cent.

While agriculture is set to perceptibly rise by 3.8 per cent (1.4 per cent last year), most sectors face lower growth. Mining is projected to slow to 2.9 per cent from 7.1 per cent, while manufacturing growth is forecast at 5.3 per cent, down from 9.9 per cent. Electricity growth is estimated at 6.8 per cent, lower than last year's 7.5 per cent, and construction is expected to grow at 8.6 per cent, down from 9.9 per cent.

The top three contributors to GDP—manufacturing, trade & hotels, and financial services & real estate—are also estimated to slow in FY25, while

public administration is expected to rise. Urban consumption has been hit because of the ravages of sticky inflation eroding the purchasing power of the urban poor. There were also factors, such as rising economic uncertainties, the base effect, and heightened geopolitical risks driving down the growth rate. The Union Budget heralded the setting up of a *"National Manufacturing Mission"* (NMM) covering small, medium, and large industries for furthering *"Make in India"* by providing policy support, execution roadmaps, governance and monitoring framework for central ministries and states.

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Macro Budget Setting

This Budget was presented at a time of heightened geopolitical dynamics and a transilience from globalisation to protectionism, with tariffs emerging as a significant component of policy frameworks. India is currently experiencing a cyclical slowdown in economic growth, driven by fiscal consolidation measures and a deceleration in credit growth due partly to the RBI's macro-prudential tightening of consumer lending. In this overarching macroeconomic framework, the FM was required to address the challenging task of maintaining fiscal discipline while meeting the revolution of rising expectations of citizens and businesses- a task handled adroitly.

The Budget's thrust on consumption-led and inclusive growth focused on agriculture, Micro, Small, and Medium Enterprises (MSME), investment, and exports augurs well for India's development odyssey. Development measures focused on Garib, Youth, Annadata and Nari are contextually significant.

Agriculture- Integral Part of the Growth Saga

There are significant measures here to boost agricultural production and productivity since agriculture, which accounts for about 18 per cent of GDP and 54 per cent of employment, continues to provide the mainstay of the Indian economy. Accordingly, Dhan Dhanya Krishi Yojna includes contextually significant measures like a rise in Kisan Credit Card limits for farmers, fishermen, etc. increase from ₹ 3 lakhs to ₹ 5 lakhs, the 6-year mission for pulses and Agri plan to cover 100 districts with low productivity in phase 1.

MSMEs- Small is Big!

MSMEs have justly been identified as *"the second engine of growth"* because of the implications of 5.7 crore MSMEs for economic growth, structural transformation, moving up the value chain, and distributive equity. There are agreeable initiatives like increased loan guarantees to micro-entrepreneurs, loans to startups in 27 focus sectors at 1 per cent guarantee fees, term loans up to ₹ 20 crore for export MSMEs, customized credit cards for Udyam registered MSMEs, and Fund of fund for startups, another ₹ 10,000 crore to be set up. The Credit guarantee cover was enhanced from ₹ 2 crore to ₹ 5 crore for MSME. Startups will have a credit guarantee of ₹ 10 crore to ₹ 20 crore, well-run MSME ₹ 20 crore, Micro-enterprises will have ₹ 5 lakh limit of credit card, development of clusters and manufacturing of toys, Footwear and Leather sector scheme to generate employment to 22 lakh people and generate investment of ₹ 4 lakh crore, exports over ₹ 1.1 lakh crore and National Manufacturing Mission for MSMEs to bring about wholesome development. These broad-spectrum measures provide an impetus to MSMEs and help them move to a new and higher level.

Adherence to Fiscal Deficit Glide Path

India's deficit and debt dynamics imperil the macro-economy. Vitor Gaspar, IMF justifiably maintains *"Countries around the world face a fiscal policy trilemma: pressure to increase spending, public resistance to higher taxes, and risks from rising debt levels. Countries must navigate these challenges to maintain economic stability and growth."*

Since 2022, India's fiscal deficit has steadily declined. The government exceeded its fiscal deficit target of 4.9 per cent of GDP despite lower nominal GDP growth than budgeted, as stipulated in the medium-term budgetary policy-cum-fiscal strategy statement with the FY25 Budget. Higher direct taxes (which rose from 52 per cent in FY22 to 57.5 per cent of gross tax revenue in FY25) and increased non-tax revenues offset shortfalls in corporate taxes and excise duties. Further, reducing capital expenditure helped counterbalance the rising food subsidy costs.

Entirely in line with our expectations, the fiscal deficit for FY 25 came in at 4.8 per cent - below the budgeted level of 4.9 per cent - and for FY 26 at 4.4 per cent. The narrower fiscal deficit target underscores the commitment to longer-term fiscal sustainability and supports the economy amid high inflation and a challenging global environment.

Over the last ten years, the NDA Government has been successfully straddling knife-edge equilibrium between the requirements of economic growth and the promotion of the welfare of the disadvantaged sections. But the NDA Government has always been conscious of the concerns (the two COVID-19 years were a once-in-a-century event, and this aberration necessitated countercyclical fiscal measures

and a more active fiscal policy for macroeconomic *stabilization*) of containing the fiscal deficit within manageable proportions.

Going ahead, maintaining the fiscal glide path by generating adequate resources for the fisc without slashing welfare programmes constitutes an important policy dilemma. All revenue streams, viz., direct and indirect taxes, disinvestment, dividends from the PSUs and the RBI and public borrowings are being explored and examined to arrive at a judicious mix of the strategy of revenue generation to meet multiple conflicting requirements, broad-based development, restricting fiscal deficits and containing the ratio of debt to GDP. Towards this end, Budget management reforms and an independent institution to monitor the implementation of rule-based fiscal policy (the Fiscal Council) as recommended by the Finance Commissions could be helpful.

The new fiscal consolidation framework, which provides greater macroeconomic stability, is greatly welcome for the domestic economy and unmistakable commitment to fiscal stability will send the right message to global investors, multilateral institutions and global rating agencies.

Relief to the Middle Class

Persistent high inflation shrunk households' disposable income, especially for urban Indians, whereas the private urban consumption expenditure took a heavy toll. As visualized by us and strongly stressed on multiple channels and in various mediums, the middle class has been given a much-needed relief with no income tax up to ₹ 12 lakhs income. For salaried persons, it will rise to ₹ 12.75 lakhs by factoring in standard deduction.

This initiative provides significant relief to the middle class, which has been hit hard by the inflationary spiral and shore up consumption and investments. More specifically, this will lead to higher household consumption, saving, and investment, and in turn, significantly raise India's economic growth. Further, there are several well-conceived TDS and TCS reforms.

Consumption Boost

No wonder, then, this development salubriously impacted stocks across multiple sectors, including FMCG, automobiles, consumer durables, insurance, and green energy, among others. Meanwhile, railway, defence, and infrastructure stocks took a hit because of the government's capex hitting a plateau. However, continuing infrastructure investments will *"crowd-in"* private investment and make growth robust and sustainable over the medium-term.

Electric vehicles (EVs), high-end imported bikes and jewellery benefitted because of lower import duties as did several life-saving medicines.

The second SWAMIH Fund will facilitate the completion of 1,00,000 stalled homes.

These appreciable measures are reminiscent of what William Shakespeare (1564–1616) wrote eloquently in *The Merchant of Venice* (Act IV, Scene I),

"The quality of mercy is not strained; It droppeth as the gentle rain from heaven Upon the place beneath. It is twice blest; It blesseth him that gives and him that takes".

Viewed thereof, this far-reaching consumption booster measure like the quality of mercy will benefit both the taxpayer and the Government by reducing tax evasion and tax avoidance, improving compliance, and incentivizing people to work and pay their legitimate dues to the Government.

Conclusion

In sum, this Budget was marked by cross-cutting strategically important themes of fiscal prudence, economic growth, structural transformation and distributive equity. Given the ravages of the inflationary spiral and the shrinking disposable income, the enhanced income tax limit was well received across the development spectrum.

The government was pilloried for conceding to the Trump administration's trade priorities, e.g., reducing or eliminating customs duties on motorcycles and marine products. The trade package will help India's exports in an external environment of geoeconomic fragmentation and uncertainty triggered by President Donald Trump's tariff policies.

This Budget, which had a slew of initiatives for Bihar, was also unjustly slammed as a *"Bihar-centric, band-aid for bullet wounds"*.

There is certainly no end to expectations and the wish- list of various sectors and classes- *"yeh dil mange more"* (this heart yearns for more)! But given the heightened global dynamics and the macroeconomic changes, the element of continuity and change, relief to the middle class, a new Income Tax Bill to simplify the tax regime and reduce the compliance burden, advancing fiscal prudence and growth-oriented tax reforms while significantly shoring up consumption, and the need to reconcile diverse- at times conflicting - elements of the fiscal calculus, the FM has done the best of a difficult task by being responsive to the *"voice of the people"*. Not too bad!

(Views are personal)