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BUDGET FOR ANM (AGRICULTURE, NBFC & MSME) & "MEASURED" FISCAL CONSOLIDATION

Issue No. 23, FY20

Date: 02 July 2019

With the monsoon firmly set and filling up the water reservoir, the run up to the Budget seems to have been blessed by the rain God!. Overall for the next budget exercise the development goal might supersede the rigid objective of 'fiscal austerity'. Given the growth slowdown, the Government should ideally keep the deficit numbers constant for the next two years before reducing it further and try to propel growth. Sticking to a particular fiscal number is not that important in the current scenario. Instead, emphasis should be on making country-mandated fiscal rules that are credible and achievable. For an economy like India, higher public borrowings are a necessary evil given the large welfare schemes of the Government. As per our estimates, there is a 40% probability of fiscal deficit for FY20 being at 3.5% to 3.6% . The market will actually be happy with such numbers given the weak growth impulses. Here the government will do well to remember the traditional wisdom in Kautlya's *Arthsastra* which states that health of State treasury (Kosa) is important because all other goals of the society (Dharma, Artha and Kama) depend on it. Continuing the good work in rural sector, addressing the NBFC sector issues and making MSME the engine of growth should be the focus in the Budget exercise.

The Budget could focus upon tweaking with the agricultural sector. A big push to the term loan will boost the agricultural sector. Further, setting up of an Agri-marketing Reforms Council (AMRC) on the lines of the GST council and an exclusive focus on harnessing the rapidly shrinking water resources also deserve higher priority. NBFC sector calls for urgent attention. Till March 2020, Rs 4.75 trillion of bonds and papers of NBFC sector are set to mature. Further, most of the NBFC exposure is to the reality sector. Some sort of demand boost for the reality sector, like GST concessions to the buyers and stamp duty rationalization could very well give a flip to the reality sector and can also help solve part of the NBFC quagmire that we are currently in. The MSME sector too needs urgent focus. Here, we believe, there is a need for amalgamation of CGTMSE and CGFMU. This will remove the complexities such as multiple coverage / non-coverage of MSME loans and understanding among field functionaries about various time norms to be adhered to under each guarantee scheme will be eliminated. Setting up of an Equity Fund on the lines of the Sinha Committee suggestions may also be crystallized.

As per our projections the yield curve may edge lower further with the 10 Yr G-sec yield likely to keep below 7% (now 6.88%) and eventually heading towards the range of 6.5 % to 6.6 %. This will be reflecting more of the growth outcomes rather than the Government borrowings.

- SBI expectations regarding the Union Budget 2019-20 are based upon principle of inclusive growth. To boost economic growth, India needs a clear focus on the rural sector. Clear and tangible efforts are needed on designing a suitable price incentive for farmers. Consolidation in banking sector, adding more infrastructure to NCLT process through judicial reforms, export promotion, boost to investment and manufacturing, focus on skilling to improve employability of Indian youth are certain other areas that require attention.
- Accordingly, the budget should give priority to the areas like: agriculture, NBFC ,MSME, insolvency & NPA resolution, infrastructure and land & labour reforms.

SUGGESTIONS RELATED TO BANKS

- Under recapitalisation, over the last 3-financial years, PSBs have been recapitalised to the extent of Rs 2.87 lakh crore, with infusion of Rs 2.20 lakh crore by the Government and mobilisation of over Rs 0.66 lakh crore by PSBs themselves. As per our estimates, additional capital is likely to lay the basis for growth capital in FY20. Assuming a 12-13% credit growth in FY20 with credit risk weighted assets of 70%, PSBs may be requiring around Rs 50,000 crore growth capital in FY20. However, the same also depends upon some major variables i.e. alternate long term investor, recoveries from NCLT, investment environment, out of NCLT settlements/auctions, treasury gains / loss, MTM provisioning of investments, additional or provision write-back.
- At present, the share of top five banks in credit is around 39%. (China: 47%) Thus, continued banking consolidation will improve the banks' ability to lend for developmental needs. There is also an immediate need to augment number of NCLT benches so that the resolution system does not get choked. HR reforms for PSBs must also be a priority for the new Government.
- Measures in respect of some lapses in NBFC sector is required to send a strong message. This is all the more urgent since if the NBFC sector health does not improve, banks will have to face fresh round of NPA provisions going forward.

Capital infused in PSBs by Government (Rs in crore)

Bank	Total
Allahabad Bank	13,691
Andhra Bank	8,265
Bank of Baroda	10,417
Bank of India	26,794
Bank of Maharashtra	8,176
Canara Bank	5,610
Central Bank of India	13,147
Corporation Bank	14,336
Dena Bank	4,091
IDBI Bank Limited*	14,371
Indian Bank	0
Indian Overseas Bank	13,308
Oriental Bank of Commerce	10,257
Punjab National Bank	21,740
Punjab and Sind Bank	785
Syndicate Bank	7,578
UCO Bank	14,838
Union Bank of India	9,177
United Bank of India	8,658
Vijaya Bank	1,277
State Bank of India	14,481
Total	**220,997**

* IDBI Bank Limited has been recategorised by RBI as a private sector bank, with effect from 21.1.2019.

FISCAL IMPERATIVE

- With the rising concern about the slowdown in economic growth, slowdown in direct taxes and GST issues, the Government should not pursue the path of *"fiscal austerity"*.
- India's Gross fiscal deficit as % of GDP has declined to 3.4% in FY19. However, to achieve this revised target in FY19 there has been a significant reduction of Rs 1.45 lakh crore in expenditure with Rs 69,140 crore cut in subsidies (major cut in food subsidy of Rs 69,394 crore), covering for Rs 1.57 lakh crore reduction in total receipts.
- As, the FY19 estimates are revised, the FY20 fiscal estimates might seem to be on the higher side, specially for tax revenue and revenue expenditure. For BE FY20, annual growth rate of tax revenue now comes to 29.1% (much higher than the 5 year CAGR of 13.2%) while, revenue expenditure growth is at 21.9% compared to 5-year CAGR of 9.9%. Thus, it seems these estimates are likely to be revised in the upcoming full budget on 05 Jul'19.
- There is a lot of conundrums on the table. The tax revenue CAGR growth was 13.2% in the last 5 year and 14% in the last 10-year. By assuming the revenue growth of 14% and expenditure growth of 20% (as was in the last year) there would be Rs 2.1 lakh crore shortfall compared to interim numbers. So, to keep the fiscal deficit at 3.4%, Government has to do aggressive expenditure cut (particularly the revenue expenditure: Rs 70,000 crore cut in food subsidy and rationalization of other expenditures), which looks very difficult. So, there is a need to enhance the disinvestment target by extra Rs 10,000 crore to Rs 1 lakh crore.
- We believe that Government should keep Nominal GDP growth at 11.5% for FY20 (Real GDP: 7.5% and inflation: 4.0%) as it was estimated in Interim Budget.
- Keeping in mind that the growth slowdown, Government should ideally keep the deficit numbers constant for the next 2-years before reducing it further and try to propel growth in the country.
- However, what should be the appropriate size of public in an economy is an unsettled question. In 2005 the Government of Japan did an extensive survey of this idea.
- This report concluded that: Generally, the size of government is expressed either as the amount of spending and burden or as the strength of government involvement in terms of regulation. In either case, when government becomes large, the effective distribution of resources by the economy as a whole will not be achieved, and economic activity is likely to be less vigorous than it is under a smaller government.

SBI Estimates of Budget 2019-20 (Rs Crore)

Item	FY19 (PE)	FY20 (Interim BE)	FY20 (SBI)	FY20 Interim BE/FY19 PE (%)	FY20 (SBI)/ FY19 PE (%)	5 Yr CAGR (FY15-19 in %)
1.1 Revenue Receipts	15,63,170	19,77,693	17,98,000	26.5	15.0	11.9
1.1.1 Tax Revenue (Net to centre)	13,16,951	17,05,046	15,28,000	29.5	16.0	13.2
1.1.2 Non-Tax Revenue	2,46,219	2,72,647	2,70,000	10.7	9.7	5.5
1.2 Capital Receipts	-	8,06,507	8,18,000	-	-	6.7
1.2.1 Recoveries of Loans	17,840	12,508	13,000	-29.9	-27.1	-1.1
1.2.2 Other Receipts	85,045	90,000	1,00,000	5.8	17.6	20.7
1.2.3 Borrowings and other liabilities*	6,34,398	7,03,999	7,05,000	11.0	11.1	5.6
1. Total Receipts	16,66,055	27,84,200	26,16,000	67.1	57.0	10.2
2. Total Expenditure	23,11,422	27,84,200	26,35,000	20.5	14.0	10.2
2.a) Revenue Expenditure	20,08,463	24,47,907	23,00,000	21.9	14.5	9.9
2.a).1 Grants for creation of Capital Assets	-	2,00,740	2,00,700	-	-	-
2. a).2 Interest Payments	-	6,65,061	6,70,000	-	-	-
2.b) Capital Expenditure	3,02,959	3,36,293	3,35,000	11.0	10.6	12.6
3. Revenue Deficit (2.a)-1.1)	4,11,669	4,70,214	5,02,000	14.2	21.9	3.0
4. Effective Revenue Deficit (2.a)-2a).1)	-	2,69,474	3,01,300	-	-	-
5. Fiscal Deficit {2-(1.1+1.2.1+1.2.2)}	6,45,367	7,03,999	7,24,000	9.1	12.2	5.6
% of GDP	**3.4%**	**3.4%**	**3.4%**	-	-	-
6. Primary Deficit	46,828	38,938	54,000	-16.8	15.3	-18.9
Revenue Deficit / Fiscal Deficit (%)	**64.8**	**66.8**	**69.34**	-		
Memo:						
Nominal GDP	1,88,40,731	2,10,07,439	2,10,07,415	-		
Growth rate	10.2	11.5	11.5			

Source:Union Budget Documents & SBI Research

Yearly Public Sector Borrowing Requirement (in Rs billion)

Year	GDP (MP)	Market Borrowing (States + Centre)	FCI Borrowing	NABRD Borrowing	Total Borrowing	Borrowing to GDP Ratio (%)
2017-18	170950	8058	2430	437	10926	6.39%
2016-17	153624	7393	1555	342	9290	6.05%
2015-16	137719	7048	1175	206	8429	6.12%
2014-15	124680	6729	1106	95	7930	6.36%

Source: RBI, SBI Research

- The traditional wisdom in Kautlya's Arthsastra States that health of State treasury (Kosa) is important in because all other goals of the society (Dharma, Artha and Kama) depend on it.

OFF BLANCE SHEET BORROWING

- We made an attempt to calculate the Public Sector Borrowing Requirement (PSBR) of the Centre, States and two major Public Sector Agency such as FCI and NABARD to come out the average yearly PSBR. Our estimate shows yearly PSBR is around 6% (excluding State public sector agency). We also have didn't include the off-budget loans of State Government and their agencies. If these are included, the full PSBR may exceed 7% of GDP.
- PSBR for the Centre, States, off-balance sheet & government-owned entities, when taken together, was at 6.39% of GDP in 2017-2018 and no different from four years earlier.

Sector-Specific Suggestions	
Agriculture	⇒ Extension of interest subvention to all farm loans, particularly covering investment credit up to Rs 3 lakhs ⇒ Set up an Agri-marketing Reforms Council (AMRC) to carry out agri-marketing reforms in states in a synchronized manner. ⇒ Government should ensure that the Model Agricultural Produce and Live-stocks Marketing (APLM) Act of 2017 is implemented by all the States.
Real Estate & Affordable Housing	⇒ The definition for Affordable Housing and that of Priority Sector should be made uniform. ⇒ The real estate sector should be given a demand boost as it will also address the problem of the NBFC sector. These could include tax benefits as well as one time relief measures on GST, Stamp Duty, Charges for the Registration of mortgage for properties bought before March 31, 2020. ⇒ Student Housing and Co living is a new concept in India. Construction mainly for students and co-living by the builders may be given benefits in form of tax concessions on rental income. ⇒ Pension and Provident Funds may be encouraged to invest in PE funds through SPV for onward investment in Affordable Housing.
Infrastructure & EPC	⇒ Creation of market friendly infrastructure for Natural Gas sector is a must. ⇒ Coastal river linking may be extended to other coastal states in western, southern and eastern states. ⇒ Public sector Banks / FIs may be permitted to source long term funds from domestic investors (rebate may be given in addition to section 80 C) to fund infrastructure projects. Tax rate concessions to lenders funding infrastructure projects of long duration say beyond 10 years. ⇒ Creation of land banks and upfront / single window approvals for infrastructure projects of national importance is the need of the hour.
MSME	⇒ There is a need for amalgamation of CGTMSE and CGFMU. This will remove the complexities such as multiple coverage / non-coverage of MSME loans and understanding among field functionaries about various time norms to be adhered to under each guarantee scheme will be eliminated. Setting up of an Equity Fund on the lines of the Sinha Committee suggestions.
NBFC	⇒ An IBC like framework for NBFCs should be created to resolve the issues in a timely manner. ⇒ Am enabling atmosphere must be created for securitization.
Source: SBI Research	

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