Asia in Focus

India's Fiscal policy: Union Budget Preview: Beyond the numbers

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- There is a growing expectation among some investors that India's final union budget for FY25 will see some relaxation in the fiscal consolidation path and a pivot towards welfare spending from capex. We push back against both views: a) there is limited fiscal space in our view to stimulate the economy given high public debt, b) India's infrastructure upgrades have created long-term positive growth spillovers which policymakers may not be willing to give up.
- We expect the general government to stick to the announced fiscal deficit target of 5.1% of GDP for FY25 (or even slightly lower) and announce further consolidation to a deficit of below 4.5% of GDP by FY26. Even if we see some expenditure allocation towards welfare spending, it may not require a reduction in capex given the higher than expected dividend transfer from the RBI.
- In the general government's budget, interest expense constitutes a large share at 5.4% of GDP and with the primary deficit at 3.5% of GDP in FY24, this leaves the general government with limited fiscal space for stimulus in FY25, in our view. Our fiscal impulse calculations also show that **general government fiscal policy** has been a drag on growth since FY22 and **will remain so in FY25 and FY26** given the fiscal consolidation target of the central government.
- The central government's fiscal impulse breakdown suggests that the very robust capex CAGR of ~31% over FY21-24 resulted in a growth boost, while welfare spending has been a net drag since FY22. In FY25, we expect capex to provide a positive impulse, while welfare spending will likely remain a drag.
- We think this budget will go beyond just fiscal numbers, and likely make an overarching statement about long-term economic policy of the government towards 2047 (100 years of Indian independence). We see an emphasis on job creation through labor-intensive manufacturing, credit for MSMEs, continued focus on services exports by expanding GCCs, and a thrust on domestic food supply chain and inventory management to control price volatility. The budget is also likely to lay out a path for the future of public finance in India, entailing: a) a roadmap for **public debt sustainability**, and b) **green finance:** the role of public finance in balancing India's energy security vs. transition needs.

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A budget beyond numbers

The central government will announce the final union budget for FY25 (March 2024 - April 2025) on July 23. Given that this comes after the below (exit-poll) expectation results of the national elections for the ruling BJP, there is growing expectation among equity investors that this budget will see some relaxation in the fiscal consolidation path and a pivot towards welfare spending from capex.

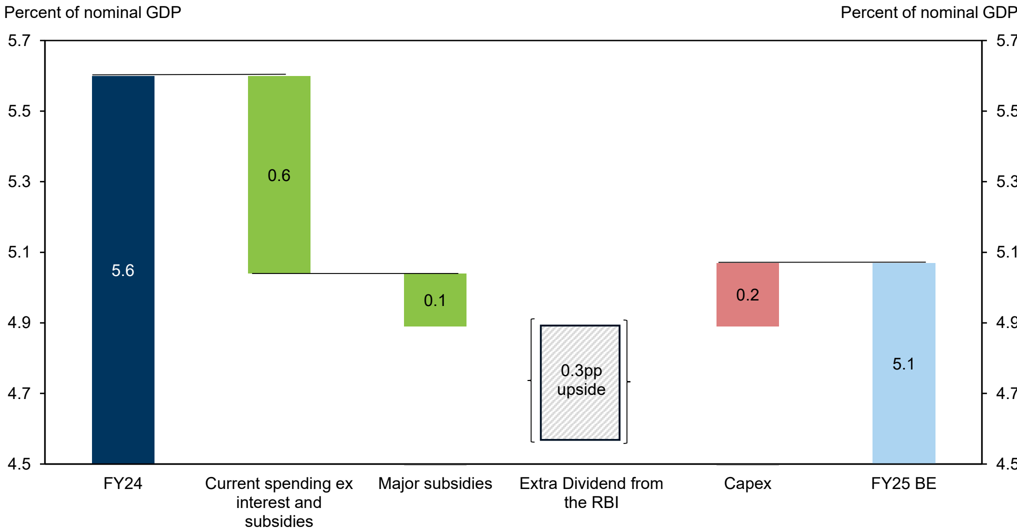
We push back against the former view given that India has limited fiscal space available, in our view, to stimulate the aggregate economy given public debt constraints. And we think the latter is unlikely as India's infrastructure upgrades over the last few years have created long-term positive spillovers which policymakers may not be willing to give up.

The government turned to capex during the pandemic as a means to buoy the economy out of the recession. Even as it consolidated the headline fiscal deficit from FY21, it continued to lean heavily on capex to boost infrastructure. Government capex growth was significantly higher than nominal GDP growth during this period (CAGR of 31% over FY21-24 vs. 12% over FY16-20), though the growth rates declined over the years as fiscal consolidation constraints dominated.

The central government over the last few years has been committed to fiscal consolidation and reduced the fiscal deficit for FY24 (April 2023 – March 2024) to 5.6% of GDP[1] from 9.2% of GDP in FY21. We expect the government to stick to the announced fiscal consolidation target of 5.1% of GDP for FY25 (or even better it slightly) and announce further consolidation to below 4.5% of GDP by FY26. Even if we see some expenditure allocation towards welfare spending, it may not require a reduction in the capex given the higher than expected dividend transfer from the RBI last month (Exhibit 1).

[1] This is 0.2% of GDP lower than the revised estimate and 0.3% of GDP lower than the budget estimate.

Exhibit 1: We expect the central government to meet its fiscal deficit target of 5.1% of GDP



Source: CEIC, Goldman Sachs Global Investment Research

Exhibit 2: We expect the government to stick to its fiscal deficit target of 5.1% of GDP in FY25

Central Government Fiscal Accounts (% of GDP)			
Key Budget Items	**2023**	**2024**	**2025-BE**
Total Receipts	**9.1**	**9.4**	**9.4**
Revenue Receipts	**8.8**	**9.2**	**9.2**
Gross Tax Revenues	**11.3**	**11.7**	**11.7**
Direct tax	**6.1**	**6.5**	**6.7**
Income Tax	3.0	3.4	3.5
Corporate Tax	3.1	3.1	3.2
Indirect Tax	**5.3**	**5.2**	**5.0**
GST (incl Comp cess)	3.2	3.3	3.3
Excise	1.2	1.0	1.0
Customs	0.8	0.8	0.7
Less Allocation to states	**3.5**	**3.8**	**3.7**
Net Tax Revenue	**7.8**	**7.9**	**8.0**
Non Tax Revenues	**1.1**	**1.4**	**1.2**
Non-debt capital receipts	**0.3**	**0.2**	**0.2**
Expenditure	**15.6**	**15.0**	**14.5**
Revenue (Current)	**12.8**	**11.8**	**11.2**
Interest Payments	3.4	3.6	3.6
Subsidies	2.0	1.4	1.3
Food	1.0	0.7	0.6
Fertilizer	0.9	0.6	0.5
Petroleum	0.0	0.0	0.0
Capital	**2.7**	**3.2**	**3.4**
Fiscal Deficit	**6.4**	**5.6**	**5.1**
Revenue Deficit	**4.0**	**2.6**	**2.0**
Primary Deficit	**3.0**	**2.0**	**1.5**

Notes:
1. Fiscal year 2025 runs from Apr 24 - Mar 25. 2025-BE Budget Estimates
2. Non-tax revenues include Dividends from the RBI.
3. Revenue spending is current expenditure.
4. Non-debt capital receipts include disinvestment receipts.

Source: CEIC, Goldman Sachs Global Investment Research

The bigger picture: A long-term vision statement

We advise investors to look beyond just the fiscal numbers in this budget. We think the government will use the budget as an opportunity to make a big picture statement about the long-term economic policy vision over the next several years, rather than minor stimulus announcements. These are likely going to align with the government's development agenda for 2047 (coinciding with centennial of Indian independence).

There is likely to be a thrust on the following key areas among others:

a) Rural economy: A thrust on food supply chain and inventory management domestically to control price volatility. This is likely to happen through focus on rural infrastructure for better connectivity, incentivizing domestic food production, cold storage and food processing.

b) Job creation through labor-intensive manufacturing: while integrating in GVCs (possible beneficiary sectors could be textile, footwear, toys etc.).

c) Support for MSMEs in the form of credit or fiscal incentives. MSMEs in India produce ~30% of output (GVA as of FY22) and employ 120mn+ workers.

d) Skilling: To bridge the education gap, we expect workers to be skilled in a short span of time through vocational programs or on-the-job training.

e) High quality services jobs: We expect continued focus on services exports through expanding GCCs, GTCs and GECs.

The reforms challenge: This is the first time in the last ten years that the BJP will be running a government without a majority on its own in the Lok Sabha (the lower house of parliament). We think a reduced political mandate will require more political capital to be spent behind passing structural reforms like land reform and farm sector reforms (Exhibit 3).

Exhibit 3: We expect a focus on rural infrastructure, labor intensive manufacturing and MSMEs

Sector	Objective	What can be expected	Implementation (Likely / Unlikely)
Rural	1) Control food inflation 2) Promote employment	- *Agri-infra projects:* Cold storage facilities, expansion of more efficient irrigation network, grading and sorting units, food processing. - *Incentives to increase domestic production* of edible oil, pulses, vegetables, and fruits, expand dairy co-operatives, fisheries. - *Reduce input costs* of machinery, increase availability of seeds, allocation for price stabilisation fund for vegetables, pulses etc.	Likely
Support for MSME	1) Socio-economic growth 2) Promote employment	- *The micro loan (MUDRA) limit may be doubled up to INR 2mn*. Total loans disbursed under the scheme from FY16 to FY24 is around INR 27tn - Reduce compliance burden for small traders and MSMEs	Likely
Manufacturing	1) Promote Private capex	- Continued focus on manufacturing, with emphasis on *labor-intensive manufacturing through fiscal incentives*: Global hub for toy, textile, apparel manufacturing - Commercial aircraft manufacturing	Likely
Housing	1) Promote welfare	- *Housing* for every poor family. Under the rural housing scheme ~26mn houses built since 2016 - *Slum redevelopment* in major cities - *Reduce regulatory costs* (registration), regulatory reforms enabling automatic approvals - *Clean drinking water* for households in rural and urban areas	Likely
Services	1) High value jobs 2) External balances stability	- *Expand Global Capability Centres (GCCs)*, Global Technology Centres (GTCs) and Global Engineering Centres (GECs) - *Focus on tourism* for job creation	Likely
Social Security	1) Promote welfare	- *Insurance for unorganized workers.* As of FY22 around INR 109bn premium was collected and INR 167bn was paid in claims under government insurance schemes - Get taxi, truck and 3-wheeler drivers under insurance schemes	Likely
Infrastructure	1) Higher investment growth	- Continued focus on infrastructure creation, through *more rail network*. Focus on East, and North-East India - Add 5000+ km of new rail tracks every year for the next few years	Likely, but fiscal allocation may shift off-balance sheet
Reforms	1) Enhance productivity	- Progress on structural reforms like land and labor market reforms to create an enabling regulatory environment for manufacturing growth. - Market linked pricing for farm produce	Difficult to implement

Source: Goldman Sachs Global Investment Research

Does India have fiscal space for a stimulus?

The pandemic had a meaningful shift towards expansionary fiscal policy, to avert negative scarring impacts on the economy. India's general government fiscal deficit expanded to 13.3% of GDP in FY21 from 7.3% of GDP in FY20, and has contracted to 8.9% of GDP in FY24[2] as per RBI estimates, with primary deficit at 3.5% of GDP and interest expense at 5.4% of GDP.

- **Interest expense** is a large part of India's fiscal deficit, averaging around 5% of GDP over FY14-24 (Exhibit 4). It has increased from 4.8% of GDP in the pre-pandemic period (FY14-20) to 5.3% of GDP post pandemic (FY21-24) as the general government debt rose from 72% of GDP in FY14-20 to 86% of GDP in FY21-24.
- **Primary deficit** (headline deficit excluding interest payments) has averaged around 3.1% of GDP over the last ten years, but there is a clear divergence in the pre and post Covid trends. It significantly increased from 1.8% of GDP (average over FY14-20) to 7.9% of GDP in FY21, driven by a broad-based increase in food subsidies, welfare spending and capex, and has been consolidating since then.

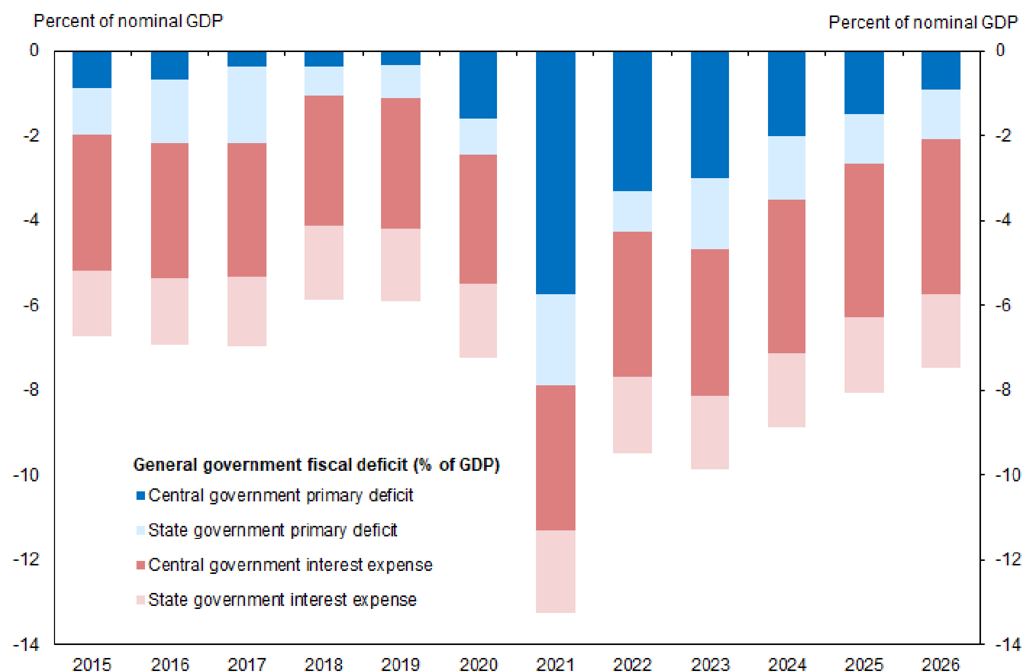
How to think about fiscal stimulus?

Headline measures of fiscal deficit are usually inaccurate when assessing the **expansionary or contractionary stance** of fiscal policy as these include the effects of automatic stabilizers[3] (effects of the economic cycle on fiscal parameters). In other words, the headline deficit figure includes two endogenous aspects that do not impact growth directly: the effect of the economic cycle and interest expense. Thus, to assess the stance of the fiscal policy in an economy we look at the **fiscal impulse.**

[2] States fiscal deficit for FY24 is as per RBI's estimates

[3] Automatic stabilizers refer to ongoing government policies that automatically help stabilize the economy without any additional policy action by the government. For example during high economic growth periods, number of jobs increase, increasing incomes and tax revenues. The net impact of fiscal policy in this situation is thus contractionary without any policy action undertaken by the government.

Exhibit 4: Interest expense is a large part of the general government's fiscal deficit



Note: i) Estimates here are based on actual fiscal deficit numbers upto FY24. ii) For the central government FY25 numbers are based on budget estimates and FY26 numbers are based on fiscal deficit assumption of 4.5% of GDP as per the central government's target. iii) For the state government FY25 and FY26 fiscal deficit is as per GSe of 2.9% of GDP

Source: CEIC

How much can fiscal deficit stimulate the economy?

The fiscal impulse is related to the fiscal deficit, but differs in three ways:

1) It is the **change** in the deficit rather than the **level** of deficit that matters most for growth[4].

2) A **change** in the structural primary deficit is referred to as the "*fiscal impulse*" in the economy, and is a better measure of the stance of fiscal policy than the all-in deficit.

3) The *'fiscal impulse'* adjusts for the different impact on growth from different sources of deficit – the marginal propensity to consume or invest – and the period over which these effects occur.

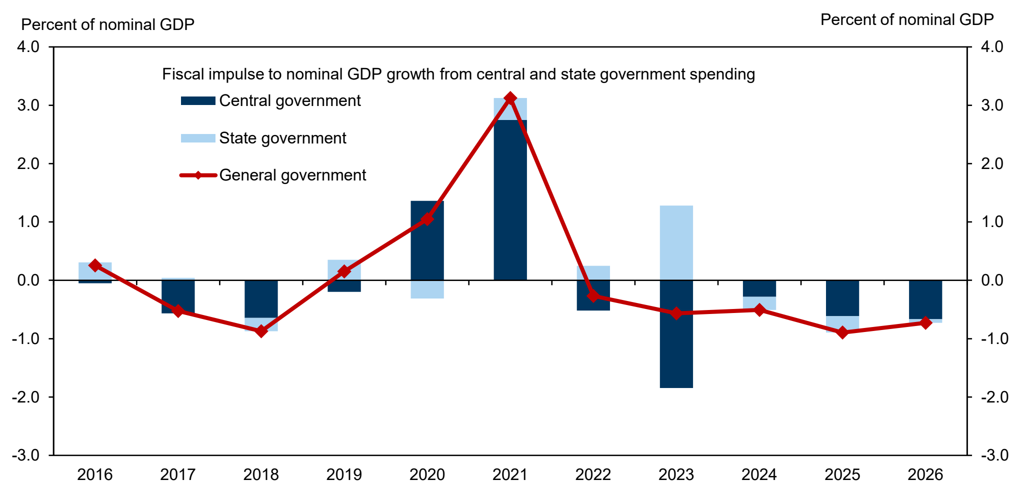
This is different from the concept of a multiplier, i.e. it does not account for what is the multiplier on growth from a unit of welfare spending or capex in subsequent periods.

To analyze the contribution of fiscal policy on consumption and by an extension to GDP growth, we re-visit our fiscal impulse measure developed previously with some modifications (Please see Appendix (Exhibit 13) for more details). We compute the net fiscal impulse on the economy by aggregating the fiscal impulse from various components of expenditure and revenue items, adjusting for the impact that different expenditure categories / tax items have on growth using our assumptions on marginal propensity to consume and invest for each of the spending and tax items.

[4] Growth itself is a measure of change rather than level.

Our fiscal impulse calculations show that **general government fiscal policy positively contributed to growth from FY20 and FY21** (after baking in scarring effects to potential growth during the pandemic) and has been a drag on growth since FY22. In our base case assumption, **it will continue to be a drag on growth in FY25 and FY26** given the consolidation target of the central government (Exhibit 5).

Exhibit 5: We estimate fiscal policy to be a net drag on nominal GDP growth in FY25 and FY26



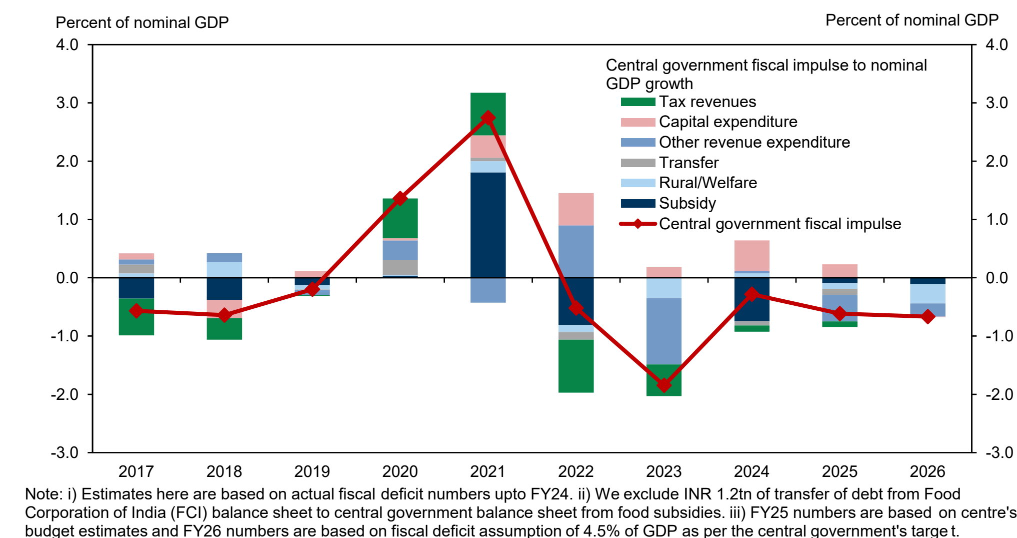
Note: i) Estimates here are based on actual fiscal deficit numbers upto FY24. ii) We exclude INR 1.2tn of transfer of debt from Food Corporation of India (FCI) balance sheet to central government balance sheet from food subsidies. iii) For the central government FY25 numbers are based on budget estimates and FY26 numbers are based on fiscal deficit assumption of 4.5% of GDP as per the central government's target. iv) For the state government FY25 and FY26 fiscal deficit is as per GSe of 2.9% of GDP

Source: Goldman Sachs Global Investment Research

A breakdown of the central government's fiscal impulse by spending and tax revenue brings forward some interesting trends:

- Higher capex growth (~31% CAGR over FY21-24) has contributed positively to nominal GDP growth since FY21, i.e. the growth in capital expenditure was higher compared to the counterfactual trend growth rate, providing a positive fiscal impulse to overall growth. We expect capex to continue to provide a positive fiscal impulse in FY25 should the government meet the budget estimate.
- Welfare spending and transfer payments had a positive impulse on FY20 and FY21 growth, while subsidies were a significant additional boost to growth in FY21, at the beginning of the pandemic. These have been a net drag since FY22 (Exhibit 6).
- Tax revenues contributed positively to growth in FY20 and FY21, as the government cut corporate tax rate from 30% to 22% in FY20.
- Based on our calculations, the net impact of fiscal policy on growth would be negative in FY25 and FY26 despite the boost from capex in FY25.

Exhibit 6: Higher capex has contributed positively to nominal GDP growth post-pandemic, while subsidies and welfare spending have been a net drag



Note: i) Estimates here are based on actual fiscal deficit numbers upto FY24. ii) We exclude INR 1.2tn of transfer of debt from Food Corporation of India (FCI) balance sheet to central government balance sheet from food subsidies. iii) FY25 numbers are based on centre's budget estimates and FY26 numbers are based on fiscal deficit assumption of 4.5% of GDP as per the central government's target.

Source: Goldman Sachs Global Investment Research

What can change? A "tilt", not a "pivot" towards welfare spending

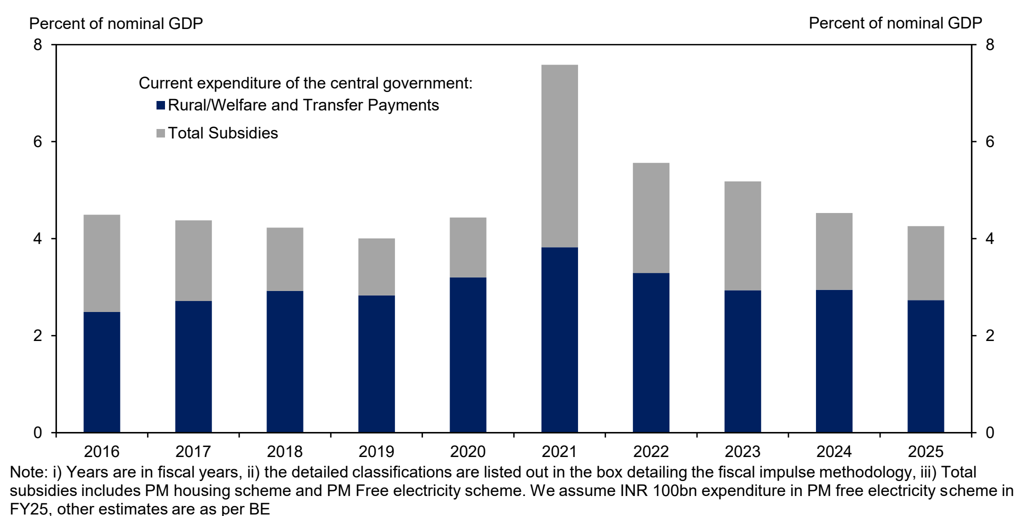
Current expenditure: We split the current expenditure of the central government into five broad categories: i) transfer to households, ii) subsidies, iii) rural expenditure, iv) welfare expenditure and v) urban expenditure (Please see Appendix for more details) (Exhibit 7).

We include pensions and farmer cash assistance programme under transfers to households. Under subsidies, we include the housing scheme and free electricity (solar panel) scheme, where the former provides a subsidy on housing loan for houses in the rural / urban areas, while the latter provides a fixed subsidy amount proportionate to the (number of) kilowatt (kW) system installed at a rural/urban home.

Based on our classification we observe some key trends:

- Outlay on total subsidies based on our classification has averaged around 1.5% of GDP in the pre-pandemic period (FY16-20). During the pandemic in FY21, it surged to 3.8% of GDP before declining to 1.5% of GDP in FY25 (as per BE) mainly due to lower outlay on major subsidies of food and fertilizer. However, there are upside risks to these numbers from higher food subsidies to deal with supply shocks from weather disturbances.
- Rural expenditure, welfare spending and transfer payments have averaged around 3% of GDP in the pre-pandemic period (FY16-20) and are now reverting to trend after increasing during the pandemic in FY21.

Exhibit 7: Subsidies budgeted to moderate in FY25



Note: i) Years are in fiscal years, ii) the detailed classifications are listed out in the box detailing the fiscal impulse methodology, iii) Total subsidies includes PM housing scheme and PM Free electricity scheme. We assume INR 100bn expenditure in PM free electricity scheme in FY25, other estimates are as per BE

Source: CEIC, Goldman Sachs Global Investment Research

Income tax cut: Income tax collections (as a % of GDP) have been gradually increasing in the pre-pandemic period from 2.1% of GDP in FY14 to 2.5% of GDP in FY20. As the economy re-opened in FY22, the ratio increased to 3.0% of GDP and has risen since then. If the government chooses to change income tax policy, based on our assessment of hypothetical scenarios[5], we estimate the revenue loss of the government to be around 5-15bp of GDP[6] with the fiscal impulse being meager around 2-7bp in FY25.

Policy options with the INR 1tn (0.3% of GDP) extra dividend from the RBI

- The RBI transferred 0.3% of GDP extra dividend to the government in May, and we provide a sensitivity analysis of fiscal deficit (% of GDP) under different scenarios of capital expenditure growth (yoy) and current expenditure (ex interest payments) growth (yoy).
- If the higher than budgeted dividend from the RBI is used for increasing expenditure, capex growth could increase to 21% yoy (from 17% yoy BE) while current expenditure growth (ex interest payments) could increase to 5% yoy if the government sticks to its fiscal deficit target of 5.1% of GDP in FY25 (Exhibit 8).
- We further analyze the fiscal impulse through current expenditure, if the extra dividend is allocated to welfare schemes/subsidies, transfer payment, or tax cuts. Given our MPC assumptions (Exhibit 13), we estimate the largest boost from subsidies and welfare expenditure, while the impact from a cut in tax

[5] We view these estimates as illustrative as the revenue loss from such a measure requires an in-depth general equilibrium analysis as a tax cut for the lower income households may raise consumption and hence indirect taxes (via GST collections) which can provide an offset to lower direct tax collections.

[6] We considered three different hypothetical scenarios of income tax policy change, i) Increasing the standard deduction limit by INR 50k under the new tax regime, ii) Increasing the net taxable income, exempted from taxation from INR 0.3mn to INR 0.4mn under the new tax regime, iii) Increasing the amount of exemption from tax savings by INR 50k under the old tax regime

rates is likely to be the least (Exhibit 9).

- We view these estimates as illustrative rather than precise estimates owing to a number of limitations. Firstly there are uncertainties around our MPC estimates. Secondly, we only measure the first order effects of government policy on GDP, but not any second round effects whereby higher capital expenditure has ripple effects on real GDP growth in subsequent years. Thirdly, we also do not include any potential offsets from monetary policy.
- As per previous studies[7], the impact multiplier for capital expenditure is around 1.3-2.5 in the year of policy change, which implies that INR 1 extra spending on capital expenditure results in INR 1.3-2.5 higher nominal GDP in the year of policy change.

Exhibit 8: Capital expenditure growth may increase to 21% yoy (vs. 17.1% budgeted growth) while current expenditure could increase to 5.0% yoy given the higher than budgeted dividend from the RBI

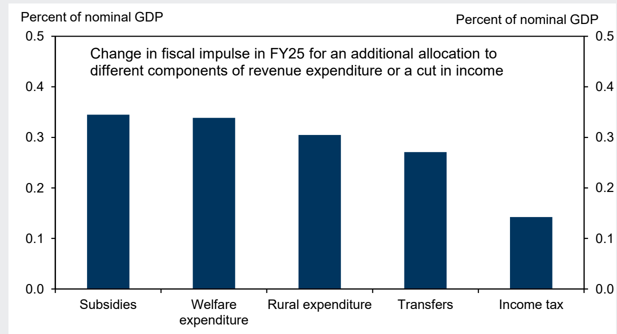
FY25 fiscal deficit (% of GDP) scenarios under different assumptions of capex and current expenditure (ex interest payments) growth

			Capital expenditure growth (% yoy)		
			BE		
		Scenarios	**17.1**	**20.7**	**30.3**
Revenue ex interest payments (% yoy)	**BE**	**1.4**	4.8	5.0	5.2
		5.0	5.0	5.1	5.4
		7.0	5.2	5.3	5.6

Note: We assume a 30bp boost to fiscal deficit from a higher than budgeted dividend from the RBI and base our growth scenarios starting from a base fiscal deficit assumption of 4.8% of GDP

Source: CEIC, Goldman Sachs Global Investment Research

Exhibit 9: We estimate the largest boost from subsidies and welfare expenditure in FY25 should the government reallocate the additional INR 1tn it received as dividend from the RBI last month



Source: Goldman Sachs Global Investment Research

- **Managing the coalition:** Given that the BJP will be running a government without a majority on its own in the Lok Sabha, there have been some questions around the financial assistance that the two major coalition partners (Bihar and Andhra Pradesh) might receive in the upcoming budget for FY25. As per media articles, the Chief Minister of Andhra Pradesh which is one of the coalition states has sought increased central assistance in the redevelopment of the state capital. The states might also aim to reduce their debt burden should they receive any assistance from the center which is at 33%/36% of state GDP (as per FY24 BE) for Andhra Pradesh/Bihar respectively. In our view, the allocation from the center might not be large as a hypothetical transfer of 0.1% of national GDP to the states would in itself imply a 3% / 2% of state GDP boost to Bihar / Andhra Pradesh.
- **Public debt:** Finally, India runs a large public debt to GDP of 84% (central: 59% of GDP, states: 25% of GDP) compared to other EMs and consequently has a large interest burden of 3.6% of GDP. The government can also choose to retire some of its outstanding debt, or quasi government debt with the extra dividend from the RBI, which may result in lower borrowings and thus gross issuance this year by say INR 500bn to INR 13.6tn (vs. INR 14.1tn as per BE).

[7] See i) Bose, Bhanumurthy, 2014 Fiscal Multipliers for India, ii) Size of Government Expenditure Multipliers in India: A Structural VAR Analysis (RBI)

Public finance for the future

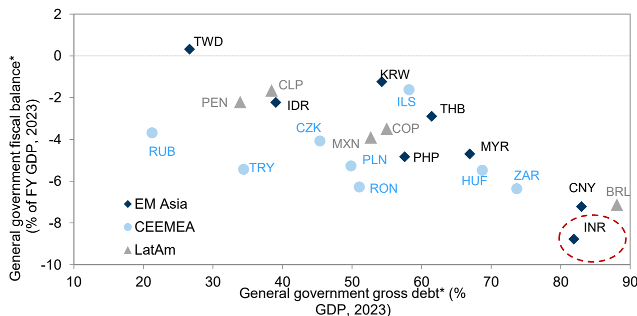
The budget is also likely to lay out a path for the future of public finance in India. The 16th Finance Commission which is responsible for determining the sharing of tax revenues between the central and the state governments is likely to submit its report by end October 2025. There are three important issues to look forward to:

a) **Debt sustainability:** A roadmap for public debt sustainability in India. India is a regional and EM outlier on both flow and stock of government debt, with a general government debt above 80% of GDP, hence the imperative for fiscal consolidation (Exhibit 10)

b) **Fiscal federalism:** Devolution of tax collection between the central and state governments, and how to raise tax to GDP ratio, which has been stagnant around 11% average over the last decade (Exhibit 11)

c) **Green finance:** How does India balance energy security vs. energy transition, and the role of public finance.

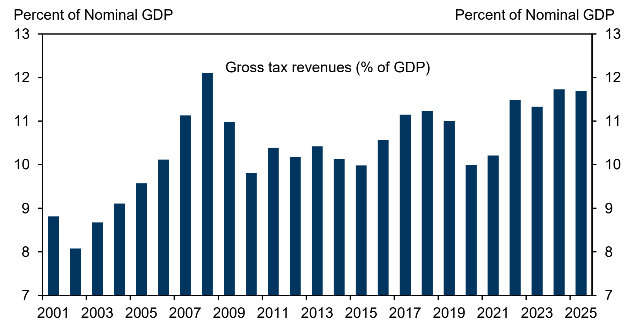
Exhibit 10: India is a regional and EM outlier on general government deficit



*General government fiscal balance and general government debt based on October IMF estimations; China general government balance based on GS estimates of China effective on-budget fiscal balance and government special bond issuance in 2023

Source: Haver Analytics, Goldman Sachs Global Investment Research

Exhibit 11: Gross tax revenues (as a % of GDP) have been stagnant, averaging around 11% over the last decade



Note: i) Years are in fiscal year. For example FY 2025 runs from April 2024 to March 2025, ii) Numbers upto FY24 are actuals and FY25 is as per the budget estimate

Source: CEIC, Union Budget

Appendix 1

Methodology for computing the fiscal impulse

We use the bottom-up methodology of deriving the fiscal impulse used by the Hutchinson Center of the Brookings Institute. We use an exhaustive list of spending and revenue items of the government on an annual basis since FY 2017.

On the expenditure side, we begin by excluding interest payments and grants given by the central government to the states from revenue expenditure as these do not add to any spending impulse in the economy. We then split the revenue expenditure (ex of interest payments and state grants) into five broad categories, i) transfer to households (including pensions and farmer assistance programme), ii) Subsidies, iii) Rural expenditure, iv) Welfare expenditure and v) Urban expenditure (Exhibit 12).

Exhibit 12: Classification of various current expenditure items

Current/Non-capital spending			
Sector	Ministry	Weight in revenue expenditure in FY24 (%)	Sector Weight
Interest Payments	Ministry of Finance	30.4	**30.4**
State Grants	Various ministries	23.1	**23.1**
Transfer to Households			**9.6**
PM Farmer assistance programme	Ministry of Rural Development	1.7	
Pension	Various ministries	7.8	
Subsidies			**13.4**
Major subsidies			11.8
Food	Department of Food and Public Distribution	6.1	
Fertilizer	Department of Fertilisers	5.4	
Petroleum	Ministry of Petroleum and Natural Gas	0.3	
PM Housing scheme			1.5
PM Housing scheme - Urban	Ministry of Housing and Urban Affairs	0.6	
PM Housing scheme - Rural	Ministry of Rural Development	0.9	
Rural	Ministry of Rural Development	3.8	**5.6**
	Ministry of Agriculture and Farmers' Welfare	1.7	
	Ministry of Fisheries, Animal Husbandry and Dairying	0.1	
Welfare	Ministry of Education	3.5	**9.8**
	Ministry of Health and Family Welfare (MHFW)	2.3	
	Department of Drinking Water and Sanitation	2.2	
	Ministry of Women and Child Development	0.7	
	Ministry of Social Justice and Empowerment	0.3	
	Ministry of Labour and Employment	0.3	
	Ministry of Tribal Affairs	0.2	
	Ministry of AYUSH*	0.1	
	Ministry of Skill Development and Entrepreneurship	0.1	
	Ministry of Youth Affairs and Sports	0.1	
	Ministry of Minority Affairs	0.0	
Urban	Ministry of Housing and Urban Affairs	0.6	**0.6**
Other revenue expenditure		7.6	**7.6**
Revenue expenditure			**100**

Note: i) Solar rooftop subsidy (PM free electricity scheme) is also included in Subsidies
ii) Rural expenditure excludes a) PM Rural Housing scheme, b) PM farmer assistance programme

Source: Goldman Sachs Global Investment Research

We categorize revenue into five broad categories, i) income taxes, ii) corporate taxes, iii) indirect taxes (which comprise primarily of GST, excise and customs), iv) non-tax revenues (dividend income from state owned enterprises, RBI) and v) capital receipts (income from sale of assets).

To calculate the impact of changes in government spending on subsidies, transfer, welfare and changes in taxes we define a set of marginal propensity of consumption (MPC)[8] and investment (MPI)[9] for the different categories of revenue and expenditure items described above (Exhibit 13).

We base our MPC assumptions on a survey of the literature, which suggests that India's MPC lies between 0.6-0.9[10]. Based on this evidence, we assume an MPC at the higher end of this range at 0.8 for transfer payments to households as these comprise pensions which go to the aged population of the economy and farm loan waivers which go to lower income households.

For subsidies and welfare expenditure, we assume an MPC of 1 as the economic agents have no other recourse to use the money other than the subsidies they are getting it for. For rural expenditure we use an MPC of around 0.9 (close to 1) as one of the major demand based, rural employment schemes by the government – Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA) accounts for close to 50% of the rural expenditure. We consider this rural employment programme as a source of transitory income which translates into an MPC of 0.9 as per previous studies. We assume an MPC of 0.6 for capital expenditure based on a previous study which assigns the multiplier of capital expenditure to growth as 2.5 in the year of policy change[11].

For personal income tax we assume an MPC of 0.7 (average of the range of India's MPC between 0.6-0.9) and for corporate taxes we assume a MPI of 0.9 based on a previous study (The Macro Economic Effects of Corporate Tax Cuts: International Evidence and Implications for India).

As households and firms typically adjust their consumption or spending patterns slowly over time, we distribute the personal income tax and corporate tax MPC and MPI over time. For income and corporate taxes we assume 60% of the impact of spending in the first year and 40% in the 2nd year after the policy change.

For non-tax income and capital receipts we assume an MPC of zero as these comprise primarily of dividend income from the central bank, or state-owned enterprises, or from asset sales, which should have limited impact on real economy spending.

Exhibit 13: Summary of our MPC assumptions for different revenue and spending items over time

MPC assumptions												
	Expenditure							Revenue				
Year	Subsidy	Rural	Urban	Welfare	Transfer	Other revenue expenditure	Capital expenditure	Corporate tax	Income tax	Indirect tax	Non-tax revenue	Capital receipts
1st year after policy change	0.0	0.0	0.0	0.0	0.0	0.0	0.0	-0.4	-0.3	-0.3	0.0	0.0
Year of policy change	1.0	0.9	1.0	1.0	0.8	1.0	0.6	-0.5	-0.4	-0.5	0.0	0.0
Total	**1**	**0.9**	**1**	**1**	**0.8**	**1**	**0.6**	**-0.9**	**-0.7**	**-0.8**	**0.0**	**0.0**

Source: Goldman Sachs Global Investment Research

We follow the Hutchins Center approach, and compute the fiscal impulse, relative to a counterfactual that assumes that various government spending, and revenue categories grow in line with potential GDP. We use our potential growth estimates from our previous study (Discovering India's potential), and then we calculate how actual government spending, transfers and revenue deviate from these counterfactual estimates. We multiply the deviation of fiscal outcomes from the potential GDP based counterfactual, with our marginal propensity estimates, to derive contribution of changes in government spending and revenues to GDP growth, and then sum across categories to calculate the aggregated contribution. We term the aggregated contribution as our measure of "fiscal impulse" (or change in the stance of the fiscal policy) to assess whether the policy adjusted for economic cycle is expansionary or contractionary.

Appendix 2

Details of some of the major schemes of the central government:

PM Housing scheme (PM Awas Yojana): The PM housing scheme was launched in June 2015 to make housing affordable for Indian citizens. In the urban areas the scheme is executed under the Ministry of

[8] The MPC is an estimate of how much of an incremental INR in personal disposable income earned by households is spent on final goods and services.

[9] The Marginal Propensity to Invest is an estimate of how much of an incremental INR of post-tax earnings by firms is spent on additional investment projects.

[10] See Chinoy, 2016; RBI Exploring The Slowdown, 2002; Raj, 1962;

[11] Growth Multipliers are defined as 1/(1-MPC). Thus a multiplier of 2.5 implies an MPC of 0.6 for capital expenditure

Housing and Urban Affairs, while in the rural areas it is executed by the Ministry of Rural Development. Under the rural housing scheme construction of 29.5mn houses has been sanctioned since 2016 and out of those 26.1mn houses have been built. Under this scheme financial assistance of INR 0.12mn is provided to the beneficiary for construction of houses in the plains while INR 0.13mn is provided in the hilly areas.

Under the urban housing scheme, construction of 11.8mn houses has been sanctioned since 2016) and out of those 8.4mn houses have been built till date. Under this scheme a maximum subsidy of INR 0.23-0.27mn on home loan interest is provided depending upon the income group of the beneficiary. The Prime Minister recently announced the construction of additional 30mn houses under the housing scheme which includes construction of 20mn houses in the rural areas and 10mn in the urban areas.

PM Free electricity scheme (PM-Surya Ghar: Muft Bijli Yojana): The cabinet on 29th February 2024 approved a package of INR 750bn to promote solar rooftop installation in India over the next five years. Under this scheme the central government would provide a maximum subsidy of INR 78,000 for the installation of a 3 kilowatt (kW) system. The remaining cost would be borne by the household. The subsidy gets credited into the bank account of the beneficiary within 30 days of feasibility approval from the distribution company.

PM Farmer assistance programme (PM Kisan Samman Nidhi): PM farmer loan assistance programme is a central sector scheme launched in February 2019 to provide financial assistance worth INR 6000 to small and marginal farmers. The amount is transferred in three equal installments, every 4 months with the amount being directly credited into the bank accounts of the beneficiaries without the involvement of middlemen.

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Reg AC

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