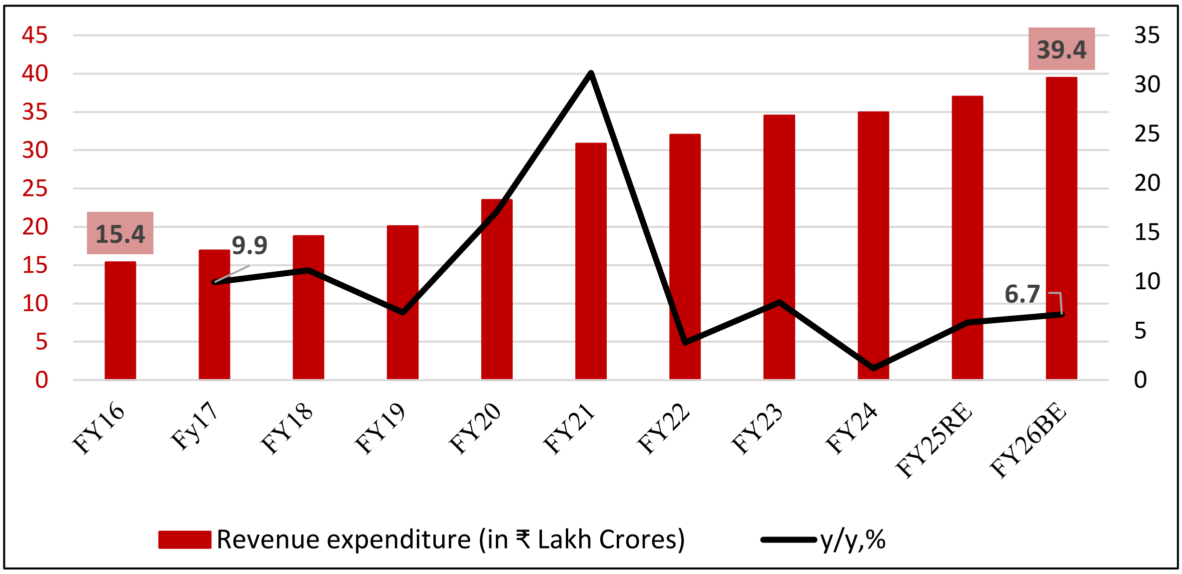
Union Budget impact on Banking sector

Union Budget 2025-26 has attempted to achieve a fine balance between growth and fiscal consolidation objectives. By estimating fiscal deficit at 4.4% the Budget has attempted to stick to the fiscal glide path though there is a slight uptick in borrowing numbers compared to the previous Budget. There is focus on agriculture, manufacturing, MSMEs, start-ups, ease of doing business and giving some respite to the salaried taxpayers by tweaking tax slabs and hiking taxable income thresholds. However, public capex share in GDP remains flat for FY26 though in absolute terms the trend is on the upside over the years.

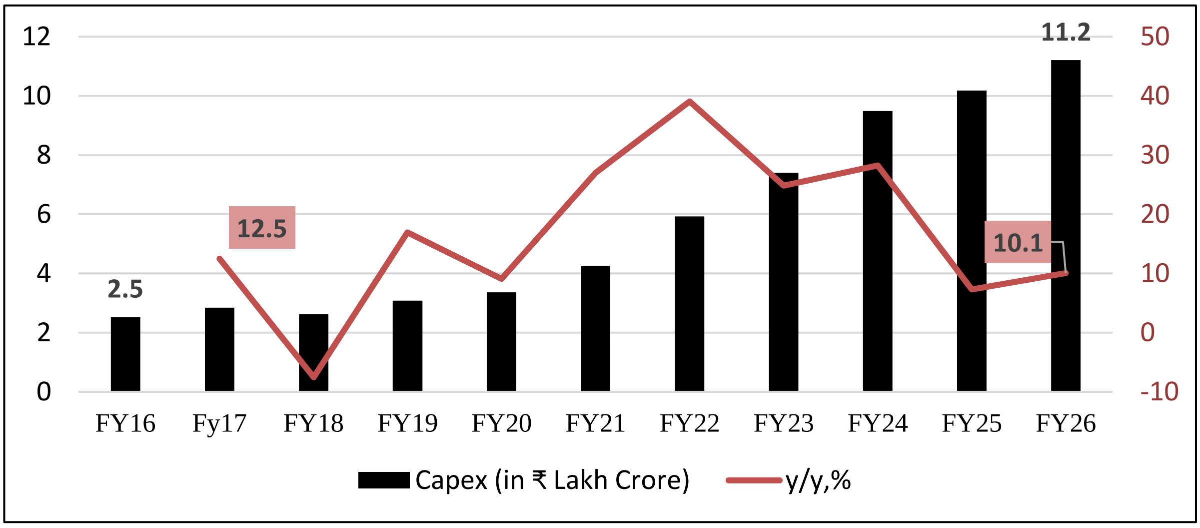
The expenditure profile of the Centre over the past decade is as shown below.

Fig 1: Revenue Expenditure



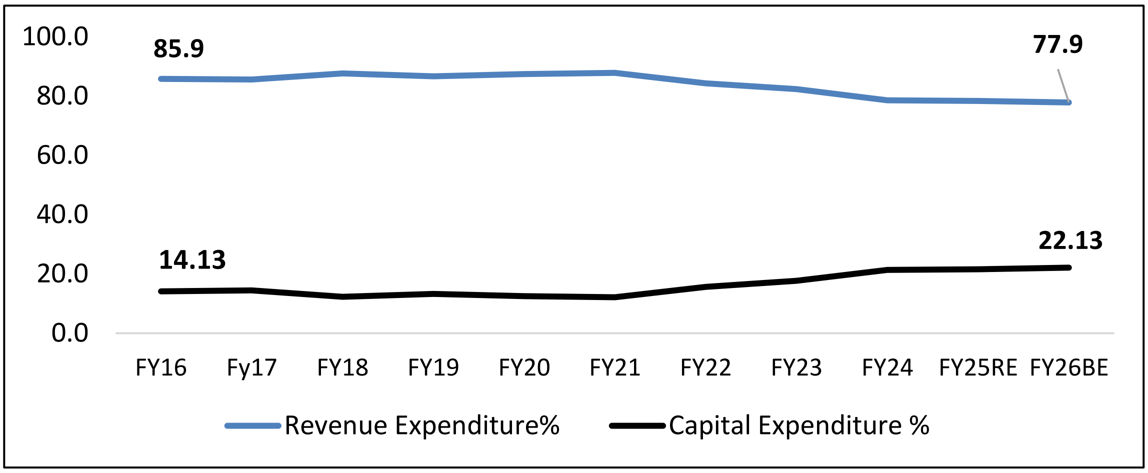
Source: Union budget documents

Fig 2: Capital Expenditure



Source: Union budget documents

Fig 3: Revenue Expenditure & Capital Expenditure in total



Source: Union budget documents

Capital expenditure has been rising at a faster pace than revenue expenditure, which has been experiencing almost flat growth since FY22. Revenue expenditure is incurred for salaries and pensions, while capex growth denotes public investment in infrastructure which has a multiplier effect on employment and growth. Since FY16, the share of revenue expenditure in total expenditure declined from 86% to 78% but capex share increased from 14% to 22%, implying capex growth has been achieved by compressing revenue expenditure - a sign of fiscal prudence.

Along with central government capex, states are granted interest free capex loans for a period of 50 years. This practice has been continued in FY26 budget also by earmarking Rs 1.5 lakh crore.

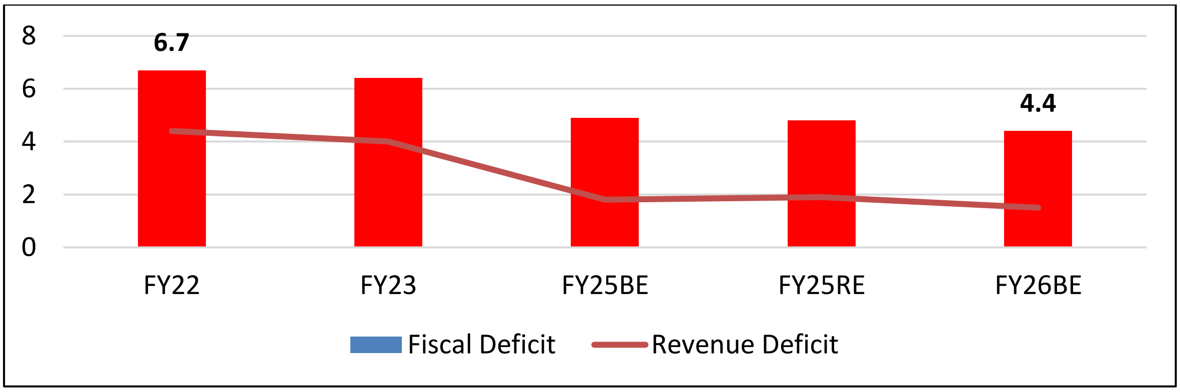
Table 1: Budget Arithmetic

Rs Lakh Cr, %	FY25 RE	Y/y, %	FY26BE	Y/y, %
Net Tax Revenue	25.5	9.8	28.4	11.0
Non Tax Revenue	5.3	32.4	5.8	9.8
Non Debt Capital Receipts	0.6	(1.3)	0.8	28.0
Total Revenue	**31.4**	**12.8**	**35.0**	**11.1**
Revenue Expenditure	36.9	5.8	39.4	6.6
Capital Expenditure	10.2	7.3	11.2	10.0
Total Expenditure	**47.1**	**6.1**	**50.6**	**7.4**
Fiscal Deficit %	**4.8**		**4.4**	
Nominal GDP Growth	**9.7**		**10.1**	

Source: Budget documents

The fiscal arithmetic shows an improvement in the quality of the exchequer with net tax revenue growing higher than nominal GDP which shows that tax cuts are not expected to make any serious dent on tax revenues. However public capex growth at 10% is still modest going by the Viksit Bharat 2047 vision.

Fig 4: Fiscal & Revenue Deficit (%)



Source: Union budget documents

Steady adherence to fiscal glide path

The budget proposed to strictly stick to the fiscal glide path announced in FY22 Union Budget. The restraint in revenue deficit, driven by fall in revenue expenditure as a share of total spending contributed to fiscal discipline. Government has also announced the intent to reduce central government debt to GDP to 50% by 2031.

The Government debt-GDP ratio is 57.1% as per FY25RE and estimates it to be 56.1% in FY26, thereby targeting a 100 bps reduction every year. Going by this logic by 2031-32, the target of 50% would be achieved. However, State governments also have to ensure similar pace of debt reduction because rating agencies look at the combined debt -GDP ratio of Centre and states to assess a nation's fiscal health.

Capex outlays for various ministries

Table 2: Capex Outlays

(₹ Lakh Crore)	FY25 RE	FY26BE	Share FY25RE	Share FY26BE
Road transport & highways	2.72	2.72	26.7	24.2
Defence	1.71	1.92	16.7	17.1
Railways	2.52	2.52	24.7	22.5
Communications	0.85	0.52	8.3	4.6
Housing & urban affairs	0.29	0.37	2.8	3.3
Total	**10.20**	**11.21**		

Source: Budget documents

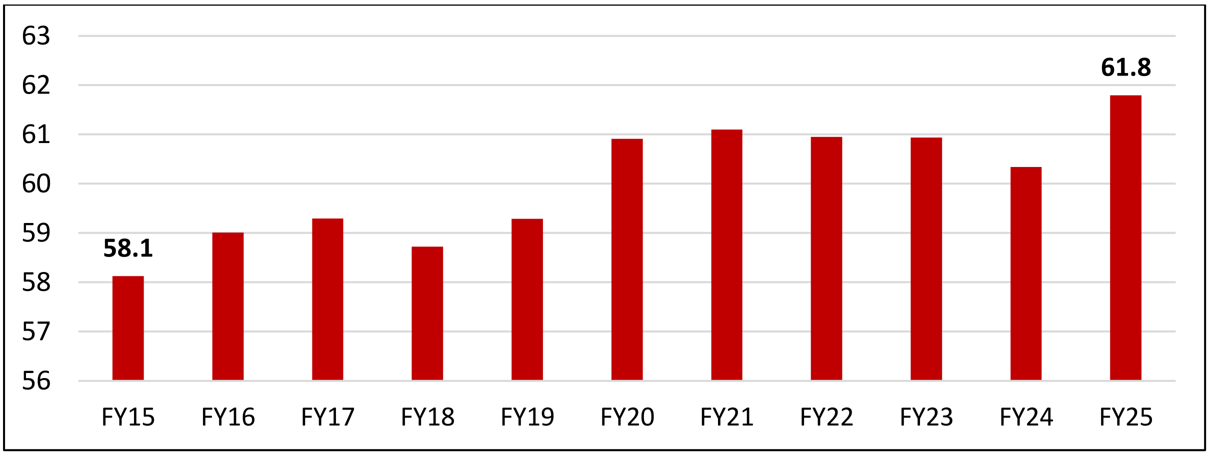
Capex outlay for road transport and highways, railways and telecommunications has witnessed a dwindling share in the total capex outlay in FY26BE compared to FY25RE though an increase is seen in defence and housing capex outlays. However, railways as well as transport still occupies the biggest share of capex outlay which augurs well for steel and cement segments. Increase in housing capex is also positive for steel, cement and construction sectors.

Effort to augment consumption

The budget has made annual income up to Rs 12 lakh exempt from income tax and tweaked tax slabs by adding more so that only an annual income above Rs 24 lakhs attracts the 30% tax slab in the new regime. This was with the aim to boost consumption.

The share of consumption in GDP at constant prices (base year 2011-12) has fallen after a peak of 58% in FY22 and is estimated to touch 56.3% in FY25 mainly due to the pickup in rural demand in the second half though urban consumption continues to lag. The tax changes are expected to add Rs 1 Lakh of disposable income and it is premised that this will augment consumption. However, consumption share in GDP at current prices has been one of the highest in FY25 as this is not inflation adjusted.

Fig 5: Consumption % to GDP at Current Prices



Source: NSO First Advance Estimates, CMIE

However, assuming the marginal propensity to consume for urban India between 0.6 to 0.7, Rs 60,000 to

Rs 70,000 Cr would be probably be spent on consumption out of Rs 1 lakh crore and the impact on GDP would be to the extent of 30-40 bps. This might be even lower if taxpayers use the additional income to pay off debt as the debt to GDP ratio of households have risen from 36% to 43%.

It is also to be noted that among up to Rs 12 lakh bucket those earning up to Rs 7.5 lakhs are not paying taxes presently due to a slew of rebates and the current changes will impact only those earning between Rs 7.5 to 12 lakhs. Viewed in this perspective the actual impact on consumption could be lower than expected.

Impact of various measures.

Table 3: Budget Announcements & Impact

	Announcement	Impact
1.	**Agriculture** • To facilitate short term loans for farmers, fishermen and dairy farmers enhanced loan of ₹5 lakh under interest subvention KCC scheme. • 5-year mission to facilitate improvements in productivity and sustainability of cotton farming	These measures will help to revive the agri GDP. Economic Survey has called for 5% growth in agriculture output as a part of achieving our potential rate of growth. Improve productivity will not only improve farm output but also bring down food inflation. There are 77.8 million KCC accounts with a total outstanding of Rs 9.6 lakh cr. The hike in limit from Rs 3 lakh to Rs 5 lakh impacts 10% of total KCC accounts and the impact on banks would not be heavy.
2.	Infrastructure and public capex: • Capex spend is budgeted to increase from Rs 10.2 Lakh Cr (FY25RE) to Rs 11.2 lakh Cr in FY26. Rs 1.5 Lakh Cr interest free loan to states for 50 years finds a mention yet again. • Asset monetization plan 2025-30 launched to plough back capital of Rs 10 lakh Cr in new projects. • Urban challenge fund of Rs 1 lakh crore to promote cities as growth engines. • SWAMIH Fund-2 Rs 15,000 crore for expeditious completion of one lakh dwelling units through blended finance.	The Union budget 2025 has provided an outlay of Rs 11.2 lakh Cr towards public capex against Rs 10.2 lakh Cr in FY25. Though capex is rising capex to GDP ratio has stagnated at 3.4%. The quality of fisc, however, is improving as the share of capex in total expenditure is steadily rising while that of revenue expenditure is declining. SWAMIH fund 2 will give a boost to affordable housing which is a positive for construction and cement industry. Affordable housing loan share in total home loans for industry have been declining.
3.	NaBFID to set up a 'Partial Credit Enhancement Facility' for corporate bonds for infrastructure.	Partial credit enhancement facility for corporate bonds will help rejuvenate the corporate bond market which will help easier fund raising by corporates, a longstanding demand for the past 20 years. However, success of the scheme depends on investor appetite as regulatory norms do not permit major players like insurance and pension funds to invest in papers rated below AA. So only if the low rated issuers get a rating upgrade, the scheme will take off.

<table>
<tr><td>4.</td><td>FDI limit for the insurance sector will be raised from 74 to 100 per cent for those investing full premiums in India</td><td>100% FDI in insurance is aimed at enhancing insurance penetration in the country which the Economic Survey had also highlighted as a necessity. It is now only 3.7% of GDP.
However, Indian insurance model is a bancassurance model for health/general insurance and agency model for life insurance. If foreign players wish to enter the space, they will have to re-work their business models which might not be easy. Inorganic growth is a possibility. If it succeeds, competition will lead to premiums coming down.</td></tr>
<tr><td>5.</td><td>Regulatory reforms
High level Committee of regulatory reforms to be set up.
The Finance Stability and Development Council (FSDC) to evaluate impact of the current financial regulations and subsidiary instructions along with a framework to enhance their responsiveness and development of the financial sector.
Jan vishwas Bill 2.0 to decriminalize more than 100 provisions in various laws.</td><td>These measures are aimed at developing a comprehensive and overarching regulatory framework which will take a closer look at all financial sector regulations by way of inter-regulatory conversations to be spearheaded by FSDC which is the supervisor of all regulators.

De-criminalisation of provisions will help in ending enormous litigation and should be seen as not only people centric but also as an ease of doing business measure.</td></tr>
<tr><td>6.</td><td>Rationalisation of customs duties in industrial goods like lithium-ion battery, open cell for LED TV, textile looms. Also 36 life-saving drugs/medicines have been added in exemption list, 6 medicines in the 5% duty list.</td><td>These measures will boost consumption of white goods like mobile phones as they could turn cheaper and this may also reduce inflation. Inclusion of more lifesaving drugs and medicines in exemption list will reduce out-of-pocket hospitalization expenses.</td></tr>
<tr><td>7.</td><td><u>MSME sector focus measures</u>:<table>
<tr><th></th><th>Inv current</th><th>Inv revised</th><th>Turnover current</th><th>Turnover revised</th></tr>
<tr><td>Micro</td><td>1</td><td>2.5</td><td>5</td><td>10</td></tr>
<tr><td>Small</td><td>10</td><td>25</td><td>50</td><td>100</td></tr>
<tr><td>medium</td><td>50</td><td>125</td><td>250</td><td>500</td></tr>
</table>Credit guarantee cover hiked-5-10 Cr for MSEs & to Rs 20 Cr for start ups.</td><td>The revised limits will enable more enterprises in the unorganized sector to be classified as MSMEs which will help them access to easier working capital limits from financial institutions at a lower cost. MSMEs are vital as they generate 45% of exports.</td></tr>
<tr><td>8.</td><td>To develop a national framework for Global capability Centres to guide states to set up such centres in Tier 2 cities.</td><td>Setting up of global capability centres will definitely will help to harness India’s comparative advantage in the services sector as services exports are currently more than $400 billion annually.

However, this also implies that there will be lot of data centres which will be set up in India and their electricity and water requirements will be huge. India will need to constantly invest in energy and water resources and we may find it difficult to reduce dependence on fossil fuels.</td></tr>
</table>

9.	Limit on Tax collected at source (TCS) on foreign remittances hiked from Rs 7 lakh to Rs 10 lakh and no TCS to be levied on forex remittance for educational purposes	This will provide a boost to the travel and tourism industry as overseas travel could see a pick up. This is also beneficial to the airline sector and those travelling abroad for medical treatment. However, as the annual LRS limit is fixed at $250.000 the hike in TCS from Rs 7 lakhs to 10 lakhs is very small.
10.	Introduction of a scheme for determining arm's length price of international transaction for a block period of three years.	This relates to transfer pricing norms. Determination of arm's length price for a 3-year period will provide more certainty, clarity and transparency in international taxation efforts.
11.	Tax deduction limit for senior citizens doubled from ₹ 50,000 to ₹ 1 lakh. The annual limit of ₹ 2.40 lakh for TDS on rent increased to ₹ 6 lakh	These measures will provide more disposable income to senior citizens and pensioners and aid consumption.
12.	Specific benefits to ship-leasing units, insurance offices and treasury centres of global companies which are set up in IFSC. Certainty of taxation to Category I and category II AIFs, undertaking investments in infrastructure and other such sectors, on the gains from securities.	These measures are expected to increase the attractiveness of GIFT IFSC as a global financial hub, rivalling London and Singapore. Taxation clarity to AIFs undertaking infrastructure investments will boost private capex and economic growth.
13.	<u>Other tax related measures</u> • TDS threshold on rent has been raised to INR 600,000 from INR 240,000 • Deadline for the incorporation of eligible start-ups to avail of the 3-year tax holiday within their first 10 years has been extended by 5 years • A new presumptive tax regime proposed for non-residents providing services or technology for setting up an electronic manufacturing facility	These measures will improve disposable income of those letting out rental property. The revised deadline for incorporation of start-ups will help more such players to be eligible for tax holiday which benefits the startup ecosystem. The new presumptive tax regime will encourage more players to set up electronic manufacturing facilities in India and also help in attracting global talent towards India.
14.	National manufacturing Mission focussed on small, medium and large industries to further promote Make in India proposed with an outlay of Rs 100 Cr. National Plan for toys is proposed to make India a global hub for toys production	These measures will help to increase manufacturing share in GDP from the current 15-18% which has been stagnant for over a decade.
15.	Tourism sector • MUDRA loans for homestays • Skill development programme for youth • Ease of connectivity through UDAAN scheme • PLI to states and streamlined e- visas and visa fess waivers.	This will augment growth in the tourism sector which is a major component of services sector occupying a share of close to 60% in GDP. Positive for overall GDP growth.
16.	A focus product scheme to be implemented in the footwear and leather sector to support component manufacturing, design capacity and machinery for production and to provide employment to 22 lakh people, with a turnover of Rs 4 lakh crore and exports worth Rs 1.1 lakh crore.	This is positive for manufacturing and employment generation and will also promote 'Atmanirbhartha' in these sectors.

Overall impact

- MSME sector will benefit from the revision of investment and turnover classification criteria by way of easier working capital loans.
- Reduction of basic customs duty on footwear, toys, lithium-ion batteries, etc. will reduce inflation
- Positive for the bond market as fiscal deficit is set to follow the glide path and market borrowing is stable
- Hike in income tax limits and slabs will increase savings/consumption
- Agri support measures for pulses, fruits and vegetables can bring down food inflation.
- Boost to tourism industry will augment service sector growth
- MSME, clean energy, tourism, food processing, education loans, affordable housing and other retail credit could be focus areas for the banking sector.

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