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Worsening Fiscal Situation FY 12

The fiscal situation in India appears to be worrisome as indicated by the official data released for the first half of FY 12 for the Central Government Accounts (CGA). The revenue position of the government up to H1 FY 12 is in stark contrast to the same period last year. Government expenditure is also clearly out of line from the budget estimates (BE) and as a result of which the fiscal deficit as at the end of H1 FY 12 has already crossed 68% of the full year BE.

This report provides an overview of the revenue and expenditure position of the government and how much more it can worsen from here on.

I. Revenue Estimates

Government estimates have pegged the total revenue collections at Rs 8.45 lac Cr for FY 12, 78.6% of which is estimated to come from tax collections. Government's estimate of 18% growth in Net Tax Revenue in FY 12, though closer to the average net tax revenues growth seen in the last five years, was a bit optimistic given that global uncertainty continued and it would be difficult for India to continue to grow at its trend growth rate. While the government appeared optimistic on the growth front, on the inflation side too, they worked on the assumption that it will remain fairly under control.

The current fiscal began on a somber note as far as the government's revenues are concerned. Centre's net tax collections were down by 27% and 6% at the end of Apr-11 and May -11 compared to the same period last year. The lower growth can be largely attributable to the dismal corporate tax collections which usually contribute a very significant part to the Centre's net tax collections. (The Income Tax department was reported to have issued record amount of refunds in the current year). Corporate tax collections though improved from June-11 onwards but still remains below the target growth rate of 21.5%.

However other indirect taxes namely, customs, excise and service tax showed resilience as they continued to record double digit growth. Robust export and import growth seen at end H1 FY 12, (exports were higher by more than 52% while imports by 32% from the year ago levels) clearly support the strong customs duty collections.

Table 1 below shows the target growth which the government seeks to achieve in the current fiscal while Table 2 shows the actual position as at the end of H1 FY12.

Table 1: Government Revenues (in Rs. Cr)				
	BE 2010-2011	RE 2010-2011	BE 2011-2012	Growth
Gross Tax Revenue	746,651	786,888	932,440	18.5%
Corporation Tax	301,331	296,377	359,990	21.5%
Taxes on Income	128,066	149,066	172,026	15.4%
Wealth Tax	603	557	635	14.0%
Customs	115,000	131,800	151,700	15.1%
Union Excise Duties	132,000	137,778	164,116	19.1%
Service Tax	68,000	69,400	82,000	18.2%
Taxes on Union Territories	1,651	1,910	1,973	3.3%
less - Transfers to Funds	3,560	3,900	4,525	16.0%
Less - State's share	208,997	219,303	263,458	20.1%
Centre's Net Tax Revenue	534,094	563,685	664,457	17.9%
Source: CGA				

Table 2: Tax Revenue position at end H1 FY 12						
	Sep-11	Sep-10	Growth	(Apr-Sep) FY 12	(Apr-Sep) FY 11	Growth
Taxes						
Corporation Tax	75,767	64,073	18.3%	127,375	123,161	3.4%
Taxes on Income	21,530	16,758	28.5%	66,249	56,480	17.3%
Customs	11,679	11,365	2.8%	74,808	61,051	22.5%
Union Excise Duties	11,486	11,493	-0.1%	59,315	52,058	13.9%
Service Tax	7,515	5,381	39.7%	37,049	26,936	37.5%
Other Taxes	1,000	1,032	-3.1%	4,557	4,711	-3.3%
Gross Tax Revenue	128,977	110,102	17.1%	369,353	324,397	13.9%
less - Transfers to Funds	323	259	24.7%	1,448	1,204	20.3%
Less - State's share	18,818	14,928	26.1%	113,174	89,778	26.1%
Centre's Net Tax Revenue	109,836	94,915	15.7%	254,731	233,415	9.1%
Source: CGA						

Scenario H2 FY 12: Centre's Net Tax revenues registered growth of a little over 9% at the end of first six months of the current fiscal. Going forward, keeping in view the ongoing turmoil in Euro area, which does not appear to be resolving in a short time, the overall global growth outlook seems to worsening with each passing day. Low or negligible global growth will surely have a bearing on the Indian economy as on many other economies via various interlinkages. Therefore we assume that growth in tax revenues in H2 FY 12 could perhaps only be a little better from the trend seen in the first half of the fiscal. We have assumed growth @ 12% as scenario 1.

Though there is nothing much of substance to suggest that globally things will improve in the second half of FY 12, however we can still hope that domestic consumption theme will play out and revenue collections will not be alarmingly bad. Moreover the second half of the fiscal is usually a little better in terms of growth owing to festive and marriage season demand. Therefore on an optimistic note we assume that even if 18% growth in Net Tax revenue is not met, it could possibly be closer to 15% (scenario 2).

Budget FY 12 pegged the Non Debt Capital receipts at Rs 55,020 Cr, out of which Rs 40,000 Cr is estimated to come by way of disinvestment of government's equity stake in various state owned entities. However, apart from the stake sale in PFC at the start of the year which gave the government Rs 1145 Cr nothing much has happened in this space apart from postponing the ONGC FPO days before it was going to hit the market. The government has been deferring the stake sales citing market volatility as the main reason. However going forward one can only be cautiously optimistic on the market sentiment, if at all, and therefore we assume that not more than 50% of the estimated Rs 40,000 will be realized through disinvestment in FY 12.

Table 3 shows our estimates of the revenue position after taking into account the above mentioned scenarios.

Table 3: Fiscal Scenario Analysis (in Rs. Cr)

	Base Case	12% Growth	15% Growth
Tax Revenues	664,457	631,327	648,238
Non Tax			
Revenue (Int/Div/Profits)	125,435	125,435	125,435
Non Debt Capital			
Recoveries of loans	15,020	15,020	15,020
Disinvestment	40,000	20,000	20,000
Total Receipts	844,912	791,782	808,693

Source: STCI PD Research

II. Expenditure Estimates

Government's Non Plan expenditure was estimated at approx 65% of the total expenditure of Rs 12.16 lac Cr. Non Plan expenditure was estimated to reduce by 0.7% in FY 12 over last year however by end Sep-11 it registered a growth of over 14%, making it apparent that target growth is unlikely to be met. Subsidies remain a major area of concern as over 23% of the Non Plan expenditure is attributable to this segment. Within this segment, petroleum subsidy is likely to see a sharp upward revision as international crude oil prices (Brent) averaged $115.08 per barrel in the HI FY12 which is 48% higher from the corresponding period a year ago.

The balance 35% of the total expenditure is Plan expenditure which was estimated to grow at 11.8% in FY 12 but by end Sep-11 has reported a much lower growth of 4.8%. We assume that government shall continue to exercise tight control over its expenditure resulting into some savings, which will help in narrowing the fiscal gap, which at this point looks quite ugly.

Scenario H2 FY 12: The under recoveries of the OMC's is estimated at Rs 1,25,000 Cr in FY 12. The government approx. shares 35% burden of the under recoveries and accordingly this works out to be around Rs 43,750 Cr. As the government has already budgeted Rs 23,640 Cr, the balance Rs 20,110 Cr will be the additional payment that the government will have to bear.

Nominal Gross Domestic Product (GDP) for FY 12 was estimated at Rs 89.80 lac Cr at the time of presentation of the Union Budget, assuming a growth rate of 14% over the advance estimates of FY 11. The average WPI inflation so far (till Oct) has been above average at 9.6%, which though is expected to moderate from Dec-11 onwards mainly because of a favorable base. We can still assume an average inflation of close to 9% for FY 12. Therefore assuming that real GDP growth in FY 12 is closer to 7%, the nominal GDP works out to be 16%. The fiscal gap in Scenarios 1(12% growth) and 2 (15% growth) is worked out with 16% GDP growth over FY 11 revised GDP of Rs 73.07 lac Cr.

Table 4 below shows that the fiscal gap may widen to the range of Rs 55,000 -73,000 Cr above the budget estimate of Rs 412,817 Cr.

Table 4: Fiscal and GDP estimates (in Rs Cr)			
	FY 12 BE	**12% Growth**	**15% Growth**
Total Receipts	844,912	791,782	808,693
Total Exp	1,257,729	1,277,839	1,277,839
Non Plan	816,182	836,292	836,292
Plan	441,547	441,547	441,547
Fiscal Gap	412,817	486,057	469,146
% of GDP	4.6%	5.4%	5.2%
GDP FY 12	8,980,860	8,476,108	8,476,108
Source: STCI PD Research			

We are reasonably optimistic that the government will keep a tight leash on its expenditure while on the revenue side though 18% growth in tax revenue appear difficult, we may end up in the range of 12-15% growth aided by indirect tax collections (mainly customs duty). The fiscal slippage could be restricted to approx Rs 55,000 Cr over and above Rs 412,817 Cr estimated at the time of budget.

III. Funding the Fiscal Gap

The funding of Rs 412,817 Cr of fiscal gap estimated at the time of budget was scheduled to be funded as shown in Table 5. Accordingly ahead of the beginning of FY 12 gross market borrowing worth Rs 417,128 Cr was announced by the government. However towards the end of H1 FY 12, the government announced an additional Rs 52,800 Cr citing shortfall under certain financing heads like small savings etc. However government maintained that this additional borrowing of Rs 52,800 Cr is only a substitution of one form of funding through another and therefore kept its fiscal deficit target unchanged at Rs 412,817 Cr. Table 6 shows the original market borrowing announced at the beginning of FY 12 and just before the beginning of the H2 FY 12.

Table 5: Funding of Fiscal Deficit (in Rs Cr)	
	BE FY 12
Fiscal Deficit	**412,817.00**
Less	
(i) Securities against small savings	24,182.46
(ii) State Provident Funds	10,000.00
(iii) NSSF	94.21
(iv) Others	(13,960.10)
Total (I to iv)	20,316.57
Govt. Cash Balance	20,000.00
External Finance	14,500.00
Market Borrowing through	358,000.43
- Dated securities	343,000
- Short term- T-bills	15,000
Source: CGA	

Table 6: Market Borrowing (in Rs Cr)	
Beginning of FY 12	
Gross Mkt Borrowing announced	417,128
less repayments	74,128
Net Mkt borrowings through dated securities	343,000
Short Term T-bills	15,000
End of H1 FY 12	
Additional Mkt Borrowing	52,800
Gross Mkt Borrowing	469,928
less repayments	74,128
Net Mkt borrowings	395,800
Source: RBI, STCI PD Research	

IV. Concluding Remarks

Going by the fiscal gap as projected in Table 4, and taking into account the additional borrowing as mentioned in Table 6 and hence the revised gross market borrowing of Rs 469,928 Cr, it appears quite likely that there may be further funding requirement of atleast Rs 50,000 Cr in the coming months in an optimistic scenario.

However the additional fiscal gap may not entirely be funded through government securities as that may be beyond the absorptive capacity of the market participants. A large part of the additional gap may be funded through short term securities like T-Bills or Cash Management Bills. Any additional borrowing through dated securities could be restricted to not more than Rs 20,000 Cr and the balance gap may be funded through increased T-bills and/or Cash Management Bills issuance.

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