

Union Budget FY27 Preview: Govt. likely to meet fiscal deficit target at 4.4% of GDP in FY26; debt target, govt. borrowing, capex to be in focus

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UB FY27 Preview I: Shift in anchor to medium-term debt consolidation and other factors influencing the fiscal math

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Focus on debt consolidation

- In the Union Budget for FY27, the government will shift its fiscal anchor from annual deficit targets to medium-term debt consolidation. In the Budget for FY26, the government had set the fiscal deficit target at 4.4% of GDP. In terms of debt, the target was 56.1% of GDP.
- In the statement of fiscal policy under the FRBM Act 2003, the Budget for FY26 set a glide path for the debt ratio to ease to 50+/-1 per cent by FY31 and constructed scenarios by degrees of fiscal consolidation and under varying nominal GDP growth rates. Despite the new anchor, markets will watch out for the implicit fiscal deficit target for FY27.
- In Apr-Nov FY26, the Centre's fiscal deficit was at 62% of BE vs. 52% of FY25BE in FYTD-FY25. Despite the accelerated pace, the government is expected to meet its fiscal deficit target for FY26. The expected shortfall in tax revenues due to GST tax cuts and slower nominal growth is likely to be offset by spending undershoot, particularly on revenue side.

Factors influencing fiscal math

- Some of the factors that are likely to influence the fiscal math include:
  - **Nominal GDP and series update:** Despite slower growth as per FAE, nominal GDP was largely in line with BE in absolute terms at ~Rs.357tn. The GDP series is undergoing revision in its base year and methodology and is slated for release in end-Feb. The new series could impact the fiscal math, though clarity will emerge only post the Budget.
  - **Devolution to States:** Under the 15th Finance Commission that was effective FY22-26, the share of States in the Centre's divisible pool of taxes was pegged at 41%. The 16th Finance Commission has submitted its report to the government that will determine for FY27-31 – central tax devolution, principles for grants-in-aid to States, among other factors. This will influence the Centre's net tax revenues.
  - **GST Compensation Cess:** In the backdrop of phasing out of GST compensation cess, the government introduced "Health and National Security Cess" on pan masala and an excise duty on tobacco and products. These will be in addition to the GST tax rate of 40%. But the new cess will not be a part of the divisible pool and thereby provide some cushion against the potential revenue loss to the Centre from GST rate cuts, effective Sep-2025.
  - **8th Central Pay Commission:** The revisions to government employee salaries and pensions under the 8th CPC will be effective 1-Jan-2026 but are expected to be paid with arrears starting mid-2027. This could entail larger outgo under revenue spending in FY28 and also possibly, in FY29, thereby narrowing the fiscal space for capital spending. It could prompt the government to maintain its focus on capex in FY27 Budget.

UB FY27 Preview II: Gross govt. market borrowing could be high, targeted support for priority sectors likely

Govt. borrowing

- In the Budget for FY26, the Centre had penciled net market borrowings from dated securities at Rs.11.5tn, and gross borrowings at Rs.14.8tn. But with mildly lower issuances announced in H2-FY26, gross borrowings will undershoot the BE. In FY27, redemptions are slated to rise to Rs.5.5tn, which could put upward pressure on gross borrowings, unless they are offset by switches or conversions to longer-term securities.

Non-tax receipts and disinvestment targets

- In recent years, high RBI dividends and lower-than-budgeted disinvestments have been among notable fiscal outcomes. These trends are likely to continue in FY27, though the RBI dividend could be lower year-on-year due to expected decline in foreign earnings amid low interest rates in most major economies and lower pace of FX sales than in FYTD-FY25.

Taxation and priority sector support

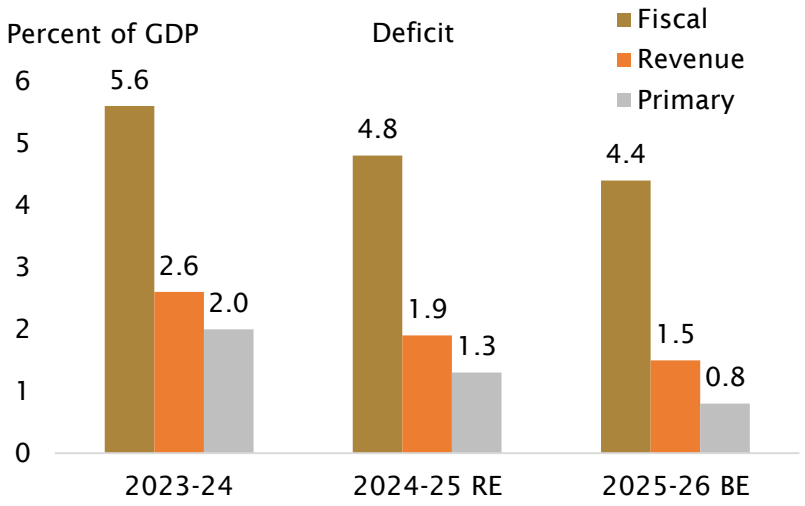
- Post the income tax relief announced in the Budget for FY26 and the recently implemented GST rate cuts, there is limited space for fiscal stimulus based on tax incentives in FY27. But there could be some changes along these lines:
  - The government could continue to rationalize the customs duty structure for more goods to correct for inversion and eliminate some of the non-tariff barriers to trade.
  - The government could announce targeted measures for priority sectors and also for exporters that have been reeling under pressure from steep US tariffs.
  - The New Income Tax Act (2025), effective from 1-Apr-2026, replaces the Income-tax Act 1961. The New Act simplifies language and removes outdated laws, among other changes. But by itself, the New Act does not have any impact on tax incidence, and will continue to incorporate the updates announced in the annual Union Budgets.

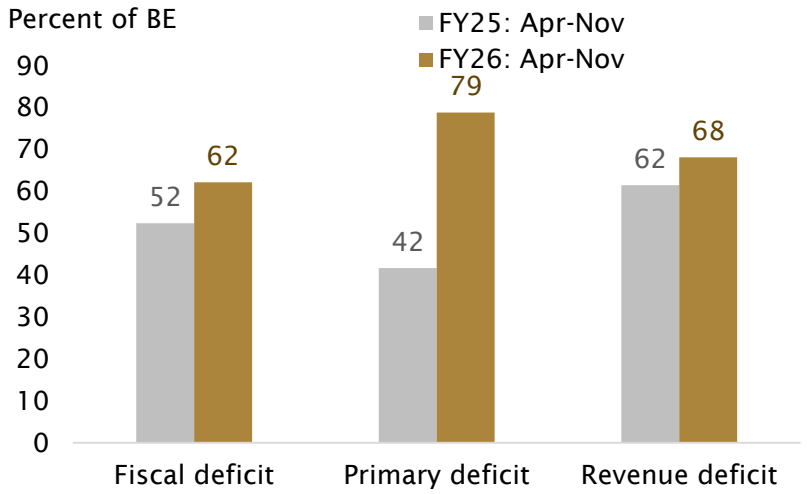
Structural reforms and governance issues

- In a major structural reform, the government notified four labour codes in Nov-2025, which consolidate 29 labour laws. The rules are yet to be finalized amid reports that 1-Apr-2026 could be the effective rollout date. The Budget could include guidelines around this, with market participants watching out for cues on next generation reforms related to any other factors of production, as was alluded to in the Budget for FY25.
- The Economic Survey FY25 noted deregulation as a catalyst for growth. But the Budget's concurrent proposal to set up a committee on regulatory reforms is yet to see the light of day. Any pointers in this direction would augur well for medium-term growth prospects.

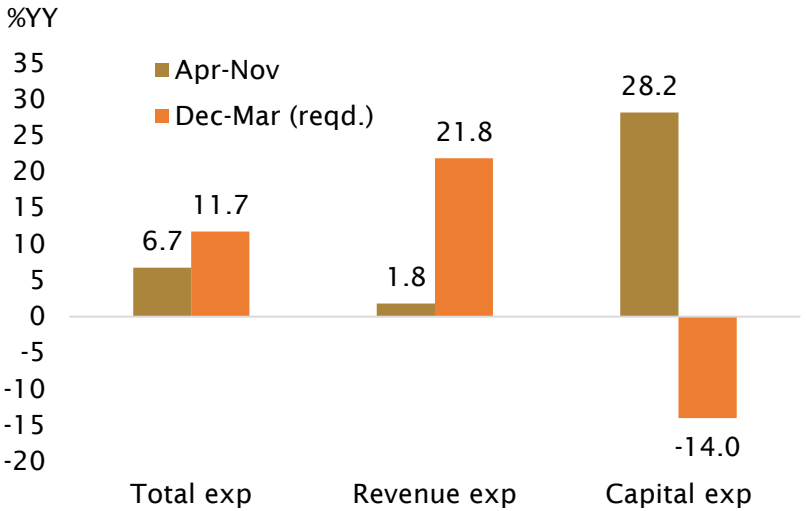
Govt. likely to meet fiscal deficit target of 4.4% of GDP, as spending undershoot could offset shortfall in tax revenues

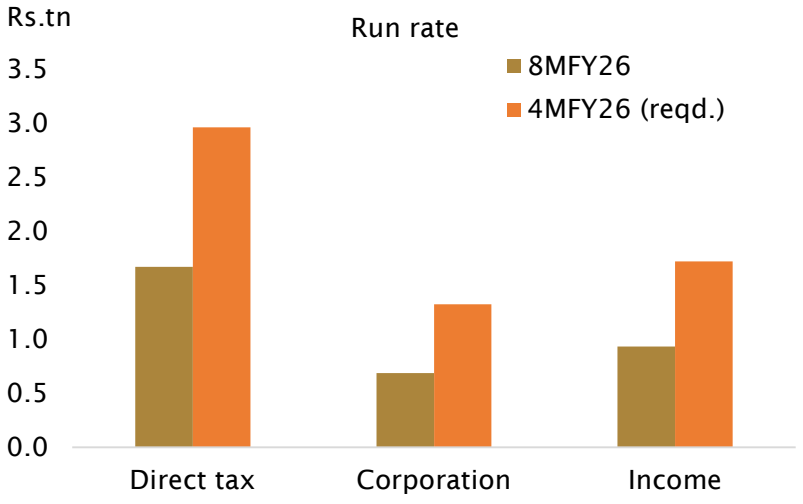
Government likely to meet fiscal deficit target of 4.4% despite higher deficit in Apr-Nov FY26 vis-à-vis FYTD-FY25





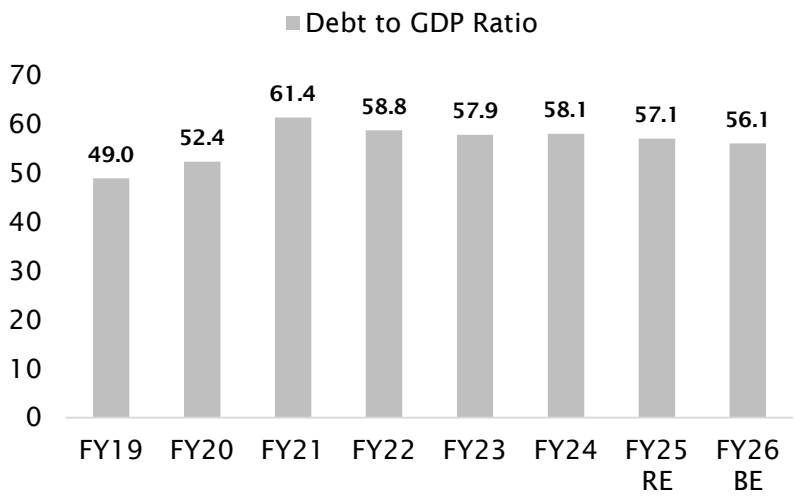
Less-than-budgeted revenue spending expected to offset shortfall in tax revenues

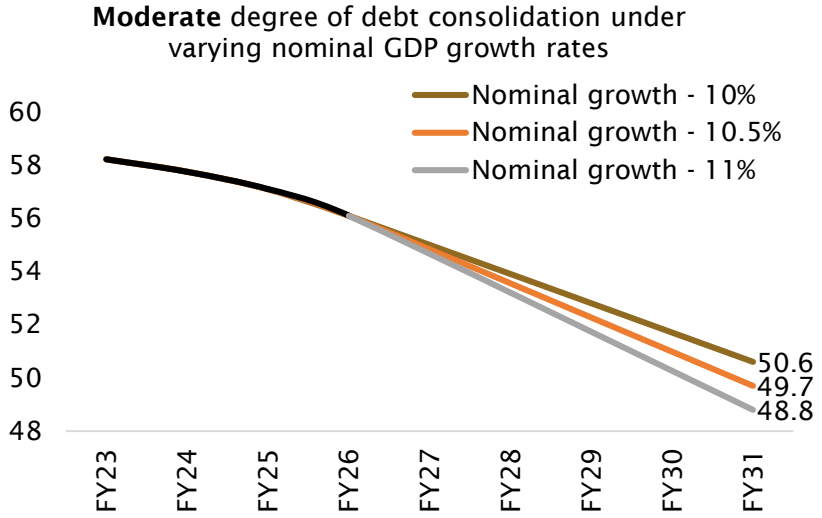




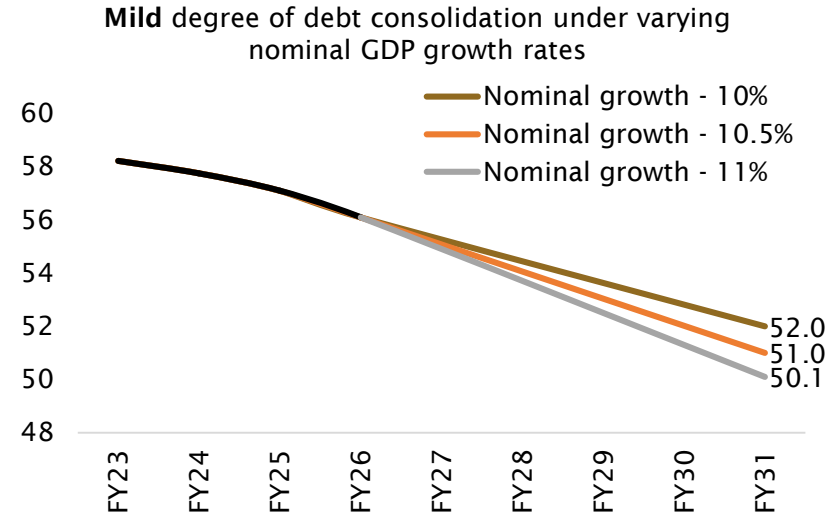
Markets will watch out for degree of debt consolidation budgeted for FY27

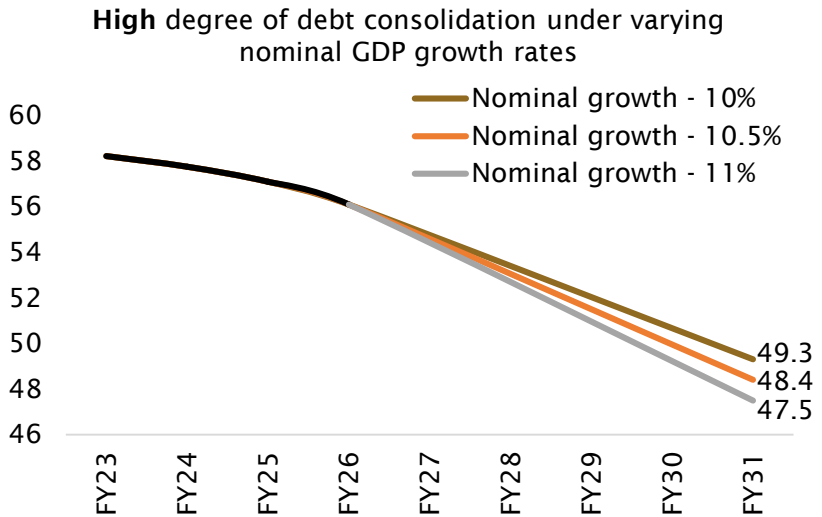
Debt for GDP ratio target at 56.1% for FY26; second chart shows scenario for moderate degree of debt consolidation





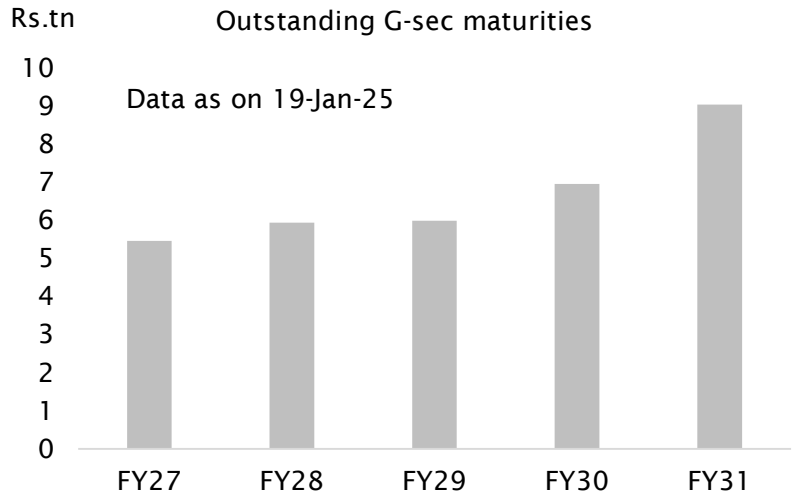
Scenarios under mild and high degrees of debt consolidation by nominal growth outlined in Union Budget for FY26





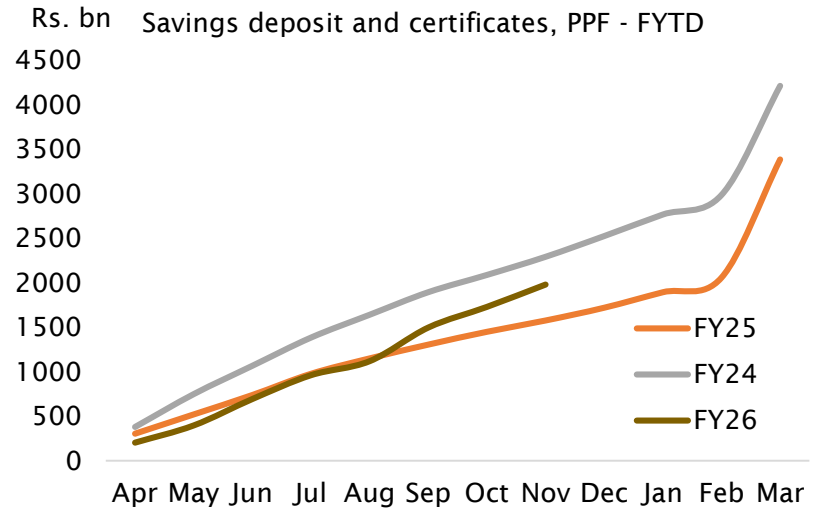
High redemption pressure in coming years could lead to increase in gross market borrowings

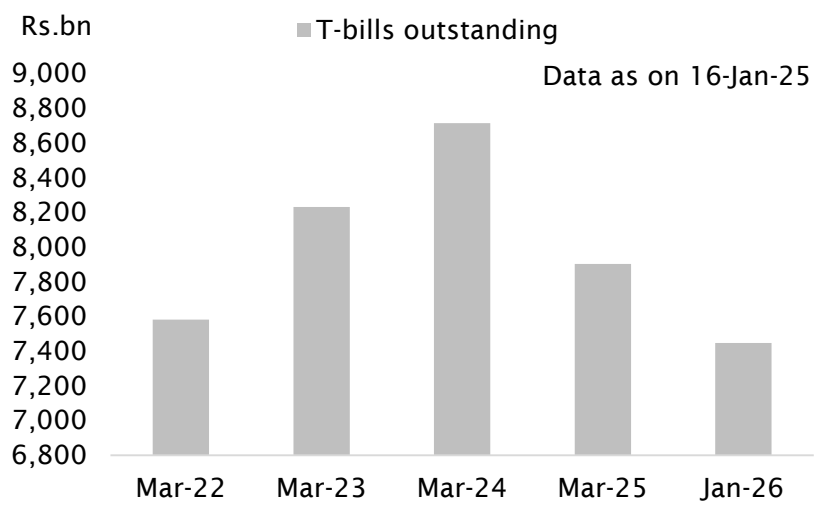
Redemption pressure to rise in coming years that could lead to increase in gross market borrowings



Rs.bn	FY23	FY24	FY25RE	FY26BE
Gross Market Borrowings	14210	15430	14007	14820
Net market borrowing	12178	12310	9545	11538
G-sec	11058	11778	10745	11538
T-bill/Short term	1120	532	-1200	0
Securities against small savings	3959	4514	4119	3434
State provident funds	51	51	50	50
Other receipts	835	-887	260	407
External debt	371	551	320	235
Draw Down of Cash Balance	-16	8	1401	25
Fiscal deficit	17378	16546	15695	15689

Surge in small savings as interest rates unchanged despite RBI repo rate cuts; o/s t-bills lower than in end-Mar 2025





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Ph: +91 22 4084 5000 • Fax: +91 22 4084 5052 • www.trustgroup.co.in