Will the Budget resurrect economic dynamism?

Rationalisation of direct taxes and relief to the salaried class must be the Finance Minister's top priority

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As India's growth engine slows, with GDP growth projected to decelerate to a four-year low of 6.4 per cent in FY25 from 8.2 per cent in FY24, the upcoming Union Budget will be a critical policy lever for reigniting growth momentum.

NSO's first advance estimates reveal some concerning trends — manufacturing growth slowing from 9.9 per cent in FY24 to 5.3 per cent in FY25; weakening investment momentum with gross fixed capital formation at a six-quarter low of 5.9 per cent in Q2 FY25; and tepid urban and rural consumption. Meanwhile, global headwinds, including subdued trade and geopolitical uncertainties, continue to strain India's export potential.

So the Finance Minister faces a complex fiscal challenge. With nominal GDP growth expected to reach only 9.7 per cent in FY25, below the FY25 Budget target of 10.5 per cent, managing the fiscal deficit will require a careful balancing act. The FY25 deficit target of 4.9 per cent of GDP may reach 5 per cent, making it crucial to maintain the fiscal glide path without compromising growth-enabling expenditure.

TAX RATIONALISATION

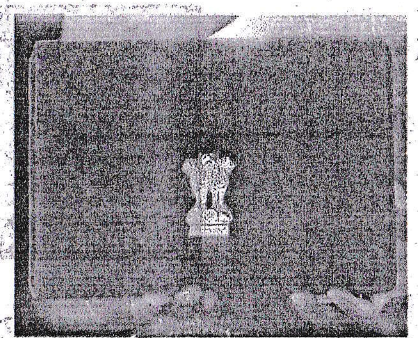
In such a context, the FM's first imperative will be to review and rationalise direct taxes. Despite reductions in corporate tax rates, SMEs and mid-sized firms face high effective rates that limit their global competitiveness. Rationalising tax rates for such firms, and adjusting slabs for inflation could spur reinvestment and expansion.

Also, for the crucial ₹15-50 lakh income segment, which forms the backbone of urban consumption, targeted relief — such as increasing the standard deduction limit; extending the HRA exemption limit to Tier 2 cities, recognizing their emergence as major economic hubs with rising living costs; and removing the ₹2 lakh cap on offsetting house property losses against other income — could boost retail spending and loan growth.

Such steps could reinvigorate private investment and revive consumption demand, which are linchpins for GDP growth.

Second, capital expenditure deserves heightened focus, too. With the Centre likely missing its FY25 target of ₹11.11 lakh crore by ₹60,000 crore, and a 14.7 per cent decline in government capital expenditure during April-October 2024, the Budget must take steps to reverse the twin slowdown in public and private investment.

This should include expanding the National Infrastructure Pipeline with time-bound execution targets; introducing tax-efficient infrastructure bonds to crowd-in retail investment; and establishing specialized credit guarantee schemes for infrastructure financing companies. Raising Section 80C limits for infrastructure-linked savings products and offering favourable depreciation regimes for new capital investments could also catalyse growth.



BUDGET. Tough options PTI

Third, India's external sector weaknesses warrant interventions, particularly as services exports emerge as a potential stabilising force amid currency and reserve pressures. While the Rupee's slide to nearly ₹87 against the US Dollar and $70 billion erosion in forex reserves are concerns, services exports offer a countervailing opportunity. Growing at a CAGR of 10.5 per cent, services exports are projected to reach $618 billion by 2030, marginally surpassing merchandise exports.

However, this growth is concentrated in software and IT services (56.2 per cent) and Other Business Services (33.2 per cent), with the US alone absorbing 70 per cent of IT exports.

The Budget should address such vulnerabilities by strengthening forex hedging facilities, providing tax incentives for companies diversifying into untapped segments like transport and financial services, and helping Indian firms capture more of the $1.8 trillion global Other Business Services market through targeted skilling initiatives and export-promotion schemes.

. Fourth, the Budget must substantially increase budgetary allocations to agriculture R&D, which can drive breakthroughs crop innovations, enhance climate resilience, and ensure food security.

Finally, the Budget must address the growing divergence between growth and employment generation. Labour-intensive industries like construction, textiles, tourism, and footwear need targeted support to create jobs and boost export revenues. Also, with female workforce participation critically low, gender-sensitive frameworks, such as formalising the care economy, are imperative.

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