BANKING ON KNOWLEDGE

Can India's upcoming budget maintain its fiscal prudence?

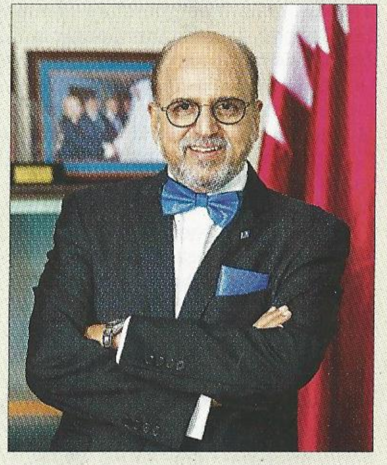
By Dr R Seetharaman

India's Finance Minister Arun Jaitley has a delicate task of balancing growth without compromising significantly on the fiscal prudence for its financial budget, which is due to be announced on February 1.

India's GDP growth rose 6.3% in the July-September period, compared with the three-year low of 5.7% growth in the April-June quarter and 7.5% in the year earlier.

The downside risks to growth faded post the demonetisation and GST, as the transformational steps announced by the government are long term positive and have been acknowledged by the International Rating agencies via sovereign rating upgrade by Moody's.

The country has inched up by 30 points to the 100th place for ease of doing business. IMF expects India's GDP growth to be at 7.4% in 2018, in



its World Economic Outlook Update, it also estimated that the Indian economy would grow by 7.8% in 2019, which will make the country the world's fastest-growing economy in 2018 and 2019.

The recent Indian Economic Survey expects FY '19 growth to be 7-7.5% vs 6.75% for FY '18. Agriculture, education, and employment will be areas of focus in the medium term, private investment is poised for growth and source of upside potential is exports sector.

India's upcoming budget assumes importance as this will be the last full year budget of the government before next year's Lok Sabha election.

As the oil prices have increased from lower levels of $26 per barrel to $66 per barrel, India's 10-year bond yields have hardened to 7.3% as India's oil bill is 30% of total imports. Jaitley has a complex task of managing any significant fiscal slippage. He has indicated fiscal deficit of 3.2%, and any significant slippage may further harden the bond yields and increase the cost of borrowing for the government, although a fiscal deviation of 20bps looks to be accepted by the market and is reflected in the Indian 10-year bond yields.

The current budget focus will be on increasing expenditure towards infrastructure, defence, power, roads, smart city development, job creation, increasing farmer's income and digitisation initiatives.

The government will look to incentivise the savings of common man. The IMF and international agencies have highlighted an urge towards strengthening the PSU banks. The government has already taken steps by announcing mega recap of $32bn for PSU banks. There has been an allocation of approximately $12.5Bn as first tranche of non-SLR bonds with a maturity of 10-15 years.

The ease in FDI norms for various sectors like aviation, construction, power exchanges and medical devices will attract long-term capital in the country.

The government is discussing to increase FDI of up to 49% in PSU banks and 100% in private banks. This is a logical step towards opening up the banking sector as it needs capital for expansion.

India needs to change its energy mix to insulate it from the rise in oil prices. The country is moving to promote gas usage in line with the commitment made at the Paris meeting on climate change, which aims to reduce India's carbon emission intensity by up to 35% from 2005 levels by 2030 and producing 40% of the power from non-fossil fuel sources by 2030. Natural gas is a good fit for decarbonising India's energy system. The government also wants to make India a gas-based economy and raise the share of natural gas in the energy mix to 15% from 6% in 2016.

India's import bill is inflated on account of increase in oil prices from $26 per barrel to $66 per barrel, which may not be sustainable for its high economic growth going ahead, so to sustain growth India has to change its energy mix, for which natural gas is a better choice.

Realignment of energy mix to natural gas will de-risk India's high reliance on oil and insulate the country's import bill from upward movement in oil prices. Qatar and India can jointly explore more synergies in this area, which will enhance bilateral trade relationships.

■ *Dr R Seetharaman is Group CEO of Doha Bank.*