

Economy

Public Finance

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RBI's bonanza to the central government

The RBI's surplus transfer of Rs2.1 tn to the central government was an upside surprise. This bumper transfer provides the government with the choices of a faster pace of fiscal consolidation and/or higher spending and/or lower taxes.

RBI announces a surplus transfer of Rs2.1 tn

The RBI has approved the transfer of Rs2.1 tn as surplus to the central government for FY2024. We expect this transfer to have stemmed mainly from (1) large interest income earnings on foreign and domestic holdings and (2) FX sales operations by the RBI. Noting the Indian economy's continued resilience and robustness in FY2024, the RBI increased the contingency risk buffer (CRB) to 6.5% (from 6.0% in FY2023).

Fiscal consolidation becomes easier

The surplus transfer of Rs2.1 tn is higher than that of FY2025BE of around Rs800 bn and market expectations of around Rs1.0-1.2 tn. The additional amount of around Rs1.3 tn over FY2025BE is around 0.4% of GDP. However, there could be a shortfall in divestment and telecom receipts that could partly offset gains from the surplus transfer. However, fiscal consolidation to the 4.5% GFD/GDP target by FY2026 is now easier for the government.

Central government has higher degrees of freedom

While adhering to the fiscal consolidation path is now relatively easier, there is space to alter the budgeted receipts and/or expenditure. The government can continue with its capex thrust by increasing allocations to roads, railways and defense (from their single-digit growths over FY2024RE). There is also room for the government to lower personal income taxes to boost consumption at the lower end of the tax pyramid. We expect the government to focus on higher capex and fiscal consolidation over any stimulus through tax cuts.

Favorable domestic cues to aid bond market sentiments

Domestic sentiments have lately turned quite favorable, amid (1) announcements of buybacks and (2) 1QFY25 T-Bill calendar lowered by Rs 600 bn. Meanwhile, liquidity conditions have tightened significantly due to slower government spending during the election period, even as currency leakage has been fairly tepid. We estimate the government's cash balance to have surged to around Rs6 tn this week (including the RBI transfer). We expect the comfortable fiscal position and surplus cash balances to provide room for further buybacks, thereby reducing the net G-sec supply, and further improving demand-supply dynamics. We expect liquidity conditions to improve from 2QFY25, led by (1) revival in government spending, (2) seasonal payback in currency in circulation and (3) likely RBI intervention to manage FPI debt flows. Although domestic factors are very conducive for a rally in bonds, we remain watchful for the possibility of sterilization of the FX intervention and upside to global yields, amid further delays in the US Fed rate cycle.

Summary of India's key macro metrics

	2023	2024E	2025E	2026E
Real economy				
Real GDP growth (%)	7.0	7.6	6.6	6.5
Nominal GDP growth (%)	14.2	9.1	10.8	10.7
CPI Inflation (avg., %)	6.7	5.4	4.5	4.2
Public finance				
Center's GFD/GDP (%)	6.4	5.8	5.1	4.5
Monetary policy				
Repo Rate (% eop)	6.50	6.50	6.00	5.50
SDF Rate (% eop)	6.25	6.25	5.75	5.25
CRR (% eop)	4.5	4.5	4.5	4.5
External sector				
Current Account Balance (% of GDP)	(2.0)	(0.8)	(1.1)	(1.0)
Brent crude oil price (avg., USD/bbl)	95.4	83.0	85.0	80.0
USD/INR (avg.)	80.3	82.8	83.1	84.0

Source: CEIC, Bloomberg, RBI, Kotak Economics Research estimates

Quick Numbers

The RBI's Board has approved the transfer of Rs2.1 tn to the central government for FY2024

Glide path to 4.5% GFD/GDP target is now relatively easier

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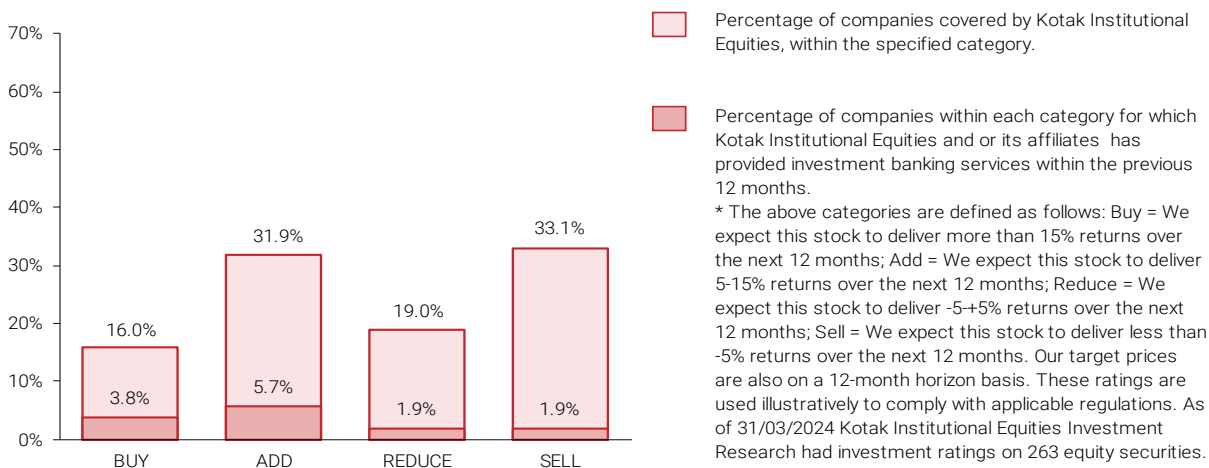
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