PNB GILTS LTD

Volume 18/2023-24
5th February 2024

ECONOMY & GILT WATCH

PNB GILTS LTD
(Subsidiary of Punjab National Bank)

INSIDE THIS ISSUE:

Budget FY 2024-25
Deeba Hasan
Vice President
deeba.hasan@pnbgilts.com

SDL Outlook
Anshul Arora
Sr. Vice President
a.arora@pnbgilts.com

Technical Outlook
Ashish Bansal
Vice President
a.bansal@pnbgilts.com

Interim Budget FY 2024-25: Fiscal Prudence at its Best

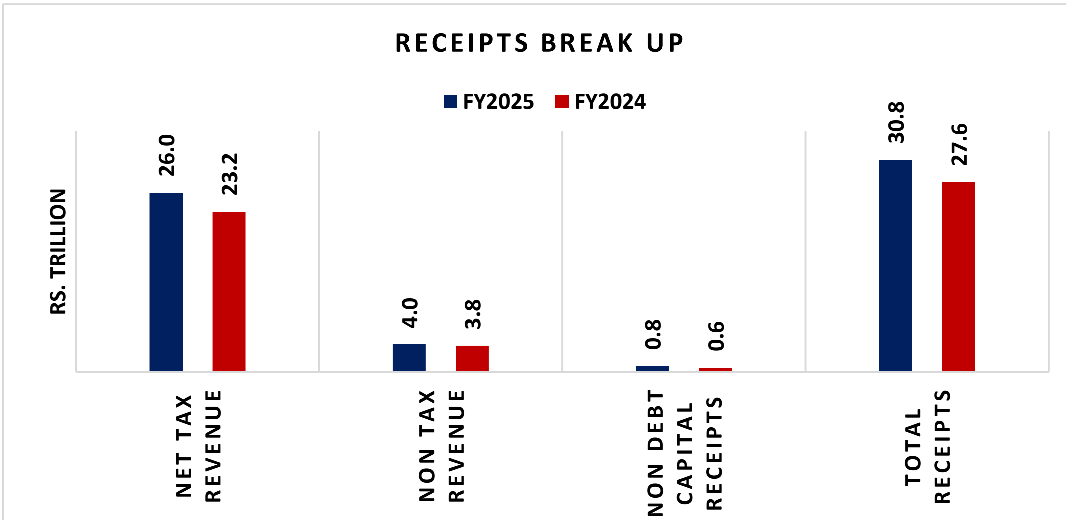
The interim Union Budget FY 2024-25 unveiled on 1st February 2024 was marked with a strong fiscal consolidation accompanied with a continuation of trend of improved quality of expenditure. The fiscal consolidation for FY 2024-25 announced came to be stronger than expected with FD to GDP target at 5.1 per cent as against revised estimate (RE) of 5.8 per cent for the current financial year. The sharply lower than expected gross market borrowing projection for FY 2024-25 was the key highlight of the budget, with borrowings pegged at ₹14.13 tn as against broader expectations of ~₹ 15-15.5 tn. Bond market was enthused by the positive announcement with respect to the fiscal contraction and lower borrowings, pushing the 10-year yield below 7.05 per cent. The term structure witnessed flattening as long end yields softened on account of tighter fiscal path envisaged for the upcoming year. In absolute terms, the fiscal deficit is projected to contract by 2.8 per cent to ₹16.85 tn in FY 2024-25 as against RE of ₹17.35 tn for FY 2023-24. The contraction in fiscal deficit is projected to be aided by a healthy growth in tax revenues. The nominal GDP, which forms the base for the FD to GDP ratio, has been projected to grow y-o-y by 10.5 per cent to ₹328 tn, which again is a reasonable assumption, with some downside risks. Other key deficit ratio, viz Revenue Deficit (RD) to GDP ratio is also projected to witness a meaningful contraction of 80 bps to 2 per cent with share of RD in FD projected to fall to 39 per cent in FY 2024-25 vis-à-vis 49 per cent in the current year. Fiscal discipline shown by the government is the hallmark of this year's budget, making achievement of 4.5 per cent FD target by FY2026 plausible, with only 60 bps consolidation required further.

Revenues: Tax Revenue to Stay Robust

Total revenues are projected to grow 11.8 per cent to ₹ 30.8 tn in FY 2024-25 as against RE of ₹ 27.56 tn in current FY. Revenue growth is expected to be led by continuation of robust growth in tax revenues. However, after a rather strong showing in FY 2023-24, gross tax revenue growth is projected to retract to 11.5 per cent in FY 2024-25 vis-à-vis 13 per cent in current year. Resultantly, tax buoyancy is placed slightly lower at 1.1 in FY 2025 as against 1.4 witnessed in FY 2024. Under direct taxes, both corporation and personal income tax growth is pegged at ~13 per cent, together forming 6.7 per cent of the GDP in FY2025 as against 6.5 per cent of GDP in FY2024. Under indirect taxes, GST collections are pegged at ₹ 10.7 tn, 11.6 per cent higher than RE for FY 2023-24. While Customs duty growth is pegged modestly at 5.8 per cent for FY 2025 (₹ 2.3 tn) on account of benign global trade environment, Union excise duties are projected to grow by 5 per cent to ₹ 3.2 tn in FY 2025. Broadly, net tax revenues are projected to lead the Centre's revenue growth, forming 84 per cent of total receipts. Non-tax revenue growth is projected to rise 6.4 per cent to ₹ 3.99 tn in FY 2025 as against ₹ 3.76 tn for RE FY 2024. Under non-tax revenues, government expects yet another year of healthy dividend and profit earnings in line with what was witnessed in FY 2024.

Healthy tax revenues are expected to continue to provide significant buffer in meeting the government's expenditure requirements

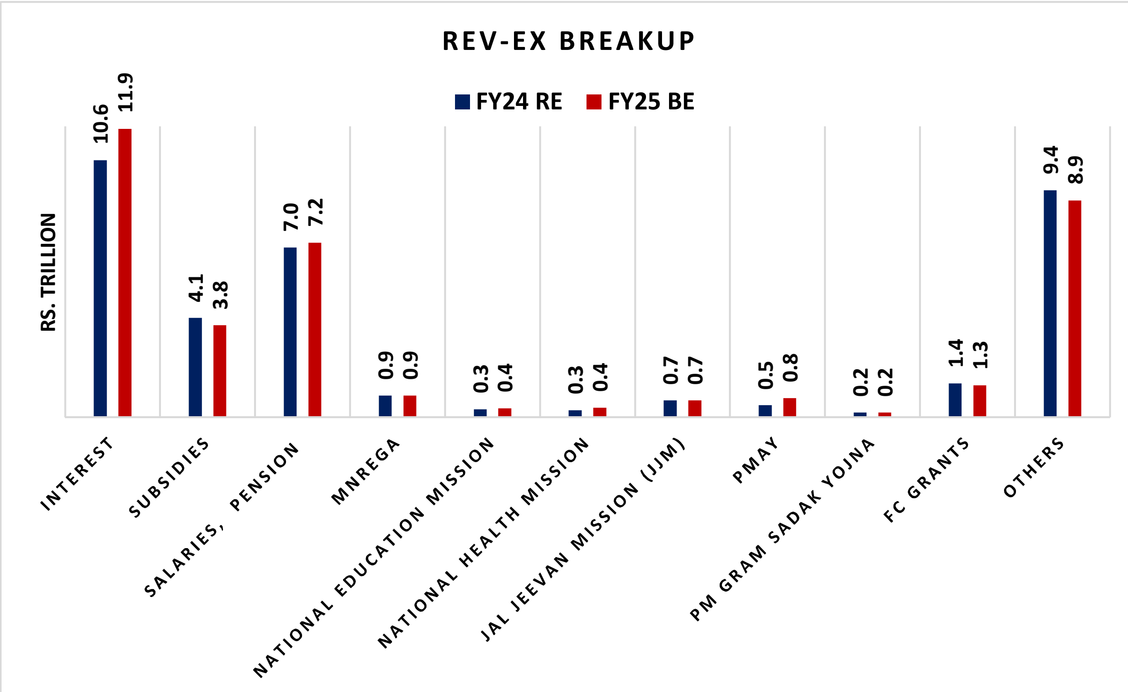
Of ₹ 1.5 tn projection of dividend and profit earnings in FY 2025, ₹ 0.48 tn are estimated as dividend earnings from PSE's and ₹ 1.02 tn from RBI, banks & FIs. Another key contributor in non-tax revenue is "Other Communication Services" with earnings budgeted at a healthy ₹ 1.20 tn for FY 2025 vis-à-vis RE of ₹ 0.93 tn for FY 2024. Under non-debt capital receipts, given muted disinvestment efforts in last two years, government has maintained low dependency on disinvestment for FY 2025, with target at ₹ 0.50 tn as against RE of ₹ 0.30 tn for FY 2024.



Expenditure: Tilt towards Cap-Ex continues

There is an effort to contain expenditure, which can be seen from slower projected growth for both Cap-Ex and Rev-Ex for FY 2025

Government emphasis on improving the quality of expenditure continues, with Cap-Ex growth pegged at 16.9 per cent while Rev-Ex growth is projected at 3.2 per cent. Nonetheless, there is an effort to contain expenditure, which can be seen from slower projected growth for both Cap-Ex and Rev-Ex for FY 2025. In absolute terms, Cap-Ex for FY 2025 is budgeted at ₹ 11.11 tn (3.4 per cent of GDP), whereas Rev-Ex is budgeted at ₹ 36.5 tn (11.2 per cent of GDP). A slower growth in Rev-Ex implies a lower Revenue Deficit for the year, with RD to GDP projected at 2 per cent for FY 2025 vis-à-vis 2.8 per cent as per RE for FY 2024. A meaningful contraction of ~8% in subsidies underpins the slower growth in Rev-Ex in FY 2025. Under subsidies, fertilizer subsidies are projected at ₹ 1.6 tn in FY 2025 as against ₹ 1.9 tn as per RE FY 2024. Food subsidy is also set to witness a modest decline of 3.3 per cent to ₹ 2.05 tn. On the other hand, interest payments are budgeted to rise by 12.8 per cent to ₹ 11.9 tn in FY2025 (which is 25 per cent of total expenditure, given that government's outstanding debt levels continue to remain elevated) from ₹ 10.6 tn in FY2024 RE. Salaries and pensions are projected to rise by 3.4 per cent in FY 2025 to ₹ 7.2 tn as against RE of ₹ 7 tn in FY 2024. Allocations towards key centrally sponsored schemes such as MGNREGA, Jal Jeevan Mission (JJM), Income Support Scheme remain broadly unchanged, whereas allocation towards Pradhan Mantri Awas Yojana (PMAY) stands increased significantly to ₹ 0.8 tn in FY 2025 as against ₹ 0.5 tn in FY 2024 RE which will give a boost to affordable housing.



Overall, the budget announcement has turned out to be a boon for the domestic bond markets and has changed the outlook for Indian debt dramatically

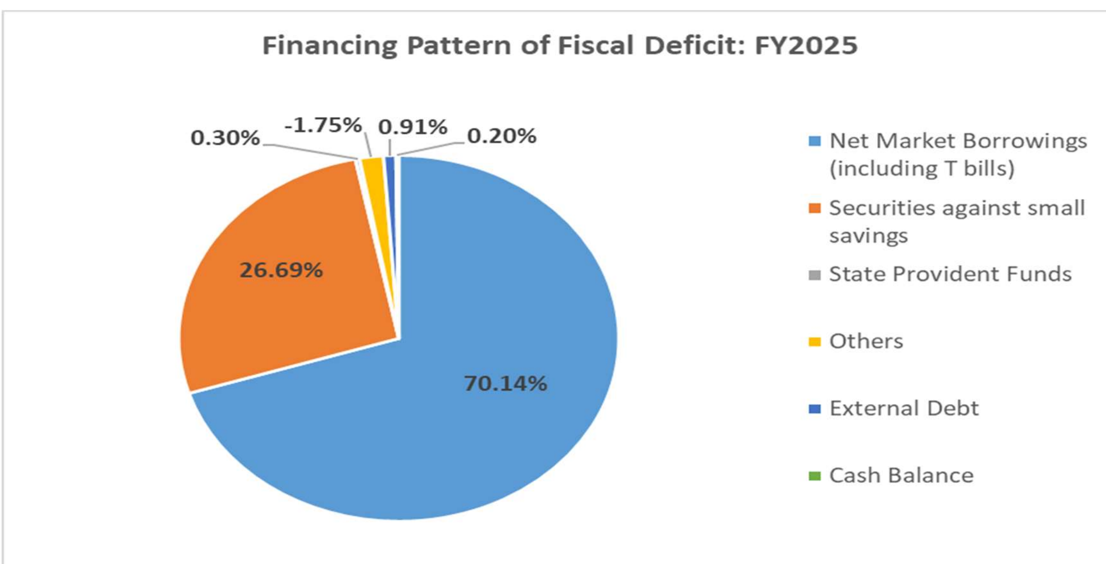
Funding of the Deficit

With 2.8 per cent contraction of the fiscal deficit, the funding requirement in FY 2025 stand lower. Even though net market borrowings are projected to finance 70 per cent of the total fiscal deficit in FY 2024-25 as against 68 per cent in FY 2023-24, the gross borrowing requirement stand lower on account of utilization of ₹ 1.23 tn from GST compensation fund to meet redemption requirement of the same amount. Hence as against scheduled redemptions of ₹ 3.61 tn, the BE redemptions for FY 2025 stand at ₹ 2.38 tn, reducing the gross market borrowing requirement to ₹ 14.13 tn in FY 2025 as against ₹ 15.43 tn in FY 2024. Securities against small savings at ₹ 4.66 tn are expected to fund the deficit to extent of ~28 per cent of the total deficit, broadly in line with FY 2024. Besides, government will resort to short-term borrowings through T-bills to the extent of ₹ 0.50 tn in FY 2025. The net borrowing requirement through dated securities stands mostly flat at ₹ 11.75 tn in FY 2025 vis-à-vis ₹ 11.80 tn in FY 2024. Bond markets reacted well to the budget announcement; on the fiscal discipline shown by the government and steering clear of populist measures despite the upcoming elections. The demand supply dynamics are expected to turn favorable in the coming FY 2025, as lower than expected CG supplies will likely meet improved demand dynamics with the onset of bond index flows as well as expected monetary easing, which will keep demand from banks also robust. Overall, the budget announcement has turned out to be a boon for the domestic bond markets and has changed the outlook for Indian debt dramatically.

Key Budget Statistics

S.No.	Particulars	FY 2023-24		FY 2024-25	
		BE	RE	BE	% Growth Over FY24 RE
1	**Revenue Receipts**	2632281	2699713	3001275	11.2
1.a	Tax Revenue (net)	2330631	2323918	2601574	11.9
1.b	Non-Tax Revenue	301650	375795	399701	6.4
2	**Non Debt Capital Receipts**	84000	56000	79000	41.1
3	**TOTAL RECEIPTS**	**2716281**	**2755713**	**3080275**	**11.8**
4	**Revenue Expenditure**	3502136	3540239	3654657	3.2
4a	Interest Payments	1079971	1055427	1190440	12.8
5	**Capital Expenditure**	1000961	950246	1111111	16.9
6	**Total Expenditure**	**4503097**	**4490485**	**4765768**	**6.1**
7	**Fiscal Deficit (6-3)**	**1786816**	**1734772**	**1685493**	**-2.8**
8	**Revenue Deficit (4-1)**	**869855**	**840526**	**653382**	**-22.3**
9	**Primary Deficit**	**706845**	**679345**	**495053**	**-27.1**
10	***Nominal GDP***	**29657745**	**29657745**	**32771808**	
11	***Nominal GDP Growth***	***8.9%***	**8.9**	**10.50%**	
12	***FD as % of GDP***	***6.0%***	***5.8%***	***5.1%***	
13	***RD as % of GDP***	***2.9%***	***2.8%***	***2.0%***	
14	***PD as % of GDP***	***2.4%***	***2.3%***	***1.5%***	
15	***Share of RD in FD***	***48.7%***	***48.5%***	***38.8%***	

Net dated G-sec borrowings will fund 70 per cent of the fiscal deficit in FY 2025



Fixed Income Outlook

Fundamental View

The domestic bond markets benefitted from the fiscally prudent interim budget announced for FY 2025 and lower gross borrowings that entail. The supply demand dynamics have been altered favourably with lower supplies set to meet improved prospective demand in the upcoming year. The next key trigger for the bond market is the MPC decision due on 8th February. The MPC should draw comfort from the counter cyclical fiscal policy delivered by the government that augurs well from inflation perspective. A change in stance by the MPC now looks plausible when seen in the light of recent RBI's continuous liquidity modulation actions to keep the operating rate tucked within the MSF rate. However, we expect the change in stance to be accompanied with cautious overtones highlighting upside risks to food inflation and commodity prices amidst ongoing geo political disturbances. On any move on stance towards the neutrality, we expect the shorter end of the curve to join the bond rally and term structure to witness bull steepening.

A change in stance by the MPC now looks plausible when seen in the light of recent RBI's continuous liquidity modulation actions

SDL Overview

During the last fortnight, 10 Yr. State Loans traded in the broad range of 7.410%-7.700%, whereas the 10 Yr. CG benchmark, remained in the range of 7.020%-7.192%. The spread between yields on the 10-year state bonds and the benchmark 10-year government bond traded in the range of 40-50 bps.

In the current financial year, the state government has borrowed around 85 % of the total borrowing announced in the calendar so far. In January 2024, the borrowings of states were lower than the budgeted amount. The FY24 Revised Estimates (RE) has indicated a higher amount of central tax devolution compared to the Budget Estimates (BE), which we believe provides a further downside to state government securities issuance in the current quarter.

We expect the yield spread between the 10-year state governments' loans and the benchmark 10-year G-sec to narrow and trade in the range of 45-47 bps in the coming weeks, and most movement will depend on the actual issuance.

Going forward, we may see time wise correction between 7.04% to 7.10% in 10-yr

Technical View

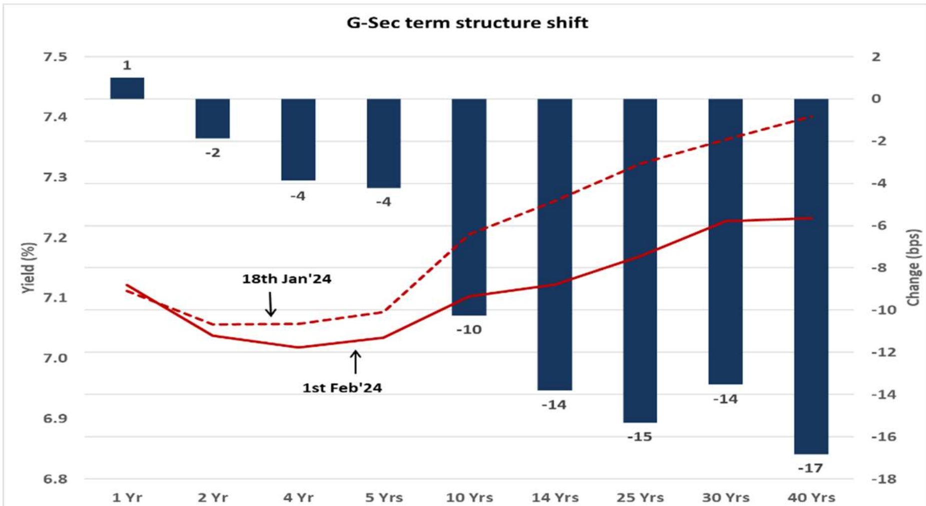
Technical Synopsis 7.18% GS 2033 Yield:

7.18% G Sec 2033 settled at 7.0555% on Friday's session. As discussed in last Newsletter, sustainability below 7.14-7.16% will trigger further softening and we may see the level of 7.04% in short term, the same was witnessed as Benchmark touched low of 7.02% and settled shop with minor bounce.

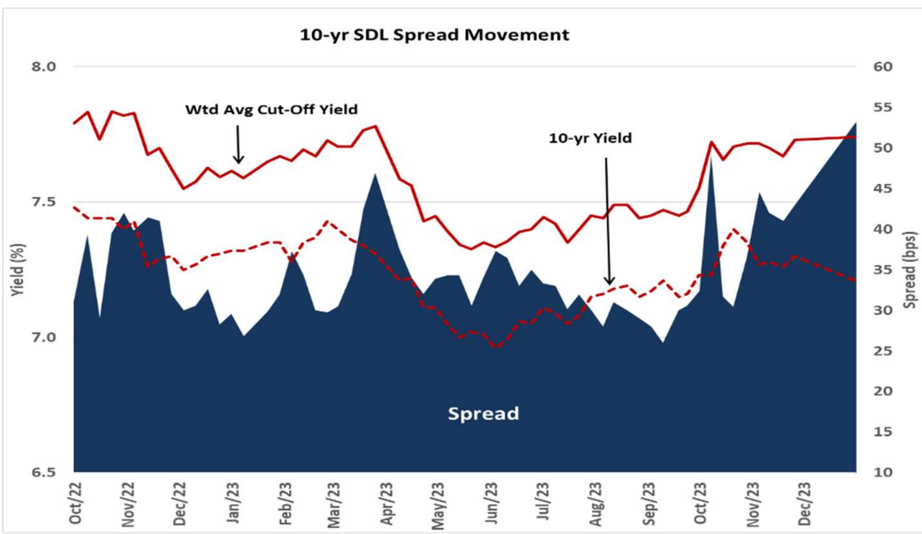
Momentum oscillator RSI is hovering around 33 level. We have witnessed a Symmetrical triangle breakout below 7.14%, indicating trend in favour of softening yields. Going forward, we may see time wise correction between 7.04% to 7.10% in 10 yr. However, any sustainability below 7.04% will open gates for 7.00%-6.96% zone. On higher side 7.10% and 7.14% will act as major resistance level for time being.

Running Chart GOI 10yr Daily. Source: Tickerplant

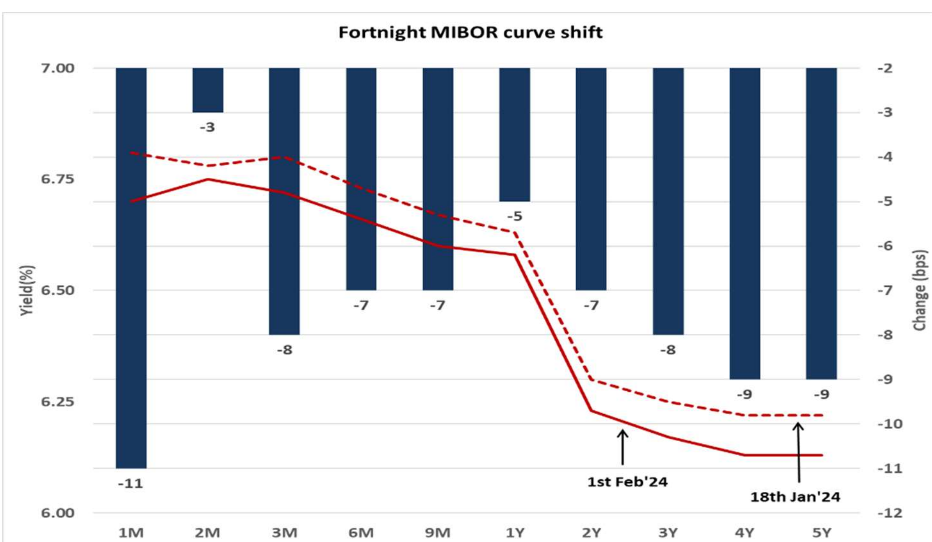
Spread Monitor



The term structure bull flattens post interim budget announcement which envisaged lower borrowings for FY 2025



The yield spread between the 10-yr SDL and the benchmark 10-yr G-sec is expected to narrow and trade in the range of 45-47 bps in the coming weeks



OIS curve shifts downwards on rate-positive budget announcement

PNB GILTS LTD.
5, Sansad Marg
New Delhi
110001

CIN:L74899DL1996PLC077120
Phone 011-23325759
For Fixed Income retail queries: 011-23321568
E Mail: marketing@pnbgilts.com
For other queries:
research@pnbgilts.com

We're on the Web!

www.pnbgilts.com

Follow us on LinkedIn

https://in.linkedin.com/company/pnb-gilts

PNB Gilts Ltd, a renowned and preferred name in the Indian debt market was one of the first entities to be granted the Primary Dealership License by the Reserve Bank of India. The company is also a subsidiary of one of the largest Indian commercial banks, Punjab National Bank. Company has played a pivotal role in strengthening of the domestic fixed income markets and is a dominant player, marking its presence with significantly high market share in the overall trading turnover.

Disclaimer