India's "all-in" economic package

Different in approach; contained in fiscal deficit

- **The last two tranches of the 10%-of-GDP economic package focused on structural reforms and increase in employment guarantee outlays**
- **The overall package focused more on medium-term supply-side measures, and funding via future public-sector liabilities**
- **As such, the central government fiscal cost is likely to be contained at 1%-of-GDP; we forecast the general government fiscal deficit at 10%-of-GDP; and growth to contract 3% y-o-y in 2020**

India's finance minister announced the fifth-and-final instalment of the 10%-of-GDP economic support plan.

What was announced today?

The seven steps announced focused on a variety of topics - MGNREGA (India's rural employment guarantee programme), ease-of-doing-business, PSE rationalization and state government resources (see table 1).

The rise in **MGNREGA outlays** was expected, and necessitated by migrant labour returning to their villages. **Easing the insolvency rules** - raising minimum threshold, suspending fresh insolvency proceedings for a year and promising a special scheme for MSMEs - are likely to provide a breather to stressed firms. Other than this, **a new PSE strategy** with a wave of privatisation, was announced. The devil, however, will be in the execution, given that several past disinvestment drives have had limited success. Finally, there was a **rise in the borrowing limits for state governments**, but with several conditionalities attached to it. States can now borrow 5% of GSDP (versus 3% earlier), but only the first 0.5% of the increase will be unconditional.

This follows from a host of announcements yesterday (the fourth instalment), which focused on implementing schemes, several of which had been outlined in the past. The highlights were implementing the **coal** commercial mining scheme, raising **defense** FDI limits (from 49% to 74%), privatising some **power distribution companies**, and auctioning out more **airports**.

The previous three instalments are discussed in these reports: (1) *India's economic package: Revitalizing agriculture: Green shoots on reforms, but at a miniscule fiscal cost,* 15 May 2020, (2) *India: Support package for migrant labour, and farmers: With a miniscule fiscal cost*, 14 May 2020, and (3) *India: First part of the 10%-of-GDP economic package announced: Liquidity to parched sectors, without a large fiscal bill*, 13 May 2020).

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Table 1: Details of today's announcements; fiscal cost is likely to be small

Category	Relief	Size of package (INR, bn)	Fiscal cost (INR, bn)
MGNREGA	Increase in budgetary allocations	400	400
Health reforms	Public expenditure on health will be increased as needed; implementation of National Digital Health Blueprint		
Ease of doing business	Exclude COVID-19 related debt from the definition of "default" under the IBC		
	Suspension of fresh initiation of insolvency proceedings for one year		
	Special insolvency framework for the MSMEs		
	Minimum threshold to initiate insolvency proceeding raised to INR 10mn		
Corporate affairs	Decriminalise minor technical defaults under Companies Act		
	Internal adjudication encouraged; amendments to de-clog criminal courts/NCLT		
	Permit direct listing of securities by Indian public companies abroad		
	Private companies with NCDs on stock exchanges not to be regarded as listed		
PSU policy	Private sector permitted in all sectors, PSUs still critical but with defined role		
	Notify 'strategic' sectors will have at least 1 PSU, but not more than 4 PSUs		
	PSUs will be privatised in 'other' sectors (depending upon feasibility)		
Suport for state governments	WMA limit increased via RBI		
	Increase state government borrowing limits to 5% from 3% of GSDP for FY21		
Total Cost (INR, bn)		**400**	**400**
% of GDP		*0.2%*	*0.2%*

Source: Ministry of Finance, HSBC

What is the overarching theme of the 10%-of-GDP package?

The 10% package covers many sectors, and touches upon some much needed reforms. For the **short run**, the following schemes seem to be most effective - rise in MGNREGA outlays, free food grains for the needy, loan guarantees for MSMEs and NBFCs, and breather from the IBC process.

If implemented well, the following can prove powerful over the **medium term** - passing laws to revitalize agriculture marketing, implementing commercial mining policy, and privatising PSEs.

The overall package is different from expectations in two ways:

Immediate government cash out-go versus rise in future public sector liabilities: Much of the 10% programme is to be funded by RBI liquidity (c4% of GDP, see table 2), a rise in future liabilities (on the back of the loan guarantee programmes), and borrowings of other public enterprises (e.g. NABARD for agriculture outlays).

Immediate demand versus medium-term supply measures: Markets were expecting a more immediate demand-side stimulus. True that some measures to remove immediate distress are contained within the package (e.g. higher food grains, MGNREGA outlays and MSME credit guarantees). However, a large part of the attention has been towards medium-term supply side measures (revitalizing agriculture marketing, stabilizing coal availability, etc).

Taking the two together, the idea here may be to raise the medium-term growth potential, which will help fund future liabilities, and lower public debt. Expectation of higher medium-term potential growth may even help raise short-term risk capital, and ease funding constraints.

However, much will depend on speedy implementation of these reforms, and in that sense, the work for the authorities has just begun.

Table 2: The 10%-of-GDP package has a 1% fiscal cost

	Date	Economic support package	Size of package (INR, bn)	Fiscal cost (INR,bn)
Fiscal measures	**Reforms** 17-May-20	Increase in MGNREGA budgetary allocations	400	400
	Total		**400**	**400**
	% GDP		*0.2*	*0.2*
	Industrial infra 16-May-20	Viability gap funding for social infrastructure	81	81
	Total		**81**	**81**
	% GDP		*0.04*	*0.04*
	Agriculture and allied 15-May-2020	Farm-gate and aggregation point infrastructure	1000	
		Fisheries	200	
		Animal husbandry	150	
		Others (animal vaccination, micro food enterprise)	150	30
	Total		**1500**	**30**
	% GDP		*0.7*	*0.01*
	Migrant & farmers 14-May-20	Concessional credit via Kisan credit card	2000	
		Emergency working capital funding for farmers	300	
		Affordable housing	700	60
		Others (food, street vendors, micro loans)	100	100
	Total		**3100**	**160**
	% GDP		*1.5*	*0.1*
	MSME, NBFCs, etc. 13-May-20	MSME	3700	140
		NBFCs/ HFCs/ MFIs	750	
		DISCOMs	900	
		Others (PF/ tax relief)	596	28
	Total		**5946**	**168**
	% GDP		*2.9*	*0.1*
	Welfare and health 26-Mar-20 and before	Welfare spending (Women, pensioners)	434	434
		Others (food, financial security)	1266	634
		Emergency health response package	150	150
		Revenue lost due to tax concessions	78	78
	Total		**1928**	**1296**
	% GDP		*0.9*	*0.6*
Monetary measures	**Reserve Bank of India**	Targeted long term repos operations	1001	
		Cash Reserve Ratio cut by 100bps	1370	
		Marginal Standing Facility limit increase	1370	
		Targeted long term repos operations, version 2	500	
		Refinancing facilities for select financial institutions	500	
		Special liquidity facility for mutual funds	500	
		Open market operations	400	
		Purchase of T-bills	900	
		WMA limit increase for centre and state	1450	
		Others (Misc.)	26	
	Total		**8016**	
	% GDP		*3.9*	
	Grand total		**20971**	**2135**
	% GDP		*10.3*	*1.0*

Source: Ministry of Finance, RBI, HSBC.

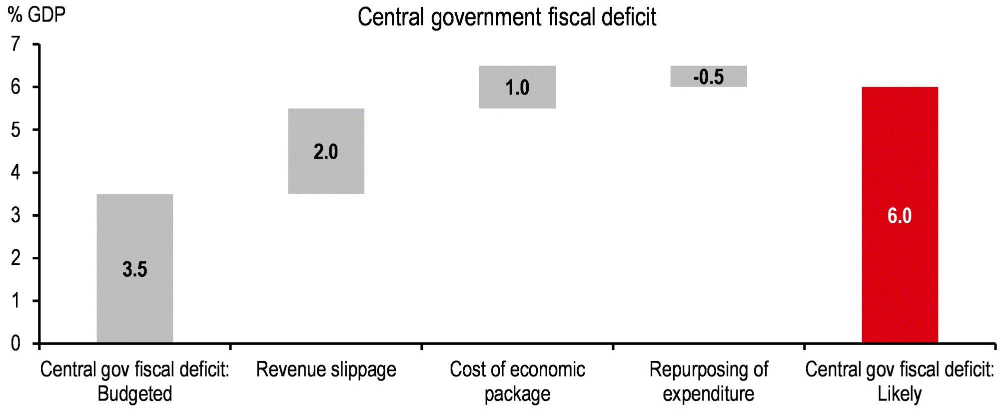
What is the fiscal cost?

As we have been highlighting in the previous notes of this series, the impact of the 10%-of-GDP package on the fiscal deficit is small. Adding across all the items, we estimate it at **1%-of-GDP** (see table 2).

Adding up (tax and non-tax) revenue shortfall and the fiscal cost of the package, the **central government fiscal deficit** will likely come in at 6%-of-GDP in FY21 (versus 3.5% budgeted, see chart 1).

The state fiscal deficit is forecasted at 4%-of-GDP, taking general government fiscal deficit to 10% of GDP.

Chart 1: Central government fiscal deficit to come in at 6%-of-GDP in FY21



Source: HSBC estimates

Where is growth likely to be?

As is clear from the fiscal math, the direct cash outgo to support immediate domestic demand remains contained.

But as the lockdown eases (gradually), postponed consumption demand and inventory restocking demand could provide a growth push.

However, once that wave is gone, India may not have a strong driver of growth, especially given weak labour markets. We therefore forecast growth to contract by 3% in 2020 (see table 3).

If the slew of supply side reforms are executed efficiently, the current fall in growth may not seep much into India's potential growth.

What next to watch out for?

Following five days of press conferences by the government, we will look out for:

(1) Steps towards speedy implementation of the reforms outlined;

(2) steps by the RBI to help recovery via further rate cuts (we expect a 40bps repo rate cut in June, taking the repo rate to 4%), extension in loan moratorium and other steps to lower regulatory burden, and

(3) Steps by the RBI to help absorb government paper (i.e. the likely increase in state borrowings, and announcement of an indicative OMO purchases calendar).

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Table 3: Our key macro forecasts

In fiscal year terms, unless otherwise stated	Unit	FY19 (Apr'18-Mar'19)	FY20 (Apr'19-Mar'20)	FY21 (Apr'20-Mar'21)
Gross domestic product (GDP), calendar year*	%y-o-y	6.8	5.3	-3.0
Gross domestic product (GDP)	%y-o-y	6.1	4.3	-2.0
Consumer price index (CPI)	%y-o-y	3.4	4.8	4.0
Current account deficit (C/A deficit)	% GDP	2.1	1.0	0.6
Central government fiscal deficit	% GDP	3.4	4.0	6.0
State government fiscal deficit	% GDP	2.5	3.0	4.0
Repo rate	%, end-period	6.3	4.4	4.0

Source: CEIC, RBI, HSBC. *FY21 refers to CY2020.

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