

India faces tough budget test as economy slows

Finance minister pressed to revive growth while maintaining fiscal discipline

JOHN REED — NEW DELHI
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India's government is under pressure to turn around a slowing economy but has little room to manoeuvre as it prepares to present one of the most consequential budgets since Narendra Modi came to power more than a decade ago.

Finance minister Nirmala Sitharaman is facing expectations to announce tax cuts, new capital expenditure and reforms to India's regulatory regime when she unveils the first full budget of Modi's third term as prime minister on Saturday.

Her ability to revive an economy mired in a broad slowdown — and allay discontent among the ruling Bharatiya Janata party's middle- and upper-class political base — may be limited.

India's pace of growth, while still the fastest among large economies, is heading for a post-pandemic low, dragged down by weaker urban consumption, persistent food inflation, stagnant wage and job growth and sluggish private sector investment. Second-quarter fiscal year growth was 5.4 per cent, the slowest pace in nearly two years, and the central bank downgraded growth forecasts for the 2024-25 fiscal year.

"There are a lot of pressures — there has been a cyclical slowdown," said Shumita Deveshwar, chief India economist with GlobalData. TSLombard.

"We have to see whether they will stick with that fiscal discipline they have exhibited over the past few years", or "do more on welfare spending".

New Delhi recently named Sanjay Malhotra, a former revenue secretary, as Reserve Bank of India governor, a move markets regarded as a commitment to the government's recent record of stronger growth and fiscal rectitude.

India's fiscal deficit is below 5 per cent of GDP and falling, and the government resisted the temptation to unleash populist spending measures in last year's post-election budget plan, which followed a nationwide election in which the BJP lost its parliamentary majority.

"This is a finance ministry that values prudence," said Shilan Shah, deputy chief emerging markets economist at Capital Economics, which expects weaker growth in the first half of this



Slow going: goods trucks in Mumbai.

India's pace of economic growth is heading for a post-pandemic

low — Indranil Mukherjee/
AFP/Getty Images

year before a gradual recovery. "A big stimulus package looks unlikely."

However, Shah added that boosting spending on infrastructure — a hallmark of Modi's tenure — "would help to support economic activity in the near-term while also lifting the economy's medium-term supply potential".

Spending is rising in some states, including Maharashtra and Karnataka, where the BJP and opposition rivals are vying to outdo one another with politically driven, open-ended welfare spend-

ing promises, pushing the country's consolidated budget deficit close to 8 per cent of GDP. Local elections are also looming this year in Delhi and Bihar, India's third-largest state.

Working in India's favour, economists forecast that the country's inward-focused economy will avoid the brunt of Donald Trump's expected barrage of tariffs on countries such as China. In a call this week, the US president urged his Indian counterpart to buy more American-made weapons, and Trump

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later said Modi would probably visit the White House next month.

The finance minister's budget address will be followed less than a week later by the RBI's first monetary policy decision under Malhotra, who replaced the more hawkish Shaktikanta Das.

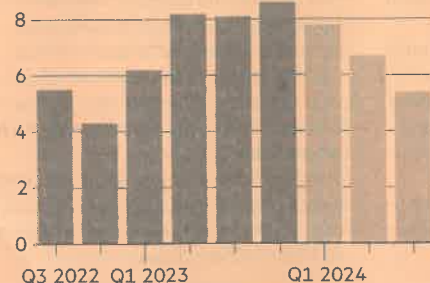
Malhotra has been facing calls to cut rates from Modi allies including Sitharaman and commerce minister Piyush Goyal, who favour lower borrowing costs to support growth, despite inflation being close to the top of the central bank's 4-6 per cent target band. Many economists expect the RBI to begin easing rates from its current 6.5 per cent level, particularly after it announced measures this week amounting to a near \$18bn liquidity infusion in the cash-starved banking sector.

Kunal Kundu, India economist at Société Générale, cautioned that the economic vulnerabilities were structural. He said fundamental shifts, including a focus on education and healthcare investment, were needed for India to create more formal jobs for its huge and under-skilled labour force.

"Employment and wages remain at the heart of the slowdown," said Kundu. "You have to have policies that eventually enable more job generation."

India's GDP growth slows for third consecutive quarter

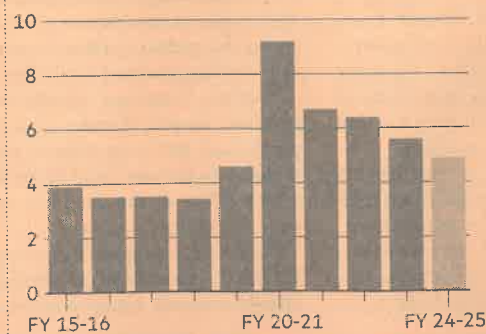
GDP growth rate, year on year (%)



Source: India's Ministry of Statistics and Programme Implementation • Data as of Q3 2024 (India's Q2 FY2024-25)

India has narrowed its fiscal deficit

Fiscal deficit (% of GDP)



Sources: India's budget documents; Ministry of Finance • Fiscal year is from Apr to Mar, FY24-25; budget estimates; FY23-24; provisional actual data