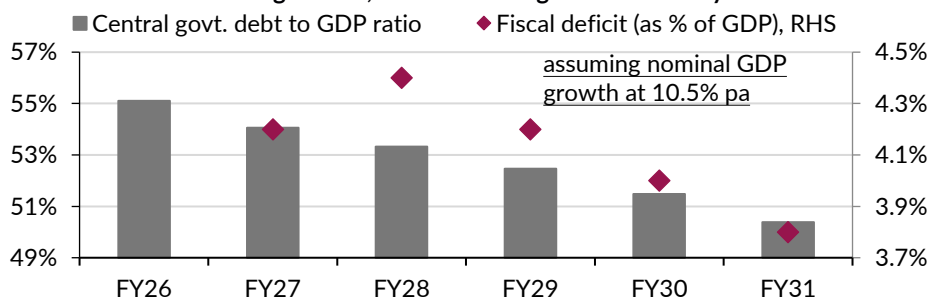


Revenue shortfall managed, deficit on target; consolidation to continue

We expect FY26 gross tax collection to be ₹2.8tn below budget estimates (BE; weaker income tax and GST). Net of transfers to states, the tax shortfall would be ₹1.8tn. Higher RBI/PSU dividends should narrow the gap in receipts vs. BE to ₹1.5tn. ₹0.7tn of the GST compensation cess related shortfall would also show up in lower expenditure. Combined with lower spend on other schemes, we expect total spend to be >₹1.4tn below BE, and the deficit ratio target to be met. In FY27, we expect deficit at 4.2% of GDP, with capex growth 11% and total spend ex-interest to grow 5% YoY. Higher inflows to small-savings schemes and more T-bills should limit net G-Sec borrowings to ₹10.5tn, in our view.

January 13, 2026

Fiscal, FY27 Budget Preview

Exhibit 1 - FY27 deficit target 4.2%; faster nominal growth necessary to lower debt ratio


Source: RBI, Axis Bank Research

Large tax revenue shortfall in FY26; tax-to-GDP unlikely to deteriorate further

We expect gross taxes in FY26RE to be 7% below BE (a Rs.2.8tn shortfall) primarily due to lower income taxes and GST. The rise in personal income tax as % of GDP (Fig 2) reversed in FY26 due to the tax cut, but the disappointment likely came from a drop in capital gains; it should stabilize now. The Centre's weak GST intake (Fig 5) is due to i) large IGST refunds; and ii) compensation cess merged into GST. Net of transfers to states, the net tax shortfall is est. at Rs1.8tn. Higher RBI+PSU dividends could add Rs. 0.6tn in revenue, and divestment proceeds maybe 0.2tn lower vs. BE. Thus, net receipts may be Rs1.5tn below BE.

A commensurate drop in spending means an intact fiscal deficit target

While expenditure should be higher than BE for subsidies like fertilizers, it is expected to be below BE on several heads, like the Rs0.7tn reduction in transfers of GST compensation cess and Rs0.5tn drop for Jal Jeevan Mission ([link](#)). Revenue expenditure growth has been weaker than BE so far: +2% YoY FYTD vs. 7% in BE implying a Rs1.7tn shortfall annualized. Though payments like food subsidy to FCI tend to be lumpy, we expect aggregate expenditure to be ~Rs1.4tn below BE, helping the centre meet its 4.4% deficit ratio target.

Fiscal consolidation to continue in FY27 but at a slower pace (20bps)

The 16th Finance Commission report (to be tabled with the budget) will affect transfers to states: devolution ratio, grants, and other transfers. For our current projections we assume a status quo. Given the FY31 debt-to-GDP target of ~50%, and the salary/pension increase of the 8th Pay Commission (CPC) expected in FY28, we expect the centre to bring down the deficit ratio to 4.2% in FY27. We expect expenditure ex-interest to grow 5% YoY, with 11% growth in capex vs. FY26RE. Low inflation means the pre-CPC hike in wages/pensions should be muted, offsetting the increase in fertilizer subsidies (higher global prices, Fig 11).

'Crowding out' reduces further, given growing economy and demand for government paper (incl. OMOs). FY26 non-market borrowing (via small savings) should be Rs. 1tn higher than BE, in our view, persisting next year. In addition, borrowing via bills may pick-up as well (> Rs. 0.5tn). We expect Rs. 10.5tn of net G-Sec borrowings in FY27. Higher states' borrowings in FY27 and elevated LCR at banks remain risks to an otherwise favourable demand-supply scenario.

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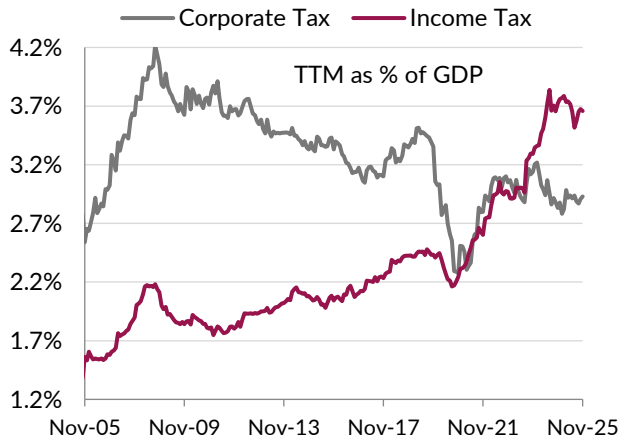
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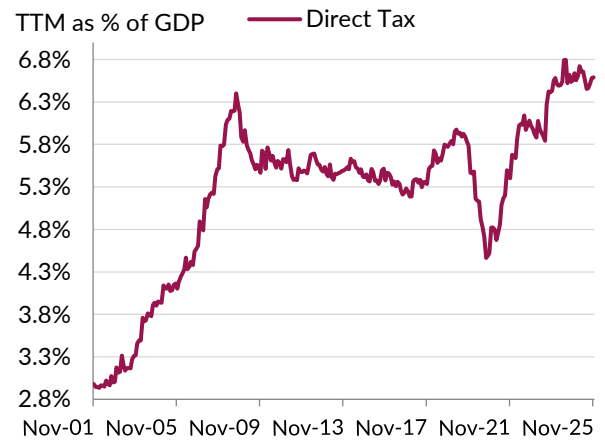
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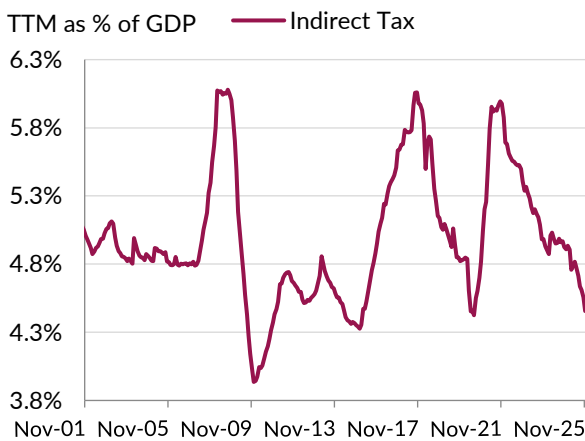
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Section 1 – Revenue receipts
Exhibit 2 - Income tax to GDP now lower vs. cyclical peak


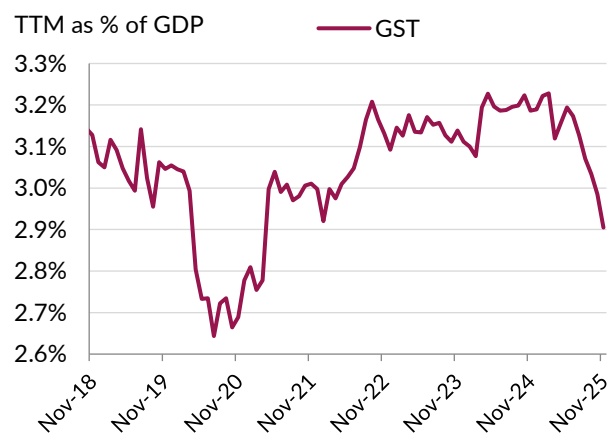
Source: CEIC, Axis Bank Research

Exhibit 3 - Direct tax to GDP now 20bps lower vs. peak


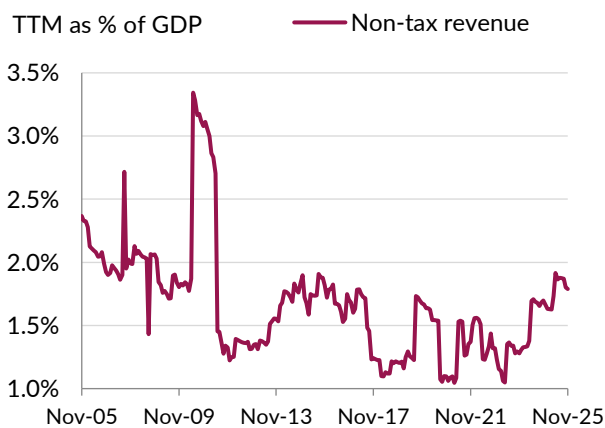
Source: CEIC, Axis Bank Research

Exhibit 4 - Overall indirect taxes may rise faster now...


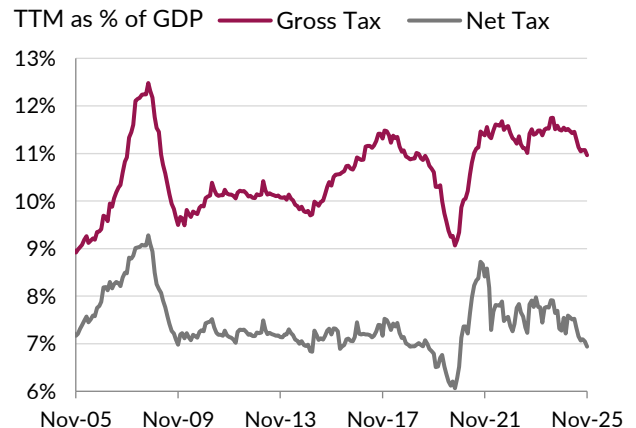
Source: CEIC, Axis Bank Research

Exhibit 5 - ... not only because GST receipts may grow faster


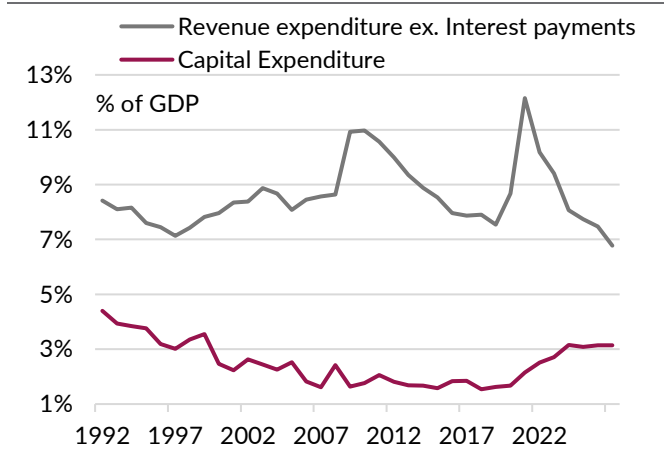
Source: CEIC, Axis Bank Research

Exhibit 6 - Non-tax revenue can stay elevated for another 1Y


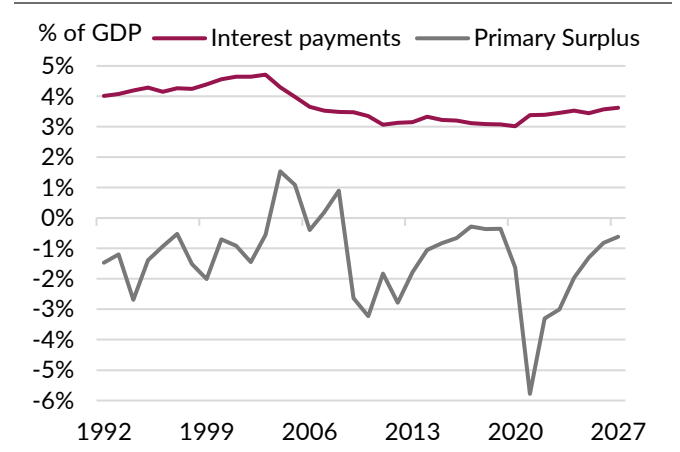
Source: CEIC, Axis Bank Research

Exhibit 7 - Net tax receipts should exceed 7% of GDP


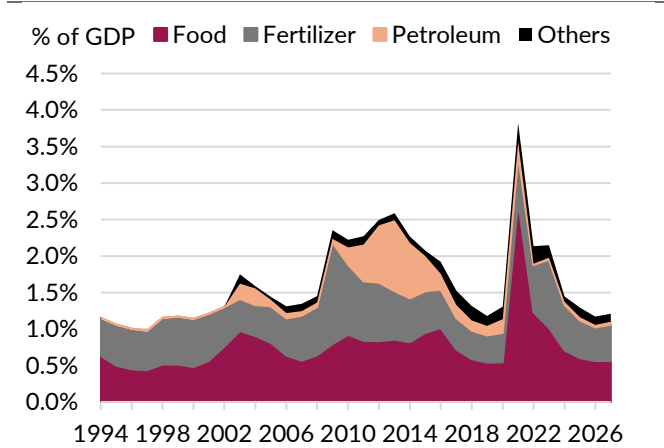
Source: CEIC, Axis Bank Research

Section 2 - Expenditure, deficits and financing
Exhibit 8 - Shift to better quality spending post COVID continues


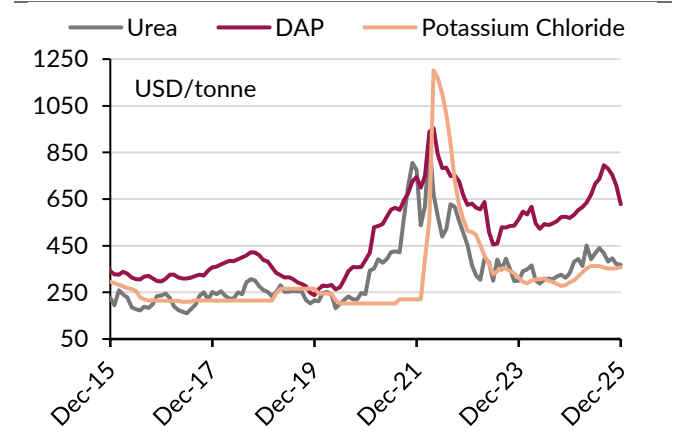
Source: Bloomberg, Axis Bank Research

Exhibit 9 - FY27 primary deficit may shrink to 0.6% of GDP


Source: Bloomberg, Axis Bank Research

Exhibit 10 - Subsidy bill unlikely to cross 1.2% of GDP


Source: Budget documents, Axis Bank Research

Exhibit 11 - Global fertilizer prices now correcting


Source: Bloomberg, Axis Bank Research

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