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The Budget and the Imperative of Fiscal Consolidation

Context

- The **Union Budget** 2026-27 is framed as a critical step in India's journey towards **Viksit Bharat** by 2047.
- It prioritises advanced **technology** sectors such as artificial intelligence, biopharma, semiconductors and critical minerals, reflecting long-term development ambitions.
- While the strategic direction is appropriate, the success of these initiatives depends on effective **implementation**, adequate fiscal space and the pace at which outcomes can be delivered in a resource-constrained environment.

Key Highlights of Union Budget 2026-27

- **Restructuring of Expenditure and Changing Fiscal Priorities**

- A key feature of recent fiscal policy has been the restructuring of government **expenditure** to accommodate new priorities.
- The share of revenue expenditure in total expenditure has declined from 88 per cent in 2014-15 to about 77 per cent in 2026-27 (BE).
- This reduction has been driven largely by a decline in central **subsidies**, allowing a corresponding increase in **capital**
- This shift signals a move away from consumption-oriented spending towards asset creation and long-term **growth**.

- **Capital Expenditure: Role in Growth and Emerging Concerns**

- Public capital **investment** has played a crucial role in supporting economic recovery in the post-pandemic period.
- Capital expenditure as a share of GDP has remained elevated, supporting infrastructure creation and demand.
- However, the momentum of this spending has weakened. Capital expenditure growth declined sharply from 28.3 per cent in 2023-24 to 4.2 per cent in 2025-26 (RE).
- Although growth is budgeted at 11.5 per cent in 2026-27 (BE), it is only marginally higher than nominal GDP growth, leaving capital expenditure nearly stagnant at around 3.1 per cent of GDP.
- Repeated shortfalls between budgeted and actual spending raise concerns about execution capacity.

- **Revenue Prospects and Tax Buoyancy Challenges**

- On the **revenue** side, tax projections appear cautious and achievable. However, the low **buoyancy** of gross tax revenues remains a constraint.
- Overall tax buoyancy is estimated at 0.8, below the benchmark of one. While direct taxes show relatively strong responsiveness, indirect taxes lag behind. In particular, **GST** collections are not expected to keep pace with GDP growth.
- With rising developmental and welfare commitments, strengthening indirect tax responsiveness becomes essential for maintaining fiscal balance.

Finance Commission Transfers and Centre-State Fiscal Relations

- The recommendations of the Sixteenth Finance Commission retain the share of **States** in the divisible pool of central taxes at 41 per cent.
- However, the discontinuation of revenue deficit grants and the absence of sector- or State-specific grants have reduced overall **transfers**.
- Finance Commission grants are projected to decline from 0.43 per cent of GDP in 2025–26 to 0.33 per cent in 2026–27.
- This reduction may constrain subnational governments at a time when their role in delivering public services and development programmes is expanding.

Challenges and the Way Forward

- **Fiscal Consolidation and the Debt-Deficit Strategy**

- The pace of **fiscal consolidation** has slowed considerably in recent years.
- While the fiscal **deficit** to GDP ratio continues to decline, the annual reduction has narrowed to just 0.1 percentage point in 2026–27 (BE).
- The shift in focus from deficit targeting to **debt**-GDP targeting does not significantly improve transparency, as both indicators are closely linked to nominal GDP growth.
- A clear medium-term glide path outlining targets and assumptions would strengthen fiscal credibility.

- **Rising Debt and Interest Payment Pressures**

- High public debt levels have increased **interest** payment pressures.
- The effective interest rate on central government debt is projected to rise to 7.12 per cent in 2026–27, with interest payments absorbing nearly 40 per cent of revenue receipts.
- This limits fiscal space for essential primary expenditure. Persistent high public borrowing also risks crowding out private investment, which could weaken medium-term growth prospects.

Conclusion

- The Budget presents a coherent **roadmap** for long-term development, with emphasis on technology-led growth and public investment.
- However, achieving these objectives requires careful balancing of ambition with fiscal **prudence**.
- Strengthening tax buoyancy, ensuring credible capital expenditure outcomes, maintaining adequate transfers to States and restoring momentum in fiscal consolidation are essential.
- Sustained economic expansion ultimately depends on macroeconomic **stability** and **sustainability**, both of which require disciplined and transparent fiscal management.

The Budget and the Imperative of Fiscal Consolidation FAQs

Q1. What is the central objective of the Union Budget 2026–27?

Ans. The central objective of the Union Budget 2026–27 is to support India’s transition towards becoming a developed nation by 2047 through growth-oriented public spending.

Q2. Why has the share of capital expenditure increased in recent years?

Ans. The share of capital expenditure has increased due to a deliberate reduction in revenue expenditure, particularly central subsidies, to prioritise long-term growth.

Q3. What concern arises from the recent trend in capital expenditure growth?

Ans. The slowdown in capital expenditure growth raises concerns about the government’s capacity to sustain public investment momentum.

Q4. Why is low tax buoyancy a fiscal challenge?

Ans. Low tax buoyancy limits the government’s ability to finance rising developmental and welfare expenditures without increasing fiscal stress.

Q5. How do rising interest payments affect fiscal space?

Ans. Rising interest payments reduce fiscal space by absorbing a large share of revenue receipts, thereby constraining productive public spending.

Source: **The Hindu**

The U.S. Trade Deal, Gains from Economic Diplomacy

Context

- India’s recent trade agreement with the United States represents a defining moment in the country’s evolving **global trade strategy**.
- Positioned within a broader architecture of strategic trade partnerships, the agreement reflects India’s shift toward predictable, rules-based, and **large-scale trade engagement**.
- More than a reduction in tariffs, the deal signals **India’s growing confidence as a global economic actor** and underscores the deepening strategic alignment between the world’s two largest democracies.

The Road to Agreement on India-US Deal and India's Expanding Network of Trade Partnerships

• The Road to Agreement: Negotiation, Diplomacy and Policy Certainty

- The India-U.S. trade deal emerged from nearly a year of **sustained dialogue**, technical negotiations, and quiet diplomacy.
- The complexity of the process highlights the **sensitivity of bilateral trade** relations and the significance of the outcome.
- The agreement to reduce **S. tariffs on Indian goods to 18%** marks a critical departure from previously elevated tariff levels that had reached up to 50%.
- This shift restores competitiveness for Indian exporters, enhances policy predictability, and reflects the effectiveness and resilience of India's negotiating approach.

• India's Expanding Network of Trade Partnerships

- The agreement with the United States must be viewed as part of **India's broader strategy** of forging comprehensive trade partnerships across regions.
- Trade agreements with the European Union, the United Kingdom, and the European Free Trade Association provide India with preferential access to European markets, while agreements with Australia and New Zealand strengthen its engagement with the Pacific region.
- Similarly, trade arrangements with the United Arab Emirates and Oman enhance access to West Asia.
- Within this expanding network, the **United States holds particular importance** as the world's largest import market and India's single largest export destination, accounting for nearly one-fifth of India's total exports.

Immediate Gains from US-India Trade Deal

• Sectoral Impact: Boosting Employment-Intensive Exports

- The most immediate gains from the tariff reduction are expected in **employment-intensive export sectors**.
- Apparel, a major contributor to industrial employment, stands to benefit significantly as Indian products now face lower tariffs than those of key competitors such as Vietnam and Bangladesh in the U.S. market.
- Other sectors, including gems and jewellery, marine products, processed foods, footwear, and leather, also gain from improved price competitiveness.
- Even modest tariff reductions in these industries translate into **meaningful cost advantages**, encouraging capacity expansion and deeper integration into global supply chains.

• Enhancing Global Competitiveness and Manufacturing Ambitions

- By lowering U.S. tariffs on Indian goods, the agreement strengthens **India's competitive position** relative to major exporting economies such as China, Bangladesh, Sri Lanka, Brazil, South Africa, Pakistan, and ASEAN countries.
- This **enhanced competitiveness** directly supports India's long-term objective of becoming a global manufacturing hub.
- Improved market access, combined with greater policy certainty, creates conditions conducive to investment, scale, and productivity growth across export-oriented industries.

• **Beyond Trade: Strategic and Institutional Implications**

- The agreement's significance extends **beyond immediate economic benefits**.
- Reduced trade frictions create momentum for advancing negotiations under the proposed India-U.S. Bilateral Trade Agreement, opening avenues for deeper cooperation in regulatory alignment, market access, and supply-chain resilience.
- The deal also encourages joint ventures, technology partnerships, and investment in high-value sectors, creating innovation, skill development, and employment generation.
- These outcomes **reinforce mutual interests** in strengthening trusted supply chains and advancing innovation-led growth.

Trade, Trust and Strategic Alignment

- From a strategic perspective, the trade deal contributes to a **broader reset in India-U.S. relations** grounded in trust and shared priorities.
- Stronger economic ties complement cooperation in strategic forums such as the Quad, where supply-chain resilience and **reliable partnerships are key objectives**.
- By aligning economic engagement with strategic cooperation, the agreement reinforces a stable and forward-looking bilateral relationship.

Conclusion

- The India-U.S. trade agreement is not merely a technical adjustment of tariff rates; it **represents a strategic consolidation** of economic and diplomatic ties.
- By enhancing export competitiveness, supporting employment-intensive sectors, and reinforcing India's global trade integration, the deal lays **the foundation for sustained bilateral growth**.
- As policy momentum now shifts toward implementation, the focus turns to industry to leverage these opportunities through investment, innovation, and scale.
- Ultimately, the agreement marks **a renewed, balanced, and strategic partnership** poised to shape India-U.S. cooperation in the decades ahead.

The U.S. Trade Deal, Gains from Economic Diplomacy FAQs

Q1. What is the main objective of the India-U.S. trade agreement?

Ans. The main objective is to enhance trade predictability, improve market access, and strengthen long-term economic and strategic cooperation.

Q2. How does the tariff reduction benefit Indian exporters?

Ans. The tariff reduction improves price competitiveness and restores Indian exporters' access to the U.S. market.

Q3. Which sectors gain the most from the agreement?

Ans. Employment-intensive sectors such as apparel, gems and jewellery, and leather benefit the most.

Q4. How does the deal support India's manufacturing ambitions?

Ans. The deal supports manufacturing by improving competitiveness and integrating Indian firms into global supply chains.

Q5. Why is the agreement strategically significant beyond trade?

Ans. It strengthens trust, reinforces strategic alignment, and complements cooperation in forums like the Quad.

Source: **The Hindu**

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