Final Countdown to Union Budget: Are We in for "Positive" Surprises?

30th January, 2026

While the Government does not wait for the Budget to announce key reforms, yet it still remains on close watch as a crucial policy document. In this context, given the "tamed" expectations from the upcoming Budget (as most key policy announcements are under execution), we question whether macros and markets are in for some positive surprises?

India: Are we in for +ve surprises in this Budget? (1)

What are the key surprises probably in store for us in this Budget on 1st February?

1. **Fiscal deficit: 4.4% *(flat)* or 4.2% *(lower)* of GDP?**
   a. *Adoption of debt to GDP targeting may support countercyclical fiscal policy if needed to support growth*
   b. *We see fiscal consolidation to continue in FY27, albeit at slower pace, to 4.2% of GDP, in order to preserve policy space in an uncertain world & ahead of Pay Commission implementation in FY28*
   c. *Policy priority likely to be capex even as revenues may continue to stay under pressure from tax cut boosters given in FY26 and discontinuation of GST Compensation cess fund from 1st Feb'26.*

2. **Lower than expected FY27 market borrowings numbers?**
   a. *Market consensus is for gross & net market borrowing numbers in ranges of Rs.15.5-16.5 lakh cr & Rs.11.5-12.5 lakh cr. UBI estimate is at lower end of ranges in baseline scenario.*
   b. *While the Finance Minister has been conservative in her assumptions to ensure credibility, we think there is some space to show lower gross & net borrowing numbers of Rs 15.5 lakh cr & Rs 10.5 lakh cr.*
   c. *Despite low probability of an "optimistic" scenario, we propagate the same given states borrowing stays elevated and overall (states plus centre) gross borrowing seen at Rs 28-29 lakh cr, may keep yields elevated despite monetary easing.*

India: Are we in for +ve surprises in this Budget? (2)

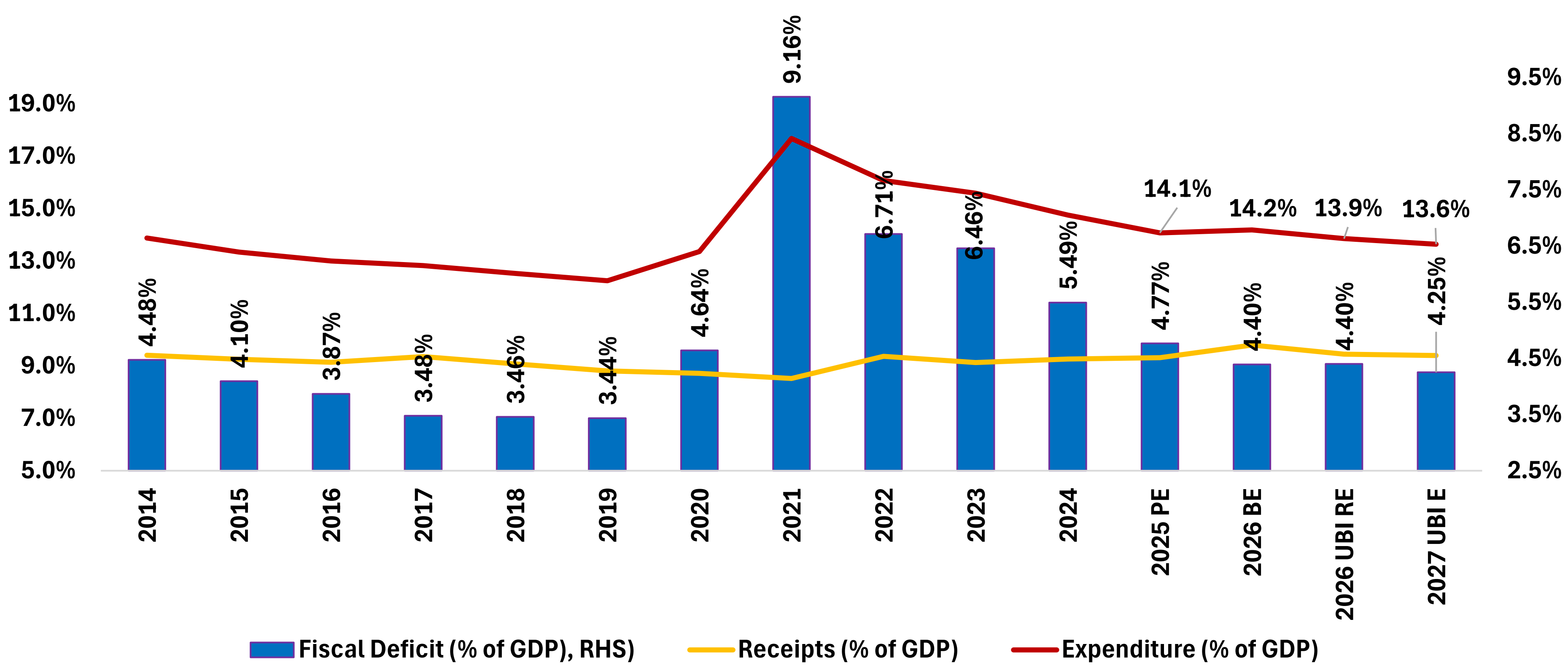
3. **Finance Commission report: will we see much-needed radical reforms in states fiscal dynamics?**
   a. *Market expectations are of minor tinkering in states' share in center's tax devolution from divisible tax pool.*
   b. *Media sources, however, are indicating that some key reform proposals may be announced with the Finance Commission report to be released to address macro urgency to handle states fiscal dynamics via:*
      - ***Fiscal roadmap for states targeting fiscal deficit to come down to sub-3% of GSDP in a prescribed time period***
      - ***As centre moves towards debt to GDP targeting during FC period, any such roadmaps or targeting paths in case laid out for individual states***

4. **Clearing of long-pending reform asks to address dislocations in macros and markets**
   a. *Tax reforms to make deposits attractive for banks to have sufficient funds to support high credit growth*
   b. *Laying the red carpet for foreign investors, given the sharp slowdown in capital flows in recent years*
   c. *Promoting sectors like Defence to help wade through geopolitical uncertainties*
   d. *Focus on customs duty rationalization & other reforms to boost manufacturing, ease of doing business & deregulation*

Unveiling the fiscal math

We see slower pace of fiscal consolidation in FY27 primarily via expenditure rationalisation

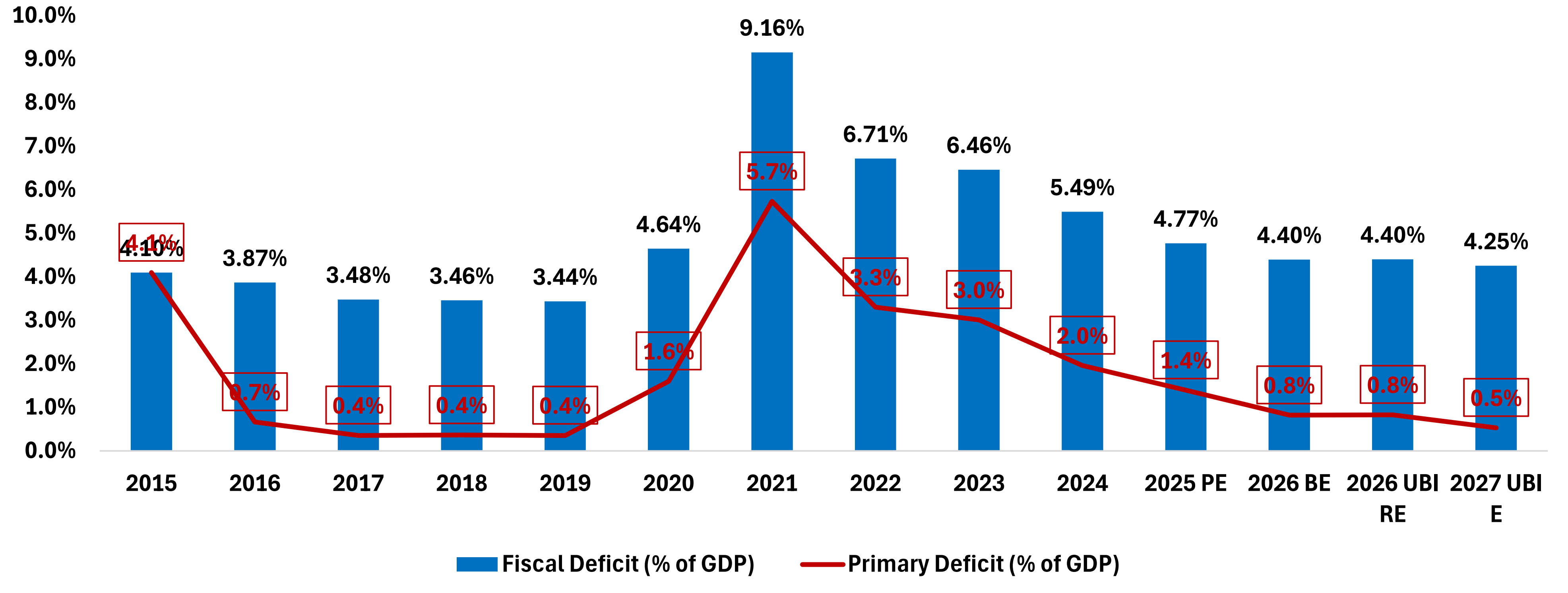
Trends in Fiscal Deficit, Receipts and Expenditure



Source: CEIC, Budget Documents, DIPAM & UBI Research

Primary balance likely to sharp consolidation…

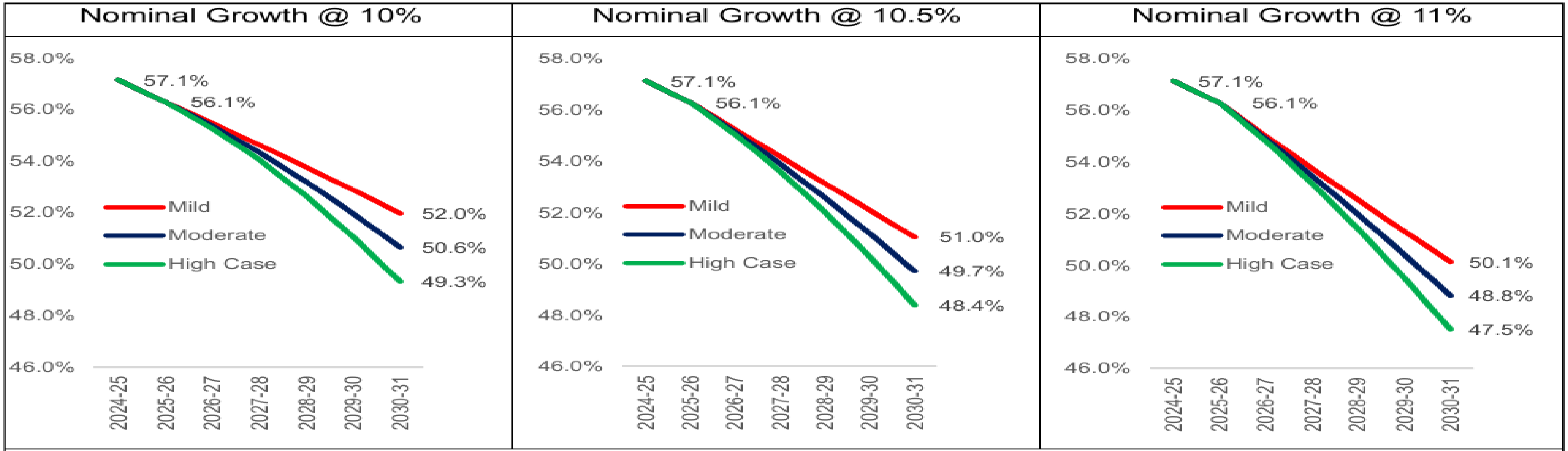
Trends in Fiscal and Primary Deficits



Source: CEIC, Budget Documents, DIPAM & UBI Research

…as the centre transitions from fiscal deficit to debt to GDP targeting framework

Debt transition roadmap to 50% of GDP target by FY31 given in last year's Budget



Note: Mild/Moderate/High case refer to degrees of fiscal consolidaton.

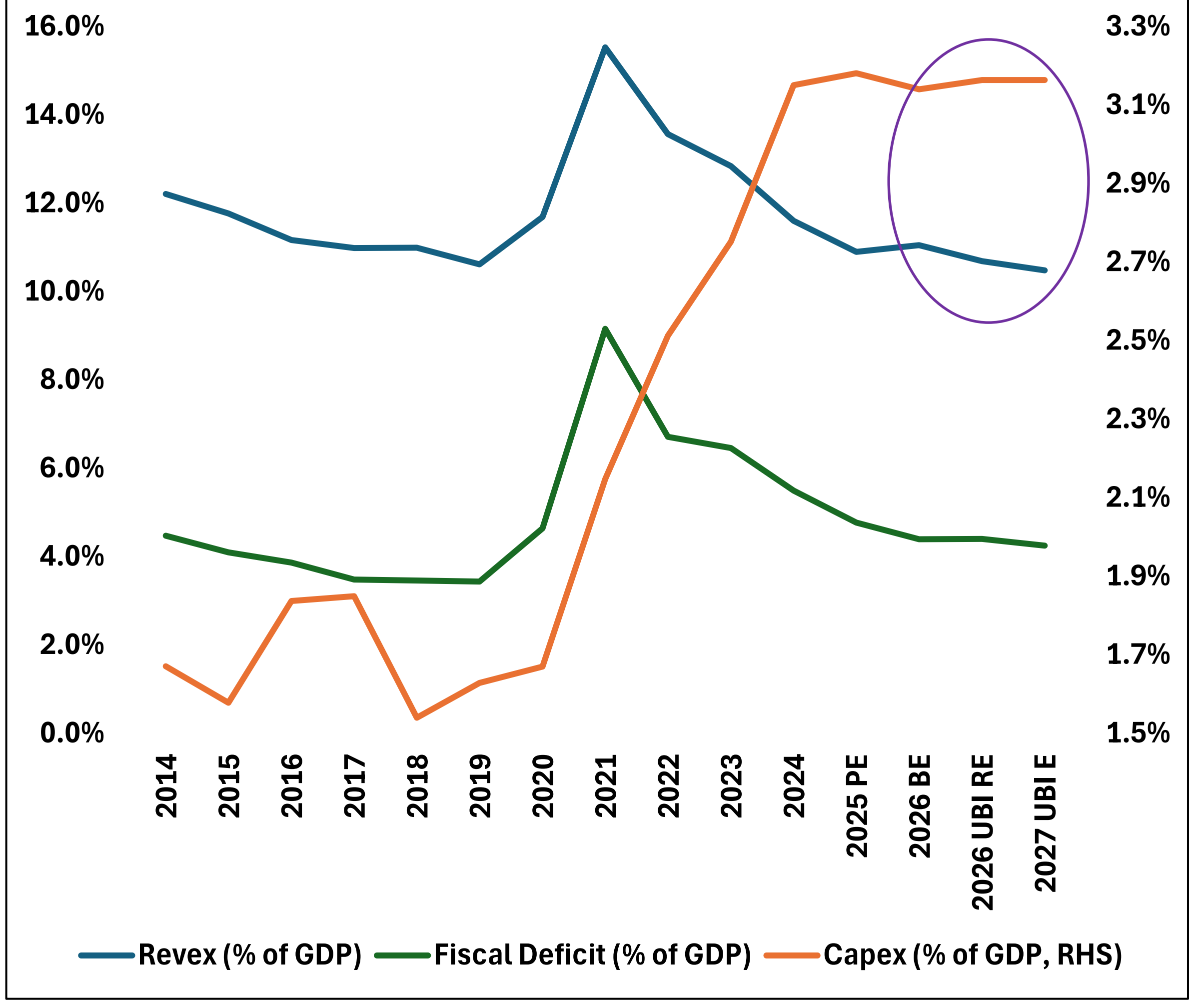
- *Centre aims to transition to a debt management approach from FY27 and would endeavour to keep fiscal deficit in each year (from FY27 till FY31) to reduce debt to GDP level to ~50±1% by FY31 (the last year of the 16th Finance Commission cycle) under various scenarios of nominal GDP growth.*

- *This debt management approach would require consolidation of primary deficit (fiscal deficit adjusted for interest payments on outstanding debt). As per our calculations, primary deficit is likely to narrow from 1.4% of GDP in FY25 to 0.8% in FY26 and likely budgeted to reduce to 0.5% in FY27.*

Source: Budget Documents & UBI Research

Focus likely to stay on quality of spending

Capex push and revex rationalisation seen in FY27



Centre's Capex: Composition & FY27 Outlook

	(Rs. Lakh Crore)				(% of GDP)			
	FY25 PE	FY26 BE	FY26 UBI RE	FY27 UBI BE	FY25 PE	FY26 BE	FY26 UBI RE	FY27 UBI BE
Capital expenditure	10.2	11.2	11.3	12.4	3.2%	3.1%	3.2%	3.2%
of which:								
Roads	2.7	2.7	2.7	2.8	0.8%	0.8%	0.8%	0.7%
Railways	2.5	2.5	2.5	2.6	0.8%	0.7%	0.7%	0.7%
Defence	3.4	3.8	3.8	4.6	1.0%	1.1%	1.1%	1.2%
Centre's Capex ex defence	5.5	5.9	6.8	7.0	1.7%	1.6%	1.9%	1.8%

Source: CEIC, Budget Documents, DIPAM & UBI Research

Drivers of fiscal consolidation in FY26 & FY27

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FY26 UBI estimates over FY26 Budget estimates

Fiscal boost	% of GDP	Fiscal Drag	% of GDP
Higher Non-tax Revenue	0.05%	Lower Tax Revenue	-0.36%
Lower Revex	0.36%	Slip in divestments	-0.04%
		Higher Capex	-0.01%
Total	**0.41%**	**Total**	**-0.41%**
		Net impact on fiscal deficit	**0.0%**

Change in % of GDP	FY26 URE over FY26 BE
Total Receipts	-0.34%
Revenue Receipts	-0.31%
-Gross Taxes	-0.54%
-Direct Taxes	-0.12%
Corporate Tax	*-0.01%*
Income Tax	*-0.11%*
-Indirect Taxes	-0.42%
GST	-0.37%

FY27 UBI estimates over FY26 UBI estimates

Fiscal boost	% of GDP	Fiscal Drag	% of GDP
Higher tax Revenue	0.01%	Lower Non-tax Revenue	-0.02%
Lower Revex	0.21%	Slip in divestments	-0.05%
Total	**0.22%**	**Total**	**-0.07%**
		Net impact on fiscal deficit	**0.15%**

Change in % of GDP	**FY27 UBI BE over FY26 UBI (our est)**
Total Receipts	**-0.06%**
Revenue Receipts	**-0.01%**
-Gross Taxes	**0.02%**
-Direct Taxes	**0.00%**
Corporate Tax	***0.00%***
Income Tax	***0.00%***
-Indirect Taxes	**0.02%**
GST	**0.00%**

Source: CEIC, Budget Documents, DIPAM & UBI Research

Expenditure rationalisation in FY26/27 primarily seen in Revex ex interest payments & subsidies

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(Rs. Lakh Crore)	FY26 BE	Apr-Nov FY26	Gap from Budget	Growth needed in Dec-Mar FY26 to meet BE target
Total exp	50.65	29.26	21.39	11.7%
Capex	11.21	6.58	4.63	-14.0%
Interest payments	12.76	7.46	5.31	15.9%
Subsidies	3.83	2.88	0.95	-12.6%
Revex	39.44	22.68	16.77	21.8%
Revex ex interest & subsidies	22.85	12.34	10.51	29.8%

Source: CEIC, Budget Documents & UBI Research

Unveiling the detailed fiscal math

	(Rs. Lakh Crore)				(% of GDP)			
	FY25 PE	FY26 BE	FY26 UBI RE	FY27 UBI BE	FY25 PE	FY26 BE	FY26 UBI RE	FY27 UBE
Total Receipts	30.78	34.96	33.75	36.90	9.3%	9.79%	9.5%	9.4%
Revenue Receipts	28.62	34.20	33.13	36.40	8.7%	9.58%	9.3%	9.3%
-Gross Taxes	36.20	42.70	40.81	44.95	10.9%	11.96%	11.4%	11.4%
-Direct Taxes	21.70	25.20	24.79	27.27	6.6%	7.06%	6.9%	6.9%
Corporate Tax	9.87	10.82	10.80	11.88	3.0%	3.03%	3.0%	3.0%
Income Tax	11.83	14.38	14.00	15.40	3.6%	4.03%	3.9%	3.9%
-Indirect Taxes	14.51	17.50	16.01	17.68	4.4%	4.90%	4.5%	4.5%
GST	9.09	11.78	10.46	11.51	2.7%	3.30%	2.9%	2.9%
-Net tax revenues	23.24	28.37	27.11	29.88	7.0%	7.95%	7.6%	7.6%
-Non Tax Revenue Receipts	5.38	5.83	6.01	6.52	1.6%	1.63%	1.7%	1.7%
Non Debt Capital Receipts	0.42	0.76	0.63	0.50	0.1%	0.21%	0.2%	0.1%
Total Expenditure	46.56	50.65	49.48	53.61	14.1%	14.19%	13.9%	13.6%
-Revenue Expenditure	36.04	39.44	38.18	41.18	10.9%	11.05%	10.7%	10.5%
-Capital Expenditure	10.52	11.21	11.30	12.43	3.18%	3.14%	3.16%	3.16%
Fiscal Deficit	15.77	15.69	15.73	16.71				
Fiscal Deficit as a % of GDP	4.77%	4.40%	4.40%	4.25%				

➢ **Assumptions**

I. Tax buoyancy of ~1%

II. Nominal GDP growth of ~10%

III. GST compensation cess will discontinue from 1st Feb’26

IV. RBI dividend : record levels likely to be repeated at ~Rs 2.5-3 lakh cr. in FY27

V. PSU dividends also likely to maintain good momentum

VI. Capex push to persist

Source: CEIC, Budget Documents, DIPAM & UBI Research

Finance Commission report: will we see much-needed radical reforms in states fiscal dynamics?

- *A key assumption of our fiscal math is that revenue sharing between centre and states would bee similar in FY27 vis-à-vis FY26. In this regard, the 16th Finance Commission report, to be tabled in Parliament along with the Budget will be in focus.*

- *Currently, centre shares 41% of gross taxes (excluding cesses and surcharges) with the states, as per the 15th Finance Commission recommendations. The sharing formulae is premised on various parameters, including a weighted sum of population, area, demographic performance, fiscal effort, income distance and forest cover.*

- *Apart from the tax devolution, centre also provides for grants and other transfers including those for centrally sponsored schemes to states and union territories*

- *While we will closely watch for trends in transfer of resources to states, devolution formulae, it would also be key to note any conditionalities / roadmap for state finances, a key pain point in general government fiscal and debt dynamics as highlighted by the Economic survey as well*

- *Hence, there is macro urgency to have a handle on states finances. In this regard, we will closely watch if the Finance Commission will lay down the following:*

  - **Fiscal roadmap for states targeting fiscal deficit to come down to sub-3% of GSDP in a prescribed time period**

  - **As centre moves towards debt to GDP targeting during FC period, any such roadmaps or targeting paths in case laid out for individual states**

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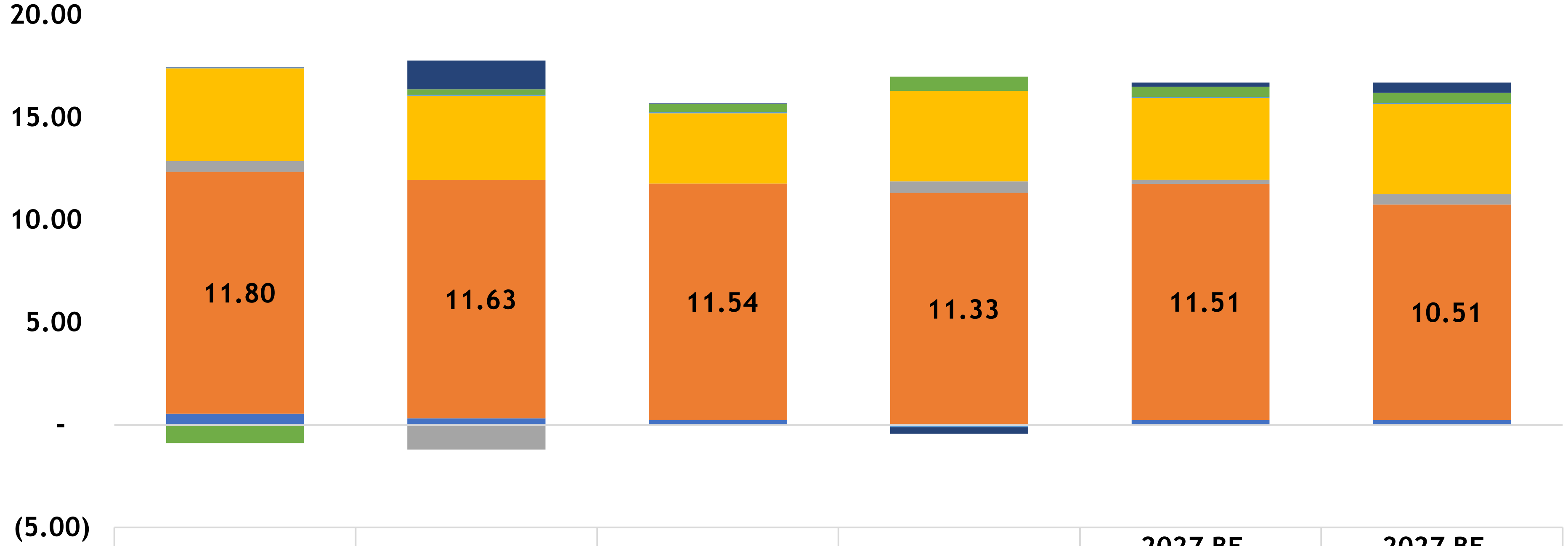
Diving deep into fiscal financing

Financing the Fiscal Deficit : small savings & use of Tbills may create space for lower Gsec borrowings



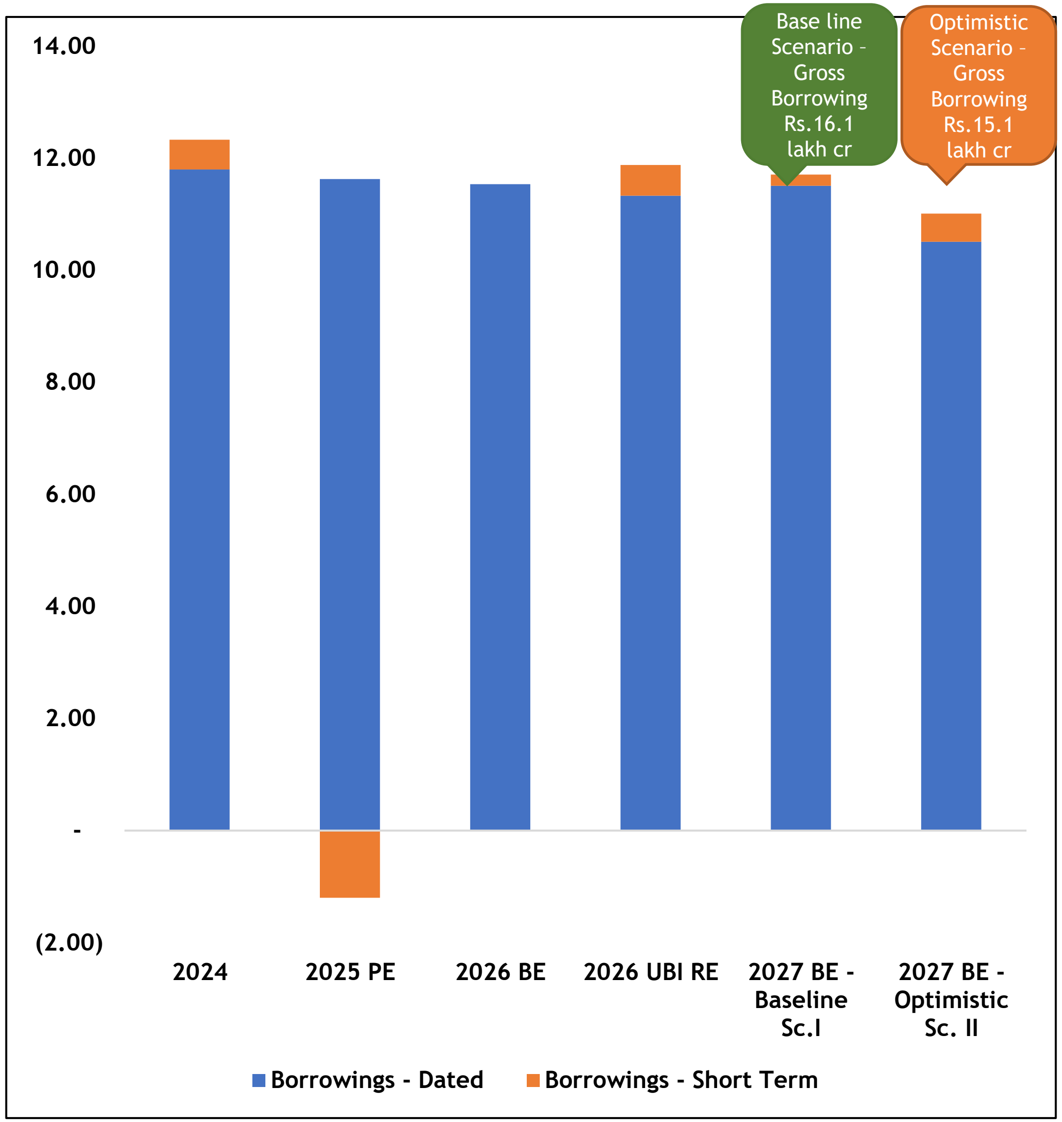
	2024	2025 PE	2026 BE	2026 UBI RE	2027 BE - Baseline Sc.I	2027 BE - Optimistic Sc. II
Cash Balance (adj for buybacks)	0.01	1.40	0.02	(0.32)	0.20	0.50
Others (Public account)	(0.89)	0.26	0.41	0.70	0.50	0.50
State provident funds	0.05	0.05	0.05	(0.11)	0.05	0.05
Small savings	4.51	4.12	3.43	4.41	4.00	4.40
Borrowings - Short Term	0.53	(1.20)	-	0.55	0.20	0.50
Borrowings - Dated	11.80	11.63	11.54	11.33	11.51	10.51
External	0.55	0.32	0.23	(0.00)	0.25	0.25

Source: Budget documents, UBI research

Borrowings likely to be Rs.16.1 lakh cr (gross) & Rs.11.5 lakh cr (net) in baseline scenario while scope for +ve surprise remains

Rs. Lakh Crore	2026 Est.	2027 BE Baseline Sc.I	2027 BE Optimistic Sc.II
Market borrowings - Dated	14.61	16.1	15.1
Redemption as on 27th Jan 2026	-	-	-
G-Sec Buyback till date	-	-	-
Further buyback expected	-	-	-
Net Redemptions	3.96	5.47	5.46
o/w funded by GST Compensation cess fund	0.68	0.86	0.86
Net Borrowings	**11.33**	**11.51**	**10.51**

Buyback of Rs.0.87 lakh crore during FY26 has been adjusted from Drawdown of Cash Balance.



Source: Budget documents, UBI research

Possibility of a sharp favorable surprise in borrowings remains even as Finance Minister is known for being "conservative & credible"

Base line Scenario - Gross Borrowing Rs.16.1

Optimistic Scenario - Gross Borrowing Rs.15.1

Rs. Lakh Crore	2024	2025 PE	2026 BE	2026 UBI RE	2027 BE - Baseline Sc.I	2027 BE - Optimistic Sc. II
External	0.55	0.32	0.23	-0.00	0.25	0.25
Borrowings - Dated	11.80	11.63	11.54	11.33	11.51	10.51
Borrowings - Short Term	0.53	-1.20	-	0.55	0.20	0.50
Small savings	4.51	4.12	3.43	4.41	4.00	4.40
State provident funds	0.05	0.05	0.05	-0.11	0.05	0.05
Others (Public account)	-0.89	0.26	0.41	0.70	0.50	0.50
Cash Balance (adj for buybacks)	0.01	1.40	0.02	-0.32	0.20	0.50
Total Financing	16.57	16.58	15.69	16.56	16.71	16.71

➢ **Assumptions**

I. Higher reliance on Small Savings
II. Higher Cash Drawdown
III. Higher Public Account Funding
IV. Switches for RBI Redemptions
V. Buybacks for market Redemptions

Source: Budget documents, UBI research

Overall Bond supply likely to be elevated in FY27 at c.Rs 28-29 lakh cr

Rs. In Lakh Crore	2022A	2023A	2024A	2025A	2026 RE	2027 BE - Baseline Sc.I	2027 BE - Optimistic Sc. II
Centre							
- Gross	11.27	14.21	15.43	14.01	14.61	16.10	15.10
- Net	8.63	11.08	11.03	10.39	11.33	11.49	10.50
SDLs							
- Gross	7.02	7.58	10.07	10.73	12.18	12.90	12.90
- Net	4.92	5.19	7.17	7.53	8.62	8.85	8.85
Total							
- Gross	18.29	21.79	25.50	24.74	26.79	29.00	28.00
- Net	13.56	16.27	18.20	17.93	19.95	20.34	19.35

Source: Budget documents, RBI and UBI research

Reform announcements are key focus are in this Budget

Reforms to make deposits attractive for banks to have sufficient funds to support high credit growth (1)

Policy Focus	Policy proposal	Rationale
Boost deposit growth for banks to have sufficient funds to support high credit growth	**Present status:** Interest earned on Bank Deposits is clubbed with total income & income tax is applicable as per the respective tax slabs. However, gains (short-term/ long term) from sale of MFs & Equities is taxed at Special rates of 20% & 12.5% respectively, making them attractive vis-à-vis Bank deposits in the hand of investors. **Policy recommendation**: Interest income from Bank's deposits may also be taxed at 12.5%.	Interest on Bank deposits is chargeable at normal tax rates: Interest on Bank deposits should be taxed at lower rate like capital gains to give a level playing field for Bank deposits and capital markets
	Present status: In terms of section 194A of the Act, subject to the prescribed exceptions, if the Bank is responsible for paying to a resident any income by way of interest (other than income by way of interest on securities) beyond the threshold of INR 50,000 (INR 1,00,000 in case of senior citizens), it has to deduct income-tax thereon at the rates in force (i.e. 10%). **Policy recommendation**: Threshold for non-deduction of TDS on Interest other than 'Interest on securities' u/s 194A may be increased to better align with inflation trends for both: - residents other than senior citizens - residents senior citizens	To promote the Bank's Term deposits, with TDS applicable only after increased threshold limit. Further, the deduction u/s 87A is available to the assessee, if their Income does not exceed 12 lakhs under new tax regime. This will be neutral to the revenue.

Source: UBI research

Reforms to make deposits attractive for banks to have sufficient funds to support high credit growth (2)

Policy Focus	Policy proposal	Rationale
Boost deposit growth for banks to have sufficient funds to support high credit growth	Applicability of TDS and TCS provisions on various income streams of bank. **<u>Policy recommendation</u>**: Blanket exemption should be provided to banks from applicability of TDS on various income streams. Similarly, banks should be exempted from TCS provisions.	The income streams of banks are subject to TDS other than those specifically exempted from TDS. Application of TDS on various income streams of banks create unnecessary administrative difficulty to banks.
	<u>Other Policy recommendations:</u> ➢ LCR relaxation for green deposits mobilization and clear roadmap for utilization of the green deposits ➢ Offer additional tax incentives for deposits with lock-in periods beyond 5 years, creating a stable long-term funding base ➢ Like PPF, Interest earned and total maturity amount at the end of the term should be exempt from taxes for Tax Saver Deposits.	To get long term funds for Banks as part of their role in funding Viksit Bharat 2047 goals

Source: UBI research

Laying the red carpet for foreign investors & boosting financial markets

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Sr No.	Policy Focus	Policy proposal	Rationale
1	Modernising foreign investor taxation	Transition from source-based to residence-based taxation for foreign investors, including reconsideration of long-term capital gains treatment	Currently, penalizing capital gains tax for FII investors as no other Asian economy is charging 20% tax on investment gains (even if threshold comes down if done via GIFT City). Hence, aligning India's tax framework with international practice would lower friction for overseas investors and improve India's competitiveness in attracting global capital.
2	Phased tax reform for trusted investors	Begin residence-based tax benefits with a defined group of regulated and compliant foreign investors under the SWAGAT-FI framework	A targeted approach limits revenue risk while signalling policy intent and encouraging stable, long-duration foreign investment
3	Revenue-neutral market taxation	Offset tax reforms through calibrated adjustments in transaction-based levies such as capital gains tax, STT, wherever appropriate	Maintains fiscal balance while shifting the overall tax burden away from long-term investment returns, improving market efficiency
4	Overseas diversification by residents	Gradually relax limits to allow Indian households and mutual funds to allocate a higher share of savings to global assets	Limited outward investment improves risk diversification, eases domestic valuation pressures, and over time enables larger and more sustainable foreign capital inflows into India
5	Broadening domestic investment avenues	Strengthen and expand access to non-equity instruments such as bonds, REITs/InvITs, municipal securities, and commodities for retail investors	A more balanced asset mix reduces excessive dependence on equities and helps build deeper capital markets, which are more attractive to long-term foreign investors

Promoting sectors like Defence to help wade through geopolitical uncertainties

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Sr No	Policy Theme	Budget Proposal	Rationale
1	Defence Budget Enhancement	Increase overall defence allocation by 12–20% to ₹7.6–8.2 lakh crore	To address evolving security challenges and ensure adequate funding for modernization and preparedness
2	Military Modernization	Higher capital outlay for procurement of aircraft, naval vessels, artillery, drones, and missile systems	To replace ageing equipment and enhance combat readiness of the Armed Forces
3	Indigenous Defence Production	Increase funding for Make in India (Defence), iDEX, and ADITI schemes	To reduce import dependency and strengthen domestic defence manufacturing ecosystem
4	Defence Research & Development	Enhanced allocation to DRDO for advanced and future technologies	To develop critical technologies such as aero engines, AI, cyber, space, and hypersonic systems
5	Defence Exports Promotion	Budgetary support and incentives to achieve ₹50,000 crore exports by 2028–29	To position India as a global defence exporter and earn foreign exchange. Guided Pinaka rockets and indigenous ammunition consignments were flagged off for export, demonstrating real payoffs of Make in India and export push
6	Naval Capacity Building	Increased funding for submarines, destroyers, and indigenous shipbuilding	To strengthen maritime security and protect India's strategic interests in the Indo-Pacific
7	Aerospace & Aero Engines	Allocation of ₹48,614 crore for aircraft and engine development	To achieve self-reliance in critical aviation technologies
8	Defence Infrastructure	Increased spending on border roads, logistics, and military housing	To improve mobility, deployment speed, and living conditions for personnel
9	Ease of Doing Business	Reforms to streamline procurement and faster project approvals	To encourage private sector participation and reduce project delays
10	MSMEs & Startups	Financial and policy incentives for defence MSMEs and startups	To promote innovation, job creation, and technology development

Focus on customs duty rationalization & other reforms to boost manufacturing, ease of doing business & deregulation (1)

SrNo	Policy Theme	Budget Proposal	Rationale
1	Customs Duty Rationalization	Rationalization of customs duty rates across select product categories, Higher customs duty on select finished goods and lower duty on raw materials	To simplify tariff structure and improve trade efficiency, to encourage domestic value addition and import substitution
2	Make in India Alignment	Customs duty adjustments aligned with Make in India and PLI schemes	To enhance competitiveness of domestic manufacturers
3	Trade Facilitation	Increased budgetary support for digital customs clearance and risk-based inspections	To reduce clearance time and logistics costs
4	Export Promotion	Duty exemptions and remission schemes for export-oriented units	To boost exports and global market integration
5	Critical Inputs & Strategic Sectors	Reduced customs duty on critical inputs for electronics, renewables, defence, and semiconductors	To strengthen strategic and high-tech sectors
6	Green & Sustainable Trade	Lower customs duty on green technologies and clean energy equipment	To support India’s climate and sustainability commitments
7	MSME Import Support	Simplified customs procedures and concessional duties for MSMEs	To reduce cost pressures and improve competitiveness amid tariff circumstances.
8	Anti-Dumping & Safeguards	Strengthening anti-dumping duties and safeguard measures	To protect domestic industry from unfair trade practices

Focus on customs duty rationalization & other reforms to boost manufacturing, ease of doing business & deregulation (2)

Sr No	Policy Theme	Budget Proposal	Rationale
9	Manufacturing Growth Push	Increased budgetary support to boost manufacturing-led growth	To raise manufacturing's share in GDP and create large-scale employment
10	Production Linked Incentive (PLI) Expansion	Extension and expansion of PLI schemes to additional manufacturing sectors	To incentivize scale, efficiency, and global competitiveness
11	MSME Manufacturing Support	Enhanced credit, subsidies, and technology upgradation support for MSMEs	To strengthen MSME contribution to industrial output and jobs
12	Ease of Doing Business	Simplification of regulatory approvals and compliance requirements	To reduce operational costs and attract domestic and foreign investment
13	Infrastructure for Manufacturing	Increased allocation for industrial corridors, logistics parks, and clusters	To reduce logistics costs and improve supply chain efficiency
14	Skill Development	Budgetary support for skill training aligned with manufacturing needs	To address skill gaps and improve productivity
15	Technology & Innovation	Incentives for adoption of Industry automation, and digital manufacturing	To enhance productivity and future-readiness of Indian manufacturing
16	Green Manufacturing	Fiscal incentives for energy-efficient and low-carbon manufacturing	To promote sustainable industrial growth
17	Export-Oriented Manufacturing	Support for export incentives and trade facilitation measures	To integrate Indian manufacturing with global value chains
18	FDI Promotion	Policy and fiscal measures to attract higher FDI in manufacturing	To bring capital, technology, and global best practices

Thank You !

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