KPMG

India Union Budget 2026-27

Point of view

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Public Finance

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Key announcements for the sector

The Union Budget 2026-27 marks a decisive strengthening of India's Public Financial Management (PFM) framework by combining disciplined fiscal consolidation with a sustained commitment to capital-led growth. Set against a nominal GDP of INR 393 lakh crore, the Budget reflects a strategic pivot from post-pandemic countercyclical spending to a structurally anchored fiscal approach focused on transparency, expenditure quality, and medium-term sustainability.

- Expenditure
  - A critical development for PFM is the calibrated rise in total expenditure to INR 53.47 lakh crore, maintaining growth while avoiding expansionary pressures. What stands out is the continued prioritisation of capital formation. Capital expenditure is budgeted at INR 12.22 lakh crore, while effective capital expenditure rises to INR 17.15 lakh crore, representing over 32 per cent of total expenditure. This shift tilts the composition of public spending decisively toward asset creation and long-term productivity enhancement. From a PFM standpoint, the fact that effective capex (INR 17.15 lakh crore) exceeds the fiscal deficit (4.3 per cent of GDP ≈ INR 16.9 lakh crore) signals that borrowings are being channeled into productive assets rather than revenue-linked consumption - a hallmark of prudent fiscal management.
- Tax revenue
  - On the revenue side, the Budget projects gross tax receipts of INR 44.04 lakh crore, broadly aligned with the 10 per cent nominal GDP growth assumption. With income tax at INR 14.66 lakh crore and corporation tax at INR 12.31 lakh crore, direct taxes now contribute nearly 39 per cent of gross tax revenue, reflecting strong formalisation and improved compliance. GST collections of INR 10.19 lakh crore reinforce revenue stability through a broad-based consumption tax. For the PFM ecosystem, this predictable revenue profile enhances budgetary credibility, supports accurate medium-term fiscal projections, and reduces uncertainty in resource allocation.
- Fiscal federalism
  - Fiscal federalism also remains central to the PFM narrative. The Budget provides INR 25.44 lakh crore in total transfers to States, including INR 15.26 lakh crore as tax devolution and INR 1.40 lakh crore in Finance Commission grants, ensuring rule-based, transparent financial flows. Importantly, the continuation of interest-free loans under the Special Assistance to States for Capital Investment (SASCI) enhances States' capacity to undertake capital expenditure - critical as States now account for nearly two-thirds of general government capex. This strengthens cooperative fiscal governance, improves alignment between Union and State investment strategies, and supports stronger outcome-based budgeting at sub-national levels.

- Borrowings and fiscal consolidation
  - The consolidation strategy is equally significant from a PFM lens. The fiscal deficit is budgeted at 4.3 per cent of GDP, down from 4.4 per cent in the previous year, while the primary deficit is contained at 0.7 per cent of GDP - demonstrating disciplined expenditure control even amid capex scaling. The revenue deficit of 2.8 per cent and a sharply reduced effective revenue deficit of 0.3 per cent confirm the narrowing gap between revenue income and revenue expenditure, an essential indicator of strengthening operational efficiency in public finances. The projected decline in central government debt to 55.6 per cent of GDP, from 56.1 per cent in FY 2025-26, reinforces long-term debt sustainability and aligns with the medium-term target of 50±1 per cent by 2030-31.

Implications for the sector

- Quality of expenditure
  - The Budget's emphasis on effective capital expenditure of INR 17.15 lakh crore (≈4.4 per cent of GDP) represents a decisive strengthening of expenditure quality from a PFM lens. By directing a larger share of public outlays toward asset creation - transport infrastructure, energy transition, logistics networks, and urban development – the Government enhances both allocative efficiency (better prioritisation of high-impact sectors) and operational efficiency (improved outcomes per rupee spent)
  - The expanding capex-to-deficit ratio signals a structural shift: borrowings are increasingly being deployed for long-term productive assets rather than short-term revenue expenditure. This supports higher fiscal multipliers, crowds in private investment, and reduces the risk of fiscal slippage, reflecting a more mature and disciplined expenditure framework.
- Tax revenue composition
  - The evolving tax structure – marked by a rising share of personal income tax and steady inflows from corporation tax - indicates a more resilient and diversified revenue base. From a PFM standpoint, this enhances revenue predictability, allowing the Government to anchor medium-term fiscal planning on stable and broad-based tax streams
  - The growing contribution of direct taxes reflects structural shifts: greater formalisation of labour markets, expanding digital compliance, and a wider tax base. While corporate tax rates remain stable, ongoing rationalisation of exemptions and incentives will be central to sustaining tax buoyancy without compromising the simplicity or equity of the tax system. This balanced revenue composition reduces volatility and strengthens the foundation for multi-year budgeting.
- Fiscal federalism
  - With States increasingly driving India's public capital formation, the Budget underscores the importance of predictable, rules-based, and timely fiscal transfers. The combination of tax devolution, Finance Commission grants, and continued interest-free capital assistance equips States to undertake large-scale infrastructure investments and improve service delivery
  - From a PFM viewpoint, this strengthens the architecture of cooperative federalism by enhancing both fiscal capacity (through assured resources) and fiscal autonomy (by enabling State-led prioritisation of capital projects). Improved Centre–State coordination - especially in utilisation of capital assistance - will be critical for maximizing developmental outcomes and ensuring consistent adherence to fiscal responsibility norms across tiers of government.

- Fiscal prudence and credibility
  - The Budget reinforces fiscal credibility by adhering to a transparent and rule-based consolidation path. With the fiscal deficit anchored at 4.3 per cent of GDP, the primary deficit at 0.7 per cent, and the debt ratio trending downward towards medium-term targets, the Government signals strong commitment to long-term sustainability
  - For the PFM ecosystem, this reinforces confidence in the stability and predictability of India's fiscal framework. Steady consolidation without compromising capital expenditure enhances macroeconomic stability, supports favorable credit assessments, and aligns fiscal strategy with the medium-term goals of the Sixteenth Finance Commission period. Rule-based fiscal management - combined with transparent disclosure of deficit and debt trajectories - fortifies India's fiscal reputation globally.

In summary, these four dimensions demonstrate that the Union Budget 2026-27 adopts a measured, credible, and PFM-aligned strategy. By elevating the quality of public expenditure, strengthening revenue stability, deepening cooperative federalism, and maintaining prudent fiscal discipline, the Budget places India's public finances on a stronger and more sustainable trajectory. As the Sixteenth Finance Commission period begins, this framework supports India's broader aspiration of progressing toward Viksit Bharat through robust, efficient, and future-ready public financial management.

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