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Does the budget have room for greater spending and tax relief?

Devina Mehra | 29 January 2026

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SUMMARY

Tax collections are falling short of official estimates and demands on the budget are piling up. As usual, there are expectations of tax concessions, although what the economy may need are enlarged outlays on health, education and employment. The FM faces an unenviable task.

On the surface, India appears to have the ultimate Goldilocks economy: one of the highest GDP growth rates in the world with historically low inflation—exactly what any government would want. In theory, this should give the government tremendous flexibility and room in the upcoming budget. However, drill down a little deeper and gaps begin to appear that will result in some furrowed brows.

As per the statistics ministry's first advance estimates for 2025-26, India's real GDP is estimated to grow at 7.4%, which makes India arguably the world's fastest growing major economy. However, nominal GDP, or GDP in current rupee terms, is projected to grow only 8%. This is against a two-decade average of approximately 12%.

While the headline GDP number talked about is always the real growth rate (GDP at constant prices), most concrete and measurable numbers in the economy, from corporate profits to tax collections, are tied to nominal GDP growth. As mentioned above, this has been anaemic at 8%.

When the budget was presented last year, the nominal GDP growth rate was estimated at 10% plus. Based on this, corporate tax collections were budgeted to grow at 10.7% and GST at 10.9%.

Surprisingly, and this is something I pointed out in this column at the time, in spite of hefty personal tax cuts, the mop-up from these taxes (or 'non-corporate tax' as per budget documents) was budgeted to grow at 14.4%.

The only explanation I could come up with was that the finance ministry was expecting hefty inflows from capital market related taxes. The securities transaction tax (STT) was estimated to rise by 40%. As I had said then, "While the regulator may be talking against excess speculation, many including the government seem to be banking on it."

Now with a slowdown in nominal GDP as well as a weaker-than-expected performance of the stock market, tax collections have been running way below the budgeted numbers. In spite of giving substantially lower refunds, even total net tax collections have grown only 8% from April 2025 to 11 January 2026, versus the 11% budgeted. If this trend continues for the rest of the months of this fiscal year, there will be a shortfall of over ₹1.3 trillion in tax collections against the budgeted number.

Meanwhile every participant in the Indian economy has given a wish list to the government, which typically includes either some tax concession or increased government spending in their area. In reality, the government has very little leeway for tax cuts or increased spending. Given the sluggish tax collections, there is simply no room available for concessions, unless it lets the fiscal deficit balloon. The latter may not be a palatable option.

The other thing to remember is that for the last few years, Indian GDP growth has been mainly dependent on government spending. Capital expenditure by the government has gone up nearly five times in the past decade.

Of course, as this newspaper pointed out a few days ago, not all of it has been productive. For instance, while an airport has been built every 50 days for the last few years, many of these are unutilized or under-utilized; 15 new airports are unutilized and nearly 50 have less than five flights a day. Hence, I am sure there is scope for some cutting in government expenditure, but it will nevertheless have a sobering impact on GDP growth.

And since it is budget season, there are always questions about my wish list. Unlike most others in my business, my list typically does not centre around the corporate world or capital markets. To my mind, the priorities the government should focus on are education, health, employment and research. These are not glamorous and the results don't show up in a single year. But spending on these heads compounds over time. These are the building blocks for a great country and economy.

For instance, India spends only 3% to 4% of its GDP on education. The target of 6% is still a long way off and rare is the budget whose education spend is even in line with nominal GDP growth. For perspective, China spends 6% plus and given that its GDP is roughly five times ours, the amount is seven-and-a-half times ours.

Now for health. As per survey data and research studies, India has the highest number of undernourished and anaemic children in the world, with about one-third being underweight and more than two-thirds being anaemic.

Even if our focus is solely on economic growth rather than society, remember education and health are the building blocks needed for us to have people who are employable. Our demographic dividend can give us returns if and only if we find jobs for our young people, which in turn means that they must have education and skills. Not to forget that this bulge of working-age Indians is available only for a limited period of time before India's population plateaus and then begins to decline.

Research is where we went above and beyond in the early years of the Republic, but have now fallen far behind with only 0.6% of GDP being spent on R&D. China spends 25 times the amount we do on research. In a fast-changing world, we need more emphasis and spending on this. The finance minister sure faces a tough ask this time.

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