

Fiscal Account

Refer to important disclosures at the end of this report

Bracing for slippages and changing rates market dynamics

- Centre's latest decision to dismiss vaccine decentralization and tiered-pricing is indeed an optimal strategy to maximize welfare and minimize cost for general government. However, the flipside is that Centre's vaccination budget would swell to ~Rs450-550bn (0.2% of GDP) vs. estimated Rs100-120bn based on the earlier arrangement between Centre and States
- In sum, Centre's FY22 fiscal math is likely to get disturbed by ~0.5% to 7.3% of GDP. The fiscal hit in the form of lower divestment, higher doles on food/fertilizer subsidy, health and NREGA may outstrip buffers such as bumper RBI surplus and wholesale inflation-led higher nominal GDP. Capex adjustment (cuts) could turn out to be the balancing/offsetting factor.
- FY22 Gross G-sec borrowings could increase by Rs650bn+ on top of Rs12.05tn. This, in conjunction with additional issuances of Rs1.6tn for GST compensation to states, will ensure pressure be felt across the G-sec curve. The GSAP+OMOs might have to be propped up beyond Rs6tn to balance the ensuing supply-demand mismatch and keep yields range-bound.
- In the near term, we are neutral on bonds amid the central bank's active support anchored at the benchmark 10-yr paper. However, we see yields inching up in an orderly and gradual fashion in H2FY22. We expect the yield curve to bear-flatten and see benchmark 10-yr yield in the range of 6.0-6.40% for the remainder of FY22.

The cost of vaccination: changing dynamics?

Centre's latest proposition to take over the vaccination drive from states is a welcome decision. We reckon that the centralization of negotiations and administration will improve vaccine efficiencies. While this would reduce net cost to general government, Centre's health spending burden will increase. The total cost of universal jabbing by Centre - which we assume will also include below-18 age category post Oct'21 - is estimated to increase to ~Rs450-550bn (~0.2% of GDP), assuming: (1) majority of the supply remains dominated by current domestic players at Rs150 per jab, but the costing landscape changes from Jul'21 and Nov'21 with enhanced role of foreign players; (2) private sector also covers 20-25% of the eligible population; and (3) there is ~10% wastage and administration costs. This compares to budgeted cost of Rs350bn for FY22, and is way above our initial estimated cost of Rs100-120bn in the earlier arrangement where only 25% of the national population (45+) was being targeted by the Centre. Now additional fiscal pressure on states will ease as most had not taken (high) vaccination cost in their budgets. Earlier strategy would have disproportionately pained state finances, with UP, MP and Chhattisgarh leading the pack.

Centre's fiscal deficit/GDP may slip ~0.5% from the budgeted 6.8% in FY22

Amid various push and pull, there is a likelihood of fiscal slippage to the tune of around 0.5% from the initially budgeted 6.8%. Even accounting for positives budget buffers such as bumper RBI surplus and higher nominal GDP on higher wholesale inflation, factors like (1) higher doles payouts than budgeted on food, fertilizer subsidy, health and NREGA, (2) possible miss on ambitious divestment targets, and (3) possible fading of the positive upside surprises on conservatively budgeted tax estimates will outweigh on the fiscal math. As of now, **we are not taking major cuts in Centre's budgeted capex**. The government narrative is still capex-driven, pushing both CPSE and its own machinery for capex frontload. But we reckon some capex cuts could be an offsetting factor. Despite the slippage, **the effective fiscal impulse will still be negative in FY22**. Given the limited efficacy of monetary easing currently, continued countercyclical fiscal policy support—and avoiding a premature consolidation—remains crucial.

Borrowings slippage by another ~Rs650-700bn; Bear-flattening of Gsec curve bias in H2FY22

As we move ahead, G-sec bond demand-supply dynamics may worsen across the curve. Amid the expected fiscal slippage, we estimate the gross G-sec loans could increase by Rs650-700bn in FY22 over and above Rs12.05tn budgeted and could pressure the belly of the curve (10-14yr). The supply will be further compounded by recently announced additional G-sec issuances worth Rs1.6tn (likely in H2FY22) to compensate states for GST shortfall and could likely be in the 3-5yr segment. With higher T-bill issuances than budgeted, the shorter end (3M-1yr) may also see pressure.

The stress on RBI will therefore intensify to keep bonds range-bound at current levels and GSAP+OMO purchases may have to be propped up beyond Rs6 tn in FY22 (our current estimate Rs4.5-5tn). However, this will likely be the story of H2FY22. In the near term, we remain neutral on G-sec bonds, helped by the central bank's visible and invisible hand. We reckon **even as yields may inch up orderly and gradually over the year, the curve will likely still flatten ahead, with the RBI keeping the 10-yr yield as rates anchor**. We expect the yield curve to bear-flatten and see the benchmark 10-yr yield in the range of 6.0-6.40% for the remainder of FY22.

Please see our model portfolio (Emkay Alpha Portfolio): [Nifty \(Page 5\)](#)

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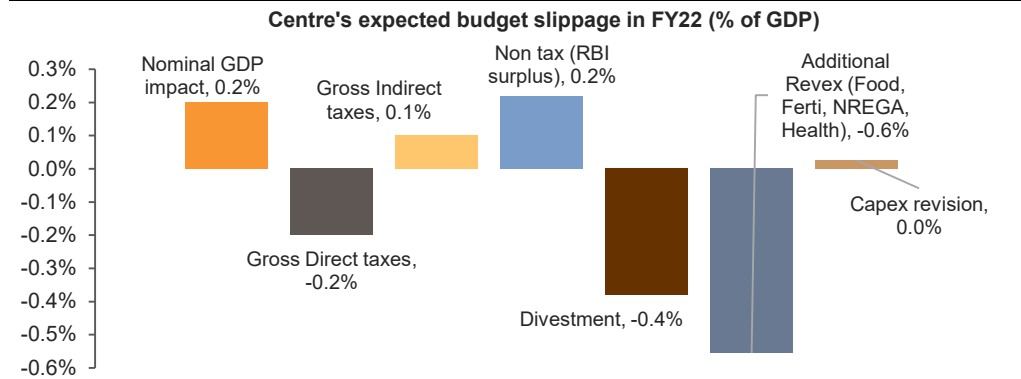
Key Highlights

- Centre's vaccination cost for 18+ age cohort to rise to Rs450-550bn vs. estimated Rs100-120bn in the earlier vaccine arrangement.
- Combined with other doles (food, fertilizer, NREGA), revex should slip by 0.6% of GDP in FY22.
- FY22 GFD/GDP to hit 7.3% assuming no meaningful capex cuts.
- Budget borrowings could increase by Rs650bn+ in FY22.
- Yield curve to bear-flatten; 10-yr yield is expected to range 6.0-6.40% in FY22, with pressure building only in H2FY22.

Centralization of negotiations and administration to improve vaccine efficiencies

As we had argued earlier, vaccine decentralization and tiered-pricing are sub-optimal and centralized negotiation, planning and coordination would lead to efficient pricing and quota bargaining with vaccination producers (virtually a monopoly). This, in conjunction with the prioritization of delivery of vaccines, appropriate supply to states as per population/population density/urban/rural ratio/wastage ratio etc., would improve distribution and administration efficiencies. We note that the private sector will still have to negotiate directly with vaccine producers for their 25% quota of vaccines produced. Our weighted measure of optimal vaccine distribution depicts that states such as UP, Delhi and TN have a much lower current share than they need, while GJ, RJ, and MH have received relatively more vaccines so far. (See our special report "Opportunity cost of sub-optimal vaccine strategy", May 11, 2021).

Exhibit 1: Higher doles and lower divestment to lead the fiscal slippage for Centre



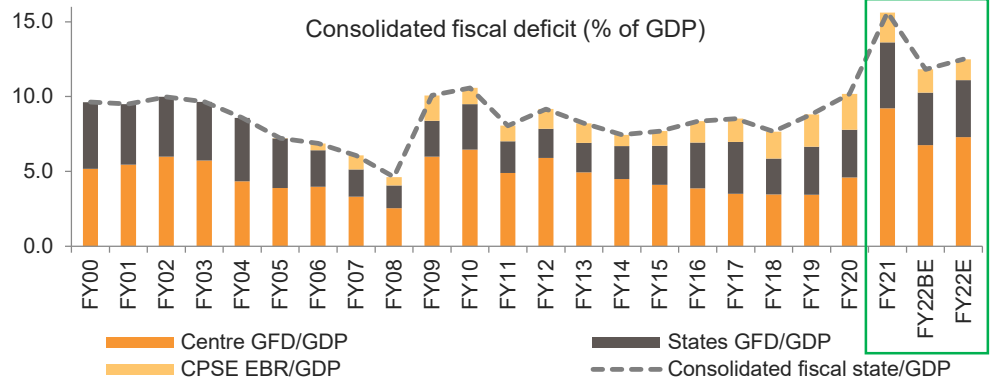
Source: India Budget, Emkay research estimates

Exhibit 2: Gross fiscal deficit to slip by 0.5% of GDP to 7.3% in FY22

% of GDP	FY19	FY20	FY21P	FY22BE	FY22E
Receipts breakdown					
Revenue receipts	8.2	8.3	8.3	8.0	8.0
Gross tax revenues	10.9	9.9	10.3	9.9	9.7
Direct taxes	6.0	5.2	4.8	5.0	4.7
Corporation tax	3.5	2.7	2.3	2.5	2.4
Income tax	2.5	2.4	2.4	2.5	2.3
Indirect taxes	4.9	4.7	5.5	4.9	5.0
Goods and Services Tax	3.1	2.9	2.8	2.8	2.8
Customs duty	0.6	0.5	0.7	0.6	0.6
Excise duty	1.2	1.2	2.0	1.5	1.6
Net tax revenues	6.9	6.7	7.2	6.9	6.7
Non-tax revenues	1.2	1.6	1.1	1.1	1.3
RBI transfer of surplus	0.4	0.7	0.3	0.2	0.4
Non-debt capital receipts	0.6	0.3	0.3	0.8	0.5
Disinvestments	0.5	0.2	0.2	0.8	0.4
Total Revenue receipts	8.8	8.6	8.6	8.9	8.5
Expenditure breakdown					
Revenue expenditure	10.6	11.6	15.6	13.1	13.4
Interest payments	3.1	3.0	3.5	3.6	3.5
Subsidies	1.2	1.3	3.5	1.7	2.0
Capital expenditure	1.6	1.7	2.2	2.5	2.4
Total expenditure	12.2	13.2	17.8	15.6	15.8
Gross fiscal deficit	3.4	4.6	9.2	6.8	7.3

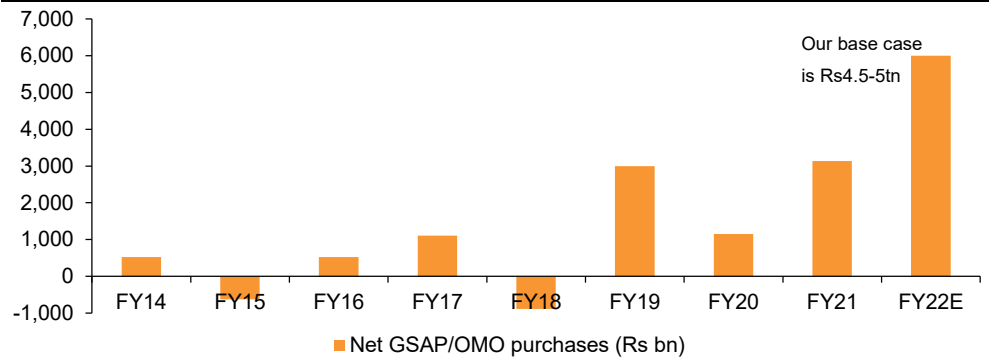
Source: India Budget, Emkay Research Estimates

Exhibit 3: Consolidated fiscal deficit expected to rise above 12% in FY22 but impulse will still fade



Source: CEIC, Emkay Research Estimates

Exhibit 4: Bond purchase amount might need to double from FY21 to keep yields range-bound



Source: RBI, Emkay Research estimates

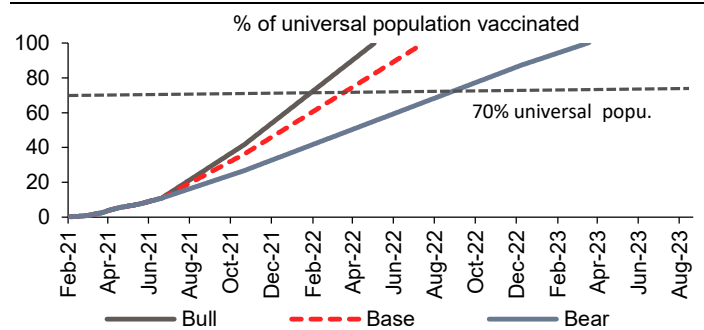
Exhibit 5: Centre's cost of jabbing for various age brackets

Estimated Vaccination Cost (Rs. Bn)	Centre		
	Universal Population	18+ Age and above	12+ Age and above
Upto 30th April	23	23	23
Upto 21st June	10	10	10
Post 21st June	652	419	508
Total Cost	684	450	540

Source: Census, Emkay Research estimates

Note: This assumes: (1) 10% wastage, logistic and administration cost; (2) Foreign supply will cost 5.5 times of domestic supply.

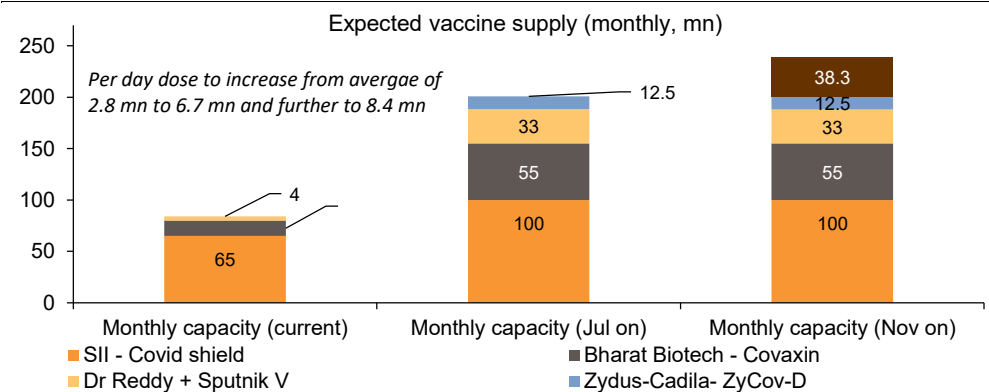
Exhibit 6: Realistically, universal population may be covered by Jul'22



Source: Census, Emkay Research estimates

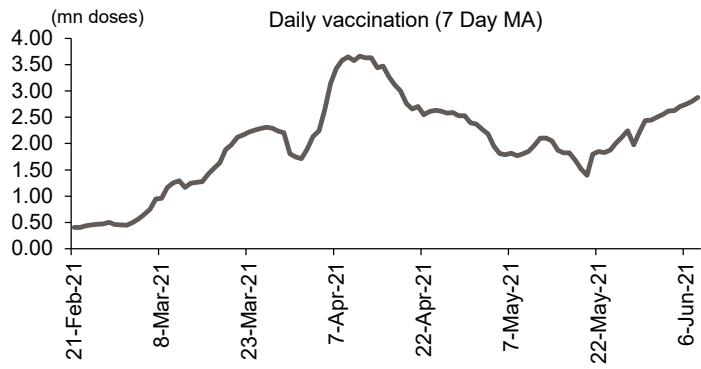
Note: 18+age bracket comprises of 70% of total population. With 70% of population likely to be completely jabbed by Mar'22, this age cohort can be assumed to be fully covered

Exhibit 7: Covishield to supply around 40% Nov'21 onward vs. 90% currently



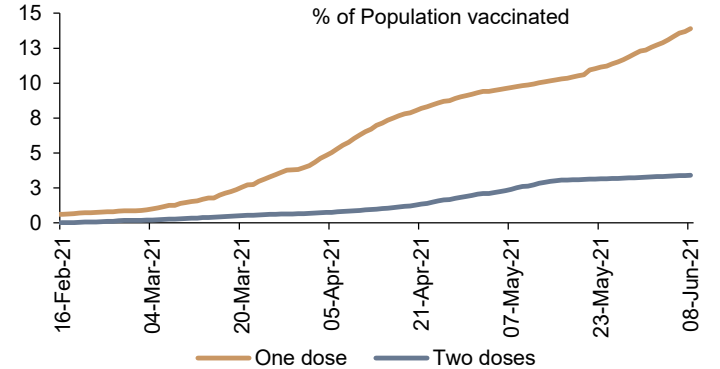
Source: Emkay Research Estimates, various media reports

Exhibit 8: Daily vaccination pace has picked up to 2.7mn doses



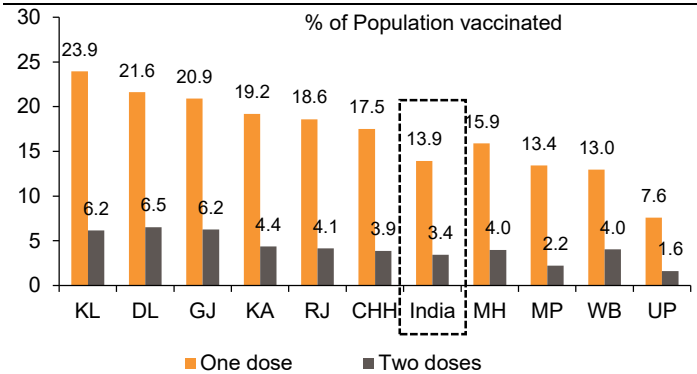
Source: CEIC, Emkay Research

Exhibit 9: Almost 14% of population has taken at least one dose



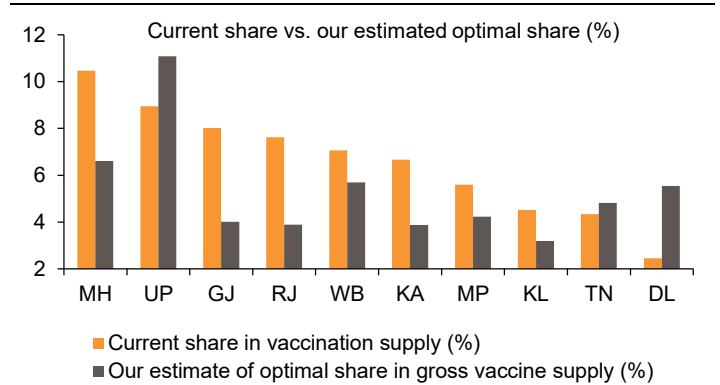
Source: CEIC, Emkay Research

Exhibit 10: UP lags the vaccination pack...



Source: CEIC, Emkay Research

Exhibit 11: ...and needs higher share than currently allocated



Source: CEIC, Emkay Research estimates

Emkay Alpha Portfolio – Nifty

EAP-Nifty (25 stocks)

Company Name	Nifty Weight	Nifty EAP Weight	OW/UW (%)	OW/UW (bps)
Agri Input & Chemicals	0.69	0.52	-25%	-17
UPL	0.69	0.52	-25%	-17
Auto & Auto Ancillaries	5.46	8.13	49%	267
Bajaj Auto	0.82	0.81	0%	0
Eicher Motors	0.57	1.18	109%	62
Hero Motocorp	0.58	0.58	0%	0
Mahindra & Mahindra	1.14	0.00	-100%	-114
Maruti Suzuki India	1.43	2.45	71%	101
Tata Motors	0.93	3.11	235%	218
BFSI-Banks	25.88	30.72	19%	484
Axis Bank	2.75	4.70	71%	195
Bandhan Bank	0.00	0.51	NA	51
HDFC Bank	9.49	9.36	-1%	-12
ICICI Bank	6.52	6.50	0%	-2
Indusind Bank	0.85	3.82	352%	297
Kotak Mahindra Bank	3.86	1.40	-64%	-246
State Bank of India	2.41	4.42	84%	202
BFSI-Insurance	1.40	1.87	34%	47
HDFC Life	0.84	0.32	-61%	-51
SBI Life	0.56	1.55	176%	99
BFSI-NBFCs	10.04	7.97	-21%	-207
Bajaj Finserv	1.04	0.00	-100%	-104
Bajaj Finance	2.24	0.00	-100%	-224
Cholamandalam Investment	0.00	1.02	NA	102
HDFC	6.76	5.92	-12%	-84
Shriram Transport Finance	0.00	1.03	NA	103
Cement & Building Materials	2.56	4.60	80%	204
Ambuja Cements	0.00	0.51	NA	51
Grasim Industries	0.84	0.84	0%	0
Shree Cements	0.57	1.60	182%	103
Ultratech Cement	1.15	1.64	43%	49
Consumer Goods & Retail	10.99	6.69	-39%	-430
Asian Paints	1.94	1.45	-25%	-49
Britannia Industries	0.62	1.14	82%	51
Hindustan Unilever	3.09	0.00	-100%	-309
ITC	2.74	1.76	-36%	-98
Nestle India	0.92	0.00	-100%	-92
Titan Company	1.05	0.78	-26%	-27
Tata Consumer	0.63	0.00	-100%	-63
United Breweries	0.00	0.54	NA	54
United Spirits	0.00	1.03	NA	103
Engineering & Capital Goods	2.75	2.74	0%	-1
Larsen & Toubro	2.75	2.74	0%	-1
Information Technology	16.26	15.23	-6%	-103
HCL Tech	1.54	2.54	65%	100
Infosys	7.69	7.66	0%	-3
TCS	4.87	1.85	-62%	-302
Tech Mahindra	0.96	1.98	106%	102
Wipro	1.20	1.19	0%	0
Metals & Mining	3.59	4.05	13%	47
Coal India	0.48	0.48	-1%	0
Hindalco	0.83	1.31	58%	48
JSW Steel	1.00	1.00	0%	0
Tata Steel	1.27	1.26	0%	-1
Oil & Gas	12.29	8.15	-34%	-413
BPCL	0.67	1.43	114%	76
Indian Oil	0.44	1.22	181%	79
ONGC	0.67	1.21	80%	54
Reliance Industries	10.52	4.29	-59%	-622
Pharmaceuticals	3.52	4.95	41%	143
Cadila Healthcare	0.00	0.51	NA	51
Cipla	0.71	1.45	104%	74
Divi's Lab	0.79	0.00	-100%	-79
Dr. Reddy's Lab	0.94	1.67	78%	73
Sun Pharma	1.08	1.32	23%	25
Ports & Logistics	0.94	0.00	-100%	-94
Adani Ports	0.94	0.00	-100%	-94
Power	1.69	1.94	15%	25
NTPC	0.81	0.81	0%	0
Power Grid Corporation	0.88	1.13	29%	25
Telecommunications	1.94	2.44	26%	50
Bharti Airtel	1.94	2.44	26%	50
Cash		0.00		
Nifty	100.00	100.00		

Source: Emkay Research; Note: *We have internally capped single stock exposure to 10% in our EAP

Sector portfolio NAV

	Base					Latest
	1-Apr-19	9-Jun-20	8-Dec-20	9-Mar-21	7-May-21	8-Jun-21
EAP - Nifty	100.0	85.5	109.1	124.3	123.2	131.7
Nifty50	100.0	86.1	114.8	129.4	127.0	134.9

*Performance measurement base date 1st April 2019

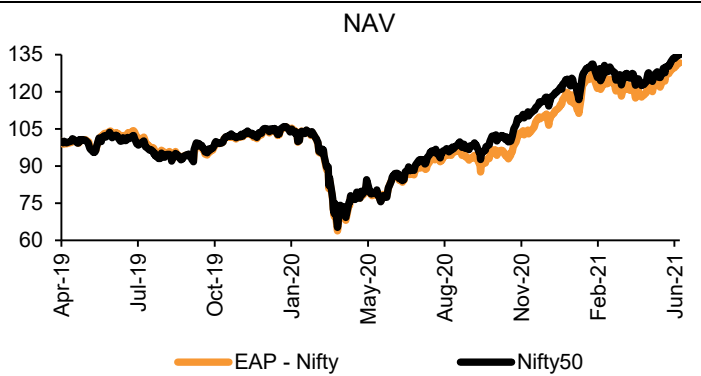
Source: Emkay Research

Price Performance (%)

	1m	3m	6m	12m
EAP - Nifty	6.9%	5.9%	20.7%	54.0%
Nifty50	6.2%	4.3%	17.5%	56.7%

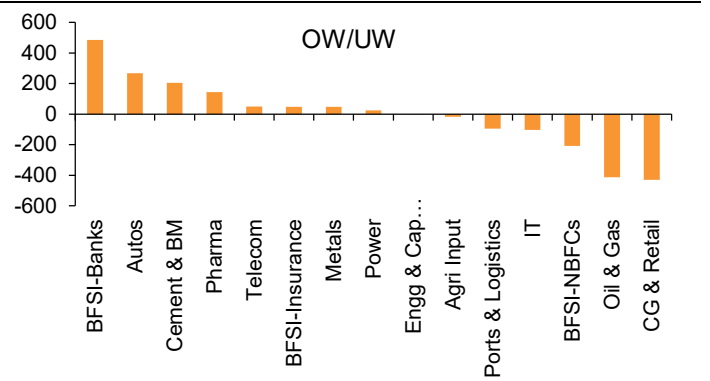
Source: Emkay Research

NAV chart



Source: Emkay Research

Sector OW/UW



Source: Emkay Research

Please see our model portfolio (Emkay Alpha Portfolio): [SMID](#)

“Emkay Alpha Portfolio – SMID and Nifty are a supporting document to the Emkay Alpha Portfolios Report and is updated on regular intervals”

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Ratings	Expected Return within the next 12-18 months.
BUY	Over 15%
HOLD	Between -5% to 15%
SELL	Below -5%

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