Pre-Budget Analysis 2026-27

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Introduction

The Union Budget 2025–26 is framed by a challenging global landscape of slowing growth, trade uncertainty, and weakened external demand. Domestically, the government is balancing a strict fiscal consolidation path against high public expectations driven by uneven growth and employment stress.

Consequently, this Budget represents a strategic choice between competing priorities rather than unrestricted spending. This analysis evaluates these choices through three primary lenses: macroeconomic stability, social welfare and capital expenditure, and the critical challenges of employment and skills.

Section I: Macroeconomic Trends and Fiscal Federalism

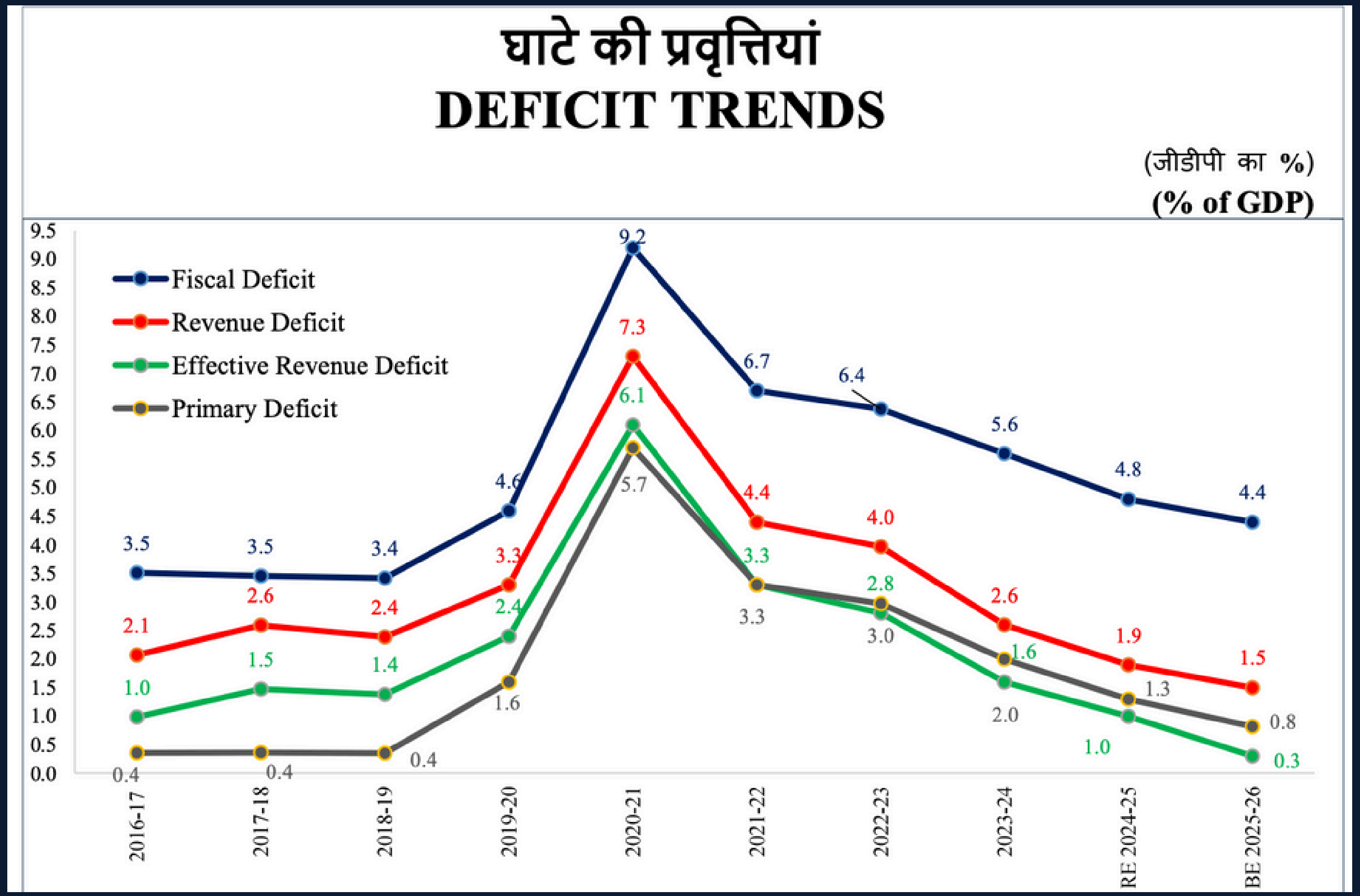
1. Fiscal Deficit, Revenues, and Overall Stability

- The fiscal deficit target set at 4.4% for the 2025-26 budget indicates continued fiscal consolidation, but at a slower pace, reflecting revenue uncertainty amid global slowdown.

- Budget math for FY 2025–26 assumes tax revenue growth of 11% over the FY 2024–25 estimates, hence the receipt budget puts gross tax revenue at ₹42.70 lakh crore for the year.

- Direct taxes are levied primarily on personal income and corporations, making them progressive in nature, hence individuals and corporations with higher profits pay a higher proportion of tax and face significantly higher burden.

- This allows governments to mobilise resources while limiting the burden on consumption. However, because direct taxes are sensitive to business cycles, global slowdowns or declines in commercial earnings, they are a relatively volatile revenue source.



Source: India budget 2024-2025

- A global economic slowdown affects government finances through a clear transmission chain: weaker global demand reduces exports, which in turn compresses corporate revenues and profit margins, especially in export oriented sectors.

- Lower profitability directly impacts corporate tax collections, with subdued wage growth, bonuses, and capital gains affecting personal income tax receipts. The slowdown also weakens linked domestic activity, affecting logistics, intermediaries, and ancillary services, thereby dampening GST collections. As a result, even if tax rates remain unchanged, overall tax revenues may fall short of budgeted targets due to cyclical pressures originating outside the domestic economy.

- Managing the fiscal deficit in such conditions requires a balance between raising revenues and controlling expenditure. On the revenue side, governments tend to prioritise tax buoyancy through compliance, base broadening, and administrative efficiency, rather than aggressive rate hikes that could further suppress demand.

- On the expenditure side, fiscal discipline focuses on containing non-productive or rigid spending while protecting growth-enhancing outlays such as capital expenditure and essential welfare support. Effective deficit management, therefore, does not rely solely on cutting spending or increasing taxes, but on calibrating both. Hence, ensuring sufficient revenues to fund priorities while maintaining expenditure quality to support medium term growth and fiscal sustainability.

2. Centre–State Relations and Transfers

- In the Union Budget, total state transfers, including state's share in taxes, grants and loans alongside releases with centrally sponsored schemes amounts to Rs.25.6 lakh crore. This stands at an increase of Rs. 4,91,668 crore over the last financial year (2023-2024).

- Transfers through tax devolution, grants, and centrally sponsored schemes, are structured to balance fiscal autonomy, equity, and national policy coordination.

- Tax devolution, guided by the Finance Commission, involves sharing a portion of Union tax revenues with States in a specified and largely untied basis, thereby correcting vertical and horizontal imbalances while preserving State autonomy.

- Grants supplement this by addressing specific fiscal gaps or needs that persist even after devolution, such as revenue deficits or sector specific requirements, and may be conditional or unconditional.

- Centrally Sponsored Schemes, by contrast, are tied and cost-shared transfers designed by the Union to implement national priorities through State governments, with funding linked to compliance, matching contributions, and performance criteria.

- The Investment Friendliness Index of States, announced in the Union Budget, is intended to create a standardised, comparable measure of how conducive each State's regulatory and institutional environment is for investment. It assesses factors such as ease of doing business, regulatory certainty, infrastructure readiness, and administrative efficiency. The Index seeks to promote competitive cooperative federalism, encouraging States to undertake reforms that improve investor confidence.

- Fiscally stronger states, those with higher own-tax revenues, better fiscal balances, and stronger administrative capacity, are generally better positioned to access and fully utilise union funds. Meanwhile, fiscally weaker states, despite often having greater developmental needs, face constraints in providing co-financing, meeting procedural requirements, or absorbing funds efficiently, which can lead to underutilisation or delayed releases. As a result, the effective access to funds can diverge from the intended equitable allocation, even when formal eligibility exists.

- Performance linked frameworks link financial support to measurable outcomes or reforms, aiming to improve efficiency and accountability in public spending. While such mechanisms can incentivise better governance and service delivery, they also raise equity concerns. States that already possess stronger fiscal and institutional capacity are more likely to meet performance benchmarks, thereby securing additional resources.

- Comparitively, weaker states may struggle to qualify, potentially reinforcing existing disparities. Thus, without adequate equalisation safeguards or capacity-building support, performance-based transfers can shift the balance from redistribution toward efficiency, affecting equality across States within India’s fiscal federal structure.

3. GST and State Finances After Compensation

- Since its introduction in 2017, GST collections have shown a gradual but uneven upward trend. In recent years, especially post-pandemic, monthly GST collections have frequently crossed Rs.1.5 lakh crore, reflecting improved economic activity and better tax administration. However, growth has been cyclical rather than stable, closely tied to inflation, consumption demand, and formal sector performance. While nominal collections have risen, real growth has been more moderate.

- At the time of GST’s rollout, states were assured a 14% annual growth in GST revenues, irrespective of actual tax buoyancy. In practice, GST collections have fallen short of this benchmark, in context of during economic slowdowns such as COVID-19. This gap highlights the structural weakness of assuming a fixed growth rate in a tax system that is highly sensitive to macroeconomic conditions. The gap has created persistent fiscal stress for states, making them dependent on compensation transfers from the Centre.

- The GST compensation mechanism formally ended amidst 2022, shifting states to a regime where revenues depend solely on actual GST performance. This transition has increased fiscal uncertainty, particularly for consumption dependent and fiscally weaker states. States now face greater pressure to either compress expenditure or seek alternative revenue sources. The end of compensation has also sharpened debates around fiscal federalism, as some states argue that the original GST bargain has been only partially fulfilled.

- GST’s design aims for a broad tax base, but exclusions such as petroleum products, electricity, and real estate significantly limit revenue potential. Additionally, the multiple rate structure and frequent rate rationalisation have complicated compliance. While digital tools like e-invoicing, have improved compliance over time, smaller businesses continue to face administrative burdens, affecting effective tax collection.

- The Goods and Services Tax Council serves as the core institutional forum for cooperative federalism under GST, where the Centre and states jointly decide on rates, exemptions, and procedural reforms. While the Council has enabled uniformity and coordination, the decision making process causes delayed reforms and constrained outcomes. After the end of compensation, disagreements within the Council have become more pronounced, reflecting divergent fiscal priorities between the Centre and states.

4. Cesses, Surcharges, and the Divisible Pool

- The Union government's growing reliance on cesses and surcharges marks a structural shift in fiscal architecture with profound federalism implications. Unlike shareable taxes that form part of the divisible pool, cesses and surcharges remain entirely with the Centre, insulating a rising share of revenue from constitutional devolution obligations. As states' share in the divisible pool is increased to 41 per cent under the 15th Finance Commission, the Centre then compensated itself by shifting towards non-shareable levies.

- What began as a temporary shift has become a permanent one. The Health Cess, effectively replacing the GST Compensation Cess, exemplifies this pattern. By shifting the attention toward cesses on consumer products such as fuel, tobacco, and vehicles rather than income tax and corporation tax, the Centre retains control over funds that would otherwise flow to states.

- This creates a paradox, on paper, the Centre transfers ₹25.6 lakh crore to states, but the shrinking divisible pool means that the states are receiving a smaller proportion of total central revenue than the Finance Commission formula suggests. Performance-linked frameworks like the Investment Friendliness Index, combined with diminished unconditional transfers, convert fiscal federalism into a system of conditionality. States must now compete for funds that were once guaranteed by constitutional design.

5. Tax Rebates and Remittances in Context

- The 2025-26 Budget's tax rebates are planned to boost domestic demand in a situation of weak demand. The zero-tax threshold, under the new taxation system, is increased to ₹12 lakh because of the increased rebate under Section 87A. This will result in a savings increase of approximately ₹1.10 lakhs per year for some taxpayers, thereby boosting their disposable income by 0.7-0.8 per cent of the GDP. When combined with the reduction in the rate of GST in September 2025, the above efforts target a revival in urban demand, which contributes above 60 per cent to the GDP.

- Despite this, tax relief is constrained by a broader environment created by remittances. India receives Rs.11.60 lakh crore (136 billion USD), which is sufficient for financing almost 50% of its merchandize trade deficit and in excess of 10 per cent of current inflows. The outcome obtained from this increase is mainly fueled by Indians employed in countries with high per capita incomes like America and Europe.

- However, the buffer zone is under pressure. The remittance tax of 1 percent imposed by the United States since January 2026 will lower remittances by an estimated 1.6 percent, with the largest effect on India. For millions of families, particularly in the countryside and semi-urban areas, remittances have constituted a welcome complement to stagnant domestic pay. In the absence of a dependable source of income, the recovery of consumption remains precarious.

6. Monetary Policy Environment and Fiscal–Monetary Interaction

- The Union Budget gains added relevance in a monetary environment that is currently accommodative. Interest rates have been on a downward trajectory, while inflation has moderated sharply. In December 2025, the RBI reduced the policy repo rate by 25 basis points to 5.25 per cent, taking cumulative rate reductions for the year to 125 basis points, following a fall in inflation to 1.25 per cent in October. The central bank has also revised its FY26 growth projection upward to 7.3 per cent and retained a neutral policy stance, signalling scope for further rate action if conditions permit.

- This interest-rate environment provides the government with greater fiscal room. Lower borrowing costs help contain the fiscal deficit, targeted at 4.4 per cent of GDP, even as the Centre projects a strong 11 per cent growth in tax revenues. Softer rates also strengthen the transmission of public spending to the real economy and support household demand through lower repayment burdens on housing and vehicle loans.

- That said, the alignment between fiscal policy and monetary conditions is not assured. The RBI's ability to maintain an accommodative stance hinges on inflation remaining under control, particularly food prices and import-related costs. Any resurgence in price pressures would constrain monetary policy space and reduce the effectiveness of fiscal stimulus. External risks further complicate the outlook: with the rupee at historic lows and the current account deficit widening, the central bank must balance growth considerations with the need to manage currency stability.

- For the moment, fiscal consolidation and supportive monetary conditions are broadly aligned, but this balance remains fragile. It depends on sustained inflation moderation, stable remittance inflows, and favourable global financial conditions. A deterioration in any of these could quickly weaken the macroeconomic buffer that currently allows the government to pursue higher spending alongside accommodative monetary policy.

Section II: Welfare Schemes, Social Spending, and Capex Choices

1. Capital Expenditure and Growth Strategy

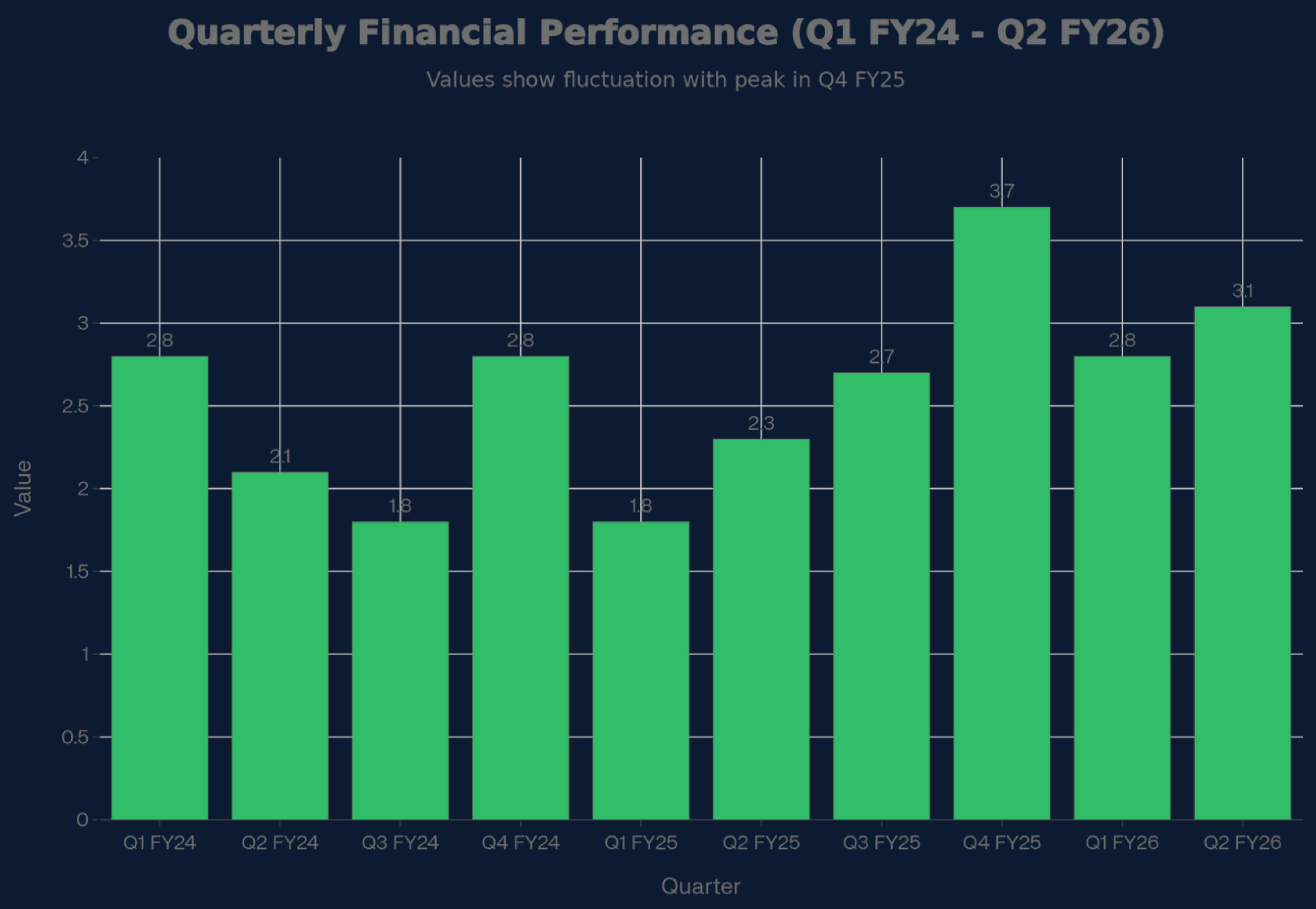
• Central capex surged 40% in H1 FY26, with FY26 budgeted at ₹11.21 lakh crore (3.1% of GDP)

• Roads and railways remain dominant, accounting for approximately 50% of central capex, with growth at 21.7% and 5.6% respectively in H1 FY26

• Quarterly performance shows peak allocation in Q4 FY25 at 3.7 trillion rupees, followed by softening to 3.1 trillion in Q2 FY26, indicating lumpy execution patterns

• Public capex is designed to catalyse private investment; corporate capex grew 11% to 9.4 trillion rupees in FY25, with the power sector leading at 72.6% growth

• Implementation bottlenecks persist with land acquisition delays, environmental clearances averaging 12 months, and skilled labour shortages constraining execution timelines



Source: ET EDGE

• State-level capex grew 13% in H1 FY26, with Maharashtra, Gujarat, and Karnataka posting 33–34% growth, but disparities remain acute

• Capex-to-employment pipeline operates with a typical lag of 6–18 months from approval to execution to job creation, while wage-based welfare schemes deliver immediate income

• Project completions in H1 FY26 reached 4.1 trillion rupees, the majority (63%) from government projects in transport services, but are concentrated in infrastructure rather than direct employment support

• Private sector investment announcements surged 15% to 15.1 trillion rupees in H1 FY26, yet capex intentions fell 26% to 4.9 trillion in FY26 versus 6.6 trillion in FY25, signalling slack between intention and deployment

• Capital goods order books grew 20.7% in FY25, a leading indicator of medium-term capex deployment, but downstream employment generation remains uncertain

• Asset-creation focus (roads, railways, power) builds long-term productive capacity but does not provide immediate purchasing power to vulnerable populations dependent on consumption support

• Strategic tension: balancing fiscal consolidation (4.4% deficit target) against immediate welfare needs reflects constrained fiscal space for both capex growth and welfare expansion

2.Welfare Schemes and Social Protection

• MGNREGS allocation remains unchanged at ₹86,000 crore for FY26, matching FY25 RE, down from ₹89,154 crore in FY24, reflecting zero nominal growth over three years

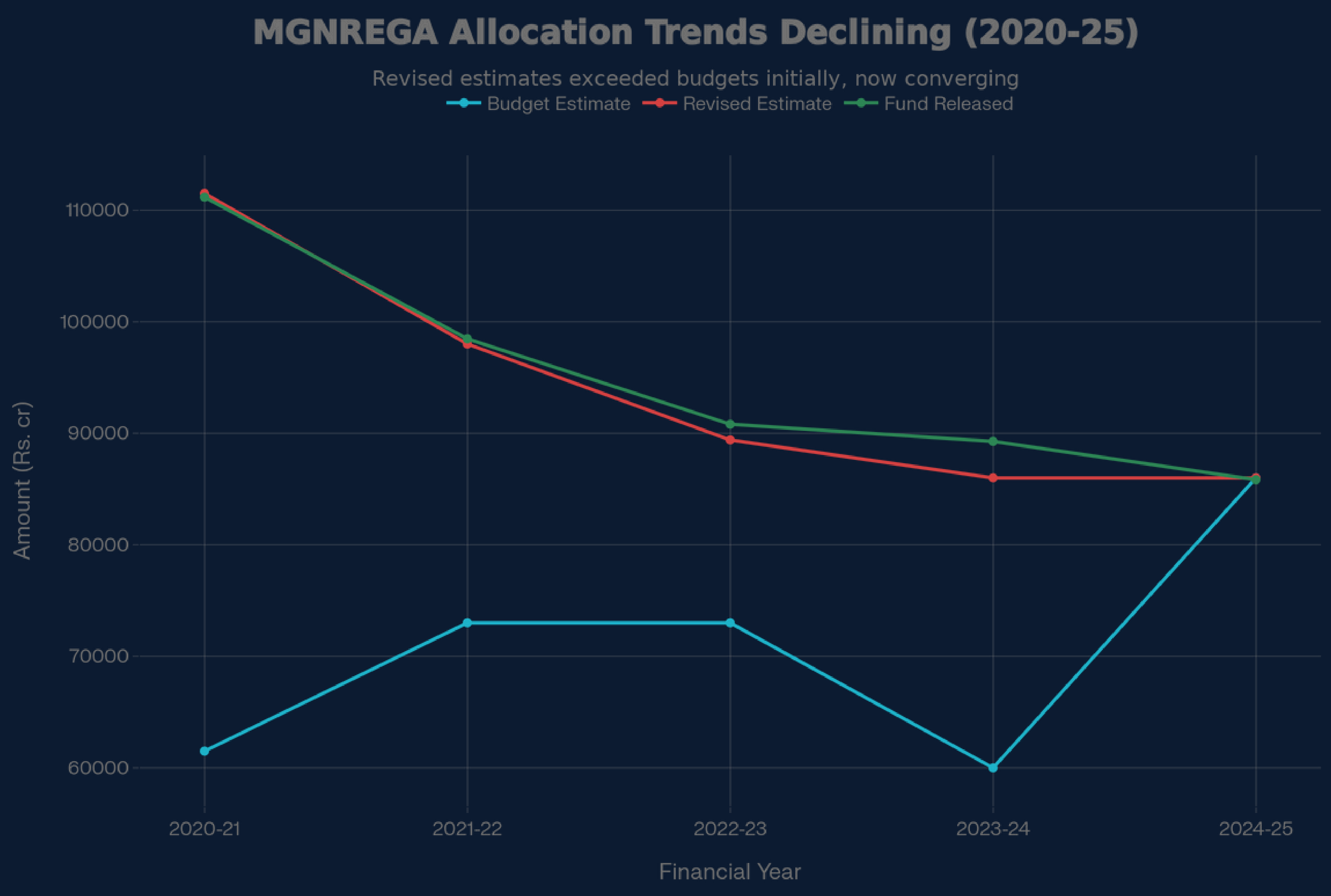
• PM-KISAN allocation stagnant at ₹63,500 crore for FY26, with no increase from FY25 revised estimate, despite inflation pressures and farm debt stress

• In real terms (inflation-adjusted), both schemes face purchasing power erosion; nominal freeze translates to 12–15% real decline over FY24–FY26 when adjusted for WPI/CPI inflation

• MGNREGS demand peaked during COVID but has not returned to pre-pandemic levels, indicating partial labour market recovery masking structural rural employment weakness

• Together, MGNREGS and PM-KISAN account for approximately ₹149,500 crore (1.8% of the union budget), signalling that welfare spending remains subordinate to capex priorities

• Budget silence on these schemes—neither mentioned in FM's budget speech for the second consecutive year—suggests policy deprioritization of rural income support



Source - Press Information Bureau, Government of India (Self Made)

3. Sectoral and Regional Spending Patterns

• Urban Challenge Fund of ₹1 lakh crore and Pradhan Mantri Awas Yojana urban allocation of ₹78,126 crore (64% increase from FY25 RE) underscore concentrated capex focus on urban asset creation and housing

• Rural capex allocation estimated at ₹1,90,406 crore (8.3% increase), dominated by PMAY-Rural, Jal Jeevan Mission (₹67,000 crore), and rural roads, but is portion-based rather than growth-driven relative to the capex envelope

• Urban capex generates asset appreciation and credit access for higher-income households; rural capex produces public goods (water, roads) with diffuse, delayed employment effects and no direct income transfer

• Rural employment support remains wage-based through MGNREGS (static allocation); urban housing policies favour asset ownership and EMI-driven consumption by middle-income groups

• State-level capex disparities persist: Maharashtra, Gujarat, Karnataka are accelerating at 33–34% growth, while fiscal weaker states (Himachal Pradesh, Assam, Mizoram, Meghalaya) struggle, reflecting dependency on central transfers

• K-shaped recovery patterns widen rural-urban income inequality; rural FMCG sales are declining while urban consumption is rebounding, signalling uneven multiplier effects from regional capex distribution

- ₹1.5 lakh crore allocated under 50-year interest-free loans to states for capital investment in FY26, maintaining centralised capex control via conditional transfer mechanism

- Unconditional state loans have declined from 80% in FY23 to 38% of total in FY26, with 62% now performance-linked, constraining the fiscal autonomy of fiscally weaker states

- Top 5 states (Uttar Pradesh, Maharashtra, Madhya Pradesh, Gujarat, Karnataka) command ~43% of state-level capex, entrenching concentration and limiting the capacity of backward regions to undertake independent capex programmes

- Reform conditions tied to capex transfers (governance, municipal reforms, land administration) impose a compliance burden on administratively constrained states, raising the effective execution cost

- Sectoral underspending persists: Jal Shakti revised estimate for FY25 was ₹51,558 crore against the budget of ₹98,714 crore (48% utilisation), indicating absorption bottlenecks despite high nominal allocations

- Regional capex disparities compound with welfare allocation freeze, deepening fiscal imbalance between infrastructure-focused, growth-accelerating states and welfare-dependent, employment-stressed regions

4. Health Spending and Human Development

• The Indian government has been very generous in its health budget over the last ten years, and at the moment, it is almost of 1.9-2.1% of the total GDP, which is a post-pandemic push toward strengthening health systems, but it still does not meet the National Health Policy (2017) target of 2.5% of GDP by 2025, the government is moving in the right direction.

• The government now accounts for almost half of total health expenditures, which is a major change from the previous scenario when the private sector bore most of the costs, but still, the household payments continue to be the second biggest source of financing healthcare in India.

• Around 40% of the total health spending still comes by way of out-of-pocket expenditures, and this shows that medical costs are still a significant cause of financial instability and distress, especially for families from middle and lower-income classes.

• The primary health care system in rural India is still characterized by severe shortages in infrastructure, despite the fact that the budget for health has been increased; official figures show that there is a 25% shortfall in Sub-Centres, a 31% shortfall in Primary Health Centres (PHCs), and a 64% shortfall in Community Health Centres (CHCs).

• These infrastructure shortcomings block access to preventive care, maternal and child health services, and early disease detection, which in turn, result in weakening long-term human development outcomes.

• The public health spending is still very much tilted in favor of operational and service-related expenses, with healthcare services such as salaries, medicines, and schemes consuming about 87.3% of the total spending and only 12.7% going to the creation of health infrastructure.

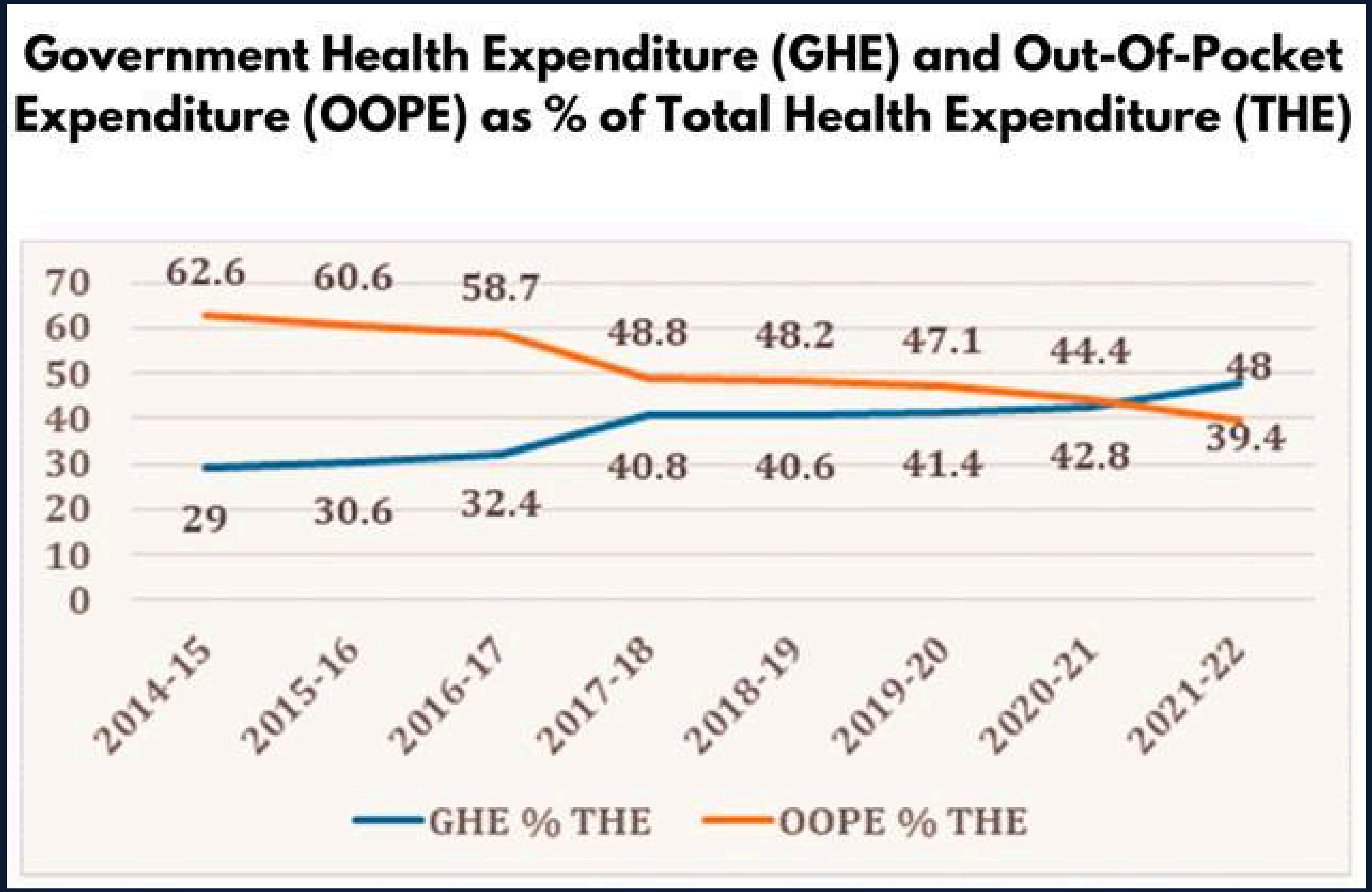
4. Health Spending and Human Development Continued

• Even if the health infrastructure investments have seen more than a two-fold increase since 2016, the expansion of capacity has not been able to fully accommodate the growth of the population, changes in the epidemiological profile, and the demand for quality healthcare that has been rising.

• The health outcome targets have shown mixed progress, with vaccination coverage topping 93%, which is indicative of the success of the public health interventions and mission-mode programmes that were implemented.

• Moreover, the ratio of doctors to the population continues to be around 1:1,511, which is lower than the WHO's recommended standard of 1:1,000, highlighting the ongoing lack of medical personnel, mainly in rural and isolated areas.

• The public health system in India spends almost 55% of its total health budget on primary health care, but still, the problems of not having enough staff, equipment, and facilities where the service is being delivered have been hindering the effectiveness of such delivery.



Source - National Health Accounts (NHA) of India.

5. Gender Budget and Social Inclusion

There has been a remarkable growth of the Gender Budget in the last few years since the allocations rose from about ₹3.27 lakh crore in BE 2024-25 to approx. ₹4.49 lakh crore in BE 2025-26, which indicates a nearly 37% annual increase.

• Consequently, the Gender Budget's proportion of the overall Union Budget has gone up to approximately 8.9%, signaling a more substantial fiscal dedication to women-oriented and gender fair development.

• The gender-related budgets are divided into three levels: full schemes that exclusively benefit women, those that have women making up 30-99% of the beneficiaries, and universal schemes that have a partial gender impact.

• The major areas of gender spending include job creation, health and nutrition, education and skill development, social protection, rural livelihoods, and financial inclusion.

• The trend of increased gender spending has coincided with better female participation in public sector jobs, which is evidenced by the fact that women account for more than 45% of the total person-days created through MGNREGA.

• The expansion of direct benefit transfer and cash transfer schemes targeted at women across multiple states highlights the growing importance of government policy on income support, household security, and women's financial autonomy.

• The higher gender allocations are expected to support the women's labour force participation improvements, which is still structurally low despite some recent gains.

6. Middle Class Consumption and Spending Trends

• The middle-class consumption has been growing steadily over the last ten years, thanks to the rise in incomes, urban migration, and the economy coming under the formal sector; in fact, household expenditure increased by about 33% since 2022.

• Presently, the middle class makes up approximately 31% of the Indian population, and it is estimated that this proportion might go up to almost 38% by 2031, thus, being a major driver of domestic demand.

• The patterns of consumption indicate a slow movement from food expenditure to non-essential and semi-essential categories like housing, transport, healthcare, education, and lifestyle services.

• At present, food and beverages are taking up around 26% of total household consumption, while the combined spending on housing, utilities, and transport is more than 30%, signifying higher hopes and pressures due to urban consumption.

• The outlay on healthcare and education has outpaced overall consumption growth, thus, showing that middle-class families are giving more importance to human capital investments.

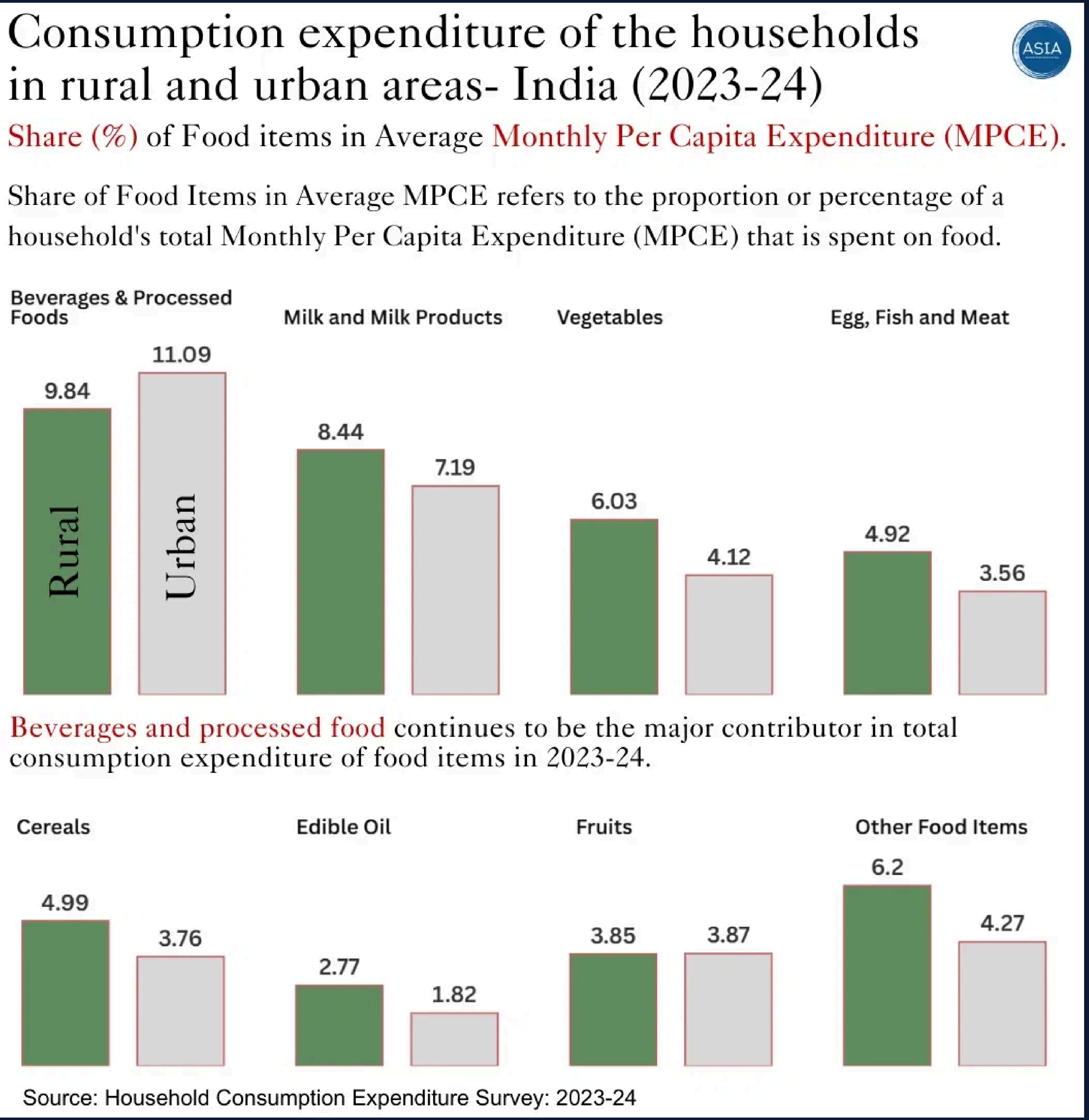
• Higher inflation, especially in food, fuel, and services, has limited the scope for discretionary spending and has also reduced real purchasing power, hence, leading to cautious consumption behavior.

• Tax concessions and nominal income increases have helped consumption somewhat, but these benefits have been partially neutralized by the rising cost of living.

•The total household loans and spending via EMIs have been on the rise, especially in the areas of housing, education, consumer goods and health care, which is a clear indicator of both credit availability and cost pressure.

• The higher credit dependence indicates the consumers' resilience that is being kept alive by loans besides the slow income increase, which is a worry about possible financial strains.

• To sum up, the middle-class spending patterns bring about a feeling of cautious optimism since the demand is still there but the confidence is still very sensitive to the factors such as inflation, interest rates, and employment stability.



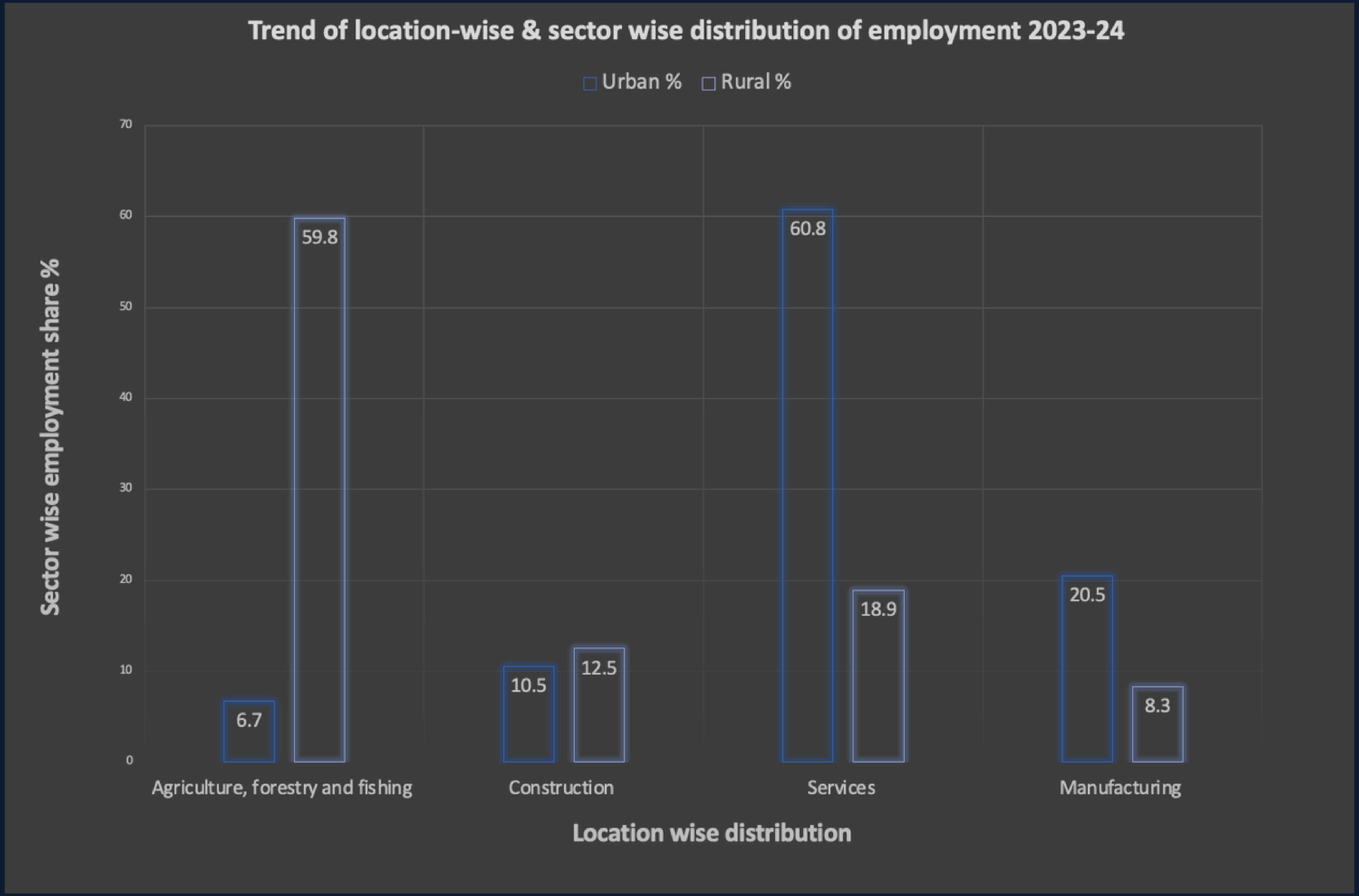
Section III: Employment, Informality, and Skills

1. Employment Trends and Policy Focus

- India’s employment trajectory continues to reflect a structural disconnect between output growth and labour absorption, particularly within services-led growth. As noted in the Economic Survey 2024–25, the annual unemployment rate for persons aged 15 years and above declined from 6.0% in 2017–18 to 3.2% in 2023–24, indicating an improvement in aggregate labour market outcomes. Over the same period, the share of self-employed workers rose to 58% in 2023–24, suggesting that a significant portion of employment expansion has occurred outside regular wage and salaried work.

- Despite this overall decline in unemployment, job-market stress remains unevenly distributed. The Economic Survey highlights that unemployment rates are highest among graduates aged 20–29, particularly in urban areas and among women, pointing to persistent educated unemployment. This pattern persists even as educational attainment has increased and services output has expanded, underscoring the limited capacity of services-led growth to generate stable, high-quality employment commensurate with rising skill levels.

- According to India’s Services Sector: Insights from Employment Trends and State-Level Dynamics (NITI Aayog, 2025), the services sector accounted for 29.7% of total employment in 2023–24, while remaining the largest contributor to Gross Value Added. The report explicitly notes this divergence between employment share and value-added share as a defining feature of India’s growth pattern.

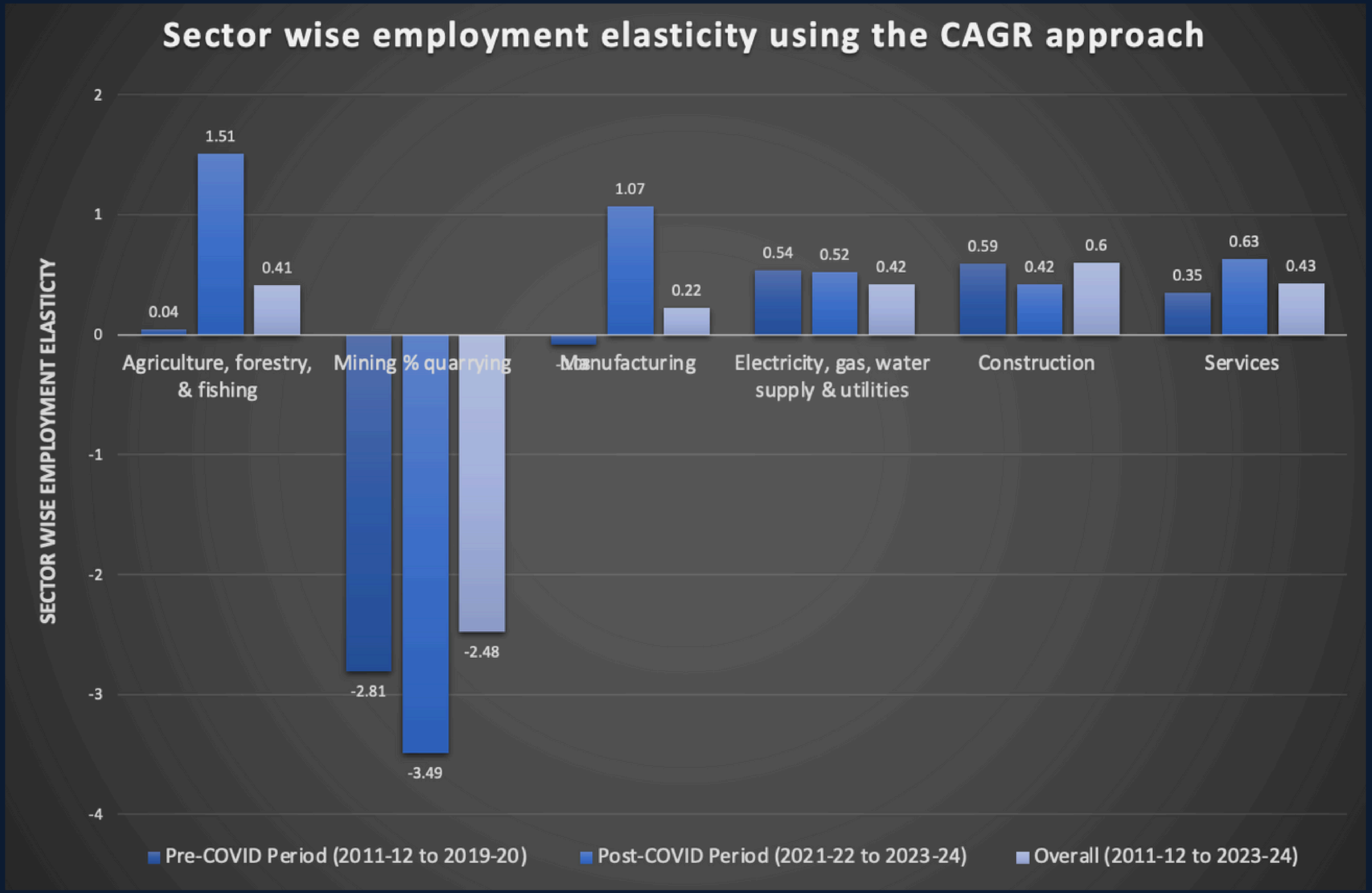


Source: NITI Aayog's India's Service Sector Report (2025) (Self-made)

- The spatial distribution of services employment further reinforces this imbalance. As shown in the figure, services accounted for 60.8% of total urban employment in 2023–24, but only 18.9% of rural employment, highlighting the strong urban concentration of services-led job creation. In contrast, agriculture continued to dominate rural employment, while industry occupied an intermediate position across both locations. This pattern confirms that the expansion of services has been spatially uneven, limiting the sector's capacity to absorb surplus rural labour and deepening rural–urban employment asymmetries.

- Employment quality within the services sector remains constrained by persistently high informality. In 2023–24, 71.3% of services-sector employment was informal, exceeding 80% in labor-absorbing sub-sectors such as trade, transport, etc, indicating that the majority of jobs generated within the sector lack employment security and social protection. By contrast, formal employment is concentrated in a narrow set of high-productivity sub-sectors — IT–BPM, financial services, and professional services — which contribute a disproportionately large share of services Gross Value Added while employing only a small fraction of the services workforce.

- Employment elasticity estimates quantify these structural constraints. As reported in the figure, services employment elasticity was 0.35 during 2011–12 to 2019–20, rose to 0.63 during the post-COVID recovery period (2021–22 to 2023–24), and stood at 0.43 over the full period 2011–12 to 2023–24. Manufacturing exhibited even lower long-term responsiveness, with an employment elasticity of 0.22, while construction recorded a higher elasticity of 0.60, reflecting its role as a labour-absorbing sector rather than productivity-led expansion.



Source: NITI Aayog's India's Service Sector Report (2025) (Self-made)

2. Informal and Gig Economy Workers

- India's integration into the global digital labour market coexists with the rapid expansion of platform-based work domestically. The International Labour Organization (2024) documents that India accounts for over 50% of global online freelancing in software and technology services, the highest share globally, reflecting strong comparative advantage in high-skill digital labour and deep integration into global value chains.

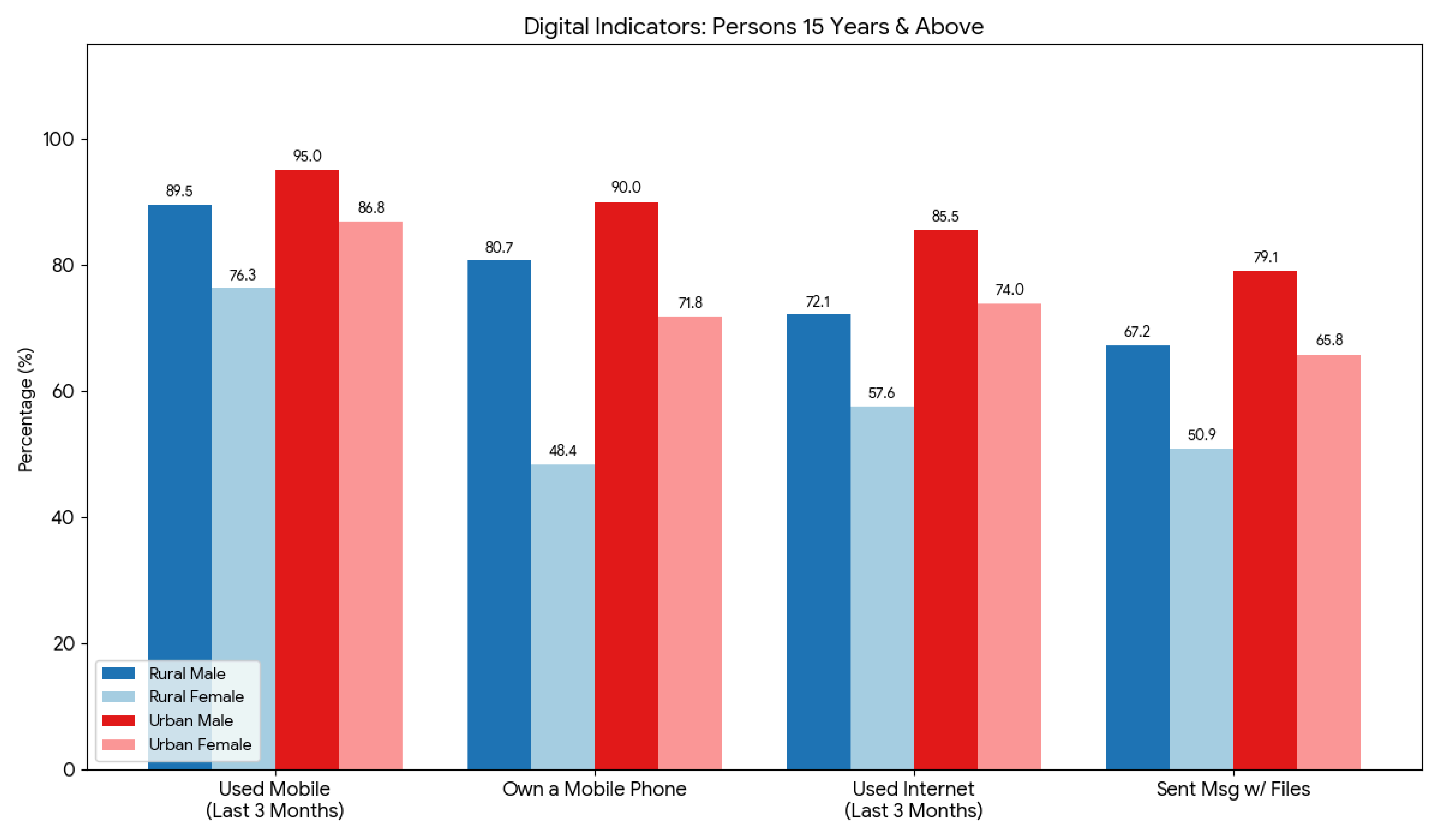
- At the same time, the National Labour Institute (2025) estimates India's gig and platform workforce at 17–20 million workers, with the majority engaged in ride-hailing, food delivery, logistics, and personal services. These segments are characterised by piece-rated earnings, algorithmic task allocation, and limited access to employment benefits or collective bargaining mechanisms.

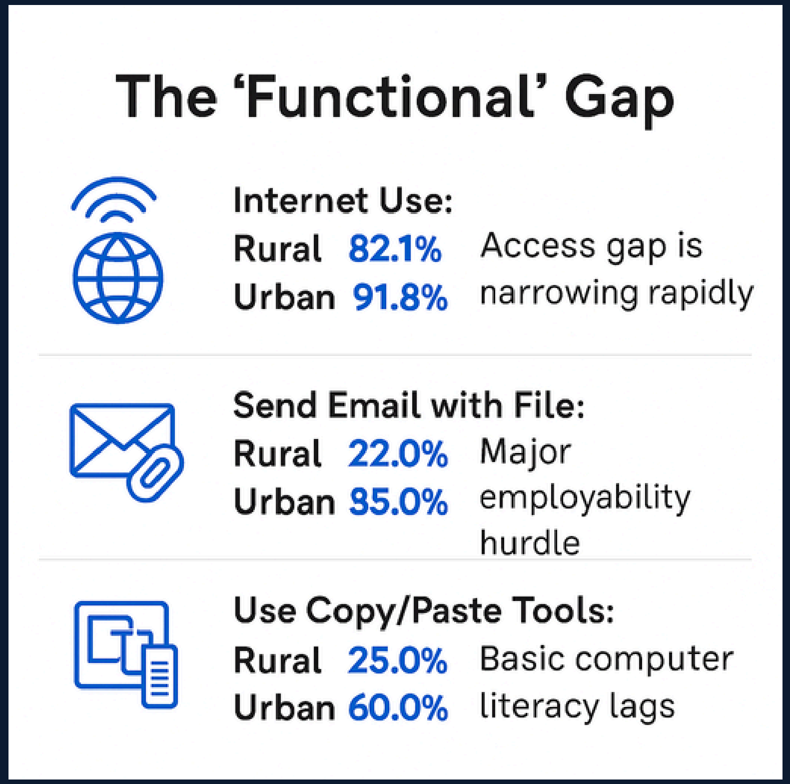
- Formalisation efforts have expanded primarily through worker identification. Furthermore, the e-Shram portal registered over 290 million informal workers by 2024, making it one of the largest labour registries globally. However, the same assessment notes that registration has not translated into uniform social security coverage. Access to schemes such as PM-JAY remains uneven, particularly for urban informal and platform workers, and does not adequately address income volatility or occupational risks.

- The Code on Social Security provides legal recognition to gig and platform workers and envisages aggregator-based contributions. However, it is observed that implementation remains limited due to the absence of a uniform contribution rate, unclear fiscal commitments, and weak enforcement capacity, constraining the conversion of legal recognition into effective protection.

3. Skills, Education, and Employability

- The Functional Gap: While internet access is high, the ability to use it for productivity (workforce readiness) remains low, particularly in rural India.

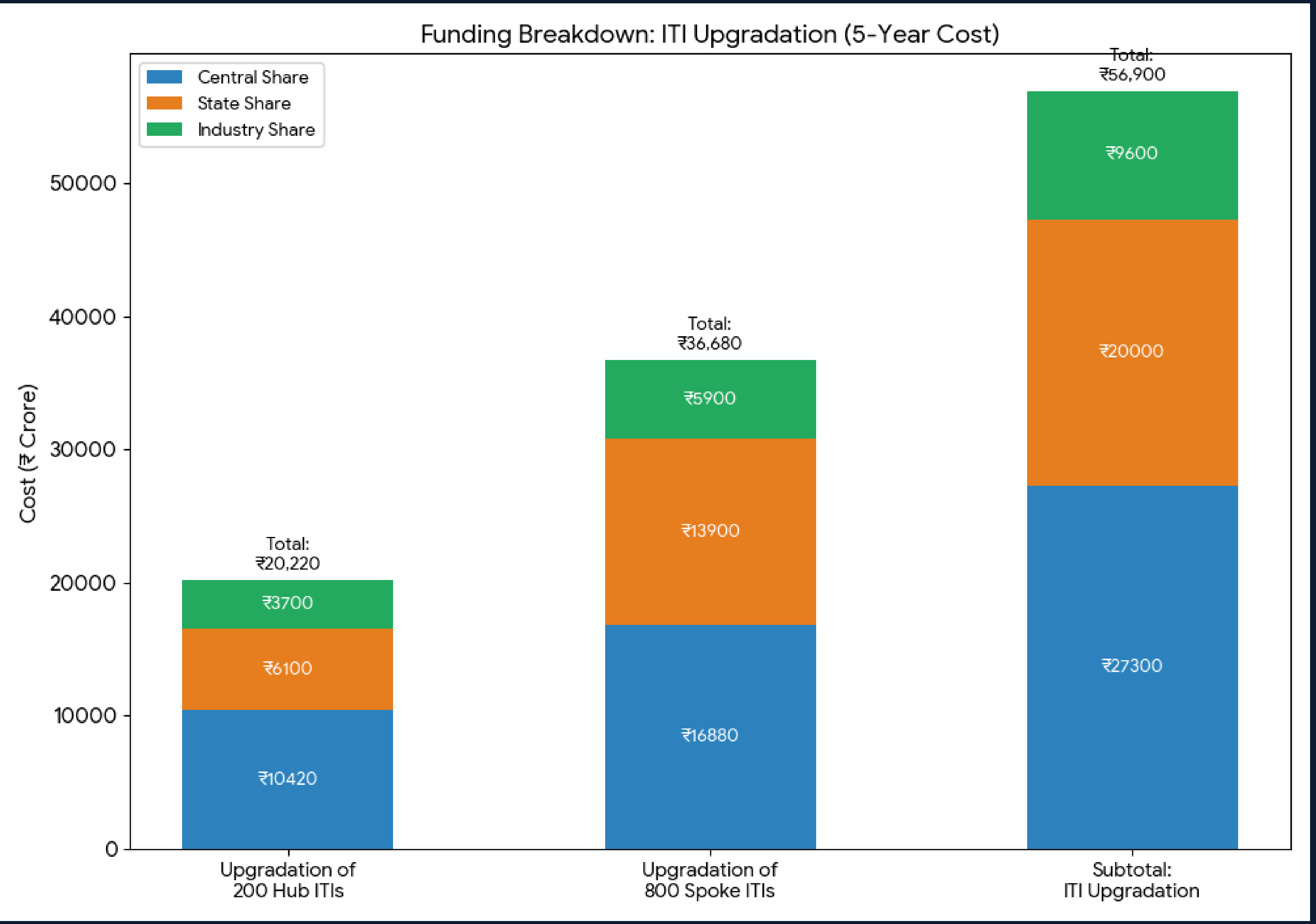




Source: NSS 78th Round (2020-21) / Projected 2025-26 Trends (self-made)

- When it comes to vocational training, India is moving away from a simple numbers game to a focus on genuine quality and relevance. The plan to upgrade Industrial Training Institutes (ITIs) isn't just superficial; it is a structural overhaul using the Hub-and-Spoke model. By positioning advanced Hub institutes to mentor smaller Spoke centers and bringing industry partners directly into the driver's seat, the curriculum is finally catching up with the market. We are seeing a critical pivot from traditional, static trades, like basic mechanics or fitting, to dynamic, future-proof fields like drone technology, EV maintenance, and AI.

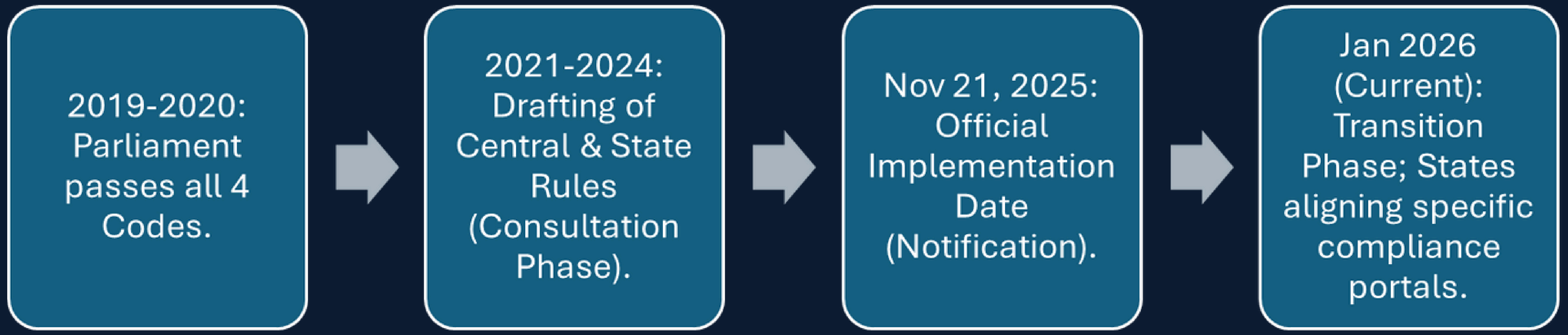
- This modernization is the key to fixing the long-standing disconnect between training and actual jobs. For years, a degree-skill mismatch meant that students held certificates but lacked the practical capabilities employers were hiring for. The current strategy aims to repair this broken link by prioritizing work-readiness over rote learning. By embedding apprenticeships directly into the coursework and aligning syllabi with industry needs, the goal is to ensure that a vocational certificate is no longer just a piece of paper, but a reliable passport to a paycheck.



Source: PM SETU (self-made)

4.Labour Codes and Implementation Capacity

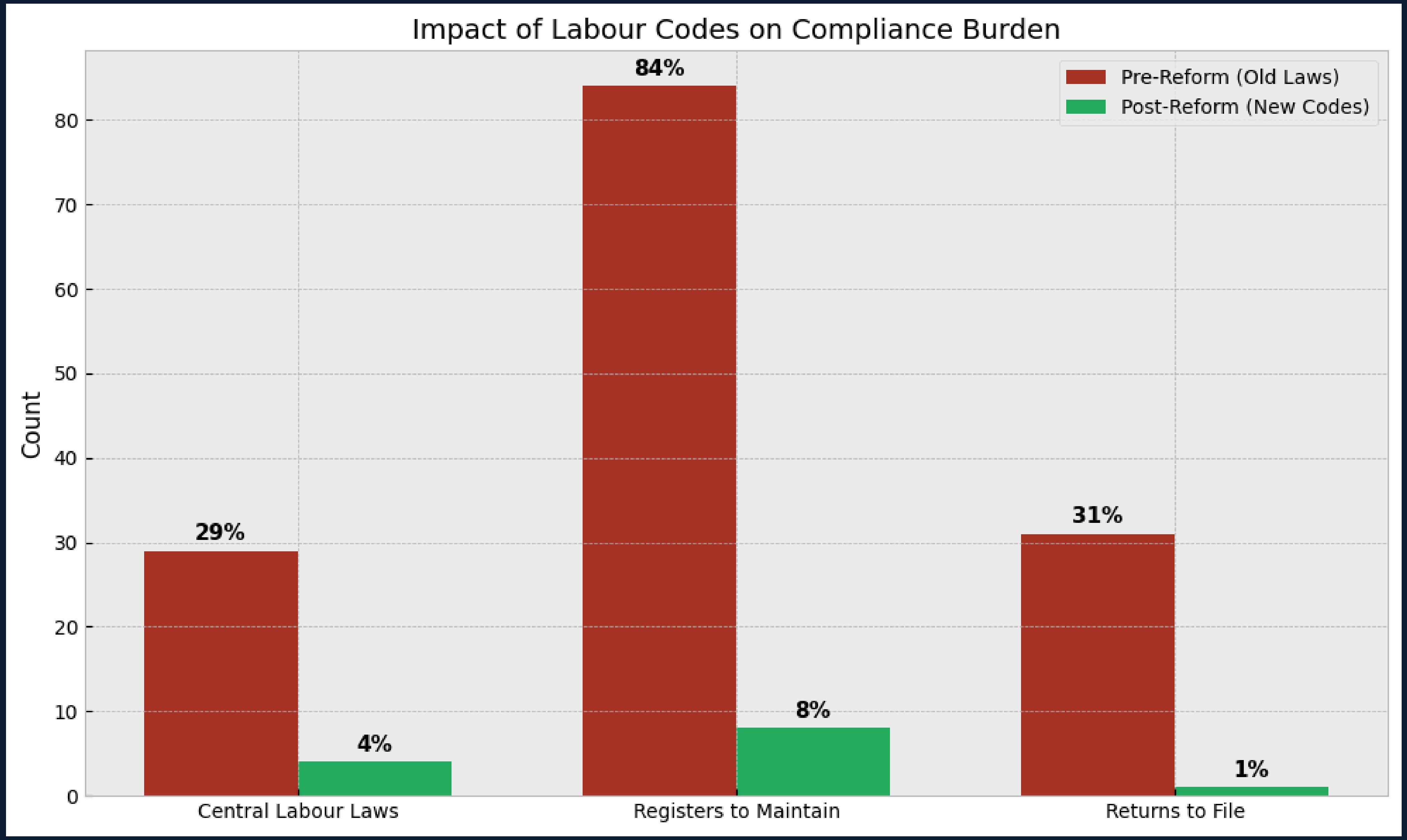
- Code on Wages: Universal floor wage; definition of wages standardized (50% of CTC must be basic pay).
- Industrial Relations (IR) Code: Fixed-Term Employment introduced; threshold for standing orders/retrenchment permission raised to 300 workers (flexibility for employers).
- Social Security Code: Extended to Gig & Platform workers; creation of a Social Security Fund.
- OSH Code: Single license regime; mandatory annual health check-ups for employees aged 45+.



- On the regulatory side, the government is trying to change its relationship with businesses, moving away from the feared Inspector model to a more supportive Inspector-cum-Facilitator model that prioritizes fixing mistakes over handing out penalties. While the introduction of randomized, web-based inspections aims to make enforcement fairer, there is a significant elephant in the room, that is, capacity. With the codes now covering the vast unorganized sector and the gig economy, there is a genuine concern that the current shortage of Labour Inspectors will make effective monitoring difficult, no matter how well-intentioned the new system is.

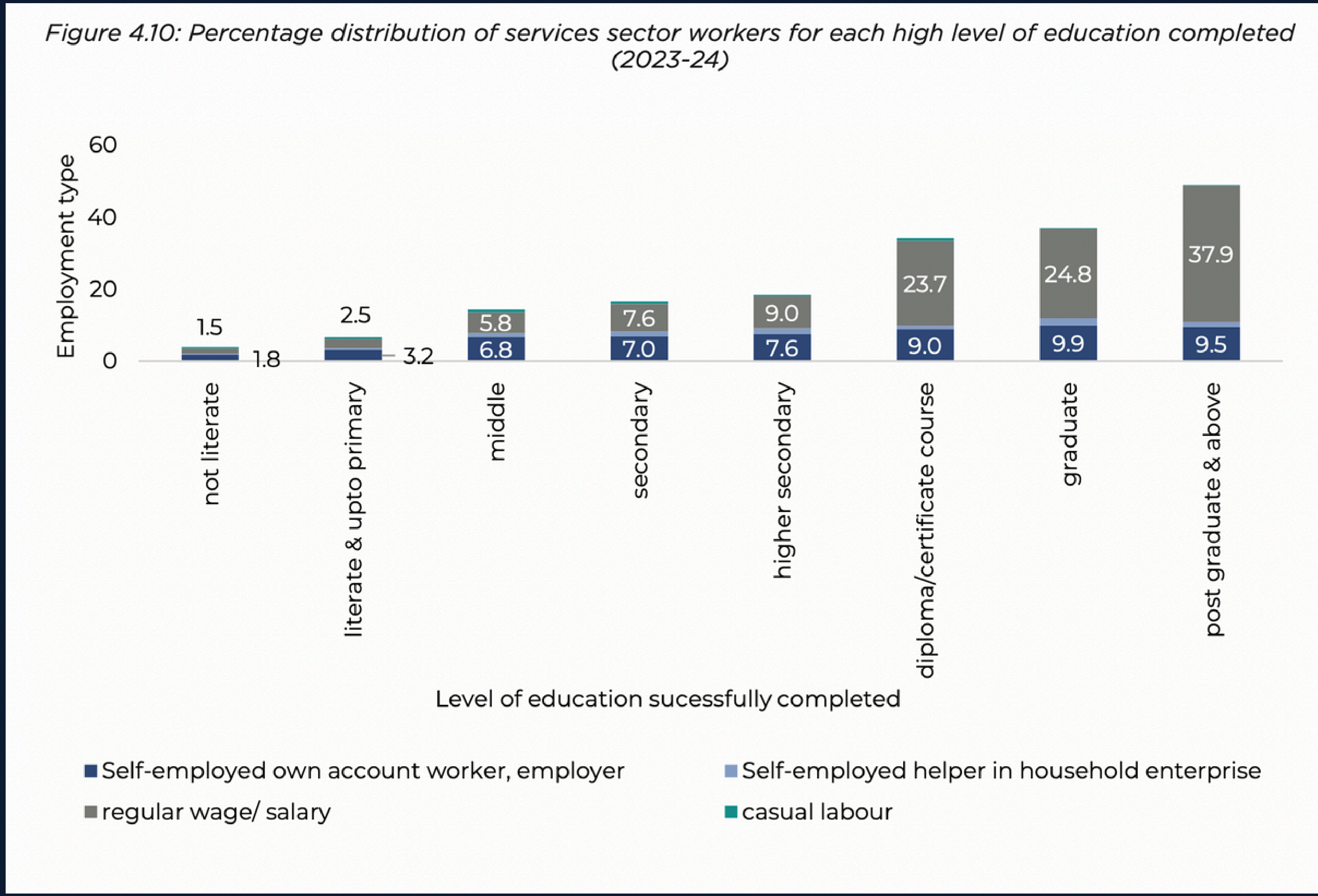
Challenges for compliance among small and informal firms:

- The shift to the new Labour Codes brings a mix of modernization and growing pains, particularly for smaller businesses. On one hand, the move toward mandatory digital filings and single-window returns promises efficiency, but it also assumes a level of digital infrastructure that many MSMEs simply don't have yet. This administrative hurdle is compounded by real financial concerns; small firms are bracing for higher costs due to increased gratuity liabilities for fixed-term workers and potentially larger PF contributions, as the new definition of wages caps allowances at 50%. Even hiring practices are being challenged, with the strict requirement for formal appointment letters clashing with the informal ways many small enterprises have traditionally operated.



Source:India's Labour Reforms: Simplification, Security, and Sustainable Growth(self-made)

5. Educated Unemployment and Incentive Schemes



Source: NITI Aayog's India's Service Sector Report (2025)

- Recent labour market indicators point to improved participation alongside persistent job-quality concerns. According to the National Statistical Office, *Periodic Labour Force Survey 2025*, the all-India unemployment rate declined to 4.7%, while the labour force participation rate rose to 55.8% and the worker population ratio to 53.2%. These gains were driven largely by rural employment recovery and increased female participation. However, urban unemployment remained elevated at 6.5%, signalling continued stress in job quality and income stability in urban labour markets.

- Employment-type data reinforces these concerns. As shown in Figure 4.10 (NITI Aayog, 2025), in 2023–24, only 24.8% of graduates and 37.9% of postgraduates and above in the services sector were engaged in regular wage or salaried employment, with the remainder either self-employed or in non-regular arrangements.

- Policy responses to educated unemployment have increasingly relied on Employment-Linked Incentive (ELI) schemes, which seek to lower the cost of formal hiring by linking incentives to EPFO-registered new employment, with a stated emphasis on manufacturing, MSMEs, and first-time job seekers. However, the scope for such incentives to deliver large-scale employment remains structurally constrained. Manufacturing's long-term employment elasticity of 0.22 over 2011–12 to 2023–24 indicates that output expansion in the sector has translated into only limited job creation, reflecting capital intensity, automation, and weak labour absorption. In this context, ELI schemes can at best encourage marginal payroll expansion or the formalisation of existing jobs, rather than generate the volume of new, stable employment required to absorb the growing pool of educated labour.

- Forward-looking evidence reinforces these limits. Projections based on NITI Aayog's gig and platform economy estimates up to 2030, extended using Exponential Smoothing (ETS) methods in the VVGNLI study, point to a continued expansion of gig and platform-based employment through 2047. This trajectory suggests that a rising share of employment generation is likely to occur in non-standard, flexible, and task-based work arrangements, rather than in regular, long-term salaried jobs. As a result, even as headline employment indicators improve, job creation is increasingly decoupled from employment security, income stability, and career progression—particularly for educated workers entering the labour market.

- Taken together, the evidence indicates that incentive-based hiring policies operate within a labour market structure that is fundamentally biased toward informal services, construction, and gig work. While such schemes may yield incremental gains in formal registration and reduce hiring frictions at the margin, they cannot, in isolation, resolve the challenge of educated unemployment or deliver sustained improvements in job quality. Addressing these outcomes requires a broader reorientation of employment strategy—one that goes beyond cost-side incentives to confront the underlying constraints of low employment elasticity, sectoral composition, and the growing dominance of non-standard forms of work.

Conclusion: Assessing the Budgetary Path

The Union Budget 2025–26 represents a strategic attempt to balance fiscal discipline with the urgent need for inclusive growth. By maintaining a strict fiscal consolidation path, the government prioritizes macroeconomic stability, yet this choice creates a visible tension between capital accumulation and the immediate demands for social protection. Fiscal and Federal Balance: The Budget navigates a delicate path between centralized revenue control, through cesses and surcharges, and the necessity of cooperative federalism. Growth vs. Welfare: A clear emphasis is placed on long-term infrastructure through capital expenditure, while attempting to sustain rural incomes through core welfare schemes.

Employment and Informality: Despite new incentive schemes and social security for gig workers, a gap remains between formalization goals and the persistent reality of informal labor. Ultimately, the Budget signals a managed contradiction, attempting to drive modernization while postponing the resolution of deep-seated structural challenges in employment and state-level fiscal equity.

Thank you!

For inputs, comments or clarifications please contact The Centre for New Economics Studies at cnes@jgu.edu.in