Union Budget 2018-19

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FOREWORD

At the onset, let me congratulate the Hon'ble Finance Minister for presenting a Budget that has contours of both work in progress and a new vision for the future. This year's Budget has continued the theme of agriculture and rural development from the previous year. However, the ambit of Government focus has clearly widened. The focus on farmers and diversification of their income is discernable from the Budget Speech.

This year's Budget exercise appeared a tad difficult as RE of Expenditure for 2017-18 shows an increase of Rs 71,015 crore over the BE 2017-18. Payment of compensation to States for revenue losses, on account of roll out of GST was a major component of this deviation. To add to this, pension payouts also increased. Despite this, one has to admit that the Budget is still able to retain its momentum from the previous years and has done a well thought balancing act.

The fiscal deviation in this year's Budget was on expected lines and fiscal deficit is estimated to be 3.5% of GDP. The introduction of the new taxation regime did impact the revenue position of the Government. Under the new GST regime, the last date for filing of GST returns is 20th of the succeeding month, even on the last day of the financial year. This means that the tax receipts during the current year was only for 11 months. The Government will target fiscal deficit as an operational target and will ensure that the fiscal deficit is 3.0% of GDP by 2020-21, clearly a more realistic glide path.

The Banking sector had already received its attention just before the Budget. Nevertheless, there are two proposals on IBC namely – doing away with the restriction on shareholding for the purpose of carry forward of loss, if reason for change of shareholding is pursuant to an approved resolution plan under IBC and permitting reduction of unabsorbed depreciation and brought forward loss from the book profit for computation of MAT. Capital gains tax has been reintroduced and tax on distributed income for equity mutual funds has been introduced at a nominal rate of 10%. Recognizing gold as an asset class and formulating a comprehensive policy for gold is a significant announcement. The merger of three public sector general insurance companies is a farsighted measure and has many positive benefits.

The Budget has been generous in its recognition of senior citizens. The four fold jump in exempted income of interest on bank deposits will effectively ensure that senior citizens get a social security of approx. Rs 4000 per month. Senior citizens will also get higher tax rebates for health expenditure spend. These are all positive measures.

The Budget has announced its intention of launching a comprehensive Health Protection Scheme for 10 crore poor families, and also a scholarship scheme for meritorious students with a caveat that such students should spend some time teaching in educational institutions. Government has emphasized its focus on TReDS as a mechanism to facilitate MSME sector. To encourage that economy continues to formalize and creates adequate employment under the formal sector, women employees' contribution to EPF will be reduced to 8% for first three years of their employment against existing rate of 12% or 10% with no change in employers' contribution.

The Budget speech has also acknowledged that combining cyber and physical systems have great potential to transform economic future of the country. The bright digital future of India will require focus on research, training and skilling in robotics, artificial intelligence, digital manufacturing, big data analysis, quantum communication and internet of things. The Budget also indicates ambition to develop indigenous 5G technology and facilitating its adoption. The Government has made its concerns on crypto-currencies unambiguously clear.

In a nutshell, the Budget has not shifted the goal post it had set in the previous Budgets. Rural development and simultaneous thrust to MSME is the best option to revive and accelerate the growth process. The focus on agriculture for exports is a huge step and is in line with ongoing negotiations under various trade forums. Additionally, the idea of addressing the impoverishment of tenant farmers is a positive move and will address the woes of indebtedness of small farmers. The Budget appears accommodating for poor sections but definitely bolsters the future outlook of growth.

Rajnish Kumar

Section 1: The Big Picture

KEY HIGHLIGHTS OF THE UNION BUDGET 2018-19

- Deviating from fiscal consolidation path, fiscal deficit for FY18 slipped from 3.2% of GDP to 3.5% of GDP. For FY19, the Government has set the fiscal deficit target of 3.3% of GDP. In actual terms, fiscal deficit for FY19 is Rs 29,427 crore more than the FY18 revised number.

- The Union Budget estimates 11.5% nominal GDP growth rate. Assuming an extremely conservative 7% real GDP growth rate, this translates into an inflation of around 4.5%. We believe, if growth comes back, on the back of synchronized global growth and lower stress in farm sector, the nominal GDP projection may be an underestimate. This may thus provide some additional spending room for the Government.

- Thrust has been given to farmers, rural population, senior citizens and underprivileged through various schemes and increased allocation of money. Social infrastructure has also been prioritised.

- ''Operation Greens'' on the lines of ''Operation Flood'' will be launched to promote Farmer Producers Organizations (FPOs), agri-logistics, processing facilities and professional management. A sum of Rs 500 crore will be allocated for this purpose.

- Standard deduction of Rs 40,000 has been proposed in lieu of the present deduction in respect of transport allowance and reimbursement of miscellaneous medical expenses. The revenue foregone of this decision is approximately Rs 8,000 crore. However, the standard deduction will be adjusted against the prevailing transport and medical allowance.

- It has been also proposed to replace existing 3% education cess on personal income tax and corporation tax with a 4% 'Health and Education Cess' to take care of the education and health needs of poor and rural families. This will enable Government to collect an estimated additional amount of Rs 11,000 crore. Both these moves will keep tax liabilities for the salaried class at nearly the same level / increase depending upon the tax bucket.

- On the back of buoyancy in equity market, the Government has now imposed a long term capital gains tax on capital gains exceeding Rs 1 lakh at the rate of 10% without allowing the benefit of any indexation. It is expected that revenue mobilisation to the tune of Rs 20,000 crore will happen because of this measure. The dividend distribution tax on equity oriented mutual funds may net another Rs 7500 crores.

- To further incentivise the domestic value addition and Make in India in sectors like food processing, electronics, auto components, footwear and furniture, customs duty on certain items has been increased.

- For FY19, the Government Borrowing is budgeted at Rs 6.05 lakh crore and a net borrowing requirement is pegged at Rs 3.90 lakh crore taking into account buybacks, switches and repayments. This is lower than Rs 4.02 lakh crore in current fiscal.

- The total dividend from the Reserve Bank of India, nationalised banks and financial institutions is estimated around Rs 54,817 crore for FY19 slightly lower than the revised estimated of FY18 (Rs 51,623 crores). For FY18, Government revised down its estimated from Rs 74,900 crore to Rs 51,623 crores due to low dividend from RBI. This indicates that the Government is expecting that banks will not park too much additional money with RBI with credit demand picking up.

- Disinvestment target for FY19 is budgeted at Rs 80,000 crore while target for FY18 has been revised upwards to Rs 100,000 crore from the budget estimate of Rs 72,500 crore. We believe that Government will be able to achieve this target given that it has approvals for a list of companies for public offerings both through initial and follow on public offers.

- A reduced corporate tax rate of 25% for companies that have reported turnover up to Rs 250 crore in financial year 2016-17 has been proposed. This will benefit the entire class of Micro, Small and Medium Enterprises which accounts for almost 99% of companies filing their tax returns but have a revenue forgone of Rs 7,000 crore.

- Gross tax revenue is expected to grow by 16.7% in FY19 to Rs 19.1 lakh crore. This revenue target from taxation is supported by 10.2% growth in corporation tax and 20.4% rise in income tax from direct tax side. The estimated tax buoyancy at 1.4 (basis gross tax revenue) is slightly more than the 1.3 of FY18. We believe that FY19 GST numbers are overambitious or the Government is expecting more compliance and hence better collection in FY19. For example, target for the GST is pegged at Rs 7.4 lakh crore that is 25% higher than FY18 after adjusting for the late GST roll out.

- Government will establish a dedicated Affordable Housing Fund (AHF) in National Housing Bank, funded from priority sector lending shortfall and fully serviced bonds authorized by the Government of India.

- An Agri-Market Infrastructure Fund with a corpus of Rs 2,000 crore will be set up for developing and upgrading agricultural marketing infrastructure in the 22,000 Gramin Agricultural Markets (GrAMs) and 585 APMCs. Government also announced to expand the coverage of e-NAM to 585 APMCs by March 2018 from the present level of 470 APMCs. This will provide farmers facility to make direct sale to consumers and bulk purchasers.

- To achieve the target of doubling farmer income by 2022, this year budget has given more focus on providing better price support for all Crops (fixing MSP at 1.5 times of cost production both Rabi and Kharif). Government also announced that whenever the price in the agricultural produce market is less than the MSP, then in that case Government will purchase either at MSP or work in a manner to provide MSP for the farmers through some other mechanism. We believe that the Central Government should come out with a scheme, like 'Bhavantar Yojana' which has been already introduced in states like Madhya Pradesh and Haryana and that will cost much less to the Government exchequer.

- Government has announced to formulate a comprehensive Gold Policy to develop the precious metal as an asset class. Apart from this, Government also declared to establish a system of consumer friendly and trade efficient system of regulated gold exchanges in the country. Gold Monetisation Scheme will be revamped to enable people to open a hassle-free Gold Deposit Account.

- Government has also proposed to merge the three public sector general insurance companies, namely National Insurance Company Ltd, United India Assurance Company Ltd and Oriental India Insurance Company Ltd, to create a single insurance entity which will be subsequently listed at the stock exchanges.

- Proposal to launch a flagship National Health Protection Scheme to cover more than 10 crore poor and vulnerable families (50 crore individuals approx.), which aims to provide coverage upto Rs 5 lakh per family per year for secondary and tertiary care hospitalization. We believe, this will be a game changer, if the new flagship scheme implemented in a mission mode, like Jan Suraksha schemes, this will be the world's largest Government funded health care programme and will bring smiles in the faces of crores of people in the country.

- In India, most regulators permit bonds with the 'AA' rating only as eligible for investment. The Budget's suggestion to encourage investment in 'A' grade bonds is a laudable step and will increase the depth of the corporate bond market. Since the share of 'A' grade bonds is merely 3.7% in total long-term corporate debt securities issuance, this share will increase if the Regulators have their way.
- Major subsidies will be increased by whopping 15.1% to Rs 2.64 lakh crore.

MACRO VIEW

The Union Budget has strived to maintain the momentum and continuity from last year with a strong focus on Agriculture, Social Sectors and MSME. The reforms related to Agriculture in terms of bolstering farm income are praiseworthy and we believe a quick roll out of the scheme along the lines of what is prevalent in states like Madhya Pradesh which will save substantial cost. Additionally, around 70% of the farm land is being currently cultivated by tenant farmers who have no access to bank loans. Hence, the move to allow them to have access to bank credit will significantly reduce rural indebtedness. The idea to launch 'Operation Green' is also a welcome step.

Minimum Support Price (MSP) which provides price support to farmers to manage the risk of any sharp fall in farm prices and is only limited to few crops. Presently, there is MSP for 25 crops, but official procurement at the MSP is effectively limited to few crops, namely rice and wheat, and concentrated in a few States. To address this issue, the Government in budget FY 2018-19, has announced to fix MSP for all Rabi and Kharif Crops (both announced and unannounced) at least 1.5 times of the cost of production. Presently, Commission for Agricultural Costs and Prices (CACP) gives three definitions of production costs: A2, A2+FL and C2. C2 costs are more comprehensive, accounting for the rentals and interest forgone on owned land and fixed capital assets respectively, on top of A2+FL.

If the MSP will be fixed at 1.5 times over and above of C2 costs, it will be beneficial to farmer otherwise if it is on A2 or A2+FL, then the incremental price on MSP will be minimal.

Increase in MSP is not the only solution and Government has realised that it is more important that farmers should get full benefit of the announced MSP. In this Budget, it has also announced whenever the price in the agricultural produce market is less than the MSP, then in that case Government will purchase either at MSP or work in a manner to provide MSP for the farmers through some other mechanism may be like "Bhavantar scheme" which has been introduced in states like Madhya Pradesh and Haryana. The detailed guidelines will be put in place by Niti Aayog, in consultation with Central and State Governments.

The decision to involve meritorious students to teach in educational institutions is a welcome move and will have far reaching impact of quality of teaching. Additionally, to improve literacy rate and to provide the best quality education to the tribal children in their own environment, Government will start Ekalavya Model Residential School in every block which has more than 50% ST population and at least 20,000 tribal persons.

The idea of providing healthcare to poor people and concessions for senior citizens are praiseworthy. There have been several measures to facilitate the MSME sector apart from bolstering employment in the formal sector.

The Union Budget estimate 11.5% nominal GDP growth rate. Assuming an extremely conservative 7% real GDP growth rate, this translates into an inflation of around 4.5%. We believe, if growth comes back on the back of synchronized global growth and lower stress in farm sector, the nominal GDP projection may be an underestimate. Interestingly, the budgeted net market borrowings (net of buyback and switch) are lower at Rs 3.90 lakh crore (FY18: Rs 4.02 lakh crore) will clearly provide a suitable message to debt market. We thus believe the spike in yields in not in sync with market fundamentals.

Gross tax revenue is expected to grow by 16.7% in FY19 to Rs 19.1 lakh crore. This revenue target from taxation is supported by 10.2% growth in corporation tax and 20.4% rise in personal income tax from direct tax side. The estimated tax buoyancy at 1.4 (basis gross tax revenue) is slightly more than the 1.3 of FY18.

We believe that FY19 GST numbers may be overambitious or the Government is expecting more compliance and hence better collection in FY19. For example, target for the GST is pegged at Rs 7.4 lakh crore that is 25% higher than FY18 after adjusting for the late GST roll out.

The growth in total expenditure is budgeted at Rs 10.1 lakh crore in FY19, which is a major improvement over the decadal averages. The cutback in expenditure has been made possible by a slower capital expenditure as compared to decadal average.

Economy Survey 2017-18 estimates that the total formal payroll (EPFO and ESIC) in India is 6 crore under the firms which are either registered under GST or not. According to the Survey, Government non-farm payroll (centre and states), is roughly estimated at 1.5 crore (excluding defence personnel). Hence, the total formal non-farm payroll from a social security perspective is estimated at about 7.5 crores. Interestingly, this number is largely similar to the estimates given by Soumya Kanti Ghosh (SBI) & Pulak Ghosh (IIMB), in their recent payroll report titled, "Towards a Payroll Reporting in India".

In order to provide further push to the employment generation Government has taken various initiates in Budget 2018-19. This includes among others, incentivizing employment of more women in the formal sector and to enable them higher take-home wages.

The Banking sector had already received its attention just before the budget. Further, Government has now allowed strong Regional Rural Banks to raise capital from the market to enable them increase their credit to rural economy. This will help the banks to expand their presence and bring efficiency in their operations.

There is also good news for the affordable housing sector as the Finance Minister has announced a dedicated fund for the sector in the Union Budget. This move is likely to provide buoyancy to the sector.

Interestingly, in the expenditure outlay for various Ministries, the allocation for IT & Telecom has the maximum increase, while that of rural development has shown the least increase (barring those showing a decline).

Budget at a glance (Rs Crore and as a % of GDP)

	FY16	FY17	FY18 (RE)	FY19 (BE)	FY19/ FY18 (%Gr)	FY18/ FY17 (%Gr)	FY17 / FY16 (%Gr)	5 Yr CAGR (FY14-18 in %)	Decadal CAGR (FY09-18 in %)
1.1 Revenue Receipts	11,95,025	13,74,203	15,05,428	17,25,738	14.6	9.5	15.0	10.4	12.1
% of GDP	**8.7**	**9.0**	**9.0**	**9.2**					
1.1.1 Tax Revenue (Net to centre)	9,43,765	11,01,372	12,69,454	14,80,649	16.6	15.3	16.7	11.7	12.4
% of GDP	**6.9**	**7.2**	**7.6**	**7.9**					
1.1.2 Non-Tax Revenue	2,51,260	2,72,831	2,35,974	2,45,089	3.9	-13.5	8.6	4.4	10.4
% of GDP	**1.8**	**1.8**	**1.4**	**1.3**					
1.2 Capital Receipts	5,95,748	6,00,991	7,12,322	7,16,475	0.6	18.5	0.9	6.9	8.4
% of GDP	**4.3**	**3.9**	**4.2**	**3.8**					
1.2.1 Recoveries of Loans	20,835	17,630	17,473	12,199	-30.2	-0.9	-15.4	8.7	12.3
% of GDP	**0.2**	**0.1**	**0.1**	**0.1**					
1.2.2 Other Receipts	42,132	47,743	1,00,000	80,000	-20.0	109.5	13.3	35.8	77.7
% of GDP	**0.3**	**0.3**	**0.6**	**0.4**					
1.2.3 Borrowings and other liabilities*	5,32,791	5,35,618	5,94,849	6,24,276	4.9	11.1	0.5	4.3	6.5
% of GDP	**3.9**	**3.5**	**3.5**	**3.3**					
1. Total Receipts	17,90,783	19,75,194	22,17,750	24,42,213	10.1	12.3	10.3	9.2	11.4
% of GDP	**13.0**	**12.9**	**13.2**	**13.0**					
2. Total Expenditure	17,90,783	19,75,194	22,17,750	24,42,213	10.1	12.3	10.3	9.2	10.8
% of GDP	**13.0**	**12.9**	**13.2**	**13.0**					
2.a) Revenue Expenditure	15,37,761	16,90,584	19,44,305	21,41,772	10.2	15.0	9.9	9.1	10.5
% of GDP	**11.2**	**11.1**	**11.6**	**11.4**					
2.a).1 Grants for creation of Capital Assets	1,31,754	1,65,733	1,89,245	1,95,345	3.2	14.2	25.8	10.0	…
% of GDP	**1.0**	**1.1**	**1.1**	**1.0**					
2. a).2 Interest Payments	4,41,659	4,80,714	5,30,843	5,75,795	8.5	10.4	8.8	9.1	11.9
% of GDP	**3.2**	**3.2**	**3.2**	**3.1**					
2.b) Capital Expenditure	2,53,022	2,84,610	2,73,445	3,00,441	9.9	-3.9	12.5	9.9	13.1
% of GDP	**1.8**	**1.9**	**1.6**	**1.6**					
3. Revenue Deficit (2.a)-1.1)	3,42,736	3,16,381	4,38,877	4,16,034	-5.2	38.7	-7.7	5.3	6.3
% of GDP	**2.5**	**2.1**	**2.6**	**2.2**					
4. Effective Revenue Deficit (2.a)-2a).1)	2,10,982	1,50,648	2,49,632	2,20,689	-11.6	65.7	-28.6	2.3	…
% of GDP	**1.5**	**1.0**	**1.5**	**1.2**					
5. Fiscal Deficit {2-(1.1+1.2.1+1.2.2)}	5,32,791	5,35,618	5,94,849	6,24,276	4.9	11.1	0.5	4.3	6.5
% of GDP	**3.9**	**3.5**	**3.5**	**3.3**					
6. Primary Deficit	91,132	54,904	64,006	48,481	-24.3	16.6	-39.8	-16.0	-8.7
% of GDP	**0.7**	**0.4**	**0.4**	**0.3**					
Revenue Deficit / Fiscal Deficit (%)	**64.3**	**59.1**	**73.8**	**66.6**					
Memoranda									
Nominal GDP	**1,37,64,037**	**1,52,53,714**	**1,67,84,679**	1,87,22,302					
Growth rate	**10.4**	**10.8**	**10.0**	11.5					

Source: Union Budget documents & SBI Research

Expenditure of Major Items (Rs crore and as a % of GDP)							
	FY16	FY17	FY18 (RE)	FY19 (BE)	FY19/ FY18 (% Gr)	FY18/ FY17 (% Gr)	FY17/ FY16 (% Gr)
Pension	96,771	1,31,401	1,47,387	1,68,466	14.3	12.2	35.8
% of GDP	**0.7**	**0.9**	**0.9**	**0.9**			
Defence	2,25,895	2,51,781	2,67,108	2,82,733	5.8	6.1	11.5
% of GDP	**1.7**	**1.7**	**1.6**	**1.5**			
Subsidy	2,41,833	2,04,025	2,29,716	2,64,336	15.1	12.6	-15.6
% of GDP	**1.8**	**1.3**	**1.4**	**1.4**			
Agriculture & allied Activities	23,694	50,184	56,589	63,836	12.8	12.8	111.8
% of GDP	**0.2**	**0.3**	**0.3**	**0.3**			
Commerce and Industry	16,247	21,364	26,310	27,956	6.3	23.2	31.5
% of GDP	**0.1**	**0.1**	**0.2**	**0.1**			
Development of North East	1,987	2,496	2,682	3,000	11.9	7.5	25.6
% of GDP	**0.0**	**0.0**	**0.0**	**0.0**			
Education	67,239	72,016	81,869	85,010	3.8	13.7	7.1
% of GDP	**0.5**	**0.5**	**0.5**	**0.5**			
Energy	21,123	30,964	41,682	41,104	-1.4	34.6	46.6
% of GDP	**0.2**	**0.2**	**0.2**	**0.2**			
External Affairs	14,518	12,753	13,690	15,012	9.7	7.3	-12.2
% of GDP	**0.1**	**0.1**	**0.1**	**0.1**			
Finance	71,213	41,549	29,449	20,342	-30.9	-29.1	-41.7
% of GDP	**0.5**	**0.3**	**0.2**	**0.1**			
Health	34,131	39,005	53,198	54,667	2.8	36.4	14.3
% of GDP	**0.2**	**0.3**	**0.3**	**0.3**			
Home Affairs	67,821	78,360	88,143	93,450	6.0	12.5	15.5
% of GDP	**0.5**	**0.5**	**0.5**	**0.5**			
Interest	4,41,659	4,80,714	5,30,843	5,75,795	8.5	10.4	8.8
% of GDP	**3.2**	**3.2**	**3.2**	**3.1**			
IT & Telecom	15,079	17,985	17,802	22,380	25.7	-1.0	19.3
% of GDP	**0.1**	**0.1**	**0.1**	**0.1**			
Others	46,008	63,667	69,515	72,845	4.8	9.2	38.4
% of GDP	**0.3**	**0.4**	**0.4**	**0.4**			
Planning & Statistics	5,959	4,494	5,063	5,199	2.7	12.7	-24.6
% of GDP	**0.0**	**0.0**	**0.0**	**0.0**			
Rural Development	90,235	1,13,877	1,35,604	1,38,097	1.8	19.1	26.2
% of GDP	**0.7**	**0.7**	**0.8**	**0.7**			
Scientific Departments	17,432	19,493	22,370	24,906	11.3	14.8	11.8
% of GDP	**0.1**	**0.1**	**0.1**	**0.1**			

Expenditure of Major Items (Rs crore and as a % of GDP)							
	FY16	FY17	FY18 (RE)	FY19 (BE)	FY19/ FY18 (% Gr)	FY18/ FY17 (% Gr)	FY17/ FY16 (% Gr)
Social Welfare	31,691	31,812	38,624	44,220	14.5	21.4	0.4
% of GDP	**0.2**	**0.2**	**0.2**	**0.2**			
Tax Administration	26,011	22,146	77,747	1,05,541	35.7	251.1	-14.9
% of GDP	**0.2**	**0.1**	**0.5**	**0.6**			
Transfer to States	1,14,802	1,32,704	1,20,265	1,42,858	18.8	-9.4	15.6
% of GDP	**0.8**	**0.9**	**0.7**	**0.8**			
Transport	87,413	1,02,200	1,07,092	1,34,572	25.7	4.8	16.9
% of GDP	**0.6**	**0.7**	**0.6**	**0.7**			
Union Territories	11,843	13,258	14,248	14,123	-0.9	7.5	11.9
% of GDP	**0.1**	**0.1**	**0.1**	**0.1**			
Urban Development	20,180	36,946	40,754	41,765	2.5	10.3	83.1
% of GDP	**0.1**	**0.2**	**0.2**	**0.2**			
Grand Total	17,90,783	19,75,194	22,17,750	24,42,213	10.1	12.3	10.3
% of GDP	**13.1**	**12.9**	**13.2**	**13.0**			
Source:Union Budget Documents & SBI Research							

FISCAL MANAGEMENT

With the current global slowdown, most of the countries have been witnessing increase in fiscal deficit. There are some minor exceptions including India, France, Germany, etc. which are on the path of fiscal consolidation.

India's Gross fiscal deficit as % of GDP, started shooting up after the 2008 financial crisis. However, with economic recovery gaining pace, Government embarked on the path of fiscal consolidation and has brought down its fiscal deficit to 3.5% of GDP in FY17. Apart from fiscal consolidation, India has also ramped up its fiscal infrastructure in a big way. Tax payments and refunds are now mostly online.

According to the Union Budget FY19, the Revised fiscal deficit estimate for FY18 is 3.5% of GDP as against the BE of 3.2%. For FY19 fiscal deficit of 3.3% of GDP has been proposed. Fiscal discipline is important, but we should always distinguish between austerity and consolidation. For us, staying on the path of consolidation is a must, but not on the path of a strict fiscal austerity when growth is just recovering. As Joseph Stiglitz says, "with austerity, there cannot be any prosperity". By assuming nominal GDP grow of 11.5% in FY19, Government is targeting fiscal deficit of 3.3% and will thus stay on the path of fiscal consolidation and there will be more fiscal space for the Government to spend in the election year ahead if picks up materially. This is expected to augur well for the market.

Fiscal Deficit (as a % of GDP)							
Country	Direction	2011	2012	2013	2014	2015	2016
China	↑	-1.7	-1.5	-2.0	-2.1	-2.4	-2.9
Indonesia	↑	-1.1	-1.8	-2.2	-2.1	-2.6	-2.5
Korea	↑	1.4	1.3	1.0	0.6	0.0	1.0
Malaysia	↑	-3.3	-4.8	-4.6	-6.0	-7.8	-5.4

Fiscal Deficit (as a % of GDP)							
Country	**Direction**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**
Thailand	↑	-0.4	0.0	0.5	-1.1	1.5	-2.2
France	↓	-0.3	0.1	0.8	0.7	0.6	0.8
Germany	↓	-1.0	0.0	-0.1	0.3	0.6	0.8
Russian Federation	↑	1.4	0.4	-1.2	-1.1	-3.4	-3.7
United Kingdom	↓	-7.5	-8.2	-5.4	-5.5	-4.3	-2.9
Saudi Arabia	↑	11.6	13.6	6.4	-2.3	-15.0	-12.8
South Africa	↑	-4.0	-5.2	-4.8	-4.7	-4.2	-4.2
United Arab Emirates	↑	-5.6	-4.8	-5.0	-2.4	-6.4	-7.8
Brazil	↑	-2.4	-1.8	-2.6	-5.0	-9.1	-7.7
India	↓	-5.9	-4.9	-4.5	-4.1	-3.9	-3.5
Japan	↓	-8.7	-9.6	-9.5	-7.4	-6.9	-7.3
Singapore	↑	7.8	6.9	6.6	5.7	2.7	3.3
Canada	↓	-1.5	-1.0	-0.3	0.1	0.0	-0.9
Source: CEIC, SBI Research							

Subsidy Trends (Rs crore and as a % of GDP)									
	FY16	**FY17**	**FY18 (RE)**	**FY19 (BE)**	**FY19/ FY18 (%Gr)**	**FY18/ FY17 (%Gr)**	**FY17 / FY16 (%Gr)**	**5 Yr CAGR (FY14-18 in %)**	**Decadal CAGR (FY09-18 in %)**
Total 3 Major Subsidies	241833	204025	229716	264336	15.1	12.6	-15.6	-1.6	7.2
% of GDP	**1.8**	**1.3**	**1.4**	**1.4**					
Fertiliser Subsidy	72415	66313	64974	70080	7.9	-2.0	-8.4	-0.9	-1.8
% of GDP	**0.5**	**0.4**	**0.4**	**0.4**					
Food Subsidy	139419	110173	140282	169323	20.7	27.3	-21.0	11.1	13.8
% of GDP	**1.0**	**0.7**	**0.8**	**0.9**					
Petroleum Subsidy	29999	27539	24460	24933	1.9	-11.2	-8.2	-26.8	27.0
% of GDP	**0.2**	**0.2**	**0.1**	**0.1**					
Source: Union Budget documents & SBI Research									

The direct tax revenue is budgeted at Rs 11.5 lakh crore, showing an increase of 14.7% from the revised estimates of FY18. The indirect tax revenue is budgeted at Rs 11.2 lakh crore, showing an increase of 19.2% from the revised estimates of FY18. The tax-GDP ratio is estimated at 12.1%, a significant improvement over FY18.

Direct and Indirect taxes (Rs crore and as a % of GDP)									
	FY16	**FY17**	**FY18 (RE)**	**FY19 (BE)**	**FY19/ FY18 (%Gr)**	**FY18/ FY17 (%Gr)**	**FY17 / FY16 (%Gr)**	**5 Yr CAGR (FY14-18 in %)**	**Decadal CAGR (FY09-18 in %)**
Gross Tax Revenue	14,55,648	17,15,822	19,46,119	22,71,242	16.7	13.4	17.9	14.3	13.9
% of GDP	**10.6**	**11.2**	**11.6**	**12.1**					
Direct Tax									
Corporation Tax	4,53,228	4,84,924	5,63,745	6,21,000	10.2	16.3	7.0	9.3	11.4
% of GDP	**3.3**	**3.2**	**3.4**	**3.3**					

	FY16	FY17	FY18 (RE)	FY19 (BE)	FY19/ FY18 (%Gr)	FY18/ FY17 (%Gr)	FY17 / FY16 (%Gr)	5 Yr CAGR (FY14-18 in %)	Decadal CAGR (FY09-18 in %)
Taxes on Income Other than Corporation Tax	2,87,628	3,49,436	4,39,255	5,29,000	20.4	25.7	21.5	16.6	17.1
% of GDP	**2.1**	**2.3**	**2.6**	**2.8**					
Indiect Taxes									
Customs	2,10,338	2,25,370	1,35,242	1,12,500	-16.8	-40.0	7.1	-5.8	3.4
% of GDP	**1.5**	**1.5**	**0.8**	**0.6**					
Union Excise Duty	2,88,073	3,81,756	2,76,995	2,59,600	-6.3	-27.4	32.5	13.1	11.0
% of GDP	**2.1**	**2.5**	**1.7**	**1.4**					
Service Tax	2,11,414	2,54,499	79,507	…	…	-68.8	20.4	-15.3	3.0
% of GDP	**1.5**	**1.7**	**0.5**						
Goods and Services Tax	…		4,44,631	7,43,900	67.3	…			
% of GDP			**2.6**	**4.0**					
Source: Union Budget documents & SBI Research									

Sources of Financing Fiscal Deficit (Rs Crore)							
	FY16	**FY17**	**FY18 (RE)**	**FY19 (BE)**	**FY19/ FY18 (%Gr)**	**FY18/ FY17 (%Gr)**	**FY17 / FY16 (%Gr)**
Fiscal Deficit	5,32,791	5,35,618	5,94,849	6,24,276	4.9	11.1	0.5
% of GDP	**3.9**	**3.5**	**3.5**	**3.3**			
Borrowings	4,54,743	3,55,206	4,79,864	4,07,120	-15.2	35.1	-21.9
% of GDP	**3.3**	**2.3**	**2.9**	**2.2**			
Securities against Small Savings	52,465	67,435	1,02,628	75,000	-26.9	52.2	28.5
% of GDP	**0.4**	**0.4**	**0.6**	**0.4**			
State Provident Funds	11,858	17,745	15,000	17,000	13.3	-15.5	49.6
% of GDP	**0.1**	**0.1**	**0.1**	**0.1**			
Other Receipts (Internal Debts and Public Account)	-12,202	86,130	34,318	84,679	146.7	-60.2	-805.9
% of GDP	**-0.1**	**0.6**	**0.2**	**0.5**			
External Debt	12,748	17,997	2,418	-2,589	-207.1	-86.6	41.2
% of GDP	**0.1**	**0.1**	**0.0**	**0.0**			
Draw-Down of Cash Balance	13,170	-8,895	-39,379	43,066	-209.4	342.7	-167.5
% of GDP	**0.1**	**-0.1**	**-0.2**	**0.2**			
Source:Union Budget Documents & SBI Research							

GOVERNMENT BORROWINGS

As against the budgeted estimate of Rs 5.80 lakh crore, total Gross Market Borrowings of the Government came in at Rs 5.99 lakh crore in FY18. In nominal terms, net borrowing is Rs 3.90 lakh crore in FY19 as against Rs 4.02 lakh crore in FY18. The bond market must take this message positively. Meanwhile, the short-term borrowing came in at Rs 77,470 crore as against the budgeted Rs 2002 crore.

For FY19, the Government Borrowing is budgeted at Rs 6.05 lakh crore and the net borrowing requirement is pegged at Rs 3.90 lakh crore taking into account repayments (adjusting for net switch of Rs zero and buyback of Rs 57016 crore) of Rs 2.00 lakh crore. Notably, the Government stocks repurchased by means of switch/ buyback will not have any impact on the fiscal situation as they will get prematurely redeemed and interest will cease to accrue on such redeemed Government stocks. Furthermore, the Government has budgeted Rs 17000 crore short-term borrowings through 91-day treasury bills. Thus the total net borrowing of the Center (taking into account the short-term borrowing as well) comes to Rs 4.07 lakh crore in FY19 compared to Rs 4.80 lakh crore in FY18.

Government Borrowings (Rs crore and as a % of GDP)							
	FY16	FY17	FY18 (RE)	FY19 (BE)	FY19/ FY18 (%Gr)	FY18/ FY17 (%Gr)	FY17 / FY16 (%Gr)
Gross Market Borrowings	585000	583045	599000	605539	1.1	2.7	-0.3
% GDP	**4.3**	**3.8**	**3.6**	**3.2**			
Less repayments	144375	174846	139590	143478	2.8	-20.2	21.1
% GDP	**1.0**	**1.1**	**0.8**	**0.8**			
Net Market Borrowings #	404050	349657	402394	390120	-3.1	15.1	-13.5
% GDP	**2.9**	**2.3**	**2.4**	**2.1**			
Source: Union Budget documents & SBI Research, # adjusted for net switch and buyback							

STATE BORROWINGS – ON THE EDGE?

In the post-global crisis period, all states have amended their fiscal responsibility legislations in FY11 in order to recommit to rule-based fiscal consolidation. Although the progress in this direction has continued up to FY12, some deterioration has been observed during 2012-15. In the last few years both among media and analysts, there is a huge debate regarding fiscal situation of Central Government. However, in our view there is a need to start a fresh debate on state fiscal position as this is the real matter of worry. The average fiscal deficit of 16 major states stood at 3.1% of GSDP (FY18 BE) with some of the states having fiscal deficit of more than 3.0% of GSDP (Kerala: 3.4%, Punjab: 4.9%).

In fact, most of the states by keeping coming elections in mind which will be held in next year, refrain of widening the tax base and imposing of new taxes. Further, there is no such control over freebies and subsidies. These two issues along with asymmetric distribution of expenditure between developmental vs. non-developmental, urban vs. rural, revenue vs. capital, etc. also make the fiscal situation of states worse.

Financing of states' fiscal deficit is to be primarily through market borrowings (more than 80%), the share of which was budgeted to increase due to net outgoes from certain public account items such as remittances and suspense and miscellaneous.

In the 16 major states, the actual market borrowing of FY18 (till Jan'18) has reached around 85% of the borrowings of FY17 to Rs 2.8 lakh crore from Rs 3.3 lakh crore in FY17. The last few financial years from FY14 to FY17 show market borrowing increasing by more than Rs 2,000 billion.

Financial Profile of States										
State	FY14		FY15		FY16		FY17		FY18	
	FD (% of GSDP)	Market Borrowing (Rs Bn)	FD (% of GSDP)	Market Borrowing (Rs Bn)	FD (% of GSDP)	Market Borrowing (Rs Bn)	FD (% of GSDP)	Market Borrowing (Rs Bn)	FD (% of GSDP)**	Market Borrowing (Rs Bn)-Actual*
Andhra Pradesh	2.1	144	3.9	180	2.8	181	2.8	195	3.0	199
Bihar	2.4	35	8.2	81	5.9	115	4.2	177	2.9	45
Chhattisgarh	2.7	23	2.7	42	2.8	49	2.9	42	3.5	51
Gujarat	2.4	91	2.1	149	2.3	163	1.8	247	1.8	180
Haryana	2.1	67	3.6	132	2.6	141	4.3	158	2.8	117
Jharkhand	1.3	13	2.5	50	2.3	54	2.5	52	2.3	55
Karnataka	2.8	98	2.7	185	2.8	162	2.2	280	2.6	221
Kerala	4.3	97	3.2	132	3.0	150	3.5	173	3.4	160
Madhya Pradesh	2.3	30	2.7	103	3.5	147	4.6	161	3.5	130
Maharashtra	1.7	187	2.2	251	1.9	325	2.2	400	4.9	374
Odisha	1.7	–	2.9	30	3.0	45	3.2	76	3.0	69
Punjab	2.8	73	3.0	90	3.0	108	13.9	136	4.9	134
Rajasthan	2.9	80	4.0	123	3.6	158	6.4	161	3.0	175
Tamil Nadu	2.4	180	2.8	256	2.7	298	4.6	373	2.8	322
Uttar Pradesh	2.7	70	2.9	175	2.9	300	4.4	411	3.0	338
West Bengal	3.6	158	3.0	219	2.7	240	2.6	344	2.6	300
Total/Average	2.5	1346	3.3	2198	3.0	2636	4.1	3385	3.1	2870

Source: RBI; SBI Research, * upto Jan'18, ** BE

For FY19 States' gross market borrowings are expected to increase significantly to Rs 5.2 lakh crore. The net market borrowing is projected at Rs 3.98 lakh crore after adjusting for 1.22 lakh crore of redemptions for FY19. Thus the total gross market borrowings of the Centre and the States together for FY19 is pegged at Rs 10.03 lakh crore (Union Government: 6.05, State Governments: 3.98).

State Borrowings (Rs lakh crore)					
	FY15	FY16	FY17	FY18	FY19 (SBI)
Gross Borrowing	2.41	2.94	3.82	4.29	5.20
Repayments	0.33	0.33	0.39	0.74	1.22
Net Borrowing	2.08	2.61	3.43	3.55	3.98

Source: RBI & SBI Research

As can be seen from the table, outstanding market debt is concentrated in 5-20 years bucket, which at the end of Mar'17 stood at 62.6% of the total dated securities portfolio and 60.8% by Jun'17. The maturity profile has shifted marginally from 10-20 years bucket to 5-10 years bucket.

Maturity Profile of Outstanding Central Government Dated Securities (% of total)								
Maturity Bucket	**End March 2011**	**End March 2012**	**End March 2013**	**End March 2014**	**End March 2015**	**End March 2016**	**End March 2017**	**End June 2017**
Less than 1 year	3.41	3.50	3.10	3.95	3.65	4.00	3.30	5.30
1-5 years	25.54	26.70	27.90	25.99	24.59	22.90	21.70	21.30
5-10 years	34.09	34.70	35.00	31.52	30.35	29.60	33.30	30.70
10-20 years	21.42	22.00	22.90	25.20	28.32	30.30	29.30	30.10
20 years and above	15.53	13.10	11.20	13.34	13.09	13.30	12.40	12.60
Source: SBI Research, DEA								

Government may continue to rely on off balance sheet financing to boost capex

A sizeable chunk of the spending on public infrastructure takes place indirectly via Government owned companies (PSUs) rather than through Budget. These PSUs in turn utilize the internal accruals as well as borrowings or extra budgetary resources (EBR) to fund their spending. For FY19, extra budgetary resources for PSU's has been budgeted at Rs 3.12 lakh crore (1.7% yoy growth). EBR for Petroleum and Natural Gas and Railways have increased while that of Power and Steel have declined.

Extra Budgetary Resources for PSUs (Rs Crore)			
	FY18 (RE)	FY19 (BE)	Growth (%)
Coal	3346	4375	30.7
Ministry of Housing and Urban Affairs	14240	15147	6.4
Petroleum and Natural Gas	14261	20536	44.0
Power	41842	33710	-19.4
Road Transport and Highways	59279	62000	4.6
Steel	5750	5400	-6.1
Railways	45100	54940	21.8
Others	123584	116596	-5.7
Total	307402	312704	1.7
% of GDP	1.8	1.7	
GDP	16784679	18722302	
Source: Union Budget Documents & SBI Research			

The Government has budgeted 16.7% increase in gross tax revenue for FY19 of which 'Net other receipts (Public Account Other than State Provident Funds) for FY19 budgeted at Rs 61,008 crore compared to Rs 14,150 crore in FY18, an increase of Rs 46,858 crore. It is difficult to recognise from where this large receipt will come.

Arithmetic of Revenue Growth					
Item (in Rs Crore)		FY16	FY17	FY18 RE	FY19 BE
Net other receipts (Public Account Other than State Provident Funds)	Actual	-18824	73636	14150	61008
	Change	-	-	-59486	46858
Reserve Funds and Deposits (Not bearing interest)	Actual	74273	79118	89291	98286
	Change	-5817	29379	10173	8995
Source: Union Budget Documents; SBI Research					

EMPLOYMENT

Economy Survey 2017-18 estimates that the total formal payroll (EPFO and ESIC) in India is 6 crore under firms which are either registered under GST or not. According to Survey Government non-farm payroll (centre and states) is roughly estimated at 1.5 crore (excluding defence personnel). Hence the total formal non-farm payroll from a social security perspective is estimated at about 7.5 crores.

Interestingly, this number is largely similar to the estimates given by Soumya Kanti Ghosh (SBI) & Pulak Ghosh (IIMB) in their recent payroll report titled, "Towards a Payroll Reporting in India". In the report it is estimated (by using big data analytics) that there are around 5.5 crore non-zero regular contributors in EPFO and 1.2 crore ESIC members, and 2.0 crore Government employee (centre and states) hence the total is 8.7 crore. If we exclude 1 crore under Amnesty scheme then the formal payroll under EPFO/ESIC comes out to be 7.7 crore, which is quite near to the Survey Estimate.

It is a matter of extreme pleasure for us that Hon'ble Finance Minister quoted the above study in his Budget speech.

Formal Non-Farm Payroll in India		
in Crore	Economic Survey	SBI/IIMB Research
EPFO	6.0	5.5
ESIC		1.2
Amnesty Scheme	-	1.0
Government	1.5	2.0
Total	7.5	7.7
Note: SBI/IIMB Research exclude 1 crore employees of Amnesty Scheme		

In order to provide further push to employment generation, Government has taken various initiatives in Budget 2018-19.

Government will contribute 12% of the wages of the new employees in the EPF for all the sectors for next three years. Also, the facility of fixed term employment will be extended to all sectors.

Finance Minister has proposed to extend the benefits under Section 80-JJAA of the Income-tax Act to footwear and leather industry. Currently, a deduction of 30% is allowed in addition to normal deduction of 100% in respect of emoluments paid to eligible new employees who have been employed for a minimum period of 240 days during the year under section 80-JJAA of the Income-tax Act. This minimum period of employment is relaxed to 150 days in case of apparel industry. Extending this relaxation of minimum period of 150 days to footwear and leather industry also, we believe this would encourage creation of new employment in this sector.

It has been further proposed to rationalise deduction of 30% by allowing the benefit for a new employee who is employed for less than the minimum period during the first year but continues to remain employed for the minimum period in subsequent year.

To incentivize employment of more women in the formal sector and to enable higher take-home wages, Budget has proposed amendments in the Employees Provident Fund and Miscellaneous Provisions Act, 1952 to reduce women employees' contribution to 8% for first three years of their employment against the existing rate of 12% or 10% with no change in employers' contribution.

GDP GROWTH AND UNEMPLOYMENT RATE

In economic literature the relationship between GDP growth and unemployment is well stated. It states that if GDP grows rapidly the unemployment rate declines, if growth is very low or negative the unemployment rate rises. We have made an attempt to examine this relationship across developed countries post financial crisis (2012-2017). The result suggests that, in countries like Canada, Germany, Portugal, Spain, Hong Kong and US, the GDP growth has increased on an average of 2.9 % and the Unemployment rate has declined by an average of 2.5 % during 2012 to 2017. Similarly in countries like Australia, Brazil, Singapore and South Africa, where the GDP has declined by an average of 1.4%, the Unemployment rate has been impacted by an average of 2.2% .

GDP and Unemployment (%)			
S.L.No	**Country**	**Change in GDP (between 2017 to 2012)**	**Change in Unemployment rate (between 2012 to 2017)**
1	Australia	-1.4	-0.5
2	Brazil	-1.2	-5.3
7	Singapore	-1.3	-0.2
8	South Africa	-1.5	-2.8
3	Canada	1.3	1.0
4	Germany	1.4	2.1
5	Hong Kong SAR	1.8	0.8
6	Portugal	6.5	3.0
9	Spain	6.0	4.3
10	United Kingdom	0.3	3.7
Source: IMF & SBI Research			

DISINVESTMENT

Though Government had set an ambitious disinvestment target of Rs 72,500 crore for FY18, it has surpassed the target and garnered Rs 100,000 crore of receipts. For FY19, Government has set the disinvestment target of Rs 80,000 crore, which we believe is on the lower side given the fact that Government has approved listing of 14 CPSEs, including two insurance companies on the stock exchanges. The Government has also initiated the process of strategic disinvestment in 24 CPSEs. This includes strategic privatization of Air India.

Disinvestment – Target vs. Actual (in Rs crore)			
Year	Budget Estimate	Revised Estimate	Actual
FY15	63,425	31,350	37,737
FY16	69,500	25,312	42,132
FY17	56,500	45,500	34,939
FY18	72,500	1,00,000	-
FY19	80,000	-	-

Source: Union Budget Documents, SBI Research

EDUCATION

Government has announced the launch the ''Prime Minister's Research Fellows (PMRF)'' Scheme under which 1,000 best B.Tech students will be selected each year from premier institutions and provided facilities to do Ph.D in IITs and IISc with a handsome fellowship. These young fellows would voluntarily commit few hours every week for teaching in higher educational institutions which will have far-reaching impact on education quality.

The literacy rate of ST population is only 58.9% (Male: 68.5% and Female: 49.3%) is far lower than the national average of 74.0% (Male: 82.1% and Female: 65.5%). Hence in order to improve literacy penetration and to provide the best quality education to the tribal children in their own environment, Government will start Ekalavya Model Residential School in every block which has more than 50% ST population and at least 20,000 tribal persons. These Ekalavya schools will be on par with Navodaya Vidyalayas and will have special facilities for preserving local art and culture besides providing training in sports and skill development.

The gradual movement from ''black board'' to ''digital board'' will increase the digital intensity in education. The Finance Minister underlined that a district-wise strategy for improving the quality of education is also being prepared. Emphasising the need to step up investment in research and related infrastructure in leading educational institutions, the Finance Minister announced the proposal to launch a major initiative named "Revitalising Infrastructure and Systems in Education (RISE)" and a total of Rs 1,00, 000 crore will be invested in the initiative for the next four years.

BANKING SECTOR

The Banking sector had already received its attention just before the budget. Government has launched the Bank recapitalization program with bonds of Rs 80,000 crore being issued this year. The programme has been integrated with an ambitious reform agenda under the rubric of an Enhanced Access and Service Excellence (EASE) programme. Government has estimated that recapitalization will pave the way for the public sector banks to lend additional credit of Rs 5 lakh crore.

Nevertheless, there are two proposals on IBC namely – getting away the restriction on shareholding for the purpose of carry forward of loss, if reason for change of shareholding is pursuant to an approved resolution plan under IBC and permitting reduction of unabsorbed depreciation and brought forward loss from the book profit for computation of Minimum Alternative Tax.

Further, Government has allowed strong Regional Rural Banks to raise capital from the market to enable them increase their credit to rural economy. This will help the banks to expand their presence and bring efficiency in their operations.

It is good news for the affordable housing sector as the Finance Minister has announced a dedicated fund for the sector in the Union Budget. This move is likely to provide buoyancy to the sector. Last week, the GST

Council recommended rationalisation of GST rates on various goods and services. The list included affordable and low-cost housing. GST would be charged at 8% on the total value of under-construction properties, which would be 4 percentage points less than the earlier effective rate of 12%.

MSME

A provision of Rs 3794 crore has been provided in the Union Budget 2018-19 for the Medium, Small and Micro Enterprises (MSMEs) to provide credit support, capital and interest subsidy and innovations to this Sector. An outlay of Rs 7148 crore has been provided for the Textile Sector.

In an effort to reduce tax burden on MSMEs and to create large-scale employment, Finance Minister has also announced measures to extend the benefit of reduced rate of 25% to companies who have reported turnover up to Rs 250 crore in FY17.

FM has referred to the review of the refinancing policy and eligibility criteria set by MUDRA for better refinancing of Non-Banking Finance Companies NBFCs. In this regard, Budget has proposed a target of Rs 3 lakh crore for lending under MUDRA for 2018-19, as the targets had been exceeded in all previous years.

The Finance Minister also referred to a Group in the Finance Ministry that is examining the policy and institutional development measures needed for creating right environment for Fintech companies to grow. Additional measures will be taken to strengthen the environment for Venture Capital Funds and for their growth and successful operation of alternative investment funds in the country.

Trade Electronic Receivable Discounting System (TReDS) – Opportunity Unlimited

Government has given a big push to bill discounting by highlighting the need for and use of Trade Receivables Discounting System (TReDS) for improving flow of funds to MSME sector by reducing the receivables realisation cycles first in the Budget 2015-16. TReDS is an online electronic institutional mechanism for facilitating the financing of trade receivables of MSMEs through multiple financiers. The TReDS Platform enables discounting of invoices/bills of exchange of MSME Sellers against large Corporates including Government and PSUs, through an auction mechanism, to ensure prompt realisation of trade receivables at competitive market rates.

TReDS allows SMEs to post their receivables on the system and get them financed. This not only gives them greater access to finance but also puts greater discipline on corporates to pay their dues on time. The Public Procurement Policy states that 20% of all procurement by PSUs are to be made from MSEs.

Government has made it mandatory for all major public sector units to register on TReDS. This is expected to give a major boost to the MSME sector with transparent price discovery mechanism and an additional avenue for getting their receivables funded.

Presently three applicants are operating Trade Receivables Discounting System (TReDS) i.e. RXIL - NSE Strategic Investment Corporation Limited (NSICL) and Small Industries Development Bank of India (SIDBI), A.TREDS, JV of Axis Bank and B2B e-commerce company mjunction and Mynd Solutions Pvt. Ltd., Gurgaon, Haryana.

Massive formalization of the businesses of MSMEs is taking place in the country after demonetization and introduction of GST. This is generating enormous financial information database of MSMEs' businesses and finances. This big data base will be used for improving financing of MSMEs' capital requirement, including working capital.

This budget has further proposed to onboard public sector Banks and Corporates on Trade Electronic Receivable Discounting System (TReDS) platform and link this with GSTN.

Online loan sanctioning facility for MSMEs for prompt decision making by the banks will be a win-win situation for all.

REFORMS IN AGRICULTURE

The Budget Focus has remained on Agriculture and Farmers, just as it was in the past year. The Government has termed agriculture as an enterprise and has reiterated its commitment to double farmers' income by 2022. The focus of Government is on securing good remuneration for farmers and generating productive and gainful on-farm and non-farm employment for the farmers and landless families.

The following steps have been taken to achieve the objectives stated above:

- Government has decided to implement Minimum support price (MSP) of at least at one and a half times the cost for all the crops.
- "Operation Greens'' on the lines of ''Operation Flood'' will be launched. ''Operation Greens'' shall promote Farmer Producers Organizations (FPOs), agri-logistics, processing facilities and professional management. A sum of Rs 500 crore will be allocated for this purpose.
- Estimating India's agri-exports potential to be $100 billion, the Government will liberalize export of agri-commodities.
- Government will also work towards building cluster based model in a scientific manner for identified agriculture produces in districts, so that specialization is achieved just as it was in the case of industrial produce. Cluster based organic farming and farming of specialized medicinal and aromatic plants will be encouraged.
- As food processing industry provides better opportunities for farmers, it will be encouraged. Allocation of Ministry of Food Processing is being doubled from Rs 715 crore in RE FY18 to Rs 1400 crore in BE FY19. Government will promote establishment of specialized agro-processing financial institutions in this sector.
- To promote non-farm income, Fisheries and Aquaculture Infrastructure Development Fund (FAIDF) for fisheries sector and an Animal Husbandry Infrastructure Development Fund (AHIDF) for financing infrastructure requirement of animal husbandry sector have been established. Total Corpus of these two new Funds would be Rs 10,000 crore. Also, Kisan Credit Cards will be extended to fisheries and animal husbandry farmers.
- Around 70% of the farm land is being cultivated by tenant farmers. He is not getting any benefit, as he is not the owner of the land. NITI Aayog will evolve a suitable mechanism to enable access of lessee cultivators to credit without compromising the rights of the land owners. This will help the tenant farmer to get all the benefits available to the land owner.
- Upgradation of existing 22,000 rural haats into Gramin Agricultural Markets (GrAMs) will take place, the physical infrastructure of which will be strengthened. These GrAMs will provide farmers facility to make direct sale to consumers and bulk purchasers. An Agri-Market Infrastructure Fund with a corpus of Rs 2,000 crore will be set up for developing and upgrading agricultural marketing infrastructure in the 22,000 Grameen Agricultural Markets (GrAMs) and 585 APMCs.
- State Governments will put in place a mechanism so that surplus solar power produced by farmers is purchased by the distribution companies or licencees at reasonably remunerative rates.
- Institutional credit for agriculture sector has been raised to Rs 11 lakh crore for FY19.
- In order to encourage professionalism in post-harvest value addition in agriculture, 100% deduction to Farmer Producer Companies having annual turnover up to Rs 100 crores in respect of their profit derived from such activities for a period of five years from FY19.

MINIMUM SUPPORT PRICE

To achieve the target of doubling farmer income by 2022, this year budget has given more focus on providing better price support for all Crops (both Rabi and Kharif) and is planning to create an institutional mechanism, with participation of all concerned Ministries, to develop appropriate policies and practices for better price and demand forecast of agricultural crops.

It has been realised that improvement in agricultural production does not always lead to increase in farmer's welfare. Despite higher agricultural production in 2016-17, which touched up to 275 million, there was farmer distress in many parts of the country. The NSSO data on Consumer Expenditure Survey (2011-12) reveals that one fifth of rural household involved in agriculture as their principal occupation were having income less than the poverty line.

Farming will be sustainable in India, when cost of cultivation is reduced, yield per hector is increased and farmers get remunerative prices on their produce. Minimum Support Price (MSP) which provides price support to farmers to manage the risk of any sharp fall in farm prices is only limited to few crops. Presently, there is MSP for 25 crops, but official procurement at the MSP is effectively limited to few crops, namely rice and wheat, and concentrated in a few States. To address this issue, the Government in budget FY 2018-19, announced to fix MSP for all Rabi and Kharif Crops (both announced and unannounced) at least 1.5 times of the cost of production. Presently, Commission for Agricultural Costs and Prices (CACP) gives three definitions of production costs: A2, A2+FL and C2. A2 costs basically cover all paid-out expenses, both in cash and in kind, incurred by farmers on seeds, fertilisers, chemicals, hired labour, fuel, irrigation, etc. A2+FL cover actual paid-out costs plus an imputed value of unpaid family labour. C2 costs are more comprehensive, accounting for the rentals and interest forgone on owned land and fixed capital assets respectively, on top of A2+FL.

If the MSP will be fixed at 1.5 times over and above of C2 costs, then it will beneficial to farmer otherwise if it will be on A2 or A2+FL, then the incremental price on MSP will be minimal. Earlier also, M S Swaminathan committee recommended to fix minimum support prices (MSP) for crops at levels at least 50 per cent more than the weighted average cost of production.

Besides cost, factors such as demand and supply, price trend in the domestic and international markets, inter-crop price parity, terms of trade between agricultural and non-agricultural sectors played an important role in determining Price of Agricultural Produce in India. For better price realization Government is planning to create an institutional mechanism that will use futures and options market, forecast demand and supply and will take decisions about specific exports and imports related measures.

Increase in MSP is not the only solution and Government realised that it is more important that farmers should get full benefit of the announced MSP. In this Budget, it announced whenever the price in the agricultural produce market is less than the MSP, then in that case Government will purchase either at MSP or work in a manner to provide MSP for the farmers through some other mechanism. The detailed guidelines will be put in place by Niti Ayog, in consultation with Central and State Governments.

Earlier, in our report on suggestion for Union Budget (FY19), we had recommended that the Central Government should come out with a scheme, say 'Bhavantar Krishi Yojana' for all Kharif and Rabi crops. This scheme will help farmer in situations when wholesale price of the crop is less than the MSP (as it happened this fiscal, Fiscal impact on Government will be minimal as procurement cost will be reduced substantially. It may boost production as extra buffer (in the terms of Model Sale price) will encourage farmers.

INFRASTRUCTURE: PHYSICAL AND DIGITAL

The Government has enhanced allocation for the Infrastructure Sector in the Union Budget 2018-19, recognizing its role as the growth driver of the economy. The budgetary and extra budgetary expenditure for the Sector has been increased from Rs 4.94 lakh crore in 2017-18 to Rs 5.97 lakh crore in 2018-19. An all-time high allocation of Rs 1,34,572 crore has been made for the transport sector.

In the Urban Infrastructure Sector, the Government proposed to develop ten prominent tourist sites as Iconic Tourism destinations through holistic infrastructure and skill development. In addition, tourist amenities will be upgraded at 100 Adarsh monuments of the Archaeological Survey of India (ASI). 99 cities have been selected with an outlay of Rs 2.04 lakh crore under the Smart Cities Mission.

Under AMRUT program, State level plans of Rs 77,640 crore for 500 cities have been approved. Water supply contracts for 494 projects worth Rs 19,428 crore and sewerage work contract for 272 projects costing Rs 12, 429 crore has been awarded. 482 cities have started Credit rating and 144 cities have got investment grade rating.

The Finance Minister has also announced that his Ministry will leverage the India Infrastructure Finance Corporation Limited (IIFCL) to help finance infrastructure projects including investment in education and health infrastructure.

In the Road sector, the recently approved Bharatmala Pariyojana aims to develop about 35,000 km of highways at a cost of Rs 5,35,000 crore in Phase I. The National Highways Authority of India (NHAI) will consider organizing its road assets into Special Purpose Vehicles and use innovative monetizing structures like Toll, Operate and Transfer (TOT) and Infrastructure Investment Funds (InvITs) for raising funds.

In order to enhance connectivity in border areas, the Finance Minister announced that the Government will take up construction of tunnel under Sela Pass. He also announced that for promoting tourism and emergency medical care, the Government will make the necessary frame work for encouraging investment in sea plane activities.

In the Civil Aviation Sector, the Budget 2018-19 announced a new initiative NABH Nirman to expand airport capacity by more than five times to handle a billion trips in a year. The expansion will be funded by leveraging the balance sheet of Airports Authority of India.

In the sector of Digital Infrastructure the Union Budget 2018-19 announced a doubling of allocation on Digital India Program to Rs 3073 crore in 2018-19. Department of Science and Technology will launch a Mission on Cyber Physical Systems to support establishment of centres of excellence for research in training and skilling in robotics, artificial intelligence, digital manufacturing, big data analysis and quantum communication.

Rs 10,000 crore have been provided in Budget 2018-19 for creation and augmentation of telecom infrastructure. The Government proposes to set up 5 lakh Wi-Fi hot spots which will provide broadband access to 5 crore rural citizens. The Finance Minister informed that the Phase I of Bharatnet Project has already enabled broadband access to over 20 crore rural Indians.

FM also announced that NITI Aayog will initiate a national program to direct efforts in the area of artificial intelligence. To harness the benefit of emerging new technologies, the Department of Telecom will support establishment of an indigenous 5G Test Bed at IIT, Chennai.

The Government will take all measures to eliminate the use of crypto-assets in financing illegitimate activities. The Government will also explore the use of block chain technology for ushering in digital economy.

RAILWAYS

- In keeping with the Government's focus on strengthening the Railways network in the country the Union Budget 2018-19 has enhanced the allocation for the Ministry. The major highlights are as follow:
- Railways' Capex for the year 2018-19 has been pegged at Rs 1,48,528 crore. Of this, the market borrowings are expected to be in the range of about Rs 55,000 crore. Include extra budgetary resource – institutional finance of about Rs 26,400 crore, to be used for project finance; and Rs 28,500 crore for procuring rolling stock.
- 18,000 kilometres of doubling, third and fourth line works and 5000 kilometres of gauge conversion would augment capacity and transform almost the entire network into Broad Gauge.
- 12000 wagons, 5160 coaches and approximately 700 locomotives are being procured during 2018-19.
- Over 3600 kms of track renewal is targeted during 2018-19. There will be increasing use of technology like ''Fog Safe'' and ''Train Protection and Warning System''. 4267 unmanned level crossings in the broad gauge network will be eliminated in the next two years.
- All stations with more than 25000 footfalls will have escalators. All railway stations and trains will be progressively provided with Wi-Fi. CCTVs will be provided at all stations and on trains to enhance security of passengers.
- In Bengaluru, a suburban network of approximately 160 kilometers at an estimated cost of Rs.17,000 crore is being planned to cater to the growth of the metropolis.
- Operating ratio has improved from 96.0 in FY18 to 92.8 in FY19.

Railway Financial (Rs Crore)

Components (Rs Cr)	FY16	FY17	FY18 (RE)	FY19 (BE)	FY19/ FY18 (% Gr)	FY18/ FY17 (% Gr)	FY17/ FY16 (% Gr)	5 Yr CAGR (FY14-18 in %)	Decadal CAGR (FY09-18 in %)
1. Total Receipts	168380	165382	187425	201090	7.3	13.3	-1.8	7.0	9.7
2. Gross Traffic Receipts	164334	165292	187225	200840	7.3	13.3	0.6	7.6	9.9
2.1 Passenger Earnings	44283	46280	50125	52000	3.7	8.3	4.5	8.2	9.6
Passenger Earnings / Gross Traffic Receipts (%)	26.9	28.0	26.8	25.9					
2.2 Freight Earnings	109208	104339	117500	121950	3.8	12.6	-4.5	5.8	9.2
Freight Earnings / Gross Traffic Receipts (%)	66.5	63.1	62.8	60.7					
2.3 Other Earnings*	10843	14673	19600	26890	37.2	33.6	35.3	21.1	17.8
3. Total Miscellaneous Receipts	4046	90	200	250	25.0	121.5	-97.8	-51.6	-21.6
4. Total Expenditure	149151	160469	181000	188100	3.9	12.8	7.6	8.3	10.7
5. Revenue net of dividend payouts	10733	4913	6425	12990	102.2	30.8	-54.2	14.5	4.1
Memoranda									
Gross Traffic Receipts (% of GDP)	1.2	1.1	1.1	1.1					
Net Revenue (% of GDP)	0.1	0.0	0.0	0.1					
Operating Ratio	90.0	96.5	96.0	92.8					

Note:1. *Other earnings are defined as the sum of other coaching earnings, sundry other earnings and suspense.

Source: SBI Research

NATIONAL GOLD POLICY

India is one the largest importers of gold since time immemorial. Our country has the largest stocks of gold, mostly collected through imports and accumulation over centuries. Gold enjoys a distinct position in Indian social customs and traditions. It is regarded as a sign of prosperity, store of value, a hedge against inflation and an easy collateral for cash. Gold also has deep social security features particularly for women in the form of stree-dhana which is the intergenerational transfer of wealth to bride during marriages. The dynamics of yellow metal therefore cannot be ignored in any discussion of Indian economy because of its impact on exchange rate management, fiscal policy and overall financial stability.

RBI constituted a Working Group in 2013 to study issues related to gold import and gold loans by NBFCs. But perhaps time has come that serious thought be given to regarding a comprehensive national policy on gold. Such thought is not new, for an idea regarding a comprehensive policy on gold had taken base at the start of financial sector reforms in 1992 when imports of gold where liberalized. This year's budget explicitly talks about a comprehensive Gold Policy to develop gold as an asset class.

Since independence, policies relating to gold have centered around five elements: i) make people migrate away from gold to other asset classes, ii) regulate the supply of gold, iii) reduce smuggling, iv) reduce household demand of physical gold and v) reduce price of gold in domestic market. To this we may add a sixth element following recent RBI studies vi) exchange rate management and financial stability.

Gold is a surrogate for foreign exchange and is a hybrid between a commodity and a financial asset. Thus in a liberalized regime, comprehensive policy on gold is also linked to capital account convertibility (CAC). The two influential Tarapore Committee reports recommended among other things a comprehensive policy on gold as precondition to CAC. Committee reports on CAC therefore stressed that over the years efforts should be made to develop a vibrant market for gold, gold related derivatives where both resident and non-residents can be allowed to participate. The stress was on the need to develop gold related financial products such as gold deposit schemes and gold accumulation plans through banks and exchange traded gold funds through mutual funds. Some of these recommendations are in various stages of development, but the seventh question in respect of gold policy is how the policy should integrate with financial sector reforms and CAC. Finally given the unique nature of gold, should there be a special regulator for gold and how will regulatory overlaps arising out of such an arrangement be addressed?

No discussion on gold will be complete without understanding how it ultimately gets accounted in national income i.e. GDP. Gold today constitutes an important item in balance of payments accounting with a share of 8.7% of total imports. In the national income accounting, under the head 'valuables' (which includes gold and other valuable items) now account for 2.5% of the GDP in FY13. Under the United Nations System of National Account 1993 (UNSNA 1993) gold is classified as: i) monetary gold, ii) gold held as store of value and iii) used as industrial purposes. The first category of gold (monetary gold) kept with Central Banks is treated for financial purposes while the transaction of gold in remaining two categories (non-monetary gold) is treated as transaction in commodity. Furthermore, under the UNSNA1993 which CSO implemented in 2000, the valuables are placed under Gross Capital Formation (GCF) as a separate heading which has inflated the CGF figures, while reducing the savings and also private final consumption expenditure (PFCE) as gold purchases are not treated as part of consumption under UNSNA1993. Hence, neither the popular perceptions that the household purchase of gold constitutes physical savings nor the perception that it is consumed by household, reflects in national income accounting. RBI 2011 working paper succinctly highlighted this anomaly that classifying valuables under GCF while not accounting them in savings or consumption implies valuables portion of GCF have no saving (financing) counterpart. Hence, it may be incorrect to treat valuables and hence gold purchases by household as GCF in the economy from technical as well as behavioral point of view (consumption, investment and social security motives).

In a similar token, IMF balance of payment manual BPM06 also retains the monetary and non-monetary classification of gold, but excludes jewellery from non-monetary gold and puts jewellery under merchandised imports. 75% of our gold demand comprise of jewellery, remaining 23% in the form of coins and bars (termed as investments demand) and rest is industrial. However, behavioral aspect of keeping jewellery is guided by consumption, investment and social security motives suggesting that gold should not be include in merchandised purchases. Further its inclusion in merchandise implies it is consumed by households but same does not feature in PFCE.

To an extent the aforesaid criticism of UN SNA 1993 stands addressed with CSO adopting the UN SNA2008 in 2016 by including a small part of the savings in valuables as assets of the household. But the conceptual problem that UN SNA 1993 has continues to plague the UN SNA 2008 because it is not in conformity with customs and preferences of the Indian household who save in gold irrespective of its from as bullion or jewellery. Furthermore, the distortions in savings and valuables portions of GCF in new estimates is even more glaring as ‘valuables constitute a negligible 1% of the total saving, whereas under GCF, “valuables” constitute about 7.5%’.

To conclude, gold constitutes a very important portion of household purchases. The present treatment of gold under national income, balance of payment and its links to CAC all need careful harmonization. At present there is no such policy that tries to reconcile these divergent aspects. We feel a gold policy is more appropriate approach to long term solution to so called gold problem. Household diversification of savings into other financial contracts like mutual funds and pension funds (including gold as pensionable asset) must also be facilitated along with active monetization of gold.

TAX PROPOSALS

Individual

These is gross disappointment for individual tax payer as income tax slab and rates remains unchanged.

Union Budget 2018-19 proposes to provide a standard deduction of Rs 40,000 from salary income to employees but also proposes to take away transport allowance, medical reimbursement and other allowances. Prima facie income exempted from tax after setting off the gain and loss is Rs 5800 only (Rs 40,000 minus 15,000 plus Rs 19,200). The tax saved for each employee on this income would depend on the tax slab that income falls into. The saving in tax would be Rs 290 for those currently paying 5% tax on this income; Rs 1160 for those paying 20% tax on this income; and Rs 1740 for those paying 30% tax on this income.

However, these savings would be nullified in most cases, except in the case of income up to Rs 5 lakh, due to increase in the cess payable from current 3% to 4% on the rest of the income tax payable by the individual. As a consequence, individuals with income above Rs 5 lakh would end up shelling out more tax after taking into account the standard deduction, the removal of the allowances and the increase in cess. We believe that this standard deduction should be around Rs 50,000 instead of the proposed Rs 40,000.

However, the pensioners will be benefited substantially, as earlier they don’t get any standard deductions/ allowances as applicable to the salaried employees. They will save the tax payable on this entire amount of deduction but of course have to pay the increased cess on the balance income.

Senior Citizen

With an objective of providing a dignified life to the senior citizens, the Finance Minister has announced a number of incentives measures in the budget. This will benefit around 9 crore senior citizens (Census 2011) in the country. The important announcements are:

The exemption of interest income on deposits with banks and post offices to be increased from Rs 10,000 to Rs. 50,000 and TDS shall not be required to be deducted on such income, under section 194A. This is applicable to all the interest income from all fixed deposits schemes and recurring deposit schemes.

FM has also announced to raise the limit of deduction for health insurance premium and/ or medical expenditure from Rs. 30,000 to Rs. 50,000, under section 80D. All senior citizens will now be able to claim benefit of deduction up to Rs 50,000 per annum in respect of any health insurance premium and/or any general medical expenditure incurred. In addition to that, Government also proposed to increase the limit of deduction for medical expenditure in certain critical illness to Rs 1 lakh in respect of all senior citizens, under section 80DDB.

All these concessions will give an extra tax benefit of Rs 4,000 crores to senior citizens and on the same vein this much amount of tax foregone. To give the assured return of 8% to the senior citizens, Government has extended the Pradhan Mantri Vaya Vandana Yojana up to March 2020. The scheme is managed by LIC of India. The existing limit on investment of Rs. 7.5 lakh per senior citizen under this scheme is also being enhanced to Rs. 15 lakh.

LONG-TERM CAPITAL GAINS TAX ON EQUITIES

On the back of buoyancy of equity market, the Government has now imposed long term capital gains tax on capital gains exceeding Rs 1 lakh at the rate of 10% without allowing the benefit of any indexation. However, all gains up to 31st January, 2018 will be grandfathered. The gains from equity share held up to one year will remain as short term capital gain and will continue to be taxed at the rate of 15%. Further, a tax will be introduced on distributed income by equity oriented mutual fund at the rate of 10% to provide level playing field across growth oriented funds and dividend distributing funds. It is expected that revenue mobilisation to the tune of Rs 20,000 crore will happen due to these measures.

Global Experience

USA: Net capital gain income (assets held longer than 12 months) is taxed at ordinary rates, except that the maximum rate for long-term gains is limited to 0% for individuals in the 10% or 15% bracket, 20% for individuals in the 39.6% bracket and 15% for individuals in all other brackets. Net capital gain is equal to the difference between net long-term capital gains over net short-term capital losses. Short-term capital gains are taxed as ordinary income (10-39.6%)

UK: For gains realized on all disposals other than those realized on residential property disposals, a 10% rate applies to chargeable gains that fall within the individual's basic rate band limit, after taking into account income as calculated for income tax purposes. Chargeable gains in excess of the basic rate band are charged at a rate of 20%.

Australia: Trading stock acquired for the purpose of resale is not subject to capital gains treatment.

Canada: 50% of the year's capital gains are included in taxable income, to the extent that the amount exceeds 50% of capital losses for the year. This includes capital gains on real estate and personal property, regardless of whether used in a trade or business, and on shares held for personal investment. The federal government, as well as the provinces and territories, impose income taxes on resident individuals, with rates varying from 15-33% for federal Government and 22-27% for provinces.

China: Capital gains derived from transfers of shares listed on China stock exchanges in the secondary market are temporarily exempt.

Brazil: Capital gains derived from the sale of shares listed on Brazilian stock exchanges are taxable if the sale price exceeds BRL 20,000.

Malaysia: No Capital gain Tax.

Thailand: Gains derived from sales of shares are generally subject to Personal Income Tax (PIT). However, gains derived from sales of securities listed on the Stock Exchange of Thailand are exempt from tax.

Indonesia: Capital gains are added to income from other sources to arrive at total taxable income and is taxed at progressive rates (varying from 5-30%).

TAX COMPLIANCE AND GST COLLECTIONS

As per an IMF Staff Report, tax compliance broadly means meeting legal obligations imposed by the tax system. So tax compliance comprises bringing more people in the tax net and then making sure that they pay their taxes in a proper legal format. The extent of compliance with the legal obligations it imposes powerfully affects the revenue yield, efficiency and fairness of any tax system.

The Report says that a range of policy choices strongly affect compliance and compliance challenges should shape policy. According to the report higher tax rates generally discourage compliance: the large reduction in higher rates of personal income tax with the adoption of the flat tax in Russia, for instance, appears to have improved compliance. Policies can also be calibrated to compliance problems: a minimum corporate tax, for instance, and royalties in the case of the extractive Industries (EIs), are often recommended, especially but not only in lower income countries, to limit evasion and avoidance. Simple tax rules, all else equal, are evidently better for well-informed compliance.

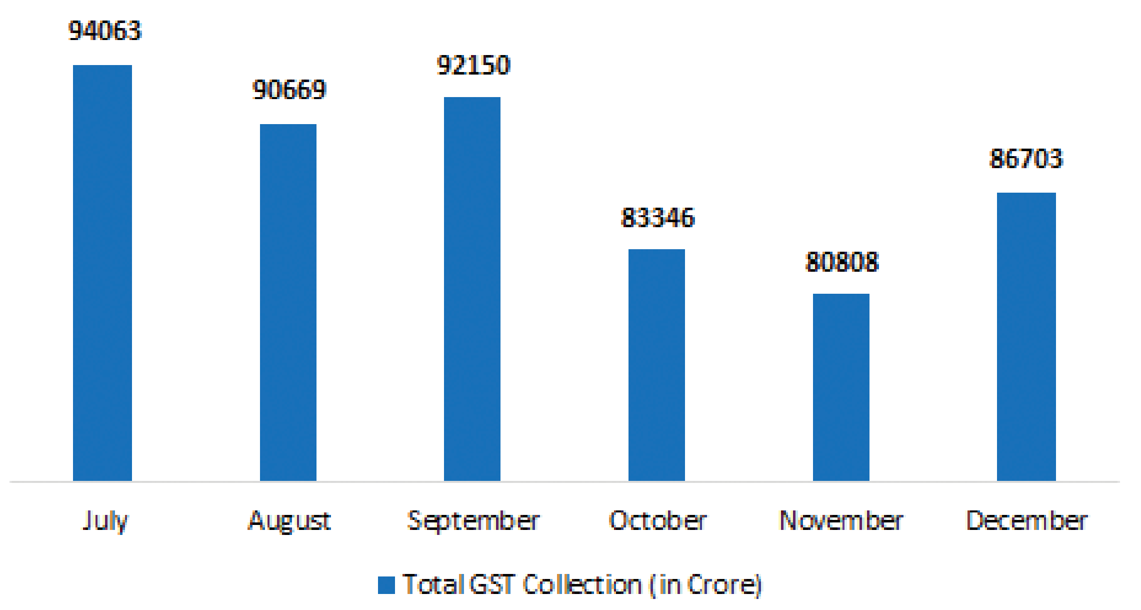
By reducing tax compliance costs and thereby lowering the overall tax burden on small businesses, simplification provisions help achieve more neutral tax treatment of firms of varying sizes, implying efficiency gains, and encourage compliance with (adherence to) the tax laws of a country, including operating in the formal rather than informal.

Case in India

In India, GST implementation is facing certain initial hiccups which are hindering overall tax compliance. In order to increase tax revenue, Government has incentivized business community to comply with the norms and file various returns. Though, the number of returns filed has increased but it has to be seen against the backdrop of relaxation/ deferment of filing of certain returns (GSTR2) and other relaxation of norms including Reverse change mechanism.

GST since its inception in July’17, had registered a steady drop till Nov’17 but the collections for Dec’17 gathered momentum by registering around Rs 6,000 crore addition (7.3% growth) as compared to the Nov’17 collection.

Total GST Collections (in crore)



Source: SBI Research

The receipts rose in December despite the cut in tax rates on 178 goods from 28% to 5% in November. The GST council of India in its 23rd meeting held in Nov'17 has taken various initiatives by relaxing various compliance norms, like extending the last dates of filing returns and summary monthly filing (Form 3B) instead of detailed filing for the entire fiscal year. Some other modifications made are as follows:

- Taxpayers with annual aggregate turnover of up to Rs 1.5 crore to submit Form GSTR 1 on quarterly basis and Taxpayers with annual aggregate turnover above Rs 1.5crore to submit Form GSTR 1 on monthly basis (with GSTR 2 and 3 being suspended).

- To address the difficulty of invoice matching procedure, the Government has decided to suspend the same during the current fiscal year and re-examine it more closely.

- The penalty for late filing of monthly summary return has been reduced substantially.

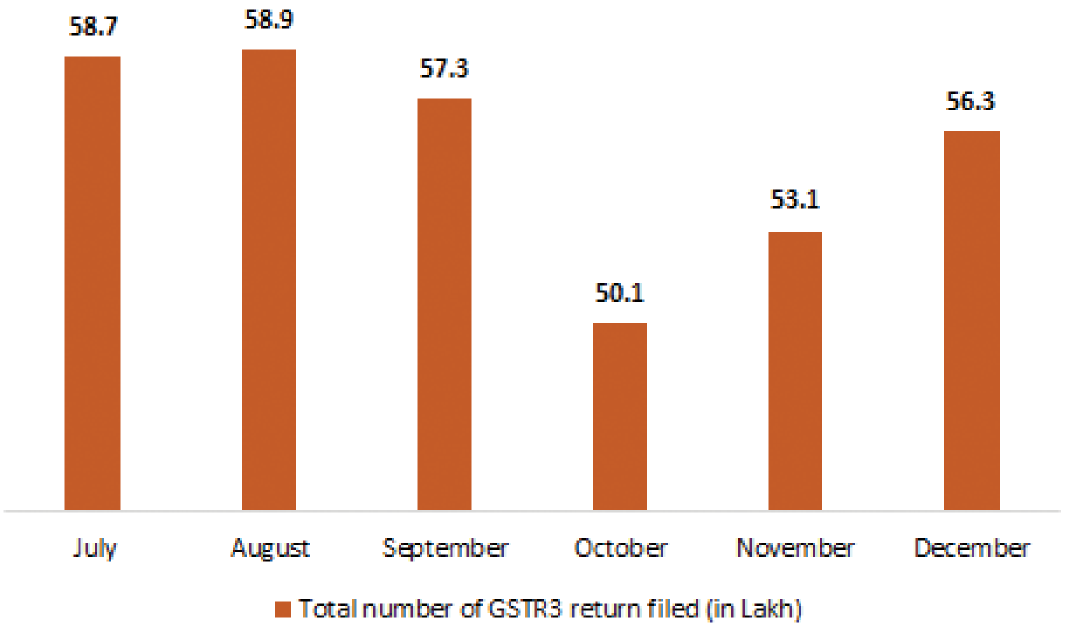
- Raising of turnover for composition scheme from Rs 75 Lakh to Rs 1 crore and deferment of E-way bill provisions till Apr'18 are indeed a big relief which will help trade and industry in getting adjusted to the GST compliance.

- E-wallet scheme for exporters and move to reimburse them within the next week, was a much needed step and would help exporters save costs of working capital.

- Service providers having annual aggregate turnover below Rs 20 lakh (Rs 10 lakh in special category States except Jammu & Kashmir) exempted from obtaining registration, even if they are providing services through an e-commerce platform.

The trend in filing of GSTR 3B return since Jul'17 indicates that number of persons filling tax declined up to October following which the pace has increased and is touching close to the July figure. This further signifies that due to the relaxation in compliance norms, more taxpayers are now coming under the tax base and filing returns.

Number of GSTR3 Returns Filed (in lakh)



Source: SBI Research

Global experiences also suggests that the countries which have implemented GST have not witnessed any extreme fluctuation in the tax revenues as a % of GDP. For Canada, though its tax revenue to GDP has not yet reached the pre-GST levels, however, the absolute amount of tax collections has increased. Meanwhile, Singapore has witnessed an increase in tax collection post GST. Malaysia introduced GST in 2015 so the time period is too small to form a definite opinion. Size of informal economy in Singapore has reduced to 12.2% in 2006 from around 14% in mid-1990s. Even according to new figures from Statistics Canada the country's underground economy has reduced to about 2.4% of GDP. Thus it can be hoped that in India's case as well the informal economy will be reduced significantly going forward.

GST implementation: Impact on tax revenue in select countries

Country	Year of implementation	Approximate Size of informal economy (% of GDP, 2006)	Tax to GDP prior to GST (%)	Tax to GDP during GST implementation (%)	Tax to GDP post GST (%)
Singapore	1994	12	10	12	11
Malaysia	2015	31	15	14	14
Canada	2008	15	13	12	11

Source: World Bank, EY, SBI Research

Country-wise GST - Year of Implementation and Peak Rate

Country	Year of Implementation	Peak Rate (%)	Country	Year of Implementation	Peak Rate (%)
Denmark	1967	25	Hungary	1988	27
France	1968	20	Estonia	1991	20
Germany	1968	19	Cyprus	1992	19
Netherlands	1969	21	Czech Republic	1993	21
Sweden	1969	25	Poland	1993	23
Luxembourg	1970	17	Slovak Republic	1993	20

Country-wise GST - Year of Implementation and Peak Rate					
Country	**Year of Implementation**	**Peak Rate (%)**	**Country**	**Year of Implementation**	**Peak Rate (%)**
Belgium	1971	21	Bulgaria	1994	20
Ireland	1972	23	Finland	1994	24
Austria	1973	20	Lithuania	1994	21
Italy	1973	22	Latvia	1995	21
United Kingdom	1973	20	Croatia	1998	25
Portugal	1986	23	Malta	1999	18
Spain	1986	21	Romania	1999	24
New Zealand	1986	15	Slovenia	1999	22
Greece	1987	23	Australia	2000	10
Source: EY; SBI Research					

ARE INCOME TAX COLLECTION NUMBERS AMBITIOUS? INDIA'S DIRECT TAX BUOYANCY

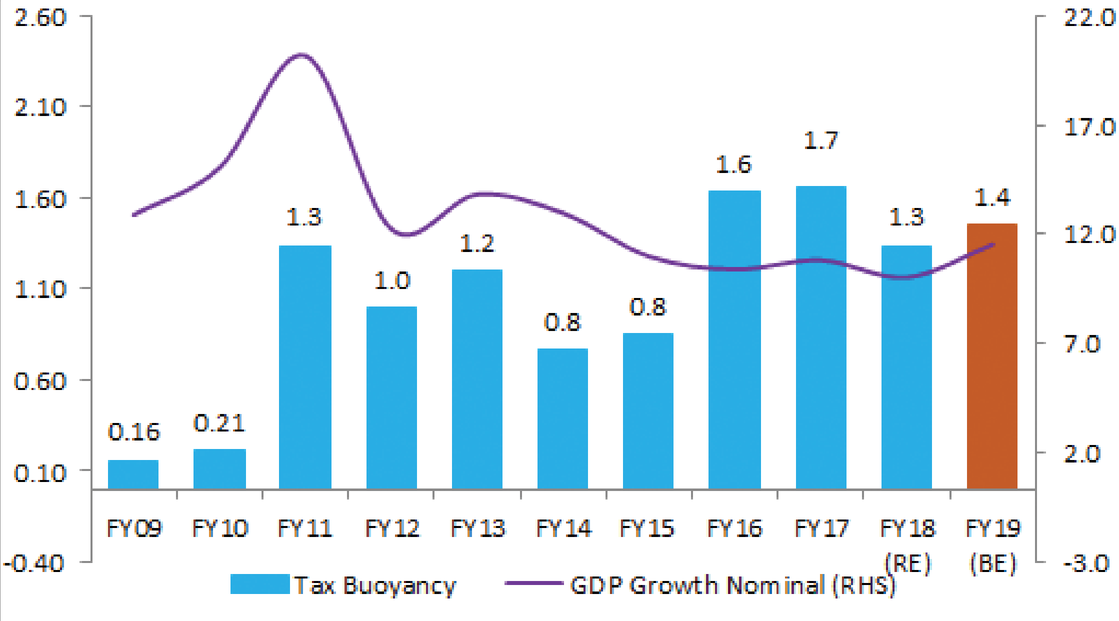
According to CBDT data, the number of effective assesses has shown a CAGR of 7% from the Assessment Year (AY) 2012-13 to AY 2016-17. The number of individual tax payers for AY 2016-17 was around 59 million. This translates into around only 4% of the entire population paying taxes.

Number of Effective Assessees					
PAN Category	**AY 2012-13**	**AY 2013-14**	**AY 2014-15**	**AY 2015-16**	**AY 2016-17**
Association of Person	124010	141019	159520	179539	185235
Body of Individuals	5688	6222	7020	7465	8035
Company	654766	707771	748237	768268	764410
Firm	995648	1044646	1094509	1160540	1183586
Government	94	208	338	483	708
Hindu Undivided Family	931387	964512	1002644	1054642	1028580
Artificial Juridical Person	9897	10197	10576	11114	11074
Local Authority	5459	6064	7160	7552	8063
Individual	44346852	49752118	53958653	57837733	59273878
Trust	193781	206219	217660	231144	228392
Source: CBDT, SBI Research					

According to the budget the number of effective tax payer base increased from 6.47 crores at the beginning of FY15 to 8.27 crores at the end of FY17. The recently released economic survey says that there does seem to have been a substantial increase in the number of new taxpayers post demonetization and GST. The survey compares the total number of new taxpayers in the 13 months since demonetization (Nov'16 – Nov'17) with previous 13-month time windows. According to the Survey, after Nov'16, 10.1 million filers were added compared with an average of 6.2 million in the preceding six years.

According to CBDT data direct tax buoyancy has improved in FY17. The budget also revealed the average buoyancy in personal income tax of seven years preceding these two years as 1.1. However, the buoyancy in personal income tax for FY17 and FY18 (RE) is 1.95 and 2.11 respectively. This indicates that the excess revenue collected in the last two financial years from personal income tax compared to the average buoyancy pre FY17 amounts to a total of about Rs 90,000 crore and the same can be attributed to the strong anti-evasion measures taken by the Government. This augurs well for the economy as our tax revenues are sensitive to growth rate. However, in a country where close to only 4% of the population pays taxes, it is urgently needed that the tax base be increased so that austerity measures are not required to remain on the path of fiscal consolidation. Also, according to an independent study, India is at the cusp of average income threshold of $2000 beyond which income tax collections as a per cent of GDP tend to rise sharply from 1% of GDP to around 5% of GDP. Combined with formal job creation happening in India, this provides the initial condition for a fiscal revolution in India.

Tax Buoyancy



Source: SBI Research

INSURANCE & PENSION REFORMS

Internationally, insurance penetration and density reflects the level of development of insurance sector in a country. Despite several measures, the insurance penetration of India is staggering at a very low level (3.49% in 2016: Life 2.72% & Non-life 0.77%), compared to advanced countries like US 7.31%, UK 10.16% and South Africa 14.27%. However, the Indian insurance industry faces a number of difficulties like higher claim ration, low premium collections, capital raising, tight regulations etc.

Though, there were several demands from the insurance sector but Government has not proposed any measures to increase the insurance penetration in the country, which is staggeringly low compared to other global peers. However, Government has focused on a number of issues like health insurance, pertaining to the insurance sector, which are discussed in a detail as follows:

Listing at Stock Exchanges

- In the Budget 2016-17, Government was proposed that the general insurance companies owned by the Government to be listed in the stock exchanges.
- To meet the desired capital and bring efficiency among the insurers, the Insurance Regulatory and Development Authority of India (IRDAI) has allowed insurance companies who have completed 10 years of operations to raise capital through Initial Public Offerings (IPOs). The Union Cabinet has also approved the public listing of five Government-owned general insurance companies and reducing the Government's stake to 75% from 100%, which is expected to bring higher levels of transparency and accountability, and enable the companies to raise resources from the capital market to meet their fund requirements.
- As per the IRDAI regulations, there are more than 30 insurers, who are operating in India in any form, are eligible to go to the market to raise the required capital. However, only 6 insurers (2-public) has raised

capital from the market, in the way of stake sale by listing themselves in the stock exchanges. However, the concerns is that most of the stocks of these insurers are listed/trading below to the issue price.

- Further, in the present budget, Government has proposed to merge the rest 3 public sector general insurance companies, namely National Insurance Company Ltd, United India Assurance Company Ltd and Oriental India Insurance Company Ltd, to create a single insurance entity and will be subsequently listed at the stock exchanges.
- However, the major concern is that the reserved portions for retail and wealth investors in all 6 insurance IPOs in FY18 were under-subscribed. The reason for decline in stock price and the poor response from retail and HNIs (high net worth investors) could be because of the complex nature of insurance business and their expensive valuations. So, Government may not get any good price in the disinvestment of the proposed merged entity, as investors may not have benefitted in the earlier insurance IPOs.

Health Insurance

At present, India has the *Rashtriya Swasthya Bima Yojana (RSBY)* that was envisaged to provide health insurance coverage to families of Below Poverty Line families. It's beneficiaries are entitled to hospitalisation coverage of up to Rs 30,000 for most diseases, while the amount is very negligible. As per estimates, around 63 million people have been driven into poverty due to the high cost of healthcare. In addition to that, around 70% of the country's population live in rural areas and around 22% is below poverty level. In the Budget, Government has proposed the following measures in the health insurance segment:

- Proposal to launch a flagship National Health Protection Scheme to cover more than 10 crore poor and vulnerable families (50 crore individuals approx.), which aims to provide coverage upto Rs 5 lakh per family per year for secondary and tertiary care hospitalization. In FY17, 33 crore individuals has covered under RSBY. Going forward, if the new flagship scheme is implemented in a mission mode, like Jan Suraksha schemes, this will be the world's largest government funded health care programme and will bring smiles in the faces of crores of people in the country.
- The new health protection scheme will encourage people to take health insurance given the fact that penetration of health insurance is quite low in India compared to emerging economies. Health insurance penetration in India is only around 5% overall with about 13-15% in urban areas. So, we believe Government should provide the same scheme to the middle class families with a low premium.
- The proposal to raise the limit of deduction for health insurance premium to Rs 50,000 from Rs 30, 000, for senior citizens will help to reduce the burden of healthcare expenditure for the aged.
- In line with the long-term motor insurance, Government has proposed that the individuals can buy long-term health insurance schemes, while the tax deductions would be allowed proportionately over the years. This long-term policies will reduce the premium paid by the individuals in buying the health insurance schemes and also help the insurers to focus on new customers, rather renewals for every year.

Insurance for All

Consequent to the Union Budget 2015-16 announcement, the Prime Minister launched three new social security schemes under Jan Suraksha initiative on 09 May 2015. The schemes include: (i) Pradhan Mantri Suraksha Bima Yojana (PMSBY) covering accidental death risk of Rs 2 lakh at a premium of Rs 12 per year i.e. Rs 1 per month; (ii) Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY) covering both natural and accidental death risk of Rs 2 lakh. The premium will be Rs 330 per year, or less than Rs 1 per day, for the age group of 18-50 Year; and (iii) Atal Pension Yojana (APY). Earlier, Government has declared the accidental insurance benefit of Rs 1 lakh and Rs 30,000 of life insurance under to Jan Dhan bank accounts. The Government has introduced the scheme with the objective of increasing insurance and pension penetration in the country. Under the Jan suraksha schemes, there are 5.22 crore families has enrolled in PMJJBY and around 14 persons have been insured through PMSBY.

- In the Budget, Government has targeted to cover all the poor households, including SC/ST households, under these scheme in a mission mode. This is a very welcome step and expected to cover all the households in the country.
- Further, to expand the coverage under Prime Minister Jan Dhan Yojana (PMJDY) by bringing all 60 crore basic accounts within its fold and undertake measures to provide services of micro insurance and unorganized sector pension schemes through these accounts.

Overall, the budget has concentrated much on the health insurance segment. If the above schemes are implemented successfully, the health insurance penetration in the country will increase by at least 2%. However, Government has not given any tax deductions to life/general insurance business, which has been much anticipated. Going forward, we still believe that, insurance should not be taxed in India, as it is an instrument that provides financial protection against risk. Further, in India the insurance penetration is low; the introduction of GST in the realm of insurance may not represent the best step forward.

NPS & PF

In the last 3-years, Government has taken a number of steps to create more jobs and facilitated more number of employment. In order to incentivize creation of new jobs in the formal sector, Government has contributed 8.33% (that is employer's contribution) and 12% for in sectors employing large number of people like textile, leather and footwear, for all new employees enrolling in EPFO for the first three years of their employment. To carry forward this momentum, Government has proposed to contribute 12% of the wages of the new employees in the EPF for all the sectors for next three years. It has announced to extend the benefit of exemption for withdrawal up to 40% from National Pension System Trust (NPS) to all subscribers and not only to employees.

Section 2: Corporate & Industry

Executive Summary

- Keeping the New India in Mind - MSME sops, merger in insurance sector and 'Make in India' to lead the march ahead upto FY2019.
- This budget has silently done one quiet job. The 'Make in India' initiative has been kept on track. Customs duty on slew of items has been increased. The automobile and auto ancilliary sector are such sectors which may require to source components from domestic units instead of imports. The capacity utilisation levels of these sectors are likely to see improvement once the increased customs tariffs kick in. The 'Make in India' initiative could also provide boost to domestic auto ancilliary industry by setting up units in electric vehicle space. This should prompt foreign entities to set up manufacturing of electric vehicle here, and boost private investment.
- In FMCG, rural incomes are likely to get a boost based on improved price discovery for farmers, better social security measures. Government spending on rural infrastructure to aid farm income is likely to broaden the consumption base.
- Fertiliser sector may see some stability due to stable rural incomes, health scheme coverage and better price discovery for agriculture produce. In Insurance, merger of three large government entities may consolidate before getting listed on the bourses. The Government thinking on insurance appears to be clear and on a guided path. India appears to be unlocking the value of its large Government entities.
- Further, MSME entities with turnover less than Rs.250 crore would have to shell out lower corporate tax. Auto ancilliary, FMCG and fertilizer and a host of sectors benefitting from turnover of less than Rs.250 crore.
- In infrastructure, Government may leverage India Infrastructure Financial Corporation Ltd (IIFCL) to lend to infrastructure to unburden the banking sector of funding infrastructure. Marquee infra programs such as Bharatmala and Sagarmala may look upon IIFCL for its funding requirement.
- On anvil is National Highway Authority of India this year may monetise its revenue earning assets to follow the investment trust route for listing, like IRB InVIT. This would allow NHAI to look at alternative funding source to pursue its growth plans beyond debt raising.

Sector : FMCG — Overall Impact : Positive

Budget Proposals and Impact

- Lower corporate tax for MSME listed entities with turnover of less than Rs. 250 crore.
- Facilitate rural consumption through increasing farm incomes.
- Increase in Minimum Support Price (MSP) for Kharif crops
- Develop and upgrade existing 22000 rural haats into Gramin Agricultural Markets (GrAMs) to provide farmers facility to directly sell to consumer and bulk purchasers.
- GrAMs to be linked electronically to E-NAM (Electronic-National Agricultural Market) and exempt from regulations of APMC for sales to end consumers.
- Enable price discovery through direct sale of produce to consumers.
- e-NAM Network- about 470 APMCs (Agricultural Produce Market Committee) out of 585 APMC have been connected to e-NAM network and the balance would be connected by March 2018.
- Agri-Market Infrastructure Fund with a corpus of Rs. 2000 crore would be set up for developing and upgrading agricultural marketing infrastructure in the 22000 GrAMs and 585 APMCs.
- National Health Protection Scheme for the 10 crore vulnerable and the poor families providing coverage upto Rs. 5 lakh crore per family for secondary and tertiary hospitalisation is one more step towards boosting consumerism. The budgetary allocation for cultivation of specialized medicinal and aromatic plants is another big positive and will help promote India's Ayurvedic heritage.
- Measures to provide livelihood, agriculture and allied activities and construction of rural infrastructure would entail a budget of Rs. 14.34 lakh crore, including Rs. 11.98 lakh crore extra-budgetary and non-budgetary resources. FMCG are in for good times in the year ahead.

Already a lot has been addressed for the sector since GST announcement in July 2017. In the November 2017 GST council meet most of the items were rationalized under four slabs. About 178 items were brought down from 28% GST tax rate to 5% - 18% tax rate. Namkeens, Khakhra, Roti, Sweets, Snacks fall under 5% bracket. Daily use items such as Milk, Buttermilk, Curd, Honey, Flour, Besan, Bread, puffed rice etc carry 0% rate.

As on 18th Jan 2018, the GST rates break up for number of food items slab-wise is mentioned hereunder:

1. 46 daily use items (excluding sub-categories) fall under 0% tax slab
2. 51 items (excluding sub categories) in 5% tax bracket
3. 25 items (excluding sub categories) under 12%
4. 23 items (excluding sub categories) in 18% tax bracket and 3 items in 28% tax bracket.

Backdrop

FMCG is fourth largest sector in the Indian economy. Recently Government announcement of allowing 100% FDI in single brand retail has set the tone for the FMCG sector, post GST and demonetisation. The restocking has also happened. The recent quarterly results also reflect the sentiment. Based on recent reported result performance, one can expect rating upgrades outpacing downgrades by March 2018. Also, going by FDI inflows, food processing appears to be attracting the attention of foreign investors. Companies too, have braced up for competition for sale through ecommerce. Patanjali Group products are now available on e-platforms. Companies such as Orient Electric also, now sell products through Amazon. This is what is happening in FMCG sector. Traditional sales channel is giving way to app based ecommerce. In its quest for Q-o-Q growth, Orient

Electric launched 'Aerostorm' premium fans exclusively through Amazon in January 2018. It is also offering discounts and cashback for Amazon buyers. The twin blues of demonetisation and GST faced difficulties in doing business during FY2017.

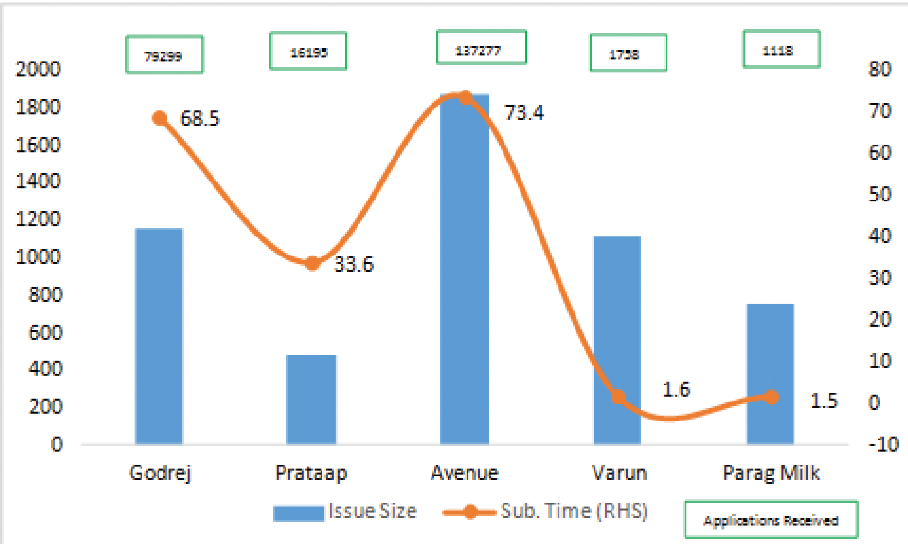
Going by recent December quarterly results of 14 listed companies, Detergents & Intermediates, Food Processing (including Mushrooms) and Indian Dairy Products appear to be faring better. The aggregate Q3FY18 over Q3FY17 numbers are exhibited below for analysis.

Key Financials	Q3FY18 Rs. in Cr	Y-o-Y Change (%)	Q3FY17 Rs. in Cr
Net Sales	13035	10	11837
PBIDT	2577	11	2315
Reported PAT	1740	23	1411
Source: C-Line; data for 14 entities reporting quarterly results for Dec 17			

The sector has four expectations from this year's budget viz., rationalisation of GST, increase in income tax exemption slab, development of infrastructure in rural areas and lower corporate tax. Demand for quality goods has also started coming in from rural areas. The biggest blockbuster IPO of Avenue Supermarts Ltd (Retail Trade) in March 2017, just four months post demonetisation, saw more than Rs. 1,20,000 crore being mopped up during IPO. The all-round support to the IPO issue, the pricing and its popular 'DMART' brand belies the demon in demonetisation. This was one of the biggest notable stories highlighted in the capital market in March 2017.

There were about 11 IPO's (Non-SMEs) viz., Godrej Agrovet Ltd; Prataap Snacks Ltd; Avenue Supermarts Ltd; Varun Beverages Ltd; Parag Milk Foods Ltd; Prabhat Dairy Ltd; Manpasand Beverages Ltd; V-Mart Retail Ltd; Future Consumer Ltd; Bajaj Corp Ltd and Jubilant Foodworks Ltd were some of the major Non-SME IPO launches. The market capitalization in November 2017 stood more than Rs. 1,30,000 crore.

Details of the few of the IPOs that hit Dalal Street in last two years are stated hereunder: -



Note: Issue Size and Application received is in Rs. Crore and Subscribed times in number

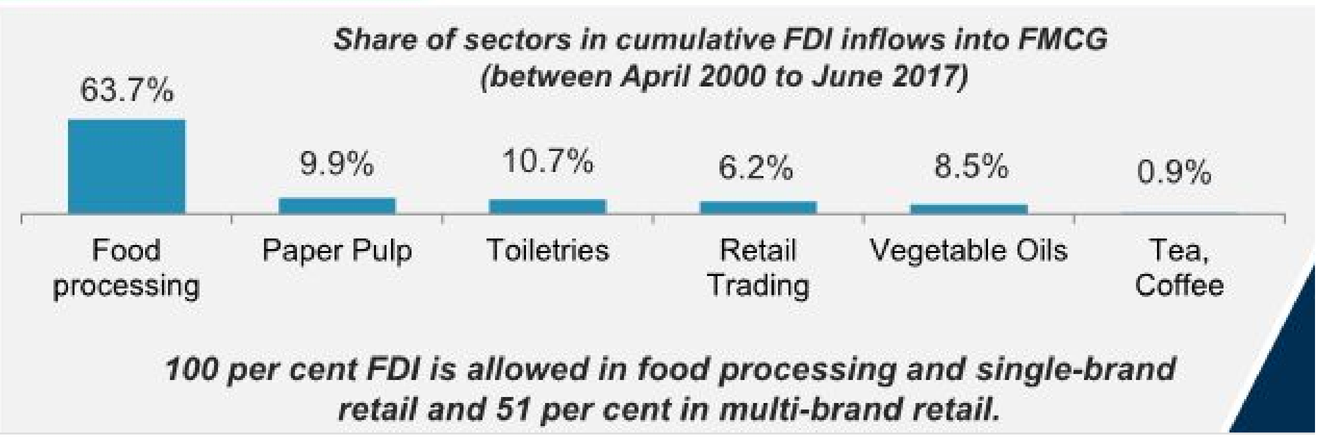
Size of FMCG market in year 2020

Total consumption expenditure [TCE] for 2020F is placed at US$ 3600 bn. FMCG constitutes roughly 3% of TCE.

Macro Trends

FDI Inflows

100% FDI allowed in Food Processing and Single Brand Retail.



Last Budget Announcements

- To Set up of Dairy Processing and Infrastructure Development Fund in NABARD with a corpus of Rs. 2000 crore and will be increased to Rs. 8000 crore over 3 years.
- A model law on contract farming to be prepared and circulated among the States for adoption.
- Coverage of National Agricultural Market (e-NAM) to be expanded from 250 markets to 585 APMCs. Assistance up to Rs 75 lakh will be provided to every e-NAM.

FMCG may be in for surprise through indirect means. Steps taken to promote contract farming, dairy milk processing doubling farmers` income in five years through sale to APMC is likely to reduce cost and bring inflation down. New APMC centres have been announced. In dairy processing, a Dairy Processing and Infrastructure Development Fund would be set up in NABARD with a corpus of Rs. 8000 crore over 3 years. Initially, the Fund will start with a corpus of Rs. 2000 crores. Increase in coverage of National Agricultural Market (e-NAM) is to be expanded from 250 markets to 585 APMCs. Assistance up to Rs. 75 lakhs will be provided to every e-NAM.

In contract farming, the Government proposes to integrate farmers who grow fruits and vegetables with agro processing units for better price realisation and reduction of post-harvest losses. A model law on contract farming would be circulated among the States for adoption.

Credit Ratios

Sector Credit Ratios (Upgrade vis-à-vis downgrades) during April'17 to December'17 as compared to previous year for the same period

Credit Ratio								
Sector	Total No. of Companies (o/s as on Dec 17)	9MFY17			9MFY18			Improvement/ detoriation in Credit Ratio (in bps)
		Upgrades	Downgrades	Ratio	Upgrades	Downgrades	Ratio	
FMCG	3353	260	170	1.53	400	406	0.99	-0.54
Source: CRISIL; SBI Research; numbers are for all rating agencies								

With 400 upgrade and 406 downgrades, credit ratios for the 9MFY18 deteriorated to 0.99 against 1.53 for the same period previous year.

Sectors Performance - Key Financials of Select Companies (Standalone)

Key Financials of Select FMCG Companies for H1FY18 vis-à-vis H1FY17 (Rs in Crore)									
Name of the Company	H1FY18			H1FY17			Growth H1FY18 on H1FY17		
	Net Sales	PBIDT	PAT	Net Sales	PBIDT	PAT	Net Sales	PBIDT	PAT
Hindustan Unilever Ltd	16600	3888	2559	15685	3490	2269	6%	11%	13%
Nestle India Ltd	4862	1062	570	4510	1038	528	8%	2%	8%
Godrej Consumer Products Ltd	2438	578	406	2274	520	365	7%	11%	11%
Britannia Industries Ltd	4451	749	454	4150	699	438	7%	7%	4%
Dabur India Ltd	2650	646	453	2651	649	467	-0.04%	-0.47%	-3%
Source: CLine; SBI Research									

FMCG sector have shown better growth numbers in H1FY18 as compared to H1FY17 as could be observed from the financials of top five companies except Dabur which reported almost flat results.

Market Reaction

Market Movement in last One Month and on Budget Day							
Sector - FMCG Name of the Companies	**01-Jan-18**	**31-Jan-18**	**01-Feb-18**	**"Movement Over 01-Jan-18"**		**Movement on Budget Day**	
Hindustan Unilever Ltd	1344.5	1369.4	1371.3	26.8	1.99%	1.9	0.14%
Nestle India Ltd	7863.2	7469.2	7310.9	-552.3	-7.02%	-158.3	-2.12%
Godrej Consumer Products Ltd	986.3	1053.4	1053.3	67.1	6.80%	-0.1	-0.01%
Britannia Industries Ltd	4738.3	4684.2	4740.5	2.3	0.05%	56.4	1.20%
Dabur India Ltd	349.0	355.6	349.7	0.7	0.20%	-5.9	-1.66%
NIFTY FMCG INDEX	26686.4	27127.3	27351.9	665.6	2.49%	224.6	0.83%
Source: NSE; closing price as on date							

Note: Movement over 1st January and on budget day indicates actual and percentage wise movement

Sector : Iron & Steel — Overall Impact : Positive

Budget Proposals and Impact

- Lower corporate tax for MSME listed entities with turnover of less than Rs. 250 crore.
- Estimated infrastructure need in excess of Rs. 50 lakh crore to connect and integrate the nation with a network of roads, airports, railways, ports and inland waterways.
- 10 Iconic Tourism destinations.
- Allocation to Railway Rs. 1.48 lakh crore for 2018-19 with large part of the Capex is devoted to capacity creation. 18,000 kilometers of doubling, third and fourth line works and 5000 kilometers of gauge conversion.
- Mumbai-Ahmedabad bullet train project
- To add 90 kilometers of double line tracks at a cost of over Rs. 11,000 crore and 150 kilometers of additional suburban network is being planned at a cost of over Rs. 40,000 crore in Mumbai.
- Elevated corridors on some sections.
- 99 Cities have been selected (Smart City) with an outlay of Rs. 2.04 lakh crore.
- Regional connectivity scheme of UDAN to connect 56 unserved airports and 31 unserved helipads across the country.
- Establishment of a dedicated Affordable Housing Fund (AHF) in National Housing Bank.

Rs. 14.34 lakh crore to be spent for creation of livelihood and infrastructure in rural areas in 2018-19 along with Smart City, Bullet Train, UDAN, construction of 10 Iconic Tourism destinations, Affordable housing itself shows huge amount of construction activity are lined up in near term. As no infrastructure can be built without steel, we see the sector will be immensely benefited from the Government's investment estimation of above Rs. 50 lakh crore in Infra to provide good quality services to our people.

Backdrop

In order to address dumping of cheap steel imports from China, South Korea and Ukraine, the Government has raised customs duty and imposed anti-dumping duty, Minimum Import Price (MIP) on a number of items in February 2016, with a sunset clause of one year. These measures helped the domestic producers and exports recovered. The Government notified anti-dumping duties and Countervailing Duties on various steel products in February 2017. The Government has rolled out a New Steel Policy in May 2017.

Steel market outlook across the world has turned positive, with industrial production growing in most of the developed and BRIC countries. Although China's fixed asset investment and industrial production growth continue to decelerate, its trade with the rest of the world (RoW) is growing, benefiting from industrial growth in RoW. China's steel exports have been declining all through CY17 on supply-side discipline, which has tightened steel markets across RoW and boosted steel prices.

Steel mills' spreads are at highs, despite modest demand growth. This is driven by large-scale closure of unorganized producers in China, triggered by pollution control and raw material oversupply. Even large mills in China are focused on productivity, pollution, and deleveraging rather than volume growth. Plenty of iron ore and coking coal supply has allowed steel mills to buy high grade material to improve furnace productivity and reduce pollution. This has pushed out a lot of low grade iron ore supply from the market. Prices of low grade iron ore supply, which accounts for 15-20% of global seaborne supply, are at steep discount.

Indian steel market has reaped the benefit albeit partially due to sluggish domestic demand. Flat product prices moved up all through CY16-17, in line with the international trend. However, long product prices underperformed flat products by ~USD100/ton due to sluggish construction. Large mills with high share of flat products in the mix – JSW Steel, Tata Steel, Essar Steel, and Bhushan Steel – witnessed significant margin expansion, but steel producers with large share of long products and plates in the mix benefitted only marginally.

Indian long product prices have spiked in the last few months, bridging the gap with flat products. This is driven by improvement in domestic demand and tightening of iron ore supply in the local market after many mines in Odisha couldn't pay the penalties (imposed by the Supreme Court (SC) of India for access mining) by December 31, 2017.

Prices of iron ore fines have increased by INR700-900/ton in the Eastern sector, which is adding INR 1,500-1,600/ton to the cost of production for a primary producer and about INR 2,500/ton for sponge iron producers. Globally, steel scrap prices have also increased ~USD50/ton. This has opened the window for Indian mills to export billets. Average steel prices are now higher by INR 6,000-7,000/ton over the average prices in 3QFY18.

Government is investing massively on building infrastructure to support India's long term growth. India is far ahead than many emerging economies in terms of providing qualitative transportation related infrastructure. In view of the above, we believe the sector will do well in the coming period.

Last Budget Announcements

- For 2017-18, total capital and development expenditure of Railways has been pegged at Rs. 1,31,000 crore.
- Railway lines of 3,500 kms will be commissioned in 2017-18. During 2017-18, at least 25 stations are expected to be awarded for station redevelopment.
- 500 stations will be made differently abled friendly by providing lifts and escalators.
- A new Metro Rail Policy will be announced with focu0073 on innovative models of implementation and financing, as well as standardisation and indigenisation of hardware and software.
- Infrastructure statue to Affordable housing.
- National Housing Bank will refinance individual housing loans of about Rs. 20,000 crore in 2017-18.

Higher Infra spending along with push on affordable housing, given infra status, redevelopment of station, Airport operations will boost steel demand in coming years

Credit Ratios

Sector Credit Ratios (Upgrade vis-à-vis downgrades) during April'17 to December'17 as compared to previous year for the same period

Credit Ratio								
Sector	Total No. of Companies (o/s as on Dec 17)	9MFY17			9MFY18			Improvement/ detoriation in Credit Ratio (in bps)
		Upgrades	Downgrades	Ratio	Upgrades	Downgrades	Ratio	
Iron & Steel	1050	79	132	0.60	125	199	0.63	0.03
Source: CRISIL; SBI Research; numbers are for all rating agencies								

Credit ratio marginally improved by 3 bps during 9MFY18 as compared 9MFY17. However, with 125 upgrades and 199 downgrades, the same is still below one at 0.63.

Sectors Performance - Key Financials of Select Companies (Standalone)

Key Financials of Select Steel Companies for H1FY18 vis-à-vis H1FY17 (Rs in Crore)									
Name of the Company	**H1FY18**			**H1FY17**			**Growth H1FY18 on H1FY17**		
	Net Sales	**PBIDT**	**PAT**	**Net Sales**	**PBIDT**	**PAT**	**Net Sales**	**PBIDT**	**PAT**
Tata Steel Ltd	26839	6060	1801	19647	4187	825	37%	45%	118%
JSW Steel Ltd	28530	5222	1264	22861	5874	1754	25%	-11%	-28%
Steel Authority of India Ltd	25197	661	-1340	20464	284	-1267	23%	132%	6%
Jindal Steel & Power Ltd	6944	1384	-433	6048	1190	-684	15%	16%	-37%
Bhushan Steel Ltd	7838	789	-1954	5554	1336	-1636	41%	-41%	19%
Source: CLine; SBI Research									

All the above five companies have reported double digit growth in the top line, however PAT growth is negative except TATA Steel. SAIL, JSPL and Bhushan has reported loss in H1FY18.

Bhushan Steel, one of the 12 non-performing accounts referred by the Reserve Bank of India for National Company Law Tribunal (NCLT) proceedings, owes an amount of more than Rs. 44000 crore to its lenders. Domestic industry major Tata Steel, JSW Steel and Vedanta are in the race for Bhushan Steel which is, according to the information on Bhushan Steel Ltd website, the 3rd largest secondary steel producer in the country with an existing steel production capacity of 5.6 million tonne per annum.

Market Reaction

Market Movement in last One Month and on Budget Day							
Sector - Steel **Name of the Companies**	**01-Jan-18**	**31-Jan-18**	**01-Feb-18**	**"Movement Over 01-Jan-18"**		**Movement on Budget Day**	
Tata Steel Ltd	722.20	705.05	696.75	-25.45	-3.52%	-8.30	-1.18%
JSW Steel Ltd	265.80	289.95	302.65	36.85	13.86%	12.70	4.38%
Steel Authority of India Ltd	92.70	88.90	89.35	-3.35	-3.61%	0.45	0.51%
Jindal Steel & Power Ltd	206.20	266.45	265.95	59.75	28.98%	-0.50	-0.19%
Bhushan Steel Ltd	69.60	51.15	50.10	-19.50	-28.02%	-1.05	-2.05%
Source: NSE; closing price as on date							

Note: Movement over 1st January and on budget day indicates actual and percentage wise movement

Sector : Fertilisers — Overall Impact : Positive

Budget Proposals and Impact

- Lower corporate tax for MSME listed entities with turnover of less than Rs. 250 crore.
- Indirect fillip by announcing slew of measures to increase the disposable incomes of the farmers.
- Efforts to double farmers` income by year 2022.
- Aim to strengthen farmers` access to markets to boost Incomes.
- Increase in Minimum Support Price by 1.5x.
- Develop and upgrade existing 22000 rural haats into Gramin Agricultural Markets (GrAMs).
- GrAMs to provide farmers facility to directly sell to consumer and bulk purchasers.
- Government to strengthen physical infrastructure of the GrAMs using MGNREGA and other government schemes.
- GrAMs to be linked electronically to E-NAM (Electronic-National Agricultural Market) and exempted from regulations of APMC to enable price discovery through direct sale of produce to consumers.
- e-NAM Network - about 470 APMCs (Agricultural Produce Market Committee) out of 585 APMCs have been connected to e-NAM network and the balance would be connected by March 2018.
- Agri-Market Infrastructure Fund with a corpus of Rs. 2000 crore to be set up for developing and upgrading agricultural marketing infrastructure in the 22000 GrAMs and 585 APMCs
- National Health Protection Scheme for the 10 crore vulnerable and the poor families providing coverage upto Rs. 5 lakh crore per family for secondary and tertiary hospitalisation is one more step towards boosting consumerism. The budgetary allocation for cultivation of specialized medicinal and aromatic plants is another big positive and will help promote India's Ayurvedic heritage.
- Measures to provide livelihood, agriculture and allied activities and construction of rural infrastructure would entail a budget of Rs. 14.34 lakh crore, including Rs. 11.98 lakh crore extra-budgetary and non-budgetary resources. FMCG are in for good times in the year ahead.

All this augur well for the farming community.

Backdrop

The fertiliser industry reported improvement in operations in terms of EBIDTA and PAT growth in H1FY18 over H1FY17. This also appears to have led to decline in gross bank credit by -4.8% or so reducing from Rs. 25,500 Cr in October 2016 to Rs. 24,300 Cr in Oct 2017. H1FY18 financials of 26 listed companies shows bottom line growth of 34% while top line grew at 2%. We give below the key financials of the sector in the table:

Parameter	H1FY17	H1FY18	Growth
Net Sales	29982	30727	2.48%
EBIDTA	3131	3326	6.23%
Reported PAT	911	1218	33.70%

Source: CLine; 26 Cos in the sector; Rs in cr

GST Impact

The recent cut in GST from 18% to 12% on fertiliser grade phosphoric acid is likely to benefit the fertiliser sector marginally. The decline in GST will result in lower working capital requirement on account of lower input tax credit. While fertilisers are taxed at 5%, taxation of inputs at 18% led to an inverted duty structure and blockage of working capital due to large unused input tax credits. The reduction in the tax rate on phosphoric acid will result in reduction of the input tax credits and associated cash flow mismatch for the industry. Industry also expected to reduce the GST for ammonia alongwith Phosphoric acid. The inverted duty structure is likely to result in large unused input tax credit or delay in input tax credit leading to higher working capital requirement.

Subsidy Update

Government's ambitious target towards doubling the farmer income by 2022 and the direct benefit transfer on pilot basis in 16 districts across India with pan India rollout in FY2018 is aimed at promoting balanced nutritional practice and improved subsidy targeting. Few Key Developments include introduction of neem based urea to plug leakages in the system; targeted subsidy; promotion of contract farming and expansion of coverage of National Agricultural Market [e-NAM] from 250 markets to 585 APMCs, rise in farmers income due to rise in minimum support price of key crops, increase in area sown in the rabi season

While the fertiliser subsidy has been pegged at Rs. 70,000 crore as per BE 2017-18 (excludes petroleum subsidy estimated at Rs. 25,000 crore), the Centre's subsidy bill in FY2018-19 is unlikely to witness sharp increase considering the BE 2016-2017 and RE 2016-17 were also pegged at same level of Rs. 70000 crore. The actual outgo for fertiliser subsidy for 2015-16 stood at Rs. 72415 crore.

The total subsidy of three major heads viz., Food subsidy, Fertiliser subsidy and Petroleum subsidy as per Budget Estimate 2017-2018 stand at Rs. 2.40 lakh crore. In case the minimum support price rises, the food subsidy bill could well see about 10~15 percent increase from the current BE 2017-18 level of Rs. 1.45 lakh crore to Rs.1.67 lakh crore.

However, the direct benefit & cash transfer is likely to see minimal rise in sops for fuel (including LPG and Kerosene) and fertiliser. As far as DBT in fertiliser is concerned, the coverage of all districts of the country by March 2018 id likely to curb leakages and save outgo on the same. Also, efforts to promote alternate fuels is further likely to discourage kerosene resulting in savings from the same.

Concerns on rising crude prices, however remain. Any increase in global crude prices will stalemate the subsidy outgo calculations. Uncertain tax revenues in 2018-19 may also be a source of worry in terms of meeting the targets and subsidies.

Number of project announcements started picking up since FY14 from 13 to 34 projects in FY17. Amount wise also project announced in fertilizer sector increased from Rs. 10172 crore in FY14 to Rs. 23614 crore in FY17 which shows the renewed interest in the sector.

Going ahead, fertilizer production in the country is expected to reach close to 40 million tons in FY 2020, from the current level of 37.2 million tons, increasing by 1.5% CAGR during FY2010-17. While manufacturing infrastructure for Urea is well developed, there is a huge dependence on imports for phosphate and potassic fertilizers.

Credit Ratios

Sector Credit Ratios (Upgrade vis-à-vis downgrades) during April'17 to December'17 as compared to previous year for the same period

Credit Ratio								
Sector	Total No. of Companies (o/s as on Dec 17)	9MFY17			9MFY18			Improvement/ detoriation in Credit Ratio (in bps)
		Upgrades	Downgrades	Ratio	Upgrades	Downgrades	Ratio	
Fertilisers	78	6	7	0.86	11	11	1	0.14
Source: CRISIL; SBI Research; numbers are for all rating agencies								

With upgrades and downgrades of 11 each during 9MFY18, credit ratio stand at 1 as compared to 0.86 during 9MFY17. Credit ratios show an improvement of 14 bps during the period.

Sectors Performance - Key Financials of Select Companies (Standalone)

Key Financials of Select Steel Companies for H1FY18 vis-à-vis H1FY17 (Rs in Crore)									
Name of the Company	H1FY18			H1FY17			Growth H1FY18 on H1FY17		
	Net Sales	PBIDT	PAT	Net Sales	PBIDT	PAT	Net Sales	PBIDT	PAT
Coromandel International Ltd	5878	771	420	5529	503	221	6%	53%	90%
Chambal Fertilisers & Chemicals Ltd	4063	538	282	3960	552	268	3%	-3%	5%
Rashtriya Chemicals & Fertilizers Ltd	3363	154	31	3322	226	63	1%	-32%	-50%
National Fertilizer Ltd	4004	268	93	3267	246	46	23%	9%	102%
Gujarat State Fertilizers & Chemicals Ltd	2678	234	120	2622	323	171	2%	-27%	-30%
Source: CLine; SBI Research									

Market Reaction

Market Movement in last One Month and on Budget Day							
Sector - Fertilisers Name of the Companies	01-Jan-18	31-Jan-18	01-Feb-18	"Movement Over 01-Jan-18"		Movement on Budget Day	
Coromandel International Ltd	556.90	554.60	549.00	-7.90	-1.42%	-5.60	-1.01%
Chambal Fertilizers & Chemicals Ltd	157.05	160.35	154.25	-2.80	-1.78%	-6.10	-3.80%
Rashtriya Chemicals & Fertilizers Ltd	96.95	97.75	93.15	-3.80	-3.92%	-4.60	-4.71%
National Fertilizers Ltd	73.35	72.95	69.80	-3.55	-4.84%	-3.15	-4.32%
Gujarat State Fertilizers & Chemicals Ltd	152.60	144.70	140.10	-12.50	-8.19%	-4.60	-3.18%
Source: NSE; closing price as on date							

Note: Movement over 1st January and on budget day indicates actual and percentage wise movement

Sector : Road — Overall Impact : Positive

Budget Proposals and Impact

- Estimated infrastructure need in excess of Rs. 50 lakh crore to connect and integrate the nation with a network of roads, airports, railways, ports and inland waterways.
- 99 Cities selected with an outlay of Rs. 2.04 lakh crore, have started implementing various projects like Smart Command and Control Centre, Smart Roads, Intelligent Transport Systems etc.
- To complete National Highways exceeding 9000 kilometers length during 2017-18.
- NHAI to organize road asset in SPV and to use innovative monetizing structures like Toll, Operate and Transfer (TOT) and Infrastructure Investment Funds (InvITs) to raise equity from market.

With ambitious Bharatmala Pariyojana for providing seamless connectivity of interior and backward areas and borders of the country to develop about 35000 kms in Phase-I at an estimated cost of Rs. 5,35,000 crore, road sector to travel a long way in the coming year.Raising equity from market through use of innovative monetizing structures like Toll, Operate and Transfer (TOT) and Infrastructure Investment Funds (InvITs) will be an enabler for the sector.

Backdrop

Government is investing massively on building infrastructure to support India's long term growth. India is far ahead than many emerging economies in terms of providing qualitative transportation related infrastructure.

The primary agenda for the Government has been building new National Highways (NHs) and also converting State Highways (SHs) into NHs. As in September, 2017, total length of National Highways (NHs) /Express Ways in India was 1,15,530 km which accounted for 2.06 per cent of the total road length. On the other hand, the length of State Highways was 1,76,166 km as on 2015-16.

In many under developed States with lower Per capita GSDP like Bihar, Odisha, Chhatisgarh, Jharkhand and Jammu & Kashmir, West Bengal, Madhya Pradesh, the density of Other Public Work Department (OPWD) Road/ District Road is very low. There is a need for developing OPWD roads including District Roads, so as to provide better access, thereby enhancing economic activities.

- Government has recently approved Rs. 7 trillion road construction plan, including Bharatmala Pariyojana with a Rs. 5.35 trillion outlay for 34,800 km with NHAI likely to spend Rs. 1.57 trillion for 48,877 km of roads.
- At a time when private investment remains muted, highways has emerged as one of the key sectors for the government to step up public investment to ramp up economic activity and create jobs.
- Boosts the demand for other sectors such as cement and steel.
- Speedy construction activity to 22.5 km a day, compared to 12 km a day in 2014-15. Till December, the daily highway construction stood at 23.6 km and the ministry is confident of pushing it to 25 km a day by March. Though, it is still far off the target of building 40 km per day, set by highways minister.

Increase Highway Spending			
Year	Spending (Rs. in Cr)	Construction (km)	Award (km)
2014-15	51,703	4410	7972
2015-16	98,761	6061	10098
2016-17	98,117	8231	15948
2017-18	130000 *	5680 #	4163 #
2018-19	150000 *	NA	NA

Source: MoRTH; # till Dec 2017; * approximate

Some of the key announcement in last budget

- In the road sector, Budget allocation for highways increased from Rs. 57976 crore in BE 2016-17 to Rs 64900 crore in 2017-18.
- 2,000 kms of coastal connectivity roads have been identified for construction and development.
- Total length of roads, including those under PMGSY, built from 2014-15 till the current year is about 1,40,000 kms which is significantly higher than previous three years.

Credit Ratios

Sector Credit Ratios (Upgrade vis-à-vis downgrades) during April'17 to December'17 as compared to previous year for the same period

Credit Ratio								
Sector	Total No. of Companies (o/s as on Dec 17)	9MFY17			9MFY18			Improvement/ detoriation in Credit Ratio (in bps)
		Upgrades	Downgrades	Ratio	Upgrades	Downgrades	Ratio	
Road	723	73	46	1.59	86	86	1.00	-0.59
Source: CRISIL; SBI Research; numbers are for all rating agencies								

With upgrades and downgrades of 89 each during 9MFY18, credit ratio stand at 1 as compared to 1.59 during 9MFY17.

Sectors Performance - Key Financials of Select Companies (Standalone)

Key Financials of Select Steel Companies for H1FY18 vis-à-vis H1FY17 (Rs in Crore)									
Name of the Company	H1FY18			H1FY17			Growth H1FY18 on H1FY17		
	Net Sales	PBIDT	PAT	Net Sales	PBIDT	PAT	Net Sales	PBIDT	PAT
Larsen & Toubro Ltd	29797	3534	1720	26606	5035	3265	12%	-30%	-47%
KNR Constructions Ltd	874	182	127	677	119	74	29%	53%	71%
Gayatri Projects Ltd	1075	180	69	782	124	28	37%	46%	146%
IRB Infrastructure Developers Ltd	1362	380	241	1604	196	34	-15%	94%	600%
Ashoka Buildcon Ltd	1102	168	95	911	151	76	21%	11%	24%
Source: CLine; SBI Research									

Except IRB, all the companies from the above have reported double digit growth in top line during H1FY18 as compared to H1FY17. Bottom line also improved in all of the above companies except L&T.

Market Reaction

Market Movement in last One Month and on Budget Day							
Sector - Roads Name of the Companies	01-Jan-18	31-Jan-18	01-Feb-18	"Movement Over 01-Jan-18"		Movement on Budget Day	
Larsen & Toubro Ltd	1260.7	1416.5	1455.6	194.9	15.46%	39.1	2.76%
KNR Constructions Ltd	319.4	307.4	305.2	-14.2	-4.43%	-2.2	-0.72%
Gayatri Projects Ltd	227.2	209.2	213.4	-13.8	-6.07%	4.2	2.01%
IRB Infrastructure Developers Ltd	234.2	241.2	243.2	9.0	3.84%	2.0	0.81%
Ashoka Buildcon Ltd	246.0	227.0	230.0	-16.0	-6.49%	3.0	1.32%
Source: NSE; closing price as on date							

Note: Movement over 1st January and on budget day indicates actual and percentage wise movement

Sector : Port — Overall Impact : Positive

Budget Proposals and Impact

- Estimated infrastructure need in excess of Rs. 50 lakh crore to connect and integrate the nation with a network of roads, airports, railways, ports and inland waterways.
- Massive investments estimated to be in excess of Rs. 50 lakh crore in infrastructure to connect and integrate the nation with a network of roads, airports, railways, ports and inland waterways.
- Allocation to Ministry of Shipping increased to Rs. 4292 crore from Rs. 3290 crore.

Under the Sagarmala project, 415 projects have been identified with investment of Rs. 8 lakh crore, and projects worth 1.37 lakh crore rupees have been taken up for implementation, which translate into significant opportunity for developers, contractors and equipment and technology providers. There will also be opportunities in the dredging and inland waterways segments.

Recently UAE-based marine and inland terminals operator DP World joined hands with the National Investment and Infrastructure Fund (NIIF) to create a platform for investing up to $3 billion in ports and logistics which further provide impetus to the sector.

Backdrop

India's 7517 km coastline is dotted with 12 major and about 187 non-major ports. In terms of capacity, major ports saw the highest capacity addition in 2016-17 at 101 mtpa (previous year 94 mtpa). As of March 2017, capacity at Indian ports stood at 1066 mt, at a capacity utilisation of 61%.

Capacity of major ports increased by around 400 MT with a CAGR of 7.4% in last 5 years from 2012 to 2017. We expect capacity addition at all major port to grow by 5-6% CAGR in the next five years between fiscals 2017 and 2022, adding 275-325 MT of capacity.

The reform process undertaken in the past couple of years is further expected to increase the overall growth of the sector. To cater to the demand in the next 10 years, capacity should be increased both by building green-field ports and by increasing capacity of existing terminals through improved mechanization and resultant efficiency and building new terminals at existing ports.

Enactment of National Waterways Act, 2016 - declared 106 waterways across 24 states as NWs in addition to the existing 5 NWs and revision in MCA (Model Concession Agreement) has brought a lot of changes with improvement and greater flexibility.

Initiated an aggressive port infrastructure programme named as 'Sagarmala' with an objective of rapid up-gradation of port connectivity and modernization to ensure efficient and cost effective evacuation of cargos. Sagarmala is a comprehensive and holistic programme and has brought in optimism in the sector.

Credit Ratios

Sector Credit Ratios (Upgrade vis-à-vis downgrades) during April'17 to December'17 as compared to previous year for the same period.

Credit Ratio								
Sector	Total No. of Companies (o/s as on Dec 17)	9MFY17			9MFY18			Improvement/ detoriation in Credit Ratio (in bps)
		Upgrades	Downgrades	Ratio	Upgrades	Downgrades	Ratio	
Port	41	4	9	0.44	2	2	1	0.56

Source: CRISIL; SBI Research; numbers are for all rating agencies

With upgrades and downgrades of 2 each during 9MFY18, credit ratio stand at 1 as compared to 0.44 during 9MFY17. Credit ratios show an improvement of 56 bps during the period.

Sectors Performance - Key Financials of Select Companies (Standalone)

Key Financials of Select Ports Companies for H1FY18 vis-à-vis H1FY17 (Rs in Crore)									
Name of the Company	H1FY18			H1FY17			Growth H1FY18 on H1FY17		
	Net Sales	PBIDT	PAT	Net Sales	PBIDT	PAT	Net Sales	PBIDT	PAT
Adani Ports & Special Economic Zone Ltd	3172.19	2862.18	1181.52	2346.63	2340.94	1519.51	35%	22%	-22%
Gujarat Pipavav Port Ltd	320.73	207.82	99.88	339.37	217.37	119.17	-5%	-4%	-16%
Source: CLine; SBI Research;									

Market Reaction

Market Movement in last One Month and on Budget Day							
Sector - Ports Name of the Companies	01-Jan-18	31-Jan-18	01-Feb-18	Movement Over 01-Jan-18		Movement on Budget Day	
Adani Ports & Special Economic Zone Ltd	399.7	428.9	428.8	29.1	7.28%	-0.1	-0.02%
Gujarat Pipavav Port Ltd	136.6	144.1	142.3	5.7	4.17%	-1.8	-1.28%
Source: NSE; closing price as on date							

Note: Movement over 1st January and on budget day indicates actual and percentage wise movement

Sector : Auto Ancillary — Overall Impact : Positive

Budget Proposals and Impact

- Increase in Customs duty to provide boost to 'Make In India' and also offer adequate protection to domestic industry.

Change in Custome Duty		
Description	**From**	**To**
Specified parts/accessories of motor vehicles, motor cars, motor cycles	7.5%/ 10%	15%
Truck and Bus radial tyres	10%	15%
Source: Budget Documents		

Backdrop

Globally, India is the largest tractor manufacturer, second largest two-wheeler and bus manufacturer, fifth largest heavy trucks manufacturer, sixth largest passenger car manufacturer and seventh largest commercial vehicle manufacturer. Thus, it provides a huge consumer base for auto component manufacturers who cater to the OEM sector.

Auto and auto-allied sectors including auto components are highly cyclical in nature. The auto component industry's performance is significantly influenced by fluctuation in automobile industry which in turn is dependent on various macro-economic factors.

Recovering production growth in automobile sector is likely to push the overall demand in the auto component industry. The industry is characterized by intensive use of raw materials, the auto component industry is highly prone to risk associated with raw material supply, input price, and currency fluctuation. In the current fiscal, with revival of demand growth, input prices of all major commodities including steel, aluminum and rubber have exhibited an improvement which may further put pressure on the industry margin.

Depreciation of the rupee, bolstered the revenue earnings of this sector from exports. Intense global competition and presence of leading automobile manufacturers in India (who have an eye for quality products) has led auto component manufacturers to set high quality facilities with state of the art manufacturing processes. This has enabled companies to produce and export quality products globally as well as domestically. However, at the same time imports have become costlier for the domestic industry on the back of a falling currency

The auto component sector is highly fragmented, comprising of 750 players in the organized sector and close to 6,000 small players in the unorganized sector. The organized sector caters primarily, to OEMs and export market, accounting for about 85% of the total industry turnover. Manufacturing units in the unorganized sector dominate the replacement market

Automotive component industry that has to transport parts to various auto hubs have been positively affected by GST. Waiting periods at state and city borders have been eliminated to a large extent. For example, trucks that took about 7-8 days to reach hubs like Chennai from the NCR or Manesar region now do the same journey in only about 4 days due to no bottlenecks at octroi points.

Last Budget Announcements

- BCD reduced from 7.5% to 5% on Clay 2 Powder (Alumax) for use in ceramic substrate for catalytic convertors, subject to actual user condition.

Credit Ratios

Sector Credit Ratios (Upgrade vis-à-vis downgrades) during April'17 to December'17 as compared to previous year for the same period.

Credit Ratio								
Sector	Total No. of Companies (o/s as on Dec 17)	9MFY17			9MFY18			Improvement/ detoriation in Credit Ratio (in bps)
		Upgrades	Downgrades	Ratio	Upgrades	Downgrades	Ratio	
Auto Anciliary	625	112	52	2.15	88	80	1.10	-1.05
Source: CRISIL; SBI Research; numbers are for all rating agencies								

With upgrades of 88 and downgrades of 80 during 9MFY18, credit ratios stands at 1.10. However, the same is much below the credit ratios for the same period previous year.

Sectors Performance - Key Financials of Select Companies (Standalone)

Key Financials of Select Auto Ancillary Companies for H1FY18 vis-à-vis H1FY17 (Rs in Crore)									
Name of the Company	H1FY18			H1FY17			Growth H1FY18 on H1FY17		
	Net Sales	PBIDT	PAT	Net Sales	PBIDT	PAT	Net Sales	PBIDT	PAT
Motherson Sumi Systems Ltd	3481	747	463	2952	608	342	18%	23%	35%
Bosch Ltd	5460	1206	656	5175	1595	1082	6%	-24%	-39%
Exide Industries Ltd	4474	605	325	3936	642	378	14%	-6%	-14%
Endurance Technologies Ltd	2252	295	141	2027	259	122	11%	14%	16%
Amara Raja Batteries Ltd	2925	457	227	2641	478	267	11%	-4%	-15%
Source: CLine; SBI Research									

Though the Auto Ancillary have shown better top line growth numbers in H1FY18 as compared to H1FY17, the same could not be seen in the bottom line for all the above companies. Motherson Sumi and Endurance Technology have reported growth in all key parameters.

Market Reaction

Market Movement in last One Month and on Budget Day							
Sector - Auto Ancillary Name of the Companies	01-Jan-18	31-Jan-18	01-Feb-18	Movement Over 01-Jan-18		Movement on Budget Day	
Motherson Sumi Systems Ltd	379.1	365.8	362.8	-16.4	-4.31%	-3.1	-0.83%
Bosch Ltd	19791.9	19400.3	19517.9	-274.1	-1.38%	117.6	0.61%
Exide Industries Ltd	219.8	223.4	219.8	0.0	0.00%	-3.6	-1.61%
Endurance Technologies Ltd	1362.5	1194.9	1200.0	-162.5	-11.93%	5.2	0.43%
Amara Raja Batteries Ltd	834.5	810.1	808.5	-26.0	-3.11%	-1.6	-0.20%
NIFTY AUTO INDEX	11890.5	11611.9	11693.6	-196.9	-1.66%	81.7	0.70%
Source: NSE; closing price as on date							

Note: Movement over 1st January and on budget day indicates actual and percentage wise movement

Sector : Automobile — Overall Impact : Positive

Budget Proposals and Impact

- Increase in Customs duty to provide boost to 'Make In India' and also offer adequate protection to domestic industry.

Custom Duty	From	To
CKD imports of motor vehicle, motor cars, motor cycles	10%	15%
CBU imports of motor vehicles	20%	25%

Backdrop

Robust growth has been seen in FY18 (upto Dec) as compared to the same period in previous year across segment in Automobile space. Heavy commercial vehicle sales recorded highest growth of 16.22% during the period. Table showing growth in each category is as under: -

Automobile - unit sale in FY18 vis-à-vis FY17			
Category	YTD FY18	YTD FY17	YoY %
Two Wheeler	11660521	10671624	9.27%
Four Wheeler	2533704	2294697	10.42%
Heavy Commercial Vehicle	460482	396211	16.22%
Source: Company data; SBI Research; YTD= upto Dec			

As can be seen from the GST table mentioned below, the rate for automobiles is 28% (minimum) and has largely been retained in line with excise structure that was prevalent before July 2017.

Three Projects in pipeline

PSA, France - A new unit is being planned by Paris based PSA. The company announced that it will manufacture vehicles near Chennai with 100000 units per year at a cost of Rs. 700 crore. The unit would also manufacture auto components. PSA has signed two agreements with Indian conglomerate CK Birla for both vehicle assembly and powertrains.

KIA, Korea - The second-largest Korean carmaker, Kia Motors, a minority-owned subsidiary of Korean auto major Hyundai Motor Company is expected to start production at the factory at Penukonda, a town 70 km from Anantapur. The factory would be the first automobile manufacturing facility in Andhra Pradesh and be roughly 350 km away from Chennai's automobile hub, where most automakers including Hyundai, Renault Nissan, Mercedes Benz, BMW, Ford and Ashok Leyland produce their vehicles. The capacity is estimated at 300000 units per year to be set up at a cost of Rs. 7000 crore.

With Kia a Korean consortium of auto component manufacturers are set to make approximately USD 1 billion investment in a supply chain for the integrated plant being set up by Kia Motors.

Maruti Suzuki is currently implementing Rs. 8500 crore project for 250000 units per year in Mehsana, Gujarat. Also on anvil, is another project for 250000 units per year costing Rs. 6000 crore. Further, reports suggest the company also has plans for launching Electric Vehicles in year 2020.

Recently Hyundai's announced plan for investing about $22 billion over five years. Besides electric and self-driving cars, the planned investment will also be in fields such as artificial intelligence, batteries and hydrogen energy, as well as start-ups.

Though Government is promoting the electric cars, clear long term policy is required to gain the confidence of the car maker before they invest heavily on it. Further related infrastructure like charging stations etc. also need to be developed beforehand to push the venture.

However, Industry expectation is to ensure zero GST on EVs and no custom duty either. The government is imposing high taxes on both imported EVs and on their batteries. At present, EVs are not very practical because the storage capacity of even the best batteries remains low.

Some of the car makers plans to build electric cars but are waiting for clear roadmap from the Government on how it aimed to achieve its target to electrify all new vehicles by 2030.

Current GST Tariff on Automobiles is as under: -

Automobiles: Present GST and Cess Tariffs		
Description	GST	CESS
	2017-18	2017-18
-Specified small cars (Length not exceeding 4000 mm)	28%	1%
Length exceeding 4000 mm but engine capacity less than 1500cc	28%	17%
Length exceeding 4000 mm but engine capacity greater than 1500cc	28%	20%
Utility vehicles (less than 1500 cc)	28%	20%
SUVs (including utility vehicles exceeding 1500 cc and length exceeding 4000 mm, ground clearance of 170 mm and more)	28%	22%
Luxury Cars	28%	20%
Two-wheelers	28%	0%
Trucks (LCVs and MHCVs)	28%	0%
Buses (LCVs and MHCVs)	28%	0%
Tractors	12%	0%

Cars and Utility Vehicles Forecast

Cars and Utility Vehicles						
Parameter Name	2013-14 A	2014-15 A	2015-16 A	2016-17 A	2017-18 F	2018-19 F
Passenger Vehicles Sales	2504	2601	2789	3047	3335	3621
Passenger Cars	1787	1877	2025	2103	2227	2415
Small Car	1575	1640	1792	1892	2016	2195
Large Car	212	238	233	211	211	220
Utlity Vehicles & Vans	717	724	764	944	1108	1206
Utility Vehicles	526	552	587	762	916	1003
Vans	191	171	178	182	193	203
Passenger Vehicles Exports	595	621	653	759	780	850
Total Installed Capacity	4569	5002	5172	5232	5408	
Realisation Per Unit (Rs.)	421037	444801	464398	489159	506935	
Op. Margin for Passenger Car Manufacturers (in %)	10.4	11.6	13.3	12.8	13.1	
Investments in Cars and Uvs Sector(Rs. In Bn)	40	10	48	49	85	
Source: CRISI L; SBI Research, unit in thousand; ; A= Actual; F=Forecast						

Credit Ratios

Sector Credit Ratios (Upgrade vis-à-vis downgrades) during April'17 to December'17 as compared to previous year for the same period

Credit Ratio								
Sector	Total No. of Companies (o/s as on Dec 17)	9MFY17			9MFY18			Improvement/ detoriation in Credit Ratio (in bps)
		Upgrades	Downgrades	Ratio	Upgrades	Downgrades	Ratio	
Automobile	46	6	3	2	4	3	1.33	-0.67
Source: CRISIL; SBI Research; numbers are for all rating agencies								

Credit ratios for the sector deteriorated by 67 bps to 11.33 in the nine month ended Dec 2017 as compared to the same period previous year. However top players like Tata, Maruti, Mahindra, Hero etc. have reported growth in both top line and bottom line in H1FY18 as compared to H1FY17. And for Q3FY18 also overall industry volumes were robust and encouraging compared to corresponding quarter last year.

Sectors Performance - Key Financials of Select Companies (Standalone)

Key Financials of Select Automobile Companies for H1FY18 vis-à-vis H1FY17 (Rs in Crore)									
Name of the Company	H1FY18			H1FY17			Growth H1FY18 on H1FY17		
	Net Sales	PBIDT	PAT	Net Sales	PBIDT	PAT	Net Sales	PBIDT	PAT
Tata Motors Ltd	22982	1505	-762	20572	1582	-605	12%	-5%	26%
Maruti Suzuki India Ltd	38571	7214	4041	32281	6558	3892	19%	10%	4%
Mahindra & Mahindra Ltd	23796	3743	2081	21818	3388	1937	9%	10%	7%
Hero Motocorp Ltd	16334	3001	1925	15195	2872	1887	7%	4%	2%
Bajaj Auto Ltd	11803	2958	2036	11593	3082	2101	2%	-4%	-3%
Source: CLine; SBI Research									

Tata Motors and Maruti have reported 12% and 19% growth in net sales in H1FY18 respectively as compared to H1FY17. However, Tata Motors have reported negative PAT in H1FY18 whereas Maruti have reported a growth of 4%.

Market Reaction

Market Movement in last One Month and on Budget Day							
Sector - Automobile Name of the Companies	01-Jan-18	31-Jan-18	01-Feb-18	Movement Over 01-Jan-18		Movement on Budget Day	
Tata Motors Ltd	424.5	399.5	393.7	-30.8	-7.26%	-5.9	-1.46%
Maruti Suzuki India Ltd	9651.9	9509.7	9401.9	-250.0	-2.59%	-107.9	-1.13%
Mahindra & Mahindra Ltd	744.7	763.1	798.8	54.1	7.27%	35.7	4.68%
Hero Motocorp Ltd	3749.1	3691.5	3733.0	-16.2	-0.43%	41.5	1.12%
Bajaj Auto Ltd	3289.3	3337.2	3413.0	123.7	3.76%	75.8	2.27%
NIFTY AUTO INDEX	11890.5	11611.9	11693.6	-196.9	-1.66%	81.7	0.70%
Source: NSE; closing price as on date							

Note: Movement over 1st January and on budget day indicates actual and percentage wise movement

Sector : Construction — Overall Impact : Positive

Budget Proposals and Impact

- Estimated infrastructure need in excess of Rs. 50 lakh crore to connect and integrate the nation with a network of roads, airports, railways, ports and inland waterways.
- 10 Iconic Tourism destinations.
- Allocation to Rail 1.48 lakh crore for 2018-1. A large part of the Capex is devoted to capacity creation. 18,000 kilometers of doubling, third and fourth line works and 5000 kilometers of gauge conversion.
- Prime Minister personally reviews the targets and achievements in infrastructure sector on a regular basis using online monitoring system of PRAGATI.
- 99 Cities have been selected with an outlay of Rs. 2.04 lakh crore.
- Projects worth Rs. 2350 crore have been completed and works of Rs. 20,852 crore are under progress.
- AMRUT programme focuses on providing water supply to all households in 500 cities. State level plans of Rs. 77,640 crore for 500 cities have been approved. Water supply contracts for 494 projects worth Rs. 19,428 crore and sewerage work contract for 272 projects costing Rs. 12,429 crore has been awarded.
- Regional connectivity scheme of UDAN to connect 56 unserved airports and 31 unserved helipads across the country.
- Rs. 14.34 lakh crore to ve spend in 2018-19 for creation of livelihood and infrastructure in rural areas. .

Opportunity is unlimited for the construction sector with Government seems high on spending towards entire Infrastructure ecosystem i.e. Road, Railways, Port, Air. Host of opportunity in area such as Railway, Smart City, Road, Udan etc. along with new announcement of construction of 10 Iconic Tourism destinations. Leveraging India Infrastructure Finance Corporation Ltd (IIFCL) to help finance major infrastructure projects, including investments in educational and health infrastructure will definitely de-risk bank balance sheet from high concentration on infra sector.

Backdrop

Mid-size and small construction entities appear to be well poised for growth, going by the order book and flexibility and maneuverability of strong project execution capabilities. Some of the mid-sized entities have been procuring new orders from irrigation as well as from roads through EPC or through Hybrid Annuity Model (HAM). Also, these entities have limited investment / financial support to Build Operate & Transfer (BOT) projects and HAM projects. Hence, to some extent this insulates the parent from adversity. The credit rating of the company in year 2008 was BBB+ and today stands at A+.

Some of the mid-sized entities have established relationship with leading players in the infrastructure segment helping in joint bidding of projects. These mid-size entities also have established relationships with state government departments, National Highways Authority of India (NHAI) and Ministry of Road Transport and Highways (MoRTH) by virtue of its track record of executing projects on time. These small success stories remain the sweet spot for these entities to keep growing on a lower base. The government also weigh such factors in evaluating projects.

Owning a fleet of construction equipment, joint bidding, foraying into complex projects, demonstrated track record and established relationships are factors that mid-sized entities may offer vis-à-vis large entities who may not be interested in small ticket size projects. Also, some of the large entities may have undergone debt restructuring.

Government spending has played a key role in the development of construction sector. Today, the development of road segment is playing a primary role in development of the construction sector. The real estate sector, these days, has taken a back seat with most of them stuck in regulatory hurdles or lender compliances. In the union budget 2017-18, the government allotted Rs. 64000 crore to NHAI for roads and highways and Rs. 27000 crore for Pradhan Mantri Gram Sadak Yojana. Apart from the above, Rs. 3 lakh crore has been earmarked for 35000 kms as per the table mentioned below.

Bharatmala Pariyojana to be implemented with an outlay of Rs. 535000 crore with proposed road construction of 34800 km.

The Road Ahead - under BMP …..	
Categories of Roads	**Kms**
Economic Corridors	9000
Inter Corridor and Feeder Route	6000
National Corridors Efficiency Improvement	5000
Border Roads and International Connectivity	2000
Coastal Roads and Port Connectivity	2000
Green Field Expressways	800
Balance NHDP Works	10,000
Total	34,800

Government is consistently increasing Public Expenditure on Infrastructure in order to provide renewed impetus to economic growth. Government total expenditure this year has crossed Rs 11.47 lakhs crore (upto Sept '17), out of the budgeted expenditure Rs. 21.46 lakhs crore. (an increase of Rs. 1.2 lakhs crore. over last year).

Special thrust of this drive is on key development sectors including Rural Roads, Housing, Railways, Power, Highways and Digital Infrastructure. The Capex target of Government of India for 2017-18 is Rs. 3.09 lakhs crore, which is 31.28% higher than last year, out of which Rs. 1.46 lakhs crore has been spent on capital works till September 2017. In addition, Government of India had fixed a Capital expenditure target for CPSEs for 2017-18 at Rs. 3.85 lakhs crore, out which capex spending of Rs. 1.37 lakhs crore has been achieved by CPSEs till Sept'17.

In Railways a target of Rs. 1,31,000 crore has been made for Capital Expenditure of which an expenditure of Rs. 50,762 crore has been achieved till Sep'17. The main thrust of Railway is on upgrading the infrastructure to improve safety, laying of new lines and providing passenger amenities.

In view of all of the above, we believe constructions sector should do well in coming period.

Last Budget Announcements

- Provision of Rs. 2,41,387 crore has been made in 2017-18 for transportation sector as a whole, including rail, roads, shipping.
- For 2017-18, total capital and development expenditure of Railways has been pegged at Rs. 1,31,000 crore.
- Railway lines of 3,500 kms will be commissioned in 2017-18. During 2017-18, at least 25 stations are expected to be awarded for station redevelopment.
- 500 stations will be made differently abled friendly by providing lifts and escalators.
- In the road sector, Budget allocation for highways increased from Rs. 57976 crore in BE 2016-17 to Rs. 64900 crore in 2017-18.
- 2,000 kms of coastal connectivity roads have been identified for construction and development.

Credit Ratios

Sector Credit Ratios (Upgrade vis-à-vis downgrades) during April'17 to December'17 as compared to previous year for the same period.

Credit Ratio								
Sector	Total No. of Companies (o/s as on Dec 17)	9MFY17			9MFY18			Improvement/ detoriation in Credit Ratio (in bps)
		Upgrades	Downgrades	Ratio	Upgrades	Downgrades	Ratio	
Constructions	2170	221	129	1.71	239	306	0.78	-0.93
Source: CRISIL; SBI Research; numbers are for all rating agencies								

With upgrades of 239 and downgrades of 306 during 9MFY18, credit ratio deteriorated by 93 bps to 0.78 from 1.71 for the 9MFY17.

Sectors Performance - Key Financials of Select Companies (Standalone)

Key Financials of Select Construction Companies for H1FY18 vis-à-vis H1FY17 (Rs in Crore)									
Name of the Company	H1FY18			H1FY17			Growth H1FY18 on H1FY17		
	Net Sales	PBIDT	PAT	Net Sales	PBIDT	PAT	Net Sales	PBIDT	PAT
Larsen & Toubro Ltd	29797	3534	1720	26606	5035	3265	12%	-30%	-47%
Sadbhav Engineering Ltd	1637	190	89	1423	158	67	15%	20%	32%
KNR Constructions Ltd	874	182	127	677	119	74	29%	53%	71%
B.L. Kashyap & Sons Ltd	454	62	13	454	52	6	0%	19%	108%
JMC Projects (India) Ltd	1326	142	47	1090	108	23	22%	31%	100%
Source: CLine; SBI Research									

Most of the construction companies from above, reported a double digit growth in top line except B.L Kashyap and bottom line except L&T.

Market Movement in last One Month and on Budget Day							
Sector - Construction Name of the Companies	01-Jan-18	31-Jan-18	01-Feb-18	Movement Over 01-Jan-18		Movement on Budget Day	
Larsen & Toubro Ltd	1260.7	1416.5	1455.6	194.9	15.46%	39.1	2.76%
Sadbhav Engineering Ltd	429.5	407.5	409.9	-19.6	-4.56%	2.4	0.59%
KNR Constructions Ltd	319.4	307.4	305.2	-14.2	-4.43%	-2.2	-0.72%
B.L. Kashyap & Sons Ltd	64.3	55.5	54.6	-9.7	-15.09%	-0.9	-1.53%
JMC Projects (India) Ltd	621.1	550.9	536.6	-84.5	-13.61%	-14.4	-2.60%
NIFTY INFRA INDEX	3636.7	3619.5	3648.1	11.4	0.31%	28.6	0.79%
Source: NSE; closing price as on date							

Notes

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