OVERVIEW

The strong verdict in the Parliamentary Elections created high expectations from the new Government’s maiden budget, to set the tone for a revival in economic growth, improve governance and focus on fiscal consolidation. Notwithstanding the short lead time of six weeks and an absence of big-bang announcements, the Government has presented an investor-friendly Budget, which is directionally positive for the infrastructure and manufacturing sectors as well as the overall investment climate.

The 2014-15 Budget has provided a thrust on reviving investments, with a significant increase in outlay on the road sector, proposal for setting up greenfield ports and airports, incentives for low cost housing, intention to revive the Special Economic Zones etc. In particular, the augmented allocation to NHAI would benefit entities in the construction sector, as it would imply more cash contracts involving lower upfront investments.

In light of the huge financing requirements to bridge India’s sizable infrastructure deficits, the permission to Banks to raise long term funds for lending to infrastructure projects with minimum regulatory pre-emption such as CRR, SLR and priority sector lending is a positive step. Moreover, measures proposed in the Budget such as tax incentives for real estate investment trusts (REITS) and infrastructure investment trusts would help ease the constraints faced in raising long term financing for infrastructure projects. With growing urbanisation and aspiration of Indians for better civic services, the focus on creation of new smart cities, improving services in rural as well as urban habitations is well-placed. However, the experience with ramping up services through the PPP mode remains limited, and has had a somewhat mixed track-record so far. Furthermore, the existing Pooled Finance Development Scheme for aiding municipal bodies in raising funds to augment urban infrastructure has met with limited success in recent years. Additional details are awaited to determine the efficacy of increasing the corpus 10-fold to Rs. 500 billion by 2019.

While there was no change in the stance regarding the sovereign right to retrospective taxation, the Government’s assurance of a stable and predictable taxation regime would help to create a conducive environment to attract investment in various sectors. Additionally, measures to enable a wider variety of advance rulings for taxation would help limit potential conflicts. Moreover, the extension of the 10 year tax holiday to entities that commence generation, distribution and transmission of power by 31.03.2017 would boost investment in this sector. Nevertheless, various issues related to the transport and availability of feedstock would need to be addressed to enable a ramp up in power generation. The investment allowance at the rate of 15% to a manufacturing companies investing in excess of Rs. 0.25 billion in any year in new plant and machinery upto 2016-17 is expected to provide a thrust to manufacturing. Furthermore, the raising of the investment limit under Section 80C of the Income Tax Act would boost the economy’s financial saving rate, while the higher deduction limit on account of interest on loan in respect of self-occupied houses would benefit the housing and construction sectors.

The new Government’s focus on fiscal prudence and announcement of the roadmap for consolidation with the commitment to reduce the fiscal deficit to 3.0% of GDP by 2016-17 are encouraging. We welcome the proposal to constitute an Expenditure Management Commission to focus on improving the efficiency of spending. However, additional clarity is awaited on plans to overhaul the subsidy regime, as improved targeting is critical to free-up resources for more productive capital spending.

In contrast to market expectations, the fiscal deficit target of 4.1% of GDP announced in the Vote-on-Account in February 2014, has been retained in the Budget for 2014-15; we maintain our view that achieving this target would be challenging. In particular, the assumption of net tax revenue growth of 20% in 2014-15 relative to provisional data for 2013-14 appears optimistic. While economic growth remained feeble in Q1FY15, the unfavourable progress of the south west monsoon so far and delay in sowing of most major crops are
expected dampen agricultural growth and rural demand in the remainder of this year. Moreover, investment activity is expected to pickup gradually, notwithstanding the constructive measures announced in the Budget for 2014-15. As a result, growth of corporation tax, excise duty and service tax are unlikely to improve substantially as compared to the performance in 2013-14. Additionally, the increase in the exemption limit under personal income tax would help buffer disposable incomes of lower income households against the relentlessly high retail inflation. In this context, the estimated 20% growth of personal income tax collections in the Budget Estimates (BE) for 2014-15 relative to the provisional actual for 2013-14 seems rather high. In particular, the lack of a roadmap for the transition to the much-awaited goods & services tax is disappointing.

Notwithstanding the improved sentiments in the equity markets, actual disinvestment proceeds would take a cue from the timing of offerings as well as valuations. Gross borrowings are indicated at Rs. 6.0 trillion in 2014-15, largely similar to the interim budget estimates and 6.4% higher than the level in 2013-14.

The stated focus on fiscal consolidation, absence of populist measures, focus on growth and other measures to revive investor confidence, would support the improved sentiments seen in recent months. Nevertheless, we continue to expect only a mild improvement in economic growth to 5.0-5.5% in 2014-15 from the sub-5% levels in 2012-14. The extent and pace of reforms carried out by the Government and the speed with which the investment cycle revives would determine whether GDP growth can accelerate to levels well above 6% over the medium term.
Assessment of Government of India’s Fiscal Situation

Contrary to market expectations, the Budget for 2014-15 (“Revised Budget Estimates” or RBE) indicates a similar fiscal deficit of Rs. 5.3 trillion (4.1% of GDP) as compared to the level indicated in the Interim Budget Estimates (IBE) for 2014-15 that had been presented in February 2014 prior to the Parliamentary Elections (refer Table 1), with the impact of lower tax revenues and higher expenditure offset by higher estimated inflows from non tax revenue receipts and disinvestment.

Overall, the RBE indicates continued fiscal consolidation (refer Chart 1), with a fall in the fiscal deficit to 4.1% of GDP in 2014-15 from 4.5% of GDP in 2013-14 (according to provisional data).

Revenue Receipts: Revenue receipts are estimated to expand by 17% in 2014-15 RBE, as compared to the level in 2013-14 (prov.), led by an estimated 20% rise in net tax revenues, which factors in GoI’s expectation that nominal economic growth would be 13.4% in 2014-15; ICRA continues to expect real growth of 5.0-5.5% in FY15.

Notably, the estimate for overall revenue receipts for 2014-15 has been revised upwards by Rs. 227 billion in the RBE for 2014-15 as compared to the IBE, on account of higher non tax revenues of Rs. 318 billion (led by dividends & profits and receipts from communication and transport), offset by lower net tax revenues of Rs. 91 billion (mainly on account of personal income tax).

Tax revenues are estimated to rise by 20% in 2014-15 RBE, as compared to the modest 9% growth in April-May 2014 (refer Tables 2 and 3). No major changes were announced in direct tax rates. Personal income tax collections are estimated to rise by 20% in 2014-15, which seems somewhat optimistic in light of the increase in the exemption limit, higher investment limit under Section 80C of the Income Tax Act as well as rise in deduction limit on loans on self occupied properties by Rs. 50,000 each.

Additionally, corporation tax collections are estimated to rise by 14% in 2014-15 RBE. Major changes include an investment allowance at the rate of 15% proposed for manufacturing companies investing in excess of Rs. 0.25 billion in any year in new plant and machinery upto March 31, 2017 and an extension of the 10 year tax holiday for entities that begin generation, transmission and distribution of power by March 31, 2017.

Table 1: GoI’s Fiscal Balances

<table>
<thead>
<tr>
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</thead>
<tbody>
<tr>
<td>Revenue Receipts</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tax Revenues$</td>
<td>10,153</td>
<td>11,671</td>
<td>11,898</td>
<td>15%</td>
<td>17%</td>
</tr>
<tr>
<td>Non Tax Revenues</td>
<td>1,992</td>
<td>1,807</td>
<td>2,125</td>
<td>45%</td>
<td>7%</td>
</tr>
<tr>
<td>Revenue Expenditure</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenue Deficit</td>
<td>-3,603</td>
<td>-3,829</td>
<td>-3,783</td>
<td>-5%</td>
<td>84%</td>
</tr>
<tr>
<td>% of GDP</td>
<td>-3.2%</td>
<td>-3.0%</td>
<td>-2.9%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital Receipts (Non Debt)</td>
<td>401</td>
<td>675</td>
<td>740</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital Expenditure</td>
<td>1,879</td>
<td>2,132</td>
<td>2,268</td>
<td>13%</td>
<td>21%</td>
</tr>
<tr>
<td>Fiscal Deficit</td>
<td>-5,081</td>
<td>-5,286</td>
<td>-5,312</td>
<td></td>
<td></td>
</tr>
<tr>
<td>% of GDP</td>
<td>-4.5%</td>
<td>-4.1%</td>
<td>-4.1%</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: GoI Budget Documents; CGA; ICRA Research
$ Net of Refunds, Net of States’ share in Central Taxes

Chart 1: GoI’s Revenue and Fiscal Deficit as a Percentage of GDP

Source: GoI Budget Documents; CGA, Ministry of Finance, GoI; ICRA Research
Gol has forecast excise duty collections to rise by 20% in FY15, following the 2% contraction in 2013-14 (prov.). To boost excise collections, higher ‘sin’ duties have been imposed on items such as cigarettes, cigars, tobacco products as well as aerated drinks. However, some relief has been extended on some categories of footwear, branded petrol etc. Various excise duty cuts announced in the Interim Budget in February, 2014 (initially for a period of three months) to boost the capital goods and automobile sector, had already been extended upto 31st December 2014.

Moreover, customs duty collections are forecast to expand by 19% in the ongoing fiscal, higher than the 17% growth in 2013-14 (prov.); the achievement of this target would critically depend on the volume of trade. Basic customs duty on various products including stainless steel, bauxite, cut and broken diamonds, specific telecommunication products has been increased while the duty structure on various types of coal has been rationalized. Additionally, education cess and secondary & higher education cess are being levied on imported electronic products so as to provide parity between domestically produced goods and imported goods.

Gol has forecast service tax collections to rise by a sharp 40% in 2014-15, higher than the 17% growth in 2013-14 (prov.), the achievement of which seems to be optimistic. The Budget proposed to henceforth levy service tax on sale of space or time for advertisement in broadcast media and radio taxis.

The RBE for 2014-15 forecast a 7% growth in non tax revenues. Dividends & profits are estimated at Rs. 902 billion in 2014-15 RBE (Rs. 882 billion in 2013-14 RE), and revenues from other communication services at Rs. 455 billion (Rs. 408 billion in 2013-14 RE).

The target for other non debt capital receipts has been set at Rs. 634 billion in 2014-15 RBE, more than twice as high as the Rs. 276 billion in 2013-14 (prov.). The former includes Rs. 434 billion as disinvestment receipts, Rs. 150 billion as divestment of Government stake in non-Government companies, as well as an additional receipt of Rs. 50 billion. Notwithstanding the recent buoyancy in the secondary equity markets, the magnitude of funds raised through stake sales in Government and non-Government companies would depend on various factors including market conditions at the time of sale, valuations etc.

**Revenue Expenditure:** Revenue expenditure is budgeted to increase by 14% in 2014-15 RBE relative to the level in 2013-14 (provisional; refer Table 5). While non plan revenue expenditure is expected to rise by a modest 9% in 2014-15 RBE, plan revenue expenditure is expected to rise by a considerable 29%.

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**Table 2: Trends in Tax Revenue Receipts in 2013-14 RE and 2014-15 BE**

<table>
<thead>
<tr>
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</thead>
<tbody>
<tr>
<td><strong>Gross Tax Revenues</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- Corporation Tax</td>
<td>3,947</td>
<td>4,510</td>
<td>4,510</td>
<td>0</td>
<td>14%</td>
</tr>
<tr>
<td>- Income Tax</td>
<td>2,378</td>
<td>3,065</td>
<td>2,843</td>
<td>-222</td>
<td>20%</td>
</tr>
<tr>
<td>- Customs Duty</td>
<td>1,695</td>
<td>2,013</td>
<td>2,018</td>
<td>5</td>
<td>19%</td>
</tr>
<tr>
<td>- Union Excise Duty</td>
<td>1,721</td>
<td>2,006</td>
<td>2,071</td>
<td>65</td>
<td>20%</td>
</tr>
<tr>
<td>- Service Tax</td>
<td>1,546</td>
<td>2,155</td>
<td>2,160</td>
<td>5</td>
<td>40%</td>
</tr>
</tbody>
</table>

Source: Gol Budget Documents; CGA; Economic Survey 2013-14; ICRA Research

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**Table 3: Trends in Tax Revenue Receipts in April-May FY15**

<table>
<thead>
<tr>
<th></th>
<th>2014-15 RBE (Rs. billion)</th>
<th>2M FY14 (Prov.)</th>
<th>% of RBE</th>
<th>Growth</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Gross Tax Revenues</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Corporation Tax</td>
<td>4,510</td>
<td>30</td>
<td>1%</td>
<td>-8%</td>
</tr>
<tr>
<td>Income Tax</td>
<td>2,843</td>
<td>354</td>
<td>12%</td>
<td>33%</td>
</tr>
<tr>
<td>Customs Duty</td>
<td>2,018</td>
<td>248</td>
<td>12%</td>
<td>-9%</td>
</tr>
<tr>
<td>Excise Duty</td>
<td>2,071</td>
<td>56</td>
<td>3%</td>
<td>-18%</td>
</tr>
<tr>
<td>Service Tax</td>
<td>2,160</td>
<td>144</td>
<td>7%</td>
<td>14%</td>
</tr>
</tbody>
</table>

Source: Gol Budget Documents; CGA; ICRA Research

\(^{\text{A Net of Refunds, Gross of States' share in Central Taxes}}\)
The estimate for revenue expenditure for 2014-15 has been revised upwards by Rs. 181 billion in the RBE as compared to the IBE. Grants for capital assets have been placed at Rs. 1,681 billion in the RBE for 2014-15, higher than the IBE of Rs. 1,466 billion and a substantial 29% higher than the level in 2013-14 (prov.).

The outlay for subsidies has been revised to Rs. 2,607 billion in the RBE for 2014-15 from Rs. 2,557 billion in the IBE for 2014-15, led by a revision in fertiliser subsidies to Rs. 730 billion from Rs. 680 billion, respectively (Rs. 680 billion in 2013-14 RE). ICRA notes that the Interim Budget for 2013-14 had increased the allocation for domestic urea by ~Rs. 100 billion vis-a-vis the 2013-14 budget, which was estimated to have been on account of the proposed increase in domestic gas prices from April 2014 that is yet to be implemented. Hence, only a part of the amount budgeted under this head is likely to be utilised for clearing the subsidy backlog. Accordingly, the subsidy backlog may decline from an estimated ~Rs. 370 billion to ~Rs. 270 billion (assuming $8.4/MMBTU landfall price), if implemented from October 2014. In case the price hike is further deferred, the shortfall will reduce to ~Rs. 220 billion, which nevertheless is still substantial. Also, subsidy delays for the P&K sector are likely to continue as the subsidy has been maintained as per the interim budget, although the budgeted amount may be sufficient to meet the subsidy requirements for 2014-15.

The fuel subsidy allocation has been retained at Rs. 634 billion in 2014-15 RBE, in line with the IBE for 2014-15, but lower than the allocation of Rs. 855 billion in 2013-14 RE. With projected gross under-recoveries (GURs) of OMCs at ~Rs. 1,045 billion in 2014-15, ICRA believes subsidy provision of Rs. ~332 billion for FY15 (net of carried forward amount Rs. 302 billion for Q4FY14) could be largely adequate, if the absolute burden of upstream companies (~Rs. 670 billion) remains at 2013-14 levels. However, if GoI decides to share 50% of GURs providing some relief to upstream companies, around Rs. 190 billion for Q4FY15 would have to be rolled over to 2015-16. While the Budget emphasises on reducing fuel subsidies, the specifics for the same are not yet announced. The rationalisation of LPG subsidies would play a major role in cutting down fuel subsidies and a concrete plan of action for the same could be imperative.

The food subsidy allocation (refer Table 4) has been retained at Rs. 1,150 billion in 2014-15 RBE in line with the IBE for 2014-15. However, this is higher than the allocation of Rs. 920 billion in 2013-14 RE, in light of the additional funding required for the implementation of the National Food Security Act (NFSA). While this allocation is lower than the estimate of ~Rs. 1,247 billion made previously by GoI for food subsidies following the enactment of the NFSA, the extension in the deadline for the identification of beneficiaries under the NFSA would reduce additional costs to some extent in the current fiscal.

<table>
<thead>
<tr>
<th>Table 4: Non-Plan Expenditure for Key Ministries/Departments in FY14</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Rs. billion</strong></td>
</tr>
<tr>
<td><strong>IBE</strong></td>
</tr>
<tr>
<td>Department of Fertiliser</td>
</tr>
<tr>
<td>Department of Food &amp; Public Distribution</td>
</tr>
<tr>
<td>Ministry of Petroleum &amp; Natural Gas</td>
</tr>
<tr>
<td><strong>Total</strong></td>
</tr>
</tbody>
</table>

*Source: GoI Budget Documents; CGA; ICRA Research*

<table>
<thead>
<tr>
<th>Table 5: Trends in Revenue and Capital Expenditure</th>
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</thead>
<tbody>
<tr>
<td><strong>Rs. billion</strong></td>
</tr>
<tr>
<td><strong>prov. (1)</strong></td>
</tr>
<tr>
<td>Revenue Expenditure</td>
</tr>
<tr>
<td>Interest</td>
</tr>
<tr>
<td>Major Subsidies</td>
</tr>
<tr>
<td>Pensions</td>
</tr>
<tr>
<td>Grants Capital Assets</td>
</tr>
<tr>
<td>Capital Exp. Gross Loans &amp; Adv.</td>
</tr>
</tbody>
</table>

*Source: GoI Budget Documents; CGA; ICRA Research*
**Capital Expenditure:** Capital expenditure and gross lending is budgeted to rise by a substantial 21% in 2014-15 RBE relative to 2013-14 prov. The forecast for capital expenditure for 2014-15 has been revised upwards in the RBE as compared to the IBE by Rs. 136 billion.

Notably, the allocation for Bank recapitalisation is set at Rs. 134.5 billion in the RBE for 2014-15, higher than the IBE of Rs. 112 billion and the outgo of Rs. 140 billion in 2013-14 RE. Notwithstanding the upward revision, the allocation is limited as compared to the prevailing asset quality trends and the capital requirements for meeting the Basel-III norms.

**Fiscal Balances:** At an absolute level, the revenue deficit and fiscal deficit are estimated to widen in 2014-15 RBE as compared to the provisional actuals for 2013-14 (refer Table 6). However, the effective revenue deficit is estimated to decline somewhat to Rs. 2.1 trillion in 2014-15 from Rs. 2.3 trillion in 2013-14 (prov.).

As a percentage of GDP, all the fiscal metrics are set to improve in 2014-15 RBE relative to 2013-14 (prov.). Moreover, the targeted fiscal deficit of 4.1% of GDP for the current fiscal is slightly lower the target that had been set in October 2012 (refer Table 7).

Curtailing the fiscal deficit to 4.1% of GDP for 2014-15 seems challenging, given the optimistic assumptions for nominal GDP growth (13.4%) and net tax revenue growth (20%). While economic growth remained feeble in Q1FY15, the unfavourable progress of the south west monsoon so far and delay in sowing of most major crops are expected dampen agricultural growth and rural demand. Moreover, investment activity is expected to pickup gradually, notwithstanding the constructive measures announced in the Budget for 2014-15.

The rolling targets indicated by GoI for 2015-16 and 2016-17 aim to curtail the fiscal deficit to 3.6% of GDP and 3.0% of GDP, respectively, in line with the targets set in October 2012. Outstanding liabilities are projected to decline to 41.5% of GDP in 2016-17, an improvement from 46.0% in 2013-14 RE.

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**Table 6: Fiscal Balances for GoI**

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</thead>
<tbody>
<tr>
<td>Revenue Deficit</td>
<td>-3,603</td>
<td>-3,829</td>
<td>-3,783</td>
<td>NA</td>
<td>NA</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>-3.2%</td>
<td>-3.0%</td>
<td>-2.9%</td>
<td>-2.2%</td>
<td>-1.6%</td>
</tr>
<tr>
<td>Effective Revenue Deficit</td>
<td>-2,305</td>
<td>-2,363</td>
<td>2,102</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>-2.0%</td>
<td>-1.8%</td>
<td>-1.6%</td>
<td>0.0%</td>
<td>0.0%</td>
</tr>
<tr>
<td>Fiscal Deficit</td>
<td>-5,081</td>
<td>-5,286</td>
<td>5,312</td>
<td>NA</td>
<td>NA</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>-4.5%</td>
<td>-4.1%</td>
<td>-4.1%</td>
<td>3.6%</td>
<td>3.0%</td>
</tr>
<tr>
<td>Total Outstanding Liabilities as a Percentage of GDP#</td>
<td>46.0%</td>
<td>44.8%</td>
<td>45.4%</td>
<td>43.6%</td>
<td>41.5%</td>
</tr>
</tbody>
</table>

Source: GoI Budget Documents; CGA; Economic Survey 2013-14; ICRA Research

#Does not include the portion of National Small Savings Fund and Market Stabilisation Scheme that are not used to finance GoI’s fiscal deficit

^ RE

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**Table 7: Fiscal Deficit Targets for GoI**

<table>
<thead>
<tr>
<th></th>
<th>Performance/Targets in Budget 2014-15</th>
<th>Targets set in October 2012</th>
<th>Targets set by ThFC</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012-13</td>
<td>-4.9%</td>
<td>-5.3%</td>
<td>-4.2%</td>
</tr>
<tr>
<td>2013-14</td>
<td>-4.5%</td>
<td>-4.8%</td>
<td>-3.0%</td>
</tr>
<tr>
<td>2014-15</td>
<td>-4.1%</td>
<td>-4.2%</td>
<td>-3.0%</td>
</tr>
<tr>
<td>2015-16</td>
<td>-3.6%</td>
<td>-3.6%</td>
<td>-3.0%</td>
</tr>
<tr>
<td>2016-17</td>
<td>-3.0%</td>
<td>-3.0%</td>
<td>-3.0%</td>
</tr>
</tbody>
</table>

Source: GoI; ThFC Report; ICRA Research
**Borrowings:** GoI has now indicated gross borrowings of Rs. 6.0 trillion in 2014-15 (refer Table 8), 6.4% higher than the level in 2013-14. The net long term borrowings are placed at Rs. 4.61 trillion in 2014-15, marginally higher than the borrowings of Rs. 4.54 trillion in 2013-14. In line with the slight increase in the fiscal deficit in the RBE relative to the IBE for 2014-15 (Rs. 25 billion), there is a marginal increase in gross borrowings (Rs. 30 billion).

Yields of dated Government securities are likely to remain elevated in the near term, based on our expectation of a low likelihood of Repo rate cuts in the near term as the Reserve Bank of India (RBI) moves towards implementing the recommendations of the Dr. Urjit Patel Committee on the revised monetary policy framework.

In 2013-14, the GoI in coordination with the RBI switched ~Rs. 310 billion of securities maturing in 2014-15 and 2015-16 for longer term securities with institutional investors. Additionally, securities amounting to Rs. 156 billion were bought back in March 2014. In continuation with this strategy of easing the redemption pressure in the near term, further buy-back/switching of shorter tenor securities worth Rs. 500 billion is proposed in 2014-15.

<table>
<thead>
<tr>
<th>Table 8: GoI’s Long-Term Market Borrowings (Rs. billion)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
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<tr>
<td><strong>2013-14</strong></td>
</tr>
<tr>
<td>Net Borrowings</td>
</tr>
<tr>
<td>Redemptions</td>
</tr>
<tr>
<td>Gross Borrowings</td>
</tr>
</tbody>
</table>

Source: RBI; ICRA Research
ICRA Sectoral Analysis

Power

Proposals

- Introduction of Deen Dayal Upadhyay Gram Jyoti Yojana with an allocation of Rs. 5 billion to ensure 24x7 power supply to all rural households.
- Proposal for rationalisation coal linkages with an objective of providing adequate coal supplies to projects, which are already commissioned or to be commissioned by March 2015.
- Encouragement for banks to lend long term funds in infrastructure sector and permission to raise finances for the same with minimum statutory requirements.
- Extension in income tax holiday under section 80-IA for the projects to be commissioned till 2016-17.
- Allocation of Rs. 5 billion towards the proposal to take up Ultra Mega Solar Power Projects in Rajasthan, Gujarat, Tamil Nadu and Ladakh.
- Allocation of Rs. 1 billion towards Ultra-Modern Super Critical Coal Based Thermal Power Technology to promote cleaner and more efficient thermal power.
- Allocation of Rs. 4 billion for launching scheme for solar power driven agricultural pump sets and water pumping stations.
- Allocation of Rs. 1 billion for the development of 1 Mega Watt Solar Parks on the banks of canals.
- Focus on facilitation of evacuation of renewable energy through faster implementation of Green Energy Corridor Projects.
- Reduction in basic customs duty from 10% to 5% on forged steel rings, which are used in manufacture of bearings of wind operated electricity generators.
- Concessional basic customs duty of 5% proposed on machinery and equipment required for setting up of compressed biogas plants.
- Basic customs duty of 5% extended to machinery and equipment required for setting up of a project for solar energy production and exemption of customs duty for inputs such as flat copper wire for the manufacture of PV ribbons.
- Marginal increase in customs duty on coal to 2.5%.
- Hike in clean coal cess from Rs. 50/Million Tonne (MT) to Rs. 100/MT.

Impact - Positive

The stated intent of rationalisation of coal linkages for the projects that have been commissioned or will be commissioned by end of 2014-15 will help ensure adequate coal availability and improve the viability of their operations. The proposal for encouragement of banks for accessing long term liabilities would help the power sector by way of improved availability of cost competitive long term funds. Further, extension in eligibility date for power projects to avail of tax holidays till 2016-17 will benefit the power projects which are scheduled to be commissioned till then. Moreover, the new rural power scheme is expected to improve power supplies for rural households as well as enable the loss reduction for the distribution utilities. However, the hike in coal cess and marginal increase in customs duty on steam coal would lead to a rise in cost of power generation by about 2.5 paise/unit, which will put a pressure on retail tariffs.
Higher budgetary allocation & duty rationalisation are positive for the clean energy sector. The announcement of ultra mega solar projects in four States is expected to facilitate a large sized solar capacity addition in the country and would also encourage domestic manufacturing of solar projects. Duty measures announced for wind and compressed bio-gas projects are a positive, which will help to reduce the capital cost and hence tariffs. In addition, focus on facilitation of evacuation of renewable energy through faster implementation of Green Energy Corridor Projects is expected to further encourage capacity addition.

**Solar Power**

**Proposals**

- Allocation of Rs. 5 billion for setting up of four Ultra Mega Solar Power Projects in the states of Rajasthan, Gujarat, Tamil Nadu and Ladakh.
- Allocation of Rs. 4 billion for installation of solar power driven agricultural pump sets and water pumping stations.
- Allocation of Rs. 1 billion for the development of canal bank solar power projects of 1 MW each.
- Exemption from basic customs duty for import of specified inputs in manufacturing Ethylene Vinyl Acetate (EVA) sheets used in solar module encapsulation.
- Flat copper wire for the manufacture of photovoltaic (PV) ribbons.
- Exemption of excise duty for the manufacture of EVA sheets and solar back sheets and specified inputs in their manufacture.
- Solar tempered glass used in the manufacture of PV cells and modules.
- Flat copper wire used in tabbing for manufacture of PV cells and modules.

**Impact - Positive**

The impact on the solar sector is positive because of the favourable policies which reaffirm the Government’s commitment towards increasing the share of alternative energy in the domestic energy basket. Additionally, the proposed allocation towards installation of solar power water pumping systems would provide funds for setting up of ~65 MW of such systems. These systems are likely to replace diesel powered pumps, reducing diesel subsidy burden, albeit marginally. Also, the duty waivers on manufacture of some of the material used in production of PV modules would result in minor reduction in their costs. However, the reduction would be higher for thin film modules, as the material intensity is more for such modules as compared to crystalline silicon based ones. Nevertheless, the fiscal incentives augur well for manufacturing these materials domestically, a significant portion of which is currently imported by the module manufacturers.
Auto – 2W/ Passenger Vehicles

Proposals
- Excise duty sop on automobiles, announced first in the Interim Budget in February 2014 and subsequently maintained as per announcement in end-June 2014, left unchanged.

Impact - Positive
In the Interim Budget presented in February 2014, the Centre had cut excise duty on small cars, two-wheelers (2W) and commercial vehicles (CV) to 8% from 12%, on mid-segment cars to 20% from 24% and on large-segment cars to 24% from 27%. Likewise, on Sports Utility Vehicles (SUVs), the excise duty was reduced to 24% from 30%, bringing it in line with that on large-segment cars. The above fiscal incentive was initially made applicable for a limited period till June 30, 2014. However, on June 25, 2014, the Central Government extended the applicable period of excise duty cut on automobiles till December 31, 2014. Since this announcement was already made prior to the presentation of the Union Budget, no separate announcement on the above was made in the budget speech of the Finance Minister. While this measure could be expected to support sales volume growth to some extent over the next six months, sustenance of the same will depend upon reassuring signs of economic recovery.

Commercial Vehicles

Proposals
- Excise duty sop on automobiles, announced first in the Interim Budget in February 2014 and subsequently maintained as per announcement in end-June 2014, left unchanged.
- Increased allocation towards infrastructure sectors, especially roads & highways to Rs. 379 billion.
- Greater thrust on creating 100+ smart cities in India, affordable housing and reviving manufacturing sectors.

Impact: Positive
With benefits of lower excise duty on automobiles being already extended by the Government prior to the budget, the automobile industry, especially commercial vehicle (CV) sector had set its eyes on measures to be proposed for kick starting investments in the infrastructure and manufacturing space. From the perspective of CV OEMs, the increased allocation towards infrastructure sector, especially roads & highways, greater focus on reviving capital spending by manufacturing sectors will be a positive in driving demand for construction-enabling CVs (i.e. tippers), which account for one-fourth of M&HCV sales in India. However, in comparison to the prior year, there was no proposal to increase allocation towards JNURM schemes, which in the past had been a meaningful driver for bus sales. Overall, with excise duty benefits expected to continue till December 2014, expectation of economic recovery and recent improvement in freight rates, we expect CV demand to improve in 2014-15 over the prior year.
Auto Components

Proposals

- Sustenance of excise duty cut on automobiles till December 31, 2014.
- Allowance of 15% provided on investments of more than Rs. 0.25 billion on new plant and machinery for a period of three years.
- Programme to be launched for youth skill development.

Impact - Positive

Auto component manufactures expected to see improved traction in supplies to Original Equipment Manufacturers (OEMs) as automobile sales pick-up on the back of excise sop applicable for a limited period. An allowance of 15% was introduced in last year’s Union Budget on investments of above Rs. 1 billion on new plant and machinery. The lowering of the above threshold to Rs. 0.25 billion is likely to encourage even small-to-mid sized entities to undertake investment projects. This benefit will be available for investments upto March 31, 2017. The Scheme announced last year will continue to operate in parallel till March 31, 2015. The skill development programme proposed to be launched could potentially provide the industry access to a more skilled pool of manpower, an issue which could hinder industry growth over the longer term if left unaddressed.

Tyres

Proposals

- 15% investment allowance: Reduction in minimum limit for investments in new plant and machinery to Rs. 0.25 billion p.a.; benefit to be available for three years (till 31.03.2017).
- Investment of Rs. 378.8 billion in National Highways Authority of India (NHAI) and State Roads.
- Reduction in basic customs duty on butadiene from 5.0% to 2.5%.

Impact - Positive

The tyre industry is expected to spend ~Rs. 100-115 billion over the next 2-3 years in new capacity additions and modernisation. With sizeable capex in the near to medium term, the reduction in minimum limit for investments in new plant and machinery to avail the 15% allowance (as announced in the last budget) to Rs. 0.25 billion, is a positive for the industry. The 15% allowance is made available for investments over next three years (i.e. till 31.03.2017). Also the government’s thrust on investing in road infrastructure is likely to spur automobile sales thereby driving tyre demand. The announcement towards the reduction in basic customs duty on import of butadiene (a key raw material used in tyres) from 5.0% to 2.5% can be expected to support margin expansion for tyre manufacturers.
Iron & Steel

Proposals

- Thrust on construction.
- Reduction in customs duty from 5% to 2.5% on steel-grade dolomite and ships for scrapping.
- Increase in customs duty on stainless steel flat products from 5% to 7.5%.
- Revision of royalty rates on minerals, resolution of issues in mining.
- Increase in clean energy cess on coal from Rs. 50/MT to Rs. 100/MT.

Impact - moderately positive

The long term impact on the steel sector is positive because of the favourable policies on demand side. Increased tax incentives to individual home buyers, enhanced allocation towards affordable housing, development of smart cities, new gas pipelines and new ports and airports would support long term steel demand. Also, the increase in custom duty on stainless steel flat products and reduction of customs duties on ships and steel-grade dolomite are positives. The Government’s intention to address current issues in mining for making it more supportive to the industry is also welcome. However, a revision of royalty rates on minerals is likely to adversely impact the cost structure of steel players. Additionally, an increase in clean energy cess on coal would impact margins of domestic sponge iron players.

Capital Goods

Proposals

- 15% investment allowance continued for investments above Rs. 0.25 billion till 2016-17.
- Allocation of Rs. 4 billion for launching scheme for solar power driven agricultural pump sets and water pumping stations.
- Allocation of Rs. 1 billion for the development of 1 MW Solar Parks on the banks of canals.
- Reduction in the basic customs duty from 10% to 5% on forged steel rings, used in the manufacture of bearings of wind operated electricity generators.
- Concessional basic customs duty of 5% proposed on machinery and equipment required for setting up of compressed biogas plants.
- Basic customs duty of 5% extended to machinery and equipment required for setting up of a project for solar energy production and exemption of customs duty for inputs such as flat copper wire for the manufacture of PV ribbons.
- Proposed measures for improving long term funding of infrastructure projects.
Impact - Marginally Positive

Given the slowdown in industrial capex since the last two years, continuation of investment allowance till 2016-17 is likely to incentivize companies across the manufacturing & infrastructure sector to invest in fresh projects, which is likely to support demand for capital goods. Further, duty rationalisation & increased budgetary allocation for renewable projects as well as measures announced to encourage long term funding for the infrastructure sector are likely to encourage capacity addition in the power and renewable energy sectors, which in turn is likely to result in boosting demand for the capital goods sector. Exemption of duties for certain inputs coupled with introduction of customs duty for final product is likely to benefit domestic manufacturing of solar products.

Tractors

Proposals

- Target for institutional credit flow to agriculture raised to Rs. 8,000 billion in 2014-15; interest subvention scheme for crop loans to continue in 2014-15 along with additional subvention of 3% to prompt-paying farmers. Proposal to setup a long-term rural credit fund to promote asset creation in agri and allied activities.
- Farmers to have direct access to markets; integration of agri-markets across the country. Dedicated programmes to protect farmers from vagaries of climate change and price volatility of agri-produce. Focus on scientific warehousing infrastructure through creation of Warehouse Infrastructure Fund.
- Allocation of Rs. 10 billion towards improving irrigation penetration, and reducing dependence on monsoons. New programme to promote watershed development.

Impact - Positive

With strong co-relation between farm mechanisation and credit availability, increase in institutional credit flow to the agri sector augurs well for the tractor industry. Focus on irrigation projects as well as setting up of funds to protect farmers from vagaries of climate change, and price volatility of agri-produce shall help provide some stability to farm inflows. A modern warehousing setup and direct access to customers through a national market shall also positively influence farmers’ bargaining power and earning capability. Further, Government’s thrust on rural development through programmes such as Pradhan Mantri Gram Sadak Yojana, and Mahatma Gandhi National Rural Employment Guarantee Scheme, is expected to have positive influence on demand side drivers in tractor industry.

Aviation

Proposals

- Scheme proposed for development of airports in Tier I and II cities.
- New airports to be developed through PPP mode.
- Tourism boosting proposals like development of five tourist circuits and e-visas at nine airports.
**Impact - Positive**

India's airport infrastructure lags behind many developed as well as emerging markets as majority of the investments have been focused on Tier I cities. The proposed scheme for development of airports in Tier I and II cities will lead to improvement in connectivity and thus propel passenger traffic growth. In addition, various proposals aimed at boosting tourism, should further increase the passenger traffic and thus passenger load factors for airlines.

### Airports

**Proposals**

- Issuance of E-visas on arrival at nine major airports.
- Development of new airports in Tier-I and Tier-II cities through Airport Authority of India or through PPP.
- Setting up of institution called 3P India for developing sophisticated contract models and dispute redressal for PPP projects.

### Impact - Positive

The above proposals will support the investments in the Airport infrastructure sector by both public and private sector. Improved connectivity across Tier-I and Tier-II cities coupled with visa-on-arrival shall support the domestic demand for air travel as well as increase in international tourists and hence improve the attractiveness of investments in the airport infrastructure sector.

### Shipping

**Proposals**

- Plan to develop the National Waterways-I (between Allahabad and Haldia covering a distance of 1,620 km) to promote coastal movement at an estimated cost of Rs. 42 billion over a period of six years.
- Policy for encouraging the growth of Indian controlled tonnage to ensure increase in employment of the Indian seafarers.
- Promoting movement of goods though inland waterway/ coastal movement by reducing the tax incidence and removing the anomalies of the service tax between inland waterways and road/ rail movement of goods.
- Plan to frame a comprehensive policy to promote Indian ship building industry in the current financial year.
- Import duty on ships imported for breaking reduced to 2.5% from 5.0%.
Impact - Positive

The proposal to develop a new inland waterway is positive towards building an efficient logistics sector and facilitating decongestion of already constrained Road and Rail network, while promoting energy savings and reducing the overall transportation costs. Presently, domestic vessel operators have to bear various other direct and indirect taxes which reduce the incentive for domestic companies to operate Indian Flag vessels. The budgetary proposal of reduction in the tax incidence of sea farers through amendment in the act and removing the anomalies of the service tax between inland waterways and road/rail movement of goods would promote movement of goods through coastal routes, besides acquisition of more Indian tonnage.

Development of inland waterways would require construction of new small size vessels of 1,500 DWT to 3,000 DWT thereby providing filling to the domestic ship building industry. A comprehensive policy is expected to be announced to promote Indian ship building industry in the current financial year. Further, import duty on ships imported for breaking has been reduced to 2.5% from 5.0% thereby benefitting the domestic shipbreaking industry. Overall, the above measures giving a thrust towards movement of goods through waterways are positives for the domestic shipbuilding & shipping sector, which has been facing several challenges such as slowdown in orders, cancellation of orders, stretched cash flows and high leverage.

Cement Proposals

- Increase in interest deduction to Rs. 200,000 on housing loan to provide fillip to housing demand.
- Enhancement in allocations for Rural Housing Fund to ensure better flow of institutional credit for housing loans.
- Several measures to promote infrastructure projects including proposal to set up new airports and metro projects under PPP route; significant allocations to develop existing ports and set up new ports; target to develop 8,000 km roads in 2014-15; significant allocations to Pradhan Mantri Gram Sadak Yojna and to Road Building Plan; slew of measures to promote renewable energy projects; and continuation of tax holiday for power companies.
- Allowing banks to raise long-term funds with minimum statutory requirements to finance infrastructure projects.

Impact - Marginally Positive

Increased provision under Rural Housing Fund and interest deduction on housing loans will boost urban and rural housing demand and in turn demand for cement. Further, government measures to promote investment in ports, roads, airports and other infrastructure projects are also likely to support cement demand. Cement companies are also likely to also benefit from the increase in long term funding availability for infrastructure projects which is likely to facilitate more investment in these sectors.
Road Sector

Proposals

- Banks will be allowed to raise long-term funds for lending to infrastructure sector with minimum regulatory pre-emption such as CRR, SLR and priority sector lending (PSL); further, Infrastructure Investment Trusts (InvITs) will be formulated, to provide funding for PPP and other infrastructure projects.
- Targeted construction of 8500 Km of National Highways for FY 15 as against 1897 km during FY 14 and 2704 km in FY 13.
- De-bottlenecking clearance process to speed up execution.
- Total budgetary allocation towards NHAI and State roads stands at Rs. 378.50 billion in FY 15 as against Rs. 373 billion in FY 14 an increase of 1.5%.
- Budgetary allocation towards Pradhan Mantri Gram Sadak Yojana (PMGSY) at Rs. 143.89 billion vis-à-vis Rs. 217 billion in FY 14- lower by 34%.
- Work initiation on select expressways in parallel to the development of industrial corridors.

Impact - Positive

Around 81 NH projects covering ~9,442 km, which were awarded more than 2 years back, were yet to start as of May 31, 2014 on account of various execution bottlenecks like unavailability of RoW, clearances from Environment and Forest ministries etc. Efforts towards de-bottlenecking clearances would kick start these stalled projects resulting in improved execution rate. The targeted completion of 8500 km of National highways in FY15, though appears aggressive when compared to actual implementation over the past few years. The government also seeks to increase the funding options for the infrastructure projects by allowing banks to raise long-term funds with minimum regulatory pre-emption such as from CRR, SLR and priority sector lending (PSL). Further, formulation of Infrastructure Investment Trusts (InvITs), with tax related incentives, can act as important alternate avenue of long-term project finance.

While the allocation to PMGSY has been lowered, it remains sizeable. This coupled with the increased allocation towards NHAI and State roads will help the order-book of road construction companies. However, absence of any mention on setting up of the Road sector regulator, may have disappointed the road sector participants.

Real Estate

Proposals

- Pass-through taxation structure for REITs.
- Reduction in FDI eligibility threshold limits in terms of area (from 50,000 sqm to 20,000 sqm) and capital (from USD 10 mn to USD 5 mn); further, no threshold limits for projects having 30% of the total cost towards low cost housing development.
- Allocation of Rs. 40 billion to National Housing Board (NHB) for providing cheaper credit for affordable housing to the urban poor/EWS/LIG segment.
- Allocation of Rs. 71 billion for development of 100 smart cities.
Increase in provision under Rural Housing Fund to Rs. 80 billion from the existing Rs. 60 billion to provide housing finance to targeted groups in rural areas at competitive rates.

Development of convention centres in PPP mode through Viability Gap Funding (VGF) scheme.

Increase in the deduction limit for interest on home loans in respect of self occupied house property from Rs. 150,000 to Rs. 200,000.

Revival of interest in SEZ projects

**Impact - Positive**

The key positives for the sector include the reduction in FDI eligibility threshold as well as the proposed tax incentives for REITs, both of which would pave way for increasing investment in the sector. The budget recognises the role of REIT as an important source of investment for the industry and looks at providing incentives to the same, which will have pass through for the purpose of taxation.

The allocation of Rs. 71 billion of funds for development of Smart Cities would give a boost to large scale township development projects. In line with the endeavour to have housing for all by 2022, the Government announced initiatives for promoting affordable housing such as availability of cheaper credit through NHB and allowing FDI without any threshold limits for projects having 30% of the total cost towards low cost housing development. Other proposals such as development of convention centres on PPP model, additional income tax benefit through increase in deduction limit for interest on home loans, and intention to revive interest in SEZ projects are also expected to augment the activity in the sector.

**Construction/Infrastructure**

**Proposals**

- Thrust on capital investment by PSUs – plan to invest Rs. 2,479 billion in FY15 to create a virtuous investment cycle; further the proposed investment allowance for manufacturing companies investing more than Rs. 0.25 billion till FY 2017.
- Extension of 80 IA benefit for the power sector till FY 2017.
- Increased outlay on various infrastructure projects across sectors including Ports, Airports, Irrigation, Roads, Metros, SEZs, Power, River linking, Gas grid and Warehousing.
- To set-up an institution (called 3P India) to provide support to mainstreaming PPPs.
- Banks to be permitted to raise long-term funds for lending to infrastructure sector with minimum regulatory pre-emption such as CRR, SLR and priority sector lending (PSL); further, Infrastructure Investment Trusts (InvITs) will be formulated, to provide funding for PPP and other infrastructure projects.

**Impact - Positive**

Recognizing the need to kick-start investment cycle, the budget plans to renew the thrust on public sector investments by proposing 65% increase in capital investment target of PSUs to Rs. 2.48 trillion in FY15 from around Rs. 1.4 trillion in FY14. Moreover, fund allocations towards infrastructure projects like highways (Rs. 379 billion for NH and state roads), rural roads (Rs. 144 billion under PMGSY), sixteen new ports (Rs. 11 billion), 15,000 km of gas grid, 1620 Km of Jal marg vikas (Rs. 42 billion) and urban infrastructure like rail, metros, LRT
will also boost capital expenditure. Other proposals including extension of 80 IA benefit for power sector, investment allowance for manufacturing companies, development of convention centres under PPP mode, augmenting warehousing capacity and proposals to increase investments in affordable housing, are expected to bolster the order-books of construction companies.

The budget also emphasized need for streamlining PPP model and has planned steps on increasing the availability of long-term funding for infrastructure projects. In this regard proposals are made to set-up a new institution by the name of ‘3P India’ to provide support to mainstreaming PPPs, as well as formulation of Infrastructure Investment Trusts (InvITs) to support long term fund availability for infrastructure sector. Furthermore, it also proposed steps to encourage lending to infrastructure projects by banks with some pre-emption of regulatory requirements of CRR, SLR and Priority Sector Lending as well as flexible structuring to absorb potential adverse contingencies.

**Oil & Gas**

**Proposals**

- Fuel subsidies to be reduced; specifics are not yet announced.
- Gas pipelines of 15,000 km length to be built to complete national gas pipeline grid under PPP model.
- Push for coal-bed methane (CBM) exploration and production.
- Focus on piped natural gas (PNG) as a cleaner fuel.
- Use of domestic as well as imported gas (RLNG) to be encouraged to reduce dependence upon any one source of energy.
- Excise duty on branded petrol reduced from Rs 7.50 per litre to Rs 2.35 per litre.

**Impact - Neutral**

With projected gross under-recoveries (GURs) of OMCs to be ~Rs. 1,045 billion in 2014-15, ICRA believes subsidy provision of ~Rs. ~332 billion for FY15 (net of carried forward amount Rs. 302 billion for Q4 FY14) could be largely adequate if the absolute burden of upstream companies (Rs. 670 billion) does not decrease vis a vis 2013-14. However, if the GoI decides to share 50% of GURs providing some relief to upstream companies, around Rs. 190 billion for Q4 FY15 would have to be rolled over to 2015-16. The budget emphasises on reducing fuel subsidies; however, the specifics for the same are not yet announced. The rationalisation of LPG subsidies would play a major role in cutting down fuel subsidies and a concrete plan of action for the same could be imperative. The budget proposes to build 15,000 km gas transportation pipelines to complete national gas pipeline grid under public-private partnership (PPP) model. Besides, piped natural gas (PNG) pipelines may be laid in more cities to enhance focus on the use of PNG (instead of LPG) as a cleaner fuel. Further, the use of domestic gas as well as RLNG would be encouraged to reduce dependence upon any one source of energy (crude oil). Overall, enhanced focus on gas sector is key positive of gas transportation players (like GAIL, GSPL etc) and city gas distribution (CGD) entities. However, the utilisation of existing and upcoming gas pipelines could vary with the availability of natural gas, which critically depends upon the faster review of domestic gas pricing along with resolution of NELP related issues. Moreover in light of low visibility on domestic gas availability in the medium term and concerns over the affordability of R-LNG, the appetite of the investors towards gas grid projects may remain low in view of the capital intensive nature of these projects.
Reduction of excise duty on branded petrol by Rs 5.15/litre will reduce the price differential vis a vis unbranded petrol; this measure could help revive branded petrol sale for OMCs, which otherwise had been experiencing sharp degrowth in the past few years due to high price differential and increasing price trends in petrol in general.

**Petrochemicals**

**Proposals**

- Reduction in basic customs duty on reformate from 10.0% to 7.5%, on ethane, propane, ethylene, propylene, butadiene and ortho-xylene from 5.0% to 2.5%, on methyl alcohol and denatured ethyl alcohol from 7.5% to 5.0%.
- Exemption on Polyester Stable Fibre (PSF) and Polyester Spun Yarn (PFY) manufactured from plastic waste and scrap from excise duty with effect from June 29, 2010 to May 7, 2012; levied an excise duty of 2.0% without Cenvat benefit and 6.0% with Cenvat benefit on such PSF and PFY.
- Investment allowance of 15% for investments above Rs. 1 billion to continue till March 31, 2015; in parallel another scheme announced for investment allowance of 15% for investments in plant and machinery of more than Rs. 0.25 billion for investments made till March 31, 2017.

**Impact - Positive**

The reduction in basic customs duty on methyl alcohol (methanol) would reduce the import parity price of these products leading to lower realisations for domestic manufacturers such as GNFC, Deepak Fertilisers and RCF which would negatively impact their profitability. However, the domestic producers have benefited from INR depreciation against USD in the last two years, and hence the impact on bottomline is muted to that extent. Lowering of customs duty on ethanol will enable some of the alcohol based chemical manufacturers to import alcohol if global prices are attractive. Similarly Oil Marketing Companies (OMCs) could be benefited if they import alcohol for the gasohol programme.

Similarly realisations of domestic manufacturers of butadiene, such as RIL and Haldia Petrochemicals, would be lower on account of lower import parity prices. However, as butadiene constitutes a small share of their sales and profits, it's unlikely to materially impact their overall profits. Nevertheless the lowering of the basic customs duty is positive for the domestic producers using these petrochemicals as raw materials as they would gain on account of lower input costs. These would include Poly Vinyl Chloride manufactures using imported ethylene, Phthalic Anhydride manufactures using ortho-Xylene as raw material and synthetic rubber and engineering plastics manufacturers such as SBR, PBR and ABS. Additionally levying of excise duty on PSF and PFY manufactured from recycled waste is marginally negative for such manufacturers but is unlikely to dampen the trend of increasing usage of recycled plastic waste in the industry for specific applications. The investment allowance of 15% for investments above Rs. 0.25 billion would benefit projects being set up from 2014-15 to 2016-17 especially considering several plastic processors would fall in this category.

**Fertilisers**

**Proposals**

- Budgetary provision for subsidy: Rs. 730 billion for 2014-15 (RE) against Rs. 680 billion (IBE).
- Subsidy on indigenous fertilisers (urea): Rs. 360 billion.
- Subsidy on imported fertilisers (urea): Rs. 123 billion.
Subsidy on decontrolled fertilisers: Rs. 247 billion.

New pricing policy for urea to be implemented.

Rs. 1 billion for provision of soil health card to every farmer.

Rs. 0.6 billion for 100 mobile soil testing laboratories to study impact of fertilisation on soil health.

National Adaptation Fund for climate change.

Long-term impetus on improving irrigation coverage and river interlinking, agro-technology management, horticulture and organic farming and improvement of soil health to improve agricultural growth.

**Impact- Marginally positive**

The GoI has increased the budgeted subsidy by Rs. 50 billion to Rs. 730 billion as compared to the IBE of Rs. 680 billion. The step is a marginal positive in terms of improving the financial health of the fertiliser industry and is noteworthy given the limited headroom for increasing subsidy on account of fiscal pressures. ICRA also notes that the interim budget had increased the allocation for domestic urea by ~Rs. 100 billion vis-a-vis 2013-14 budget, which was estimated to have been on account of the proposed increase in domestic gas prices from April 2014 and the same has not actually been implemented so far. The increase in domestic gas prices is expected in the near term, probably by October 1, 2014. Hence, only part of the amount budgeted under this head is likely to be utilised for clearing the subsidy backlog. Accordingly, subsidy backlog may decline from an estimated ~Rs. 370 billion to ~Rs. 270 billion (assuming $8.4/MMBTU landfall price), if implemented from October 2014. In case the price hike is further deferred, the shortfall will reduce to ~Rs. 220 billion. The shortfall is still substantial and implies a continuation of high subsidy receivables for urea companies. Also, subsidy delays for the P&K sector is also likely to continue as the subsidy has been maintained as per the interim budget, although the budgeted amount may be sufficient to meet the subsidy requirements for 2014-15.

The budget has also emphasised the formulation of a new pricing policy for urea. The GoI appears to be moving in the direction of some sort of linkage between urea retail prices and domestic gas prices and / or implementation of nutrient-based subsidy for urea to address concerns on soil health due to differential pricing between urea and non-urea fertilisers. Measures have also been announced to help improve growth rate of agriculture, such as irrigation management, management of soil health and addressing agro-climatic impact of weak monsoons, which may have an indirect positive effect on the fertiliser sector in the longer run.

**Pharmaceuticals**

**Proposals**

- No major announcements apart from increased budgetary allocation in the healthcare space and focus on providing affordable medicines.
- Proposal to provide assistance to strengthen States’ drug regulatory infrastructure.
- Reduction in limit from Rs. 1 billion to Rs. 0.25 billion for attracting investment allowance of 15% towards capex would however encourage higher spending towards manufacturing and R&D facilities.
Impact-Neutral

There is no specific announcement in the budget for 2014-15 which can have a material impact on the pharmaceutical industry. However, measures such as increased allocation towards healthcare sector, greater focus towards providing 'Free Drugs and Diagnostics' services will result in higher demand for low-cost generic drugs and diagnostic equipment going forward. This will be positive for pharmaceutical firms generating a sizeable share of business from Government-backed healthcare institutions. The Central Government’s proposal to provide assistance to States’ drug regulators for improving their infrastructure may also be seen as a positive step towards speeding up the approval process for launching new drugs in India. Although not directly, but the Government’s proposal to bring down the minimum investment requirement to attract investment allowance will also encourage higher spending by smaller & medium-sized pharmaceutical companies in manufacturing and R&D facilities.

Healthcare

Proposals

- Announcement related to Health for All with the two key initiatives Free Drug Service and Free Diagnosis Service to be taken on priority.
- Setting up of two National Institutes of Ageing at AIIMS, New Delhi and Madras Medical College Chennai to achieve universal access to early quality diagnosis and treatment to TB patients.
- Four new All India Institute of Medical Sciences (AIIMS) proposed in addition to six already operational.
- Setting up of Model Rural Health Research in the states in a bid to provide affordable healthcare and augment transfer of technology for better healthcare services in rural India.
- Central Government Assistance to strengthen States’ Drug Regulatory and Food Regulatory Systems by creating new drug testing laboratories and strengthening the existing 31 State laboratories.

Impact-Neutral

The intent to improve access to quality healthcare has been highlighted as the focus area by the Government with investments proposed towards strengthening the delivery institutions. Additionally, the financial assistance from Central Government to strengthen State Drug Regulatory Systems is a positive – a strong State FDAs would help in ensuring compliances with Good Manufacturing Practices in the State and thus, ensuring availability of quality drugs.

Textiles

Proposals

- Overall budgetary allocation for textile sector increased by 21% to Rs. 57 billion as against RE of Rs 47 billion for 2013-14, of which allocation for TUFS increased to Rs. 23 billion for as against RE of Rs. 20 billion.
- Investment allowance of 15% of investments of Rs. 0.25 billion (reduced from Rs. 1 billion earlier) or more in plant and machinery, which is in addition to existing depreciation rates available till FY 2017 (extended by two years).
- Increase the duty free entitlement for import of trimmings, embellishments and other specified items from 3% to 5% of the value of readymade garments.
- Reduction of basic customs duty reduced on specified inputs for manufacture of spandex yarn from 5% to Nil.
- Exemption of service tax on loading, unloading, storage, warehousing and transportation of ginned or baled cotton.
- Allocation of Rs. 2 billion for setting-up six more textile mega-clusters.
- Levy of 2% (without CENVAT benefit) and 6% (with CENVAT benefit) for PSF and PFY manufactured from plastic waste and scrap.

**Impact - Neutral**

The major incentives for the sector such as TUFS allocation and investment allowance has been continued with enhanced allocation under TUFS and reduced investment allowance eligibility, which will continue to support the investments in the sector. Moreover incremental proposals such as rejigging of the duty structure on inputs for certain segments, exemption of service tax on cotton handling and transportation will have marginal positive impact on the industry. Also the proposal for Textile mega-clusters will help in development of the textile infrastructure in medium to long-term, which is positive for the textile industry as a whole. The levy of excise duty on recycled PSF and PFY is negative for the manufacturers and given that this segment has achieved significant size (~20% of total polyester consumption), it will adversely impact the industry participants.

**Retail**

**Proposals**

- Cut excise duty on food processing and packaging machinery to 6%.
- Increased focus on reducing transportation and distribution losses.
- Allocation of Rs. 50 billion towards warehouse infrastructure fund.
- Exemption of customs duty on sub-19 inch LCD, LED panels; levy of 10% customs duty on imported telecommunication products.

**Impact - Neutral**

Increased focus on transportation and warehousing should facilitate improvement in supply chain efficiencies and thus reduction in transportation and distribution losses. While no clear guidelines on GST roll-out have been indicated, the Budget has laid emphasis on bringing about a solution this year.
Media and Entertainment

Proposals

- Service tax levied on sale of space or time on online and mobile advertising; sale of space for advertisements in print media remains exempted.
- Ensuring broadband connectivity at village level.
- Allocation of Rs. 1 billion to support 600 new and existing Community Radio Stations.
- Colour picture tubes exempted from basic customs duty; cathode ray televisions to be made cheaper.
- Exemption of customs duty on sub-19 inch LCD, LED panels and on specified inputs used in their manufacture.

Impact - Neutral

While levy of service tax on online and mobile advertisement will result in additional outflow for the advertisers, this may not have any major impact on advertising volumes or rates. The duty concessions on televisions will help improve penetration of television in India. This along with improvement in broadband connectivity will lead to an overall increase in viewership and thus better reach for advertisers. As such, since no major announcements have been made, the overall impact on the media & entertainment sector is neutral.

Hotel and Tourism

Proposals

- Electronic Travel Authorization (E-Visa) to be introduced at nine airports in India; further, increase in countries under Visa on Arrival facility to boost Foreign Tourist Arrivals.
- Measures announced to enhance women security, transport infrastructure and sanitation to create an environment conducive to promote tourism.
- Development of five tourist circuits, preservation of six heritage sites, Integrated Ganga Conservation Mission, beautification of riverfronts and ghats at seven locations and Pilgrimage Rejuvenation and Spiritual Augmentation Drive; all these expected to attract tourism; thrust on Public-Private partnership mode to improve tourist infrastructure.
- To set up a world class convention facility at Goa to further promote tourism in the region.
- Proposal for CENVAT credit for services rendered by rent-a-cab and tour operators; exemption of service tax for tour operators for services provided to foreigners for tours conducted wholly outside India; rent-a-cab to come under service tax net.

Impact - Marginally Positive

By announcing a timeline of six months for setting up the infrastructure for e-visa facility at nine airports, the government has stated its intention to provide easier visa environment for foreign tourists, thus boosting arrivals into India. Various measures towards ensuring women’s safety, development of road and air transport infrastructure, preservation of heritage / pilgrimage sites, development of tourist circuits, and proposed involvement of private sector in building tourist infrastructure are major positives for the tourism Industry. In addition, allowing CENVAT credit for services rendered by tour operators shall lower tour packages rates, thereby catalyzing demand. The impact of bringing rent-a-cab services
under service tax-net is expected to be partially mitigated by allowing CENVAT credit for services. However, the announcement regarding exemption of service tax for Indian Tour operator is not expected to significantly impact the industry.

**Information Technology**

**Proposals**

- Removal of special additional duty (SAD) on all inputs/components used in the manufacturing of personal computers.
- Impose education cess (3%) on imported electronics products.
- Strengthening of Advance Pricing Agreement (APA1) and introduction of “Roll Back” Provision in the APA schemes.

**Impact - Neutral**

Removal of special additional duty on imports of components used in manufacturing of personal computers will help revive the domestic personal computer manufacturing and assembly sector compared to imports from China and other low cost countries. Education cess of 3% on import of electronic products will further bring parity between domestically produced goods and imported goods. The proposal to strengthen the Advance Pricing Agreement will speed up the approval process relating to Transfer Pricing issues. Under the “Roll Back” provisions, APA entered into for future years may be applied to international transactions undertaken in previous four years in specified circumstances thereby facilitating faster resolution of pending Transfer Pricing issues between tax authorities and companies.

**Telecommunication**

**Proposals**

- Proposal to launch pan-India programme – ‘Digital India’, that will provide broadband connectivity and other Information Technology (IT) facilities at village level.
- To impose basic customs duty at 10% on specified telecommunication products that are outside the purview of the Information Technology Agreement.
- The BE of non-tax revenues from communication services for 2014-15 stands at Rs. 455 billion. The RE for 2013-14 stands at Rs. 408 billion which is same as the BE for 2013-14.

**Impact - Positive**

The broadband access has been a key focus area for GoI and it expects broadband to play a key role in achieving its objectives of financial inclusion, e-health initiatives, greater opportunities for education and entrepreneurism, and improved access to government services for people in remote areas. As a thrust towards the same the Government plans to

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\(^1\) An APA is a contract, between a taxpayer and tax authority specifying the pricing method that the taxpayer will apply to its related-company transactions.
launch ‘Digital India’ which will bring broadband connectivity and other IT facilities to village level. This is expected to provide opportunities for telecom operators (telcos) to increase their coverage and grow data centric revenues. Apart from increased penetration, the proposal to impose basic customs duty of 10% on specified telecommunication products is likely to boost domestic manufacturing.

GoI expects to raise Rs. 455 billion in 2014-15 BE from communication services, which include receipts from spectrum sale, licence fees and spectrum charges (including one time spectrum charges). This represents growth of 11% over the RE for 2013-14. The growth is expected to be driven by increase in industry revenues (resulting in higher license fee and spectrum charges) and future spectrum auctions.

**Banking and Financial Services**

**Proposals**

- Banks will be permitted to raise long term funds for lending to infrastructure sector with minimum regulatory pre-emption such as CRR, SLR and priority sector lending.
- Increase in tax rate on long term capital gains from 10% to 20% on transfer of units of mutual funds (other than equity oriented funds) and increase in the period of holding in respect of such units from 12 to 36 months.
- As per budget speech, public sector banks (PSBs) would need common equity capital of Rs 2.4 trillion over the period of FY2015-FY2018 to meet the Basel III norms. However, no significant roadmap given to achieve the same.
- Bank’s effective lending yields, under the interest subvention scheme for short term crop loans for loans to farmers retained at 9%.
- The Government has set a fiscal deficit of 4.1% of GDP for current financial year.
- Increase in deduction limit on account of interest on loan in respect of self occupied house property from Rs. 150,000 to Rs. 200,000.
- Increase in investment limit under section 80C of the Income Tax Act from Rs. 100,000 to Rs. 150,000.
- Allocation to Rural Housing Fund in 2014-15, increased from Rs. 60 billion to Rs. 80 billion.
- Additional allocation of Rs. 40 Rs. 150,000 to NHB to incentivize development of low cost affordable housing projects.

**Impact-Positive**

Permission to banks to raise long term funds with minimum regulatory pre-emption such as CRR, SLR and priority sector lending would reduce effective cost for the banks while raising funds for on lending to infrastructure sector as well as would be positive for their liquidity profile specifically in light of stringent norms on liquidity coverage ratio and net stable funding ratio under Basel III norms. The availability of long term funds at cheaper rates could also improve banks’ appetite for lending to infrastructure sector. Furthermore, this could improve volumes in Indian bond market.

Increase in tax rate as well as holding period for long term capital gains in respect of debt mutual funds could switch some of savings from mutual funds to bank deposits and could improve banks’ deposits growth rate.
The lower fiscal deficit vs. expectation for current financial year and expected moderation in fiscal deficit over the next two years could lead to decline in yields for government securities which in turn could offer higher treasury gains to banks.

In ICRA’s estimate, PSBs would need common equity capital of Rs 2.7-3.0 trillion during FY2015-FY2019 of which around 70-80% could be raised from public while maintaining GOI minimum ownership at 51% in PSBs and balance 20-30% (Rs 0.6-0.9 trillion) would needed to be infused by GOI through annual budgetary allocation. While minimum capital infusion requirement for FY2015-FY2019 from GOI does not appear a big challenge given their annual capital allocation of Rs 100-150 billion, however, such a large capital raising from public would require strong investor appetite for PSBs, absence of same would increase PSBs requirement for GOI recapitalisation. Moreover, in ICRA’s estimate PSBs would need to raise capital in the form of additional tier I capital instruments of Rs 1.4-1.5 trillion during FY2015-FY2019, lack of investor appetite for same could increase PSBs common equity capital requirement. The government neither has increased the annual allocation for recapitalisation of PSBs (Rs 112 billion allocated in 2014-15 interim budget) nor has given any clear road map on holding company or any other structure to enable PSBs to raise such large amount of capital.

Bank’s effective lending yields, under the interest subvention scheme for short term crop loans for loans to farmers retained at 9% which remains well below their base rate as well as remains a drag on banks’ overall profitability given higher NPAs and also higher operating cost while lending to the agriculture sector.

Increased tax incentives (on account of both higher tax exemption on interest on home loans for self occupied properties and increased limits under section 80 C which includes principal repayment of home loans) could lead to improved affordability for borrowers which could lead to some increase in home loan demand.

Increased fund availability with NHB at competitive rates for on lending to HFCs especially those HFCs which are focused on rural housing and affordable housing segment. However owing to the interest spread caps (2.5-2.75%) and implementation issues for selection of borrowers, the attractiveness of these schemes has reduced. In 2013-14 out of a total allocation of Rs. 80 billion, NHB was able to disburse about 55% of the allocated amounts. In ICRA’s estimate, the established HFCs could benefit and report reasonable returns at the prescribed spreads. However, newer HFCs catering to the low ticket affordable housing segments typically operate at relatively higher expense levels (~4-5% in relation to average assets) and thus would require a spread of at least 6-7% to be able to report reasonable returns. Thus NHB may have to expand the interest spread caps under these schemes to increase the demand for borrowings under these funds.

Insurance

Proposals

- Composite cap of FDI in Insurance raised from 26% to 49% through the Foreign Investment Promotion Board (FIPB) route.
- Full Indian management and control.
- Proposal to take up pending Insurance Bill.

Impact - Positive

On expected lines, the composite cap on FDI in insurance has been increased from 26% to 49% through the FIPB route. The hike in FDI will help the players to raise capital as well as attract more foreign players to enter the Indian insurance market which remains an underpenetrated market. The penetration reduced to 3.2% in 2012 for Life segment from 4.6% in 2009 and remains even lower at 0.8% for non-life segments in 2012. The Insurance Bill, which has been pending from 2008, if passed during the current year could bring in more reforms and aid in increasing the performance and penetration levels. While the General Insurance sector would require capital of Rs 75-175 billion over the next five year with higher
requirement from the private sector, the Life Insurance companies are well capitalised as on date on the back of improved profitability and moderation in growth and accordingly would require capital only as the growth picks up.
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