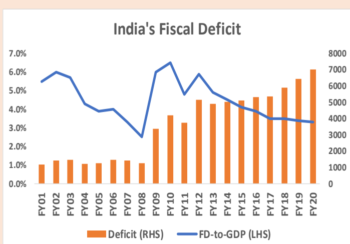
Modi 2.0's first Union Budget

July 2019

Our View

Nirmala Sitharaman, newly appointed Finance Minister for India, delivered the Union Budget for FY20 on Friday, July 5th. The key messages in the budget was the need for capital for India's growth, whilst maintaining fiscal prudence. Equity markets were looking for greater fiscal stimulus to drive growth, however it appears the Government is willing to allow monetary policy to take the driver's seat for now.

We expect that the equity market impact will be benign to weak in the short-term, given high expectations on boosting economic growth. The agenda of the Budget was very much directed towards a 10-year plan to transform India. Economic recovery is largely being dealt with by improvement of the banking system, liberalisation and monetary policy. **We remain cautious in terms of our view on the market, with upcoming 1Q20 earnings likely to provide the next trigger and greater clarity on market direction in the short-term.**



1. **Budget deficit target is 3.3% of GDP for FY20**
2. **GDP Growth target is 7.0% for FY20**
3. **Significant disinvestment target**
4. **Tax collection targets scaled back**

Fiscal Prudence + Capital Allocation

The Government continued to remain vigilant on fiscal prudence when many had called for utilising expenditure to re-ignite a weaker economy (March Quarter GDP growth was 5.8% vs average of 7% over the past 20 years). The fiscal deficit target was set to 3.3% (FY20), against last year's 3.4%, with GDP growth forecast at 7.0% for FY20.

Expenditure is budgeted to grow by 20.5%, with revenue set to grow by 25.0%. Revenue projections were boosted by enhancing non-tax projections and disinvestment (A$22bn in FY20).

The budget focused on striking a balance between welfare and growth by seeking to attract capital, while continuing to look after lower socio-economic parts of society.

Measures were put in place which recognise that the cost and availability of capital are constraints for India's growth. Disinvestment targets have been increased, raising foreign shareholding limits, government borrowing in foreign currencies, legacy dispute resolutions and liberalisation of certain sectors (aviation, insurance, media) are all likely to provide liquidity and capital to a country requiring a significant rise in the level of private investment.

1) Scaling Back Tax Projections

The Government has pruned back expectation of GST collections for FY20, given lower achievement relative to forecast in FY19. Projections have been pulled back by A$21bn for the GST, which leads to lower expectation on tax revenue of 9.5% growth vs 13.5% forecast earlier. There may be some downside to tax projections overall if GDP growth doesn't come in at expectations, given a potential global slow down.

Extra taxes were levied on the wealthy in India, with taxes rising 3% for those earning above US$300k and 7% for those above US$725k. Corporate taxes were cut to 25% firms (from 30%) with turnover less than US58m – that's 99.3% of firms.

2) A more supportive financial system to unlock private investment

A further A$15bn was set aside for injection into state-owned banks. This may equip funding required for consolidation of weaker banks and to push credit growth to the infrastructure sector. It may also take heed of more surprises on the credit-loss front. The liquidity at Banks is now quite strong and it's a question of how to push this through to the real economy. Additionally, the Budget provided a lifeline via state owned banks buying pooled assets worth A$21bn of highly rated companies, which eases liquidity concerns.

The RBI is to take on a greater role in supervision of NBFC's and Housing Finance companies. The RBI is therefore likely to take bolder steps to resolve solvency issues which previously existed. The Finance Minister pointed out progress made on commercial bank recovery as a result of insolvency laws which has resulted in lower provisioning and an improving financial system.

3) Infrastructure spending of US$1.5tn over next 5 years

Whilst the Government had reiterated significant spending on infrastructure in the budget, there was not much detail of this for FY20. It is likely that infrastructure may be more focused on specific areas to unlock bottlenecks. One of the key areas being focused on is urbanization and its efficiency. Spending is directed on alleviating cluster cities and allowing for a greater spread. The key to this remains infrastructure spend on railways, roads and ports as well as improving internet penetration.

- Improving railway infrastructure / modernizing railway stations (A$103bn, 2018-2030)
- Building 125,000 kms of roads (A$17bn, 2019-2024)
- Entering aircraft leasing and financing to increase self-reliance and create jobs
- Blueprint for gas and water grids, information highways and regional airports
- Building of world class educational institutions to foster improving education

4) Focus on clean energy and livelihoods

- Favourable policies for MSME's of India in terms of interest rate subsidies and lower taxes in place. A platform will also be created to file bills and make payments in a timely manner

- The Government will build 1.5m homes for the rural poor, and provide each one with a toilet, clean cooking gas and electricity

- A 3,000 Indian rupee (A$63) a month pension for informal workers such as farm labourers or builders, expanded to include 30 million small retail businesses

- Income tax requirements have also been withdrawn for those earning less than 500,000 Indian rupees ($7,288) annually.

- Reaffirmed its commitment to providing piped water to every home by 2024

- Under the Faster Adoption of Electric Vehicles-II scheme, the Government will spend heavily over the next three years to ensure that Indians' growing demand for owning their own car will increasingly be met with an electric version.

5) A boost for rural and low-cost housing

- Proposed that several land parcels held by Central Government, States would be used to build large public infrastructure and affordable housing

- Streamline highly un-organised Indian rental market, estimated A$29bn as per IMF

- Under the 'Housing for All by 2022' mission, the Government aims to build 20m houses

- Interest deduction up to A$7,000 for affordable housing priced below A$90,000

- By 2022, ensure that every rural family has electricity and facilities for clean cooking

- Schemes for Roads, Rural employment, Farmer-Producer organisations to improve efficiency and income for farmers and the broader rural population

- Promote digital literacy across rural India. Bharat Net takes high speed internet to rural areas