BUDGET

2017-18

Remarkably well-balanced

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Union Budget 2017-18

Remarkably well-balanced

1 February 2017

INDIA STRATEGY | Post Budget Review

Amid fears of wavering on the path of fiscal consolidation in the aftermath of disruptive demonetisation, the NDA government delivered a very pleasant surprise in a remarkable, well-balanced, and prudent Union Budget for fiscal 2018. It has managed to juggle the multiple objectives of rural/infrastructure spending, fiscal prudence, widening of the tax base, and reviving economic growth. The Budget's three-point agenda (TEC – Transform, Energize, and Clean) was largely in line with our expected themes of job creation, rural spending, digitisation, and GST. While the budget delivered on several expectations, lack of visibility on reduction in corporate taxes and lower-than-expected recapitalisation of banks curbed the investors' delight a bit – but overall, the budget was a welcome relief.

Our key themes from the budget of fiscal 2018 are as follows:

Fiscal consolidation and economic growth: The government pegged the fiscal deficit at 3.2% of GDP (in line with our estimates), while citing the need for higher public investments against a backdrop of sluggish private sector investment and slow global growth. We expect this target to be achieved (in line with the norm) with a widening tax base, and view the uptick in infrastructure spending by 11% yoy as positive because execution in FY17 was better than expected. Broadly, we like the government's push towards fiscal prudence via quality spending. Net borrowing is restricted to Rs. 3.5tn (from Rs 4.25tn in FY17) and revenue deficit is lower as well at 1.9% (from 2.3% in FY17).

Rural and housing to emerge as growth drivers: The NDA government reinforced its rural and agriculture focus with a target of doubling farm income in the next five years. It raised total allocation to agriculture and allied sectors by 24% yoy to Rs 1.87tn. Allocation to rural-focused schemes like MGNREGA (highest ever allocation of Rs 480bn) and crop insurance (up 64%) and irrigation schemes rose significantly. Housing for all by 2022 has been at core of the budget – with a focus on affordable housing to overcome the slow private capex. Increased allocation of Rs 230bn under PMAY, higher NHB refinance of Rs 200bn, and other fiscal incentives, indicate strong government thrust on the sector. As housing is a key job creator, it can trigger demand revival and translate into higher GFCF – which is a much-needed for sustainable GDP growth.

Many hits, some misses: Banks saw only limited recapitalisation (Rs 100bn), but abolishment of the FIPB and further liberalisation of the FDI policy is likely to be taken positively by the street. In addition, the proposed listing of Railways' PSEs (IRCTC, IRFC, and IRCON), resurgence in real estate activity (on the provisions mentioned above), and a lending target of Rs 2.4tn under the Pradhan Mantri Mudra Yojana, should bode well for the broader financial sector. The incentives given for digitisation and the disincentives for cash transactions will help in better retention of bank deposits, which will bring down the market interest rates further.

Key themes and stock picks from the budget:

- **Key budgetary beneficiaries:** Banks, housing, cement, and infra companies, sectors/companies catering to the rural segment
- **Our key ideas:** ITC, DCB Bank, Bharat Financial, Repco, IRB Infra, Ashoka Buildcon, Finolex Cables, Va Tech Wabag, KEC, India Cement, Ultratech and Escorts.

Sectoral Impact

POSITIVE

Agri Inputs
Automobiles
BFSI
Consumer
Capital Goods & Power
Cement
Infrastructure
Midcap
NBFC
Oil & Gas

NEUTRAL

Metals
Pharmaceuticals
Specialty Chemicals
Telecom

India Research Team

FY18 Macro Budget Review

Fiscally prudent, policy continuity – act balanced

As expected, the fourth budget of the NDA government focused on fiscal prudence, rural development, income tax rebates, and usual spending trends – unlikely to significantly alter the growth path for FY18. However, the core of the budget continued to be about widening the tax base and compliance – which is a significant medium-term positive that will support quality spending for the future. A continued thrust on the rural sector (housing, rural development) and incremental income tax rebates should be consumption positive. Investment growth of 11% is directionally stable, but is not likely to push up the capex cycle as both state capex (due to 7th PC implementation) and private-sector capex will be weak. Sectors that attracted higher allocations are energy, health, rural development, social welfare, and transport. Few changes were made in excise and service tax rates ahead of the GST since it is likely to be implemented in 3-6 months.

More hits than misses – structural changes underway: The government has projected a fiscal deficit of 3.2% of GDP for FY18 vs. 3.5% in FY17. While we expect the FY18 target to be achieved (in line with the norm), this is likely to come at the cost of lower capital expenditure, as we see downside risks to the revenue estimates primarily from income-tax collection and disinvestment. The government has not accounted for any gains from a drop in currency liability post demonetisation. The earlier method of classifying expenditure under plan and non-plan has been rightly (and as expected) replaced with scheme and non-scheme expenditure. Also, railway has been clubbed with the union budget on strong fundamental grounds. We are impressed with the government's continuing push towards curbing black money – reflected in announcements such as a limit of Rs 300,000 on cash transactions and cash funding of political parties being reduced to Rs 2,000 from Rs 20,000 earlier.

Tax-GDP ratio is stable and elevated at 11.3%: Gross tax revenue is likely to rise by 12.2% vs. 17% last year – lower growth as petroleum excise-duty benefit are there in the FY17 base and service tax rate was left unchanged. While FY18 tax-GDP ratio is stable at 11.3%, we see downside risk as FY17 tax collections received a fillip from one-off gains like IDS, demonetisation, etc. Before FY17, tax-GDP ratio was at 10.7% and below. We find direct tax growth assumptions aggressive at 25% vs. already elevated/one-off growth levels of 22.8% last year. While the government is focused on increasing tax compliance, we expect benefits to play out only in the long run – so we find income-tax targets aggressive. Indirect tax growth at 9% is reasonable vs. 22% in FY17. States' share in taxes is assumed at 35%.

Disinvestment, dividend, telecom auctions: Disinvestment receipts for FY18 are set at a sharply higher Rs 725bn (Rs 465bn as disinvestment receipts, Rs 150bn as strategic disinvestment, and Rs 110bn from listing of insurance companies). For FY17, the government revised disinvestment to Rs 455bn vs. BE of Rs 565bn (above our expectation). While the government is optimistic on achieving its target, past trends indicate downside risks. Dividend income from PSEs is set at Rs 675bnbn (vs. Rs 771bn last year) and from RBI at Rs 749bn (vs. 762bn last year). For FY17, the government received Rs 294bn in higher-than-budgeted dividend. Funds from telecom auctions are assumed to fall to Rs 443bn vs. Rs 787bn last year (BE was at Rs 990bn).

Capital expenditure to rise faster than revenue: Total expenditure growth for FY18 is estimated at 6.6% vs. 12.5% last year. Revenue expenditure growth is estimated at a muted 6% vs. 12.8% last year due to an elevated base. While capital spending growth at 10.7% vs. 10.6% last year is not sufficient, it is considered reasonable considering the government's focus on fiscal consolidation. Scheme expenditure growth is at 8.6% vs. 20% last year and non-scheme at 5% vs. 7.4% last year.

Sectors that attracted higher allocations are energy, health, rural development, social welfare, and transport. While spending rise in agriculture and urban development is muted vs. in last few years, the base has expanded. MNREGA allocations have been increased to Rs 480bn vs. Rs 475bn in FY17RE and Rs 385bn in FY17BE. Subsidies will marginally rise to Rs 2.7tn (1.6% of GDP), led by higher food subsidy.

Lower government borrowing: Gross government borrowing for FY18 is estimated at Rs 6.05tn vs. Rs 6.22tn last year while net government borrowing is estimated at Rs 3.48tn vs. Rs 3.47tn last year, due to higher security buyback by the RBI at Rs 750bn vs. Rs 595bn. Bonds were largely unchanged after the budget announcement as gross and net market borrowing are closer to last year as well as **expectations. A rate cut from the RBI in the forthcoming monetary policy will be positive for bonds** – we anticipate a 25-50bps cut and fiscal consolidation (along with comfortable inflation) to offer an additional push towards a rate cut.

Central government fiscal account

	Rs Bn				% of GDP				yoy growth (%)		
	FY16	FY17BE	FY17RE	FY18BE	FY16	FY17BE	FY17RE	FY18BE	FY17BE	FY17RE	FY18BE
Nominal GDP	**135762**	**150650**	**150754**	**168475**					**11.0**	**11.0**	**11.8**
Revenue receipts	**11950**	**13770**	**14236**	**15158**	**8.8**	**9.1**	**9.4**	**9.0**	**15.2**	**19.1**	**6.5**
Tax (net)	9438	10541	10888	12270	7.0	7.0	7.2	7.3	11.7	15.4	12.7
Non - tax	2513	3229	3348	2888	1.9	2.1	2.2	1.7	28.5	33.2	-13.7
Capital receipts	**5958**	**6010**	**5908**	**6310**	**4.4**	**4.0**	**3.9**	**3.7**	**0.9**	**-0.8**	**6.8**
Recovery of loans	208	106	111	119	0.2	0.1	0.1	0.1	-49.0	-46.9	7.8
Other reciepts (mainly PSU disinvestment)	421	565	455	725	0.3	0.4	0.3	0.4	34.1	8.0	59.3
Borrowings and other liabilities	5328	5339	5343	5465	3.9	3.5	3.5	3.2	0.2	0.3	2.3
Total receipts	**17908**	**19781**	**20144**	**21467**	**13.2**	**13.1**	**13.4**	**12.7**	**10.5**	**12.5**	**6.6**
Scheme Expenditure	**7251**	**8020**	**8698**	**9451**	**5.3**	**5.3**	**5.8**	**5.6**	**10.6**	**20.0**	**8.6**
Revenue A/c	5456	6019	6315	6741	4.0	4.0	4.2	4.0	10.3	15.7	6.7
Capital A/c	1795	2001	2383	2710	1.3	1.3	1.6	1.6	11.5	32.8	13.7
Non-Scheme Expenditure	**10657**	**11761**	**11446**	**12017**	**7.8**	**7.8**	**7.6**	**7.1**	**10.4**	**7.4**	**5.0**
Revenue A/c	9921	11291	11030	11629	7.3	7.5	7.3	6.9	13.8	11.2	5.4
Interest payments	4417	4927	4831	5231	3.3	3.3	3.2	3.1	11.5	9.4	8.3
Capital A/c	735	470	415	388	0.5	0.3	0.3	0.2	-36.1	-43.5	-6.6
Total revenue expenditure	**15378**	**17310**	**17346**	**18369**	**11.3**	**11.5**	**11.5**	**10.9**	**12.6**	**12.8**	**5.9**
Total capital expenditure	**2530**	**2470**	**2798**	**3098**	**1.9**	**1.6**	**1.9**	**1.8**	**-2.4**	**10.6**	**10.7**
Total expenditure	**17908**	**19781**	**20144**	**21467**	**13.2**	**13.1**	**13.4**	**12.7**	**10.5**	**12.5**	**6.6**
Fiscal deficit	**5328**	**5339**	**5343**	**5465**	**3.9**	**3.5**	**3.5**	**3.2**	**0.2**	**0.3**	**2.3**
Revenue deficit	**3427**	**3540**	**3110**	**3212**	**2.5**	**2.3**	**2.1**	**1.9**	**3.3**	**-9.3**	**3.3**
Effective Revenue deficit	**2110**	**1872**	**1395**	**1258**	**1.6**	**1.2**	**0.9**	**0.7**	**-11.3**	**-33.9**	**-9.8**
Primary deficit	**911**	**412**	**512**	**235**	**0.7**	**0.3**	**0.3**	**0.1**	**-54.8**	**-43.8**	**-54.2**
Gross Market Borrowing	**6233**	**6000**	**6225**	**6050**	**4.6**	**4.0**	**4.1**	**3.6**	**-3.7**	**-0.1**	**-2.8**
Net Market Borrowing	**4041**	**4252**	**3472**	**3482**	**3.0**	**2.8**	**2.3**	**2.1**	**5.2**	**-14.1**	**0.3**

Source: Budget Document, PhillipCapital India Research

Tax components

	Rs Bn				YoY Growth				% of GDP			
	FY16	FY17BE	FY17RE	FY18BE	FY16	FY17BE	FY17RE	FY18BE	FY16	FY17BE	FY17RE	FY18BE
Gross Tax Revenue	**14556**	**16309**	**17032**	**19116**	**16.9%**	**12.0%**	**17.0%**	**12.2%**	**10.7%**	**10.8%**	**11.3%**	**11.3%**
Direct Tax	**7419**	**8471**	**8471**	**9800**	**6.7%**	**14.2%**	**14.2%**	**15.7%**	**5.5%**	**5.6%**	**5.6%**	**5.8%**
Personal Income Tax	2876	3532	3532	4413	8.2%	22.8%	22.8%	24.9%	2.1%	2.3%	2.3%	2.6%
Corporation Tax	4532	4939	4939	5387	5.7%	9.0%	9.0%	9.1%	3.3%	3.3%	3.3%	3.2%
Indirect tax	**7098**	**7797**	**8519**	**9269**	**30.0%**	**9.8%**	**20.0%**	**8.8%**	**5.2%**	**5.2%**	**5.7%**	**5.5%**
Excise Duty	2881	3187	3874	4069	51.7%	10.6%	34.5%	5.0%	2.1%	2.1%	2.6%	2.4%
Customs Duty	2103	2300	2170	2450	11.9%	9.3%	3.2%	12.9%	1.5%	1.5%	1.4%	1.5%
Service Tax	2114	2310	2475	2750	25.9%	9.3%	17.1%	11.1%	1.6%	1.5%	1.6%	1.6%

Source: Budget Document, PhillipCapital India Research

Outlay on major schemes

	Rs Bn				yoy growth (%)		
	FY16	FY17BE	FY17RE	FY18BE	FY17BE	FY17RE	FY18BE
National Social Assistance prog	8616	9500	9500	9500	10.3	10.3	0.0
MNREGA	37341	38500	47499	48000	3.1	27.2	1.1
Green Revolution	9777	12560	10360	13741	28.5	6.0	32.6
Pradhan Mantri Krishi Sinchai Yojana	7781	5767	5189	7377	-25.9	-33.3	42.2
Pradhan Mantri Gram Sadak Yojna	18290	19000	19000	19000	3.9	3.9	0.0
Pradhan Mantri Awas Yojna	11603	20075	20936	29043	73.0	80.4	38.7
PMAY: Rural	10116	15000	16000	23000	48.3	58.2	43.8
PMAY: Urban	1487	5075	4936	6043	241.3	231.9	22.4
National Rural Drinking Water Mission	4370	5000	6000	6050	14.4	37.3	0.8
Swachh Bharat Mission (SBM)	7469	11300	12800	16248	51.3	71.4	26.9
SBM: Rural	6703	9000	10500	13948	34.3	56.6	32.8
SBM: Urban	766	2300	2300	2300	200.3	200.3	0.0
National Health Mission (NHM)	20213	20762	22598	27131	2.7	11.8	20.1
National Rural Health Mission	18254	18087	19462	21189	-0.9	6.6	8.9
National Urban Health Mission	717	950	575	752	32.5	-19.8	30.8
National Education Mission	27066	28330	28251	29556	4.7	4.4	4.6
National Programme of Mid day meal	9145	9700	9700	10000	6.1	6.1	3.1
Development Services	16835	16260	16580	20755	-3.4	-1.5	25.2
National Livelihood Mission-Ajeevika	2783	3325	3334	4849	19.5	19.8	45.4
National Rural Livelihood Mission	2514	3000	3000	4500	19.3	19.3	50.0
National Urban Livelihood Mission	269	325	334	349	20.8	24.2	4.5
Jobs and Skill Development	1177	2900	2450	4089	146.4	108.2	66.9
Urban Rejuvenation Mission : AMRUT	7296	9559	9000	9000	31.0	23.4	0.0
Modernisation of Police Forces	1581	1685	2235	2022	6.6	41.4	-9.5
Bharatnet	...	...	6000	10000			66.7
MRTS and Metro Projects	9300	10000	15700	18000	7.5	68.8	14.6
Interest subsidy for credit to farmers	13000	15000	13619	15000	15.4	4.8	10.1
Namami Gange-National Ganga Plan	1000	2150	1441	2250	115.0	44.1	56.1
LPG connection to poor households	...	2000	2500	2500			0.0
National SocialAssistance Progamme	8616	9500	9500	9500	10.3	10.3	0.0
Crop Insurance Scheme	2983	5500	13240	9000	84.4	343.8	-32.0
Duty Drawback Scheme	1189	1200	1200	1100	0.9	0.9	-8.3
Interest Equalisation Scheme	1100	1000	1000	1100	-9.1	-9.1	10.0
India Post Payments Bank	...	150	300	500			66.7
Price Stabilisation Fund	...	900	3400	3500			2.9
Recapitalization of PSBs	25000	25000	25000	10000	0.0	0.0	-60.0
Police Infrastructure	3739	3265	3183	4447	-12.7	-14.9	39.7
Interest Subsidy for guarantee funds	1960	1950	1850	1950	-0.5	-5.6	5.4
Credit Support Programme	71	50	2018	3002	-29.6	2742.3	48.8
Prime Minister Employment Gen Prog (PMEGP)	1281	1139	1120	1024	-11.1	-12.6	-8.6
Gram Jyoti Yojna	4500	3000	3350	4814	-33.3	-25.6	43.7
Integrated Power Dev Scheme	1002	5500	4524	5821	448.9	351.5	28.7
Construcution of New Lines	15828	13463	15160	13333	-14.9	-4.2	-12.1
Road Safety Works	2603	2998	3745	5217	15.2	43.9	39.3

Source: Budget Document, PhillipCapital India Research

GoI expenditure break-up

	Rs Bn				YoY Growth			% of total expenditure			
	FY16	FY17BE	FY17RE	FY18BE	FY17BE	FY17RE	FY18BE	FY16	FY17BE	FY17RE	FY18BE
Pension	968	1234	1282	1312	27.5	32.4	2.4	5.4	6.2	6.4	6.1
Defence	2259	2491	2480	2624	10.3	9.8	5.8	12.6	12.6	12.3	12.2
Subsidy								0.0	0.0	0.0	0.0
Fertiliser	724	700	700	700	-3.3	-3.3	0.0	4.0	3.5	3.5	3.3
Food	1394	1348	1352	1453	-3.3	-3.0	7.5	7.8	6.8	6.7	6.8
Petroleum	300	290	275	250	-3.3	-8.2	-9.2	1.7	1.5	1.4	1.2
Agriculture and Allied Activities	237	504	538	570	112.9	127.1	5.9	1.3	2.5	2.7	2.7
Commerce and Industry	162	181	229	247	11.2	41.2	7.5	0.9	0.9	1.1	1.1
Development of North East	20	24	25	27	22.3	27.0	6.3	0.1	0.1	0.1	0.1
Education	672	724	736	797	7.7	9.5	8.3	3.8	3.7	3.7	3.7
Energy	211	295	301	367	39.6	42.3	22.1	1.2	1.5	1.5	1.7
External Affairs	145	147	134	148	1.0	-7.5	10.2	0.8	0.7	0.7	0.7
Finance	712	486	435	295	-31.7	-39.0	-32.0	4.0	2.5	2.2	1.4
Health	341	384	399	489	12.6	16.8	22.6	1.9	1.9	2.0	2.3
Home Affairs	678	752	788	838	10.9	16.2	6.4	3.8	3.8	3.9	3.9
Interest	4417	4927	4831	5231	11.5	9.4	8.3	24.7	24.9	24.0	24.4
IT and Telecom	151	128	185	208	-15.0	23.0	12.1	0.8	0.6	0.9	1.0
Others	460	584	615	677	26.9	33.7	10.1	2.6	3.0	3.1	3.2
Planning and Statistics	60	50	50	50	-15.3	-15.4	0.1	0.3	0.3	0.3	0.2
Rural Development	902	1025	1149	1286	13.6	27.4	11.8	5.0	5.2	5.7	6.0
Scientific Departments	174	195	201	223	12.1	15.1	11.1	1.0	1.0	1.0	1.0
Social Welfare	317	334	336	394	5.4	6.2	17.0	1.8	1.7	1.7	1.8
Tax Administration	260	223	221	127	-14.4	-15.1	-42.5	1.5	1.1	1.1	0.6
Transfer to States	1148	1255	1334	1371	9.3	16.2	2.8	6.4	6.3	6.6	6.4
Transport	874	1071	1035	1244	22.5	18.4	20.2	4.9	5.4	5.1	5.8
Union Territories	118	128	134	134	7.8	12.7	0.1	0.7	0.6	0.7	0.6
Urban Development	202	299	378	406	48.3	87.5	7.4	1.1	1.5	1.9	1.9
Grand Total	**17908**	**19781**	**20144**	**21467**	**10.5**	**12.5**	**6.6**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Budget Document, PhillipCapital India Research

Agricultural – Positive

WINNERS: Input players in seed and pesticides. Fertilizers to benefit from better cash flow. Kaveri, PI, Rallis, Zuari, Chambal, and Coromandel International

LOSERS: None

Higher budgetary allocation will lead to sector growth and prosperity among farmers. The expected 4.1% growth in agriculture, with an increased focus on crop insurance and irrigation, is positive. Though there is no increase in total fertiliser subsidy, lower raw material costs will help reduce arrears and working capital for fertiliser companies.

Budget Proposals	PhillipCapital Perspective
• Total fertiliser subsidy at Rs 700bn same as last year. (urea Rs 498bn + nutrient-based Rs 202bn). Agri credit target is at a peak of Rs 10tn	• Budgetary support will trickle down to small and marginal farmers, mitigate risk, and improve affordability for high-yielding variety seeds, fertilisers, crop-protection chemicals, and irrigation equipment
• *Fasal Bima Yojana:* Allocation of Rs 90bn, up 64% from budgeted Rs 55bn in FY17. The coverage of scheme will be increased to 40%/50% of cropped area in FY18/19 from 30% in FY17	• Should increase the risk-taking appetite for farmers and lead to more spending on agri inputs and fertilisers
• Soil health card gaining momentum. Government will set up new mini labs in Krishi Vigyan Kendras (KVKs) and ensure 100% coverage of all 648 KVKs in the country. In addition, 1,000 mini labs will be set up by qualified local entrepreneurs. Government will provide credit-linked subsidy to these entrepreneurs.	• Help to shift to proper crop patterns and yield improvement for farmers
• Irrigation: Allocation to the Pradhan Mantri Krishi Sinchai Yojana (PMKSY) aggregated across three ministries increased by 28% to Rs 73.7bn • A Long Term Irrigation Fund has already been set up in NABARD. Government has announced an addition of Rs 200bn to its corpus, taking the total corpus to Rs 400bn. A dedicated Micro Irrigation Fund will be set up in NABARD to achieve the goal, 'per drop more crop' with an initial corpus of Rs 50bn.	• Should reduce the dependence on rain and lead to more sustainable income for farmers
• The coverage of National Agricultural Market (e-NAM) will be expanded to 585 APMCs from the current 250 markets. Assistance up to a ceiling of Rs 7.5mn will be provided to every e-NAM market for establishment of cleaning, grading, and packaging facilities. This will lead to value addition of farmers' produce.	• For the post-harvest phase, the government has taken steps to enable farmers to get better prices for their produce in the markets. Transparency in agri trading and integration of value chain. Better price for farmers for their output.

Automobiles – Marginal positive

WINNERS: Escorts, Hero Motocorp, M&M

LOSERS: None

Budget Proposals	PhillipCapital Perspective
• Boost to the rural sector	• Positive for Escorts, MSIL, Hero Motocorp and M&M. Escorts has ~80% revenue exposure to rural markets, M&M and Hero Moto both have c.50%. Maruti generates ~35% of its revenues from the rural segment.
• Infrastructure focus	• Strong focus on infrastructure will boost MHCV sales. Ashok Leyland to be a key beneficiary

BFSI – Positive

WINNERS: DCB Bank, Bharat Financial, Repco Home Finance, Gruh Finance

LOSERS: None

This budget is positive for the BFSI sector

Budget Proposals	PhillipCapital Perspective
• Recapitalisation of PSBs pegged at Rs 100bn in FY18, with assurance of an increase if required	• Allocation in line with 'Indradhanush'. Some disappointment, as expectations were high • **-/+PSBs**
• Increase in allowable provision for non-performing asset to 8.5% of total income u/s 36(1)(viia) from 7.5%.	• Marginal reduction in tax liability for banks reeling under NPA pressure. **+ve ICICIBC, AXSB,PSBs**
• Listing and trading of security receipts issued by a securitisation company or a ARC under the SARFAESI Act will be permitted in SEBI-registered stock exchanges	• This is positive for banks as it provides liquidity and price discovery of such instruments and exit opportunities for banks
• Increased allocation under MUDRA loans to Rs 2.44tn	• Positive for micro credit and micro finance due to increased allocation. **+BHARATFIN, UJJIVAN, EQUITAS**
• Corporate income tax for SMEs upto Rs 500mn turnover has been reduced to 25% from 30%	• Positive for SMEs as the segment has been under pressure after demonetisation. This will improve cash flow and help the segment to overcome GST implementation challenges. **+DCBB, Federal bank, CUB, KVB**
Housing sector • National Housing Bank to refinance individual housing loans of about Rs 200bn in FY18 • Infrastructure status for affordable housing • Allocation under PMAY–Gramin Rs230bn in FY18 (Rs 150bn in FY17). • Reduced holding period (to be considered capital gains) for immovable property to two years from three. • Notional rental income on stock in trade for builder to be given one-year breathing space	• Increased allocation for refinance by NHB and infrastructure status to affordable housing to provide adequate funding for the sector • Incentive on capital gain encourages investments in the housing sector • These incentives, along with credit-linked subsidy scheme, to provide impetus to affordable housing. Positive for HFCs like **Repco, Gruh and CanFin Homes**
Thrust towards cashless transaction • No deduction shall be allowed under the section 80G for donations of any sum exceeding Rs 2,000, unless such a sum is paid by a mode other than cash. • No deduction on capital expenditure above Rs 10,000, if incurred in cash • In order to disincentivise cash transactions, it is proposed to amend the provision of section 40A of the Act to reduce the existing threshold of cash payment to a person to Rs 10,000 in a single day from Rs 20,000; shall not be allowed as deduction in computation of income from "profits and gains of business or profession". • No person shall receive an amount of Rs 300,000 or more— (a) in aggregate from a person in a day; (b) in respect of a single transaction; or (c) in respect of transactions relating to one event or occasion from a person, other than by an account payee cheque, or account payee bank draft, or use of electronic clearing system through a bank account	• The thrust on digitisation and disincentive for cash transactions supports deposit accretion. The increase in CASA after demonetisation may remain sticky if the thrust on cashless transaction remains a priority. These moves are positive for the entire banking sector in general and particularly banks like +**SBI, ICICIBC, HDFCB, AXSB,** due to the large CASA base and strong retail fee income

Capital Goods & Power – Positive

WINNERS: L&T, Va Tech Wabag, KEC International, Voltas

LOSERS: Inox Wind

Budget Proposals	PhillipCapital Perspective
• Estimated spending by central PSUs projected to decline modestly by 3% to Rs 5.03tn	• Growth in capex by railways (+8% yoy) and roads (+12% yoy) will be unable to offset lower capex in power (flat yoy) and MoPNG (-18% yoy).
• Railway capex to grow 8% yoy to Rs 1.31tn • Funding the capex will not be a challenge • Listing of railway' subsidiaries is a positive for future capex funding	• Capex to be driven by new lines and signalling. Investments in network decongestion projects and rolling stock are expected to decline. • Budgetary support is expected to increase by 19% yoy to Rs 550bn while other forms of finance are expected to remain flat yoy • Railways plans to list its three subsidiaries – IRFC, IRCTC, and IRCON – which would help government fund capex
• Capital outlay for defence (ex-construction and land) to grow modestly by 10% to Rs 763bn on a low base	• Defence outlay still out of sync with the project approvals accorded by the government (Rs 3tn). Beneficiaries: BEL, L&T, Tata Power, Astra Microwave
• Allocation to irrigation-led schemes raised by 42% yoy to Rs 74bn	• Higher capex under PMKSY and drip irrigation positive for pump companies. Beneficiaries: Kirloskar Brothers, Crompton Greaves, V-Guard, KSB
• Allocation to rural and urban electrification schemes – DDUGJY and IPDS – increased by 35% in FY18BE	• Positive for companies such as KEC International, L&T, Voltas, ABB, Schneider Electric
• Funding from the National Clean Energy Fund to Ministry of New & Renewable Energy has increased by 25% to Rs53.4bn	• 65% of the allocation is towards funding of solar projects. Positive for companies such as ABB, GE T&D, Siemens, Suzlon
• Allocation to Namami Ganga at Rs 22.5bn (+56% yoy)	• After missing its FY17 capex target, the government expects to start awarding projects under the Hybrid Annuity Model in FY18, leading to a sharp increase in fund allocation. Beneficiaries: Va Tech Wabag, L&T, ION Exchange, SPML, Ramky Infra
• No mention of continuation of Generation-Based Incentives (GBI).	• GBI was to expire in March 2017. The budget fine print makes no mention of its renewal, bringing in ambiguity for wind and solar developers. Negative in the near term for Inox Wind and Suzlon

Cement – Positive

WINNERS: All: *especially* - India Cements, Dalmia Bharat, JK Cement, JK Lakshmi Cement and UltraTech Cement.

LOSERS: None

In our opinion, this budget is the most structurally positive one for the cement sector in the last decade. Although there were no direct announcements by the Finance Minster for the cement sector, a number of his announcements will lead to increased and sustained consumption of cement

Budget proposals	PhillipCapital Perspective
• 10mn houses by 2019 for the houseless	• Implies incremental cement demand of ~75mn tonnes over the next 2-3 years
• 100% rural electrification by 1st May 2018	• Implies deeper penetration of development opportunities in rural India in the form construction of houses, roads; hence a structural positive
• Continued focus on sanitation	• Sanitation coverage in rural India is currently 60%. Budget commentary remained very positive on sanitation projects. In our recent ground checks, we found that sanitation projects are one of the key demand drivers for cement. Continued thrust on such projects will help boost cement demand
• Higher investment in Affordable Housing and Affordable Housing being granted 'Infrastructure' Status	• More cement consumption for such projects. Grant of infrastructure status means more participation on the supply side by construction companies/ contractors/ builders and faster execution of such projects
• Fostering a conducive labour environment	• Labour issues are one of the key ones in construction projects. Continuous availability of labour is frequently a problem at most sites (most labour is generally migrant). The government's focus on developing a conducive labour environment will mean labour issues being sorted out to a large extent, implying smooth execution of projects at construction sites with steady cement consumption. This will also mean the other regular labour concerns for contractors (wages, job benefits) are resolved, which will remove ameliorate labour-migration concerns
• Thrust on rail modernisation / station redevelopment projects – 25 stations to go for redevelopment	• Material cement consumption
• Introduction of Metro Rail Act / Metro Rail Policies	• Faster and structured execution of metro-rail projects implies better visibility of cement demand
• Increased investments in the roads sector / 2,000 kms of coastal roads identified for development	• More cement demand from road projects
• Airport upgradation / maintenance projects	• May imply increased cement consumption. Consumption may be even higher if upgradation work involves runways
• Amendment of the Negotiable Instruments Act, 1881	• This was one of the key demands from north India channel partners and distributors. North is a largely a cash-and-carry economy and issuing post-dated cheques is a normal practice. Trade associations in these regions

	had approached the government for these amendments (we highlighted these in our recent visit note (**Click here**) to north India). With this development, the supply chain should be more comfortable with such instruments. We found north India averse to digital wallets and the swipe machine culture given 1-2% transaction charges involved
• Change in dynamics of affordable housing – to 30/60 sq. mt. carpet from 30/60 sq. mt. built up	• Larger sizes of such houses will mean higher cement consumption
• Tax 'Notional Rent Income' for unsold inventory for builders - post one year of receiving the commencement certificate if such house remains unsold / unoccupied	• This means correction in real estate prices / rentals, implying quicker-than-anticipated (though lower) cash flows to builders. Builder will be able to execute projects faster and transparently, implying better cement demand
• Exemption of capital gains tax for people whose land is being pooled for the creation of Andhra Pradesh's capital city if the person was holding the land as on 2.6.2014	• Implies more transparent and faster execution of the capital city of Andhra Pradesh and quicker than anticipated cement demand. India Cements will be the key gainer followed by Dalmia Bharat, Ramco, and other south companies
• Reduction in holding period for considering capital gain tax to two years from three years. Change of base year for indexation to 2001 from 1981, reduces the capital-gains tax liability	• This will mean quicker decisions in the real-estate markets to buy/sell (as the holding period comes down) and will also prompt builders for faster execution of projects, implying more sustained demand of cement from real estate
• Increase in disposable income by a marginal reduction in tax rates in the Rs 250,000-500,000 tax bracket to 5% from 10%	• Sentiment booster for those within this bracket aspiring to buy new houses

FMCG – Positive

WINNERS: ITC, Emami, Dabur, Bajaj Corp, Colgate, and HUL

Budget Proposals	PhillipCapital Perspective
• Increase in excise duty on cigarettes by 6%	• ITC will be able to pass on the excise duty hike easily in FY18 and manage reasonable volume growth • We expect GST will be in the range of 30%-35% and in both the case the company will able to manage double digit EBITA growth
• Increased allocation to rural schemes such as MNREGA, Pradhan Mantri Gram Sadak Yojana, grants to panchayats, rural electrification	• Stimulus will help revive rural growth • Will benefit companies with high rural exposure – Emami, Dabur, BajajCorp, HUL and Colgate

Infrastructure – Positive

WINNERS: IRB Infra, Sadbhav Engineering, Ashoka Buildcon, NCC, PNC Infratech, KNR Construction, JKumar Infraprojects, ITD Cementation, HCC, Adani Ports

LOSERS: Ahluwalia Contracts (Minor)

Budget Proposals	PhillipCapital Perspective
Increased allocation for roads, railways, and urban development • 21% increase in budgetary allocation for roads • 23% increase for metro projects • 20% increase for railways	• The increase in allocation was along expected lines • Positive for road companies – IRB, Ashoka Buildcon, Sadbhav Engineering – and EPC companies – NCC, PNC, KNR, HCC • Positive for companies in MRTS segment – J Kumar, ITD Cementation, HCC
Increased allocation for ports and shipping • 21% increase in budgetary allocation for Sagar Mala project • 43% increase in allocation for sagar mala project	• Positive for Adani Ports & SEZ
Lower/flat allocation for Smart Cities and AMRUT • 21% decrease in budgetary allocation for Smart Cities • 3% increase in allocation for AMRUT	• Minor negative for Ahluwalia Contracts

Total Budgetary allocation

Rs bn	FY16	FY17E	FY17RE	FY18E	Increment	% Increase
Roads	469.1	579.8	524.5	649.0	124.5	21%
NHAI	230.2	196.5	149.8	238.9	89.2	45%
Urban development	184.2	245.2	325.5	342.1	16.6	7%
Smart cities etc	14.8	32.1	46.8	40.0	-6.8	-21%
AMRUT	27.0	40.8	48.8	50.0	1.2	3%
Metro projects	93.0	100.0	157.0	180.0	23.0	23%
Railways	350.1	450.0	461.6	550.0	88.5	20%
Shipping	13.2	15.3	14.5	17.7	3.2	21%
Sagar mala, ports	1.4	4.5	4.1	6.0	1.9	43%
Inland transport	3.4	4.3	3.7	3.5	-0.2	-5%
Power	77.3	122.0	104.8	138.8	34.1	28%
Aviation	41.7	25.9	34.5	27.0	-7.5	-29%

Metals – Neutral

WINNERS: None

LOSERS: None

Budget Proposals	PhillipCapital Perspective
• Export duty on laterite ore increased to 15% from nil earlier	• No impact for aluminium producers
• Customs duty on nickel scrapped, from 2.5% earlier	• Positive for stainless steel producers as the prices of nickel increased significantly in 2016
• Reduction in customs duty on certain grades of flat steel (subject to actual user condition): ○ MgO-coated cold-rolled steel to 5% from 10% ○ HR coil used in welded tubes and pipes for oil & gas to 10% from 12.5%	• No significant impact as the imported volumes are relatively low

Midcap – Positive

WINNERS: KEI Industries, Finolex Cables, Havells, V-Guard Industries, Sterlite Technologies, Somany ceramics, Kajaria, AGL, Sintex, Pennar Industries, SCI, Mercator

LOSERS: KDDL

Budget Proposals	PhillipCapital Perspective
Tempo of rural electrification maintained • Allocation for Deendayal Upadhyay Gram Jyoti Yojana (rural electrification) increased by 35% to Rs 106bn	• This allocation is in line with the government's capex and timetable. Ripple effect of electrification is already visible in the steady consumption of wires, cables, switches, lighting, fans, and appliances. Electrical companies with comprehensive portfolios that include wires and cables stand to benefit the most – KEI Industries, Finolex Cables, Havells, and V-Guard
Reduced custom duty in LED • Custom duty reduced to 5% on all LED lights or fixtures, including LED lamps and parts of LED	• This will promote more imports of LED parts (majorly LED Drivers) and help Indian manufactures (assembling units) to procure RM (LED lamp parts) at a lower rate. This move will result in further reduction in LED prices.
Increase custom duty in optical fibres • 10% increase BCD in telecommunication-grade optical fibres or optical-fibre cables	• This will help domestic manufactures compete with imported cables. Companies like Sterlite Technologies and Finolex Cables will benefit
Focus on Swachh Bharat Abhiyan, affordable housing, and other rural development schemes: • Increased allocation in Swachh Bharat Mission by 27% to Rs 162bn and in Pradhan Mantri Awas Yojna by 39% to Rs 290bn. *Building 100mn house by 2019 (for those living in kutcha houses) under PMAY – Gramin* • Affordable housing will now be given infrastructure status • Affordable housing criteria increased from 'built up' to 'carpet' area • To provide safe drinking water to over 28,000 arsenic and fluoride affected habitations in the next four years. This will be a sub mission of the National Rural Drinking Water Programme (NRDWP) • Mid-day meal in school allocation of Rs 100bn, up 3%.	• Will create demand for toilets, modern sewage systems (bath fitting), tiles and other building material products. Positive for the Indian ceramic industry - Somany Ceramics, AGL, Kajaria Ceramics, Cera and HSIL to benefit • Affordable housing, government spending on health and water along with mid-day meal is positive for prefab players like Sintex
• In solar energy, government to take up the second phase of Solar Park development for additional 20,000 MW capacity • Custom duty on solar tempered glass for use in the manufacture of solar cells/panels/modules reduced to zero from 5%. • CVD - Additional Duty of Customs on parts/raw materials for use in the manufacture of solar tempered glass for use in solar photovoltaic cells/modules, solar power generating equipment or systems, flat plate solar collector, solar photovoltaic module and panel for water pumping and other applications reduced to 6% from 12.5%	• Positive for V-guard, Pennar Industries
• The government has suggested no transaction above Rs 300,000 should be permitted in cash	Government's focus on reducing cash transactions will impact KDDL, whose ~40% revenue is in cash

NBFC – Positive

WINNERS: CIFC, MMFS, SCUF, SHTF

Budget Proposals	PhillipCapital Perspective
• Focus on enhancing expenditure in priority areas – housing, sanitation, farm, and rural sectors. Total allocation for rural, agriculture and allied sectors increased to Rs 1.87tn vs. Rs 1.69tn last year.	• Increased spend in rural regions to improve cash flow in rural geographies. Positive for MMFS, as 80% of its branches are concentrated in rural areas
• Allow systemically important NBFCs regulated by RBI and above a certain net worth to be categorised as QIBs	• To provide more investment avenues to NBFCs and bring them at par with banks and insurance companies. This will also help in strengthening the IPO market and channelize more investments
• Increased investments in the road sector. Allocation to road transport and highways increased by 24% to Rs 649bn	Increased connectivity to drive demand for more vehicles like cars and trucks. Hence, positive for vehicle financiers like SHTF, CIFC, MMFS
• Target amount sanctioned under Pradhan Mantri Mudra Yojana increased to Rs 2.44tn from Rs 1.22tn	• Positive for NBFCs, MFIs, and NBFCs – Mudra provides refinance at much cheaper rates
• Extension of concessional withholding rate (5%) for foreign investors till 30 June 2020 from 30 June 2017. This benefit is also now extended to Rupee Denominated (Masala) Bonds. A concessional withholding rate is being charged on interest earned by foreign entities in external commercial borrowings or in bonds and government securities	• Will continue to help in raising funds from overseas investors
• Increased focus on digital payments	• To result in improved operating efficiency across companies, which will help in improving profitability in the medium to long term
• SME tax rate reduced by 5% – to 25%	• To result in improved profitability of the SME sector, hence improving repayment capability. To benefit SME financiers like SCUF and Cholamandalam

Oil & Gas – Positive

WINNERS: Gas companies including Petronet LNG, GAIL, Gujarat Gas, GSPL, Indraprastha Gas, Mahanagar Gas

LOSERS: None

While there were quite a few big announcements expected (reducing upstream cess rate and blanket tax cuts in the gas sector), lowering customs duty on LNG and adequate petroleum subsidy provision are nonetheless relieving. The proposal for an integrated PSU oil & gas entity is an eye-catcher, though, for now, it seems a bit farfetched .

Budget Proposals	PhillipCapital Perspective
• To set up two strategic crude reserves in Odisha and Rajasthan to increase capacity to 15.33mmt	• Government is serious about strategic oil stocks, and at current low oil price scenario, is pushing for these
• To create an integrated PSU 'oil major' to match the performance of MNCs/private players	• A challenging move, considering potential job losses, duplication of facilities and disposal – potentially too big to manage. Do not see this happening soon
• To promote and possibly mandate petrol pumps to have facilities for digital payments	• It will impact margins of oil and gas marketing companies in the near term, as they may have to absorb charges and discounts, but they would eventually adjust pricing
• To cut basic customs duty on LNG from 5% to 2.5%	• Positive for the sector as lower gas costs would improve the demand scenario and support distributors' margins. Gas companies are beneficiaries
• FY18 petroleum subsidy budgeted at Rs 291.6bn, including capital outlay.	• This amount of subsidy is comfortable in the context of an oil price of US$ 55/bbl, as under recoveries of Rs 275bn (excluding impact of uncompensated costs) would be covered
• Petroleum excise budget estimate for FY18 at Rs 3.43tn	• Implies a 5% yoy growth, which is in line with total petrol-diesel sales growth (petrol at 10%, diesel at 3-4%). Hence, the government is not building in excise cuts
• Crude oil cess – FY18 budget estimate at Rs 140bn	• Implies a 1% yoy growth; government is not building in a hike in oil prices

Pharmaceuticals – Neutral

WINNERS: Apollo Hospital, Narayana Hrudayalaya, Healthcare Global

LOSERS: None

Budget Proposals	PhillipCapital Perspective
• Budget allocation raised (by 28% to Rs 488bn) towards health and family welfare, by 31% to Rs 271bn towards the National Health Mission scheme (covering government insurance and mediclaims)	• Indirect positive for the Indian healthcare sector (more for corporate hospitals than pharmaceuticals)
• Abolished Foreign Investment Promotion Board	• With this, all the inbound cross-border M&A deals will happen through the automatic-approval route. This is positive for M&A-heavy sectors like Indian pharma
• Proposed to amend the Drugs and Cosmetics Rules to ensure availability of drugs at reasonable prices and promote use of generic medicines	• This could be a small negative for Indian pharma, as it could lead to more price-control measures
• New rules for regulating medical devices will be formulated and will be internationally harmonised	• These will attract investments into this sector, make the segment organised, and reduce the cost of such devices. However, fresh regulations could pose challenges for the devices segment, where there is no large player in India

Specialty Chemicals – Neutral

WINNERS: Aarti Industries, Vinati Organics, Deepak Nitrite, I.G. Petro

LOSERS: SRF

Budget Proposals	PhillipCapital Perspective
• Basic customs duty on o-Xylene reduced to zero from 2.5%	• o-Xylene is a key raw material used in manufacturing pigments, pharma intermediates, and agrochemicals. The duty cut will help raw material costs to fall
• Abolishment of FIPB	• It will pave the way for increasing FDI flow in the sector led by the automatic route
• Basic customs duty on nylon monofilament yarn (falling under customs tariff) for use in monofilament long-line systems for tuna fishing reduced to 5% from 7.5%	• SRF is amongst the leading player manufacturer of nylon monofilament yarn; reduction in customs duty will hurt realisation
• Proposed to repeal The Research and Development Cess Act, 1986	• Many specialty chemicals companies import product- or process-specific technology and there was a cess (not exceeding 5%) on all payments made towards such imports. The repeal will help ramp up such activities.

Telecom – Neutral

Budget Proposals	PhillipCapital Perspective
• Proceeds from the telecom sector are budgeted at Rs 443bn for FY18 vs. revised estimated receipt of Rs 787bn in FY17 • FY17 receipts include upfront spectrum payment of Rs 325bn; hence, adjusted for these, the government expects lower recurring revenue (i.e., SUC and license fees) in FY18 – despite JIO's full-fledged commercial launch in that financial year.	• Negative for incumbents – the government is factoring in lower revenue for the sector in FY18
• No service tax hike	• Sentimentally positive for the sector. As the government is likely to implement GST from Q2 and service tax could rise, we believe the companies would be unable to pass on the impact to subscribers due to the ongoing intense tariff war

Rating Methodology

We rate stock on absolute return basis. Our target price for the stocks has an investment horizon of one year.

Rating	Criteria	Definition
BUY	>= +15%	Target price is equal to or more than 15% of current market price
NEUTRAL	-15% > to < +15%	Target price is less than +15% but more than -15%
SELL	<= -15%	Target price is less than or equal to -15%.

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