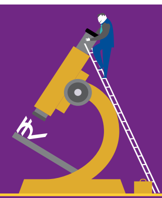
KPMG

India Insights

Union Budget 2018-19

Contents

CEO's perspective



The Union Budget 2018-19 covered a wide range of areas – from allocations aimed at promoting inclusive growth to investments in infrastructure that are so critical to enhancing the competitiveness of the economy. Agriculture and rural areas received special focus.

Adjustments to fiscal deficit targets for Financial Year (FY) 2017-18 were caused by shortfalls in tax and non-tax revenues including due to lower accruals from spectrum auctions. Targets for FY2018-19 have been revised to cover for higher public spending undertakings as well as the downside risks, within reasonable expectations, of rising oil prices.

Building on recent reforms, the progress in ease of doing business in India and a credit environment that is expected to improve, the government's objective to achieve 8 per cent plus growth is credible and re-assuring to both domestic and global investors.

The slow growth of Agricultural sector and the consequent implications on farm incomes is sought to be reversed. The government held out a goal of doubling farmer income by 2022. Various allocations are intended to lay a stronger and transformative base for the sector at large. These steps should also aid in the generation of significant employment.

An ambitious focus on holistic healthcare with strong proposals that are truly cutting-edge in terms of sheer size, coverage and sum insured per family can transform the social safety net for millions. Measures to enhance efficacy in education at all levels – primary, secondary and tertiary – are aimed at overcoming a fundamental constraint, the lack of relevant skills and knowledge, to growth over a longer period.

Within physical infrastructure, rail and roads were provided with all-time high allocations. Measures have been proposed for the rail network to enhance coal access to thermal power stations. Further, the government

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continues in its commitment to develop smart cities and bullet trains.

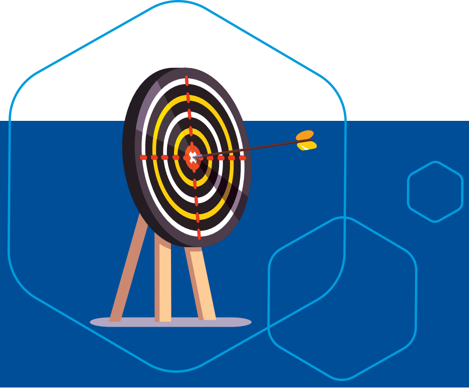
On the taxation front, data indicates a significant increase in direct and indirect tax collection, despite the expected disruptions induced by demonetisation and implementation of Goods and Services Tax (GST). However, as evident, the negative impact of GST was transient and further streamlining of the tax has started to have positive impacts. The extension of 25 per cent corporate tax rate to companies/ MSMEs having turnover of up to INR250 crore (approx. USD39 million) in FY2016-17, helps a sector of industry that is the most effective in job creation.

For the first time in last seven years, the government has exceeded its disinvestment target of FY2017-18 and has increased the goal for the FY2018-19 by over 10 per cent. This is encouraging as a measure to help cover the revenue shortfall, as GST rollout has led to uncertainty in meeting indirect tax collection targets for FY2017-18.

Further on the Indirect Tax front, custom duties were increased in selected sectors such as Consumer Electronics and Automobiles, to provide a fillip to 'Make in India.' At the same time, existing Education Cesses (3 per cent) on customs duty have been abolished and will be replaced by a new Social Welfare Surcharge of 10 per cent on basic customs duties on import. This will lead to imports becoming costlier across the sectors, approximately by 1 per cent. The government has also announced measures to improve customs trade facilitation, pre-notice consultation and time bound adjudication of cases which should enhance the ease of tax compliance and reduce litigations.

Overall, the Union Budget 2018-19 has aimed to address areas that could provide impetus to inclusive growth. Policy and programme execution will continue to remain critical. The series of Budgets over the last few years reminds us that well sequenced, well-crafted and well executed reforms have a crucial role to play in enhancing India's economic development and success.

1. Summary of Budget 2018-19, Press Information Bureau, Governemt of India, Ministry of Finance; 1 February 2018



Analysing sectoral impact

Energy and Renewable Resources[2]

The Union Budget 2018-19 has played a catalyst role in enhancing the ambit of existing schemes in the sector to reach the last mile. While historically the Energy sector has focused on upstream and mid-stream capacity creation i.e. power generation and transmission, refineries, pipelines etc. This Budget is clearly end-user oriented. An end-user focus on energy infrastructure access to last mile coupled with overall focus to improve rural household income is likely to enhance the overall demand and reap long-term benefits for the sector. The reduction of corporate tax rates for corporates with turnover of upto INR250 crore (USD39 million) would benefit renewable energy companies and distributed power players and may enhance the tariff competitiveness. Allowing 'A' rated issuers to access bond capital via institutional investors is a welcome move and may induce a large number of Energy sector companies to access such finance particularly in clean energy space. Overall, the Budget focusses on stimulating customer level demand for energy usage and aims to socialise the recent gains made in energy security by the country. The Budget does lay down a path for achieving the twin objective of access and affordability of energy to the masses.

2. Union Budget 2018-19, Our Point of View, Energy and Natural Resources, KPMG in India analysis, 2 February 2018

Transport and Logistics[4]

- Increased allocation in the development of road network including the 'Bharatmala Pariyojana' would enable the creation of seamless connectivity to remote areas and country borders, improving the safety and reducing the cost of transportation while also allowing business activities to flourish in such areas.
- The plans put forth for the Indian Railways, once executed effectively, would make rail travel convenient as well as safe, fast and passenger-friendly, proving to be prosperous for the organisation on the whole.
- The proposed expansion of 'Ude Desh ka Aam Nagrik' (UDAN) scheme is expected to make air travel affordable for the masses, and could prove to be an impetus for the airline industry.

4. Union Budget 2018-19, Our Point of View, Transport and Logistics, KPMG in India analysis, 2 February 2018

Education[3]

The Union Budget 2018-19 marked the much needed focus on quality of education. This year, the emphasis was more on learning outcome improvement, teacher training programmes and gradual transition from blackboards to digital infrastructure in schools. The government also took to an inclusive approach to education by announcing a schooling model for tribal regions to promote holistic education and preserving local arts and culture.

The Budget saw specific sector-based allocations targeted on specialised skill development (Agriculture, MSME sectors, Digital Technology). However, it had no special focus on 'Skill India' and lacked the vital impetus on International Skills Centre, enhancing private sector participation and a larger apprenticeship programme.

Research and Development (R&D) has been given the much needed fillip. To enable a culture of original research and innovation, the process of leveraging relevant assets and delivering guidance to younger faculty can be improved. Moreover, consolidation of scholarships and monitoring and impact assessment system can be introduced to identify and streamline beneficiaries.

3. Union Budget 2018-19, Our Point of View, Education, KPMG in India analysis, 2 February 2018

Analysing sectoral impact

Healthcare[5]

India has leaped significantly towards universal health coverage as envisaged in the National Health Policy, 2017 with enhanced focus on increased health coverage for the less privileged. Among the various proposals announced, the National Health Protection Scheme under the cover of 'Ayushmaan Bharat' emerged as the showstopper to cover 100 million poor and vulnerable families with a coverage of up to INR5 lakh (approx. USD7800) per family and flagged as the world's largest governemt funded healthcare programme. This is a significant increase from the coverage under the 'Rashtriya Swastha Bima Yojana', benefitting 45-50 crore families in providing access to secondary and tertiary care services.

This increasing government's support and coverage, will boost demand of medical services in the country, giving an opportunity to healthcare providers and insurance companies to partner with the government. It will also reduce the financial and mental burden of healthcare costs on the less privileged. Amidst all the initiatives, more clarity is required regarding the breakdown of allocated Budget and a road map to implement these plans. Convergence with existing government schemes and implementing these measures at such a scale will require close coordination of all stakeholders. Barring the announced efforts to increase medical colleges, more efforts are required to reduce the existing manpower and skill gap. There was also no mention of measures to support investment and collaboration with technology to upgrade quality of care. The government needs to incentivise healthcare providers to imbibe technology and digitise the Healthcare sector.

5. Union Budget 2018-19, Our Point of View, Healthcare, KPMG in India analysis, 2 February 2018

Financial Services[6]

The decrease in corporate tax rates to 25 per cent for Micro, Small and Medium Enterprises (MSMEs) will result in higher availability of residual 'profits after tax' which can be ploughed back into strategic investments and business expansion, leading to higher credit-offtake.

The proposal to withdraw tax exemption for long-term capital gains for the equity market segment and equity mutual funds and units of INViTs/ REIT's is no surprise. This is expected to adversely impact investor sentiment and market growth. This move comes with a relief in the gain computation methodology for securities acquired before 1 February 2018. While this relief is meant for investors at large, the ability of foreign portfolio investors to claim it needs clarity. In a related move, mutual funds have now to pay tax on distribution of dividend in equity oriented schemes.

Certain advocated reliefs claimed for companies under insolvency/ bankruptcy proceedings – relief from Minimum Alternate Tax (MAT) and impairment of carry forward losses upon change of shareholding – have come through. Tax relief for non-residents trading in stock exchanges located in Indian Financial System Code (IFSC) is a welcome move.

6. Union Budget 2018-19, Our Point of View, Financial Services, KPMG in India analysis, 2 February 2018

Analysing sectoral impact

Technology, Media and Telecom[7]

The Union Budget 2018-19 has set the course for the country to emerge as a digital nation. Allocation of INR10,000 crore (approx. USD1.56 billion) for augmentation of telecom infrastructure, prioritisation of next generation technologies such as 5G and Artificial Intelligence (AI), setting up WiFi hot spots and connecting gram panchayats through high speed fiber optic network sends a clear message of digitisation. Further, to continue on its agenda of improving ease of doing business the government has proposed an increased focus on e-governance through national logistics portal, e-office and other e-governance initiatives.

However, while the Budget has been deemed progressive on the digital front, certain critical requirements of the sector have not been addressed. Reducing the overall tax and increasing the ease of doing business through seamless implementation of Right of Way (ROW) have not been covered in the Budget. Similarly the expectation of reduction in tax slabs for the technology and media sector has been ignored and there were no solutions suggested on Goods and Service Tax (GST) compliance simplification.

Overall, while digitisation will thrust India on a fast technology lane, the absence of critical sector reforms will pose a challenge for the sector.

7. Union Budget 2018-19, Our Point of View, Technology, Media and Telecom, KPMG in India analysis, 2 February 2018

Agriculture and Rural Economy[8]

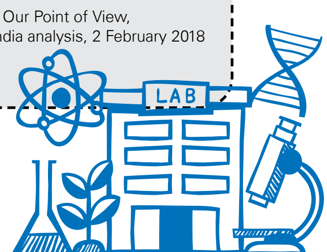
- Minimum Support Price (MSP) for all unannounced kharif crops will be one and half times of their production cost like majority of rabi crops: Institutional Farm Credit raised to INR11 lakh crore (approx. USD171.6 billion) in FY2018-19 from INR8.5 lakh crore (approx. USD132.6 billion) in FY2014-15.
- Around 22,000 rural haats to be developed and upgraded into Gramin Agricultural Markets to protect the interests of 86 per cent small and marginal farmers.
- 'Operation Greens' launched to address price fluctuations.

Life Sciences[9]

- Launch of NHPS is expected to increase the usage of generic products in the country.
- One medical college for every three parliamentary constituencies and at least one government medical college in each state of the country is a big step that can help life sciences companies spread their reach.
- Allocation of INR1200 crore (approx. USD0.18 billion) to set up 1.5 lakh health and wellness centres, addressing even non-communicable diseases and focusing on maternal and child health services is expected improve access of healthcare services and consumption of life science products.

8. Summary of Budget 2018-19, Press Information Bureau, Government of India, Ministry of Finance, KPMG in India analysis, 1 February 2018

9. Union Budget 2018-19, Our Point of View, Life Sciences, KPMG in India analysis, 2 February 2018



Other key takeaways[10]

1. Macro economy

- Gross Domestic Product (GDP) pegged at 7.2 to 7.5 per cent for H2FY2017-18
- Fiscal deficit estimated at 3.5 per cent of GDP for FY2017-18 projected at 3.3 per cent for FY2018-19
- Indian economy size has reached USD2.5 trillion; currently seventh largest economy in the world and is expected to be fifth largest economy

2. Digital initiatives

- Allocation to the 'Digital India' initiative doubled to INR3073 crore (approx. USD0.47 billion) in 2018-19
- Mission on Cyber Physical Systems to be launched to support establishment of centres of excellence for research
- Nearly 500000 Wi-FI hotspots to provide broadband access to five crore rural citizenship
- An indigenous 5G Test Bed to be established at IIT, Chennai

3. Initiatives in taxation

- The Central Board of Exercise and Customs (CBEC) to be renamed as Central Board of Indirect taxes and Customs (CBIC)
- E-assessment of income-tax to be rolled-out across the country to transform age-old assessment procedure
- To incentivise 'Make in India', customs duty increased on mobile phones and TV parts
- Corporate tax reduced to 25 per cent for firms with turnover of up to INR250 crore (approx. USD39 million) in FY2016-17
- Long-term capital gains tax on equity market; long-term capital gains over INR1,00,000 (approx.USD1560) to be taxed at 10 per cent

4. Defence[11]

- India's defence allocation for FY2018-19 has been increased by 7.81 per cent over Budget estimates for FY2017-18
- Private investment in defence production opened up including liberalising foreign direct investment
- Measures being undertaken to develop two defence industrial production corridors in the country
- Industry friendly Defence Production Policy 2018 to be developed to promote domestic production by public sector, private sector and MSMEs

5. Miscellaneous

- NITI Aayog to initiate a national programme on Artificial Intelligence (AI)
- Centres of excellence to be set up on robotics, AI, Internet of Things (IoT)
- Comprehensive gold policy will be formulated to develop gold as an asset class

10. Summary of Budget 2018-19, Press Information Bureau, Government of India, Ministry of Finance, 1 February 2018

11. Defence Budget 2018-19, Press Information, Government of India, Ministry of Defence, 1 February 2018

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