September 2017

India Insights

The Indian economy newsletter

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India at a glance: Quarterly update

Q1FY17-18

Macroeconomy[1]

- **Gross Domestic Product** (GDP) expanded at 5.7 per cent in Q1FY17-18 vis-à-vis 7.9 per cent in Q1FY16-17 - the slowest in three years
  - GDP and Gross Value Added (GVA) started tapering before demonetisation (right from June 2016), indicating the economy was already weakening before the demonetisation shock hit the economy
  - The fall in growth in the June quarter (FY17-18) is also on account of the disruption caused by the introduction of the Goods and Services Tax (GST) and destocking activities
  - The **external sector** has been a drag on growth, since growth in exports has been much slower than that of imports

Government finances[2]

- **Fiscal deficit** as a percentage of GDP is pegged at 3.2 per cent for FY17-18
- **India's trade deficit** for the month of June 2017 narrowed to about USD12.96 billion from USD13.8 billion in May 2017

Forex[4]

- Foreign Exchange Reserves stood at a record high of USD386.53 billion as on 30 June 2017

Foreign Direct Investment[3]

- Foreign Direct Investment in the country increased by 37 per cent to USD10.4 billion in Q1FY17-18 vis-à-vis USD7.59 billion in Q1FY16-17
- Mauritius remained India's top FDI source for Q1FY17-18

Inflation[5]

- **Consumer Price Index (CPI)** hit a record low of 1.5 per cent in June 2017, lowest since 1999, owing to a sustained dip in food prices
- **Wholesale Price Index (WPI)** eased to 0.9 per cent in June 2017 (slowest in 11 months) from 2.17 per cent in May 2017. The subdued numbers reflect the weak trends displayed by various food items and commodities

1. Press Note on Estimates of Gross Domestic Product for the First Quarter (April – June) 2017-18
2. Key Economic Indicators; Office of the Economic Advisor; accessed on 21 August 2017
3. Factsheet on Foreign Direct Investment (FDI); Quarterly Fact Sheet; DIPP; updated upto June 2017
4. Weekly Statistical Supplement; Reserve Bank of India; 30 June 2017
5. Index numbers of Wholesale Price in India (Base: 2011-12= 100); Review for the month of July, 2017; Government of India; Ministry of Commerce and Industry; Office of the Economic Advisor; 14 August 2017

DIPP's Consolidated FDI Policy 2017: Key highlights

Effective 28 August 2017

Over the past decade, Foreign Direct Investment (FDI) into India has nearly doubled to USD43.47 billion, which is 1.9 per cent of GDP in FY2016-17.[1] This compounding growth in foreign investments inflows into India was predominantly observed post 2014 general election, with the government making sustained efforts to unwind norms in various sectors including defence, civil aviation, private security business etc. in a phased manner.

In the latest consolidated FDI policy, the government has laid down specific provisions that are believed to provide the required boost to India's start-up industry. In this regard, the Department of Industrial Policy and Promotion (DIPP) introduced a separate section on start-ups for the first time and spelt out **'competent authority'** for FDI approvals, delegating powers to essentially administrative departments in the absence of the Foreign Investment Promotion Board (FIPB).[2]

The policy also clarified that restriction of 25 per cent on sales of one vendor or their group companies through an e-commerce marketplace will be computed on a financial year basis. The period to be considered for compliance wasn't mentioned earlier.[3]

The document also contains provisions concerning issues of equity/equity-linked instruments/debt instruments and convertible notes by start-ups. Almost all these provisions have already been notified by the authorities, mainly the Reserve Bank of India (RBI). However, the policy has put together several of these under one chapter, adding clarity and simplicity to most of them. For instance, it says start-ups can issue equity or equity-linked instruments or debt instruments to foreign venture capital investors against receipt of foreign remittance, as per the Foreign Exchange Management Act (FEMA), 1999. This was notified by the RBI in October last year. Start-ups can also issue convertible notes to persons resident outside India, albeit with certain conditions. A person resident outside India (other than citizens/entities of Pakistan and Bangladesh) will be permitted to purchase convertible notes issued by an Indian start-up company for an amount of INR25 lakh (Approx USD 38.871.2) or more in a single tranche.[3]

While the administrative ministries will have to approve proposals relating to banking, mining, defence, broadcasting, civil aviation, telecoms, pharmaceuticals etc., the authority to clear proposals relating to areas including retail (single and multi-brand, and food) will rest with DIPP. For proposals relating to financial services activities that are not regulated by any financial sector regulator or where only part of the financial services activity is regulated or where there is doubt regarding the regulatory oversight, the department of economic affairs will clear the proposals.

The policy also simplifies the definition of 'venture capital fund' defined FDI-linked performance conditions without diluting substance. So instead of complex definitions under the earlier FDI regime, 'venture capital fund' is now defined as a fund registered under the SEBI (Venture Capital Funds) Regulations, 1996, while FDI-linked performance conditions are basically the sector-specific conditions for companies receiving foreign investment.

It also clarified that the conversion of a Limited Liability Partnership (LLP) into a company and vice versa is allowed under the automatic route for sectors where 100 per cent FDI is permitted through the automatic route and there are no FDI-linked performance conditions.[3]

1. Factsheet on Foreign Direct investmet (FDI); Quarterly Factsheet; DIPP; March 2017
2. India's new FDI policy includes startups for the first time; ET tech; 29 August 2017; Consolidate FDI Policy (Effective from 28 August, 2017; Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, Government of India; 28 August 2017
3. Consolidate FDI Policy (Effective from 28 August, 2017; Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, Government of India; 28 August 2017

Tune in

Advance Pricing Agreements (APAs) in India - An update

Ever since Transfer Pricing (TP) regulations were introduced in India in 2001, the Indian TP regime has been plagued with huge TP adjustments and lengthy litigations, earning India the reputation of being an aggressive TP regime. However, over the last few years, there has been a considerable shift in government's stance towards making India a more investor friendly destination. In 2012 the Indian government introduced the APA programme to bring in some measure of tax certainty and has been a huge success since its introduction. About 815[1] applications have been filed and 171[2] APAs signed till date.

In May 2017, five years since the inception of the APA programme, the Central Board of Direct Taxes (CBDT) released its first annual report on the progress of the Indian APA programme. The APA annual report 2016-17[3] includes statistics on number of APAs filed and signed or resolved, information on unilateral and bilateral APAs, time taken to resolve unilateral and bilateral APAs etc. and various other facts and figures about the Indian APA programme.

The CBDT attributed the success of the APA regime to the use of electronic mode of communication (e-mail/CDs), confidentiality maintained by APA team as well as the taxpayers and the rational approach adopted by APA team.

The APA annual report 2016-17 shows a favourable comparison between India and China with India concluding more APAs than China, despite China's APA regime being much older than ours. India has concluded more APAs within four years (152) as against China in ten years (113).[4] Further, Indian APA authorities have performed better than United States of America (USA) in terms of duration of concluding APAs. (India - average duration 29 months and 39 months for unilateral and bilateral APAs respectively and USA - average duration 34 months and 51 months for unilateral and bilateral APAs respectively).[5] With regard to bilateral APA applications being filed with other countries, once the USA opened its bilateral APA programme with India in February, 2016, applications for India-USA bilateral APAs have increased. However in the initial years, majority of APAs were being filed/ negotiated with UK and Japan.

In terms of APAs signed, service sector dominates with 72 per cent of the total unilateral APAs signed. Information technology and banking/finance industries lead with almost 50 per cent of the total unilateral APAs. Further, APAs have been concluded with respect to about 20 different industries.

In May 2017 KPMG in India carried out a survey, titled, Advance Pricing Agreement Survey Report 2017 wherein it gathered responses from taxpayers as well as the tax authorities, making it the first-ever survey of its kind which offers observations from both, taxpayers and the tax authorities.[6] As per the survey report, majority taxpayers have lauded the APA programme, 68 per cent felt that APA authorities have displayed a rational

Rahul Mitra

Partner and Head
Transfer Pricing - Tax,
KPMG in India

1. APA Annual Report 2016-17 issued by the Central Board of Direct Taxes; 01 May 2017
2. CBDT Press release; 31 July 2017
3. APA Annual Report 2016-17 issued by the Central Board of Direct Taxes; 01 May 2017
4. Advance Pricing Agreements: India's Scorecard Versus China and U.S.; Bloomberg; 29 May 2017
5. Advance Pricing Agreement survey report 2017; KPMG in India; 12 May 2017
6. Advance Pricing Agreement Survey Report 2017; May 2017

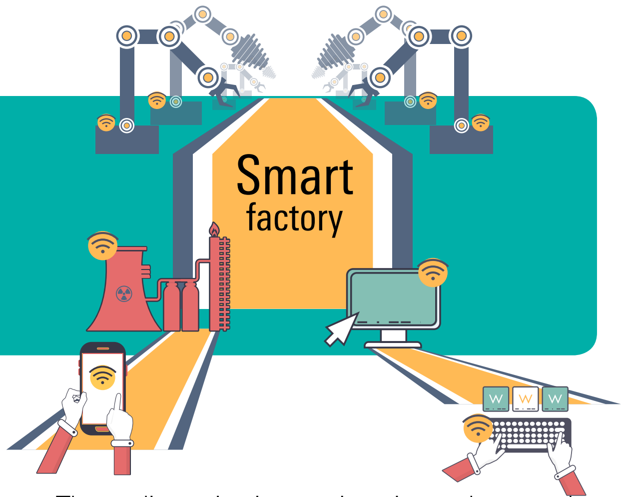
and pragmatic approach to APA and 73 per cent appreciate the APA teams technical expertise. However, 49 per cent taxpayers also expect faster resolution of APAs while 62 per cent feel that the APA team needs more bandwidth. Also approximately 50 per cent taxpayers feel that APA authorities need more clarity around certain complex issues related to APAs.

With regard to factors impacting APA outcomes, the importance of historical orders of Tribunal/ High Court, MAP and bilateral APA outcomes have been emphasised upon both by taxpayers and the CBDT. Further, majority of the respondents favoured unilateral APAs in comparison to bilateral ones due to resolution in a shorter time frame and existence of transactions with AEs in multiple jurisdictions.

The survey brought out some noteworthy observations/responses of the CBDT as well, including the need for the applicants to respond to APA authorities on time, more transparency and collaborative approach in sharing relevant information. Further it recommended to file applications throughout a year instead of pushing them till the end of the year etc.

Overall, the APA programme has been successful among the Indian taxpayer community owing to the positive approach of the APA authorities which is indeed very reassuring. With newer challenges such as implementation of the Organisation for Economic Co-operation and Development (OECD's) Base Erosion and Profit Shifting (BEPS) recommendations, APAs seem to be the best bet to obtain certainty in tax matters for taxpayers involved in complex transactions in huge volumes.

Opinion



"Expanding a business is a long and arduous journey with no shortcuts and can only happen by doing something no one has ever done."

Smart factory is no longer just another buzz word making the rounds in the current business landscape. It holds a bright future for the manufacturing sector as convergence between trends and technologies gains a firm footing in the industry.

The last decade has been a game changer for the industry in more ways than one. The Indian business landscape has undergone a paradigm shift owing to a significant attitudinal shift in the consumer's mindset.

Today's evolved and connected consumer demands new, superior quality products within the shortest possible time. They believe in the mantra - 'right here, right now.'

To cater to the needs of this new age connected consumer, the entire manufacturing ecosystem is gearing up by adopting smart and innovative manufacturing techniques. The aim is to enhance efficiency and profitability, accelerate innovation, and ensure safety and performance.

The concept of smart factory is steadily gaining ground with manufacturing units getting smarter as connected products and systems function as part of a larger, more responsive and agile information infrastructure. Smart manufacturing can help to create a competitive edge with products of unmatched precision and world-class quality.

A question which comes to mind is 'how will the smart factories of the future work?'

For smart factories to be connected with demand-driven supply chains, a seamless interface and connectivity between different equipments which can help ensure an integrated shop floor, needs to be estabilshed.

Smart factories are set to redefine the future of manufacturing in India. One of the sectors where smart factories are currently showing positive results is the Indian automotive sector. The Indian automotive sector, given its potential contribution to GDP and employment, presents a significant opportunity to be one of the biggest growth drivers for the economy. To tap its full potential, the Government of India and the Indian automotive industry are working towards creating an enabling ecosystem and incorporating smart manufacturing, enabling India to emerge as a 'world-class automotive manufacturing hub'.

The customers shall then be able to customise their individual requirements by telling a factory what car to manufacture and what features they would need in their car.

These disruptive innovations in products and processes will redefine the whole customer experience.

Smart factories hold a lot of promise for the Indian manufacturing industry but, the horizon is definitely not a clear, straight road. There are many twists, turns and bumps ahead. The risks in the form of hacking, data theft, and industrial espionage should be looked at as obstacles. Business leaders who have ensured robust cybersecurity standards in place are likely to be the ones who enjoy this new journey somewhat unknown, sometimes serendipitous yet, fruitful and meaningful in the end.

Leveraging the full potential of smart factories can help ensure highly efficient and advanced products which in turn shall ensure India's position on the global manufacturing map.

Samiron Ghoshal

Partner and Head
Alliances
KPMG in India

Market trends

IoT-ification of the Indian healthcare: Beginning of an era of digitally equipped healthcare

Internet of Things (IoT) has emerged as one of the major technological forces that impacts every industry globally. The Indian market is also witnessing its potential, as the Indian IoT market is expected to reach USD15 billion in 2020 from USD5.6 billion in 2016.[1] Although several industries such as manufacturing, transport and logistics, and automotive are expected to generate demand for industrial IoT applications, healthcare is amongst the most popular verticals for the development of IoT solutions.

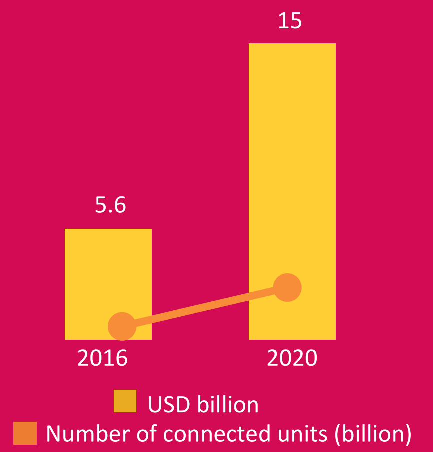
The applications of IoT are expected to gradually knit into the healthcare ecosystem, both at a physician as well as the patient's site. Connecting medical devices, such as ultrasound, thermometers, glucose monitors and electrocardiograms used for tracking patients' overall health; smart beds in hospitals to circumvent the need of nurses; and smart medication dispensers at homes that automatically upload information into the cloud, show the extent of IoT potential in the healthcare industry. In India, with a scarcity of healthcare resources (0.62 doctors per 1,000 patients)[2] and lack of infrastructure (0.9 beds per 1,000 patients),[3] IoT can not only enable doctors to cater to a larger population base, but also bring treatment at patients' doorsteps.

IoT is expected to bridge the gap between healthcare surveillance and implementation of healthcare initiatives

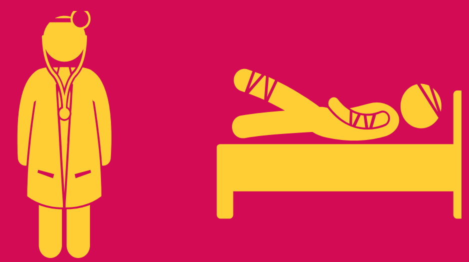
Healthcare surveillance is one of the key factors determining the need of new healthcare initiatives for the improvement of the existing system. In India, healthcare surveillance is about constant monitoring and collation of data from healthcare centres, hospitals and health camps. Currently, most of the data collection is carried out manually and is extremely time-consuming. With the emergence of IoT, data collection can be eased with the help of distributed devices, which would collate, analyse and communicate healthcare related information. The data collected can further be leveraged not only in early detection of health issues, but also to focus on areas requiring government's attention.

One such example is Swasthya Slate, launched in 2014 starting with the state of Jammu and Kashmir, which is a healthcare device that connects to Android™[4] based devices and conducts 33 diagnostic tests within a few hours.[5] The device can collect the data and send it to a central server, creating record of a patient. Data from such devices can be further utilised to implement healthcare initiatives of the government in an area with extensive healthcare needs.

Indian IoT market, 2016 – 20[6]



IoT can be leveraged to overcome the scarcity of resources in the Indian Healthcare system

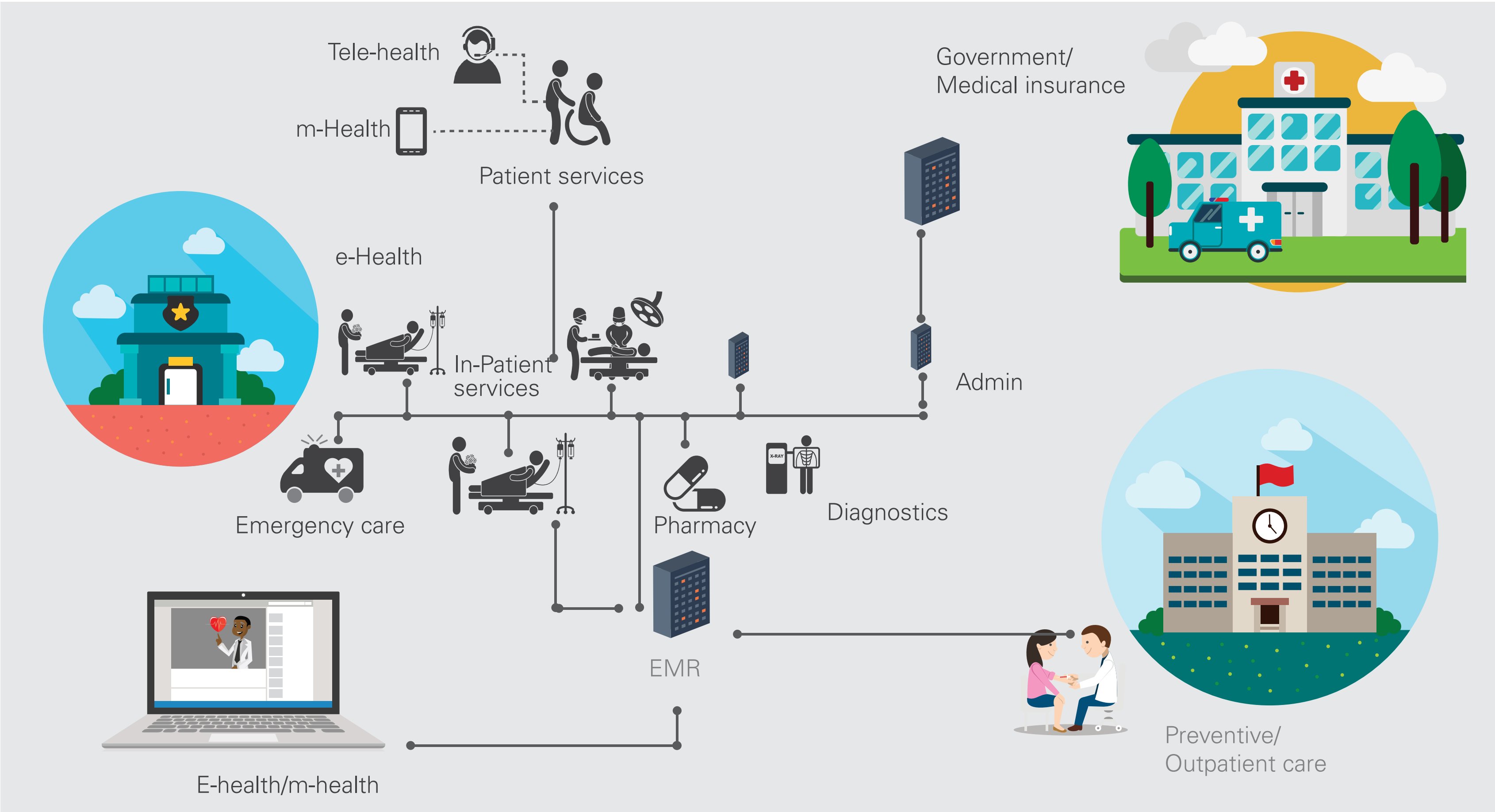


0.62 doctors per 1,000 patients[2]

0.9 beds per 1,000 patients[3]

1. Indian IoT Market Set to Grow uptoUSD15 Billion By 2020; NASSCOM; 5 October 2016
2. Less than one doctor for 1000 population in India: Government tells Lok Sabha, Indian Express, 21July 2016
3. Healthcare, Union Budget 2017-18, KPMG website, accessed on 01 August 2017
4. Android is a trademark of Google Inc.
5. Ministry of Health and Family Welfare launches Swasthya Slate project in Jammu and Kashmir, Public Health Foundation of India, 16 December 2016
6. Less than one doctor for 1000 population in India: Government tells Lok Sabha, Indian Express, 21 July 2016

Integrated Digital Healthcare System: With the help of IoT, an integrated digital healthcare system can be established that not only would reduce the healthcare cost but would also improve the efficiency of the system



Key recommendations on areas of improvement in the Indian healthcare system with IoT implementation

1. **Emerging use of point-of-care technologies:** Point of care monitoring or bedside monitoring, which include devices such as sensors and wearable devices, can leverage the concept of IoT, by feeding health data directly from the patients' site to a central repository. By gathering data from different devices (e.g., monitors, images and therapeutic devices), a complete picture of patient's health status can be obtained. Such data can further contribute in early prevention and intervention leading to a better as well as timely health outcomes.

2. **Reducing healthcare cost:** IoT devices can also enable the clinical staff to work remotely, yet as a team, and thereby bypassing the need to be physically present at patient's location. This can bring

down the cost of healthcare by reducing readmissions and avoiding high cost of in-patient services.

3. **Improvement of treatment protocols:** Significant amount of health data gets generated by means of remote monitoring, smart devices and medical device integration which can be used for improving the treatment protocols of healthcare ailments as well as improving the way care is delivered by physicians. One such example is the use of cognitive intelligence by a Bangalore based hospital chain that involves processing significant oncology data from research papers and patient records as input, to device better diagnoses and treatment options. Such data, when collated with the aid of IoT devices and fed into Artificial Intelligence (AI) systems, can bring a significant change in the way the treatment of complex diseases, such as cancer, is addressed.[7]

4. **Training physicians and patient compliance:** The scope of IoT ranges from training physicians to ensuring treatment compliance for patients'. Gamification can be used specifically for encouraging patients to follow their treatment regimes. One of the examples include game application developed by an EU-based pharma company to prompt children suffering from diabetes to test their blood glucose levels regularly. Further, using gamification with internet-connected devices can serve as a source of training for physicians to assess the improvement areas.

5. **Home healthcare:** Advent of remote monitoring, which uses medical devices that can communicate data, by physicians from home could drastically reduce the need of routine checkups and reviews. With home healthcare, patients are allowed to leave the hospital early, as physicians can observe them from home.

Key challenges and risks associated with IoT

1. **Data security:** One of the major concerns with healthcare data is its security and confidentiality. With constantly evolving regulations and security requirements, it has become important to determine the security of healthcare data while designing the patterns of IoT to be used. Owing to the lack of common security standards and practices around IoT, there are risks associated with health data management, such as device tampering and data breaches. Additionally, such sensitive information is often subjected to cyberattacks, leading to reputational damage, or career damage at times.

2. **Centralised EHR integration:** Lack of availability of a centralised Electronic Health Record (EHR) system makes it difficult for the information collected from IoT devices to include patients' vital signs to reach to the provider for making treatment decisions.

3. **Lack of interoperability:** Owing to lack of adequate interoperability, data from different devices collated by patients lose the clinical value for physicians' or patients' clinical care team.

4. **Extensive infrastructure requirements:** Digitisation of health data and its expansion in the country may put pressures on the data centres. With increase possibilities for data collection and the need for predictive analysis by physicians, the need for data centres and infrastructure is likely to increase manifolds.

A meticulous IoT implementation is expected to take the Indian healthcare a long way

IoT offers significant potential to revolutionise the healthcare system and is expected to considerably improve the process healthcare surveillance, patients monitoring, treatment protocols and meeting treatment compliance. However, there is a need to tackle the risks and challenges associated with data security protocols, infrastructure, and expertise. This requires a meticulous and a systematic approach with involvement of all the stakeholders namely government, private players and patients'.

Nilaya Varma

Partner and Head
Government and Healthcare, IGH,
KPMG in India

7. How IBM Watson is helping doctors diagnose & treat cancer in India, Economic Times, 23 August 2016

KPMG in the News

KPMG 2017 CEO Survey: 90% of CEOs see strong growth for their company going ahead | Moneycontrol | 11 July 2017

Q: The report highlights that confidence of CEOs in growth is still high but it is low than what it was last year. Could you start there?

A: The confidence of CEOs in India is very high. 90 per cent of the CEOs that we surveyed, a 130 CEOs reflected high confidence in the growth prospects. It was down a couple of points, 92 per cent last year, but 90 per cent is a pretty solid number. So, the indication would be that 90 per cent of significant companies feel that they have strong growth prospects in the years ahead.

– Arun M Kumar, Chairman and CEO, KPMG in India

CEOs must pick teams with the right skill sets: KPMG India CEO | Forbes India| 27 June 2017

Q: How do you think the role of the CEO has evolved from, say, ten years ago?

A: The role of CEOs has always been complex because there are multiple stakeholders, multiple issues and disciplines that have to be dealt with. What I have noticed is things are changing so much faster and the technology of five years ago may not be the technology of the next five years. So being on top of the change is critical. No CEO can be knowledgeable about everything. A CEO has to surround himself or herself with different sets of skills at the top leadership. That is a critical element of future CEOs—they have to find that team where there are different skill sets. Technology, regulatory, depending on the industry.

– Arun M Kumar, Chairman and CEO, KPMG in India

Global interdependence will drive India's economic prosperity| Hindustan Times | 16 August 2017

Going beyond bilateral collaboration, India could benefit from multilateral synergies. A three-way collaboration of India-US-Israel holds economic promise. Combining US and Israel's expertise in advanced technologies with India's large talent base would enable businesses in the three countries to gain competitively. Likewise, promoting collaboration at the level of the respective country's states, between large economies like the U.S. and India, will open new economic opportunities.

– Arun M Kumar, Chairman and CEO, KPMG in India

Cos must create collaboration quotient to push inclusive culture: The Times of India| 19 July 2017

Understanding collaborative quotient (CQ) and leveraging it the right way at various levels in an organisation is imperative to build an inclusive culture, while also addressing the "what's in it for me?" question. Additionally, if CQ can be embedded in the work approach, delivery models, performance development and career progression philosophy, it could go a long way to build the desired culture in a more sustainable manner.

– Shalini Pillay – Partner and Head, People, Performance and Culture KPMG in India

Featured publications

Indian Real Estate - Unfolding the new era of growth

The report calibrates the steps taken so far to streamline the sector, while identifying the opportunities and highlighting the key trends therein for industry professionals, policymakers and key stakeholders.

Click here for the report

ASEAN-India: Growing together

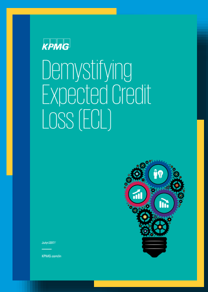
The FICCI-KPMG report explores various investment opportunities for ASEAN in India, especially in digital and creative industries. The report also highlights various policies of the Government of India to attract more investments in the country.

Click here for the report

Accelerating growth and ease of doing business

This report is a representation of ideas from a diverse base of stakeholders in Telecom industry including telecommunications service and infrastructure providers, equipment manufacturers, industry associations, policy makers and thought leaders. It is aimed at presenting a consolidated view of the industry to facilitate a healthy discussion amongst the stakeholders to identify solutions and to alleviate concerns that the industry currently is facing.

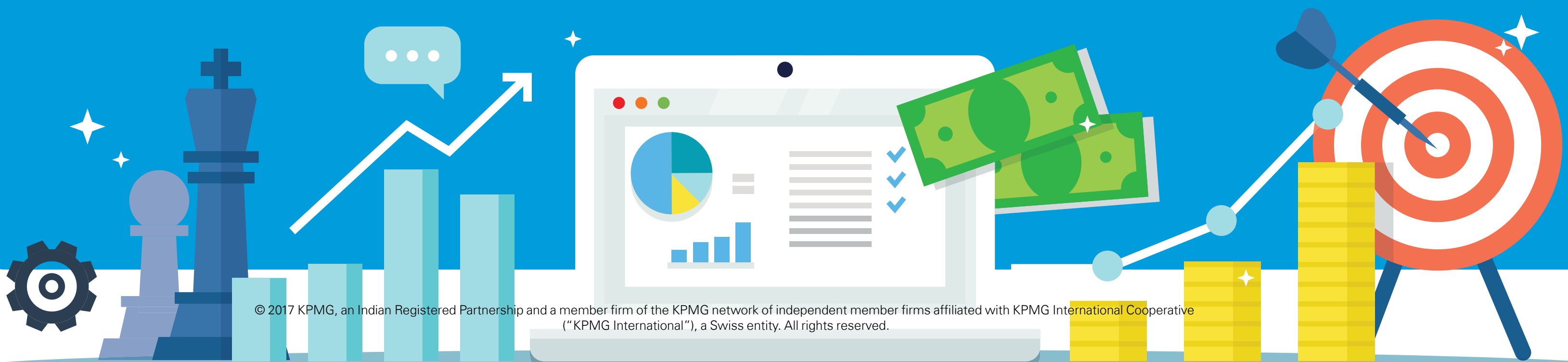
Click here for the report



Demystifying Expected Credit Loss (ECL)

The report aims to demystify the requirements of provisioning using the ECL model under the new Indian Accounting Standards (Ind AS) that are converged with International Financial Reporting Standards (IFRS). This report has been developed based on our implementation experience across Indian, Middle East and South East Asian Banks with regional and global presence.

Click here for the report



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