beyondtheheadlines

2 March 2016

OUR TAKE ON INDIA'S FY2017 (FY17) BUDGET

Indian Finance Minister Arun Jaitley on Monday (29 February 2016) unveiled the FY17 Union Budget. The government's decision to stay on the fiscal consolidation path was well-received. Here are our key take-aways:

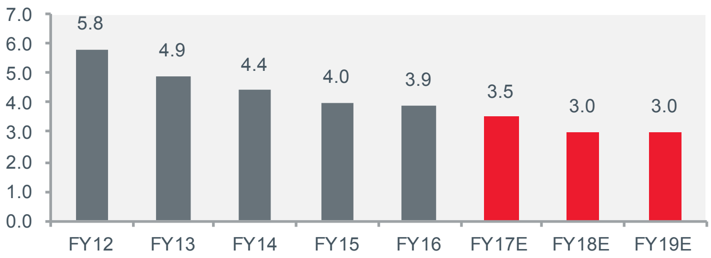
1. Fiscal prudence sets ground for rate cut

Prior to the Budget announcement, debate had raged over whether the government would put fiscal discipline on hold, and instead opt for measures to spur economic growth. Encouragingly, the government has set its FY17 fiscal deficit target at 3.5% of GDP and 3% for the next two years, having achieved the FY16's 3.9% target.

This bodes well for India's large public debt and high bond yields, and may pave the way for a rate cut at the Reserve Bank of India's April policy meeting—which may in turn stimulate growth.

The government's decision to stay on its consolidation course, especially at a time when India faces headwinds from slower demand, demonstrates its commitment and will likely boost confidence within the investment community.

Fig 1: Central government fiscal deficit (% of GDP)



Source: Union Budget FY17, Haver Analytics, CEIC, Goldman Sachs Global Investment Research, 29 February 2016. FY16 is revised estimate and FY17E-FY19E are Budget estimates.

Fig 2: Thrust on nine distinct pillars to "Transform India"

› Agriculture & farmers' welfare	› Financial sector reforms
› Rural sector	› Government & ease of doing business
› Social sector including healthcare	› Fiscal discipline
› Education, skills, job creation	› Tax reforms
› Infrastructure & investment	

Source: Union Budget F17, 29 February 2016

2. Capex subdued; roads and railways still prioritised

Owing to the implementation of the 7th Pay Commission's recommendations (to raise central government employees' salaries), growth in revenue expenditure is budgeted to pace ahead of that in capital expenditure. Overall growth in FY17's capex was raised 4% year-on-year (yoy), much lower than FY16's 21%. This is understandable given the focus on reining in fiscal deficit. The good news is that the government has retained its thrust on infrastructure; spending is expected to be up by 18% yoy with a focus on roads, railways and power.

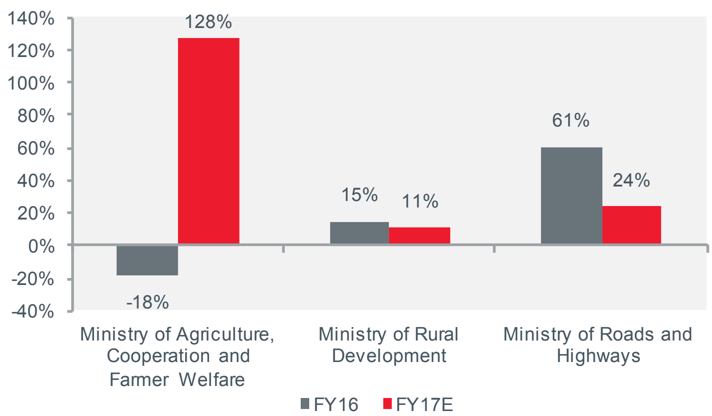
3. A rural-focused Budget

The Budget has been touted as favouring India's rural community. In a bid to revive farm growth and rural economy, the government intends to improve water resources, irrigation and soil fertility to double farmers' income by 2022. The increase in rural spending is mainly driven by higher outlays on crop insurance, irrigation, and rural infrastructure.

Importantly, the government is focusing on creating assets, rather than cash handouts to boost the rural economy. Overall subsidies have been reduced by 0.3 percentage point of GDP.

At the same time, corporate tax rates for large companies were kept unchanged at 30%, a levy introduced on luxury cars, and cigarette duties raised.

Fig 3: Agriculture, roads and highways among the beneficiaries of spending allocation (YoY change, %)



Source: Union Budget FY17, Ambit Capital Research, 29 February 2016. FY16 numbers are revised estimates and FY17E numbers are Budget estimates.

4. Limited cash injections for public sector (PSU) banks

The government offered no more than the INR250 billion it had pledged late last year to recapitalise debt-laden PSU banks. This is perhaps one of the biggest disappointments from the Budget, given the severity of non-performing assets at the banks.

However, a day after the Budget announcement, the central bank relaxed capital adequacy norms; estimated to release a significant INR250-500 billion of capital for the PSU banks.

5. Reforms still on the cards

Some measures show the government is still committed to longer-term reforms. For example, to improve the ease of doing business, a task force will be set up to rationalise human resources in government and autonomous agencies. To promote "Make in India", foreign investors may be granted residency status, beyond the current five-year business visa, and to encourage new businesses, start-ups will receive full tax exemption for the first three years.

This document is produced by Eastspring Investments (Singapore) Limited and issued in:

Singapore and Australia (for wholesale clients only) by Eastspring Investments (Singapore) Limited (Company Reg. No: 199407631H), which is incorporated in Singapore, is exempt from the requirement to hold an Australian financial services licence and is licensed and regulated by the Monetary Authority of Singapore under Singapore laws which differ from Australian laws.

Hong Kong by Eastspring Investments (Hong Kong) Limited and has not been reviewed by the Securities and Futures Commission of Hong Kong.

United Arab Emirates by Eastspring Investments Limited which has its office at Precinct Building 5, Level 6, Unit 5, Dubai International Financial Center, Dubai, United Arab Emirates. Eastspring Investments Limited is duly licensed and regulated by the Dubai Financial Services Authority (DFSA). This information is directed at Professional Clients as defined by the Conduct of Business rulebook of the DFSA and no other person should act on it.

United States of America (for institutional clients only) by Eastspring Investments (Singapore) Limited (Company Reg. No. 199407631H), which is incorporated in Singapore and is registered with the U.S Securities and Exchange Commission as a registered investment adviser.

Luxembourg (for institutional and professional investors only) by Eastspring Investments (Luxembourg) S.A., Grand-Duchy of Luxembourg.

United Kingdom (for institutional and professional investors only) by Eastspring Investments (Luxembourg) S.A. - UK Branch, 125 Old Broad Street, London EC2N 1AR.

Chile (for institutional clients only) by Eastspring Investments (Singapore Limited (Company Reg. No: 199407631H), which is incorporated in Singapore and is licensed and regulated by the Monetary Authority of Singapore under Singapore laws which differ from Chilean laws.

The afore-mentioned entities are hereinafter collectively referred to as Eastspring Investments.

This document is solely for information purposes and does not have any regard to the specific investment objective, financial situation and/or particular needs of any specific persons who may receive this document. This document is not intended as an offer, a solicitation of offer or a recommendation, to deal in shares of securities or any financial instruments. It may not be published, circulated, reproduced or distributed without the prior written consent of Eastspring Investments.

Past performance and the predictions, projections, or forecasts on the economy, securities markets or the economic trends of the markets are not necessarily indicative of the future or likely performance of Eastspring Investments or any of the funds managed by Eastspring Investments.

Information herein is believed to be reliable at time of publication but Eastspring Investments does not warrant its completeness or accuracy and is not responsible for error of facts or opinion nor shall be liable for damages arising out of any person’s reliance upon this information. Any opinion or estimate contained in this document may subject to change without notice.

Eastspring Investments (excluding JV companies) companies are ultimately wholly-owned / indirect subsidiaries / associate of Prudential plc of the United Kingdom. Eastspring Investments companies (including JV's) and Prudential plc are not affiliated in any manner with Prudential Financial, Inc., a company whose principal place of business is in the United States of America.