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India: 2009 Union Budget—spotlight on infrastructure

- The closely watched Union budget to be presented on July 6 will be important in gauging the new government's policy stance. We think it will have a big focus on infrastructure.

- We expect the budget to also emphasize low-cost housing, rural spending, and support for the exportable sectors.

- Given the spending pressures, we expect the central government's fiscal deficit to remain high at 6.5% of GDP and the consolidated deficit at 10.1% of GDP in FY10 despite a fall in oil and fertilizer subsidies. The deficit, we think, will likely be financed comfortably due to disinvestment and the auctioning of 3G license proceeds.

- Consequently, we think that long bonds which have sold off recently in part due to concerns about funding the fiscal deficit, may rally.

- We continue to expect the INR to strengthen over a 12-month horizon, and think that concerns over financing the fiscal deficit are overdone. Our 12-month target for USD/INR is 44.7.

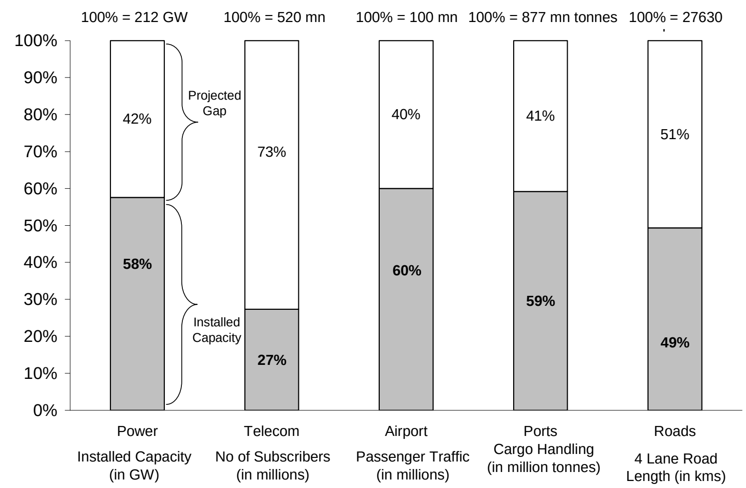
- Our sector analysts have outlined their expectations on the budget, and the impact on their respective sectors. We expect the budget to be positive for IT, capital goods, logistics, and financials.

The Union Budget to be presented on July 6 is being keenly watched by market participants, not only to convey the fiscal stance of the government for the coming year, but more importantly, its attitude towards and roadmap for, structural policy reforms. We have written extensively (see *Reforms—great expectations*, India Macro Stance, June 16) on the likelihood of reforms, a majority of which may be announced in the budget itself. The main ones include a big push in infrastructure spending—especially roads and ports; opening up the insurance sector to greater foreign direct investment (FDI) and its ability to raise capital through IPOs; divestment in government-owned enterprises; a roadmap for fiscal consolidation, including the implementation of the Goods and Services Tax (GST); and education and governance reforms. Below we discuss our expectations of the key themes and sectoral implications of the budget.

Building India

We expect a big boost in infrastructure spending in the upcoming budget. The government has identified infra as a key thrust area—both in its manifesto and in the President's speech outlining the policy priorities for the new government. Infrastructure remains woefully undersupplied in India—according to the Planning Commission, India may need to nearly double its ports, roads, power, telecom, and airports capacity (see Exhibit 1).

Exhibit 1: Building India



Source: Planning Commission, GS Global ECS Research.

We expect a big stimulus to be provided to roads and ports in particular. A changing of the guard at the Ministry of Surface Transport is giving the roads sector a big impetus, and we expect speedy regulatory approvals, more budgetary allocation, and the setting up of a "Roads Finance Corporation" to fund road projects which would securitize its income and list on the stock exchange, among others.

For power, we expect the budget to contain significant increases in spending, including for generation, rural electrification, and for minimizing transmission and distribution losses.

Other measures which the budget may announce on infra would be to give greater flexibility to the Infrastructure Investment and Financing Company Ltd. (IIFCL), which has been set up as a refinancing facility for infrastructure projects, to deploy funds; liberalize investment guidelines for insurance and pension funds in related sectors; increase the exposure limits of banks for specific sectors; and give a big push to Public Private Partnership (PPP) projects in infra.

Low–cost housing—a roof over every head

Low-cost housing in India is seriously undersupplied. There is currently an estimated supply shortfall of over 30 million units in India, while demand continues to rise due to urbanization, demographic change, and falling household sizes. Although there has been a real estate boom in recent years, it has been limited to the middle and upper-income residential and commercial property markets. Low-income households, quite unlike the US, did not partake in the boom. We have previously written about low-cost housing as a key theme for 2009 (see *India: Four macro themes for 2009*, Asia Economics Flash, January 20).

We expect the budget to continue to provide incentives for low-cost housing. In recent months, the government has prioritized this area, and given it significant fiscal incentives as part of stimulus packages during the downturn. We expect these incentives to continue and to be buttressed. These include providing income tax exemptions to developers, incentivising state governments to encourage affordable housing by a reduction in stamp duties, and improving access to funds through the National Housing Board for refinancing.

Exhibit 2: Low-cost housing—the new focus of government incentives

Measures over the last 2 months to promote low-income housing	
Measure	**Date**
Allow the use of ECBs for the 'development of integrated townships'	2-Jan
GOI will work with State Govts. to encourage them to release land for low income and middle income housing schemes.	2-Jan
Increased funds from the US$ 4300 mln pool (of increase in plan expenditure) for the rural housing programme - Indira Awas Yojna	7-Dec
Refinance facility of Rs.4000 crore for the National Housing Bank	7-Dec
Bank loans below Rs. 20 lakhs to be eligible for priority sector lending, thus availing lower rates	7-Dec
Public banks to announce new package for borrowers of home loans in two categories: (1) upto Rs.5 lakhs and (2) Rs 5 lakh-Rs 20 lakh.	7-Dec
Provide concessional regulatory treatment for exposure to real estate, capital market exposures and personal/ consumer loans	7-Dec

Source: Government of India, Reserve Bank of India, GS Global ECS Research.

Exhibit 3: The fortune at the bottom of the pyramid—"aspiring", "seeking" and "striving" for a house of one's own

FY08 estimate		Deprived	Aspirers	Seekers	Strivers	Near rich	Clear rich	Sheer rich	Super rich
Number of households	'000	122998	63340	17538	4453	1632	686	162	86
% of total households	%	58	30	8	2	1	0	0	0
Annual Income	US$	<2070	3335	8050	17245	34485	80460	172415	>229890
	Rs. '000	<90	145	350	750	1500	3500	7500	>10000

Source: NCAER, GS Global ECS Research.

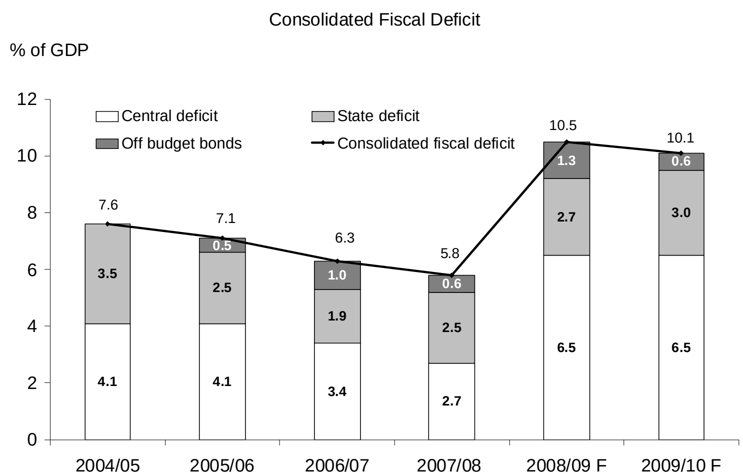
Tax rationalization, rural spending, help for exporters

We expect the budget to continue to focus on the rural sector, and also incentivise the exportable sector. We expect more outlays for the government's flagship programs: the National Rural Employment Guarantee Act (NREGA) and rural infrastructure (Bharat Nirman). On the revenue front, we think the government may unwind some of the tax incentives given earlier during the stimulus packages, especially excise duty cuts (see below for our expectations on sectoral incentives and taxes).

Rising fiscal deficit funded by disinvestment

We expect the central government's deficit to remain at an elevated level at 6.5% of GDP, and the overall deficit to be 10.1% of GDP in FY10. The spending priorities of the government, on infrastructure, low-cost housing, rural sector, and health and education suggest an increase in spending, despite a decline in the on-budget subsidy bill due to a fall in fertilizer prices, and a pickup in revenues in the second half of FY10 as activity recovers. We think the overall deficit may come down marginally in FY10 to 10.1% of GDP from 10.5% of GDP in FY09 due to the large decline in the issuance of off-budget bonds for oil and fertilizer subsidies offsetting the spending increases outlined above.

Exhibit 4: The overall deficit may come down marginally in FY10



Note: F - Forecast

Source: Government of India, Reserve Bank of India, IMF, CEIC, GS Global ECS Research.

Although the deficit will be high, we think it can be easily financed, in part due to impending disinvestment and the auctioning of 3G licenses. Long bonds may rally as a result. We were more concerned about the financing of the deficit before the elections than after. This is mainly due to the ramping up of disinvestment proceeds and the auctioning of the 3G licenses, which we expect will fetch the government about 0.4% and 0.5% of GDP respectively and help finance the deficit. Along with the Reserve Bank of India's pre-announced purchase of government bonds, and the continued deposit growth in the banking system, these can finance more than 80% of the government's borrowing needs. Therefore, we think the government's market borrowing, minus bank subscriptions, may actually be lower in FY10 than in FY09. Hence, long bonds, which had sold off in recent weeks, in part due to concerns about financing the deficit, may rally.

Exhibit 5: Sources of funding the centre's fiscal deficit

	FY09	*FY10*		
	Rs bn	*Rs bn*	*US$ bn*	*% of GDP*
Central Fiscal deficit	3,265	3,865	81	6.5
Short term borrowings	575	0	0	0.0
External assistance (Net)	96	160	3	0.3
Securities issued against Small Savings	13	133	3	0.2
State Provident Funds (Net)	48	50	1	0.1
Other Receipts (Net)	-387	-101	-2	-0.2
Draw-down of cash Balance	300	0	0	0.0
Disinvestment**	0	250	5	0.4
3G	0	300	6	0.5
Incremental bank deposits	1,583	1,839	39	3.1
RBI	0	800	17	1.4
Net market loans*	1,036	434	9	0.7
Rescheduled repayment	446	531	11	0.9
Gross market loans	**1,482**	**966**	**20**	**1.6**

Note: FY09 fiscal numbers are from the government's revised estimates
*** In FY09, selling shares vested with SUTI is treated as a revenue item in the revised estimates of the government*
** to be subscribed by LIC, UTI, NABARD, EPF, primary dealers and others*

Source: Government of India, Reserve Bank of India, IMF, CEIC, GS Global ECS Research.

We do think, however, that the high fiscal deficit remains a key vulnerability for the economy. Although prospects for reform have improved after the elections, a medium-term plan for deficit reduction is critical. Important elements of such a plan should include a successor to the Fiscal Responsibility and Budget Management Act (FRBM) mandating annual reductions in the central and state deficits; the implementation of the GST; reform in fertilizer and oil subsidies; orienting spending to more investment rather than consumption; and better tax administration to increase the number of taxpayers.

We continue to remain positive on the INR. There are some concerns that the high fiscal deficit will impact the INR negatively. We think that these concerns are overdone, due to the available financing for the government, as discussed above. The catalysts for INR appreciation remain, including stronger domestic demand than elsewhere, prospects of higher capital inflows, in part due to reforms, and a lower current account deficit. Our 3, 6, 12-month targets for USD/INR are 47.3, 46.0 and 44.7.

Exhibit 6: Major reforms, likelihood of implementation, and potential impact

Reform Area	Key Issues	Likelihood of Reform	Description	Potential Impact*
Infrastructure	Roads & Ports	High	Public-Private partnership model to be made more investor-friendly, especially in Roads and Ports; Major projects to be monitored directly by PM's Office	Speedy regulatory clearance positive for roads and ports sectors
	Power	Medium		
	Airports	Low		
	Urban Infrastructure	Low		
Financial Sector	Pension and Insurance	High	Set up an independent regulator for pensions; more flexibility to state insurance companies to raise capital; increase FDI limit for insurance sector from 26% to 49%	Greater channeling of domestic savings for long-term investment; positive for insurance and financing for infrastructure
	Banking	Low	Further opening up banking to foreign banks	Incumbents in banking system, including public sector banks, to face less threat of competition
	Financial Inclusion	High	Revamping of banks and post offices to become outreach units for financial inclusion	Increase savings intermediated through the formal sector
Governance	Delivery Monitoring Unit in the Prime Minister's Office	High	Monitor flagship programmes and iconic projects	More timely implementation of government projects
	Civil services reform	Medium	Stability of tenure of civil servants; Model Public Services Law giving greater accountability and performance related pay	Improve efficiency and accountability of government
	Judicial Reform	Medium	Roadmap for judicial reform in 6 months; network of fast-track courts across country	More timely enforcement of justice
	Right to Information	High	Public data policy to place all information covering non-strategic areas in the public domain	Greater transparency in government functioning
Divestment in government companies	Sell minority stakes in government owned companies	High	Sell stakes in government owned companies, especially to retail investors, while keeping government ownership above 51%	Garner funds for financing the fiscal deficit, including foreign funds; reduce govt. market borrowing and lower bond yields
Privatization of government companies	Outright sale / sale to strategic investors	Low	Sell majority stakes and stakes to large strategic investors	Inability to bring in more efficient resource allocation which could have happened through outright sales
Fiscal Reforms	Goods & Services Tax	High	A unified nation-wide goods & services tax to replace complex array of state and central taxes (Planned for April 1, 2010)	Increase efficiency by creating a national common market; remove tax distortion in indirect tax structure; but will not generate large revenue increase
	FRBM II Act *(Fiscal Responsibility)*	High	Credible commitment to bring down fiscal deficit to acceptabl levels in medium-term	Instil investor confidence in govt finances, boost domestic savings, reduce crowding out
	Reduction in subsidy bill, especially oil and fertilizer	Low	Link final prices to global levels in order to reduce subsidies	Reforms could have removed distortions and created fiscal space for growth-enhancing spending on infra, health & education
	Reform of administered oil pricing mechanism	Low	Review of administered pricing mechanism underway, but consensus will be difficult	
Labor reforms	Flexibility in Hiring and Firing of Workers	Low	Legal changes to allow greater flexibility to hire and fire workers	Reforms could have made private sector more competitive and created opportunities for unorganized sector workers
Education	Private / foreign investment in higher education	High	Improved investment climate for private players; Bill to allow foreign universities	Major improvement in quanity and quality of higher education options
Food Security & food subsidies	Right to Food	High	Right to food to all citizens; Rice/wheat at Rs.3/kg to all poor families; better targeting to public distribution system	For equality and improved nutrition; could have large negative fiscal impact
Mining Development & Coal reforms	Opening up Mining to greater exploration and less regulation	High	Private sector oil exploration model to be implemented in other mining sectors; implementation of coal sector reform blueprint	Greater private sector investment; positive for metals and mining sector
FDI	General liberalisation	High	FDI policy likely to be investor friendly in some non-strategic sectors	Potential of enhancing availability of foreign funds in areas which get liberalised
	Retail	Low	Unlikely, in order to protect local players, especially in the unorganized sector	

** Based on the likelihood of reform getting implemented*

Source: GS Global ECS Research.

Exhibit 7: Summary of our sectoral expectations from the budget

Sectors	Key expectations from budget	Probability/Impact
Metals & mining		
	Introduction of ad valorem royalty rate for iron ore mining	high/negative
	Potential reversal of excise duty cuts on steel products	moderate/neutral
Cement		
	Rationalisation of tax structure	moderate/positive
Automobiles		
	Review of excise duty rates	low/negative
Capital goods		
	Higher allocation for building roads, ports and urban infrastructure	high/positive
	Steps to make land acquisition for projects quicker and easier	moderate/positive
	Bring back investment allowance provisions	low/positive
Media		
	Removal of fringe benefit tax for media agencies	moderate/positive
	Removal of duty on the import of equipment for broadcasting services	moderate/positive
	Import duty on digital set-top boxes being removed	low/positive
	Cut in DTH license fee from 10% to 6%	high/positive
Logistics/transportation		
	Clarity and roadmap towards achieving GST by April 2010	high/positive
	Incentives in the rail budget to increase annual freight loading	moderate/positive
	Higher allocation in the roads and ports sector	high/positive
Real estate		
	Tax benefits on housing loans	moderate/positive
	Moves that could improve liquidity for the sector such as relaxation of FDI norms, easier access to debt or low-interest loans to buyers/developers	low/positive
	STPI tax holiday extension	high/positive
FMCG		
	Increase in excise duty on cigarettes	high/marginally positive
	Reversal in recent duty cuts	low/negative
Healthcare		
	Income Tax exemptions for R&D spend	moderate/positive
	Increase government spending on public healthcare and health insurance coverage for BPL families	moderate/positive
Information technology		
	STPI tax holiday extension	high/positive
	Treatment of packaged and customized software/ clarity on service tax, FBT, and transfer pricing	moderate/positive
Financials		
	Changes in the foreign ownership ceiling for insurance	high/positive
	Hike in tax incentives for individuals on purchase of property	moderate/positive
Energy		
	Clarification on the definition of "mineral oil" for the purpose of 80IA deduction	moderate/positive
	Increase in budget provision for LPG and Kerosene	moderate/positive
	Increase in customs duty for crude, petrol and diesel to align with the rates that prevailed in June 2008	high/positive
Utilities		
	Increase in outlay for power sector	moderate/positive
	Setting up additional ultra mega generation and transmission power projects	high/positive

Source: GS Global Investment Research.

Metals and mining

By Pritesh Vinay

We think that after the rationalisation of import duty structures for metals (both non-ferrous as well as steel and their raw materials) over the past four years, there is very little room left for any major changes.

Royalty rates for iron-ore mining. The budget may introduce an ad valorem rate of royalty for iron ore mining, given that current royalty rates are a pittance as compared to market prices for iron ore. We do not expect significant increases to the current export tax regime, given that large portions of India's iron ore exporting industry are under stress at current international prices of iron ore.

Changes to duties for the steel sector. Government had cut excise duty on steel products in December 2008 as a part of the fiscal stimulus. It is expected that this may be restored to original levels—and align it in line with expected GST from next year. We do not expect additional measures to protect the steel industry from competition from imports, given that domestic demand has been strong over the last few months, India remains a net importer of steel products and most flat steel producers are currently operating at high utilization rates. However, marginal changes to import duty rates (from current 5% to 10%) or safeguard duty cannot be ruled out.

No changes for base metals. We do not expect any changes in non-ferrous metals (aluminium, copper, zinc, lead) duty structure.

Cement

By Pritesh Vinay

Rationalisation of taxes for the cement sector. The cement industry has been lobbying for a rationalisation of taxes for quite some time now—the current excise regime (from 3 slabs) is sought to be streamlined to a uniform ad valorem slab. Also, cement current enjoys a VAT of 12.5% and the industry has been seeking a rationalisation to bring it on par with steel (4%). There could be some progress on these two issues.

Automobiles

By Sandeep Pandya

Potential review of excise duty rates. There is a possibility of a review of excise duty rates for certain segments such as two-wheelers. Year-on-year demand growth has been strong over last few months, and producer margins are improving on the account of falling metal costs. However, we think that the government will most likely maintain the status quo for one more year, and avoid putting at risk the nascent sequential recovery in demand. In our view, the government would seek to boost revenues through higher demand rather than higher rates of excise duty.

Capital goods

By Ishan Sethi

Higher allocation for building roads, ports and urban infrastructure. The Road Transport and Highways Ministry is seeking doubling the budgetary allocation of roads that do not fall under NHAI @ Rs 6000 crore vs. the Rs 3350 available now.

The Ministry of Roads is also pitching for including innovative financing schemes including setting up of a Road Finance Corporation with an initial corpus of Rs500 crores to provide easy financing options for the sector.

Steps to make land acquisition projects quicker and easier. Higher allocation for viability gap funding (Rs27900 crores was approved in 2008-2009) and quicker processing for accessing Viability Gap Funding.

Impact: The eleventh plan targets an addition of 7000 kms to the national highway network. However, a majority of the NHDP projects are yet to be awarded. The execution of a majority of port projects are also behind schedule. Execution of the above measures could lead to the awarding of many infrastructure-related projects, speed up the execution and also make PPP more investor friendly.

Media

By Ishan Sethi

Broadcasters:

Removal of service tax on broadcasting services.

Removal of duty on the import of equipment for broadcasting services.

DTH players:

Import duty on set-top boxes being removed.

Cut in license fee from 10% to 6%.

Impact: Set-top boxes currently incur a cumulative tax of ~40%, given the multiple taxation they are subjected to—removal of the import duty would make the Set Top Boxes more affordable. The cut in service tax for all media companies is also positive for the space—likelihood is moderate, in our view.

Logistics/Transportation

By Ishan Sethi

Clarity and roadmap towards achieving GST by April 2010.

Incentives in the rail budget to increase annual freight loading.

Higher allocation in the roads and ports sector.

Impact: The complex, non-standardized nature of the Indian tax structure has contributed to the inefficiency of the Indian logistics sector. The phase out of the CST of 3% by April 2010 coupled with the introduction of the GST and steps to improve logistics infrastructure would improve the efficiency of the Indian logistics sector which at 13% of GDP is one of the most inefficient globally.

Real estate

By Vishnu Gopal

Key expectations: In our view, any incentives related to tax or liquidity could be positive for real estate developers.

Low-cost housing. Given the housing shortage among lower-income groups in India, any schemes that encourage major developers to undertake mass lower-income housing projects would be beneficial for the sector. Some developers have already announced projects with ticket sizes as low as Rs2 million an apartment.

Tax benefits on housing loans. Individuals are allowed tax deductions of up to Rs100,000 on principal payments on home loans and up to Rs150,000 on interest on home loans. Any moves to raise either of these thresholds could be beneficial for end user demand and real estate developers.

Liquidity measures: Any moves that could improve liquidity for the sector such as relaxation of FDI norms, easier access to debt or low-interest loans to buyers/developers for low cost housing projects could encourage developers to execute more projects.

STPI tax holiday extension. The IT/ITES industry accounts for 60%-70% of office demand and has been impacted by the slowdown in global markets. With the STPI scheme due to expire in March 2010, an extension for 2-5 years could be on the budget agenda. With developers also putting projects on hold, we believe an extension could boost demand for IT park space prompt a recovery in the office lease market. However, there could be a trade-off with lower demand for SEZs.

Impact: We believe any of the above, if implemented, could lead to a sustainable recovery in sales and lease volumes, which in turn should benefit listed developers

Consumer goods

By Vishnu Gopal

Key expectations: We believe incentives for rural and social sectors are likely to be an area of focus for the UPA government and this should benefit some FMCG companies that derive a significant proportion of their turnover from rural India. That aside, we believe the key area of interest will be any changes to excise taxes

Excise tax—cigarettes. Taxation on cigarettes has not been favorable over the past two years with the introduction of 12.5% state-level VAT in 2007-2008 and the steep increase on non-filter cigarette tax in 2008-2009 to bring them on par with filter cigarettes. While there is a risk that the tobacco industry could be subject to adverse tax hikes yet again, we believe the changes over the past two years were structural in nature and our expectation is that taxes could rise at a high single-digit rate given the large fiscal deficit—we would therefore view any news of moderate excise tax increases e.g., 5%, as reassuring from the tobacco industry's viewpoint.

Taxation—others. Measures announced post the interim budget in 1Q2009 include the extension of a 4% Cenvat rate cut, a 2% reduction in service tax and a 2% cut in excise duty for certain products. At the very least, we believe news that recent cuts will not be reversed could be positive and should benefit manufacturers of household and personal care products. We could also expect more clarity on the introduction of goods and services tax, which is not expected before the end of fiscal 2009-2010.

Impact: We believe that FMCG companies with exposure to rural India may continue to benefit from the budget, provided the monsoon does not play spoilsport. As long as tobacco tax hikes are moderate, we believe the tobacco industry may be able to offset this impact through selling price increases

Health care

By Balaji Prasad

In summary, we believe that healthcare may not be a significant area of focus in this budget and hence, have limited expectations—despite the industry continuing its clamour for greater R&D sops. Other demands by the industry (mentioned below) do not have any meaningful direct / near-term impact on our estimates for the India pharma / hospitals sector.

Income tax exemptions for R&D spending: Indian pharma executives have been demanding IT exemption and fiscal incentives for promoting Basic Research (Drug Discovery R&D) in India. They have also demanded a decision on the central drug authority bill (provisions for a centralized licensing authority on the lines of the USFDA), which has been pending in Parliament for the last five years. Additional demands are geared towards the small and medium enterprises (a large corpus to support Schedule M compliance, increase limit of excise exemption for small scale industries).

Clinical trials: Demands to expedite the process of granting approvals for clinical trials and new drugs.

Hospitals: Demand to increase government spending on public healthcare and health insurance coverage for BPL families, in line with the UPA’s election manifesto.

Information technology

By Julio C. Quinteros, Jr.

Key expectations:

STPI tax holiday extension. Representatives from Nasscom, major IT services companies, and the Ministry of Communications & IT have been persistently pitching for an extension of the STPI scheme that is set to expire in March 2010. This comes at a time when the demand backdrop in US and Europe, the two major end-markets of IT services companies, has been severely impacted by the recession, high currency volatility, and a protectionist US policy. A key concern for the industry, particularly for small and medium enterprises, as they struggle to maintain profitability is that they can hardly afford incremental investments setting up units in SEZs when the STPI tax holiday ends. Moreover, India’s diminishing competitiveness against alternative offshore destinations such as Egypt, China and the Philippines, also offers a compelling reason to enact an STPI extension for the IT services sector, which is among the largest employers in India. With the STPI clause set to expire this fiscal year, we believe an extension for 2-5 years could be on the budget agenda.

Treatment of packaged and customized software/ clarity on service tax, FBT, and transfer pricing. Resolution of indirect taxes duplicity for packaged software, clarity on policies for service tax refunds, uniform approach on transfer pricing and amendment of fringe benefit tax on ESOPs are among the priority items on the IT industry’s wish-list for this year’s budget. Other items include acceleration of IT adoption in government, nation-wide broadband roll-out, and education and skill building.

Impact: An extension in the STPI tax holiday scheme, which is currently not built into our estimates, would provide incremental benefit to earnings for the sector. If enacted, this would not impact FY2010 estimates but could provide earnings benefit starting in FY2011. Our models currently assume that the tax rate goes from mid-teens on average to about 20%-25% in FY2011. For perspective, in a scenario where the tax rate stays at current levels, starting in FY2011 it would benefit earnings by about 7% for the US-listed Indian IT services companies, and by about 10% for the locally listed Indian IT services companies based on our estimates. Separately, any positive amendments in service tax, FBT, transfer pricing or treatment of packaged software could also be beneficial for the sector longer-term.

Financials

By Sampath Kumar

Two key changes possible in the budget, both potentially impacting the sector positively.

Changes in the foreign ownership ceiling for insurance: Foreign ownership ceiling for the insurance sector could be raised to 49% from 26%. This would allow companies that are currently sponsors of the insurance companies either to sell down their stake to JV partner and realize more value or list them resulting in a market driven price discovery process for these businesses. Both are likely to be positive catalyst for the sector. This change need not be linked to the budget, however, expectations are factoring initiation of change as discussed before during the budget session of the parliament.

Hike in tax incentives for individuals on purchase of property: The current incentive for buying property is Rs250,000 including both interest and principal repayments. The incentive for principal repayments that can be set off against taxable income is capped at Rs100,000. If this is raised further, it could prop up demand for housing and hence mortgages. Currently, mortgage loans are expected to grow by 20% over the medium term. We estimate a hike in incentive and launch of more affordable housing by the property developers could potentially take up the growth rate to 25%-30% over the next three years.

Oil and gas sector

By Nilesh Banerjee

Clarification on the definition of “mineral oil” for the purpose of 80IA deduction. We expect the finance bill to include the word “gas” under the definition of mineral oil to remove the ambiguity as to whether gas based producers are entitled to tax benefits.

Increase in budget provision for LPG and Kerosene. Cooking fuels constitute almost 50% of the gross under-recoveries and the current budget provision is in-adequate.

Increase in customs duty for crude, petrol and diesel to align with the rates that prevailed in June 2008. Increase in oil cess and rationalization of excise duties on petchem products.

Power sector

By Durga Dath

Increase in outlay for power sector: We expect the budget to earmark funds to 1) finance power generation projects in India; 2) increase rural electrification; and 3) provide incentives to reduce transmission and distribution losses (T&D). Completion of financial closure is critical for execution of power projects and timely availability of funds will reduce project timelines by approx 12-15 months. Investment in transmission and distribution segments would lead to decline in T&D losses leading to improvement in finances of state electricity boards.

Ultra mega power projects: The budget may notify setting up additional ultra mega generation and transmission power projects with the objectives of 1) enhancing power infrastructure; 2) bringing efficiencies though scale and 3) reducing rising demand/supply power deficit.

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