Angel Broking

UNION BUDGET 2020-21 PREVIEW

Bold measures need of the hour to boost growth

Given recent slowdown in the economy there are expectations that the budget would contain bold measures to boost the economy. Tight fiscal and monetary policy over the past few years coupled with major structural changes have taken a toll on growth which was further exacerbated post the IL&FS crisis and its fallout. This is reflected in the GDP numbers which slowed down to 4.5% in Q2FY20 from 8.0% in Q1FY19.

Given the shortfall in tax collections as well as lower non tax revenues (on account of shortfall in disinvestment targets), markets are concerned about fiscal slippage in FY20 and FY21. However in the backdrop of the current slowdown we believe that fiscal slippage is necessary and will go a long way in boosting growth given that India doesn't have a twin balance sheet problem like 2013.

While the corporate tax cuts was a game changer move by the Government and would go a long way in attracting investments over the medium term we believe that more needs to be done in order to boost consumption demand which has slowed down sharply from 10.6% in Q4FY18 to 5.1% in Q2FY20. Given the severity of the slowdown we feel that expansionary fiscal and monetary policy is the need of the hour to revive the economy.

Major expectations form the Union Budget

1) **Personal income tax** – The Government can try and address the slump in consumer spending by providing tax breaks to the middle class which could be either by the way of restructuring the tax slabs or by increasing the limit of the deductions under Sec 80 C.

2) **Housing** – The Government is expected to continue it's focus on affordable housing and we could see greater allocation under the Pradhan Mantri Aawas Yojna along with focus on execution. The Government could also increase the tax exemption limit on housing loan interest from current levels of ₹ 2 lakh. The Government could also look at expanding the scope of affordable housing by increasing the carpet area as well the ticket size.

3) **Auto** – the government is expected to announce measure to shore up the auto industry which was impacted by the credit crisis and implementation of BS6 norms from April 2020. There is very high probability that the Government will announce an incentive based scrappage plan in the budget which will benefit the sector, especially the MHCV space, which has been the worst impacted.

4) **Make in India** – In line with the recommendations made by the commerce ministry the Government can hike import duties on various items like paper, footwear, rubber items and toys as well as address the issues of inverted duty structure in certain sector like chemicals, furniture, rubber paper etc.

5) **Abolition of LTCG on equities and DDT** – There are expectations that the Government may abolish LTCG on equities while definition of long term can also be changed from one to two years. There are also expectations that the Government might do away with the Dividend Distribution Tax DDT on equity given that the Government want to attract investments.

FY20 Fiscal deficit and borrowing numbers expected to be on the higher side given shortfall in tax collection numbers

The Fiscal deficit estimate at 3.4% of GDP was well ahead of glide path of 3.1% for FY2020. While net borrowing figures are manageable at ₹4.73 lakh cr, gross market borrowings are already significant at ₹7.61 lakh cr in FY2020 against ₹5.71 lakh cr in FY2019.

Given a shortfall in revenues till date in FY20 and slowdown in the economy revenue targets set for FY20 in the final budget is not achievable. Nominal GDP growth has also been revised down to ~8% from earlier 11% given slowdown in GDP growth in the first half of FY20.

Fiscal deficit till November 2019 is up by 12.7% YoY and stood at 114.8% of full year's budgeted estimates despite transfer of ₹1.48 lakh cr. of surplus from the RBI against budgeted transfer of ₹90,000 cr. for FY20. There has been a significant shortfall in tax collections till date along with lower disinvestment proceeds which is expected to lead to a 20-30 bps slippage for FY20.

Fiscal Slippage a necessity to boost growth

Given that there is going to be revenue shortfall, it would be a challenge for the government to meet the fiscal deficit target of 3.3% for FY20. The Government over the past few years has generally tried to keep fiscal deficit in check by 1) Rollover of some expenditure to the next financial year, 2) Cut back in expenditure, 3) Increase in off balance sheet expenditure with portion of subsidies being transferred to state owned enterprise balance sheet.

In the past whenever there has been any pullback in government expenditure it has largely been on the capital expenditure side which is not desirable given the current slowdown in the economy. We believe that while some pullback on the revenue expenditure the Government still has enough headroom on the fiscal side to provide stimulus to the economy.

A 20-30bps increase in fiscal deficit for FY21 will not worry the markets much and some amount of fiscal slippage has already been factored in by the bond markets with the 10 year G-Sec trading at ~140bps above the repo rate as compared to normal spread of ~75bps.

Given the severity of the slowdown we feel that expansionary fiscal and monetary policy is the need of the hour to revive the economy before the slowdown becomes deep rooted and well entrenched. The RBI if required could push down long term rates by through unconventional monetary measures like Open Market Operations (OMO) or by buying longer dated bonds while selling shorter dated ones (Operation Twist).

Budget 2019-20 at a glance

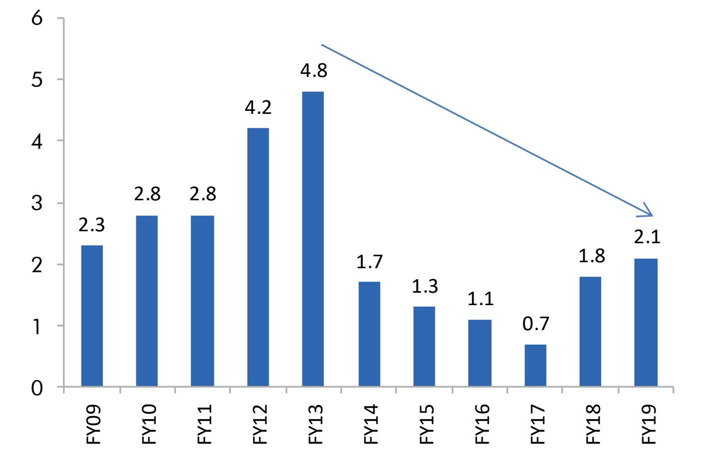
	(₹ in Cr)				YOY (%)	
Particular (₹ in Cr)	FY18A	FY19RE	FY19A	FY20BE	FY19A	FY20BE
(A) Revenue Receipts (1+2)	14,35,233	17,29,882	15,63,170	19,77,693	9	27
Gross Tax Revenue (a+b)	19,19,009	22,48,175	20,78,405	25,52,131	8	23
Devolution to States/Trf to NCCD	6,73,006.0	7,61,454.0	7,61,454	8,44,605.0	13	11
%	35.1%	33.9%	36.6%	33.1%		
1) Tax Revenue (Net to Centre)	12,42,488	14,84,406	13,16,951	17,05,046	6	29
a) Direct Taxes	10,01,974	12,00,000	11,25,220	13,80,000	12	23
Income Tax	4,30,772	5,29,000	4,61,650	6,20,000	7	34
Corporate Tax	5,71,202.0	6,71,000	6,63,570	7,60,000	16	15
b) Indirect taxes	9,16,972	10,48,175	9,53,185	11,72,131	4	23
Custom Duties	1,29,030	1,30,038	1,17,930	1,45,388	-9	23
Excise Duties	2,59,431	2,59,612	2,30,900	2,59,600	-11	12
Service Tax	81,228	9,283	6,880	0	-92	-100
GST	4,42,562	6,43,900	5,83,970	7,61,200	32	30
Others	4,721	5,342	13,505	5,943	186	-56
2) Non Tax Revenue	1,92,745	2,45,476	2,46,219	2,72,647	28	11
(B) Capital Receipts (3+4+5)	7,02,649	6,86,352	7,48,250	7,55,210	6	1
3) Recovery of Loans	15,633	13,155	17,840	12,508	14	-30
4) Disinvestment	1,00,045	80,000	85,045	90,000	-15	6
5) Borrowings and Other Liabilities	5,86,971	5,93,197	6,45,365	6,52,702	10	1
Total Receipt(A+B)	21,37,882	24,16,234	23,11,420	27,32,903	8	20
(C)Revenue expenditure	18,78,835	21,40,611	20,08,460	24,47,908	7	22
6) Of which interest payments	5,28,951	5,87,570.0	5,87,570	6,65,061	11	13
(D) Capital expenditure	2,63,140	3,16,624	3,02,960	3,36,292	15	11
Total Expenditure (C+D)	21,41,975	24,57,235	23,11,420	27,84,200	8	20
(E) Fiscal Deficit (C+D-A-3-4)	5,91,064	6,34,198	6,45,370	7,03,999	9	9
(F) Revenue Deficit (C-A)	4,43,602	4,10,729	4,45,290	4,70,215	0	6
(G) Primary Deficit (E -6)	5,91,064	46,628	57,800	38,938	-7	-33
GDP	1,68,87,543	1,86,52,882	1,90,10,200	2,07,05,853	13	9
Fiscal Deficit (% of GDP)	3.5%	3.4%	3.4%	3.4%		

Exhibit 1: Key Financial Indicators (% of GDP)

% of GDP	FY18A	FY19RE	FY19A	FY120BE
Gross Tax Revenue	11.4%	12.0%	10.9%	12.3%
Devolution to States	4.0%	4.1%	4.0%	4.1%
Net Tax to Centre	7.4%	8.0%	6.9%	8.2%
Direct Taxes	5.9%	6.4%	5.9%	6.7%
Indirect taxes	5.4%	5.6%	5.0%	5.7%
Capital Receipt (ex borrowing)	0.7%	0.5%	0.5%	0.5%
Revenue Expenditure	11.1%	11.5%	10.6%	11.8%
Subsidies	1.3%	1.6%	1.6%	1.6%
Total Capital Expenditure	1.6%	1.7%	1.6%	1.6%
Total Expenditure	12.7%	13.2%	12.2%	13.4%
Revenue Deficit	2.6%	2.2%	2.3%	2.3%
Fiscal Deficit	3.5%	3.4%	3.4%	3.4%
Primary Deficit	0.4%	0.3%	0.3%	0.2%

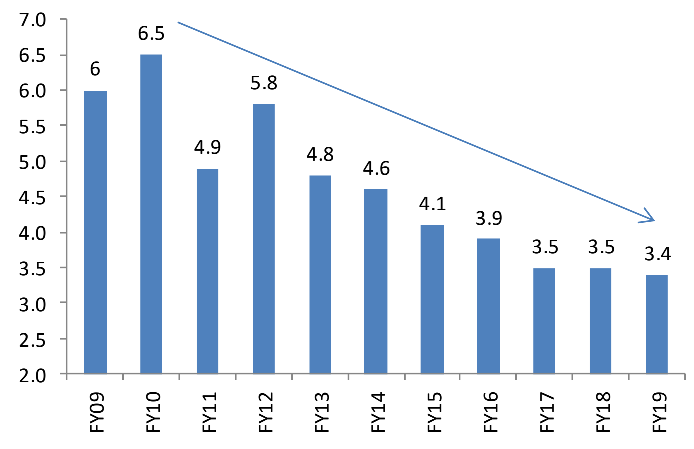
Budget document, angel Research

Exhibit 2: India Current account deficit (%)



Source: Company, Angel Research

Exhibit 3: India Fiscal deficit (%)



Source: Company, Angel Research

Likely focus areas in Union Budget

- Agriculture - Government expected to reiterate it's focus on the rural sector.
- Full benefits of the "Pradhan Mantri Kisan Samman Nidhi (PM-KISAN)" would be felt in FY21 post full rollout of the scheme.
- We also expect some further measures like tweaking of the MSP programme.
- The Government is also expected to increase outlays on the MNREGA scheme and continue it's focus on rural electrification and roads.

Impact on sectors

- Positive for all Agri input related companies, as farmer income will go up marginally.
- This will be positive for the FMCG sector, as it will increase the disposable income in the hands of rural households. Positive for FMCG companies like HUL, Dabur, Marico, etc.
- This is likely to create a positive sentiment among first time buyers for entry-level small cars, two wheelers and tractors.

Likely focus areas in Union Budget

- Infrastructure – Given that Infrastructure is one of the key focus area of the Government we don't think that there is going to be any cut back in capital expenditure for FY21 despite shortfall in revenues.
- We believe that the Government would use the Union Budget to highlight their plans and execution over the next five years. Recently released National Infrastructure Pipeline (NIP) gives us broad idea about investment by Government in Infrastructure.

Impact on sectors

- Positive for L&T and other Infrastructure (Road) companies such as PNC Infratech, KNR Constructions etc
- Positive for cement companies such as Ultractech, ACC, Shree Cement, JK Laxshmi etc.
- Positive for railways allied companies like Titagarh Wagons, Texmaco Rail etc.

Likely focus areas in Union Budget

- Housing - The Government could also try and stimulate the economy by increasing the tax breaks available for interest paid on housing loans which would lower taxable income in the hands of the salaried class.
- The Government can also look at expanding the definition of affordable housing by increasing the ticket size and area which will bring more projects within the ambit of affordable housing policy.

Impact on sectors

- Positive for Real estate companies like Sobha Developers & Godrej Properties.
- Positive for housing allied sectors like paints, plywood tiles and cement.

Likely focus areas in Union Budget

- Make in India – There are expectations that there could be sector specific increase in import duties on specific items while the inverted duty structure on certain sectors could also be rationalized.

Impact on sectors

- Positive for sectors like footwear, chemicals & agrochemicals

Likely focus areas in Union Budget

- Gold – Lowering import duty on gold from current 12.5%

Impact on sectors

- Reduction in import duty will reduce the price of gold. This would create buying sentiment in consumer which will be Positive for companies like Titan.

- Auto - The year 2019 was one of the toughest years the Indian automobile industry has had to undergo as a severe slump in sales affected almost all vehicle manufacturers. Wish list of the sector from Budget 2020 are – (a) GST reduction (on vehicles) from the existing 28% to 18% even if with a sunset clause; (b) Incentive-based scrappage policy; (c) Abolition of duty on import of lithium-ion battery cells; (d). Increase in re-registration charges of vehicles to discourage use of old vehicles; (e) Withdraw proposed hike in vehicle registration fees.

- GST reduction on vehicles to boost consumption on the back of slackening demand and price hikes led by BSVI implementation from April 2020. (Positive for all OEMs across the segments.
- The policy will make it obligatory to dispose of old vehicles (older than a specified period of holding) which will create demand for new (commercial) vehicles in the market. (Positive for companies like Ashok Leyland, Tata Motors, M&M, Automotive axle etc in CV space.
- Lithium-ion is vital to develop the EV ecosystem in India, notably battery manufacturing. The finance minister should also give incentives for local manufacturing of EV batteries.
- Increase in re-registration charges of vehicles to discourage use of old vehicles will boost new demand.

Budget Picks

	CMP	Target Price	Sales (₹ Cr)		OPM (%)		PAT (₹ Cr)		ROE (%)		P/E (x)		EV/Sales (x)	
			FY20	FY21	FY20	FY21	FY20	FY21	FY20	FY21	FY20	FY21	FY20	FY21
L&T	1,352	1,809	91,855	1,02,877	9.8	9.8	8,637	8,721	15.6	14.3	21.9	21.8	2.1	1.8
Ultratech Cement	4,643	4,984	4,3916	47,482	22.3	22.7	4,051	4,670	12.3	11.8	33.0	28.7	3.5	3.2
Ashok Leyland	86.45	95	21,193	23,376	9.6	9.9	1,103	1,228	12.6	12.8	22.9	20.6	1.0	0.9
Kajaria Ceremics	574	671	3,209	3,564	15.2	15.7	286	339	15.8	16.1	32.0	26.9	2.8	2.5
Sobha Dev.	439	500	3,786	4,152	19.9	20	313	377	13.4	14.4	13.2	11.1	-	-

Particular	CMP	Target Price	NII (₹ Cr)		PAT (₹ Cr)		EPS (₹)		ROE (%)		P/BV (x)	
			FY20	FY21	FY20	FY21	FY20	FY21	FY20	FY21	FY20	FY21
Canfin Homes	471	534	601	728	367	449	28	34	19	19	2.9	2.5

CMP is Closing price as of 24th January 24, 2020

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