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Indian Budget 2010-11 An Effort to Sustain Growth Momentum

Introduction:

The economic growth continues to be quite resilient in India despite the global crisis, and the business sentiments, which were earlier impacted, have been improving especially for the past two quarters. The Indian economy grew by 6.7 percent during the fiscal year 2008-09, lower than the robust annual growth of plus 9 percent in the previous three years. During the first three quarters of the current fiscal year (2009-10), the economy grew by 6.7 percent. The growth was very much supported by the stimulus packages initiated by the government, which also resulted in heightening the fiscal deficit to 6.7 percent of GDP (2.6 percent in 2007-08). This year, the government is facing three major challenges, i.e. sustain the growth momentum, reduce high fiscal deficit, and strengthen the measures for 'inclusive' growth in the country. The Union Budget 2010-11 presented in the Parliament reflects government's move to meet these challenges and at the same time address a pressing problem - inadequate infrastructure - as it hinders the optimum utilisation of business potential existing in the country.

Some key budgetary proposals relevant for business:

- To reduce surcharge on corporate tax from 10% to 7.5%, bringing the corporate tax rate down marginally from 33.99% to 33.22%
- To increase Minimum Alternate Tax from 15% to 18%
- To give tax benefits to individuals by increasing income tax slabs in order to propel private consumption
- To introduce Goods and Services Tax (GST) and Direct Tax Code (DTC) from 1 April 2011
- To reduce customs duty on specified equipment meant for renewable energy, infrastructure, and agriculture sectors
- To reduce SAD (special additional duty) on import of most medical equipments
- To increase customs duty on crude oil by 5%, and increase excise duty on diesel oil
- To increase general excise duty rate from 8% to 10%, in a way bringing the rate of taxation of goods and services at the same level
- To enlarge Service Tax net by including new services, e.g. health services provided by insurance companies, brand promotion services etc.
- To increase the weighted deduction for in-house R&D expenses from 150% to 200%, and from 125% to 175% for contributions for R&D activities in approved research institutions
- To give new licences to private sector banks.

Impact on some specific sectors:

Food/Agriculture: A number of measures have been announced to help increase agricultural output in the country. For example, equipment to set up cold storage facilities, industrial units

to process food items would attract lower import duties, as these will be considered as 'project' imports. A new strategy is planned to increase food grains, pulses, and oil seeds production.

Pharmaceutical: The increase in weighted deduction on account of R&D expenditure will have positive effects on pharmaceutical, and other knowledge-based industries.

Power: High allocation for the infrastructure sector will provide a fillip to the power equipment industry as well. The government has increased the outlay on power sector by 100 percent, that will eventually lead to higher capacity creation in this sector.

Renewable energy: Increasing allocation for the renewable energy sector by 61% is a good sign of government's plan to address the issues of climate change and energy security. The new National Clean Energy Fund, which will be funded through an energy cess on coal consumption, is expected to help introduce/develop innovative technologies in this field. The government has also announced reduction in excise duty on certain parts used in wind turbines as well as LED lights.

Consumer goods: The government has exempted the pre-packaged goods from additional duty (4%), as these goods are meant for retail sale. The exemption has also been provided to mobile phones, watches, and garments. This measure will help reduce blockage of funds by importers who have to face substantial compliance costs in getting refunds of this additional duty after payment on VAT at the time of actual sale.

Comments:

The Indian economy grew by 6.7 percent in the first three quarters of the current fiscal year, and the government estimates the GDP growth to be 7.2 percent this year (industry 8.2, agriculture -0.2, services 8.7 percent). That means the economy must register a growth of 8.8% in the fourth quarter ending 31st March 2010. It should be possible to reach this figure provided the agriculture sector shows good revival and the buoyancy seen in industrial growth in recent months (16.8 percent y-o-y growth registered in December 2009) is maintained. On external front, the scenario has improved as both imports and exports have come out from negative growth trajectory to good growth in the previous 2-3 months. In January 2010, the exports grew y-o-y by 11.5 percent and imports by 35.5 percent.

Corporate India did have great expectations from the budget this year as the economic recovery, mainly due to government stimuli, is still at a nascent stage. However, they were of the opinion that the time was good to introduce some significant reforms, but this did not happen. The plan towards fiscal consolidation has also been appreciated by the business community, though it involves a partial roll back of stimulus package, but will help to strengthen the macroeconomic fundamentals of the economy. The companies are 'positive' on consumption push due to increased fund allocations on various rural development schemes, infrastructure, and availability of more money in the hands of middle class. The moderate excise duty increase will not have much adverse impact on the growth buoyancy, and most of the manufacturers will be able to pass on this increase to the customers. However, this, together with the hikes in fuel prices, could put upward pressure on the inflation which is already roaming around 8 percent.

A key demand of Corporate India will be met next year, if the government is able to implement Goods and Services Tax and Direct Tax Code effective 1st April, 2011. The task is not easy to accomplish, but will definitely help to create better and predictable business environment in the country.

The government has planned to mop up INR 400 billion from sale of shares in public enterprises and INR 350 billion from auction of telecom spectrum. This will assist in partially

reducing the fiscal deficit to 5.5% in 2010-11. The government has announced to include off-budget subsidies such as oil bonds and fertilizers bonds in the fiscal deficit to give a more transparent scenario of the fiscal health of the economy in future.

For Swiss companies looking for partnership with Indian industry to do research and development work here will find the conditions more conducive. The companies engaged in the infrastructure sector, e.g. power equipment, cement etc., will have better business opportunities. The emphasis on the development of renewable energy sector will bring out increased opportunities for business partnerships with Indian companies.

Government's commitment to continue with its reform process, albeit only tax reforms in the near term, and to maintain growth momentum to achieve 9 percent GDP growth by 2011-12 is a positive sign. The increased outlays on infrastructure, rural development schemes, energy sector will certainly fuel demand and help the economy to move forward, but sustaining future growth at the desired 9 percent is unlikely unless and until the human and physical infrastructure constraints are firmly tackled.