

In a national address on 31 December 2016, Prime Minister, Narendra Modi announced a slew of measures to offset some of the demonetisation pain – Budget rural housing schemes, interest waiver for sowing loans, social welfare schemes and improving the ‘ease of doing business’ for traders/MSMEs. As expected, the focus was also on boosting digital transactions and doling out more through direct benefit transfers (DBTs). However, no mention was made of expected gains from currency delegalisation, the source from which large-scale stimulus to the economy was expected. Given the economic impact on rural India, and trading and manufacturing sectors, we expect more such imminent measures in CY17 Union budget. Enhanced MNREGA focus, possible minor individual income tax cuts and more tax breaks to small traders/MSMEs (NDA’s key vote bank) are anticipated. Populist measures will also find favour given the upcoming state elections in key states of Uttar Pradesh, Punjab etc. Interest rebate of 3-4% on small-ticket home loans in CY17 may not be negative for banks as such subvention will be compensated for by the government. Added push to rural housing under Pradhan Mantri Awaas Yojana would be positive for aggregate demand. Housing/construction sector is one of the largest job providers and hence critical for economic revival. While we were positive on the market when the previous budget shifted its focus to consumption and bolstering income, a populist budget this year may not be taken positively if enough currency delegalisation gains do not materialise. We retain our top picks, focussing on export-related segments, B2B category, regulated returns and OMCs, while avoiding consumer-facing companies.

- Lacking stats on demonetisation:** Contrary to expectations, PM’s recent address did not provide any details on delegalised currency deposited into the banks or on declaration under the new amnesty scheme – He only mentioned that the guilty would not be spared. The PM mentioned that merely 2.4m filed returns showing income in excess of Rs1m, which implies that the government could work towards increasing this number rapidly. However, despite insinuations on tax crack-downs, no specific action plan was mentioned.
- Cash crunch to continue:** In the latest RBI circular, ATM cash withdrawal limit has been increased to Rs4,500 per day from Rs2,500 – The overall withdrawal limit has been retained at Rs24,000/week. As the remaining restrictions continue to hold, we believe, it would take another 4-5 months (time required to replenish cash in the system) for normalcy to return. For details on currency printing expectations, please refer our note ‘*Delegalisation maths*’ dated 24 November, 2016.
- Ongoing policy support for digital payments:** Given the ensuing cash crunch emanating from lack of enough physical currency, the government has increased its focus on digital payment infrastructure. The PM elucidated on benefits of digital transactions. Key announcements were tax breaks for small businesses transacting digitally and easier working capital loans. However, the key question is to which extent digital transactions will absorb the economic disruption caused by non-availability of cash in near term. To understand this better, we analysed the penetration of retail digital payments in overall non-cash transaction eco-system. Retail electronic transfers were ~5% of total payment ecosystem and digital payments (POS sales, m-wallet and PPI transactions) 0.3% of the total transactions, while cash accounted for ~16% of total transactions. Given the very small size of digital retail transactions, possible absorption of economic disruption from ensuing cash crunch seems a long drawn affair (Exhibit below).

**Digital retail payments are 0.3% of total non-cash transactions**

	Total value of non cash transaction (Rs bn)*	yoy, (%)	Digital payments (retail) #	yoy, (%)	Share ^	Retail electronic transfers	yoy, (%)	Share ^
2011-12	10,66,547	8.5%	1,562	36.8%	0.1%	20,576	72.3%	1.9%
2012-13	13,12,601	23.1%	2,052	31.3%	0.2%	31,881	54.9%	2.4%
2013-14	14,99,794	14.3%	2,575	25.5%	0.2%	47,856	50.1%	3.2%
2014-15	16,61,194	10.8%	3,326	29.1%	0.2%	65,366	36.6%	3.9%
2015-16	18,13,742	9.2%	4,483	34.8%	0.2%	91,408	39.8%	5.0%
2016-2017 (YTD)	12,71,436	22.1%	3,319	34.4%	0.3%	67,495	39.2%	5.3%

Source: RBI, IDFC Securities Research

\*[Less ATM transactions], # [includes POS sales and transactions through m-wallets and PPI cards], ^ Share as a percentage of overall payments ecosystem

- **Expect more dole-outs via DBT in FY18 Union Budget; DBT timelines to be met:** Transfer of sowing loan interest waivers and social welfare benefits for pregnant women through DBT was announced. We expect more subsidies to be brought under DBT in the forthcoming Budget, in line with FY18 deadline for full DBT implementation. PDS (food subsidy) and fertiliser subsidy transfer pilots for DBT are ongoing in 16 districts of India. These subsidies stand at ~Rs2trn of total Rs2.5trn annual subsidies. Our interaction with bureaucrats in a few sample districts indicated a timeline adherence on DBT implementation.
- **Enhanced focus on rural economy:** The government has waived-off 60-day interest on existing farm loans taken in the Rabi season from district cooperative banks and primary societies. Similarly, to allow lending at cheaper rate by refinance agency, the government is expanding NABARD's lendable corpus pool by Rs200bn from existing Rs210bn. Also, 30m farmers with Kisan credit cards would be given RuPay debit cards within three months so that they can transact anywhere (rather than visiting banks to withdraw money).

As the rural economy has been hit more by demonetisation, most welfare schemes were focused on rural India and 'bottom of pyramid' population. We expect FY18 Union budget to continue with this theme, in line with recent measures (focus on budget housing, interest waiver for farmers and welfare schemes for women/senior citizens). We also expect DBT focus to intensify.

- **Thrust on Housing/construction segments - Interest rebate on small-ticket home loans announced for poor/middle class.** About 3-4% of interest rebate on new home loans in 2017 should boost housing demand. Also, rural housing push under Pradhan Mantri Awaas Yojana would be positive for sectors such as cement and Iron & Steel. We do not expect this to be negative for banks as the government is likely to provide interest subvention (similar to farm loans).

However, we are awaiting clarity on the property value for availing this interest subvention. To illustrate, priority sector lending (PSL) definition has a similar clause of individual loans up to Rs2.8m (metros) and Rs2m (other centres) which would qualify for PSL provided the cost of dwelling should not increase to Rs3.5m and Rs2.5m, respectively.

Housing/construction sector is one of the largest job providers and hence is critical for economic revival. Any boost to this segment should add to economic growth through backward and forward linkages. **Three major announcements for this segment are:**

- A 4% interest rebate on home loans up to Rs0.9m and 3% interest rebate on home loans up to Rs1.2m for urban poor.
- A 3% interest rebate on home loans up to Rs0.2m for new housing or extension of housing in rural areas.
- A 33% increase in number of houses built for rural poor under Pradhan Mantri Awaas Yojana.

**Benefits for trader community and MSME:** While most welfare schemes had rural/social focus, a few announcements were made for traders/MSMEs. Our ground research on demonetisation indicated that traders/MSMEs saw a drop in business activity given their high cash dependence (refer our demonetisation report, *'What's moving on the ground! - Demonetization special'* dated 13 December, 2016). Hence, the schemes focused on easing working capital and tax breaks. Following are the key schemes:

- Cash credit limit for small businesses increased to 25% from 20%.
- Credit guarantee for small traders to be increased to Rs20m from Rs10m.
- For enterprises transacting digitally, working capital loans to be increased to 30% of turnover from 20%.
- For MSMEs with turnover up to Rs20m, taxes were calculated at 8% of the turnover. For businesses transacting digitally, this number would come down to 6%, thus bringing the effective tax down by 25%.

Though these schemes will improve the 'ease of doing business' currently, the compensation may not be up to the point of business lost, given the high cash dependence. Hence, we need to monitor the pace of adjustment (new ways of doing business) and economic value lost in this process.

- **Populist budget likely given upcoming state elections:** As discussed earlier, we expect the budget to offer more benefits to 'bottom of pyramid' population, and increase focus on rural economy and improving DBT share. Hence, we expect enhanced allocation towards MNREGA, tax breaks for small traders/MSMEs (NDA's key vote bank) and some tax relaxation on individual income tax (to pacify expectations of demonetisation benefits).

**Exhibit 1: Major announcements**

Sectors	Key benefits	Major announcements
<b>Housing sector</b>	Interest rebate	<ul style="list-style-type: none"> <li>4% on HLs up to Rs0.9m and 3% on HLs up to Rs1.2m for urban poor</li> <li>3% on HLs up to Rs0.2m in rural areas.</li> </ul>
	Pradhan Mantri Awaas Yojana	<ul style="list-style-type: none"> <li>33% increase in number of houses built for rural poor</li> </ul>
<b>Farm sector</b>	Interest waiver	<ul style="list-style-type: none"> <li>60-day interest waiver for farm loans (Rabi crop) from district cooperative banks and primary societies.</li> </ul>
	Higher NABARD lendable corpus	<ul style="list-style-type: none"> <li>Expanding NABARD's lendable corpus pool by Rs200bn to provide farmers with better access to loans.</li> </ul>
	Issuance of RuPay debit cards	<ul style="list-style-type: none"> <li>30m farmers with Kisan credit cards to be given RuPay debit cards within three months.</li> </ul>
<b>MSME</b>	Increased credit limit	<ul style="list-style-type: none"> <li>To increase cash credit limit to small businesses to 25% of turnover from 20%.</li> <li>To increase working capital loans to 30% of turnover from 20% earlier for enterprises using digital transactions.</li> </ul>
	Credit guarantee	<ul style="list-style-type: none"> <li>For small entrepreneurs, credit guarantee would be raised from Rs10m to Rs20m.</li> <li>This will cover loans given by NBFCs also.</li> </ul>
	Lower tax liability	<ul style="list-style-type: none"> <li>Tax liability lower by 25% - business income from digital transactions with turnover of up to Rs20m will now be calculated at 6% of turnover (non-digital: 8%).</li> </ul>
<b>Women/weaker section</b>	Financial assistance to pregnant women	<ul style="list-style-type: none"> <li>Rs6,000 to be transferred directly to bank accounts of pregnant women.</li> </ul>
	Double the reach of MUDRA Yojana	<ul style="list-style-type: none"> <li>Planning to benefit 70m with priority given to dalits, tribals, backward classes and women.</li> </ul>
<b>Senior citizen</b>	Interest on FDs	<ul style="list-style-type: none"> <li>To earn a fixed 8% interest on deposits of up to Rs0.75m for 10 years</li> </ul>

Source: PIB, Government of India

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