MOTILAL OSWAL
Investment Services

# Union Budget 2023-24


## Populism gives in to investment-led spending growth strategy

### Modest fiscal consolidation continues in FY24BE

The Union Budget 2023 was presented on 1st Feb'23 amid high expectations. Since this was the last full budget before 2024 General Elections, it was expected that the government could announce some income support for the rural sector or implement some measures to boost consumption growth in the economy. However, the government did not give in to these expectations and continued with its investment-led spending growth strategy along with modest fiscal consolidation. Although the Economic Survey projected a nominal GDP growth of 11% YoY in FY24, the Budget assumed 10.5% nominal GDP growth next year.

**Fiscal deficit budgeted at 5.9% of GDP in FY24BE, kept unchanged at 6.4% of GDP in FY23RE:** Contrary to our expectation of lower-than-budgeted deficit in FY23, the Government of India (GoI) kept it unchanged at 6.4% of GDP in FY23. This means that fiscal deficit was revised up to INR17.6t in FY23, from BE of INR16.6t. At the same time, the GoI has budgeted the deficit at 5.9% of GDP (INR17.9t) for next year, which is in line with the market consensus but higher than our expectations of 5.7%. Total liabilities of GoI are likely to rise to 56.2% of GDP in FY24BE from 55.9% of GDP in FY23RE owing to weaker growth and modest consolidation. Moreover, although the bonds market cheered the lower-than-expected gross market borrowings (albeit net borrowings were in line with the market consensus), the GoI has assumed another INR4.7t worth of financing from small savings. The latter seems highly ambitious to us, and any shortfall in FY24E could mean either lower spending growth and/or higher market borrowings.

**Tax receipt estimates more realistic v/s extreme conservatism in the past two years:** As highlighted in our Budget preview, the GoI could not have afforded to be conservative in its receipt estimates amid an expected general global slowdown in CY23. Accordingly, the GoI has budgeted 10.4%/11.7% YoY growth in gross/net taxes in FY24BE against 12.3%/15.7% in FY23RE, respectively. Although we expect nominal GDP growth to be much weaker than the GoI's expectations, we also believe that tax buoyancy could be better. Thus, we do not expect any shortfall in tax receipts next year. Further, while the GoI could also meet its non-tax revenue receipts, there may be some challenge to meet its divestment target (of INR610b) next year.

**GoI continues to focus on better spending quality:** At a time, when there were high expectations to announce measures to support the rural sector, the GoI kept revenue expenditure growth at minimal (just 1.2% YoY), and propelled capital expenditure (capex) strongly for the third consecutive year. Excluding subsidies, revenue expenditure is budgeted to grow 7% YoY in FY24BE, marking the slowest growth in eight years. GoI's capital spending, however, is budgeted to grow 37.4% YoY in FY24BE following a 23% YoY growth in FY23RE. The government's capital spending has surged almost 2.5x in the past three years to INR10t in FY24BE from INR4.2t in FY21. Since total government expenditure is budgeted to grow just 7.5% in FY24BE, the share of capital spending is budgeted to rise to 22.2% of total spending, marking the highest share in 18 years (up from just 12-13% in pre-Covid years).

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**Including IEBR, however, investment growth is more modest:** Notably, as highlighted in our recent report, a large portion of GoI's higher capex is re-allocated from the internal and extra-budgetary resources (IEBR) of public sector enterprises (PSEs). Including IEBR, the aggregate capex is expected to fall sharply to just 3.5% of GDP in FY23RE, before recovering to 3.9% in FY24BE, same as in the pre-Covid years.

**Overall, it was a relief to see the GoI resisting populism pressures. At the same time, neither the aggregate capex growth nor the tweaks in taxation is likely to make a big difference. With 5.9% budgeted deficit in FY24E, the task of bringing it down to 4.5% of GDP becomes even more challenging. It is possible only and only if the GoI keeps its spending growth extremely muted for the subsequent two years, thus restricting its ability to support economic growth.**

## Market strategy

The Union Budget 2023 was presented amid a backdrop of rising global headwinds with slow-down in growth, higher rates and geopolitical volatilities. India's sharp outperformance in CY22 has started fading in Jan'23 with a relatively muted corporate earnings season coupled with sharp FII selling (CYTD USD3.7b).

However, the Budget presented by the Honorable Finance Minister has demonstrated continuity and builds on last year's budget announcements with intensifying focus on capex. Navigating the growth paradox amid an increasingly volatile global backdrop remains the key challenge. The GoI has largely continued with its focus on driving capex by enhancing the gross budgetary support for roadways, railways and defense sectors. The budget had a strong focus on capex and infrastructure development as well as giving more money in the hands of the middle class and improving agri income along with job creation through skill development for the weaker section. The new increased tax rebate would benefit the salaried class and aid in boosting consumption.

Resisting the temptation of populist giveaways ahead of the nine state elections in CY23, the government has largely remained on course with a focus on long-term structural growth drivers. Fiscal deficit is expected to moderate to 5.9% in FY24BE from 6.4% in FY23RE. The budget numbers look pragmatic on revenue receipts and the overall budget projections look credible in our view. The bond markets reacted favorably to the gross market borrowings and net borrowings of INR15.4t and INR11.8t, respectively, which were in-line with market expectations.

Overall from an equity market perspective, we believe the budget, on balance, has no unpleasant surprises while there remains some room for consumption push as there is a clear evidence of demand moderation in corporate commentaries from the ongoing 3QFY23 earnings season. Though there are some disappointments on the absence of measures to improve consumption, moderation in inflation with stability in commodity prices will offer some hope to revive consumption growth.

Given the continuity of policy focus and pronouncements, we believe markets will discount the budget and shift their focus to: a) overall growth-inflation paradigm in a challenging global backdrop and b] corporate earnings growth trajectory, which has remained resilient so far in 1HFY23 (albeit witnessing some challenges with downgrades outweighing upgrades in 3QFY23). The forthcoming RBI policy meet will be an important policy event to gauge any pause in the near-term monetary tightening measures. After the recent correction, valuations are in the fair value zone with Nifty trading at 17.5-18.0x FY24E EPS band and thus offering room for upside if the corporate earnings delivery continues. We prefer BFSI, IT, Industrials, Auto and Cement while we are UW on Energy in our model portfolio.

**Top ideas: Large-caps –** L&T, Axis Bank, Bajaj Finance, Bharti Airtel, TCS, ITC, Titan, ONGC, Maruti, and Sun Pharma.
**Mid-caps –** Samvardhana Motherson, APL Apollo, Dalmia Bharat, Angel One, and Lemon Tree.

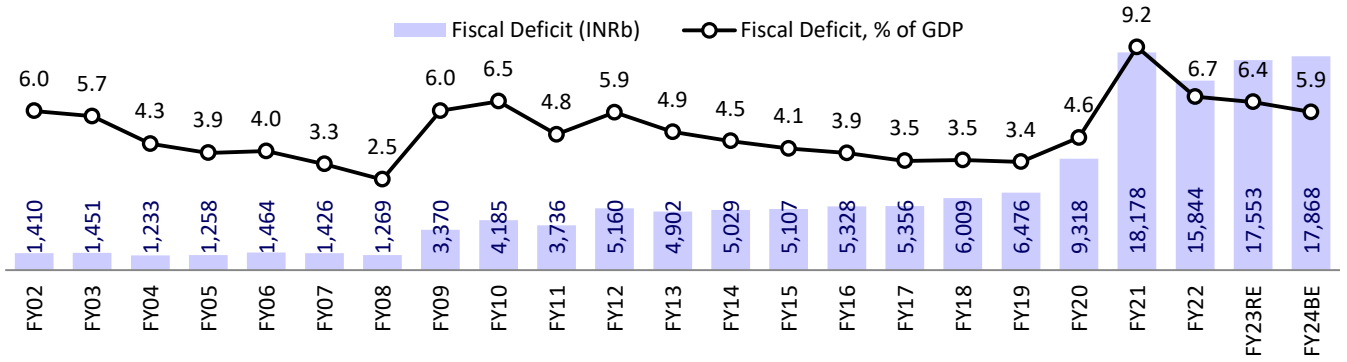
## FY24 gross borrowings lower than market expectations

**Fiscal deficit estimated at 6.4%/5.9% of GDP in FY23/FY24, respectively**

Unlike the past two years, the Union Budget 2023 estimates appeared neither conservative nor over optimistic. While there were barely any deviations between the government's revised estimates and our forecasts for FY23, there were some (albeit minor) deviations between the budgeted estimates and our FY24 forecasts.

While the government raised its total receipt estimates to INR24.3t in FY23RE (from INR22.8t in FY22BE), the expenditure target was elevated to INR41.9t in FY23RE (from INR39.4t in FY22BE). After making these changes, the fiscal deficit stands at INR17.6t in FY23RE (from INR16.6t in FY23BE). However, due to a relatively higher nominal GDP growth of 15.4% YoY in FY23 v/s the earlier expected 9% YoY in FY22BE, government's fiscal deficit remains unchanged at 6.4% of GDP in FY23RE. Further, the government expects total receipts to rise 11.7% YoY to INR27.2t in FY23RE (as against our forecast of 9.4% YoY growth to INR26.8t). It assumes total expenditure to grow 7.5% YoY to INR45.0t (v/s our assumption of 5.5% YoY growth to INR43.5t). Therefore, in line with broad market expectations, the government has pegged FY24E fiscal deficit at 5.9% of GDP (assuming nominal GDP growth rate of 10.5% YoY, higher than our **expectation** of 7.0-7.5% YoY – refer to *Exhibit 1)*.

**Exhibit 1: Trends in fiscal deficit over the past two decades; fiscal deficit expected to reduce to 5.9% of GDP in FY24BE**




Source: Government, MOFSL

With higher estimated total expenditure combined with lower nominal GDP growth in FY24, the government expects NMBs at INR11.8t and GMBs at INR15.4t, lower than market consensus of INR16t

The gross market borrowings (GMBs) and net market borrowings (NMBs) for FY23 have been revised marginally to INR14.2t (from INR15.0t in FY22BE) and INR11.1t (from INR11.2t in FY23BE), respectively *(Exhibit 2)*. With higher estimated total expenditure combined with lower nominal GDP growth in FY24E, the government expects NMBs at INR11.8t and GMBs at INR15.4t, lower than market consensus of INR16t. These led to marginal cheer in the debt market as the benchmark 10-year bond yield dropped 6bp to 7.28% on 1st Feb'23 as against 7.34% as on 31st Jan'23.

What surprises us is that the government plans to fund 26% of its fiscal deficit through small savings schemes. Excluding FY21/22 (Covid years, when on an average, ~31% of fiscal deficit was financed through small savings), this is one of the highest percentage share of small savings. We believe that this is unlikely to work out for the government considering only INR1.7t (38% of FY23RE) has been raised in the first nine months of FY23 and the situation might be similar even in FY24. If so,

the government might not have much choice than to either cut their spending target (to reduce their fiscal deficit) or increase their borrowing sometime in the second half of FY24. Neither of them will be welcomed by the debt market *(Exhibit 3)*.

**Exhibit 2: NMBs to grow only slightly to INR11.8t in FY24 and short-term borrowings to actually reduce…**

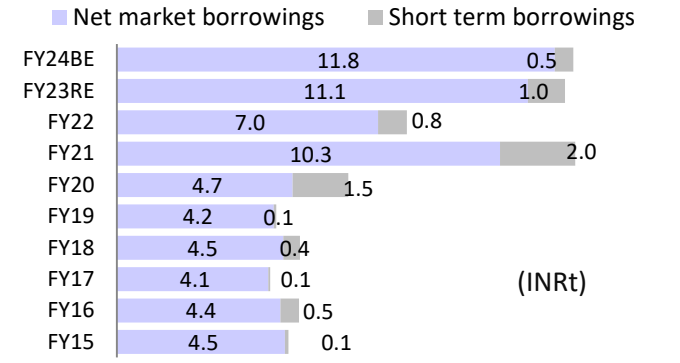
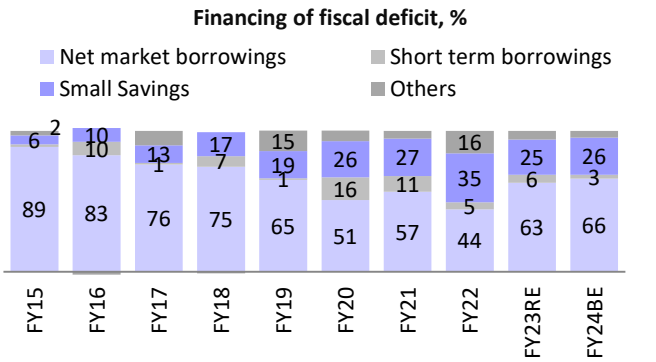



**Exhibit 3: …because over one-fourth of the fiscal deficit is expected to be financed by small savings**




Source: Government, MOFSL

**Exhibit 4: Union Budget 2023-24 in numbers**

| | FY21 | FY22 | FY23RE | | | FY24BE | | |
|---|---|---|---|---|---|---|---|---|
| | INR t | INR t | INR t | % YoY | % of GDP | INR t | % YoY | % of GDP |
| **Total Receipts** | **16.9** | **22.1** | 24.3 | **10.1** | **8.9** | 27.2 | **11.7** | **9.0** |
| Revenue receipts | 16.3 | 21.7 | 23.5 | **8.2** | **8.6** | 26.3 | **12.1** | **8.7** |
| Gross Taxes | 18.9 | 27.1 | 30.4 | **12.3** | **11.1** | 33.6 | **10.4** | **11.1** |
| Net Taxes | 14.3 | 18.0 | 20.9 | **15.6** | **7.6** | 23.3 | **11.7** | **7.7** |
| Direct taxes | 9.4 | 14.1 | 16.5 | **17.2** | **6.0** | 18.2 | **10.5** | **6.0** |
| Corporation Taxes | 4.6 | 7.1 | 8.4 | **17.3** | **3.1** | 9.2 | **10.5** | **3.1** |
| Income Taxes | 4.9 | 7.0 | 8.2 | **17.1** | **3.0** | 9.0 | **10.5** | **3.0** |
| Indirect taxes | 9.4 | 13.0 | 13.9 | **7.1** | **5.1** | 15.4 | **10.4** | **5.1** |
| Customs | 1.3 | 2.0 | 2.1 | **5.1** | **0.8** | 2.3 | **11.0** | **0.8** |
| Excise Duties | 2.5 | 3.9 | 3.2 | **-18.9** | **1.2** | 3.4 | **5.9** | **1.1** |
| Goods & Services Tax (GST) | 5.5 | 7.0 | 8.5 | **22.3** | **3.1** | 9.6 | **12.0** | **3.2** |
| Devolution to states | 6.0 | 9.0 | 9.6 | **5.7** | **3.5** | 10.3 | **7.7** | **3.4** |
| Non-tax revenue | 2.1 | 3.7 | 2.6 | **-28.3** | **1.0** | 3.0 | **15.2** | **1.0** |
| Non-debt capital receipts | 0.5 | 0.4 | 0.8 | **112.1** | **0.3** | 0.8 | **0.6** | **0.3** |
| Divestment | 0.3 | 0.1 | 0.6 | **309.9** | **0.2** | 0.6 | **1.7** | **0.2** |
| **Total Expenditure** | **35.1** | **37.9** | 41.9 | **10.4** | **15.3** | **45.0** | **7.5** | **14.9** |
| Total excl. Subsidies | 27.5 | 32.9 | 36.3 | **10.2** | **13.3** | 41.0 | 13.1 | **13.6** |
| Revenue expenditure | 30.8 | 32.0 | 34.6 | **8.1** | **12.7** | 35.0 | 1.2 | **11.6** |
| Interest payments | 6.8 | 8.1 | 9.4 | **16.8** | **3.4** | 10.8 | 14.8 | **3.6** |
| Defense | 2.2 | 2.3 | 2.6 | 13.5 | **1.0** | 2.7 | 4.1 | **0.9** |
| Subsidies | 7.6 | 5.0 | 5.6 | 11.5 | **2.1** | 4.0 | -28.3 | **1.3** |
| Pensions | 1.7 | 2.0 | 2.4 | 23.0 | **0.9** | 2.3 | -4.3 | **0.8** |
| Grants to states/UTs | 5.7 | 6.2 | 6.1 | -0.5 | **2.2** | 6.6 | 7.6 | **2.2** |
| Non-defense Pay/allowances | 3.3 | 2.5 | 2.8 | 12.3 | **1.0** | 2.9 | 5.1 | **1.0** |
| Other | 3.6 | 6.0 | 5.6 | -6.6 | **2.0** | 5.6 | 0.3 | **1.9** |
| Capital expenditure | 4.3 | 5.9 | 7.3 | 22.9 | **2.7** | 10.0 | 37.4 | **3.3** |
| **Fiscal Deficit** | **18.2** | **15.8** | **17.6** | | **6.4** | **17.9** | | **5.9** |
| **Revenue Deficit** | **14.5** | **10.3** | **11.1** | | **4.1** | **8.7** | | **2.9** |
| **Capital Deficit** | **3.7** | **5.5** | **6.4** | | **2.4** | **9.2** | | **3.0** |
| **Primary Deficit** | **11.4** | **7.8** | **8.1** | | **3.0** | **7.1** | | **2.3** |
| **Nominal GDP** | **197.5** | **236.6** | **273.1** | **15.4** | | **301.8** | **10.5** | |

Source: Union Budget documents, MOFSL

## FY24 receipt expected to grow 12% YoY v/s 10% in FY23

Following a 3.6% YoY growth during 9MFY23, the government expects total receipts to grow 10.1% YoY to INR24.3t in FY23. This implies that 4QFY23 total receipts are likely to rise sharply by 36.1% YoY, which we believe is achievable.

Following a 3.6% YoY growth during 9MFY23, the government expects total receipts to grow 10.1% YoY to INR24.3t for the entire year. This implies that 4QFY23 total receipts are expected to rise sharply by 36.1% YoY, which we believe is achievable given the high GST collections and expected advance direct tax collections during the quarter. Based on FY23RE, the government assumes total receipts to grow 11.7% YoY to INR27.2t in FY24BE. We believe this is a normal target to assume; it is neither conservative, nor over optimistic. As a percentage of GDP, however, total receipts are expected to remain largely flat at 8.9%/9.0% in FY23/24, respectively, (similar to 8.9% average seen during FY18-22; *Exhibit 5)*.

Within total receipts, the government has estimated a ~16% YoY growth in net taxes and a contraction of ~28% YoY in non-tax receipts in FY23. The decline in non-tax revenue stems mainly from very low dividends received by the government this fiscal. The net tax receipts are likely to grow only 11.7% YoY and non-tax receipts are actually projected to grow 15.2% YoY in FY24 (which will be due to a low base). Therefore, net taxes are likely to account for ~86% of total receipts in FY24, similar to that in FY23 *(Exhibit 6)*.

**Exhibit 5: Receipts expected to grow decently…**

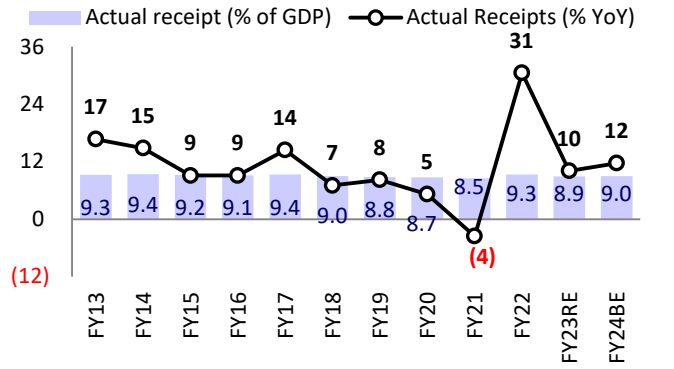
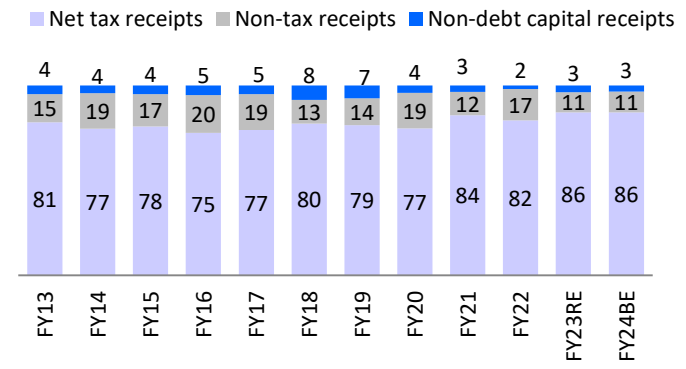



**Exhibit 6: …taxes to account for 86% of receipts in FY24BE**




Source: Union Budget documents, MOFSL

Due to a 10.4% YoY growth in gross tax revenue and 10.5% YoY growth in nominal GDP, government is expecting a tax buoyancy of 1x in FY24, higher than 0.8x in FY23RE.

### The government raised their tax buoyancy expectation for FY24…

Due to a 10.4% YoY growth in gross tax revenue and 10.5% YoY growth in nominal GDP, the government is expecting a tax buoyancy of 1x in FY24, higher than 0.8x in FY23RE. Although this seems positive, India's tax buoyancy would still be lower than 1.2x on an average during FY15-19. On the contrary, we had expected tax buoyancy at 1.3x in FY24 entirely on account of lower nominal GDP growth rate and lower growth in gross tax receipts.

### …but the disinvestment target for FY23 looks inflated

The government continues to assume INR650b worth of disinvestments to come in FY23, while only INR386b has been achieved in 9MFY23. This implies that the government expects disinvestment proceeds worth INR264b in 4QFY23, which seems unrealistic given there is no such pipeline in place (*refer to Exhibit 7)*.

**Exhibit 7: Details of receipts in the Union Budget 2023-24**

| | FY22 | FY23RE | | | FY23E* | FY24BE | | | FY24E* |
|---|---|---|---|---|---|---|---|---|---|
| | INR t | INR t | % YoY | % of GDP | INR t | INR t | % YoY | % of GDP | INR t |
| **Total Receipts** | **22.1** | **24.3** | **10.1** | **8.9** | **24.5** | **27.2** | **11.7** | **9.0** | **26.8** |
| Revenue receipts | 21.7 | 23.5 | 8.2 | 8.6 | 24.0 | 26.3 | 12.1 | 8.7 | 26.2 |
| Gross Taxes | 27.1 | 30.4 | 12.3 | 11.1 | 30.9 | 33.6 | 10.4 | 11.1 | 33.8 |
| Net Taxes | 18.0 | 20.1 | 15.6 | 7.6 | 21.5 | 23.3 | 11.7 | 7.7 | 23.5 |
| Direct taxes | 14.1 | 16.5 | 17.2 | 6.0 | 16.4 | 18.2 | 10.5 | 6.0 | 18.0 |
| Corporation Taxes | 7.1 | 8.4 | 17.3 | 3.1 | 8.3 | 9.2 | 10.5 | 3.1 | 9.1 |
| Income Taxes | 7.0 | 8.2 | 17.1 | 3.0 | 8.1 | 9.0 | 10.5 | 3.0 | 8.9 |
| Indirect taxes | 13.0 | 13.9 | 7.1 | 5.1 | 14.5 | 15.4 | 10.4 | 5.1 | 15.8 |
| Customs | 2.0 | 2.1 | 5.0 | 0.8 | 2.2 | 2.3 | 11.0 | 0.8 | 2.4 |
| Excise Duties | 4.0 | 3.2 | -18.9 | 1.2 | 3.3 | 3.4 | 5.9 | 1.1 | 3.6 |
| Goods & Services Tax (GST) | 7.0 | 8.5 | 22.3 | 3.1 | 8.6 | 9.6 | 12.0 | 3.2 | 9.4 |
| Non-tax revenue | 3.7 | 2.6 | -28.3 | 1.0 | 2.4 | 3.0 | 15.2 | 1.0 | 0.9 |
| Dividends from financial sector | 1.0 | 0.4 | -58.7 | 0.1 | 0.4 | 0.5 | 17.2 | 0.2 | 0.5 |
| Non-debt capital receipts | 0.4 | 0.8 | 112.1 | 0.3 | 0.6 | 0.8 | 0.6 | 0.3 | 0.7 |
| Divestment | 0.1 | 0.6 | 309.9 | 0.2 | 0.4 | 0.6 | 1.7 | 0.2 | 0.5 |

*MOFSL estimates

Source: Union Budget documents, CGA, MOFSL

# Total spending budgeted to grow 7.5% YoY in FY24E…

## …the lowest in nine years

The government expects total expenditure at INR41.9t, a 10.4% YoY growth (v/s INR39.4 in FY23BE) in FY23. This has been possible due to high receipts mop-up in FY23.

The government expects total expenditure at INR41.9t, a 10.4% YoY growth (v/s INR39.4 in FY23BE) in FY23. This has been possible due to high receipts mop-up in FY23. This implies that the government expects a 7.5% YoY growth in total spending in 4QFY23, which we believe is totally possible *(Exhibit 8)*. The government forecasts spending to grow 7.5% YoY in FY24, which is in line with our thesis of lower government spending in the coming years. It also means that the impetus provided by the government to economic growth is likely to subside. As a percent of GDP, it is likely to drop only slightly to 14.9% of GDP in FY24 from 15.3% of GDP in FY23 *(Exhibit 9)*.

**Exhibit 8: Total spending growth budgeted to increase 7.5% in FY24BE followed by 10.4% YoY in FY23RE**

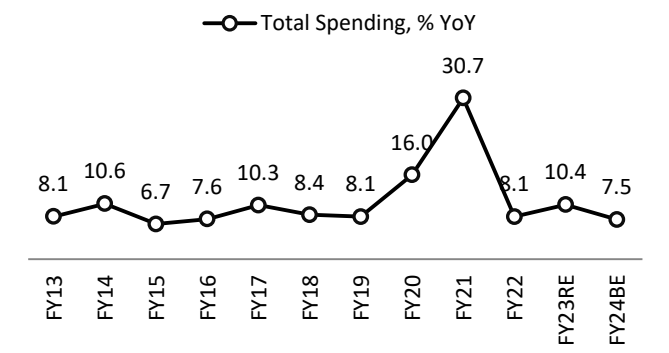
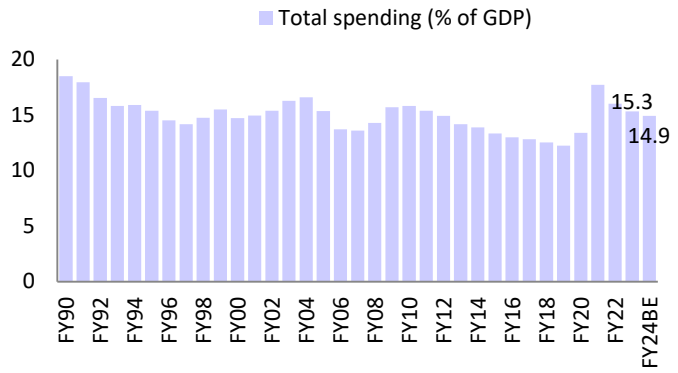



**Exhibit 9: Total spending budgeted to decelerate to only 14.9% of GDP in FY24BE**




Source: Government, MOFSL

Total spending growth of 7.5% YoY in FY24 is largely aided by 37.4% YoY growth in capital spending of the government.

## Government's focus on improving spending quality continues

Total spending growth of 7.5% YoY in FY24E is largely aided by 37.4% YoY growth in capital spending of the government. The government's capital spending has surged almost 2.5x in the past three years to INR10t in FY24BE, from INR4.2t in FY21. Revenue spending growth is actually expected to decline 1.2% YoY next year. Accordingly, capital spending as a percent of total spending stands at a 19-year high of 22% in FY24 *(refer to Exhibits 10, 11)*.

**Exhibit 10: Capital spending (as a % of total spending) is budgeted to rise to a 19-year high in FY24BE…**

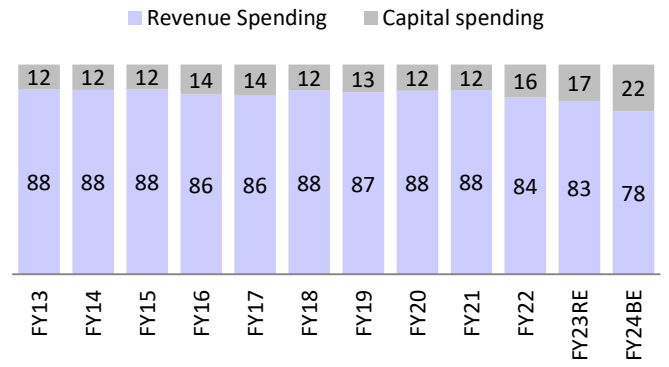
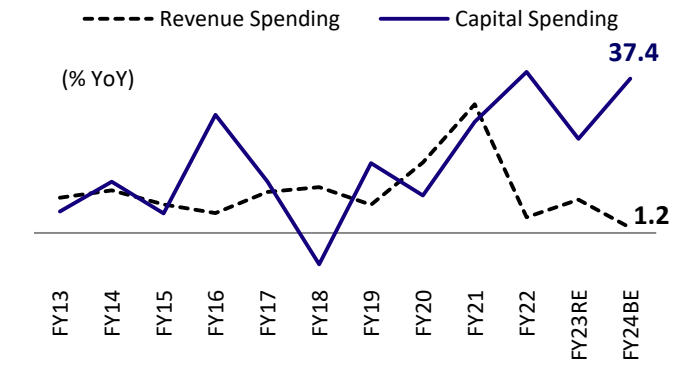



**Exhibit 11: …as capex is expected to grow sharply by 37.4% YoY during the year**

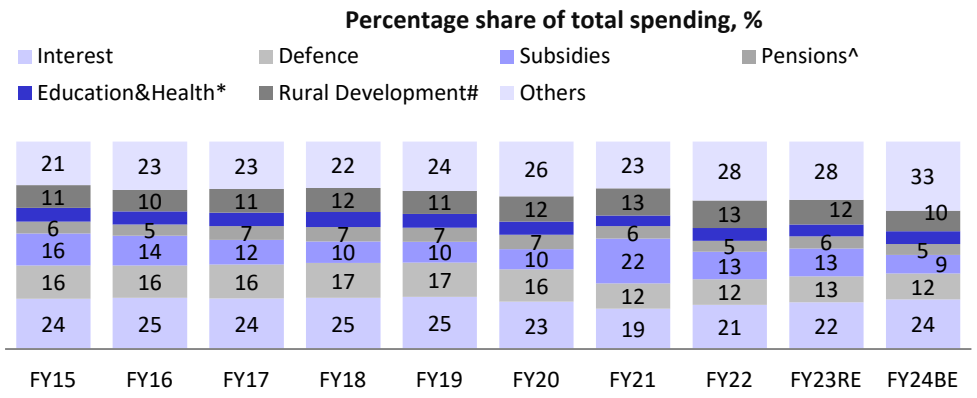



Source: Union Budget documents, MOFSL

## …but spending in almost all major ministries to reduce in FY24E

A close look at major department-wise expenditure share in total expenditure of the government reveals that the share in total spending of almost all ministries to reduce in FY24E. Most surprising is the deceleration in defense/rural spending to 12%/10% in FY24BE from 13%/12% in FY23RE, respectively. The share of spending on interest payments has increased to 24% in FY24E from 22% in FY23E, on account of higher borrowing costs expected during the year and that of education and health has remained unchanged at 6% (mainly due to a sharp rise in spending in the department of water and sanitation – refer to *Exhibit 12)*.

**Exhibit 12: Share of major departments in government's total spending**



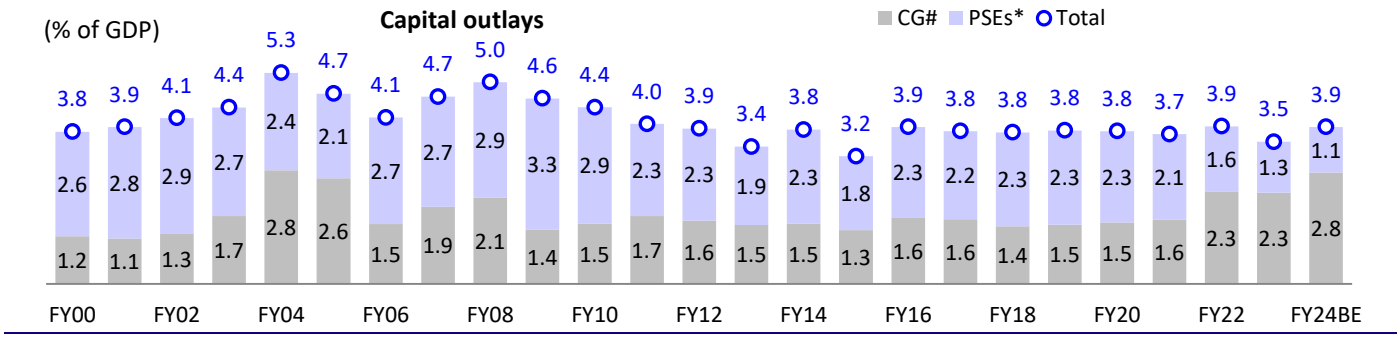

^Including defense pensions; *Including water and sanitation; #includes ministry of rural development, agriculture, Panchayati Raj and fertilizers

## Actual capex projected to grow only 22.1% YoY in FY24

The total government capex is projected to increase to 3.9% of GDP (level similar to pre-Covid) in FY24 from 3.5% in FY23

Although the Central government has targeted a 35% YoY growth in total capex (excluding loans and advances), the same for Central Public Sector Enterprises (PSEs) has actually been estimated to contract for the fourth consecutive year by 1% YoY in FY24. This implies a growth of only 22.1% YoY in aggregate capital spending, which is aided by a low base of 6% YoY growth in FY23. As a percentage of GDP, while PSEs' capex is likely to reduce to 1.1% in FY24 that of the government is expected to increase to 2.8%. Therefore, the total government capex is projected to increase to 3.9% of GDP (level similar to pre-Covid) in FY24 from 3.5% in FY23 *(refer to Exhibit 13)*.

**Exhibit 13: While the Center's capex as % of GDP is expected to rise, that of PSE's is expected to reduce in FY24BE**




*Public Sector Enterprises

#Central Government Capital Outlay (After adjusting capex for loans and advances)

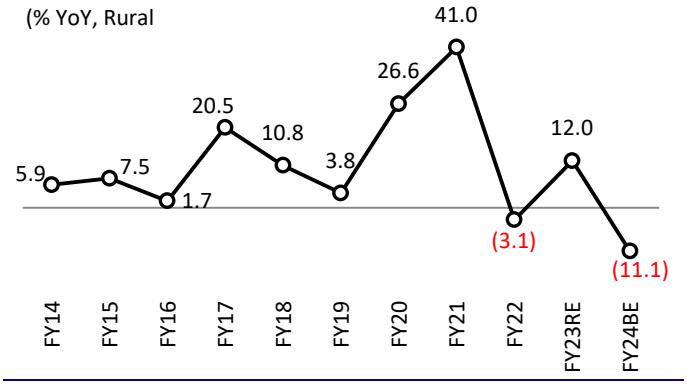
Source: Union Budget documents, MOFSL

## A few other noticeable points in the Budget are as follows:

Following a 12% YoY growth in FY23RE, the government has estimated rural spending of INR4.4t in FY24BE, a decline of 11.1% YoY during the year

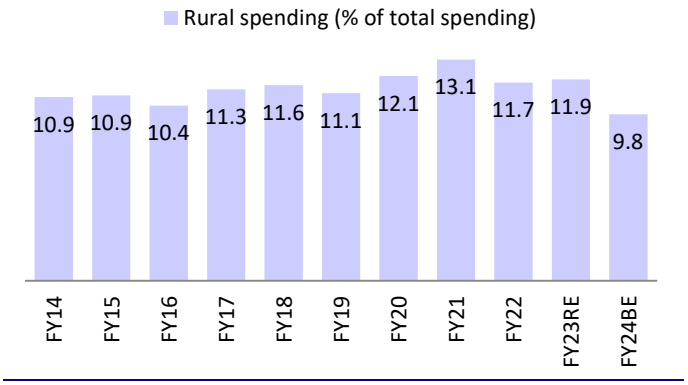
1. Following a 12% YoY growth in FY23RE, the government has estimated rural spending of INR4.4t in FY24BE, a decline of 11.1% YoY during the year. While the decline was expected due to super high base of FY21/22 on account of COVID-led rural spending, we were positively surprised at the government's resistance towards freebies to the rural sector *(Exhibit 14 and 15)*.

**Exhibit 14: Rural spending is budgeted to contract…**




Ministry of rural development, Panchayati Raj, Fertilizer and Agriculture

**Exhibit 15: …leading to lower share in total spend in FY24BE**




Source: Union Budget documents, MOFSL

2. After the new personal income tax regime was introduced three years back in Union Budget 2020-21, the government has once again brought in significant changes in it. The government has enhanced the tax exemption limit to INR0.3m from INR0.25m and it has also reduced the number of tax slabs to five from the initial six. Moreover, the rebate limit in the new tax regime has been increased to INR0.7m from INR0.5m earlier. Lastly, the highest effective personal income tax, which was 42.7%, has now been reduced to only 39%. The catch, however, in all these announcements is that they can be availed only by those who are opting for the new personal income tax regime, which is a very small portion of total tax payers in the country. Therefore, as far as actual benefits go, there is not much to these announcements.
3. Although the fiscal deficit targets for FY23/24 are in line with market expectations, the government reiterated its target of achieving fiscal deficit of below 4.5% of GDP by FY26. This implies a consolidation of 140bp over two years, which seems like a very unrealistic target at this stage.
4. Two years ago, the government had undertaken the noble task of transferring major PSE borrowings in its own books, thereby bringing in more transparency in fiscal accounts. One of these PSE's was the Food Corporation of India (FCI), whose capex had reduced to INR569b/INR612b in FY21/22 from INR1.8t in FY20 and it is expected to remain at similar level at INR553b in FY23. However, in FY24, FCI's capex is again expected to increase to INR1.4t. *Is the government undoing the good it did in the last two years?*

## Government resists populism; spending quality continues to improve

The Government did not give in to these (income/consumption support) expectations and continued with its investment-led spending growth strategy, along with modest fiscal consolidation.

Since this year's budget was the last full budget before 2024 General Elections, it was expected that the government could announce some income support for the rural sector or implement some measures to boost consumption growth in the economy. However, the government did not give in to these expectations and continued with its investment-led spending growth strategy along with modest fiscal consolidation. Although the Economic Survey projected a nominal GDP growth of 11% YoY in FY24, the Budget assumed 10.5% nominal GDP growth next year.

The GoI kept revenue expenditure growth at minimal (just 1.2% YoY), and propelled capex strongly for the third consecutive year. GoI's capital spending, however, is budgeted to grow 37.4% YoY in FY24BE following a 23% YoY growth in FY23RE. The government's capital spending has surged almost 2.5x in the past three years to INR10t in FY24BE from INR4.2t in FY21. Since total government expenditure is budgeted to grow just 7.5% in FY24BE, the share of capital spending is budgeted to rise to 22.2% of total spending, marking the highest share in 18 years (up from just 12-13% in pre-Covid years).

Because of weaker growth and modest consolidation, total liabilities of GoI are expected to rise to 56.2% of GDP in FY24BE, up from 55.9% of GDP in FY23RE.

Notably, as highlighted in our recent report, a large portion of GoI's higher capex is re-allocated from the IEBR of public sector enterprises (PSEs). Including IEBR, the aggregate capex is expected to fall sharply to just 3.5% of GDP in FY23RE, before recovering to 3.9% in FY24BE, same as in the pre-Covid years.

Contrary to our expectation of lower-than-budgeted deficit in FY23, the Government of India (GoI) kept it unchanged at 6.4% of GDP in FY23. This means that fiscal deficit was revised up to INR17.6t in FY23, from BE of INR16.6t. At the same time, the GoI has budgeted the deficit at 5.9% of GDP (INR17.9t) for next year, which is in line with the market consensus but higher than our expectations of 5.7%. Total liabilities of GoI are likely to rise to 56.2% of GDP in FY24BE from 55.9% of GDP in FY23RE owing to weaker growth and modest consolidation.

With 5.9% budgeted deficit in FY24, the task of bringing it down to 4.5% of GDP becomes an even more difficult task

Overall, it was a relief to see the GoI resisting populism pressures. At the same time, neither the aggregate capex growth nor the tweaks in taxation is likely to make a big difference. With 5.9% budgeted deficit in FY24E, the task of bringing it down to 4.5% of GDP becomes even more challenging. It is possible only and only if the GoI keeps its spending growth extremely muted for the subsequent two years, thus restricting its ability to support economic growth.

## Agri — Budget Impact: Positive — Sector Stance: Positive

The Union Budget 2023 has reflected the government's focus on increasing digitization and developing a strong agri-tech industry. The key announcements influencing the Agri sector and farmers, are:

| Area | Key proposal | Impact |
|---|---|---|
| Fertilizer subsidy reduced 22% to INR1,751b *(over FY23 Revised allocation)* | ❖ Overall budget allocation for fertilizer subsidy was cut 22% to INR1,751b (Urea subsidy lower by ~15% to INR1,311b and Complex Fertilizer subsidy cut by 38% to INR440b). The key raw materials are currently on a downtrend and hence we believe the government will revise subsidy allocation as per the requirement and on assessing the raw material scenario during the year. The government had revised fertilizer subsidy in 2022-23 by 2.1x over budgeted subsidy allocation to INR2,252 (Urea subsidy higher by 2.4x to INR1,541b and Complex Fertilizer subsidy higher by 1.7x to INR712b) | **Neutral** |
| Boosting allied agriculture sectors by increasing credit to INR20t and launch of new schemes | ❖ The government has increased the agriculture credit to INR20t focusing on animal husbandry, dairy, and fisheries industries. Further, the government launched a new sub-scheme of PM Matsya Sampada Yojana with targeted investment of INR60b to further enable activities of fishermen, fish vendors, and micro & small enterprises, and improve value chain efficiencies, as well as expand the market | **Positive** |
| Setting up Agriculture Accelerator Fund | ❖ The government is setting-up Agriculture Accelerator Fund to encourage agri-startups by young entrepreneurs in rural areas. The Fund will aim at bringing innovative, modernized and affordable solutions to farmers. | **Positive** |
| Promote efficient farming | ❖ To focus on efficient and balanced use of chemical fertilizer, the government is launching "PM Programme for Restoration, Awareness, Nourishment and Amelioration of Mother Earth". The government will also facilitate over 10m farmers to adopt natural farming. | **Positive** |
| Digitizing public infrastructure for Agriculture | ❖ To support the growth of agri-tech industry, the government will build a digital public infrastructure as an open source, open standard and inter-operable public good where farmers can obtain relevant information services for crop planning and health, improved access to farm inputs, credit, and insurance, help for crop estimation and market intelligence. | **Positive** |

### Outlook and recommendations

For the agriculture sector, the Budget focused on: i) building a strong agri-tech industry, ii) boosting growth in the other allied agriculture sectors such as animal husbandry, fisheries and dairy, and iii) promoting efficient and balanced use of chemical fertilizer. The strategy of the government, with its long-term objective of increasing farmers' income, is to benefit the Agrochemical and Fertilizer companies.

## Autos Budget Impact: Positive Sector Stance: Positive

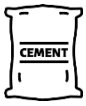
The Union Budget 2023 has focused on driving localization of EVs through various means, viz., raising customs duty for imported BEV (both SKD & CBUs), reducing custom duty for the capital goods required to manufacture Li-ion cells (to nil), and increasing allocation to various incentives (FAME & PLI). Further, increase in outlay towards capex and allocation for scrapping of old government vehicles augurs well for demand. However, a reduction in the allocation towards MGNREGA may hurt rural-focused segments such as 2Ws and Tractors. Key announcements directly influencing the sector are:

### At a glance

| Area | Key proposal | Impact |
|---|---|---|
| Increased allocation to FAME-2 scheme | ❖ There is an increase in the number of EVs targeted through FAME-2 scheme in the terminal year (FY24). The targeted volumes for incentives are: 4.09k e-buses (+86%), 15k e-PVs (15x), 100k e-3Ws (+33%), and 320k e-2Ws (+28%). This in turn is reflected in 78% rise in the budget for FAME-2 for FY24 to INR51.7b (cumulative over FY19-24 = INR96.9b v/s total allocation of INR100b). | **Neutral** |
| PLI scheme allocation | ❖ The allocation towards PLI scheme was at INR6.04b for Auto/Auto components and INR10m for ACC (cell-manufacturing). An estimated incremental sales of INR279.3b by the approved applicants covered under the scheme in FY24 along with an investment of INR200b (INR80b by OEM and INR120b by the Ancs) is anticipated. | **Neutral** |
| Allocation to scrap government vehicles older than 15 years | ❖ Scrapping of old government vehicle (>15 years) is promoted by allocating adequate funds to the Central Govt. and including scrapping as one of the purposes to allocate 50-year interest-free loans to states. | **Positive** |
| Battery energy storage | ❖ The battery energy storage system with a capacity of 4GWh will be supported by viability gap funding. This augurs well for players like EXID, AMRJ etc., which are currently offering battery pack based on imported cell and are in the process of putting-up cell manufacturing plants. | **Positive** |
| Custom duty increased for imported vehicles | ❖ There in a rise in effective customs duty (after surcharge) for: a) imported vehicles on SKD basis by 4pp to 35%, and b) imported vehicles on CBU basis by 6.4pp to 70%. This increase in duty will encourage localization. | **Positive** |
| Custom duty related to Li-ion | ❖ Lithium-ion cell import duty of 5% has been extended for one more year (v/s proposed 10% from Apr'21 as a part of the Phased Manufacturing Proposal for FAME-2 subsidies). Further, custom duty on capital goods for Li-ion cell manufacturing has been removed. | **Positive** |
| Customs duty hike on Compounded Rubber | ❖ Customs duty on compounded rubber has been increased from 10% to 25% or INR30/kg whichever is lower. This may have a minor impact on tyre players, though a large part of rubber (including compounded rubber) is imported from countries where India has FTAs. | **Negative** |

### Outlook and recommendations

As expected, the Union Budget 2023 did not have any big announcement specific to the auto sector, though there were some specific measures that were largely positive. While increased outlay for capex is a positive particularly for the CV segment, lowered outlay for the rural markets could adversely influence demand, particularly 2Ws and Tractors.




## Cement **Budget Impact: Neutral** **Sector Stance: Positive**

There has been no direct announcement for the Cement sector in the Union Budget 2023, though, the allocations on Housing schemes, Roads, etc., have been increased on a higher base of last year.

### At a glance

| Area | Key proposal | Impact |
|---|---|---|
| Allocation for Housing schemes | ❖ Allocation for Housing schemes (PMAY-Gramin and PMAY-Urban) stood at INR796b, up 3.2% YoY v/s 2022-23RE. This will continue to boost cement consumption. | **Neutral** |
| Allocation for Roads | ❖ Allocation for Roads (including IEBR) stood at INR2,063b, up 25% YoY v/s 2022-23RE. Allocation for Pradhan Mantri Gram Sadak Yojana stood at INR190b, flat YoY. | **Positive** |

### Outlook and recommendations

**Cement:** We remain positive on the sector as we expect demand to improve going forward, led by the government's thrust on Infrastructure spending and a pick-up in demand from the urban Real Estate sector. Cement demand is likely to outpace clinker capacity additions over FY22-25E. This should lead to an improvement in clinker utilization and thus profitability for the industry. Clinker utilization over Jan-Mar'23 is estimated to be at ~89%, largely in line with the utilization trend of 4QFY19 (90.7%) when the industry began to exhibit pricing power. UTCEM is our top pick in the largecap space, followed by DALBHARA and JKCE in the midcap space.

## Specialty Chemicals Budget Impact: Neutral Sector Stance: Neutral

Through the Union Budget 2023, the government has aided domestic companies by imposing customs duties on key raw materials. The key announcements influencing the chemicals sector are:

### At a glance

| Area | Key proposal | Impact |
|---|---|---|
| Changes in Customs Duties | ❖ The BCD on denatured ethyl alcohol has been reduced to Nil from 5% for use in the manufacture of industrial chemicals through the IGCR route<br>❖ The BCD on acid grade fluorspar (containing by weight more than 97% of calcium fluoride) has been reduced to 2.5% from 5.0%<br>❖ The BCD on crude glycerin has been reduced to 2.5% from 7.5% for use in the manufacture of Epichlorohydrin through the IGCR route<br>❖ The BCD on Naphtha has been increased to 2.5% from 1.0%.<br>❖ The BCD on styrene has been increased to 2.5% from 2.0%.<br>❖ The BCD on Vinyl Chloride monomer has been raised to 2.5% from 2.0%. | **Neutral** |

### Outlook and recommendation

The aforementioned changes in customs duties would be beneficial to companies such as Navin Fluorine among our Coverage companies. Cheaper availability of raw materials coupled with increasing domestic competition in the space would create an overhang on the long-term terminal growth of the companies. The much awaited PLI scheme for the chemical sector was not announced yet again in the Budget, which appears to be a negative in our view.

## Consumer Budget Impact: Marginally Negative Sector Stance: Neutral

There was no material announcement in the Union Budget 2023 that could significantly impact any of the stocks in our Consumer Universe (either positively or negatively). Lower allocations towards fertilizer subsidies (both Urea-based and Complex) as well as a 33% lower MNREGA allocation are all sentimental downers while other provisions are not material. The 15-16% increase in NCCD on cigarettes will not have any material impact as NCCD forms ~10% of total indirect taxation on cigarettes, which is 60% of MRP. Hence, the effective impact of the increase will be less than 1% of MRP.

### At a glance

| Area | Key proposal | Impact |
|---|---|---|
| NCCD on cigarettes | ❖ NCCD on all four categories viz. less than 65mm, 65-70mm, 70-75mm and above 75mm is increased by 15-16%. However, total NCCD across these segments is less than 10% of the total indirect taxation, which is 60% of MRP. Hence, the effective increase would be less than 1%. | **Not material** |
| Customs Duty on Gold | ❖ Basic customs duty on Gold (including gold-plated with platinum) in unwrought/semi-manufactured/powder forms reduced to 10.0% from 12.5%; however, AICD on the same increased to 5.0% from 2.5%.<br>❖ BCD on Gold Dore reduced to 10.0% from 11.85%; however, AICD increased to 4.35% from 2.5%. | **Neutral** |
| Customs Duty on Naphtha | ❖ BCD on Naphtha increased to 2.5% from 1.0%. | **Marginally negative** |

### Outlook and recommendation

ITC has not taken any price hike in either the Dec'21-Jan'22 period or the Dec'22-Jan'23 period, unlike the usual increase every year. Hence, this gives the company immense room to take a miniscule price hike of 1-2% (please note – ITC usually takes price hikes of more than indirect tax hike). This implies that unless there is an increase in GST in the next council meeting, cigarette volumes that have been very healthy at mid-single digit (3-/4-year CAGR) in the recent quarters are likely to sustain, unlike flattish growth over preceding 10 and 20 years. We like ITC from one-year perspective. Slight Increase in Naphtha customs duty would marginally impact JYL and HUVR.

## Financials Budget Impact: Negative for Insurance Sector Stance: Positive

The Union Budget 2023 announcements were Neutral for the banking sector but sharply negative for the Insurance industry. The key government recommendations were as follows: (i) proceeds from life insurance policies (other than ULIPs) issued on or after 1st Apr'23 having an aggregate premium of >INR0.5m will be taxable; (ii) the Credit Guarantee Trust Scheme for MSME has been upsized; (iii) there is an enhancement in limit for senior citizens savings scheme; and, (iv) allocation under PMAY has been enhanced. The government further announced operational measures to improve the efficiency and governance while higher capex outlay will boost the overall credit demand.

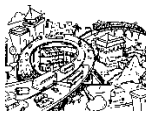
### At a glance

| Area | Key proposal | Impact |
|---|---|---|
| Proceeds from life insurance policies to be taxable | ❖ The government has proposed to tax the proceeds (other than death benefit) received from life insurance policies (barring ULIPs) having an aggregate premium of greater than INR0.5m in a year. This provision will be applicable for policies issued on or after 1st Apr'23. This measure will impact the sale of guaranteed return/non-par business adversely, where the entire industry has been witnessing strong growth. | Negative |
| Credit Guarantee Trust for MSME to be revamped | ❖ The Credit Guarantee Trust for Micro and Small Enterprises (CGTMSE) scheme was upsized, facilitating additional credit of INR2t for MSMEs. | Positive |
| Vivad se Vishwas | ❖ To provide relief to MSME, in cases of failure to execute the contracts during the Covid period, 95% of the forfeited amount relating to bid or performance security will be returned to them by government and government undertakings under the Vivad se Vishwas scheme. | Neutral |
| Pradhan Mantri Awas Yojana (PMAY) | ❖ Allocation towards the PMAY scheme has been increased to INR800b from INR480b in the previous year. | Positive |
| Increased capex outlay to facilitate credit | ❖ Government has increased the capex to INR10t from INR7.5t in the previous year, while outlay for Railways has also been increased to INR2.4t. This should aid capex recovery and boost credit demand. Target for Agriculture credit has been raised to INR20t from INR18t. | Positive |
| Enhanced limit for senior citizen savings scheme | ❖ The maximum limit for Senior Citizen Savings Scheme has been increased to INR3.0m v/s the current limit of INR1.5m. This will further increase competition and may hurt liability accretion for banks from senior citizens. This can also compete with select non-par products from life insurers. | Negative |
| Improving operational efficiencies and governance | ❖ A slew of measures were announced to facilitate financial inclusion and ease of availing credit such as setting up of National Financial Information Registry and Central Data Processing Centre. Further, banking amendments have been proposed for improving the governance. | Positive |
| Enhancing spot gold market | ❖ Government has proposed to exclude the conversion of physical form of gold into EGR and vice versa by a SEBI registered Vault Manager from the purview of 'transfer' for capital gains purposes. | Positive |

### Outlook and recommendation

Taxability of proceeds from life insurance policies will impact the sale of guaranteed return/non-par business adversely where the entire industry has been witnessing strong growth. This can further hit the profitability and margin profile of companies as these products generate higher margins. With these measures, the Government is aiming to plug the arbitrage which HNIs and other wealthy individuals are employing to get healthy tax-free returns on their lumpy insurance purchases. This will thus reduce the attractiveness of non-par products for such customers thereby impacting business growth adversely.

The revamping of the CGTMSE scheme would provide further impetus to the MSME sector – which has still not completely recovered from the impact of the pandemic. Further, the thrust on infrastructure spending and higher government capex is positive for credit growth. **Our top ideas:** AXSB, ICICIBC, SBIN and FB.



# Infra

**Budget Impact: Neutral** **Sector Stance: Positive**

## Capex trend robust – Roads and Railways key beneficiaries; Defense outlay moderate

### At a glance

| Area | Key proposal | Impact |
|---|---|---|
| Roads | ❖ While gross budgetary support rose 25% YoY to INR2.6t in FY24BE, the funding via IEBR has been pegged again at zero. | Positive |
| Railways | ❖ The sector has witnessed a 15% growth on the overall capex outlay. While budget-linked allocation has grown 50% YoY, the IEBR has been pegged lower by 45%. | Positive |
| Defense | ❖ Defense capex increased 8.4% to INR1.63t. | Neutral |
| Others | ❖ Allocations towards the Jal Jeevan Mission increased 27% to INR700b in FY24BE. | Positive |

### Outlook and recommendations

- **Infrastructure:** Overall, capex growth was supposed to have a big impetus on infrastructure spending, and it was in line with our expectation of decent growth. Roads and Railways' capex remained strong. Defense capex, however, saw moderate growth.
- **Our top pick:** Within the Roads segment, we continue to prefer KNR Constructions.

## Logistics Budget Impact: Neutral Sector Stance: Positive

### Focus on promoting Coastal shipping

### At a glance

| Area | Key proposal | Impact |
|---|---|---|
| Logistics | ❖ Coastal shipping will be promoted as an energy efficient and lower-cost mode of transport, both for passengers and freight.<br>❖ The PPP model along with viability gap funding would be considered to promote coastal shipping. | Positive |

### Outlook and recommendations

- **Logistics:** The Coastal shipping network in India is a small portion in the Modal mix with robust growth potential. Development here would improve operational efficiency and reduce logistics costs.
- **Our top picks: VRL Logistics and Transport Corporation** are our preferred plays in the Logistics sector.


## Metals

**Budget Impact: Neutral** **Sector Stance: Positive**

The continued thrust on infrastructure spending is positive for the Metals sector. The sector did not witness any significant budget proposal that would have impacted the stocks positively, but the overall emphasis on capex by both Central and State Governments should boost demand for metals.

### At a glance

| Product | Key proposal | Impact |
|---|---|---|
| Ferrous waste and scrap | ❖ Import duty on ferrous waste and scrap was maintained at 0% for one more year. It is mildly positive for the sector, and will not materially influence the earnings for companies under over coverage. | **Neutral** |
| Coal, peat, and lignite | ❖ The effective duty on coal stood at 2.5%, which comprises 1% BCD and 1.5% Agricultural and Infrastructure Development cess. Now the BCD has been increased to 2.5% and Agricultural cess has been reduced to NIL. Effectively there is no change in duty and it continues to be at 2.5% | **Neutral** |
| Raw materials for use in manufacture of CRGO steel | ❖ Import duty on raw materials for use in manufacture of CRGO steel was maintained at 0% for one more year. It is mildly positive for the sector, and will not materially influence the earnings for companies under over coverage. | **Neutral** |

### Outlook and recommendations

- **Steel:** Infrastructure contributes ~60% of the total domestic steel demand with construction at ~20%, and automobile at ~8%. The domestic steel demand has bounced back strongly post-Covid. The duty on exports was removed in Nov'22, which would improve volumes in 4QFY23E.
- While global markets continue to remain challenging, most of the players have indicated a strong demand environment in the domestic markets that should support volumes.
- We maintain our positive view on metals with JSPL being **our top pick** in the ferrous domain.

## Oil and Gas

**Budget Impact: Neutral** **Sector Stance: Negative**

Through the Union Budget 2023, the government has tried to focus on green and renewable energy. Accordingly, the government has announced INR350b of investments towards energy transition and net-zero emission and reiterated its ambitious target of producing 5mmt of Green Hydrogen by 2030. However, it is unclear whether the capital support of INR300b to OMCs is included in the INR350b investment. The key announcements influencing the Oil and Gas sector are:

### At a glance

| Area | Key proposal | Impact |
|---|---|---|
| Capital support | ❖ The government has announced a capital support of INR300b to the OMCs in FY24E. However, there would be no LPG subsidy v/s INR220b given in FY23, while the DBT on LPG continues. There is no DBT for Kerosene in FY24 as well. | **Neutral** |
| Ambitious target of Green Hydrogen | ❖ There would be an outlay of INR197b to facilitate transition of the economy to reduce its dependence on fossil fuel imports. The government has a target to produce 5mmt of Green Hydrogen by 2030. | **Neutral** |
| Promotion of blended CNG | ❖ The government has exempted CNG from the duty excise leviable on the amount of GST on biogas or compressed biogas blended with CNG. However, the manufacturers of such blended CNG have to meet three criteria, before obtaining such an exemption. | **Positive** |
| Renewable energy from Ladakh | ❖ There would be an inter-state transmission system constructed for evacuation and grid integration of 13GW renewable energy from Ladakh with an investment of INR207b, including Center's support of INR83b. | **Positive** |

### Outlook and recommendation

Demand for blended fuel will improve in line with the stated aim of 20% ethanol blending by 2025. However, there would no further LPG subsidy for the OMCs and no DBT on Kerosene as well. We reiterate our negative stance given the highly volatile macro environment as of now with sustainable earnings being a concern.

# Real Estate

**Budget Impact: Neutral** **Sector Stance: Positive**

In the Union Budget 2023, the government has capped the limit for capital gains deduction under section 54 and 54F to INR100m, if capital gains arising from asset sale are re-invested for residential house purchase. Players such as DLF, Oberoi and Sunteck with some exposures to ultra premium projects could witness a negative impact due to this but we may see an upsurge in ultra-luxury housing demand over the next two months. Government has also decided to tax the income arising out of distribution by way of repayment of SPV debt in the hands of unit holders. This will adversely impact the Embassy and Brookfield REITs as 50% and 45% of their respective distribution is in the form of SPV debt repayment.

## At a glance

| Area | Key proposal | Impact |
|---|---|---|
| Capping of capital gains | ❖ Deduction against re-investment of capital gains arising from asset sale are now capped at INR100m | Negative |
| Tax on distribution by REIT | ❖ Distribution by way of SPV debt is now taxable in the hands of unit holders | Negative |

## Outlook and recommendations

While much was anticipated on the real estate sector, there was a very little mention about the sector in the overall budget. Except for DLF, Oberoi Realty and Sunteck Realty, we do not foresee any negative impact on listed developers on account of the new capital gains proposal announced as most of them cater to the mid-income segment. On the other hand, the new taxation norms on distribution of SPV debt could adversely impact the REITs (especially EOP and Brookfield) as the norms significantly hurt the post-tax yields on their distribution.

| REIT | Annualized distribution per unit (FY23) | Post-tax distribution per unit | Gross yield % | Post-tax yield % |
|---|---|---|---|---|
| EOP | 21.4 | 17.5 | 6.7 | 5.5 |
| Mindspace | 19.1 | 18.9 | 5.8 | 5.7 |
| Brookfield | 20.4 | 15.1 | 7.1 | 5.3 |

Note: We have assumed highest marginal tax rate for debt component

# NOTES

| Explanation of Investment Rating | |
|---|---|
| **Investment Rating** | **Expected return (over 12-month)** |
| BUY | >=15% |
| SELL | < - 10% |
| NEUTRAL | > - 10 % to 15% |
| UNDER REVIEW | Rating may undergo a change |
| NOT RATED | We have forward looking estimates for the stock but we refrain from assigning recommendation |

*In case the recommendation given by the Research Analyst is inconsistent with the investment rating legend for a continuous period of 30 days, the Research Analyst shall within following 30 days take appropriate measures to make the recommendation consistent with the investment rating legend.

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