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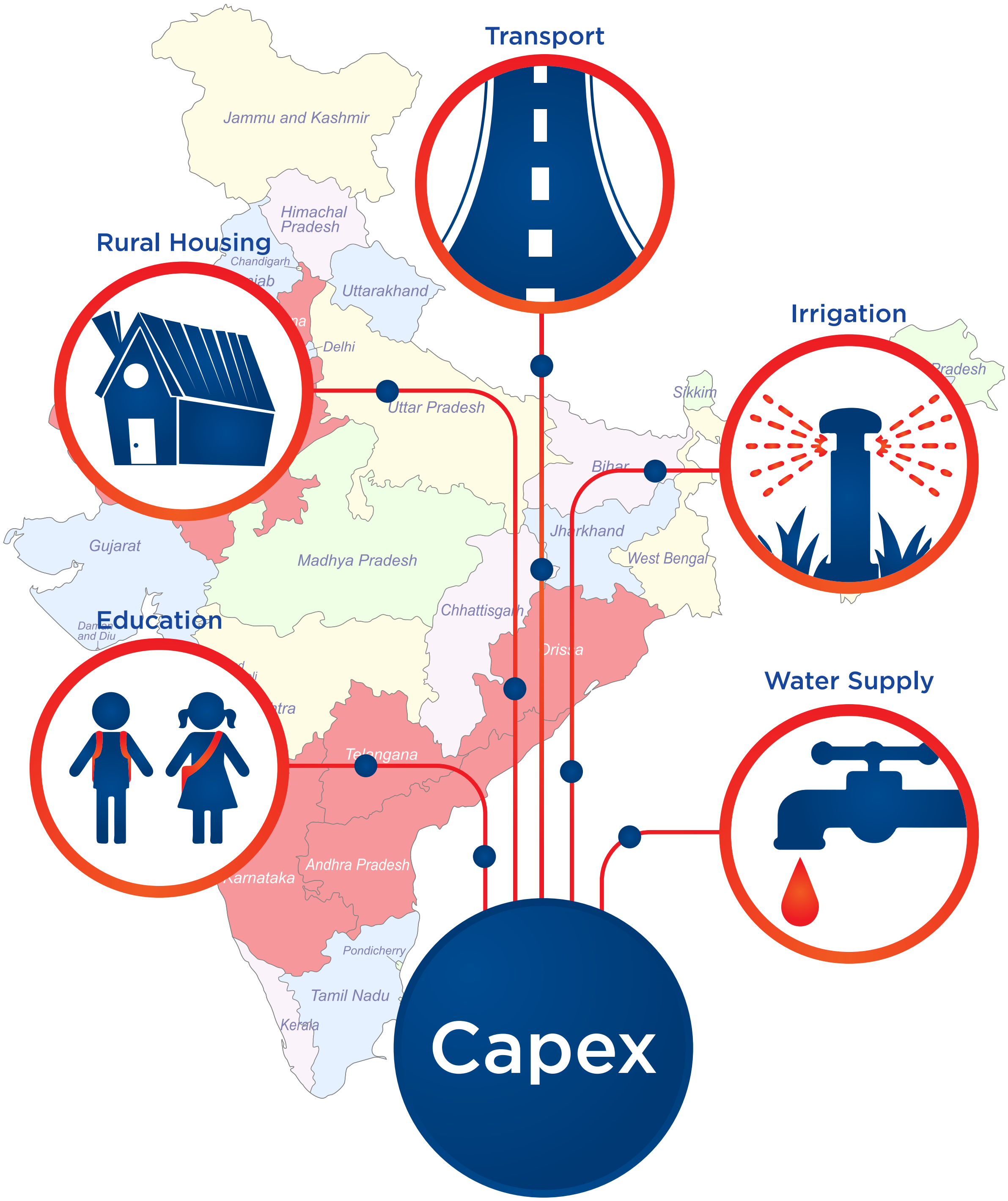
JM FINANCIAL

Indian States Borrow More to Spend on Capex



JM Financial Institutional Securities Limited

FY18 State Budgets

Analysis #3 – Strong capex growth within FRBM barricade

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In this report, we present seven state budgets, namely Haryana, Rajasthan, AP, Telangana, Karnataka, and Odisha which together account for 29% of the Indian GDP. Now having analyzed 13 states in total, which constitute 58% of the Indian GDP, we find enhanced inclination towards capex (exception Odisha). Capital expenditure growth for the 13 states stands at 18%YoY compared to 10% for revenue expenditure. The states spending on capex is typically 1.6 times that of the Centre and hence is an important driver for various sectors. The main beneficiaries of capex by the states are social services like water supply, sanitation, housing & urban development and education. Rural related spending (rural roads, rural housing, irrigation, agri and allied activities) also continues to be strong with 15%YoY growth. Despite this high growth in capex, the estimates for the combined Gross Fiscal Deficit (GFD) stand at 2.5% for the 13 states. This, we believe, is due to a) the share of capex in total expenditure still stands below 20% (at 18%) and b) most states are yet to account for the new salary proposals for the government employees. In FY17, the gross borrowings of states were 58% lower than that of the Centre while in FY18, the gross market borrowings for just these states is projected to increase 23.1%YoY vs. flat change for the Central government (though net borrowings have increased 4.2%YoY), implying catch up.

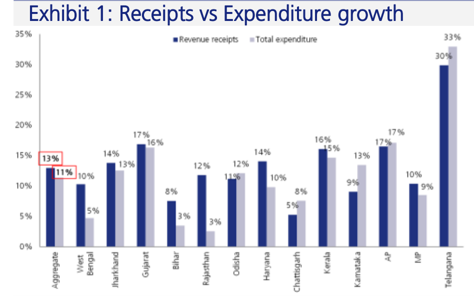
- **Realistic tax revenue projections by states:** At an aggregate level, revised tax revenue collections for FY17 were 98% of budget estimates. Excluding Gujarat, Telangana & Rajasthan, all other states expect tax revenues above 97% of budget estimates (as shown in Exhibit 3). For FY18, tax revenue is estimated to grow by 13%YoY, mainly led by Telangana (22%YoY) and Kerala (18%YoY) while Chattisgarh expects 7%YoY growth. Aggregate tax to GSDP ratio stands at 10.7% vs 11.75% for the Union Budget.

- **Capex growth at 18%YoY vs 10% revenue expenditure growth:** Budgeted aggregate capital expenditure growth has surged to 18%YoY, almost 2 times that revenue expenditure growth (10%YoY) for the 13 states. Capex as a % of GSDP stands at 3.2% vs 1.8% in the Central government Budget. While Telangana (65%YoY) and AP (55%YoY) drive the hike in capex growth, Rajasthan is the only state with de-growth in capex. At a more granular level, capex is focused towards social services (38%YoY) compared to economic services (21%YoY). Major beneficiaries of these are services like education (52%YoY), water supply, housing, sanitation & urban development (42%YoY). Capex on economic services like transport and rural sector (irrigation, rural development, agri & allied activities) have also seen growth in mid-teens.

- **Aggregate GFD within FRBM limits:** In FY17Revised Estimates, the GFD is estimated at 3.3% for these states. On the other hand, In FY18BE (budget estimates), aggregate expenditure is estimated to grow by 11%YoY vs. revenue receipts growth of 13%; helping to contain overall fiscal deficit to 2.55% of total GSDP. However, most states that have announced implementation of the 7th Pay Commission recommendations (all 13 except JHA, WB, Kerala, AP & Telangana) have not accounted for the hike in revenue expenditure completely. Additional costs of UDAY have been budgeted for by all states that have signed an MoU under the scheme (exception WB, Kerala & Odisha).

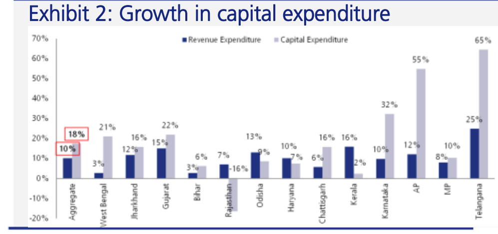
- **Market borrowing of the State Govts. soar:** The gross market borrowing for the 13 states so far has reached Rs 2.97trn in FY18, higher than FY17's figure of Rs 2.41trn. This 23.1%YoY growth has triggered expectations that of state borrowing converging to centre's borrowing in the near future which currently is projected at Rs5.8trn for FY18.

Exhibit 1: Receipts vs Expenditure growth



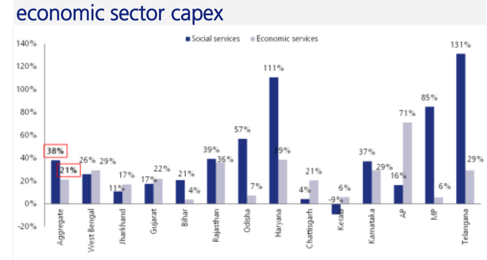
Source: State Budgets, JM Financial

Exhibit 2: Growth in capital expenditure



Source: State Budgets, JM Financial

Exhibit 3: Social sector spending overtakes economic sector capex



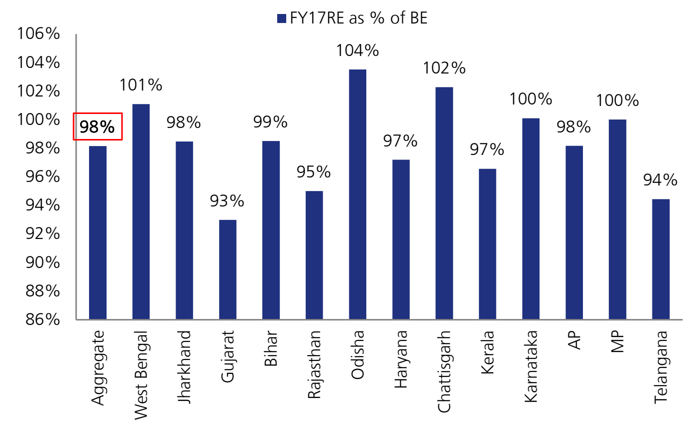
Source: State Budgets, JM Financial

JM Financial Research is also available on:
Bloomberg - JMFR <GO>,
Thomson Publisher & Reuters,
S&P Capital IQ

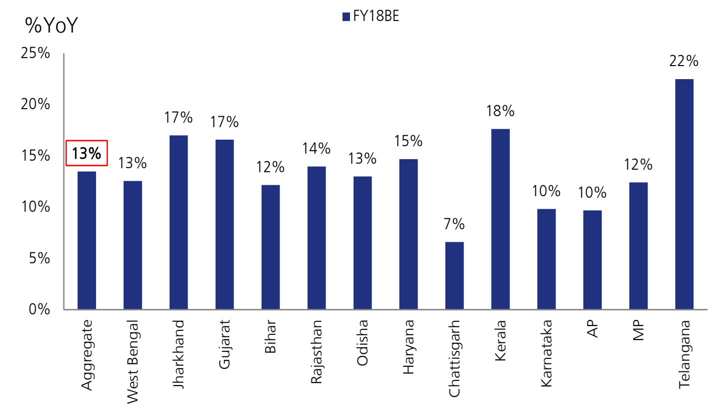
Please see Appendix I at the end of this report for Important Disclosures and Disclaimers and Research Analyst Certification

Exhibit 4. Healthy growth expectations for own tax revenue collection

FY17 tax revenue collection as percentage of budgeted estimates



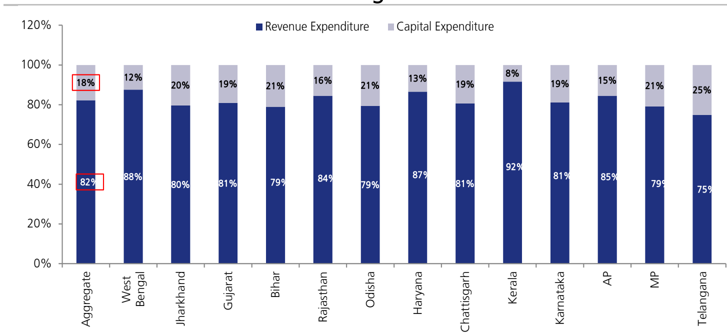
Growth of states tax revenue collection



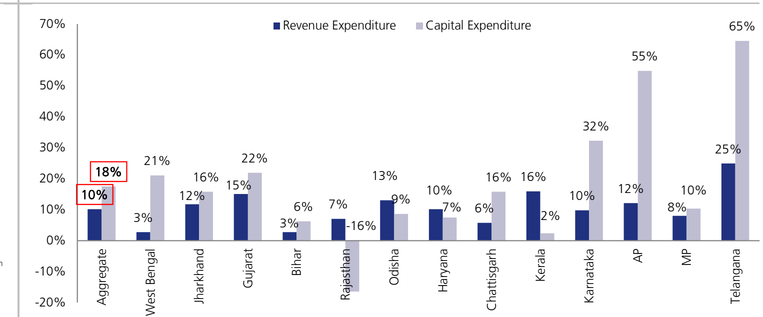
Source: State Budgets, JM Financial

Exhibit 5. States' focus on capex growth blatant

At an aggregate level, capex share stands at 18% vs 14% in Union Budget

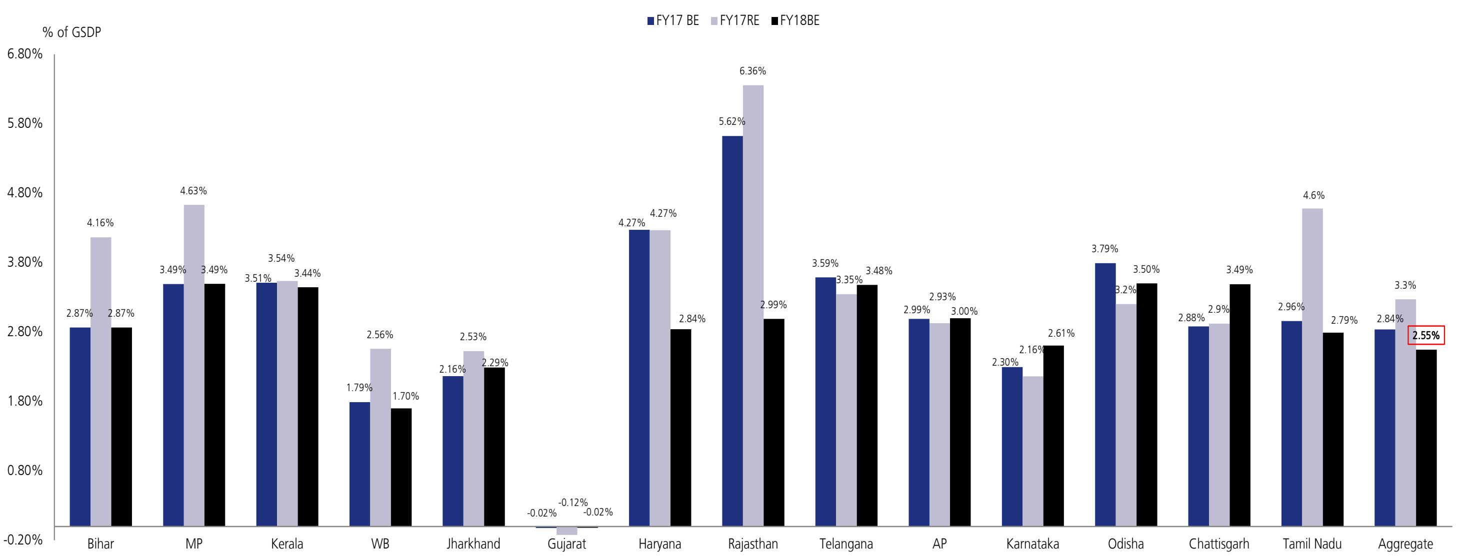


Capex growth almost 2x of revenue expenditure growth



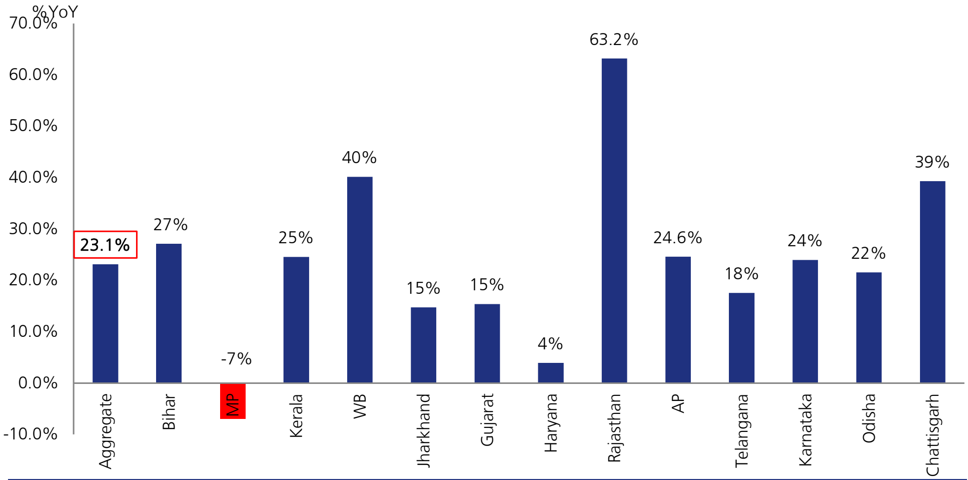
Source: State Budgets, JM Financial

Exhibit 7. Aggregate Fiscal Deficit for 14* states stands at 2.55% of GSDP vs 3.3% in FY17



Source: State Budgets, JM Financial; *Inferred through budget speech of Tamil Nadu

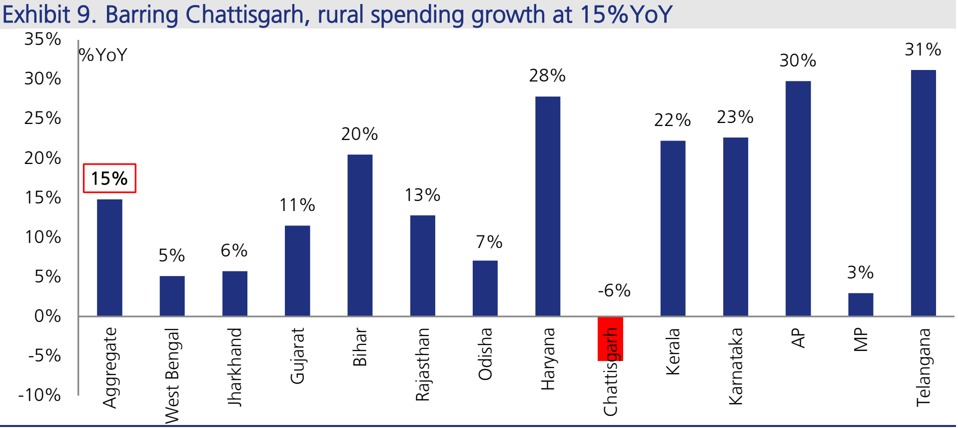
Exhibit 8. Market borrowing for states has reached Rs 2.97trn; 23%YoY mainly driven by Rajasthan



Source: State Budgets, JM Financial

Barring MP, all states sense urgency for higher market loans

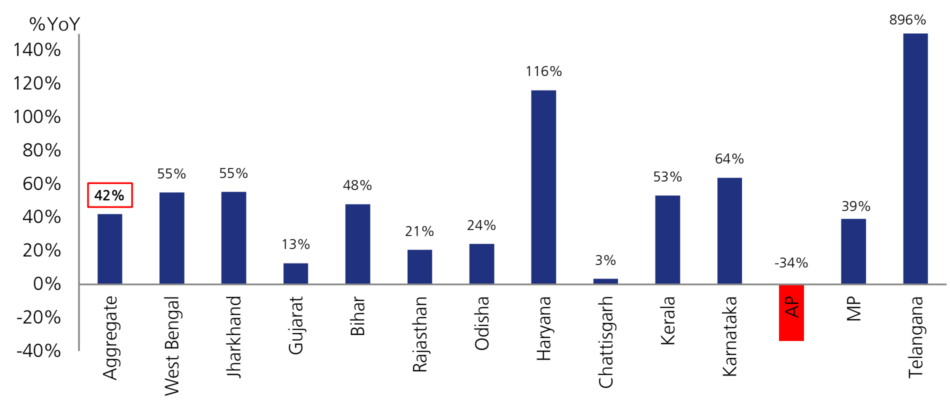
Exhibit 9. Barring Chattisgarh, rural spending growth at 15%YoY



Source: State Budgets, JM Financial; Note: Rajasthan spending also includes expenditure on Energy

Rural spending growth for the aggregate of 13 states continues to be ahead of Union Budget's 11%YoY

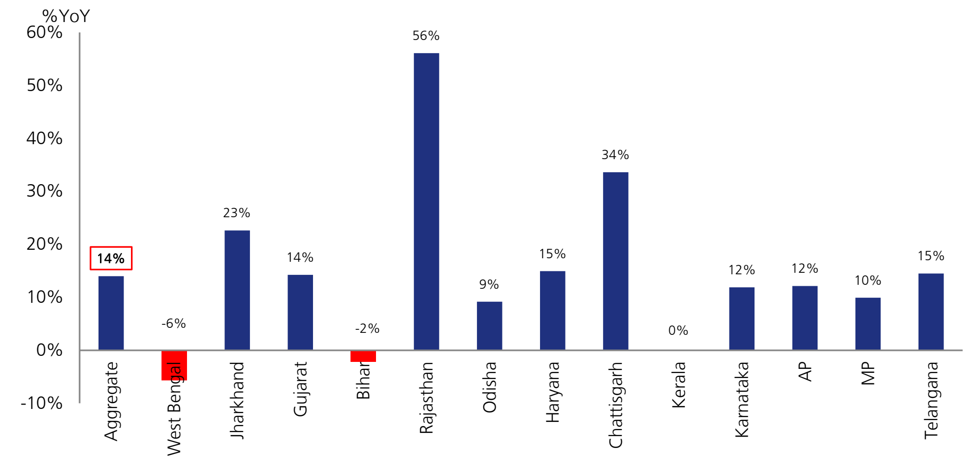
Exhibit 10. Capex on Water, sanitation, housing and urban development has surged across states



Source: State Budgets, JM Financial

Urban sector spending holds dominant share within social sector and is expected to grow by 42%YoY

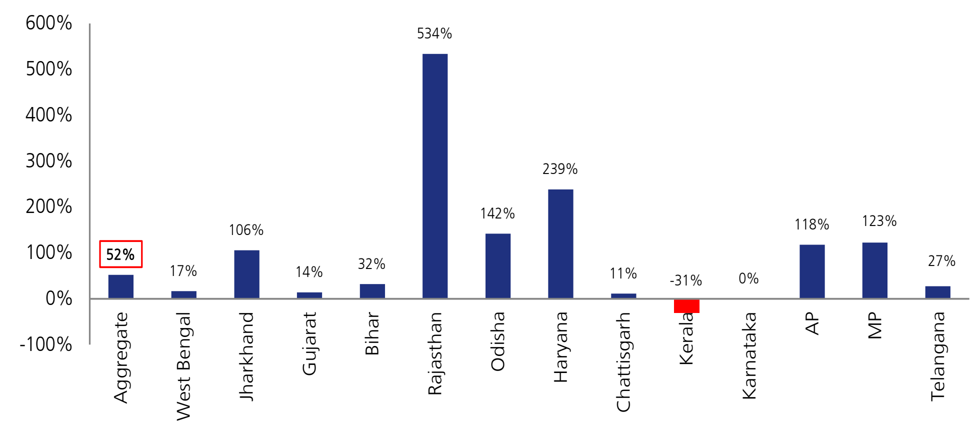
Exhibit 11. Transport, which forms a major head under total spending, is expected to expand by 14%YoY



Source: State Budgets, JM Financial

Transport individually holds a substantial portion of capex. Total spending is projected to expand by 14%YoY

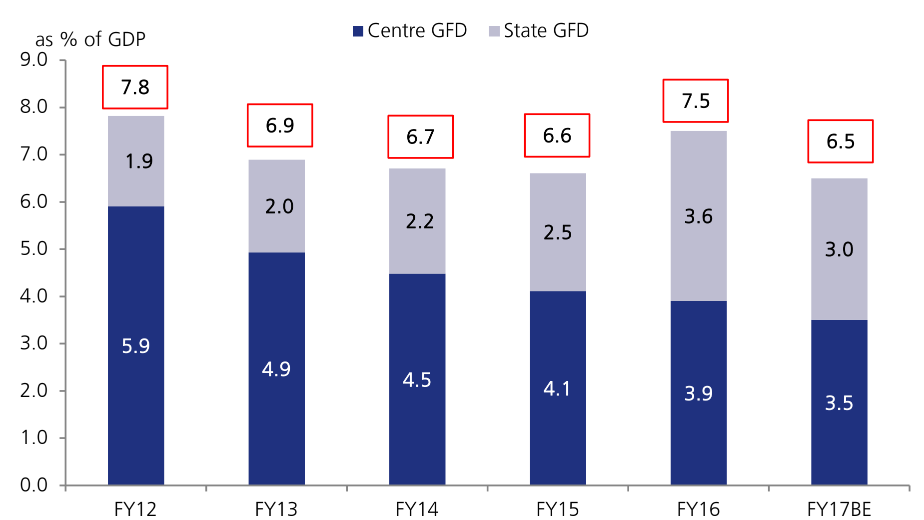
Exhibit 12. Capex growth towards education is encouraging



Source: State Budgets, JM Financial

Continued focus towards education highlights willingness to enhance human capital

Exhibit 13. Combined Fiscal deficit trend



Source: Economic Survey 2016-17, JM Financial; FY16 figures for States are Revised estimates; GFD for States includes UDAY costs

The Centre and states are gradually moving towards the fiscal discipline path

Budget Review- Haryana

In continuation with its effort to bring down the fiscal deficit, Haryana expects to limit the fiscal deficit at 2.84% vs 6.49% in FY16 and 4.27% in FY17. The debt to GDSP ratio also stands within the prescribed limit of FRBM (at 22.93%). The state presented a budget of size Rs 0.9trn, and expects GSDP to grow by 9% in FY18 (vs 8.7%YoY in FY17).

- Haryana manages to limits GFD within FRBM limit for FY18: With overall revenue receipt growth at 14% (vs 27% in FY17) and total expenditure growth at 10%YoY (vs 4% in FY18), the fiscal deficit is estimated to be at 2.84%. Among revenue receipts, own tax revenue (58% of total revenue) is expected to expand by 15% with an increase across heads - corporation tax, income tax, customs, excise & services tax. However, grants in aid, which comprise 9% of total revenue, are expected to fall. On the expenditure side, although capex (7%YoY) has revived (vs -43%YoY in FY17) and is expected to slower than revenue expenditure (10%YoY). The state has increased spending on social sectors by 20% (vs 29% in FY17) with special focus on water, sanitation & urban development (32%YoY), education (19%YoY) and health & family welfare (15%YoY). On the other hand, economic sector spending is estimated to grow by 10%. While allocation towards transport has risen by 15%YoY, spending on energy (comprising 13% of total spending) has declined by 5%. Rural spending is encouraging with agri & allied activities receiving major hike in allocation 48%YoY, followed by rural development (18%YoY) irrigation (14%YoY).

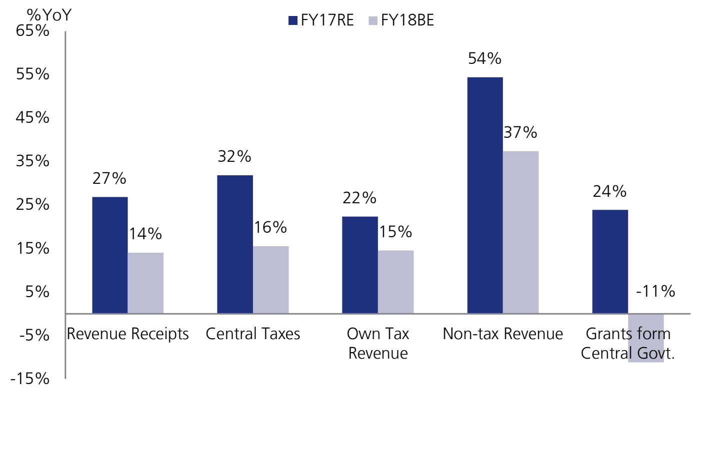
- Social sector receives major boost in capex: The share of capital expenditure in total expenditure has fallen to 13% in FY18 from 25% in FY16. There has been a significant surge in capex towards social services like education (239% YoY), health & family welfare (71%YoY) and Water, sanitation, housing, urban development (116%YoY). Among economic services, rural spending (8% of capex-includes rural development and agri & allied activities)) is expected to increase by 1624%YoY. Capex on energy is projected to fall by 19%YoY (12% of total capex) while transport spending (18% of capex) will expand by 15%YoY.

- Demonetisation & GST implementation: To ease the impact of demonetisation and encourage digital payments, the state has announced 5% rebate for the use of the BHIM app. The finance minister did not introduce any new taxes and no changes in VAT rates were announced.

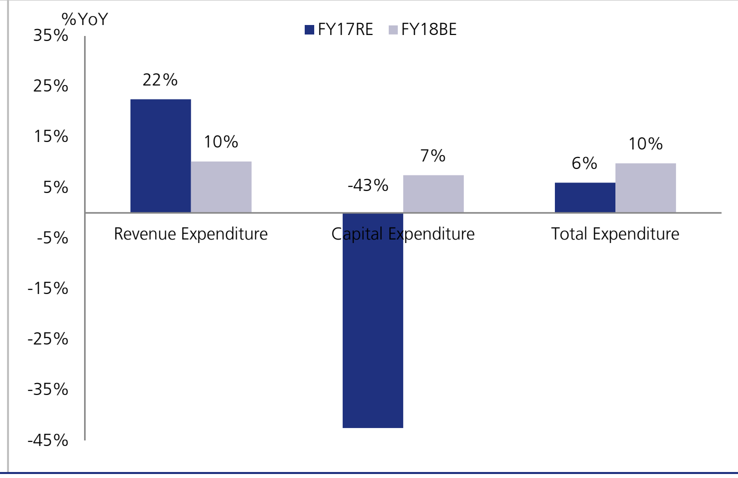
- UDAY & 7th Pay Commission: Haryana has signed an MoU under UDAY scheme. With clear allocation of debt takeover in the budget as per the MoU, we believe that the state has taken into account the additional costs arising from UDAY. The state has announced implementation of the 7th Pay Commission (7PC) for state govt. employees and pensioners from Jan'16, and attributes the Rs 47.7bn rise in revenue expenditure due to hike in DA and salaries owing to the scheme. Salaries and pensions are expected to rise by 15%YoY.

Exhibit 14. Revenue receipts expand faster than expenditure, aiding GFD at 2.84% of GSDP

Trend of revenue receipts



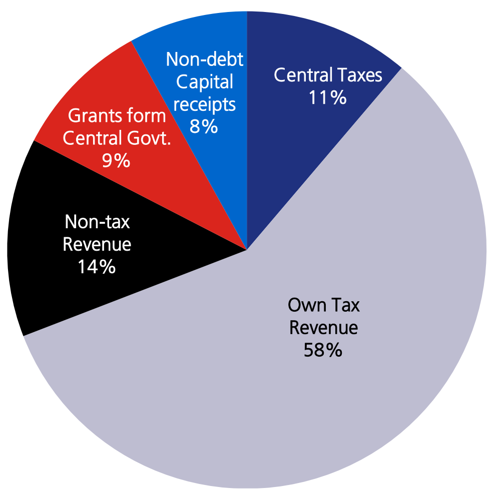
Trend of expenditure disbursements



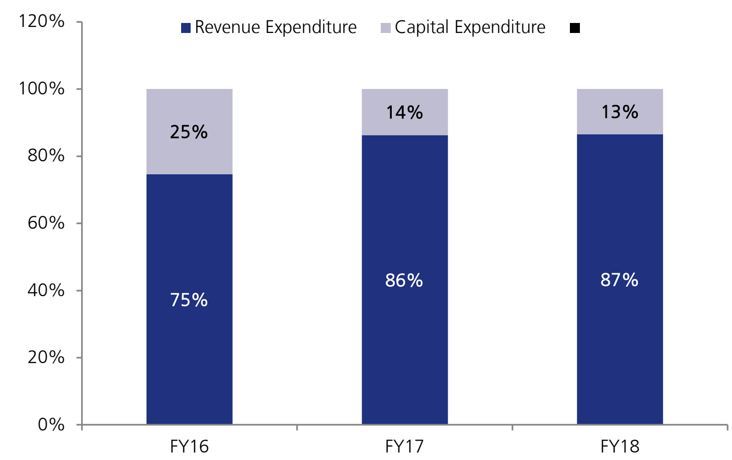
Source: Haryana State Budget, JM Financial

Exhibit 15. Haryana's principal source of revenues is its own taxes; Capex share has been declining

Split of revenue receipts



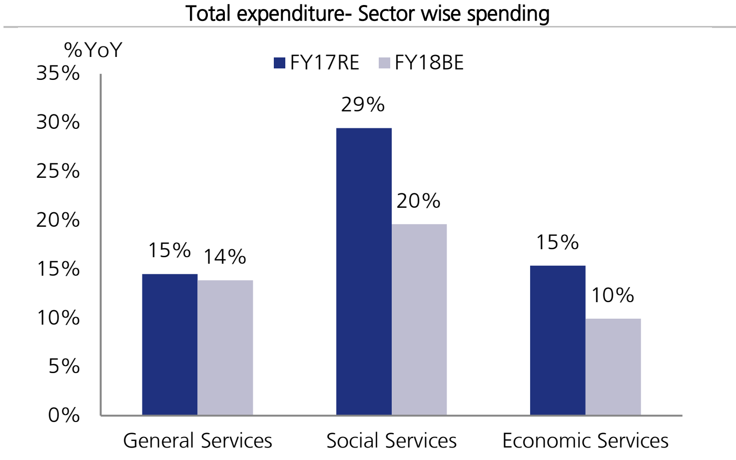
Share of Capital expenditure has fallen to 13% in FY18 vs 25% in FY16



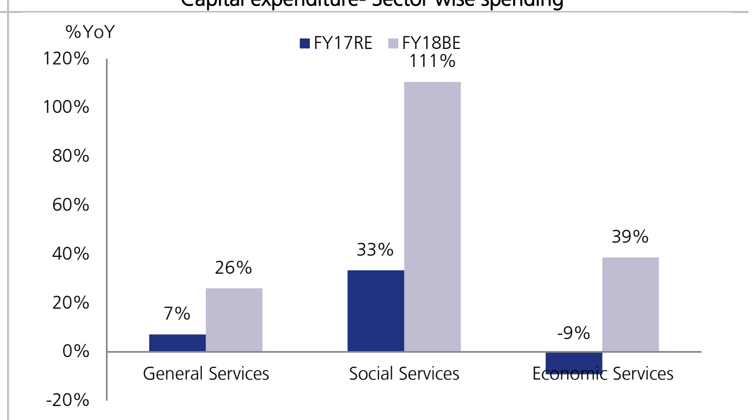
Source: Haryana State Budget, JM Financial

Exhibit 16. Increased allocation towards Social services

Total expenditure- Sector wise spending



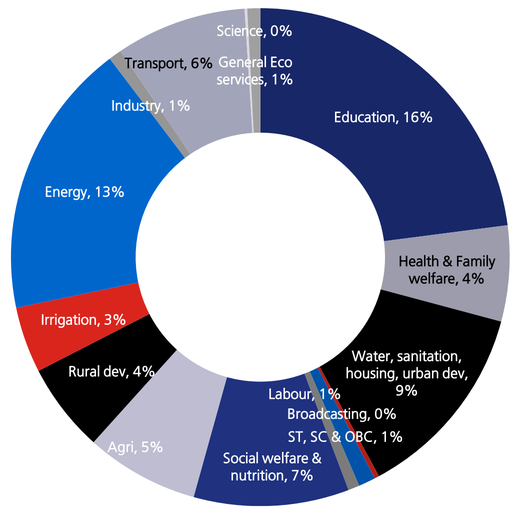
Capital expenditure- Sector wise spending



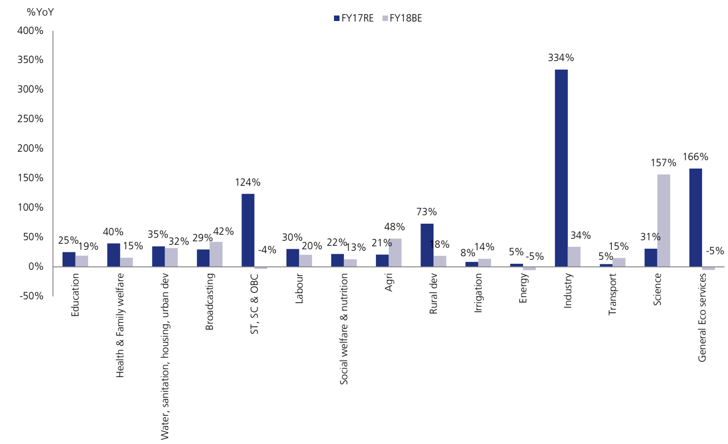
Source: Haryana State Budget, JM Financial

Exhibit 17. Health & family welfare, Education & Water supply & sanitation are priority spending areas

Sub-Sector wise share in total spending



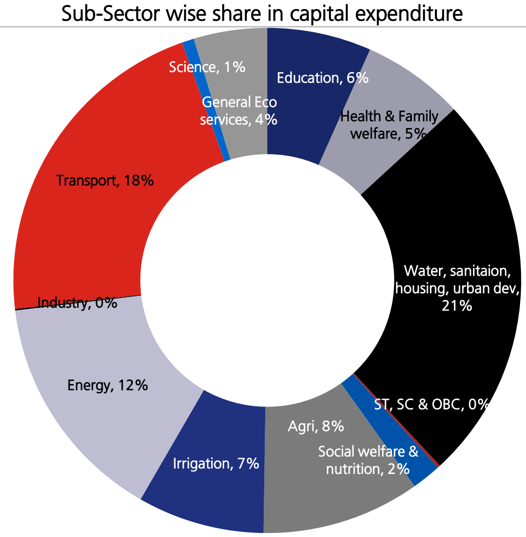
Major spending heads such as education (19%YoY), water supply (32%YoY) and health & family welfare (15%YoY) see upturn in spending



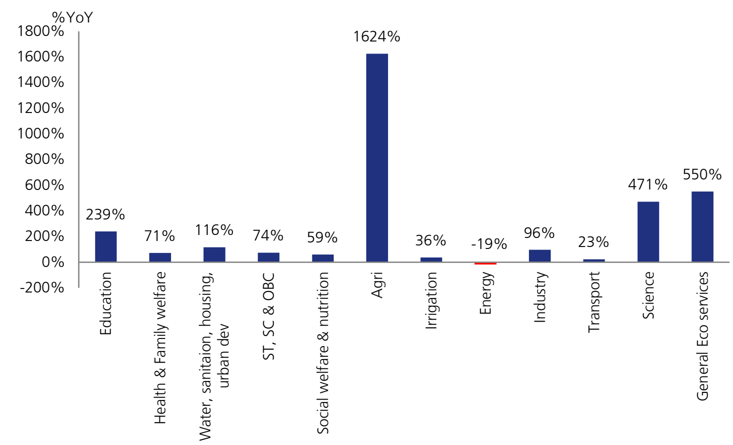
Source: Haryana State Budget, JM Financial

Exhibit 18. Capital expenditure steered by social services, though rural spending remains generous

Sub-Sector wise share in capital expenditure



Capital expenditure growth on agri and education lead



Source: Haryana State Budget, JM Financial

Budget Review- Rajasthan

With a budget of size Rs 1.7trn, Rajasthan expects a fiscal deficit within FRBM norms of 2.99% of GSDP. The state expects one of the highest debt to GSDP ratio of 33.61% by Mar'18. The state has presented its GFD under two scenarios, With UDAY and without UDAY. While it adheres to the FRBM Act under the latter scenario, the former case results in GFD of 6.36% in FY17 and 9.38% in FY16 (vs 3.37% and 3.42% without UDAY).

- With revenue growth 4x that of expenditure, Rajasthan expects to adhere to FRBM: Own tax revenue forms the dominant source of revenue for Rajasthan (38%) and is expected to rise by 16%YoY while share in Central taxes (which comprise of 26% of receipts) are projected to grow by 11%YoY. These buoyant revenues pull overall receipts to 12% YoY growth. On the expenditure side, capital expenditure is estimated to de-grow by 16%YoY, for the second time in a row after it de-grew by 46% in FY17, resulting in overall expenditure growth of 3%YoY. Revenue expenditure on the other hand continues to grow by 7%YoY as against 26% in FY17. Total spending is inclined towards economic services (16%YoY) instead of social services (6%YoY). Irrigation & Energy and transport are the major heads that have received magnified allocation (by 19%YoY & 56%YoY respectively). On the other hand, social services like education (16%YoY) and Health & Family welfare (14%YoY) draw major attention.

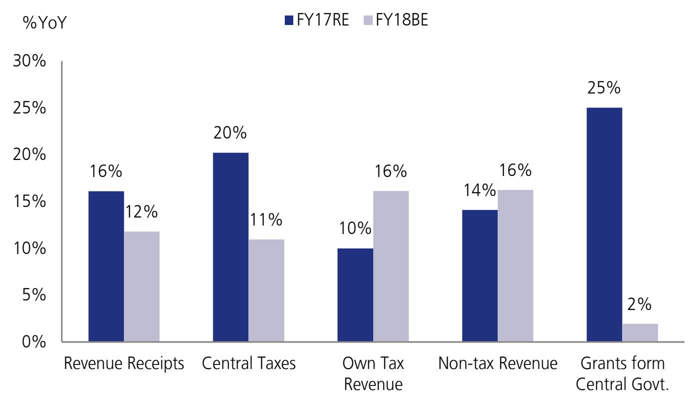
- Capex share continue to decline: Share of capital expenditure has fallen from 36% in FY16 to 16% in FY18, but remains balanced across sectors. Despite the fall in overall capex, allocation towards general, economic and social services has increased as the fall in capex is driven by the 94%YoY decline in loans and advances. Economic sector capex is estimated to grow by 36%YoY with irrigation (29% share) and transport (19% share) spending to expand by 88%YoY with water supply, sanitation, housing & urban dev (26% share) driving capex by 21%YoY.

- Relief against demonetisation and GST implementation: Post demonetisation, amendments in VAT/Electricity duty, luxury tax Act/Rules were made to provide relief to dealers. The state government has provided relief in Stamp duty and registration fees and introduced e-governance measures for the same. No new taxes in VAT, entry taxes, luxury tax and entertainment tax besides the increase of VAT on cigarette by 15%. The state is prepared for GST implementation through training, centralized call centers, simulation center (to be established in Jaipur), and GST help desk. So far c.80% of registered dealers have migrated to GST through primary enrolment.

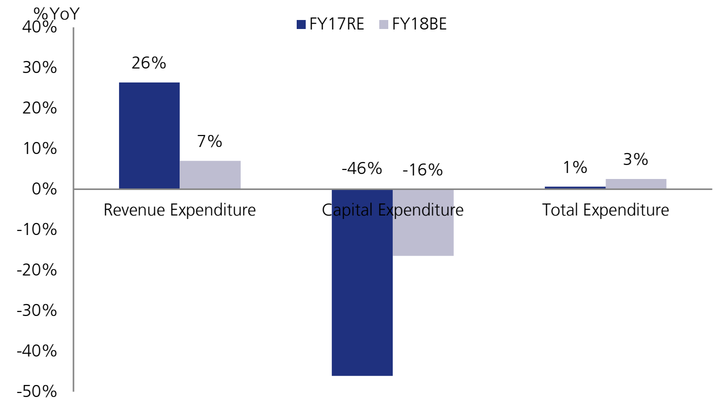
- UDAY & 7th Pay Commission: The state govt. has signed separate MoUs for Ajmer, Jodhpur and Jaipur under the UDAY scheme. They have accounted the additional costs in their budget, the reason for their GFD touching 5.62% and 6.36% in FY16 and FY17 respectively. Rajasthan has formed a three member to study the burden and impact of 7PC on state finances. A decision will be taken post the recommendations for the state level committee. In the budget, salaries and wages are expected to grow by 39%YoY while pensions at 11.7%YoY.

Exhibit 19. Strong revenue growth is expected to bring down the GFD to 2.99%

Trend of revenue receipts



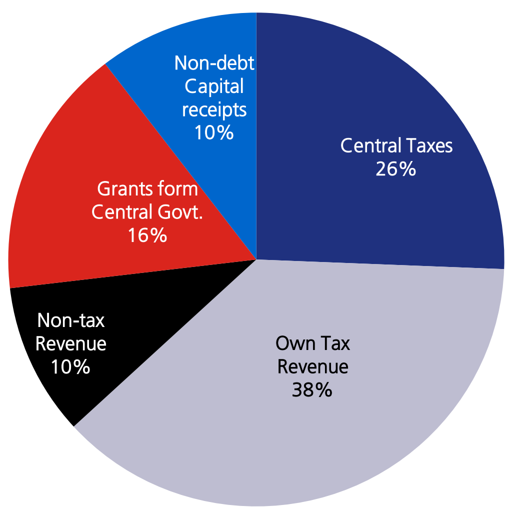
Trend of expenditure disbursements



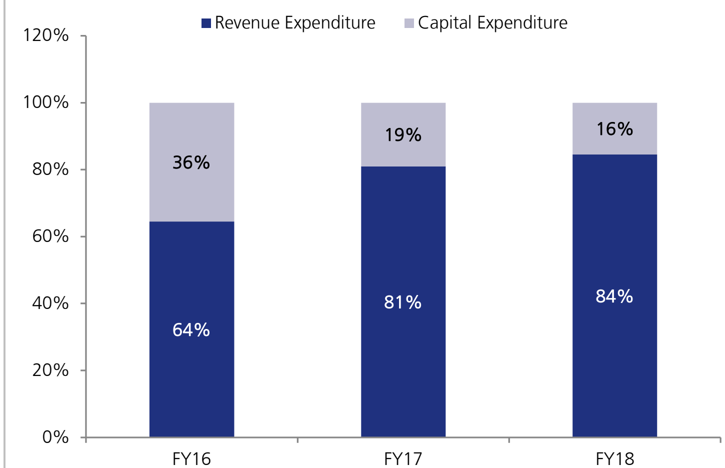
Source: Rajasthan State Budget, JM Financial

Exhibit 20. Central taxes & Own-taxes hold major share in total receipts

Split of revenue receipts



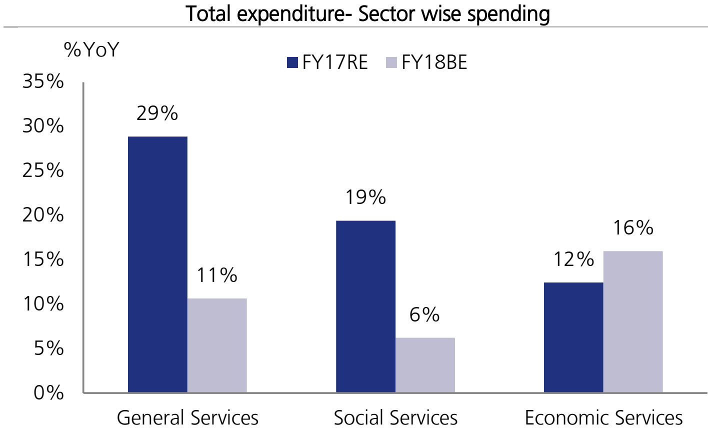
Share of Capital expenditure fall further to 16%



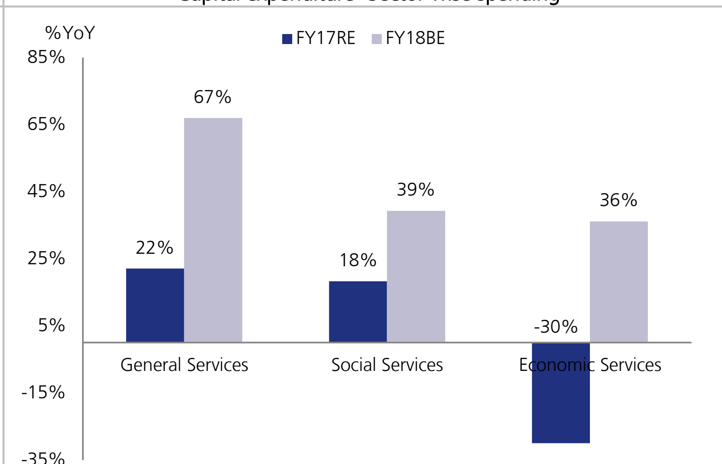
Source: Rajasthan State Budget, JM Financial

Exhibit 21. Increased capex allocation towards General services

Total expenditure- Sector wise spending



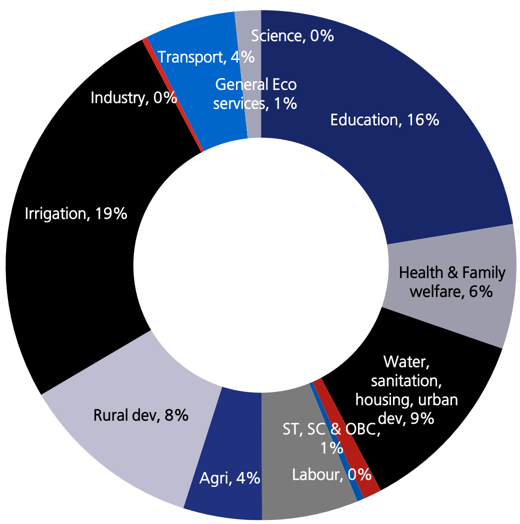
Capital expenditure- Sector wise spending



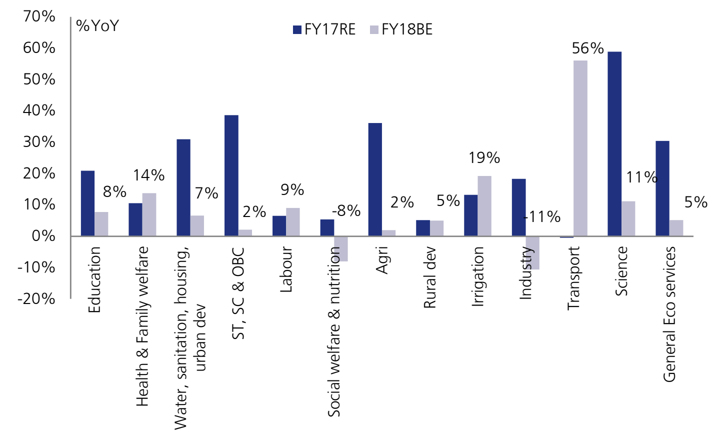
Source: Rajasthan State Budget, JM Financial

Exhibit 22. Trends in Total Expenditure

Sub-Sector wise share in total spending



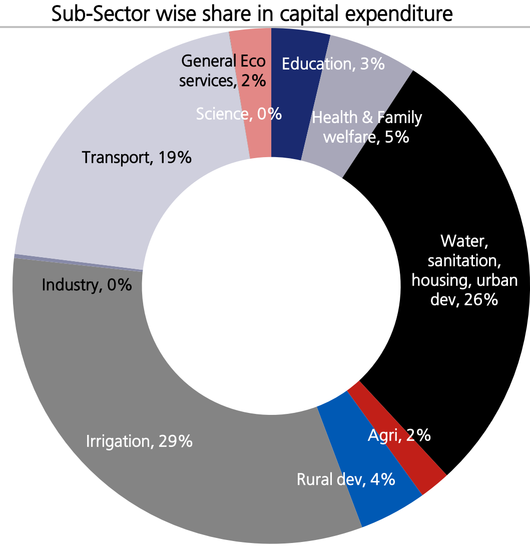
Economic services drive total expenditure



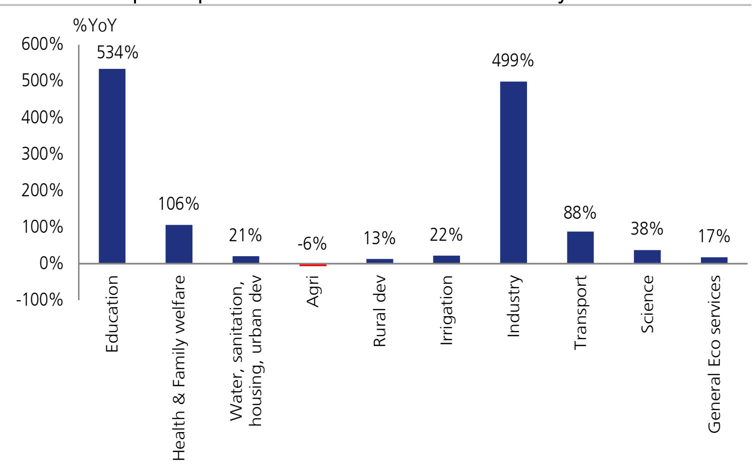
Source: Rajasthan State Budget, JM Financial, * Irrigation includes expenditure on power

Exhibit 23. Capital Expenditure has fallen 16%YoY but due to fall in loans and advances (-94%YoY)

Sub-Sector wise share in capital expenditure



Capital expenditure on social services increases by 39%



Source: Rajasthan State Budget, JM Financial; * Irrigation includes expenditure on power

Budget Review- Andhra Pradesh

AP has presented a budget of size Rs 1.49trn, with fiscal deficit within the FRBM target of 3%. The state claims to lead real GSDP growth in the country with 12%YoY. Despite the reduction in debt to GSDP ratio from 28.5% in FY16 to 27.6% in FY17, the state projects the ratio to surge to 28.11% again, owing to high outstanding debt of the govt. Being predominantly agrarian, with 60% of population deriving their livelihood from the primary sector, the state has laid special emphasis on rural spending.

- Healthy growth in receipts keep deficit under control: Although AP's dominant source of revenues are its own tax revenues (43%, 9%YoY), it heavily depends on the Centre for grants (30% share; 36%YoY). Overall revenue receipts are expected to grow by 17%YoY as against 22%YoY in FY17. Both, share in Central Taxes and own tax revenue have seen a decline in growth rate vis-à-vis FY17 (11% vs 20% and 9% vs 23%YoY respectively).On the expenditure side, total expenditure growth remains steady at 17%YoY vs 15% in FY17. Total outlay is driven by capital expenditure (55%YoY vs revenue expenditure growth at 12%). Share of capex has increased to 15% in FY18 vs 13% in FY16. Total spending is directed towards economic services (29%YoY), followed by general services (16%YoY). Rural development (26%YoY) and irrigation (58%YoY) drives the total spending in economic sectors. Social services like education (comprising of 15% of total spending) and welfare of Minority (8% share in total spending) are expected to grow by 10% and 23% respectively. Given these, the fiscal deficit is expected to be at 3.0% of GSDP vs 3.06% in FY17.

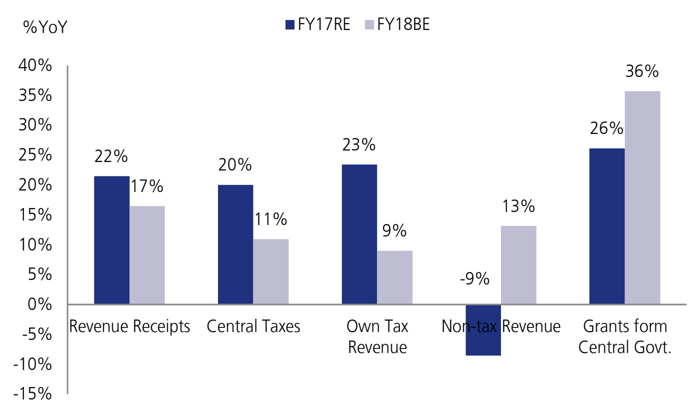
- Capex on economic services revives: As against the de growth in economic sector capex in FY17, economic services (71%YoY) are expected to witness higher growth at the cost of social services (16%YoY). Among economic services, irrigation has maximum share of 52%, followed by transport (9%). While irrigation spending is expected to grow by 62%, the latter bears reduced funds (-3%YoY).Other components of rural spending such as agriculture and allied activities and rural development on roads and housing have received a major boost. Among social services, capex has been channeled majorly towards education (118%YoY) and welfare of SC, ST & OBCs (89%YoY). Spending on water supply, sanitation, housing & urban development, which constitutes 6% of capex has been projected to fall by 34%YoY.

- Demonetisation and GST implementation: No new taxes have been introduced as GST is expected to be implemented. Post demonetisation the state has been encouraging adoption of digital payments. Through a campaign mode, the state has helped rural merchants, agri laborers, self-employed and SHG women members to obtain RuPay Debit Cards, use mobile banking apps for facilitating cashless transactions. Aadhaar Enabled Payment System has been made functional in all fair price shops

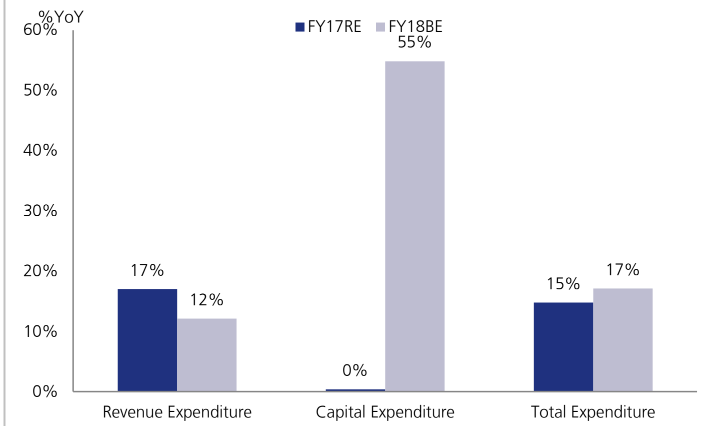
- UDAY & 7th Pay Commission: AP has signed for the UDAY scheme in Nov'15 and took over Rs 82.6bn of debt of its DISCOMS, has accepted that it is likely to deteriorate its finances in the coming years. The state has not implemented the 7th Pay Commission but continues to revise the salaries and pensions more frequently than the Centre .It also seeks to release installments of Dearness Allowance arrears to employees for FY17 and FY18.

Exhibit 24. AP expects a fiscal deficit well within FRBM limits

Trend of revenue receipts



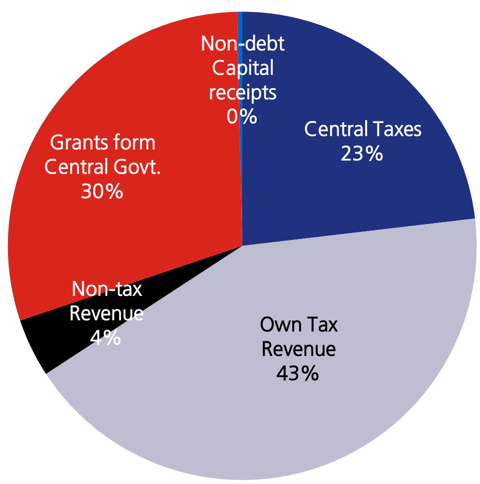
Trend of expenditure disbursements



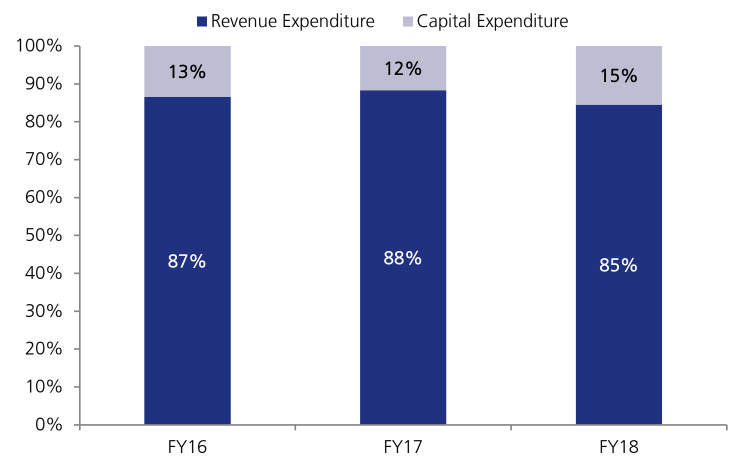
Source: AP State Budget, JM Financial

Exhibit 25. While own taxes from dominant source of revenue, AP relies heavily on the Centre for grants

Split of revenue receipts



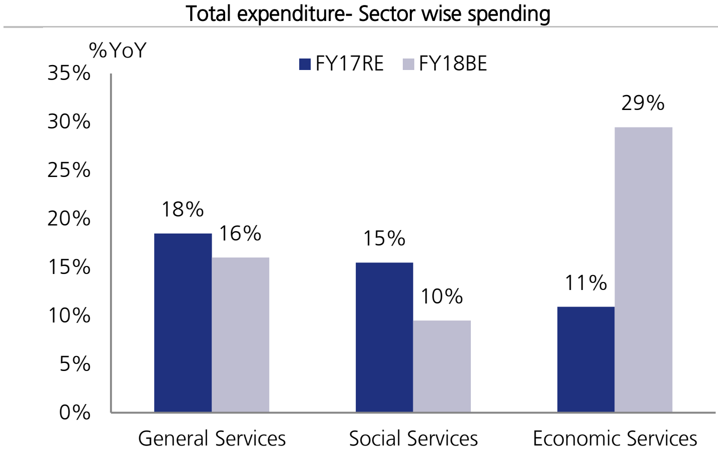
The share of capital expenditure has improved to 15%in FY18



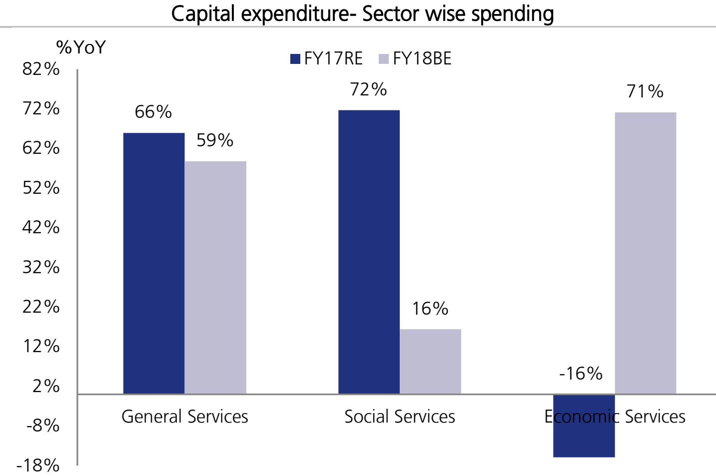
Source: AP State Budget, JM Financial

Exhibit 26. Economic Services preferred at the cost of Social Services

Total expenditure- Sector wise spending



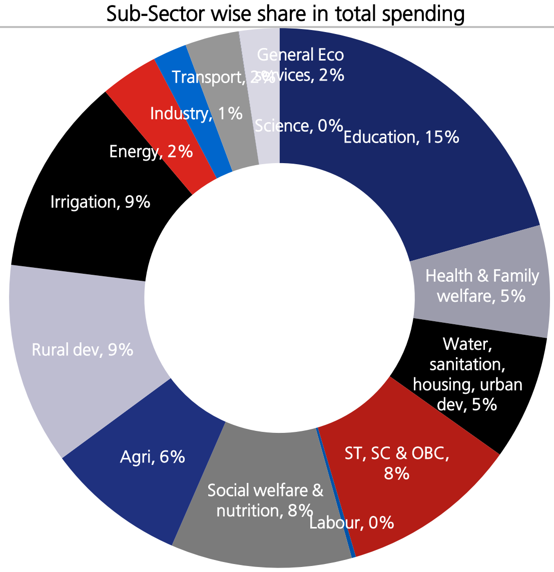
Capital expenditure- Sector wise spending



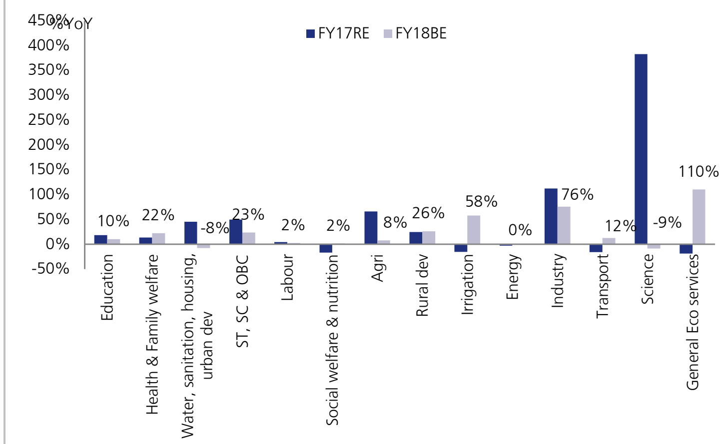
Source: AP State Budget, JM Financial

Exhibit 27. Trends in Total Expenditure

Sub-Sector wise share in total spending



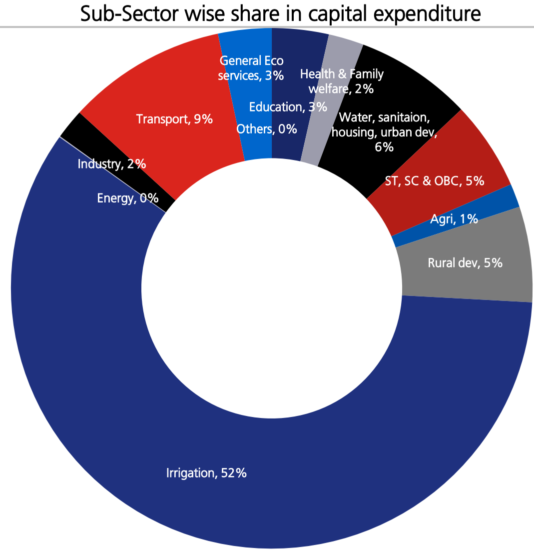
Economic services like irrigation & Transport drive total expenditure



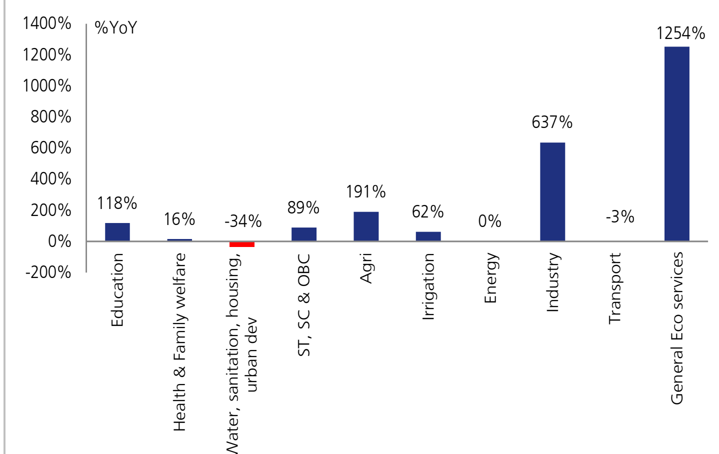
Source: AP State Budget, JM Financial

Exhibit 28. Irrigation and Education drive capital expenditure

Sub-Sector wise share in capital expenditure



Capital expenditure on rural sector rises substantially



Source: AP State Budget, JM Financial

Budget Review- Telangana

Presenting a budget of size Rs 1.45trn, Telangana expects a double-digit real GSDP growth of 10.1% in FY17 vs national GDP growth of 7.1%, despite demonetisation. The GFD for FY18 is estimated at 3.48%, within the FRBM Act vs 3.35% in FY17RE. The budget focuses on welfare of poor and employment generation for them. It claims to rank first among all states in terms of welfare programs, as it has implemented more than 30 special welfare programs.

- Telangana fiscal deficit at 3.48% of GSDP despite robust expenditure growth: Own tax revenues are the principal source of revenue (53%) for Telangana. Accusing demonetisation to adversely affect revenue collections under stamps and registration and to some extent even VAT collections, the revised tax revenue for FY17 has been reduced by 6%. However, tax revenues for FY18 are expected to witness healthy 22% YoY. The second major source of revenue are grants from Centre (23%) which are projected to grow by 98%YoY driving overall revenue receipts by 30%YoY. On the other hand, total expenditure is expected to grow by 33%YoY vs 15%YoY in FY17, with capex growth (65%YoY) more than twice that of revenue expenditure (25%YoY). The state has increased spending on social sectors by 30% with special focus on water, sanitation & urban development (95%YoY), Minority welfare (31%YoY) and education (23%YoY). Although less preferred, economic services like irrigation (51%YoY) and Rural development (11%YoY) drive the 23%YoY increase in economic sector spending.

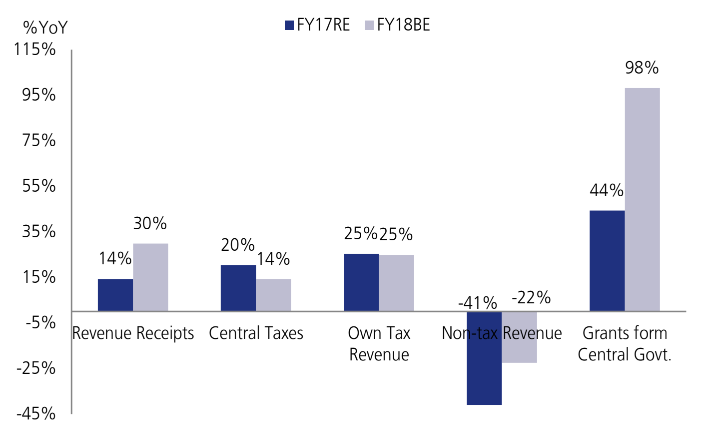
- Capex concentrated towards Social services: The share of capital expenditure in total expenditure is expected to rise to 24% in FY18 vs 20% in FY16. Water, sanitation & urban development (comprises 10% of total capex) is expected to increase by 896%YoY. Other social services like Welfare of SC, ST & OBCs and Health & Family welfare have received increased allocation by 8%YoY and 56% YoY. Industry & minerals spending is projected to surge by 3126%YoY but this comprises merely 1% of total capex. While irrigation constitutes 41% of total capex, allocation for FY18 has increased only by 4%YoY. Overall focus on rural has been maintained through expenditure on rural development and agri and allied activities.

- Demonetisation & GST implementation: The state did not introduce any new taxes in view of GST implementation. The state claims to do well despite demonetisation and has hence not announced any specific measures to soften the adverse impact of demonetisation, although rural spending stands at 31%YoY (double of the 13 state average so far) attributable to various welfare programs.

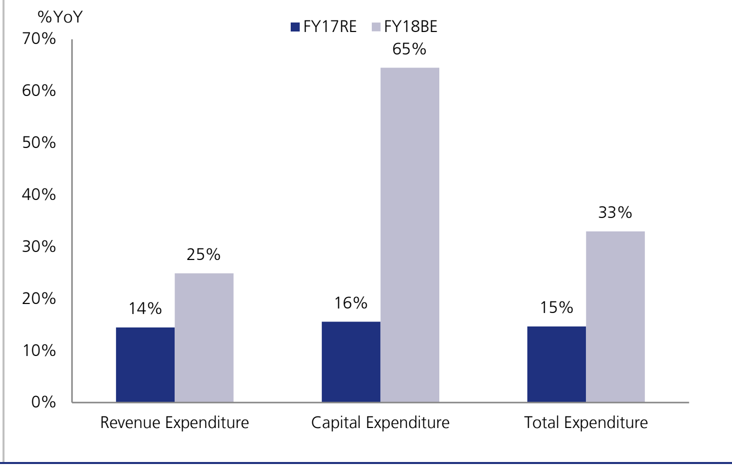
- UDAY & 7th Pay Commission: Telangana has signed up for the UDAY scheme. The finance ministry in his speech announced that they have taken over the debt of Rs89.23bn from its DISCOMS. The state has not implemented the 7th Pay Commission but revises the salaries of its employees every five years (more frequently that Central Govt).

Exhibit 29. Revenue receipts & Expenditure grow robustly by 30%+YoY; GFD within FRBM limits

Trend of revenue receipts



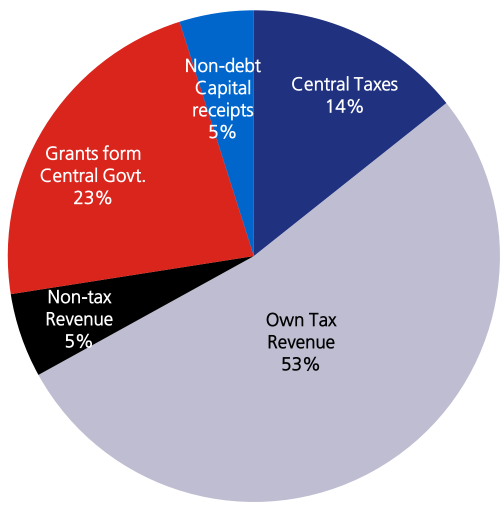
Trend of expenditure disbursements



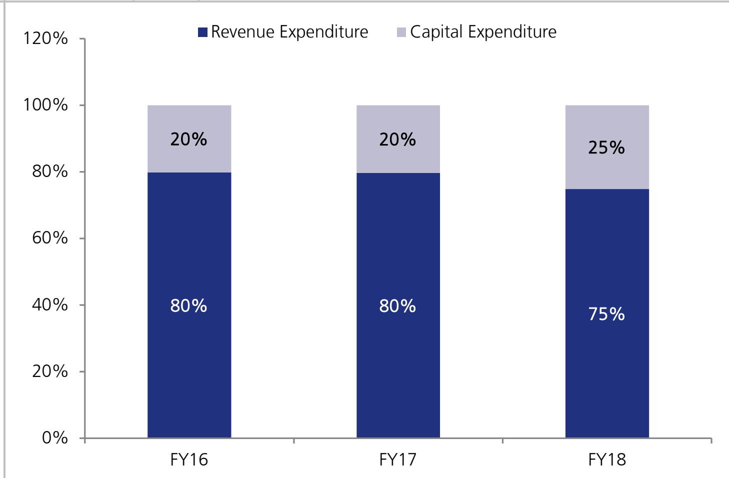
Source: Telangana State Budget, JM Financial

Exhibit 30. Own tax revenue leads as revenue source; Capex share increased to 25%

Split of revenue receipts



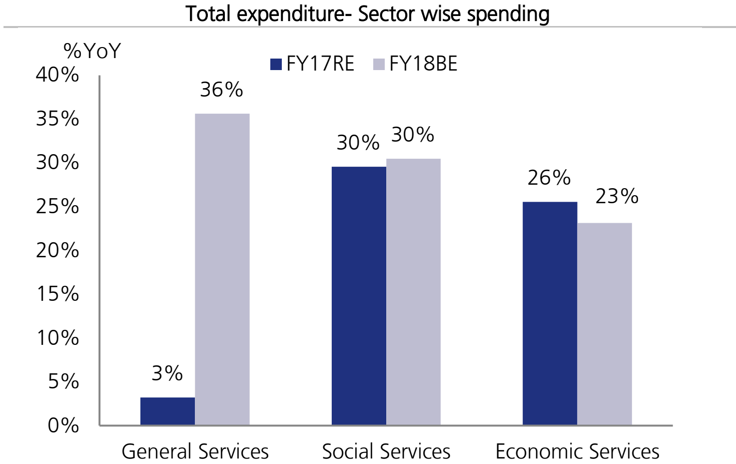
Share of Capital expenditure has increased to 25% in FY18 vs 20% in FY17



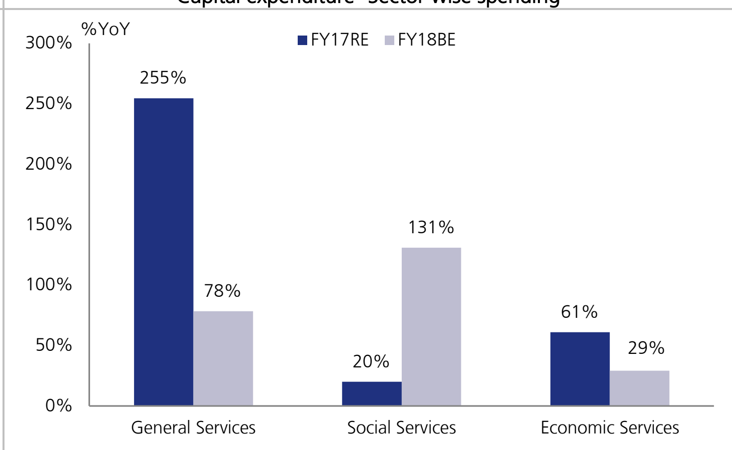
Source: Telangana State Budget, JM Financial

Exhibit 31. Increased allocation towards General services; Social Services preferred over economic services

Total expenditure- Sector wise spending



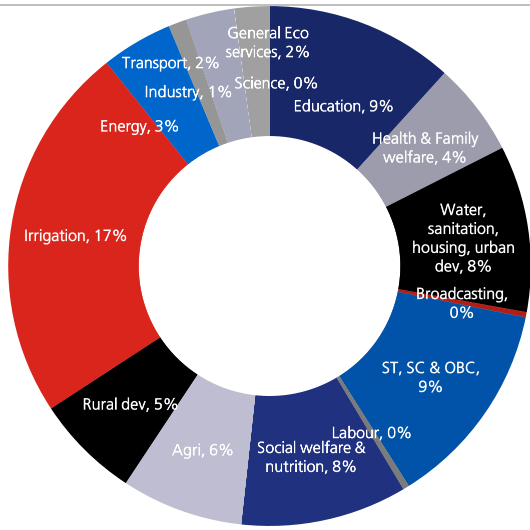
Capital expenditure- Sector wise spending



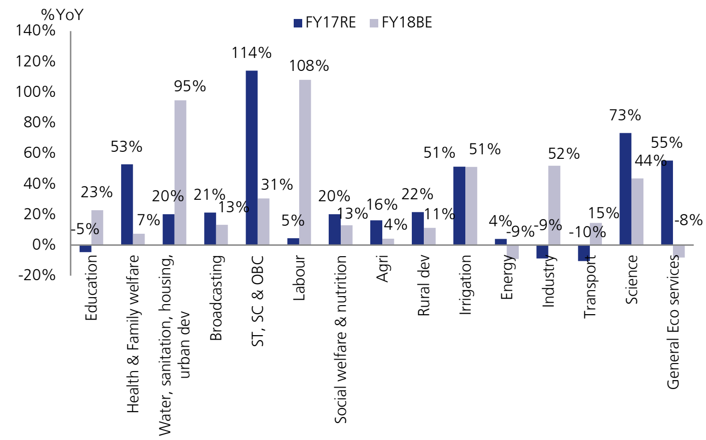
Source: Telangana State Budget, JM Financial

Exhibit 32. Water supply, sanitation, housing and urban development are priority spending areas for Telangana

Sub-Sector wise share in total spending



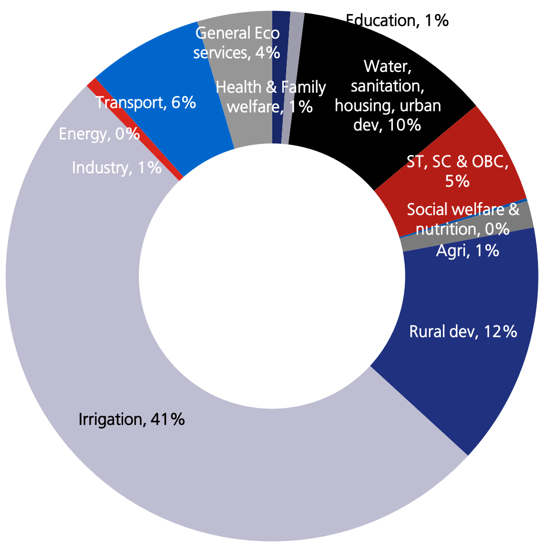
Major spending heads such as irrigation (51%YoY), water supply (95%YoY) and education (23%YoY) witness higher allocation



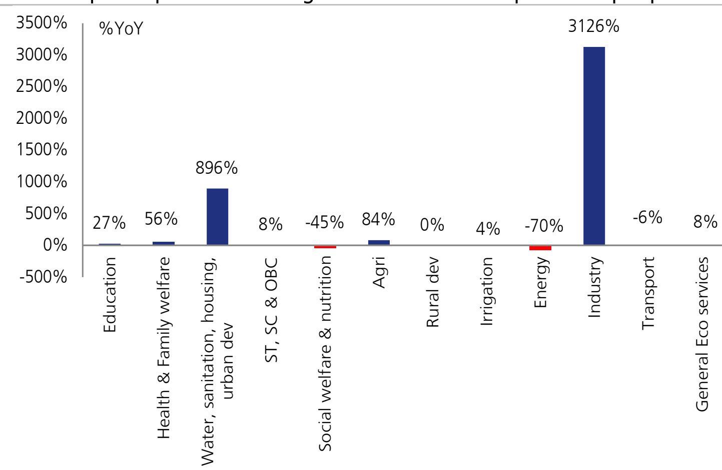
Source: Telangana State Budget, JM Financial

Exhibit 33. Capital expenditure governed by social services, though rural spending remains steady

Sub-Sector wise share in capital expenditure



Capital expenditure on irrigation and rural development steps up



Source: Telangana State Budget, JM Financial

Budget Review- Karnataka

Presenting a budget of size Rs 1.78trn, Karnataka not only adheres to the GFD limit of FRBM (2.61% of GDSP vs limit of 3.5%), but also expects its debt to GSDP ratio at 18.93% (within FRBM limit of 25%).

- Karnataka adheres to fiscal indicators of the FRBM: Karnataka has managed to adhere to the FRBM act norms, despite the fact that its total expenditure for FY18 is expected to grow faster than revenue receipts (13%YoY vs 9%YoY). On the receipts side, own tax revenues (which constitute 62% of total revenue) are expected to grow by 9%YoY; identical to grants from the Centre. The state derives 61% of own taxes revenue from Commercial taxes followed by state excise (20%). FY17 witnessed a fall in own tax revenue because hit in collections of stamps and registration department owing to demonetisation. On the other hand, total expenditure is expected to grow by 13%YoY vs 15%YoY in FY17, mainly driven by capex. Growth in spending on economic services (17%YoY) is almost double than that of social services (8%YoY). Major heads under economic sector like irrigation (43%YoY), agri (16%YoY), energy (21%YoY) and transport (12%YoY) receive major boost in spending. The state has increased spending on social sectors by 8% with special focus on water, sanitation & urban development (21%YoY) and Minority welfare (24%YoY), while education is expected to witness de-growth in spending (-5%YoY).

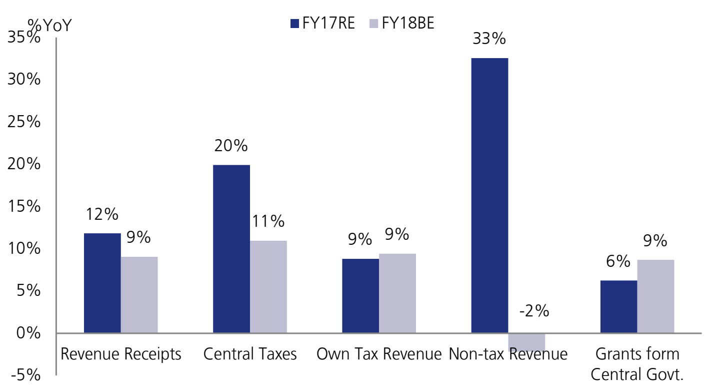
- Capex on Social and economic services to grow by 29%+YoY: The share of capital expenditure in total expenditure is expected to rise to 18% in FY18 vs 15% in FY16. Social services (37%YoY) have received priority over economic services (29%YoY). Social services like Welfare of SC, ST & OBCs (31%YoY, 9% share) and water, sanitation & urban development (64%YoY, 10% share) pull capex towards social services. Among economic services, irrigation (47%YoY, 39% share) and transport (8%YoY, 19% share) spending is projected to surge.

- Demonetisation & GST implementation: Post demonetisation, the state suffered in terms of revenue. The state has hence made significant changes in the tax structure. Administrative fee on spirit was withdrawn. While the VAT on beer, fenny, liquor and wine has been removed, additional Excise Duty (AED) has been increased. The state proposes to welcome GST by allowing industry and trade to clear pending tax liabilities. For this, it has proposed Karasamadhana Scheme to waive 90% of penalty and interest on payment of full tax and remaining 10% of penalty and interest by 31st May 2017. It has exempted taxes on flour of Navane, Same, Aaraka and Baragu and husk of coconut and pulses. The state is holding workshops to increase awareness on GST along with e-initiatives like e-UPaSS.

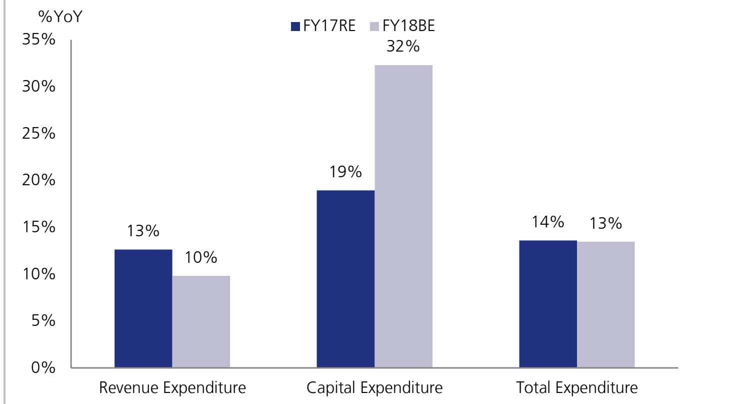
- UDAY & 7th Pay Commission: Karnataka has signed an MoU under UDAY scheme. It is not very clear whether Karnataka has accounted for all its additional costs from UDAY, but its GFD is expected to remain under 3% of GSDP. The state has announced to implement the 7th Pay Commission (7PC) but the salary & pension growth of 12%YoY (14% and 8.7% respectively) in the budget signals some unaccounted cost.

Exhibit 34. Despite higher expenditure growth, Karnataka expects a fiscal deficit of 2.61%

Trend of revenue receipts



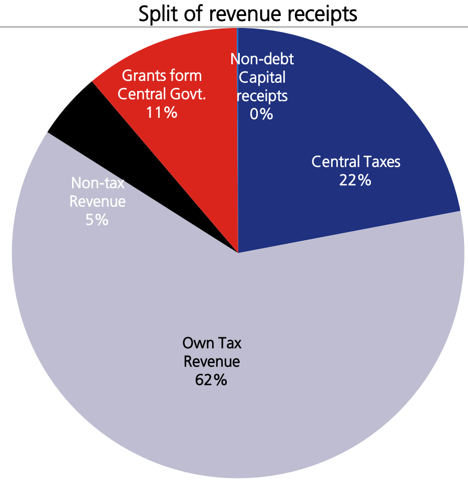
Trend of expenditure disbursements



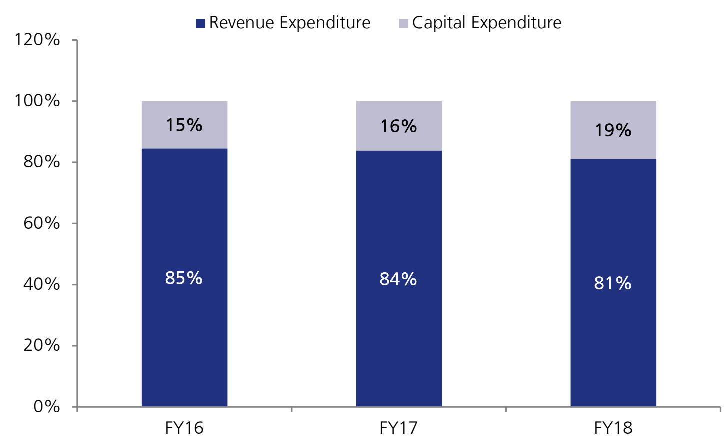
Source: Karnataka State Budget, JM Financial

Exhibit 35. Own tax revenue constitutes 62% of revenue receipts; Capex share increased to 19%

Split of revenue receipts



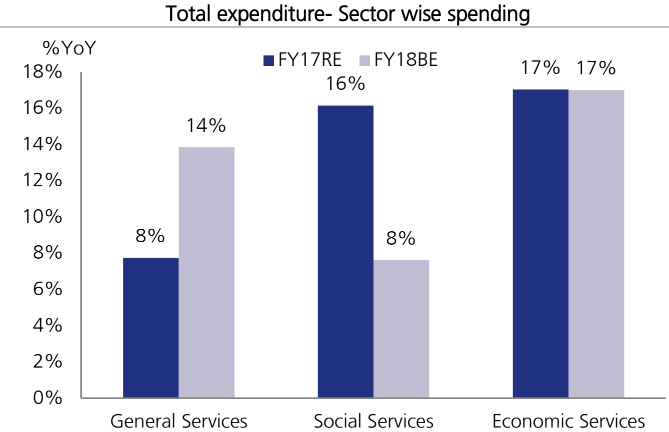
Share of Capital expenditure has increased to 19% in FY18 vs 15% in FY16



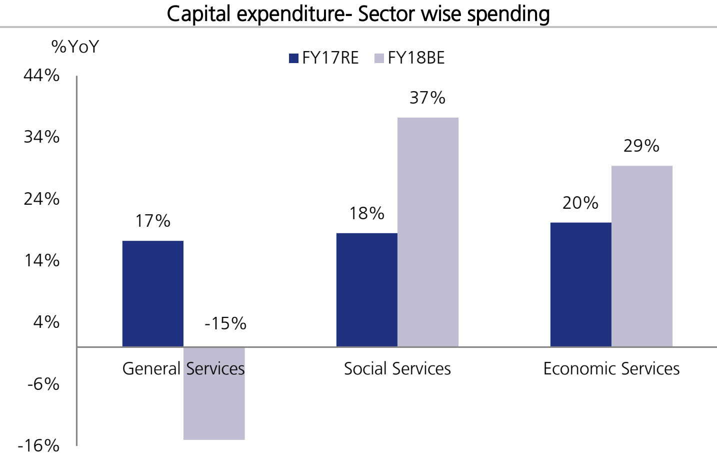
Source: Karnataka State Budget, JM Financial

Exhibit 36. Social and Economic services constitute major spending

Total expenditure- Sector wise spending



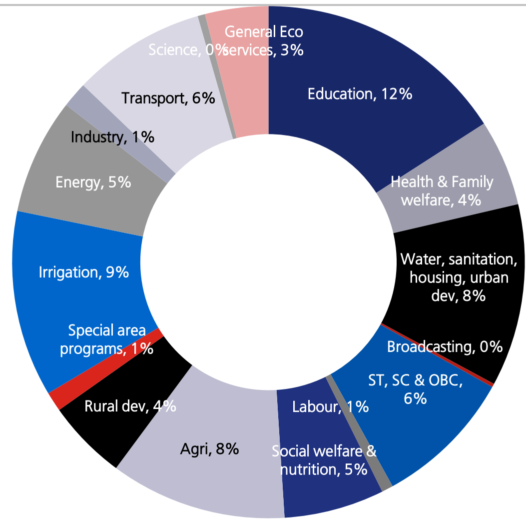
Capital expenditure- Sector wise spending



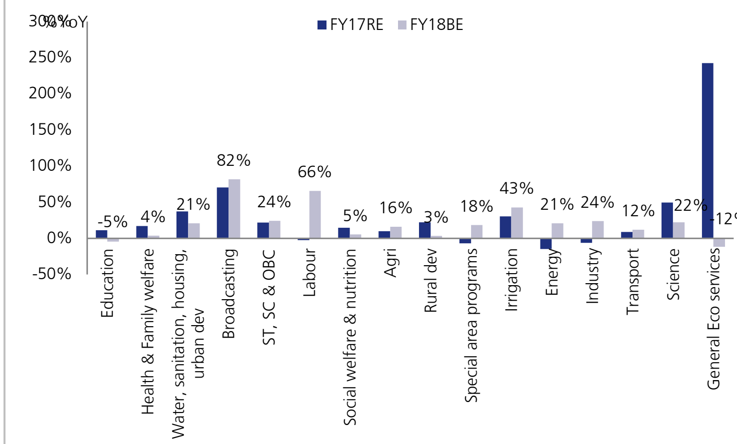
Source: Karnataka State Budget, JM Financial

Exhibit 37. Water supply, sanitation, housing and urban development, energy and irrigation priority spending areas

Sub-Sector wise share in total spending



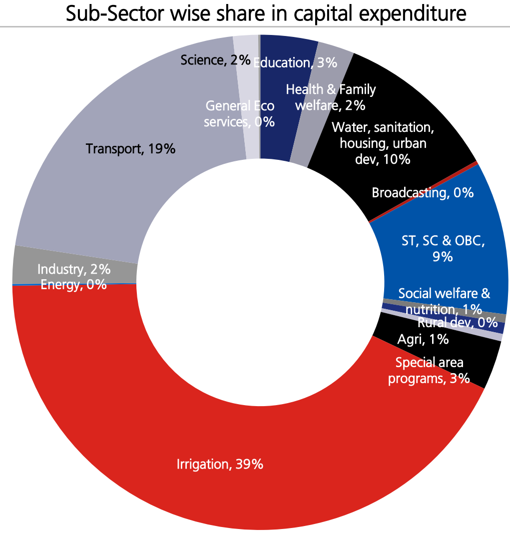
Major spending heads such as irrigation (43%YoY), water supply (21%YoY) and energy (21%YoY) witness higher allocation



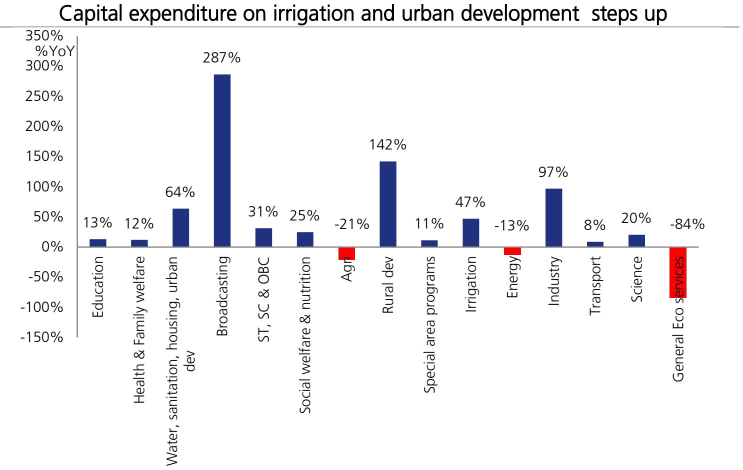
Source: Karnataka State Budget, JM Financial

Exhibit 38. Social and economic services to grow by 29%+YoY

Sub-Sector wise share in capital expenditure



Capital expenditure on irrigation and urban development steps up



Source: Karnataka State Budget, JM Financial

Budget Review- Odisha

The state of Odisha has tabled a budget of size Rs 1.03trn with fiscal deficit at 3.5% of GSDP. It has brought down its debt to GSDP ratio from 50.73% (highest in the country) as on Mar'03 to 15.21% by Mar'16 and further expects it to be at 18.61% by Mar'18. Despite demonetisation, the state expects a nominal GDSP growth of 10.85%YoY for FY17 due to higher growth in agricultural sector (above national estimates). The budget focuses on inclusive development and has spent extensively on social welfare schemes.

- Odisha fiscal deficit at 3.5% of GSDP: The state expects a tax to GSDP ratio for FY18 at 6.50% with tax revenue growth at 13%YoY. Share in central taxes forms dominant source of revenue (35%) and is expected to grow by 11%YoY. Own tax revenues which comprise 30% of revenue receipts, are expected to grow by 16%YoY. Overall revenue receipts are expected to grow by 11% vs 16% in FY17. Outlays, on the other hand are projected to expand by 12%YoY, mainly driven by revenue expenditure (13%YoY vs 24%YoY in FY17). The pattern of expenditure preference has remained identical as FY17, with general services leading (20%YoY), followed by social (17%YoY) and economic services (6%YoY). Major spending heads under social sector such as education (16% share, 24%YoY), health & family welfare (5% share; 17% YoY) and water supply, sanitation, housing and urban development (6% share, 16% YoY) drive social spending. Among economic services transport (9% share, 9%YoY), irrigation (9% share, 21%YoY) receive thrust of spending.

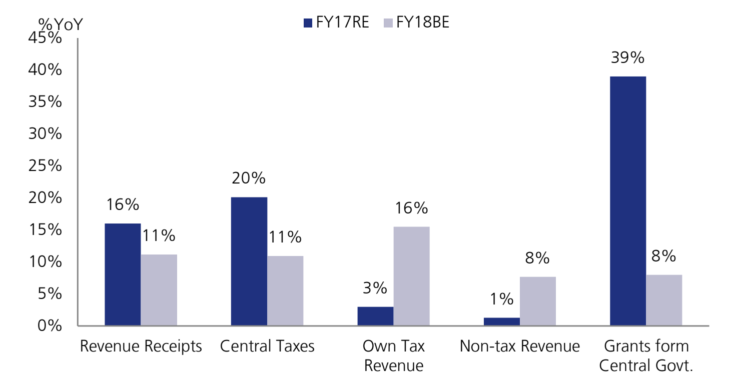
- Capex towards Social services witnesses upsurge: The share of capital expenditure in total expenditure is expected to remain stagnant at 22% in FY18. Although irrigation and transport form the chief capital spending areas (33% and 31% share respectively in total capex), social services have received the bulk of increase in capex with health and family welfare (5% share, 206%YoY) and education (4% share, 142%YoY) expenditure advancing substantially. Irrigation and transport capex is projected to grow by 24%YoY and 2%YoY respectively.

- Demonetisation & GST implementation: The finance minister did not introduce any new taxes. Various preparatory activities such as establishment of GST Network, training of officers, migration of dealers to GSTN and engagement with different Stakeholders are being undertaken by the state. Post demonetisation, initiatives has been taken to ensure Government Offices and agencies are enabled to receive digital payments of all kinds including net banking, debit and credit cards and Aadhar-based payment.

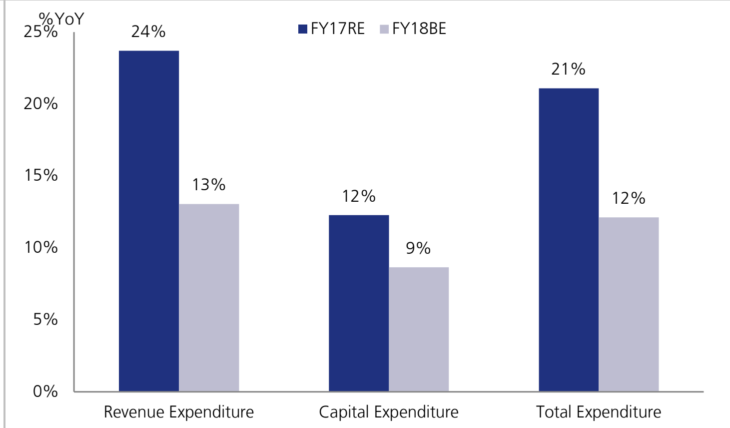
- UDAY & 7th Pay Commission: Odisha has not signed MoU under UDAY scheme. As far as 7^{th} Pay Commission (7PC) is concerned, with recent announcement of implementation of the scheme for state govt. employees and pensioners from Jan'16. We believe that the additional costs due to 7PC has been taken into account as salaries and pensions are expected to rise by 17%YoY in FY18 (22% and 10.6% respectively)

Exhibit 39. With buoyant tax revenues, GFD at 3.5% of GSDP-within FRBM limits

Trend of revenue receipts



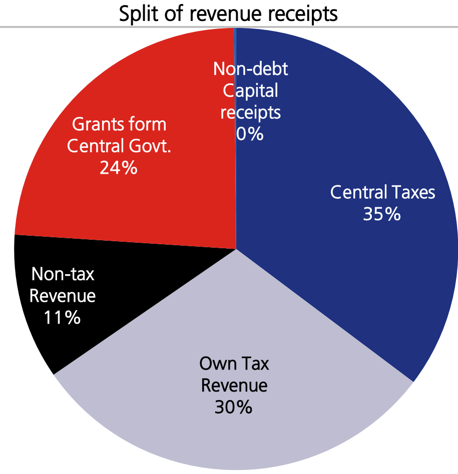
Trend of expenditure disbursements



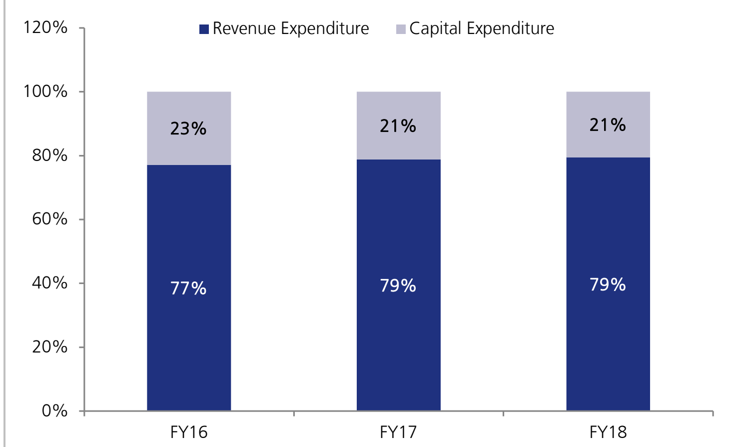
Source: Odisha State Budget, JM Financial

Exhibit 40. Odisha is dependent on the Centre for 60% of revenue receipts; Capex share stagnant at 21%

Split of revenue receipts



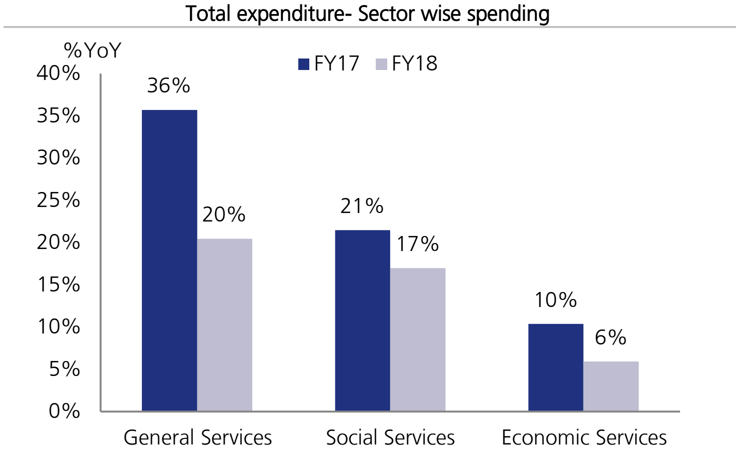
Share of Capital expenditure has not picked since FY16



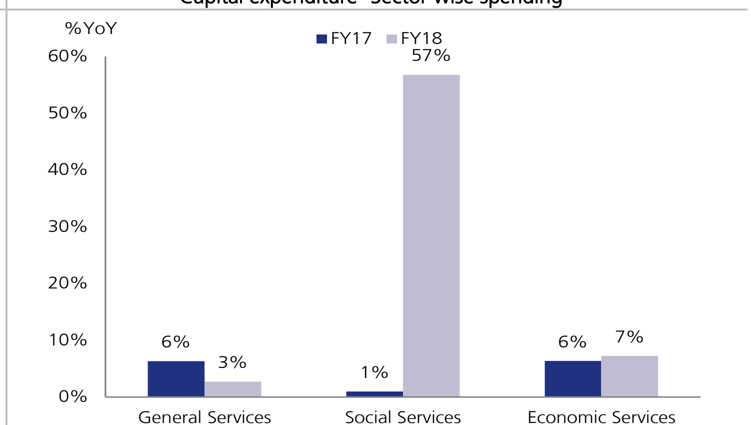
Source: Odisha State Budget, JM Financial

Exhibit 41. Increased allocation towards General services; Social Services preferred over economic services

Total expenditure- Sector wise spending



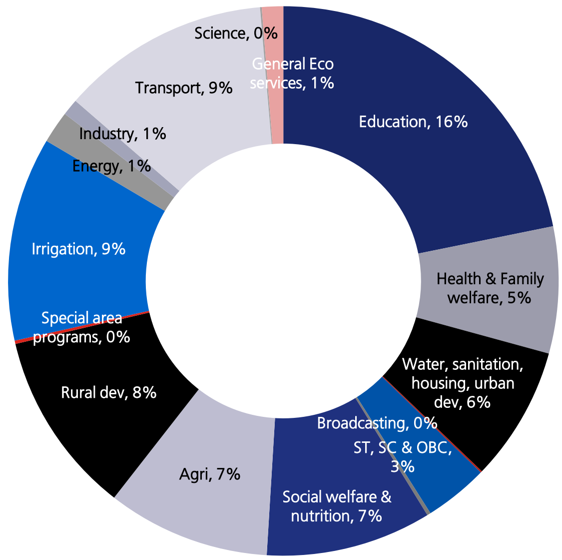
Capital expenditure- Sector wise spending



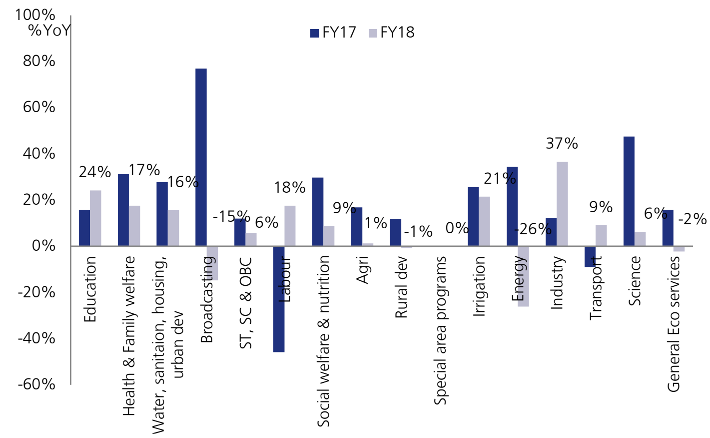
Source: Odisha State Budget, JM Financial

Exhibit 42. Education & Health & family welfare are priority spending areas for Odisha

Sub-Sector wise share in total spending



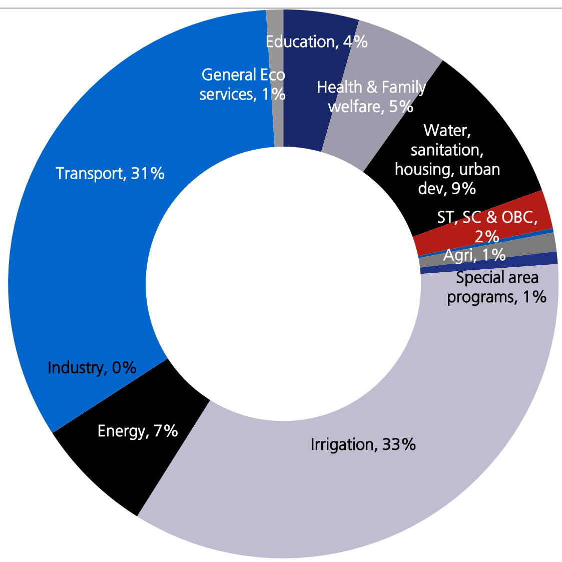
Social services such as education(24%YoY), health & family welfare (17%YoY) and urban dev(16%) pull total spending



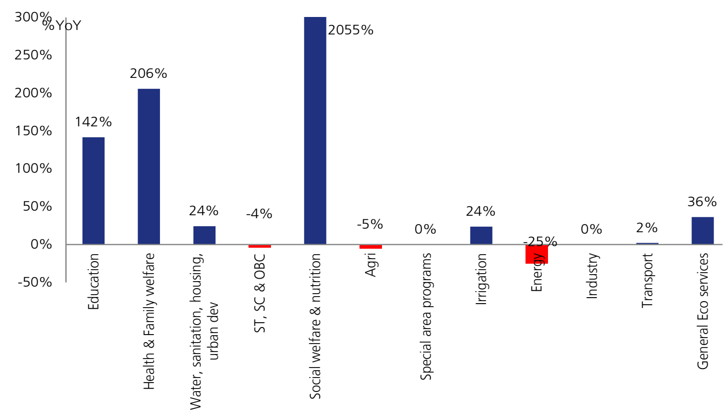
Source: Odisha State Budget, JM Financial

Exhibit 43. Social services witness capex intensification

Sub-Sector wise share in capital expenditure



Capital expenditure on education, urban dev & social welfare & nutrition hikes



Source: Odisha State Budget, JM Financial

Budget Review- Chattisgarh

With a budget of size Rs 0.76trn, Chattisgarh expects a nominal GSDP 5% than FY17RE. Its debt to GSDP ratio is estimated at 18.47% of GSDP by Mar'18 (vs 17.28% in FY17).

- Chattisgarh witnesses increase in fiscal deficit, though within FRBM limits: The fiscal deficit for the state has risen from 2.92% of GSDP in FY17RE to 3.49% in FY18, although it still adheres to the FRBM Act. On the receipts side, all sources have witnessed slower growth, owing to the high base; as a result overall revenue receipts are projected to grow by 5% (vs 36% in FY17). Own tax revenue (35% share) and Central taxes (31% share) which form major sources of revenues, are expected to grow by 3%YoY and 11% YoY respectively. A glance at the expenditure reveals capex (16%YoY) as the driver of total expenditure (8%YoY). Total spending is inclined towards general (19%YoY) and economic services (10%YoY). Within economic sector, transport (10% share) and energy (4% share), drive spending by 34%YoY and 92%YoY respectively. Water, sanitation, housing & urban development (9% share; 9%YoY) and health & family welfare (6% share; 7%YoY) receive priority in spending.

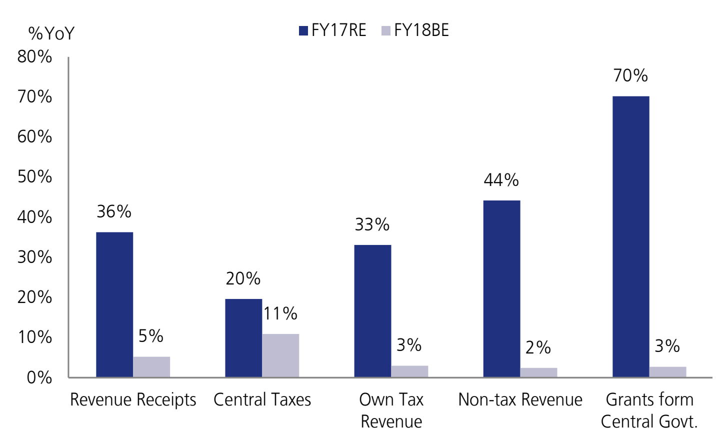
- Capex towards General and Economic services remains buoyant: Share of capital expenditure has slightly improved to 19% vs 17% in FY17. Low base has resulted in step up of capex on general services up by 80%. Although economic services are preferred in capex than social sector, most heads have witnessed a decline in allocation. However major spending heads like Transport (38% share) and Irrigation (15% share) are expected to grow by 36%YoY and 17%YoY respectively. Capex on social sectors such as education (5% share) and urban sector (9% share) is projected to rise by 11%YoY and 3%YoY respectively.

- Demonetisation and GST implementation: The government has allocated Rs2bn for providing smartphones to families under poverty line and university students. The state also announced discount of 0.5% on tax on goods (except pan masala, motor vehicles, coal, diesel, steel, cement) if payment is made using digital payments, till GST is introduced.

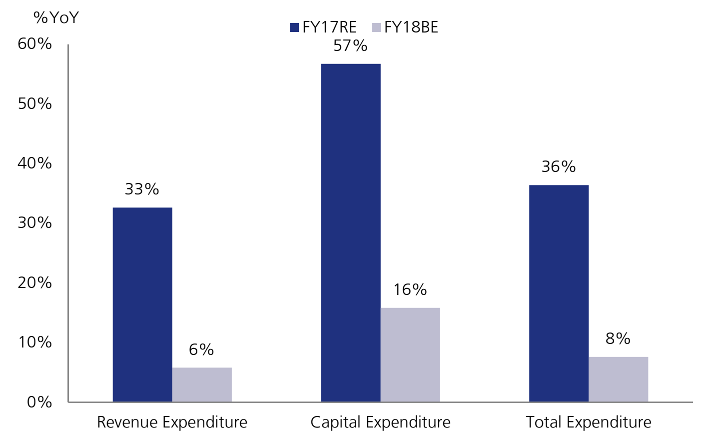
- UDAY & 7th Pay Commission: The state has signed up for UDAY scheme. The state has accounted for the cost arising from the scheme. The state was expected to announce implementation of 7th Pay Commission recommendations (after a notification by the Finance Minister in Dec'16) but hasn't mentioned anything in the budget speech. It has budgeted a 13.4%YoY increase in salaries, while pensions are expected to grow by 25%YoY.

Exhibit 44. Balanced growth in expenditure & receipts help contain fiscal deficit within FRBM limits

Trend of revenue receipts



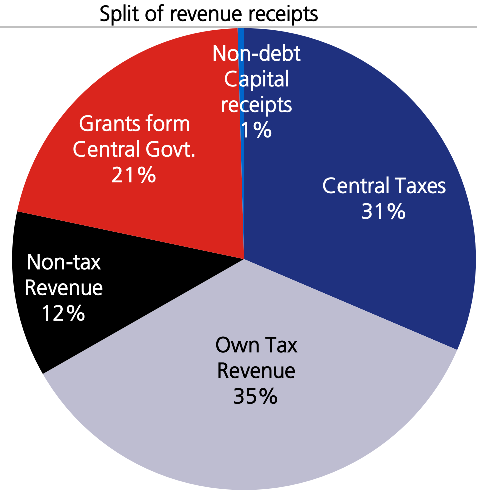
Trend of expenditure disbursements



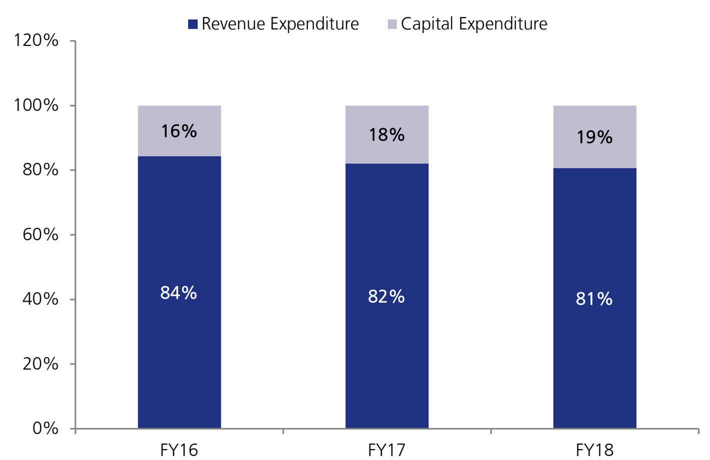
Source: Chattisgarh State Budget, JM Financial

Exhibit 45. Central taxes & Own-taxes have a major share in total receipts; Capex share rises marginally

Split of revenue receipts



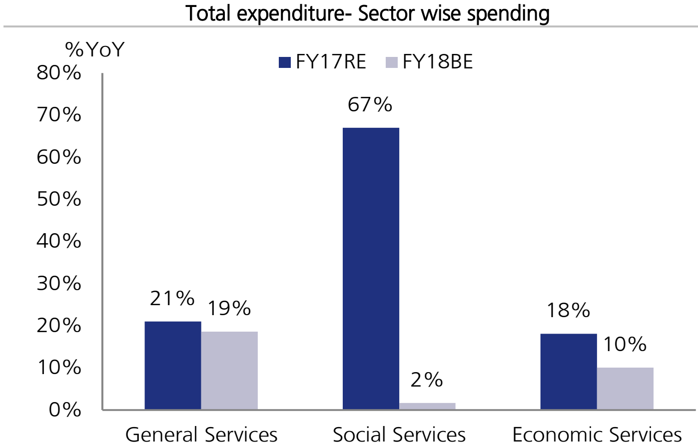
Share of Capital expenditure increases marginally to 19%



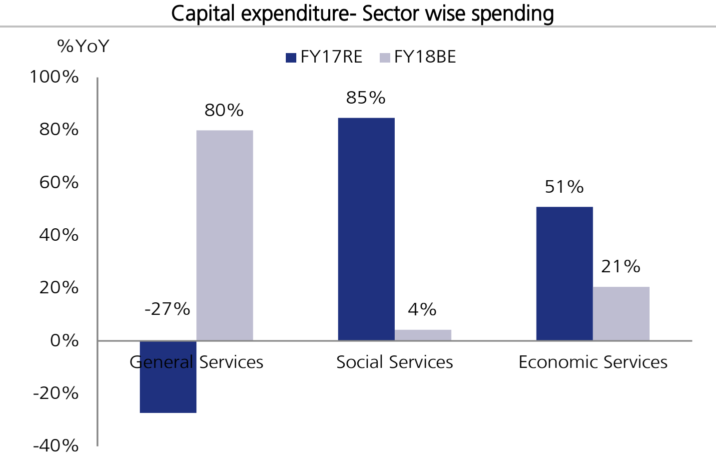
Source: Chattisgarh State Budget, JM Financial

Exhibit 46. Economic Services preferred over social services

Total expenditure- Sector wise spending



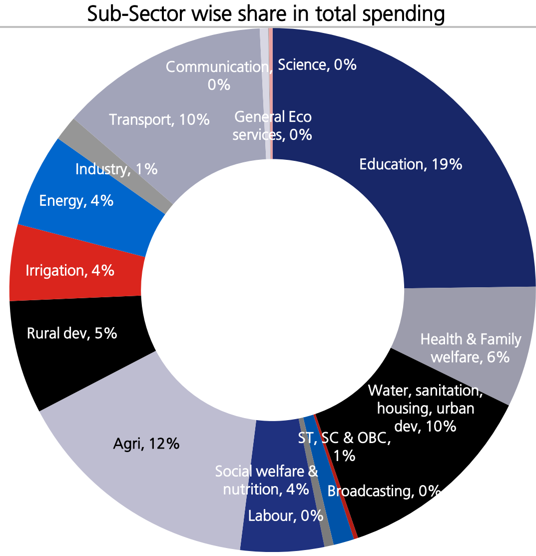
Capital expenditure- Sector wise spending



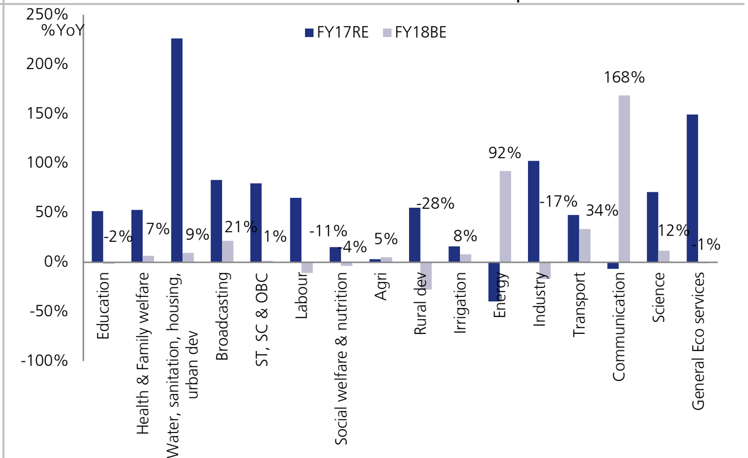
Source: Chattisgarh State Budget, JM Financial

Exhibit 47. Trends in Total Expenditure

Sub-Sector wise share in total spending



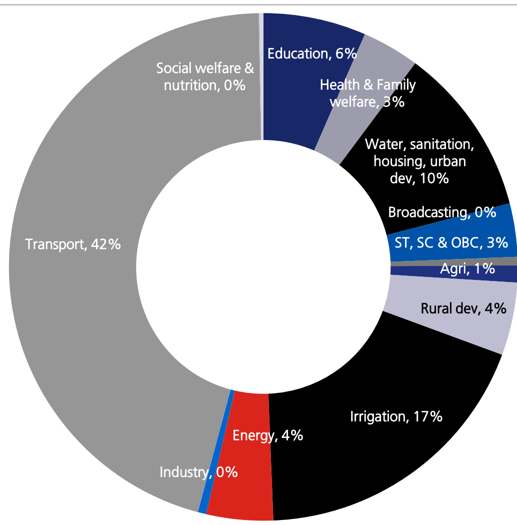
General & Economic services drive total expenditure



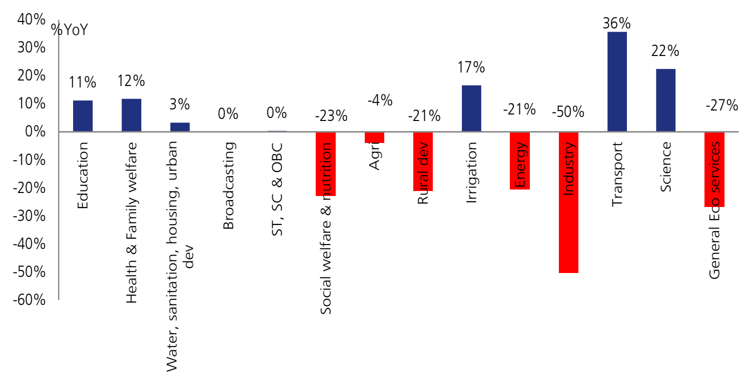
Source: Chattisgarh State Budget, JM Financial

Exhibit 48. Capital Expenditure, driven by economic services driven by transport and irrigation

Sub-Sector wise share in capital expenditure



Capital expenditure on transport (36%YoY) and Irrigation (17%) drive capex for economic services



Source: Chattisgarh State Budget, JM Financial

APPENDIX I

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SEBI Registration Nos.: BSE - INZ010012532, NSE - INZ230012536 and MSEI - INZ260012539, Research Analyst – INH000000610
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Rating	Meaning
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Hold	Price expected to move in the range of 10% downside to 15% upside from the current market price.
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