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ICRA Looks at Sectoral Development Prospects for **NDA 2.0**

NDA regime's continuity augers well for the industry

The continuity of the NDA regime post the General elections augers well for the economy and the key sectors. With political stability assured for the next five years, the general view is positive on growth and; signals better days ahead. However there are some key concerns and a serious focus by the continuing dispensation will be needed. We take a look at how the re-elected NDA regime can actually give momentum to the macro-economic growth and the key sectors by continuing with its focus and support initiatives.

The macro fundamentals of the Indian economy have taken an unfavourable dip in terms of slowdown in GDP growth rate, moderation in consumption, liquidity tightness and contraction in agricultural and industrial output. This apart, unemployment rate is at a 45 year high. Therefore revival of economic growth will be of utmost priority for the new government. With the focus also being on fiscal consolidation, how revival will be done, remains to be seen. The other factors which may play spoil sport are inflation and worsened trade deficit, crude price volatility which can disturb the long-term dynamics of India's current account deficit. Amidst all these the government will have to boost infrastructure investment and private consumption, while maintaining fiscal discipline.

The following paragraphs highlight the sectoral concerns in the Indian economy.

The **port sector** will certainly benefit from the new NDA regime and will be credit positive. Sustainability of major initiatives can be expected – such as Sagar Mala, reforms on the tariff side for Major Ports, new model concession agreement (MCA) and several trade facilitation measures such as "Direct Port Delivery" model and simplification of customs procedures, which have benefitted the sector participants. Adequate budgetary support and finalization of some of the long pending bills though will be critical for growth.

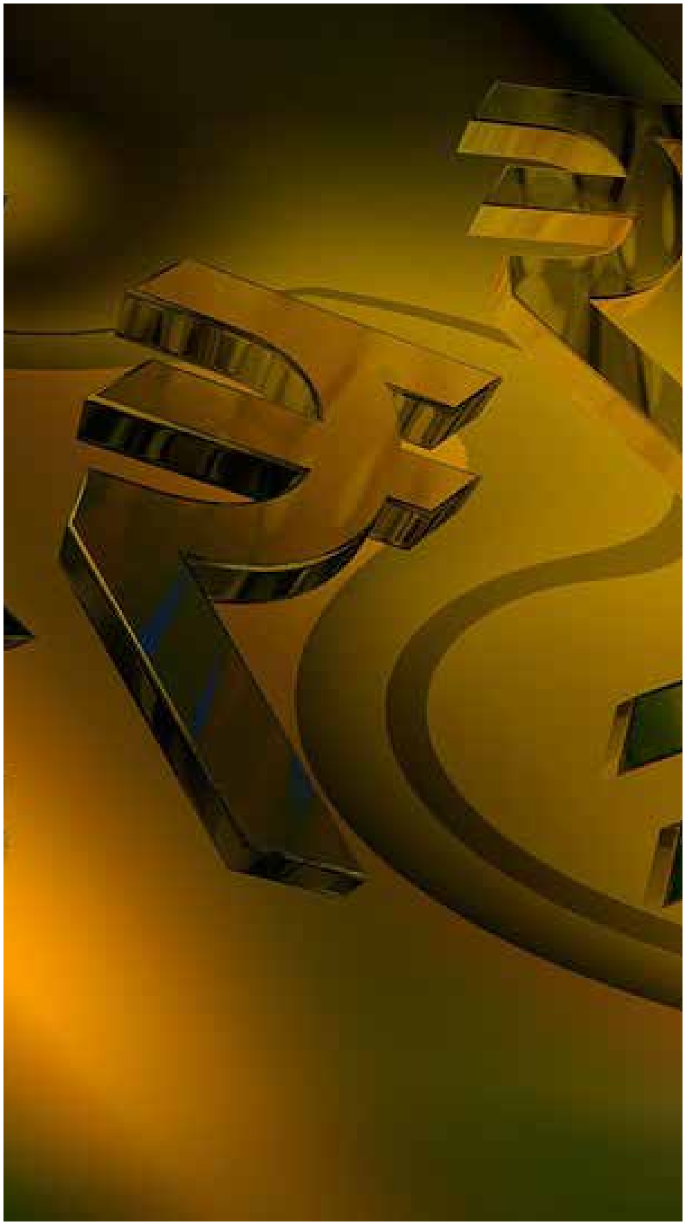
Another sector that needs attention is the **fertiliser sector** as it is grappling with severe liquidity crisis, due to delayed subsidy payments, consequently higher working capital borrowings and slim bottomlines. Poor collections have further aggravated the situation. Therefore rapid clearance of subsidy payments will be a key thing for the sector's profitability and credit matrix.

For the **oil and gas sector**, ND's re-election will be credit neutral. The credit profiles of the oil & gas companies are getting strained. Therefore initiatives such as reinvigorating the exploration & production sector, deeper penetration of natural gas through aggressive roll out of CGD infrastructure in new cities and new LPG connections, which should help the companies in the sector going forward. However, adequate subsidy provision and clarity on pricing freedom on sensitive products too will be critical.

With the return of the NDA government, **Infrastructure** push is expected to continue which will benefit industry players. Over the last five years, there has been massive push towards infrastructure projects -viz. Bharatmala, Sagarmala, Inland waterways, Housing for all, AMRUT, Smart Cities, Metro Rails and Railways. With the continuity in the Government, the total budgetary allocation is estimated to grow. Besides, the earlier government has taken several steps towards de-bottlenecking execution impediments which will need to be continued.

With large scale capital infusion of Rs 2.46 lakh crore in **public sector banks (PSBs)** during previous NDA regime and strengthening of balance sheets, PSBs should be relatively better placed in the current NDA regime to support the credit demand of the economy. Resolution of stressed assets remained slow and needs to be fastened to put the capital for better use, while the financial sector bankruptcy laws needs to be enacted. The government has also indicated the need for consolidation of PSBs and we look forward for early identification of such merging entities.

The re-election of the NDA augers well for the **renewable energy sector** as the Central government is expected to continue the policy focus on augmentation of RE based capacities, mainly wind and solar. However, improvement in the transmission infrastructure will remain critical. The project awards by the central nodal agencies and state distribution is expected to increase the share of RE in the all India generation to about 10% by FY2020, as per ICRA's estimate. However, serious efforts are required by the utilities towards improving the operating efficiencies and this coupled with timely subsidy support, tariff revisions remain extremely critical going forward.



Growth revival to be primary task of the re-elected regime

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The macro fundamentals of the Indian economy have taken an unfavourable turn, with various concerns coming to the fore in the past few quarters. The pace of growth of GDP fell to a 20-quarter low 5.8% in Q4 FY2019 from 6.6% in Q3 FY2018, led by a moderation in the expansion of private final consumption expenditure (PFCE; to +7.2% from +8.1%), as well as a sharp fall in the growth of gross fixed capital formation (GFCF); growth in GFCF fell to a modest 3.6% in Q4 FY2019, which may partly have been on account of deferral of investment decisions prior to the elections. The moderation in consumption growth, which has been one of the key drivers of the Indian economy in the recent years, reflects a combination of weak rural sentiment and the liquidity tightness related to the recent concerns related to NBFCs. The growth in GVA at basic prices also eased to a 20-quarter low 5.7% in Q4 FY2019 from 6.3% in Q3 FY2018, reflecting the contraction in agriculture, forestry & fishing (to -0.1% from +2.8%), and a slowdown in industry (to +4.2%

from +7.0%). In annual terms, GDP and GVA growth fell to five-year low 6.8% and 6.6%, respectively, in FY2019 from 7.2% and 6.9%, respectively, in FY2018. The unemployment rate at the All-India level rose considerably to a 45-year high of 6.1% in FY2018, as per the latest round of the Periodic Labour Force Survey, released in May 2019. Therefore, reviving economic growth, both through addressing rural concerns as well as boosting job creation, is likely to be a key feature of the economic agenda for the new government.

While healthy growth in government expenditure had boosted economic expansion in the recent years, this is unlikely to sustain going forward, given that the government is likely to focus on fiscal consolidation. The GoI's fiscal deficit eased mildly to 3.39% of GDP, as per the provisional numbers released by the Controller General of Accounts from 3.5% of GDP, each in FY2017 and FY2018. However, the budget financing through extra budgetary resources has doubled from Rs. 2.7 trillion in FY2017 to Rs. 5.6 trillion in FY2019 RE. Moreover, the GoI boosted its disinvestment proceeds in FY2019 through various buybacks by PSUs, as well as the sale of its stake in certain entities to other PSUs. Going forward, the GoI may not be able to shore up its receipts using similar practices, which highlights the need for a sustainable path of fiscal consolidation for the future.

India's retail inflation eased to 3.4% in FY2019 from 3.6% in the previous fiscal. Moreover, the CPI inflation for FY2019 undershot the Monetary Policy Committee's (MPC's) medium-term inflation target of 4.0% for the second year in a row. However, a closer look at the inflation dynamics reveal an unfavourable detail. Much of the easing in CPI inflation during FY2019 was led by softening trends for food and beverages sub-index. The CPI print for food and beverages fell to a series-low 0.7% in FY2019, even as core-CPI inflation (excluding food and beverages, fuel and light, as well as petrol and diesel for vehicles) hardened to a five-year high print of 5.8%. This indicated a considerable worsening in terms-of-trade for the agricultural sector. In addition, the sharp moderation in food inflation in the just-concluded was indicative of rural distress in the economy, which needs to be addressed, going forward.

The merchandise trade deficit worsened to US$176.4 billion in FY2019 from US$162.1 billion in FY2018. Moreover, the current account deficit (CAD) during 9M FY2019, at US$51.8 billion, already exceeded the full year CAD of US$48.6 billion in FY2018. The continued volatility in crude oil prices, and the uncertainty regarding its outlook, have cast a shadow in the long-term dynamics of India's current account deficit.

The government will need to address these emerging concerns by focussing on measures that boost infrastructure investment and private consumption, while maintaining fiscal discipline. The following paragraphs highlight the sectoral concerns in the Indian economy.

New NDA regime to continue strength-ening of the PSBs

By:
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Credit rating agency ICRA expects public sector banks (PSB) s to be comfortable in the second NDA regime and better placed to not only report profits during FY2020 but also support increasing demand for credit by the various sectors of the economy.

The government support to them is likely to be sustained. The PSBs under the previous NDA regime received a large capital infusion of Rs 2.46 lakh crore which largely helped to strengthen their balance sheets. With large scale capital infusion, the PSBs have not only been able to recognise and provide for their stressed assets but also improve their capital ratios. PSBs are likely to report profitable operations during FY2020 after four consecutive years of losses, i.e. FY2016-19. As per ICRA, the GNPAs and NNPAs of PSBs is expected to decline to 8.1-8.4% and 3.5-3.6% by March 2020, as against 10.3% and 5.3-5.4%, estimated for March 2019. Further, reducing fresh slippages will imply less credit provisions.

While the banks were facing stress, during the last regime and unable to fulfil credit demand, the gap was filled by non-banking financial companies (NBFC)s which played a significant role in meeting the same. But there is a situation turnaround for NBFCs too lately. In a bid to cater to credit demand, NBFCs resorted to increased borrowings leading at higher costs due to limited funding options. This apart, increased government borrowings, inadequate incremental FDI flows and capital outflows by FIIs during last year, besides slackening deposit mobilisation also contributed to the liquidity squeeze and higher borrowing costs.

While the PSBs are now better placed to cater to credit demand, the need of the hour is to increase foreign capital flows, savings to GDP and remove impediments to ensure adequate funding and liquidity for NBFCs for last mile credit delivery. This will also lead to better consumer demand for credit and improved investor's confidence, shaken as a result of delicate credit profile of a few players.

The other important consideration that will simultaneously PSBs is the recent consolidation exercise of merging weaker banks with stronger peers. This will reduce multiple lending to the same entity and hence better control over NPAs. Consolidation is one good thing to have happened in the banking system provided the merged entity is able to capitalise on the synergies, driven by improving pan-India presence of merged banks. However, while the integration processes may take some time, credit delivery should not be impacted during the transition period. Besides strict adherence to the timelines in resolution of stressed assets under the Insolvency and Bankruptcy laws and recovery of capital will help PSBs to increase lending to better/ more productive use. Hitherto the resolution of stressed assets has remained slow and needs to be stepped-up to deploy capital for optimum use. The financial sector bankruptcy laws also need to be enacted.

Continued reliance and further penetration of digital banking, increased financial inclusion and ensuring direct benefit transfers reach the beneficiaries needs to be ensured. These were important reforms in the direction to bringing banking to the doorsteps of poorest of the poor.

Lastly, though budgetary allocation, the new regime will have to ensure availability of capital for economic growth. It will also be pertinent upon the banks not to fall again into bad debts trap.

Stable policy likely to support capacity growth in renewable energy sector following re-election of NDA Government

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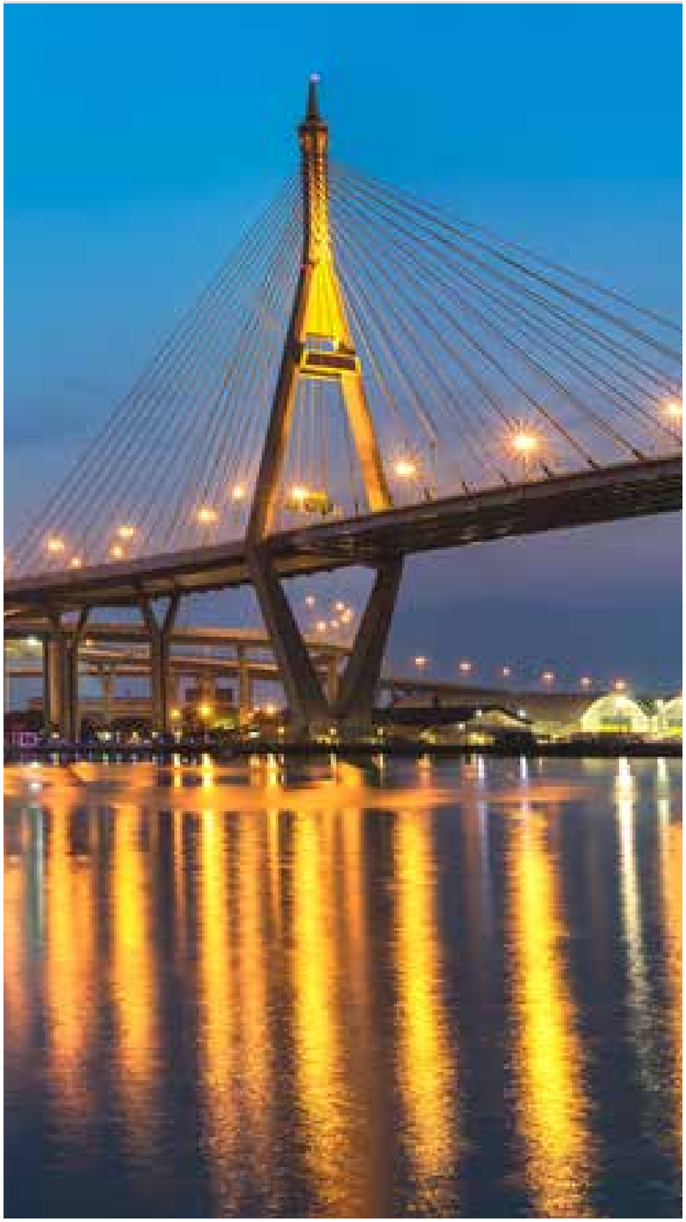
The policy support by the Central Government as well as improved cost competitiveness has increased the share of renewable energy (RE)-based capacity in the overall installed power generation capacity to 21.8% as on March 31, 2019 from 12.9% as on March 31, 2014. Similarly, the share of RE-based generation in the overall generation mix at the all India level increased to 9.2% in FY2019 from 5.6% in FY2015. With the re-election of the NDA, the Central Government is expected to continue the policy focus on augmentation of RE-based capacities, mainly wind and solar.

The re-election of the NDA Government is a positive development for the RE sector for policy stability. The support for schemes like KUSUM, roof-top and off-grid solar applications is expected to continue under the new Government, along with support for the growth of domestic manufacturing in the solar power segment. However, improvement in transmission infrastructure, especially in the inter-state network for supply of wind and solar power from high generation potential regions in the western and southern regions to other regions, will remain critical.

The project awards by the Central nodal agencies and state distribution utilities in CY2017 and CY2018 provide a reasonably healthy visibility for RE capacity addition in FY2020 with an expected addition of about 11-12 GW in FY2020. This is expected to increase the share of the RE in the all India generation to about 10% by FY2020, as per ICRA's estimate.

However, renewable IPPs, especially wind and solar energy plants, are facing challenges in terms of a mixed trend with respect to a collection pattern from state distribution utilities, with deteriorating receivable position in a few states. Serious effort is, therefore, necessary to improve the operating efficiencies and this, coupled with timely subsidy support and adequate tariff revisions by the state regulators, remains extremely critical for a sustained improvement in the financial performance, going forward.



Transport infrastructure to continue as key focus area for new Government; massive capital outlay of up to Rs. 30 trillion likely over next five years

By:
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The new Government is likely to maintain the continuity on the major programmes launched during its last tenure viz. the Bharatmala Pariyojana (Highways), Sagarmala (Ports), the railway station redevelopment programme, the inland waterways development project, Namami Gange, the Swachh Bharat Mission, UDAN (Airports), AMRUT and Smart Cities (Urban Infra) projects. Over the last five years, there has been a massive push towards infrastructure projects in roads, railways, water, irrigation and urban infrastructure. With the re-election of the Government, the total budgetary allocation towards these segments is estimated to grow.

Taking cues from the BJP manifesto, ICRA expects transport infrastructure (roads, railways, metro, airport, ports, inland waterway, etc.) to remain the main focus area for the new Government.

As per the manifesto, the next five years will see massive infrastructure build-up in India. The capital investment in the infrastructure sector has been proposed at Rs. 100 trillion over the next five years - which is a huge increase from the current level of capital investment in the sector. Amongst the key segments, transport infrastructure is expected to see a major jump with an estimated Rs. 25-30 trillion of capital outlay over the next five years. Such an investment will provide tremendous long-term benefits for the Indian economy. The construction companies are likely to be the major beneficiaries and will witness strong order inflows, estimated between Rs. 15-18 trillion on the basis of these infrastructure capex plans.

Sector	Major capex plans	Expected capital outlay over five years
Railways	DFC, railways capex, Bullet Train, station modernisation	Rs. 10-12 trillion
Roads and Highways	60,000 km over next 5 years	Rs. 7-9 trillion
Urban Infra	AMRUT, smart cities, metro/MRTS	Rs. ~3 trillion
Ports	Sagarmala	Rs. 2-3 trillion
Airport	~100 new airports	Rs. ~2 trillion
Inland Waterways	Development of national waterways, other related capex	Rs. ~1 trillion

On the road sector, the manifesto mentions constructing 60,000 km of National Highways over the next five years – at an average rate of 12,000 km per year. Given that the highway construction pace had grown significantly over the last four to five years (pace of highway construction increased from 4,410 km in FY2015, to 9,829 km in FY2018, and ~10,855 km in FY2019), with sizeable under-implementation projects, the target seems achievable.

For the railways, the manifesto has proposed a conversion of all viable rail tracks to broad gauge, electrification of all railway tracks, and completion of the two dedicated freight corridor projects (EDFC, and WDFC) by 2022. Further, a large investment is also envisaged towards railway station modernisation across the country.

Significant investment is also expected for the metro, airport, ports and inland waterways. The aim is to increase metro rail infrastructure to 50 cities from around 20 cities where the project has been approved so far. With regard to airport infrastructure, the target is to double the number of functional airports from around 101 currently. Similarly, port capacity is aimed to be doubled over the next five years and the Sagarmala project is to be fast-tracked. Development of inland waterways is another potential area.

The Government had taken several steps towards the de-bottlenecking of execution processes, thereby resulting in a substantial jump in the overall pace of execution. Such a sharp focus on execution is required to meet the ambitious targets set forth in these segments. Further, a large increase in capital investments in the infrastructure sector will require significant Government push in the form of policy reforms, including providing a conducive environment for public private partnership, and promoting alternate avenues of fund raising like Infrastructure Investment Trusts, NIIF, etc., as well as a major increase in public sector spending. Given the fiscal constraints, these can be achieved by way of asset monetisation or asset recycling.

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Oil & Gas Sector

"The re-election of the NDA will be credit neutral for the domestic oil and gas sector. Even while the credit profiles of the oil and gas companies are getting strained due to debt-funded consolidations among the PSUs, several initiatives like large dividend payouts and share buyback, and intervention into the pricing of auto fuels when crude prices were ruling high have helped reinvigorate the exploration & production sector. Deeper penetration of natural gas through aggressive rollout of the CGD infrastructure in new cities and new LPG connections should also help the companies in the sector going forward.

"However, adequate subsidy provisions and clarity on pricing freedom on sensitive products will be critical for the financial profile of the PSUs in the sector, as the crude prices have the potential to rise sharply in the near term, given the geo-political tensions in the Middle East."

Ports Sector

"The re-election of the NDA will be a credit positive for the domestic port sector, as they are expected to continue with their port-led developmental model, which will throw open several business opportunities for the incumbents. During the earlier regime, major policy initiatives were rolled out such as the Sagarmala project, reforms on the tariff side for major ports, the new model concession agreement (MCA) and several trade facilitation measures such as the Direct Port Delivery model and simplification of customs procedures, which have helped the sector participants. Going ahead, adequate budgetary support will be imperative to realise all the goals identified under the Sagarmala programme. Moreover, finalisation of some of the long-pending bills on the governing structure for major ports will be critical to realise the potential in the sector."

Fertiliser Sector

"The domestic fertiliser sector requires the urgent attention of the new NDA Government, as the industry reels under severe liquidity crisis, due to delayed subsidy payments. ICRA observes a significant rise in the working capital borrowings of the fertiliser companies over the last three to four months, due to subsidy delays and weaker collections from the retail market due to poor monsoons in some of the key agricultural states. This has strained the profitability and key credit metrics of the major players in the sector. Faster clearance of the overdue subsidy payments, through a special banking arrangement, will help the companies tide over the liquidity problem, even as they face an uncertain monsoon scenario in FY2019-20."

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