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India Union Budget 2021-22

Point of view

Aerospace and Defence

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Budget Allocations for the Defence sector

- The total Defence budget (including the defense pensions) amounts to INR 478,196 crore (~ USD 66.95 Bn).
- The budgetary allocations between capital and revenue expenditure for the defence sector stand as under:

(in INR crores)

Particulars	FY 2020-21	FY 2021-22	Percentage Change
Capital Expenditure	INR 113,734 (~USD 15.92 Bn)	INR 135,061 (~USD 18.91 Bn)	**18.75%**
Revenue Expenditure	INR 209,319 (~USD 29.3 Bn)	INR 212,028 (~USD 29.68 Bn)	**1.29%**
Defence Pension	INR 133,825 (~USD 18.74 Bn)	INR 115,850 (~USD 16.22 Bn)	**(13.43%)**
MoD (Civil)	INR 14,500 (~USD 2.03 Bn)	INR 15,257 (~USD 2.14 Bn)	**4.18%**
Total Defence Budget	**INR 471,378 (~USD 65.99 Bn)**	**INR 478,196 (~USD 66.95 Bn)**	**1.45%**

- Capital outlay on defence services as under*: *(in INR crores)*

	Allocation	% of Total Capital Outlay
Army	INR 36,482 (~USD 5.1 Bn)	27.01%
Navy	INR 33,254 (~USD 4.65 Bn)	24.62%
Airforce	INR 53,215 (~USD7.45 Bn)	39.4%
Others (Ordnance factories, R&D, Inspection, Technology development, etc.)	INR 12,110 (~USD 1.69 Bn)	8.97%
Total	**INR 135,061 (~USD 18.91 Bn)**	

**excluding allocation towards Ministry of Defence (Civil)*

- In the Revised Estimate for FY 20-21, the capital outlay for defence sector was increased to INR 134,510 crore (~USD 18.83 Bn) as compared to the budgeted estimate of INR 113,734 crore (~USD 15.92 Bn). The same was presumably owing to the result of the situation at the northern frontier. The capital outlay for this year has been pegged at INR 135,061 crore (~USD 18.91 Bn) which is in line with the revised estimate for previous year.

Key announcements for the Aerospace & Defence sector

- No change in direct tax rates proposed for corporates operating in the sector.
- Exemption for royalty income of a non-resident, on account of lease of an aircraft, paid by a unit of International Financial Services Centre (IFSC), under prescribed conditions.
- Introduction of a tax exemption on transfer of aircraft or aircraft engines by such units operating in IFSCs in specific situations.
- Next lot of airports will be monetized for operations and management concession in tier 2 and 3 towns and cities.
- Defence is classified as a strategic sector by the government with an intent to have minimum presence of the public sector enterprises in a Strategic sector.
- Rationalization of the provisions of Equalisation Levy (Digital Tax) to exclude consideration which are taxable as royalty or FTS in India. In addition clarifications provided in the definition of online sale of goods, online provision of services, and consideration received or receivable from e-commerce supply or services requiring everyone to revisit the impact of Digital Tax in India.
- Change in Basic Customs Duty rate:

Sl. No	Tariff	Commodity	Change in rate of Basic Customs Duty	
			From	To
1.0	Any chapter	Components or parts, including engines, for manufacture of aircraft or parts of such aircraft, by Public Sector Units under Ministry of Defence subject to condition specified	2.5%	0%

- Customs exemption notifications will be valid till 31st March falling immediately after 2 years from the date of such notification. In addition, 2 years will be computed from 01st February 2021, for all existing notifications.

Key policy takeaways for the Space sector

- The Department of Space (DoS) has been allocated INR 13,949 crore (~USD 1.9 Bn) in Budget 2021-22, out of which INR 8,228 crore (~USD 1.15 Bn) has been earmarked for capital expenditure. A steep hike of INR 4,449 crore (~USD 0.62 Bn) from the revised budget 2020-21, is a laudable move.
- Besides the above, in late 2020, the DoS announced the draft Spacecom Policy- 2020 to boost private participation in space activities and provides an opportunity for private companies in satellites, launches, and space-based services. With growing Government focus on space sector, it is expected from the private enterprises to leverage the opportunity of end-to end space activities on the back of strong start-up base.

Key Implications

Defence continues to be a priority area for the Government considering the situation at the Northern frontiers. Moreover, when it comes to the defence sector, Government's vision has been clear and unwavering – 'Make in India'.

Both of these sentiments are reflected in today's budget allocation for the defence sector. While the total defence budget for FY 21-22 increased marginally by 1.45% to USD 66.95 Bn, there is a significant increase of almost 19% in capital procurement outlay (i.e. USD 18.9 Bn), the enhanced capital outlay shall significantly impact future defence contracting and ensure streamlined acquisitions of key platforms like multi role fighter aircraft, light combat aircraft, unmanned aerial vehicles and future infantry combat vehicles.

The budget allocation is backed by a number of constructive policy changes brought into force in 2020. These policy reforms are

- introduction of import embargo on defence items;
- increase in automatic FDI limit in defence to 74%;
- announcement of a revamped defence offset procedure and offset guidelines;
- revised framework for micro, small and medium enterprises;
- introduction of a draft overarching vision document on Defence Production and Export Promotion (DPEPP).

The above clearly demonstrate the Government's focus on indigenous capability development.

With the ban on import, the orders of about INR 400,000 Crore (~USD 56 Bn) shall be placed with the domestic industry in the next five to seven years. Of these, the likely orders of INR 130,000 Crore (~USD 18.20 Bn) with Army and INR 140,000 Crore (~USD 19.6 Bn) with Navy and remaining with Air Force shall be pursued.

However, one expected an earmarked amount for domestic capital procurement in line with draft DPEPP. Further, with no specific direct tax holidays/ production linked incentives announced for the defence sector and no reduction in 18% GST rate on procurements, achieving Government's ambitious vision of achieving a turnover of INR 175,000 Crore (~ USD 24.5 Bn) including exports of INR 35,000 Crore (~ USD 4.9 Bn) in aerospace and defence goods and services by 2025 seems to be difficult.

Note – All figures have been converted to USD using exchange rate of 1 INR = USD 0.014 as on 01 February 2021.

KPMG in India contact

Gaurav Mehndiratta
Partner and Head
Aerospace and Defence
E: gmehndiratta@kpmg.com

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KPMG Assurance and Consulting Services LLP, Lodha Excelus, Apollo Mills Compound, NM Joshi Marg, Mahalaxmi, Mumbai - 400 011
Phone: +91 22 3989 6000, Fax: +91 22 3983 6000.