KPMG

India Union Budget 2025-26

Point of view

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Aerospace and Defence

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Budget Allocations for the Aerospace and Defence sector

- In the Union Budget 2025, INR 681,210 Crore (~USD 78.8 Bn) is allocated towards the total Defence Budget (including defence pensions) for FY 2025-26.
- The breakup of the budgetary allocations into capital and revenue expenditure, along with the comparative figures of Budget 2024 are as below:

(in INR crore)

Particulars	FY 2025-26	FY 2024-25	Percentage Change
Capital Expenditure	INR 180,000 (~USD 20.8 Bn)	INR 172,000 (~USD 19.9 Bn)	5%
Revenue Expenditure	INR 311,732 (~USD 36 Bn)	INR 282,773 (~USD 32.7 Bn)	10%
Defence Pension	INR 160,795 (~USD 18.6 Bn)	INR 141,205 (~USD 16.3 Bn)	14%
Ministry of Defence (Civil)	INR 28,683 (~USD 3.3 Bn)	INR 25,963 (~USD 3 Bn)	10%
Total Defence Budget	**INR 681,210 (~USD 78.8 Bn)**	**INR 621,941 (~USD 71.9 Bn)**	**10%**

- The overall defence allocation has increased by INR 59,269 Crore (~USD 6.85 Bn) with an increase of ~10 per cent in the overall defence budget of FY 2025-26 as compared to the original budget of FY 2024-25, while the increase when compared to revised estimate of FY 2024-25 is ~6 per cent.
- Further, the capital expenditure on Defence services is envisaged as below*:

in INR crore)

Particulars	Allocations	% of total capital outlay
Aircraft and Aero Engines	INR 48,614 (~USD 5.6 Bn)	27%
Other Equipment	INR 63,099 (~USD 7.3 Bn)	35%
Naval Fleet	INR 24,391 (~USD 2.8 Bn)	14%
Construction Works	INR 11,452 (~USD 1.3 Bn)	6%
Technology Development	INR 2,037 (~USD 0.24 Bn)	1%
Others (Land, Naval Dockyards, Special Projects etc.)	INR 30,407 (~USD 3.5 Bn)	17%
Portion of total expenditure covered	**INR 180,000 (~USD 20.8 Bn)**	

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

Key announcements for the sector

Direct Taxes

- New Income-tax bill is expected to be introduced next week. The same is envisaged to be clear and direct in text with close to half of the present law, in terms of both chapters and words
- It is proposed to exclude transactions/activities undertaken by non-resident confined to purchase of goods from India for purpose of export from purview of Significant Economic Presence ('SEP')
- Introduction of new presumptive taxation regime for non-residents engaged in provision of services or technology in India to a resident company engaged in electronic manufacturing business
- Abolishment of collection of tax at source ('TCS') at rate of 0.1 per cent, on sale of goods
- Restriction on the carry forward of losses in the hands of successor entity in case of amalgamation to 8 Assessment Year from immediately succeeding the year in which the loss as first computed for the original predecessor entity
- The sunset date for commencement of operations of IFSC units (including aircraft leasing) for tax concessions for several incomes has been proposed to be extended to 31st March 2030 from 31st March 2025
- Exemption on capital gains tax on transfer of equity shares of domestic companies being units of IFSC engaged in aircraft leasing proposed to be extended to capital gains tax on transfer of equity shares of domestic companies being units of IFSC, engaged in ship leasing.

Indirect Taxes

Customs tariff related changes

- Rationalisation of customs tariff structure and reduction of 7 rate slabs to 2 – effective rate maintained approximately at par with the existing rates
- Time limit extended till 31 March 2035 in respect of concessional rates on specified ships/ vessels and on raw materials, components, consumables or parts, for use in the manufacture of ships/vessels
- BCD exemption allowed on import of ground installations for satellites and payloads, spares and consumables of such installations
- Nil BCD (currently 5 per cent) allowed on import of goods used in the building of launch vehicles and launching of satellites.

Customs law related changes

- Two-year timeline introduced for finalization of provisional assessments (extendable further by one year). Deadline to start from the Finance Bill's assent date for pending cases
- Amendment to permit voluntary revision of import/export entries within specified timeframe and under certain conditions
- Trade facilitation for goods imported under IGCR[1] – extension in timeline for fulfilling end use of imported goods from 6 months to 1 year, provision for filing quarterly statement instead of monthly statement.

GST law related changes

- Input tax credit ('ITC') provisions amended retrospectively w.e.f. 1 July 2017 to replace the phrase 'plant or machinery' with 'plant and machinery' to remove ambiguity in interpretation for availment of ITC
- Clarification on conditions regarding reduction of tax liability on issuance of credit notes - explicit requirement for reversal of ITC by recipient corresponding to tax portion of credit note
- Supply of goods warehoused in SEZ/ FTWZ to any person before clearance for exports or to DTA to be treated as neither supply of goods nor as supply of services.

Key takeaways for the Space sector

- Overall, an under-utilisation of capital outlay by 15 per cent is observed for FY 2024-25. However, to continue the impetus for growing the space economy in line with the decadal vision for the sector, the Department of Space (DoS) has received a capital budget of INR 6,103 crore (~USD 0.7 Bn) in budget 2025 with a year-on-year (y-o-y) increase of about 10 per cent, which is also an increase of about 30 per cent over the revised estimates
- As part of India's Space Vision 2047, the Union Cabinet has approved four key projects: the Gaganyaan follow-on mission; the Chandrayaan-4 Lunar Sample Return Mission; the Venus Orbiter Mission
- The Union Budget for 2025-26 presents a progressive outlook for India's space industry, allocating funds to advance space exploration, satellite advancements, and geospatial proficiency.

Key Implications for the Defence sector

The last year 2024-25 being an election year saw under-utilization of the capital budget and an overall increase in revised estimates only on account of increase in revenue expenditure and defence pensions. Even in the current budget, the allocations are a mixed bag with certain hits and misses. The same has been broadly outlined below:

- Research and development (R&D)
  - The capital budget allocation for R&D and technology development for FY 2025-26 emphasizes the government's continued impetus towards the strengthening of R&D efforts. It also promises a push towards funding of prototype developments, indigenisation efforts and domestic defence design work. It is expected to boost the domestic defence research capabilities, as indicated in the analysis below:
    - Capital budget allocation for R&D has been increased from INR 13,208 crore (~USD 1.53 Bn) to INR 14,923 crore (~USD 1.73 Bn), an increase of ~ 13 per cent y-o-y and an increase of ~9 per cent over the revised estimates of INR 13,667 (~USD 1.58 Bn) crore for FY 2024-25
    - Make category projects of the Indian Army have received a substantial y-o-y increase in the capital budget allocation of about 235 per cent to INR 335 (~USD 0.04 Bn) crore from INR 100 crore (~USD 0.01 Bn)
    - Similarly, make category projects of the Indian Air force have received an allocation of INR 1,702 crore (~USD 0.2 Bn), an increase of about 351 per cent over the revised estimates.

1. Import of Goods at Concessional Rate of Duty for Manufacture of Excisable Goods Rules, 2017

- Capital outlay for armed forces
  - The revised estimates of INR 159,500 crore (~USD 18.4 Bn) for FY 2024-25 indicate pervasive under-utilisation of the capital outlay wherein 7 per cent (i.e. INR 12,500 crore (~USD 1.45 Bn) of the overall capital budget of INR 172,000 crore (~USD 19.88 Bn) for FY 2024-25 remains unutilised
  - The budget of INR 2,329 crore (~USD 0.27 Bn) for FY 2024-25 for land platforms remains under-utilised at 36 per cent, as indicated by the revised estimates. The budgetary allocation for FY 2025-26 of INR 1,021 crore (~USD 0.12 Bn) has seen an increase of 21 per cent over the revised estimates, which is unlikely to address the expected modernization needs
  - The aircraft and aero engines head has received an allocation of 27 per cent of the overall capital budget, with a 21 per cent y-o-y increase from INR 40,278 crore (~USD 4.66 Bn) to INR 48,614 crore (~USD 5.62 Bn). However, it's a moderate increase of ~4 per cent over the revised estimates. This is likely to be in view of the ongoing procurement of HAL Tejas fighter aircraft, C-295 transport aircraft and the multiple helicopter platforms such as Army's AH 64 Apache and Prachand attack helicopters
  - The allocation for rolling stock has increased from INR 200 crore (~USD 0.02 Bn) to INR 500 crore (~USD 0.06 Bn), an increase of ~150 per cent, indicating creation of infrastructure towards establishing of a Theatre Command
  - The allocation for Naval Fleet has remained almost stagnant with just minimal increase of 2 per cent to INR 24,391 crore (~USD 2.8 Bn) over the budget estimate of 2024-25.
- Revenue outlay of armed forces
  - The budgetary allocation for Agnipath Scheme across the forces for FY 2025-26 of INR 11,040 crore (~USD 1.28 Bn) sees a substantial increase of INR 5,060 cores (~USD 0.58 Bn) i.e. about 85 per cent as compared to current year's budget and 48 per cent over the revised estimates of FY 2024-25, highlighting the broadening importance of the scheme within the armed forces.
- Government's focus on the sector can be witnessed from the 50 per cent increase in Indian defence production from FY 21 to FY 24; a 31-fold increase in exports over the past decade and in a first of its kind announcement of 2025 as the 'Year of reforms' in defence. In this backdrop, the industry expected higher capital budget allocation. Further, as a recommendation, future budgets should consider the 15 per cent concessional corporate tax rate for defence sector (including MRO) and offer tax holiday for defence manufacturing operations, which could act as necessary fuel for the sector. The industry would now look forward to active interactions with the government for the upcoming Defence Acquisition Procedure (DAP) 2025.

Note – All figures have been converted to USD using the exchange rate of USD 1 = INR 86.5 as in Feb 2025

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