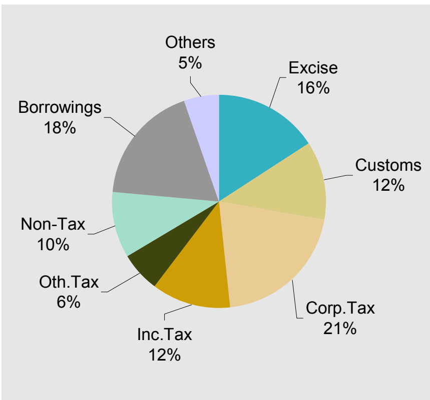
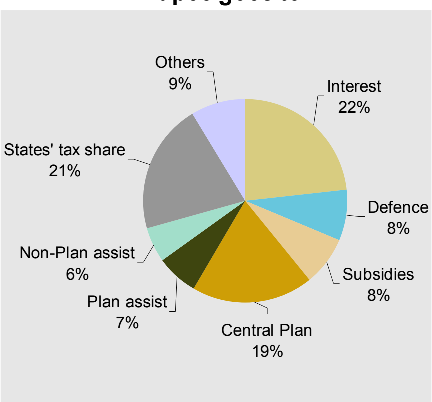
ANANDRATHI **BUDGET**

Union Budget 2007-08 — *A Neutral Budget*

Rupee comes from

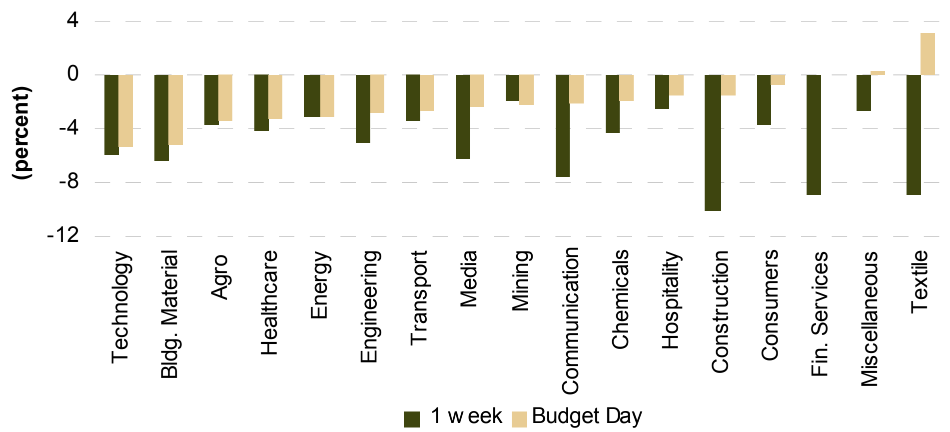


Rupee goes to



- Fiscal deficit is down to 3.7% (FY07RE) and is further expected to improve to 3.3% (FY08BE)
- Fiscal improvement a reflection on growth rather than management
- Inflation is becoming a cause of concern. Budget may not bring it down and we don't believe it is the tool to address it
- Emphasis on social sector, agriculture and sustainable growth
- Growth targets being broad based and equitable
- The budget has left major items untouched, and has not addressed major policy issues
- Overall a neutral budget

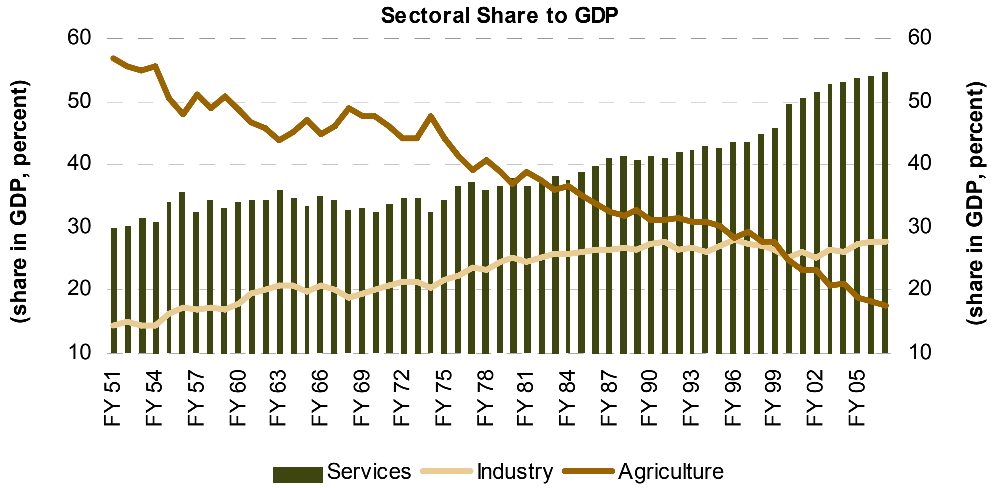
Price performance



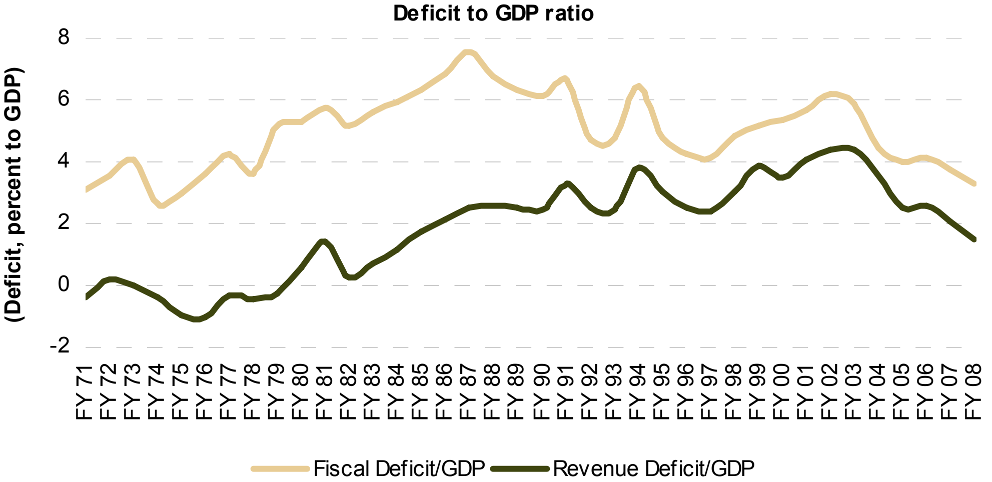
	(Rs. billion)	FY 06 Actuals	FY 07 BE	FY 07 RE	FY 08 BE	FY08/FY07RE % change
1	**Revenue Receipts (2+3)**	**3,475**	**4,035**	**4,233**	**4,864**	**14.9**
2	Tax Revenue (net)	2,703	3,272	3,460	4,039	16.7
3	Non-tax revenue	772	763	774	826	6.7
4	**Capital Receipts (5+6+7)**	**1,587**	**1,605**	**1,583**	**1,541**	**(2.7)**
5	Recoveries of Loans	106	80	55	15	(72.5)
6	Other receipts*	16	38	5	17	212.7
7	Borrowings & other liabilities	1,464	1,487	1,523	1,509	(0.9)
8	**Total receipts (1+4)**	**5,061**	**5,640**	**5,816**	**6,405**	**10.1**
9	**Non-Plan Expenditure (10+12)**	**3,655**	**3,913**	**4,089**	**4,354**	**6.5**
10	On revenue account	3,279	3,444	3,622	3,835	5.9
11	of which interest payments	1,326	1,398	1,462	1,590	8.8
12	On capital account*	376	468	467	519	11.0
13	**Plan Expenditure (8+9)**	**1,406**	**1,727**	**1,727**	**2,051**	**18.7**
14	On revenue account	1,119	1,438	1,446	1,744	20.6
15	On capital account	288	290	281	307	9.2
16	**Total Expenditure (9+13)**	**5,061**	**5,640**	**5,816**	**6,405**	**10.1**
17	Revenue expenditure	4,398	4,882	5,068	5,579	10.1
18	Capital expenditure*	664	758	749	826	10.4
19	**Revenue Deficit (17 -1)**	**923**	**847**	**834**	**715**	**(14.3)**
	As % of GDP	2.6	2.1	2	1.5	
20	**Fiscal Deficit (16-(1+5+6)**	**1,464**	**1,487**	**1,523**	**1,509**	**(0.9)**
	As % of GDP	4.1	3.8	3.7	3.3	
21	**Primary Deficit (20-11)**	**138**	**89**	**61**	**(80)**	**surplus**
	As % of GDP	0.4	0.2	0.1	-0.2	

** Exclude revenue neutral transaction on account of transfer of SBI ownership from RBI to Government for FY 08BE*

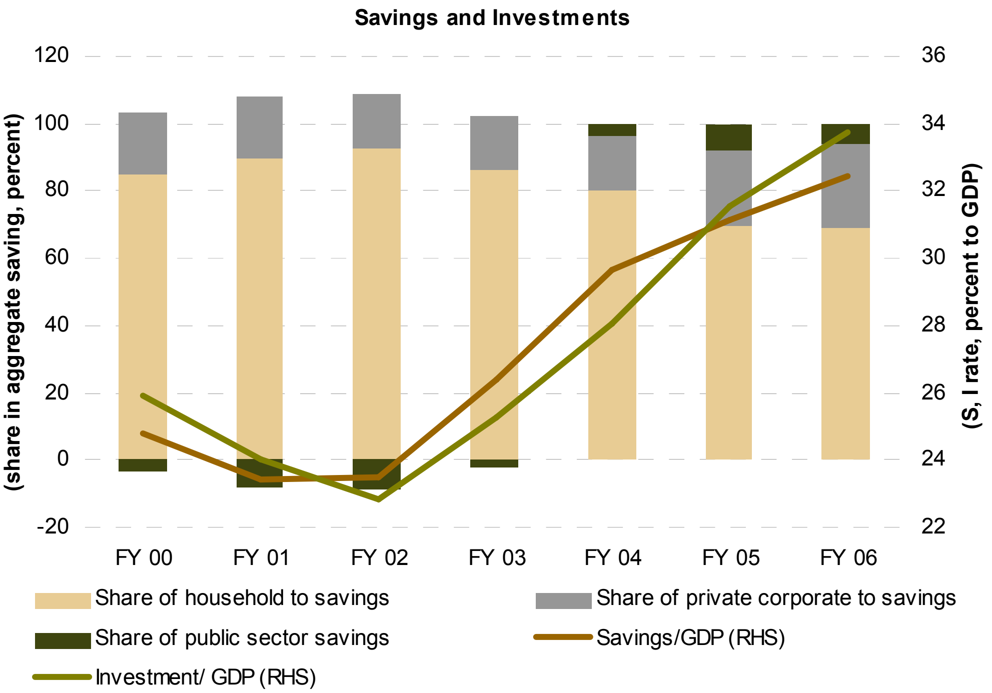
Services leading the growth process and industry has joined the party



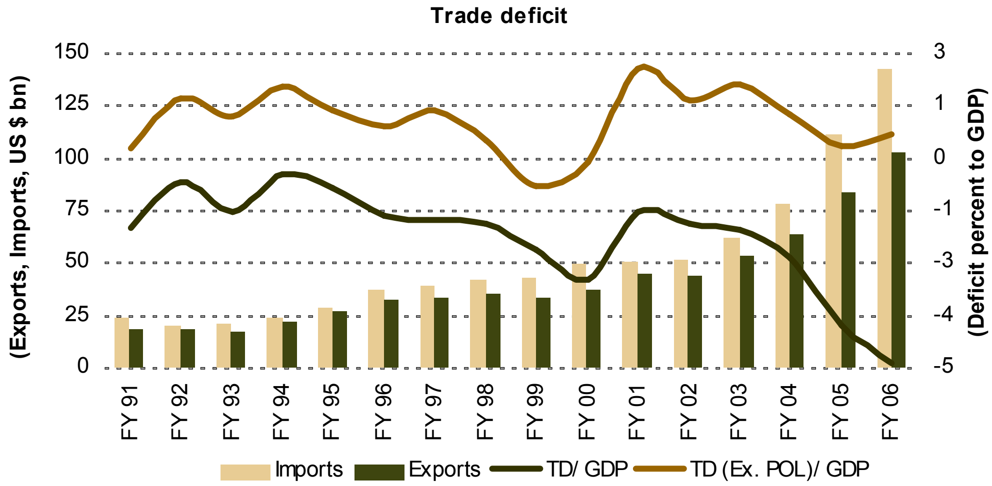
Government is ahead of FRBM in deficit control



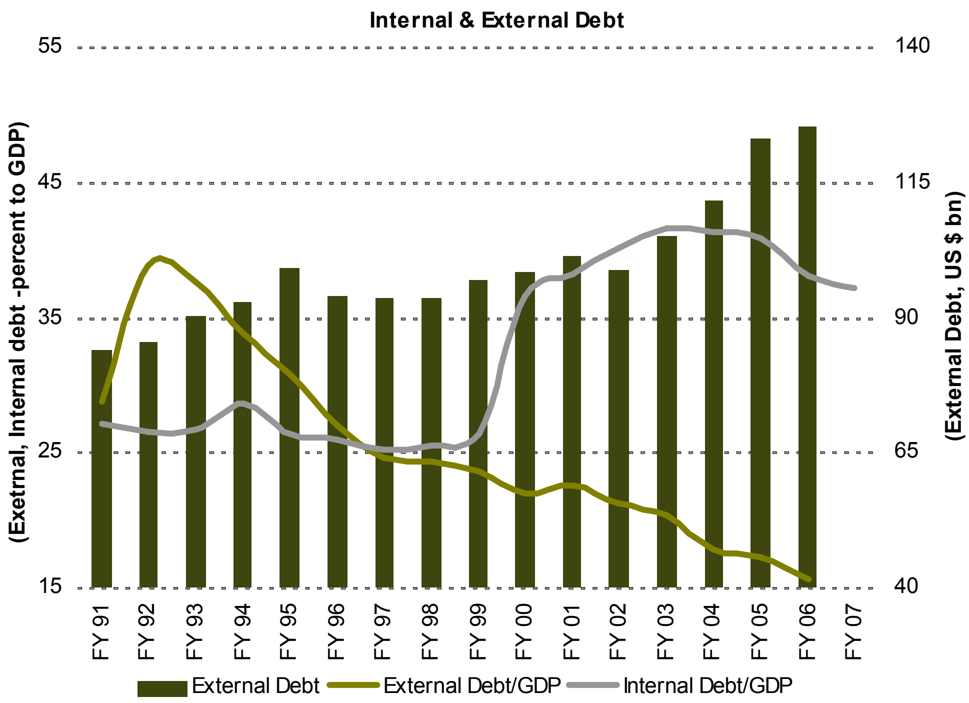
High saving-investment rates are main signs of India's take-off



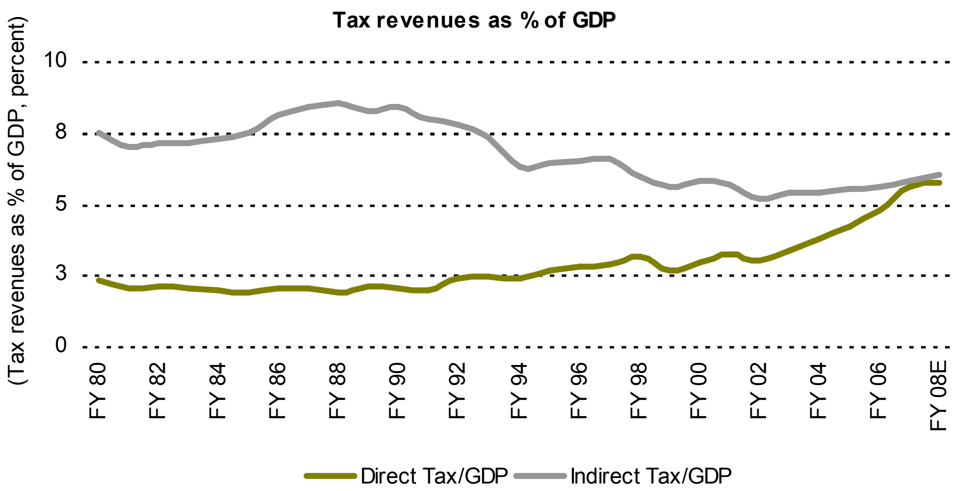
Trade deficit on account of oil and with sustainable limits



Both external and internal debt to GDP ratios are on decline



Both direct and indirect tax-GDP ratio on the rise



Budget 2007-08 - An Overview

The budget for 2007-08 is overall **Neutral** from equity market perspective. Overall it warrants a tag of being a "Non-Event". Last year we had argued that an event like "Budget" should be a non-event from an investment decision perspective. To repeat it once again, budgets are a platform to impart broad directions and review past actions. This year again we feel positively inclined to see it becoming more of a Non-Event.

Our **economy** is growing at more than 9%, which is the prime reason for overall improvement in fiscal performance. While the growth is good, it is not supported from agriculture sector (growth is just 2.7%). This segment is also contributing the maximum to inflation. In this budget, some long term measures to improve farm productivity have been announced. Revenue collections have grown by 22%, yet the fiscal deficit in absolute has gone up instead of declining. Moreover, the deficit is on account of revenue expenditure rather than capital expenditure. Thus our comfort from fiscal improvement is lacking. The visual appeal in improvement is a credit to economic boom rather than prudent management.

Future estimates indicate that the fiscal deficit is likely to improve from 3.7% (revised estimate for FY07) to 3.3% in FY08 (budgeted estimate). It is our opinion that the numbers for FY07 are conservative. We believe that the fiscal deficit for FY07 could well be around 3.5%. The implicit growth of economy in the official estimates is about 13% (8% real growth and 5% inflation). On future estimates we believe that the collections would surpass the estimates by at least Rs45 bn. On growth front we believe that the economy would grow by 12% (8.5% real growth and 3.5% inflation), hence the fiscal deficit is more likely to be around 3.1%.

Inflation at current levels of 6.6% has created a fear. Importantly inflation in primary articles is at 11.5%. This budget did not address inflation directly nor did the customary speech indicate any intention to be targeting inflation. The market was expecting some moves in this direction. We feel that this is a very positive step as any fiscal measures to control inflation are counter productive. Some cursory measures in the form of reduction in tariffs for key items like oil seeds, chemicals and plastic have been taken. Dual excise duty structure linked to cement prices indicates that the government is trying to control cement prices. However, our analysis indicates that this move will result in cement price hikes (which may well exceed the hike in duty), thereby creating further pressure on inflation.

Thematic focus of the budget has been on growth - sustainable, high and equitable. This is to be balanced with moderate inflation and fiscal prudence. In our opinion this is just a statement of the budget as no concrete action plan is visible to demonstrate any of the objectives. There were no major policy decisions / announcements. Fiscal prudence is more on account of growth rather than any concrete measures. To the credit of government, there are some encouraging announcements on social sector especially on health, education, employment and gender equality.

Best practices are being implemented by introduction of Public Debt Office. This would result in shift of debt management function from RBI to Government as is the practice followed by most other countries. In line with this thought, the government is also transferring the ownership of SBI from RBI to itself.

The correction in market is more on account of global sell-off rather than fallout from budget. In relation to the growth potential, the valuations are now looking attractive enough for long-term investments. We believe that this presents a good buying opportunities into equities especially in technology, cement and construction sector.

Budget 2007-08 - Impact analysis

Sector	Budget Impact	Research outlook
Agro-chem	Neutral	Neutral
Agro-product	Positive	Cautious
Airlines	Neutral	Cautious
Auto	Neutral	Positive
Auto Anc	Neutral	Positive
Bldg Material	Neutral	Positive
Communication	Neutral	Positive
Construction	Negative	Positive
Engineering	Neutral	Positive
Financial services	Neutral	Positive
FMCG	Positive	Neutral
Healthcare	Neutral	Positive
Hospitality	Positive	Positive
Logistics & offshore	Negative	Neutral
Metal - Ferrous	Positive	Neutral
Metal -Non ferrous	Neutral	Neutral
Oil/Gas	Neutral	Neutral
Pipes	Positive	Positive
Power	Neutral	Neutral
Shipping	Neutral	Cautious
Technology	Negative	Positive
Textile	Positive	Positive

(for price index chart (page 1)sectors are combined as: - Agro = Agro-chem+Agro-products, Transport = Airlines+Auto+Auto Anc+Shipping+Logistic, Consumers = FMCG, Engineering = Engineering+Industrial, Mining = Pipes+ Metals, Energy = Oil/Gas+Power)

Sectors like cement, technology and construction have reacted very negatively to budget on account of higher excise duty and removal of exemptions. The budget move in these sectors is negative. However, impact may not be negative or is not as much as the market believes it to be. The stock market has punished these sectors far more than the justifiable reasons. This according to us gives a good investment opportunity into these sectors.

- **Cement:** Dual excise duty structure linked to cement retail prices is a step less likely to result in price declines. Our analysis indicates that cement companies will hike prices more than enough to pass on the excised duty hike (they could well rise it more than the duty hikes as is observed in Cigarettes). Overall this means well for profitability and growth is more on account of demand factors (which remain positive). The negative reaction of stock markets to cement stocks gives a good investment opportunity.
  - Recommended buys - Gujarat Ambuja, Shree Cement and Orient Paper
- **Technology:** Introduction of MAT does not change the overall liability of the companies. The cash outflow will increase in FY08 & FY09 due to the MAT. Nevertheless, the FY09 onwards the perceived outflows will be lower due to MAT credit (Sec-10A & B were to be phased out any ways from 2009, thus effective tax rate was to go up from FY10 onwards). Thus this move is short-term negative, but long-term neutral (marginally negative).
  - Recommended buys - TCS and Polaris
- **Construction:** The dark clouds created by taxation issues in this sector may not be as bad as being perceived. One, we expect clarifications to result in improving perceptions. Two, service tax outgo is potentially lower than the current perception of it being higher.
  - Recommended buys - L&T, IVRCL and HCC

Agro-product Positive

Segment	Companies	Impact
Seeds	Monsanto, Zuari, Syngenta.	Positive
Irrigation	Jain Irrigation, Finolex industries	Positive
Edibles	Ruchi Soya, KS oils, Gujarat Ambuja Exports	Positive
Paper	BILT, TNPL	Positive
Coffee/Spices	Tata Coffee	Positive
Bio-Diesel	Ruchi Soya, Praj Inds	Positive
Starch	Riddhi Siddhi Gluco	Neutral

Major Announcements

- An Additional 2.4 mn Hectares will be bought under Irrigation under Bharat Nirman Project, increasing the land available for cultivation
- Customs Duty on sprinklers & drip irrigation systems reduced from 7.5% to 5%
- Special thrust seems to have been given to the seeds sector, as Capital grants will be provided to seed companies. Also, Venture capital investments in seeds cos has been given the pass through status.
- Special purpose Fund for re-planting & rejuvenation of Coffee, Rubber, Spices & Coconut will be set up on the lines of Special Purpose Tea Fund (SPTF)
- Nabard will earmark Rs 18 bn to be used for Ground water recharching & small farmers would get 100% subsidy on the same, while other farmers will be given 50% subsidy
- A special weather based crop insurance scheme will help the farming community to hedge his earnings from weather vagaries & Rs 1 bn subsidy has been provided for the same
- All edible grade veg oil to be exempt from 4% additional Customs duty. Also, Customs duty on crude Sunflower oil has been reduced from 65% to 50% and on refined sunflower oil has been reduced from 75% to 60%
- Customs on DMH(Dextrose Monohydrate) reduced from 30% to 20% & Sorbitol to 7.5%
- Excise completely exempted from Biodiesel to boost domestic production

Impact

- Broad Agriculture related announcements seem aimed to throttle it into a higher growth orbit & contribute more significantly in overall economic growth.
- Focus on Seeds companies is a major positive, as they have the capacity to enhance farm yields to global standards & can be significant tool in ensuring food security under current constraints
- DMH customs reduction is unlikely to have any impact on starch industry
- Special thrust on education to benefit paper manufacturers
- Biodiesel production is expected to be boosted, thereby partly derisking the economy from crude shocks
- Special funds for Coffee, Rubber and Spices positive are likely to lead to greater yields & more productions from existing farms.
- Excise reduction on edibles is positive for solvent extracting companies

Agro-chemicals Neutral

Segment	Companies	Impact
Fertilisers	Coromandal fertilisers, Chambal Fertilisers, Zuari, DCM shreeram consolidated	Neutral

Major Announcements

- Higher agriculture focus positive for fertilisers & pesticides companies
- Newer methods of direct delivery of fertiliser subsidy to farmers are being contemplated & we seem to be slowly moving towards deregulation of the fertiliser sector
- Increasing thrust on natural gas will ease supply pressures for fertiliser manufacturers

Automobile and Auto ancillaries Neutral

Segment	Excise Duty		Import Duty	
	From	To	From	To
2-3 Wheeler	16	16	60	60
Small Cars	16	16	60	60
Large Cars	24	24	60	60
CV	16	16	12.5	10
CV - petrol based	24	24	12.5	10

Major announcements

- Farm credit of Rs 2,250 bn envisaged for 2007-08.
- Higher provision for NHDP to Rs 106.67 bn.
- Custom duty on CV has been brought down from 12.5% to 10% in line with reduction in peak custom duty.
- Custom duty cut on alloy steel from 7.5% to 5%.
- Custom duty on butyl rubber reduced from 10% to 5%.
- Five year extention of 150% weighted deduction in R&D investment.

Impact

- Higher farm credit lending is positive for tractor and farm equipment manufacturers. Positive for M&M.
- Increased highway connectivity to help in CV demand. Positive for ALL, Tata Motors.
- Excise duty for large cars (above 4 mtrs) has been kept unchanged at 24%. This is positive for small car manufacturers like Maruti and Tata Motors as price differential will be maintained.

Airlines Neutral

Company	Impact
Jet, Deccan, Spicejet	Neutral

Major Announcements

- ATF sold to all small aircraft with maximum takeoff mass of less than 40,000 kgs operated by scheduled airlines to be covered under declared goods.

Impact

- Though the ATF to smaller aircraft has been covered as declared goods is positive, we do not forsee any impact on future earnings for any of the listed airlines due their existing operating fleet and ordered aircrafts. Hence, the budget stands neutral for scheduled airline operators.

Cement — Neutral

Major announcements

Specific rates of excise duty on cement have been revised as under:

S.No.		From	To
1	Cement manufactured by mini-cement plant cleared in packaged form		
	(a) of retail sale price not exceeding Rs.190 per 50 Kg bag or per metric tonne retail sale price equivalent not exceeding Rs 3,800	Rs. 250 per tonne	Rs. 220 per tonne
	(b) of retail sale price exceeding Rs.190 per 50 Kg bag or per metric tonne retail sale price equivalent exceeding Rs 3,800	Rs. 250 per tonne	Rs. 370 per tonne
2	Cement, manufactured by other than mini-cement plant, cleared in packaged form		
	a) of retail sale price not exceeding Rs.190 per 50 Kg bag or per metric tonne retail sale price equivalent not exceeding Rs 3,800	Rs. 400 per tonne	Rs. 350 per tonne
	b) of retail sale price exceeding Rs.190 per 50 Kg bag or per metric tonne retail sale price equivalent exceeding Rs 3,800	Rs. 400 per tonne	Rs. 600 per tonne

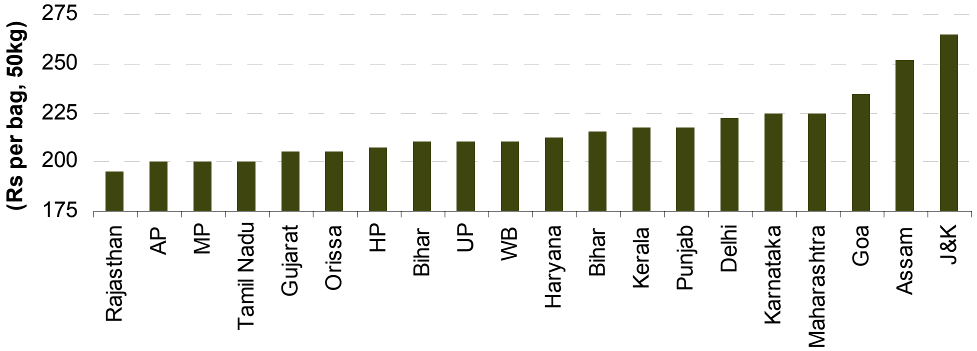
Impact

Measure intended to garner additional excise duty

The industry capacity utilisation rate for the first ten months of 2006-07 has been ~94% indicating a bargaining power in favour of the manufacturers. This is expected to continue till Q4FY08 by when additional capacity gets commissioned and eases off some supply pressures.

Retail prices in the country barring some regions in Rajasthan and Andhra Pradesh, are well over Rs 200 per bag. Cement prices have firmed up in the last one year and show no signs of slackening, backed by robust demand growth.

Average Cement prices in key states



All this indicates that the cement industry can easily pass through the proposed additional excise duty burden (Rs 10 per bag) to the end consumer. This has been corroborated by most of the cement manufacturers across India during our interaction with them. Some of the cement manufacturers across India have already planned an immediate price hike ranging from Rs 5 to Rs 12 per bag.

With an estimated demand growth of 10% CAGR over FY06-08, the domestic consumption in FY08 is expected to be ~165 mn tons. An incremental excise duty of Rs 200 per ton would result in an additional excise mop up of ~Rs 33 bn from the cement industry. Cement contributes ~2% to the basket of goods used for calculation of wholesale price index. Therefore the proposed measure is seen as a tool to mobilize additional revenues rather than a step to control inflation.

Therefore we believe that the proposed measure would not impact the profitability of the cement manufactures. On the contrary, the profitability would be boosted if the implemented price hike is more than the rise in excise duty.

Construction and Real Estate Negative

Major Announcements

- Increase in outlay for the following
  - Bharat Nirman by 31% to Rs246 bn for 2007-08
  - The Jawaharlal Nehru Rural Urbanisation Mission (JNRUM) by 8.5% to Rs49.8 bn.
  - Irrigation by 54% to Rs100 bn, aiming to cover an additional 2.4 mn hectares under irrigation.
- Corpus of Rural Infrastructure Development Fund to be raised from Rs100 bn to Rs120 bn with a special window for development of rural roads at Rs40 bn.
- Provision for National Highway Development Program to be increased from Rs99 bn to Rs106 bn.
- Public Private Partnership (PPP) and Viability Gap Funding: Revolving fund with a corpus of Rs1bn to be set up to quicken project preparation. This fund will contribute up to 75% of preparatory expenditure in the form of interest free loan to be recovered from the successful bidder
- The Memorandum-1 of the budget document says that Sec 80 I (A) benefits will no longer accrue to a company which undertakes projects on a cash contract basis. Instead it will only accrue to those companies which invest equity in the project and undertake the development work themselves. Added to this the amendment to this section is with retrospective effect from the assessment year FY01 and beyond.
- Mutual Funds to launch dedicated infrastructure funds.
- Service tax extended to the rentals from commercial properties
- Tax exemption under section 80 I (B) for home sizes upto 1,000 sq ft in Delhi and Mumbai and within 25 kms of city limits and for 1,500 sq ft for non-metros approved prior to March 2007 and to be completed within a period of four years, has not been extended
- Five year tax holiday for hotels and convention centers has been introduced. A special emphasis has been laid on the 2,3,4 star hotels and convention centers, which would be launched and commence operations from April 2007 to March 2010 in the NCR region mainly comprising of Gurgaon, Faridabad, Ghaziabad, and Gautambuddha Nagar. This is mainly on account of the Common Wealth Games to be held in 2010.

Impact

- The increase in infrastructure spending through Bharat Nirman, JNRUM, NHDP, PPP and increase in irrigation to have a positive impact on HCC, Gammon, NCC, IVRCL and Era Construction
- The non extension of the section 80 I (B) clause to be negative for real estate developers like Sobha Developers, DS Kulkarni Developers and Prajay which have been enjoying tax exemption under this section.
- Cash contracts executed by infrastructure companies since FY2000 and profits derived there under were subject to tax rates prescribed under Sec115JB. The tax paid was on the MAT rate. Companies which paid taxes on the MAT rate will now have to compute their tax liability by applying the normal corporate tax rate of 33.4% from FY01 and beyond. This will be treated as a prior period expenditure and could be adjusted as an extra ordinary expenditure or a below the line adjustment. Although the amendment in the law still does not offer clarity on the exact treatment of profits for these companies. On the face of it the announcement is a negative for all construction companies except for L&T & HCC which don't claim Sec 80-IA benefits.

- Extension of the service tax to rental income from commercial properties to be negative for real estate companies like Anant Raj Industries Ansal Properties, and Parsvnath Developers as they may not be able to pass on the increase to the end users.
- Extension of the five year tax holidays for the hotels and convention centers to be positive for Anant Raj Industries and Parsvnath Developers.

Metals - Ferrous — Positive

Impact	Company
Positive	Tata Steel, SAIL
Neutral	
Negative	Sesa Goa

Major announcements

- Customs duty on seconds and defectives of iron and steel reduced from 20% to 10%
- There will be no Customs duty on coking coal. It used to be 5% last year.
- Export duty imposed on Iron Ore at Rs 300 per MT
- Export duty imposed on chromium ores and concentrates at Rs 2,000 per MT

Impact

- **Seconds and Defectives:** Small steel manufacturers which use scrap as key raw material for production of steel are likely to be the key beneficiaries from reduction in customs duty.
- **Coking Coal:** Large layers like SAIL and Tata Steel import close to 66% and 33% respectively of their coking coal requirement. We expect the decrease in customs duty to have a positive impact on steel producers.
- **Iron Ore:** The government has imposed an export duty on iron ore. We expect this will have a negative impact on iron ore exporting company's like Sesa Goa.

Custom Duties (%)	From	To	Impact
Stainless/Alloy Steel	5	5	Neutral
Ferro Alloys	5	5	Neutral
Scrap	20	10	Positive
Coking Coal	5	0	Positive

Metals - Non Ferrous — Neutral

The custom duties on key non-ferrous metals were reduced from 7.5% to 5% in Jan 2007.

Impact	Company
Positive	
Neutral	Sterlite, Hindalco, Nalco and Hindustan Zinc
Negative	

Major Announcements

With no major announcement in the non ferrous space, we remain neutral to the sector.

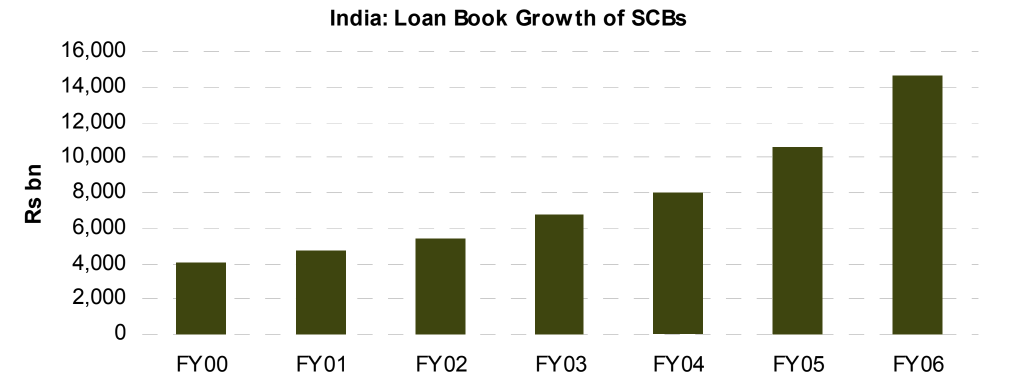
	Current Custom Duties (%)	Impact
Aluminium	5	Neutral
Calcined Alumina	5	Neutral
Copper	5	Neutral
Zinc	5	Neutral

Financial Services — Neutral

We remain neutral on the financial services sector after the pronouncements of the Annual Budget for FY08. There is increased emphasis to lend to the agriculture sector and strengthen the banking infrastructure in semi urban/ rural regions through increased presence of regional rural bank (RRBs).

Strong Macro factors key Catalyst for Credit Growth

With an average GDP growth of over 8% in the last three years (FY03-06), India remains one of the fastest growing economies globally. The strong growth momentum continues in FY07 where the growth is expected to be over 9%.The industrial and the services sector are expected to grow at 10% and 11% respectively in FY07. This is driving growth in the banking sector.



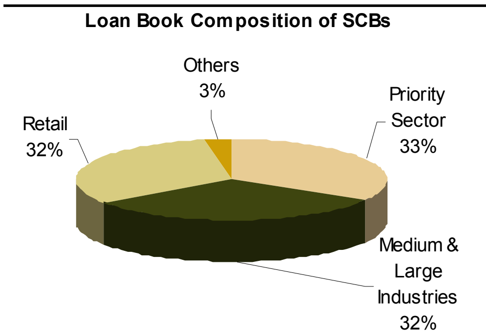
Strong Credit Growth: Key Drivers being Retail and SME sectors

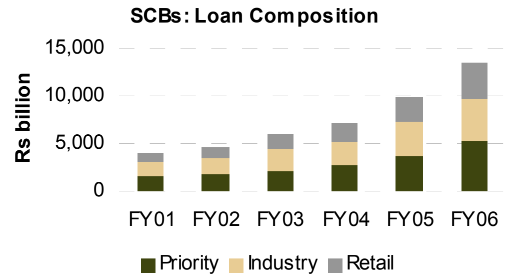
The loan book of the scheduled commercial banks (SCBs) exhibited a CAGR of 25% during FY01-FY06. The average growth rate over the last two years has been 35%. In the current fiscal, the growth until Feb 2007 has been 31% y-o-y. The strong economic growth, strong capex cycle, changing demographics, rising disposable income and lower interest rates (in the earlier years) have been the key drivers.

Rs. Billion	Feb-05	Feb-06	Feb-07	Growth (Y-o-Y)	
Non-Food Credit	10,078	13,425	17,526	33%	31%
Investments	7,120	7,240	7,576	2%	5%
Forex Reserves USD bn	133	141	189	6%	34%
PLR (%)	10.25-10.75	10.25 -10.76	11.5-12.00		
Inflation (WPI) (%)	5.3	4.0	6.7		

Loan Composition: Rising share of Retail Loans

The composition of loan book for SCBs is broadly spread over three sectors: Priority, Medium & Large Industries and Retail.





These three comprise about 97% of the gross non-food credit of the banking sector. Retail Loans have grown at a CAGR of 32% during FY01-FY06. Agricultural loans have exhibited a CAGR of 27% over the same period. Retail share has increased from 22% in FY01 to 30% in the first half of FY07.

Key Announcements

Farm Credit: Increased thrust on agriculture continues

- SCBs have been directed to increase the quantum of farm credit from Rs. 1,253 bn in FY05 to Rs.2,250 bn by FY08.
- An additional five million farmers are expected to be added as bank customers for agricultural credit in FY08.
- The Government will continue to ensure that farmers receive short-term credit at 7%, (with a two per cent interest subvention scheme to SCBs), entailing a provision of Rs.16.77 bn
- NABARD to issue Government guaranteed rural bonds to the extent of Rs.50bn for refinancing rural credit cooperatives

SME Credit: SCBs urged to fix interest rates with respect to credit rating

- SCBs have been encouraged to continue lending to SMEs, with interest rates related to the credit rating acquired by an SME

Housing Credit: New initiatives

- Reverse mortgage for senior citizens to be introduced by the National Housing Board
- Regulations to allow the creation of mortgage guarantee companies to be put in place

Regional Rural Banks (RRBs): To assist the government's rural lending objective

- RRBs have been urged to expand aggressively in the bank's quest for increasing rural and semi-urban credit, with at least one branch in the country's 80 uncovered districts
- The SARFAESI Act, relating to securitization, will be extended to RRB advances
- RRBs will be permitted to accept NRE and FCNR deposits
- Ailing RRBs, having negative net worth, will be recapitalized in a phased manner.

Cooperative banks: Tax incentives for consolidation

- Cooperative banks will be allowed tax deductions in respect of provisions for bad and doubtful debts under section 36(1)(viia)
- Tax benefits from the amalgamation and de-merger of banks will be extended to cooperative banks

Insurance: Primarily social security initiatives

- The exclusive health insurance scheme for senior citizens launched by National Insurance Company in December 2006 will also be launched by LIC, GIC and New India Assurance in FY08.
- A social security scheme for unorganised workers to cover the rural landless households which enjoy no cover, of which the Central Government will bear half of the premium of Rs.200 per year per person, and the State Governments are expected to bear the rest.

Impact

Increased focus on farm credit: Negative for Banks and positive for NBFCs with a rural / semi-urban presence

Companies to benefit: Mahindra Finance

Extension of service tax to renting of immovable property for use in commerce or business: Marginal negative impact for banks

- Banks which have rented out commercial properties for their branches will be only marginally affected by this move.
- Rental expenditure for SCBs ranges from 1% to 3% of their total expenses (including interest expended).
- After factoring in the service tax paid on rents, the incremental increase in operating expenses for SCBs (sample size of 32 banks) is 0.31%.

Rs. Mn	Rent Paid	Operating Expenses	Employee Expenses	Interest Expended	Total Expenditure	Increase in rent (Service Tax of 12.5%)	Increase in Operating Expenses
32 SCBs	32,400	119,824	260,616	875,894	1,288,735	4,050	0.31%

FMCG — Positive

Major Announcements

- Import duties on a lot of products are reduced so as to keep inflation under control.
- Dividend distribution Tax has increased from 12.5% to 15% which is a negative for FMCG sector as most of them are high dividend paying companies.
- There is increased focus on farm credit and agriculture.
- The alterations in Import and Excise Duty were as follows.

Items	Duty	From	To	Impacting Industry & Companies	Impact
Edible Oil	Additional	4.0%	0.0%	Biscuits - Britannia	Positive
	Customs Duty			Ready Food- Frito Lays	Positive
				Edible Oil Player - Marico	Negative
Titanium Dioxide	Customs Duty	12.5%	10.0%	Paint Industry Asian Paints Kansai Nerolac, Berger, ICI	Positive
Food Processing Machinery	Customs Duty	7.5%	5.0%	Agro Processing Industry	Positive
Sunflower Oil					
Crude	Customs Duty	65.0%	50.0%	Edible Oil Player- Marico	Negative
Refined	Customs Duty	75.0%	60.0%		
Packed Biscuits of MRP less than Rs 50 per Kg.	Excise Duty	8.0%	0.0%	Biscuit Companies ITC Britannia	Positive
Food Mixes	Excise Duty	8.0%	0.0%	Instant Food Companies HLL, ITC, Nestle	Positive
Boric Acid	Customs Duty	10.0%	5.0%	Antiseptic cream - Emami	Positive
Footwear Parts/ Components	Excise Duty	16.0%	8.0%	Footwear- Liberty Shoes Mirza Tanners, Bata	Positive

Tobacco Products	Duty	Rs per 1000 Present	Rs per 1000 Prposed	Impacting Industry & Companies	Impact
Non Filter Cigarettes					
Not Exceeding 60 mm in length	Excise Duty	160	168	Cigarette Industry	Positive
Exceeding 60mm but less than 70 mm	Excise Duty	520	546	ITC, Godfrey, GTC, VST	
Filter Cigarettes					
Not Exceeding 70 mm in length	Excise Duty	780	819	As cigarette industries generally increase prices more than excise increase there can be margin improment	
Exceeding 70 mm but not 75 mm	Excise Duty	1,260	1,323		
Exceeding 75 mm but not 85 mm	Excise Duty	1,675	1,759		
Other cigarettes	Excise Duty	2,060	2,163		
Cigarettes of tobacco substitutes	Excise Duty	1,150	1,208		
Bidis					
Manufactured without aid of machines	Excise Duty	12	16	Bidi Manufacturers	Negative
Manufactured with aid of machines	Excise Duty	22	29		
Pan Masala without Tobacco	Excise Duty	66.0%	45.0%	Mouth Freshners- Kothari Products	Positive

Impact

- The focus on rural economy will help the FMCG sector to increase the penetration in rural areas as the people in rural areas will enjoy higher disposable income.
- Excise duty cut will help companies like Britannia to ease the margin pressure.
- The reduction in duty on machinery and food products will help the food processing companies to grow rapidly.
- Increase in excise duty on cigarettes can be easily passed on to the end customers due to strong brand recall.

Hospitality — Positive

Company	Impact
Royal Orchid Hotels Ltd	Positive

Major announcement

- Five year tax holiday for hotels (2, 3, and 4 star category) and convention centers (seating capacity more than 3,000) coming in NCR region during April 2007 and March 2010
- Increased thrust on tourism with budget allocation to the sector increased by 18%
- Long awaited issues like- granting hotels an Infrastructure status and increase in depreciation rate (from 10% to 20%) for building- were not addressed

Impact

- Service Tax (@ 12.36%) has been extended to renting of immovable property for commercial purpose, which can prove to be marginally negative for Royal Orchid Hotels Ltd, whose all hotels are presently under lease contract

- Five year tax holiday for hotels in NCR region between April 2007 and March 2010, would benefit Royal Orchid Hotels Ltd, planning to build a 4 star property in this region in near future.
- Positive impact for the overall sector with increased thrust on tourism and infrastructure, higher budget allocation, increased provision for building tourist infrastructure (from Rs4230mn to Rs5200mn) and pass through status to venture capital fund going into the business tourism

Information Technology — Negative

Smaller and mid-sized companies to be negatively impacted due to the non-extension of STPI benefits beyond 2009

10A/10B exemption to be included for calculation of MAT

FM introduced Minimum Alternative Tax (MAT) on companies claiming 10A/10B benefit. Companies with less than 11.33% tax outgo will have to shed more cash outflow for FY08 and FY09. However, such Tax outgo must be available as a MAT credit after FY09.

Companies highlighted in the table below would have a higher impact on profitability.

Size	Company Name	Year End	Tax Rate Standalone FY06	Tax Rate TTM
Large	HCL Technologies	200606	2.4%	2.1%
	Tech Mahindra	200603	8.5%	3.5%
	TCS	200603	11.0%	7.9%
	Infosys Tech.	200603	11.1%	11.1%
	Wipro	200603	13.7%	12.2%
	Satyam Computer	200603	14.3%	10.0%
	I-Flex Solutions	200603	15.7%	9.5%
Medium	Aztecsoft	200603	0.0%	6.0%
	Aptech	200612	0.0%	0.0%
	Zensar Technolgs	200603	0.0%	0.3%
	Prithvi Info	200603	0.2%	0.5%
	NIIT Tech.	200603	0.5%	1.7%
	Hexaware	200612	1.4%	1.3%
	NIIT	200603	1.7%	0.0%
	3i Infotech	200603	2.0%	1.8%
	MphasiS Ltd	200603	2.5%	7.5%
	Geodesic Inform.	200603	5.2%	0.0%
	Nucleus Software	200603	6.0%	1.7%
	Mastek	200606	6.0%	5.9%
	Northgate Techno	200603	9.2%	3.9%
	Rolta India	200606	9.4%	10.5%
	Sonata Software	200603	9.7%	0.0%
	Infotech Enterpr	200603	16.2%	14.2%
	Polaris Software	200603	16.7%	15.5%
	Geometric Soft.	200603	19.0%	12.1%
	Cranes Software	200603	22.5%	8.5%
	Sasken Comm.Tech	200603	25.3%	13.2%
	iGate Global Sol	200603	53.3%	5.3%
Small	Allsec Tech	200603	0.0%	0.1%
	Logix Microsys.	200603	0.0%	0.0%
	Megasoft	200512	1.3%	0.9%
	Datamatics Tech.	200603	2.1%	2.0%
	Kale Consultants	200603	2.6%	4.0%
	Four Soft	200603	14.3%	6.4%

Source : capitaline

HCL Tech and Tech Mahindra would be impacted the most due to its tax rate being the lowest.

Infosys indicated that their tax rates would move from 11.3 % to 16 % and impact their net margins by 150bps.

Service tax on rented commercial properties

Service tax on rent of commercial properties will be negative for companies using rented commercial properties rent outgo to increase by 12%. There will be 10 -20 bps impact on companies where the rent ranges 1%-2% of revenue

ESOPs included under Fringe benefit tax

Fringe benefit tax on Grant of ESOPs will negatively impact the profits. Quantum of taxation has not yet been notified.

Increased allocation on Education

Increased allocation for teacher training and increased class room to positively impact education based IT companies like Educomp, NIIT Ltd and Aptech Ltd. Increased education focus to help the industry over a longer run. The budget proposed to increase the provision for strengthening teachers training institutions from Rs.1.6 bn to Rs.4.5 bn.

Increased allocation for E-Governance

Increased allocation for E-governance from Rs 3.95 bn to Rs 7.19 bn will help companies like Vankrangee Software to a large extent. The Central Government will be supporting e-governance action plans at State levels, with an increase in the allocation from Rs.3 bn in 2006-07 to Rs.5 bn in 2007-08

Increased dividend distribution tax

Increase of Dividend Distribution tax from 12.5% to 15% to negatively impact the Cash flows

Logistics & Offshore — Negative

Segment	Company	Impact
Logistics	Gateway, Aegis, AllCargo, Concor, Gati, TCI	Neutral
Offshore - Oil Drilling	Aban Offshore ltd, Shiv-Vani oil, Dolphin Offshore Enterprise ltd, Jindal Drilling, Garware Offshore Ltd and SEMAC	Negative
Offshore - Helicorp Services	Global Vectra Helicorp	Negative

Major announcements

- Service tax extended to services outsourced for oil or gas industry
- Levy of 3% import duty on all private import of aircraft including helicopters. Such import will also attract countervailing duty and additional customs duty.

Impact

- No impact on logistics segment
- Extension of service tax to oil and gas services will increase the exploration & development costs impacting the upstream companies
- It will impact the margins of the service companies

- Global Vectra Helicorp Ltd. has applied for clarification with its customs consultant in order to clear whether it is covered under the levy of import duty and service tax as per this budget.

OIL/GAS — Neutral

Segment	Company	Impact
Natural Gas	GAIL, GSPL	Positive
Exploration & Production	ONGC, Reliance, Cairn India, GSPC	Negative
Refining & Marketing	HPCL, BPCL, IOC	Neutral

Major announcements

- Infrastructure status under Section 80-IA, extended to cross country Natural Gas pipeline companies.
- Ad-valorem component of excise duty on Petrol (Motor Spirit) and High Speed Diesel (HSD) reduced from 8% to 6%.
- Customs duty on PTA MEG and DMT reduced from 10% to 7.5%
- Service tax extended to services providers in Oil & Gas exploration activities.
- Dividend disbursement tax increased from 12.5 percent to 15 percent
- Definition of specified end user for allotment of Coal Blocks extended to include Underground Coal Gasification and Liquefaction companies.

Impact

- Infrastructure status (under section 80-IA) extended to natural gas transportation pipeline companies would promote provide higher cash surplus for reinvestment and promote more investment in the segment. This would thus have a direct positive impact on companies like GAIL and GSPL.
- Reduction of the ad-valorem component of excise duty on Petrol and Diesel from 8% to 6% would be positive for oil marketing companies to the effect of reducing their under recoveries and partially compensate for the recent reduction in petrol by Rs. 2/liter and diesel prices by Rs.1/liter.
- Custom duty reduction on PTA MEG and DMT would have a neutral impact as both Reliance Ind & IPCL produce these for internal consumption.
- Extension of service tax to Oil & Gas Exploration service providers would have negative impact on ONGC, Reliance Ind and Cairn India Ltd as it would have increase exploration block development cost.
- High dividend outflow in case of PSU Oil & Gas companies would have increased outflow on account of increase dividend disbursement tax and thus reduced carried forward profits on books. This would thus have some negative impact on the future investment and growth momentum of these companies. Negative for all Oil & Gas PSU companies.

Pharmaceuticals — Neutral

Companies	Impact
Aventis Pharma, Merck, Cipla, Matrix, Aurobindo Pharma	Positive

Major announcements

- Budget allocation for healthcare and family welfare raised by 21.9% to Rs 152.9bn.
- Peak custom duty has been reduced on bulk drugs and formulations.
- Concessional rate of 5% customs duty plus Nil CVD on specified items, extended to all research institutions registered with the Department of Scientific & Industrial Research.
- Concessional rate of 5% customs duty available on specified items for pharmaceutical and biotechnology sector when imported for R&D purposes, extended to 15 additional items.
- Customs duty on medical equipment reduced from 12.5% to 7.5%.
- Weighted deduction of R&D spend extended by 5 years up to March 2012
- Budgetary allocation for the National Rural Health Mission raised from Rs.82.1 bn to Rs.99.5 bn.
- Rs 12.9bn provided for polio eradication.
- Provision for AIDS control programme stepped up to Rs 9.7bn
- Clinical research organizations exempted from service tax.

Impact

- Aventis Pharma, Merck with a relatively high level of imports stand to benefit marginally.
- Indian majors are marginally affected by the reduction in import duty on bulk drugs.

Excise duty (%)	From	To	Import duty (%)	From	To
Bulk drugs	16	16	Bulk drugs	12.5	10
Formulations	16	16	Formulations	12.5	10

Pipes — Positive

Impact	Company
Positive	PSL, Jindal SAW, Welspun Gujarat Stahl Rohren, Man Industries and Electrosteel
Neutral	Maharashtra Seamless

Major announcements

- Drinking water pipes with diameter greater then 8 inches (200 mm) would be exempted from excise duty.
- Cross country gas pipelines brought under Sec80I-A

Impact

- We believe the net impact would be negligible because the proportion of revenues derived from sale of water pipes by the pipe manufacturers is below 30% for most companies. In addition, we believe more than 50% of the resulting benefit would be passed on to their customers.
- Cross country gas pipelines being brought under the infrastructure status would increase the pace of the projects in the country, which is expected to benefit the pipe manufacturers.

Power & Engineering — Neutral

Major Announcements

- The defense budget has been increased to Rs.960 bn of which capital expenditure is Rs.419.22 bn.
- The peak customs duty has been reduced from 12.5% to 10% for all non-agricultural items.
- Seven Ultra Mega Power Projects (UMPPs) are under process of which at least two will be awarded by July, 2007. Other initiatives taken by the Ministry of Power include facilitating setting up of merchant power plants by private developers and private participation in transmission projects.
- A service tax levy of 2% on the services part of the works contract or an optional scheme under which service tax imposed will be 2% of the total value of the works contract however, this does not include works contracts related to Infrastructure projects in the area of roads, airports, railways, transport terminals, bridges, tunnels & dams.. This is in addition to the works contract tax collected by the state which is 2-4% depending on the state in which the job work is executed.

Impact

- Duty reduction will be beneficial for project imports thereby benefiting utility players like Tata Power, Reliance Energy etc.
- Increase of 21.6% in capital expenditure from Rs.344.58 bn to Rs.419.22 bn for the Defence services will have a positive impact on domestic defence equipment manufacturers like BEML, BEL, Dynamatic Technologies, L&T and Tata Power especially after the introduction of offset agreements.
- We believe that service tax levy of 2% on the services part of the works contract tax will effectively bring down the incidence of the existing service tax liability .The current computation for service tax was on the labour applied on the contract which is equal to 1/3rd the size of the contract. Hence service tax= 1/3 (contract size) *12.24%=4% which now the budget proposes to bring it down to 2% of the works contract.

Shipping — Neutral

Major announcements

- Customs duty has been reduced on dredgers from 5% to Nil.

Impact

- Reduction of custom duty on dredgers will benefit Dredging Corporation of India for capex to be made by the company

Telecom Neutral

Major Announcements

- No increase in service tax as was expected
- Levy of service tax on renting of immovable property
- Extension of exemption on additional customs duty on cell phone parts, components and accessories till 30.06.2009.
- Department of Telecommunications (DOT) has been requested to study the various levies on the telecom sector and give suitable recommendations to the government.

Impact

- Service tax on renting of immovable property will be marginally negative for the service providers who are using the premises for cell sites on lease
- Appears that the government may consider the recommendations from the DOT and maybe some relief in the form of reduced levies may be forthcoming for the sector.

Textile Positive

Company	Impact
BRFL, Gokaldas, Indorama Synthetics, Sangam India, JBF Inds, Alok	Positive
LMW, SRF	Neutral

Major Announcement

- The Technological Upgradation Fund (TUF) scheme has been extended by another 5 years, till 2012. The provisioning of funds under the TUF has been increased from Rs 5.35 bn in FY07 to Rs 9.11 bn in FY08
- Allocation on account of Scheme for Integrated Textile Parks (SITP) has been increased from Rs1.89 in FY07 to Rs 4.25 bn in FY08
- Custom duty on polyester staple fibers and polyester filament yarn has been reduced from 10% to 7.5%
- Custom duty on polyester chips, DMT,PTA and MEG has been reduced from 10% to 7.5%
- Excise duty has been reduced on caprolactum and nylon chips from 16% to 12%
- Excise duty has been reduced on benzene for manufacturer of caprolactum from 16% to 12%
- Optional excise duty at 12% has been specified on fishnet grade nylon yarns, fishnet fabrics, fishnet twine and fishnets
- Full exemption from excise duty on specified textile machinery has been withdrawn and an excise duty of 8% gas been imposed thereon
- Ad valorem component of custom duty on textile fabrics and garments has been reduced from 12.5% to 10%. There is, however no change in specific component of custom duty

Impact

- The policy extension on Technological Upgradation Fund (TUF) scheme is a positive signal from the Government, for the much required capital infusion in the sector. This would help bring economies of scale and modernization in the sector and would keep the investment momentum going particularly in the weak links of the value chain – weaving and processing
- Reduction on the custom duty on raw material is positive for the man made polyester fiber industry

Appendix – Budget 2007-08: Key Highlights

- Increase in budgetary outlay for Bharat Nirman by 31.6%, for education by 34.2% and for health and family welfare by 21.9%.
- Coverage of National Rural Employment Guarantee Scheme (NREGS) to be expanded from 200 districts to 330 districts and budget allocated Rs.120 bn. for the scheme.
- Targeted PDS to be computerised and put under an integrated information system.
- Integrated Oilseeds, Oilpalm, Pulses and Maize Development programme would be expanded.
- Financial mechanisms for re-plantation and rejuvenation would be put in place for coffee, rubber, spices, cashew and coconut.
- In order to divert rain water into dug wells, 100% subsidy would be given to small and marginal farmers and 50% subsidy to other farmers.
- A pilot programme to be implemented for delivering fertilizer subsidy directly to farmer.
- 'Aam Admi Bima Yojana' would be introduced for death and disability insurance cover to rural landless households with 50% premium subsidy from the Centre.
- National Housing Bank would introduce 'reverse mortgage' under which a senior citizen can avail of a monthly stream of income against mortgage of self-occupied house.
- PAN would be made sole identification number for all participants in securities market.
- Mutual funds would be permitted to launch and operate dedicated infrastructure funds.
- Individuals would be permitted to invest in overseas securities through Indian mutual funds.
- Short selling settled by delivery and securities lending and borrowing to facilitate delivery, by institutions would be allowed.
- Enabling mechanism would be put in place to permit Indian companies to unlock a part of their holdings in group companies for meeting their financing requirements by issue of exchangeable bonds.
- India Infrastructure Finance Company Limited Funds has been allowed to borrow from National Small Savings Fund.
- Possibility of borrowing from foreign exchange reserves from RBI for infrastructure financing would be examined.
- An autonomous Debt Management Office would be set up for public debt management.
- Reduction in peak rate for non-agricultural products from 12.5% to 10%.
- Customs duty has been abolished for all coking coal, dredgers, crude and refined edible oils to be exempt from additional CV duty of 4%.
- Reduction in duty on most chemicals and plastics from 12.5% to 7.5%, on seconds and defectives of steel from 20% to 10%, on polyester fibres and yarns from 10% to 7.5% and related raw material from 10% to 7.5%; on cut and polished diamonds from 5% to 3%; on rough synthetic stones from 12.5% to 5%; on un-worked corals from 30% to 10%, on irrigation-related machinery from 7.5% to 5%, on medical equipment to 7.5%, on sunflower oil to 15 %, on pet foods from 30% to 20%; on watch dials and movements and umbrella parts from 12.5% to 5%; on specified machinery for pharmaceutical and biotechnology sector from 7.5 % to 5 %.
- A 3% duty would be levied on all private import of aircraft, per tonne export of iron ore and chrome ore would attract duties of Rs.300 and Rs.2,000, respectively.
- Excise duty exemption limit for small scale industry (SSI) to be raised from Rs.10 mn to Rs.15 mn.

- Excise duty has been abolished for biscuits (with MRP up to Rs.50/KG), bio-diesel, specific water purification devices, all pipes of diameter exceeding 200 mm used in water supply systems and food mixes including instant mixes.
- Ad valorem excise duty on petrol and diesel has been reduced from 8% to 6%, on umbrellas and parts of footwear from 16% to 8%; on plywood from 16% to 8%.
- Customs duty on cement has been changed from Rs.400/tonne to Rs.350/tonne for MRP up to Rs.190 per bag and to of Rs.600/tonne for others
- Taxes on cigarettes have been increased by 5% and biries from Rs.7-17 to Rs .11-24 per thousand.
- Service tax has been extended to services outsourced for mining of mineral, oil or gas; renting of immovable property for use in commerce or business, development and supply of content for use in telecom and advertising purposes; asset management services provided by individuals; design services; services involved in execution of a works contract with an optional composition scheme under which tax will be levied at only 2% of the total value of works contract.
- Threshold limit of exemption on personal income tax has been extended giving a relief of up to Rs. 2,000 to senior citizens and up to Rs. 1,000 to others.
- Surcharge on income tax on all firms and companies with a taxable income of Rs.1 crore or less would be removed.
- Concessions under section 80IA for infrastructure facilities would be extended to more facilities.
- Issue of tax-free bonds through State Pooled Finance Entities formed for raising funds for a group of urban local bodies would be allowed.
- A five year income tax holiday for two, three or four star hotels and for convention centres with a seating capacity of not less than 3,000; they should be completed and begin operations in National Capital Territory of Delhi or in the adjacent districts of Faridabad, Gurgaon, Ghaziabad or Gautam Budh Nagar during April 1, 2007 to March 31, 2010.
- Concession under section 35(2AB) to be extended for five more years until March 31, 2012.
- Tax holiday to undertakings in Jammu & Kashmir to be extended for another five years up to March 31, 2012.
- Minimum Alternate Tax (MAT) to be extended to income in respect of which deduction is claimed under sections 10A and 10B; deduction under section 36(1)(viii) to be restricted to 20% of profits each year.
- Pass-through status would be granted to venture capital funds with respect to investments in specified activities.
- Limit of Rs.5 mn per investor per year with respect to capital gains bonds issued by NHAI and REC under section 54EC would continue.
- Rate of dividend distribution tax would be raised from 12.5% to 15% on dividends distributed by companies; and to 25% on dividends paid by money market mutual funds and liquid mutual funds to all investors.
- Expenditure on free samples and on displays to be excluded from the scope of Fringe Benefit Tax (FBT); ESOPs to be brought under FBT.
- Cash withdrawals by Central and State Governments to be excluded from the scope of Banking Cash Transactions Tax (BCTT); exemption limit for individuals and HUFs to be raised from Rs.25,000 to Rs.50,000.
- An additional cess of 1% on all taxes to be levied to fund secondary education and higher education and the expansion of capacity by 54% for reservation for socially and educationally backward classes.
- List of declared goods under section 14 of the CST Act to be amended to cover all small aircraft with minimum takeoff mass of less than 40,000 kgs operated by scheduled airlines.

NOTES

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