Budget Preview 2011-12

MONARCH

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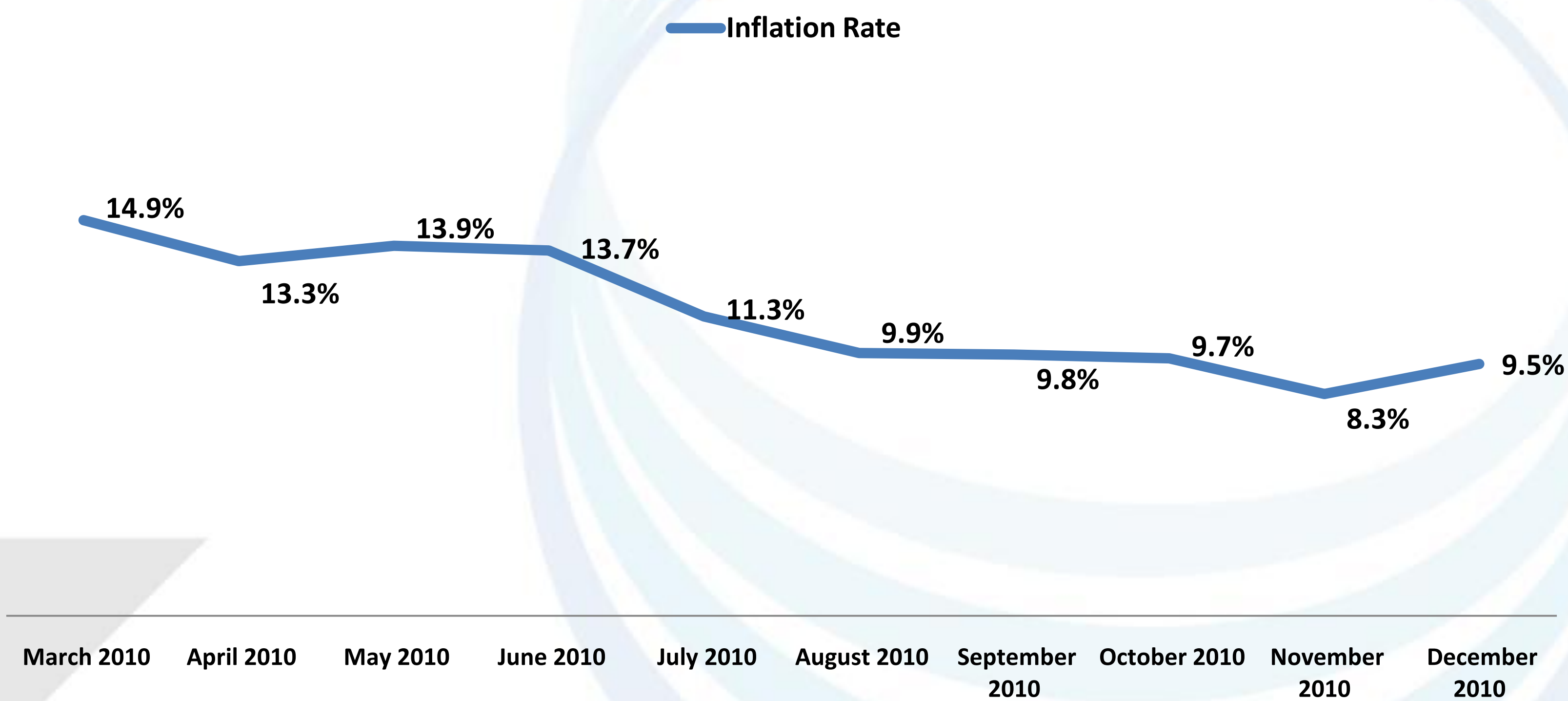
ECONOMIC BACKDROP

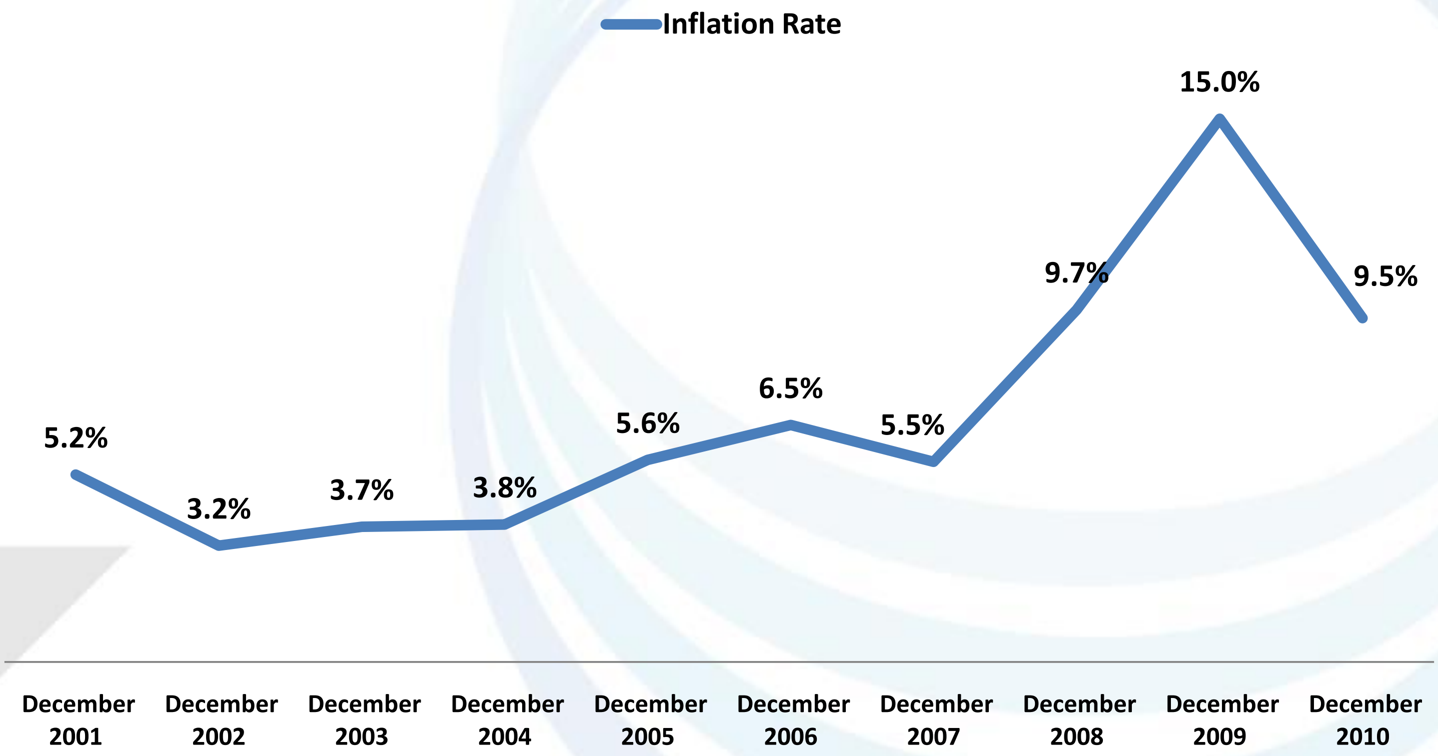
Inflation – 2010

The start for the year saw Inflation in double digits. After a magnificent year in terms of revival from global meltdown, Indian economy faced a daunting task in terms of rising prices. After an aggressive monetary tightening by the RBI the inflation cooled off and dropped towards the 9.5% mark. The economy is in dilemma with banks facing tight liquidity positions and the every rising cost push inflation.



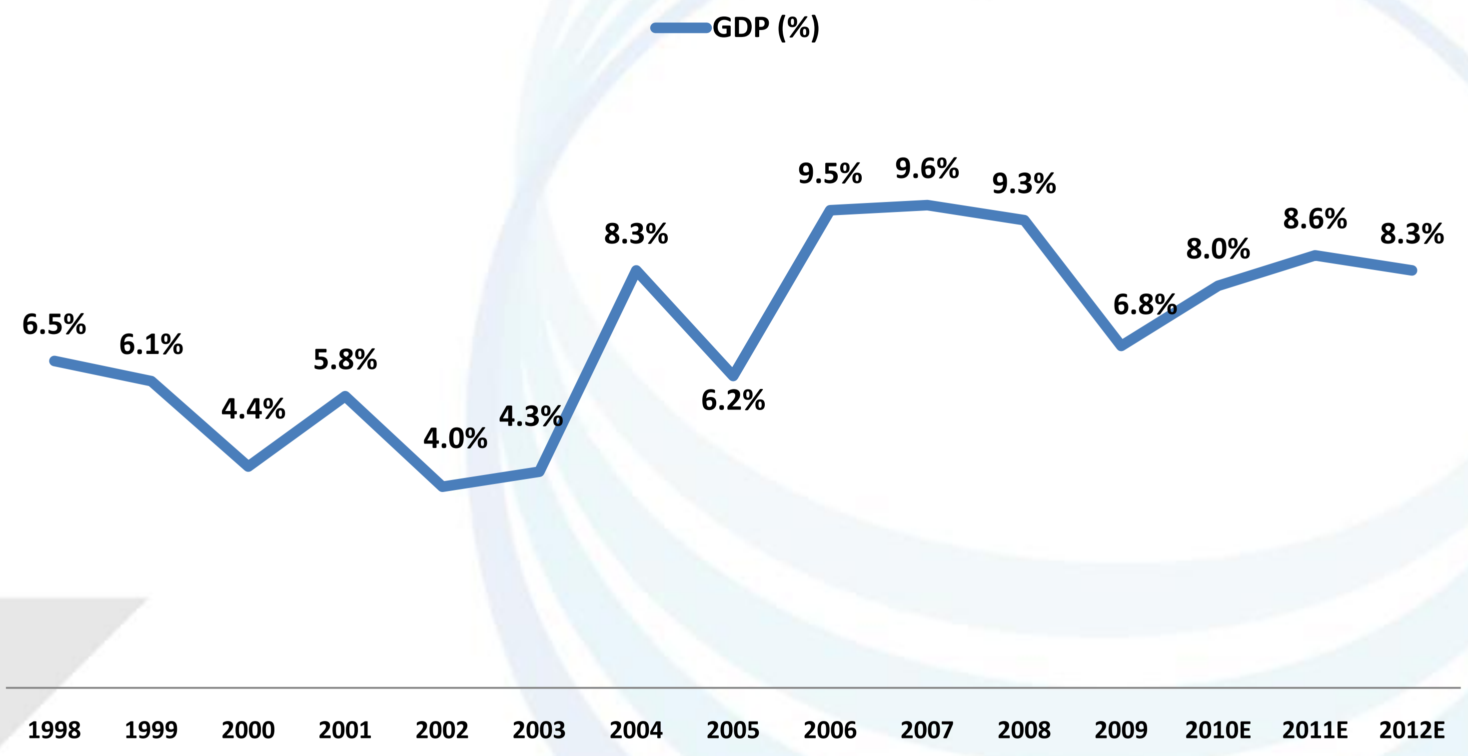
Inflation – historical…..

The historical inflation peaked out in the year 2009-10. Some stern steps by the governing body has lead to the recent most figure come at around the 9.5% mark. On an average Indian inflation has come around 6.76%-7% mark. The targeted inflation for the next fiscal is near the 5%-7% range and at the moment it is the single most worry for the country.



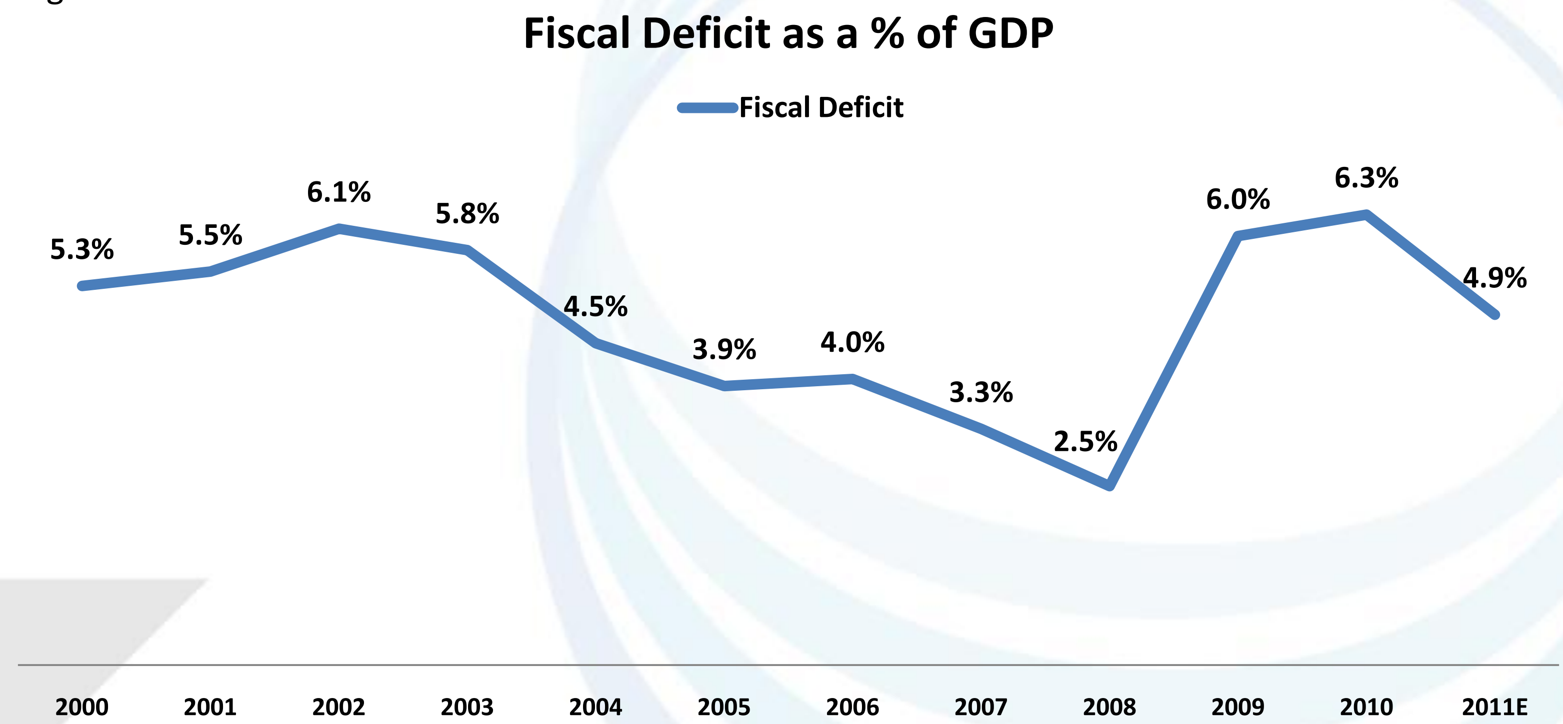
Gross Domestic Product

The country's GDP has been robust. The government has had a robust 2010 however during the end of the year the expected GDP is estimated to be around 8%. For the next year (FY11) the growth is estimated at 8.6%. The average GDP growth for the last decade has been around the 6.7%-7% mark.



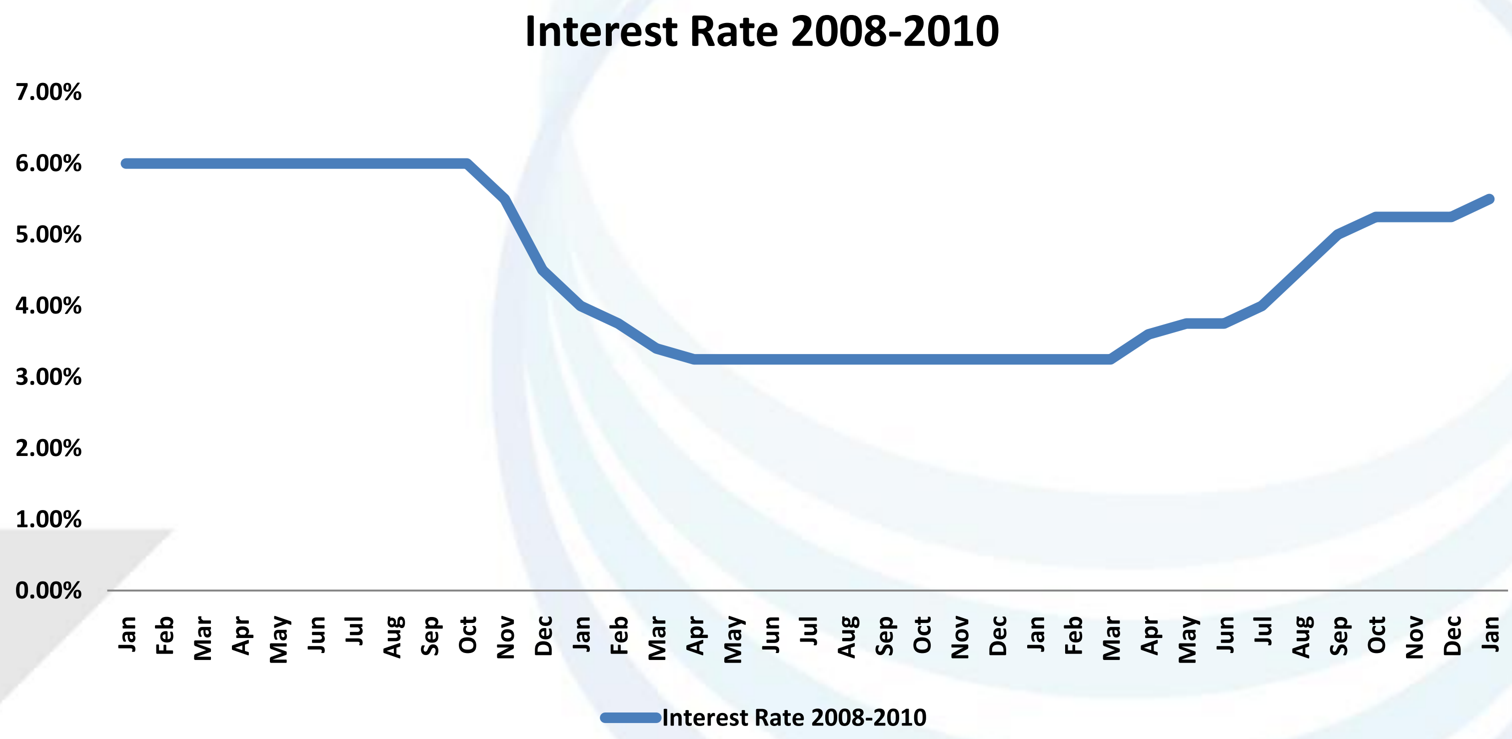
Fiscal Deficit – a rising concern

The Fiscal Deficit has been a major problem for the government. The problem however should ease going forward as the gap should come down by a significant amount due to the increased revenue collection from the recent 3G auctions and the dis-investment process under taken. There are concerns again on this front as the targeted collection may fall short however the Fiscal deficit would come down to near the 5% mark. The government is targeting 4.8%.



The Interest rate curve

The RBI has been criticized for being behind the curve as far as inflation is concerned. The RBI has been very careful in raising the rates. There are primarily two concerns. The liquidity in the system is dry and the inflation is near the highs. The challenge would be to strike the right balance so that banks can grow as it is very crucial for economic growth and that inflation does not slip out of hands.



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DIRECT TAX

The “Direct Tax” – the major expectations

• The industry was disappointed when MAT was increased from 10% - 15%. This has hampered many companies profitability. Reduction of this tax is one of the top contenders in the corporate wish lists. An industry survey even suggests a complete abolishment of MAT, which is unlikely, however a reduction can be a rare possibility. If not abolished for all companies it should be abolished for infrastructure companies.

• Other major tax proposal is regarding the surcharge and cess. Surcharge on IT was at 2.5% and was increase to 10%. The recent Bill in 2007 has exempted companies with taxable income less than 1cr from surcharge. The industry expects that the surcharge should be lowered or even abolished on individuals as well as companies and that the education cess should not be levied separately and included in Direct Tax collection.

• EOU’s operational from the year 2005-2006 can only claim tax benefits till year 2011 as against the full benefit of 10 years which is enjoyed by existing EOU’s. This is a provision which needs to be extended for encouraging exports. Industry expects that this period should be extended by at least 5 years.

• Derivative trading and hedging done by banks to develop the derivative markets in India and/or to improve their B/S should not be treated as speculative transaction like they are as of now. There is a minor expectation that these transaction will be considered as a regular business activity and be treated for IT purposes.

SECTOR OUTLOOK

Automobile

Automobile sector has outperformed since 2008 recession. In India, economic automobile sector has contributed ~10% to the nation's Gross Domestic Production (GDP). In the current fiscal this sector has shown a growth of 30% (April-Dec'10 as compared to last year same period) in Sales Volume. For the coming year we are expecting that the growth rate will come down due to the surge in the raw material cost, fuel price and the interest cost. With the increase in the cost of the steel prices and the tightening of the liquidity by increasing the interest rate will lead to increase in the vehicle price . **The industry hopes minimal change in the budget.**

Issue	Current Status	Industry Expectation	Stocks Impacted
Excise Duty	10% (Small Car, 2Ws, 3Ws CV) 22% +15000 (Utility Vehicle & sedan Cars)	Duty will remain constant Duty is expected to increase by 2% or 5000	Neutral for whole industry Negative for M&M
Lowering the excise duty on Petrol/ Diesel	24%	Lowering the excise duty on diesel to control the inflation	Positive for the CV segment (+ve for Tata Motors, Ashok Leyland, Force motors)
Custom duty on imported vehicle	110%	Expected to come down	Positive for all luxury vehicle importers
Reduction in the import duty of rubber and rubber product	20% on natural rubber (for import up to 14,000MT the duty is reduced to 7.5%) 7% on finished rubber product	Reduction in the disparity of the duty between rubber and rubber products)	Positive for Ceat, Apollo Tyre, MRF and JK Tyres
Retain R&D Benefits	200% weighted Reduction	Retain Same	Positive to neutral for Autoline Ind., Hero -Honda Bajaj Auto
Spending and allocation for Rural Markets	Rs. 41000Crs	Increase in the allocation	Positive for M&M, Tata motors, Ashok Leyland

Banking & Financial Services

Huge divergence between the growth rates of deposit and credit has been witnessed from April-Dec'10. Due to the disinclination of banks in hiking interest rate in line with the RBI directives these gap between credit and growth has peaked at 9%. The increase in delinquency rates coupled with stipulated provisioning coverage ratio of 70% hampered the margins of many banks in the year to date. Recently banks have started increasing interest rates and have seen huge jump in incremental deposits.

Issue	Current Status	Industry Expectation	Stocks Impacted
FDI Limit for insurance	26%	Increase in FDI limit to 49%	+ve for Kotak Bank, ING Vysya. ICICI, HDFC, SBI
Infrastructure Bond	Till date only banks are allowed to raise 5yr deposit, which are eligible for tax deduction under 80C	Recently NBFC and few Corporate body has got license to raise money through Infra Bond	+ve for IDFC, IFCI, LT
Reduction in tenure for tax exempt deposit	5yr	Reduced to 3yrs	+ve for All Banks
Government Borrowings	The government is likely to borrow about Rs4.5 trillion in FY11, cushioned by the collections from the 3G auctions and the proceeds from divestments.	The government's expenditure should be within limits as its spending may further aggravate the liquidity Problem.	Negative for all banks as net borrowings are expected to be higher. Lower repayments,
Listing of Insurance Company	Insurance Company are not Listed	Insurance Company can enter into Capital Market	-
Steps on STT	2%	Reduce it to 1%	+ve for Religare
Clarity on issuing Banking licenses			+ve for all NBFC like IFCI, IDFC.

Cement

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Revenues of the cement companies were weak during last 1 year on account of lower cement prices due to excess supply as well as poor volumes on account of slower execution of infrastructure projects. Furthermore, raw material (mainly coal) and freight costs have also been on a rising trend, further affecting profitability of the cement companies. Hence in the short term until capacities get fully absorbed the sector could see profitability margins remaining under pressure.

Further, We expect demand of cement to grow by 9-10% over long term on the back of demand coming from rural housing and push up from the government in the form of higher fund allocation and incentive for public private partnership projects in infrastructure space. Hence, we remain bullish on cement companies on long term basis.

Issue	Current Status	Industry Expectation	Stocks Impacted
Import Duty	Currently Coal, Gypsum and pet coke are charged with an import duty of 5%	The industry wants these duties to be completely abolished	Positive-Ambuja Cement, Ultratech, India and Shree Cement
Excise Duty	MRP not exceeding Rs 190 per 50 kg bag then a specific rate of excise duty of Rs 290 per tonne, if MRP exceeds Rs 190 per bag then duty of 10% of MRP. For institutional sale 10% or Rs 290 per tonne whichever is higher.	The cement industry wants a abatement of 55% in Excise duty and has requested uniform rate of excise duty	Positive-For all Companies
VAT	VAT on cement is charged at 12.5%	VAT on cement should be brought in line with similar construction material like steel to 4%.	Positive-For all Companies
Taxes	Taxes and levies constitute a r o u n d 3 3 % , which constitutes 60% or more of the ex- factory price.	Some Tax incentives	Positive-For all Companies
Credit for Royalty on limestone and duty / cess on indigenous coal	Royalty on limestone is one of the levies for which credit is not allowed at present	The industry is seeking the royalty paid on Limestone to be allowed as credit either as Cenvat credit.	Positive-For all Companies

Capital Goods & Engineering

In the first half of the FY11 we have seen decent order inflow in the engineering sector. However this has not been reflected on the books of the company due to the delay in the execution as well as the payment received. It has been also been witnessed that operating margins of the company's were under pressure due to surge in the raw material price and the high competitive environment. Though there is a backlog of the strong order book supported by the huge industrial Capex this sector will face difficulties on the back of increase in the raw material price, increase in the interest cost and high competition from the domestic and overseas companies

Issue	Current Status	Industry Expectation	Stocks Impacted
Custom Duty on Power	Custom Duty exempt under mega Power plant	Exception on custom duty for power plant	+ve for all the Engineering Company. LT, BHEL
Allocation on renewable energy		Increase in the allocation for renewable energy production	+ve for Suzlon, Moser bear and Premier Ltd.
Increase in the excise duty	10%	Could go up-to 12%	-ve for all the company's effecting the operating margins.
Excise duty on Air Condition	8%	Expected to increase upto 10%	-ve impact on Blue Star, Voltas, Videocon
Chinese import duty		Increase in the excide duty on the import of chinese electric equipments	+ve for Power Ancillary Crompton graves, Havel's, BHEL & ABB

Construction

The construction industry will remain in a sweet spot during the country's transition from being a developing country to a developed country. The government in recent years has realized that in order to support the growing GDP, a much better transportation system for commercial and social purposes, increasing power generation and transmission capacity to support the growing need of power both at consumer and industrial level, a larger irrigation network to support agriculture and urgent need of improving water purification and sewerage systems for the well being of a burgeoning population and increasing urbanization is needed. Further in order to support the above, cement, steel and other industries have announced aggressive expansion plans going forward. All of these, in our view, would result in unprecedented order flows for domestic construction companies. Especially we remain bullish on construction companies engaged in constructing roads & highways, Irrigation & water treatment plants and industrial facilities.

Issue	Current Status	Industry Expectation	Stocks Impacted
MAT	Infrastructure projects are paying 18% MAT raised from 15% in the previous budget.	MAT should be lowered from the current levels	Positive - For companies in BOT projects (IVRCL, NCC, Sadbhav, Gayatri Projects)
Infrastructure financing	Infra bonds and financing of infra projects through the medium of IFCL introduced last year	A number of measures required to still ease out infrastructure financing.	Positive-For all Companies

FMCG

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Fast Moving Consumer Goods (FMCG) is the fourth largest sector of Indian economy with the market size of 130,000Crs. This sector has shown a CAGR of 11% of the decade. FMCG companies has shown a volume growth of 15-17% proves the consumerism and demographics of the country. Further, it has been witnessed significant growth in the rural area on the back of good monsoon, direct subsidy to farmers and govt. initiative like NREGS. Though the company's revenue is growing there is a high margin pressure on the back of increase in the raw material cost and reduction in the realization cost.

Issue	Current Status	Industry Expectation	Stocks Impacted
Focus on rural development	Allocation under NREGA at 40,000Crs. and others	Increase in the allocation to enhance the rural income	+ve for all FMCG companies
Increase in MAT	18%	Rise upto 20%	-ve for all FMCG Companies
Increase in the excise duty	10%	No. Change	Neutral for all Companies
Divided distribution Tax	Currently 15% (1.66%-surcharge + education cess)	Reduce to 10%	+ve for GSK, HUL,ITC,
Segment Excise Duty 1. Cigarette 2. Packaged Water 3. Sugar Confectionary 4. Biscuits 5. Sanitary Napkins	1. Irrationalized duty w.r.t type 2. 8% 3. 10% 4. 4% 5. 10%	1. Increase by 6-8% 2. Full Exempt 3. Reduce it to 4% 4. Full exempt 5. Full exempt	1. Neutral for ITC 2. Positive for Tata Beverages 3. +ve for Bajaj hind, Renuka 4. +ve for HUL, ITC, Britannia 5. +ve for HUL
Trade & Copy right law		FMCG companies want the trademark and copyright laws enforced more strictly	+ve for all the company for branding company HUL, Marico, DABUR.

Health Care & Pharma

The health care and pharma industry have had robust growth in the past decade. India is having a huge potential to become a low cost health care provider in the world. Beside the R&D cost are one of the lowest the pharma markets over the world can offer. The health care industry as a whole is at a very crucial stage of its life cycle. The Indian demographics and government policies will play a crucial role in determining the future for the industry.

Issue	Current Status	Industry Expectation	Stocks Impacted
Expenditure on HC	Currently at Rs 22000 crore	Increase the allocation to boost the sector, and give it an infrastructure status	+ve Fortis, Wockhardt & Apollo Hospitals
Research & Development	200% weighted deduction on R&D, 175% on outsourced work	Extend the benefits on other out of the facilities R&D such as clinical trials.	+ve Biocon, Piramal Life-Science

Metal

It has been witnessed in the first nine months of FY10-11 metal price has significantly increased. Steel prices have almost increase by doubled. But even though these increase has not been reflected on the books of the company basically due to increase in the price of Raw material i.e. Coal & Coke, there prices has increase by more than double which showed pressure on operating margins of the Metal companies. In late 2010 Steel prices came in line off the international prices which were falling from May 2010.

Issue	Current Status	Industry Expectation	Stocks Impacted
Import Duty 1. HR Coil 2. Pig Iron 3. Copper Concentrate	1. 5% 2. 5% 3. 2%	1. Increase upto10% 2. Full Exempt 3. Full Exempt	1. +ve for Tata Steel,JSWSteel 2. +ve for Sesa Goa, NMDC 3. +ve Hind. Copper, Hindalco
Custom duty on Vanadium Pent oxide and Vanadium sludge / Ammonium Metavanadate	7.5%	Full Exempt	+ve for SAIL, NMDC & Essasr Steel
Ore for manufacturing Ferro Alloys	2%	Full Exempt	+ve for MOIL, OMC, Tata Steel & Hind Zinc
Custom Duty on Ferro Alloy	5%	Increased to 7.5% (except Ferro Nickel as it is fully imported)	+ve for Tata Steel, JSW Steel, Jindal Steel, Sterlite Industries, Hindalco
Export Duty	15%	Increase it to 20% uniformly	-ve Sterlite Industry, Sesa Goa

Power

Till April-Dec'10 India has generated 669bn units of power while keeping the supply demand deficit of 8%. As against the targeted addition of power capacity of 21,441MW we have achieved added the capacity of 10,210 MW taking the total Power production capacity of India to 170,228MW. One of the major concerns in the power sector is to control the losses in the power distribution. Another biggest concern for the power producer is the increase in the raw material Cost i.e Coal, which has already shown an effect on the operating margins of power producer company.

Issue	Current Status	Industry Expectation	Stocks Impacted
Inters on loan taken by State Electricity Board (SEB)	0% Discount	Discount of 3-5% Depending on performance	+ve for all the company
Benefits of 80IA	The benefits were expected to be avail till 31/03/11	Expected to increase till 31/03/15	+ve for complete Power Sector
Incentive on the usage of Renewable source of energy	5% discount on the custom duty of Solar power equipment and excise duty benefit on rotor blade of wind power generator	Improvement in plan allocation for the renewable energy segment and the continuation of the existing Concessions	+ve for Suzlon, Indosolar,
Import Duty on Coal	5%	Full exempt	+ve for torrent Power, NTPC, Adani Power, Tata Power
Debt Fund		Formation of Debt Fund that will raise low cost and long-term recourses to re-finance power projects	If implemented +ve for L&T, BHEL

Real Estate

The overall Outlook for this sector seems negative. The sector is facing structural problems such as higher land investments, rising interest rate and increase in labour cost due to the higher inflation. These factors have already had a significant impact on the financials of the companies. The already debt burden companies have been impacted most as their pricing powers have been curbed. The increase in loan to value to 80% has further dampened the sentiment of the sector. Further, Liquidity crunch is hurting the growth prospects of the companies.

Issue	Current Status	Industry Expectation	Stocks Impacted
Interest Subsidy	Interest subvention of 1% on loans of up to Rs1 million on property of Rs 2 million up-to March 2011	To continue in the next year	+ve for all the company
Stamp duty	The stamp duty rates vary between 5 per cent to 14 per cent.	The government should also reduce stamp duty rates across the states to 2 per cent.	+ve for all the company

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Research Team

Manoj Sathawara	Manoj.Sathawara@monarchproject.com
Rushabh Shah	Rushabh.Shah@monarchproject.com
Dipti Saraf	Dipti.Saraf@monarchproject.com
Suhani Patel	Suhani.Patel@monarchproject.com
Chintan Antani	Chintan.Antani@monarchproject.com
Sankit Shah	Sankit.Shah@monarchproject.com
Nishant Bali	Nishant.Bali@monarchproject.com

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