# Run-up to Budget 2008-09

In all probability the last budget to be presented by the United Progressive Alliance government is likely to be a populist budget, considering the general parliamentary elections in 2009 and the forthcoming elections in some of the politically important states like Rajasthan, Madhya Pradesh, Delhi and Chattisgarh. In line with this, the finance minister is likely to substantially increase the allocation for health, rural development and employment generation schemes. Moreover, we expect some relaxation in tax structure that would benefit the lower- and middle-income population (the *Aam admi*).

However, given the distinct moderation in the gross domestic product (GDP) growth, the government is expected to take steps to stimulate investment and consumption demand. Inflation concerns coupled with turmoil in financial markets worldwide, would also weigh on the budget. The task ahead for the finance minister is to strike a fine balance between political compulsions and economic objectives in this budget.

We expect the following changes in the budget:

### Taxation

- Roadmap to introduce Goods & Services Tax (GST) in FY2010 and accordingly rationalise the existing excise duty structure
- Lower the peak custom duty to 7.5% from 10% currently
- Lower custom duty on commodities (to tackle inflation) and increase export duty on natural resources like iron ore
- Rationalise the existing excise duty structure on petroleum products (another step to control cost push inflation)
- Provide some tax relief to individual taxpayer through either reduction of surcharge and/or increasing the tax exemption limit and standard deduction
- Keep the service tax rate unchanged but bring in more services under the tax net
- Capital market related: 1) Reduction in dividend distribution tax to 12.5% from 15% currently 2) Marginal increase in securities transaction tax (STT)

### Expenditure

- Increase in allocation towards health and education
- Increase in allocation for rural development and employment generation schemes
- Enhanced credit for agriculture to address lagging growth and ensure all inclusive economic growth
- Focus on improving financing options for infrastructure development by a possible inclusion of infrastructure sector as part of 'priority sector', increased viability gap and/or tax exemption on infrastructure bonds and/or more liberal norms on external commercial borrowings for infrastructure projects
- Provide relief package for export-oriented industries that have huge employment potential like textiles, garments and IT-enabled services

**Sectors to benefit from the budget**

- Engineering and capital goods
- Textile and garments
- Education
- Infrastructure financing companies
- Fertiliser industry
- Oil and gas

### Buoyant tax collections

Tax collections have been buoyant during the first nine months of FY2008. The government has been able to surpass the budgeted growth rate in tax collections from most of the segments such as corporate tax, income tax, excise tax etc. With this, the net taxes collected have grown by 27.5% year on year (yoy) during April-December FY2008 period, well above the budgeted 16.7% growth for FY2008. The strong momentum in tax collections has continued post

M9FY008 as evident by 41.4% year-on-year growth in direct tax collections during the period April-February 15, 2008.

While the buoyancy in tax collection should help the government dole out tax benefits in the likely-to-be populist budget, the anticipated higher expenditure due to increased spending on social infrastructure (education, health etc) and interest expenses would leave lesser room for tax relief reforms. Notably, the interest expenditure is expected to be higher on account of bond issued for market stabilisation scheme (MSS) to contain rupee appreciation, and other off-balance sheet items such as oil bonds and fertiliser subsidies.

**Robust tax collection (Rs '00 crore)**

| Tax collections | Apr-Dec | | Budgeted growth | |
|---|---|---|---|---|
| | FY08 | %yoy | FY08BE | Rate (%) |
| Corporate | 1,287 | 37.1 | 1,684 | 15.0 |
| Income | 663 | 42.7 | 988 | 19.8 |
| Customs | 745 | 17.0 | 988 | 20.7 |
| Excise | 755 | 5.1 | 1,302 | 11.0 |
| Others | 444 | 44.4 | 520 | 30.6 |
| Gross taxes | 3,893 | 27.0 | 5,482 | 17.2 |
| Devolvement to states | 917 | 25.2 | 1,443 | 18.4 |
| **Net taxes** | **2,960** | **27.5** | **4,039** | **16.7** |

Source: Ministry of Finance, Sharekhan Research

## Fiscal deficit under control

Due to continued strong growth in revenue receipts (on the back of improved tax collections) and largely contained expenditure, the government is expected to comfortably meet or even exceed the revenue and fiscal deficit targets set in the budget 2007-08. For the first nine months of FY2008, the fiscal deficit was 51.4% of the budgeted figure of Rs150,948 crore, much lower than 62.3% in the corresponding period last year.

## Fiscal discipline needs to be maintained this year too

Given the expected increase in planned expenditure towards social infrastructure (health, education and rural development) and the likely implementation of the sixth pay commission this year, there could be temptation to deviate from the deficit targets set under the Fiscal Responsibility & Budget Management Act (FRBM). The act provides for bringing down the fiscal deficit and the revenue deficit by 0.3% & 0.5% respectively every year. Any material deviation from FRBM targets will be a negative from the reforms perspective especially for the foreign investors who watch this benchmark carefully.

## Moderation in GDP growth

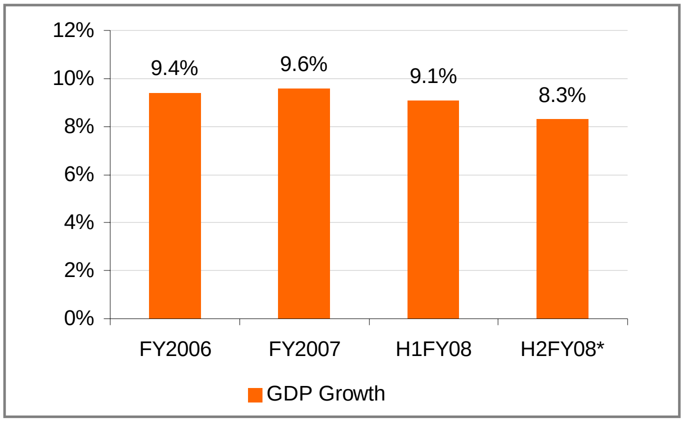
The Indian economy appears to be in a consolidation phase. After growing by 9.4% in FY2006 and 9.6% in FY2007, the advance estimates by the Central Statistical Organisation (CSO) clearly indicate a moderation in the growth rate to 8.7% in FY2008. What's more, given the healthy growth of 9.1% in GDP during H1FY2008, the implied growth rate stands at just 8.3% for the second half of the fiscal. The appreciation in the rupee that is hurting exports, Reserve Bank of India's (RBI) hawkish policy stance that is moderating the credit growth and the uncertain global

**Central government finances for FY2008**

| (Rs '00 crore) | FY2005A | FY2006A | FY2007RE | FY2008BE | FY2008E |
|---|---|---|---|---|---|
| Gross tax revenues | 3,060.0 | 3,701.4 | 4,678.3 | 5,481.2 | 5,964.7 |
| *% change yoy* | *20.3* | *21.0* | *26.4* | *17.2* | *27.5* |
| Net tax revenues | 2,248.0 | 2,702.6 | 3,459.5 | 4,038.7 | 4,410.8 |
| *% change yoy* | *20.2* | *20.2* | *28.0* | *16.7* | *27.5* |
| Non tax revenues | 812.0 | 772.0 | 773.6 | 825.5 | 946.7 |
| Total expenditure | 4,976.8 | 5,061.2 | 5,816.3 | 6,805.2 | 7,152.5 |
| *% change yoy* | *5.6* | *1.7* | *14.9* | *17.0* | *23.0* |
| Plan expenditure | 1,322.8 | 1,407.0 | 1,727.3 | 2,051.0 | 2,061.2 |
| *% change yoy* | *8.2* | *6.4* | *22.8* | *18.7* | *19.3* |
| Non plan expenditure | 3,654.1 | 3,654.2 | 4,089.0 | 4,754.2 | 5,091.3 |
| *% change yoy* | *4.7* | *0.0* | *11.9* | *16.3* | *24.5* |
| Fiscal deficit | 1,252.8 | 1,464.8 | 1,523.4 | 1,509.5 | 1,468.3 |
| *As % of GDP* | *4.0* | *4.1* | *3.7* | *3.3* | *3.2* |
| Revenue deficit | 783.5 | 923.0 | 834.5 | 714.8 | 689.0 |
| *As % of GDP* | *2.5* | *2.6* | *2.0* | *1.5* | *1.5* |
| Primary deficit | -16.5 | 138.8 | 61.5 | -80.5 | -184.3 |
| *As % of GDP* | *-0.1* | *0.4* | *0.2* | *-0.2* | *-0.2* |

scenario is taking its toll on the overall growth in the economy. In fact, the moderation is more than expected. For instance, the year to date (YTD) non-food credit growth this year has slowed to 22.4% against the RBI's own target of 24-25% range and much lower than 39.6% growth in FY2006 and 27.95% growth in FY2007.

**GDP growth (%)**

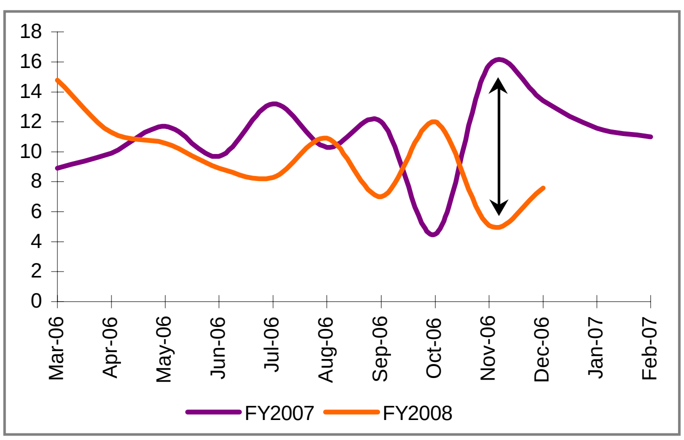



Source: CSO, Sharekhan Research

*Implied growth based on CSO's advance estimate of 8.7% growth

The major reason for the slowing GDP growth rate has been the slower growth in manufacturing and agriculture sectors. Agriculture (accounting for about 17% of GDP) has been a laggard after growing at its peak rate of 10% in FY2004. It is expected to grow at 2.6% in 2007-08 down from 3.8% in 2006-07. Manufacturing (which makes up about 25% of the GDP) is likely to grow at 9.4% in 2007-08 as against 12% last year.

**Slowdown in manufacturing sector (%)**



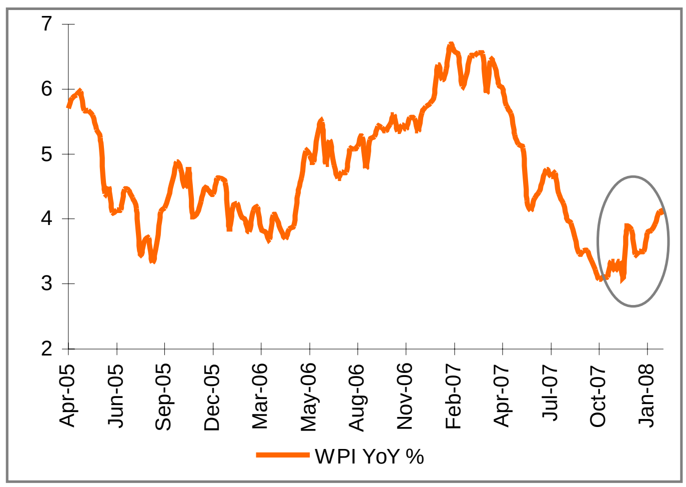

Source: Bloomberg, Sharekhan Research

Consequently, we believe that the finance ministry would take steps to provide the much-required stimulus to investments in infrastructure and some relief to large labour-intensive industries like textiles, garments, IT-enabled services etc. The consumption demand stimulus is likely to be limited to tinkering with tax structure for individual taxpayers in the budget. The finance minister would largely rely on the implementation of sixth pay commission to boost the consumer demand in the economy.

### Inflation concerns

As shown in the chart below inflation has been coming down since the beginning of CY2007 following RBI's tight monetary policy. The inflation rate reached a low of 3.07% in October 2007. However it has been showing an uptick since November 2007 end and at present (February 02, 2008) stands at 4.07%. In addition fuel prices (petrol and diesel) were raised by 3-4% from those of last week. Our calculations indicate that the inflation rate will go up by 11 basis points as a direct impact of this increase in addition to an indirect impact of around 11-13 basis points on the inflation rate.

**Inflation under control**




Source: Bloomberg, Sharekhan Research

However, we expect the inflation to remain within the RBI's tolerance range of below 5% in 2008-09. The government is expected to take some steps to reduce cost pressures in the budget. We believe that the government could reduce custom duty and excise duty on metals and some other commodities to control cost push inflation. Another possibility is the reduction in the excise duty on petroleum products, especially given the spiraling prices of crude oil.

## Sector-specific impact

### Automobiles

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Excise duty on cars | 16% on small cars; 24% on all other cars and UVs | Uniform rate of excise duty on small as well as big cars at 16%. | **Positive** for Maruti, M&M and Tata Motors. Lower prices should help in volume growth |
| Excise duty on motorcycles | 16% | 8% | **Positive** for Hero Honda, Bajaj Auto, TVS Motors. Lower prices should help in volume growth |
| Increased expenditure on agriculture | - | - | **Positive** for tractor sector. Positive for M&M |

### Auto ancillary

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Excise duty on raw materials | Key raw materials like GP/GC sheets, HR coils, Aluminium, Copper and Nickel attract excise duty of 16.5% | Reduce excise duty on these key raw materials | **Positive** as lower raw material prices will reduce the costs |
| Excise duty on tyres | 16% | To be reduced to 8% | **Neutral** for the tyre sector. We believe this is unlikely to happen this year |
| Customs duty on raw material for tyres ie natural rubber | 20% | 10% | **Positive** for tyre companies like Ceat and Apollo Tyres. |

### Banking

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Tax saving deposit under section 80C | Five-year lock-in and restrictive in nature | The lock-in period for the term deposit may be reduced from five years to three years to bring it at par with other tax saving instruments such as ELSS and mutual funds | **Positive** for the sector as it will help banks tide over the problem of deposit mobilisation to a great extent |
| FII investment limit | Capped at 20% for public sector banks (PSB) | Increase in limit of FII investments | **Positive** for PSBs, as this would lead to capital infusion and help accelerate growth |
| TDS on fixed deposits | TDS ceiling at Rs5,000 | Likely to be increased to Rs10,000 | **Positive:** Higher TDS limit would aid deposit growth |
| Infrastructure financing | Tax break on interest earned on long-term lending to infrastructure industries (u/s 10-23G) was removed | Re-introduce the tax exemption on long-term infrastructure lending | **Positive:** Such measure would help accelerate overall advances growth |

## Cement

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Excise duty on cement | In case MRP is less than Rs190 per bag, excise is fixed at Rs350 per tonne. In case of MRP being in the range of Rs190-250, excise is charged at 12% of MRP, and in case if MRP exceeds Rs250 per bag, excise will be charged at Rs600 per tonne | To rationalise the duty structure, providing abatement of 35% on the excise duty levied on MRP | **Positive** for the sector as a whole, as prices will reduce or the manufacturers will get some cushion against increasing cost |
| VAT | VAT on cement and clinker is charged at 12.5% | VAT on cement and clinker should be brought in line with similar construction material like steel to 4% | Will bring down the price for users and will be **positive** for the sector. However, we believe this is unlikely |
| Import duty on coal and pet coke | Non coking coal and pet coke attract import duty of 5% | Reduce to 2% | **Positive** for sector as this will improve the operating margins |
| Royalty on lime stone | Rs67 per tonne | Reduction in royalty | **Positive** as cost of production will come down |

## Engineering, capital goods and construction

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Excise duty on power equipment | Currently at 16% | Likely to be reduced | **Positive:** Reduction in operational cost and input cost |
| Custom duty on project imports | Peak duty of 10% | Likely to be reduced to boost infrastructure investment | **Marginally negative:** While the rupee appreciation has reduced the cost of exports, further decrease in excise duty may put domestic manufactures in a cost disadvantage |
| Subsidy on shipbuilding | Subsidy of 30% expired on August 2007 | Extension in subsidy likely | **Positive:** All shipbuilding companies; positive for L&T |
| Excise duty on ACs | Currently at 16% | Likely to be reduced to promote energy efficient devices | **Positive:** Companies manufacturing ACs would benefit |
| Infrastructure spending | - | Continue emphasis on increase in spending | **Positive:** Investment flows to continue, which will add to the already bulging order books of E&C companies |
| Section 80IA | Only available to developers | More clarity is expected in the budget and it should be extended to contractors as well. | **Positive** for the sector as it will reduce the tax liability of the contractors |

## FMCG

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Cigarettes | Specific excise duty (varies with type and length of cigarette) | Status quo | None |
| Biscuit | Excise duty of 8% on biscuits priced above Rs50 per kg | Total excise duty exemption, similar to the that granted to other food mixes in the Union Budget 2007-08 | **Positive** for Britannia and ITC |
| | VAT of 12.5% | To reduce from current 12.5% to 4% | **Positive** for Britannia and ITC |
| Processed foods | Excise duty levy of 16% | To reduce from current 16% to 8% (except pan masala and tobacco products) | **Positive** for Nestle, Britannia, ITC, HUL and Agro Tech Foods |
| Packaging material | Excise duty levy of 16% | Reduced to 8% | Duty cut on packaging material can bring **positives** for all FMCG companies. |
| Lauryl alcohol (input for toothpastes, shampoos, soaps and detergents) | Custom duty of 15% | Reduced to 10% | **Positive** for Colgate, HUL, ITC, Godrej Consumer and P&G |
| Custom duty on palm oil and other edible oils | Crude palm kernel oil having Free Fatty Acid (FFA) attract customs levy of 12.5% | Reduced to 10% | **Positive** for HUL, Godrej Consumers and ITC |
| | Oils (except crude palm oil and crude palm stearin) having FFA 20% or more imported for manufacturing of soaps, industrial fatty acids and fatty alcohol by a manufacturer attractcustoms levy of 20% | Reduced to 10% | We believe that marginal reduction in custom duty is possible which can bring **positives** for HUL, Godrej Consumers and ITC |

## Fertilisers & Chemicals

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Removal of custom duty on imported LNG | 5% | 0% | **Positive** for urea or nitrogen based fertiliser manufacturers, as natural gas is used as feedstock and fuel |
| VAT on natural gas | NG is kept out of VAT in some states, which levy sales tax as high as 20% | Likely to come under "declared goods", thus under uniform sales tax/VAT of 4% | **Positive** for urea or nitrogen based fertiliser manufacturers, as natural gas is used as feedstock and fuel |
| Customs duty on soda ash | 7.50% | 5% | **Negative** for the sector, as cheaper imports may put pressure on realisation |
| Excise duty on pesticides | 16% | 8% | **Positive**, as it would lead to increased usage of pesticides |

## Sugar

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Molasses | Excise duty levy of Rs750 per tonne | Reduced to Rs250 per tonne | Shall boost the ethanol blending programme. **Positive** for ethanol manufacturers such as Bajaj Hindustan, Shree Renuka Sugars and Balrampur Chini |

## Education

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Allocation for education sector | Allocation in 2007-08 budget of Rs32,362 crore (increase of 34.2% over previous year) | Similar increase in allocation expected | **Positive** for Navneet Publications, Educomp Solutions and Everon Systems |

## Media and entertainment

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Reduction in excise on STBs and its major components—tuner, RF modulator and remote control unit | Excise levy of 16% | Reduced to 8% | Will reduce cost of imported STBs, as CVD will get reduced in line with excise duty. This apart from lowering subsidy burden on MSOs and DTH operators will enable faster rollout of CAS and DTH services. **Positive** for WWIL, Dish TV, HTMT |

## Metals & Pipes

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Excise duty on steel products | 16% | Reduction likely | **Positive** |
| Customs duty on stainless steel products | 7.5% | To be increased to 10% | **Positive** to extent of reducing imports |
| Customs duty on raw materials such as met coal, scrap, nickel | 5% | 2% | **Positive** for metal companies as well as pipe manufacturers |
| Duty on export of Iron ore | Rs50 for ferrous content ≤ 62%<br>Rs300 for ferrous content > 62% | Likely to increase | **Positive**. Will discourage exports |
| Water infrastructure | - | Likely increase in spending on water infrastructure | **Positive** for the sector. **Positive** for Jindal Saw, Ratnamani Metals |

## Hotels

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Section 80ID—100% deduction of profits from 2, 3 and 4 star hotels constructed in NCR and allied districts between April 2007 -March 2010 | 1) Deduction not applicable to 5 star hotels<br>2) Deduction is for 5 years | 1) Deduction to be extended to 5 star hotels<br>2) Tax holiday to be extended from 5 yrs to 10 yrs | **Positive** for hotels coming up in the region |

## Oil & Gas

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Service tax on exploration and production activities | 12% | Removal of service tax | **Positive** for oil E&P companies as cost of production would decrease |
| Custom duty on crude imports and petroleum products (Petrol, Diesel) | 5-10% | 2.5-5% | Reduction of import duties for crude and petroleum products will reduce the under-recoveries for marketing of petroleum products |
| Reduction of ad-valorem excise on Petrol/Diesel | 6% | 4% | Reduction of duties will reduce the under-recoveries from the sale of petroleum products |
| Removal of custom duty on imported LNG | 5% | 0% | **Neutral** |
| VAT on natural gas | NG is kept out of VAT in some states, which levy sales tax as high as 20% | Likely to come under "declared goods", thus under uniform sales tax/VAT of 4% | **Neutral** |
| Infrastructure status | LNG regassification terminals do not enjoy the infrastructure status | LNG terminals may get infrastructure status | **Positive** for the sector as infrastructure status will encourage more companies to set up LNG terminals |

## IT Services

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Demand from Government to focus more on e-governance projects | Government has spent so far Rs3.9 billion in current year on e-governance projects. Increase this allocation to Rs7.9 billion | Government may increase allocation for e-governance projects | **Positive** for companies like 3i Infotech, CMC, and Wipro Info that focus on e-governance contracts |
| Extension of tax exemptions U/S 10A and 10B. | Tax exemption under section 10A and 10B for STP registered units to expire by March 2009 | Extension by one year of direct tax exemptions under section 10A and 10B on STP registered units | **Positive:** It will be more benefical to mid-cap IT companies who do not have scale that justify setting up centers in SEZs. Movement of resources to SEZs may not be accepted well by employees. In light of probable US slowdown it may bring some relief to IT companies. Non-extension will increase effective tax rates for IT companies. This, in turn, would lower the net margin by 150-300 basis points. Impact will be more pronounced for mid-cap IT and ITES/ BPO units sector, which generally make lower operating margins compared with large IT companies. |
| Excise duty levied on packaged software sold over the counter | Presently, 8% duty is levied on package software sold over counter | Complete abolishment of excise levied on customised and package software | It will have positive impact on software industry and also help in curbing piracy, as customers might resort to buying genuine softwares. Cost of administration and compliance for IT companies will be also reduced |
| Facility under large tax payer scheme | Companies with at least Rs10 crore advance tax are eligible | Industry wants this limit to be relaxed | **Positive**. Even smaller IT companies would benefit from reduced compliance cost and delays |
| Fringe benefit tax(FBT) on employee stock options plans (ESOPS) | FBT levied on ESOPS to be effective from April 01, 2008 | Industry wants clear-cut guide lines for accounting of ESOPS | **Neutral**. IT companies would have to pay upfront FBT, which they will recover from employees. |

## IT Hardware

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Personal computers (PCs) are at present classified as a capital good under the CENVAT Credit Rules, 2004, whereby the credit is available only if the computer is used in the factory of manufacturer of final products | Credit is available only if PCs are used in the factory of manufacturer of final products | The scope of availing the credit of CVD/Excise duty paid on PC should be widened to include any use within the business, whether in the factory or in the office of the manufacturer | **Positive** for hardware manufactures if scope is widened, as It will boost the sales and increase the penetration of PCs |
| PCs in India currently face a 4% CST for both manufacturers and service providers. Dealers/resellers can avail a concessional CST rate of 3% on providing the statutory forms (Form-C), though the tax is non-creditable for any class of buyer. Larger user do get benefits of CST | Larger user do not get benefits of CST | There are various service sectors such as banking & insurance, hospitality & leisure, education, and so on, that are large consumers, but do not currently qualify for the beneficial rate of 3% CST. They should be allowed the same benefit. | **Positive.** It will boost the sales and increase PC penetration. Large user industry will benefit. Large penetration will also be beneficial to companies dealing in maintenance contracts |
| The IT hardware industry including the PC industry currently needs a stable environment to thrive and the government can provide this by avoiding any short-term reforms in the current duty structure | Uncertainty in reforms | Changes in the duty structure should be proposed only once the government has finalised a long-term fiscal framework | Industry will be in a better position to grow and thrive once it has proper policy framework |

## Pharmaceuticals

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Research and development (R&D) | Weighted deduction of 150% on R&D expenditure incurred up to March 31, 2012 is available for in-house R&D facility. | Extension of the benefit for five more years beyond March 31, 2017. An increase in the weighted deduction from 150% to 200%. | It would induce pharmaceutical companies to invest more in discovery R&D. It would also increase India's attractiveness as a global R&D hub. |
| | The weighted deduction of 150% is only available for incidental R&D expenses incurred at manufacturing facility | Expand the scope of the weighted deduction to encompass all expenditure on basic research carried out at any standalone R&D facility, as also clinical trials, bioequivalence studies that are done outside the R&D facility, whether in India or abroad | It will be beneficial for pure R&D companies like SPARC and the demerged R&D entities of Nicholas, Wockhardt and Ranbaxy |
| | ANDA filing expenses and cost of filing patents are not eligible for weighted deduction | ANDA filing expenses and patent filing costs should become eligible for weighted deduction | This would benefit players like Ranbaxy, Dr Reddy, Lupin, Sun Pharma, Nicholas Piramal and Aurobindo Pharma, which have high ANDA filing costs |
| Excise duty | Levy of excise duty at the rate of 16% on the MRP with an abatement of 42.5% | Elimination of excise duty on 354 drugs specified in the national list of essential medicines | Elimination of excise duty on the 354 essential drugs is less likely, as it will have revenue implications for the government. However, if it does happen, the cost savings will be passed on to the consumer and hence will not have any impact on pharmaceutical companies. |
| | - | For all other drugs, reduction of excise duty to 8% and/or an increase in the abatement to 55% | If it does happen, it will lower the cost of drugs for consumers and thus may spur an increased offtake in volumes<br>If the proposal passes, it will result in a more level playing field for smaller players like Ajanta Pharma and Zandu Pharma, who have no presence in excise-exempt areas |
| Custom duty | Customs duty in the range of 5-10% is levied on life saving drugs | Life saving drugs to be exempted from customs duty. | If passed, life saving drugs will become more affordable. It might lead to an increased offtake for MNC players like GSK, Novartis and Aventis. |
| Income tax | Tax exemption for the profits of a 100% export oriented unit (EOU) u/s. 10B is available only April 2009 | Tax exemption should be extended beyond April 2009 | It is likely for the exemption to be extended to provide some relief to the export oriented sectors (like IT and pharma), which have been reeling under the pressure of the rising rupee. If the exemption is extended beyond FY2010, it will have a positive impact on companies like Cipla, Orchid. |

**Contd...**

## Pharmaceuticals (contd...)

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| | Tax exemption for the profits of a scientific R&D company u/s 80IB stands expired as of March 2007 | The tax exemption should be extended for an additional five-year period | This benefit is likely to get extended in order to promote research on NCE/NDDS. It will be beneficial for companies with high spending on innovative research. |
| | Income from royalty/fees for technical know-how related to IPR development is fully taxable | There should be some provision for deduction/tax exemption on income from royalty/fees for technical know-how related to IPR development | This proposal is likely to get passed and will be positive for companies with strong focus on IPR development like Glenmark and Lupin |
| Infrastructure status for healthcare industry | - | In view of the burgeoning demand and the rising cost of health services, the healthcare industry should be granted 'infrastructure status'. This will enable them to avail related tax holidays and exemptions. | If implemented, it is likely to be beneficial for companies like Apollo Hospitals, Fortis Healthcare, Max Healthcare and Wockhardt hospitals, as it will not only enable them to avail of tax benefits but also provide finance for capital expenditure at lower interest rates. |

## Real estate

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Dividend on REITs | Unclear in SEBI's REITs proposal document | Should be tax free in the hands of unit holders in line with mutual fund unit holder | **Positive:** would channelise funds from retail investors into the sector |
| Reclassification of bank financing norms for SEZ projects | Commercial real estate project financing | Infrastructure project financing | **Positive** for Mahindra Lifespace Developers |
| Concession on group housing projects | No incentives | Financing for these projects should be made available easily and exemption on excise, custom, VAT and service tax on building material and services for these projects should be provided | **Positive** for the companies having presence in middle income housing |
| Section 80 IB | Available for projects approved before March 31, 2007 | Renewal of 80 IB benefits | **Positive** for the companies having presence in middle income housing |
| Service tax on residential units | Service tax of 12% is levied on the value addition by the developer based on the cost of land and construction material | To scrap 12% service tax on residential units | **Positive** for the sector |
| Uniformity in stamp duty | Different rate in different states | Uniform stamp duty across states | **Positive:** This will remove hurdle for real estate Mutual Fund and will provide another financing avenue for the sector |

## Telecom

| Issue | Current status | Proposal/Likely changes | Impact |
|---|---|---|---|
| Licence fee as revenue share | Revenue share is based on category of circle: 10% for metros, 8% for category A circles and 6% for category B circles | Reduce to a uniform rate of 6% across circles | **Positive** for all private sector telecom operators like Bharti Airtel, Reliance Communications and Tata Teleservices. It is a long-awaited demand from the industry |
| Multiple levy structures | Presently the sector suffers from multiple taxes in the form of 12% service tax, 6-10% license fee, 2-6% spectrum charges, and 2% education cess | Adopt a single levy structure | **Positive** for all private sector telecom operators as this would reduce ambiguities that form part of multiple levy structures |
| Excise duty on Internet/ Broadband data card | Excise duty of 16% applicable | Reduce excise duty to 8% | **Positive**—would further increase subscriber penetration, as the benefits are likely to be passed on to end users, resulting in affordable internet usage |
| Corporate tax | Benefits under section 80IA applicable for five years. | Extend the benefits under section 80IA for additional five years. Further, section 80IA benefits should be made available to companies undergoing amalgamation or demerger after March 31, 2007 | **Positive**—would reduce tax burden on private telecom operators for another additional years. Applicability to amalgamated or demerged companies would increase M&A activities within the sector |

The author doesn't hold any investment in any of the companies mentioned in the article.

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