Macquarie
Equities Research

The Asia Specialist

## INDIA

### Stock impact

**Stocks impacted**

| Sector | Positive | Negative |
|---|---|---|
| Banks | AXSB, BOB, PNB, SBIN, BOI, RCFT, IDFC | |
| Oil& Gas | CAIR, ONGC | RIL, BPCL, HPCL |
| Infrastructure | BHEL IN, LT IN, IVRC IN, NJCC IN, ABB IN, SIEM IN, CRG IN, JPA IN, PEC IN | |
| Commodities | SESA | STLT |
| Consumer | HUL | ITC, |
| Power | | TPWR IN, RPWR IN, ADANI IN |
| Auto | TTMT IN, MSIL IN, AL IN | |
| Pharma | RBXY IN, DRRD IN, SPADV IN, | |

Source: Macquarie Research, February 2010

### Top picks

| Ticker | Rec. | Price (Rs) | TP (Rs) | Upside |
|---|---|---|---|---|
| AXSB | OP | 1,125 | 1,220 | 8% |
| DRRD | OP | 1,142 | 1,440 | 26% |
| GAIL | OP | 399 | 506 | 27% |
| JSP | OP | 632 | 943 | 49% |
| LT | OP | 1,564 | 1,825 | 17% |
| TCS | OP | 762 | 925 | 21% |

Source: Macquarie Research, February 2010

### Least preferred

| Ticker | Rec. | Price (Rs) | TP (Rs) | Upside |
|---|---|---|---|---|
| BJAUT | UP | 1,818 | 1,400 | -23% |
| IDEA | UP | 61 | 35 | -43% |
| SBI | UP | 1,974 | 1,750 | -11% |

Source: Macquarie Research, February 2010

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# India budget review

## Delivering on expectations and more

### Event

- **7 out of 10:** The Union Budget of FY11 exceeded our (admittedly moderate) expectations. While the steps for fiscal consolidation and reversal of stimulus announced were modest, the broad trajectory of reforms is encouraging. Overall, we would rate the budget 7/10 and would have appreciated a more aggressive reversal of the stimulus measures.

### Impact

- **Realistic fiscal consolidation targets**. The budget deficit target for FY11 is 5.5% (including previously off-budget subsidies), as expected. Government borrowings (pegged at Rs3.45tn) are in line with our expectations and go some way in reducing concerns on the crowding out of private investments.
- **Infrastructure** was a key focus area once, with planned expenditure for the sector up 17% YoY, and accounts for 46% of total planned expenditure. On the funding side, the disbursement targets for IIFCL have been nearly doubled, and a Rs20,000 additional tax deduction limit for investing in infra bonds will help channel greater savings into the sector. Stocks to play **LT, IVRC, NJCC**.
- **Banking** sector gains, with crowding out concerns abating. While the nudge to RBI for giving out more licences is more a long-term play, in our view, the extension of the farm loan waiver repayment period and the infusion of more capital in weakly capitalised banks would have a more immediate impact, with SOE banks the major beneficiaries (**AXSB** and **BOB** are our top picks).
- **Petroleum** sector saw disappointment as Dr. Kirit Parikh's committee report is to be taken up separately (usually the case with large reforms). We see **Cairn India** as the **clear beneficiary**, with an ~8% gain in profits on the re-introduction of a 5% import duty on crude oil. **RIL** would be **hit on two fronts** as import duty changes of ~2.5% reduce profits as does a 3% increase in MAT.
- **Consumer, Auto and Basic Materials** benefits from higher demand, given the increased disposable income from reduced direct taxes, and offsets the impact of the excise duty increase. The surprise came in higher than the increase in the excise duty on tobacco. We have a **positive** outlook for **Maruti** and **HLL**, and a **negative** outlook for **ITC**.
- The increased deduction for R&D expenses is **positive** for the Pharma sector, as it moves from generic to product development. **DRRD** remains a top pick.
- **Major reforms outside of budget.** GST and Direct tax code implementation from Apr2011, Change in fertiliser subsidy mechanism, Appointment of Coal Regulatory Authority, etc. are some of the reforms indicated for implementation. We have a positive outlook for **JSP** and **Sterlite**.

### Outlook

- **Remain positive:** Overall we continue to be positive in our view on the Indian economy and its pass through to corporate profitability. Our **top picks** are GAIL, JSP, TCS, DRRD, Axis Bank, and LT. Our **least-preferred** stocks are IDEA, BJAUT, and SBI.

## Economics view: Budget FY11 - Adopting a disciplined approach

The Indian government announced a budget that focuses on fiscal consolidation, while ensuring higher spending in the right areas, such as infrastructure (rural and urban), and promoting more financial inclusion and a social safety net. The Budget measures hint that the government is keen to ensure that economic growth picks up further in a sustained manner and becomes more inclusive, and is responsible in dealing with the existing fiscal pressures.

It is also a budget that shows the real thinking of Prime Minister Manmohan Singh's government: it realises that the economic pie has to grow faster to generate resources for its redistributive policies, and the government seems mindful of the importance of avoiding crowding out of private investment.

The Budget focuses on three key issues: (1) gradual withdrawal of stimulus measures; (2) cutting the fiscal deficit and signalling fiscal consolidation; and (3) guidance on the implementation of some key fiscal reforms such as the goods and service tax (GST), the direct tax code, and scaling back of oil and fertilizer subsidies. The budget spends on key areas such as social and physical infrastructure, and also understandably enhances the redistributive landscape of the government, but it does so in a responsible manner by cutting the fiscal deficit.

Overall, we would rate the budget 7/10. A more aggressive reversal of the stimulus measures, which, given the underlying impressive pace of recovery, could have been absorbed, would have earned the government a higher score. The budget should ease concerns over India's fiscal dynamics, and it further solidifies our conviction over the emerging growth acceleration toward 8-9% over the next 2-3 years.

The key macro takeaways are as follows:

**Fiscal deficit and consolidation:** Most important, the government is positioning in FY11 to cut the fiscal deficit without hurting growth. The federal fiscal deficit is forecast at 5.5% of GDP, down from a revised 6.7% of GDP (6.9% including off-budget subsidies) for FY10.

Importantly, we believe the FM has undertaken a significant step by doing away with the below-the-line items such as off-budget bonds for state-owned oil and fertilizer companies. Thus, the revised estimate for the fiscal deficit at 6.9% in FY10 includes the off-budget subsidy to oil and fertilizer companies, and should be correctly compared to a deficit of 7.8% (inclusive of off-budget subsidies) in FY09.

Total spending is forecast to increase 8.6% over FY10BE (budget estimate), owing to a 15% increase in Plan Expenditure and only a 6% increase in non-plan Expenditure. Actual infrastructure spending should be higher than the overall increase in Plan Expenditure.

The tax revenue assumptions appear realistic, and the **divestment** has been assumed at Rs400bn. The key on divestment is how well the government will handle the execution.

**Government borrowing:** Equally important, the FY11 net government borrowing of Rs3.45trn (FY10: Rs3.98trn) is along expected lines and prompted a sigh of relief from the bond market. Gross borrowing is pegged at Rs4.57trn, owing to sizeable redemptions in the next fiscal year.

**Fig 1 India: federal government finances**

| % of GDP, FY end Mar | 2008-2009 Actuals | 2009-2010 BE | 2009-2010 RE | 2010-2011 BE |
|---|---|---|---|---|
| 1. Revenue Receipts | 9.7 | 10.0 | 9.4 | 9.8 |
| 2. Tax Revenue (net to Centre) | 8.0 | 7.7 | 7.5 | 7.7 |
| 3. Non-tax Revenue | 1.7 | 2.3 | 1.8 | 2.1 |
| 4. Capital Receipts (5+6+7)$ | 6.2 | 6.6 | 7.2 | 6.2 |
| 5. Recoveries of Loans | 0.1 | 0.1 | 0.1 | 0.1 |
| 6. Other Receipts | 0.0 | 0.0 | 0.4 | 0.6 |
| 7. Borrowings and other | 6.0 | 6.5 | 6.7 | 5.5 |
| Liabilities* | 0.0 | 0.0 | 0.0 | 0.0 |
| 8. Total Receipts (1+4)$ | 15.9 | 16.6 | 16.6 | 16.0 |
| 9. Non-plan Expenditure | 10.9 | 11.3 | 11.5 | 10.6 |
| 10. On Revenue Account of which | 10.0 | 10.0 | 10.4 | 9.3 |
| 11. Interest Payments | 3.4 | 3.7 | 3.6 | 3.6 |
| 12. On Capital Account | 0.9 | 1.2 | 1.0 | 1.3 |
| 13. Plan Expenditure | 4.9 | 5.3 | 5.1 | 5.4 |
| 14. On Revenue Account | 4.2 | 4.5 | 4.3 | 4.5 |
| 15. On Capital Account | 0.7 | 0.8 | 0.8 | 0.8 |
| 16. Total Expenditure (9+13) | 15.9 | 16.6 | 16.6 | 16.0 |
| 17. Revenue Expenditure (10+14) | 14.2 | 14.6 | 14.7 | 13.8 |
| 18. Capital Expenditure (12+15) | 1.6 | 2.0 | 1.9 | 2.2 |
| 19. Revenue Deficit (17-1) | 4.5 | 4.6 | 5.3 | 4.0 |
| **20. Fiscal Deficit** {16-(1+5+6)} | **6.0** | **6.5** | **6.7** | **5.5** |
| 21. Primary Deficit (20-11) | 2.6 | 2.8 | 3.2 | 1.9 |

1. BE; Budget Estimate; RE: Revised Estimate
2. FY11E of nominal GDP is government's assumption of an increase of 12.5%
3. Fiscal deficit for FY 11 will not have any explicit off-budget subsidy bonds. Note that the fiscal deficit for other years excludes issuances of special bonds to oil/food/fertiliser companies amounting to 0.8% of GDP in FY08, 1.8% in FY09 and 0.2% in FY10

Source: CEIC, MoF, Macquarie Research, February 2010

**Direct tax changes:** The key positive surprise here was the broadening of the current personal income tax slabs, which will favourably affect discretionary consumer spending. The government also announced an unexpected cut in the surcharge on domestic companies to 7.5% from 10%.

On the negative side, it increased the minimum alternate tax (MAT) to 18% from 15% of book profit to promote equity among corporate taxpayers.

**Indirect tax changes:** The increase in excise duty to 10% from 8% was widely anticipated. The excise on smoking and non-smoking tobacco has been increased. The government is restoring the basic duty of 5% on crude petroleum, 7.5% on diesel and petrol, and 10.0% on other refined products. Also, the Central Excise duty on petrol and diesel has been increased by Re.1 per litre each. These changes will push up inflation in the near term but is a small price to pay to gradually wean off subsidies that are unsustainable.

Overall, the budget for FY11 signals the start of a gradual improvement in India's fiscal dynamics, driven by a combination of the cyclical upswing and implementation of some key fiscal reforms. The Budget should further ease concerns over India's fiscal dynamics. The next step is going to be the implementation of GST and the Direct Tax Code that should come into play from 1 April 2011. More details on these and on further subsidy reforms are likely over the course of the year. The government will likely move gradually, at best.

### Fig 2 Tax and non tax revenue

| | 2008-2009 | 2009-2010 | 2009-2010 | 2010-2011 |
|---|---|---|---|---|
| Rs bn, FY end Mar | Actual | BE | RE | BE |
| REVENUE RECEIPTS | | | | |
| 1. Tax Revenue | | | | |
| Gross Tax Revenue | 6053 | 6411 | 6331 | 7467 |
| Corporation tax | 2134 | 2567 | 2551 | 3013 |
| Income tax | 1060 | 1129 | 1250 | 1206 |
| Other taxes and Duties* | 149 | 4 | 69 | 81 |
| Customs | 999 | 980 | 845 | 1150 |
| Union Excise Duties | 1086 | 1065 | 1020 | 1320 |
| Service Tax | 609 | 650 | 580 | 680 |
| Less States' Share | 1602 | 1644 | 1648 | 2090 |
| Centre's Net Tax Revenue | 4433 | 4742 | 4651 | 5341 |
| 2. Non -Tax Revenue | | | | |
| Interest Receipts | 207 | 192 | 192 | 193 |
| Dividend and Profits | 386 | 498 | 520 | 513 |
| External Grants | 28 | 21 | 31 | 21 |
| Other Non-Tax Revenue | 340 | 685 | 368 | 746 |
| Receipts of Union Territories | 8 | 8 | 11 | 9 |
| Total Non-Tax Revenue | 969 | 1403 | 1122 | 1481 |
| Total Revenue Receipts | 5403 | 6145 | 5773 | 6822 |

* Includes Wealth Tax, Securities Transaction Tax and Banking Cash Transaction Tax in RE 2009-10; and Wealth Tax and Securities Transaction Tax in BE 2010-11

BE; Budget Estimate; RE: Revised Estimate

Source: CEIC, MoF, Macquarie Research, February 2010

## Fig 3 Sectoral impact

| Event | Vs Expectation | Impact | Companies Affected: Positively – Bloomberg Code | Companies Affected: Positively – Impact on Earnings | Companies Affected: Negatively – Bloomberg Code | Companies Affected: Negatively – Impact on Earnings |
|---|---|---|---|---|---|---|
| **Auto** | | | | | | |
| Excise duty hiked to 10% from 8% and from 20% to 22% for large cars | Neutral | Largely neutral as this was well expected by the markets | | | AL IN, BJAUT IN, HH IN, MSIL IN, MM IN, TTMT IN | |
| Weighted deduction for R&D increased to 200% from 150% | Positive | The deduction should help companies with relatively large R&D spend to lower taxes and thus improve profitability | TTMT IN, MSIL IN, AL IN | | | |
| Increased tax slabs for direct taxes | Positive | This will increase disposable income for consumers and can thus lead to higher demand for 2Wheelers and car space | HH IN, BJAUT IN, MSIL IN, TTMT IN (car space) | | | |
| Petrol and Diesel levy increased by Rs1 per litre. | | While this increases the cost of ownership, it is unlikely to have strong negative impact in the near term on auto demand | | | AL IN, BJAUT IN, HH IN, MSIL IN, MM IN, TTMT IN | |
| Six months extension for farm loan payment, increased interest subvention for timely payment from 1% to 2% and increase in rural spending including National Rural employee guarantee scheme | | Should result into better than expected income in hands of rural population which is positive for M&M, Hero Honda and Maruti in that order. | MM IN, HH IN, MSIL IN | | | |
| Kirit Parikh committee recommendation to be considered later, nothing to be implemented immediately | Neutral | This is positive for diesel car/ UV manufacturers as the committee had proposed special excise of Rs80,000 per vehicle. | MM IN, TTMT IN, MSIL IN | | | |
| **Banks** | | | | | | |
| Fiscal deficit/ borrowings within expectations | Neutral | Largely along expected lines. However positive for the sector as the negative overhang due to potentially large government borrowings gone, reducing crowding out concerns somewhat. | All banks | | | |
| Rs20,000 tax deduction limit for retail investors for buying infrastructure bonds | Positive | Positive for banks, IDFC, PFC. Will increase appetite for infra bonds and reduce ALM mismatch for banks. | Positive for sector | | | |
| Extension of period for the repayment of the farmer's portion in the farm debt waiver scheme by 6 months (from Dec 09 previously) | Positive | Positive for the state banks which would otherwise have taken a hit on their asset quality. In fact BOB and PNB had already recognised loans as NPLs which they will now likely reverse. | State owned banks - SBIN, BOB, BOI, PNB | | | |
| RBI to consider banking licences for private players, NBFCs | Long term positive | Long term positive for the sector. However, likely to be a long-term project involving decision on giving concessions (if any) in terms of CRR/SLR for the new players. Also it would be time before any new players develop a branch network large enough to become serious players. For NBFCs, given the comfortable liquidity and rising regulatory forbearance for banks (CRR/SLR), the short term incentives are much reduced from the peak of credit crunch. | RCFT | | | |
| Rs165bn to be infused as tier I Capital for banks | Positive | Positive for SOE banks which were in need of | IDBI, SNDB, | | | |

## Fig 3 Sectoral impact

| Event | Vs Expectation | Impact | Companies Affected | | | |
|---|---|---|---|---|---|---|
| | | capital. Although the quantum of individual injection is still to be decided and may fall short of what banks want. | VJYBK | | | |
| **Basic Materials** | | | | | | |
| Imposition of Rs50/t cess on coal | Negative | Very small to really make any impact here. | | | | |
| Increase in Excise duty from 8% to 10% | Negative | While this is negative but was very well anticipated. Given that for most large buyers of metal get modvat credit, it is a pass through for them, we see it getting passed on to the actual consumer and should not impact metal companies. More so that it has come during busy season makes it pretty easier. | | | No major loser here | |
| Increase in MAT from 15% to 18% | Negative | The MAT rate has been increased from 15% to 18% while surcharge has been reduced from 10% to 7.5%. While this negatively impacts the power companies like Jindal Power and Sterlite Energy in our space as tax increases by 180bps, but the parent company benefits due to reduction in surcharge, the impact on consolidated earnings are limited to 1-2%. | | | JSP IN, STLT IN | ~1-2% |
| No increase in export duty for Iron Ore | Positive | No increase in export duty of iron ore or imposition of any special duty will ensure that iron ore exports from India remain competitive | SESA IN | | | |
| Formation of Coal regulatory Authority: | Positive | This is to provide a level playing field for coal resource allocation. Can benefit companies like Sterlite who are struggling to get coal resources inspite of being so well advanced in their projects. | | | STLT IN | |
| **FMCG** | | | | | | |
| Hike in cigarette excise duty - 11-18% | Higher than mkt expectations of 6-8%, | ITC had taken some price hike recently in anticipation of excise hike. We believe volumes will be hit especially if the states also increase the VAT rates. | | | ITC | ~5% |
| Excise duty hike of 18% on less than 60mm | Higher than expected | Due to the large cut in excise duties on less than 60mm cigarettes, ITC may enter that size (filter/non-filter) which it had exited 2 years back. ITC will launch cigarettes at low price points, where conversions from illegal cigarettes and other cheaper alternatives are likely to happen. | ITC | | | |
| Excise duty hike by 2% | In line with expectations | Marginal impact, if any. Companies will be able to pass the 2% hike. | | | HUL, DABUR, MRCO, GCPL | Less than 1% |
| Changes in personal income tax slabs | Positive surprise | It will increase the disposable cash in the hands of consumers. Likely to boost consumption growth. | HUL, ITC, DABUR, MRCO, GCPL, NEST | Positive bias over a long term time frame | | |
| Focus on growth in agriculture sector, farm loan interest subsidies, increased allocation under rural employment guarantee scheme | In line with expectations | Indirect benefits for income levels- primarily in rural areas | ITC,MRCO, HUL, DABUR | Positive bias over a long term time frame | | |
| MAT increased from 15% to 18% | Unexpected | The cash component of taxes paid would go up. Accounting taxes would not change materially | | | DABUR, HUL | ~2% |

## Fig 3 Sectoral impact

| Event | Vs Expectation | Impact | | Companies Affected | |
|---|---|---|---|---|---|
| Excise Impact on Cigarette | | | | | |
| Non-filter | Excise duty hike | Contribution to ITC's existing volumes | | | |
| Less than 60mm | -18% | 0% | | | |
| 60-70mm | +11% | 0% | | | |
| Filter | Excise duty hike | | | | |
| Less than 60mm | -18% | 0% | | | |
| 60-70mm | +18% | 82% | | | |
| 70-75 | +11% | | | | |
| 75-85 | +11% | 7% | | | |
| Others | +9% | 11% | | | |
| **Infrastructure** | | | | | |
| Investment limit hiked for individuals. Additional Rs20,000 allowed to be invested in infra bonds | positive | This would help attracting funds into the infra space | Entire infra space | | |
| IIFCL (India Infrastructure Finance Company ltd) re-financing budget doubled. IIFCL disbursement target increased to Rs200bn from Rs110bn earlier | positive | This would allow banks to lend to infra sector without being too concerned on asset-liability mismatch. | Entire infra space | | |
| 13% increase in National Highway Development Programme (NHDP) | positive | Investment in roads sector would get further boost. This adds to the viability gap funding pool. However, given the projects are on PPP (Public-Private-Partnership) model, equity and debt financing would still have to be arranged by developers | IVRC IN, NJCC IN, LT IN, HCC IN, PEC IN | | |
| Surcharge reduced | positive | Full tax rate to reduce to 33.21% from 33.9% | BHEL IN, LT IN, IVRC IN, NJCC IN, ABB IN, SIEM IN, CRG IN, JPA IN, PEC IN | | |
| Excise duty reduced on CFL from 8% to 4% | positive | Impact on Compact Fluorescent Lamp manufacturers | CRG IN, HAVL IN | | |
| Customs duty reduced on motor equipment for wind | positive | Input cost for wind equipment manufacturers to reduce | SUEL IN | | |
| Road equipment import norms eased | positive | Positive for contractors - Given that the equipment is not sold within 5 years | NJCC IN, IVRC IN, HCC IN, PEC IN | | |
| Monorail customs duty reduced | positive | Reduced to 5% - small positive | LT IN | | |
| Clean energy fund | positive | Not a huge positive as this fund would only be used for research and not as additional equity contribution to wind sector | SUEL IN, MBI IN | | |
| Outlay for Ministry of New and Renewable energy increased to Rs 10bn (+61%) | positive | This would have huge focus on solar energy | MBI IN | | |
| Effective MAT rate increased from 17% to 19% | negative | Effective tax rate for infra developers to go up | | GMRI IN, GVKP IN, Other infra developers | |
| **IT** | | | | | |
| MAT rate increase from 15% to 18% | Negative | MAT rate increase is NEGATIVE for IT services companies, who currently pay MAT. Smaller IT companies currently enjoy lower tax rate vs. Tier 1 companies and hence this is more negative for them. | | INFO IN, TCS IN, WPRO IN | Less than 1% impact on EPS. |
| No Extension of STPI sunset clause | Neutral | This was expected and hence is not a negative | | | |

## Fig 3 Sectoral impact

| Event | Vs Expectation | Impact | Companies Affected | | | |
|---|---|---|---|---|---|---|
| | | surprise | | | | |
| Service tax rate maintained at 10% | Positive | This is positive vs. market expectation of service tax increasing to 12%. | INFO IN, TCS IN, WPRO IN, FSOL IN | Minimal since revenues from India contributes less than 10% to top-line. | | |
| Telecom | | | | | | |
| MAT rate increase from 15% to 18% | Negative | Negative for the sector | | | RCOM IN, Bharti IN | |
| Diesel Price hike | Negative | Since the rural base station operates on diesel. Price hike will negatively impact the sector and increase their network opex. | | | RCOM IN, Bharti IN, IDEA IN | |
| | | | | | | |
| **Oil & Gas** | | | | | | |
| Re-introduction of 5% import duty on crude oil | Positive | 5% higher landed cost of imports benefits especially Cairn India. Similar large subsidy benefit to ONGC and OIL may be partially diluted due to corresponding rise in subsidy. | CAIR IN, ONGC IN, OINL IN | +10% CAIR, +8% ONGC. | | |
| 5% import duty increase on ~3/4ths of petroleum products including petrol & diesel. However, naphtha, LPG, LNG, petroleum gases and pet coke duty continues at 5% | Negative | As duty has been hiked by 5% on 3/4ths of products, while input crude oil has also increased the net impact should be a ~US$ 0.5/bbl fall in domestic GRMs | | | RIL IN, BPCL IN, BPCL IN, IOCL IN | -2.5% RIL |
| Kirit Parikh committee recommendations implementation shall be examined separately. Petrol & diesel prices increased by Rs 2.71 and 2.55/litre respectively after budget, compared to a Rs 1/litre increase in excise duty | Mixed | Major reforms rarely implemented in budget, but some investors expected otherwise. Price hikes exactly offsets hike in excise and increase in petrol and diesel due to 5% rise in refined products. Negative margin for diesel at Rs 5.3/litre and petrol at Rs 5.8/litre remains. | | | BPCL IN, HPCL, IOCL IN | |
| Increase in Minimum Alternate Tax (MAT) from 15% to 18% | Negative | ~3% reduction in RIL's earnings as tax rate is typically at MAT. Cairn's earnings would be hurt in the first couple of years of Rajasthan oil production start-up | | | RIL IN, CAIR IN | -3% RIL, -2.4% CAIR |
| | | | | | | |
| **Pharma** | | | | | | |
| Increased weighted deduction on expenditure incurred on in-house R&D from 150 per cent to 200 per cent. | Positive | Pharma Companies have on an average R&D expenses of 5% of Net Sales and increasing the weighted deduction to 200% will positively impact earnings by 1-1.5% | RBXY IN, DRRD IN, SPADV IN, | Positive Impact on EPS by 1-1.5% | | |
| Input duty on drugs increased by 2% | Neutral | We believe the companies have pricing power to pass on the increased excise duty to customers | | | | Across Sector |
| MAT rate increased from 15% to 18% and Surcharge decreased from 10% to 7.5%. Effectively the MAT tax rate would increase 290bps to 19.9% from 17% earlier | Marginally Negative | Negatively impact earnings of companies under MAT taxation | | | PIHC IN, JOL IN | Negative impact on earnings depending on the revenue from manufacturing facilities which come under MAT |
| | | | | | | |
| **Power** | | | | | | |
| Clean energy cess on coal produced in India at a nominal rate of Rs.50 per tonne. This cess will also apply to imported coal. | Negative | Will Negatively Impact EPS | | | TPWR IN, RPWR IN, ADANI IN | Negative Impact on EPS |
| MAT rate increased from 15% to 18% and Surcharge decreased from 10% to 7.5%. Effectively the MAT tax rate would increase | Negative | Negatively impact earnings of Power station under MAT taxation | | | Across Sector | Negative impact on EPS |

## Fig 3 Sectoral impact

| Event | Vs Expectation | Impact | Companies Affected | |
|---|---|---|---|---|
| 290bps to 19.9% from 17% earlier | | | | |
| | | | | |
| **Property** | | | | |
| Interest subvention for affordable housing projects | positive | Extends 1% interest subsidy till 2011 on home loans for housing projects of up to Rs2m | DLFU IN, UT IN | |
| Extension of 1 yr for completion of housing projects which claimed for tax holiday under Section 80-IB (10) | positive | Extension of 1 yr will allow these projects to get completed, which was affected due to slowdown in FY09. | DLFU IN, UT IN | |
| Focus on urban development (e.g. allocation under Urban Renewal Mission increased) | positive | Indirect benefits for development of infrastructure in urban areas, which help property demand | DLFU IN, UT IN, HDIL IN, IBREL IN, ARCP IN | Positive bias over a long-term timeframe |

Source: Company data, Macquarie Research, February 2010

### Fig 4 Coverage Universe

| Company Name | Reco | Bloomberg ticker | Price Target (Rs) | Price (Rs) | Upside | Analyst Name |
|---|---|---|---|---|---|---|
| Aban Offshore | Outperform | ABAN IN | 1,490 | 1,183 | 26% | Jal Irani |
| ABB India | Underperform | ABB IN | 484 | 795 | -39% | Inderjeetsingh Bhatia |
| Associated Cements | Neutral | ACC IN | 815 | 923 | -12% | Rakesh Arora |
| Ambuja Cements | Outperform | ACEM IN | 111 | 107 | 4% | Rakesh Arora |
| Ackruti City | Underperform | AKCL IN | 364 | 486 | -25% | Jal Irani |
| Ashok Leyland | Underperform | AL IN | 43 | 50 | -13% | Sanjay Doshi |
| Anant Raj Industries | Outperform | ARCP IN | 180 | 123 | 46% | Jal Irani |
| ICSA | Outperform | AURFI IN | 205 | 132 | 55% | Inderjeetsingh Bhatia |
| Axis Bank | Outperform | AXSB IN | 1,220 | 1,125 | 8% | Mudit Painuly |
| Bharti Airtel | Underperform | BHARTI IN | 280 | 279 | 0% | Shubham Majumder |
| Bharat Heavy Electricals | Neutral | BHEL IN | 2,488 | 2,349 | 6% | Inderjeetsingh Bhatia |
| Bajaj Auto | Underperform | BJAUT IN | 1,400 | 1,818 | -23% | Sanjay Doshi |
| Bank of Baroda | Outperform | BOB IN | 590 | 584 | 1% | Mudit Painuly |
| Bank of India | Underperform | BOI IN | 300 | 333 | -10% | Mudit Painuly |
| Bharat Petroleum | Outperform | BPCL IN | 695 | 564 | 23% | Jal Irani |
| Cairn India | Underperform | CAIR IN | 198 | 266 | -26% | Jal Irani |
| Cipla | Underperform | CIPLA IN | 275 | 316 | -13% | Abhishek Singhal |
| Crompton Greaves India | Outperform | CRG IN | 509 | 416 | 22% | Inderjeetsingh Bhatia |
| Dish TV India | Outperform | DITV IN | 55 | 37 | 48% | Nitin Mohta |
| DLF | Outperform | DLFU IN | 387 | 298 | 30% | Jal Irani |
| Dr. Reddy's Laboratories | Outperform | DRRD IN | 1,440 | 1,142 | 26% | Abhishek Singhal |
| GAIL India | Outperform | GAIL IN | 506 | 399 | 27% | Jal Irani |
| Glaxosmithkline Pharmaceuticals | Outperform | GLXO IN | 1,660 | 1,710 | -3% | Abhishek Singhal |
| GMR Infrastructure | Underperform | GMRI IN | 57 | 55 | 4% | Inderjeetsingh Bhatia |
| Gujarat NRE Coke | Outperform | GNC IN | 103 | 73 | 41% | Rakesh Arora |
| Grasim Industries | Outperform | GRASIM IN | 3,404 | 2,696 | 26% | Rakesh Arora |
| GVK Power and Infrastructure | Outperform | GVKP IN | 53 | 43 | 22% | Inderjeetsingh Bhatia |
| HCL Technologies | Underperform | HCLT IN | 93 | 367 | -75% | Nitin Mohta |
| Housing Development Finance Corp | Outperform | HDFC IN | 2,700 | 2,500 | 8% | Mudit Painuly |
| HDFC Bank | Neutral | HDFCB IN | 1,635 | 1,705 | -4% | Mudit Painuly |
| Housing Development and Infrastructure | Outperform | HDIL IN | 441 | 302 | 46% | Jal Irani |
| Hero Honda | Underperform | HH IN | 1,510 | 1,778 | -15% | Sanjay Doshi |
| Hindalco Industries | Outperform | HNDL IN | 170 | 163 | 5% | Rakesh Arora |
| Hindustan Petroleum | Outperform | HPCL IN | 460 | 347 | 33% | Jal Irani |
| Hindustan Zinc | Underperform | HZ IN | 1,029 | 1,124 | -8% | Rakesh Arora |
| Indiabulls Real Estate | Outperform | IBREL IN | 203 | 160 | 27% | Jal Irani |
| India Cements | Neutral | ICEM IN | 118 | 118 | 0% | Rakesh Arora |
| ICICI Bank | Underperform | ICICIBC IN | 700 | 872 | -20% | Mudit Painuly |
| IDBI | Underperform | IDBI IN | 70 | 119 | -41% | Mudit Painuly |
| Idea Cellular | Underperform | IDEA IN | 35 | 61 | -43% | Shubham Majumder |
| Infrastructure Development Finance Company | Underperform | IDFC IN | 125 | 160 | -22% | Mudit Painuly |
| Infosys Technologies | Outperform | INFO IN | 2,980 | 2,602 | 15% | Nitin Mohta |
| Indian Oil | Outperform | IOCL IN | 390 | 317 | 23% | Jal Irani |
| IVRCL | Outperform | IVRC IN | 436 | 322 | 35% | Inderjeetsingh Bhatia |
| Jaiprakash Associates | Outperform | JPA IN | 178 | 132 | 35% | Inderjeetsingh Bhatia |
| Jindal Saw Limited | Outperform | JSAW IN | 242 | 194 | 25% | Amit Mishra |
| Jindal Steel and Power | Outperform | JSP IN | 943 | 632 | 49% | Rakesh Arora |
| JSW Steel | Outperform | JSTL IN | 1,259 | 1,070 | 18% | Rakesh Arora |
| Kotak Mahindra Bank | Neutral | KMB IN | 825 | 744 | 11% | Mudit Painuly |
| Larsen & Toubro | Outperform | LT IN | 1,825 | 1,564 | 17% | Inderjeetsingh Bhatia |
| Mundra Port & Special Economic Zone | Outperform | MSEZ IN | 727 | 674 | 8% | Inderjeetsingh Bhatia |
| Maruti Suzuki India | Outperform | MSIL IN | 1,770 | 1,460 | 21% | Sanjay Doshi |
| MTNL | Underperform | MTNL IN | 47 | 72 | -35% | Shubham Majumder |
| National Aluminium Company | Underperform | NACL IN | 237 | 385 | -38% | Rakesh Arora |
| NTPC | Outperform | NATP IN | 258 | 203 | 27% | Adam Worthington |
| Nagarjuna Construction Company | Outperform | NJCC IN | 206 | 155 | 33% | Inderjeetsingh Bhatia |
| Oil and Natural Gas Corporation | Underperform | ONGC IN | 865 | 1,118 | -23% | Jal Irani |
| OnMobile Global | Outperform | ONMB IN | 700 | 370 | 89% | Shubham Majumder |
| Patel Engineering Company | Outperform | PEC IN | 552 | 426 | 30% | Inderjeetsingh Bhatia |
| Petronet LNG | Underperform | PLNG IN | 49 | 74 | -34% | Jal Irani |
| Punjab National Bank | Underperform | PNB IN | 650 | 901 | -28% | Mudit Painuly |
| Power Finance Corp | Outperform | POWF IN | 280 | 250 | 12% | Mudit Painuly |
| Provogue | Underperform | PROV IN | 45 | 49 | -9% | Amit Mishra |
| Punj Lloyd | Neutral | PUNJ IN | 200 | 175 | 14% | Inderjeetsingh Bhatia |
| Ranbaxy Laboratories | Underperform | RBXY IN | 380 | 470 | -19% | Abhishek Singhal |
| Reliance Capital | Outperform | RCFT IN | 1,014 | 786 | 29% | Mudit Painuly |

### Fig 4 Coverage Universe

| Company Name | Reco | Bloomberg ticker | Price Target (Rs) | Price (Rs) | Upside | Analyst Name |
|---|---|---|---|---|---|---|
| Reliance Communications | Underperform | RCOM IN | 160 | 158 | 2% | Shubham Majumder |
| Reliance Industries | Outperform | RIL IN | 1,250 | 979 | 28% | Jal Irani |
| Rolta India | Outperform | RLTA IN | 435 | 176 | 147% | Nitin Mohta |
| Steel Authority of India | Underperform | SAIL IN | 196 | 219 | -10% | Rakesh Arora |
| State Bank of India | Underperform | SBIN IN | 1,750 | 1,974 | -11% | Mudit Painuly |
| Siemens India | Underperform | SIEM IN | 438 | 684 | -36% | Inderjeetsingh Bhatia |
| Syndicate Bank | Underperform | SNDB IN | 41 | 84 | -51% | Mudit Painuly |
| Sterlite Industries | Outperform | STLT IN | 940 | 782 | 20% | Rakesh Arora |
| Suzlon Energy | Underperform | SUEL IN | 65 | 72 | -10% | Inderjeetsingh Bhatia |
| Sun Pharmaceuticals | Outperform | SUNP IN | 1,650 | 1,540 | 7% | Abhishek Singhal |
| Tata Steel | Outperform | TATA IN | 726 | 574 | 26% | Rakesh Arora |
| Tata Communications | Underperform | TCOM IN | 315 | 283 | 11% | Shubham Majumder |
| Tata Consultancy Services | Outperform | TCS IN | 925 | 762 | 21% | Nitin Mohta |
| Tata Power | Outperform | TPWR IN | 1,625 | 1,213 | 34% | Adam Worthington |
| Tata Motors | Outperform | TTMT IN | 826 | 711 | 16% | Sanjay Doshi |
| Union Bank of India | Underperform | UNBK IN | 225 | 256 | -12% | Mudit Painuly |
| Unitech Limited | Outperform | UT IN | 97 | 72 | 35% | Jal Irani |
| Ultratech Cements | Underperform | UTCEM IN | 831 | 1,040 | -20% | Rakesh Arora |
| Vijaya Bank | Underperform | VJYBK IN | 21 | 48 | -56% | Mudit Painuly |
| Welspun Gujarat Stahl Rohren | Outperform | WGS IN | 360 | 240 | 50% | Amit Mishra |
| Wipro | Outperform | WPRO IN | 800 | 678 | 18% | Nitin Mohta |
| Zee Entertainment Enterprises Ltd | Underperform | Z IN | 130 | 247 | -47% | Shubham Majumder |
| Zee News | Outperform | ZEEN IN | 73 | 56 | 29% | Nitin Mohta |

Prices as of 26 February, 2010.

Source: Bloomberg, Macquarie Research, February 2010

## Important disclosures:

### Recommendation definitions

**Macquarie - Australia/New Zealand**
Outperform – return >5% in excess of benchmark return
Neutral – return within 5% of benchmark return
Underperform – return >5% below benchmark return

**Macquarie – Asia/Europe**
Outperform – expected return >+10%
Neutral – expected return from -10% to +10%
Underperform – expected return <-10%

**Macquarie First South - South Africa**
Outperform – expected return >+10%
Neutral – expected return from -10% to +10%
Underperform – expected return <-10%

**Macquarie - Canada**
Outperform – return >5% in excess of benchmark return
Neutral – return within 5% of benchmark return
Underperform – return >5% below benchmark return

**Macquarie - USA**
Outperform (Buy) – return >5% in excess of Russell 3000 index return
Neutral (Hold) – return within 5% of Russell 3000 index return
Underperform (Sell)– return >5% below Russell 3000 index return

**Recommendations** – 12 months

**Note:** Quant recommendations may differ from Fundamental Analyst recommendations

### Volatility index definition*

This is calculated from the volatility of historical price movements.

**Very high–highest risk** – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.

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* Applicable to Australian/NZ/Canada stocks only

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Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives & hedging, IFRS impairments & IFRS interest expense
Excluded: non recurring items, asset revals, property revals, appraisal value uplift, preference dividends & minority interests

**EPS** = adjusted net profit / efpowa*
**ROA** = adjusted ebit / average total assets
**ROA Banks/Insurance** = adjusted net profit /average total assets
**ROE** = adjusted net profit / average shareholders funds
**Gross cashflow** = adjusted net profit + depreciation
*equivalent fully paid ordinary weighted average number of shares

All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).

### Recommendation proportions – For quarter ending 31 December 2009

| | AU/NZ | Asia | RSA | USA | CA | EUR | |
|---|---|---|---|---|---|---|---|
| Outperform | 47.94% | 60.52% | 37.50% | 43.42% | 65.26% | 41.60% | (for US coverage by MCUSA, 3.76% of stocks covered are investment banking clients) |
| Neutral | 35.58% | 18.70% | 53.13% | 49.06% | 29.11% | 36.80% | (for US coverage by MCUSA, 4.51% of stocks covered are investment banking clients) |
| Underperform | 16.48% | 20.79% | 9.38% | 7.52% | 5.63% | 21.60% | (for US coverage by MCUSA, 0.00% of stocks covered are investment banking clients) |

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| Justin Crawford (Asia) | (852) 3922 2065 |
| Peter Slater (Boston) | (1 617) 598 2502 |
| Jeffrey Shiu (China & Hong Kong) | (852) 3922 2061 |
| Thomas Renz (Geneva) | (41) 22 818 7712 |
| Andrew Mouat (India) | (9122) 6653 3200 |
| Stanley Dunda (Indonesia) | (6221) 515 1555 |
| Kenneth Yap (Indonesia) | (6221) 515 1555 |
| JJ Kim (Korea) | (822) 3705 8799 |
| Jason Lee (Malaysia) | (603) 2059 8888 |
| Gino C Rojas (Philippines) | (632) 857 0761 |
| Greg Norton-Kidd (New York) | (1 212) 231 2527 |
| Luke Sullivan (New York) | (1 212) 231 2507 |
| Scot Mackie (New York) | (1 212) 231 2848 |

### Regional Heads of Sales cont'd

| | |
|---|---|
| Sheila Schroeder (San Francisco) | (1 415) 835 1235 |
| Angus Kent (Thailand) | (662) 694 7601 |
| Michael Newman (Tokyo) | (813) 3512 7920 |
| Charles Nelson (UK/Europe) | (44) 20 3037 4832 |
| Rob Fabbro (UK/Europe) | (44) 20 3037 4865 |
| Nick Ainsworth (Generalist) | (852) 3922 2010 |

### Sales Trading

| | |
|---|---|
| Adam Zaki (Asia) | (852) 3922 2002 |
| Mike Keen (Europe) | (44) 20 3037 4905 |
| Yat Quan Tan (Hong Kong) | (852) 3922 2028 |
| Stanley Dunda (Indonesia) | (6221) 515 1555 |
| Michael Santos (Philippines) | (632) 857 0813 |
| Dominic Shore (Thailand) | (662) 694 7707 |

### Sales Trading cont'd

| | |
|---|---|
| Mario Argyrides (Korea) | (822) 3705 8610 |
| Edward Robinson (London) | (44) 20 3037 4902 |
| Matthew Ryan (Singapore) | (65) 6231 2888 |
| Isaac Huang (Taiwan) | (8862) 2734 7582 |
| Phil Sellaroli (Tokyo) | (813) 3512 7837 |

### Alternative Strategies

| | |
|---|---|
| Convertibles - Roland Sharman | (852) 3922 2095 |
| Depository Receipts - Robert Ansell | (852)3922 2094 |
| Derivatives - Wayne Edelist | (852) 3922 2134 |
| Futures - Tim Smith | (852) 3922 2113 |
| Structured Products - Andrew Terlich | (852) 3922 2013 |