Strategy Focus

COUNTRY RESEARCH

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India: Budget FY09

Stay Steady, Nudge Growth and Be Popular

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India Research Team

- **Balancing fiscal, consumption and election** – This budget looks fiscally ambitious, consumer and consumption oriented, and populist for the farmer. The overall package though, from an economic, political and market perspective, seems fairly balanced. It seeks to address flagging consumption – favors auto and consumer sectors and hurts banks – but is not decisive for market direction or level.

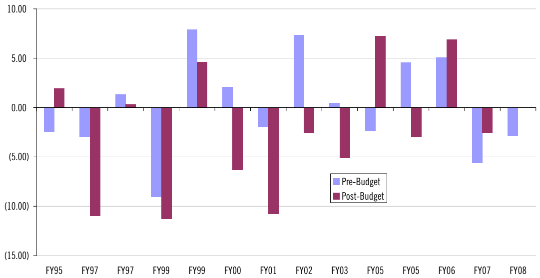
- **Fiscally ambitious, though there are a few gaps** – The budget appears fiscally conservative with targeted deficit of 2.5%, but is not necessarily so. Revenue numbers are conservative, but expenditure growth at only 6% is not, with no provision for likely costs on pay increases, farmer loan write-offs, and other subsidies. Effectively, while the fiscal direction is right, the level is probably not.

- **Consumption thrust the highlight** – Decisive consumption push: effective income tax rates for middle income lowered (through tax slab adjustments), indirect taxes on good reduced 1-2%, and car/scooters get hefty tax cut. This should bolster consumption in a large section of the populace, and an area of economic slack.

- **Agriculture loan waivers - populist and questionable** – The budget has proposed a significant farmer loan write-off – the scale is large (Rs600b), the financing and maths not clear (yet), and the risk to banks (earnings and policy) high. It is populist, but the moral hazard risk possibly bigger than the economic cost.

- **Capital gains tax hurts market, but not directional otherwise** – Higher short term cap-gains tax (10% to 15%) has colored market's reaction. More fundamentally, budget seeks to keep the ship steady, gives some growth nudges and be popular.

1 month Pre- and Post-Impact of the Budget on the Market—Sensex Returns



Source: Citi Investment Research

See Appendix A-1 for Analyst Certification and important disclosures.

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India Strategy

What does this budget seek to achieve? Balance and popularity

We had felt this budget would have its surprises and risks given general elections now around the corner, signs of growth easing and inflation rising, and a challenging political environment for the governing party that recently lost key state elections. As it turns out, the budget does have its surprises and carries its share of risks.

However, we believe the budget strikes a certain balance – is tilted towards populism, as it is to the right economics, and to some discipline on the fiscal side. Effectively, we believe it largely keeps the economy on track – does not do enough to move it into higher gear, nor does it do too much to derail it. Popular and reasonably practical.

What is the positive, who gains?

The positive is in its consumption thrust, achieved by a) Rationalizing income tax slabs which meaningfully lowers effective tax rates for large segments of the middle classes and a large consuming class; b) Cutting indirect taxes by 1%-2% (Central Sales Tax by 1%, CENVAT down from 16% to 14%); and c) Cutting excise duties on small cars/2 wheelers from 16% to 12%. We believe this is a focused measure – slackening consumption has been the weak point of the economy, and this measure is well targeted. We also believe this is the segment that is likely to spend the most as well as one of the most pressured in recent years by inflation. So while the measure could be interpreted as populist (a large voting segment), we see a strong economic rationale for it and a leg for broader economic growth.

We believe 2 wheeler (Bajaj Auto Hero Honda) and car manufacturers (Tata Motors), and consumer goods companies (HLL, ITC) are gainers.

What is the negative, who loses?

It's the big farmer loan write-off. The government has announced a loan write-off of about RS600b by the banks for small and marginal farmers who have defaulted. This is large (about 3% of system loans), likely to have a meaningfully positive social impact and should be popular. But we believe it could well carry longer-term moral hazard and economic costs that might well outweigh the near-term economic benefits. While the modalities of this announcement are not out yet, which could be a key determinant of its economics, this does appear more populist than economic. It also risks meaningfully impacting the fiscal deficit.

We believe the downsides of this measure lie with banks in the form of a) Economic cost – The government has suggested it will bear the cost, and banks will be compensated. There are no details yet, but even a part sharing of the costs will hurt banks; b) Moral hazard – With defaulters getting waivers, the rest of banks agricultural loan portfolios could be exposed; c) Perceived policy risk on banks could well be damaging for valuations. While banks stocks have bounced back after an initial slump, we believe this is an overhang. We think government bank stocks (State Bank of India, Punjab National Bank, Canara Bank) are most at risk.

Economics – Looks a little better than it is. We highlight this in a later section.

Not a market mover, though short-term capital gains hurt near term

We do not believe this budget, like some of its more recent predecessors, will meaningfully impact the market's direction or level. This is in part because a) The budget is a reflection of government finances, rather than meaningful policy directions; b) Tax structures have largely settled down; and c) There has been continuity of the government, and hence policies. In effect, the budget itself has focused on stability, a little rationalisation, and popularity. And the objective would appear to be to consolidate on the growth rates achieved, the tax momentum that has been established, and a level of stabilisation being witnessed in the government finances.

The market has, however, fallen largely on account of the short-term capital tax being raised to 15% (from 10%) against expectations. This hurts equity market participants, likely colors their judgment, but likely has little implications for long-term market or economic direction

In this report, we highlight sector specific changes, implication for businesses, and impact on stocks. In our view, the budget would have a positive impact on autos and pharma. Sectors that would be negatively impacted are public-sector banks and, marginally, cement. Impact on other sectors would be largely neutral.

India Economics

Budget FY09 – Provides an Impetus for Growth, though Certain Measures look Populist

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- **Budget – No real surprises:** With FY09 being a pre-election year, the budget contained no real surprises and increased outlays for agriculture, rural development, health and the education sector. Certain measures look populist e.g., the loan waiver/relief to farmers to the tune of Rs600bn, which could create the problem of moral hazard in future. However, the reduction in excise duty from 16% to 14%, coupled with the increase in exemption limits for personal income tax and the raising of tax slabs should spur growth. On the flip side, the increase in short-term capital gains tax from 10% to 15% caught the market by surprise.

- **FY08 Budget arithmetic excludes the off-balance-sheet items:** While the printed FY08 fiscal deficit number stands at Rs1,437bn or 3.1% of GDP – lower than targeted, as mentioned before, these do not include the various off-balance-sheet items (oil/food/fertiliser bonds). If added, the headline deficit number would be closer to 4.2% of GDP. However, what was encouraging was that the FM has finally acknowledged the need to bring these liabilities above the line in the fiscal accounting framework.

- **FY09 revenue and growth assumptions look realistic…**Going forward for FY09, the FM is targeting a reduction in the fiscal deficit to Rs1,332bn or 2.5% of GDP and the revenue deficit to Rs552bn or 1% of GDP. While this makes the fiscal deficit *"on paper"* is in line with the FRBM[1] targets, the revenue deficit is not. The budget assumptions are based on a nominal GDP growth of 13% (real GDP of 8.0%-8.5% and inflation of 4.5%-5.0%) and assume gross taxes rising by 17% v/s 24% seen in FY08. These we believe are realistic and achievable.

- **…but 6% expenditure increase looks a bit under-stated:** There are two key reasons for this: (1) There appears to be no provision for the recommendations of the **sixth pay commission** due next month which will be reviewing the salary structure of over 3m central government employees and will submit its report on March 31, 2008. It is reported that [2] implementation would involve an additional Rs200bn in pays and allowances. (2) There is a grey area on who will bear the cost of the proposed Rs600bn **loan waiver/relief to farmers**. While the budget has made no provisions of it, in a post budget interview, the FM has said that he would provide extra liquidity to banks over a period of ~3 years.

[1] Under the **FRBM Act,** beginning FY05, the central government has to reduce its fiscal and revenue deficit by 0.3% and 0.5% of GDP a year so as to eliminate the revenue deficit by 2009

[2] **A Pay Commission** is a body that is periodically constituted to examine pays and allowances, retirement benefits, conditions of service and promotion policies among other issues of central government employees. For details please see Economic Times dated 21 July 2006 'Centre okays Sixth Pay Panel'

Revenues…Budget measures should stimulate growth

The budget assumes gross taxes rising by 17.5% v/s 23.6% seen in FY08. This is based on income tax up16.9%, corporate taxes up21.6%, excise duties up 7.8%, customs duties up 18.0% and service tax up by 27.4%. These appear realistic.

Trends in Tax Revenues (Rs Bn, %)

	FY03	FY04	FY05	FY06	FY07	FY08RE	FY09BE
Corporation tax	462	636	827	1,013	1,443	1,861	2,264
% YoY	26.1	37.7	30.1	22.5	42.5	29.0	21.6
% to total taxes	21.3	25.0	27.1	27.7	30.5	31.8	32.9
Income tax	369	414	493	560	751	1,183	1,383
% YoY	15.2	12.3	19.0	13.6	34.1	57.6	16.9
% to total taxes	17.0	16.3	16.2	15.3	15.9	20.2	20.1
Excise duty	823	908	991	1,112	1,176	1,279	1,379
% YoY	13.4	10.3	9.2	12.2	5.7	8.8	7.8
% to total taxes	38.1	35.7	32.5	30.4	24.8	21.9	20.0
Customs collections	449	486	576	651	863	1,008	1,189
% YoY	11.4	8.4	18.5	12.9	32.7	16.7	18.0
% to total taxes	20.7	19.1	18.9	17.8	18.2	17.2	17.3
Service tax	41	79	142	231	376	506	645
% YoY	24.8	91.4	80.0	62.4	63.1	34.6	27.4
% to total taxes	1.9	3.1	4.7	6.3	7.9	8.6	9.4
Gross Tax Collections	**2,163**	**2,543**	**3,050**	**3,662**	**4,735**	**5,854**	**6,877**
% YoY	15.6	17.6	19.9	20.1	29.3	23.6	17.5
% to GDP	8.8	9.2	9.7	10.2	11.4	12.5	13.0
Net Tax Collections	**1,585**	**1,870**	**2,248**	**2,689**	**3,512**	**4,318**	**5,072**
% YoY	19.0	17.9	20.2	19.6	30.6	22.9	17.5
% to GDP	6.5	6.8	7.1	7.5	8.5	9.2	9.6

Source: Budget Documents

KEY MEASURES

Customs Duty: While the government has kept the peak customs duty unchanged at 10%, there have been sector specific reductions to provide a fillip to industries.

Excise Duties: In a bid to provide a stimulus to the manufacturing sector, the budget has reduced the CENVAT rate on all goods from 16% to 14%, while in certain sectors where growth is flagging the excise cuts have been greater. For autos, the excise duty has been lowered from 16% to 12% while in pharma from 16% to 8%.

Service Tax: The service tax remains at 12% but widened to include asset management services provided under ULIP to bring it on par with mutual funds.

Direct Taxes: While there is no change in corporate tax, the increase in basic exemption limit and tax slabs is a positive for consumption demand.

Income Tax Slabs: Old and Revised (Rs)

	OLD	NEW
Nil	0-110,000	0-1,150,000
10%	110,001-150,000	150,001-300,000
20%	150,001-250,000	300,001-500,000
30%	250,001+	500,001+

Source: Budget Documents

Capital Gains: The increase in short term capital gains tax from 10% to 15% was a bit of a disappointment to the markets.

Expenditure…Appears to be Understated

Expenditure is broadly divided into Plan[3] and Non Plan Expenditure. Total expenditure in FY09 has been budgeted to rise by a modest 6%yoy to Rs7,509bn. The expenditure numbers appear a bit under-stated as there appears to be no provision for the recommendations of the pay commission due next month. Further, the cost of the proposed Rs600bn loan waiver/relief to farmers is a grey area.

Trends in Expenditures (Rs Bn, %)

	FY03	FY04	FY05	FY06	FY07	FY08RE	FY09BE
Defence	557	601	759	805	855	925	1,056
%YoY	2.6	7.9	26.3	6.2	6.2	8.2	14.2
% of total Expenditure	13.5	12.7	15.2	15.9	14.7	13.0	14.1
Interest Payments	1,178	1,241	1,265	1,326	1,503	1,720	1,908
%YoY	9.6	5.3	1.9	4.8	13.3	14.4	11.0
% of Total Expenditure	28.5	26.3	25.4	26.2	25.8	24.2	25.4
Subsidies	435	443	460	475	571	697	714
YoY	39.4	1.9	3.7	3.4	20.2	22.1	2.4
% of Total Expenditure	10.5	9.4	9.2	9.4	9.8	9.8	9.5
Administration Expenses	374	422	470	484	553	558	601
%YoY	12.2	12.9	11.4	3.0	14.1	1.0	7.7
% to Total Expenditure	9.0	9.0	9.4	9.6	9.5	7.9	8.0
Other Non-Plan exp)	474	783	707	560	653	1,118	795
% to Total Expenditure	2.4	3.4	2.6	1.0	0.8	1.8	0.8
a. Total Non-Plan	**3,018**	**3,489**	**3,660**	**3,651**	**4,135**	**5,018**	**5,075**
%YoY	15.6	15.6	4.9	-0.2	13.3	21.4	1.1
% of GDP	12.3	12.7	11.6	10.2	10.0	10.7	9.6
% of total expenditure	73.0	74.0	73.4	72.2	70.9	70.7	67.6
b. Plan expenditure	**1,115**	**1,223**	**1,323**	**1,406**	**1,699**	**2,075**	**2,434**
YoY	10.1	9.7	8.2	6.3	20.8	22.2	17.3
% of GDP	4.5	4.4	4.2	3.9	4.1	4.4	4.6
% of total expenditure	27.0	25.9	26.6	27.8	29.1	29.3	32.4
TOTAL EXPENDITURES (a+b)	**4,132**	**4,712**	**4,983**	**5,057**	**5,834**	**7,094**	**7,509**
%YoY	14.1	14.0	5.7	1.5	15.4	21.6	5.9
% of GDP	16.8	17.1	15.8	14.1	14.1	15.1	14.2

Source: Budget Documents

Focus on the Social Sector and Agri Development

In line with expectations and the government's mantra of 'inclusive growth', the FM has devoted considerable fiscal space toward social sector measures. Key focus areas have been on the eight flagship schemes[4], rural and agricultural growth.

Social Infrastructure[5]; particularly health and education, have received higher outlays. For **health**, key schemes that have benefited include the National Rural Health Mission[6], the Rajiv Gandhi Drinking Water Mission, and the Total

[3] **Plan expenditure** is developmental in nature and is the amount for expenditure on projects and programs announced in the Plan. The capex spend refers to new spending while the revenue plan expenditure refers to expenditure on maintaining assets created in previous Plans. **Non-Plan Expenditure** covers spending not included in the Plan. Interest, subsidies, wages, defense are classified under revenue expenditure, while transfers to states and acquiring new defense equipment comes under capex

[4] **Eight Flagship Schemes** include the National Rural Health Mission, the Rajiv Gandhi Drinking Water Mission, and the Total Sanitation Campaign. For Education, the Sarva Sikha Abhiyan, Mid-Day Meal Scheme, and the Integrated Child Development Services scheme, The JNURM and the National Rural Employment Guarantee Scheme.

[5] For details on government's initiatives in the social sector please see our report India in 2008 – A year of priorities dated January 9, 2008 at https://www.citigroupgeo.com/pdf/SAP12399.pdf

[6] Launched in April 2005, the **NHRM** aims to strengthen primary healthcare for the rural population, with a special focus on 18 states that have particularly weak health indicators. During the period 2005-12, the NHRM

Sanitation Campaign. For **Education**, the Sarva Sikha Abhiyan[7], Mid-Day Meal Scheme, and the Integrated Child Development Services scheme have been major beneficiaries.

Physical Infrastructure: While outlays for the Jawaharlal Nehru National Urban Renewal Mission[8] and Bharat Nirman[9] have been raised by 25% and 27% respectively and will help improve urban and rural infrastructure, other measures include increased allocations for the National Highways Development Program, and the Accelerated Irrigation Benefit Program. The FM has also proposed to create a national fund for transmission and distribution reform in the power sector.

Agriculture Sector Initiatives

The debt relief package will cover 4% of total bank loans

In a bid to raise agri growth to the 11th Plan target of 4%, and to provide some debt relief to small and marginal farmers, the budget has provided a debt waiver on loans overdue as on Dec 2007-Feb 2008 through a one-time-settlement scheme. This would cover as many as 400mn farmers with the total value of loans being waived and the OTS relief on overdue loans pegged at Rs600bn. Finally, as far as rural development is concerned, the FM has proposed to expand the National Rural Employment Guarantee Scheme to all 596 rural districts in the country.

Central Plan Outlays by Major Sectors (Rs Bn, %YoY)

	FY08RE	FY09BE	%YoY
Agriculture and Allied Activities	85	101	17.9
Rural Development	211	238	12.7
Irrigation and Flood Control	5	4	-9.5
Energy	722	938	29.9
Industry and Minerals	180	288	60.6
Transport	689	842	22.1
Communications	166	219	32.2
Science Technology & Environment	77	93	19.9
General Economic Services	30	61	98.9
Social Services	752	959	27.6
General Services	5	12	115.8
Grand Total	**2923**	**3755**	

Source: Budget Documents

seeks to halve infant mortality from 60 to 30 per thousand, upgrade community health centres and increase bed occupancy. To strengthen rural healthcare, the Mission provides for the appointment of an Accredited Social Health Activist (ASHA) in each village.

[7] **Sarva Siksa Abhiyan** is the flagship program initiated in 2001 that aims at free and compulsory education to children of ages 6-14 (estimated at 205mn) by 2010. A third of the program allocation is aimed at developing the physical infrastructure and mandates the participation of the local community in all civil works in order to instill a sense of ownership in them.

[8] The **JNURM** program aims to help large metropolises in the country to tackle the fast pace of urbanization and migration from rural areas that have strained civic amenities. It covers the seven mega cities, all cities with a population of over a million, and some other towns. Initiatives include the Mumbai Metro Rail Project, the Mumbai Trans Harbor Link, the Mumbai Western Expressway Sealink Project

[9] The **Bharat Nirman Project** is a time-bound plan that aims to achieve goals in six areas of rural infrastructure (irrigation, water supply, housing, roads, telephony, and electrification) should greatly unlock the potential of rural India.

BUDGET FY09: KEY HIGHLIGHTS

Peak customs duty and service tax remain unchanged at 10% and 12% respectively,

Excise duty has been lowered from 16% to 14%

Higher exemption limits and tax slabs will help boost growth

Expenditure Targets seem ambitious and do not take into account :

(1) off-balance sheet items such as oil/food bonds

(2) Pay Commission

(3) Farm debt waiver

Fiscal Deficit targets are well within FRBM targets…

But it would take one additional year to eliminate the revenue deficit

Snapshot of Government Finances

Rs Bn, % GDP	FY04	FY05	FY06	FY07	FY08RE	FY09BE
a. Gross Tax Revenue	**2,543**	**3,050**	**3,662**	**4,735**	**5,854**	**6,877**
% to GDP	9.2	9.7	10.2	11.4	12.5	13.0
Corporation tax	636	827	1,013	1,443	1,861	2,264
Income tax	414	493	560	751	1,183	1,383
Excise duty	908	991	1,112	1,176	1,279	1,379
Import duty	486	576	651	863	1,008	1,189
Service tax	100	163	326	502	523	662
b. (-) Devolvement to States & UTs	674	802	972	1,223	1,536	1,806
c. Net tax revenues (a-b)	1,870	2,248	2,689	3,512	4,318	5,072
d. Non tax revenues	769	812	768	832	933	958
e. Net revenue receipts (c+d)	**2,639**	**3,060**	**3,458**	**4,344**	**5,251**	**6,029**
f. Non-debt capital receipts	841	665	122	64	406	147
Recovery of loans	672	620	106	59	45	45
Privatisation	170	44	16	5	361	102
g. TOTAL REVENUES (e+f)	**3,480**	**3,725**	**3,580**	**4,408**	**5,657**	**6,176**
% YoY	29.8	7.0	-3.9	23.1	28.3	9.2
h. Revenue expenditure	**3,621**	**3,843**	**4,394**	**5,146**	**5,886**	**6,581**
Interest (1)	1,241	1,269	1,326	1,503	1,720	1,908
Defence	432	439	482	517	548	576
Subsidies	443	460	475	571	697	714
Pensions	159	183	203	221	242	251
Grants to States	137	148	305	357	364	433
Admin and social services	422	470	484	553	558	601
Plan expenditure	786	875	1,119	1,424	1,756	2,098
i. Capital expenditure	**1,092**	**1,139**	**664**	**688**	**1,208**	**928**
Defence	169	320	323	338	377	480
Loans	487	371	52	75	512	111
Plan expenditure	436	448	288	274	319	336
j. Plan exp on rev & cap a/c	1,223	1,323	1,406	1,699	2,075	2,434
k Non Plan expen on rev & cap a/c	3,490	3,660	3,651	4,135	5,018	5,075
l. TOTAL EXPENDITURE (h+i) = (j+k)	**4,713**	**4,983**	**5,057**	**5,834**	**7,094**	**7,509**
% YoY	14.0	5.7	1.5	15.4	21.6	5.9
Deficit trends						
m. Fiscal deficit (l-g)	**1,233**	**1,258**	**1,478**	**1,426**	**1,437**	**1,333**
% to GDP	4.5	4.0	4.1	3.4	3.1	2.5
n. Revenue deficit (h-e)	**982**	**783**	**936**	**802**	**635**	**552**
% to GDP	3.6	2.5	2.6	1.9	1.4	1.0
o. Primary deficit (m-1)	**-8**	**-12**	**137**	**-77**	**-283**	**-575**
% to GDP	0.0	0.0	0.4	-0.2	-0.6	-1.1
Financing the deficit						
Market borrowings	889	460	953	1,104	1,107	1,006
PPF & special deposits	50	-4	60	52	48	48
Small savings	0	0	0	0	-18	99
Net external assistance	-135	148	75	85	100	110
Others	468	736	584	140	382	-2
Cash Surplus	-39	-82	-195	45	-182	72
Total financing	**1,233**	**1,258**	**1,478**	**1,426**	**1,437**	**1,333**
Memo items (% to GDP)						
Centre	4.5	4.0	4.1	3.4	3.1	2.5
State	4.5	3.5	3.2	2.6	2.5	2.4
Combined	8.5	7.5	6.7	6.4	6.0	5.7

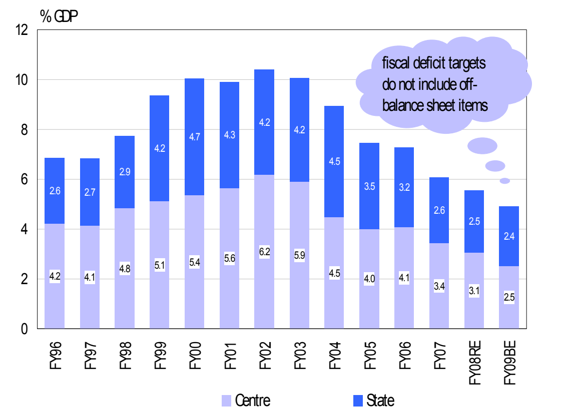
BE- Budgeted Estimated; RE- Revised Estimates. Source: Budget Documents

India- Government Finances in Pictures

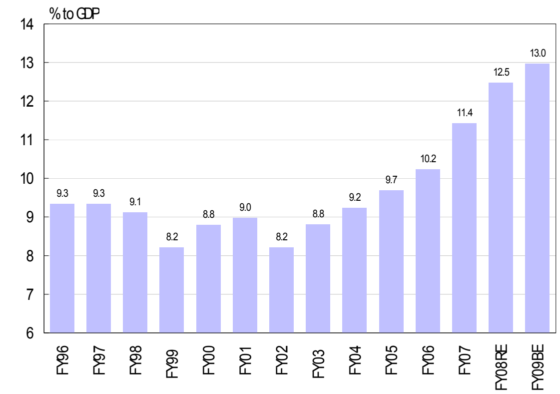
With the FY08 Budget pegging the center's fiscal deficit at 3.1% of GDP. In FY09, the deficit is estimated at 2.5%- well in line with FRBM targets. However, the revenue deficit, at 1% of GDP in FY09- is not

Fiscal consolidation is largely due to continued buoyancy in tax revenues at 12.5% of GDP in FY08. These are budgeted to further rise to 13% of GDP in FY09

Trends in the Fiscal Deficit (Centre +States, % GDP)



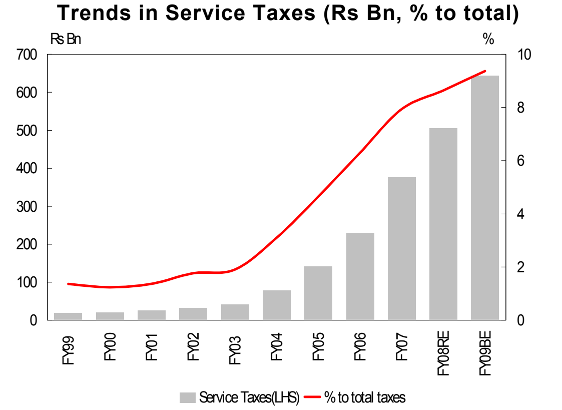
Trends in the Tax-GDP Ratio (%)



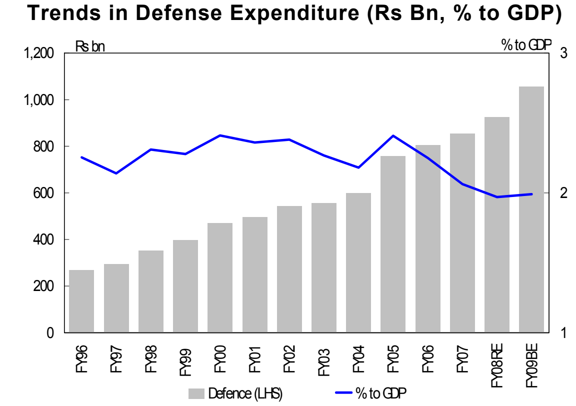
Service Taxes remain a major contributor to total taxes. While the rate has been left unchanged at 12%, 4 new services have been included

On the expenditure front, allocation for Defense has been increased by 10%yoy to Rs1056bn; or 14% of total expenditure

Trends in Service Taxes (Rs Bn, % to total)



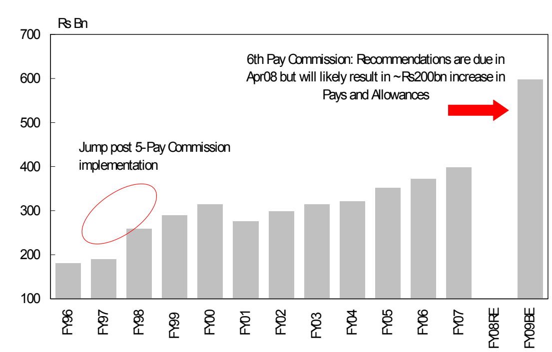
Trends in Defense Expenditure (Rs Bn, % to GDP)



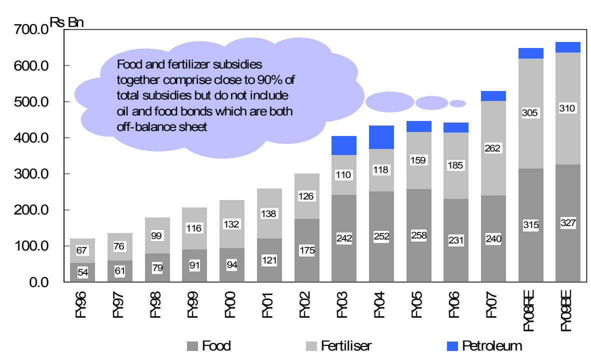
Pays and Allowances are also likely to rise by approximately Rs200bn, with the implementation of the 6th Pay Commission (rpt due in Apr08)

Finally, in addition to budgeted subsidies, the govt has been issuing food and oil bonds (off-balance sheet items) to curb price rise

Trends in Pays and Allowances (Rs Bn)



Trends and Components of Subsidies (Rs Bn)



Source: Budget Documents

Sector Notes

Autos

Budget Refocuses on Discretionary Consumption

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- **Overall: Positive** — The entire sector benefited from a broad-based reduction in indirect taxes across 2 and 3 wheelers, small cars and buses. The reduction in income taxes on personal income should also benefit the 2 wheeler sector and certain sections of the passenger car market. The waiver on loans to small / marginal farmers should be a long term negative. In the short term, we believe it improves sentiment – and possibly valuations – for the farm equipment sector (Mahindra, Punjab Tractors are the key beneficiaries), but longer term results in a moral hazard situation which might translate into the banking sector curtailing lending to the sector.

- **Reduction in tax rates to boost discretionary spending** — We calculate that the overall basic tax incidence on a family with an income of Rs400,000 pa has declined by almost 50% to Rs35,000. We believe this would positively impact discretionary spending – especially in segments like 2 wheelers and small cars.

- **Excise duty reduction** — Excise duties on small cars, 2 wheelers, 3 wheelers and buses have been reduced to 12% from 16%. Given the reduction in cenvat to 14% (from 16%) on inputs, most players will get a c2-2.6% savings on ex-factory prices (though this will not be applicable on manufacturing units in tax free zones). We believe players will pass through the benefits to the consumers (Maruti already has) and this could improve demand growth.

- **Greater emphasis on the agricultural sector** — The agriculture lending target has been increased to Rs 2,800 billion (+16.7% Y/Y), which positively impacts the farm equipment space. We adversely view the decision to waive loans for certain classes of farmers and give a 25% rebate on outstanding loans of other farmers under an OTS (one time settlement) scheme as longer term, it could create a moral hazard.

Implications of Budget Recommendations on Automotive Sector

Change	Business Implication	Stock Impact
Reduction of Excise duty to 12% from 16%: applicable on small cars, 2 wheelers, 3 wheelers and buses	Partially passed on to customer, which will positively impact volume growth. Net benefit to auto manufacturers will be ~2.6% as tax is payable on value addition in manufacturing (Cenvat also cut to 14% from 16%)	Positive for 2 wheelers – Bajaj (2 and 3 wheelers), Hero Honda, TVS, Maruti and Mahindra (3 wheelers), Tata Motors (small cars, buses) and Ashok Leyland (buses)
Reduction of Excise duty to 14% from 24%: applicable on hybrid cars	Players like Mahindra are contemplating commercialising hybrid vehicles in the medium term	Nil
Greater emphasis on increase in rural credit, target set at Rs2,800 bn; Waiver of loans for small and marginal farmers, 25% rebate under OTS (one time settlement) scheme for other farmers	Overall increased focus on the agricultural sector is a positive for 2 wheeler sales and also tractor sales. Loan waivers, OTS is also a short term positive	Positive for Hero Honda, Bajaj Auto, M&M
19% increase in allocation for the National Highway Development Program	Improvement in road infrastructure is a long term positive for trucking	Long term positive for Tata Motors, Ashok Leyland
Increase in disposable income by changing tax slabs	Increase in discretionary spend from customers likely to result in increase in automotive sales	Positive for 2 wheelers and small cars
Reduction in CENVAT rate to 14% from 16%	Reduces overall manufacturing costs	Positive for the entire auto sector
Reduction in CST from 3% to 2%	Marginally lowers retail prices – positively impact demand	Positive for the auto sector except for Maruti (already pays 2% CST due to waiver by Haryana Government)

Source: Citi Investment Research

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Banks, Financial Services

The Union budget is usually not very material for the banking system – the RBI's credit policy is the bigger policy announcement platform. However, this year has been an exemption – there are policy developments that will impact the banks.

Key measures and impact

- **Loan waiver for overdue small/marginal farmers loans (government estimate Rs600b – 3% of system loans)** – Not enough clarity, but it appears banks will need to write-off these loans – no clarity on compensation (if any), modalities, and the effective cost for these write-offs. Key questions include a) The level of compensation – risk that banks could take meaningful earnings hit; b) Moral hazard – Rural / agricultural lending could see significant risks if this becomes an expectation. The government suggests over 30m farmers will benefit; c) Bank valuation structurally, given the government policy override; and d) Disconnect between government numbers (Rs500b overdue) and RBI numbers (Rs74b).

- **Government has not accounted for reimbursement in current budget** – While there is an expectation that the government will compensate banks and there appears press suggesting government clarification of the same, there is no compensation accounted for in the budget financials. This essentially raises reimbursement risk and/or modality of this compensation.

- **Other measures** – The government has scrapped the banking transaction tax and the dividend distribution tax at the parent level, and advised banks to add at least 250 rural household accounts every year.

India Banks Agricultural Exposure (Rs M,%)

FY07	Net worth	Profits	Agri Loans	Total Loans	Agri Loans/ Total Loans	Agri NPA	Agri NPA / Agri Loans
All Banks	2,191,740	312,026	2,301,800	18,418,780	12%	73,670	3%
PSU	1,356,305	201,522	2,050,910	14,401,229	14%	65,060	3%

Source: RBI, Citi Investment Research

Banks Budget Implications

Change	Impact	Business Implication	Stock Impact
Agricultural Loan Write-off	Negative	Banks to write of overdue loans to small farmers – clarity needed on compensation. Could result in large hits, with meaningful moral hazard issues	Banks (-ve) more for PSU Banks
Banking Transaction Tax	Positive	Removes operational onerous tax	Positive for banks with large ATM networks. SBI, Axis, ICICI, HDFC Bank
Dividend Distribution Tax	Positive	No double taxation on dividend paid by subsidiary companies	HDFC (+ve), ICICI (+ve), SBI(+ve)
Service tax on ULIP	Negative	12.5% charge on fund management charges of Insurance companies	Banks having insurance business ICICI (-ve), SBI(-ve), Kotak(-ve)
Securities transaction tax	Negative	Now treated as an expenditure would get only 33% relief on tax vs 100% rebate earlier	Negative for brokers, banks with Securities businesses – Kotak (-ve)

Source: Citi Investment Research

Capital Goods

Rural Infrastructure Gets Boost

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- **Rural infrastructure and irrigation projects receive boost** — Budget 2008-09 continues the government's focus on creating grass root infrastructure: 1) Accelerated Irrigation Benefit Programme (AIBP) allocation is up 82% to Rs200bn; 2) Increase in the size of rural infrastructure development fund to Rs140bn; 3) Increase in allocation for NHDP by 19% to Rs129bn; and 4) Increase in allocation for urban infrastructure by 25% to Rs69bn.

- **Commitment to power sector reiterated** — But no major new sops to the sector. FM urged states to expedite bidding for remaining five UMPPS and announced the creation of a national fund for transmission and distribution. Inline allocation to schemes like Rajiv Gandhi Grameen Vidyutikaran Yojana and Accelerated Power Development and Reforms Project.

- **Indirect tax measures to benefit domestic power equipment manufacturers** — The withdrawal of exemption on power generation and T&D projects (except mega power projects) from the 4% additional CVD should benefit domestic equipment manufacturers, particularly BHEL, Thermax, etc. Exemption of excise duty on certain refrigeration equipment may benefit Voltas.

- **Infrastructure asset holding companies to benefit from change in incidence of dividend distribution tax** — Parent company can now set off the dividend received from subsidiary against dividend distributed by itself, provided that the dividend received is net of dividend distribution tax and the parent company is not a subsidiary of another company.

Capital goods, construction and electric utilities – Budget impact

Change	Expectations	Business Implication	Stock Impact
Emphasis on irrigation and water supply projects	In line with expectations	Positive	Positive - IVRCL, Gammon and HCC
Reduction in Cenvat Rates	No expectations	Positive	Positive - L&T, BHEL, Thermax, Voltas
CVD on imports for power equipment	No expectations	Positive	Positive - BHEL and Thermax
Dividend Distribution tax structure change	No expectations	Positive	Positive - L&T, JPA, Punj Lloyd
Excise exemption on certain refrigeration equipment	No expectations	Positive	Positive - Voltas
Increase in sales tax on works contract to 4%	No expectations	Neutral since it's a pass through	

Source: Citi Investment Research

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Cement

- **Excise duty changed** — (1) Excise duty has been revised on bulk cement from Rs400/t to 14% ad valorem or Rs400/t, whichever is higher; and (2) Excise duty has been increased on clinker from Rs350/t to Rs450/t.

- **Impact on bulk cement** — On all bulk cement *(which most likely includes bagged cement with no printed RSP-retail selling price)*, excise shall be charged according to the new regime. It is yet to be clarified on what basis the ad-valorem duty is to be charged. Assuming it is charged on the invoiced value, the impact would be in the range of Rs3-10/bag (2% to 4%) using a price range of Rs190-250/bag.

  We have assumed that bulk cement also includes bagged cement with no printed RSP. However, if this were to be excluded, the impact of the new excise duty would be limited as bulk cement alone accounts for only ~5-7% of sales.

- **Impact on bagged cement** — In the Budget speech, the Finance Minister has stated that he proposes to bring parity in the excise duty rates on bulk cement and packaged cement. Hence, it is likely that the new excise duty payable on bulk cement becomes applicable to bagged cement as well. Based on the pricing in most markets, ranging from Rs190-250/bag, the impact is Rs4-5/bag (2%). The FY08 excise duty on bagged cement was Rs350/t, if the cement was priced at/below Rs190/bag and 12% ad-valorem for cement priced above Rs190/bag (to a maximum of Rs30/bag).

  Based on the Finance Minister's speech that he proposes to bring parity in the excise duty rates on bulk cement and packaged cement, it is possible that the new excise duty of 14% could be applicable to bagged cement as well. We are still awaiting clarification on this. If excise duty on bagged cement continues at the old rate, there will be no impact.

- **Impact on clinker** — There is hardly any impact of the higher excise duty being charged on clinker as most companies do not sell clinker.

- **Reiterate Sell** — We maintain our Sell recommendations on cement stocks on the back of steady stream of new capacities in FY09/FY10, which is expected to disrupt pricing.

Cement – Impact of Budget

Change	Expectations	Business Implication	Stock Impact
Excise duty revised on bulk cement from Rs400/t to 14% or Rs400/t, whichever is higher	Negative - If this includes bagged cement with no printed RSP	Impact is Rs3-10/bag	ACC, Ambuja, Grasim, UltraTech
	Marginally negative – if chargeable only on bulk cement (5-7% of sales)	Negligible impact	
Assuming the new excise duty on bulk cement is also applicable on bagged cement	Negative	Impact is Rs4-5 per/bag	ACC, Ambuja, Grasim, UltraTech
	No impact, if the old excise regime on bagged cement remains (no clarity yet)	No impact	
Excise duty increased on clinker from Rs350/t to Rs450/t.	Marginally negative	There is hardly any sale of clinker in India	

Source: Citi Investment Research

Consumer & Retail

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- The debt relief scheme announced by the government – waiving off overdue agricultural loans, increased government expenditure on irrigation, target to increase the agricultural farm growth – would lead to an increase in disposable incomes in rural areas and demand generation. Consumer companies with exposure to rural India stand to benefit. The major beneficiaries will be HUL, Asian Paints, Dabur, ITC, Marico and Godrej Consumer.

- The excise duty on non-filter cigarettes has been increased to bring it on par with the filter cigarettes. Excise on filter cigarettes has remained unchanged. On a weighted average basis, the overall increase in excise duty for ITC is 16%. More importantly, the new excise duty structure will make micros and plain non filter cigarettes uncompetitive (overall 30% share of cigarette industry volumes). We expect ITC to pass on these excise increases, which is likely to adversely impact volumes, although margins for ITC may improve. ITC is also likely to gain market share from smaller players which manufacture only non-filter cigarettes.

- Excise duty on paper and paper products has been reduced from 12% to 8%. This is positive for paper and paperboard manufacturers like ITC.

- Creation of crop insurance schemes for tea and coffee would benefit tea and coffee plantation companies. Excise duty on tea and coffee mixes has been removed from 16% earlier which is positive for HUL, Tata Tea and Nestle. Duty on breakfast cereals has been reduced from 16% to 8% which is positive for the food processing industry.

Consumer			
Change	**Expectations**	**Business Implication**	**Stock Impact**
Debt waiver for small and marginal farmers	-	Positive for demand generation	Positive for for all consumer cos HUL, ITC, Marico, Asian Paints, Dabur, Godrej Consumer etc
Excise duty on non filter cigarettes - plains has increased from Rs0.562/stick to Rs1.32/stick. For micros, the increase has been from Rs0.168/stick to Rs0.819/stick	Overall 5-6% increase.	Negative for volume growth	Negative for ITC's cigarette volume growth.
Excise duty on tea and coffee mixes has been removed from 16% earlier	-	Positive for increasing demand	Positive for HUL, Tata Tea and Nestle.
Excise duty on paper and paper products reduced from 12% to 8%.	-	Positive for increasing demand	Positive for ITC
Creation of crop insurance schemes for tea and coffee	-	Positive for improving yields	Positive for tea plantation cos
Duty on breakfast cereals has been reduced from 16% to 8%	-	Positive for increasing demand	Positive for the food processing cos.

Source: Citi Investment Research

Hotels

Marginally Positive

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- **5-yr tax holiday for new hotels in heritage sites** — This is available to two, three or four star hotels established in specified districts having UNESCO-declared 'World Heritage Sites', key locations near Agra, Goa, Delhi. The hotels should start operations during Apr'08 to Mar'2013.
- **Impact, marginally positive** — We see this as marginally positive for the hotel sector – 1) should encourage investments in hotels, and 2) address shortage of rooms in tier II and tier III cities. We believe, Indian Hotels' Ginger, the budget chain, could potentially benefit from this tax-break for some of its hotels.

Hotels			
Major changes	**Expectations**	**Business Implication**	**Stock Impact**
5-yr tax holiday for new 2,3 and 4-star hotels in Heritage sites operational between Apr'08 to Mar'2013	Marginally Positive	Encourage fresh investments, address shortage of rooms	Indian Hotels +ve
Parent company allowed to set-off dividend distr. tax on dividend recd from sub against div distributed by parent Co.	Positive	Reduced double taxation	Indian Hotels +ve

Source: Citi Investment Research

Media

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Source: Citi Investment Research

- Customs duty on parts of set top boxes parts like SMPS board IR module has been exempted. This will be helpful in faster penetration of DTH as the set top boxes become more affordable. Positive for broadcasters like Zee and Sun TV.

Media

Change	Expectations	Business Implication	Stock Impact
Customs duty on parts of set top boxes removed	-	Positive for making set top boxes more affordable	+ve broadcasters (Zee).

Source: Citi Investment Research

Metals

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- **Measures announced** — (1) General rate of excise duty (CENVAT) has been reduced from 16% to 14%; (2) Customs duty on iron or steel melting scrap has been reduced from 5% to nil; (3) Customs duty on aluminium scrap has been reduced from 5% to nil; and (4) Export duty rate on chromium ores has been increased from Rs2,000/t to Rs3,000/t.

Impact of measures

- The reduction in excise duty should be a marginal positive for metal demand.
- The impact of zero customs duty on steel scrap should marginally benefit non-integrated EAF steel producers importing scrap. A decrease in landed cost of steel scrap imports could lead to downward pressure on sponge iron prices.
- Zero customs duty on aluminum scrap would hardly impact the integrated producers. There could be a marginal positive impact for secondary aluminium producers using scrap for blending purposes.

Metals

Change	Expectations	Business Implication	Stock Impact
CENVAT reduced from 16% to 14%	Marginally positive	Increase in metal demand	JSW Steel, Sterlite, Nalco, Hindalco
Customs duty on iron or steel melting scrap reduced from 5% to nil	Marginally positive	Marginally benefits non-integrated EAF steel producers importing scrap	
	Marginally negative	Downward pressure on sponge iron prices	Jindal Steel & Power, Grasim
Customs duty on aluminium scrap reduced from 5% to nil	Marginally positive	Marginally benefiting secondary aluminium producers using scrap	

Source: Citi Investment Research

Oil & Gas, Petrochemicals

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Key Measures and Impact

- **Excise duty change on auto fuels mainly cosmetic** — The excise duty rates on unbranded gasoline and diesel have been changed. The ad valorem component has been removed while the specific duty component has been increased by Rs1.35/l – without any change in the retail price. The excise duty now stands at Rs14.35/l and Rs4.60/l on unbranded gasoline and diesel. The impact on total excise duty payable in absolute terms is, however, negligible as there is no change in the ex-storage price (and therefore the assessable value) of the fuels. This is, hence, largely neutral for the OMCs as well as the refiners.

- **Customs duty of 5% on naphtha, marginally negative for RIL** — Duty on imported naphtha used for polymer production has been increased from Nil to 5%. This is negative for companies like RIL, which uses imported naphtha for its ethylene cracker. The potential impact is, however, manageable at ~1.5% of RIL's FY09E EPS.

- **Government's subsidy contribution unchanged** — Subsidy contribution on LPG/SKO has largely remained flat at Rs29bn. Including oil bonds disbursed so far (Rs113bn in 1HFY08), total contribution of the govt. stands at Rs142bn.

- **Increasing focus on natural gas** — The government intends to promote the use of renewable energy sources such as gas, amongst others, and plans to establish a permanent institutional mechanism in developing and coordinating such initiatives. We view this move as small but important step towards long-term energy planning. This could also be a structural positive for gas consumption.

Oil & Gas, Petrochemicals

Change	Pre-budget	Post-budget	Stock Impact
Excise duty on unbranded gasoline	6% + Rs13.0/litre	Rs14.35/litre	Neutral for R&M companies
Excise duty on unbranded diesel	6% + Rs3.25/litre	Rs4.60/litre	Neutral for R&M companies
Customs duty on imported naphtha for manufacturing polymers	-	5%	Marginally negative for RIL
Polyester Filament Yarn	1% NCCD (National Calamity Contingent Duty)	nil	Marginally positive for polyester demand and RIL

Source: Citi Investment Research

Pharmaceuticals, Healthcare & Agrochem

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- **Marginally positive for pharma –** We see no structural positive or negative for the pharma sector from the policy initiatives announced. Several companies would benefit from the slew of tax related measures (lower excise duty, weighted deduction on outsourced R&D); however, the impact is unlikely to be as positive as it appears upfront. We expect the net impact to be marginally positive for companies.

- **Excise duty on all pharma goods (formulations) cut to 8% from 16% –** This is positive for companies that have high exposure to the Indian market.

  However, upside from this could be marginal as most companies have already shifted their production to excise free zones, such as Baddi, effectively lowering overall excise duty being paid. Secondly, the rate of abatement has been reduced from 42.5 to 35.5 – as such, the effective reduction in excise duty is from 9.2% to 5.2%.

  We also believe that there is a reasonable probability that a large part of the benefit would have to be passed through by way of lower prices. Most companies have some part of their domestic revenues coming from price controlled drugs, where the lower duty will be passed on automatically. Besides, the competitive intensity in the market as well as pressure from the Ministry for Chemicals & Fertilizers (which is pressing for more drugs to be brought under price control) would also lead to companies opting to pass on a large part of the benefit to customers.

- **5 year tax window for new hospitals –** set up anywhere in the country except certain specified urban agglomerations (including Greater Mumbai, Delhi, Kolkata, Chennai, Hyderabad, Bangalore and Ahmedabad). This is positive, given that hospital companies have high effective tax rates – a profitable hospital would have an effective tax rate of over 30%. Near-term upside for the listed companies (Apollo & Fortis) appears marginal as most hospitals scheduled to commence operations in the next 2 years are in the excluded regions. Besides, most of these hospitals would have negative to marginal profitability in the first 2-3 years after commencement of operations.

- **Weighted deduction on outsourced R&D –** to the extent of 125%. This is marginally positive for most Indian companies as several of them have been looking at the option of outsourcing some of their R&D activities. However, this is marginal and unlikely to have any major impact on our estimates.

Indian Pharma – Effective Excise Duty

Company	Excise Duty as % of Sales
Aurobindo	**7%**
Biocon	4%
Cadila Healthcare	5%
Cipla	3%
Dishman	1%
Dr Reddy	1%
GlaxoSmithKline Pharma	**8%**
Glenmark Pharma	2%
Jubilant Organosys	7%
Matrix Lab	2%
Nicholas Piramal	4%
Orchid Chemical	0%
Ranbaxy	1%
Shasun Chemicals	2%
Sun Pharma	5%
Wockhardt	1%

Source: Citi Investment Research

- **Thrust on agriculture positive for seeds / crop protection –** a) Waiver of loans to the tune of Rs600bn and general thrust on agriculture would increase spending power in the hands of farmers leading to greater demand for crop protection, seeds & fertilizers; b) Inclusion of seeds manufacturers in the list of sectors that qualify for weighted deduction is positive for United Phosphorus, as it has an associate company, Advanta (49% stake) in the seeds business.

New Hospitals Planned in Next 3 Years

	No of Beds	Eligible for Tax Exemption
Apollo Hospitals		
First Med Expansion (Chennai)	40	No
Madurai Expansion	50	No*
Hyderabad Expansion	500	No
Mauritius	200	No
PH Road (Chennai)	150	No
Speciality Expansion (Chennai)	30	No
Navi Mumbai	350	Yes
Bhubaneshwar	222	Yes
Vishakapatnam	222	Yes
Fortis Healthcare		
Navi Mumbai	152	Yes
Shalimar Bagh	258	No
Gurgoan	350	No

*brownfield expansion; may not qualify as a new hospital

Source: Citi Investment Research, Company

Impact Analysis – Pharma, Healthcare & Agrochem

Change	Impact	Business Implication	Stock Impact
Pharmaceuticals & Healthcare			
Lower Excise duty on all pharma goods: down to 8% from 16% earlier **Abatement level reduced** to 35% from 45% earlier	Marginally Positive	• Positive for companies with high exposure to Indian market. • Upside would be restricted given that most companies have shifted manufacturing to excise free zones • We also believe companies may have to pass on the benefit to consumers	GSK (++), Sun Pharma (+), NPIL (+), Ranbaxy (+)
5-year tax window for hospitals set up in any part of India barring certain urban agglomerations **Excluded areas**: Greater Mumbai, Delhi, Kolkata, Chennai, Hyderabad, Bangalore, Ahmedabad, Faridabad, Gurgaon, Ghaziabad, Gautam Budh Nagar, Gandhinagar & Secunderabad	Positive	• Significant reduction in effective tax rates given that profitable hospitals have effective tax rates of c30% • Upside limited given that several cities that are part of the expansion plans of private hospitals do not qualify for this tax window • No major impact on earnings over the next few years as most hospitals are not profitable in the first 2-3 years of operations	Apollo (++), Fortis (+)
Tax incentive on outsourced R&D – qualifies for 125% weighted deduction	Positive	• Positive for companies exploring options to outsource R&D to service providers	Most Indian pharma companies
Agrochemicals (Seeds & Crop Protection)			
Seeds manufacturers allowed weighted deduction of 150 per cent on any expenditure on in-house scientific research	Positive	• Lower effective tax rate for seeds companies in India	United Phosphorous (via its 49% stake in Advanta) (++)
Overall thrust on agriculture - waiver of debt for small & marginal farmers, higher allocations for irrigation etc	Positive	• Additional spending power for farmers could translate into greater demand for seeds, fertilizers and pesticides	United Phosphorous (+)

Source: Citi Investment Research

Real Estate

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- **Impact, Neutral** — The budget is largely neutral for real estate sector with no material changes. While we see some likely indirect benefits – 1) greater demand for upcoming IT SEZs with tax exemption likely to end for Software Technology Parks by 31st Mar'09, and 2) higher disposable income for individuals following increase in tax exemption – to help improve housing demand; possible increase in cement prices due to new duty structure would offset some of these indirect benefits.

IT Services

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- We were not expecting any major tax changes from the Union Budget 2009 for Indian IT companies (we are already building in 20-22% tax rates in FY10 for all companies). However, some clarity on transition from STPI to SEZ was expected from this budget. There were no details on the same.
- Custom software development for domestic use attracted ~12% service tax, while packaged software sales attracted 8% excise duties. Budget proposes to bring both at parity by increasing excise duty to 12% on packaged software. However, this has little implication for IT services companies as most of them are in the custom software area (where there is no change) and those with software products have very small domestic exposure.
- Higher IT and educational spend by Indian government should be marginally positive for HCL Info, educational services companies and IT services companies focused on domestic business.
- Lower personal income taxes should lead to higher disposable income helping consumption at the broader economy level. This should also spur demand for electronics goods (positive for HCL Info).

Technology Sector – Budget Highlights

Change	Expectations	Business Implication	Stock Impact
IT services			
No major changes in taxes	Clarity on STPI/SEZ policy	Nil	Neutral
Minor Changes			
Software sales excise increased from 8% to 12%	-	This brings custom software development (which attracts ~12% service charge) at par with software products.	Marginally positive for IT services companies and negative for software product companies with high domestic sales
FBT exemption on creche; Guest houses	-	Marginally lower PBT outflow	Marginally positive
Lower personal income taxes	-	Companies can work with lower wage inflation	Marginally positive
Educational Services			
Higher allocation to education spend	Continued support to Educational IT spend by government	More state government schools to get covered under IT infrastructure	Marginally positive for Educomp and NIIT
Hardware (HCLI and MBI)			
Higher government IT spend	-	More system integration projects from government	To benefit HCL Info, Wipro and TCS
Lower personal income taxes	-	Higher disposable income to spur higher demand of electronics goods	Marginally positive from demand perspective for HCL Info
Focus on Renewable Energy	Concrete steps to improve Solar energy usage in India	Government has proposed further usage of clean energy. No immediate impact	Neutral to marginally positive for Moser Baer

Source: Citi Investment Research

Telecom

A Non-event

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- **Most changes in convergence products** — Specified parts of set-top boxes have been exempt from customs duty. Similarly customs duty on all MP3/MP4 or MPEG 4 players, with or without radio/video reception facility has been reduced from 10% to 5%. Also, concessional rate of 8% excise/CVD has been extended to these products. While this helps the DTH/IPTV business models by reducing costs of set-top boxes, we think the impact is relatively small for listed telcos as these businesses are still at infancy.

- **Duties slashed on wireless data cards** - Similarly, wireless modem cards are being fully exempt from excise duty/CVD (16% earlier), although additional customs duty of 4% (earlier Nil) has been introduced. This will help RCOM and TTML, which are active in the wireless data card market.

- **Duty increase on handsets illogical but only a marginal negative** — There is 1% increase in excise duty on mobile phones. On imported mobile phones, this will be levied as an additional customs duty. While it is difficult for us to understand the rationale, we think the impact is negligible given the global deflation in handset prices in any case.

Textiles

Marginally Positive

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- **Increase in TUF provision; Resources for Integrated Textile Parks** — Key measures include 1) Increased provision for TUF (Technology Upgradation Fund) to Rs10.9bn in FY09E vs. Rs9.1bn in FY08; 2) Maintained provision of Rs4.5bn for integrated textile parks; looking at the good progress - 30 parks approved with 20 units in 4 parks having commenced production, and 3) Removed 1% excise NCCD (National Calamity Contingent Duty) imposed on Polyester Filament Yarn (PFY).

- **Impact, marginally positive** – We see these initiatives as marginally positive for the textile sector. We believe this should support further investments and help enhance scale. Cut in duty would provide some relief in rising raw material cost of man-made fabric manufacturers like Raymond, S Kumars.

Textiles

Change	Expectations	Business Implication	Stock Impact
Increase in TUF to Rs10.9bn from Rs9.1bn	Positive	Encourage investment in textile sector	+ve for Alok
Removal of 1% excise duty on PFY	Positive	Help reduce raw material costs for yarn and fabric	+ve for Raymond and S Kumars

Source: Citi Investment Research

Citi India Universe Valuations

Company	RIC Code	Rating	Price 2/29/08	MktCap US$m	P/E	P/B	Div. Yield	EPS Growth	ROAE	EPS
Aban Loyd Chiles Offshore	ABAN.BO	1M	4,112	3,899	10.7	5.9	0.2%	250.3%	86.5%	385.7
ABB India	ABB.BO	2L	1,156	6,146	30.0	10.1	0.2%	55.2%	39.8%	38.5
ACC	ACC.BO	3M	793	3,731	11.9	2.9	2.0%	-14.1%	26.7%	66.6
Alok Industries	ALOK.BO	1M	69	325	5.8	1.0	4.3%	22.4%	18.4%	12.0
Ambuja Cements	ABUJ.BO	3M	121	4,619	13.3	2.9	2.3%	-9.7%	23.9%	9.1
Amtek Auto	AMTK.BO	1M	304	1,077	8.8	1.3	1.5%	19.6%	17.6%	34.8
Amtek India	AMTI.BO	1M	137	384	7.4	1.1	2.1%	38.6%	21.5%	18.5
Andhra Bank	ADBK.BO	1L	91	1,102	6.1	1.1	4.6%	16.5%	18.9%	14.8
Ansal Properties & Infrastructure	ANSP.BO	3H	215	613	4.0	1.3	0.5%	69.8%	37.6%	54.0
Apollo Hospitals	APLH.BO	1M	496	730	25.0	2.4	2.1%	20.8%	10.1%	19.8
Arvind Mills	ARMI.BO	3M	49	258	16.0	0.6	0.0%	98.2%	3.7%	3.1
Ashok Leyland	ASOK.BO	3L	37	1,250	10.9	2.2	4.5%	7.0%	20.6%	3.4
Asian Paints	ASPN.BO	1L	1,112	2,675	20.8	10.5	3.1%	23.0%	50.0%	53.4
Aurobindo Pharma	ARBN.BO	3L	330	445	10.0	1.6	0.5%	25.8%	17.1%	32.9
Axis Bank	AXBK.BO	2L	1,019	9,140	23.2	3.5	0.4%	30.9%	16.5%	44.0
Bajaj Auto	BJAT.BO	1L	2,280	5,787	17.3	3.3	2.2%	13.0%	20.4%	132.1
Bajaj Hindustan	BJHN.BO	3M	246	874	15.6	2.2	0.0%	na	15.5%	15.8
Balrampur Chini Mills	BACH.BO	3M	94	600	15.6	2.3	0.0%	na	16.2%	6.0
Bank of Baroda	BOB.BO	1M	366	3,342	7.4	1.2	1.6%	12.8%	16.8%	49.3
Bharat Forge	BFRG.BO	2L	290	1,619	16.1	3.2	1.6%	20.7%	23.0%	18.0
Bharati Shipyard	BHAR.BO	1M	630	432	11.9	2.8	0.5%	52.4%	39.4%	52.7
Bharti	BRTI.BO	1L	826	39,305	18.5	5.7	0.8%	25.0%	35.1%	44.5
BHEL	BHEL.BO	1L	2,282	28,022	25.4	7.6	0.7%	32.8%	33.7%	89.8
Biocon	BION.BO	3L	446	1,120	15.2	2.5	1.0%	35.0%	18.1%	29.5
Britannia Industries	BRIT.BO	1L	1,377	825	13.2	3.5	1.5%	34.0%	29.4%	104.4
Cadila Healthcare	CADI.BO	3L	261	822	9.7	2.4	1.5%	20.8%	27.3%	26.8
Cairn India	CAIL.BO	1M	228	10,180	144.3	1.4	0.0%	26.8%	1.0%	1.6
Canara Bank	CNBK.BO	1M	278	2,860	6.0	0.9	2.4%	19.0%	15.2%	46.1
Castrol	CAST.BO	1M	276	855	14.6	7.0	4.5%	2.2%	51.5%	19.0
Central Bank of India	CBI.BO	3M	104	1,050	5.7	0.9	3.9%	35.3%	14.5%	18.3
Centurion Bank	CENB.BO	2M	49	2,362	36.2	3.8	0.0%	27.3%	12.0%	1.4
CESC	CESC.BO	1L	533	1,672	17.3	1.7	0.8%	16.5%	10.1%	30.9
Chennai Petroleum	CHPC.BO	1L	300	1,122	6.5	1.2	4.7%	-22.9%	19.5%	46.4
Cipla	CIPL.BO	3L	207	4,041	23.0	3.8	1.1%	4.3%	17.7%	9.0
Colgate-Palmolive India	COLG.BO	1L	373	1,271	16.7	11.2	3.8%	14.8%	74.9%	22.4
Corporation Bank	CRBK.BO	1M	326	1,171	5.9	0.9	3.1%	21.8%	17.2%	55.4
Dabur	DABU.BO	1L	100	2,160	20.0	16.4	2.0%	23.4%	84.6%	5.0
Deccan Chronicle Holdings	DCHL.BO	1M	170	1,042	12.1	3.2	1.2%	22.3%	29.0%	14.0
Dishman Pharmaceuticals & Chemicals	DISH.BO	1M	291	575	14.9	3.4	0.5%	35.7%	26.5%	19.6
DLF	DLF.BO	1M	781	33,380	13.4	5.0	1.0%	42.8%	42.5%	58.2

Source: Citi Investment Research

Citi India Universe Valuations (Contd.)

Company	RIC Code	Rating	Price 2/29/08	MktCap US$m	P/E	P/B	Div. Yield	EPS Growth	ROAE	EPS
Dr Reddys Lab	REDY.BO	1M	583	2,458	16.9	2.0	0.8%	37.9%	12.2%	34.5
Educomp Solutions	EDSO.BO	3H	4,251	1,839	60.9	23.7	0.1%	76.5%	51.3%	69.8
EIH Ltd	EIHO.BO	3L	173	1,700	22.4	4.2	0.9%	19.0%	20.3%	7.7
Everest Kanto Cylinder	EKCL.BO	1M	316	802	19.3	5.1	0.8%	55.1%	31.2%	16.3
Federal Bank	FED.BO	1M	297	637	9.5	1.1	1.2%	-4.6%	12.6%	31.2
Fortis Healthcare	FOHE.BO	1M	85	485	145.4	2.8	0.0%	-126.9%	1.9%	0.6
Gammon India	GAMM.BO	1L	499	277	26.7	3.7	0.1%	42.0%	14.9%	18.7
Gas Authority of India Ltd.	GAIL.BO	1L	423	8,965	13.1	2.5	2.8%	10.1%	20.1%	32.2
Gateway Distriparks	GATE.BO	1M	110	318	10.0	1.7	3.6%	20.9%	17.6%	10.9
Glenmark Pharma	GLEN.BO	1M	485	3,015	19.4	6.2	0.2%	14.0%	42.8%	25.0
Godrej Consumer Products	GOCP.BO	1L	135	764	16.8	13.5	3.6%	16.8%	92.6%	8.0
Grasim Industries	GRAS.BO	3M	2,888	6,642	15.0	2.9	1.2%	-8.4%	20.8%	192.4
Great Offshore	GOFS.BO	1M	836	799	13.7	2.9	1.5%	13.1%	24.5%	61.1
GSK Consumer	GLSM.BO	1L	607	641	12.4	3.7	4.5%	17.4%	31.7%	49.0
GSK Pharma India	GLAX.BO	3L	1,109	2,357	20.3	6.5	2.7%	15.7%	34.2%	54.6
Gujarat Gas	GGAS.BO	1L	314	506	12.5	2.9	1.0%	23.0%	25.2%	25.1
Gujarat State Petronet	GSPT.BO	1L	71	997	31.5	3.3	1.0%	54.1%	10.8%	2.2
HCL Infosystems	HCLI.BO	1M	213	9,091	9.0	2.8	3.8%	24.4%	35.0%	23.8
HCL Technologies	HCLT.BO	1M	278	4,631	13.7	2.7	2.9%	10.6%	21.8%	20.3
HDFC Bank	HDBK.BO	2L	1,453	12,919	24.7	3.8	0.6%	24.0%	16.6%	58.8
Hero Honda	HROH.BO	3L	764	3,829	14.8	4.4	2.6%	17.0%	32.0%	51.5
Hexaware Technologies	HEXT.BO	1H	75	268	8.6	1.2	3.2%	9.2%	14.6%	8.6
Hindalco	HALC.BO	3M	203	6,247	14.5	1.4	0.9%	-19.1%	10.3%	14.0
Hindustan Construction	HCNS.BO	1L	166	1,066	35.6	3.5	0.6%	62.4%	11.8%	4.7
Hindustan Lever	HLL.BO	1L	227	12,420	23.8	17.7	4.0%	7.9%	75.7%	9.5
Hindustan Petroleum	HPCL.BO	3M	299	2,541	8.0	0.9	3.8%	-15.0%	11.5%	37.4
Hindustan Zinc	HZNC.BO	1M	655	6,945	6.5	1.8	1.2%	15.3%	32.5%	100.7
Hotel Leela Venture	HTLE.BO	1M	51	483	14.0	1.5	0.8%	11.1%	10.6%	3.6
HT Media	HTML.BO	3L	195	1,145	23.0	4.3	0.9%	27.9%	20.3%	8.5
ICICI Bank	ICBK.BO	1L	1,091	30,447	20.7	2.3	1.0%	34.5%	11.7%	52.6
IDEA Cellular	IDEA.BO	1L	110	7,282	23.9	6.1	0.0%	18.5%	29.4%	4.6
I-Flex Solutions	IFLX.BO	3H	1,075	2,259	20.0	2.8	0.0%	26.9%	15.1%	53.7
IL & FS Investsmart	ILFI.BO	3M	165	288	13.5	1.3	1.7%	2.0%	10.2%	12.2
Indiabulls	IBUL.BO	3M	615	3,910	15.9	3.2	0.7%	22.9%	20.8%	38.7
Indian Hotels	IHTL.BO	1L	125	2,274	16.1	2.6	1.1%	24.1%	15.9%	7.8
Indian Oil Corporation	IOC.BO	3M	561	16,768	9.5	1.4	2.5%	-20.8%	14.9%	59.1
Indraprastha Gas	IGAS.BO	1L	147	515	11.2	3.0	2.7%	13.6%	29.0%	13.1
Info Edge	INED.BO	2L	1,039	711	44.7	8.9	0.1%	20.3%	21.9%	23.2
Infosys Technologies	INFY.BO	1M	1,547	22,178	16.4	4.6	1.3%	17.0%	31.6%	94.5
Infrastructure Development Finance	IDFC.BO	3M	195	6,336	22.1	3.8	0.6%	35.0%	18.4%	8.8

Source: Citi Investment Research

Citi India Universe Valuations (Contd.)

Company	RIC Code	Rating	Price 2/29/08	MktCap US$m	P/E	P/B	Div. Yield	EPS Growth	ROAE	EPS
ITC	ITC.BO	1L	202	19,103	18.8	5.2	2.1%	22.0%	30.2%	10.8
IVRCL Infra & Projects	IVRC.BO	1M	470	1,563	23.6	3.5	0.3%	54.8%	16.5%	20.0
Jagran Prakashan	JAGP.BO	1L	113	855	21.0	5.5	2.6%	38.6%	27.6%	5.4
Jaiprakash Associates	JAIA.BO	1L	262	7,637	37.1	7.6	0.3%	62.0%	25.9%	7.1
Jet Airways	JET.BO	3M	737	3,963	20.3	1.7	1.1%	219.5%	8.8%	36.3
JSW Steel	JSTL.BO	1M	1,062	4,368	9.2	2.0	2.1%	18.8%	22.9%	115.2
Jubilant Organosys	JUBO.BO	1L	358	1,301	16.2	3.3	0.6%	27.3%	28.8%	22.1
Kotak Mahindra Bank	KTKM.BO	2M	801	6,923	26.9	4.1	0.1%	22.5%	16.1%	29.8
KPIT Cummins	KPIT.BO	1H	84	164	9.7	2.0	0.9%	23.4%	23.0%	8.7
Larsen & Toubro	LART.BO	1L	3,523	25,820	34.9	8.6	0.5%	39.9%	28.1%	101.1
Mahindra & Mahindra	MAHM.BO	1L	693	4,271	15.7	3.2	1.7%	10.2%	23.4%	44.2
Marico	MRCO.BO	1L	63	962	19.8	10.5	2.5%	25.7%	61.1%	3.2
Maruti Udyog	MRTI.BO	1L	867	6,285	11.3	2.4	0.7%	17.5%	23.3%	77.1
Matrix Lab	MAXL.BO	3M	192	744	14.6	2.2	1.0%	42.8%	16.2%	13.2
Mindtree Consulting	MINT.BO	3H	350	333	11.4	2.1	0.9%	14.1%	20.4%	30.6
Moser Baer India	MOSR.BO	3H	177	746	7.5	1.2	0.6%	149.5%	19.8%	23.5
Motilal Oswal Financial Services	MOFS.BO	1M	919	655	9.5	n/a	0.0%	63.0%	n/a	96.4
Mphasis	MBFL.BO	1H	229	1,200	13.1	3.2	1.3%	42.2%	27.5%	17.6
MTNL	MTNL.BO	3L	118	1,871	21.0	0.6	3.4%	-29.0%	3.1%	5.6
Nagarjuna Construction	NGCN.BO	1M	272	1,563	20.8	3.0	0.5%	60.0%	16.8%	13.1
Nalco	NALU.BO	3M	463	7,490	18.0	2.9	1.4%	-7.5%	17.4%	25.7
Nestle India	NEST.BO	3L	1,372	3,319	25.6	23.3	2.6%	28.7%	102.3%	53.7
Nicholas Piramal	NICH.BO	1M	274	1,437	12.3	3.8	1.6%	28.5%	35.6%	22.4
NIIT	NIIT.BO	3H	124	512	19.4	4.1	0.9%	44.9%	23.3%	6.4
Northgate Technologies	NOTC.BO	1M	528	462	28.2	2.6	0.0%	-0.3%	10.0%	18.8
NTPC	NTPC.BO	1L	202	41,729	18.5	2.8	2.0%	11.5%	16.1%	10.9
Oil & Natural Gas Corp	ONGC.BO	1L	1,012	54,316	8.6	2.4	4.9%	13.2%	29.2%	117.1
Omaxe	OMAX.BO	1H	255	1,111	6.3	2.0	0.4%	37.5%	37.8%	40.5
Orchid Chemicals	ORCD.BO	1L	252	416	6.7	1.4	2.4%	13.4%	22.2%	37.7
Oriental Bank of Commerce	ORBC.BO	1M	251	1,578	8.4	0.9	1.8%	22.5%	11.9%	29.9
Pantaloon	PART.BO	3M	528	1,998	39.7	5.6	0.1%	25.9%	15.0%	13.3
Parsvnath Developers	PARV.BO	3H	269	1,245	4.0	0.9	0.9%	83.3%	29.4%	67.6
Patni Computer	PTNI.BO	1H	241	841	8.0	1.1	2.1%	-8.3%	14.8%	30.3
Petronet LNG	PLNG.BO	3M	74	1,389	13.6	3.1	2.0%	16.1%	24.9%	5.4
Punj Lloyd	PUJL.BO	1L	378	2,876	24.8	3.8	0.1%	55.3%	18.4%	15.2
Punjab National Bank	PNBK.BO	1M	604	4,778	8.3	1.4	1.7%	16.2%	17.7%	73.0
Puravankara Projects	PPRO.BO	1M	311	1,665	13.6	3.8	0.5%	92.7%	31.6%	22.8
Ranbaxy	RANB.BO	1M	446	4,172	20.5	5.1	2.0%	10.7%	26.4%	21.8
Raymond Ltd	RYMD.BO	1L	342	527	14.4	1.3	1.8%	27.9%	9.4%	23.8

Source: Citi Investment Research

Citi India Universe Valuations (Contd.)

Company	RIC Code	Rating	Price 2/29/08	MktCap US$m	P/E	P/B	Div. Yield	EPS Growth	ROAE	EPS
Reliance Communication Ventures	RLCM.BO	1L	575	29,758	16.3	3.7	0.3%	33.0%	25.0%	35.2
Reliance Energy	RLEN.BO	3L	1,568	9,302	32.2	3.4	0.4%	13.8%	11.6%	48.7
Reliance Industries	RELI.BO	1L	2,458	89,638	18.0	3.8	0.8%	34.3%	23.5%	136.8
Reliance Petroleum	RPET.BO	3L	175	19,777	12.6	4.1	0.8%	n/a	32.7%	13.9
Religare Enterprises	RELG.BO	3H	460	878	19.7	n/a	0.0%	53.0%	n/a	23.3
S Kumars Nationwide	SKMK.BO	3M	155	770	15.7	3.2	0.0%	17.6%	22.0%	9.9
Sasken Communication Technologies	SKCT.BO	3H	129	92	8.8	0.8	1.6%	13.1%	8.8%	14.6
Satyam Computers	SATY.BO	1M	434	7,298	14.9	3.5	2.3%	17.1%	26.3%	29.2
Shasun Chemicals & Drugs	SHAS.BO	1M	62	74	4.7	1.1	3.7%	14.8%	25.5%	13.0
Shoppers' Stop	SHOP.BO	3M	473	413	43.4	4.9	0.6%	68.6%	11.8%	10.9
Spice Communications	SPCM.BO	1M	35	597	33.2	4.1	0.0%	1468.6%	13.3%	1.0
State Bank of India	SBI.BO	1L	2,110	33,423	17.9	2.6	0.8%	14.1%	15.5%	117.7
Sterlite	STRL.BO	1L	837	14,882	9.6	2.2	0.5%	37.5%	18.3%	87.0
Sun Pharmaceuticals	SUN.BO	1L	1,226	6,196	18.1	5.1	1.3%	17.0%	32.0%	67.6
Sun TV	SUTV.BO	3M	315	3,109	27.9	7.4	1.4%	31.9%	28.7%	11.3
Suzlon Energy	SUZL.BO	1L	281	10,563	24.4	3.9	0.4%	61.0%	16.5%	11.5
Tata Communications	TATA.BO	2M	508	3,635	21.0	2.0	1.2%	10.0%	9.8%	24.2
Tata Consultancy	TCS.BO	1M	874	21,462	15.0	5.1	1.8%	12.3%	38.4%	58.3
Tata Motors	TAMO.BO	1L	700	6,772	17.5	2.9	1.9%	16.3%	19.7%	40.0
Tata Power Co Ltd	TTPW.BO	1L	1,401	7,641	48.6	4.2	0.8%	16.6%	9.8%	28.8
Tata Tea	TTTE.BO	1L	823	1,276	10.1	1.2	3.0%	41.4%	11.8%	81.7
Tata Tele (Maharashtra)	TTML.BO	3M	35	1,674	n/a	2.9	0.0%	-76.4%	-1.2%	(0.1)
Tech Mahindra	TEML.BO	3H	688	2,095	9.6	3.3	0.4%	20.5%	44.0%	71.4
Thermax	THMX.BO	1L	661	1,974	23.4	7.4	0.9%	13.1%	36.0%	28.2
TVS Motor	TVSM.BO	3M	44	260	9.8	1.1	2.3%	43.3%	11.3%	4.5
Ultratech Cement	ULTC.BO	3M	911	2,846	13.1	3.3	0.5%	-13.0%	28.0%	69.4
Union Bank of India	UNBK.BO	1L	186	2,352	6.2	1.3	2.2%	29.9%	22.3%	29.9
Unitech	UNTE.BO	1M	359	14,629	21.2	9.3	0.1%	68.2%	55.7%	17.0
United Phosphorus	UNPO.BO	1L	335	1,794	12.8	2.1	0.4%	58.3%	19.4%	26.1
United Spirits	UNSP.BO	1L	1,696	4,240	26.2	7.6	0.4%	56.6%	30.4%	64.7
UTV Software Communications	UTVS.BO	1H	817	480	32.3	6.7	0.4%	94.5%	22.9%	25.3
Voltas	VOLT.BO	1M	203	1,682	21.9	8.1	0.6%	35.1%	44.0%	9.3
Wipro	WIPR.BO	1M	435	15,923	16.3	4.3	1.8%	20.4%	29.0%	26.6
Wockhardt Ltd	WCKH.BO	1L	337	925	9.3	2.5	2.4%	21.3%	32.9%	36.3
Yes Bank	YESB.BO	1M	247	1,833	26.9	3.8	0.0%	40.2%	15.2%	9.2
Zee	ZEE.BO	1L	241	2,623	20.4	5.0	2.5%	28.7%	24.9%	11.8

Source: Citi Investment Research

Appendix A-1

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