Union Budget 2011-2012 (First cut)

Stated fiscal consolidation over ambitious

Edelweiss Research

February 2011

Union Budget- Key highlights

Stated fiscal consolidation will be hard to achieve

- Govt announces gross fiscal deficit for FY12 at 4.6% of GDP (against 5.1% of GDP in FY11), which was lower than our expectation of 4.9-5.0% of GDP.
- Net market borrowing for FY12 at INR 3.43 trn, which again is much lower than our expectation of ~INR 4 trn.
- Lower than expected fiscal deficit/market borrowing numbers are mainly due to much lower than expected subsidy bill of INR 1.44 trn as against our expectation of INR 1.88 trn. However, govt. remains committed to provide subsidy through cash and not bonds.
- We believe that there is an upside risk to both fiscal deficit as well as net market borrowing numbers estimated by the government. We expect deficit to be as high as ~5% of GDP for FY12.
- Revenue deficit was estimated at 3.4% of GDP for FY12, same as FY11, indicating no consolidation on revenue front. Besides, estimated revenue deficit is higher than 2.8% prescribed by 13th Finance Commission

Stress on inclusive agenda continues

- Allocation to social sector schemes increases to INR 1,609 bn (17% Y-o-Y), constituting 36.4% of the plan expenditure. Within this allocation to Bharat Nirman amounts to INR 580 bn (compared to INR 480 bn in FY11) and to education amounts to INR 520 bn (24% Y-o-Y).
- MGNREGA has been linked to CPI index for agricultural labour.

Growth continues to be a focus area

- No major changes in indirect taxes in view of continued uncertainty in global economy and to prepare ground for transition to GST. This along with increased social spending is likely to keep consumption growth strong in the economy.
- Thrust on infrastructure continues; allocation of INR 2,140 bn (~ 23% y-o-y) which constitutes 48.5% of plan expenditure. Allowance of tax free bonds of INR 300 bn to be issued by various government departments such as NHAI.

Union Budget- Key highlights contd…

- No meaningful reforms undertaken
  - No announcement on allowing FDI in sectors like retail, insurance.
  - No major step was taken in order to increase the investment activity in the country.
  - No major reform was taken in order to address the supply side pressures plaguing the economy.

Budget at a glance

Budget at a glance (INR Bn)

	FY09	FY10	FY11(BE)	FY11(RE)	FY12(BE)
Revenue Receipts	**5,403**	**5,728**	**6,822**	**7,838**	**7,899**
Tax Revenue (net to Centre)	4,433	4,565	5,341	5,637	6,645
Non-tax Revenue	969	1,163	1,481	2,201	1,254
Capital Receipt	**3,437**	**4,517**	**4,265**	**4,327**	**4,678**
Recoveries of Loans	61	86	51	90	150
Other Receipts	6	246	400	227	400
Borrowings and other Liabilities	3,370	4,185	3,814	4,010	4,128
Total Receipts	**8,840**	**10,245**	**11,087**	**12,166**	**12,577**
Non-plan Expenditure	**6,087**	**7,211**	**7,357**	**8,216**	**8,162**
On Revenue Account of which,	5,590	6,579	6,436	7,267	7,336
Interest Payments	1,922	2,131	2,487	2,408	2,680
On Capital Account	497	632	921	948	826
Plan Expenditure	**2,752**	**3,034**	**3,731**	**3,950**	**4,415**
On Revenue Account	2,348	2,539	3,151	3,269	3,636
On Capital Account	405	495	580	681	779
Total Expenditure	**8,840**	**10,245**	**11,087**	**12,166**	**12,577**
Revenue Expenditure	7,938	9,118	9,587	10,537	10,972
Capital Expenditure	902	1,127	1,500	1,629	1,606
Revenue Deficit	**2,535**	**3,390**	**2,765**	**2,698**	**3,073**
Fiscal Deficit	**3,370**	**4,185**	**3,814**	**4,010**	**4,128**
Primary Deficit	**1,448**	**2,054**	**1,327**	**1,602**	**1,448**
Revenue Deficit (% of GDP)	**4.5**	**5.2**	**4.0**	**3.4**	**3.4**
Fiscal Deficit (% of GDP)	**6.0**	**6.4**	**5.5**	**5.1**	**4.6**
Primary Deficit (% of GDP)	**2.6**	**3.1**	**1.9**	**2.0**	**1.6**

RE: Revised Estimates BE: Budget Estimates

Source: Budget documents, Edelweiss research

Minor changes in direct taxes

- No change in headline corporate tax rate
- Surcharge for domestic companies reduced to 5.0% from 7.5%—largely positive
- MAT hiked from 18% to 18.5%. Further SEZs and units operating under SEZs brought under MAT ambit- negative for both SEZ operators and units functioning within SEZs
- Minor tinkering to personal tax structure- largely favorable to tax payers in low income bracket

Old slab (in INR)	Tax rate
0-160,000	Nil
180,000- 500,000	10%
500,000-800,000	20%
Above 800,000	30%

New slab (in INR)	Tax rate
0-180,000	Nil
180,000- 500,000	10%
500,000-800,000	20%
Above 800,000	30%

Source: Budget documents, Edelweiss research

Sector wise expectations

Sector	Industry/market wishlist	Edelweiss expectation	Announcement in the budget	Impact on sector/company
Auto	Excise duty- to keep it unchanged	Roll back of duty cut is unlikely in this budget	Maintained status quo	Neutral
	MGNREGA	Increased allocation to the scheme	Indexing NREGA wages to CPI	Positive for tractors, two wheelers and cars
	No additional excise on diesel cars	An outside possibility of increasing excise duties	No hike in excise duty for diesel cars	Positive for M&M and partially for Tata Motors and Maruti as the street was assigning high probability to such hike
	Additional incentives for green cars	Support in concessional rate of loans, benefits of accelerated depreciation and softer loans	Excise duty on hybrid/electric vehicles to be reduced from 10% to 5%	Marginally positive for M&M
			To set up National Mission for hybrid and electric vehicles	
			Credit flow for farmers raised from INR 3,750 bn to INR 4,750 bn in 2011-12	Positive for Tractors demand
			Allocation of INR 214,000 crore for infrastructure in 2011-12. This is an increase of 23.3 per cent over 2010-11. This also amounts to 48.5% of total plan allocation	Positive for Trucks and Buses. Company: Tata Motors & AL

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BFSI	Government subsidy/concessions on interest rates to be provided on lending to SEBs, given their weak financial health	Separate subsidy/fund to be created to meet financing requirement of SEBs	Nil	
	Limit of refinancing from IIFCL to commercial bank loans for PPP projects in critical sectors expected to be raised from INR 60 bn	Last year also it was doubled, but considering growth, this year as well limit could be further raised	Nil	
	Tax break on longer tenor deposits	Considering low deposit mobilization and lending skewed towards longer tenor assets, tax break will provide some relief to ALM	Nil	
			Net market borrowings announced at INR 3.43 tn, below expectations of around INR 4 tn	Though we will believe borrowing number will be revised upwards going into FY12, sentimentally it will be positive for banks largely PSU banks
			Allocated INR 60 bn for PSU banks' recapitalisation	Lower than recapitalisation in FY11 and seems it does not include SBI's right issues
			Banking license guidelines to be issued before the end of this fiscal	Clarity to emerge as to who all will be eligible for banking licence
			Equity fund for microfinance institutions of INR 1 bn and for women self help groups of INR 5 bn	Though the quantum is low, it is sentimentally positive as it categorically stated that MFIs are critical for financial inclusion
			Interest subvention limit on housing loans has been raised from INR 1 mn to INR 1.5 mn and priority sector lending limit has been raised to INR 2.5 mn from INR 2 mn	Positive for low-ticket housing financiers
			Interest subvention to farmer repaying loans on time – raised from 2% to 3%	

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Capital goods	Import duty on power equipment for mega power projects; import duty, at 15-20%, to provide a level-playing field to domestic boiler and TG manufacturers	Not expected, owing to strong lobbying by utilities	While new mega or ultra mega power project imports continue to enjoy exempted status in customs and excise duty, domestic players supplying equipment for **expansion** of existing mega or ultra mega power projects were required to pay 10% excise duty, which now stands reduced to 2.5% (in line with concessional basic customes duty of 2.5% on imports)	Positive for domestic BTG players like BHEL, LT etc.

Sector	Industry/market wishlist	Edelweiss expectation	Announcement in the budget	Impact on sector/company
Cement	Uniform rate of excise duty on cement	No change expected	Existing excise duty rates replaced with composite rates having an ad-valorem rate and specific component.	Negative for prices below INR 190/bag and Neutral to marginally positive for prices above INR 190/bag
	Abatement on excise duty levied on MRP basis	No change expected	No announcement	Nil
	Zero import duty on coal, pet coke, gypsum and other products	No change expected	Customs duty on pet coke and gypsum proposed to be reduced to 2.5% from 5%	Marginally positive for Shree Cements (~2-3% positive impact on earnings) and broadly neutral for the sector.
			Fly ash to attract 1% excise duty without Cenvat credit facility	Marginally negative as fly ash is just 2/3% of the cost of production
			5% excise duty on RMC with 1% concessional duty without Cenvat Credit facility	Neutral as the industry will pass on the increase to consumers

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Construction	Relaxation of ECB norms	May happen due to liquidity crunch	No announcement	Neutral
	Increase in central govt. outlay for roads and urban infra	Likely to happen as infra remains a top priority for govt.	Allocation for infra increased to INR 2.14 trillion, which is 23.3% higher than current year	Positive
	Further clarity on refinancing/takeout provisions for IIFCL funding	Likely to happen, but may not result in immediate benefits	No announcement	Neutral
			The FII limit for investment in corporate bonds, with residual maturity of over five years issued by companies in infrastructure sector, is being raised to USD 25 bn from USD 5 bn earlier	Positive

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FMCG	Rural initiatives on income generation	We expect this to continue	Allocation under Rashtriya Krishi Vikas Yojana to be raised to INR 78.60 bn; To index NREGA wage rates to CPI	Positive for FMCG companies
	Tax exemption limit	We expect this to increase	Tax exemption limit enhanced from INR 1,60,000 to INR 1,80,000 to give consumers more disposable income	Positive for FMCG/Retail companies
	Excise duty for cigarettes	We expect excise to increase by 8-10% for cigarettes	No increase in excise duty	Positive for tobacco companies i.e. ITC, Godfrey Philips and VST Industries. We feel that since legal business in cigarettes was pressurized, Govt has likely left legal cigarettes untouched. Cheap, contraband cigarettes were flourishing (already ~9% of the industry)
	MAT rate	Increase may happen as it could be a step towards direct tax code	MAT raised to 18.5% of book profits (from 18.0%); surcharge on MAT has reduced to 5% (from 7.5% earlier)	Marginally negative for FMCG companies under MAT i.e. Dabur, Emami, Marico and Godrej Consumer| effective MAT rate has increased from 19.93% to 20.007% i.e. MAT rate increase of ~8bps
	Service tax on Hotel accomodation		Levied service tax on hotel accommodation in excess of declared tariff of INR 1,000 per day with a abatement of 50%, so that the effective burden is only 5% of the amount charged	Marginally negative for ITC's Hotel business
	Palm oil		INR 3 bn provided to improve production of pulses (to bring 60k hectares more in edible oil plantations)	Positive for FMCG (HUL, Marico, GCPL) companies exposed to import of edible oils
	Cold storage projects		Cold storage projects classified as infrastructure sector	Positive for FMCG companies in Foods category

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Fertiliser			To provide boost to production in agriculture space, benefits of investment linked deduction are extended to fertiliser production	Positive
			Capital investment in fertiliser production to be included under infrastructure sub-sector	Positive
			Reiterated the proposal to have direct transfer system of cash subsidy to people with regard to fertilisers, from the current system of payment of subsidies to fertiliser companies, which is dependent on the successful implementation of the UID project	Positive
			Reiterated that the payment of subsidy to fertiliser companies would be paid in cash and not in bonds	Positive
			Though mentioned that extension of the NBS regime to cover urea is under active consideration; however no timeline has been given and current uncertainty over urea policy continues	Negative

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Hospitality and airlines				
Airlines			Increased service tax on domestic and international airfares by INR 50 and INR 250, respectively.	Negative for airlines companies
			Propose to tax travel by higher classes on domestic travel at the standard rate of 10% to bring it par with the higher classes on the international travel.	
Hotels			Hotel accommodation in excess of declared tariff of INR 1000 to get an abatment of 50%, keeping the service tax impact to be 5%.	Negative for hotel companies
			Air-conditioned restaurants serving liquor by a license to get an abatment of 70%, keeping the service tax impact at 3%.	

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IT	Extension of the sunset clause on tax exemption for software technology parks under Sec. 10A / B, which is due to expire in March 2011	Unlikely that the sunset clause on tax exemption will be extended	Exemption not extended	**Neutral,** as the increase in effective tax rate is already factored by the street
			MAT imposed on profits from SEZ	**Negative.** However, it will only have incremental cash flow impact and no p/l impact. Further, for companies where the effective tax rate is already higher than MAT rate (18.5%), there is no cash flow impact
				Cash flow impact seen on eClerx, Hexaware, Mphasis

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Media	FDI norms get liberalised for some of the segments like radio, DTH and cable	This may happen as the recommendations have been given by TRAI	None	
	Rationalisation and parity in the service tax paid by TV and radio broadcasters on revenues accrued by them from ads	This seems unlikely, as this demand has been pending for many years	None	
	Provision for doubtful debt be allowed as expense in MAT profit calculation	Looks unlikely	None	
			Tax exemption limit enhanced from INR 1,60,000 to 1,80,000	Positive for DTH companies
			Concessional basic Custom Duty of 5 per cent and CVD of 5 per cent available to newspaper establishments for high speed printing presses extended to mailroom equipment.	Positive for print companies
			Jumbo rolls of cinematographic film fully exempted from CVD by providing full exemption from Excise Duty.	Positive for movie producers

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Metals & Mining	Industry looking for increased infra spending	Increased thrust on infrastructure spending which has been slow currently		
	Increase import duty on HR coil from 5% to 10%	No change	No change	Neutral
	Increase in import duty on ferro alloys from 5% to 7.5%	No change	Reduced customs duty from 5% to 2.5%	Marginal positive for all steel players, negative for ferro alloy makers
		Low probability: Increase in export duty on fines from current level of 5% to 15%	Ad valorem export duty of 20% both on lumps and fines	Negative for iron ore exporters. Sesa Goa worst impacted
		Specifics regarding coal regulator which was introduced last year	No announcement	
			Fully exempt basic customs duty on stainless steel scrap	Positive for Jindal Stainless/ JSL

Sector wise expectations

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Oil & Gas	Cut in import duties on crude from 5% currently to NIL	No change expected	No change in excise and import duties on crude and petroleum production	This will lead to continuance of higher under recoveries for the PSUs
			Sunset clause to impose MAT on SEZ units/developers FY12 onwards	No impact on RIL's EPS as high cash taxes will be offset by lower deferred taxes. However, there will be a cash flow impact and RIL's SOTP will reduce by INR ~15/share (~1.3%)
			Import duty on petroleum coke reduced from 5.15% to 2.58%	This will be marginally negative for pet-coke producing refineries. Overall, the import duty protection on an average Indian refinery will fall from 1.11% to 1.02%. Refining margins will fall by ~USD 0.08/bbl
			GoI to directly provide cash subsidies for kerosene and LPG to people living below the poverty line. Rollout expected by March 2012	Positive for OMCs as this will reduce the burden of under recoveries. We believe the implementation target is aggressive. Only expect to be rolled once the UID project gathers pace, which is still a long way ahead. UID only has 2.0 mn population covered till date
			Overall corporate tax rate reduced from ~33.2% to ~32.45%	Profits for full tax-paying companies will increase by 1.16%. All PSU companies are full tax paying
			MAT increased from ~19.93% to ~20.01%, increase of ~7.7bps	This will have marginal impact of profits
			Tax benefits from NELP blocks no longer available for NELP blocks awarded after 31 March 2011	Attractiveness of the NELP reduces

Sector wise expectations

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Pharma	Excise duty structure to remain at current levels	Parity between formulations (4% excise duty) and APIs (10% excise duty) to reduce	Increase in excise duty form 4% to !	Marginally negative for formulation players; Largely to be passed on
	Extension of the list for life saving drugs- List should be expanded to cover more drugs	Likely to be announced for certain categories	IV fluids and vaccines to attract 1% excise duty	Marginally negative for Claris Lifesciences, Panacea Biotec and GSK
	Tax holiday on healthcare infrastructure in tier-2 and tier-3 towns; should be extended from 5 years to 10 years	Likely to be announced	Nil	
			Service tax of 5% (with 50% abatement) on Inpatient treatments by hospitals with >25 beds. The scope of service tax also includes diagnostics services and consultation fees on outpatients.	Service tax to be paid by patients, hence no negative impact in near term. Long term negative impact on price realizations for high-end specialty treatments in specialty hospitals.
	200% weighted deduction on R&D; should be extended to standalone R&D and outsourcing	Not expected	Nil	
	Extension of Sun Set clause	Not expected	Propose to levy MAT on SEZ units	Negative for Companies like Cipla (1% of EPS); Divi's (3-4% of EPS) and Ipca Labs (2-3% of EPS). However no impact on DRRD, LPC, Sun Pharma, Glenmark , Torrent and Aurobindo.Ranbaxy has not commenced its operation from SEZ, therefore no impact.
	Reduction in Surcharges	Not expected	Reduced from 7.5% to 5%	Positive for full tax paying companies such as GSK, Pfizer and other MNCs

Sector wise expectations

Sector	Industry / market wishlist	Edelweiss expectation	Announcement in the budget	Impact on sector / company
Real Estate	Increase in exemption limit for interest payment and on loan repayments	Nil	Nil	NA
			Home loan limit under interest subvention scheme increased to INR 1.5 mn from INR 1 mn and home value limit increased to INR 2.5 mn from INR 2 mn	Positive for developers with presence in affordable housing and in Tier II/III cities - Unitech, Puravankara, HDIL, Parsvnath, Ansal Properties and Omaxe
			Both SEZ developers/units to come under MAT	Negative for developers with presence in SEZs - DLF, Unitech and Mahindra Lifespaces, but already factored in estimates

Sector	Industry / market wishlist	Edelweiss expectation	Announcement in the budget	Impact on sector / company
Retail	FDI norm gets liberalized for different formats	This could happen as many government departments are supporting this and this could be used to fight food inflation by getting higher investments in cold storage, technology and logistics	No mention	Negative for Retailers
	Tax exemption limit	We expect this to increase	Tax exemption limit enhanced from INR 1,60,000 to INR 1,80,000 to give consumers more disposable income	Positive for FMCG/Retail companies
	Excise duty on branded garment players		To levy central excise duty of 10% on branded clothes	Slightly negative for Retailers
	Excise duty for Jewellery manufacturers		Concessional excise duty of 1% without CENVAT credit facility is being imposed on the articles of jewellery manufactured or sold under a brand name	Slightly negative for Retailers
	Cold storage projects		Cold storage projects classified as infrastructure sector	Positive for Retailers looking to set-up back end supply chain

Sector wise expectations

Sector	Industry / market wishlist	Edelweiss expectation	Announcement in the budget	Impact on sector / company
Telecom	No import duty to be imposed on handsets	Import duty is likely to be imposed on handsets, to encourage local manufacturing	Nil	Nil

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