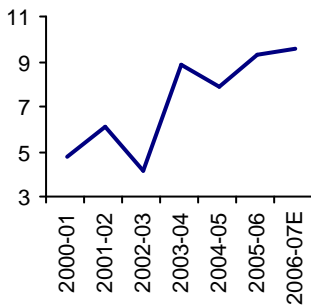


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# Union Budget Analysis FY2008

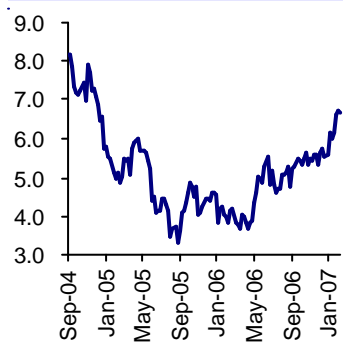
## Pause inflation, play growth

### GDP growth (%)



Source: Economic Survey 2006-07

### Inflation (%)



Source: Bloomberg

- Continued focus on sustainable long-term growth through focused investments in infrastructure and agriculture.
- Inclusive growth sought through focus on agriculture, social initiatives and small and medium enterprises.
- Supply side initiatives taken to control inflation in the longer-term. Focus on raising agricultural production and productivity with a view to improve supplies. Confident of containing inflation in the short-term through fiscal and monetary measures (by RBI)
- Fiscal prudence shown by adhering to FRBM targets. Fiscal deficit targeted at 3.3% of GDP and revenue deficit at 1.5% of GDP in 2007-08. Non-plan expenditure projected to rise only by about 6.5% in 2007-08 v/s about 31% rise in plan expenditure.
- Tax reforms continue with peak customs duty down to 10%, re-iteration of April 1 2010 as the deadline for GST. CST phase-out process started. Continuity maintained in direct taxes with minor changes.
- Utilizing the increased corporate earnings to improve tax revenues. In addition, Dividend Distribution Tax increased to 15% v/s 12.5%, additional secondary and higher education cess of 1%.
- No changes in securities transaction tax and capital gains tax are a positive for capital markets. Short selling by institutions has been allowed (supported by lending/borrowing mechanism), in order to enable better price discovery and reduce volatility.
- Overall, we see the Budget helping the economy maintain its high growth through additional investments. We share the Government's optimism on containing inflation in the longer term and promoting equitable growth provided there is effective implementation of the proposals.
- Negative implications on few sectors including cement, information technology and construction may continue to engage the market's attention in the short-term. However, we see the continued growth in the economy helping overall corporate profit growth, in turn positively impacting the market in the longer term.

### Sectoral impact

#### Budget Impact Sectors

Positive	Capital Goods, Electrical Equipments, Food Processing/FMCG, Hotels, Logistics, Oil & Gas, Pharma, Textiles
Neutral	Auto Components, Automobiles, Banking, Media, Metals, NBFC, Sugar
Negative	Cement, Construction, Information Technology

Source: Kotak Securities - Private Client Research

## FOCUS ON GROWTH THROUGH INVESTMENTS

*Focus on growth in line with 11th Five Year plan*

The Finance Minister has expectedly maintained his focus on sustaining the high growth in the economy. This is in line with the overall target of 9% growth in the Eleventh Five Year plan, including 10% growth towards the end of the plan.

*31% rise in plan expenditure*

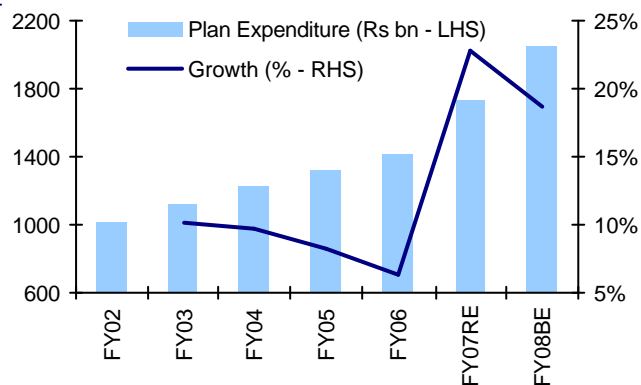
With India still being an investment-led economy, the Budget has allocated increased amounts for investments in infrastructure, agriculture and social initiatives. This is adequately reflected in the 31% rise in plan expenditure, mainly towards these areas. On the other hand, the non-plan expenditure is expected to rise only by about 6.5%.

### Plan allocation (Rs bn)

	FY06	% of total	FY07RE	% of total	FY08BE	% of total
Agriculture & Allied Activities	59.07	2.9	73.91	3.0	85.58	2.7
Rural Development	167.16	8.1	182.68	7.5	203.42	6.4
Irrigation & Flood Control	4.18	0.2	4.62	0.2	5.07	0.2
Energy	537.20	26.2	688.25	28.2	791.58	24.7
Industry and Minerals	100.63	4.9	125.88	5.2	204.34	6.4
Transport	404.12	19.7	498.19	20.4	715.89	22.4
Communications	175.25	8.5	178.51	7.3	258.12	8.1
Science Technology & Environment	60.32	2.9	67.74	2.8	88.16	2.8
General Economic Services	28.14	1.4	25.66	1.1	36.32	1.1
Social Services	512.71	25.0	591.43	24.2	803.15	25.1
General Services	4.60	0.2	5.42	0.2	8.29	0.3
<b>Grand Total</b>	<b>2,053.38</b>	<b>100.0</b>	<b>2,442.29</b>	<b>100.0</b>	<b>3,199.92</b>	<b>100.0</b>

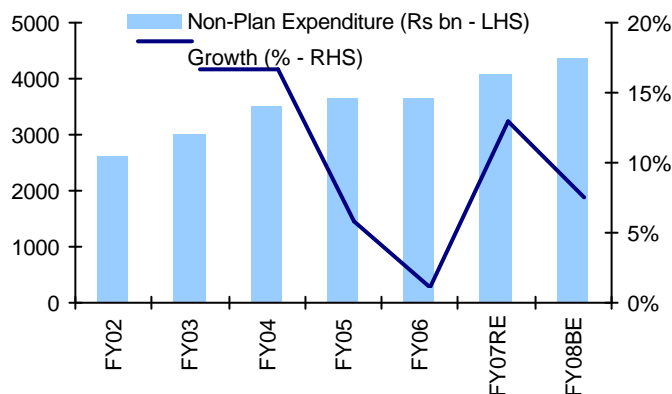
Source: Budget document 2007-08; Note: RE: Revised Estimate; BE: Budget Estimate

### Plan expenditure



Source: Economic Survey 2006-07, Annual Budget FY2006-07

### Non-plan expenditure



Source: Economic Survey 2006-07, Annual Budget FY2006-07  
Note: FY08BE numbers exclude the Rs.400 Bn on account of transactions relating to transfer of RBI's stake to the Government

*Continued focus on power, highways and communications*

As can be seen in the accompanying table, within infrastructure, there has been an increased allocation to power, transport and communications. The major provisions related to infrastructure include

- Allocation of Rs.65 bn for National Highway Development Programme and Rs.37 bn for development of national highways.
- Awarding at least two ultra mega power projects (UMPP) by July 2007 and facilitate setting up of merchant power projects by private parties.
- Increase in allocation to Rajiv Gandhi Grameen Vidyutikaran Yojana from Rs.30 bn to Rs.40 bn.

*Public-private partnership stressed on*

The Budget has also stressed on the importance of the public private partnership in infrastructure development by setting up a revolving fund to quicken project preparation with a corpus of Rs.1 bn. The government has decided to set up two foreign subsidiaries in order to use a part of foreign exchange reserves of \$185 bn in more productive way for infrastructure projects.

## INCLUSIVE GROWTH

### *Significant increase in outlay for social initiatives*

We see Budget 2007-08 continuing to focus on equitable growth in the long-term through focused investments in agriculture and in several social initiatives. The Government is cognizant of the fact that high growth in the economy can be sustained only if it is equitable and inclusive in nature.

As displayed in the accompanying table, social initiatives like education, public health and employment have seen increased allocation, in a bid to make the growth more inclusive. The Budget seeks to increase allocation for Bharat Nirman by 31.6%, education by 34.2% and family welfare and health by 21.9%.

With about 62.9% of the population expected to be in the earning age of 18-64 years by 2026, increasing the demographic dividend is high on the Government's agenda. Major initiatives include:

### Education

- Increase in allocation for school education by 35% to Rs.231 bn of which, Rs.107 bn is for Sarva Shiksha Abhiyan.
- Target for adding 200,000 more teachers and 500,000 more schools,
- National Means-cum-Merit scholarship to be introduced to arrest drop out ratio from schools from standard VII, with each eligible student to be given Rs.6000 per annum. Total outlay of Rs.7.5 bn to cover about 100,000 students,
- An allocation of Rs.29 bn for technical education

### Employment

- Allocation of Rs.120 bn for National Rural Employment Guarantee Scheme, coverage to expand from 200 to 330 districts,
- Increased allocation under the Swarna Jayanti Shahari Rozgar Yojana to increase urban employment and for promoting self employment among rural poor

### Public health

- Allocation of Rs.110 bn for National Rural Health Mission. All districts to complete preparation of District Health Action Plans by March 2007
- Target to cover all habitations and settlements under the Integrated Child Development Services program,

### Small-scale sector

The Budget has also sought to provide relief and encouragement to the small-scale sector by including specific provisions like raising the exemption limit for excise duty from Rs.10 mn to Rs.15 mn and the exemption limit for service tax from Rs. 400,000 to Rs.800,000.

## AGRICULTURE - INCREASED ALLOCATIONS TO HELP GDP GROWTH AND CONTROL INFLATION

### *Investments in agriculture needed for sustainable GDP growth and control in inflation*

With the Government focusing on sustaining growth, the contribution of agriculture becomes important. With the sector expected to grow only 2.7% in FY07, the allocations for the same have increased in the Budget.

With inflation crossing 6.5% in recent weeks, the Finance Minister has indicated his intention to ease supply bottlenecks in the sector. The measures are expected to yield higher production and productivity in agriculture, which, in turn, are expected to raise supplies of agricultural products.

The Finance Minister has resorted to taking longer-term structural measures to tackle inflation while expressing confidence in bringing down inflation in the near term through fiscal and monetary measures. The fiscal measures in the Budget, which are anti-inflation, include reducing peak customs duty to 10% from 12.5% (on non-agricultural products), reducing excise duty on specific items like petrol and diesel and also keeping the fiscal deficit under check. Measures like imposing differential excise duty on cement may not lead to desired impact on inflation.

The various measures taken by the Budget are enumerated in the accompanying table.

### Agriculture Sector Initiatives

Issues	Initiatives
Farm credit	<ul style="list-style-type: none"> <li>■ Target of Rs.2250 bn for 2007-08 with an addition of 50 lakh new farmers to the banking system</li> <li>■ Provision of Rs.16.8 bn for 2% interest subvention for short-term crop loans</li> <li>■ Rs.124 bn on water related schemes</li> </ul>
Mission for Pulses	<ul style="list-style-type: none"> <li>■ To fund the expansion of Indian Institute of Pulses Research, Kanpur, and offer other producers a capital grant or concessional financing to double production of certified seeds within a period of three years</li> </ul>
Plantation Sector	<ul style="list-style-type: none"> <li>■ Financial mechanisms for re-plantation and rejuvenation to be put in place for coffee, rubber, spices, cashew and coconut</li> </ul>
Irrigation	<ul style="list-style-type: none"> <li>■ Outlay to be increased from Rs.71.2 bn to Rs.110 bn</li> <li>■ Additional irrigation potential of 900,000 hectares to be created</li> </ul>
Water Resources Management	<ul style="list-style-type: none"> <li>■ World Bank loan agreement signed with Tamil Nadu for Rs.21.8 bn to restore 5,763 water bodies having a command area of 400,000 hectares</li> <li>■ Agreement for Andhra Pradesh expected to be concluded in March 2007 to cover 3,000 water bodies with a command area of 250,000 hectares</li> </ul>
Ground Water Recharge	<ul style="list-style-type: none"> <li>■ 100% subsidy to small and marginal farmers and 50% subsidy to other farmers to be given to divert rain water into 'dug wells'</li> </ul>
Agricultural Insurance	<ul style="list-style-type: none"> <li>■ National Agricultural Insurance Scheme to be continued for Kharif and Rabi 2007-08 with a provision of Rs.5 bn</li> </ul>
Fertiliser Subsidies	<ul style="list-style-type: none"> <li>■ A pilot programme to be implemented for delivering subsidy directly to farmer</li> </ul>
Rural Infrastructure Development Fund	<ul style="list-style-type: none"> <li>■ Corpus of RIDF-XIII to be raised from Rs.100 bn to Rs.120 bn</li> <li>■ Separate window for rural roads to continue with a corpus of Rs.4,000 crore</li> </ul>
Training of Farmers	<ul style="list-style-type: none"> <li>■ Institutions like Indian Council of Agricultural Research to train 100 trainers and 1000 farmers every year</li> <li>■ Interest free loan of Rs.3 crore to be provided to each institution to create a corpus fund</li> </ul>

Source: Budget document 2007-08

## FISCAL PRUDENCE

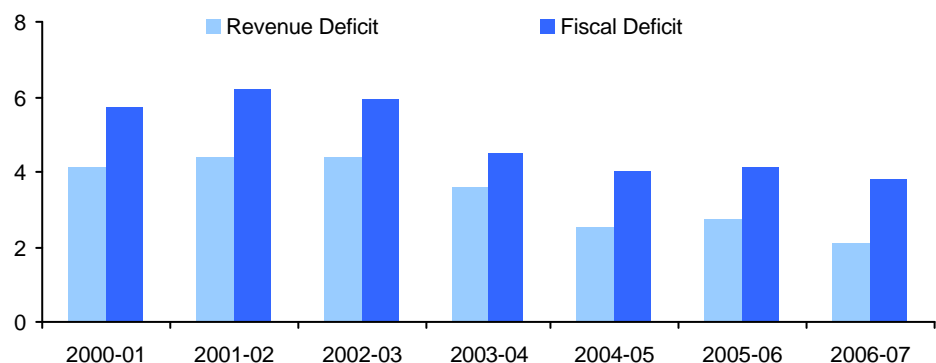
*Fiscal deficit targeted at 3.3% of GDP - A positive*

We believe one of the cornerstones of the budget is reducing the fiscal and revenue deficit. The FM has exercised fiscal prudence by adhering to the FRBM targets. The fiscal deficit is expected to reduce to 3.3% of GDP in 2007-08 while the revenue deficit is expected to reduce to 1.5% of GDP.

This has been done partly by restricting the increase in non-plan expenditure to just about 6.5%. Plan expenditure, on the other hand, is expected to grow by about 31% during the year.

Reducing the deficit helps improve international ratings, which, in turn, makes borrowings cheaper. We believe this is important also due to the fact that lower market borrowings will restrict increase in interest rates.

### Chart showing fiscal and revenue deficit (%)



Source: Budget document 2007-08

## TAX REFORMS CONTINUE, SOME SURPRISES NOTWITHSTANDING

The Finance Minister has largely continued with the tax reforms process. The peak import duty has been cut from 12.5% to 10%, which is in line with the ultimate goal of bringing these down to Asean levels.

*Reduction in peak customs duty, phase out of CST initiated, no increase in rate of service tax*

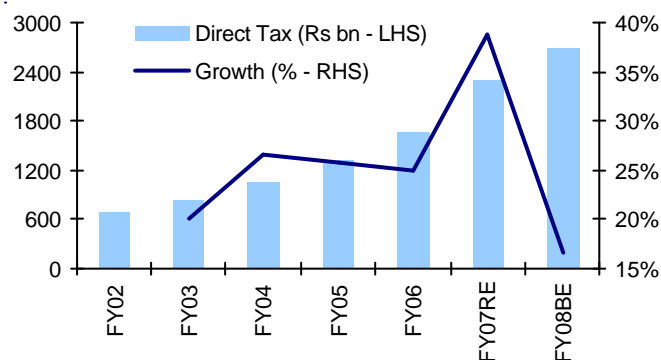
Specific cuts in steel scrap and seconds, in coking coal and in chemicals/plastics like PTA, MEG, etc are expected to partly help in containing inflation. However, agricultural products have been excluded with a view to restrict competition to these products.

The Finance Minister has reiterated his goal of introducing the unified Goods and Services Tax by April 1 2010. In order to achieve this, the Budget has initiated the process of abolishing the Central Sales Tax by reducing it from 4% to 3%. There have been cuts in excise duties in several items like petrol and diesel.

*Increase in DDT and education cess - negative surprises*

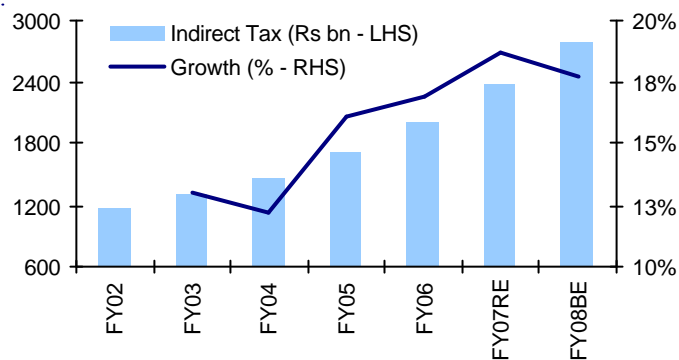
On the direct tax front, the increase in Dividend Distribution Tax (DDT) came as a negative surprise and so did the addition of secondary and higher education cess by 1%, to fund secondary school initiatives, offsetting the small increase in the basic exemption by Rs.10,000. The education cess will impact companies all across, albeit marginally.

### Direct taxes



Source: Economic Survey 2006-07, Annual Budget FY2006-07

### Indirect taxes



Source: Economic Survey 2006-07, Annual Budget FY2006-07

## Capital market outlook - Long-term positive

There have been no changes in the capital gains tax and securities transaction tax, which is a positive. Also, allowing short selling by institutions through the borrowing/lending mechanism will allow better price discovery in the markets.

The exchangeable bonds would help Indian companies in cross border acquisition by raising funds via domestic bond markets by using cross holdings as collateral.

We believe the Budget has done the right thing by focusing on sustainable long-term growth of the economy. While structural measures to control inflation may have an impact in the longer term, we expect the Government to take fiscal and monetary steps to control inflation during the year.

On the corporate profits front, we do not expect a major impact due to the 1% extra educational cess. We expect dividend payments to be adjusted to accommodate the higher dividend distribution tax. However, this may make dividend yields in several stocks unattractive as compared to the returns outside the capital markets.

*We maintain our long-term positive outlook on the markets*

The markets have reacted negatively to the provisions relating to specific sectors like IT, cement and construction. While these factors are expected to keep the markets range-bound in the near term, we expect the economic growth and investments to fuel corporate profits in the medium to long-term and remain positive on the long-term prospects of the markets.

## CENTRAL GOVERNMENT FINANCES

Central Government Finances (Rs bn)						
	FY06	FY07BE	FY07RE	% Gth	FY 08BE	% Gth
<b>REVENUE</b>						
<b>Tax Revenue</b>						
Corporation Tax	1,012.77	1,330.10	1,464.97	10.1	1,684.01	15.0
Income Tax	559.76	734.09	727.10	-1.0	868.29	19.4
Excise Duty	1,112.26	1,190.00	1,172.66	-1.5	1,302.20	11.0
Import Duty	650.67	770.66	818.00	6.1	987.70	20.7
Service Tax	230.55	345.00	381.69	10.6	502.00	31.5
Other Taxes	95.51	51.68	114.06	120.7	137.02	20.1
<b>Gross Tax Revenue</b>	<b>3,661.52</b>	<b>4,421.53</b>	<b>4,678.48</b>	<b>5.8</b>	<b>5,481.22</b>	<b>17.2</b>
Less: States' share	943.85	1,134.48	1,203.77	6.1	1,424.50	18.3
<b>Net tax Revenue</b>	<b>2,717.66</b>	<b>3,287.05</b>	<b>3,474.71</b>	<b>5.7</b>	<b>4,056.72</b>	<b>16.7</b>
Non-tax Revenue	1,591.74	1,614.49	1,763.66	9.2	1,779.76	0.9
<b>Gross Receipts</b>	<b>4,309.40</b>	<b>4,901.54</b>	<b>5,238.37</b>	<b>6.9</b>	<b>5,836.47</b>	<b>11.4</b>
<b>EXPENDITURE</b>						
<b>Revenue Expenditure</b>						
Interest	1,326.30	1,398.23	1,461.62	4.5	1,589.95	8.8
Defense	482.11	515.42	515.42	0.0	540.78	4.9
Subsidies	475.20	462.13	534.63	15.7	543.30	1.6
Admn & Sockal Services	995.42	1,068.52	1,110.16	3.9	1,161.43	4.6
<b>Plan Expenditure</b>	<b>1,118.58</b>	<b>1,437.62</b>	<b>1,445.84</b>	<b>0.6</b>	<b>1,743.54</b>	<b>20.6</b>
<b>Total Revenue Expenditure</b>	<b>4,397.61</b>	<b>4,881.92</b>	<b>5,067.67</b>	<b>3.8</b>	<b>5,579.00</b>	<b>10.1</b>
<b>Capital Expenditure</b>						
Defense	323.38	374.58	344.58	-8.0	419.22	21.7
Plan Expenditure	287.80	289.66	281.46	-2.8	307.46	9.2
Loans	52.44	93.75	122.66	30.8	499.53	307.2
<b>Total Capital Expenditure</b>	<b>663.62</b>	<b>757.99</b>	<b>748.70</b>	<b>-1.2</b>	<b>1,226.21</b>	<b>63.8</b>
<b>Plan Exp on Rev &amp; Cap a/c</b>	<b>1,406.38</b>	<b>1,727.28</b>	<b>1,727.30</b>	<b>0.0</b>	<b>2,051.00</b>	<b>18.7</b>
Non-plan Exp on Rev & Cap a/c	3,654.85	3,912.63	4,089.07	4.5	4,754.21	16.3
<b>Total Expenditure</b>	<b>5,061.23</b>	<b>5,639.91</b>	<b>5,816.37</b>	<b>3.1</b>	<b>6,805.21</b>	<b>17.0</b>
<b>Deficits</b>						
	<b>FY06RE</b>	<b>FY07BE</b>	<b>FY07RE</b>	<b>FY08BE</b>		
Fiscal Deficit	1,464.35	1,486.86	1,523.28	1,509.48		
<i>% of GDP</i>	<i>4.1</i>	<i>3.8</i>	<i>3.7</i>	<i>3.3</i>		
Revenue Deficit	922.99	847.27	834.36	714.78		
<i>% of GDP</i>	<i>2.6</i>	<i>2.1</i>	<i>2.0</i>	<i>1.5</i>		
Primary Deficit	138.05	88.63	61.36	(80.47)		
<i>% of GDP</i>	<i>0.4</i>	<i>0.2</i>	<i>0.1</i>	<i>-0.2</i>		

Source: Government of India, Annual Budget FY2007-08

## BUDGET HIGHLIGHTS FY2007-08

Changes in direct taxes		
Item	Pre Budget	Post Budget
Corporate Tax Rate	30%	30%
Individual tax slab	Threshold limit of Rs.100,000	Threshold limit rose Rs.10,000 in cas of all assesses
Surcharge on income tax	Taxable in all cases	Firms and companies with a taxable income of Rs10mn or less exempted
MAT	10%	Extended to income in respect of which deduction is claimed under sections 10A and 10B
Deduction under section 36(1)(viii)	40% of the profits	Restricted to 20% of profits each year
Capital gains bonds under section 54EC	Limit of Rs5mn per investor per year	Status quo maintained
Dividend distribution tax	12.5%	Increased to 15%
Cess on taxes	2%	An additional 1% cess to fund secondary education and higher education

Source: Budget document 2007-08

### Service Tax

- Exemption limit for small service providers to be raised from Rs.400000 to Rs.800000
- Extension of service tax to following
  - a) Services outsourced for mining of mineral, oil or gas
  - b) Renting of immovable property for use in commerce or business (residential properties, vacant land used for agriculture and similar purposes, and land for sports, entertainment and parking purposes & immovable property for educational or religious purposes to be excluded)
  - c) Development and supply of content for use in telecom and advertising purposes
  - d) Asset management services provided by individuals and design services;
  - e) Services involved in execution of a works contract with an optional composition scheme under which tax will be levied at only 2% of the total value of works contract.
- Exemption to following services:
  - a) Services provided by Resident Welfare Associations to their members who contribute Rs.3000 or less per month for services rendered
  - b) Services provided by technology business incubators, their incubates whose annual business turnover does not exceed Rs.50 lakhs to be exempt for first three years
  - c) Clinical trial of new drugs to make India a preferred destination for drug testing.

Source: Budget document 2007-08

<b>Change in Indirect Taxes (%)</b>		
	<b>Pre-budget</b>	<b>Post-budget</b>
<b>CUSTOMS DUTIES</b>		
Non-agricultural products	12.5	10
Most Chemical and Plastics	12.5	7.5
Seconds and defectives of steel	20	10
Coking coal irrespective of ash content	10	Nil
Polyester fibres and yarns	10	7.5
DMT, PTA and MEG	10	7.5
Cut and polished diamonds	5	3
Rough synthetic stones	12.5	5
Un worked corals	30	10
Drip irrigation systems, agricultural sprinklers	7.5	5
Food processing machinery	7.5	5
Medical equipment	12.5	7.5
Crude and refined edible CVD	4	Nil
Sunflower oil both crude and refined	-	15% Reduction
Pet foods	30	20
Dextrose Monohydrate (Derivative of cornstarch)	30	20
Watch dials and movements and umbrella parts	12.5	5
15 specified machinery for pharma and biotech	7.5	5
Private import of aircraft including helicopters	0	3
Export of iron ores concentrates	0	Rs 300/ton
Export of chrome ores and concentrates	0	Rs 2000/ton
<b>EXCISE DUTIES</b>		
Ad valorem component of excise duty on petrol and diesel	8%	6%
Exemption limit for small scale industry (SSI)	Rs 1 crore	Rs 1.5 crore
Umbrellas, parts of footwear, Plywood	16%	8%
Bio diesel	-	Nil
Water purification devices	-	Nil
Pipes used for carrying water	-	Nil
Food mixes including instant mixes	(0-16%)	Nil
Biscuits with retail price less than Rs.50 per kg	16%	Nil
Cement sold at not more than Rs 190 per bag	Rs.400 per tonne	Rs.350 per tonne
Cement sold at more than Rs 190 per bag	Rs.400 per tonne	Rs.600 per tonne
Cigarettes	-	5% Increase
Duty on pan masala not containing tobacco	66%	45%
Duty on ATF used for small aircraft with take off mass less than 40000 Kg	As per sales tax of the respective states (Up to 30%)	3% CST

Source: Budget document 2007-08

## SECTOR SUMMARY

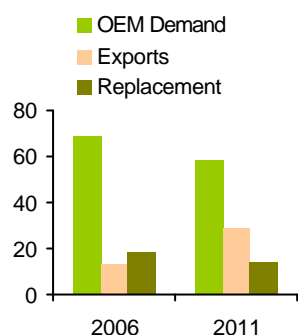
Sector summary		
Sector	Budget Impact	Top Picks
Auto components	Neutral	Amtek India, Subros, Tube Investments
Automobiles	Neutral	Bajaj Auto, Mahindra & Mahindra, Maruti
Banking	Neutral	HDFC Bank, ICICI Bank, J&K Bank, UTI Bank
Capital Goods	Positive	L&T, Mather & Platt Pumps, AIA Engineering, Everest Kanto Cylinder
Cement	Negative	India Cement, Shree Cement
Construction	Negative	Era, Madhucon, Patel Engg, Nagarjuna Const
Electrical Equipments	Positive	Crompton Greaves, Easun Reyroll
Food Processing / FMCG	Positive	Gujarat Ambuja Exports, Riddhi Siddhi Gluco Biols
Hotel	Positive	-
Information Technology	Negative	Infosys, TCS, HCL Tech, Satyam, Zensar, NIIT Tech
Logistics	Positive	Allcargo Global Logistics, CONCOR, Gateway Distriparks, Gati
Media	Neutral	ENIL, UTV Software, HT Media
Metals	Neutral	-
Oil & Gas	Positive	ONGC, HPCL, BPCL, Great Offshore, GSPL, IGL
Pharmaceuticals	Positive	Alembic, Aventis, Cipla, Jubilant, Nicholas Piramal, Panacea
Power	Neutral	-
Sugar	Neutral	-
Textiles	Positive	GHCL, JBF Industries, Vardhman Polytex

Source: Kotak Securities - Private Client Research

# SECTOR IMPACT ANALYSIS

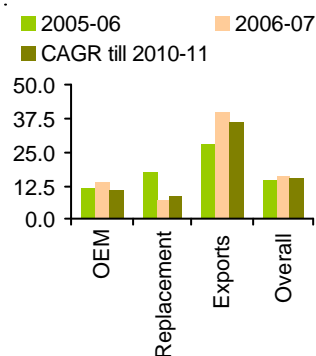
**BUDGET IMPACT: NEUTRAL****AUTOMOBILES & AUTO ANCILLARIES****BUDGET HIGHLIGHTS & IMPACT**

Share of ancillary exports to double by 2011



Source: Cris Infac

Ancillary demand projection growth (%)



Source: Cris Infac

- The peak rate of customs duty is proposed to be reduced from 12.5% to 10%.

**Impact:** This should not impact low-end auto component manufacturers given the labor arbitrage existing in the country in terms of product import. On the other hand, it should marginally benefit companies like Subros and Maruti having high import content.

- Status quo maintained on excise duty front

**Impact:** We remain positive on the overall demand growth for two-wheelers and four-wheelers in the future. Our confidence also stems from the fact that India's GDP is in a sustained growth trajectory and its impact would lead to higher per capita income. Given the current penetration levels there is ample scope for the industry to sustain 13-14% CAGR in the next three to four years.

- On the infrastructure spend front, Rs.246.03 bn has been allocated to the Bharat Nirman project (from Rs.186.96 bn last year) and the Rural Infrastructure Development Fund outlay has been raised to Rs.120 bn (from Rs.100 bn last year).

**Impact:** The government's thrust on infrastructure augurs well for the future prospects of the auto sector. We believe higher focus on rural (specially agriculture) development would lead to higher purchasing power in the rural area resulting in higher demand pull in future years.

- The weighted deduction of 150% for R&D expenditure incurred by automobile companies to continue till March 2012

**Impact:** Although, Indian auto companies so far have not focused on R&D, we believe this is a positive step for auto companies as they are looking to move up the value chain and develop proprietary products in a bid to gain international market share.

- Levy of additional 1% cess on all taxes to fund secondary education and higher education

**Impact:** It would impact all companies marginally negative in terms of tax outgo. However, Maruti has already announced hike in car prices to offset the impact and we expect other companies to follow suit. Hence, these companies are not likely to be impacted by the additional cess burden.

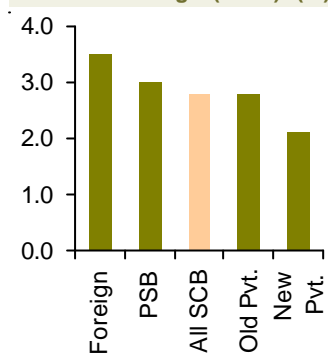
**TOP PICKS**

- Bajaj Auto
- Maruti Udyog
- M&M
- Amtek India
- Subros
- Tube Investments

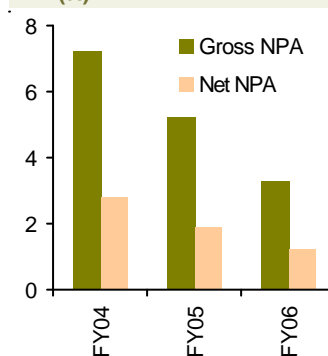
**Impact on EPS**

Company	FY2007E	FY2008E		Reco	Remarks
		Pre Budget	Post Budget		
Bajaj Auto	119	145	145	BUY	No major impact
Maruti Udyog	53	61	61	BUY	No major impact
M&M	41	46	46	BUY	No major impact
Amtek India	9.2	15.9	15.9	BUY	No major impact
Subros	24	30	30	BUY	No major impact
Tube Investments	4.4	5.9	5.9	BUY	No major impact

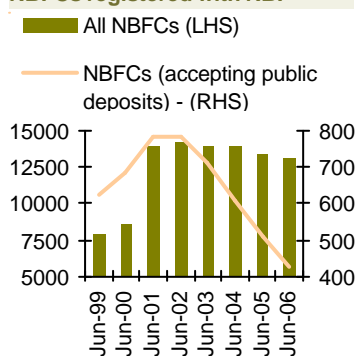
Source: Kotak Securities - Private Client Research

**BUDGET IMPACT: NEUTRAL****BANKING & FINANCE****BUDGET HIGHLIGHTS & IMPACT****Net interest margin (FY06) - (%)**

Source: Economic Survey 2006-07

**NPA (%)**

Source: Economic Survey 2006-07

**NBFCs registered with RBI**

Source: Economic Survey 2006-07

- **Dividend Distribution Tax raised to 25% on dividends paid by money market mutual funds and liquid mutual funds**

**Impact:** We think this is positive for banks, as it will indirectly make deposits with the banks more attractive and bring it at par with other investment instruments. So, in a situation where banks are finding it difficult to mobilize deposits to fund the credit off take, they will get a breather.

- **Interest subvention of 2% for farm crop loans to continue in 2007-08**

**Impact:** This is also positive for banks, as they will continue to get 2% extra interest from the government for lending to the agricultural sector.

- **Lower Government borrowings - Indicative from lower CAD and Fiscal Deficit**

**Impact:** This will indirectly benefit banks due to the benign interest rate scenario in the economy. In the past, higher government borrowings have crowded out private sector investment by way of higher interest rates. So, this will put a check on rising interest rates in the economy.

- **Deduction under section 36(1)(viii) to be restricted to 20% of profits each year**

**Impact:** We think this is negative for long-term financial corporations. This is applicable to institutions providing long-term finance (not less than five years) for industrial, agricultural or infrastructure and public companies providing long-term finance for construction or purchase of residential houses, which were entitled to a deduction of 40% of their profit if the same is carried to special reserve account. This will negatively impact HDFC, IDFC, LIC Housing Finance and Dewan Housing Finance by increasing their effective tax rate by 4-6%.

- **Bank cash transaction tax limit raised to Rs.50,000**

**Impact:** This will not have any material impact on banks.

**TOP PICKS**

- HDFC Bank
- ICICI Bank
- J&K Bank
- UTI Bank

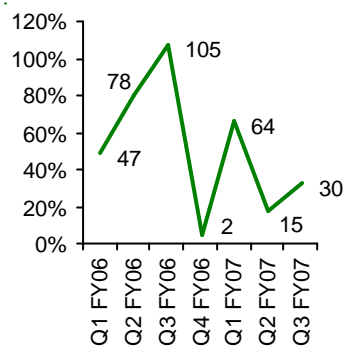
**Impact on EPS**

Company	FY2007E	FY2008E		Reco	Remarks
		Pre Budget	Post Budget		
HDFC Bank	37.1	48.2	48.2	HOLD	No major impact
ICICI Bank	36.5	46.9	46.9	BUY	No major impact
J&K Bank	62.9	79.0	79.0	BUY	No major impact
UTI Bank	22.8	31.3	31.3	BUY	No major impact

Source: Kotak Securities - Private Client Research

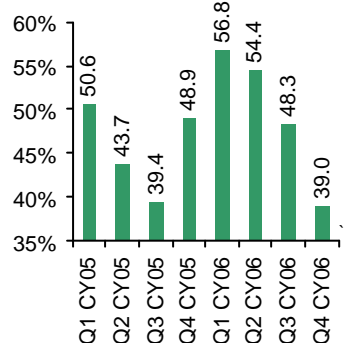
**BUDGET IMPACT: POSITIVE****CAPITAL GOODS & ENGINEERING****BUDGET HIGHLIGHTS & IMPACT**

Growth in order inflows for L&amp;T (YoY)



Source: Company

Growth in order inflows for ABB (YoY)



Source: Company

- **Increased allocation on Accelerated Power Development and Restructuring Programme (APDRP) and Rajiv Gandhi Vidyutikaran Yojana (RGVY).**

**Impact:** Under APDRP outlay on meters for monitoring of power consumption has been raised by 23%. This is likely to benefit electric meter manufacturers like Emco and Genus Overseas. Higher allocation on RGVY to benefit transformer makers like Emco, Bharat Bijlee, Indotech, Jyoti Structures and Kalpataru Power

- **Higher allocation on irrigation development**

**Impact:** Allocation hiked by 55% to Rs.110 bn. Should benefit irrigation pump makers like Kirloskar Brothers, M&P Pumps and Jyoti Ltd

- **Increase in plan capex on defence:**

**Impact:** The 12% increase in defence capex is the highest in three years and is positive for BEL, L&T and Astra Micro

- **Extension of TUF into eleventh plan:**

**Impact:** Should benefit LMW (largest textile machine manufacturer in India) and Voltas.

- **Additional cess of 1% on all taxes to be levied to fund secondary education and higher education**

**Impact:** Move would be marginally negative for companies.

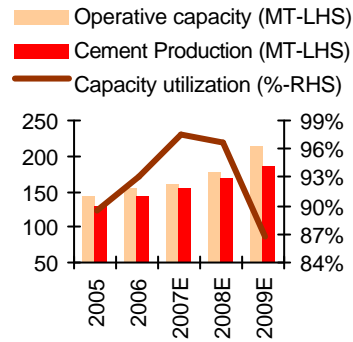
**TOP PICKS**

- Siemens
- Larsen & Toubro
- Crompton Greaves
- M&P Pumps
- Easun Reyrolle
- AIA Engineering
- Everest Kanto Cylinder

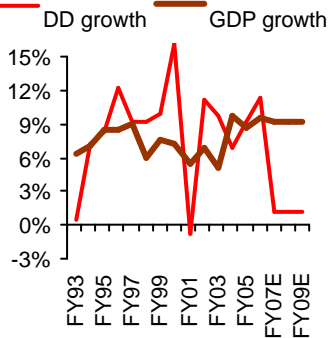
**Impact on EPS**

Company	FY2007E	FY2008E		Reco	Remarks
		Pre Budget	Post Budget		
Siemens	36.7	52.6	52.6	HOLD	Play on investment in power sector
Crompton Greaves	7.7	10.7	10.7	HOLD	Play on investment in power sector
Easun Reyrolle	45.0	57.0	57.0	BUY	Play on investment in power sector
L&T	52.7	66.1	66.1	BUY	Thrust on infrastructure
M&P Pumps*	10.2	19.1	19.1	BUY	Enhanced allocation to irrigation sector
AIA Engineering	52.0	76.6	76.6	BUY	Play on investment in infrastructure
Everest Kanto Cylinder	30.5	51.1	51.1	BUY	Leading manufacturer of high pressure cylinder

Source: Kotak Securities - Private Client Research; \* CY06 &amp; CY07

**BUDGET IMPACT: NEGATIVE****CEMENT****BUDGET HIGHLIGHTS & IMPACT****Rising utilizations till FY08**

Source: Kotak Securities - Private Client Research, CMA

**Trend in GDP and cement growth**

Source: Kotak Securities - Private Client Research, Cris Infac

- **Excise duty increased to Rs.600 per ton on cement to be sold in retail for more than Rs.190 per bag and reduced to Rs.350 per ton for cement prices less than Rs.190 per bag.**

**Impact:** Impact of increase in excise duties is negative for cement companies since the average retail price of cement for all companies is more than Rs.190 per bag. This additional rise of Rs.10 per bag will hit the net profits of cement companies if they are unable to pass on the rise to consumers.

- **Import of coking coal, a key input for cement companies, has been made fully exempt from customs duty.**

**Impact:** Customs duty on import of coking coal has been abolished, which will result in saving the power cost of cement companies and, hence, will enhance the efficiencies of cement companies.

- **Thrust on infrastructure creation**

**Impact:** The thrust of the Budget in creating infrastructure related to roads, irrigation, rural and urban development should allow the demand for cement to grow at more than 9% every year.

**Overall Impact:** We have evaluated the impact of a rise in excise duty for cement companies on their profitability. The company managements believe they would be able to pass on the increase to the customers. However, in the event of being unable to pass on the rise, we expect a 19% decline in the EPS of Shree Cement and 16% decline in EPS for India Cements for FY08. The stocks have corrected significantly, thereby factoring in the increase in excise duty, provide a good buying opportunity.

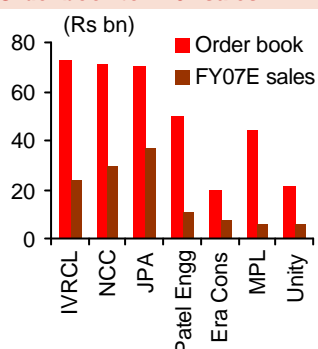
**TOP PICKS**

- Shree Cements
- India Cements

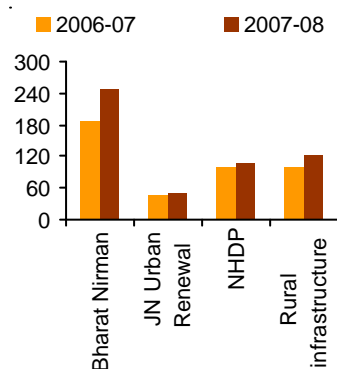
**Impact on EPS**

Company	FY2007E	FY2008E		Reco	Remarks
		Pre Budget	Post Budget		
Shree cements	94	133	110	BUY	EPS reduced to factor in increase in excise
India Cements	18	24	20	BUY	EPS reduced to factor in increase in excise

Source: Kotak Securities - Private Client Research

**BUDGET IMPACT: NEGATIVE****CONSTRUCTION****BUDGET HIGHLIGHTS & IMPACT****Order book to FY07 sales**

Source: Company

**Budgetary allocations (Rs bn)**

Source: Budget document 2007-08

**Impact of higher tax outgo**

	Tax outflow (Rs mn)	% EPS decline
NCC	403	13
Patel Engineering	384	21
Era Constructions	0	0
Madhucon Projects	190	17

Source: Kotak Securities - Private Client Research

- Provisions of tax benefit under section 80IA will not be applicable for construction companies, which are carrying out only civil construction work. This amendment will take retrospective effect from April 1st, 2000 and for subsequent years.

**Impact:** This amendment would be extremely negative for construction companies that were claiming tax benefits under section 80IA. Firstly, they would have to take a hit on their profitability or through their reserves for the past six years. Secondly, it would imply that their future tax rate would also be raised from current lower levels.

- Continued thrust of the Government on Bharat Nirman and for creating urban and rural infrastructure. For the Eleventh Five Year Plan, provision for Bharat Nirman has been increased by 31.6%. For NHDP, it has been increased to Rs.106.67 bn from Rs.99.45 bn. Corpus for Rural Infrastructure Development Fund has also been raised from Rs.100 bn to Rs.120 bn. A revolving fund has also been set up to quicken the project preparations for PPP model.

**Impact:** Increased focus on Bharat Nirman, NHDP and rural infrastructure should benefit all construction companies in the form of higher order inflows and hence provide more visibility to their revenues in terms of higher order books.

- Outlay for irrigation raised from Rs.71.2 bn to Rs.110 bn including the grant component to state governments of Rs.35.8 bn.

**Impact:** Higher outlay for irrigation would be beneficial for companies which have expertise in irrigation and water related projects.

- Continued focus on ultra mega power projects, higher budgetary support for APDRP and Rajiv Gandhi Grameen Vidyutikaran Yojana

**Impact:** New mega and merchant power projects should be positive for companies, which have expertise in building power projects.

**Overall impact:** Impact of removal of benefits under section 80IA will have a negative impact on the construction companies for past six years as well as for future earnings. Although with continued focus on road, irrigation, power related projects etc, companies will benefit in long term but their profitabilities will be impacted by higher tax outgo. We expect the negative impact of past years to be adjusted with reserves and assumed a higher tax rate of 28% for future estimates.

The stocks have corrected significantly in the recent past. We recommend bottom fishing in these stocks with a long term perspective.

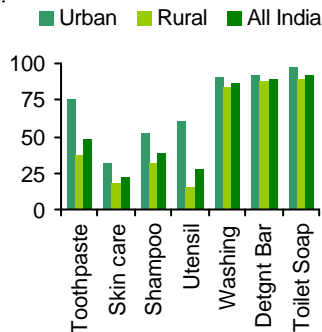
**TOP PICKS**

- Era Constructions
- Nagarjuna Constructions
- Patel Engineering
- Madhucon Projects

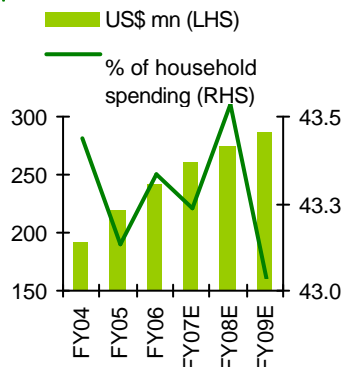
**Impact on EPS**

Company	FY2007E	FY2008E		Reco	Remarks
		Pre Budget	Post Budget		
NCC	8.5	12	10.5	BUY	Earnings adjusted for higher tax outgo
Patel	17.0	24	19	BUY	Earnings adjusted for higher tax outgo
Era Constructions	38.0	46	46	BUY	No negative impact since co pays full tax
Madhucon Projects	12.0	19	15.8	BUY	Earnings adjusted for higher tax outgo

Source: Kotak Securities - Private Client Research

**BUDGET IMPACT: POSITIVE****FOOD PROCESSING & FMCG****Penetration levels across ind. (%)**

Source: MRUC Hansa Research 2006

**Indian consumer expenditure on food and beverages**

Source: EIU country briefing on India 2005

**BUDGET HIGHLIGHTS & IMPACT**

- **Customs duty on the food processing machinery has been reduced from 7.5% to 5%.**

**Impact:** Reduction in customs duty on imports of food processing machinery would lead to easy and economical access to sophisticated food processing machineries, thereby leading to higher productivity and efficiency and finally turning into better profitability for the food processing companies.

- **Biscuits, whose retail sale price is less than Rs.50 per kg is fully exempt from excise duty.**

**Impact:** Exemption in excise duty on biscuits with selling price less than Rs.50 per kg would reduce the prices and thereby boost the consumption leading to higher profitability.

- **All kinds of food mixes including instant mixes would be fully exempt from excise duty**

**Impact:** Last year's Budget had exempted only idli and dosa mixes from the excise duty but now all food mixes including instant mixes are exempted from the excise duty. This would lead to reduction in prices of the instant and processed foods and hence would lead to growth in consumption of the processed and packaged foods.

- **Excise duty on cigarettes have been increased by 5%**

**Impact:** The increase in excise duty on cigarettes will have a marginally negative impact that will be offset largely by the price inelastic nature of the product.

- **Crude as well as refined edible oils are exempt from the additional countervailing duty (CVD) of 4%. Also, this Budget has seen duty on sunflower oil, both crude and refined, reduced by 15 percentage points.**

**Impact:** Import of crude and refined edible oil would now become cheaper with the exemption from CVD. This is positive for solvent extraction and edible oil refining companies, as now their cost of key raw material would come down.

- **Customs duty on dextrose monohydrate (DMH) reduced from 30% to 20%.**

**Impact:** Reduction of customs duty on imports of DMH is marginally negative for cornstarch processing companies in a way that the domestic prices cannot increase beyond the import prices. However, currently the landed cost of DMH works out to anywhere between Rs.28 to Rs.29 per kg whereas current domestic prices are approximately Rs.26 to Rs.26.5 per kg. Hence, we do not see any major negative impact on the cornstarch processing companies.

- **Increase in dividend distribution tax from 12.5% to 15% and additional 1% cess on tax for funding secondary and higher education.**

**Impact:** Increase in dividend distribution tax to 15% and additional 1% surcharge on tax would marginally increase the total tax outgo for companies. However, this is not expected to significantly impact the profitability of the companies. Hence, we maintain our earnings estimates.

**TOP PICKS**

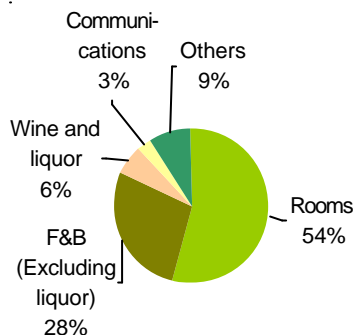
- Gujarat Ambuja Exports, Riddhi Siddhi Gluco Biols

We do not cover FMCG sector

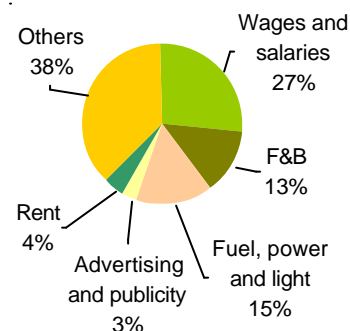
**Impact on EPS**

Company	FY2007E	FY2008E		Reco	Remarks
		Pre Budget	Post Budget		
Gujarat Ambuja Exports	3.4	5.2	5.2	BUY	Agro processing conglomerate
REI Agro	18.2	24.0	24.0	HOLD	No major impact
Riddhi Siddhi Gluco	24.4	36.9	36.9	BUY	Leading player of cornstarch and its derivatives

Source: Kotak Securities - Private Client Research

**BUDGET IMPACT: POSITIVE****HOTELS****BUDGET HIGHLIGHTS & IMPACT****Revenue composition of hotels (%)**

Source: WTTC

**Expenditure composition of hotels (%)**

Source: WTTC

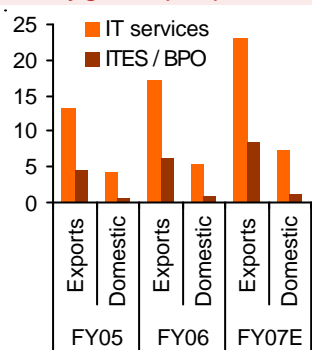
- **Provision for building tourist infrastructure has been raised from Rs.4.23 bn in 2006-07 to Rs.5.2 bn in 2007-08.**

**Impact:** Positive for hotel companies as it has direct relationship with tourism.

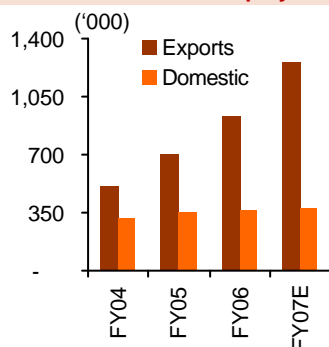
- **Infrastructure status has been granted to budget hotels to be set up in the Delhi-NCR region, to meet demand during Commonwealth Games**

**Impact:** Positive. A five-year income tax holiday will be granted for two, three and four-star hotels as well as for convention centre, with a seating capacity of not less than 3,000. They should be completed and begin operations in the National Capital Territory of Delhi or in adjacent districts during the period April 1 2007 to March 31 2010.

We do not have active coverage on the sector.

**BUDGET IMPACT: NEGATIVE****INFORMATION TECHNOLOGY****BUDGET HIGHLIGHTS & IMPACT****Industry growth (\$ bn)**

Source : Nasscom

**Growth in number of employees**

Source : Nasscom

- **Minimum alternate tax (MAT) has been extended to income in respect of which deduction has been claimed under sections 10A and 10B. The rates applicable to all corporate incomes, including IT firms, will be 11.22% of adjusted book profits.**

**Impact:** The extension of MAT to companies availing deductions under sections 10A & 10B will be negative for the industry. Effective tax rates for companies as a result will go up and impact earnings estimates negatively. In case companies are able to claim credit for MAT, the impact on the company's valuation over the longer term could get negated.

- **Employee stock options (Esops) brought under the ambit of the fringe benefit tax (FBT).**

**Impact:** Esops being brought under the ambit of FBT is also negative for the industry and will impact net profits of the company negatively. FBT would now be levied on the difference between market price and exercise price of the option at the time of exercise of the option. This will, consequently, increase the tax outgo of companies that have an Esop scheme.

- **Service tax of 12% is applicable on rented/leased immovable property that is used by companies during the course of business.**

**Impact:** The companies that use rented/leased facilities will be liable to pay service tax, which is also negative for the industry and will impact profit estimates for such companies negatively, though to a limited extent.

- **The provisions of the Union Budget have been negative for the sector. However, we believe the fundamentals of the sector remain strong. The stock prices have reacted significantly over the past one week. This, in our opinion, discounts the negatives.**

We maintain our positive bias on the sector over the medium to long term, given the healthy fundamentals underpinning the sector.

**TOP PICKS**

- Infosys, TCS, Satyam, HCL Tech, NIIT Technologies and Zensar

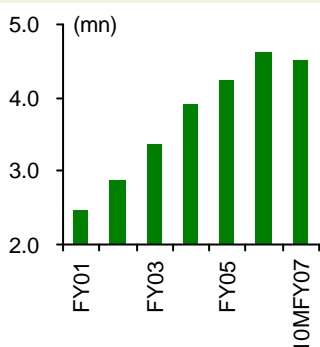
**OTHERS**

- Wipro (HOLD), Patni (BUY), NIIT Ltd (HOLD), Allsec (HOLD), KPIT (HOLD), R Systems (BUY), Aztec (BUY), Geometri (HOLD), Mphasis (HOLD), I-flex (HOLD).

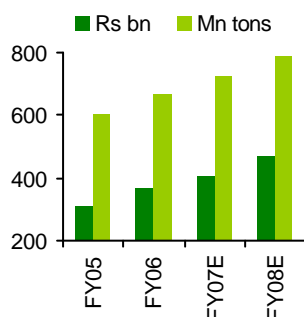
**Impact on EPS**

Company	FY2007E	FY2008E		Reco	Remarks
		Pre Budget	Post Budget		
Infosys	67.4	87.9	82.6	BUY	Proxy for the sector. Sustained growth expected
TCS	42.1	54.6	52.4	BUY	Consistent growth expected, current valuations attractive
Satyam	20.7	24.8	23.6	BUY	Valuation discount to Infosys could narrow
HCL Tech	33.7	38.3	36.3	BUY	Consistency in growth expected. Attractive valuations
NIIT Technologies	30.8	38.3	37.4	BUY	Carlyle's presence bodes well for the long term
Zensar	23.2	31.3	30.3	BUY	Good acquisition. Undemanding valuations

Source: Kotak Securities - Private Client Research

**BUDGET IMPACT: POSITIVE****TEUs handled at India's major ports**

Source: ipa.nic.in

**Transport of goods on railway wagons**

Source: Rail budget documents

**LOGISTICS****BUDGET HIGHLIGHTS & IMPACT**

- **Small aircraft with maximum takeoff mass of less than 40,000 kg operated by scheduled airlines can consider aviation turbine fuel (ATF) as a declared good. They are, hence, covered under CST.**

**Impact:** Since Indian aviation companies are expanding their operations to smaller airports and to remote parts of the country through smaller aircraft they will be able to obtain ATF at concessional rates of CST. A lot of aviation companies like Air Deccan, Jet Airways and Kingfisher Airlines operate smaller aircrafts like ATR turbo props, which would become eligible to obtain ATF by paying CST as against paying very high rates of sales tax across the country.

- **Construction of dedicated rail freight corridor to start in FY08**

**Impact:** In the railway budget, the government has announced that the construction of the Rs.300 bn dedicated rail freight corridor would begin in FY08. It is expected to be operational in the Eleventh Plan itself. With robust growth in the economy and export import trade, the movement of containers through railways is expected to rise significantly, thus providing additional business opportunities to companies like Allcargo Global Logistics, Concor, and Gateway Distriparks.

**TOP PICKS**

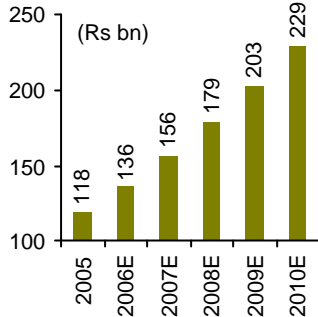
- Allcargo Global Logistics
- Concor
- Gateway Distriparks
- Gati

**Impact on EPS**

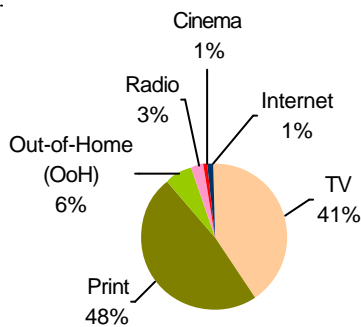
Company	FY2007E	FY2008E		Reco	Remarks
		Pre Budget	Post Budget		
Allcargo Global *	56.5	70.8	70.8	BUY	Multimodal transport operator
CONCOR	108.4	126.7	126.7	BUY	Leader in transportation of containers through railways
Gateway Distriparks	7.8	8.7	8.7	BUY	Play on port based logistics services
Gati **	3.7	6.0	6.0	HOLD	Leading player of express cargo

Source: Kotak Securities - Private Client Research; \* December end \*\* June end

Analyst holding: Concor - 50 shares

**BUDGET IMPACT: NEUTRAL****MEDIA****BUDGET HIGHLIGHTS & IMPACT****Growth in overall ad revenues**

Source: Industry, FICCI-PwC, Kotak Securities - Private Client Research

**Add revenues break up in 2006**

Source: Industry estimates compiled by Adex India

- **Service tax of 12% is applicable on rented/leased immovable property that is used by companies during the course of business.**

**Impact:** Companies that use rented/leased facilities will be liable to pay service tax, which is negative for the industry and will impact profit estimates for such companies negatively. Within the media sector, multiplexes use rented properties extensively and operating margins for multiplex players will be impacted, more so for properties in high rental areas like metros.

- **Levy of additional 1% cess on all taxes to fund secondary education and higher education.**

**Impact:** This would impact all companies marginally negatively due to a consequent increase in the tax outgo. The impact on earnings though would be marginal, not warranting significant changes to estimates.

- **Service tax of 12% is applicable on companies involved in development and supply of content - mobile VAS, music, movie clips, ring tones, wallpaper, information and animation films.**

**Impact:** Companies involved in the above activities will be impacted marginally negatively. Listed players like UTV, which have an emerging presence in these segments believe this could be passed on to the customers.

- **Service tax is applicable on companies providing design services in relation to furniture, websites, logos etc. Print media companies continue to be out of the ambit of service tax.**

**Impact:** Status quo maintained on the print media sector vis-à-vis service tax. We continue to remain positive on the print sector given the healthy macro scenario coupled with the healthy share of print in the ad revenue pie. Within media, print (HT Media) is a segment that is expected to see healthy return ratios going forward on the back of leverage emerging in the business.

From a longer term perspective, we believe that on the back of greater spending power, growing consumerism and India's evolving demographics consumer discretionary sectors like media and entertainment will continue to enjoy healthy growth prospects.

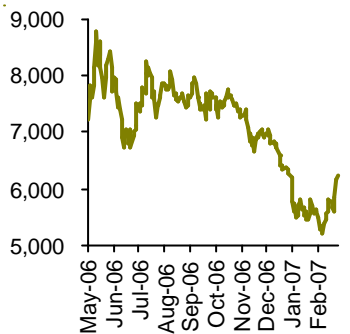
**TOP PICKS**

- ENIL
- UTV Software
- HT Media.

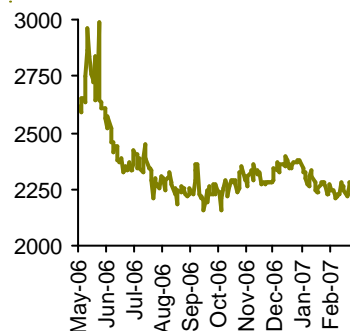
**Impact on EPS**

Company	FY2007E	FY2008E		Reco	Remarks
		Pre Budget	Post Budget		
ENIL	7.2	11.2	11.2	BUY	No major impact
HT Media	5.6	8.2	8.2	BUY	No major impact
UTV Software	6.6	13.6	13.6	BUY	No major impact
TV 18	10.5	14.4	14.4	HOLD	No major impact

Source: Kotak Securities - Private Client Research

**BUDGET IMPACT: NEUTRAL****METALS****BUDGET HIGHLIGHTS & IMPACTS****Copper prices (\$/ton)**

Source: Bloomberg

**Aluminium prices (\$/ton)**

Source: Bloomberg

- **Export duty of Rs.300 per metric ton to be levied on export of iron ores and concentrates and Rs.2000 per metric tons on export of chrome ores and concentrates**

**Impact:** There are not many exporters of iron ores and chrome ores in India. It would be marginally negative for companies such as Sesa Goa (iron ore exporter), Nav Bharat (chromium ore exporter).

- **Custom duty on coking coal irrespective of ash content to be fully exempt**

**Impact:** Coking coal is used in blast furnaces. Hence, it is positive for sponge and pig iron (steel intermediate) producing companies, which import coking coal.

- **Extension of service tax to services outsourced for mining of minerals**

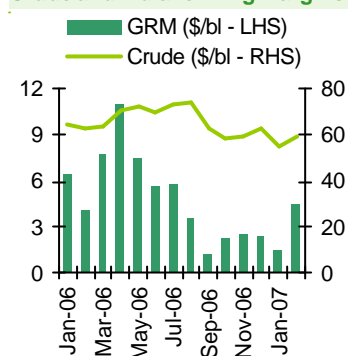
**Impact:** Marginally negative for all metal ore extractors.

- **Customs duty on prime steel remains at 5%, while on seconds and defectives of steel it has been reduced from 20% to 10%.**

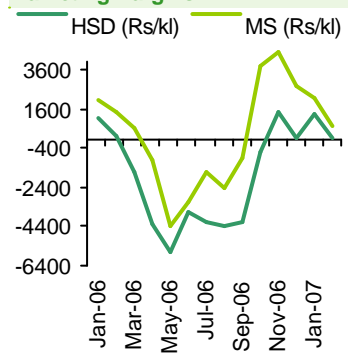
**Impact:** The reduction in duty would be positive for companies, which use steel scrap as feedstock for steel. These companies are one's with electric furnaces like Bhushan, Mukund and Telemettalic. Since steel scrap competes with sponge iron it could put some pricing pressure on sponge iron steel intermediates like Electro Steel, Lanco Industries. Hence, the impact would be marginally negative for them.

Overall, as expected, after the January 7, 2.5% duty cut there has been no change in the excise and customs duties on ferrous as well as non-ferrous metals. Customs duty on ferrous (steel and intermediates) and non-ferrous (aluminum, copper, zinc) metals remains at 5%, while excise duty remains at 16%.

We do not have active coverage on the sector.

**BUDGET IMPACT: POSITIVE****OIL & GAS****BUDGET HIGHLIGHTS & IMPACT****Crude and India refining margins**

Source: Bloomberg, Crisil

**Marketing margins**

Source: Kotak Securities - Private Client Research; Crisil

- **Reduction in ad valorem component of excise duty on petrol and diesel from 8% to 6%.**

**Impact:** This would benefit OMCs (HPCL, BPCL, IOC) and lower overall gross industry under-recovery in FY08 by approximately Rs.35 bn to Rs.475 bn. The benefit in marketing margins in petrol and diesel would be approximately Rs.500/kl.

- **Concessions under section 80IA for infrastructure facilities to be extended to cross country natural gas distribution network, including gas pipeline and storage facilities integrated to the network; and to navigation channel in the sea.**

**Impact:** The move would benefit gas transmission and storage companies like GAIL, GSPL, RIL, P-LNG in the form of tax benefits and lower cost of borrowing.

- **Extension of service tax to services outsourced for mining of oil or gas**

**Impact:** Slightly negative for oil exploration companies (ONGC, RIL), no change in our earning estimates as ONGC has got its own exploration equipments.

- **Rate of dividend distribution tax to be raised from 12.5% to 15% on dividends distributed by companies**

**Impact:** Like any other company, the move would be marginally negative for companies under our coverage (HPCL, BPCL, ONGC), which have dividend yield of about 2-3%.

- **An additional cess of 1% on all taxes to be levied to fund secondary education and higher education**

**Impact:** Like any other company, the move would be marginally negative for companies under our coverage (HPCL, BPCL). The additional cess would be approximately Rs.50/kl on petrol and diesel.

- **Reduction in custom duty on most chemicals and plastics from 12.5% to 7.5%. Reduction in duty on polyester fibres and yarns from 10% to 7.5% and on raw materials such as DMT, PTA and MEG from 10% to 7.5%.**

**Impact:** The move would be slightly negative for petrochemical producing companies like RIL, GAIL, IOC and IPCL

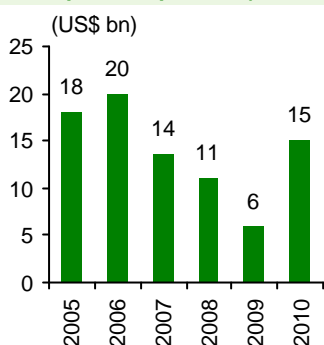
**TOP PICKS**

- ONGC, HPCL, BPCL, GSPL, IGL and Great Offshore

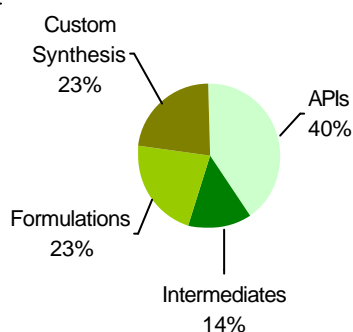
**Impact on EPS**

Company	FY2007E	FY2008E		Reco	Remarks
		Pre Budget	Post Budget		
ONGC	86	97	97	BUY	Marginally negative
HPCL	28	34	34	BUY	Excise duty reduction positive, however no change in earnings as oil bonds would be reduced accordingly.
BPCL	28	31	31	BUY	Excise duty reduction positive, however no change in earnings as oil bonds would be reduced accordingly.
Gujarat State Petronet	1.8	2.2	2.2	BUY	Infrastructure status; Positive
Indraprastha Gas	9.4	10.7	10.7	BUY	Infrastructure status; Positive
Great Offshore	35	59	59	BUY	No major impact

Source: Kotak Securities - Private Client Research

**BUDGET IMPACT: POSITIVE****PHARMACEUTICALS****Global patent expiration (2005-10)**

Source: Kotak Securities - Private Client Research

**Global pharma outsourcing market**

India: A preferred outsourcing destination.  
Global opportunity: US\$ 48bn.  
India opportunity: US\$ 6.0bn

Source: Kotak Securities - Private Client Research

**BUDGET HIGHLIGHTS & IMPACT**

- **A weighted average deduction of 150% u/s. 35 (2AB) of Income Tax Act for expenditure relating to in-house research and development extended by five years until March 31 2012.**

**Impact:** Positive for companies, which incur high R&D expenditure. This would encourage companies to focus on NCE/NDDS research and R&D related activities.

- **Peak custom duty on bulk drugs is proposed to be cut to 10% from 12.5%**

**Impact:** Positive for major pharma companies.

- **Customs duty on specified medical equipment reduced to 7.5%.**

**Impact:** Positive for healthcare companies like Max Healthcare and Apollo Hospitals.

- **Customs duty on 15 specified machinery used by the pharma and biotech industry reduced from 7.5% to 5%.**

**Impact:** We expect this move to benefit those companies, which are going for capex/expansion.

- **Excise duty exemption on life saving vaccines.**

**Impact:** Likely to be positive for companies, which are engaged in the manufacture of life saving vaccines like Panacea, Wockhardt, Aventis, GSK Pharma etc.

- **Clinical trials on drugs in India are exempted from the levy of service tax.**

**Impact:** Positive for those companies, which provide clinical trials of drugs and clinical research services, for example, Nicholas Piramal, Jubilant Organosys, Biocon etc.

- **National Rural Health Mission (NRHM): Allocation increased from Rs.82.07 bn to Rs.99.47 bn.**

- **Focus on tuberculosis, malaria and mother-child care.**

- **Allocation increased for polio eradication to Rs.12.9 bn.**

**Impact:** Increased allocation for health is positive for the pharma industry.

**Overall Impact:** Overall, we believe the Budget has a 'positive impact' on the pharmaceutical industry as increased allocation for the National Rural Health Mission (NRHM) by 21% at Rs.99.5 bn and separate allocation of Rs.12.9 bn for polio eradication are positive. More focus on HIV/AIDS eradication (allocation of Rs.9.69 bn) is positive for MNC pharma companies while increased immunization programs will promote pharma industry.

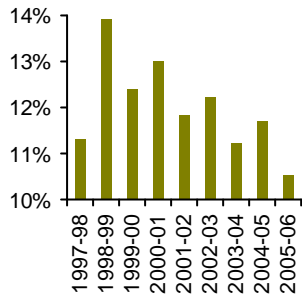
**TOP PICKS**

- Alembic Ltd, Aventis Pharma, Cipla, Jubilant Organosys, Nicholas Piramal and Panacea Biotec

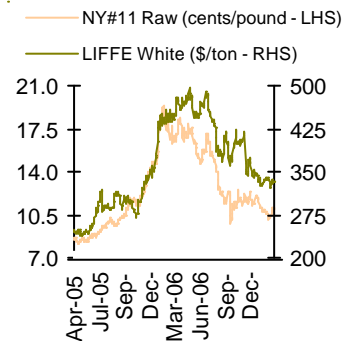
**Impact on EPS**

Company	FY2007E	FY2008E		Reco	Remarks
		Pre Budget	Post Budget		
Alembic	6.2	8.4	8.4	Buy	Reduction in peak custom duty to have marginal positive impact
Aventis Pharma^	80.3	91.4	91.4	Buy	Excise duty exemption on life saving vaccines is positive for Aventis
Cipla	9.1	11.1	11.1	Buy	Play on formulation export and inhaler business in Europe
Jubilant Organosys	15.1	18.0	18.0	Buy	Exemption of service tax on clinical trials is positive
Nicholas Piramal	10.9	15.8	15.8	Buy	Exemption of service tax on clinical trials is positive
Panacea Biotec	21.4	30.2	30.2	Buy	Increased allocation for polio eradication is huge positive.

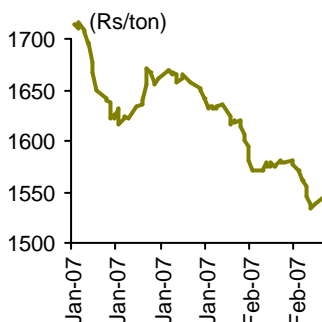
Source: Kotak Securities - Private Client Research; ^ December year end

**BUDGET IMPACT: NEUTRAL****Peak power deficit (%)**

Source: Annual report 2005-06 on power sector

**BUDGET IMPACT: NEUTRAL****International prices**

Source: Bloomberg

**Domestic sugar price**

Source: Bloomberg

**POWER****BUDGET HIGHLIGHTS & IMPACT**

- 80IA provisions for income tax maintained till 2010.

**Impact:** maintained status quo.

- Additional cess of 1% on all taxes to be levied to fund secondary education and higher education

**Impact:** Move would be marginally negative for companies.

We do not have active coverage on the sector.

**SUGAR****BUDGET HIGHLIGHTS & IMPACT**

There is no industry specific provision in this year's Budget for the sugar industry. This is a bit disappointing especially on the ethanol front. Extending the benefits of section 80-IA to ethanol production would have given a fillip to ethanol program in the country and provided necessary support to sugar companies, given the current downturn in sugar prices.

We expect sugar prices to remain muted, going forward, not only due to higher production both domestically and globally but also given the government's concerns on curbing inflation. We have a negative view on the sector in the near future as earnings would come under pressure from lower sugar realizations as well as higher interest and depreciation costs due to the ongoing capex program.

There have been reports on decontrolling the sector as well as creating buffer sugar stocks that would be beneficial for the sector. However, so far there has been no action on this front. Currently, we have a SELL rating on Bajaj Hindusthan, Balrampur Chini and Dwarikesh Sugar.

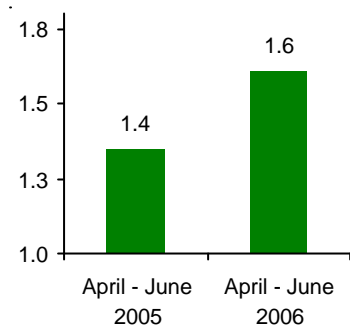
The companies would, however, be affected by the following provisions:

- Levy of additional 1% cess on all taxes to fund secondary education and higher education

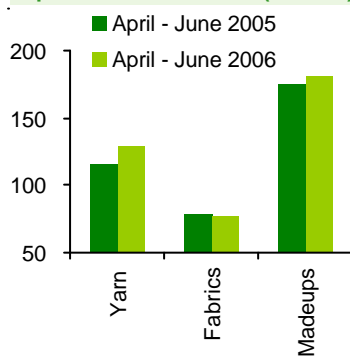
**Impact:** It would impact all companies marginally negatively in terms of rise in tax outgo.

- Rate of dividend distribution tax to be raised from 12.5% to 15% on dividend distributed by companies

**Impact:** It would impact all companies negatively in terms of dividend tax outgo especially high dividend yield companies like Balrampur Chini. However, companies may reduce the rate of dividend.

**BUDGET IMPACT: POSITIVE****TEXTILES****BUDGET HIGHLIGHTS & IMPACT****India's textiles exports (US\$ bn)**

Source: Texprocil

**Exports of cotton textiles (US\$ mn)**

Source: Texprocil

- **Allocation for Technology Upgradation Fund (TUF) enhanced from Rs.5.3 bn to Rs.9.1 bn and the scheme eligibility extended upto FY12.**

**Impact:** The TUF scheme has interest subsidy of 5% on the machinery bought for upgrading the technology. There is 72% higher allocation for the TUF scheme which is positive for the entire industry. The eligibility period of the scheme has also been extended up to FY12. As a result of this, we expect more investments to be made in the textile sector, thereby making it more competitive and profitable in the long run.

- **Customs duty on DMT, PTA and MEG has been reduced from 10% to 7.5%.**

**Impact:** DMT, PTA and MEG are raw materials used in the manufacture of man-made fibers and reduction in customs duty on them from 10% to 7.5% will reduce the raw material cost and prevent higher domestic prices.

- **Allocation for Integrated Textiles Parks (ITP) scheme increased from Rs.1.9 bn to Rs.4.25 bn.**

**Impact:** The scheme for 30 ITPs was launched in FY06. A total of 26 of them have already been sanctioned and are under implementation. The government has further identified locations for more ITPs and has allocated Rs.4.25 bn towards the same. This is positive for the textile sector as this will lead to better technology and efficiency in the textile sector leading to higher exports and increasing profitability.

- **Increase in dividend distribution tax from 12.5% to 15% & additional 1% cess on tax for funding secondary and higher education.**

**Impact:** Increase in dividend distribution tax to 15% and additional 1% cess on tax would marginally increase the total tax outgo for companies. However, this is not expected to significantly impact the profitability of the companies. Hence we maintain our earnings estimates.

**TOP PICKS**

- GHCL
- JBF Industries
- Vardhman Polytex

**Impact on EPS**

Company	FY2007E	FY2008E		Reco	Remarks
		Pre Budget	Post Budget		
GHCL	12.4	22.1	22.1	BUY	Present in yarn to retailing
JBF Industries	12.9	17.1	17.1	BUY	Leading player in polyester chips and POY
Vardhman Polytex	16.7	18.2	18.2	BUY	Reputed player in cotton yarn

Source: Kotak Securities - Private Client Research

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