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Budget 2016 Simplified

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PRE-BUDGET ANALYSIS

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PRE-BUDGET NOTE - FEBRUARY 2016

The Finance Minister, Mr. Arun Jaitley, will present the 2016-17 budget amid a weak global setup and an anemic domestic recovery. The consumption stimulus (OROP and 7th Pay Commission) and investment stimulus (with private sector capex is yet to recover) are expected to result in higher spends. Thus, the FM will have to be resourceful enough to meet the FD targets. We look for an 'Achievable' and 'Sustainable' budget; one of the pre-requisites for further monetary policy easing by RBI.

EXPECTED SECTORAL IMPACT

POSITIVE: Auto, Banking/NBFCs, Capital Goods, Cement, Construction, Metals & Mining, Oil & Gas, Paints, Power, Shipping & Logistics.

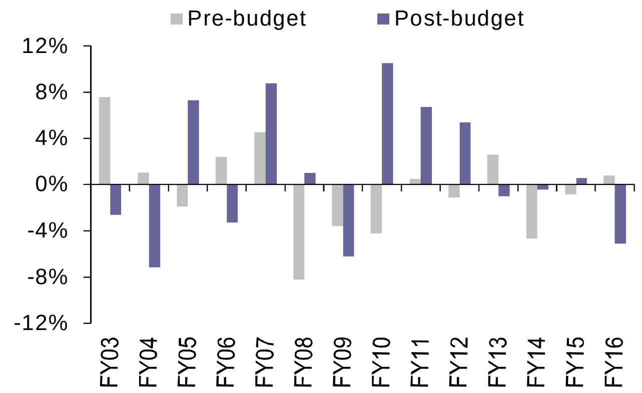
NEUTRAL: Agro Chemicals, Aviation, FMCG, Information Technology, Media, Pharmaceuticals, Real Estate

The FM's priority in the 2016-17 budget will be higher growth, with fiscal rectitude, we believe. With the private sector capex yet to pick up, he will budget for higher plan capital expenditure (investments), in addition to the higher spends on OROP and CPC, which need to be factored in. These will be proposed to be financed by higher revenues from divestment/privatisation, higher indirect tax rates, telecom auctions and better tax compliance, apart from a cut in non-plan expenditure (subsidies) via DBT.

A lower fiscal deficit will leave more money available for the private sector, help in easing inflation, and moderate interest rates further. We expect targets under the FRBM Act to be largely maintained. We expect the FM to target a fiscal deficit of 3.7% for FY17 and budget for a gradual reduction in fiscal deficit per annum to 2.5% by FY19.

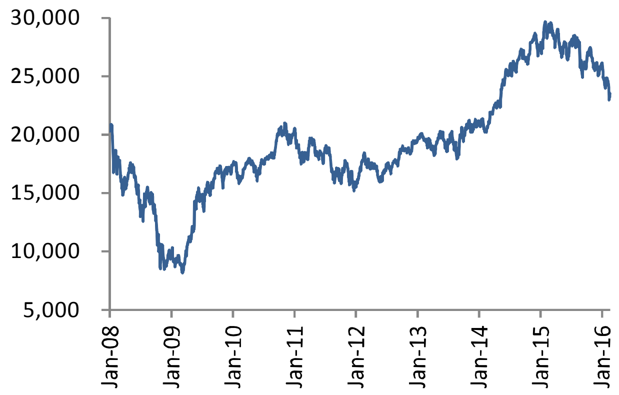
We also expect the FM to target real GDP growth of 7.7% in FY17 and bring it to over 8% next year. Larger and targeted plan expenditure capital outlays, with strict implementation timelines, would likely be announced, to ensure economic recovery and sustainable growth. We expect plan expenditure target to increase by 30% over FY16RE. The budget will aim to provide an investment - led supply aid to growth (with private sector participation via Make in India campaign) as well as a consumption - led demand pull growth via 7th CPC, OROP and DBT of subsidies.

Market movement - one month before and after budget



Source: Bloomberg

Sensex performance



Source: Bloomberg

On taxation front, we expect the Government to initiate reform process in direct taxes, in line with the announcements of the previous budget. The tax rate is expected to gradually come down from 30% to 25%, with a corresponding removal of exemptions / deductions available currently. On indirect taxes, we expect increase in service tax rate to bring it in line with the proposed GST rate of about 17-18%. Similarly, excise duties will likely be levied on various exempt items and increased for various items which are currently taxed at concessional rates. We are not expecting change in base rate of excise duty.

The FM will have to restrict non plan expenditure to meet his FD targets. While the food subsidy burden will be taken up, we believe the FM will budget for lower fuel subsidy bill on the back of lower crude prices. He will also better target subsidies through the JAM trinity. The government has already announced on January 1, the launch of DBT for kerosene subsidy in a bid to cut down the diversion and black marketing of the fuel. The kerosene subsidy in FY15 was pegged at about Rs.248bn. As per reports, Direct Benefit Transfer (DBT) for LPG had resulted in savings of about Rs.140bn in FY15. We expect DBT to be gradually used for more subsidies. Implementation of DBT for fertilizer and crop subsidy could result in substantial savings.

To provide higher employment opportunities and to make the workforce employable, we expect measures to promote the 'Make in India' and 'Skill India' initiative. We also expect higher allocations towards agriculture and rural sector to support rural growth, after two continuous drought years in the country.

We expect the divestment target to be increased to Rs.500bn in FY17 v/s the FY16RE of Rs.200bn. Tax revenue targets (net) may be set at Rs.10.2trn, an 8% growth over FY16RE. Customs duty may be tweaked on several items to further the 'Make in India' cause. We expect implementation of GAAR to be postponed to FY18. We also expect tax benefits for the export-oriented sectors, in view of the consistently falling exports and some measures to restrict dumping.

We do not expect any major initiatives for the stock markets. Some minor adjustments could be in offing for increasing retail participation in equities (directly/indirectly). Reduction in STT, if any, will be cheered by the markets, while any tax liability on LTCG will be a severe negative. We believe focus of the markets will be largely on fiscal prudence, on effective implementation of investments, and on sectors which are impacted by the budget proposals. Off-budget investment and governance reforms announcements will continue to impact the markets.

We believe that, the budget may have the following implications for the sectors:

Expected sectoral impact

Budget impact	Sector
Positive	Auto, Banking/NBFCs, Capital Goods, Cement, Construction, Metals & Mining, Oil & Gas, Paints, Power, Shipping & Logistics.
Neutral	Agro Chemicals, Aviation, FMCG, Information Technology, Media, Pharmaceuticals, Real Estate

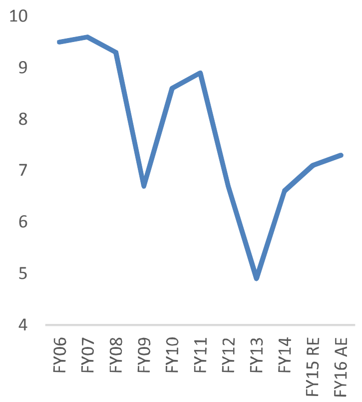
Source: Kotak Securities - Private Client Research

We expect the budget to continue its focus on sustained high growth in the economy over the next several years. The FM will announce concrete initiatives in line with the Government's long term vision, which was laid down in the previous budgets as well.

The Government has clearly highlighted its long-term priorities like infrastructure (smart cities, renewable energy, railways, roads, inland waterways, etc), manufacturing (Make in India), employment (skills development, education), predictable and non-adversial tax regime, Swacch Bharat (clean Ganga, etc), removing supply bottlenecks, ease of doing business, maximum governance, among others. We expect significant allocations / announcements towards such initiatives.

We also feel that, the budget will continue on the path of fiscal rectitude and lay down targets for reduction in fiscal deficits going forward too. We expect the reforms process to be carried forward with increased stress on effective and timely implementation.

GDP growth (%)



Source: CSO; GDP data till FY13 is based on 2004-05 prices

Improving GDP growth

India's GDP growth rate will likely stay at a below-potential 7.6% (value added basis) in FY16, as compared to the revised rate of 7.2% in FY15. The growth in 3QFY16 decelerated to 7.3% as against 7.7% in 2Q. If India achieves 7.6% growth in FY16, it will be the fastest-growing economy in the world, ahead of China. However, the challenge is now to sustain this growth and take it higher over the years.

We expect the FM to increase allocations towards planned capex, with a view to improve the rate of growth. We also expect time-bound and effective implementation of these budgets. On the other hand, the FM will account for the increased spend of Rs.100 bn on OROP and Rs.1trn towards the 7th central pay commission recommendations, which should give a significant consumption boost to the economy.

Sustenance and improvement of growth is very important to make the benefits of this growth reach all sections of the society. The target growth for real GDP may be set at 7.7% for FY17 as compared to 7.6% for FY16RE.

Real GDP Growth

(%)	2012-13*	2013-14	2014-15 RE	2015-16 AE
Agriculture & Allied activities	**1.2**	**3.7**	**-0.2**	**1.1**
Industry				
Mining & quarrying	-0.2	5.4	10.8	6.9
Manufacturing	6.2	5.3	5.5	9.5
Electricity, gas & water supply	4.0	4.8	8.0	5.9
Construction	-4.3	2.5	4.4	3.7
Services				
Trade, Hotels, Transport, Communication	9.6	11.1	9.8	9.5
Finance, Real Estate, Other Businesses	8.8	7.9	10.6	10.3
Community, Social & Personal Services	4.7	7.9	10.7	6.9
Total	**4.9**	**6.6**	**7.1**	**7.3**

*Source: CSO; * Stands for GDP on 2004-05 prices*

Infrastructure and manufacturing to get significant attention

Higher allocations for investments, mainly in infrastructure, are expected to continue. We understand that, infrastructure construction accounts for the maximum share (about 54%) of construction activities. Industrial expansion contributes to about 36% of overall construction activity, and residential and commercial are at 5% each.

Plan capital expenditure will likely be pegged 30% higher over FY16RE. We note that, in the FY16 budget also, the FM had budgeted for a central plan expenditure increase of 37% YoY, both on the capital and revenue fronts. In the first 9 months of FY16, Government capex expenditure has gone up by 64% to 1.15 trn in Apr-Dec period this year vs 700 bn in same period last year.

We expect higher allocations to various areas like Ports, industrial corridors, Roads/Highways, Rurbanisation of India, Housing, Mining, Manufacturing, etc. We also expect increased allocations for various ambitious projects of the Government viz.: smart cities, river inter-linking, renewable energy, among others.

Continued focus towards infrastructure creation in North-East regions is likely. Providing investment allowance benefit to infrastructure sector and to larger companies will attract more private sector investment.

We expect stringent measures to ensure effective implementation of such initiatives. Stricter monitoring of progress of projects and linking the release of budgets to actual performance can be good ways of ensuring better implementation. Regular reviews, say, on a quarterly basis, will ensure even spending across the fiscal and not bunching up of spends towards the end of the fiscal. Un-locking the value stuck in various public-private-partnership (PPP) projects by re-pricing some of these and changing the rules in others will also provide impetus to the sector.

We understand that, several issues may not really fall under the purview of the Budget and the intent of effective implementation will have to be seen in legislative and administrative action over the coming months.

OROP and 7th pay commission recommendations - to provide consumption boost

We expect the FM to provide for Rs.1.1trn, towards One Rank, One Pension (OROP) and the 7th Pay Commission requirements.

The Seventh Pay Commission's recommendation of a 23.55% increase in the pay and allowances of government employees from 1/1/2016, will need an estimated Rs.1.02trn extra expenditure, including arrears, we understand.

Besides, the government had recently set a deadline for the nationwide implementation of the Food Security Act by April 1. As a result, the food subsidy bill is expected to exceed Rs.1trn next year. Government recently announced near completion of digitization process of ration card data. Weeding out duplicates and intended beneficiaries is likely to bring substantial savings and improve delivery mechanism. We do expect DBT is now a near possibility towards implementation, we expect pilot projects to be announced in the budget. Full implementation of DBT for Food Security Act could result in substantial reduction of food subsidy bill.

This expenditure, while making the fiscal math difficult for the FM, is likely to provide the consumption stimulus to the economy.

Focus to be on equitable growth

Equitable growth has been one of the important cornerstones of the Government's campaign and we expect the same to be reflected in the budget. We expect measures to provide further impetus to these schemes to ensure rural upliftment, employment, education, agricultural growth and public health. Initiatives on agriculture also help in easing supply side constraints and sustaining the GDP growth rate.

In order to help farmers and the overall agriculture sector, the budget will likely contain measures necessary to raise productivity, policies ensuring remunerative prices for farmers, reforms necessary in the area of land leasing and titles, a mechanism to bring quick relief to farmers hit by natural disasters, and initiatives necessary to spread Green Revolution to eastern states.

We expect rural development to be a focus area of the budget. Additional funds will likely be allocated for rural jobs, rural roads, rural housing and for overall rural development. We expect additional contributions towards the schemes like Shyama Prasad Mukherji Rurban Mission, Deen Dayal Upadhyaya Gram Jyoti Yojana (for feeder separation to augment power supply to the rural areas), Start Up Village Entrepreneurship Programme, etc. We also expect continued support to newly launched schemes like Pradhan Mantri Suraksha Bima Yojana (covers accidental death risk), Atal Pension Yojana (provides a defined pension) and Pradhan Mantri Jeevan Jyoti Bima Yojana.

However, we also expect some of these schemes to be discontinued or merged with other schemes. The Government may tweak some entitlement schemes and further align them with specific tangible outcomes. Several of these schemes may also be handed over to the State Governments with commensurate share of resources, for their effective execution.

To improve the employability level of the Indian demography, we expect the FM to announce more initiatives on education, skills and health. The Skill India program has already been announced by the Government and will likely see more allocations from the FM.

We believe these are important initiatives which provide inclusive and balanced growth and reduce the migration to cities from towns and villages over the medium to long term.

Fiscal deficit - Hoping for an achievable budget

The FD was pegged at 3.9% for FY16. The lower growth in nominal GDP (about 8.64% growth in FY16) and the likely shortfall in direct tax / divestment revenues have made the fiscal deficit target difficult to achieve.

However, we expect higher-than-expected collections from indirect taxes, lower subsidy burden, as well as a calibrated non-plan expenditure to help achieve the target. We expect a fiscal deficit of 3.9% for FY16RE.

The fiscal deficit picture is concerning for FY17, however. We do hope that, the FY17 budget will be an achievable budget and will progress on the path of fiscal prudence. For FY17, we expect the FM to target a fiscal deficit of 3.7%, based on achievable numbers slightly higher than 3.5% indicated in FRBM Act. We expect FM to give reducing fiscal deficit target for next two years FY18 & FY19 at 3% and 2.5%, respectively.

Revenues

On the revenue front, we expect the FM to budget for a 7% increase in overall revenue receipts, on the back of a 7.5% rise in net tax receipts. We expect the growth in direct tax revenues to be pegged at 10%.

For indirect taxes, we expect a 20% YoY increase. We expect service tax rate to be increased from 14% to 16%. Similarly, excise duty will likely be imposed / increased on various goods, to better align the rates to the proposed GST rates. The Government has already increased excise duty on petrol / diesel by Rs.4/ liter and Rs.7/ litre to Rs. 21.5 /liter and Rs. 17.33/liter, respectively, in FY16. The full-year impact of this will bring in additional Rs.500-600 bn for the Government in FY17, we estimate.

An expected improvement in economic activity and the GDP growth will justify the higher revenue growth target. (We expect nominal GDP growth to be pegged at 13% in FY17, lower than FY13, FY14 nominal GDP growth although higher than FY16 nominal GDP growth of 8.6%).

FM is likely to announce a relatively realistic disinvestment target of Rs.500bn in the Union Budget for FY17, much lower than the current financial year's target of Rs.695bn. However, at least half of that amount (Rs.250bn-Rs.300bn) could be the target for sale of the stake in loss-making state owned companies. Government is expected to provide a major push to strategic stake sales of loss-making PSUs.

Also auction proceeds of Rs500 bn from telecom frequencies will be penciled in by the FM, we believe. We also believe that, the Government may look at monetizing some of its non-core assets (eg. vacant land) to raise funds for infrastructure.

Expenditure

We expect greater focus on capital expenditure in the budget. The private sector is burdened with high debt levels and is also operating at lower capacity utilization levels. It is imperative for the government to support via infrastructure spends. We expect the FM to budget for a 30% increase in plan capital expenditure. Allocations towards important infrastructure sectors like Power, Railways, Roads, Ports, Rivers, etc will likely be enhanced, in line with the PM's goals. The focus will be on stricter and time-bound implementation of these budgets. Also, in line with the recent indications, we expect allocations for defense to be higher.

Subsidies account for about 15% of the Government's total expenditure. The sharp fall in crude prices, de-control of fuel prices and better targeting of subsidies will allow the government to provide a lower amount towards fuel subsidies in FY17. As per reports, Direct Benefit Transfer (DBT) for LPG had resulted in savings of about Rs.140bn in FY15. The government has already announced on January 1, the launch of DBT for kerosene subsidy, in a bid to cut down the diversion and black marketing of the fuel. The kerosene subsidy in FY15 was pegged at about Rs.248bn.

Apart from the above, we expect the FM to provide benefits / support to the export sector, which has been reeling under a sustained global slowdown and higher exports from China. Tax benefits in the form of MAT removal for SEZs, are likely to be announced in the budget.

On the other hand, we also expect support to the Start-Up India program of the Government, in the form of tax benefits to start-ups. The FM may look at according beneficial tax treatment to their brand building expenses in the forthcoming Budget. Start-ups and e-commerce companies will likely be allowed to appropriate initial brand building expenses over several years for taxation benefits.

Direct tax reforms to be initiated; indirect tax rates to go up

In line with the announcements made in the previous budget, we expect the FM to initiate the process of making the direct tax regime simpler. Towards this, we expect the corporate tax rate to be reduced from 30% to 25%. Correspondingly, we also expect a few exemptions / deductions to be removed. The net impact on the budget is expected to be marginal.

On the other hand, we expect the service tax rate to go up by 200bps to 16%, to bring it in line with the proposed GST rate of about 17-18%. Towards this end, we also expect excise duty to be imposed / increased on several goods, especially in some consumer goods like Green tea, dairy spreads, yoghurt, cheese, ice-cream, frozen food products, pasta, ready-to-eat foods, packaged fruit juices and soya milk. These could see excise duty kicking in or going up to the standard rate of 12.5%. Many of these products currently attract NIL-6% excise duty.

Stock markets

We do not expect any significant measures for the stock markets. Markets will be pleasantly surprised if there are downward revisions in STT rates - especially for delivery-based transactions. However, if there is a move to tax long-term capital gains, it will be a significant negative for the markets, at least in the short term. We do however believe that if such taxes are to be introduced it may happen from FY18 along with GAAR implementation, propectively.

Sectoral implications

We believe that, the focus of the markets will be more on :

Sectoral implications

We believe that, the focus of the markets will be more on :

- Maintaining fiscal rectitude,
- Initiatives to sustain and improve the GDP growth through better implementation,
- Announcement and speedier implementation of reform initiatives and
- Sectors which will be positively impacted by the budget proposals

We expect the following sectors to be positively impacted by the budget :

Expected sectoral impact

Budget impact	Sector
Positive	Auto, Banking/NBFCs, Capital Goods, Cement, Construction, Metals & Mining, Oil & Gas, Paints, Power, Shipping & Logistics.
Neutral	Agro Chemicals, Aviation, FMCG, Information Technology, Media, Pharmaceuticals, Real Estate

Source: Kotak Securities - Private Client Research

Budget estimates

(Rs bn)		2013-2014 RE	2014-2015 RE	2015-2016 BE	2015-2016 RE	2016-2017 BE
1	**Revenue Receipts**	**10,147**	**11,263**	**11,416**	**11,730**	**12,556**
2	Tax Revenue (net to centre)	8,159	9,085	9,198	9,480	10,193
	Gross Tax Revenue	11,387	12,514	14,495	13,980	16,043
	Corporation Tax	3,947	4,261	4,706	4,500	4,950
	Income Tax	2,429	2,786	3,274	3,000	3,300
	Customs	1,721	1,887	2,083	2,000	2,200
	Union Exicse	1,702	1,855	2,298	2,350	3,055
	Service Tax	1,548	1,681	2,098	1,950	2,340
	Other Taxes	41	44	36	180	198
	Assignment to States	3,182	3,378	5,240	4,500	5,850
3	Non-Tax Revenue	1,989	2,178	2,217	2,250	2,363
4	**Capital Receipts (5+6+7)**	**5,447**	**5,549**	**6,359**	**5,870**	**6,547**
5	Recoveries of Loans	125	109	108	108	118
6	Other Receipts	294	314	695	450	700
7	Borrowings and other liabilities	5,029	5,126	5,556	5,313	5,729
8	**Total Receipts (1+4)**	**15,594**	**16,812**	**17,775**	**17,600**	**19,103**
9	**Non-Plan Expenditure**	**11,061**	**12,132**	**13,122**	**13,050**	**14,308**
10	On Revenue Account	10,190	11,219	12,060	12,000	13,100
	of which,					
11	Interest Payments	3,743	4,114	4,561	4,555	4,783
12	Subsidies	2,447	2,539	2,274	2,130	2,325
	Food	920	1,227	1,244	1,250	1,450
	Fertiliser	673	710	730	660	750
	Fuel	854	603	300	220	125
13	On Capital Account	871	913	1,062	1,050	1,208
14	**Plan Expenditure**	**4,533**	**4,679**	**4,653**	**4,550**	**4,795**
15	On Revenue Account	3,527	3,669	3,300	3,200	3,040
16	On Capital Account	1,006	1,011	1,353	1,350	1,755
17	**Total Expenditure (9+13)**	**15,594**	**16,812**	**17,775**	**17,600**	**19,103**
18	Revenue Expenditure (10+14)	13,718	14,888	15,360	15,200	16,140
19	Of Which, Grants for creation of Capital Assets	1,294	1,319	1,106	1,050	1,000
20	Capital Expenditure (12+15)	1,877	1,924	2,414	2,400	2,963
21	**Revenue Deficit (17-1)**	**3,570**	**3,625**	**3,945**	**3,470**	**3,585**
	% of GDP	3.2	2.9	2.8	2.6	2.3
22	**Effective Revenue Deficit (20-18)**	**2,276**	**2,306**	**2,839**	**2,420**	**2,585**
	% of GDP	2.0	1.8	2.0	1.8	1.7
23	**Fiscal Deficit {16-(1+5+6)}**	**5,029**	**5,126**	**5,556**	**5,313**	**5,729**
	% of GDP	4.5	4.1	3.9	3.9	3.7
24	**Primary Deficit (22-11)**	**1,286**	**1,013**	**995**	**758**	**946**
	% of GDP	1.1	0.8	0.7	0.6	0.6
	Nominal GDP	112,728	124,882	141,089	135,672	153,309
	Nominal GDP Growth		10.78	12.98	8.64	13.00

Source: Budget documents 2015-16; Kotak Securities - Private Client Research

Sectorwise Expectation

AGROCHEMICALS

EXPECTED BUDGET IMPACT: Neutral

LONG TERM OUTLOOK: Positive

Current view

- India is the fourth largest producer of crop protection chemicals globally, after United States, Japan & China. The size of Indian agro chemical industry was USD 4.25 bn in FY14 and is growing at double digit growth rate with USD2.25bn of domestic sales and USD2bn of exports.
- Indian agrochemicals industry has witnessed sharp uptick in the past 10 years led by increasing awareness, thrust on farm income through rise in minimum support price, etc.
- The industry is expected to grow at 12% CAGR in the next 4-5 years, which would be driven by 8% CAGR in domestic consumption and 16% CAGR in exports.
- Indian agrochemicals Industry is more fragmented with 60 % of market catered to by 15-20 players while globally it is less fragmented with 6-7 players catering to 70-80% of the market. R&D spend in India is 1-2% of revenues while globally R&D spend is 10-12%.
- Indian agrochemicals industry is driven by generic products which contribute 70% of the market. India is targeting to become next manufacturing hub after China for agrochemicals with industry players emphasizing on R&D and contract manufacturing by partnering with global players.
- Agrochemicals are an important ingredient for the agriculture sector as they play a significant role in enhancing agricultural production. Thus the sector needs similar treatment for the purposes of levy of excise duty as the fertilizer sector. As per industry players, excise duty on pesticides which is presently at 12.5% needs to be brought on par with the duty on fertilizers.

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Reduction in excise duty	■ Reduction in excise duty from 12.5% to 8%	■ We do not expect any reduction	■ It will impact government revenue	■ Neutral

Source: Kotak Securities - Private Client Research, Industry

Top picks

Company	Price (Rs)	EPS (Rs) FY16E	EPS (Rs) FY17E	PE (x) FY16E	PE (x) FY17E	Recommendation as per our last report
NOT UNDER ACTIVE COVERAGE						

AUTOMOBILES

EXPECTED BUDGET IMPACT: Positive

LONG TERM OUTLOOK: Positive

Current view

- Auto sector performance in FY16 has been mixed. Medium and heavy commercial vehicle (MHCV) segment grew at robust pace on the back of replacement demand and lower base. Passenger car sales growth was slow and driven mainly by the new launches. In the two wheeler segment, scooters continued to grow - though at a slower pace as compared with FY15. Motorcycle demand was tepid due to weak demand in rural areas. Back-to-back poor monsoons led to additional pressure on tractor sales.
- In order to grow at a sustained healthy pace, the auto sector is expecting certain positive announcements in the upcoming budget. On the macro front, the industry is expecting the government to take steps to turnaround the sluggish rural demand. Higher budgetary allocation/stimulus could be probable ways of reviving rural demand. Give weakness in rural demand, we expect the government to focus on rural economy revival. Recovery in rural demand will be positive for players like M&M, Hero MotoCorp, Escorts and Maruti Suzuki.
- In recent times, government's focus on pollution control has increased significantly. Recently, there has been temporary ban on diesel vehicles (above engine capacity of 2000cc) in the NCR region. In that backdrop, the industry will seek more clarity about government's stance on the diesel run vehicle issues.
- Accordingly, the industry is seeking announcement on scrappage policy that would provide incentive for replacing old vehicles with new vehicles. Recently, the government has talked on this issue and we expect that there could be some announcement on this front. We believe that this would be positive for players like Ashok Leyland, Eicher Motors and Tata Motors as this will give additional spurt to MHCV demand.
- In the diesel passenger vehicle segment, the industry is looking at lowering excise duty difference between small cars and large cars/SUVs. Currently excise duty on small cars is 12.5% as against up to 30% on large cars/SUVs. Industry is looking to bring down the excise duty on large cars and SUVs to 20%. We do not expect reduction in excise duty on large cars/SUVs as the government is looking at curbing pollution and also due to revenue considerations.
- Currently, for large cars/SUVs, there are three excise duty tax slabs of 24%, 27% and 30%, depending upon car length, engine size and ground clearance. Industry is looking at rationalization of three slab excise duty structure to single slab. We believe there is possibility to unify various tax slabs for large cars/SUVs as this would fall in line with proposed two slab tax structure in GST. We believe that will be positive for M&M as it will give them level playing field.

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Lower differential excise duty	Lower excise duty on large cars/SUVs to 20% from upto 30%	Unlikely	Given govt focus on controlling pollution and revenue considerations, don’t expect excise duty to be lowered for large cars/SUVs	Neutral

Automobiles (contd...)

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Rationalize excise duty slabs on large cars/SUVs	■ Rationalize excise duty slabs on large cars/SUVs from three to one	■ Likely	■ Lower number of tax slabs will be in line with proposed GST	■ Positive for M&M
Scrappage Policy	■ Industry wants scrapping of old vehciles	■ Likely	■ Govt has talked about this in recent past	■ Positive for Ashok Leyland, Tata Motors, Eicher Motors
Incentives for green vehicles	■ Industry wants incentives for promoting green vehicles	■ Likely	■ Govt has been focusing on reduction in pollution	■ Neutral
Rural stimulus	■ Industry expects stimulus to improve demand in Rural areas	■ Likely	■ Back to back weak monsoons has significantly impacted rural demand	■ Positive

Source: Kotak Securities - Private Client Research, Industry

Top picks

Company	Price (Rs)	EPS (Rs)		PE (x)		Recommendation as per our last report
		FY16E	FY17E	FY16E	FY17E	
Maruti Suzuki	3,749	157.3	214.6	23.8	17.5	BUY
Tata Motors	310	33.9	36.0	9.1	8.6	BUY

Source: Kotak Securities - Private Client Research

AVIATION

***EXPECTED BUDGET IMPACT:* Neutral**

***LONG TERM OUTLOOK:* Neutral**

Current view

- For the aviation sector, FY16 has been a better year after a long period. Sharp fall in crude oil prices led to steep drop in ATF prices. ATF forms single largest cost component for the aviation industry. As a result of decline in ATF prices, airline operators were able to pass on some benefit in the form of reduction in fares which, in turn, translated into strong growth in domestic passenger traffic. Accordingly, airline operators have been able to report strong profits in recent quarters.
- While the current situation is favorable for aviation industry, there remains threat on account of reversal in crude oil prices. In order to mitigate the impact in ATF prices on operational performance, the industry continues to demand bringing ATF under declared goods category. Given, that the sales tax comes under the purview of state government, it will be difficult for the finance minister to make any announcement on this regard. We do not expect any significant announcement for the aviation sector in the budget. We expect the budget to likely be neutral for the aviation sector.

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Declared goods status for Aviation Turbine Fuel (ATF)	Include ATF under declared goods	Unlikely	Lowering sales tax on ATF will require approval from state governements	Neutral

Source: Kotak Securities - Private Client Research, Industry

Top picks

Company	Price (Rs)	EPS (Rs) FY16E	EPS (Rs) FY17E	PE (x) FY16E	PE (x) FY17E	Recommendation as per our last report
NOT UNDER ACTIVE COVERAGE						

Banking & NBFCs

EXPECTED BUDGET IMPACT: Positive

LONG TERM OUTLOOK: Positive

Current view

- The credit growth for the banking system has witnessed moderate growth at 10.9% YoY (as on January 22, 2016) while deposit mobilization has grown at slightly muted pace (10.3% YoY), which has led to improvement in the C/D ratio to 76.5% as on January 22, 2016 vs. 74-75% levels seen during a quarter back. We are of the view that this could be due to few opportunistic lending towards PSU undertakings rather than any sustained revival in capex cycle. Moderation in loan growth in recent times has largely come on back of subdued performance of corporate segment while retail segment continues to grow at ~15% YoY. Private sector banks have done relatively better on back of healthy growth in their retail segments. Banks have been aggressive in building retail portfolio in absence of enough corporate demand and as a result there is some pressure on yield of interest earning portfolio.
- Bank's NIM has come under pressure as most of the banks had cut the base rate by 25-30 bps during the month of September and its full impact was visible in the current quarter (Q3FY16). Several PSU banks have reported compression in NIM (QoQ) largely due to reversal of interest income as fresh slippage spiked on account of RBI's Asset Quality Review (AQR). Although we expect cost of funds to come off from current levels, there is likelihood of higher pressure on yield on assets due to shift in bargaining power in favor of borrowers along with shift in asset mix towards lower yielding secured retail portfolio (Mortgages). Hence, we are modeling marginal compression in NIM, going forward. Nonetheless, we also take cognizance of falling wholesale rates as well as sharp cut on FD rates during previous few quarters which could cushion the fall in the margins.
- Although there are few green shoots visible in the macro-environment, we believe, near term outlook remains challenging (especially PSU banks) due to higher slippage expected during Q4FY16 on account of recent RBI's AQR (Asset Quality Review). We will continue to be cautious on high exposure to stressed sectors like Infrastructure, Iron & Steel, Textiles, Agriculture, Construction and SMEs etc. Infrastructure especially power sector is under stress mainly due delay in project implementation and shortage of fuel-linkages. Although some measures have been taken in right direction, it will take some time to show material difference. For many PSU banks, stressed portfolio (Net NPA + Restructured book) has crossed 14-16% of their loan book which continues to be a risk, going forward.
- Several PSU banks having Tier-I capital at ~8%, require huge amount of capital to meet the BASEL-III regulatory norms. As per the recent GOI estimates, PSU banks would require Rs.1.8 tn during next 4 years and government has announced its plan to infuse Rs.70 bn over three years (Rs.25 bn in FY17). This is likely to help PSU banks in effectively dealing with asset quality issues and potentially growing at 12-15% (depending on size) as against the current growth rate of ~7% YoY. However, majority of them trade at <1.0x BV, so any equity issuance at CMP is likely to be book value dilutive in nature, negative for the stock performance, in our view.
- Last but not the least, consolidation in the industry has so far only been restricted to roundtables (except few deals). Now is the time to act on this, as duplication of IT infrastructure, manpower and capital is becoming prohibitively costly.

Banking & NBFCs (contd...)

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Recapitalization of PSU banks	Capital infusion in the form of tier-I capital for PSU banks (Rs.250 bn)	Likely	To improve Tier-I capital (CAR) and meet BASEL-III norms	Positive, it will provide adequate capital to support increased lending in the economy.
Deduction on provision for NPAs to NBFCs	To allow deduction to the extent of 7.5% of gross income {similar to banks under sec 36 (1) (viia)}	Likely	Remove the discrimination between banks and NBFCs.	Positive, it will improve the profitability as provision for bad & doubtful assets would be allowed as deduction.
Enhance deduction of Life Insurance Premium under sec 80C of IT Act	Enhance the investment limit from Rs.0.15 mn to Rs.0.20 mn	Status quo likely to be maintained	Fiscal constraints may limit government's ability to increase the limit	Neutral
Deduction for creation of special reserves to NBFC-MFIs	To allow deduction for creating special reserves to the extent of 20% of profits derived from eligible business.	Likely	Remove the discrimination between banks and NBFC-MFIs.	Positive, it will improve the profitability as creation of special reserves would be allowed as deduction.
Lower the TDS rate on interest earned through bank deposits	Lower from 10% to 5%	Likely	Attract more high-value term deposits	Positive, it will help bank in mobilising high value deposits.
Relaxation in the lock-in period for savings to qualify for tax benefits (Under section 80C)	Reduce from five years lock-in period to three years.	Status quo likely to be maintained	Banks are comfortable on balance sheet liquidity	Neutral

Source: Kotak Securities - Private Client Research, Indian Banking Association

Top picks

Company	Price (Rs)	PE (x) FY16E	PE (x) FY17E	P/ABV (x) FY16E	P/ABV (x) FY17E	Recommendation as per our last report
Axis Bank	403	11.5	9.8	2.0	1.8	BUY
SBI	159	11.9	9.2	1.3	1.1	BUY
IDFC Bank	52	NM	16.0	1.3	1.2	BUY

Source: Kotak Securities - Private Client Research, Indian Banking Association

CAPITAL GOODS

***EXPECTED BUDGET IMPACT:* Positive**

***LONG TERM OUTLOOK:* Positive**

Current scenario

- The initial optimism created by the new government has seen some moderation in the months leading upto to the upcoming budget. While earlier there was a broad consensus within corporate India that the economy is at the cusp of a capex cycle revival, the wait appears to have only got longer. The recent turmoil in financial markets, weak commodity cycle and continuous fall in demand from global markets has lead to risk-aversion among the corporates and this has adversely impacted the pace of order finalization. A reflection of this is the recent IIP data, which clearly indicates that the economic activity lost momentum in Q3 of 2015-16, pulled down by slackening agricultural and industrial growth. The Index of Industrial Production (IIP) stood at a negative 1.3% in December 2015.
- The RBI's quarterly survey of industrial capacity utilization and order books, indicated that the capacity utilization at 70.6% was lower at the end of the second quarter compared to the corresponding quarter of the previous year. The average new orders grew marginally in Q2FY16 from its level of previous quarter. However, it remained unchanged from its level a year ago, the report indicated.
- The stock of stalled projects rose to Rs.10.7 trillion by end-December compared with Rs.10.5 trillion at the end of September, according to data from the Centre for Monitoring Indian Economy (CMIE). The quantum of stalled projects as a percentage of those under implementation remained flat at 11.8%, the same as the September quarter, but worse than the 10.6% seen in June.
- Project tenders from government agencies in the first nine months have posted a substantial increase of 46% yoy. There has been a step-up in government spending during the current fiscal in areas like Roads, Power T&D and Railways. However, project tenders from the private sector has remained weak during the timeframe.
- Emphasis on renewable power has increased in last one year. Momentum is strong in wind and solar power installations. Wind energy sector has clocked a substantial uptick in order flows of 3200 MW in FY16. We expect momentum to continue over the next few years.
- The Budget may need to address key concerns such as declining share of domestic manufacturers following the rise in imports, resulting from free trade agreements/ preferential trade agreements signed with various countries. These agreements have not only dented the share of domestic manufacturers, resulting in under-utilisation of capacity, but have also led to inverted duty structures, which have created an uneven playing field between domestically made goods and imported products, thereby imposing higher costs on domestic manufacturers.
- The Budget is expected to focus on providing renewed thrust on domestic manufacturing. There is expectation of reinstatement of tax exemption for companies operating out of SEZs. The government is coming out with a new "Defence procurement policy" in the first week of April. The government has also unveiled a National Capital Goods Policy, which among other things aims to raise the share of capital goods in manufacturing from 12% to 20% by 2025. Though these interventions are not part of the Budget but it indicates government's priority to boost domestic manufacturing.
- At this stage, between expectation of a recovery and actual recovery, we prefer companies which have stronger earnings delivery potential and limited scope for disappointment over the next 12-18 months. Thus, we advise buying in Cummins, Voltas, AIA Engineering, Greaves Cotton and Carborundum Universal.
- On the other hand, late-cycle companies like BHEL, Thermax, EIL, Siemens and L&T would see broad-based traction in order flows only 3-4 quarters down the line.

Capital Goods (contd...)

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Duty on raw material like copper	■ To bring it in line with that on finished products	■ Likely	■ To correct the inverted duty structure and promote "Make in India"	■ Positive for Siemens, CG and ABB
plan expenditure	■ Increase in plan expenditure	■ Likely	■ Increase is needed to boost growth	■ Positive fr general capital goods
Rooftop solar installations	■ Increase subsidy on rooftop solar installations	■ Likely	■ Government has constantly emphasised rooftop solar installations	■ Positive for companies like Swelect and Ujaas
Renewable energy tax free bonds	■ Introduction of tax free bonds for renewable energy	■ Likely	■ The move shall aid funding in alternate sources of power	■ Positive for companies like Suzlon, Inox Wind, Swelect
NIIF Funding	■ NIIF funding for four projects including Hyderabad metro	■ Likely	■ To bridge viability gap	■ Positive for L&T
Duty waiver on water treatment equipment	■ Exscise Duty waiver on water treatment equipment	■ Likely	■ Impetus to zero liquid discharge systems	■ Positive for Wabag and Praj

Source: Kotak Securities - Private Client Research

Top picks

Company	Price (Rs)	EPS (Rs)		PE (x)		Recommendation as per our last report
		FY16E	FY17E	FY16E	FY17E	
L&T	1122	44.3	54.5	25.3	20.6	BUY
Praj	82	3.5	4.8	23.3	17.0	BUY
Blue Star	338	9.8	14.7	34.5	23.0	BUY
Cummins India Limited	888	27.1	30.9	32.8	28.7	ACCUMULATE
Engineers India Ltd (EIL)	147	8.8	12.0	16.7	12.3	BUY

Source: Kotak Securities - Private Client Research

CEMENT

EXPECTED BUDGET IMPACT: Positive

LONG TERM OUTLOOK: Positive

Current view

- Union Budget 2016-17 is expected to be positive for cement sector which is linked with the growth in infrastructure sector. Cement demand growth had lagged the expectations during FY16 due to slow pick up in infrastructure projects as well as lack of demand from rural sector. We expect government to continue its focus on infrastructure development. Hence, higher allocations for infrastructure sector coupled with focus on affordable housing is expected to drive cement demand growth going forward. We also expect government to provide impetus for implementing smart cities, airports, river linking projects which are also expected to boost cement demand. Along with this, we also expect specific measures from the government to ease stress in the rural economy which was impacted from two years of consecutive droughts. This is likely to improve cement demand from the rural sector also in medium to long term.
- Cement industry expects reduction in the excise duty rates as the commodity is highly taxed but we expect excise duty structure to remain same. Industry is currently burdened with high taxes and cost pressure. Though costs are likely to remain at similar levels but with implementation of GST, cement industry expects reduction in overall taxes.
- Key beneficiaries from demand improvement are expected to be Grasim Industries, Ultratech Cement, Shree Cement, ACC, Ambuja Cements etc. We continue to remain positive on Grasim Industries and Ultratech Cement.

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Higher focus on infrastructure sector	Higher spend on infrastructure segments such as roads, urban infra, irrigation, buildings etc to boost cement demand	Spending to be increased	Inline with government's target to revive the infrastructure sector	Positive for the sector
Smart city development	Incremental spend on smart city development to drive cement demand growth	Spending to be increased	In line with government's vision to develop smart cities as satellite towns of larger cities	Positive for the sector
Focus on low cost housing	Higher focus on low cost housing development	Incentives for investment in low cost housing to be announced	In line with government's vision of Affordable housing by 2022	Positive for the sector
GST implementation	Expects sooner implementation of GST	May get delayed beyond FY17	It is expected to take time to pass GST bill	Neutral for the sector

Source: Kotak Securities - Private Client Research, Industry

Top picks

Company	Price (Rs)	EPS (Rs)		PE (x)		Recommendation as per our last report
		FY16E	FY17E	FY16E	FY17E	
Grasim	3,456	226	354	15.3	9.8	BUY
Ultratech Cements	2,777	84.5	131.6	32.9	21.1	BUY

*Source: Kotak Securities - Private Client Research; * Cash EPS for Shree Cements*

CONSTRUCTION

EXPECTED BUDGET IMPACT: Positive

LONG TERM OUTLOOK: Positive

Current view

- Fiscal 2016 has seen healthy activity in the road sector and government is on target to award 10,000 km of road projects from NHAI and MoRTH. Urban infra and railways segment has also witnessed improved traction but private sector capex continued to remain subdued due to stressed balance sheets. Thus, initiatives such as faster land acquisition and project clearances to boost private sector investment are expected in the Union Budget 2016-17.
- Construction sector has witnessed increased activity on government projects specifically from the roads, urban infra, buildings and hospitality segment but sector is awaiting 'on the ground' improvement in terms of project awards across all segments. We thus expect government to enhance allocations for roads, irrigation, urban infrastructure, ports, airports, railways, power etc to put infrastructure development on fast track. Efforts to ease long term financing for the sector by inviting sovereign wealth funds to partner with NIIF and addressing issues related to short term working capital would be keenly watched out for in the budget. To improve the viability of the infrastructure projects, industry expects MAT to be abolished for the tax holiday period during Section 80IA benefits; though we don't expect the same to happen. Industry is also demand removal of DDT on SPVs under infrastructure investment trust model which we believe should be addressed.
- Key beneficiaries from higher order inflows in roads, irrigation and urban infra are expected to be IL&FS transportation network, IRB Infra, NCC, KNR Construction, PNC Infratech, NBCC, JKumar Infra, Pratibha Industries, Simplex Infrastructure etc. We continue to maintain positive stance on IRB Infra, NCC, KNR, PNC Infra and NBCC and expect these companies to benefit from incremental order inflows.

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Fund allocation	Higher budgetary allocation for roads, irrigation, urban infra	Higher allocation in budget	Would support infrastructure creation which has been impacted by lack of order inflows	Positive for the sector
Private sector participation	Enhance private sector participation	Provide projects on plug and play basis	Faster commencement and completion of projects	Positive for the sector
Easier financing	Partnering international sovereign funds with NIIF	Expect it to be materialized as government is in touch with various sovereign funds	Easier financing of big ticket projects	Positive for the sector
Smart city development	Increased allocation for development of smart cities	Higher allocation to come through in Budget	"In line with Government's vision vision to develop smart cities as satellite"towns of larger cities"	Positive for the sector

Construction (contd...)

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Faster claim settle-ment	Faster claim settle-ment to resolve working capital issues	Setting of faster claim settlement committee which would club all claims together and process them faster.	Help in freeing up working capital and enable players to bid for more projects	Positive for the sector
Bond guarantee fund	Enhance ratings and ease funding	Setting up of a guarantor for corporate bonds and underwrite bonds by compa-nies in order to enhance their ratings	Ease funding for the sector and help in setting up of greenfield and brownfield projects	Positive for the sector
DDT on SPVs on Investment trusts	Removal of DDT on SPV's under infra-structure investment trust model	Likely to be removed	Provides clarity on taxation on InVits and may fast track launch of investment trusts	Positive for the sector
MAT during the period of availment of Section 80IA	MAT should be abolished for the tax holiday period during Section 80IA benefits to improve viability of projects	Status quo maintained	Tax collection for govern-ment may get impacted	Neutral for the sector

Source: Kotak Securities - Private Client Research, Industry

Top picks

Company	Price (Rs)	EPS (Rs) FY16E	EPS (Rs) FY17E	PE (x) FY16E	PE (x) FY17E	Recommendation as per our last report
IRB Infrastructure	214	17.8	16.7	12.0	12.8	BUY
NCC	65	3.7	3.9	17.6	16.7	BUY
PNC Infratech	506	24.2	30.4	20.9	16.6	BUY
NBCC	857	27	34	31.7	25.2	BUY

Source: Kotak Securities - Private Client Research

FMCG

***EXPECTED BUDGET IMPACT:* Neutral**

***LONG TERM OUTLOOK:* Neutral**

Current view

- GST rollout is the most eagerly awaited event for the industry for several years now. GST is likely to help the industry, on the following counts: a/ level playing field with unorganized sector, b/ supply chain improvements can be brought in, c/ higher GDP growth a possibility with GST rollout. However, we think that the rollout is likely to be delayed. The issue is unlikely to have any impact on the sector.
- Related with the GST rollout is the issue of alignment of taxes towards the minimum rate in GST. As a result, there is likelihood that taxes on items such as edible oils and biscuits could be raised. This could have a negative impact on companies such as Marico and Britannia.
- Recent newspaper reports indicate that the government could significantly raise food subsidies, and spends on MGNREGA. The same shall have a positive impact on companies with greater rural exposure, such as Hindustan Unilever, and Dabur.
- Given the decline in cigarette consumption over the past year, we believe that the incremental gains from 15% hike in cigarettes shall be modest. We expect, therefore, that this budget shall see moderate rise in excise duties on cigarettes (likely 5-10%, in our opinion). If duty hike is in line with our expectations, we would expect the impact on ITC to be positive. A 15% hike in duties shall have a negative sentimental impact; however, we believe the same is factored into the price as of now.

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Goods and Services Tax	Clear timeline for GST implementation, implementation in FY17	Expect positive intent from the government, rollout in FY17 unlikely; expect excise duties on some items to rise as a pre-cursor to rollout in FY18	Political hurdles remain, on-ground preparation for rollout questionable	Dealys in rollout are factored in, so no broad negative impact. Hike in excise duties may affect categories such as edible oils, biscuits
Focus on Rural Growth	Re-energised focus on rural growth, in terms of programs such as MGNREGA and Food Subsidy	Expect significant growth in subsidies and employment generation programs	Govt. could be looking to aid rural growth after two successive weak monsoons	Expect positive impact across stocks, stocks with greater exposure to rural economy to benefir more
Excise Duties on Cigarettes	No Change, given distortionary impact of differential tax rates on tobacco products	We expect 5-10% rise in excise duties on cigarettes	We believe that successive excise duty hikes in prior budgets have reduced room for revenue enhancing excise hikes	Medium-term impact to be neutral on ITC; expect negative sentimental impact if hike is close to 15%

Source: Kotak Securities - Private Client Research, Industry

FMCG (contd...)

Top picks

Company	Price (Rs)	EPS (Rs) FY16E	EPS (Rs) FY17E	PE (x) FY16E	PE (x) FY17E	Recommendation as per our last report
Dabur India	241	7.1	8.2	34.0	29.4	BUY
ITC	300	12.5	13.8	24.0	21.7	ACCUMULATE

Source: Kotak Securities - Private Client Research

Information Technology

EXPECTED BUDGET IMPACT: Neutral

LONG TERM OUTLOOK: Positive

Current view

- FY16 has been a year of transformation for the IT services exports sector. Traditional services continued getting commoditized, whereas the new-age Digital services have grown at a fast clip. Exports are expected to grow at 12.3% in FY16 to $108bn. NASSCOM has projected a growth of 10% - 12% for FY17 in CC terms. There is stability in USA, while Indian companies are trying to increase market share in Europe. However, sector-specific concerns on sectors like Energy / Utilities and Telecom continue to impact growth rates. Digital spends are increasing, giving an impetus to discretionary spending.
- The industry is expected to have provided direct employment to 3.7mn people in FY16 and indirect employment to another 10mn. In this backdrop, the budget is expected to focus on maintaining an environment conducive to the future growth of this largely export-oriented industry.
- We expect the focus of the budget to be on Make in India as well as Digitalising India and hence, we expect various enabling measures for the sector, which is one of the facilitators for the same.
- We remain optimistic on the longer term prospects of the industry. Indian vendors have moved up the value chain. They are focusing on newer Digital opportunities like cloud, mobility, Social, Analytics, etc. Newer pricing models will likely make them participate in the growth prospects of the clients while also making business more non-linear. Also, focused smaller companies with expertise on select verticals will be able to move up the value chain and attract larger clients, thereby, improving their longer term prospects. Companies, however, need to contend with higher competitive pressures and improve efficiencies.
- We expect decent returns in IT stocks over the medium term, subject to near term volatility. At current levels, we prefer larger names like Infosys and TCS; we also retain our positive bias for select mid-caps like Geometric and KPIT.

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Support for start - ups and E-commerce ecosystem	Startups be exempted from direct / indirect taxes, including MAT	Government will address this issue	It will reduce compliance burden and reduce cash outflows	Positive
	Remove angel tax	Government will address this issue	To encourage angel funding, which is the only available source for start-ups	Positive
	CF of losses even if change in ownership structure, if it for capital infusion	Government will address this issue	To allow start-ups culture to fluorish	Positive
Deductions U/S 35	Deduction for R&D and Skill Development be allowed U/S 35	Will not be allowed	Government is looking at simplifying direct tax structure	Neutral

Source: Kotak Securities - Private Client Research, Industry, NASSCOM

Information Technology (contd...)

Top picks

Company	Price (Rs)	EPS (Rs) FY16E	EPS (Rs) FY17E	PE (x) FY16E	PE (x) FY17E	Recommendation as per our last report
Infosys	1098	58.7	67.5	18.7	16.3	BUY
TCS	2276	122.3	136.8	18.6	16.6	ACCUMULATE
Geometric	149	15.4	16.8	9.7	8.9	ACCUMULATE
KPIT Technologies	120	14.4	16.5	8.4	7.3	BUY

Source : Kotak Securities - Private Client Research

MEDIA

EXPECTED BUDGET IMPACT: Neutral

LONG TERM OUTLOOK: Positive

Current view

- The industry has been demanding infrastructure status in the backdrop of rollout of DAS, which requires heavy investments in equipment. This has been a long-standing demand, and we believe it is unlikely to be met, as we think that if the government was sympathetic on this issue, there would have been concessions earlier.
- The rollout of GST can be a significant development for the industry. We note that the Media sector suffers from multiple taxation issues, especially in cable/ DTH and movies exhibition. While taxes are likely to be subsumed into GST, we believe the rollout of GST shall be delayed. In the meanwhile, there is a likelihood of higher service tax (for alignment with GST), which would be a modest negative for the industry.
- Media companies have been demanding tax holiday for radio FM and setting up new multiplexes. We do not think these shall be priority areas for the government (seen more as indulgence than necessities). As a result, we do not expect any action on this issue.
- Net-net, we think the budget shall be a non-event for the sector.

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Infrastructure Status	Grant of Infrastructure status to the media sector	Unlikely	Long-Standing demand, fiscal pressures, non-grant during Phase-1 and Phase - 2, and prior to Phase - 3 DAS indicate govt. has decided against	No impact, non-grant is factored in
Goods and Services Tax	Ensure inclusion of highly taxed sub-sectors in GST, rollout of GST	Expect delays in GST rollout, likely in FY18, rise in service tax (alignment with GST)	Political hurdles remain, on-ground preparation for rollout questionable	No impact of delays in GST rollout; negative impact on DTH from higher service tax
Tax Holiday	Tax Holiday for FM Radio players and setting up new multiplexes	Unlikely	Fiscal pressures; the industries looked at as self-sustaining and indulgence rather than necessity	No impact

Source: Kotak Securities - Private Client Research, Industry

Top picks

Company	Price (Rs)	EPS (Rs)		PE (x)		Recommendation as per our last report
		FY16E	FY17E	FY16E	FY17E	
HMVL	268	24	27.6	11.2	9.7	ACCUMULATE
TV18 Broadcast	37	1.1	2.1	33.2	17.4	BUY
ZEE Entertainment	371	10.5	13.8	35.3	26.9	BUY

Source: Kotak Securities - Private Client Research

METALS & MINING

***EXPECTED BUDGET IMPACT:* Positive**

***LONG TERM OUTLOOK:* Neutral**

- We expect the union budget to have a positive impact on the prospects of Metals & Mining Industry and companies operating within it.
- We believe that higher fund allocation for infrastructure development in road, power, railways, ports and airport sectors would lead to improved demand for metals.
- We also believe that various measures by the government in terms raw material security would go a long way to make metal sector more competitive.
- We expect budget to have a positive impact on the sector, however, near term outlook remain cautious because of weak global scenario.

Key budget expectations - Metals & Mining

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Bauxite: Ban on export or increase export duty	50%	25%	Bauxite exports to China have increased 45% YoY, leading to the paucity of the raw materials	Positive for aluminium players
Increase in import duty **a) On aluminium from 5%** **b) On aluminium scrap from 2.5%**	10-15%	a) 10% b) 5%	As share of imports has risen sharply YoY to 51% vs 40% earlier	Positive for aluminium players
Increase in tariff rate of basic custom duty from 15%	25%	20%	MIP has been imposed for the period of 6 months. Post that, increase in import duty and other measures would protect the industry from cheaper imports, provided MIP is not extended.	Positive for all steel players
Reduction in iron ore export duty **a) For grade below 58 per cent from 10%** **b) For other grade from 30%**	Nil	a) Likely for grade below 58% b) Unlikely	There are hardly any buyers of iron ore for the grade below 58 per cent. As over 85% of the iron ore export constitutes of fines or low-grade ore, we do not expect any reduction in export duty of high grade ore	Neutral
Removal of custom duty on coking coal from 6% (2.5% import duty and 3.5% clean energy cess)	Nil	Unlikely	Revenue implication for Government, as protection already given to steel companies.	Neutral
Removal of inverted duty structure and slashing import duty on aluminium Fluoride, caustic soda which is at 7.5% and 5% for coal tar pitch	Nil	Likely	Import duty on key raw materials is affecting the cost competitiveness of domestic aluminium industry. However, if import duty on aluminum is increased, then slashing of import duty on key raw materials is unlikely.	Positive for aluminium players

Metals & Mining (contd...)

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Thrust on infrastructure	■ Infra push.	■ Likely	■ Significant increase in allocation to key infrastructure projects will drive demand	■ Positive for steel companies present in long product segments

Source: Kotak Securities - Private Client Research, Industry

Top picks

Company	Price (Rs)	EPS (Rs)		PE (x)		Recommendation as per our last report
		FY16E	FY17E	FY16E	FY17E	
Tata Sponge	364	16.3	45.4	22.3	8.0	BUY
National Aluminium Company	33	2.7	2.9	12.1	11.2	BUY

Source: Kotak Securities - Private Client Research

OIL & GAS

***EXPECTED BUDGET IMPACT:* Positive**

***LONG TERM OUTLOOK:* Positive**

Current view

- We expect Union Budget to lay down road map for the sector. It will focus on reforms which are crucial for the sector and overall economy. In order to ensure energy security for the economy, the Government of India has accorded high priority to extraction, production of crude, Petroleum oil and Natural gas. We expect government to make policies which would attract large foreign investments in the sector. Clarification on the divestment policy is also required.

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Cess on domestic production	Upstream companies want reduction in Cess	Reduce from Rs.4500/mt to Rs.2500/mt	To provide relief to upstream companies. Govt. can recoup the same by hiking excise duty on petrol and diesel.	Positive for upstream companies
Tax Holiday for Exploration and Production activities relating to natural gas and CBM	Explicitly provide that the term 'mineral oil' will include natural gas and CBM for all past and future rounds of NELP for the purposes of Section 80-IB of the Act.	We expect clarity on the same.	This will avoid uncertainty among upstream players.	Positive for CAIRN India, RIL, HOEC, Selan exploration.
MAT - exempt from the purview of Section 115JB of the Act	Oil exploration and production companies should be exempted from the purview of Section 115JB of the Act to promote the domestic exploration and production. This will reduce import dependence of the nation.	We do not expect the same	Considering the tight fiscal situation government may not do so	Neutral
Custom duty on crude	Upstream companies want govt. to hike custom duty on crude oil imports	Custom duty may be restored	We expect custom duty to be hiked to support producers	Positive for upstream companies such as ONGC, OINL, Selan explora-tion, etc. Negative for OMCs.
Exempt LNG from 5% import duty	Import duty on LNG to be reduced from 5% to NIL.	We do not expect reducing duty to NIL.	It will significantly impact government revenues. GOI may prefer direct subsidy to power and Fertilizer sector.	Neutral
Focus on building strategic petroleum reserves	MoPNG has sought Rs 150 bn from the Ministry of Finance to build the second phase of the country's strategic petroleum reserves	Government may draw a road map for the same	India is planning to build a 12.5 mmtpa of storage capacity under phase-two at four locations-Bikaner (Rajasthan), Rajkot (Gujarat), Chandikhol (Orissa) and Padur.	Positive for PSU refineries

Oil & Gas (contd...)

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Support to startups engaged in the oil sector	■ Financial support to startups engaged in the oil sector	■ This may be taken separately	■ Financial partnerships to new startups engaged in exploration and production and downstream activities to encourage local innovation and add skills.	■ Positive

Source: Kotak Securities - Private Client Research, Industry

Top picks

Company	Price (Rs)	EPS (Rs) FY16E	EPS (Rs) FY17E	PE (x) FY16E	PE (x) FY17E	Recommendation as per our last report
MRPL	60	0.66	8.85	91.0	6.8	BUY
Oil India	316	37.7	40.7	8.4	7.8	BUY

Source: Kotak Securities - Private Client Research

PAINTS

EXPECTED BUDGET IMPACT: Positive

LONG TERM OUTLOOK: Positive

Current view

- Performance of the paint sector is strongly correlated to GDP growth in the country. The volumes for paint companies would be driven by factors like: 1) Growth of the real estate sector, 2) Push for infrastructure projects, 3) Increase in construction activities, 4) Initiatives like SMART CITY programme and 5) Demand for vehicles.
- Paint companies want the government to continue with its reform process in the real estate and infrastructure segment which would indirectly stimulate demand both for decorative and industrial paints.
- Paint companies are also looking forward to effective implementation of the SMART CITY imitative
- Long-term case for high growth for paints remains is valid in a country like India where per-capita consumption is low, urbanization trends are picking up, re-painting cycles are getting shorter, and consumers are incrementally trading up.

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Infrastructure push	Reforms for Infra push	Likely	India is lacking in infrastructure	Would create demand for industrial paints directly/ decorative paints indirectly
Smart city	Speedy implementation of smart city plans	Likely	Decongestion from big cities and broadbased growth	Improved demand across industries

Source: Kotak Securities - Private Client Research, Industry

Top picks

Company	Price (Rs)	EPS (Rs)		PE (x)		Recommendation as per our last report
		FY16E	FY17E	FY16E	FY17E	
Asian Paints	856	19.1	23.2	44.8	36.9	ACCUMULATE

Source: Kotak Securities - Private Client Research

Pharmaceuticals

***EXPECTED BUDGET IMPACT:* Neutral**

***LONG TERM OUTLOOK:* Positive**

Current view

- Indian pharma market has witnessed a robust 13% CAGR over last ten years, except 2013. The slower growth in 2013 was due to the new NLEM (National List of essential medicines) implementation. The NLEM policy led significant price reductions in medicines which resulted in a mere ~6% growth in IPM in 2013. Year 2015-16 has been a muted year as companies regained their composure and lost sales, however growth gradually inched up to double digits. We believe, companies will continue to face bouts of price controls which will continue to impact profitability. However, as the contribution from Indian market for individual companies are on slide, we do not foresee any threat per se.
- On the exports front India continues to be a major supplier and has showcased its cost competitiveness as well as R&D capabilities well enough. India has been third largest supplier of drugs globally and is expected to continue to grow at mid-teens CAGR over the next few years.
- However, as far as local API consumption is concerned, India has become highly dependent on China for APIs (Active Pharmaceutical Ingredient). For widely prescribed antibiotics like Pencilin-based drugs, India is 100% dependent on China. Companies have lost to Chinese competitors on the API front only because of the lack of cost competitiveness. Recently, government raised the customs duty on 61 bulk drugs (APIs) to 10% from 5% earlier, but more needs to be done.
- With the new government's focus on 'Made in India', Industry expects some rebate on pharma SEZ's, which will encourage manufacturing expansion locally. The sector also expects some relief on R&D tax exemptions. As of now the companies can claim up to 200% of claim on R&D expenses incurred in India. But companies are expecting this deduction to be extended to the R&D expenses incurred abroad which is usually done for filings in export markets.
- We expect the budget to be Neutral for the sector. Key things to watch: Changes in government spend on Healthcare, Tax relief to pharma SEZ's, Tax benefits on R&D expense, Excise duty on APIs.

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Weighted deduction on R&D expenses	Expand weighted deduction on R&D expenses to outsourced clinical trials/R&D and DMF/ ANDA filings with the US FDA	Status Quo	Weighted deduction to R&D is for encouraging innovative medicines in India only and will be limited to the same	Neutral
Tax incentive on SEZ	Exempted SEZ's from MAT once again	Expect some relief	India has become highly dependent on Chinese imports for APIs, tax rebates would encourage expansions locally	Positive
Excise duty on APIs	Excise duty reduction for API manufacturers	Expect some relief	Under the current excise regime, inputs i.e. APIs attract higher rate of excise at 12.5 per cent whereas the output is taxed at 6%. The excise duty rate of APIs should be rationalised and made at par with pharma goods	Positive

Source: Kotak Securities - Private Client Research, Industry

Pharmaceuticals (contd...)

Top picks

Company	Price (Rs)	EPS (Rs)		PE (x)		Recommendation as per our last report
		FY16E	FY17E	FY16E	FY17E	
Alembic Pharma	609	22	33.1	27.7	19.6	BUY
Sun Pharma	856	22.9	37.1	37.4	23.1	ACCUMULATE

Source: Kotak Securities - Private Client Research

Power

EXPECTED BUDGET IMPACT: Positive

LONG TERM OUTLOOK: Neutral

Current scenario

- During Apr-Dec period of FY15, the power generation capacity addition stood at 11226 MW vs 10610 MW during the corresponding period of the previous fiscal.
- As against a demand of 837 bn units in April-December 2015, the power availability was 819.2 bn units, implying a power deficit of 2.1% in the period. The deficit was highest in the Northern region at 5.0% followed by the Southern region.
- While on the face of it, it may appear that supply deficit in power has been largely plugged. However, the fact remains that power discoms are not buying enough power from generation units. This has resulted in decline in PPAs floated by discoms resulting in a significant installed capacity remaining idle.
- Average PLF of thermal power utilities stood at 61.7% vs 64.5%, well below the normative level of 85% required to recover fully the fixed costs
- The coal supply situation has eased in recent months thanks to a combination of weak industrial demand, outtages by discoms and improvement in domestic coal supply. Thus, the reported number of plants with coal stock at the critical level has fallen sharply.
- At the current juncture, the most critical issue for the power sector is that of weak financials of state discoms. However, the recently announced "UDAY" (Ujjwal Discom Assurance Yojana) programme attempts to address this problem. One of the aims of the programme is targeted reduction of AT&C losses, which would require interventions at various levels in terms of 1) investment in metering at feeder and distribution transformer level, 2) Smart meter and 3) upgradation of distribution transformers. Through this programme, the participating Discoms can look forward to higher free cash flows as interest burden would decline significantly after bulk of borrowings are transferred to state governments and the rest are converted into bonds at lower cost of borrowing.
- Healthy distribution utilities would reduce the risk associated with investments in power sector stocks such as NTPC, Powergrid and Tata Power.

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Removal of clean energy cess (Coal cess)	Thermal power companies seek removal (or reduction) of clean energy cess	Unlikely	Government is committed to clean energy like wind and solar	Neutral
MAT	Abolition of MAT	Unlikely	Unlikely	Neutral
80 IA benefit	Continuation of 80 IA benefit	Likely	Need to make cost of power affordable	Neutral
Infrastructure status to power T&D	Granting of infrastructure status to power T&D	Likely	T&D sector is highly under-invested in India. The move shall promote participation in the sector	Positive for Sterllite Power and Techno Electric

Source: Kotak Securities - Private Client Research, Industry

Power (contd...)

Top picks

Company	Price (Rs)	EPS (Rs)		PE (x)		Recommendation as per our last report
		FY16E	FY17E	FY16E	FY17E	
Tata Power	59	8.3	9.4	7.1	6.2	BUY

Source: Kotak Securities - Private Client Research

REAL ESTATE

***EXPECTED BUDGET IMPACT:* Neutral**

***LONG TERM OUTLOOK:* Cautious**

Current view

- During November 2015, government had relaxed FDI norms for the sector including restrictions of minimum area, minimum investment required as well as easing of provisions to exit once lock-in is complete even if the project is not completed.
- We expect Union Budget 2016-17 to be largely neutral for real estate sector. Sector has been plagued by demand slowdown, high interest rates and delays in approvals from past several quarters. Problems associated with land acquisition, lack of transparency and clarity in land titles compounded the issues, thereby impacting sector.
- From Union Budget, industry is expecting measures to boost demand for the sector which include higher disposable income as well as subsidized interest rates for low cost housing. In order to fast track the projects, industry also expects measures to ease land acquisition, single window clearance as well as implementation of real estate regulatory bill.
- We also expect clarity to emerge on tax treatment of REITs which may fast track the launch of REITs and hence will be positive for the sector. Industry is also expecting faster implementation of GST which we believe would take time.

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Income tax exemption limit on interest payment	Increase the limit from Rs 2 lac to Rs 3 lac	Status quo maintained	Provides benefit to home buyers but may impact tax collections	Neutral for the sector
Income tax exemption limit for principal repayment	The deduction for principal repayment of housing loan under Section 80C should be either increased from the existing limit or the principal repayments considered for a separate tax exemption	Status quo maintained	Provides benefit to home buyers but may impact tax collections	Neutral for the sector
Tax incentives for rental housing	Tax breaks specific to rental housing to boost rental supply in cities	Status quo maintained	It may impact tax collection	Neutral for the sector
Tax treatment of REITs	a)Dividend distribution tax on dividend by SPVs to REIT should be done away with b)Stamp duty and taxes on rents should be exempted	Can be implemented	Provides clarity on taxation on REITs and may fast track launch of REITs	Positive for the sector
Stamp duty exemption	REITS should be exempted from stamp duty, taxes on rent etc	Status quo maintained	Stamp duties are to be decided by State government	Neutral for the sector

Real Estate (contd...)

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Incentivize affordable housing	■ Subsidised interest rate, easier financing for developers of low cost housing	■ Possible	■ To give boost to sector and the low income population	■ Positive for the sector
Industry status	■ Sector seeks industry status as it generates countless jobs across its verticals and would also enable easier lending for the sector	■ Status quo maintained	■ It may take a while before it gets implemented. Regulatory norms (like high risk weight etc) itself discourage lending to this sector	■ Neutral for the sector
Single window clearance for projects	■ Industry expects a single window clearance to enable faster execution of projects	■ Status quo maintained	■ It may take a while before it gets implemented as it requires approvals of various state and central government departments	■ Neutral for the sector
Infrastructure status for development of integrated townships	■ Industry wishes infrastructure status for township development so that banks are able to give priority sector lending to the sector	■ Can be implemented	■ Development of large townships will mitigate housing shortage.	■ Positive for the sector
GST implementation	■ Expects sooner implementation of GST	■ May get delayed beyond FY17	■ It is expected to take time to pass GST bill	■ Neutral for the sector

Source: Kotak Securities - Private Client Research, Industry

Top picks

Company	Price (Rs)	EPS (Rs) FY16E	EPS (Rs) FY17E	PE (x) FY16E	PE (x) FY17E	Recommendation as per our last report
Phoenix Mills	286	11.4	12.9	25.1	22.2	BUY

Source: Kotak Securities - Private Client Research

Shipping & Logistics

***EXPECTED BUDGET IMPACT:* Positive**

***LONG TERM OUTLOOK:* Positive**

Current view

- The Baltic Dry Index (BDI) is trading at its historical low (at 313) weakest since 2010 primarily due to slowdown in the Chinese economy and a huge over-capacity in vessels. Freight rates in the bulk sector are currently so low that it fails to cover even the operating cost of running a vessel. (Without taking into account possible financing). On the other, with crude oil prices falling considerably, net importing countries like China and to some extent India are importing more oil keeping the dirty tanker/product segment firm.
- The Indian shipping and the shipbuilding sector is primarily looking for financial support from the government by way of subsidies.
- Despite holding promise the logistics sector in India remains mired in several complexities which have the potential of holding it back. These include significant inefficiencies in transportation, poor storage infrastructure and a complex tax structure.
- The Indian logistics companies operate in the areas of warehousing, container freight station (CFS), container rail, freight forwarding, non-vessel owning container carrier (NVOCC) and trucking. In our discussion with companies, most of the companies including Concor, Gateway Distriparks Limited (GDL) and Allcargo are expecting the Finance Minister to announce measures for speedy implementation of the dedicated freight corridor (DFC), speedy implementation of the ongoing infrastructure projects and faster roll out of the Goods and Services Tax (GST) which would help the industry to realign infrastructure and improve it cost structure
- Roll out of the Goods and Services Tax (GST) which would help the industry to realign infrastructure and improve it cost structure
- As per our estimates, investments worth ~USD 1 trillion are in the pipeline for the logistics sector in India covering rail, road, ports, airlines, logistics service providers, warehouses and warehousing-zone. Pick-up in trade and a favorable investment environment are likely to benefit the entire sector

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Subsidy allocation for Indian shipbuilding industry	Substanial allocation for shipbuilding subsidy	Likely	Shipbuilding is a global business and globally Indian Shipbuilding companies receive plenty of tax sops and other financial sops from the government	Positive as it will enable the shipbuilding companies to become competitive and attract more orders
Road map for GST roll out	Abolishing Central sales tax and State-Value Added Tax (VAT)"	Likely	Current supply chains are inefficient with warehouses in almost every state.	Positive as it would realign warehousing in the country and lower turn-around time for trucks benefiting logistics companies
Transport infrastructure	Speedy implementation of projects and increased focus on road, rail and ports	Likely	Transport infrastructure is still underdeveloped in the country and is integral for economic development	Positive as an efficient, reliable, and safe transport system is vital for fostering rapid economic growth

Shipping & Logistics (contd...)

Key budget expectations

Issues	Industry wish-list	Our expectation	Rationale for our expectation	Impact of our expectation
Dedicated Freight Corridor (DFC)	Faster roll- out of DFC	Likely	Passenger rail services are given priority over container/cargo train which increases the turnaround time and operating cost	Positive as it would lower the turnaround time for rail companies, increase container volumes and decongest the roads.
FDI	Industry wants FDI in ports and hinterland connectivity	Unlikely	Road, rail and ports are important strategically and from security perspective	Neutral
Industry status	Industry Status to Logistics Industry	Unlikely	Logistics industry cost ~13% to the GDP but is largely fragmented and unorganised and works with high operational expense	Positive as it would facilitate easier access to finance, meaningful regulations and rationalisation
Decentralising Indian Railways	Delinking of Indian Railways and Ministry of Rail to avoid conflict of interest	Unlikely	Indian Railways is the largest employment generator and one of the largest revenue generator for the government and hence the government would like to keep complete control on the segment through a ministry	Neutral

Source: Kotak Securities - Private Client Research, Industry

Top picks

Company	Price (Rs)	EPS (Rs)		PE (x)		Recommendation as per our last report
		FY16E	FY17E	FY16E	FY17E	
Allcargo Logistics	155	10.5	12.3	14.7	12.6	BUY
Gujarat Pipavav Port	154	5.5	6.5	14.5	16.5	BUY
Adani Ports and SEZ	213	13.1	16.8	16.2	12.6	BUY
Concor	1187	59.3	66.3	20.0	17.9	BUY

Source: Kotak Securities - Private Client Research

RATING SCALE

Definitions of ratings

BUY	–	We expect the stock to deliver more than 12% returns over the next 9 months
ACCUMULATE	–	We expect the stock to deliver 5% - 12% returns over the next 9 months
REDUCE	–	We expect the stock to deliver 0% - 5% returns over the next 9 months
SELL	–	We expect the stock to deliver negative returns over the next 9 months
NR	–	**Not Rated.** Kotak Securities is not assigning any rating or price target to the stock. The report has been prepared for information purposes only.
RS	–	**Rating Suspended.** Kotak Securities has suspended the investment rating and price target for this stock, either because there is not a sufficient fundamental basis for determining, or there are legal, regulatory or policy constraints around publishing, an investment rating or target. The previous investment rating and price target, if any, are no longer in effect for this stock and should not be relied upon.
NA	–	**Not Available or Not Applicable.** The information is not available for display or is not applicable
NM	–	**Not Meaningful.** The information is not meaningful and is therefore excluded.
NOTE	–	Our target prices are with a 9-month perspective. Returns stated in the rating scale are our internal benchmark.

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