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CONTENTS

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Mcap : Rs45,53,796 cr.
BSE
52 Wk H/L : 15600.30/7697.39

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by **S. Gopichand** on behalf of Karvy Stock Broking Limited.

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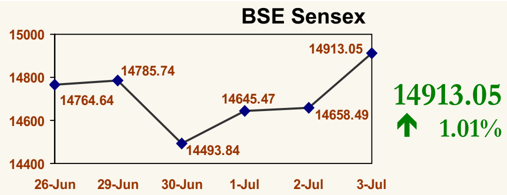
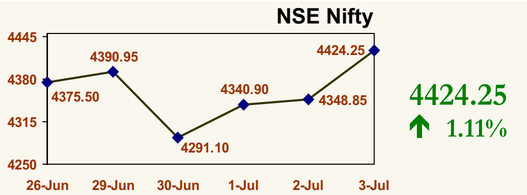




Union budget- Thumbs up or down?

Contrary to the widely perceived pre-budget rally, the markets remained cautious and languished with a negative bias for most part of last week. However, on the day of the railway budget, the markets showed some resilience and managed to close near the highs made during the week. The markets surged after the Railway Minister announced a number of new initiatives in the 2009-10 Rail Budget, including a plan to improve railway infrastructure across a large number of railway stations and railway land bank development through public-private partnership (PPP). Clearly, the last day of the week was the most convincing for the bulls (inspite of the negative global cues) as the indices closed by over 1.7% for the day on the back of a pro-business and pro-consumer railway budget. The bellwether BSE Sensex and NSE Nifty closed the week at 14913.1 and 4424.3, showing a week-on-week rise of 1.01% and 1.11%, respectively.

Among the sectoral indices, the BSE PSU index rose the most by 3.84% during last week, buoyed by the divestment and related reforms expected to be announced by the UPA government in the Union Budget 2009-10 on Monday, July 6, 2009. Meanwhile, the Economic Survey released on July 2 appeared to be very much in favor of further liberalization. It called for a review and phasing out of surcharges, cesses and various transaction taxes, such as commodities transaction tax (CTT), securities transaction tax (STT) and fringe benefit tax (FBT). Others include foreign direct investment (FDI) in multi-format retail starting with food retail, raising foreign equity share in insurance to 49%, rationalizing dividend distribution tax, and revival of the disinvestment plan to generate at least Rs25,000 crore annually. If the government goes ahead and announces some of these reforms, the markets could give a thumbs-up. However, we believe that keeping fiscal deficit under control may limit the government's ability to go overboard with a large increase in spending. This uncertainty was reflected in last week's trade, and the further trend in the markets will be determined from the final outcome of the "Union Budget".

KBB weekly recommendations for the week beginning 06th July.

Scrip	Action	CMP	Entry	Stop Loss	Target	Time Frame
HCC	Buy	109.05	108-110	104.80	118-120	5-6 Days
ABB	Buy	784.70	Above 788	774.10	848-850	5-6 Days
Crompton Greaves	Buy	300.90	Above 303	295.80	328-330	5-6 Days
Tata Power	Buy	1187.10	1180-1185	1170.80	1238-1240	5-6 Days
PFC	Buy	208.70	205-208	202.05	227-230	5-6 Days

Disclaimer: The above recommendations are purely based on technical analysis. Hence, the stop loss should be strictly adhered to.

KBB weekly performance monitor

Scrip	Action	Entry	SL	Target	Shares(#)	P/L	Return	Remark
LT	Buy	1600-1610	1562.00	1700-1705	143	-6,136.54	-2.68%	SLT
HDIL	Buy	246-250	240.10	272-274	-	-	-	CMP
IFCI	Buy	55-56	51.80	65-66	4127	-15,270.00	-6.67%	SLT
IVRCL	Buy	374-378	368.10	405-406	609	-4,812.49	-2.10%	SLT
Alok Inds	Buy	21-22	19.80	29-30	-	-	-	NI
Total						-26,219.03		

Balance on inception (26- Jan- 09)	Balance last week (26-June-09)	Balance current week (03-July-09)	Abs. returns WoW (%)	Abs. returns since Jan 26, 2009(%)
5,00,000	6,87,151	6,60,932	(3.82)	32.19

TA - Target achieved; SLT - Stop loss triggered; CMP - Closing price as on last trading day; NI - Not initiated; # No. of Shares; SL - Stop Loss; P/L - Profit/Loss

Budget Expectations

The stock market expectations remain high as the countdown commences for the presentation of the Union Budget—the first from the re-elected United Progressive Alliance (UPA) government on July 6, 2009. The capital market is of the view that the government can stimulate the economy, reinforce fiscal prudence and yet enhance social welfare programmes. However, we are less optimistic and although we believe that the government would announce some stimulus packages for the economy, fiscal deficit constraints would limit the efficacy of such proposals.

Investment in the economy remains the key

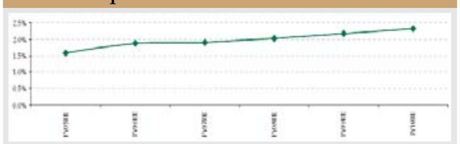
Over the last 16 years, the central government abdicated its responsibility to create infrastructure in the economy by reducing its planned capital-expenditure-to-GDP from 3.9% in FY1994 to 0.6% for FY10BE. Although this neglect was partially compensated by private sector investment in FY06-FY08, the private sector is currently unable to drive investment in the economy due to economic slowdown and the drying up of global liquidity. Therefore, only the government can raise resources and undertake risks for capital investment during a slowdown.

Plan capital expenditure to GDP (%)

Source: KSBL Research

As India's GDP for FY2010 is estimated at Rs60,214 bn (US$1.25 trillion), the government has to significantly increase its plan capital expenditure to GDP over a sustained period to achieve a higher GDP growth. The current expenditure of 0.6% of the GDP is far too trivial to make an impact on the economy. To achieve a high sustained investment programme, the fiscal deficit has to increase in the short-term to generate resources to invest, as a sustained and inclusive growth can take place only through higher investment (especially in labour-intensive sectors). However, in the medium term, the fiscal deficit would reduce as higher revenues will be generated from the increased investment in the economy. Although we believe that the government is unlikely to venture on such a bold programme of investment and it will instead announce public-private partnership proposals. The only issue in such cases would be the ability of the private sector—in a period of economic slowdown—to undertake risk and to get the necessary funding support.

Welfare Expenditure to GDP



Source: KSBL Research

Welfare programmes may again peak in the last year of the current government

There are expectations that following the electoral success of the Bharat Nirman programme and the farm loan waiver scheme, the government may continue to announce many more schemes, thereby putting further pressure on the fiscal deficit. We believe that the government would again gradually increase the welfare schemes, which would peak as the next election draws close. During the last five years, welfare expenditure to GDP gradually increased from 1.6% of GDP in FY05 to 2.3% for FY10BE. Such a gradual accelerated programme not only promoted development but also contributed to the UPA's re-election.

Divestment and revenue from telecom bids

There are indications that the government would announce major divestments of government companies aggregating around 0.5-1% of the GDP over the following four years. We believe that if the proceeds of divestment are used merely to offset the deficit, then the government would be imprudently utilising one-off revenue items to offset normalized revenue expenditure. This would merely postpone the problem and the government's finances may be in a worse state after selling off its silver. The government has the option of creating a separate capital expenditure fund from such proceeds, but even at 1% of GDP, it is not very significant. Furthermore, since FY1992, the government has cumulatively raised only Rs516 bn from divestment

The net deficit bridged in the sale of 3G and WiMax spectrum is expected to be Rs234 bn (0.4% of the GDP).

3G or third-Generation is a family of standards for wireless communications defined by the International Telecommunication Union that includes GSM EDGE, UMTS, and CDMA2000 as well as DECT and WiMAX. Moreover, services include wide-area wireless voice telephone, video calls, and wireless data, all in a mobile environment. Compared to 2G and 2.5G services, 3G allows simultaneous use of speech and data services and higher data rates.

Particulars	Rs bn
Amount raised through auction of 3G spectrum	294
Amount raised through auction of WiMax license	88
Amount to deployed in building alternative communications network for Defence	(148)
Net deficit expected to be bridged through the spectrum sale	234

The long awaited auction of 3G licenses in the Indian telecom market is due to happen in the coming days. The major points to be noted here are –

✓ The minimum bid amount for pan-India spectrum is double that recommended by the telecom department and stands at Rs40.4 bn per license. However, we believe that the median amount raised per license may be around Rs42 bn.

✓ According to industry sources, the pricing will act as a deterrent for relatively new telecom players to participate in the auction as they would need to invest an additional ~$1 bn for the 3G licenses over and above the investments they are making to roll out their new 2G networks.

✓ We do not expect very aggressive bidding for the spectrum given the current global scenario and liquidity constraints.

✓ It has been decided that up to seven operators (with one slot being reserved for state-owned telecom companies, BSNL and MTNL) will be allowed to offer 3G services across the country. However, the government telecom companies will have to match the highest bidder.

✓ Going by the assumption that all slots get booked, the government is expected to raise ~Rs294 bn through the auction of 3G licenses.

✓ Operators are likely to go for 3G spectrum for voice services.

WiMax

WiMax or the Worldwide Interoperability for Microwave Access is a telecommunications technology that provides wireless transmission of data at a speed of up to 3 mbps without the need for cables and even while on the move. The technology will give an impetus to the penetration of broadband in the country and give immense push to the various

Market pulse

Bulk Deals			
Company	Wt. Avg. Price (Rs.)	Traded Qty	Acquirer/Seller
Buy			
United Spirits	879.88	1060000	Capital International Emrg Markets Fund
Aurobindo Pharma	460.00	1417000	HSBC Invest (Hk) Ltd A/c HGIF India Equity Fund
Avery India	133.47	267619	Deutsche Trustee Servicesindia Pvt Ltd
Voltamp Tran	869.99	310000	Deutsche Securities
Sell			
Kalin Rail	223.35	83152	Matrix Equitrade Pvt. Ltd
Ispat Industries	22.02	11266446	Jaypee Capital
Everonn	440.88	132745	Multiplex Capital Ltd

Top Gainers (Weekly)			
Company	03-July	26-June	%Change
Tata Steel	437.95	388.55	12.71
GAIL	316.85	284.35	11.43
BPCL	459.90	421.35	9.15
ONGC	1136.15	1044.60	8.76
Axis Bank	873.35	818.05	6.76
SAIL	161.65	151.60	6.63
HDFC	2586.30	2435.15	6.21
PNB	694.45	655.20	5.99
M&M	738.70	698.10	5.82
NTPC	204.40	194.95	4.85

Top Losers (Weekly)			
Company	03-July	26-June	%Change
Suzlon	106.85	123.50	-13.48
Tata Motors	300.80	340.25	-11.59
Idea Cellular	74.40	79.50	-6.42
Rcom	292.55	312.35	-6.34
ACC	768.70	799.10	-3.80
Hindalco	83.80	86.70	-3.34
National Aluminium	298.85	308.00	-2.97
Hero Honda	1370.10	1406.20	-2.57
ITC	191.70	196.70	-2.54
Cair India	228.90	234.10	-2.22

	FII Invt (Rs.cr)		MF (Rs.cr)	
Date	Purchases	Sales	Purchases	Sales
29-Jun-09	2547.70	1874.80	1013.40	838.20
30-Jun-09	2388.10	1990.90	932.50	1212.60
1-Jul-09	2952.10	2723.20	625.20	791.20
2-Jul-09	1448.60	1284.90	755.70	962.80
3-Jul-09	2302.70	1900.80	-	-
Total	**11639.20**	**9774.60**	**3326.80**	**3804.80**

Corporate Actions		
Company	Date	Purpose
Infosys	10-Jul-09	Audited Results
Axis Bank	13-Jul-09	Unaudited Results
Power Finance Corp	14-Jul-09	Unaudited Results
HDFC Bank	14-Jul-09	Unaudited Results
Bajaj Auto	16-Jul-09	Unaudited Results

(Compiled by Krishna Veni M.)

e-governance programmes. India has about 6 million broadband connections now and is adding around 1 million subscribers per year. However, the government had set a target of 20 million users by 2010. The major points to be noted regarding WiMax auction are:

✓ The minimum bid amount for pan-India WiMax license is expected to be approximately Rs20.2 bn. However, we believe that the median amount raised per license may be around Rs22 bn.

✓ Going by the assumption of 4 slots getting booked, the government is expected to raise ~Rs88 bn through the auction of WiMax licenses.

✓ Once WiMax spectrum auction takes place, WiMax BTS can be deployed by operators within 90-120 days.

✓ Telecom operators are expected to use WiMax for data services like video streaming.

Defence sector to get ~$3.1 bn from 3G auction

Over $3.1 billion of the proceeds from the upcoming 3G spectrum auctions is likely to be given to the defence forces to build an alternate communications network. However, it is the state-owned BSNL, which is likely to be the biggest beneficiary, since the entire sum will be given to the telecom company to build and maintain this network for the armed forces. The major points to be noted are:

✓ BSNL is slated to complete the defence network, which involves 50,000 km of fibre in core network, 10,000 km of fibre in access network and will interconnect 270 locations by 2011.

✓ The armed forces will release spectrum, the airwaves on which communication signals travel, in a phased manner, depending on the progress of this alternate network.

✓ According to industry sources, out of the amount allocated to the defence network, 6.9% will be used for alternative air force network, 56.6% will be used for building similar facilities for the army and the navy and 36.5% will be used for maintaining this infrastructure for the next 10 years.

If the government is totally committed towards providing a major impetus to the economy and towards development, then it has to deploy significant resources as a percentage of the GDP which would imply a much higher borrowing programme and a higher deficit. As global credit rating agencies are already warning of a likely downgrade of the Indian paper, we believe that the government would not want to increase its fiscal deficit and would instead try to rely on private sector investment and foreign capital flows to compensate for its lack of investment. As the global situation remains subdued and the Indian private sector is unwilling to take risks, it is unlikely that they would provide the boost to the economy.

Automobile

The auto sector had a difficult FY09 in terms of sales volume as well as profitability. Sales volume took a huge hit during 3QFY09. However, since then, the situation has improved for the auto sector. Due to slowdown in the economy, the commercial vehicles sector was the worst hit during FY09. On the back of robust demand from rural India, the two-wheeler segment and the passenger car segment (compact cars) have shown some signs of improvement, but the commercial vehicle (CV) sector continues to face the brunt of the economic slowdown.

Budget expectation

On excise duty: In order to bring about a spurt in the economy, the government brought down the general excise duty rate from 14% to 8% through a couple of stimulus packages since December 2008. Post excise duty cut, the two wheeler-segment and compact car segment has seen revival in sales volume. We think the government would not like to meddle with sales volume recovery in these segments and will therefore maintain "status quo" on the existing excise duty rates. However, if the government plans for partial/complete roll-back on the excise cuts, then it would be negative for the two-wheeler and small car players.

Differential excise duty rates (8%) exist between small cars and large cars (20-22%). Since the sales of large cars are impacted due to economic slowdown, large car manufacturers are hoping for a lowering of excise duty, in line with the excise duty rates on small cars. However, we do not expect the excise duty rates on large cars to be changed because customers of such cars are less sensitive to price changes. Hence, bringing down the excise duty rate may not necessarily increase demand for large cars.

On depreciation: Due to slowdown in the economy, the commercial vehicles sector was the worst hit during FY09. In order to provide a demand push, the government, through its second stimulus package, announced an accelerated depreciation of 50% on commercial vehicles purchased between

January-March 2009. Players in the CV segments are expecting that the accelerated depreciation benefit will be extended beyond March 31, 2009. Due to continuing economic slowdown, the CV sales continue to remain under pressure. Hence, we expect the benefit of accelerated depreciation to be extended beyond March 31, 2009.

Overall, we believe that the budget will be neutral for the auto sector as we do not foresee any direct measures (except for CVs) to be announced which will benefit the auto sector. However, the sector can indirectly benefit from additional farm loan waiver and improved financing scenario.

Banking

Increase in foreign direct investments in insurance sector from present 26% to 49%: We expect the Finance Minister to increase FDI limit in the domestic insurance sector to 49% to facilitate the much-needed fund infusion for future growth.

Expectation of 50-75 bps reduction in government small saving interest rates: We expect the FM to reduce small saving interest rates to provide room to commercial banks to further cut their deposit and lending rates.

Permission to infrastructure sector lenders to issue tax-free bonds: We expect the FM to permit infrastructure lenders likes (PFC, IDFC, etc.) to issue tax-free bonds to increase their resource base. If this is permitted, then infrastructure lenders would benefit but commercial banks would be at a slight disadvantage.

Increase in limit of tax deduction on interest payment on housing loans: We expect that the budget may propose to increase limit of tax deduction on interest payment on housing loans from the present level of Rs0.15 mn to make housing loans more attractive.

Overall, we expect the budget to be positive for the banking industry at large. Considering the sharp run-up in stock prices, we are negatively biased on the Indian banking sector.

Cement

Restoration of excise duty from current 8% to 12%: The government reduced the excise duty from 12% to 8% during the year to stimulate cement demand. However, the industry has increased prices due to strong demand. We believe that the excise duty would be restored at 12% which will negatively impact the industry.

Abatement on excise duty: Currently, the excise duty on cement is based on MRP and the industry gets abatement whenever excise duty is based on MRP. However we don't expect the abatement on excise duty to be given in this budget.

Abolition of import duty on pet-coke and coal: Coal is the major fuel for the production of cement. Currently, there is a 5% import duty on coal and pet coke. We expect the import duty on pet coke to be abolished from 5% to nil. The abolition of import duty would reduce the operational cost for the cement industry.

Subsidy on freight cost on export of cement and clinker: Most plants are in the hinterland which makes exports unviable due to higher freight cost. We believe the industry would be in surplus in H2FY10. Hence, the government may provide the freight subsidy to make exports viable.

We expect the budget to be negative for the sector. However, it would indirectly benefit through increase in allocation for various infrastructure schemes.

Construction

Increased allocation under various infrastructures schemes: We expect the government to increase the allocation under various infrastructure schemes like NHDP, Pradhan Mantri Gram Sadak Yojna (PMGSY), accelerated Irrigation Benefit Programme (AIBP) and Bharat Nirman to drive the economy.

Clarification on section 80IA benefit: There is varying interpretation of section 80IA to claim benefit (currently allowed to developers of projects). We believe section 80IA benefit would be clarified and construction companies would be included under the purview.

Re-introduction of tax benefit u/s 10 (23G): The income of the companies engaged in infrastructure projects by way of debt or equity was exempted from tax under Section 10(23G) which was removed. We believe the exemption would be re-introduced which will bring down the interest cost of the funds for infrastructure companies as lending institutions may pass on the benefit, or otherwise improve the interest in funding for infra projects.

We expect the budget to be positive for the sector.

Fertiliser

Agriculture contributes to around 17% of India's GDP and supports more than 60% of the population. We believe that as the country targets a higher agrarian growth rate, the government will focus on improving the yields per hectare of different crops. This can be done only by increasing investment and reforming the agricultural machinery, finance, irrigation, and fertiliser sectors. Within this space, we believe that the government will encourage investments in the fertiliser sector through regulatory reforms, especially for urea. In the recent past, the government has started taking steps to reform the fertiliser industry. A part of the urea price is linked to the international price parity for de-bottlenecking and brown-field expansion. On the other hand, the government has assured the priority of KG basin gas supply to encourage new green-field capacities with complete pricing power.

We believe that the government will now target long-term issues like regulated pricing, an increasing disparity between costs of production and selling, which are to be compensated through irregular subsidy disbursals. The government tried to resolve this issue through introduction of a new price mechanism based on import price parity (IPP). To resolve these issues, we opine that the government is likely to take further necessary regulatory reforms in the fertiliser sector in budget 2009-10. The policy could look at incentives for greenfield expansion of urea capacities, assured feedstock supply, minimum assured returns on new urea capacities and introduction of full cash payment of subsidies.

Our Expectations:

✓ The government may announce incentives for greenfield expansion for urea capacities.

✓ The government may also announce assured feedstock supply and minimum assured returns on new urea capacities.

✓ Currently, the government disburses subsidy in cash as well as in bonds. In budget 2009-10, the government may introduce full cash payment of subsidies.

We expect the budget to be positive for the sector. Our top pick is Tata Chemicals.

Infrastructure

Infrastructure spending has been the focus of government spending to mitigate the impact of the economic slowdown. We believe that the budget will outline favourable policies and spending for infrastructure development, both at private and at public level.

Higher budgetary allocation in infrastructure development schemes: We expect the budget to be positive for the infrastructure sector with higher budgetary allocation to propel domestic growth with job creation. We expect higher fund allocation to various infrastructural development schemes like National Rural Employment Guarantee Scheme (NREGS), Bharat Nirman Phase II, Jawaharlal Nehru National Urban Renewal Mission (JNNURM), Accelerated Irrigation Benefit Programme (AIBP), National Highway Development Programme (NHDP), and Pradhan Mantri Gram Sadak Yojana. The government used schemes like NREGS as a trump card in the elections. Hence, higher budgetary allocation to these schemes is expected in the budget.

Road development to get a new face with higher allocation: We expect higher allocation for the road and transport sector. The road and transport ministry is targeting a four-fold increase in highway construction to 20 km per day, which needs significantly higher allocation to meet its target. During 2008-09, the allocation for National Highways Development Project (NHDP) was enhanced to Rs12,966 crore and it could go up further in this budget. Furthermore, the government may consider setting up a road finance corporation, in line with the proposal of Mr. Kamal Nath, which would be for easy financing of large-scale road projects.

Steps to ease out infrastructure funding: The most critical challenge for the government for the next five years would be to streamline the dedicated funds from the government exchequer to the infrastructure players. Major problem faced by these infrastructure companies is financial closure, which has become chronic during turbulent times like these. We believe that the government would initiate steps to remove financing bottlenecks so that critical infrastructure projects go through smoothly on schedule.

Setup monitoring units: Considering the importance of infrastructure execution and its multiplier effect on the domestic economic machinery, we believe that the government will consider a proposal to set up an integrated monitoring unit which will track execution progress and fund flow of infrastructure projects.

Social infrastructure focus to continue: Investment in social infrastructure like education and health should continue to get focus. We expect continued allocation and steps for public-private partnerships to fuel infrastructure improvement in these areas.

We expect the budget to be positive for the infrastructure sector. We believe companies with execution expertise and high borrowing capacity would benefit in the coming days. *Key beneficiaries could be NCC, IVRCL, Madhucon Projects, Gammon, and Simplex Infrastructure.*

Metal

Reversal of excise duty on steel from 8% to 12% would be negative for the sector as companies may not be able to pass through the entire hike in duty to the end-customer. This would impact their margins.

We also expect a hike in import duty on steel from 5% to 15% to safeguard domestic producers from cheap imports. This would benefit primary steel producers.

Clarity regarding the government's divestment plans would also speed up the capacity expansion plans of domestic players as it would enable quicker access to capital.

Implementation of the National mineral policy (NMP) recommendations should give a boost to the mining sector. It would speed up exploration as well as the lag between successful prospecting and the start of mining.

We expect the budget impact to be largely neutral.

Multiplex

Rationalization of E-Tax: Entertainment tax being a state subject varies across different states. The range is wide with E-Tax being 20% of the net ticket revenue in some states like Andhra Pradesh to being 100% of the net ticket revenue in others like Gujarat and Assam. We expect the government to push for the uniformity of entertainment tax across states. The government may propose a narrower range of say 10-30% within which the states can fix their respective E-tax rates. In other countries it is attached to VAT (Value Added Tax). As the entertainment industry in India is one of the highly taxed in the world (attracting service tax, VAT and stamp duty at various points), we believe that reduction of entertainment tax will aid in the uniform growth and penetration of the entertainment industry across the country.

Removal of service tax on rentals paid on immovable property: The Delhi High Court, in a recent landmark judgement, called for removal of service tax on lease rentals from immovable property by declaring it ultra-vires to the provisions of 'The Finance Act 1994'. We had been expecting this since Budget 2008 as we believe that leasing should not come under the service tax gamut. We expect the government to reiterate the same.

Top Picks: PVR, Inox, Cinemax, Fame

Oil & Gas

Extension of income tax holiday on gas production: This will benefit RIL and other companies like ONGC and GSPC, which would start producing gas from the NELP blocks in the next few years.

De-regulation of petro-product prices (partial/ complete) and transparency in subsidy sharing: The move would be beneficial to PSUs like ONGC, GAIL, IOC, BPCL and HPCL and the extent of deregulation or transparency would be the chief matter to watch out for.

Increase in duties on crude and petro-products: OMCs might be negatively impacted if the higher duties are not passed on to end consumers through retail price hikes of auto fuels. However, refiners (including independent refiners like CPCL, MRPL) could be negatively impacted only if the duties on crude oil are increased /restored while the duties on petro-products are left untouched, and, therefore, the duty protection available to refiners is taken away. In such a case, while the marketing division of the OMCs might not lose, refining margins would suffer.

Extension of "infrastructure status" to avail of a ten-year tax holiday: Refiners impacted positively, E&P marginally.

Infrastructure status would help the refiners: Although RIL, Essar Oil, IOC, BPCL and HPCL will be impacted positively, the others in the E&P domain will only be benefitted to the extent of a seven-year tax holiday being extended to ten years.

Cess on auto-fuels for road development: IOC, BPCL and HPCL might be negatively impacted if the higher cess is not passed on to end consumers.

We expect the budget impact to be largely neutral.

Paper

The current global meltdown has made the Asian paper market very vulnerable to a demand slowdown. To protect the paper industry, the government decreased the excise duty on paper and paper boards from 8% to 4% in the first stimulus package announced on December 7, 2008. The companies passed the entire benefits to consumers which led to an increase in paper demand. On the global supply front, there have been concerns that major players in Indonesia and China are all set to push large quantities of coated and wood-free grades of paper into the Indian paper market. We expect a pre-emptive dumping of cheap finished goods in the market, and the government is likely to increase the customs duty on paper/paperboards to protect the rise in supply from Indonesia and China.

Our Expectations:

1. The government may increase the peak rate of basic customs duty from the current level of 10% to 15% on paper/ paperboards to protect from increasing supply from Indonesia and China.
2. We expect that the government may maintain the excise duty at 4% in the medium term.
3. During budget 2008-09, budget allocation for schemes like Sarva Shikha Abhiyan and secondary education increased by 22.8% and 20% to Rs131 bn and Rs45.5 bn, respectively, over 2007-08. During budget 2009-10, we expect that the government is likely to improve the budget allocation for schemes like Sarva Shikha Abhiyan and secondary education. The higher budget allocation would boost the demand of printing and writing paper.

We expect the budget to be positive for the sector. Our top pick is Tamil Nadu Newsprints & Paper

Pharmaceutical

✓ Extension on the weighted deduction of 150% on in-house research and 125% on research outsourced to a third party for another five years from 2012.

✓ A 4% excise duty on finished dosage and 8% excise duty on Active Pharmaceutical Ingredient should continue at current levels.

✓ Grants will be linked to specific activities such as discovery, regulatory, safety and toxicity studies and clinical trials.

✓ Outlay on healthcare is likely to be increased from 0.9% to 2%.

✓ Customs duty on all life saving drugs such as antibiotics, anti-cancer and HIV should be exempted.

Extension of EOU benefits for another 3 years.

Power

We believe government would take broader steps to encourage private participation in the sector in line with the PPP (Public Private Partnership) model.

Benefits under Section 80 IA of Income Tax Act 1961 to be extended: The benefits under section 80 IA are also available to undertakings, which are engaged in generation, transmission or distribution of power, albeit in a restricted manner. Now, due to restrictive wording of the provisions, the benefits are available only to power generation, transmission and distribution companies and not to the turnkey contractors, who supply, operate or maintain the equipments. We believe that such benefit extension would initiate a surge in activity in the power sector—as seen in other infrastructure projects.

Power funding under priority lending and special dispensation for UMPP funding: Power companies, like any other infrastructure player, are facing a financing crunch. We believe that despite the government's best possible efforts over the years to provide ample financing stimulus to the power sector, a lot is still to be done. We believe that power companies may qualify for banks' priority sector lending. We further believe that such a step would have a far-reaching effect as priority sector lending norms suggest 40% disbursement for agriculture, exports and SME (small and medium enterprises). Apart from this, we also believe that the ceiling on power sector lending by banks should be increased from the present rate to boost the sector. Industry is asking for an increase in the exposure limit of capital funds of banks—from 20% to 50% for a single borrower and from 30% to 70% for group borrowers. However, we believe that the ceiling relaxation may not be on RBI's cards as of now. We strongly believe that focus this year would be primarily on development of new alternate financing resources on the lines of the corporate bond market. Considering the size and difficulty of fund requirement, the government may provide a special dispensation for ultra-mega power projects (UMPPs).

Reform programs/schemes should continue to get focus: We expect the government to continue to focus on reform schemes like APDRP projects (Accelerated Power Development and Reform Program) and RGGVY (The Rajiv Gandhi Gramin Vidyutikaran Yojana). This move will increase investments in T&D and rural electrification, thus benefiting T&D companies, including Kalpataru Power, Jyoti Structures, KEC International, EMCO, ABB, among others.

Recommendation: We expect the budget to be moderately positive for the power sector. We believe companies who win UMPP would be the biggest beneficiaries in generation capacities.

Our top pick for the transmission sector is Kalpataru Power.

Real Estate

Resume tax exemption under section 80 IB (10) to promote mass housing: Section 80 IB (10) of the Income Tax Act 1961 gives tax relief to builders who construct units with less than 1,000 square feet of built-up space in metros of Delhi and Mumbai and a maximum of 1,500 sq ft elsewhere. However, the benefits under this section have been stalled since 2007. The real estate sector has been battered in the last one year as the developers faced huge cash flow problems and the consumers were in a wait-and-watch mode as they expected the prices to correct. We expect that the government could resume the tax benefit under Section 80 IB (10) to encourage builders to build affordable mass housing within and outside the metros in order to increase the real estate off-take and help the dependent industries to manage the business downturn.

Increase the tenure of tax holiday to hotels under section 80ID: We expect the government to increase the tenure of the tax holiday available to hotels under section 80ID to 10 years from the existing time limit of five years. The gestation period in the hotel industry stretches from 4 years to 5 years. This will not only encourage the developers to build quality hotels across various classes but will also give a fillip to India's tourism industry.

Increase the exemption limit of home loan interest payable under section 24 (b): This section deals with exemption on interest payable by home loan buyers for self-occupied houses. Currently, the exemption stands to the extent of Rs1,50,000. We expect that the government could extend this to at least Rs3,00,000. This will not only help the middle class home buyers to pay for their existing home loans but also encourage first-time homebuyers.

Service tax provisions relating to real estate: It has been clarified that no service tax should be levied in case of pre-construction sale of residential complex where the seller and the buyer enter into an 'agreement to sell'. We expect that a similar clarification can be issued for pre-construction sale of commercial complexes as well.

The Delhi High Court, in a recent landmark judgement, called for the removal of service tax on lease rentals from immovable property by declaring it ultra vires to the provisions of 'The Finance Act 1994'. We had been expecting this since Budget 2008 as we believe that leasing should not come under the service tax gamut.

The imposition of service tax on lease rentals impacts the commercial real estate business as it (1) increases the commercial real estate prices; and (2) reduces rental yield of developers from commercial properties.

Now, with the High Court passing this judgement, we expect the government to reiterate the same.

Clarifications on REMFs and on setting up of REITs including tax treatment: We believe the government may clarify on the treatment of REMFs in line with equity oriented mutual funds. Also, the government may address about the possible introduction of REITs in India. We believe that as and when it happens, it will be positive for the real estate sector as it will bring in more liquidity into the market and help in easier absorption of developers' properties and also create a healthy secondary market for real estate assets. Moreover it will be a less risky and safer opportunity for retail investors to invest in the real estate sector. SEBI has already issued its draft guidelines on the setting up of REITs last year, but was silent on the tax treatment of the income from REITs.

Lower and uniform stamp duty rates: The stamp duty rates are one of the highest in India; with as high as 14-15% in some of the states. If we compare this to 1-2% stamp duty in countries like Singapore, we believe that there is a vast scope of cutting the stamp duty rates. We believe that it will be a positive step for the government, investors and for the market, as we think it may increase the overall stamp duty revenue for the government, reduce tax evasion to a great extent, and help make the market more transparent.

We can see a short-term upside in realty stocks if any of the above expectations is met in the budget. However, we believe that any decisive upside has to be backed by a significant revival in the property sales, which we believe, may not happen in the short term.

Shipping

The UPA government has split the Surface Transport Ministry into two separate ministries, viz., Road Transport and Shipping.

Domestic fund availability: Creation of Shipping Finance Corp as a separate financing arm to meet the requirement of domestic shipping companies. Creation of a ship acquisition fund for availability of long-term finance in the wake of the current global recession.

Tax restructuring: Indian shipping companies are paying around twelve different taxes like seafarers taxation, withholding tax on charter charges paid to foreign ship owner, interest paid to foreign players, service tax, etc. The cumulative effect of these taxes leads to a cost disadvantage of ~4% to 5% as compared to foreign ship-owners. The restructuring of these taxes is expected to have a positive impact on the industry.

Tonnage tax benefit on interest income: Tonnage tax benefits should be allowed for interest income on tonnage tax reserve. The companies are paying corporate tax on the interest income of tonnage tax reserve (shipping companies keep 20% of profits as tonnage tax reserve for fleet acquisition).

Tax exemption on income on sale of ship: Shipping companies are paying as per Minimum Alternative Tax (MAT) on profits earned from sale of ships. In almost all the major maritime countries such as the Netherlands, Belgium, Singapore, Spain and Ireland, profit or loss on second hand ships is part of tonnage tax regime.

Shipbuilding subsidy: The shipbuilding industry should be given an infrastructure status or extension of 30% subsidy scheme with retrospective effect which ended on August 2007. Any announcement on fringe benefit tax (FBT), service tax and Minimum Alternate Tax (MAT) are likely to impact the shipping sector (shipping companies that avail ship management services from brokers and the profit of sale of ship comes under the MAT provision).

We expect the budget to be positive for the shipping sector.

Sugar

The government has already taken some steps to control increase in domestic sugar prices due to supply shortage. It has removed the 60% import duty on raw and white sugar in June 2009 until the end of the sugar season, i.e., September 2009. The government has also removed a re-export obligation to export similar quantity (with adjustment of process loss of 5%) within 24 months, for duty-free import of raw sugar allowed under the advance licensing scheme. The sugar importers will continue to pay countervailing duty (CVD) of Rs850 a tonne.

We do not expect major announcement for the sugar sector. Sugar mills are not keen on ethanol blending and demand "Declared Goods" status for ethanol, considering higher realisation on other distillery products (~Rs 30 per litre) as compared to the fixed price for ethanol at Rs21.5 per litre. Following are expectations from the budget 2009-10.

✓ We expect excise duty to remain at current levels for Levy and Free sale sugar. (Note: Current Levy Sugar percentage is 10%)

Rs Per MT	Basic	Additional	Cess	Total
Levy Sugar	380	0	140	520
Free sale	710	0	140	850

✓ To lower excise duty on molasses from Rs750 per MT to Rs500 per MT or may be levied at 8% 'ad valorem'.

✓ Expectation of 80% depreciation benefit on plant and machinery for ethanol manufacturing to be at par with other renewable energy equipments.

✓ De-control of sugar by freeing the industry from the obligation to supply levy sugar (at price below the cost of production) and from release mechanism.

✓ Incentives and tax holidays on cost (i.e., weighted deduction of 150%) incurred by sugar factories on constructing roads in rural areas.

We expect the budget to be neutral for the sugar sector.

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