Budget Analysis

No Major Positive Takeaways

The budget has fell short of most of our expectations. The increase in excise duty and service tax is likely to add to inflationary pressures as industry is likely to pass the increase in cost. This is a major negative for the economy as it would likely to hamper growth going ahead. Fiscal deficit target of 5.1% for FY13 seems to be optimistic considering the fact that the government's subsidy provision is likely to be inadequate. Infusion of Rs 158.88 bn for capitalization of public sector banks and financial institutions to attain minimum 8% tier I capacity by 31st March 2013 would help the public sector banks but however raising the agricultural credit target to Rs 5,750 bn will strain the PSU bank finances as it could increase the NPA levels. There were some positive takeaways for sectors like Power while broadly it has been neutral to negative for most industries.

Key budget highlights

- India's GDP for FY13 expected to grow by 7.6% (plus or minus 0.25%).
- Fiscal deficit target for FY13 seen at 5.1% of GDP, as against 5.9% in revised estimates for 2011-12.
- Fuel subsidy is estimated at Rs 436 bn in FY13 vs Rs 685 bn FY12. If fuel prices are not increased in FY13, then the estimated fuel subsidy may rise sharply, thus adversely impacting the fiscal deficit targets of the government.
- Agricultural credit target is raised to Rs 5,750 bn in FY13 as compared to Rs 4,750 bn in FY12.
- Gross expenditure for 2012-13 is budgeted 18% higher than 2011-12 at Rs 14,909 bn (planned expenditure at Rs 5,210 bn; non plan expenditure at Rs 9,699 bn).
- Investment in infrastructure to go up to Rs 50,000 bn during the 12th Plan period, of which half is expected to be met from private sector.
- Tax Free Bonds of Rs 600 bn to be allowed for financial infrastructure projects.
- Allocation of Road Transport and Highways Ministry enhanced by 14% to Rs 253 bn.
- Standard rate of excise duty proposed to be raised from 10% to 12%; service tax rates raised from 10% to 12%.
- No time-line given on implementation of Direct tax code (DTC) and Goods and Service tax (GST).
- Income tax exemption limit for individual is proposed to be raised from Rs 1.8 lakh to Rs 2 lakh.
- Interest from savings bank accounts deductible up to Rs 10,000; deduction of up to Rs 5,000 for preventive health check-up.
- Securities transaction tax (STT) on cash delivery reduced by 25% to 0.1%.
- Tax free bonds worth Rs 600 bn allowed for financing infrastructure projects in FY13 as compared to Rs 300 bn in FY12.

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- Based on recommendation of task force headed by Mr. Nandan Nilekani, a mobile-based Fertilizer Management System has been designed to provide end to end information on movement of fertilizers and subsidies.
- Divestment target for FY13 is set at Rs 300 bn.
- Efforts to reach broad based consensus on FDI in multi-brand retail.
- Rajiv Gandhi Equity Saving Scheme: to allow income tax deduction to retail investors on investing in equities upto Rs. 50,000.
- Government would infuse Rs 158 bn for capitalization of public sector banks and financial institutions to attain minimum 8% tier I capacity by 31st March 2013.
- Planned outlay for Department of Agriculture and Co-operation increased by 18%. Outlay for Rashtriya Krishi Vikas Yojana (RKVY) increased to Rs 92 bn; Outlay for Bringing Green Revolution to Eastern India (BGREI) increased to Rs 10 bn in FY13 as compared to Rs 4 bn in FY12; Rs 22 bn project to improve dairy productivity; Rs 5 bn for coastal aquaculture.
- Interest subvention for short-term crop loans to farmers at 7% interest continues; additional 3% for prompt paying farmers.
- Rs 2 bn for awards to incentivize agricultural research.
- Interest subvention of 1% on housing loans up to Rs 1.5 mn extended for one more year.
- UID-Aadhar to get adequate funds for enrolment of 400 mn persons, in addition to the 200 mn persons already enrolled.
- In order to widen the tax base vis-à-vis profit linked deductions, it is proposed to amend provisions regarding Alternate Minimum Tax (AMT) contained in Chapter XII-BA in the Income-tax Act to provide that a person other than a company, who has claimed deduction under any section (other than section 80P) included in Chapter VI-A under the heading "C - Deductions in respect of certain incomes" or under section 10AA, shall be liable to pay AMT. (discussed in detail at the end).
- Propose to retrospectively amend the Income Tax Act, 1961, that could make cross border M&A transaction liable to be taxed.

Automobiles

Excise duty hiked on Automobiles

Category	Criteria	Feb-07 Union Budget 2007	Feb-08 Union Budget 2008	Dec-08 Fiscal Stimulus Package Phase 1	Feb-09 Fiscal Stimulus Package Phase 3	Jul-09 Union Budget 2009	Feb-10 Union Budget 2010	Feb-11 Union Budget 2011	Mar-12 Union Budget 2012
Two Wheelers		16%	12%	8%	8%	8%	10%	10%	**12%**
Small Cars (Upto 4m-Petrol/Diesel)		16%	12%	8%	8%	8%	10%	10%	**12%**
Sedans ((Above 4m-Petrol/Diesel)	Upto 1500cc	24%	24%	20%	20%	20%	22%	22%	**22%**
	Above 1500cc							22%	**27%**
UVs	Upto 1500cc	24%	24%	20%	20%	20%	22%	22%	**24%**
	Above 1500cc							22%	**27%**
MHCVs,LCVs,3 Wheelers									
Goods Carriers		16%	14%	10%	8%	8%	10%	10%	**12%**
Passenger Carriers		16%	12%	8%	8%	8%	10%	10%	**12%**
Three Wheelers		16%	12%	8%	8%	8%	10%	10%	**12%**
LCVs- Buses		16%	12%	8%	8%	8%	10%	10%	**12%**
LCVs- Trucks		16%	14%	10%	10%	8%	10%	10%	**12%**
CVs- Trucks		16%	14%	10%	8%	8%	10%	10%	**12%**
CVs- Buses		16%	12%	8%	8%	8%	10%	10%	**12%**
Specific Duty									
Category		Engine Capacity		June 2008		Budget 2009			
Sedans & UVs (Above 4m-Petrol)		>1200cc		Rs 15,000	Rs 15,000	Rs 15,000	Rs 15,000	Rs 15,000	**Rs 15,000**
Sedans / UVs (Above 4m-Diesel)		>1500cc		Rs 20,000	Rs 20,000	Rs 20,000	Rs 20,000	Rs 20,000	**Rs 20,000**

- Excise duty was hiked across the board by 200 bps for automobiles.
  Impact: -Ve for the Auto industry.

- Excise duty on large cars (above 4m in length and engine displacement of above 1500cc) hiked by 500bps to 27%.
  Impact: MSIL's 20%, TML's 26% and M&M's 94% fall in the category of passenger cars/UVs/ Vans having a length of >4mts and engine capacity above 1500cc. On the face of it, it's the most negative for M&M. But the stock was beaten down over the past month as expectations were built in for additional duty of upto Rs 80,000 on diesel passenger vehicles which didn't come through. So this led to the positive uptick in the stock price.
  -Ve for M&M, MSIL and TML

- Import duty on fully built cars increased from 60% to 75%.

  Impact: There are no major imports by listed Indian companies. But TML imports some 1200 units per month of JLR cars while M&M would be importing Ssangyong Motor products in due course.
  -Ve for TML

Cement

- The budget has proposed unified rate of 12% + Rs 120 per tonne for non-mini cement plants and 6% + Rs 120 per tonne for mini-cement plants. It is proposed to charge this duty on the Retail Sale Price less abatement of 30%. *(Currently the industry is charged differential rate of tax of 10% ad-valorem + Rs 80 per tonne (retail sale price declared, not exceeding Rs 190 per bag of 50 kg or Rs 3800 per tonne of cement), 10% ad-valorem + Rs 160 per tonne (retail sale price declared exceeding Rs 190 per bag of 50 kg or Rs 3800 per tonne of cement) and 10% ad-valorem for packed cement for industrial & institutional consumers & other than packed cement, i.e. loose cement and clinker.)*
- The budget has proposed for full exemption from basic customs duty of 5% and a concessional CVD of 1% to imported thermal coal and LNG till 31st March, 2014.
- Many other allocations and stimulus for various infrastructure sectors and social programmes will indirectly help the industry.
- The budget was silent on the exemption of customs duty for pet coke and gypsum.
- Neutral **for the cement industry in general.**
- Although the increase in excise duty for the industry is a negative, we believe that the abatement of 30% on the retail sale price would result in lower effective excise duty. Either way the industry is in a very healthy position to pass on the hike in cost.
- The exemption of customs duty on imported coal is mildly **+Ve** for **UltraTech and India Cement**

Information Technology

- The Government has sanctioned Rs 140 bn for the UIDAI project. This budget amount will help enrollments of about 400mn Indian residents by June 2013. UIDAI has completed about 200 mn enrollments with 140mn Aadhaar numbers have been issued till date.

  The finance minister also approved the 'IT strategy' proposed by Nandan Nilekani for direct transfer of subsidy into bank accounts of beneficiaries. Mobile based fertilizer subsidy and new public distribution systems are expected to help IT cos in bagging Government contracts.

  Impact: Software solutions for UIDAI's biometrics service, Implementation of IT backbone would lead to more contracts for IT firms. It may be noted that HCL Infosytems recently bagged a Rs 2.2bn order for implementation of IT backbone for the Aadhaar contract.

  +Ve for TCS, HCL infosystems, Mindtree

- The weighted deduction of 200% for R&D expenditure done in an in-house facility which was set to expire on March 31, 2012 is extended for five more years. This extension was inline with our and industry expectations and would continue to incentivize the industry to spend money on R&D activities.

  Impact: The IT product companies and companies which invest in R&D would benefit.

  +Ve for TCS, Infosys, Oracle financial services, Persistent Systems, Polaris, Financial technologies

Oil and Gas

- **Basic customs duty on Liquefied Natural Gas (LNG) and Natural Gas (NG) is being fully exempted**
  In the budget, the government slashed the custom duty on natural gas/ LNG from 5% to 0% in line with the expectations; however, the budget did not address the declared good status for natural gas/ LNG. Nonetheless, we believe the decrease in the custom duty of LNG to NIL would further increase the cost competitiveness of LNG vis-a-vis other fuels used for city gas distribution (CGD) and industrial purposes, thus, will give fillip to LNG demand in India. We believe this is **+Ve** for **PLNG, GAIL, IGL, GSPL, Gujarat gas.**

- **The rate of cess levied on indigenous crude under is increased 80% to Rs. 4,500 per tonne:**
  The government increased the cess on domestic crude oil from Rs. 2,500 per tonne to Rs. 4,500 per tonne which came in as a negative surprise for the sector. The increase in the cess will increase the statutory levies of the upstream oil producers. We believe this would be **-Ve** for **ONGC, OIL India** and **CAIRN India**. We estimate ONGC EPS to come down, ceteris paribus, by 11% for FY13E.

- **For FY12 the Government increased the oil subsidy provision to Rs. 650 bn**
  On account of the higher than estimated crude oil prices, the government revised the oil subsidy upwards to Rs. 650 bn which is inclusive of the last reimbursement of Rs. 200 bn that the government paid for the FY11 subsidy in the current fiscal year. For 9M, the oil marketing companies (OMCs) have incurred under recoveries of Rs. 973 bn on selling diesel, kerosene and LPG at subsidized rate. Of the total under recovery of Rs. 973 bn, the government provided Rs. 450 bn (46% of the gross under recoveries) to support the OMCs, while the upstream oil companies shared Rs. 369 bn (38% of the gross of under recoveries). The government has made oil subsidy provision of Rs. 400 bn for FY13E. We believe the substantial part of the subsidy provision is likely to be the last reimbursement by the government for the FY12 subsidy burden but paid in FY13. With current crude oil hovering around $125 per barrel, the under recoveries of the sector without any fuel prices hike would reach unsustainable proportions and thus has become imperative to hike fuel prices which would be **+Ve** for upstream oil companies **(ONGC, OIL India** and **GAIL)** and OMCs **(IOC, BPCL & HPCL)**.

- **Subsidy in cash and not as bonds while direct transfer of cash subsidy considered:**
  Government continued its earlier practice of issuing subsidy to the oil marketing companies (OMCs) in cash and not by issuing bonds. Also, the recommendation of the Task Force on direct transfer of cash subsidy for PDS kerosene and LPG has been given in principal approval. We believe this is **+Ve** for **OMCs**.

Pharma

- The weighted deduction of 200% for R&D expenditure done in an in-house facility which was set to expire on March 31, 2012 is extended for five more years. This extension was inline with our and industry expectations and would continue to incentivize the industry to spend money on R&D activities. **+Ve** for core R&D players like **SPARC, Biocon, Sun Pharma, Lupin, Wockhardt, Glenmark** and **Ranbaxy.**

- **The introduction of the AMT will impact the pharma sector as a whole.** Companies which are making profit and paying tax lower than MAT of 18.5% will now have to pay the minimum tax. The tax outgo for the companies will increase. **-Ve** for **SUN Pharma, Cadila Healthcare.**

- It is proposed to allow a deduction up to Rs5,000 for preventive health check-up for Individual. This is **+Ve** for **Fortis Healthcare, Apollo Hospital.**

- It is proposed to extend concessional basic customs duty of 5% with full exemption from excise duty/CVD to six specified life-saving drugs/ vaccines. These are used for the treatment or prevention of ailments such as HIV-AIDS, renal cancer, etc. **+Ve** for **Cipla, Natco.**

Other Positive highlights for the sector are

- It is proposed to reduce basic customs duty on Soya protein concentrate and isolated soya protein from 30% or 15% respectively to 10%. Simultaneously, excise duty on all processed soya food products is being reduced to the merit rate of 6%.

- It is proposed to provide a concessional basic customs duty of 2.5% along with reduced excise duty of 6% on iodine.

- Probiotics are a cost-effective means of combating bacterial infections. It is proposed to reduce the basic customs duty on this item from 10% to 5%.

- It is proposed to increase the allocation to National Rural Health Mission (NRHM) from Rs181 bn in 2011-12 to Rs208 bn in 2012-13.

FMCG

- Excise duty increased to 12% . **-Ve** for consumer companies like **HUL, GSK & Pidilite.**

- Increase basic excise duty on cigarettes of more than 65mm length by adding an *advalorem* component of 10% to the existing specific rates. **Neutral** on **ITC**.

Power & Power Equipments

- External Commercial Borrowings (ECB) to be allowed to part finance Rupee debt of existing power projects.
- The budget has proposed for full exemption of basic customs duty of 5% and a concessional CVD of 1% to imported thermal coal and LNG till 31st March, 2014.
- Full exemption from basic duty proposed for certain fuels for power generation and full exemption from basic customs duty to coal mining project import is also proposed.
- Extension of sunset clause under section 80 IA tax benefits until Mar-13.
- Withholding tax on ECB reduced from 20% to 5%.
- +Ve for **Adani Power, Lanco Infra, Tata Power.**

Our View

Allowing External Commercial Borrowings (ECB) to part finance Rupee debt of existing power projects and the proposed full exemption from basic customs duty of 5% and a concessional CVD of 1% to steam coal and LNG till 31st March, 2014 is a major positive for the entire power industry. However the budget was completely silent on the proposal of imposing 19% (5% basis, 10% CVD and 4% SCVD) duty to be levied on power plant equipments for mega projects. This is a disappointment for the power equipment manufacturers.

Telecom

- Budget proposes viability gap funding for telecom tower and fixed line assets
- +Ve for **Bharti Airtel and Idea Cellular**
- No major announcement was announced in the budget. However viability gap funding for telecom tower and fixed line assets will help Bharti Airtel and Idea Cellular.

Metals and Mining

- Overall there weren't any major announcements for the metal sector. However, the removal of customs duty of 5% on steam coal and the exemption of basic customs duty to coal mining project imports are some of the positives for the metals and mining sector.

Banking

- Agricultural credit target has been raised to Rs 5,750 bn in FY13 as compared to Rs 4,750 bn in FY12.
  Impact : -Ve for PSU banks
- High borrowing programme of the government is expected to keep the interest rates under pressure.
  Impact : -Ve for the banking sector
- Public sector bank capitalisation of Rs 158.9 bn to ensure 8% Tier 1 CAR by March 2013.
  Impact : +Ve for PSU banks

Infrastructure

- It has proposed to allow tax free bonds from Rs.300bn to Rs.600bn- Positive for infra sector.

Major Negative Takeaways

- **Widening of Tax Base -** ***Alternate Minimum Tax (AMT) on all persons other than companies***

  Under the existing provisions of the Income-tax Act, Minimum Alternate Tax (MAT) and Alternate Minimum Tax (AMT) are levied on companies and limited liability partnerships (LLPs) respectively. However, no such tax is levied on the other form of business organisations such as partnership firms, sole proprietorship, association of persons, etc.

  In order to widen the tax base vis-à-vis profit linked deductions, it is proposed to amend provisions regarding AMT contained in Chapter XII-BA in the Income-tax Act to provide that a person other than a company, who has claimed deduction under any section (other than section 80P) included in Chapter VI-A under the heading "C - Deductions in respect of certain incomes" or under section 10AA, shall be liable to pay AMT.

  Analysis

  We believe introduction of AMT (Alternate Minimum Tax) will impact the companies which are paying tax lower than MAT (i.e. 18.5%). AMT will force companies to pay a minimum tax of 18.5% (i.e. MAT) which will be irrespective of the deduction available to the companies (For eg. Deduction in case of manufacturing facilities in backward areas). At present the companies avoid tax by forming a partnership company within the parent company and the manufacturing facility is established as per provisions under partnership firm to avoid tax as there was no MAT for partnership firm until now, but now with the introduction of AMT they have to pay a minimum tax of 18.5%. This introduction of AMT will largely impact companies who avoid taxes by taking the partnership route.

- **Propose to retrospectively amend the Income Tax Act, 1961, that could make cross border M&A transaction liable to be taxed.**

  The major negative takeaway from the budget is the retrospective amendment to the Income Tax Act, 1961, that could make transactions such as the USD 11.08 bn Vodafone-Hutchison deal liable to tax. The provision was revealed in the Union budget on Friday although it wasn't mentioned by Finance Minister Pranab Mukherjee in his budget speech.

  The government's amendment includes explanations which clarify that the law inherently empowered the tax authority to tax such cross-border deals. "For the removal of doubts, it is hereby clarified that an asset or a capital asset being any share or interest in a company or entity registered or incorporated outside India shall be deemed to be and shall always be deemed to have been situated in India, if the share or interest derives, directly or indirectly, its value substantially from the assets located in India," reads one of the explanations inserted into the Income Tax Act. The retrospective amendment is a major negative. Much clarity on the same is awaited.

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