



Budget Impact

Union Budget 2006-07

Presented in this report is the impact of the recent Budgetary announcements on the companies covered by us in our report "Investments Ideas for 2006". We have employed a "broad-brush" approach for the same, as the impact of many of these changes cannot be precisely quantified at this stage.

Textiles

Textiles is one of the few industries, which enjoyed prominence in the Union Budget 2006-07 presented today. The positive initiatives for the industry has accentuated, as witnessed in the favourable budgetary policies for the fourth time in a row. We list down the key budgetary highlights for the textile sector.

Highlights:

Indirect Taxes - Reduction of Custom & Excise Duties

Products	Excise Duty		Custom Duty	
	2005-06	2006-07	2005-06	2006-07
PX	16.0%	16.0%	5.0%	2.0%
PTA/MEG/DMT	16.0%	16.0%	15.0%	10.0%
MMF Fibres - PSF, ASF, VSF	16.0%	8.0%	15.0%	10.0%
Cotton Yarn	4.0%	4.0%	15.0%	12.5%
Filament Yarn	16.0%	8.0%	15.0%	10.0%
Spun Yarn & DTY	8.0%	8.0%	15.0%	10.0%
Fabric - Cotton	4.0%	4.0%	15.0%	12.5%
Fabric - Polyester	8.0%	8.0%	15.0%	12.5%
Garments - Cotton	4.0%	4.0%	15.0%	12.5%
Garments - Polyester	8.0%	8.0%	15.0%	12.5%

1.Reduction of excise duty on all man-made fibre yarn and filament yarn from 16 per cent to 8 per cent:

While the inverted duty structure for the Spun Yarn & DTY stands corrected, fibre & filament yarn now get exposed to an inverted duty structure. The duty reduction would cause the companies lower their product prices and increase its competitiveness and augment revenues. User industries (fabric) will definitely benefit on account of lower yarn costs. **Positive for Sangam India, Indo Rama Synthetics, Century Enka, Garden Silk Mills, Banswara Synthetics, Raj Rayon, JBF, Alok, Siyaram, Donear, etc.**

2.Import duty on all man-made fibres and yarns from 15 per cent to 10 per cent:

Lower import duty exposes the players to competition from cheaper imports. At least the final product prices would remain under check. **Negative for Indo Rama Synthetics, Century Enka, Garden Silk Mills, JBF, etc. Yarn exporters like Banswara, Sutlej,**

etc may benefit. User industries, mainly fabric companies like Siyaram, Donear, S Kumar Nationwide, Raymond, etc. will benefit.

3.Import duty on raw materials such as DMT, PTA and MEG from 15 per cent to 10 per cent; Import duty on Paraxylene reduced to 2%:

Lower raw material prices will help the polyester companies significantly. Margins should see a distinct improvement on account of this. **Positive for Indo Rama Synthetics, etc.** Neutral for Bombay Dyeing as the negative impact of lower custom duty on final product, DMT (cheap import) would to an extent will get compensated by lower raw material prices (Paraxylene). For Reliance the benefit of lower excise duty final product prices (PFY) would to an extent will get negated by the reduced custom duty on PTA. **Lower duty on MEG bodes negatively for IPCL.**

4.Reduction in peak Custom Duty from 15% to 12.5%:

This will impact segments like Textile Machinery, Cotton Yarn, all Fabrics & all Garments. Lower custom duty at 12.5% will encourage imports of machineries & auger well for the textile players. The reduction in the custom duty on cotton yarn will strengthen the export opportunity & ergo help neutralise the negative impact of the increasing competitiveness of synthetics; Fabric players on an overall are a big beneficiary of the benign yarn prices after the indirect tax rate changes. Lowering of custom duty on Fabrics will auger well for the exporters, while the domestically focused unbranded players could see some increased inflow of the Chinese products, mainly in the synthetics types. Garmenters should benefit on account of the lower custom duty as their competitiveness will further increase as against the competitive nations. Overall benign raw material prices should help improve the operating margins for garment exporters. **Slightly negative outlook for textile machinery companies like Lakshmi Machine Works & Veejay Lakshmi Engineering & also for cotton yarn players like Nahar Group; Positive for Banswara, Bombay Rayon, Gokaldas, Celebrity Fashions.**

Technology Upgradation Fund (TUF) allocation enhanced from Rs.435 Crs. to Rs.535 Crs. - The aforesaid 5% subsidy scheme has been instrumental in the revival of the textile industry in the

recent times. A number of industry representatives were looking at some announcement to extend the TUF scheme beyond March 2007, considering the fact that the Indian textile industry is still at the cusp of rapid growth and such a scheme would be necessary to help the players grow & brace up themselves to face the severe competition. While the Finance Minister has not touched upon the extension issue so far, he has certainly provided a further bolster with the enhanced allocation for FY07. [Positive for Alok, Banswara, etc.](#)

Rs.189 Crs. to be provided for Scheme for Integrated Textiles Parks (SITP)- Overall, an very positive impact. The resulting infrastructural benefits & economies of scale would enable thriving of the large & still fragmented Indian Textiles. [Positive garmenting companies like Kitex, etc.](#)

Jute Technology Mission to be launched; a National Jute Board to be established - This should provide a much needed impetus to the Indian Jute industry. This would help the players to expand & compete with the Bangladeshi peers. [Positive for Champdany Industries & Cheviot Company.](#)

Preferred Budget Picks :

Our Universe

- Banswara Syntex (Synthetic Yarn, Fabrics & Garments)
- Gokaldas Exports (Garment Exporter)

Others

- Cheviot Company (Jute Goods)
- Raymond (Domestic Branded & Exports of Fabrics & Apparels)
- Celebrity Fashions (Garment Exporter & Domestic Branded Retail)
- Sangam India (Blended Yarn & Fabrics)
- Indo Rama Synthetics (Synthetic Fibre & Yarn)

Banking

State Bank of India (SBI) is a market leader in the micro finance segment with a 35% market share. As SBI and Punjab National Bank (PNB) are already aggressively concentrating in agriculture the increased focus in this segment will have little impact on the bank.

As SBI's current short term lending to the agriculture segment is at 7-7.25%, the maximum decline in the yield will be 0.25%. This proposal will exert pressure on the margins of the banks. However the budget mentions subvention to NABARD so that they can provide refinance at economical rates.

Inclusion of food processing in priority sector credit a big positive for all the banks as it not only increases the avenues for lending but also reduces the overall cost with higher loans to a single

entity and faster processing. Further the yields are higher than agriculture loans.

Increase in limit of FII investment in Government securities from \$1.75 bn to \$2 bn is not substantial hike to improve the depth of the government securities market. Further as the interest rate differential is not high, the impact will be very small. The hike in FII limit investment in corporate debt from \$0.5 bn to \$1.5 bn will be improving the liquidity in this segment.

It has been proposed that capital injected in the banks in the form of special securities will be converted to tradable SLR Government of India dated securities. The government support in the form of non-tradable government securities were only issued to weak and sick PSU banks. SBI does not have any of these securities. Further the bank has SLR securities well above the required 25% limit. However the bank will consider purchasing these securities only if the yields on these securities are higher than the loan yields. PNB holds around Rs 5500-6000 mn of these special securities.

The inclusion of investments in fixed deposits in scheduled banks for a term not less than 5 years in section 80C of Income Tax Act will lead to an increase in senior citizens deposits. However the impact is not going to be substantial.

It has been proposed to include ATM operations under the service tax net. Thus a service tax of 12% will now be levied on SBI 's revenue from its ATM operations, which currently stands at Rs 500 mn. The bank has yet to make a decision whether this charge will be transferred to its customers.

The fiscal deficit is low at 4.1% thereby reducing the pressure on interest rates.

Clarifications are awaited on the statement mentioning service tax will be levied on credit card, debit card, charge card or other payment related services.

The fillip given to some sectors with reduction in customs and excise duties will boost demand for both retail and corporate credit.

IT / Software

Infosys Technologies Ltd. - Neutral

FBT has continued but the Super Annuation contribution for employees, under Rs.100,000 will be exempt from FBT. This will have a small positive on the tax rate of companies.

There is a 8% excise duty charge on Packaged Software sold over the counter (OTC), which would increase Infosys' cost by around Rs.6 - 7 cr. (less than 0.3% of profits) as they buy OTC software of around Rs. 70 cr.

We believe this should not affect Infosys's Banking product Finacle (4% of revenues) as it is not sold over the counter.



Satyam Computers Ltd. - Neutral

FBT has continued but the Super Annuation contribution for employees, under Rs.100,000 will be exempt from FBT. This will have a small positive on the tax rate of companies.

There is a 8% excise duty charge on Packaged software sold over the counter, which would increase Satyam's cost by around Rs.2 cr. as they buy Over the counter software of around Rs.20 cr.

Food Processing Industry

Budget impact on the Food Processing Industry: Marginally positive overall.

1. Exemption from excise duty for condensed milk, ice cream, preparations of meat, fish and poultry, pectin, pasta and yeast from excise duty.

Impact: Heritage Foods Ltd. to benefit marginally.

2. Reduction of Excise duty from 16% to 8% on Ready to Eat packaged food and instant food mixes such as dosa and idli mix.

Impact: Satnam Overseas to benefit.

3. Food processing to be treated as priority sector for bank credit.

Impact: Again Satnam Overseas to benefit.

4. NABARD to create a separate window with a corpus of Rs 1000 cr for "refinancing loans" to the food processing sector, especially for Agro processing infrastructure and market development.

5. Customs duty on packaging machines for food processing industry reduced from 15% to 5%.

Impact: Cosmo Films Ltd. has indicated that the budgetary changes will positively impact their Profit before tax by Rs. 2 crores.

Defence

Bharat Electronics Ltd. - Neutral

The defence budget growth has been slightly lower than the past (7% Y-o-Y, totaling Rs. 89000 crores).

The Capital Outlay in the defence budget is to the tune of Rs.37450 cr. up from Rs.34000 cr. last year, which is a 10% increase. Technically, this is lower than the average CAGR of 18% over the last 8 years, although this number is very much skewed due to an almost 100% jump in Capital outlay in 2004 -2005.

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