

Key highlights of 2nd stimulus package

- RBI cuts key rates: The repo and reverse repo rates were slashed by 100 bps each while the CRR was slashed by 50 bps
- The 'all in cost' ceiling on external commercial borrowing (ECB) would be removed, under the approval route of the RBI
- The development of integrated township would be permitted as an eligible end use of the ECB, under the approval route of the RBI
- NBFCs, dealing exclusively with infrastructure financing would be permitted to access ECB from multilateral or bilateral financial institutions, under the approval route of the RBI
- FII investment limit in rupee denominated corporate bonds in India would be increased from US\$ 6 billion to US\$15 billion
- Credit targets of public sector banks are being revised upwards, which will be monitored by the government on a fortnightly basis
- EXIM bank has obtained line of credit of Rs 5000 crore to provide pre and post shipment credit to Indian exporters
- Accelerated depreciation of 50% will be provided for commercial vehicles purchased between 01/01/2009 and 31/03/2009
- Importantly, the government will closely monitor its spending to expedite the pace of expenditure for all schemes and programmes
- The government has re-imposed countervailing duty (CVD) of 8% and special CVD (special additional duty of customs) of 4% on imported cement, thereby providing a level playing field for domestic suppliers
- Withdrawal of exemptions from CVD on TMT bars and structurals
- Withdrawal of full exemption from basic customs duty on zinc and ferro alloys

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Banking and Financial services

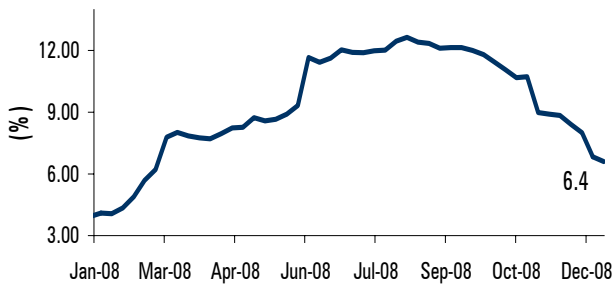
Key Rates Cut...

CRR	↓50bps to 5 %
Repo rate	↓100bps to 5.5 %
Reverse repo	↓100bps to 4 %

Proactive measures from RBI: Once again...

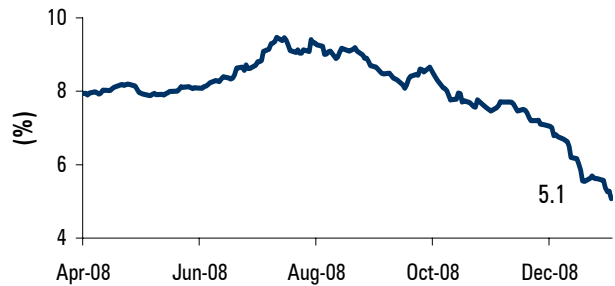
With the pressure shifting from inflation to growth, we are seeing aggressive rate cuts from the RBI in tandem with other global economies. The cut of 50 bps in CRR to 5% will infuse about Rs 20,000 crore in the system and will ease the pressure on bank's margins. Also, repo and reverse repo rate cuts of 100 bps each will induce banks to further cut lending and deposit rates and, thereby, reduce cost of funds for the Indian corporate sector. Though banks are still hesitant to lend in spite of having adequate liquidity and are conserving cash, we may see some incremental credit offtake, going ahead, as the government pushes credit targets of PSU banks. The two stimulus packages to push demand will take some more time to yield results and stimulate growth in the economy.

Exhibit 1: Inflation at 10 month low



Source: Reuters, ICICIdirect.com Research

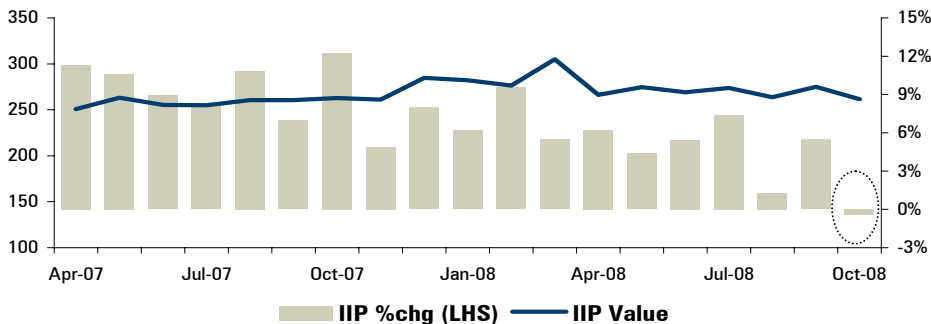
Exhibit 2: 10 year G Sec yield on a downturn



Source: Reuters, ICICIdirect.com Research

Inflation has fallen from the highs of above 12% to 6.3% and 10-year G-sec yields are off their highs of above 9% to sub 6% (5.1%). We see the downtrend in rates, inflation and yields continuing till the RBI is comfortable with the fact that economic growth will not deteriorate further from hereon since the last released data on exports growth and IIP were both on the negative side. Even the RBI seems to be extremely cautious on account of the global slowdown and uncertain times ahead.

Exhibit 3: Negative IIP data: A cause for concern

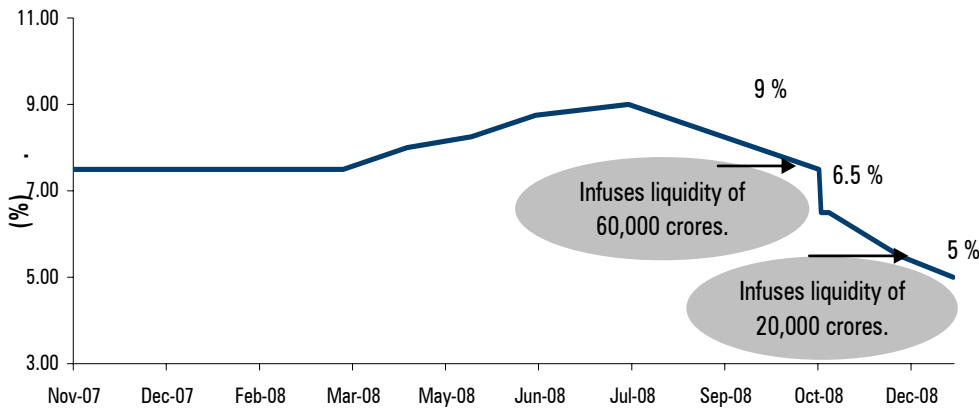


A fall in IIP for the first time in last 15 years- warranting prompt actions from both monetary & fiscal aspects

Source: CMIE, ICICIdirect.com Research

Monetary policy measures

Exhibit 4: CRR: Falling like a house of cards

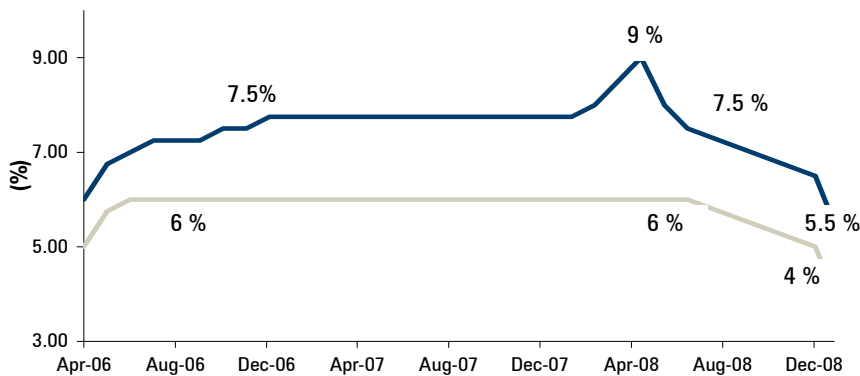


A 400 bps cut has helped CRR to come to its November 2006 levels of 5% after peaking at 9% in July 2008.

Source: RBI, ICICIdirect.com Research

The cumulative amount of primary liquidity made available by various measures initiated by RBI is over Rs 300,000 crore.

Exhibit 5: Movement in Repo and Reverse repo rate.



Source: RBI, ICICIdirect.com Research

The cumulative amount of primary liquidity made available by various measures initiated by RBI is over Rs 300,000 crore.

Impact

Though the rate cuts are positive for the banking sector, still managing risk will be essential in a rising NPAs scenario. We assume most of the impact of rate cut is priced in G-sec yields but immediate reaction cannot be denied. The banks are expected to start cutting both lending and deposit rates more aggressively than earlier rate cuts, with PSU banks taking the lead.

Public sector banks are expected to be capitalised to the tune of Rs 20000 crore over the next two years, thereby, boosting balance sheet growth and profitability. We see the CRR cut impacting margins positively but continuous fall in bond yields and lending rates will put some pressure on margins on account of declining interest income.

Preferential capital of Rs 20000 crore announced in this package will benefit banks where government holding is less than 55%. The banks, which fall under this category, are **Andhra Bank, Bank of Baroda, Dena Bank, IDBI Bank and Oriental bank of Commerce**. Among the coverage universe we are bullish on **SBI, PNB and IDFC**.

Automobile – Commercial vehicles

Stimulus package for CVs

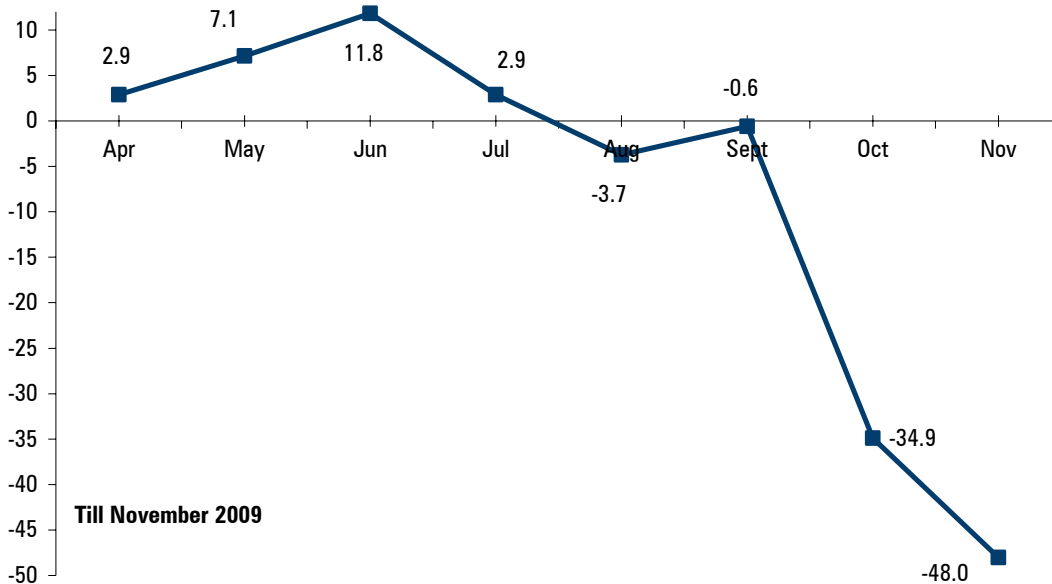
Accelerated depreciation for purchase of CVs (Jan – Mar'09) - 50% Vs 30%

Likely arrangement between PSU banks with NBFCs for CV financing

One-time assistance to states until June'09 towards purchase of buses for urban transport systems

The de-growth witnessed in commercial vehicles (CVs) and plant shutdown (temporary) announced by major original equipment manufacturers (OEM) are indicators of a bleak outlook for the segment. The announcement of a fiscal package by government for the industry is a kind of a light at the end of the tunnel. The policies announced are positives for the industry growth. However, stricter lending norms and economic slowdown are the main hurdles for growth, going forward.

Exhibit 6: State of industry (month wise yoy growth (%))



Tata Motors' CV sales were down by 53.6% in December, while M&M CV sales were down by 60% (Reported till date)

Source: SIAM

Measures announced

- **Accelerated depreciation of 50% for commercial vehicles purchased during January 1 2009 – March 31 2009 as against 30% normally available**
 - It is a positive step by the Centre as it would provide additional incentives to customers to replace existing vehicles or buy new ones in an effort to get rebate on income tax
- **An arrangement to be worked out with public sector banks (PSU) to provide a line of credit to non banking finance companies (NBFCs) specifically for purchase of commercial vehicles**
 - Financing was the major concern. This step would help in improving lending, which would boost CV sales, which would be a very positive step for CV financing. However, the success of this move depends upon PSU banks' lending norms
- **A direct stimulus to sales of buses in one-time measurement up to June 2009. Accordingly, states will be provided assistance under JNNURM (Central government sponsored scheme to encourage urban development) for purchase of buses for their urban transport systems**
 - This is a positive step for enhancing bus sales. However, how effective it would be depends upon the financial position of most states and its fund requirements for urban infrastructure. The government is also yet to announce the details of the scheme in terms of quantum and criteria for bus purchases.

The major boosters for CV sales are improving economic conditions through improvement of industrial and agriculture production, and improvement in freight rates. Some more positive steps from the government are needed to boost the demand.

Positive for companies

1. Tata Motors – enjoys over 60% of market share
2. Ashok Leyland
3. Mahindra & Mahindra
4. Eicher Motors

CVD & Special CVD re-imposed on imported cement

Measures announced

- The government has re-imposed countervailing duty (CVD) of 8% and Special CVD (special additional duty of customs) of 4% on imported cement, thereby providing a level playing field for domestic suppliers.
- In India, cement is mostly imported in the northern states viz. Punjab, Himachal Pradesh from Pakistan, which was expected to be 0.8-1.0 MT in FY09. It constitutes less than 1% of the all-India cement consumption and around 2.5% of the estimated consumption in the northern region for FY09. Weak demand and imports has suppressed the volume growth of the players in the northern region forcing ACC to shut down its Gagal-II plant in HP.

Subsequent to impositions of CVD and special duty, the landed cost of imported cement would be at par with prices in domestic markets. The landed cost of imported cement is likely to be in the range of Rs 220-230 per 50 kg bag against the price of Rs 200 per bag before the imposition of duty.

Impact: Marginally positive

Thus, we believe the development would be marginally positive for the northern India players like

1. Shree Cement
2. ACC
3. JK Cement

Measures announced

- Withdrawal of exemptions from CVD on TMT bars and structurals
- Withdrawal of full exemption from basic customs duty on zinc and ferro alloy

Impact analysis

In the second stimulus package announced on Friday, January 2 2009 to boost the domestic economy along with other measures the government has withdrawn the exemptions from countervailing duty (CVD) on TMT bars and structurals.

The government had earlier removed the 10% CVD that was imposed on TMT bars and structurals to contain inflation and support the real estate and infrastructure sectors. However, in the backdrop of sharp correction in prices of TMT bars and structurals globally and in the domestic markets, the decision to withdraw the exemption of CVD should help the domestic players at a time when they are facing a slowdown in overall demand. Companies like RINL and SAIL are set to get the benefit of this move as, along with many small manufacturers of TMT bars, these companies were also taking a hit by selling those products at a price even lower than the cost of production during the recent past due to low demand and cheaper imports.

The second stimulus package has also brought some good news for domestic manufactures of zinc and ferro alloys, as the government has announced the withdrawal of the basic custom duty exemption on these two products. The government had earlier exempted 5% basic customs duty on zinc and ferro alloys to bring down the prices of these products in the domestic markets by encouraging cheaper imports with the main aim of curbing soaring inflation. However, zinc prices have started coming down sharply along with other metals and fell by more than 50% in 2008 due to demand slowdown and sharp build up of stocks in LME warehouses, posing threat to further cheaper imports. Ferro alloys prices have also come down significantly over the past three to four months due to sharp downward correction in steel and nickel prices and demand slowdown for stainless steel.

In view of the above and a sharp fall in the headline inflation coupled with a slowdown in the economy as a whole, the government has initiated the latest move, which should help domestic producers by protecting them against cheaper imports. **Hindustan Zinc and JSW Steel**, among the big players, is likely to be the major beneficiaries of this move.

However, we believe that though the abovementioned companies should benefit from this move, the extent is not likely to be very high.

Measures announced

The government has permitted states to access the market for borrowing about Rs 30,000 crore to meet additional expenditure during the year. The government has eased the external commercial borrowing (ECB) norms and hiked the foreign institutional investor (FII) investment limit in rupee-denominated instruments to \$15 billion from the current ceiling of \$6 billion.

Impact analysis

Infrastructure companies that were facing constraints in achieving financial closure for their projects can now breathe a bit easy. The second stimulus package will benefit all the companies in the infrastructure space, which have been facing delays in achieving financial closure of their projects. These moves will surely inject some liquidity into the system, which is badly needed at this point of time. The Government has allowed IIFCL to raise Rs 30,000 crore by way of tax free bonds for refinancing projects mainly in the highway and port sectors. The companies which will benefit the most are **Hindustan Construction Company** and **Nagarjuna Construction Company** as they have more exposure towards the road sector. NHA will now find more bidders for the road projects it is planning to announce in the near term as this is the sector, which is facing major execution delays. **GMR Infra and Reliance Power** will also benefit as these companies are in the process of achieving financial closure of their announced projects and these moves will help them achieve it.

Measures announced

The second stimulus package that has been announced has very little in store for the textile sector, which has been unable to satisfy the industry's demands

- The reduction in CRR, repo and reverse repo rate is expected to benefit the textile companies with high debt and aggressive expansion plans like Alok Industries and Bombay Rayon Fashions.
- The government extended the Duty Entitlement Passbook (DEPB) scheme till December 31 2009 and restored the rates at those prevailing prior to November 2008 i.e. 7% (increase of 3% from current 4%). This may improve the competitiveness of the textile exporters against other low-cost countries like China, Pakistan, Vietnam and others.
- Duty drawback rates on knitted fabrics and specified varieties of yarn have been enhanced with retrospective effect from September 1 2008.
- EXIM Bank has obtained a line of credit of Rs 5,000 crore from the RBI and will provide pre-shipment and post-shipment credit, in rupees or dollars, to Indian exporters at competitive rates. The textile sector contributes approximately 13% to the overall exports from India.

Impact analysis

The above measures will benefit, though very marginally, the exporting companies in the textile sector like **Gokaldas Exports, Bombay Rayon Fashions, Welspun India and Alok Industries.**

The industry had raised the following demands in order to facilitate growth, which have not been considered yet:

- Two-year moratorium on repayment of loans,
- A special package for working capital consisting of 7% interest rate for cotton purchase
- Reduction in margin money for working capital from 25% to 10%
- Enhancement of credit limit from three months to nine months
- A 2% increase in the interest subvention for export credit.

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