Sanctum View

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Union Budget FY20-21

Budget Highlights

The budget tried to accommodate expectations of various set of groups and attempted to take balanced approach in terms of allocation with focus on developing rural economy, infrastructure, healthcare and education. While equity markets were expecting some big bang reforms to revive demand situation amidst slowing economy, budget lacked major measures to immediately boost demand. Abolition of Dividend Distribution tax is a positive while tweaks in Personal Income tax needs to be probed further to derive exact benefit to middle income group.

Doubling farmers' incomes by 2022

The government remains committed to the goal of doubling farmers' incomes by 2022. Focus on cultivation of pulses, expansion of micro-irrigation through Krishi Sinchai Yojana, have raised the self-reliance of the country. The government also announced viability gap funding for creation of efficient warehouses & cold storages on PPP mode. The government will also facilitate doubling of milk processing capacity and put in place a framework for development, management and conservation of marine fishery resources in order to grow fish production at rapid pace.

Spending on Infrastructure remains in Focus

The government reiterated its plan for spending INR 100 lakh crore on infrastructure projects in the next 5 years. This is likely to provide huge employment opportunity to India's youth in construction, operation and maintenance of infrastructure. The focus remained on developing road infrastructure and monetization of existing assets to generate liquidity for NHAI. Similar steps are taken to boost other means of transport like rail, air and inland waterways.

Marginal deviation from fiscal glide path

The economy has slowed down considerably owing to various global and macro factors. As a result, the fiscal deficit for FY20 has been revised to 3.8% from 3.3% earlier. For FY21, the fiscal deficit target has been revised to 3.5% with a nominal GDP growth assumption of 10%. The marginal increase in the fiscal deficit is broadly in line with the investor expectations, however, for FY21 the reduction in fiscal deficit is more through divestment, which is targeted at INR 2.1 lakh crores, double the amount targeted in FY20.

Middle class tax relief or status quo?

While the government intended to simplify and reduce the tax burden for the middle-class Indians, it appears to have complicated the tax calculation process. Under the new tax regime there are seven slabs of different rates as against four slabs earlier. However, the exemptions and deductions available in the old tax regime are not available should the taxpayer opt for the new tax regime. This makes the tax liability calculation cumbersome for an average individual. On our back of the envelope calculation of tax liability for a person earning Rs. 15 lakhs per annum, the tax liability looks lower in old tax regime if he opts for most of the exemptions. Thus, the question arises as to the change is really bringing down the average tax rate for India's middle class.

Dividend taxed in the hands of the receiver

The government abolished dividend distribution tax paid by corporates while making it taxable in the hands of the receiver. This is positive for the high cash flow generating high dividend paying companies as it will reduce the tax leakage while distributing the profits. This will also reduce the cost of capital of foreign promoters. However, this is a negative development for the high net worth individuals as the dividend distribution which was taxed at 15% will now be taxed at slab rates which is higher in most cases.

Other Key Budget Highlights

- In a major initiative, the government proposed to sell a part of its holding in LIC by way of Initial Public Offer. The government has pegged disinvestment for FY21 at INR 2.11 lakh crore. For FY 2019-20, the disinvestment target has been brought down to INR 65,000 crores from INR 1.05 lakh crore budgeted earlier.
- In order to give a boost to the start-up ecosystem, FM proposed to ease the burden of taxation on the employees by deferring the tax payment on ESOPs.
- Turnover threshold for audit of MSMEs hiked to INR 5 crores provided 95% of the receipts are in non-cash form.
- To further deepen the corporate bond market the FPI limit in corporate bonds was increased from 9% to 15%.

- Deposit Insurance coverage on deposits with banks was increased to INR 5 Lakh from INR 1 Lakh.
- NRIs allowed to invest in certain categories of G-secs
- Affordable housing tax holiday deadline extended by a year

Outlook

On equity markets

The market was disappointed as the budget lacked any significant measure to stimulate demand and did not provide any relief on capital gains tax as expected from budget. The equity markets sold off with headline Nifty crashing 2.5% and midcap index falling 2.7%. Some of the sectors which sold off sharply were insurance and PSU banks. Realty index also witnessed a sharp sell off as there was no major booster provided to the ailing real estate industry.

While, there are enough talks about the dichotomy in the Indian markets over last one year. We have seen some revival in the broader markets in the hope of economic recovery led by expectation of good Rabi crop and some green shots in lead economic indicators. This market is expected to increasingly become a bottom up stock pickers market and staying invested in good quality high growth companies will be key to generating alpha going forward.

On debt

As a result of lower GDP growth and slowing tax collections, the fiscal deficit has been revised to 3.8% from 3.3% earlier. The revised fiscal deficit and growth assumptions seem to be more realistic however, a stretched divestment target for FY21 can be negative for the bond investors.

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