Market’s most awaited document

UNION BUDGET

2015-16

ALPHA CAPITAL

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UNION BUDGET ANALYSIS (2015 – 16)

Indian economy has weathered many challenges successfully in recent times and is currently placed on a cyclical upturn, on the back of strong policies and a whiff of new optimism.

The growth rate of the economy, measured by the growth in GDP at constant (2011-12) market prices, is projected to clock 7.4 per cent in 2014-15, according to the Advance Estimates released by the Central Statistics Office.

India is one of the very few countries for which IMF and World Bank have raised their growth forecast.

The clear thrust in the Budget for 2015-16 has been on infrastructure. Apart from increasing investments in infrastructure, there are a series of announcements with respect to:

- setting up of National Investment and Infrastructure Fund.
- tax free infrastructure bonds, taxation benefits in respect of Real Estate Investment Trusts (REITs).
- existing excise duty on petrol and diesel to the extent of Rs. 4 per litre is to be converted into Road Cess, intended to fund investment in roads and other infrastructure.

The “Make-In-India” programme has received attention through phased reduction in corporate tax rates.

The innovative proposals for monetising gold, if successful, would result in greater financial savings as compared to physical savings.

FISCAL DEFICIT

The journey for fiscal deficit target of 3% will be achieved in 3 years rather than 2 years. The fiscal deficit targets are 3.9%, 3.5% and 3.0% in FY 2015-16, 2016-17 & 2017-18 respectively.

The government is proposing to increase the plan capital expenditure by 33% in FY16 over FY15, which is aimed at boosting productive assets.

The quality of the deficit would be dependent on the realization of the disinvestment targets and the high tax buoyancy assumed within the budget.

	2014-15	2015-16	% Change
GDP	12,653,762	14,108,945	11.50%
Fiscal Deficit as %GDP	4.10%	3.90%	
Non Plan Expenditure	1,213,224	1,312,200	8.16%
Plan Expenditure	467,934	465,277	-0.57%
Total Expenditure	1,681,158	1,777,477	5.73%
Tax Receipts	908,463	919,842	1.25%
Non Tax Revenue	217,832	221,733	1.79%

To name a few reasons for increase in Non -plan expenditure –

- Increase is mainly on account of higher requirement for payment of interest on market loans, cash management bills, treasury bills and reserve funds.
- Increase in higher provisioning for grants to States – because of revenue losses due to phasing out of CST.
- The outlay for food subsidy may need to be revised upwards if the National Food Security Act is rolled out pan-India on April 1, 2015 and the entitlements are not curtailed.

TAXATION

While nominal GDP growth is expected to remain unchanged at 11.5% in 2014-15 and 2015-16, GoI has forecasted a rise in growth of its gross tax revenues to 15.8% in 2015-16 BE from 9.9% in 2014-15 RE.

This increase is reported due to hike in –

- indirect taxes
- increase in surcharge of direct taxes
- impact on excises hikes of petrol & Diesel instituted since Nov'13.

	2014-15 BE	2014-15 RE	2015-16 BE	Variation 2014-15	Growth in 2015-16
Gross Tax Revenues	13645	12514	14495	-1131	16%
Corporation Tax	4510	4261	4706	-249	10%
Income Tax	2843	2786	3274	-57	18%
Customs Duty	2018	1887	2083	-131	10%
Union Excise Duty	2071	1855	2298	-216	24%
Service Tax	2160	1681	2098	-479	25%

Growth of net tax revenue is subdued on account of the sharp step up in devolution of central taxes to state governments. Higher amount of capital receipts have been estimated, by betting on the success of achieving the disinvestment target of Rs. 410 Billion.

TAXATION - DIRECT

Tax Payers

- **Good**
  - Wealth Tax abolished with effect from 2015-16.
  - One can invest upto Rs. 1.5 lakh in NPS, additional Rs. 50,000 will get deduction under 80CCD
  - Exemption limit for transport allowance doubled from Rs. 800 to Rs. 1600.
  - Deduction limit for health insurance premium upto Rs. 25,000.
  - Investments in Sukanya Samriddhi Scheme eligible for tax deduction under 80C
- **Bad**
  - Surcharge on income of super rich individuals increased from 10% to 12%. The effective tax rate now 34.6% against 33.9% earlier.
  - No change in personal Income Tax Slabs

Investors

- **Good**
  - Tax free infra bonds in roads, rails and irrigation.
  - More choice for gold buyers such as coins and new gold schemes
  - Mutual fund merger now exempt from capital gains tax.
  - Employees now have an option to choose between EPS and NPS.
  - Tax pass through to be allowed to both category I and category II AIF.
- **Bad**
  - Lower dividend for shareholders as surcharge on DDT up from 10% to 12%
  - No increase in limit of exemption u/s 80C.

EXEMPTIONS IN PERSONAL TAX

Deduction u/s 80C	150,000
Deduction u/s 80CCD	50,000
Deduction on account of interest on house property loan(Self occupied Property)	200,000
Deduction u/s 80D	25,000
Exemptions of transport allowance	19,200
Total	**444,200**

TAXATION – INDIRECT

Indirect Taxation

- Service Tax Hike - from 12.36% to 14%.
- CENVAT hike - from 12% to 12.5%.
- Excise duty on leather footwear with retail price greater than Rs. 1000 per pair reduced to 6%.
- Excise duty increased - 25% for cigarettes of length less than 65 mm and 15% for other lengths.
- Service tax exemption on services provided by mutual fund distributor/agent to AMC stands withdrawn.

Corporate Tax

- Rates of corporate tax remains unchanged for both domestic and foreign companies.
- The rate of corporate tax is proposed to be reduced from 30% to 25% over the subsequent four years.
- The various exemptions provided to companies will be removed and the corporation tax rate cut will take effect from FY 2016-17.
- Rate of surcharge increased, hence maximum tax rate for Domestic companies -
  - 1 cr< income< 10 cr - from 32.45% to 33.06%
  - income>10 cr - from 33.99% to 34.61%
- Proposed to levy a surcharge of 12% as against 10% on additional income-tax payable by companies on distribution of dividends and buyback of shares, or by mutual funds and securitisation trusts on distribution of income.

DEBT MARKET

GoI has indicated gross borrowings of Rs. 6.0 trillion in 2015-16, marginally higher than the level in 2014-15. The net long term borrowings are placed at Rs. 4.56 trillion in 2015-16, 2.1% higher than the borrowings of Rs. 4.46 trillion in 2014-15.

This in addition with the expectation of 25-50 bps of Repo rate cuts over the course of 2015, is likely to dampen yields of dated Government securities.

RBIs statement with reference to budget – 4th March, 2015

RBI cut the repo rate by 25 bps (from 7.75% to 7.5%) on 4th March on the back of government resolve shown in the budget to take fiscal consolidation religiously.

In the monetary policy statement RBI governor said –

There are many important and valuable structural reforms embedded in this Budget, which will help improve supply over the medium term. In the short run, however, the postponement of fiscal consolidation to the 3 per cent target by one year will add to aggregate demand.

The fiscal consolidation programme, while delayed, may compensate in quality, especially if state governments are cooperative. Given low capacity utilisation and still-weak indicators of production and credit off-take, it is appropriate for the Reserve Bank to be pre-emptive in its policy action to utilize available space for monetary accommodation.

EQUITY MARKET – SECTORAL IMPACT

Iron and Steel – Moderately positive Impact

Proposal

- Focus on infrastructure and construction.
- Increase in tariff rate on iron & steel and articles of iron or steel from 10% to 15%.

Synopsis

- Increased tariff rate on iron and steel from 10% to 15% is expected to discourage imports.
- The emphasis on housing as well as other infrastructure areas like roads and railways is a positive.

Oil and Gas – Marginally Positive Impact

Proposal

- Provision of subsidy for sensitive petroleum products: Rs. ~301 billion for 2015-16 (BE); could be adequate for full FY16.
- Subsidy rationalization to continue; specifics have not yet been announced.

Synopsis

- The budgetary provision for fuel subsidy of Rs. ~301 billion for FY16 could be adequate for full FY16 This could lead to lower interest cost and improved liquidity position for the OMCs.
- The DBT scheme of LPG could play a modest role in cutting down the fuel subsidies in this regard.

Power – Positive Impact

Proposal

- Announcement of 5 coal based Ultra Mega Power Projects (UMPPs) to be awarded with all approvals in place.
- Formation of National Investment Infrastructure Fund announced.
- Scale up in renewable energy capacity addition programme to 175 GW by FY 2022.

Synopsis

- The announcement of 5 UMPPs to be awarded along with approvals in place is a positive for the power sector, which is expected to facilitate timely implementation of such large sized thermal projects as well as meet the increasing energy requirements in the long run.

Capital Goods – Marginally Positive

Proposal

- Increased budgetary allocation by Rs. 700 billion in FY 2015-16 for infrastructure sector.
- Formation of National Investment Infrastructure Fund announced; re-introduction of tax free bonds by FIs for funding in infrastructure projects.

Synopsis

- Given the slowdown in capex by the private sector in the last two-three year period, the increased budgetary allocation towards capex in infrastructure sector & also higher capex by public sector entities remain positives and this in turn is likely to improve demand for capital goods in the near term.

- The scale up in renewable energy capacity addition programme as well as 5 UMPPs would result in increased demand for capital goods in the medium to long run.

- Measures announced to encourage long term funding by way of re-introduction of tax free bonds as well as creation of National Investment Infrastructure Fund are also positives for the capital goods sector.

Cement – Marginally Positive Impact

Proposal

- Increase in freight rate on cement and coal in the Rail Budget.
- Increase in clean energy cess on coal from Rs. 100/MT to Rs. 200/MT.
- Increase in ad valorem rate of Basic Excise Duty from 12.36% (inclusive of educational cesses) to 12.5%.

Synopsis

- The increase in freight rate in rail budget and excise duty on cement is likely to hurt the margins of cement companies since they may not be able to fully pass on the hikes to the customers given the competitive pressures.
- The higher freight rates and clean energy cess on coal too is likely to result in cost pressures.

Real Estate – Moderately Positive

Proposal

- Pass-through taxation structure for the rental income earned by REITs from their own assets.
- Allowance of foreign investments in Alternative Investment Funds.
- Allocation of Rs. 224.07 billion for housing and urban development.
- Introduction of Benami Transactions (Prohibition) Bill to curb domestic black money in real estate.

Synopsis

- Pass through status of REITs to provide a boost to investment in Real Estate Sector.
- Tax incentives to REITs by providing a tax pass through status to rental income earned by the REIT from its own assets.

- The allowance of foreign investment in Alternate Investment Funds (AIF) would provide further impetus to investments in the sector.
- In line with the endeavor to have housing for all by 2022, the government has set a target of constructing 60 million affordable houses across urban and rural areas and has allocated Rs. 220.47 billion towards housing and urban development. This is expected to provide a boost to the low cost housing segment.
- Introduction of Benami Transaction Bill may act as deterrent and may impact demand.

Construction/ Infrastructure – Positive Impact

Proposal

- Higher capital outlays for Roads (increase by Rs. 140.31 billion) and Railways (increase by Rs. 100.50 billion) to support infrastructure projects. Investment in infrastructure is proposed to increase by Rs. 700 billion in FY16 over FY15.
- Conversion of Rs. 4 per litre of excise duty on petrol and diesel into Road Cess to provide additional ~Rs. 400 billion to fund investment in roads and other infrastructure.
- Annual flow of Rs. 200 billion to a proposed trust - National Investment and Infrastructure Fund (NIIF). NIIF can further raise debt and invest as equity in infrastructure finance companies.
- Re-introduction of tax-free infrastructure bonds for projects in the rail, road and irrigation sectors.
- Setting up a Public Debt Management Agency (PDMA) to deepen the Indian Bond market to provide additional fund raising avenues for infrastructure sector.
- Pass through status provided to all the sub-categories of category-I and category-II Alternative Investment Funds (AIFs).
- Setting up 5 new Ultra Mega Power Projects (UMPPs), each of 4000 MWs, in the plug-and-play mode (all clearances and linkages will be in place before the project is awarded).
- Housing for all by 2022, the government has set a target of constructing 60 million affordable houses in urban and rural areas.

Synopsis

- With the infrastructure as a key priority, the budget has proposed multiple steps to ease availability of funds for infrastructure sector, improve private sector participation, as well as allocated higher funds towards public sector infrastructure projects.
- Conversion of excise on petrol/diesel into Road Cess will enable higher public spending towards these infrastructure projects.

FMCG & Consumer Durables – Negative Impact

Proposal

- Excise duty on tobacco increased to Rs 70/Kg from Rs 60/Kg; excise duty on cigarettes increased by 15%-25%.
- Excise duty on mineral water and aerated drinks raised to 18% from 12%.

Synopsis

- Excise duty hike will hinder the demand

BANKS – Negative Impact

Proposal

- Provision of Rs. 95.55 billion for recapitalization of Public Sector Banks/FIs.
- Comprehensive Bankruptcy Code to be introduced in fiscal 2015-16.

Synopsis

- Inadequate provisions of Rs. 95.55 billion as against Rs. 500 billion Tier 1 capital requirement of PSBs in FY 2016.
- The bankruptcy code could aid the financial sector in their recovery efforts from borrowers who file for bankruptcy in future.
- The increase in limit for deduction from taxable income on account of contribution to Pension Fund and New Pension Scheme will lead to increase in financial savings which eventually may increase the investment appetite for debt instruments.

Financial Institutions and NBFCS – Positive Impact

Proposal

- NBFCs with more than Rs 5 billion asset base to be covered under SARFAESI Act, 2002.
- MUDRA Bank to be set up, with a corpus of Rs 200 billion, and credit guarantee corpus of Rs 30 billion.
- To permit tax free infrastructure bonds for the projects in the rail, road and irrigation sectors.
- Establish a National Investment and Infrastructure Fund (NIIF), with annual flow of Rs 200 billion.
- Comprehensive Bankruptcy Code to be introduced in fiscal 2015-16.

Synopsis

- SARFESI access for NBFCs to improve recoveries from immovable asset financing, such financing constitutes around ~14% of Rs. 10 trillion credit pie of NBFC.
- MFI's funding diversity, cost of funds and liquidity to improve with access to refinance from MUDRA Bank. Eventually end borrowers may benefit as MFI lending spreads are capped at 10%.
- Tax free infrastructure bonds to reduce cost of funds for entities operating in the rail, road and irrigation sector.

Insurance and Pension – Marginally Positive Impact

Proposal

- To increase in the limit of deduction for individuals in respect of health insurance premium from Rs. 15,000 to Rs. 25,000 (from Rs 20,000 to Rs 30,000 for Senior Citizens).
- The limit on deduction on account of contribution to a Pension Fund and the New Pension Scheme is proposed to be increased from Rs. 100,000 to Rs. 150,000 and an additional deduction of Rs. 50,000 is proposed to be provided for contribution to the New Pension Scheme under Section 80CCD.

Synopsis

- Current penetration levels on health insurance as well as corpus under New Pension Scheme are low, the proposals could help in improving the same.

Gold

Proposal

- Formation of Sovereign Gold Bond (an alternate to purchasing metal gold). The bonds will carry a fixed rate of interest and also be redeemable in cash in terms of the face value of the gold, at the time of redemption by the holder of the bond.
- Gold Monetisation scheme will replace present gold deposit and gold metal loan.
- Work on developing an Indian Gold coin, which will carry the Ashok Chakra on its face.

Impact

- Gold Monetisation will curb the import demand for gold and further help in containment of trade deficit and CAD.
- The coin would help reduce the demand for coins minted outside India and also help to recycle the gold available in the country.

Mutual Funds

- Merger of two or more schemes will be exempted from capital gain tax and will not be treated as a mere 'transfer' of the mutual fund units.
- Service tax in respect of mutual fund agents and mutual fund distributors services shall be paid by AMC or, as the case may be, by the mutual fund receiving such services.
- The dividend distribution tax will be increased to effective rate of 28.84% from 28.34%, due to proposed increase in surcharge from 10% to 12%. This will impact the returns of investors opting for the dividend option in debt funds.

Concluding Remarks

The Union Budget for 2015-16 has attempted to strike a balance between supporting investment, boosting social sector spending and introducing investor and market friendly measures –

- deferral of GAAR for two years
- rationalising capital gains at the time of listing of REITs and Infrastructure Investment Trusts (INViTs)
- allowing foreign investments in Alternate Investment Funds (AIF)
- doing away with the distinction between foreign direct investments and foreign portfolio investments
- providing a roadmap for rationalization of Corporate taxes and re-emphasising on the need for having a stable and predictable tax regime.

Budget contains a series of incrementally positive steps, with the focus firmly on reviving investments in infrastructure, improving the ease of doing business and augmenting funds in the hands of the middle class.

Key disappointments include the increase in indirect taxes and certain surcharges on direct taxes, as well as the inadequate outlay for bank recapitalisation.

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