#BUDGET 2020 withHDFCSEC

Relaxation or Taxation...

PRE-BUDGET EXPECTATIONS

Pre Budget Equity Strategy

The first full Budget from Modi 2.0 is due on February 01. Given the tight fiscal situation and slowing domestic growth, it would be a challenge for the FM to balance the two objectives and kick start growth. Also given the shadow of the global impact due to the coronavirus, the task of the FM has got a bit tougher. If the outbreak is contained soon, we may not see much disruption globally and on India; but if this elongates then we could see further challenging times and bolder steps (under pressure) after the Budget.

The Modi government is likely to deviate from its policy of fiscal consolidation for the first time in six years and may go for a higher fiscal deficit to boost growth in the budget on Feb 01. Given the fact that the first two years of any Govt sees the most reforms undertaken, it is normal to expect some path breaking announcements in the forthcoming Budget, though a lot can be done outside the Budget. The Govt needs to give a serious push to improve the business environment. One only hopes that the recent political reverses suffered by the ruling coalition does not bring down its enthusiasm to go whole hog on the reform path even if hurts some segments of population temporarily.

In the past FMs have tried to do too much in the Budgets and try to appease as many constituents as possible, with the result that we have seen revenue shortfall and expenditure that is constrained by smaller revenues and the Govt departments not having the time or scale to spend so much money. The FM should hence try to do less number of things which are for the overall good of the economy even if they temporarily impact some portions of the population. Main focus should be on increasing investments and raising productivity, though it could take time to show effect.

Given below are some of our thoughts ahead of the Budget.

Fiscal situation

For FY20, lower revenue collections and disinvestment proceeds (less than 20% of FY20E received so far) could be compensated by excess RBI dividend, expenditure cut in the last quarter and subsidy rollover. Date of receipt of Telecom AGR payments could impact FY20 or FY21 fiscal deficit. We expect FY20 to end with a fiscal deficit of 3.5-3.7% vs the original estimate of 3.3% of GDP. For FY21, fiscal deficit may be projected at 3.4-3.5% of GDP. Fiscal consolidation roadmap may be deferred by one more year. However given the effect of higher fiscal deficit on interest rates, ratings and capital markets, the FM may not budget too high fiscal deficits for FY20 and FY21.

Though economists hope for a cleanup of fiscal situation by bringing off balance sheet items (FCI, NHAI etc) on the books, it may not happen in this Budget.

Bond Yields

Bond yields could remain high for some time due to inflationary and fiscal pressures and large amount of G-sec maturity in the coming few years. Ongoing sluggish growth in revenues have raised the possibility of additional borrowings in Q4FY20. However if growth does not resume due to any reason including global events, the pressure on yields could reduce. However if the Govt taps the foreign borrowing route, it could reduce the pressure on domestic yields.

Economic growth

FY20 nominal growth could come in at 7.5% and real GDP @4.6-4.7%. For FY21 the numbers could be 10% and 5.3-5.5% respectively.

Some green shoots are visible including better finance availability and high festive sales. Agriculture output could also grow well given the high rabi sowing and sufficient water availability.

Scrappage policy for commercial vehicles may be announced with a staggered implementation and limited fiscal impact.

Personal tax rates

Though expectations have been built on a sharp cut in personal tax rates following corporate tax cut announced in Sept 2019, we think that two large giveaways in quick succession is hoping for too much. If at all, some tinkering of tax slabs may be possible which may put Rs.5,000-8,000 in the hands of tax payers. This may not revive consumption in a big way.

Long term capital gains on equities/equity MFs may be abolished (though the holding period may be extended to 2 years vs the current 1 year) as it has not resulted in any significant revenue while dampening the sentiments. Dividend distribution tax may be abolished, but recipients of dividend may be taxed on the whole of dividend received by them.

Infra spend

Infra spend (essentially capital spend) will grow in line with the growth in nominal GDP growth. A new scheme to replace the existing UDAY may be announced to improve power distribution, ensure power 24x7, reduce T&D losses and enforce discipline among state utilities.

Government may take incremental steps to revive real estate sector (because of its high multiplier effect on the economy) by expanding the definition of affordable housing, providing higher income tax deduction and improving liquidity to real estate players.

Rural / social spend

Incrementally no large allocations are expected. We need to spend the allocated monies well and increasingly focus more on human development (education, healthcare) giving other spend secondary importance.

Divestment/privatization

The FM may present a credible privatization program and asset monetisation plan. The Govt has to take some hard decisions regarding the ownership of even erstwhile ‘strategic’ PSU companies.

For FY21, divestment target of Rs.1.50 lac cr may be announced (compared to Rs.1.05 lac cr for FY20). This may be due to impending privatization of companies like Air India, BPCL, Concor etc.

Tax leakages

GST frauds may be termed as a non bailable offence. The Ministry of Finance is looking to expand its tax base in the Union Budget 2020-21 by plugging loopholes in the law, especially in areas of tax exemptions, input tax credits and concessional tax schemes.

Indirect taxes

Inverted duty structure may be rectified partly. Import duties may be hiked on some electronics, electrical goods, chemicals, handicrafts etc to protect domestic industries.

Steps to help banking/NBFC sectors to enable them to provide more credit to real estate, MSME and other sectors.

Lenders should be allowed a one-time restructuring of certain real estate loans – like projects stuck due to approvals or finance. A TARP like program (Troubled Assets Relief Program) could be introduced for restoring the flow of liquidity to the businesses and give an extension to lenders for recovery from select sectors. For 50 large NBFCs, Govt could defer principal repayments for a specified period.

PSU Insurance companies may need capital infusion for meeting solvency requirements which may be provided.

FDI limit relaxation

FDI limits may be hiked in some sectors including aviation (to 100%) to attract foreign investment.

Exports push

The recent retrospective withdrawal of Merchandise Exports India Scheme for textile exporters does not augur well for pushing exports. Govt should have stability in policies and incentivize labour intensive sectors to export more and to that extent some sops may be announced.

Budgets have lately become a non-event except for media and economists and its effect is worn off 2-3 days post the event. Markets may slide ahead of the Budget on apprehensions on Budget and also due to coronavirus scare. However post the announcement of the Budget, once the uncertainty is out, markets may bounce and rise towards the recent highs.

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