



Budget 2020

A Boost For Equities?

As with any budget, there will always be positives and negatives. However, in this budget, the negatives slightly outweigh the positives. In my view, the key problem we face is that of slowing growth, a challenging global environment, and low business confidence. It will be prudent for retail investor to invest in mutual funds offering equity funds in the mid-cap and small-cap space as a budget strategy.

On the day of the budget presentation on February 1, I was asked by *Khaleej Times* (a UAE-based newspaper) about my initial reaction and this is what I said:

“It is a budget high on speech time and low on delivery. As expected the budget reduced income tax burden on tax payers. However, this will leave more money in the pockets of tax payers; but will that result in increased consumption is a key question. Because the budget also removed 70 of 100 exemptions which can actually increase the tax paid. Good moves included removal of Dividend Distribution Tax (DDT) and increasing deposit insurance to 5 lakhs. But is that enough to accelerate investment and consumption cycle, I am not so sure. This budget focused heavily on agriculture and farmers at the cost of industry. In short the market was expecting a bold visionary budget

and what they got was a humble budget with no sense of urgency. I hope a detailed reading of the budget can change perspectives.”

Let us see if I have changed my perspective and more importantly focus on the impact of budget on the market.

Before we get into that question, let us look at the broad key proposals that this budget unveiled:

- Reduction in personal income-tax rates
- Abolition of DDT
- Increase in deposit insurance cover for banks from ₹1 lakh to ₹5 lakh
- Privatizing LIC
- Divestment target of ₹2.1 lakh cr

Among the sectors that benefitted include agriculture, infrastructure, transportation, banks, NBFC’s, and metals and mining. Agriculture seem to enjoy some special focus in this budget where government is targeting to

double farm income by 2022. It has increased the coverage on crop insurance and proposed to have robust warehouses and cold chain infrastructure to ensure better farm storage. The Kisan Rail project under PPP route is pro-

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posed for faster movement of perishable goods. The focus on infrastructure is also noticed especially in irrigation through Jal Jeevan Mission which aims to provide piped water supply to all households. The budget announce-

ments also include more allocation for roads, highways, railways, economic corridors, solar power generators, etc. More importantly Sovereign Wealth Funds (SWFs) that provide infrastructure financing will enjoy 100% tax exemption from interest, dividends and capital gains. Sectors negatively impacted included fertilizers, tobacco, insurance, Real estate (especially REITs) and capital goods (to some extent). The negative impact comes mainly through higher custom duties while for REITs, the abolition of DDT is also perceived negative. It is not the intention of this article to go into details of the budget proposals, but rather focus on how this will impact stock market. Let us see how the market reacted to this budget before and after.

Market performance during budget

I have presented the stock market reaction to the budget for this year and last year. We can see that in 2019 when Nirmala Sitharaman presented the budget, the market clearly gave a thumbs down with Nifty dropping from 11,947 to 11,553. However, in the 2020 budget, the market initially reacted negatively to the budget but in the next five days recovered smartly. The key questions then are: Why did the market react so negatively on the day of the budget and more importantly what caused the market to bounce back?

The negative reaction can be assessed mainly on the factor that the market was building huge expectations from the finance minister to provide a 'big-bang' budget and the finance minister also gave enough hints that there will be bold reforms. But none of that happened. One example of the big bang reform expectation was the abolition of long-term capital gains tax. Market was nearly hopeful that it will be abolished. While the government abolished the DDT for companies, what this means is that instead of companies, it

will be dividend recipients (individuals) that will now pay the tax at their applicable rates. While the government announced a new revised tax rates and slabs for personal income tax, it has also announced abolition of a slew of exemptions which are expected to increase the tax liability. The new tax regime is optional though. However, this is another area where the market was expecting some 'big-ticket' announcements and what they got was an ordinary deal. The market was also expecting some solid and strong support to the beleaguered real estate sector and infrastructure. Announcements in these



In my view, the key problem we face is that of slowing growth, a challenging global environment, and low business confidence. Due to this we are creating fewer jobs and companies are not investing enough (even though they have more cash now due to lower taxes).



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two areas were either status quo or cosmetic. Again no big bang announcements. The great privatization target has now become an annual joke with targets never achieved. LIC privatization ambition comes on the same heel. Privatizing a \$550 bn behemoth with huge NPA's can be definitely tricky. However, it will be also interesting to see what caused the bounce back. The main reason could be fall in oil price which provided huge relief to the economy. Our current account deficit reduced last year from 2.1 to 1.5% mainly due to lower imports and any reduction in oil price will be a great news on that front. Also, the manufacturing PMI touched an 8-year high which was not expected. Market saw great positives in credit guarantee for NBFC's and factoring support to MSME's, two sectors that

were seriously affected due to demonetization. As with any budget, there will always be positives and negatives. However, in this budget the negatives slightly outweigh the positives. In my view, the key problem we face is that of slowing growth, a challenging global environment, and low business confidence. Due to this we are creating fewer jobs and companies are not investing enough (even though they have more cash now due to lower taxes). Since the corporates are not yet ready to prop up the investment cycle, it is now left to retail individuals to augment growth through higher consumption. This budget did not put enough money in the hands of individuals to prop up consumption. India needs to accelerate the investment/consumption cycle in order to go back to 7 to 8% growth (from the current 4 to 5%) and create the needed jobs. While it is not a bad budget per se, it did miss an opportunity. Thankfully, this government is only in its 1st year of the new term and hopefully we can expect more in the coming years.

Opportunities do exist

As investors, there will always be plenty of stock picking opportunities in sectors that enjoyed favorable treatment in the budget (like footwear, cement, consumer durables, household appliances, mattresses, pipes, power, print media, solar pumps, etc.). It is observed that most of the stocks recommended by brokerage house post the budget fall in the mid and small cap segment with very few large cap names. Only few names like L&T, HDFC, and Tata Motors figure in the list of large caps. Given the volatility of mid and small cap stocks, and also given the fact that they had fallen in value steeply during the last two years, it will be prudent to invest in mutual funds offering equity funds in the mid cap and small cap space as a budget strategy.

Happy Investing! ■

Reference # 20M-2020-03-10-01