

# Note on Union Budget for FY 2015-2016

As on 28<sup>th</sup> February, 2015

Uday Kotak's Tweet: -

*“(There are) 5 Budget themes -*

- Infra Push,
  - Financial Savings,
  - Away from Cash, *(towards cashless society)*
  - Simpler Tax,
  - Higher Deficit = Interest rates drop slower.
- (Overall) Reasonable budget.”*

Nilesh Shah's views: -

***“Government is playing the game for a test victory while the market probably expected a T20 spectacle. The policy framework is being redesigned to transit India from command economy to co-operative federalism. This budget is seeking to create a unified market to generate and percolate overall growth by means of GST. The beneficial impact of budget on economy will be reflected over the next few quarters.”***

# KEY Highlights of the FY16 Budget



## ECONOMY

- Reversal of Inverted Duty Structure to benefit Manufacturing Sector
- GST roll out and National Market for Agriculture to create Unified Market. One Country One Market will benefit better tax collection and higher productivity. GST roll out can give boost to GDP growth in FY 17.
- Plug N Play mode of roll out for UMPP and other infrastructure projects can be a game changer. Investors will prefer fully approved projects which will help reduce the execution time significantly
- Proposal for a new Bankruptcy Code, if inline with the similar regulations (Chapter 11 regulation of USA) will help in NPA management for the banking sector and take the stress out of the stressed assets portfolio
- Refinancing for Micro Sector through Mudra bank and E Platform for SME funding will reduce the cost of borrowing for this sector.

## MARKET

- FMC AND SEBI merger to integrate commodity and capital markets.
- Changes in permanent establishment act to bring currently offshore fund management business to India. It can develop Mumbai as a regional financial center
- Changes in REITs on capital gains and pass-through of Rental income will help Real Estate sector
- FII have been permitted to invest in Alternate Investment Funds. Positive for the alternate investments especially in real estate sector
- Tax Free Infra Bonds and Gold Bonds will provide one more alternative to HNI Investors
- Merger of FPI and FDI limits will facilitate flows into India and ease constraint on investment in Banking Sector.

## KEY Highlights of the FY16 Budget

- Financial Savings will be encouraged as Incentives are given for contribution to New Pension Scheme 50,000 80 CCD ( Hopefully it will be extended to Mutual Fund retirement products also )
- Stricter penalty for Black Money, Limiting Cash transaction especially in investment in Real Estate , Making PAN card mandatory for purchase above Rs 1 Lacs and incentivizing Rupay Card usage will help increase financial savings

### Mutual Funds

- The increase in the service tax rate from 12.36% to 14% (plus educational cess) would increase the cost of operation for the mutual funds as the billing amount on various services is expected to rise.
- The Budget has also proposed for the inclusion of IFAs and Mutual Funds Distributors in the service tax net.

## DEBT MARKET

- Establishment of Public Debt Office will streamline Government's borrowing program. Mandating RBI to target inflation under a Monetary Policy Framework will move India at par with developed nations in Monetary Policy Management.
- Fiscal deficit at 3.9% of GDP for FY16 is ahead of expectations but Revenue Deficit at 2.8 % of GDP for FY16 will contain Net borrowing Program at Rs 4.56 lac crore .
- The Budget is likely to be Non inflationary in nature but RBI would like to wait for more confirmatory data before reducing policy rates.

## EQUITY MARKET

- Disinvestment target set at Rs 69,500 crore for 2015-16. There will be strategic divestment also. SUUTI stake as well as HZL and Balco stake sell possible.
- Corporate tax rate to be reduced from 30% to 25% over four years; deductions and exemptions to be rationalized. However, Corporate tax will go up in FY16 due to additional surcharge. Overall, the outlook is positive for corporate earnings.
- Finance minister has proposed to set up the National Investment and Infrastructure Fund with Rs 20,000 crore contribution. This can be leveraged and provided as equity for infrastructure development. At that, the Union Budget provides additional funds of Rs 70,000 crore for investment in infrastructure. These measures are likely to kick start the investment cycle.
- Increase in Service tax, excise duty on cigarettes and tobacco products to have stock specific impacts.

# FISCAL AGGREGATES – the Big Picture



- The FY16 fiscal deficit increased by only 8% against the FY15 estimates.
- 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.

Deficit Numbers (in Rs Billion)			
	FY14 (actuals)	FY15 (RE)	FY16 (BE)
Revenue Deficit	3570.48	3624.86	3944.72
	-3.1%	-2.9%	-2.8%
Effective Revenue I	2276.3	2305.88	2839.21
	-2.0%	-1.8%	-2.0%
Fiscal Deficit	5028.58	5126.28	5556.49
	-4.4%	-4.1%	-3.9%
Primary Deficit	1286.04	1012.74	995.04
	-1.1%	-0.8%	-0.7%

Glance at the Budget (In Billion Rupees)			
	FY14 (actuals)	FY15(RE)	FY16(BE)

## Receipts

1	Revenue Receipts	10147.24	11262.94	11415.75
2	Tax Revenue (net to centre)	8158.54	9084.63	9198.42
3	Non-Tax Revenue	1988.7	2178.31	2217.33

4	Capital Receipts (5+6+7)\$	5447.23	5548.64	6359.02
5	Recoveries of Loans	124.97	108.86	107.53
6	Other Receipts	293.68	313.5	695
7	Borrowings and other liabilities *	5028.58	5126.28	5556.49
8	<b>Total Receipts (1+4)\$</b>	<b>15594.47</b>	<b>16811.58</b>	<b>17774.77</b>

## Expenditures

9	<b>Non-Plan Expenditure</b>	<b>11061.2</b>	<b>12132.24</b>	<b>13122</b>
10	On Revenue Account	10190.4	11218.97	12060.27
	of which,			
11	Interest Payments	3742.54	4113.54	4561.45
12	On Capital Account	870.8	913.27	1061.73
13	<b>Plan Expenditure</b>	<b>4533.27</b>	<b>4679.34</b>	<b>4652.77</b>
14	On Revenue Account	3527.32	3668.83	3300.2
15	On Capital Account	1005.95	1010.51	1352.57
16	<b>Total Expenditure (9+13)</b>	<b>15594.47</b>	<b>16811.58</b>	<b>17774.77</b>

# Exemptions in the Personal Tax



the mathematics behind this exemption:

Under Head's	In Rs amount
Deduction u/s 80C	Rs 150,000
• Deduction u/s 80CCD	Rs 50,000
• Deduction on account of interest on house property loan (Self occupied property)	Rs 200,000
• Deduction u/s 80D on health insurance premium	Rs 25,000
• Exemption of transport allowance	<u>Rs 19,200</u>
Total	Rs 4,44,200

- Finance Minister has placed the gross borrowings at around Rs 6 Lakh crores, while the net borrowings is estimated at around Rs 456,000 crs.
- This borrowing figure is largely at similar levels last year. On that account, the demand supply equation provides reasons to believe that the interest rate environment is set for a gradual softening in yields.
- However, the quality of fiscal deficit is dependent on around Rs 69500 cr disinvestment (vis-a-vis the Rs 30,000 crore disinvestment in FY15 ) and around 15.83% (gross) tax buoyancy. So the fruition of these assumptions is necessary to maintain the quality of the fiscal deficit.
- We believe that the FM has relaxed the FRBM norm this year to create additional fiscal space for investment in infrastructure. So, while the re-evaluation of the fiscal deficit to 3.9% may seem disappointing, the investments would free-up supply bottlenecks and support growth.
- RBI has been given ample headroom by the Finance minister while balancing the political, fiscal and growth exigencies.
  - Therefore, we believe that RBI would continue to remain on path of monetary easing and additional rate cuts in around the April monetary policy may be possible.
  - Overall, there may be room for additional 50-75 bps rate cut in the next fiscal year.
- We recommend investors to grab duration for capital appreciation through Kotak Bond Fund and Kotak Gilt Fund.
- Investors can also choose Kotak Income Opportunities and Kotak Medium Term Plan for carry .



## Equity - View & Outlook



- The Budget is pro Growth, pro Investment and pro Job creation
- The Budget is supporting low inflation through fiscal consolidation ( albeit a year delayed ) , Growth through enhanced spending on Infrastructure and encouraging higher savings and investment through incentives for financial savings
- FII will find the Inflation targeting and fiscal consolidation theme attractive. We expect FII flows to remain strong in FY 16.
- Corporate earnings will get supported by higher capacity utilisation, lower commodity prices, reduced working capital cycle and lower interest rates over the next eight quarters. We expect earnings growth to be back ended with more sharper acceleration in FY 17.
- Indian Market is trading at a fair valuation. It is trading at around the historical average valuation of 23.8 P E (trailing) ratio and 3.8 (trailing) times PB . The market cap to GDP ratio is at 73% (1 year forward)
- India is relatively better valued among its peer of Russia, Brazil China, South Africa, Indonesia, and Turkey
- Large cap and mid cap valuations are at similar level and hence we prefer large cap stocks in this allocation
- We recommend Kotak Select Focus and Kotak 50 for general equity exposure
- For the purpose of investment in midcap segment, we recommend Kotak Emerging equity but through the SIP mechanism to mitigate short term volatility.
- For investors seeking to ride the infra play, investments in the Kotak Infrastructure and Economic reform fund is recommended.

- Assuming an agnostic perspective on risk, the following recommendations can be prescribed:-
  - Around half the money in SIP
  - The rest of the corpus can be placed aside for event related volatility, such as:
    - A possible Greece exit or similar global turbulence
    - A possible US fed rate hike
    - Any commodity price spike
    - Earnings disappointment creating a correction in market
- In the absence of significant event risk, one can look at fresh issuance opportunities with attractive valuations in
  - IPO, OFS and FPO or LAUNCH OF PSU ETF (like in Feb 2014)

## Investment Play through Mutual Funds







Investment Play	Funds
Duration play	Kotak Gilt / Kotak Bond Fund
Carry Play	Kotak Medium Term Plan / Kotak Income Opportunities Fund
large cap	Kotak Select Focus and/or Kotak 50
Infrastructure revival	Kotak Infrastructure and Economic Reform Fund
Through SIP	Kotak Emerging Equities Fund
short term parking of funds	Kotak Equity Arbitrage Fund

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# Product Labeling



Name of Scheme	Type of Scheme	Scheme Re-opened on	This product is suitable for investors who are seeking*
Kotak Mahindra 50 Unit Scheme	An open ended equity scheme	January 21, 1999	<ul style="list-style-type: none"> <li>• Long term capital growth</li> <li>• Investment in portfolio of predominantly equity &amp; equity related securities</li> <li>• High risk  (Brown)</li> </ul>
Kotak Mahindra Balance Unit Scheme 99	An open ended balanced scheme	November 29, 1999	<ul style="list-style-type: none"> <li>• Long term capital growth</li> <li>• Investment in equity &amp; equity related securities balanced with income generation by investing in debt &amp; money market instruments</li> <li>• High risk.  (Brown)</li> </ul>
Kotak Equity Arbitrage Scheme	An open ended equity growth scheme	October 3, 2005	<ul style="list-style-type: none"> <li>• Income from arbitrage opportunities in the equity market</li> <li>• Investment in arbitrage opportunities in the cash &amp; derivatives segment of the equity market</li> <li>• Low risk.  (Blue)</li> </ul>
Kotak Medium Term Plan	An Open ended Debt Scheme	March 28 <sup>th</sup> , 2014	<ul style="list-style-type: none"> <li>• Income over a medium term investment horizon</li> <li>• Investment in debt, government securities &amp; money market instruments with a portfolio weighted average maturity between 3-7 years</li> <li>• Low risk.  (Blue)</li> </ul>










## Product Labeling






Kotak Select Focus Fund	An open ended equity scheme	September 11, 2009	<ul style="list-style-type: none"> <li>• Long term capital growth</li> <li>• Investment in portfolio of predominantly equity &amp; equity related securities generally focussed on a few selected sectors</li> <li>• High risk  (Brown)</li> </ul>
Kotak Emerging Equity Scheme	An open ended equity growth scheme	Scheme converted to an open ended scheme on: March 31, 2010	<ul style="list-style-type: none"> <li>• Long term capital growth</li> <li>• Investment in equity &amp; equity related securities predominantly in mid &amp; small cap companies</li> <li>• High risk.  (Brown)</li> </ul>
Kotak Infrastructure & Economic Reform Fund <i>(formerly known as “PineBridge Infrastructure &amp; Economic Reform Fund”)</i>	An open ended equity scheme	February 27, 2008	<ul style="list-style-type: none"> <li>• long term capital growth</li> <li>• long term capital appreciation by investing in equity and equity related instruments of companies contributing to infrastructure and economic development of India</li> <li>• High risk.  (Brown)</li> </ul>

# Product Labeling



Name of the Scheme	Type of the Scheme	Scheme reopened on	Name	This product is suitable for investors
Kotak Mahindra Gilt Unit Scheme – 98 Investment Plan	An open ended dedicated Gilt Scheme	January 5, 1999	Kotak Mahindra Gilt Unit Scheme - 98 Investment Plan	<ul style="list-style-type: none"> <li>Income over a long investment horizon</li> <li>Investment in sovereign securities issued by the Central and/or State Government(s) and/or reverse repos in such securities</li> <li>Low risk  (Blue)</li> </ul>
Kotak Mahindra Bond Unit Scheme 99	An Open Ended Debt Scheme	November 29, 1999	Kotak Bond	<ul style="list-style-type: none"> <li>Income over a long investment horizon</li> <li>Investment in debt &amp; money market securities</li> <li>Low risk  (Blue)</li> </ul>
Kotak Mahindra Liquid Scheme	An Open Ended Debt Scheme	October 6, 2000	Kotak Liquid	<ul style="list-style-type: none"> <li>Income over a short term investment horizon</li> <li>Investment in debt &amp; money market securities</li> <li>Low risk  (Blue)</li> </ul>
Kotak Bond Short Term Plan	An Open Ended Debt Scheme	May 3, 2002	Kotak Bond Short Term Plan	<ul style="list-style-type: none"> <li>Income over a medium term investment horizon</li> <li>Investment in debt &amp; money market securities</li> <li>Low risk  (Blue)</li> </ul>
Kotak Floater Short Term Scheme	An Open Ended Debt Scheme	July 15, 2003	Kotak Floater ST	<ul style="list-style-type: none"> <li>Income over a short term investment horizon</li> <li>Investment in floating rate securities, debt &amp; money market securities</li> <li>Low risk  (Blue)</li> </ul>
Kotak Floater Long Term Scheme	An Open Ended Debt Scheme	August 13, 2004	Kotak Floater LT	<ul style="list-style-type: none"> <li>Income over a short term investment horizon</li> <li>Investment in debt &amp; money market securities</li> <li>Low risk  (Blue)</li> </ul>
Kotak Flexi Debt Scheme	An Open Ended Debt Scheme	December 6, 2004	Kotak Flexi Debt	<ul style="list-style-type: none"> <li>Income over a medium term investment horizon</li> <li>Investment in debt &amp; money market securities</li> <li>Low risk  (Blue)</li> </ul>
Kotak Income Opportunities Fund	An Open Ended Debt Scheme	May 12, 2010	Kotak Income Opportunities	<ul style="list-style-type: none"> <li>Income over a medium term investment horizon</li> <li>Investment in debt &amp; money market securities</li> <li>Low risk  (Blue)</li> </ul>
Kotak Banking and PSU Debt Fund	An Open Ended Debt Scheme	Kotak Mahindra Gilt Savings Scheme – 98 – Savings Plan has been converted into Kotak Banking and PSU Debt Fund on August 14, 2013.	Kotak Banking and PSU Debt Fund	<ul style="list-style-type: none"> <li>Income over a short to medium term investment horizon</li> <li>Investment in debt &amp; money market securities of PSUs, Banks &amp; government securities</li> <li>Low risk  (BLUE)</li> </ul>

\* Investors should consult their financial advisers if in doubt about whether the product is suitable for them. Note: Risk may be represented as:

Investors understand that their principal will be at Low Risk  (Blue), Investors understand that that their principal will be at Medium Risk  (Yellow), Investors understands that their principal will be at High Risk  (Brown)