

# THE UNION BUDGET 2010-11

## Implications of Direct Tax Changes and Impact on Capital Market

by

**Prof. Kanu H. Doshi**

**Miss Divya Vasantharajan**



**FORUM**  
OF FREE ENTERPRISE

*"Free Enterprise was born with man and shall survive as long as man survives".*

- **A. D. Shroff**  
Founder-President  
Forum of Free Enterprise

## INTRODUCTION

The budget 2010-11 has been scripted against a fortuitous backdrop of a remarkable turnaround in the economy – the estimated healthy 7.2% real GDP growth; more commendable industrial resurgence with a double digit growth rate; corporate profitability regaining its lost ground; exports gradually recovering; business confidence progressively improving; the surge in Sensex over the year restoring substantial fortunes of investors, even after factoring in the recent volatility; rising foreign capital inflows; and capital investments gaining momentum; and all these and more.

Contrast this scenario with tough times that are still ordained for almost all the advanced countries of the world. The economic recovery for these countries continues to be in a slow and hesitant mode; and there are still fears of “double-dip” recession. Even at home, there are also several formidable concerns, especially about (a) stubbornly high food inflation, and (b) unsustainably high revenue and fiscal deficits, and consequential rising indebtedness. Given such complex mixed scenario, the FM seems to be striving for a virtuous cycle essentially driven by five main forces:

First, the four-pronged strategy for agricultural resurgence; second, providing distinctive focus on rural development through significantly higher public spending allocations, as an integral part of “inclusive” development strategy; third, the thrust on infrastructure investment which has received as much as 46% (or Rs.173,552 crores) of total central plan allocations; fourth, expanding scope and content of financial allocations for the social sector (education, health, welfare of

the deprived sections of the society) and the last by giving a thrust on tax reforms mainly through the roll-out of the Direct Tax Code (DTC) and General Sales Tax (GST) in the current year.

This well-meaning strategy might encounter many challenges in its successful implementation. Thus we are sceptical about coordination and cohesion among coalition partners; would the F. M. be able to handle the tasks within an acceptable time-frame? Or else, the neat strategy will be untidily rolled over, as has been the case of critical reforms agenda for the past many years! Like-wise, India can not afford to be complacent about the prospect of global economic recovery since it continues to be shrouded in uncertainty (e.g. recent developments in Greece and the EU).

The success of the budgetary strategy would also be determined by some key risk factors, namely, the probability of (a) agricultural resurgence – next normal monsoon (?); inflationary cycle – manufacturing inflation replacing food inflation - or cost push measures (?); rising interest rates and gradual tightening of liquidity (?); exchange rate behaviour - the shape of capital inflows. It is imperative also to watch out the impact of "exit policy"; and all the key efforts to bring about fiscal consolidation.

In the meantime, we are pleased to present on behalf of the FORUM two very insightful articles: the first by Mr. Kanu Doshi, Chartered Accountant and tax expert, on salient features and implications of direct tax changes in the budget; and second by Ms. Divya Vasantharajan, financial analyst, on the impact of the budget on capital market.

Mr. Kanu Doshi concludes his analysis on optimistic notes by stating that "this Budget will go a long way in encouraging savings and spending ....." and that "capital market should also remain bullish with Sensex scaling new highs during the year ....". Ms. Divya Vasantharajan from her sectoral impact analysis also ends with very positive futuristic perspective and observes that "we have some of the most learned minds at the helm of our polity and bureaucracy, we can hope to see more calibrated efforts directed to steering India towards the very coveted double-digit growth".

We are confident that our avid readers will greatly benefit from the expert opinions of these two separate articles in this booklet.

**Sunil S. Bhandare**  
Editor

# THE UNION BUDGET 2010-11

## I

### The Budget is for Khas Admi

by

**Prof. Kanu H. Doshi\***

#### INTRODUCTION TO DIRECT TAXES:

The Budget presented by Finance Minister on 26th February, and passed by the parliament is for KHAS ADMI and not for AAM ADMI. KHAS Admi is a taxpayer. KHAS Admi is an Investor. There is therefore a refreshing change this year that for the first time the Union Budget has been designed to address the woes of middle class with modest taxable incomes. Accordingly, the F.M. has calibrated the tax slabs in a manner which leaves the taxpayer with a larger after tax income than ever in the past.

#### TAX RATES

Rates for Individuals, HUFs, AOPs and BOIs for assessment year 2011-2012:

The threshold limit of basic exemption has not been raised. However, there is substantial scaling up of the slabs of income for determining rate of tax.

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The new slabs are as under:

Total Income Slab	TAX RATES		
	Resident senior citizens	Resident women Below 65 years of age	Others
Up to Rs.1,60,000	NIL	NIL	NIL
Rs. 1,60,001 to 1,90,000	NIL	NIL	10%
Rs. 1,90,001 to 2,40,000	NIL	10%	10%
Rs. 2,40,001 to 5,00,000	10%	10%	10%
Rs. 5,00,001 to 8,00,000	20%	20%	20%
Above Rs. 8,00,000	30%	30%	30%

Tax saving for the assesseees (including women and senior citizens) at various levels of total income as under:

Tax (including Cess) for

Taxable Income Rs.	Resident senior citizens		Resident women below 65 years		Others		Saving for all in Rs.
	AY	AY	AY	A	AY	AY	
	2010-11	2011-12	2010-11	2011-12	2010-11	2011-12	
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
300000	6180	6180	11330	11330	14420	14420	0
400000	26780	16480	31930	21630	35020	24720	10300
500000	47380	26780	52530	31930	55620	35020	20600
600000	78280	47380	83430	52530	86520	55620	30900
700000	109180	67980	114330	73130	117420	76220	41200
800000	140080	88580	145230	93730	148320	96820	51500
900000	170980	119480	176130	124630	179220	127720	51500
1000000	201880	150380	207030	155530	210120	158620	51500

- For all other assesseees there is no change in the tax rates.
- Surcharge continues to be applicable only to domestic companies and foreign companies where the total

income exceeds Rs 1 crore. However for domestic companies the surcharge is reduced from 10% to 7.5%.

- Additional surcharge at 3% called "Education Cess" and "Secondary and Higher Education Cess" for all assesseees remain unaltered.

### **NEW SECTION 80CCF: DEDUCTION of Rs. 20,000:**

Budget 2010 through a new section 80CCF in the Income Tax Act, has granted an additional deduction of Rs. 20,000 from the gross total income if the assesseees (Individuals & HUF) were to contribute to Infrastructure Bonds (to be notified by Central Government) during the year. This is a welcome tax incentive to garner long term funds for Infrastructure investments

This deduction is over and above the existing aggregate deduction under section 80C of Rs. 1,00,000 available for contributions to EPF, PPF, LIP, ULIPs, ELSS, NSC VIII, repayment of Housing loans, School fees of children, etc.

### **MINIMUM ALTERNATE TAX (MAT) - SECTION 115JB**

The rate of MAT is increased from 15% to 18%. The MAT rate is effectively now 19.9305%, as against the earlier rate of 16.995% (for companies with book profit exceeding Rs. 1 crore). Carry forward and set off of MAT credit for ten years continue as before.

### **CONVERSION OF A PRIVATE COMPANY OR AN UNLISTED PUBLIC COMPANY INTO A LIMITED LIABILITY PARTNERSHIP - SECTIONS 32(1), 35DDA(4A), 43, 47, 47A, 49, 72A and 115JAA**

Under Limited Liability Partnership Act, 2008 (LLP Act) a

private company or an unlisted public company may be converted into a limited liability partnership (LLP). Amendments have been made for dealing with such conversion. Similarly, a private company may also get converted to LLP without attracting any capital gains tax.

### **(i) Capital Gain - Sections 47, 47A & 49**

Clause (xiib) has been inserted in Section 47 providing that conversion of a private company or an unlisted public company in to an LLP in accordance with Sections 56 and 57 of the LLP Act will not be regarded as a transfer, if the following conditions are fulfilled:

- (a) All the assets and liabilities of the company become the assets and liabilities of the LLP.
- (b) All the shareholders of the company become the partners of the LLP and their profit sharing ratio and the capital contribution in the LLP are in the same proportion as their shareholding in the company on the date of conversion.
- (c) Shareholders of the company do not receive any consideration or benefit, directly or indirectly, other than share in the profit and capital contribution in the LLP.
- (d) For a period of at least five years from the date of conversion, the erstwhile shareholders of the company in aggregate are entitled to at least 50% of the profits of the LLP.
- (e) The total sales, turnover or gross receipts in the business of the company in any of the three years preceding the year of conversion do not exceed Rs. 60 lakh.

(f) For a period of three years from the date of conversion, the accumulated profits of the company on the date of conversion are not paid to any partner of the LLP, whether directly or indirectly.

Consequential amendment is made in Section 49, to provide that cost of acquisition of the capital assets acquired by the LLP in the process of conversion shall be deemed to be the cost for which the converted company had acquired the assets.

Further, sub-Section (4) has been inserted in Section 47A providing that if any of the conditions in (a) to (f) above are not complied with, then the profits arising from transfer of capital assets or intangible assets on conversion of the company to the LLP not charged under Section 45 shall be taxed in the hands of the LLP in the year in which the conditions are violated.

#### **(ii) Business Income - Sections 32(1), 35DDA(4A) & 43**

The fifth proviso to Section 32(1) has been amended to provide that the aggregate depreciation allowable to the converted company and the LLP shall not exceed the depreciation allowable, had the conversion not taken place. Such depreciation shall be apportioned between the two entities in the ratio of the number of days for which the assets were used by them.

The provisions of Section 35DDA have been amended to provide that the balance deduction in respect of expenditure incurred on voluntary retirement scheme allowable to the converted company will be allowable to the LLP from the previous year in which the conversion takes place.

Explanation 2C has been introduced in Section 43(6) to provide that the actual cost of the block of assets, in the hands of the LLP, shall be the written down value of the said block of assets in the hands of the converted company as on the date of conversion. Further, explanation 13 to Section 43(1) has been amended to provide that the actual cost of any capital asset in the hands of the LLP will be taken as nil, in case deduction for the entire cost of the said asset has been allowed under Section 35AD in the hands of the converted company.

#### **(iii) Carry Forward and Setoff of Losses - Section 72A**

Section 72A provides for carry forward and set off of the accumulated losses and unabsorbed depreciation of predecessor assessee in the hands of the successor assessee in certain cases of succession. The cases of succession presently covered by the provisions of Section 72A are conversion of a firm or a proprietary concern into a company and amalgamations and demergers of companies. This section is amended so as to include within its scope also the conversion of a private company or of an unlisted public company into an LLP.

#### **(iv) MAT Credit - Section 115JAA**

Sec. 115JAA has been amended to provide that the MAT credit of the converted company will not be permitted to be carried forward by the LLP, irrespective of whether the exemption under Sec.47(xiii b) has been availed of or not.

#### **WEIGHTED DEDUCTION FOR EXPENDITURE ON SCIENTIFIC RESEARCH - SECTION 35(1)(ii), 35(2AA) & 35(2AB)**

Weighted deduction of 125% allowable under Section

35(1)(ii) in respect of sums paid to a specified scientific research association, or to a university, college, or other institution, which is notified and approved, to be used for scientific research, has been increased to 175% of the sums paid.

Similarly, payments to a National Laboratory, university or Indian Institute of Technology in respect of approved programmes of scientific research will also be eligible for weighted deduction of 175% of the sums paid under Section 35(2AA) as against 125% available presently.

Weighted deduction of 150% under Section 35(2AB) allowable to companies engaged in the business of biotechnology or in any business of manufacturing articles or things, not being items mentioned in the Eleventh Schedule, in respect of scientific research expenditure (excluding cost of land or building) on an approved in-house research and development facility has now been increased to 200%.

### **APPROVED RESEARCH ASSOCIATIONS - SECTIONS 35(1)(iii), 10(21) & 80GGA**

Weighted deduction of 125% in respect of contribution for research in social science or statistical research under Section 35(1)(iii) which was hitherto available only in respect of sums paid to an approved university, college or institution, will now also be available in respect of sums paid to approved research associations carrying on research in social science or statistical research.

Presently, deduction under Section 80GGA is available to donations made to approved scientific research

associations. The said section has been amended to extend the deduction in respect of donations to approved research associations which have as their objects undertaking of research in social science or statistical research. Any income of a scientific research association approved under Section 35(1)(ii) is presently exempt from tax under Section 10(21). The exemption is now also extended to associations engaged in research in social science or statistical research covered under section 35(i)(iii).

### **RELAXATION IN PROVISIONS RELATING TO DISALLOWANCE OF EXPENDITURE WHERE TAX IS NOT DEDUCTED AT SOURCE - SECTION 40(a)(ia)**

Presently, in respect of any interest, commission, rent, royalty etc., if an assessee does not deduct tax at source or after deducting does not pay the tax so deducted within the stipulated time limit, the relevant expenditure is disallowed under Section 40(a)(ia). The stipulated time limit is March 31 of the previous year in cases where tax is deductible during the months of April to February in a given previous year and it is the due date of filing the return of income in cases where tax is deductible during the month of March.

The section is now amended to provide that the stipulated time limit for the relevant expenditure to be allowable shall be the due date of filing the return of income irrespective of the month in which the tax was deductible during the relevant previous year.

It is further provided that if tax is deducted and paid in any subsequent year or if it has been deducted in the previous

year but is paid in any subsequent year after the due date of filing the return of income, then the deduction for the relevant expenditure shall be granted in such subsequent year of payment.

The above amendments are introduced with effect from assessment year 2010-11.

### **DEDUCTION IN RESPECT OF CAPITAL EXPENDITURE OF CERTAIN NEW HOTELS - SECTIONS 35AD & 80A**

Presently, deduction under Section 35AD is allowed in respect of capital expenditure incurred during the year wholly and exclusively for a specified business subject to fulfillment of certain conditions. The definition of 'specified business' in Section 35AD(8) has been enlarged to include within its purview the business of building and operating a new hotel of two-star or above category anywhere in India which starts functioning on or after 1st April, 2010.

It has further been provided that if deduction is claimed and allowed in respect of capital expenditure of specified business under Section 35AD for any assessment year then no deduction would be available under Chapter VI-A in any assessment year.

Simultaneously, Sub-section 7 has been inserted in Section 80A to provide that if deduction is granted under any of the provisions of Part C of Chapter VI-A dealing with 'Deductions in respect of certain incomes', in respect of business of building and operating a new hotel referred in Section 35AD(8), then the assessee shall not be granted deduction under Section 35AD in respect of such business.

### **INCREASE IN THRESHOLD LIMIT OF TURNOVER ETC. FOR THE PURPOSE OF TAX AUDIT - SECTION 44AB**

The threshold limit of total sales/turnover/gross receipts for the purpose of audit of accounts under Section 44AB in the case of persons carrying on business has been increased from Rs. 40 lakh to Rs. 60 lakh. Similarly, the threshold limit of gross receipts in the case of persons carrying on profession has been increased from Rs. 10 lakh to Rs. 15 lakh. The earlier limits were originally fixed by the Finance Act, 1984 with effect from assessment year 1985-86 by the same Finance Minister.

### **TAXATION OF GIFTS - SECTION 56(2)(vii) & (viiia)**

Finance (No. 2) Act, 2009 had inserted clause (vii) in Section 56(2) with effect from 1st October, 2009 under which any sum of money received without consideration or any specified property (including immovable property) received without consideration or for inadequate consideration by an individual or HUF is taxable as income. In case of immovable property the taxability was determined with reference to the stamp duty value of such property. Prior to 1st October, 2009, Section 56(2)(vi) was applicable only to any sum of money received without consideration.

It is now provided that the clause (vii) would apply only where the immovable property is received without any consideration and will not apply to a transaction where the immovable property is received for inadequate consideration. The amendment is effective from 1<sup>st</sup> October 2009 and thus receipt of immovable property for inadequate consideration will not get covered within the ambit of the

provision from inception. It effectively means that only gift of immovable property without any consideration will fall under the mischief of this provision.

Bullion is now added to the list of specified non-monetary movable assets covered within the ambit of the above clause with effect from 1st June 2010.

Further, it is provided that only such property (whether movable or immovable) which is in the nature of capital assets would be covered by this clause. Hence, the clause will not apply to stock-in trade, raw material, consumable stores or any other trading assets. This amendment restricting the application of the clause to only capital assets is also effective from inception of the clause, i.e. from 1st October 2009. Presently, Section 56(2)(vii) is applicable only to individuals and HUFs. However, a new clause (viiia) is inserted with effect from 1st June, 2010 to provide that a firm (which includes LLPs) or a company, not being a company in which the public are substantially interested (closely held company), would be liable to tax, if shares of a closely held company are received by such a firm or a closely held company without consideration or for inadequate consideration. The clause will not apply where such shares are received in certain specified transactions arising out of business reorganization, amalgamation and demerger that are not regarded as transfer under clauses (via), (vic), (vicb), (vid) and (vii) of Section 47.

Consequential amendments are made in Sec.2(24) to include the value of such shares in the definition of income and in Section 49(4) to provide that the cost of acquisition of such shares will be the value which has been subjected to tax as above.

## **REFERENCE TO VALUATION OFFICER - SECTION 142A**

The power to make reference to the Valuation Officer for making an estimate of the fair market value of any investment, bullion, property, other valuables referred to in Sec. 69, 69A or 69B is further extended for estimating fair market value of the property referred to in Sec.56(2) of the Act.

This amendment is effective from 1st July, 2010.

## **DEDUCTION FOR INVESTMENT IN INFRASTRUCTURE BONDS - SECTION 80CCF**

New Section 80CCF has been inserted to provide for deduction up to Rs. 20,000 for investment made in long-term infrastructure bonds to be notified by the Central Government. This deduction is in addition to the deduction of Rs. 1 lakh under Section 80C etc.

## **PERIOD OF COMPLETION FOR HOUSING PROJECTS - SECTION 80-IB(10)**

Under Section 80-IB deduction is available in respect of profits derived from developing housing projects if the project is completed within a period of 4 years from the end of the financial year in which the project was approved. In respect of projects approved after 31st March 2005, the period within which the project may be completed, is being extended to 5 years from the end of the financial year in which the project was approved.

Further, the built-up area for shops and other commercial establishments in the project can now be 3% of the aggregate built up area or 5,000 sq. ft, whichever is higher. Presently, the limit is 5% or 2,000 sq. ft, whichever is lower. The Explanatory Memorandum to the Finance Bill states

that this benefit will be available to projects approved after 31st March, 2005 which are pending for completion in respect of the income relating to assessment 2010-11 and subsequent years.

These amendments are effective from assessment year 2010-11.

### **INCREASE IN THRESHOLD LIMITS FOR TDS - SECTIONS 194B, 194BB, 194C, 194D, 194H, 194I & 194J**

The threshold limits for deduction of tax at source are increased as under:

Section	Nature of Payment	Existing threshold limit of payment (Rupees)	New Threshold limit of Payment (Rupees)
194B	Winnings from lottery or crossword puzzle	5,000	10,000
194BB	Winnings from horse race	2,500	5,000
194C	Payment to contractors	20,000 (for a single transaction)	30,000 (for a single transaction)
		50,000 (for aggregate of transactions during financial year)	75,000 (for aggregate of transactions during financial year)
194D	Insurance commission	5,000	20,000
194H	Commission or Brokerage	2,500	5,000
194-I	Rent	1,20,000	1,80,000
194J	Fees for Professional or technical services	20,000	30,000

The above amendments are effective from 1st July 2010.

### **CERTIFICATE FOR TAX DEDUCTION/COLLECTION-SECTIONS 203 & 206C**

With the computerization in the income-tax department, it was proposed to dispense with the requirement to issue physical TDS/TCS certificates. Accordingly, deductor/collector of tax was not required to furnish certificates for deduction of tax at source or collection of tax at source from 1st April, 2010 under the existing provisions.

The practice of furnishing TDS/TCS certificate by the deductor/collector will now continue even after 1st April, 2010.

### **PENALTY FOR FAILURE TO GET ACCOUNTS AUDITED - SECTION 271B**

Presently, any person, who fails to get accounts audited or to furnish audit report as required under Section 44AB, is liable to pay penalty of ½% of the total sales, turnover or gross receipts subject to a maximum penalty of Rs. 1,00,000.

Maximum penalty leviable is now enhanced to Rs. 1,50,000.

### **ALLOTMENT OF DOCUMENT IDENTIFICATION NUMBER - SECTION 282B**

Every Income Tax authority was required to allot a computer generated Document Identification Number (DIN) in respect of every notice, order, letter or any correspondence issued by him/received by him to/from any other Income Tax authority or to/from assesseees or to/ from any other person, effective from 1st October, 2010.

The implementation of this provision is now postponed to 1st July, 2011.

#### **CONCLUSION:**

As stated at the outset, this Budget will go a long way in encouraging savings and spending, by the citizens. Consumer spending triggered by tax savings through reduced tax burden across the board will have multiplier effect on the trade and industry. Capital market should also remain bullish with Sensex scaling new highs during the year creating favorable climate for massive disinvestment of PSU shares to generate about Rs. 40,000 crores as estimated by the Finance Minister.

## **II**

### **Impact on the capital Market**

by

**Miss Divya Vasantharajan\***

The recent global financial crisis feared as a replay of the Great Depression of the 30s came under control thanks to the drastic and in strong support lent to the financial institutions of the world. The financial markets of emerging economies brought in a thrust of fresh foreign capital. Smaller economies almost defaulted on sovereign debt, while giants were cut to size.

2010-11 dawned as a year of hope and optimism, especially after the financial damage to the global economy in two earlier years. In India, we suffered during the turmoil to the extent of our exposure to complex foreign instruments. Corporates did suffer a slump in business and growth slowed but, it was better than most other economies and kept the "emerging markets" story exciting. Foreign Institutional Investments (FIIs) (till March 10th 2010) aggregated to \$23 billion which led to the stock market buoyancy with Sensex moving from 9000 to 17500 in May, 2010.

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There were anxieties like: a rollback of the government stimulus to corporates marginal increase in individual corporate taxation to reduce the fiscal deficit, curtailment in the allocation of funds for crucial sectors.

However, Finance Minister Mukherjee did surprise us on the tax giveaways and stressed the need for fiscal prudence in the budget. Overall, a good budget that will do what it could in the current cautious environment.

### **KEY NOTES FROM THE BUDGET**

1. Clear indication to introduce of the Direct Tax Code (DTC) and the Goods & Service Tax (GST) from April 2011 shows the Government's seriousness to simplify tax.
2. RBI to look into providing new private banks licenses; to ensure better services, better outreach, and faster growth in an underpenetrated financial services sector.
3. Attention to infrastructural development within the country.
4. The advance estimates for GDP growth for 2009-10 at 7.2%.
5. Number of steps taken to simplify the FDI regime.
6. Apex Financial Stability and Development Council to strengthen and institutionalize the mechanism for financial stability.

### **PERSONAL TAXES**

India's strength is her youthful, consumption crazy population. Accordingly, the Budget changes in the direct

tax slab rates would increase disposable income by Rs 500001- per annum across the board.

### **SCOPE OF THIS WRITE UP**

This write up seeks to highlight the effect of the Budget on various sectors of the Economy.

### **AGRICULTURE, TEXTILES & AGRO INDUSTRIES**

Agriculturalists have little to cheer about from this budget except the extension of the credit period to farmers. The sector has failed to garner attention to its core issues: fragmented land, ignorance of better farming technology & financing options and lack of bargaining power to improve earnings. The solution can be contractual farming by corporates - like fertilizer or irrigation companies; as in Punjab, where farmers are grouped and farmlands are worked on as one large landmass on the lines of the co-operative set-up of the milk producers under the AMUL in Gujarat. Relationship between the corporates with a bargaining power and the means to provide financial and technological support and farmers is the path for growth in this sector. The higher prices for agricultural products would incentivize the farmers to increase investments in the quality seeds and fertilizers.

The Indian textile industry largely depends on the demand from US and UK. In the current year, this demand has picked up. Forex loss due to the downward movement in the value of the rupee against the US dollar is a vital factor. Exporters struggle to secure profitable orders due to unorganized domestic competition and lack of more sophisticated currency hedging practices among industry

players. Some firms have ventured into retail chains which have added to their rental and lease outflows and hence, form an impediment to attain reasonable profit margins.

## **BANKS & FINANCIAL INSTITUTIONS**

The global financial crisis proved to all critics of the Indian banking system that caution always pays over recklessness in the guise of liberalization. While globally banks buckled under the strain of leveraged balance sheets, Indian banks not only stood tall but also took several leaps forward in adding to their consolidated presence across the country. PSU banks during last two years are the largest campus recruiters of MBAs, adding a taskforce of nearly 30000 new recruits mostly in the area of retail banking.

Budget has maintained its focus on sustaining inclusive growth and financial consolidation in promising sectors. Reference to licensing of private banks being scrutinized in the speech sent two strong messages to the banking community. The existing PSU players are forewarned to spruce up their operations to face oncoming competition from large private players known for their speed, aggression, and process efficiencies. Newcomers in the sector were sent a signal that they will need to conform to a higher authority and that RBI will not relinquish its hold over the banking system. This bodes well for retail participants in the industry who depend on banks for basic deposits and withdrawal facilities as well as financial advisory roles.

The banking phenomenon is yet to occur in the country with 70% of its population unexposed to even basic banking facilities. The scope for growth in this sector is enormous.

Consolidation has begun in phases with smaller banks joining hands to increase their outreach.

## **ENERGY, POWER, OIL & GAS**

India is a net importer of oil and gas which accounts for nearly 70% of its total consumption. This sector is highly sensitive considering far reaching effects it can have on both the economy and the end-consumer. NELP (New Exploration and Licensing Policy) was a program created to focus on improving self-sufficiency and increasing self-dependence in the country through better exploration activities and higher production. The gas discoveries of the KG basin and the oil fields in Rajasthan bear testimony to the success of this initiative. The upstream companies are subject to the volatility of the global demand-supply of crude oil and any increase in the price will yield abnormal profits while the downside risk holds true as well. The downstream companies on the other hand continue to bear losses because of government regulations. The customs and excise hike announced in the budget is viewed with skepticism by both the industry and the aam-admi. It is unclear to guess whether the finance minister's version of the hike is in line with the oil minister's acceptance of the Kirit Parikh committee on fuel pricing.

The power sector continues to remain in its infancy. The current revival in the economy certainly is an added bonus to all power companies who can now step-up momentum of their capacity. Power consumption in India has begun to gather pace given that the economy is growing at nearly 8% every year. Deficit in power is likely to push the government to add infrastructure and provide support and

give impetus to industrial and retail consumption. Raw material prices (coking coal) are expected to rise due to global demand patterns and hence, may be a cause of concern in the future.

### **INFRASTRUCTURE & ENGINEERING GOODS**

Demand for infrastructure has gained momentum in the last five years. Growth in the economy at the rate of 8% cannot be sustained with the current infrastructural set-up. FM announced higher allocations and incentives to boost housing, road, port, and airport development. Rs 1,735 billion earmarked for the infrastructure development in FY 2011, is an indication of the seriousness of the government in ensuring sustained growth in the infrastructure space.

The tax exemption under section 80-IA has not been extended and is a dampener. However, the growth drivers in this sector are the raw demand for addition of infrastructure and the pace with which this demand is pressing on the government. The most crucial issue in this sector is the credit availability which had slowed in the previous year. This had resulted in halting of many projects. Higher allocation to important infrastructure centric sectors in the budget will provide an impetus to many project-oriented companies in the engineering sector. The selective exemption on renewable energy-related apparatus and equipment will work positively for capital goods companies in the engineering sector.

### **AUTOMOBILES & AUTO COMPONENTS**

The Indian auto sector was the silver lining during the dark clouds of 2009. Almost all segments of the automobile sector

and their ancillary units did a great job. On the back of low interest rates, rural cash sales, government stimulus measures and a consumption-driven population, auto sales hit record highs. The budget has consciously refrained from disturbing the growth in this sector and hence, save for the 2% hike in excise duty, not much has changed for the sector. The hike in fuel prices is expected to be absorbed by the end consumer owing to better improving employment statistics in the country over the year and the income stimulus in the direct taxes, and hence will not be a deterrent to the growth in this sector. Auto demand is expected to continue to thrive on individual demand arising out of greater personal disposable income from the reduced tax rates (passenger vehicle segment) and improving economic conditions (commercial vehicle sector) in the short run and the additional impetus provided to infrastructural development with special focus on roads and increased defence allocations.

### **STEEL**

The Steel sector had two V-shaped cycles in 2008-09 and 2009-10. Largely driven by global demand-supply situations, this sector faces large volatility which can be tracked only if one understands China's buying patterns. Domestically however, steel prices faced an upside pressure in the first half of the year largely due to rising demand in the housing, consumer durables and the auto sector. Currently, with the budget's increased focus on infrastructure spending, step up in economic performance and increased global demand sector is poised for significant growth over the medium to long term. This sector has huge growth potential in the long term, given that India's current consumption levels are far below global standards.

## INFORMATION TECHNOLOGY & TELECOM

Budget has not given anything to the Indian IT sector directly. The hike in MAT and the decrease in surcharge to 7.5% will bring the total tax burden to 18%. The budget's focus on improving government's delivery mechanisms through IT initiatives will create a larger market for IT services. Indian IT companies who have increased their focus on the domestic market during the slowdown in the US IT market will gain from increased usage of technology by the government.

The Indian Telecom industry continues to penetrate Indian market which is now being supported by affordability and awareness of telecom as a welcome change. With many new entrants launching services in India, competition has reached unprecedented levels. The new entrants have offered attractive schemes to tap into the large consumer base. This is a sector where a combination of volume-based revenue and value-added services will determine the winner in the long-run.

## PHARMACEUTICALS

The Indian pharma sector depends heavily on foreign markets especially USA. The economic slowdown, inability to meet the stiff quality standards of the US, delay in receiving approvals, and declining interest in global pharma majors for research collaborations with Indian counterparts owing to cost inefficiencies are some of the disadvantages to this sector. Budget's increased focus on public healthcare schemes is a huge positive for domestic pharma companies who have greater presence in the generics

space. Higher deduction for R&D will provide the much-needed impetus to in-house R&D in domestic companies.

## CONCLUSION:

The lesson one learns from the global meltdown and the surprising speed of recovery is that the very large population that India possesses which was once upon a time, viewed as a burden on weak economy, has, today, turned into the growth driver for the economy. Nobody can predict the future for developed and advanced economies but everyone can vouch for critical events in developing nations which will more or less follow similar growth trail, which in investor parlance is the "emerging market story".

If the Indian economy continues to maintain its current growth rate, it will soon emerge as one of the most powerful economies in the world. Given that we in India have some of the most brilliant minds at the helm of our polity and bureaucracy, we can hope to see more calibrated efforts at steering India towards the very coveted double-digit growth. This Budget has a lot to offer to its citizens and hence it is for us now to come up with the response in terms of savings, tax payments and consumption and overwhelm the Finance Minister.

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*The views expressed in this booklet are not necessarily those of the Forum of Free Enterprise.*

## SHAILESH KAPADIA

(24-12-1949 - 19-10-1988)

Late Mr. Shailesh Kapadia, FCA, was a Chartered Accountant by profession and was a partner of M/s G.M. Kapadia & Co. and M/s Kapadia Associates, Chartered Accountants, Mumbai.

Shailesh qualified as a Chartered Accountant in 1974 after completing his Articles with M/s Dalal & Shah and M/s G.M. Kapadia & Co., Chartered Accountants, Mumbai. Shailesh had done his schooling at Scindia School, Gwalior and he graduated in Commerce from the Sydenham College of Commerce & Economics, Mumbai, in 1970.

Shailesh enjoyed the confidence of clients, colleagues and friends. He had a charming personality and was able to achieve almost every task allotted to him. In his short but dynamic professional career, spanning over fourteen years, Shailesh held important positions in various professional and public institutions. His leadership qualities came to the fore when he was the President of the Bombay Chartered Accountants' Society in the year 1982- 83. During his tenure he successfully organized the Third Regional Conference at Mumbai. He was member, Institute of Fiscal Studies, U.K.; member of the Law Committee and Vice-chairman of the Direct Taxation Committee, Indian Merchants' Chamber. He was also a Director of several public companies in India and Trustee of various public Charitable Trusts.

He regularly contributed papers on diverse subjects of professional interest at refresher courses, seminars and conferences organised by professional bodies.

*"People must come to accept private enterprise not as a necessary evil, but as an affirmative good".*

**- Eugene Black**  
Former President  
The World Bank

# FORUM

## of Free Enterprise

The Forum of Free Enterprise is a non-political and non-partisan organisation started in 1956, to educate public opinion in India on free enterprise and its close relationship with the democratic way of life. The Forum seeks to stimulate public thinking on vital economic problems of the day through articles, booklets, meetings, and other means as befit a democratic society. The Forum is also involved in building good citizenship through elocution and essay competitions, leadership training camps, etc., for the youth.

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