BUDGET 2014: Post Budget Market Direction?

7th July, 2014

The first Budget of Namo Government is expected to be growth oriented with definite direction towards higher Tax compliance, lowering of Subsidies and reduction in Taxes. Markets may read into the long term implications which should lead to a continued bullish trend.

Domestic indications for the Budget:

- Services activity rises to 17-month high on strong order flow in the first month of NDA,
- June factory activity grows at fastest pace in 4 months,
- June car sales rise hinting at recovery,
- After a dry June, monsoon is expected to advance,
- Venture capital investments in India rose 40% in first half of 2014,
- M&A at 7 year high, volume rose to $6.9 billion in April from $1.8 billion a year ago,
- QIPs rise 10 fold in April-June,
- Fitch raised India's growth targets to 5.5% in 2014-15 and 6.5% the next year,
- Overseas investors have poured in a staggering Rs 19,772 crores (USD 3.35 billion) into the Indian debt markets in May, the highest monthly inflow in about two and a half years, and
- Indian households' savings in physical assets (including gold) are at 10 years' highest levels whereas savings in financial assets are at 10 years' lowest level.

  These positions are expected to change and we expect big inflows from physical assets to more productive financial assets after budget, driving the markets further higher.

Global indications:

- Worst of Iraq crisis is over and has been discounted by markets as reflected in falling crude prices,
- Growth at US factories held near the fastest pace of the year, and
- China and Japan gained pace in manufacturing activity.

Major Path-breaking Decisions Expected from Budget (That will boost markets post budget):

- First major revamp in decades of India's archaic labor laws to take place soon leading to revival of flagging economy, boost to manufacturing, and creation of millions of jobs. Labor reforms can create a virtuous cycle in Indian manufacturing. Rajasthan has already started working on it.
- GST (Goods and services tax) is expected to be introduced which would result in a major rationalization and simplification of the consumption tax structure at both the center and state levels by replacing all central and state level indirect taxes such as value added tax (VAT), excise duty, service tax, entertainment tax among others bringing relief to the common man. GST is the most ambitious indirect tax reform in India ever attempted and aims to create one "borderless domestic market". If GST is implemented without many exemptions and with a single rate, the following benefits will accrue: * Macro: Successful pan-India implementation will add 1-1.7 % to the GDP and boost the tax/GDP ratio. * Micro: Incidence of tax will come down in case of manufactured goods. However, in case of services the incidence and coverage of tax may rise resulting in higher prices. * Industry: Volume growth will accrue as incidence of taxation is minimized. Also, supply chain efficiencies will accrue as there will be no need for multiple depots and warehouses.

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