PERSPECTIVE

SEPTEMBER 2019

Well to start with, it has been a dramatic quarter where market sentiment changes from fear to greed. As lastly discussed that some budget proposals regarding tax surcharge and change in shareholding pattern will spoil the market mood and then the geopolitics risk, news of demand slowdown, reduced auto sales, GDP at 6 year low, biscuits not selling and so on was creating fear among market participants. Now the best part is Government has become proactive and taken necessary steps/reforms which will help in reviving sentiments and kick start the economy which has been under pressure for the last few quarters.

Tax reduction: The basic tax rate for all companies will be lowered from 30percent to 22percent, and after adding surcharges, the final figure will be 25.17percent instead of 34.94percent.Even lower basic income tax rate of 15 percent tax for new companies in the manufacturing sector has been announced.

Impact: On the fiscal front, the tax cuts mean that the government will have Rs.145000crore size hole in its revenues. For Equity holders, this means their earnings on an average will increase not just in FY20 but in the future as well. The rise in the market post the tax cut announcement will give rise to the Wealth Effect i.e when someone has to spend money; it is not that he has to necessarily withdraw it from his savings. He spends it from his regular earnings. But to spend a bit more, he needs to have the confidence that his savings are doing well. Otherwise, he tends to pull back on his expenditure. Now that the value of his portfolio has suddenly gone up with the rise in the market, he will feel more confident of spending. This is likely to lead increased demand.

This is, of course the optimistic scenario and how this actually plays out will be evident in time. As we know, in short term market is driven by news/events and sentiments. In long run, underlying earnings of companies play a significant role.

What next for investors !?: Simply, reduction in tax rate should not change your immediate investment strategy.It is well-known that equities generate better returns than any other asset class in long run. With 2-3 year returns turning negative for SIP and LUMSUM investment, investors are wondering how long is long term. So to address the same, Good news and Good prices do not come together hence long-term investors should consider all corrections as investment opportunities. From a pure asset allocation perspective, long-term should be defined as minimum 12-15 year. Equity allocation is usually restricted to 50% for goals that fall between 7 and 10 years and should shift from equity to debt as the goal approaches/nearby.