The Indian EXPRESS

An Expert Explains: Road to India's economic recovery from the pandemic

Ahead of the Budget, one of India's top capital markets experts writes an open letter to Finance Minister Nirmala Sitharaman, listing a dozen ways to raise funds to finance India's recovery from the pandemic.

Written by **Nilesh Shah** | December 21, 2020

Respected Finance Minister,

Despite demands for more government spending, total expenditure was curtailed by 0.6%, as total receipts dropped by 33% in 1H FY21. You optimised spending, borrowing and fiscal prudence. Covid-19 impacted segments like hospitality and MSMEs, which need fiscal support. There is demand for reduction in consumption taxes for a period of time to support demand creation. I am sure you are inundated with demands for money. I am taking the liberty to suggest ways to raise resources to finance spending. They aren't easy, but if you won't make an attempt, who will?

Gold disclosure scheme

1. Like kasturi mrig, we are roaming the world searching for money, but are ignorant of money that lies among us. In the last two decades, we have spent $373 billion for net imports of gold. Smuggled gold and jewellery worn by travellers will take that amount beyond $500 billion.

   Unfortunately, the bulk of this gold is blocked in the black economy. A Gold Disclosure Scheme will mobilise taxes, unlock capital lying in the black economy, and upgrade India's sovereign rating. Good structuring and execution with precision, targeting 10% of the stock of gold has the potential to raise Rs 3,50,000 crore in taxes and unblock capital of Rs 10,50,000 crore.

Convert gold import duty to GST

2. The levy of import duty on gold has encouraged smuggling and enhanced the attractiveness of gold by increasing the rupee value of gold. A shift of taxation on gold from import duty to GST will increase tax revenues as smuggled gold gives way to official imports.

   Jewellers won't be impacted due to the pass through, but will come under the tax net. In the import duty regime, the investor perceives gold as an item of investment, as his cost and market value is the same at Rs 112.50 (12.5% import duty on gold). In the GST regime, the ultimate gold investor will have to pay Rs 112.50 to get gold valued at Rs 100. Instant loss recognition will diminish misallocation of our savings and make available domestic capital to finance growth.

THE EXPERT

Nilesh Shah, Managing Director of Kotak Mahindra Asset Management Co Ltd, has over a quarter century's experience in captail markets and market-related investments. He is one of the country's most astute financial analysts.

Realising better value for PSUs

3. In January 2008, the BSE PSU Index peaked at 11,205, and the Sensex at 20,827. After 12 years, the Sensex is up 2.25 times to 46,960, and the PSU Index is down 48% to 5,871. The PSU Index having underperformed the market by 173% in the last 12 years, the trades below book at 0.92 times despite a high dividend yield of 2.9%.

Piecemeal and predictable market divestment among other reasons have resulted in a sharp de-rating of PSUs. Successful strategic divestment of one PSU can re-rate all PSUs. If PSUs trade at the higher end of their valuations, the market value of the government's holdings will appreciate in excess of Rs 7,00,000 crore. Forty-five per cent of HZL was strategically divested in 2002-03 for Rs 769 crore. The residual 30% government stake is valued at Rs 30,000 crore, an appreciation of more than 59 times in 18 years.

Bring black market economy to white economy

4. Indians are large spenders in casinos at Macau, Singapore, Las Vegas, and Nepal. Large-scale betting happens on the IPL, elections, and other events. Matka thrives. We must legalise such activities with necessary safeguards. This will transit criminal activities to responsible businesses, raise taxes, cut off funding to criminals, and support the tourism industry that has been the hardest hit by Covid-19. In 2018, Kerala lottery had turnover of Rs 12,000 crore and a profit of Rs 2,500 Crore. Lottery sales contributed 80% of non-tax revenue to the state.

Plug the tax leakage on smuggled/fake cigarettes

5. As per the Tobacco Institute of India, the representative body of stakeholders in the tobacco industry, smuggled/fake cigarettes account for 25% of cigarette volumes. It is such an attractive business that some of the Covid-19 returnees smuggled in cigarettes for quick gains.

We need to curb smuggling of cigarettes/manufacturing of fake cigarettes through focused efforts. This has the potential to generate taxes of Rs 10,000 crore. In the longer term, we need to bring bidi and other tobacco products, which accounts for 91% of tobacco consumption, in the tax net.

Monetisation of enemy property assets

6. Properties (including encroached and disputed) and financial assets aggregating more than Rs 1,00,000 crore have been held by the Custodian of Enemy Property since 1968. A fast track mechanism to liquidate the same can raise resources and help catch up with Pakistan, which liquidated their enemy properties way back in 1971.

Unblock capital stuck in commercial disputes

7. From the 1992 securities scam to the 2018 IL&FS and DHFL cases, trillions of rupees are stuck in the absence of resolution. A fast-track mechanism for speedy resolution of commercial disputes will unblock the stuck capital. From being equal to us in the 1980s, China has leapfrogged to become five times bigger, based on higher credit creation. Such decadal blockage of capital constrains credit creation and adversely impacts our growth.

Sale and lease-back of government properties

8. The government can do a sale and lease-back of its incredible sets of properties. Rental cost to the government will be lower than borrowing cost through gilts. Obviously the government will miss on the real estate appreciation. Investors queue up to get the government as a long-term tenant at attractive terms in a low-interest-rate environment. Auction the bragging rights of saying “the government is my tenant”.

Estate Duty

9. In the United States, estate duty goes as high as 40%, albeit with several exemptions. Many Indians are happily paying estate duty in the US on their inherited assets in India. We should levy estate duty on unproductive assets like precious metals & stones, art, and offshore assets. This will encourage investment in financial assets that will provide domestic capital to accelerate growth.

Plug tax loopholes

10. Ethical hackers are rewarded to find loopholes in programming. Ethical tax practitioners should be rewarded for plugging tax loopholes. For example, there is a cottage industry running to convert interest income taxable at 43% to long-term capital gains taxable at 10% through zero coupon listed debentures. Dividend stripping could take away hundreds of crores in taxes in the stock of a tech company that recently declared a large dividend. You will be surprised what well-motivated ethical tax practitioners will be able to plug leaks in our tax system.

Improve ease of doing investments

11. In the last two decades, more than Rs 1,00,000 crore of investor money is stuck in collective investment schemes ranging from NBFCs, jewellers, chit funds, Vishi (a scheme similar to chit funds and popular in Gujarat), agro tech/forest/emu rearing companies. Buying a financial product isn’t as easy as buying gold. Multiple and high-cost of KYC constrains penetration of regulated financial products among bottom-of-the-pyramid investors. Simple and cheaper KYC will ensure more flows to financial products and enhance availability of domestic capital to finance growth.

Allow PSUs to manage treasury on a commercial basis

12. Private corporates invest in mutual funds to optimise their treasury income. PSUs don’t enjoy similar flexibility. Better treasury management will help PSUs to pay more dividend and help re-rate valuations. I must disclose my conflict as a mutual fund manager. However, our clients will vouch for my suggestion.

There will be many arguments why the above suggestions can’t be implemented. Accelerated growth of India financed by domestic capital is the only reason why the above suggestions need to be implemented.

Yours truly,
Nilesh Shah

Source: *https://indianexpress.com/article/explained/an-expert-explains-road-to-indias-economic-recovery-from-covid-19-7112777/*