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FM keen to bring foreign fund managers to India

by Pravin Palande | Feb 28, 2015

Jaitley doesn't crunch numbers, looks at long-term measures

Budget 2015 proved to be a disappointment for day traders as Finance Minister Arun Jaitley decided to move long term instead of the usual practice of looking at the micro aspects. "This was probably the first budget where the FM concentrated more on the long-term measures than simply talk numbers about the sector. Obviously, the day trader is not going to like it," says Vikas Gupta, head-research at Arthaveda Fund management. The Sensex remained flat at 29,246.

Agreed that the FM did not have much to give away about the earning potentials of sectors and companies, but he did make some interesting points about improving the financial markets and its infrastructure.

Jaitley talked about streamlining the taxation regime of Alternative Investment Funds (AIFs), which normally have foreign investors and are either managed from Singapore or Mauritius, where the tax structures are friendly towards both the fund management companies as well as the investors. Had these companies been run out of India, the investors get taxed at 40 percent and so does the fund manager. While the FM did not give any specific guidelines about how he plans to get these fund managers on the Indian shores he did say, "With a view to facilitate relocation of fund managers of offshore funds in India, it is proposed to modify the permanent establishment (PE) norms."

This is will be a gamechanger because if these fund managers do set up shops in India, they can be taxed as their fees exceed $8 billion per year. They are now taxed as per the laws of the land where these companies set up shop. "But what is also important is that a lot of other paraphernalia that includes custodian services, lawyers and accounts will see a demand for their services. That will help the entire financial sector in the country. This will eventually add up to the setting up of financial SEZs like the GIFT in Gujarat," Gupta adds. The FM has said in his speech that the first phase of GIFT will soon become reality and appropriate regulations will be issued in March 2015.

The other aspect of the Budget dealt with deepening of the bond markets. While the FM talked about permitting tax-free infrastructure bonds in the areas of rail, road and irrigation sector, which will attract a lot of foreign as well as domestic investments, improving the bond markets on the corporate side will be a difficult task. This is because the size of the Indian corporate bond market is limited and unlike developed countries, where the size of the bond issue itself gives it liquidity.

But this can change as the requirement of companies as well as decreasing interest rates could attract companies to this instrument. But the biggest problem is that bonds are not like equities.
"Each issuer typically issues just a single equity instrument. But in the case of debt, each issuer issues many debt instruments across various maturities and types. As a result, individual debt instruments do not have a large issuance amount and achieving liquidity at an instrument level is extremely difficult" says Rajiv Shastri, Managing Director and CEO at Peerless Funds Management Co Limited

Overall, Shastri agrees that it is a welcome change for the government when it comes to raising money for infrastructure projects as they are in a position to get big investments through these products.

The FM has also talked about a merger of the Forward Markets Commission (FMC) with Sebi. It's a big step to move towards a super and single regulator for all financial markets. India is one of the few countries that have different regulators for different products in financial markets.

Today, mutual funds are not in a position to invest in commodities because they are not considered as securities but mere contracts. With the merger of the FMC and the Sebi, commodities can become securities and separate mutual fund products can be launched by mutual funds. "Sebi as an autonomous regulator will, of course, be a big advantage for the commodities industry. It will also help in faster integration of the commodities futures industry into the financial trading landscape. I am sure Sebi will also be well equipped to handle the new challenges, which come with the introduction of a new product line under its regulatory oversight," says Jayant Manglik, president-retail distribution at Religare Securities.