Govt ETFs await Budget incentives

Centre yet to notify Section 80C tax benefit, even as it plans another tranche; demand may be muted

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Mumbai, 28 January

PSU exchange-traded funds (ETFs), which have made significant contributions to the government's disinvestment plans in the past, are yet to receive tax benefit proposed in the FY20 Budget, even as the Centre lines up yet another share sale through this route.

Among the key proposals of Finance Minister Nirmala Sitharaman's maiden Budget was extending the Section 80C tax advantage to PSU ETFs. However, the proposal is yet to be notified.

Industry players say this could hurt the demand as the latest tranche of government ETFs is being launched at a time when retail investors earmark funds to park into tax-saving products.

"If PSU ETFs had the additional benefit of tax savings, they could have garnered higher demand from investors looking for tax-saving options under Section 80C around this time of a financial year," said Amol Joshi, founder of Plan Rupee Investment Services.

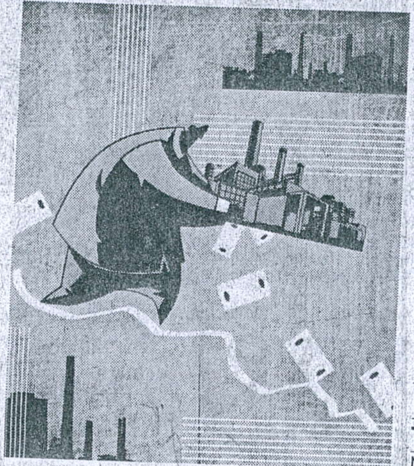
ILLUSTRATION: BINAY SINHA

"In the absence of tax benefit, the government will not be able to capitalise on this opportunity," said a senior executive of a fund house. The seventh tranche of CPSE ETF — which opens on Thursday — is aimed at raising ₹10,000 crore.

Investors can claim a tax deduction of up to ₹150,000 from the overall gross revenue under Section 80C of the Income Tax Act. Equity-linked savings schemes (ELSS) are popular among mutual fund (MF) investors looking at this tax-saving option.

Industry players said operational difficulties, such as providing the option for a lock-in period, have delayed the ratification. More clarity can be expected in the upcoming Budget, they said. The 2020-2021 Union Budget will be presented this Saturday.

According to investment bankers, tax incentive on ETFs could help the government improve its disinvestment kitty. "The government is finding it difficult to meet its disinvestment target as large-ticket strategic sales look unlikely in this fiscal year. ETFs can bring in more funds if the government sweetens the offering through tax benefits," said a merchant banker.

The government's disinvestment target for 2019-2020 stands at ₹1.05 trillion. Thus far, the government has raised ₹18,094 crore through disinvestments this fiscal year, just 17 per cent of the target.

Last fiscal year (2018-2019), ETFs played a significant role as the government raised 56 per cent (₹45,079 crore) of its disinvestment target through this route.

According to a fund manager, getting retail flows will also help fund houses manage PSU ETFs.

"PSU ETFs tend to attract institutional investors and high-net worth investors, who typically make short-term investments to take advantage of the discount offered on issue prices. On the other hand, retail flows are relatively sticky in nature," the fund manager said.

In the past, huge redemptions by large investors have led to erosion in PSU ETFs' assets under management (AUM).

Besides CPSE ETF (managed by Nippon India MF), there is Bharat 22 ETF, which is managed by ICICI Prudential MF. The AUM of CPSE ETF stood at ₹10,459.53 crore as of December 31, 2019, while the AUM of Bharat 22 ETF stood at ₹8,136.16 crore.

GAINING GROUND

ETFs have grown in prominence as the government's preferred disinvestment route (Figures in ₹ crore)

Mode of disinvestment	FY18	FY19	FY20 till date
IPO	24,040	1,704	1,114
ETF*	14,500	45,079	14,369
OFS	13,711	5,236	730
Strategic disinvestment	4,154	6,713	NA
Buyback	5,207	10,291	NA
Off-market deal	36,915	14,500	NA
Enemy share sale	NA	NA	1881.21
Total	**98,526**	**83,522**	**18,095**

Note: Strategic disinvestment includes Suuti stake sale; off-market deal includes transfer of govt shareholding in a PSU to another PSU

Source: DIPAM