

# A SHOT IN THE ARM FOR THE INVESTOR ECOSYSTEM IN INDIA

Relevant for: Indian Economy | Topic: Issues relating to Growth & Development - Public Finance, Taxation & Black Money incl. Government Budgeting

We missed a golden opportunity to initiate goods and services tax reform

While the focus is on the edifice, the most impressive part of Budget 2022 is the foundation laid through prudent fiscal management over the last year. A low fiscal deficit, pegged at 6.4% for FY23, has helped manage inflation and created the space to drive growth through India's largest infrastructure funding budgetary allocation at 2.9% of gross domestic product (GDP) to help India continue being the fastest growing major economy in the world.

This, to me, is the principal highlight of this year's budget. In that sense, this is a dream budget that hopefully sets the stage for our lawmakers to hard code fiscal responsibility into our constitution, Germany style.

This budget will also be remembered for steps taken towards providing a level playing field for startups vis-à-vis large, listed enterprises. A notable step is limiting the surcharge on long-term capital gains (LTCG) in unlisted companies to 15%. The surcharge could be as much as 37% previously, resulting in an effective capital gains tax of 28% on unlisted stocks. This has come down to around 23% and is hopefully the first step of many, resulting in equal LTCG in unlisted and listed companies.

There is a growing amount of private equity and venture capital activity in India, with 5.5 trillion being invested by these vehicles in 2021, but only 10% of this was Indian capital. Onshoring the offshore has been the industry's war cry for the past few years but the tools were missing. This budget is path breaking from this perspective, as it has announced the move for the government to sponsor a fresh set of fund of funds.

This was first done under Sidbi's fund of funds structure to funnel capital under the government's Startup India initiative and was a huge success in improving the flow of domestic capital to Indian startups. The announcement is a doubling down on a successful initiative by the government. What makes it even more special is that the fund of funds will be managed by the private sector and deliver 5x leverage and an incremental 10x leverage at an individual fund level; 10,000 crore invested in this initiative could end up creating 500,000 crore of funding for startups in India.

There is more for the VC/PE industry—this budget for the first time has accorded recognition to the industry by proposing an expert committee to examine regulatory and other frictions. A longstanding demand of the industry, which last year alone delivered nearly \$60 billion of capital to the nation. India is on track to become a \$100 billion PE market by 2025, and the industry will be at the forefront of economic growth and innovation. Establishing an expert committee with industry representation is another step in the right direction for the startup economy as reducing friction for investors will reduce friction for startups.

India has come a long way in terms of the ease of doing business. But we still have miles to go before doing business in India becomes more of a pleasure than it is. Conflict between businesses and the State is natural but India's slow legal system demonizes regulation as it often leads to a mountain of litigation. The budget aims to reinstate the trust between the

department and the taxpayer. The step to allow refiling of tax returns, and to limit litigation by government departments are both long-pending, and gladly welcome changes. The latter hopefully is the first of many steps to reduce the burden of litigation on an already overburdened system, given that the government is a party in more than 50% of disputes in India.

Favourites must be reserved for the last and mine is the move to allow foreign universities to be set up in GIFT city and that too without subjecting them to domestic regulations. This step could bring world-class education and globally-advanced technology to our doorstep—reducing cost, increasing capacity, and plugging the drain on our economy and talent.

While hoping for the perfect budget would have been unreal, we missed a golden opportunity to initiate goods and services tax reform. Good intentions must be followed by fair actions. While the intent behind GST is universally lauded, GST in its current form accords an unfair advantage to large businesses over small and medium business due to its complexity. Hopefully the next budget brings lower tax rates, reduced tax slabs, reduces complexity and makes doing business in India simpler and easier.

Views are personal.

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