

## India: Personal income tax cuts likely in the pipeline

Economics/Growth/Fiscal/Rates/India

DBS Group Research

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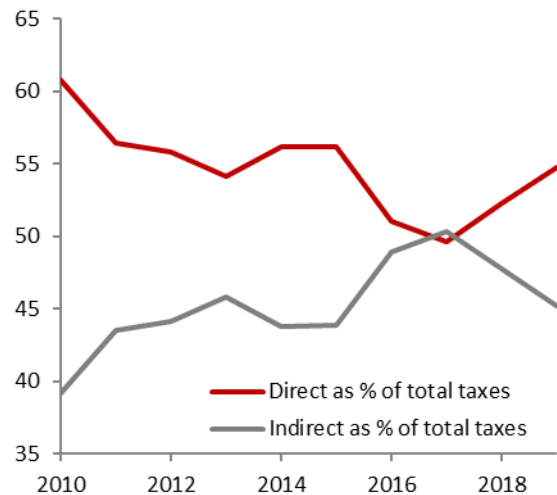
- Speculation is mounting on personal income tax rate cuts
- It might be announced as part of the annual Budget in February 2020
- We assess the likely impact
- Lower tax rates will provide short-term fillip to disposable income
- But this will entail fiscal costs
- Factoring in lower revenues and need to maintain spending points to a miss in the FY20 deficit target and slower pace of consolidation in FY21

Following the surprise move to cut corporate taxes last month, speculation is high that a reduction in personal income taxes is on the cards next (see our post-corporate tax cut note [PDF](#), [HTML](#)). With the all-in corporate tax rate at 25%, it is likely that personal income tax rates, which are at 30%+ levels, will also be lowered, surcharges notwithstanding. Markets are divided on the timing of such a move. Speculation is that the announcement is imminent, but the authorities might also prefer to bide time and announce any rework in the personal income taxes at the FY21 Budget due in February 2020.

### Past trends

The share of direct taxes to India's total tax revenues peaked at 61% in FY10 and has since stabilised around 55% last year. As a % of nominal GDP, tax revenues make up around 11%, within which the share of direct taxes has hovered around 5.5-6% of GDP in the past three-four years.

### Contrib of direct taxes to total tax revenues as % of total



Source: CDBT, DBS

Income tax collections amounted to **INR4.7trn** last year i.e. **2.5% of GDP**. This year's target for personal income tax is budgeted to rise by an ambitious 23% YoY compared to a subdued 10% growth in FY19.

### Income tax slabs for resident individuals below 60yrs

Income slabs (INR)	Tax rates* (prevailing); in INR and %
Up to 0.25MN	Nil
INR0.25MN-INR0.50MN	5% of the excess over 250k
INR501-INR1MN	12.5k + 20% on excess over 500k
INR1MN and above	112.5k + 30% of the excess over 1MN

Source: Tax authorities, DBS, \*does not incl cess, surcharges

The table above captures the income tax slabs for resident individuals below 60Y, with rates differing for senior citizens depending on their age. The top marginal tax rate is 42.7% imposed on incomes above INR5MN, which is higher than the average in the region at 30%. There is also an additional cess of @4% imposed on the taxpayers. Returns are filed by about 55MN individuals, which make up a fifth of total households and about 5% of the economy's estimated working age population.

### What changes are likely

A combination of an increase in the basic exemption limit and introduction of a differentiated tax rate structure for higher incomes might be on the cards – for instance, the minimum tax slab could be raised to INR0.50MN vs INR0.25MN presently. Tax rate on incomes over INR0.5MN might be lowered and subjected to differentiating rates (10%, 20%, 30% etc.). Such an arrangement will lower the burden on smaller taxpayers, modestly better for mid-tier but raise tax incidence on higher tiers. We note the imposition of additional surcharges on the high net worth individuals in the FY20 Budget in July (INR5MN onwards), which has already raised the net burden on the high-income brackets.

### Economic impact

Any increase in the basic exemption limit will be beneficial for the small taxpayers whose total income is below INR0.5MN (note that the Feb19 Budget had already provided rebate relief for INR0.5MN and below). Short-term fillip to consumption spending is likely, while a sustained improvement will require confidence in employment prospects and a sustained push towards raising job creation. Lower tax outgo

leaves room for higher discretionary spending, which will boost demand for white goods, travel etc., but unlikely to evidently improve for large ticket spending (e.g. real estate). The latest RBI consumer confidence made for sombre reading as the current and future expectations index extended the decline in September, along with weaker readings for perception and expectation of employment conditions.

Estimates of the likely cost of a review of the existing income tax slabs range from INR1trn-INR1.5trn. Considering the revenue arrangements with the states, the impact on the centre's finances could be to the tune of 0.3-0.5% of GDP.

As it stands, fiscal costs of the corporate tax reduction (likely to be smaller than earlier anticipated as not all firms are willing to forego exemptions to avail the new corp tax rate) coupled with below budgeted run-rate of direct and indirect taxes point to an at least 0.2-0.3% of GDP miss in the FY20 deficit target. Encouragingly, efforts to expedite receipts from divestment efforts is underway. Apart from ETFs and IPOs to raise funds, the stake sale pipeline consists of two oil majors, an electricals firm, national air carrier, corporatizing the national airports carrier, minority stakes in commodity names, amongst others. Hopes are high that total sales could outdo the budgeted target of INR1.05trn, a rerun of FY18, and help to narrow the anticipated tax shortfall.

Assurances that tax departments will be more taxpayer friendly, and almost all verification and audit of returns will be done electronically etc. are encouraging moves. Improving tax compliance is a necessary long-term change, to structurally improve collections and boost the headroom to increase productive spending.

## Appendix - Assessment year FY19 - Individual - Gross Total income

### Assessment year FY19 - Individual - Gross Total income

Income levels (INR)	Number of returns	Sum of Gross Total income (in crores)	Average tax payable (in 000s)
<=0	170767		
0 to <= 150k	2378193	19439	
>150k to <=200k	1376970	24389	
>200k to <=250k	3787092	88749	
>250k to <=350k	14275685	435583	0.3
>350k to <=400k	5025936	187421	6.4
>400k to <=450k	4156142	176437	9.1
>450k to <=500k	3783374	179602	11.7
>500k to <=550k	2999708	156922	17.8
>550k to <=950k	11153567	786895	55.7
>950k to <=1MN	600970	58565	112
>1MN to <=1.5MN	3001781	358928	178
>1.5MN to <=2MN	998299	171450	341
>2MN to <=2.5MN	508642	113143	499
>2.5MN to <=5MN	736059	247793	855
>5MN to <=10MN	209345	141704	2109
>10MN to <=50MN	89793	161142	6215
>50MN to <=100MN	5132	34814	24116
>100mn to <=250MN	2089	31046	53099
>250MN to <=500MN	451	15474	122882
>500MN to <=1BN	147	9929	242124
>1BN to <=5BN	74	13130	636403
>5BN	3	2344	2803200

Source: CBDT, press, websites, DBS

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**Sources:** Data for all charts and tables are from CEIC, Bloomberg and DBS Group Research (forecasts and transformations).

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