

Weekly Market Chatter @ Sensex 17,503.2

- Sunday Business Line

Index Outlook: Stocks in a flutter before budget

Our hope of a sedate jog to the Union Budget appears unlikely given the violent jig in stock prices last week. Stocks first plummeted lower dragged by slowing economic growth rate in China and the Congress debacle in the Assembly election. Then prices whooshed higher on Friday, probably due to the effect of Holi's 'rang' and 'bhaang'.

There was plenty to depress market watchers too — slowing exports growth, widening trade deficit, depreciation in rupee and crude oil at elevated levels.

The budget week is here and investors will be engrossed through the week with the Railway Budget, the Economic Survey, the Union Budget, the Monetary Policy and other macro data such as the Industrial Production numbers for January and headline inflation for February. Market also has to react to the RBI's surprise cut in CRR on Monday morning. No points for guessing that it is going to be one wild ride for investors next week. Fortunately Euro zone's troubles appear to have abated, at least temporarily, giving us some respite from that bug bear.

Volume in the cash segment was low. Derivative segment recorded sharp spike in volume on Tuesday. FIIs continued to be net buyers this month as well. Open interest accumulation is not too high at about Rs 1, 20,000 crore, implying that traders are not too sure about the direction in which the market will move after budget day.

Oscillators in the daily chart declined into the negative zone, in line with the on-going short-term downtrend. Weekly oscillators continue in the positive territory implying that the medium-term trend continues to be up for the Sensex and the Nifty. The hammer formation in the weekly chart of

the Sensex and the Nifty means that a short-term trough could have been formed last week.

The Sensex (17,503.2) tumbled to the intra-week low of 17,008 before Friday's recovery helped it close with a mild 133 points loss. The index is half-way through a correction and is well positioned to gyrate wildly in the upcoming sessions. The Sensex can move higher to 17,586, 17,765 or 17,944 in the run up to the Budget. Reversal from either of these levels will result in the index moving in a range between 17,000 and 18,000 in the upcoming week.

Short-term supports for the index would be 17,008, 16,829 and 16,429.

Nifty (5,333.5)

The Nifty declined to the intra-week low of 5,171.5 before closing 26 points lower. The index breached the key support at 5,231 briefly but managed a close above it.

In the near-term, the Nifty can move higher to 5,346 or 5,454 if the pre-budget excitement continues. Traders can initiate fresh short positions on reversal from either of these levels. Downward targets will be 5,171, 4,995 and 4,950.

Most global benchmarks held on to higher levels, though they closed slightly in the red. China's Premier, Mr Wen Jiabao, cutting the country's growth target to 7.5 per cent this calendar dampened sentiment across global markets in the early part of the week. However CBOE VIX traded between 16 and 21, denoting that investors were not too worried.

The Dow too ended the week 55 points lower to end below the 13,000 mark. The formation on the weekly Japanese candlesticks chart over the last three weeks denotes loss of momentum. But there is no outright reversal in this index yet.



Near-term support is at 12,374. The index needs to close below this level to signal that the short-term trend is reversing lower.

Signposts for the Budget-day

Budget is one of the market moving events that can affect the medium-term trend in the index. If the Finance Minister makes dire pronouncements that give market a jolt, the index can collapse to 16,430 after the Budget.

This is the medium-term trend deciding level. Investors can stay sanguine as long as this level holds. But the floodgates of selling will open if the index breaches this level.

There will then be the possibility of decline to 15,358 or 15,135 in the period after the Budget.

The key medium-term support for the Nifty is 4,950.

We will have to assume that the long-term trend has resumed only if this level breaks. Subsequent targets would be 4,695 and 4,588.

What if the Finance Minister removes STT or gives some other surprise bonanza to investors?

In such a scenario, the Sensex can shoot higher to the recent high at 18,523. Target on break above this level are 18,826 and 19,093.

First target for the Nifty on a euphoric reaction to the Budget is the previous peak at 5,630. Targets on break above this level are 5,647 and 5,850.

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CREATING VALUE FOR YOUR MONEY

How to save long-term capital gains tax

By investing the profit you make from selling a house, you can avail tax exemption. Here are the options that can help you get the tax benefit

Bindisha Sarang – Mint March2, 2012

If you earn anything, it’s minus taxes; if you buy anything it’s plus taxes,” goes a witty one-liner, which is quite true for all practical purposes. Like most other earnings, when you make a capital gains by selling your residential property, you are liable to pay tax. Here, your gain is the difference between the price at which you buy and the price at which you sell.

You can make two kinds of capital gains by selling a house property, depending upon the time you have sold the property. Says Parag Paranjpe, a Nagpur-based chartered accountant and certified financial planner, “If you hold a house for less than three years before selling it, then it is considered a short-term capital gain (STCG) and you have to pay tax according to your income-tax slabs. If you sell the house after three years or 36

QUICK GUIDE TO CAPITAL GAINS ACCOUNT SCHEME

Capital Gains Account Scheme

	Account A	Account B
Account category	Savings Account	Term deposit
Interest rate	As per bank's savings account rate	As per bank's term deposit rates
Options	—	Cumulative (interest reinvested) Non-cumulative (quarterly withdrawal)
Withdrawal	Any time	Pre-mature withdrawal permitted*

*By converting term deposit to savings account and by levying 1% penal interest for premature payment as in case of term deposit receipts.

MAKING THE MOST OF 54 EC BONDS

If your long-term capital gain (LTCG) is ₹1 crore or above, you can double your tax benefit if you sell your asset in or after October in any year.

LTCG	Maximum investment per fiscal year	Investment period
₹1 crore	₹50 lakh	Within six months of transfer of assets or capital gains

₹20 lakh
Tax benefit (at 20%)

Scenario 1

₹10 lakh
Tax benefit (at 20%)

- Asset sold between April and September
- Investment Opportunity Six months covered in same fiscal year
- Investment amount ₹50 lakh

Scenario 2

₹20 lakh
Tax benefit (at 20%)

- Asset sold between October and March
- Investment opportunity Two fiscal years will fall in six months
- Investment amount ₹1 crore (₹50 lakh per fiscal year)

Source: Mint research

months, then it’s considered long-term capital gain (LTCG) and you have to pay 20% of the profit as tax.”

On LTCG, you can claim tax exemption under certain conditions. Also, you get the indexation benefit on LTCG. Here are some ways through which you can claim exemption.

Buy a new property

One way to get an exemption on LTCG received from sale of a house property is to buy a new residential house within the stipulated time period.

Says Parizad Sirwala, partner, KPMG, an audit and consulting firm, “To get the exemption, you need to purchase the new residential house within a period of one year prior to or two years after transfer of the original house. As far as under-construction house goes, the construction needs to be completed within three years from the date of transfer of the original house.”

If you don’t plan to construct your own property, you can even book a residential under-construction house to avail this exemption.

You can get an exemption for an amount equal to the cost of a new house, or the amount of capital gains, whichever is lower. So let's say, you sold your house for Rs80 lakh, made LTCG of Rs40 lakh, and bought a new house worth Rs20 lakh. On the remaining Rs20 lakh amount, you will have to pay LTCG tax at 20%, that comes to Rs4 lakh.

There is a good chance that you may not get a new house of your choice within the stipulated time period. In that case, the Capital Gains Account Scheme (CGAS) can come to your aid.

Open a CGAS

You can deposit the capital gains amount in a CGAS before the due date of filing tax returns (31 July) to save LTCG tax. But treat CGAS as a parking place, where you can deposit money until you find a house that suits you, but of course within a time limit. The amount has to be parked in CGAS with the intention to use the funds to buy a new house within two years or to construct one within three years.

If you fail to buy or construct a new house within the stipulated period, the entire amount is treated as LTCG and you will have to pay tax on it. For instance, let's say, you sold a property in April 2010. The capital gain made should be used to either buy a house by April 2012 or construct a house by 2013. Until then, you can deposit the money in a CGAS account before the date of filing returns, which in this case was 31 July 2011, to save tax.

If you do not acquire the new property till April 2013, the LTCG would be taxable in the fiscal year 2013-14.

Where can you open it? You can open a CGAS account at an authorized government-owned bank.

It's important to remember that the amount you withdraw from CGAS should be used to purchase a house within two months from the date you've withdrawn these funds. Paranjpe says, "In case you buy a new house, ensure that you do not sell the new house within three years or you stand to lose the exemption. In such a case, you will have to pay LTCG tax in the year you sell the new house."

Invest in 54EC bonds

But what if you don't want to buy a property at all with the LTCG amount? You can still get tax exemption, but you will have to invest the amount in specific bonds that fall under section 54EC of the Income-tax Act. These bonds are issued only by the National Highways Authority of India and Rural Electric Corp. Ltd.

To get the tax benefit, you have to hold these bonds for at least three years. Keep in mind that as per the said section, capital gains have to be invested in the bonds and the benefit is allowed to the extent of the amount invested. Therefore, if you've made LTCG of, say, Rs30 lakh and have invested it in one of these bonds, the amount will be exempt from tax. But if you invest only a part, say, Rs10 lakh, you will get an exemption only on that part and will have to pay LTCG tax on the remaining Rs20 lakh.

Sirwala says, "To avail the exemption, you need to invest the whole or part of the capital gains in these bonds within a period of six months after the date of such transfer."

As per the Act, the exemption under this section is available provided the investment is made on or after 1 April 2007. Exemption is allowed on an amount up to Rs50 lakh in one fiscal. Paranjpe says, "Since the rule says that the maximum amount is Rs50 lakh per fiscal, you can take advantage if the six-month limit falls between two fiscal years."

In fact, you could time the sale of your house property in such a way that this period of six months actually falls between two fiscal years. So, if you sell the house between October and March, you come in the six months limit between two fiscal years. In that case, you can invest Rs1 crore in total over two financial years and get the tax benefit (see table).

Bond features: You can invest a minimum of Rs 10,000 and a maximum of Rs50 lakh. The face value is Rs10,000 per bond and you can buy up to 500 bonds. The bond is available for three years and can be redeemed only after three years. They come with a coupon rate of 6%, payable annually.



If for some reason, you are unable to keep the bond for three years, your tax exemption will be withdrawn and you will have to pay LTCG tax in the subsequent year. Also, if you avail a loan against such bonds within three years, you will have to let go of the exemption.

Recent Happenings and News

Should the ONGC issue bailout by LIC worry you, the policyholder?

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Expense Account | Monika Halan

The government recently gave the go-ahead to LIC to raise its stake in PSU banks higher than the 10% threshold the regulator mandates

Last week's bailout of the ONGC stake sale by Life Insurance Corp. of India (LIC) has turned the spotlight on an institution that is a household name in India and now finds itself being publicly questioned over its investment decisions. Should you be worried about your money in government-owned LIC that was set up by an Act of Parliament and carries a sovereign guarantee? The guarantee gives policyholders the safety net they need in terms of a promised return of their money, but to contemplate a government payback of just over Rs 25 trillion (the sum assured on almost 300 million policies), in a situation where such a bailout is needed, would be quite a disaster. But let's not think about that. It's safer to stay with worrying about returns rather than the risk of a sovereign default.

What does LIC sell? LIC is seen as a giant money collecting machine that has its reach all over the country through three million agents selling insurance. Except that they don't. What they really sell is a cumulative bond that returns not more than 5% with a tiny crust of life cover. No wonder that the average sum assured—or the death benefit in case of an untimely death of the policy holder—for LIC is just over Rs 93,000, even lower than the industry average of Rs 1.17 lakh. This means that if the policy holder dies, his family gets around Rs 1 lakh as death benefit—the reason people buy insurance. The reason people should buy insurance is to give the family a lump sum large enough to replace the income the policy buyer would have lost by dying. LIC, with the tiny term insurance (pure life cover with no investment) portfolio, is not selling insurance as its core offering. So what does LIC sell?

The bulk of LIC's portfolio comprises what is called "with-profit traditional policies". These are endowment or money back plans that get a share in the profit that the investment part of the premium makes. What it really sells is the promise of recurrent collection of money in the form of premiums (we could also call it a deposit and not be wrong) and a pay-out either on death or at maturity of an amount that has cumulatively earned about 5% annual return. That's below inflation, so why does it sell so well? Well, if you're the government then you can fix that. The premium gets a tax break, the corpus on death or maturity is tax free, making it more palatable to the investor. Throw in first-year commission of 40% to the selling agent, and you have a fat pipeline that sucks out money from the small investor. (As an aside, despite this gouging of commission from the premium, the incentive was not good enough to increase insurance penetration beyond 2% for the decades that LIC was a monopoly.)

So, where does this money go? The circle gets completed when you look at the investment pattern of LIC. Almost 60% (Rs 5.9 trillion) of policy holders' investments (according to form L-13 available here: <http://bit.ly/yjvhKH>) are in government securities and government-guaranteed bonds including treasury bills. While LIC (and other insurance companies) buying government bonds is an old story and is according to the rules of the game, the new story is the use of LIC policy holders' funds to buy stock of public sector units (PSUs) in breach of rules fixed by the Insurance Regulatory and Development Authority (Irda). The government recently gave the go-ahead to LIC to raise its stake in PSU banks higher than the 10% threshold the regulator mandates. Both mutual funds and insurance regulators prescribe prudential norms of investment that stipulate a limit of 10% in the equity of a company. LIC's investment in PSU banks has recently breached this limit with the permission of the government. The regulator is reduced to expressing unhappiness in press reports at this violation of its rules.

The government's comfort in having LIC at the other end of its phone line is felt by the regulator in its day-to-day functioning as well. Offline conversations with people in Irda reflect their inability to get LIC to play ball even in bread-and-butter regulatory issues. Irda's annual report some years back, say insiders, was delayed



almost by a year as data from the PSU insurer was difficult to get. For those who've followed markets in India, can you remember another government-promoted monopoly, that, after liberalization of the industry, hid behind its special status for a long time; did not submit to the new regulator; was opaque about its functioning? Until something called the Unit 64 fiasco tipped it over. It's still early days to say if ONGC will be the beginning of a bigger unravelling.

Sources: *ET/valueresearchonline.com/Business Line/Business Standard/Personalfn.com /BSE /NSE/ Moneycontrol.com /SEBI/Outlook Money/Money Today/DNA/Mint/MoneyLife*

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