Will the middle-class meltdown over the budget hurt the BJP politically?

By Abhik Deb, Published on 27th July 2024

Apart from continuing ideological support, experts say there are pragmatic reasons why there is unlikely to be a major backlash.

Nripendra Chauhan is furious that the Modi government's latest Union Budget has increased taxes on capital gains. The 38-year-old who runs a security guard agency in Noida is unhappy that his income from selling stocks – or capital gains – will now incur higher taxes. Over the last four years, Chauhan said he had invested more than Rs 6.5 lakh in equities.

"It is always the middle class that gets squeezed," he said. "The poor are getting free rations and the rich have their finances sorted anyway. We are the ones who have to bear the burden of taxes and do not get anything for free either." Chauhan identifies as a supporter of the Bharatiya Janata Party. Yet, he blamed the government for undermining the interests of the "taxpaying middle class".

This sentiment is not uncommon. After the Budget announcement on Monday, many have expressed their disappointment on social media. On Twitter, people expressed anger about taxpayers being "looted", criticised the prime minister for being "detached from the middle class" and pointed out that the salaried class had higher tax rates than the corporate sector.

The discontentment in this section is significant because the BJP has been the popular choice among urban, affluent Indians, who are often called the middle class, even though they are among the top 5% of the country by income.

Have the Budget's tax provisions dented support for the party among this section? We spoke to several BJP supporters like Chauhan to find out what was fuelling their anger and whether this is making them rethink their allegiance to the party.

What is causing the discontent?

The dissatisfaction with the Budget centres around changes introduced in the tax rates and regulations related to earnings from assets in the form of stocks, real estate and gold.

The tax rate on long-term capital gains across all financial assets has gone up from 10% to 12.5%, while the tax rate on short-term capital gains has risen from 15% to 20%.The period for which the financial asset is held determines whether the gains made on its sale are considered as long-term or short-term. For example, the holding period for equities is one year. This means that if an investor sells a stock within a year of buying it, she will be charged 20% tax on the gains made from the sale. For sales made subsequently, the tax rate will be 12.5%.

Moreover, this year's Budget also removed the benefits of indexation which allowed the capital gains on assets like real estate and gold to be adjusted for inflation. While the tax rate on these assets have been slashed from 20% to 12.5%, the phasing out of indexation means that holding these assets for a longer time could lead to a higher tax burden.

The government has said that the decision to do away with indexation was aimed at "simplifying the taxation of capital gains and their easy computation". The reasoning, however, has not stuck even among supporters of the government.

Rishabh Soni, a 43-year-old bank employee who owns three apartments in Noida and Gurugram, said the change in the rules defeated the purpose of buying real estate.

"You do not buy a home to sell it off very soon," Soni said. "The idea is to keep it as a no-risk asset and sell it off after retirement or if there is an emergency in the family to get a lump sum amount."

Soni added that his chartered accountant told him that he would have to pay more taxes now if he wanted to sell any of his apartments. “I do not plan to sell them anytime soon, I hope that the decision [on indexation] is rolled back by the time I decide to sell them,” he said.

Rajesh Kumar, a 48-year-old businessman from Jamshedpur, also said he would wait and watch. Kumar runs a garment shop and a medical store in Jamshedpur and owns two apartments in the city and one in Kolkata. He too was miffed with the decision to remove indexation benefits.

“I paid interest on home loans, I paid stamp duty, I paid registration fees and now the government wants more tax too,” he said. “The middle class does not get subsidies for anything and pays taxes for everything.” But the changes relating to real estate are not the main driver of anger among the middle class. The hike in taxes on capital gains on equities is what is causing the most resentment.

There is a reason for this: there has been a huge influx of retail investors in the stock markets in recent years.“During Covid, as incomes became uncertain, many Indians took to the stock markets as a means to make quick money, and because they could trade sitting at their homes,” said Suresh Sadagopan, the founder of financial advisor firm Ladder7 Wealth Planners.

The finance ministry’s economic survey for 2023-’24 noted that the number of investors registered with the National Stock Exchange in March had almost tripled to 9.2 crore from four years ago when the pandemic broke out. It flagged concern over the “possibility of overconfidence” in the markets.

A report released by markets regulator Securities and Exchanges Board of India on Wednesday showed that the influx in stock markets was led by young traders who typically invest smaller amounts. The share of traders with an annual intra-day turnover of Rs 5,000 has more than doubled between 2018-’19 and 2022-’23. The share of traders under the age of 30 has gone up by more than 2.5 times during this period.

Akash Kanojia, a 28-year-old digital marketing professional, fits the demographic profile that has driven the stock market rush. A resident of Prayagraj, Kanojia handles social media pages and WhatsApp groups for local BJP leaders, but he was not happy with the new tax regime.

“The government is saying that there is no rise in income tax, but is using capital gains tax as a backchannel to take our money,” he complained. “I think this move will discourage people from investing in stock markets.”

Kanojia said he had made profits of more than Rs 1.5 lakh from stock markets over the last two-and-a-half years, but was bracing for a greater tax burden because he typically invests on a short-term basis, for which capital gains tax has gone up from 15% to 20%. “If I had to park my money for a longer period, what is the difference between investing in stocks and investing in a fixed deposit?” he questioned, It is exactly this sort of investor behaviour that the government is looking to curb by raising capital gains taxes, said Vishal Dhawan, financial advisor at Mumbai-based firm Plan Ahead Wealth Advisors.

“The differential between short-term and long-term capital gains tax has gone up from 5% to 7.5%, that is the number we should be looking at,” he said. “The government is essentially pushing investors towards long-term investments.

Kanojia, however, was not convinced about this rationale. “It should not be the government’s prerogative whether I invest long-term or short-term,” he said.

Will the Budget hurt BJP politically?

Even though BJP supporters that *Scroll* spoke to were unhappy with the Budget, they continue to politically lean towards the Hindutva party.

Kumar, the garment and medicine shop owner from Jamshedpur, was candid in saying that the government had given sops to Bihar and Andhra Pradesh to keep its allies Janata Dal (United) and Telugu Desam Party happy. “But that is also important, because this government should stay,” he said. “Which party will replace this government? This is the best option we have now. At least this government is not giving freebies to its vote bank like [Arvind] Kejriwal in Delhi."

The argument against so-called freebies, a term often used by BJP leaders and supporters for social welfare schemes, found resonance with Chauhan, the security guard firm owner in Noida too. "In every state where the Congress is in power, it is because of its free guarantee schemes," Chauhan said. "Who pays for these guarantees? It is the middle class only. If I have to anyway pay taxes, I might as well pay for a nationalist government."

Nationalism in the Narendra Modi era is no longer just about protecting India's interests, as the BJP claims the prime minister has done by making the country a "vishwaguru" or world leader. It also contains antagonism towards religious minorities, particularly Muslims, as well as towards ideological adversaries who are often attacked as "anti-nationals".

This was evident in the comments of a social media user who identified as a BJP supporter while expressing disappointment with the Budget. She said she would continue to support the party despite the disappointment, but she urged Modi to take steps to "eliminate anti-nationals". She also suggested that the government move away from "sabka saath, sabka vikaas", or development for all sections, because the "other community" – a reference to Muslims – would never vote for the BJP.

In the past as well, economic setbacks have not dampened the enthusiasm for the BJP's Hindutva project, which political commentators say remains a potent force despite the party's reduced mandate in Parliament.

Soni, the bank employee, said that he would not shift his political allegiances yet. "Every government has a saturation point, the Congress government reached that point due to corruption," he said. "This government has done nothing for the middle class…no tax benefits ever, nothing. But it has not reached the saturation point yet."

How bad will the tax changes hurt?

Although BJP supporters have couched their reasons for continuing to support the party in ideological terms, financial sector experts told *Scroll* that there could be more pragmatic reasons for this.

The indexation move will not have an immediate impact on homeowners like Kumar and Soni as they do not have plans to sell their properties in the near future, Sadagopan said.

"Those who have two or three properties in real estate, you would see most of them putting their homes on rent, the tendency is not to sell but to keep real estate as an asset" he said. "The indexation move will hurt those who have several homes and are probably in the business of selling property. And this section cannot really be called middle class." Sadagopan also pointed out that even with a higher tax burden, equity investments were more profitable than putting money in fixed deposits offered by banks. "The interest rate for fixed deposits is a little more than 7%, but equities, even with a moderate estimate, will give you 10% to 14% returns," he said.

Investors' faith in the equity markets as a financial asset is also affirmed by a trend noted by a Reserve Bank of India research paper released earlier this month. Between 2012 and 2023, the share of financial assets in the form of bank deposits has declined from 51% to 43%, while those in equity and investment funds have gone up from 11.2% to 17.6%, the study found.

Financial advisor Vishal Dhawan of Plan Ahead Wealth Advisors said that this trend was expected to continue, pointing out that there was no massive-scale selling in the markets even after the budget announcements. He said that as a result of the government's push towards long-term investments, investor behaviour was likely to stabilise."There could be some activity in investor behaviour in terms of changing their position from short-term to long-term, but with the returns that the stock market is giving, I do not see them exiting the markets," he said.