A Beginner's Guide To Infra Bonds

Weekly Schedule

MON	Growth Investing
TUE	Income Investing
WED	Insurance
THU	Borrowing
FRI	Real Estate and Spending

Most of the bonds come from strong companies, but the fact that the interest will be taxed is a major dampener

INFRASTRUCTURE bonds are the talk of the town. Most taxpayers are happy that they have one more avenue to save taxes from this year. Till last year, they could invest only ₹1 lakh and save tax of ₹30,900 if they were in the highest tax bracket under Section 80C of the Income Tax Act. However, from this year, investors can invest an additional Rs 20,000 in infrastructure bonds under Section 80CCF. In effect, people in the highest tax bracket (30.9%) can now save an additional ₹6,180 from this year.

"From 2010-11, the finance minister has created a win-win situation both for infrastructure financiers as well as investors", says Anil Chopra, Group CEO, Bajaj Capital. "Investors can invest an additional ₹20,000 in infrastructure bonds under Section 80CCF, while infrastructure finance companies can raise funds for five years and 10 years through this process, which can be used to fund long-term infrastructure projects across various sectors."

Rewind Mode: Infrastructure bonds are not new to Indian investors. These bonds existed till 2005, when Section 88 of the Income Tax Act, 1961 was in force. "Infrastructure bonds were offered by financial institutions such as ICICI and IDBI, and had a lock-in period of three years," says Chopra. Investors could invest ₹1 lakh under Section 88 in those days, but it was structured differently. You could invest ₹30,000 in infrastructure bonds and ₹70,000 in other tax-saving instruments like equity-linked saving schemes (ELSS), Public Provident Fund (PPF) and National Savings Certificates (NSC) to claim tax benefit. Alternatively, you also had the option to invest the entire ₹1 lakh in infrastructure bonds. However, Section 88 was done away in the budget for 2005-06 and Section 80C was introduced.

Under the new section, an investor could offerings before the end of the financial year.

Waiting For More: However, according to experts, investors seem to be waiting for more issues before the financial year-end. "With bond issues of SBI and mega IPO of Coal India, investors were short of cash and a lot of them decided to invest in the latter half of the financial year," says Anup Bhaiya, MD, Money Honey Financial Services, a Mumbai-based financial products distributor. The interest offered by these bonds could be another reason for the low participation. The IDFC and L&T Infra issues offered 7.5-8.0%, varying marginally on account of buyback and listing options.

"The interest rates offered by these bonds are linked to the 10-year government of India bond, and cannot exceed that," says Vishal Dhawan, a Mumbai-based certified financial planner. Currently, the 10-year government bonds is close to 8% and the interest rate offered by L&T Infra issue, currently open, is between 7.5% and 7.75%, depending on the options you choose.

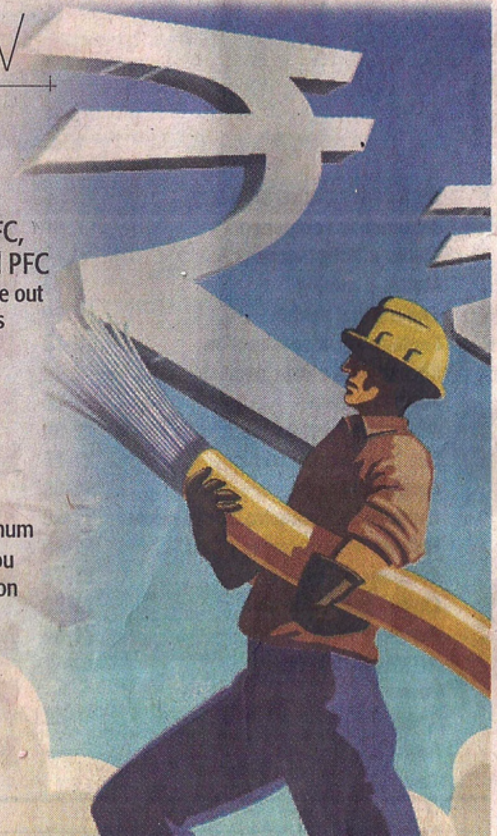
Dhawan adds that there are only two factors to consider in these bonds — the credit rating and the interest rate. "We do not expect interest rates to move up significantly from here and, hence, are advising investors to invest right now and not wait for other issuers or till the year-end," says Anil Chopra, Group CEO, Bajaj Capital. He also adds that there is no guarantee if the same issuers will tap the market again or not.

Bonding Time: Applying for these infrastructure bonds is very easy. All one needs is a PAN card. You could hold the investment in physical certificates too, in case you do not have a demat account. "In case you do have a demat account, it makes sense to hold these bonds in the demat form, as it eliminates the risk of losing paper or misplacing it," says Anup Bhaiya. "Coupon

BOND WITH THE BEST

Infrastructure bonds are back in the tax-saving league after five years. Here's a bird's eye view on what you can expect from them:

THEN	NOW
Offered under Section 88	Offered under Section 80CCF
Offered by ICICI and IDBI	Offered by IFCI, IDFC, L&T Infra. LIC and PFC are also likely to come out with infra bond issues
You could invest up to ₹30,000 and get tax benefits	Tax benefits only for investments up to ₹20,000
Lock-in of 3 years	Lock in of for a minimum 5 years. Post that you have a buy-back option
TDS paid on interest	No TDS
PAN not mandatory	PAN mandatory



Under the new section, an investor could claim deduction up to ₹1 lakh by investing in any of the instruments. However, somehow infrastructure bonds did not figure in the list. Realising the increasing focus on infrastructure, the finance minister introduced infrastructure under Section 80CCF in his last budget.

Offers Galore: IFCI, IDFC and L&T Infra have been some of the first to offer the new breed of bonds. Power Finance Corporation (PFC) and Life Insurance Corporation (LIC) are expected to join the list soon. IFCI was a private placement issue and mopped up ₹50 crore, according to distributors. IDFC Infrastructure Bonds was the first public offering that closed on October 22. Larsen & Toubro Infra issue is open to subscription till November 2. Essentially, non-banking finance companies, classified as infrastructure finance companies by the Reserve Bank of India (RBI), can issue these bonds. Though IDFC's first issue has closed for subscription, the institution has indicated that it may raise as much as ₹3,400 crore through the issue of bonds during this financial year. It is likely that IDFC could come up with at least a couple of more misplacing it," says Anup Bhaiya. "Coupon rates of 8% are not that attractive to merit investing a higher amount, though there is a reinvestment risk at the end of five years," adds Dhawan. Also, since the bonds have a five-year lock-in period, they offer no liquidity. However, these bonds score on pedigree, as they come from strong companies like IDFC and L&T Infra. The major dampener on these bonds is the fact that the interest earned on them will be taxable.

Finally, experts want that investors should first take care of their investments under Section 80C before chasing infrastructure bonds. "You should think of investing in infrastructure bonds only after exhausting your limits under Section 80C for the financial year," says Bhaiya. Also, it doesn't make much sense to invest in multiple-bond issues to diversify your holdings. "Most of these companies enjoy strong credit rating. Investing a small amount in two companies makes it a hassle to track the two of them later," adds Chopra.

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TOMORROW: KNOW YOUR INSURANCE POLICY BETTER

TAKE YOUR PICK

Tax-Saving Instruments: A Comparison

Index	Lock-In	Maximum Investment Limit	Interest Rate	Tax Impact On Interest
National Savings Certificate (NSC)	6 years	1 lakh	8%	Taxable
Public Provident Fund (PPF)	15 years	Up to 70, 000	8%	Tax-free
Equity-Linked Savings Schemes (ELSS)	3 years	1 lakh	NA	Tax-free dividends#
Tax Saving Bank Fixed Deposit	5 years	1 lakh	7-8%	Taxable
Infrastructure Bonds	5 years	20,000	7.5-8%	Taxable
Employee Provident Fund	NA	1 lakh	9.5%*	Tax-free

#If declared, *As per interest declared for FY10-11