

**A STUDY OF CORPORATE TAXATION AND ITS IMPACT ON
ECONOMIC VIABILITY AND FINANCIAL PERFORMANCE
OF MAJOR FMCG COMPANIES IN INDIA**

ABSTRACT

**SUBMITTED TO
BABASAHEB BHIMRAO AMBEDKAR UNIVERSITY
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ABSTRACT

Introduction

In India, corporate earnings taxation is one of the public finance subjects that has grabbed the most emphasis. Since our country's economy was liberalized, the share of corporate profits tax revenue to total direct tax revenue collected by the central government has been steadily increasing. As a result, only in the event that Indian industry expanded significantly would a boost in corporate tax collection to the government budget be feasible. Since the appropriate proportion of debt and equity are what drives a company's expansion, making a sensible capital allocation decision between these two sources is crucial to any firm's effectiveness. However, the decision between debt and equity is heavily influenced by corporate taxation. If raising money for a new project required maximizing profits for shareholders and using the interest paid on further borrowings as a tax shelter, a corporation would choose to use debt over equity. That indicates that a company's capacity to obtain external funding for expansion and diversification is largely reliant on the corporate tax laws of the nation. The needed rate of return on investment is raised by corporate taxation, which discourages future investments in equity or retained earnings and favours future debt investments over equity or retained earnings. Since the fast-moving consumer goods (FMCG) industry, which is the fourth-largest sector in India, has been growing at a healthy rate over the years due to factors including rising disposable income, an increase in the number of young people, and increased consumer brand awareness. With 50% of FMCG sales in India coming from the home and personal care sectors, the sector plays a significant role in the country's GDP. Three million people are employed in the FMCG sector in India, which makes up around 5% of all industrial jobs. Sales of FMCG increased by 7-9% in the nation in 2022–2023. The sector's main development drivers are favourable government efforts and policies, a growing youth population and rural market, new branded items, and the expansion of e-commerce platforms. Thus, it is necessary to find out how upto what level corporate taxation has affected financial performance of FMCG companies over the period of time in India.

Nor'Azem, and Bardai (2010) study looked at how a company's corporate income tax liabilities affected various aspects of its operations, including costs, cost of sales, and gross profit. A sample of 7,306 businesses was selected for the accounting periods 1995 to 2000, comprising 6,594 businesses in the business services and 1,484 businesses in the transportation manufacturing sectors. The sample was drawn from the hotels and restaurants sector. Corporate income tax has been found to have a negative impact on corporate institutions' profitability. S. Sreedharan (2010) highlights the value of ratio analysis and how it contributes in analyzing a company's financial performance. He makes it clear that the two companies' circumstances are not the same. In the same way, the variables impacting the business's success in one year could vary in the next. It is also useful for examining the company's earnings, which supports the business's long-term survival and expansion. As a result, analyzing the ratio is crucial to evaluating and analyzing the company's financial performance. Jens and Schwellnus (2008) examined the effects of corporate income taxes on two of the main drivers of growth, profitability and investment of firms in European OECD member countries over the time period of 1996-2004, through stratified sampling this is found to be true across firms of different size and age classes, except for young and small firms. The results suggest that corporate income taxes reduce investment through an increase in the user cost of capital.

Many studies, including the ones that are listed above, have tended to issues of corporate taxation, capital structure, profitability, turnover affects financial performance of corporates. The gap that emerges from the current literature review concern the fact that no particular study has been found in context which has focused on a unique interpretation of corporate taxation and its impact on economic viability of FMCG companies in India.

It is also observed that there is lack of research on the combined effects of corporate tax rates and other relevant factors on firm profitability in the FMCG sector is clear. The identification of unique FMCG Industry characteristics that may be statistically important in predicting business performance is frequently ignored in current studies, especially with a focus on corporate tax rates.

Objectives

1. To analyze the total income taxation in general and corporate taxation in particular over the time period in India since 1990-91 to 2022-23.
2. To assess the tax buoyancy of corporates over the period of time since 1990-91 to 2022-23.
3. To present an overview of Indian FMCG sector.
4. To examine financial performance of selected FMCG companies' comparatively since 2000-01 to 2022-23
5. To find out factors affecting financial performance of sampled FMCG companies since 2000-01 to 2022-23.

Hypotheses of the Study

1. There is significant effect of corporate tax comparatively Income tax in a growth of total income tax revenue.
2. There is comparatively decline in tax buoyancy of corporates over the time period.
3. There is a negative association between corporate tax and financial performance of selected FMCG companies.
4. There is positive association between financial performance and firm's size, firm's age, liquidity and growth of companies.

Methodology

Data has been collected from various secondary sources such as the Finance Acts of relevant years, The Central Board of Direct Taxes' circulars and notifications, the Indian Economic Survey, the Income Tax Act of 1961, the Income Tax Rules of 1962, the Budget speeches of the Finance Ministers, the Reports of the Comptroller and Auditor General of India on Direct Taxes, the Economic and Political Weekly, newspapers, and so on are all sources of information about the Central Government's budget/Survey. Additionally, data was gathered via the websites of the Ministry of Finance, the Income Tax Department, the Ministry of Statistics, and the Comptroller and Auditor General of India. The secondary data covers the years 1990-91 to 2022-23 for corporate taxes. For FMCG companies secondary data used in the study was

gathered from companies' financial statements, India Brand Equity Foundation (IBEF) and reports and time period for the study is 2000-01 to 2022-23.

Estimation Method and Variables

Calculating Financial Performance, there are many critical ratios that are extensively used in the business world to assist and evaluate a company's overall performance have been used. For comparative analysis Mean, SD, of selected FMCGs are being compared together. The variables utilised in the analysis to compare financial performance.

1. Liquidity Ratio
2. Cash Ratio
3. Turnover Ratio
4. Operating Cycle Ratio

Time Period

Time period of study is 23 years from 2000-2022.

Methodological Framework

Using the most relevant statistical approaches, secondary data was analyzed in order to verify numerous hypotheses within the logical positions necessary to support the research's major hypothetical subject. The following are the main methodological parameters:

1. To analyze the total income taxation in general and corporate taxation in particular over the time period in India, has been analyzed using buoyancy coefficient, simple growth rate, compound annual growth rate, and percentage change.
2. To assess the tax buoyancy of corporates over the period of time in India has been calculated by dividing percentage change in corporate tax by percentage change in GDP.
3. To present an overview of Indian FMCG sector, study aims to critically assess and give a quick outline of the FMCG companies. The secondary data used in the study was gathered from companies' financial statements, India Brand Equity Foundation (IBEF) and reports.
4. Calculating Financial Performance, there are many critical ratios that are extensively used in the business world to assist and evaluate a company's overall performance have

been used. For comparative analysis Mean, SD, of selected FMCGs are being compared together.

5. To find out factors affecting financial performance of sampled FMCG companies. Least Square Dummy Variable (LSDV) Panel Regression (Random Effect) model to represent impact of independent variables (eg; corporate income tax, age of firm, firm size, liquidity and growth of firms) on dependent variable performance.

Model

Least Square Dummy Variable (LSDV) Panel Regression (Random Effect) model to represent impact of independent variables (eg; corporate income tax, age of firm, firm size, liquidity and growth of firms) on dependent variable performance.

$$\text{PERF} = \beta_0 + \beta_1 d_1 + \beta_2 d_2 + \beta_3 d_3 + \beta_4 d_4 + \beta_5 d_5 + \beta_6 d_6 + \beta_7 d_7 + \beta_8 d_8 + \beta_9 d_9 + \beta_{10} \text{ CIT} + \beta_{11} \text{ FIRM SIZE} + \beta_{12} \text{ AGE} + \beta_{13} \text{ LIQUIDITY} + \beta_{14} \text{ GROWTH RATE} + U_i$$

$$D_1, D_2, \dots, D_9 = 0$$

Intercept: Coefficient

PERF = Performance

β_0 = Constant

β_1 = Coefficient of dummy variable 1

β_2 = Coefficient of dummy variable 2

β_3 = Coefficient of dummy variable 3

β_4 = Coefficient of dummy variable 4

β_5 = Coefficient of dummy variable 5

β_6 = Coefficient of dummy variable 6

β_7 = Coefficient of dummy variable 7

β_8 = Coefficient of dummy variable 8

β_9 = Coefficient of dummy variable 9

β_{10} = Coefficient of corporate income tax

β_{11} = Coefficient of firm's size

β_{12} = Coefficient of firm's Age

β_{13} = Coefficient of firm's liquidity

β_{14} = Coefficient of firm's growth rate

U_i = Error term

Above model represent Least Square Dummy Variable (LSDV) random effect as we have incorporated 9 dummy variables and have consider one FMCG firm as a reference category firm on the basis of low standard deviation of descriptive statistics and thus to demonstrate factors which are responsible for affecting financial performance.

Rationale of the Study

Taking a close look at the research problem prompts us to investigate the nature of the study, which is that the FMCG business is the fourth-largest sector in the Indian economy and corporation tax is a significant component of government fiscal expenditure. Fast Moving Consumer Goods (FMCG) companies generate a huge amount of employment possibilities and considerably increase India's GDP. They facilitate the broad accessibility of necessary goods in rural as well as urban areas. India's competitiveness in the global market is increased by FMCG firms, which also drive sustainable practices and product innovation.

Outline of the Study

The study comprises of **seven chapters** as follows –

Chapter-1: Introduction, considers a general overview of the issues in India regarding the study of corporate taxation and its impact on economic viability and financial performance of major FMCG companies. The chapter covers a detailed context of the study followed by a relevant review of literature and the research gap observed therein. It, then, outlines objectives, hypotheses, sources of data and methodology, and significance of the study. The primary objective of this chapter is to familiarise the reader to the research work.

Chapter-2: Theoretical and Conceptual Framework, presents a series of conceptual themes concerning the study wherein first section deals with the theories of corporate taxation, the second section outlines theories regarding economic viability, third section provides theories of financial performance.

Chapter-3: Taxation System in India: Focusing on corporate taxation and total income taxation over the period of time, this chapter deals with the analysis of total

income taxation in general and corporate taxation in particular over the time periods in India. This chapter also deals with buoyancy of corporates. Buoyancy coefficient shows what is the percentage change in GDP with respect to percentage change in corporate tax.

Chapter-4: An Overview of the Indian Fast-Moving Consumer Goods Industry, this chapter deals with an overview of the FMCG companies. ‘PEST’ and ‘SWOT’ analysis of FMCG sector. This chapter also deals with current scenario of FMCG sector with digital platform as well as recent developments and investments in the FMCG sector and government initiative to promote FMCG sector.

Chapter-5: A comparative study on various financial performance ratio in order to depict best performer among selected FMCG companies, this chapter analysed financial performance on the basis of Financial Performance Indicators i.e., Liquidity Ratios, Cash Ratios, Turnover Ratios and Operating Cycle Ratios. Financial performance of an enterprise is ascertained through analysing the financial statement. Financial Statements are usually thought of as a place to find information about firms and also play an important role in fundamental analysis. The analysis involves comparing the firm’s performance with that of other firms in the same industry and evaluating financial trends of the respective firms.

Chapter-6: To analyze the factors influencing the financial performance of sampled FMCG companies, this chapter examines the factors affecting the financial performance of selected major FMCG companies. All of the necessary factors that must be taken into account in order to consider the financial performance of FMCG companies. In this chapter we have included descriptive analysis and Least Square Dummy Variable (LSDV) Pannel Regression (Random Effect) model to represent impact of independent variables (eg; corporate income tax, age of firm, firm size, liquidity and growth of firms) on dependent variable performance.

Chapter-7: Conclusions and Policy Implications, this last chapter elaborates on the theoretical foundations and summarizes the findings of the preceding chapters in light of the study's objective. In view of the circumstances, goals, and research findings, this chapter makes recommendations for policy.

Concluding Remarks

- The current study focused on exploring the relationship between factor affecting financial performance of sampled FMCG companies. The study covered 10 major FMCG companies as per their market revenue share, for a period of 23 years spanning from 2000 to 2022.
- Factors affecting the financial performance are included. Descriptive analysis and Least Square Dummy Variable (LSDV) Panel Regression (Random Effect) model have been used to represent impact of independent variables (eg; corporate income tax, age of firm, firm size, liquidity and growth of firms) on dependent variable performance.
- As per market capitalization Hindustan Unilever Limited is at top and Glaxo Smith Kline at bottom among selected major 10 FMCG companies but as per performance we have P & G company at top while Marico at bottom.
- All the framed hypotheses have been found relevant which is there is a negative and significant impact of corporate tax and financial performance of selected FMCG companies.
- There is a positive and significant relationship between liquidity and financial performance of selected companies but there is insignificant and positive relationship between firm size and growth of the companies as well as insignificant and negative relationship between age of the firms and financial performance. So, for second hypothesis it is true only for liquidity, that is positive association between liquidity and financial performance of FMCG companies.
- LSDV model were run then following are the order of companies as per individual performance equation and performance value P& G = 0.921 NESTLE = 0.872 DABUR = 0.793 BRITANNIA = 0.72 GSK = 0.668 COLGATE & PALMOLIVE = 0.622 ITC = 0.562 HUL= 0.483 GODREJ = 0.471 MARICO = 0.349.

Policy Recommendations

Based on the study, the following policy improvements are recommended to enhance the plan in order to fulfill the worthy objective of enacting a straightforward tax system with reduced rates and few deductions:

- To make simpler the approach, all manufacturing and non-manufacturing businesses should be able to receive the identical optional reduced tax rate, say 20%. This could include the several lower rates of 25%, 22% and 15%.
- Not being able to claim loss carryover and depreciation allowances is a significant barrier, particularly for start-ups and other smaller, newer companies. This ought to be added back into the simplified plan.
- The tax code must to be kept simple and unambiguous by an excessive number of policy goals. Outside of the tax system, policymakers ought to take action to offer complete incentives to creative start-ups. Productivity-linked incentive (PLI) programs, venture financing, and suitable incubation facilities are a few examples of such measures.

Fast-moving consumer goods, or FMCG, companies must deal with a variety of policy implications that may have an effect on their operations, strategy, and financial performance. The following are some significant policy implications:

- **Tax Policies:** Modifications to tax rates, deductions, and incentives may have an impact on the investment choices and profit margins of FMCG companies.
- **Regulatory Compliance:** Tighter restrictions governing the branding, packaging, and safety of products can have an effect on product development and raise expenses.
- **Trade Policies:** The pricing, market access, and worldwide supply chains of FMCG companies can be impacted by tariffs, quotas, and trade agreements.
- **Environmental Policies:** FMCG firms may be compelled to implement eco-friendly practices by regulations pertaining to waste management, sustainability, and carbon emissions.
- **Consumer Protection Policies:** FMCG firms' marketing plans and customer interactions may be impacted by laws pertaining to product liability, consumer data privacy, and advertising.
- **Labour Policies:** The labour management and costs of FMCG companies can be impacted by minimum wage laws, working conditions, and employment restrictions.
- **Food Safety and Standards rules:** The manufacturing procedures and product quality of FMCG companies might be impacted by compliance with food safety rules.

- Policies pertaining to the digital economy: FMCG firms' online sales and marketing strategies may be impacted by laws governing digital taxation, data localization, and e-commerce.

For FMCG firms to remain competitive, maintain conformity, and stimulate growth, they need to be on the lookout for shifting policy settings and adjust accordingly.

Limitations of the Study

The limitation of the study is that merely major ten corporates in FMCG sector has been included for analysis. Since selected FMCG has been taken on the basis of market capitalization. Aggregately sampled FMCG companies share contributes nearly 50% market share of entire FMCG revenue, so top ten FMCG has been included.