Indian Economy · GS - III

Examine the potential benefits and limitations of reducing the long-term capital gains tax burden on foreign portfolio investors in India.

EXAM YEAR	PAPER	SUBJECT
DAILY PRACTICE 02/11/2026	GS - III	Indian Economy

MARKS	WORD LIMIT
10	~150 words

Answer Hint

Foreign portfolio investment; capital gains taxation; investment inflows; market competitiveness; revenue implications; tax certainty; financial stability

Model Answer

Introduction

Foreign Portfolio Investment (FPI) provides capital to Indian equity and debt markets. Tax policy can influence the attractiveness of these markets, although investment decisions also depend on economic fundamentals and global financial conditions.

Potential Benefits

1. Investment Inflows

A lower tax burden may improve post-tax returns and encourage foreign investors to allocate more capital to Indian financial assets.

2. Market Development

Greater participation can improve market liquidity, facilitate price discovery and support access to capital for businesses.

3. International Competitiveness

Predictable and transparent tax rules can strengthen India's position relative to other emerging markets.

Limitations and Risks

1. Fiscal Revenue: Tax concessions may reduce government revenue, creating trade-offs with public expenditure priorities.

2. Volatility: FPI flows can reverse rapidly in response to global interest rates, geopolitical risks or changes in investor sentiment.

3. Policy Fairness: Tax changes should consider consistency, administrative simplicity and the treatment of different investor categories.

Way Forward

Any reform should be evaluated through evidence on investment responsiveness, revenue effects and market stability. Clear rules and stable tax administration are essential.

Conclusion

Capital gains tax reform may support investment, but its effectiveness depends on balancing market competitiveness, fiscal sustainability and equitable taxation.

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