

## Growth, of course

We put the dividend vs growth debate to rest with this conclusive study

Feb 21, 2019



Income seekers usually prefer the dividend option of debt-oriented funds as it gives them the psychological comfort of getting an 'income' without eating into the capital. However, this comfort comes at the cost of a higher tax outgo, thereby reducing the very income they are seeking.

The table below mentions the tax treatment of your investments in debt-oriented funds. As you can see, while you don't have to pay any tax on the dividend income, what you receive in the form of dividends is already after deducting the dividend distribution tax (DDT). Including the cess and surcharge, this tax aggregates to a hefty 29.12 per cent of the dividend declared. This works out to be much more than the capital gains tax you pay in case of a growth option, even at the highest tax bracket of 30 per cent. Let's understand this with an illustration.

Taxation of debt-oriented mutual funds

	Capital Gains		
Dividend income	Short term (Up to 3 yrs)	Long term (More than 3 yrs)	
Dividend distribution tax of 25% (plus surcharge and cess) to be deducted and paid by the AMC	Gains are taxed at 5%, 10% or 20% (plus surcharge and cess as applicable), depending upon which slab the investor falls in	Gains are taxed at 20% after providing the indexation benefit	

## Dividend vs Growth

Suppose you invest Rs 10 lakh each in the monthly dividend and growth options of ICICI Prudential Regular Savings Fund at the start of 2016. This fund has a regular dividend paying history in the last three years and therefore lends itself well for this example.

For the growth option, you create a monthly income stream by redeeming exactly the same amount as the gross dividend declared under the monthly dividend option. This basically means that their pre-tax monthly payouts are exactly similar. As the first chart shows, the growth option provides higher post-tax payouts even at the highest tax slab of 30 per cent. That's because in the growth option, tax is applicable only on the gains and not the entire redemption proceeds. On the other hand, in the dividend option, DDT is applicable on the entire dividend amount. Not only that, the value of investment is also higher in the growth option (see the second chart and table - Value of Investment).

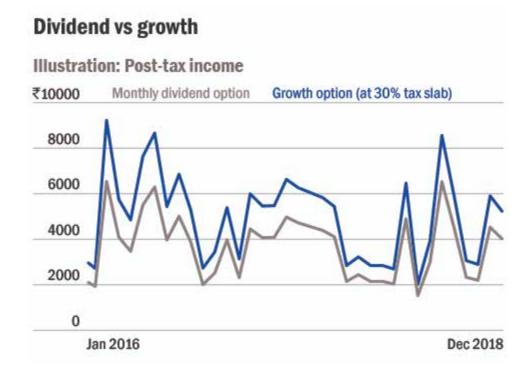


Illustration: Value of investmen	it
₹12.0 lakh	
11.5	
11.0	~~~ ~
10.5	
10.0	
9.5	
Jan 2016	Dec 2018

Monthly	Dividend option	Growth option
Amount invested at the start of 2016	Rs 10 lakh	Rs 10 lakh
Pre-tax income (2016-2018)	Rs 1.8 lakh	Rs 1.8 lakh
Post-tax income (2016-2018)	Rs 1.3 lakh	Rs 1.7 lakh*
Fund value at the end of 2018	Rs 10.2 lakh	Rs 11.1 lakh
*Assuming a 30% tax bracket		

Even a regular income seeker should invest in the growth option and periodically withdraw a part of his investment to derive income. This can be put on auto-pilot with a systematic withdrawal plan (SWP). But before you rush to exit from the dividend option of your funds, do consider the exit-load implications and time your redemption to avoid any extra costs.

Powered by Value Research Disclaimer of Axis Securities Limited:

market risks, read all scheme related documents carefully.



This Document has been prepared by Value Research. This document is not, and should not be construed, as an offer to sell or solicitation to buy any units, securities etc. by Axis Securities Limited (ASL). This document may not be reproduced, distributed or published, in whole or in part, without prior permission from Value Research. ASL does not guarantee that the document is complete or accurate and it should not be relied on as such. Investors should make his/her own research, analysis and investigation as he/she deems fit and reliable to come at an independent evaluation of an investment (including the merits, demerits and risks involved), and should further take opinion of their own consultants, advisors to determine the advantages and risks of investment. ASL, its affiliates, group companies, directors, employees, agents or representatives shall not be held responsible, liable for any kind of consequential damages whether direct, indirect, special or consequential including but not limited to lost revenue, lost profits, notional losses that may arise from or in connection with the use of the information in the document. Mutual Fund Investments are subject to