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GROUND VIEW

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STRUCTURAL CHANGES FOR A *BRIGHTER FUTURE*

GST . AADHAAR . DBT . TECHNOLOGY

PhillipCapital

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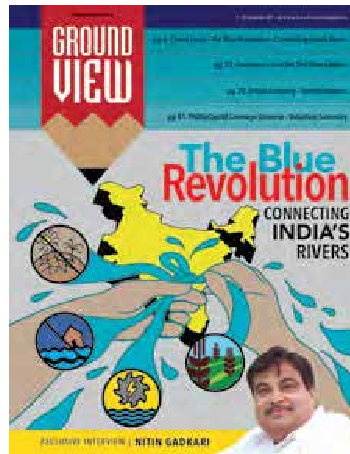

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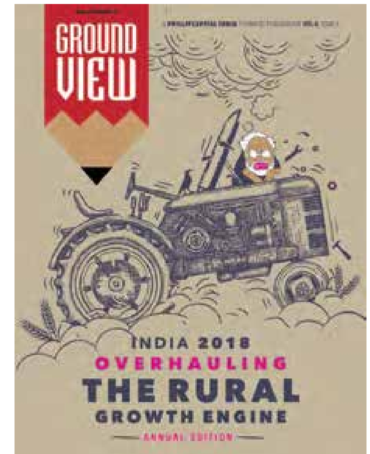

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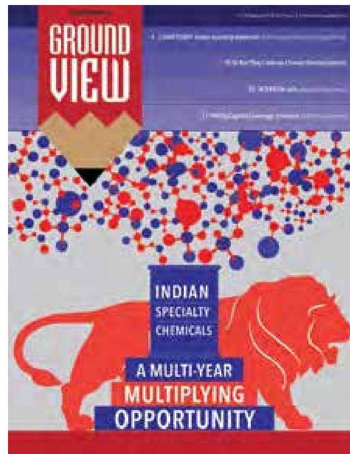

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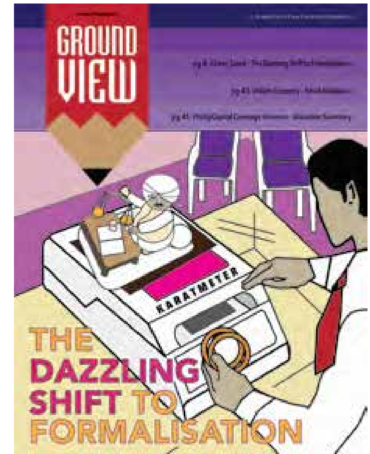

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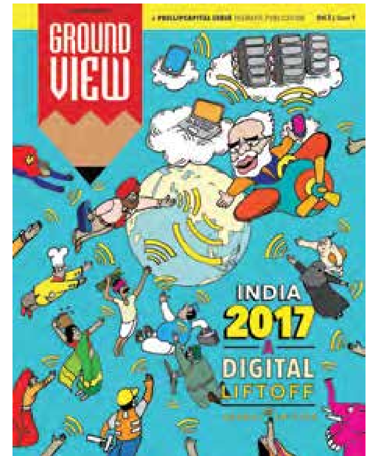
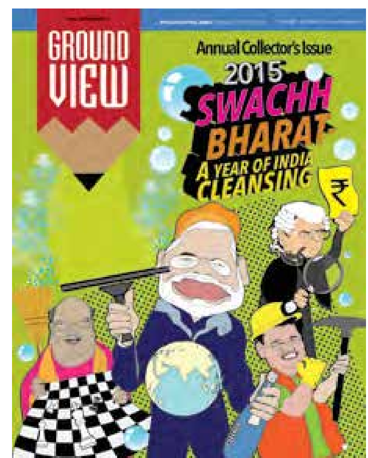


I am very pleased to present the sixth edition of our annual Ground View magazine to our readers, in which we have tried to explore emerging themes for 2019. The ongoing year will be a political one, with the general elections mid year; we hope for stability and policy continuity. The year that went by saw India transitioning – the country's economic and political equations underwent tremendous transformations. Many game-changing policies were implemented over the last few years, including GST, DBT, demonetisation, E-way bill, and axle-load norms – 2018 was the year when the structural impact of these policies was felt. Was it positive or negative? These schemes were aimed at raising the share of the organized economy by tracking financial transactions in order to widen the tax base and revenues. Through them, the government initiated the process of blocking/disincentivising financial leakages, black money, and the parallel economy. Their scale and intensity will only increase in coming years.

As these policies were bunched up, and implemented at a time when the Indian economy actually needed a stimulus due to the policy paralysis of the previous government, they dented business and employment. While the Indian economy remains one of the fastest growing in the world, its momentum suffered due to these structural changes. However, the way of doing business in India has undergone a reasonable change due to these policies. People are willing to switch to the organized structure of doing business, mainly because it has now become easier for the government to track and bring to book evaders and offenders. This has also increased compliance cost across businesses, along with additional stress from rising competition and changing technology. The result has been business consolidation – smaller businesses are struggling to survive and larger ones are gaining. The tax base is widening – its expansion should continue.



In this issue named "STRUCTURAL CHANGES FOR A BRIGHTER FUTURE" the PhillipCapital Research Team has tried to decipher ongoing changes in businesses and their economic impact. We travelled across India to bring our incisive analysis to you and we do hope you find it useful. Have a great year ahead!

Best wishes

Vineet Bhatnagar

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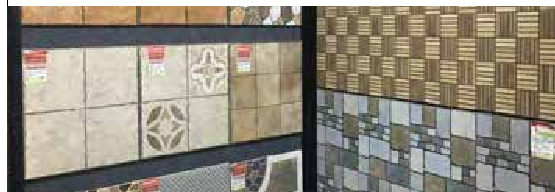

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STRUCTURAL CHANGES: FOR A BRIGHTER FUTURE

By ANJALI VERMA

Structural changes that have been taking place in India have made 2018 and its preceding years stand out. At the heart of these changes have been government policies. This was an interesting phase when the Indian government introduced various policies mainly to record or track financial transactions – the core objective was to strengthen the country's tax base (organised economy) and bring in fiscal savings. Through these policies, the government has created a system that has minimised regulatory leakages. These policies may not have been revolutionary or implemented in the best way, but in the long-term, as loopholes keep being plugged, they should pay-off and serve their purpose. **The ground reality is that over the last few years, the way of doing business in India has undergone a significant change due to government policies (eased considerably) and the paradigm shift underway from technological evolution.**

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A lot has been said about the timing, preparedness, and quality of these policy changes, which caused various challenges. However, the fact is that they have shaken up the previous methods of doing business in India. While new policies are facing resistance, the government's force and incentives have effected positive changes across businesses. Its ability to track offenders and plug leaks will make these policies more successful in the long-term. The ongoing (not-so-strong) economic growth trends are also attributed to these structural changes, as they have taken place across sectors. It is also noteworthy that the government rushed ahead with these policies when the Indian economy needed a push as it was in the midst of a political deadlock, weak business and consumer sentiments, and high inflation-interest rate environment. Some adjustment pain is still left – maybe a couple of years more.

The government, through policy framework, has laboured towards strengthening India's tax structure and addressing the black money issue.

These policies can be clubbed under the following heads:

- **Strengthening the tax base:** GST, RERA, and demonetisation.

- **Reducing black money:** Demonetisation, leading to a rise in digitization. While the objective of this move and whether it was successful is murky, people's mind-set towards digital transactions definitely improved after demonetisation. The government quickly followed up with a regulatory overhaul of digital payment platforms – there has been a surge in mobile wallets in India. Demonetisation has also led to a swell in financial savings.

- **Better traceability:** E-way bill, axle load norms, DBT

- **Incentivising organised business (modern trade):** Lower GST rates will push the unorganised sections towards becoming organised.

Based on industrial feedback, the government has been fairly amicable towards amending policy structures and compliance norms; various amendments have been brought under GST.

Businesses that are unwilling to adapt, innovate, and re-invent will find survival difficult

GST's success has been tepid so far – collections have fallen badly short of the government's expectations. However, policies have brought about other benefits such as rise in the number of tax payers (smaller businesses), reduced cash transactions, fear in the minds of offenders, trails of business transactions, and voluntary compliance. On-going structural changes will show results in time as processes are streamlined and mind-sets change. GST revenues should gradually trend higher.

The GV team travelled across India, looking at various sectors and interacting with stakeholders at all levels to gauge the impact of factors such as government policies on economic growth. These interactions indicated that businesses are affected by recent changes and are grappling to find their place – smaller businesses more, as they suffer due to rising compliance, taxes, technology advancements, lack of innovation, rising competition, and scale of volumes. Businesses that are unwilling to adapt, innovate, and re-invent will find survival difficult – these include small-scale real estate builders, grocers, unorganised FMCG players, and smaller consumer durable traders. Consolidation seems one way for Indian businesses to expand, but it could have an adverse impact on employment generation.

- In real estate, small-scale builders have been hit by RERA, GST, and poor liquidity. However, larger players are thriving.
- In FMCG, general trade (kirana shops) is under threat from modern trade due to GST, competition, and dependency on cash transactions (particularly after demonetisation).
- Small businesses in consumer durables sector are also suffering for similar reasons.

Over the last few years, while certain policies were affecting businesses negatively, the government contributed to the growth engine through infrastructure investments. Ordering and execution in roads and for metro railways has been strong. The capex cycle has picked up despite lack of support from the private sector. Infrastructure investment by states has also increased (particularly in metro rails and housing under PMAY). Cement demand has been strong due to robust construction activity, but the industry has been impacted due to poor pricing power, axle load norms (overloading has completely stopped), and rising competition.

New ordering pace has slowed for the roads sector for some time due to lack of funds and land acquisition. Few months of slippage can be managed. However, if this does not revive once the new government is in place and spreads to other sectors, capex cycle can be negatively affected.

Both centre and state governments have invested substantial funds and designed supportive policies for empowering and upgrading rural India – this includes roads, housing, health facilities, irrigation, agriculture infrastructure, and banking facilities. One of the biggest policy changes by the government is in the form of distributing subsidies through Direct Benefit Transfers (DBT). The current government incentivised the rural population to open bank accounts. This, along with Aadhaar card issuances, has made it possible to target the needy population and ensure that benefits reach them. The government's willingness to electronically transfer subsidies to beneficiaries' bank accounts has led to huge fiscal savings, which in turn can be used for rural development. The ongoing farmer stress (possibly not real) is due to lower output prices and rising cost of production. The sitting government will continue to offer more benefits to rural India so that it benefits in the upcoming 2019 general election. Consumption should remain stable to strong, particularly for consumer staples.

The automobile sector has been hit by higher insurance cost, the E-way bill, axle-load norms, and higher interest costs. It will remain under pressure due to BS-6 implementation (effective April 2020), which will increase current MRPs by about 15%. PVs will be least impacted while CVs and 2Ws will see greater impact in FY21. FY20 volumes could be better due to pre-buying, but this is not sustainable. Additional margin pressures will come from capex spends to roll-out electric vehicles (EVs) in coming years.

For now, it seems like the re-election of the BJP government at the centre for the next five years will be the best possible outcome for policy continuity and for the Indian economy. In fact, such a scenario should lead to more economic gains in the government's next term. If a non-BJP coalition government forms at the centre, growth could be damaged. The future course of growth will depend on the stability of the government followed by its policies.

BY DEEPAK CHITRODA

DBT: A RE-RATING CARD FOR FERTILISERS

DBT for fertilisers was rolled out on a pan-India basis from 1st February 2018, after a pilot stage that was implemented across 19 districts. However, it is not DBT in the true sense because subsidy continues to be reimbursed through the fertiliser industry, and not directly into the bank accounts of farmers as is the case with LPG subsidy. Nevertheless, the government has hailed fertiliser DBT (in its current form) a success. While media reports indicate that the industry claims subsidy arrears of about Rs 250-300bn, government has asserted that the outstanding is 'only' Rs 100bn. Despite challenges and delays, what GV gathered from its recent on-the-ground travels is that the new system is well appreciated by most and perceived to be effecting positive change. It seems to have already increased the accountability of stakeholders, including fertiliser manufacturers, wholesalers, and retailers, reduced subsidy outgo, and enhanced transparency because it is now possible to track the physical movement of fertilisers from the factory to the farmer. This has reduced the diversion of fertiliser for other purposes.

Previous system

- Sale was reported (for subsidy dispensation) when fertilisers were sold to wholesalers/retailers.
- Challenges created during this system included diversion of urea for non-agricultural use, imbalanced use of fertilisers, delay in subsidy receipts from the government, and protection of some legacy and inefficient plants.

Current system

- Sales are reported only after actual sale to farmers.
- Some negative impact on working capital cycle of the fertiliser industry due to a large subsidy backlog, inadequate subsidy provisioning in the Union Budget, limited subsidy inflows during off season, and shifting of subsidy realisation from point of dispatch to point of retail sale.
- For ongoing sales, the government is slowly starting to pay subsidy within a week or more.
- Challenges in DBT: Aadhar authentication failure, weak internet connectivity, delay in update of stock position by wholesalers, and stock reconciliation issues.
- Already observed positives: Fewer instances of retailers overcharging farmers, better reduction in diversion of subsidised fertilisers to neighbouring countries, and limited usage by other industries such as plywood after 'neem' coating.

Future

- Subsidy directly credited to farmers' bank accounts, just like LPG subsidy. In this system, farmers will be provided with recommendations about which fertilisers and how much to use based on the data captured in the PoS devices and correlating it with the soil health in that area.
- Challenges for a 'true' DBT rollout: Improper land records, large number of tenant farmers, and integrating the entire system for transferring benefits to farmers' bank accounts.
- Companies will become free from subsidy receivables and operate in the open market like other industries. Working capital costs will reduce substantially and margins will improve rapidly. Incompetent and loss-making companies would need to reform their business segments.

INDIA'S UREA PROBLEM

India suffers from a serious anomaly in the fertiliser policy framework.

Urea: The government directly controls urea. It fixes its MRP and its subsidy is variable. This has kept urea prices artificially low.

Phosphorus and potassium fertilisers: The government indirectly controls other fertilisers such as NP/NPK through the 'Nutrient Based Subsidy' policy of April 2010. Under NBS, the government provides a fixed subsidy and manufacturers have the freedom to fix MRP (more or less). Because the government provides only a fixed subsidy on these fertilisers and due to rising international market prices, their MRP has increased significantly.

Because urea prices are extremely low and other fertilisers are high, farmers have been overusing urea. There has created a serious imbalance in the use of fertilisers in India, leading to a weakening response of yield to fertiliser use, adversely affecting agricultural productivity.

Unloading of water soluble fertilisers in GSFC, Gujarat

Rolling out the DBT (direct benefit transfer) mechanism has had its share of problems, especially the ones faced by retailers/dealers across the country. However, today, the future of DBT seems bright. Mr Dharmesh, who runs a wholesale and retail fertiliser and agrochemicals business in a village near Vadodara, Gujarat, with a turnover of Rs 30-40mn, told GV, “Delhi door che saheb, pan lamba samye badha mate saru che” (a long way to go for DBT, but it will benefit everyone in the long term).

Banana plantation in Gujarat

To understand DBT, historical context is needed. In 1977, the government allocated subsidy worth Rs 0.6bn for the fertiliser sector with a view to support farmers by keeping prices low and stable. In subsequent years, it continued to raise subsidy allocation because of increasing production cost and capacities, particularly after 2004-2005, when oil prices started to rise. Over the years, polices evolved, and the government began to focus on farmers’ needs and improving industry-wide efficiency.

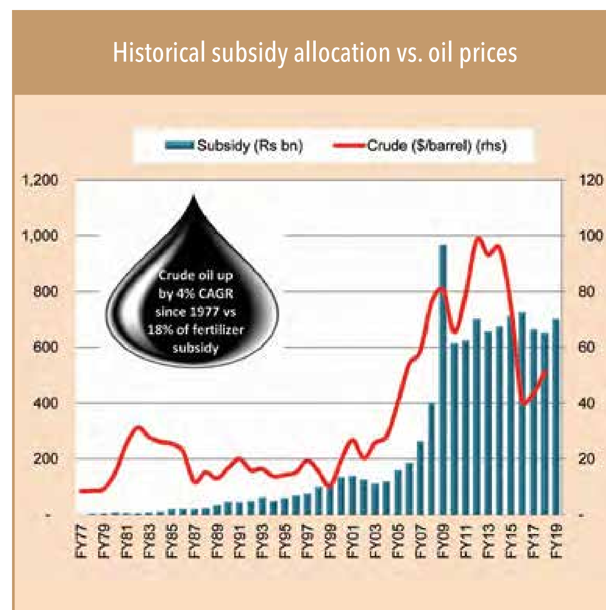
However, producers’ working-capital needs increased substantially over the past decade, as the government continued to delay subsidy payments because of limited fund allocation in the budget. “Carry-over liabilities have continued to rise. They remain at about Rs 300-400bn, at least for the past 6-7 years, stretching the working cost for the industry,” said Dr Goel,

A SELECTED TIMELINE OF THE FERTILISER SECTOR IN INDIA

- **1977** The Government of India (GOI) introduces the fertiliser subsidy scheme due to rising prices (both finished and raw material) in the international market as oil prices rise. Subsidy to farmers is routed through the fertiliser industry for 'administrative convenience'.
- **1992** A joint committee recommends decontrol of phosphatic and potassic fertiliser with rising input costs. Also, imports of raw materials such as phosphate rock, sulphur, ammonia, and phosphoric acid are de-canalised.
- **'92-'93** Introduction of ad-hoc concession on phosphatic and potassic fertilisers with retail prices rising significantly.
- **2003** New pricing scheme for urea units effective. This scheme aims at greater transparency, uniformity, and efficiency in disbursement of subsidy to urea units. Implemented in three stages (2003-2004, 2004-2006, and 2006 onwards).
- **2007** Fertiliser monitoring system (FMS) to monitor sale of fertilisers up to wholesale dealers.
- **2010** Implementation of Nutrient-Based Subsidy (NBS) for phosphatic and potassic fertilisers by decontrolling MRPs – which means subsidy would be fixed while MRPs would be flexible). The aim of keeping subsidy fixed was to promote balanced fertiliser usage. However, because urea was kept out of the policy (urea has fixed MRP and flexible subsidy) it resulted in significant difference in MRP between urea and phosphatic and potassic fertilisers (almost 5x since 2010).
- **2013** New Investment Policy 2012 – to attract new investment in the urea sector by brownfield or greenfield projects.
- **2014** Amendment to New Investment Policy of urea in response to the industry's tepid interest. Policy terms and incentives are revised and led to at least a few serious players showing interest in investing in this sector.
- **2015** New Urea Policy 2015 for existing gas-based urea units introduced, in order to improve efficiency of each unit and reduce energy consumption. Also, mandatory production of 'neem' coating of urea introduced (up to 75%) to reduce industrial usage of subsidised urea.

  Pooling of gas prices for urea units introduced to deliver gas at uniform prices to all gas-based connected urea producers. This helped the government to save some subsidy and companies to better account for costs.
- **2018** Introduction of 45kg bags for urea, to reduce consumption and promote balanced usage of fertilisers.

CEO & Principal Consultant of MG Consultancy in Delhi. "Current issues of delayed subsidy will be over only after implementation of DBT in the true sense, and that is likely to take some time. There is renewed interest in the sector after DBT announcements, and many overseas clients are likely to show interest in India once they see a smooth rollout of DBT," he added.



Source: Industry, PhillipCapital research

ALL ABOUT DBT (Direct Benefit Transfer)

The government launched the DBT scheme in 2013 with an aim to pay subsidy directly to beneficiaries' bank accounts in food, petroleum, and fertiliser sectors. It spends about 2% of GDP as subsidies for these sectors. After seeing successful implementation of DBT for LPG, the government was keen to implement a similar structure for the fertilisers sector. It started with pilot projects in a few districts before going for a countrywide rollout to examine the various difficulties – such as multiple products with different subsidy rates, linking of land records, and the farmers' inability to pay full fertiliser prices upfront. The pilot project was implemented in 19 districts, in which companies were directed to distribute Point of Sale (PoS) machines to each retail shop. However, unlike the LPG version of DBT, in this version, subsidy is paid to companies rather than to farmers.

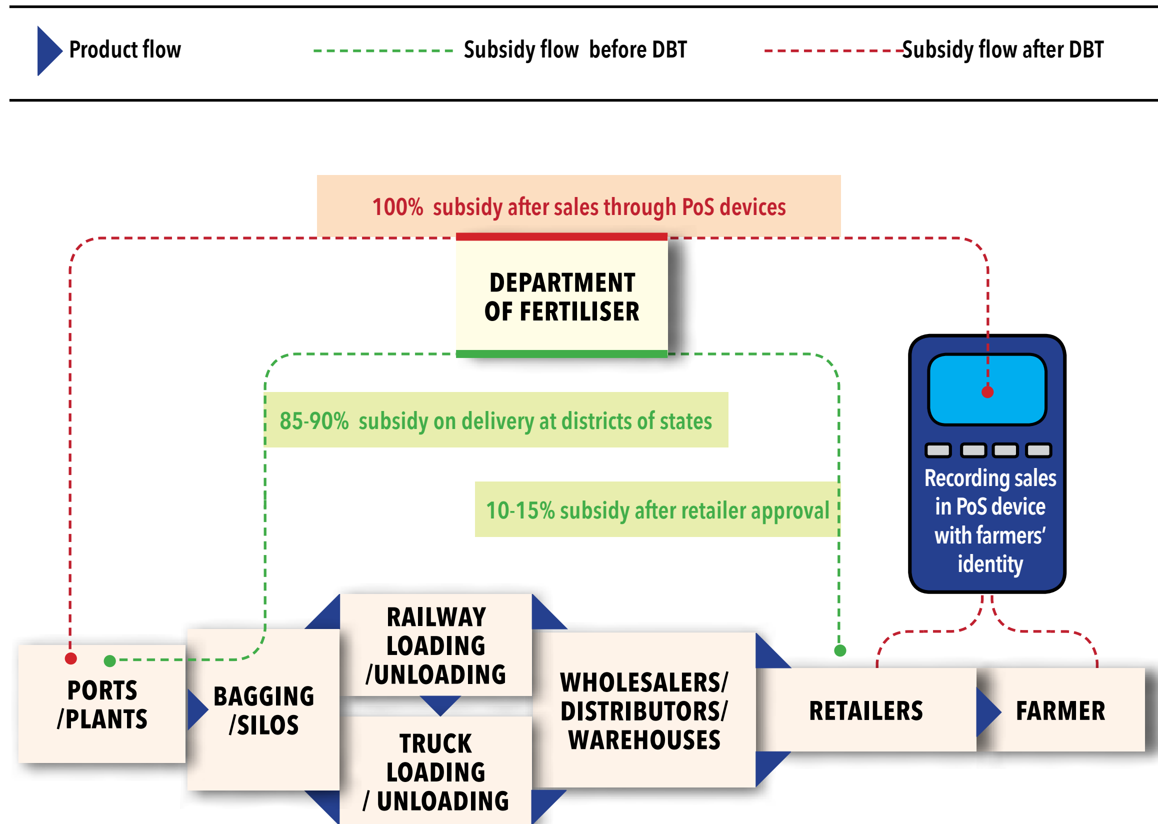
A retailer enters details of a farmer in a PoS machine in a village in Gujarat with Aadhaar authentication

Capturing every transaction...

Despite myriad issues and limited learning from the pilot project, the government fully implemented DBT in April 2018. Under this, fertiliser sales have to be conducted only through PoS machines by presenting the identity cards of purchasers (farmers) – such as Aadhaar, Kisan Credit Card, and Voter Identity Card.

In early 2018, companies were not able to procure PoS machines due to unavailability of stock. However, GV's checks with dealers in Gujarat, Maharashtra, and Uttar Pradesh revealed that machine availability is not a problem anymore. A General Manager, Marketing, of one of India's largest urea producers said that the situation is better, and that about 200,000 retailers across the country are not facing availability issues anymore.

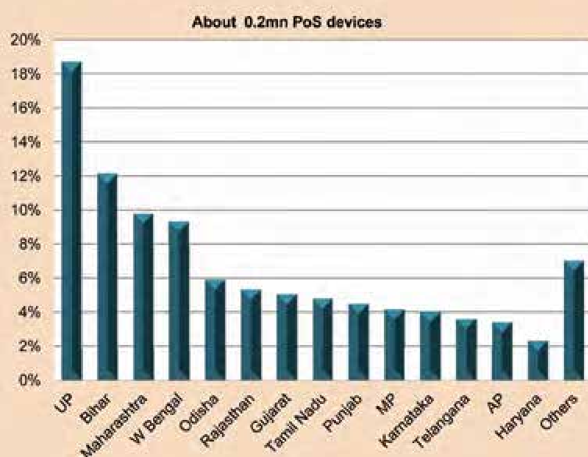
Subsidy flow before and after DBT implementation



Other major DBT-related issues

- **Connectivity:** In remote areas, retailers often face telecom network issues because of which they are unable to enter 30-40% of daily transaction volumes into the machines. Even according to the government's pilot project data, about 2/3rd of sales were manual and it took two or more attempts for about 40% of sales for authentication. A dealer in Satara, Maharashtra, with an annual turnover of about Rs 40-50mn said, *"Humko bina PoS entry karna padta hai kyoki peak season hai, nahi to kisan ki lambi line lag ja ti hai. Hum ledger me entry karte hai aur jab network aata hai tabhi hum farmers ko bula ke finger print lete hai* (we have to sell without PoS entry because it is peak season, otherwise there will be a long queue. We record sales in a private ledger and once the network is back, we call farmers to take a finger print for the PoS device."

State-wise share of PoS machines



Source:Industry, PhillipCapital research

Companies make sure that every transaction is recorded in order to get subsidy on time. Marketing staff of various companies in Maharashtra, Gujarat, and Haryana confirmed that they make sure that they record every transaction by retailers with the correct name, quantities, prices, and company names. Most expect network issues to resolve soon because the government's agency, National Informatics Centre (NIC), is working on this problem, and things have improved compared to early 2018.

Most of the time, a Satara dealer's PoS machine didn't have network

Due to network issues, an entry into a PoS machine in Satara took longer

- **On-time subsidy realisation:** Besides connectivity, companies need to make sure that retailers enter the right volumes against the company name, because subsidy realisation is processed accordingly. Delays in putting entries into PoS machines make it difficult to reconcile inventories and raise real-time invoices, which lead to a delay in subsidy payments. A senior marketing officer for a company said, "We need to work extra these days to make sure that retailers enter the sales volumes sold by us via PoS machines". Subsidy settlement is also taking longer than a week (as proposed by the government) due to the auditing and reconciliation process. According to one of the top management employees of a NP/NPK/NPS producer, "Subsidy of about Rs 250bn was paid against bill generation of about Rs 274bn and for balance, invoices couldn't be generated. Apart from a delay in the initial payment of subsidy under DBT, prior subsidy bills along with freight, are not yet paid to industry"

A large dealer in Satara with his suppliers and PhillipCapital's analyst Deepak Chitroda

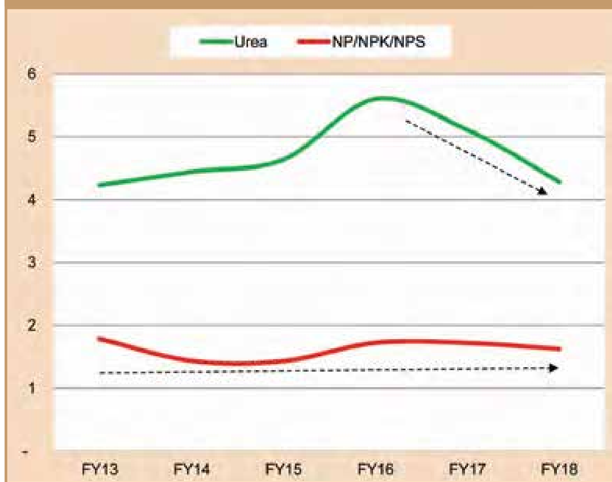
- **Working capital scenario under DBT:** Companies are facing working-capital issues regularly. With DBT in place, they will only receive subsidies after actual sales. In the previous system, 90-95% of subsidies were claimable after volumes were delivered to state districts. The seasonal demand for fertilisers arises in kharif and rabi season, which adds up to about six months in a year. With DBT in place, companies will only realise major subsidy inflows during these peak seasons, and for the rest of the year, they would need additional working capital to run their businesses.

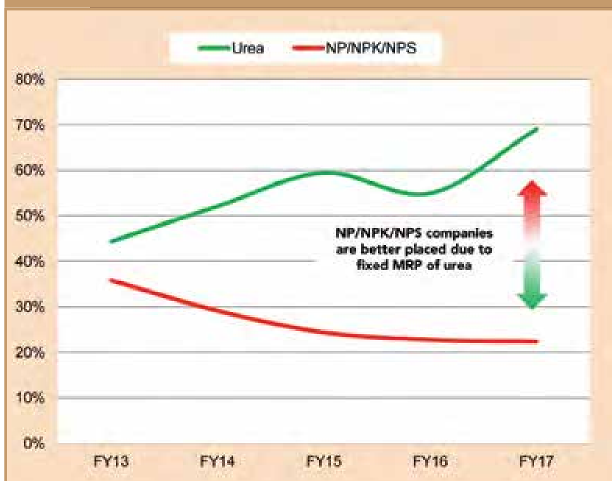
  Therefore, urea producers are demanding to extend working days (from current 45 days that the government currently considers under subsidy payment for fixed cost) to 180, in order to receive some relief on working capital cost. Also, urea producers can't afford lower capacity utilisation due to technical reasons. "We can't change production rapidly during off season, given the production technology and distribution plans set by the government every month. Also, energy saving can only be maintained or improved if plants operate at an optimum level," disclosed a Finance Officer of a urea producer. NP/NPK/NPS producers are expected to be least impacted so far, because of the flexibility of production between various grades.

The health of the industry....

Urea producers are facing unnecessary hardships due to the government's total control – under urea subsidy, companies realise MRP from farmers after sale and the

A Satara fertiliser dealer has stocked inventory for rabi demand

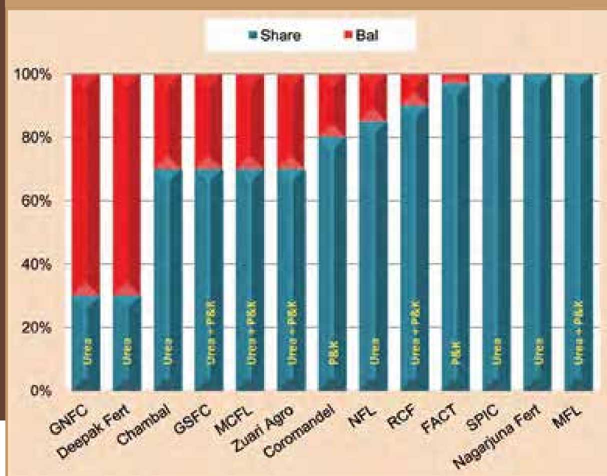




balance of their realisation as subsidy (about 70% of realisation), which is always delayed. To overcome higher receivables from the government, many producers such as GSFC, Chambal Fertiliser, Zuari Agro, and GNFC have diversified into trading and chemicals, which has reduced the 'subsidy' contribution to their revenue to about 60-70% from 100% earlier.

NP/NPK/NPS producers are in a much better place vs. urea producers due to partial decontrol, under which incremental cost is passed on to farmers via an increase in MRP. The contribution of subsidy (as % of revenue) for some major phosphate fertiliser companies (Coromandel, GSFC, Deepak Fertiliser, Zuari Agro) is only about 20% now, and it has declined rapidly over the past 5-6 years with a fall in subsidy allocation.

The duration of receivables for phosphate fertiliser producers is also much lower at about two months vs. four months for urea producers. "We have not gotten used to living in the higher working-capital environment, but DBT, in the true sense, will surely change this negativity for the sector. We expect that within 2-3 years, things will be visible on the ground," said a senior public sector official.



The way forward

In its current format, there are various challenges towards implementing DBT – from connectivity to recoding sales on a real-time basis. Industry experts told GV that 'true' DBT implementation is not going to be easy and involves setting up a entire new infrastructure, convincing stakeholders right from farmers to companies, developing and stabilising an IT technology platform, defining farmers, and mapping land, among other hurdles.

However, there is evidence that some benefits are already visible even with the current format of DBT – these include higher volumes of subsidised urea not being sold for industrial usage and illegal sales in nearby countries such as Nepal and Bangladesh reducing, resulting in some savings in terms of subsidy for the government. A large dealer of fertilisers in Madhya Pradesh with an annual turnover of about Rs 2bn confirmed, "Yes, things have changed. Large dealers are not taking any risk of selling to industrial customers, farmers are getting urea at MRP only, and neem coating is limiting industrial usage."

Additionally, a study conducted by NITI Aayog during a pilot project in 2017 revealed that about 300 retailers in several districts of Madhya Pradesh, Himachal Pradesh, Rajasthan, Telegana, and Andhra Pradesh didn't renew licences after the Aadhaar card linking process was initiated. This indicates that the DBT process is pushing stakeholders to move towards accountability and transparency with fewer chances of bogus transactions.

It will take some time before the replication of the LPG DBT model is implemented in other sectors

The government's aim is to achieve transparency and traceability in the system. The PoS data recorded can be leveraged to pass on other welfare benefits of the government such as farm loans, procurement of crops from famers at MSP, recommending usage of agriculture inputs, etc. However, gains will be realised only if the subsidy reaches the ultimate beneficiary (the farmers) who then make informed decisions based on recommendations from the data captured including status of soil health, type of crop sown, and farmers' buying patterns.

"We are aware of the current status for DBT and we are in the process of stabilising the first phase"

– A senior policy maker in the ministry

Companies are now receiving subsidy more or less within a week, which is much better compared than previous systems when it used to take about 2-4 months. Discussion are on for the next phase of directly transferring subsidy to farmers, but this will take some time – may be another year, as challenges such as integrating land records, soil health cards, and banks accounts of farmers need to be overcome, said a senior person involved in policy making.

Many industry market participants seemed optimistic, despite upcoming challenges for the government, and most expect direct transfers to take about 2-3 years. However, a marketing person of a urea producer made an interesting comment. "Political environment in 2019 will play a big role for pushing DBT; if the present government is re-elected, than we may see a much faster DBT rollout," he said.

BY VISHAL GUTKA & PREEYAM TOLIA

GENERAL TRADE: DOWN, BUT NOT OUT

Analysts Vishal Gutka and Preeyam Tolia travelled across north and west India to meet distributors and wholesalers in general trade (GT) and senior representatives of modern trade (MT) and cash and Carry (C&C) chains. The aim was to understand if the inherent competitive advantage of GT in this moment of crisis was sustainable. The analysts received interesting insights on why the traditional (indirect) channel continues to remain under pressure despite the impact of demonetisation and GST being largely over. Their story also sheds light on how modern trade is grabbing all opportunities to make inroads into the US$ 650bn+ Indian retail market.

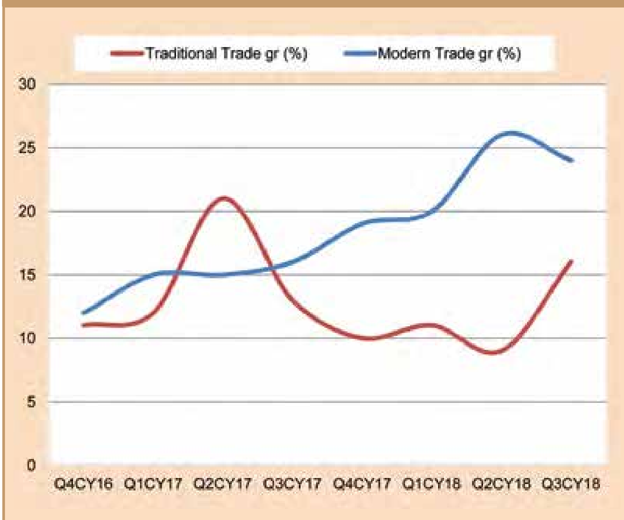
Traditional distributors facing the heat from e-commerce and MT

Traditional distributors are finding it difficult to compete with new-age e-commerce and MT players, including C&C chains. The latter are using disruptive techniques to garner market share and customers. C&C players, who are fully compliant, are moving quickly to fill the void left by the reducing penetration of traditional wholesalers, who are finding it difficult to compete in a fully compliant era. In fact, they have become quite aggressive after November 2016 when they saw big opportunity come knocking when demonetisation had reduced the availability of cash, which led to several wholesalers downsizing their businesses. These businesses, which are largely cash driven and work on wafer-thin margins, have come under significant pressure due to increased compliance with GST norms, lower availability of cash, and payment of higher income taxes (which they were evading earlier).

"Business has slowed significantly after demonetisation and GST implementation. Increasing competition from organized wholesalers (cash and carry) and aggression by the modern-trade channel (D-Mart) is making matters worse for us"

– Ashish Jain, a mutli-brand distributor in Ujjain, MP

Modern trade's metamorphic rise in past few quarters



Source: Nielsen

Mom-and-pop shops under tremendous pressure too

Re-emergence of C&C channels (organized wholesalers), modern trade's aggressive store expansion, and the price-discounting strategy adopted by well-funded ecommerce players for customer acquisition have added to small shopkeepers' woes and dented general trade the most. Apart from competition, day-to-day challenges such as unavailability of labour, spiralling operating costs, and higher compliance requirements after GST are pushing them towards the brink of closure. Some have found a via media by renting out their establishments or letting other businesspeople run them for a share of profits. "I have given my shop located at Virar East (60-70kms away from Mumbai) on rent after D-Mart entered in October 2018. I earn more in rentals in the long term than what I would make from running the shop," said Bakul Dedhia, 55, who has been involved in the retail trade for more than three decades. Dedhia said he took a pre-emptive call after seeing many small shops closing down in Virar West when D-Mart started operations there.

Prominent Modern Trade outlets in India

Distributors' and wholesalers' pain = Cash & carry's gain

C&C is a membership-based retail format, where goods are purchased in bulk directly from FMCG companies and sold to mom-and-pop retailers and HORECA (hotels, restaurants, and catering services) players at prices lower than what distributors/ wholesalers quote. Most C&C outlets put a minimum floor value of Rs 500 for purchases. Anybody with a Gumasta license (Shop & Establishment License) / FSSAI License / GST registration certificate can become a C&C member; so kirana retailers, HORECAs, and co-operative housing societies can become C&C members as well.

C&C chains are able to sell at lower costs vs. traditional distributors because: (1) Economies of scale gives them cost / procurement advantages, (2) distributors give 15-20 days credit to retailers. C&C players do not. They receive spot cash payments, and (3) distributors have to deploy manpower in order to serve retailers. C&C works on a pull model – retailers come to the C&C outlet to pick up goods. Of these advantages, the last one has changed slightly. While so far, most C&C chains were operating on the pull model, lately they have deployed their own sales staff to take orders from small retailers. Most make free deliveries to stores (shops) if order size exceeds Rs 5,000.

Retailers are using C&C players to squeeze better terms from distributors

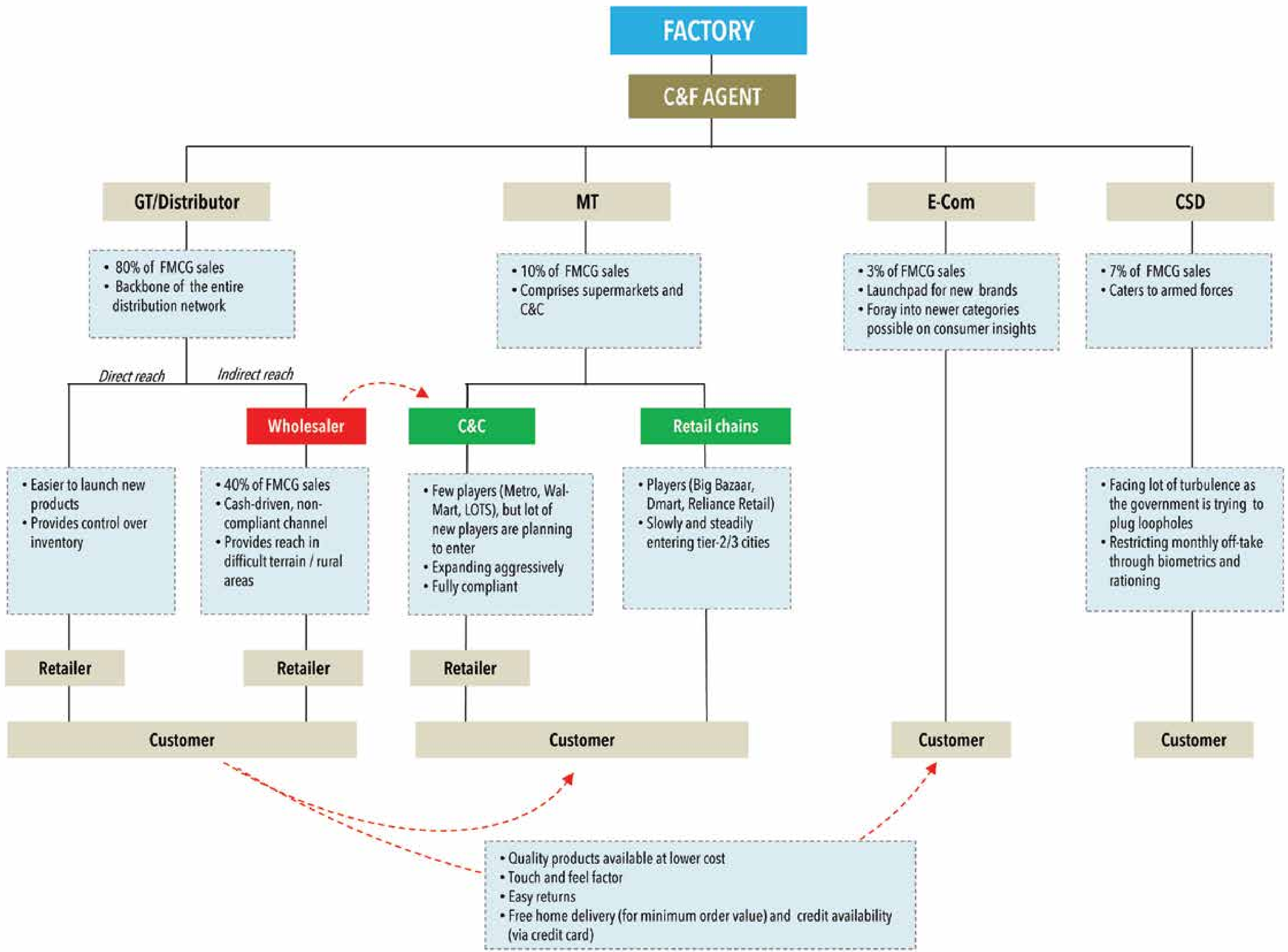
Retailers are smart buyers, and their final purchase from distributors or C&C chains depends on the best deal being offered. Distributors usually provide goods to retailers on credit for 10-15 days. Retailers sell these goods to customers in cash and use this cash to purchase goods from C&C chains, which offer a little more discount than distributors so retailers don't mind paying them on the spot (C&C chains don't offer credit). This practice by retailers has led to distributors' business volume reducing to an extent. More importantly, with additional bargaining power, retailer are demanding more credit terms from distributors, negatively affecting their ROIs.

C&C players have forged a symbiotic relationship with retailers....

With traditional retail being cash driven, demonetisation led to customers' shifting loyalties to modern trade from general trade. Moreover, GT retailers were reluctant to accept digital payments or give credit to their customers (especially during demonetisation, when it was needed the most) since they were not receiving any credit from distributors/ wholesalers because they in turn were affected by shortage of notes.

In the subsequent crisis in GT, C&C players are handholding retailers and are actually acting as consultants to them, instead of just vanilla suppliers of goods. They provide retailers with POS terminals worth Rs 30,000-35,000 (interest cost for these is borne by the C&C chain) which in turn helps small

General distribution structure for FMCG in India



shopkeeper to manage credit given to customers, communicate with them about promotions and offers, accept digital payments, and auto-replenish inventory for top-selling SKUs.

Special programmes such as "Mera Kirana" (Wal-Mart), "Kirana Success Centre" (Metro), and Happy Shoppers (Booker Wholesale) are helping retailers to modernise their stores with better utilization of infrastructure, which in turn helps to optimize space and drive a better assortment of products.

With the assistance of C&C chains, kirana stores are even planning to take on modern trade and e-commerce players in urban areas and tier-1 cities. However, C&C chains will find it difficult to compete with general trade in tier 3/4 cities due to lower offtake and difficult terrain.

While selling to kiranas, for most top-selling SKUs across categories, C&C chains try to match the price quoted by modern trade outlets so that end customers stay with general trade. GT outlets are displaying digitized boards highlighting the discounts offered on key SKUs.

ShopKirana
Empowering Retailers

- B2B e-commerce platform
- Connects individual retailers with brands, ensuring retailers get products at discounts.
- Brands can directly connect with retailers for promotions and NPD, bypassing distributors and wholesalers altogether.
- Provides credit facilities to retailers through tie-up with NBFCs, which is otherwise very difficult for them.

HUL

- HUL has recently started directly supplying goods to retailers, under which distributors only act as facilitators.
- Launched an app called 'Shikar' that enables traders to place orders online and not wait for distributors to visit their stores.

WAL-MART'S MERA KIRANA

- Under this programme, Wal-Mart creates zones in its Best Price Wholesale Stores that are designed to resemble a modern kiranas (mom-and-pop grocery store).
- It serves as a model for kirana store owners to replicate when it comes to assortment and placement. Wal-Mart also sends its teams out to Kirana stores in order to work directly with them.
- Since Best Price Wholesale Stores require huge space (4 acres) and the process of getting approvals and performing due diligence for setting up stores is tedious (used to take four years, now takes 2.5), it is focusing on setting up more fulfilment centres for kiranas. These fulfilment centres are housed in warehouses operated by third-party logistics firms and they can start functioning within 60 days. With increasing scale and more such centres, the quality of service to GT is likely to improve in coming quarters.

"The focus is on the omni-channel strategy and digitization of kirana stores. The stores need to look much better and inviting, and we want to transform them into self-service stores. We are partnering with suppliers to sell them at 10-15% lower than MRP and pass the benefit on the consumers to compete with the D Marts of the world" – Arvind Mediratta, MD and CEO, Metro Cash & Carry.

Tapping their balance sheet strength, C&C chains are making loans available to small kiranas via tie-ups with banks. These retailers would not otherwise receive easy credit from the system, especially after the IL&FS crisis. Kotak Mahindra Bank has tied up with Metro C&C for credit cards that will enable retailers to avail a 15-day credit for their businesses, which is slightly impacting distributors as of now.

...however, aggressive expansion by C&C chains has also started hurting kiranas to some extent

Some of the end customers are directly buying from C&C (by-passing retailers), since current flaws in existing regulations allow such purchases of goods to be made.

"Housing Co-operative societies, who are actually allowed to buy items only for official functions (AGM/ festivals) misuse cards (two cards allocated per co-operative

C&C chains have aggressive store expansion plans

No of stores	Country of origin	CY14	CY18	Future plans
Metro	Germany	16	27	Plans to open 50 stores by 2020
Walmart - Best Price	USA	20	23	Plans to open 50 stores by 2021
LOTS	Thailand		3	Started Jul '18. Plans to open 15 stores by '21

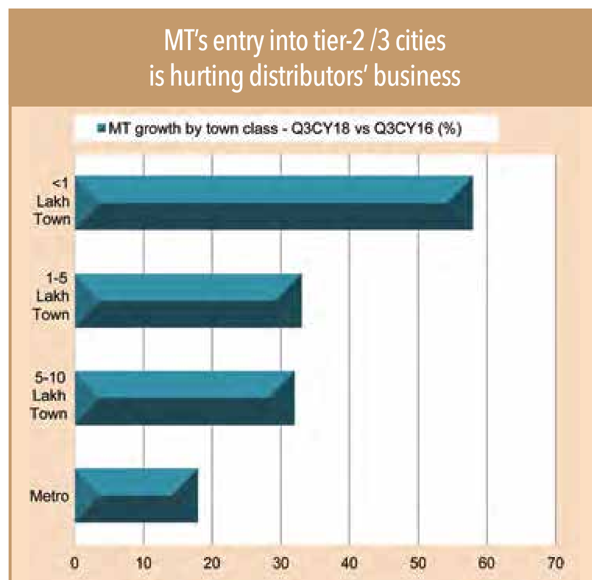
Source : Economic Time, Business Standard

society) given to them. Most members residing within the co-operative society actually purchase goods from C&C chains for their own household consumption," said a sales executive of a prominent C&C chain.

Registered Business Users (e.g. practicing CAs, lawyers) can avail membership cards from C&C chains based on their Gumasta License. In theory, these users are allowed to make purchases for their offices, but they give cards to employees for personal monthly household shopping. However, so far, this damage is limited as only consumers and employees staying near C&C stores come to purchase goods; carrying goods from the C&C store to residences is a task in metro/tier-1 cities.

Aggressive expansion by MT has affected distributors negatively

Modern Trade's presence was earlier restricted only to metro/tier-1 cities, so FMCG companies preferred dealing with MT through distributors instead of creating a separate channel for them. However, increasingly, FMCG companies seem inclined to deal directly with MT, as the latter have expanded their scale of operation to tier 2/3 cities. The direct approach helps FMCG companies in better product placements, pushing New Product Development and blocking competitors' products.



MT's entry into tier-2 /3 cities is hurting distributors' business

Source: Nielsen

"Demonetisation was a black swan event for the Indian economy. Among many challenges, the biggest disruption was caused in the distribution network for FMCG companies" - Lalit Malik, CFO, Dabur India

Credit crunch during demonetisation led to customers shifting loyalties to MT

GT's resistance towards digital payments during the crisis led to customers permanently switching to modern trade. In addition, during demonetisation, kirana retailers were not able to provide credit to customers, when it was needed the most to ensures stickiness. This was because kiranas were not receiving any credit from wholesalers/distributors who were also badly affected by the shortage of notes.

Why have customers stayed with MT despite GT stabilising?

- Touch and feel factor: In MT, customers have plenty of time to touch and feel products, which may not be possible in kirana shops.
- MT has better quality products at relatively lower costs.
- MTs have increasing tie-up with credit card companies.
- Relatively easy returns/replacement guarantee vs. kirana stores, whose operators show extreme reluctance to take back goods once sold.

"I had purchased return gifts on my daughter's birthday, but due to excessive rain, not as many party guests turned up. D-Mart (with no questions asked) accepted all my unused purchases and immediately paid cash to me" - Amruta Chadawar, Thane

Other problems that distributors are facing

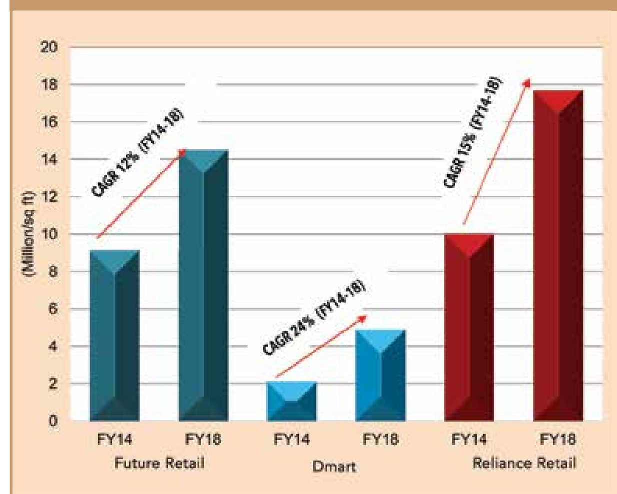
Distributors margins flat due to deferred price hikes by FMCG majors

Most of the FMCG companies have deferred taking price hikes in the past two years because of a weak macro environment (demonetisation) and benign input cost environment. After GST implementation, FMCG companies were sceptical of taking price hikes, as they feared being prosecuted under anti-profiteering provisions of the GST Act and price increases remained elusive for the FMCG industry.

Limited price hikes by FMCG companies during the past few years has dented distributors' margins

Source: Nielsen

CAGR for Reliance Retail



Source: Company

"In FMCG, distributors' margins are linked to MRPs. Since the last two years, business have remained flat and companies have taken limited price hikes. Due to this, our cost of servicing has increased significantly. Moreover, companies are now dealing directly with MTs against the earlier practice of MT business being through distributors. This is adding to our woes," said Pratik Jadeja, a Jamnagar-based distributor for Parle and Nirma.

Next-gen is not always keen on the family business, adding to GT woes

Modern Trade is overcoming all disadvantages it had vs. General Trade such as free home delivery and credit to end customer. However, lack of interest from the second generation of shop owners with improved employment opportunities in the organised sector and worsening economics of running a retail store is a unique problem for GT.

Distributors do not prefer single brands or companies that operate across categories

Distributors are not comfortable dealing with single-brand companies – since slowdown in the category's growth rates and increased competition dents growth. Single brands can have flattish sales, higher cost of servicing, and more category-related competition. This leads to frequent churn of distributors for companies such as Bajaj Consumer Care and Colgate. They are also not easy with large companies like HUL, since the number of SKUs that they need to keep across categories and the effort involved is humungous.

HPC pips food

Trade partners prefer HPC companies over foods brands. This is because there is higher complexity involved in foods distribution as food is more prone to breakages, has lower shelf life. However, food has higher returns.

Distributors are gravitating towards multi-brand FMCG companies with a strong HPC portfolio (such as Marico and Emami) and are less inclined towards food companies.

"Colgate has disproportionate shelf space in D-Mart stores, as we want to provide tremendous value to customers in Naturals and CDC (our core portfolio) and restrict Patanjali from making any further inroads"

– Shivraj, a Colgate executive inside D-Mart's Mulund store.

Incidentally, with distributors not enthusiastic about taking on single-brand/multi-brand companies, product availability at small shops has suffered. This has also driven customers towards MT. Conversely, product availability has never been an issue for MT, since such outlets directly deal with FMCG companies.

"When retailers returns products after expiry or breakage to distributors, they immediately pay the retailers. However, for distributors, it is a cumbersome process to get money from the company because there is a detailed audit process for reimbursements, which takes 3-4 months. This negatively affects the distributors' ROIs", said Alok Singh, a distributor in Jabalpur, MP, who is less inclined to take on food distribution.

Will General Trade continue to hold the fort despite challenges?

The going is difficult and structural changes are taking place, but the end is NOT near

Sceptics have been predicting the death knell of General Trade (kirana stores) after the emergence of Modern Trade two decades ago, and with the advent of well-funded e-commerce players. With aggressive expansion by MT players to every corner of the country due to improving profitability, this time they are predicting certain death for small stores. Small retailers are facing many challenges. Foreign funded start-ups are deploying strategies of deep discounting, cash back, convenience, and better service to make inroads into India's US$ 600bn retail market. Kirana owners' next generation is showing disinterest.

For 3/4-tier cities and towns, kirana stores are sometimes the only viable option

For now it seems like traditional kirana stores will continue to prevail in rural and tier-3/4 cities as lower off-take on a per-capita basis, difficult terrain, and other complexities will make it tough for online players/big retailers to operate in these areas. However, in urban areas, these stores are not doing very well due to the deteriorating economics of running a retail store.

Even so, the sheer convenience that these kirana stores provide is unbeatable for now.

"I cannot travel to the D-Mart store for every single purchase. It is located five kilometres away. For e-commerce, you have to have minimum order size and it takes at least one day"

- Shraddha Gada, 36, a homemaker from Thane (Mumbai)

E-commerce is a threat, but cannot yet match the convenience of kiranas

E-commerce is stepping up its game to deliver faster deliveries. BigBasket delivers the next day while Amazon Prime Now provides deliveries in just two hours in some cases – but conditions apply, such as minimum order size and annual membership fees, which restricts the adoption of online market places quickly. Moreover, many purchases are impulse driven on an 'as and when required' basis. So it is nearly impossible to put everything on the 'monthly supermarket list'.

Close relationships with customers is a key USP of kirana stores

In the past, many modern trade players have suffered because taste and preferences varies every 100kms in India, making it difficult to manage inventory efficiently and to scale-up. As kirana shop owners usually have personal relationships with customers, and know what goods can be sold in their area – they are at an advantage. Modern Trade players such as D-Mart and Future Retail have been able to synchronize their supply chain systems to some extent with regional tastes and preferences, but it will be next to impossible to replicate the relationships that kirana owners have with their customers.

New brands eventually need GT for reach, but MT/ecommerce provide inexpensive marketing platforms

Pushing new brands through MT

MT players such as D-Mart have pushed the emergence of new brands such as Chedda Chips, Paperboat Chikki, and Chitale UHT Milk, which offer quality products at reasonable prices. It is typically a win-win situation. For brand owners, the advantage is that they receive traction via BTL (below the line) activities by using discounts to gain consumer acceptance; most are not certain about above the line (ATL) activities delivering desired results. For MT players such as D-Mart the attractive offers given by new brands ensures that these MT outlets earn better margin and manage higher throughput vs. incumbent mainstream-category brands. However, nobody benefits as much as customers – they get to try new products at relatively lower costs. Once brands start gaining traction, brand owners gradually start reducing the discount on MRPs and eventually price their products at only marginal discounts to MRPs.

In India, developing a brand from scratch has proven quite difficult. In the past decade, the number of new brands that have been nurtured are limited – these include Paperboat, Pulse, Gowardhan, Paytm, and ID. Factors that have hindered the development of brand include strong distribution reach of existing players in GT, and higher search costs (earlier it was difficult to get information about ingredients/application of a particular product).

Traditional retailers do not like to stock new brands since these block their working capital and impact their ROIs. Most of the customers are not aware about new brands since companies have limited ad spends and budgets for sampling when the brand is in its infancy. Sometimes, existing incumbent FMCG companies may adopt defensive tactics (trade-related schemes / discounts) which may lead to new products not receiving shelf space in kirana stores.

E-commerce provides an effective and economical launch pad for creation of new brands

E-commerce provides the distribution network for new brands. With the explosion of the internet and 4G devices, new-age brands such as Beardo in hair-care; BoAT in consumer electronics, and Yoga Bar in foods have started to emerge. E-commerce provides the distribution network for new brands. Most brands generally operate in the mass-premium segment, since it coincides with an online customer base. Prohibitive search costs were an entry barrier and advantage for strong brands in the non-internet era.

"An online launch gives companies an idea of how their product will work once they take it offline, as they get feedback from consumers and can accordingly tweak the product. At the same time, it costs less for companies to launch products online than offline"

\- Prashant Agarwal, Jt. MD at Wazir Advisors.

Even incumbent FMCG companies are using e-commerce for their new category forays and for differentiated products as it offers the following advantages over launching in General Trade:

- Much cheaper. There is no need to fill the trade channel ahead of the launch or tackle returns if the new launch does not work.
- Can produce goods based on demand.
- Easier to get direct customer feedback. Can make the product better based on feedback, before a full-throttle offline channel launch.

"Beardo started in the 'online only' format, but it has now started expanding offline too. It will target salons and modern trade formats initially. Over a period, we will also target neighbourhood salons with our offerings," said Ashutosh Valani, Co-Founder, Beardo.

Once exclusively e-commerce brands reach a certain scale, they will begin to face challenges on the growth front (e-commerce is only 3% of overall FMCG sales) and will have to take the GT route for further distribution expansion. These brands generally tend to forge M&As with companies that have a strong GT network. For making these e-commerce brands large and taking them to next level, that is making them available all over India, they need the support of a massive distribution network, which only general trade can provide. Modern trade and e-commerce have their limitation in terms of reach.

Private labels and brands

Some MT players such as Future Retail have started focussing on creating private labels (through Future Consumer) which are at par in terms of quality with existing brands. Future Consumer is using its captive distribution network (Big Bazaar, EasyDay, Heritage Stores which contribute 80% of Future Retail sales) to create a number of in-house brands such as Tasty Treat, Golden Harvest, Clean Mate, Kosh, and Karimq, based on customer insights, prominent shelf space, innovative packaging, and reduced time to market.

Can private labels become a bigger threat to existing FMCG companies?

Private labels have become a very important source of income for e-commerce players and comprise 10-15% of their total revenue. Amazon and Flipkart currently have private labels across categories and have plans of these labels a bigger part of their businesses.

Amazon introduced its first private label (in batteries) in the US market in 2009 and gradually it has started expanding into other categories. It currently has eight key private label brands – Symbol, Myx, House & Shields, Arthur Harvey (clothing), Vedaka (grocery), Presto! (Home care), Amazon Basics and Solimo (accessories and other household items). Amazon's Presto! (Paper

towels), Mama Bear (Diapers) and Amazon Essentials clothing are among the top-rated private labels in the US provide tough competition to existing incumbents.

Historically, customers in mainstream categories do not easily shift loyalties unless the challenger brand is superior or is offered at a significant discount to well-established brands. Amazon's strategy is simple – it offers quality products across categories at reasonable prices and with its umbrella branding strategy, customers are quite comfortable trying Amazon products.

Amazon India is looking to scale up its private labels rapidly in India by entering into new categories every year. However, in India, its strategy is to target categories that are relatively under-penetrated and less serviced. "The role of private brands for us is to fill in specific need gaps that are not being serviced," Amazon India head Amit Agarwal.

If private labels of e-commerce companies (B2C) start gaining traction, then these companies can simultaneously forward integrate (websites provide a retail counter) and backward integrate (in-house manufacturing), cutting through lot of inefficiencies in the system. With increasing profit and scale, e-commerce companies can become detrimental to the existence of FMCG companies.

Recent policy changes have limited online market place players (Amazon, Flipkart) from selling any product in which it has direct/indirect control over inventory. However, in the past, e-commerce companies have found a way to work around stringent conditions.

Alternate business models for new-age brands: Case studies

Millennial customers are demanding products that are fresher, natural, and more convenient to use than pre-existing products available in market. In order to serve this unique demand, new age companies (ID Fresh Foods and Raw Pressery) with the support of technology and data-analytical tools are creating differentiated brands and distribution networks, which are completely different from the traditional distribution structure.

"Our product is our hero. When the whole world is investing in R&D to extend the life of the product, we have a business model to sell fresh," said PC Mustafa, MD, Co-Founder, ID Fresh Foods.

Most of the fresh food & beverage companies need to have their manufacturing facilities and procurement centres near their demand centres. This becomes difficult for large FMCG companies to replicate, given lower returns on higher capex requirements.

Why did ID Foods decide to take the non-traditional route?

ID Fresh Foods started out by selling just 100 packs of fresh idli batter a day in Bangalore. It now sells 55,000 kgs a day across 12 cities in India. What is its USP and what is the reason for such phenomenal growth? The ready idli and vada batter market is largely unorganised. These unorganized manufacturers maximize profits by adding soda and preservatives. ID Fresh Foods supplies superior quality natural batter, which is standardised and free from soda and preservatives.

Idli batter has a low shelf life of just three days and following a conventional distribution network would have led to many complexities. Instead, ID Foods directly supplies goods to General Trade (no distributor) and has thus been able to reduce wastage (0-1% vs. industry average rate of 10-20%) and has ensured customer stickiness.

Using geo-tagging on their product packs, ID Foods is also able to forecast daily sales at a particular outlet, and supplies accordingly. Moreover, usage advanced data analytics, it predicts road traffic, which in turn optimises the route of delivery vehicles. This helps to reduce wastage and fuel cost.

Raw Pressery disrupted the juice segment

Raw Pressery retails 100% organic, fresh, cold-pressed juices across 13 cities in India. It also exports to Doha, Qatar, Dubai, Abu Dhabi, Saudi Arabia and Singapore. Cold-pressed juices use the hydraulic-press technique to extract juice, which ensures maximum retention of nutrients. Such juices have a shelf life of only 21 days under specialised refrigeration (4-8 degrees) which is not possible for traditional kirana stores, who usually switch off refrigerators at night. Therefore, for now, Raw Pressery has focussed on Modern Trade outlets, as these are able to provide specialized refrigeration facilities. In order to promote the brand in the GT channel, Raw Pressery is looking for strategic outlets that have the potential to sell 300-500 litres per month, in which case it can provide free 50-litres chillers as a part of its promotional activity.

To conclude, GT is on the back foot for now; MT/e-commerce on front foot

Demonetisation and GST have brought in a lot of turbulence within general trade, but this has created platforms for new brands to emerge due to increasing proliferation of modern trade and e-commerce. Although companies are increasing their focus on these emerging channels, they need to be careful about any channel becoming so large that it begins dictating terms. For e.g., if FMCG companies become too dependent on modern trade, then they can ask for relaxation of credit terms and conditions, which will dent return ratios.

While MT and e-commerce is making firm inroads into urban and metro cities, in rural and semi-urban areas (which account for 60% of India's population) GT will continue to be relevant. MT and e-commerce players will find it difficult to operate in these areas given the complexities in supply chain, lower purchasing power, and difficult terrain.

BY NITESH SHARMA & VIPUL AGRAWAL

Pictures from past GV editions

EV BUG COULD BITE INDIA SOONER

More than a year ago, GV's December 2017 edition had highlighted how electric 3Ws are penetrating even villages of Bihar. This time around, GV began its journey by meeting pioneers of E-rickshaws based out of Delhi and Jaipur to understand costing, how and from where they source various parts, and economics of an E-rickshaw. Meetings with a range of dealers in Delhi NCR, Jaipur, Varanasi, and Vijayawada provided a flavour on how auto demand and consumer sentiment has panned out across the country. Overall, demand and sentiment remained subdued, more so in the urban region, with some revival likely from mid-January when the marriage season begins in a big way, dealers said.

EV mania – Blast from the past

GV analyst Nitesh Sharma has always been an ardent supporter of electric vehicles. In an earlier GV edition, he detailed his visit to Norway where he drove across the country in an EV to get first-hand knowledge about why the EVs ecosystem is so successful there. As such, he was super excited to see E-rickshaws flooding India, even in the hinterlands of Bihar. If lithium-ion battery prices collapse, then the infra set up and EV adoption in India could increase surprisingly rapidly, given the low cost of ownership. This is already visible in the fast-paced adoption of E-rickshaws in India.

Meeting the man who brought the first E-rickshaw to India

"E-rickshaw has come a long way from 100% imported models from China to 95% localised production in India," said Mr. SK Jain, a large E-rickshaw manufacturer based out of NCR. Justifiably proud, Jain believes that he was the first person to start the E-rickshaw revolution in India when he imported his first consignment from China in 2011. Now, after over seven years, his vehicles are nearly fully localised – leading to 40%+ cost savings due to scale benefits and improvement in the quality and availability of spare parts. He said he and other Indian manufacturers were now giving Chinese manufacturers a run for their money in the international markets too. Over the years, Jain has exported his E-rickshaws to European, African, and some Asian countries, and firmly believes that the EV story has tremendous mileage in India.

Here is Jain's explanation of why E-rickshaw's picked up and how their total cost of ownership is much better than traditional fuel-based rickshaws – the MRP of the E-rickshaw is Rs 120,000. The Delhi government offers a subsidy of Rs 30,000 on one E-rickshaw per person. Financing (75% of total value) is easily available for these vehicles – another catalyst. Also, these rickshaw's have four lead-acid batteries and offer a range of 100km per charge, leading to a running cost of just Rs 0.3 per km. This, he believes, is the key reason for strong demand for E-rickshaws.

Jain Power Corp' E-rickshaw with c.95% Indian parts

Differential and axlehub imported from China; costs Rs 2,500

Electric motor imported from china; costs Rs 3,500

Controller/motherboard is imported as well; costs Rs 1,800

Mr. Jain was working on a lithium-ion-battery-based rickshaw. However, he cited a Mr. Kundan from Jaipur, who was already selling L-ion based vehicles. As it happened, Mr. Kundan was very happy to display his new offerings – E-rickshaws already running on lithium batteries. Mr Kundan believes there L-ion E-rickshaws have a whole bunch of advantages over lead-acid ones. With the new lithium batteries, his rickshaws are able to achieve 90% more efficiency than lead-acid batteries; this figure was 60% a year ago. Mr Kundan said that with L-ion there were no acid spills, batteries were light-weight (30% lighter), and fast charging (takes just two hours to charge up to 90% vs. 7-8 hrs for lead-acid batteries). However, lithium-ion battery based rickshaws cost Rs 50,000 more than lead-acid ones. Kundan believed that if L-ion battery prices were to fall further, his demand would pick up faster.

Indians have found a way around charging difficulties

E-rickshaw manufacturers, dealers, and drivers in different cities confirmed that EVs can become a preferred choice, with even the rural market adopting E-rickshaws rapidly. There is a lot of uproar about the lack of charging infrastructure in India. However, surprisingly, it is really the cost of the batteries and vehicles that will be a deciding factor on how EVs pan out in India. It was amusing to see how E-rickshaw owners and drivers managed their charging needs the Indian way (jugaad). Drivers typically pay Rs 100 a day to small unorganized players who manage their overnight parking and charging at this price. If these unorganised players can find a way around limited charging infrastructure, then large OEMs can surely manage.

With the recent launch of Mahindra Treo, 3Ws should see rapid electrification, much before what Dalal Street analysts are expecting, igniting an EV revolution in the country.

Imported differential axle-hub set

A lithium-ion battery is 1/4th the size of a lead acid one used in E-rickshaws

Comparison: Lead acid, lithium, CNG three wheelers

	Lead Acid battery	Lithium Battery		CNG Rickshaw
		Local made Rickshaw	Mahindra Treo	
Cost (INR)	**1,20,000**	**1,60,000**	**2,40,000**	**2,40,000**
Passenger Capacity	6	6	3	3
Weight Capacity (kg)	600	600	450	400
Fuel	Electricity	Electricity	Electricity	CNG
Engine/ Motor	Electric Motor	Electric Motor	Electric Motor	Combustion Engine
Charging time	7 hrs	2 hrs	4 hrs	NA
Fuel Cost/ km*	0.35	0.46	0.50	2
Range	90km	60km	130km	NA

* Fuel cost for E Rickshaw includes electricity cost plus charging point rental

An almost empty showroom decorated in anticipation of heavy footfalls during the festive season. According to this dealer, on the same day last year, his showroom was packed with customers

Hero dealers are flush with inventory; expect recovery from the second half of January

Two-wheelers: Increased insurance premium takes a toll

High discounts and higher inventory was visible across two-wheeler dealers. Higher insurance premium have elevated prices for consumers. With India being extremely price sensitive for most products, not surprisingly, customers have stalled buying vehicles, especially those from rural regions. Urban dealers were able to manage to a certain extent, as financing is widely available. However, the rural segment struggled as financing for the customer profile in these areas was difficult. Mr. Singh, a dealer of Hero Motocorp, said, *"Sirji, gaav ke log motorcycle lene ke liye lambe samay tak paisa jodte hai, ek dum se 3000-4000 rupay aur lana unke leye mushkil hota hai* (village people save money for a long time to purchase a motorcycle, a sudden increase of Rs 3000-4000 is difficult for them)". "*Gaav mein customer profile weak hai, is liye financing sirf 25% gaadiyo pe hoti hai* (the customer profile in villages is very weak; generally only 25% of my sales are financed)."

Many dealers said that two-wheeler companies have widely used BBND (billed but not delivered) in November and December. "Sir, *company ke sales manager jabardasti BBND karwa rahe hai retail sales dikhaane ke liye* (company sales managers are forcing us to use BBND to show retail sales and low inventory)," said a Hero dealer. In BBND, dealers mark inventory as sold, despite sales not really taking place.

To lure reluctant customers, Hero had rolled out discounts of up to Rs 3,000 on its scooters and its Glamour portfolio. However, higher insurance premiums have acted as a damper – with most dealers highlighting flat (at best) November-December 2018 retail sales. Dealers griped about more than 60 days of inventory, which has been eating into their margins. "High inventory has increased our financing cost and the dealership had to rent a godown at Rs 100,000 per month to keep additional inventory. We are currently running into losses and don't see any hope yet," said Mr. Agarwal – a large Hero dealer in Uttar Pradesh who was sitting on two months of inventory. "We have cut our December wholesales by 75% in order to streamline our inventory, yet weak demand has taken a bigger toll," he added.

When probed about the performance of Hero's newly launched scooter and premium motorcycle, Agarwal said, "The key problem is that customers don't consider Hero's scooter and premium motorcycle, which is why footfalls and enquiry are low. The company will have to undertake some big marketing to lure customers". Dealers see retail sales picking up from the end of January, when the main marriage season begins.

Varanasi and Jaipur TVS dealers were happy with their sales, crediting their success to a great product portfolio

TVS: Best of the lot

The largest TVS dealers in UP and Rajasthan region were the only 2W dealers that seemed relaxed. These dealers had a reason to rejoice – demand for TVS' scooters – Jupiter and Ntorq – has been better than the industry; this, despite TVS not offering any major discounts to push sales. TVS' dealers praised the company's management for not bombarding them with inventory, which their peers were apparently doing. Most dealers ended the year with normal inventory (one month) while registering a growth of 5-10% in November-December.

Pulsar: Bajaj's lone warrior

Bajaj's 5-5-5 scheme helped boost sales. The scheme offered 5 years of free 'own damage' insurance, 5 free services, and 5 years of free warranty. Bajaj dealers were happy about how this scheme initially helped them outperform the industry – with 5-10% growth during the festive season. However, come December, momentum fizzled out. What really worries dealers is where Bajaj will take its Pulsar portfolio, and if it might see some brand dilution.

Bajaj: Steep discount helped sail through, but dealers remain worried

Bajaj diluted its Discover brand by launching multiple engines and variants under it. Few dealers were worried that Pulsar might see a similar fate. Interestingly, while Bajaj dealers were holding relatively lower inventory, it was still at 5-6 weeks. Also, financers (apart from Bajaj Finance) were staying away from financing Platina/CT100 due low resale value.

Honda Motorcycles and Scooters: Focus is back to scooters

Dealers were happy about the company's newly rolled out strategy. A visibly elated dealer, Mr Singh said, "*Company ko ab samajh aa gayaa hai aur puraa focus scooter pe hi rakhegii, motorcycle ab secondary hai, scooters leke Honda number 1 banegi* (the company has now understood that it needs to focus mainly on its core strength of scooters; with this approach, Honda will become the number 1 player)". Improving road quality in rural areas and Honda's ineffectiveness in dislodging Hero in motorcycles are believed to be the main reason for its shift in strategy.

MHCVs – no respite

Dealers and fleet operators were sombre. MHCV sales have been strong due to elevated discounts over the last year, attractive financing, GST-offset benefits, and robust fleet demand. However, there is now an oversupply situation because of strong tonnage addition and full implementation of increased axle load norms by October-November. This, along with slowing financing, sluggish fleet operators revenue, and higher diesel prices, dampened festive demand. Industry participants said that fleet operators were getting up to 120% LTV on MHCV financing, but from October 2018, banks and NBFCs turned cautious about this segment. They now offer 80-90% LTVs, at best. Also, dealers said that most new buyers have down-traded

their purchases after the increase in axle-load norms and that discounts currently stand at life highs.

Small and mid-level operators appeared the hardest hit among the lot due to high operating costs. Large fleet operators and single-truck owners were able to cope by operating on thin margins. An operator from Mumbai (fleet size of 45 trucks) said that he has bought 18 trucks in the last 14 months due to high discounts but is now running only 30 trucks, that too at a loss, because of oversupply in the market and competitive prices.

M&M is slowly gaining ground and becoming a popular brand with large fleet operators due to its mileage guarantee experience and good drivers' experience in the Blazo series. A fleet operator who recently added Mahindra Blazo and Bharat Benz vehicles in his fleet said, "*Jaha driver Tata aur Ashok mein din ka 300 km chalata hai, wahi pe Mahindra aur Bharat Benz mein din ka 400 km aaram se chala leta hai aur isme dono ka fayada hota hai*".

Passenger vehicles: Heavy discounts to lure customers, liquidate inventory

Maruti: Urban dealers faced fall in volumes (by up to 10% in Q3FY19), while (in a trend divergent from 2Ws) rural dealers posted strong growth. However, most dealers said that Maruti had to buy growth by offering larger discounts. A dealer from rural Uttar Pradesh saw 15% yoy growth in sales and said "Is baar company ne kafi discount diya hai aur isiliye sales acha hua hai warna mushkil tha (this time sales were good mostly because of discounts, otherwise things would have been difficult)". While inventory was high in November (most dealers said 6-8 weeks), lower December wholesales and strong discount-led retails caused inventory across dealers to fall to 3-4 weeks. Dealers expect strong growth from February.

M&M: A dealer in Jaipur said he was expecting rejuvenation in sales from Marazzo as it was 'a very good vehicle' that was properly positioned in its category. However, his dealership sold only 90 vehicles in the initial three months. Dealers said that Marazzo did not find a place among customers because the new Ertiga stole the show. In most other states Marazzo was doing reasonably well. Ex-Marazzo, most dealers saw a flat to double-digit drop in their retails.

Tractors: The only silver lining

Tractor dealers were the happiest in northern India. Being under priority sector lending, they were the least affected by the NBFC liquidity crunch, unlike the MHCV segment. These dealers saw strong retail offtake and inventory was as low as 2-3 weeks. However, this wasn't the case with southern markets, where retails have been sluggish and inventory has been high.

Tyre dealers: Vietnamese tyres are gaining momentum, but restricted by supply constraints

Tyre dealers in Delhi are facing tough times as their sales fell by 40% due to GST, Green Tax, and "restricted entry of trucks", an Apollo tyre dealer confirmed. Indian tyre companies have increased prices by 10%+ in the last three quarters to Rs 40,000 (for a pair of truck tyres) whereas Chinese tyres (from Vietnam and Thailand factories) are available at Rs 30,500 per pair. Imported tyre sales have gone up in Delhi transport market to 2,000 per month from 1,100 per month earlier, because of this wide gap in pricing. However, given capacity constraints, dealers do not see any major increase in imports.

Tyres from Vietnam

EVENTS 2019

BY NEERAJ CHADAWAR

JANUARY

Jan 14th - 27th - Tennis Australia open

Jan 15th - March 4th - Kumbh mela, Allahabad

Jan 18th - 20th - Vibrant Gujarat Global Summit 2019

Jan 22nd - 25th - World Economic forum, Annual Meeting, Davos

Jan 24th - ECB monetary policy meeting

Jan 24th - 30th - IMTEX 2019 - Machine tools, Bangalore

Jan 29th -30th - FOMC meeting

FEBRUARY

Feb 1st - Vote on Account in Parliament

Feb 2nd - 3rd - Sula Fest 2019, Nashik

Feb 7th - RBI Monetary Policy Meeting

Feb 20th - 24th - Aero India Show 2019 - Ministry of Defence, B'luru

Feb 27th - Mar 1st - Indian Ceramics Asia '19 Trade Fair, Gandhingr

Feb 28th - Mar 2nd - ACREX India 2019 - AC & HVAC Event

Feb 28th - National Accounts Data (GDP)

MARCH

Mar 1st - US China, 90 days trade negotiation window ends

March 23rd - April * - IPL 2019

March 7th - ECB monetary policy meeting

March 19th-20th - FOMC Meeting

March 29th - Brexit day

APRIL

First Bi-monthly RBI Monetary policy meeting*

Rabi Harvesting Begin

IMD - First forecast on 2019 Monsoon *

OPEC Meeting, Vienna, Austria

April - May * - 2019 General Election

Apr - May * - '19 Assembly Elections– AP, Odisha, J&K, Arunachal, Sikkim

April 10th - ECB monetary policy meeting

April 12th-14th - IMF/World Bank Meeting

April 17th - Indonesian General Election 2019

April 30th - May 1st -FOMC Meeting

MAY

US-Iran Oil Sanctions Waiver expire

May 18th* - Australian Federal Election

May 23th -26th - European Parliament Election, 2019

May 26th - July 15th - Tennis French Open

May 30th - July 14th - ICC Cricket World Cup 2019

May 31st - National Accounts Data (GDP)

*Tentative

JUNE

Second Bi-monthly RBI Monetary policy meeting*

IMD - Second forecast on 2019 Monsoon *

June 8th-10th - Vibrant India 2019, Pragati Maidan, New Delhi

June 18th - 19th - FOMC meeting

June 28th-29th - G20 Summit, Osaka Japan

JULY

Kharif Sowing

July 1st- 14th - Wimbledon

July 25th - ECB monetary policy meeting

July 30th- 31St - FOMC Meeting

AUGUST

Third Bi-monthly RBI Monetary policy meeting*

Aug 1st - Sep 16th - Ashes Cricket Series, UK

Aug 26th - Sep 9th - Tennis US Open

Aug 30th - National Accounts Data (GDP)

SEPTEMBER

20th Sep- 2nd Nov - 2019 Rugby World Cup, Japan

Sep 17th -18th - FOMC Meeting

Sep 12th - ECB monetary policy meeting

OCTOBER

Fourth Bi-monthly RBI Monetary policy meeting*

Rabi Sowing

Oct- Nov* - 2019 Assembly Election– Maharashtra, Haryana

Oct 18th-20th - IMF/World bank Meeting

Oct 21st - Canadian federal Election

Oct 24th - ECB monetary policy meeting

Oct 27th - Diwali festival Lakshmi Pujan

Oct 29th - 30th - FOMC Meeting

NOVEMBER

Kharif Harvesting

World Bank - Ease of doing business ranking *

Nov 14th- 17th - ACETECH Mumbai 2019 - Asia's Largest architecture, building materials, design & decor exhibition

Nov 29th - National Accounts Data (GDP)

DECEMBER

Dec* - 2019 Assembly Election in Jharkhand

Fifth Bi-monthly RBI Monetary policy meeting*

Dec 10th - 11th - FOMC Meeting

BY DHAVAL SOMAIYA

PARADIGM SHIFT IN GROWTH DRIVERS

Annuity and PMAY emerge as drivers of Indian real estate amid continued slump in the residential segment, ongoing NBFC crisis, and lax RERA implementation

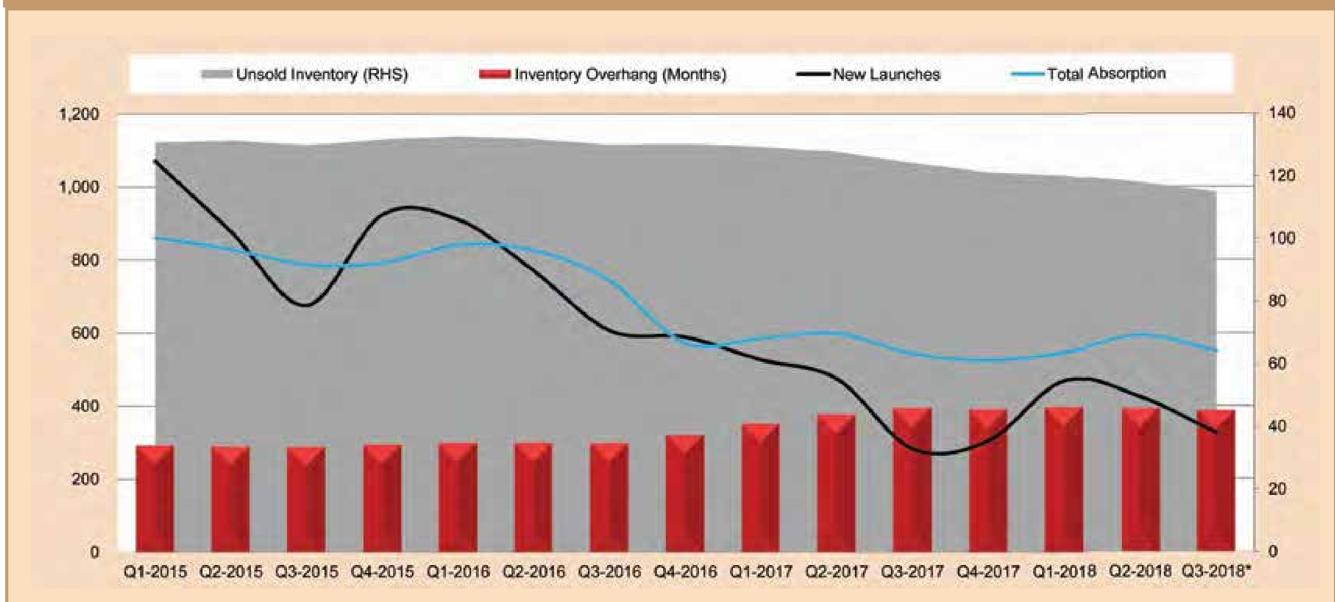
Residential sector: Weak revival; further price correction unlikely

After a bull run from 2000-08, the Indian real estate sector entered a bearish phase. It had just started to show some signs of revival in early 2016, when a series of structural and regulatory changes (demonetisation, RERA, GST, and most recently, the NBFC liquidity crisis) pushed the sector into an abyss.

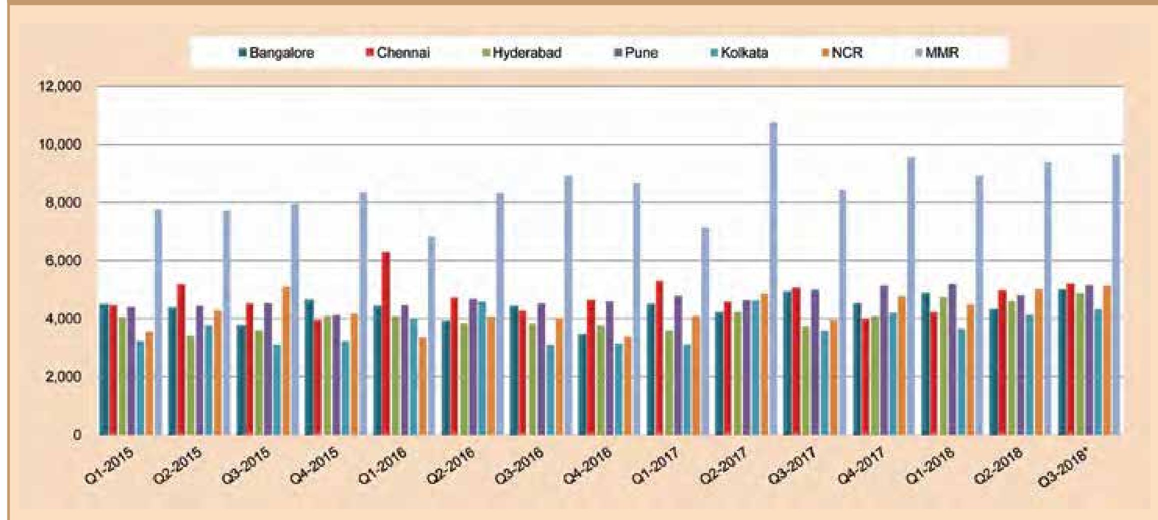
CY17 had been a very sluggish year due to RERA implementation, GST, and demonetisation. In CY17 new launches in top-8 cities dropped by almost 45% yoy to 185mn sq. ft., while total absorption dipped 25% to 262mn sq. ft. Despite a strong H1 CY18 (supply up by 25% yoy to 116mn sq. ft., overall price trends over Q3 CY17 and Q3CY18 for various cities have been flattish.

With the price appreciation gains drying up, 12% GST on under-construction flats, and compulsory registration of the unit as per RERA, the real-estate sector is undergoing a massive transformation. It is reshaping itself for a shift to end-user-led demand from investor-led demand previously. Pricing power may not return to the sector in the next 8-10 quarters because of a massive inventory overhang, a sluggish economy leading to lower end-user demand, and investors refraining from investing in the sector as an asset class.

2018: Mild revival signs evident with falling inventory and demand outstripping supply



Source: Knight Frank, Phillip Capital Research



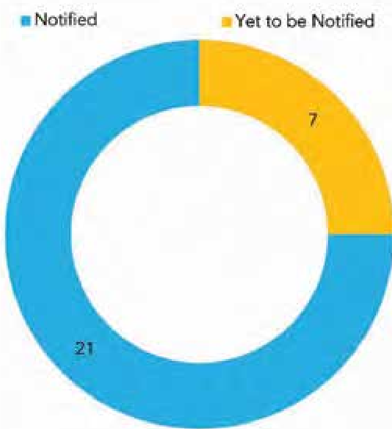
Flattish price trend: An indicator of transition from pricing play to volume play

Dwarka Expressway (NCR): A ghost town with massive inventory overhang and very low absorption

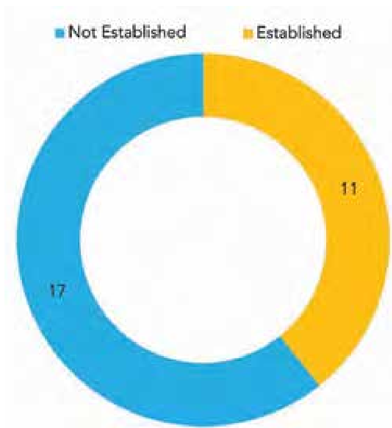
The sector may see consolidation as small developers and 'land-owners-turned-developers' face liquidity shortage, lower IRR (due to RERA), and higher cost of compliance because of RERA. Meanwhile, Tier-1 players, flush with liquidity, may also drive consolidation as these players have access to cheaper bank funding and most of them have ended up raising money via QIB/equity infusion by global players.

Yet, conditions apply – successful implementation of RERA and resolution of the NBFC liquidity crisis are important factors towards consolidation. Despite being a landmark reform, and even after more than two years of its passing, RERA has failed to make a mark. As land is a state subject, the implementation of RERA has been left to the states. However, with the developer community's 'influence' in the political world, many states have been lackadaisical towards implementing RERA, or are even trying to bypass it altogether. While 21 states have notified RERA norms (eight haven't), only four states have implemented it in true sense. The situation in Union Territories has been similar. So far, only Delhi has been able to complete the RERA setup (in November 2018). A few examples of states dragging their feet about RERA – West Bengal has enacted its own 'Housing & Industry Regulation Act. Kerala is planning to follow suit. Goa, which has been able to implement RERA norms, has only one person on its RERA 'committee'.

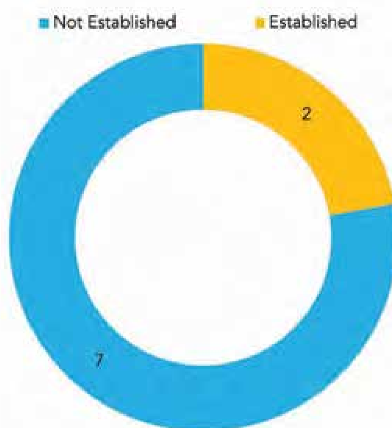
Seven states haven't even taken the first step towards RERA implementation



Permanent regulator: Only 11 states have finished step-2 of RERA implementation



Permanent regulator: Only 2 UTs have finished step-2 of RERA implementation



For the ailing residential segment to revive and for protecting the rights of home buyers, it is crucial that RERA implementation takes place as planned.

NBFC crisis: A ticking time bomb?

The NBFC liquidity crisis has been casting dark shadows over the past quarter and the real-estate sector is expected to take some heat because NBFCs have stalled all fresh lending lines along with the existing lines' drawdowns over ALM concerns. For a sector of its size and magnitude, liquidity hasn't been a concern for real estate in the past. However, after demonetisation and RERA, developers started facing liquidity issues due to the nature of reforms, seizing up of investor-led demand due to the slowdown in the sector, and steep price correction due to the massive inventory overhang and developer inventory facing steep competition from cheaper inventory released by panicked investors. This was the time when NBFCs stepped up to fill the void and started lending aggressively to the real-estate sector – this lending has seen 26% CAGR over the past two years.

LRD is a term loan offered usually to property developers against rental receipts from lease contracts with their corporate tenants. Such a loan is based on the discounted value of the rentals and the underlying property value

Based on research on these regions – NCR, MMR, Pune, Bangalore, Ahmedabad, Indore, Hyderabad, and Chennai – it appears that the NBFC crisis has impacted the residential sector the most. Small and medium developers have slowed down construction and are currently financing their working capital needs at a very high cost from alternate sources. On the other hand, commercial projects (with quality office spaces) are not facing an issue, because majority of their borrowing is in the form of Lease Rental Discounting (LRD).

It appears that if the crisis is not resolved by Q4FY19, the real-estate sector could see widespread defaults in the medium term. Many developer accounts are already on the verge of NPAs. If their borrowing needs are not augmented soon, issues with more severe consequences could emerge than previously expected.

The total outstanding credit to the housing finance sector stands at Rs 4.5tn. Out of this, combined lending by NBFCs/HFCs (Rs 1.30/1.34bn) is Rs 2.64tn, which is approximately 60% of the total credit towards commercial real estate.

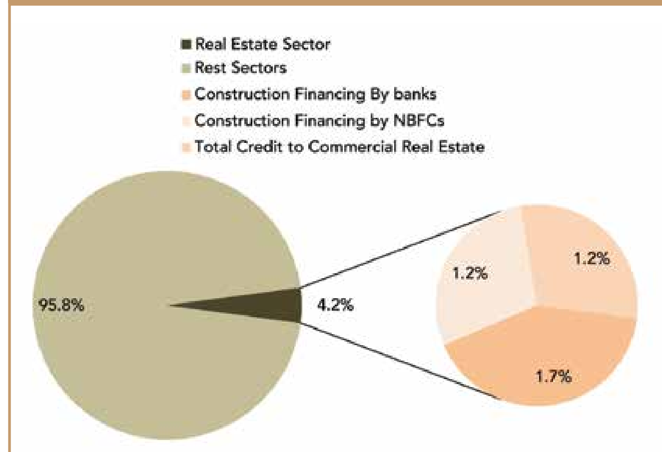
The majority of this exposure is towards Mumbai (28%) and Delhi (20%) followed by Bengaluru (15%), which indicates that the real estate sector in these cities is at a substantial risk in case of a wide-spread crisis among developers.

What happens in the shorter term?

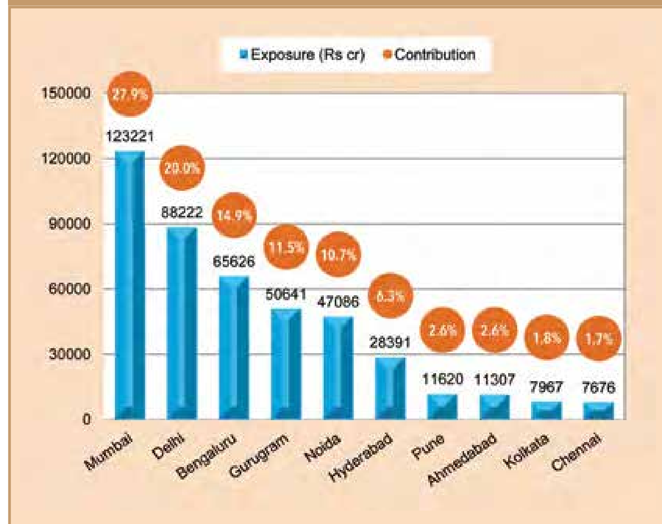
- Realisation rates remain under pressure (down 5-7%) and supply decreases. This provides some opportunities for tier-1 players to buy land parcels at discounted prices, as they are flush with liquidity and have bank funded construction financing.

- Pricing power returns to the sector.

Presently HFCs and NBFCs dominate the previously bank-dominated construction financing segment



Top 10 cities by borrower



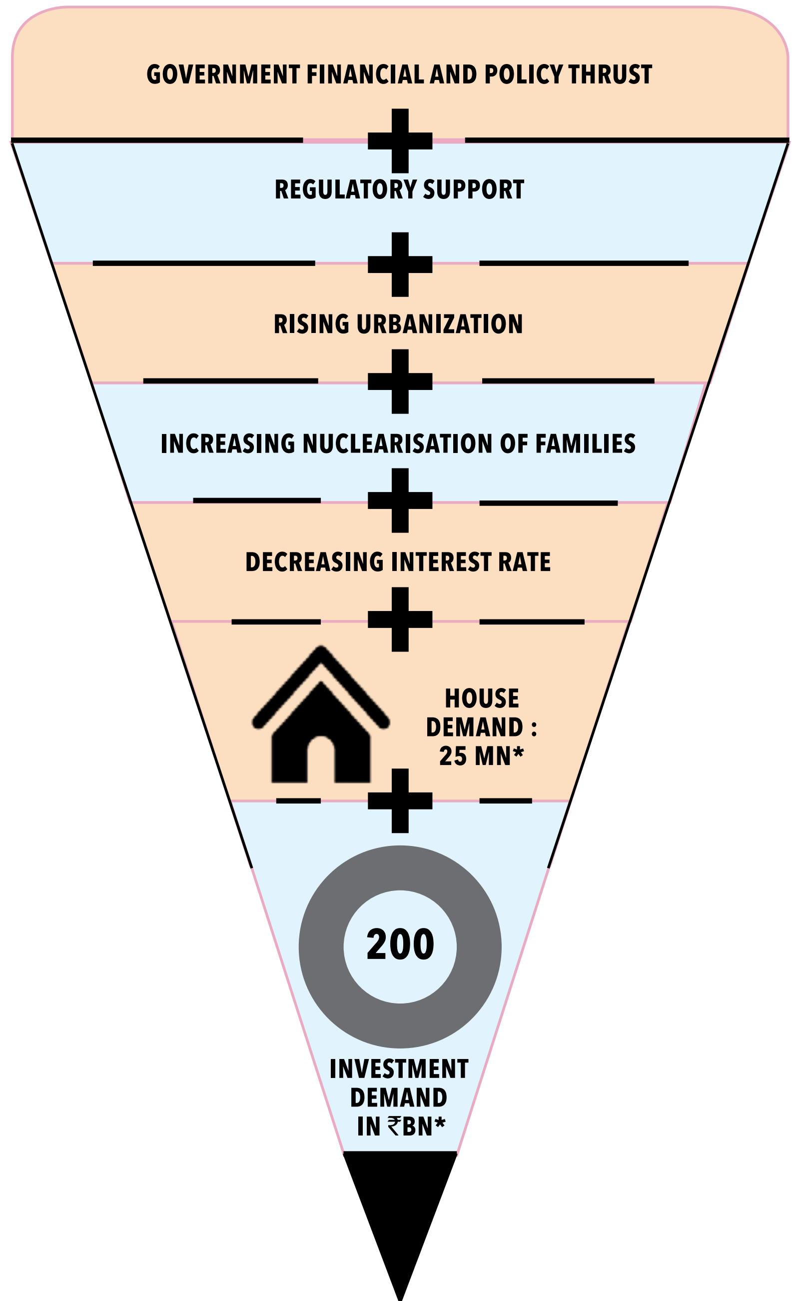
Source: CRE Matrix

Analysis of a couple of micro markets like Gurugram, Pune, Mumbai, Navi Mumbai, Thane, and Noida suggests that CY19/20 may see 80-100% higher inventory. This is because of a spill-over of pent up inventory (execution) of the past two years due to RERA implementation and slowdown in construction due to liquidity issues. Key micro markets that are likely to be affected the most are Thane, Gurugram, Greater Noida, Pune and Bangalore -- in next two years these cities may see an average of 60-80% more supply vs. CY18.

PMAY and affordable housing

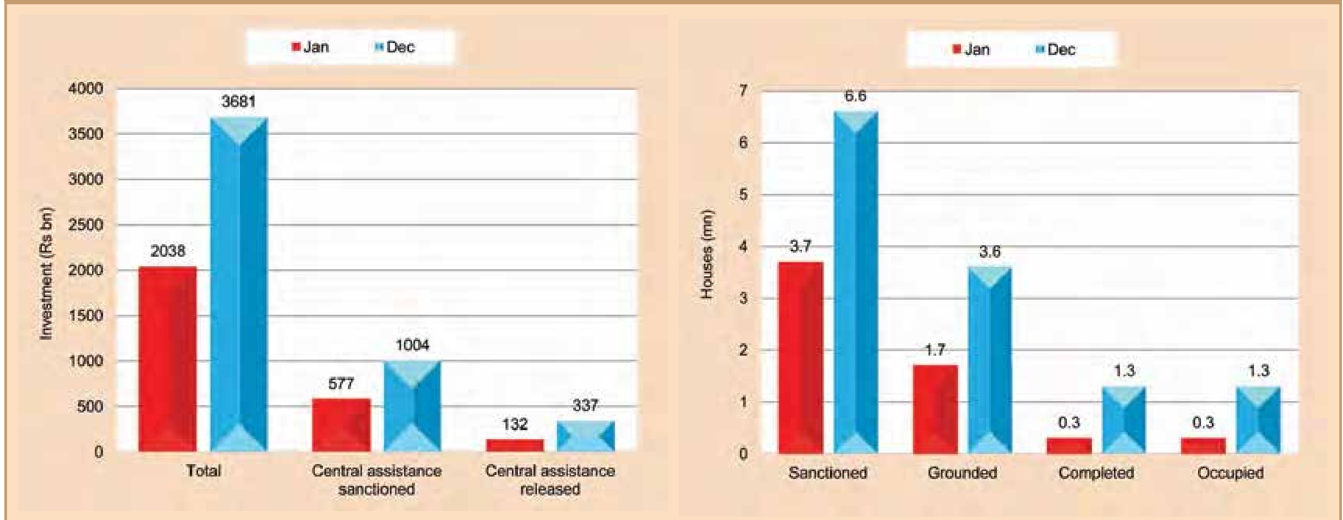
PMAY and affordable housing (houses falling under PMAY as well as low ticket sized units by private players) are going to be key drivers of the real-estate sector. PMAY has been picking up traction over the past year. Its investment amount rose by almost 83% in the past one year to Rs 3,681bn with the number of houses sanctioned going up to 6.6mn in December 2018 from 3.7mn in January 2018 and a total of 1.3mn houses constructed and already occupied. This shows that the government has remained committed towards the housing segment.

Demand for affordable houses is 25mn (PhillipCapital estimates). Sector dynamics are shifting from investor-driven demand to end-user-driven demand. On the Affordability Index, the industry is at its best point of the past five years. Per-capita income is rising. Private-sector players (both availing and not availing 80 IB benefits) that sell units in the Rs 25-50mn range will see demand and will also have some pricing power and command better realisations over the next 2-3 years. In fact, homes in this price range will be the key drivers of the residential sector while those priced higher will be continually plagued by sluggish demand and an inventory overhang, translating into weaker pricing power.



Increased impetus to the creation of affordable housing along with quicker approvals and other supportive policy changes coupled with the massive overhang in the conventional residential sector has transformed affordable housing into a key driver for the sector

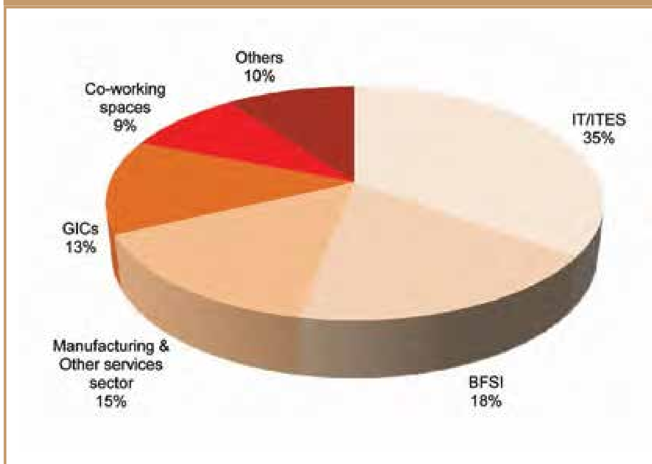
Housing in 2018: Full throttle



Commercial sector: Annuity party continues on weak supply

Over the past couple of years, due to lack of supply of 'quality' office spaces, overall vacancy in quality commercial spaces has been declining continuously. From highs of 17% in 2015, vacancy levels have dropped to 11% in 2018 on a pan-India level. The good demand in the commercial sector is due to gradually improving macros and lack of quality office supplies. This has led to 11% CAGR in rentals over the past five years. Demand has been driven by the IT/ITES sector (35%), followed by BFSI (18%), and manufacturing and other services sectors (15%). While the IT sector has slowed down, other sectors are emerging as demand drivers for the commercial space including co-working spaces (9%) and GICs (Global In-House Captives, 13%).

Despite a slowdown, IT continues to drive major commercial demand



The vacancy levels in primary IT cities Bangalore and Pune and Central Business Districts of Gurgaon, Hyderabad and Chennai is in low single digit and the price escalation in rentals in past 2 years have been in range of 35-45%. While the MMR, Noida and Ahmedabad markets have been relatively sluggish but mainly owing to the lack of supply of Grade A quality office spaces. Drivers for the commercial segment are:

- India's growth potential
- Ability to bypass RERA as the project is not being sold and leased out and can therefore remain outside RERA's gamut
- Liquidity availability due to massive interest by private equity players and funding from banks and NBFCs in the form of LRDs.

The situation is robust currently, but clouds of a glut loom on the horizon. Despite the capital intensive nature of the commercial sector, huge supply is likely to arrive into the market by 2021-22, especially in certain specific micro markets of NCR, MMR, and Hyderabad. If core demand for commercial spaces (driven by better macros and fundamental growth) does not increase by then, this sector may also start slowing down.

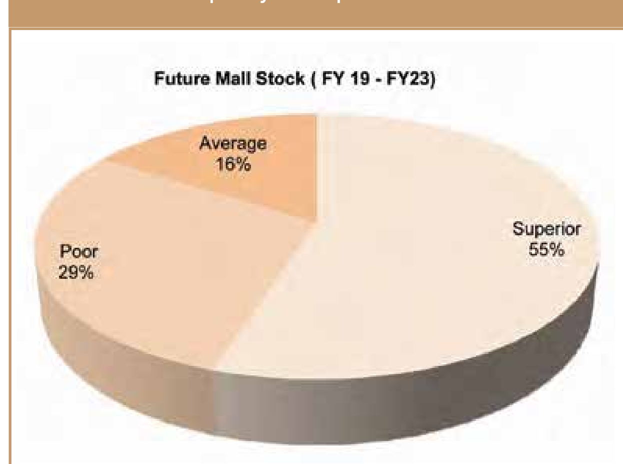
Commercial Market (H1 2018)

City	New Completions (in mn sq.ft)	Transactions (in mn sq.ft)	Vacancy	Avg. Increase in Rental
Ahmedabad	0.9	0.4	24%	6%
MMR	4.4	2.9	20%	-3%
NCR	3.6	3.4	11%	9%
Hyderabad	1.7	2.7	6%	8%
Chennai	1.2	1.8	11%	6%
Pune	2.7	3.9	5%	8%
Bangalore	3.7	6.5	3%	19%
Pan India	18.2	21.5	11%	9%

Vacancy levels: At decadal lows

Period	Vacancy Level
H1 2015	17%
H2 2015	16%
H1 2016	15%
H2 2016	13%
H1 2017	12%
H2 2017	12%
H1 2018	11%

Lack of quality mall spaces to continue



H12018:
The last couple of years have been stellar for the commercial segment

The retail space has seen good 8% CAGR in rentals over the past three years due to the lack of superior mall spaces. The ability of a mall to garner higher rentals depends on the successful management of its space and its capacity to generate footfalls continuously. Over the next three years, around 30mn sq. ft. of retail space shall be coming to the market, out of which around 55% is likely to be of superior quality, which would command better rental realizations.

The residential segment will continue to be sluggish over the next 2.0-2.5 years, after which some pricing power may return to the sector. The real estate sector from here will be a volume play rather than pricing play, and due to this PMAY and houses in the affordable segment (i.e., ones with low ticket size and those that come under 80 IB benefits) will drive the sector. The commercial segment continues to enjoy decadal low vacancy levels and high pricing power due to a shortage of quality spaces. However, a large supply wave may hit the market in 2021-22. If there is a commensurate increase in the demand for office space by then, the commercial sector should continue to perform well; else, it too may slow down relatively. In retail, lack of supply of superior mall spaces will continue; therefore, premium players will keep enjoying pricing power and minimal vacancy levels for the next few years.

BY DEEPAK AGARWAL & AKSHAY MOKASHE

THE TOWER OF PORCELAIN

Despite the sluggishness of the Indian economy, particularly the real-estate construction space, the domestic tile industry continues to grow at c.10% per annum, driven by individual construction in non-urban areas, government spending on the social sector, and exports. The industry achieved a size of Rs 270bn in CY18 and saw more than 80% CAGR in exports over the last three years.

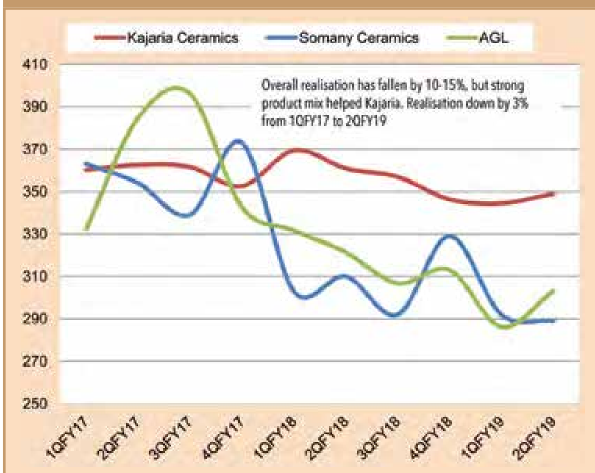
DEVELOPMENTS IN THE **INDIAN TILE INDUSTRY** OVER THE LAST 2-3 YEARS

- Oversupply due to heavy capacity addition
- Pressure on realisations
- Working capital needs increased
- Exports rose strongly

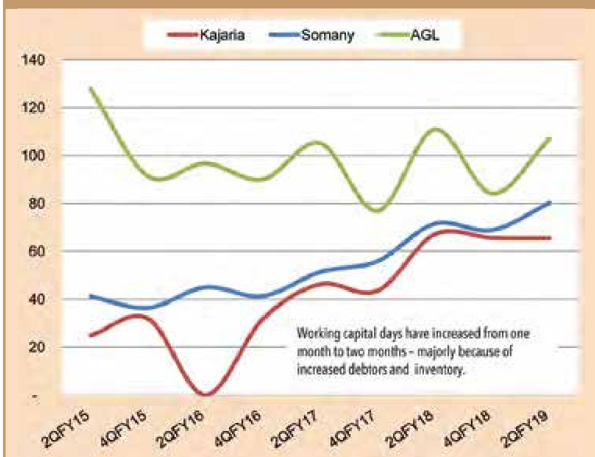
MORBI DEVELOPMENTS

- 100 plant additions mainly in GVT in the last one year
- c.450 msm capacity addition

Impact on average realisation



Working capital impact



MORBI: Excess capacity dented industry realisations

GVT (glazed vitrified tiles) realisation in India fell by c.25% over last year, which dented industry profitability. In order to achieve higher volume share, Morbi players began to offer higher incentives to their channel partners, such as discounts and credit.

Strong growth in the exports market resulted in Morbi increasing its exposure to this segment and it started working on open credit; the resultant higher receivable cycle and bad debt impacted balance sheet and profitability.

Strong competition from Morbi players *(detailed in the May 2016 Ground View)*, dented realisation and working capital of large listed and unlisted companies.

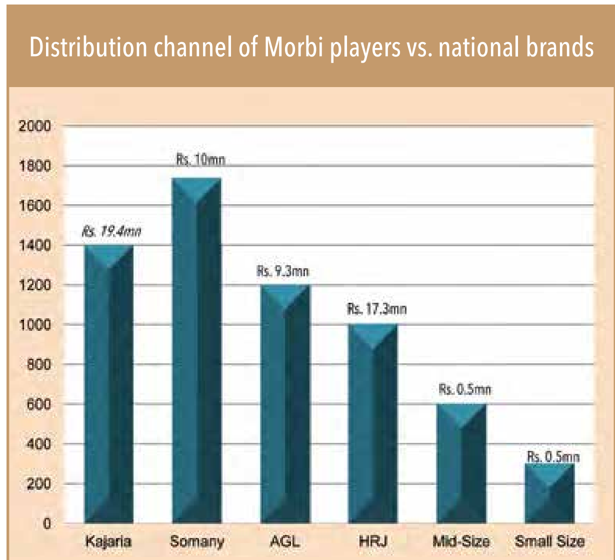
Margins for players have been moving south. The only way to survive is innovation, i.e., moving up in premium products such as large slabs – MD of an unlisted player in Morbi

Morbi is a big factor: Some more pain left

Morbi is Asia's largest tile manufacturing hub. This Gujarat town accounts for c.80% of the Indian tiles industry and generates in excess of Rs 220bn in annual revenue. The town emerged as a global manufacturing hub due to easy availability of raw materials, reliable supply of power, and logistics (it is near the ports). Co-operative culture, cost management, aggressive launches and strong interest from national and overseas brands resulted in strong growth for Morbi players over CY14-17. Additionally, it is easier to install plants in Morbi because of easy availability of resources, equipment and Morbi's working style – in Morbi it takes 6-8 months for plants to become fully operational while in the rest of the country it takes 1.5 years. Not surprisingly, Morbi saw strong capacity addition of c.100 plants (300msm) in CY17. Capacity addition in GVT was mainly because of higher realisations (margins).

Over the last 5-6 years, players in Morbi have started focussing on brand creation (participating in exhibitions, road shows). All mid-size players in Morbi are talking about brand and retail distribution. Channel checks suggest that in order to make their brands stronger, new players have started adding dealers and distributors; leading brands already have a strong presence.

Distribution channel of Morbi players vs. national brands



In a candid conversation, Mr KG Kundalia, President, Morbi Ceramic Manufacturers Association explained, "Yaha sab co-operation se chalta hai, sab ek dusre ki madad karte hai (everything here in Morbi operates on the principle of co-operation, everybody helps each other)," – which pretty much sums up how the town has metamorphosed into the second-largest tile manufacturing cluster in the world in a short span of two decades.

Lower offtake in demand and strong capacity addition in Morbi (mismatch in demand and supply) dented industry realisations and resulted in increased inventory levels at both the manufacturing level and in the channel. Many channel partners emphasised that receivable days have increased to 120 from 60 earlier, majorly for Morbi's mid-sized players. To stay ahead of the competition, some large national brands have also fallen into the working capital trap by given higher credit to the channel.

Now margins are not too exciting. I don't expect any further capacity addition in Morbi

– An industry expert

Tile dealers associated with large brands

Dealer Name	City	Area of shop (sq. ft.)	Dealer Name	City	Area of shop (sq. ft.)
Surendra Sangwan	Bhiwani, Haryana	13,000	S. Muthuraman	Coimbatore, Tamil Nadu	45000
Naresh Gupta	Dhanbad, Jharkhand	12,000	Neeraj Vasant	Raipur, Chattisgarh	10,000
Eldho Varghese	Ernakulum, Kerala	30,000			

In basic products, some plants are operating at breakeven. So we don't expect any further price fall in products such as ceramic tiles

– Mr Girish Patel, MD of an unlisted tile company

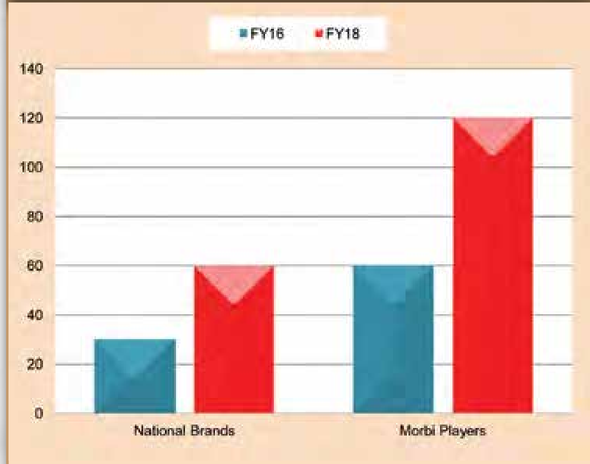
Mid-size and smaller players are not doing well

People working in Morbi expect the tiles industry there to undergo a consolidation, as smaller players are facing pressure in terms of realisations (selling products at cost mainly to run the plant) and working capital (receivables are up to 120 days). Smaller players do not have a strong enough balance sheet to avail loans, said a Morbi-based financial advisor. Every year 15-20 enterprises shut shop in Morbi due to various reasons, but rarely insolvency. However, this time there seem to be more shut downs and capacity consolidations. Many Morbi players believe there won't be too much capacity addition over the next two years because the focus has shifted to cash flows and survival.

"Bankruptcy toh yaha 1% se kam hai. Kabhi kabhi kuch karan se unit band karna padta hai, but this time thoda zyada pain haa, many small plants are on ventilator (instances of bankruptcy are less than 1% in Morbi, there are several other reasons for closure but this time we are seeing more pain – I expect more shutdowns or consolidation)," said a promoter of a large manufacturing unit.

"Brands that have strong control on costs and offer contemporary products at the right price will have good market share. Today the customer is spoilt for choice, so a brand will only succeed if it delivers on its promise of price and quality simultaneously. Additionally, companies that have strong control on cash flow and balance sheet will stand out from the crowd," said a financial adviser for Morbi players.

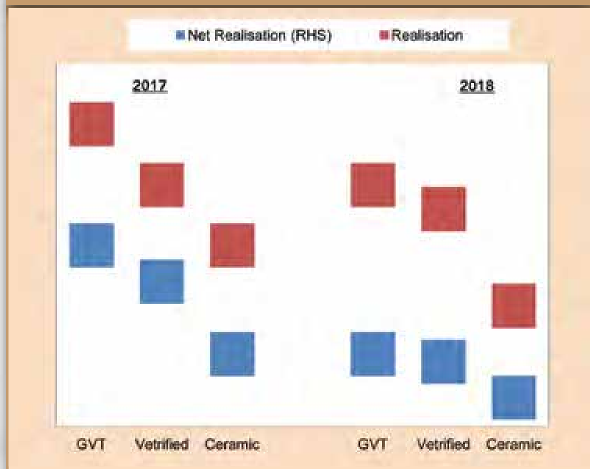
Working capital impact



A LARGE MORBI PLAYER

- We are also facing realisation pain, but product mix (new innovation) is helping us.
- Overall working capital has increased to about 5 months vs. 2-3 months earlier.
- Mainly working with large distributors (so bad debt is lower).
- Exports is a good market; working only with LCs.
- Domestic sales slowly picking up.

Impact on realisation

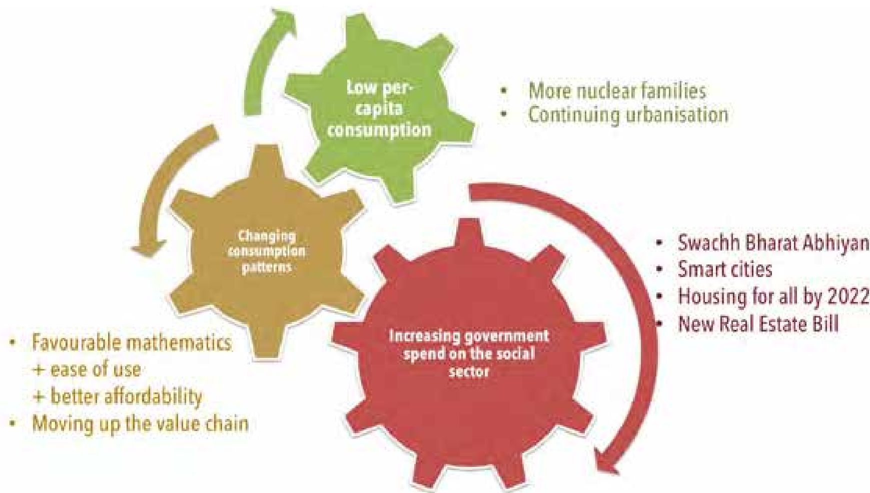


MID-SIZED / SMALL MORBI PLAYERS

- Witnessing realisation pain, currently working on break -even – just for operating the plant.
- Overall working capital has increased to c.6 months vs. c.3 months earlier. Collection is a pain. Expect some bad debt.
- Some companies are exporting without LC.

Source: PhillipCapital Research (GV interaction data)

Tile industry growth engines remain intact



DOMESTIC DEMAND DRIVERS

- Private builders' execution picking up
- Government initiatives such as Pradhan Mantri Awas Yojana (PMAY), Smart Cities etc.
- Additional supply to Kerala for flood-related rebuilding
- Lower per-capita consumption vs. global countries

EXPORT DEMAND DRIVERS

- China facing environment issues
- Other countries opening doors for India

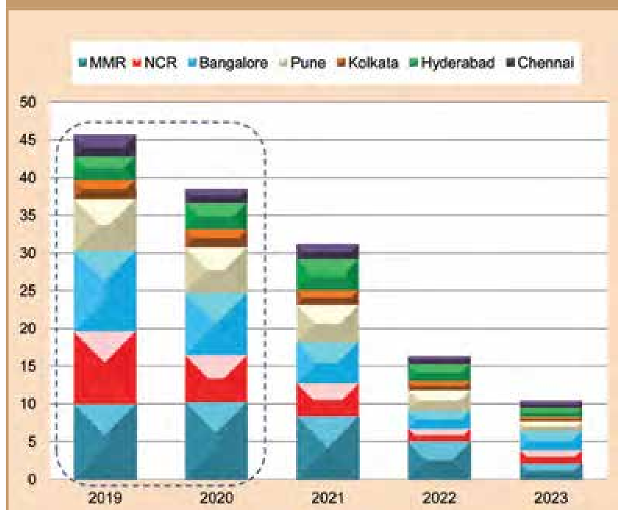
Real estate market is picking up pace

The sector had slowed down from FY16 due to demonetisation and GST. Cash inflows in the market had been strictly monitored. However, participants talk about some amount of revival over the past 2-3 quarters. The construction segment is slowly and gradually picking up pace. RERA's stringent norms delivered a ray of hope to customers. It has caused pain for builders who were delaying project deadlines. Inventory overhang from CY16 to CY17 had reached its peak of 46 months from 35 months earlier. It is currently at 45 months and is likely to stabilise soon. Metro cities have started seeing a push in the commercial segment because of the Make in India Campaign.

CHANNEL CHECK

- Builder and residential demand picking up over the last six months – seeing strong volume of c.15-20%, mainly from residential (tier 2 and tier 3 cities – said the largest marble/tile dealer near Coimbatore, Tamil Nadu.
- Small and mid-sized flats are in demand. Premium flats have great demand in NCR – said a builder from the region.
- Commercial segment is picking up, as concept such as We-Work are rising. IT hubs will see higher demand.
- PMAY is picking up in tier-2 and 3 cities.
- In south India, small ticket sizes and larger builders are seeing strong demand.

Expected delivery of major projects in key cities (msm)



In seven key cities, major deliveries will take place in 2019-20, which will generate a tile demand of c.120msm in FY19-20 . Major growth will come from tier-2 and 3 markets

View on major cities

City Name	Comments
Bangalore	Commercial thrives – residential slow recovery
NCR	Commercial moderate – residential suffers with massive inventory overhang
Pune	Commercial thrives – residential sluggish
Hyderabad	Commercial and residential thrives
Chennai	Commercial thrives with residential demand intact
MMR	Commercial thrives – residential sluggish
Kolkata	Commercial thrives – residential flattish in growth with slight price appreciation

Note: Taken construction time of 5 years. This is excluding new launches, data is based on current pipeline

Rebuilding Kerala (Kerala districts and key affected areas)

Total number of census houses	Total number of occupied census houses	Residence	Others	PC: Impacted Household	To be Reconstructed @ 300sqm (msm)
1,12,17,853	1,00,28,709	76,58,685	23,70,024	3,38,881	102

Note: As per our interaction with the experts in our GV, base case ~5% of the housed will go for reconstruction

- Kerala floods destroyed c.20,000 houses and left 50,000 houses damaged. Rebuilding activity is in progress and demand for basic products such as cement, tiles, and bricks is high.
- The Kerala market is divided into two – south and north. In the southern market, brands are preferred because this market is more organized. Unorganised brands are preferred in northern Kerala.
- Also, commercial business is picking up in the north (such as for hotels and other small units).
- In south Kerala, Kajaria, Somany, and HR Johnson have higher market share.
- Some people believe reconstruction will go on for the next one year and total tile consumption from this will be c. 300 msm.

Cities hit by the Kerala floods

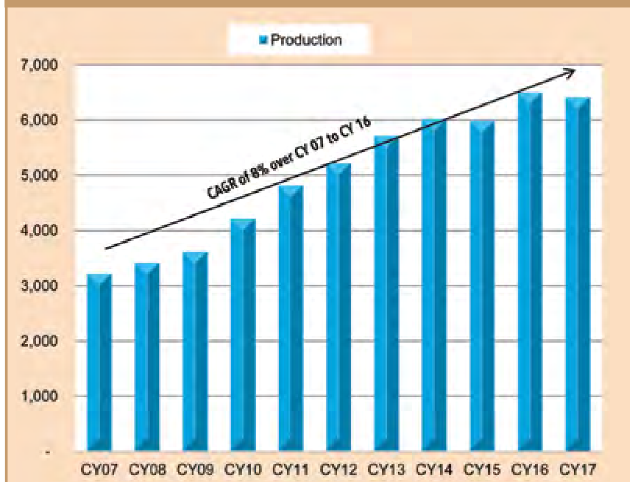
Source: Reuters

Exports: A Big opportunity for Indian companies

China facing environment issues – this means a larger export opportunity for India

China is the largest producer of tiles: China = 6.5bn msm vs. India = 955msm. However, it is in the process of a massive environment conservation exercise due to extensive excessive manufacturing-related damage to its ecology. It has started transforming its coal-based plants to natural gas and shifting its manufacturing units to outside the cities.

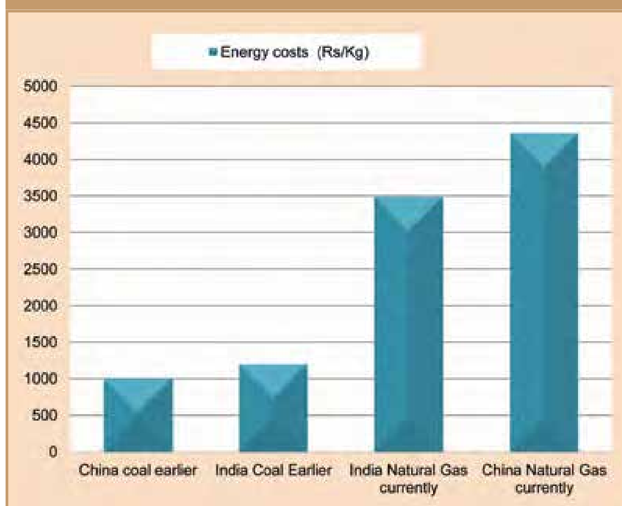
China tile production msm (50% of global tile production)



Source: Indian Ceramic Association, Industry

China domestic consumption msm

Energy costs in China saw a huge jump after a coal ban



Source: Reuters ,Industry.

China's central government has ordered regions near the capital to shut 44,000 coal-fired boilers that provide steam and energy for factories, including steel rolling mills, ceramics, and chemical manufacturers, and convert or replace them with gas-fired boilers or switch to electricity. They have also been asked to shift manufacturing clusters/hubs to outside the cities.

Impact on China's tile industry

Zibo was China's ceramics capital with a production capacity of c.1.3bn msm, mainly floor and wall tiles. In November 2017, Zibo shut more than 150 companies and 250 production lines as part of a ruthless war on pollution – thereby slashing its capacity by 70%!

A factory owner in China said that he has lost 80% of his domestic clients and half of his overseas ones, with many frustrated by the stop-start nature of production. Many players are shutting down their plants, mainly because the price of gas is 6-7 CNY per cubic meter, up from 2 CNY in 2017. "If we open, we are going to run at a loss," he said, and added that it was difficult for him to secure gas supplies.

In Zibo, annual production capacity slashed to 246 msm, compared to 827 msm before the campaign began

Dr. Hu's insights on energy cost (from PC's China visit in 2018)

The ban on coal usage and mandatory shift to natural gas resulted in a multi-fold jump in energy cost for all the manufacturers. Gas costs four times more than coal to produce the same amount of energy. In the first place, supply of natural gas is limited. Now, with this additional demand, gas prices have already shot up.

Morbi and exports

- Currently, c.30% of the plants are exporting tiles.
- In exports, Morbi has seen c.40% growth.
- The margins in exports are better than domestic margins. In fact, a Morbi player who is a sanitary ware manufacturer has now started sourcing tiles from other Morbi players and exporting them. "Realisations are better in export," he shrugged.
- Recently, some (Qutone, AGL) have bagged orders for exports to China.
- Supplying tiles to China under white labels. Also supplying to other countries under Chinese brands.
- Indian players compete with China in PGVT.
- Chinese players are visiting Morbi for tie-ups. China has started importing large-format tiles and value-added products from Morbi players.
- Due to pollution, China was impacted by c.50% (exports head of a Gujarat-based tile company).

Results of China's environment clean-up exercise

- Production loss: As many plants have shut down due to shifting from coal to gas and outside cities.

- Increasing manufacturing cost: Rising demand for natural gas has resulted in demand/supply mismatch (availability shortage) and price increases. Additionally, employee cost, which used to be c.7% of total cost has increased 2-3x. Some peg increase in production cost at c.30%.

- During the physical shifting of a manufacturing unit, production undergoes disruption (stop-start) which has resulted in business losses, delays in dispatches, and losing customers.

- Production shortage: Shut down of some plants, which used to mainly focus on lower value-added products and were not able to pass on the prices.

- Increase in realisations: By 15-25% increase seems to have already taken place.

Road less travelled: Insights from travels across India

Cash crunch

Construction activity has slowed after demonetization, GST, and RERA. Markets in south India were dependent on cash inflows from the Midde East because a large number of people from Kerala work in the Middle East. These cash inflows took a big hit as regulations in India became stringent. Many small players are facing difficulties while running their businesses – late payments or payment defaults abound. Cash inflows have reduced substantially, which has slowed down growth in construction. However, over the last six months, construction has seen a comeback driven by new projects in the affordable segment and some pick up in tier 2 and tier 3 cities.

Advantage: Savvy companies

With intensive competition and market conditions, many players have started losing share. This has proved advantageous to those tile manufacturers that have not compromised on quality, added new products, maintained a strong balance sheet, and are aggressive in marketing. Dealers and distributors have started selecting companies that give them higher margins and provide them more shelf space. Players have started to deepen their reach. Unbranded and cheaper tiles are preferred in tier 2 and 3 cities.

S A L E–S A L E–S A L E at both ends – manufacturing companies and channel partners

Larger Morbi players had to cut down their prices due to intensive competition. Tile manufacturers started dumping material on dealers to increase sales volumes. Inventory started piling up and caused problems for dealers, as they had to sell at lower prices than competitors to maintain market presence. Slowdown in the construction segment was also a big

factor that caused disruption in the tiles market. To remain competitive, branded players focused on volume growth and increased their creditor days, which stretched their working capital cycle as inventories began piling up.

Ironically, small players who sparked the price war are struggling to sustain themselves

Lured by good margins and low entry barriers small players (dealers-distributors) moved into the market and slashed their prices to increase sales. A price war ensued and damaged the entire industry. Many dealers started selling products at 50% discount just to clear their stock – a clear indicator of a major slowdown ahead. Meanwhile, many new dealerships of leading brands were created in the past year, increasing competition. In the aftermath, it looks like only those channel partners (distributors/dealers) with a strong base (balance sheet and cash flows) are likely to survive. The channel has already begun to feel major pressure in terms of working-capital receivable days – which increased to more than 80 in southern India from 15-30 earlier. This has resulted in weaker (usually smaller) players shutting shop.

Quality players will sustain

With margins shrinking, small tile manufacturers started compromising on their product quality, which caused loss of customer faith. With more customer complaints, dealers started shifting back to organized branded players with better product quality and durability. Branded players have always maintained their quality and kept launching new products with different designs. This helped them to remain strong in a volatile market. The sales head of leading tiles brand said, "We have seen some amount of orders coming back, mainly because of our quality. While some customers were taking products from Morbi's small players earlier, they have now started buying from us or other leading brands. For government orders too, all leading brands are supplying."

OUTLOOK:
Survival of the fittest

After big shocks, the tile industry has slowly started correcting past mistakes. While large branded players with deep pockets also faced difficulties, their strong balance sheets, cash flows, and organized structure provided them with sustaining power. Overall, companies are trying to reduce working capital – it had increased by 60-90 days for most players in 1HFY19. Small players have started shutting down their plants or operating only one klin, as most haven't been able to deal with mounting debts. Being unorganised, smaller players do not have ready access to inexpensive bank funding. As such, companies with stronger balance sheets and cash flows will be the 'last ones standing' in this down cycle.

Future Tense or Future Perfect – Which is it to be?

A little bit of both. Extensive interactions with companies (listed and unlisted), channel partners, architects, and industry observers indicate several changes on the horizon for the domestic tiles industry. The real questions is about the extent and timing of these shifts. Cash-flow management will also take centre stage.

Medium-term

- **Prices to remain static in the near term:** An increase in competitive intensity could contribute to pricing pressure. For basic products, not much price correction is likely as plants are operating at cost. In premium products, pressure on realisations should continue, mainly because of higher competition. Within these, premium products such as large-slabs are operating at healthy margins. Manufacturing costs (power, fuel) will also play an important role; for example, companies have recently hiked

prices due to an increase in fuel costs. Any sharp movements in gas prices will result in price movements in tiles.

- **National brands to churn out more products frequently:** Most companies introduce 3-4 new tile designs every month. Dealers and architects point out that in order to step up their game and compete effectively against imports and smaller Morbi players, listed players and larger Morbi players are gradually stepping up this game. While this could not be verified from Gujarat-based players, it seems perfectly logical, since this would contribute immensely towards maintaining market share, presence, and customer satisfaction.

- **Exports focus to intensify:** The imposition of punitive duties on Chinese tile exports in most global markets and the pollution issue (capacity shut down in China) has opened up exports avenues for Indian companies, either through white-label supplies or under their own brand. While markets in the neighbouring SAARC countries have always been targeted, manufacturers in Morbi are increasing their shipments to the Middle East and Europe. Using dynamic feedback, exporters from Morbi are stepping up customisation and broadening their range. This, coupled with competitive pricing, is enabling several unlisted Indian manufacturers to increase their quantum of exports – a trend that should gather momentum in the near term. Additionally, with capacity shutdowns and increasing costs, India has started exporting tiles to China. Morbi players said that Chinese players have started looking at JVs or partnerships with them to supply products to China and other countries.

Long-term

- Innovation, distribution, brand are a key to success.

- Growth through the JV model/outsourcing will be pursued more aggressively: Several rounds of capacity expansions are likely over the next decade, as manufacturers move to satisfy volume and variety – both local and exports. However, capital efficiency and compartmentalisation of competencies could lead to companies collaborating with each other through JVs. These alliances could be for outsourcing production, sharing of specified output, marketing tie-ups, or a combination of all three in a hybrid form.

- **Cash-flow management will be a key focus area for small and large players.**

  Smaller players will have to up their game or face stagnation. Competitive intensity in the domestic tile industry will increase necessitating innovation and operational flexibility. Companies with smaller scale may have to invest more bandwidth and material resources to be fleet-footed in order to survive and grow.

"Traditional soch se hatna padega, nahi toh mushkil ho jayegi (it will be difficult unless the conventional thought process is modified)"

Mr Kundalia, Morbi Ceramic Association President, about the future of small-scale manufacturers in Morbi

BY VIBHOR SINGHAL

TURNING A NEW LEAF – EXECUTION OUTPACING AWARDS

Historically, execution on various infra projects has always trailed awarding activity. And the reason is pretty obvious and logical – while awarding entails just preparing the DPR and selecting from various bidders, execution involves multiple steps like land acquisition, financing and other hurdles. Over the last few years, many projects have witnessed delays of over 2-3 years, and many were cancelled because multiple attempts to revive them failed.

In that sense, CY18 will turn out to be a landmark year – the year in which execution, for the first time, seems to have outpaced awarding. Across sectors (especially roads), execution on various projects has been steady (in fact ahead of expectations) – while order-award activity has been pretty dismal through the year (especially in roads). This same can be attributed to two reasons – one positive and the second negative

+Positive

The government's debottlenecking of execution processes over the last few years have meant that projects do not face much execution troubles after being awarded. Key debottlenecking initiatives:

- Minimum 90% land acquisition before awarding.
- Ensuring project finance is in place for the projects.
- Shorter duration projects with timely payments.

-Negative

The order-award activity has undergone a significant slowdown. While the pipeline remains robust, individual sectors have been impacted by different factors.

- **Roads –** In CY18, NHAI has struggled with land acquisition for new projects and also wanted to give bidders of the last cycle some breathing space.
- **Metros –** the segment witnessed unprecedented awarding in last three years (especially Mumbai metro, which awarded Rs 250bn projects), rendering the remaining pipeline dry (limited number of cities planning metros).
- **Irrigation and housing –** awarding has been impacted by various state elections.

GV travelled extensively across the country to gauge the state of execution on various projects and get updates on the awarding activity by the authorities. Here are the findings:

Execution in progress at Lucknow-Sultanpur (UP) project

Roads

Awarding
Has been pretty dismal in FY19 – especially by NHAI – with the government body having awarded only about 450km of road projects YTD (vs. 7,400km in FY18). The segment awarding has been boosted by some high-ticket state highway projects such as Purvanchal expressway (UP, Rs 230bn) and Mumbai-Nagpur expressway (Maharashtra, Rs 460bn).

Execution
Across the country, we have seen significant pick-up in pace of road construction activity. As per the government data, 5800km of highways have been constructed in 9MFY19 – amounting to construction pace of 25km/day – inline with 27km/day in FY18. In Dec-18 however, the rate of road construction touched a peak of 32km/day. We found strong execution activity in states of UP, Maharashtra, J&K, and North-East.

Key road orders awarded in CY18

Project	State	Agency	Length	Cost (Rs bn)	Winners
Purvanchal expressway	UP	UPEIDA	343	230	PNC, Gayatri, GR Infra, Oriental, Apco
Mumbai Nagpur expressway	Maharashtra	MSRDC	701	460	NCC, L&T, PNC, Sadbhav, AFCONS
Mumbai Coastal Road	Maharashtra	MSRDC	30	110	HCC, L&T
Bandra Versova Sealink	Maharashtra	MSRDC	17	70	Reliance Infra
NHAI TOT Package	Across	NHAI	648	97	McQuarie-Ashoka JV
Rewari Ateli Mandi	Haryana	NHAI	31	4	HG Infra

Housing

Housing segment has witnessed strong pace of execution and award - driven by projects under the Pradhan Mantri Awas Yojna (PMAY). Housing construction data under the PMAY scheme, over the last 10 months, clearly corroborates the trend.

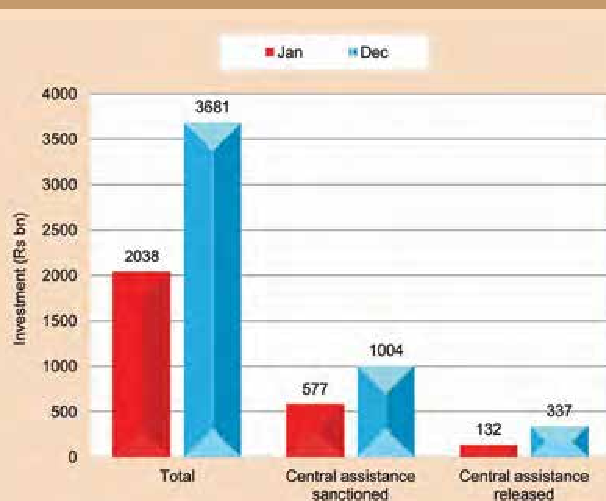
Awarding

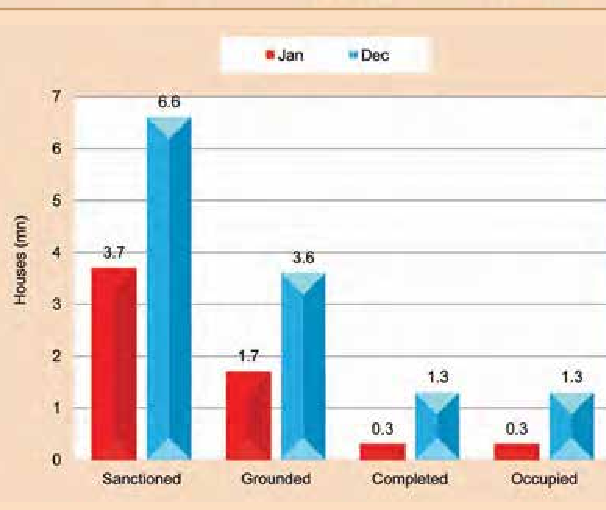
Over CY18, 2.8mn houses were sanctioned, amounting to central assistance of Rs 42.5bn being sanctioned (43% of the total).

Execution

Over CY18, 3.9mn houses were 'grounded or construction / completed / occupied' across 25 states, amounting to Rs 204bn of central assistance being 'released' (61% of the total).

Housing in 2018: Full throttle





PMAY project site in Rajahmundry (AP)

Structure erected from aluminium formworks

Aluminium formworks used in MIVAN technology

View of a block of flats complete

Interior of a ready-to-move-in flat

Metros

Awarding

FY17 and FY18 saw unprecedented awarding in the metro segment, driven primarily by two cities – Mumbai and Bangalore. The two cities awarded metro projects worth Rs 350bn over the two years, paving the way for strong execution over FY19-23. However, these awards also led to a temporary 'drying-up' of the order award pipeline for FY19, as metro projects in other cities are still 'under development' and a few quarters away from being awarded. Nevertheless, with Delhi Metro Phase 4 (106km, Rs 550bn) receiving both central and state government approval, the award pipeline for FY20 and beyond looks healthy.

Execution

Across the country, we have seen a significant pick-up in the pace of metro construction activity. While two packages of the MM3 in Mumbai faced a few litigations, which delayed work by about 6 months, other projects have seen smooth and steady execution YTD FY19.

Key metro orders awarded in CY17-18

Project	Total Length (km)	Cost (Rs bn)	Stretch awarded (km)	Winners
Mumbai Metro Line 2B	23.5	110.0	23.5	RCC-MBZ, Neeraj-Guan, Simplex
Mumbai Metro Line 4	40.0	120.0	40.0	Tata Projects, Reliance Infra
Mumbai Metro Line 6	14.5	67.0	5.8	Jkumar
Pune Metro	31.5	115.0	18.0	NCC, HCC, Jkumar
Bangalore Metro	58.9	126.0	58.9	ITDC, Simplex, L&T, HCC, Afcons
Kanpur Metro	32.0	180.0	8.3	Bids invited, yet to be awarded

Mumbai Metro Line 3 update: Site-wise progress

Site ->	Cuffe Parade-CSMT	CSMT-Mumbai Central	Mumbai Central-Worli	Worli - Dharavi	Dharavi Santacruz	Santacruz Sahar	Sahar Seepz
No. of Stations	4	4	4	3	4	3	3
No. of TBMs	2	2	2	3	4	1	3
Total Length of Tunnel (km)	5.88	7.64	7.40	10.95	7.99	6.94	7.07
Tunnel Completed (km)	0.04	1.74	2.00	3.46	1.85	-	1.26
Total Muck Volume (thousand cu. mt.)	1,050	686	2,100	929	1,070	1,360	1,100
Muck Disposed (thousand cu. mt.)	250	227	91	247	187	701	235
Disposal Sites	Kalwar & Ulwe	Mhape MIDC & Ambernath	Dapode & Bhi-wandi	Dapode & Waliv	Waliv & Daniv	Waliv & Daniv	Talawali Pise

The Mumbai Metro Line

Source: MMRDA

Airports and Railways

The newly constructed swanky railway station at Katra (J&K) and airport at Pakyong (Sikkim)

While not much was expected from these 'relatively smaller' segments (in terms of order award potential), ordering as well as execution activity was surprisingly higher than expected.

Awarding

Under the 'UDAN' scheme, multiple teir-2/3 airports are being modernized, and we saw tenders for Lucknow and Goa airports being awarded this year. While anecdotal data is not available for railways, the department has been continuously awarding projects for electrification of railway lines and upgradation of tier-2/3 railway stations.

Execution

It was amazing to see how the condition of various airports and railway stations across India has improved over the last two years. As many as 9 new airports commenced civil flights in CY18. The images below bear a testimony to the pick-up in execution speed and enhancement in quality.

Airports that started civil operations in CY18

City	Commencement Date
PATHANKOT	05-Apr-18
SALEM	25-Mar-18
SHIMLA	27-Apr-17
VIDYANAGAR	21-Sep-17
KANPUR	03-Jul-18
JAGDALPUR	14-Jun-18
JHARSUGUDA	22-Sep-18
PAKYONG	04-Oct-18
KISHANGARH	08-Oct-18

Over the next few months, as the country comes out of election mode, awarding bottlenecks are removed, and the banking system opens up to lending, awarding is likely to return to normal. At the same time, it is likely (hoped) that with fundamental improvement in the execution process, the positive momentum in execution will not reverse. Thus, 2019 could be the year in which we see BOTH execution and awarding reaching individual peaks.

BY VIKRAM SURYAVANSHI

LOGISTICS:
CHANGING LANDSCAPE

Key changes in the sector and impact

2018 was year of survival and hope for the sector with key policy changes affecting companies at the ground level. Important shifts included: (1) change in CFS and ICD business after direct port deliver (DPD) under ease of doing business, (2) growing demand for A-grade warehousing after GST and growth in e-commerce, and (3) continued focus on inland waterways.

DPD update: Changing rules of the game

DPD is a classic story of a struggle between the government's desire for structural changes and resistance from established stakeholders. With trial and error, the government is now trying to find the balance between efficiency and cost of operation in exim trade. Under the ease of doing business, JNPT (the largest container port in India) issued a trade notice (on 9th February 2016) to extend the DPD facility to all ACP (Accredited Client Program) clients irrespective of their monthly volume. Under ACP, importers can undergo custom clearance at the port itself, and take the delivery of their container at the port instead of the normal routine of going to the CFS for custom clearance. This move extended DPD benefits to more importers. Before the trade notice was issued, only 11 agencies were availing of the DPD facility from JNPT. This number increased to 2,110 registered users in December 2018.

DPD benefits

- Lower costs for importers due to reduced handling and storage expenses – an importer is assured cargo clearance in less than 48 hours under DPD, while through a CFS, this takes an average of seven days.
- Delivery of containers at terminals takes place 24x7 (not available for custom bounded warehouses).
- As per data released by JNPT, the collective benefits of DPD to importers is c.Rs 15,000 per container.

The AEO programme provides businesses with an internationally recognised quality mark, which indicates their secure role in the international supply-chain and that their customs procedures are compliant.

Authorized Economic Operator (AEO) Programme

As a next step towards trust-based compliance, Indian Customs introduced the New AEO Programme in 2016 – with the amalgamation of the ACP (Accredited Client Programme) and AEO programmes. Under this, extensive benefits, including greater facilitation and self-certification, were provided to those entities who have demonstrated strong internal control systems and compliance. DPD functions under the AEO Programme, which is under the Central Board of Excise and Customs (CBEC).

A few Custom Houses across India, such as the Jawaharlal Nehru Custom House and the Chennai Custom House, have extended the DPD facility to non-AEO clients. The non-AEO DPD programme ensures decongestion of ports and faster evacuation of cargo. Direct delivery was allowed earlier under the different programmes mentioned below, but they could not succeed due to rigid norms set by the CBEC. The new AEO programme has led to the success of DPD.

What is DPD?

Under Direct Port Delivery, the import container is cleared at the port itself instead of transferring it to CFS for customs clearance and duty payment. Before February 2016, importers had to take delivery from a CFS, mostly designated by the shipping line that they used. At JNPT, customs has specified a time limit of 48 hours (from the time of berthing or inward entry) for evacuation of DPD containers from the terminal; at Chennai Port, this time limit (free period) is 72 hours. Importers have to complete all formalities – obtain a delivery order from the shipping line, pay duty, attain 'out of' charge from customs, and arrange for transport with RFID/PIN – within this stipulated period. When an importer is unable to evacuate within this free period, the container is moved to designated container freight stations.

Operators – going from denial to fear

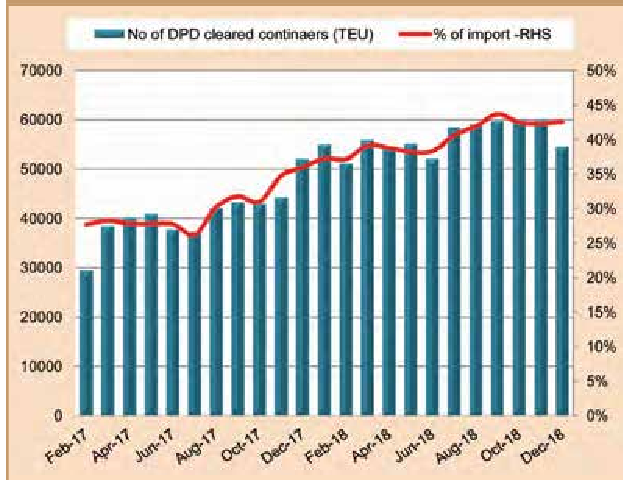
JNPT Port has 33 CFS operating with total handing capacity of c.3mn TEU In 2017, most CFS operators used to say that DPD had a limited impact on their business. The finance head of one CFS had said then, "Direct delivery at port is already prevalent for select importers with minimum volume per month and it is not successful." Importers didn't have enough storage and container handing facilities at their factory so they would come to the CFS because they also needed to return empty containers to shipping lines after unloading their cargo – an additional cost. "Most importers received credit and free days from CFS', which will not be the case with a port," an operational head at another CFS had said.

With the government's efforts, DPD has become partially success with c.42% share of imports at JNPT in November 2018 from 28% in March 2017.

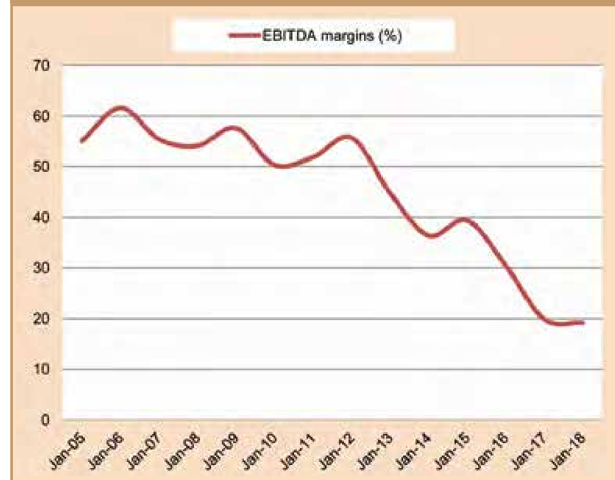
JNPT Port has 33 CFS' operating at a total handing capacity of c.3mn TEU

DPD under different programmes

Share of DPD has stabilised at c.42% after initial success

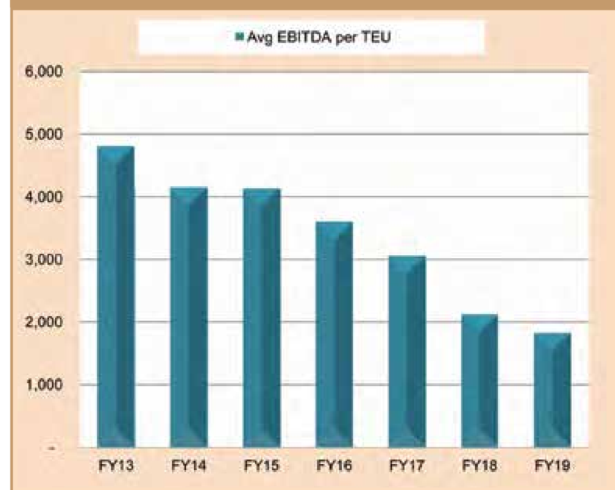


Decline in margins for CFS business



With higher share of DPD-cleared containers, the bargaining power shifted from CFS' and shipping lines to importers, CHAs (Customs House Agents), and freight forwarders. This resulted in a sharp decline in CFS' operational profitability at JNPT port and lower utilisation at some facilities, denting business pricing. Some CFS' started providing incentives to CHAs or freight forwarders to attract DPD-cleared containers. "CFS margins have reduced to around Rs 2,000 per TEU from c.Rs 4,000 earlier for imports; for exports, they are substantially below Rs 2000 now," said a CFO of one private CFS.

CFS average profitability (Rs per TEU)



"CFS margins have reduced to around Rs 2,000 per TEU from c.Rs 4,000 earlier for imports; for exports, they are substantially below Rs 2000 now" - a CFO of one private CFS.

Port officials emphasized that a decline in volumes is not a big concern for CFS players, even after DPD, as most containers go back to CFS'. The initial panic and culture of discounting by CFS' resulted in a decline in profitability. Earlier, CFS players used to provide incentives to shipping lines. Now, they have started to provide discounts to freight forwarders in order to attract cargo.

Managing the interest of local people

Local people's dominance (mainly political) is very high at JNPT and creates disturbance for any change. A few examples:

- In May 2018, region-based 'nominated transporters' were announced to move DPD containers. The idea was to support to-and-fro movement of DPD containers to cut down on logistics costs and save time for select routes, and to give best transport rates to customers. However, truckers at JNPT port went on an indefinite strike for almost a week to protest against the new system.

- In September 2018, locals disrupted operations at JNPT port after a private CFS operator laid off employees. Police deployed to handle the situation were also injured in attacks by locals.

Percentage share of import containers at JNPT

No material benefit for end customers

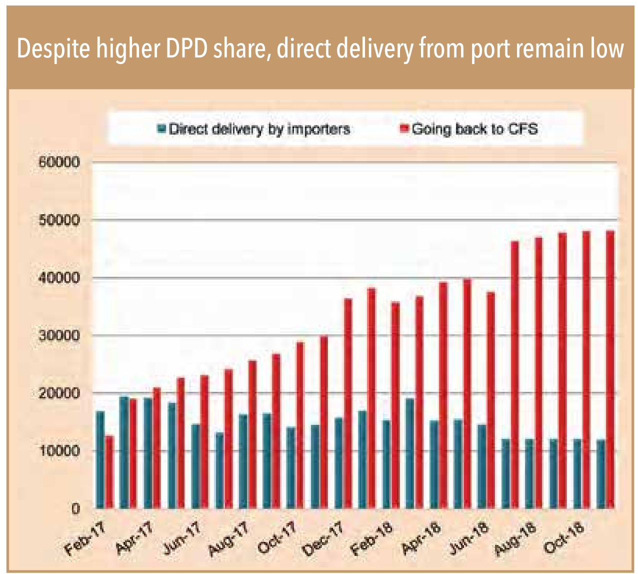
Since it is now apparent that DPD and congestion inside the port are directly co-related, the government has dropped its initial idea of 80% DPD cargo handling. Recent interaction with port officials and CFS operators revealed the possibility of a more balanced DPD target. "DPD has limited success because direct delivery by customers (port to factory) is stagnant at below 10%. In fact, it was around 8% in November 2018. The remaining containers are going through CFS, mainly due to issues at the customers' end in finance, storage, and logistics," said an executive working with a port's traffic department.

DPD to stay...with changes

Some media articles suggested that DPD would be scrapped. This is unlikely. DPD will continue, but there could be some changes that would support CFS operations and improve efficiency at ports. Currently, each CFS has its own fleet that arranges movement of containers from CFS' to ports. To reduce congestion inside a port area, the government will soon come up with new ways for transporting containers to CFS. "Trailers entering ports with import cargo will have to also exit (evacuate) delivery cargo of any CFS based on the queue and the container assigned to it," said one private CFS operator. Currently, ports need to keep a separate storage area for DPD and exim containers meant for CFS, which is reducing efficiency. Also, ports are not designed for individual container delivery, leading to multiple handling of containers.

Under DPD, the importer has to submit a hard copy of the original Bill of Lading (B/L) before IGM (Import General Manifest) filing by the shipping line. The stipulated timeframe for filing IGM is up to 72 hours before the berthing of a vessel. This practice is mostly prevalent at JNPT; at other ports, an electronic B/L or intimation by the importer's bank is also accepted. However, operationally, the DPD process proves to be difficult for importers. Traders need to provide the original B/L to the shipping line. It takes 12-15 days (assuming there is no holiday or break in the chain of activities) for this B/L to reach the importer, making it nearly impossible to produce an original B/L where the ship transit time is less than 12-15 days (ships from Dubai, Colombo, Karachi, Bandar Abbas, Singapore, Malaysia, and China take less than 15 days to reach Indian ports).

Despite higher DPD share, direct delivery from port remain low



Hope on the horizon

Stabilisation of volume for DPD at c.42% and no further push by the government is likely to provide relief to CFS players. A pick up in volume at the recently started fourth container terminal should increase business opportunity for CFS'. At JNPT, capacity was a major issue for the past ten years, which is addressed now – after the completion of phase-2 of the fourth container terminal in 2022, capacity is likely to increase to 10mn TEU per annum from 4.5mn TEU in FY18. JNPT port has vast addressable market, which require CFS services; so removal of capacity constraints is a positive for CFS players ahead, as volume picks up.

Increasing land price and improving infrastructure at port

- JNPT SEZ, a multi-product SEZ, is coming up on 684 acres of freehold land at JNPT. So far, JNPT has leased 75 acres of land for a period of 60 years for Rs 6.30bn, including 31 acres to 15 MSME investors in the SME Zone. The recent auction of SEZ land at the port at 4x the reserve price signals the future business potential. For port-led industrialisation, JNPT SEZ, has leased a plot of 44 acres to Dubai-based DP World's India arm for Rs 5.7bn.

- Fourth container terminal: Phase-1, 1km berth length, 2.4mn TEU capacity; started in December 2017. Phase-2 of equal length and capacity is expected to start in December 2022. Capital expenditure for Phase-1 and 2 is c.Rs 79bn.

- JNPT is improving its road evacuation system. All connecting roads to the port are to have 6/8 lanes. All roads will connect to NH-4, Sion-Panvel Highway, and NH-17 – and will be completed in 2019-20.

- JNPT Port is widening and deepening its navigational channel with a capital expenditure of Rs 20bn for a depth of 15mtr. This will help to berth larger ships of 12,500 TEU capacity while currently it handles 6,000-9,00TEU.

New 'A-grade' warehouses – with natural light, firefighting, drainage systems

Warehousing: Beyond storage

Visit to a Bhivandi warehouse: The godown-to-warehousing journey

The warehouses were situated at Bhivandi, a warehousing hub near Thane, Mumbai. It was surprising to see the pace, scale, and technical advancement of warehousing being developed. A preconceived notion – that reorientation of warehousing and supply chain would be slow and that companies would take a long time to understand the trade pattern, study and evaluate supply chain, and finalise warehousing and outsourcing requirements – proved wrong. With GST, companies are organizing their distribution models based on logistics efficiency and consolidating at much larger

Wider approach road for 40ft containers

Construction of warehouses with PEB structures

and modern facilities. The growth in e-commerce companies and entry of multinationals is changing the requirements for warehousing facilities compared to traditional godowns (i.e., small standalone warehouses).

Bhiwandi has developed as a warehousing hub mostly for domestic cargo while JNPT and Navi Mumbai cater to EXIM cargo.

Bhiwandi advantages.

1. One-day distance for distribution of cargo to Mumbai, Pune, and Ahmedabad.
2. Development of logistics infrastructure with labour and transportation network.
3. Continuous large land parcels and development of warehousing clusters.

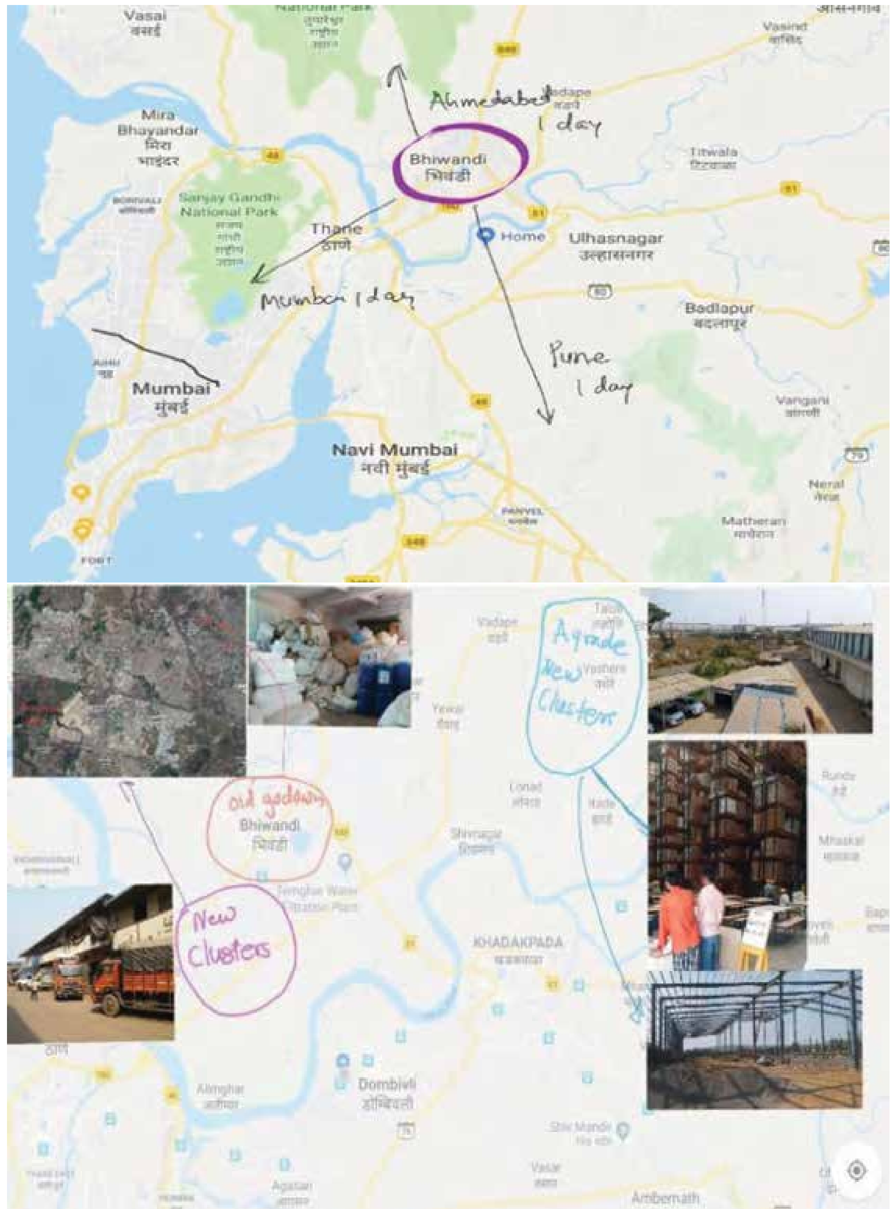
Big corporates and MNCs are shifting to new and bigger warehousing facilities in the cluster format. Clusters are being developed on continuous land (100-150 acres) with warehousing space of c.25,000 sq. ft. per acre. Developers are providing common user facilities with mostly standard warehousing (few are built to suit) and sell it to investors in small parcels with an annual yield of 8-9%, with 3-5% escalation. The new warehouses are taller – with a height of 12.5mtr vs. 6-7mtr for the older ones – which helps to go up to 6-7 stacking with a racking system.

Roads are up to 90mtr wide and are present (mostly) on both sides of the warehouse for inward and outward cargo. Wider roads also allow easy movement of larger trailers carrying 40ft containers. These warehouses are equipped with natural light, have heat-resistant coating, fire-fighting equipment, and water drainage. New clusters are being developed 4-5km away from the main city on the Thane-Nashik road. In the last 3-4 years, there has been c.70mn sq. ft. A-Grade warehousing construction in and around Bhiwandi. New supply is growing by c.20-25mn sq. ft. per annum.

All big corporates and third-party logistics service providers (3PL) are moving to the A-Grade warehousing space. Dominant players are

D-MART (single location 450,000 sq. ft.; adding 500,000 sq. ft. per year) Pidilite Industries, Flipkart, Reliance, Amazon, Apple, DHL, DB Schenker, Stellar Value Chain solutions, LP Logistics, etc.

A-Grade warehousing rents are around Rs 17-20 per sq. ft. per month including Rs 1.5-2.0 as monthly maintenance charged by developers (for security, drainage, etc.). It also includes an unofficial payment to locals known as varai. Rent is more a function of facilities such as height, clear span, floor strength and quality, road width around the warehouse, fire-fighting, and water drainage. Warehousing charges for the old godown at Bhivandi are Rs 9-14 per sq. ft. per month. New clusters do not face restricted entry for LCVs (large commercial vehicles) during the daytime. However, such restrictions are applicable for warehouses inside Bhiwandi City – which is surprising considering that Bhiwandi is an industrial and warehousing hub. Huge traffic jams stretching up to 2km even in the middle of the day are fairly common. Predictably, heavy vehicles were allowed to enter the city by paying a hafta (bribe) of around Rs 600 per truck.



Bhivandi: Advantageous location for cargo delivery with a supporting eco-system

PEB construction is becoming popular

Land required for a warehouse set-up is mostly jointly developed by builders and land owners, where the landowner retains around 40% of the developed area that is leased out. A JV structure provides regular income to the owner instead of a one-time payment, which is good for the long-term socio-economic sustainability of the area (in earlier models, one-time payments were made but it was observed that land owners quickly run through the money and then tend to disrupt operations with demands for more money by gathering locals). Warehouse construction costs range from Rs 1,200-1,500 per sq. ft., excluding land, with an FSI (Floor Space Index) of 0.5.

PEB construction costs vary from Rs 400-700 per sq. ft. and these structures cost typically 30-33% of traditionally constructed ones. Most dominant market players in PEB structures for warehouses are Zamil – a Pune based PEB player, Everest Industries – all India player, and Sankalp Systems based in Vadodara.

First multimodal terminal of IWAI at Varanasi

INLAND WATERWAYS – FINDING ITS OWN WAY

The government is developing NW-1 (River Ganga) under the Jal Marg Vikas Project (JMVP) – from Haldia to Varanasi (1,390 km) – with technical and financial assistance from the World Bank at an estimated cost of Rs 54bn.

The project entails construction of:

- 3 multimodal terminals (Varanasi, Sahibganj and Haldia)
- 2 intermodal terminals
- 5 Roll On — Roll Off (Ro-Ro) terminal pairs
- A new navigation lock at Farakka
- Assured depth dredging
- Integrated vessel repair and maintenance facility
- Differential Global Positioning System (DGPS)
- River Information System (RIS)
- River training
- River conservancy works

NW-1 is being developed for navigation of large vessels of up to 3,000 tonnes of weight by maintaining a draft of 2-3 metres. The proposed Multi-Modal Terminal and Freight Village at Varanasi are likely to generate direct employment for 500 people and create more than 2,000 indirect employment opportunities. The objective is to promote inland waterways as a cheaper and more environment friendly means of transport, especially for cargo movement.

Inland Waterways Authority of India (IWAI) is the project Implementing Agency. It plans to develop ferry terminals in Bihar at Digha, Gandhighat, Gaighat, Kanganghat (Patna), Kastharni Ghat and Babua Ghat (Munger), and Mahadev Ghat (Tintanga). It has installed the River Information System (RIS) and Vessel Traffic Management System (VTMS) on the Farakka to Patna stretch of the Ganga river. As a part of the project, six base stations and one control station have been installed in Bihar.

Visit to Varanasi Multimodal Terminal

Varanasi, known for its spiritual roots, is set for a big Smart City makeover with a capital investment of c.Rs 25bn. The Varanasi Multimodal Terminal was inaugurated by Prime Minister Narendra Modi on 12 November 2018 on the day it received its first container cargo. The MMT has a capacity of 1.26mn tonnes per annum of cargo and is built on an area of 34 hectares. Varanasi is the first of the three multi-modal terminals and two inter-modal terminals being constructed on the Ganga River.

This is the first container movement on an inland waterway in India after Independence: Inland waterways authority of India (IWAI) transported its first container cargo belonging to PepsiCo (India) from Kolkata to Varanasi on NW-1 on 30 October 2018 – the 1,500-dwt vessel, named MV Rabindranath Tagore, carried 16 containers of 9 tonne weight and took 12 days to sail. On its return journey, it carried fertilisers belonging to IFFCO procured from its Phulpur plant near Allahabad.

The inland waterways terminal at Varanasi has a natural draft of 15mtr and both sides have sharp turn, which restrict sand accumulation – so maintenance-dredging cost is minimum. The cost of developing the first phase is Rs 1.70bn with an additional cost of Rs 200mn for constructing the connecting road.

The terminal has imported two cranes for bulk and container handling at a cost of ₹490mn. Since the approach road is not yet developed and cargo movement frequency is very low, the driver (crane operator) is called from Kolkata when required. “It (the terminal) will have a permanent driver once it will start regular service,” said a local employee.

The project construction work is given to Afcons Infrastructure, a part of the Shapoorji Pallonji Group. The access road and service

First phase of the waterfront berth is complete

Road construction to the terminal will be compete in 1-2 months

room for the turbine are expected to be completed by January end. The administrative building is expected to be ready by March 2019.

The first container vessel, which sailed on 30 October 2018, was of 1,500dwt and IWAI is designing two barges of 3000dwt each, which can navigate with a 3mtr draft. "The Ganga river will have draft problem between March and April and would require dredging to maintain even minimum draft of 1.5mtr," sail a local sailor. For the cargo terminal to be successful, there should be parallel development at Sahib Gang and Farrakhan, which can increase the overall cargo potential. "Inauguration was too early. The government temporarily developed a small approach road with a capital expenditure of Rs 3.5mn and spent around Rs 4mn on an event with additional cost for police and security for 10 days," said a local person.

IWAI had invited bids for the operation, management, and further development of the MMT (project is to be operated on a public-private partnership model). Private players such as Dubai-based DP World, Singapore-based Portek in a joint-venture with India's ACTL, and two other Indian companies — JM Baxi Group and IL&FS – are interested in operating the Varanasi multimodal terminal. "With BJP's recent poor performance in three major state elections, i.e. Rajasthan, MP, and Chhattisgarh, private participation is going slow and private players will start bidding for projects once political clarity emerges. If BJP government come to power in the upcoming central elections, then there will be sudden jump in private participation," said a construction manager at the site.

the temporary approach road developed for inauguration

Phase-1 construction – likely to be complete by March 2019

"Around 500 boats run on diesel around Ganga Ghats – the government should provide benefits for shifting to solar or CNG"

- A local operator

BY VAIBHAV AGARWAL

VISIBLE REGULATION - DRIVEN CHANGES; PRICING IN SHARP FOCUS

PhillipCapital analyst Vaibhav Agarwal travelled exhaustively across all regions of India – north, east, central, south, and west; states toured included Rajasthan, Madhya Pradesh, West Bengal, Tamil Nadu, Andhra Pradesh, Telangana, Chhattisgarh, Karnataka, and Maharashtra – to catch up on current trends, recognise challenges, and to gather feedback. The key intent was to understand cement-pricing nuances and fathom why prices were not recovering despite healthy demand. This was a great opportunity to observe cultural changes in the sector in terms of the operating business environment.

Tightening regulation is changing industry dynamics

Cement pricing and its direction is a mix of production discipline and many other qualitative factors such as efficient management of the supply-chain, including the distribution channel, alignment in the business philosophy of all individuals within an organisation, and also importantly, the requirements of individual cement manufacturers, which keep changing and vary according to their business models and market conditions. The operational business environment has changed dramatically in terms of tighter compliance prerequisites at every level – right from limestone quarrying to distribution – which makes better cement prices the need of the hour for everyone. Some examples – royalties are now pre-paid, which increases the working capital cycle of companies; overloading is no longer practiced in the industry.

A tollgate detailing the penalty on overloaded vehicles in Hindi

Not just about production discipline.... individualistic thinking has propagated

Despite far-reaching changes in the industry, the recovery in cement prices will be slow and steady. This is because now it is largely a free market and as the requirements of individual business entities differ (depending on both internal and external factors) they will not easily align with others. Cement prices are no longer dependent on just production discipline, but also on the fundamentals of demand and supply. For individual players, marginal cost is determining the price at which they want to sell – they have started looking at their absolute profit earning capabilities. While not all players are equally margin conscious, MOST are cash-flow conscious. Many companies are happy to earn a decent absolute EBITDA / cash flow by

For individual players, marginal cost is determining the price at which they want to sell

selling higher volumes. Individual players are now deciding the price of their product based on their production costs and volumes; earlier, they decided based on only price and volumes – i.e., most were not too concerned about cost of production as pricing was lucrative.

Importance of a disciplined approach is well entrenched – a qualitative positive

It is a widely known that in India, cement prices were based on production discipline. However, recently, most stakeholders were worried that if the philosophies of manufacturers were not aligned due to increased individualistic thinking, pricing would pay the price. Management commentaries also reflected some amount of misalignment.

Systemic changes have come about in the operational environment of the industry by way of much more stringent and unavoidable compliance norms

However, discussions with participants across the value chain reveal that almost everyone favours a 'discipline-based' pricing approach presently, irrespective of varying business models. More important, there seems to be more peace among participants – lesser misconceptions and a greater level of understanding. In fact, it seems like manufacturers are genuinely interested in accommodating each other's business models and needs to arrive at a more disciplined pricing approach.

It seems like manufacturers are genuinely interested in accommodating each other's business models and needs –to arrive at a more disciplined pricing approach

Overloading is no longer practiced in most regions. This truck, which left the erstwhile Binani Cement plant on the day of the takeover by UltraTech, is very efficiently loaded

Though loopholes persist, in many areas of operations, compliance is redefined

In the past, in many areas of operations and in the supply-chain, several activities were not fully compliant with existing laws – possibly due to a relaxed approach by regulatory authorities, which proved advantageous to cement manufacturers (directly or indirectly) in terms of better margins. However, over the last 1-2 years, systemic changes have come about in the operational environment of the industry by way of much more stringent and unavoidable compliance norms thereby making it more difficult for any breach. For example, trucks are being monitored online in many cases to avoid overloading, breaking environmental norms, etc. This stringency has had a structural impact on the industry's operating environment and implies higher cost of operations, suggesting that the days of the undue margin advantage are now over.

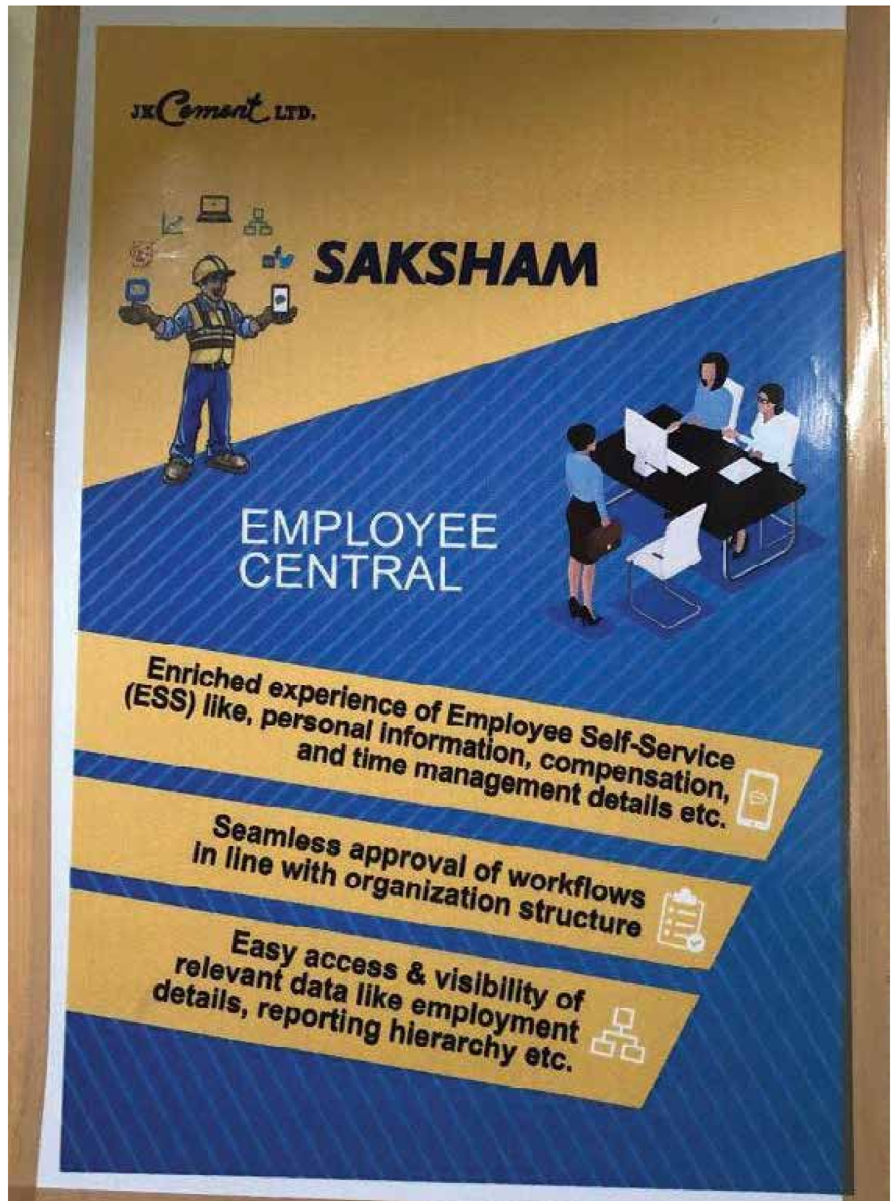
Eventually, prices will increase; it is now a necessity: For the business environment to stay feasible, the tougher operating environment will translate into an increase in cement prices. It is now no longer a need of only the followers but also the leaders – since both are facing equal margin strain and price increases are necessary for everyone. Price increases may not remain 'production-discipline based' but would be rather be 'need based'.

Since each manufacturer's needs differ, they may not align with others. This could keep cement prices volatile for the time being. However, directionally, prices will be on an uptrend.

Qualitative factors are as important for a stable business environment:

It is a myth that only demand-supply equations, a production-discipline based approach, and market share are responsible for cement prices. Price is ultimately a derivative of many other qualitative factors such as:

- Internal connect of employees within an organization at every level – marketing offices, distribution centres, various plants, and even different plants in different regions.
- Educating the ground force. In many cases, these employees work only with individual targets and agendas, which may be very different to the overall organisation-level goals. This is a serious concern, especially in the supply-chain, and ultimately keeps prices uncertain and non-aligned with the top management's agenda.
- Developing employee skills and aligning individual goals to organization goals – in many cases, aspirations of the ground-level employees are not understood well, which keeps their motivation low.
- Making the business model and the distributor network flexible to adjust it for prices or volumes, as per the company's needs.



Organisations are experimenting with innovative mechanisms to educate employees and to bring transparency in their ethos.

Organisations that remain focused on addressing structural and qualitative issues get a lead

Very few organizations have an all-inclusive approach currently where the entire production staff and the supply-chain management are in sync with the company's vision. This is largely because of absence of comprehensive employee development and strong internal connect within employees.

Organisations who adopt best practices early are long-term winners and better insulated vs. peers and competition in a volatile business environments. Manufacturers who take this first-mover advantage will structurally redefine their business models and business practices far better than others.

A newly opened shop of UltraTech Building Solutions (widely called UBS) in the outskirts of Chennai. UBS is an attempt by the cement major to provide full service to an individual home builder

System-wide abuses prevail; this is a key damaging element for prices

Compliance norms at various ends of the supply-chain (loading norms, distribution practices) have been made more transparent and stringent with the implementation of structural regulations such as GST and E-way bill. However, many of the legacy (unethical) practices still exist, especially in the supply chain and distributor network – leading to instability in prices. These practices allowed money-making opportunities for almost everybody in the supply chain through actions such as 'back and forward loading' and material pilferage, but also let to undercutting of cement prices. Given that the regulatory environment is getting tighter, manufacturers have begun to curtail these practices. Players who plug leakages first will definitely have an early mover advantage. If the system eventually becomes smooth (very little choice left, given the dynamic changes in the regulatory environment) overall stability in cement prices will be much better.

Incremental efficiency scope at plant level is limited; challenge is to make distribution chain error-free

In the past, most cement manufacturers tried to discover better margins by making their production operations more efficient in the face of near continuous stress on margins. This was because they either would not or could not delve deeper into the various underhand practices in their supply chain. However, with regulatory tightening and with incremental production efficiencies appearing increasingly limited, manufacturers are likely to focus their full attention on cleaning up their supply-chain efficiency, which will mean better and more stable cement prices.

Some manufacturers already have very efficient plants and have taken up the challenge of correcting supply-chain errors. More companies will follow suit and this transition will bring a sea change in the stability of sector earnings and will also significantly reduce cement price volatility.

Capex cycle has moderated; select companies are spending aggressively on logistics management – A right move

Although the sector is not completely out of the capex cycle, the cycle has moderated. Capacity growth is likely to be at half of its historical pace (3-4% p.a. vs. a CAGR of 7-8% over the past 6-7 years). Select manufacturers have realized the increased importance of inventory management and investments in logistics management (building more depots, silos). The average size of a clinker unit in the sector is nearly double its historical average. Clinker capacity is a key variable that affects the supply dynamics of the sector. Current clinker capacity implies that in the absence of an efficient inventory-evacuation mechanism, pressure on cement prices can be phenomenal, as it will result in a volume push. With the sector's growing capacity, select manufacturers are investing aggressively in logistics and inventory management to ensure that they remain insulated from the risks of fluctuating demand. This is a structural necessity and a long-term positive for the sector.

Not all brands are created equal

Branding with premium and super-premium brands is the 'new' thing but not of them all are able to command and sustain a premium – and this is visible on the ground. Only players

who have an early-mover advantage (started 4-5 years ago) have been able to make a mark in the premium brand segment.

It's a myth that a new brand is only about brand premiums – it is also about gaining market share

Whenever a cement manufacturer talks about launching new brands (most management commentaries have of late) there is general belief that these are with a view to garner additional price premiums. However, new brand launches are not necessarily in the premium brand segment, but are also in lower categories. These launches are about gaining market share, not just brand premiums.

New brands mean new marketing channels

Generally, every new cement brand launched has its own separate parallel marketing channel. However, the scale of operations of a new brand is usually not enough to compensate for cost overheads of its launch, promotions, and channels. All earlier brand launches (and most materialised 4-5 years ago) happened when the market had space and a vacuum for them; that's why they could scale up volumes and manage cost overheads. This is not necessarily true now, so a balanced approach between new brand launches, costs, and revenues is essential to ensure that new brands are not earnings dilutive.

Differentiated channel incentive structure remains a key reason for weak pricing

Barring the ones in south and west India, cement channels are not incentivized for increasing cement prices – a key reason why pricing remains weak in few regions and better in others. In the south and west, the channel actually cares for pricing because the incentives in these regions are ad-valorem and not fixed commissions per bag. The channel's earnings potential improves if it supports better prices.

Directionally, cement prices will be on an uptrend but short-term volatility still persists.

Conclusion

- For now, the cement industry's 'production-discipline' based approach is over. While players appear more inclined towards working with a disciplined approach, it is not something that is likely to materialise soon.

- Efficiency improvements are no longer enough. Bringing back focus on pricing is the key way for the industry to improve margins ahead, given increasing cost overheads and a flawed marketing channel. Few manufacturers have already deemed that stable-to-improving prices is the only way towards a better earnings profile.

- Cement makers have also started shifting their focus from production to supply-chain efficiency, which will eventually bring in much required broader stability in cement pricing. It won't be long before the entire industry throws its weight behind making the supply chain more efficient.

- Conversations with various stakeholders (along the supply-chain and distribution network) revealed much less complaining about competition undercutting prices – which in a way is also a structural positive.

BY ANKIT KEDIA

OTT SERVICES:
AT AN INFLECTION POINT

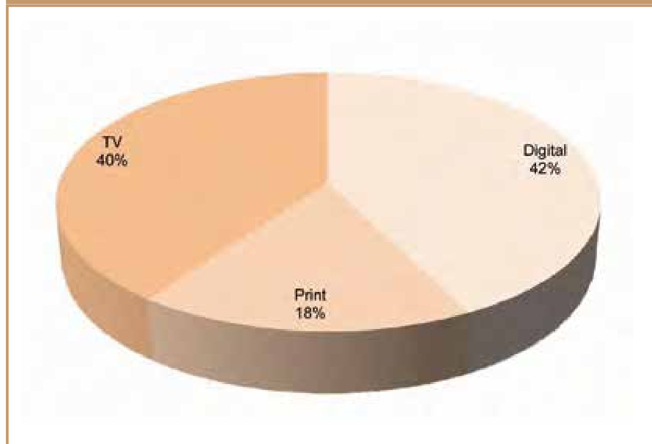
India is potentially at an inflection point for growth in OTT on: (1) increasing connectivity with cheap data prices, (2) increasing supply of differentiated content at affordable price points, (3) increasing affordable smartphone penetration, and (4) favourable demographics.

While TV is reaching maturity levels at 190mn households**, OTT services have a long way to go before they achieve maturity.** Almost every Indian who owns a mobile is a big opportunity for OTT services. Consumers are accessing content on both TV and mobiles. Video watching time has shifted to mobiles over a period from TVs. As per a BCG report, time spent on accessing media through digital mediums is 1.7 hours per day vs. 1.6 hours on TV and digital viewing time is likely to grow exponentially. Few years ago, the OTT audience was young, metro centric, and male. However, today, the audience has changed; there is equal viewing from women, metros are no more the major markets, and the age of the viewer has increased to 44 years from below 35 years.

OTT stands for "over-the-top," the term used for the delivery of film and TV content via the Internet, without requiring users to subscribe to a traditional cable or satellite pay-TV service.

Industry experts indicated that TV shows now get movie budgets to produce quality content. **There is a significant need for good storytelling, which would engage the viewers.** Currently, this is a gap that needs to be filled in TV. For the digital medium, this is an opportunity to attract

Time spent on accessing media (hours/day, % share)



viewers. OTT players are developing consumer habits with quality content. Good stories make good content, which will eventually attract viewers on to the digital platform; TV has not been able to deliver this.

Access, affordability, and availability are the key to success in the OTT space, along with user experience, technology, and content. To be one-up on competition, players would need to partner and collaborate across the value chain – with customers, creators, and advertisers.

For OTT players, depth is the key – they need to reach deep into a particular market or genre in order to gain customer loyalty. Players will achieve size as they deliver regional content. Voice search is gaining traction from customers at the bottom of the pyramid because they are not comfortable typing on the small screen. At the top end, customers use voice searches because they have begun to use devices such as Amazon Echo (Alexa) and Google Home. In the near future,

voice search will be a big driver of growth and most screens will be connected for streaming – companies need to start planning for this eventuality. Currently, there are 32 OTT apps in the Indian market and a BCG reports suggest that 81% customers install only three apps of which the first choice is YouTube, which is anyway pre-loaded in most smartphones today. With increasing competition, content and UI will differentiate players – in that spirit, Amazon has started a Hindi UI and will extend this to Tamil and Telugu languages to attract local customers. Meanwhile Zee5 has launched UI, voice search, and content in 12 languages. More than 60% of the content consumed on OTT platforms is in non-Hindi.

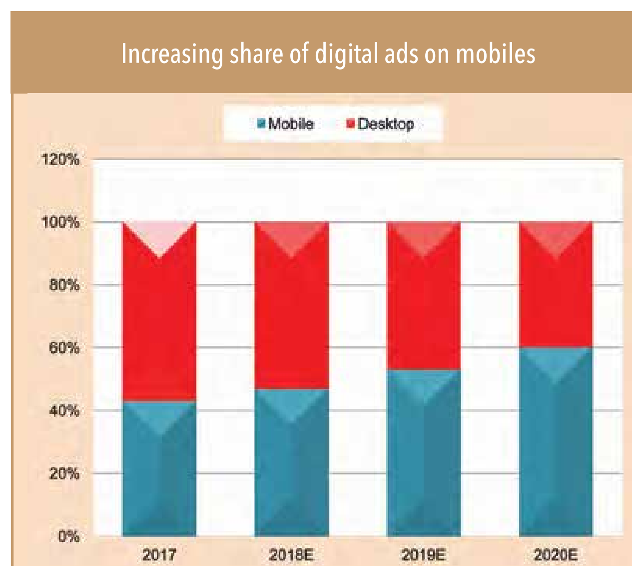
In the Indian ecosystem, **OTT service providers work on three platforms – AVOD (ad-based video on demand), SVOD (subscription video on demand), and the telco-driven aggregator model.** Currently, the India OTT market is a mere US$ 0.5bn, but it is expected to grow to US$ 4.5-5.0bn by 2023 according to a BCG 2018 report. Of this grown market, 43% is likely to be AVOD vs. 82% currently. Therefore, SVOD revenue is likely to grow at a faster clip compared to AVOD revenue for the OTT industry.

For all three OTT business models (AVOD, SVOD, telco), the key to watch would be the lifetime value of customers against the cost of their acquisition, given that churn is very high in the industry. In the AVOD business model, companies would try and maximise watch time and reach. For SVOD, the aim is likely to be maximising subscription and minimising churn. In the telco-driven aggregator model, for further upside, OTT players should tie-up with telcos with high minimum guarantees (against content) and link it with a certain number of subscribers

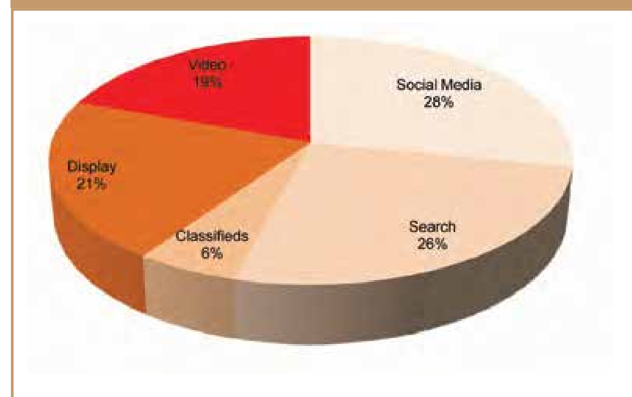
Currently, advertisements are a major source of revenue for OTT players. Gautam Mehra, Chief Data Officer, Dentsu Aegis Network – a company that helps clients with their communication strategies, said that of total digital advertising, Google and Facebook account for 75%, followed by Hotstar at 5-6%. CPM (Cost per million) rates for vanilla ads on Facebook are Rs 50-60 while at its peak, these can go up to Rs 90. For Youtube, CPM rate is Rs 80 with a peak of Rs 200. Similar number for OTT apps are Rs 120-200. However, each app's performance varies in metrics such as completed views and cost per 10/20/30 second view.

Most OTT players are eyeing the ad revenues of FB and Google, so TV will not be immediately impacted. However, if companies change their media plans, then it is possible that incremental share will be given to digital advertising from other categories.

So far, OTT has taken away advertising share from YouTube and FB, not from TV. Mr Mehra was critical and eluded that Google and FB are walled gardens (closed ecosystems) and advertisers/media planners have little choice given their scale. But if OTT and other video players think that they can be wall garden, then there won't attract serious investments. They need to open up and become more transparent.



Breakup of digital advertising (2018); Rs bn and % share of total



Source: DAN E4M Digital report 2019

OTT platforms are targeting premium ads. – that is the Sec A/A+ (socio-economic class) audience and sectors such as auto and BFSI who would not otherwise advertise on niche channels that garner low ratings. Currently, fill rates for OTT players are not at optimal levels.

Another media agency expert said that TV and OTT are experiencing rapid change and advanced analytics are changing dynamics that used to be simple earlier. There is no centralised measurement system in OTT and every player has a different base. In terms of measurement, the digital video space is very fragmented – a third-party measurement will help and drive scale. Focus on the niche audience is best for OTT to derive value in ads as seen in English programming. Ads on OTT offer engagement while ads on TV offer reach.

Vijay Koshy, Head, Brand Partnership at The Viral Fever (TVF) believes that ad-funded content would continue to grow. TVF charges Rs 1.0-1.5mn per episode from advertisers currently, which previously used to be Rs 2.5mn per episode. However, the content has increased to 30-40 episodes/month from 4-6 earlier. Vijay Koshy said that the cost of production for OTT series is twice to four-times more than TV content because: (1) fixed cost is amortised in just 8-10 episodes for OTT episodes against over a few hundred episodes for TV serials, (2) shooting is done usually outdoors for OTT against the studio model for TV, which saves a lot of money, and (3) web series can have big stars while TV takes new comers sometimes. However, web series deliver lifetime value and offer return over a longer period while TV serials have a shorter shelf life.

Advertisers and brands are looking to leverage the audience using content that is more native in nature. This increases the engagement rates and the health of the brand with its audience.

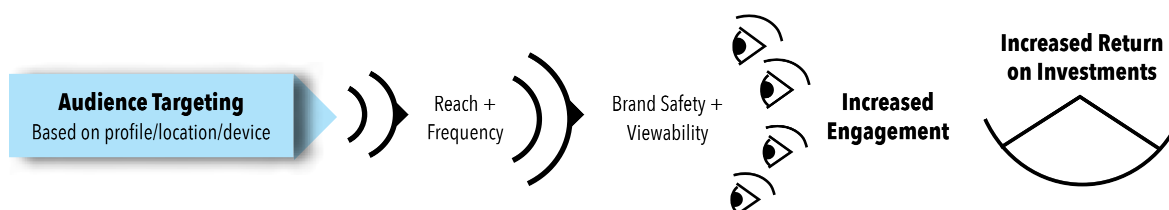
Industry experts suggested that the current market is not an SVOD or AVOD model but AVOD and SVOD model – as seen globally. Customers are willing to pay for subscription at a particular price point for quality content, despite India being a price sensitive market. Content such as cinematic originals and movie premiers do well for SVOD. Sports is always sold through the SVOD model and does very well for Hotstar and Sony Liv.

Subscription packages of various OTT Service providers

OTT Apps	1 month	1 year	6 months
Zee5	99	999	599
Sony Liv	99	499	299
Eros Now	99	950	NA
Hotstar - Premium	199	999	NA
Hotstar Sports	NA	299	NA
Amazon Prime	129	999	NA
Netflix	500-800		
Alt Balaji	NA	300	100 (3 months)

Uday Sodhi, Business Head (Digital) at Sony Pictures Network India, revealed that currently subscription revenues are highly dependent on willingness to pay, ability to pay, and amount to be paid. Uday believes that customers are willing to pay on the spot, but the major issue is ability to pay on a monthly basis through auto payments. Paytm would have 35% of the total transactions for Sony Liv and customers tend to have a balance of only Rs 20 when their auto payments come up. Churn is high because of this, as customers have difficulty paying. However, Uday is confident that subscription revenue can become 5-10x in the next few years on higher subscribers and increase in package prices. He believes that ex-Netflix and ex-telcos industry subscription revenues would be less than 10%.

Effectiveness of OTT



BY SURYA PATRA & MEHUL SHETH

INDIAN SPECIALTY CHEMICALS TO CONTINUE ON SPLENDID GROWTH PATH

Ground view organised a "Phillip Capital's 4th Annual Specialty Chemicals Conference" as a follow-up to its detailed research on the India specialty chemicals sector (February 2018 issue) that talked about exponential growth for the Indian specialty chemicals industry. In this day-long event, GV hosted Shri Samir Kumar Biswas, Joint Secretary, Ministry of Chemicals & Fertilizers, Shri Satish Wagh, Chairman, Chemexcil, Leading specialty chemicals consultant from China, Shanghai, China, Shri Vivek Gadre, President Commercial, Atul Ltd, Shri L. Balakrishna, MD, Brenntag Ingredients (India) and Shri Amit Gandhi, Partner & Director, The Boston Consulting Group, India.

The panel discussion as well as the presentations by the chemical consultant from China and the Boston Consulting Group reaffirmed PhillipCapital's prediction of "multi-year and multiplying growth for the Indian specialty chemicals industry".

Panellists believed that the Indian specialty chemicals industry is set for strong sustainable growth led by healthy domestic demand, backed by strong GDP progress, and rising per capita income. However, they emphasised the need to invest in technology platforms, R&D, and IPR, in order to differentiate, create greater customer value, and develop strategic partnerships with customers.

The Government of India, represented by Mr Samir Kumar Biswas, Joint Secretary, Ministry of Chemicals & Fertilizers highlighted its initiatives such as Make-in-India and FDI through the 100% automatic route, but reaffirmed its stance on environmental protection (no relaxation in environmental clearance requirements). Also, visualising the opportunity flowing into India as a consequence of China-related issues, Mr Biswas said that the long-standing issue of feedstock availability for the Indian chemicals industry should be resolved due to the signing of a US$ 44bn refinery + petchem project with Saudi Aramco (plant to be set-up in Maharashtra).

Incremental exports opportunity for the Indian industry became apparent in a presentation by one of the leading chemicals consultants from China on the ongoing challenges for the Chinese chemical industry.

Key highlights about China and inferences for the Indian specialty chemicals industry are detailed below:

The Chinese government is firm about its environmental policy implementation; not likely to relax: China's emerging middle classes are health conscious and are forcing the government to fight pollution. Therefore, regulation of China's chemicals industry is already tight. Steady GDP growth despite planned clampdowns of polluting industries have strengthened the Chinese government's resolve about remaining strict as far as environmental policy implementation is concerned.

Half of China's chemicals industry WILL relocate, that too in a set period: China's government has already made it mandatory for chemical plants to operate from chemical parks, but only c.45% are currently complying with this norm. This implies major plant shutdowns or relocations ahead. Moreover, the government wants plant

relocations to take place in a time bound manner and has accordingly set a deadline of CY20 for small-/mid-sized plants and CY25 for large ones.

Inference for the Indian industry: Given the time-bound relocation plan, plant shutdowns and relocations in China are likely to continue over the next few years. Since Chinese exports of specialty chemicals is about 10x larger than the Indian industry, a visible slowdown here could multiply the size of the Indian specialty industry over the next couple of years.

Rationalisation of chemical parks and restrictions have led to uncertainty: China expects to restrict the number of its chemicals parks in order to reduce overcapacity in low-end products and achieve better control over effluents. For example, the Shandong Province has decided to halve the number of its chemicals parks to less than 100, and has tightened the certification criterion accordingly. Such initiatives have led to uncertainty for many industry participants.

Additionally, restrictions like prohibition of chemicals production within a kilometre of the Yangtze river (the world's third-longest river, which flows through nine provinces of China), environmental tax (imposed from January 2018) and specific emission norms (implemented from July 2018) have added to the woes of chemicals players in China.

Inference for the Indian industry: The environmental policy initiatives, selective restriction practices by various Chinese provinces, and rationalization of chemicals parks have made the functioning of a large set of China's chemicals players uncertain. Additionally, the country no longer holds its age-old cost advantage in terms of wages, input materials, utilities, etc. Consequently, MNCs (sourcing of input chemicals from China) will be forced to de-risk their procurement strategies (yet to play out). India, being a cost effective manufacturing base with a presence across segments, should be in a good position to grab this huge export opportunity.

Not only have regulations tightened, implementation has really become stricter: The discovery of facts that ~55% of chemical companies (out of the 45,000 inspected over H2CY17) are non-compliant to the environmental policy norms, and a consequent anti-corruption campaign initiated by Xi Jinping from early 2018 has already made evasion of regulation via bribery and/or local connections quite difficult in China. Another round of inspections across China started in June 2018 and will continue until April 2019. For this, the central government has appointed about 18,000 inspectors under 200 teams.

China's concerns about pollution and overcapacity ensure that most plants closed in the course of the environmental campaigns will not reopen: Environmental protection and safe chemical production remains the core objective of China's government. Towards this, it considers overcapacity in polluting chemical industry and presence of large number of fringe chemical manufactures as hurdles. To do away with these impediments, the Chinese government has created entry barriers such as scale/size and investment restrictions for players with weak market competitiveness and small scale. For example – Shandong Province has imposed a minimum investment restriction of RMB 300mn (about EUR 40mn). Similarly, Fujian province wants consolidation in its chemical industry.

China's central government has decided to disallow relocation of those chemicals manufacturers that are found guilty of not complying with waste disposal norms during the countrywide inspections into chemical parks – implying their complete closure.

Inference for the Indian industry: China's planned efforts to reduce overcapacity in basic chemicals have already reduced the concern of dumping, leading to stabilisation in prices. This would help Indian companies with exposures in dyes, amines, carbon black, chloromethane, fluorine/nitrogen compounds, and benzene derivatives.

Chemicals prices in China have already appreciated and are likely to remain firm ahead: Prices have already risen by 25-40% because of the continuing clampdown and consequent shortages in various chemicals, coupled with rising operating cost caused by environment compliance and relocation. Even if such prices do not sustain in the long term, the pricing scenario should remain firmer than before, as most of the policy changes and their consequences (in terms of cost escalation) are structural.

The benefit of rising prices – aggregate profit of the Chinese chemicals industry YTD CY18 increased 15% while aggregated sales growth was just 6%; this, despite a shutdown of 6% chemicals companies.

China has become a market with huge opportunities: While tightened environment regulations in China may have a negative effect on companies sourcing chemicals from China, it should benefit companies that compete with Chinese chemicals producers. Additionally, in some cases, increased environment regulations have turned China from an exporter to an importer, providing a positive outlook for demand and pricing.

Inference for the Indian industry: Weakening competitiveness of Chinese players (caused by operating restrictions), shortage of various chemicals (due to continued clampdown), significant rise in chemical prices (prevailing higher than international market prices) and the sheer size of China's market (US$ 1.5tn, c.45% of total global market) offers great value/volume opportunities for select Indian companies with a market presence in China. Specifically, leaders such as Aarti Industries and Vinati Organics with an established market presence in China should be key beneficiaries. China has been reported to import dye raw materials such as vinyl sulfone and H-Acid (dye intermediates) from India, reversing its previous role as an exporter to India (as local production

of these chemicals declined by 50-60%) – this should benefit leading integrated dye companies such as Bodal Chemicals and Kiri Industries.

Environmental changes are not temporary; the mind-set of local officials in China has changed: China's central government has already made surprise inspections of chemical manufacturers a regular phenomenon, and set up a team of 18,000 inspectors. Accordingly, the mind-set of governing body at provinces, local officials, and administrative bodies at specific chemical parks is well aligned with the central policy.

China to remain the global leader in chemicals, but may not be export oriented: Given the increase in operating cost structures in China, chemicals prices have risen there beyond the levels in international markets. This offers better realisations to chemicals companies in the domestic market itself, where they have well established supply chains; an added advantage is that China is the biggest market for most chemicals produced. Due to this change, China expects to become self-sufficient in chemicals, with limited focus on exports.

Inference for the Indian industry: Given China's limited focus towards chemicals exports (China's chemical export is worth c.US$ 210bn (c.6x India's as of CY17), India could prove to be the leading beneficiary of this export opportunity.

Areas of opportunity for India: The Chinese government is keen to supplement innovation towards complex chemistry but its core focus remains on scalable segments. Hence, Chinese peers are not keen on specialty chemicals those are niche but low volume opportunities and require customisation. Also, Indian companies will be beneficiaries in the non-priority areas of China (i.e less supported by Chinese policy), particularly the segments with commodity and polluting nature.

Inference for the Indian industry: China, with larger focus on scale, should not pose a threat to the Indian industry, which has always been focused on customised products. Aarti Industries, with its strategic focus on customized benzene derivatives, should benefit. Going by China's prioritization, Indian companies with a focus on dyes, solvent-based coatings, plastics, and rubber additives, chlorine chemicals, agrochemicals, intermediates (agro/Pharma), and leather chemicals should benefit.

OPERATING OUTPERFORMERS

According to PhillipCapital India Research, the following companies will deliver significant operational outperformance in 2019, driven by rural as a growth theme and infrastructure plays.

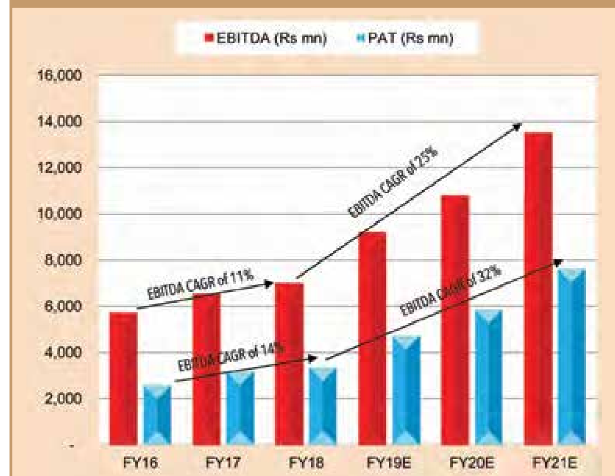
Aarti Industries Ltd

ARTO IN | MCap: Rs 127bn

Target: Rs 1600 | Rating: **BUY**

- ARTO's unique business model of manufacturing customised products (85% of sales) for global MNCs stands out among its Indian peers.
- To see healthy growth led by:
  - Global leadership in chemical processes like chlorination, nitration, hydrogenation, ammonolysis.
  - Longest chain of benzene derivatives strength.
  - Long-standing supply pacts with global MNCs.
  - Established supply-chain management.
  - India-specific cost advantage.
  - Weakening of Chinese chemical manufacturing competition.
- ARTO is also a key beneficiary of a visible manufacturing shift into India after the Chinese clamp down on manufacturing.
- We estimate healthy earnings growth trajectory of 33% CAGR over FY18-20. We see this accelerating further backed by its two multi-year supply pacts with MNCs (10-year pact – Rs 40bn opportunity; 20-year pact for Rs 100bn starting from FY21).

Aarti Industries: Set to deliver secular growth



Axis Bank

AXSB IN | MCap: Rs 1789bn

Target: Rs 765 | Rating: **BUY**

- The 'rating downgrade' cycle seems to have normalised, thus moderating the incremental flow to its watch list. As a result, vulnerable pool of loans has declined to Rs 96bn in Q3FY19 – or 1.9% of loan book – from 9% in Q1FY17.
- As the bank moves out of a high credit-cost cycle, we expect it to fire up its growth engine under the new management.
- High growth along with lower credit cost should lead to rising RoE. We expect RoE to improve to +16% by FY21 from 6% in FY19. In addition, we expect substantial amount of value unlocking from its subsidiary and the option value from its Insurance distribution business.
- At CMP, the stock trades at 2.4x/2.2x our FY20/21 BVPS of Rs 270/306. We value the bank at 2.5x FY21 ABVPS of Rs 306.

Axis Bank: Normalisation of credit cost to drive ROE

Bajaj Electricals

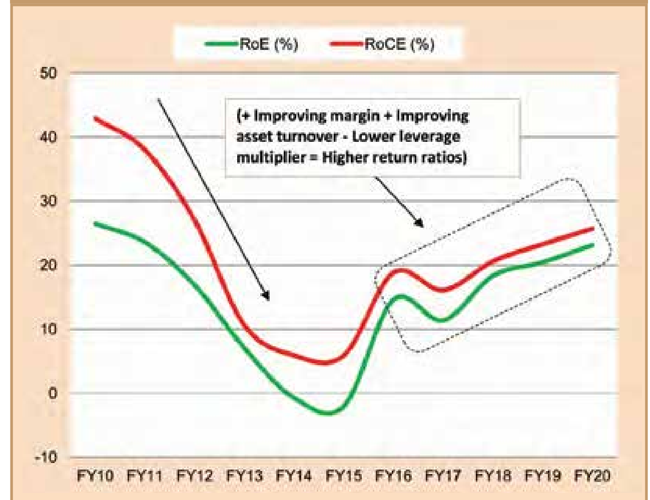
BJE IN | MCap: Rs 48bn

Target: Rs660 | Rating: **BUY**

- Implementation of TOC (Theory of Constraints; started two years ago) and RREP (Range and Reach Expansion Program) have begun to yield strong results.
- Solid distribution channel with 185,000 touch points.
- Increased product penetration and improving visibility, which channel partners indicate has resulted in a strong double-digit revenue growth in CD (consumer durables).
- In E&P, execution has increased and it is more selective about projects. The company has also improved margins and reduced WC through lower inventory (order book of Rs 7bn).
- Tight control on working capital and channel financing under TOC is resulting in lower working capital needs in CD business.
- We assign a target multiple of 30x to CD (15% discount to the industry average) and 8x EV/EBITDA for E&P. SOTP-based target of Rs 660 (Rs 491 CD + Rs 169 E&P).

Bajaj Electricals: Strong growth from CD and E&P business

Bajaj Electricals: Improvement in profitability resulting improvement in return ratios



Container Corporation of India

CCRI IN | MCap: Rs 322bn

Target: Rs 900 | Rating: **BUY**

- Concor enjoys a significant competitive advantage and economies of scale due to scheduled services between major port traffic centres and its nationwide terminal network. It has market share of c.73% in exim container rail movement while the second largest player is c.1/10th of its size in term of infrastructure.

- Western Dedicated Freight Corridor will enhance its competitive edge significantly (hub-and-spoke model gaining prominence) by reducing lead times with higher speed (c.2x) and higher cargo carrying capability by double stacking of containers yielding significant reduction in capital intensity resulting in improvement in return ratios. Concor has c.84% market share for rail movement at largest container port i.e JNPT and would be major beneficiary of DFCC due to double stacking of containers form JNPT after DFCC.

- The company is leveraging its strong asset base to benefit from multimodal movement and providing end to end third party (3PL) logistics solutions with focus on coastal shipping and distribution logistics. The company has ambitious plans for its coastal shipping business and has finalised one contract for the west coast - Kandla to Cochin. Under distribution logistics, it is providing last-leg logistics support with value addition in packing, labelling, and storage on a PPP basis. It is developing businesses with asset-light models.

- CCRI's stock is trading at a PE of 20x FY21 and EV/EBITDA of 11x. We expect revenue and earnings CAGR of 19% and 14% over FY18-20, assuming economic recovery and operating leverage from current capex. We have not assumed SEIS benefit from FY21. We continue to value the company on DCF (to account for its aggressive capex plans to capitalise on container growth once freight corridors are operational).

Divi's Laboratory Ltd

DIVI IN | MCap: Rs 398bn

Target: Rs 1610 | Rating: **BUY**

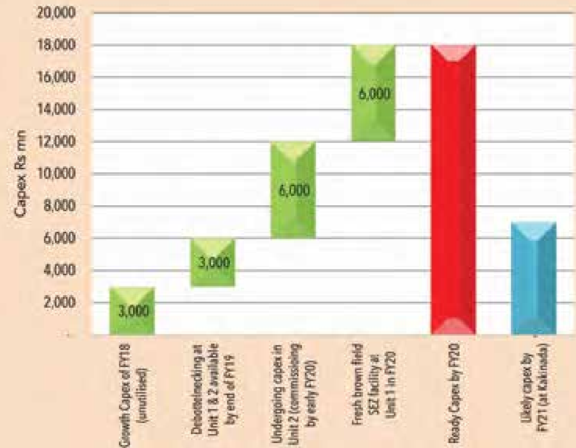
- Best beneficiary of two structural opportunities – global innovative pharma outsourcing and Chinese supply disruption.

- Spots multi-year business opportunity from China's supply disruptions: While the global pharma industry is worried about ongoing supply disruptions and inflationary pressures in drug prices in the wake of ongoing environmental concerns in China, DIVI, being one of the leading global manufacturers of APIs and intermediates, sees great supply opportunities.

- Custom synthesis outlook remains robust: Conducive outlook for pharma outsourcing emerging from price challenges for innovative drugs, reduced R&D productivity, and increased regulatory requirements should ensure sustained long-term growth for DIVI, based on its strong track record with top-10 global innovators.

- Well-placed with ready capex to grab opportunity: DIVI announced a brownfield capex of Rs 18bn recently, which provides enough visibility of growth.
- Outlook: We expect 29% PAT CAGR over FY18-20, which makes it a preferred/safe investment idea in the wake of weakening outlook for generics pharma peers.

Divis Laboratory Ltd : Well-placed with ready capex to grab opportunity from Chinese concerns



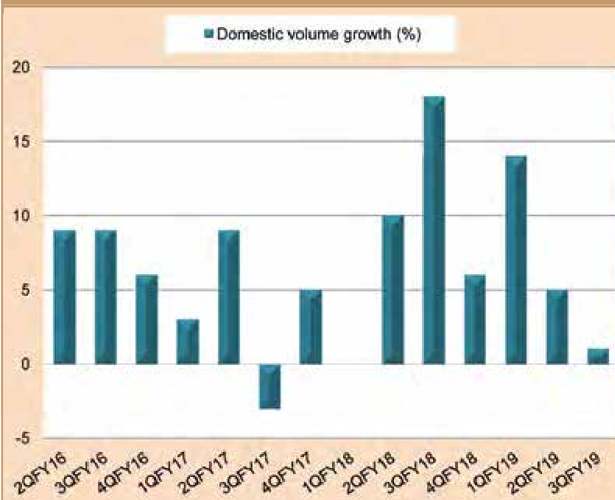
Godrej Consumer

GCPL IN | MCap: Rs 774bn

Target: Rs 645 | Rating: **SELL**

- Household insecticides (50% of domestic business) is likely to see subdued growth due to extreme weather conditions, increased competition from unorganized incense sticks players.
- International business (50% of overall sales) performance has been very volatile due to geopolitical risks and macro-economic instability in key geographies. We do not foresee any meaningful change in the medium term.
- Lower ROCE, higher working capital requirements and instability in operating performance vs. FMCG peers calls for lower valuation multiple vs. sector.

GCPL: Domestic volume growth (%)



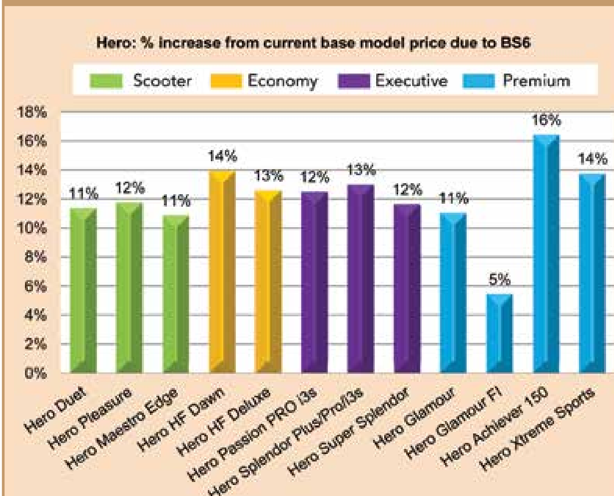
Hero Motocorp

HMCL IN | MCap: Rs 558bn

Target: Rs 3000 | Rating: **NEUTRAL**

- Hero Motocorp will underperform its peers as:
- Cost pressure will increase due to mandatory CBS/ABS from April 2019 and BS6 from April 2020 leading to 13-15% price hikes by the OEMs.
- After strong industry growth in FY20 (PC estimate 13%) we see volumes declining by 8-10% in FY21 as sharp price hikes lead to demand postponement.
- Honda's renewed aggression and aim to become the #1 player (led by scooters) will keep Hero's marketshare performance under pressure.

Hero: % increase from current base model price post BS6



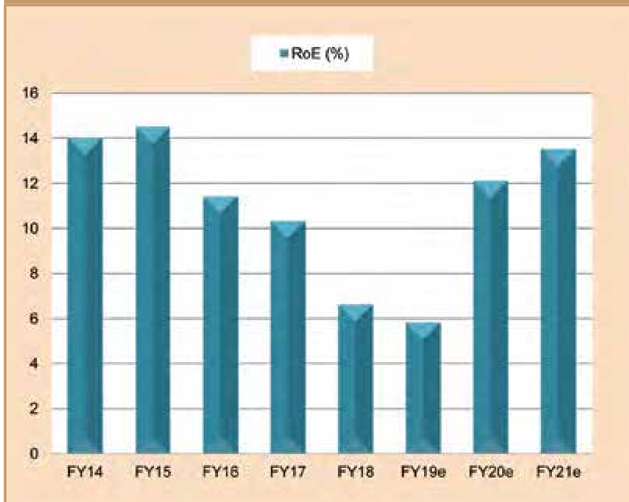
ICICI Bank

ICICIBC IN | MCap: Rs 2355bn

Target: Rs 460 | Rating: **BUY**

- Strong credit growth, recovery of NPAs, and margin improvement should trigger earnings upgrades.
- The bank has developed a strong and stable retail franchise in terms of both liability and loan book.
- Rising interest rate and tight liquidity should enable it to gain market share from non-banks.
- Reversal in the corporate NPA cycle, declining credit costs, and expected earnings trajectory would culminate into growth coming back to the corporate banking segment as well.
- Low cost of deposit, absence of interest reversal, and recovery of large-ticket NPAs would be a key catalyst for NIM expansion in our view.
- Strong provision coverage of 69%, moderating slippage, and improving recovery of bad loans will bring down its provisioning requirement ahead thus driving profitability.
- At CMP, ICICIBC trades at 1.35x FY21 core ABVPS of Rs 177 (valuing subsidiaries at Rs 104). Inexpensive valuations and a visible turnaround in the NPA cycle make ICICI a strong candidate for re-rating.

ICICI Bank: ROE to move towards its long-term average



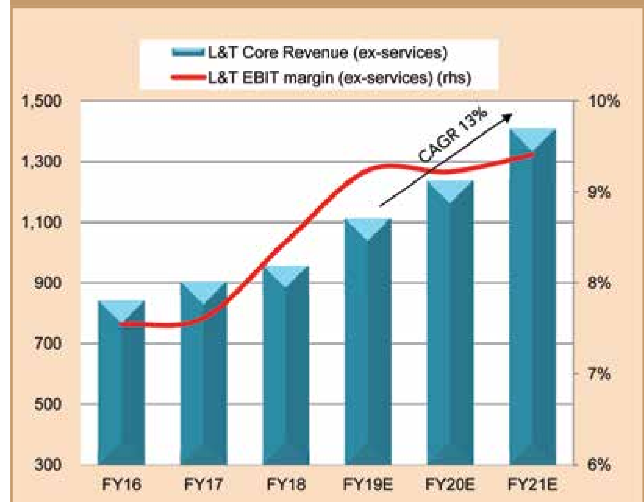
Larsen & Toubro Ltd

LT IN | MCap: Rs 1834bn

Target: Rs 1520 | Rating: **BUY**

- L&T is India's largest EPC player and has an exposure to the entire capex cycle. It will be a key beneficiary of the pick-up in the domestic capex cycle driven by the government in defence, hydrocarbons, roads (Sagarmala project), railways, metro rails, water, and irrigation. It is also engaged in financial services and IT & technology services through its subsidiaries, which contribute significantly to its profitability.
- Incrementally, the environment for execution has improved and L&T's strong order book (2.7x TTM sales) and controlled working capital allow it headroom to push for execution.
- Expect L&T to gain market share as complexity of projects increase over the next three years in the domestic market. This along with pick up in orders from the Middle East and Africa could offset the temporary slowdown in domestic orders.
- It may generate strong cash flows with the completion of major capex/investment (Hyderabad metro in FY20) and pick up in monetization of real estate at the Hyderabad Metro along with divestment of stake in non-core business.
- L&T's focus on its strategic plan-2021 to achieve RoE of 18% in FY21 (vs. 15% in FY19) will result in payback by the company to the investors in the form of higher dividend payouts and share buybacks.

L&T: Core in E&C business to report health growth in revenue and improvement in margin



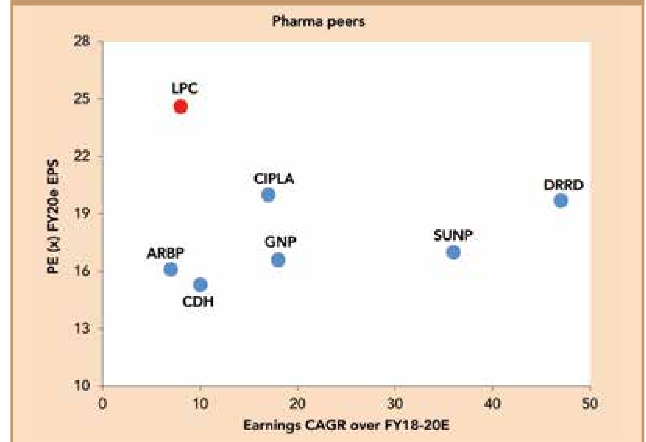
Maruti Suzuki

MSIL IN | MCap: Rs 2175bn |

Target: Rs 8000 | Rating: **BUY**

- Easing macro concerns and cooling oil prices to improve demand outlook
- Structural story intact with PV penetration still remaining low at c.2%.
- Softening of commodity prices, favourable model cycle, and new launch pipeline to aid margin improvement.
- Maruti is the only company in our coverage that is least impacted because of the impending shift in emission norms to BS6.
- We remain firm on the name and see the stock outperforming its peers.

Lupin: Concerned about growth and regulatory challenges



Lupin

LPC IN | MCap: Rs 392bn

Target: Rs 670 | Rating: **SELL**

- LPC has already reported 70% decline in earnings in H1FY19 due to continued underperformance in its US business (flagship segment with 38% sales contribution) caused by no new meaningful drug launches and continued pricing pressure. LPC has few interesting launches over next few quarters – Levothyroxine, gRanexa, and couple of respiratory drugs in the US market). But we expect earnings downgrades soon, led by structural challenges in the US including intense competition, pricing pressure, and political intervention.
- Ongoing regulatory concern over its key plants – Goa and Pithampur – which are under warning letter from USFDA since November 2017 and saw repeat observations in re-inspection – could potentially delay key drug approvals and hence growth.
- While domestic formulation (26% of sales) is on a steady growth path, its third-largest market (Japan with 15% sales mix) is declining due to compulsory bi-annual price cut.
- Addition to growth concerns, rising material costs, increasing R&D spend, building up of specialty sales force and weak revenue mix will certainly hurt operating efficiency.
- Despite muted earnings growth (estimated 8% CAGR over FY18-20) and continued underperformance, LPC trades at >30% premium multiple to industry peers.

NCC Ltd

NJCC IN | MCap: Rs 52bn |

Target: Rs 145 | Rating: **BUY**

- NCC has corrected significantly over the last year (CY18, -36%) – and is trading at FY20 P/E of 8x, at a discount to peers (average 10x).
- No better rerating candidate in the infrastructure space than NCC based on strong and diversified orderbook (3.4x book-to-sales), sturdy balance sheet (0.3x debt:equity), and FY19-20 topline/earnings CAGR of 35%/52%.
- Despite the lax order award activity in FY19, NCC has managed to clock c.Rs 110bn orders YTD and topline of Rs 55bn (+65% yoy) in 1HFY19 – looking well set to exceed its order inflow guidance of Rs 140bn and revenue guidance of Rs 110bn (+45% yoy) in FY19.
- At the same time, its subsidiary losses have come down significantly (from Rs 2.5/1.5bn in FY17/18 to only Rs 46mn in 1HFY19), leading to superior profitability at the consol level.

NCC: Strong topline growth with stable margins

Tata Consultancy

TCS IN | MCap: Rs 7151bn |

Target: Rs 2300 | Rating: **BUY**

- TCS' stock, while expensive, will keep getting more dear as its performance continues to defy gravity.
- We believe TCS belongs to the category of stocks such as HUL, Maruti, HDFC Bank, and Sun Pharma – market leaders in their respective domains, who command a significant premium over peers because of their positions.
- Capturing large deals has been its USP.
- TCS has reported unprecedented deal-flow in last four quarters at US$ 9.8bn, including multi-year billion-dollar deals from Nielsen, Transamerica, and Prudential. Strong deal-flow and return of large deals augur well for the company.
- We expect the momentum provided by the recent deal-flow to help TCS deliver sustainable double-digit USD revenue growth in FY20 and beyond. At the same time, its margins will remain stable.
- Essentially, TCS is the only company in the large-cap space, with NO concern over its growth or margins, while delivering a superior ROE of 30%.

TCS: Strongest topline growth (among large-caps) with stable margins

Tech Mahindra

TECHM IN | MCap: Rs 700bn |

Target: Rs 650 | Rating: **SELL**

- Over the last seven quarters, it has fired over 9,800 of its software employees and awarded below industry average hikes after two years of no salary hike. Meanwhile, its trainee count in the system is almost ZERO and utilization is at unsustainable 82%. These statistics point to a precariously poised operational model – we anticipate possible delivery issues in near future for the company.
- TechM's telecom vertical (+US$ 2bn) has become too big to grow in double-digits – especially with global giants like AT&T, Verizon, and BT already under its belt.
- Its Enterprise division has been driven inorganically; the company does not have any significant USP in segments such as BFSI, retail, and manufacturing.
- Over the medium-to-long term, TechM's telecom vertical will grow BELOW industry average and the enterprise business will grow AT industry average. This combination – of half of its business growing 'AT' and the other half 'BELOW' industry average – will keep TechM's growth, and therefore multiples, lower than peers.

Tech Mahindra: Significant reduction in software employee workforce over the last seven quarters

Titan Company

TTAN IN | MCap: Rs 852bn |

Target: Rs 1075 | Rating: **BUY**

- Titan remains a key beneficiary of an increasing consumer shift to organised jewellers as unorganised jewellers find it difficult to operate due to increasing cost of compliance in an industry where margins are wafer-thin
- Foray into the highly lucrative wedding jewellery market, increasing traction on the revised gold exchange programme (providing more value to customers by cutting rate of deduction to 0%), and continued traction for its Golden Harvest Scheme.
- Improving margin trajectory in its watches business on improved sales mix, cost control initiatives, and price-correction measures taken in the eyewear segment will also aid growth.

Titan: Market share gains to continue in Jewellery segment

Wipro

WPRO IN | MCap: Rs 1640bn

Target: Rs 390 | Rating: **BUY**

- Wipro has been hit hard due to its unique business mix. A sharp fall in crude prices in FY16 meant most of its E&U clients postponed their IT spending. In FY17, the uncertainty related to the future of Obamacare (with the advent of Donald Trump) led to a decline in the HPS business. Wipro has the highest exposure to this segment (12% E&U, 14% healthcare), which had a significant impact on its growth.
- However, over the last six quarters, while Wipro's overall revenues have seen moderate growth, growth excluding E&U and healthcare has been much superior to peers. It has been driven by large verticals of BFSI, manufacturing, and consumer, which have all consistently reported strong growth. We believe that with crude prices now stabilizing and if ambiguity about Obamacare clears soon (hopefully), a revival in these segments is imminent and it will benefit Wipro as disproportionately positively as it had negatively.
- In addition, Wipro has been following one of the most efficient capital-allocation policies amongst its peers – with a healthy balance of dividend, buybacks (two in last three years), and acquisitions. We expect a healthy mix of organic growth and efficient capital allocation to lead to significant rerating of the stock.

Verticals Growth (yoy %)	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19	Q3FY19*
Communications	-8.6%	-8.9%	-8.5%	-11.3%	-15.4%	-11.1%	-7.4%
BFSI	6.5%	13.7%	18.2%	18.5%	15.5%	12.8%	15.1%
Manufacturing & Technology	2.1%	6.9%	7.7%	6.4%	2.8%	-2.6%	-5.3%
Healthcare & Lifesciences	-1.2%	-10.0%	-7.4%	-4.8%	-6.9%	-5.3%	-5.0%
Consumer	2.1%	6.4%	7.1%	4.2%	4.1%	3.9%	7.2%
Energy & Utilities	3.7%	10.0%	0.9%	0.7%	-4.1%	-5.4%	6.2%
Total Growth (yoy %)	2.1%	5.1%	5.8%	5.5%	2.8%	1.4%	3.7%
Growth (Ex E&U) (yoy %)	1.9%	4.3%	6.5%	6.2%	3.8%	2.4%	3.4%
Growth (Ex E&U, Healthcare) (yoy %)	2.5%	7.6%	9.7%	8.6%	6.1%	3.9%	5.0%

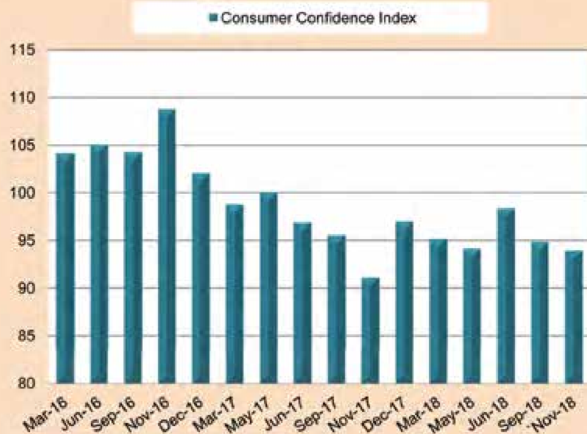
EVENTS THAT DEFINED 2018

BY ROSHAN SONY

#AmericaFirst #26/11NeverForget
#ImranKhanPakPM #AIRINDIA#AtalBihari
Vajpayee #AadhaarLeak #ANGELAMERKEL
#IndiaMonsoonToll #AugustaWestland
#AlokVerma #BOKOHARAM #IndonesiaTsunami
#AvniMurder #BankRecapitalisation
#BinnyBansal #BYJU #JairBolsonaro #BorderWall
#Comcasa #MailBombs #Brexit #GiuseppeConte
#KartiChidambaram #CambridgeAnalytica
#DalitAgitation #GOOGLEWAYMO #KathuaCase
#ChandaKochhar #FacebookUnderFire
#GUNCONTROL #MarathaReservation #IL&FSCrisis
#H1BVisaRestrictions #HIJABPROTESTS
#IranNuclearDeal #HimanshuRoy
#IndiaGST #JamalKhashoggi #ISIS
#NationalCitizensRegister #YellowVestMovement
#LandmarkSCJudgements #NuPower
#LTCGIsBack #Rajnikanth #MeTooIndia
#RakeshAsthana#NaMo #SabrimalaWomenEntry
#Nipah #Sentinelese#NiravModi #SouthChinaSea
#Padmavat #StatueOfUnity #PNBScam
#SyriaChemicalAttacks #RafaleDeal
#TalibanResurgence #RaGa #YemenCrisis
#Section377 #Telangana #Shridevi #Zainab
#Uighurs #ThaiCaveRescue #TradeWars
#Unnao#Trump #WorldCup #UrjitPatelResigns
#XiJinPingForever #ISRAEL

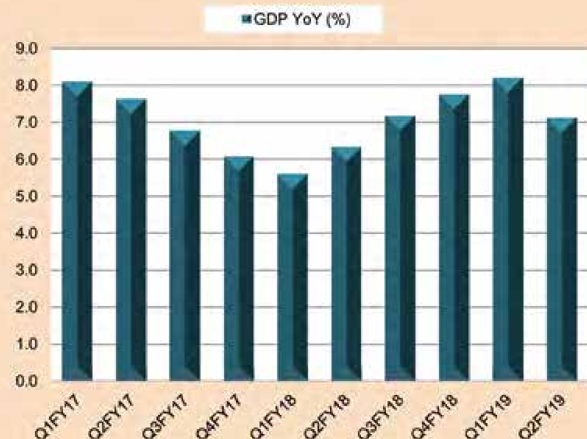
INDIA 2018: YEAR IN CHARTS

Brief mid-year spike in consumer confidence

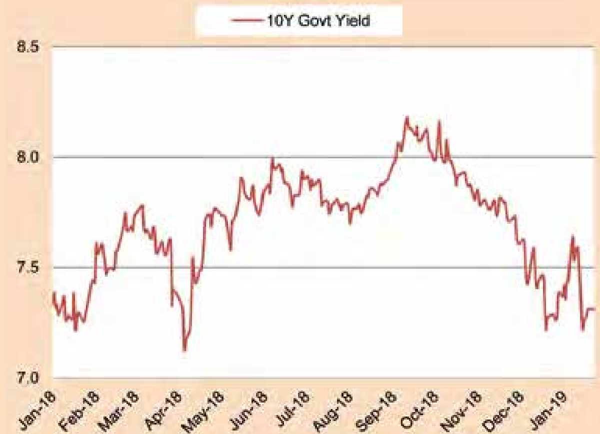


Volatile. Rose to 38,000+ between April and September. +Fell sharply to below 34,000 by November

India GDP growth – dipped in Q2FY19

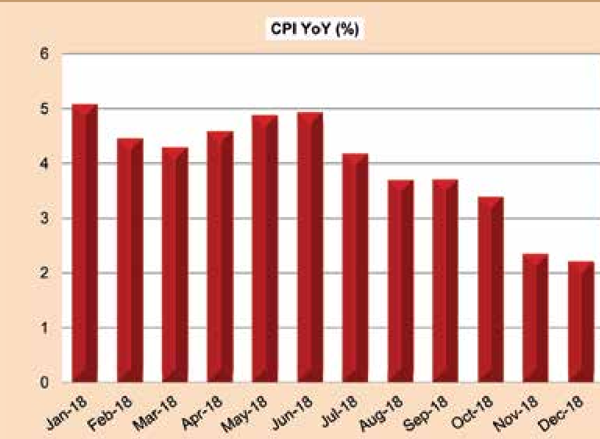


Volatile. Fell to almost 7% in April 2018, spiked to 8%+ in October 2018

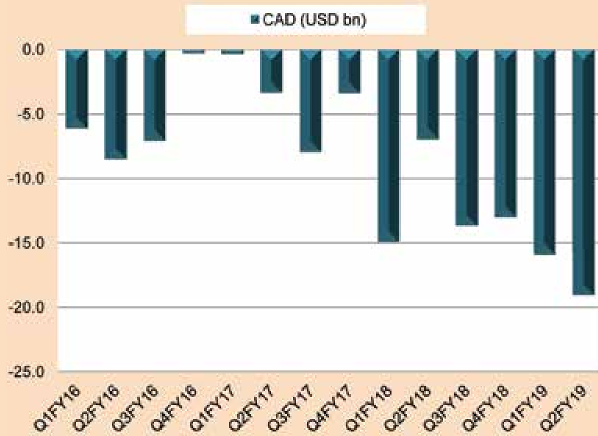


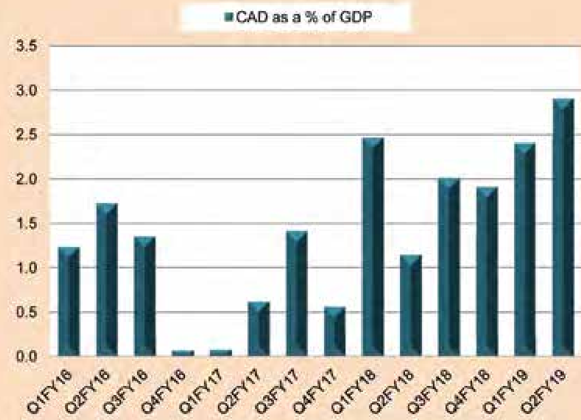
USDINR went all the way from below 64 to above 74 this year

Inflation was between 4%+ and 5% from January to June 2018. Began to fall steadily after that – touched 2.19% in December. Food inflation down sharply after October

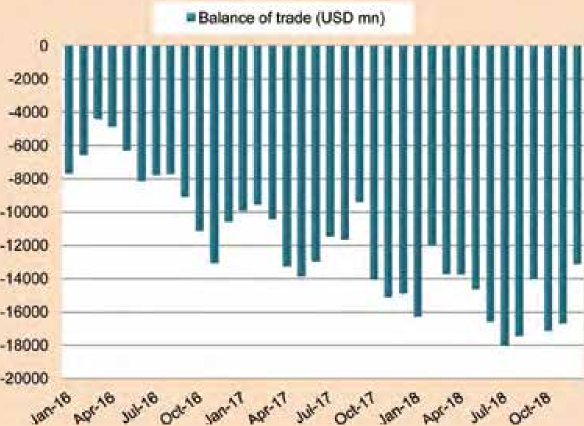


Current account deficit: Under pressure. Kept widening through the year

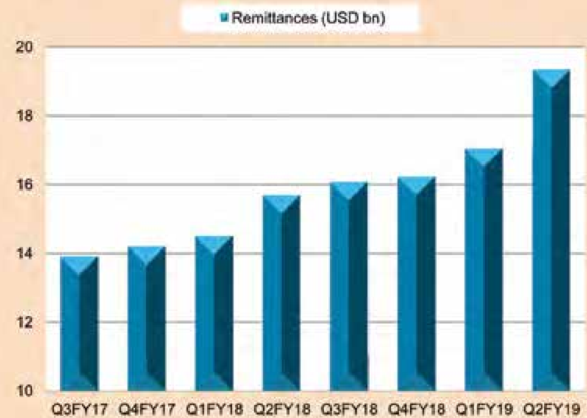




Balance of trade: Strained. With China-US trade wars, worries on this front have escalated

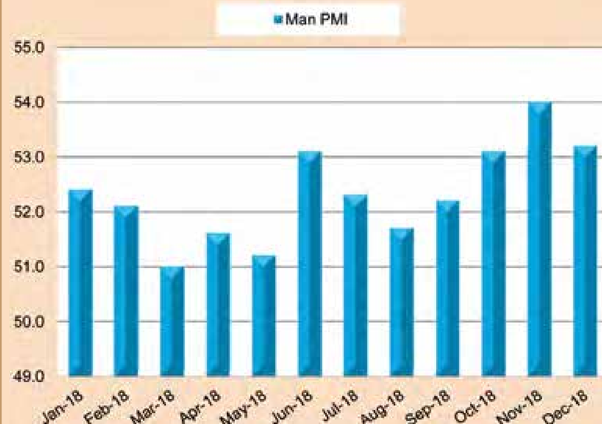


Remittances have risen sharply in 2018.



Gold reserves – up sharply. The RBI was buying gold for the first time in nine years as a hedge against volatile currency markets.

After a slump in August 2018, Manufacturing PMI has been rising



INDIA 2018: YEAR IN CHARTS

IIP: Sharp drop in November 2018

Aluminium prices stayed subdued in 2018

Copper prices stayed subdued in 2018

Steel prices fell in 2018. Asia demand seen flat

Volatile. Went up from below US$ 70 per barrel to above US$ 89 by September. Crashed to almost US$ 50

Gold ended the year flat after a sharp mid-year dip. Outlook is neutral

RETROSPECTIVE PERSPECTIVE

Can a year be non-exciting? In today's fast-paced digital world, that's unlikely, isn't it? State elections in India, the US-China tariff war, Brexit negotiations, the IL&FS crisis, the RBI governor's shocking resignation, the PNB Scam, Facebook under fire – there really was no dearth of news. And to top it all, Tamil Superstar Rajinikanth entered politics – how much more exciting can things get?

It was a good year for economic growth – world GDP grew almost 4% in 2017, a pace that it is likely to have maintained in 2018. Most of the bad news was surrounding volatile US-China trade relations, which also sparked turbulence in global markets. In the developing trade war between the two giants, both sides have suffered heavy losses. However, pundits suspect that China's would be bigger and deeper and that it will blink first – it has already run out of goods to tax and the Shanghai Composite Index was the worst performing major stock market of 2018. Fears of China's economy slowing down and the spectre of its US$ 3tn debt loom large. Its central bank has already embarked on an expansionary policy to stave off a major downturn. While India's manufacturing sector will benefit to an extent due to China's slowdown, slackening global trade will prove detrimental for India's already poor balance of trade and current account deficit situation.

The year saw its share of political upheavals for India. Towards the end, the ruling BJP lost key states of Madhya Pradesh, Chhattisgarh, and Rajasthan leaving political commentators scrambling to make sense of the implications for the General Elections 2019 – likely to be the biggest event for India this year. They believe that the Indian voters understand the difference between state and central issues and could vote differently for national elections – so the outcome is anybody's guess.

Some Indian parties are trying to forge a 'Mahagathbandhan (mega alliance)' and idea initially propagated by West Bengal's Mamata Banerjee and Telangana's K. Chandrashekhar Rao. However, experts point out that India's political theatre is complicated and the sustainability of any coalition is arduous. There are regional successors of legacies – such as Odisha's Naveen Patnaik (heir to the legacy of his father Biju Patnaik), UP's Akhilesh Yadav (of Mulayam Singh Yadav), J&K's Omar Abdullah (of Farrokh Abdulla) or Mehbooba Mufti (of Mufti Mehmood Sayeed), Bihar's Tejaswi Prasad (of Laloo Prasad Yadav), Punjab's Sukhbir Badal (of Prakash Singh Badal), Maharashtra's Uddhav Thackeray (of Balasaheb Thackeray), M K Stalin (of M Karunanidhi), and Karnataka's H D Kumaraswami (of HD Devegowda). Then there are the single-leader parties with no clear successors or second rungs – such as Sharad Pawar, Mayawati, Mamata Bannerjee, K Chandrashekhar Rao, Chandrababu Naidu, and Nitish Kumar. Political experts say that it is difficult to imagine voters accepting parties with very different agendas coming together to form a credible national front.

From a global political perspective, Trump dominated the conversation. Tough trade talks, a love-hate relationship with Russia or insistence on the border wall that eventually led to the longest shutdown of the US – the President of the United States was never not in the news. The sustainability of Trump's Presidency will be closely watched in 2019. With the Democrats controlling the House from January, more investigations into Trump are possible.

Another key event that will be keenly watched is the impact of Brexit on Britain's economy and its impact on the European Union. It is feared that a successful exit could intensify talks of leaving by countries such as Hungary and Denmark. Many important elections will also take place this year – in Israel, Indonesia, Philippines, Portugal, Afghanistan, the European Parliament, the Canadian federal election, and of course, Lok Sabha polls in India. The US Fed is likely to keep hiking rates through the year – it has said it will hike rates at least twice, the street predicts more. Observers believe Europe looks poised for a turbulent year with a further dip in growth, Brexit impact, and a possible hike in the ECB's rate late in the year. Japan is likely to hike its VAT rate in October 2019, which could affect the country's economy.

Pic: CDC Global

The US-China Trade War

US-China trade relations deteriorated dramatically in 2018. Below the fault lines between the two economic giants are IP violations. In August 2017, the US had opened a formal investigation into China's attacks on intellectual property, which it claimed led to US$ 225-600bn in losses for America. Another bone of contention is that China has instituted numerous non-tariff barriers, which insulated some of its sectors from international competition. The EU Chamber of Commerce had also complained that European companies wanting access to the Chinese market often had to agree to transfer vital technology. Interestingly, while all this was happening, the Chinese government actually granted 18 trademarks to companies linked to US President Donald Trump and his daughter.

So far, both countries have suffered enormous losses due to the tariff wars. However, China's stock market and economy have taken more knocks. China's central bank cut its reserve ratio five times in 2018 in an attempt to free up money for new lending – to reduce the risk of a sharp economic slowdown. If China's economy slows down significantly, the entire world is expected to feel aftershocks.

Here is how the US-China tariff war played out in 2018

January: US imposed 30% import tariff on foreign solar panels and 20% on washing machines. China is the world leader in solar panels and in 2016 it had exported US$ 425mn worth of washers to the US.

March: US imposed 25% tariff on imported steel and 10% on aluminium – this also affected Canada and South Korea. China retaliated by imposing tariffs on 128 products from America.

May: Trade talks between the two nations seemed to go well. However…

…by June: US imposed 25% tariff on US$ 50bn worth of Chinese exports. China said US has launched a trade war and it would respond in kind. China's stock market was spooked.

August: US put 25% tariffs on 279 Chinese goods worth US$ 16bn. China retaliated.

September: US levied tariff on US$ 200bn worth of Chinese goods. By then, China had either imposed or proposed tariffs on US$ 110bn of US goods, representing most of its imports of American products.

October: US withdraws from Universal Postal Union – seeks same rates for all countries.

November: Trump signs a revised US-Mexico-Canada Agreement. The USMCA contains an article that aims to prevent any non-market economy, especially China, from taking advantage of the agreement.

December: Planned increases in tariffs are postponed. Negotiations begin. Huawei's Chief Financial Officer Meng Wanzhou, daughter of Huawei's founder Ren Zhengfei, arrested in Canada at the behest of US authorities.

2018 IN TRUMP

The government shuts down, twice

Once in January 2018 and the second time from 22 December 2018 – the longest shutdown in US history. The Senate and House were in stalemate over the border wall issue.

International affairs – on fire!

While the year started off with Trump and Kim Jong-un trading barbs, it ended on a much better note with visits, talks, and promises of a better understanding in the future. Also early in the year, Donald Trump criticized Pakistan saying it has given the US "nothing but lies and deceit" and suspended about US$ 2bn in 'security aid' to Pakistan for failing to clamp down on the Afghan Taliban and the Haqqani Network terror groups. He cut more than US$ 200mn in aid to Palestine and ended funding for Palestinian refugees.

Mid-year, the US engaged in joint military strikes with France and the United Kingdom against Syria and withdrew from the Obama-era Iran nuclear deal and reinstated sanctions on the country. The most shocking announcement was towards the end of the year – Trump said US troops would withdraw from Syria within 30 days, sparking fears that the US would play into the hands of Russia and Iran. Defense Secretary Jim Mattis criticized this move and resigned in protest. The withdrawal deadline was subsequently extended four months, but latest media reports say that there isn't really a timeline for withdrawal. The White House also said that the US isn't withdrawing from Afghanistan (as widely reported by the media earlier).

While Trump's Davos visit went relatively well (he was the first US president to attend after Bill Clinton), his Helsinki summit with Russia was widely panned. He drew bipartisan censure when he criticised his own country and the Mueller investigation for the freeze in relations between

Russia and the United States, and refused to recognize the Russian government's interference in the 2016 US elections. He then retracted his statement about Russia saying he misspoke. Trump also drew widespread criticism when he tried to dilute the CIA assessment that Saudi Crown Prince Mohammed bin Salman ordered the killing of Washington Post columnist Jamal Khashoggi.

The Mexico-US border continued to be the centre of a political tornado. Trump signed a proclamation directing the deployment of the National Guard to the US-Mexico border in anticipation of a breach of the border and was accused of overreacting to a perceived threat. However, migrants did attempt to storm the border and were tear-gassed by US forces.

Special counsel Robert Mueller's year was as busy as Trump's

There was never any let up in Mueller's investigation of Russian interference in the 2016 election. Subpoenas flew, indictments rolled out, and guilty pleas were aplenty.

The Michael Cohen controversy

Trump's former lawyer, Michael Cohen, eventually claimed that Trump had contemporaneous knowledge of the June 2016 Trump Tower meeting between campaign officials (including Trump's son, Don Jr., and son-in-law, Jared Kushner) and Russian lobbyists.

Mid-term elections

Democrats made significant gains in the House of Representatives and in state elections, while Republicans strengthened their slim hold on the Senate, which will allow Trump to push his decisions through. The Democrats' gains give the party the ability to control committees to investigate President Trump and his administration beginning January 2019.

North Korea turns friendly: Will wonders never cease!

Not only did Trump and Kim meet in Singapore in June 2018, the year proved historic even for North Korea-South Korea relations, when interactions warmed considerably during the winter Olympics and seemed to improve steadily from there. However, by December, tensions with the US increased, when North Korea said it would not denuclearize until the US reduced its nuclear-capable 28,500 US troops in South Korea.

Busy year for the Supreme Court of India too

The Supreme Court collegium picked Indu Malhotra as the first woman advocate to be recommended for appointment as an SC judge. In the same month, the SC was thrown into its biggest-ever crisis when its four senior-most judges publicly accused Chief Justice Dipak Misra about arbitrarily assigning important cases to benches headed by junior SC judges, ignoring senior ones.

In September 2018, the SC unanimously ruled that Section 377 is unconstitutional, much to the joy of India's LGBT community – homosexuality is no longer a crime in India. The SC also struck down a law criminalizing adultery as unconstitutional, stating that such a law treated women as the property of their husbands. The court gave a landmark judgment to ease land acquisition – it said purchases by a government agency cannot be quashed because of delay on the part of landowners to accept compensation. It also legalised passive euthanasia and approved the 'living will' to provide terminally ill patients or those in a persistent and incurable vegetative state a right to choose a dignified way to die.

The Supreme Court also issued a directive excluding the 'creamy layer' from SC/ST reservations and upheld the validity of the Aadhaar Act. In another important ruling, it allowed all pilgrims regardless of gender entrance to the Sabarimala, sparking widespread strikes and protests, especially in Kerala.

The Aadhaar breach case

Kerala-based lawyer, Shamnad Basheer, alleged that there were several breaches of the Aadhaar system leading to leakage of personal information of individuals since January this year. He contended that UIDAI and the Centre are liable to compensate people whose data was compromised. His plea urges the court to direct the Centre to either allow people to opt out of the system or delete the entire existing UIDAI data in view of alleged security breaches. In January 2018, UIDAI's lodging of an FIR against a 'The Tribune' newspaper journalist for publishing a story about the breach drew strong reactions from journalists' bodies.

The PNB Scam

The PNB scam came to light in early 2018 when fraudulent LoUs worth Rs 143.6bn (US$ 2.1bn) were issued from its Brady House branch in Fort, Mumbai. The bank initially said that two of its employees at the branch were involved in the scam; as the bank's core banking system was bypassed when the corrupt employees issued letters of undertaking (LoUs) to overseas branches of other Indian banks, including Allahabad Bank, Axis Bank, and Union Bank of India, using the international financial communication system, SWIFT. The fraud was allegedly organized by jeweller and designer Nirav Modi. Those said to be involved include Modi's wife Ami Modi, brother Nishal Modi, and uncle

Mehul Choksi (all partners of the firms, Diamond R US, Solar Exports, and Stellar Diamonds), along with PNB officials and employees. Nirav Modi and his family absconded in early 2018, days before the news of the scam broke in India – he is currently in the UK. Modi is on the Interpol's wanted list.

The fraudulent transactions came to light when they were 'noticed' by a new employee of the bank. The bank complained to the CBI, which named key officials Usha Ananthasubramanian, former CEO of PNB, executive directors KV Brahmaji Rao and Sanjiv Sharan in a charge-sheet holding them responsible for failure to implement several circulars and caution notices issued by the RBI regarding the reconciliation of SWIFT messages and core banking systems.

IL&FS crisis

India's leading infrastructure finance company IL&FS defaulted on payments to lenders triggering panic in the markets. The crisis came to light in September 2018 when IL&FS Financial Services, a group company, defaulted payment obligations. Shortly, it began to receive notices for delays and defaults. Subsequently, rating agency ICRA downgraded it. The IL&FS group has at least 24 direct subsidiaries, 135 indirect subsidiaries, six joint ventures and four associate companies. Its debt is about Rs 910bn of which nearly Rs 600bn is at the project level. Its debt-to-equity ratio is 18.7. A large chunk of its troubles came about due to issues in land acquisition, which made many of its projects unviable while cost escalation led to many incomplete projects.

Patel's exit

The level of reserves to be maintained was one of the major flashpoints in a bitter battle between the RBI and the government. The central government believes that the RBI is more than adequately capitalised and should pass on the surplus. RBI's reserves as a percentage of assets stand at around 25% against the global average of about 16%. It all came to a boil when the finance ministry initiated discussions under the Section 7 of the RBI Act, which empowers the government to issue directions to the RBI Governor periodically; however, Section 7 had never before been invoked. By November, tensions between the government and RBI governor Urjit Patel seemed to have eased with the central bank appearing to climb down on several issues pushed by New Delhi, such as loan restructuring for small businesses, easier norms for weak banks, and pumping of more cash into the system. The government totted up gains in terms of having a say in defining what should be the appropriate level of reserves and an understanding that could result in banks potentially lending an additional Rs 4 lakh crore ahead of the 2019 LS polls. However, in a completely unexpected move, RBI Governor Urjit Patel resigned in December citing personal reasons. Shaktikanta Das took over.

Brexit

Negotiations with EU officially started in June 2017, aiming to complete the withdrawal agreement by October 2018. In July 2018, the British Cabinet agreed to the Chequers plan, an outline of proposals by the UK Government. In November 2018, the Draft Withdrawal Agreement and Outline Political Declaration, agreed between the UK Government and the EU, was published.

The size of the "divorce bill", UK's inheritance of existing EU trade agreements, and relations with Ireland and other EU member states remains uncertain. The precise impact depends on whether the landing will be hard or soft. A Treasury publication of November 2018 on the potential impact of the Chequers Proposal estimated that it would leave the UK economy "3.9% worse off after 15 years compared with staying in the EU". As of November 2018, the Withdrawal Agreement stated that UK's financial contribution (outstanding commitments towards what it approved while still a member of the EU) would be £ 39bn. Brexit is fixed for 29 March 2019, 11.00 p.m.

Since the referendum, absolute employment in the UK has continuously risen to previously unrecorded levels, and by early 2018, relative unemployment reached its lowest level (4.2%) recorded since 1975. Immigration into the UK has only slightly decreased. However, while EU immigration decreased, non-EU immigration increased. On 10 December 2018, Theresa May chose to postpone the vote on her Brexit deal in Parliament.

There is overwhelming or near-unanimous agreement among economists that leaving the European

Union will adversely affect the British economy in the medium and long term. A September 2018 analysis by the think tank Centre for European Reform showed that losses due to Brexit amounted to 2.5% of UK's GDP. A 2018 analysis by economists at Stanford University and Nottingham University estimated that uncertainty around Brexit reduced business investment by c.6 percentage points and reduced employment by c.1.5 percentage points.

India's defence achievements in 2018

In November, India's long-awaited nuclear triad, or the capability to fire nuclear weapons from land, air and sea, is now finally operational almost five decades after it was first conceived for credible strategic deterrence and 20 years after the Pokhran-II tests. The Indian Army also inducted its first advanced 155mm howitzers after three decades! The Bofors scam had hindered all its artillery modernisation plans.

India's proposed acquisitions of the French-built Rafale fighter jets and the Russian S-400 Triumf air defence systems are likely to give the country's defence systems an edge. In October, India signed a $5.4 billion deal for five S-400 Triumf surface-to-air missiles from Russia. This missile can track and destroy combat aircraft, even stealth aircraft at unprecedented ranges. This deal would have automatically attracted crippling sanctions under the Countering America's Adversaries through Sanctions Act, but the Trump administration made an exception for India, which shows the strategic value that the US attaches to its relation with India.
In 2018, the Indian Army eliminated nine out of 12 top terrorist commanders in Kashmir. According to government data, the Army killed almost 250 terrorists in 12 months.

Impact of long-term capital tax

The 2018 budget saw the reintroduction of tax on capital gains from stocks and equity mutual funds that were held for more than a year (against none earlier). The LTCG tax was fixed at 10%. Equity-oriented mutual fund investors have to pay LTCG tax, but ULIP holders don't. The stock market reacted badly to this news and the Sensex went from above 34,400 on 26th February 2018 to below 32,600 on 26th March.

Crude oil movement in 2018

Crude oil played havoc in 2018, going from about US$ 55 per barrel at the beginning of the year all the way up to US$ 76 per barrel in October. From there it kept falling, touching a low of about US$ 43 late December. Crude prices saw unprecedented volatility in 2018. Experts point to changing dynamics – there is oversupply. The US, backed by its Shale Revolution, is now the largest producer of crude surpassing even Saudi Arabia and Russia. Additionally, OPEC is not really able to play market stabiliser; not all its members appear to adhere to the agreed production cuts. The US-China trade war and a strengthening dollar based on Fed rate hikes should add to crude price volatility in 2019.

THE YEAR THAT WAS….

January

INDIA: • Tamil Superstar Rajinikanth enters politics • Telangana becomes the first Indian state to provide 24/7 free power to farmers • PM Modi personally receives Israeli counterpart Benjamin Netanyahu and wife at Palam airbase in Delhi

• Haj pilgrims subsidy ends • Five-year jail term for Laloo Prasad Yadav for the Fodder Scam • Central Statistics Office estimates GDP growth at 6.5% for FY18 • Government lowers additional borrowing requirement for FY18 to Rs 200bn from Rs 500bn. Market reacts positively. Bank credit grows highest in two years • Jio's Q3 profit comes in at Rs 5bn • Maruti plans to shift manufacturing of Swift to Gujarat from Haryana • Sensex crosses 36,000 • Centre allows overseas airlines to own up to 49% of Air India • India's government details its Rs 880bn bank recapitalisation plan • SEBI bars Price Waterhouse from auditing any Indian-listed company for two years (Satyam Computer scam)

INTERNATIONAL: • Trump completes one year as US President; US government shuts down • China's GDP accelerates for the 1st time in seven years in Q4CY17 • US slaps 'America First' tariffs on washing machines, solar panels • Taliban strikes Kabul; blast toll crosses 100 • IKEA founder Ingvar Kamprad passes away • VAT introduced in Saudi Arabia and the United Arab Emirates for the first time

February

INDIA: • Weeks after Israeli leader Netanyahu's visit, PM Modi says India in favour of an independent Palestine • The government passes a pro poor, pro farmer budget, health scheme that covers 40% of the population, long-term capital gains tax comes back, cess up by 1% • SC cancels 88 Goa mining leases, says govt flouted laws to help private firms • RBI keeps key interest rates on hold, hikes inflation outlook, trims growth forecasts • SBI reports first quarterly loss in nearly two decades • PNB scam comes to light. New RBI norms require lenders to classify a loan as non-performing immediately upon restructuring. Bad loans soar • Ambuja, ACC call off merger after 10 months.

INTERNATIONAL: • Maldives crisis begins. Country sends out pleas to India for help • SpaceX's Tesla

Roadster, launched on a Falcon Heavy rocket, cruises above Earth • Xerox combines operations with Fujifilm Holdings of Japan • In shocking judgement, Samsung Group heir Jay Y Lee is freed • Uber agrees to pay US$ 245mn to Google's Waymo to settle theft lawsuit • H1B visas get tougher • China's parliament scraps two-term limit. Xi Jinping to continue in power indefinitely.

March

INDIA:

• No automatic arrest under SC/ ST (Atrocities) Act, says SC, allows bail. Violent protests erupt • AMFI says fifth consecutive financial year of outflow from gold ETFs • Aircel declares bankruptcy • Dish TV India, Videocon DTH merger complete • Government offers to sell 76% stake in Air India to private bidders • TDP quits Modi cabinet • BJP wins two-thirds majority in Tripura • CBI arrests Karti Chidambaram for allegedly taking a bribe when his father was FM.

INTERNATIONAL: • Whistle-blowers reveal that personal information from

over 87mn Facebook users was sold to Cambridge Analytica • Vladimir Putin wins fourth term as Russia's president • US, Europe expel nearly 150 Russian diplomats; Russia expels 59 from 23 countries. US imposes new sanctions on Russia • President Trump fires secretary of state Rex Tillerson • Reports say China sold Pakistan a powerful tracking system that can speed up development of multi-warhead missiles • Top physicist Stephen Hawking passes away.

April

INDIA: • India claims bodies of 38 workers abducted in Mosul by ISIL in 2016 • Capital punishment for men who rape children under the age of 12 • Government says electricity has reached all villages; next step – all households • Saudi Aramco says will buy 50% stake in US$ 44bn refinery planned in Maharashtra by a consortium of Indian government oil companies

• Axis Bank chief Shikha Sharma's tenure to end 2.5 years ahead of schedule • RBI bars banks from crypto services • India's tax department says 10mn new tax filers added in 2017-18.

INTERNATIONAL: • First time a North Korean leader sets foot in South Korea • First-ever India-China "informal" summit • TCS marketcap touches US$ 100bn. Overtakes Accenture's marketcap • Chemical attack in Syria kills several. Soon after, joint strike by US, UK, France pound Syria with 100 missiles.

May

INDIA: • Walmart acquires a 77% controlling stake in Flipkart for US$ 16bn

• SEBI serves notice to ICICI's Chanda Kochhar on NuPower • Sterlite shuts TN unit permanently • Nipah virus outbreak begins • UltraTech buys Century's cement business • India's CAG says root cause of banking sector crisis in India is the bond market because RBI acts as a regulator as well as a trader

• Karnataka election: BJP's B S Yeddyurappa resigns. JD Kumaraswamy becomes chief minister backed by Congress-JD(S) alliance

INTERNATIONAL: America imposes tough trade measures on China • US withdraws from the Iran nuclear deal • China's Air Force lands bombers on disputed islands and reefs in the South China Sea • Trump administration sounds alarm about possible sonic attacks against its citizens that could cause brain injury • Zuckerberg apologises to EU lawmakers, says FB didn't do enough to prevent data breach

June

INDIA: • The RBI issues warnings about 11 public sector banks • Swiggy joins the Unicorn Club • In Jammu & Kashmir, the PDP-BJP coalition collapses • ICICI's Chanda Kochhar goes on leave till conflict-of-interest enquiry is complete • India successfully tests Agni-V ICBM missile at base near Odisha • Plastics ban begins in Maharashtra, including Mumbai • To counter US tariffs, India ups duties on US bikes, almonds, apples • FY18 current account up 42% to US$ 160bn • 25-basis-point hike in India's policy rate to 6.25%; first hike in Modi's term • India's SC allows Centre to implement long-stalled reservation in promotion policy.

INTERNATIONAL: • US Supreme Court upholds Trump's travel ban • Turkey's Recep Tayyip Erdogan wins presidential and parliamentary elections • Giuseppe Conte is sworn in as new Prime Minister of Italy • The new Catalan regional government takes office in Barcelona

•

Saudi women begin to drive • Audi CEO Rupert Stadler arrested as part of a probe into emissions test cheating • Trump-Kim meet • South China Sea: US' Mattis criticizes China for maritime 'intimidation'

July

INDIA: • Floods and landslides in Kerala bring the state to a standstill. Almost 500 people die over July-August and property damage is estimated at US$ 5.6bn • 4mn people declared illegal in Assam, not eligible for National Register of Citizens • Hindalco to acquire Aleris at an EV of US$ 2.58bn • Government says the RBI does not need more powers • Flipkart shuts down eBay India • Government cuts GST on 100 mass-use items • CBI charges Congress leader P Chidambaram, son Karti among others for alleged bribery in the controversial Aircel-Maxis deal • LIC board okays 51% stake buy in IDBI Bank • Unnao rape case: CBI files charge-sheet against BJP MLA • Minimum support price of 14 summer crops for 2018-19 season hiked.

INTERNATIONAL: • EU fines Google US$ 5.1bn over Android antitrust violations

• France wins football world cup; last win was in 1998 • New US rules allows deportation if H-1B extension is rejected • Former Pakistan PM Nawaz Sharif arrested – to serve 10-year jail sentence for graft • Trump in the UK amid protests • Thai cave boys: 18 day ordeal ends. All 12 boys and their football coach rescued • Facing severe backlash, Angela Merkel agrees to build border camps for asylum seekers and to tighten border with Austria.

August

INDIA: • India's overall monsoon death toll comes to almost 1,000 with 7.5mn families affected in 5 states • RIL becomes the first Indian company to hit Rs 8tn market cap • RBI says Uday Kotak has to dilute equity in Kotak Mahindra Bank to 20% by year end

• Former India PM Atal Bihari Vajpayee passes away • Private equity giant KKR & Co acquires 60% stake in Ramky Enviro for US$ 530mn • Neeraj Singhal, former promoter and MD of Bhushan Steel, arrested • Maratha quota agitation turns violent • IMF says India to drive global growth for 30 years; predicts 7.3% growth for FY19 • M Karunanidi passes away. RBI raises repo rate by 25bps to 6.5%.

INTERNATIONAL: • Australia's PM Turnbull ousted. New PM Scott Morrison • Imran Khan new Pakistan PM • Taliban overruns a base in northern Afghanistan, killing 17 soldiers • UN panel says China holding 2mn Uighurs and Muslim minorities in secret camps.

September

INDIA: • The IL&FS crisis comes to light • Retail petrol prices reach a record high in Mumbai • 'Comcasa' at India-US '2 plus 2' dialogue – the defence pact allows India to access encrypted technologies for the first time • SC decriminalises homosexuality • Indian mutual funds assets cross Rs 25-lakh crore • UK national Christian Michel James, a key accused in the VVIP chopper scam, to be extradited to India • Sebi drastically reduces charges that investors pay to mutual fund houses to manage their money

INTERNATIONAL: • Coke buys UK coffee brand Costa for US$ 5bn • Pentagon scraps US$ 300mn aid to Pakistan • Feared militant Jalaluddin Haqqani dies • China allows Nepal the use of four of its ports • Setback for China in Maldives. President Abdulla Yameen suffers defeat • Oyo joins Unicorn Club • BNP sells entire 33% Geojit stake.

October

INDIA: • Statue of Unity in Gujarat depicting Sardar Vallabhbhai Patel becomes the world's tallest statue • 150,000 vials tainted

with type 2 polio virus, putting at risk India's 'polio-free' status • Rs 220bn Dharavi Redevelopment Project revived • In the wake of sexual harassment allegations, Jr. external-affairs minister M J Akbar resigns • Study says India has 340,000 USD millionaires with US$ 6tn total wealth • TCS offers double pay for fresh hires with new-age digital skills. Cognizant Technology Solutions lets go of about 200 senior employees as part of its plan to align its talent pool to newer digital requirements • Government sends CBI's director Alok Verma and special director Rakesh Asthana on leave.

INTERNATIONAL: • Putin arrives in India • Indonesia quake and tsunami toll rises to more than 800 • Meng Hongwei, Chinese Interpol President, disappears during a visit to China

• Journalist Jamal Khashoggi disappears • Nikki Haley cites burnout, quits Trump cabinet • Google+ data leak • Facebook confirms hackers stole names and contacts of 29mn users • Mail-bombs delivered to various top Republicans and Democrats in the US • Indonesian Lion Air aircraft with 189 people on board crashes into the Java Sea • Jair Bolsonaro wins Brazil's presidential election • Trump dispatches 5,200 troops to Mexico border • Yuan hits decade low amid US trade dispute.

November

INDIA: • US temporarily allows India to buy Iranian oil • J&K governor dissolves assembly •I-T department serves notices to Flipkart promoters on the Walmart deal. Binny Bansal quits abruptly • India set to beat Brazil in sugar output after 15 years in 2018-19 • Maharashtra approves 16% maratha quota • Online fashion retailer Jabong to merge its operations with Myntra • Amazon loses close to US$ 1bn in FY18. India's top three e-commerce companies lose Rs 113bn.

INTERNATIONAL: • After eight years of being in the opposition section, the Democratic Party recaptures the House of Representatives. Republicans expand their Senate majority • A 27-year-old American Christian missionary is killed by indigenous Sentinelese people upon landing on North Sentinel Island • Migrants from Central America storm the US border from Mexico • International police body Interpol elected Kim Jong-yang of South Korea as president. Russian candidate loses race • CIA implicates Mohammed Bin Salman - Saudi crown prince in Khashoggi killing.

December

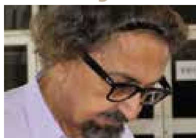
INDIA: • DoT rejects RCom-Jio spectrum trading deal

• State Elections: Congress sweeps Chattisgarh; forms government in Rajasthan and MP too. TRS wins in Telangana, MNF in Mizoram • National Pension withdrawal at the time of retirement becomes tax-free • Education technology platform Byju Raises US$ 400mn; valued at US$ 3.6bn • RBI Governor Urjit Patel resigns, citing personal reasons. Shaktikanta Das takes over • Centre's notification allows data interception; 10 agencies can snoop on phones and computers in India • HUL found not passing on lower GST benefits to the tune of Rs 3.83bn

• Supreme Court gives a clean chit to the Narendra Modi government for its decision to procure 36 fully loaded Rafale fighter jets from French company Dassault Aviation• Government tightens guidelines for FDI in e-commerce; bars players from selling exclusive-only products.

INTERNATIONAL: • A US federal judge rules Obamacare 'invalid'• Tsunami strikes Indonesia without warning; death toll above 350 • India's government says it will merge 12% / 18% GST rates; remove 28% slab • Japan says it will resume commercial whaling • Russia's announces new strategic weapon that flies 27 times faster than the speed of sound.

I N D I A : T H O S E W E L O S T …

January **Kapil Mohan,** 88, Indian beverage and food executive (Old Monk, Mohan Meakin), cardiac arrest February **Sridevi,** 54, Indian actress (English Vinglish), accidental drowning. March **Patangrao Kadam,** 74, Indian politician, kidney disease May **Himanshu Roy,** 54, Indian police officer, Director General of Police for Maharashtra, suicide by gunshot. July **Rita Bhaduri,** 62, Indian actress August **M. Karunanidhi,** 94, Indian politician and writer, Chief Minister of Tamil Nadu (1969–1971, 1971–1976, 1989–1991, 1996–2001, 2006–2011), multiple organ failure **Anant Bajaj,** 41, Indian businessman (Bajaj Electricals), heart attack. **Ajit Wadekar,** 77, Indian cricketer (Bombay, national team), cancer **Atal Bihari Vajpayee,** 93, Indian politician, Prime Minister (1996, 1998–2004), Minister of External Affairs (1977–1979), multiple organ failure September **Kalpana Lajmi,** 64, Indian filmmaker (Rudaali), kidney and liver failure. November **Alyque Padamsee,**  87, Indian actor (Gandhi) and adman December **Nana Chudasama,** 86, Indian jurist and public servant. **Mrinal Sen,** 95, Indian film director (Bhuvan Shome, Mrigayaa, Khandhar), heart attack **Kader Khan,** 81, Afghan-born Indian-Canadian actor (Daag, Family: Ties of Blood, Tevar) and screenwriter

Indian Economy – Trend Indicators

Monthly Economic Indicators

Growth Rates (%)	Nov-17	Dec-17	Jan-18	Feb-18	Mar-18	Apr-18	May-18	Jun-18	Jul-18	Aug-18	Sep-18	Oct-18	Nov-18	Dec-18
IIP	8.5	7.1	7.4	7.1	4.6	4.8	3.8	7.0	6.5	4.7	4.5	8.4	0.5	
PMI	52.6	54.7	52.4	52.1	51.0	51.6	51.2	53.1	52.3	51.7	52.2	53.1	54.0	53.2
Core sector	6.9	3.8	6.1	5.4	4.5	4.6	4.1	7.8	7.3	4.7	4.3	4.8	3.5	
WPI	3.9	3.6	3.0	2.7	2.7	3.6	4.8	5.7	5.3	4.6	5.2	5.5	4.6	3.8
CPI	4.9	5.2	5.1	4.4	4.3	4.6	4.9	5.0	4.2	3.7	3.8	3.3	2.3	2.2
Money Supply	7.3	10.2	10.8	10.5	9.9	10.6	10.4	10.1	10.2	10.0	10.0	10.0	10.3	10.4
Deposit	5.4	3.2	4.3	5.3	6.1	8.1	7.5	7.4	7.7	8.0	7.8	8.4	8.8	8.8
Credit	8.7	9.8	10.4	10.4	10.5	12.1	12.4	12.4	12.2	12.7	12.6	14.0	14.6	14.7
Exports	30.9	12.4	9.1	4.5	-0.4	5.2	20.2	17.6	14.3	16.9	-2.2	17.9	0.8	0.4
Imports	21.2	21.1	26.1	10.4	7.9	4.6	14.9	21.3	28.8	25.4	10.5	17.6	4.3	-2.4
Trade deficit (USD Bn)	6.3	41.1	64.6	25.8	31.2	3.6	5.6	28.1	57.4	49.4	48.9	22.2	10.4	-12.1
Net FDI (USD Bn)	-1.3	4.3	1.9	4.0	1.8	4.8	3.8	1.8	1.9	2.0	3.9	3.7	0.9	
FII (USD Bn)	2.7	-0.4	3.5	-2.4	1.2	-3.0	-1.7	-4.2	4.6	-4.9	-2.1	-5.1	1.8	
ECB (USD Bn)	3.0	1.3	0.5	3.1	5.1	3.9	1.3	2.7	2.2	4.8	1.7	1.4	2.1	
Dollar-Rupee	64.5	63.9	63.6	64.4	65.0	65.7	67.6	67.8	68.7	69.6	72.3	73.6	71.8	70.7
FOREX Reserves (USD Bn)	400.7	409.4	417.8	420.6	424.4	420.4	412.8	406.1	404.2	400.1	400.5	392.1	393.7	393.4
NRI Deposits (USD Bn)	120.9	123.3	124.4	124.3	126.2	124.6	123.5	124.3	124.9	123.0	121.9	121.5	125.7	

Quarterly Economic Indicators

Balance of Payment (USD Bn)	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19
Exports	67.4	68.8	77.4	73.1	76.1	77.5	82.2	83.4	83.4
Imports	93.1	102.0	107.1	115.1	108.5	121.6	123.8	129.1	133.4
Trade deficit	-25.6	-33.3	-29.7	-41.9	-32.5	-44.0	-41.6	-45.8	-50.0
Net Invisibles	22.2	25.3	26.3	27.0	25.5	30.3	28.6	29.8	30.9
CAD	-3.4	-8.0	-3.5	-15.0	-7.0	-13.7	-13.1	-15.9	-19.1
CAD (% of GDP)	0.6	1.4	0.6	2.5	1.1	2.0	1.9	2.4	2.9
Capital Account	12.8	6.1	10.4	26.9	16.9	22.5	25.0	5.4	16.3
BoP	8.5	-1.2	7.3	11.4	9.5	9.4	13.2	-11.3	-1.9

GDP and its Components (YoY, %)	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19
Agriculture & allied activities	4.1	6.9	5.2	2.3	2.7	4.1	4.5	5.3	3.8
Industry	6.5	7.2	5.5	1.5	7.0	6.8	8.0	10.8	6.5
Mining & Quarrying	-1.3	1.9	6.4	-0.7	7.1	-0.1	2.7	0.1	-2.4
Manufacturing	7.7	8.2	5.3	1.2	6.9	8.1	9.1	13.5	7.4
Electricity, Gas & Water Supply	5.1	7.4	6.1	7.0	7.7	6.1	7.7	7.3	9.2
Services	7.4	6.4	5.7	7.8	6.6	7.6	8.2	7.5	7.5
Construction	4.3	3.4	-3.7	2.0	2.8	6.8	11.5	8.7	7.8
Trade, Hotel, Transport and Communications	7.7	8.3	6.5	11.1	9.3	9.0	6.8	6.7	6.8
Finance, Insurance, Real Estate & Business Services	7.0	3.3	2.2	6.4	6.4	6.7	5.0	6.5	6.3
Community, Social & Personal Services	9.5	10.3	17.0	9.5	5.6	7.2	13.3	9.9	10.9
GDP at FC	6.8	6.7	5.6	5.6	6.2	6.7	7.6	8.0	6.9

Annual Economic Indicators and Forecasts

Indicators	Units	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19E
Real GDP/GVA growth	%	8.6	8.9	6.7	6	5.6	7.1	7.9	6.6	6.5-6.7	7-7.5
Agriculture	%	0.8	8.6	5	1.5	4.2	-0.2	0.7	4.9	2	3
Industry	%	10.2	8.3	6.7	5	4.5	6.5	10.2	7	4.9	5.8
Services	%	10	9.2	7.1	6.1	8.2	9.4	9.1	6.9	8.6	8.8
Real GDP	₹ Bn	45161	49185	52475	85992	90844	97190	104905	111854	119349	127942
Real GDP	US$ Bn	953	1079	1096	1694	1581	1589	1603	1667	1843	1984
Nominal GDP	₹ Bn	64778	77841	87360	99466	112366	124451	136820	151837	167173	186230
Nominal GDP	US$ Bn	1367	1707	1824	1828	1859	2035	2090	2264	2582	2887
WPI (Average)	%	3.8	9.6	8.7	7.4	6	2	-2.5	3.7	3	3.5-4
CPI (Average)		12.4	10.4	8.3	10.2	9.5	6.4	4.9	4.5	3.4	3.7-4.2
Money Supply	%	19.2	16.2	15.8	13.6	13.5	12	10.3	7.3	9.5	10
CRR	%	5.75	6	4.75	4	4	4	4	4	4	4
Repo rate	%	5	6.75	8.5	7.5	8	7.5	6.75	6.25	6	6
Reverse repo rate	%	3.5	5.75	7.5	6.5	7	6.5	5.75	5.75	5.75	5.75
Bank Deposit growth	%	17.2	15.9	13.5	14.2	14.6	12.1	9.7	11.2	8	11
Bank Credit growth	%	16.9	21.5	17	14.1	13.5	12.5	10.7	4.7	9	10
Centre Fiscal Deficit	₹ Bn	4140	3736	5160	5209	5245	5107	5328	5343	5684	5959
Centre Fiscal Deficit	% of GDP	6.4	4.8	5.7	5.2	4.6	4.1	3.9	3.5	3.4	3.2
State Fiscal Deficit	% of GDP	2.9	2.1	1.9	2	2.2	2.6	3.6	3	3.5	3.2
Consolidated Fiscal Deficit	% of GDP	9.3	6.9	7.6	6.9	7.1	6.6	7.5	6.5	6.9	6.4
Exports	US$ Bn	182.4	251.1	309.8	306.6	318.6	316.7	266.4	280.1	299.7	305.7
YoY Growth	%	-3.5	37.6	23.4	-1	3.9	-0.6	-15.9	5.2	7	2
Imports	US$ Bn	300.6	381.1	499.5	502.2	466.2	460.9	396.4	392.6	459.3	470.8
YoY Growth	%	-2.5	26.7	31.1	0.5	-7.2	-1.1	-14	-1	17	2.5
Trade Balance	US$ Bn	-118.2	-129.9	-189.8	-195.6	-147.6	-144.2	-130.1	-112.4	-159.6	-165.1
Net Invisibles	US$ Bn	80	84.6	111.6	107.5	115.2	116.2	107.9	97.1	108.3	116.2
Current Account Deficit	US$ Bn	-38.2	-45.3	-78.2	-88.2	-32.4	-27.9	-22.2	-15.3	-51.2	-48.8
CAD (% of GDP)	%	-2.8	-2.6	-4.2	-4.7	-1.7	-1.4	-1.1	-0.7	-2	1.5-2
Capital Account Balance	US$ Bn	51.6	62	67.8	89.3	48.8	90	41.1	36.5	64.9	82
Dollar-Rupee (Average)		47.4	45.6	47.9	54.4	60.5	61.2	65.5	67	64.8	64.5

Source: RBI, CSO, CGA, Ministry of Agriculture, Ministry of commerce, Bloomberg, PhillipCapital India Research

PhillipCapital India Coverage Universe: **Valuation Summary**

		CMP	Mkt Cap	Net Sales (₹ mn)		EBIDTA (₹ mn)		PAT (₹ mn)		EPS (₹)		EPS Growth (%)		P/E (x)		P/B (x)		EV/EBITDA (x)		ROE (%)		ROCE (%)	
Name of company	Sector	₹	₹ bn	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
Mahindra & Mahindra	Automobiles	726	1,144	539,684	610,549	80,413	94,024	45,489	54,149	38	46	8.6	19.0	19.0	15.9	2.6	2.3	0.0	0.0	13.6	14.5	12.5	13.5
Escorts	Automobiles	736	110	57,294	62,899	7,018	8,161	4,704	5,469	39	46	33.8	16.3	18.7	16.1	2.9	2.5	-0.3	-0.9	15.7	15.5	15.8	15.9
Tata Motors	Automobiles	186	821	3,125,033	3,335,842	351,017	472,026	58,758	119,527	18	37	-19.1	103.4	10.2	5.0	0.9	0.8	2.2	1.8	8.8	15.6	3.1	6.0
Bharat Forge	Automobiles	491	300	99,672	111,613	21,503	25,195	11,758	14,337	25	31	38.4	21.9	19.4	15.9	4.8	4.0	0.9	0.6	24.8	25.2	19.7	21.0
Bajaj Auto	Automobiles	2,710	779	299,639	347,319	51,068	57,707	43,597	49,090	151	170	6.3	12.6	18.0	16.0	3.6	3.1	-0.1	-0.1	20.1	19.7	20.3	20.1
Hero MotoCorp	Automobiles	2,877	651	342,014	392,192	53,107	61,903	36,353	41,266	182	207	-1.0	13.5	15.8	13.9	4.3	3.7	0.1	-0.0	26.9	26.2	26.9	26.6
Apollo Tyres	Automobiles	218	164	174,529	196,239	21,335	26,097	9,175	12,256	16	21	26.7	33.6	13.6	10.2	1.2	1.1	1.7	1.4	8.7	10.5	6.3	7.7
Mahindra CIE	Automobiles	233	96	66,676	71,194	7,709	8,084	3,470	3,774	9	10	-5.0	8.8	25.4	23.3	2.3	2.2	1.3	1.3	9.0	9.5	8.3	9.1
Ceat	Automobiles	1,229	57	71,118	81,223	8,795	10,568	4,590	5,500	113	135	71.7	19.8	10.9	9.1	1.7	1.5	1.9	2.3	15.5	16.1	13.1	11.9
Ramkrishna Forgings	Automobiles	516	22	17,085	20,243	3,691	4,419	1,548	2,001	48	61	63.7	29.2	10.9	8.4	1.9	1.5	1.5	1.3	17.1	18.2	17.2	17.3
Maruti Suzuki	Automobiles	7,307	2,775	871,682	988,167	129,782	155,251	84,225	106,272	279	352	9.1	26.2	26.2	20.8	4.7	4.0	0.0	-0.2	17.9	19.4	17.2	19.2
Ashok Leyland	Automobiles	94	348	277,692	308,982	31,449	36,619	19,075	22,839	7	8	21.1	19.7	14.4	12.0	3.1	2.5	0.3	-0.2	21.4	20.7	22.0	21.5
BHEL	Capital Goods	68	272	316,597	374,180	24,961	35,333	14,321	19,215	4	6	222.1	34.2	16.6	12.4	0.7	0.7	-2.2	-1.2	4.4	5.8	3.8	4.9
Larsen & Toubro	Capital Goods	1,344	1,805	1,381,876	1,583,230	179,137	197,182	86,775	92,608	65	69	24.8	6.5	20.8	19.5	3.4	3.0	6.3	6.1	16.4	15.6	6.9	6.7
VA Tech Wabag	Capital Goods	306	20	30,885	37,316	2,648	3,604	1,212	1,826	22	33	-11.9	50.7	13.8	9.2	1.4	1.2	1.2	0.2	9.9	13.3	6.9	9.4
CG Power & Industrial	Capital Goods	45	39	69,266	82,063	6,131	8,196	1,636	3,031	3	5	231.0	85.3	17.1	9.2	1.1	1.0	2.2	1.6	6.4	11.0	6.3	9.1
GE T&D	Capital Goods	315	72	45,500	44,435	4,091	4,340	2,354	2,685	9	10	-3.3	14.1	34.2	30.0	5.9	5.1	-1.5	-2.1	17.3	17.1	21.6	20.9
Voltas	Capital Goods	534	190	75,214	87,202	7,840	9,490	5,988	7,132	18	22	8.1	19.1	29.5	24.8	4.1	3.6	-0.2	-0.5	13.8	14.6	14.5	15.5
Bharat Electronics	Capital Goods	89	289	118,111	133,929	23,790	27,354	15,461	17,584	6	7	5.1	13.7	14.0	12.3	2.5	2.2	-0.9	-0.7	17.7	18.0	16.0	16.4
Engineers India	Capital Goods	122	86	24,509	32,944	3,917	4,973	3,637	4,396	6	7	6.7	20.9	21.3	17.6	3.3	3.1	-7.8	-6.2	15.6	17.5	18.2	20.8
KEC International	Capital Goods	274	84	117,933	136,874	12,090	13,767	5,355	5,980	21	23	13.3	11.7	13.1	11.8	2.8	2.4	2.4	2.3	21.7	20.1	14.4	12.4
Cummins India	Capital Goods	841	194	56,963	64,109	9,180	10,112	7,867	8,580	28	31	11.0	9.1	29.6	27.2	5.5	5.1	-0.6	-0.7	18.4	18.7	17.3	18.0
Siemens	Capital Goods	1,058	361	126,399	126,099	12,309	12,719	8,391	9,035	24	25	21.7	7.7	44.9	41.7	4.5	3.7	-2.9	-4.5	10.1	8.8	9.8	33.0
ABB India	Capital Goods	1,288	256	108,383	116,357	9,397	10,884	5,460	6,372	26	30	31.7	16.7	50.0	42.8	6.8	6.0	-1.1	-1.4	13.5	14.0	12.8	13.7
Thermax	Capital Goods	1,095	137	54,849	69,746	5,000	6,651	3,316	4,365	28	37	42.8	31.6	39.3	29.9	4.4	4.0	0.2	-0.1	11.2	13.2	10.6	12.5
Cochin Shipyard	Capital Goods	368	322	29,431	27,875	5,776	4,880	4,709	3,864	36	29	20.3	-17.9	10.3	12.5	1.5	1.4	-4.9	-4.3	14.1	10.9	12.8	10.2

PhillipCapital India Coverage Universe: **Valuation Summary**

		CMP	Mkt Cap	Net Sales (₹ mn)		EBIDTA (₹ mn)		PAT (₹ mn)		EPS (₹)		EPS Growth (%)		P/E (x)		P/B (x)		EV/EBITDA (x)		ROE (%)		ROCE (%)	
Name of company	Sector	₹	₹ bn	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
Hindustan Aeronautics	Capital Goods	775	171	182,158	202,808	25,081	27,685	15,225	19,079	46	57	-26.5	25.3	17.0	13.6	2.0	1.9	-5.8	-5.7	12.0	13.9	7.8	9.2
Bharat Dynamics	Capital Goods	292	69	45,178	36,630	7,470	5,824	5,443	4,686	30	26	-7.0	-13.9	9.8	11.4	2.3	2.1	-1.9	-3.4	23.6	18.0	19.6	15.4
India Cement	Cement	88	36	56,402	62,467	6,789	8,661	497	1,805	2	6	-25.2	263.1	54.4	15.0	0.5	0.5	4.7	3.9	1.0	3.5	2.7	4.0
JK Lakshmi Cement	Cement	307	38	37,739	41,810	5,387	7,558	1,062	2,870	9	24	102.3	170.3	34.0	12.6	2.4	2.1	3.7	2.1	7.0	16.5	7.6	11.7
JK Cement	Cement	736	53	48,918	51,024	8,089	8,492	2,691	2,335	38	33	-11.1	-13.2	19.1	22.0	2.4	2.3	3.2	4.4	12.7	10.5	8.3	7.2
Sanghi Cement	Cement	61	24	11,210	13,050	2,507	3,227	483	597	2	2	-25.0	23.4	31.6	25.6	0.9	0.9	5.5	4.6	3.0	3.5	4.8	4.7
Star Cement	Cement	97	48	18,402	20,748	5,098	5,459	3,068	3,220	7	8	16.3	5.0	13.3	12.6	2.3	1.9	1.1	1.2	17.1	15.2	14.9	13.5
Mangalam Cement	Cement	231	7	10,765	11,339	1,027	1,423	222	482	8	18	95.0	117.3	27.8	12.8	1.1	1.0	3.0	1.7	4.0	8.1	5.5	7.8
Dalmia Bharat	Cement	2,438	239	92,979	101,813	23,856	25,127	5,849	6,711	66	75	9.2	14.7	37.2	32.4	3.3	3.0	1.9	2.2	8.9	9.3	7.6	6.5
Ambuja Cement	Cement	217	449	267,822	283,283	42,805	49,261	17,375	20,725	9	10	41.4	19.3	24.8	20.8	2.1	2.0	-1.3	-1.1	8.3	9.4	8.4	9.7
Ultratech Cement	Cement	3,883	1,148	390,413	497,438	73,031	95,461	29,101	43,593	106	151	13.2	42.5	36.6	25.7	3.7	2.9	1.6	1.6	10.1	11.4	7.9	9.5
HeidelbergCement	Cement	152	36	21,394	22,447	3,943	4,302	1,857	2,206	8	10	39.4	18.8	18.5	15.6	2.8	2.4	-0.1	-0.8	15.1	15.2	11.4	11.9
ACC	Cement	1,477	287	147,483	158,128	19,659	24,035	12,118	14,545	64	77	30.8	20.0	22.9	19.1	2.8	2.7	-1.5	-1.1	12.4	14.1	10.6	12.9
Shree Cement	Cement	15,861	606	119,963	147,398	28,024	33,991	13,117	15,581	377	447	-5.2	18.8	42.1	35.5	5.5	4.9	-0.8	-1.0	13.1	13.7	11.6	12.6
ICICI Bank	Banks	375	1,960	256	306	223	262	87	135	14	21	28.1	54.7	27.8	18.0	2.2	2.0	8.8	7.5	8.1	11.7	1.0	1.4
State Bank of India	Banks	303	2,667	865,140	1,008,337	594,257	692,955	69,410	303,369	8	33	-206.0	323.5	39.0	9.2	1.4	1.2	0.0	0.0	3.5	14.0	0.2	0.9
Bank of Baroda	Banks	121	395	182,743	222,890	133,603	169,687	24,663	82,427	8	28	-191.2	234.2	14.5	4.3	0.8	0.6	0.0	0.0	5.6	16.1	0.3	1.0
Punjab National Bank	Banks	84	243	167,584	211,645	96,986	118,933	-11,529	27,533	-3	8	-92.3	-338.8	-24.6	10.3	0.6	0.6	0.0	0.0	-2.9	6.5	-0.2	0.3
Canara Bank	Banks	276	213	138,482	169,710	96,973	117,022	-11,060	-3,069	-12	-3	-38.4	-72.3	-23.4	-84.3	0.7	0.7	0.0	0.0	-3.0	-0.8	-0.2	-0.0
HDFC Limited	Banks	1,975	3,339	133,590	153,879	162,341	163,131	90,437	103,709	62	61	-14.3	-2.6	31.8	32.6	4.6	4.3	0.0	0.0	13.4	13.6	2.2	2.2
AXIS Bank	Banks	662	1,475	215,460	258,215	179,754	213,628	35,226	92,340	13	35	-12.6	160.8	49.3	18.9	2.6	2.3	0.0	0.0	5.4	13.0	0.5	1.2
Indian Bank	Banks	257	175	74,915	89,708	55,390	67,486	12,679	28,311	26	59	0.7	123.3	9.7	4.4	0.7	0.6	0.0	0.0	7.8	15.8	0.5	0.9
HDFC Bank	Banks	2,117	5,526	467,627	567,826	381,497	463,872	209,779	252,696	78	93	15.1	20.5	27.3	22.7	3.9	3.5	0.0	0.0	16.6	16.2	1.9	1.9
Indusind Bank	Banks	1,525	1,210	93,670	117,349	82,604	102,087	45,412	56,456	76	94	25.9	24.3	20.2	16.2	3.3	2.8	0.0	0.0	17.6	18.7	1.9	1.9
DCB Bank	Banks	181	50	11,776	14,972	6,338	8,648	3,034	4,165	10	12	23.7	25.9	18.3	14.6	1.8	1.5	0.0	0.0	10.2	11.5	0.9	1.0
Union Bank	Banks	96	103	108,547	124,228	76,712	88,209	-5,826	12,423	-3	7	-92.8	-313.2	-29.6	13.9	0.6	0.6	0.0	0.0	-2.3	4.5	-0.1	0.2

PhillipCapital India Coverage Universe: **Valuation Summary**

		CMP	Mkt Cap	Net Sales (₹ mn)		EBIDTA (₹ mn)		PAT (₹ mn)		EPS (₹)		EPS Growth (%)		P/E (x)		P/B (x)		EV/EBITDA (x)		ROE (%)		ROCE (%)	
Name of company	Sector	₹	₹ bn	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
Oriental Bank of Com	Banks	98	52	48,359	57,178	40,944	47,279	-2,482	5,452	-3	6	-96.9	-319.6	-34.1	15.5	0.6	0.6	0.0	0.0	-2.1	3.9	-0.1	0.2
Kotak Mahindra Bank	Banks	1,204	2,496	113,145	142,486	88,783	113,721	50,518	66,508	27	35	23.2	31.7	45.4	34.5	5.4	4.7	0.0	0.0	12.7	14.6	1.7	1.9
Britannia	FMCG	3,176	767	110,585	124,596	17,925	21,014	11,532	12,983	96	108	14.8	12.6	33.1	29.4	9.1	7.5	-0.2	-0.5	27.5	25.6	30.3	28.7
Jubilant Foodworks	FMCG	1,216	191	35,708	41,123	6,030	7,672	3,197	4,216	24	32	54.9	31.9	50.1	38.0	12.3	9.7	-0.6	-1.0	24.4	25.4	26.8	28.1
ITC	FMCG	294	3,716	441,878	485,353	173,818	193,139	120,045	133,156	10	11	11.0	10.9	30.0	27.1	6.6	6.2	-0.2	-0.3	22.0	22.8	21.9	22.8
Hindustan Unilever	FMCG	1,773	3,810	339,260	390,450	72,760	85,178	52,990	61,361	25	28	44.9	15.8	72.3	62.4	54.1	47.7	-0.4	-0.5	74.9	76.4	65.5	68.0
Colgate	FMCG	1,326	305	45,971	50,504	12,867	14,239	7,705	8,540	28	31	12.5	10.8	46.8	42.2	23.9	24.9	-0.4	-0.3	51.0	59.0	46.8	55.6
Glaxo Smithkline Con	FMCG	7,445	286	40,970	45,852	8,834	11,248	7,001	8,968	166	213	6.6	28.1	44.7	34.9	9.0	7.9	-4.0	-3.6	20.1	22.7	20.0	23.0
Titan Company	FMCG	961	812	187,944	222,178	21,305	26,807	14,521	18,358	16	21	15.7	26.4	58.7	46.4	13.7	11.3	-0.6	-0.9	23.3	24.4	26.4	27.8
Asian Paints	FMCG	1,389	1,354	194,454	222,789	35,692	42,888	21,940	26,680	23	28	11.4	21.6	60.7	49.9	14.3	12.7	0.1	-0.0	23.5	25.5	22.6	24.7
Godrej Consumer Prod	FMCG	775	905	109,334	121,084	22,017	24,799	15,159	17,466	15	17	4.2	15.2	52.2	45.3	11.7	10.8	0.6	0.4	22.3	23.9	17.1	18.2
Emami	FMCG	436	258	28,004	31,378	7,791	8,789	3,450	4,255	8	9	12.3	23.3	57.4	46.5	9.2	9.1	-0.1	-0.4	16.1	19.5	16.8	19.4
Agro Tech Foods	FMCG	610	16	8,709	9,562	703	800	347	404	14	17	9.6	16.6	42.9	36.7	4.0	3.7	-0.7	-1.0	9.4	10.0	9.8	10.5
Marico Industries	FMCG	381	453	75,189	84,100	12,946	15,342	9,411	11,181	7	9	15.5	18.8	52.2	43.9	17.5	15.4	0.1	-0.1	33.5	35.2	34.7	36.9
Dabur India	FMCG	424	771	87,538	98,860	18,063	20,703	14,757	17,023	8	10	7.5	15.4	50.8	44.0	13.7	11.6	0.5	0.0	26.9	26.4	24.9	27.1
Bajaj Corp	FMCG	389	61	8,670	9,452	2,608	2,834	2,142	2,033	15	14	1.5	-5.1	26.8	28.2	11.6	11.4	0.0	0.0	43.3	40.4	42.4	39.8
Parag Milk Foods	FMCG	243	26	22,366	26,335	2,395	2,999	1,168	1,581	14	19	48.7	35.3	17.5	12.9	2.5	2.1	0.7	0.3	14.1	16.2	18.1	20.0
Nestle	FMCG	11,050	996	112,792	126,945	27,730	31,700	16,594	19,383	172	201	35.4	16.8	64.2	55.0	28.0	24.8	-0.8	-1.0	43.6	45.2	28.5	29.6
Thangamayil	FMCG	360	6	15,937	19,151	725	969	312	444	23	32	36.3	42.4	15.8	11.1	2.6	2.1	2.0	1.7	16.1	19.3	23.5	27.5
Sadbhav Engineering	Infrastructure	214	49	39,958	47,949	4,595	5,514	2,748	2,555	16	15	24.5	-7.0	13.3	14.3	1.7	1.5	2.9	2.4	12.9	10.8	9.9	8.8
KNR Construction	Infrastructure	216	33	20,012	26,016	3,702	4,293	2,092	1,881	15	13	-23.1	-10.1	14.5	16.2	2.2	2.0	0.6	0.6	16.6	12.9	15.1	11.9
IRB Infrastructure	Infrastructure	155	69	69,265	71,725	33,393	29,094	8,818	5,631	25	16	11.2	-36.1	6.2	9.7	0.8	0.8	4.2	5.3	13.7	8.2	4.8	3.8
Ahluwalia Contracts	Infrastructure	320	21	19,759	23,711	2,618	3,142	1,515	1,852	23	28	31.3	22.2	14.1	11.6	2.8	2.2	-0.4	-0.4	21.8	21.5	22.1	21.8
PNC Infratech	Infrastructure	151	40	27,849	37,596	4,038	5,376	2,440	2,538	10	10	-2.8	4.0	15.9	15.3	1.9	1.7	1.3	1.5	12.7	11.8	12.1	11.0
Adani Ports & SEZ	Infrastructure	389	829	112,389	126,480	73,751	84,840	45,107	49,167	22	24	9.0	9.0	17.9	16.4	3.3	2.8	2.3	1.8	18.7	17.2	9.7	11.9
NCC	Infrastructure	89	55	115,658	138,789	13,011	15,267	5,630	6,661	9	11	55.8	18.3	9.5	8.0	1.1	1.0	1.5	1.4	11.9	12.5	13.2	13.6

PhillipCapital India Coverage Universe: **Valuation Summary**

		CMP	Mkt Cap	Net Sales (₹ mn)		EBIDTA (₹ mn)		PAT (₹ mn)		EPS (₹)		EPS Growth (%)		P/E (x)		P/B (x)		EV/EBITDA (x)		ROE (%)		ROCE (%)	
Name of company	**Sector**	**₹**	**₹ bn**	**FY19E**	**FY20E**	**FY19E**	**FY20E**	**FY19E**	**FY20E**	**FY19E**	**FY20E**	**FY19E**	**FY20E**	**FY19E**	**FY20E**	**FY19E**	**FY20E**	**FY19E**	**FY20E**	**FY19E**	**FY20E**	**FY19E**	**FY20E**
Ashoka Buildcon	Infrastructure	130	41	32,072	41,694	4,169	5,212	2,581	2,529	9	9	8.9	-2.0	14.2	14.5	1.6	1.4	1.1	1.4	11.2	9.9	12.4	10.9
Tata Consultancy	IT Services	1,873	7,578	1,453,554	1,635,178	398,821	451,312	309,293	346,343	82	92	21.9	12.0	22.7	20.3	8.2	6.7	0.0	-0.1	36.3	32.9	34.6	35.2
Infosys Technologies	IT Services	736	2,977	819,541	911,492	214,604	241,069	164,759	183,030	38	42	12.3	11.1	19.4	17.5	4.9	4.4	-1.5	-1.6	25.5	25.0	25.2	26.4
Wipro	IT Services	337	1,259	570,529	613,718	119,394	129,910	89,507	99,368	20	22	6.3	11.0	16.9	15.3	2.7	2.4	0.4	0.2	16.2	15.8	15.7	15.4
HCL Technologies	IT Services	939	1,343	592,332	659,799	139,539	156,417	98,613	106,961	73	79	15.0	8.5	12.9	11.9	3.1	2.6	0.2	0.1	24.0	22.0	23.4	21.6
Tech Mahindra	IT Services	700	649	341,217	368,645	59,868	63,272	39,556	41,204	45	47	3.5	4.1	15.6	15.0	3.1	2.8	-0.2	-0.4	20.0	18.5	14.7	14.3
L&T Infotech	IT Services	1,769	296	91,020	105,107	16,970	19,403	13,838	16,169	81	95	19.2	16.8	21.8	18.7	6.9	5.5	-0.3	-0.5	31.8	29.6	30.9	30.2
L&T Technology Serv	IT Services	1,658	146	49,156	57,493	8,644	10,358	7,091	7,984	70	79	40.0	12.6	23.8	21.1	7.8	6.1	0.1	-0.0	32.7	29.0	31.8	29.5
Mindtree	IT Services	837	157	68,009	77,605	10,438	12,181	7,269	8,330	44	51	27.5	14.6	18.9	16.5	4.2	3.6	-0.4	-0.7	22.4	21.8	24.3	23.5
Cyient Limited	IT Services	625	78	47,287	54,837	6,871	8,146	5,054	6,209	45	55	17.8	22.9	13.9	11.3	2.6	2.2	-1.3	-1.5	18.5	19.4	18.3	19.1
Persistent Systems	IT Services	552	67	34,109	37,351	5,806	6,351	3,670	4,159	46	52	13.6	13.3	12.0	10.6	1.9	1.7	-0.2	-0.4	15.6	15.7	15.2	15.6
NIIT Technologies	IT Services	1,209	79	36,169	41,785	6,353	7,390	4,136	4,754	68	78	47.6	14.9	17.9	15.6	3.7	3.2	-1.2	-1.6	20.9	20.3	20.9	20.8
Intellect Design Arena	IT Services	217	26	14,165	16,996	1,292	1,683	1,141	1,023	9	8	133.8	-10.4	25.0	27.8	3.1	2.8	1.1	1.5	-	-	7.9	9.5
Majesco	IT Services	495	15	9,629	11,278	673	999	518	679	18	24	-2,653.9	31.2	27.0	20.6	2.3	2.1	-1.0	-1.1	8.5	10.0	8.0	8.4
Praj Inds.	Logistics	154	15	10,794	13,303	886	1,658	602	1,168	3	7	100.1	93.9	45.9	23.7	3.7	3.3	-1.3	-1.2	8.0	14.0	8.0	14.3
Pennar Inds.	Logistics	38	6	20,698	23,096	1,742	2,203	623	840	5	7	8.5	34.9	7.3	5.4	0.7	0.6	1.5	1.3	9.7	11.9	12.7	14.6
Indo Count Industries	Logistics	55	17	20,304	22,768	2,395	3,005	1,163	1,456	6	7	-7.1	25.1	9.3	7.5	1.0	0.9	1.5	1.5	11.2	12.5	10.7	12.1
KDDL	Logistics	501	5	5,709	6,741	527	675	166	228	15	21	-3.7	38.0	32.8	23.8	3.8	3.5	3.0	2.7	11.7	14.6	8.3	10.0
Gateway Distriparks	Logistics	117	19	4,297	4,595	830	938	1,015	1,179	9	11	22.1	16.2	12.5	10.8	1.2	1.2	1.2	0.9	9.9	11.4	9.9	11.3
Container Corp Of India	Logistics	694	313	66,658	81,640	14,790	18,617	12,200	15,512	25	32	16.3	27.1	27.7	21.8	3.4	3.1	-1.5	-1.4	12.1	14.4	12.1	14.5
Navkar	Logistics	52	20	4,731	6,125	1,485	1,990	585	984	4	7	-42.0	68.2	13.2	7.9	0.4	0.4	2.7	1.7	3.2	5.1	3.7	5.0
Allcargo Logistics	Logistics	110	31	67,405	74,358	4,462	5,346	2,154	2,856	9	12	20.9	32.6	12.6	9.5	1.3	1.2	0.5	0.2	10.3	12.5	9.8	11.9
VRL Logistics	Midcap	288	31	21,203	23,774	2,366	3,057	940	1,256	10	14	1.5	33.6	27.7	20.7	4.1	3.6	0.8	0.7	14.7	17.4	12.0	14.0
VGuard Industries	Midcap	207	90	26,496	30,405	2,362	2,975	1,704	2,152	4	5	28.0	26.3	51.8	41.0	10.4	8.7	-0.1	-0.2	20.0	21.2	20.7	22.1
Bajaj Electricals	Midcap	479	62	67,398	77,716	4,392	6,092	2,299	3,235	23	32	33.0	40.7	21.1	15.0	4.8	3.8	2.6	2.1	22.8	25.2	15.2	16.7
Finolex Cables	Midcap	450	94	n.a.	n.a.	-26,639	-29,690	-27,503	-30,799	-180	-201	-867.8	12.0	-2.5	-2.2	2.8	2.4	0.0	0.1	-110.8	-109.5	-114.3	-113.4

PhillipCapital India Coverage Universe: **Valuation Summary**

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Name of company	Sector	₹	₹ bn	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
Havells India	Midcap	682	400	100,219	114,610	16,582	19,881	12,313	14,469	20	23	22.1	17.5	34.6	29.5	10.1	8.9	-0.2	-0.2	29.3	30.2	27.9	29.3
Indiabulls Housing Fin	NBFC	832	586	53,594	63,661	63,889	74,924	42,676	52,362	100	123	18.9	22.7	8.3	6.8	2.4	2.0	0.0	0.0	30.3	32.4	3.0	3.1
Muthoot Finance	NBFC	536	165	44,850	49,935	30,347	33,911	18,668	20,858	47	52	8.5	11.7	11.5	10.3	2.3	2.0	0.0	0.0	22.1	21.0	5.4	5.5
Shriram City Union Fin	NBFC	1,735	128	37,000	40,510	23,443	25,483	8,999	9,585	136	145	35.4	6.5	12.7	11.9	1.8	1.6	0.0	0.0	15.3	14.5	2.9	2.8
Cholamandalam Inve	NBFC	1,188	224	36,815	44,543	21,704	25,845	11,047	13,104	71	80	13.4	13.2	16.8	14.9	3.1	2.2	0.0	0.0	19.7	17.7	2.5	2.5
Shriram Transport Fin	NBFC	1,188	325	74,407	83,540	58,499	65,026	22,676	27,043	100	119	53.7	19.3	11.9	10.0	1.9	1.6	0.0	0.0	16.7	17.1	2.4	2.5
LIC Housing Finance	NBFC	483	272	38,520	44,281	33,649	38,672	21,941	24,931	43	49	10.3	13.6	11.1	9.8	1.6	1.4	0.0	0.0	15.6	15.2	1.2	1.3
Repco Home Finance	NBFC	441	38	4,647	5,178	4,036	4,461	2,263	2,561	36	41	8.9	13.2	12.2	10.8	1.8	1.6	0.0	0.0	15.8	15.5	2.2	2.2
Dewan Housing Fin	NBFC	224	196	21,225	23,924	18,188	20,488	10,849	12,118	35	39	-7.4	11.7	6.5	5.8	0.7	0.6	0.0	0.0	11.7	11.8	1.1	1.2
Mahindra & Mahindra F	NBFC	446	312	45,153	51,332	30,778	34,922	13,535	16,084	22	26	59.3	18.8	20.2	17.0	2.6	2.3	0.0	0.0	13.6	14.3	2.3	2.4
Manappuram Finance	NBFC	97	95	23,080	26,452	12,737	14,981	7,997	9,410	9	11	14.2	17.7	10.3	8.7	1.8	1.6	0.0	0.0	19.3	19.4	4.9	4.9
Magma Fincorp	NBFC	108	40	13,261	14,466	7,229	7,952	3,343	3,801	12	14	27.7	13.7	8.7	7.6	1.1	1.0	0.0	0.0	13.3	13.2	2.4	2.5
Ipca Laboratories	Pharma	789	97	36,299	42,411	6,786	8,187	4,299	5,381	34	43	79.9	25.2	23.0	18.4	3.2	2.7	0.3	-0.2	13.9	14.8	11.7	13.1
Aurobindo Pharma	Pharma	788	365	189,052	216,697	39,512	47,673	24,087	29,690	41	51	-1.1	23.3	19.1	15.5	3.3	2.7	0.8	0.3	17.2	17.7	17.5	18.7
Divi's Laboratories	Pharma	1,520	320	46,815	55,270	17,321	20,450	12,066	14,198	45	53	42.1	17.7	33.4	28.4	5.9	5.1	-0.0	-0.1	17.7	17.9	-	-
Cadila Healthcare	Pharma	353	386	122,342	136,026	26,981	30,971	17,422	20,278	17	20	-1.5	16.4	20.7	17.8	3.4	2.9	1.1	0.6	15.9	15.5	11.3	12.0
Sun Pharma	Pharma	453	105	304,948	352,607	71,190	88,400	44,636	59,037	19	25	2.9	32.3	15.8	18.4	0.0	2.3	1.5	-0.6	10.6	12.3	8.8	10.4
Cipla	Pharma	511	516	16,488	18,687	4,204	5,045	1,548	2,031	19	25	5.2	31.2	26.5	20.2	2.6	2.4	0.5	0.1	17.4	19.2	-	-
Lupin	Pharma	861	401	161,691	181,374	28,092	35,197	10,798	15,881	24	35	-20.1	47.1	36.0	24.5	2.7	2.5	2.1	1.5	7.5	10.2	-	-
Glenmark Pharma	Pharma	655	169	96,271	107,869	17,990	21,327	8,445	10,865	30	39	8.8	28.7	21.9	17.0	2.9	2.5	1.7	1.3	13.3	14.7	9.6	11.0
Dr Reddy's Labs.	Pharma	2,619	378	154,350	174,370	30,870	37,664	16,187	21,627	95	127	59.9	33.6	27.6	20.6	3.2	2.9	1.3	0.8	11.7	13.8	7.2	8.9
Biocon	Pharma	651	351	54,227	70,124	12,589	19,028	6,703	11,400	11	19	131.7	70.1	58.2	34.3	6.8	5.7	0.9	0.3	11.2	16.2	11.1	16.1
SRF	Specailty Che	2,044	100	72,923	82,582	13,491	16,351	6,473	8,216	113	143	55.8	26.9	18.1	14.3	2.8	2.4	2.2	1.7	15.7	16.9	10.0	11.0
Meghmani Organics	Specailty Che	63	24	20,700	24,955	4,492	5,690	2,121	2,705	8	11	23.0	27.5	7.5	5.9	1.4	1.1	1.3	0.7	18.2	19.0	14.8	15.5
Camlin Fine Sciences	Specailty Che	56	11	8,561	12,182	805	2,010	82	935	1	8	-126.9	1,044.7	83.1	7.3	1.8	1.4	5.5	1.8	3.9	22.3	-	-
Aarti Industries	Specailty Che	1,530	103	48,399	56,591	9,196	10,809	4,694	5,846	58	72	41.0	24.5	26.5	21.3	6.1	4.8	2.3	2.1	23.8	23.1	-	-
Vinati Organics	Specailty Che	1,566	51	10,075	14,538	3,566	4,803	2,392	3,181	47	62	76.2	33.0	33.6	25.3	7.9	6.1	1.1	0.6	23.6	23.9	-	-
Atul	Specailty Che	3,453	87	40,437	44,621	7,400	8,300	4,519	5,067	152	171	60.7	12.1	22.7	20.2	3.9	3.3	-0.5	-1.0	16.8	16.1	-	-

Source: PhillipCapital India Research Estimates

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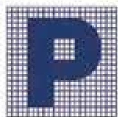

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