New Year Special Edition

IIFT'S Business & Finance Magazine

# INFINनीति

January 2015

End of QE Tapering: Challenges for World Economy

Financial Inclusion in India: All Talk, No Action?

# Fundraising in E-COMMERCE Companies

New Development Bank: Role of India and Unmet Expectations

Growth Vs Taming the Inflation

Fall in Crude Price: Repercussions for India

The Next Reserve Currency of India

RBI Rate Cut: An Ideal Time?

Nehruvian Socialism Vs Modinomics

**Also In This Edition:**

Internship Experience: Langham Capital

MakeMyTrip Equity Research Report

Fin-Cross Fin Trend

Experts Take on Mining Industry: TIPL

## FROM THE EDITOR'S DESK



*Dear Friends,*

*Wish you all a happy and prosperous New Year*

***The past year has seen major developments in the field of business, banking and finance. With the new government coming in, there was a renewed push to restore sentiment and bring India back to the path of high growth. With this in mind, many reforms were pushed in sectors as varied as finance to banking to education and more.***

***With the changing business climate came renewed optimism about the future of the Indian market, leading to a surge in investment inflows. These fresh inflows were targeted at sectors as diverse as e-commerce to aviation, automobile to pharmaceuticals, financial services to hospitality and more.***

***Owing to these inflows, perhaps no other industry has seen as much media attention in recent times as the E-commerce industry. With an ever-changing business landscape, the increasing thirst of the Indian consumer to consume, extravagant valuations in other countries and an increasingly net-savvy populace, India's e-commerce industry finds itself at the centre of the 'Next Big Thing' debate. In this edition, we take you through one of the most significant aspects of this burgeoning industry - its fundraising.***

***The Indian rupee has seen a volatile run in the past few years with the US dollar causing significant fluctuations in its value. In this issue, we try to analyze how India's reserve system works and the alternate options for reserve currencies.***

***We then take you through a sector considered crucial to the growth of India as also the developing world. The international banking sector has seen many developments over the past few months, none as significant as the proposal for a 'New Development Bank'. We try to give our readers a recap of what has happened till now and the challenges and opportunities ahead.***

***Perhaps the single most talked about incident this past year has been the Quantitative Easing Tapering announced by the US Federal Reserve. With the taper coming to an end, we analyze the ramifications on major developed and developing economies. We try to understand how financial markets have responded in the past and are likely to respond in the future to this development.***

***With the Construction and manufacturing sector being among the largest beneficiaries of the inflow of foreign funds, we try to gain insights from our expert Mr. Ayan Banerjee of Tractors India Pvt. Ltd. on the future developments expected and also his take on major finance related issues in Indian industry.***

***We then turn to the oil industry which has seen major developments in terms of technology and the US' shift from being the largest importer to a net exporter of oil. We try to give our readers an Indian perspective to all that has happened the world over and its consequences on our economy.***

***Recently the rate cut by RBI has been a much talked about and awaited move by India Inc. In this edition, we cover the pros and cons of such a move as also its result on the external sector of India.***

***The elections which happened last year saw an intense debate on the brand of economics that the new government was likely to follow. Here, we try to give an interesting take on India's long-standing question on Nehruvian Socialism v/s Modinomics.***

***We continue with our regular column on Equity Research. This time we present to you a report on makemytrip.com giving a blow-by-blow account of the company and its sector along with an analysis of its financial ratios, key performance indicators and valuation.***

***The edition also discusses perspectives on the growth v/s inflation debate and effectiveness of a national plan centred on financial inclusion. Besides these, the edition also features regular columns like FIN-Trivia, FIN-Cross, FIN-Trend and News Chronicles.***

***As the new team taking over, we see the coming year with hope that we can live up to the high standards that our readers have come to expect from InFINeeti. We hope that you will enjoy reading this edition as much as we have enjoyed creating it.***

***We also see this magazine as an opportunity to learn from our readers through their feedback. Do write to us with your suggestions and recommendations. We can be reached at infineeti@gmail.com.***

***Happy Reading!!!***

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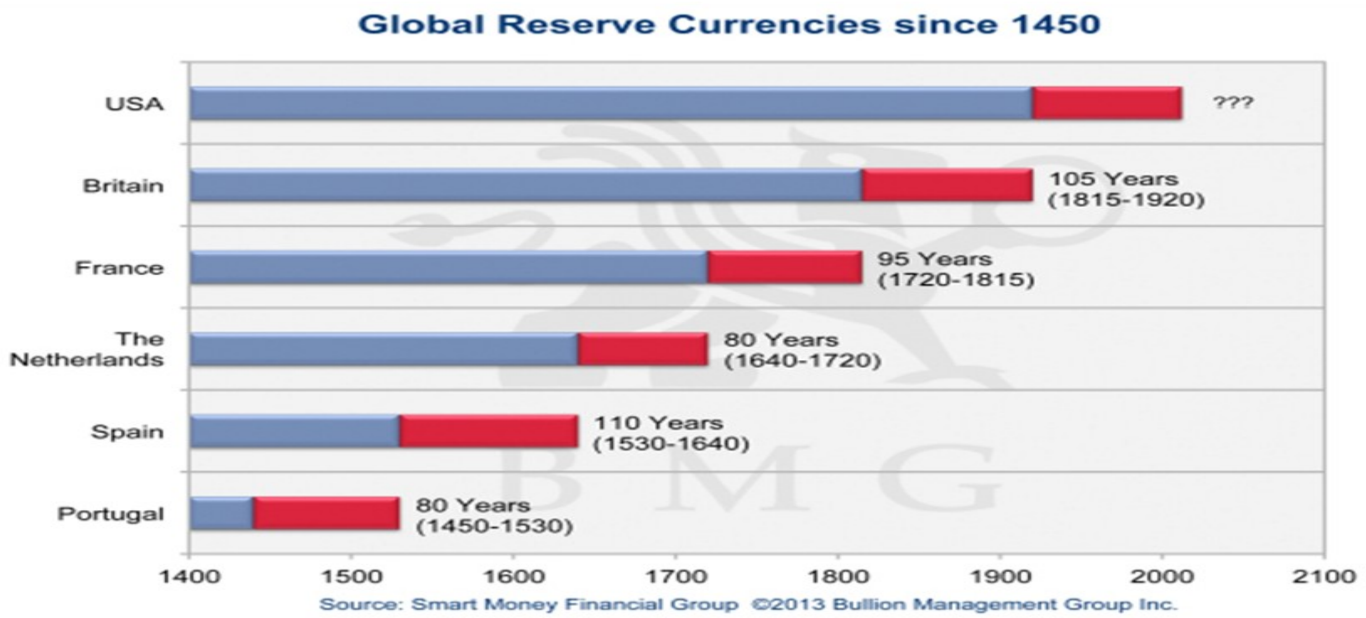
# THE NEXT RESERVE CURRENCY

-BY SAUMYA SINGH & ANSHNI DATA
NMIMS, MUMBAI




***"There are many roles that an international currency can play but of all the international roles a currency may play, none bestows as much social status or monetary power upon a nation than issuing an important reserve currency"***

Reserve currency is a currency that is held in significant quantities by governments and institutions as part of their foreign exchange reserves and is commonly used in international transactions. When a country acquires reserves, it doesn't place the currency in general circulation. Instead, it deposits the reserves in the central bank. The popularity of reserve currency is easy to see: between 1995 and 2011, the amount of currency held as reserve increased by over 730%, from around $1.4 trillion to $10.2 trillion.

The advantage of being the country issuing a reserve currency is greater number of transactions in that currency which provides more liquidity for this currency. Another advantage is that reserve currency issuing countries are exposed to a lesser level of exchange rate risk.

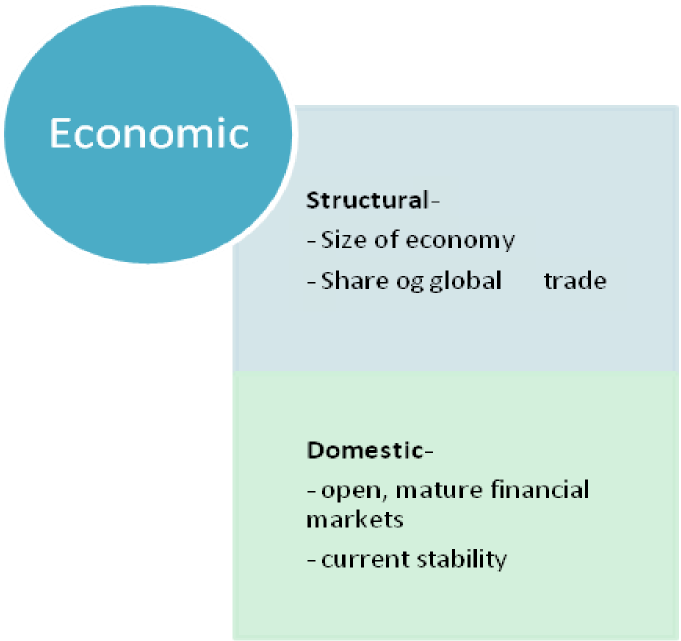
However, there are some costs of being a reserve currency issuing country. When these international reserve currencies are also domestic ones, the supply of global liquidity arises from one or more "core countries". Over time they tend to take benefit of other countries' high reliance on their domestic money. By exploiting this "exorbitant privilege", these countries can develop policy incentives to accommodate shocks (financing of a war) that can be sustained only if the rest of the world completely demands their liquid, safe assets. Such actions could impair the smooth functioning of the international monetary and financial system.

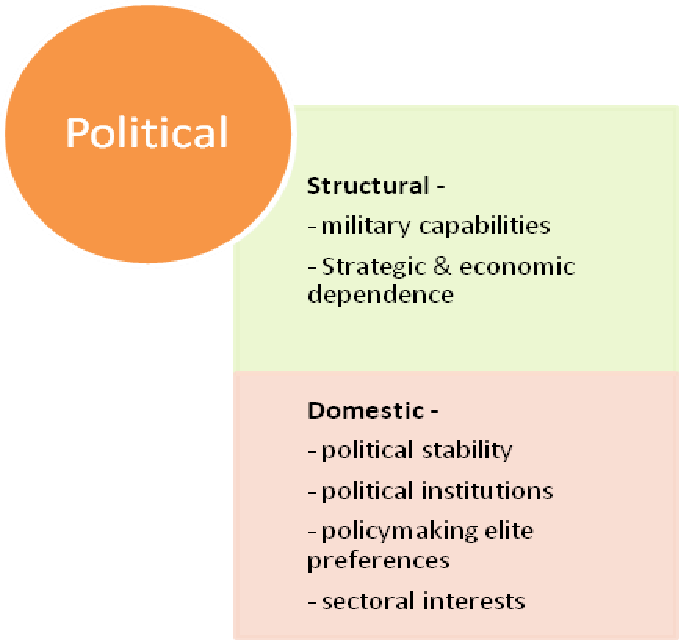
**What makes a currency suitable candidate for a reserve currency?**

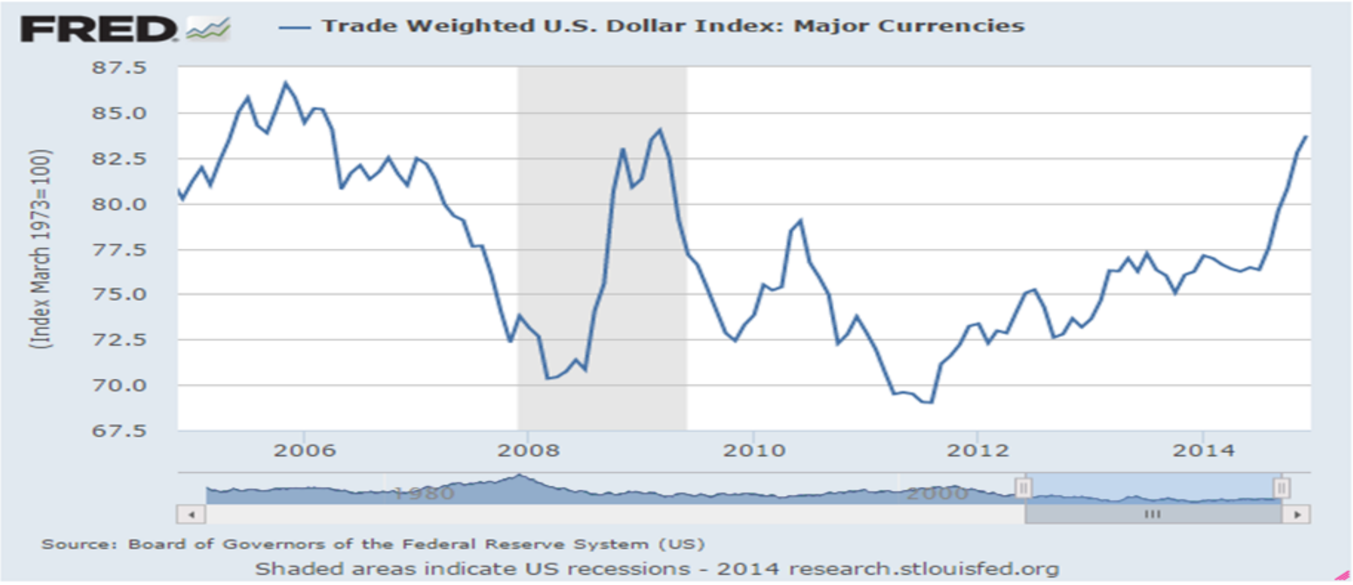
An international reserve currency must meet three conditions: stable value, high transparency and low transaction costs. The trading volume should be high on daily basis in international market. The perceived confidence in a currency is also a function of its country's political situation, fiscal and trade balances, central bank's policy and projected economic outlook.

In Indian context, the opening up of economy in 1990's followed by the Asian financial crisis as well as 2008 financial crisis led to India looking for a stable currency that fulfilled the above requirements. Dollar was a strong candidate as volume of trade with U.S was significant and it was also globally accepted as a hard currency. It has remained the most important currency for international transactions since Bretton Woods Agreement, signed in July, 1944.Currently major transactions and price settlements take place in dollar, even when U.S.A is not part of those transactions. Also it prides itself upon being liquid and the most transparent financial market while enjoying dependence of many nations on it as the destination of export as well as military support.

However, from time to time U.S dominance had been challenged by many currencies such as Yen in 1970's followed by Euro in 2000's and now by Yuan. The movement of Trade weighted dollar index (measure of the value of the United States dollar relative to other world currencies), continues to weaken (Fig 2). Apart from the low saving rates of U.S, current account as well as trade account deficit questions U.S. authority to be a reserve currency. Many countries are now looking for alternatives to dollar. DuPont settles many of its international accounts in Yuan and Euros. Additionally, among today's top reserve holders are Brazil, Russia, and India. Collectively, these countries not only hold a massive portion of global dollar reserves, but they also share a widespread frustration with the existing dollar-based monetary system. The possibility that the BRICS might someday bring together diversification of their reserves away from the dollar and into one of their own currencies (the Renminbi being the likely candidate) could






lead to rise of an alternate currency to dollar.

## RISE OF THE CHINESE REDBACK

As mentioned above, U.S dominance as reserve currency has been challenged from time to time. Yen's rise in 1970's was limited by inflationary monetary policy, high transactions cost as well as volatile exchange rate. In 2000's,The euro was seen as a prime candidate for those seeking alternatives to the dollar, but it unfortunately faced its own share of uncertainties arising from the euro zone debt crisis. This has led to increasing interest across the world in holding non-traditional currencies in foreign exchange reserves. Many global investors and central banks are increasingly seeing the Yuan as another alternative. The reasons for being optimistic about Yuan becoming the next reserve currency are many. First, China's increasing share of world trade would clearly justify greater use of the Yuan. Second, China's record of supportive government policies and macro-economic stability has undoubtedly contributed to the RMB's appeal in recent years. Third, China has strong official and institutional support. At the China Development Forum in March 2014, the People's Bank of China deputy governor, Yi Gang, emphasized the need of strengthening financial regulations and improving market-driven exit mechanisms for financial institutions. We should expect to see improvement in industry-side infrastructure, including back-office support, settlement, and linkages to the over-the-counter market. This will help to ensure the safe and efficient operation of the financial market and systematic stability. Fourth, the opening up of China's onshore capital market will be an important step in the Yuan becoming a major investment currency China has a three-pronged approach to Renminbi internationalization: expand the currency's role in foreign trade settlement (it has already overtaken the euro to become second only to the dollar) – encourage its use in cross-border investment, and develop offshore Renminbi centers.

Beijing is already freeing up rates for foreign-currency deposits, easing limits on cross-border capital flows in the Shanghai FTZ, easing global investors' access to Chinese markets .The daily trading band for the Renminbi-dollar rate has now been doubled to + or -2%. As a consequence, several foreign central banks now hold Yuan reserves, suggesting some already see the Yuan as a workable reserve currency.

But it is not that everything is in favor of RMB becoming the next reserve currency. There are blockages too. Because China is still a single-party dominated nation, its fiscal and monetary policies won't react to market forces the way a democracy's do, and it creates a strong chance of uncertainty. The huge divide between urban and rural could lead to social instability that could threaten the country's economy and currency. The U.S. economy relies on innovation and competition to generate productivity; without those free-market forces China's medium-term competitiveness is more uncertain. Conversely, China's far more opaque institutions and the potential for political instability may slow adoption of the Renminbi as a reserve asset. So if China wants to "Yuanify" some of its claims on the rest of the world, it needs have to open its financial system to the world.

**INDIAN CONTEXT**

Traditionally India's has held U.S dollar in reserves as its major international currency. But rising acceptance of Yuan in global markets may cause policy makers to think about the current composition of foreign reserves. It is true that the past decade has seen a rapid increase in India and China's trading pattern. China has emerged as its biggest trading partner in the current fiscal replacing the UAE and pushing it to the third place, according to a study conducted by PHD Chamber of Commerce. India-China trade has reached $49.5 billion with 8.7% share in India's total trade, while the US comes second at $46 billion with 8.1% share and the UAE third at $45.4 billion with 8% share during the first nine months of the current fiscal. All these figures points to growing need to adopt china's as our reserve currency. But many national issues starting from the border dispute to managing the balance of power in South Asia may act as a hindrance.

So with given situation India has to judge carefully. It has to choose whether to engage with the superpower and the emerging superpower at the same time.

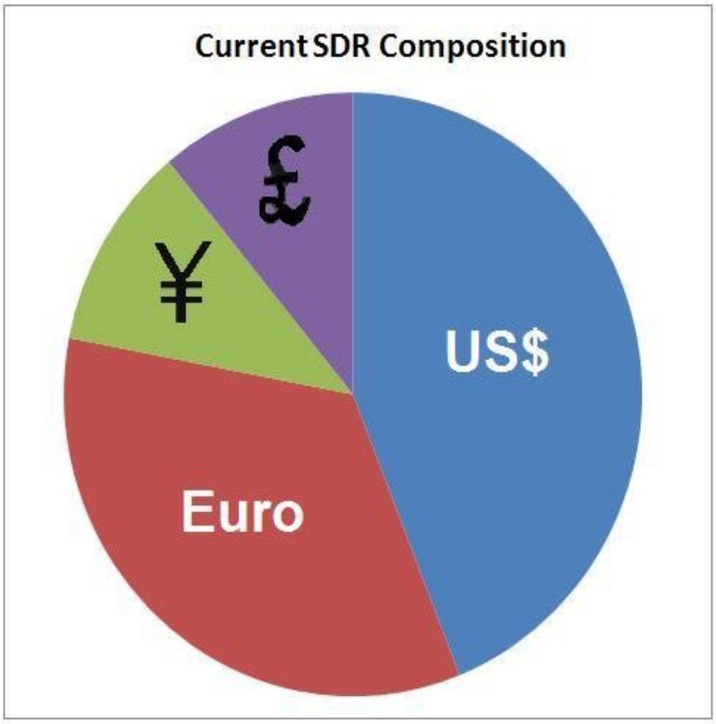
True China became India's largest trading partner, overtaking America in March 2008. But along with it has come an unsustainable trade deficit that amounts to around $40 billion. Trade relations with America are equally important because current and potential business with America, particularly in software and defense, is so enormous that we can't avoid importance of dollar. America's overall investment in India far exceeds China's investments. Also, for international issues like United Nations Security Council membership, Nuclear Security Group membership, global terrorism, there is no option but to engage with America.

We can look at our emerging trade partners also such as ASEAN nations, Brazil, Russia, and South Africa However they suffer from obstacles to reserve currency status including closed or opaque domestic asset markets, partial convertibility, political instability, and military tensions.

Other options include adoption of SDR as well as Bit coin or maintaining Gold reserves. However, the chances of SDR becoming a world reserve currency are bleak. The reason being SDR is not a currency. It is linked to a basket of currencies with a weight of 44% for the dollar, 34% for the euro, and 11% each for the yen and pound sterling. If India wants to use its SDRs, it will typically ask the IMF for dollars in exchange. The IMF will debit India's SDR account, credit America's SDR account, ask the US for the corresponding dollars, and hand these to India.

Although Bitcoin's popularity is on rise in India, the recent warning of RBI against use of virtual currencies, pointing out that users expose themselves to potential financial, legal and security risks undermines possibility of Bitcoins becoming the next reserve currency of India.

Looking at gold, it limits liquidity during the times of massive infusions of liquidity or cash, such as the global




***Source: huffingtonpost.com***

financial crisis. Also the supply of gold is limited. If a country is tied to gold, it can't print money at will.

**CONCLUSION**

The world for which we need to prepare is thus one in which several international currencies exist simultaneously. In coming years, a "reserve currency basket" may emerge, with central banks storing wealth in a blend of dollars, Yuan, Rupee, Rubles, as well as valuable metals and cyber currencies. Keeping in mind these trends, India might have to move to ***Reserve Diversification*** instead of relying excessively on dollar or Yuan.


# NEW DEVELOPMENT BANK: ROLE OF INDIA AND THE UNMET EXPECTATIONS

-By Ayan Deb

## The Old World: Dominance of the West

Post World WAR II, all the nations formed a consortium of power that would help prevent the recurrence of such wars. Thus the Bretton Woods Conference lead to the establishment of three such institutions that facilitated harmony and stability in the world through trade and financial support. These institutes were World Trade Organization (to facilitate trade), International Monetary Fund (to promote macroeconomic stability) and World Bank ffor development assistance).

The funding from World Bank was primarily used to rebuild Europe. Asian development needs suffered as most of the financial aid by World Bank was directed towards the West. In fact, till now India does not have a seat in the World Bank.

The IMF unlike World Bank is not a democratic institution i.e. larger your contribution, larger is your voting right. USA enjoys a voting right of 17.69% where as China and India have 4.0% and 2.44% respectively. In 2011 the world's largest developing countries i.e. the BRIC nations have issued a statement declaring that the tradition of appointing a European as managing director undermined the legitimacy of the IMF and called for the appointment to be merit-based.

## The New Beginning: Emergence of the "NDB" out of the Political Gridlock

The five BRICS countries comprise Brazil, Russia, India, China, and South-Africa. BRICS represent almost 3 billion people which accounts for 40% of the world population, with a combined nominal GDP of US$16.04 trillion i.e. 20% world GDP. The BRICS nations represent 18% of the world economy.

With the growth of the BRICS nations there was a need to have a separate bank. Reforms to allocate more voting power to the emerging economies like the BRICS nations were agreed by the G20 in 2010; however Congress has not yet approved these recommendations. Thus the heavy handedness of the IMF and World Bank lead to the rise of the New Development Bank –"NDB" (BRICS Bank).

World Bank

INTERNATIONAL MONETARY FUND

The NDB would have its headquarters in Shanghai, China but it would be headed by an Indian president. Also the first chair of Board of Governors will be from Russia and the first chair of the Board of Directors will be from Brazil while a regional office centre would be established in South Africa.

## Interesting Time: The New Dynamics

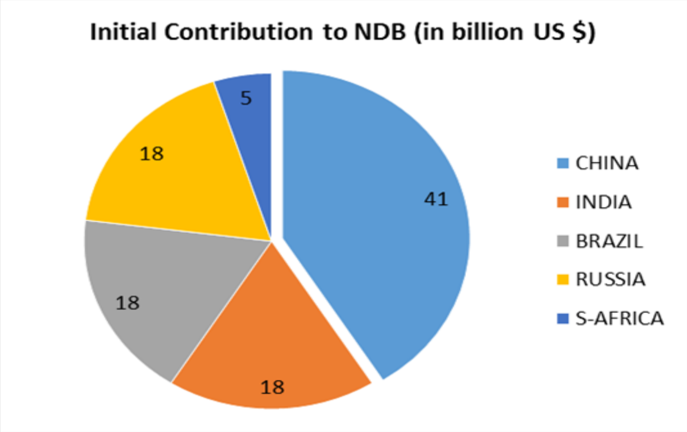
The world is no more a unipolar arena where power-politics is dominated by the West; instead we are experiencing a new era of economic and social growth driven by the developing economies. The dominance of the US dollar as a reserve currency is deemed to be undermined if the NBD, i.e. the BRICS bank can transform itself into a clearing house for trade and finance in non-USD currencies. Thus there could be gravitation toward different currency pricing for trade in emerging markets and investors will have to rethink their risk models in regard to the currencies. These would further lessen the dominance of the US and the sanctions it has impose on some countries of the world. As an instance we assume that in the Russia-Ukraine crisis the stance of US would be to put sanctions, but if Russia can convince the NBD to support its cause, all the US sanctions would become useless. The world is thus becoming increasingly multi-polar. The epicenter of power is shifting from US to the emerging nations.

The IMF and World Bank have failed to meet the demands of the developing economies. The establishment of the NDB might initiate a change in the status quo of IMF and World Bank where in they would try to incorporate more voting rights for the BRICS nations.

The NDB demonstrates the viability and dynamics of the emerging economies despite all the negative criticisms by West dominated economists.

Some critics argue that there would be conflict of interest and power amongst the BRICS nations since China would aggressively try to amass disproportionate wealth and power through NDB. China is expected to make the biggest contribution of $41 billion followed by $18 billion each from India, Brazil and Russia and $5 billion from South-Africa. China has contributed most to the NBD, it has the biggest surpluses and foreign exchange reserves in the world (nearly $4 trillion, almost one-and-a-half times the size of Indian economy) and hence its influence on NBD would be greater than that of the other members.

This thought is counteracted by the logic that the BRICS nations have set up the NDB for development activities in these nations. This single objective will be the unifying thread for the BRICS nations.




The NDB is a testimony to China's global leadership. China needs to be careful to balance its own influence on the bank and the impact of other members. This becomes all the more crucial when BRICS members have diverging interests and even conflicting interests (such as territory disputes between China and India) among themselves.

## BRICS BANK AND INDIA

India being one of the major growing economies has earned its mettle among the BRICS nations. Through the NBD India is improving on her bilateral ties with China

The status quo is already changing as India was recently invited by China to be a member of the 21-nation Asia-Pacific Economic Cooperation (APEC). This move will not only boost India's economy but also enhance the effectiveness and importance of the APEC. As a member of the G20, the East Asia Summit, as well as an ASEAN partner, India is already capable of playing a very important role in deepening trade and increasing investment in the region. India has propagated its 'look east' policy from 1991 and has already signed trade agreements with Japan, South Korea, Singapore, Thailand, Malaysia and ASEAN. India can transform itself into the production network hub for the region. Also it would encourage India to speed up its trade liberalization process. Thus this new membership in APEC will enhance capacity building, trade proliferation and investment cooperation in the region.

The Chinese President Xi had also asked India to deepen its involvement in the Shanghai Cooperation Organization (SCO). SCO includes only six nations – China, Russia, Tajikistan, Kazakhstan, Kyrgyzstan and Uzbekistan. The importance of the SCO is that India can form larger relations with South Asia and Central Asia. Thus the NBD i.e. the new BRICS Bank has provided India the platform to pitch herself to the rest of Asia as a new powerful nation, an alternative to China.

However, critics have started picking holes in the structure, operations and potential limitations of the new bank. According to reporters, the selection of Shanghai as the headquarters for the BRICS Development Bank might hurt Narendra Modi's domestic ratings. But the Prime Minister of India, Mr. Modi was quick to dismiss all these apprehensions and he underscored India's priorities by highlighting the importance of resolving the boundary dispute. He has also urged the Chinese President, Xi Jinping that peace must be maintained on the border until there is a resolution. There have been frequent incursions by Chinese troops across the Line of Actual Control. India and China have land disputes over the Himalayan border over which the two countries went to war in 1962. Xi also called for speedy negotiations to settle this boundary dispute and dismiss all the allegations of cross-border incursions.

Modi has tried to balance two things – the trade relationship with China as well as India's security interests. He is actively seeking Chinese investment in infrastructure projects that was proposed in the recent Indian Budget. At the same time, Indian government is also proactive with the Chinese counterparts on the issue of trade imbalance which is currently in China's favor.

## CONFRONTATION VS COLLABORATION

The NBD has a planned capital base of US$50 billion, rising eventually to $100 billion while the World Bank has US $232 billion capital reserves. We must realize that the NBD is not a competitor to World Bank but it is an attempt by the BRICS nation to provide hassle-free funding for the infrastructural projects through its Contingent Reserve Arrangement (CRA) framework and thus creating better conditions of living in these nations.

Thus most certainly the new BRICS development bank is not going to replace the IMF and World Bank any time soon as the latter will still remain powerful players in the global economic arena. The relationship between these two is a complementary relationship rather than a conflicting one. But in the long run the competition between the two might intensify and the final outcome will depend on the balance of power between the two poles of the world: the developing countries and the developed countries.

# END OF QE TAPERING:
# CHALLENGES FOR THE WORLD ECONOMY

-By Prateek Keshwani
& Aniket Kumar

IIFT, Kolkata


## MONETARY POLICIES BEFORE QE

For 95 years of its 101-year existence, the Fed exercised monetary control through supply of credit to the banking system to lower short-term interest rates or withholding credit to increase short-term interest rates via open market operations. The Fed also has the right to change the banking system reserve requirements (or liquidity ratio), the amount of cash and other liquid assets banks need as a percent of deposits (similar to SLR and CRR in India), and the bank rates, the amount the banks pay to borrow reserves from the Fed.

## QUANTITATIVE EASING

QE is a tool enacted by several Central Banks to increase the money supply and avoid deflationary pressures. All this started in late 2008 post the Lehman brother crisis. There was a huge liquidity crunch in the market and banks did not have money. Whenever there is a huge liquidity crunch the central bank reacts to infuse liquidity into the system. That's exactly what the US central bank did. US central Bank (Federal Reserve Bank of US or Fed) started with measures to infuse liquidity into the system. Liquidity is typically infused into the system by two common methods:

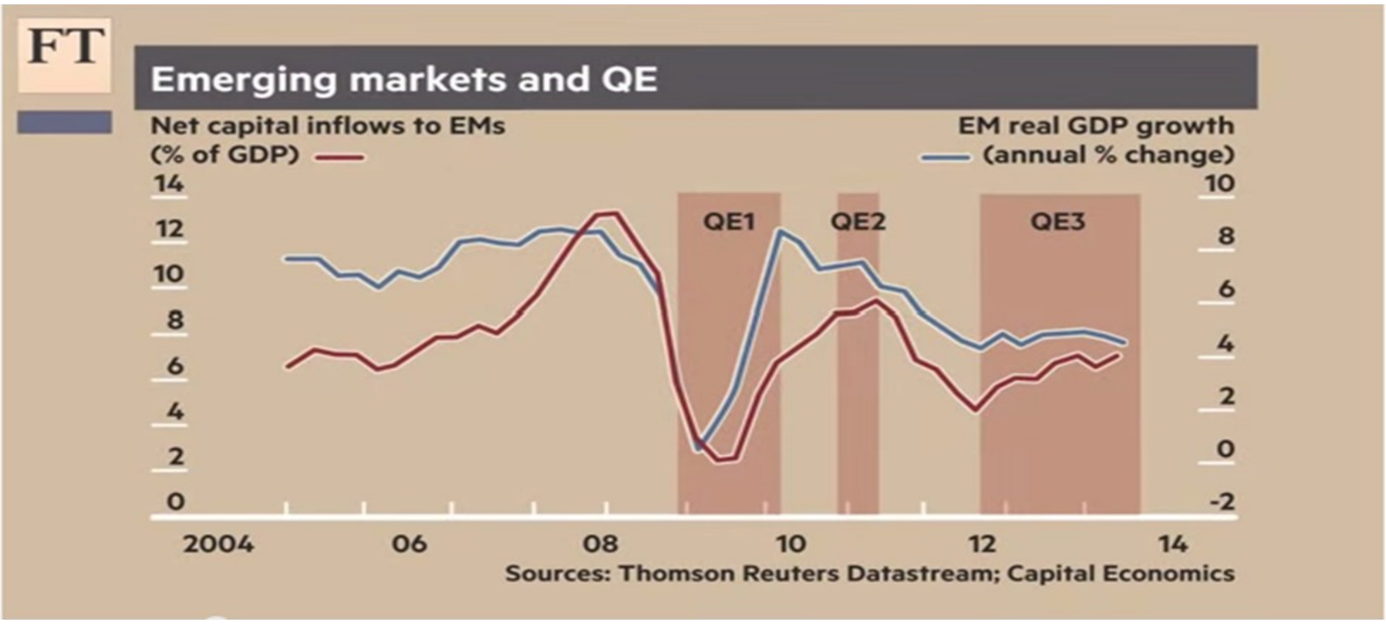
- OMO (Open Market Operations)
- By decreasing the interest rates (Repo & Reverse Repo) in the market.

To infuse liquidity into the system the Fed followed the first method (through OMO), which they called as Quantitative Easing (or QE). In the OMO:

- The Federal Reserve purchases bonds from financial institutions such as banks.
- The increase in reserves is expected to help decrease borrowing rates.
- Buying bonds is also expected to raise their

value, thus reducing long-term interest rates.

There is a wide consensus that quantitative easing (QE) worked. The practice - characterized by asset-purchasing programs by central banks - has been instrumental to keep interest rates low and help deliver economic incentive. But, as developed economies resume a growth trajectory after the Great Recession, the key question ahead is, since the QE has come to an end how will the central banks bring monetary policy back to "normal" without creating massive financial market dislocations?

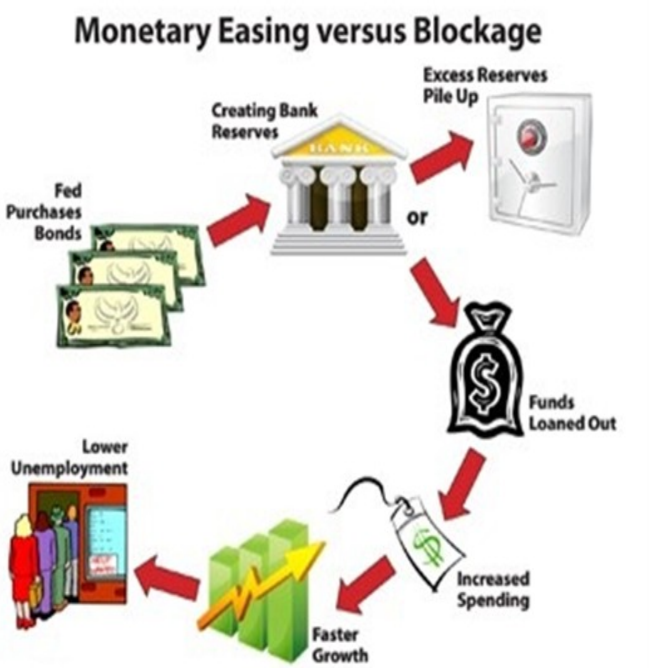



## IMPACT ON EMERGING ECONOMIES

Over the past 6 years, emerging markets have lived in a world defined by the US Fed's policies of easy money. Streams of liquidity from developed economies have flowed to developing economies, financing corporate investment and infrastructure and allowing consumers to indulge in credit fuelled retail dreams. So, therefore the US Fed's announcement that it will draw QE3 to a close represents something of a leap into the unknown.

The chart above gives an impression of the type of impact that the QE appears to have had on emerging market's growth since it started in late 2008. From 2008 to 2010 the impact was pretty dramatic. The liquidity that flowed from the fed's money printing exercise helped float a lot of emerging market boats off the ropes at that time.

The average EM growth went from around 3% in early 2009 to over 12% in early 2010.The subsequent rounds of



QE (QE2 & QE3) had less of an impact, but still helped to keep the overall growth trajectory of the emerging markets moving upward. This was mainly because QE led to a sharp increase in investment inflows from the developed to the developing world. A lot of this money went into the local currency bond markets and stock markets in developing countries. The emerging economies' debt market is so popular because it pays a very high interest (close to ~8%). Whereas, in the US, the investor gets an interest rate of close to ~2.25%.

The concern now is that with the Fed stilling its printing presses the surge in liquidity available to emerging markets will decline. Also, if the Fed moves to tighten monetary policy in the coming months, liquidity may start to retreat from emerging markets and gravitate back to the US to take advantage of the higher returns available.


## CHALLENGES FOR WORLD ECONOMY

**Challenge 1: Dealing with excess liquidity**

The unconventional monetary policy & QE put excessive liquidity around the world which did have the impact of inducing much more external borrowing than should have taken place in many of the emerging market economies. The big question that many emerging nations are facing now is "How do they reduce their dependence on QEs?"

**Challenge 2: Managing Potential Market Distortions**

With the low interest rate environment for an extended period of time and with ample liquidity moving around the globe, there is a feeling that market participants may take too much risk which might later on turn into bad debt situation. The market making capacity of many institutions is limited by regulatory constraints which leads to less of liquidity and a lot more of volatility.

**Challenge 3: Hot Money flowing into Emerging Market**

Most emerging markets have already developed enough immune system to deal with the tapering of QE except for the handful of 1 or 2 economies which are in trouble. China is now basically immune from many of the implications of the ending of QE. But still, there exists the market sentiment that investors might start shifting their money back to the US market from the emerging economies' market.

## Cause of Panic among Investors

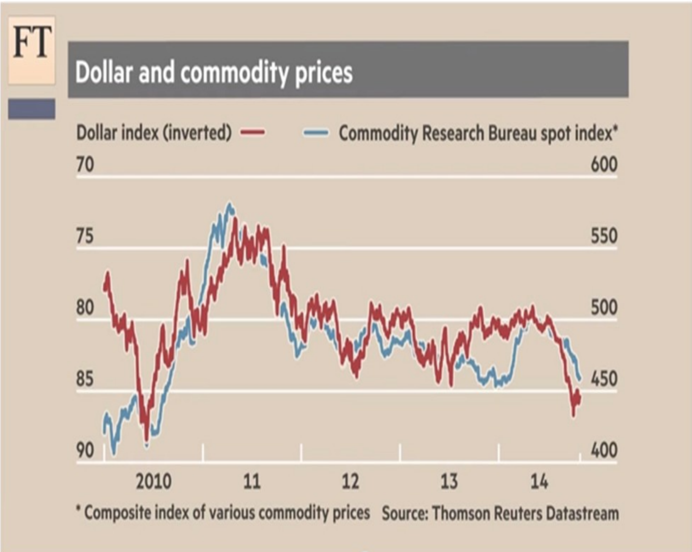
The first is the **Taper Tantrum**. On July 9, 2013 Mr. Ben Bernanke (then Fed chief) made the announcement of tapping down QE3 by late 2013. This announcement had severe repercussions in the financial markets around the world. The next day Indian stock exchange opened 500 points low, Indian Rupee hits lifetime low of 59.9850, the debt market hit a lower circuit. These were huge after-effects and weren't one of those normal trading days' effects where things go bad and then get recovered. This situation wherein investors were caught unaware and there was a huge market sell-off, came to be known as the "taper tantrum." So, the investors are quite wary of the history repeating itself.

The second is the **Currency Effect**. It is the gain or loss on foreign investments due to changes in the exchange rate of the foreign currency compared to home currency. A rising foreign currency means foreign investments will result in lower returns when converted back to the home currency. The opposite is true for a declining foreign currency. This leads to currency volatility, which in turn leads to fear, which further leads to more volatility. Besides these two issues there are certain other questions which need to be answered so as to allay the investors' fear.

The Market's Reaction to Fed Actions

| Fed Announcement | Dates | Market Reaction |
|---|---|---|
| QE1 announced | 11/25/08-1/2/09 | +24% |
| Market anticipates QE1 end | 1/2/09-3/5/09 | -27% |
| QE1 extended | 3/5/09-3/31/10 | +79% |
| QE1 ends | 3/31/10-8/27/10 | -13% |
| Bernanke hints at QE2 | 8/27/10-6/30/11 | +21% |
| QE2 ends | 6/30/11-9/30/11 | -17% |
| Operation Twist announced | 9/30/11-4/30/12 | +30% |
| Mkt anticipates Twist's end | 4/30/12-6/5/12 | -9% |
| Operation Twist extended | 6/5/12-8/15/12 | +8% |
| QE3 announced | 8/15/12-present | +29% |

The third issue is that the QE's ending is not happening in isolation. The emerging world is also being buffeted by significant declines in the prices of commodities, including oil, base metals and food. The chart above shows the sharp slump in the commodity prices since the middle of 2014 and it shows a correlation between falling commodity prices and the appreciation in the US dollar. This correlation is not axiomatic, but it's prevalent mainly because commodities are generally priced in US dollar. So, when the dollar rises, buyers of commodity seek discounts from those selling, whatever the commodity may be (oil, iron ore, food etc.). This is particularly important because in this case the end of QE and the expectations of tighter monetary US policy to come is helping to drive the US dollar's appreciation. So, the weakening commodity prices is something that we may see for a while to come. Particularly, striking has been the slump in the price of oil with Brent Crude down 17% to around $86 a barrel from its price at the end of August. Obviously, this trend tends to hit commodity exporters such as Brazil, Russia and Chile. Conversely, it benefits commodity importers with India, Philippines, Thailand and Turkey in the latter category.




## Impact on Indian Economy

India is relatively well placed in the sense that we do not have a huge amount of hot money flowing into the market. Also, India has been able to manage its macro situation relatively well compared to other emerging economies. Growth is getting back and there is restoration in business sentiment and investment cycle. The Indian currency is stable against the US dollar. Although, the equity markets across the globe are taking a battering. But even then, India has actually performed better on both fronts – currencies and equities markets.

## CONCLUSION

Having said all this though, it's important to know that there are silver linings. The era of easy money is not suddenly coming to an abrupt halt. Japan maintains its program of monetary easing and the Euro zone has also moved in that direction too since the growth continues to disappoint. As commodity prices fall, so does the inflation, pretty much throughout the emerging world, setting the stage for monetary policies to remain accommodative in many of the emerging markets. The era of abundant liquidity is by no means over.

# EXPERTS SPEAK: TRACTOR INDIA PRIVATE LIMITED (TIPL)

## -BY MR. AYAN BANERJEE

## (GENERAL MANAGER-FINANCE)

**Team Infineeti: Mining as we know has undergone testing times in the past decade registering negative growth in many years. Construction and Power have faced their own set of challenges. As a company working in these sectors, do you think the recent economic turnaround has been able to benefit your industry as well and how do you see the growth prospects for a company working in these sectors?**

**Mr. Ayan:** The sector that I am working in goes through construction and also mining. The current situation or rather from the past five years had seen more of construction and a push for the mining sector as well. There has been a sentimental improvement. Of course in reality, especially in Asia, especially after recession, there has been an improvement of the people's psyche. As of now on count, there hasn't been much traction. The demand is moving up slowly. The economy is improving. The stage has been set ready. The Supreme Court's order of clearing the old coal blocks has to come into reality. We are waiting for big thing to happen. Internally a lot of changes have to happen. A lot of manufacturing and mining companies have cut down on their plans. They are trying to reduce their working capital costs.

**Team Infineeti: What are the main reasons for the downturn of the mining sector?**

**Mr. Ayan:** The main reason is because the government is holding back all the environmental clearances. The other problem with the industry is huge capacity but low demand. It became a viscous circle in a country like ours, where the government projects were stalled. Where as in countries like Australia, where there was push from the industry itself. That we have to come out of which I feel is a matter of time and it will soon be back and should come back in a period of about 18 months.

**Team Infineeti: Project appraisals play an important role in the expansion of any company. We've read textbooks describing NPV vs. IRR and a host of other methods as best for project appraisal. As an expert, could you guide us on how project appraisal is done in practice?**

**Mr. Ayan:** In a project appraisal which is going on for more than let's say two years, in such a case you would obviously like to keep the fixed assets higher and see what you are going to do over the period of time. Especially if you consider the mining project, the revenue generation is much more skewed, the costs which you incur now will be in the lower scale and the revenue and the cost gap is quite big. But when you are progressing down the line on the third year or fourth year, there are a lot many costs occurring in the form of project driven duty costs (in mining management). There are a number of software tools available for capital budgeting but these tools don't actually help much in assessing much about the project. What you need to do is, on the basis of the current budget you have to estimate the revenue growth, the costs incurred, and the uncertainty factors. NPV and IRR are fine from the perspective of a venture or a company's growth but at the same time you have to forecast future operating cash flows and most importantly return on capital employed for a period 3 or 4 years down the line. Because at the end of the day return on capital employed is what we are looking for. When you are looking for a long project where the capital investment is quite high, and we are looking at monetarily basis, it should not so happen that its invested very heavily on in the initial stage and then jump for some block later on.

**Team Infineeti: Another important aspect of expansion are M&As. could you tell us whether companies in your sector prefer organic growth or inorganic and why.**

**Mr. Ayan:** The core competency for a business lies in its basics where you know your risks and know how to go about it. I would rather say when the economy is not good and you are trying to come out of recession, with inflation in place, and a situation with more demand and less capacity of production, then its predominantly organic growth which I will prefer. Inorganic growth works out when the things are much more comfortable. It's a situation in which you are touching the roots of your area and going horizontally to other areas. So if you ask me, I will always go for organic growth at this stage where you can go for reduction of your capacity very carefully in line with the market. Because it should not so happen that you end up in a situation in the process of allocation that you expand your capacity and then end up in a situation where you cannot manage the demand. To answer you, first of all I would say it's the organic growth. I would supplement my answer by saying that question that needs to be asked is if you really need an acquisition or not. So at the end of the day you have to look into the basics of the company and see to it that you do things the better and the smarter way so as to have a healthy organic growth. Have proper entry of accounts into the books, good cash into the system, reduce unnecessary expenditure, and rationalize your costs. These are the fundamentals of operations which are to be looked into so as to have an organic growth.

**Team Infineeti: Can you throw some light on the inorganic growth which happens in your sector?**

**Mr. Ayan:** In mining and construction companies the increase is only organic. You will not see a construction company going for a retail of any consumer good. There are companies who have gone for IT like L&T but that is for their own consumption. Very few of them have gone into an area which is very intrinsic for their business. Therefore these companies are much more into their own business model.

**Team Infineeti: What are the challenges faced by an accountant in the industry you are working in?**

**Mr. Ayan:** The most important thing for an accountant is the keeping of books. So books and accounts in line with whatever is happening in business are to be maintained. The basic challenge which comes up is to show and reflect the proper book of accounts. That's a challenge and especially for the companies for which the system is still not in line with the new standards. So you often find a conflict between book keeping, interpretation of records and then managing it. For the proper interpretation to happen, the books of accounts have to be maintained in line with the business. Only then will it show the real impact and that's the basic issue and challenge faced by not just a GM but any accountant. Going back to basics helps the company by seeing whether proper practices have been laid down or not, properly accounted for or not, checked if there is any gap and if any, whether rectified or not. Unless you do that, the basic part and basic objective of the accounting is not met.

**Team Infineeti: India's convergence with IFRS was recently in news with (ICAI) stating that it aims to finalize the standards by December 2014. What impact do you see of the adoption of the standards? Are private companies also forthcoming in adopting these standards to avoid accounting hassles when they decide to go public?**

**Mr. Ayan:** Let's first talk about the Indian accounting standards, IFRS, and the US GAAP. The fundamentals of the accounting standards lie in the fact that the disclosure in the books of accounts is proper. The proposal to have a predominant accounting system after the period of recession is to regularize the accounting standards in a very pragmatic way. The available Indian accounting standards for revenue recognition or for foreign exchange accounts are enough to cater to the needs of what we have. International accounting standards is a form where a large sect of people can understand. It is not paramount to have international accounting standards so as to go international. The company needs to be international, and then you apply your accounting standards. Your accounting standards don't make the company international. The changes that you are referring to, the private companies are very much keen to do that but I am not very sure if they are ready to accept the philosophy of the international standards and imbibe it into the company or not. That is something for the company management to decide. And obviously the motive to adopt the international accounting standard is there. It's got quite an impact on the company like ours which has got quite a big assets base. Intention is very much there but before that the company's internal basic structural intention has to be firmly inclined. A company applies for international standards only when it is trying to listed on NASDAQ or NYSE. If your intention is only that, then these accounting standards don't help you much. What I am trying to say is that from the internal structure itself the company has to make its standards.

**Team Infineeti: Can you explain in detail what would be the initial hassles faced by the private companies on shifting towards the new accounting standards?**

**Mr. Ayan:** The real challenge is to maintain the asset register properly.

For example, for the impairment of assets, you have to consider not only the depreciation, but also the value of the assets as of today, considering how much time has been passed and the market value of the particular assets today. To do that, you have to recognize all of your assets and record that into your assets register properly. So that it is identifiable and you have a system in place where you have appraised the market prices of all of these assets. Unless you do that how will you ascertain the market value of the assets. So it is based on your assumption that your asset register is properly maintained. With most of the Indian conventional companies who are properly maintained you will find their asset register is not properly maintained. Either their inventories are not properly segregated or they not identified or there are adjustments which are to be taken care of.

**Team Infineeti: What is the main reason or obstacle which prevents these companies from maintaining proper records?**

**Mr. Ayan:** In Indian industry today, you will have a mix. Previously, the annual accounts which had to be maintained used to have a big register where all the assets registered had a tag number. Then had come in the computerized system and this move is not so easy. This had to be done by physically accounting your assets. The migration from previous legacy to new accounting system has to be proper. If it's not proper then there comes a leakage in place. On that basis if you do impairment it will not be correct. That is creating a problem for the medium sized companies. The small sized and the large sized companies have managed it but for the medium sized companies, it has always been a problem. The challenge lies in the lack of means and in few cases, in the lack of intention. Lack of means implies that it has to be more scientific and gradual while moving from our legacy to the computerized system. The fore sightedness of a company to move into this platform is lacking and is hence creating a problem. In my experience, in all these areas of fixed assets, valuation of inventory, these are contentious issues in accounts. This requires, from the accounting side, a strong will to do it the right way. If accept it the way it is and start comprising, the gap will start widening with time to come. We should have a very strong checking mechanism in place from whereby these gaps are minimized day after day. It's not a question of time. It depends on the company, what its objective is and what it wants to resolve in the process. So unless you do that, this will take a very long time to get it resolved.

**Team Infineeti: How disciplined or strict are the standards followed in the mining or construction sector?**

**Mr. Ayan:** They are very strict. Most of the engineering companies, which are in this sector like the ones in infrastructure and construction business, follow a very strong and robust accounting system. It's not just the economic situation but time which is the biggest variability of the project. Hence these companies cannot afford to be loose in the accounting standards. The working capital management in this industry is of very high priority. The costs incurred are very high. In case of a service sector, the working capital is just the debts. But in case of engineering companies, the working capital is debts, inventories, few receivables. It is in the interest of the company to have the accounting standards strong and solid to identify, protect and control the problems so that the holding costs come down. So proper software packages have to be in place so as have a proper visibility of the working capital management.

**Team Infineeti: Another important decision a company has to make is whether to go public and when. In your view, what are the factors a company should consider while making such decisions?**

**Mr. Ayan:** It depends upon fund mobilization and comes from within. When does a company go public? It goes when it requires a bigger involvement. It's a fundamental of the company to raise the economic multiplier. If the company's sole aim is to create money by getting money from the public and internalize it, then you have a problem of Ponzi schemes coming into picture But if the company's fundamental is to create an economic multiplier and therefore give it back to the society then comes the question of raising money from the public and bringing the public into the portfolio. Hence I would say it is more of economic rather than just basic objective of the company. If the company's objective is to cater to a very niche section then the company need not go public. Because money is not a problem as there is enough wealth in the world. Hence when the company goes public, the company is working towards having a greater economic multiplier and create a much better economic yield. The other things that a company would look into before going public would be a few financial ratios like debt equity ratio. Going to the public to my mind is much more an objective of a company rather than economics of the company which becomes secondary.

**Team Infineeti: What do you feel the government can do in order to boost your industry?** Are there pending decisions from the government that the industry is looking forward to?

**Mr. Ayan:** GST implementation is something which is looking forward to. Any company for which the work involves moving of goods from place to another, this involves form c. Even the nuances of the local sales taxes create a lot of problems. Hence the implementation of GST becomes the call of the day. From my perspective, I would rather rely on the decisions taken by the RBI than those of the government's. Interest rate cut is the call of the day as per me. But I would rather leave the decision to the RBI and the government as they are the right institutions to come up with a decision. But I would rather depend on RBI than the government as the decision should not be politically motivated.

**Team Infineeti: How would the implementation of GST help your industry as a whole?**

**Mr. Ayan:** The optimism that we have is that GST will come into place and it will have a positive impact on the industry. There is a huge administrative cost for the compliance of indirect taxation for the company. It has to reduce. Worldwide it has reduced. So there is a pressure from outside as well as demand from inside that will reduce our tax compliance administration costs. That's the only way. State wise you have a different rate of tax for different commodities, and along with that there are various nuances for compliance. So if you want to eradicate those then it is very important that you have a common general tax structure which is also a VATable. May be we are looking for a GST which is common for the states but not common for the commodities. So there are products which are out of the GST like petroleum where states have their own leverage. The sooner it happens, the better for us.

**Team Infineeti: Has deregulation of diesel prices attracted any kind of investment into your industry?**

**Mr. Ayan:** Deregulation of prices has started sometime back which has surely helped. But not always does it help to be honest especially in the finance sector where you are protected by very strong RBI regulations. These regulations are helpful both for the depositors and the industries as well. But the general deregulation measures especially on the taxes and policies point of view turns out to be helpful.

**Team Infineeti: With any change in the government policy, how long does it take to show an effect on your business?**

**Mr. Ayan:** In a manufacturing and a mining industry it takes a long time. It takes nearly a year and a half but depends on the type of the project as well. There is no standard norm. If you are into building roads or or dams, it takes a long time but if you are in a housing sector, things are much direct depending upon the policies undertaken. In those cases the impact is much more visible. In our sector as of now there hasn't been much of a change but by at least the next annual budget of 2016, we should be expecting a radical change.

**Team Infineeti: What stands the main reason for the profits before tax of TIPL to show a huge jump from Rs. 4 Crore last year to Rs. 11 Crore this year?**

**Mr. Ayan:** I would not go into the details. But can say that any profit that is 10% of its total revenue, then you should consider looking at the balance sheet but not the real profit. That is the thumb rule of an accountant. But the overall industry went to a back phase last year. It had a very high foreign exchange fluctuation which had touched 68. So that affected the industry heavily with low demand in the market which impacted the industry heavily.

**Team Infineeti: How long does it take in your industry to breakeven?**

**Mr. Ayan:** Any conventional BEP has to be within three years. Anything which is going beyond three years is termed risky. It becomes critical. There a number of projects in the company itself which are taking more than 5 years to get completed. The performance based contract is going into 5 – 7 years. These are very critical where sensitivity of costs overrun as well as performance is very important. To manage those kinds of projects, we require a special kind of software, special kind of a visibility and an attention to detail. The performance, control and monitoring becomes important.

**Team Infineeti: During a slowdown, how does your company manage its finances?**

**Mr. Ayan:** Slowdown is difficult to manage. In engineering project companies, it is very difficult to cut down costs because costs are very intrinsic to its nature. You cannot lay off people because in a project the people's capital is very vital as they know the processes. And it takes ages to get the kind of manpower who knows the internal processes hence it's very difficult to replace manpower. It's tough but what you need to do is to go into a shell where you cut down your unnecessary costs, reduce your operating expenses but you hardly touch manpower. You might ask your people to go for a study leave or on a vacation but you cannot retrench people in this situation. So the basic way of doing things whether you are in a good shape or a bad shape is to use flaps, reduce costs though the very sustainability in this kind of an industry is always having a strong scrutiny of your cost price so that you become cost agile.


# *Cover Story: Fundraising in ecommerce Companies of India*

## *How do the ecommerce companies raise money in spite of being in losses?*

## *Is this just a bubble?*

# FUNDRAISING IN ECOMMERCE COMPANIES OF INDIA

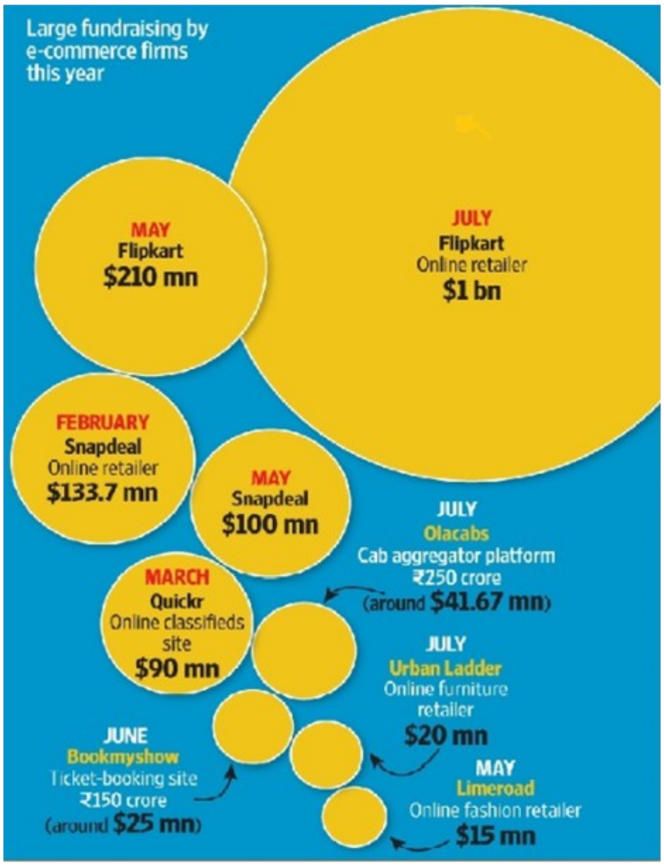
-BY PARTH POTDAR & KUMAR GAURAV
IIFT, KOLKATA

## INTRODUCTION

E-commerce sector in India is quite unconventional and it raises more questions than it answers. The **cost of customer acquisition** is high, **conversion** is low and **return of products** are high due to cash on delivery. The question then is whether the business is really profitable. If not, then why are people investing in the sector. As G.T. Smith has rightly said *"Donors don't give to institutions, they invest in ideas and people in whom they believe".* Fundraising in e-commerce has been in the news for quite some time and every other day we hear a company raising millions of dollars. What do investors look for? How much time are they willing to give to a business? Do they have an exit policy? Let us try and understand how fund raising works in E commerce.

The 2 major ecommerce players **Myntra** and **Flipkart** in India have raised funds in different ways. Flipkart has raised over **540mn USD** in over 6 years where as Myntra has raised only **75mn USD** and their investors are more or less the same. But the fundamental question here is ***why do ecommerce companies need so much money?*** The ecommerce industry is growing exponentially and if a player is not growing at the same pace then he is out of the competition. The money is needed to keep on improving i.e. to better the distribution, the technology and enhance their existing business model. A huge chunk of the money is needed to fend off the big players entering the market for e.g. Flipkart needs the money to compete with Amazon which has deep pockets.

Now let us look at the other side of the coin, why do venture capitalists invest in startups, and how risky is the project. As the ecommerce sector in India is booming and **internet penetration** is only increasing in the country this is a lucrative opportunity. Rapid growth **in sales** and **high valuations** in the market allow the investor to exit later through an **acquisition** or an **IPO**. **Accel India** has raised **250mn USD** in its latest round of VC funding and has investments in **Flipkart**, **Bookmyshow** and **Taxiforsure**.



## WHAT HAPPENED WITH ALIBABA?

Russian billionaire **Alisher Usmanov** was an investor in Ali Baba prior to the IPO. He told CNBC that his investment increased by 500%. This kind of exponential gain is impossible to achieve in any other kind of investment.

In 2005 **Yahoo** paid **1bn USD** for 40% stake in **Alibaba** and it also merged its China based subsidiaries into Alibaba. Following the IPO, Yahoo retained 383 million shares of Alibaba which is around 15% stake in the company. It made 9.4bn USD out of it and Yahoo CEO Marissa Mayer is planning to use the money to repurchase shares of Yahoo and increase the stock price. Other investors in Ali Baba like the Softbank's founder Masayoshi Son became the richest man in Japan at least on paper.

So we can say that investing in startups are **high risk high return investments**, but venture capitalists don't just invest in one company i.e. they don't put all their eggs in one basket. **Tiger Global management** has **105 investments** in **37 companies** and has had **8 exits**, 3 through IPOs and 5 through acquisitions.

### PROCESS OF FUND RAISING

Companies use 2 main strategies when raising funds. There is no right or wrong strategy. It depends on each company and the business situation

- **Raise as much as possible as soon as possible:**

  Here the aim is to grow and expand and not wait for revenue to grow. This is mainly used when the company wants to cash in on the first **mover advantage** and capture the market. The downside to this method is that the **ownership is diluted** and the growth may or may not be sustainable as the growth is on investors' money and not on customers' money.

- **Raise as little as possible as late as possible**

  Here the company aims to achieve sustainable growth; they want **healthy revenues** and growth using the customers' money. So when you rise the **ownership is not diluted by much** and when the business grows the company will get a lion's share of the profits.

In the ecommerce sector the growth of the company needs to be rapid as the sector is growing very fast so all the companies go for the ***raise as much as possible as soon as possible***. So it is safe to say that the ecommerce sector is growing on the investors' money.

Venture capitalists use a basic criteria to decide whether to invest or not in a particular firm.

- Business Momentum
- Management Team
- High growth potential
- Future profitability

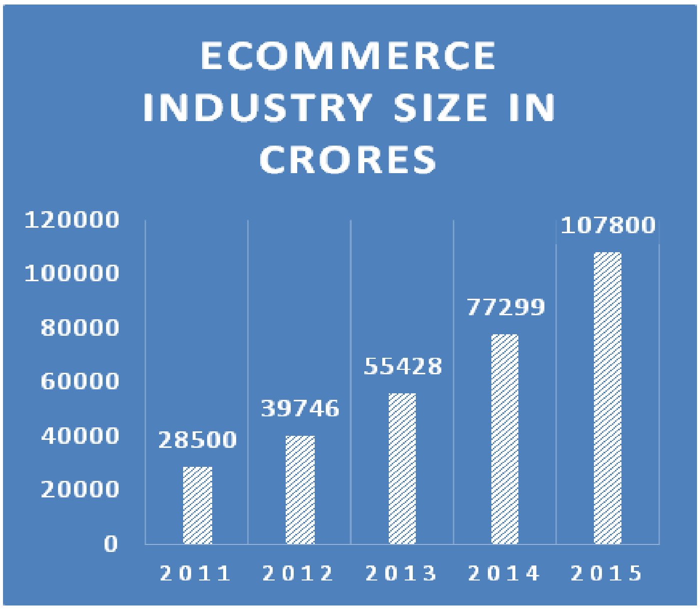
Out of these criteria the 2$^{nd}$ one is the most important. VCs get directly involved with the companies in which they are investing and the attitude of the management team makes a difference. When Accel partners-India invested in Flipkart they were very impressed by Sachin and Binny Bansal and they believed in their idea and their potential.

### Risks involved

The future of the company depends on the Investor relationship. The investor may have to ditch the company due to their bad financial planning or because the may get themselves into a tight situation due to which they may have to cut the funding.

There may be a change in the investor's top management and they may decide that investing in a company is a bad idea. Or to exit on their position they may pressurize the company to merge with any other company or sell the company even though that may not be beneficial in the long term interest of the company.

Looking at the risks it may seem like using investors' money should be the last resort but it also has many perks. You get money to expand when you need it, you don't have to worry about your **working capital** requirements and you will always have funds to implement your ideas.




## WHERE IS THIS HEADED?

Why are all the e commerce sites raising money when none of them is profitable? What is the end game here? According to leading industry experts all the players in the e commerce sector are busy establishing dominance. They want to increase their customer base to such an extent that all the other players are driven out of the market. Everyone wants to be the *last man standing* in the sector but is this even possible. Economics teaches us that **monopoly is not very good for the customer** as it restricts the choices. But is ***converting a perfect competition into monopoly* even possible?**

According to **KPMG report** ecommerce **industry** has **grown** by more than **150%** in the last 3 years. External factors such as increasing **urban households**, **increasing internet** and **smart phone penetration** in rural areas are causing a growth in the industry. These factors are increasing the customer base for e commerce companies fueling investment.

## FUNDING BASED ON VALUATION

How is a private company valued? There are no market multiples available and fundamental valuation does not take into account the market sentiments, so it will not

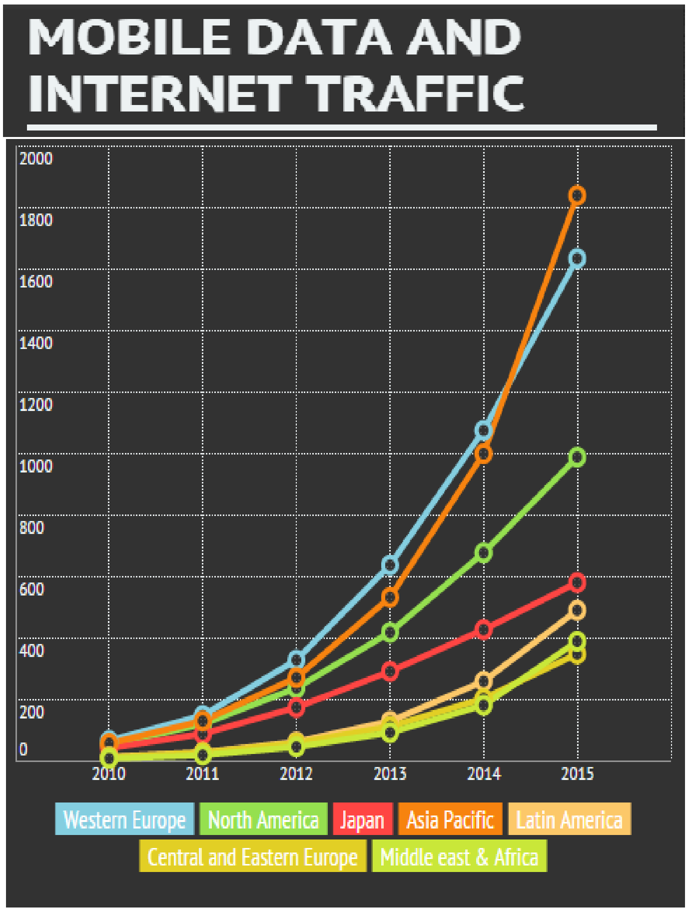
**TOP INVESTORS AS ON DECEMBER 2014**

| RANK | COMPANY | # OF DEALS | SUM OF AMOUNT |
|---|---|---|---|
| 1st | Sequoia Capital | 8 | $212,999,999 |
| 2nd | Accel Partners | 7 | $228,621,000 |
| 3rd | Khosla Ventures | 5 | $123,500,000 |
| 4th | GGV Capital | 5 | $123,000,000 |
| 5th | Metamorphic Ventures Llc | 5 | $12,800,000 |
| 6th | Softbank | 4 | $352,000,000 |
| 7th | Madrona Venture Group | 4 | $55,750,000 |
| 8th | Matrix Partners | 4 | $48,000,000 |
| 9th | True Ventures | 4 | $35,500,000 |
| 10th | Northzone | 4 | $25,200,000 |

Source: whogotfunded.com

lead to an accurate figure. Ever wondered how did **Flipkart** achieve a **valuation of $7bn** even though it is still making losses. It is done on the basis of expectations of profits tomorrow. Latest funding plays a major factor in valuation of a private company, after Flipkart confirmed that it raised **$1bn** through **private equity funding** it determined that it has value in the sector.

Revenues are taken into consideration while valuing a private company, even though a company may be making losses but if the revenues are growing it implies increasing demand for the products of that company. Flipkart reported revenues of 6000cr INR in 2013-2014 from 205cr INR in 2011-2012. This **exponential growth in sales** indicates the demand for goods from Flipkart. If a company has a high valuation then when the company goes for an IPO the stock will open at a higher price increasing the value of the investors.




| | Amount (usd) | Investors |
|---|---|---|
| Myntra.com | 45000000 | Accel - Tiger Global |
| Quikr India Pvt Ltd | 122000000 | Ebay Matrix Norwest Warburg Pincus Kinnevik |
| Zomato | 107000000 | Info Edge, Sequoia Capital |
| Snapdeal | 358800000 | Bessemer Blackrock Temasek and more |
| Hike | 86000000 | Bsb |
| Bookmyshow | 25000000 | Accel Partners, Network18, SAIF Partners |
| Flipkart | 3343150000 | Accel Naspers Iconiq Tiger Global Morgan Stanley & more |

## CONCLUSION

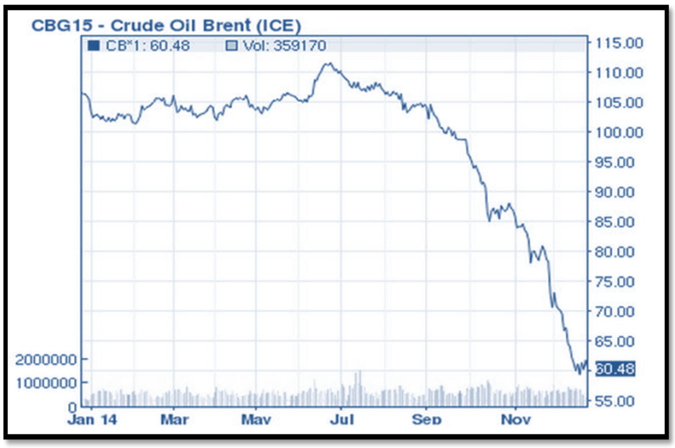
Fundraising is not as difficult as it used to be. If the idea is good with a business model in place and a reasonable consumer base then funds will come to you. You can receive a **fund** of **25lakhs-2crores** from **NASSCOM** itself under its **10000 start ups initiative** if there is a working prototype and customers love the product/service. At this point of time, e-commerce is in the growth stage, hence we are looking at this kind of VC and PE funding but when the industry reaches its maturity stage around 5-7 years from now, we will see a boom of IPOs and less of Venture capitalists and Private equity in e-commerce.

# FALL IN CRUDE PRICES:
# REPERCUSSIONS FOR INDIA

-BY GUDIMETLA SANDEEP
IIM, LUCKNOW

## INTRODUCTION

Oil is so much more than a fuel. It's a weapon and a strategic asset for political players. It's a maker of fortunes and a leading indicator of the global economic outlook. It's also




called as the resource curse, a term made popular by the British economist Richard Auty.

No wonder, when the price of such an important asset declined by more than 45% in the year 2014 alone, it hogged the limelight in the global economic front. It has almost dragged Russia to the brink of currency crisis in early December 2014 and has also made OPEC irrelevant for the first time in the collective memory of this generation.

Supply disruptions amid global tensions in the Middle East during this year were expected to lead to an increase in the crude oil prices. However, an unexpected trend of decline in the oil prices caught everyone off guard.

## REPERCUSSIONS FOR INDIA

Before understanding the nature of the impact of oil price slump on Indian economy, it is better to understand the extent of India's dependency for oil imports.

### Import dependency

India was the fourth largest consumer of crude oil and petroleum products in the world, after the United States, China and Japan in the year 2013. It depends heavily on imported crude oil, mostly from the Middle East. The petroleum imports account for 77% of its oil requirements and for 1/3rd of its gross imports. Figure 2 shows the extent of India's import dependency. It also shows the vulnerability of India to changes in the global oil prices.

Having understood the criticality of India's import dependency, let us understand the repercussions of the recent unexpected decline in the global oil prices on India

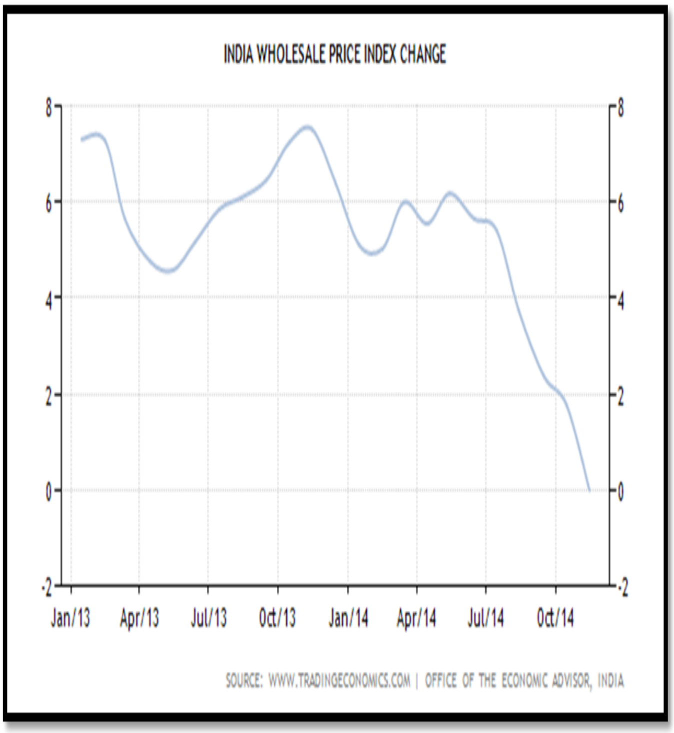
### Lower Inflation

In India, inflation is measured using Wholesale prices (WPI) and also using retail prices (CPI). Given the higher share of tradable goods in WPI basket, the impact of lower oil prices is more on WPI than on CPI. Crude petroleum and fuels excluding Kerosene and LPG constitute 8.6% of the WPI basket. So, lower oil price directly impacts 8.6% of WPI basket and around 5% indirectly through lower price of crude derivatives such as chemicals. As per Nomura estimates, every $10 decline in crude oil price results in a

| | Petroleum & Natural Gas Sector | Unit/Base | 2013-14 (P) | November | | April-November | |
|---|---|---|---|---|---|---|---|
| | | | | 2013 | 2014 (P) | 2013 | 2014 (P) |
| 1 | Crude Oil Production In India | MMT | 37.8 | 3.1 | 3.1 | 25.2 | 25.0 |
| 2 | Consumption of Petroleum Products | MMT | 158.4 | 13.3 | 13.9 | 104.2 | 108.0 |
| 3 | Production of Petroleum Products | MMT | 220.2 | 17.5 | 18.9 | 146 | 145.6 |
| 4 | Imports & Exports: | | | | | | |
| | Crude Oil Imports | $ Billion | 142.9 | 11.2 | 8.8 | 95.4 | 89.3 |
| | Petroleum Products (POL) Imports | $ Billion | 12.3 | 0.8 | 0.9 | 7.5 | 8.8 |
| | Gross Petroleum Imports (Crude + POL) | $ Billion | 155.2 | 12.0 | 9.7 | 103.0 | 98.1 |
| | Petroleum Products Exports | $ Billion | 60.7 | 4.7 | 4.6 | 41.0 | 37.3 |
| 5 | Petroleum Imports as % of India's Gross Imports | % | 34.4 | 35.5 | 22.6 | 34.1 | 31.3 |
| 6 | Petroleum Exports as % of India's Gross Exports | % | 19.4 | 19.4 | 17.7 | 20.0 | 17.3 |
| 7 | Import Dependency (Based on Consumption) | % | 77.6% | 77.4% | 78.0% | 77.3% | 78.1% |

decline of WPI by 0.5 % and CPI by 0.2 %.

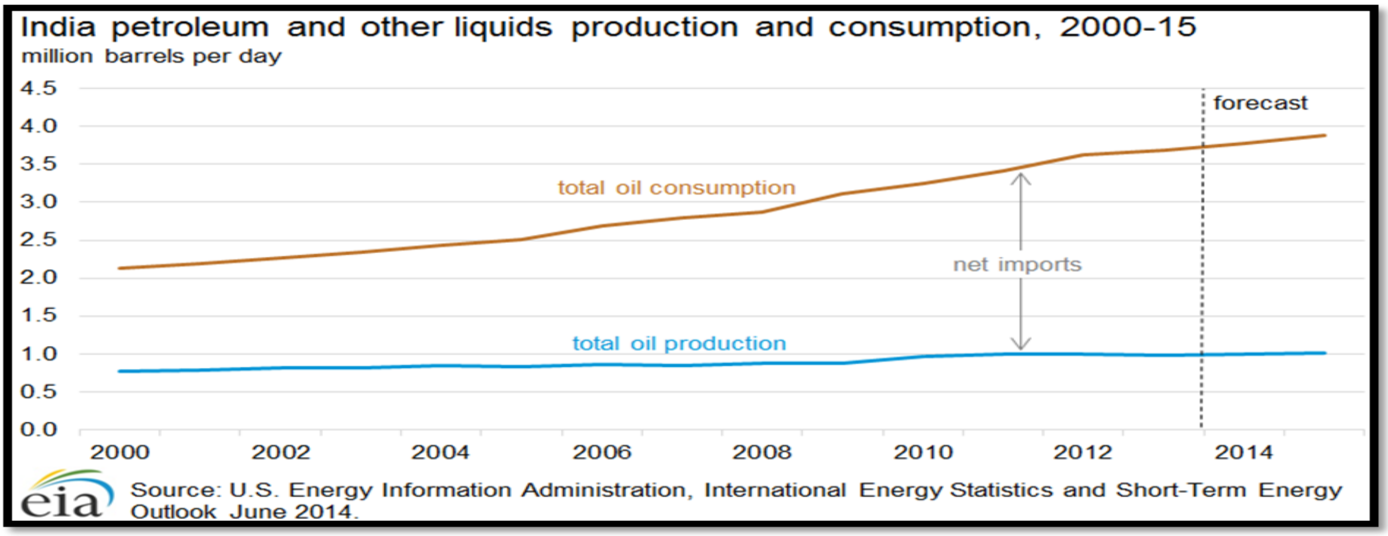
It is evident from the following figure that the trend of inflation due to lower oil prices has been only south in the last few quarters.

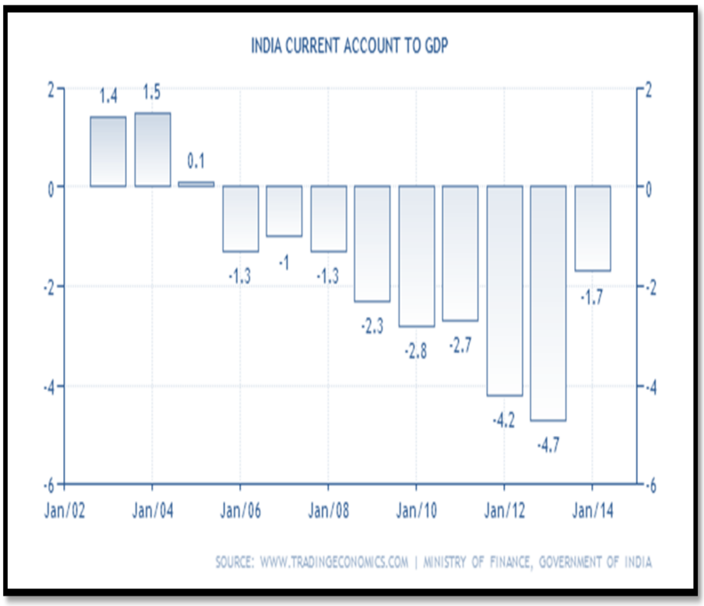


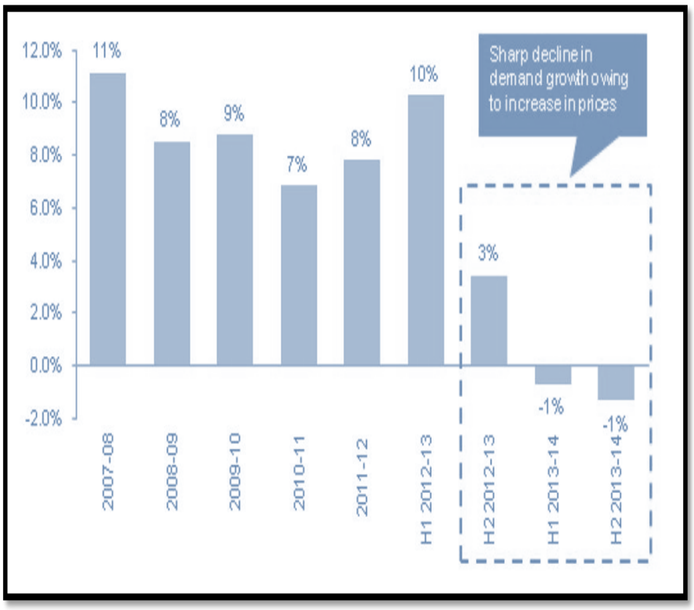

**Lower Current Account Deficit (CAD) and fiscal deficit**

The current account deficit of India has declined to 5-year low of 1.7% of GDP in the year 2014 on account of the controls on gold imports and timely intervention by the central bank of India by selling forex reserves to prop up the rupee. This is expected to continue in the coming year due to lower oil prices. Every $1 per barrel decline in crude oil price decreases import bill by Rs.8345 cr ($1.38 bn).

Similarly, every $10 per barrel fall in crude oil price im-






proves India's annual current account balance by around USD 9 billion or 0.5 percent of GDP, according to Macquarie.

**Lower subsidy burden**

The deregulation of diesel by the government of India benefits all the stakeholders - the government, OMCs and upstream companies. Earlier, the consumers were protected by the subsidies against an increase in the oil price. Now, the deregulation curbs the wasteful consumption of diesel and it will also increase the competition in the marketing segment. Thus diesel demand will adjust to prices.

The following figure shows the decline in the demand growth post the implementation of deregulation of bulk diesel in January 2013 and the subsequent increase of the retail prices by 50p/month.

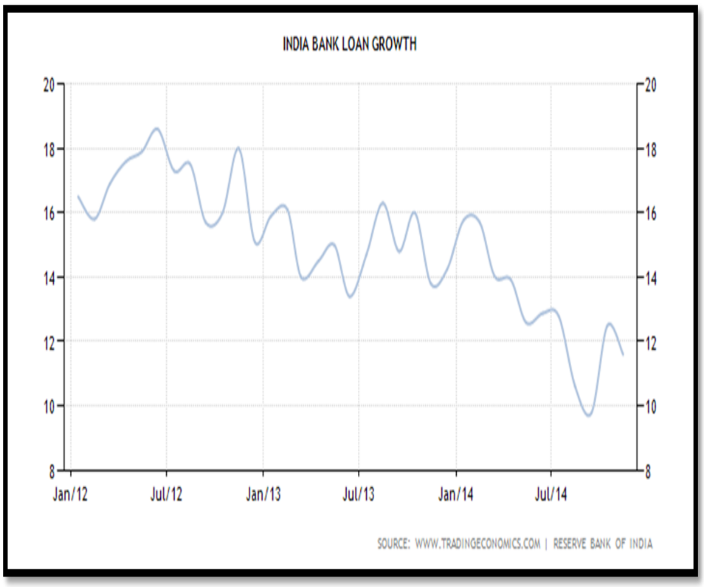
Going forward, diesel usage efficiencies will improve and demand will increase by only 4-5% over the next 2-3 years- compared to 8-10 % seen in the past- as economic activity picks up.

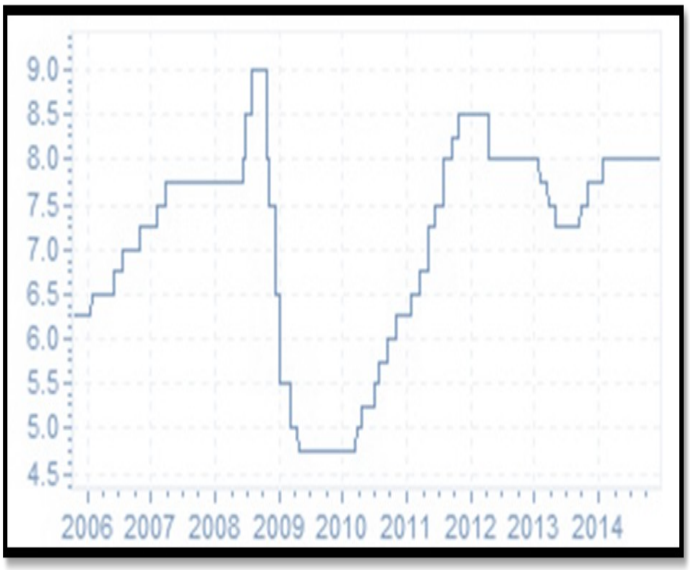
**Higher GDP**

The preceding points make a case for growth in GDP of India. It usually happens through multiple channels

- Lower inflation will increase the household's real disposable income and push the consumer discretionary demand.
- Lower oil prices also result in lower input costs for many companies, especially raw material intensive companies in India. The improved profit margins due to the lower input costs will act as a tail wind in increasing the business sentiment and thereby increase willingness for investments in India. The abysmal business sentiment is evident from the lower credit growth seen in the last few years. It recently touched 9% which was the least since the government started collecting data about credit growth in India. So, lower oil prices will undoubtedly result in the credit growth take off in India.
- Improvement in inflation and twin deficits would give space for Reserve Bank of India to ease interest rates. High interest rates have been the main culprit for the low credit growth in India in the last few years.

According to Nomura, Every $10/ barrel fall in crude oil price boosts GDP growth by 0.1% or 1 basis point .




**Likelihood of lower capital inflows**

Not everything is hunky-dory with the unexpected lower oil prices. Indian markets are much more globally linked than the Indian economy.

In early November 2014, BNP Paribas came out with a research report in which it had stated that the energy exporting countries are set out to pull out the 'petrodollars' from the world markets for the first time in 18 years.

For years, huge profits made by the oil exporting countries found their way into the global capital markets adding to the global liquidity. Sovereign wealth funds of oil rich nations have been the major FIIs for many countries. In mid-2013, post the sudden decline in Indian rupee, the exhortations made by the then finance minister P. Chidambaram to the sovereign wealth funds of the west Asian countries to look at Indian investments makes a strong case for the dependency of India on these capital flows. As surpluses with the capital exporting countries (oil producers) are eroded, they would have less capital to invest abroad and capital flows could get constrained for India.

In case, they pull out their capital from the capital markets it will put pressure on Indian markets and the Indian rupee. This scenario has to be viewed in conjunction with the likelihood of increase in the US interest rates which will only strengthen the already robust dollar. The occasional steep corrections in the month of December validate this argument.

India has seen record inflows of over $40 billion into debt and equity markets this year. It could halve to $18-20 billion next year on slow down in the sovereign wealth funds. This is because of the fact that the recent QIPs and foreign currency bond issues have seen heavy interest from the investors in West Asia, according to a Credit Suisse report.

More than 50% of the CNX Nifty revenues are globally linked and any disorderly correction in global markets impacts many sectors and materials in particular. The Indian broader equity markets may also take a hit as they are strongly correlated with the global markets.

**CONCLUSION**:

The lower crude oil price in the second half of the year 2014 has been a shot in the arm for the business sentiment in India which are already buoyed by the stable regime at the centre in the recently concluded elections. There is little doubt that the lower oil price will benefit


India, which depends on imports for its oil requirements. The accrued benefits will help rein in the stubbornly high inflation and the twin deficits of CAD and fiscal deficits. The recent diesel de-regulation has reduced the subsidy burden considerably and it will likely help in keeping the Indian rupee strong. All these factors make a strong case for achieving 6%+ growth in the coming year.

However, the dependence of Indian markets on FII flows makes it vulnerable in case they pull out their investments which may happen because of a rise in the US interest rates in the coming year. Such a pull out may put pressure on Indian rupee and may also result in steep correction in Indian stock market. It may directly affect the business sentiment across businesses in India.

So, even as the benefits of lower oil prices on the government finances and to an extent on inflation are celebrated , it may be worth keeping a wary eye out for new risks that may emerge in the next few months.

# NEWS CHRONICLE

## MICROMAX INFORMATICS SOON TO DIAL DALAL STREET FOR RS 3,100-CRORE IPO

Micromax Informatics, one of India's top mobile phone makers, has begun short-listing investment bankers to manage an initial public offer to raise as much as $500 million (Rs 3,170 Crore) in the domestic market by diluting a minority stake in the next financial year starting April.

## RBI UNEXPECTEDLY CUTS INTEREST RATES

Home and auto loans will become cheaper as the Governor Raghuram Rajan-led Reserve Bank of India (RBI) changed the policy rate after keeping it unchanged for the fifth time in a row. RBI had hinted at softening its stance “early next year” in 2015 if inflation continued to abate and there was an improvement in fiscal health.

The decision to change the short term lending (repo) rate to 7.75 per cent was welcomed by the industry which said RBI Governor Raghuram Rajan had been accommodating this time around to help prop up the sagging economy.

## GOVT. APPROVES ORDINANCE TO EASE LAND ACQUISITION ACT TO PUSH REFORMS

The government approved an ordinance to amend the Land Acquisition Act to remove barriers in a range of sectors like power, housing and defense to kick-start stalled projects. At a news briefing, finance minister Mr. Arun Jaitley said the five areas were clearance for land for defense purposes, rural infrastructure, affordable housing and housing projects for poor, industrial corridors, and infrastructure or social infrastructure projects, including those in public-private projects in which ownership of land will remain with the government.

## FM TABLES GST CONSTITUTIONAL AMENDMENT BILL IN LOK SABHA


After months of dilly-dallying the finance minister Arun Jaitley tabled the GST Constitutional Amendment Bill in the lower house of Parliament. Speaking in the Lok Sabha, the FM said the government has made sure that no state

NEWS CHRONICLE

will lose money and it will be a win-win tax reform for both the Centre and the state governments. Assuaging fears of state governments, Jaitley said the government will compensate the losses incurred by them for the initial five years. "GST will ensure seamless transfer of goods and services, absence of Inspector Raj and no tax on tax," Jaitley told reporters soon after tabling the 122nd Constitution Amendment Bill in the Lok Sabha.

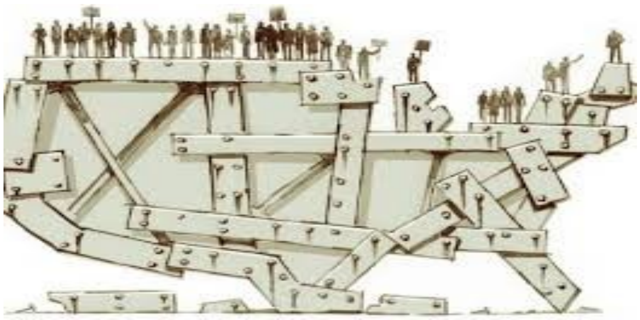
**INDIAN ECONOMY STARES AT DEFLATION AS INFLATION HITS ZERO IN NOVEMBER**

India's economy may be staring at deflation, at least statistically, a condition where prices come down below their level a year ago with inflation rate turning negative, taking away pricing power from companies, eroding their profit, and forcing them to lay off employees. The situation arose with the wholesale price inflation rate turning zero in November, meaning overall prices didn't rise from their level a year ago. In October, WPI (Wholesale Price Index) inflation was 1.77%.

**FISCAL DEFICIT REACHES 99% OF BUDGET ESTIMATES**

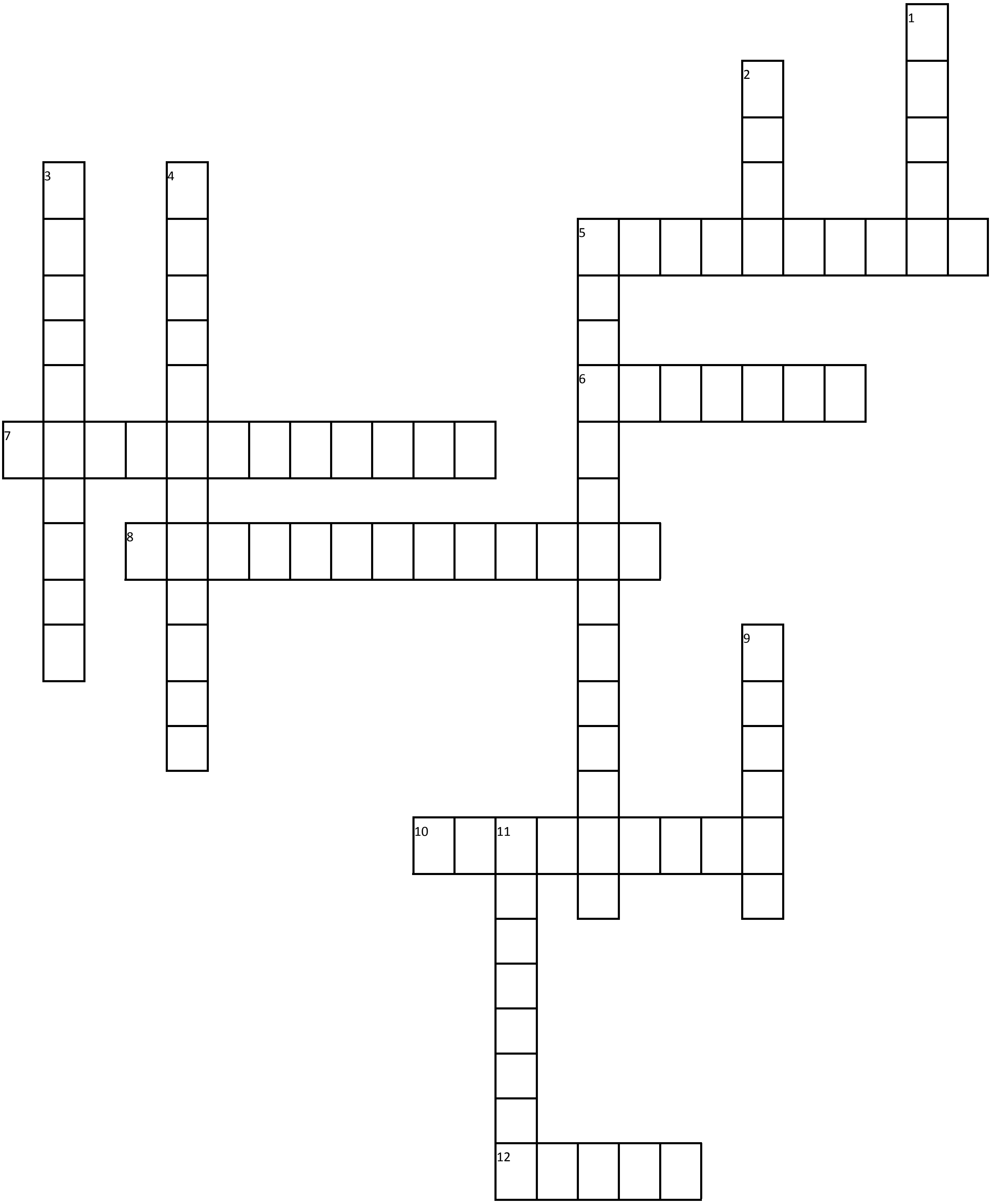
The government's fiscal deficit for April-November, the first eight months of the current financial year ending March 2015, touched 98.9 per cent, or Rs 5.08 lakh crore, of the Budget estimate. The fiscal deficit in 2014-15 is estimated to be at Rs 5.31 lakh crore or 4.1 per cent of the GDP. The fiscal deficit had stood at 93.9 per cent of the Budget estimates in April-November of 2013-14 fiscal

**THIRD-QUARTER U.S. ECONOMIC GROWTH STRONGEST IN 11 YEARS**



The U.S. economy grew at a 5.0 percent clip in the third quarter, its quickest pace in 11 years and the strongest sign yet that growth has decisively shifted into higher gear. Some of the strength appears to have been sustained, with other data showing consumer spending rising solidly in November 2014, offsetting surprisingly weak durable goods orders. The reports further set the U.S. economy apart from the rest of the world, where growth is sputtering or activity shrinking.

# FIN CROSS



# FIN CROSS

**Across**

**5.** Founded Pratichi trust with his prize money

**6.** Derived from 'Oikonomia' meaning 'House Management'

**7.** 'Thundering Herd' of Financial World

**8.** 'The Oracle of Omaha'

**10.** This option allows underwriters to buy an additional percentage of shares at offering price of an IPO

**12.** Fund earmarked for a loosely defined, but legitimate, purpose that is instead surreptitiously used for an illegitimate purpose

**Down**

**1.** Currency of Russia

**2.** Currency that a government has declared to be legal tender, but is not backed by a physical commodity

**3.** One of the founders of Wall Street Journal

**4.** Depreciating an intangible asset

**5.** Buying a company just to sell its Assets

**9.** Derived from the French word Bougette or 'Little Bag'

**11.** 'E' in CAMEL- System of ratings used by banks

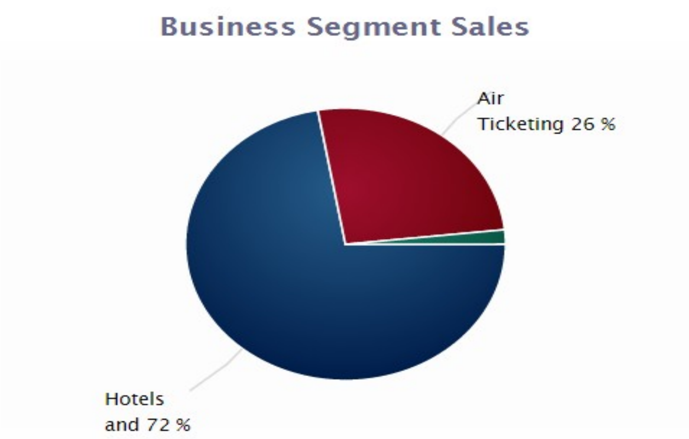
For solutions, check Page No. 44

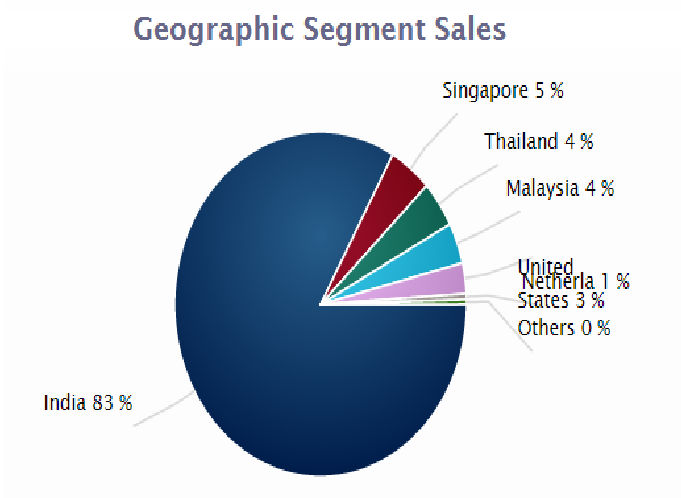
# EQUITY RESEARCH REPORT ON MAKEMYTRIP.COM

-BY GAYATHRI BHUVANAGIRI

## MAKEMYTRIP COMPANY SUMMARY:

MakeMyTrip Limited is an online travel portal which provides travel products and solutions both in India and worldwide. The services and the products of the company include air tickets, bus tickets, car hire, customized holiday packages, hotel bookings. It provides other ancillary travel requirements which include facilitating access to travel insurance and Visa processing. MakeMyTrip Limited is the parent company of MakeMyTrip India (Private) Limited. The company operates on the following websites of makemytrip.com, easytobook.com, hoteltravel.com, makemytrip.ae, makemytrip.ca, makemytrip.com.sg. The company allows the travelers to firstly research, then plan, book, and purchase a range of travel services and products through the above websites, and other technology enhanced distribution channels which include travel stores, call centers, travel agents' network, and mobile services platform. It serves leisure travelers and small businesses as well. The company was founded in the year 2000 and has its headquarters situated at Gurgaon, Delhi. It is listed on the U.S stock exchange.




**Where does MakeMyTrip earn most of its revenues from?**

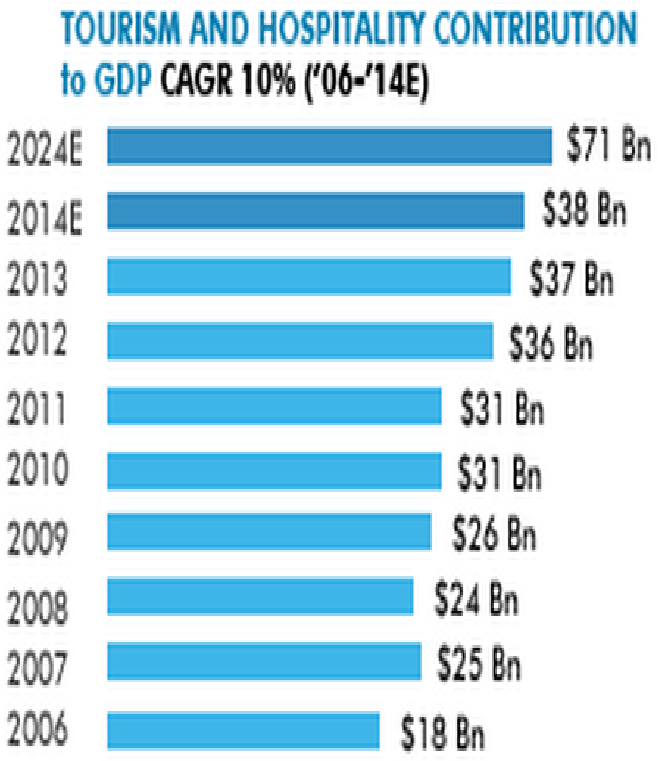
The company generates most of its revenues from the bookings of airlines operating in India such as Go Air, Indigo, Spice Jet, Jet Airways and Indian Airlines. But owing to the tough phase the Indian airways is going through which has led to the reduction of prices of air tickets, the company recently has been trying to concentrate more on hotel bookings and holiday packages which tend to have higher margins than airline bookings .

## TRAVEL AND TOURISM SECTOR IN INDIA:

The fluctuating exchange rates have helped in increasing the inbound tourism as this contributed to strong growth of arrivals. Airline industry has got a much needed boost. In spite of the difficulties faced by the airline industry, there comes a ray of hope with the increase in the new entrants namely, Air Costa, TATA SIA Airlines Ltd, and AirAsia India Private Ltd. The above has resulted into a much needed boost with the return of large number of customers due to the reduction of prices of air tickets.

Hotels and Packages have become a booming segment. Hotel bookings also recorded a strong growth in the previous year. The hotels and Packages business has contributed approximately 39% to net revenues of the company as compared to the 60% contribution made by the air ticketing business.

Even the new government is expected to push the travel and tourism sector aggressively with a strong investment in the development and restoration of archaeological sites in the country. The infrastructure and tourist attraction development within the country also led to the country's tourism growth.

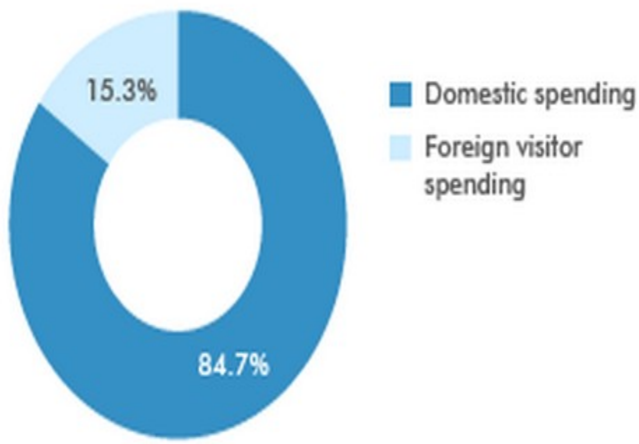



**Travel related ecommerce industry:**

As per Avendus Capital, the Indian Ecommerce market is estimated at $ 6.3 Billion. The online travel market constitutes a sizeable portion of 71% of this market. Around 30% of the total travel bookings in India is done online. This penetration is all set to increase given the fact that the cost of online travel booking is comparatively lower. Besides the hotels and packages business, MakeMyTrip is trying to increase its presence in mobile. MakeMyTrip app has already crossed 4 million downloads till recently. The company even pointed out that more than a third of their total online visitors come via mobile. In the last quarter, the mobile bookings accounted for over 16% of the total online transactions for domestic flights.

**Recent Acquisitions of the company:**

The recent acquisition of easytobook.com by MakeMyTrip is hoping to increase the company's revenue earned through online hotel bookings. With this acquisition, the company plans to expand beyond South East Asia. More importantly, it has significantly added to the company's technology stack and has also enhanced the international hotel offerings portfolio in both standalone and package deals.



**Risks Factors related to the Industry and the Company:**

Declines and disruptions such as fuel price volatility, civil and political unrest, continued fare increases could adversely affect the business. Owing to the sensitivity of the safety concerns, the business has declined in the past and might decline in the future as well.

For the company whose presentation currency is in U.S dollars whereas the functional currency is in Indian Rupees, any fluctuations in the currency exchange rates will affect the results of the operations. The drop in the value of the Indian Rupee Vis-à-vis the U.S Dollar adversely impacted the travel industry as it especially made the outbound travel more expensive.

The travel industry both in the country and worldwide is intensely competitive. With a number of competitors such as yatra.com, goibibo.com, Travelocity.co.in, expedia.co.in and a number of traditional travel agencies, travel suppliers and tour operators, the company has to continuously keep updating itself with superior technology and resources and a bigger inventory.

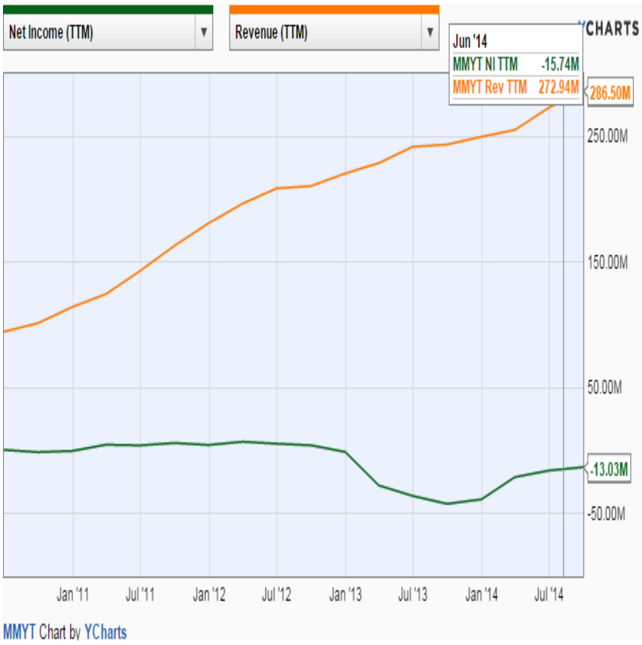
The state of the economy also plays a huge factor as it affects the margins earned on the tickets and packages.

## FUNDAMENTALS OF THE COMPANY:

As per the above analysis done both on the company and the industry, it can be said that the company holds strong fundamentals.

## FINANCIAL PERFORMANCE:

Revenue Vs Net Income for MMYT:




**Key Performance Indicators:**

| | |
|---|---|
| Share Price (as on 1 Jan 2015) | **$ 25.99** |
| Shares Outstanding (in millions) | **41.68** |
| Market Capitalization (in millions) | **1132.81** |
| Sales (in millions) | **255** |
| EPS (ttm) | **-0.3060** |
| Current P/E Ratio (ttm) | **N/A** |
| P/S (ttm) | **3.79** |
| P/B | **7.17** |
| Annual Dividend | **0** |
| Dividend Yield | **0%** |
| Beta | **1.49** |

**Valuation:**

| | |
|---|---|
| Debt/Equity Ratio | **0.2** |
| Risk Free Rate (5 Year U.S Treasury Bond) | **1.61%** |
| Beta | **1.49** |
| Rm for the ecommerce segment | **0.2** |
| Risk Premium | **18.39%** |
| Cost of Equity (Using CAPM) | **29.01%** |
| Cost of Debt | **0.348** |
| Corporate Tax Rate in U.S | **40%** |
| Discount Rate (WACC) | **0.276582802** |
| Long-Term Growth rate | **0.27** |
| Enterprise Value | **$5201534.51(in 000)** |
| Total Debt | **$427296** |
| Free Cash Flow to Equity (FCFE) | **$4774238.51(in 000)** |
| Outstanding Shares | **157910000** |
| Intrinsic Share Price | **$30.23** |

Assumptions made For Valuation:

- Discounted Cash Flow (DCF) model has been used to Value the company.
- Two-stage growth model is used. Moderate growth for a period of 5 years starting 2015 and then a stable terminal value is assumed.
- The Free cash flows are assumed to grow at a rate of 27% based on the previous 5 years data. The negative Net Operating Cash flows for the year 2014 is mainly owing to reason of clearing the accounts payable. Keeping that in mind, the free cash flow for the subsequent year i.e. 2015 is estimated to be around $ 8000 (in 000) and projections based on that are made for a period of 5 years.
- Levered Beta is taken as per Zacks estimate.
- Cost of Equity is calculated using CAPM and Discount rate using WACC.
- All other values calculated as per given data.

The Fair or the Intrinsic Value of the share price comes out to around $30.23 which is higher than the current market price of $25.99.

**Comparable based Valuation:**

The above graph (blue line representing MMYT, Yellow-Expedia, and Purple-Ctrip) gives a comparative analysis of the share prices of 3 companies in the same industry.

The MMYT stock tends to be a more volatile stock indicating that the stock has more potential to increase its share price in the short run.

| Comparables | MMYT | Industry |
|---|---|---|
| P/E (ttm) | 0 | 55.9 |
| P/B | 6.7 | 4.2 |
| P/S | 3.7 | 3.4 |
| Dividend Yield | 0 | 0 |
| Net Margin | -5% | -1% |
| ROE | -7% | 2% |

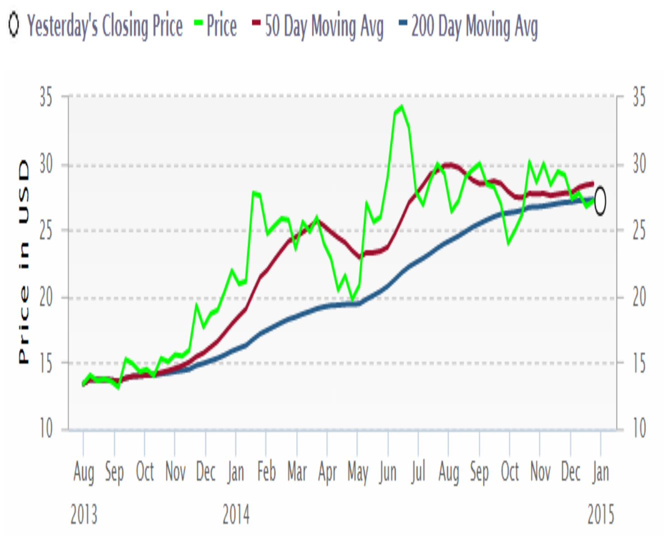
Industry Comparables:

The industry for the next five years is set to grow on an average of 22.4 % whereas MMYT is set to grow on an average of 27%.

**Risk Analysis:**

The risk of default as per Credit Suisse for MMYT is 0% whereas for the industry its stands around 1%. It holds a good rating in terms of asset quality, expense recognition, inventory and net income. Whereas in terms of accounts payables, cash flows, revenue recognition and balance sheet, the rating comes out to be below average. The overall accounting quality stands out at below average.

| **Price Momentum** | | | | | |
|---|---|---|---|---|---|
| | 18 mth | 1 yr | 6 mth | 1 mth | 1 wk |
| Absolute | 92.77 | 33.30 | -16.91 | -6.69 | 1.53 |
| Rel. To Peers | 92.77 | 33.30 | -16.91 | -8.20 | 2.61 |




The above price momentum table gives us the price change of the firm relative to itself and its peers. The above indicates the drastic change the share prices for the company have undergone over a 1.5 years' time. This price momentum as observed from the graph indicates that the share price should hover between $25 and $30.

**INVESTMENT CONCLUSION:**

- The DCF Valuation technique shows us that the stock is currently undervalued at $25.99 and has the potential to go up to $30.23. Thus the stock has good potential for growth.
- Even the fundamentals of the company stand in place.
- The comparables based valuation also points out the fact that the company is performing in tandem with the industry and has a lot of scope for growth.
- The company might face some risks from the rising competition both domestically and internationally. But the brand equity of the company mitigates these risks.
- Investing in MMYT is a good long term bet on the growth of the Indian economy and the increasing internet and mobile penetration.

## Recommendation:

CMP $ 25.99

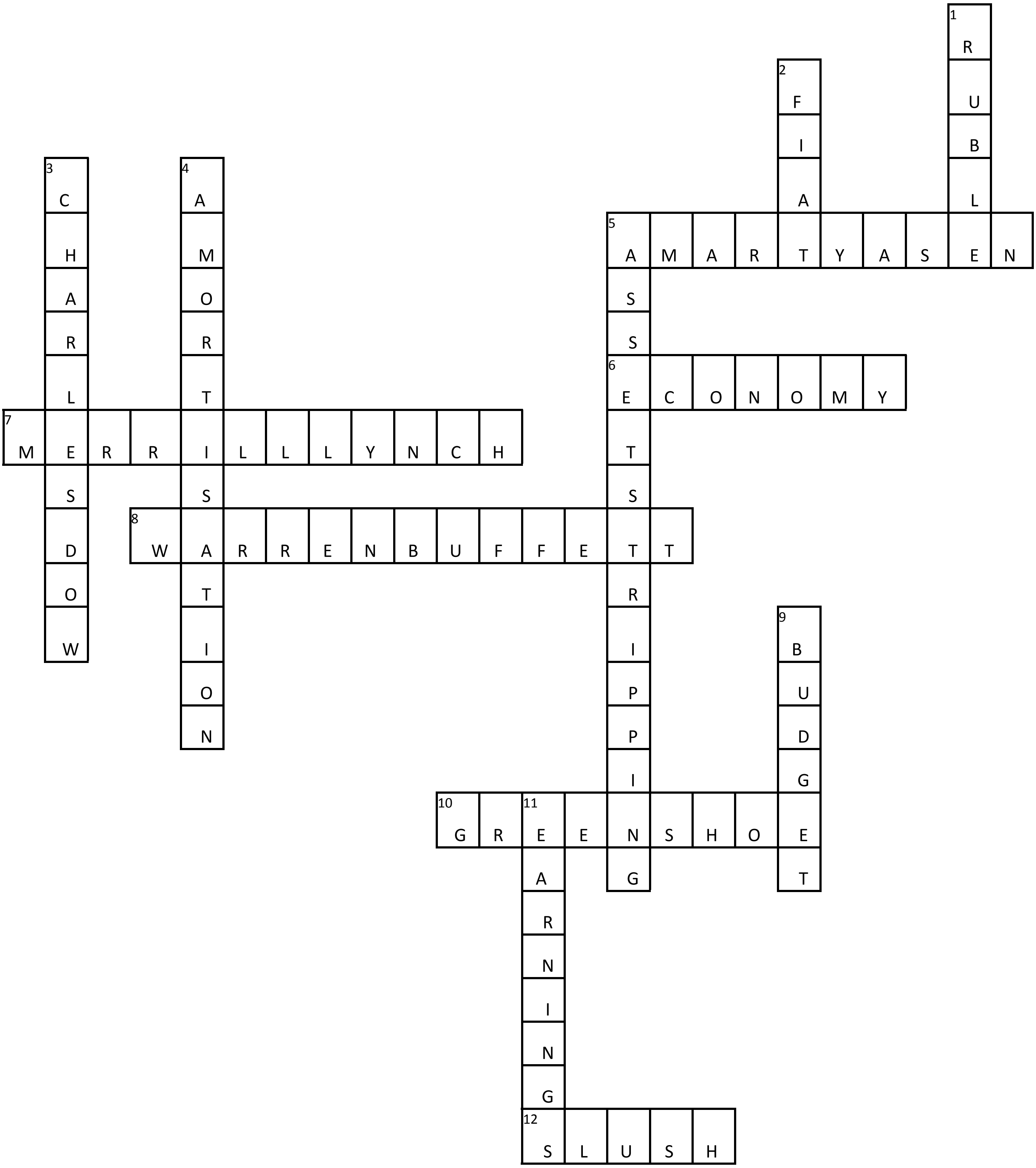
Fair Value $ 30.23

BUY

## Disclaimer

Utmost care has been taken so to ensure accuracy and objectivity while preparing this report based on the information available in the MMYT annual report, Bloomberg and the public domain or from sources considered reliable. However, neither accuracy nor completeness of information is guaranteed. Opinions expressed herein are my current opinions as on the date of this report. The recommendations is also based upon my individual view and is hence not be taken for granted. So the reader is sincerely requested to do his/her valuation before investing in this particular stock. The impact of market factors can distort the price of the security thereby deviating from the intrinsic value over an extended period of time. This report should not be constructed as recommendation to buy, sell or hold a security, whatsoever. The reader assumes the entire risk of any use made of this report or data herein. Research is not responsible for any errors or omissions in analysis or for results obtained from the user of this information contained in this report.

## FIN CROSS SOLUTIONS

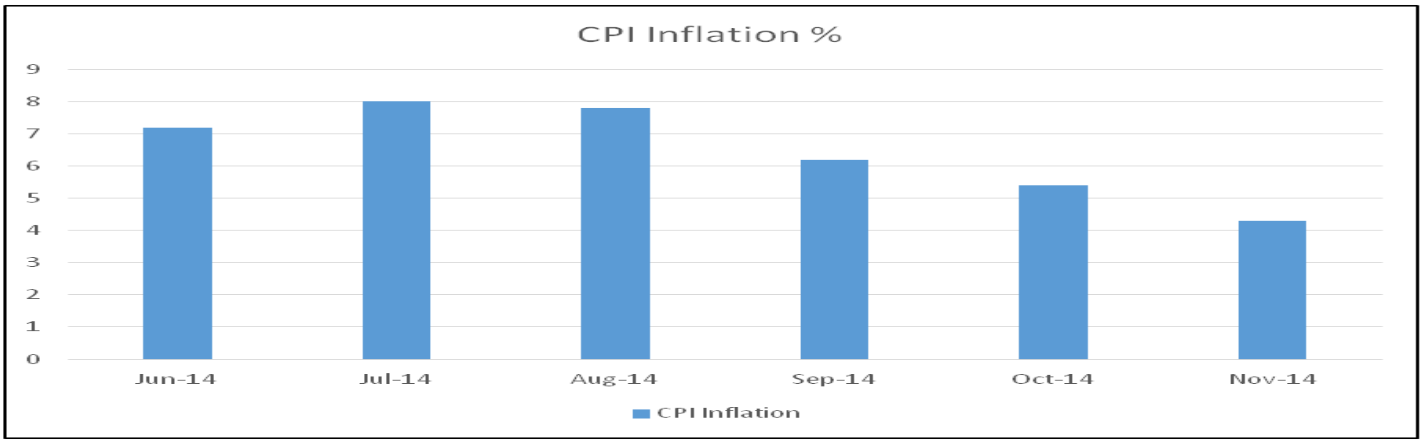


# RBI RATE CUT: AN IDEAL TIME?

-By Sahil Sharma & Manas Mendiratta

- IIFT, Kolkata

"The Reserve Bank of India (RBI), recently, reduced repo rate by 25 basis points from 8% to 7.75%. The industry, which has welcomed the move now demands even more rate reduction. The rate cut is largely symbolic and may not lead to a significant drop in borrowing costs for both individuals and companies. However, it may act as mood booster for the market. We shall explore whether the RBI should be more cautious or continue with its easing policy."




India's economy is expected to grow by around 5.5% this year. More public spending is required to turnaround the economy. Manufacturing sector, which is in doldrums, needs to be given a push to revive the economy. Industrial output has contracted to a shocking 4.2% in October 2014.

There has been clamor of interest rate cuts for quite some time which is going to become even more intense now. Rate cuts are believed to be panacea for all issues pertinent to manufacturing sector. CPI inflation is on the decline. As shown in the graph, during the last four months, inflation has come down, whether it is CPI (Consumer Price Index) or WPI (Wholesale Price Index). Latest estimates report it to be around 4.5%. There has been consistent demand from industry to cut rates. Even Finance Minister, Mr. Arun Jaitley has called for increasing the flow of funds in the market. He has signaled time and again to Reserve Bank of India (RBI) to cut interest rates in view of slipping industrial output.

Proponents of rate cuts attribute cost of capital to be the singular factor that has contributed to the slowdown of manufacturing growth. Due to costly capital, manufacturers find it difficult to afford it, thereby delaying credit off take and infrastructure creation. Factory output has registered a negative 4.2% growth during October as compared to last year.

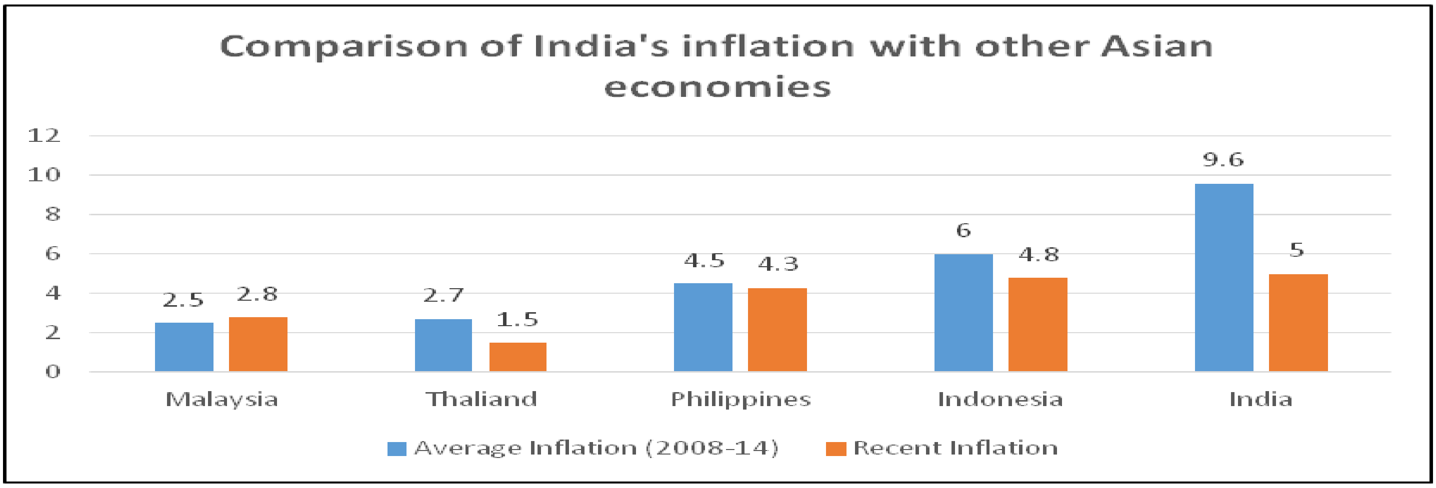
Despite mounting pressures, RBI has spurned all these calls for an interest rate cut. The main reason for maintaining status quo by RBI is to ensure that commodity prices do not rebound and to meet the target of attaining

6% inflation by January 2016. The repo rate, the rate at which RBI lends funds to commercial banks, stays at 8% and the cash reserve ratio, the portion of deposits that lenders need to keep with the central bank, remains at 4% after the December policy review.

**POLICY RATES** (IN %)

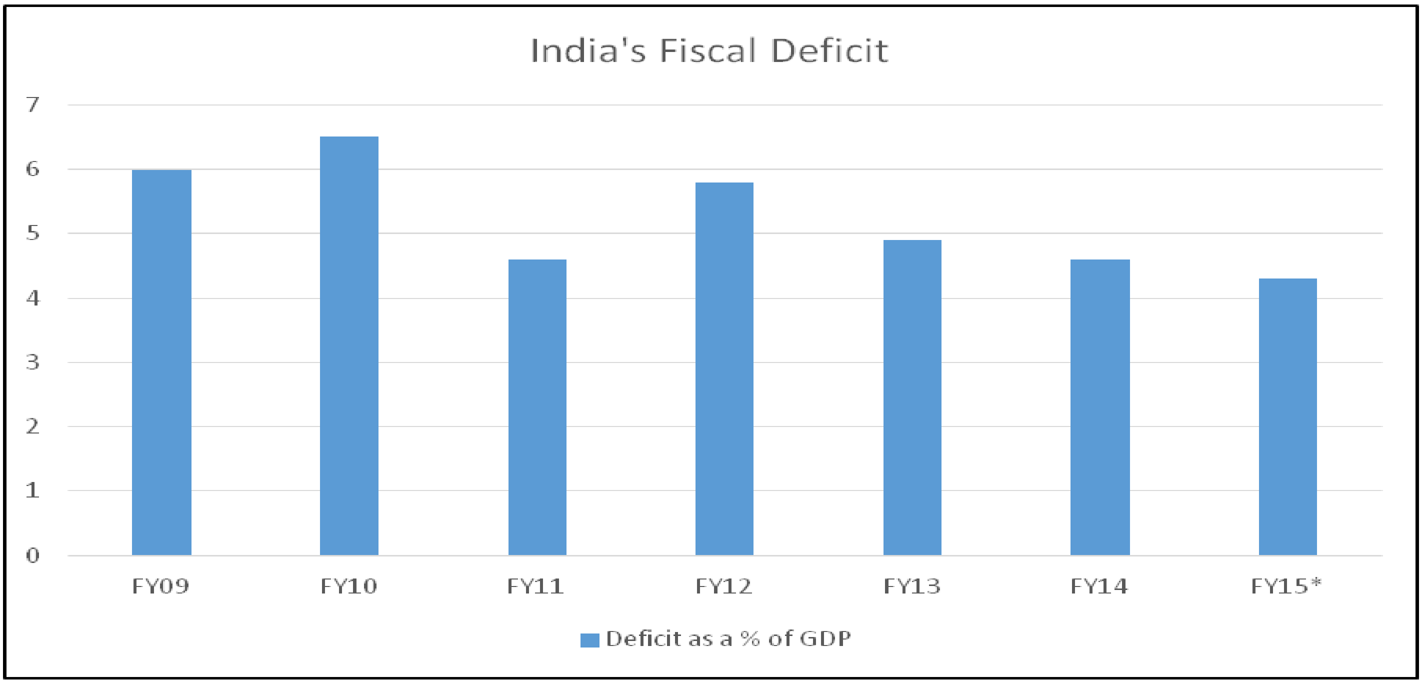
| | MAR '10 | MAR '12 | MAR '13 | JUN '13 | SEP '13 | DEC '13 | MAR 14 | JUN '14 | SEP '14 | DEC '14 |
|---|---|---|---|---|---|---|---|---|---|---|
| Repo Rate | 5.00 | 8.50 | 7.50 | 7.25 | 7.50 | 7.75 | 8.00 | 8.00 | 8.00 | — |
| CRR | 5.75 | 4.75 | 4.00 | 4.00 | 4.00 | 4.00 | 4.00 | 4.00 | 4.00 | — |

Throughout this decade, RBI has followed the policy of tightening and then immature easing. As a result the policy has not yielded the desired results. Between March 2010 and April 2012, the RBI hiked the Repo rate by 375 basis points to 8.50 per cent amid global financial crisis. The RBI slashed Repo rate by 125 bps between April 2012 and July 2013 when the financial situation improved. Since July 16, 2013, the RBI hiked the Repo rate by 75 basis points to battle inflation. After taking over in September 2013, RBI Governor Raghuram Rajan hiked the repo rate by 75 bps in three steps of 25 bps each, reinforcing the anti-inflation stance of the monetary policy.




The main reason that is holding back the RBI from accommodating demands of rate cuts is the turn of the US rate cycle. It is believed that Federal Reserve could move back to normalization in near future. With the strengthening of US dollar and weakening of Indian Rupee, inflow to India is expected to decrease. The fact that FII holdings in Indian debt is more as compared to equities means situation is quite volatile. In case RBI cuts interest rates, country could witness significant outflows, which would weaken the currency further, thereby creating a vicious cycle. Therefore, it is prudent that RBI allows INR to depreciate gradually by using its foreign reserves and minimizing volatility.

Although inflation has declined in past few months, but taking into account GDP growth rate of around 5%, it's still very high. For example, in the start of this century, India's GDP growth rate was around 4.2%. At that time CPI inflation was around 2-5%. Clearly, right now, inflation is still on a higher note. As indicated in the graph, India's inflation is still high as compared to other emerging economies of Asia.  Moreover, India's inflation remains higher than that of many other Asian economies. Recent moderation in inflation is a beginning of disinflationary process. Inflation should be allowed to fall further before any rates cuts are adopted.




Monetary policy and fiscal policy should run in synchronization with each other. Fiscal deficit has already touched 90% of its target in this financial year. Moreover, tax collection is unlikely to meet its target. This means that in order to meet the target of 4.1% fiscal deficit, fiscal policy would witness contradiction. In lieu of contracting fiscal policy, monetary policy should also witness a tightening mode. It is imperative that government is successful in reducing fiscal deficit before RBI goes ahead with rate reduction. To achieve this balance, there is a dire need to revive stalled projects.

Contrary to common perception there is no strong correlation between bank lending rate and real lending rate. There is a positive correlation between real interest rate with credit growth and industrial growth. This indicates that demand and supply of funds determine the interest rates. Higher growth puts upward pressure on rates and lower growth cycle induces downward pressure on rates. Investment is not constrained by interest rates. It depends on many other factors such as productivity of capital, sales growth cycle, balance sheet position, and operating margins. Thus, it would become difficult to revive investment cycle merely by reducing rates.

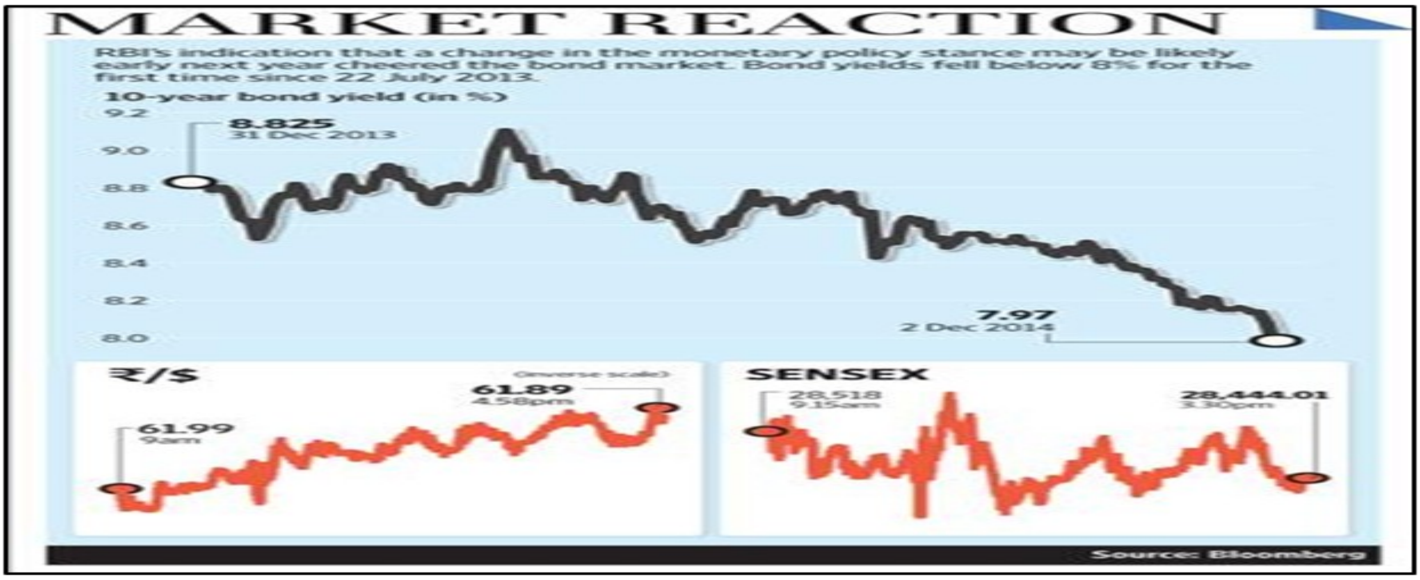
It needs to be kept in mind that households save more than half of their financial savings with banks. However, households' financial savings fell to 25-year low of 6.8% of GDP in FY14. If banks continue to reduce deposit rates, households will prefer physical savings over savings in banks. This will have a detrimental effect on investment and GDP growth.

Under Basel III, banks are required to meet significant amount of capital in reserves. These norms come into effect from March 2019 and require banks to maintain minimum Tier-1 capital of 7% and another 2.5% of common equity. In case interest rates are reduced, there is a possibility that NPA might shoot up. This would make banks less attractive for investments.

There is a considerable misinformation about flexible inflation targeting framework among some politicians and businessmen. Flexible inflation targeting (FIT) was recommended by Urjit Patel Panel Report in early 2014 and it is essential that centre agrees to some of its prerequisites for its success.

Politicians, perhaps, believe that RBI may not pay adequate attention to boost economic growth post this reform. This is not true. Monetary policy has to ensure macro stability by keeping interest rates such that the needs of borrowers and depositors are balanced. It has to be understood that monetary policy, unlike fiscal policy, cannot be a popularity contest. Sustained low and stable inflation has its own benefits that will facilitate a sustained decline in interest rates in the long run. So businesses and politicians have to broaden their myopic view. RBI should not be blamed in case the companies fail to service their costly debts.

After so many years of high retail prices, inflation has slowed down in the past two months. RBI needs to ensure that inflation reduction is sustainable. It's only been two months since real policy rates have turned positive and RBI should wait for another couple of months to see what trend develops and how the government manages its fiscal policy. Therefore, Mr. Rajan is right in being adamant in keeping rates unchanged until the price pressures are completely off. RBI has told in a recent statement that if current inflation momentum continues and fiscal developments are encouraging, it is ready to change the stance on monetary policy early next year, including outside the policy review cycle.




High inflation and high growth cannot grow hand in hand. Oil prices comprise around 30% weightage in CPI basket. The fall in oil prices has aided fall in retail inflation. But oil prices are reversible. If RBI maintains the rates constant for now, it would clearly indicate that whether current softening in commodity prices is likely to persist. This is important to meet inflation target of 6% by January 2016.

RBI is taking its time to ensure that cooling is well entrenched in the economy and will not reverse. One of the other reason that RBI is holding its guard is recent monetary easing by European Central Bank (ECB) which could see capital inflow into India.

We have seen that in the past three months, inflation has decreased significantly. Although it is too early to celebrate, it appears that the central bank's policies are creating the desired results. So, it makes sense that RBI should continue to stick to its policy of inflation control without yielding to the demands of rate cut in a haste. As Mr. Rajan says it's better to win the fight against inflation once and forever.

# NEHRUVIAN SOCIALISM VS MODINOMICS

-BY Mohd Zeeshan & Shubham Jain

IIFT, Kolkata

If there has been one topic in the politico-economic discourse of our country that forms the crux of how things have changed in the past one year, it has been 'Modinomics'. If for nothing else, we should at least give credit to Mr. Narendra Modi for bringing the Indian Economy into discussions taking place in drawing rooms, at every nook and cranny pan shop, in local trains, in classrooms among other places. When debating Modinomics and Nehruvian Socialism, proponents of both types of political ideology take to statistics to prove their point. But the issue goes beyond mere statistics and the various development indicators.

## THE ADVENT OF NEHRUVIAN SOCIALISM:

Nehruvian Socialism can be traced back to the 1955 AICC session at Avadi wherein Jawaharlal Nehru with Morarji Desai and other Congress leaders declared that a socialistic pattern of society was the goal of the Congress. The manifesto clearly stated, "It is not possible to pursue a policy of laissez-faire in industry. It is incompatible with any planning." It was basically the Soviet Model of Development camouflaged in Devnagari script.

### Drawing analogies

If Gujarat, which has been the subject of Modinomics for the past decade, gives us a good indicator of the relevance of Modinomics, then analogies can be drawn to Bengal to gauge the significance of Nehruvian socialism in our country. The 'Bengal Model' is one in which the state plays an domineering, almost absolute role. The state is obliged to provide for everything-from womb to tomb - to every individual of the state. With the creation of the Bengal Model, the focus shifted from 'duties' of the individuals to 'rights' of the individuals. The public sector units were accorded the status of 'temples of modern India' by Nehru . The system was a labyrinth of regulations and the license-permit-quota raj the key to it. Not only did it lead to corruption and nepotism, but also ensured that our growth did not exceed the Hindu rate of growth. Entrepreneurship became a 'taboo' and profits were treated with cynicism. The Soviet Union collapse in the late 1980s shook the very foundation of socialism in our country. The financial crisis of 1991 proved to be the last nail in the coffin for socialism and forced a rethink of our economic policies. The path was paved for liberalization and opening up of the economy.

### The ills of socialism:

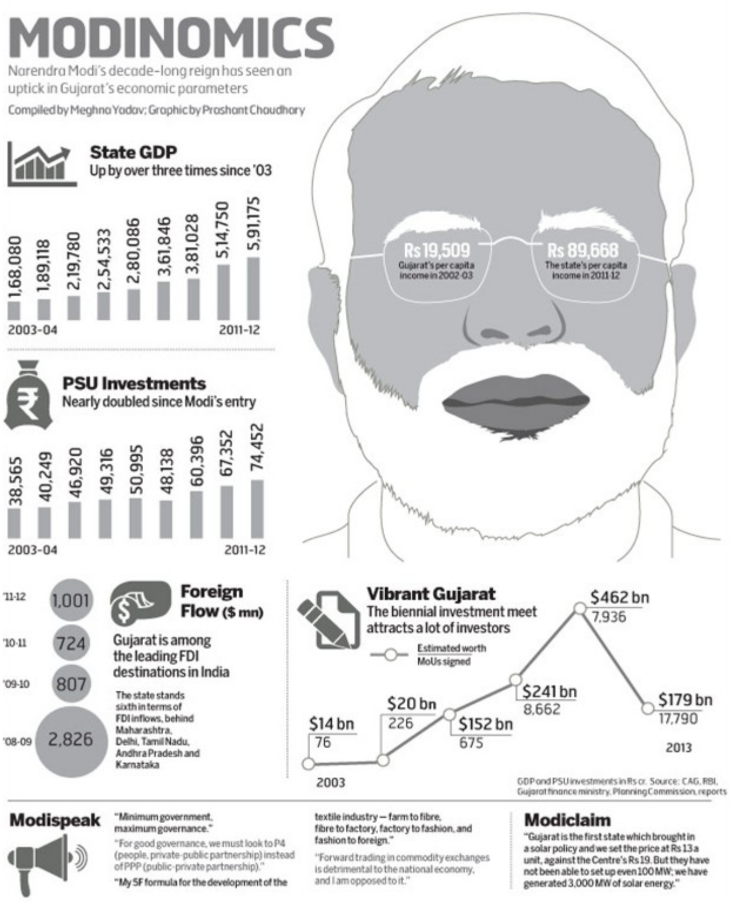
However socialism was deeply imprinted on the psyche of the nation and the Frankenstein state of sixty years had resorted to subsidies that put enormous burden on the exchequer. Various types of rights like the right to food, right to employment and education etc. were conferred on the citizens. The degenerate system was incapable of delivering these rights in a fair and effective manner and it basically a way to siphon away public resources under the garb of legitimacy. Gigantic amount of resources were used to fund the subsidies which enabled crony capitalists to tweak the free market system and derive benefits that ensured that the top 1 % were in control of the 99% of the resources.

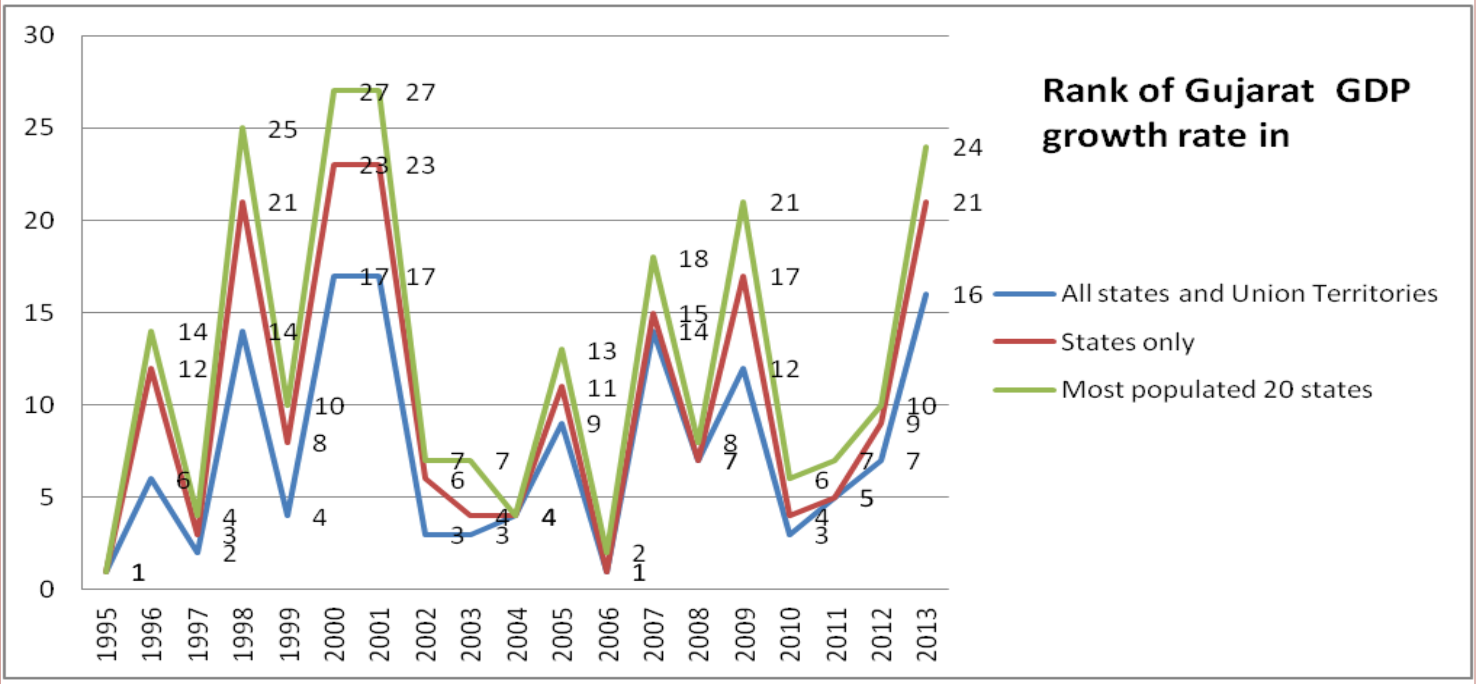
**'MODIFYING THE ECONOMY':**

Modinomics, however, proposed an alternative to this- a policy wherein the role of the state was receded to the background and the importance of the role of the citizens assumed centre stage. In such states, entrepreneurship is seen as the major generator of employment and therefore highly encouraged. Moreover an ecosystem that facilitates conditions to make the individuals self-sufficient and responsible is created. Emphasis is laid on voluntary self-regulations rather than mandatory restrictions. The legal framework based on self-regulations is driven by an effective as well as efficient judiciary. To bring more clarity in to the discussion, let us take the example of power supply and distribution. While Gujarat model would charge for power but the supply would be consistent and continuous. But when it comes to the Bengal model, power would be available rather cheap or even free, but it would be marred by erratic power cuts.

**Modinomics Not Picture-perfect:**

However to say that Modinomics is the remedy to all problems facing our country would be stretching it too far. While the chants of 'Vibrant Gujarat' have been pretty pervasive and Modi's neo-liberal policies have been instrumental in his earth-shattering popularity, yet the truth is that Gujarat has fared not much better than the other states following the socialism way of governance. Moreover, it is also felt that mid-sized Gujarat, having a well-established system of trade and business, has a differential advantage compared to other humungous, underdeveloped states. In the 1990s,the growth rate in Gujarat was 4.8% as compared to the national average which was 3.7 %. In 2000s it was 6.9% while that national average was 5.6%. Therefore the difference in the average growth rate varied from 1.1 percentage points in the 1990s to 1.3 percentage points in the 2000s. However, when it comes to the state at the lowest rung as far as per-capita income is concerned, we find that Bihar has taken huge strides in development. While its growth rate in the 1990s was 2.7 percentage points below the national average, it underwent spectacular levels of development to exceed the national average by 2.3 percentage points in the 2000s. Therefore, one cannot say that only Modinomics has brought about extraordinary results.

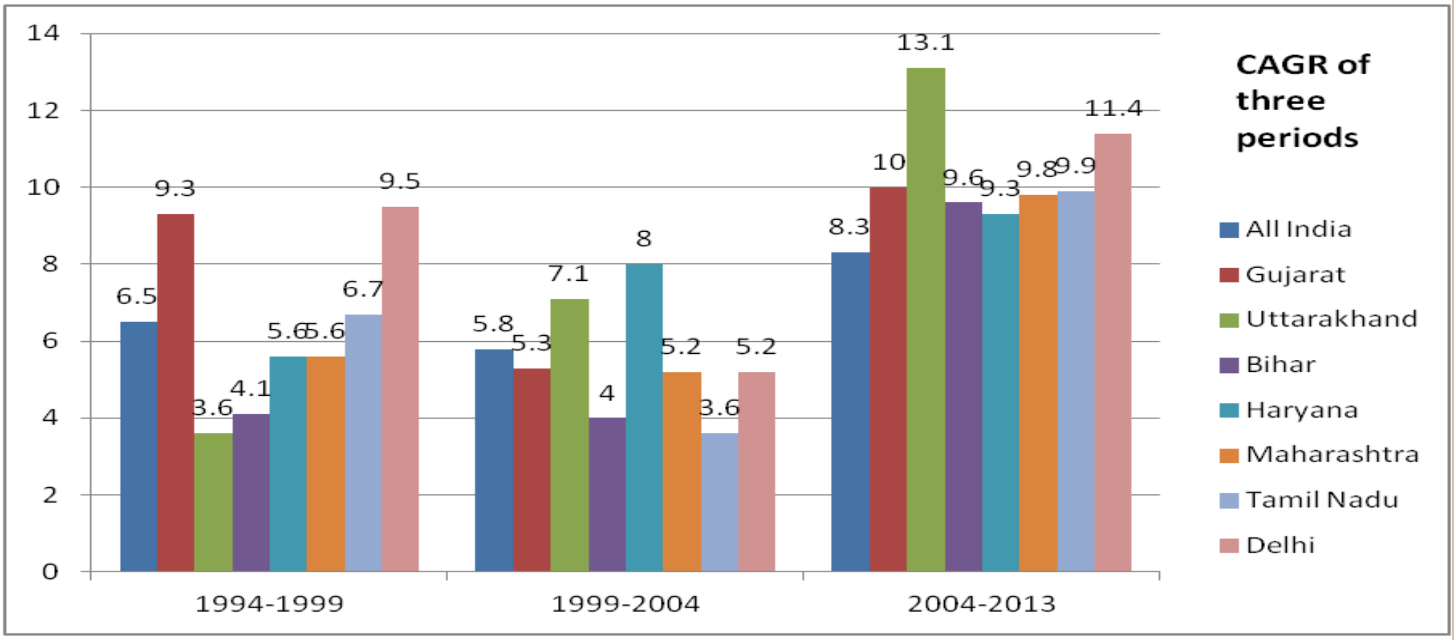





The slowing pace of growth in the last few years can be attributed to the high interest rates as well the inflexible labor rights. Moreover, the IMF also blames the pessimism prevalent in the economy and the increasingly uncertain and bleak outlook for this downturn . The IMF wants the government to take some dynamic and dashing initiatives to bring about a turnaround in the economy.

**THE BIG DEBATE:**

Therefore it may be summarized that the battle between Nehruvian socialism and Modinomics has no clear winner. When it comes to devising strategies for a country as huge and diverse as India, there is no one policy that paints all. It is a tectonic shift and cannot be concluded merely by looking at the numbers. What is needed is a comprehensive and personalized polity of governance that ensures that the diversity of our country is celebrated in the truest possible manner.



# GROWTH VS TAMING THE INFLATION

-By Saurabh Dongare & Anshita Lalwani

NMIMS

*A perfect storm is in the making: financial uncertainty, economic downturn, government cuts, rising unemployment and a future that looks less clear the more we try to fathom it.*

-Jonathan Sacks

The whole debate revolves around Economic uncertainty, its effect on monetary policy and its impact on growth.

## CURRENT SITUATION (POLITICAL INTEREST OF ECONOMIC GROWTH VS ECONOMIC INTEREST OF RBI TO CONTROL INFLATION)

India is walking on Mr. Modi's path of "Make in India". With 16% contribution to GDP, Manufacturing sector in India is struggling to mark its footprint. The government has identified and prioritized the concern as the most paramount one. So the political inclination is to revival of the growth of manufacturing sector and to improve the investment scenario in the country.

On the other hand, when India was haunted by high inflation of above 8% (CPI), Mr. Raghuram Rajan (RBI Governor of India) had decided to tackle the situation by implementing tight monetary policy. As a result, the repo rate has been increased to 8%. In recent times, RBI is able to bring the inflation rate under control. Its target is to bring down the inflation rate to 6% by January 2015 and further to 3% by January 2016.

This high repo rate of 8% had a direct impact on growth rate of the country. High interest rates resulted into low investment. Home loan, car loan became expensive. Low money supply is forcing the consumer to spend less resulting into low demand. This has impacted the production (Supply) by the firms forcing them to engross them with further investment plans, employee layoffs etc. As a result GDP has fallen from 5.7% to 5% in just quarter time.

To summarize, there are two conflicting school of thoughts. The **political** one is inclined towards reviving the growth rate and the **technocratic** one is inclined towards reducing the inflation in the country.

## GROWTH VS INFLATION. WHAT IS IMPORTANT FOR INDIA?

It is not difficult to understand that there is a trade-off between growth and inflation. Growth is always associated with inflation, Certain level of inflation is not a concern (Up to 3%).Beyond that, growth is always accompanied by high inflation, high interest rate (implemented as a measure to control inflation) , lower investment and hence fall in the growth. If the repo rate remains intact at 8%, the GDP may fall further. On the other hand if RBI decreases the repo rate, the inflation may again soar up. Again and again it has been seen in India, and outside India also, that the way to sustainable growth is to have moderate inflation. Though there are some countries like China which can manage growth with high inflation.

For a country like India where per capita income is 5000$ against 53000$ that of USA, high inflation rate may severely impact the livelihood of the people of the country. Growth is obviously the need of the hour, but it is unwise to attain growth at the cost of increasing inflation. Controlling inflation is a prerequisite for a good economy.

**Why RBI is reluctant to decrease the rates**

Though the WPI has dropped to zero percent, a five year low figure, RBI is reluctant to decrease the growth rate.

The answer to this paradox is UNCERTAINITY prevailing in the economy. Falling inflation is likely to reverse the course. The figures for December may show a rising trend, says a report by Dun & Bradstreet. The US-based global research firm D&B expects the headline WPI inflation to increase by 1.0-1.5 per cent during December 2014. Uncertainty over monsoon and its effect on the food prices is another concern that is inhibiting RBI from reducing interest rates. The Central Bank wants to be confident that underlying trends for non-food inflation are moving in the right direction before reducing interest rates.

**Only rate cut is enough to review the growth?**

Even if RBI reduces the repo rate, this will not solve the problem of subdued growth in the country. There is need to review the Capital investment. A strong reform is required to revive economic growth.

Some positive signs of growth can be still found in such economic situation. The surprising rebound can be seen, with a 6.3 per cent growth in the core sector – indicating an increase in factory output – had kept everybody guessing about the policy which Rajan adopted.

The auto companies also reported an over 10 per cent growth in sales for November, after a dip in the preceding month, indicating a revival in the manufacturing sector.

This indicates that ONLY rate cut is not the solution to growth problem.

**Has RBI vanished the Euphoria of growth?**

When inflation is touching lowest of the season, RBI is now planning to cut the rates. This is in the anticipation of inflation target that had been set by RBI.

There is lot of opportunities for investment in Indian economy. The investment friendly labor policies, good investment sentiments are some good signs for economic growth. Though the growth may be deferred for some time it is certainly anticipated in coming years

**Is it right to tackle Inflation growth by controlling repo rate?**

CRR and interest rate (repo rate) are the two means used by RBI to control inflation as a part of their monetary policy. Since 2003 RBI has changed the repo rate 37 times to control inflation.

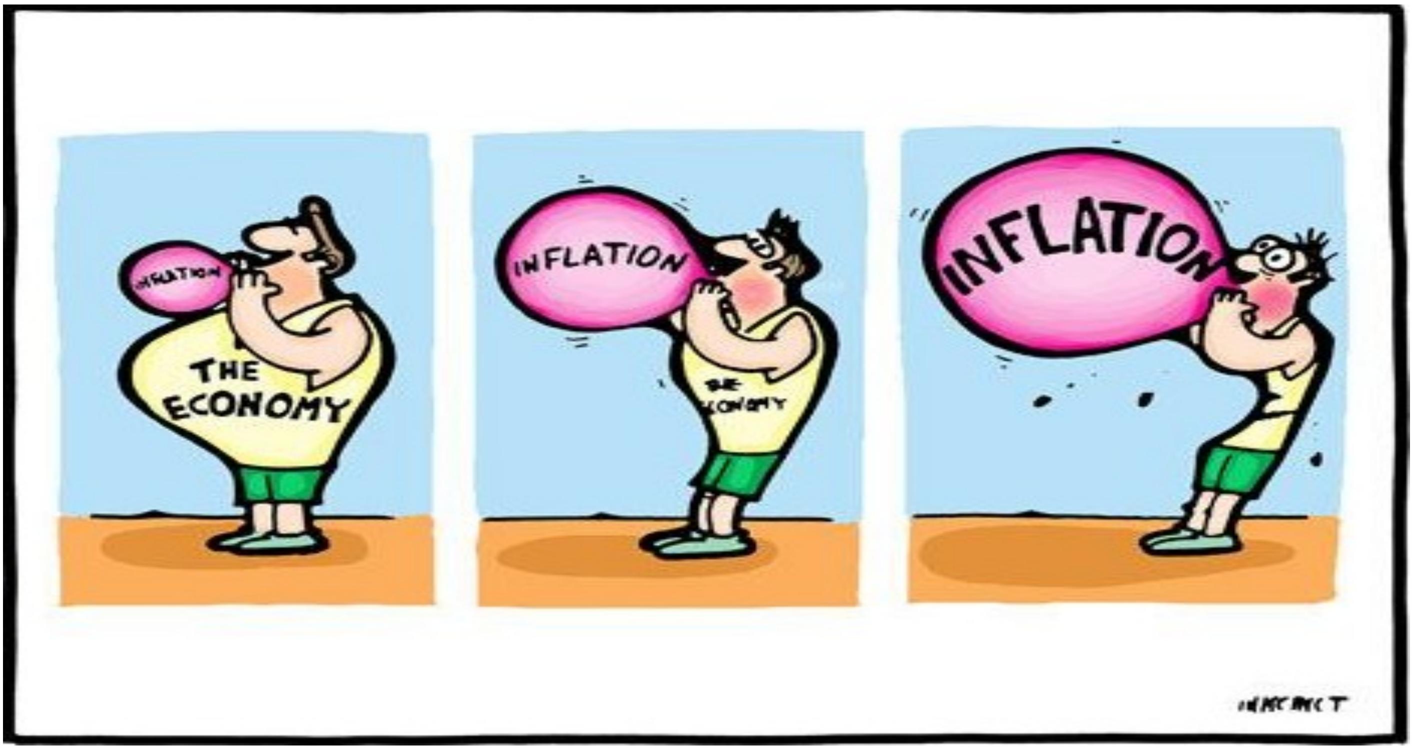
In this era of Keynesian recession, monetary policy won’t work .Rather its impacting the country in negative way. The interest rates are too high thereby resulting in increase in the FII flow.  FII is unstable form of capital inflow. Reverse flow may happen if world interest rate stabilizes (QE tapering). This will in turn destabilize the Indian economy. Another major issue is, with the manufacturing sector in India which is seeing low investment thereby impacting the economy growth as a whole.

## Suggestions

In this situation, major emphasis should be put on capital investments though channels like FDI , expansionary fiscal policy , investor friendly laws , liberal labor laws. This will solve both the problems of Inflation as well as growth in long term.

Growth of economy is increase in the natural output at full employment level. This is possible with increase in the productivity of the labor. Automation, technological advances, IT solutions are some of the means to attain higher growth.

It is seen that every country grows at its own pace. There is no way by which government or central bank can expedite the growth by just pumping more money in economy or playing with the interest rates. This will lead to inflation and economic instability. Growth above natural rate is possible only at the cost of inflation. This is not certainly acceptable for country with low per capita like India. Hence, a balanced way is to ensure high growth and low inflation at the same time.




Source: theviewspaper.net

# FINANCIAL INCLUSION IN INDIA: ALL TALK, NO ACTION ?

-By Roshan P R
NMIMS

***"The test of our progress is not whether we add more to the abundance of those who have much; it is whether we provide enough for those who have too little."***

***- Franklin D. Roosevelt***

It is merely the delivery of financial services to sections of disadvantaged and low-income segments of the society at affordable costs. Practically, it means that those sections of the society that are financially *excluded* will –

- Not be able to access affordable credit,
- Have difficulty in obtaining a bank account,
- Be under financial risk by not having home insurance,
- Struggle to budget money or plan for the unexpected.

Why do we need it?

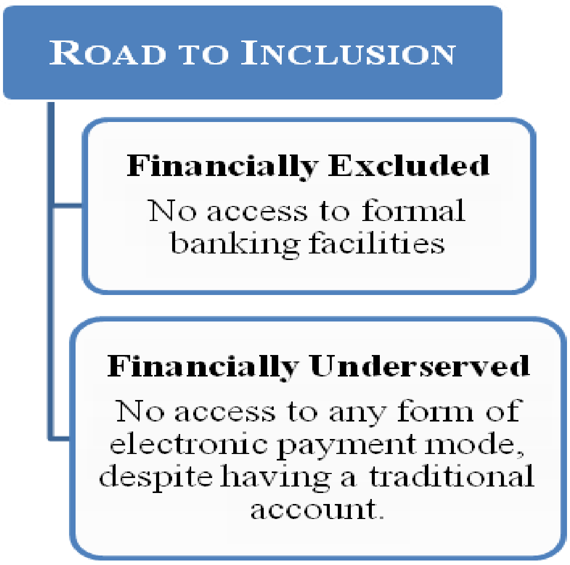
Common sense states that "financial inclusion" is key to stimulate growth, control inflation and enhance efficiency and transparency in public services.

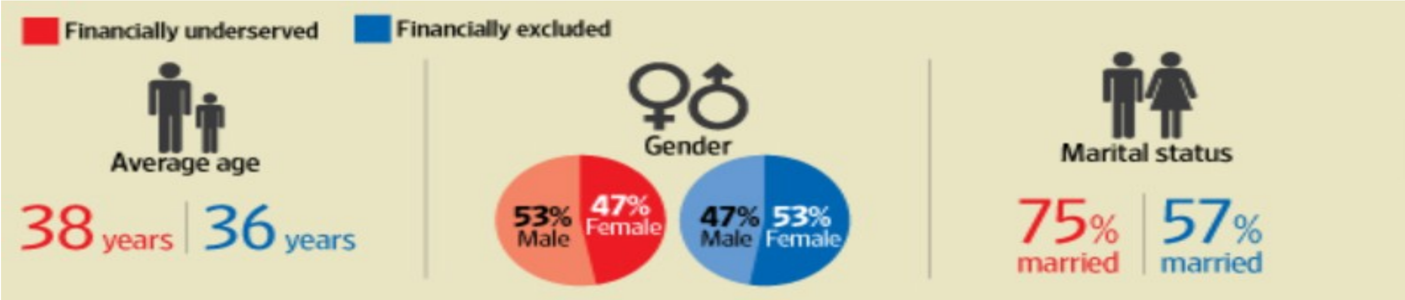
To put it simply, Financial *Exclusion* makes it much more expensive to be poor.

- Homeless wage earners in urban areas keep their money with their contractors in the absence of saving options.
- For transferring money, there is no choice but to use expensive informal modes or go to post offices
- Savings are stored either in the form of gold or in hard cash hidden somewhere in the house.
- For emergency borrowings, they turn to money-lenders who charge notoriously high interest rates.

Bank accounts also help poor people join the mainstream economy.

It connects the poor to formal financial institutions and provides easy access to transactions and payments. Over time, these transactions leave a digital footprint that functions as a kind of financial history, which can help the poor qualify for affordable loans.





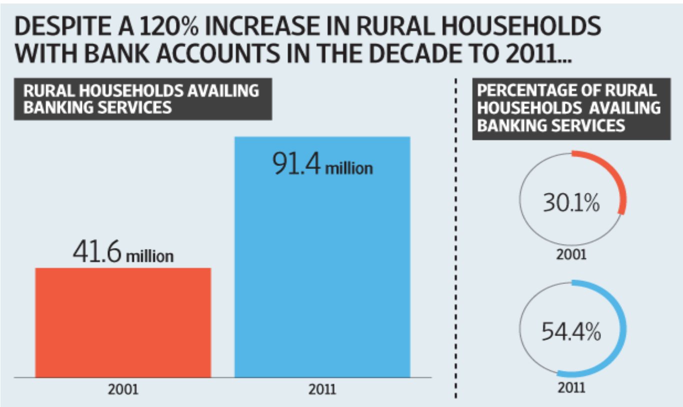

Source: MasterCard Research study

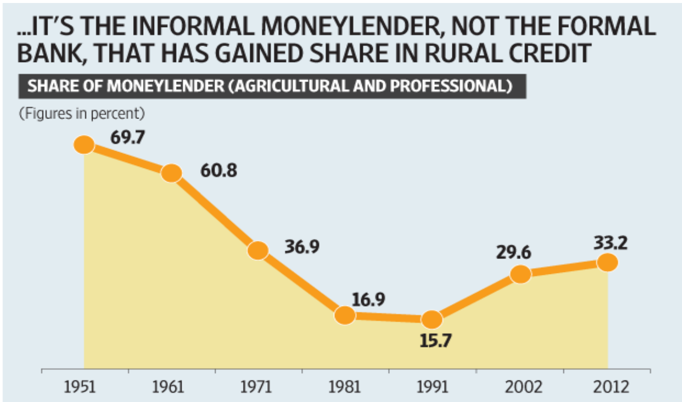
THE INDIAN STORY

***"Poverty is the worst form of violence."***

***- Mahatma Gandhi***

In India, the idea of Financial Inclusion has been floating around for nearly a century. Such a scheme was introduced way back in 1928 by Syndicate Bank - "Pigmy Deposit Scheme", to help daily wage earners, small traders and farmers inculcate a saving habit. The scheme exists even today with over 10 lakh accounts churning out profits of about Rs.3000 crores for the bank.




Source: National Sample Survey Report - Indebtedness and asset holdings of 62,000 rural households across 4,529 villages

It formally started as a state partnership with co-operatives in the 1950s, followed by the nationalization of banks in the late 1960s and the setting up of regional rural banks in the mid-1970s.

According to Census 2011, only 59% of the 246.7 million households across India have access to banking services - 54% of the 167.8 million rural households and 67% of the 78.9 million urban households.

So far the story in India has been – "Too much talk, too little Action". But, the year of 2014 has brought great promise in the form of a Dynamic RBI Governor and a Forward-looking Government at the Centre.

COMPREHENSIVE FINANCIAL INCLUSION PLAN

***"If the misery of the poor be caused not by the laws of nature, but by our institutions, great is our sin."***

***- Charles Darwin***

CFIP has two key end goals – greater access to the formal banking system, replacing India's myriad welfare schemes with a simple non-discretionary income transfer to all citizens.

In 2013, RBI Governor Raghuram Rajan set up the *Nachiket Mor Committee* to examine the various challenges in financial inclusion and remittance services in the country. The committee has estimated that more than 60% of the adult population is still excluded from basic services such as having a bank account for savings and remittance purposes.

On 28 August 2014, The Indian Government rolled out

**Pradhan Mantri Jan Dhan Yojana**

*" Every account holder will receive a RuPay debit card, will be able to use mobile banking services, will get accident insurance cover of Rs.1 lakh, will get a life insurance cover of Rs.30,000 will get an overdraft facility of Rs.5,000 once the account is operational for 6 months "*

The unit of contact is not the village but a household now, which makes the goal much more ambitious. A few steps taken to meet the end goals are:

- Business Correspondent Model:

  This model was re-introduced to address the *Last Mile problem* by offering simple credit and deposit products to customers.

- Moving past the Brick & Mortar structures

  Banks can encourage people to go for branchless digital banking, which will help in bringing down the intermediation cost.

- "Know Your Customer" Norms

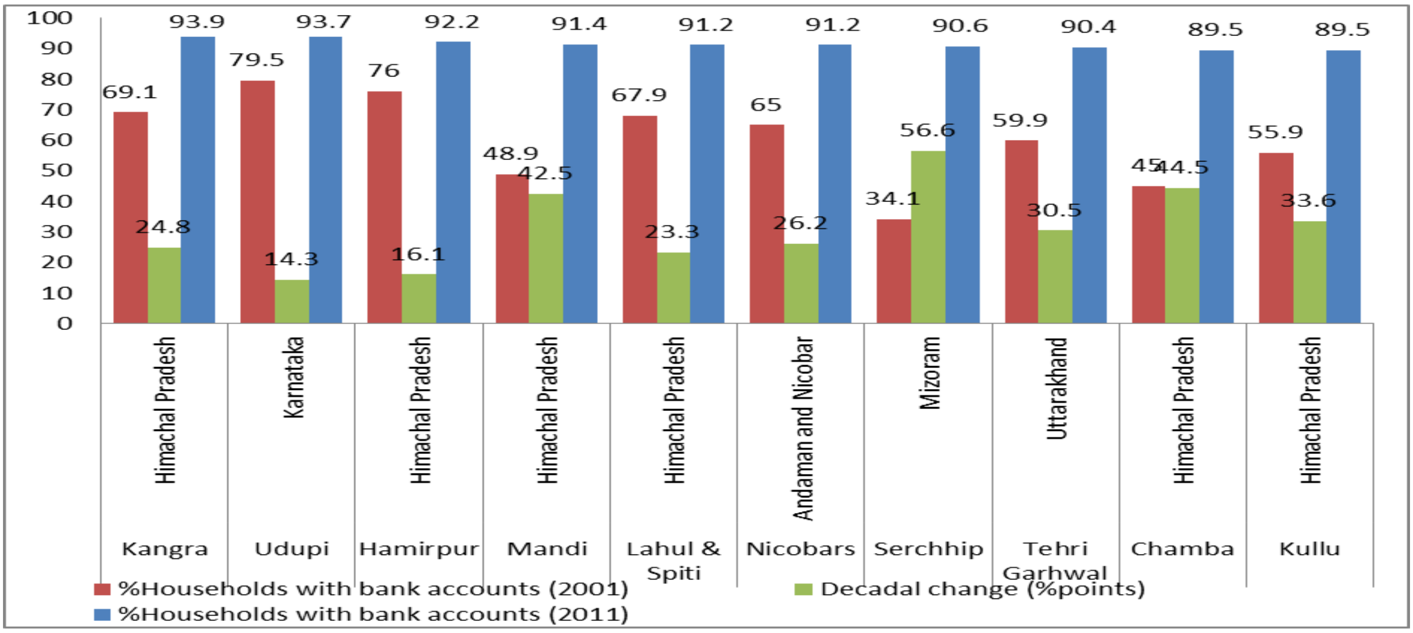
  Insistence on KYC norms has hindered the opening of new accounts even in urban areas. Great significance is, therefore, attached to e-KYCs.

- Introduction of Payment banks & Small Banks

  The RBI opened up the Banking Sector by issuing new bank licenses to banks that offer payments, deposit accounts but not loans.

- RuPay Debit Cards

  It transforms the entire landscape, from just cash-in services to cash-out services too. It will enable customers to operate their accounts even without BCs.




**Best Performing Districts** (Source: Census)

OVERCOMING BARRIERS

The success of any banking and financial system is judged on key indicators like performance and ease of access.

**Credit is unavailable/expensive**

Shut out from established sources of credit, the poor and small entrepreneurs typically end up borrowing from local money lenders at exorbitant rates of interest. Even when available, the bank prime lending rates tend to be several points higher than the RBI's benchmark lending rate.

**Debilitating lack of competition**

The biggest banks function as near-oligopolies with little incentive to expand coverage and lend to the poor or to small entrepreneurs. Only with more competition, rather than expensive populist schemes - will it be possible to fulfill what is undoubtedly a critical and praiseworthy goal.

**Duplication of accounts**

To meet the stringent target of opening 100 million accounts by 26 Jan 2015, many accounts are being opened for existing account holders. This issue can be resolved by *Aadhar*-linking the existing accounts and using the banks' existing CBS to syndicate the KYC data across all banks.

**High Capital Expenditure**

This issue can be solved as demonstrated by ING Direct—a branchless retail bank. In Dec 2013, it successfully provided a range of banking products through call centers and Web access, with two million transactions through 55 million mobile money IDs. The advantage of having a branchless bank is that it leads to a higher ROI and low capital expenditure.

**Oligopolistic Nature of the International Payment Systems**

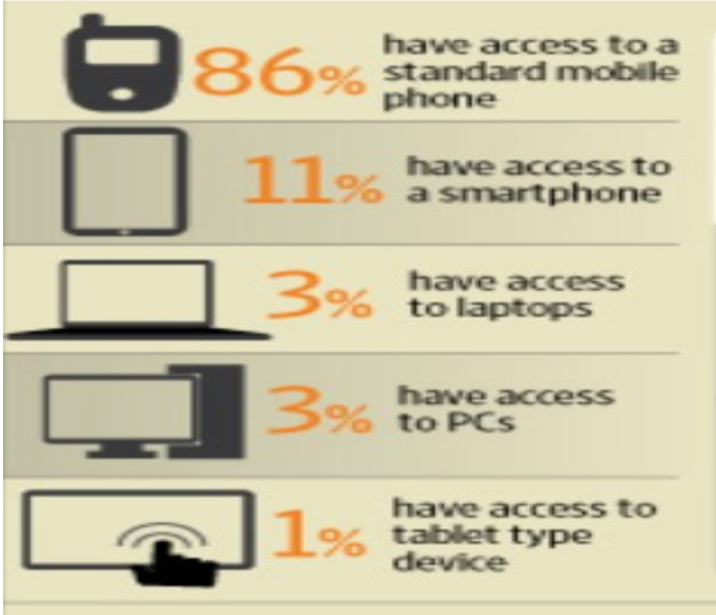
Dominated by MasterCard, Visa, American Express, it is difficult for a new player to make a breakthrough in this market because of the chicken and egg problem. Customers would not opt for RuPay cards till they have usage points. Establishments would not offer RuPay payment options unless there is demand.

Through PMJDY, there would be a massive inventory of cards with consumers. It is only a matter of time before merchant establishments start accepting RuPay cards to capture the business of the poor.

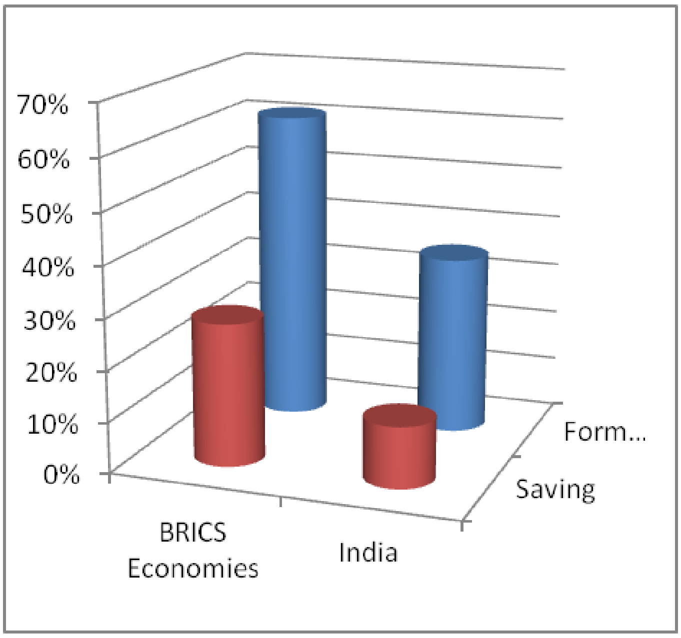
**Reaching out to the Corners of the Nation**

Pawan Agrawal, Senior Director, Ratings at CRISIL Ltd, said financial inclusion in India has so far fallen short of target because it was too branch-centric, with only 100,000 branches trying to reach six Lakh villages.

- The new banks will take banking to where people are staying. The front runners for the payment banks are -
- Mobile telephone companies with their extensive network in both urban as well as rural areas,
- Supermarket chains because of the economies of scale this new business brings to them,
- India Post, with its pan-India network. This has been done in China and Japan to expand financial services in rural pockets.
- Microfinance companies, committed to opening at least 30 million bank accounts across the nation.




Source: MasterCard Research study




**High Cost of Delivery**

In 2009, India Post alone handled 96 million money orders having a total value of about Rs.75 billion with an average size of remittances about Rs780. To allow small deposits, a '*No frills account*' with minimum balance requirements has been made available. To reduce the cost borne, the volume generated has to be very large.

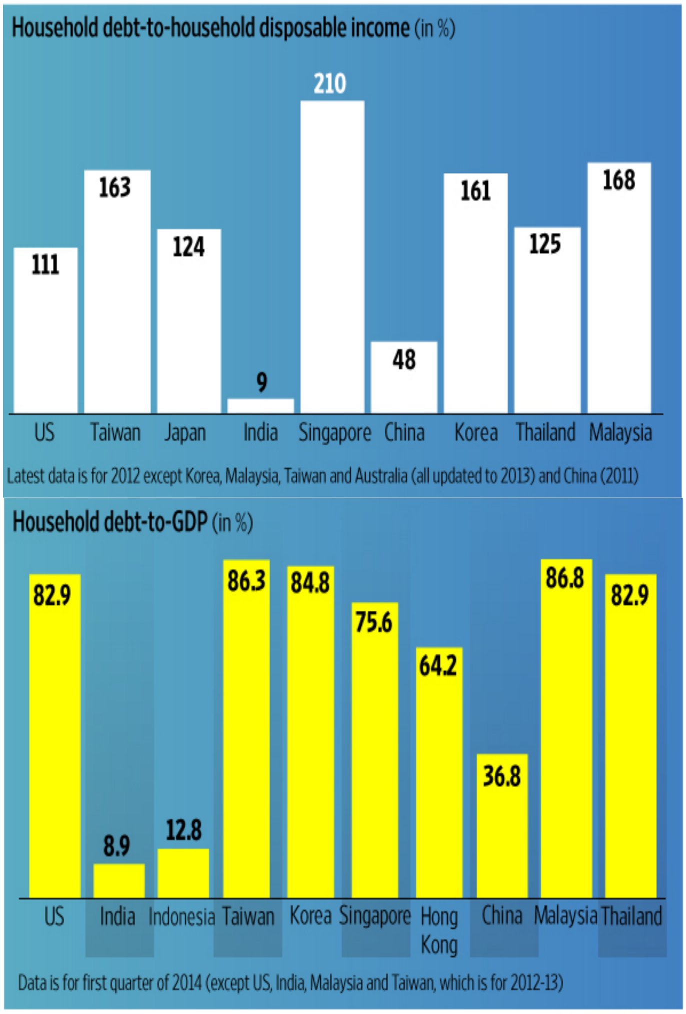
**Dormancy of accounts**

By mandating handing over of RuPay cards to every poor customer, the PMJDY has solved the interoperability problem. If wages under employment guarantee and the other direct benefit transfers get into a RuPay enabled bank account, it would drive traffic to keep the accounts alive.

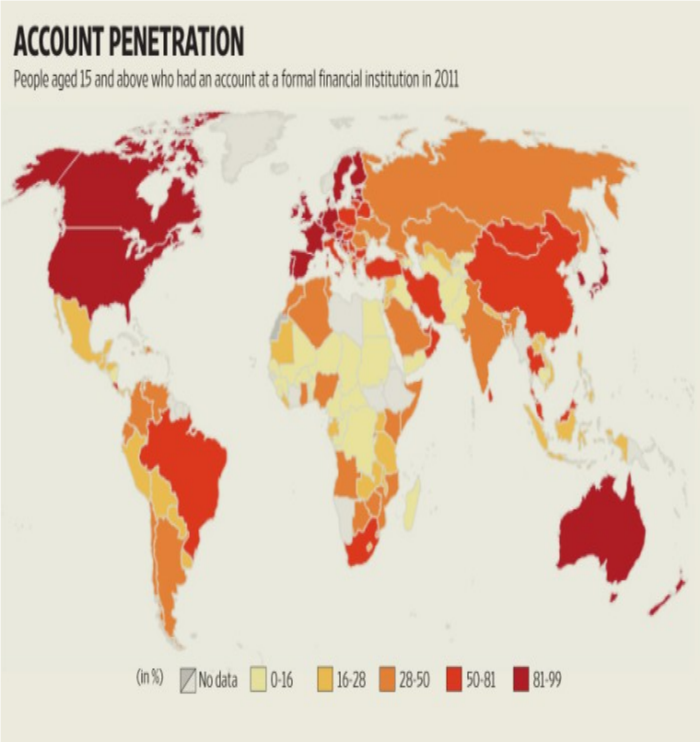
**INDIA, COMPARED TO THE WORLD**

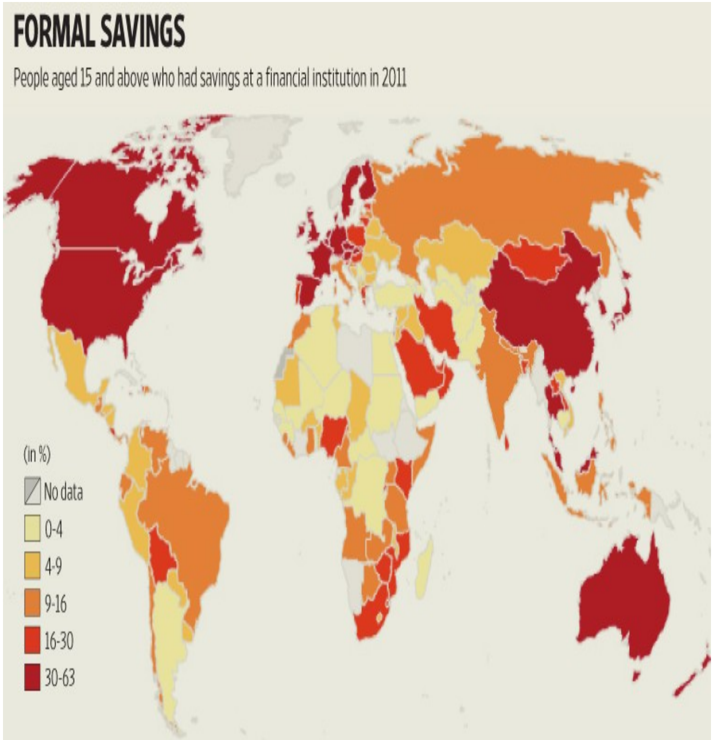
***"Unrestrained access to public goods and services is the sine qua non of an open and efficient society"***

India remains a vastly under-banked country. What matters most for households is not opening deposit accounts, but access to credit. It's in this regard that India's track record is abysmal. Its household debt-to-GDP ratio is a mere 8.9%, the lowest among its Asian peers.




Source: Citi Research

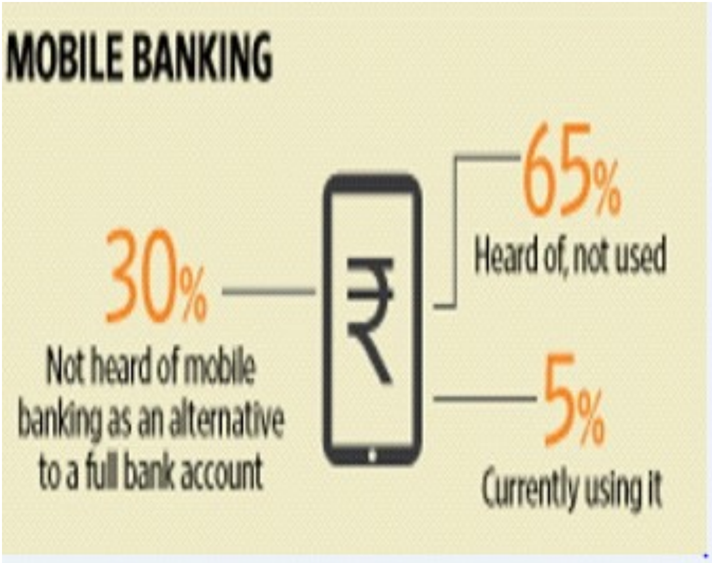



FUTURE SCOPE

M-Banking: One-third of India's 1.2 billion people have a bank account. Twice as many people - 900 million - own mobile phones.

TranServ was awarded the Aadhaar Governance Award instituted by UIDAI in 2012, for its work in large scale financial inclusion and direct benefits transfer programmes. It enabled real-time transactions through VISA and RuPay, authenticated by Aadhaar.




Source: Mastercard Research

# SUMMER INTERNSHIP EXPERIENCE ( LANGHAM CAPITAL)

-By Kartik Puri, IIFT

From the first day we step into the MBA journey, the significance of the summer internship is dawned upon us. For several students, this provides the first foray into corporate life. The first three months of the MBA are highly crucial as students prepare full throttle for the summer placements. I was focused on making my career in finance since I came from a commerce background and had prior experience of working in the financial research sector.

The selection process for the summer internship required capabilities in both technical and soft skills. Langham Capital, a boutique investment bank based out of Gurgaon conducted a case-study based GD that tested students on financial modeling and valuation. It was followed by a grilling 1 hour interview that focused on financial statement analysis and the motivation for working with an investment bank. The hurdle was passed and I waited to get the first glimpse into the world of investment banking.

During the 2-month stint, I worked for a start-up ecommerce firm as they looked to raise their first round of PE funding. This was a real-time transaction where I was treated as a full-time analyst and not an intern. Each day provided a new learning experience as I worked on preparing marketing collateral for the client including information memorandum, teaser, financial model and list of potential PE firms. Weekly team meetings and conference calls with other Langham bankers placed out of London and New York provided a holistic view of the investment banking industry.

The peer group at Langham was highly knowledgeable with lunch discussions hovering around new investments by clients and economic policies. I also gained insight on how several M&A's get holed up due to regulatory hurdles. The open-door culture at Langham allowed me to express my views and discuss nuances related to valuation and financial projections.

My tenure at Langham was of immense help as I sat for my final placement process. My interview at Flipkart for the Corporate Finance role revolved primarily around my internship and the experience of working in the ecommerce space was the primary reason for my selection.

# CHINA SLOWDOWN: EFFECTS ON INDIAN ECONOMY

-By U Sai Bharath and Aditya Chitta

IIFT, Kolkata

**Introduction**

China, the second largest economy in the world with a GDP of $9.24 trillion and with a contribution of 17.4% to the world exports, is the largest exporter in the world. Thus, quite fittingly it is called growth engine of the world. So, if it falters, the world economy slows down. According to the OECD if the growth rate of China decreases by 2 percentage points for the next two years the GDP of the world may contract by 0.3 percentage points per year (i.e. $224 billion).

**Reasons for Slowdown**

The last two years have seen a significant decline in growth rate of China. There has been a structural change in the labour force. China's population is aging- the average age of a Chinese worker is 37 years now; the growth of the employable labour force has decreased. Workers especially in the urban areas have been demanding more wages. All this has lead to increase in production costs. This coupled with the fall in real estate market has only exacerbated the downward trajectory of China's growth. Also the investment in the manufacturing sector has taken a hit after the Euro-crisis, which has induced a slowdown in the manufacturing sector. HSBC/Markit Purchasing Managers' Index (PMI) for China in December '14 was at 49.6, a shade below 50.0 which is a delineating level between growth and contraction. The growth rate for China is at a 24 year low at 7.4% and if experts are to be believed the bottoming out of the economy is yet to occur. The Chinese economy is undergoing a transition from an industrial to a post industrial economy in which the domestic as well as international markets can no longer support its high growth rate.

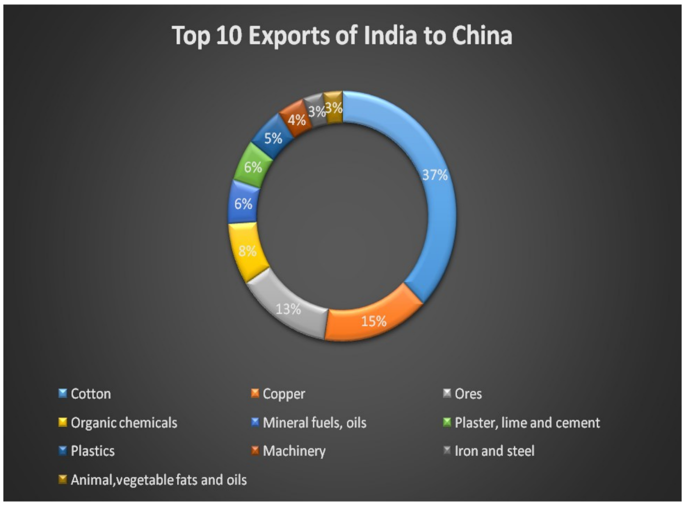
**Impact on India**

The falling domestic demand has compelled Chinese manufacturers to push their products at cheaper rates. The US has already invoked Anti-Dumping laws to keep a check on this. This would force cheaper Chinese goods into emerging markets. This has ramifications on the world economy and India being its close neighbor and a significant trade partner would be impacted considerably.

Trade with China accounts for 9% of the total trade by India. The falling demand for goods in the Chinese market has lead to a steep decline in India's exports to China, while the falling prices of various commodities have increased China's net exports. The trade deficit between India and China is being pegged in tunes of $36 Billion, with Indian exports to China at $15 Billion and imports at $51 Billion.

**Impact on Indian Exports**

The Slowdown in Chinese market has impacted commodity prices worldwide which remain at an all time low. They are expected to be quite low even through 2015. This would have a negative impact on India's exports. Let us examine its impact. The following are the top ten exports from India to China:

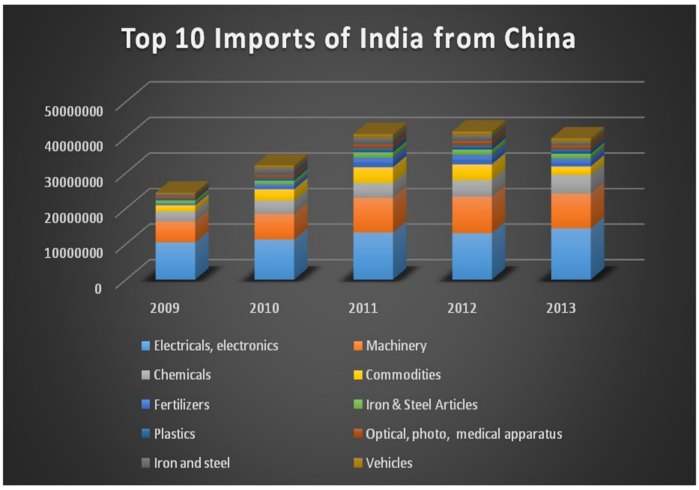



The Cotton Advisory Board (CAB) conservatively estimates India's exports in 2014-15 to be 9 million bales which is 23% lower than last year's export of 11.7 million bales. A large reason for this is attributed to the slowdown in buying from China because two thirds of India's cotton exports (6.2 million bales) go to China. However analysts believe that this may to some extent be offset by the growing demand from Bangladesh, Vietnam and Thailand's garment industries. This would also depend on whether Indian exporters are willing to scale down from their present cotton price which is 22 cents a pound higher than the global market level.

Indian Copper and Iron Ore exports to China are estimated at $ 3.7 billion and will take a hit following the fall in commodity prices. The clamping down by Chinese authorities on the stockpiling of Ores and the slowdown in real estate are all expected to impact the demand from China. The 30% export duty by Indian authorities has not helped matters much. Companies like Tata Steel and SAIL which have their own mines will be the worst hit but companies like JSW which buys iron ore from the open market might not be affected much. There has also been a reduced demand of precious metals and gems from China of which India is the largest exporter. The declining price of rubber would make tyres cheaper to manufacture in India.

**Impact on Indian Imports**

There would be a surge in the volume of imports from China. This would adversely affect the local manufacturers. The following are the top ten imports from China over the years:




The last few years have seen a widespread acceptance of Chinese products in India. The market would be flooded with cheap electrical and electronics goods. The second largest import from China is Capital Machinery. This would help India's production. It would be a boon that manufacturers especially in the Micro and SME sectors can lay their hands on manufacturing equipment at lower rates. Large Capital equipment importers however would find the going tough for them. The Indian Chemical Sector accounts for 8-9% of India's imports every year. A surfeit of Organic Chemical would compound India's trade deficit with China but on the upside it would be an enabler to many allied industries depending on cheap, processed organic chemicals.

However all is not gloomy on the industrial front. Weak Chinese industrial growth coupled with lower commodity prices gives Indian firms an opportunity to assert their manufacturing prowess. Low commodity prices would benefit automobile and its related ancillary industries. Manufacturers of consumer durables and capital goods would be rubbing their hands in glee.

**Can India compete with China in manufacturing?**

Prime Minister Narendra Modi's 'Make in India' campaign which aims to increase manufacturing growth to 12% to 14% over the medium term might find it harder than anticipated. The recent directive that all public agencies must procure electronic equipment domestically is a right step in that direction. However, as Chinese goods become cheaper, the market becomes more competitive thus, dissuading Indian producers.

What would be a pivotal element in the days to come would be how efficiently India is able to implement the GST bill. An efficient inter-state GST policy would create a truly national market for goods and services. It would make India a more lucrative place to invest in.

The slowdown has lead to a spate of consolidations in Chinese state owned corporations. To begin with, the China National Nuclear Corp. and China General Nuclear Power Corp merger and the China CNR Corp. and CSR Corp. merger, China's two largest train makers has revealed China's ambitions in taking on its foreign rivals even in these turbulent times. It is but apparent that they have their eyes set on plush gains from India's plans to get its first bullet train.

So, can India now compete with China in manufacturing?

China is an investment driven model; While, India is a consumption driven model. India has the advantage of lower minimum wages and a huge consumption friendly populace. China is right now going through a corrective transition. With the right policy decisions like easing of FDI norms, a friendlier shipping policy, a seamless GST and lower interest rates would trigger an exodus of manufacturers from China to India.

# ECONOMIC IMPACT OF SHALE GAS IN USA

-By Anmol Garg & Anand Shekhar
IIFT, Kolkata

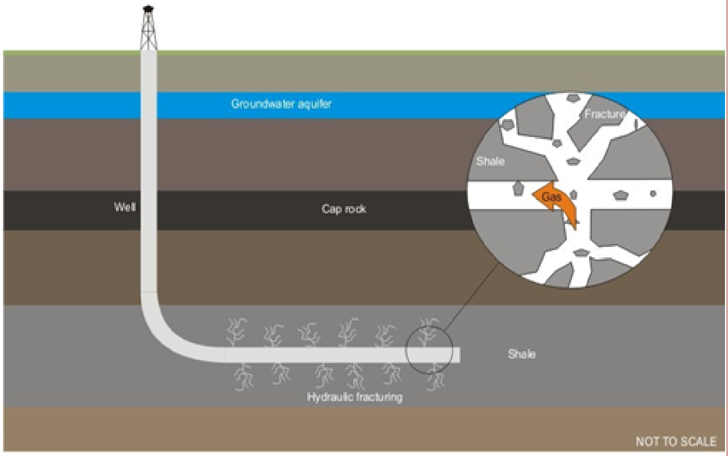
## Introduction

For a real long time in the recent history oil played an important role in the economy. Oil ruled politics, it got its own currency (Petro-dollars) and it still decides where the need of democracy is. But with dwindling oil reserves in the Arab world and Russian Arctic, disruptions over oil supplies, and increasing pressure for clean fuels driving US away from the traditional energy sources like Oil and Coal. Although the invention of shale technology and extraction of shale gas started as early as 1825, the first successful economical extraction started during 1990-2000 period. The improvement of technology played a very crucial role in the reduction of cost. The method of shale extraction is the most difficult and controversial today. But what makes shale that attractive today?

## History

The first extraction of Shale was done in NY using mild fracking. Shale gas is not the conventional Natural Gas. Natural gas can be easily extracted. It's a giant bubble where we've to pinch a hole and suck gas carefully. It's like a thick layered balloon with a small opening.

Shale gas is not that easy to extract. It is a gas trapped inside multiple rocks. Think about extracting air in the bubbles of the bubble wrap. We've to carefully blast all rocks away so that the trapped gas bubbles can be forced through the hole created. For this, the drilling has to be horizontal as the gas is trapped in a sediment called Devonian Rocks. As we know, these sediments are horizontal layers and hence the horizontal drill. This entire process is called fracking and it requires a lot of water and some dangerous chemicals.

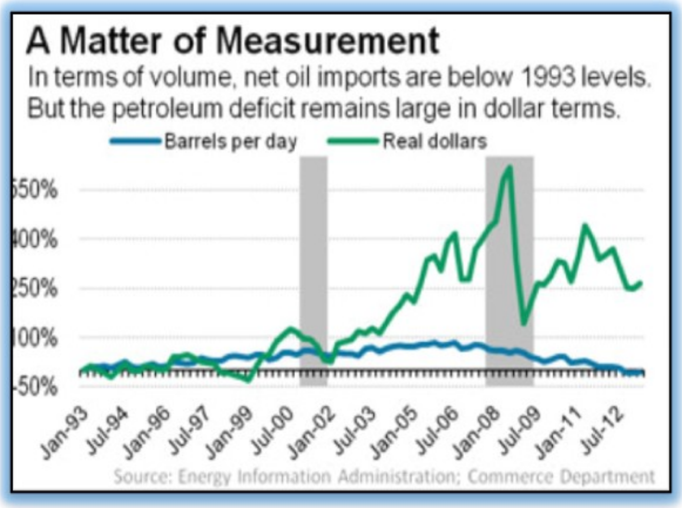



*Source 1https://www.dur.ac.uk/unconventionals/topics/shale_gas/*

## Impact on Traditional Fuels

The major impact the Shale gas creates is the drop on traditional fuel prices. Since the introduction of shale gas, the prices of natural gas dropped. Although they just got more popularity and profits since the new millennium, their prices started falling since 2009. And the fall is still continuing. This is attributed to the increasing popularity of the Shale Gas.

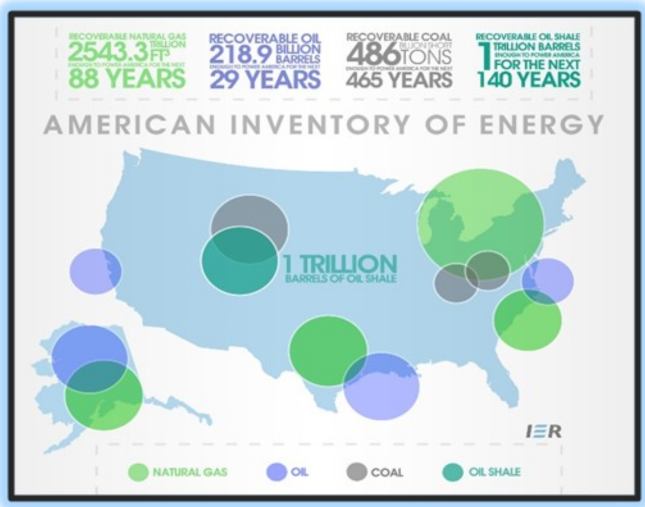
But interestingly, the prices of crude oil did not fall much as expected. In fact they are increasing and the US is paying dearly for these prices. Even the imports are reducing the amount of expenditure is still high. This might be the reason behind the increase in the shale production . This will help in reducing the trade deficits with the OPEC countries. US is importing almost same amount of oil compared to two decades ago. But the increase of payments tripled even after adjusting inflation. This trend might continue in the near future as the Arab countries might try to get more profit on the last remaining reserves. The spike in the graph has no relation to Middle East conflicts.




*Source 2 Wall Street Journal*

**Impact on American Energy Industry**

Only seven years before everyone predicted that oil consumption is going to peak as the American natural gas production declined due to high costs and low availability. The immediate effect of shale gas in the US is the diversification of energy. But a caution here. With increasing shale production, the Arab countries are now in danger. This is the main reason why Saudi decided to keep the oil prices low despite heavy losses to cash flow. It's not just Arabs; Even the American and European oil companies are feeling the heat. One way to reduce the loss of cash flow is to produce high. The France based Total S.A. company CEO announced that they are trying to increase the production by 30% by 2017. However ambitious the claim is, we now know the alternatives companies trying to stay in the business. The American industry will surely exploit the drop in the oil prices. The imports in the future might tend to rise if the oil prices still stay low.

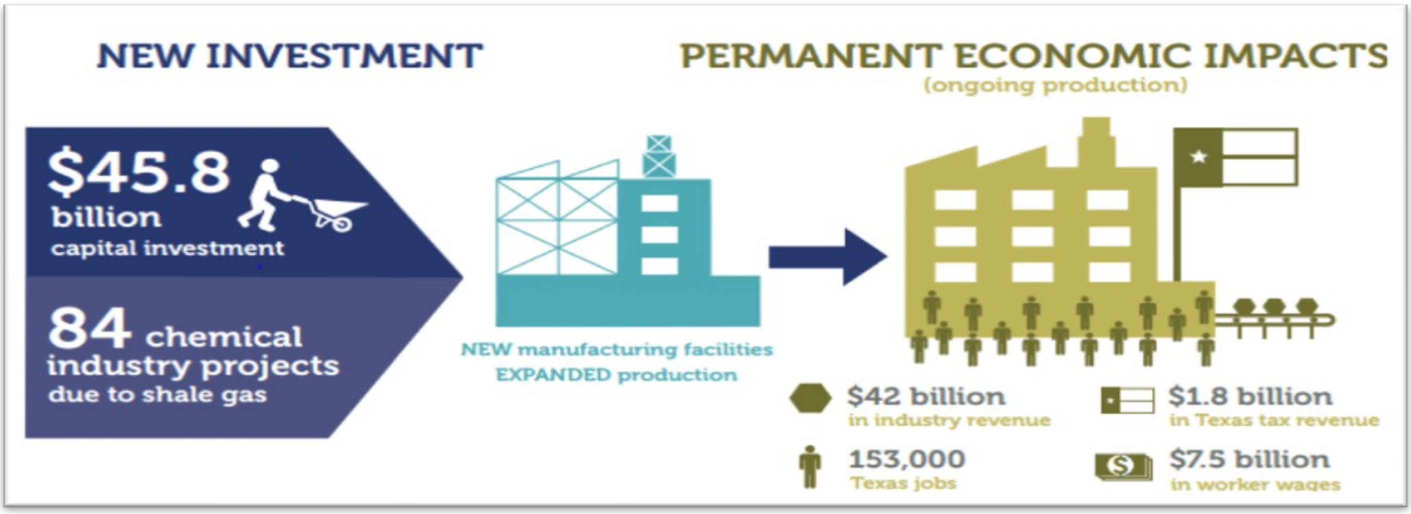



*Source 3 http://industryinfographics.com/*

But there seems to be no stopping to shale gas. Government of the US until now has put up no barriers to the production to save oil companies. Also, the Shale gas bubble is not bursting anytime soon as hoped by oil companies. Hence oil companies has to adjust space with the Shale gas. The infographic shows the amount of shale reserves US have. This will be enough to keep the US busy for another 100 years alone. Together with oil, shale will be a major contributor for the future American Energy industry. As the demand for energy is not going to recede anytime soon, exploring shale would be a greater advantage for USA and it will now have less impact of oil unavailability. As this gas is comparatively cleaner energy than the oil, we can expect this to sneak into domestic consumption market too.

**Impact on Overall American Economy**

The impact can be categorized into two parts




*Source 4 that is just Texas: http://chemistrytoenergy.com/*

1. Increase in Purchasing power/ income

2. Substitution effect.

The increase in the income due to the increase in the economy causes a positive trickledown effect. The USA can easily solve its unemployment problem clearly.

The substitution effect is due to the fall in the prices of goods due to cheaper production costs. The reduction in fuel prices leads to more production and ultimately more consumption. But the caveat here is not all industries can easily switch to gas immediately. Hence the ones which switched will have a cost advantage and consumers tend to buy these newly produced goods instead of the ones produced using oil. This will have some impact on productivity in many sectors.

As discussed already, American trade imbalances are going to settle due to Shale revolution. The imports are reducing or at least not growing as much as they should with respect to increase in the demand. May be uncle Sam will be able to clear up that $16Trillion debt.

A tough competition with china in the energy sector is the biggest concern for the United States. Contrary to popular belief, China is the biggest oil investor in Iraq. China is now in Africa too, helping nations explore oil at a very cheap rate. IT is sending millions of their citizens to work in these fields, providing technical knowhow to the local countries. To keep Chinese at bay, the USA has to force lower prices on oil.

**Hurdles**

As the IMF points out, the revolution in the US has caused natural gas prices to fall sharply there, even as they have risen in Europe and Japan. This is because gas, unlike oil, cannot be easily transported around the world, meaning that regional prices vary widely according to the location of the energy source.

In addition, improvement of GDP due to shale scenario over a long time sees no much difference. The shale revolution has to be observed cautiously as it might not be the panacea one expects it to be. The estimation of GDP change from 2012 to 2040 is only about 0.575% as an income effect. A multi-model comparison study by Stanford University came up with a meagre 0.46% of for the long-term GDP impact of shale gas.

Another major issue is that the environmental impact of shale gas. Shale extraction is one of the biggest concern for environment. Not only its unconventional style but also the scale is raising fears. It needs vast amounts of layers to be fractured and needs a huge dose of chemicals which are known carcinogenic. Without a proper watch, this might go on to become a second lead scandal in the energy industry.

**Conclusion**

The United States' gas revolution reminds us of the oil revolution in the early 1900s. It replaced coal as the primary energy source and gradually became the most popular energy source in the world. It forced coal to become cheaper. It even forced some coal mines across USA to shut down. But, in any case it is beneficial to the world. If USA can keep up the production and keep Saudis and Russians on their toes, the economy will surely grow and the world is going to be a better place both for the US and the third world countries.

# FIN TREND

***Shariah Compliant Funds: Ethics meets Economics***

Shariah Compliant Funds (SCF) is a type of mutual investment fund which conforms all of the requisites of Shariah law and also follows the principles of Islamic Finance. SCFs restrict investment only in Shariah-compliant companies by appointing a Shariah board and it must carry out an annual Shariah audit purifying certain prohibited types of income (e.g. interest) by donating them for charity. It never invests in companies which are involved in the business of gambling, alcohol, tobacco, pork and pornography. To run the fund, so, a significant amount of effort is required to compliance with Shariah principles, both at operating levels as well as underlying investments. Though Shariah may allow a small part of the investment to be done for those businesses but the profit earned due to the investment should be donated for charity.

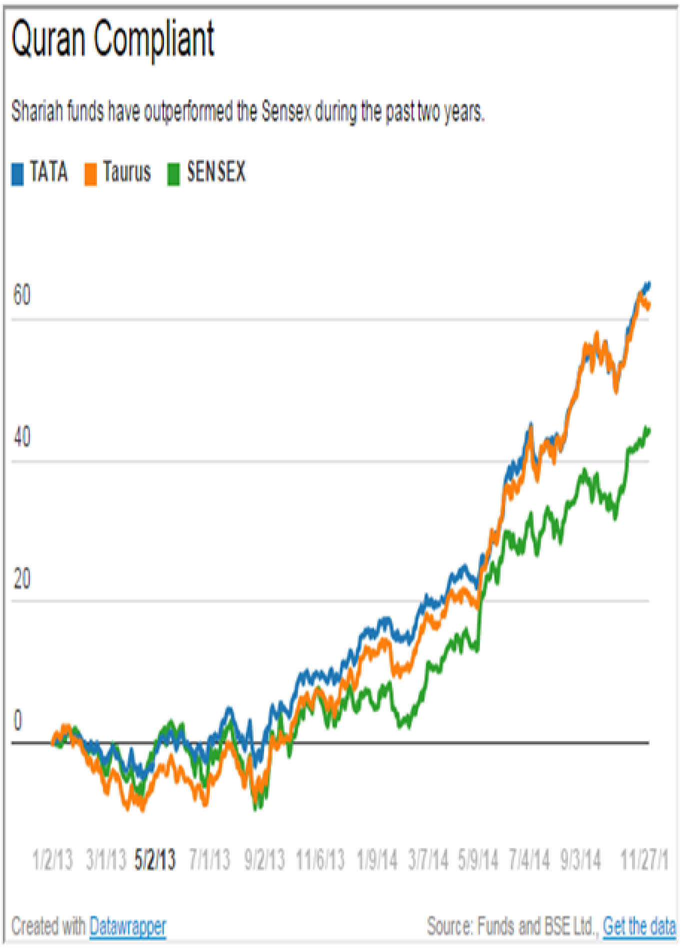
It has been in the market for around more than four decades but started gaining popularity only in the last five years. They first appeared in Malaysia in late 1960s and in the Middle-East in mid 1970s. High Net worth Individuals were the early adopters and it all started with individual mode having attracted by faith based investments.

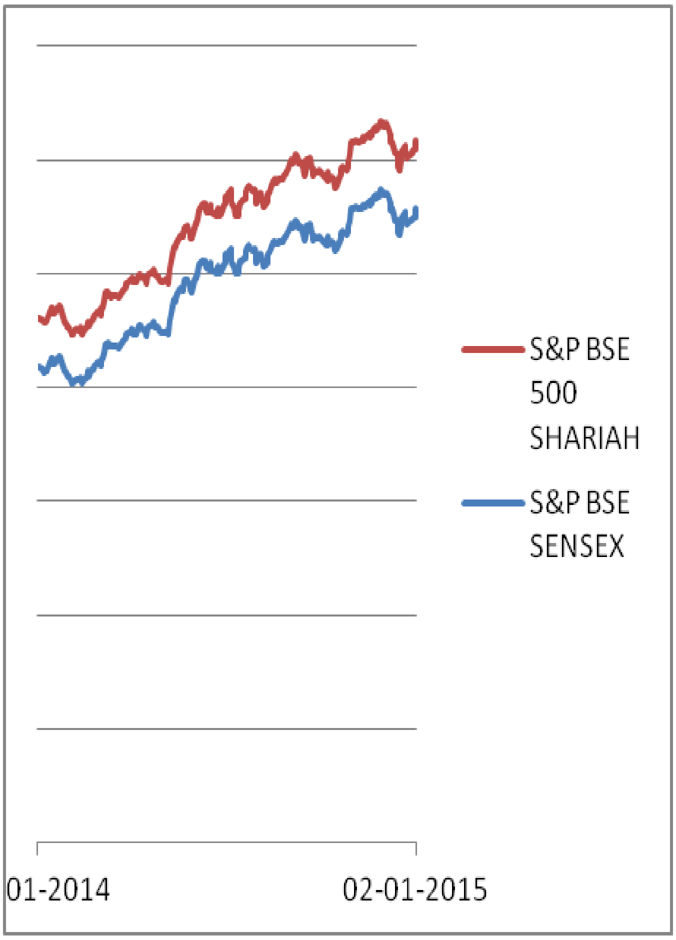
Currently the Muslims represent almost a quarter of the world population and only 1% of the financial assets are Shariah compliant, globally. Apart from this stark contrast another cause for increasing demand of these funds is the major savings by the oil exporting nations. Large Sukuk issuance in the recent years is also responsible for the surging popularity of SCF.

In India, Taurus Ethical Fund is the first of its kind which provided the investment option in compliance with Shariah laws. Goldman Sachs' GS S&P Shariah BeES fund also started operating in April, 2009. Tata Ethical Fund entered the market a bit late at 2010. Tata and Taurus already have raised $40 million since setting up the equity funds by targeting the 166 million populations in India. Another interesting fact is that not only Muslims but also Jains are heavily investing in these funds. But all those hustle and bustle started when State bank of India, the biggest public sector bank in India planned to launch an SCF called SBI Shariah Equity Fund on 1st December, 2014. SBI Funds Management Private Limited is a joint venture between SBI & Amundi Group SA, France. The scheme targets to provide medium to long term growth options in regular and direct plans. Now, let's look at it from a pure finance perspective.

All that matters to a perfect investor is the return on in-

# FIN TREND




All that matters to a perfect investor is the return on investment while investing in a mutual find or for that matter any financial scheme.

So even though these funds have restrictions regarding investments, still their performance has remained strong as they are allowed to invest in pharmaceutical, software and automobile companies which are amongst India's best run companies and biggest exporters. In addition to that there are more companies to invest in yet as the fund managers suggest the potential is still untapped. Still there are proponents who are emphasizing on the flipside of these types of fund.

Firstly, how a public sector, also the biggest, bank of a secular country can issue any service which is strictly targeted toward a specific religion or community and also adhere to some sort of religious practices. Though Mr. Raghuram Rajan, the incumbent governor of RBI, led a

# FIN TREND

panel of experts who recommended that the country should allow banking that complies with Islamic Finance, still these initiatives can hurt the sentiment of secularity when we talk about India.

Secondly, on one hand the prime minster Mr. Narendra Modi launches Jan Dhan Yojana to bring all the Indians under banking systems and encourage every Indian to join the mainstream banking; but on the other hand the same government allows state owned banks to offer financial products that appeal to religious identity. More broadly, instead of promoting the rather factious vision, India should do exactly the opposite. Rather than minimizing Muslim exposure to regular financial instruments, India should try to encourage more and more Muslims to enter the financial mainstream.

Now the ball is in the court of SBI as well as the government. They can either go for a silent burial and close the issue or encourage more similar funds by public and private banks and institution to maintain the fine balance of economics and politics.


By Pratik Mishra, IIFT-Kolkata

# 10 LATEST FINANCIAL EVENTS

- **India's E-Commerce Sector Awaits More Billion Dollar Babies in 2015**


From Amazon to China's Alibaba to Flipkart, everyone wants to have a pie of the burgeoning e-commerce market in India and consumers are not complaining with sweet sale deals coming their way.

No one has any doubt about future growth prospects of the e-commerce market in India and experts believe that the country may see many more billion-dollar entities in this space during the new year 2015, while expanding the size of this over $3 billion marketplace.

- **Planning Commission is now 'Niti Aayog'**


The NITI Aayog, which will replace the Planning Commission, will be responsible for formulating what the government described as "a Bharatiya approach to development". The new organisation - NITI stands for National Institution for Transforming India - is being seen as a think tank that will foster "cooperative federalism" rather than take a top-down approach.

- **Brazil's incumbent Dilma Rousseff wins by a whisker**


Brazilian President Dilma Rousseff has been re-elected by a whisker after a dramatic run-off and a tense campaign. Ms Rousseff, 66, won the closely-fought election with Aécio Neves, the leader of the Brazilian Social Democratic Party. The 51.6 win secured her second term and the fourth consecutive mandate of the leftist Workers' Party.

# 10 LATEST FINANCIAL EVENTS

- **Oil Price fall 46% in 2014, worst since 2008**


Oil prices fell and ended the year with the worst annual price drop since 2008, reflecting the global supply glut caused by slowing demand from China and the booming U.S. shale production. U.S. crude (West Texas Intermediate) settled down 85 cents to $53.27. It dropped 46% for the year. Brent was down 57 cents to $57.33. It fell 48% for the year.

- **Modi talks about 'closer South Asian integration' at SAARC Summit**

Prime Minister Narendra Modi stressed on closer regional cooperation between SAARC countries and suggested five pillars for achieving that goal.

"For India, our vision for the region rests on five pillars — trade, investment, assistance, cooperation in every area, contacts between our people — and, all through seamless connectivity," Mr. Modi said, in his inaugural address, in English, to the 18th SAARC Summit in Kathmandu.

- **Alibaba Claims Title For Largest Global IPO Ever With Extra Share Sales**


After claiming the record for the largest US-listed initial public offering, Alibaba Group can now say its record-breaking IPO was the biggest in the world. The company announced that underwriters had exercised an option to purchase additional shares at the $68 IPO price, boosting the total amount raised by Chinese e-commerce giant and its selling shareholders from $21.8 billion to $25 billion

# 10 LATEST FINANCIAL EVENTS

- **On Christmas, Obama marks end of Afghan combat**

President Barack Obama marked the end of more than a decade of combat in Afghanistan by paying tribute to America's military, telling troops on Christmas Day that their sacrifices have allowed for a more peaceful, prosperous world to emerge out of the ashes of 9/11.

At an oceanfront Marine Corps base in Hawaii, Obama told troops that while tough challenges remain for the U.S. military in hotspots like Iraq and West Africa, the world as a whole is better off because American troops put country first and served with distinction.

- **Flipkart kick starts the festive Season with 'Big Billion Day Sale'**

Flipkart.com, one of India’s most popular e-commerce websites has kicked off the festive season with its ‘Big Billion Day Sale’ on October 2014. Considered to be an unprecedented and one of its kind festive season sales, Flipkart is offering lucrative discounts on a wide range of products including the launch of some its exclusive range. The Big Billion Day Sale as the name suggests has been designed keeping in mind the high number of people purchasing goods online

- **India Inches Towards Manned Space Mission, Tests Crew Module**

Inching towards realizing India's ambition to send humans to space, ISRO today successfully tested an unmanned crew module on board an experimental mission of its heaviest rocket GSLV Mark-III that blasted off from here.

Around 730 seconds after it lifted off at 9.30 AM from the Second Launch Pad of the Satish Dhawan Space Centre here, the crew module--CARE (Crew Module Atmospheric Re-entry Experiment)--splashed down into the Bay of Bengal

- **PM Narendra Modi launches 'Make in India' campaign with portal, logo**

Prime Minister Narendra Modi launched his flagship 'Make in India' campaign to put the country prominently on the global manufacturing map and, in turn, facilitate the inflow of new technology and capital, while creating millions of jobs.

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