PRIMUS PARTNERS

POLICY NOTES

March 2021

Monthly Update

Core Inflation comes to fore!

Core inflation is a prime indicator of underlying long-term inflation, given how rising prices impact consumer income. Core inflation (which excludes food, fuel and light) increased to 5.6 per cent in February, from 5.3 per cent in January. Most economists are worried, and Moody's Analytics described this as "uncomfortably high". With all projections on GDP growth being optimistic and the economy rebounding, controlling this inflation may become a significant challenge. India and the Philippines are the exceptions in Asia when it comes to higher inflation. This is happening at a time when India is looking to continue to attract global capital, while the US 10-year Treasury yield recently hit the highest level since January last year. This will impact global money flow. It is also at a time when the US just announced a massive infrastructure spend of over US$2 trillion that also includes a proposal to pay for the package with tax increases. The US wants to raise the corporate income tax to 28 per cent and set a 21 per cent minimum levy on global corporate earnings. While the spending would be temporary, the tax hikes would be permanent - at least until new legislation is enacted to change them. The plan would also impose a minimum tax on the profits that US corporations earn overseas, increasing the rate to 21 per cent from roughly 13 per cent. Several measures have been included that would penalize companies that move assets and jobs offshore and eliminates current preferences to book profits overseas. All of this makes the role of mandarins at the Ministry of Finance and RBI interesting!. A recent quote from Federal Reserve Bank of Dallas' President Robert Kaplan may be very relevant. "A lot of what's going on right now is unprecedented, and I think the smartest thing I can do is keep an open mind, be humble and be open to learning and adjust my views as this unfolds."

A brighter future for India's 2 crore orphans

Less than 4,000 of these distressed children get adopted each year, with many others languishing on the streets or in Child Care Institutions (~20 per cent of which lack basic amenities). The Ministry of Women and Child Development is shining a spotlight on child development and care through its reform of the Juvenile Justice Act. With the streamlining of the adoption process and granting of rights to DMs and ADMs to authorize adoptions, we may be likely to see many more children get homes. Minimum qualifications of child welfare committees with structured DM oversight on the committees and Child Care Institutions are likely to aim at improved governance and performance of these institutions. Continued revamping and revitalization of the childcare ecosystem are expected through the Ministry's recently announced Mission Vatsalya.

President Biden 1st Press Conference, big event but the other statements were the real story.

Last week, we saw President Biden's much anticipated 1st solo press conference. However, the real story for India came from statements and actions outside of the press conference. This included the much-discussed "Putin is a killer" remark and his articulating "growing rivalry with China" as a critical challenge facing the United States, with Secretary Blinken describing China as "the biggest geopolitical test" of this century. We also saw the recent comment of the US Admiral chosen to lead the Pentagon's Indo-Pacific region stating that the Chinese threat to invade Taiwan is serious and more imminent than many understand. Additionally, recent news reporting that the Philippine military is sending light fighter aircraft to fly over hundreds of Chinese vessels in disputed waters in the South China Sea implies a significant shift in US stance with respect to China (especially for a Democratic administration). Coming back to the press conference, two of the biggest takeaways were the rather awkward response to him running for 2nd term and continued use of the word faith to answer the key question by the president. We believe President Biden is looking to be a one-term president keen to create a legacy which will be underwritten by a) Controlling the pandemic; b) Reintroducing the US as the World's policeman, and c) spending money (especially infrastructure and for bringing back global supply chains) to create jobs for Americans. All of these have a significant impact for India, perhaps positive for India in the short term (especially vis a vis China), with softening stance on CAATSA (assuming India continues to be a vital defence market for the US) and an attractive export market for Indian companies (supported because of continued spending), but it will also mean significant irritants to issues relating to perception on religious freedom and press freedom with vocal left leading Democratic base in the US, which will play on the "faith" and "beliefs" of the US President.

Privatizing BEML – will this be the benchmark?

The Government has set a disinvestment target of INR 1.75 lakh crore for FY22. BEML, a defence PSU (Mini-Ratna), forms one of the first disinvestments, thus providing a road map for future endeavours. As a framework, the bid's monetisation has been stripped, with land and other assets not being part of the strategic disinvestment. Government has also tried to calm workers that this will not lead to job losses (significant as most workers in these companies earn significantly more than their more efficient counterpart in the private sector). With a shareholding of 54.03 per cent, the Government will disinvest 26 per cent of the BEML stake, with management control transfer to a private entity. Since BEML is a listed entity, the acquisition of 26 per cent of stake by any investor(s) would trigger a mandatory open offer of 25 per cent, potentially providing majority holding to the investing entity.

BEML has three major segments with Mining & Construction (M&C) having revenue of INR 1,493 crores (49 per cent of the revenue share), Metro & Rail (M&R) with INR 1,105 crores (36.4 per cent) and Defence with INR 431 crores (14 per cent). It has a declared order book worth approximately INR 10,000 crores. This, Government hopes, will bring in serious players and provide significant proceeds.

It would be interesting to see how companies that have bid evaluate risk vs. return as therefore how they value BEML, given that most individual investing entities are unlikely to have an existing portfolio encompassing the expanse of BEML capabilities. This could also mean investments are likely to come about from entities who are looking at this as a "financial investment" with an intent to expand their capabilities into hereto unexplored avenues, or through a joint bid of entities with overall capabilities encompassing BEML portfolios. The issues will possibly get more complex in realising the management norms in the latter, while the former may increase incubation timelines. In both cases, there is potential for synergising the advantages, in market outreach, of a Government enterprise with the private bidder's inherent efficiency. The challenge will come in the Management of the enterprise wherein the intrinsic strengths of the hereto Government-mandated organisation (on socialist lines of governance) will be merged with the best of Corporate culture, to bring impetus to the company which has shown a Profit before Tax of about INR 24 crores, as against a sizeable revenue in 2019-20. In all, this paves a way to the realisation of Strategic Partnership in which the PPP Model comes into play with the Government on the Management Board to watch and assist while leaving the orchestration and running of the enterprise to the Private majority holder.

Self-Reliance in Indian Defence Sector: Strategic Planning in a Competitive Era

The Indian defence manufacturing industry is a significant contributor to overall manufacturing growth and is likely to further grow with rising national security concerns. As the country is steadily moving towards transforming itself to global economic power, the defence and homeland security sector has assumed a crucial role in long term strategic planning. Over the past few years, achieving self-reliance and indigenisation in defence manufacturing has been one of India's key objectives.

Self-reliance is a major foundation on which the military capability of any nation rests. To achieve substantive self-reliance in the design, development and production of equipment, weapon systems and platforms required for defence, India needs to create conditions conducive for the private sector to play an active role in this endeavour.

The indigenisation in the defence sector is increasing at a sluggish rate. Manufacturing of defence products depends heavily on imports from foreign vendors even though manufacturing capability exists. This is due to licensed production of equipment under Transfer of Technology, non-availability of technical specifications, delay in developing certified processes, etc. The Defence Ministry plans to put 101 defence items (artillery, guns and assault rifles) under import embargo to offer potential military hardware manufacturing opportunities to the Indian defence industry. This will boost domestic production and attract foreign companies to invest and set up their manufacturing facilities in India. Furthermore, India needs to modernise its armed forces and reduce dependence on imports.

Monthly Update

Can India's E-commerce sector Learn from its IT sector?

The Government has made a number of statements as well as initiated a large number of dialogues with a very diverse set of stakeholders as it moves forward to bring in an E-commerce Policy. The positions of many of these stakeholders seem too divergent to really reconcile. In that context, it will be informative to look back into history and see how India's Information Technology (IT) sector became India's crowing jewel is not only creating jobs but also in India's positioning in the world. India has fundamentally changed since the post-1991 liberalisation policy. It witnessed a new economic dawn in the subsequent decade and entered the global arena with full fervour. One sector that significantly drove India's rise was Information Technology. With a limited regulatory burden or oversight, the sector went on to dominate global markets. Digital India is where Silicon Valley has been investing in the last few years. Last year, Reliance raised $26 billion for its online and retail businesses from global investors, including Facebook and Google. Another $16 billion was paid by Walmart for the E-Commerce website Flipkart, and billions of dollars were committed to India by Amazon.

Digital India's success has enabled the E-commerce industry in the last decade. Today, India's E-Commerce industry is pegged to grow to $100 billion by 2024. Some estimates even peg an upshoot of up to $300 billion by 2030 that will drive jobs and also help MSMEs in a way policies have not. Today India hosts not only TCS, one of the most valued IT companies in world but also global giants like Accenture, whose largest workforce works in India,

The need of the hour as we go about developing the E-commerce policy is to be forward-looking, provide policy certainty (no change provision for a few years), not discriminate between foreign and domestic. The guiding principle should always be that as long as customers are winning and jobs are getting created, both homegrown companies and global e-commerce platforms need to feel confident in doing business in India and compete against each other as per the rule of law.

Housing for Labour – Not only a need but will redefine Urban Landscape

Labour housing has been a long-neglected subject in India's Housing Conversations. Industries employ a large number of migrant workers and families who do not have access to affordable and adequate housing near their workplace.

As a result, these migrant labour settle in informal settlements, unorganised accommodations, shanties, slums etc. These are generally illegal structures that are not very safe and densely populated (social distance norms non-compliant). They also lack basic facilities like water, sanitation, waste disposal mechanisms, and no health & hygiene protocols. There is a need to ensure adequate housing for labour in urban areas in India.

It is proposed that all industries employing more than 50 migrant workers should ensure adequate housing for their employees (Staff Quarters). Employers may adopt multiple innovative models for the same to ensure minimum upfront expenditure. For instance: Large Manufacturing Industries may contribute land (which they have in ample) and partner with Rental Management players who shall construct and operate the labour housing. HRA deducted from employees shall be utilised for monthly rental payments towards this housing stock. Through this model, employers shall have minimal capital cost and ensure decent accommodation for their employees.

The proposed strategy shall result in the overall development of staff quarters/employee accommodation across cities, thereby fulfilling the housing requirement of a large group of migrant labour.

Monthly Update

India Infrastructure will remain a strong story in pandemic recovery phase, and beyond

The focus on infrastructure will remain a vital part of India's growth and recovery story. As progress on the national infrastructure pipeline builds up, India is expected to become the third-largest construction market, requiring an investment of rupees 50 trillion across many sectors. In addition to transport and energy, there are significant developments in play for cross-sectoral programs. These include initiatives like housing for all, smart city mission, digital India, and an emphasised focus on the northeastern region and the Hill areas.

Indian infrastructure sector valuations remain high, which is seen in the form of sustained investor interest, especially for asset monetisation programmes. Both foreign and domestic investors are seen in the play. The National Highways Authority of India's wholly-owned special purpose vehicle DME Developers (DMEL) has raised INR 9,731 crore to part-fund the 1,276 km greenfield Delhi-Mumbai expressway. NHAI has disclosed that the major investors are a syndicate of Indian banks, State Bank of India, Punjab National Bank, Bank of Maharashtra and Axis Bank. NHAI will also launch its first Infrastructure Investment Trust (InvIT) in April 2021 to mop up INR 4,000-5,000 crore. It is felt that InvIT, along with the monetisation of operational assets via the toll-operate-transfer model and toll securitisation, would help boost non-debt resources. Participation from a wide class of foreign institutional investors can be expected.

Exhibiting further resolve to ensure adequate liquidity for infrastructure investments, the Government announced the setting up of India's new Development Finance Institution. Finance Minister Nirmala Sitharaman also urged the global multi-lateral development banks to work closely with the upcoming DFI for funding infrastructure.

With adequate capital, government focus, and a charged developer interest, India Infrastructure's next chapter has begun well.

Coping up with the shift of trends in the Indian automotive industry

The Indian automotive industry comprising the automobile and the auto components sector is one of the core industries of the Indian economy. It constitutes a central place in the entire MSME ecosystem. With the penetration of electric and hybrid electric vehicles into the sector, it becomes crucial for the traditional MSMEs of the auto-component sector to reconfigure their activities and redefine their supplier base to continue having a strong base in the market.

Taking into cognizance this transition towards EVs, the Indian auto component manufacturers must enter into other industries such as aerospace and defence, which can evolve as propitious markets at times of changing market dynamics and demands.

It will also be critical for the traditional players to undertake research and innovation, get access to newer markets and finance, and develop newer technologies such as offering electric mobility solutions to shift towards non-traditional sub-components to enter the new value chain.

Monthly Update

About Primus Partners

Primus Partners has been set up to partner with clients in 'navigating' India, by experts with decades of experience in doing so for large global firms. Set up on the principle of 'Idea Realization', it brings to bear 'experience in action'. 'Idea Realization'— a unique approach to examine futuristic ideas required for the growth of an organization or a sector or geography, from the perspective of assured on ground implementability.

Our core strength comes from our founding partners, who are goal-oriented, with extensive hands-on experience and subject-matter expertise, which is well recognized in the industry. Our core founders form a diverse cohort of leaders from both genders with experience across industries (Public Sector, Healthcare, Transport, Education, etc), and with varied specialization (engineers, lawyers, tax professionals, management, etc).

PASSION
for providing solutions to help clients achieve their goals

RESPECT
For all and alternate viewpoints

INTEGRITY
of thoughts and actions

MASTERY
of our chosen subject to drive innovative and insightful solutions

US
Representing the Primus collective, where each individual matters

STEWARDSHIP
for building a better tomorrow

Contact Details

Pooja Ahluwalia

pooja@primuspartners.in

Bengaluru
T1, GN, 25th A Cross,
25th Main, HSR Layout,
Bengaluru – 560102

Chandigarh
2nd Floor, Netsmartz,
Rajiv Gandhi Chandigarh
Technology Park,
Chandigarh – 160019

Delhi
Rear Block, Upper Ground
Floor,
ALPS Building,
56 Janpath,
New Delhi – 110001

Jaipur
86/SP, 63,
Behind Yes Bank,
Pratap Nagar, Jaipur,
302033

Mumbai
601, 6th floor,
Raheja Centre,
Nariman point.
Mumbai – 400021

Primus Partners India   @partners_primus