श्री LAKSHMISHREE

Gateway to your Financial Goals

Knock Knock... Omicorn Is Here !!

NOTE: Unlock your phone rotation to read the Report.

Invest Today,

For

Better Tomorrow !!

From Managing Director's Desk To Readers

Is Omnicron Variant Impacting Stock Market?

Domestic stock markets have witnessed a spike in volatility over the past few trading sessions as investors remain worried about the overall impact of the Omicron variant of coronavirus.

Both S&P BSE Sensex and NSE Nifty 50 went through two big crashes last week, following reports that the new coronavirus variant is spreading rapidly across countries. This has led to some countries imposing fresh restrictions as scientists have classified the new variant as highly transmissible.

Many market experts are worried that hasty decisions taken by countries to prevent the spread of the new Covid variant could ultimately end up hurting global economic recovery and markets. This, in turn, could have a damaging effect on the Indian stock markets as well.

STOCK MARKET CORRECTION LIKELY

Experts tracking the stock market recently predicted domestic stocks to correct further as Omicron has added to existing issues such as higher inflationary pressure, possible hike in interest rates and global supply disruptions.

While benchmark indices Sensex and Nifty rose on Wednesday after the country reported strong growth in the second quarter, markets remain highly volatile at the moment.

A poll of strategists, conducted by news agency Reuters, indicated that domestic equities will not recover from recent losses until after mid-2022. This is due to concerns over Covid-19 resurgence and global monetary tightening. Further corrections can also be expected in the next six months.

However, it is too early to predict how the new Covid-19 variant will impact the global economy. As scientists around the world try decoding the new variants, market experts have asked investors to exercise caution while placing new bets and avoid any panic-driven decisions.

EXPERTS ON FUTURE MARKET MOVEMENT

The Indian stock market has made a remarkable recovery following the two previous waves of Covid-19, with Sensex rallying nearly 20% year-to-date (YTD). However, the index has dropped around 8 per cent from its all-time high of 62,245.43 amid rising concern over the new Covid-19 variant.

The poll of 35 equity strategists suggested that the benchmark Sensex will again touch 60,450 by mid-2022, up over 5 per cent from Monday's close of 57,260.58.

We believe the inflation fear combined with the rise in Covid-19 cases globally may continue to trigger corrective moves in the following months.

However, the index is expected to rise and hit a high of 63,000 by the end of 2022. "We could see a 5-10% correction for Indian markets as valuations adjust to the moderation in earnings momentum.

-- Salil Shah

Managing Director
Lakshmishree Investments & Securities Pvt Ltd

Look What Our Research Analyst Has To Say…

S&P CNX NIFTY INDEX FUTURES (CONTINUOUS: CURRENT CONTRACT IN FRONT) · 1D · NSE O14823.10 H14975.00 L14760.10 C14953.35 +201.05 (+1.36%)

NIFTY CHART

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FOR THE MONTH OF DECEMBER 2021

Nifty has shaken out many weak hands in the fears of new corono virus.

It is trading in a falling channel and as and when we breach above the falling channel above 17600 the uptrend will resume and we shall hit fresh new all time highs. On the contrary any failure around the said levels will immediately plunge the index to channel bottom placed at 16450. On and all the markets will remain dominated by global news flows like update son corona virus, Crude and US federal reserve policy changes for the month of December.

Anshul Jain

Research Analyst

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Stocks To Watch

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1. Asahi India Glass Ltd.

Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
Auto Ancillaries	Rs 490.9	Buy in Rs 490-495 band & add more on dips to Rs 437-442 band	Rs 538	Rs 581	2 Quarters

Shree Varahi Scrip Code	
BSE Code	515030
NSE Code	ASAHIINDIA
Bloomberg	AISG IN
CMP Nov 18, 2021	490.9
Equity Capital (cr)	24.3
Face Value (Rs)	1
Eq. Share O/S (cr)	24.3
Market Cap (Rs cr)	11934
Book Value (Rs)	59.2
Avg.52 Wk Volume	207,000
52 Week High (Rs)	533.0
52 Week Low (Rs)	230.3

Share Holding Pattern % (Sept, 2021)	
Promoters	54.3
Institutions	2.5
Non Institutions	43.2
Total	100.0

Our Take...

Asahi India Glass (AIS) is present across the entire value chain of architectural and automotive glass. The company has been introducing new products looking at the changing life styles and customer demands and in order to stay competitive and relevant in the market. Slowdown in automobile sales and improvement in real estate industry has led to increased revenue share of the float glass business which has a higher margin.

Asahi has a dominant 74% market share in Indian passenger car glass market and is the 2nd largest producer of architectural glass in India (FY21 market share ~18%, up from 16% in FY20). Ambitious investments in the affordable infrastructure space by the Government and increasing volumes in the real-estate industry are likely to be the growth drivers in the coming years. The company has shown resilience and focused on generating incremental benefits on the back of product diversification and cost reduction initiatives. The company had commissioned phase-I of operations at Gujarat plant in H2FY22, which is expected to provide incremental capacities of 0.7mn sq.mtr. for tempered glass and 0.8mn pieces for laminated glass from FY22 onwards. With capex done, the company is paring down its debt levels. It has reduced its borrowing in H1FY22 by Rs 157cr to Rs 1099cr. Further, during FY21, the company had replaced some of high-cost and shorter tenor term loans with low-cost and longer tenor loans to ease its future repayment obligations, exhibiting financial flexibility.

The company is evaluating further expansion opportunities over the next 3-4 years including a greenfield solar plant in partnership with Vishakha group. Its joint strategic understanding is to leverage the entire solar glass value chain of Vishakha Group and its associates / promoter companies and the techno-commercial knowhow of AIS, with a target to set up India's largest solar glass manufacturing plant with the most competitive costs. The project is progressing well on schedule and it should commission the first green-field plant at Mundra, Gujarat within the next 15-18 months.

On January 8, 2021, we had initiated coverage on the stock (Link) with a recommendation to 'Buy on dips to Rs 262-264 band and add more in Rs 233-235 band' for base case fair value of Rs 293 and bull case fair value of Rs 317. The stock entered our buying range on January 18 and achieved base case target on February 3 and bull case target on March 4, 2021.

Valuations...

AIS will be a key beneficiary of growth in passenger vehicles production in India, coupled with rise in content led by premiumisation and rising share of SUVs. Asahi's content per vehicle will rise with the improving segment mix and rise in penetration of value added glasses like IR and UV shield glasses. The demand outlook for the architectural glass has improved with the revival in residential real-estate demand. For the medium term the recent four initiatives being considered by the company could lead to healthy growth in top and bottom line. We expect PAT CAGR of 51% over FY21-24E, led by EBITDA margin improvement on cost savings, import restrictions on float glass and reduction in net debt. Revenue is expected to grow at 19% CAGR driven by higher share of float glass business. We expect RoE to improve from ~10% in FY21 to ~21% in FY24. AIS faces no threat from the advent of Electric Vehicles. Its presence in high value architectural segment will help grow revenues and maintain high margins. We feel investors can buy the stock in the band of Rs 490-495 and add on dips to Rs 437-442 (32x Sep-23E EPS) for a base case fair value of Rs 538 (32.5x Sept23E EPS) and bull case fair value of Rs 581 (35x Sep-23E EPS).

Financial Summary…

(RsCr)	Q2FY22	Q2FY21	YoY (%)	Q1FY22	QoQ-%	FY21	FY22E	FY23E	FY24E
Revenues	796.5	638.8	24.7	603.8	31.9	2,421	3,018	3,466	4,033
EBITDA	186.9	122.2	52.9	118.4	57.9	435	583	690	839
APAT	81.1	37.3	117.7	35.3	129.6	133	255	345	461
Diluted EPS (Rs)	3.3	1.5	117.7	1.5	129.6	5.5	10.5	14.2	19.0
RoE (%)						9.7	16.5	19.1	21.4
P/E (x)						89.7	46.8	34.6	25.9
EV/EBITDA (x)						30.2	22.8	18.8	15.1

Income Statement…

(Rs Cr)	FY20	FY21	FY22E	FY23E	FY24E
Net Revenues	**2643**	**2421**	**3018**	**3466**	**4033**
Growth (%)	**-9.3**	**-8.4**	**24.7**	**14.8**	**16.3**
Operating Expenses	2209	1987	2436	2776	3194
EBITDA	**435**	**435**	**583**	**690**	**839**
Growth (%)	**-14.8**	**0.0**	**34.0**	**18.4**	**21.6**
EBITDA Margin (%)	**16.4**	**17.9**	**19.3**	**19.9**	**20.8**
Depreciation	137	132	150	160	169
Other Income	13	36	15	17	20
EBIT	**311**	**339**	**448**	**547**	**690**
Interest expenses	146	143	116	105	94
PBT	**161**	**195**	**332**	**441**	**596**
Tax	19	74	96	119	161
PAT	**142**	**121**	**236**	**322**	**435**
Share of Asso./Minority Int.	12	12	19	23	26
Adj. PAT	**154**	**133**	**255**	**345**	**461**
Growth (%)	**-19.2**	**-13.4**	**91.5**	**35.3**	**33.6**
EPS	6.3	5.5	10.5	14.2	19.0

Balance Sheet...

As at March (Rs Cr)	FY20	FY21	FY22E	FY23E	FY24E
SOURCES OF FUNDS					
Share Capital	24	24	24	24	24
Reserves	1278	1415	1634	1930	2333
Shareholders' Funds	**1302**	**1440**	**1658**	**1954**	**2357**
Minority Interest	-14	-16	-19	-23	-27
Borrowings	1388	1255	1380	1255	1065
Net Deferred Taxes	-87	-51	-51	-51	-51
Total Source of Funds	**2590**	**2628**	**2968**	**3135**	**3344**
APPLICATION OF FUNDS					
Net Block & Goodwill	2035	2219	2286	2316	2304
CWIP	489	262	131	66	33
Investments	55	69	68	83	108
Other Non-Curr. Assets	37	31	66	76	89
Total Non Current Assets	**2615**	**2581**	**2551**	**2541**	**2534**
Inventories	14	58	52	185	279
Trade Receivables	722	654	744	836	972
Cash & Equivalents	261	268	347	380	442
Other Current Assets	163	161	227	261	304
Total Current Assets	**1161**	**1141**	**1371**	**1662**	**1997**
Trade Payables	578	639	645	712	773
Other Current Liab & Provisions	608	455	309	355	413
Total Current Liabilities	**1186**	**1094**	**954**	**1068**	**1187**
Net Current Assets	-26	47	416	594	810
Total Application of Funds	**2590**	**2628**	**2968**	**3135**	**3344**

2. Siyaram Silk Mills Ltd.

Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
Textiles	Rs. 461	Buy in the band of Rs.460-465 & add more on dips at Rs.410	Rs. 503	Rs. 559	2 Quarters

Shree Varahi Scrip Code	
BSE Code	503811
NSE Code	SIYSIL
Bloomberg	SIYA IN
CMP Aug 27, 2021	461
Equity Capital (Rs cr)	9
Face Value (Rs)	2
Equity Share O/S (cr)	4.5
Market Cap (Rs cr)	2161
Book Value (Rs)	173
Avg. 52 Wk Volumes	190,750
52 Week High	518
52 Week Low	138

Share Holding Pattern % (Sept, 2021)	
Promoters	67.1
Institutions	12.6
Non Institutions	20.3
Total	100.0

Our Take…

Siyaram Silk Mills Ltd (SSML) has one of the most prudent capital allocation track record in the textile and apparel space in India. Despite the covid-19 pandemic related turmoil, it operated at a Net D/E of 0.1x as on FY21. It has been in a constant endeavor to establish itself as an asset light and a pure branded fabric and apparel player in the highly commoditized and working capital intensive textile industry. SSML is one of the largest poly viscose blended fabric player in India. Its portfolio of products include suiting fabrics, shirting fabrics, casual and formal apparels and home furnishing. SSML has registered a smart recovery in earnings post the 2nd covid-19 wave whereby it reported best ever quarterly performance in Q2FY22. In Q2FY22, it reported a PAT of Rs. 52Cr which was mainly driven by strong operating leverage and its lean cost structure. SSML has positioned its products mainly in the mid-market whereby it competes directly with unorganized and regional fabric players. Its strong balancesheet, deep penetration with consistent and focused approach toward brand building were the key growth drivers for the company. Over FY10-20, it had undergone a cumulative investment of ~Rs. 600Cr behind A&P activities which accounts for 4% of its cumulative revenues. Key demand drivers like social gatherings, marriage season and festivals are likely to play out in H2FY22.

Valuations…

Going forward, we are positive on the future growth prospects of SSML and we expect it to be a key beneficiary of the unorganized to organized shift in a highly fragmented textile and apparel industry. The shift from un-organized players to organized is a big opportunity as many smaller un-organized players have been impacted by liquidity and survival issues, which can lead to a sustainable tailwind resulting in market share gains for larger organized players like SSML. Further it aims to improve its efficiency and improve its working capital requirements by reducing its exposure to the consignment driven modern trade segment (for the branded apparels business) which is highly working capital intensive. SSML's core strategy is to consistently invest behind its brands, enhance its product mix and have a deeper penetration thereby leveraging its distribution network in the traditional retail channels.

Margins may dip a bit going forward as there could be some normalization of marketing spend. Also the low cost inventory benefit enjoyed by the company in Q2FY22 may not be available going forward. In our view, SSML's revenue and EBITDA is likely to record a growth of 23% and 73% CAGR over FY21-24E while PAT for FY24E is likely to reach Rs. 183Cr v/s Rs. 3.5Cr in FY21 and Rs.69Cr in FY20. Along with this, we expect the company to benefit from strong operating leverage and generate consistent FCF with improvement in working capital and ROCE from 7% in FY20 to 19% by FY24E.

For Siyaram Silk Mills Ltd its recommended to buy at LTP at Rs 349 and add further on dips to Rs. 311 for base case target of Rs 395 and bull case target of Rs 431. The stock has achieved its bull case target on 13th July 2021. Given the healthy growth outlook and strong set of numbers in Q2FY22, we re- iterate our positive view on the stock and expect the stock to further get re-rated. Consequently, we have now revised earnings and increased the target price for SSML. We feel investors can buy the stock in the band of Rs. 460-465 and further add on dips at Rs. 410 for a base case fair value of Rs. 503 (13.5x Sept FY23E) and bull case fair value of Rs. 559 (15x Sept FY23E) for a time horizon of 2 quarters.

Financial Summary...

Particulars (Rs Cr)	Q2FY22	Q2FY21	YoY-%	Q1FY22	QoQ-%	FY20	FY21	FY22E	FY23E	FY23E
Total Operating Income	480	174	176	233	106	1699	1089	1609	1814	2013
EBITDA	85	-6	-1544	29	192	167	54	253	259	278
Depreciation	16	16	-1	15	6	73	61	64	67	69
Other Income	7	12	-46	8	-19	34	41	35	38	42
Interest Cost	5	9	-47	5	-5	43	30	17	10	6
Tax	18	-5	-490	4	360	16	0	52	55	61
APAT	52	-14	-471	13	301	69	3	155	165	183
Diluted EPS (Rs)	11.2	-3.0	-473.3	2.6	330.8	15.3	1.1	33.1	35.2	39.1
RoE						9%	0%	19%	18%	19%
P/E (x)						30	407	14	13	12
EV/EBITDA						13	42	9	9	8

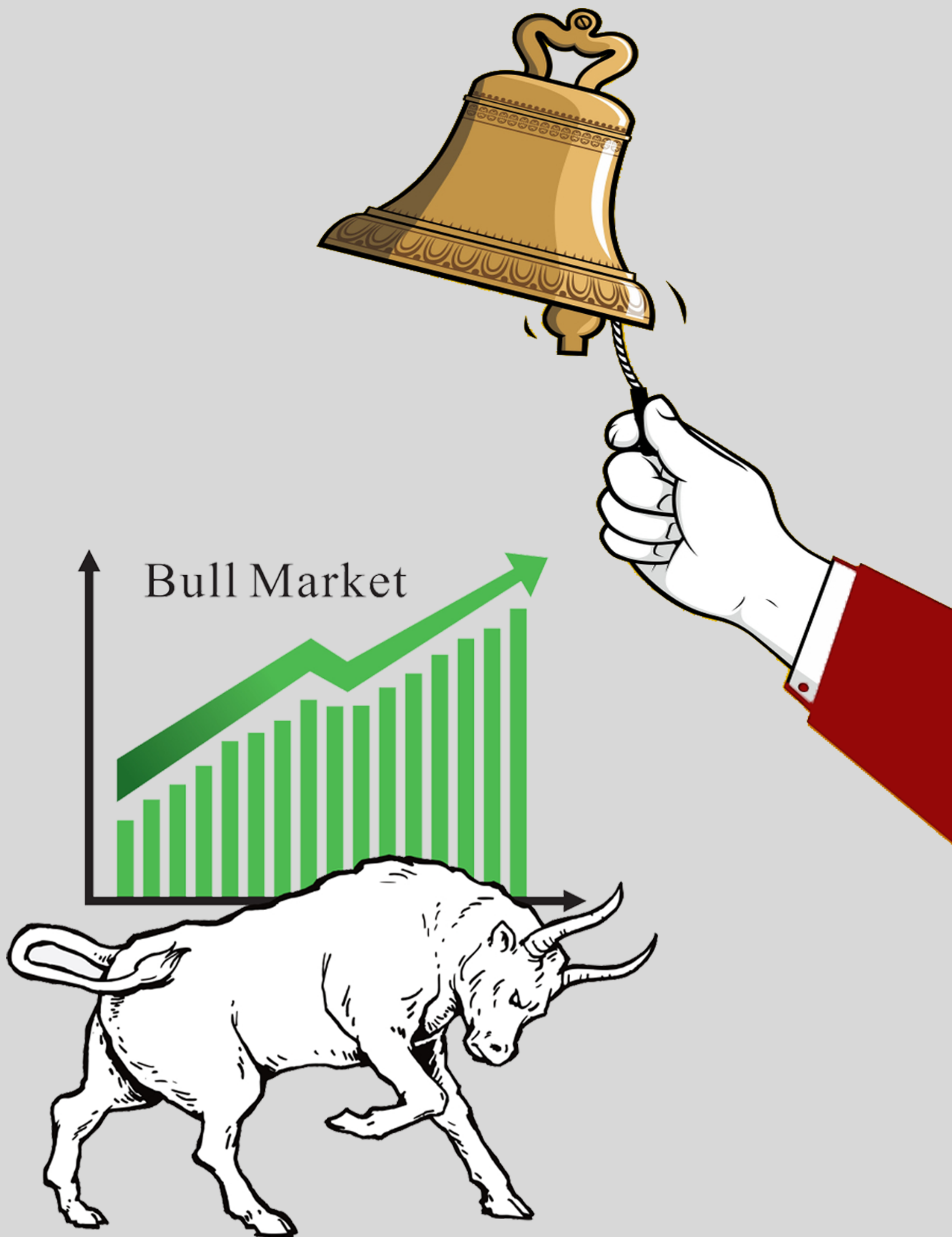
Income Statement...

(Rs Cr)	FY20	FY21	FY22E	FY23E	FY24E
Net Revenues	**1699**	**1089**	**1609**	**1814**	**2013**
Growth (%)	-6%	-36%	48%	13%	11%
Operating Expenses	1532	1035	1356	1554	1735
EBITDA	**167**	**54**	**253**	**259**	**278**
Growth	**-30%**	**-68%**	**372%**	**3%**	**7%**
EBITDA Margin	**9.8%**	**4.9%**	**15.7%**	**14.3%**	**13.8%**
Depreciation	73	61	64	67	69
EBIT	**94**	**-8**	**189**	**192**	**208**
Other Income	34	41	35	38	42
Interest expenses	43	30	17	10	6
PBT	**85**	**3**	**207**	**220**	**244**
Tax	16	0	52	55	61
RPAT	**69**	**3**	**155**	**165**	**183**
APAT	**69**	**3**	**155**	**165**	**183**
Growth (%)	-31%	-95%	4544%	6%	11%
EPS	15.3	1.1	33.1	35.2	39.1

Balance Sheet…

As at March	FY19	FY20	FY21	FY22E	FY23E
SOURCE OF FUNDS					
Share Capital	9	9	9	9	9
Reserves	758	758	851	933	1025
Shareholders' Funds	**767**	**767**	**860**	**942**	**1034**
Long Term Debt	428	79	159	99	59
Other Liabilities	82	71	78	86	94
Minority Interest					
Total Source of Funds	**1276**	**917**	**1097**	**1127**	**1187**
APPLICATION OF FUNDS					
Net Block & Goodwill	548	469	445	413	373
CWIP	4	3	3	3	3
Other Non-Current Assets	21	52	80	100	111
Total Non Current Assets	**573**	**523**	**528**	**515**	**487**
Current Investments	25	37	37	37	37
Inventories	428	255	441	447	469
Trade Receivables	324	261	397	422	441
Cash & Equivalents	14	13	-4	28	111
Other Current Assets	133	93	121	145	161
Total Current Assets	**923**	**659**	**991**	**1080**	**1219**
Trade Payables	182	176	198	199	221
Other Current Liab & Provisions	38	89	224	269	297
Total Current Liabilities	**220**	**265**	**422**	**468**	**518**
Net Current Assets	703	393	569	612	701
Total Application of Funds	**1276**	**917**	**1097**	**1127**	**1187**

This Might Impact Your Investments !!



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India, US make the right moves to improve trade ties

At a recent event held in New Delhi, minister of commerce and industry Piyush Goyal stated he was eyeing an ambitious bilateral, trade target of trillion dollars between India and the United States by 2030. Currently, that number is ~$150 billion.

Goyal stated that “posterity would hold us responsible for not getting these two democracies together”, and that it behoved Washington and New Delhi with their shared democratic values, the diaspora connect, and synergy across technology and innovation to further this trade partnership, in order to benefit the global community at large.

On November 23, the US-India Trade Policy Forum (TPF) resumed dialogue after a hiatus of four years, after US Trade Representative Katherine Tai’s maiden visit to New Delhi as US President Joe Biden’s trade czar. Tai and Goyal put out a joint statement after the twelfth ministerial-level TPF, and espoused a shared vision for “the future of the trade relationship”, as bilateral merchandise trade in the current year is poised to cross the $100 billion mark.

Goyal touched on the reforms and progress made by the Government of India, namely the infrastructure boosts through schemes such as Gati Shakti, along with the $1.5 trillion National Infrastructure Pipeline (NMP) in green and brown field projects. The creation of an asset reconstruction company to resolve bad assets in the banking system, reducing corporate tax to 15 percent, removing retrospective taxation, and moving towards a simplified tax regime was welcomed.

The elephant in the room was the trade deal or a free trade agreement (FTA), where Goyal reminded that India has many such agreements in place. India currently has an FTA with Japan, and there is an early harvest deal with Australia, and the target is to have an FTA by the end of 2022.

Outside the Quad, India has the India-ASEAN FTA agreement with the 10 Southeast nations, an FTA with South Korea, and even a SAFTA neighbourhood agreement. There are discussions in advance stages for FTAs with the United Arab Emirates (UAE), the United Kingdom, and the European Union.

While India has inherently been accused of being protectionist, and abjuring from larger trade deals such as the Regional Comprehensive Economic Partnership (RCEP), it still continues to engage with RCEP members in all sincerity. In nutshell, New Delhi says it prefers an ‘honest system instead of an opaque system’, alluding to China’s presence in the trade pact, and the access Beijing would receive to Indian market if India were to have signed the RCEP.

Goyal said that India wants to deal with “likeminded democracies, that support transparent, and rules based international order.”

When it comes to trade between India and the US, it’s best described in a Frostesque sense, as both have “miles to go, before they sleep”. The US has long argued for key market access for agricultural produce, dairy products, medical devices, and high-end electronics. New Delhi feels it’s prudent to start small with an early harvest deal. India wants the resumption of export benefits under the Generalised System of Preferences (GSP) programme.

Goyal recalled how under the Donald Trump administration, there were harbingers of such a deal fructifying but quipped how the red tape, and that too not from the Indian side, precluded it from happening.

But there was progress at the 12th ministerial-level meeting of TPF, as both sides agreed to resolve differences on outstanding market access issues for agriculture and non-farm goods, protection of intellectual property rights, and encouraging digital trade. India once again highlighted its interest in restoration of its beneficiary status under the

US GSP programme, as Tai and Goyal agreed to hold TPFs at regular intervals to address the finer nuances. The TPF has now reactivated working groups on agriculture, non-farm goods, services, investment, and intellectual property.

Goyal had earlier stated that India was ready and willing to expand the economic partnership in the spirit of reciprocity, and equality. At a time of rebuilding resilient supply chains, as the recent Quad summit touched, the clarion call is for India, and the US to build on what Goyal described as the five I's: intent, inclusion, investment, infrastructure, and innovation.

GDP catch-up is just about while consumption decline deepens

The GDP outturn for July-September showed the economy grew 8.4 percent in the quarter on annual basis, and 10.4 percent over the preceding quarter. Against a deep contraction (-7.4 percent) last year, the quarter-on-quarter improvements in private consumer and business demand were a respective 9 percent and 12 percent, while government spending increased by10 percent with exports at 8.4 percent.

Private consumption and fixed assets creation added a respective 4.7 and 3.5 percentage points to GDP growth in the quarter, with net exports at -6.5 points. The supply side rebound was also broad-based on annual basis, with the quarter-on-quarter performance of some components, viz. trade, hotels, transport, communication, etc. and manufacturing standing out.

Encouraging as the data may be, it is superficial over the deep troughs of one year ago. Compared to the pre-pandemic levels, the overall growth catch-up is a bare 0.33 percent rise in correspondence. Assessments of post-pandemic economic performance have to be reserved at this point as not only did the COVID-19 second wave partially spill into the second quarter, but many services also remained restricted, un- or partially-opened. In particular, the comeback of the trade, transport, and hospitality sectors that are major employers of the informal, unskilled, and low-income population, and which largely remained without meaningful policy support through the pandemic, is yet to be fully observed — the segment was -9 percent below July-September 2019. A truer picture of economic recovery will have to await the current quarter's performance.

Two features are noteworthy at this point, and what they augur for the future path of recovery. The first is the evolution of consumer demand. This reflects a continuation or rather, a worsening of the deterioration that had set in well before the pandemic. The robust quarterly rebound masks the extent of depression in consumer spending, which measured -3.5 percent below its level two years ago along with an eroding share in aggregate expenditure.

The second is inflation. The GDP deflator rose 9.1 percent year-on-year, and stood 11.8 percent higher over the September 2019 quarter. The price growth is an adverse portent for consumer demand, which it is likely to blunt. Incomes have not only fallen below previous levels but even the meagre spending capacities are being swept away by higher prices of goods and services.

Both have a bearing upon demand endurance once the distortions induced by the pandemic have worn off. One, the likelihood of consumption restoring to former strength is not assured at this point. Several indicators point to this; for example, the lagged official as well as contemporary private data on unemployment show this is still high, the depressed two-wheeler vehicle sales, and the feeble growth of fast-moving consumer goods in September quarter, among others.

Two, there's reason to be apprehensive about what will propel growth — necessary for income improvements that majorly fire consumption that in turn, feeds into future investment. Government spending amounts are too small relative to the depth of demand decline for a meaningful impetus – in real terms, this is -17% over September 2019

quarter for instance; moreover, this has run its course with debt levels in excess of 90 percent of GDP and set to consolidate further on.

Three, the sudden developments about a new, seemingly potent mutation of the coronavirus (Omicron) are not a good augur for inflation, which could get aggravated by more containment restrictions. Four, the positive spark to demand from exports – 17 percent growth over the matching 2019 quarter — could be dented by another layer of uncertainty imposed by Omicron.

The weight upon consumption to uplift growth beyond the initial outburst after reopening is considerable in the light of these settings. Here, sustained export performance, which can impart a strong income effect to both consumption and investment, is of paramount importance in forthcoming months.

The just-released manufacturing PMI for November, which rose at its fastest pace in 10 months and 1.7 points over October to 57.6, is a mixed guide in the context - new export orders rose slightly at a weaker pace (quite similar across Asia) and domestic demand was the primary driver with intense cost pressures and decline in sentiments to a 17-month low.

Considering the fast rebound of manufacturing and exports in September quarter GDP outturn, the overall signs of weakening demand and a clouded outlook suggests keeping fingers crossed for a durable recovery ahead.

Cryptocurrency | What happens when RBI issues a digital currency?

The markets have been buzzing with the Government of India’s new Bill, ‘The Cryptocurrency and Regulation of Official Digital Currency Bill, 2021’. The Bill proposes to ban all private cryptocurrencies in India. Even before passing of the Bill, it has created an impact with prices declining across key cryptocurrencies.

Union Finance Minister Nirmala Sitharaman on November 30 said that the Bill will be introduced in Parliament only after Cabinet approval.

The Bill proposes the Reserve Bank of India (RBI) create an official digital currency, a Central Bank Digital Currency (CBDC), and it makes certain exceptions to promote the underlying technology used by cryptocurrency.

Let’s discuss the RBI issuing a digital currency.

How will a CBDC be created? Will the RBI use its centralised ledger system or use the decentralised blockchain model to create it? The centralised system gives more control, whereas a decentralised model is supposed to be more efficient. BIS economist Raphael Auer and Rainer Boehme, a Professor at University of Muenster, in their research note discussed different technologies that can be deployed to create a CBDC. The RBI will need to learn from global experiences, and shape its own technology given the context, and history.

Should the CBDC be wholesale, or retail, or both? A wholesale CBDC means a digital currency for financial institutions, whereas a retail CBDC means a digital currency for the general public. In a wholesale CBDC, the idea is that financial institutions use it to transact with each other in central bank money to settle their accounts. In several ways, much of this activity is already digitised with institutions using central bank reserves to settle transactions. So even if the RBI shifts from digital reserves to wholesale CBDC, it might not change much in terms of the overall development.

The real deal is the creation of a retail CBDC, which leads to multiple inter-related questions of distribution, bank stability, and technology mediums. For distribution of physical banknotes, the RBI uses the extensive currency chest, and bank branch network. For distribution of the CBDC, while one can stick to the current system, there is a more efficient way wherein the central bank issues the CBDC directly to the people.

So far we see people opening accounts at respective banks which becomes a medium to access banknotes as well. Technology can enable the RBI to open bank accounts with itself, and distribute the CBDC directly to the people. Due to technology people can open an account with the RBI to invest directly in government securities. Similar accounts can be created to issue the CBDC.

However, this direct distribution model could create instability in the banking system. One of the major liabilities of banks is public deposits, and banks are often seen as its guardians. If the RBI chooses to distribute the CBDC directly to people, there is a strong possibility that people transfer their deposits to the central bank. What could be more secure than keeping one's deposit with a central bank. This transfer of deposits will resemble a bank run, and destabilise the banking system. The banks also lose deposits which are a vital part of their liabilities.

If the central bank takes this route, it will become a narrow bank, which for long has been touted as one of the ways to limit the crisis in banks. A narrow bank is a bank which does not lend, but invests deposits in the safest of securities. The RBI does invest its assets in the safest securities. On the other hand, commercial banks will become like financial institutions which rely more on bonds for liabilities.

How will people hold RBI-issued CBDCs? Currently, people hold money and make payments in multiple ways. They hold RBI-issued physical cash in their wallets. They also hold digital cash issued by their respective banks in mobile wallets operated either by the bank or other payment providers.

In the case of an RBI-issued CBDC, how will all this work? Will the RBI develop its own wallet? If it does, what will happen to existing services providing wallets? Physical cash can be held by anyone, ensures privacy, and anonymity in transactions. With digital money people at least need a phone with Internet connection, and all these transactions leave a digital imprint. There will always be some people who do not either have a phone or Internet. Private options can choose to exclude people but public options need to be all inclusive.

One also needs to consider cases when technology fails, and still people are able to pay. We often see people pay with physical cash when digital payment platforms fail. While private digital payment options can ignore these cases, public digital payment by the RBI needs to consider all the possible cases, and not leave anything to imagination.

Finally, what will be the implications of a CBDC on monetary policy? Fabio Panetta of the European Central Bank in a speech pointed out that with the reduction in the usage of physical cash, central banks lose the lever of monetary policy. Panetta says that central banks such as the ECB should issue a digital currency for this very reason. Sajjid Chinoy of JP Morgan broadens the discussion by writing on the implications of private cryptocurrencies on fiscal and monetary policies. He argues that private cryptocurrencies could undermine the effectiveness of monetary policy which will put additional pressure on fiscal policy to stabilise economies. It will also lead to capital outflows as money moves to those economies which have these cryptocurrencies.

In India, cash usage has not declined, and we are going to ban private cyptocurrencies, so Panetta's and Chinoy's views add to the list of questions posed above. To sum up, designing a new digital currency leads to several challenges which will interest the monetary policy researchers once the Bill is passed.

Cryptocurrency Bill | Are we asking the right questions?

What are the qualities of a good regulatory framework? First, it has to be as unambiguous as possible. In other words, there should be clarity on what activities are permitted, and what are prohibited, as well as the penalties for violations. Second, the regulator — usually a State body — should have the powers to proactively detect violations, and when detected, the ability to effectively bring violators to book.

In the ongoing melee of analyses over the imminent law to regulate cryptocurrencies, too much attention is being given to the first, and hardly any over the second. Assuming the law bars cryptocurrency transactions, and somebody holding a few Bitcoins sells them in a private transaction, the fact is, it is highly unlikely the government will come to know. Even if transactions are permitted within a regulatory framework, is there any way to detect a private transaction between two traders using their personal wallets? Good luck with taxing such a transaction.

Suppose a crime involving cryptocurrencies has been discovered, and the accused nabbed along with the spoils (stolen coins). As we saw recently, the police often does not even have the necessary expertise to ensure that the seized coins be appropriated, and kept in custody.

Or suppose the IT system of an electricity company, or a hospital, is hacked into and taken hostage by cybercriminals demanding ransom in cryptocurrency. The fact that Bitcoins are banned in India will hardly work as an excuse. The victim will be forced to 'make arrangements', likely at an exorbitant cost.

In short, a regulatory framework that merely addresses what activities are permitted does not serve any purpose. Why, even a complete ban (which would meet the test of clarity) would mean nothing, if the State does not have the means, or expertise, to enforce the ban.

It is often said that cryptocurrencies today are what the Internet was back in the '90s — championed by a few geeks, while the rest of us shrug in part-amusement, part-disquiet. It could well be that the technologies which cryptocurrencies are based will define our lives in the decades (or years) to come.

What the government ought to focus is on permitting the development of this technology, while protecting both the economy and the individual citizen from lasting harm. Meanwhile, defenders of cryptocurrencies could probably help by acknowledging its real potential to cause lasting harm, if they are to be taken more credibly.

The harms are primarily of three kinds: One, the anonymity that crypto-transactions operate under mean that they are going to be used for illegal activities – almost all cyber-crime nowadays involve demands for ransom in the form of cryptocurrencies. Banning won't make this problem go away, as India's share in the global trade involving cryptocurrencies is small.

Just as importantly, the anonymity coupled with irreversibility of transactions mean that it is almost impossible to identify whether lost Bitcoins were in fact stolen by an insider, or lost to a hack by an outsider, or even to a forgotten password. After all, even the most secure system is vulnerable to hacks.

An extreme response to this would be to prohibit holding of cryptocurrencies in trust on behalf of others (which would wipe out exchanges), making each person responsible for their coins' safety. A more moderate approach would be to make exchanges absolutely liable for loss of coins — irrespective of whether it was stolen or lost. Needless to say, customers would bear the brunt of losses due to fluctuations in price.

The second harm, already seen in India aplenty, is that the wild price increases would be used to attract 'investors' looking to make a quick buck. However, this harm can be addressed through criminal (and securities) law, since it

almost entirely transpires in the physical world (advertising fraudulent schemes, collecting money, etc.). Unapproved schemes for collecting money from investors are prohibited by law. The government's role would be to create greater awareness.

Finally, and this is not talked about enough, mainstreaming of cryptocurrencies will increase wealth inequality. People who own large tranches of crypto-assets acquired them at throwaway prices long ago, or even received it as a joke. Today, as prices have soared (100x, compared to just seven years ago) many who have hoarded them would be richer than the world's wealthiest people. Remember, this is money that has no underlying value — or sovereign guarantee. It will necessarily inflate prices in the economy, pulling off the ultimate con — self-printed money.

The government could address by prohibiting the use of cryptocurrencies for purchases (such as for pizza or cars) — that is, prohibit their use as currency, and permitting their use only as assets to be held or traded. A blanket ban, on the other hand, would be both futile, and unnecessary.

Cryptocurrencies a bad omen for gold

Historically, copper, gold, and silver coins were legal tender in the Indian subcontinent, and other regions across the world. Traditionally, in India, these metals have enjoyed acceptance as 'sacred metals' due to their religious, medicinal, and economic importance.

With the rise in its industrial use, copper may have lost its 'precious' status, but gold and silver still continue to enjoy the attention. Nowadays, even the acceptance of gold and silver as 'sacred metals' is gradually diminishing.

In past few years, the Government of India has made significant efforts to encourage people to own gold in a non-physical form, through sovereign gold bonds (SGBs). In recent years, digital gold has also gained in popularity due to its ease of transaction, and holding.

Cryptocurrencies (such as Bitcoin) are a relatively new phenomenon in the global financial ecosystem. These are not yet currencies in the traditional sense — except in El Salvador, which has declared Bitcoin as legal tender. Some jurisdiction (such as China, Indonesia, etc.) have banned the use of all cryptocurrencies as a medium of exchange.

To achieve a 'currency' status, cryptocurrencies would need to gain much wider and deeper acceptance; which usually comes with time and awareness. Gold took centuries to gain wide acceptance as a medium of exchange, and become a valuable asset. A few cryptocurrencies may gain this status in future, simply because modern technology has made things much faster.

In India, cryptocurrencies have gained tremendous popularity over the past five years. It is estimated that there are over 100 million people in India owning one or more cryptocurrencies; the largest number for any country in the world. This number is materially higher than the number of people owning publically-listed shares in India. The value of cryptocurrencies owned by Indian citizens is estimated to be close to $900bn.

Regulating Cryptocurrencies

The government has proposed to introduce 'The Cryptocurrency and Regulation of Official Digital Currency Bill 2021' in the winter session of Parliament to regulate cryptocurrencies. It aims to "create a facilitative framework for creation of the official digital currency to be issued by the Reserve Bank of India", and prohibit private cryptocurrencies, with certain exceptions to promote the underlying technology and its uses.

Earlier, a high-level inter-ministerial committee suggested a ban on private cryptocurrencies, except any virtual currencies issued by the State. However, the government refrained from pushing the legislation in the budget

session. It was felt that a balanced approach is required in the matter, for which wider consultation with all stakeholders is important.

It appears that the government is against the use of cryptocurrencies as a medium of exchange (legal tender), but supports the development and use of blockchain technology. It is, therefore, likely that a regulatory framework may be provided for ownership, transfer, sale and taxation of cryptocurrencies. If so, cryptocurrencies may be treated as 'capital assets' under the taxation laws.

It is also likely that the proposed legislation may permit a digital currency based on blockchain technology, to be developed by the RBI or any other public agency. Obviously, such currency will not have the traits of a Bitcoin, which is a decentralised and distributed digital token with a finite supply. The RBI's digital currency will most likely be a centralised currency with infinite supply, just like a fiat currency. In simple terms, the RBI's digital currency may be a dematerialised currency note that is delivered as a book entry in the receivers' account.

Therefore, a fiat digital currency should not be confused with a decentralised and distributed cryptocurrency.

An Idea Whose Time Has Come

In every democracy, especially in socialist ones, governments tend to regulate every innovation, because most new innovations make a few people rich, leaving the rest behind, and this increases the fear of rising inequality. The tendency to overregulate innovations is usually driven by the concerns to assure the majority of population that stays at the bottom of the pyramid.

An example of this was the attempt of British government to ban use of cars on public roads in early years of automobiles. The argument was that this may have negative implications for the employment of poor people running horse carts on London's streets.

The good thing is that there is no historical evidence of a government regulation killing an innovative idea which was ready for adoption by the wider sections of the public. Expansion of organised retail in India is an example.

A Bad Omen For Gold

A well-regulated cryptocurrency market could be a bad omen for 'valuable assets' such as gold and silver. Factors like popularity and spread of technology; the rise of fascist and communist tendencies due to worsening socio-economic disparities; the rise in electronic transactions lowering the risks arising from physical transactions; the emergence of new articles of luxury; stronger and deeper social security programmes; etc. are all leading to the sustainable decline in traditional demand and pre-eminence of gold. This decline is set to continue.

The table below clearly shows that gold and cryptocurrency are comparable assets in most respects. Some argue that gold has an 'intrinsic' value, whereas cryptocurrencies have none. The intrinsic value of gold developed over many centuries of wider acceptance by the State and religion. This intrinsic value has been on the decline for the past few decades.

Insofar as the volatility is concerned, in the past two centuries, gold has seen many bouts of wild volatility, similar to what cryptocurrencies are witnessing these days.

RBI must conduct periodic reviews to better ease of compliance

The World Bank's Doing Business rankings were in the news recently. The World Bank put an embargo on further publishing on the rankings. There have been allegations that the rankings have been compromised under political pressure from select nations. While it is highly welcome to clean up the rankings, the idea of making business easier across the economies has merits. The rankings show how certain regions suffer from high compliance and regulatory burdens. If the leaders understand the lessons correctly, they could boost business, and economic growth by merely easing these said burdens.

In similar spirit, the RBI had constituted the Regulations Review Authority (RRA) in April to reduce the compliance burden on RBI-regulated entities. The RRA was required to review all the existing regulations, circulars, and instructions, and make them "more effective by removing redundancies and duplications, if any".

The RRA was also required to seek feedback from the regulated entities to simplify "procedures and enhancement of ease of compliance". The aim of this exercise was to streamline reporting mechanisms, revoke obsolete instructions, and obviate paper-based submission of returns. The RBI appointed Deputy Governor Rajeshwar Rao as the authority of the RRA, signalling the importance of this clean-up.

This is not the first time the RBI has organised an RRA. In March-1999, the RBI instituted the first RRA (RRA 1.0) whose job was the same to simplify regulatory structure. The authority of RRA was then RBI Deputy Governor YV Reddy. The RRA 1.0 was also established for a year, but its contract was extended for another year given the volume of work. The RRA 1.0 received 235 applications, and more than 400 suggestions, pertaining to various functional areas of the RBI. The review streamlined the RBI's functioning with the public, and rationalised a number of statistical returns and reports. The review also led to merger of several circulars into subject-wise master circulars, a practice RBI continues till date.

The current RRA (RRA 2.0) released interim recommendations, and has broadly followed up with work done by the RRA 1.0. In one sweep, the RRA 2.0 has recommended withdrawal of 150 circulars. The RBI has accepted the recommendations, and issued notifications striking off circulars issued by multiple RBI departments.

The rising cumbersomeness in banking regulations has become a concern in some other economies too. In the 2008 crisis, we saw banks and financial institutions collapse in economies who took pride in their financial systems, such as the United States and the United Kingdom. The crisis saw a spate of regulations in these economies. In the US, we saw the Dodd-Frank Act and the UK saw the Vickers Report where the aim was to strengthen financials of banks, and improve regulation. While economists still debate on the impact of these reforms, it was clear that the reforms will add to the complexity in regulatory compliance.

Andy Haldane, a former chief economist of the Bank of England, in a 2012 speech mentioned that the Dodd-Frank could comprise 30,000 pages of rulemaking, which is thousand times larger than its closest legislative cousin, the Glass-Steagall Act (1933). He also said that a survey of the Federal Register showed that complying with these new rules would require an estimated 2.2 million labour hours every year, which was equivalent to over 1,000 full-time jobs.

In the same speech, he said Europe's own regulation could add up to 60,000 pages. The Bank of England's Victoria Saporta in a recent speech, said that there has been a near-doubling in the length of the UK banking regulation to almost three quarters of a million words since the 2008 crisis. She added that while new rules were needed to strengthen banks, the rules have also added to the complexity. The rising complexity leads to higher costs as financial firms hire staff to interpret rules and new requirements. Within the financial firms, it is the smaller firms which suffer more due to these new costs.

Given this, it was timely for the RBI to establish the RRA 2.0. A review was needed to cleanse the complexity and redundancy in regulations and circulars which would have gone up given the nature of banking development.

Going forward, it is a good idea for the RBI to conduct these reviews periodically, say once in five years. With the rise of digital banking, the complexity will only grow. The RBI has also released its committee report on digital lending which has recommended a separate new legislation to prevent illegal digital lending activities, and for ensuring customer privacy. A future RRA will be needed to understand and streamline different legislation in offline and online financial services. Such cleansing reform exercises do not get the desired attention but are quite effective in not just banking but also in overall economic development.

COVID-19 and After | Large listed companies gain at the expense of smaller, unlisted peers

Slower economic growth in the five years leading to March 2020 and the COVID-19 pandemic that followed have weighed heavily on the corporate tax revenue.

In the financial year 2019-20, corporate tax collection registered the lowest five-year moving compound annual growth rate (CAGR) of 5.4 percent in four decades.

The onset of COVID-19 at the beginning of 2020 and attendant lockdown restrictions added to India's economic and financial woes, leading to a steeper drop in corporate tax collection (-19.9 percent in 2020-21).

The share of corporate tax receipts in the government's overall direct tax revenue fell to sub-50 percent for the first time in 30 years in the fiscal year ended March 2021.

The pandemic had been initially expected to weigh significantly on corporate profitability. But an early and faster-than-expected economic recovery, proactive and aggressive fiscal and monetary support extended by the government, and importantly, expense management meant that listed companies posted unexpectedly good earnings.

Corporate tax payments surged ~17 percent in FY21, based on the Prowess data base of financial statements of 4000+ listed companies maintained by the Centre for Monitoring Indian Economy (CMIE).

Listed Companies Overtake Unlisted Rivals

In absolute terms, the aggregate corporate tax paid by companies in the listed space surpassed that of the unlisted space for the first time in nine years.

The share of corporate tax payments by Nifty 50 and Nifty 500 companies in the government's corporate tax kitty rose to more than 15-year high levels in the fiscal year gone by.

In fact, it was the first time since 2004-05 (first year of our analysis) that Nifty 500 companies contributed more than 50 percent to overall corporate tax collections in 2020-21.

Importantly, the size-based differentiation in corporate tax payments, which has been in existence to some extent, has exacerbated during the pandemic even within the listed space.

This is reflected in a steeper jump in contribution of Nifty 50 companies to the government's overall tax collection in 2020-21 (+7.8 percentage points to a 16-year high of 30.5 percent) as compared to Nifty 500 ex Nifty 50 (+7.4

percentage points to 20.7 percent) and overall listed ex Nifty 500 companies (+1.8 percentage points to a 10-year high of 5.7 percent).

Despite policy support extended by the government, the adverse impact of the pandemic-induced lockdowns, mobility restrictions, and consequent supply chain disruptions was far more severe on the unlisted and unorganised sector.

This is reflected in a 44 percent drop in corporate tax payments by unlisted companies in FY21, and ~30 percent drop on a CAGR basis during FY19-21. The share of unlisted companies in the Centre's overall corporate tax collections fell to 17-year lows of 41.7 percent in FY21 — the first sub-50 percent share in nine years.

Large companies are better equipped to deal with economic downturns, and have more favourable access to funding (equity, and especially debt). Their positions in supply chains, and more favourable contracts also allow better shorter cash conversion cycles.

How Listed Companies Gained An Edge

During the pandemic, these companies benefited at the expense of smaller listed/unlisted companies by capturing market share. They managed to report strong growth in profitability despite a contraction in India's gross domestic product (GDP) by changing their business models to suit the new COVID-19-appropriate environment, and capturing market share from unorganised entities.

Don't get your hopes high, bond market development could be a mirage

Fond hopes of bond market development arise every time issuances go up. But step out of easing and negative real interest rate cycles and look at the trend. This time may be no different.

Corporate bond issues as a proportion of national income have ranged 3-3.5 percent of the GDP from the time since policy attention focused on developing this market to replace the closure of development finance institutions. Corporates shift from banks to bond financing whenever interest rates are ultra-low or negative as now. A rational response but never lasting enough to become a trend.

Classic features of underdevelopment persist — 99 percent of bond issues are privately placed, the private, non-financial firms are a few and top-rated (almost half of outstanding amounts are AAA-rated), public sector presence dominates while the finance and infrastructure companies have almost two-third share.

With such elements intact for over two decades, it won't be any surprise if this time turns out no different from past episodes of negative real rates. As the chart below shows, corporates get interested in bonds during such periods, but retreat when the cycle turns. This was the case with non-financial bond issues, and its more insightful, private sector subset, in the noughties.

Perhaps rapid growth then provided extra fuel, and helped by the infrastructure investment push to replace demand loss after the 2008 crisis, total non-financial bond volumes touched 2 percent of the GDP in 2009-10. These were quick to scale back as monetary policy tightened thereafter.

A similar cycle is playing out now, creating illusions of bond market progress. In the pandemic year 2020-21, these touched 1.5 percent of the GDP from 0.9 percent in 2017-18 as real rates became negative in the pandemic monetary easing. Before that, the private, non-financial segment was in retreat although the total, which includes the public sector, reached 1.3 percent of the GDP in 2016-17, and remained comparably strong to 2018-19. The

latter deviation is explained by finance and infrastructure companies that raised 90-92 percent of the funds, no doubt to strengthen balance sheets, and finance public investments as was the case in the late nineties and early 2000s; these entities enjoy implicit sovereign guarantee and best pricing as a result of which market-sourced debt is better.

Private firms find overseas debt comparably cheaper unless of course, domestic interest rates are so low so as to eliminate the cost gap. Coupled with the fact that almost half of the privately placed bonds are secured, it is no surprise they turn here sparely, never enduringly, the long intervals in bond issues depriving the market of depth and liquidity, or in other words, development!

There's mutual reinforcement from banks too, the more so when they are risk-averse as in the last few years — loans are preferable to bonds that have to be marked to market, and, therefore, vulnerable to changes in interest rates.

Both past trends and persistence of backward features indicate the current cycle is no different. Instead of misplaced beliefs, it would be more useful to focus on why the bond market refuses to breakout despite numerous efforts and initiatives of two decades.

Why are the gaps in spreads of top-rated companies and moderate- to low-rated ones so wide? Does private placement encourage transparency and trust in retail investors whose presence is minimal? If information dissemination by credit rating agencies (CRAs) hasn't helped, will the Insolvency and Bankruptcy Code (IBC), 2016, help?

Wishing bond market development on spurious signs will not deliver one, but improving corporate governance to inspire the trust essential for financial contracts may do so. Until then, it would be wiser to look at trends than cycles.

Will RBI be like Abhimanyu or Arjuna to break the easy monetary policy chakravyuh?

The 2008 crisis led central banks on a path not seen before in the history of monetary policy. This was particularly true for advanced countries where policy rates not just touched near zero levels but balance sheets also rose manifold. As central banks were trying to undo these policies, the pandemic struck.

As the pandemic is starting to ease, and inflation appears to be more than transitory, the pressure is back on central banks to think about rolling back their ultra-easy monetary policies. One big central bank expected to reverse its policy stance was the Bank of England. In the Monetary Policy Committee meeting held recently (November 4), the markets expected the central bank to increase policy rates. The UK economy was recovering post pandemic and inflation was higher than target of 2 percent. However, the second oldest central bank not just voted to keep policy rates unchanged at 0.1 percent but also continued to expand balance sheet by buying assets. The yields of the UK 10-year sovereign bond had risen from a low of 0.5 percent in August 2021 to around 1.05 percent before the November policy. Post-policy, the yields dropped to 0.82 percent.

We have seen other major central banks such as the US Federal Reserve and the European Central Bank also showing reluctance to reverse their policy stance despite rising inflation. The officials of these central banks have treated rising inflation as transitory. Having said that, we have seen some central banks reverse policy stance. The Central Bank of Norway has raised policy rates whereas New Zealand has halted expansion of its balance sheet.

The RBI followed the book of global central banks during the pandemic. It lowered the policy repo rate from a pre-pandemic level of 5.15 percent to 4 percent during the pandemic. The central bank also ushered in multiple policies to ease liquidity conditions and as a result its balance sheet also expanded significantly. We can see that in terms of scale, RBI's balance sheet has expanded more than that of the ECB and is just lower than that of Federal Reserve.

Like advanced economies, inflation in India has been higher than the target 4 percent, but within the upper tolerance limit of 6 percent. In the October policy statement, the RBI has projected annual CPI inflation at 5.3 percent for 2021-22 and quarterly inflation at 5.1 percent for Q2, 4.5 percent for Q3; 5.8 percent for Q4 of 2021-22.

On the growth front, the RBI has kept GDP growth at 9.5 percent in 2021-22 consisting of 7.9 percent in Q2, 6.8 percent in Q3 and 6.1 percent in Q4 of 2021-22. There are indications that final growth numbers could be higher as indicated by rising GST tax collections, record festive shopping and so on. We have to see whether higher growth numbers will also lead to higher inflation.

Like advanced country central banks, the RBI has been ignoring calls to unwind the easy policy stance as there is uncertainty regarding the growth outlook. There is also concern that a tighter policy sooner than required will reverse the gains in economic growth. In the 6-member Monetary Policy Committee, we have seen 5 members agreeing to a continued accommodative stance with Professor JR Varma being the lone dissenter. Varma has mentioned that the pandemic has been more of a human tragedy rather an economic crisis. He opined that fiscal policy is more effective compared to monetary policy in providing relief to the impacted population. Moreover, there are signs of persistent inflation pressures than was the case earlier, which means RBI needs to act quickly by removing the accommodative stance. However, he is of the view that RBI should first raise the reverse repo rate and look to raise the repo rate over time.

Even if the RBI has chosen to keep the easy policy, the yields in bond markets have other ideas. The benchmark 10-year bond yield has increased from 6.25 percent in October 21 to near 6.4 percent recently. In the early part of the financial year, there was a tug of war between the RBI and financial markets. The latter, anticipating higher inflation and growth, bid upwards of 6 percent for 10-year bond auctions. The RBI had rejected these bids and tried to keep 10-year yields pegged to 6 percent. Eventually, the central bank started accepting the yields higher than 6 percent.

Given this background, the path to normalising monetary policy is as tricky for the RBI as for other global central banks. RBI Governor Shaktikanta Das in a recent interaction with Business Standard mentioned that normalizing monetary policy is not like rolling back a carpet. He mentioned that most of the liquidity schemes announced during the pandemic have a sunset clause and normalcy will be restored as they eventually end. He added that the RBI has been surprised by rising capital flows which has led to rise in liquidity.

Das's three-year term was recently extended for another three years. The highlight of his first term was RBI fighting the pandemic-induced economic crisis. His second term will be marked by how RBI tackles the unwinding of its easy monetary policy. The experience with global central banks suggest this situation is a lot like Mahabharat's chakravyuh where it is easier to get in but very difficult to get out. Will RBI be like Abhimanyu who was unable to break the chakravyuh or like Arjuna who had the knowledge to break the battle formation?

Shareholder activism is here to stay, and companies need to be responsive and responsible

My first brush with an activist shareholder was in 2017 when a globally well-known activist investor fund came calling. I walked into the meeting quite unprepared for a gloves-off, no-holds-barred meeting.

The fund had sent a relatively junior employee from its London office, but he seemed well-trained to use the appropriate language, adroitly skirting the thin line between threat and strong advice. He took notes whenever I spoke, making me very careful about the words I chose.

Once I came out of the meeting, and reflected on the experience, one aspect struck me quite hard. The fund had done its homework very thoroughly. It had done some sophisticated analysis, and quite correctly done a good peer benchmarking on key parameters.

Doubtlessly, corporate India is now dealing with some very motivated, goal-oriented, and incisive investors who are not squeamish about asking hard questions, and challenging the owner-managers.

In 2018, we all saw a significant activist shareholder-orchestrated event. Two large institutional shareholders called an extraordinary general meeting, and removed the chairman and board of directors of Fortis Healthcare. The motion got almost complete support from minority shareholders, which was quite well-justified when the new board cleared the way for a sale at a good value to a strategic buyer, thereby saving the company from a possible collapse.

More recently at Eicher, Hero MotoCorp, Balaji Telefilms, Lupin, Vedanta, V-Mart, Burger King, and Zee, the top management has been at the receiving end of activist shareholders. Even relatively well-run companies can face the ire of well-informed investors when there is misalignment on issues of remuneration of top management, employee stock options, and special rights.

Annual general meeting resolutions are no longer assumed to be boxes to tick. Even non-institutional shareholders are much better informed with access to proxy advisory firms.

Lethargy

A well-known retail pioneer once told me that he was great when it came to taking a business from zero to one, but needed someone to take it from one to 100. I was amazed that a person with his stature had such an honest, and humble opinion about his own strengths, and shortcomings.

But how many top managers realise their shortcomings? Top posts at large companies and institutions are held for years on end by the same owners and professionals.

While this imparts a sense of continuity and stability, it also makes these individuals larger than life, and above reproach internally. I struggle to give examples of board members who have stood up to such towering personalities.

Greater Good

In this environment, is it any surprise that activist shareholders see an opportunity to pull the rug from under the feet of otherwise well dug-in owner-managers? Companies with inefficient operations, and a lethargic management that cannot solve simple issues are the prime targets of activist investors.

It is simplistic to view activist shareholders as acting in their own selfish, short-term self-interest. Often, in the process of taking a hard stance against bad managements, they help all shareholders to benefit in the longer run.

Activist shareholders can, when things go right, deliver tangible benefits for all shareholders such as market value re-rating, more efficient capital allocation, credit upgrades, and better strategic alignment of management with shareholders.

Not all activism is aggressive and public. Most often, investors communicate and present ideas and proposals in private. However, if they are stonewalled, as they often are, the more aggressive ones can and do launch shrill media and public campaigns.

Better Communication

Companies, especially those that are dependent on public trust, need to be highly sensitive to market communication, which needs to be two-way traffic. So often we see companies undertake a major transformational event such as entering a new product category, a large M&A, or a new market entry without carefully explaining long-term shareholder value, and communicating accordingly.

Good governance, credible management, and proactive and clear investor communication will no longer be desirables, but an absolute standard way of operating businesses. A responsive management will build credibility, and trust.

Investor relations has usually been seen as a department meant to draft communications after an event. However, now is the time to enhance the profile of the investor relations department, and hire the right professionals who can proactively manage investor activism through timely, and effective communication.

Companies cannot wish away activist shareholder focus, and can no longer work behind walls. If you have public funds, you have to be responsive and responsible, or else you pay the price.

Data Privacy | Strengthening consent will make India a global leader in individual-centric data economy

In the first week of September, India told a bold leap towards empowering Indians with their data by launching the Account Aggregator (AA) system to help consolidate their financial data in one place. Every Indian can then choose to share this data with other businesses, such as insurers and lenders, thus enabling faster onboarding and more customised products. Eight of India's largest banks have signed on, which makes the system accessible to most Indians.

The importance of this moment cannot be overstated. While Europe and the United States are struggling to push through laws with the idea of users owning their data, India has gone a step further and made it possible through technology. In future, this system could be extended to areas such as healthcare and telecom, thus unifying large parts of an Indian's digital footprint in one place — right under their control. The AA system is, therefore, an inflection point in the remarkable journey that the digital Indian has taken in the past few years.

User consent lies at the centre of the system's effort to empower Indians. Data can be transferred from one business to another only if the user consents to it. When a business initiates a transfer request, the individual receives details about what data is being sought, by whom, from whom, for what duration, at what frequency, and for what purpose. They can then sign the consent electronically — a record is generated in the system and can be revoked later. This also makes the entire system transparent, and auditable.

Since user consent is the fulcrum around which the AA system revolves, it is important to get it right. However, consent is a complex issue, both conceptually and practically.

When the bargaining power between a business and individual is lopsided — for example, if there is only one major bank in an area, or if the user only has a few minutes to decide whether to approve a data transfer request — it calls into question whether the consent given is truly meaningful. Moreover, individuals may not be able to parse through technical, and legal information to truly understand what they are consenting to.

Therefore, we need to test innovative ways to allow individuals to better understand how their data is being handled. Online lab tests conducted by the Centre for Social and Behaviour Change (CSBC) at Ashoka University and the Busara Center for Behavioural Economics with 5,547 Indians provide some insights that can be explored further.

The research found that forcing individuals to stay on the privacy policy for a few minutes had the strongest impact on their understanding of what they are consenting to. Once this happened, people also trusted the business more, and were willing to share more information. Therefore, even though this mandatory 'cool-down period' may introduce friction in the AA processes, that may be compensated by greater trust, and participation in the system.

The research also found that a 'privacy rating' allowed people to differentiate between businesses, and share more data with those that had a higher rating. In practice, such a rating could be based on factors such as compliance with data privacy laws, incidents of data breaches, and robustness of cybersecurity practices. Sahamati, the self-organised collective of Account Aggregators, could be the custodian of this rating system.

These top-down interventions are necessary, but not sufficient. To create a system where individuals are equal participants, we need individuals to actively manage their data, which requires behavioural change. The aforementioned research has a remedy for this too — it found that Indians spend more time reading a privacy policy when presented with a message such as 'over 70% of users spend 5 minutes to read our privacy policy' or '80% of Internet users do not read privacy policies, exposing themselves to avoidable risk'. The Account Aggregator system could mandate that any consent be preceded by such a message, so that users spend time to understand what exactly they are consenting to.

These examples show that it is possible to equip and incentivise individuals to exercise greater control over their data. Through the Account Aggregator system, India has already laid the technological foundation for a frictionless, and empowering data economy. With additional focus on meaningful consent, we can push the boundary on inclusivity, and privacy, thereby cementing India's position as a global leader in an individual-centric data economy.

Is the power sector in India ready for derivatives?

The Supreme Court in October finally permitted power exchanges regulated by the Central Electricity Regulatory Commission (CERC) to offer monthly, seasonal or even annual contracts. As per the press release on the judgment, the apex court resolved a decade-long jurisdictional battle between the CERC and the Securities and Exchange Board of India (Sebi) on regulating forward contracts in power exchanges.

Forward contracts are those where delivery is made after 11 days. Currently, exchanges only offer contracts that are settled within 11 days.

With the judgment, the CERC will have exclusive jurisdiction to regulate all physical delivery contracts. However, financial derivatives, yet to be introduced in the power sector, will be regulated by Sebi.

For power distribution companies (discoms), flexibility and choice are crucial, given the growing demand uncertainty driven by the rising share of variable renewable energy. The uncertainty is amplified with industrial consumers investing in electricity supply from sources other than the discom.

Thus, seasonal surpluses, and shortages are becoming a challenge. To reduce costs, and increase operational efficiency, long-term supply arrangements need to be complemented with other contracts. Monthly and seasonal contracts would help address this challenge, and aid planning for eventualities such as the recurring crises due to dwindling coal supply.

Discoms, and industrial consumers rely on traders, and bilateral contracts to meet their seasonal power requirements. With forwards, industrial consumers will have more choice. Currently, seasonal procurement is through non-transparent, fragmented processes. Discoms will benefit, too, as most short-term contracts take place through the government-administered DEEP portal with limited participation, and options.

Power is unscheduled mostly due to low demand, and discom consent for sale, though required, is seldom provided. Recently, the ministry of power issued guidelines allowing the sale of unscheduled power on the exchanges without additional permission from contracting discoms. With these guidelines, the use of multiple exchange contracts will reduce idle capacity, improve price discovery, and reduce costs.

Forwards provide a new avenue for competition among the three power exchanges, presently facing low liquidity in the term-ahead segment, limited to less than 1 percent of the electricity supplied in India.

Price Signals

The exchanges account for 4-5 percent of the country's electricity supply but are witnessing high volume growth, and addition of new contracts. With these changes, the introduction of financial derivatives, which are transferable contracts that do not translate to physical power delivery, must be approached with caution.

The power ministry, the finance ministry CERC, Sebi, the Central Electricity Authority, the Power System Operation Corporation Ltd, and the exchanges have deliberated on the launch of financial derivatives since 2018. However, many aspects are yet unclear.

With separate regulators for forwards and futures, the need for concurrent, connected market monitoring, though paramount, has not yet been detailed. Further, it is unclear if Sebi's jurisdiction will extend to non-power exchange contracts. Would Sebi regulate derivatives such as contracts for differences to operationalise virtual power plant arrangements? If so, state electricity regulators would also be involved, adding another layer of jurisdictional complexity.

When seen with other considerations, financial derivatives in the power sector can provide helpful signals to investors. However, given their speculative nature, these prices make poor benchmarks in decision-making processes.

The outcomes in the derivatives market should not be used to set ceiling tariffs for competitive bidding or to determine limits for short-term power. It would be tragic if high prices in this speculative market are used as a signal to justify increased investments in capacity addition by bankers, developers or regulators.

Thank

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