श्री LAKSHMISHREE

Gateway to your Financial Goals

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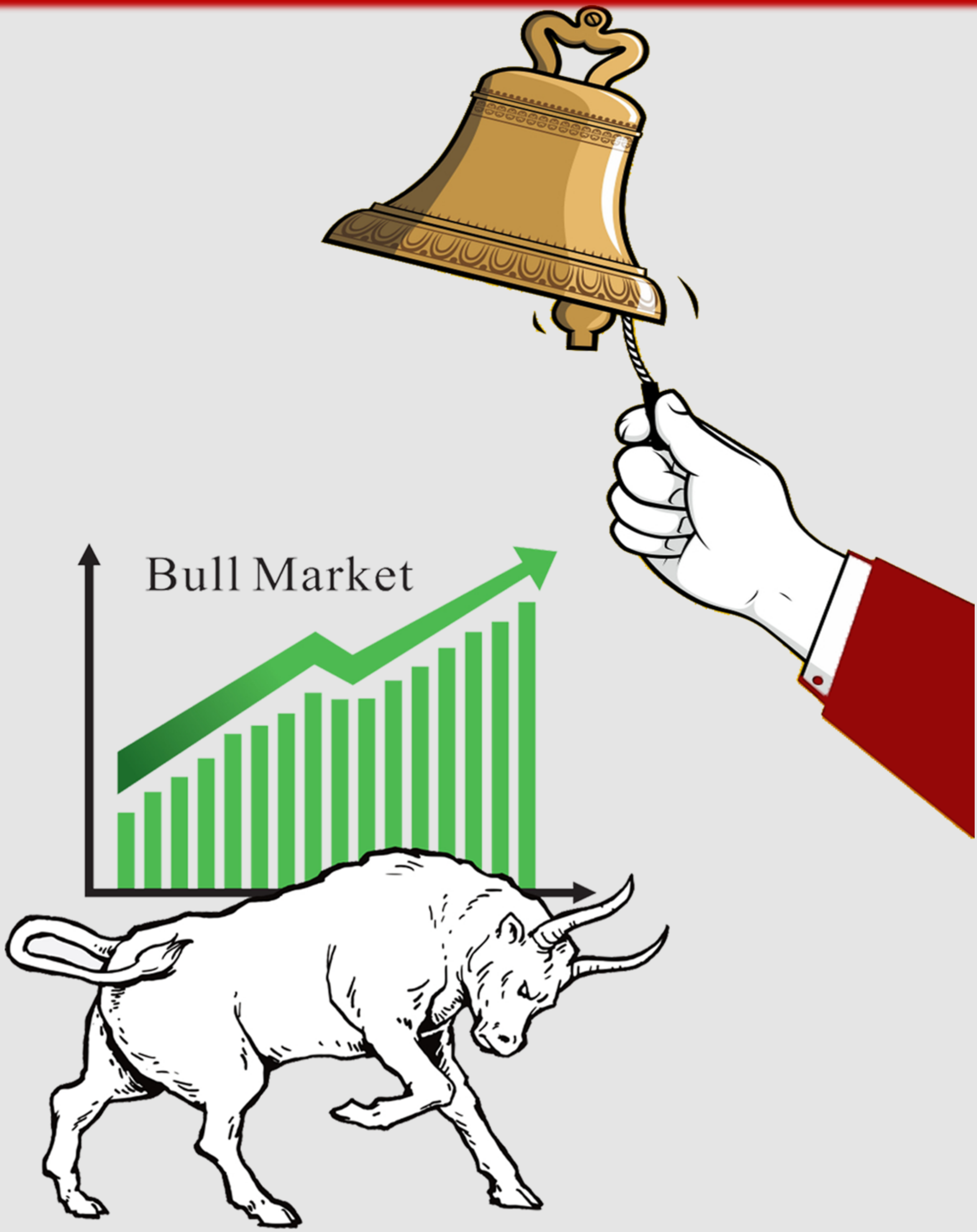

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Indian Money Markets Comes Of Age

If you ask an average Indian investor about the state of the markets, their answer will invariably be a health check of the equity markets. Unfortunately, domestic participants think equity markets are the only game in town but globally equity markets are the smallest in terms of turnover. The biggest market is the foreign exchange (forex) market with a turnover of $6.80 trillion in 2022 and is expected to clock US$ 7.50 trillion in 2023, reaching 10.8 percent CAGR.

These numbers do not include the OTC (over the counter) market where banks transact amongst themselves. The competition for the second and third place is between commodities and bond markets. Turnover depends on time of the year (cyclicality), geo-political developments and economic data.

In reality, it is the bond market that finances growth in markets for other asset classes. To that extent it is the fountainhead of money supply for other markets. A vibrant and growing bond market accelerates economic growth at a faster clip in any developing nation. This market facilitates raising of long term funds at pre-determined coupon rates and repayment schedules.

The first signs of the dawn of a new era emerged as the government of India launched the RBI retail direct G-sec portal on 1 October 2021. Investors can open an account online and buy and sell government bonds directly to/from banks without any brokerage or execution costs. Moreover, these sovereign guaranteed bonds are 100% guaranteed by the government, unlike bank fixed deposits which are insured up to Rs 5 lakh per individual. The scheme was an instant hit with resident and non-resident Indian investors.

The next step was to free the state governments and city level municipalities from restrictions on raising money from the bond markets. Last year the Indore Municipal Corporation raised money via bonds at a coupon rate of 9.25%. This was a mouth-watering return for any fixed income investor. State governments can now tap the bond markets for building highways, developing cities, airports, railroads and other infrastructure and welfare projects. State government bonds are also classified as "sovereign guaranteed" bonds and enjoy high credit ratings.

The Ace of Spades

The final breakthrough came recently as Indian government bonds are going to be listed in overseas bond indices. That would open the floodgates of FII inflows in the debt market. For those new to the subject, the following flow of events is likely over the coming years:

- Fresh dollar inflows: Just like index funds buy stocks that constitute the indices in the same proportion as their weightage in the indices, overseas investors will have to buy Indian government bonds in their bond portfolios in the same proportion as their weightage. This can result in substantial fresh dollar investments. Remember what I wrote about the size of the bond markets worldwide. It is second or third in turnover and size. Just 1-2% weightage in the global bond indices can trigger between US$ 20 – 40 billion fresh inflows into India. Compared to the miniscule annual inflows into stocks, this is a major breakthrough.
- Quality of inflows: Equity inflows tend to be “hot money.” Investors buy shares as long as the markets are bullish. They sell equally quickly when markets fall. This results in large swings in inflows and outflows. The INR experiences volatility and Indian export-import trade gets impacted due to the currency peg. Since bond investors are long term players, they invest in multiples of five years or longer. The INR will, therefore, see improved stability and help importers and exporters to plan their trades.
- Trickle-down effect: Salesmen know that buyers who enter a department store to buy a specific item can be encouraged to buy a few more hot selling items as well. Similarly, bond investors can also invest in Indian equity markets, leading to accelerated inflows.
- Improved FDI: History has shown that overseas investors in financial markets can also invest in infrastructure and business projects. Take the case of Qatar's investment in Indian expressways, equity and debt markets. Qatar is not alone. The Saudis are investing in Indian refineries projects. The list can and will get longer. This helps generate employment, GDP growth and per capita income.

Higher returns for investors: Since Indian bond yields are significantly higher than that of their western counterparts, FII investors stand to get higher return on investments. Since long term bond investors will hedge their currency exposure in the Indian forex markets, that asset class will get improved depth too. This is a win-win situation for all.

Investors should start looking at the bigger picture and look beyond the near term volatility in financial markets. We are at the dawn of a new era in which our money markets will start vying with developed nations. India is moving towards reclassification into a developed market from a developing market.

Lessons For India From China's EV Strategy

On September 13, the European Commission (EC) started investigating whether Chinese electric vehicles (EVs) imported into the European Union (EU) benefit from state subsidies. EC President Ursula von der Leyen argued, "Global markets are now flooded with cheaper electric cars. And their price is kept artificially low by huge state subsidies," and went on to specifically target China. The EC now has 13 months to initiate anti-subsidy measures, with provisional measures imposed no later than nine months from the start of the investigation if legally warranted.

Nearly half the cars imported into the EU are from China. In 2022, the country accounts for around 60 percent of global electric car sales, according to the International Energy Agency (IEA). Europe was the second largest market where electric car sales increased by over 15 percent in 2022, as per IEA.

China, predictably, argued. The country's Commerce Ministry said, “China believes the investigations announced by the European Union in the name of ‘fair competition' are actually aimed at protecting its own industries… It's a blatantly protectionist act that will seriously disrupt and distort the global — inclusive of the EU —automotive industry and supply chain and will have a negative impact on China-EU economic and trade relations.”

But the cries of subsidies, protectionism, and the complex geopolitics notwithstanding, China's carefully crafted strategy to gain ascendancy needs attention. The strategy bears lessons for Indian policy makers, if the country is to secure itself in EVs both domestically and globally.

Crafting An Advantage

China's EV policy involved central and provincial governments, crafting incentives for both manufacturers and consumers. It recognised that EV adoption could be a challenge for consumers with uncertainties over range, charging infrastructure, resale and the balance between upfront costs and future savings.

China then, over the years, incentivised both scale and consumer preferences in a way that no other market across the world had done. Policies were specifically designed to give the sector a competitive edge globally, a strategy that can be traced back to at least 2009.

UBS analysts, Paul Gong, pointed out in a note, "The Chinese BYD Seal car has 15 percent lower cost than [Tesla's] Model 3 made in Shanghai, and more than 35 percent lower than VW ID.3 made in Germany." The low costs stemmed not just from subsidies, but the business model applied by the state towards the EV industry. "Chinese manufacturing efficiencies as well as substantial supplies of core components contribute to it a cost advantage, but also technology know-how," Gong's note said.

The Chinese government identified EVs as a priority sector in 2001 and EV technology was earmarked as a priority science research project in China's Five-Year Plan. Between 2009 and 2022, Beijing had handed out nearly $29 billion into subsidies and tax breaks. The subsidy policy also involved a system called 'dual credits', which commenced in 2017, somewhat akin to a carbon trading system where automobile manufacturers could make several thousand dollars on each EV sold by selling credits.

In the early years the government incentivised EV companies by providing procurement contracts for public transportation. BYD, the world's second largest manufacturer after Tesla, had close ties with the provincial government in Shenzen which became the world's first city with a completely electrified bus fleet in 2017.

China's provinces and cities regularly announced targets for EV manufacturing and incentivised both the demand and supply side of the market with various subsidy incentives. Recently, for instance, a municipality in China, Chongqing, has announced targets to produce and sell 10 percent of the country's EVs in three years, while the province of Jilin targets an annual production of one million EVs by 2025.

The Heart Of The Strategy

The core of the Chinese strategy is to build cost-efficient scale with policies targeting the complete value chain— from inbound raw materials across operations down to market and sales. Battery costs, for instance, are a third of the cost of EVs. China controls the necessary battery materials with world dominating refinery capacity across components like cobalt, nickel sulfate, lithium hydroxide, and graphite. BYD makes its own batteries; it's integrated with contracts into materials refiners and miners worldwide. BYD today has a 16.2 percent market share in batteries, second only to another Chinese company, CATL.

Financial incentives were designed in a way that balanced out the cost differential between an EV and an internal combustion engine vehicle (ICEV). Policies are meant to directly and indirectly facilitate both a manufacturing and consumer shift towards EVs. Demand is boosted by influencing purchase preferences for EVs over ICEVs with taxes heavily weighted towards the former. ICEV customers face higher taxes on the vehicle, including pollution taxes.

Supply side policies are designed to lower the cost of finance through cheaper loans. The incentives also target barriers to research, technology introduction and focus on specific stages of the manufacturing output offering a combination of subsidies with tax reliefs.

BYD's strength in managing battery production costs drives its product choice strategy, which in turn is closely intertwined with its operations cost for EV manufacturing. Government subsidies on the supply side then play a role in BYD's economics enabling crucial economies of scale. Others, like SAIC not quite as vertically integrated as BYD, have still been heavily incentivised over the years through tax breaks, cheap land, and finance subsidies to manage manufacturing costs profitably.

The policies are not designed for Chinese manufacturers alone. Tesla has benefitted over the years. BMW and Volkswagen are benefitting from the low cost of finance and easy and cheap land procurement policies. This incentivises US and European brands to export back to their home markets creating a piquant situation for any potential EU action on import taxes. Cars made by European brands would then have to be taxed at the same level as Chinese brands.

As Cui Dongshu, secretary general of the China Passenger Car Association pointed out on his WeChat account, China's EV exports have stronger volumes because the country's industrial supply chain has become highly competitive and market competition in the domestic market is strong. Dongshu claims that Chinese EVs exported to Europe retail at nearly twice the price of their cost in the home market, indicating the success of both China's policy strategy over the years and its global scale efficiencies.

Lessons For India

There's a message herein for India. While policies like the PLI schemes are incentivising both EV manufacturing and production, the incentives are still not quite enough to enable manufacturers to build scale and drive down upfront consumer costs to levels that balance out EV demand against ICEV demand. The incentives available under the PLI schemes are interesting enough to build early manufacture, but not quite enough to build scale and sustain pricing from an early-stage market to market saturation.

For instance, the PLI for the advanced chemistry cell (ACC) battery is $2.2 billion, incentivising 50 GWh of production for five years with a domestic value-add of 60 percent targeted in year five. Yet, if IEA data is any indication the 50 GWh production target is 50 percent higher than anticipated domestic demand, meaning demand side incentives now need to be pushed considerably harder changing consumer preferences quickly.

In 2022, 25 percent of EV purchases were by fleet operators. Though 55 percent of the three -wheelers sold were EVs, a mere two percent of the four-wheelers sold were electric. If FAME II is withdrawn in 2024, it will have to be replaced by policies akin to those of China, building demand for EVs over ICEVs, while allaying consumer anxieties and drastically changing preferences through major tax breaks and incentives.

China's strategy was carefully thought through and built over the decades. The EU is attempting to craft strategies now, simultaneously playing the protectionism card. India has played the protectionism card by blocking BYD's $1 billion investment last month. It's now up to New Delhi to craft a strategy that's quite as efficient as China's to build India a national competitive advantage in EVs.

Look What Our Research Analyst Has To Say...

Nifty for the entire week traded sideways in a wide range as the Monthly derivatives expiry had huge Open Interest Pending to settle or rollover. The index did give widest range bar in near past but Fridays inside bar absorbed the selling well. On the weekly frame the index has formed a DOJI candle which is sign of indecision after the wide selloff in the previous week The indecision can turn out to be in favor of bulls as the index has closed right above the Quarter VWAP and will act as a major support. Since it will be a truncated week Global cues will weigh heavy on Tuesdays opening which also happens to be the weekly expiry of Finnifty. Ont he downside strong support is placed at 19580-19550 zone and on the upside 19800 will act as a major resistance which also happens to be the anchor vwap of selling from ALL TIME HIGH.

Anshul Jain

Sr. Research Analyst

Stock To Watch

DEN NETWORKS LTD.

Market Cap.	EPS	Net Profit	ROE	Promoter Holding
₹ 2,415 Cr	₹ 5.71	₹ 266 Cr	6.01%	74.9%

Den Networks Ltd is a leading Indian mass media and entertainment company, offering cable TV, OTT entertainment, and broadband services to over 13 million households across 13 states and 433 cities, establishing itself as the largest cable player in India. Notably, it operates as a subsidiary of Reliance Industries, with Reliance holding approximately 75% of the company as of FY23. Their revenue in FY23 is diversified, with 53% stemming from subscriptions, 36% from placement, 5% from activation, and 6% from internet services and other sources.

In addition to their cable TV and broadband services, Den Networks boasts an OTT platform called Den TV Plus, providing access to 130 TV channels, thousands of movies, and a wide range of content. The company prides itself on maintaining a debt-free status in FY23 and introduced new software, LCO Light House, to enhance customer engagement. Notably, in FY22, they decided not to proceed with a proposed amalgamation scheme with other companies.

Parag Milk Foods Ltd.

Market Cap.	EPS	Net Profit	ROE	Promoter Holding
₹ 2,542 Cr	₹ 5.58	₹ 64.4 Cr	7.88%	41.6%

Parag Milk Foods Ltd, founded in 1992 by Mr. Devendra Shah, is a leading player in the Indian dairy industry. They specialize in fresh cow's milk and dairy products, with a diverse portfolio in over 10 categories. Notable achievements include being the 2nd largest cheese player in India with a 35% market share, leading the Cow Ghee category with 'Gowardhan' Ghee, and launching India's first 'Made-in-India' B2C Whey protein powder under 'Avvatar' in 2017. Their product brands include 'Gowardhan' for daily dairy, 'GO' for UHT milk and cheese, 'Pride of Cows' for premium farm-to-home milk, and 'Avvatar' for sports nutrition. Revenue is predominantly from consumer products, with a focus on value-added items. They have advanced manufacturing facilities and acquired a key facility from Danone.

Parag Milk Foods has a robust distribution network, procuring milk from farmers, and serving institutional clients. Future plans involve expanding processing units and emphasizing health and nutrition, targeting 7% of their portfolio, and exploring opportunities in lactose products.

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