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From Managing Director's Desk To Readers

Budget 2023: Capex bazooka to keep GDP growth all fired up

Amid a slowing global economy and an uneven domestic recovery, the Union Budget for FY2024 has prudently raised the high-multiplier capital spending significantly, while simultaneously pursuing fiscal consolidation, aided by the cushion provided by a sharp decline in the subsidy burden. The Government of India (GoI) has clearly enunciated in its medium-term fiscal policy that "the budget aims at sustaining growth through a renewed emphasis on capital expenditure, strengthening of the social safety net for the poor and vulnerable through prudent and responsible fiscal management".

The GoI's capex has been budgeted to rise by an unprecedented 37.4 % to Rs 10 lakh crore in FY2024 from Rs 7.3 lakh crore in FY2023. The Rs 2.7 lakh crore increase in the capex amount stems from a sharp rise of Rs 0.8 lakh crore in the capex on railways (albeit partly offset by a Rs 0.4 lakh crore decline in the internal extra budgetary resources or IEBR), Rs 0.5 lakh crore on roads, and Rs 0.6 lakh crore on account of the increased allocation for the 50-year interest free loans to state governments for capital expenditure.

The sharp increase in the allocation for roads and railways is likely to augment activity in projects that are under implementation in these segments. The push to commission such projects, which are nearing their final stages of completion, ahead of the general elections, is likely to support India's GDP growth amid global headwinds. Moreover, it should have positive spinoffs for the associated sectors such as steel, cement, commercial vehicle, and construction equipment.

Further, the budgeted amount for the capex loan scheme for the states has been pegged at a massive Rs 1.3 lakh crore in FY2024, about 73 % higher than the revised amount of Rs 0.8 lakh crore for FY2023. Front-loaded capex by the states in FY2024 should help to enhance GDP growth over the next few quarters.

In addition to the sharp increase in the budgeted capex, the CPSE's IEBR are projected to rise by a healthy 21.6 % to Rs 4.9 lakh crore in FY2024 over the revised number for FY2023. Adding this to the GoI's own capex, the total capex of the Centre and the CPSEs (IEBR) is expected to rise quite sharply by 31.8 % to Rs 14.9 lakh crore in FY2024. This amounts to 4.9 % of the GDP as against 4.1 % in FY2023, and would play an important role in supporting investment demand and 'crowd in' private investments.

Notably, the GoI has not budgeted any capital allocation for public sector banks in FY2024; this is in line with our expectations, given their improved profitability and asset quality position.

Apart from capex, the GoI has increased the allocation for PLI schemes in FY2024 vis-à-vis FY2023, with continued allocation for pharmaceuticals, large scale electronics manufacturing, food products, auto and auto components, and drones and drone components segments. Moreover, the announcements pertaining to the agri sector are quite positive.

The budget also stressed 'green growth' with an allocation of Rs 35,000 crore for priority capital investments towards energy transition and net zero objectives, and energy security. Besides, it announced a green credit programme to encourage environmentally sustainable actions by individuals and corporates and allocated funds for scrapping old vehicles of the central government.

The budget will also leave higher disposable income at the hands of the salaried class if the new rates are adopted by them, which will give a fillip to consumption-oriented sectors such as automobiles, housing, electronics, and hospitality.

The GoI's subsidy bill is expected to fall to Rs 3.7 lakh crore in FY2024 from Rs 5.2 lakh crore in FY2023, led by a sharp decline in food and fertiliser subsidies. This has helped contain revex (revenue expenditure) growth at just 1.2 % in FY2024, while providing headroom to expand capex sharply. Nonetheless any sharp rise in crude, natural gas, and fertiliser prices, could upset the subsidy arithmetic.

Gross tax revenues are budgeted to rise by 10.4 % in FY2024, in line with the nominal GDP growth of 10.5 % projected by the GoI. However, we believe that the assumptions for non-tax revenues and disinvestment receipts are somewhat optimistic.

Accordingly, the GoI's fiscal deficit is budgeted to rise slightly to Rs 17.9 lakh crore in FY2024 from Rs 17.6 lakh crore in FY2023. However, as a percentage of GDP, it is expected to moderate to 5.9 % from 6.4 % in FY2023, implying that the budget has managed to curtail the deficit while enhancing productive spending.

Salil Shah

Managing Director

Lakshmishree Investments & Securities Pvt. Ltd.

Look What Our Research Analyst Has To Say..

Nifty Finally has made a lower high rejecting the quarterly CPR and also has made a lower low denting into the uptrend. The current fall has been very orderly coiled into a falling channel. Channel drawn connecting high and lower high has bottom placed around 16850 and that will be our target for the month of March 2023. Rallies back into resistance zone of 17600-17900 will be opportunity to open aggressive longs.

Budget 2023 is a balancing act with a focus on prosperity and inclusiveness

The first budget of the Amrit Kaal (Budget 2023) is prudent against a tough macro backdrop of a high current account deficit (CAD) of over 3%, global monetary policy tightening and recessionary fears.

Though, finance minister Nirmala Sitharaman (FM) has kept a sharp focus to maximize the impact of every rupee spent to generate a multiplier impact in the economy.

A 10-lakh crore outlay from the central government for capital investments lays the foundation for strong multi-year growth for the country during its Amrit Kaal. Together with an extension of 50-year interest-free loans to state governments to boost capex, this is one of the highest pushes for capital investment in recent years.

The FM has continued to direct spending towards improving the lives of the people. The strong outlays for the Jal Jeevan Mishan to ensure drinking water for all and towards PM Avaas Yojna ensuring shelter for all have continued unabated.

Tourism has been a focus area for the government in the last few years because of its potential to generate revenue (both domestic and foreign) and employment. The budget is targeting 50 destinations to be selected via a challenge mode this year to be developed as full-fledged tourist spots for both foreign and domestic tourists.

Urging states to develop a Unity mall in the state capital or other prominent tourist centres to promote one district, one product, GI products and other handicraft products shall also boost the earnings of locals and help employment generation at the grass root level.

The budget also aims to boost manufacturing in India and has seen a sharp increase in incentives to accomplish the same. The government is also incentivizing the creation of future capabilities in areas of green hydrogen, chip manufacturing and artificial intelligence.

Amidst the focus to boost capital spending, the FM has not kept her sight away from being fiscally prudent and she has kept the fiscal deficit under control at 6.4 per cent of the GDP. Simultaneously, it has been ensured that spending is directed to better the life of the countrymen, especially the vulnerable.

The bulk of the spending is to uplift the poor and the neglected. The FM has continued her support for the free grain distribution benefitting 80 crore people for another year.

The boost in skill development and education is a focus area for the government that shall pave the way for future growth of the youth and in turn the country.

The middle class has also been a beneficiary of the budget with a little more money in their pocket. Raising tax slabs along with a reduction in peak surcharge shall result in around Rs 35,000 crore being saved by taxpayers and hopefully being spent to boost consumption.

At a time when the government will be going into general elections and many state elections coming ahead, the FM has refrained from the populist path and presented a balancing act.

Stock market closing down post-budget in our view has little to do with the budget speech and more with the premium valuations India is trading at compared to its peers.

Anshul Jain

Research Analyst

Stocks To Watch

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1.Sonata Software

Sonata Software Limited is a leading Modernization and digital engineering company, headquartered in Bangalore. Sonata provides modernization services using its proprietary Platformation approach. It specializes in cloud and data modernization, Microsoft Dynamics Modernization, Digital contact center setup and management, managed cloud services and digital transformation services. Founded in 1986, the company has since grown to have a presence in North America, Europe, and Asia-Pacific.

Particulars

Market Cap.	₹ 9,785.7 Cr
Total Debt	₹ 38 Cr
Cash and Investments	₹ 914.4 Cr
52 Week Range H/L	753/ 458
Equity Capital	13.9
EV	₹ 8,909.3 cr

Shareholding Pattern

	Mar-22	June-22	Sep-22	Dec-22
Promoter	28%	28%	28%	28%
FIIs	14%	13%	13%	13%
DIIs	15%	15%	13%	14%
Public/Other	43%	44%	46%	45%

Profit and Loss Statement

Y/E March (Rs Cr)	FY 22	FY 23E	FY 24E	FY 25E
Total Revenues	5553	7146	8336	9311
Growth (%)	31.3	28.7	16.6	11.7
Total Operating Expenditure	5090	6534	7538	8360
EBITDA	464	613	798	951
Growth (%)	22.2	32.1	30.3	19.1
Depreciation & Amortization	47	57	67	74
Other Income	102	46	58	58
Interest Costs	18	18	66	73
PBT before Exceptional Items	500	583	723	862
Growth (%)	42.1	16.6	24.0	19.1
Tax	124	140	179	207
PAT Before Exceptional Items	376	443	544	655
Exceptional Items	-	-	-	-
PAT Before MI	376	443	544	655
Minority Int & Pft from Associate	-	-	-	-
PAT	376	443	544	655
Growth (%)	54	18	23	20
EPS	27.2	31.6	38.8	46.7
EPS (Growth %)	16	16	23	20

Balance Sheet

Y/E March (₹ Crore)	FY 22	FY 23E	FY 24E	FY 25E
Equity	10	14	14	14
Reserves & Surplus	1089	1263	1480	1742
Net Worth	1099	1277	1494	1756
Minority Interest	-	-	-	-
LT Liabilities & Provisions	166	166	166	166
Total Debt	38	38	38	38
Source of Funds	1303	1481	1698	1960
Net fixed Assets	206	196	184	166
Goodwill	221	221	221	221
Long term loans and advances	-	-	-	-
Other non current assets	188	250	285	314
Loans and advances	-	-	-	-
Inventories	-	-	-	-
Current Investments	145	145	145	145
Debtors	893	1041	1214	1356
Cash & Cash Equivalents	770	875	1105	1385
Other Current Assets	133	187	219	244
Current Liabilities	1223	1390	1622	1811
Provisions	29	46	54	60
Net Current Assets	688	811	1008	1259
Application of Funds	1303	1481	1698	1960

Cash Flow Statement

Y/E March (₹ Crore)	FY 22	FY 23E	FY 24E	FY 25E
Net Profit Before Tax	500	583	723	862
Depreciation & Amortization	47	57	67	74
WC Changes	100	(81)	(0)	(0)
Other non cash adju.	(6)	(28)	8	15
Income taxes Paid	(156)	(140)	(179)	(207)
CF from Operations	486	392	619	744
Capital Expenditure	(10)	(25)	(29)	(33)
Change in Investments	(123)	-	-	-
CF from investing activities	17	46	58	58
Issue of Equity				
Change in debt funds/ lease liabilities	(81)	(24)	(24)	(24)
Dividends paid	(187)	(266)	(326)	(393)
Other financing cash flow	(3)	(18)	(66)	(73)
CF from Financial Activities	(271)	(308)	(416)	(489)
Change in Cash and Cash Bank Balance	96	105	231	280
Effect of Exchange rate changes	(3)	-	-	-
Opening Cash	677	770	875	1105
Closing Cash	770	875	1105	1385

Our Take...

Sonata Software (Sonata) offers IT services (30%) and product licensing & deployment (70%).
The company provides IT services to travel, retail, agri & commodities and manufacturing and software vendors. It also offers a Net debt-free and healthy double-digit return ratio (with RoCE of >30%)

Sonata's wholly-owned US subsidiary signed a definitive agreement to acquire a 100% stake in US-based Quant Systems (QS) for total consideration of US$ 160 mn (4.3x sales), US$65 mn to be paid upfront while the rest US$95mn to be paid in next 2 years based on certain milestones.
The acquisition is in line with Sonata'a strategy to accelerate IT services growth from hereon as well as strengthen its offering in BFSI and Healthcare verticals. Quant Systems's revenue grew 4x in the last 2 years and growth going forward is also expected to be strong. EBITDA margins for the company are also healthy i.e., upwards of 30%

The new CEO in the Q3FY23 earnings call had indicated that they are looking to double IT services revenue growth in the next 3-4 years and key levers for the same are:

1. Winning large deals & large accounts;
2. Continue expanding the services portfolio and develop a strong partner ecosystem to guide modernization outcomes,

1) Strengthen its presence in BFSI and Healthcare & Life science verticals

QS reported >100% CAGR revenue growth in CY20-22 reaching US$37mn in CY22. The company indicated that the EBITDA margin for the QS is upwards of 30%. Sonata indicated that for CY23 & CY24 QS's revenue is expected to grow by 30-35% and the EBITDA margin is expected to be in the range of 30-35%.
The company indicated strong growth for QS in the last 2 years, as well as higher revenue per employee, which could be attributed to data analytics, data engineering, and data privacy work projects which they have started recently as it commands a premium billing rate. Sonata also indicated that the lower end of billing rates for QS on-site employees are even higher than the highest billing rate currently being given to Sonata onsite employees.

Outlook & Valuation

Sonata's share price has grown by ~3x over the past five years (from ~| 238 in February 2018 to ~| 706 levels in February 2023).
We maintain our BUY rating on the stock.

Cyient

Cyient Limited (Cyient) formerly known as Infotech Enterprises Ltd is engaged in providing global technology services and solutions specializing in geospatial engineering design IT solutions and data analytics. Having its headquarters and development facilities in India Company serves a global customer base through its subsidiaries in the United States of America (USA) United Kingdom (UK) Germany Japan Australia Singapore and India.

Cyient's range of services includes digitization of drawings and maps photogrammetry computer-aided design/ engineering (CAD/CAE) design and modelling repair development engineering reverse engineering application software development software products development consulting analytics and implementation.

Market Data

Bloomberg	CYL In
Equity Shares (m)	113
Market Cap.	Rs. 106.8 billion
52 Week Range H/L	995/ 724
1, 6, 12 Rel. Per (%)	15/ 16/ 15
12M Avg Val	Rs 232 million

Shareholding Pattern

	Dec-22	Sep-22	Dec-21
Promoter	23.4%	23.4%	23.4%
FIIs	32.1	33.6	34.7
DIIs	25.0	23.7	22.8
Public/Other	19.6	19.3	19.1

Income Statement

Y/E March (Rs Mn)	FY 21	FY 22	FY 23E	FY 24E	FY 25E
Sales	41325	45344	59748	73588	82359
Change (%)	(6.7)	9.7	31.8	23.2	11.9
Cost of Services	27162	28453	37111	45589	50733
SG & A Expenses	8056	8675	12607	14769	16472
EBITDA	6107	8216	10023	13230	15154
As a percentage of net sales	14.8	18.1	16.8	18.0	18.4
Depreciation	1944	1923	2593	3238	3541
Other Income	684	687	123	221	247
PBT	4847	6980	7560	10213	11860
Tax	1133	1761	1845	2655	3084
Rate (%)	23.4	25.2	24.4	26.0	26.0
Net Income	3714	5219	5715	7558	8776
Change (%)	(0.3)	40.5	9.5	32.2	16.1

Balance Sheet

Y/E March	FY 21	FY 22	FY 23E	FY 24E	FY 25E
Share Capital	550	552	552	552	552
Reserves	29023	30614	32406	35729	38939
Net Worth	29573	31166	32958	35981	39491
Other Liabilities	3812	4061	7735	9534	10675
Loans	2755	3264	7264	7264	7264
Capital Employed	36140	38491	47957	52779	57430
Applications					
Gross Block	18558	19223	26223	27223	28223
Less: Depreciation	10779	11959	14552	17789	21331
Net Block	7181	6787	11671	9434	6892
CWIP	113	134	134	134	134
Intangibles	7191	6662	16662	16662	16662
Other Assets	1925	5318	5591	5854	6020
Current assets	28518	28972	28799	37807	46234
Debtors	8026	7333	10804	13306	14892
Cash and Bank Balance	14408	12157	6472	9125	12974
Other Current Assets	6084	8616	10157	12510	14001
Current Liab. & Prov.	8488	9382	14901	17111	18512
Trade Payables	4532	5259	8185	10081	11282
Other Liabilities	3872	3709	5820	5927	5995
Provisions	384	414	896	1104	1235
Net Current Assets	19730	19590	13898	20696	27722
Application of Funds	36140	38491	47957	52779	57430

Cash Flow Statement

Y/E March	FY 21	FY 22	FY 23E	FY 24E	FY 25E
CF from Operations	5872	7318	8307	10795	12318
Cash for working capital	2686	(973)	7908	(1108)	(702)
Net operating CF	8558	6345	16215	9687	11615
Net Purchase of FA	(949)	(626)	(7000)	(1000)	(1000)
Free Cash Flow	7609	5719	9215	8687	10615
Net Purchase of Invest.	(58)	(3197)	(11471)	(1500)	(1500)
Net cash from Invest.	(1007)	(3823)	(18471)	(2500)	(2500)
Proc. From Equity Issues	37	121	0	0	0
Proceeds from LTB/STB	(2134)	(1994)	0	0	0
Dividend payments	(10)	(2952)	(3429)	(4535)	(5266)
Cash flow from Fin.	(2107)	(4825)	(3429)	(4535)	(5266)
Exchange Difference	(31)	52	0	0	0
Net Cash Flow	5413	(2251)	(5685)	2653	3850
Opening Cash Balance	8995	14408	12157	6472	9125
Add: Net Cash	5413	(2251)	(5685)	2653	3850
Closing Cash Balance	14408	12157	6472	9125	12974

Our Take...

Cyient (CYL)'s operating performance has inherently been subdued over the past several years as a few of its growth engines remained weak and underperformed that of its peers. In addition, execution challenges have marred the company's overall topline growth.

According to the management, the challenges under Aerospace and Communications segments (~50% of service revenue) have bottomed out and these segments are likely to improve and stimulate overall organic growth (guided at 13-15% in constant currency (CC) terms) in FY23E.

Additionally, its revenue growth should also amplify led by the inorganic components (~14-15% of FY23E revenue) and gradual recovery in its Design Led Manufacturing (DLM) business (guided high single-digit CC growth).

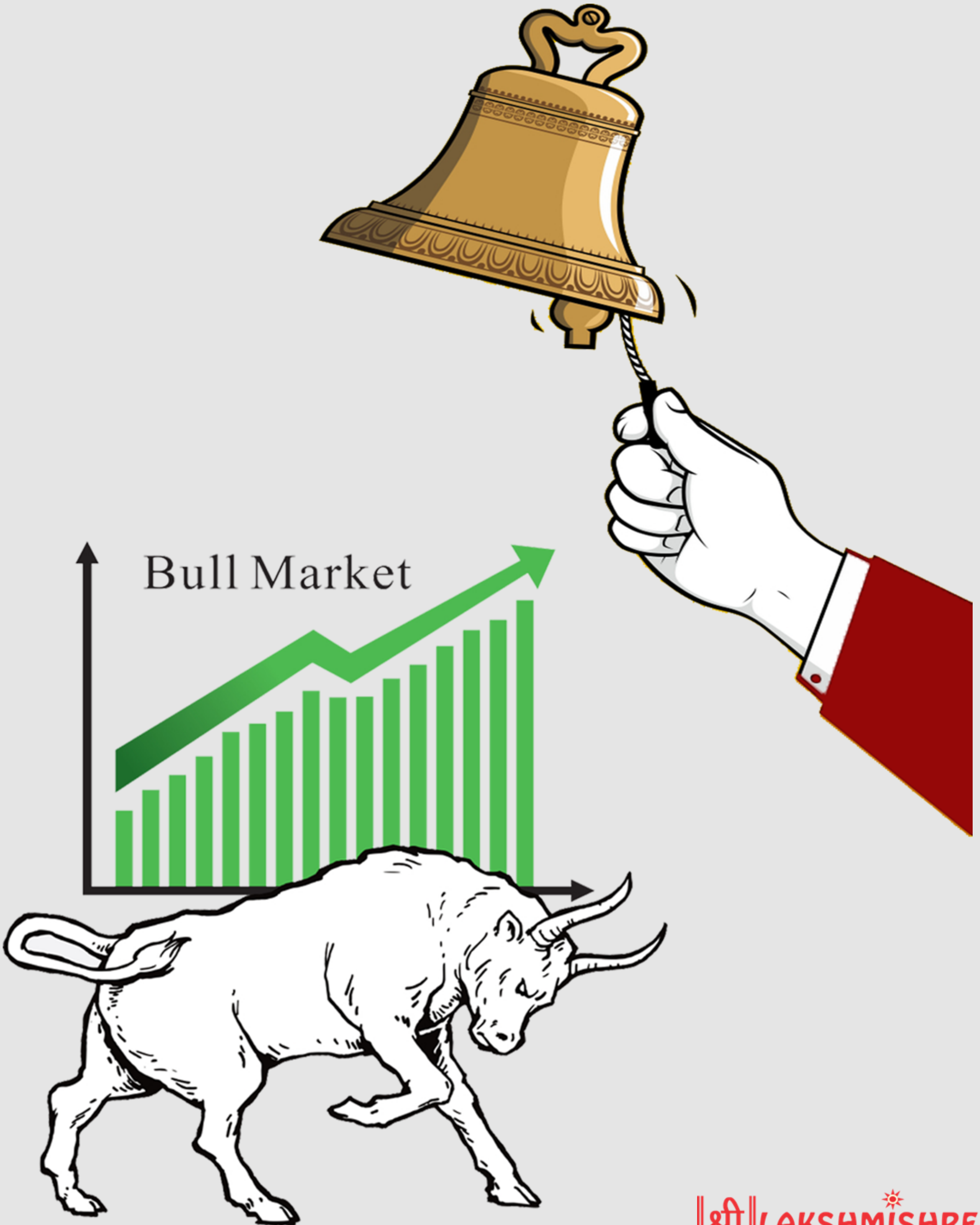
CYL has reported organic service revenue CQGR of 2.4% between 1QFY22 and 3QFY23 despite the Aerospace, Rail and Communication (ARC) segment remaining soft, which reported a 0.9% CQGR during the same period.

Outlook & Valuation

CYL's service segment is shaping up quite well with a majority of its growth engines (excluding Rail, Consulting and Utility) sustaining the positive momentum and delivering robust growth of 15% YoY in 9MFY23. Conversely, other segments are on the verge of recovery and should incrementally contribute to its overall growth in FY24E.

However, the current valuations at 18x/14x FY23E/FY24E EPS of INR51.9/ INR68.6 appear highly attractive giving us more comfort to maintain our BUY rating.

This May Impact Your Investments!!



Four Economic Trends That Will Impact India

Four broad trends will impact the Indian economy in the years to come. The Budget for 2023-24 affirms these trends.

1. Government capital expenditure will drive the economy in the medium term:

The latest Economic Survey underlines the fact that government capital expenditure has risen from a long-term average of 1.7% of gross domestic product (GDP) in the period FY09 to FY20 to an estimated 2.9% of GDP in FY23. The latest central Budget expects capex to rise to 3.3% of GDP in FY24. This points to an inconvenient fact: Private investment has remained sluggish and the government has had to compensate. The behavior of private investment is not unique to India. It is part of a trend that is seen in emerging and developing economies (EMDEs). As the World Bank's *Global Economic Prospects* (2023) points out, investment growth in EMDEs in 2022 remained about a 5% age point below the 2000-2021 average, and nearly 0.5% age point below in EMDEs, excluding China. The World Bank does not see private investment returning to the level suggested by the pre-pandemic trend through 2024. It lists several factors responsible for the slowdown in investment growth in EMDEs: Slower output growth in 2010-19; lower commodity prices; lower and more volatile capital inflows to EMDEs; higher economic and geopolitical uncertainty; and a substantial build-up of public and private debt. Many of these factors apply to India. The government sees a sharp rise in capex in FY24 as boosting output growth. This overlooks the fact that the fiscal deficit is projected to decline by 0.5% of GDP in FY24. We have a withdrawal of stimulus, something that is contractionary in nature. True, the composition of expenditure has shifted even more towards capex, and this is expansionary. But this effect can overwhelm the contractionary effect of a fiscal deficit decline only if the rise in capex is greater than the decline in the fiscal deficit. In the budgetary projections, the rise in capex is 40 basis points whereas the decline in the fiscal deficit is 50 basis points. The net effect will, therefore, be contractionary.

2. High fiscal deficits are here to stay:

Analysts cheered the finance minister for sticking to the fiscal deficit of 6.4% for 2022-2023, and projecting a fiscal deficit of 5.9% for 2023-2024. The figure for 2023-2024 is a budget estimate. If the Ukraine conflict escalates and the global situation worsens, government subsidies (which have been pruned in FY 2023-2024) will rise and we could be back to square one. We must also expect sops to be rolled out in the run-up to elections in 2024.

The fiscal situation can be turned around in a fundamental way only if the tax-to-GDP ratio goes up significantly (say, above 12% of GDP) or if capital receipts from disinvestment rise significantly or both. On either count, the outlook is not promising. The tax-to-GDP ratio is estimated at 11.1% for 2023-24. The peak in the past decade has been 11.4%.

As for the proceeds from disinvestment, the Economic Survey notes that total proceeds from the sale of equity in public sector units (PSUs) amounted to ~4 trillion in the eight-year period from 2015 to January 2023, or an average of ~50,000 crores in a year. Strategic sales have yielded a mere ~69,412 crore in the entire period. It does look as though the Fiscal Responsibility and Budget Management target of 3% will remain a distant dream. After the global financial crisis and then the pandemic, we are seeing a rise in government deficits and public debt everywhere. India is no exception. If anything, the rise in debt-to-GDP ratio from 81 to 85% between 2005 and 2021 looks modest in comparison with the increases elsewhere — 66 to128% in the US; 39 to 95% in the UK;26 to 72% in China; and 69to 93% in Brazil. India's public debt position looks even better when we take into account the fact that 95% of the liabilities are domestic, and we have the growth-interest differential working in our favor.

3. Inflation will be higher than before:

High fiscal deficits can be expected to translate into high inflation. That apart, deglobalization will happen to a greater or lesser degree. The movement may be gradual, but the direction is clear enough. Globalization was about procuring goods and services at the lowest cost from almost anywhere in the world. Princeton historian Harold James noted recently that there is a historical pattern of globalization driving disinflation. Alas, it appears the trend toward globalization is now being disrupted. Post-Covid and post-Ukraine, every country is reassessing its extent of dependence on outside suppliers for a range of goods and services. The US and its allies are determined to reduce dependence on China to the maximum extent possible as the containment of China have become the West's strategic priority. There has been serious academic discussion in the US about revising upwards the inflation target of 2% so that monetary policy has more room for maneuvering in the downward direction. In India, the inflation target of 4% threatens to become largely notional. We would be thankful now if inflation falls below 6%.

4. Self-reliance and import-substitution are a reality:

For the reasons cited in (3) above, "make at home" will gain importance. This will be especially important for leading economic and military powers. As India moves towards becoming the third largest economy in the world with matching military clout, a lurch towards greater self-reliance is inevitable. We need not be unduly apologetic about this trend: We are only falling in line with a worldwide trend. The adjustments in tariffs in the recent Budget, analysts have noted, are aimed at helping the domestic industry. It's no use bemoaning the trend towards protectionism in various economies, including India. It makes more sense instead to make a success of schemes such as production-linked incentives. We must find ways to limit abuse of discretion in industrial policy. We need to monitor the effectiveness of the PLI scheme using appropriate metrics. Industrial policy will be integral to economic policy in the years to come.

Macroeconomic outcomes in the coming years will be governed by the four trends outlined above.

India's Reputation Will Survive Hindenburg

In India, the consensus is very difficult to achieve about anything. But there is a surprising degree of consensus in the public sphere about the possible fallout of the Hindenburg Research report on the finances of the Adani Group. Few believe, even today, when some Adani stocks hit multi-year lows, that the group will be forced to go out of business. Few believe that Prime Minister Narendra Modi, with whose rise to power the Adani Group has long been associated — fairly or unfairly — in the public mind, will suffer serious political repercussions from this. Mr Modi's popularity is too deep-rooted for one such story to make a difference. And nobody thinks that India's current economic strategy, which depends upon the identification of leading sectors and national champions, will change because one of those champions is under pressure.

Instead, both critics and supporters think that the real impact of the Adani saga will be on the reputation of India itself — as a policy jurisdiction, as an investment destination, and as a place to do business. The more conspiratorial-minded of our fellow countrymen, who are hopefully over-represented on social media, believe that such stories are coordinated and designed to make India look bad. Others, perhaps more rational, are concerned that the impact of such stories will be to turn the world off India at a point when it seemed that investor interest was spiking.
Both views are in fact wrong. One very much so, and one less so.

The conspiracists must recognize that there is no great lobby in the Western world that seeks to undermine India. Quite the opposite, in fact. The West has bet heavily on India's long-term prosperity. Rather than being wedded to the notion that India will fail and thus creating stories intended to bring it down if Western opinion possesses any institutional biases about India they are the following: First, the notion that India will grow sufficiently to counter-balance China; second, that there will be investment opportunities (such as those provided by national champions including Adani) that make Western investors money; and third, that India is substantively different from China in that it has more open and transparent systems. There is simply no lobby with any influence in the Western world that seems to bring India down. Such conspiracists can never explain concisely and rationally what the incentives for such a lobby would be.

What about the other side of this consensus? Those who worry that such stories will turn the world off India are not looking at the entire picture.

The sole accusation that has been levelled at Indian institutions, regulators, or politicians in this saga is the suggestion that the securities market regulator has not moved swiftly enough on investigation of concerns about some investments in the Adani Group. This is an accusation that can be easily answered — and, if found to be fair, as easily corrected. The impact of any such course change on the broader Indian economy need not be strongly negative. The impact on trust in Indian institutions will be strongly positive.

It is also worth noting that statements from government officials on this matter have been restrained, and clearly seek to dissociate the government from the issues at stake. The Union finance minister has said that “one instance, no matter how much it is talked about globally, is not going to be indicative of how well the Indian markets are governed”. This does not prejudge the truth of the allegations one way or the other, but merely points out that Indian market governance has a reputation independent of and beyond this case. It is hard to see how this statement could have been bettered. The Union commerce minister said in Parliament that the government has “no role” in “purported wealth” that is a “share market calculation”. No attempt to backstop the group rhetorically or actively is visible at this point. Meanwhile, various regulators, including the Director General of Corporate Affairs, have reportedly responded to the story by having a look at the allegations in it.

If such an attitude continues to characterise the official response, then it is hard to see why the current level of trust in Indian institutions will be irreparably damaged.

As India rises, and as its economy becomes more consequential and its companies and institutions acquire global reach, they will face more scrutiny. This should not be seen as a danger, but as a normal byproduct of size and influence. Not all these stories will be positive. But even the negative ones need not harm the broader national interest, as long as our response to them is rational and transparent. Let that be the immediate lesson we take home from the Adani saga.

Air India is blazing a comeback trail

The announcement by Air India that it will buy 470 aircraft – 250 European Airbus and 220 American Boeing – in what has been described as the largest single-tranche aircraft purchase in the world, marks a breath-taking revival of the carrier in barely a year. The Tatas, who had founded the airline nearly a century ago, have returned to revive it with resources, expertise and certainly a degree of emotion.

The mega purchase comes close on the heels of several other critical initiatives underway. The carrier is expected to complete by the end of the next financial year the merger of Vistara with Air India, and Air India Express with Air Asia.

What is more important and underlines the way the health of the formerly ailing airline has been turned around, it is expected to post a consolidated profit in the current financial year (2022-23), compared to a standalone loss of Rs 7,000 crore in the previous year (2021-22). This has been built on the foundation of an upswing in revenue, from around Rs 70 crore per day pre-privatisation to Rs 100 crore post-privatisation.

Profitability has been improved by following a two-pronged strategy. One is bolstering the topline by increasing the capacity to carry more passengers. The number of seats on offer has been raised by getting to fly more aircraft which have been sitting on the ground. Plus, action is being taken to improve loyalty programmes and partnerships to attract more passengers. The second initiative is to tackle the cost structure through automation and most recently the deployment of artificial intelligence.

The progress made in a single year has been described by Air India's new CEO Campbell Wilson as "nothing short of stunning". All this makes the privatisation of Air India stand out against the backdrop of the government missing its disinvestment target year after year.

Several elements have gone into the turnaround in the performance of the company. One of the most dramatic is the improvement in its on-time performance. From being the sixth in April in terms of overall performance, it has improved its position to third in September, behind Vistara and Air Asia, according to DGCA data. At 87 per cent, it is ahead of the industry market leader Indigo's 84 per cent.

According to an analysis by Forbes, in chalking out a turnaround strategy Air India had to make a choice – offer an exceptionally cheap or an exceptionally good product. It chose the latter. It also set itself the foremost target of growing its network and fleet. On this it has just made its major announcement.

The strategy also outlined a whole set of facets that would go to improve the customer experience. On that foremost came reliability and on-time performance. Progress on the latter has already been achieved. It will also try to be the best in the industry in terms of technology and sustainability. In terms of timelines, the first six months will address issues accumulated over time, the next 18 months will focus on systems, people, aircraft and training. Over the next couple of years, it will do all the myriad things that take an organisation from being merely good to being world-class.

Where will all this lead? Air India will target at increasing its domestic market share to 30 per cent in the next five years and significantly growing its international routes. Till September it had achieved a market share of 9 per cent, compared to the market leader Indigo's share of 58 per cent.

What has and will continue to help Air India as also the other carriers is the decline in the COVID pandemic which is giving people the confidence to travel more. There is also a bunching up of demand, so to speak, as people are seeking to undertake all those trips that they could not do earlier because of COVID lockdowns and restrictions.

Additionally, the Indian economy is growing at a relatively healthy pace, compared to most other large economies. This growth in the case of India has assumed a K shape which is putting a disproportionate amount of additional income in the hands of the better off. This is allowing overall discretionally spend in the economy to go up much faster than general rise in income. As a result, the amount of spend that air travel is being able to attract is up sharply.

Against these positives there is a major adverse development that carriers across the world have to live with for now – the Ukraine war which has caused fuel prices to not just skyrocket but also make the market volatile. Even as more people travel and there are more 'bottoms on seats', carriers' margins are being hit by the rise in fuel prices, market volatility and supply uncertainty. This cannot bode well for the health of the industry and its leading players.

A Great Year For Railways

For the Ministry of Railways, which is focusing on leapfrogging to a freight volume of 3 billion tonnes over the next decade, the finance ministry has provided a marvelous bonanza —budgetary support of ~2.4 trillion. The entire 11th five-year plan (2007-12) could promise less than this outlay for the Railways.

There must be reasons for such encouraging support. One is that the government is pleased with the Railways moving towards 1.5 billion tonnes of freight loading in 2023, a milestone despite the Covid-19 pandemic. Next, 2023 will be a great year. Economic, and commerce and industry ministries are poised to unveil some highly visible projects that are nearing completion at a frenzied pace.

The showcase projects of Railways, too, now have an opportunity to accelerate the hectic pace of last-mile connectivity, and funds must not be a constraint at all. In 2022, one of the highly visible symbols of modernization in Railways was the new Vande Bharat train sets. Nationally, they have attracted a lot of attention.

The freight business unexpectedly made enormous gains even during the second wave of Covid-19 and even later. The Railways, which stimulate almost all sectors of industries and commerce by transporting raw materials and finished goods, is moving much more BTKMs (billion-tonne kilometres) during and post-pandemic times. BTKMs are the Railways' bread-winners. After Covid hit, freight has emerged from the decade-long hapless trap of clocking 691 billion in 2011-12 and 707 billion in early 2020. These gains since 2021-22 were possible only because of the Centre's substantial fiscal support for infrastructure expansion and modernization through the finance ministry and the Railways' intense use of its assets — track and rolling stock — by stretching their capacities to absorb the pent-up demand.

Freight BTKMs leapfrogged from 707 billion in 2019-20 to 807 billion in 2021-22. In the fiscal year 2022-23 (FY23), even as pent-up demand is plateauing, my guess is that the Railways is preparing for another big leap in BTKM. Despite even a likely drop in tonnes moved in FY23, higher leads (average distances that the freight moved) are pushing up BTKMs. BTKM, as a reliable performance index, is a combination of kilometers over which tonnes of freight are moved. The Railways' freight rates are also among the lowest among global peers.

Now, about the future of BTKMs-led rail business growth during times of climate change. Roughly, 60 % of India's rail BTKMs are from non-coal commodities and 40 % from coal. Will coal start shrinking in the Railways' commodity basket? Not likely. One offshoot of the present global energy crisis is the revival of coal-based power plants and the coal industry is likely to get a new lease on life. However, for the Railways, expanding the non-coal commodities basket is of paramount importance.

With bigger BTKMs, and revenue passenger kilometers returning to expected levels, rail finances appear to be somewhat stable. There is a need to strengthen the sales teams to raise more interstate, intercity, long-distance, and ordinary passenger ridership. There is a need to have a deep look at sundry and other earnings. Possibly, better expertise may be required to expand the parcel business and land asset monetization plans. Both of them need new business and revenue models.

Sebi order against 'dubious' Telegram channels is an eyeopener

A year ago, SEBI had carried out search and seizure operations against several parties across various towns for allegedly carrying out market manipulation activities through channels hosted on the messaging app Telegram. The operations followed complaints about the circulation of stock tips through this channel. After detailed investigation and evidence-gathering (which, surprisingly for such alleged activities, was available aplenty), correlation, etc., SEBI has now, on 25th January 2023, passed an interim order against 19 parties. This order gives several directions against the parties, including asking them to refrain from dealing in securities markets and has impounded gains of Rs 3.89 crores.

The order displays the use by SEBI of the latest technology combined with a healthy dose of old-fashioned detective work. The findings of SEBI are by way of an interim order and hence issued before giving an opportunity to the parties to present their case. As will be seen, the findings may be disputed by the parties and the outcome may become known much later. Yet, the findings are as much predictable as depressing. Predictable because similar alleged pump-and-dump operations have been heard of repeatedly in the past. It is also depressing to see how so many people fall prey to greed. Further, just two Telegram channels had about 23 lakh subscribers and, as SEBI rightly observes, even if a minuscule number of these people act on fraudulent suggestions, the manipulators can earn crores in a short time. Let us first quickly summarise what happened as described in the order.

SEBI raided persons against whom there were complaints of giving such tips through messaging app. Mobiles, hard disks, pen drives, etc. were seized. While, as said earlier, the broad nature of pump-and-dump operations are well known, this is for the first time that the modus operandi is revealed in vivid forensic detail, worthy of a thriller movie or book. SEBI has examined call records, locations from where calls were made from, examined call recordings, WhatsApp chats, bank records, etc. A person who controlled a broking firm and a listed company was alleged to have taken the help of certain persons operating Telegram channels to boost up the price of the listed company's shares. This was pre-planned with the end objective being to offload shares to those subscribers to Telegram channels. As SEBI said, psychological tactics were applied, making subscribers feel the Fear Of Missing Out (or FOMO, as the slang goes) and hence making them jump on the bandwagon to buy shares. SEBI also detailed how the price was first boosted by the parties through internal trading.

However, while this is the broad picture, the details and specific issues make this case even more interesting. One is about how rampant such Telegram channels are. Just the two channels run by the parties had more than 23 lakhs subscribers. Many of these were paid ones too with the subscribers paying a substantial sum Rs 5,000 to Rs 10,000 per week/fortnight/month for getting tips. This by itself is a money spinner but may be an illegal operation if carried out by unregistered parties and against SEBI regulations. Such channels are rampant even today. A cursory search by me showed up several channels with lakhs of subscribers.

SEBI describes the parties as technically sophisticated. However, curiously, the gadgets themselves gave away the game. The parties had recorded the telephone conversations of the sharing of illicit gains, part of which SEBI has transcribed in the order and even uploaded for anyone wanting to hear it! Working of the gains and its allocation to respective parties was shared by WhatsApp, which too was found by SEBI and these are also part of the order. As is now common in such investigations, SEBI checked the call records and even the mobile locations to corroborate its allegations about the contacts between the parties and that they were acting in concert.

Call recordings and WhatsApp messages act like the proverbial smoking guns giving that conclusive evidence that investigators dream of. They lay bare the detailed discussions of how much high the price should be taken to, how the profits beyond a particular price would be shared and even how and why a certain amount would be retained as security. At one point, the recording reveals how the alleged mastermind, while explaining why he needs to retain some amount as security, says, “Mein beimaan aadmi nahi hu lekin…” (I am not a cheat but…). The sheer irony here cannot be missed and how, while on one hand, unsuspecting investors were being fleeced, there is also solemn swearing of honesty between the parties.

The order also finds trails from the bank statements of the parties of the flow of monies between them, particularly the alleged sharing of gains. Here again, they fall together in a place like a jigsaw puzzle with the call recordings, WhatsApp chats and mobile data records to complete the picture. The 93-page order has several more such findings.

However, two questions arise here. Will the order stick in all aspects and all the parties? Secondly, will such an order prevent further such cases?

The first question points to the difficulties of bridging the gap between the findings and allegations and putting them through the eyes of the law. To reiterate, it is an interim one-sided order and hence all the findings can be treated as allegations at this stage. At times, if there is overzealousness, some or all parts of the conclusions and orders may fail. It is seen that a lot of the evidence could be disputed. Some of the conclusions are based on alleged confessions and statements of parties against the other. The accused may demand cross-examination of these parties. They may also claim that the statements may be self-serving, under duress, etc. The accused may raise questions about whose voice was in the call recordings. Plausible explanations may be offered for the calls, for financial transactions, etc. The task of the authority would become even more difficult during criminal proceedings against the parties if initiated (indeed, if the findings are true, there cannot be more deserving cases for prosecution). Criminal proceedings require a much higher benchmark of proof.

On the second question, the reality is that despite such searches and seizures being widely reported, Telegram channels and other means continue uninterrupted. Also, parties could be even more technically sophisticated. Not all parties keep call recordings that are readily available or make bank transactions directly between them. Messaging apps provide for ‘disappearing’ features where chats get periodically purged – and of course, parties may delete incriminating messages themselves. Above all, greed for quick and easy profits is almost hard-wired in many members of the public. The positive aspect here is the case has been made after truly conscientious efforts by SEBI to investigate the case. More such cases, which are then well-publicized and discussed, should make a very large section of the public aware and would then, hopefully, resist such temptations.

Fortunes Of The Cotton Textile Industry Go Into A Tailspin

The uptick seen in textile exports from India at the beginning of 2022 failed to sustain in the latter part of the year. Rising interest rates and inflation-led price increases punctured consumer demand in Europe and the US, which are big markets for Indian textiles.

Within this, the cotton textile industry -raw cotton, yarn, ready-made, knitwear and home textiles- has been crippled by the geopolitical ramifications of the Russia-Ukraine war and the pandemic on global trade and demand-supply dynamics. Industry data shows that between April and December 2022, exports of cotton yarn, textiles, ready-made and handlooms together plunged by 27 per cent year-on-year (YoY). It worsened in January 2023 when exports dropped by a sharper 32 per cent YoY.

The overarching reason is a slowdown in demand in Europe and the US, which individually account for between 27-30 per cent of India's total exports. The economic slowdown lowered discretionary spends in these nations affecting demand for fabric, ready-mades and home textiles. China's extended lockdown exacerbated the situation. Meanwhile, lower-than-expected cotton production on home soil along with duty on imports also kept prices of cotton and yarn elevated. This, in turn, contributed to lower demand from end-users.

As a result, after peaking at abnormally high levels in May (cotton touched Rs1,00,000 per candy, which is equal to 356 kilograms of ginned cotton), cotton prices started tumbling. The February cotton price is about 20 per cent lower than a year ago and 37 per cent lower than peak levels of May. Yarn prices have been falling with a similar momentum.

Analysts reckon that skyrocketing cotton and yarn prices in the last one year punctured demand, triggering the demand drop. Trading at a premium to international prices meant that India's cotton and yarn became uncompetitive.

Given this scenario, textile mills and integrated units are now in the "wait-and-watch" mode. There have been production cuts in the last few months. Utilisation levels have dropped. Profit margins are being squeezed amid weak prices and high all-round costs. Job cuts are feared in a substantial way if there is no relief soon. "Globally, ready mades demand is likely to remain muted at least in the first half of fiscal 2024 as well. So, it is unlikely that existing capacities of players, especially export-oriented SMEs which account for a majority of the sector, will be fully utilized," says Aniket Dani, Director - Research, CRISIL Market Intelligence and Analytics.

However, there is a ray of hope that the reopening of China's economy, which accounts for around 20 per cent of cotton yarn exports from India, will fuel global demand for textiles and yarn. Analysts are unsure though of the extent of benefit. While the reopening might improve yarn demand, it may not boost textile exports since China also uses yarn for its own production of fabric and garments. Further, in developed markets, apparel demand itself is expected to remain low in the near to medium term.

Making matters worse for India is that cotton yarn imports witnessed manifold increase during the first nine months of FY2023. This is particularly from Vietnam, as domestic cotton prices were rising sharply and prevailed above international prices.

To sum up, the cotton textile industry has been in a tough spot during the past few quarters. A changing global environment has marred fortunes of both the spinning and weaving industry. Further, most mills carried sizeable inventory of raw materials when raw material and other commodity prices surged, in a bid to minimise the impact of rising input prices. However, this backfired when cotton and yarn prices tumbled in the last six months, leaving smaller mills saddled with higher inventory carrying costs that weighed down on profitability.

It is too early to gauge the impact of China's reopening on the cotton textile industry. In the near term, only an easing of costs of raw materials such as cotton and yarn would result in a brightening of prospects.

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