M&A Insights
India

HIGHLIGHTS | DECEMBER 2019

TMT
TMT still a star attraction

HEALTHCARE
The best prescription for the global medicine space

TMT
Digitalization drives Indian M&E sector expansion
It is my pleasure to present to you the inaugural edition of the M&A Insights – India magazine. Apart from updates on promising sectors for M&A in India, the magazine will also showcase conversations with India’s prominent finance and business leaders. In this inaugural issue, which I have the pleasure of co-editing, we are sharing a brief introductory overview of the Indian M&A landscape.

Over the past decade, Indian companies have mainly focused on the domestic market for consolidation. This is largely due to high domestic growth (a GDP increase of more than 7% over the last five years), with substantial future expansion opportunities making domestic acquisitions attractive: and also, because of the increasing cost of cross-border acquisitions (due to the high cost of capital; debt financing can be upwards of 8.5% without currency hedge and the steady depreciation of the Indian rupee versus the US dollar).

2018 was a milestone year for markets, as M&A activity in India hit US$130 billion in value. This was characterized by platform transactions in infrastructure and energy, inbound M&A transactions, financial sponsor buy-outs and industry consolidation opportunities arising out of the Insolvency and Bankruptcy Code (IBC) process (more on that later).

2019 has seen subdued M&A activity, given the stress in the financial system due to various challenges — including accelerated reforms disrupting the usual way of doing business, some related stress in financial institutions and geopolitical tensions, among others. With the emphatic election victory of the ruling National Democratic Alliance (NDA) coalition in the recent general election, the Modi 2.0 government has undertaken decisive policy reforms and initiatives — like sharp, corporate tax cuts to stabilize and grow the economy. There is a virtual, ongoing detoxification of the economy and, while the outlook has been neutral to negative on M&A activity, many business leaders see the current churn as long-term positive.
The Indian economy is going through a painful period but is expected to emerge with greater transparency and an emphasis on high standards of corporate governance in the business community. Focus is on strong auditing and credit-rating standards. Banks and financial institutions are being held accountable for robust risk management and credit rating.

The government is committed to enhancing the ease of doing business in India, and Modi 2.0 has introduced pathbreaking structural reforms. It is not possible to discuss them all in the context of this summary, so we encourage you to read additional material on initiatives like JAM (Jan Dhan: ensuring all Indians have a bank account; Aadhar: unique identity number; Mobile: access to affordable mobile data). Some notable focus areas include 100% electrification/grid access, which will bring an additional 30%+ of the population into the mainstream economy. The IBC ushered in a substantial insolvency reform, enabling banks to resolve delinquent accounts transparently and rapidly in a time-bound manner. The goods and services tax (GST) has made the tax structure much simpler. The government has offered significant corporate tax cuts, making India an attractive tax regime on par with other South East Asian countries. Several other reforms are in various stages of implementation.

The current government is expected to continue its reform process and make India a much more enticing investment destination for overseas investors, corporate houses and, of course, for domestic M&A.

Pension Fund Limited managers, largely out of Canada (CPPIB, CDPQ, Brookfield and others) and, to some limited extent, Australia, have introduced long-term patient capital to the Indian economy. Most have preferred a platform approach to M&A and have built up large, hard business assets around a competent core of management.

Preferred sectors are commercial real estate, warehousing, toll roads and renewable energy. India recently saw the first-ever public listing of infrastructure investment trusts (InvITs) and real estate investment trusts (REITs).

Most global private equity funds and sovereign wealth funds have local presence and have been actively investing in India. Historically, funds have focused on growth capital taking minority stakes in high-growth companies and exiting either through a strategic sale or an initial public offering (IPO). In the last few years, there have been various opportunities for buy-out, and this is now becoming a preferred route for funds.

Significant disruptions of business models are hitting Indian shores as well. The technology, media and telecom (TMT) sector has seen major consolidations, with the emergence of new players. Internet of Things (IOT)-enabled businesses in logistics, FinTech, food delivery and eCom are receiving capital from global investors. We fully expect continued business activity in TMT, logistics and infrastructure in the coming years as India catches up with the rest of the developed world markets. This will open up various opportunities for inward investments in these sectors.

The next few years will be very exciting, as the country reaps the benefits of reforms and global capital makes its way to India. With its deep demographic advantages and the availability of a robust financial sector backed by a business-reform-oriented government, we expect M&A activity to increase manifold.

I hope you will enjoy reading this magazine and benefit from it. We welcome your feedback and any suggestions on what you would like to see in future issues.

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COMMENTARY | TMT

TMT still a star attraction

Despite a decline in overall deal value and volume this year, strong demand in the technology, media and telecom (TMT) sector continues, particularly for companies involved in data collection and analysis.

COMMENTARY

Update on Indian economy

Amidst a challenging and uncertain global economic backdrop, India's relative global appeal remains intact.
The best prescription for the global medicine space
The Indian pharmaceuticals sector is the third-largest market globally in terms of volume and the 13th largest in terms of value.

Digitalization drives Indian M&E sector expansion
The Indian media and entertainment (M&E) sector is a US$24 billion industry and is expected to reach US$34 billion by fiscal year 2020–2021 (FY21).

Ambition on a grand scale
Anshuman Singh, chairman and managing director of Stellar Value Chain Solutions, talks about the US$40 billion to US$50 billion of investment needed to modernize and restructure India’s logistics sector to support the phenomenal growth expected over the next five years.

The opportunity to apply a global outlook to local consumption
Future Group CFO Sanjay Jain provides key insights into the structure of India’s vast, US$800 billion to US$850 billion retail market, which grows by US$50 billion every year, and the wealth of investment opportunities available in catering to its 1.3 billion inhabitants.
Preparing for sustainable growth

Amidst a challenging and uncertain global economic backdrop, where geopolitical uncertainty and trade tensions have taken center stage, India’s relative global appeal remains intact, albeit in the medium term.

India is fundamentally well positioned, with its core strength residing in the increase in the share of working-age population along with the recent reset in the corporate tax rate, which has boosted the country’s global competitiveness.

However, near-term concerns have emerged with Q1 FY20 GDP growth slipping to a 25-quarter low of 5% and a widening of the negative output gap for FY20. Not only do the leading indicators of urban and rural consumption, along with that of investment, paint a dismal picture, but also uncertainty about global demand is taking its toll on India’s exports. The anemic growth of all major growth drivers is clouding fiscal consolidation prospects with fisc coming under pressure from various stimulus measures announced in the last three months against a background of a slowing economy.

Despite fiscal consolidation pressure coming to the fore, the government is cognizant of the growing need to bolster the economy. Its efforts to revive the animal spirits in an ailing economy range from implementing demand-side measures, like the PM-KISAN scheme in the FY20 union budget and the increase in dearness allowance for central government employees, to promoting supply-side measures, like targeted micro steps for sectors such as auto; micro, small and medium enterprises (MSMEs); affordable housing and non-banking financial companies (NBFCs)/housing finance companies (HFCs). According to our estimate, after adding the budgetary allocation for PM-KISAN, the net fiscal stimulus for FY20 comes to ~US$26 billion (0.9% of GDP). The fiscal impact of all the non-budgeted measures comes to ~US$15.4 billion (0.5% of GDP) on a net basis.

The big-ticket reduction in corporate tax is a major fiscal policy lever adopted by the government that has not only resulted in improved market sentiment — as seen by the outperformance of the Indian equity market relative to most of its peers since the announcement of the corporate tax cut — but has also led to price cuts by a few companies (especially in the auto space). Even as the effective corporate tax rate has been brought down for existing companies, the effective tax rate of 17% for new manufacturing setups incorporated post 1 October 2019 is a win-win situation. This could potentially help companies (in search of new production facilities) consider India as an investment option in the face of the ongoing trade war.
Among such measures, the government’s cash transfer program further catalyzes the near-term growth momentum. Total cash-based transfers have increased from 0.1% of GDP in FY14 to 1.1% in FY19. This is likely to touch 1.4% in FY20. We also note a structural shift in the pace of bank-based transactions post-demonetization. The government’s emphasis on the Digital India drive, the liberalization of the e-commerce sector and steadily growing income levels are expected to support online consumption in India. This is likely to improve economic efficiency in the longer run.

All these measures, coupled with the accommodative stance of monetary policy, are likely to provide a leg up to economic growth in the next six to eight quarters. Following the cumulative 135 bps reduction in the repo rate since February 2019, bank lending rates have also started to respond in the same direction. Provision of surplus liquidity in the banking system would further aid transmission, as there is normally a two- to three-quarter lag between policy rate and economic variables.

Besides the government measures, the Reserve Bank of India (RBI) has also undertaken steps to support sentiment and growth via boosting primary liquidity in the market, providing record high transfers to the government, the introduction of external benchmarks for improving policy transmissions, relaxation of external commercial borrowings (ECB) requirements and relaxing the prompt corrective action (PCA) framework.

However, the sharp, negative surprise in the Q1 FY20 GDP print gave rise to expectation of a severe downturn in economic growth momentum, leading us to mark down our FY20 GDP growth forecast to 6% with downside risk. We do not expect any near-term impact on GDP growth from the current set of measures outlined above. However, the near-term revival in sentiment is likely to be palpable, which in turn should arrest the current downside risks.

The favorable monsoon outturn in 2019, with the south-west monsoon ending with a surplus of 10% (vis-à-vis the long period average [LPA]) in contrast to the forecast of a deficit of 4%, is likely to aid rural consumption. The recent spurt seen in food-price inflation is likely to be transient, and we expect it to be offset by the arrival of kharif produce and better prospects for rabi sowing, led by surplus rainfall and adequate water reserves.

With consumer price index (CPI) inflation projected to remain below 4% (averaging at 3.5% in FY20 as compared with 3.4% in FY19) for the third year in a row, and the monetary policy reaction function of the RBI becoming more sensitive to a negative output gap, expectation of further monetary easing remains on the table. The overnight index swaps (OIS) market expects about 45 bps of incremental monetary easing from the RBI over the next year. We expect the RBI to deliver another 25–40 bps in the remainder of FY20, before getting into a prolonged pause.

Over the next six to eight quarters, the impact is likely to play out as the tax multiplier kicks in.

According to our estimate, the corporate tax rate cut will eventually bring about higher growth in the medium term via a multiplier of ~1. The boost to bottom line for companies is likely to manifest in the form of (i) higher capex, (ii) higher payment to shareholders and/or (iii) payment of past debt. Similar expansion is likely to be experienced via the PM-KISAN rollout, which also has a multiplier of ~1. This is likely to boost investments and consumption in the economy over the medium term.

Foreign investment inflows have started to improve on the back of a stable exchange rate, positive election outcome, gradual economic liberalization and anticipated monetary policy easing in the USA in the coming quarters. Recent relaxation of foreign direct investment (FDI) norms for single-brand retail, digital media, coal mining and contract manufacturing bodes well for further traction. The easing of ECB norms since December 2018, coupled with low US dollar rates, has led to a jump in ECB flows.

With pickup in foreign investment flows amidst a moderating trade deficit on account of lower export and import demand, volatility in the Indian rupee (INR) is likely to remain limited. However, uncertainty over oil prices and global trade tensions (that could morph into a currency war) are likely to keep the INR on a tensed turf, although we expect the INR to trade in the range of 69–73 over the course of next year. Over the longer term, increasing growth premium and inflation stability would be supportive of the currency.
“When it comes to Indian buyers of TMT companies in the USA, the ongoing trade battle between the USA and China should open up acquisition opportunities.”

REED PHILLIPS, PRESIDENT, OAKLINS
TMT still a star attraction

Despite a decline in overall deal value and volume this year, strong demand in the technology, media and telecom (TMT) sector continues, particularly for companies involved in data collection and analysis.

Following a record year in 2018 for M&A overall, and for middle-market transactions in particular, the decrease in deal activity this year is less an indication of a market slowdown and more a reaction to geopolitical tension and trade uncertainty. Buyers are being more cautious, but that doesn’t mean they aren’t buying.

In fact, middle-market deal activity in India this year has held up better than in most other regions around the world. According to financial data provider Refinitiv, during the first half of 2019 only six of 20 countries posted either a year-over-year dollar or volume increase compared to 2018. While India wasn’t one of those countries, its 4% decline in dollar amount and 13% decrease in deal volume were among the lowest of the 14 other countries. In another report about mid-market deal activity this year, global consultancy BDO wrote that “there were marked declines in North America, China and Europe: only the Middle East, India, Africa and Japan held up.”

Part of the reason for that, says Oaklins’ President Reed Phillips, is because of continued strong demand in the TMT sector. “Companies in India are still very interested in acquiring technology and marketing capabilities from the United States to deploy throughout the country as a way to grow revenue,” says Reed.

Technology ranked as the third-biggest sector for M&A deals in India during the first half of 2019, holding a 12.7% market share — an increase from 2018 and trailing only financials and energy & power in market share.

However, not all TMT companies — and, by extension, deals — are created equal. Given India’s more than 1.3 billion people, Reed says companies involved in data collection and insights are especially hot targets, as acquirers are interested in ways to gather, access, deploy and analyze data from the population to optimize the delivery of products and services. Those kinds of companies, along with digital marketing and specialized information services (i.e. financial, legal and healthcare information providers) are still commanding deal multiples of between 10 and 15 times EBITDA.

At the opposite end of the spectrum are companies considered of lower value, which is to say traditional and digital media companies. “Media companies are generally not attractive to buyers in India because most media doesn’t travel well. Buyers can’t use content developed in the USA in India and vice versa, which depresses interest,” says Reed, noting that media deals that are being negotiated are typically for just four to six times EBITDA.

While the USA still accounts for the majority of cross-border deals with Indian companies, coming in at 26.3% of all inbound deals in the first half of this year according to Refinitiv, Phillips says that in recent months he has been seeing more activity between Indian and European companies. That may be because of proximity, or more investments already in place between companies in the regions.

“Chinese buyers were aggressive bidders when they wanted to buy, but a lot of companies in China and the USA won’t buy each other because of the trade war,” says Reed. With Chinese targets off the radar and Chinese buyers sidelined for at least the near-term, US and Indian companies looking to grow, or in need of putting capital to work, could find opportunities at attractive prices.

Indeed, corporate balance sheets are flush with cash, and there are more private-equity funds with more capital in reserve than ever before. At the same time, as BDO notes, TMT remains one of the dominant industry sectors for mid-market M&A, not just for strategic buyers but also for acquirers of all types.

“TMT in India is in a hyper-growth phase. Indian companies are leveraging artificial intelligence (AI), analytics and robotics to drive the next phase of growth in Indian industry. Disruptions in business models are driving the need for M&A to acquire technology, platforms and new age applications. A young, highly aspirational and upwardly mobile demographic will continue to drive growth in content consumption. Affordable broadband and the high penetration of smart devices will further spur this growth in the coming years.”

VIKAS DAWRA, MANAGING DIRECTOR
OAKLINS, INDIA
The Indian pharmaceuticals sector is the third-largest market globally in terms of volume and the 13th largest in terms of value.¹ It has witnessed steady growth on the back of increasing export opportunities in the generic medicine space and a large domestic market, to reach revenues of US$37 billion in FY18.² With a strong network of 3,000+ companies and 10,500+ manufacturing units,² India is expected to clock up revenues of US$55 billion in FY20² to become one of the leading pharmaceuticals markets globally. Key Indian players in the sector include Sun Pharma, Cipla, Lupin, Dr. Reddy’s, Aurobindo Pharma, Zydus Cadila and Glenmark Pharmaceuticals.

India’s major role in driving better health outcomes through its world-class formulation development capabilities and its low-cost structures has catapulted the country to become the leader in the global, generic medicine space. It exports around 50% of its total pharmaceutical production to 200+ countries and accounts for 20% of the world’s generic drug exports (in terms of volume).² Major export markets (FY18) are North America (31%), Africa (19%) and the European Union (16%) (IBEF Pharmaceuticals, August 2019 Report).

INDIA PHARMACEUTICALS SECTOR: HIGHLIGHTS

- Indian players account for eight out of the top 20 global generic companies (FY18)³
- Highest US Food and Drug Administration (USFDA)-approved generic drug facilities outside the USA
- Accounted for approximately 50% of USFDA-approved generic drugs in 2018⁴
- Supplies 40% of US generic medicine demand⁵
- Supplies 25% of all medicines consumed in the UK⁶
- Supplies 60% of global antiretroviral drugs used to combat AIDS⁶
- 60,000+ generic brands in 60 therapeutic categories⁵

KEY POLICY INITIATIVES

The Indian government has been at the forefront of supporting the pharmaceuticals sector’s growth. It has undertaken various initiatives, including a reduction in approval timelines for new facilities, a proposal for single-window clearance for biosafety products and the liberalization of foreign direct investment.

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1 Pharmaceutical Industry: Analysis and Scope of Partnership between India and Germany, December 2018 by Economic & Commercial Wing – Consulate General of India, Frankfurt
2 Indian Pharmaceuticals – A formula for success, https://www.investindia.gov.in/sector/pharmaceuticals
4 ANDAs remain pillar of Indian pharma, www.nishithdesai.com, 2 January 2019
5 Indian pharmaceutical market, strong the weight of generics, www.pharmaworldmagazine.com
(FDI) norms, etc. to increase the attractiveness of the Indian market. It has also recently introduced New Drug and Clinical Trail Rules, 2019, which aims at promoting clinical research through a transparent and faster approval process. These new rules are expected to encourage local drug development and will help in getting early access to high-impact medicines for better patient care.

The Government of India, in order to boost local manufacturing, has recently slashed corporate income tax rates to historic, low levels. This is expected to provide the necessary thrust for increased investments in the local manufacturing of pharmaceuticals. The reduction can help India to enhance exports-led growth and will provide Indian players with increased ammunition to compete with global pharmaceuticals companies.

FOREIGN INVESTMENTS

Low manufacturing costs, the availability of skilled manpower, socioeconomic changes, significant domestic market opportunities and a liberalized FDI regime (100% in greenfield projects and 74% in brownfield projects under the automatic route) have translated into growing interest in the Indian market from global players. The Indian pharmaceuticals sector attracted FDI inflows of US$16.2 billion between April 2000 and June 2019 with key global players, including Mylan Laboratories, Amneal Pharmaceuticals, Abbott, Johnson & Johnson, GlaxoSmithKline, Novartis, Pfizer, Sanofi and AstraZeneca, operating in the Indian market.

Recent marquee foreign investments include (VCCEdge):

- US-based Baxter International’s acquisition of Claris Injectables for US$625 million
- China-based Shanghai Fosun Pharmaceutical Group’s acquisition of Gland Pharma for US$1,091 million
- Sweden-based Recipharm AB’s acquisition of Nitin Lifesciences for US$103 million and Kemwell Biopharma’s contract development and manufacturing organization (CDMO) business for US$205 million

Recent engagements in the cross-border space involving Oaklins’ Indian team include:

- Advising Germany-based Dr. Willmar Schwabe on its acquisition of Sanat Products, a leading manufacturer of herbal extracts and phytopharmaceutical products
- Advising a leading domestic intellectual property (IP)-driven active pharmaceutical ingredient (API) manufacturer for a full sale to global strategics and large, private-equity funds

OPPORTUNITIES IN THE INDIAN MARKET

- New manufacturing units (formulations, APIs and intermediates)—The availability of skilled labor, considerable opportunities in the domestic market and liberalized FDI and taxation regimes provide a perfectly blended opportunity to set up new manufacturing facilities.
- Contract research and manufacturing services (CRAMS)—India, through its high number of manufacturing facilities approved by various global pharmaceuticals authorities, presents a great platform for global companies to outsource manufacturing activities for affordable and quality products accepted across various geographies. The availability of laboratories and of skilled manpower, including a high density of PhD students and scientists, act as major drivers for outsourcing research and development (R&D) activities at an affordable cost. In FY18, revenue from CRAMS was estimated at approximately US$17 billion.
- Clinical trials—The recent introduction of globally competitive clinical trial rules, combined with a genetically diverse population and a skilled doctor pool, signifies the Indian market’s potential to offer the best opportunities for conducting clinical trials. The United States National Library of Medicine’s database of global clinical studies reported that India engaged in 3,618 clinical trials between March 2018 and February 2019, most of which were conducted for global players.
- IP protection—The Government of India, to provide Indian patients with better access to blockbuster life-saving drugs and encourage global majors to participate in the Indian market, has enacted patent laws that allow exclusivity in the marketing and distribution of such drugs.
GLOBAL PRESENCE

Indian companies, in their quest to achieve scale and category leadership in niche therapies, have been on a constant lookout for quality manufacturing assets as well as complex generic brands and product portfolios. These help Indian players get access to newer markets and approved manufacturing facilities, diversify into newer therapeutic categories, and allow scope for further value addition and expansion of product portfolios in existing markets and categories.

Key outbound transactions include (VCCEdge):

- Aurobindo Pharma’s acquisition of the dermatology business and generic US oral solids portfolio of Sandoz (a division of Switzerland-based Novartis) for US$900 million (the largest outbound pharmaceuticals acquisition by an Indian company) (announced but not closed)
- Lupin’s acquisition of US-based Symbiomix Therapeutics LLC for US$150 million to expand its branded women’s health specialty business
- Piramal Enterprises’ acquisition of the spasticity and pain management portfolio of UK-based Mallinckrodt Pharmaceuticals for US$203 million
- Aurobindo Pharma’s acquisition of Portugal-based Generis Farmaceutica SA for US$143 million to become the leading generics group in Portugal with the ability to service European markets with a low lead time
- Lupin’s acquisition of US-based Gavis Pharmaceuticals for US$880 million to broaden offerings in dermatology, controlled-substance products and other high-value and niche generics
- Strides’ acquisition of the generic pharmaceuticals business of South-Africa-based Aspen Pharmacare in Australia for US$300 million to become one of the top three generic pharmaceutical suppliers in Australia and among the top 10 pharmaceutical companies in the country.

CONCLUSION

The Indian pharmaceuticals sector has been a standout performer in India’s growth story. It has grown consistently, navigating through regulatory and other challenges. With increased R&D expenditure from major players and proposed new drug launches making their impact, coupled with government-sponsored healthcare schemes and a liberalized regulatory regime, the pharmaceuticals sector is expected to move towards an even higher growth trajectory.
The Indian media and entertainment (M&E) sector is a US$24 billion industry and is expected to reach US$34 billion by fiscal year 2020–2021 (FY21) (EY FICCI report, March 2019). Already a global leader in many sub-segments, the industry is on the cusp of a further strong phase of growth on the back of digitalization, high internet penetration and increasing content consumption.

**SECTOR HIGHLIGHTS**

India has the largest film industry in the world, in terms of the number of films produced and released every year (1,500 to 2,000 films). This segment shows a lot of future potential, as India is currently an under-penetrated market with limited multiplexes and low ticket prices that are showing signs of catching up to international levels.

Increased availability of data has led to content reaching Indian consumers in diverse regional markets and smaller towns. Dubbing in around four to six regional languages has helped Hollywood blockbusters like *Avengers, Mission: Impossible* and *Jurassic World* amass significant box-office returns in India. Recognizing this potential in regional markets, global streaming platforms such as Netflix and Amazon have recently focused on investing in local content and originals.

Higher uptake of high definition (HD) channels and digitization of cable services has helped India emerge as the second-largest pay-TV market after China. The massive fall in data prices in 2016 resulted in India having the cheapest mobile broadband prices in the world. This, coupled with the high video-content consumption habit in India, led to Hotstar, an Indian over-the-top (OTT) platform, having the highest number of concurrent video viewers (a staggering 25.3 million) anywhere in the world.

The print sector witnessed growth of 4.5% in FY19 to reach a size of US$4.8 billion. While advertising revenues continued to grow, circulation growth was muted due to digital adoption.

Foreign direct investment (FDI) regulations in the industry have been considerably relaxed over the past few years, especially in sectors like teleports, direct-to-home television (DTH) and cable networks.

**KEY SECTOR TRENDS**

**Consolidation on the rise:** Over the past few years, sectors like multiplex, radio and cable have witnessed consolidation. Deal value in the M&E sector more than doubled between 2017 and 2018 to reach US$2.8 billion, with about 66% of deals led by strategic investors (EY FICCI report, March 2019).

PVR Cinemas, India’s largest multiplex chain (market cap of US$1.2 billion), acquired SPI Cinemas, a leading multiplex player in South India, in a deal worth over US$90 million, while Reliance Group acquired a majority stake in two of India’s largest cable operators: Den Networks and Hathway Cable & Datacom.

The DTH business housed under Videocon d2h Limited was merged with Essel Group’s Dish TV. This transaction was one of the largest ever deals in India’s M&E sector. YES Securities acted as the lead financial advisor to Videocon Group in this deal.

Additionally, Music Broadcast Ltd. is acquiring Reliance Broadcast, which houses private FM brand Big FM. Regulatory approvals have already been sought for this deal.

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Internet penetration driving data consumption: Data usage per smartphone in the country stood at 9.8 GB per month in 2018, and this number is set to double by 2024. India has one of the highest per capita consumption rates of online video in the world. This fascination for consuming entertainment online, along with the creative freedom being offered in the digital world, has resulted in content creators and talent switching over from old media forms to OTTs.

Real-money games and e-sports models finally realizing their potential: The gaming segment has been one of the outperformers in the M&E industry. In FY19, the gaming market grew at a rate of 41.6% to reach US$886 million. While traditional casual games continue to grow, the money-spinner is real-money gaming (RMG). RMG includes games like online rummy and poker, which contributed to an upswing in average revenues per user (ARPs). A new sub-segment, e-sports, is fast emerging and has the capacity to bring further high growth to India’s gaming industry.

Large Indian businesses in tech-media space: Tech-enabled media services are gaining popularity, with companies like Prime Focus and Amagi dominating the landscape and becoming world leaders in their respective segments. Prime Focus is one of the top four visual effects (VFX) players in the world and also provides other technology products and services, such as CLEAR Media ERP Suite, and cloud-enabled media services, production and postproduction services to the M&E industry. The company has won multiple Oscar awards for its work. Another interesting company in this space is Amagi, which was among the first few players in the industry to use cloud technologies for broadcasting and targeted advertising.

INVESTMENT OPPORTUNITIES

The broadband industry offers significant potential, owing to India’s ever-rising data demand, and new avenues are opening up beyond Tier 1 and Tier 2 cities. Content creators are direct beneficiaries of this easily available data, with digital subscription growing by 250% last year, due to the rising spend on online content consumption. VFX and animation players are attractive targets because of the significant work flowing from international markets on the back of a cost-effective talent pool in India and an expanding audience on OTT platforms watching animated shows.

In an increasingly digital world, event management companies focusing on product activations have gained prominence as a crucial means of getting the look and feel of the product across to consumers, enticing them to buy products. There is also an opportunity for global players to invest in tech-enabled media service companies and consolidate their global leadership position.

The percolation of international and regional movies into the overall stream of movie-watching entertainment leaves no doubt about the multiplex segment’s strong future outlook. This is one sector that is bound to see increased investment in the coming years.

The past few years have seen an increasing craze and fan-following of Indian sports leagues, such as the Indian Premier League (IPL) and Pro Kabaddi, as well as of international sports leagues like the English Premier League and events such as Wimbledon. There is a potential to monetize this fan-following to create a gaming powerhouse. Eventually, such companies could also move to include e-sports-based gaming under their belts, a model that is widely tipped to drive the next phase of this sector’s growth in India.

India’s family entertainment is limited to malls and theme parks, which attempt to house all sorts of entertainment and leisure facilities. However, the concept of entertainment centers and holistic entertainment destinations is a largely untapped market in India, leaving ample potential for investors to earn good returns. Players in the M&E space are now transcending boundaries and expanding outside India. While content creators are looking to acquire studios with strong IP in foreign countries, one of the biggest multiplex chains in India is actively looking at acquisitions in the Middle East and North Africa (MENA) region.

Overall, the Indian M&E industry offers significant investment opportunities for both financial and strategic players, with several sub-segments poised for exponential growth in the near future.

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Can you provide an overview of the logistics sector in India? What in your opinion are the key emerging trends in this sector? How have recent regulatory and taxation changes impacted the logistics sector?

Firstly, most of the consumer companies in our unorganized logistics sector use carrying and forwarding (C&F) agents to manage their logistics. C&F, in my opinion, will be history in five years’ time. The few C&Fs that have the ability to scale up to serve modern supply systems and practices would convert to third-party logistics (3PL) companies, and the rest will turn obsolete. Secondly, a lot of companies used to manage their own logistics in the past. Since that space will be taken up by modern 3PL companies in India, a lot of companies that used to carry out their logistics and supply chain management in-house will start outsourcing more, and this new outsourcing will propel the sector.

Thirdly, the entire sector has also been unorganized on the transportation side, and it will witness the presence of organized logistics players in the future. Globally, all organized 3PL players are either in transportation or in warehousing, and 95% of logistics are organized in the developed countries. In India, 90% of logistics are in the unorganized sector. So, that’s the runway available for the organized logistics space in India, and you needed a trigger like goods and services tax (GST) to actually propel it — and that’s exactly what is happening. So what will happen now is that you’ll need a lot of good-quality infrastructure to support this change, which the introduction of GST is helping to bring about. GST is the single biggest trigger for the largest impetus to the logistics sector. And why is that? Because the need for organized logistics is largely driven by the consumer sector. Commodities are still in the low-cost, efficient logistics system that has been developed over the last few decades, and they continue that way. However, the consumer sector is the one that really needs an organized supply chain. The creation of GST has driven supply chain modeling by companies to move from the tax-based supply chain of the past to the present and the future of inventory and speed-based supply chains. Now, that’s a big change for the country. In fact, the GST is the biggest game changer for the supply chain sector and for the consumer sector. Earlier, based on tax-based planning, each manufacturer, brand or company had to set up storage points in all 32 states of the country. That led to a fragmentation of inventory, inefficiencies in the inventory, a lot of markdowns and obsolescence, and disorder in logistics management. But, it was very tax-efficient. With GST we have one nation, one tax. So the need for 32 stock points for higher inventories for savings on tax no longer exists. Today’s GST sector allows you to service the entire country from one location, and the tax impact will be the same. So depending on the product category, the manufacturer size and the penetration of the consumer market, now companies can decide to have only one stock point in the country, or four stock points, or nine stock points or more as per necessity. No one needs 32 stock points any more to service the country based on tax needs. And this has been the single biggest game changer.

What are the investment opportunities you see in organized logistics space over the next few years? In your opinion how much capital is required over the next few year in this sector?

On the infrastructure side, good-quality warehouses will be the need of the hour. If you look at the multinational companies in the 3PL space, or even the Indian companies, the largest spaces around are seven or eight million square feet each. So the total organized sector would be less than 50 million square feet, while there are 900 million square feet of warehousing space in the country. So that’s the gap between organized and unorganized. In the next five years, at least 150 to 200 million
square feet of organized logistics space will be required. Now, 150 to 200 million square feet of organized logistics space requires a lot of money. If you do some simple math, the land plus building costs will range anywhere between 1,500 to 2,000 rupees (US$21 to US$28) per square foot. So a million square feet would require 2,000 million rupees (US$28 million).

If you look at Stellar, we ourselves are planning to build 35 logistics parks on 50 million square feet in 21 cities. So in Stellar, I am planning to get 100 billion rupees (US$1.4 billion) of investment for just the warehousing infrastructure. If I connect these 21 logistic parks with each other across the country to serve the consumer market, Stellar will require around 50,000 trucks, which is an investment of another 100 billion rupees (US$1.4 billion). In addition to that, we will need to put infrastructure such as shelving, racking, material handling equipment, conveyors and sorters inside the warehouses, which will require another investment of 50 billion rupees (US$0.7 billion). These are not all going to be on my books, except the capex inside the warehouses. I am going to get partners to invest in build-to-suit buildings, and transporters to come in as partners with me on a lease basis. I am going to have 10,000 trucks and 50 million square feet of warehousing infrastructure built for Stellar, which will require 250 billion rupees (US$3.5 billion). If a US$4 billion investment is required in only one company, you can say that a US$40 billion to US$50 billion investment will be required in the country in the next three to four years to build the infrastructure just for the consumer sector. Investments over the last few years have been in the range of US$2 billion to US$4 billion in total. The country will require more than 10 times that in the next four years, and that’s why most investors recognize this is an extremely interesting sector to invest their money in.

The challenge is that not many companies in the country are in this space. So this will lead to some foreign companies coming to India, which will lead to the emergence of new entrepreneurs and people like me setting up big companies. The investments that have come into the country so far have been in companies like mine and also companies in the e-commerce space. In fact, e-commerce has been the sector that has driven the most investments, because two of the largest e-commerce players in the world originated in this country. Those investments are also a necessary part of setting up this new business model, because it has not yet reached a profitable scale and is still going through the growth and stabilization phases. It’s a model that will need to be perfected over a period of time. The classic bricks-and-mortar supply chain model used in the consumer space, however, is well established in the country.

The fact remains that there are no companies of scale, so people, entrepreneurs or companies that can think at scale — Stellar being one of them — can actually attract a lot of investments in infrastructure, transportation, technology, automation and talent, which will yield very handsome returns over the next few years. This sector has lagged behind in the economic growth of India but it is now catching up, and catching up big time. It will see phenomenal growth over the next decade and super phenomenal growth over the next five years.

Companies that make the right investment in the right people, the right talent and the right companies over the next five years are going to reap generous returns.

*Conversion rate of 1 USD = 71 INR has been used*
What are your views on the investor interest and investment opportunities in the retail sector in India?

Immense future growth opportunities are driving the investor interest in this sector. Firstly, India’s economy is currently close to US$2.3 trillion, and consumption is over US$850 billion. Even in a conservative case, if the gross domestic product (GDP) grows by 6% on average, that means an additional US$50 billion in consumption every year. Secondly, there is a structural shift happening towards the ever-more-organized retail sector. The current, large, growing addressable market is attracting a lot of foreign investment into the country. It’s a long-haul game. Restrictions exist around solicitation of foreign capital in the retail sector. But there are specific pockets where there can be 100% ownership by foreign investors — for example, in single-brand retail or e-commerce platforms. I believe the vast nature of the market and the expected growth ahead are the driving factors for investment.

What are the unique challenges faced by a retail operator in a vast and diversified market such as India? How has Future Group innovated to emerge as a winner in this challenging market? What is likely to be your future course of action to sustain growth and enhance customer base?

I believe getting your back end and the entire logistic supply chain from farm to fork is key towards successfully running a retail chain in India. At Future Group, we have a presence across almost every state. You put a finger on the map in terms of where the consumption is happening, and we have a store there. In India, every 500-700 km, you find a different culture and different cuisine, and unique preferences. Customizing your product range to cater to these diverse consumption patterns is the key driver for success, in my view. After the effort put in over the last 30 years, the product range in our stores really reflects that local consumption pattern. And now as we try to cater to 1.3 billion Indians who have local consumption patterns every 600 km, it helps that you have a vast supply chain in place. For our high-end stores in big cities, typically one would have 80,000 to 100,000 stock keeping units (SKUs), whereas at our smaller stores the SKUs will be much larger. You are also then handling the complexity. On one hand you have a geographical spread, on the other hand you have the complexity of handling the SKUs. So I guess we have been continuously investing in building our product and supply chain capabilities. We now have close to 500 million annual customer footfalls, nearly 150 million unique footfalls, and close to 45 million active customers on various loyalty programs. So we have to make a relative choice about whether we should start focusing on increasing footfalls or whether we believe there is enough footfall and, through better engagement via data, loyalty programs, etc., we can aim at a larger share of the customer’s wallet. Can we provide a more customized service to the customer and therefore get a larger share of the revenue? So data and supply chain are key driving factors as far as our trajectory ahead is concerned.
Future Group has successfully completed several M&A transactions. What have been the key drivers to pursue this inorganic strategy?

Firstly, retail is a business where size and scale is very important — this has driven consolidation in the Indian retail sector over the last few years. In this sector, there is a back-end cost to doing business. Unless you can amortize this cost over a larger base, getting the desired amount of returns is a difficult task. These consolidation opportunities helped Future Group come closer to that objective. Secondly, as I said, it’s one economy, one country, but at the same time there is huge diversity. So in order to meet our twin objectives of achieving larger scale to improve cost-efficiencies and get better foothold in local markets, we acquired/merged some regional players who have built successful regional businesses. I think we have been pretty active and made the most of the attractive consolidation opportunities in this sector. I guess right now and for the foreseeable future, the focus will be to get the best out of the organizations we have merged with or acquired.

But equally importantly, you have also been raising equity capital from marquee investors during your growth life-cycle. How have you been able to attract marquee investors and do you believe there are significant investment opportunities in the future not only for Future Group but also across the entire Indian retail value chain?

As I said, it is a US$800 billion to US$850 billion market, increasing by US$50 billion every year. There is a structural shift happening from unorganized to organized, so there is a tremendous opportunity in hand and ahead of us. If these opportunities are available, and if you are an investor who comes across a credible operator who is very well placed to make the most of these opportunities, I think that is where the successful deals happen. We have spent the last 30 years making the most of this scenario. Slowly and gradually, the restrictions around multibrand retailers have been easing off. For example, any foreign portfolio investment (FPI) can go up to 9.99% in multibrand, in single-brand it can be up to 100% ownership. At our end, as a group, we maintain an active interface with the investors, and that is resulting in some attractive investments coming our way.

I don’t think any conversation about retail would be complete without some discussion of online versus bricks and mortar. In India, we see that the opportunity is so huge that both can coexist. But are you seeing some pressure on the modern retail format from the e-commerce online players, or do you think there is still some leeway for both to coexist and grow?

We should probably reassess the word “versus.” It is no longer online versus offline. Twenty years back, a lot of mindshare was with modern retail. Everybody felt that the days of Kirana (mom and pop) stores were gone and the era of modern retail had begun. But look where we are 20 years down the line. Modern retail growth is somewhere around 10%. In the last few years we have seen the mindshare growing for online entities. The realization is that online and offline are going to work together. Physical retail has built a strong on-the-ground presence. In various categories the customer wants to touch and feel the products. But, let’s acknowledge the fact the online is here to stay and grow. If online channels generate some interesting leads and through the physical store layout those leads can be fulfilled at an optimum cost, then it’s an excellent combination. If at all, these partnerships should lead to more and more throughput for the physical retailers. As I said, at every single store of ours, every 600 km, the assortment reflects the consumption. So if integration with e-commerce allows the lead to get passed on to that store, then the assortment is nothing but the inventory. For me as a physical retailer, it’s an additional channel leading to sales. My entire gross margin goes to my EBITDA margin. For the online retailer, the cost of delivery can probably be the lowest. In some of the global acquisitions, in places such as North America (the upcoming market of e-commerce), the touchpoint with the customer is very important. But at the same time, as a physical retailer I believe e-commerce is here to stay and grow. So let’s work together. For me, it’s not versus e-commerce anymore, it’s with.
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