# Some way to go before the finish

## Implementation of policy is key to the success of private players in the rail freight arena

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The Railway Ministry's plans to allow private companies to run freight trains from their own private terminals may lead to faster evacuation of cargo, but the proposed move faces multiple challenges, said analysts.

"The move may be widely seen as ushering of fundamental reforms in the stodgy behemoth but past experience does not exactly paint a positive picture," said Rohit Chaturvedi, managing partner Kitzo Management Advisory, a logistics strategy and operations consulting firm.

**Poor past experience**

"Even less ambitious initiatives like allowing Private Container Terminal Operators (CTOs), Multi Modal Logistics Parks or most recently Private Freight Terminals (PFTs) have not met with desired success," said Mr. Chaturvedi, formerly director of Crisil Risk & Infrastructure Advisory. "To be fair, PFT has shown a glimpse of railways' readiness to take necessary steps in the right direction, but not sufficiently," he added.

As per plan, firms and manufacturers that transport bulk of their produce through the railway network would be allowed to set up their own private terminals from where their own trains would ply to delivery centres. The trains will run on Indian Railways' tracks and the operation of the trains will remain with the railways. This is per the provisions of the Special Freight Train Operations Scheme of the Ministry of Railways.

However, the problems being faced by Indian Railways such as creaky signalling infrastructure and tracks needing maintenance will largely remain the same. The problem is compounded on congested routes such as between Delhi and Mumbai, which already face pressure from both passenger and freight trains, analysts said.

"This is a good initiative and can help players with bulk movements such as coal, sugar, cement and fertilizers for faster movement of their cargo," said Ganesh Rewanwar, director & CEO, Saanvad Ventures Pvt. Ltd. which runs freightbazaar, an e-transportation market-place catering to the trucking industry. "It will also help in multi modal infrastructure development and speed up investment in infrastructure," he added.

**Slow movement:** The impact of the move may not be immediate since it would require more time to build infrastructure. Land acquisition and terminal utilisation are said to be the major challenges. ▪GETTY IMAGES/ISTOCK

He said the impact may not be immediate since it would require more time to build up infrastructure. "The major challenge will be land acquisition and terminal utilisation. It is not expected to affect long-haul road transport in a major way. However, it will be a boost for the first-mile and last-mile logistics sector," he said.

The Railways, under Minister Suresh Prabhu, may be undergoing transformation, but scepticism persists.

"The move is seen [as] positive for large corporates with heavy volume of cargo as freight movement by railway is suitable for long distance over 500 kms," said Kamal Podar, managing director, Choice Group which is into financial services and management consulting in the infrastructure space.

"However, so far we have seen limited success in private container train operations since it was introduced in 2006, due to lack of conducive policies," he added. "The railway traffic is caught between subsidised passenger traffic and premium tariff for cargo which is benefiting other modes of traffic like road and shipping," he added.

Besides, the precedence given to passenger trains is expected to cause uncertainties in running freight trains in a scheduled manner. This may defeat the very purpose behind the partial opening up of the freight transport arm of the railways. Apart from the convenience of transporting cargo through own trains, the economic viability of any such operation would remain a major question for private operators.

Going by past experience, most Container Terminal Operators have either burnt their fingers or not started operations in a meaningful manner. In fact, there have been instances of licence-holders operating only a few rakes merely to prevent their licences from being revoked.

**Charges, changes**

Analysts said the main cause of unprofitable operations may be attributed to the charges by Railways and ad-hoc changes in tariffs for some of the profitable cargo (heavy cargo and long distance haulage). Also lack of guarantee of timely delivery of the consignment has repulsed the EXIM cargo, they added. For example, the railways command less than one third of total container volumes at JNPT, the largest container port in India located in Mumbai. JNPT attracts most of the cargo from long distances from the North and West of India. This situation is unheard of in any other country with advanced logistics systems, industry watchers said. Long distances must mean competitive advantages to railways over road.

Analysts believe that the problems such as heavy detention charges, fixed haulage charges, whether the rake is full or empty, coupled with the lack of certainty on timely movement of rakes would affect the private rail operators in the same way as they affected the Container Terminal Operators.

Another concern that bogs potential private operators is the lack of clarity on whether they would be allowed to run their rakes on the proposed Dedicated Freight Corridors (DFCs) being set up in the country.

In addition, there is lack of clarity on the approval process for rakes and the design specifications. As per existing rules, the approval has to come from the Research Designs & Standards Organisation (RDSO) of the Railways is required for running any non-standard rake. It is feared that the approval process could take a long time and bureaucratic hassles would jeopardise the genuine intent, said industry sources.

The absence of a credible dispute resolution mechanism has also been red flagged by analysts. The Railways, being both the operator and regulator, meant that the dispute resolution system in place may not be adequately effective, they said. However, it is expected that the proposed Rail Development Authority may address the issues of effective and efficient regulation as well as dispute resolution.

Finally, although the intent to allow private operators to run their own rakes is laudable, ambitious and bold, it has to be backed by proper implementation mechanism, according to consultants.

"If implemented properly, it can begin the virtuous circle by freeing up the resources of Indian Railways and providing focus on basic infrastructure such as modern signalling equipments and robust rail network," Mr. Chaturvedi said. "The result will be more capacity augmentation from existing infrastructure and more cargo movement… [and] thus more resources for the railways," he added.

# Are the stock markets too hot to handle?

AARATI KRISHNAN
CHENNAI

Now that the S&P BSE Sensex has breached 30,000 and is at a new life high, is the stock market too hot to handle? Or is it just warming up to create new records?

To gauge this, it is best to look at the valuation multiple at which the index trades, rather than the absolute index level. As per BSE data, the Sensex currently trades at a price-earnings (PE) multiple of 22.5. That is, investors are currently paying ₹22.5 by way of stock price for every rupee of profits earned by the Sensex companies in the last 12 months. Views are still sharply divided on whether 22.5 is a pricey valuation or a reasonable one.

**The bull case**

Bullish brokers and fund managers assure us that a Sensex PE of 22.5 isn't cause for alarm. For one, they argue, big market reversals in the past have unfolded at a much higher multiple. In February 2000, the Sensex PE was 24.3 before the dot-com bubble burst. In December 2007, it hovered at about 27 before the global credit crisis precipitated a meltdown.

Two, the current PE appears high because the denominator — earnings — is unusually depressed. Profits for Sensex firms have increased at just 5.4% annually in the six years from FY11 to FY17. Once earnings growth reverts to 15% or so, they reckon, the PE will collapse.

As stock prices are all about expectations, they point out, the forward PE multiple (the price per rupee of next year's earnings) is the must-watch indicator, rather than the historical one. So, assuming that Sensex firms expand their profits at 16-17 % for FY18, the Sensex forward PE is 17.8 times. That's in line with the 20-year average of 18 times.

The other argument is that even if the PE is elevated, other valuation indicators such as market cap-to-GDP and Price-to-Book Value (P/BV) suggest a moderately-valued market.

Of course, the clinching argument is the flood of liquidity, both from foreign and domestic investors, that is chasing the 'India story' and propelling stock prices higher.

The bears, however, have credible counter-arguments to all this. For starters, even if the PE of 22.5 has room to expand before the inevitable correction, the downside to markets from here would be higher than the upside. And who can catch the exact tipping point? It is true that Sensex earnings growth has been unusually depressed in the last six years. But what's the guarantee that it will normalise this year? For the last three years, brokerages and analysts have optimistically 'modelled' Sensex profit growth of 15-20%, only to sheepishly downgrade their estimates by the year-end and roll them forward.

In April 2015, analyst estimates for Sensex earnings for the year were at more than ₹1,750 - a 20% growth over the previous year. Actual earnings for the year stood at just ₹1,385. Undaunted, in April 2016 they again projected a 20% expansion to ₹1,670 for FY17. But the results for the first nine months suggest that the number may just top ₹1,430.

While the first half of FY17 was a damp squib, December quarter numbers have offered hope that growth for corporate India is finally shifting to a higher gear. But the past record of analysts in predicting earnings still injects a healthy dose of doubt into their estimates of ₹1,685 to ₹1,700 for FY18.

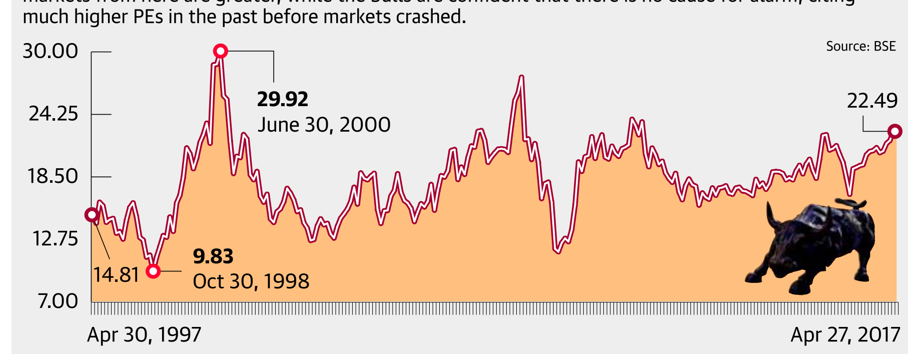
As to other indicators such as P/BV or liquidity, that's akin to shifting the goalposts in the middle of the game. Bearish folk remind us that in the long term, stock prices are slaves to earnings growth. So if corporate India fails to deliver on that much-awaited profit rebound, why would foreign and domestic investors continue to sink in new money?

So, with both camps sticking to their guns, what should a lay investor do? Well, panicking and exiting all your equity investments can lead to missed opportunities. Who knows if that earnings rebound is just around the corner?

But making out-sized bets on equities because you are bedazzled by recent gains is equally fraught. Phasing out your investment through vehicles such as Systematic Investment Plans seems to be the best bet. Sticking to diversified funds and large-cap stocks may be safer than playing sectors or small businesses. And as long there's a bear camp in the market that is warning of over-heating, you can rest assured that we're not in bubble territory. It's when the last bear switches camp that the real bear market will begin.

**The P/E story**

Views are divided on whether price-to-earnings is high at 22.5. The bears ask if the downsides to markets from here are greater, while the bulls are confident that there is no cause for alarm, citing much higher PEs in the past before markets crashed.




EXPLAINER

# What you need to know about Infrastructure Investment Trusts

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CHENNAI

The initial public offering (IPO) for IRB InvIT, India's first infrastructure investment trust fund will open for subscription on May 3 and close on May 5. Sponsored by road developer IRB Infrastructure Developers Ltd., the trust aims to raise up to ₹4,035 crore. Reliance Infrastructure, Sterlite Power Grid Ventures and other infrastructure firms are also gearing up to unveil InvITs.

**What are InvITs?**

■ InvITs are similar to mutual funds. While mutual funds provide an opportunity to invest in equity stocks, an InvIT allows one to invest in infrastructure projects such as road and power.

**How do InvITs work?**

■ InvITs raise funds from a large number of investors and directly invest in infrastructure projects or through a special purpose vehicle. Two types of InvITs have been allowed: one, which invests in completed and revenue generation infrastructure projects; the other, which has the flexibility to invest in completed or under-construction projects. InvITs which invest in completed projects take the route of public offer of its units, while those investing in under construction projects take the route of private placement of units. Both forms are required to be listed on stock exchanges.

**How do InvITs help the developer?**

■ InvITs allow developers of infrastructure assets to monetise their assets by pooling multiple projects under a single entity (trust structure). For instance, IRB InvIT constitutes six special purpose vehicles consisting of toll-road assets aggregating to 3,645 lane kilometres of highways located across the states of Maharashtra, Gujarat, Rajasthan, Karnataka and Tamil Nadu. Infrastructure projects suffer from lack of availability of long-term capital and have depended on bank finance which typically has a short tenure. InvITs are designed to attract low-cost, long term capital and the underlying focus is to reduce the funding pressure on the banking system as well as generating fresh equity capital for infrastructure projects.

**What is the structure of InvITs?**

■ InvITs are registered as trusts with SEBI and there are four parties — trustee, sponsors, investment manager and project manager. In the case of IRB InvIT, IRB Infrastructure Developers Ltd. is the sponsor, IDBI Trusteeship Services Ltd. is the trustee, IRB Infrastructure Pvt. Ltd. is the investment manager and the project manager is Modern Road Makers Pvt. Ltd.

**What is each party's role?**

■ Sponsors are the firms which set up the InvITs. Investment managers manage assets and investments of InvITs and undertake activities of the InvIT. The project manager is responsible for executing the projects. The trustee oversees the role of InvIT, investment managers and project manager and ensures that all rules are complied with.

**For which class of investors are InvITs suitable?**

■ As per present regulations, InvIT investments are not open for small and retail investors. The minimum application size for InvIT units is ₹10 lakh. The main investors could be foreign institutional investors, insurance and pension funds and domestic institutional investors (like mutual funds, banks) and also super-rich individuals.

**What do InvITs mean to investors?**

■ According to SEBI rules, at least 90% of funds collected, after paying for expenses, taxes and repayment of external debt, should be passed on to investors every six months. IRB InvIT is expected to pay about 12% as returns to investors. Dividend income received by unit holders is tax exempt. Short-term capital gain on sale of units is taxed at 15%, while long-term capital gains are tax exempt. Interest distributed to unit holders is taxed.

**What are the potential investment risks?**

■ InvITs are listed on and are subjected to the vagaries of the stock exchanges, resulting in negative or lower returns than expected. An economic downturn or project delays may hit infrastructure projects and result in lower returns. As in mutual funds, investors in InvITs have no control over investments and exits being made by the trust.

# 'Hire locally' is the new mantra for IT

## As protectionism hits firms, Indian staff going abroad in large numbers may no more be the norm

PRADEESH CHANDRAN
BENGALURU

Indian IT services is traversing a tough period. The business, which had witnessed turmoil primarily fuelled by macroeconomic conditions, is now facing challenges such as protectionist policies and shifts in technology, besides sector-specific hurdles.

First in a slew of protectionist measures was the proposed overhaul of the H-1B visa by the Donald Trump administration. H-1B is the short-term visa used by Indian IT companies to send employees to work in a client's location in the U.S.

The U.S. President has signed an executive order for an overhaul of the visa system. Senator Zoe Lofgren had tabled a bill that was aimed at raising the minimum salary of an H-1B worker to $130,000 from $60,000.

"Although… refining the proposed measures into real executed actions will take time, any drastic change to visa administration, regulation, or legislation that aims to restrict free movement of resources to where they are most needed will bring harm to almost all U.S. verticals, especially IT and IT services," said Hansa Iyengar, senior analyst, large enterprise services, Ovum in a research report.


**Raising walls:** The anti-outsourcing sentiment in the U.S. was primarily due to a notion that Indian IT firms are violating visa regulations and taking away jobs from locals. ▪GETTY IMAGES/ISTOCK

The anti-outsourcing sentiment in the U.S. was primarily due to a notion that Indian IT firms are violating visa regulations and taking away jobs from locals. The rise in unemployment after the 2008 financial crisis also acted as a catalyst in the U.S. for the anti-outsourcing campaign get louder. This has also engendered a string of lawsuits against Indian IT services majors in the U.S. for alleged visa violations.

In 2013, Infosys had paid $34 million after a federal investigation found visa misuse by the company. In 2015, there was a separate investigation by the U.S. agencies against TCS and Infosys for visa violation in an outsourcing contract involving utility firm Southern California Edison in which both firms were freed of charges.

North America contributes to about 60% of the total revenue of Indian IT companies.

"Global delivery models are deeply embedded in almost every business globally and it is impossible to suddenly 'get rid' of outsourcing," wrote Ms. Iyengar. "Any changes that do occur… will be for curbing the abuse of the visa norms that is rampantly done by body-shopping companies."

According to the U.S. Citizenship and Immigration Services, H-1B applications for 2017 fell below 2,00,000 for the first time in five years. It received 1,99,000 applications in 2017 compared with 2,36,000 in 2016. About 85,000 visas are granted annually in a lottery system.

**U.K. follows suit**

Another major market for Indian IT, the U.K., too decided to impose restrictions on work visas. The U.K. government scrapped the Tier-2 short-term visa category used by Indian IT companies to send software engineers to work on projects there. According to Nasscom, the industry's apex body, there are about 30,000 Indians in the U.K. in that visa category.

Other countries like Singapore and Australia are also imposing visa regulations. Australian Prime Minister Malcolm Turnbull announced the scrapping of the Australian 457 visa programme that allowed Australian companies to hire Indians in skilled jobs.

"While India continues to consolidate its position as the global hub for IT-BPM services, due to several factors, there is a concern on the future growth opportunities in the industry," said Sangeeta Gupta, senior vice president, Nasscom. "We believe that these uncertainties are bottoming out," she said.

The IT industry body has raised questions about the regulations and said that the long-term view for the industry is bullish and that the industry is on track to meet the targets it has set for itself for 2025. The industry body, along with member companies, has been working with government stakeholders from India and the U.S. to raise the issues on the right political platforms. As per Nasscom, only 6 firms of the top 20 H-1B recipients were Indian. The Indian government too has raised the issue with the U.S. administration.

Many companies have also starting putting in pace measures to even out the pains anticipated due to visa curbs.

For example, companies are ramping up local hiring in the U.S. to help mitigate risk arising from regulations.

The country's second-largest IT services company Infosys said it continued to invest in the local communities including hiring local American top talent, bringing education and training to shrink the skills gap in the U.S.

Its rival Wipro also said it is planning to increase local hiring in the U.S. and intends to have 50% of its employees in the U.S. as locals by Q1 FY18.

Meanwhile, TCS has decided to rely on more less visa-dependent business model.Talking about the challenging visa regime in U.S., U.K. and Australia, TCS HR head Ajoy Mukherjee said, "…[given] the kind of work we do and the kind of demand, talent is not available and it's a fact. So, we are educating people there to create the skillset. The work will move from place to place. The fact is that we have to hire locally to move away from the visa-dependent business model."

When asked if the industry failed to lobby against U.S. visa cuts, C.P. Gurnani, CEO, Tech Mahindra said, "I don't think it's fair to say that. Whatever you see here are Mr. Trump's election promises. Who do you lobby [with]? Nasscom is very active in this area."

Tech Mahindra is planning to hire more locals. "About 30% of our workforce in U.S. or in Australia are local citizens. If the skills are available, the first choice is local. The cost is less if we hire locally. It's not that Indian engineers are fighting to go there. Half the time we have to persuade them," he said.

*(With inputs from Piyush Pandey)*