INTERVIEW|SOUMITRA DUTTA

‘China seen as more innovative in IT than India’

Asian rival doesn’t have a TCS, but it has a Tencent and Alibaba which are more dominant and valuable in the future

VIKAS DHOOT

A 7% growth rate is not good enough for India and its IT industry has missed the bus on innovation by sticking to a template that worked 25 years ago, believes economist Soumitra Dutta who co-authors the World Economic Forum’s annual Global Information Technology report. Layoffs and adjustments, to tumult in its largest market –the U.S. – are transient factors and the real worry is that China is seen as more innovative now than India in the IT space, said Mr. Dutta, who is the Dean, Cornell SC Johnson College of Business. Edited excerpts:

Are Indian student applications falling in U.S. universities under the Donald Trump administration?

■ Generally, foreign student applications are down this year. This is across the U.S. due to uncertainty about the visa and work situation after studies. Canada is being very aggressive to bring in foreign students and it’s also a very attractive country to go to.

In the short-term, some negative impact is happening. But more worrying is the potential cuts the Donald Trump administration is making in research areas, because as grants go down, it affects output. And that’s the part that really worries me in the university much more.

There is also a concern about the environment on campuses as people are much more divided in terms of political views, but I am more concerned about the possible loss of R&D funding with many key research programmes losing out.

A lot of the funding for climate change will disappear. If you remove the intellectual horsepower that feeds the universities, that hurts more than losing student applications.

What are your views on the Indian IT industry’s current woes?

■ I think the traditional Indian IT players will have to restructure their business model and hire more people in the U.S. The costs will go up, so they will have to think about what that means for the employee balance across countries and the cost structures. That will of course, have a short-term effect on margins and they will have to look for new markets.

A bigger issue that I see with the Indian IT sector is it was very innovative 25 years ago. There hasn’t really been another big innovation in the IT sector. They have been following the same template for too long. As a result, you don’t have an Indian Microsoft or an Indian Alibaba. And that’s the problem.

The product investment is not there, nor is the consumer Internet boom. So in some sense, the Indian IT industry hasn’t innovated in the last 15 years enough.

China doesn’t have a TCS, but it has a Tencent and Alibaba which are more dominant and valuable in the future. China has succeeded in skipping a generation altogether and they got leadership in the next generation. Today, if you ask the question is China more innovative in the IT industry than India, people would probably say yes. The answer wouldn’t have been the same 15 years ago. So India has lost the leadership of the IT industry in many ways.

So do you see the current spate of layoffs in the sector as an outcome of redundant skill sets?

■ The Indian IT sector layoffs are, in my view, just a temporary balancing of the workforce. All companies go through this... The basic model of the IT industry is still stable and there’s enough business. They might have lower margins and lesser people. They are not going to go out of business, they will adjust a bit. There will be healthy companies like TCS and Wipro. But they are not going to be the next generation companies and they will never be. TCS, Infosys or Wipro will never be the next Alibaba. And that’s a problem.

The next generation of IT companies are coming from the U.S. and China, not India. If you look at the market capitalisation of top 10 tech companies in the world, Alibaba and Tencent are No. 9 and No. 10. And the top five are big U.S. companies.

So India, despite having all the lead in IT, doesn’t have an entry in that. That is not an easy problem to fix. Because you miss a generation, it takes 15 years to catch up.

Any attempt for India to make a bid for that will require us to think about what’s the next big leap and be able to make that generational leap. Because 20 years ago, there was no vision of Alibaba or Tencent. But some people in China made that leap and got lucky.

We need someone out here to think about what will happen 15 years from now. That is a big question mark. Because what we have right now in India is essentially copies of American businesses like Amazon or eBay. There’s no real innovation happening in the Internet space.

What’s your view on India’s growth slipping to 6.1% in the last quarter of 2016-17?

■ The slight dip is not what worries me. What worries me is the overall number. I think 6% or 7% growth is not enough for India. Any country that has become an emerging global power needs to have 10-20 years of 10% growth. We are nowhere near that.

> Indian IT industry hasn’t innovated in the last 15 years enough

Brazil at some point had 10% growth for 15 years. China had it for 20 years. India’s never actually had that. What worries me is will we actually hit 8%, 9% or 10% and will we be able to sustain it over 10 or 15 years. I am keeping my fingers crossed that the government’s focus on building institutions will lead to long-term results.

So I am not too concerned with the short-term dip which might be because of demonetisation and whatever other reasons. I am more concerned about can we move from 7% to 9%. Because at 6% or 7%, you are not really making a dent on the poverty reduction front, at least not fast enough. If you want to make it fast enough, we need to move at a different pace. We shouldn’t forget that India’s economy is still quite small with a very low per capita income.

The U.S. economy is roughly 16-17 trillion dollars, China is about 10-11 trillion dollars, India is around two [trillion]. And India’s nominal GDP per capita is still very low.

From a foreign investors’ lens, if a government with such a majority cannot address the tough structural reforms such as in factor markets like land and labour, is there a concern that India’s potential will remain untapped?

■ Now what the Prime Minister has really done is consolidated the BJP’s power at both the national and State level. In many ways, that was an important foundation to be laid. Hopefully, that will lead to faster and more effective action going forward. I think people and business like stability more than anything else. Emerging markets have a problem as they usually don’t have stability. That’s what people hate about emerging markets. So the fact that the same party now controls the Centre and a large part of the States gives a sense of stability to the foreign investor and businesses. That is important as once you have confidence and stability, people take the right decisions or at least are more encouraged to take the hard decisions.

Would now be a good time to take up land acquisition reforms, for instance?

■ I think so. There will always be some changes that are hard to do because of politics and democratic systems. There’s always a cost of change. But I think if we can still do a lot to simplify things and focus on health, education and infrastructure, it will help. There’s a lot of low-hanging fruit in India. It’s good to have analysis and new ideas, but I think the problem in India is less about ideas and more with execution. I do believe that government’s focus on stability and a sense of calmness and focused discipline on execution is critical. It’s very hard to govern a large and diverse country like India. It’s a significant achievement just to provide a sense of stability, direction and some positive confidence.

How do you see business education evolving? Will we see more consilience being weaved into what are traditionally learnt at B-schools?

■ I am also the chair of the AACSB, the global body for business schools’ accreditation. We went through a vision exercise recently and two themes came out strongly. The future would be about making connections between disciplines like engineering and business, health and business and so on and secondly, the connection with industry. The second theme was disruption. There was a strong feeling that the way we have done business education in the past will not be the same going forward.

We will have to rethink business education for the future. There’s no clear model but the field is ready for disruption and you can see that already with the traditional MBA market stagnating to some degree. We see some of the weaker players dropping out, some schools are stopping their MBA programmes.

There’s a feeling that what got us here will not get us through the next 50 years.

GUEST COLUMN

Drop anchor at a better port

Stay nimble: Investors must remain anchored to fundamentals underlying the stock rather than the price . •REUTERS

ANAND SRINIVASAN

You stand in a queue in a supermarket to pay your bills, if another stranger tries to jump the line you are bound to get upset. This is because you believe you own the place in the line. This belief is called anchoring in behavioural economics.

When we buy a stock at a certain price, the investor gets anchored to the price at which he has bought the stock. All the future decisions of the retail investor get anchored to the price. Under the normal practice of the investor, if the price drops significantly he or she will not sell the stock and switch to a more profitable investment. They wait for years for the stock to return to its original price before selling the stock.

The investor would have been better of selling the stock for a loss and investing the same when in a different stock or asset class.

Let us take the example of one of India’s most respected companies Tata Steel. The stock traded at ₹939 in January 2008. The company had acquired Corus by leveraging its balance sheet and borrowing several billion dollars.

2008 crisis

In 2008, when the world financial markets collapsed, the price of Tata Steel plummeted to ₹166.50. If the investor instead of staying anchored to his position in Tata Steel had sold the stock and booked a loss of ₹773 and switched his funds to JSW Steel, a company in the same sector the stock adjusted for a split would have been available for ₹22.16. An investor could have bought eight shares. The stock is currently trading at ₹194, while Tata Steel is trading at ₹492. The investor who stayed anchored with Tata Steel would have lost ₹447 till date. A person who made the switch to JSW Steel would have seen his investment grow to ₹1,552. He would have made a profit of ₹613 on his initial investment of ₹939.

> Markets are fluid and fundamentals can change dramatically

This calculation discounts the dividend earned in both stocks. The result would have been more spectacular if the investor had moved to another sector. The moral of the story is that the investor must remain anchored to the fundamentals underlying the stock they have invested in rather than the price at which they bought the stock.

Even though Tata Steel is a better run company, with better corporate governance the huge debt accumulated by the company altered the fundamentals. The stock will take another decade before an investor anchored at his entry price of ₹939 is able to exit at a profit.

Markets are fluid and fundamentals can change dramatically.

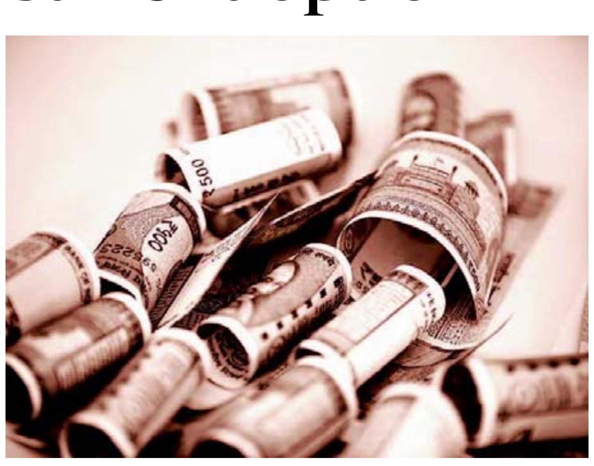
A smart investor must know when to drop anchor and when to lift the same to enable him to sail in the high seas in search of a better port to drop anchor.

(The writer is an author & a consultant)

EXPLAINER

Demystifying debt funds as an investment option

ASHISH RUKHAIYAR



A safer bet: Debt funds are generally used by banks and corporates for their treasury operations. •GETTY IMAGES/ISTOCK

What are debt funds?

■ While equity funds invest mostly in shares of listed companies, debt funds invest in instruments like government bonds, commercial papers (CPs), certificate of deposits (CDs) and non-convertible debentures (NCDs). Debt funds invest in such securities and earn interest income that is shared among the investors after deducting the fund-management charges. By investing in such debt schemes, investors can indirectly invest in instruments like government bonds as well where direct retail investment is not possible.

What are the different types of debt funds?

■ Debt funds can be classified on the basis of the tenure of the bonds or instruments in which they invest. Liquid funds invest in instruments that have a tenure of less than 90 days. Then come the short-term funds that invest in instruments that typically have a tenure of three to six months. There are corporate debt funds too that could have a tenure of up to three years. The long-term funds would invest in bonds that have a tenure of three to five years or even more like in the case of government bonds (G-Secs).

Do retail investors invest in debt funds?

■ The share of real retail money in debt funds is still minuscule though the share is rising as more and more investors take to financial planning wherein a certain portion of the investment fund is allocated to debt products. Most fund houses now offer systematic investment plan (SIP) facility for debt funds as well. Interestingly, debt funds are popular among high net worth individuals (HNIs) to park their money temporarily before moving to other asset classes, mostly equity. Debt funds are generally used by banks and corporates for their treasury operations.

Are they better than bank deposits?

■ Debt funds offer more return than bank fixed deposits and that is one reason why many HNIs and institutions use such schemes for their treasury operations. While debt schemes offer comparatively higher returns, the risk is also higher compared to the safe FDs that offer assured returns. In the case of bonds, the price could fall due to various reasons thereby impacting its price and ultimately the return. There have been cases where the securities have been downgraded that has led to the scheme taking a hit. Taurus Mutual Fund, for instance, took such a hit early this year when Ballarpur Industries failed to honour its maturity obligation and the fund house had to mark down the CPs to zero.

What about tax liability?

■ The gains made on the investment in debt schemes are taxable. If the securities are sold within three years, it is considered short-term wherein the gains are added to the income of the investor and taxed as per the applicable tax bracket. If the securities are held for more than three years before selling, there are long-term capital gains tax.

The tax rate is 20% with indexation and 10% without indexation. Indexation refers to the mechanism wherein the gains are adjusted against the rate of inflation to derive the net taxable gains from the schemes.

Centre may break up AI as it hastens sale

Air India has $8.5 billion debt burden and the government has injected $3.6 billion since 2012

REUTERS
NEW DELHI

India is considering selling state-owned Air India (AI) in parts to make it attractive to potential buyers, as it reviews options to divest the loss-making flagship carrier, several Government officials familiar with the situation said.

Prime Minister Narendra Modi’s Cabinet gave the go-ahead last month for the Government to try to sell the airline, after successive Governments spent billions of dollars in recent years to keep the airline going.

Air India – founded in the 1930s and known to generations of Indians for its Maharajah mascot – is saddled with a debt burden of $8.5 billion and a bloated cost structure. The Government has injected $3.6 billion since 2012 to bail out the airline.

Once the nation’s largest carrier, its market share in the booming domestic market has slumped to 13% as private carriers such as InterGlobe Aviation’s IndiGo and Jet Airways have grown.

Quick take-off: Air India has six subsidiaries three of which are loss-making with assets worth about $4.6 billion and has an estimated $1.24 billion worth of real estate. •REUTERS

Unsuccessful attempts

Previous attempts to offload the airline have been unsuccessful. If Mr. Modi can pull this off, it will buttress his credentials as a reformer brave enough to wade into some of the country’s most intractable problems.

His office has set a deadline of early next year to get the sale process under way, the officials said, declining to be named as they were not authorized to speak publicly about the plans.

The timeline is ambitious and the process fraught, with opinion divided on the best way forward: should the Government retain a stake or exit completely, and should it risk being left with the unprofitable pieces while buyers pick off the better businesses, officials said.

Already, a labour union that represents 2,500 of the airline’s 40,000 employees has opposed the idea of a sale even though it is ideologically aligned to Mr. Modi’s Bharatiya Janata Party.

‘Complex exercise’

Officials who have to make it happen are grappling with the sheer scale of the exercise. Air India has six subsidiaries three of which are loss-making with assets worth about $4.6 billion. It has an estimated $1.24 billion worth of real estate, including two hotels, where ownership is split among various Government entities.

No one has properly valued the company’s various businesses and assets before, two officials with direct knowledge of the process said. Earlier this month, about $30 million worth of art, including paintings by artist M. F. Husain, went missing from its Mumbai offices, chairman Ashwani Lohani said.

“The exercise is complex and there is no easy way out,” said Jitendra Bhargava, operational head of Air India in 1997-2010. “At this juncture, selling even part of Air India is far from certain.”

Mr. Lohani declined to comment on the sale process. The prime minister’s office and the civil aviation ministry also declined to comment.

A committee of five senior federal ministers, led by Finance Minister Arun Jaitley, is expected to meet this month and begin ironing out the finer details of the plan. Besides deciding about the size of the stake sale, the panel will set the bidding norms. It will also take a call on the carrier’s debt, de-merger and divestment of its three profit-making subsidiaries.

Mr. Modi’s office has said the Government has no business being in hospitality and travel, suggesting the prime minister wants to sell as much of Air India as possible, the officials said.

Back to Tata?

Analysts say the Government may prefer to keep the airline in Indian hands. At least two potential Indian suitors, the Tata Sons conglomerate and IndiGo, have shown early interest.

In recent weeks, officials in Mr. Modi’s office and from the Civil Aviation Ministry met Ratan Tata, the patriarch of the $100 billion-a-year Tata Sons, to gauge the company’s interest in a deal, a close aide to Mr. Modi said.

Tata would be an attractive buyer for the Government. The company founded and operated Air India before it was nationalised in 1953.

“Seems like Tata will come forward and make the best offer,” the aide said, adding the Centre would be keen to see that jobs are not lost.

Tata’s ventures

Tata, however, already has two other airline joint ventures in India, and it’s not clear what parts of Air India it would be interested in. A Tata spokeswoman declined to comment. IndiGo said on Thursday it was interested in the international operations and in Air India Express, a low-cost carrier.

Mr. Modi’s office has told officials to work out exactly how much each of Air India’s subsidiaries are worth to make it easier to break up the carrier if needed, two of the officials said. The Government is expected to appoint outside consultants to help with the exercise.

Anshuman Deb, aviation analyst at ICICI Securities, said splitting the airline will maximize value for the Government.

“Let us be realistic. It’s very clear that a single buyer cannot buy an entire state-owned company,” said a senior aviation ministry official involved in the process.