

MAHESHWARI & CO.

ADVOCATES AND LEGAL CONSULTANTS

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❖ PE deals touch \$6.4 billion

Downturn in the world economies notwithstanding, India is witnessing increasing number of private equity (PE) deals with the total value touching \$6.4 billion so far this year. PE deals in the country have fared well since the beginning of this year despite credit crunch, high oil prices, inflation among others.

"The total number of PE deals during in the first five months of 2008 stands at 170 with an announced value of \$6.4 billion against 159 deals amounting to \$4.9 billion during the corresponding period in 2007," global consulting major Grant Thornton said. Meanwhile, another global deal-tracking firm Zephyr said India is among the top 10 countries in the term of value of PE deals across the world.

India Inc witnessed the announcement of \$640 million worth of PE deals in May this year, a whopping increase of over 603% over last month figure while 1,1805 jump from corresponding period last year, Zephyr said in its latest report. In April 2008, \$91 million worth of PE deals were announced, it added.

Meanwhile, as per data compiled by Grant Thornton, the total number of PE deals announced during May stood at 14 with an announced value of \$1.45 billion as against 32 deals amounting to \$650 million in the month of April this year. Some of the significant PE deals in May include Golbot Holdings' investment of \$175 million for 3.68% stake in M & M and Symphony Capital's \$450 million investment in DIF Assets, the property fund of DIF Ltd.

Beside, Providence Equity partner's infusion of \$640 million for 20% stake in Aditya Birla Telecom (ABTL), a subsidiary of Idea Cellular was the other major PE deal of the month. Market observers are of the opinion that the strong growth fundamental of the country would help PE investment to hit around \$16 billion, mark this year and India is likely to remain a popular destination for the next few years.

Some of the factors that could pose challenges to PE investment include lower growth rate of export-based industries due to strong rupee, high oil prices that is one of the reason behind high inflation and potential capital gains tax on external funds routed through Mauritius. Meanwhile the bearish trends in the global and domestic economies have hit the country's merger & acquisition (M&A) transactions hard.

❖ Hard time for small telecoms in future

The acquisition of Spice by Idea Cellular has closed the chapter on almost the last of the mobile service providers with a small presence. Spice operates in the circles of Karnataka and Punjab and the buyout will help Idea in increasing its presence from 11 circles to 13. This is, of course, less than Bharti or Vodafone, even as it provides Idea a much-needed leg-up.

With an exception of players such as BPL Mobile, MTNL, Shyam Telelink and HFCL Infotel, every other operator has a large presence—meaning at least 10 circles. The top six operators in India—Bharti,

Reliance, Vodafone, BSNL, Idea and Tata Teleservices—account for 258 million subscribers out of India's 277.39 million subscribers at the end of May. That is a whopping 93%! Aircel has 11.49 million subscribers across 10 circles while a smaller one like BPL Mobile is restricted to Mumbai. MTNL is a two-city operation (Delhi and Mumbai). It is at a time like this when new players like

Videocon, Unitech, AT&T, and Russia's Sistema among others are looking to enter this highly competitive market. At a subscriber base of 277.39 users out of a population of over a billion people, India is said to have a reasonably healthy penetration level. Clearly, the rest of the population will be one possible target for the new entrants. Videocon Group chairman Venugopal Dhoot pretty much confirms

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this when he says there is a large market, which is still not in possession of a mobile. However, the story is rather different in a city like Mumbai, which is also an independent circle.

Mumbai alone accounts for over 12.3 million subscribers against a population of 19 million that translates to a penetration level of 65%, which compares to a national average of less than 28%. "I do not think that is a cause for concern since they're a market of over six million which can be addressed," thinks Dhoot.

A market surely does exist but the question is how much it can bring in as revenue. After all, all the big and medium users of a mobile phone are already locked into one operator or the other. "The lower end of the pyramid is one where the pre-paid component is big. The Average Revenue per User (ARPU) also, as a result is much lesser," says KPMG executive director (Telecom) Romal Shetty. Consider another large circle like Delhi where the ARPU for the October-December quarter, according to figures released by the Cellular Operators Association of India, stands at Rs 379.73. This is down from Rs 391.27 for the preceding quarter.

The fall in Kolkata, like Delhi, is around three per cent, while the fall it is at a more worrying 6.86% for Chennai. How much more this can fall remains to be seen. Unitech is another entrant waiting to launch services. Its managing director, Sanjay Chandra, has said that India is an underpenetrated market in terms of the number of operators and that there is place for more. Without a doubt, the new players will need a clear differentiator in this market.

"This could be on pricing or possibly on quality of service," says Shetty. Dhoot, for his part, speaks about his existing distribution as an advantage. "We have access to 50,000 dealers who can sell our mobile service. It, therefore, becomes very easy for us," he says. Dhoot says that he will launch his operations on August 15 from Chennai. More operators mean more competition resulting in a possible pressure on tariffs. "I think there is scope to relook at tariffs," concedes Dhoot. This comes after the government has said there will be a three-year lock-in period for the new entrants implying they cannot engage themselves in M&A activity. For the new entrants, starting afresh in large circles will not be easy.

The way forward looks interesting with talk of mobile portability (retaining the same number while changing the operator) looming large. The scenario looks interesting, as the consumer gets ready to be pampered again

❖ SEZ land come under I-T scanner

Land acquisition by special economic zones (SEZs) has come under tax scanner. The income tax department has upped the ante on tax deduction at source (TDS) on payments made for purchase of land for these projects. Inspections and surveys by the I-T department have revealed that in several recent SEZ land transactions; there was no deduction of tax. TDS, in such cases, has to be deducted at the rate of 1% for payments exceeding Rs 15 lakh. Though most of the companies that plan to set up a SEZ largely acquire land on their own, they also form special purpose vehicles (SPVs) with state agencies or even acquire land through these bodies. Any such entity buying

land has to deduct tax while making payment when the sale deed is registered. Besides these project-implementing authorities, public utilities implementing projects under fast track authorities will be under the watch in cases where implementation is not done directly by the state government. TDS on SEZ land acquisitions

- There has been an increased focus on the TDS by the I-T department
- Officials have been instructed to specially watch out for such transactions for additional revenue mobilization in the current fiscal.
- Land acquisition by special economic zones (SEZs) has come under tax scanner

issue figured at the annual conference of chief commissioners and directors general of income tax. Officials have been instructed to specially watch out for such transactions for additional revenue mobilization in the current fiscal, sources told ET.

The move comes close on the heels of the some state governments questioning the Centre's stamp duty exemption for such land purchases through provisions in the SEZ Act. States like MP and Orissa have written to the Centre, seeking a clarification on the issue.

There has been an increased focus on the TDS by the I-T department, which created a separate directorate to monitor collections under this head. The government's TDS collections grew by 51% in 2007-08 to Rs 1, 06,700 crore from a mere 2.36% in 2004-05. The total tax collection in the fiscal stood at Rs 3, 14,486 crore.

❖ India credit rating faces pressure

Global ratings major Standard and poor's (S&P) have expressed concern over rising subsidies, especially in the form of oil, food and fertilizers bonds. These subsidies are not explicitly accounted for in the budget accounts and are not reflected in the fiscal deficit numbers. These off-budget items account for almost 1% of GDP, it said. In a report released on Tuesday, S&P has said, "A reversal of the fiscal consolidation process, especially with rising off-balance sheet subsidy costs, in tandem with deterioration in the country's balance of payments (Bop) performance, could put pressure on India's credit standing."

The ratings agency has said that India's current ratings reflect the country's strong economic prospects, solid external balance sheet, and deep capital market, which support a weak, but improved fiscal position. However, it has warned that the key to India's creditworthiness will be the continued efforts at further economic reforms amid the vested interests of unions, public-sector managers, and political parties.

With elections expected in the next 12 months, the government is acutely aware that the failure to manage both rising domestic prices and an economic slowdown may bring retribution in the polls, it notes. The recent rise in domestic prices has resulted in a sharp rise in subsidies.

While India's official fiscal deficit position has improved to 2.5% of GDP in fiscal 2007-08, rising subsidies relating to oil, food, and fertilizers were not accounted for, and are estimated to have understated deficit by about 1% of GDP. Recent higher global oil prices are putting further pressure on the government's fiscal position in terms of supporting India's oil-marketing public companies, leading the government to announce an increase in petroleum and diesel prices. Although this will reduce the fiscal burden, the government still had to issue bonds worth Rs 94,600 crore, or 1.8%, of GDP in oil bonds. The fiscal deficit is expected to face further pressures. Rising commodity prices are likely lead to

subsidy increases and the Sixth Pay Commission has recommended salary increase for government employees.

As for inflation, the benchmark wholesale price index (WPI) rose to 8.1% in late May, the fastest pace since November 2004 and above the Reserve Bank of India's (RBI) target of 5% for FY08. On Tuesday, RBI increased

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the cash reserve ratio by 50 bps to 8.75%. With fuel-price hikes, the WPI is expected exceed 11% in the near term. The authorities are also grappling with signs that the economy is slowing — the forecast is for 7.5% growth in fiscal 2008-09, down from 8.7% in 2007-08 and 9.6% in 2007-06.

❖ CLB likely to replace BIFR for practicing euthanasia

Sick industrial units may no longer have to wait for decades for the authorities to decide whether they should be revived or liquidated. To fast track the determination of industrial sickness of enterprises, the government is planning to expand the scope of the Company Law Board (CLB) to assess whether a sick unit should be liquidated or revived. At present, the Board carries out this procedure for Industrial and Financial Reconstruction (BIFR), which would be wound up.

The corporate affairs ministry is working on a proposal to vest CLB with this authority. While the original idea for the ministry was to close both BIFR and CLB to make way for a multi-purpose forum called the National Company Law Tribunal (NCLT), legal complexities have come in the way. This has forced the government to seek alternative routes to speed up the process of reviving sick units. Officials attribute the ministry's Proposal to pass on BIFR's powers to CLB on the government's urgency to settle large number of cases pertaining to industrial sickness.

Officials say even though both BIFR and CLB would event usually be wound up, CLB is considered to be better poised to fast dispose of such cases. For this reason, the government is also working on a scheme to improve CLB's administrative setup. While the BIFR is regulated by provisions of the Sick Industrial Companies Act, (Sica) the CLB is governed by the provisions of the Companies Act. The new company law bill, expected to be placed in Parliament this monsoon session, would propose strengthening the powers

of CLB as the government fears that setting up of NCLT and its appellate tribunal would still take some time.

In the present scenario, the government sends the names of suspected sick companies to BIFR to decide as to whether they could be financially revived or liquidated. The BIFR, known for its procedural delays, takes years for a decision. The framework is time-consuming as well as inefficient, sources said.

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