

Heard on the Street

Dalal Street Pays for Its Performance

Foreign portfolio investors have dumped shares worth ₹1,400 crore in the first two days of 2019, resulting in the stock market starting the New Year on a sombre note. The Sensex and the Nifty have declined 2% in the last two days. The speculation is that the foreign fund outflows have been driven by selling from some global exchange traded funds (ETFs) to trim their overweight on India. The Indian equity market was the second best-performing among emerging economies for 2018 after Brazil. Most of the ETFs track benchmarks like MSCI or S&P indices. If one country outperforms and ETFs weight goes above the country-specific weights of MSCI or S&P, ETFs are forced to sell stocks proportionately, said market participants.

Contributed by Rajesh Mascarenhas

Street Signs

Sebi Comes Out With Rules for Single Regime for FPI, NRI Fund Flows

MUMBAI: Markets regulator Sebi has come out with rules for merger of foreign portfolio investment (FPI) and non-resident Indian/overseas citizens of India routes to bring in a single regime for foreign investors and regulate NRI and person of Indian origin fund inflows. Sebi has also exempted housing finance companies and systemically important NBFCs (non-banking financial companies) from disclosure of increase or decrease in shareholding due to encumbrance or release of encumbered shares, Sebi said in a notification. - PTI

ECL Finance Issue Fully Subscribed

MUMBAI: The public issue of secured redeemable non-convertible debentures by ECL Finance (ECLF), the NBFC arm of Edelweiss Group, was fully subscribed across categories. The issue successfully mobilised over ₹1,000 crore, making it one of the only in the last quarter to have even the green shoe option fully subscribed. The issue has seen keen interest from retail investors with the retail bucket being oversubscribed by 1.78 times with total collection of ₹500 crore against the bucket size of ₹300 crore. The issue was widely supported as subscription from high networth individual category stood at ₹230 crore with an average application size of around ₹44 lakhs from around 550 investors. - Our Bureau

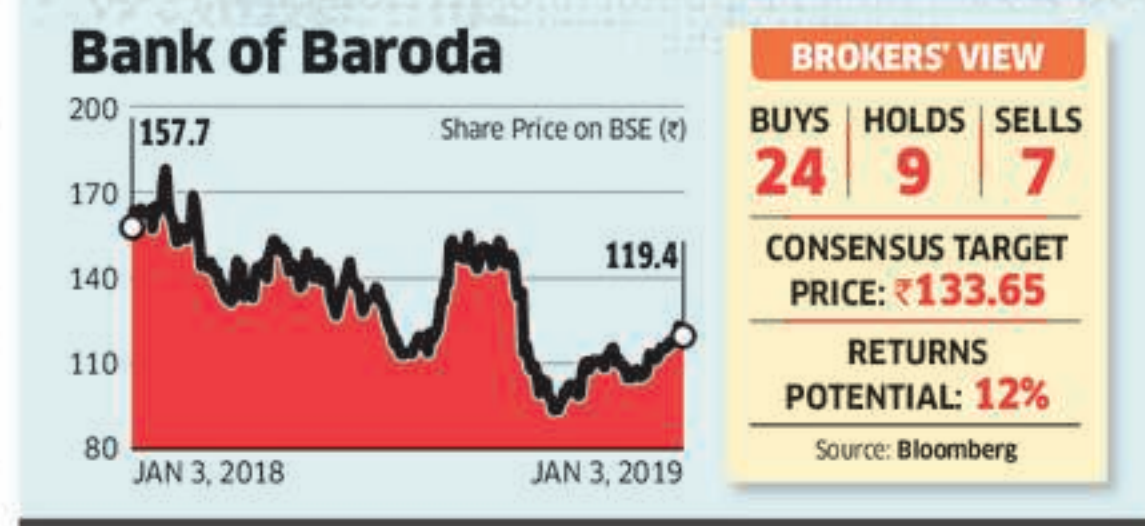
US Factory Activity Hits Two-Year Low

NEW YORK: US manufacturing activity slowed sharply to a two-year low in December amid a plunge in new orders and hiring at factories, which could further stoke concerns about how immune the US economy is to a global growth slowdown. The Institute for Supply Management survey published on Thursday offered a downbeat assessment of the manufacturing sector, with almost all components declining last month. - Reuters

THE FINANCIALS of Bank of Baroda are likely to be diluted immediately after the merger with Dena Bank and Vijaya Bank, but in the long term, the PSU bank stands to benefit 'Swap Ratio in Mega Merger of 3 PSU Banks Favours BoB'

Our Bureau

Mumbai: The swap ratio for the merger of the three state-owned Dena Bank and Vijaya Bank with Bank of Baroda is widely seen as favouring the last possibly to compensate for asset quality dilution, said analysts recommending a buy on Bank of Baroda. "Post-merger, the financials of BoB is likely to be diluted in the initial phase of the merger due to high NPA of Dena Bank. Also, technology related expenses, possible NPA provisions etc are also likely to take a toll on the merged entity profitability," said Lalitabh Shrivastava, assistant VP, research, Sharekhan. "However, we believe the share swap discount is done to either sweeten the deal for better-run banks or in anticipation of higher clean up in Dena Bank, which would, therefore, not upset the asset quality and earnings picture of the combined entity meaningfully," he added. While the process of merging



Dena Bank and Vijaya Bank with Bank of Baroda will present its own set of challenges in the near term, Bank of Baroda stands to benefit over the long term, analysts said. "Such a large-scale merger will present its own set of challenges in the near term, but the recovery in the NPL cycle, credit growth and the prospects of adequate capital infusion from the government will aid smoother integration and help in returning to normal operations" said Gautan Duggad, head of research, Motilal Oswal Securities. "The favorable swap ratios have resulted in 8.2% and 2.2% increase in book value and adjusted book value for BOB." Shares of BoB ended flat at ₹119.40 while Dena Bank and Vijaya Bank shares declined 20% and 7.25% to close at ₹14.40 and ₹47.35 respectively. The total number of shares post-merger is 342.5 crore and the net worth of the combined ₹55,600 crore. With an adjusted book value

for the merged entity at ₹80 per share, the combined entity is currently valued at 1.5 times its book, said analysts.

"The merged bank entity would be the third-largest commercial bank with a total business size of ₹15.4 trillion and loan book size of ₹6.6 trillion and branch network of 9,511," said Rakesh Kumar, analyst, Elara Capital. "As on September 2018, the entity net NPA and provision cover would be at 4.93% and 58.4%, respectively, relatively better than the overall state-owned banking vertical."

After the merger was announced, BoB shares have underperformed Bank Nifty and its peers by 13-15% and are currently trading at a fair valuation, said analysts.

"The stock trades at reasonable valuations of 0.8 times FY2019 book value in a corporate cycle, which is likely to improve" said Sohail Halai, analyst, Antique Stock Broking. "We continue to value the stock on standalone basis until better clarity on the merger process emerges."

JET AIRWAYS DEFAULT

RBI is on Test Under Das. Is It Kingfisher 2.0?

The Skeptic



MC GOVARDHANA RANGAN

Vijay Mallya, after a great run in building a liquor business, is now the poster boy of 21st century India's Robber Barons, though more qualified men compete for that title.

If banks are to be blamed partly for the magnitude of the losses in Kingfisher Airlines default, the remaining lies at the doorsteps of the Reserve Bank of India.

Sometime in 2010, being king trumped other obligations. The regulator abandoned its role of a referee and decided to play the saviour. It extended the much-abused Corporate Debt Restructuring scheme to the services sector too as it attempted to save an airline that was about to run aground instead of flying. Despite the noble intentions, it met its fate.

While the extension of that restructuring provision might be justified in the absence of a bankruptcy law then, it still exposes the regulatory weakness which let itself to be pulled in the direction that vested interests desire.

That ultimately led to bloating up of Kingfisher Airlines' debt and default. Depositors' money vanished in thin air and the fallout was even worse for some bankers who had to face jail, whether deserved or otherwise.

Come 2019. The question is will history repeat itself? Or, this time is different? Jet Airways, the second biggest domestic carrier, has defaulted. A few years ago, its default wouldn't be even public. Transparency has increased and the regulator has learnt from mistakes to plug the gaps that borrowers gamed at will.

At least on paper, this time is different. The country has a functioning bankruptcy law. There is a transparent procedure instead of a few bankers and the promoter drafting an unworkable formula that was aimed at saving their skins instead of re-creating an enterprise.

Yet another development has been the RBI's February 12 circular that forces banks to treat missing payments by a day as default and begin work on ensuring that the enterprise doesn't get into a deeper hole.

For obvious reasons, that has become the lightning rod for industry. Banks waited for an account to become a bad loan to initiate resolution, which meant waiting for three more months after a default. By then the damage is more severe.

The February 12 circular attempts to change the basic premise of banking in India. The assumption was defaults happen due to extraneous reasons and things would improve, which will

bring businesses back to normal. That works if you lend money to your neighbour on goodwill. Unfortunately, the money banks lend belong to unknown millions. So, bankers should arrest it before it gets worse.

Literary giant Ernest Hemingway encapsulates businesses better than economists from Harvard or MIT management gurus. "How did you go bankrupt? Gradually, and then suddenly," wrote Hemingway.

Jet reported a loss of ₹2,587 crores in September half year. Its accumulated losses are at ₹13,500 crore, making the net worth negative. It has nearly ₹6,300 crore loans coming up for repayment in about 24 months.

"Furthermore, the liquidity strain has aggravated due to delays by the company in implementation of its liquidity initiatives," says ICRA, a rating company. "Till the company



IN AIR POCKET Jet reported a loss of ₹2,587 crore in Sept half year. Accumulated losses are at ₹13,500 crore

starts reporting profits on a sustained basis, the debt levels are expected to continue to remain high."

If a company operating at near 100% capacity is unable to meet its financial obligations, something is amiss. One can blame oil prices, airport charges and many more. But none of these matters to bank depositors.

In the current regulatory regime, banks will have to drive the resolution in the next 180 days failing which it goes to bankruptcy courts. The solution is either the promoters bring in equity if the bankers have to sacrifice a portion of what is owed to them, or banks begin to look out for new investors to revive the firm.

The already loud chorus that February 12 circular is draconian may get louder. With the man behind that rule out of the way on Mint Street, the permission to restructure SME loans by the new Governor Shaktikanta Das has lit hopes of a rollback of the one-day default rule as well.

Well, if those hopes are met, it will be a throwback to the age of Robber Barons rather than entrepreneurship.

M-CAP-TO-GDP RATIO, largely known as Buffett indicator, now stands at 80% against a long-term average of 78%

Buffett Indicator Shows We're in for Big Gains in '19

Amit Mudgill@timesinternet.in

ETMarkets.com: The sharp correction in domestic stocks from their August peak levels has put Indian equities back on foreign investors' radar.

Multiple factors have turned favourable for domestic equities: Dollar bulls are no more roaring, commodity prices are in a free fall, excessive valuations froth has got wiped out and Sensex earnings — on likely revival in three banks namely ICICI Bank, Axis Bank and State Bank of India — look set to grow 20% in FY2020 from 13-14% in FY19E.

Dalal Street's only problem right now is volatility, which creates a risk that investors might get trapped in low quality stocks.

Analysts, who expect a better but choppy year ahead for equities, say investors should consider growth stocks on any reasonable fall to make most of the post-election opportunities. "As we head into 2019, the Indian



market is likely to remain volatile. We take a balanced approach to investing by being selective in taking risk (diversified equity exposure) while keeping a greater margin of safety and keeping some power dry for tactical opportunities through the year," said Nitin Singh, MD, Standard Chartered Wealth Management.

INDIA NO MORE OVERVALUED The market cap-to-GDP ratio, largely known as Buffett indicator, now stands at 80% against a long-term

average of 78%. This is much better than 113% for US and 82% for the rest of the world.

With earnings improving in the next couple of quarters, this indicator may drop to 75 level, which may make domestic equities attractive.

"Incorporating the growth prospects domestically, we seem to be well placed with India's stock market cap quoting at 80% on a trailing GDP basis, and 75% on next year's GDP assumptions. Hence, India is not overvalued and certainly well below the vulnerable mark i.e. 100%," ICICI Securities said in a note.

The recent market correction from the 2018-peak has created a greater valuation buffer, with valuations converging closer to longer-term averages, compared with the peak valuations a few months back, Standard Chartered said in a note.

The three biggest worries for stocks i.e. shadow banking crisis, inflation and general elections, may not impact India's macro drivers majorly in the long term, unless the situation worsens.

APPLE'S OUTLOOK CUT may have been a trigger: Jefferies; yen may continue to rally

'Flash-Crash' Moves Hit Currency Markets

Bloomberg

Mumbai: It took seven minutes for the yen to surge through levels that have held through almost a decade.

In those wild minutes from about 9:30 a.m. Sydney, the yen jumped almost 8% against the Australian dollar to its strongest since 2009, and surged 10% versus the Turkish lira. The Japanese currency rose at least 1 percent versus all its Group-of-10 peers, bursting through the 72 per Aussie level that has held through a trade war, a stock rout, Italy's budget dispute and Federal Reserve rate hikes.

Traders across Asia and Europe are still seeking to piece together what happened in those minutes when orders flooded in to sell Australia's dollar and Turkey's lira against the yen. While some pointed to risk aversion triggered by Apple



Inc. cutting its sales outlook, others said Japanese retail investors were bailing out of loss-making positions. Whatever the cause, the moves were exacerbated by algorithmic programs and thin liquidity with Japan on holiday.

"The moves were very violent," said Stephen Miller, an adviser at Grant Samuel Funds Management Pty in Sydney and former head of

fixed income at BlackRock Investment Management (Australia). "It would have caught some by big surprise."

With Japan on a four-day holiday this week, traders said they struggled to handle a flood of sell orders with pricing erratic. Once the yen strengthened past 105.50 against the dollar, others were forced to cover their short yen positions, said traders who asked

not to be identified as they aren't permitted to speak publicly. "It looks more like a liquidity event with the move happening in the gap between the New York handover to Asia," said Damien Loh, chief investment officer of hedge fund Ensemble Capital Pte., in Singapore. "It was exacerbated by a Japan holiday and retail stops getting filled on the way down especially in yen crosses."

As a result, the yen surged against every currency tracked by Bloomberg, and was up 1 percent against the dollar at 107.78 by 9:30 a.m. in London. The haven asset has strengthened against all its major counterparts over the past 12 months as concerns over global economic growth mounted and stocks tumbled. It rose 2.7% against the dollar last year, the only G-10 currency to gain versus the greenback.

FEDERAL RESERVE RISKS HAVING STOCK MARKET DEFINED AS BAROMETER OF SUCCESS

Powell and Trump Are Locked in a Battle for Wall Street's Trust

Bloomberg

Jerome Powell has been sucked into a one-sided communication fight with Donald Trump, who blames the Federal Reserve chairman for losses in the stock market.

Powell can't match the president's megaphone on social media. But he can try to prevent equity prices from becoming the barometer of Fed success by reminding the public that Congress gave it a different mandate: stable prices, and jobs for as many Americans as possible.

Trump's Twitter feed is "drowning out the message that the economy is doing well with low inflation and record low unemployment," said Sarah Binder, a senior fellow at the Brookings Institution in Washington.

Since October 3, US equity prices have plunged almost 15%, and Trump has put the blame squarely on the Fed. He tweeted on December 18 that central bankers needed to "feel the market" and hold off from hiking — one day before they raised rates. Bloomberg News reported Dec. 21 that the president had discussed

firing Powell.

The Fed chief has a chance to snatch the initiative back with public appearances on Friday in Atlanta and January 10 in Washington.

"The burden is on him to come back and say we are taking everything into account and we are also doing it independently," Diane Swonk, chief economist at Grant Thornton LLP in Chicago. "There is no easy answer here," she said, because the Fed can't be entirely separated from the causes of stock market volatility.

While investors had expected last month's rate increase, which showed Powell was willing to defy the president, they were alarmed by projections for two more hikes in 2019. The S&P 500 index fell more than 5% from December 19-21.

NOT JUST FED

The slide in share prices has many causes, analysts say.

Stocks may have been over-valued relative to a forecast for moderating US and global growth in 2019. Domestic stimulus engineered by Trump in early 2018 will fade in the coming quarters. China and the eurozone both show signs of slowing

Donald J. Trump @realDonaldTrump

I hope the people over at the Fed will read today's Wall Street Journal Editorial before they make yet another mistake. Also, don't let the market become any more illiquid than it already is. Stop with the 50 B's. Feel the market, don't just go by meaningless numbers. Good luck!



The economic outlook could deteriorate further amid Trump's trade dispute with China and the threat of a disorderly UK exit from the European Union.

The Fed did acknowledge those growing risks in its December 19 policy statement, pledging to monitor

"global economic and financial developments." That left investors puzzled over what it would take for the central bank to shift into a holding pattern — especially when there are few signs of rising inflation.

For all that, the data show the Fed is doing what Congress asked it to. The

jobless rate is below the Fed's estimates of what constitutes full employment, and inflation is running close to its 2% target.

LOUDER VOICE

Moreover, Powell and his colleagues have said they'll pull back if new data

RBI to Meet Foreign Investors

From ET Markets Page 1

"Why is RBI forcing FPIs to buy five company bonds if the investor has long-term plans," said a person advising FPIs.

Foreign investors have also not been able to access the government securities market directly even after RBI permitted them. They have

been doing it through banks.

"Unfortunately, foreign investors have not been able to log-in because of electronic signature requirement. The issuing authority is Income Tax and you have to do separate KYC (Know-your-customer) for that," the person quoted above said. "There will be some suggestions on that also, besides on allowing investments in all maturity papers."

confirm the market's more pessimistic outlook. The two projected rate hikes could disappear, just as four increases foreseen at the end of 2015 turned into just one during 2016. Investors, however, aren't getting that message. Two possible reasons stand out: The critics have a louder voice, and Fed communication hasn't been clear.

Trump has 57 million followers on Twitter and each of his tweets on the Fed is amplified by blaring media headlines. The Fed Board has 500,000 followers, and generally limits its tweets to dry topics like speeches or economic research. And, while the world's most powerful central bank does get plenty of media coverage, its own communication can be hard to decode — even for market professionals.

COULD DO BETTER

It could do better, according to Richard Torrenzano, chief executive of The Torrenzano Group, which counsels corporations and executives on reputational strategy.

"The Federal Reserve does have a large megaphone and bully-pulpit

platforms they have chosen not to use," Torrenzano said. "They need to explain why and what they are doing in an active and thoughtful way," including on social media, he said. "Until they do, they will continually get beat up."

One example is the current Fed dependence on incoming data, which officials could do a better job of explaining. It's not the first time they've had this problem. In 2006, the Fed's then-Vice Chairman Donald Kohn urged his colleagues to spell out what that meant. "We have all said in our speeches, we are becoming more data-dependent," he said. "It behooves us to explain to the public what data we're looking at."

Another difficulty for Powell is that investors have an exaggerated sense of what problems the Fed can or should solve, according to Mickey Levy, chief US and Asia economist at Berenberg Capital Markets. He thinks Powell should stick to emphasizing his progress toward meeting the central bank's statutory goals.

"Markets expect the Fed not just to manage the real economy, but to prop up the stock market," Levy said.