BANKERS TALK

"Governments do not have magic wands for economic revival"

The Government is taking all the necessary steps to revive the economy. It has taken quick decisions and is also focusing on executive and administrative capability to implement them. The bureaucracy has to be energised to get things going on the ground and then come the fiscal challenges which all of us are interested in seeing how they have to be tackled, says **G Krishnamurthy, Chief Executive Officer, L&T Infra Finance**.

Firstly, could you walk us through your outlook for the infrastructure sector for this year? How hopeful are you that infrastructure will see a turnaround?

There is a lot of hope that things will change. There is a belief and we think the Government has been making all the right noises and the first steps that they have done are all in the right direction. They have tried to empower the bureaucracy as far as decision making is concerned, as finally decision making has to structurally happen at the bureaucratic level. So that's we see is on top of the agenda.

What kind of enthusiasm are you seeing on part of banks to lend to the infrastructure segment? We have seen a lot of banks shying away from lending to infra projects in this kind of an environment.

There are lots of positive messages coming out of what is happening. But this is a very early part of the whole story, in terms of how things need to pan out eventually. Infrastructure has struggled from 2010 to 2014… It's been four years of difficulty. And difficulties have come as a result of a multiple things, multiple things starting from the famous go, no-go decision, which people didn't understand for a couple of years. Then subsequently there was this freeze at the State level. Meanwhile, there's not much fresh capex (coming in) so banks' appetite has not been tested. Having said that, many banks have taken a hit as the proportion of stressed assets in infrastructure is higher than other sectors. Given this factor, the banks are cautious. In the Budget we expect measures to enhance flow of credit. We expect IDFs to create fresh headroom. The infra sector was completely starved for equity for quite a few years, whereas they were building assets at a very furious pace, which was supported by a heavy degree of leveraging. So there was actually very less equity.

When do you see the government likely to remove barriers for accessing debt capital markets for infrastructure financing?

Given that there is three-four years of history, the build-up of issues has happened due to multiple factors. There are also the external factors which came in, commodity shorts which happened, foreign exchange volatility which happened. Nobody is born with a magic wand. And by creating very high expectations we'll be actually impeding growth. What we would prefer is a slow and steady progress and some of these things will require a year or so to be completely unwound in a slow and steady manner. The Government is facing fairly heavy challenges on multiple fronts and expecting them to completely change things around in a sector like infrastructure within a quarter is not the right set of expectations. So our expectations are that things will pan out for a few quarters, but we already have the right elements in play. The first cut which has already happened is expectations led to the right sentiment. So we have really heavy investor sentiment which is there on the equity side as well as on the debt side, particularly bond markets.

Looking at the investor side, we have seen a few foreign entities making investments in coal (thermal) which was unthinkable some time ago. In other sectors also there has been a slight pick-up in M&A activity in infra where assets which were there on sale for quite some time are being sold. So there is a trickledown effect, there is a positive environment which is already happening.

So what we would expect is some of these policy decisions and executive decision making processes to take place over a couple of quarters. The first issue is therefore addressing projects which have already either been completed and not working or which are in the process of being completed. The Government has to get the framework right for those projects, by policy and executive and administrative actions, so that these projects either start functioning or they start getting back into competition or conception mode.

A number of projects have received necessary approvals from the Government of India over the past few months. Has this translated into any new investment in the infrastructure sector?

The demand for infrastructure has changed. (Compared to) what was there three-four years ago, the demand for infrastructure has come down. Like in the roads sector, traffic growth rates have come down. There is actually de-growth happening in specific segments, which is linked in a way to auto sales. It's linked to commercial vehicles and construction equipment sales, all of which have de-grown.

In terms of priorities, standard infrastructure projects have started moving at a policy level. We are also improving the global competitiveness of our manufacturing sector. The good thing is that a few large auto companies are reporting around 30 per cent growth. We don't know if this is one-time demand or pent-up demand.

We have seen entire sectors, like textiles and sugar go through a phase of difficulty. Order inflow into Indian private industry has not happened, large capacities have been built up in anticipation for submarine orders which never came, for naval orders which never came, for defence orders which never came.

In the manufacturing sector de-growth can be addressed and addressed fairly quickly and this along with policy changes for infra will be the key markers that we will be looking towards. And the next stage is when we really expect a revival cycle in terms of fresh capex for infra.

Governments do not have magic wands. I think the Government is doing all the right steps. They have taken quick decisions. They are focusing on the manufacturing sector, they are focusing on executive and administrative capability to implement decisions. There are so many decisions to be done, that a few ministers can't do it. The bureaucracy has to be energised to get things going on the ground. Then come the fiscal challenges which all of us are very interested in seeing how they need to be tackled. It's a fairly difficult issue and the Budget will be something which all of us will be very keenly watching.

> “The Government is facing fairly heavy challenges in a sector like infrastructure within a quarter is not the right set of expectations.

What about the projects where there have been no investments so far?

Projects which are operational typically happen when there is an ability to deliver greater amount of financing which helps them to actually grow capital. That's because the average infrastructure project is 30 years long; the first round of financing is 15 years. The project is now up and running. More financing or replacement financing, is in effect a substitution, and it also generates growth capital for the industry. So refinancing has been one focus. We have as a company specialised and we've created a niche area of franchise in renewables. Ours is the only portfolio where you will see that our exposure to solar, wind and hydro is more than our exposure to coal/thermal projects. Nobody else in the country has taken this call.

That has supported our growth in the last few years because this is one area where capex has been fairly continuous. Some of the issues which we faced in our gas sector or coal-thermal sector have not been there. They are small-sized projects. Land acquisition is not such a big issue, re-settlement is not such a big issue, rehabilitation and approvals are not big issues. These issues can be handled by mid-level management. At the same time, we also created an IDF business model. Today as a country we have a problem coming in terms of the ability of the banking system to deliver credit to infrastructure. Even if there is a strong demand for capex support, banks are not being able to support the infrastructure sector. This is in addition to the Basel III issue. That's an issue for flow of credit to any sector sector. What I'm talking about is even if banks have invested capital, do they have the ability to deliver credit to infrastructure?

So what is required is to create mechanisms for improving credit flow to the infra sector and IDF has been one such stellar initiative. This is a vehicle which can vary in a focused manner and finance only operational projects. What it will do is to take out the banking system and do this financing. And then there will be less reliance on the banking system; there will be larger reliance on the domestic bond markets as well as global investors. So some degree of facilitation has already been done out there.

So I think the right steps have already been taken and we think IDF will be able to play a much larger role in the years to come in evacuating loans from banking systems for operational projects. IDFs will create the ability for the banking system to support constructional finance. What's left is to allow IDFs to operate through an NBFC format.

How are you addressing these concerns while advising your clients? Are promoters getting good valuations for these assets? What about the asset quality situation? How soon can we expect a revival?

As a group, we have aspirations of providing end-to-end services to the customer. We would like to be present across every market segment and every customer segment and to deliver every such product which is possible. Therefore in that context we actually are calling ourselves less of an infrastructure project financing company anymore, which is what we were talking about, maybe a year ago. L&T Financial Holdings has now conceptually got three main businesses: the wholesale lending arm, the retail lending arm and the asset management business.

We are also now looking at non-infrastructure selectively. We are already engaged in increasing the market space in which we are there. Of course having said this there are limited opportunities because of some issues. For example, there are larger issues in iron & steel as compared to the infra sector. So there is opportunity, and we are already on the job, creating institutional processes and systems. IT

- RAHUL KAMAT