

India Notes

India GDP grows most since Dec 2007; tightening seen

India's economy grew at its fastest pace in nearly three years in the April-June 2010 quarter on strong manufacturing growth and better farm output that may keep the Reserve Bank of India (RBI) on its gradual monetary tightening path. Data released in the first week of September 2010 showed annual rate of growth picked up to 8.8 percent from 8.6 percent in the previous quarter, underscoring continued growth momentum in Asia's third-largest economy amid a slowing pace of global recovery.

India May Reap Bumper Winter Crop

India may reap a bumper winter-sown crop including wheat and oilseeds this crop year as heavy monsoon rains have raised water reservoir levels beyond the 10-year average and increased soil moisture. Water reservoir levels are 136% more than a year ago and have touched 102% of the 10-year average. The rains couldn't have come at a better time as the country's farmlands were parched after the worst drought in nearly four decades in 2009. High water reservoir levels particularly help winter-sown crops as seasonal monsoon rains usually end in September.

Land Deals on a high, it's residential this time though

Tier I cities in North and Western India continued to see a uplift in land acquisition transactions as bids have started touching record levels seen in 2007-08. The key differentiator this time is the expected land use which is skewed significantly towards residential as compared to commercial developments in the last peak. While in South India, land transactions continue to be far and few, as most developers are now treading a cautious path and looking for joint development agreements rather than outright purchase of land due paucity of funds

Investor Update September, 2010

<i>In this issue:</i>	<i>Pg</i>
<i>Economy & Markets</i>	<i>2</i>
<i>Real Estate</i>	<i>4</i>

Contact Us

Yatra Capital Limited

43/45 La Motte Street
St. Helier
Jersey JE4 8SD
Email: info@yatracapital.com
Website: www.yatracapital.com

Gavin Wilkins

Tel: +44 (0)1534 702 815
Fax: +44 (0)1534 702 870
Email: Gavin.Wilkins@minerva-trust.com

Investment Advisor



Saffron Capital Advisors Limited

Saffron Capital Advisors Limited
4th Floor, Ebene Heights
34 Cybercity, Ebene, Mauritius

Ajoy Veer Kapoor Vijay Ganesh

Tel: +230 4034384
Fax: +230 4673100
Email: vganesh@saffroncapitaladvisors.mu
ajoyveer Kapoor@saffronadvisors.mu
Website: www.saffronadvisors.com

Economy & Markets

India GDP grows most since Dec 2007; tightening seen

India's economy grew at its fastest pace in nearly three years in the April-June 2010 quarter on strong manufacturing growth and better farm output that may keep the Reserve Bank of India (RBI) on its gradual monetary tightening path. Data released in the first week of September 2010 showed annual rate of growth picked up to 8.8 percent from 8.6 percent in the previous quarter, underscoring continued growth momentum in Asia's third-largest economy amid a slowing pace of global recovery. The robust growth bolsters the case for further interest rate increases and some bond dealers anticipate a 25-basis point rate rise already at the Sept. 16 Reserve Bank of India policy review. The RBI, however, appears reluctant to hurt growth by raising rates aggressively, so it is expected to continue using a combination of small rate rises in conjunction with keeping banking system liquidity tight. The benchmark 10-year bond yield fell by two basis points to 7.95 percent after the release of data.

However, with inflation still in double-digit territory in recent months, the RBI remains firmly focused on getting price pressures under control. Analysts continue to expect further policy tightening in coming months, forecasting benchmark rates to be hiked another 50 basis points by the end of the year.

Inflation Focus

The Reserve Bank of India has raised interest rates four times since mid-March 2010 and has said it may have to give precedence to containing inflation over other policy objectives. Strong economic growth has raised the spectre of capacity constraints, which analysts hold partly responsible for the stubbornly-high headline inflation, which stood at 9.97 percent last month. Although India's wholesale price index in July 2010 rose at its slowest pace in six months, underlying price pressures remain.

The ruling Congress party has said that controlling prices must be the top goal in the face of popular discontent with rising costs affecting hundreds of millions of people who live on under \$1.25 a day.

RBI Governor Duvvuri Subbarao has also reiterated that inflationary pressures were easing, but analysts say this is unlikely to deter him from raising rates again to slow down headline inflation to 6 percent by March 2011.

Growth Optimisim

Policymakers are confident India will meet growth targets in the current financial year. On the whole, the projection that we have been making of 8.5 percent stays though it could be a little better. Government spending is also expected to pick up after the monsoon. There are, however, signs India's break-neck growth may be moderating, with recent data showing a slowdown in factory output growth. Industrial output in June 2010 expanded at its slowest rate in 13 months.

The pattern mirrors that in Asian peer China, the only major economy which is growing faster than India, where worries of softening growth were accentuated by data that showed easing in investment and factory output. But India's domestic-demand driven economy is benefiting from buoyant consumer demand that is pushing up car sales and making factories produce to their optimum capacity. Annual car sales in India rose 38 percent in July 2010. India's June-quarter manufacturing output jumped 12.4 percent year on year compared with a revised annual rise of 3.8 percent in the previous year.

It's farm sector expanded 2.8 percent and is expected to see robust growth on good monsoon rains, which is likely to further boost consumer demand by lifting rural income.

India May Reap Bumper Winter Crop

India may reap a bumper winter-sown crop including wheat and oilseeds this crop year as heavy monsoon rains have raised water reservoir levels beyond the 10-year average and increased soil moisture. Water reservoir levels are 136% more than a year ago and have touched 102% of the 10-year average.

High water reservoir levels particularly help winter-sown crops as seasonal monsoon rains usually end in September. Higher output of foodgrains, oilseeds and other crops would ease food inflation, which rose to multi-year highs after last year's drought.

Adequate rains in the northern grain-bowl regions of Punjab and Haryana will likely offset the impact of dry spells in the three rice-growing eastern states of West Bengal, Bihar and Jharkhand. India, the world's second-largest rice grower, may reap a bumper harvest of 100 million metric tons in 2010-11, up 10% from a year earlier thanks to more plantings in productive regions and better adoption of high-yielding seeds.

Good News for Crops and food security

The country will likely produce a record pulses crop of 16.5 million tons in 2010-11 because areas under the protein-rich staple have risen due to high state-fixed prices and government incentives. India is the world's largest consumer of pulses, and higher output will help it reduce imports from around 3 million tons a year. Summer rice planting until Sept. 2 rose 6.6% to 31.87 million hectares thanks to normal monsoon rains, official data showed. Rice is primarily a summer-sown crop, but it is also grown in winter. The area under pulses cultivation increased 21.4%.

Widespread showers in the past two to three weeks have brought India's monsoon rains up to the long-term average level, data from the weather office showed. From the start of the season on June 1 until Sept. 5, the country received 752.7 millimeters of rain, just higher than the 50-year average of 752.4 mm.

Domestic Demand Going Strong

Auto Sales Going Strong

India's domestic sales of passenger cars grew by more than 33% in August 2010 to touch a new record high, as rising incomes coupled with a growing economy and a spate of new launches continued to lure customers to showrooms. Auto makers sold 160,794 cars in August 2010 compared with 120,681 in the same month a year earlier, the Society of Indian Automobile Manufacturers (SIAM) announced.

Car sales had grown by 38% to 158,764 units in July 2010. That was also a new record. The jump in domestic car sales for August was the 19th consecutive increase. Domestic passenger vehicle sales, which include vans and sport-utility vehicles, gained 34% to 204,227, the SIAM statement said. Local two-wheeler sales stood at 957,304 units versus 776,772 units in the corresponding month a year earlier, according to the SIAM data.

Sales of Commercial Vehicles (trucks and buses) were at 52,030 units as against 40,609 units sold in August 2009, the SIAM data showed. But, vehicle exports declined 7.4% to 38,279 units in August 2010.

18 % drop in FDI inflow in first half

The uncertainty in the global economy seems to have impacted the flow of foreign funds into India. Coming close on the heels of the decline in exports is the news that foreign direct investment (FDI) declined by 18.3 per cent to € 8.27 billion (\$10.77 billion) in the first half of 2010 as compared to January-June 2009, where the country received FDI worth € 10.13 billion (\$13.19 billion).

The decline in FDI inflows is a cause for concern for the government which is seriously looking at foreign funds to boost investment in the infrastructure sector. The continued slump of economic activity in the Western countries and European nations has had an adverse impact on foreign inflows into India. The sectors which attracted the maximum overseas investment include services, telecommunications, construction activities, housing and real estate, power and automobile.

The country received the maximum investment from countries like Mauritius, the U.S., the U.K., Singapore, the Netherlands and Japan. The government is making sustained efforts to make the FDI policy regime more attractive and investor-friendly, with a view to attracting investments from all major investing countries, the release added.

The government had recently floated discussion papers for public debate to liberalise FDI in multi-brand retail and the defence sector. FDI at \$25.88 billion in 2009-10 was lower by 5 per cent against \$27.33 billion in the previous fiscal.

Exports grow by 13.2% to \$16.24 bn in July 2010

Exports grew by 13.2 per cent to € 12.47 billion (\$16.24 billion) in July 2010 compared to the same period last fiscal, posting growth for the ninth month in a row. Imports too jumped by 34.3 per cent to € 22.41 billion (\$29.17 billion) in July 2010 compared to the same month last fiscal, according to the official data released on Wednesday. During April-July 2010, exports posted a growth rate of 30 per cent to € 52.71 billion (\$68.62 billion) on year-on-year basis.

Imports during the April-July 2010 grew by 33.3 per cent to € 86.18 billion (\$112.2 billion). Oil imports in July 2010 grew by 4.4 per cent to € 5.84 billion (\$7.6 billion), while non-oil imports jumped by 49.6 per cent to € 16.52 billion (\$21.5 billion). The country's trade deficit widened to € 9.93 billion (\$12.93 billion) in July 2010 compared to the year-ago period.

FII's pump \$2.5 bn into Indian stocks

Maintaining their bullish stance for the third month in a row, global fund houses made a net investment of € 1.92 billion (USD 2.5 billion) in Indian equities in August 2010. As per the data available with capital market regulator SEBI, foreign institutional investors purchased shares worth € 1.04 billion (Rs 62.19 billion), while they offloaded equities worth € .84 billion (Rs 50.1 billion) during August 2010, resulting in a net investment of € 202 million (Rs 12 bn).

With the August 2010 inflow, the total investment made by FIIs in the local stocks now stands at € 10.06 billion (USD 13.1 billion) so far this year.

Real Estate

Realty giants to bare it all from April 2011

Large real estate companies will be forced to give elaborate details of their assets and land banks from the first quarter of the next financial year as they come under International Financial Reporting Standards (IFRS) regime from April 2011. Big real estate companies with a net worth of more than € 169mn (Rs 10 billion) such as DLF, Unitech, Peninsula Land and Puravankara Projects, among others, will report the June 2011 quarter numbers under IFRS as per the schedule approved by the government. Other BSE Realty index constituents such as HDIL, Indiabulls Real Estate, DB Realty, Anantraj Industries, Sunteck Realty, Sobha Developers, Phoenix Mills, Parsavnath Developers, Orbit Corporation and Ackruti City will also be migrating to the regime as per the net worth criteria.

Accounting firms advising companies on IFRS believe real estate companies would face severe accounting hurdles during the transition phase. In certain cases, where builders have sold ongoing projects and collected a part of the money for the work completed, they will not be able to report any sale or profit in their books of account. For tax purposes, the income-tax department has directed real estate companies to report sales using the percentage of completion method (POCM) but that will not be acceptable under IFRS. Such transactions will affect the dividend distribution capability of some real estate companies and even the remuneration of managers.

Under IFRS, sale of residential units will in most instances be accounted for as sale of goods, not as a construction contract. It means that revenue will only be recognised when the property is completed and the transfer of title and rights of ownership is done. However, there are some real estate companies that are happy to adhere to elaborate disclosure requirements under IFRS, even when they too feel revenue recognition is an issue.

A lot of real estate companies set up special purpose entities for the purpose of acquiring land, where share capital is owned by somebody else (lawyers or a legal firm) but are funded by these companies themselves. Such assets are not shown in the books of the companies unless transferred to them after the aggregation of smaller parcels of land (agricultural or otherwise) is completed. Also a lot of land owned by real estate companies which have not been disclosed so far in their respective books (but shown as a loan given to, say, a legal entity) will have to be disclosed much earlier now under the IFRS regime.

Also private equity investments in a “project entity” floated by real estate companies, where the PE firm agrees to exit by selling the shares back at a fixed price plus a percentage of the principle amount after a certain period, will be considered as a “borrowing” and not a sale to a third party under IFRS. Such disclosures will multiply the problems faced by real estate companies as they will worsen their high debt levels. In such cases, banks will take extra caution while lending to real estate companies because debt-equity ratio would go up, leading to a possible breach of the debt agreement.

Residential

The first half of 2009 saw developers cut prices by 25-30% and start to concentrate on the mid-income residential property. This implied lower prices, lower unit sizes, and no frills. The central bank reversed four years of tightening through a cut in policy rates (Repo) and the cash reserve ratio (CRR). Sales of mid-income residential property surprised positively, as consumers took advantage of improved affordability, especially in the NCR.

Prices, in the Tier II and Tier III cities, are still close to the bottom, but inventory clearance is now under way. In areas such as Mumbai, the lack of supply has led to price increases in some cases beyond the 2007 peak. The Delhi and Gurgaon markets also have seen appreciation of 25-30% in prices since the bottom seen last year due to strong demand. We expect the prices in NCR to remain stable from here on, while Mumbai prices could soften a bit, as volumes have started dipping post the sharp increase in prices in the last 12 months. But in South India and other Tier 2 & 3 locations, price increase continues to be moderate, with volumes seeing a good traction.

High-end residential, which had not seen any major pickup in 2009 (except Mumbai and parts of NCR), is also starting to turn around, with the revival in the economy. And, as absorption increases in high-end homes, we believe the prices will also soon follow.

Commercial property: Revival underway

The IT/ITeS sector accounts for 70-75% of the commercial property demand. Financial services in Mumbai and Delhi make up the bulk of the rest. Rents fell dramatically from late 2007 to 1H09, driven by the broader economic downturn, specifically in the financial services and IT/ITeS sectors.

Announcements by companies suggest a pickup in hiring in major cities such as Mumbai, Delhi/ NCR and Bangalore. Financial services firms (concentrated in Mumbai and some areas of Delhi) have started hiring in the last three quarters, while IT/ITeS companies have started hiring and announced major employee addition plans in the last 6 months. It is expected that these are leading indicators of a pickup in leasing activity for commercial property in the next 3-6 months in the financial services and IT/ITeS sectors. The supply of upcoming/half-finished commercial buildings is likely to cap rents for 12 months but they may start inching up by second half of 2011.

Retail property: Some rays of hope

Massive store roll-out plans by domestic and foreign retailers led to a flurry of supply in 2005-07. However, it also led to skyrocketing rentals until supply actually hit the market. The market, therefore, saw rents fall dramatically, driven by a high base effect, oversupply, and the downturn in the economy. The pace at which rents were falling has reduced, but they remain under pressure due to weak volumes. As retailers move back into expansion mode, volumes are picking up in some areas, such as Mumbai and select micro markets. Rents are likely to stabilize by the second half of 2010. In some markets (like Mumbai), they may start inching up, due to a pickup in demand and limited supply in 2011.