‘Centre has become smart in how it conducts disinvestment’

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Kotak Investment Banking managing director and chief executive S. Ramesh.

Indian capital markets are at an inflection point, says S. Ramesh, managing director and chief executive at Kotak Investment Banking. He expects to see Rs 1 trillion of fund raising in the next 12 months. In an interview, Ramesh says the Indian market is likely to witness a record fund raising spree with the banking, financial services and insurance (BFSI) space dominating. Ramesh believes 5-7% of incremental domestic money will flow into insurance initial public offerings. He also says that domestic flows are unlikely to choke secondary market liquidity. Edited excerpts:

What is your view on the Indian capital markets? I believe that Indian capital markets have been at an inflection point from fiscal 2015. So fiscal 2015 to date, from what I saw of the tally of the numbers, India Inc, in various forms has raised close to $36 billion and close to $60 billion have been the inflows from foreign institutional investors (FII) and mutual funds. So we are in for interesting times and I just want to say that it may not be 18 months, it may be in 12 months that you will see Rs100,000 crore being raised in India.

There is a lot of argument that there is a huge gush of domestic liquidity which is helping this secondary market to rally. From your perspective, with this supply of paper coming in, will this choke the secondary market liquidity or do you think this will enhance expanding the bull market?

The answer is clearly the latter. If you look at just the mutual fund collection, the net mutual fund collection which we are witnessing in recent months, it is Rs6,000 crore a month and there are two other things I want to quickly add. Out of the Rs100,000 crore expected to hit the market, a lot of paper is out of insurance, banking and the financial services.

Insurance is a space where we have not seen much initial public offering or any form of paper come to the market and mutual funds are actually wondering where they should deploy this collection. And it will be a great fit to what they want to do. Close to 33% of the domestic and international money is in the financial services and my judgement is 5-7% out of this will now incrementally move to the insurance sector. So it is exactly what the doctor ordered.

So from a valuation point of view, do you think that is a sector which is poised for growth which would mean that there is a lot of demand for insurance paper over the next six months?

If you look at the profile of the market today, both secondary and primary, there is no presence of infrastructure in real estate. So these are high growth companies with high return on equity (ROE). My definition of high ROE is in the high teens, with formidable growth in great governance. So valuations tend to be a little high, but I think they deserve these valuations. What do you make of the overall banking, financial services and insurance space? Do you think there is a kind of a bubble forming up in BFSI and one needs to be a little careful now?

Not at all. If you look at the BFSI space, there is a lot of variety that is coming into this. The reason I am asking is AU Small Finance Bank at eight times, RBL Bank at six times, is there a risk of valuation in that space?

The answer is that with many of these companies in the BFSI space, I think valuations are going to set a new normal. So, I do not think the valuations bubble is of any concern and investors are looking forward to investing in these companies because of their historical high Roes and great growth.

Then the big question is what this means for the PSU banks. You think there is a ray of hope for the PSU banks?

The PSU banks, we recently did a qualified institutional placement for State Bank of India (SBI) which was the largest Qualified Institution Placement (QIP) in the market. It was very well received. Secondly, investors have started to take note of some resolution around the non-performing loans (NPL) and talk around the merger, so they will be selective on the PSU banks. But I want to go back to the BFSI space. In addition to historical non-banking financial companies (NBFC) and banks, now there are more private sector banks, but interestingly, insurance IPOS and now we are also going to see exchanges coming, mutual funds coming. So there is a lot of variety to choose for these investors. What is your view on the 12 cases which are in National Company Law Tribunal (NCLT)?

I think there is already one that has really come to conclusion or very close to conclusion. In any of these new thematic significant structural stuff that you do, it will never be wrinkle free, but I am optimistic that you will see a few cases over time, which are successful and in a way, that will reflect on the stock prices of these banks and institutions. So I am definitely hopeful. The one big trend that I saw personally in that IPO market over the last 12 months was that a lot of the IPOS which hit the market were exits for the private equity (PE) guys rather than fresh capital for the businesses. Is that going to be a change in terms of IPO profile of companies because a lot of insurance companies are going to come?

The aspect that you referred to now does not apply to insurance companies, but what you talked about, these are companies from the non-infra, nonreal estate which got PE funding 4-5 years back and all of these are now due and ripe for exit. But, the three characteristics I would like to repeat, in most of these companies, if not all, many of these companies are close to a billion dollar market cap. Secondly, their Roes are very good which is a key barometer investors look at. Thirdly, they are phenomenally high growth firms with great governance and young promoters. This is the trend of the IPO market today—this trend will continue.

Coming to the divestment agenda now. In fact, we are in the middle of NTPC'S offer for sale (OFS) of 5%. You expected almost 10% to be sold over a period of time in NTPC and there are a few others as well lined up. Good timing by government in terms of selling out selectively into the open market.

I would like to give you a trendy answer on disinvestment. I am optimistic that the government disinvestment programme will broadly meet what its objectives are.

But as a person who has been observing this for a number of years, what I do see is that the government has become adept and smart in how they conduct their disinvestment. Earlier it was restricted to a few companies, but today that basket has widened.

INTERVIEW