

Insight

Primed to grow

Prime Focus Ltd, one of the largest integrated post-production and visual effects (VFX) services companies in the world, on Thursday announced that it was acquiring two unlisted US firms — Post Logic Studios and Frantic Films — for \$43 million (Rs 170 crore). However, the markets don't seem to be impressed as the stock dropped 2.5% on a day the broader based BSE Sensex recorded a marginal rise of 0.3%, following the announcement.

The deal awaits certain statutory and regulatory approvals and will be financed by a \$55 million (Rs 218 crore) FCCB issue the company is planning. The amount remaining after funding the US acquisitions could be used for another small acquisition, though nothing has been finalised yet.

Apart from an entry into the US market, the acquisitions give the company 55,000 sq ft of land in Hollywood. It will also get access to the R&D division of Frantic Films, which markets and develops visual effects software solutions. The acquisitions are expected to contribute to the consolidated financials of Prime Focus from 2009 and will add about a third to its total revenues.

Prime Focus has been on an acquisition spree for sometime now. In 2006, it acquired a 55% stake in VTR (UK's fourth-largest post-production company) for Rs 41.6 crore and a 100% stake in Clear, which provides VFX services through VTR. VTR currently contributes around £18-20 million (Rs 147-163

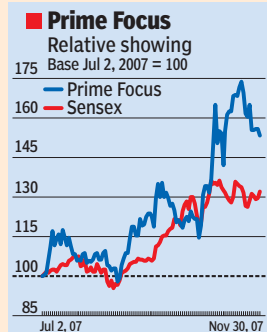
crore) to its annual revenues.

In September this year, it acquired the post-production business of UTV Software Communications for \$3 million.

Analysts maintain that the share of Indian operations will decline post this acquisition. Domestic revenues formed 39.6% of its total revenues in the quarter ended September (Q2) and grew 92% to Rs 23.17 crore, thanks to extensive post-production work done for various films and two VFX projects for VTR. Its net profit grew at a slower pace by 58.29% to Rs 8.88 crore as other income dropped by 65.7% and the tax outgo increased by 96%. Consolidated revenues and net profit for Q2 stood at Rs 58.45 crore and Rs 9.66 crore, respectively.

Meanwhile, the stock has outperformed the Sensex and appreciated by a whopping 262% in the past one year. At Rs 1,182, it trades at 21.45 times its estimated earnings for 2009. Analysts maintain that valuations at these levels appear sustainable on the back of its expanding global presence, higher budgets for post-production and increasing role of visual effects in movies these days.

Prime Focus is also expected to benefit from cost arbitrage through outsourcing. Given that it is still in its nascent stage, and most filmmakers are giving importance to the kind of services it provides, there is a huge growth potential. The stock merits attention on declines.



Potent but pricey

The stock of UTV Software Communications, an integrated media and entertainment company engaged in television content & services, broadcasting, movies, animation and gaming, has appreciated by an impressive 223% and outperformed the broad-based Sensex in the past one year.

For almost a month now, rumours about Walt Disney acquiring further stake in UTV have been all over the place. The company denied this on Friday, following which the stock fell by 1.41%. The stock, though, is still up by 13.35% in the past one-month.

UTV derives around 47% of its revenues from the film and production business and has a presence in both domestic and international markets.

It recently acquired Indiagames and Ignition to enter the mobile and console gaming space and has regained presence in the broadcasting business with the launch of the Bindaas channel. It also produces television content and has a 225-seater animation studio. A fairly diversified business model remains its key positive.

As for financial performance, it reported net sales at Rs 71 crore for the quarter ended September 2007 (Q2), up 89% as compared to the same period last year. This emanated primarily from the films division, which saw good momentum with a revenue growth of 365%. Revenues from the animation and gaming business dropped by 17.5%, as there

were no game releases this quarter and Indiagames was not consolidated pending closure of the deal.

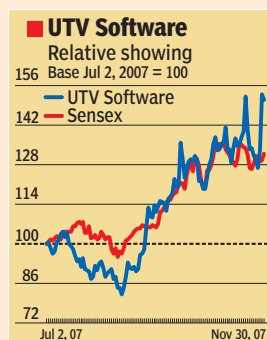
The company's earnings before interest, taxes, depreciation and amortisation increased by 148% in Q2 to Rs 18 crore and profit after tax rose 221% to Rs 13 crore.

Going forward, UTV plans to launch eight channels by 2009 across various genres. Its success story largely depends on the quality of content it will be able to provide. Besides, one can only wait and watch UTV's performance in the highly competitive industry. The films division, too, seems strong and UTV has performed well so far, despite the high-risk business, as revenues depend on its films' performance at the box office.

The animation and gaming business is still at a nascent stage in India and has good potential. The Indian gaming segment, comprising mobile, computer and console games and development, stood at Rs 192 crore in 2006. Nasscom estimates the same to cross Rs 1,700 crore by 2010.

At Rs 789.15, the stock trades at 18.8 times its estimated earnings for 2009. The company's prospects certainly look promising. Analysts maintain that the stock is a good bet in the space.

Contributed by Pallavi Pengonda & Devangi Bhuta



B L Kashyap arm to raise Rs 250 cr

Soul Space will issue new shares to PE funds, take loans

Subramaniam Sharma, New Delhi

B L Kashyap & Sons Ltd, a contract builder for Indian developers including DLF Ltd, plans to raise as much as Rs 250 crore (\$63 million) for its real estate unit through loans and a private share sale.

"We are in talks with banks and several overseas funds," managing director Vineet Kashyap, 53, said in an interview at the company's New Delhi headquarters, without giving a timeframe. The unit plans to raise about Rs 150 crore through sale of new shares to private equity funds, he said, adding, the rest would be raised as loans.

B L Kashyap owns almost 98% of Soul Space Projects Ltd, which is developing 2 million square feet of shops and owns a combined 250 acres of land in Bangalore, Pune and Bikaner, Kashyap said.

B L Kashyap, which raised Rs 190 crore selling 2.75 million shares in an initial public offering in March last year, is close to hiring an investment

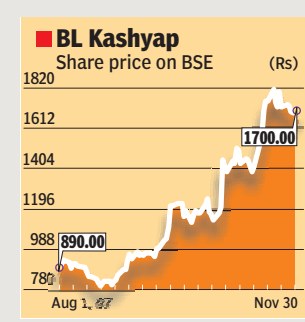


Realty rush

The subsidiary is developing 2 million sq ft of shops

It owns a combined 250 acres of land in Bangalore, Pune and Bikaner

B L Kashyap owns almost 98% of the company



bank to advise it on the sale in its real-estate unit, Kashyap said.

Soul Space is expected to increase annual profit to about Rs 1,000 crore on sales of about Rs 2,500 crore in three years, Kashyap said. Revenue at the parent may more than triple to Rs 2,700 crore by the year ending March 31, 2009, he added.

According to him, B L Kashyap, which had Rs 1,900 crore of orders in hand as of October 31, expects to complete about half by the end of March.

Real estate prices in India have surged after an average 8.6% growth in the economy in the last four years raised incomes and demand for homes, shopping malls and offices. The stock of B L Kashyap, which

builds offices, shopping malls, hotels, factories and homes, has more than doubled this year, beating the benchmark BSE Sensex's 38% gain.

"There's a housing shortfall and huge job creation in India," Kashyap said, adding, "Wherever there's job creation, real estate and urban infrastructure will grow."

Mumbai has the world's second-highest office rents after London's West End, according to data compiled by real-estate broker CB Richard Ellis.

Rental values at Forum, a shopping mall in Bangalore, have risen 49% between March and September this year, according to Bloomberg data.

Rental values for shops at Koregaon Park, a residential district in

Pune, have gained 20% in the same period.

Real estate developers in Asia's third-biggest economy have sold stakes in projects to overseas private equity funds. DLF, India's largest developer by market value, raised \$377 million selling 49% in seven residential projects to a Merrill Lynch & Co fund on November 19.

In September, Deutsche Bank AG, Germany's biggest bank, led a group of private equity companies to invest \$425 million in Mumbai-based developer Lodha Group.

JPMorgan Chase & Co and ICICI Bank Ltd's venture capital unit had already invested in the group. — Bloomberg

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Sistema gets nod

Sistema is likely to increase its stake to 51%, and subsequently to 74% in Shyam Telelink. Currently, the FDI cap in telecom sector is 74%. "The overall value of the deal may touch \$58.1 million at that point," Sistema had said referring to a 51% stake in Shyam Telelink.

Sistema is the first Russian company to enter the Indian telecom market. It reported revenues of \$2.7 billion for the first quarter of 2007 and had total assets of \$21.6 billion as of March 2007.

Shyam Telelink, which has a subscriber base of 2.57 lakh, has applied for unified access service licences across the country. According to analysts, its application for pan-India operations would push up its valuation to around Rs 1,000 crore to Rs 1,200 crore.

Sistema has tried to enter the Indian telecom market earlier also. For instance, it was believed to be in talks to acquire AT&T's stake in Idea Cellular some time back. It also figured among the names doing the rounds when Hutch was selling its stake in its India operation-Hutch Essar. The other foreign players in the Indian telecom market include Vodafone, Singtel, Telekom Malaysia and Maxis.

Shyam Telecom had, around four years ago, sold its GSM operation Oasis in Rajasthan to Bharti. Shyam Telelink, which had demerged from parent Shyam Telecom group recently, has been operating CDMA and fixed phone services since then.

Tata Steel inks JV

Michael O'Keefe, chairman, Riversdale said, "The formation of the joint venture with Tata Steel would en-

sure the coal project in Mozambique is well positioned to exploit the full potential of the Moatize region."

"This was a major consideration for Riversdale and the joint venture with Tata Steel represents the best possible outcome for these tenements in Mozambique. The global business of Tata Steel has an increasing need to source coal and the Mozambique project is well positioned to help meet their future demand for hard coking coal," O'Keefe said.

Riversdale recently announced a capital-raising plan to mobilise up to \$207 million of additional funds to develop the company's projects in Mozambique. Mozambique is fast becoming a region of global significance for the coal sector. In addition to Riversdale and Tata Steel's involvement, one of the world's largest mining groups, Companhia Vale do Rio Doce, too, has invested significantly in plans to advance a massive coal project next to Riversdale's tenements in Moatize.

B Muthuraman, managing director, Tata Steel, said, "We have vast experience in coal mining, spanning several decades and will be contributing technical expertise to the joint venture."

Cruz sacked

Cruz thought Pandit should allow her to take bigger trading risks to improve revenue, while Pandit thought any blame for the unit's underperformance should lie with Cruz, according to the book.

Cruz became a more divisive figure at the firm after she accepted the promotion to co-president along with then-chief financial officer Stephen Crawford. The action caused senior executives including Pandit, John Havens,

Joseph Perella and Terry Meguid to quit the firm in protest. None was willing to return to Morgan Stanley, even after Purcell's departure, as Mack didn't replace Cruz, people familiar with the situation said at the time.

Morgan Stanley spokesman Mark Lake said Cruz and Mack declined to comment. — Bloomberg

Pinning footnote

"These details were not carried as part of the announcement. However, after the DNA Money report, we felt further clarification was needed, and therefore, the footnotes giving the dates on which the trades happened were added to the original announcement."

An NSE spokesman, too, said so much. "The company has clarified with the exchange after the news article in DNA Money, following which the footnotes describing the period in which the shares were sold was added," he said. The sale operation of 18.4 crore shares was so savvy that hardly anyone in the markets was aware of the seller's identity, till the unloading lasted for about 10 days.

On November 6, RIL sold the largest chunk of 7.18 crore shares, which amounted to 1.60% of RPL and earned about Rs 1,691.48 crore, at an average sum of Rs 235, in the process.

This was the single-largest chunk to be unloaded, with the subsequent tranches accounting for less than 1%.

After November 6, there was a lull. RIL returned to the markets on November 13 to 16, selling 0.30%, 0.65%, 0.38% and 0.13% RPL stakes, respectively. From November 19 to 23, the shares sold were again less than a percentage point. In this period, RIL sold

0.34%, 0.22%, 0.08%, 0.20% and 0.12% of RPL stake, respectively.

While RPL and RIL clearly adhered to every law on reporting norms such as informing the exchanges etc, some questions still linger.

While DNA Money had earlier reported about spikes in the futures & options segment before the share unloading, it now emerges that the cash segment was also not immune to a couple of spikes that reflected in unnatural delivery of shares. They were not operators, but people who owned the shares. And they sold at higher prices than what RIL's sales fetched.

What's intriguing is that huge voluminous trades were registered a few days before RIL started selling RPL shares. The whole November saw intriguing trading spikes in the RPL counter.

On November 1, the two premier exchanges witnessed frenetic activity as the refinery share recorded an intraday all-time high of Rs 295 before it ended the day's high-octane trading at Rs 261.85 per share. On that day, the delivery of shares accounted for 4.5 crore. And the character of trading that day was also very different as it ended with an unusually huge wave of deliveries.

About 4.46 crore RPL shares were delivered that day. On November 2, the deliveries recorded in the RPL counter in both the exchanges were muted at 1.76 crore share. On November 5, the spike was witnessed again as deliveries pole-vaulted to 3.36 crore and the share price ended at Rs 267.55.

While some demand was witnessed in the counter, it should be noted that there were sellers who matched the wits of buyers by unloading shares for delivery instead of squaring off, as in day trading.

Thinking modalities for a sovereign wealth fund

The least it would achieve is much better returns on the forex reserves

In a recent lecture, Y V Reddy, the Reserve Bank of India (RBI) governor, rejected the idea of having a sovereign wealth fund (SWF) citing reasons like current account deficit, vulnerability to oil price volatility, fluctuations in food grain production and hot money (portfolio flows).

Should we feel proud of being the fifth-largest accumulator of foreign exchange reserves sitting on \$260 billion? And if we cannot stem the accretion in reserves, shouldn't we at least try to increase the returns on them? Forming a sovereign wealth fund could just be a win-win solution.

SWF is a special purpose vehicle of the government, funded by foreign currency assets, with a higher risk tolerance and higher return expectation. The management of assets under SWF is separate from the management of the official reserves. Unlike official reserves, which are usually held in short duration US bonds, the SWF portfolio has a product mix of different fixed income, equity, commodity and realty instruments. Since the funding is being done in foreign currency and also since the investments are done in foreign markets, there can be no inflationary pressures due to sterilisation (which could have been the case if the reserves were being used for infrastructure funding).

So, what is the relevance of SWF to the Indian scenario?

Asian central bankers, including RBI, have been financing the current account deficit of the US and there is absolutely no indication that this will cease in the near future. The RBI's intervention in the market to stem appreciation in rupee will just result in further accretion of forex reserves. The calculation of forex reserves adequacy, using any of the theoretical models available, will show that we are well over the prescribed requirement.

I quote two of the most frequently used norms to measure the current forex reserves adequacy in India.

* **Import cover:** Reserves should be sufficient to cover 3-4 months of import. India has reserves sufficient to cover 15 months of imports (June 2007)

* **Greenspan-Guidotti rule:** Reserves should be equal to one-year short-term external debt. At the end of June 2007, the ratio of India's short-term debt to forex reserves was only 7.9%. Forex reserves were 129% of the entire external debt, thus exceeding the entire external debt by a whopping \$48 billion. Even by the most conservative approach, this \$48 billion can be considered as excess reserves.

Meanwhile, RBI has been sterilising the continuous appreciation of the rupee by issuing domestic debt at 7.4% (average yields for dated securities in primary market in 2005-06).

Unfortunately, as per the latest available figures from the Report on Foreign Exchange Reserves-2006-07, the return on the forex reserves was a dismal 3.9% for 2005-06 (July-June).

Thus, sadly, we are earning a return of just 3.9% on assets financed by a debt of 7.4%. Moreover, with rupee appreciating, reserves in national term are actually much less than in dollar term. Is this the right way of managing our country's assets?

One of the solutions to this situation obviously lies in actively managing the excess reserves to obtain better yield. That can be achieved by forming a SWF. Let's call it the Indian Wealth Fund (IWF). Let us assume that at the end of October 2007, IWF has strategic asset allocation like a balanced fund, with 60% investment in fixed income, 30% in equities and 10% in cash (or Fed funds).

We create a model case by using different benchmarking indices for the different asset classes (see table). A rough estimate shows that the return could have been 13.78% in the last one year. Assuming \$20 billion of the excess reserve is available for investments through the IWF, the returns (at Rs 39.5 per dollar) alone would be sufficient to finance 90% of health sector expenditure proposed in



Money's worth

Benchmark	Returns (%)	Allocation	Weighted returns
Lehman Aggregate Bond Index*	5.38	0.60	3.23%
S&P 500 Index	14.56	0.10	1.46%
MSCI EAFE**	22.02	0.10	2.20%
MSCI Emerging Market	64.24	0.10	6.42%
Cash (Fed fund)***	4.67	0.10	0.47%
Aggregate	—	1.00	13.78%

* Source: Bloomberg, MSCI
* Lehman Aggregate Bond Index covers USD-denominated investment-grade, fixed-rate bonds from the Treasury, gov-related, corporate, MBS, ABS, and CMBIS sectors; ** MSCI EAFE (Europe, Australasia); The index includes a selection of stocks from 21 developed markets, but excludes those from the US and Canada; *** Assuming cash balance can be put under Fed-50 bps

the 2007-08 budget. Similar calculations show that the aggregate returns from the investment would have been in tune of 10% and 6.5% for 5 years and 10 years, respectively. Of course, changing the allocation and time period variables will alter returns, but the point remains that investment through the IWF will inductibly lead to enhancement of returns.

Internationally, there are about 15-20 SWFs. Recently, China came up with an SWF named China Investment Corporation, which had an initial asset size of \$200 billion, i.e., around 15% of the country's forex reserves (excluding gold). One of the oldest SWFs, Norway's Global Pension Fund, with an asset allocation of 40% in equities and 60% in fixed income, earned nominal returns of 6.5% with a management cost of just 0.09% per annum.

How do we go about forming an IWF in India? It will be a separate autonomous body under the Constitution, with initial set-up funding from the government. Like any other investment fund, it will have a trustee and an asset management company (AMC). Trustees will constitute representatives from RBI, the ministry of finance and academicians, and will have fiduciary responsibility for setting investment objectives and ensuring proper benchmarking and risk management systems. The AMC will draw out professionals from the market, offering them competitive remunerations.

Asset or waste?

RBI has been sterilising the continuous appreciation of the rupee by issuing domestic debt at 7.4%

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IWF will be responsible for managing a portion of excess reserves transferred from the official reserves. The asset size can be increased from time to time with accretion in forex reserves.

The IWF will have investment objectives (decided by investment trustees), mainly to increase returns on foreign currency assets, and the AMC will work towards achieving those objectives.

It may be mentioned here that presently, Indian forex reserves are held in the form of short duration government securities and deposits with other central banks in four currencies, viz., the US dollar, euro, yen and pound sterling. Such allocation is driven by a low risk appetite and desire for high liquidity.

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Asian Oilfield to offer offshore services

Will expand seismic and drilling businesses

Promit Mukherjee, Mumbai

Baroda-based Asian Oilfield Services Ltd, which provides various onshore services to oil and gas majors, plans to expand its portfolio of services.

Gaurav Sud, vice-president - corporate strategy, said the company is looking to offer offshore seismic and drilling services, among others.

It is also considering acquisitions to expand presence and moderate the seasonal nature of its business. "We are scouting for business outside India and also looking at M&A opportunities in the country," he said.

Having started off with workover rig and shot hole drilling services, the firm has emerged as an integrated seismic data acquisition service provider.

Sud said it expects revenues to the tune of Rs 55 crore this fiscal and aims to cross the Rs 100 crore mark by the end of next fiscal. It has confirmed orders of Rs 72 crore now and is the L1 bidder in projects worth over Rs 65 crore.

The company has recently decided to raise close to Rs 51 crore through a preferential issue of 15,00,000 equity shares and 12,00,000 convertible share warrants to non-promoter strategic investors, as per a notice sent to BSE.

"By September 2008, Asian Oilfield Services would have approximately Rs 80 crore investible surplus in its balance sheet, which will be invested in incremental capital expenditure and new ventures of the company," Sud said.

