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Rural demand recovery might take longer: Religare Capital Markets

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The government's demonetization move will have a significant negative impact on earnings and sales, according to a survey done by Religare Capital Markets on a recent road-trip across India.

Gautam Trivedi, managing director and chief executive of Religare Capital Markets; Varun Lohchab, managing director and head of research, Religare Capital Markets; and Navin Sahadeo, vice president of Religare Capital Markets, discuss the findings of the road trip. Edited excerpts:

How are things looking right now, because November sales didn't really look that problematic but you think going forward there would be some pain in the system?
Trivedi: We will have to focus on December numbers; I think the December numbers will invariably end up surprising people. Not necessarily as we just come back from 10-day road trip and we have seen the pain that is out there within the country but the reality is that most of the places we went to people have not even seen the new Rs 500 note, let alone the Rs 2,000 note. The people who have got their hands on the Rs 2,000 note unfortunately are saying we can't use them because there isn't enough change on the other

side.

This is going to have a significant negative impact immediately on sales, that is one. Two, if you look at the auto sector in the two-wheeler space, we have seen a massive contraction in sales. Again that is also because most two-wheelers are below the Rs 2,00,000 Permanent Account Number (PAN) card radar and 50-60% of their sales are indeed in cash as a result. So, that is where we are seeing a lot of pain, we met the dealers of most of the big manufacturers. Unfortunately that is the

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I wanted to ask you about the sowing itself, if you all got any details? We were told that the net sown area is not very different from last year's same time. However, because of lack of money people are not able to put in inputs. Did you get a sense that this agricultural season as well might give less in terms of income?

Lohchab: The feedback was slightly different from state to state, so Maharashtra and Madhya Pradesh (MP) we saw that sowing is progressing well as per schedule. Uttar Pradesh (UP) typically goes for a rabi sowing a bit late, so out there it is delayed a bit further due to this demonetization. Apart from sowing, so I think overall sowing number may not come down dramatically but if you look at the internals of that, a lot of people are using older seeds like last year's crop

for the new crop plus they are using government seeds in which case the yields could be a bit lower. They are not going to use too much of fertilisers and pesticides. So the essentials, again out there the essentials, the seeds are still seeing some off take but pesticides and anything, which enhances the yield we are seeing a sharp drop out there. It will be difficult for yields to be maintained on a rabi crop. Therefore even though the area under the acreage might look good but you might have a lower crop output.

So, general purchasing power could take a hit?

Lohchab: We believe because kharif—again the realizations have got impacted especially for the perishable. So, cereals we have still seen good realization for farmers but for perishable whatever yields were good this time around in kharif got negated to some extent by the lower realizations. In the rabi case we believe the yields itself might be lower. So, for both kharif and rabi compared to what the expectation was in terms of the realisation for a farmer the farm income will take a hit and therefore the rural demand might take a bit longer than expected. That is the view we are getting.

Are there any states or any pockets which are moving seamlessly to sort of cashless transfers and are being able to cope up with demonetization quickly?

Trivedi: We haven't seen too much evidence of that as yet unfortunately. However,



Religare Capital Markets managing director and chief executive Gautam Trivedi.

Indians can adapt fast when the guns put to their head and frankly this is what Prime Minister Modi has done. So, we didn't see much use of Paytm. Some people said what is Paytm? I think this is a new concept to them but I think Unified Payment Interface (UPI) which for some reason is not being as heavily advertised as Paytm is by the RBI or by the government. I think they should promote that because that is SMS based and you really don't need a smart phone. So, finally that has started to happen, but people will have to adapt and change to the new environment.

The other issue is on housing and cement because that is the other big worry, what has happened in that space, especially in the hinterland.

Trivedi: On the housing bit—again in all three states that

we went to, everyone said that land should correct 30-40% and built-up real estate should correct anywhere from 15-25 percent depending on who you speak to. But the problem is, that has not happened yet. No transaction has taken place as yet. So, it is very early days and until we do not see a transaction happening, and of course, logically they should correct because the cash elements have been sucked out at least for the time being.

Sahadeo: In cement, what we have seen certainly first is of course the knee-jerk reaction. So, in November, most of the large stockists which we met, they said that their sales on a year-on-year basis, were down almost about 20-30%. But when we interacted with the retailers, the small time cement dealers, for them the sales in fact was a much higher 50-60%. Now, for December,

the general expectation on the street is that the numbers in absolute volume terms could be better as compared to November.

But, to our surprise, the feedback is that the December numbers could well be at par to November or in fact could be a tad lower than that.

Can you give us some regional colour on this?

Sahadeo: If I were to talk about Uttar Pradesh first, now the sand related issue, specific to this state, has been impacting demand right from July. October, as a month, they saw a severe brunt of it, wherein as compared to September the numbers were down almost 20% in October already. And because of this demonetization, there is a further dip of almost about 15-20% on that low number in the month of November.

South?

Sahadeo: South was not part of our road trip, but of course, prior to this, we did make a visit there. Now this is very region specific.

That same period last year, November, in Tamil Nadu in particular, there was a huge impact of heavy floods there. So, on that low base, November could turn out a very big surprise of 20-30% growth for companies.

But now, as we speak, dealers are definitely worried in terms of their offtake which is seeing a slowdown now. Very quickly, I want to highlight to your point about adaptability to that new mode of transaction.

The general feedback is that in the south, the resilience to this new payment will be far bigger. A very quick observation there being that even today, you see queues outside banks and ATMs even in Mumbai, leave aside the other place like north or central or west.

But in Chennai, I was surprised to see hardly any such queue and even if there was a queue, it was a fairly small queue, just 2-3 people there, particularly in Chennai.

What about the trucker's space because a lot of people tell us that long haul operators have faced quite a bit of issue and they have a lot of their payments that happen in cash when they move from one state to another. How much pain do you still see there and when do you see recovery in the commercial vehicle (CV) space?

Lohchab: Commercial vehicles, the consistent feedback, which we were getting was that it was anyway weak before this demonetization

issue. The fleet operators, profitability and the freight was anyway on the weak side, so the space has been under pressure for last almost 12-18 months across most of the regions and this is an additional hit. So, we saw that the movement of goods was still happening. So, it is not that things have come to a grinding halt in terms of the transportation, but, anyway, the volume oftake for the freight operators was weak and it has weakened further after this demonetization. The expectations of recovery in that space were quite weak compared to a lot of other segments when we look at that partly because the underlying fundamentals were anyway weak.

And in terms of the commercial vehicle financiers also we met, the used truck demand has fallen and therefore the rates have fallen out there and there is no incentive for a freight operator to go and buy a new truck either, a new one or a used one.

So, commercial vehicle (CV) transportation industry will remain under pressure in our view for some more time at least and that will have a ripple effect on the CV industry as well.

Trivedi: Let me just add something to that. The other thing which is interesting is that one of the dealers that we met, he said that the body of the truck, it is actually completely unorganized.

It is mom and pop shops who actually make the body of the truck. So, when you buy a truck, you do not get the whole body with it, you only get the front cabin and the rest of the truck. So, that entire industry is cash based and that has come to a grinding halt as well as a result.