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'We're frittering away gains of the last 15 years'

Rahul Bhasin has seen three bear cycles so far, having set up Barings Private Equity's India operations in 1997. While peers such as Blackstone and Warburg Pincus have made quite a few bold investments last year, Barings has been unusually quiet. Bhasin shares the reasons in an interview with *DNA Money*. **Page 30**

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DNA MONEY

'We're frittering away gains

Rahul Bhasin *has seen three bear cycles so far, having set up Barings Private Equity's India operations in 1997.*

Among the most notable investments by Barings was in MphasiS BFL and Msource. The investment in MphasiS was more than three tranches and in Msource, at least seven tranches. At the time of investment, both firms had less than 10 people on rolls. Today, the combined outfit has 30,000. Barings remains invested in the firm that was taken over by EDS a couple of years ago. Interestingly, while peers such as Blackstone and Warburg Pincus have made quite a few bold investments last year, Barings has been unusually quiet.

Bhasin, who lost his father recently, was in town to meet his sister. **Satish John & Ashish K Tiwari** *met up with him at a five-star hotel where businessmen and venture capitalists kept interjecting to say a quick hello. Excerpts from the interview*

q&a

As a private equity investor, where do you see the stock market headed?

I think we have caution today... *(pauses)* We still don't have fear in the market. The situation would get worse when that fear steps in. The markets will look very different when fear steps in. The pain will be felt in the next financial year, because of the lag effect. The foreign investors are not aware of the implications *(pauses and smiles to see if we comprehended the bold statement).*

Can you elaborate? After all, Barings raised quite a bit of money through its India-specific fund...

Our risk appetite has reduced considerably. As a result, we have significantly slowed down our investments here in the last 12-15 months. I can tell you that we are sitting on huge amounts of cash today. We have raised $600 million, but we haven't spent a dime. This is because of our nervousness.

What are you waiting for?

I really need the comfort of responsible policy direction. Look, there is a price for every investor. We don't look at short-term returns of one year. We look at returns over 10 years. To that extent, I need far more comfort on policy direction. You have to demonstrate responsibility. You have to stand up and explain that oil is more expensive. If you are going to use it, better pay for it or use less... you can't do what you are doing... you can't become an ostrich.

I feel strongly about this, because we are not dealing with small numbers.

Here we are not talking about (economic) cycles. We are talking about inopportune macro-economic management. We are frittering away our gains made in the last 15 years.

Your investors may get impatient...

We have no pressure from our investors. So I can easily sit on it. A new private equity firm may not be in a similar situation. I won't say that we won't invest in this market situation, but the risk has gone up considerably. What we really need at this stage is the comfort of a responsible policy direction to start investing all over again. Capital is available very easily. The US has a mature industry to give out capital for investments. Even the excess money from oil producing nations is routed via the United States. In fact, if one traces the origin of all the money that is being raised, the main source would be the oil producing countries and mainly the Gulf nations.

"The Prime Minister going out requesting people to be austere will not work. But if he tells you that you'll have to pay Rs 100 more for the same resource, it will work."

What returns can you give by sitting on cash?

We earn bank interest.

Is that all? The currency has depreciated...

(Smiles) Yes.

So does it add up to 10-11% returns?

(Smiles again and nods) The alternative was to lose 40% in the market. But we continue to look at deals. On an average, we earn our investors about 15% over a 10-year timeframe.

What do the current market sentiments mean to private equity mavens like you?

You have to understand that when there is a bull market, we all are geniuses and vice versa. So if it is a bear market now, the best thing for us to say is that we can cleverly blame the environment for the same. But, on a serious note, I don't think it is a minor one and I don't think it is a short-term one.

I think we are heading towards a 'bubble-burst' scenario and this time, it will be for a longer period than before.

What makes you feel hard times are nigh?

The unfortunate reality is that the country's energy bill has gone up from $40 billion to $110 billion. So, whichever way you look at it, the view is very depressing. For the same economic activity, we are paying a substantially steep price and this is a big hit. An increase of $70 billion, which is 6.5% of the country's GDP... Think about the fact that our tax base is just about 11% of the GDP and 6.5% of the GDP is a huge number. When you have an extra cost of this nature, you can either monetise it or pass on the cost to the system. If you pass on the cost to the system, then whoever is using the energy can modify his behaviour, leading to better resource efficiency.

If fuel subsidies are removed, wouldn't it hit the poor below the belt?

The energy bill has a unique characteristic, because the consumption of energy is exponentially related to your income level. Thus, the poor use very little energy, but as your wealth increases, you consume more. Actually, if you pass on the energy costs, you will correctly distribute the incidence to the richer sections of the society — not to the poorest. The alternative is to monetise it, but that will create structural inflation. Our policymakers are following the path of monetising energy costs. The $70 billion is only a direct hit. There is also a hit if you also look at our fertilisers budget — Rs 31,000 crore. The reality is Rs 150,000 crore because the feedstock for urea is natural gas, a commodity whose prices have escalated exponentially.

Today, people are not really thinking about conserving energy or using it in the best possible manner. The Prime Minister of the country going out requesting people to be austere will not work. But, if he tells you that you'll have to pay Rs 100 more for the same resource, it will very well work.

"The consumption of energy is exponentially related to your income levels. Thus the poor use very little energy, whereas as your wealth increases your energy consumption grows exponentially. Actually, if you pass on the energy costs you will correctly pass on the costs to the richer sections of the society. Not to the poorest."

That's the reality. Can it be helped?

It is a very bad situation and I'm not saying that any political party is to be blamed for this. The reality is that the terms of trade have changed drastically. There is no denying that we are a poor country, but we have only created a far bigger monster by reacting the way we have to this situation. Instead of having tamed inflation, we will suddenly see that inflation is going to become structural. I think it is a very, very dangerous situation *(shakes his head).*

And what about foreign investments into the country?

I am certain it will slow down dramatically. I don't think foreign investors have understood all the implications yet.

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DNA MONEY

of the last 15 years'

"We have created a far bigger monster by reacting the way we have to inflation. Instead of taming it, we will suddenly see that inflation is going to become structural. I think it is a very, very dangerous situation."

There is a school of thought that feels the culprit is excessive speculation...

Prices can go up only if I am an actual user. If I buy a contract for 100 crude oil futures, at the end of the month I have to sell it. This is absurd *(shrugs)*. You don't kill the messenger.

The Essential Commodities Act was a very sensible one, but banning futures is not a solution to deal with this market situation. If I hoarded it, or took it away from the market, then I can understand why the authorities need to be aggrieved. But, it is not Indian politicians alone who think this way; even in the US, we are hearing this language.

By your premise, the secondary markets will see more pain next year...

If inflation remains quite high, the cost of capital will jump up. Running with it is the fiscal deficit ... then your ability to invest in infrastructure is zero. You already face physical constraints. If you juxtapose all this, the economic outlook becomes quite scary. So, whether it is private equity or listed equity or your own capital, the cost will be very high.

India needs a lot of investment in the infrastructure sector...

The cost of capital will go up. Investments will slow down dramatically. I don't think people have understood the implications. I don't think foreign investors have understood the problem.

But foreign institutional investors have been selling...

Well, only marginally. Thus far, they have sold about 2% of the investible funds (FII investment is $70 billion as on date), which is roughly $5-6 billion of the foreign funds. Imagine the effect if they start selling 20% of their funds *(shrugs shoulders again)*.

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