



**POTENTIAL DIVESTMENTS**

**Oil Marketing Co’s**

India’s oil marketing companies are likely to be first on the chopping block. Bharat Petroleum, Hindustan Petroleum, Indian Oil and Natural Gas Corporation.

**Other Industries**

GAIL and Gujarat Gas are both Government assets to be divested. Air India has long been slated for sale and will benefit greatly by being run by private investors such as the Tata Group.

**NDA Success**

The current Government has been more successful in achieving targets than the previous UPA leadership. Likely to see further 100% achievements given requirements

**GOVERNMENT DIVESTMENT**

**FUNDING REQUIRED FOR MORE STIMULUS**

The Government of India is likely to announce divestment of majority owned government assets to help fund further stimulus and infrastructure to kick-start the Indian economy from its current slowdown. The Government is starting to show a level of urgency with regards to getting divestments done prior to the end of the current fiscal year (31 March 2020), given their target of A\$22bn for FY20. For this to happen announcements on divestments need to be made in this calendar year, with a following roadshow.

The Government does not have a strategic intent in owning Coal, Oil, Shipping and Infrastructure assets. This is where there are likely to be divestments. Additionally, the Government is unlikely to desire cross holdings across various entities to achieve majority ownership as this leads to inefficient structures being formed. The existing sell-down of some holdings through an ETF is the preferred route for ongoing divestment in smaller parcels. However, this does create an overhang in the valuation of these businesses.

| Disinvestment: targets and achievements |                 |        |        |        |        |        |        |        |          |        |
|---|-----------------|--------|--------|--------|--------|--------|--------|--------|----------|--------|
|   | UPA 2           |        |        |        |        | NDA 2  |        |        |          |        |
|   | FY10            | FY11   | FY12   | FY13   | FY14   | FY15   | FY16   | FY17   | FY18     | FY19   |
| Actuals (INR Cr)                        | 23,553          | 22,144 | 13,894 | 23,957 | 15,819 | 24,349 | 23,997 | 46,247 | 1,00,057 | 84,972 |
| BE (INR Cr)                             | No target fixed | 40,000 | 40,000 | 30,000 | 40,000 | 43,425 | 41,000 | 56,500 | 72,500   | 80,000 |
| Actuals as share of BE                  |                 | 55.4   | 34.7   | 79.9   | 39.5   | 56.1   | 58.5   | 81.9   | 138      | 106.2  |
| Actuals as % of GDP                     | 0.37            | 0.29   | 0.16   | 0.24   | 0.14   | 0.2    | 0.17   | 0.3    | 0.59     | 0.45   |

Source: Department of Investment and Public Asset Management, Ministry of Finance, GoI

# DIVESTMENT FORMULA

It is our view that we are likely to see a significant divestment announced in CY2019. The most likely candidate discussed in the marketplace is Bharat Petroleum (BPCL), an oil marketing company of which the Government currently owns a 53.3% stake. The sale of BPCL alone can fetch close to Rs.700bn (Government divestment target of Rs.1.05 trillion). The current market capitalization of BPCL is Rs.1.13 trillion (valuing the Government’s stake at over Rs.600bn). Any strategic investor will gain 34 million tons of refining capacity and access to 25% of India’s fuel marketing.

It is more likely that the Government will relinquish control entirely, rather than sell down their stake. This will have the positive impact of improving governance and efficiency of these businesses. The Government does not see the need to hold onto assets or “control”, unless there is a strategic requirement e.g. Defense, Power.

However, rather than an IPO, it is widely expected to opt for a strategic stake sale. The key to this will be how much of the “ownership or control” premium will the Government receive. A recent IPO of the Indian Railway Catering business was completed at a price far lower than what could have been received in a strategic sale with a pre-bid consultation. With greater insight into the potential of a business, suitors are far more likely to be able to decipher the unlocked value that exists for their business to make a strategic purchase.

The Government control stake has left several power, utility and infrastructure companies listed in India with a de-rated multiple. Hence the ideal outcome would be a strategic stake sale of the entire holding, moving businesses into private hands and removing control by Government (by selling down below 50% ownership or exiting completely).

This can potentially create value for these businesses by unlocking the existing de-rated multiple and provide positive sentiment for the broader stock market, especially given the knowledge that the Government is likely to be putting in place much needed reform.



# MARKET IMPACT

We expect the stock market impact to be significant from a sentiment perspective. If the first such divestment / strategic sale can occur, it will create a blueprint for further strategic sales. It will also provide the market with the knowledge that further stimulus and reform can occur. With slowing growth, there is increasing concern of weak tax collections impeding the fiscal deficit. **We expect the market to set new highs on news of a successful divestment strategy by the Government.**

It should also be an impetus for **closing the “Valuation Gap”** which was created from January 2018 to September 2019 between the top-15 stocks by market cap and the broader market. We expect the market refocus on “Value” as a concept and the gap between defensives and cyclicals start to close, particularly with the economy given a greater chance to recover from its existing position.

Our Fund is well placed to take advantage of the closing valuation gap.

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