



# ***THE NEWSMAKER***

(Newsletter of DMS Financial Services Co. (P) Ltd., Chennai)

Volume: 13

for PRIVATE CIRCULATION ONLY

November 2009

---

## **CONTENTS**

**A) HOSTILE TAKEOVERS – EQUITY WARRANTS TO PROMOTERS - page 1**

***by Suresh S., Director, DMS Financial Services Co.P.Ltd.***

**B) CONTAINER TERMINALS - FINANCING INDIA'S SUNRISE SECTOR - page 3**

***by Padmalatha S.***

---

## **HOSTILE TAKEOVERS – EQUITY WARRANTS TO PROMOTERS**

***by Suresh S.***

**Director, DMS Financial Services Co. (P) Ltd.**

One of the methods for Promoters and owners to keep control of their companies from the glare of hostile take overs is by purchase of more shares in their company.

One of the ways this is being done is by having the companies issue share warrants to the promoters. Another way is through share buy backs. When a company has enough cash resources, it could announce offer to buy back its shares. The floating stock of shares thereby comes down and this in turn increases the percentage of promoters' holdings. This would typically happen when the markets are in decline phase. In the latter part of 2009 the share markets have bounced back to much higher levels. The prices offered for buy back now turn out to be lower than the prevailing market prices. Hence these buy back programmes would be unsuccessful.

**Do give your feedback to us at < [dms.financial.services@gmail.com](mailto:dms.financial.services@gmail.com) >  
(web site: [www.dms-finance.com](http://www.dms-finance.com) )**

---

## Warrant conversion

- ❑ When the promoters exercise the warrants conversion, they get shares in the company.
- ❑ If they do not exercise the option to convert, they forfeit the opportunity to convert.
- ❑ When they therefore decide to consider converting they take into account the prevailing market price of the share, the price committed by them to convert and if the price prevailing is very high, it is economic to exercise conversion.
- ❑ If the price is not very different or the market price is lower than the conversion price, they may not convert depending on whether they will forfeit the minimum price paid earlier by them and whether that is still more economic.
- ❑ If the threat of a hostile takeover is strong they may decide to convert even if the market price is lower.
- ❑ Companies where promoters have converted the warrants ahead of maturity are:
  - Aditya Birla Nuvo
  - HCL Infosystems
  - Amtek Auto
  - Amtek India

The Table below gives the comparison of conversion price and market price:

Company	Acquirer	Qty(Lakh/Nos.)	Conversion Price (Rs.)	Present Day Price (Rs.)(27nov'09)
Amtek auto	Promoters	76	133	186
Amtek India	Promoters	59	41	49
Aditya Birla Nuvo	Turquoise Inv. & Fin.	23	541.19	806
HCL Infosystems	HCL Corpn.	150	152.9	146

- ❑ In the case of Amtek, there have been rumours of mergers within the group. Amtek The Board of Directors of the Company in their meeting held on July 08, 2009 had allotted 150,00,000 warrants convertible into equivalent number of equity shares of Rs 2/- each at a premium of Rs 131/- aggregating to Rs 199.50 Crores to the promoters group companies by way of preferential allotment.
- ❑ HCL Infosystems had raised Rs 472 crore by way of QIP and another Rs 320 crore would be coming from the promoters by way of subscription to warrants. The total is Rs 740 crore. This money will be used towards beefing up capabilities in service capability, in system integration, for working capital as well as for possible M&As to fill up certain gap areas.

- ❑ A lesser significant reason for promoters converting warrants is that the companies may be in need of cash for business purposes and the conversion generates that cash
- ❑ The trend in 2008 and early part of 2009 has been reversed. At that time the promoters had allowed the warrants to lapse as the market prices were at a steep discount compared the price of conversion making the investment unprofitable.
- ❑ In the process the promoters would stand to lose the initial contribution when warrants were allotted. Even this is a price they considered worth paying rather than opt for conversion.
- ❑ SEBI had earlier set a limit of 10% for upfront payment for allotment of warrants. Now this has been increased to 25%. This is to discourage promoters from issuing shares to themselves cheap when the markets are on a bull run, and later on, not convert when the markets decline. This norm has put pressure to promoters to proceed ahead with conversion.

\*\*\*\*\*

## **CONTAINER TERMINALS – FINANCING INDIA’S SUNRISE SECTOR**

***by Padmalatha S.***

Ports are a country’s strategic assets. The strong growth in world trade has been putting enormous pressure on governments to not only develop adequate port infrastructure, but also to improve services, and expand facilities to accommodate larger cargo flows..

At the same time, ports, once labor intensive, are becoming more capital intensive. Thus, evolution of new markets, services, technologies and regulations are gradually metamorphosing ports into integrated global logistics chains. The regulatory framework for ports should also promote the cost effective use of infrastructure and machinery, encourage decision taking by staff in their respective levels and enable port stakeholders to plan future investments.<sup>1</sup>

---

<sup>1</sup> 1999, ECLAC [Economic commission for Latin America and the Caribbean], “Port Modernisation: A pyramid of interrelated challenges”, United Nations

The global diffusion of benefits and the value of services provided by ports that transcend regional and national borders have brought to the limelight the need for large scale investment in this sector. However, public port authorities have not been able to measure up to these demands.

It is thus evident that there is a need for large scale investment in the ports sector, especially in container terminals. At present, the investment is being facilitated [a] by large private port service providers, who have grown increasingly global in scope and scale, and [b] through strategic alliances, both within the global shipping and the port services industry. Both these developments are bound to have far reaching impact on the financing, operation and regulation of ports in future.

## PORT SERVICES IN INDIA

India requires a huge investment in infrastructure of USD 475 bn at current prices, as estimated by the Planning Commission. Of this, about 15% would go to modernization and upgradation of highways, 20% to railways, and about 2% each to aviation and ports.

The proposed allocations reflect the growing importance of maritime infrastructure for the globalizing Indian economy. About 95% by volume and 70% by value of the country's international trade happens through ports.

In particular, the traffic projections at various major and other ports are as given in

**Tables 1A and 1B:**

**(It is noteworthy that while traffic at all ports is likely to grow at a compounded annual rate of growth [CARG] of 7.57%, the highest CARG is expected in container traffic – estimated at 17.3%)**

**Table 1A: Port traffic projections –major ports- 2011-12<sup>2</sup>**

(In MMT)

Commodity	Existing traffic 2005-06			Projected traffic 2011-12	
	Major Ports	Non-Major Ports	Total	Total	Major Ports
POL	142	75	217	378	215
Iron Ore	79	28	107	128	99
Coal	59	13	71	139	109
Container (Million TEUs)	62 (4.6)	4 (0.3)	66 (4.9)	170 (14.2)	144 (12)
Other cargos	82	32	113	194	141
Total	424	151	575	1009	708

Source: Planning commission documents

**Table 1B :**

**Port traffic projection- all ports- 2013-14<sup>3</sup>**

<sup>2</sup> 2007, "Report of the Task force: Financing plan for ports", page 5, The Secretariat for the Committee on Infrastructure, Planning Commission, Government of India

<sup>3</sup> 2006, "Report of the Committee of Secretaries- Road rail connectivity of major ports", page 5, The Secretariat for the Committee on Infrastructure, Planning Commission, Government of India

(in million tonnes)

Commodity	Existing Traffic in All Ports during 2003-04	Projected Traffic 2013-14	Compound Annual Rate of Growth (CARG)	Share of Major Ports 2013-14
POL	182.26	290.00	4.75%	191.2 (66%)
Container TEUs	51.00 (3.90)	251.40 (20.95)	17.30%	181.20 (15.10) (72%)
Iron Ore	75.62	131.50	5.69%	97.50 (74%)
Coal	58.63	135.90	8.77%	109.90 (81%)
Other Cargo	96.15	152.75	4.74%	126.04 (83%)
Total	463.66	961.55	7.57%	705.84 (73%)

*Source : Planning commission documents*

The growth in traffic as shown above necessitates huge levels of capacity addition, since almost all ports are heavily congested.

How much investment does this planned capacity addition at major ports require? The total investment is estimated at over Rs 57000 crore, of which, understandably, the bulk [about 58%] is aimed at Berth development. Spread evenly over creating container terminals, POL berths and other cargo berths, the investment is envisaged to be made almost exclusively by the private sector, under the PPP model. Taken together, private investment required in major and non major ports amounts to Rs 66743 crore upto 2011-12, translating to an average annual investment of about Rs 13300 crore.

What are the incentives for private players to participate in port services, especially container terminal development? Would the returns be commensurate with the risks of the projects? How would risks be allocated and mitigated? How would lenders to these projects mitigate their risks? These are the issues that would have to be looked at before the investment required becomes a reality.

### **RISKS FACED BY PRIVATE OPERATORS**

The private terminal operator typically carries two fundamental risks – completion risk [due to cost overruns] and revenue or market risk.<sup>4</sup> However, if the contract between the public authority and the private operator is clear and fair in its terms and content, the contractor would have to bear the construction risk completely. Containerization presupposes a seamless link with road and rail network ('end to end' transport system).

The estimated fund requirement for road and rail projects to be completed in respect of major ports amountS to Rs 7003 crore [Rs 8053 crore with 15% escalation built in, as assumed by the planning commission documents].

The risk-return tradeoffs as above are a likely explanation for the entry of large international players into the Indian market for setting up container terminals at major ports, as well as the increasing trend toward consolidation and convergence among the top terminal operators of the world.

However, in order to attract investors, the projects will have to be bankable and investment grade. Some innovative financing mechanisms that have been used in other countries include

- 'flexible match funding' - where the value of private contribution offsets the state's share

<sup>4</sup> 2007, "Port reform toolkit", 2<sup>nd</sup> ed, Module 5, "Financial implications of port reform", page 203

- reimbursement of bond financing costs by the state to private investors to ensure that they tap the markets to the full
- ‘tapered match funding’, where the state funding is higher during the initial period till viability is established
- partial conversion of advance construction- where the state may obligate funds for advance construction in a phased manner
- ‘green financing’, comprising of environment friendly instruments backing ecologically sustainable projects issued by the government, reinvested in strategic assets like port services.
- Subsidies and fiscal incentives for projects to improve cash flows
- Encouraging the development of vibrant corporate long term bond and derivatives markets to provide liquidity and risk mitigation to all capital providers
- Broadening the institutional investor base by allowing insurance companies and pension funds to bring in long term sources of funds and participate in infrastructure projects
- Fostering credit enhancement mechanisms such as monoline insurance so that lenders feel comfortable with the credit risk.

It is thus evident if private participation has to drive global competitiveness of Indian ports, financial, regulatory and legal reforms will have to happen simultaneously

\*\*\*\*\*

### **Services offered by DMS Financial Services Co. (P) Ltd.**

- **Outsourcing in the financial function**
- **Placement of human resources**
- **Training in finance, sales, operations and soft skills**

**For details, please contact Mr.Karthi on 044-24995672.**