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The article should be non-technical and should be within 1600 words. It should be typed in MS Word in Times New Roman 12 with paragraph spacing 1.5. Figures and simple, small tables can be incorporated. There should not be any notation or equation. Full forms of each abbreviation should be mentioned at first instance. Upto eight references can be included in the article. Limited number of short footnotes may also be included if necessary. Send your manuscript along with your name, designation, institutional affiliation, email ID and contact number to the editorial office at imikonnect@imi-k.edu.in mentioning the area viz. Marketing, Finance, OB & HR, Economics, Strategy, IT & Operations, Management Education and Others.

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Mergers & Acquisitions in India: Trends, Prospects & Challenges

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Mergers and Acquisitions (M&As) have picked up in the Indian market in the last decade. Here is an account of M&As, the trends, prospects and challenges from an expert from the industry.

IMI Konnect: *What are the trends in Mergers and Acquisitions (M&As) for Indian companies in the foreseeable future?*

BM: Tracing back to 2004 one may find that there were not too many deals in India on the M&A horizon, but the number of deals shot up during 2004-05 and that sort of set the pace for the M&A roadmap in India. The deals entered into over the last 7-8 years were predominantly in core sectors like steel, cement, telecom and the likes. In the current scenario, an increasing number of multinationals and external companies are looking at India with a lot of interest and I expect this trend to be on the rise dramatically in the next few years. There are several reasons behind this thought process.

Firstly, a lot of the Indian companies have strong balance sheets in terms of reserves and cash surpluses and they are under pressure from shareholders/stakeholders to deploy the cash efficiently. Secondly, the capital markets are in good shape and external funding is not too difficult to come by in recent times with the interest rates coming down. Third, a lot of these market players are looking at volume consolidation. Therefore while considering Greenfield (organic growth) vs Acquisition (inorganic growth) routes, the Greenfield approach is considered to be a more difficult option with a longer gestation and painstaking in terms of obtaining new licenses and new approvals. Thus, many companies today would prefer to consolidate through the acquisition route. Furthermore, a lot of the big private equity players are coming in from the overseas market viz. KKR and Black Stone. They have been looking into the Indian market closely and their deal books are on the rise in India.

IMI Konnect: *Yes, there was a marked increase in M&As during 2005-06 in the Indian Market. However, after the recession in 2010, it has slightly come down. What according to you may be the reason for this substantial increase?*

BM: There have been no major policy changes as such that led to such a fillip. However, there were some big deals or mega acquisitions viz. Tata Steel's acquisition of Corus, Hindalco's acquisition of Novelis, Jaguar Land Rover's acquisition by Tata motors that led to such growth. If these big sized deals are taken out, the growth is not that significant. Not too much has been done in opening up except the fact that capital inflows have been easier to handle and as India is becoming more global, the companies are having an appetite for growth and are willing to carve out a niche for themselves on the global front.

IMI Konnect: *Is it necessary for the target firm to have a healthy financial position to become an attractive proposition for acquisition?*

BM: The rationale for acquisition is always the key to an acquisition. The acquirer reviews his own strategy in terms of portfolio gap, access to new markets, new manufacturing capabilities, project management resources, technology, or even R&D facilities, possible revenue and cost synergies etc. before engaging in further discussions with the target. There has to be a clear rationale for the acquisition based on above factors and as to what the target has to offer. Sometimes acquisitions are also made to safeguard the acquirer's competitive position against his major competitors.

Therefore, it really does not matter whether a target firm has healthy financials or not, simply because when a deal is entered into, the focus is not on whether the past financials of the company are healthy and/or the financials for the next five years are encouraging. The financial position of the target impacts the valuation and has not so much to do in pushing the deal through. Therefore, the financial position of the target by itself is not an attractive proposition for acquisition, it can only sweeten the process once, in the negotiation phase.

IMI Konnect: *In India, do you think the objective is to make an entry into a new market or the like?*

BM: What happens is normally most acquisitions are in related areas, their core businesses, something which they are comfortable with including forward and backward integration. Companies in general stick to their core and do not like to experiment into unrelated areas through the acquisition route. This is the trend seen in most of the deals.

But it may be different for private equity players who are in this market as a different business model and are focused on making investments, taking management control, turning around companies and divesting them at a profit. While buying into a venture, their objective is to get a return on investment in the quickest period possible, (more like a banker's perspective). So, the objectives do differ.

IMI Konnect: *It has been observed that the strategy of power sharing in a merger does not work well and the merged company ends up having one top manager. What makes this an ineffective strategy?*

BM: "Power sharing" generally happens more in a merger of the equals where each one wants to have his way and this more often than not leads to issues in managing.

A merger of equals poses extreme challenges in making things work. There will be issues on co-managing, issues with respect to equal rights and representations, diversity in formation and culture. The issues start arising right from composition of Board of Directors, who has the majority, appointment of CEO and CFO, implementing policies, getting things done through board resolutions, organization structure etc. Over a period of time taking the business forward becomes a challenge as additional bureaucracy sets in. In this process, planned synergies which possibly were the basis for the deal get diluted and over a period destroyed. So in reality in case of such mergers, after a brief period one party will want to exit and sell his stake.

IMI Konnect: *How are the employee issues addressed after a merger and an acquisition?*

BM: The employee issues are possibly the most important aspect of any M&A and also the most overlooked or "taken for granted" or underestimated!

Global surveys done throw up a trend that 8 out of 10 deals do not deliver the expected value due to the inefficient handling of such issues. The synergies are threatened with depletion in people's morale and productivity as well as attrition in human resources.

In such situations post the acquisition, communication of the business rationale behind the acquisition to the employees is very important. HR is expected to play a key role along with the new management in communicating, hand holding and explaining the necessities and threats. Secondly, it is very important to set up a dedicated integration team after the deal. In any acquisition at least 20-25 percent of the positions of the top and the middle level of the target get endangered. The emphasis will therefore be on how to keep the morale and productivity high in such a situation and also when the cultural integration takes place. Finally it is the financial part, i.e., employee compensation, that calls for a lot of detailing and special attention, in the initial 3-12 months post the acquisition. This involves looking at the job descriptions, profiling them into the new set up, mapping and restructuring the grades and emoluments. Some people having higher designations could land up with lower ones. Again people earning less, may be put into a bigger structure, on account of mapping into the new grade structure. So there will always be some winners and losers.

IMI Konnect: *There are cultural issues too. When Tata Tea acquired Tetley in Great Britain, they faced a lot of problem with the people who were already working in Tetley. What are the other related challenges in case of a cross border acquisition?*

BM: We have also experienced such issues here. In case of overseas/cross border acquisitions related to employees, one key topic is long term employee obligations in terms of retirals, pension funds etc. They impact the valuation significantly, and one will find that there are a lot of contingent liabilities relating to these aspects included in the balance sheet, which need to be honored post the acquisition. As mentioned above these are basically the long term benefits in terms of superannuation, provident fund and pension funds. These can be very difficult to handle as they have a major impact on the cash flow and changing this is not an easy task. Therefore, it's a major concern in case of an off-shore acquisition especially where you have blue collar workers.

IMI Konnect: *What are the challenges faced in restructuring the departments, personnel and practices within the newly merged company?*

BM: Let's take an example. Suppose, when a manufacturing company is acquired, the first challenge will be on how to integrate the various departments viz. HR, finance, sales, operations, legal etc. into the corporate structure of the newly formed company. The acquirer and the acquired will have their own departments with their respective heads. If both companies are situated at the same location, and one is looking at cost synergies and optimization, these will become major challenges.

The sales and marketing side too needs a lot of detailing and a lot of thought goes into it. On top of that the HR issues need to be handled with care. Basically the acquirer has to look at the organization chart, the structure, the competence and all these have to be carried out gradually. There is no universal formula for this.

IMI Konnect: *What are the possible deal breakers in case of an acquisition or a merger? How are such issues settled?*

BM: The target has a perception of his own business and the price that it expects. So a major deal breaker can be the difference in the expected valuation and what the acquirers are willing to pay. Secondly, legal issues like some regulatory approvals may pose a serious problem on account of the acquirer becoming a dominant player, or cartels being formed, or deals against public interest etc.

Again, at times the financing of the deal does not go through as expected. The target gets impatient and calls the deal off.

Valuation of the deal from the acquirer's perspective is often impacted by the fact that the entire business of the target company may not be attractive to the acquirer. For instance, when the target has three businesses, one business may be very interesting for the acquirer, so he will give a bump to the valuation upwards; but the one he does not want, will be quoted at a discount; the final one may be just okay with no real synergies and to the acquirer it is not going to make a difference but he can do with it and thus, the overall valuation considers all these aspects. The target would never be satisfied with this cherry-picking attitude of the acquirer and sometimes this can also be a deal breaker. Another possible deal breaker can be the Earn-out model. Earn-out is a pricing mechanism in M&As where the sellers have to earn a part of the purchase price based on the business performance following the acquisition. Under these circumstances, the buyer will have to ask the seller to control the company for the first 5 years and deliver the committed revenues or profit targets (reflected in the projected five year financials shared during the negotiation phase) so as to earn the expected price. The Earn-out model is still not so popular in India, it is more of a western concept.

IMI Konnect: *How is the financing of a Merger or an Acquisition undertaken?*

BM: Financing may be done through either an all-cash/part cash deal with share swap. Essentially it is financed by debt, equity and internal accruals. One may also get some equity funding. A lot of the Indian companies are also tapping overseas funds at present on account of attractive interest rates.

IMI Konnect: *Are there any differences in the trends in M&A observed in India vis-à-vis the rest of the world?*

BM: Not really! As I mentioned the only difference is the Earn-out model. Earn-out model is quite popular in the western world but rare in India. In India the methodology is that the acquirer would like to take over full control from day one! The acquirer would not want any interference or a two way split or a transition model where for the first 5 years someone else runs it. This is more of a cultural mindset.

Crowdfunding for the Indian Startups and SMEs: A Need of the Time

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According to the United Nations, India's population stood at 1,326,801,576 in July, 2016. Not only that, India is projected to be the world's most populous country by 2022, surpassing China. It is estimated that by 2050, its population will be reaching 1.7 billion. In the political history of the entire mankind, India is thus, expected to become the first entity to be home to more than 1.5 billion people. Importantly, about 12 million people join India's workforce every year while the number of new jobs in offer is much lower. And this situation is expected to continue in the foreseeable future. So, when employment generation is the issue, India should be a top taker of any good advice. No wonder, to assist that cause, clearing the ways for crowdfunding for individuals, startups and Small and Medium Enterprises deserves the attention of the appropriate Indian authorities.

As a concept, crowdfunding is a way of raising capital which entails the use of internet or social networking sites or even some dedicated websites. Under this process, one party is "financing a project by requesting and receiving small contributions from many parties in exchange for a form of value to those parties. Crowdfunding connects investors with small business startups and projects through an online transaction portal that removes barriers to entry" (Patnia, 2013). At the practical level, a number of models have evolved for crowdfunding including lending model, reward model, equity (investment) model, donation model, loyalty model, etc.

Though the term crowdfunding is relatively new but this method of financing has been in practice in India for a long period of time, much before the term was coined, for various social and religious works. Once, the small but growing textile business of Dhirubhai Ambani, the founder of the Reliance Industries, was crowdfunded by communities across the Indian state of Gujarat. More recent examples of attempts of crowdfunding for initiatives like the 'Goa Project' and campaigns like 'Teach for India' could also be mentioned. Also, for the Indian film industry, crowdfunding is slowly becoming an alternative funding channel.

However, at this stage of rapid economic transition, encouraging and structuring a strategy for crowdfunding as a regular source of finance for startups and SMEs could play an important role in technology development and employment generation in India. As we can see, SMEs are still very much relevant to the Indian social and economic context, but access to capital market for finance remains a serious roadblock for them. Moreover, as a growing and vibrant nation, more and more ideas are expected to come from the people in the future. Thus, providing an additional channel to many of them for early stage funding could see a burst of entrepreneurial activities in the economy.

As a source of financing, however, the size of crowdfunding in India has remained small so far. The primary reason for this is that its crowdfunding has been restricted to micro-financing category projects and the occasional donation-reward funding category. Crowdexpert.com gives an estimate that in 2015, a total of US$ 34 billion has been raised worldwide through crowdfunding. In that, China has emerged by far the single largest market followed by the USA, the UK, France and Japan. Statista (2017) predicts India to be a growth market in the near future. The transaction value of crowdfunding is expected to reach US$16 million in 2021. Meanwhile, a number of crowdfunding sites have emerged in this segment of capital market, e.g. Bitgiving, Milaap, Ketto, Start51, Fund Dreams India, WishBerry.in, Catapooolt and so on. Small brands, healthy snacks, ethnic foods, small clinic, real estate, etc. could be some of the areas where crowdfunding may find space. However, from the perspective of the Indian 'crowd', sources of finance such as funding, lending, equity investment and reward models may have a higher chance of succeeding.

But there are some obstacles to the promise of this financing method. Lack of awareness, lack of confidence on the net based functionality, absence of any financial promises to the contributors by the crowdfunding platforms, etc. are some hindrances in building the level of confidence needed for a healthy growth and development of the sector. Moreover, no crowd-funding regulation exists in India so far. The Securities and Exchange Board of India (SEBI) has released only a consultation paper that speaks about the need for regulations. To be sure, the Indian entrepreneur community needs an Indian version of crowdfunding platforms like Kickstarter, Indiegogo to help startups and individuals to launch a product as well as to test the acceptance of the product in the market. Without a proper legal backing this may not be expected to happen very soon. However, by looking at the potentials of unleashing innovation, business creation and employment generation, the Government of India should take steps to pass the necessary regulations soon for regularizing crowd-funding for the relevant sectors. It, probably, is a need of the time.

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IPO Underpricing in India

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Introduction to Initial Public Offer (IPO)

In the area of finance, the concept of going concern and profitability of a firm plays the most important role in investment decisions. Hence, the objective of any firm is to sustain through its core operations and remain profitable over time for the stakeholders (specifically to shareholders). A growing business needs money to invest and that can be generated from various sources of funds such as owners' capital, outside equity, debt, or many other forms. Apart from owners' capital and retained earnings firms usually raise money from outside market through different ways such as private placements, venture capital, loan, issuing debt or equity. Sometimes traditional sources of finance (owners' capital, debt and retained earnings) are also not sufficient to finance the company due to rapid growth or higher cost. Rock (1986) stated that one important motive of the firms behind going public is risk aversion of owners as risk is shared limitedly among owners and financial backers of publicly listed companies. Thus, one important mode of raising fund is to go for Initial Public Offer (IPO). IPOs are most popularly used to raise funds from the market for the purpose of investing in a project, promoting a new venture and diffusing ownership through listing on the stock exchange. Loughran et al (1994) found three different mechanisms of such offerings across different countries: fixed price offers , auctions and book building. Sherman (2005) suggested that book building is a superior method compared to auctions and it is also a less risky process as the underwriter ensures the participation of a minimum number of informed investors.

IPO Underpricing

IPO underpricing, basically, is the difference between the closing offer price of a stock (through IPO) and the closing price of the same on first trading (listing) day if the listing price is higher. Naturally, it provides a short-term investment opportunity for the investors. Hence, a huge rush of firms towards listing on stock exchange and generating funds through IPO is also trademarked with a large queue of investors waiting for IPO allotments, development of regulatory framework and growth of investment banking in the domain of primary market. These unique characteristics have made IPO underpricing an interesting event to study in finance.

A firm announces the IPO or an offer to issue new equity to the market by disclosing necessary information about the background of the firm, its prior financial performance, the purpose behind such an offer and future prospects along with the risk. This risk may be of investment in risky project or may be of non-allotment of shares due to oversubscription and such risk needs to be compensated in some way. It has been observed that most IPOs, generally, are traded on higher price on the listing day. Therefore, the firm is encountering an opportunity loss and it could raise more money by offering higher price which actually it didn't. It evinces that the investors have different beliefs about the future prospects of the company i.e. the firm has been valued wrongly and it deserves a higher price. The higher the amount of underpricing, greater is the money the firm could generate through the higher price offer, but firms have lost that money. This particular incidence is coined as 'money left on the table' by the issuers (Pande and Vaidyanathan, 2009).

Why Underpricing?

In academic literature, various factors have been considered as the potential reasons for IPO underpricing. The most prominent among them is information asymmetry. It can be present at two levels: a) between the underwriter and the issuer (Baron, 1982; Muscarella and Vetsuypens, 1989); and b) between the uninformed and the informed investors (Rock, 1986). Besides, there are some other factors which play a significant role in IPO underpricing. One such factor is the age of the firm. It has been empirically found that over-subscription occurs for older firms as the investors possess higher confidence in the prospects of the older firms (Reside et al, 1994; Shelly and Singh, 2008). This results in higher IPO underpricing. In similar lines, different studies revealed that the higher reputation of underwriter leads to over-subscription of new issues which in turn causes higher underpricing (Chemmanur and Fulghieri, 1994; Shelly and Singh, 2008). The nature of industry to which the firm belongs is another important aspect in this regard. Researchers indicated that there is a significant difference in level of underpricing between natural resource firms and non-natural resource firms (Ritter, 1984) and between financial and non-financial firms (Alli et al, 1994). The most possible reason behind such finding is the requirement of greater regulatory disclosures for the natural resource firms and the financial firms. It reduces information asymmetry in the primary market for these firms and subsequently results in lower underpricing. Shah (1995) found that listing delay (time between day of offer and listing) causes higher underpricing due to increase in information asymmetry and risk of rationing.

The Indian IPO Market

While studying the nature of IPO underpricing, we find the Indian market to be more interesting as compared to other markets due to few of its unique characteristics such as constrained access to debt, concentrated ownership and prevalence of family owned businesses. In spite of that, Indian market is comparatively efficient and well equipped with technology now just as other markets are. India is the first country in the world to introduce the concept of equity rating (Pande and Vaidyanathan, 2009). The Indian primary market is having a different regulation history, a special kind of institutional investment, the sheer size, large number of firms going for listing and the large number of retail participants applying directly. In India, an IPO is also rated prior to listing on the basis of the disclosures made in their prospectus, not on the basis of quality or valuation of the issue. Although this rating does not tell anything about the issue and the firm, it serves as a signal to the retail investors in the market. The only limitation of the Indian market is the data availability within a short span of time.

The Indian IPO market has grown rapidly with economic liberalization of 1990s. The regulatory body named the Controller of Capital Issues (CCI) was abolished and after some time in 1992, the Securities and Exchange Board of India (SEBI) was established as the monitoring body of capital market in India, which gradually became powerful over time. Prior to 1990s when CCI was in existence, companies with substantial reserves only could issue shares on premium. This rule has been changed by SEBI in 1992 and companies can issue shares on premium if they are generating a profit for the last 3-5 years or if the promoting company having 50 percent post-IPO ownership has the same record. During CCI, the "CCI Formula" was used to calculate the fair price of equity on the basis of book value using accounting information and that often led to extreme low prices; hence debt was a more preferred choice than equity (Shah, 1995).

Even post liberalization, studies conducted in Indian stock market reported higher level of IPO underpricing. Singh and Mittal (2003) found that this phenomenon of IPO underpricing persists in India with an average of 83.22 percent between 1992 and 1996. Shah (1995), using the data of 2056 offerings listed on BSE during 1991-1995, stated, "the listing delay is positively related to underpricing to the extent that the issuing firm earns the interest rate float on the application money, and to the extent that investors lose liquidity on their application money, they must be compensated for it by enhanced underpricing." Karmakar (2002) computed the initial return of Indian IPOs which was abnormally high (289 percent) and much higher than the average initial return of other developed countries. Sahoo and Rajib (2009) reported an underpricing of 46.63 percent for the period 2001 to 2005. Ansari (2006) observed the same to be 40.9 percent for IPOs during 2005.

Reforms Concerning IPOs

In view of transforming the Indian IPO market and making it more competitive with the world market, SEBI changed listing guidelines from time to time during the decade. The process of going public in India is almost similar to that in other developed countries, i.e. filing draft prospectus first with SEBI, getting it through with eligible investment bankers and then filing to the Registrar of Companies. The change in the regulatory environment reformed the Indian primary market which resulted in huge rush toward going public. Some of the major implications are: a) The offer price is chosen by firm and merchant banker, not using any fixed formula; b) Approved offer price by SEBI can be increased by 20 percent to adjust listing delay effect; c) Marketing of IPO is increased widely to appeal to a large number of investors; d) The issue usually closes within 4-10 days and listing delay is also reducing gradually.

Post such reforms, Ghosh (2005) found that the underpricing in Indian market is relatively lower than the international markets. Pande and Vaidyanathan (2009) also spotted an improvement in valuation of IPOs as the level of underpricing has decreased over time in the study of 55 firms listed on National Stock Exchange (NSE) during the period March 2004-October 2006. They observed that if the final price of offer is fixed at closer to the higher side of the band then it serves as a signal for good quality and leads to higher underpricing, which supports the study of Benveniste and Spindt (1989). More recent studies, e.g. Brooks et al (2014) stated that the IPO underpricing in Indian market has been lowered significantly.

If we try to explore the reasons behind such improvement in Indian IPO market, few activities that reduce potential asymmetric information come into the picture. Most importantly, the mandated IPO grading which has not only reduced the level of underpricing but also acted as a signal for potential investors. Apart from that a sequence of activities such as the regulated book-building process, presence of unregulated IPO grey market (over-the-counter market prior to auction and listing), availability of analyst's recommendation and disclosure of group affiliation have contributed significantly to reduction of IPO underpricing.

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Does Cash Dividend Influence Stock Returns in India?

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Introduction

Corporate cash dividend announcement and its impact on share prices has been one of the active and prominent areas of research in finance literature. This is so because the existing literature has more puzzles than answers. The important question of why companies pay cash dividends when these are often taxed more heavily than capital gains has puzzled researchers for several decades. Dividend announcement is considered to be an effective mechanism to signal the market about the confidence of the management on firm's profitability and future growth prospects.

Dividend Distribution in India

Earlier, in India, dividends were taxed in the hands of the shareholders only. But after the introduction of Corporate Dividend Tax (CDT) in the Finance Act 1997, Indian firms are required to pay a corporate dividend tax to the Government (presently the effective rate of CDT is about 20 percent) before they pay cash dividend to their shareholders and such dividend is a tax free income to the shareholders. However, investors need to pay additional 10 per cent tax on their total dividend, if the amount of dividend received exceeds ₹ 10 lakhs in a year. Hence, at present, shareholders get lesser amount as dividend because the firm has to pay a portion of the amount to the Government as CDT. As a result, shareholders may not like cash dividend and instead they may prefer ploughing back of their profits into the firm as this may favourably influence company's share prices and shareholders enjoy the capital gain, which is more tax effective to the investors (for short term capital gain, the tax rate is 15 percent and for long term capital gain the tax rate is zero). This raises the important question as to whether the investors prefer cash dividend at all in India.

Corporate Sector in Developed and Developing Economies

Several studies have examined the relationship between cash dividend announcements and stock returns, majority of them are based on developed economies and their findings may not be applicable in the emerging market economies like India. There are some important issues that are quite different for the emerging markets compared to the developed markets. At present, the rate of growth in the corporate sector is much higher in the emerging economies compared to that of the developed economies. The corporate sector in many emerging market economies, like India, is characterized by high ownership concentration, arising from the dominance of family business groups and an imperfect capital market. In India, the majority of the industrial landscape is dominated by family business houses where the family members often occupy the key managerial positions in businesses. As a result, managerial perspective of corporate payout policy in family business houses will be different from that of firms which are characterized by wide spread equity model. Moreover, the role of imperfect capital market is an interesting issue in the context of dividend announcement policy of firms.

Cash Dividend and Stock Returns

Saravanakumar (2011) finds that investors do not gain significant value in the pre-announcement period as well as surrounding the announcement day. However, dividend announcements can give value in the post-announcement period. Maitra and Dey (2012) find significant abnormal returns (positive or negative or both) upon dividend announcement which is more evident under the CAPM model. Chatterjee and Dutta (2017) have studied 210 dividend announcements of Indian companies and following are the findings from the study: a) An increasing trend in the amount of average cash dividend payment is observed during the period 2010 (₹ 9430 million) to 2014 (₹ 16418 million); b) The dividend payout ratio ranges between 26.81 percent and 38.50 percent over the period 2010 to 2014 and shows an overall upward rising trend; c) Overall, no empirical evidence behind the existence of significant abnormal stock returns around dividend announcements is observed in the National Stock Exchange of India Ltd. This finding is contrary to the findings of many other studies based on the data of developed economies (e.g.: Allen et al., 2000; Guay and Harford, 2000); d) Just after the dividend announcement, large payout firms experience greater abnormal stock returns compared to the smaller payout firms; e) Stock returns following dividend announcements in India do not vary across firm size.

Conclusion

Overall, it is observed that dividend announcements in India do not carry much information to the investors. The reason behind this could be that the investors are more interested in capital gains. It is the increase in share price that actually motivates investors to invest in shares rather than just receiving cash dividends from the companies. The relative tax disadvantage associated with cash dividend may be the underlying factor behind such type of preference for capital gains. Managers should realize that paying regular cash dividends may not necessarily increase stock prices.

Ownership structure of the Indian firms may be another factor explaining this finding. Ownership structure of the Indian firms is distinctively different from those in the developed markets and there exists high ownership concentration in India. This can be observed in Table1, which shows that the average aggregate shareholding of the promoter and non-promoter institutions over the period 2010 to 2014 is as high as 86.14 percent, while, the average shareholding of the non-promoter non-institutions is only 13.59 percent during this period. Majority of the listed firms are owned by the founding families and institutional shareholders who do not trade actively. As a result, share price reactions may not fully reflect the impact of dividend announcements. Promoters as well as the institutional investors put more importance on capital gains and not on cash dividends.

Table1: Average Shareholding Patterns of the Sample Firms from 2010 to 2014 (in %)

Year	Promoter	Non Promoter Institution	Promoter + Non Promoter Institution	Non Promoter Non Institutions	Total
2010	55.80	30.05	85.85	14.15	100.00
2011	53.81	32.20	86.01	13.99	100.00
2012	52.88	32.89	85.77	14.23	100.00
2013	52.92	33.43	86.35	13.65	100.00
2014	52.61	34.12	86.73	13.27	100.00
Average	**53.60**	**32.54**	**86.14**	**13.59**	**100**

Source: *Based on sample data of Chatterjee & Dutta (2017)*

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India's New Fiscal Roadmap

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The global economy is passing through a new phase of politico-economic uncertainty. This includes productivity shocks and changing pattern of global integration with several other major transformations. Given such circumstances, public policy takes an increasingly important role that can re-shape and re-design incentives to facilitate these transformations. In order to boost the domestic productive activities the government needs to provide infrastructure and a conducive business environment and at the same time, make the growth more 'inclusive', which needs special emphasis on schemes and social programmes that are job-intensive in nature. But, burgeoning government expenditure on account of subsidies, loan waivers, pay commission rewards and a number of large legally backed schemes have constrained the fiscal space. Felt as the need of the hour, the government enacted a fiscal consolidation act long back in the early 2000s. But to keep the pace of our fiscal reforms in sync with the rapidly changing global and domestic scenarios, some refinements in the fiscal consolidation became necessary.

Accordingly, the central government constituted the Fiscal Responsibility and Budget Management (FRBM) Review Committee (N. K. Singh committee) in 2016 that has reviewed the existing fiscal rules and the FRBM Act 2003, and have come up with a number of recommendations. Since an efficient and smooth transmission mechanism necessitates complementary and accommodative regulatory reforms, it is quite understandable that financial and monetary sector reforms cannot be undertaken on a piecemeal basis. In the last couple of years spanning from 2014 till date, India has undertaken drastic regulatory reforms in the monetary and financial sector viz. formation of Monetary Policy Committee (MPC) with amendments in the archaic RBI Act 1934, adoption of inflation targeting, proposal to form a separate Public Debt Management Agency, drafting of Indian Financial Code, Goods and Services Tax (GST) bill, to mention a few.

Where Does India Stand at Present?

The International Monetary Fund (IMF) in its country report of 2017 has mentioned that India still remains one of the fastest growing emerging economies. Although concerns remain over the recent disruptive phase of cash shortages triggered by demonetization (nevertheless, another structural policy intervention). This gets reflected in the IMF's downgrading of growth forecasts to 6.6 percent for the fiscal year 2016-17 and to 7.2 percent in 2017-18. On the development front, India has made appreciable progress on achieving the Millennium Development Goals of halving poverty, infant and child mortality, and maternal mortality rates. Significant progress has been made in financial inclusion and leveraging technology.[1] As policy recommendations IMF has suggested structural reforms for the Indian economy,

[1] http://www.imf.org/en/News/Articles/2017/02/21/NA022217-For-India-strong-growth-persists-despite-new-challenges

which includes labour market interventions and complementary regulatory reforms, to correct the labour market rigidities and high level of informalization. In the recently released Fiscal Monitor 2017[2] IMF has predicted a modest improvement in the fiscal deficit during 2017 and 2018 (6.4 percent and 6.3 percent of GDP respectively), consistent with a gradual fall of the same from 2010 to 2016. Notably, this is an improvement from its earlier prediction of 6.6 percent in 2016. On the debt front, it predicted the general government debt would be 67.8 (percent of GDP) in 2017 and 66.1 percent in 2018, a reduction from 69.5 percent predicted last year. The IMF praised the FRBM review committee's recommendation of anchoring debt-to-GDP ratio to 60 percent by 2022-23, which, with specific timelines, was never targeted before by the extant FRBM rules.

Statement of the recently held meeting of Monetary Policy Committee (MPC) on April 5-6, 2017[3] too shows an optimistic scenario for the Indian economy, and that is reflected in the MPC's decision to take a neutral stance in the monetary policy. Gross Value Added growth for instance, is projected to strengthen to 7.4 percent in 2017-18 from 6.7 percent in 2016-17. Headline consumer price index (CPI) inflation is projected to undershoot the target of 5.0 percent for Q4 of 2016-17 and for 2017-18 inflation is projected to average 4.5 percent in the first half of the year and 5 percent in the second half. It mentions the possibility of risks emanating from increasing pressure on the general government's expenditure due to 7th Central Pay Commission award commitments, farm loan waivers etc., which will add to the general government's deficit, which is already quite high as compared to other emerging peers, and poses risk for the inflation path.

FRBM Review Committee Recommendations: What's New?

Starting from its enactment in 2003 following a sustained widening of the fiscal deficit in 1980s and early 1990s, the FRBM Act has undergone multiple amendments. Nonetheless, it is notable that following the FRBM enactment, India achieved a more disciplined fiscal path in mid 2000s. But this got disrupted by the suspension of FRBM Act post-2008. This was characterized by highly unstable macroeconomic environment which reached its peak in 2013. Therefore, the new FRBM rules, with a little "quantitative" tweaking, appeared in 2013 via an amendment in the Finance Act 2012, though the heart and soul remained the same.

The FRBM Review Committee, constituted in May 2016, submitted its report on January 2017 (report made public in April 2017). The committee felt the need of fiscal adaptation and adoption of new generation "smart fiscal rules" with the dramatic changes in the global economy and India's increasing financial integration (for example, capital and portfolio flows have shown new heights). The committee has recommended a repeal of the FRBM Act 2003 and adoption of Debt and Fiscal Responsibility Act. Following a Debt Sustainability Analysis the committee chose a 60 percent debt target (40 percent for Centre) to be achieved by 2022-23, which will automatically lead to the fiscal correction and hitting the fiscal deficit target of 2.5 percent in FY 2023. It needs to be mentioned here that the FRBM Rules 2004 had

[2] https://www.imf.org/en/Publications/FM/Issues/2017/04/06/fiscal-monitor-april-2017

[3] https://rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=40224

also prescribed targets on annual accumulation of debt that the Central Government shall not assume liabilities (including external debt at current exchange rate) in excess of 9 percent of GDP in 2004-05 and in each subsequent year, the limit of 9 percent shall be progressively reduced by at least 1 percentage point of GDP. Hence, the new debt obligation, which is a "terminal" target, as distinct from an "annual" target that was already existing in the FRBM Rules, is like serving old wine in a new bottle.

Many of India's emerging peers who are doing very well on the fiscal front, have adopted the so called "new generation rules", which incorporate setting up of Fiscal Council that will make an independent analysis and forecast, and will serve as an advisory body to the government. Also, making escape clauses well defined to increase the credibility of the fiscal consolidation exercise and reduce its mis-use, the committee has recommended for both - constitution of Fiscal Council and strengthening the definition of escape clauses. The procyclicality of fiscal deficits, which are typically observed in developing countries, needs suitable correction to better understand the true fiscal stance of government. When growth is high tax revenues are higher (due to the cyclical component), implying lower fiscal deficit, although there is no change in the government's "discretionary" expenditure. Typically, governments in developing countries do not cut expenditures during this "good" time, which is perceived to be an un-populist measure. Instead, the fiscal space that is being created by the "cyclical" component of growth, should be preserved (saved) or used for expenditures that are less populist, yet provide higher longer term returns (for example, capital expenditure, infrastructure). To assess government's true (discretionary) fiscal stance, that eliminates movements in the deficit numbers due to movements in the cyclical components, many countries have started reporting government's "cyclically adjusted deficits". Therefore, many countries have adopted cyclically adjusted deficits. The committee however, came to a consensus that though its significance is commendable, operationalization is very difficult in the Indian context. The committee emphasized on institutional reforms such as fiscal transparency following global best practices, to facilitate the fiscal reform and its impacts. Last but not the least, the committee acknowledges the strengthening role of state finances, as revealed from several issues such as a quantum jump in the tax devolution proposed by the 14th Finance Commission and higher state expenditure as compared to the centre (as percentage of Gross State Domestic Product). Therefore, it was recognised that states' fiscal policy roadmaps are equally crucial to meet the medium term fiscal targets and bring long term fiscal discipline in India.

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