In This Perspective

It is with a tremendous sense of satisfaction and pride that we present the first Technopak Perspective. This quarterly publication is a collation of our current research and thinking covering the industries of Retail, Consumer Goods, Fashion, Healthcare, Hospitality & Tourism, Education and Food & Agriculture. In this maiden issue, we cover a number of areas that business leaders will be interested in, including strategy, consumer insights, marketing, M&A, industry overviews, and human capital management, amongst others.

Understanding and tracking the Indian consumer lies at the heart of our work. We present Nine Consumer Trends in India for 2009. We look at how consumer attitudes and preferences have changed as a result of the economic slowdown. What opportunities and challenges does this shift in attitudes and preferences bring to firms and their marketers?

Modern retail in India has seen its most challenging 12 months yet. In a piece titled The Indian Retail Landscape: Now and Beyond we look at how modern retail’s landscape is changing and what we can expect in the near term. We analyze how some retailers are entering the rebuilding phase with a focus on resizing, relocating, restructuring stores. We look at the impact of consumer product companies investing in traditional retail, outline the emergence of collaborative models in retail real estate, and define the required focus on retail back end and supply chain.

India’s textile and apparel industry has various inorganic cross-border opportunities to grow and maximize shareholder value. In Riding High on the Back of Inorganic Growth, we review how firms can take this path, what the attractive M&A destinations are, the process for approaching M&A deals, and present some case studies.

A Capsule on Healthcare Trends examines key trends that will change the face of India’s healthcare sector and present some future scenarios – growth led by public-private partnerships, corporatization of medical education, emergence of healthcare cities, designing cost-effective infrastructure, new partnership models for healthcare delivery and lastly, standardization of clinical protocols.

Two brief industry reports on India’s Hospitality and Food & Agriculture sectors cover various aspects of these industries’ evolution phases, growth drivers, emerging trends, challenges and opportunities.

Our Report Card on India’s Education Sector presents the financial potential in this sector for private investments. We project emerging demand supply gaps in higher education and the likely mismatch between stream wise development of seats and the needs of the country.

The past 12 months have been particularly hard on the job market, and especially for those best qualified. The article on Managing the People Impact of the Slowdown in Consumer and Service Industries talks about what the economic slowdown means for employers, employees and job seekers and what strategies should they have in place in these trying times.

This first issue of the Perspective aims to provide insights across a range of consumer industries in India. Our firm has come a long way since we started out in 1992 as a textile industry focused marketing consulting firm; and here’s to the many more milestones in the future! We look forward to your feedback.

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The Need for a Marketing Stimulus

This article appeared in the Business Standard on March 26, 2009

Across most of urban India and particularly in the major metros, there are now clear signs of a lowered consumer optimism and declining confidence leading to the deferment of consumer spending. This deferred or reduced spending is now extending across most major consumption sectors such as discretionary food and groceries, clothing and home textiles, consumer durables and home appliances, jewellery, furniture and furnishings, leisure travel, and entertainment.

Oddly, the response of many manufacturers, marketers and retailers has been counter-intuitive. While most of them tried to stimulate consumer demand in the last quarter of 2008 through aggressive discounting and promotional activity, the same enthusiasm is not so visible in the first quarter of 2009. It is, therefore, no surprise to observe very substantial decline in customer traffic in shopping high streets and malls. It is unlikely that there is going to be any further external trigger leading to an upsurge in consumer sentiment, and with the onset of the summer and summer vacations, there is going to be a further attrition in consumer’s intentions to spend on discretionary goods and services. Hence, in such an environment, it is extremely crucial for manufacturers and retailers to think harder and more innovatively, and then launch their own “marketing stimulus” efforts without any further delay.

In these times of already dented sales growth and reduced margins, the temptation to preserve further erosion of prices and margins is understandably high. For listed companies, already reeling under drastically reduced valuations of their equity, the announcement of financial results that reflect further reduction in their gross margins may put further pressure on the performance of their scrips on various bourses. Hence, there would also be pressure on marketers from their Board Members and Chief Executives to shore up the margins rather than undertake any further price reductions or additional sales promotional activity. This is already visible in the steady creeping up of prices, notwithstanding the recent reduction of Cenvat rates across the board, including automobiles, airfares, hotel room tariffs and new summer clothing ranges. In some instances, the fig leaf of justification is the weakening of the rupee while in others, it is the increase in input costs even though in most cases the input costs have actually come down. Nothing can be more dangerous for such companies since any further sharper fall in consumer spending is bound to be highly damaging to the top lines of these businesses and lead to a collapse in the bottom line immediately.

The reassuring factor for the marketers and retailers should be that India is not seeing any across-the-board decline in consumer income and, therefore, its discretionary spending/purchasing power. There is a slowdown in the growth of incomes, and in some sectors, a marginal reduction in incomes. However, India has yet not seen massive layoffs and with the economy still expected to grow at 5% or more, there will be a corresponding increase in the overall consumer purchasing capacity. Hence, an intelligently “administered” marketing stimulus should deliver the desired results in terms of increased sales and thereby, increased overall financial contribution for businesses that can enable them to meet their fixed expenses more easily.

The starting point, for most companies and retailers, is to come up with a product assortment that can deliver more value to the consumers at this time. Mere discounting is not enough. Excessive, sustained discounting can be extremely dangerous to the power of such brands themselves and does actually erode consumer’s trust in those brands. In the backdrop of the Nano-saturated media, manufacturers across other consumer product categories and even services (especially food services and entertainment) have to think innovatively and come out with their equivalents of Nanos at the earliest. Retailers have to work more closely with their vendors to create a product assortment that is much more value-oriented, and be willing to sacrifice gross margins in the near term for sustaining consumer spending in their outlets.
The next step is to get the consumers out of their homes and bring them back in droves to the markets and shopping malls. This, of course, has to be city and market specific but, by and large, it will need a collaborative effort between brands, landlords and retailers to come up with localised efforts and promotions to get the shoppers to come again in large numbers. It will also require a pragmatic approach towards removing irritants such as parking (free valet parking or free parking in general), clean and safe environment without mindless harassment of visitors purportedly on account of enhanced security measures, in-the-market excitement reminiscent of a mela-like environment, appropriate food options including licensed hawkers for “street” food etc.

The final step is to come up with attractive and sometimes bundled packages for goods and services that tempt consumers to spend more, and feel good about spending rather than feeling guilty. Further, this effort has to be sustained through the next two quarters, i.e. till the onset of the autumn/winter season when further momentum may be achieved with the onset of festival buying.

In the absence of this marketing stimulus, there is a real danger of a total seizure of consumer spending that will be disastrous for all.

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Nine Consumer Trends for India in 2009

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From Splurging to Saving

In the past few years, Indians had been earning more than ever before and spending equally well. Splurges on branded products, eating out, multiplex tickets and foreign holidays were becoming more common. Living on EMIs was becoming the norm for young people.

However, with the economic downturn, people will revert to the traditional consumption. Thinking twice before spending every penny and tightening the purse strings will be the norm.

Indians have already begun to spend less and save more, as evident in the BACSI (Boston Analytics Consumer Sentiment Index) monthly consumer sentiment index, which hit an 11 month low in November. BACSI has been declining since June signalling consumer’s pessimism and fear about the current and expected state of economy.

Discretionary spending is likely to continue falling over the next year too if consumers don’t hear some good news on the economic front soon. Leisure, entertainment and purchasing activities will decline. Malls are already wearing a deserted look, restaurants and stores are facing up to 75% drop in clientele. Landmark has seen sales of music, movies, toys and gifts dropping in the last three months. Desperate consumers are, however, not drowning their sorrows in drink, as even liquor shops and bars are seeing fewer footfalls.

From an attitude of wanting to boast about how much they spent on the latest Louis Vuitton handbag, kitty party conversations are now about how much they saved on a particular item by being canny. People are saving up and paying cash rather than whipping out the credit card, and waiting for the annual sales rather than buying on impulse. While the middle class always valued promotional offers and could be swayed by them, today even affluent consumers are carefully scrutinising on-pack information to opt for better value deals. Discount retailers are already talking about an upswing in their footfalls and sales levels. Many retail firms including the Future Group are talking about expanding the network of discount stores in their chains. Big Bazaar, in fact, is seeing a huge upswing in footfalls.

Over the next year, consumers will continue to focus on pruning unnecessary expenses and shop with a list. Many of them may turn away from modern retail to traditional kirana shops offering discounts based on knowing their clientele, or credit periods which would be a boon to the harried housewife trying to manage a shrinking budget. Big entertainment could still tempt punters while smaller marque names won’t see much of a turnout. Rental services like online libraries for books and movies will see a spike. Retailers and brands who can offer better value for money and communicate their added value better, should see an increase in footfalls, as consumers across income classes try to stretch their rupee farther.

The Opportunity:
Up-front the value a brand offers the consumer. Help consumers feel smart about getting better bargains through innovative schemes and promotions. Enhance the aspirational value of brands so the consumer feels better about spending.
Fear Factor Casting its Shadow

From September 2002 to November 2008, India has witnessed 19 terror events, culminating in the 26/11 attack in Mumbai. More than 600 people have been killed and hundreds injured in the last 6 years. As a result, people are feeling more and more fearful for their own lives and those of their families and taking pre-emptive measures to protect themselves. This is illustrated by the reduced footfalls in public areas, especially during festivals.

Many outdoor service industries have felt the pinch after 26/11. The multiplexes of Mumbai saw less than 30% occupancy during the weeks after 26/11. Many small budget movies which don’t have star value have suffered as a result, as people don’t want to take the risk for something smaller.

The Hard Rock Cafe has seen huge cancellations of bookings post 26/11. Employees of the Cafe say it’s because people are just not coming out of their homes. Clubs too are seeing reduced footfalls as people prefer to stay at home with their families.

As a result of the state of fear, companies in the security business are finding a new burst of popularity. Hotels, hospitals, malls, multiplexes and offices are enquiring about security agencies for their establishments. Consumers also want to buy safety devices for their homes. The manager of Detech Devices Pvt. Ltd. claims that his firm used to get around 50 enquiries per day, now it is getting 500 calls daily.

What’s likely to happen over the next year is an increase in sales of mobile phones, especially the base-level models, as families ensure that each and every family member is able to stay in touch whenever they are out of the house. The penetration of mobile phones is likely to see a surge both among the youth and the elderly, as their families want to ensure they are able to be contact at all times. Traditional kirana stores would again benefit, as families shy away from shopping at big outlets in malls. Stand-alone cinemas could see a boost in ticket sales, as people prefer to flock there rather than to prominent venues like multiplexes. Parties are more likely to shift to private venues like farmhouses and homes rather than five star hotels. Security devices for the home will see a big boost in sales.

Best of all, consumers will actually become more cooperative when faced with security checks.

The Opportunity:
Brands and products which empower the consumer to feel safer. Enhancement and highlighting of product safety aspects.
Focus on Home and Family

Difficult times have the ability to bring families closer physically as well as emotionally. Economical slowdown, financial crisis, inflation, terror – all of them have created a state of anxiety and uncertainty in which people are naturally drawn to their families for emotional support. The fear of going out to popular and crowded public places further serves to bring the family closer together.

This will have an impact on the age at which young people want to move out of the parental home and become independent. At present, it is common in India for youth to stay with their parents even after they have begun working. The length of the stay is likely to increase further, with economic uncertainty looming. Marriages could get postponed to a later age as people want to feel secure in their earnings before they get married.

Given the uncertain world outside, the home more than ever becomes the place for people to congregate, to stay close to their loved ones, to insulate themselves from the harsh realities of the outside world. People will want to cocoon themselves within its four walls.

Homes have already undergone a change in recent times, becoming more comfortable as well as good looking. Now people will be willing to go the extra mile in making their homes all the more interesting for all family members to hang out in. Ordering food in will become more common as families prefer to eat in the safety of their homes. DVD rentals and sales of home theatre systems will rise as people want to enjoy the movie experience but at their own place. Products targeted at family consumption rather than individual consumption are likely to do better in these times - family packs of snacks and RTEs (Ready-to-Eat), movies that families can watch together, family offers at restaurants.

The Opportunity:
Target the family as the purchase unit, rather than the individual. Create opportunities for people to have fun with their families in safer environment – clubs, parks etc. Products that enable the family to bond and have fun while staying at home – popcorn tubs, delivery of icecreams and other fun foods, board games, RTE versions of exotic cuisine.
In Search of Smaller and Cheaper Alternatives

In times of economic slowdown people are no longer able to afford all the luxuries they have been used to. However, no one wants to become an ascetic, and therefore, we believe that the next couple of years will see a rise in small indulgences. Leonard Lauder, the chairman of Estee Lauder, coined the term ‘lipstick indicator’ which indicates what happens when the economy gets tough - lipstick sales go up. Consumers cut down on their spends on expensive creams, fashion and other categories considered as ‘frippery’ but continue to spend on small items like lipstick and nail polish, as they cost much less and yet feel like an indulgence.

People will look for cheaper entertainment options and cheaper ways of pampering themselves and their loved ones. Children will be indulged with more candy but less expensive toys. Chocolate sales and those of other inexpensive treats will rise – microwave popcorn, DVD, RTE food.

Downsizing will be in the form of having coffee at a Café Coffee Day rather than expensive meals at restaurants, watching the latest movie on cable or DVD. Women will colour their own hair rather than getting it done at a parlour and get a massage from the ‘maalish waali’ rather than going to spas. People would go shopping in their friends’ closets rather than to stores. Walks will become more popular than visits to the gym. Vacations may either be downsized to long weekend trips to nearby destinations or trips to visit relatives.

India has always had a thriving trade in second-hand goods. There is a tradition of passing down everything from clothing to utensils to needy members of the family. This is going to become much more of a need and consumers will be more willing to accept second-hand goods in more categories – white goods sales may rise in the second hand market, as will brown goods. Music CDs and movie CDs or DVDs may find a market.

Consumers will feel the need to demonstrate their own sense of control over the purse, whether they need to do so or not. And only brands which make a conscious effort to help them do so, will continue to rack up sales in the next few years.

The Opportunity:
Combine enticement and affordability in the brand – communicate the enticement and demonstrate affordability. Have small-sized packs of indulgence products, be it face cream or expensive chocolates. Create forums for exchange of used products, a la Craig’s list, or have an organised buy-back/ exchange program.
People were slowly turning to more and more branded products, as much for their badge value as for the purported quality that brands promised. But at a time when they are trying to economise, consumers are more concerned about getting good value for their money and will eagerly turn to unbranded products that offer similar functionality in many product categories.

Says Jayshree Sundar, a former senior professional in advertising, “My daughter needed floaters for her school camp. Earlier, I would have gone to a Reebok or Adidas and swiped the credit card for some US$71 to US$ 95. But this time, I told her we are only going to Bata. Then, on the way, we spotted a small street market which had unbranded floaters for US$ 7. I promptly went and bought them, and I’m proud of myself.”

As the shift from branded products back to the market is a bit harsh for many customers, private label brands may find a huge opportunity. For example sales of private labels in Vishal Megamart jumped from 5% to 6% of total turnover to 17% to 18% in the last 3 to 4 months, and similar growth rates are being noticed by other retailers too. People are not shifting away from brands per se, but evaluating where brands are not indispensable.

Brands will need to offer more real value than ever to ensure that consumers stay with them. From needing the emotional payoff of lifestyle or lifevalue similarities, consumers are beginning to value the rational payoff of a better deal.

The Opportunity:
Continue investing in brand building so that when the good times come back, there is a substantial ‘aspiration bank’ from repressed consumers. Focus on ensuring that brands move towards MOC / MOUs that are brand-indispensable. Private labels with the twin offer of quality at a fair price. Brands and retailers working together to create special branded store-brands which offer the same brand value but at the store price.
As people become more economically secure, they become much more confident in themselves and at the same time have an increased awareness of their rights. As a result, they start demanding much more accountability and transparency, both from government and from business. India too has been seeing a slow rise in social consciousness over the past few years.

Moreover, people have slowly seen a rise in the power of individuals to make a difference. The ‘angry young man’ has given way to the ‘determined young man or woman’ who has managed to fight the system and get his way. Incidences like the Supreme-Court-granted-power to fly the Indian flag, due to a legal battle by one person, have had an impact on people’s perception of their own power. The mobile phone has suddenly given Indians everywhere, from small villages to large metros; a voice, and information at their fingertips. The RTI legislation too has been important in giving the average citizen a sense of much-needed control and the ability to ask the government machinery to be transparent in its decision-making. Media too has jumped into the bandwagon, espousing causes and getting the government machinery to act, as the recent example of the ‘Hindustan Times’ series on the lack of infrastructure in Gurgaon demonstrated.

In recent weeks, one has seen much more of this kind of activism, be it the various citizen’s groups which sprang up after 26/11, the demonstrations in big cities which were unique for having many middle and upper middle class participating voluntarily rather than the paid rent-a-crowds of political parties. The state elections which took place immediately after 26/11 also saw the highest-ever voter turnouts in Indian history, announcing the arrival of an era wherein citizens are eagerly exercising their rights. Individuals are feeling a sense of entitlement to their rights and are feeling more secure in their power to be the change that they want to see. People want to take control of their own lives to a much larger extent, be it in terms of security or finances. Many brands including Idea and Tata Tea have already started capitalizing on this new spirit through their communication.

This is likely to increase substantially in the future. This will have a rub-off on companies and brands as well, as consumers ask for increased transparency from India’s corporates. Particularly at a time when consumers are finding their purses under threat, they need the brands and the companies they buy from to be accountable and to show accountability. Also, brands and products which help the consumer gain a sense of control over their lives are likely to see an upsurge.

The Opportunity:
Empower consumers to participate through feedback and dialogue in the process of product enhancement and correction. Help the consumer be in control of their access to products and services.
Investments in Gold and Jewellery

In the last few years, there were few asset classes which were not rising, be it stocks, real estate, art or commodities. However, all of a sudden almost all asset classes seem to be in a freefall, and the only ones holding their heads up are gold and silver. At times like these, when nothing else seems to be stable, traditional investments like gold and jewellery seem extra attractive, and these categories of products are likely to see a real boost in the next few years.

Just recently, Christie’s sold a 36-carat diamond for the highest ever price of US$ 24.3 million, claiming at the same time that the first half of 2008 ending with jewellery sales of US$ 226 million was “the best jewelry season ever seen at the auction”. As per the Retailers Association of India, the jewellery sector might expect a boost of even 25% to 40% !

Ordinary consumers are rushing out to invest in gold and diamond jewellery, silver utensils and even gold biscuits - assets that are real and tangible and can be kept under supervision. These are also seen as assets which never depreciate and which can then be exchanged or sold off in case of dire need. As long as gold prices remain at a viable level, one expects the upsurge in gold and jewellery sales to continue.

The Opportunity:
Highlight the investment nature of gold and jewellery products to make it easier for consumers to rationalise their purchase. Have promotional offers involving gold and silver coins with other products.
The Rise of Spiritualism

When companies face turbulent times, they turn to the government. When consumers face uncertain times, they turn to the Supreme Power and Religion, to ask for a bail-out. Now that the bad times not only seem certain but also there is uncertainty over when those bad times will be over or how bad can they likely get, religion is poised to get a huge boost in terms of adherents. Since people don’t know what rational means they can personally use to bring more stability into their lives, people are going to turn to spirituality or superstition.

New-age spiritual beliefs as well as superstitions are going to become stronger. Be it Feng Shui or Vaastu, ways of bringing in good luck and repelling bad luck have been becoming popular, and this is only going to increase in the next few years. The number of people going to ‘future-tellers’ like tarot readers, palmists, horoscope readers or ‘Naadi’ readers is also going to rise.

Newspapers and magazines are showing more ads for things like healing crystals or good-luck rings, all meant to boost career and money. Sites like astrologyzone.com and other ‘divine intervention’ websites are suddenly seeing a lot more traffic.

The Opportunity:
‘Vaastu’ or ‘Feng Shui’ compliant properties. Integrated ‘puja’ services or online services which would perform the right pujas at the right time for interested consumers, and give them a webcast of the same.
As brands and corporates see consumers becoming increasingly watchful of their spending, and more likely to switch brands or service providers for financial reasons, they will go out of their way to bind the consumer closer through Customer Relationship Management (CRM) programs. A lot more time and money will be spent below the line on strengthening CRM programs and getting more consumers into their net, as brands try and retain their goodwill bank.

This has already begun in various service industries, with brands from Jet Airways to Kingfisher making more strenuous efforts than before to woo travellers. The frequency of mailers and communication from the brand to the consumer has gone up already and is likely to increase.

Many brands are trying to tie-up with like-minded and well positioned brands to provide more package benefits to consumers. More brands will be on the lookout for such tie-ups that can help manage the cost of the outreach programs, provide access to more consumers and help build in more loyalty.

What will be interesting to observe is whether the heightened levels of attention and service remain constant once the economic crisis subsides!

**The Opportunity:**

*Build a closer relationship with the consumer which can continue long after the slowdown is just a memory. Use the closer relationship to build differentiation.*

**To Sum Up:**

*Overall there seems to be a move in values and lifestyles to those of the 1970s, where conservatism was the order of the day. Consumers seem to have gotten off the greed bandwagon that characterised consumption in recent years and want to get back to a time when the act of consumption was more considered and rational. Brands that speak to those conservative values or that help the consumer continue to ‘live the good life’ while enabling him to spend like the old days should do well.*

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The Indian Retail Landscape: Now and Beyond

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Reasons to be Cautiously Optimistic

The year 2008 witnessed economies becoming sluggish, stock markets crashing, banks going bust and falling consumer confidence all over the world. India has also been adversely affected. However, the Indian growth story is driven by strong fundamentals. Hence, even in the relatively lower GDP growth scenario (projected downwards from 8% to 6.5%), the Indian growth promise remains intact.

Despite the turbulent times, sectors such as FMCG, Consumer Durables and Rural Economy have done reasonably well. Infact, some of the sectors have seen unprecedented growth in the wake of softening commodity prices and recent excise duty cuts. Input costs have dropped by roughly 25% to 30% in several categories. Inflationary pressures have eased and the interest rates are projected to head downwards. Hence, the ‘Great Indian Retail’ story is still intact and will continue to witness evolutionary growth and opportunities in the years to follow albeit with some short-term hiccups.

It can also be argued that the current turbulence is something not completely undesirable. It has been a reality check for retailers to take stock of their operations and strategy. This will make them go through a sanitisation phase of restructuring, reconfiguration, re-planning and renegotiation towards robust & efficient business models leading to stronger proposition and long term sustainability.

Technopak expects the best phase in Indian retail sector is yet to come in the next five years, when the sector would see major expansion by national & international players, consolidation and operational efficiencies would set in.

In this document, we have tried to capture a few trends in the Indian retail landscape. These reflect the future of Indian retail and the picture as we see it, continues to be promising.
Phase of Rebuilding Begins

Modern retail in India has been going through a steep learning curve. The first phase of setting shop is now over and it has entered a new phase where retailers are taking a hard look at their fundamentals. The last few years have seen players experimenting with formats, product mix, locations, sizes, customers and now is the time when we expect the phase of rebuilding would begin. The key areas of rebuilding would include:

Re-Sizing and Relocation
With recent drop in rentals, many leading retailers are in the process of re-negotiating rentals with the developers. They are also planning to relocate stores which are economically not viable or where rentals are more than market rates and resizing others to make them more profitable. Retailers are identifying stores to find out opportunities for resizing, closure or relocation.

Resizing would be a major phenomenon with the big formats getting even bigger.

- Larger stores would enable the retailers to offer more variety to the consumer and meet all consumer needs with “All Under One Roof” proposition, thus capturing a bigger chunk of consumer wallet and larger consumer base
- This will also enable retailers to realize higher margins by adding more non-food & grocery (F&G) lines since F&G is essentially a low margin category
- This will further enable cross-subsidization of essential items for which the consumer price sensitivity is high

At the same time smaller formats may further get smaller in order to get closer to the customer and offer greater convenience.

New Formats
Most of the players are operating across multiple formats. We have seen a rapid scale-up of operations by “older players” and “new entrants” and expansion into specialty formats along with the core F&G. Retailers are experimenting with new formats in order to hit the “right formula” as well as to target a larger share of consumer wallet. Future Group had 4 formats in 2003 and now it has more than 16 formats. Reliance also has more than 12 formats.

Reaching to New Consumers
With a presence in top 70 to 80 cities, modern retail is still currently under- penetrated and actually serves 7% to 8% of the total Indian population. Retailers are moving to a larger consumer base with focus shifting from upper income consumers to middle class, and finally into the markets of the urban poor/rural market. Lower income segment is being targeted by a different value proposition of products/ prices/ services such as deep discount, private labels.
Spreading to New Geographies
Though most retailers’ initial focus has been on metros and mini-metros, they are rapidly moving into smaller towns and even rural India. This is because metros have already witnessed 15% to 25%+ penetration of modern retail (compared to 4% to 5% at all India level) and all the attention and investments are already leading to:

- Cost escalation - real estate, services, people
- Margin dilution - due to competition, market share wars
- Cannibalization - over saturation of certain locations

So while retailers are not ignoring these thriving markets, they realize that they need to look beyond metros and larger cities now to achieve ambitious growth. It is expected that by 2013, modern retail would have reached at least top-600 Indian cities and towns, and perhaps directly or indirectly will have access to over top 50,000 villages e.g. from 5 cities in 2003, Koutons is present in more than 250 cities now. Vishal Megamart is present in more than 100 cities, Big Bazaar in more than 60 and Café Coffee Day in more than 200 cities.

Restructuring of Operations
Last few years witnessed frenzied activity in terms of store opening and this led to a lot of inefficiency creeping in the operations of the company. Slowdown has given an opportunity for retailers to streamline their operations. A number of retailers are restructuring their operations through combining the operations of various formats to reduce overheads and achieve economies of scale. In addition, retailers are also restructuring their supply chain by reducing inventory and logistics costs to reduce working capital requirements.
FDI Relaxation at Inflection Point

India is today the only major economy that still does not permit FDI in retail trade. Currently, the Government policy allows up to 51% FDI in single-brand retailing, and 100% FDI in cash-and-carry wholesale trading. FDI in retail is not allowed in multi-brand retailing.

One of the major reasons for indecision in opening up FDI in retail has been the fear of its adverse effect on the small retailers. Also, the political repercussions of this decision has made the government overcautious in its approach.

However, the need for relaxing the FDI norms now is more than ever before. In order for GDP in India to grow at a level of 7% to 8% in this current global slowdown scenario, it requires raising the rate of investment as well as generating demand for the increased goods and services produced. FDI will lead to increase in exports due to high level of sourcing from India, technological and processing capabilities, infrastructural developments, increased employment, and inflow of funds and investment in the country. Hence, FDI can catalyze the retail boom and provide an upward push to the overall economic growth of the country.

Given the need of the hour, we may see an overall easing out of FDI norms once the new government takes over. However, FDI will still be eased in a phased manner with Food & Grocery (F&G) being last of the categories to be relaxed.

Ahead of Commonwealth Games 2010, the Government may want to meet the arising demand in sports and electronic goods by facilitating foreign companies to make direct investment. Also, it may ease out relatively less-sensitive sectors like apparel, lifestyle products, house ware, and entertainment etc. over the next few quarters.
The consumer shopping behavior has undergone an evolutionary change with the advent of modern retail. With increasing exposure, the consumer of today is getting comfortable with modern format and also more experimental than in the past. Modern format stores provide a conducive environment for the consumer to become more involved in the product selection and up-gradation.

The plethora of brands available in a modern format store forces a shopper to spend more time in comparing the benefits, cost and finding the best that suits his/her needs. Even if the shopper has a brand in mind he/she looks for new opportunities and products that may add to his satisfaction. Such stores provide an environment where the shopper likes to spend more time and choose his/her basket of products.

As a result of more exposure and time spent, consumers are trying new brands and variants while shopping in modern format stores. Almost half the time they end up buying new brands or variants for many categories.

This has a cascading impact on the type of products and promotions of consumer product companies. Consumer product companies have understood the shopper trends in modern retail and are adding high variants to their modern retail portfolio to lure the consumers. Companies are also able to launch high end products through modern retail and can find market for several niche variants which they were unable to promote through traditional retail stores, where space and ambience are serious constraints. For example, Dabur India launched a 400 gram squeeze pack of Dabur Honey only through modern format stores. Later, the company also launched two variants of Chyawanprash, a sugar-free version and another that claims to combat stress, both in modern format stores where the target customer is likely to shop and, perhaps more importantly, is willing to pay a premium that products charge over regular variants.
The growth of modern retail has posed a different challenge to consumer product companies. The availability of the manufacturers/vendors and the hindsight learnings have led to the early onset of turf war between the consumer product companies and retailers.

The realization is fast dawning upon several consumer product companies that the rules of modern retail are different from traditional retail and success in one does not guarantee success in the other. There are several examples where industry leaders enjoying the lion’s share of traditional trade are reduced to minority players in modern retail. For example one of the leading Consumer Durables & IT (CDIT) company with more than 15% share of traditional market has only 7% to 8% share of CDIT sales from modern trade which would become a cause of concern in future as modern trade grows bigger in value and volume. Many consumer product companies are unable to get similar success across both traditional and modern trade due to their “same size for all” attitude, even though the channels are very different from each other. These differences include:

- The consumer behavior across both channels is very different. Modern trade provides an environment where shopper spends more time in choosing the products. They compare different brands, variants before making the final purchase decision and hence are highly involved. They end up trying new brands and variants while shopping in modern format stores.

- Most modern retailers prefer a Terms of Trade (TOT) document that defines the relationship between the two parties. The key challenge for suppliers is to prevent margin dilution with the increasing power of retailers. Very large retailers may have to be treated as key accounts and suppliers may have to come up with innovative schemes such as co-branding, exclusive promotions to maintain a win-win relationship.

- Organization structure for modern retail needs to be different. Modern retail needs a structure that provides stability in a dynamic environment and offers flexibility to prepare for the high volume business.

- Parameters like category management and new product launches, which were not so important in traditional retail gain importance in modern trade. Modern retailers use parameters like fill rate, category management, margins, organization commitment, new product launches etc to evaluate the suppliers.
Additionally, the increasing penetration of private labels of retailers dilutes the bargaining power of the consumer product companies. Indian consumers are willing to spend money, yet they are value conscious. Private labels, on an average, offer price discount of 15% to 30% versus their branded counterparts and therefore, have brought new customers and lead to increased consumption. Given that the sale of every private label item replaces the sale of a potential branded item are getting more empowered retailers and getting better margins. It also gives retailers more negotiating power in the product category. For these reasons, retailers are also promoting regional and smaller brands. Juice, for example, is a category where almost 30% market has been taken up by the relatively unknown brands/private labels. In the long run, private labels can also help differentiate one retailer from others and can be used to build store loyalty. Since private labels play a crucial role in the power shift from brand manufacturers to retailers, all major retailers would sooner or later focus on it.

Given the challenges, we will witness evolution and differentiation of channel strategies of consumer product companies as modern trade grows.

Technopak’s interaction with some of the leading consumer products and consumer durable companies has revealed that the companies are getting ready in terms of redesigning their service models, organization and processes to meet the expected demand from modern retail. Many of them are beginning to understand the so far neglected area of shopping behaviour.

Branded outlets are rediscovering themselves (e.g. Sony, Canon etc) to create the preferred outlet for brand communication and also stand in good position while dealing with the retailers.

Consumer product companies are also trying to protect their turf by investing in traditional retail channels and upgrading them to maintain their stronghold. Large players are partnering with local vendors to revamp and modernize their retail outlets and upgrade the overall retail environment. HLL Super Value Stores, and Marico Mera Bazaar have undergone this transformation.
The first two quarters of 2008 witnessed a steep escalation in real estate prices especially mall and high street rentals that retailers started pulling out of malls or delaying their expansion plans than operating unprofitably. As a result, several malls could not get full occupancy thus, adversely affecting footfalls.

The third quarter of 2008 brought some correction in real estate prices. With inflationary trends, high operating costs and low footfalls, major metros started witnessing a dip in rentals. The fourth quarter of 2008 witnessed more corrections and further drops. Most of the markets have witnessed a correction of 15% to 40% in rentals. Rentals in many malls have witnessed renegotiations and corrections.

As a result, the developers are on their back foot. They have begun to realize that their role needs to extend beyond mall construction and cover mall management as well.

Both retailers and mall developers have realized the need of collaborative models to create a win-win situation for the retailer, mall developer as well as the consumer. Retailers cannot afford rentals more than a percentage of sales on an average across categories and developers need a minimum return over inflation rate or base lending rate to justify the investment. Therefore, the need for a model based on minimum guarantee or revenue share, whichever is higher, works well for both the parties, and hence we see the increasing adoption of revenue sharing model. Revenue sharing that implies mall developers need...
to create ways to attract footfalls and retailer revenues and not “abandon” the mall once leased out. Since mall quality has not been a focus for most developers in the past, a large chunk of retail space would be untenable due to poor quality or location. Therefore, the next few months will see the retailers choosing reliable developers and selection of location would be very critical. Cases of better quality malls in same area commanding higher rentals are a testimony to the importance of mall quality.

Mall management has been a major challenge for India’s developers, who until recently have mostly developed properties and then sold it to investors who further lease it out to the retailers. This has resulted in unplanned and uncontrolled developments of the malls and may lead to eventual loss of rental values. Given the increasing competitiveness, developers need to focus on mall management aspects such as location, research on catchment area analysis, right mix of component and tenants and right zoning. Hence, mall developers are also getting serious. They have increased focus on tie-ups, better quality malls, innovation, mall development and management.

Technopak also expects that given the financial difficulties faced by mall developers, there would be a significant delay/postponement in a number of planned malls thus leading to shift of retailers to high street locations.
Supply Chain to Get its Due Consideration

Till date, the retail investments were focused more on the front end than on the back-end. As a result though most players have several stores in place, they have no rigorous supply chain to generate the cost efficiencies and fill rates needed to improve the bottom line and improve customer experience.

Retailers are increasingly realising that it can be handed over to specialists. This is leading to rise in Third Party Logistics (3PL) industry, thus enabling retailers companies to leverage their resources, bring down fixed and working capital investment, spread risks and concentrate on core business matters vital to survival and future growth.

Besides modern retail growth, other factors which have fuelled up 3PL growth are simplification of tax structure, increasing investment in infrastructure, increased incentives by Government through logistics parks, free trade warehousing zones coupled with correction in real estate prices which will lead to availability of retail space at cheaper cost and large investment in setting up big warehouses.

Amid a surge in demand for logistics and warehousing activities, many logistics companies are reinventing themselves and targeting larger roles. The entry of global firms such as UPS, TNT, NV and DHL International GmbH has made domestic players better and more competitive. Traditional Indian logistics players are now organizing themselves in order to become more scalable. Even logistics players that provided limited supply chain services, are now moving to a strategic role that involves complete end-to-end solutions to improve efficiencies. As a result, while overall logistics pie is growing at a CAGR of 8%, 3PL revenues are growing at 22% faster than any other logistics segment.

On the warehouse front too, we expect to see more activity. Historically, warehouses have been located in close proximity with primary markets. However, the abolishment of Central Sales Tax (CST) and an improvement in infrastructure would enable companies to realign their supply chain and move closer to consumer markets. As a result, demand for real estate will no longer be restricted just to the existing primary logistics hubs in the country and will boost the real estate market.

However, it is unlikely that we will see the benefit of all the current and planned investments in the short term because most of the investments are either at nascent stage or would take time to reap benefits. Hence, the entire supply chain would still need more time, effort and investment to streamline, optimize and result in significant cost advantage and efficiency.
Despite all the mass advertising, the truth remain that more than 60% of the purchase decisions are made at the point of sale. Key influencers and activations used are:

- Brand advisors/ sales staff
- Free sampling in some categories
- Promotions in terms of freebies, discounts etc
- Visibility
- Display aesthetics

The economic downturn has increased focus on cost cutting measures and one area which companies are taking a relook at is their marketing investments. They are evaluating and attempting to optimize their Returns on Marketing Investments (ROMI).

Many companies have stated their intent on cutting back marketing expenditure that is not yielding desired results and backing investments they are sure about. High viewership fragmentation on mass media like TV has made them look at micro marketing in a big way. A leading consumer products Company, which has followed the practice of running six-seven communication pieces for select brands within a year, is now planning to do just one or two.

In tough times, marketers feel the need to create the urgency to buy — a need fulfilled by tactical advertising. Therefore, the emphasis on new marketing models that look beyond the traditional media and television commercials like digital, mobile and PoS initiatives. It is expected that there will be a shift in investments from Above-The-Line (ATL or mass media) to Below-the-line (BTL) during the slowdown, partly because in absolute terms, the investments in BTL are lower and the flexibility to adjust the scale is higher.

In 2008, the advertising industry grew at 14% to 15% while BTL expenditure grew by 18% to 20%. In 2009, it is expected that advertising spend would grow at 8% to 10% and BTL at around 15%. Experts believe that the shift in investments from ATL to BTL could be anything between 5% to 10%, depending on the advertiser.

BTL also appears to be more productive. In mass-media advertising, only 2% to 20% may be the target customers – Hence, even though it has a higher reach, it leads to more wastage and is less productive. On the other hand, promotions touch the consumer directly. As a result many companies are looking at radio, experiential marketing, PoS activation and digital media more seriously than they ever did. BTL may not always be tactical and short-term e.g. relationship marketing, hence it can lead to long term impact too.

Therefore, We can expect that 2009 will be the year of non-classical advertising. The focus would be on becoming more productive, more effective and closer to point of sales.
Reducing Costs

2008 has been a challenging year for retail. With the economic slowdown and falling sales, many retailers were forced to review and rationalize their costs. As a result overall employee remuneration witnessed a lesser growth and in some cases de-growth too in the last two quarters. Since the sales are not expected to change, it is expected that retailers will adopt a more cautious approach in 2009, given the need to further reduce/ rationalize costs.

The irrationally high compensation packages which had become common for hiring talent in the past will now be fewer and far between. Companies will tend to focus on grooming internal talent and build from within to manage their future talent needs. This can be perhaps viewed as a good time for organizations to consolidate their HR strategies towards a high performance orientation and also look at eliminating HR redundancies.

Balance Struck in Expatriate Recruitment

Another retail HR related trend is the movement of expatriates. Several businesses in the last a few years had hired expatriates in their top management. This was primarily because the retail industry in India was at the nascent stage and there was a lack of local expertise and competencies in India. On the other hand, developed economies had people who had expertise in managing large retail businesses and were well versed with the best practices of the industry. Hence, many retailers recruited expatriates in their top management to mentor the Indian teams and establish their businesses. However, we have seen that many of these expatriates have moved back to their countries or moved on to other assignments.

For instance one of the leading Indian retailer had hired 50 executives from leading retail companies across the globe. These executives came from mature markets such as the US, UK, France, Germany, Australia and Singapore and had at least 25 to 30 years experience in the retail business. From this pool of 50, around 30 executives returned to their respective countries in mid 2008.

There are several reasons for movement of expatriates. Some of these are:

- High costs
- Cultural differences, making it difficult for expatriates and their families to plan long term stay
- Inability to handle the complex Indian retail challenges like the inefficient supply chain and lack of systems and processes
- Increasing availability of Indians returning to work in the country
- As organized retail is no longer an unknown territory it used to be, getting competent local talent is becoming relatively easier

This does not imply that international expertise is no longer needed by Indian businesses now. However, Indian retailers are now more aware of the business environment and hence, would be able to identify specific areas where the expatriates can add real value to the business.

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Riding High on the Back of Inorganic Growth

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Background

The Textile and Apparel (T&A) industry in India is a major contributor to the GDP, exports, employment and foreign exchange earnings. It contributes about 14% to the industrial production, 4% to the GDP and 17% to the country’s export earnings. It is also the second largest provider of employment after agriculture, providing direct employment to over 35 million people.

The domestic size of the Indian T&A industry was about US$ 33 billion in 2008. It is projected to grow at an annual growth rate of around 10% to reach US$ 47 billion by 2012. Additionally, T&A exports were US$ 22 billion in 2008 and are estimated to reach US$ 36 billion by 2012 at an annual growth rate of 13%.

Today, it is not enough for T&A companies to merely keep pace with the changes in the business environment. They are expected to outdo competition and innovate in order to continuously maximize shareholder value. Inorganic growth strategies like mergers, acquisitions, takeovers, spinoffs, joint ventures and strategic alliances are useful engines that can assist several companies in entering new markets, expanding customer base, beating competition, consolidating, growing quickly and employing new technology with respect to products, people and processes.

Evolution of Textile and Apparel (T&A) Industry

The global T&A industry has come a long way since the days when manufacturing was primarily done in the consumption centers of US, Europe and Japan. With the development of US and European economies, T&A manufacturing increasingly became uncompetitive in these countries. Various phases that the global T&A industry has under gone are shown in Exhibit 1 and include.

**Multi Fibre Arrangement (MFA) regime (1974 – 1994)**

The MFA envisaged quota restrictions on imports into developed countries. During the MFA period, from 1974 to 1994, trade shift occurred from Newly Industrialized Economy (NIE) countries like Hong Kong, Taiwan and Korea to less developed Asian countries including India. China emerged as a major force with its economy opening up to foreign investments in 1979. This period witnessed initial growth of the emerging Indian T&A industry.

**Agreement on Textiles and Clothing (ATC) Regime (1995 - 2004)**

Developing countries protested against quota restrictions and subsequently MFA was replaced by ATC in 1995 for phasing out quotas. ATC envisaged elimination of all T&A quotas by 2005. During this period, Indian T&A industry experienced growth along with a considerable increase in number of SMEs and production capacities.

**The Post Quota Era (2005 onwards)**

After the quota restrictions were eliminated from all the T&A products imported by the developed countries, buyers were expected to shift sourcing to lower cost Asian countries. China was the major gainer despite safeguards applied against some of its key products in European Union (EU) and US markets. South Asian countries also gained due to their cost advantage as compared to African, European and South American countries. During this era, the Indian T&A industry saw an increase in number of big players to achieve cost effectiveness through economies of scale.
Several factors affected the trade shifts in T&A trade landscape. Key factors are more at a macro level than at a micro level as shown in Exhibit 2 and some factors played a bigger role than others. These include:

- Factor cost – specially labor cost
- Availability of quotas
- Regional and bilateral trade agreements
- Raw material competency
- Proximity/ transportation infrastructure
- Government policy / political factors like import tariffs

### Inorganic Growth as an Emerging Opportunity

Today, the business environment is rapidly changing with respect to competition, products, people, manufacturing processes, markets, customers and technology is embedded in all these functions. It is not enough for companies to merely keep pace with these changes but also to outdo competitors and innovate in order to continuously maximize shareholder value. Inorganic growth strategies like mergers, acquisitions, takeovers, spinoffs, joint ventures and strategic alliances are useful engines that can assist several companies in entering new markets, expanding customer base, beating competition, consolidating, growing quickly and employing new technology with respect to products, people and processes. Therefore, inorganic strategies are regarded as fast track strategies for growth and unlocking value to shareholders.

Compared to organic growth, inorganic growth is often seen as a quicker way for a company to grow as shown in Exhibit 3. Growth is often accelerated through increased innovation, and one way for firms to compete is to align themselves with those companies that are developing innovative technology.
Inorganic Growth in the T&A Industry

With respect to the global dynamics of T&A industry, inorganic growth (especially M&A) primarily serves as a tool for maximizing shareholder value for companies looking for the following:

- Expanding into new markets and access to distribution networks
- Bridging the gaps in technological know-how and product development
- Value addition for financial gains and stronger positioning for growth
- Diversifying into new products for spreading risks
- Cost reduction by taking advantage of macro-economic incentives (like duty benefits, low labor cost etc.)

In India, the prevailing cutting edge competition has called for the following measures, which are addressed by many through inorganic tools like M&A and alliances:-

**Expansion to New Markets**
Companies are seeking expansion to new markets to achieve economies of scale. Examples include Bombay Rayon Fashions Ltd. (BRFL) which has now access to the Italian retail market.

**Brand Value and Product Development Capabilities**
Companies are expanding brand value and acquiring capabilities in supply chain and product design & development in order to enhance shareholder value. Gujarat Heavy Chemicals Ltd. (GHCL), after acquiring a European brand in home textiles, has extended the brand to India. They have thus leveraged on the capabilities of the acquired brand.

**Vertical Integration**
Companies are looking to evolve from fabric manufacturing to garment manufacturing or from manufacturing to retail in new markets. Examples include Welspun, BRFL and Himatsingka Siede, all of whom have made overseas acquisitions recently.

**Scaling up in Low Cost Manufacturing Destinations**
Companies are also seeking to acquire manufacturing facilities in low cost countries like Vietnam, Cambodia and Bangladesh to take advantage of their duty benefits to EU markets and cost benefits (as compared to India). Companies making such acquisitions include House of Pearl, Spentex, Reliance etc.

**Enhancing Technology**
An important need of Indian companies is improving their plant efficiencies. Technology is a key competitive advantage in the T&A industry and Indian companies need technology to compete favorably against low-cost competitors. An example of an Indian company acquiring factories for technology is Orient Craft. It acquired a Levi’s factory in Spain in 2005, mainly for its superior machinery to be brought to India. Many companies have entered into strategic alliances to bring new technology to India. Indian big names like Arvind Mills, Alok Industries, Sri Ram Fibres, Himatsingka Siede, Century textiles have established technical collaborations with technologically superior companies in EU for improving their competitiveness.

**Global Presence for Improved Service Level**
In today’s world of fast changing consumer trends with a plethora of options available with the consumers, service levels form an important component of ‘winning’ strategies. Improved supply chain is the need of the hour to meet varied needs like ‘fast fashion’ to provide value for money.

**Development of a Robust Model for Retail**
Transnational corporations have emerged as important players in the global distribution and production of T&A sector. Large retailing firms in developed countries exert a strong influence on pricing and sourcing locations because of the independent labels they carry and their growing volumes of private-label production.
There has also been a move towards “lean retailing”, wherein retailers have increasingly brought their suppliers under more direct control. They want their suppliers to implement information technologies, use modern methods of material handling and use standards for product labeling etc.

**Consolidation within India**

The potential for the sector’s growth are ample, but the trick lies in competing effectively against rivals. Consolidation of the industry for delivery of better quality at effective rates and minimum lead times can help the players surmount competitive pressures.

The Indian T&A industry is currently caught in the midst of a global demand slump and increasing competition from nearby low cost countries. Even though many companies may not be in a position to invest at the moment, for many T&A companies looking to grow fast from a long term perspective, this may be the right time to make in-roads in “new markets with existing products” and with “new products in existing markets”. The best way to do this would be to look for strategic options across the value chain and see where the company can add value quickly by the inorganic route. If there are still any apprehensions, attractive valuations might just be the driving force for the M&A route.

However, this is not to say that inorganic route is recommended for all T&A companies. There are several cases of companies that have chosen to grow organically and have done well in the long term. There are several examples of failed M&As and alliances too.

**Attractive M&A Destinations**

Different countries and geographies offer different benefits for M&As. Attractive M&A destinations for the T&A industry include Vietnam, Cambodia, Bangladesh because of cost and duty benefits and Mexico, South America, Europe due to availability of technology better technology and proximity to the markets.

**Evaluating Inorganic Growth Opportunities**

Despite the possible benefits that inorganic deals like M&A bring to the table, there are several pitfalls and deals can go wrong if companies evaluate them incorrectly or there are bottlenecks in deal implementation. It is a fact that majority of the global M&A deals are unsuccessful in increasing shareholder value and hence it is important for companies to evaluate their own need for such growth. They should value prospective deals from a long term strategic perspective rather than for short term financial gains.

Companies first need to understand whether going for deals like M&A makes sense for their business going forward. Hence, a broad strategic perspective needs to be formed before looking out for targets. For this, companies should follow a four step process as shown in Exhibit 5.

- **Plan:** Determine how fast the company wants to grow and whether it is ready to diversify and take risks for this purpose
- **Scan:** Scan the macro-environment for identifying the avenues of growth keeping in mind industry life cycle / growth phase, competition intensity, entry barriers, market demand etc.
- **Synergize:** Once avenues of growth are identified, the company needs to identify synergies between its vision, existing capabilities and available options of growth
- **Analyze:** Finally, it needs to analyze the available options from financial and integration perspective for closing on the best deal

**Exhibit 4:**

<table>
<thead>
<tr>
<th>M&amp;A Destinations</th>
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<tbody>
<tr>
<td>Low cost manufacturing</td>
<td>Bangladesh, Vietnam</td>
</tr>
<tr>
<td>Product Diversification</td>
<td>China, Sri Lanka, Italy</td>
</tr>
<tr>
<td>Market Access</td>
<td>Romania, Turkey, Russia, South America, China</td>
</tr>
<tr>
<td>Vertical Integration</td>
<td>Europe, US, China</td>
</tr>
<tr>
<td>Technical Knowhow / Brand</td>
<td>Europe, US, Japan</td>
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While analyzing deals in the final step, companies should be careful not to assess deals only from the financial perspective since financial parameters like ROI, DCF, NPV, market value etc. used alone can skew the partnership/merger toward short-term goals and measures.

Instead, as shown in Exhibit 6, companies should base their evaluation on Strategic Return On Investment (STROI) which takes a long view on partnership, different from the conventional way that focuses on short-term financial goals. STROI defines strategic end-state results in concrete terms apart from establishing a common vision. It provides a bridge between strategy and operations for the design of the operations plan. It actually provides the basis for later performance measures that quantifies non-financial returns.
Case Studies

Welspun India Ltd.

Welspun India Ltd. is part of the US$ 1.5 billion Welspun Group and amongst the top-4 terry towel manufacturing companies in the world. It has strengthened its brand and market through inorganic route as shown in Exhibit 7.

Exhibit 7: Inorganic Growth of Welspun

- Upgrade to Brand
  - Acquisition of UK’s largest towel company Christy
- Stronger brand presence
  - Acquisition of Sorema
  - Enhancement in market presence

Bombay Rayon Fashions Ltd. (BRFL)

BRFL is one of the leading, vertically integrated textile companies in India. They have a strong presence across the entire value chain - from design, yarn dyeing, weaving, fabric processing to garment manufacturing and retail. They have been a firm believer of inorganic growth strategy and have made several acquisitions to achieve different ends.

Exhibit 8: Inorganic Growth of BRFL

- Manufacturing synergies reached
  - Takeover of Leela Scottish Lace Pvt. Ltd.
  - Acquisition of LNJ Apparel
  - Acquisition of Maryan Apparels Pvt Ltd.
- Access to new markets
  - Acquisition of DPJ Clothing Ltd.
- Consolidation of businesses
  - Consolidation of partnership firms Garden City Clothing and BR exports
- Brand building
  - Takeover of ‘Guru’ and other retail business of Jam Session Holdings Srl, an Italian company
The Road Ahead

Some of the major global T&A manufacturers have already shown interest towards investing in India. While Italian fashion garment manufacturing major Carrera has firmed up plans to invest around US$ 200 mn in Maharashtra, another Italian group is carrying out feasibility studies for setting up the “Italian Fashion Village” in Kerala. German investors have invested in export of textile products and a Danish firm too has got approval for setting up a unit for export of textile products. Besides these, UK has lined up FDI for setting up an export-oriented unit for manufacturing of other fabrics.

These are encouraging developments which need to be harnessed for increasing India’s share in the global market. Entry of these foreign firms in the T&A sector can become an important step towards improving competitiveness and efficiency of Indian manufacturers, provided they pave way for others to follow.

However, low labor cost alone may not be sufficient to attract export-oriented FDI as there will always be other low-cost production sites. Industry-level efforts are also required to increase competitiveness. Investment in information technology in order to reduce lead times and developing marketing professionals is essential. Developing indigenous sources of textiles, accessories and other inputs is also crucial to export success.

An important factor for companies to keep in mind is to be wary of blindly following the inorganic route for achieving quick growth and rush into inorganic deals like M&As. Some of them may not need to adopt this path and some of those who would need it, have to be fully prepared for the challenges involved.

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An Overview

“Healthcare is one of the few industries which has time and again shown itself to be the last to be impacted by the downturn in the economy.”

With the clouds of economic uncertainties looming over the world, today few countries or sectors are immune to this downturn. Global demand is slumping as the developed world plunges into what could be their deepest recession since the 1930s. However, a few industries have been relatively insulated from this downturn. Healthcare is one of these and has time and again shown itself to be the last to be impacted by the downturn in the economy.

In the Indian healthcare sector, there is no data to substantiate the correlation between a slowdown in the economy and its impact on healthcare sector. However, this has been well documented in the developed economies. When the dot com bubble burst in the US in the 1990s, healthcare was the only sector where the number of jobs increased in the coming decade. Over 1.1 million jobs were added in healthcare while every other sector saw a reduction in the number of people employed.

The fiscal concessions given in the budget for a tax holiday in tier-II and tier-III cities has already resulted in a flurry of activity in these towns. Besides the current hospital operators, corporate houses and international healthcare chains are also looking at the prospect of taking their branded models of healthcare delivery beyond the current urban conglomerates in which they operate. The experience of players who have ventured into these towns has been very encouraging.

Besides hospitals, other emerging healthcare segments like healthcare retail, diagnostic chains, assisted living centres, day care ambulatory surgery clinics and centers for alternative medicine are increasingly attracting investments. The renewed focus on Private Public Partnerships (PPP) brings together the operational efficiencies of the private sector and the mammoth infrastructure of the public sector, surging growth in the dormant public sector hospitals.

The accessibility to quality healthcare in the private sector which was limited due to the high costs involved, is dramatically changing with the advent of health insurance as the preferred tool to finance healthcare expenditure. The phenomenal growth of health insurance players coupled with the entry of newer players will help in further penetration of this product.
The proposed corporatization of medical education will address one of the roadblocks to the growth of the shortage of trained manpower. The renewed focus of the new US administration to provide healthcare benefits to over 40 million uninsured citizens would aid the growth of Medical Value Travel (MVT) and the medical outsourcing market.

Though there is a temporary slowdown in investments in Indian healthcare industry, past investment figures as well as future studies reveal tremendous potential for healthcare in the coming decades. According to Emerging Markets Private Equity Association (EMPEA), PE investments in India’s healthcare sector have tripled from US$ 126 million in the first half of 2007, to US$ 459 million between January and June 2008.

Given the highly skewed demand-supply equation, we expect healthcare to sustain its growth even in the new paradigm of muted economic growth.
Public Private Partnership: The Current Imperative

Indian healthcare is witnessing a renewed interest in PPP as a measure to spur growth in this sector. Internationally, the PPP have proved to be successful models in providing care. The UK government has used PPP in financing, construction and facility management for many public hospitals. In Australia, this model has been introduced in more than 50 public hospitals through several different mechanisms.

For a PPP to be successful in healthcare sector, especially in a developing economy like India, there has to be a perfect synergy between the two partners supported by their respective strengths.

PPP models are primarily based on a harmonious arrangement between the public sector’s objective of providing equitable healthcare services with the private sector’s aim of building a scalable and financially sustainable business model. Furthermore, the benefits of such a partnership ensures economies of scale, exchange of skills and expertise between both the sectors. This would lead to optimum utilization and equitable provision of public resources which till date has been a challenge.

This change in role is further strengthened by the evaluation of individual advantages the two sectors hold. While the Government is in the best position to finance the infrastructure, the private sector excels in operations and management, hence improving the overall quality of the care. As shown in Exhibit 4.

Exhibit 3:
Advantages of PPP Model:
- Economies of scale
- Improved quality and efficiency
- Exchange of skills and expertise between the public and private sector
- Optimum utilization of public resources
- Equitable healthcare
- Broad range of services

Exhibit 4:

The Challenges Today:
- Absence of a governance structure
- Less accountability
- Unclear deliverables/KRAs
- Political intervention
- Ambiguity in the process of identification and insurance cover
Corporatization of Medical Education: The Impact

One of the pivotal factors to sustain the projected growth of the healthcare industry in India will be the availability of a trained healthcare workforce. The quality and density of health work has a direct correlation with the positive health outcomes of any country. With a view to increase the skill set base, the Government is now looking at allowing corporate entities to venture into medical, nursing and paramedical education.

The healthcare manpower added every year is not sufficient to keep pace with the growing healthcare demand today. India produces over 30,000 medical graduates every year from over 290 medical colleges, and only 12,000 post graduate seats are available. With this small annual medical manpower entering the mainstream, one can only imagine the lamentable gap between the educational capacities in this sector versus the requirements. To fulfill the additional requirement of health manpower, it is essential to explore a range of partnership/collaboration options with the private/corporate sector.

Emergence of AMC Model
The Government’s initiatives and changing guidelines will spur the growth of Academic Medical Centers (AMCs) in future. AMCs are the conglomeration of research, direct patient care & education facilities. Such an integrated clinical setting facilitates delivery of high quality care, better training and research. This gives it a distinct edge over stand alone medical colleges. Such settings also help attract the best talent pool by offering them a broader perspective to their work. Considering the huge shortfall of doctors, nurses and paramedics, the healthcare industry is now looking at this model with a hopeful eye on filling this vast need gap.

Exhibit 5: Reaching the Global Average
To meet the global average of 1.24 physicians and 2.56 nurses per thousand population in coming 15 years, India needs to open 600 medical colleges (100 seats per college) and 1500 nursing colleges (60 seats per college).

Exhibit 6:

What is Lacking in Medical Education?
- Insufficient seats both at graduate and post graduate level
- Inadequate infrastructure
- Lack of qualified faculty base
- Outdated curriculum
- Inadequate exposure to technology
- No mechanism to monitor continuous medical education

What are the Entry Barriers for Corporates?
- As of now, only trusts and societies in private sector are entitled to establish a medical college
- There is a statutory requirement for a single plot of 25 acres of land for establishment of medical college
- Annual seats for the students for graduate and post graduate courses needs to be optimized
Med-polis: The Emerging Healthcare Cities

The concept of a medical or health city stands unprecedented in India. This is basically a one stop shop for all the healthcare needs of an individual, besides having other components like educational institutions, hospitality, retail, commercial and residential complex sprawled across acres of land.

Medical cities bring along all components of healthcare, education, research and skill development under one roof, thereby increasing the quality of care and services offered to the patients and other consumers. It provides a great opportunity to the providers to setup a world class infrastructure within the reach of the target population.

In what could be the beginning of a healthcare renaissance, medical cities could change the way healthcare delivery, medical education and research & development is conducted in India.

The aim of a Med-polis is to create an eco-system that offers medical services through super specialty hospitals of international standards, ancillary facilities, research institutions, health resorts, rehabilitation centres and residential apartments. It will translate into a self sustainable township, training medical manpower, generating jobs in various disciplines and ensuring overall development of the region. It provides an opportunity to bring all stakeholders i.e. the providers, the professionals, the researchers, the service facilitators and the care seeker under one roof. Such a confluence can itself provide a platform leading to new business avenues.

Given the favorable factors in India, we envisage the growth of Med-polis resulting in steady delivery of healthcare.

Exhibit 7: Texas Medical Center
- World’s largest medical district
- 46 institutions (specializing in every imaginable aspect of health care) that includes 13 renowned hospitals and 2 specialty institutions, 2 medical schools, 4 nursing schools, and schools of dentistry, public health, pharmacy, and virtually all health-related careers
- Clinics, offices, and other facilities in neighborhoods throughout Houston and one of the major contributor to Texas economy

Exhibit 8: Healthcare City: Concept

Upcoming Projects in India
- Healthcare City in Hyderabad Economic City
- Mihan Healthcare City in Nagpur
- Global Healthcare City in Gurgaon
- Fortis Medicity in Gurgaon and Lucknow
- Chandigarh Health City in Chandigarh
Majority of ailments (almost 80%) can be diagnosed and treated completely in secondary care set-ups. Traditionally, Indian hospitals have opted for a multispecialty format with a focus on tertiary care. While this has been a successful model in the metros, its replicability in tier-II and tier-III cities is limited. Moreover, there is a negligible presence of organized secondary care providers in these markets.

There is a latent demand for quality healthcare provider in India’s smaller cities & towns. Besides their own population, these towns also attract a large proportion of patients from rural areas. It is estimated that more than 46% of the patients travel over 100 kilometers from small towns to these facilities to seek proper medical care. (Source: Technopak’s India Healthcare Trends ’08).

The five year tax holiday announced in the last budget for hospitals having more than 100 beds, will give a further impetus to the growth of hospitals outside the metros. Thus, we envisage the major growth of hospital beds in the secondary care delivery format to be in tier-II & tier-III cities.

**What is Lacking in the Current Secondary Care Facilities?**
- Few organized healthcare players
- Uniform care delivery
- Standardized clinical protocols
- Transparency in charged tariff

**Typical Financials of a Secondary Care Hospital:**
- Cost per bed ~ US$ 95,000 (without land)
- Capex to Annual Revenue = 1:1
- EBIDTA Margins ~ 25%
- Breakeven time ~ 18 months

Given the clinical service mix, lower capital expenditure and appropriate technology, this model insures itself against the risk factors which are likely to afflict a bigger facility.
Designing Cost Effective Infrastructure: A Green Approach

Cost effectiveness implies optimum utilization of time and resources to achieve better quality infrastructure as compared to that achieved with conventional methods. Cost effective does not imply ’Low-Cost’.

Cost effectiveness can be achieved by adopting strategies and measures that encompass all possible elements such as: Human resource, technologies, operations and design & planning. Organizations such as JCI (Joint Commission International) provide guidance on achieving these project goals.

Project management can be an effective tool in optimizing performance at every stage of the project in addition to offsetting any additional costs or delays that may occur elsewhere. Along with ‘Inception Management’, a project manager should at all times, know the project cost and its budgetary implications. This “Design-to-Cost Model” approach is very efficient in controlling costs at every stage of the project. During ‘Design Management’, with appropriate design and planning, efficiencies for the complete life cycle of the project can be achieved. Healthcare infrastructure being largely operations and services driven, this stage becomes extremely important. ‘Procurement Management’, which encompasses the sourcing and purchasing of goods, materials and services, helps in efficient resource management and contracting. The stage of ‘Construction Management’ involves good phasing strategy, proper scheduling for every activity and correct identification of staging areas. ‘Facility Management’ provides for total integrated service solution encompassing both building fabric and services.

Key Features of Design-to-Cost Model:
• Understanding of clients affordability viz-a-viz project vision
• Understanding and integration of First Cost and Life Cycle Cost models for a project
• Understanding of the cost drivers of a project
• Establishment and allocation of target costs for every resource or component of project
• Value engineering for better alignment of target and actual cost estimates

Exhibit 10: An Integrated Approach Towards Cost-Effective Design

Exhibit 11: Sustainability

Exhibit 12: Key Features of Design-to-Cost Model:

Exhibit 13: Cost Benefits

On average, green buildings are 28% more efficient than conventional buildings and generate 2% of their power on-site (photovoltaic)

An average kWh reduction in energy use of 30% and an average peak kW reduction of 40%
Newer Partnerships: Catalyzing Growth of Healthcare Delivery

Given the highly skewed demand supply equation, Indian healthcare needs to look at innovative models to propel its growth.

One such concept is the Propco/Opco arrangement. In this, one party owns the property assets and leases it to another party that operates it. The advantage of such arrangement is that the entire business generates profit from the property leased and the operating profit left after rent. Moreover, the capital expenditure is lower for the operator.

Another important model is the Build-Lease-Transfer (BLT) model which is a variant of Build-Operate-Transfer (BOT) model. In BOT, the private player builds & operates the facility on Government’s or another private player’s land and after a fixed period of time, transfers the ownership to that player. Whereas in BLT, the private player builds and then leases the facility to the Government or a private player for a fixed term such as 25 years after which the ownership is transferred to that player. A modification that can be brought about here, is a joint venture between the asset owner and operations owner. BLT ensures better co-ordination, risk allocation and speedy completion of the project.

To answer the high land cost obstacle, Real Estate Investment Trusts (REITs) can be brought into picture. REIT is a tax-advantaged entity designed specifically to own and sometimes operate real estate. REIT pays no corporate taxes but must distribute at least 90% of its taxable income to shareholders annually in the form of dividends. The guidelines for notifying REITs is yet to take off in India.

Exhibit 15:

<table>
<thead>
<tr>
<th>Various Partnership Models</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Build-Operate-Transfer (BOT)</strong></td>
</tr>
<tr>
<td>BOT is a form of project financing, wherein a private entity receives a franchise from the private or public institution to finance, design, construct, and operate a facility for a specified period, after which ownership is transferred back to the funding entity</td>
</tr>
<tr>
<td><strong>Built-Lease-Transfer (BLT)</strong></td>
</tr>
<tr>
<td>Ownership of the infrastructure facility is transferred to the Government upon completion of construction, and the concessionaire is granted the right to operate the facility and receives Government payments based on its operational performance for a specified period of time</td>
</tr>
<tr>
<td><strong>Real Estate Investment Trust (REITs)</strong></td>
</tr>
<tr>
<td>A corporation or trust that uses the pooled capital of many investors to purchase real estate and manage income property and/or mortgage loans</td>
</tr>
<tr>
<td><strong>Propco/Opco</strong></td>
</tr>
<tr>
<td>Consists of two entities which focus on their core competence; Propco – develops the property and Opco- operates the property</td>
</tr>
</tbody>
</table>
Appropriate Technology: Optimizing Healthcare Delivery

Medical equipment is one of the components that takes a large piece from investment in healthcare. No other industry uses such a wide range of technology for its operational efficiency. Therefore, it is becoming increasingly important to manage medical equipment to contain costs, and yet be able to improve efficiency, quality and performance of the equipment being used.

The first step in this management process is to make sure the hospital buys the most appropriate equipment. Planning is the initial step in the overall management of that medical equipment in a healthcare institution.

The entire equipment planning process needs to be managed and overlooked by an advisory group in consultation with management, administration, physicians, finance and accounting, biomedical engineering, construction and services team, information technology (as required) and clinical specialty (as required).

The cost of medical technology needs to be considered over its complete life cycle as has been depicted in the adjoining graph. It has been estimated that proper medical technology planning can bring down medical equipment life time costs by about 20%.

Exhibit 16:
Medical Technology: The Imperatives
- One of the major components of capital expenditure in hospitals
- High cost of operations and maintenance
- Increased importance in determining clinical outcomes
- Fast rate of obsolescence
- Maintaining cost over the life cycle
- Plan for obsolescence and replacement
- Increasing failure rate with time

Exhibit 17:
Medical Equipment Lifestyle - Bathtub Curve
- Decreasing Failure Rate
- Constant Failure Rate
- Increasing Failure Rate

Exhibit 18:
Steps in Equipment Planning:
- Determination of equipment needs and budget pricing
- Development of room by room equipment lists and refinement of lists through design - development
- Preparation of medical equipment RFP
- Inventory, assessment of existing equipment and inventory allocation
- Coordination with project management, architects, materials management etc
- Vendor interaction
- Determination of equipment specifications and model specific information
- Preparation of medical equipment RFP

Exhibit 19:
Key factors to be considered during the planning process to acquire appropriate technology:
- Ownership
- Budget
- Catchment area
- Level of care
- Specialty
- Type of hospital
- Volume of patients
- Anticipated revenue generation
Lean Thinking: Improving the Bottomline

In spite of the recent economic recession hitting the markets across the globe which has caused a domino effect in almost all the industries, there is one industry that remains largely insulated against any kind of slowdown, and that is Healthcare. The healthcare industry including hospitals is still making profit and generating revenues but definitely facing margin erosion, which can be attributed to the rising manpower and consumables costs.

Hence in today’s scenario, to ride the storm of recession, the best advised practice would be reduction and minimization of waste (process/material) by adopting “Lean” methodology.

‘Lean Thinking’ which was principally limited to manufacturing industries, is now in vogue in many service sectors including healthcare. Lean thinking begins with driving out waste so that all work adds value and serves the patient’s needs. Lean thinking in healthcare organization can lead to positive impact on productivity, cost, quality, and timely delivery of service.

### Exhibit 20: Common Areas for Waste Reduction in Healthcare

<table>
<thead>
<tr>
<th>Waste Type</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overproduction</td>
<td>Lab reports printed when not needed</td>
</tr>
<tr>
<td>Movement</td>
<td>Walking to get equipment and medication, chart, hunting for other care members</td>
</tr>
<tr>
<td>Inventory</td>
<td>Stock of forms, supply closets, drawers full of outdated items</td>
</tr>
<tr>
<td>Processing</td>
<td>Capturing redundant information upon admission, multiple recording and logging of data, writing by hand rather than via PC</td>
</tr>
<tr>
<td>Waiting</td>
<td>Patient waiting rooms, waiting for call backs, waiting for equipment for supplies</td>
</tr>
<tr>
<td>Transportation</td>
<td>Patient moving from location to location, equipment moved to patient location, information triplicates</td>
</tr>
</tbody>
</table>

### Exhibit 21: “Lean Thinking basically means doing More with Less.”

Lean principles come from the Japanese manufacturing industry. The term was first coined by Professor James P. Womack and consultant Daniel T. Jones

**ADVANTAGES**

- Improves patient outcomes and satisfaction
- Enables fast and efficient healthcare services for the patient
- Shorter patient lead-times
- Empowered and motivated staff
- Improves staff satisfaction
- Flexible, educated, cross-trained staff
- Continuous improvement culture - sustainable and long-term
- Improved cost effectiveness

### Exhibit 22: Lean Thinking Approach

**CHECK**

Understand current performance - “what and why” using staff who do the work

**PLAN**

Identify levers for change & experiment to get to perfect

**DO**

Implement the changes
Clinical Protocols: Standardizing Care

The standardization of healthcare practices in terms of clinical protocols and actual delivery, produces superior outcomes, reduces error probabilities and provides transparency on the effectiveness of the treatment.

In many large medical practices, the frequency of medical staff rotations is high, resulting in difference in the clinical experience and judgment leading to variations in treatment plans. In the absence of disease-specific protocols, each clinical provider relies upon his/her own level of expertise and judgment when approaching patient education, assessment, and treatment. This resulting variability in inpatient care leads to development of clinical protocols defining standards of practice.

The clinical decision-making is no longer the exclusive domain of the healthcare practitioners. Consumers, as patients and as business providers, have more influence over the decision-making process and greater access to information regarding health care practices and measures of quality. The providers are being held more accountable for their clinical decision-making and are being scrutinized on the use of inpatient stays, procedures, tests, and technologies.

Adoption of clinical protocols in India will result in standardization of care and cost reduction.

Exhibit 23:
Clinical Protocols: The Imperatives
- Better direction for health care policy development
- Stimulus for professional self-improvement
- Comparative information for consumers to support a “buy right” strategy
- Development of performance-based education, certification & recertification processes
- Licensing based on compliance with standards
- Reimbursement decisions based on guideline compliance
- Basis for shared patient and physician decision making
- Framework for malpractice decisions
- New textbooks organized around guidelines

Exhibit 24:
Types of Clinical Processes that Merit the Development of Protocols:

1. High risk procedures and surgeries such as CABGs
2. Expensive procedures, such as organ transplantation or complex diagnostic work-ups
3. Procedures or diagnostic work-ups for which significant overuse has been documented such as back surgery or cesarean section

According to a recent American Survey, adoption of Clinical Protocols can reduce healthcare costs by 25%.
Ever since the opening of health insurance to private sector, there has been a phenomenal increase in health insurance and its extent of cover. The increase in the incidence of lifestyle diseases coupled with the rising cost of health care, has further spurred the growth of this sector. This has led to an exponential rise in the number of people purchasing the health insurance products.

There has been a 60% growth in the premium of health insurance in the last year which makes it the fastest growing segment in general insurance portfolio.

Over the years, there has been a shift in insurance companies policy in using Third Party Administrators (TPA). TPAs were envisaged as an interface between the insurance companies and the consumers for better claims management and value added services such as cash-less hospitalization. However, recently we have seen that most insurance companies prefer to keep this role in-house. This is principally because services from the TPA have been below expectation and the high volume has made it cost effective for the insurance companies to settle claims themselves. TPAs need to reinvent themselves to add value to the claim settlement process. There may also be a case for revisiting the regulations.

Hospitals across the country will soon be rated based on the standard of medical facilities and healthcare they provide and the patients will be able to make an informed choice. The Insurance Regulatory Development Authority (IRDA) and the Health Ministry are taking active steps to implement this.

Health Savings Account (HSA) could be a good alternative for health care financing in India. Already successful in Singapore, in this mechanism some portion of the individual’s income is deposited in HSA. This saving can only be used by individuals for his/her medical needs.

### Exhibit 25:
Population with Voluntary Health Insurance (in Millions)

<table>
<thead>
<tr>
<th>Year</th>
<th>2008</th>
<th>2013</th>
<th>2018</th>
<th>2023</th>
<th>2028</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value</td>
<td>30</td>
<td>80</td>
<td>210</td>
<td>420</td>
<td>680</td>
</tr>
</tbody>
</table>

### Exhibit 26:
Insurance companies settling claims by themselves
- Bajaj Allianz General Insurance
- Reliance General Insurance
- ICICI Lombard
- Cholamandalam MS General Insurance Company
- Star Health and Allied Insurance Company

### Foreign Direct Investment (FDI) to increase from 26% to 49%
- The capital flow would increase in the sector
- Top international health insurance companies enter into India
- More stand alone health insurance companies may come up
- Better products and processes

### What can we expect in 2009?
- Out-patient consultation, dental covers with some rider policies
- Enhanced daily hospital cash benefits
- More comprehensive critical illness cover
- Better disease management cover
- Increased overseas medical insurance benefits

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Rebuilding to Last

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There is no doubt anymore that the world economy has never seen the kind of turbulence and the all-around collapse of stability, not to mention the collapse of prospects of growth in the near future, as we are seeing today. All the G-7 nations, and then many more of the other developed nations, are simultaneously poised to register a negative growth of GDP. In fact, of all the major economies, China and India are the two that are still likely to post 5% or higher growth in 2009 and 2010.

Internationally, the collateral damage from this contagion is no longer confined to the financial services institutions and the real estate sector only. The manufacturing sector has been the next to be impacted with shrinking or even a virtual collapse of user demand. This impact on the manufacturing sector is even pronounced in those countries that have a very high dependence on exports including China, Korea, Taiwan, and even Japan. As we also now know, the world economy is much more interlinked than what mere trade and capital flow movements may have indicated till some time ago, and hence, it is a matter of time before every other sector of economic activity across the world starts feeling the impact of these crises.

Having said this, while most of the developed world is fully occupied with fighting current and new fires, India and Indian businesses still have the luxury of thinking about building for the future. The Indian financial services system has been tested hard but still seems to be in relatively good health and seems to be functional. There is adequate liquidity available in the market for day-to-day running of most businesses, and there is still some availability of risk capital and equity capital to fund new businesses too. There may be some uncertainty on the political front but it must be also kept in mind that India has now seen coalition governments both at the Centre as well as in states for many years now, and there is no reason to despair too much on account of which coalition comes to power in May this year. The country will still be governed if not optimally, and the economy will certainly occupy the highest attention of the ruling coalition irrespective of its ideology.

Indian businesses should see this global meltdown and its collateral damage in India on their own businesses in a pragmatic way. It starts with the acceptance of the reality that their businesses have suffered or are suffering damage already and some more damage may yet be in store. Once this reality has been accepted, and whatever measures that can still be taken to minimise this damage are still being taken, the business leadership must urgently get down to the task of thinking about the future. If they believe in India’s future, then the task of building (or rebuilding) a business for that future should be an encouraging and exciting one. This encouragement comes from many oft-stated but still fundamentally valid reasons including the overall composition of the Indian economy, its demographic divide potential, the pent-up internal demand for extraordinary levels of economic activity be it related to physical or social infrastructure, housing, agriculture and agro businesses, and a complete array of consumer goods and services.

Building from scratch, or rebuilding extensively damaged structures, allows the luxury of building businesses for the future. This should be seen as India’s more alluring opportunity. With the end user demand potential within India for just about every category of goods and services still very enticing, businesses and new entrepreneurs should take the current pause in an otherwise frenetic business life to reflect on what the current and emerging needs of Indian consumers and customers are. Many Indian businesses expound the virtue of being customer-driven but very few have built customer-centric businesses. This would be as good a time as anytime in the future to do so.
With customer acquisition becoming increasingly harder for companies across the world, and collaboration and strategic alliances no longer anathema to anyone, Indian businesses should give a completely new look as to which link or links of the value chain they would like to directly get involved in and which they would like to outsource or manage through strategic alliances. Many Indian businesses are too vertically integrated - this would be a good opportunity to reflect hard and objectively to then decide where they should compete in the future, e.g. marketing (including branding), distribution, manufacturing, or product design.

Lastly, this rebuilding effort must be undertaken after a very hard look has been given on the fundamental cost structures of that business. Many Indian companies had become very profligate in recent years on account of easy availability of capital and a rapidly growing market. Relocating factories and administrative offices beyond the top-12 or top-20 cities, investing in hiring fresh recruits and then training on the job, energy-efficient buildings and operations, and allocating higher research budgets for manufacturing efficiencies are some areas of opportunity that must be explored vigorously.

In short, the business strategy should no longer just be to preserve but to rebuild or build from scratch.

Author
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An Overview

The Indian Hospitality Industry is one of the fastest growing sectors of the Indian economy. Riding on the economic growth and rising income levels that India has witnessed in recent years, the sector has emerged as one of the key sectors driving the country’s economy. The current market size is US$ 23 billion, accounting for 2.2% of India’s GDP. Rising disposable incomes and increase in double-income households have also played a part in this growth phenomenon.

The size of the Indian hospitality industry is estimated as a sum of revenues of two segments; revenues generated from travel for purposes such as business, leisure, visiting friends and relatives, religious, meetings and conferences, and revenue generated by consumers eating out at any form of outlet – restaurants, fine dining, Quick Service Restaurants (QSRs), takeaways, dhabas or any other form of unorganized eateries.

Indian Hotel Sector

As per an analysis by the Economy Survey of India and Technopak (2008), the Indian hotel industry is estimated at US$ 17 billion; 70% (US$ 11.85 billion) contribution comes from the unorganized sector and the remaining 30% (US$ 5.08 billion) comes from the organized sector.

The foremost contribution of the organized hotel industry comes from 5-star hotels as shown in (Exhibit 1). Despite a dip in the year 2009, an upward trend in growth of the overall hotel sector is expected, whereby the industry is expected to grow to US$ 36 billion by 2018 as shown in Exhibit 2.

There has been a consistent increase in the number of hotel rooms in recent years; growth of 5% in the last 3 to 4 years. However, this rate of increase is still not enough to meet the rising demand; further investment is required in this sector to meet this demand. The hotel sector is expected to see an estimated investment of US$ 12.17 billion in the next 2 years, and an addition of over 20 new international hotel brands by 2011.

Indian Restaurant Sector

The size of the Indian restaurant sector as shown in Exhibit 3 is estimated to be US$ 6 billion now and expected to approximately grow to US$ 10 billion by 2018. Almost 90% of the industry is unorganized; close to the remaining 10% is organized and an urban phenomenon. Despite the slow down, the unorganized sector is expected to grow at more than 5% until 2011. The organized sector, is in fact, expected to grow faster, at 20% to 25%.
Within the overall restaurant sector, the quick service restaurants (QSRs) segment will grow the fastest. Along with the entry of new international brands, transactional QSRs are expanding their presence. Café Coffee Day, Domino’s Pizza, KFC are some examples; each having remarkable expansion plans as shown in Exhibit 4.

### Phases of Growth

The growth story started in the 1980s, when the development of several hotel projects kicked off to cater to The Asiad Games in New Delhi. The hotel sector in the past used to be polarized into two extremes – luxury hotels on one end and unclassified hotels on the other. However, lately there has been an emergence of mid-segment chains of hotels.

Geographically, while initially the focus was on the major metros, the shift is now towards tier-II and tier-III towns and cities. In the future, there will be more multi-tourism in the offering, spanning different geographies. In terms of operational aspects, there has been a shift from ownership and franchise model to the management model.

The evolution of the hotel industry over the years has been illustrated below under the various heads of operations, location and proposition (Exhibit 5 to 7).
There have also been changes in the strategic focus as well as investment requirements of the hotel industry (Exhibit 8 & 9).
Phase I
While the first phase of business in the 1990s saw aggressive expansion in the 5 star hotel segment, it also saw the entry of several franchise and Hotel Management Companies (HMC). This created a big gap in the mid-market segment as the organized sector had nothing to offer to this segment. The value of land of a hotel project stood at 5% to 10% of the overall project cost in metros during this period and debt was primarily raised through conventional methods of approaching banks or Tourism Finance Corporation of India Ltd (TFCI).

Phase II
The next decade saw a shift of ownership model towards HMC, considering that the new brands entering into the business had by then made inroads and were on an expansion spree. These new entrants focused on the mid-segment – largely neglected in the first half of the cycle.

While the aggressive and rapid expansion pushed the real estate costs up, it affected infrastructure development, new businesses and at the same time new hotel projects. The growing economy did bring into limelight the advantages that a tier-II or tier-III city had to offer in terms of lower land and other costs, and the more friendly nature the State Boards acquired in order to boost this much wanted development.

This led to the entry of existing brands into this budget segment/mid-market hotel segment and also the entry of several new players. The investment needs for this cycle were achieved by both conventional means and through joint ventures and private equity investments. Existing corporations in diverse fields of business ventured into hospitality to take advantage of their brand equity.

Phase III
The coming years, post 2010, however, will see a rebound of the first phase. While the growth of budget brands will continue as that has been regarded as the long term area of growth, the industry will see a lot of consolidation. Over 65% unorganized sector is bound to go through a phase of identification – evaluation – selection, wherein the franchisee partner is bound to have its flag hoisted once the evaluation criteria is passed.

Growth Drivers
The tremendous growth of India’s hospitality industry can be attributed to a number of factors which may be broadly classified into three categories - regulatory, external, internal.
Regulatory Growth Drivers

Policy & Tax Incentives and Amendments
The Department of Tourism, Government of India has initiated a number of steps as listed below:

- Foreign Direct Investment (FDI) allowed in all construction development projects including construction of hotels and resorts, recreational facilities, and city and regional level infrastructure
- Reduction of expenditure tax for upscale hotels
- Introduction of a new category of visa - ‘Medical Visa’ (‘M'-Visa) for Medical Tourism
- Tie-up with the United Nations Development Program (UNDP) to promote rural tourism. The Ministry has also sanctioned 102 rural tourism infrastructure projects to spread tourism and socio economic benefits to identified rural sites with tourism potential
- Plans to permit the issuance of visa-on-arrival by 2009 for persons arriving from specific countries under the pilot project

Additionally, several incentives have been announced at the Central as well as State levels. These are summarised in Exhibit 10.

External Growth Drivers

Rising GDP
The Indian economy has been growing at a rate of 9.6% and 9% in 2006-07 and 2007-08 respectively. Despite the slowdown, the GDP growth for 2008-09 is at 7.1%. The hospitality sector is expected to contribute up to 2.2% to the GDP.

Foreign Direct Investment (FDI) Inflow
Of the total FDI inflow between 2000 and 2008, the hospitality sector attracted 1.56%, amounting to US$ 1.07 billion. The hospitality sector still requires over US$ 10 billion in the next two to three years for which the Government is relying partly on FDI.

Changing Consumer Dynamics & Ease of Finance
India is the second fastest growing financial cards market in the Asia-Pacific region. The credit card base in 2008 is estimated at 25 million and is expected to grow at 20% to 25% per annum. Driving this growth
is the increased use of credit cards for the purpose of purchasing, due to attractive and consumer friendly schemes being offered by various banks. Travel, hotel and dining category accounts for 35% of credit card usage as shown in Exhibit 11.

Players like Thomas Cook, Cox & Kings and SOTC have tie-ups with ICICI Bank, Citibank and Kotak Mahindra Bank to offer “holiday now...pay later” schemes, such as, the Thomas Cook-Citibank Holiday loans. These banks also offer products such as personal loans for the purposes of travel.

Increasing Domestic & International Tourist Arrivals

There has been an increase in tourist flow, both domestic as well as international. From 310 million domestic visits in 2003, the number rose to 529 million in 2007, a CAGR of 14%. The Ministry of Tourism’s vision is to achieve a level of 760 million domestic visits by the year 2011, with an annual average growth of 12%.

Foreign Tourist Arrivals (FTAs) were up by 5.7% during 2008 and clocked 5.37 million compared to 5.08 million during 2007. Foreign exchange earnings increased by 8%, to US$ 11.5 billion in 2008 from US$ 10.7 billion in 2007. The Ministry of Tourism aims to achieve a figure of 11 million foreign tourist arrivals by 2011.

Internal Growth Drivers

Demand Supply Imbalance

As per the latest available statistics, India currently has approximately 114,000 hotel rooms spread across the various hotel categories (Exhibit 13) and is facing a shortfall of 156,000 rooms. The impact of this demand and supply gap is felt by way of increased room tariff. In metro cities the room rents have simply skyrocketed. This is especially the case with mid-segment and budget hotel categories that face a large gap in supply.

Emergence of New Players

Real Estate Companies: Real estate companies have the bandwidth to invest high amount of capital required by the hospitality industry

IT Companies: IT and ITes companies are amongst the biggest hospitality clients. The need of accommodating their clients and visitors luxuriously is prompting them to maintain their own accommodation facilities

Private Equity Firms: Many private equity funds are allocating as much as 50% of their planned real estate investments into the sector as hospitality remains a highly under serviced area with a huge demand supply imbalance

Internal Diversification: Established leaders in various core sectors and at times family owned have diversified into hospitality business on a strong financial backing and an urge to make a mark in this sector

Example

In 2007 DLF Ltd. announced its equal partnership with Aman resorts. The transaction is estimated to be valued at USD 360 million

Some of these PE investments include Warburg Pincus US$ 60 million investment in Lemon Tree Hotels

US$ 60 million investments by Credit Suisse in the Park Hotels

Infosys Technologies has a country wide room inventory of 13000, Wipro has an inventory of 500 rooms

ADAG is in talks with Starwood Hotels & Resorts for bringing their luxury brand, St. Regis in India via SPV after acquiring 30% stake in Viceroy Hotels

Vijay Mallya owned UB Group diversified to set up Kingfisher Airlines and acquired Air Deccan

Source: Industry Reports, JLL Report 2008
Emerging Trends

The hospitality industry is continuously evolving catering to the diverse and ever changing consumer and market needs. Some of the emerging trends as witnessed by this industry are discussed below:

Trends in the Hotel Industry

Rapidly Changing Operating Models
Unlike in the west, the franchise model has not been a success in India. What accounted for its success in the west is a consistency in the product offering along with strict regulations by the Government on hygiene and health standards, which helped the franchise model to flourish. Recent trends strongly suggest that the franchise model of business has taken a backseat and the focus is shifting to the management model. Factors driving this operating model are:

- Hotel operation is a critical area where efficiency has to be spot on and this is where the management model stands out
- There are a number of properties developing with a fewer number of operators

Emergence of Mixed Land Usage
Mixed-use developments incorporating residential, retail, entertainment, hospitality and corporate offices are fast emerging in metros tier-II and tier-III cities. Some examples are as below:

- Kshitij introducing ‘Market Cities’, retail-led mixed-use development projects in Mumbai, Chennai and Bengaluru
- Brigade group is focusing on the ‘hotel-cum-mall’ options with Brigade Metropolis, a business hotel being developed at Chennai
- The Leela Kempinski, Gurgaon is located in a mixed-use complex of luxury residences, retail spaces, entertainment and wellness facilities

Diminishing Brand Loyalty
Guests today are becoming increasingly unpredictable and quickly switch their patronage for better deals across hotel segments, thereby reducing efficacy of many loyalty programs which hotels target towards their customers.

However, the mid-segment budget hotels are still offering loyalty programs, a trend which has lately been visible internationally as shown in Exhibit 14.

Exhibit 14: Loyalty Programs Offered by Mid-segment Budget Hotels

<table>
<thead>
<tr>
<th>Hotel</th>
<th>Loyalty Program</th>
<th>No. of Members (in Million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Starwood</td>
<td>Starwood Preferred Guest</td>
<td>9 (worldwide)</td>
</tr>
<tr>
<td>Hyatt</td>
<td>Hyatt Gold Passport</td>
<td>18 (worldwide)</td>
</tr>
<tr>
<td>Intercontinental</td>
<td>Priority Club Rewards</td>
<td>40 (worldwide)</td>
</tr>
<tr>
<td>Marriott</td>
<td>Marriott Rewards</td>
<td>20 (worldwide)</td>
</tr>
<tr>
<td>Accor group</td>
<td>A</td>
<td>Club</td>
</tr>
<tr>
<td>Hilton</td>
<td>HHonors</td>
<td>17 (Worldwide)</td>
</tr>
</tbody>
</table>

New Avenues of Growth
Service apartments, time sharing, fractional ownership, and company hotels or guest houses, have immense potential to grow. Their growth is likely to be due to increased demand of the IT, ITES, BPO, KPO, biotechnology and medical tourism sectors.

Heightened awareness of consumers towards their environment has brought into prominence the concept of ‘eco tourism’ and ‘agri-tourism’.
There is an increased flow of people, especially those from the west, to India for medical services. This has also brought into limelight the concept of ‘medical tourism’. The current market for ‘medical tourism’ in India is US$ 533 million, and is expected to grow to US$ 3.29 billion by 2018.

Diversification holds the key to survival in the long run. The hotel industry isn’t behind. Spas are appearing at hotel properties at a remarkable rate and are becoming independent profit centers. Cafes, lounges and bars which have high profit margins, are increasing their presence in several hotels.

Growth of Budget Hotels
Leading groups present in this segment are Ginger Hotels, Lemon Tree, Sarovar Hotels, Fortune Hotels, Ibis and Choice Hotels. Currently, 3 & 4 star category hotels together account for 22% of the total room supply in India, which clearly indicates a huge growth potential for budget hotels. Due to the vast demand-supply gap of mid-segment hotel rooms, an investment of US$ 835 million (Exhibit 15) is proposed for this hotel category over the next three years. Furthermore, for the Commonwealth Games in 2010, the Government is expected to provide 10,000 budget rooms while the requirement would be for 40,000 to 50,000 rooms in this category.

Trends in Restaurant Sector
Leisure & Entertainment with Eating Out
Eating out is an activity closely associated with fun. Almost 50% of Indians eat out regularly, even if it might not be an immensely entertaining activity just yet. Increasingly food and entertainment are being brought together by Indian entrepreneurs. Examples are:

- Café with Library: The Library Bar - Leela Palace Kempinski, Bengaluru; Ego Thai - New Delhi
- Café with Movie screening: The Mocha Film Club
- Café with Art Gallery: Kashi Art Café - Cochin, Le Cafe De Art Coffee Shop - Hyderabad, Monastery of Art - Boutique Art Café - Kolkata
- Sports Bars: The All Sports Bar - New Delhi; Amoeba Sports Bar - Bengaluru

Rise in Multi Specialty Cuisine
With higher inclination towards “fun” and “time with family”, and rising “individualism”, guests in a specialty restaurant are restricted to order food from just one cuisine. Hence “multi-specialty” restaurants draw a balance by providing choice while maintaining a specialty theme or cuisine and offering wider options to the consumers.

Changing Business Model
Hotels are bringing in restaurateurs under either a management contract or lease format, to capitalize on a proven restaurant concept that generates substantial revenue by attracting hotel guests and local
residents. Sagar Ratna & F-Bar at Ashoka Hotel, Delhi; Barista Crème at The Leela Palace Kempinski, Bengaluru; Café Coffee Day at Ginger Hotels are some of the examples.

On the other hand, popularity and brand value of certain restaurants within a hotel enables them to become individual profit centers and move out of the hotels. They leverage on this brand by opening chain restaurants outside hotels. Some of the popular examples are The Great Kebab Factory- originally at Radisson; ITC retailing Bukhara products.

**Front End & Back End Integration**
With increased focus on productivity and efficiency level enhancement, companies are moving towards front-end and back-end integration. ‘Farm to Fork’ concept aims at minimizing the steps from the farmer to the final consumer. Retailers are in the process of establishing direct consumer points to enable a smooth transition of goods from the farm to the consumer and enhance brand value.

## Challenges Faced

The optimism surrounding the Indian hospitality industry is not without glitches. The industry faces certain challenges, which need to be overcome to realize its potential to the fullest. These challenges may be broadly classified into 3 categories - regulatory, external and internal.

### Regulatory Challenges

**No Uniformity in Taxes & High Tax Structures**
Due to high duties and the imposition of several taxes by state governments, the industry ends up paying multiple taxes, substantially increasing overall costs, and impacting profit. India has the highest tax rate on tourism projects in the Asia Pacific region. Each state has its own criteria for luxury tax, varying from 5% to 20% on rack rate, rather than the actual rate. Luxury tax on the rack rate increases the effective rate of tax to 25% to 30%.

Similar challenges are also faced by the restaurant sector; some examples are listed below.

- Highest import duty on alcohol: Although the rates of basic duty have been brought down to 182% from 210%, the same remain at considerably high levels
- High import duty on kitchen equipment: Current import duty on kitchen equipment is 31%, plus 4% surcharge

### External Challenges

**Economic Slowdown**
Average room rates have fallen by 10% to 15%. As cost cutting measures hotels have put on hold their expansion plans for the moment. There has also been a freeze on new recruitment.

**Impact of Terrorism**
Leisure destinations like Goa and Kerala are likely to be affected more than business destinations. It is expected that average occupancy levels across major cities is likely to decline from the current average of 65% to 58%.

**Cost of Land**
Land prices in India constitute almost 25% of the cost of the property, whereas it accounts for only 15% to 20% of project cost overseas. This cost has only been on the upward side. The rising land cost and low Floor Space Index (FSI), adds to the industry’s financial dilemma.
Cost of Debt
The industry is capital intensive and has a long gestation period, with repayment of loans beyond 11 to 15 years. However, the current borrowing and lending scenario is not something to cheer about, as (a) banks are not looking at funding beyond a period of 7 to 9 years; and (b) they have made lending norms and the process more rigorous. Even the RBI has stopped foreign currency loans under its External Commercial Borrowing (ECB) guidelines to the hospitality industry, thereby further choking debt funds. Moreover, since the sector has not yet received ‘Infrastructural’ status, this has impacted government allocations and subsidies towards the sector.

The only silver lining remains in the fact that there has been no major impact on the private equity fund flow into the country as these funds prefer to stay invested for the longer term.

Internal Challenges

Skilled Manpower Shortage
The hotel sector is labor-intensive with an average employee-to-room ratio of 1.8 : 1 in India, compared to 1.5 : 1 globally. However, there exist a huge gap in manpower availability, especially in the budget hotel segment.

Currently, there are 25 ‘Institutes of Hotel Management’ and another 180 Institutes providing Degree/Diploma courses in F&B service, F&B production and Housekeeping. These training facilities produce approximately 10,500 graduates in various courses every year. However, this does not solve the crisis faced by the budget hotel segment, given the preference of graduates for the 5 star segments.

Other reasons contributing to the manpower worries include:
• Bright and educated younger generation has never considered hotel industry as a progressive employment option
• There is more demand overseas for trained hospitality workers

Emerging Opportunities

New Avenues of Growth

MICE
‘Meetings, Incentives, Conventions and Events’ - is a new concept which many hospitality companies including travel trade are adapting to. The inbound MICE segment is growing at 15% to 20% annually. Countries like Singapore and Malaysia have grown exponentially in the MICE segment. India gets close to 0.96% share of the world’s meetings which though miniscule, has ample room for growth.

Mall-Hotel a Win-Win Scenario
There is shortfall of 30,000 to 40,000 rooms in the budget category for Commonwealth games 2010. In this scenario, the mall-hotel arrangement is a win-win situation for both hoteliers and developers. Smaller hotels in malls would lead to lesser investment due to decrease in real estate cost and lesser inventory.

Investment in Hospitality Institutes
There is scope for more hotel groups to come up with their own institutes or programs to meet the demand for trained personnel in the industry.

In order to achieve this, international linkages have been formed for the qualitative growth of these institutes; the National Council has signed a Memorandum of Understanding (MoU) with VATEL International Business
Growth of Group Purchase Organizations (GPO)
Currently, in India there is no major domestic player that can leverage the purchasing power of a group of businesses to obtain discounts from vendors based on the collective buying power of the GPO members. There is an annual operating expenditure addressable market of US$ 1 billion in the current year and it will be US$ 1.2 billion by 2010 and US$ 1.5 billion by 2013. There will be a total capital expenditure (Furniture, Fixtures & Equipment (FF&E)) addressable market of US$ 4 billion over the next 5 years.

Based on an assumption of 10% market share and a 2% administration fee of this value, the GPO revenue potential from FF&E categories would be US$ 8 million over the next 5 years. Revenues from annual administration fees from operating expenditure category would be US$ 2.45 million in 2010 and US$ 3 million by 2013.

Home Meal Replacement Market
The market for ready-to-eat / ready-to-make products in India is growing tremendously. Factors such as increased time pressures, busy lifestyles and increase in the number of dual income households have led to a steady growth in sales of ready-to-eat packaged food. The ready-to-eat food sector is growing at 20% annually. Today, the market is worth US$ 15.6 to US$ 17.8 million (discounting the larger ready-made market comprising juices, noodles, etc which together put the market size to US$ 222 million).

There is also a rising demand for frozen food. As per industry estimates, by the year 2009, the Indian market for frozen and processed foods products will be US$ 148 million.

Innovative Operating Models
Hotels are adapting to innovative operating models by bringing in external brands of restaurants, spas and lounges on lease or management contracts. Success and popularity of restaurants, spas and lounges within hotels enables these players to become individual profit centers and move out of hotels as separate chains and thereby expand their presence in the market.

Key Recommendations
The hospitality sector in India has tremendous growth opportunities. However, there are changes/amendments required in the rules and regulations to provide momentum for growth. These are:

• The Government should accord the ‘Infrastructure status’ for hotel sector under Section 80 I/A of the Income Tax Act, 1961. The sector should be given full benefits of concession for infrastructure facilities available to other sectors like airports, seaports, power projects and gas distribution networks.

• Section 32 of the IT Act should be amended to restore the depreciation rate to 20%. The additional depreciation applicable to ‘plant & machinery’ under section 32 1 (ii a) should also be allowed to hotels that make heavy investments in plant and machinery.

• The FSI norms need to be rationalized across the country in order to allow maximum utilization of space and thereby making rooms affordable. Most comparable cities across the world offer better FSIs than their Indian counterparts. New York offers up to 15 FSI while NCR region offers a dismal 1.75 FSI.

• The abolition of service tax on tour packages will also help push tourism in the country. A uniform tax structure for rooms and food & beverage across the country is much required.

• An extension of tax holidays on a pan India basis and not just limited to the NCR region.
Poor infrastructure including power shortages, bad roads, inadequate water supply and unreliable communications has a direct impact on the growth of the hospitality industry. While the airports are now going for aggressive face uplift, work has to be done to ensure consumer experience is uniform across the country.

Apart from changes in the regulatory system, the industry must also take the following steps in order to address and tackle issues they face.

- The annual demand for trained manpower in hotels and restaurants is likely to touch 29,000 by the year 2010. However, currently only 10,500 students are being trained in hotel management and food craft annually. Hotel-run-institutes besides addressing part of this shortfall, will also tackle the escalating attrition rates, currently growing at 10% per annum, on a base of 18% to 25%, hotels in metros.

- Uniformity in price points across various seasons and a competitive pricing compared to the South Eastern Asian destinations will definitely help in getting more tourist arrivals in the country in the long run.

The future development of the hospitality industry is through Public Private Partnership (PPP) across various tourism projects in the country. PPPs enable the public sector to benefit from commercial dynamism, the ability to raise finance in an environment of budgetary restrictions, innovation and efficiencies harnessed through the introduction of private sector investors who contribute their own capital, skills and experience.

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Under the Lens - India’s Food & Agriculture Basket

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Background

While the Indian economy’s growth in the recent years, has been propelled by the growth of the service and manufacturing sectors, agriculture still plays a significant role by contributing 17% of the GDP and providing employment to 60% of the population. With the increasing focus and investments from the large national and international food and retail companies, the sector is bound to grow much faster in the coming years. As this sector has a strong social implication, it has also been accorded a high priority status by the Government, which is facilitating its growth by charting favourable initiatives at different policy levels. The changing consumption dynamics coupled with the growth of modern retail, the processed food industry offers tremendous opportunities for all stakeholders in the areas of production, processing, marketing, supply chain, infrastructure development, technology up gradation and education.

Food Industry Overview

The size of the Indian food industry is estimated at about US$ 236 bn. It is growing at about 5% year on year (YoY) and will reach US$ 314 bn by 2015. The processed food segment’s contribution is currently at about 43% i.e. US$ 120 bn, this is expected to grow much faster, and contribute about 50% to the total food market by 2015. The proportion and value of each sector in the Indian food processing industry is shown in Exhibit 1.

The processed food industry is highly fragmented and is dominated by the unorganized sector. The organized food processing segment contributes about 30% of the market; however with the entry of large players both domestic and international, the market is expected to growing at 25% per annum and will account for 40% of the market by the next 5 years. At the moment the Indian food market is still dominated by the staples like wheat, rice and pulses followed by fruits & vegetables and dairy products with minimal value addition before being consumed by the masses. The production of each sector amount and it’s standing in the world is summarised in Exhibit-2.

Though India has a strong agricultural production base, the wastage in the sector is very high. The lack of storage & processing facilities leads to significant wastage, especially in categories like fruit and vegetables with an estimated wastage of about 35% (estimated value of US$ 8 bn annually). The level of food processing varies considerably across sub-sectors in the country. In the case of perishables like fruit and vegetables, only 2% of production is processed, it is more than 90% of non perishable products such as cereals and pulses. However, the processing in staples involves very little value addition, and is mostly confined to grading, cleaning, milling, and packing; with negligible use of additives, preservatives, and flavours etc.

Exhibit 2:

<table>
<thead>
<tr>
<th>Category</th>
<th>Production per Annum</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Milk</td>
<td>90 million tons</td>
<td>Highest in the world</td>
</tr>
<tr>
<td>Fruits &amp; vegetables</td>
<td>150 million tons</td>
<td>Second highest in the world</td>
</tr>
<tr>
<td>Livestock</td>
<td>485 million</td>
<td>Largest in the world</td>
</tr>
<tr>
<td>Food grain</td>
<td>204 million tons</td>
<td>Third highest in the world</td>
</tr>
<tr>
<td>Fish</td>
<td>6.3 million tons</td>
<td>Third largest in the world</td>
</tr>
<tr>
<td>Poultry</td>
<td>489 million</td>
<td>-</td>
</tr>
<tr>
<td>Eggs</td>
<td>45,200 million</td>
<td>-</td>
</tr>
</tbody>
</table>

Source – Ministry of Food Processing
Sector Wise Production Level
The diverse agro-climatic conditions in India, offer huge potential for a wide variety of crops including cereals, pulses, fruits and vegetables all round the year. Also, India is a leading producer of crops like Basmati rice, Alphonso mango, cumin, cardamom, tea, coriander, cashew and a range of vegetables and fruits, which have a global demand. In addition, India has the advantage of the low cost of production, which provides an unbeatable competitive edge in the global market place.

Major Initiatives

Government Initiatives
The Ministry of Food Processing Industries (MoFPI) is the nodal agency established by the Government to ensure development of the food processing sector in India. The key objectives of the MoFPI includes improving utilization & value addition of farm produce, minimizing wastage, technology introduction & upgrades, promoting R&D, initiatives for policy development and development of critical infrastructure for supply chain.

With an intention to grow the food processing sector, the Government has made a sharp increase in the plan outlay and expenditure in the last couple of years and has approved outlays of over US$ 1 bn in the 11th plan. Exhibit 3 give the details of approved outlay for the 11th Plan.

<table>
<thead>
<tr>
<th>S. No.</th>
<th>Scheme</th>
<th>Outlay (US$ bn)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Scheme for infrastructure development</td>
<td>0.62</td>
</tr>
<tr>
<td>2.</td>
<td>Scheme for technology up-gradation/establishment/modernization of food processing industries</td>
<td>0.14</td>
</tr>
<tr>
<td>3.</td>
<td>Scheme for quality assurance, Codex standards and R&amp;D</td>
<td>0.06</td>
</tr>
<tr>
<td>4.</td>
<td>Scheme for human resource development</td>
<td>0.015</td>
</tr>
<tr>
<td>5.</td>
<td>Scheme for strengthening of institutions</td>
<td>0.077</td>
</tr>
<tr>
<td>6.</td>
<td>Scheme for up-gradation of quality of street foods</td>
<td>0.042</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td><strong>0.96</strong></td>
</tr>
</tbody>
</table>

Policy Initiatives
To help promote the food processing industry, the Government has over the years taken various policy initiatives. Key policy initiatives include:

- Exemption of most processed food items (except items reserved for SSI & Alcoholic Beverages) from purview of licensing under the Industries (Development & Regulation) Act, 1951
- Food processing industry covered under priority sector bank lending
- Foreign investments of up-to 100% allowed under the automatic route
- Excise & Customs Duty reduction in processed items & plant and machinery
- Income Tax holiday for certain categories of processing industries
- Delegation of licensing powers to regional authorities
Infrastructure Initiatives

One of the major factors hindering the growth of the food processing industry relates to inadequate infrastructure. To meet this challenge of inadequate infrastructure, the MoFPI in its 10th Plan has focused on developing various food related infrastructure that include:

**Food Parks**
This initiative of the Government is targeted to provide common infrastructure for the industry. As per the 10th Plan schedule a total of 56 Food Parks were planned. The 11th Plan has a target of establishing 30 mega food parks across the country. The key objectives of this initiative includes providing infrastructure, support value addition of agricultural commodities, establish raw material supply chain, induction of latest technology, integration of complementary resources and improved quality assurance.

**Integrated Cold Chain Facility**
This scheme is targeted to improve viability of cold storages and add capacity.

**Packaging Centre**
The Government intends to develop packing centers facilities so as to help enhance the shelf life of food products and bring international acceptability.

**Value Added Centre**
The value addition centre’s are intended to bring about value addition leading to higher realization along with enhancing shelf life.

**Irradiation Facilities**
The meet the challenges brought about by infestation, the Government has plans to setup irradiation facilities.

**Modernization of Abattoir**
For the 11th Plan, the Government is planning a comprehensive scheme for modern abattoirs across the country.

Growth Drivers

The changes in the consumer preferences and inclinations have had a definite impact on the level and directions of food processing. The reasons for the change in the Indian consumer are:

**Rising Income Levels**
In India, the per capita income has almost doubled in the last 7 years and is now about US$ 1000 per annum. The consistent rise in the middle class income has resulted in a consuming class with higher disposable income.

**Changing Food Habits**
With growing affluence, the eating out incidences has increased in the urban India. The 'Young India' is also experimenting with new tastes and preferences and tastes are getting diffused across geographies. Pan-Indian cuisines as well as cuisines from other countries have also found their way into people’s kitchen across the country. There is a growing trend towards balanced and health consciousness diet in the new generation of consumers.

**Growing Need for Convenience Food**
Increased income levels, urbanization and a greater proportion of urban working women in India is leading to increased convenience-seeking behaviour of Indian consumers. There has been an increasing demand for processed & convenience foods such as in ready-to-eat, ready-to-cook, ready-to-serve and ready-to-heat categories.
Growth in Organized Retailing

The organized retail accounts for about 1.5% of the total food & grocery market in the country, however with growing investments in this sector, it is expected that the organized retail will account for more than 7.5% of the market by 2013. The organized retail with modern supply chain and temperature controlled stocking will lead to increased distribution of imported foods, branded foods and processed foods etc.

Challenges Faced

The Indian food processing industry currently faces a lot of challenges addressing current gaps in the value chain as well as leveraging on various advantages the country provides. Investors in the sector need to be aware of these factors and build required capabilities in their business to ensure success.

Fragmented Supply Base

Indian agriculture is predominantly a production driven market supply instead of market driven production, leading to inconsistency in quality of produce and supply. With more than 70% of the landholding smaller than 1.5 hectares, the average land holding in India is very small leading to poor economy of scale for the farmers to apply modern techniques in their farms.

Poor Quality Control

Though Indian growers and exporters have now been able to match up to global standards, meeting these standards with up-scaled production will be big challenge. The challenge becomes much bigger where there are differences in standards and consumer preferences across potential markets. The issues of traceability in fresh produce and poor hygiene generated infections in packaged foods need to be addressed.

Inadequate Infrastructure and Supply Chain

While India is the leading producer of many of the crops in the world, nearly 25% to 35% of this production is spoiled due to the lack of inadequate supply chain and poor infrastructure. Non-availability of core infrastructure like high-tech controlled production facilities, grading, packaging, cold chains, logistics, warehousing, integrated processing units, inefficient supply chain, poor transportation and erratic power supply are the major concerns in the country. Also, there are very few specialized distribution companies, providing refrigerated transport and warehousing for perishable produce/ processed food products.

Food Regulations and Taxation Issues

Both the Indian food industry and the processing industry are governed by multiple legislations. Though many initiatives have already been taken by the Government, there is still need and scope for harmonization of taxation norms and systems across the country. Exhibit 4 enlists certain acts passed by the Government that have been passed.

Limited Market Linkages

The food value chain in India is highly fragmented leading to poor quality, lower price realization and increased wastage of produce at the farm level. Improvement in the marketing infrastructure and also identification of new export markets for their produce, are the two major issues facing the industry.

Exhibit 4

<table>
<thead>
<tr>
<th>Government Acts passed</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Prevention of Food Adulteration Act 1954</td>
</tr>
<tr>
<td>2. Essential Commodities Act, 1955</td>
</tr>
<tr>
<td>3. Fruit Product Order, 1955</td>
</tr>
<tr>
<td>4. Meat Food Products Order, 1973</td>
</tr>
<tr>
<td>5. Milk and Milk Products Order, 1992</td>
</tr>
<tr>
<td>6. Agriculture Produce (Grading &amp; Marking) Act (Ministry of Rural Development)</td>
</tr>
<tr>
<td>7. Standards of Weights and Measures Act, 1976</td>
</tr>
<tr>
<td>8. The Warehousing (Development and Regulation) Bill, 2005</td>
</tr>
</tbody>
</table>
Emerging Opportunities

The Indian food industry, however, is in a unique position with both challenges and opportunities existing at the same time. Till the late 70s, India was a food deficit nation. Post-70s, the country moved to become a food surplus nation, thanks to efforts from eminent personalities like Dr. Swaminathan who led the “Green Revolution” drive. Today, India is the second largest producer of food, next only to China. Around 26% of GDP in India comes from food and agriculture. Food processing sector ranks fifth in terms of its contribution to GDP. There is tremendous untapped potential which is presently languishing in darkness. India has incredible opportunities in the field of food processing because of various factors.

India has the second largest arable land in the world. It has diverse agro-climatic zones: hot and humid in its long coastal line area, dry and cold in mountain ranges, hot and dry in plateau regions. This makes India unique for producing many kinds of horticultural and agro-products. Apart from this, India with a population of 1.08 billion, growing at 1.6% per annum, has a favorable demographic profile making it one of the largest consumption hubs.

**Food Processing**
The production potential and significant variations in food habits and culinary traditions across the country translate into immense processing opportunities for the companies. Also, there is an opportunity for key suppliers for machinery, technology and infrastructure for the industry.

**Sourcing**
*Export Opportunities*: Indian agribusiness industries provide opportunities not only to cater to the growing Indian middle-class but also for export market. India with its strong agricultural production base, easy availability of raw materials and the growing food processing industry, is strategically poised to capitalize on the global food processing market.

*Building forward linkages*: Leading product brands and retailers are integrating their agri supply chain with processing plant or retailing business. With a well established agriculture practice, India presents vast opportunities in the domain of contract farming. Already contract farming is successfully practiced for the production of the crops such as potato, tomato, maize and gherkins, among others.

**Back End Services**
*Temperature controlled infrastructure*: Even though India is the second largest producer of food in the world, the facilities required for food storage and infrastructure for refrigerated transportation are grossly inadequate. Tremendous potential for investment exists in the areas of procurement and delivery systems, pre-cooling facilities, refrigerated vehicles, cold stores/ controlled ambience stores, warehouses and traceability issues, among others.

**Creation of Infrastructure**
*Production infrastructure*: India needs modern facilities in germplasm and seed multiplication facilities, agricultural inputs (seeds, plant nutrients and plant protection chemicals), irrigation, controlled production facilities, farm mechanization etc to improve its agri produce infrastructure.

*Processing infrastructure*: Investment in farm level post-harvest facilities – cool chambers, grading and sorting facilities, pack houses for the back-end support; integrated industrial processing units for processing and value addition.

*Distribution infrastructure*: There is a need to establish an integrated supply chain like warehousing, cold chain and transport from farm gate to the food plate for strong backward and forward integration. Supply chains are to be created in such a way that they can be utilized round the year for multiple commodities to increase the efficiency of utilization.
Opportunity to Launch New Products/Brands

**Mass market basic foods:** High volume opportunities like flour, fresh poultry, edible oils, sugar etc. the key will be to integrate the supply chain with the retail distribution.

**Mass market value added products:** Key categories include bakery, dairy products, tea, coffee etc. which have a large volume and branding plays a key role. The key challenges include adaptation to the local tastes and local distribution.

**Niche market products:** Key categories include ready-to-eat, ready-to-cook, chocolates, fruit juices, branded staples, spices, pickles, snacks etc. Product development and brand building will be the key for the success of the brand.

**Food exports:** Key categories include, ‘Basmati’ rice, spice, pickles, snacks, ready to eat, dry fruits etc. the key is to set-up high grade production facilities with complete quality control.

Export Opportunities
India has the potential to grow its export of processed food which are driven by key factors like ample availability of raw material & low production cost driven by availability of cheap labour.

Key Success Factors

**Growth of Domestic Market**
The overall penetration of processed foods in the domestic market is low. This leads to a large untapped market with propensity to consume processed food.

**Appropriate Product Concept**
For any successful business, it is important to have the right product concept that meets consumer expectations and the food industry is no exception. Innovative products, leading edge technology, fast changing consumer needs and preferences, are all aspects that need to be focused.

**Competitive Pricing of Products**
Processed food companies need to understand the price sensitivity of the Indian consumer. The market demand is for competitively priced products with multiple pack sizes & price points.

**High Quality Raw Material with Sustainable Supply Chain**
This is the first and foremost prerequisite to determining the final quality of a product. In the food industry, the supply chain has to be sustainable so that the right quality product reaches the consumer.

**World Class R&D and Manufacturing Resources**
In a global business environment to keep pace with fast changing technology/innovations, it is essential have a world class R&D and manufacturing facility. This is the key to building capacity.

**A Qualified Manpower Resource**
Adequate resource of qualified manpower is another aspect of capacity building and is a very important asset for success in business.

**Safe and Healthy Products**
Consumption of food products pertain directly to the health of people. Hence, it is of utmost importance to have quality systems like Hazard Analysis & Cuticle Control Points (HACCP) to deliver safe and healthy products to consumers.
Continuous Investment in Training and Technology Up-Gradation
This is a vital step to capacity building and is applicable to the food industry as well.

Innovative Packaging
In a highly competitive business environment, innovative packaging is another important facet of capacity building that can provide a leading edge.

Conducive Regulatory Framework
In addition to the above, proactive support from lawmakers to amend and modify laws that accommodate new innovations Genetically Modified Organism (GMO), concepts (Nutraceuticals) etc is critical for capacity building in the food industry.

Creating Appropriate Market Environment
To be a market leader, it is essential for the industry to create an appropriate market environment for selling products.

These are exciting times for the food processing industry in India, and the opportunity to enter the market is huge. The domestic market consumption is changing and the level of processing will increase significantly, and at the same time, India remains disproportionately a small player in the export market compared to its production capability in various raw products. The opportunity is also huge for back-end infrastructural companies, as product and brand companies looking at increasing investments in this sector.

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A Report Card on India’s Education Sector

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Background

India has amongst the largest student populations in the world (over 230 million enrolled in schooling and higher education) and a low literacy rate of 65% (ranked 172 globally). Also, there is a short supply of educated manpower which is employable. To meet existing and emerging demand, India needs to significantly gear up its education infrastructure.

The Government of India (GoI) targets to guarantee elementary education to every child between the ages of 6 to 14 years and for this purpose, it needs to increase access to education as well as improve the quality of education. On recommendations of the Kothari Commission, the GoI, in 1968 fixed a target of investing 6% of GDP on education by 1986. But this target was not achieved by a long distance. Current spending on education in India is not more than 3.5% of GDP and has never risen beyond 4.3% of GDP. Also, spending per student has fallen and the share of education in the five-year plans has reduced considerably. In comparison, the US spends 12% on education, France 7%, Malaysia 20% and Thailand 27%. Since the 11th Five Year Plan, the GoI has been laying greater emphasis on the quality of education. Also, with the GoI showing a clear willingness to engage the private sector in the education sector, there are significant opportunities for companies both in government and private schools.

Increased demand for education has led to some growth in supply in the recent years, largely through increased private participation. However, the increased capacity falls significantly short of the needs of the country. Given this background, this paper presents a report card on India’s education sector. We examine seven areas in detail below.

Enrollment in Schooling and Higher Education

Based on current trends, we estimate that India would see a shortfall of 4 million seats in higher education by 2015 and 7 million by 2020

Education comprises three broad segments – schooling (pre-school and kindergarten to class 12 or K-12), higher education (graduate, post graduate and PhD programmes) and vocational education (IT, hospitality, financial services, aviation, retail, etc.). This segment examines enrollment in the first two.

India has a population of about 434 million in the age group of 5 to 24 years of which 304 million are in the school going bracket (Exhibit 1) and the remaining 130 million in the higher education age group. In the school going bracket, only 227 million of the eligible 304 million are in school. The ‘gap’ is due to a combination of reasons including children not in school, high dropout ratios at different levels and the demand supply gap. The enrollment ratio at primary level (class 1 to 5) is 106%, dropping down to 42% in classes 9 to 12.

<table>
<thead>
<tr>
<th>Grades</th>
<th>Enrolled, Mn</th>
<th>Eligible, Mn</th>
<th>Gap, Mn</th>
<th>Enrolled Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 – 5</td>
<td>127</td>
<td>134</td>
<td>(7)*</td>
<td>106%</td>
</tr>
<tr>
<td>6 – 8</td>
<td>77</td>
<td>51</td>
<td>26</td>
<td>66%</td>
</tr>
<tr>
<td>9 – 12</td>
<td>100</td>
<td>42</td>
<td>58</td>
<td>42%</td>
</tr>
<tr>
<td>Total</td>
<td>304</td>
<td>227</td>
<td>77</td>
<td>75%</td>
</tr>
</tbody>
</table>

*Enrollment is more than 100% because a number of children entering schools in Class 1 are either older than or younger than 6 years.

The Gross Enrollment Ratio (GER) in higher education in India (percent of relevant age group enrolled in higher education) is estimated at 11%. In comparison, enrollments levels are 60% in the US and 16% in China. Of India’s eligible population base of 105 million people in the age group of 20 to 24 years, roughly 11 million (Exhibit 2) are enrolled in higher education. This number is expected to grow at over 5% annually, through a combination of increasing GER and growth in population.

If these trends in higher education continue, and the new supply of seats for higher education builds up at the current pace, we estimate that India would see a shortfall of 4 million seats in higher education by 2015 and 7 million by 2020.

**Faculty-wise Enrollment in Higher Education and Industry Needs**

About 50% of graduates are studying Humanities & Arts, while the industry needs much higher numbers of Engineering, Medical, Finance and Service professionals.

The most popular fields / streams are Humanities and Arts, followed by Social Science, Business and Law (Exhibit 3). The first two streams together attract nearly 2/3rd of the students enrolled, while engineering attracts only 7%. In comparison, China has more than 1/3rd of its enrolled students in engineering. Brazil and Russia have high enrollments in social sciences, business and law and a significant number in education.

**Exhibit 2: Higher Education – Enrollment Levels**

**Exhibit 3: Graduation Rates by Field**

Source: University Grants Commission (2006) & Technopak Analysis

Source: Goldman Sachs
There is clearly a mismatch in the faculty wise enrollment in India and industry requirements. The ten high growth industries / sectors in India are telecom, IT-ITES, healthcare & pharmaceuticals, banking & finance, engineering goods, real estate & construction, retail & consumer goods, tourism & hospitality, automotive and aviation & airlines. The future employment demand for these industries is estimated at 5 million and 6.5 million by 2015 and 2020 respectively. These industries will require a much higher numbers of engineering, management, business, finance, and service industry professionals.

Almost 6 million college seats are required in the 2009 school-leaving year. Against this, the total number is below 4 million and that includes all seats irrespective of their quality and geographic clustering. What is even more worrisome is the lopsided addition of higher education capacity. For example, India certainly needs more engineers especially in the context of the massive investment needs in basic infrastructure including construction, power, telecommunication and manufacturing. Yet, of the estimated 300,000 engineering seats available each year, a disproportionately high number is focused on IT while a very low number is available for disciplines such as civil, material, bio-medical and industrial engineering.

For an economy that is just about 7% the size of the US, India has almost 50% more seats for MBA and even more disturbingly, a rapidly expanding availability of seats for more exotic versions such as BBA. For the expected massive investment in the real estate sector over the next 20 years, there are less than 5,000 seats available for architecture, and less than 1,000 seats for industrial design, whereas there are over 5,000 seats available for fashion design notwithstanding the fact that a majority of fashion design graduates just fade away in buying houses and garment exporters’ offices doing anything but actual design. Likewise, against a current deficit (and increasing each year) of almost 500,000 doctors, the total intake of fresh students is less than 40,000 per year.

There is a pressing need for re-orienting the stream wise enrollment. In addition, the number of colleges and institutes need to be increased to cater to increased enrollment levels. If the Government does not liberalize the education sector immediately, and encourage massive public as well as private investment in this sector, India will have the youngest population in the world which is also the least educated.

Projected Growth in India’s Private Education

Private education is currently (2008) estimated at US$ 40 billion, and is projected to grow to US$ 115 billion in 10 years (from demand perspective, if supply can keep pace)

India’s private education sector currently (2008) stands at US$ 40 billion. The GoI allocated US$ 8.6 billion to education in its budget for FY09, but the private sector is almost five times this amount. Of the US$ 40 billion in private education, K-12 schooling (tuition, text books, stationary, etc.) makes up 60%, Higher Education (largely engineering, medical, MBA, etc.) 17%, tutoring (for school children) 13%, vocational education 6% and test preparation 4%. The education sector is projected to grow at 11% (from demand perspective) over the next 10 years, to reach US$ 70 billion by 2013 and US$ 115 billion by 2018.

There is a growing shift towards private schooling. Close to 34% of school going children attend 20% of the schools (private schools). This trend is set to continue, as gap in quality between public and private schools widens.
Exhibit 4: Private Education – Size and Projected Growth

Schooling

<table>
<thead>
<tr>
<th>Main Segment</th>
<th>2008</th>
<th>CAGR</th>
<th>2013</th>
<th>CAGR</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>US$ Million</td>
<td></td>
<td>US$ Million</td>
<td></td>
<td>US$ Million</td>
</tr>
<tr>
<td>Pre-School</td>
<td>1,200</td>
<td>20%-25%</td>
<td>3,500</td>
<td>10%-15%</td>
<td>5,800</td>
</tr>
<tr>
<td>K-12</td>
<td>21,000</td>
<td>5%-10%</td>
<td>30,800</td>
<td>5%-10%</td>
<td>43,200</td>
</tr>
<tr>
<td>Tutorial</td>
<td>5,000</td>
<td>8%-13%</td>
<td>8,000</td>
<td>5%-10%</td>
<td>11,800</td>
</tr>
<tr>
<td>Books</td>
<td>1,700</td>
<td>5%-10%</td>
<td>2,400</td>
<td>3%-8%</td>
<td>3,000</td>
</tr>
<tr>
<td>Stationery</td>
<td>1,380</td>
<td>5%-10%</td>
<td>2,000</td>
<td>3%-8%</td>
<td>2,600</td>
</tr>
<tr>
<td>Education CD-ROMs</td>
<td>120</td>
<td>25%-30%</td>
<td>390</td>
<td>20%-25%</td>
<td>1,100</td>
</tr>
<tr>
<td>Multimedia in School</td>
<td>25</td>
<td>60%-70%</td>
<td>320</td>
<td>50%-60%</td>
<td>3,300</td>
</tr>
<tr>
<td>Total</td>
<td>30,425</td>
<td>47,410</td>
<td>70,800</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Higher Education

<table>
<thead>
<tr>
<th>Main Segment</th>
<th>2008</th>
<th>CAGR</th>
<th>2013</th>
<th>CAGR</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>US$ Million</td>
<td></td>
<td>US$ Million</td>
<td></td>
<td>US$ Million</td>
</tr>
<tr>
<td>Higher Education</td>
<td>6,700</td>
<td>8%-13%</td>
<td>11,200</td>
<td>7%-12%</td>
<td>18,100</td>
</tr>
<tr>
<td>Preparatory</td>
<td>1,600</td>
<td>13%-18%</td>
<td>3,200</td>
<td>10%-15%</td>
<td>5,900</td>
</tr>
<tr>
<td>Total</td>
<td>8,300</td>
<td>14,400</td>
<td>24,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Vocational Education & Skill Development

<table>
<thead>
<tr>
<th>Main Segment</th>
<th>2008</th>
<th>CAGR</th>
<th>2013</th>
<th>CAGR</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>US$ Million</td>
<td></td>
<td>US$ Million</td>
<td></td>
<td>US$ Million</td>
</tr>
<tr>
<td>Child skill enhancement</td>
<td>740</td>
<td>20%-25%</td>
<td>2,200</td>
<td>17%-22%</td>
<td>5,600</td>
</tr>
<tr>
<td>IT training</td>
<td>195</td>
<td>35%-45%</td>
<td>1,050</td>
<td>33%-38%</td>
<td>4,700</td>
</tr>
<tr>
<td>E-learning</td>
<td>45</td>
<td>35%-45%</td>
<td>240</td>
<td>33%-38%</td>
<td>1,100</td>
</tr>
<tr>
<td>Finishing school</td>
<td>25</td>
<td>50%-60%</td>
<td>235</td>
<td>45%-55%</td>
<td>1,800</td>
</tr>
<tr>
<td>Vocational</td>
<td>1,500</td>
<td>15%-20%</td>
<td>3,100</td>
<td>10%-15%</td>
<td>6,200</td>
</tr>
<tr>
<td>Teacher training</td>
<td>15</td>
<td>50%-60%</td>
<td>140</td>
<td>45%-55%</td>
<td>1,100</td>
</tr>
<tr>
<td>Total</td>
<td>2,520</td>
<td>6,965</td>
<td>20,500</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Market Sources and Technopak Analysis

Pre-schools, K-12 schooling and higher education will together represent about 2/3rd of the sector, with a small percentage drop in 10 years, as other segments grow faster. Multimedia in schools, child skill development, IT training and E-learning, preparatory and vocational studies, though relatively small segments in 2008 are forecasted to grow in the range of 25% to 60% and will together represent 1/4th of the sector. Pre-school, educational CD-Roms and child skill enhancement segments are likely to continue to remain an urban phenomenon. Teacher training is likely to continue to grow at 40% to 50%, as the requirement for quality teachers will be very high.

Besides schooling and higher education, other high growth areas include:

Test Preparation
Consumption of private tutoring for competitive exams of all levels is embedded in the Indian culture. Test preparation has been in existence for quite some time for taking any competitive exams. Mostly the preparation starts during classes 11 and 12 for engineering and other competitive exams. In 2008, about
320,000 students (almost 70,000 more than the previous year) appeared for the IIT-JEE exam, while as many as 270,000 students appeared for the CAT exam.

Apart from the above two, a substantial number of students prepare for and take the GMAT, GRE and SAT exams every year. This is not surprising given the high number of Indian students going abroad to pursue higher education. Indian students now constitute 15% of the total US foreign enrollment.

**Vocational Training**

Indian education has so far not given due importance to vocational education. As a result, there remains a gap between the requirement and availability of skilled manpower. Vocational training courses include: Typewriting, Stenography, Secretarial Practices, Computer Operator & Programme Assistant, Architectural Draughtsman, Desk Top Publishing, Electrical Technician, Electronics, Refrigeration & Air Conditioning, Plumbing, Library Assistant, Cutting/Tailoring & Dress Making, Hair & Skin Care, and Fruit & Vegetable Preservation Programs (basically training for airlines, retail chains, hotels, financial services and basic skills). With a significant growth projected in these sectors and a shortage of skilled manpower, the Government intends to open 250,000 vocational schools in India in the next five years via the Public Private Partnership (PPP) model, where the private sector may play a major role.

**Online Education**

Online education is an emerging segment. Some initial apprehensions about online education are now reducing. As per a recent survey, 63% of those surveyed thought that online and e-learning is equally good or better than classroom teaching, as compared to 52% in 2003.

With the number of internet users increasing, online education in India is looking up and its scope growing as well. Apart from course work, some e-learning portals are also conductng mock tests for various competitive examinations like engineering, medical and management.

**Educational Material**

Education CD ROMs are gaining popularity. When compared to conventional books, they occupy less space and are able to store substantial information: a typical CD Rom can store 650 MB or more of information, equivalent to about 250,000 pages (A4 size) of text. Additionally, digital publishing is economical too. There is no centralized source for data on electronic publishing in India, but it seems to be on the rise in the country. Almost all renowned newspapers and magazines are available on the web.

Some institutions such as the Indian National Scientific Documentation Centre (INSDOC) and the National Institute for Science Communication (NISCOM) are playing predominant roles in bringing out various scientific publications in CD ROMs (e.g. Asian Health, Environmental & Allied Databases (AHEAD) published by NISCOM, CD-ROM on Indian Patents and the National Union Catalogue of Scientific Serials brought out by INSDOC etc.). Educomp Solutions, a leading technology driven K-12 education company provides education related CD ROMs, amongst other tutorial products.

**Regulation**

Low levels of regulation have been a catalyst in creation of quality education in developed countries, but Indian systems are archaic and a hurdle in promotion of increase in capacity and improvement in quality

Shortage of quality education institutions is a product of India’s tightly controlled regulatory structure. Education, covered by the ‘Concurrent List’ of the Indian Constitution, is regulated at both the Central and
State Government levels. Regulation differs, sometimes radically, from state to state. For example, Delhi refrains from commercialization of education, while Maharashtra, Haryana and Gujarat permit ‘for profit’ schools. Higher education has several regulatory bodies, including AICTE (All India Council for Technical Education) and UGC (University Grants Commission), but there is no umbrella regulation for K-12 schools, nor a uniform law for schools.

Currently, the Government regulates who you can teach, what you can teach them and what you can charge them. It also has huge regulatory bottlenecks. There are considerable entry barriers: Universities can be set up only through acts of legislation, approval procedures for starting new courses are cumbersome, syllabi revision is slow, and accreditation systems are extremely weak and arbitrary. Exhibit 5 outlines the restrictions on different segments of education.

### Exhibit 5: Regulatory Framework in Education

<table>
<thead>
<tr>
<th>Segment</th>
<th>Authority</th>
<th>Mandatory Recognition</th>
<th>Fee Structure</th>
<th>Course Content</th>
<th>Profit Making</th>
<th>Quotas</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pre-School</td>
<td>State Dept. of Education, City Municipal Dept., Society Registrar</td>
<td>Yes</td>
<td>Not Controlled*</td>
<td>Not Controlled*</td>
<td>Ambiguous as reasonable surplus not defined</td>
<td>No quotas</td>
</tr>
<tr>
<td>Primary</td>
<td>State Dept. of Education, City Municipal Dept., Society Registrar, NCERT</td>
<td>Yes**</td>
<td>Not Controlled</td>
<td>Controlled</td>
<td>Not Allowed</td>
<td>25% for aided schools in some states – Delhi, Haryana</td>
</tr>
<tr>
<td>Secondary / Higher Secondary</td>
<td>NCERT / CBSE / ICSE / State Board (for course affiliation)</td>
<td>Yes</td>
<td>Not Controlled</td>
<td>Controlled</td>
<td>Not allowed</td>
<td>25% for aided schools in some states – Delhi, Haryana</td>
</tr>
<tr>
<td>Tutoring</td>
<td>NCERT / CBSE / ICSE / State Board (for course affiliation)</td>
<td>Yes</td>
<td>Not Controlled</td>
<td>Not Controlled</td>
<td>Allowed</td>
<td>No quotas</td>
</tr>
<tr>
<td>Higher Education</td>
<td>UGC/Councils for recognition and affiliation. Deemed University or affiliate to any Indian University</td>
<td>Yes</td>
<td>Partly Controlled</td>
<td>Partly Controlled</td>
<td>Not Allowed</td>
<td>22.5% current (for private aided &amp; unaided); likely to go up to 49.5%</td>
</tr>
<tr>
<td>Vocational Training</td>
<td>State Govt. for registration. DGET, NCVT/SCVT for affiliation</td>
<td>Yes</td>
<td>Not Controlled</td>
<td>Not Controlled</td>
<td>Allowed</td>
<td>Certain states – Tamil Nadu</td>
</tr>
<tr>
<td>Preparatory</td>
<td>Registrar of companies in a state</td>
<td>No</td>
<td>Not Controlled</td>
<td>Not Controlled</td>
<td>Allowed</td>
<td>No quotas</td>
</tr>
</tbody>
</table>

*except in some states like Maharashtra  
**except in some states like Punjab

A low level of regulation has been the catalyst in creation of quality education in developed countries. Exhibit 6 examines this in greater detail.

### Exhibit 6: Comparison of Regulation Across Countries

<table>
<thead>
<tr>
<th>Segment</th>
<th>India</th>
<th>US</th>
<th>UK</th>
<th>Korea</th>
<th>Brazil</th>
<th>Singapore</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pre-School</td>
<td>Profit motive allowed</td>
<td>Profit motive Allowed</td>
<td>No regulations</td>
<td>Low regulatory barrier</td>
<td>Low regulations</td>
<td>Low regulations</td>
</tr>
<tr>
<td>K-12</td>
<td>Non profit motive</td>
<td>Profit motive Allowed</td>
<td>Profit making not allowed</td>
<td>Low regulatory barrier (Fee hike cannot be more than inflation)</td>
<td>No government interference in fees / profitability</td>
<td>Profit making allowed</td>
</tr>
<tr>
<td>Tutoring</td>
<td>Profit motive allowed</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Higher Education</td>
<td>Non profit motive</td>
<td>Profit motive Allowed</td>
<td>Profit making allowed (since 2004)</td>
<td>Low regulatory barrier</td>
<td>No government interference in fees / profitability</td>
<td>Profit making allowed</td>
</tr>
<tr>
<td>Vocational</td>
<td>Profit motive allowed</td>
<td>Profit motive allowed</td>
<td>Not controlled</td>
<td>Not controlled</td>
<td>Not controlled</td>
<td>Special policies to encourage growth</td>
</tr>
<tr>
<td>Preparatory</td>
<td>Profit motive allowed</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>


Source: Published reports/articles; Ministry of Education and Human Resource Development, India; AICTE, UGC, Indian Ministry of Human Resource Development and Ministry of Education; CLSA Asia-Pacific Markets, Media reports, Departments of Education of respective countries.
Foreign Participation

About 185,000 Indians study overseas, spend US$ 4 billion annually and some are now returning to Indian jobs. Foreign institutions want to be in India, but are currently not permitted to do so. Lack of political will makes a change in this scenario unlikely for now

Numerous foreign educational institutions have shown keen interest in coming to India. Currently, foreign universities are not permitted to open campuses or confer degrees in tie-ups with Indian partners. However, various foreign universities are operating in India through collaborations and ‘twinning’ arrangements. The AICTE has recently notified such unrecognized tie-ups for technical and management education as illegal.

A bill to allow entry (the Foreign Educational Institutions Bill (FIEB)– Regulation of Entry and Operation, Maintenance of Quality and Prevention of Commercialization) was introduced in Parliament in 2007 and has made little progress due to limited political will.

The National Knowledge Commission (NKC), has also urged Prime Minister (PM) Dr. Manmohan Singh to open up the higher education sector. “We must formulate appropriate policies for the entry of foreign institutions and for the promotion of Indian institutions abroad,” the NKC said in its note to the PM. It has also called for making “a conscious effort to attract foreign students for higher education to enrich our academic milieu”. The NKC has also suggested the setting up of an independent regulator for higher education, which would also have degree-granting powers. Currently, any university or deemed institute has to seek AICTE’s approval before getting into a foreign collaboration for technical education.

Key Features of FEIB are:

- Only the FEIs which are accredited in their country of origin and meet the standards set by UGC will be allowed to operate in India
- Their admission process, fee structure, period of operation / renewal will be regulated by UGC
- They will have to be incorporated under Indian law & will be given ‘deemed to be university’ status
- They can grant admission, award degrees, diplomas or certificates
- Invest at least 51% of capital expenditure required
- Surplus from Indian operations has to be re-invested in India

Interestingly, many state governments are eager to attract foreign education service providers. Maharashtra is in the race, along with many other states, to attract the largest number of foreign universities. About 40 international universities have sought land for their campuses, along the Mumbai-Pune ‘knowledge corridor’ and also in the Mumbai-Nashik-Pune triangle. A Gulf-based institute wants to invest US$ 300 million in a new campus, while others are planning facilities along the Mumbai-Pune expressway. Several IT and software parks have come up along this 100 km stretch and new SEZs are also being promoted here.

Two foreign institutions (Georgia Tech University, USA and Schulich School of Business, Canada) are in discussions for acquiring land for their new campuses on the outskirts of Mumbai. The American University, Washington DC, is also considering a tie-up with an Indian business group, for a campus near Mumbai.
Top American universities including Stanford, Harvard and Wharton, and Europe’s INSEAD Business School, are also keen on offering courses to students in India. While many international universities are awaiting the final clearance from the Union Cabinet, some have already gone ahead with tie-ups. They include Stanford University (with IIM, Bangalore), Columbia University (with IIM, Ahmedabad), and Purdue University.

About 185,000 Indians study overseas and spend US$ 4 billion annually. This is almost 10% of the private spend on education, coming from a very small 0.001% segment of the student population. A number of these students are now returning to India after completing their studies, as job markets in India are more attractive, especially in contrast to weak macro scenarios in the western markets. Entry of leading foreign institutions will enable some of this US$ 4 billion spend to stay in India, and also provide a much needed boost to quality. However, given that about 90% of all engineering seats in the country are run by politicians, political will to make required changes remains a big question.

Private Sector Participation

Education presents a large opportunity to the private sector, especially corporate India, who need to look at education not just as Corporate Social Responsibility (CSR), but also as a profit venture that will also create trained manpower for their other businesses.

There is clearly an opportunity for private players to enter the education space. There is a large demand-supply gap, which is further exaggerated due to the low quality of education and capacity constraints at the premium colleges / institutions. This opportunity exists in all three segments – schooling, higher education and vocational training, and in almost all parts of India. Some success stories are Manipal University, Amity University and the Indian School of Business. Also, private sector participation is more likely to lead to the creation of thought leadership and centers of excellence in the country. This can then support policy development and at the same time incorporate industry demands in a market based curriculum.

Schooling and higher education are ‘not for profit’ ventures due to the requirements of being registered as a Trust or Society. However, an ‘operate and manage’ model is now legally accepted and enables a ‘for profit’ model in education. In such ventures, financial returns are attractive, with EBITDA levels of 30% plus and project IRRs ranging from 20% to 30% levels.

Corporate participation is clearly required in building the education landscape of India, as such firms not only bring in project management experience and financial capability, but also the mindset to achieve the right quality. Some examples of corporates in education are:

**K12 Schooling**
- Dhirubhai Ambani International School, by Reliance Industries
- Stonehill International School, by Embassy Group
- Educomp Millennium Schools, by Knowledge Tree Infrastructure, a subsidiary of Ansal API and Educomp’s subsidiary, Edu Infra

**Higher Education**
- Proposed Vedanta University by Mr. Anil Agarwal, Chairman of Vedanta Resources Plc, spread across 6,000 acres with estimated investment of more than US$ 3 billion in Orissa
• Proposed multi-disciplinary University by HCL’s Founder and Chairman, Mr. Shiv Nadar, spread across 300 acres in NOIDA

• Corporate India backed Indian School of Business (ISB) has announced plans for a second campus near Mohali

• Microsoft India announced an investment of $20 million in the Indian education sector over the next five years. To mark a beginning, Microsoft would be training 50,000 teachers in IT skills under their flagship program ‘Project Shiksha’

• Reliance Industries (RIL) is planning to set up a full fledged university in the state. The company is learnt to have zeroed in around 800 acres on the outskirts of Vadodara for the proposed university project

• Adani Group is planning to establish an Institute of Infrastructure Management, a university and an Adani Knowledge Centre

### Private Equity Investment

Apart from Indian Corporate entering the education space, private investors have been carefully monitoring the education sector realizing the great potential that the sector has to offer; considering the huge demand from consumers. They have been actively looking out for deals in the areas where profit is allowed. This can be clearly seen in the number of private equity deals that were finalized in the last two years. Table 6 summarizes these deals.

#### Exhibit 7: Private Equity Deals in the Education Sector

<table>
<thead>
<tr>
<th>PE / VC Investments in Education Companies</th>
<th>Target</th>
<th>Deal Size (US$ Million)</th>
<th>Period</th>
</tr>
</thead>
<tbody>
<tr>
<td>WestBridge Capital Partners</td>
<td>Brainvisa</td>
<td>5.5</td>
<td>Jan-2006</td>
</tr>
<tr>
<td>Sequoia Capital</td>
<td>Tutorvista</td>
<td>2.0</td>
<td>Jun-2006</td>
</tr>
<tr>
<td>Lightspeed Venture Partners &amp; Sequoia Capital</td>
<td>Tutorvista</td>
<td>10.0</td>
<td>Dec-2006</td>
</tr>
<tr>
<td>IDFC Private Equity</td>
<td>Manipal Universal Learning</td>
<td>31.0</td>
<td>May-2007</td>
</tr>
<tr>
<td>Manipal Education &amp; Medical Group (HSBC Private Equity Asia)</td>
<td>Meritrac</td>
<td>18.0</td>
<td>May-2007</td>
</tr>
<tr>
<td>Helix Investments</td>
<td>Mahesh Tutorials</td>
<td>12.0</td>
<td>Aug-2007</td>
</tr>
<tr>
<td>SAIF Partners</td>
<td>ICA</td>
<td>12.0</td>
<td>Oct-2007</td>
</tr>
<tr>
<td>Gaja Capital</td>
<td>Career Launcher</td>
<td>8.3</td>
<td>Oct-2007</td>
</tr>
<tr>
<td>Helion Ventures</td>
<td>Hurix Systems</td>
<td>5.1</td>
<td>Oct-2007</td>
</tr>
<tr>
<td>SAIF Partners</td>
<td>VETA</td>
<td>10.0</td>
<td>Dec-2007</td>
</tr>
<tr>
<td>KPCB, Sherpalo Ventures &amp; Inforedge</td>
<td>Study Places</td>
<td>3.0</td>
<td>Jan-2008</td>
</tr>
<tr>
<td>Aditya Birla Group</td>
<td>Core Projects</td>
<td>3.5</td>
<td>Jan-2008</td>
</tr>
<tr>
<td>D E Shaw</td>
<td>Excelsoft</td>
<td>31.0</td>
<td>Apr-2008</td>
</tr>
<tr>
<td>Blackstone, New Vernon &amp; Reliance (part of ADAG)</td>
<td>Everonn Systems Ltd.</td>
<td>31.0</td>
<td>May-2008</td>
</tr>
<tr>
<td>Light Speed Venture Partners &amp; Sequoia Capital</td>
<td>Tutorvista</td>
<td>18.0</td>
<td>Jul-2008</td>
</tr>
<tr>
<td>Matrix Partners</td>
<td>India Tree House</td>
<td>7.5</td>
<td>Jul-2008</td>
</tr>
<tr>
<td>Capital 18, the venture capital arm of media group Network 18</td>
<td>24x7 Solutions Learning Pvt. Ltd</td>
<td>4.0</td>
<td>Oct-2008</td>
</tr>
<tr>
<td>Intel Capital, Helion Ventures</td>
<td>Global Talent Track</td>
<td>6.5</td>
<td>Jan-2009</td>
</tr>
<tr>
<td>Zephyr Peacock</td>
<td>WLC India</td>
<td>NA</td>
<td></td>
</tr>
<tr>
<td>Bergruen Holdings</td>
<td>UEI Global</td>
<td>NA</td>
<td></td>
</tr>
<tr>
<td>EMPGI</td>
<td>HMSC Learning</td>
<td>NA</td>
<td></td>
</tr>
</tbody>
</table>

Source: Media reports, Published articles, www.indiapex.com
Conclusion

Although globally education as a business does not lend itself to “corporatization”, as there are limited economies of scale, in India corporate participation in education is essential because of the sheer number of seats that need to be created. This capacity build-up needs to be done with a strong project execution mindset and this can probably be done by corporate India alone, as opposed to small scattered entrepreneurial ventures or large though inefficient new government initiatives.

Key success factors for private education in India include:

• Creation of a strong brand which can command a premium with the student community and signal quality to employers and differentiate with other institutes
• Management of regulatory environment by creating a clean for-profit structure
• Strong academic partnerships to differentiate on content and its delivery. A strong product to support the brand and international collaborations with the best universities / institutions
• Industry relationships to co-create curriculum and guarantee placements and increase employability dramatically
• Governmental relationships to facilitate necessary approvals
• Public-private-partnerships, academia-industry partnerships, academia-research laboratories, public-NGOs, public-community etc. will need to be the models rather than working in separate compartments

Clearly, the demand-supply gap in education (especially so in higher education) in India is glaring, especially when “quality supply” is considered. However, for private participation to quicken, rules and regulations surrounding “not for profit” need to be reviewed. Also, increasing competitiveness requires participation from international world class institutions in setting up campuses in India. The big question that remains is-when will the powers-that-be act on these two critical aspects that will possibly have a very significant impact on the overall economic growth of India?

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Managing the ‘People Impact’ of Slowdown

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Outlook for Consumer and Service Industries in India

Recent GDP growth data from the Government shows Quarter 3 (ending December 2008) growth at 5.3%, much below government projections of 7.1% for the quarter. This presents a downward trend, when compared with 7.9% and 7.6% in the first two quarters of fiscal 2008-09, and was sharply lower than the 8.9% growth achieved in the same period last year. For the nine months to end-December 2008, GDP expanded by 6.9%.

While this data is not helping sentiment in the country, it is still a very far cry from “recession”, a word being used fairly loosely and frequently in India in the recent months. Also, India is nowhere close to the situation in countries like Japan (expected to contract by 10%+ in 2008), US and Europe (expected to see their economies contract by between 2% to 5% in 2009, and now seeing unemployment levels in the high single digits!).

Exhibit 1:

This overall macro-economic scenario has specific and different impact on various consumer and service industries / sectors in India. The table below provides an overview of current (2008) and projected (2013) industry size and employment data for seven such industries/sectors. These seven industries make up about 51% of India’s GDP and employ almost 62% of its non-farm employment.

As can be seen from this table, these seven sectors are projected to grow by almost US$ 250 billion in the next five years (average CAGR of 9%) and create 35 million new jobs (average CAGR of 7%). Clearly, these will be amongst the largest job-creators in India, with opportunities across male and female, highly educated and less educated, and urban as well as rural. However, short term concerns are quite high! Let us look at these industries individually in some more detail.

Retail
Retail in India is a US$ 375 billion industry and has been growing at 10% to 11% over last 5 years. Of this, modern retail (which has a 5% to 6% share and is 15 years old in the country) was growing at 35% to 40% YoY and traditional retail at 8% to 9%. Along with the about 6.5% GDP growth for 2008-09, if we add inflation of 4% to 5%, consumer spending in retail in India will grow by 10% to 12%. This translates into

<table>
<thead>
<tr>
<th>S. No.</th>
<th>Industry / Sector</th>
<th>2008</th>
<th>2013</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Size, US$ Bn</td>
<td>Employment, Mn</td>
</tr>
<tr>
<td>1</td>
<td>Retail</td>
<td>375</td>
<td>24</td>
</tr>
<tr>
<td>2</td>
<td>FMCG</td>
<td>18</td>
<td>3</td>
</tr>
<tr>
<td>3</td>
<td>Fashion</td>
<td>52</td>
<td>36</td>
</tr>
<tr>
<td>4</td>
<td>Healthcare</td>
<td>40</td>
<td>6</td>
</tr>
<tr>
<td>5</td>
<td>Hospitality</td>
<td>23</td>
<td>7</td>
</tr>
<tr>
<td>6</td>
<td>Food Processing</td>
<td>85</td>
<td>2</td>
</tr>
<tr>
<td>7</td>
<td>Education (Private)</td>
<td>40</td>
<td>4</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>509</td>
<td>81</td>
</tr>
<tr>
<td></td>
<td>Total GDP</td>
<td>1,000</td>
<td>1,338</td>
</tr>
<tr>
<td></td>
<td>% of GDP</td>
<td>51%</td>
<td>57%</td>
</tr>
<tr>
<td></td>
<td>Total Employment</td>
<td>350</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Non-farm Employment</td>
<td>130</td>
<td></td>
</tr>
<tr>
<td></td>
<td>% of Non-farm Employment</td>
<td>62%</td>
<td></td>
</tr>
</tbody>
</table>

Note: FMCG, 60% of Fashion (domestic market share) and Food Processing are included in Retail in revenue terms, but not in employment terms
Source: Central Statistical Organization, Industry Reports and Technopak analysis
US$ 40 billion, and is a figure that many countries would really be envious of! Traditional retail is expected to continue seeing growth in line with GDP growth (6% to 7% in real terms), while modern retail may slow to around 22% to 26% levels in the short term. Consistent growth segments are formats focused on “necessities” while those focused on “discretionary products” will see a slowdown, in line with consumer sentiments.

From an HR standpoint, modern retail was expected to create a very large number of new jobs. Since modern retailers are currently facing issues of overall weak macros and consumer sentiment, rapid front end expansion with insufficient supply chain investment, incorrect business models (in some cases), disproportionate real estate prices (though, these have / are correcting rapidly), slow down of international entrants, and some recent very public “controversies”, this job creation is expected to be weak in the short term (2009).

**Consumer Products**

Of the top 10 performers on the Bombay Stock Exchange (BSE) Sensex in calendar 2008, 5 were FMCG companies (sure, the Sensex did not have a great year!) So, “necessities” focused consumer product companies did well, while those at the “discretionary and lifestyle” end of the market saw average growth, where consumers tend to downgrade in difficult times. This trend applies to the international firms (P&G, Colgate, HUL, Nestle, etc.) as well as Indian ones (Dabur, Marico, Rasna, etc.).

Given the above, the FMCG sector re-emerged (after a number of years) as amongst the most sought after at b-school placements. With the expected countrywide Goods and Service Tax (GST) implementation in 2010 (replacing central and state VAT), resulting reduction in overall taxation on consumer products, and given their high price elasticity, consumer products are expected to continue with their growth levels. Also, we will see more innovative products being launched by FMCG companies targeting middle-upper class segment of consumers, leveraging the efficient and cost effective distribution platform provided by the modern retail. This augurs very well for current employees as well as for new job creation. Also, there will be jobs created in the Small and Medium Enterprises (SME) segment, as they will play a major role of private label manufacturers for modern retail in the years to come.

**Fashion**

The domestic apparel, textiles and home textiles market in India is estimated at US$ 30 billion, and grew by 5% to 6% in 2008. Including the export sector, the size of the industry is US$ 52 billion. The export sector faced a relatively tougher year last year, given weak retail environment in US, Europe and Japan.

Apparel, accessories and footwear were amongst the first categories to see emergence of modern retail in India with the likes of Shoppers Stop, Lifestyle, Pantaloon, Adidas, Reebok, Nike, etc. Given current consumer sentiment, job creation in the domestic apparel market is expected to be, at best, in line with overall GDP growth. On the export side, the 80:20 rule (80% of business coming from 20% of companies) is likely to get further skewed to a 85:15 or even 90:10. This is because price pressures will continue in the international markets and economies of scale will play a significant role. Companies that supply to WalMart, IKEA, etc. from India reported healthy growth last year. However, job creation was largely at a shop floor / labour level, as opposed to middle / senior management, signaling continued pressure.

**Healthcare**

Here is the first real silver lining amongst the 7 industries analyzed in this paper! About US$ 40 billion per annum is spent on healthcare in India (4% of GDP). The healthcare market is growing at 15% year on year (YoY) and is expected to double to US$ 80 billion by 2013. However, only 6% of delivery is organized and less than 10% of India’s population is covered by any form of healthcare cover or benefit.

A growing and ageing population, rising income, growing urbanization, increasing burden of chronic disease, increasing accessibility to health insurance, and medical value travel are some key reasons fuelling this growth. We see the imminent entry of large corporate players in this sector, which will lead to new jobs for medical professionals (doctors, nurses, paramedics), and also numerous job opportunities for healthcare administrators, managers, corporate staff, project managers, etc.
Hospitality
Hotels and restaurants is a US$ 23 billion sector in India. Global slowdown / recession and the 26/11 Mumbai attacks (and so lesser foreign tourist arrivals), coupled with a slower domestic environment are likely to have a contractionary impact on hospitality (especially hotels) in 2009. Given the real estate intensiveness of hotel projects (land makes up over 30% of most project costs) and the current lack of equity and debt financing for such ventures, numerous projects in the pipeline are being delayed.

The medium term outlook is of course perfectly fine, especially given that India has just 115,000 hotel rooms while over 270,000 are required (and an estimated 85,000 rooms are in the pipeline). This large demand-supply mismatch has also catapulted hotel rates in India to disproportionate levels (5 star rooms at over US$ 300 a night were the norm till a few months back), beating prices in New York, London, Tokyo and Paris. This is now correcting, and we hope hotels can develop sustainable business models at more reasonable room rates. We expect hospitality to grow to US$ 38 billion by 2013, and job creation to be proportionate.

Food Processing
This sector represents the second silver lining. As is well known, Indian agriculture contributes 17% to GDP and provides 60% of employment. The Indian food industry stands at US$ 200 billion (2006-07), with food processing making up for a 43% share (US$ 85 billion). Share of food processing is slated to increase from 43% to 50% by 2015, and combined with sectoral growth, this is expected to be a US$ 140 billion industry by 2015.

Job creation is expected across the board – in operations, distribution and management. Most companies (other than the likes of Nestle, ITC Foods, Ruchi Soya, Suguna Chicken, etc.) are relatively small and are non-MNCs, and in the past have been unable to attract talent the way IT / ITES, MNCs, etc. have. Given the growth contrasts, this may be well set to change, at least partly!

Education
This sector brings up the third real silver lining in the current macro-economic environment. The current private education market of US$ 40 billion is expected to grow to US$ 70 billion in the next 5 years, and US$ 115 billion in the next 10 years. This comprises 3 segments – schooling, higher education and vocational education. In higher education, given current growth in demand for seats and increasing supply, a shortfall of almost 5 million seats is expected by 2015! There is a pressing need for world’s best-in-the-class institutes focused not only on engineering, medicine, management but also on law, industrial design, architecture, healthcare administration, food (culinary) and hospitality.

The Jobs Recession
As explained earlier in this article, India’s GDP is not undergoing a recession but a slowdown. However, there is certainly a deep recession as far as jobs for the higher educated is concerned. Ironically, this may be the first time in India’s history when it is more difficult for the professional graduates to find employment or appropriate employment, compared to the less educated millions. Those who are currently struggling to find a decent job include engineers, management graduates, IT sector trained professionals, fashion designers, merchandisers and other retail sector professionals, pilots and other aviation industry staff, and other professionals. The problem is even more acute for those in the middle and senior management functions who have lost their jobs in the last a few months.

To compound the misery further for these job seekers, even if the overall business sentiment improves in India during this year sometime, it is very unlikely that prospective employers will go back to aggressive hiring of professional staff anytime during the next 12 to 18 months. In most of the 90’s and early 2000’s, developed countries such as the USA and in the EU shed hundreds of thousands of middle-management
jobs. Even in the boom times of the last 5 years, many of those jobs were never really filled up. The job creation actually happened in different sectors e.g. real estate and housing, financial services, travel and hospitality, retail, and healthcare just to list a few. These job seekers will also be facing the adverse fallout of the otherwise much heralded demographic divide of India. In the next 12 months, India will add more than 3 million graduates to the pool of employable. Of these, there will be more than 10,000 engineers from just the top 25 colleges alone (including the IITs), more than 5,000 MBAs from the top 25 Business Schools, more than 500 textile, apparel and accessories designers from the top-10 fashion institutes, more than 2,000 retail sector professionals (corporate staff level) from miscellaneous sub-streams of specialization, and more than 2,500 aviation sector professionals (cockpit and cabin staff level), etc. And finally, a trickle has already begun of the professionals of Indian origin returning to India as job opportunities dry up in USA and other developed economies.

The booming IT / ITES and Financial services business’s back-office sectors, till recently, absorbed just about every category of professionals including all kinds of engineers, architects, MBAs and other graduates even though the inductee’s job profile had no match with their professional qualification. Hence, perhaps an illusion was created about the actual demand of some of these professional’s categories especially that for MBAs. The manufacturing sector could indeed absorb all or most of the output of the engineers but was unable to do so on account of its inability to compete with the lure of the IT sector and the MNC financial institutions (even if the job was that of a glorified BPO operator).

What should Employers, Employees and Job Seekers do?

Employers
Till about 12 months ago, it was becoming difficult for HR Managers to spot poor performers, because the growth wave enabled even ordinary efforts and abilities to result in great results. Entire sales teams were beating targets, and it was hard to distinguish between better effort + ability and sheer luck + momentum. The opposite has quickly become true now, and it is becoming difficult to spot the good performers, as the slow down takes root. More than ever before, human resource management needs to be looked at as a main line function (with active participation from MDs, CEOs, COOs, and other senior management), as opposed to a support function. Some key points for employers to keep in mind during current market conditions include:

- **Be transparent:** Share strategic, financial, operational and HR related updates with employees. Let them know about the health of the firm, and share challenges it faces. Effective, frequent and honest communication to employees and engaging employees more in decision making will help their morale. Employees will appreciate this, and even if they leave / are asked to leave a company, transparency will help in establishing long term linkages and stronger alumni relations; an area where most Indian firms fall short.

- **Use the opportunity to upgrade teams:** This is an opportunity to attract the best talent to your firm, even if your firm has not attracted the best of talent during normal years (investment banking, management consulting, some MNCs, etc. have enjoyed this position). This may require substituting average talent for high quality. These are hard decisions, but should be made.

- **Restructure compensation first, before layoffs:** A lower fixed and higher variable compensation structure may yield better results in reduction of fixed costs and higher employee morale. This is especially true for service firms, where employee costs can make up about 33% of all costs.

- **Keep top performers motivated:** These are the resources companies do not want to de-motivate or lose. Feedback, motivation, monetary and non-monetary incentives, discussions on concerns, etc. are essential.
• **Provide inputs and suggestions to younger employees, beyond work related issues:** In India, most employees with less than 6 years of work experience have only experienced the heady years of 9% GDP growth and do not really know how to handle a slow down. Suggestions on personal finances and management during a slow down are essential.

**Employees**

Complementary areas as above, and a few others, are some points for employees to keep in mind:

• **Be transparent:** Share challenges and concerns with seniors, HR and peers. Actively seek support, where required.

• **Upgrade skills:** Improved performance and differentiation are more important than ever before. Acquiring new skills or upgrading current ones through own initiative and in personal time become very important.

• **Be willing to restructure own compensation:** Much preferable than being laid off

• **Keep seniors, HR and peers updated:** Managing the boss’s expectations and keeping peers updated, along with putting in the right efforts, helps in seeking assistance where and when required.

**Job Seekers**

What should the newly graduates (and their parents) do? They have to start with the acceptance of this new ground reality that merely a professional degree even, if it is from a top-10 or a top-25 institute, is not enough to guarantee them a job of their choice. In the euphoria of recent years, many of these fresh professionals had started to believe the illusion that they can have their pick of the industry, the company, the city, the job profile, and the compensation package. Hence, civil and mechanical engineers could decide to sit in swank Bangalore or Hyderabad campuses of the IT companies ensconced in front of a computer screen in an air-conditioned almost 5-star hotel environment rather than being in the field or on the shop floor. It is important for those who are in the job market today to understand that India’s economy is spread across India and not confined to the top 8 or 9 cities only. Hence, jobs are also spread across the entire urban and even rural India and therefore, the employees must be willing to work from there. Similarly, the current and future growth of India will actually be driven by agriculture including food processing, manufacturing, and relatively less attractive service areas such as real estate, infrastructure, travel and tourism, transportation etc.

Once this reality is accepted, the next adjustment has to be in the mindset regarding the employers themselves. Most young professionals in India have an extraordinary affection for MNC employers. They should understand that there are just good companies and not-so-good companies. Likewise, small and medium businesses can be as professionally rewarding as those having global or local headcounts of 10,000 or more.

The final reality that the young job seekers must accept is that all professional and financial aspirations cannot be met in their first 5 years of employment. Hence, initially there should be less focus on compensation package and job titles, and more on building a career that is rewarding in many ways over the next 30!

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About Technopak

We are a management consulting firm with a difference. Founded in 1991 on the principle of “concept” to “commissioning”, we are in the top 5 consulting firms in India by revenues. We are strategic advisors to our clients during the ideation phase, implementation guides through start-up phase, and trusted advisors overall. The industries we serve include Retail, Consumer Products, Fashion (Textiles & Apparel), Healthcare, Hospitality & Tourism, Leisure & Entertainment, Food & Agriculture and Education.

Our clients are leading Indian and international businesses, entrepreneurs, investment houses, multilateral development bodies and governments. Our 600+ clients include Aditya Birla Group, Apollo Hospitals, Arvind Limited, Asian Development Bank, Asian Paints, Bill & Melinda Gates Foundation, Essar, GMR Group, Godrej Group, Gujarat Government, Hospital Corporation of America, ICICI Limited, Hindustan Unilever Limited, International Finance Corporation, Lenovo International, Mahindra Group, Marks & Spencer, Mother Dairy Foods, Ministries of Food Processing, Textiles & Commerce, Raymond, Reliance Industries, Samsung, Sequoia Capital, Starwood (Sheraton), Tata Group, United Nations Development Program, Walt Disney, Warburg Pincus and many other Indian and international leaders.

Services we offer in Management Consulting

At Technopak, we foster innovation and creativity which challenge conventional thinking and generate practical and far reaching solutions for our clients. In 2008, we worked with over 130 clients across 180+ projects, in 20 countries besides India, across 5 continents.

Our key services are:

Business Strategy. Assistance in developing value creating strategies based on consumer insights, competition mapping, international benchmarking and client capabilities.

Start-Up Assistance. Leveraging operations and industry expertise to ‘commission the concept’ on turnkey basis.

Performance Enhancement. Operations, industry & management of change expertise to enhance the performance and value of client operations and businesses.

Capital Advisory. Supporting business strategy and execution with comprehensive capital advisory in our industries of focus.

Consumer Insights. Holistic consumer & shopper understanding applied to offer implementable business solutions.
Services we offer through our Group Companies

**foleydesigns**
Insights and innovation led product, packaging, space and strategic design, including design research, concepts, engineering and prototyping. A blend of unique, contemporary and relevant concepts and solutions.
[www.foleydesigns.com](http://www.foleydesigns.com)

**MINDSCAPE**
Holistic consumer understanding applied to offer implementable business solutions revolving around shopper insights, trend insights, design and innovation insights, marketing communication and measuring customer delight.
[www.indiamindscape.com](http://www.indiamindscape.com)

**VERTEBRAND**
Strategizing, planning and managing creation, development and growth of brands through a scientific, transparent and process-driven methodology.
[www.vertebrand.com](http://www.vertebrand.com)

**technopak Engineering**
Planning, implementation and project management of plants, warehouses and entertainment centers with a focus on modernization, process improvement, technical valuation, power & water audit and environmental engineering.
[www.technopak.com/engineering](http://www.technopak.com/engineering)

Services we offer through our Strategic Partnerships

**CUSHMAN & WAKEFIELD**
World’s largest privately held real estate services firm. We offer, through them, comprehensive retail real estate solutions to our clients.
[www.cushwake.com](http://www.cushwake.com)

**DALZIEL+POW**
UK’s leading design consultancy for developing brand environments. We offer, through them, design solution for retail environments.
[www.dalziel-pow.co.uk](http://www.dalziel-pow.co.uk)

**ENVIROSELL**
Global research and consulting firm specializing in the study of human behavior in retail, service, home, and online environments. We offer consumer and shopper insights.
[www.envirosell.com](http://www.envirosell.com)
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