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Higher rates not to put off capex: CFOs

But next 18-24 months seen hostile

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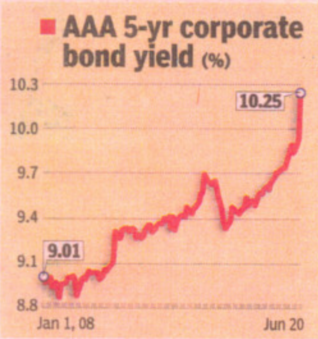
In spite of rising interest rates, India Inc is not putting its expansion plans on hold, though margins are seen taking a hit.

With inflation at 13-year high, a hike in interest rate is given, which would further accentuate the challenges of corporates given a slowdown in demand and rising input cost. Hence on the one hand their cost of fund will shoot up and on the other, a slowdown in market will ensure that they cannot fully pass on price increases to the end customer and would instead end up taking a hit on their profitability.



"Over the last one year, we have seen cost of funds rising by 1.5% to 2.5%. Our expansion or growth plans are not going to reduce or stop. These are business opportunities and not we don't review them because in the short term, interest costs have gone up," P Sampath, group chief financial officer, RPG Group said.

The group is on a big capex drive. Over the next few years, it's power generation arm CESC will invest Rs 9,000 crore, transmission tower company KEC has plans to invest Rs 1,500 crore, tyres maker Ceat would set up two plants at a cost of Rs 1,700 crore, and retail arm Spencers plans would spend Rs 2,500 crore network.

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Higher rates

Also, between entertainment company Saregama and technology firm Zensar, another Rs 1,500 crore would be invested.

On a group level, Sampath said higher interest rates would not impact margins beyond 0.25%-0.5% .

"I expect total borrowing costs will further rise by 100-200 basis points over the next 18-24 months and most will think twice about raising debt and would prefer equity. As far as we are concerned, as a group we are underleveraged and we don't foresee any problem raising money, though it would now cost a bit more," Prabal Banerji, Group CFO of the Hinduja Group said.

Hindujas have also lined up massive capacity expansion plans in its auto, auto ancillary, media, and ITeS business. Commercial vehicle major Ashok Leyland plans to invest Rs 3,000 crore over the next two years in doubling capacity and another Rs 600 crore as equity in its light commercial vehicle joint venture with Nissan. Subsidiary Hinduja Automotive also has lined up investments worth Rs 350 crore.

"We are not delaying or stopping our expansion plans simply because even if the cost of fund is rising, the business retunes are far higher. Interest payout also provides a tax shield and hence the net interest cost is about 8%. Returns in business, which typically is around 18%, is far higher and hence it makes no sense to go slow in capacity expansion. Working capital cost will also increase but one must remember that only about 40% of the working capital requirement is borrowed. Rest is met by vendor credit. In these situations, I expect vendor payout days to rise," Bannerji said.

For many firms, more than interest rates, its is availability of credit is a concern. "Bigger concern than rising interest rates is credit crunch, i.e. funds not made available on time. If there is a delay of 15 days in releasing funds, then procurement, production, etc. could get delayed, resulting in far greater loss than pure interest rate rise," B Brahmaih

vice president, Sujana Tower said.

Sujana has raised debt of Rs 100 crore at 12% per annum rate for two years, to expand its tower making capacity. It however sees a 1.0-1.5 rise in its working capital requirement, which currently stands at another Rs 100 crore. "I don't expect more than 5% impact on margins. This year (ending June) we were targeting a bottomline of Rs 54 crore, which may become Rs 52 crore owing to oil and interest rate hikes," Brahmain said.

Companies meanwhile will work on improving efficiencies and select price hikes.

And the silver lining could be a while away.

"For the next 18-24 months, it is going to be a hostile market scenario for corporates. I don't expect any moderation in inflation unless crude falls below $75 a barrel," Bannerji said.

RPG's Sampath doesn't see the situation improving at least till December. "I believe interest rates will remain firm till December and could further rise by 0.5-1.0 percentage points from these levels. My personal belief is post December, we could see some moderation. Hence our strategy is not to get tied up with long term fixed rates. To bring down our interest cost, we will look at forex loan for imported equipment. I see arbitrage opportunities of 2-3 percentage points on fully hedged position on forex borrowing," he said.