Deloitte.

The CFO Program

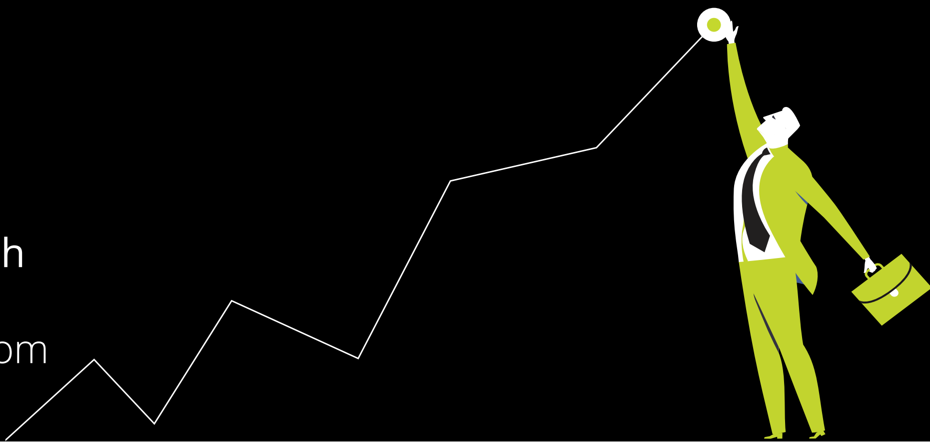
CFO Perspectives

CFO Speaks

India | CFO Newsletter | December 2016

CFO Speaks

Mr. Mitesh Shah
Head – Finance
Bookmyshow.com



1. The entertainment industry is growing rapidly and also witnessing a shift in consumer behavior. As a CFO what is your strategy for growth?

Today, the role of CFO has changed from being a finance gate keeper to that of a business partner. We need to keep exploring business opportunities and bring investors on the board for partnering business and creating a win-win situation. In the current era, CFOs need to strike these relationships to build alliances for business growth.

Further, the business cycles have different requirements for finance function. In a competitive environment, we look for more consumers, and thus need to respect business sentiments and be flexible when it comes to spending. As a CFO we should not always look at how much money is being spent; rather we should look for the right return and analyze if we are going in the right direction. Sometimes the returns are also intangible and hence that needs to be taken in consideration. Always there is a dilemma between striving for profitability versus investment in growth. However, if it is a disruptive business model, it makes sense to invest in cost, time and resource to satisfy consumers and vendors, and to build upon the business model.

As a CFO, I would definitely want investment in disruptive business ideas. Profit follows in the long-run and investments are bound to pay tangible returns, creating value for the investors.

2. CFOs need to keep a personal track of new laws and regulations in force, and the knock-on effect of new laws can have a serious consequence to the firm's strategy. How do you manage these complexities and regulatory changes?

Today for CFOs, legal is an important domain. We can never afford to take eyes off from what is happening in the legal. It is important to be proactive in meeting respective agencies and being informed. The challenge is that earlier everything was manual and our laws are designed accordingly, but with business now becoming electronic, the laws have to be tweaked to suit the current needs. Thus, there is bound to be a friction, as there is a thin line of difference between the legal and illegal. However, the best part is the government agencies now-a-days are open to discussions and they understand the genuine issues. Today the business model is changing, and advocacy is the key. Internally also we need to work closely with organization's legal team.

Also, our urge to government would be to have a holistic view, as each state government sometimes have different laws and these fragmented laws across length and breadth of the country makes things difficult at operational level. Thus, a CFO needs to deep dive to have a holistic view.

Lastly, whenever there are regulatory changes, we should quickly tweak our business models accordingly; for example, once GST is implemented, then our vendor management policy has to be tweaked.

3. As online customers spend minimal time to execute transactions, how do you leverage technology and harness the power of analysis to determine how best to analyze and project trends?

Analytics is the most crucial thing in today's new e-commerce business model, and everything is about data. We need to listen to what data is talking, then capture and analyze the trends, to get specific results on customers' tastes, preferences, likes and dislikes. We need to know the customer to best possible extent. For example, if a customer likes an action movie, we need to send an alert and offer discounts when any such movie is released to keep the customer engaged. It is imperative to be focused and targeted in the marketing strategy.

We should revamp the technology to adapt; and keep a close watch on the data, analyze quickly and act speedily. The key to success is, "never ignore any signal coming from data analytics and ensure minimal blip".

4. New payment methods have added to customer convenience, however, it comes with increased risks. How secure do you think the industry is to these frauds and what further measures could be taken to make the transactions more secure; especially in the light of recent events like the debit card frauds?

It is law of the nature that as we evolve, technology can also be used against us. We are so used to technology that we can't stop and customer being a king, we need to offer all options for payment. In fact, we customize the product and payment modes to suit customer requirements. Though the kind of security standards we see today are much advanced; it can also be cracked and everything is vulnerable. As a merchant, it is important for us to analyze trends, we have a risk team too which flags off the exceptional items. In such cases, we check the KYC details and do a background check; in case we find something suspicious we report to the banks. For us, ticket size may be small but volume is huge.

In tech-driven businesses like ours, the risk of cyber-attacks have been increasing with 90 percent transactions happening on mobile phones, credit and debit cards. To be on safer side, we go for compliance and PCIDSS (Payment Card Industry Data Security Standard) certified regulatory standards. Internally too, a lot of checks and balances are applied; and experience also teaches a lot. World is evolving with new challenges every day and in this dynamism no one can be 100 percent secure. We can try and factor in everything but risk comes daily in different forms. System, if cannot prevent fraud, should at least detect early and send an alarm to help minimize the risk, if not eliminate it completely. Hence, when the data gives a warning or an alert, it should always be analyzed.

5. The ability to attract and retain talent as well as foster an environment of an engaged workforce is seen as a key requirement for the CFO of the 21st century. It becomes more challenging for start-ups! How do you work towards building your finance team and retaining talent in order to boost your own performance and that of the organization?

Each individual is tailor-made differently and they have different aspirations in life. Cultural fit for the prospective employee and the employer is very important. In general, there are two types of organizations and work environment. First is a "tread mill", wherein one slogs hard and gets quick growth. The second is "methodological", where one works more logically and as per set SOPs (standard operating process) to achieve the best outcome and growth comes sequential. So it's all about assessing individual and seeing that the mindsets are matching with the organization. In our case, the candidate needs to be passionate to learn quickly and perform. At the same time, it is important to retain them and also ensure that the burn-out doesn't happen. The work place needs to be more interesting and an environment such that people want to stay and feel good about it. Pressure will always remain, but how to handle them is a key! Money is not the only important expectation for an employee; job satisfaction and work environment adds a lot of difference for people to stay motivated and be associated with the organization.

6. What are the 3 key challenges you face as a CFO of start-up? How does it differ from the challenges that typical CFOs from established industries face?

1. As a start-up CFO, one needs to unlearn lot of things. In a traditional business environment we have set templates to work and parameters like profitability ratio, debt-equity ratio, etc. which defines the business model. However in a start-up, we have to translate intangible value adds into the business model. It's basically about selling the vision to the investors, which is the toughest task.

2. Secondly, CFO is part of the founder group and is trusted by the CEO and probably the only person who can say 'no'. CFO has to play the role of "devil's advocate" and always needs to ask the questions like – is the investment justified? What's the return? As a CFO, we need to ensure the best utilization of investors' money and control the organization to move in the right direction and spend wisely.

3. Lastly, a CFO should inculcate the discipline of respecting money. It flows from investors and they need to know their "path to profitability" and unit level economies of the business. Profit is important to keep the wheel churning and to move forward. CFO also needs to maintain cash flow apart from the operations and during recession period of the business, a CFO should be able to show cash for the survival. It is said that, **"topline is vanity, bottom line is sanity, and cash flow is reality."**

Expert Views

Demonetization drive: Short term negative for the FMCG sector

The government has pulled off arguably the most significant reform measure in its tenure. While this expeditious move to boldly counter the black money and parallel economy threat is likely to have significant repercussions, importantly, this effort will also have a visible impact on how the current government's policies are perceived in international circles of economic power. Most of the macroeconomic impact will be felt in the short term, though there are larger implications in the medium to long term. We have tried to answer some of the more immediate questions:

What are some of the short-term impacts?

There will be a disruption in the current liquidity situation as households are likely to get affected by the note exchange terms laid by the government. Though clarity is unfolding on this, commodity transactions and general cash market transactions are likely to feel an immediate impact.

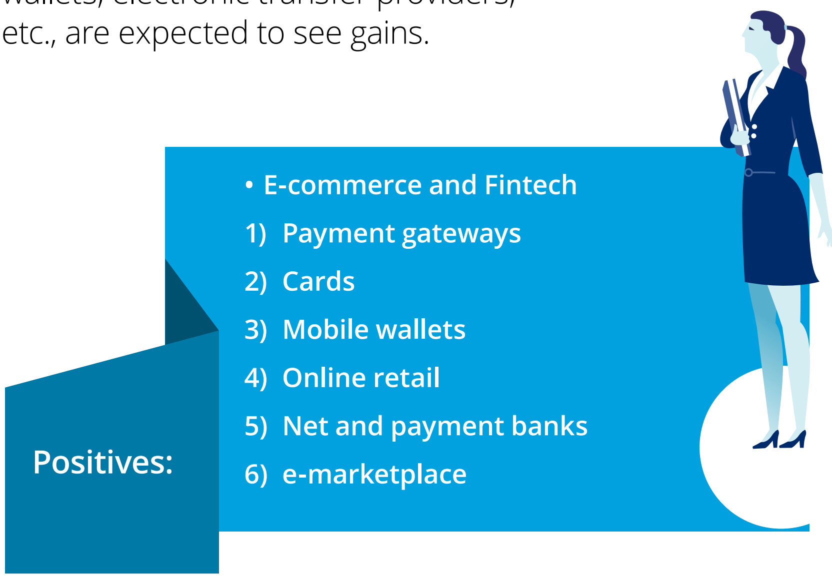
Unorganized sector proceedings including small trade market activities will remain volatile in the short term. Roadside vendors, cab drivers, kirana stores, etc. have already stopped accepting INR 500 and INR 1000 notes. It is important to note that a significant percentage of the Indian workforce is employed in this sector which is likely to be affected by immediate liquidity issues. Overall negative impact on disposable income is expected along with likely disruption in the consumption patterns of the general populace.

It is estimated that there will be a negative GDP impact in the current quarter as consumption gets a shock in the immediate term. However, quantum and degree of this impact cannot be ascertained now.

What could be some of the sectoral impacts?

While sectors with linkages to the unorganized economy are likely to be affected, technology and financial services are expected to gain in the medium to long term. On a sectoral basis, the commodities and agricultural sector, including the market for consumer durables and non-durables, is expected to feel the heat. In the short to medium term, large denomination purchases will likely be made via electronic purchases rather than through brick and mortar outlets. This will impact the retail sector adversely. The real estate sector is likely to see a significant negative impact in the medium to long term particularly in the repurchase market. There are expectations of a revaluation of current real estate transactions across the board representing possible losses to players in the sector. The luxury goods market is also likely to get affected as this move represents an erosion of real wealth to a large number of people. Areas of sub-sectoral impact will be felt in luxury cars, SUVs, gems, jewelry, gold and high-end branded products.

On the positive side, there is likely to be a reset of spending patterns as this move indirectly represents a significant push towards a cashless economy. Businesses in the fin-tech sector including payment banks, mobile wallets, electronic transfer providers, etc., are expected to see gains.



What is the likely impact on the FMCG sector?

Before we delve into the details, it is important to note that India has perhaps one of the highest ratios of cash to GDP in the world at 12.4%, much ahead of countries like China and Brazil[1]. Furthermore, the notes being banned accounted for approximately 85% of all the currency in circulation. As such, most purchases of FMCG goods in the country are still made in cash, both in the urban and rural areas.

Going beyond these arguments we believe that the FMCG sector will also be negatively affected in the below mentioned ways.

1. The bulk of sales still happens through small retail units or mom and pop stores. These stores are found across the country in close vicinity of human settlements. Further they accounted for around 92% of the retail market in 2015 and are estimated to be over 15 million[2]. Their major mode of sales has been through cash transactions and have stopped accepting payments of INR 500 and INR 1000 notes since the government's announcements.

2. The other side of the story is the emergence of a liquidity crunch for households across the spectrum. Behavioral economics dictates that households will temporarily become risk averse and only end up spending money on the most basic of needs while postponing any kind of expenditure deemed unnecessary on account of uncertainty and inability to make these purchases.

3. The third aspect is to with the income lost on account of trying to get the money changed from banks. Reports suggest that people have been spending hours to get their money exchanged and this situation is likely to continue given the extent of cash in the system.

4. Lastly, as a second order effect, any income lost on account of the above three facts for retailers is likely to limit their purchases of goods beyond what is necessary. It may also affect their expectation of future income giving another possible jolt to their consumption plans.

Now, the current structure of the economy is such that the bulk of the cash finds its way into the informal sector, wherein it provides a part of the essential liquidity for almost all transactions. These transactions happen within the confines of the informal sector and also with the formal sector. Given the fact that the informal sector in India accounts for approximately 45% of GDP and around 80-85% of employment, any disruption of this liquidity would have its negative effects on consumption[3].

These effects can get magnified as a large part of the rural economy had just harvested their produce and were looking to sell it in the open market. An absence of necessary liquidity is likely to affect their sales and income generation in the near future.

1. India's love for Cash, TNN, Jan 19th, 2015
2. IBEF retail market report
3. Shock and oh damn, Ideas for India, Nov 14th, 2016

Going beyond the daily use products, any consumption of white goods could also get affected as consumers are likely to postpone any purchases that are not borne out of an immediate need. The negative wealth effects of an erosion in existing wealth could also potentially curtail any extravagant purchases.

While there is bound to be a disruption in the consumption patterns that will have a knock on effect on the FMCG sector and overall growth for the quarter, the essential question remains whether they are likely to be transient in nature or permanent. We believe that these effects are only transient in nature and are likely to wear off once there is substantial liquidity in the markets. As such, things should return to their norm over the next 3-4 months.

What are some of the longer-term implications?

This essentially represents a change in regime for the real and financial economy. Domestically, there could be some turmoil as the effect will be disproportionately felt by the lower and upper income classes. Internationally, the government is likely to get a thumbs up for the move and more countries could potentially see this as a viable option to curb black money and stem illegal financial activity.

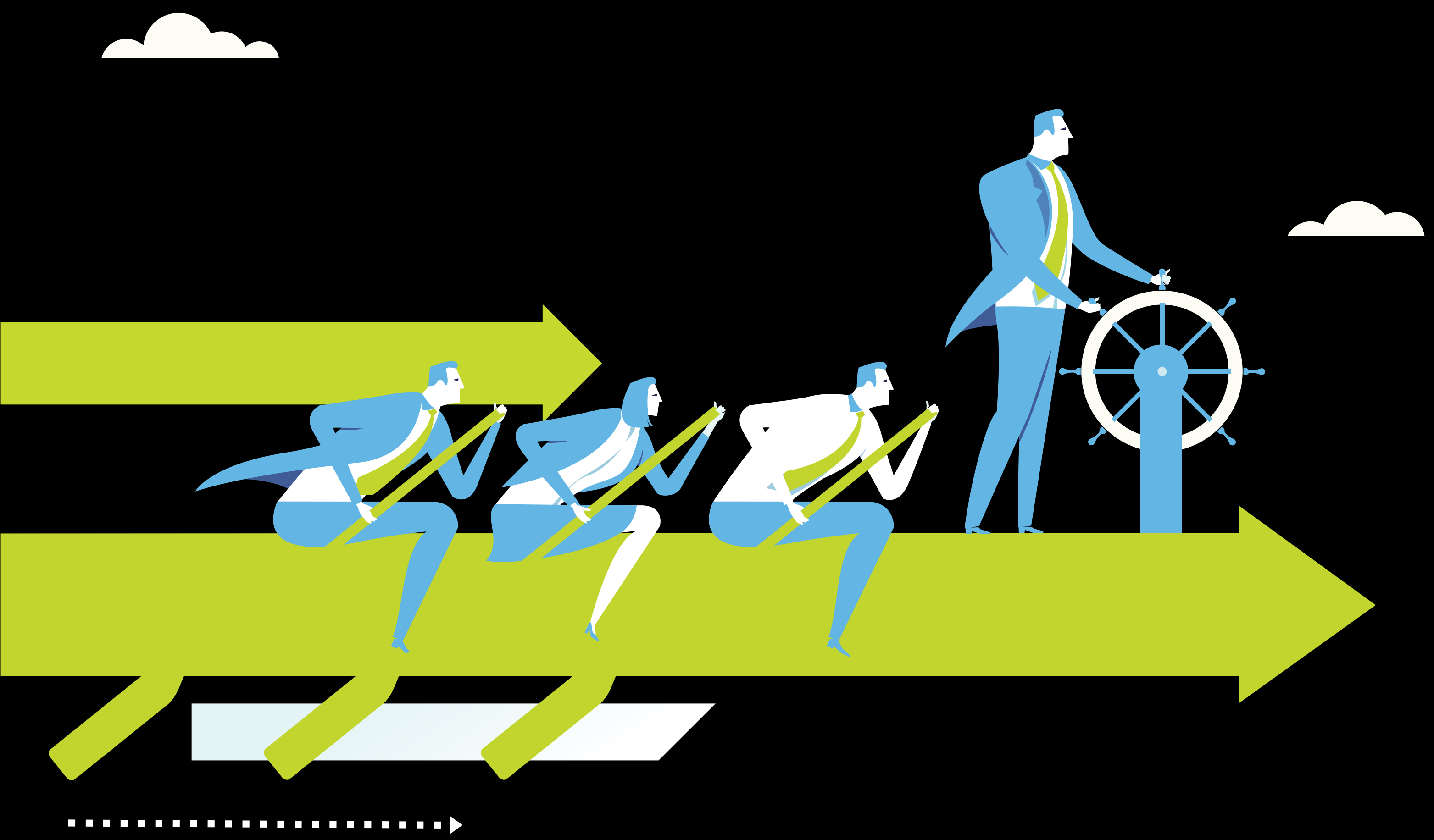
Lastly, though this move by the government may not be a first (having being tried by earlier governments as a tool to fight corruption), such an action achieves larger significance for a globally connected India as it shows boldness in tackling an issue which has remained a thorn in the growth success story of this generation.

Source: India Human Capital Trends report 2016

About Deloitte's CFO Program

The CFO Program brings together a multidisciplinary team of Deloitte leaders and subject matter specialists to help CFOs stay ahead in the face of growing challenges and demands. The Program harnesses our organization's broad capabilities to deliver forward thinking and fresh insights for every stage of a CFO's career – helping CFOs manage the complexities of their roles, tackle their company's most compelling challenges, and adapt to strategic shifts in the market.

For more information feedback or suggestions, please write to us at: incfo@deloitte.com



Deloitte.