



## Toronto research firm rocks clubby world of India Inc.

By STEPHANIE NOLEN  
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*Veritas' reports spark scrutiny into governance issues and have made some powerful enemies*

A series of scathing reports by a small Toronto investment research house targeting some of India's corporate heavyweights is riveting the country's business community, and sparking intense scrutiny of the state of corporate governance in one of the world's hottest economies.

**Veritas Investment Research Corp.** has alleged "manipulative accounting," poor disclosure practices and other gaping flaws in transparency at major Indian real estate, communications, and infrastructure firms. In the process, the company has shone a rare light on the fragility of oversight in the Asian giant – and made some powerful enemies.

Earlier this month **Veritas** released a report on IndiaBulls Group, a one-time brokerage that has branched into real estate and other businesses. Although fast-growing IndiaBulls has a "buy" or "hold" rating from almost every Indian analyst, **Veritas** advocates an immediate sell.

The report – titled "Bilking India" – opens with the allegation that the sole reason for the creation of IndiaBulls' real estate division "is to bilk institutional and retail investors for the benefit of select insiders. The controlling shareholders are running the organization as a piggy bank." **Veritas** said the information in the report was drawn from dozens of public documents including annual reports and court filings.

The company responded with a bitter denunciation of **Veritas** and its staff, saying it had knowingly published incorrect information – and lodged a criminal complaint, alleging that **Veritas'** researchers asked for a bribe to suppress a negative report.

The police case is a new twist for **Neeraj Monga**, **Veritas'** executive vice-president and one of two authors of the IndiaBulls report (with Nitin Mangal), although not an uncommon tactic in the business world in India. **Mr. Monga** called the bribery charge baseless and **Veritas** has released the correspondence between him and an analyst at a U.K.-based brokerage, the exchange that is the basis for the IndiaBulls legal case, as evidence there was no impropriety. In that correspondence, **Mr. Monga** cites the company's \$40,000 (U.S.) subscription fee and offers to hold release of the IndiaBulls report for a day if the brokerage wishes to purchase it.

**Mr. Monga**, who is Indian-born and grew up in Delhi, went to Canada for an MBA at the Richard Ivey School of Business in 1998, and was soon hired by Michael Palmer, a Bay Street broker setting up a new firm specializing in independent research, including forensic accounting, on Canadian public companies.

A few years ago, the firm branched into research on international firms. "Given the significant interest in BRIC [Brazil, Russia, India, China] countries and my background in India, and knowing the Indian place on the world transparency index, we said maybe we should look deeper into India," **Mr. Monga** said.

India offers ample fodder for what **Veritas** is best at ferreting out, **Mr. Monga** said: "Improper accounting, siphoning of funds, poor quality balance sheets, poor disclosure." The company sells its research on a subscription basis to institutional investors, in North America and abroad.

Last year, **Veritas** said that based on its books, Kingfisher Airlines, one of India's major carriers, was in fact "insolvent." The company later grounded most of its fleet and stopped paying salaries. This year, the research firm said DLF Ltd. – India's biggest realty company by sales, and a market darling – is a "crumbing edifice."

And **Veritas** has repeatedly slammed the Reliance group – which is controlled by the Ambani family, India's richest. A June report called the accounting practices of the behemoth Reliance Communications "whimsical."

"We neither believe in the reported book equity of the company nor in its reported fixed asset base," **Mr. Monga** and his colleagues wrote. They accused the controlling family of causing a \$4.5-billion loss to shareholders by de-merging its communications business and transferring it through a series of transactions to the younger of the Ambani brothers. The telco's stock fell to its lowest level ever after the release of the Canadian research; the company called the findings "*mala fide* [with or in bad faith] in intent and approach."

**Mr. Monga** seems almost to revel in playing an "emperor's new clothes" role, speaking what he says is unvarnished truth about major business players that get an easy ride from Indian investment research analysts.

"The intent is not to be deliberately provocative – but once you see such blatant disregard for your investors and such bravado – you feel the need to be strident," he said in a telephone interview from Toronto. "The intent is to ensure that people understand that this is unacceptable. It's trying to contribute at policy level in India – this is advocacy."

Arun Jain, an expert on corporate governance who teaches at the elite Indian Institute of Management in Lucknow, said the hard-hitting **Veritas** reports raise the question of why no Indian firm is doing similar work. "Sometimes the gap between who is being analyzed and who is doing the analysis is not big," he said.

India's business world can be a cozy one. "You know that someone you write about this week could be a potential client next week, so if you don't have something nice to say, you just don't do a report," said an analyst who has worked for the Indian branches of several international firms, and who did not want to be quoted by name.

"There is no independent research in India – research here is done to hawk stuff not detail something," said Dharendra Kumar, who heads Value Research Online, a Delhi-based investment analysis firm. "The whole system is embedded with conflict of interest." And the firms **Veritas** has taken on "are very powerful," he added. "Not too many domestic people within India would like to get into them with the same language that **Veritas** been able to do."

Indeed, in India the power of the Ambanis is perceived as virtually without limit. A chief player at IndiaBulls is the close relation of a powerful chief minister.

N. Balasubramanian, founding chair of the Centre for Corporate Governance and Citizenship in Bangalore, noted that in India, a large proportion of listed companies have concentrated ownership or controlling entities, such as family groups or the state (much as in Canada, he added). "Such ownership obviously is a fertile field for tunnelling or diversion of wealth and other private benefits of control," he said, but, "Investors are aware of this and build in the extra governance risk premium in their valuations."

International investors, with their willingness to tolerate practices that wouldn't be acceptable in their own countries, aren't helping the situation in India, **Mr. Monga** said – and they need to stop hiding behind the excuse that this is an evolving market. "If they continue to fund questionable corporate houses in order to participate in the Indian growth story, they are actually strengthening the hands of those who are undermining the Indian institutional framework," he said. "Some of these corporate houses are circumventing the spirit of the Indian regulatory process in order to enrich insiders at the expense of retail institutional investors."

Prof. Jain was pessimistic about the prospects for improvement. "None of these practices have become better in the last few years, the regulatory environment has not become more stringent – I don't think there is improvement at all," he said. "I would put the role on the stock exchanges themselves, to act in a more vigorous manner – and SEBI [the Securities and Exchange Board of India] has to become more pro-active."

Prof. Balasubramanian, however, believes that the Indian regulatory framework is solid and that agitation such as that by **Veritas** is going to have a noticeable effect. "I believe it is a sign of the Indian market 'growing up' and in the process exposing these pains in the maturation process."

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## FIGHTING WORDS

**IndiaBulls Group:** "A piggy bank" for controlling shareholders.

**Kingfisher Airlines:** "Insolvent."

**DLF Ltd., real estate company:** A "crumbing edifice."

**Reliance Communications:** "Whimsical" accounting practices.