# Banking & financial services sector

## Dealtracker

**Providing M&A and PE deal insights**

# Introduction

The only thing consistent in the world today is the fact that everything is so inconsistent. It is quite a paradoxical world that we live in today. When the world just thought that the post-pandemic recovery is going to take the world to new levels of growth, the Ukraine crisis, coupled with the rising Sino-American tensions, upended the supply chain systems throughout the world. Supply-side issues resulted in an inflationary situation throughout the world. Inflation was first thought to be transient and was expected to go away once the supply-side issues settled down. The world realised that this was not going to be anytime soon. Rightly so, the central bankers across the world resorted to a war against inflation. The US Fed alone raised 450 basis points in a year, with the UK, Europe, Australia, Japan and India, among others, doing the same. When interest rates spike so much in such a short time, financial stability risks are bound to materialise, especially for those financial institutions that did not plan for capital and liquidity under such stressed conditions. This is what has caused the banking crisis that is currently playing out across both the sides of the Atlantic in the US and UK. This has resulted in a very muted global growth scenario, which does not seem to change until the Ukraine conflict sees a resolution. Even with that, there are various geopolitical factors at play, which post some challenges to global growth.

Given that India is very much an integral part of the global ecosystem today, these variables have their impact on the country as well. However, the silver lining is that the impact is not as much as one would expect in other advanced economies. India has been acknowledged formally by multiple agencies as the bright spot in a sombre world today.

The demographic dividend, the innovation ecosystem, the infrastructure push and a strong reform-focused government – all point to a strong growth story. The regulators and the government alike are focused on the ease of doing business as a theme and a lot of operational efficiencies are being put in place by the government on a continuous basis. This sentiment is reflected in the deal activity that has been taking place in the country. Some of the largest deal activities have been taking place within the fintech ecosystem in India – more so with a very specific focus on credit and investments. Fintechs have moved from being an aggregator of financial products and services to the manufacturer of products and services in India today, which is one of the reasons why there is such an increased interest in seeking licenses for credit and investment activities from the Reserve Bank of India and the Securities and Exchange Board of India. Insurance penetration is another area of focus of the government, and we are seeing increased interest in the life and non-life insurance space in India, with the focus only increasing over the next few years. The GDP growth projected to the country will result in an aspirational growth for many people, who will increasingly look towards wellness as an option and hence will see an increased focus on health insurance in the country and the health insurance players experiencing some significant growth in the coming years. The continued focus on digitisation by the government will result in financial inclusion, with the fintech players democratising the products around credit, savings, investments and insurance.

Opportunities for the country exist significantly, and it is only important that we make the most of the same. We have all the right elements in place, and we just need to stay on course. India would truly witness some great times in the years to come and so would the financial services sector.

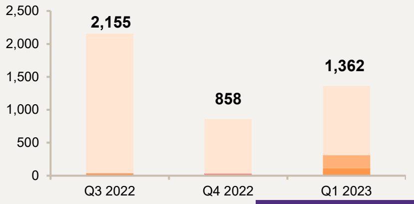
# Q1 2023 deal snapshot

| Deal summary | Volume | | | Value (USD million) | | |
|---|---|---|---|---|---|---|
| | 2021 | 2022 | 2023 | 2021 | 2022 | 2023 |
| Domestic | 15 | 8 | 8 | 508 | 153 | 112 |
| Cross-border | 0 | 2 | 1 | - | 178 | 200 |
| **Total M&A** | **15** | **10** | **↓ 10% 9** | **508** | **331** | **↓ 6% 312** |
| Private equity | 52 | 69 | ↓ 55% 31 | 1,091 | 1,743 | ↓ 40% 1,050 |
| **Grand total** | **67** | **79** | **↓ 49% 40** | **1,599** | **2,074** | **↓ 34% 1,362** |
| **Cross-border includes** | | | | | | |
| Inbound | 0 | 1 | 1 | - | 167 | 200 |
| Outbound | 0 | 1 | 0 | - | 11 | - |

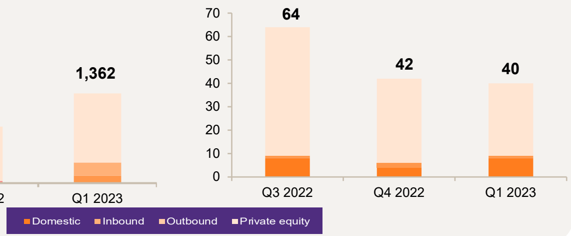
Q1

## Three quarterly deals trend

Trend based on deal values (USD million)




Trend based on deal volumes




## PE / VC investments dominated deal activity despite downtrend

- India Inc. recorded 40 deals valuing USD 1.4 billion, indicating a 49% decline in volumes, while a 34% decline in values when compared to Q1 2022. This is attributed to the geopolitical tensions and rising interest rates continuing in the quarter. The drop in the deal activity can also be attributed to a significant decline in the PE investment activity.
- While PE activity dominated the deal volumes with 84% of the overall deals, the PE activity also witnessed a declining trend and recorded only 31 deals with investment values of USD 1.1 billion on account of the absence of big-ticket investments. While Q1 2022 witnessed 10 high-value investment of USD 100 million and above, Q1 2023 saw only 5 such investments. Around 32% of the total PE deals came from the seed and pre-seed funding rounds.
- Investments in the fintech segment continued to drive the PE volumes, with 84% of the deals in Q1 2023 coming from the segment.
- M&A deal activity witnessed only 9 deals worth USD 312 million, also driven by the fintech segment, which accounted for 89% of the total M&A volumes as businesses looked to extend their presence in the new domain in this dynamic industry.
- While the M&A deal volumes marked the second lowest quarterly volumes, the quarter saw one marquee deal – Walmart's investment in PhonePe amounting to USD 200 million – to build and scale new businesses such as insurance, wealth management, lending, stockbroking, ONDC-based shopping and account aggregators.

## Deal values showed a 1.6x growth in Q1 2023 compared to Q4 2022

- Driven by high-value deals in the fin-tech, insurance and NBFC space, deal values saw a 59% increase over Q4 2022. Deal volumes, on the other hand, witnessed a Q-o-Q decline.
- While PE activity witnessed a Q-o-Q decline in deal volumes, the M&A activity showed Q-o-Q growth, recording 9 deals in Q1 2023 from 6 deals in Q4 2022, and values increasing from USD 29 million in Q4 2022 to USD 312 million in Q1 2023.



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# Top deals: Q1 2023

Top deals accounted for **91% of deal** values, **constituting 25% of volumes**

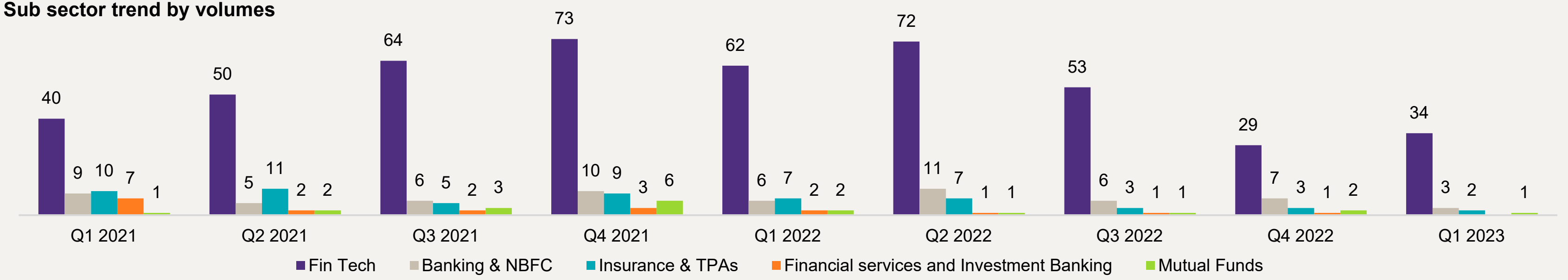
| Investor/acquirer | Investee/target | Deal type | Sub-sector | Stake % | USD mn |
|---|---|---|---|---|---|
| General Atlantic | PhonePe Internet Private Limited | PE | Fin tech | - | 350 |
| Walmart Inc | PhonePe Internet Private Limited | Inbound-Minority Stake | Fin tech | N.A. | 200 |
| Goldman Sachs Asset Management, TVS Capital Funds, Investcorp, Avataar Ventures and LeapFrog Investments | Girnar Insurance Brokers Pvt. Ltd - InsuranceDekho | PE | Insurance and TPAs | N.A. | 150 |
| PremjiInvest, Norwest Venture Partners, Elevation Capital and International Finance Corporation | Mintifi Pvt. Ltd | PE | Fin tech | N.A. | 110 |
| Advent International | Finnovation Tech Solutions Pvt Ltd- KreditBee | PE | Fin tech | N.A. | 100 |
| Ribbit Capital, Tiger Global, and TVS Capital Funds | PhonePe Internet Private Limited | PE | Fin tech | N.A. | 100 |
| Kedaara Capital | Avanse Financial Services Ltd | PE | Banking and NBFC | N.A. | 98 |
| Kotak Mahindra Bank Ltd | Sonata Finance Pvt Ltd | Domestic acquisition | Banking and NBFC | 100% | 65 |
| West Street Global, TVS capital fund, Investcorp Private equity, Avataar Ventures, Alstroemeria Investments, and angel investors | Girnar Insurance Brokers Pvt. Ltd - InsuranceDekho | PE | Insurance and TPAs | N.A. | 37 |
| Elevar Equity, Elevation Capital, Temasek and TVS Capital | SarvaGram Fincare Private Limited | PE | Fin tech | N.A. | 35 |

# Top trends

## Fintech continues to drive the deal activity

- There is an increased deal activity in the fintech space, especially in the domain of credit and investments. This signifies a belief of the investor community in the growth story of the country, where it is believed that the population of the country would experience prosperity, necessitating the need for savings through investment opportunities and credit for exponential growth.
- The fact that the fintech space is seeing a lot of deal activity is also due to a desire to move towards becoming a manufacturer of financial services products rather than just a provider through alliances and partnerships with traditional players. We expect increasing licensing support being sought by more of these fintech entities with the Indian regulators in the coming quarters.
- Deal activity in the banking space has slowed down, as the banking crisis, which is currently unfolding, will necessitate banks to re-look their operating models and look at the risks that their businesses are exposed to. Banks will focus internally over the next two to three quarters. Given the high interest rate regime, deal activity in the banking space will be slower.
- The Indian financial services sector offers significant growth opportunities, driven by factors such as increasing financial inclusion, rising income levels, and the adoption of new technologies. The Indian financial services sector will continue to be an attractive destination for private equity investment, while the M&A activity is likely to be driven by companies seeking to capitalise on these opportunities and strengthen their position in the market.

**Sub sector trend by volumes**



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# Budget 2023-24 highlights / Regulatory insights

## International Financial Services Centre (IFSC)

- In order to encourage the migration of offshore funds to the IFSC, tax exemption is available to offshore funds and its unit holders' shareholders on the transfer of capital assets of the offshore fund (or of its wholly owned special purpose vehicle) on account of relocation if undertaken on or before 31 March 2023. The sunset clause has now been extended to 31 March 2025.
- The definition of original fund [offshore fund], in the context of relocation, is expanded to include an investment vehicle in which the Abu Dhabi Investment Authority (ADIA) is directly/indirectly a shareholder/beneficiary, and it is wholly owned and controlled by the ADIA and any fund as the central government may notify.
- Pursuant to enactment of the IFSCA (Fund Management) Regulations, 2022 [FME Regulations], the funds in the IFSC shall now be regulated by the FME regulations. The definitions of 'specified fund', 'resultant fund' and 'investment fund' is amended to include reference to the FME regulations.
- The income distributed on Offshore Derivative Instruments (ODIs) to non-residents (NRs) by the IBU is now exempt from tax.
- Dividend income received by a NR from an IFSC, which is currently taxable at the rate of 20% (plus surcharge and cess), shall now be taxable at the rate of 10% (plus surcharge and cess).
- At present, the interest income received by a NR from specified bonds issued prior to 1 July 2023, and which are listed only on the IFSC stock exchanges, are taxed at the rate of 4%. The said income with respect to the specified bonds referred above issued on or after 1 July 2023 shall be taxed at the rate of 9%.
- Surcharge and cess shall not be applicable while computing advance tax on the prescribed income (i.e., any income other than capital gains) earned by the specified fund in an IFSC.
- Exemption is provided to a NR on the income earned from the portfolio managed by a portfolio manager in an IFSC that was accruing or arising outside India and was received in an account maintained with Offshore Banking Units (OBUs) in an IFSC. The above exemption shall now also be available to such activities carried out by specified persons as may be notified by the central government.
- Currently, a tax holiday is provided to an OBU in a Special Economic Zone (SEZ) to the extent of 100% of the income for 5 consecutive years from the year in which the RBI's approval for the set-up of an OBU was obtained and 50% of the income for the next 5 years. It is now proposed that the tax holiday of 100% of profits shall be provided to OBUs set up prior to 1 April 2020 for their remaining period of tax holiday out of 10 years.
- The sale of equity shares of an IFSC unit engaged in aircraft leasing to a NR or another IFSC unit engaged in aircraft leasing shall be exempt, subject to certain conditions.
- The dividend income received by a unit in an IFSC engaged in aircraft leasing from another unit in IFSC also engaged in aircraft leasing shall be exempt.
- Ship leasing entities in an IFSC can now opt for tonnage tax regime within three months from the end of their tax holiday period.
- The tax collected at source (TCS) on foreign remittances under the Liberalised Remittance Scheme (LRS) by resident individuals has been increased from 5% to 20%. Furthermore, the scope of remittance subjected to TCS is expanded by covering all remittance made under LRS and not just remittances made 'out of India' (thus including remittance to IFSC), with effect from 1 July 2023.

# Budget 2023-24 highlights / Regulatory insights

## Debt securities
## Market-linked debentures

- Capital gains arising on redemption, transfer or maturity of market-linked debentures (MLDs) shall be deemed to be short-term capital gains.
- MLDs are now defined in the Income Tax Act 1961 (Act) to include security by whatever name called with an underlying principle component with debt security and where returns are linked to market returns / other underlying securities / indices, and include securities classified / regulated as MLDs by the Securities and Exchange Board of India (SEBI).

## No extension of sunset clause for concessional tax rate on interest earned by a non-resident

- Currently, the Act provides for a concessional tax rate of 5% / 4% on the income payable by way of interest to a non-resident, in respect of monies borrowed before 1 July 2023. Similarly, the Act also provides for a concessional tax rate of 5% on interest payable before 1 July 2023, on specified securities to Foreign Portfolio Investors (FPIs).
- However, there is no proposal in the Union Budget 2023 to extend the above sunset clause.

## Mutual funds

- Tax treaty rates shall be considered for the purpose of tax withholding by mutual funds on income distribution for NRs.
- Capital gains arising from specified mutual funds acquired on or after 1 April 2023 shall be deemed to be short-term capital gains (similar to the provisions introduced for MLDs). A specified mutual fund has been defined to mean a mutual fund where not more than 35% of its total proceeds is invested in the equity shares of domestic companies.

## Insurance

**Proceeds from life insurance policies [other than Unit Linked Insurance Plans (ULIPs)]**

- The sum received under any life insurance policy (other than ULIPs), issued on or after 1 April 2023, shall now be taxable under the head 'income from other sources' if the annual premium payable exceeds INR 5 lakh except where the amount received upon the death of the policyholder, it shall continue to be exempt irrespective of the amount of the annual premium.

# Budget 2023-24 highlights / Regulatory insights

## NBFCs

**Interest deductibility rules for NBFCs**

- Thin capitalisation norms restricting interest deduction at 30% of EBITDA in respect of debts and guarantees issued by the NR Associated Enterprises (AEs) are not applicable to Indian banking or insurance companies or PE of the banking or insurance companies incorporated outside India. This benefit is now extended to such class of NBFCs to be notified by the central government.

**Categorisation of NBFCs**

- Presently, the deduction for the interest paid to deposit-taking NBFC and systemically important (Non-deposit-taking) NBFC is available on a payment basis. Also, the interest on the NPA earned by such NBFCs is taxable on a receipt basis.
- Given that the RBI is no longer adopting such classification of NBFC for asset classification purposes in the NBFC regulations, it is now proposed to substitute the aforementioned class of NBFCs with such class of NBFCs as may be notified by the central government.

## Other key highlights

- The last date of incorporation for claiming a tax holiday by an eligible start-up is extended by one year to **31 March 2024.**
- In case of a change in the shareholding of an eligible start-up, the period of relaxation for carry forward and the setting-off of losses, which is currently 7 years, has been extended to 10 years from the date of incorporation.
- Tax is now required to be withheld on the interest paid to residents on securities that are held in a dematerialised form and are listed on a recognised stock exchange in India in accordance with the Securities Contract (Regulation) Act, 1956.
- Presently, the royalty and fees for technical services earned by non-residents or foreign companies is taxable at the rate of 10%, which is now to be taxed at the rate of 20%.
- The relaxation available to non-residents from gift tax provisions has now been removed.

# Budget 2023-24 highlights / Regulatory insights

## Policy proposals - IFSC

- Delegation of powers under the SEZ Act to the International Financial Services Centre Authority (IFSCA).
- Setting up a single window IT system for registration and approval from the IFSCA, SEZ authorities, GSTN, RBI, SEBI and IRDAI. This shall simplify the registration process and timelines, resulting in ease of doing business.
- Amending the IFSCA Act to introduce statutory provisions for arbitration is in furtherance to the announcement during the last budget to establish an arbitration center in the GIFT City.
- Amending the IFSCA Act to introduce statutory provisions for ancillary services.
- Permitting acquisition financing by the IBU of foreign banks to provide more flexibility to banking business in an IFSC.
- Establishing a subsidiary of EXIM Bank for trade re-financing.
- Amending Section 18A of the Securities Contracts (Regulation) Act, 1956, prescribing the derivative contracts, which shall be legal and valid to now also include ODI contracts issued by the FPI in an IFSC.
- Setting up data embassies in an IFSC for countries looking for digital continuity solutions.

## Policy proposals - Others

- Financial sector regulators to carry out a comprehensive review of existing regulations to simplify, ease and reduce the cost of compliance.
- With a view to facilitate optimum regulation in the financial sector, public consultation will be brought to the process of regulation-making and issuing subsidiary directions.
- Amendments proposed in the Banking Regulation Act, Banking Companies Act and Reserve Bank of India Act will improve bank governance and enhance the protection of the investors.
- To enable fintech innovative services, the scope of documents available in the DigiLocker for individuals will be expanded.
- To simplify the KYC process, it is proposed to adopt a 'risk-based' approach instead of 'one size fits all' approach.



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# Current global trends

While the list may not be exhaustive, the seven global trends that we see within the financial services ecosystem are as below:

1. There is a significant focus on financial stability risks by the regulators across the globe today. Most of the financial stability risks have materialised on account of unprecedented changes in the external environment today. We can expect some macro prudential regulatory changes in the times to come around stress-testing requirements, especially within the banking system today.
2. The recent spate of the banking crisis, witnessed across different parts of the globe, will result in consolidation within the banking domain, with many stressed players being taken over by existing players. We may also see significant bail outs of some large banks in the European region in the time to come.
3. The focus on governance, risk management and compliance will continue to grow significantly, as has always been the trend in the aftermath of a crisis.
4. With rising geopolitical tensions globally, globalisation as a theme has been replaced with regionalisation, and now, we will see a lot more trade agreements being regional rather than global, which while inefficient, will become the need of the day. This will also result in near shoring, which is a trend that has been in place for quite sometime.
5. The biggest trend that we can see is the move towards green energy. This will result in significant changes in sustainable finance in the times to come.
6. The central bank-backed digital currency initiatives will see a lot more push in terms of innovation and adoption in the next three to four years.
7. With increased adoption of artificial intelligence (AI) within mainstream financial services, hyper-personalisation will become a norm.



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# Grant Thornton Bharat sector case studies

**Client profile:** A leading financial institution headquartered in the UAE with an expanding footprint across the Middle East and a strong presence in Europe, Asia, Africa and the US, with its international offices offering a wide range of financial products and services.

The firm is engaged with the client on global strategic and significant projects as well as building the entire ecosystem together as one unit. This includes business risk / cyber resilience / data framework / best practices for data management and building a sound security culture.

## Situation and problem statement

- The client wanted to review their information security governance framework and perform gap assessment for information security documentation.
- The client also wanted to carry out a bank wide risk assessment programme for their business units to assess information security risks to mitigate them.
- Both the exercises were being executed for the first time and they also had an objective of enhancing information security awareness across the organisation through these programmes.

## Our solution

- Two teams of experts from the firm helped the client to meet these requirements.
- One team reviewed and enhanced its existing information security governance framework and documentation in line with ISO 270001, NIST and UAE IA frameworks/regulations and with the best industry practices. Meanwhile, the other team planned, designed, and executed the risk assessment programme bank wide for 435 business units.
- This programme achieved 75% success rate, wherein several risk findings and risk themes were brought out and remediation plans were recommended to mitigate the risks.

## The impact and value addition

The firm was able to comprehensively review the information security governance framework and structure, thereby enhancing the security posture of the bank. The second programme, besides creating awareness, brought out the risk themes for the bank, and remediation plans were implemented in collaboration with each business unit. Detailed delivery reports were also rendered to the client.

# Grant Thornton Bharat sector case studies

**Client profile:** The client is a fintech pioneer and trusted payment service provider, powering customers across North America, CEMEA and APAC and partners with banks, non-bank financial institutions (NBFIs), acquirers, issuers and card scheme networks, supporting 17 billion+ transactions annually.

The firm has worked with the client on more than five work streams and has been a trusted advisor to the promoter and managing director on various issues.

## Situation and problem statement

- There were two engagements structured to address the client need.
- The workstreams in the first engagement were:
  - Direct to customer/merchant strategy and business plan development.
  - Business architecture and digital transformation roadmap to assist the client in designing a winning B2B business architecture that will enable the client's growth potential.
  - Budget and business plan for the company for FY23.
- The workstreams in the second engagement were:
- Implementation of business architecture and digital transformation roadmap
  - Implementation of direct to merchant strategy and operationalisation
  - Consulting services for supporting fund-raising through strategic capital investment

## Our solution

- The engagement team delivered the direct to merchant strategy and new business architecture as part of the first engagement, which was used by the client for their application with the Reserve Bank of India for the PPI and PAPG license. The team also delivered presentations to the regulator, which helped them with successful applications for the PAPG and PPI license.
- The team from the firm supported the client on a minority investment deal, right from the preparation of the pitch deck to the deal closure. There was a valuation increase by three times from the previous private round.
- The team also supported the client's management with implementation of new business architecture and merchant acquiring business.
- Business architecture and the digital transformation initiative was executed across assessment, concept design in wave 1 and detail design and implementation support in wave 2 over approximately 9 months.

## The impact and value addition

The firm's support on the engagements helped the client at various levels, including getting the PAPG and PPI license in September 2022 from the regulator, an increase in valuation by three times for the investment deal and successful business architecture and digital transformation implementation.

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