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War, What Is It Good For?

India and Pakistan snapped back late last week after Indian Prime Minister Vajpayee said he sees a "clear sky" ahead, which seemed to diminish the risks of war over Kashmir, India's only state with a Muslim majority. Still, the Mumbai Sensitives index fell 2.4% on the week, while Karachi was Asia's worst performer, with a loss of 6.6%. Tensions have simmered since terrorists attacked an Indian army camp in Kashmir on May 14. India claims Pakistan is backing Islamic militants, whom it says are waging war to achieve Kashmir's independence. Midway through last week, Vajpayee said the time had come for a "decisive fight."

There may not be a full-scale land war or nuclear exchange, but Pakistan said it would conduct missile tests over the weekend. India and Pakistan have fought two wars over Kashmir since achieving independence from Britain in 1947. A war would make a huge difference to Pakistan, where the military accounts for an enormous chunk of the economy. Yet both markets surely will suffer in a war scenario. And in the latter, investors probably would prefer surgical strikes against putative terrorist training camps in Kashmir, a disputed territory. Much worse would be attacks on Pakistani soil.

Any military action would need to occur soon, because monsoons start in four to six weeks, and that would make it pretty difficult to move around. Yet some believe India won't move until after September, when elections take place in Kashmir state.

The markets may jump higher if the weekend passes without incident. Jon Thorn, the chief of India Capital Fund PCC, has been buying **Reliance Industries**, whose Reliance Petroleum has the world's fifth largest refinery and is within "a gun-blast" of the border. He says “The good thing is they have insurance, and the risk is built into the stock,” which fell last week. What else will fare well in a war? **Bharat Electronics**, one of India's largest defense contractors, which dropped through Thursday and then surged on Friday to 212.55 rupees.

Getting the (Elevator) Shaft

But of late, **India Capital’s** Thorn has focussed most of his energies on **Otis Elevators (India)**, which has a market cap of about 3.5 billion Indian rupees ($71 million). Otis India is 80% owned by Otis Elevators, a unit of United Technologies. Thorn maintains that **United Technologies** is trying to buy Otis on the cheap. After all, United Technologies, through its Carrier subsidiary, offered to buy out the 13.7%.of Bombay-listed **Carrier Aircon** it didn’t own. Carrier Aircon trades at 98 rupees, less than a third of its 1997 high of 328. Similarly, Otis India trades at 279.5 rupees, versus 500 in 1999.

And taking companies private means the number of investable companies shrinks.

Thus, Thorn has enlisted the help of HDFC, the big financial institution that is led by Deepak Parekh, one of the most respected people in Indian finance, and value investor Aberdeen Asset Management. Together, the three control 5.6% of the equity, and a quarter of the free float. They want to form a shareholder association to block a buyout, a move that Thorn proposed at Otis India's annual meeting this month. Such a move, Thorn says, "would send a very strong message to other Indian corporates, multinational or domestic, that Otis is a leader in India in minority shareholder enfranchisement and corporate governance transparency."

Says Thorn: "United Technologies wants to take it private at a big discount." Otis's cash alone, he notes, is equivalent to 22% of the company's market cap, and Thorn reckons that fair value for the stock is 900 rupees. Says Thorn: "They have 85% of the elevator market in India. This is the best housing infrastructure business in a booming housing infrastructure market. This is the best business I know in India. I am stupid enough to sell it for 280 rupees? That's clinically insane."