Equity Market Outlook

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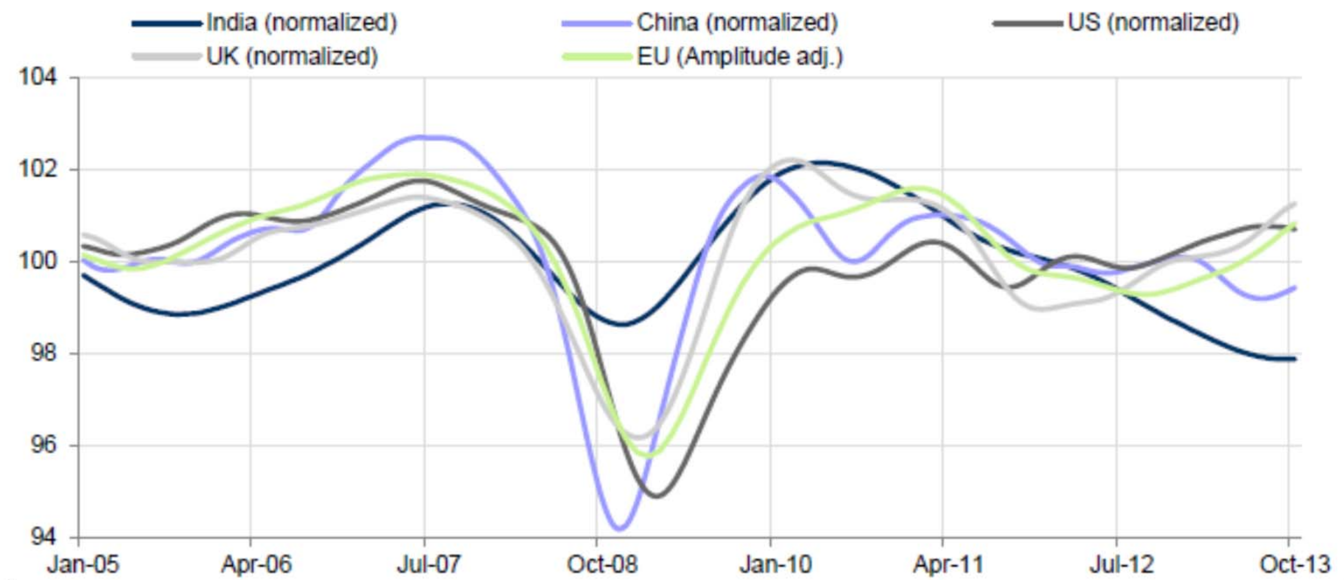
Equity Market Outlook

- Lead Indicators for global economies are providing mixed signals
- India's GDP growth has stabilised at lower levels – sub 5% for 5th consecutive quarter
- Investment cycle continues to remain weak as projects under implementation(but stalled) continue to rise; now almost 10% of total projects under implementation
- India's lead indicator – PMI is providing mixed signals; manufacturing PMI is in expansionary mode while services continue to be in contractionary mode; Composite PMI is implying weak trends ahead
- Current account deficit has exhibited a sharp improvement in 2Q14 to 1.2% of GDP aided by fall in gold imports and pick up in exports
- However high level of inflation and high fiscal deficit continue to be areas of concern
- Valuations are in line with long term averages

Source: Markit Economics, CSO, Morgan Stanley Research, MOSPI, CEIC, RCML, CGA, Capitaline, Quant Global Research, Factset, IBES. PMI: Purchasing Managers Index.

Global Macro - OECD Lead Indicators – Mixed Trends

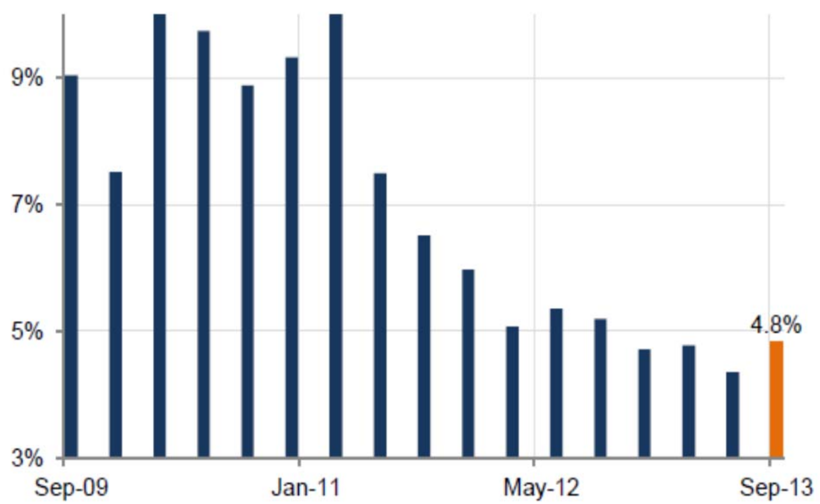


- Euro Zone and UK improved
- US was marginally lower but its GDP growth has bettered expectations
- China registered a marginal improvement

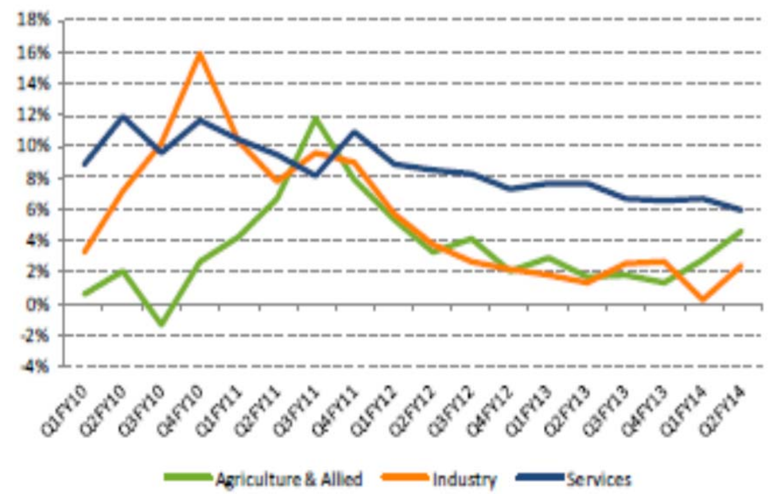
Source: Datastream,RCML Research. **Note**: The Organization for Economic Co-operation and Development (OECD) is system of Composite Leading Indicators (CLIs), a qualitative indicator, which is designed to provide early signals of turning points in business cycles with fluctuations in economic activity around its long-term potential level

India - GDP Growth
Stabilising at lower levels

Quarterly Real GDP Growth (%)



YoY Growth in Agriculture, Industry & Services



- India's GDP grew at 4.8% in 2Q14; 4th consecutive quarter of sub 5% growth
- Good monsoon helped agriculture growth
- Weaker currency also provided a boost as net exports added 4% to growth rather than being a drag

Source: MOSPI, RCML Research, CSO, ICRA Research

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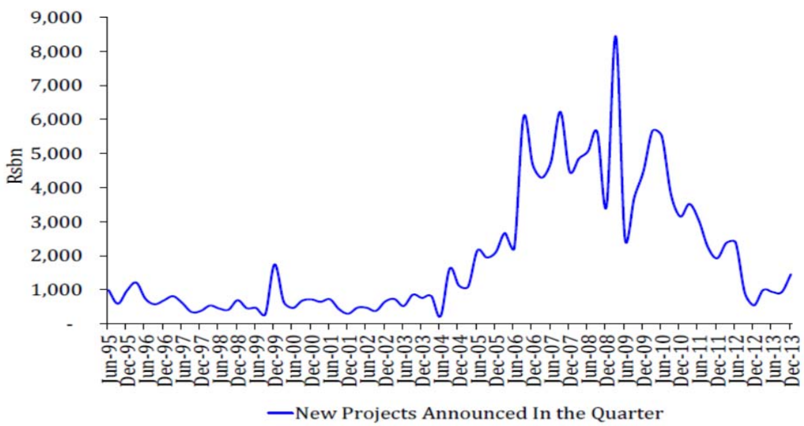
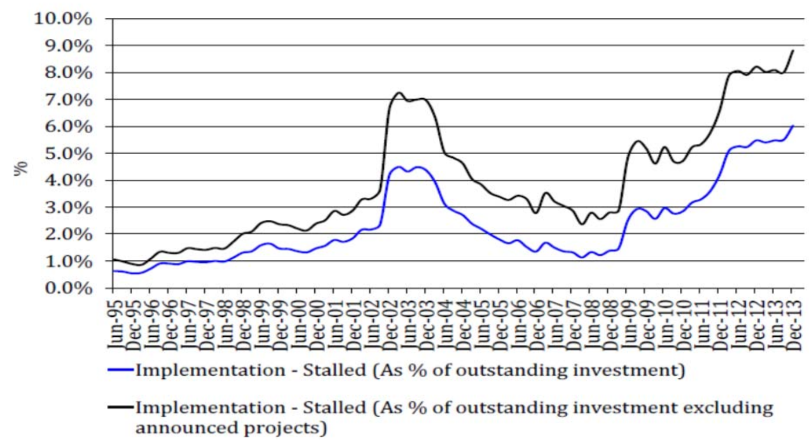
India - Investment Cycle
- Weak

New Project announcements (Rs bn) – back to 96-FY04 levels



Projects under implementation but stalled as % of total O/S Projects

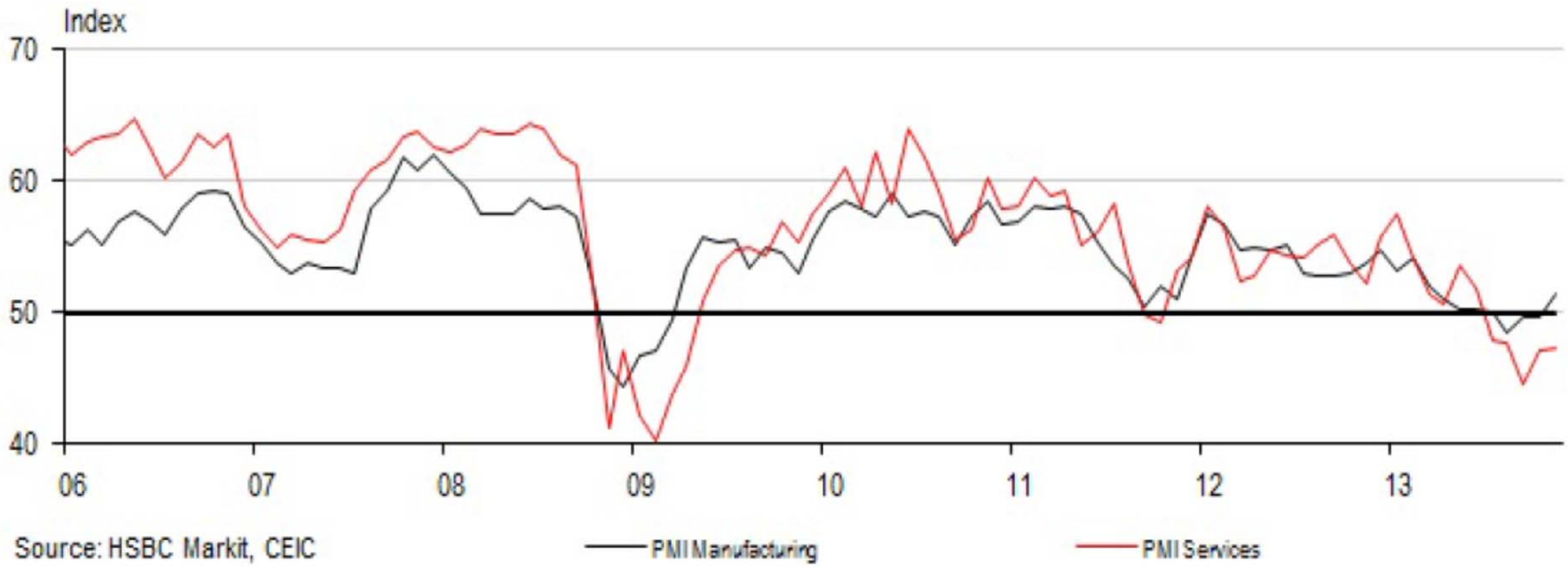


- New project announcements for CY13 are down 14% YoY, after declining 40% and 50% for FY12 and FY13 respectively
- “Projects under implementation but stalled “ continue to rise and represent almost 10% of total projects under implementation
- In order to facilitate passage of high-value infra projects, government has set up a Project Monitoring Group (PMG) in June 2013.
- The group has so far taken up projects valued at Rs. 16.9 tn and resolved projects valued at Rs. 3.8 tn
- Progress of these resolved projects and progress of PMG in resolving remaining projects would be a key factor in revival of the investment cycle in the future

Source: CMIE, Citi Research

India – Lead Indicators
-Mixed

India Manufacturing and Services PMI

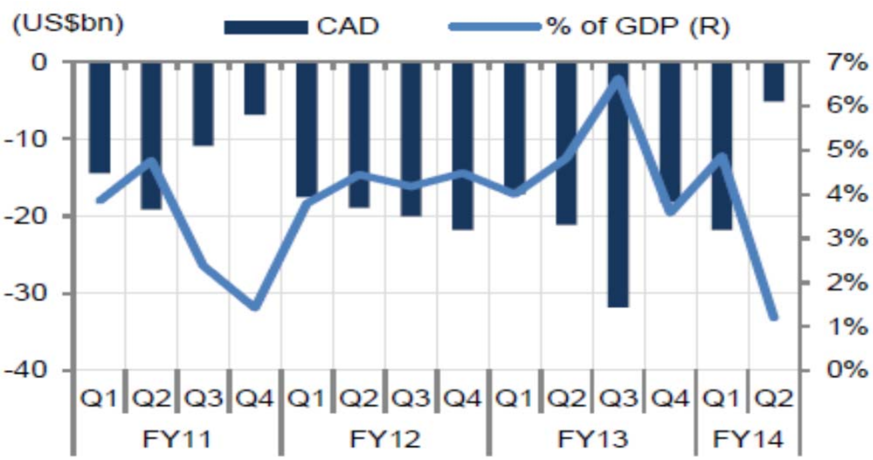


- India Composite PMI in Nov-13 continued to contract (48.5 vs 47.5 in Oct -13) but by less than Oct-13 due to growth in Manufacturing
- Services PMI continued to contract for 5th consecutive month
- Manufacturing PMI returned to expansionary mode in Nov-13 post 4 months of contraction and continued to stay in expansionary mode even in Dec-13

Source: HSBC Markit, CEIC. The above is the monthly data series for the year 2013. PMI: Purchasing Managers Index

India - Twin Deficit
Mixed Developments

Quarterly CAD Trend (US$bn, % of GDP)



Fiscal Deficit (12M Trailing Sum % of GDP)

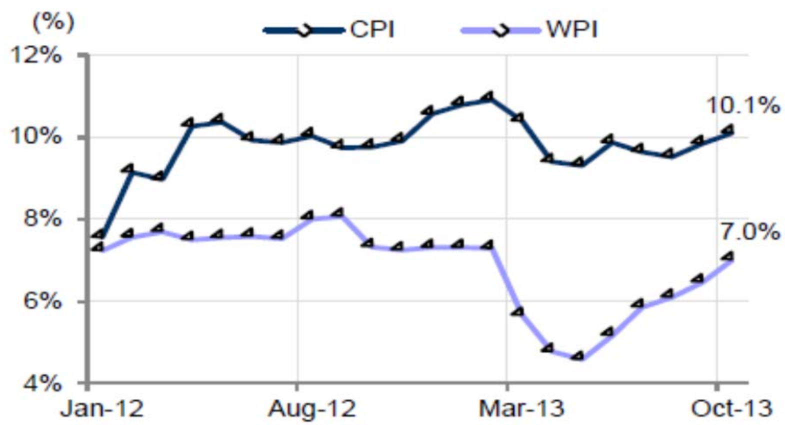
- India's 2Q14 Current account deficit came in at USD 5.2 bn or 1.2% of GDP; sharp fall from 1Q14 of 4.9%
- Growth slowdown, fall in gold imports and a pick up in exports have all contributed to improvement
- But the fiscal deficit continues to be an area of concern as trailing 12-month fiscal deficit (at Nov 2013 end) is at 5.4% against the FY14 full year budgeted estimates of 4.8% of GDP
- Slippage on the fiscal front is largely on account of the shortfall in tax revenues as the economic slowdown has impacted the earnings of the corporate sector

Source: RBI, CGA, RCML Research, Morgan Stanley Research

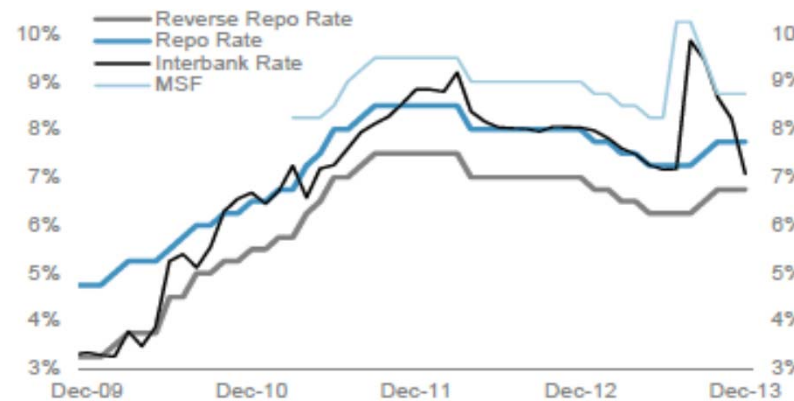
India - Inflation

High and sticky

WPI inching up, CPI remains high



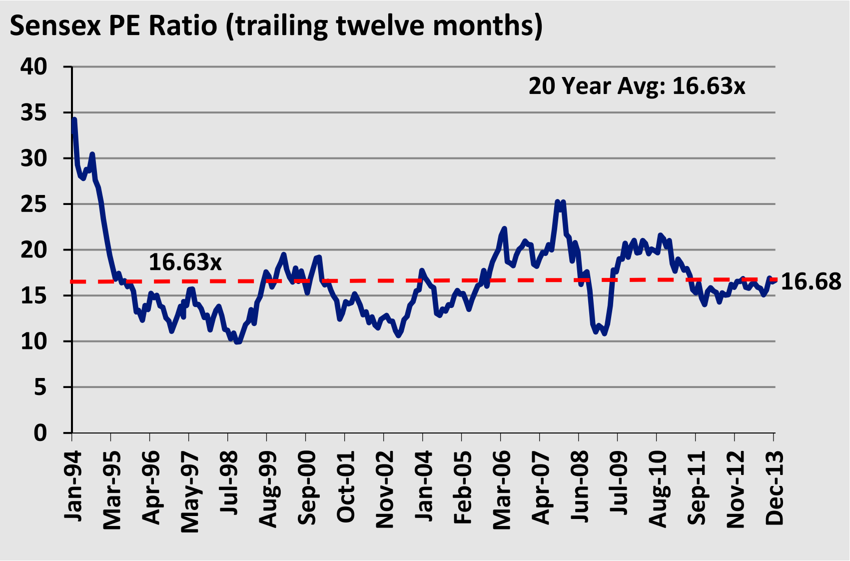
Inter-bank rate vs Policy Rates

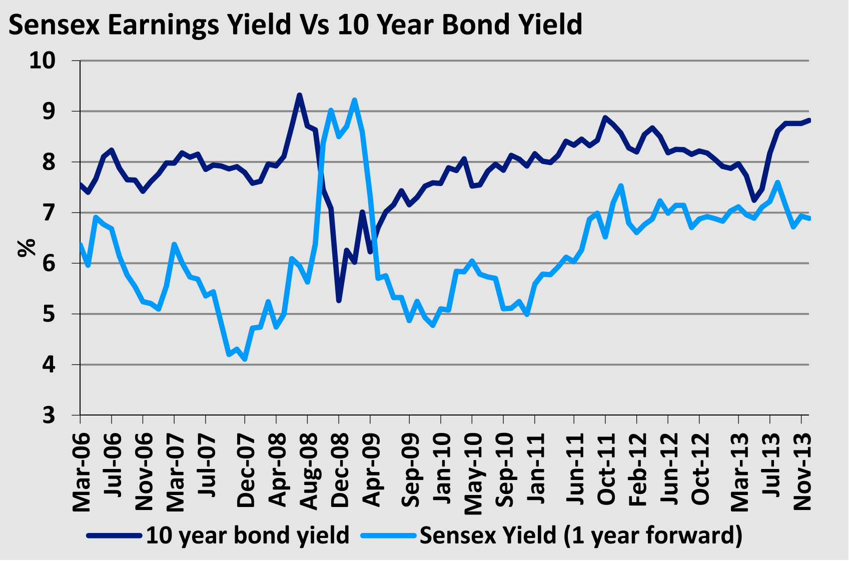


- Inflation both CPI and WPI continue to remain elevated; high and sticky inflation are embedding very high household inflationary expectations
- Expecting a fall in food inflation in coming months, Reserve bank of India maintained status quo and kept interest rates unchanged in its monetary policy. However, high and sticky inflation meant that monetary policy maintained a hawkish stance
- Short term nominal rates (inter-bank call rate) in December eased to near Repo rate (7.75%) as liquidity conditions have improved with FX swap related inflows of 34 bn USD

Source: MOSPI, CEIC, RBI, RCML Research, Bloomberg Finance LP, Deutsche Bank

Valuations - In line with long term averages





- Sensex is currently trading at 16.68x its trailing earnings – in line with historical 20-year average trailing PE of 16.63x
- The FY14 Sensex forward earnings yield gap with the 10- year bond yield which had narrowed to 35 bps in June 2013 has widened to 190 bps

Source: MOSL, Religare Invesco AMC Research

Opportunities – Stock Picking

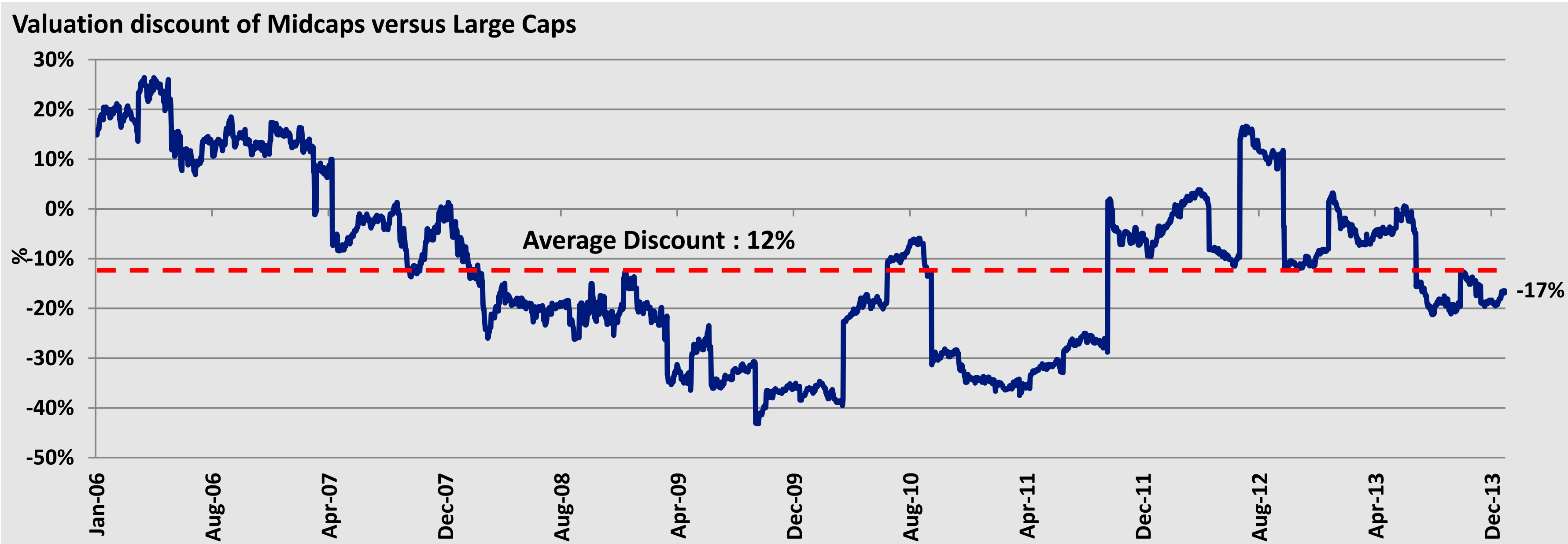
Sectors	2013		2012		2011	
	Best	Worst	Best	Worst	Best	Worst
Auto	50%	-16%	120%	0%	7%	-37%
FMCG	34%	-18%	287%	20%	31%	-66%
Oil & GAS	8%	-23%	49%	-7%	25%	-36%
Banks	13%	-44%	95%	11%	-4%	-45%
Healthcare	107%	-71%	470%	5%	24%	-68%
Capital Goods	45%	-62%	66%	-8%	19%	-67%
IT	126%	0%	599%	-16%	128%	-55%
Metal	26%	-41%	60%	-1%	-4%	-57%
Power	43%	-51%	90%	-8%	2%	-70%

Note: Percent stated above indicate the returns given by best stock & worst stock in respective sectors(in terms of returns). Returns are for calendar year.

- Large Gap between best and worst performing stocks across all sectors highlights importance of stock picking

Source: Bloomberg.

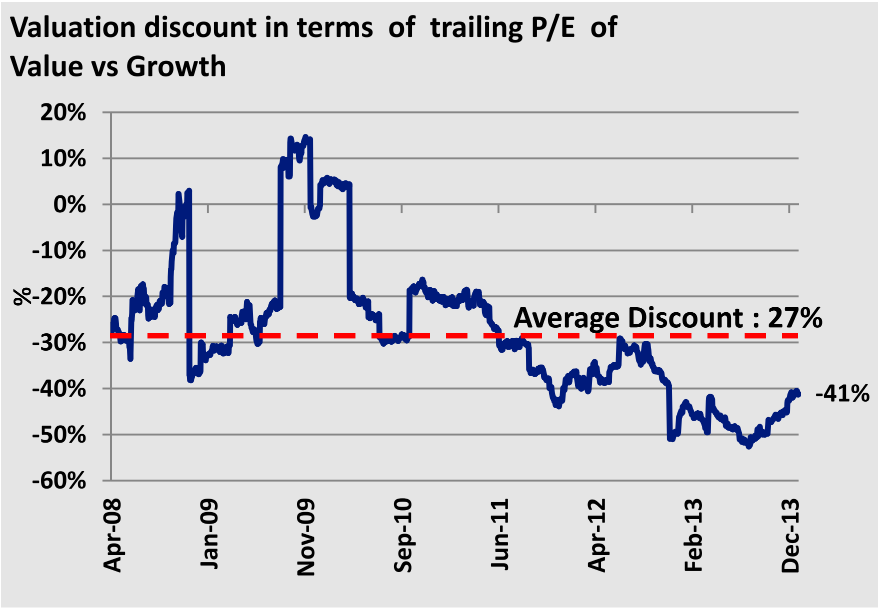
Opportunities – Midcaps trading at a discount to large caps

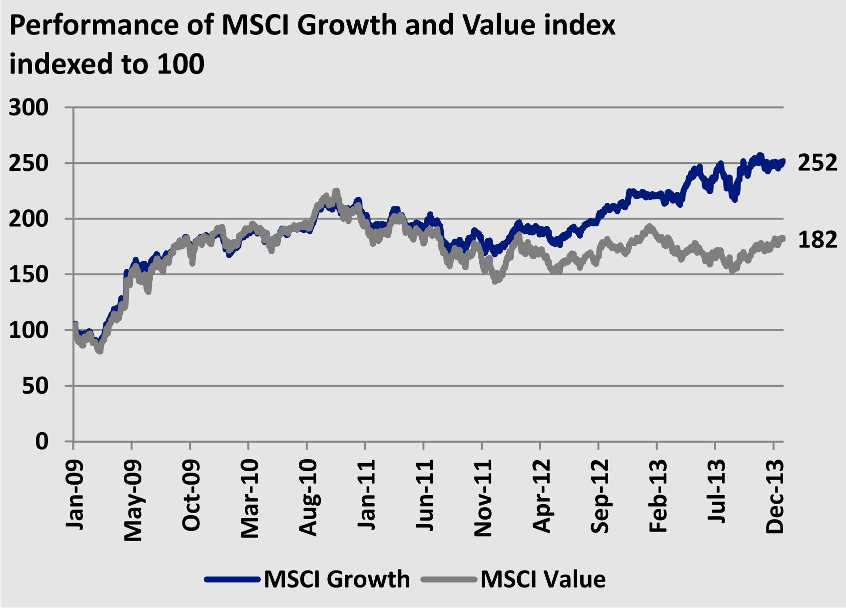


- Valuation discount of midcaps to large caps is 17% compared to the long term average of 12%
- Valuation gap provides attractive bottom opportunities in mid cap space

Source: Bloomberg

Opportunities – Valuation Gap between Growth and Value

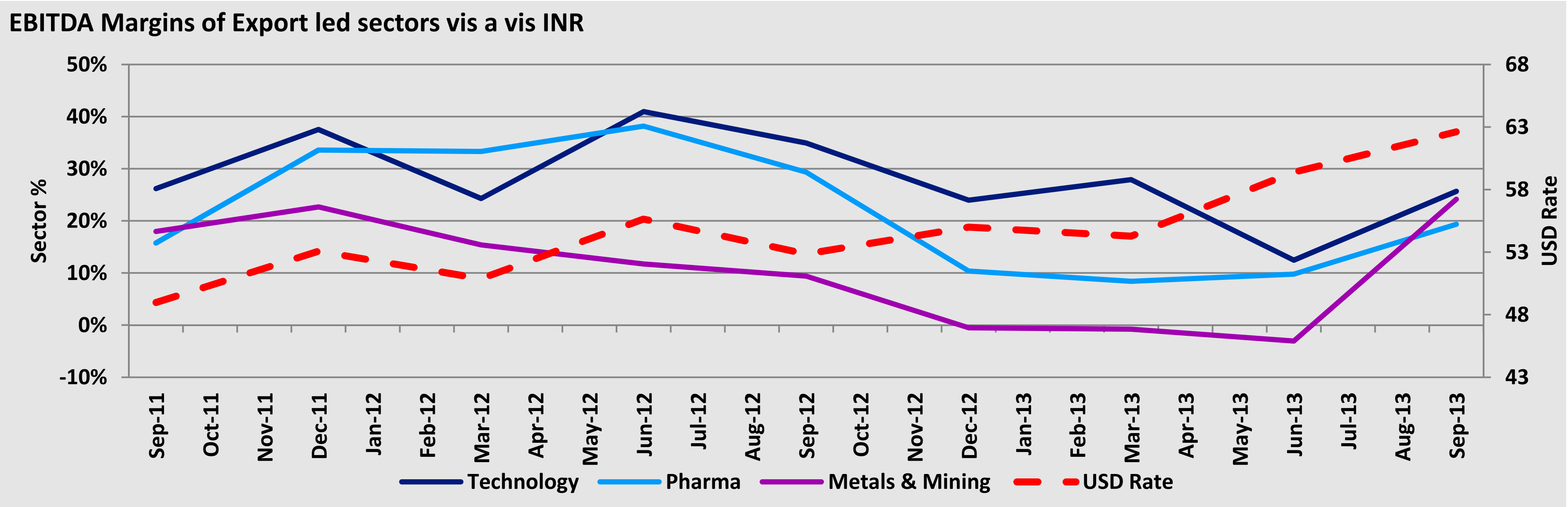




- Valuation discount of MSCI India Value Index to MSCI India Growth index is 41% compared to the long term average of 27%
- Since 2009, MSCI growth index has significantly outperformed MSCI Value index

Source: Bloomberg

Opportunities – Beneficiaries of Currency Depreciation



- INR Depreciation has provided a significant lever for exporters. This can be utilised either to boost volumes or make investments
- 16 companies out of 30 companies of Sensex representing 58% of total market cap of Sensex are beneficiaries of currency depreciation

Source: Bloomberg, Kotak Intuitional Equities; EBITDA Margin for each sector = Total Reported EBITDA Margins for companies under coverage within the sector/Total Reported Net Sales for companies under coverage within the sector

Market Outlook

RELIGARE Invesco Mutual Fund

- Valuations are in line with long term averages; they are neither cheap nor expensive
- Given current valuations; our emphasis on bottom up stock picking continues
- Small & Midcap companies are at an attractive discount to large cap stocks
- Incrementally, we are more constructive on companies belonging to cyclical sectors like Industrials, Consumer Discretionary and Materials due to attractive valuations. While most of these companies do not offer strong near term growth visibility, we are willing to take the risk due to attractive valuations
- We have also added exposure to companies, which are beneficiaries of currency depreciation
- We continue to avoid companies with balance sheet risk

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