Equity Markets :

Current Environment and Outlook

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January 2013

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Current Environment

- Global Equity markets went up in January 2013, with the MSCI World Index rising by 5.93%
- Indian markets under performed the global market trend and rose by 2.41%
- Commodity prices under performed the trend in equities, as benchmark CRB Reuters Jefferies total return index was up by 2.8% during the month
- IT and Teck were the best performing sectors while Metal and Auto were worst performing sectors during the month*
- FII inflows during the month were at Rs.221 bn. MF's were net sellers at Rs.52 bn, while DII's were net sellers of Rs.175 bn during the month
- Trading Activity increased in January as cash market trading turnover rose by 22% MoM. Average open interest remained flat MoM

* Please refer slide 4 for sector performances

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 Source: RMF, Bloomberg

Global Equities

Index	Country	Closing Price*	1 Month Return (%)	YTD Return (%)	Category
SSE Composite Index	China	2385.42	5.13%	5.13%	EM - Asia
BSE Sensex	India	19894.98	2.41%	2.41%	EM - Asia
Kospi	South Korea	1961.94	-1.76%	-1.76%	EM - Asia
Taiwan Weighted	Taiwan	7850.02	1.95%	1.95%	EM - Asia
Thailand SET 50 Index	Thailand	988.21	4.53%	4.53%	EM - Asia
Jakarta Composite Index	Indonesia	4453.70	3.17%	3.17%	EM - Asia
KLSE	Malaysia	1627.55	-3.64%	-3.64%	EM - Asia
Ibovespa Sao Paulo Index	Brazil	59761.49	-1.95%	-1.95%	EM
Mexico IPC	Mexico	45278.06	3.56%	3.56%	EM
Russian RTS Index	Russia	1622.13	6.23%	6.23%	EM
Philippine PSEi	Philippines	6242.74	7.40%	7.40%	EM
Merval Buenos Aires Index	Argentina	3462.42	21.31%	21.31%	EM
HangSeng	Hong Kong	23729.53	4.73%	4.73%	Developed - Asia
Nikkei	Japan	11138.66	7.15%	7.15%	Developed - Asia
Strait Times	Singapore	3282.66	3.65%	3.65%	Developed - Asia
Dow Jones	USA	13860.58	5.77%	5.77%	Developed
CAC 40 Index	France	3732.60	3.10%	3.10%	Developed
All Ordinaries Index	Australia	4901.01	4.60%	4.60%	Developed
DAX Index	Germany	7776.05	2.15%	2.15%	Developed
Swiss Market Index	Switzerland	7390.86	8.33%	8.33%	Developed
FTSE 100	UK	6276.88	6.43%	6.43%	Developed
MSCI World Index	--	1405.47	5.93%	5.93%	--

* as on 31st January, 2013. Source: Bloomberg
EM – emerging markets, Developed – developed markets

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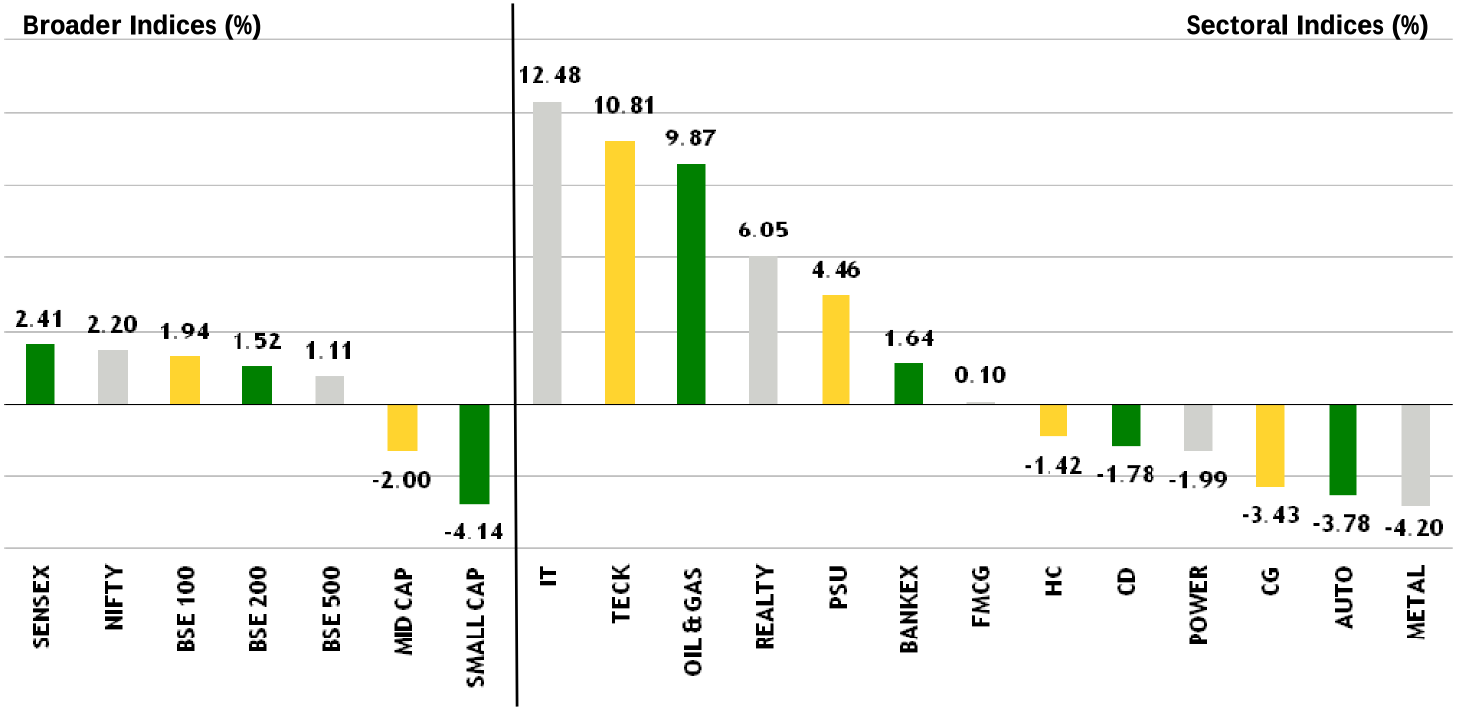
India : Sector performances



- Nifty rose by 2.2% over the previous month
- MidCaps and Small Caps underperformed LargeCaps with 2% fall and 4.14% fall respectively
- IT and Teck sectors delivered the best return for the month
- Metal and Auto were the worst performing sectors

Source: BSE,NSE. one month performance as on 31st January, 2013. CD: Consumer Durables, CG: Capital Goods, HC: Health Care. FMCG: Fast Moving Consumer Goods

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Top Gainers / Losers - Nifty

Top Gainers for the month			
Gainers	52 week H/L	Last Price#	% Gain*
ONGC Ltd	355 / 227.4	339.7	26.75%
DLF Ltd	279.4 / 169.75	277.6	20.38%
Infosys Ltd	2994 / 2060.55	2789.5	20.30%
BPCL Ltd	449 / 282.33	410.45	15.18%
HCL Technologies Ltd	721.3 / 439.5	688	11.20%
Top Losers for the month			
Losers	**52 week H/L**	**Last Price#**	**% Loss***
Tata Power Co. Ltd	121.2 / 84.6	101.1	-8.38%
Hindustan Unilever Ltd	580.45 / 376.1	473.95	-9.70%
Jaiprakash Associates Ltd	106.7 / 58	86.95	-10.27%
Hindalco Industries Ltd	164.9 / 100	116.2	-10.96%
Ranbaxy Laboratory Ltd	578.4 / 395	447.65	-11.00%

closing price as on 31st January, 2013.* one month performance as on 31st January, 2013.
Source: Capitaline

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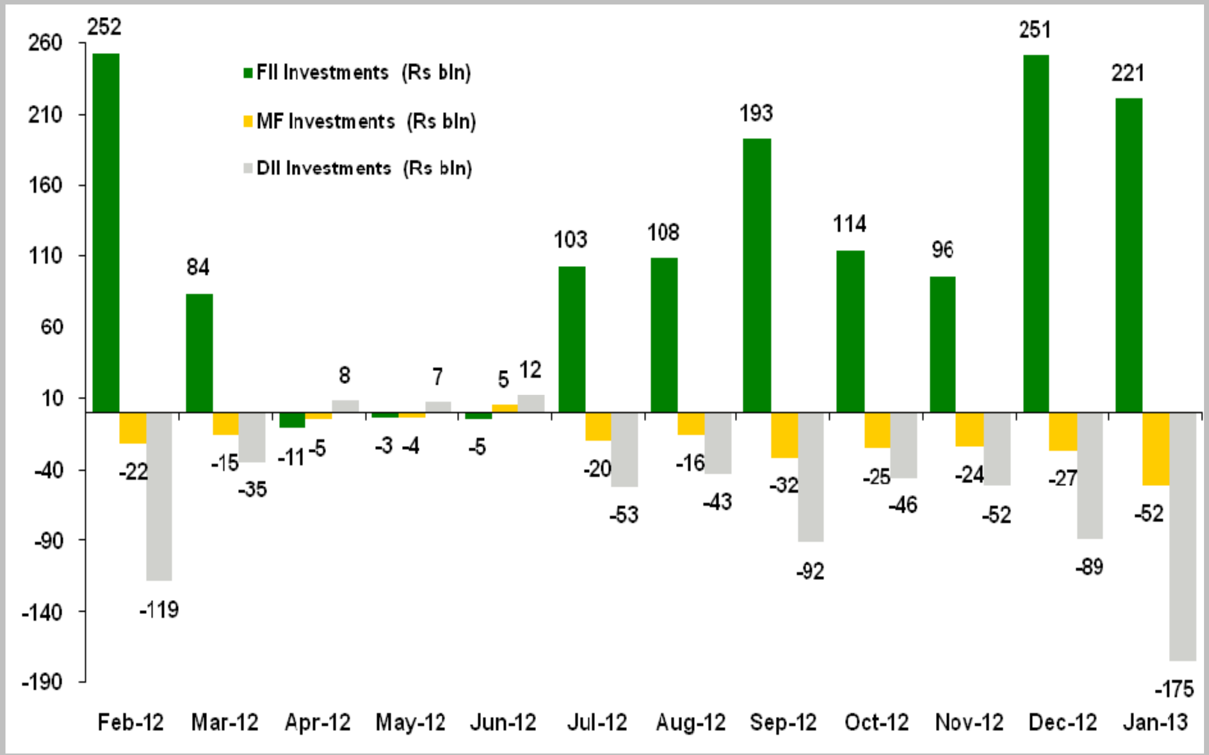
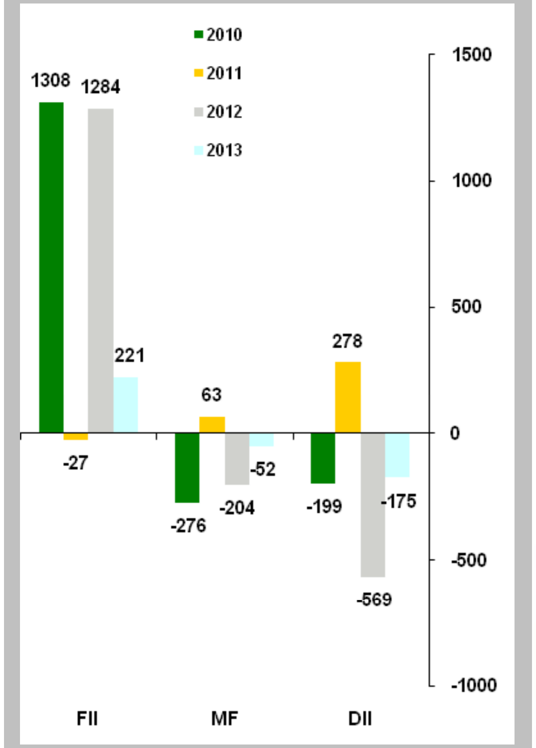
FII & DII Inflows



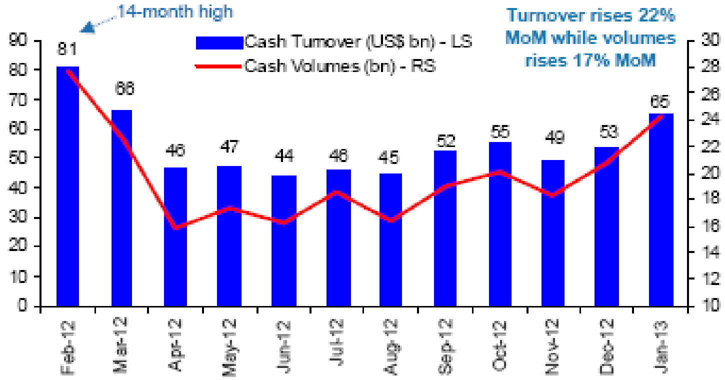


- Institutional activity was mixed during the month
- FII inflows during the month were at Rs. 221bn. FII inflows were at Rs. 1284bn for CY12 after a Rs.27 bn outflow in CY11 and Rs.1308bn inflow in CY10
- MF’s and DII continued to be net sellers at Rs 52 bln and Rs 175 bln during the month

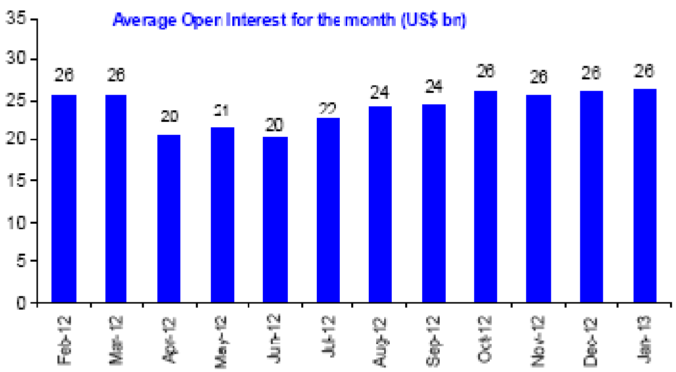
FII - Foreign Institutional Investors, DII - Domestic Institutional Investors (Includes Bank, DFIs, Insurance and MF)
Source: SEBI, BSE

Market Activity

Cash Turnover & Volumes: 11-Month Highs



Average Open Interest: Rises Marginally MoM



- In Jan 2013, cash market trading turnover rose by 22% MoM
- At the end of January 2013, average open interest remained flat on a MoM basis

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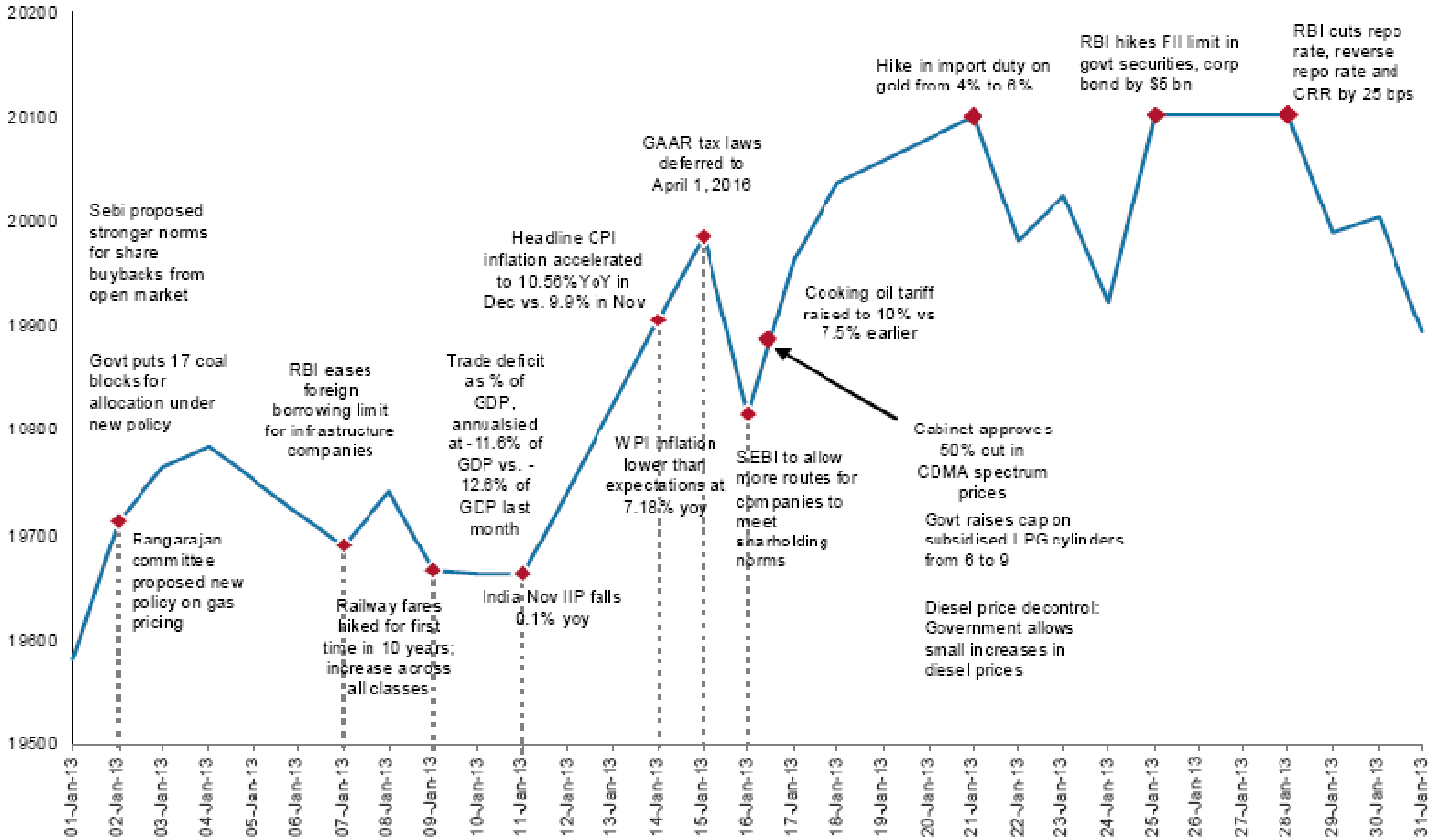
Sources: Bloomberg, Morgan Stanley

January 2013 events timeline



Source: Bloomberg, Economic Times, Business Standard, Morgan Stanley Research.
Note: The above shown index is BSE Sensex .

Religare MF: Equity Market Outlook and Opportunities

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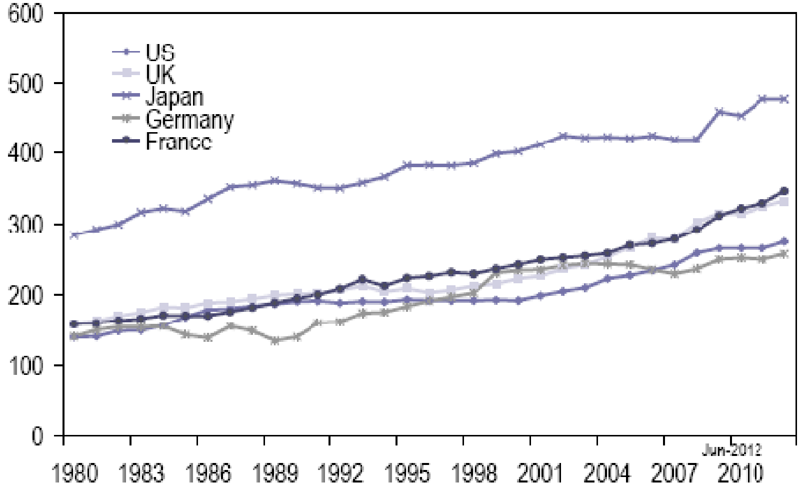
Equity Market Outlook

- The de-leveraging of advanced economies is likely to weigh down heavily on their national income growth rate
- Global economic conditions led by emerging markets and US have improved modestly in Dec'12 to 3%
- However future forecasts for global economies continue to be scaled downwards by international agencies
- India's GDP growth is stabilsing at lower levels of 5%-5.5% range and expected to improve going ahead
- However one of the key drivers – revival in investment demand remains weak
- While wholesale inflation has moderated, India continues to face headwinds from its twin deficits – current and fiscal
- RBI has reduced key policy rates and CRR by 25 bps
- Moderation in inflation and positive signal from government on reigning in fiscal deficit provides space, albeit limited, for RBI to give greater emphasis to growth and adopt an accommodative stance
- Earnings season so far has been slightly better than beaten down estimates. Economic slowdown is now quite widespread with weakness reflected even in non cyclical sectors like FMCG and consumer staples.
- Consensus expectations of earning forecasts for FY13E and FY14E have stabilised at around 5% and around 14%-15% respectively

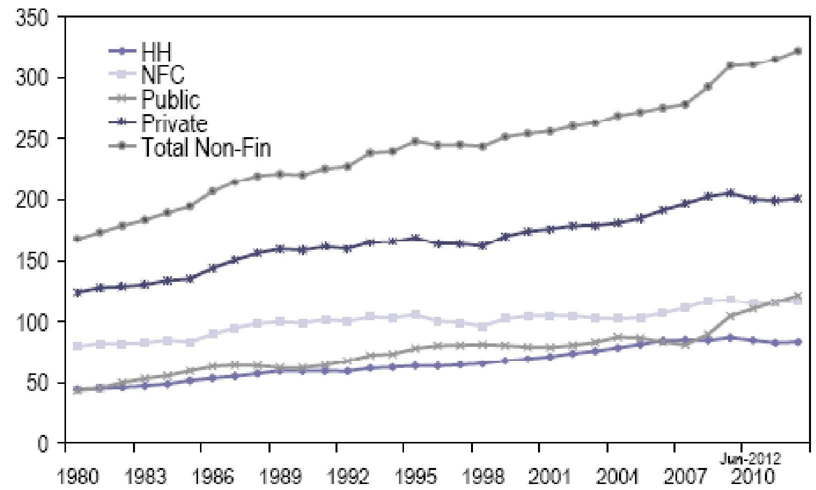
Source: RMF, FactSet, IBES Estimates, Morgan Stanley Research, Citi Research, Bloomberg

Global Macro – Debt stock fairly high, deleveraging ahead

Non Financial Sector Gross Debt as % of GDP



Advanced Economics – Gross Debt by Sector – (% of GDP)



- Total non-financial sector (NFS) gross debt in 17 developed markets rose from $12.3 trillion or 168% of the GDP in 1980 to $128.5 trillion (over 10X) in 2011 amounting to 315% of GDP
- Although growth in debt has slow down since 2008, it has not led to any deleveraging yet as economic growth has also slow down
- Deleveraging is likely to continue to weigh heavily on growth in highly indebted economies

Note: Advanced economy gross debt by sector is constructed as gross debt weighted by shares of nominal GDP in 17 countries (Australia, Austria, Belgium, Canada, Finland, Germany, Greece, Italy, Japan, Korea, Netherland, Portugal, Spain, Sweden, UK and US). HH: House Hold, NFC: Non Financial Companies

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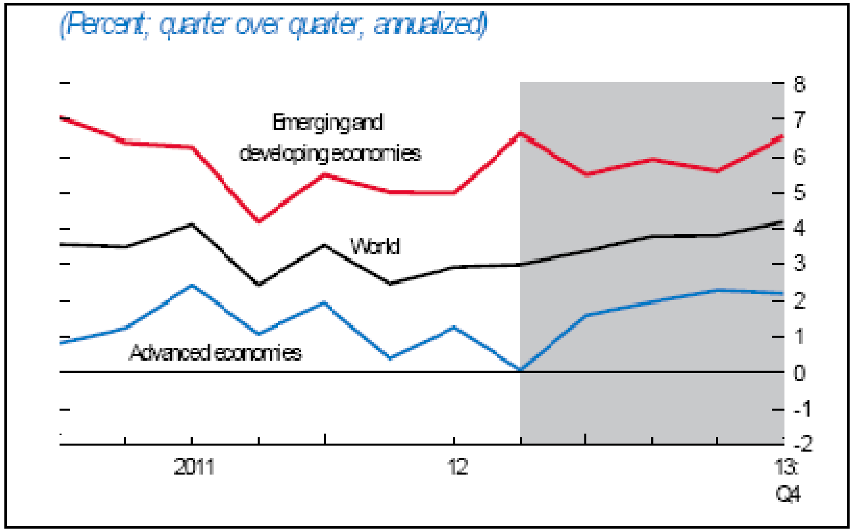
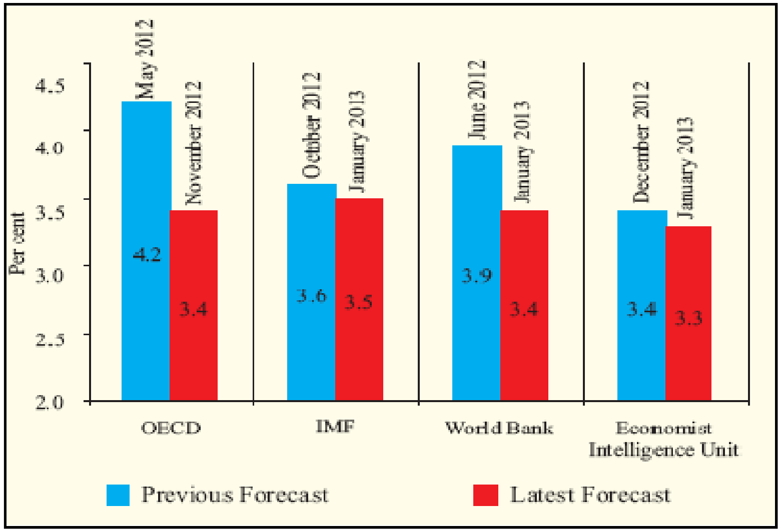
Source: IMF, OECD, National Sources and Citi Research

Global Macro – Modest improvement, outlook weak

Global GDP Growth



Global Growth forecasts for FY13E

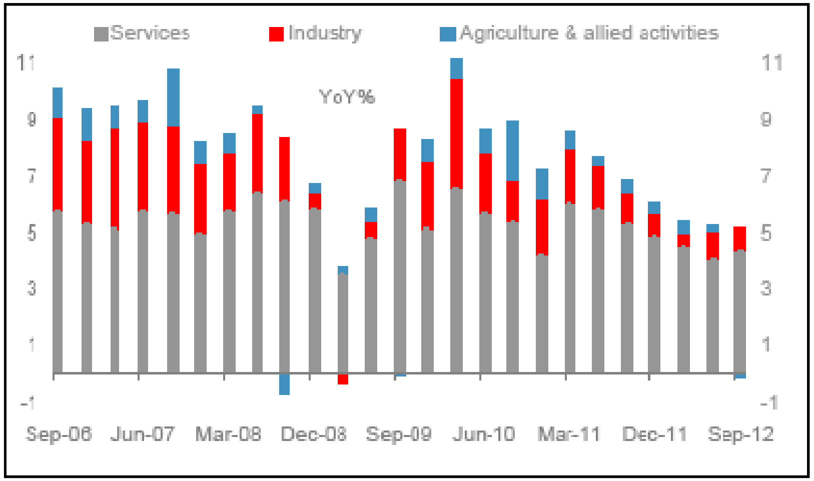


- Global Economic conditions improve modestly in 3rd quarter 2012 – global growth increased to 3%
- Main source of Growth acceleration were emerging markets
- Within advanced economies, trends were mixed - US expanded 3.1% while Euro and Japan contracted
- Even in US, growth uptick was partly due to temporary factors, including inventory accumulation
- Global Growth forecasts for FY13 – being scaled downwards by international agencies

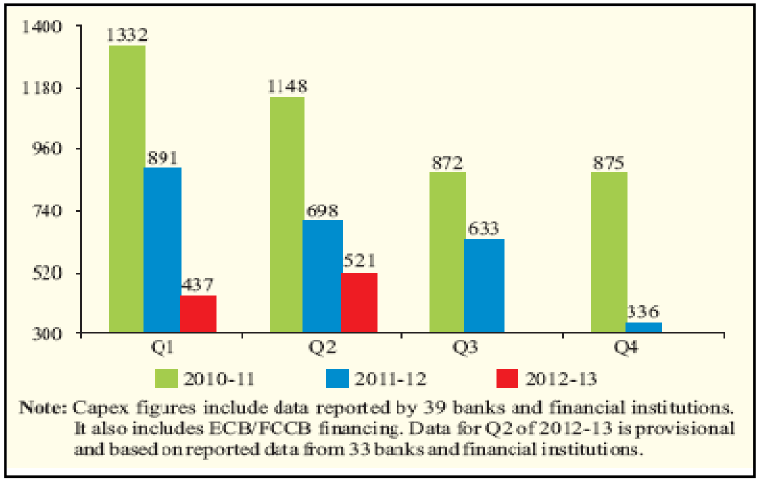
Source: IMF, RBI

India’s GDP Growth – stabilizing at lower levels

Quarterly GDP growth trend



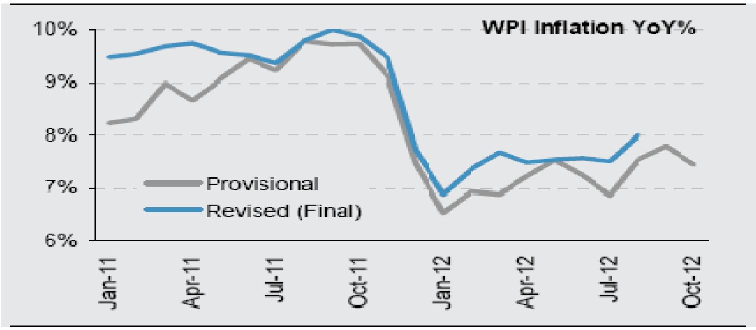
Value of fresh Sanctions (Rs. Billion)

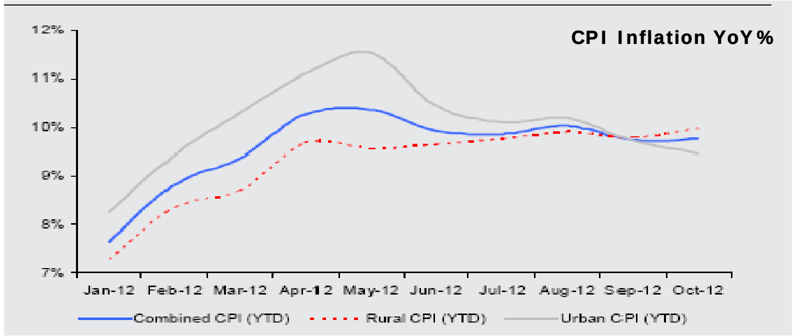


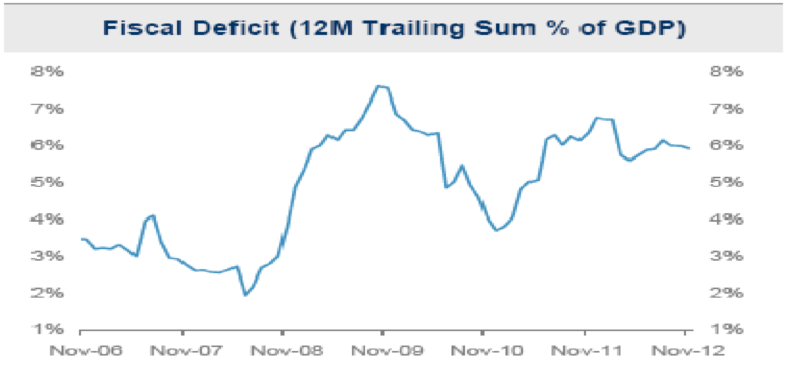
- India’s GDP growth – stabalizing at lower levels of 5-5.5% range
- RBI has cut FY13E GDP forecast from 5.8% to 5.5%
- RBI’s survey of Professional forecasters projects FY13-14E GDP growth to improve to 6.5% led by revival in investment demand
- But overall investment cycle remains quite weak – sanctions for fresh projects down 25% YoY during 2Q13.

 Source: RBI , Morgan Stanley Research, CSO,

India's Macro Economic Indicators – still streched







- While Growth has stabilised and inflation has moderated, trade and fiscal deficit are still stretched
- Trade deficit narrowed in December but still remain fairly elevated at 11% of GDP
- Fiscal Deficit for the period April – November grew by 16.9% YoY as against budget targets of 0.8% growth for the full year
- Recent Government measures to contain fiscal deficit like partial deregulation of diesel prices, cut back in plan and non plan expenditure, thrust on divestment and increased thrust on direct transfers of subsidies are encouraging signals to address fiscal imbalances

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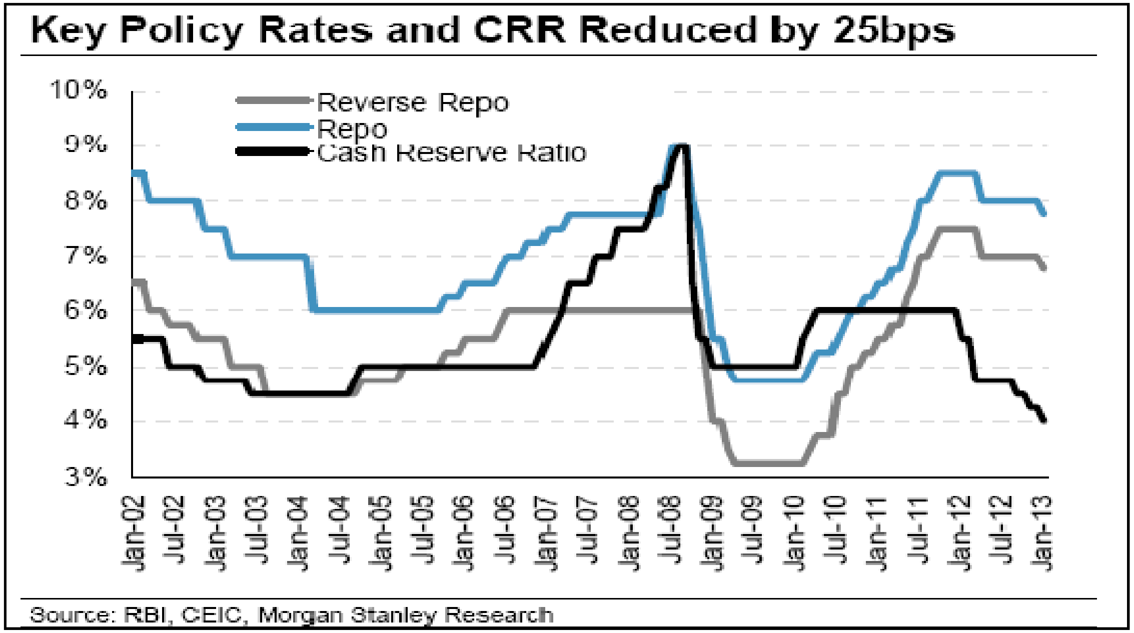
Source: RBI, CEIC, Morgan Stanley Research

Reserve Bank - cuts interest rates



- Reserve Bank of India in its quarterly review of monetary policy on January 29, lowered the repo rate and reverse repo rate by 25 bps each to 7.75% and 6.75%.
- The Cash Reserve ratio (CRR) was also cut by 25 bps to 4%
- Moderation in inflation and positive signal from government on reigning in fiscal deficit provides space, albeit limited for RBI to give greater emphasis to growth and adopt an accommodative stance
- However scope for future rate cuts is limited and downcycle in rates unlikely to resemble 2008-09 experience

Source: RBI, CEIC, Morgan Stanley Research

Dec 2012 Earnings so far – slightly better than beaten down estimates

Quarterly Earnings for QE Dec-12 Snapshot

YoY Revenue growth	Q4F12	Q1F13	Q2F13	Q3F13E	Q3F13E*	Q3F13
MS coverage	22%	14%	14%	7%	11%	14%
MS coverage ex-oil psu	16%	17%	14%	9%	11%	14%
MS coverage ex-energy	16%	16%	12%	9%	11%	12%
Broad Market (1179)	20%	14%	15%		-	-
Broad Market ex-oil psu	19%	15%	13%		-	-
Broad Market ex-energy	16%	15%	12%		-	-
BSE Sensex	19%	17%	12%	9%	9%	12%
YoY Earnings growth	**Q4F12**	**Q1F13**	**Q2F13**	**Q3F13E**	**Q3F13E***	**Q3F13**
MS coverage	33%	-43%	64%	9%	14%	12%
MS coverage ex-oil psu	10%	6%	11%	10%	14%	12%
MS coverage ex-energy	16%	13%	13%	9%	12%	9%
Broad Market (1179)	19%	-33%	61%		-	-
Broad Market ex-oil psu	4%	3%	20%		-	-
Broad Market ex-energy	6%	6%	20%		-	-
BSE Sensex	19%	15%	4%	10%	12%	13%

- So far, 16 Sensex companies have reported topline growth of 12% against expectation of 9% and earnings growth of 13% against expectation of 12%

- In terms of broader market, earnings are showing a similar modest trends with sales growth of 10%, EBITDA growth of 14% and Net profit growth of 11%

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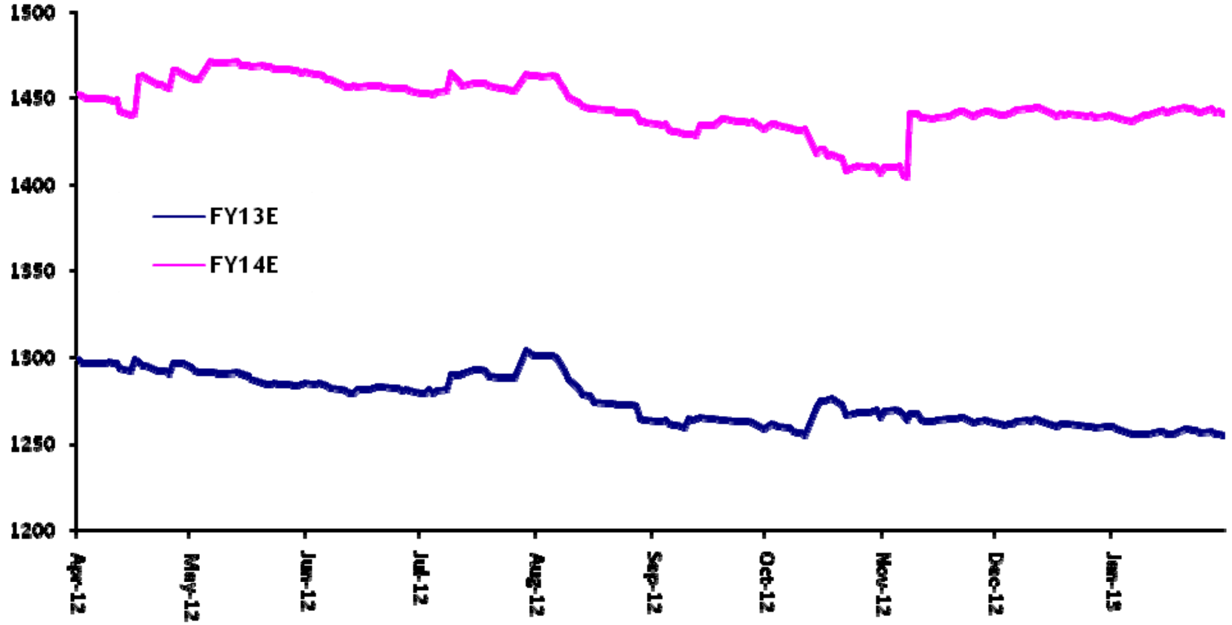
Sources: Company data, Capitaline, Morgan Stanley Research

Earnings Forecasts – Stable



- Consensus expectations for FY13E earnings growth are at about 5.2% growth, revised downwards by 0.6% during last one month
- However, expectations for FY14E EPS have also been revised upwards by 0.1% implying a growth expectation of 14.8%

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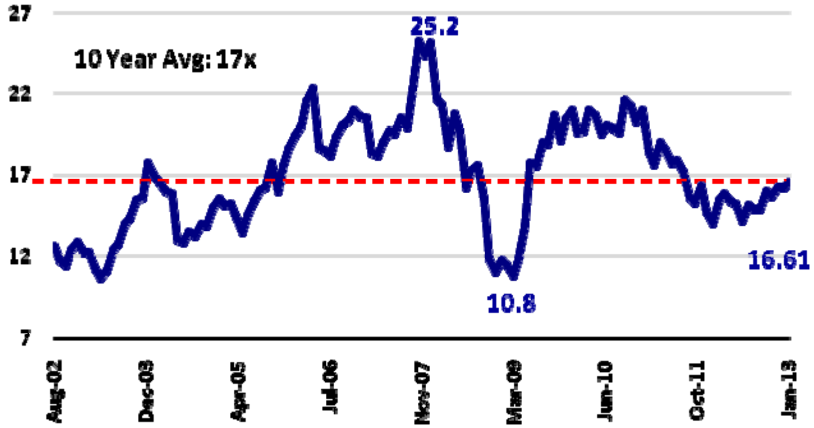
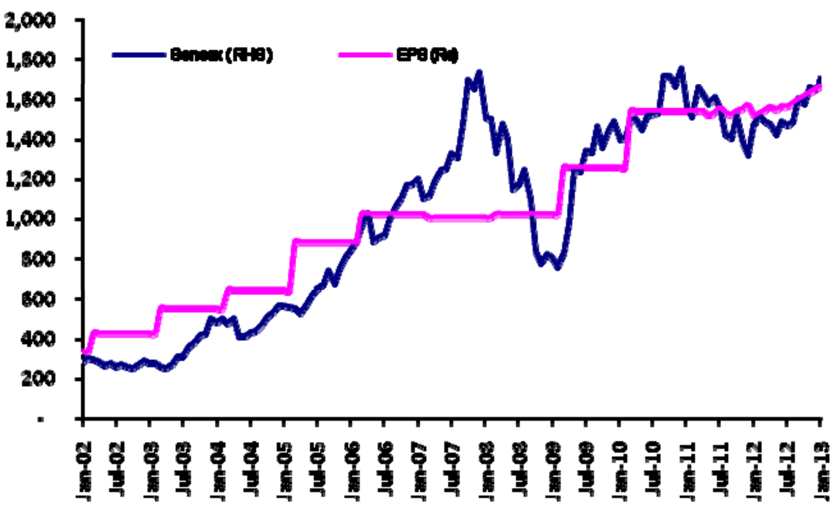
 Sources: IBES Estimates, Bloomberg

Valuations – At Reasonable Levels

Sensex PE Ratio (trailing twelve months)





- Sensex is currently trading at 16.61x its trailing earnings. It is now 4% lower than its historical 10-year average trailing PE of 17x
- On a 1-yr forward basis, Sensex is trading at 14.6x which at 1.7% premium to its 10 year average PE
- The de-rating of market since 2007 is evident in the accompanying chart with earnings considerably above the 2007 levels whereas the markets have not progressed much over the past 5 years

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Source: Bloomberg; MOSL

Looking Ahead...

- Global growth – Expected to strengthen gradually through 2013 but lower than previous projections
- Japan’s currency depreciation versus major currencies to have a significant negative impact on top global exporters – mainly Euro region and number of export oriented emerging market economies
- India’s growth has stabilised at 5%-5.5% range and expected to improve led by revival in investment demand. However current weak trends pertaining to investment cycle provide poor visibility for revival and to that extent pose a risk to FY14E GDP forecasts
- Government’s focus on fiscal deficit reduction – although will add pain in short term will be a key catalyst in reviewing the investment cycle in the long term
- However there is degree of uncertainty towards complete execution of announced measures and translation of intent into action given it’s a pre election year
- Valuations are reasonable; but at a slight premium to long term averages
- Gap in terms of valuations between cyclicals and non cyclicals is fairly high with non cyclicals trading at very rich valuations
- Overall emphasis on bottom up stock selection continues
- Companies with businesses having reasonable growth prospects and in a healthy financial position, which can ride out the challenging environment and benefit from an improvement in the economic outlook would be preferred. We are also open to making selective investments in areas where valuations already reflect a high degree of stress

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