

# Equity Markets : Current Environment and Outlook

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# Current Environment

- Global Equity markets consolidated its gains in July, with the MSCI World Index rising by 1.2%.
- Indian markets under performed their global peers, falling by 1.1%.
- Commodity prices rose sharply with the benchmark CRB Reuters Jefferies total return index rising by 5.4%.
- Healthcare and Consumer Durables were the best performing sectors, while IT and Teck sectors delivered the worst return for the month\*.
- FII inflows during the month were at Rs.103bn. MF's were net sellers at Rs.20bn, while DII's were net sellers of Rs.53bn during the month.
- Trading Activity increased in July, with the cash market trading turnover increasing by 11% MoM and the average open interest increasing by 10% on a MoM basis.

\* Please refer slide 4 for sector performances



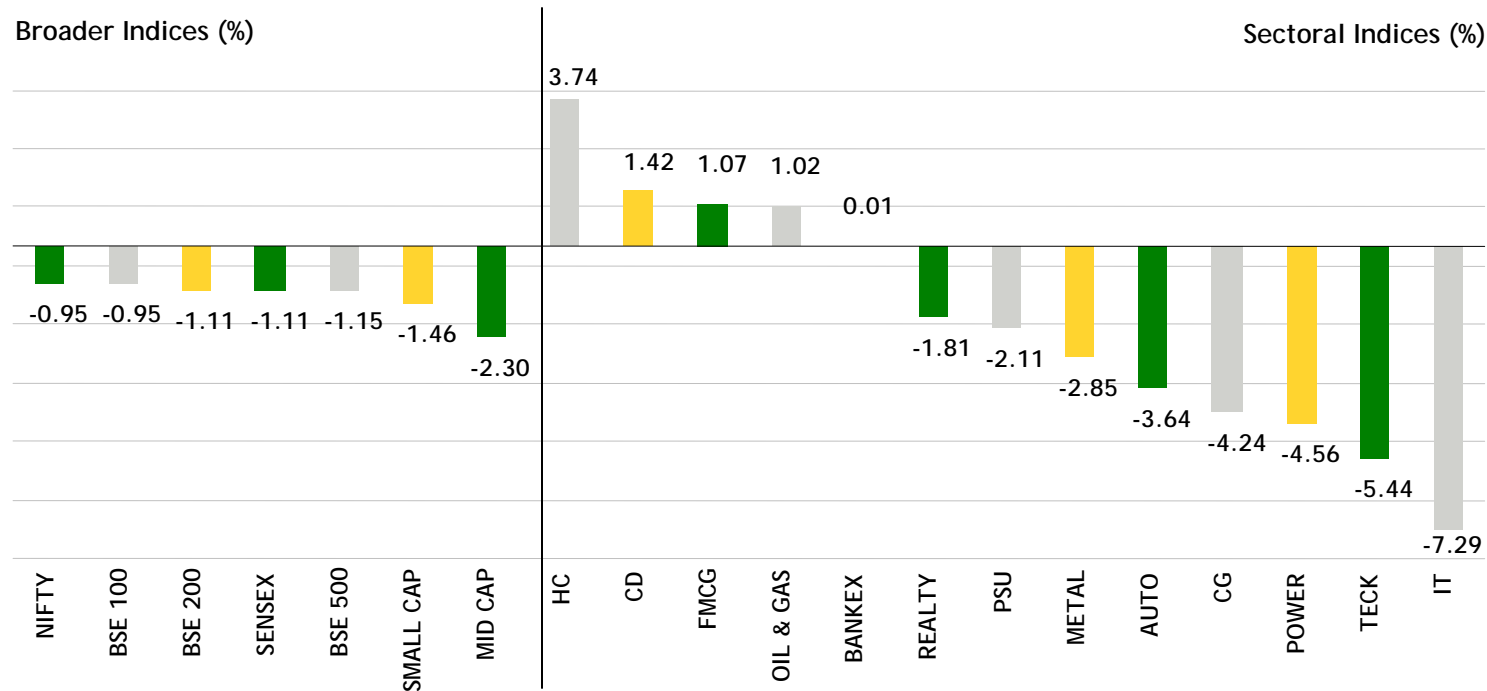
# Global Equities

Index	Country	Closing Price*	1 Month Return (%)	YTD Return (%)	Category
SSE Composite Index	China	2103.64	-5.47%	-4.35%	EM - Asia
BSE Sensex	India	17236.18	-1.11%	11.53%	EM - Asia
Kospi	South Korea	1881.99	1.51%	3.08%	EM - Asia
Taiwan Weighted	Taiwan	7270.49	-0.35%	2.81%	EM - Asia
Thailand SET 50 Index	Thailand	828.67	1.75%	15.35%	EM - Asia
Jakarta Composite Index	Indonesia	4142.34	4.72%	8.38%	EM - Asia
KLSE	Malaysia	1631.60	2.03%	6.59%	EM - Asia
Ibovespa Sao Paulo Index	Brazil	56097.05	3.21%	-1.16%	EM
Mexico IPC	Mexico	40704.28	1.26%	9.78%	EM
Russian RTS Index	Russia	1377.35	1.99%	-0.33%	EM
Philippine PSEi	Philippines	5307.66	1.17%	21.40%	EM
Merval Buenos Aires Index	Argentina	2400.31	2.29%	-2.53%	EM
HangSeng	Hong Kong	19796.81	1.83%	7.39%	Developed - Asia
Nikkei	Japan	8695.06	-3.46%	2.84%	Developed - Asia
Strait Times	Singapore	3036.40	5.49%	14.74%	Developed - Asia
Dow Jones	USA	13008.68	1.00%	6.48%	Developed
CAC 40 Index	France	3291.66	2.97%	4.17%	Developed
All Ordinaries Index	Australia	4289.38	3.72%	4.34%	Developed
DAX Index	Germany	6772.26	5.55%	14.82%	Developed
Swiss Market Index	Switzerland	6399.27	5.48%	7.80%	Developed
FTSE 100	UK	5635.28	1.15%	1.13%	Developed
MSCI World Index	--	1250.57	1.20%	5.75%	--

\* as on 31<sup>st</sup> July, 2012. Source: Bloomberg  
EM – emerging markets, Developed – developed markets.



# India : Sector performances



- Nifty fell by 0.95% over the previous month.
- MidCaps and SmallCaps under performed LargeCaps with 2.3% fall in the MidCap index and 1.46% fall in SmallCap index.
- Healthcare and Consumer Durables were the best performing sectors.
- IT and Teck sectors delivered the worst return for the month.

Source: BSE,NSE. one month performance as on 31<sup>st</sup> July, 2012. CD: Consumer Durables, CG: Capital Goods, HC: Health Care. FMCG: Fast Moving Consumer Goods



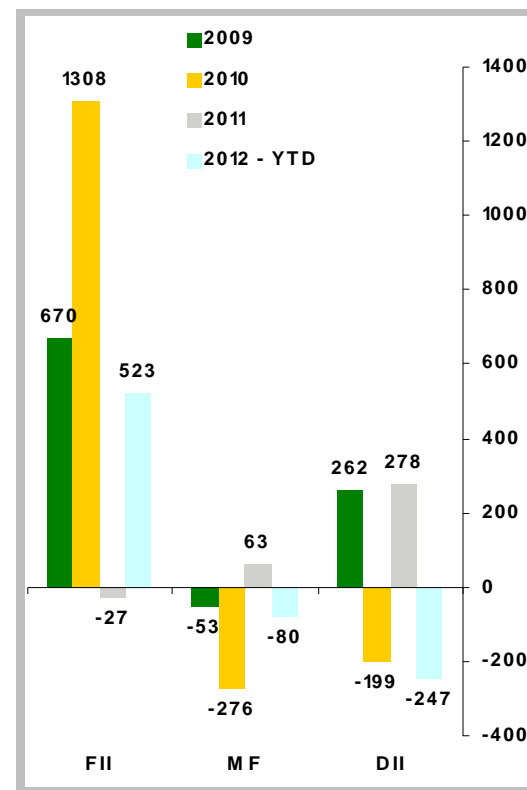
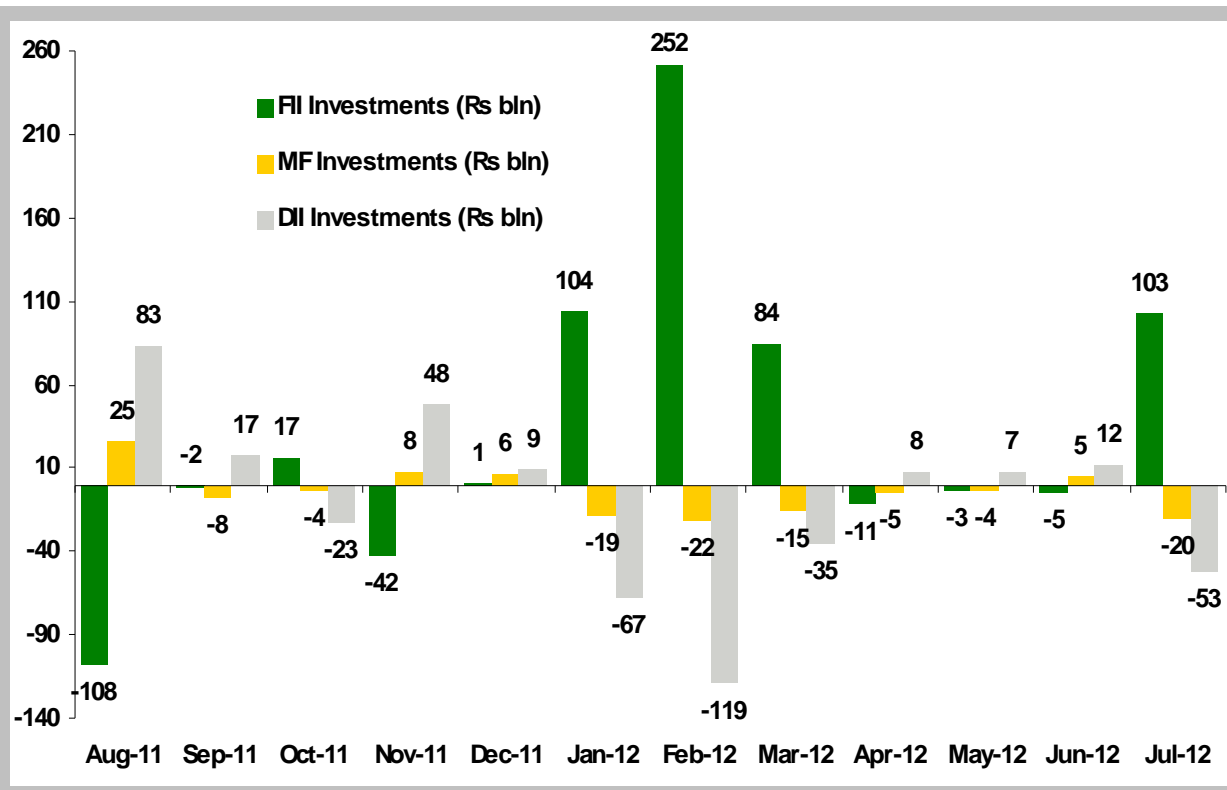
# Top Gainers / Losers - Nifty

Top Gainers for the month			
Gainers	52 week H/L	Last Price#	% Gain*
HCL Technologies	524.45 / 360	518.55	8.84%
Grasim Inds	2928 / 2015	2870.25	8.68%
Cairn India	401.1 / 249.3	333.7	8.50%
Cipla	359.95 / 272.85	338.6	6.97%
ICICI Bank	1059.7 / 641	961.4	6.88%
Top Losers for the month			
Losers	52 week H/L	Last Price#	% Loss*
Bank of Baroda	897.95 / 615	656.1	-10.48%
Infosys	2994 / 2101.25	2226.95	-11.25%
Reliance Infra.	679.75 / 328.3	494.65	-11.39%
Wipro	453 / 310.5	340.05	-14.97%
Jindal Steel	664 / 389.2	398.65	-15.24%

# closing price as on 31<sup>st</sup> July, 2012.\* one month performance as on 31<sup>st</sup> July, 2012.  
Source: Capitaline



# FII & DII Inflows



- Institutional activity picked up in July.
- FII inflows during the month were at Rs.103bn. FII inflows were at Rs.523bn for CY12 YTD after a Rs.27bn outflow in CY11 and Rs.1308bn inflow in CY10.
- MF's were net sellers at Rs.20bn, while DII's were net sellers of Rs.53bn during the month.



# Market Activity



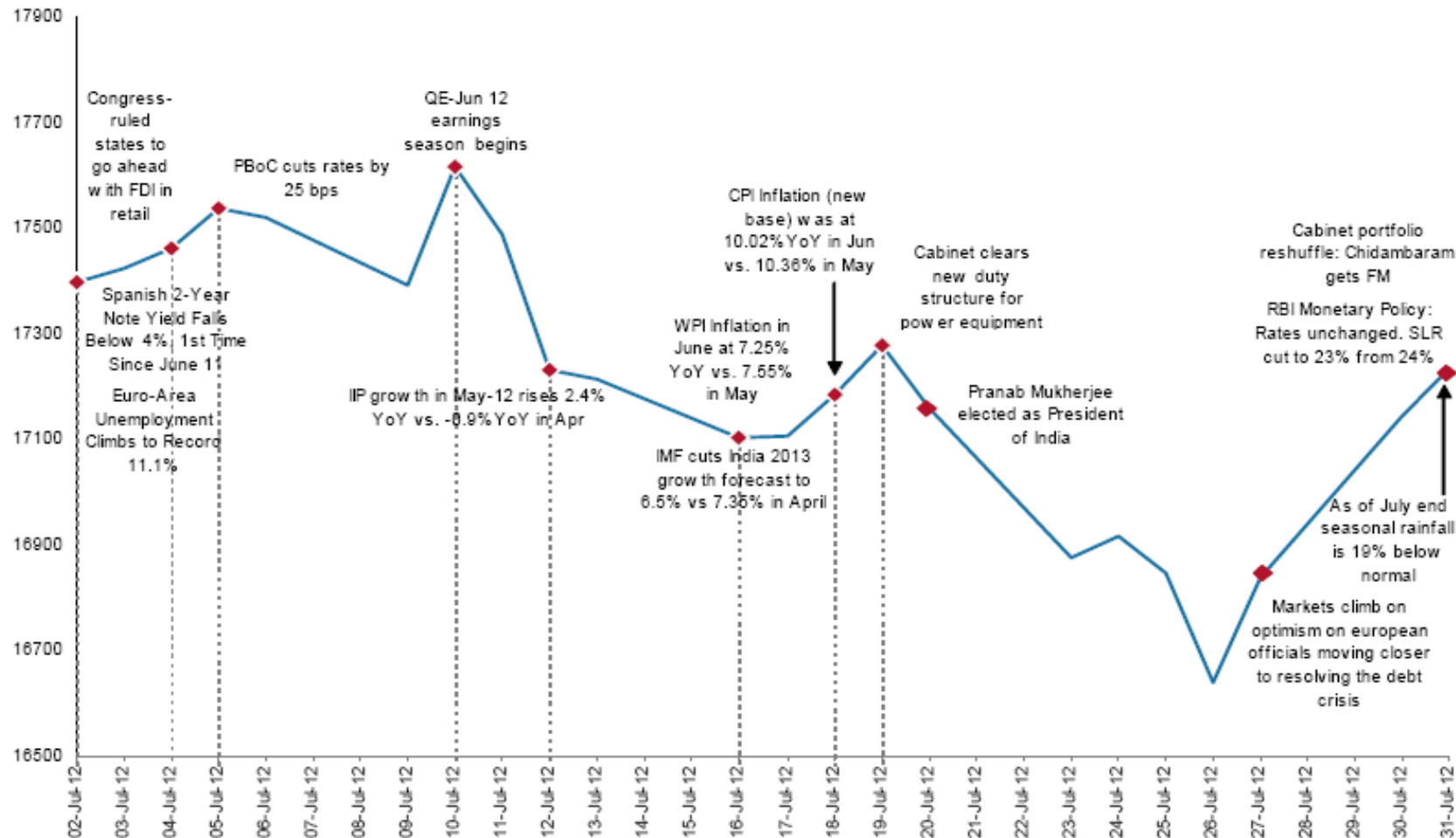
- In July 2012, cash market trading turnover increased by 11% MoM.



- At the end of July 2012, average open interest increased by 10% on a MoM basis.



# July 2012 events timeline



**Source:** Bloomberg, Economic Times, Business Standard, Morgan Stanley Research.

**Note:** The above shown index is BSE Sensex .





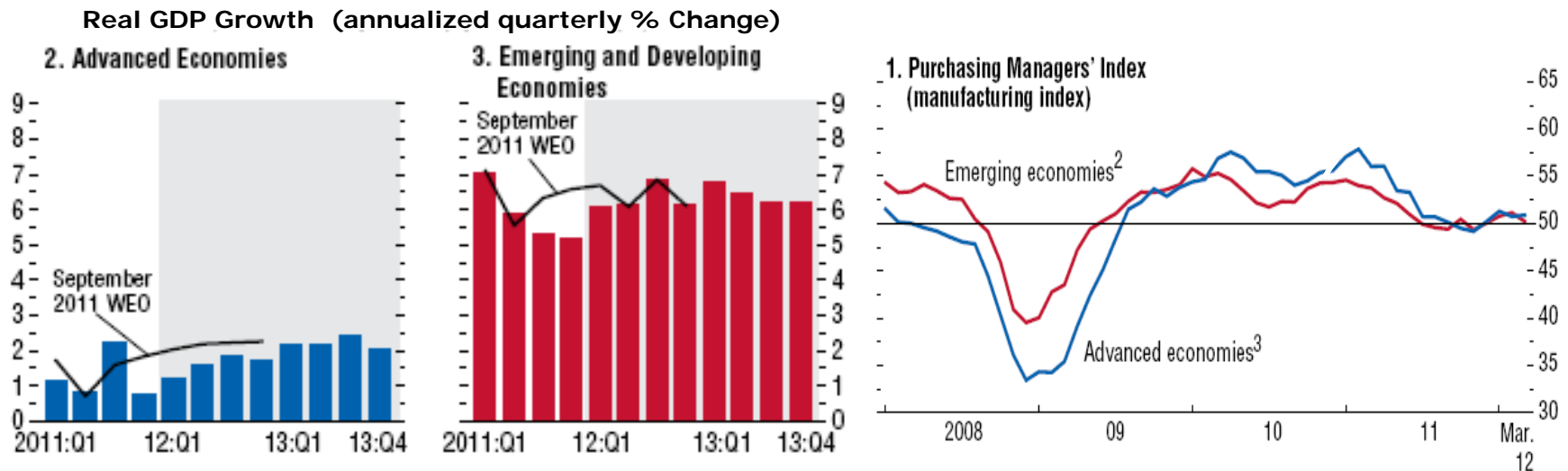
# Religare MF: Equity Market Outlook and Opportunities

# Equity Market Outlook

- The IMF has cut its global growth outlook recently, with global economic growth projected to drop from about 4% in CY2011 to about 3.5% in CY2012 because of weak activity during the second half of 2011 and the first half of 2012.
- The growth slowdown is expected to be led by Euro Area, which is expected to report a decline in GDP in CY12 (as per IMF estimates).
- India's GDP growth decelerated to just 6.5% in FY12, largely led by fall in investment demand. This in turn is affecting consumer sentiment & demand.
- Decline in capital formation is due to a multitude of reasons, prominent amongst them being policy & implementation bottlenecks and high cost of money.
- The IMD has recently forecasted poor rainfall for the remainder of monsoon season, which can potentially lead to a draught like situation. This may increase pressure on the agricultural contribution to GDP.
- In the earnings season so far, the aggregate earnings growth for Sensex companies have been in line with expectations.
- Consensus market expectations for FY13 earnings are at 14% growth, which may be difficult to achieve in the current scenario and may be moderated going forward.



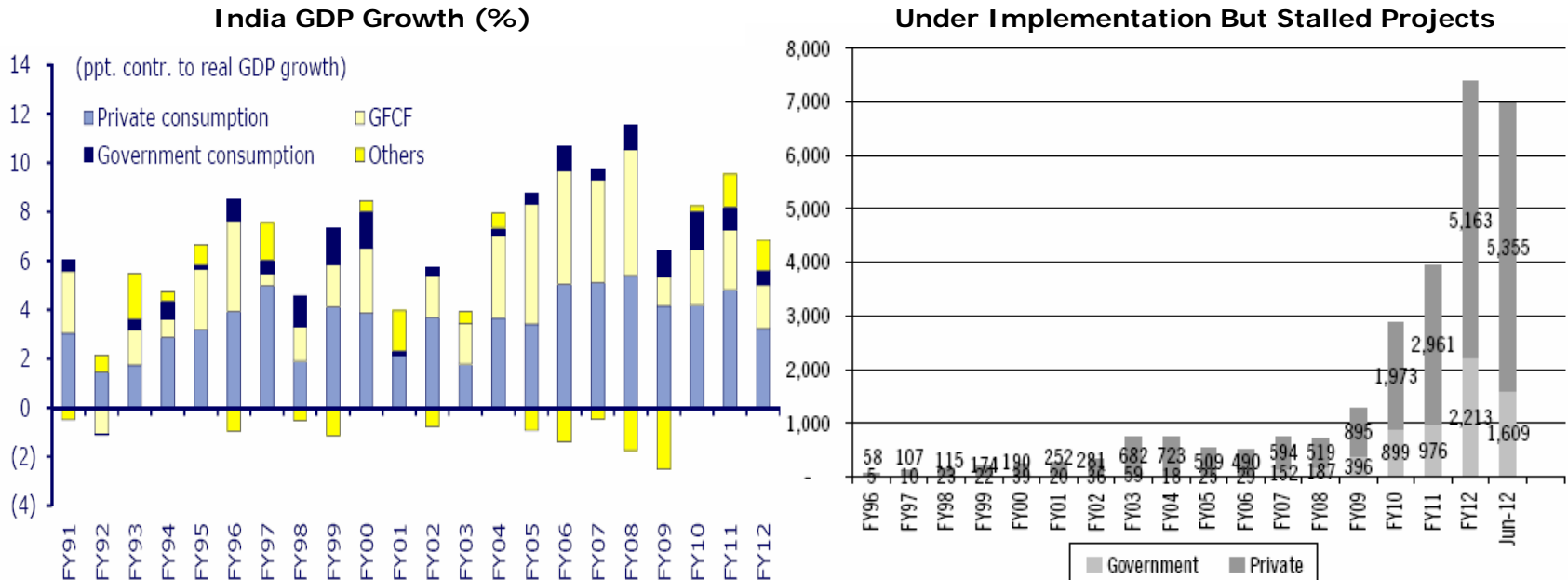
# Global Macro – IMF raises red flag on global growth



- The IMF has cut its global growth outlook recently, with global economic growth projected to drop from about 4% in CY2011 to about 3.5% in CY2012 because of weak activity during the second half of 2011 and the first half of 2012.
- The growth slowdown is expected to be led by Euro Area, which is expected to report a decline in GDP in CY12 (as per IMF estimates).
- The reacceleration of activity is expected only during the course of second half of CY2012, which in turn is expected to lead to global growth of about 4% in 2013 (as per IMF estimates).

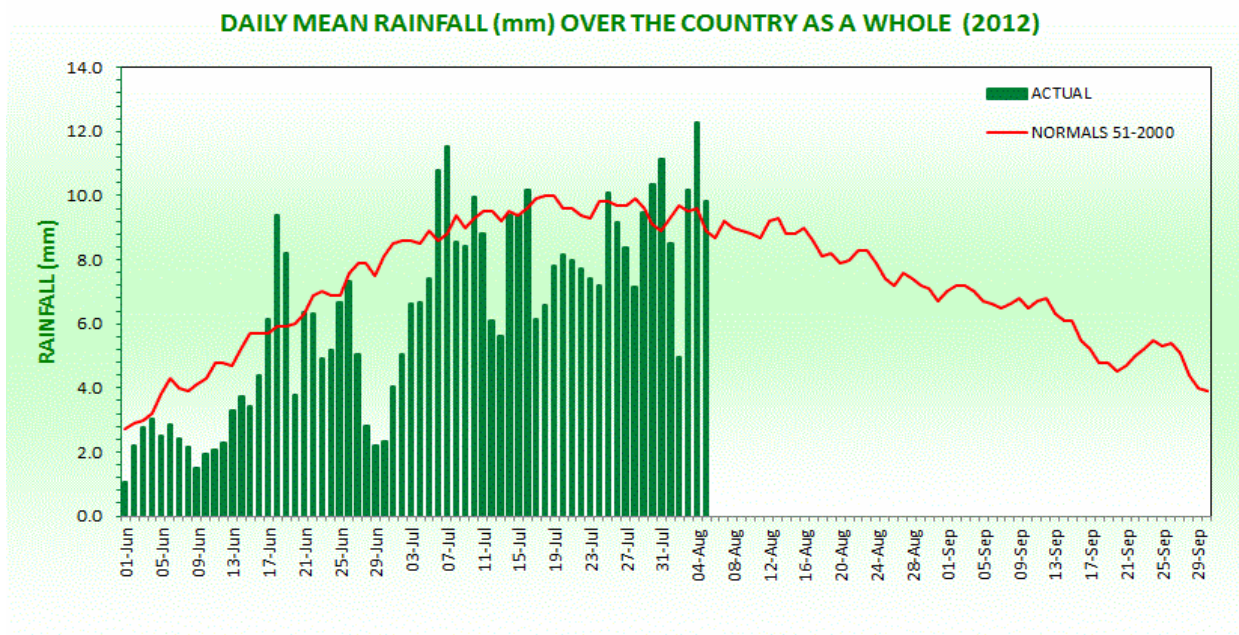


# India's GDP Growth – slowdown led by fall in investment demand



- India's GDP growth decelerated to just 6.5% in FY12, largely led by fall in investment demand. This in turn is affecting consumer sentiment & demand.
- Decline in capital formation is due to a multitude of reasons, prominent amongst them being policy & implementation bottlenecks and high cost of money.

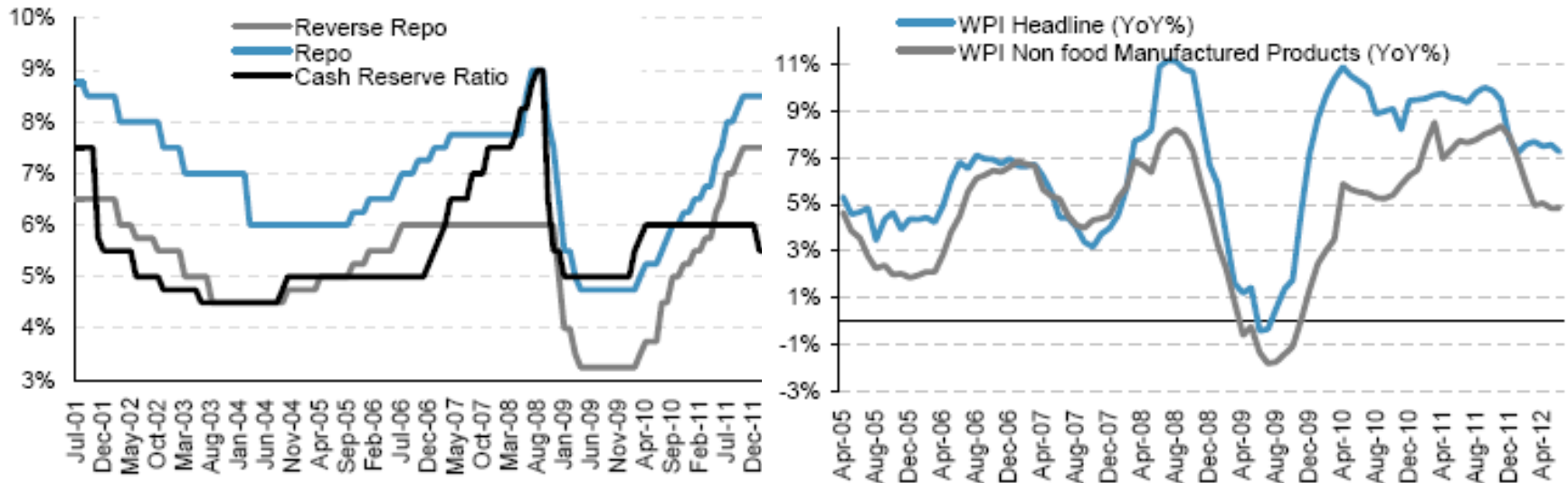
# Monsoons - IMD confirms draught like situation



- India received 19% lower rainfall than the long period average (LPA) for the first two months (June-July) of the season and even for the balance period of August and September. IMD has forecasted a 62% probability of the country's rainfall being below normal.
- This will have a follow-on impact on the winter crop and the agriculture sector output looks set for a decline in FY13.
- This will likely lead to a GDP estimates being cut to below 6% for FY13.



# RBI Policy – Hawkish stance maintained



- The Reserve Bank of India (RBI), in its quarterly review of monetary policy on July 31, kept the repo and reverse repo rates unchanged at 8% and 7%, respectively.
- RBI has reduced the statutory liquidity ratio (SLR) to 23% from 24% as a small measure to reduce funding costs for banks in times of extreme liquidity tightness.
- The RBI acknowledged that the economy is growing below potential but said that it remained concerned about inflation.
- Also the RBI reiterated that the Government must focus on fiscal control and stimulating the supply side as a precursor for any RBI action.



# Earnings Season So Far – Earnings in line with expectations

## Actual vs Expected

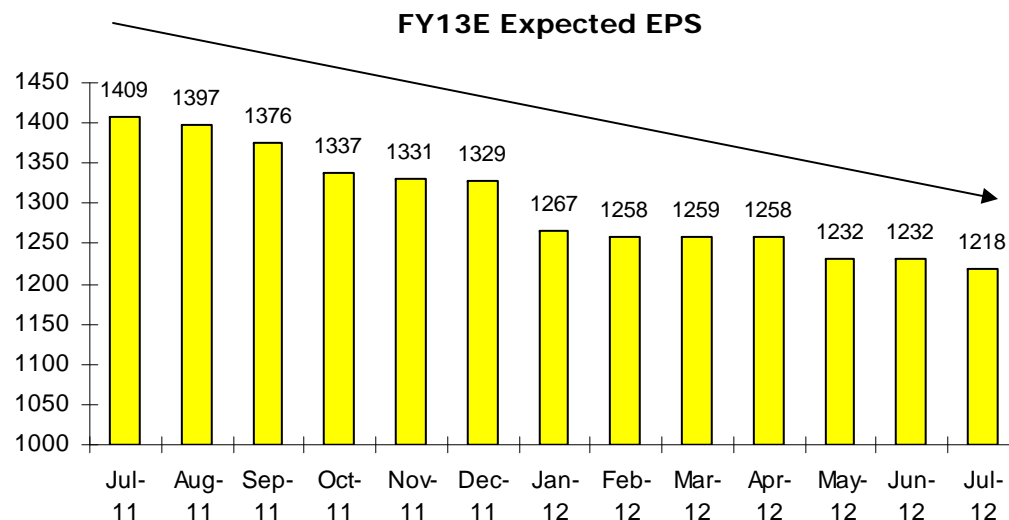
Aggregate	Sales		EBITDA		PAT		Act. Vs. Est.
	Expected	Actual	Expected	Actual	Expected	Actual	
Sensex (17/30)	11.5%	17.8%	9.6%	6.7%	13.6%	12.1%	⇔
Citi Universe	13.8%	18.6%	12.5%	11.6%	12.0%	15.5%	⇔
Citi Univ ex-Fin	13.2%	18.2%	9.5%	8.0%	9.2%	14.5%	↑
Citi Univ Ex-Energy	18.8%	20.9%	21.2%	20.2%	19.9%	20.0%	⇔
Citi Univ ex-Fin, Energy	18.5%	20.5%	21.0%	19.1%	19.2%	20.4%	⇔
Sensex ex-Energy (16/30)	18.8%	21.4%	25.4%	22.6%	25.2%	22.9%	⇔
Sensex ex-fin	11.1%	17.5%	7.5%	2.7%	11.4%	9.1%	⇔
Citi Universe ex-Metals	13.6%	18.7%	13.8%	13.3%	12.6%	16.0%	⇔
Citi Univ ex-Energy, ex-Metals	19.0%	21.3%	24.0%	23.5%	21.6%	21.2%	⇔

- With almost 17 of 30 Sensex companies having reported earnings, sales have surprised on the upside, while margins have disappointed.
- This is in line with our hypothesis that as growth slows; the battle for market share will lead to margin pressures.
- However, the reported profit growth of 12.1% is almost in line with expectations.





# Earnings Forecasts – Earnings Expectations Moderated

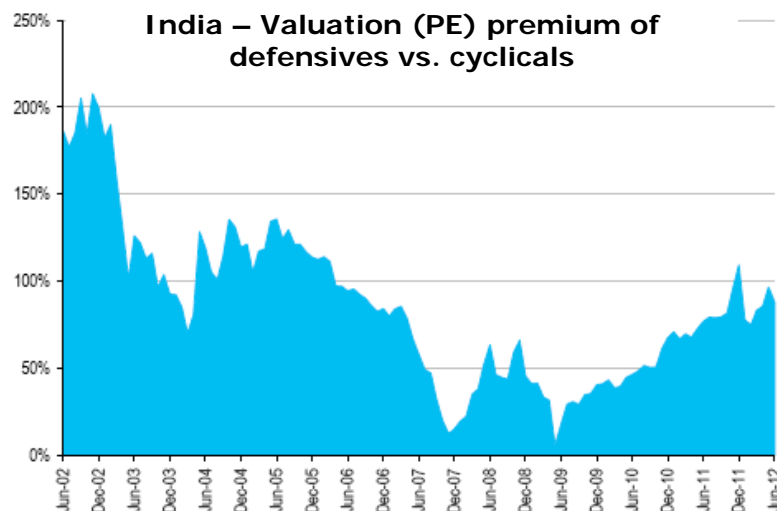


- Estimates for both FY13 and FY14 earnings have been cut by 1% each to 1218 and 1387 respectively.
- Consensus market expectations for FY13 earnings are at 14% growth, which may be difficult to achieve in the current scenario and may be moderated going forward.
- The poor monsoon may not have a significant impact on aggregate earnings forecasts though companies with higher exposure to rural markets could see pressures.

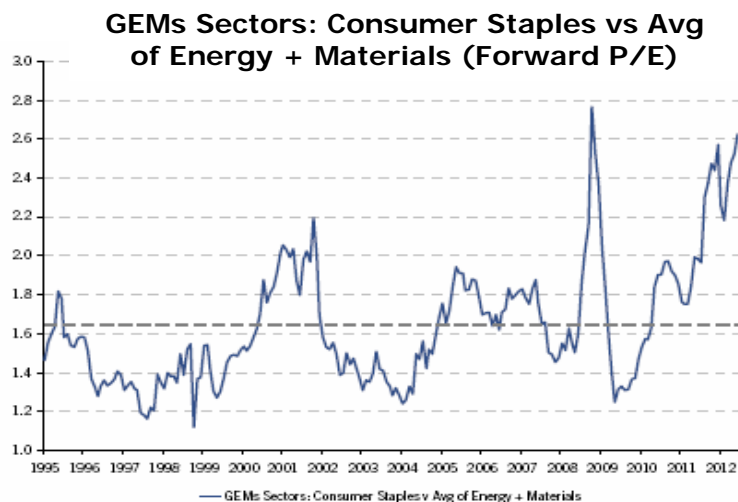




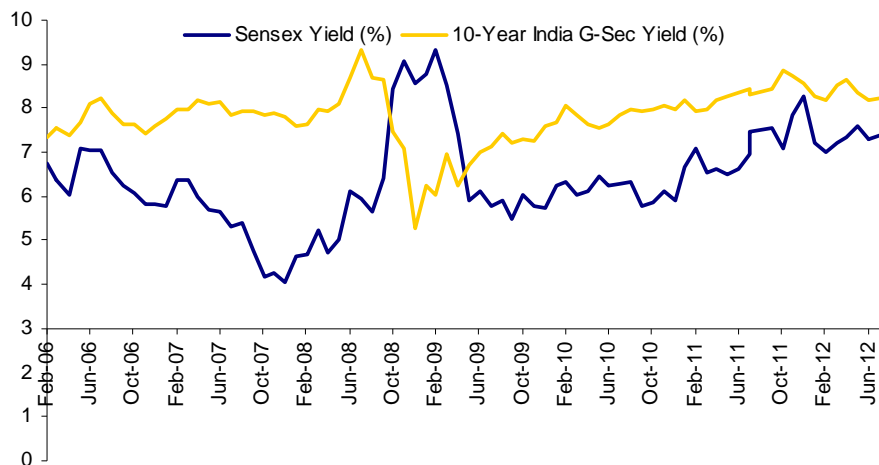
# Valuations – dichotomy between sectors



- Valuation premium of defensive vs cyclicals is currently at a 5-year high.
- This is visible in both Global Emerging Markets (GEMS) as well as India PE ratios of defensives vs cyclical sectors.
- Note: For GEMS, we have used Consumer Staples Sector as the representative of defensives and an Average Forward PE of Energy + Materials as the representative of Cyclicals.

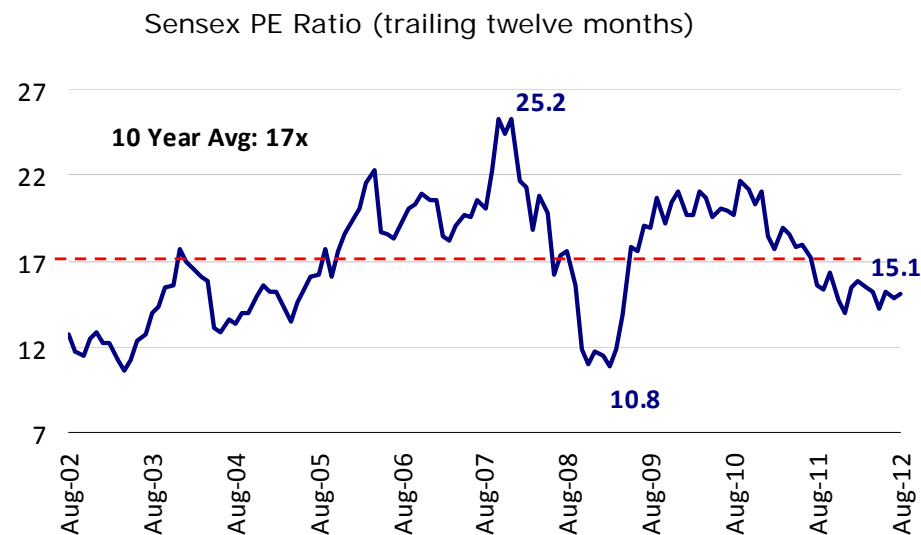


# Valuations – At Reasonable Levels



- The gap between Sensex earnings yield and bond yield has remained similar during the month as both Sensex and Bond yields have remained almost stagnant.

- Sensex is currently trading at 15.1x its trailing earnings. It is now 11% lower than its historical 10-year average trailing PE of 17x.



- On a 1-yr forward basis, Sensex is trading at 13.5x which is about 7% below its 10 year average PE.



# Looking Ahead...

- The Government has incrementally started to deliver sound bytes, which are liked by the markets. Thus, the newly appointed Finance Minister, Mr. P Chidambaram has 'talked' about reviewing retrospective taxes, reviving the investment climate and intention to reduce the fiscal deficit.
- However, we have yet to see any concrete steps being taken in the above direction and until that time, policy directions remains the key monitorable.
- Fiscal control and policy moves to boost the supply side are a precursor to any RBI action. The RBI remains concerned about inflation.
- The poor monsoon has led to cut in output forecasts for the agriculture sector and as a result GDP growth for FY13 is now forecast at 5.5-5.9%.
- The poor monsoon may not have a significant impact on aggregate earnings forecasts, but it raises the risk of higher food inflation in the months ahead. While the Government has adequate buffer stock of food grains, there could be pressures from other items such as oilseeds & pulses.
- The macro situation remains challenging. However, less cyclical components of the market are trading at rich valuations and pockets of under valuation exist in the cyclical areas.
- Hence, we are preferring to emphasize the bottom up stock selection over macro and sector views.
- 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. However, in areas where valuations already reflect a high degree of stress, we have been open to making selective investments.



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