Equity Markets :

Current Environment and Outlook

Vetri Subramaniam, Chief Investment Officer

September 2012

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Current Environment

- Global Equity markets continued to consolidate its gains in September, with the MSCI World Index rising by 2.52%
- Indian markets sharply out performed their global peers, rising by 7.65%
- Commodity prices reflected the gains in the global equity markets with the benchmark CRB Reuters Jefferies total return index rising by 0.8%
- Realty and Capital Goods were the best performing sectors, while Healthcare and FMCG sectors delivered the worst return for the month*
- FII inflows during the month were at Rs.193bn. MF were net sellers at Rs.32bn, while DII were net sellers of Rs.92bn during the month
- Trading Activity increased in September with cash market trading turnover increasing by 20% MoM. However, average open interest remained flat on a MoM basis

* 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	2086.17	1.89%	-5.15%	EM - Asia
BSE Sensex	**India**	**18762.74**	**7.65%**	**21.40%**	**EM - Asia**
Kospi	South Korea	1996.21	4.78%	9.34%	EM - Asia
Taiwan Weighted	Taiwan	7715.16	4.30%	9.09%	EM - Asia
Thailand SET 50 Index	Thailand	886.58	5.51%	23.41%	EM - Asia
Jakarta Composite Index	Indonesia	4262.56	4.98%	11.53%	EM - Asia
KLSE	Malaysia	1636.66	-0.57%	6.92%	EM - Asia
Ibovespa Sao Paulo Index	Brazil	59175.86	3.71%	4.27%	EM
Mexico IPC	Mexico	40866.96	3.67%	10.22%	EM
Russian RTS Index	Russia	1475.70	6.19%	6.79%	EM
Philippine PSEi	Philippines	5346.10	2.88%	22.28%	EM
Merval Buenos Aires Index	Argentina	2451.73	1.80%	-0.44%	EM
HangSeng	Hong Kong	20840.38	6.97%	13.05%	Developed - Asia
Nikkei	Japan	8870.16	0.34%	4.91%	Developed - Asia
Strait Times	Singapore	3060.34	1.15%	15.64%	Developed - Asia
Dow Jones	USA	13437.13	2.65%	9.98%	Developed
CAC 40 Index	France	3354.82	-1.71%	6.17%	Developed
All Ordinaries Index	Australia	4406.34	1.55%	7.18%	Developed
DAX Index	Germany	7216.15	3.52%	22.34%	Developed
Swiss Market Index	Switzerland	6495.88	1.69%	9.43%	Developed
FTSE 100	UK	5742.07	0.54%	3.05%	Developed
MSCI World Index	--	1311.50	2.52%	10.90%	--

* as on 28th September, 2012. Source: Bloomberg
EM – emerging markets, Developed – developed markets

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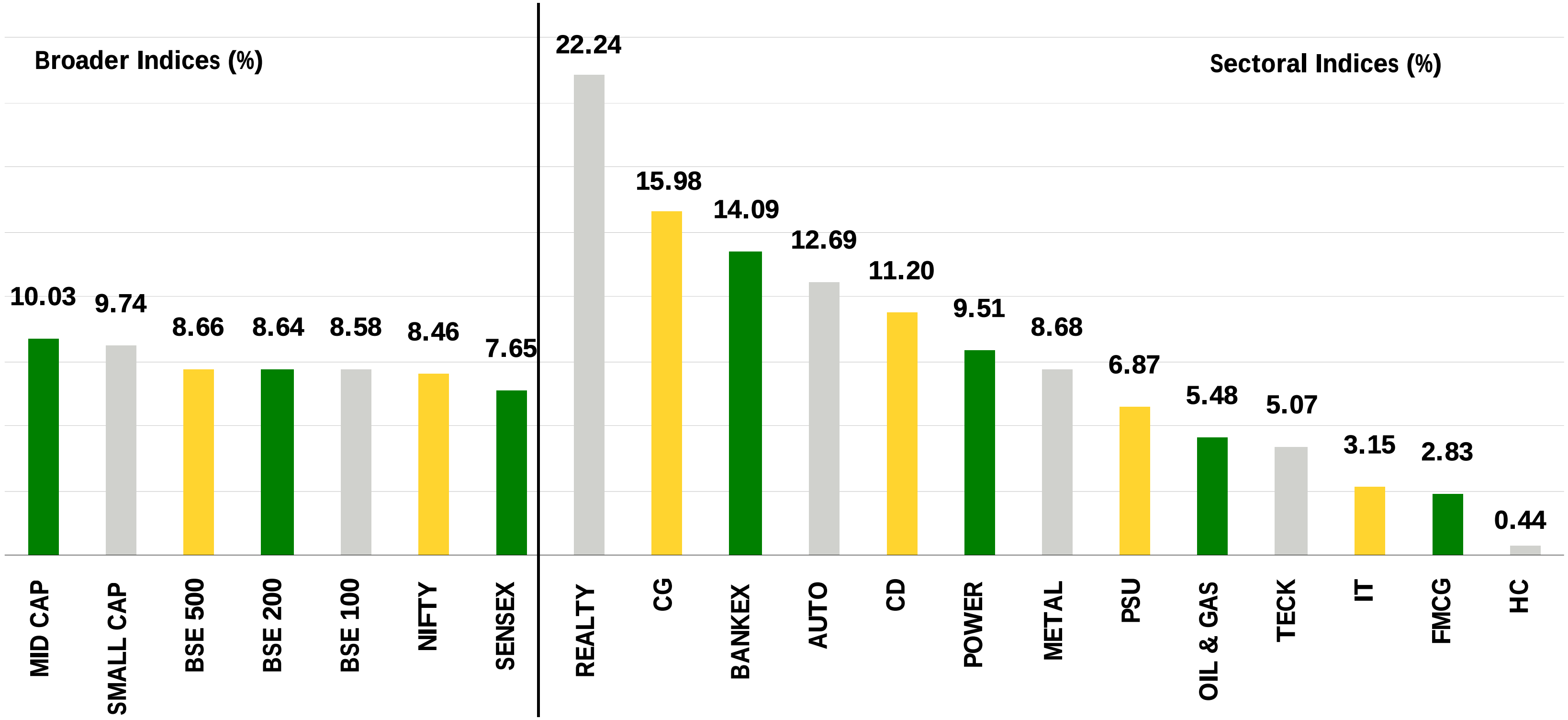
India : Sector performances



- Nifty rose by 8.46% over the previous month
- MidCaps and SmallCaps out performed LargeCaps with 10.03% rise in the MidCap index and 9.74% rise in SmallCap index
- Realty and Capital Goods were the best performing sectors
- Healthcare and FMCG sectors delivered the worst return for the month

Source: BSE,NSE. one month performance as on 28th September, 2012. 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*
JP Associates	88.95 / 50.35	82.25	27.42%
Bank of Baroda	881 / 605.55	797.80	26.26%
Punjab Natl.Bank	1091.05 / 659.2	840.30	24.20%
St Bk of India	2475 / 1571.1	2240.60	21.95%
Jindal Steel	664 / 320.4	427.15	21.30%
Top Losers for the month			
Losers	52 week H/L	Last Price#	% Loss*
Sesa Goa	270 / 148.3	171.20	-0.15%
Dr Reddy's Labs	1815.85 / 1440.8	1645.65	-1.90%
Cairn India	401.1 / 258	331.05	-2.65%
TCS	1439.8 / 1015.3	1295.90	-3.56%
Ranbaxy Labs.	578.4 / 365.5	529.75	-3.98%

closing price as on 28th September, 2012.* one month performance as on 28th September, 2012.
Source: Capitaline

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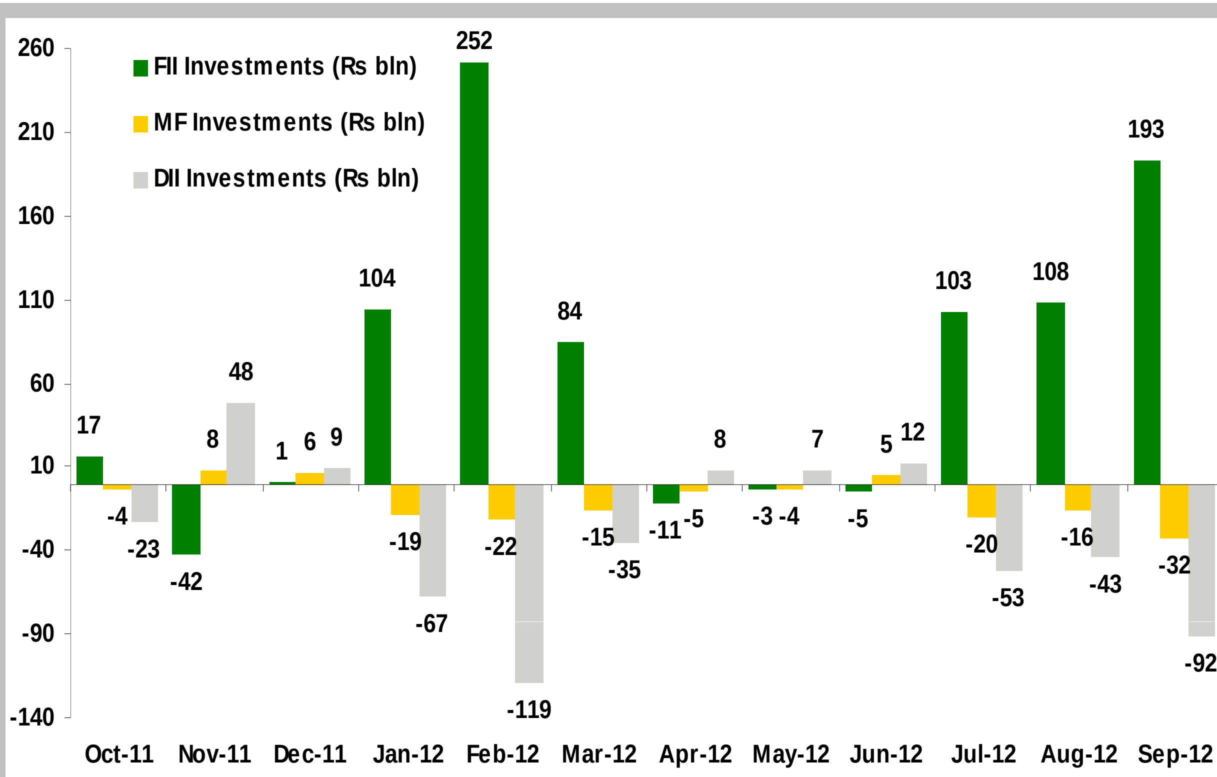
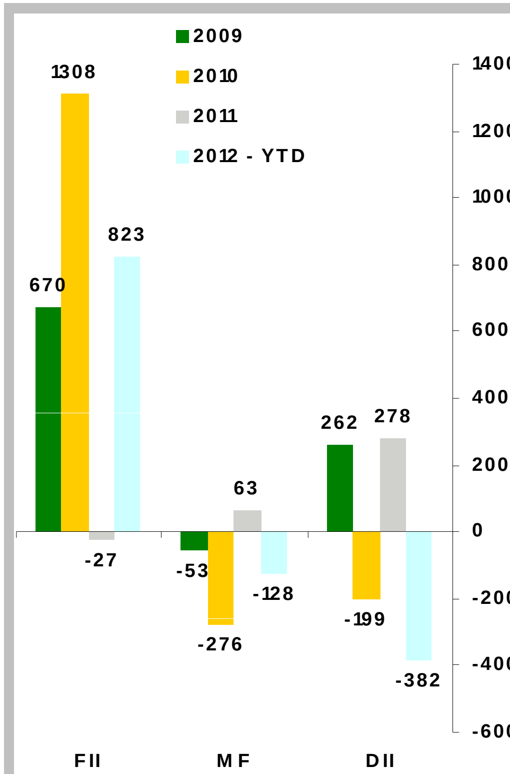
FII & DII Inflows





- Institutional activity remained upbeat in September
- FII inflows during the month were at Rs.193bn. FII inflows were at Rs.823bn for CY12 YTD after a Rs.27bn outflow in CY11 and Rs.1308bn inflow in CY10
- MF were net sellers at Rs.32bn, while DII were net sellers of Rs.92bn during the month

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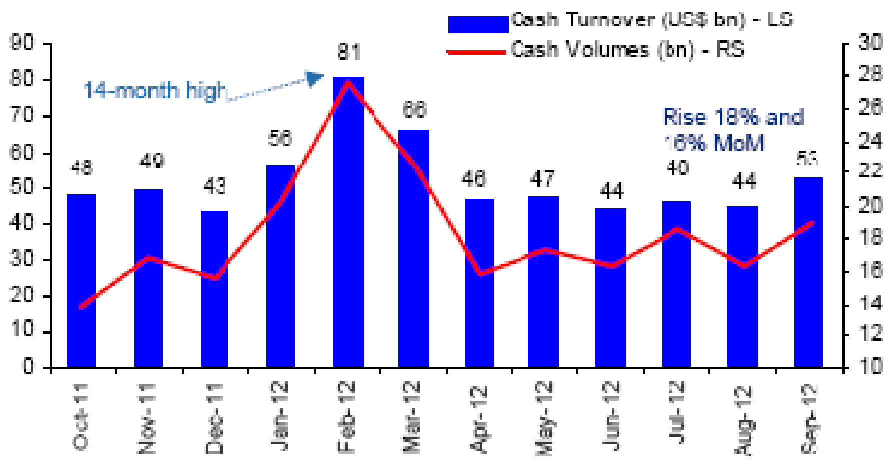
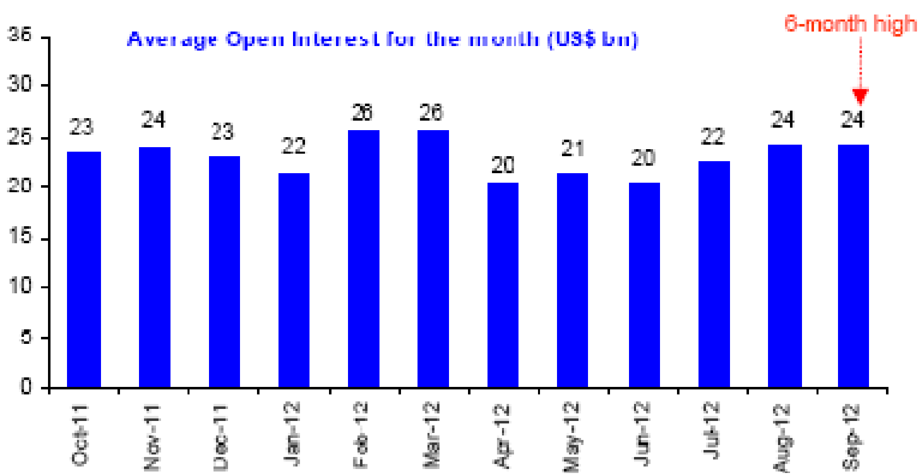
FII - Foreign Institutional Investors, DII - Domestic Institutional Investors (Includes Bank, DFIs, Insurance and MF)
Source: SEBI, BSE

Market Activity





- In September 2012, cash market trading turnover increased by 20% MoM
- At the end of September 2012, average open interest remained flat on a MoM basis

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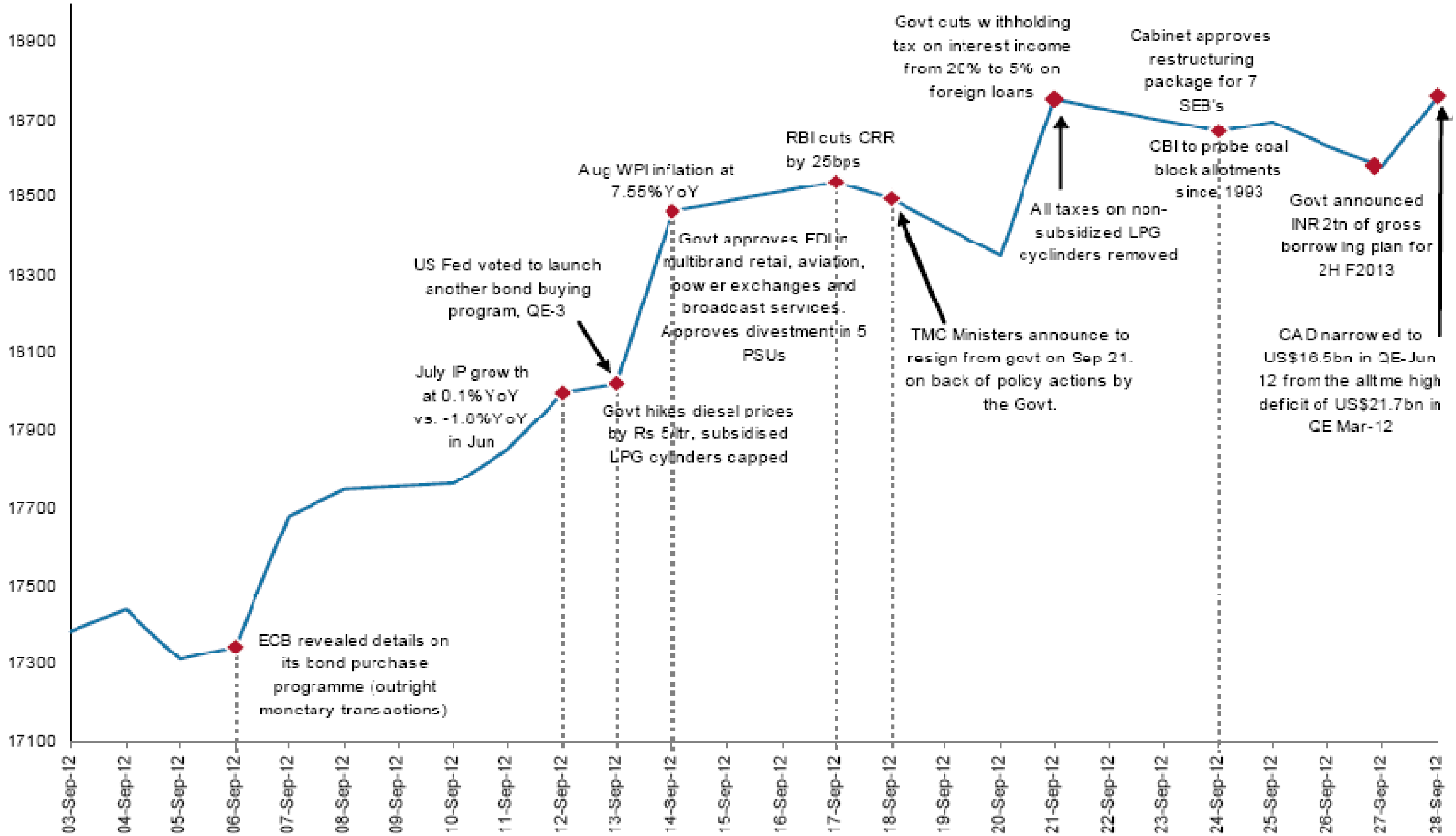
Sources: Bloomberg, Morgan Stanley

September 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

- Global economic growth is sluggish. Both the US FED and ECB have announced practically unlimited quantitative easing or refinancing of assets to keep their respective economies on liquidity support

- India's GDP has been mirroring global growth trend with Q1FY13 growth at 5.4%, slightly better than the 5.3% reported in Q4FY12

- One of the biggest concerns dogging the Indian economy is lack of investment demand. New project announcements in 2QFY13 caved in. New project announcements declined by a massive -75% QoQ and - 75% YoY in 2QFY13

- The government has unveiled a slew of reforms aimed at kick starting, by opening up sectors such as Retail, Aviation & Insurance to further FDI. An attempt has also been made to rein in fuel related subsidies

- The currency markets have also responded positively to this move, with the Rupee gaining 5.2% this month. The gain in the rupee dampens inflationary pressure and also reduces fuel related subsidies

- But in order to revive growth the crucial challenge is to revive the investment cycle while keeping a lid on the fiscal situation

- India's 2QFY13 earnings growth should be steady with Sensex ex-oil earnings growing by about 10% YoY, largely in line with the last four quarters earnings trajectory

- Consensus expectations for FY13 earnings growth are at about 10% growth, which appears reasonable

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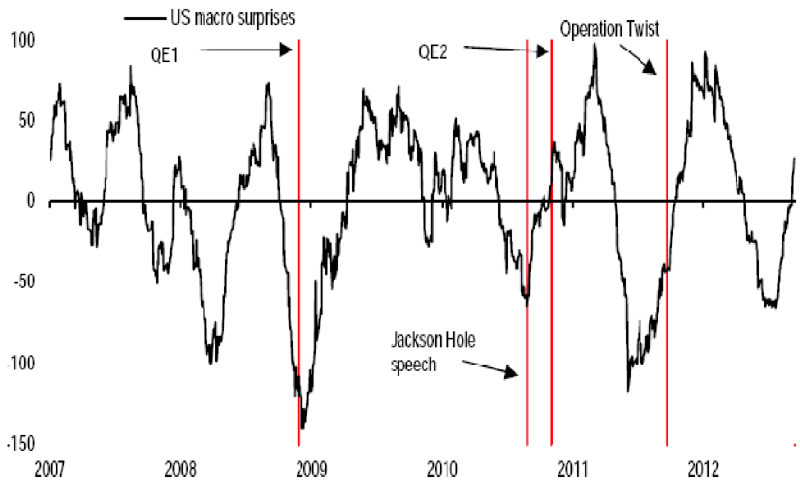
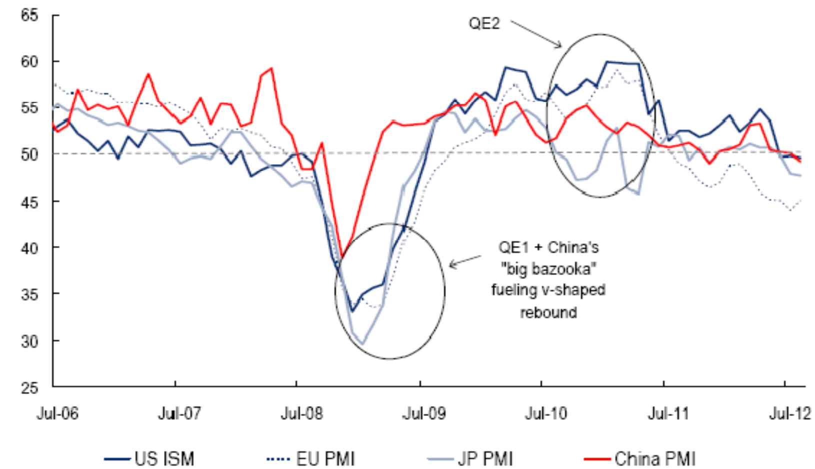
Source: RMF, FactSet, IBES Estimates, Morgan Stanley Research, Citi Research

Global Macro – Massive quantitative easing underway!

US Macro Surprises Index



Global PMI Index



- Its raining dollops of liquidity with both the US FED and ECB having announced practically unlimited quantitative easing or refinancing of assets
- While such steps lead to an immediate booster dose for both the markets as well as the economy, past history suggests its impact has not remained sustainable, with both the economy and markets faltering after an initial round of exuberance

Source: Thomson Reuters, Credit Suisse research, CEIC Data Company Ltd., Citi Research Estimates

India's GDP Growth – slowdown continues

- India's GDP growth for Q1FY13 was at 5.4%, slightly better than the 5.3% reported in Q4FY12
- Both the agriculture and industrial growth were higher on a sequential basis, but are expected to slow down in the near term due to poor monsoons and subdued investment demand respectively
- Also while the GDP growth is slightly better than expected, the slowdown in services is concerning and can lead to further slowdown in the near future

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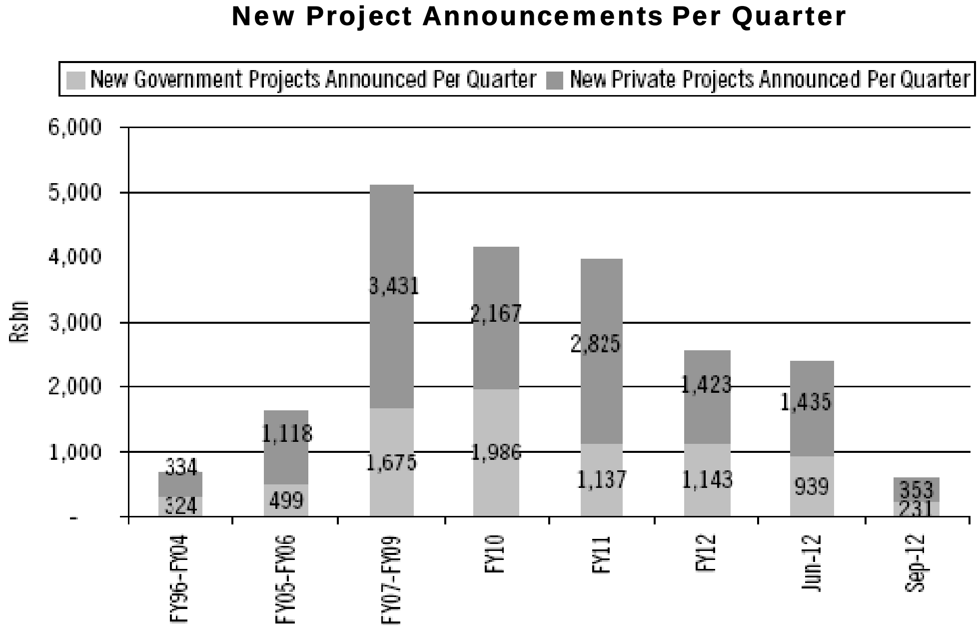
Source: Religare Capital Markets Research

Capex Cycle – are we closer to trough?



- New project announcements in 2QFY13 caved in. New project announcements declined by a massive -75% QoQ and - 75% YoY in 2QFY13
- The fall is equally sharp in both private and government projects
- A pickup in new projects and ultimately the investment cycle is the key to a meaningful revival in the Indian economy

Source: Centre for Monitoring Indian Economy, Citi Research

Reforms – biggest political gamble in recent times

- Government has finally tried to revive the animal spirits of the economy by unleashing long pending and much needed reforms booster
- In Phase 1 it announced prudent fiscal (Diesel hike, disinvestment), and investor-friendly measures (FDI in retail, aviation and broadcasting)
- In Phase 2 the cabinet cleared a slew of bills like
  - Insurance Laws (Amendments) Bill (hiking FDI limit to 49%)
  - Pensions Bill (hiking FDI limit to 49%)
  - Companies Amendments Bill
  - Forward Contract Amendment Bill
  - Amendments to the Competition Act
- The Kelkar committee appointed by the government to review the fiscal situation has made a strong case for fiscal controls & reducing the deficit. However the willingness to take hard decisions on the fiscal front is limited by the fluid political situation
- A few of the above reforms require parliamentary approval and hence can meet strong resistance from opposition parties. However, the government has clearly signaled its intent and urgency to embrace reforms
- The UPA government now has to rely on outside support to continue to remain in power. The government has taken one of the biggest political gamble in recent times
- While the decisions must be applauded we also recognize that political risk has now escalated

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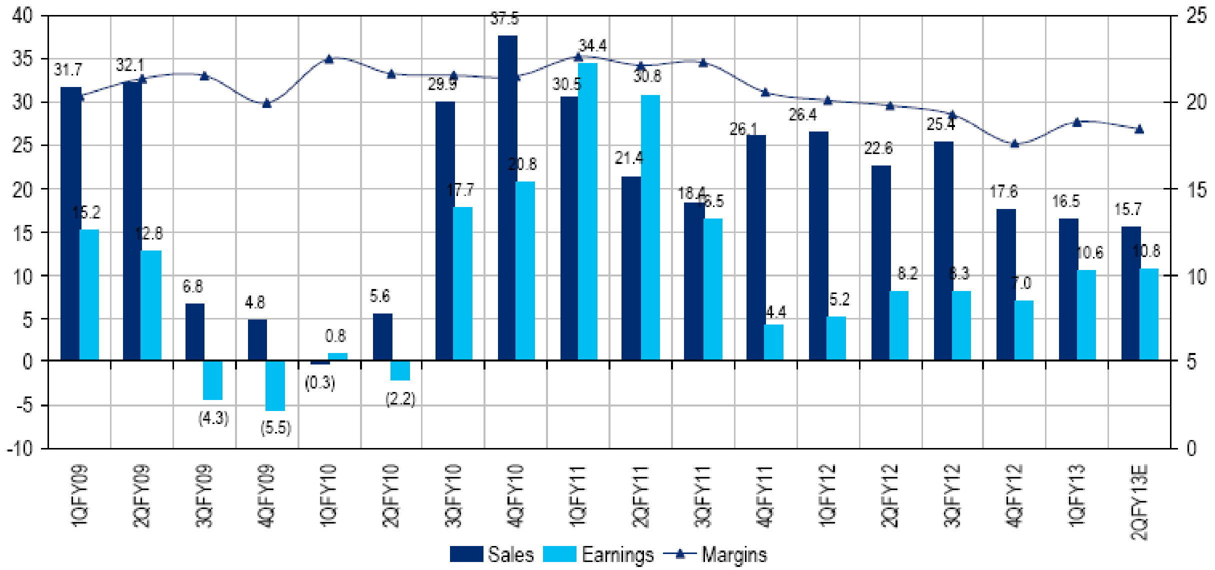
Sept 2012 Earnings – growth similar to June'12 qtr expected

Sensex ex-oil sales growth, earnings growth and EBITDA margin trends



- India's 2QFY13 earnings growth should be steady: + 10% YoY (Sensex ex-oil), largely in line with the last four quarters earnings trajectory
- Margins are expected to decline marginally driven by softness in sales

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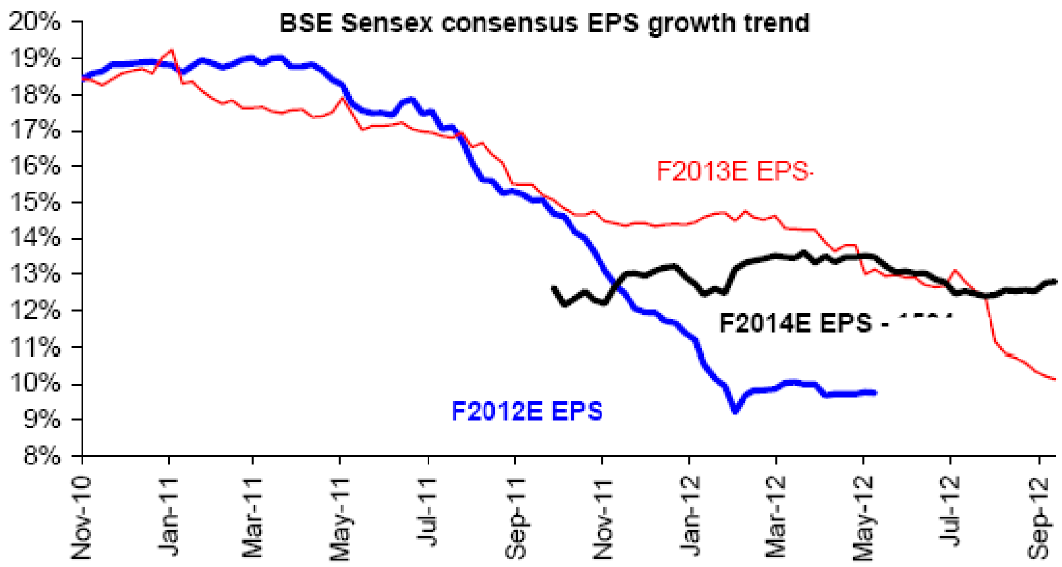
Sources: Company data, Citi Research

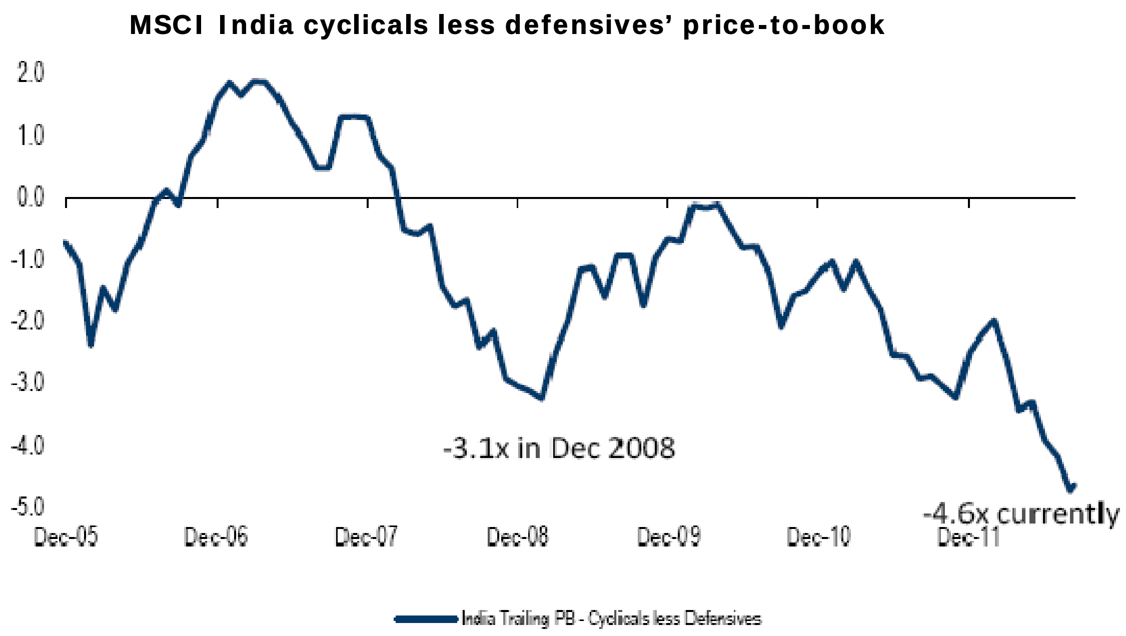
Earnings Forecasts – Earnings Expectations Moderated



- Consensus expectations for FY13 earnings growth are at about 10% growth, which appears reasonable
- Though the poor monsoon may not have a significant impact on aggregate earnings forecasts, however companies with higher exposure to rural markets could see pressures

Sources: FactSet, IBES Estimates, Morgan Stanley Research

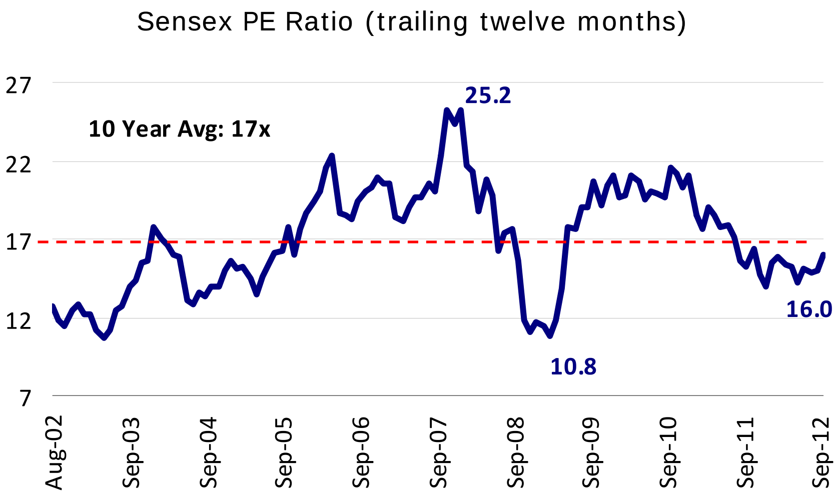
Valuations – dichotomy between sectors continues

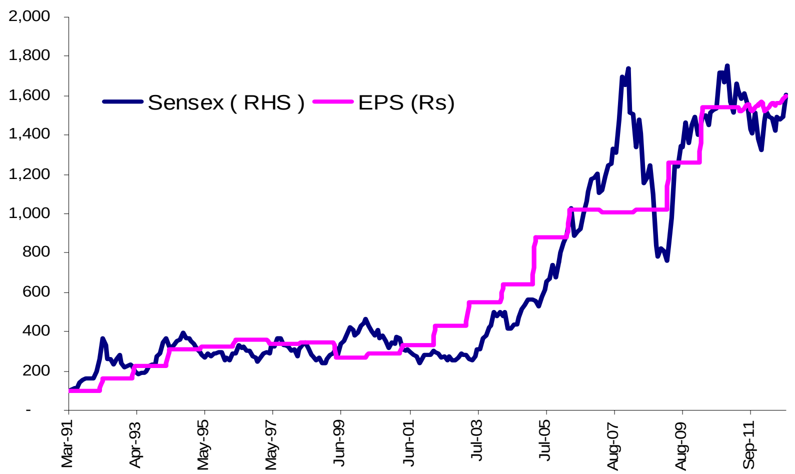


- In the last two years, globally cyclicals have underperformed the defensives. However, the problem is more pronounced in India
- In India, the price-to-book gap between cyclicals and defensives is 4.6x versus 3.1x at the 2008 lows

Source: Factset, MSCI, Morgan Stanley Research

Valuations – At Reasonable Levels





- Sensex is currently trading at 16x its trailing earnings. It is now 6% lower than its historical 10-year average trailing PE of 17x
- On a 1-yr forward basis, Sensex is trading at 14.4x which is about 0.5% below its 10 year average PE
- The derating 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

Source: Bloomberg; MOSL

Looking Ahead...

- Liquidity is expected to increase sharply post the US FED and ECB announcing practically unlimited quantitative easing or refinancing of assets for their respective economies
- The Government has finally tried to unleash the animal spirits of the economy by unleashing the long pending and much needed reforms booster. We feel these actions have strong signaling intent to the investment community
- It has also taken a large political gamble as one of its key ally Trinamool Congress has withdrawn support to the Govt., which is now relying on outside support to continue its term
- Fiscal control and policy moves to boost the supply side are a precursor to any RBI action. The RBI remains concerned about inflation
- 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
- September witnessed a role reversal with cyclical business and companies with weaker balance sheets out performing their sounder peers
- Valuation discount to long term averages has compressed and is no longer as attractive as it was earlier this year. But valuations remain in the comfort zone
- 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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Get In Touch

Corporate Office:
Religare Asset Management Company Limited
3rd Floor, GYS Infinity, Paranjpe 'B' Scheme, Subhash Road,
Vile Parle (East), Mumbai - 400 057
T +91 22 67310000 F +91 22 28371565

Call: 1800-209-0007 > sms 'Invest' to 56677
www.religaremf.com

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