Top 10 Issues For 2014

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Performance of Major Asset Classes in 2013

G-Sec Yield	(%)
31-Dec-2012	8.108
31-Dec-2013	8.825
*Data from Bloomberg	

Commodity	(%)
Gold	-4
Silver	-23

International Indices	Return (%)
S&P BSE SENSEX	9
CNX Nifty Index	7
Dow Jones	26
NYSE	23
Nasdaq	38
Hang Seng	3
KLSE Composite	11
CAC 40	18
DAX	25
FTSE 100	14
Shanghai Composite	-7
Bovespa	-15
Jakarta Composite	-1
Nikkei 225	57
Seoul Composite	1
RTS Index	-6

Indices	Return (%)
S&P BSE AUTO Index	7
S&P BSE BANKEX	-9
S&P BSE Capital Goods	-6
S&P BSE Consumer Durables	-25
S&P BSE FMCG	11
S&P BSE Health Care	23
S&P BSE IT	60
S&P BSE METAL Index	-10
S&P BSE Mid-Cap	-6
S&P BSE OIL & GAS Index	4
S&P BSE PSU	-19
S&P BSE Realty Index	-32
S&P BSE SENSEX	9
S&P BSE Small-Cap	-11
S&P BSE 100	6
S&P BSE 200	4
S&P BSE 500	3
S&P BSE TECk Index	47
S&P BSE Power Index	-15
S&P BSE IPO Index	-18

Portfolio Flows

DII and FII Net Investment in 2013 (Rs Crore)

Month	FII-Equity	FII-Debt	FII-Total	DII (BES+NSE)*
Jan-13	22,059	2,947	25,006	-17,542
Feb-13	24,439	21,326	28441	-8,819
Mar-13	9,124	5,795	14,919	-7,872
Apr-13	5,414	5,334	10,749	-2,701
May-13	22,169	5,969	28,138	-12,048
Jun-13	-11,027	-33,135	-44,162	8,427
Jul-13	-6086	-12038	-18124	-1,541
Aug-13	-5,923	-9,773	-15,695	6,285
Sep-13	13,058	-5,678	7,380	-9,130
Oct-13	15,706	-13,578	2,128	-12,411
Nov-13	8,116	-5,984	2,133	-9,147
Dec-13**	16,086	5,290	21,376	-7,586
TOTAL	113,136	-50,848	62,288	-74,085

SEBI website; *bseindia.com ; **Provisional data subject to change

FII Investment Activity Equity (Rs Crore)

	Equity	Debt	Total
2013*	113,136	-50,848	62,288
2012	128,361	34,989	163,350
2011	-2,714	42,067	39,353
2010	133,267	46,408	179,675
2009	83,424	4,563	87,988
2008	-52,987	11,772	-41,216
2007	71,486	9,429	80,915
2006	36,540	4,049	40,589
2005	47,182	-5,518	41,664
2004	39,205	3,080	42,285
2003	30,459	4,694	35,154
2002	3,630	48	3,678
2001	13,128	171	13,300

SEBI Website; *provisional data for 2013

Top Ten Themes

1. Elections
2. Inflation
3. Taper
4. Infrastructure
5. Fiscal Deficit
6. RBI Actions/Bank Licenses
7. What will retail investors do?
8. Technology stocks
9. Midcaps
10. Interest Rates

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1. ELECTIONS

- General Elections
  Anti-Congress sentiments were reflected in the state elections of December 2013.
- However, AAP (Aam Admi Party) has the potential to convert the General Elections of May '14 from a bipolar fight to a triangular contest
- 3 Scenarios are likely:

Hung Parliament or 3rd Front forms the government

Indian National Congress led UPA wins with majority

BJP led NDA wins with majority

ELECTIONS

- A decisive majority will be a positive for the markets
- There could be a lot of volatility leading up to and closely following the election verdict.
- State Elections due in 2014
  - Andhra Pradesh, Arunachal Pradesh, Chattisgarh, Haryana, Maharashtra, Odisha and Sikkim
  - The important ones are Andhra Pradesh (LS-42 seats), Maharashtra (LS-48 seats), Haryana (LS-10 seats) and Odisha (LS-21 seats)

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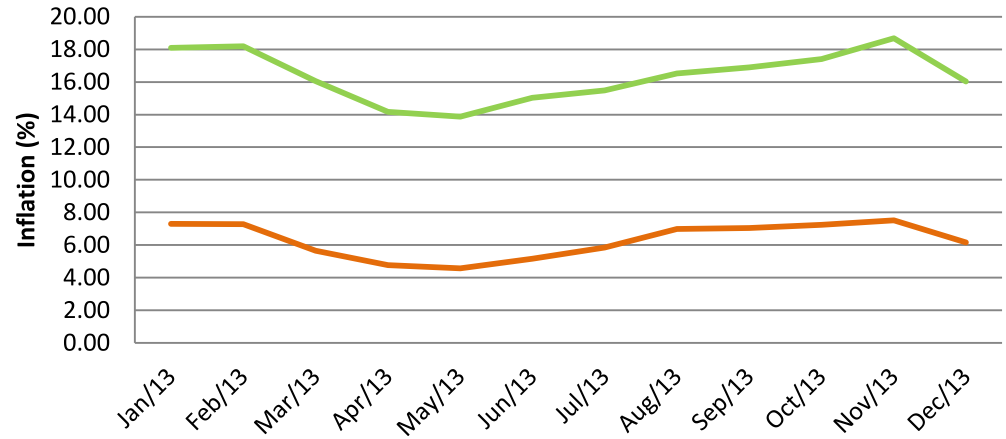
2. INFLATION

- India currently has the highest inflation rate in Asia

- The major reasons for high inflation have been rise in vegetable prices and a massive rupee depreciation seen in 2013.

- Factors which may keep inflationary pressures high:
  - Hike in administered fuel prices by the government
  - Rupee Depreciation
  - Supply-side shortages

INFLATION TREND-2013



	Jan/13	Feb/13	Mar/13	Apr/13	May/13	Jun/13	Jul/13	Aug/13	Sep/13	Oct/13	Nov/13	Dec/13
CPI	10.79	10.91	10.39	9.39	9.31	9.87	9.64	9.52	9.84	10.17	11.16	9.87
WPI	7.31	7.28	5.65	4.77	4.58	5.16	5.85	6.99	7.05	7.24	7.52	6.16

- The Wholesale Price Index (WPI) rate reversed its declining trend and started increasing steadily from May to November
- The retail inflation or CPI also was on a declining trend between February to May after which it steadily accelerated from May to November.

2. INFLATION…………..Outlook

Agency	WPI Projection	CPI Projection
Goldman Sachs	6.5%	9.7%
FICCI	6%	
World Bank	5.3%	

- The RBI is likely to shift its focus from WPI to CPI as is the practice in most developed economies.
  - Urjit Patel Panel has proposed targeting inflation at 8% in the next 12 months, 6% in 24 months and @ 4% with a band of 2% thereafter.
- Inflation is likely to moderate in 2014 due to:
  - Base effect
  - Better fiscal and external account management
- This view will be negated by:
  - Sharp rise in crude prices
  - Populist measures by the new Government
  - Sudden surge in economic activity leading to liquidity constraints in the short term

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3. TAPER

- When the US Federal Reserve first indicated cutting down its massive stimulus programme in May the emerging market currencies were hit badly and there was foreign investment pull back
- The US GDP grew at its fastest rate in 2 years in the third quarter at 4.1% annualised rate.
- On December 18, the Fed finally announced its first reduction from $85 billion to $ 75 billion a month January onwards. It also promised to keep interest rates at record-low levels between 0 to 0.25% at least as long as unemployment is above 6.5% and inflation remains 0.5% above or below 2%..
- Many experts believe that the QE taper may continue and will be over by the end of 2014. However, uncertainties remain because the extent will depend on employment and inflation data
- Janet Yellen will take charge as the Fed Chairman from 1st February 2014.
  - Her priority will be to keep inflation and unemployment low. Many experts believe that since inflation is already below the Fed target of 2% Yellen may not rush as far as tapering is concerned.

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4. INFRASTRUCTURE

- Infrastructure investment of Rs 65 lakh Crore (or $1 trillion) is targeted over the duration of the Twelfth Five Year Plan in order to sustain a real GDP growth rate of 9%. However, government has fallen short of implementation goals
  - The percentage of total projects delayed on account of land acquisition-related issues more than trebled to 11.3 percent as of March 2013 from six years ago
  - It takes about 295 days to acquire or lease public land in India, more than twice the global average
- The government's Cabinet Committee on Investment (CCI), set up by Prime Minister Manmohan Singh in January, was charged with solving inter-departmental disputes and speeding up clearances, especially environment and fuel permits.
- Government has also liberalised foreign direct investment (FDI) norms.

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PROJECT CLEARANCES BY CCI

	NO OF PROJECTS	NO OF ISSUE	INVESTMENTS WORTH (RS IN CRORE)
Projects accepted	400	943	1,800,000
No action required	20	138	202,000
All issues resolved	122	181	401,101
Projects under consideration	227	418	970,191
Projects to be considered	28	201	243,066

SECTOR	CLEARED PROJECTS	INVESTMENTS (RS IN CRORE)	PROJECTS AWAITING APPROVAL	INVESTMENTS (RS IN CRORE)
Power	82	341,924	78	494,464
Shipping	3	1,802	13	21,341
Oil & Gas	5	4,199	38	236,880
Steel	3	3,259	27	408,979
Roads	4	4,454	28	39,000
Railways	3	7,116	21	38,015
Coal	18	10,839	42	24,777
Mines	1	7,009	6	37,399

Source: Economic Times

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Views on CCI’s effectiveness

- Vinayak Chatterjee, head of the Feedback Infra Consultancy, said the clearances were a positive step, but resistance from ministries keen to guard their veto rights has watered down the CCI's powers.
  - He also feels that the second phase of Indian infrastructure building will start in the next couple of years with long-term stable investors and that the real action will begin after the elections
- According to Barclays, “While the CCI has cleared the projects, there is no clear uptick in activity related to such projects”

5. FISCAL DEFICIT

- According to CRISIL, the government will overshoot its 4.8 per cent fiscal deficit target
- The fiscal deficit touched 94% of the budget estimate of Rs. 5.42 lakh crore at the end of November
- The government has so far received Rs 3,000 crore from disinvestment as against the budget target of Rs 40,000 crore
- Net tax receipts in the April-November period stood at Rs 5.02 lakh crore, 47.6% of the estimated revenue.

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6. RBI ACTIONS

- The repo rate was on a downward trajectory in the beginning of 2013 with RBI slashing rates by 25 basis points thrice – in January, March and May.
- However, following the US Fed's announcement on QE taper in May the Rupee depreciated sharply and impacted bond markets significantly, hence RBI had to intervene with extraordinary measures.
  - July 15: The following measures were announced:
    - The Marginal Standing Facility (MSF) was recalibrated at 300 basis points above the policy rate, making it 10.25 per cent.
    - The overall allocation to Liquidity Adjustment Facility (LAF) was capped at 1 per cent of the Net Demand and Time Liabilities (NDTL) of the banking system or Rs. 75,000 crore
  - August 20: RBI announced the following:
    - Repurchase of government bonds to make cash available
    - Regulations required banks to bring down their statutory liquidity ratio (SLR) securities in held to maturity (HTM) category from 25% to 23% of their NDTL in a required time frame. This requirement was relaxed by allowing banks to retain SLR holdings in HTM category

      at 24.5%

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6. RBI ACTIONS…..contd

  - Banks were allowed to transfer SLR securities to HTM category from available for sale (AFS) / held for trading (HFT) categories up to the limit of 24.5 per cent as a one-time measure
  - Banks were allowed to spread over the net depreciation on account of MTM valuation of securities held under AFS/HFT over the remaining period of the current financial year
- On August 29, RBI opened a forex swap window for public sector oil marketing companies (OMCs) in order to curtail volatility of exchange rate
- In his first monetary policy review Dr. Raghuram Rajan in September decided to begin rolling back some extreme measures:
  - Reduced the marginal standing facility (MSF) rate by 75 basis points from 10.25% to 9.5 %
  - Increased the repo rate by 25 basis points from 7.25% to 7.5%
  - Reduced the minimum daily maintenance of the cash reserve ratio (CRR) from 99% to 95%

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6. RBI ACTIONS……..New Bank Licenses

- In October 2013 RBI hiked the repo rate by 25 basis points again – from 7.5% to 7.75% as inflation was still not under control. The MSF was reduced from 9% to 8.75%.
- The rates were left unchanged in the December policy review
- BANK LICENSES
  - In the past 20 years, RBI has given licenses for 12 new banks in the private sector, in two phases
  - RBI received 26 applications for bank licenses by July 1, 2013. Later Tata Sons and Value Industries withdrew their applications
  - RBI planned to issue new banking license in January 2014. However, it is likely that it misses this deadline. The RBI and the government are trying to announce the first set of licenses by March 31, 2014

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7. WHAT WILL RETAIL INVESTORS DO?

- Domestic participation in Indian equities has been quite low
- Some activity was seen towards the latter half of 2013, however:
  - political misgivings
  - Sharp rally in the indices
  - Lack lustre economic performance

  is holding back retail investors
- Strong appetite for high yielding debt
- Lucre for gold waning due to import restrictions and halt in the rally of prices
- New insurance guidelines will force insurers to re orient strategies
  - In the short term it may dent insurance penetration
- Primary markets are likely to warm up in the latter half
- Fixed return options will continue to attract retail
- Equity will be a very small proportion of the allocation

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8. TECHNOLOGY STOCKS

- Although the overall economic scenario was gloomy in 2013, IT was one sector that did exceedingly well. BSE IT gave an extraordinary return of 60%
- The reasons for the rally are:
  - US economic recovery leading to higher IT spends
  - Rupee Depreciation
  - Bell weather stock Infosys rallied on the return of Mr. Narayan Murthy at the helm. Stocks like TCS and HCL put up a great show in terms of revenue growth and stock price growth
  - Indian IT companies are moving up the value chain
- The future growth in this sector will depend on the following factors:
  - Recovery in developed countries like US, Eurozone and Japan
  - New US Immigration laws
  - Value of the Rupee: If the order book grows, only if the rupee appreciates drastically will it adversely affect the margins of IT stocks
- According to Nasscom the industry will grow faster in 2014-15 than it did in 2013-14. Nasscom has also deployed lobbyists in the US to thin down the visa restrictions

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9. MIDCAPS

- The calendar year 2013 saw large caps outperforming mid caps with Sensex giving 8.9% return and BSE Midcap yielding -5.7%
- However, the BSE Midcap performance can be broken down into 2 cycles :
  - Downward: From 1st January 2013 to 28th August 2013: - 27%
  - Upward: From 28th August 2013 to 31st December 2013: + 28%
- The reason for the underperformance in the downward phase are:
  - Lower retail investor participation in this segment.
  - FIIs, the main drivers of Indian stock markets also primarily invest in the large-cap stocks.
  - The earnings growth slowed down in the mid-cap space due to high interest rates and economic slowdown
- A survey of Indian fund managers revealed that 10 out of 16 of them plan to increase their allocation to mid-cap companies in the January-March quarter
- The valuation gap between large caps and mid caps is still big and midcaps will rally the most in case of an economic recovery.

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10. INTEREST RATES

- Inflation is the key driver for monetary policy at the current juncture. Therefore interest rates are likely to follow the path of inflation

- The future path of interest rates will also be determined by the government which is elected. Populist measures like NREGA are likely to keep inflationary pressures high and hence interest rates may remain elevated.

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GDP GROWTH FORECASTS FOR INDIA

Agency	GDP Growth (%) – for FY14
Asian Development Bank	4.7
RBI	5.5
Finance Ministry	5-5.5
Barclays	4.8
Fitch	4.8
Nomura	4.2
Macquarie	5.3
OECD	5.3
HSBC	4
Credit Suisse	6
IMF	5.4

ECONOMIC OUTLOOK OF MAJOR WORLD ECONOMIES

- According to World Economic Outlook from IMF, the world economy is likely to grow at 3.7% compared to 3% in 2013 mainly due to growth in advanced economies. The projections in % growth are as follows:

	2013	2014 (Projected)
United States	1.9	2.8
Euro Area	-0.4	1.0
Germany	0.5	1.6
United Kingdom	1.7	2.4
Italy	-1.8	0.6
Spain	-1.2	0.6
Japan	1.7	1.7
Brazil	2.3	2.3
India	4.4	5.4
China	7.7	7.5
Russia	1.5	2.0

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