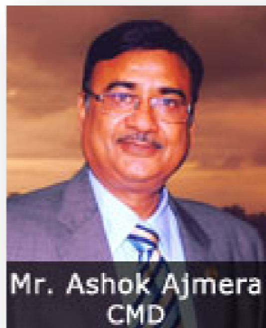
26 YEARS OF EXCELLENCE



Mr. Ajmera's column as on 10th August, 2013

"RBI's CMB move to restrict speculative activity in rupee; accumulate good companies"...

Domestically, BSE Sensex and the NSE Nifty lost further during the week, falling by ~2.0% each. The BSE Mid-Cap index fell by just 0.40% while the BSE Small-Cap index rose by ~1.0%. The NSE Banking index continued to fall, losing another ~1.80%. Ranbaxy, Ambuja Cements, Hindalco, Reliance Infra and NTPC were the top leaders in Nifty this week. BHEL, Asian Paints, Tata Power, Sun Pharma and BPCL were the top five losers in Nifty this week. STC, Ranbaxy, Hindustan Copper, HCC and IRB Infra were the main winners of the week in the BSE 500 index. MCX, BHEL, Educomp Solutions and Core Education were the noteworthy losers in the broader market during the week. The monsoon session of parliament starts amid less disruptions although geopolitical tension between India and Pakistan does stir up passions. Overall, this parliament session appears to be better than the previous session with the main opposition party, the BJP looking to play a more constructive role. As expected the Reserve Bank of India (RBI) further curbed the availability of funds (liquidity) in the markets to stem the rupee's free fall against the US dollar. The central bank will now auction the government of India cash management bills (CMBs) to raise Rs. 22,000 crore on every Monday.

CMB: It is a kind of short-term debt market instrument, which can be issued by the Union government on ad hoc basis for maturities of less than 91 days. The only difference between treasury bills and CMBs is maturities. T-bills can be upto one year. For the last couple of weeks, the RBI has been conducting auctions of CMBs. Last Monday itself, it mopped up Rs. 3,000 crore through seven-day-CMB with a cut-off yield at 9.926 percent. Over the last two months, RBI has instituted several measures to contain the volatility in the foreign exchange market. On a review of the impact of these measures and for effective liquidity management, it has been decided that the RBI will auction Government of India CMBs for a notified amount of Rs. 22,000 crore once every week on Mondays.

First auction on August 12: RBI will sell CMBs of 35 and 34 days, maturing on September 17, 2013. The notified amount is Rs 11,000 crore each issue.

How will it work? RBI wants to suck out excess liquidity from the banking system. This will help stop speculative trading in the currency market. Speculators are not likely to play their game borrowing money from banks. Cash flows will be limited after this CMB move. The move will discourage forward import covers while encouraging the same for export covers. The central bank wants to keep short term rates elevated. If sovereign instruments give higher rates, other short term papers will be subscribed at a minimum premium of 50 basis points over and above that. Banks are already paying 10.25 percent in MSF. It is widely alleged that many importers are buying dollars to book long term forwards. They are clung to idea that the US dollar will rise further against the rupee. This speculative nature collectively aggravating the rupee slide against the US dollar. A contraction of fund flows will squeeze this practice.

Past measures

In July this year, the central bank had raised the Marginal Standing Facility (MSF) rates by increasing the repo rate by by 300 basis points to 10.25 percent. MSF is one type of RBI window wherein banks can borrow overnight. Later, the RBI capped banks' borrowing to 0.50 percent of individual total deposits (or net demand and time liability as it is known in banking parlance). That essentially meant, banks would be able to borrow around Rs. 32,000 crore in total from the repo window at 7.25 percent. Besides, it had put curbs on gold imports while conducting open market operations of government bonds.

Impact of new move....

On Monday, the CMB cut-off yields are expected to be around 11 percent as against 9.92 percent in the previous auction held on August 6. The 10-year (7.16 percent) government bond yield is likely to rise 10-15 bps from 8.15 percent, recorded on Thursday. Banks which issue and subscribe certificate deposits may have to pay higher rate there. CD rates would quote higher than sovereign papers, guaranteed by the government with no chance of default. On every auction, RBI declares a cut-off yield, above which auction participants are not allowed to quote.

Rupee slide

The Indian rupee dropped more than 7 percent to close at 60.88/USD on 8th August, 2013 (Thursday). Earlier, the RBI had issued a raft of measures to tighten liquidity in the market so that it creates demand for rupee-funds and thereby, bring stability in the rupee-dollar rate

FIIs and MFs activity

FIIs invested ~US$114.0mn into Indian stocks between August 2 and August 7, taking their total investment for the month to ~US$189mn. Their net outflows for July stood at ~US$1.0bn after being net sellers of US$1.85bn in June. Their net investment into Indian shares for May was at ~US$4.0bn versus US$1.0bn in April and ~US$1.67bn in March. FIIs poured in US$4.57bn into Indian shares in February after pumping US$4bn in January. FIIs invested US$24.0bn into Indian shares in 2012.

Mutual Funds offloaded Indian shares worth INR 406.9mn during the week ending August 8 (barring Friday). They had sold Indian stocks worth more than INR 1,000 crore in July after selling INR 269.0 crore in June. They offloaded shares worth INR 3,508.0 cr from Indian equities in May. Mutual Funds were net sellers of ~INR 894.00 crore in April. They had net sold Indian shares worth INR 1,767 crore in March. They were net sellers of Indian equities worth INR 847.90 crore in February after being net sellers of INR 5,212 crore in January. The domestic mutual fund industry is facing severe redemption pressures due to herd mentality of the small investors.

Global scenario

US

Globally in US, earnings from consumption companies will be keenly looked into. Earnings from major retailers and data on consumer spending with the hope that the numbers will show that Americans have indulged in some retail therapy in recent weeks. Good news on the shopping front could provide some potential catalysts for a stock market that has stumbled a bit of late. The last two full weeks of earnings season are packed with consumer bellwethers. Macy's is scheduled to report results on Wednesday, while Wal-Mart Stores Inc, the world's largest retailer, will release quarterly earnings on Thursday, along with upscale department store Nordstrom and discount retailer Kohl's. Home Depot, Target and Staples will follow the week after that. Positive news about consumer spending could give the market some upward momentum, which has lagged since stocks wrapped up a strong July. The S&P 500 fell 1.1 percent this week - its worst weekly performance since June. In the absence of strong earnings and economic data, however, we believe that the market is likely to trend lower as volume thins out heading into the latter half of August. US is a consumer-driven economy, so if those earnings come in shy of expectations, the lack of personnel on Wall Street could certainly cause some weakness. Earnings on the whole have topped expectations, with 67 percent of the 446 companies in the S&P 500 that had reported earnings so far beating estimates. About 54 percent of companies have reported revenue above expectations, exceeding the average of the past four quarters, but below the historical average. According to Thomson Reuters, the consumer discretionary sector has tallied the second-best earnings growth of the 10 S&P 500 industry sectors, with 8.5 percent growth in the second quarter, according to Thomson Reuters data. Consumer staples have been weaker, with earnings growth at 3.8 percent for the second quarter.

In addition to earnings, the coming week's numbers will include consumer spending and sentiment figures. The economic data will include a reading on inflation, measured by the U.S. Consumer Price Index. On Tuesday, the Commerce Department will release data on July retail sales. The forecast is for a 0.3 percent gain since June, with a 0.4 percent rise expected when car sales are excluded. July CPI will be released on Thursday. If the CPI figure comes in between 2 percent and 2.5 percent higher year-over-year, the Fed is likely to take the data as a sign that it can start trimming its stimulus as early as September.

Ajcon's view and Recommendations:

Going ahead, all eyes would be on the following events:

12-Aug: Fortnightly Credit Growth Update, Industrial Production YoY for June, Monthly New CPI YoY% for July
14-Aug: Monthly Wholesale Prices YoY% for July, MSCI Indices Quarterly Index Review
20-21 Aug: Promoter Pledging Data for QE Jun-13
27-Aug: Fortnightly Credit Growth Update
30-31 Aug: Aug Centre's Gross Fiscal Deficit and its financing, Qtrly GDP for 1Q F2014, Monthly Old CPI YoY% for July

Indian markets trade at ~13.0x FY14E and ~12.0x FY15E versus historic average of 16x.

At this junction, we believe markets offer value buying opportunities in midcap space. Investors with a longer term horizon should ideally pick good large cap stocks as well at this moment. We recommend "Accumulate" Banks for long term (above one year horizon) on every decline like State Bank of India, Bank of Baroda, Allahabad Bank, Union Bank of India, State Bank of Bikaner and Jaipur, State Bank of Travancore, Bank of India and in private sector recommend ICICI Bank, Axis Bank, HDFC Bank, ICICI Bank, Yes Bank, DCB and Standard Chartered Bank, Union Bank of India, Syndicate Bank. In the NBFC space, we recommend to accumulate IDFC, L&T Finance and Aditya Birla Nuvo. In the IT space, we recommend buying TCS, Wipro (trades at 14x 1-year forward (FY15E) at ~30% discount to TCS) and Persistent Systems. In the telecom sector, we recommend Bharti Airtel and Idea Cellular for long term investors. In the Oil and Gas space, we recommend buying Reliance Industries, Oil India, ONGC and Cairn. In the Commodities space, we recommend investors to accumulate NMDC, Coal India and Manganese Ore. In the Pharma sector, we advise to accumulate stocks like Dr. Reddy's, Cipla, Merck, Glenmark Pharma, Alembic Pharma, Torrent Pharma, Divi's Lab, Unichem Labs and SPARC and Wockhardt (after the steep fall). In the Consumption space, we recommend accumulating ITC, Jyothy Labs, and Nestle on every declines. In the midcap space, we recommend investors to accumulate Cera Sanitaryware, Astec Lifesciene, Apcotex, Liberty Phosphate, Petronet LNG, VaTech Wabag, Sangam (India), Voltas, Can Fin Homes, United Phosphorous, Tata Chemicals, Tata Global Beverages, KSB Pumps, Hathway Cable, Industrial Prudential and Investment Company. In entertainment space and gaming, we recommend Eros International and Delta Corp.

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Ashoka Ajmera

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