ING INVESTMENT MANAGEMENT HOUSEVIEW

Indian Economic Outlook

- RBI continued with its tightening process in its quarterly review of monetory policy by raising both the repo and reverse repo rates. Repo rates were raised by 25bps to 5.75% while reverse repo rates were raised by 50bps to 4.50%, thereby narrowing the LAF corridor to 125bps.

- The central bank raised the FY11 GDP growth forecast to 8.5% from 8.0% and the inflation projections to 6% (at year end) from 5.5% earlier.

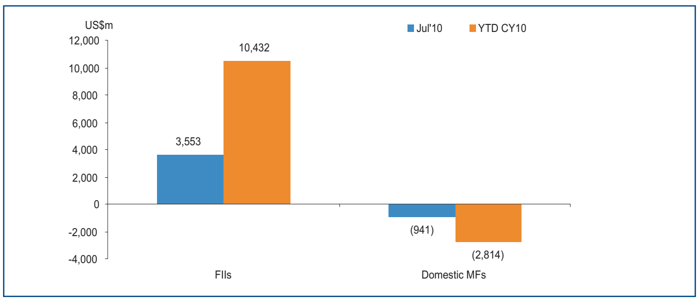
- WPI inflation continued to rise in June and came in at 10.60%, although a bit lower than expectations. However, full impact of fuel price hike has not set in and one can expect the inflation to inch up further for sometime.

- The Index of Industrial Production (IIP) disappointed in May with 11.5% yoy growth against the market expectations of 15-16%. This compares with growth of 16.5% yoy (revised) in April. Capital goods and consumer goods slowed down significantly leading to slow growth in the overall index.

Indian Equity Market Insights

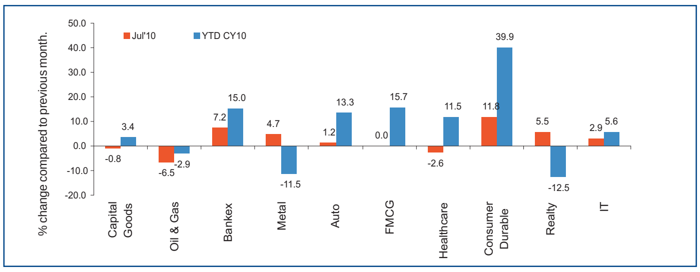
- After a couple of poor months, global markets rebounded in July with most developed market indices registering handsome gains. Lack of further bad news from Europe also augured well for Euro with the currency recovering strongly against the US$.
- Indian markets underperformed its global peers with Sensex gaining only 1% during the month. Poor first quarter results by many corporates also led to a little lacklustre month for Indian markets.
- FIIs liking for Indian equities continued with net FII inflow of ~US$3,553mn in July alone. FIIs have invested a total of US$10,432mn since the beginning of the year. Domestic MFs, however, continued their selling spree and sold US$941m worth of equities.
- Consumer Durables and Banks were in favour in July with both indices registering steller returns. Oil & Gas and Healthcare, on the other hand, did not have a great month with both the indices ending the month in red.

FII and MF Trend



Source: SEBI

Snapshot of Sectoral Trend *(% change compared to previous year)*



Source: Bloomberg

ING OVERVIEW OF SECTORAL TREND

TELECOM

Telecom sector continued to bleed due to hyper competition in the market. However early indications from 1st quarter results suggest a strong resilience from large companies. New players have not really been able to take away the revenue market share from the incumbants. There is still a lot of uncertainty on the regulatory front which remains a huge cause of concern. We remain negative on the sector.

INFORMATION TECHNOLOGY

The first quarter results for most large cap IT players were better than expectation. While the pressure of pricing is still visible, volume growth surprised positively. However, in spite of high volume growth, margins remained under pressure due to cross currency movements and wage hikes by most players. The results for mid cap players were mixed with a few companies disappointing on all fronts. Valuations for large cap players remain very rich and don't leave much scope for upside. We are neutral on the sector.

BANKING

Banks were the only standout sector in Q1 in terms of results and that rightfully reflected in their sharp outperformance in July. There were positive surprises on loan growth and net interest income growth. However, asset quality concerns were observed for most public sector banks. We expect core business performance of banks to improve further over the next 9 months with credit growth of over 20%. In a rising-interest-rate scenario, we believe banks with high proportion of low-cost deposit ie. Current Account & Savings Account (CASA) are better placed than their peers.

AUTO

Most Auto companies reported sequentially weaker margins in the 1st quarter of FY2011 due to higher input costs which were only partially offset by price increases and the benefits of operating leverage. Going forward, we expect margins to improve due to lower commodity prices and recent pricing action undertaken by most companies. Volume growth across 2 wheelers and cars continues to remain strong, with most companies experiencing capacity constraints. Strong volume growth in the commercial vehicles segment continues, in the run up to the expected change in emission norms in September 2010.

CEMENT

The cement market witnessed a volatile start to FY2011 as prices, which saw sharp increase in February, March and April declined from mid-May. Cement prices collapsed in June particularly in South India. These factors would lead to cement companies reporting diverging earnings depending on regional exposure. Cement prices are expected to continue to weaken with the onset of the monsoon and increased supplies from newly commissioned plants. Weaker prices combined with higher input costs will negatively impact margins over the next couple of quarters.

METALS

Steel companies have been hurt by a combination of large imports since April, and steel buyers de-stocking on expectations of further price cuts. Quarterly results for most steel companies (domestic) are expected to be weaker on a quarter-on-quarter basis as the sharp price increase in Feb-Apr-10 are likely to be offset by low sales volumes and the subsequent fall in steel prices. Non-integrated players would also see partial impact from higher cost raw material contracts (iron ore and coking coal) in the quarter. We expect realizations to continue to remain weak over the next couple of months.

CONSUMER STAPLES

Direct to Market is the new strategy with some of the major FMCG players, off-late. To drive volumes in the competitive markets, the FMCG players are expanding their retail models. To begin with, Dabur is expanding its retail model—New stores from 16 to 50 in this fiscal. Marico is also evaluating further expansion of its retail brand—MERA Stores across the country. Yet another FMCG major, ITC Personal Care is aggressively selling its premium personal care range Fiama Di Wills and Essenza Di Wills at ITC's retail model Wills Lifestyle stores. On the back of recent stock run ups, we remain equal weight on the sector with selective exposure to the duet of Brand strength and Valuation comfort.