ING INVESTMENT MANAGEMENT HOUSEVIEW

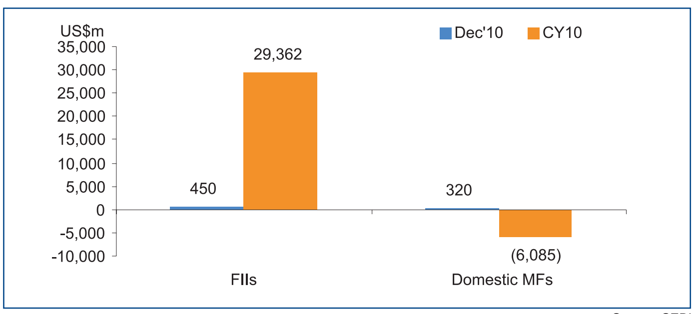
Indian Economic Outlook

- Industrial growth roared back to double digits in Oct'10 after falling to a 16-month low in Sep'10. Strong growth in manufacturing and electricity sector led to the strong overall growth. The index of industrial production (IIP) grew 10.8% yoy in Oct'10 compared to growth of 4.4% yoy in September.
- The RBI took a breather after a few successive rounds of tightening. In its mid quarter review of monetary policy it kept the policy rates at the same levels. RBI has hiked repo rate by 150bps, reverse-repo rate by 200bps, and CRR by 100bps since beginning of 2010.
- The favorable base led to softening of wholesale price index (WPI) inflation in Nov'10. The WPI came in at 7.5%yoy in Nov '10 from 8.6%yoy in Oct'10. For Sep'10, WPI inflation was revised to 8.9% from 8.6% earlier.
- Credit growth continued to be robust at 23.71% surpassing the central bank's target of 20% for the fiscal. However, deposit growth continues to remain sluggish at 14.71%.

Indian Equity Market Insights

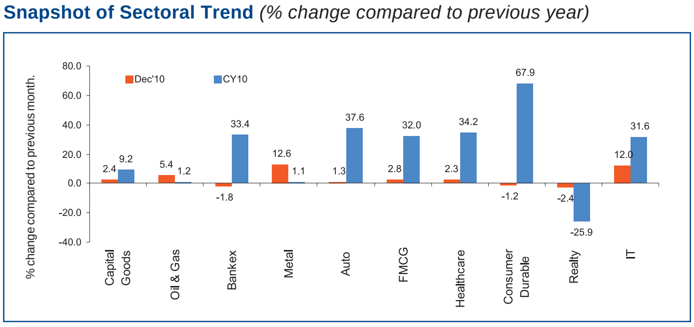
- Most global markets went up during the month but on low volumes. Later half of the month saw very limited activity as holiday season kicked in.
- Indian market also took cue from global markets and the large cap index Sensex was up 5.1% during the month. Midcap and Small caps underperformed the large caps and registered returns of -0.6% and -0.8%, respectively.
- Volumes were low in December as the holiday season started. FII flows to Indian markets were positive with net inflow of US$450m. FIIs invested total of US$29,362m in Indian market in CY10, an all time record.
- Amongst the sector indices, Metals and IT had a great month with both sectors delivering returns in excess of 12%. Realty had a poor month and year and was the only sector delivering negative returns during CY10.

FII and MF Trend



Source: SEBI

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



Source: Bloomberg

ING OVERVIEW OF SECTORAL TREND

AUTO
Sales of cars and two wheelers showed strong growth in the first half of FY2011, driven by rising disposable incomes, easy availability of finance and launches of new models. Growth rates in the second half of the fiscal year will be dampened, mainly due to the higher base, new year price hikes and rising interest rates. However, growth will continue to be healthy, supported by growing incomes and a buoyant economy.

CEMENT
As expected, Indian cement companies have reported weak sales growth, specially coming on the back of very strong October cement sales. While un-seasonal rains in North India, onset of the re-treating Monsoon in South, and festivals in the first half of November are some of the reasons, we also believe that overall the real under lying demand has been weak over the last few months. While private spending in infrastructure has been lackluster, government spending has not yet picked up. The sharp recovery in cement prices from the levels in 2QFY11 are unlikely to sustain with sub-optimum capacity utilization set to continue over the next few quarters.

BANKING
In the mid quarter policy review (mid-December 2010), the RBI announced liquidity enhancing measures— Open Market operations (OMO) of INR 480 bn and SLR cut from 25% to 24%—to address the persistent shortfall in domestic liquidity. Credit growth momentum has been strong at 12.3% YTD (23.7% on a YoY basis) as of 17 December 2010. Deposit growth remained subdued at 14.71% reflecting investor's preference for higher yielding assets due to the soaring inflation. Rising rate would keep funding cost high and margin pressure intact (although with a lag). Nevertheless, we believe select PSU and private banks with better funding franchise, Current Asset & Saving Account (CASA) ratio, lower dependence on bulk deposits, and a well-managed Asset Liability Management (ALM) profile would be able to protect margins effectively.

METALS
The combination of cost increases (both iron ore and coking coal are moving up) and a seasonal pick-up in demand is driving up global steel prices. However, the Indian flat steel market has become increasingly tough and competitive given the spate of new capacities being commissioned. Demand has been lackluster, adding to the pressure and increasing inventories in the system. A tight coking coal market could become tighter if the current wet weather in Australia continues. Potential steel capacity re-starts in China, combined with lower iron ore exports out of India, could result in iron ore prices remaining elevated. In the current situation, we believe integrated steel mills are better positioned in the market due to their cost advantage.

INFORMATION TECHNOLOGY
Cues from global markets remained pretty good with most global IT companies delivering good results. Early indications suggest flat to marginally increasing IT budgets for next year which should auger well for Indian IT companies. Sharp increase in salary levels remain a risk and needs to be watched closely. We maintain a positive stance on the sector going into 2011.

TELECOM
Telecom sector was rocked by 2G scam reports and Radia Tapes. A lot of uncertainty looms over the sector with no clarity over the government's stance on the whole issue. In addition, much delayed Mobile Number Portability (MNP) was finally launched during the month and will be launched throughout the country by 20th Jan. We expect pricing to remain under pressure with fierce competition expected in the post paid sector. We maintain our negative stance.

CONSUMER STAPLES
Sector showed very flattish and uneventful trend, like the broader market. Month started with cigarette companies stopping production, on lack of clarity on pictorial warning. Dabur saw problems in its Nepal manufacturing unit for fruit juices. Raw materials like Copra, Palm Oil and Soya continued their ascent. This could impact margins in coming quarters.

UTILITIES
Utilities continued its spate of underperformance. Incremental data is suggesting lower power off take by State Electricity Boards (SEBs) on rising loss burden. Merchant tariffs continue to maintain their downward trajectory in October averaging Rs4/kwh in bilateral trades. Growth in energy requirement has lagged availability, thus further narrowing the demand-supply gap. Currently energy deficit stands at 6.5%.

INDUSTRIALS
Order inflows for construction companies from NHAI, Power T&D companies and from Power Grid Corporation of India Limited (PGCIL) have seen some pick-up in the last month after a virtual shutdown in ordering activity from both PGCIL and NHAI. We expect this pick-up in tendering activity to continue till at least March 2011, which is the time when Government and PSU budgets lapse. Even though we expect the ordering activity to improve, we still remain cautious on the sector on account of concerns on execution capabilities and high competition which could impact profitability adversely.

HEALTHCARE SECTOR
Sun Pharma received a favourable Appeals Court ruling to launch generic Eloxatin 'at risk' in the US market. If Sun decides to launch in January 2011, it could be the sole generic company in a US$1.3bn market (pre-genericisation) for 20 months. Ranbaxy received US FDA approval to launch generic version of Aricept (US$2bn revenue in US) under 180 days exclusivity and Sun Pharma, along with other generic players, lost the patent litigation for the generic Abilify (a US$2bn drug) to innovator BMS; the launch is now expected in 2015.

ENERGY SECTOR
Dated Brent prices crossed the $ 90/bbl mark in December v/s $ 88.2/bbl mark in November 2010.The light-heavy differential shrunk in November because of healthy physical demand for crude. Demand for sour crude improved due to: strong demand from the US refineries with their return from the maintenance period; and heating demand due to cold weather in the US. Singapore and Dubai crack margins, as quoted by Reuters, stood at US$6.1/bbl in December vs. US$ 6.02/bbl in November. This rise in margins was mainly due to increase in crude prices and gains in light and middle distillate cracks. Henry hub December gas prices averaged at US$ 4.2/mmbtu, as against US$ 3.7/mmbtu in November. The gas market continued to improve due to increasing demand owing to falling temperatures.