INSIGHT

November, 2014

REFORMS ON FAST TRACK

ONGC | Cadila Healthcare Ltd.

Karur Vysya Bank Ltd. | J.K Lakshmi Cement Ltd.

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- Stock Picks
- Valuation at a Glance
- Capital raising through QIP
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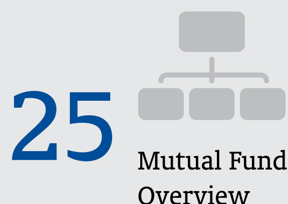

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Market Overview

The reform process has got new wings after BJP's thumping win in key states – Maharashtra & Haryana. In Haryana, BJP has secured a full-fledged majority while in Maharashtra; it is the single largest party and is sure to form the government. Soon after the elections are over, BJP spent no time in de-regulating the diesel prices. Probably, considering that this was the best time for India to go ahead with the crucial and one of the most sensitive reforms as the oil marketing companies (OMC) started making profits on selling diesel as against under-recoveries earlier. Mr. Modi also pushed ahead with the important labour reforms by partially dismantling the factory inspector raj, perceived by industry to be arbitrary and corrupt. Under the proposed reforms, labour inspectors will lose their power to decide which unit to visit and the number of forms related to compliance with labour laws that employers have to file will drop from 16 to 1. The government has issued an Ordinance to facilitate an auction of the coal blocks that the Supreme Court had struck down as illegal last month. The new government indicated that the cancelled coal mines would be e-auctioned to all private consumers of coal (power, cement, state, aluminum) even as the state-owned companies (such as the National Thermal Power Corporation (NTPC)) would be allocated coal mines and therefore won't be participating in the auctions. Although, the details are still awaited, the reform process particularly regarding the e-auction of coal blocks have been fretted with criticisms from the opposition parties as well as the trade unions. The leftist party has termed the recent reform policies of the government to be "anti-people" and more corporate friendly. Thus, although we are pretty certain that the reform process will continue, we are again back to the same old question of implementation.

Incidentally, BJP is still the second largest constituent of the 245 member Rajya Sabha with 43 seats, after Congress which has 68 seats. Thus, it has still to depend on the alliances and friendly regional parties as well as opposition parties for all the legislations, in order to get the assent of the Upper House. The investor fraternity is eyeing the winter session of the parliament after BJP's success in the previous session. The winter session is scheduled to begin from November 24 till December 23. The cabinet committee on parliamentary affairs (CCPA), headed by union home minister Rajnath Singh, suggested a total of 22 sittings in the session during the course of which the government will try to pass 67 Bills—eight pending in the Lok Sabha and 59 in the Rajya Sabha .Goods & services Tax (GST) Bill, the Land Acquisition and Rehabilitation and Resettlement Bill, Insurance (Laws) Amendment Bill and coal ordinance are some of the bills to name a few, which will be in the radar. Amendments in the Factories Act, Apprentices Act and Labour Laws (exemption from furnishing returns and maintaining registers by certain establishments) Act will also be in the limelight. Although, there are strong expectations on the reforms front, however, one thing's pretty certain that there will be strong resistance from the opposition parties who are sure to go against the coal ordinance. In the case of labour reforms too, employee unions have accused the government of ignoring the interests of workers in seeking to enhance the ease of doing business in the country. Thus, the winter session of the Parliament will not be as smooth as the previous one. The only other alternative which will be at government's disposal will be to go in for joint session to pass the ordinance. A joint session can be called (after such piece of advice is given to the President by the government) once a House has passed a Bill but the other has rejected it, or does not act on it for six months.

The mood among the global investors as well as rating agencies is positive for India and continues to be so with the plethora of reforms on the cards as promised by the ruling government. The recent announcement by the government to scrap Planning Commission was applauded by the rating agency major S&P. The rating agency opined that Prime Minister Narendra Modi's scrapping of India's Planning Commission was a significant step in enhancing the autonomy of the states particularly in deciding their own spending priorities. Moreover, Fiscal decentralization should result in more competition between states in attracting investment and promoting growth, setting the stage for further economic reform and modernization. Standard & Poor's affirmed its 'BBB-/A-3' long- and short-term sovereign credit ratings on India on Sept. 26, 2014, and revised the outlook to stable from negative. According to S&P, Modi will seek to win in as many state elections as possible, especially in the next two years, to gain seats in the upper house of parliament and ease the passage of legislation. The recent rejig of the economic team at the cabinet is also perceived to be a significant thoughtful decision ahead of the budget. Finance & Economic Affairs Secretary Arvind Mayaram was shifted to the tourism ministry, after exercises for the 2015-16 Budget had begun. Rajasthan Chief Secretary Rajiv Mehrishi, handpicked by Chief Minister Vasundhara Raje, was made the new economic affairs secretary. And, in the department of economic affairs, US-based economist Arvind Subramanian was appointed to fill the long-vacant post of the government's chief economic advisor.

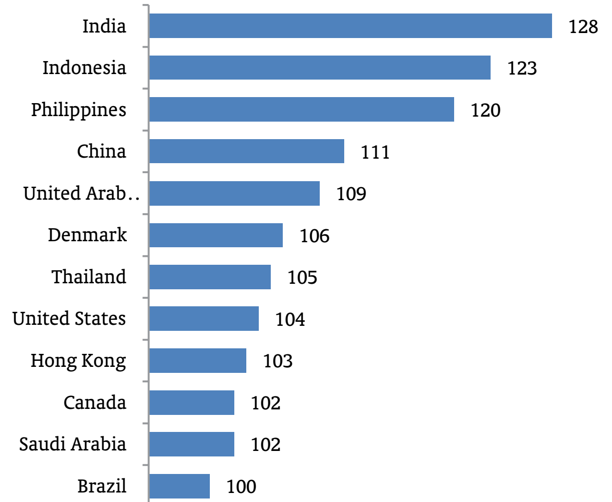
The government plans in the next parliamentary session to scrap nearly 300 outdated laws. It has already hiked defence and insurance foreign investment caps to 49 percent from 26 percent and announced plans for private-public partnership to build more roads, railway and other infrastructure. Although, there has been broad based optimism created by Mr. Modi himself, one cannot also deny the luck factor running for the present government. The benefits which bode well for India amid fall in the global commodity prices such as crude, coal, metals in mammoth proportions. India is net importer of these essential commodities and a fall in the prices result in multiple benefits of lower inflation together with benign food inflation, improvement in fiscal & current account deficit and lowering of the interest rate structure in the economy. Incidentally, all these factors were of major headache and adverse effects talked about in great lengths when UPA government was at the centre.

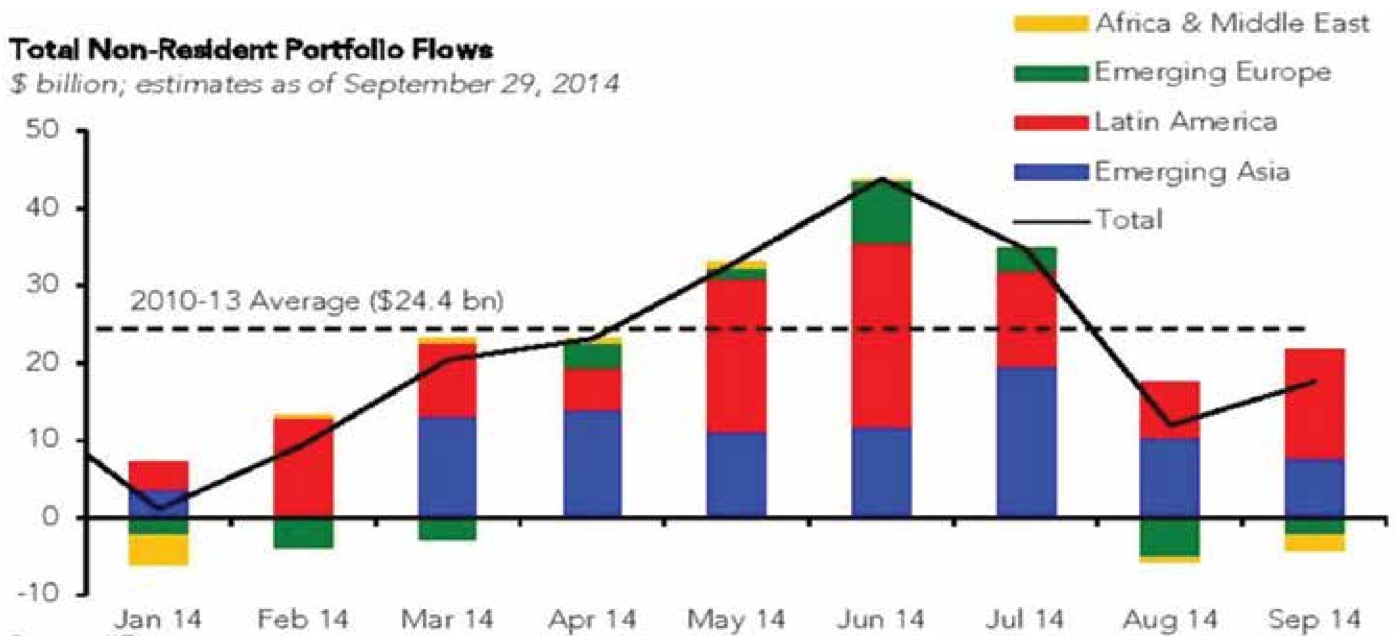
Together with benign global commodity prices, fiscal balance will also get support from the proposed disinvestment of PSU companies. ONGC is believed to be the first one in the Modi era wherein the government has hoped to raise $3 billion from five-percent stake sale. The time is indeed ripe with the optimism around and stock markets at all time highs. The bond markets have already started to factor in lower

interest rates in the future, a prime condition to promote "Make in India". It is also believed RBI has put its best efforts to keep the rupee volatility under check and in the range of Rs 58 to 63 per dollar. In fact, with apprehensions of higher interest rates in US in the future amid improving economic growth, there has been appreciation in US dollar. The concerns with regards to capital flights from emerging nations is in the offing and more severe implications for the ones with widening current account deficits, which would make emerging market countries more vulnerable to rising interest rates.

The portfolio flows to the emerging nations have been volatile with declines reported in July & August 2014 after the highest mark witnessed in June. The declines were largely due to the impending US rate hike. The foreign portfolio inflows for the month of September however staged smart comeback as The Indian and Mexican bond markets and the Brazilian equity market saw significant inflows. According to IIF EM Portfolio Flows Tracker, emerging markets received $18 billion in September, up from $12 billion in August (revised up by $3 billion). On a component basis, estimates indicate that portfolio equity inflows slowed marginally to $8 billion, while portfolio debt inflows picked up to $10 billion. Indeed, there might be some pain in the short term for EMs, but with growth back for the largest economy, the long term prospects are brighter. The same is captured by the latest Global consumer confidence by Neilson, which have increased one index point to 97 in the second quarter of 2014, following a two-point rise at the start of the year. According to the survey, Regional consumer confidence increased in North America (103) and Europe (77), rising three and two points, respectively, compared to the first quarter. Confidence was highest in the Asia-Pacific region, which held steady from the first quarter with a score of 106. Confidence declined in the Latin America (90) and Middle East/Africa regions (93), dropping three points and one point, respectively. Incidentally, for the latest survey, India (128) increased seven points to report the highest consumer confidence index score, surpassing Indonesia (123), which previously held the top spot for five consecutive quarters. Thus, the focus is truly on India even as concerns surrounding China's hardlanding and deflation in Europe take centre stage.

Q2 2014 Consumer Confidence Optimism in the Economy





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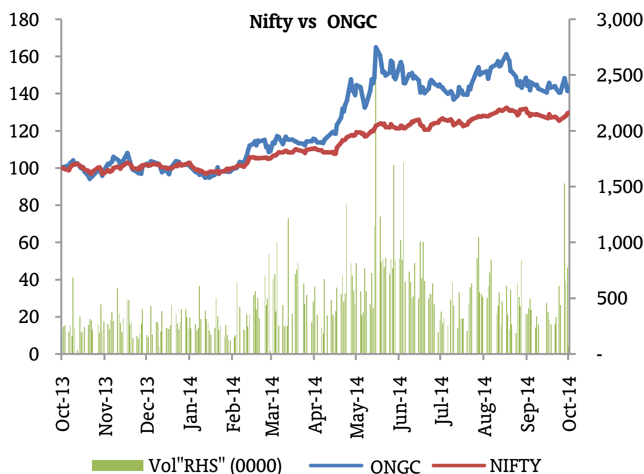
Stock Picks

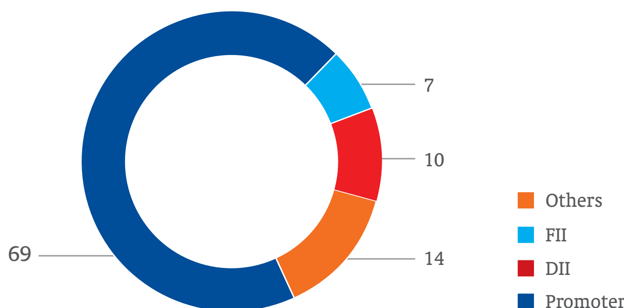
ONGC CMP: 395/- Rating: Buy TGT: 516/-

Company Information

BSE Code	500312
NSE Code	ONGC
Bloomberg Code	ONGC IN
ISIN	INE213A01029
Market Cap (Rs. Cr)	3,37,728
Outstanding shares(Cr)	856
52-wk Hi/Lo (Rs.)	472.0/263.30
Avg. daily volume (1yr. on NSE)	46,12,071
Face Value(Rs.)	5.0
Book Value (Rs)	201.22



Shareholding pattern as of September 2014 (%)



Particulars (In Rs. Cr.)	FY13	FY14	FY15E	FY16E
Net Sales	162,403	174,477	192,302	205,416
Growth (%)	10%	7%	10%	14%
EBITDA	44,092	49,195	68,336	77,905
EBITDA Margin (%)	27.1%	28.2%	35.5%	37.9%
Net profit	23,994	26,665	31,642	37,291
Net Profit Margin (%)	14.8%	15.3%	16.5%	18.2%
EPS (Rs)	28.31	0.98	36.70	42.99

Source: Bloomberg

Company Description

Incorporated in 1956, ONGC is India's largest national oil & gas company, primarily engaged in the exploration, development and production of crude oil and natural gas in both India and overseas. The company also has presence in downstream refining and marketing segment in India, which operates through its subsidiary MRPL with an installed capacity of 15 MMTPA. Recent reforms announced by Government in Oil & gas space would provide a fillip to ONCG's future earnings.

Investment Rationale

Diesel deregulation- long waited reform comes to play

Government has announced the long waited reform of diesel price deregulation amid declining crude oil price since August 2014. Diesel deregulation means its prices will now be market linked, making the customer pay more when global crude oil prices rise and vice versa. Such reform would provide a fillip to upstream companies like ONGC, Oil India and Gail, as they share 50% of fuel subsidies with government. Diesel accounts for 55% of total under-recoveries and diesel deregulation would bring down the up-stream's subsidy burden to Rs 527 billion in FY15 and Rs 487 billion in FY16 from Rs 670 billion in FY14. As ONGC accounts for 84% of total upstream distribution, the company has to share most of the subsidy burden among all upstream companies. Diesel price deregulation came in the wake of lower crude price which stood at USD 87 per barrel and Indian crude basket is averaging at USD 86/barrel against the earlier assumption of USD 100/barrel. It is also expected that elimination of the diesel subsidy would lead to a 24% rise in net crude oil realization, to USD 58/barrel by FY16, resulting in USD 700 million annual improvement in Oil companies cash flow over FY14-FY20 period. Thus ONGC is the maximum beneficiary of ongoing reforms in Oil and Gas sector due to its strong presence in the sector.

Gas Price Hike

In a recent move, Indian government has increased the gas price to USD 5.61/mmbtu from current USD 4.2/mmbtu based on the modification to the Rangarajan's committee's suggested formula, which is effective from 1st November 2014. With the announcement of the gas price hike, the long awaited overhang on gas price issue came to an end. Also premium provided for discoveries in deep-water, ultra-deep water etc. would also lure further exploration activities. The gas price hike is a big boost for upstream oil companies, though the earlier committee recommendation was tad higher than USD 5.61/ mmbtu. The Rangarajan Committee had earlier recommended the new pricing norm which was trailing 12-months average of weighted price of imported LNG, US Henry hub, UK NBP and JCC, while new formula removed the JCC, Henry Hub price and imported LNG cost while included Alberta Gas reference price, and consumption of gas in Russia and EU, thus resulted in almost 75% lower gas price hike as compared to earlier formula. ONGC, with significant presence in the sector hence would be benefited from gas price increase and it is estimated that for every USD 1 rise would increase ONGC's earning per share by Rs 2.5, thus provide a fillip to its earnings. The earnings growth would amplify more if the company works towards raising its output from 2.4 billion cubic meters (bcm) to 4 bcm in the next couple of years. Thus, higher gas price and gradual ramp-up in production is likely to drive ONGCs earnings and RoE.

Venturing into fuel retailing

With the diesel price deregulation, the sector is again opened for private fuel retailers, who refrained from selling diesel price owing to steep difference between market and selling price. Such development, lure ONGC to decide on venturing into fuel retailing through its listed subsidiary Mangalore Refinery and Petrochemicals Limited (MRPL), thus helping the company to garner some market share in fuel retailing market. According to the ONGC's management with the current petrol and diesel prices, it is the right time for MRPL to venture into fuel retailing. However, in the meanwhile, MRPL already has a blueprint in place to roll out 120 retail outlets in the first phase of expansion strategy in the state of Karnataka. MRPL has the approval to set up 500 retail outlets and its parent company, ONGC, has approvals to set up 1100 retail outlets. However, as on date, only 3 outlets are in operation and management conveyed that before moving further into the business, company will undergo a retail portfolio reassessment and outline the best possible expansion or ramp-up model for the outlets. Though entry of private players could intensify the competition, however, given ONGC's strong presence in the sector it could mitigate the price pressure and also open up new avenue of revenue generation for ONGC.

New projects to drive volume growth

The company has already done with its capex program and as per the company the projects such as G1 & GS-15, North Tapti, BHE, SB-14, B-46 are completed. Further the development of B-22 cluster, B-46 cluster, C-series, North Tapti, D-1 is ongoing, albeit the production from these projects has also commenced. ONGC is envisaging of starting 11 additional projects, of which 5 would be commissioned in FY15, 6 in FY16 and 1 project (development of Vasistha and S-1) in FY17E. The commencing of these new projects would ramp up the production, thus propelling the volume growth for ONGC.

Key Risks

- High volatility in crude price would increase fuel subsidy burden for ONGCs, thus have a direct bearing on earnings growth.
- Historically, ONGC has failed to meet its annual production target of crude oil and natural gas, hence any future slippages could impact overall revenue growth.
- Company is operating in highly regulated sector, hence any adverse regulation imposed by government could be negative for ONGC.

Valuation

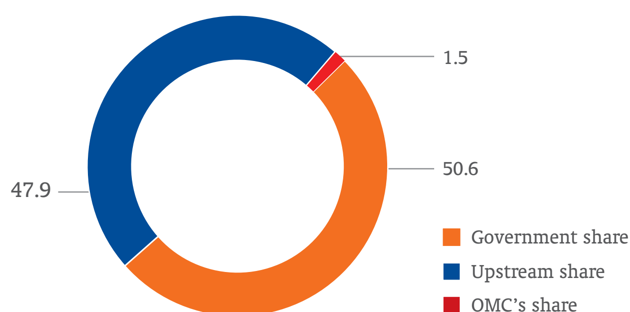
ONGC is a Maharatna PSU company with strong presence in oil and gas space and a key beneficiary of ongoing reforms announced by the new government to revive the ailing domestic economy. Diesel price deregulation, gas price hike, planning to venture into fuel retailing and commencement of new projects are the long term triggers for ONGC to outperform the benchmark index. Moreover, domestic LPG subsidies should also reduce as the new government is reviving direct benefit transfer, thus providing a huge boost for ONGC as the company has to share most of the fuel subsidy burden. It is estimated that at current crude oil price, a lower subsidy burden would improve ONGC's net realization to about USD 50-60 per barrel. Even, if crude oil prices move higher, with diesel under-recoveries eliminated, ONGC's net realization should improve. Such reforms are Earnings accretive for ONGC and thus we provide a positive stance on the scrip with target price of Rs 516 for 12 months investment horizon. On valuation front, the scrip is trading at P/E multiple of 9.1x of FY16E EPS of Rs 42.99.

Status of the New projects

Project	No. of fields	Status
Current/ongoing projects		
G1&GS-15	2	Production commenced
Development of North Tapti, BHE ,SB-14, B-46	8	Projects completed
B-22 cluster, B-46 cluster, C-series, North Tapti, D-1		Projects ongoing but production commenced
New projects		
11 new projects	33	Estimated capex of Rs 363bn
-4 projects		Expected completion in FY15
-6 projects		Expected completion in FY16
-1 project (development of Vasistha and S-1)		Expected completion in FY17

Source: company

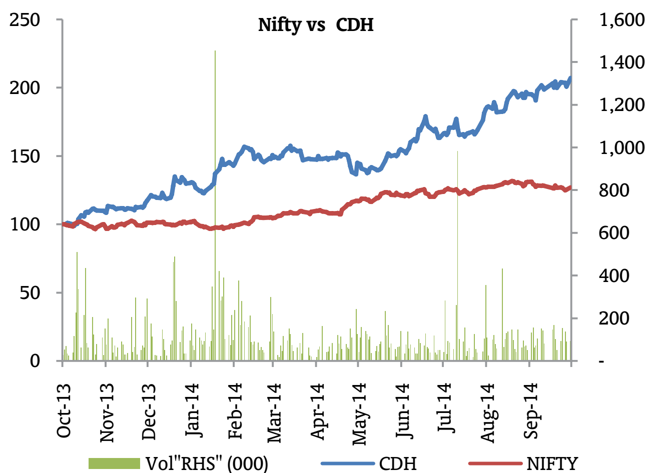
Fuel subsidy burden sharing (%)



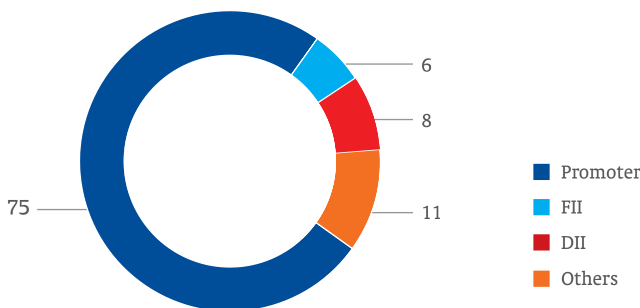
Cadila Healthcare Ltd. CMP: 1384/- Rating: Buy TGT: 1600/-

Company Information

BSE Code	532321
NSE Code	CADILAHC
Bloomberg Code	CDH IN
ISIN	INE010B01019
Market Cap (Rs. Cr)	27,824.30
Outstanding shares(Cr)	20.47
52-wk Hi/Lo (Rs.)	1397.7/650
Avg. daily volume (1yr. on NSE)	118,928
Face Value(Rs.)	5.0
Book Value (Rs)	161.16



Shareholding pattern as of September 2014 (%)



(In Rs. Cr.)	FY13	FY14	FY15E	FY16E
Net Sales	6,155	7,060	8,395	9,822
Growth (%)	21%	15%	10%	14%
EBITDA	1,138	1,221	1,542	1,909
EBITDA Margin (%)	18.5%	17.3%	18.4%	19.4%
Net profit	690	836	1,027	1,300
Net Profit Margin (%)	11.2%	11.8%	12.2%	13.2%
EPS (Rs)	32.01	39.25	50.28	64.00

Consensus Estimate: Bloomberg

Company Description

Cadila healthcare (CDH) is a leading Indian pharmaceutical company with strong presence in US generic drug market. The company's key operating segments include US generic, Domestic (formulation, API and wellness), International markets and Joint ventures. CDH is a part of Zydus group with a significant presence over 90 countries. The company's manufacturing facilities are located in the state of Gujarat, Jammu (India) & Ethopia and are approved by all prominent international regulatory bodies including USFDA, WHO-GMP, WHO-Geneva (GDF site for Anti-TB), TGA Australia (PIC/S), MHRA-UK, MCC-South Africa, ISO 9001 and ISO 14001. CDH is among the top 5 pharmaceutical companies in India and 8th largest Generic company in US in terms of prescriptions.

Investment Rationale

US market poised for higher growth

CDH has considerable presence in US generic drug market and it is now the 8th largest generic company in terms of prescription. Over the years, company has been strengthening its foothold in US with revenue contribution from the market increasing from 14% during FY09 to 30% in FY14. CDH's US sales has shown strong growth momentum during FY09-14 by growing at a CAGR of 40%, backed by aggressive fillings and product launches. Such phenomenal growth has also attributed to company's acquisition of Nesher in US, which bolstered the US portfolio by adding a pipeline of controlled release substances. The US pipelines include 225 ANDA fillings, 85 approvals and 60 launches so far in FY15. In the past few years, all large generic drug makers in the US are increasing their product exposure to complex and difficult segments due to stiff competition and consolidation among distributers. Hence to match with the peers, CDH has been increasing its US filings among niche segments in past 5 years in an intention to build strong footprint in US generic market in niche and complex segments to sustain in highly competitive market scenario. Apart from filing drugs in niche segment, company is also working to launch innovative products in US. Hence, it is expected that all these strategies would bode well for the company and the US market would poise for higher growth for CDH.

Domestic formulation business expected to revive post restructuring

CDH is the third largest drug player in India with market share of 4.03% as per AIOCD (All Indian Origin Chemists & Distributors Ltd.) and also holds 2nd position in dermaceutical segment. The company has 15 brands among top 300 brands in India with domestic formulation business contributing about 30% of total revenue. The domestic portfolio constitutes of 69% acute and 31% chronic. During FY14, the company has launched 75 products in domestic market, including 19 first in class drug. However, the impact of NLEM (National List of Essential Medicines), trade channel issues and product withdrawal adversely impacted domestic formulation sales which grew mere 6% YoY during FY14. Nevertheless, the effect of NLEM has normalized, thanks to restructuring of the business initiated by the company coupled with CDH's aggressive approach towards products launch and ability to launch first in market products, CDH domestic formulation

business would likely to get a fillip going ahead. Company's continuous focus on increasing domestic field force (increased from 3000 in FY09 to ~5000 in FY14) to support its large product pipeline and line extension would also support its future growth.

Market leader in Wellness segment

Zydus Wellness, a subsidiary of CDH (72% holding) is a market leader in domestic sugar free, peel-off and scrub range of skin-care products. In wellness segment, CDH earned maximum revenue from Sugarfree segment followed by Nutralite and Everyuth segments. During the period between FY10-14, company's wellness business grew at a CAGR of 13% led by Sugarfree segment on the back of sharp increase in diabetic patients in India, rising health awareness, new product launches across the segments and line extension. In low-calorie substitute market segment, CDH's sugarfree segment holds 93% market share and thus the competition in this segment is lower compared to Nutralite and Everyuth segments. To revive Nutralite and Everyuth segment, management has restructured the businesses and expect the growth to resume during FY15. Economic rebound and increasing health awareness would drive the revenue growth of wellness segment for CDH.

Strong Financials

Over the years, company has been delivering strong financial results with revenue growing at a CAGR of 20% during FY10-14, followed by EBITDA growth of 11% and PAT growth of 12%. Healthy cash flow led the company to maintain gearing ratio under comfort level despite its expansion in existing capacity and acquisition of Nesher and Biochem. Company has good track record of rewarding shareholders by dividend and it has maintained healthy payout ratio of 20% in past 4 years. Given its strong product launches in US and reviving of its domestic formulation business, it can be expected that Cadila would be able to sustain such growth momentum in near future.

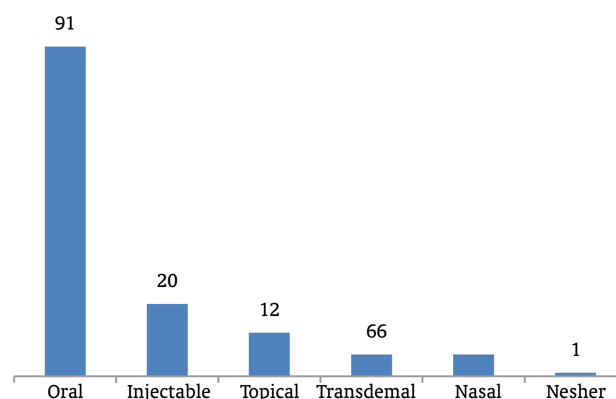
Key Risks

- **Currency volatility:** Export contributes ~55% of total revenue, hence any currency volatility could impact future earnings for the company.
- **Operating in highly regulated sector:** The company is operating in a highly regulatory market and thus any adverse litigation issue could have a negative bearing on company's business.

Valuation

Cadila Healthcare is the 8th largest generic drug manufacturer in US and third largest in India. Over the years, the company has aggressively launched generic drug version in US which make its product pipeline strong with 225 ANDA fillings and 85 approvals. US drug market accounts 30% market share of the total global drug market, hence it is poised for higher growth for all generic drug makers. Hence to increase its generic market share in US, CDH has been increasing its US filings among niche segments and we believe it would bode well for the company in the long run as it would amplify future earnings growth. With the normalization of NLEM effect coupled with CDH's aggressive approach towards products launch and ability to launch first in market products, CDH domestic formulation business would likely to get a fillip going ahead. On financial front, the company has shown strong resilient over the years with revenue and net profit growing at a CAGR of 20% and 12% respectively. Given its aggressive product launches in US, revival of domestic formulation business, healthy RoE of 27% and consistent dividend payout are the key fundamental highlights to support its premium valuation. Hence, despite of steep rally in last one year we believe that there is enough steam left for the stock to move higher, thus we recommend our investors to BUY the stock with target price of Rs 1,600 from 12 months investment perspective. On valuation front, the scrip is trading at P/E multiple of 21x of FY16E EPS of Rs 64 (Bloomberg estimates).

Pending approvals in niche segments



Source: company

US ANDA filings overview

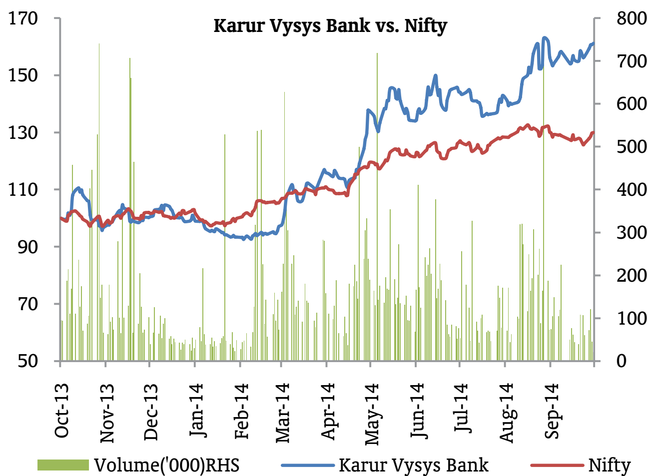
	FY09	FY10	FY11	FY12	FY13	FY14	Filings
Oral	12	4	18	19	22	34	171
Nasal	2	1	2	0	0	1	6
Injectable incl Partners)	5	9	4	0	8	5	31
Transdermal	0	0	0	2	1	3	6
Topical	0	0	0	0	2	6	10
Nesher (control substance)	0	0	0	0	0	1	1
Total ANDA filed	**19**	**14**	**24**	**21**	**33**	**50**	**225**

Source: company

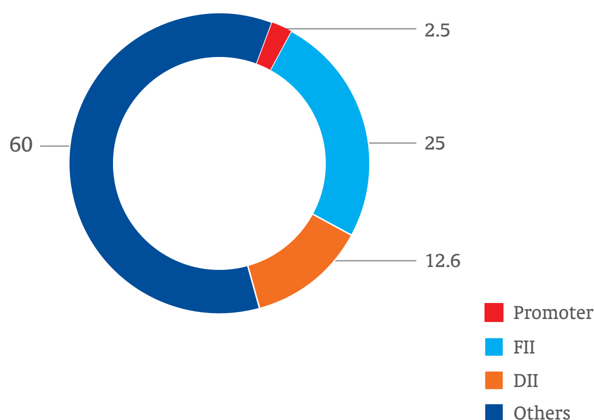
Karur Vysya Bank Ltd. CMP: 541/- Rating: Buy TGT: 700/-

Company Information

BSE Code	590003
NSE Code	KARURVYSYA
Bloomberg Code	KVB IN
ISIN	INE036D01010
Market Cap (Rs. Cr)	6549
Outstanding shares(Cr)	10.7
52-wk Hi/Lo (Rs.)	554.7 / 310.1
Avg. daily volume (1yr. on NSE)	156,912
Face Value(Rs.)	10
Book Value	327.0



Shareholding pattern as of September 2014 (%)



(In Rs. Cr.)	FY13	FY14	FY15E	FY16E
Net interest Income	1158	1284	1491	1805
NIM (%)	3.0	2.8	2.9	3.0
Operating Profit	849	838	1058	1289
PAT	550	430	568	704
EPS (Rs)	51	40	53	66
BV (Rs)	288	309	347	393
GNPA (%)	0.96	0.82	0.90	0.96

Source: Ashika Research

Investment Rationale

Economic recovery to lead growth

Karur Vysya bank (KVB) has delivered robust growth in loan book at 27% CAGR between FY09-14 on the back of expansion drive wherein it increased the no. of branches 1.8x from 312 in FY09 to 572 in FY14. The bank has changed its focus from corporate and commercial segment to retail lending in last 2 to 3 years and is also gradually lowering its dependence on gold loans. Management took conscious decision and scaled its temptation of higher loan growth in FY14 particularly in the gold loan segment. Overall loan book growth was 15% in FY14 and retail book grew by 21% YoY. With the revival in economic growth, KVB is in the driver's seat to deliver high double digit loan growth.

Higher CASA ratio to improve margins

KVB has changed its focus from corporate and have been pushing to increase its share of retail in total loan book. The same seems to reflect in improving CASA ratio from 19% in FY12 to 21% in FY14. However, there is ample opportunity for the bank to increase CASA thus improving margins.

NIMs bottomed out, bounce back ahead

Net interest margin (NIM) of KVB has come off to 2.6% in FY14 from 3-3.4% in FY11-13 led by lower loan growth and consequently lower growth in net interest income (NII). High slippages and significant increase in interest expense has resulted in Lower NII growth. However, with lot of the concerns addressed, KVB is likely to register higher NIM margins of ~3% in the next few quarters on the back of lower cost of funds, recent capital infusion & higher corporate loan growth. Further, focus on retail deposits will help in improving NIMs going ahead.

Stabilizing cost to income ratio

KVB's cost to income ratio increased substantially from 42% in FY11 to 55% in FY14 on the back of branch expansion drive resulting in higher operating expenses. Besides, a few one-off expenses, like the cost of stock options (issued at a lower price) and provision for wage settlement, impacted costs in FY14. However, going ahead there will be slowdown in branch and employee additions over the next few years which is expected to help improve the bank's cost to income ratio, thus resulting in higher operating profit.

Improvement in Asset Quality

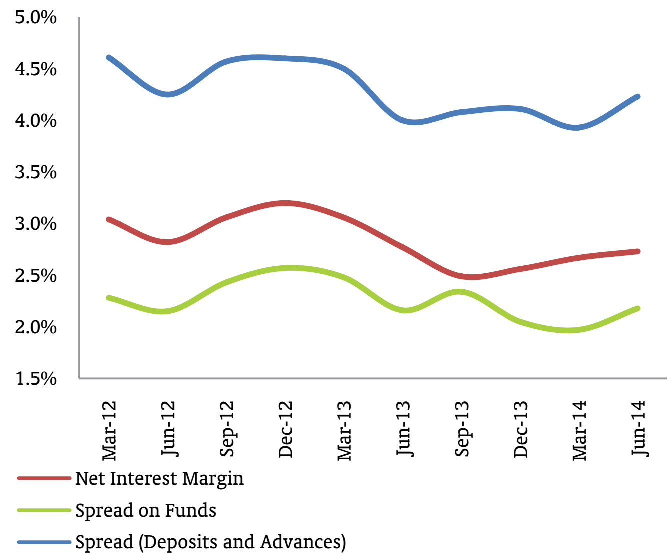
The asset quality of the bank has improved during FY14 partly due to conservative approach to loan growth & higher coverage ratio. Gross as well as Net NPA improved to of 0.82% & 0.41% in FY14, down from 0.96% & 0.37% in FY13 respectively with healthy provision coverage ratio of 75%. Fresh slippages were also contained at 1.5 bn (0.5%) in FY14 vs Rs 2 bn (0.8%) in FY13. The bank has curtailed to loan to stressed sectors and the same is visible with Infrastructure exposure (as % of total loan book) coming down significantly from 13% in FY12 to 9% in FY14.

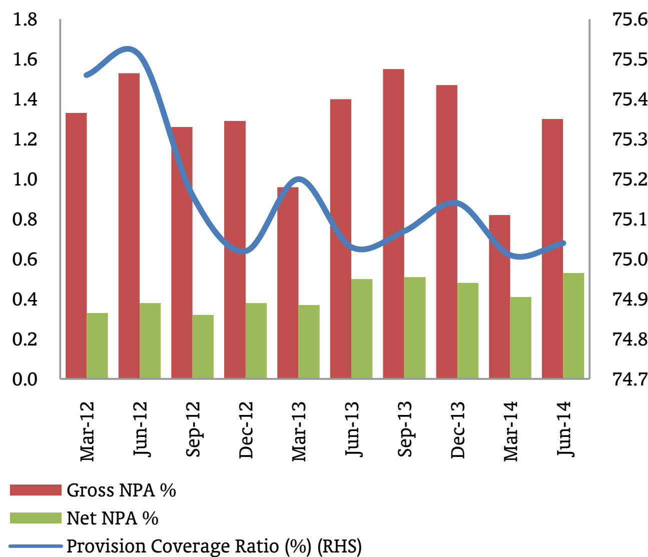
Key Risks

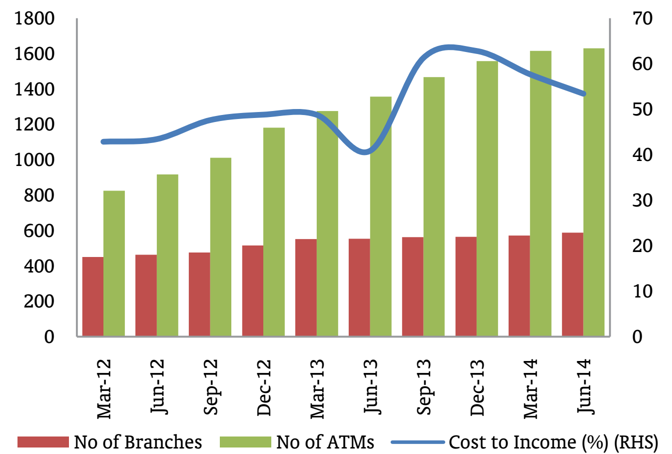
- Higher than expected decline in net interest margins
- Higher than expected worsening of asset quality
- Increase in interest rates in the economy

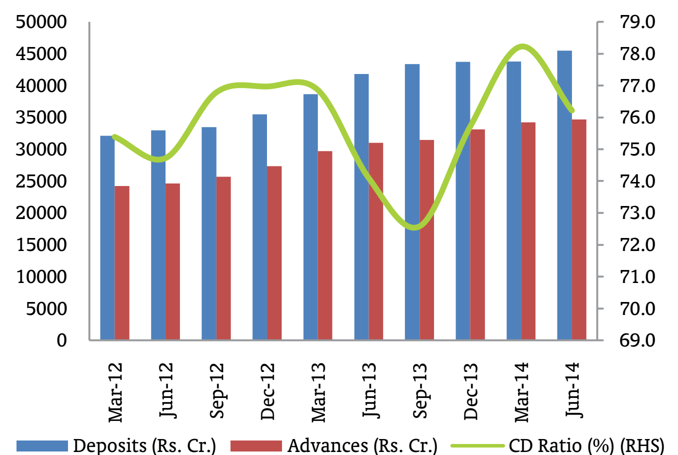
Outlook & Valuation

With revival in economic growth together with subdued outlook for future interest rates looks promising for KVB in the mid size segment. We expect credit growth momentum to pick up especially towards corporate segment in coming quarters with improving economic environment as well as margins to improve on the back of lower cost of funds as well as higher CASA ratio. We believe maintaining operating costs will lead to higher operating profit while the asset quality has bottomed out and is expected to improve from here on. Due to slower business growth and higher cost structure, ROE / ROA have come off to 13.4% / 0.9% in FY14 from 19% / 1.3% in FY13. However, the return ratios are expected to pick up on the back of improving financial metrics. We assume credit growth of ~20% CAGR for FY14-16E. At the CMP of Rs 541, the scrip trades at 1.38x FY16E book value of Rs 393 and recommend BUY for a target of Rs 700, implying a return of 30%.





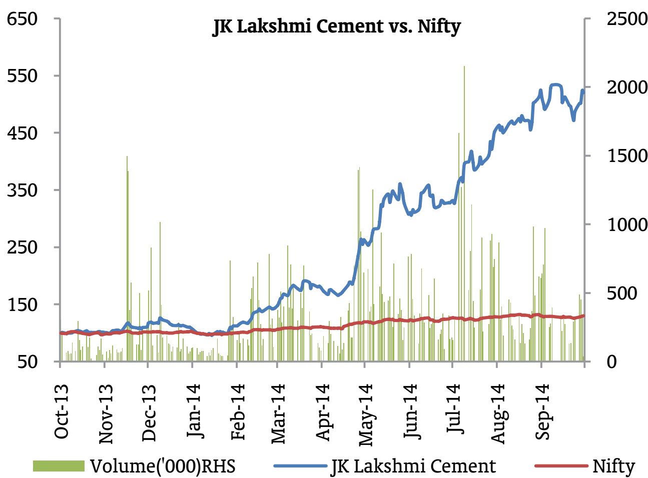




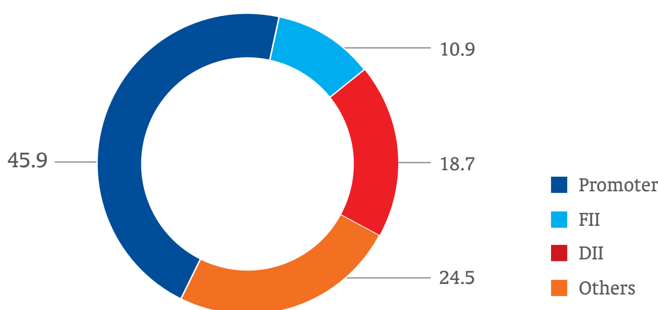
J.K Lakshmi Cement Ltd. CMP: 348/- Rating: Buy TGT: 396/-

Company Information

BSE Code	500380
NSE Code	JKLAKSHMI
Bloomberg Code	JKLC IN
ISIN	INE786A01032
Market Cap (Rs. Cr)	4138
Outstanding shares(Cr)	11.8
52-wk Hi/Lo (Rs.)	369.2 / 62.25
Avg. daily volume (1yr. on NSE)	344,523
Face Value(Rs.)	5
Book Value (Rs)	109.6



Shareholding pattern as of September 2014 (%)



(In Rs. Cr.)	FY13	FY14	FY15E	FY16E
Net Sales	2055	2056.6	2462.9	3153.9
Growth (%)	19.5%	0.1%	19.8%	28.1%
EBITDA	428.7	302.0	428.1	623.9
EBITDA Margin (%)	20.9%	14.7%	17.4%	19.8%
Net profit	187.2	106.0	164.8	235.3
Net Profit Margin (%)	9.1%	5.2%	6.7%	7.5%
EPS (Rs)	15.9	9.0	14.0	19.9

Consensus Estimate: Bloomberg

Company Description

JK Lakshmi cement (JKLC), an ISO 9002 certified company, started its operation in the year 1938 in Sirohi district located in Rajasthan. It manufactures wide range of cement. It is part of diversified JK Group having business ventures in various segments such as paper, tyres, sugar, agri genetics and clinic research. The group has a turnover of Rs 1500 crore. The company has a network of 70 cement dumps and over 2200 dealers spread across the states of Rajasthan, Gujarat, Delhi, Haryana, U.P, Uttaranchal, Punjab, J&K, Mumbai and Pune.

It became first cement manufacturer in north India to introduce colour bags to promote its product. The company's product is chosen for various important projects such as IGNP, Sardar Sarvorar Dam and also by major corporations like L&T, Reliance, Essar and Airport Authority of India. JKLC manufacturing facility has been rated amongst Greenest Cement Plant of India by CSE GRP 2005.

JKLC with installed cement capacity of 5.3mtpa and a CPP capacity of 66MW, which makes it self-sufficient in energy. While the North and the West account for 90-95% of its current dispatch mix, ongoing greenfield expansion of 2.7mtpa at Durg in Chhattisgarh would enhance its presence in the central and eastern markets, raising total capacity to 9.2mtpa by FY15.

Investment Rationale

Near doubling of capacity over FY14-16 to boost volumes

JKLC expanded its clinker and cement capacity in FY14. It achieved this through de-bottlenecking clinker capacity by 0.3mtpa and addition of a 0.6mtpa split grinding unit at Haryana by end of FY14. JKLC 2.7mtpa greenfield cement capacity in Chhattisgarh in eastern part of the country is likely to go live in Q3Fy15. Further, JKLC's 75% subsidiary, Udaipur Cement Works, is likely to commence capacity of 1.4mtpa in FY16. Post this expansion the total capacity of the company will reach 10.0mtpa with this capacity ramp-up. We expect a surge in its volumes along with high realization to improve its top line significantly.

Increase in utilisation in northern and western regions to boost margins

About 90% sales volume of JKLC is from the northern and western regions: JKLC's cement capacities are located in Rajasthan, Gujarat and Haryana: it has 4.2mtpa capacity in Rajasthan, 0.55mtpa in Gujarat and 1.1mtpa in Haryana. The sales mix comprises: 25% sales from Rajasthan, 35% from Gujarat, 8% from Maharashtra, and 32% from other northern states and Uttar Pradesh. Following expansion of capacity in the eastern region, each of the regions is likely to account for a third of sales. We expect improvement in demand growth to boost utilisation and pricing power in the northern and western regions for the next 2-3 years. We believe that infighting in the northern region seen during the major part of FY14 is unlikely to continue and could lead to increase margins.

Realization to improve with revival in demand

Average pan-India cement prices reported moderate growth of 1.8% yoy in 2013-14, owing to a slowdown in demand. The convergence

of high cost/leveraged capacity additions and subdued realizations/ demand has resulted in unfavorable operational economics. However, we expect realizations to improve from here on owing to demand recovery under the stable Government. We have already seen a hike of Rs 30-40 per bag which constitutes ~10% increase in realization.

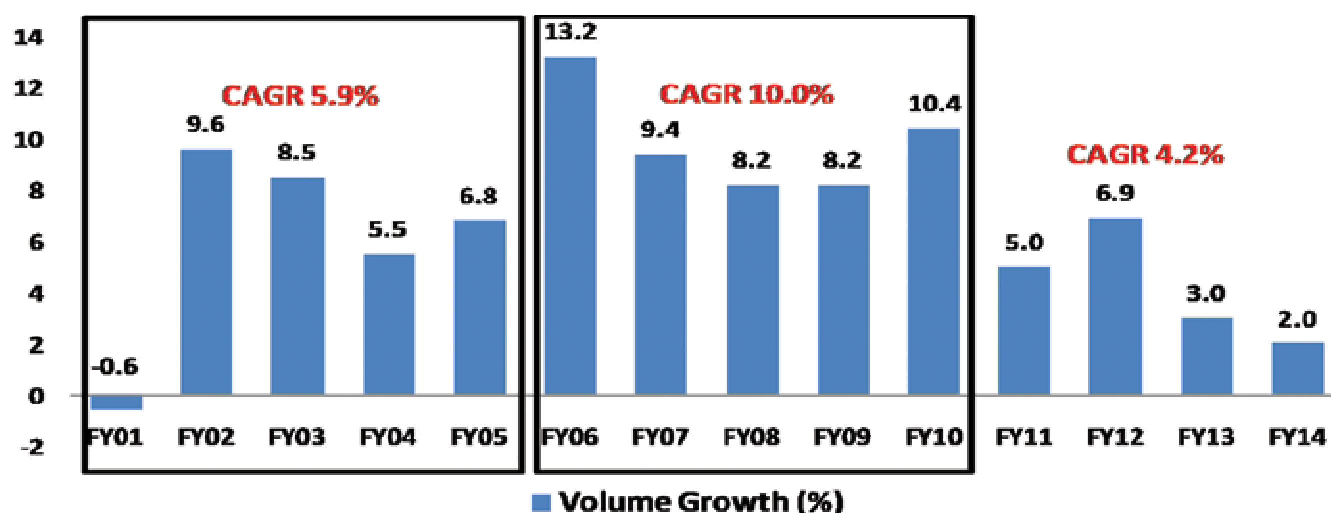
Sector Outlook: Demand on cusp of bottoming out

Lag in recovery to be shorter, given pent-up demand and enabling governance

Worst run for the cement demand in the last two decades, with 4.2% CAGR over FY10-14. Cement demand typically lags GDP growth by 1.5-2 years. Yet, recovery could be faster this time due to high pent-up demand in the system. If stable governance and improving fundamental factors start acting in congruence, normalized cement demand growth of 1.25x GDP could be achieved over FY14-16.

Worst period of cement growth in last 2 decade

Cement demand has witnessed the worst run in two decades over the last 4 years. Demand CAGR over FY10-14 plunged to 4.2% against ~10% over FY06-10. The current period of weak demand is also the longest compared to earlier down-cycles of FY93, FY01, or FY04-05.



Key Risks

- **Input cost pressure:** Historically, cement companies have been able to pass on the rise in input costs to end consumers. However, in a scenario of oversupply, the companies may not be in the position to pass on the increase in input costs. Hence, substantial increase in pet coke prices, domestic coal prices, crude oil and further increase in freight charges can pose downside risk to our estimates.
- **Sharp drop in demand:** Continuing weak demand into next year could adversely impact volumes of the company.
- **Increasing pricing pressure:** With no clear-signs of pick-up in infra projects pricing will be under pressure.

Outlook & Valuation

With strong government at the center, the cement sector will benefit from a potentially faster recovery in the investment cycle, especially in infrastructure. While sector profitability could remain under pressure over the next 1-2 quarters, the long-pending infrastructure projects could be fast tracked by the new government, resulting in a demand recovery and higher profitability in the next two years. JKLC is entering a phase of transformation from a single-region small-cap company to a multi-region mid-cap player. We believe with capacity expansion in place, a strong regional mix and focus on cost efficiency (fuel consumption to decline for per mt of cement); JKLC is poised for the next spurt of growth. With increase in realization due to improvement in demand and better operating leverage would help margins to improve going forward. At the CMP of Rs 348, the stock is trading at 13.2x and 9.1x of its FY15E and FY16E EV/EBITDA respectively. We value JKLC business at 10x FY16E EV/EBITDA (25-30% discount to its average) and arrived at a price target of Rs 396, implying an upside potential of ~14% in 12 months.

ASHIKA

Valuation at a Glance

Sl	CNX100 Company	CMP (Rs.)	Mkt Cap (Rs. Cr.)	Est. P/E FY15	Est. P/E FY16	Est. P/B FY15	Est. ROE FY15	Est. ROE FY16	DPS FY14	Dividend P/O FY14	Dvd Yield FY14
1	Aditya Birla Nuvo	1667.9	21701.4	15.4	12.2	1.9	11.1	13.1	7.0	8.0	0.4
2	ACC	1460.1	27412.7	24.9	18.9	3.5	14.4	16.4	30.0	51.5	2.1
3	Ambuja Cements	221.4	34283.4	23.5	19.7	N/A	N/A	14.4	3.6	43.5	N/A
4	Adani Enterprises	463.8	51003.7	19.3	14.0	2.1	9.8	13.2	1.4	6.9	0.3
5	Adani Ports	263.9	54618.3	23.9	18.6	6.2	23.0	24.1	1.0	12.3	0.4
6	Apollo Hospitals	1089.2	15152.8	39.8	32.1	5.1	11.1	13.7	5.8	25.3	0.5
7	Asian Paints	648.8	62228.0	41.1	33.9	15.4	32.8	34.5	5.3	41.7	0.8
8	Axis Bank	426.8	100720.0	N/A	N/A	2.6	17.6	20.0	4.0	17.5	0.9
9	Bharti Airtel	414.6	165712.2	31.2	23.5	2.7	5.4	9.7	1.8	25.9	N/A
10	BHEL	252.7	61838.6	22.2	20.6	1.9	11.0	8.1	2.7	19.8	1.0
11	Bharat Forge	766.9	17853.0	28.2	21.2	6.7	20.2	23.6	4.5	19.7	0.6
12	Bajaj Auto	2517.5	72846.7	20.1	17.0	7.2	37.1	33.3	50.0	50.1	2.0
13	Bajaj Finserv	1065.1	16948.1	9.9	9.1	1.8	18.0	17.7	1.8	1.8	0.2
14	Bajaj Holidings	1400.0	15581.1	N/A	N/A	1.3	17.8	N/A	30.0	16.8	2.1
15	Bank of Baroda	905.7	38890.0	N/A	N/A	1.0	14.1	N/A	21.5	21.7	2.4
16	Bank of India	271.5	17434.2	5.8	4.5	0.6	10.8	11.2	5.0	12.6	1.8
17	Bosch Ltd	14970.0	47004.2	N/A	N/A	7.5	14.9	N/A	55.0	19.5	0.4
18	BPCL	686.2	49614.4	15.5	13.7	2.6	21.6	15.9	17.0	31.4	2.5
19	Cairn India	277.4	51998.0	5.3	5.4	0.9	23.6	13.9	12.5	19.2	4.5
20	Canara Bank	388.4	17915.3	6.6	5.3	0.6	9.5	N/A	11.0	19.3	2.8
21	Container Corp	1344.9	26222.1	24.0	20.2	3.8	14.5	15.6	12.3	25.2	0.9
22	Cipla Ltd	628.1	50431.5	33.5	25.5	5.0	14.6	16.3	2.0	11.6	0.3
23	Colgate-Palmolive	1722.7	23427.5	N/A	N/A	70.9	159.2	N/A	20.0	62.7	1.2
24	Coal India Ltd	356.5	225178.4	13.5	12.0	5.3	33.3	36.2	29.0	121.2	8.1
25	Crompton Greaves	178.6	11190.6	26.1	16.6	3.1	6.8	15.4	1.2	30.8	0.7
26	Dabur India Ltd	209.4	36778.2	34.3	28.8	13.7	38.5	34.2	1.8	33.4	0.9
27	Divi's Lab	1803.4	23936.6	26.5	22.0	8.1	28.3	27.6	20.0	34.3	1.1
28	DLF Ltd	110.5	19690.3	22.6	14.4	0.7	2.4	4.5	2.0	55.1	1.8
29	Dr Reddy's Lab	3105.8	52889.8	22.8	19.6	5.8	26.3	21.9	18.0	14.2	0.6
30	Exide Industries	156.4	13294.0	20.7	17.8	3.8	16.7	19.8	1.8	28.1	1.2
31	Federal Bank	138.4	11830.6	N/A	N/A	1.7	12.9	14.1	2.0	20.1	1.4
32	GAIL	486.6	61717.8	13.3	12.4	1.9	15.6	13.1	10.4	27.6	2.1
33	Godrej Consumer	914.3	31125.0	34.4	28.1	8.2	21.4	22.6	5.3	23.5	0.6
34	GlaxoSmith Pharma	2700.0	22869.8	44.8	38.4	11.5	24.1	29.3	50.0	87.9	1.9
35	Glenmark Pharma	715.6	19412.8	22.4	18.1	6.5	18.9	24.6	2.0	10.0	0.3
36	Grasim Inds	3388.0	31117.0	14.3	11.1	1.4	10.0	11.4	21.0	9.3	0.6
37	HCL Tech	1496.8	104972.0	14.5	13.0	5.0	37.0	28.8	12.0	20.7	N/A
38	HDFC	1036.8	162694.8	N/A	N/A	4.3	22.9	21.3	14.0	27.5	1.4
39	HDFC Bank	897.3	216625.0	20.2	16.9	4.9	21.6	20.7	6.9	18.8	0.8
40	Hero Motocorp	3083.0	61562.7	23.3	19.4	10.9	N/A	44.4	65.0	61.7	2.1
41	Hindalco	147.4	30426.3	10.7	8.6	0.7	5.7	7.9	1.0	9.5	0.7
42	HPCL	515.9	17468.1	11.5	9.0	1.2	7.8	12.3	15.5	48.6	3.0
43	Hindustan Unilever	720.5	155844.1	38.5	34.5	44.0	123.3	101.8	13.0	71.3	1.8
44	ICICI Bank	1573.1	182063.8	N/A	N/A	2.4	15.2	15.9	23.0	24.1	1.5
45	IDBI Bank	68.4	10963.1	N/A	N/A	0.5	5.1	N/A	1.0	13.9	1.5
46	Idea Cellular	156.9	56411.9	19.6	17.4	3.2	12.8	13.3	0.4	6.8	0.3
47	IDFC	144.2	22931.7	11.5	10.8	1.5	12.6	11.7	2.6	21.9	1.8
48	IndusInd Bank	696.8	36800.4	N/A	N/A	3.7	17.5	N/A	3.5	13.1	N/A
49	Infosys	3803.1	218384.9	17.8	15.9	4.3	25.3	23.4	63.0	39.9	N/A
50	ITC	349.6	278965.3	27.1	23.2	10.2	35.3	35.8	6.0	53.7	1.7

N/A: Not Available

Source: Bloomberg Consensus as on October 27, 2014

Valuation at a glance

Sl	CNX100 Company	CMP (Rs.)	Mkt Cap (Rs. Cr.)	Est. P/E FY15	Est. P/E FY16	Est. P/B FY15	Est. ROE FY15	Est. ROE FY16	DPS FY14	Dividend P/O FY14	Dvd Yield FY14
51	Jaiprakash Associates	29.2	7102.8	N/A	12.6	0.6	-7.2	4.8	0.0	N/A	0.0
52	Jindal Steel & Power	152.6	13956.9	6.5	6.0	0.6	8.7	9.9	1.5	7.2	1.0
53	JSW Steel	1233.4	29814.0	11.2	9.7	1.4	2.2	12.1	11.0	62.7	0.9
54	Cummins India	711.8	19729.7	27.4	21.9	13.3	34.0	N/A	4.7	38.5	0.7
55	Kotak Mahindra Bank	1085.0	83689.8	27.7	22.5	4.4	14.4	15.8	0.8	2.6	0.1
56	LIC Housing Finance	334.2	16865.8	12.2	9.7	2.2	18.7	N/A	4.0	17.2	1.2
57	Lupin	1393.3	62562.7	26.9	22.6	9.0	30.3	27.4	6.0	14.6	0.4
58	Larsen & Tourbo	1567.4	145486.5	29.5	22.9	3.9	13.7	14.4	14.3	26.9	0.9
59	Mahindra & Mahindra	1256.8	78058.9	15.4	12.5	3.2	21.6	18.4	13.5	18.5	1.1
60	M & M Financial	289.5	16465.7	16.2	12.9	3.1	19.3	18.5	3.8	22.6	1.3
61	Mphasis	403.9	8486.5	11.5	10.4	1.7	N/A	14.6	N/A	N/A	N/A
62	Maruti Suzuki	3169.7	95750.3	26.1	19.7	4.5	14.1	17.6	12.0	12.7	0.4
63	NMDC	163.6	64862.8	N/A	N/A	2.2	N/A	N/A	8.5	52.9	5.2
64	NTPC	145.9	120260.1	12.4	11.4	1.4	13.6	11.1	5.8	41.6	3.9
65	Oracle Financial Servc	3208.0	27131.2	18.8	17.0	3.1	16.8	18.8	0.0	0.0	0.0
66	Oil India	598.5	35978.0	9.6	8.1	1.8	14.8	18.3	21.5	43.9	3.6
67	ONGC	394.7	337642.4	10.8	9.2	2.0	16.3	18.0	9.5	30.7	2.4
68	Petronet LNG	194.6	14595.0	N/A	N/A	2.9	15.1	N/A	2.0	21.1	1.0
69	PNB	932.6	33764.8	N/A	N/A	0.9	10.0	N/A	10.0	12.8	1.1
70	Power Finance	277.0	36558.5	5.4	5.6	1.3	21.3	20.4	9.0	21.8	3.2
71	Power Grid Corp	142.1	74314.7	14.0	11.8	2.1	14.9	15.7	2.6	30.9	1.8
72	Ranbaxy Lab	598.6	25414.9	23.8	26.2	7.7	N/A	19.1	N/A	N/A	N/A
73	Reliance Capital	458.5	11261.0	13.7	11.5	0.9	6.1	6.8	8.0	28.0	1.7
74	RCOM	99.5	23903.0	22.4	16.0	0.8	N/A	4.1	0.0	0.0	N/A
75	Rural Electrification	286.0	28241.3	N/A	N/A	1.4	24.7	N/A	9.5	19.8	3.3
76	Reliance Industries	941.4	304489.3	11.8	10.7	1.4	11.8	12.0	9.5	12.4	1.0
77	Reliance Power	71.8	20126.8	19.7	15.9	1.0	5.4	5.9	0.0	0.0	0.0
78	Steel Authority of India	82.3	33969.8	12.6	10.4	0.8	6.2	7.1	2.0	31.5	2.5
79	State Bank of India	2597.8	193944.8	10.9	8.9	1.3	10.4	12.7	30.0	15.8	1.2
80	Shriram Transport Fin	897.6	20363.9	13.9	10.9	2.4	17.1	17.3	7.0	11.7	0.8
81	Siemens	859.2	30596.0	N/A	N/A	7.7	24.5	N/A	6.0	23.5	0.7
82	GlaxoSmithKline Cons	5279.0	22201.1	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
83	Sesa Sterlite	249.1	73835.2	10.6	8.6	1.0	13.9	10.6	3.3	15.3	1.3
84	Sun Pharma	805.2	166765.3	26.9	23.0	9.0	18.7	27.2	1.5	9.9	0.2
85	Tata Steel	450.5	43753.3	10.1	8.4	N/A	N/A	11.2	10.0	28.4	N/A
86	TCS	2457.2	481288.8	22.2	19.1	9.5	43.2	35.8	32.0	32.8	1.5
87	Tech Mahindra	2326.4	54786.5	17.5	14.6	5.9	41.5	26.9	20.0	15.4	0.9
88	Tata Global	156.3	9665.6	22.0	19.2	1.7	9.0	8.2	2.3	29.0	1.4
89	Tata Power	88.5	23922.4	15.2	12.8	1.9	-3.2	11.9	1.3	N/A	1.4
90	Titan Industries	400.8	35582.5	40.7	33.2	14.1	32.7	30.6	2.1	25.4	0.5
91	Tata Chemicals	404.0	10292.2	13.8	11.4	1.8	-17.2	14.6	10.0	N/A	2.5
92	Tata Motors	503.7	151036.6	8.6	7.4	2.5	23.2	22.9	2.0	5.4	0.4
93	United Breweries	698.0	18455.5	65.7	48.9	11.3	14.6	18.7	0.9	10.7	0.1
94	Union Bank of India	228.0	14495.8	N/A	N/A	0.8	9.3	N/A	4.0	15.0	1.8
95	United Spirits	2662.2	38689.2	109.0	58.4	12.8	-114.8	16.1	0.0	N/A	0.0
96	United Phosphorus	336.0	14399.0	12.2	10.4	2.7	19.2	19.7	4.0	18.1	1.2
97	Ultratech Cement	2430.6	66695.1	25.3	18.2	3.9	13.6	16.6	9.0	11.2	0.4
98	Wipro	554.8	136913.1	15.7	14.0	3.7	24.8	22.2	8.0	25.1	N/A
99	Yes Bank	644.0	26794.9	12.5	10.5	3.3	24.9	19.9	8.0	17.9	1.2
100	Zee Enternainment	330.4	31728.4	35.0	28.5	11.7	26.6	22.2	2.0	21.8	0.6

N/A: Not Available

Source: Bloomberg Consensus as on October 27, 2014

Pent-up in demand of capital raised through QIP

Introduction

The oxygen of any business is funds or cash which keeps it going indefinitely as per the Going Concern Concept of GAAP principles. There is plethora of sources from where an organization can raise funds for accomplishing activities of expansion, growth and diversification. These funds could be raised either from domestic market or foreign market. Raising funds from domestic market involves the routed through IPO for equity shares, preference shares and/or debentures; bank loan and finally QIP. Whereas raising funds from foreign market involves the route of ADR/GDR/FCCB. All these modes are highly differentiated in respect to ownership dilution, cost of issue, time of issue, increased liability, more regulations etc.

Current Scenario

The market for initial public offers (IPOs) may not have revved up yet, but companies are raking in the moolah through institutional placements. Fund raising through the qualified institutional placement (QIP) seems to be gaining traction among Indian firms, with total amount mopped-up via this route crossed the Rs 26,000 crore mark this year.

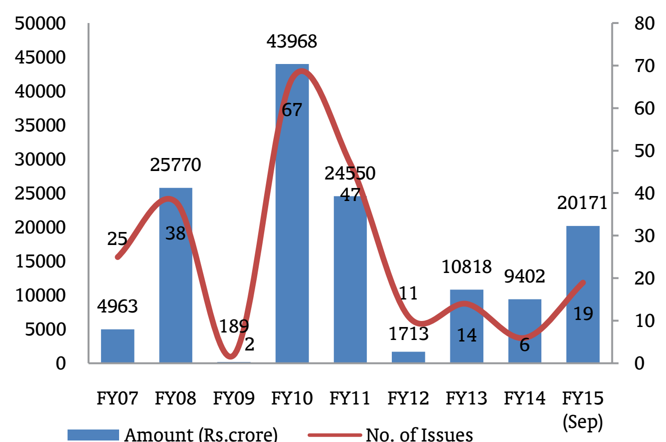
Indian companies have raised a total of Rs 26,354 crore in the first eight months of the calender year, more than double the amount garnered in the entire 2013. This is the highest since 2009-10 when 25 QIPs raised 21,755 crore between April and August. During January-August period of 2014, funds were garnered through as many as 21 QIP issuance.

Return of investor confidence in the equity markets has encouraged some of the large firms to mop-up funds through QIP route. The pent-up demand for capital is now being released and the pipeline for fund raising too is extremely robust. Interestingly, most of the funds were raked in through QIP issuances after the election verdict was announced in May, thus clearly showcasing the revival of investor sentiment, backed by a strong secondary market. Among the firms which garnered funds via QIP segment this year included State Bank of India (SBI), Yes Bank, Idea Cellular and Reliance Communications.

The largest QIP so far in 2014-15 is from Reliance Communications, which raised 4,808 crore, followed by Idea Cellular (3,000 crore) and Yes Bank (2,942 crore).

Fund raising via institutional route dried up between 2011 and 2013 as a rapidly slowing economy put a brake on investments and capacity expansion by companies. It hit a nadir in 2012. Only two QIP issues that raised a mere Rs. 429.4 crore went through in April-August 2012. There was only one IPP that managed to get Rs. 370.5 crore during the period.

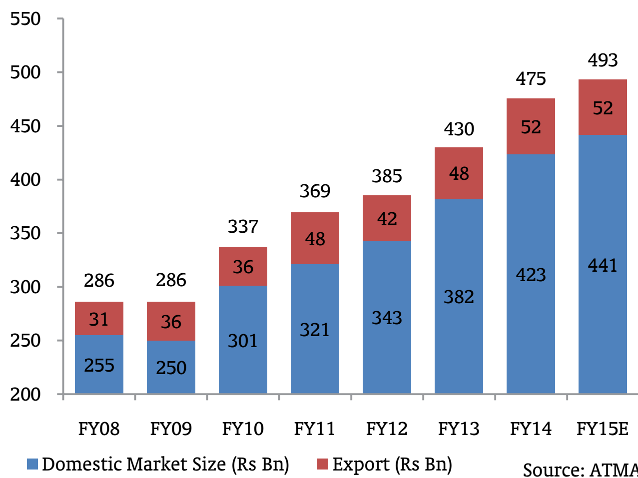
The chart represents the amount of money raised by companies through QIP and the number of issues hit the market in that year. There is a clear pent-up emand for capital in 2014-15 and more so post the new stable government taking helm at the center.



Sector Outlook: Tyres

The Indian tyre industry has reported revival in growth figures, impelled by the rise in the automobile industry led by passenger vehicles and two-wheelers. The Indian tyre industry has appeared as one of the most viable markets in the world and with the appearance of new technology, ultra modern production facilities and availability of raw materials, the sector is poised to grow going ahead. As Indian tyre industry is highly capital intensive, so it is mostly organized and is subjugated by cross ply tyres. Commercial Vehicle (CV), Passenger Vehicle (PV), two and three wheelers, tractor, construction equipment and other off-the-road (OTR) tyres are the various classes of the industry. CV tyre division is the most important demand driver for the Indian market whereas for established markets like North America, PV tyre division works as the key demand driver.

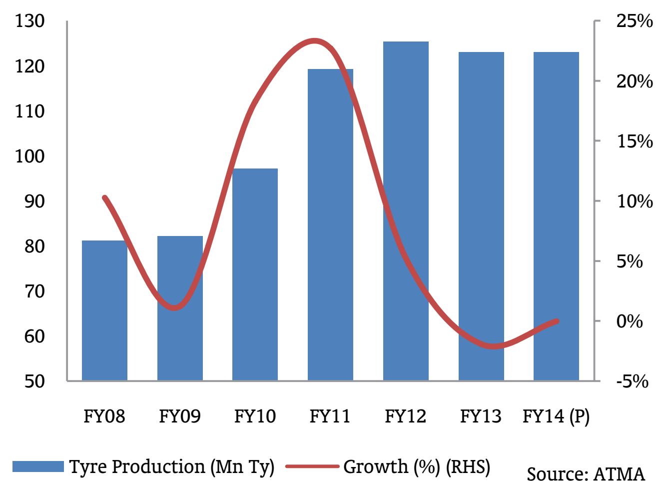
Domestic tyre industry market size



Source: ATMA

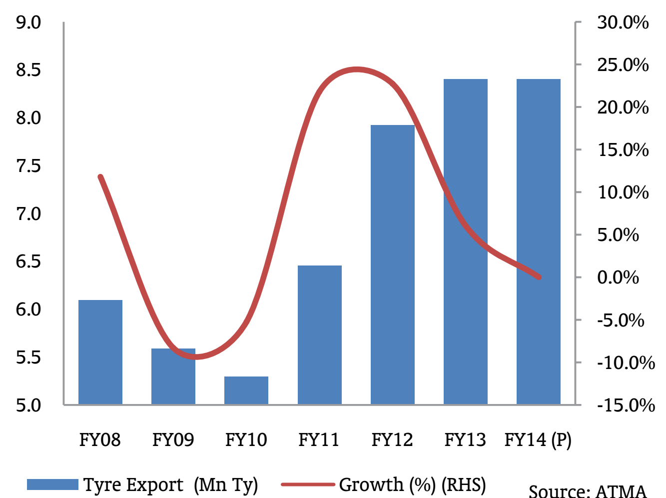
Domestic tyre industry is expected to grow by approximately 8% to Rs. 493 billion during the current fiscal according to the ratings agency ICRA and is expected to achieve CAGR of 11%-12% during the next three years to touch Rs. 623 billion by FY17 with the support of around 6% domestic volume growth. Natural rubber (NR) and crude oil are the major raw material for the tyre sector and fall in these prices will help the companies to improve margin and also it provides headroom for passing on the price benefits to the consumers, however other expenses like inflationary pressure on advertising, employees and some other consumables expenses has increased considerably for quite a few players in the industry over the past two years. Despite the other expenses weight on realizations, for FY15, market expects the notably softer NR prices to filter down into margins, leading to constant and soaring operating margins of 13%-14%. Although the industry has sustained to invest during the past several years, especially towards radial capacities, considerable capital expenditure is expected between 2015-17, with investments for enhancing capacities-both green field and brown field in India and new capacities in other countries like Hungary and Bangladesh. During FY14, tyre demand has grown by a muted 1%, largely supported by two-wheelers and tractors, at the same time as demand from LCV and PV segments cut down. This followed by 2% de-growth observed by the industry during FY13 due to reduction in the high volume two wheeler and tractor segments. Increase in demand for tyres during FY15 is expected to be determined largely by Truck and Bus (T&B), PV and scooter segments. Replacement demand for T&B is also expected to rise as the economic activity in the country revitalizing, thus leading to increased goods movement

Tyre Production trend



Source: ATMA

Tyre Export trend



Source: ATMA

Automotive OEM recovery and improved replacement segment to drive tyre industry demand

It is a well known fact that the growth of the tyre industry is directly linked with the growth of the automobile industry. The latest data of auto sales figures imply the commencement of revival in the auto industry, and this will result into higher order inflow for the tyre manufacturing companies. The tyre manufacturing companies has started getting the advantage of declining rubber prices, and with the increase in auto demand, the industry will have the benefit of both declining raw material price and increasing sales volume growth. Additionally, the replacement market is already giving a good business. As a result the view for the industry is stout going forward. Further the monthly sales data of automobile industry shows a rising trend in demand for the last four months. For the month of August car sales in India jumped by 15.2% to 153,758 units as against 133,513 units in August 2013. With the passage of the festive season, the demand stance turned positive for the industry and to meet the expected increase in demand by the OMCs, the tyre companies have started the process to meet such demand. This can be justified by the latest data from the state-run Rubber Board presenting growing rubber import on the back of increasing overseas purchase of rubber by the tyre makers mainly due to a steep fall in the international rubber prices.

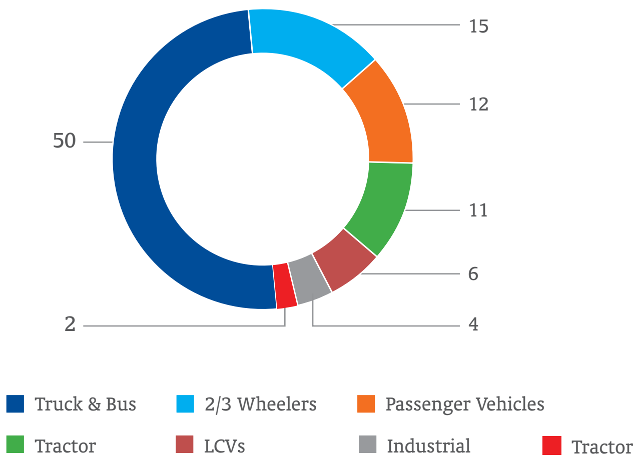
M&HCV segment demand supply gap

	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15e	FY16e
M&HCV population estd. (units)	2,039,819	2,126,216	2,251,493	2,429,770	2,690,081	2,873,689	2,963,928	3,098,118	3,368,306
Avg. tyre per vehicle (units)	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5
M&HCV tyre population in use (in '000s)	15,299	15,947	16,886	18,223	20,176	21,553	22,229	23,236	25,262
OEM sales (units)	274,582	183,541	245,058	322,788	348,570	262,732	196,500	216,150	270,188
Avg. tyre per vehicle (units)	8	8	8.1	8.1	8.1	8.2	8.3	8.4	8.5
Tyres demand from OEM (in '000s)	2,197	1,468	1,985	2,615	2,823	2,154	1,631	1,816	2,297
Replace. demand (in '000s) (~1.5 yrs avg. life)	7,905	8,992	10,327	12,149	13,450	14,368	14,820	16,597	18,713
Annual M&HCV tyre demand (in '000s)	10,102	10,460	12,312	14,763	16,274	16,523	16,451	18,413	21,009
Growth (%)	12.5	3.6	17.7	19.9	10.2	1.5	-0.4	11.9	14.1
Radial M&HCV tyre demand (in '000s)	994	1,258	2,043	2,657	3,255	3,635	3,619	4,235	5,042
Avg. radialisation (%)	9.80%	12.00%	16.60%	18.00%	20.00%	22.00%	22.00%	23.00%	24.00%
Growth (%)	26.5	26.5	62.4	30.1	22.5	11.7	-0.4	17	19.1
M&HCV radial tyre supply ('000s)	394	528	993	1,200	2,200	2,600	3,000	3,500	4,000

Source: ATMA, Industry

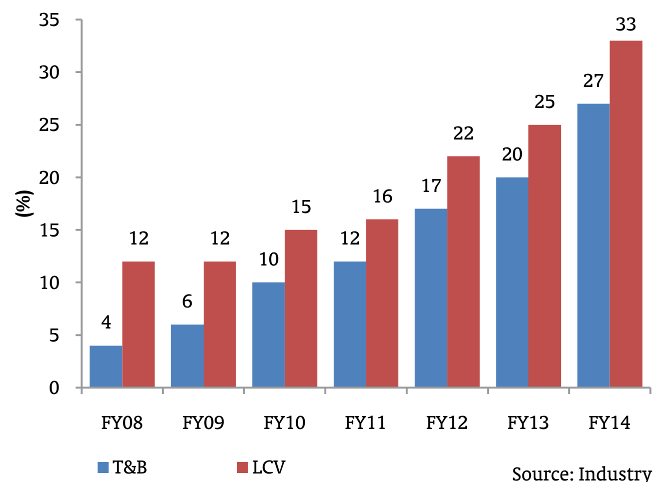
Tyre industry observes lethargic growth in FY14 to about 3%. Lower volumes in the automotive OEM segment (which represent ~30% of the overall demand) and lower replacement sales due to lethargic economic growth impacted the demand. The OEM segment has revealed improvement in the last four months post cut in the excise duties and enhancement in the consumer sentiment after election of stable government. Automotive volumes in the passenger vehicle, two wheelers and the MHCV division have increased by double-digits. Higher demand is expected for tyres during FY15 driven largely by T&B, PV and scooter segments with revival in growth of economic activity. Economic growth showed improvement in Q2FY15 with the GDP growing by 5.7%. However it is expected that the economic growth to improve on back of speedy policy action by the government and improvement in the investment cycle which would boost the automotive OEM volumes. Further, improved fleet utilization due to better economic outlook is likely to boost the replacement segment. Uptick in the OEM demand coupled with strong replacement segment would lead to double-digit growth in tyre demand over the next two years

Segmental demand of tyre (%)



Source: Industry

India's Segment wise Redial Tyre Usage (%)

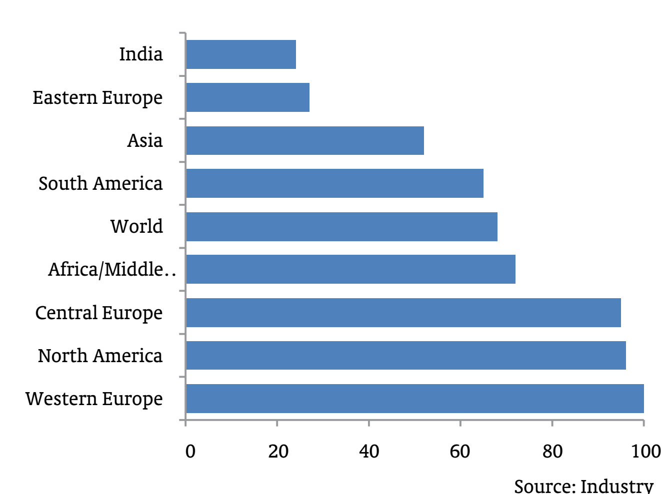


Source: Industry

Move to radialisation tyres the next big growth driver

Mechanically, the tyre industry is divided into two segments, cross ply tyres and the technologically radial tyres. The expansion for radialisation is scattering in the domestic market due to increased acceptance in the commercial vehicle OEM segment which is focusing on launching next generation trucks which demand premium products. Radialisation in the Indian passenger car segment has reached almost 100%; it is currently low in the T&B segment at ~20%, compared to a world average of 68%. With the increasing awareness about the cost-benefit metrics of the radial tyres, it has started gaining momentum in the Indian market. In fact, the tyre industry has earmarked capex of ~Rs60bn over the next 3-4 years mostly for radial tyre capacity. Such investment should lead to strong growth for the industry and in next 3-4 years it is expected to reach 50% levels.

Worldwide Redial Tyre Usage (%)

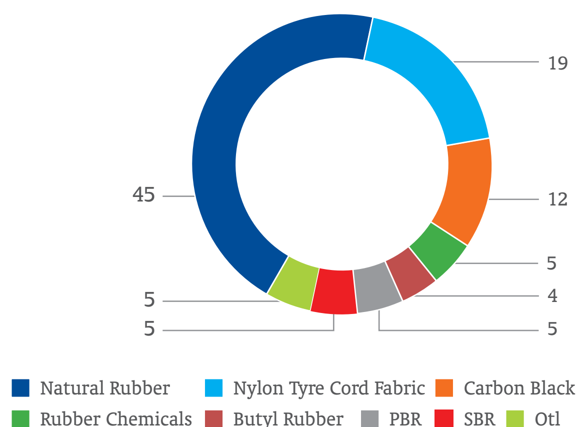


Source: Industry

Sunken rubber and crude oil price – Indispensable for the industry

The Indian tyre industry is highly raw material (RM) intensive, with RM accounting for about 65-70% of the production cost for tyres. The key raw materials used in the manufacturing process are natural rubber (NR, about 45% of the total raw material); and crude derivatives such as synthetic rubber (SR, about 15%); nylon tyre cord fabric (NTCF, 18%); carbon black (about 11%) and rubber chemicals (about 5%).

Raw Material Cost Segregation (%)



Source: Rubber Board

Rubber import increases due to lower production

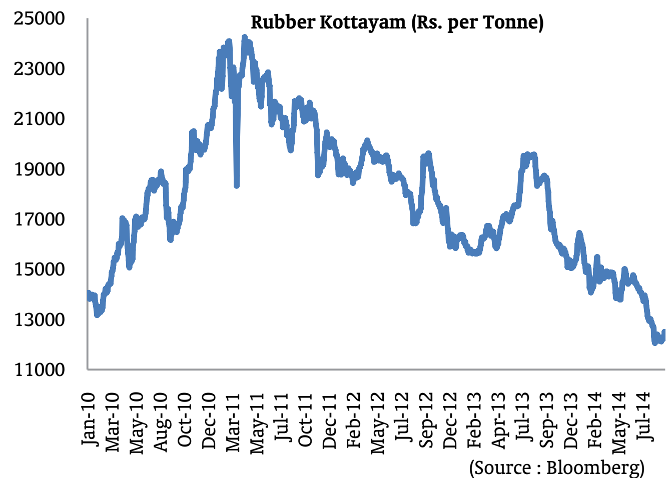
Year	Production	Consumption		Total Cons.	Imports
		Tyre Sector	Non Tyre Sector		Total
2004-05	749660	54%	46%	755400	68700
2005-06	802625	55%	45%	801110	45285
2006-07	852895	56%	44%	820305	89799
2007-08	825345	58%	42%	861455	86394
2008-09	864500	58%	42%	871720	77616
2009-10	831400	62%	38%	930565	177130
2010-11	861950	63%	37%	947715	190692
2011-12	903700	65%	35%	964415	213785
2012-13	913700	65%	35%	972705	217364
2013-14	844000	65%	35%	981520	325190

Source: Rubber Board

Global natural rubber prices under pressure due to oversupply conditions

Recently, global rubber prices have gone into a descending curved with increasing distress on demand-supply inequality. The benchmark Bangkok RSS-4 rubber prices have declined from $2.2/kg in March to ~$1.7 levels. These are five-year low prices. Currently news is coming from the Thailand government that they will sale 200,000 MT of rubber stocks and this has resulted in with more fear in the existing market. On the demand side, global studies and major manufacturers comments imply automotive tyre demand will rise by ~4-5% in volume terms. The international inventory of NR has been gradually increasing. At the end of 2013 the worldwide inventory stood at 2.9 mn tonnes, equivalent to 90 days of demand for NR, up from 41 days in June 2011. This would be divided with demand expanding well in the North American region while Europe and Japan would continue to be lethargic. Emerging markets like India and China are expected to witness a modest improvement.

Domestic rubber price trend

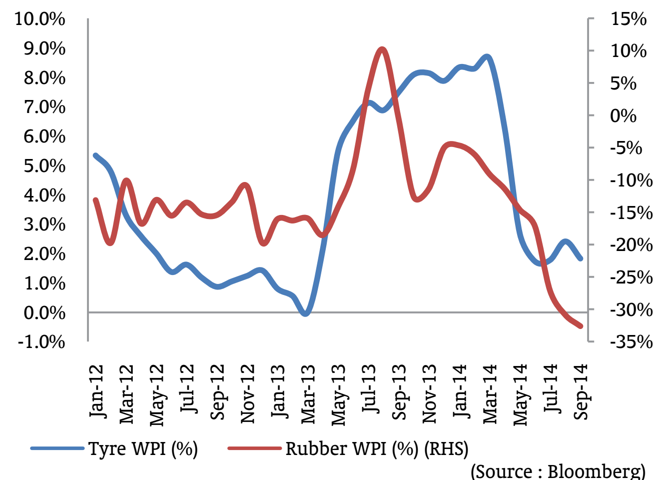


(Source : Bloomberg)

Malaysian Standard Rubber Index

(Source : Bloomberg)

WPI trend of Tyre and Rubber



(Source : Bloomberg)

Lower natural rubber price aid to improve margin for domestic tyre industry

The prices of rubber, which is the chief raw material for the tyre companies, have been on a weakening trend for the last four years. They have dropped from the highs of Rs. 24250 per 100kg in April 2011 to Rs. 12500 per 100kg. The decrease in NR prices in the last six months is due to lethargic global demand particularly from China and surge in the production by Thailand and Vietnam led to fall in price of natural rubber to five years low this in turn has converted into a significant gain in profitability for the tyre companies. The basis for the steep decline in prices is multifold as the local market is in front of a demand slide and imports are higher in the current financial year. The inventory levels have increase over the last two quarters applying pressure on the prices. Rubber prices are expected to stay soft in the medium term given the surplus supply. The spike in the rubber prices had rigorously affected the margins for the tyre companies in Q1FY12. With NR ruling at about Rs. 240 per kg in Q1FY12, the average gross profit margin (GPM) of the industry touched a low of 24.5% whereas it is currently at over 35%. Also the weak NR prices does not led to advantageous for the customers as the companies have to compensated for an increase in the prices of the other raw materials, namely tyre cord and carbon black which would aid in margin improvement.

Advantage of subdued raw material prices is expected to continue for next two years

Globally natural rubber (NR) prices have been under strict stress since mid 2011 as the supply of rubber surpasses the demand. The domestic NR prices, which peaked at Rs. 240 per kg in April 2011, have seen an extended fall and are currently quoting at Rs. 125 per kg after hitting a low of Rs. 120 per kg in Sep 2014. The global demand-supply variance for NR is expected to maintain in 2015 and 2016. The Thailand military government has approved a plan to sell its 200,000 tonnes of rubber and this is expected to hit prices in the short term. Thailand, the world's biggest exporter, normally ships 300,000 tonnes a month. Global prices have fallen 25% this year from a year ago, due to oversupply and worries about a fall in demand from top consumer China. According to experts as reported, the global market is likely to see a surplus for another three years, causing gluts of 652,000, 483,000 and 316,000 tonnes in 2014, 2015 and 2016, respectively. This will ensure that NR prices remain under pressure in the next couple of years. Even though the price of NR is expected to climb from the five-year low level at which it is currently trading, yet no sharp surge is expected in the price. Due to this industry EBITDA margin is expected to increase by 100-120 bps over the next two years.

World natural rubber production and consumption trends (Quarterly)

('000 tonnes)	Q1FY12	Q2FY12	Q3FY12	Q4FY12	Q1FY13	Q2FY13	Q3FY13	Q4FY13	Q1FY14	Q2FY14	Q3FY14	Q4FY14
World NR prod.	2,485	2,997	2,907	2,672	2,734	3,157	3,039	2693	2671	3214	3464	2729
World NR usage	2,731	2,890	2,744	2,694	2,732	2,762	2,838	2678	2886	2911	2881	2811
Surplus/ (deficit)	-246	107	163	-22	2	395	201	15	-215	303	583	-82
Inventory							2320	2334	2119	2423	3006	2925

World natural rubber production and consumption trends (Annually)

Rubber production (000's MT)	2005	2006	2007	2008	2009	2010	2011	2012	2013
Natural rubber	8,921	9,850	10,057	10,098	9,723	10,393	11,230	11,603	12,036
Synthetic rubber	12,025	12,700	13,367	12,738	12,393	14,115	15,073	15,142	15,495
Total rubber	**20,946**	**22,550**	**23,424**	**22,836**	**22,116**	**24,508**	**26,303**	**26,745**	**27,531**
Rubber consumption (000's MT)									
Natural rubber	9,049	9,513	10,133	10,181	9,361	10,773	11,007	11,027	11,322
Synthetic rubber	11,731	12,434	13,087	12,517	12,129	13,984	14,803	14,925	15,483
Total rubber	**20,780**	**21,947**	**23,220**	**22,698**	**21,490**	**24,757**	**25,810**	**25,952**	**26,805**
Supply demand surplus/deficit									
Natural rubber	-128	337	-76	-83	362	-380	223	576	714
Synthetic rubber	294	266	280	221	264	131	270	217	12
Total rubber	**166**	**603**	**204**	**138**	**626**	**-249**	**493**	**793**	**726**

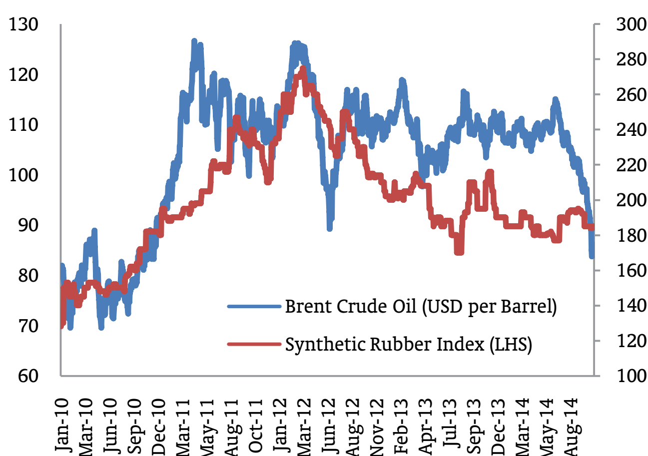
Lift in imports of natural rubber due to lower global price

A revival in demand of tyres by India's auto industry has lifted the imports of natural rubber for making tyres in this fiscal year. For industrial users, imports make sense, as in the Bangkok market price of natural rubber is quoted at Rs 108 a kg for RSS-4. According to latest data of the Rubber Board, during the period between April 2014 and July 2014, the rubber import has increased by 47% to 133,789 tones as against 90,580 tonnes in the same period of FY14. This is for the first time that the import has crossed 100,000 tonnes in four months. While for six month ended September 2014, the import of natural rubber has increased by 24% to 225,652 tonnes. In 2013-14, India imported a record 325,190 tonnes of natural rubber. As per industry estimates, Imports could raise to 400,000 tonnes this year as prices are lower in the world market and demand is rising while dealers say that imports could rise sharply to about 5 lakh tonne this year.

Fall in crude prices could make synthetic rubber more attractive

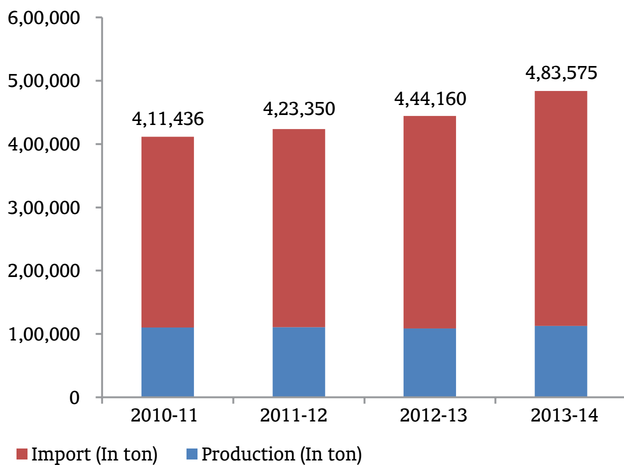
As crude oil prices continue to decline, synthetic rubber -- which is made from a byproduct of crude oil -- is likely to become even more attractive to manufacturers that use the product. Brent crude prices have been heading southward from nearly $115 a barrel in mid-June to just about $85 a barrel, a 48-month low - largely because of rising global supplies from US shale reserves and Libya, and subdued demand due to economic weakness in China and Europe. This prices advantage is likely to tilt the scales even more in favour of synthetic rubber globally. European manufacturers have already shifted to using more synthetic rubber, a trend that is also being seen in major rubber producing countries like India, resulting in natural rubber falling over the past few years. According to estimates, European manufacturers use 60% synthetic rubber and 40% natural rubber while in India the usage ration is 70:30, given that natural rubber is cheaper. The fall in crude prices, however, could change that pattern, especially given the quality of synthetic rubber. In India, natural rubber's share of the market has fallen almost 10% in the past few years to about 70% now. Synthetic rubber prices dropped 15% in Europe and 5% in USA in the second quarter of FY15 from the corresponding period last fiscal. In line with the increased preference for synthetic rubber, data from India's Rubber Board show a 40.1% jump in synthetic rubber production during the April - May period of the current financial year over the same period last fiscal. Production of natural rubber, on the other hand, saw a drop of 7.1% in the same period. Synthetic rubber consumption also increased at a greater pace than natural rubber, going up 5.6% to 84,575 tonnes during April - May period while natural rubber consumption increased only 0.6% to 80,100 tonnes. The mismatch in production and consumption of synthetic rubber has also meant higher imports of the product into India, with 371,839 tonnes brought into the country during 2013-14 whereas natural rubber was 325,190 tonnes.

Price trend of synthetic rubber with crude oil



(Source : Bloomberg)

Synthetic rubber import increases



Capital expenditure plans to resume after better capacity utilization

The tyre industry is currently operating at utilization levels of about 75-80% and expected to reach close to 90% levels by the end of FY15. Given the improvement in the demand, the capacity utilization level is expected to inch up going forward. The truck & bus tyre segment accounts for nearly 50% of the total revenues of the tyre industry. The radialisation levels in the truck & bus segment are significantly lower than the international average. With the increasing acceptance of radial tyres, radialisation in the segment is expected to increase from the current level of 25% to about 40% in the next three to four years. This will result in the existing bias capacity becoming redundant and players investing in new radial capacity. Sufficient capacities in the T&B radial (TBR) segment and the outlook for relatively softer input costs over the next 12 months places the industry in a sweet spot to capitalize on the next demand wave in the automotive industry. The capex cycle is expected to start from FY15-end itself especially towards radial capacities, with investments for enhancing capacities-both green field and brown field in India and new capacities in other countries like Hungary and Bangladesh. The high profitability of the last two years has helped deleverage balance sheets which will help in the expansion plans. In view of the healthy build up in equity base, we also anticipate further project announcements in the industry going forward. Tyre companies have started planning for the next phase of capacity increases. JK Tyre & Industries will be investing Rs. 1,430 crore over the next two years to increase the capacity for truck & bus radials (TBR) at the Chennai plant. For Apollo Tyre, it will be the East European facility capex of EUR500mn in addition to domestic capacity addition, which will impact cash flows. For Ceat, the Rs. 500 cr. capex for brownfield expansion of its Hallol plant, investments in its Bangladesh and Sri Lanka joint ventures, and maintenance capex will push its capital expenditure needs higher in late FY15 and FY16.

Outlook

Indian tyre market is clearly one of the fastest growing markets globally. Strong developments in almost all the major automobile segments would infuse tyre demand in the country in the coming months. Further, tyre manufacturers are ramping up their production capacities to cope with the growing automobile sales. The Indian automobile industry slowdown seems to have hit the rock bottom and things can clearly improve from here.

Industry estimates (ICRA) the domestic tyre industry to grow by approximately 8% to Rs 493 billion during the current fiscal and achieve CAGR of 11%-12% during the next three years to touch Rs 623 billion by 2016-17. The growth will be supported by 6% domestic volume growth even as falling raw material prices will pressure tyre companies to pass these benefits to consumers in the replacement segment. Lower natural rubber (NR) and crude oil prices could provide headroom for passing on benefits to the consumers, inflationary pressure on advertising, employees and some other consumables has increased significantly for several players in the industry over the past two years. Keeping in mind the eventual permeation of radial tyres, tyre manufacturers have committed substantial amount of investments in the past and further expected to have huge capex in FY16 to meet the increasing demand.

As per reports, domestic rubber prices have seen sharpest fall in five years, hitting Rs. 120 per kg. Decline in rubber prices could boost profit margin of tyre firms. Rubber is a key raw material in tyre manufacturing. Also recent steep decline in crude oil prices aided rally in tyre stocks. Nearly 30% of raw material for tyres is derived from crude products. Despite the pressure on realisations, for 2014-15, market expects NR prices to decline significantly and would trickle down into margins, leading to stable and high operating margins of 13%-14%.

Valuation Matrix

	CMP (Rs)	Market Cap (Rs cr)	Sales (Rs cr)	EBITDA Margin (%)	PAT Margin (%)	P/E Ratio (x)	P/E FY15E (x)	P/Bv ratio (x)	ROE (%)	ROE FY15E (%)
MRF	30634	12992	122482	14.9	6.6	16.1	15.3	3.6	24.8	25.3
Apollo Tyres	218	11089	133103	14.2	7.6	10.4	9.4	2.4	25.2	18.8
Balkrishna Inds	744	7187	37719	26.0	12.6	13.1	10.8	3.8	28.4	23.9
CEAT	865	3109	55540	11.9	4.9	10.5	9.1	2.9	29.9	23.4
JK Tyre & Indust	501	2057	76518	12.0	3.4	6.3	5.6	1.9	26.3	22.5
Goodyear India	638	1472	15687	9.4	6.0	15.6	12.0	3.5	24.2	22.1
TVS Srichakra	1067	817	19118	7.8	2.9	14.5	11.7	4.0	30.2	23.5
PTL Enterprises	47	308	2633	24.1	9.2	17.0	14.9	2.7	15.5	13.3
Dunlop India	25	177	0	-4.7	-60.1	N/A	N/A	0.2	-1.1	N/A
Falcon Tyres	24	81	9783	7.6	-5.8	N/A	N/A	0.7	-22.6	N/A

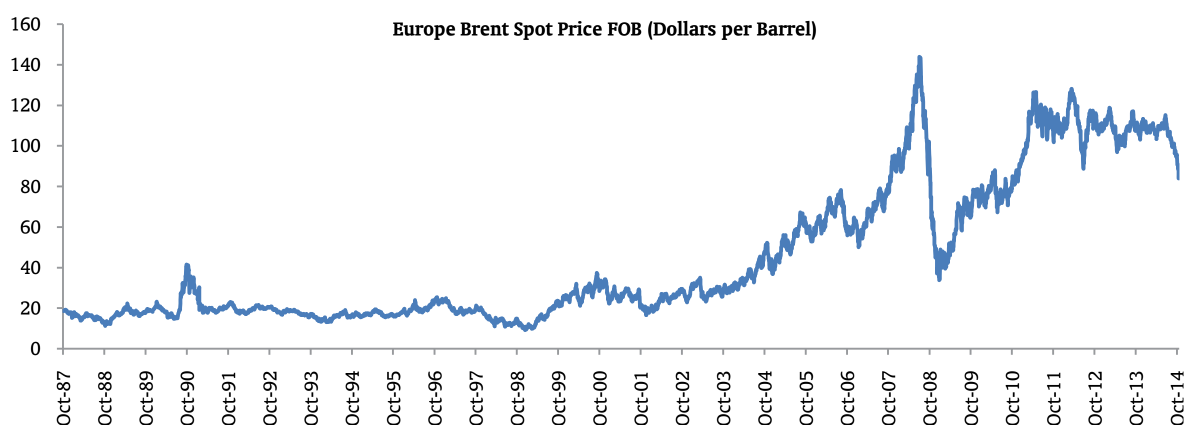
Source: Bloomberg, Capitaline, Ashika Research

Economy Review

In emerging economies, domestic bond yields typically reflect the inflation expectations in the future. The focus is right now on the Indian bond markets considering the prospects of lower inflation in the future. In fact, the situation is befitting if one considers the fall in global commodity prices and particularly crude oil prices. A notable study on the domestic bond yields in emerging economies by IMF highlights, that when global risk aversion is low, domestic bond yields are mostly influenced by inflation and real GDP growth expectations. However, when global risk aversion is high, creditors' are concerned with default risk which takes the center stage, also expectations regarding fiscal deficits and government debt play a significant role in determining domestic bond yields. Every additional percentage point in the expected debt-to-GDP ratio raises domestic bond yields by 6 basis points; and every percentage point expected worsening in the overall fiscal balance-to-GDP ratio raises yields by 30 basis points. These findings have critical implications for India in the backdrop of dwindling crude prices considering that India imports about 80% of its oil. There is a strong negative correlation of 0.9 between Indian stock markets and crude over the long term and against such backdrop the markets gave strong positive return for the past three months post sharp correction in crude..

What's driving the crude prices lower?

The crude oil prices have skidded by ~25% since the high of $115 in June 2014. The decline is believed to be tracking the muted global growth, anticipated hike in the US interest rates thus resulting in dollar strength. Besides, no clear guidance from OPEC about its willingness to curb supply and defend the price also seems to acting as a catalyst. To add to the woes, US is believed to have increased its supply of shale gas. The slowdown of the global growth is however not in best interests for emerging nations like India. Usually in a scenario when global growth concerns resurface, there is a sell-off in the risky assets such as Emerging markets and commodities. The consensus view is that OPEC although not acting now is sure to act soon in the future, if oil prices continue to slid. The reason being simple, the oil producing nations will be adversely affected with worsening fiscal balance and it is surely not in interest of OPEC. Below $90/bbl, only the UAE, Kuwait and Qatar would have budget surpluses in 2015 while Saudi Arabia, Iran, Bahrain will experience budget deficit.



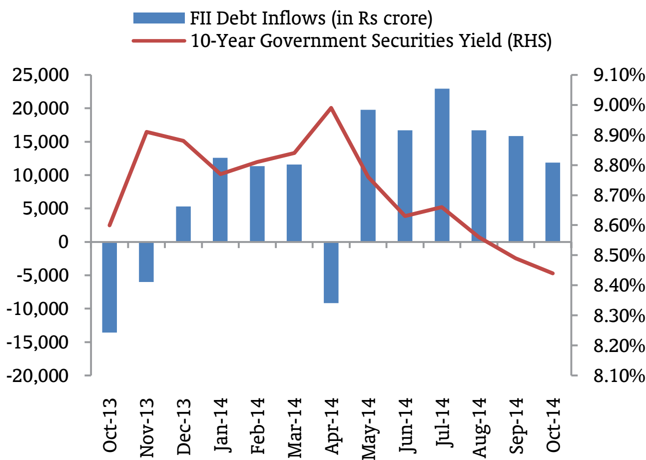
Source: EIA

Lower bond yields in hope of the strong economic recovery, lower inflation

The recent success by BJP in the state elections in Maharashtra & Haryana further instills confidence in Modi led government and the belief that the reform process will continue. Indeed, we believe that the reform process will continue as it is a continuous process. The de-regulation of the diesel and the hike in gas prices are indeed steps in that direction. Further, the preview and the intention to revamp the coal sector norms and streamlining of the auction process promises for more. Lower crude prices throw plethora of opportunities for a crude importing nation like India in terms of lower subsidies, lower inflation & thereby lower fiscal deficit. The rosy expectations in the future are captured by the falling 10 year bond yields for India, which slumped to a 13-month low on October 20th to 8.36%. The bond yields eased despite 10 year bond sale by RBI to the tune of Rs 10,000 crore as part of open market operation (OMO) to suck out excess liquidity.

Although, the equity markets in India are ruling at relatively high levels and have been driven by higher foreign fund flows. However, the foreign institutional investors or foreign portfolio investors (FPIs) are not averse against the bond market either. In fact, for the whole year, FIIs/FPIs have invested to the tune of Rs 1,30,217 crore in the debt market against Rs 80,094 crore in equity markets. Such interest in domestic bond markets instills the confidence in improving economic climate for India, which have been further corroborated by the improvement in the credit outlook for India by S&P. Besides, there is abundance of liquidity at the global level as many economies are going through a slowdown particularly Europe. In such a situation, the general trend among investors is to borrow money at low interest rates (from developed economies) and invest in assets fetching high interest rates (in emerging economies). Further, global commodity prices have softened and investors money is now flowing into bonds.

The expectations on future exchange rates and volatility also looks promising. One-month implied volatility in the rupee, a gauge of expected moves used to price options, slid to 7.30% while one-year interest-rate swaps, derivative contracts used to guard against swings in funding costs, plunged to 8.07%, the lowest since July 2013.



Source: RBI, SEBI, NSDL

Fiscal Deficit to be contained at 4.1% of GDP with certainty

The fiscal deficit in India is capped at 4.1% of GDP for FY15, a target which was a challenge even accepted by the finance minister at the time of presenting the budget. However, with the recent global developments, economists as well as the finance ministry is almost sure to pull it off. Some has even presented a more optimistic figure of 4%. The finance ministry has estimated a far lower subsidy burden on account of oil owing to falling crude prices for the year 2014-15 at around Rs 80,000 crore. Considering that the crude oil prices to be in range of $90-93 per barrel, the subsidy burden on account of oil has come down from a high of 1.39 lakh crore for the last year 2013-14 to around Rs 80,000 crore. Last year, fuel subsidies accounted for 0.8% of GDP and lower crude prices goes a long way to improve the fiscal position of the economy. There is huge boon for the upstream as well as downstream oil companies as they are making profits on sale of diesel to the tune of Rs 3.56 per litre as of 16th October, 2014 against under recoveries earlier. Under recoveries for Q1FY15 stands at Rs 28,691 crore compared to Rs 1,39,869 crore for FY14. Although, diesel prices have been deregulated, OMCs are still losing Rs 31.22 per litre on sale of PDS Kerosene and Rs 404.64 per cylinder on domestic LPG. Usually, crude oil is sold to the Asian buyers at a premium, however, correction in global crude oil has forced Saudi Arabia to sell crude at lowest prices since 2008. Incidentally, most of the oil marketing companies (OMC) in India have recently renewed their contracts in the first quarter of the financial ending September 2014 and many of them are purchasing fresh as well and at a rate favourable to them. Now if we extrapolate the findings in the IMF study earlier mentioned, there is indeed a logical explanation for the lower bond yields as there is an explained negative correlation between the two. Although, the recent move by the government to hike gas prices by ~46% is believed to impact the fiscal balance adversely. Although, the government will gain from higher royalties, profits and taxes, it will be more than offset by increase in higher production cost of urea based fertilizers. The net impact is believed to be ~Rs 25 bn.

Total Subsidy on Petrol, Diesel, PDS Kerosene & LPG by PSU Oil companies (Rs. / Litre / Cylinder)

Year	Petrol	Diesel	PDS Kerosene	Domestic LPG
2005-06	2.34	2.90	12.10	152.46
2006-07	1.63	3.85	15.17	156.08
2007-08	5.27	6.31	16.23	214.05
2008-09	3.29	8.46	24.06	234.88
2009-10	2.90	1.40	14.85	178.13
2010-11	4.64*	4.91	17.39	249.94
2011-12	NA	10.39	26.46	320.30
2012-13	NA	11.26	31.16	427.14
2013-14 (April - December)	NA	8.49	33.12	440.39

*Under recovery on petrol is only up to 25th June 2010.

Source: PPAC

Current Account deficit (CAD) could improve to ~1.5% of GDP

Crude oil accounts for 37% of total annual imports and 67% of the trade deficit. According to calculations by economists, for every dollar decline in crude oil price the trade deficit shrinks by US $1bn (~Rs 6,100 crore) and India's import bill drops by ~ Rs 3,700 crore. Low crude oil further means lesser under-recoveries to be incurred by the oil marketing companies due to selling fuels LPG and kerosene - below cost. The total under-recoveries of the OMCs are set to fall to under Rs. 90,000 crore in 2014-15 from nearly Rs. 140,000 crore last fiscal year. Despite the fact that April-September trade deficit at US $70.4 billion inched closer to the year-ago period at US $76.7 billion, CAD is however expected to decline to ~1.5% of GDP due to softer crude and continuing curbs on gold imports. Calculations by economists suggest, for every $10 per barrel correction in crude oil prices will lead to an annual improvement in the current account to the tune of $10 billion, or ~0.5% of GDP. Thus, the prospects for Indian economy are extraordinary, in the context of global development.

Bigger fall in WPI than CPI

Given the higher share of tradable goods in the wholesale price index, the impact of lower commodity prices is much higher on WPI inflation than CPI inflation. Lower oil price directly impacts 8.6 percent of the WPI basket (crude petroleum and fuels excluding kerosene and LPG) and, additionally, around 5 percent indirectly through lower price of crude derivatives such as chemicals. Thus it is estimated that for every USD 10 per barrel fall in crude oil price lowers WPI by around 0.5 percent and CPI by about 0.2 percent. The recent diesel price regulation and subsequent price cuts by Rs 3.37 a litre is estimated to lower WPI by ~30 bps however, the effect on CPI is expected to be limited, more so with a lag effect. Diesel has a 4.67% weight on the wholesale price index, thus the direct impact is apparent. On the contrary, higher gas prices (following recent gas price hikes by BJP) will impact CPI since public transport has a weight of ~8 per cent on the CPI. However, one also needs to point out that Indians only spend a small proportion of their income on transport. A much larger portion is spent on food (~43 per cent in CPI). A recent RBI study (RBI working paper: Analytics of Food Inflation in India) finds that the persistence of food inflation in recent years can largely be attributed to higher real wages, particularly in the rural sector, which were pushed up further by hikes in the Minimum Support Price (MSP) of rice and wheat, and input cost inflation. The authors of the report expect pressure on food prices to increase once durable traction on economic growth is gained. Apart from growth, there are multiple structural factors that influence food price, which cannot be solved in a year. Thus, it is apparent that unless retail food inflation comes off, there will be little respite on CPI. The WPI has incidentally fallen to a five year low of 2.38% while CPI dropped to 6.46 per cent in September and the target of 8 per cent looks achievable. The Reserve Bank of India has targeted to bring down retail inflation to 8 per cent by January 2015, 6 per cent by January 2016 and 4 per cent by January 2017. The general view from the economists is that if the recent trend continues CPI could be lower by ~1.8% over the next twelve months.

External shocks & India's rising external debt- a risk for rupee

The slowdown in global growth and monetary policy tightening in the US is expected to increase global financial market volatility and strengthen the US dollar. However, India is in a lot better shape in terms of external balance for the economy and as stated above there are chances to reduce vulnerability even further. However, Indian rupee might be susceptible again, more so with the appreciation of the US dollar amid expectations of hike in US interest rates. With Dollar index rising to ~86 levels again, apprehension regarding another bout of depreciation pressure on the Indian Rupee has come back to the fore. India's external debt has risen significantly and is placed at US$ 450.1 billion as of June 2014, an increase of US$ 7.9 billion or 1.8 per cent over the level at end-March 2014. As % of GDP, India's external debt stands at 23%, higher than 22% in 2013 and 20.5% in 2012. India's short term external debt (original maturity), accounts for ~19.5% of total external debt, is comfortable and is unlikely to pose problems in a situation of external shock. Incidentally, the short term component has come down from the figures of 23.9% & 20.2% in June2013 & March 2014 respectively. The two factors which provides confidence are: (a) low short term external debt (original maturity) to FX reserves ratio at 27.8% in June 2014 compared to 29.3% in March 2014 (b) high share of trade credit in total short term debt (residual maturity) at ~72%, which are generally rolled over and do not pose significant risks to the loans component of BoP. Overall, India's external debt is at par with other emerging nations and is not at an alarming situation.

However, the component which is an area of concern is the higher FII investment G-Sec and corporate debt, which has increased by ~USD 14 bn in the current fiscal and the outstanding currently stands at USD 54 bn. This component accounts for ~12% of external debt and in the event of capital outflows amid increase in interest rates in US, poses a larger risk for Indian rupee. With regards to IIF's October 20th 2014 issue, this states that capital flows to emerging markets so far this year have turned out somewhat stronger than what earlier projected, but have continued to be very choppy. According to the report, the period from March to July was marked by a surge in portfolio equity and debt inflows. Since August, however, investors have taken a more cautious attitude towards emerging markets (EM) assets. Portfolio inflows have slowed sharply, dropping to $12 billion in August and $18 billion in September, after an average of $37 billion per month in the period from May to July. Asset prices have followed suit, with the MSCI EM Equity index losing over 8% of its market value since early September and sovereign and corporate bond spreads widening by about 20bp, following a sustained run-up since March. This poses risks for the EM and more volatility may be on the cards.

India's external debt position (US$ Billion)

Memo Items	Outstanding at the end of			Absolute variation		Percentage variation	
	Jun 2013 PR	Mar 2014 PR	Jun 2014 P	Jun-14 over Jun-13	Jun-14 over Mar-14	Jun-14 over Jun-13	Jun-14 over Mar-14
1. Multilateral	51.7	53.4	53.7	2.0	0.4	3.9	0.7
2. Bilateral	24.8	24.7	24.7	-0.1	0.0	-0.4	0.1
3. IMF	6.0	6.1	6.1	0.2	0.0	2.8	0.0
4. Export Credit	17.5	15.9	16.0	-1.5	0.1	-8.5	0.8
5.Commercial Borrowings	135.8	147.6	153.8	18.0	6.3	13.3	4.3
6. NRI Deposits	71.1	103.8	106.3	35.1	2.4	49.4	2.3
7. Rupee Debt	1.2	1.5	1.5	0.2	0.0	19.8	1.9
8. Short term Debt	96.8	89.2	87.9	-8.9	-1.3	-9.2	-1.5
Total Debt	405.0	442.2	450.1	45.1	7.9	11.1	1.8
Memo Items							
A. Long-Term Debt	308.2	353.0	362.2	54.0	9.3	17.5	2.6
B. Short-Term Debt	96.8	89.2	87.9	-8.9	-1.3	-9.2	-1.5

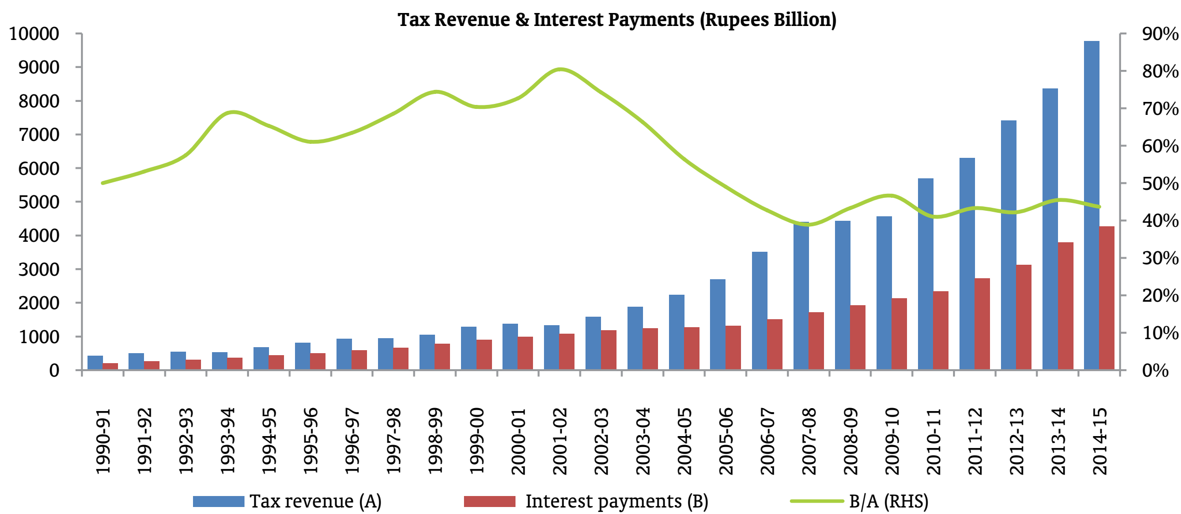
P: Provisional. PR: Partially Revised.

Source: Ministry of Finance, Government of India and Reserve Bank of India

Higher Public debt, interest payments leave little room for fiscal prudence

While India's external debt, even though accelerating, is still at comfortable levels. The public debt has been in an uptrend too and together with it are higher interest payments for the government to service the huge debt burden. Rising interest payments add to government's revenue expenditures, leaving less resource for the use of capital expenditure. Moreover, they are a drag on the present generation as they reflect past consumption and do not contribute to current productive uses and are primarily tax financed. Since tax collection can't be increased and the implementation of GST is still some time away, it is prudent for the government to reduce its dependence on higher debt. Central government's internal debt has stabilised at 48% of GDP in the last two years after declining steadily since fiscal 2005 (following FRBM Act 2003 of the central government), when it peaked at 60% of GDP. The reduction was also attributed to high nominal GDP growth vis-à-vis incremental debt. Including external liabilities, the centre's debt burden is higher at 51% of GDP and the debt burden of centre & states is even higher at 66% of GDP. The reason being apparent that the growth in GDP since FY13 is at a lower rate than the growth in public debt, thus worsening the debt-GDP ratio for India.

However, the growing size of debt levels has resulted considerable debt-service burden and rising interest payments. In FY02, over 80% of net tax revenue to the Central Government was being used for meeting interest payment commitments of past debt. However, with the process of fiscal consolidation (during FY05 to FY08), this percentage came down to about 39% in FY08. Thus, more funds were at disposal for the government for developmental needs. However, following expansionary fiscal policy in FY09 & FY10, to counter the adverse effect of the global recession, the ratio climbed back again at 47% in FY10. Since then, government have been unable to bring down the ratio below 40% and the figure for FY14 stands at 45% and projected at 45% for FY15. During these time frame, inflation remained sticky and thus the average cost of borrowing have been high at 8.3% in FY14 as against 7.6% in FY08, thus causing the debt to grow faster. A RBI research Paper reveals that there is a statistically significant non-linear relationship between public debt and growth, implying a negative impact of public debt on economic growth at higher levels. The threshold level of government debt-GDP ratio for India has been found out to be 61%, i.e., the level beyond which an inverse relationship is observed between debt and growth. However, the actual level of debt is at 66% in FY14, higher than this threshold level. The increased debt service burden is therefore not sustainable in the long-run as it would limit the prospects of fiscal prudence and deployment of funds for key infrastructure.



Source: RBI

Select debt indicators of the central and state governments (as % of GDP)

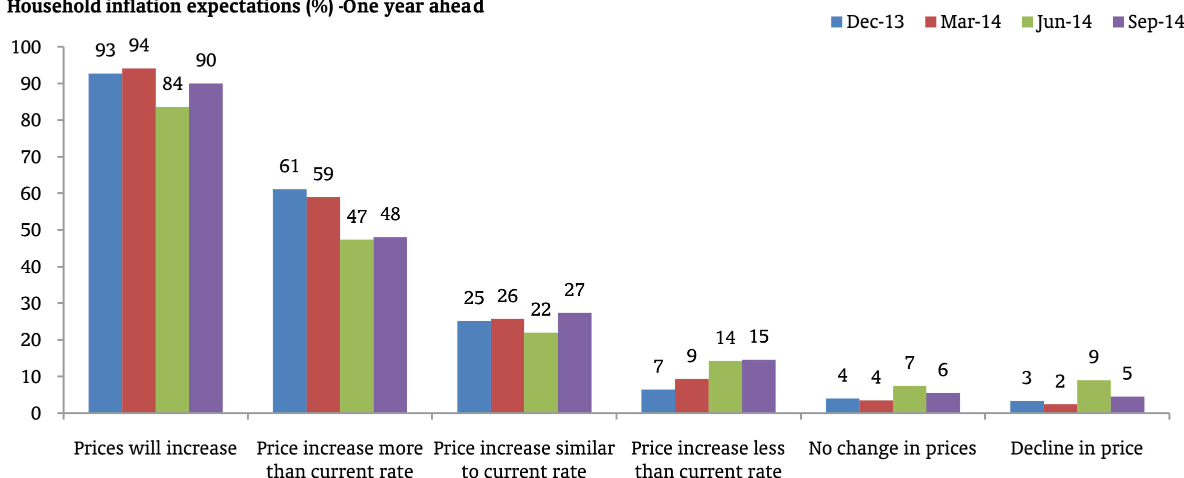
Year	Domestic liabilities of Centre	Total liabilities of the Centre	Combined domestic liabilities of Centre & States	Combined total liabilities of Centre & States
1991-92	47.15	63.42	56.61	72.89
1992-93	46.43	62.05	56.39	72.01
1993-94	48.31	62.65	58.05	72.39
1994-95	46.64	60.27	56.41	70.04
1995-96	45.24	57.34	55.18	67.28
1996-97	43.79	54.32	53.83	64.37
1997-98	45.98	56.24	56.02	66.29
1998-99	46.28	56.14	57.24	67.11
1999-00	47.58	56.81	61.24	70.47
2000-01	50.64	59.36	64.94	73.67
2001-02	54.96	63.44	70.32	78.79
2002-03	59.12	66.85	75.13	82.86
2003-04	59.5	65.98	76.75	83.23
2004-05	59.64	65.53	76.24	82.13
2005-06	58.64	63.9	73.82	79.07
2006-07	56.72	61.4	69.98	74.66
2007-08	54.65	58.86	67.23	71.44
2008-09	53.93	58.62	67.52	72.21
2009-10	52.42	56.27	66.78	70.63
2010-11	48.51	52.08	61.95	65.53
2011-12	48.09	51.68	61.57	65.16
2012-13	48.38	51.67	61.63	64.91
2013-14	47.6	50.9	63.22	66.24
2014-15	46.86	49.81	-	-

Source: RBI

Rate cut? Probably not yet

As inflation abates more so at the wholesale level, RBI is mounted with significant pressure to ease the interest rate cycle. However, Mr. Rajan has made his intentions clear that he will not be influenced by base effect distortions. In fact, going ahead, inflation can be on the rise due to base effect only. The RBI released its first detailed Monetary Policy Report at its September rate review, including its long-term inflation and growth outlook. Growth outlook for the economy as suggested by apex bank is cautious, expecting the economy to expand 5.5% this year and 6.3% in FY16. On inflation, the authorities are confident of meeting the January 2015 target but see upside risks to the early-2016 goal of 6.0%. RBI is expected to maintain its stance to mould inflationary expectations and revert back its inflation fighting capabilities. The RBI is believed to be in a prolonged pause on the policy front for whole of FY15 and only expected to go for lowering rates after the 6% inflation target is achieved next year. Besides, the inflation expectations based on RBI's survey of households suggests higher inflation going ahead. Household inflation expectations in India are mainly influenced by food and fuel. Recent price corrections in both food & fuel should help dampen expectations going forward. However, it will take time for households to alter their current expectations sufficiently to permanently improve the growth-inflation trade-off, which in a way will add to some stickiness to inflation.

Household inflation expectations (%) -One year ahead



Mutual Fund Overview

DSP BlackRock Opportunities Fund - Regular Plan (G)

Equity: Large Cap

Fund Objective: An Open Ended growth Scheme seeking to generate long term capital appreciation and whose secondary objective is income generation and the distribution of dividend from a portfolio constituted of equity and equity related securities concentrating on the investment focus of the Scheme.

Fund Commentary: Around for over a decade, the fund has pleased its investors with its long-term numbers. Its 10-year return is around 20% annualized. Over the past five years, the fund (up 14% annualised) has outperformed the peer group average (up 12% annualized) and the benchmark (up 10% annualised). The fund typically invests about 70-75% in large caps, the balance invested in good quality mid caps. The aim of the fund is to adopt an opportunistic investment approach with aggressive sector and stock positions. The manager implements an unconstrained, benchmark-agnostic approach— the fund's sector weights can deviate by a maximum of 15% (absolute) compared with the benchmark CNX 500's weights. Typically the fund scouts for stocks that have high/rising return on equity (ROE) along with good scalability prospects. While the strategy is primarily growth-oriented, the fund manager also shows a value bias by investing a small portion of his portfolio in companies that trade at close to half their book value.

Important Information

NAV (Rs.)	131.55
Inception Date	April 18, 2000
Fund size(in Rs cr)#	576.18
Fund Manager	Apoorva Shah
Entry load	N.A.
Exit Load	1%, if redeem within 1 yr
Benchmark	CNX 500
Min Investment	Rs. 5000
Min Sip Investment	Rs. 500

as on Sep 31, 2014

Key Ratios

Beta	0.90
Standard deviation (%)	16.45
Sharpe Ratio	0.69
Alpha	2.43
R Squared	92.66
Expense ratio (%)	2.71
Portfolio Turnover ratio (%)	82.00
Avg Market cap (Rs in cr)	41,055

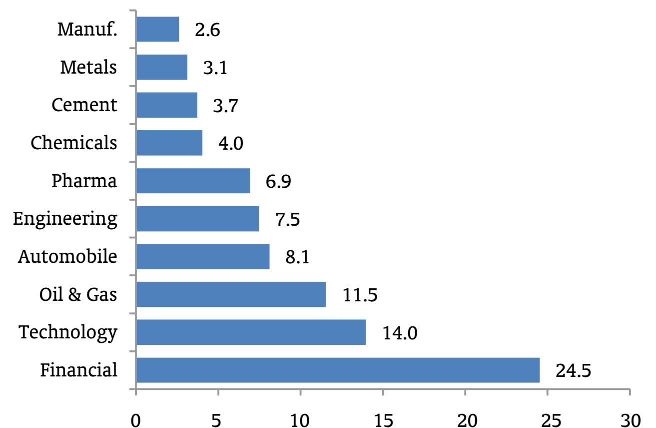
as on Sep 31, 2014

Top Ten Holdings

Stocks	% of Net assets
HDFC Bank	6.05
ICICI Bank	4.78
TCS	4.07
Infosys	3.93
BPCL	3.71
SBI	2.97
ONGC	2.85
Larsen	2.71
Reliance	2.43
Axis Bank	2.35

Asset Allocation

Equity	Debt	Cash & Equiv.
93.27	0.00	6.73



Month of Recom.	Recommended in the Past	Returns till date (%)
Nov-13	Birla Sun Life Frontline Equity Fund (G)	40%
Dec-13	ICICI Prudential Focused Bluechip Equity (G)	39%
Jan-14	Axis Equity Fund (G)	32%
Feb-14	Franklin India Smaller Companies Fund (G)	73%
Mar-14	HDFC Mid-Cap Opportunities Fund (G)	53%
Apr-14	Mirae Asset Emerging Bluechip Fund (G)	46%
May-14	Birla Sun Life Long Term Advantage Fund (G)	28%
Jun-14	Birla Sun Life Infrastructure Fund (G)	8%
Jul-14	HDFC Index Fund - Nifty Plan (G)	6%
Aug-14	SBI Magnum Midcap Fund (G)	11%
Sep-14	ICICI Prudential Value Discovery Fund (G)	3%
Oct-14	Franklin India Prima Plus Fund (G)	4%

Performance Of The Fund

	1 month	3 months	6 months	1 year	3 Years	5 Years	Since Inception
Fund (%)	-1.7	6.8	26.8	41.7	19.1	13.2	20.0
CNX 500 (%)	0.1	3.2	20.5	36.8	16.9	9.5	--

Technical view

Key takeaways from October 2014

- CPI for September came down to 6.46% as compared to 7.8% in August.
- WPI for September stood at 2.38% as against 3.74% in August.
- IIP growth remained subdued at 0.4% in August 2014 compared with 0.5% in July.
- September trade deficit widened to $14.25 billion versus $10.84 billion in August.
- India's export rose to 2.73% to $8.9 billion in September against 2.35% in August due to surge in gold imports.
- BJP witnessed impending electoral victories in Maharashtra and Haryana in the recent assembly election.
- Government deregulated diesel prices and formalized price formula for natural gas and freed the economy from the clutches of fuel subsidy.
- IMF lowered global growth forecast to 3.8% from 4%

Classical theory of Technical Analysis

Indian Equity market maintained its upward trajectory for 9 consecutive months in a row and ended with a gain of 3.25%. Higher high formation in the monthly chart was under threat as Nifty traded below the previous months low and was on the verge of altering the existing uptrend in the market. Volume too in the market got depleted as investors remained uncertain about the future directional movement. As the result season kicks off stock specific movement was eminent with Metals and Real Estate sector constituted the major decline. Slowdown in FII flows remained a major concern during the month. Advance decline ratio remained evenly skewed in favor of both the bulls & the bears. However midcap and small cap index remained resilient to price correction and performed in line with the broader index, hence the correction in the market was majorly attributable from its large cap counterparts. This has been characteristic of every Bull Run and the recent correction can be inferred to be temporary in nature.

Consecutive higher high formation in monthly chart has lead Nifty to trade amidst the rising trendline and the next crucial support level from the said trendline presently seen at 7500. So any meaningful dip towards the crucial trend deciding level needs to be utilized to enter long. However on the daily chart since June 2014 Nifty had been trading within the rising channel formation and fifth leg of the pattern seems to have ended taking support around 7790. Nifty if able to sustain above the said support level might conclude that Nifty have bottomed out and higher target of 8150-8200 can be seen in immediate term. However on the flipside breach of previous swing high of 7780-7790 would be negatively interpreted and lower levels of 7500-7600 can be seen.

Since the start of the month Nifty had been in an intermediate term correction which resulted in to form bullish downward sloping wedge formation in daily chart. Nifty took support from the lower panel of the trendline and provided the necessary pullback. Further Nifty breached past the upper panel of the pattern at 7950 and provided a decisive close above it confirming of a valid pattern break. If the said pattern materializes then higher target of 8150-8250 can be seen.

Hence to sum up though Key benchmark indices witnessed substantial correction during the month it can be inferred that the present correction might be temporary in nature and uptrend in the market is likely to resume. The previous swing low 7500 is likely to act as crucial support in days to come.

Modern approach in Technical Analysis

On the oscillator front Nifty in daily time frame had been trading in oversold price condition with sell crossover while in the weekly time frame also Nifty is in sell mode trading in neutral price territory. Both the time frame had been suggesting downside flap in Nifty however due to its oversold reading Nifty got the necessary push for pullback. ADX is presently trading at its historical low of 20 with buy crossover being initiated after a prolonged two months of sideways consolidation. Based on the present setup in oscillator it can be concluded that correction in the market was expected during the month of October 2013 due to the presence of negative divergence and

hence posed downside risk however the forthcoming month might prove differently as prices seems to have cooled off and pullback is likely.

Band Bollinger study in daily chart reveals that the lower band of the study initiated support around 7700-7730 which Nifty did honored during the month and sustained above it. While in weekly chart the said level of 7730 coincided with the mid band of the study. So, due to the presence of oversold reading in oscillator the Index provided the necessary pullback and hence in order to maintain it upward trajectory Nifty need to provide a decisive close above the mid band in daily chart at 7950. Successive close above the trend deciding level would aim higher till the upper band at 8140-8190 in both the time frame. Onus remains on the positive side in the forthcoming month for Nifty while crucial support is seen at 7700-7730.

Moving average define the broader trend in the market and hence according to the said study longer term outlook in the market continues to remain positive as prices are trading decisively above the longer term average of 100 & 200dma. Nifty took the necessary support from 100dma at 7730-7740 during the month October while the long term average of 200dma is still distant away. The shorter term averages of 20/50 were however acting as major obstacle for the Index around 7950. Hence it can be concluded that Nifty in order to maintain its upward trajectory need to maintain above 7950. In the forthcoming month on the basis of moving average Nifty is presently in a no trading zone and fresh trend in the market would emerge if Nifty trades past the narrow trading range of 7700-7950.

India VIX

Volatility Index is used to measure the market risk or rather used to gauge investors fear in the market. An inverse relation exists between Index with that of the VIX i.e. when prices fall, VIX index rises and in contrast when prices rises VIX fall. India VIX for the past two months had been trading at its historical low level of 15-16 amidst global chaos however during the month on technical parlance India VIX witnessed minor pullback which resulted in Nifty to observe correction. India VIX breached the downward sloping trendline and hence prices sustaining above 18 would be negatively taken by the market and further correction in the market in medium term perspective is eminent.

Gann Theory of Time cycle

According to classical theory of technical analysis a twin fold bullish structural formation might be in the making, first being the breach of downward sloping wedge formation and secondly being the rising channel formation. Both the said formation projects an upside potential till the next crucial resistance level of 8350-8400 in medium term. Nifty since the start of the calendar year had been trading amidst the 23.6 degree angle of inclination. Hence according to W.D. Gann the said angel denotes 1 unit of price change with ¼ unit of time frame. Therefore the said target of 8400 might be achieved within 3.5 months time frame

Calculation:

Current Market price- Projected price= 8400-8000= 400

Now, Time required to complete the target = 400/4=100~3.5 months.

Retracement principle:

As indicated earlier in our previous monthly write up about the crucial resistance level of 8190 emerging from Aug'13 low of 5118 to Dec'13 and projected from Feb'14 low of 5933 of 150% retracement level proved sturdy enough to breach past in the earlier month further on the shorter time frame 38.2% retracement of the entire rise since Aug'14 is seen at 7930 hence it can be concluded that immediate resistance in Nifty in the forthcoming month is seen at 7930-7950 followed by 8190. While on the flipside immediate support in the Index is seen from 23.6% retracement of the euphoric rise since February 2014 till Sept'14 at 7640-7650. Hence it can be concluded that presently Nifty is trapped amidst a narrow range of 7640-7950, breach on either side would dictate the next directional movement in the market.

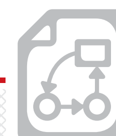
Future Projection – November 2014

5-legged extracting triangle has been structurally developing since October 2013 onward. Presently price structure reveals that Nifty might be unfolding into an elongated zigzag f-leg of the larger diametric pattern and now Nifty need to stay above the trend deciding level of 7600 to reach its higher target of 8400 and then towards its final destination of 9000 in medium term. Failure to do so would induce short term correction towards 7300. Another set of assumption which can be identified in the short term is the newer impulse wave since August 2013 onward. According to the assumption the rally from 5118 till 6343 can be earmarked as wave 1 followed by a correction till the level of 5933 which has been assumed as corrective wave 2 formation. From there onward Nifty unfolded into wave 3 after reaching all time high of 8180. Correction during the month of October ended to form the last leg of corrective decline as wave 4 with a progressive zig-zag formation. Now Nifty is proceeding for its 5 and final leg of the Bull Run towards 8450 or higher.

Inter-market analysis

U.S Market: US market took a breather during the month with a substantial correction. The sell-off came after negative cues from the global front firstly Europe again in danger of tipping into recession and China's growth were far below what the market expected and hence it seems that the 3% growth in the US isn't enough to withstand the ugly global block. On technical front since January 2009 onward DJIA had been in a secular Bull Run taking support from its rising trendline. DJIA took support from the said trendline for the fourth time during the month of October. DJIA if able to sustain above the support level of 15700 would again witness resumption of its uptrend and is likely to trade on a positive note. The worst case scenario which might develop is DJIA consolidating at present level in the forthcoming month. Positive correlation exist between US market with that of Nifty hence DJIA witnessing signs of bottoming out might augur well for the Indian market.

Dollar Index: For last few years the common reason cited by market participant for any asset class appreciation has been the 'flow of liquidity'. To elaborate that it has been the common believe that whenever US Dollar Index has appreciated (i.e. money flowing into US), the stock market across the globe especially the emerging countries like the Brazil, China and India in particular has declined. In other words an inverse relation exists between them. On technical parlance Dollar Index had been surging for the past 3 consecutive month in a row and halted its winning streak in the previous month and ended with a sizable decline. Though the correction was significant but prices were able to sustain above the downward sloping trendline of the broader



symmetrical triangle in weekly chart. Hence presently the support level of 84 would be crucial for Index to head higher. It seems dollar Index would be withstanding the decline and if the inverse correlation exists in the future then domestic market can await further negative surprises in the coming months.

Nymex Crude: Crude oil price continued to decline in the previous month reaching its four year low. The increase in global demand for oil this year is turning slower because of weaker than anticipated growth in China and Europe while oil supplies remain strong leading to growing inventories. On technical front Crude oil breached the upward sloping trendline since May 2010 during the month of August and hence changed outlook in the commodity to negative from neutral. Crude oil prices further breached the 38.2% retracement of the entire rise since 2008 indicating further downside awaited. However on the oscillator front Crude oil presently is trading in oversold price region in both daily and weekly time frame and price consolidation or minor pullback in prices is the most preferred action in technical parlance. Further decline in crude oil prices from present level would act positively for Indian equity market as crude oil constitutes a major chunk of the India's import bill which in turn would help to reduce the twin deficit which had been looming the country's economy for a considerable time.

10 Year Indian Bond Yield: India's 10 year government bond prices rose pushing the yield to its 13-month low on speculation of interest rate cut as lower crude oil price cooled inflation. For RBI inflation had been the major concern and had expressly stated of bringing down the CPI to 6% till January 2016 and hence falling crude oil prices negates upside risk to RBI's inflation target. The boost to bond further came after government lifted diesel price control and raised the cost of natural gas a twin move to reduce the countries fiscal subsidies. Continuous decline in the bond yield has a negative connotation as it might lead to fund outflow from domestic market and seek to yield superior return from other asset classes. The same has been witnessed as there has been a steady decline of FII participation in the Indian market. On technical parlance 10 year bond yield had been steadily declining within the downward sloping channel line and hence outlook continues to remain negative and lower levels of 8.25 can be seen in near term.

10 Year US Bond Yield: US Govt. bond yield slumped as anxiety over the pace of the global growth intensified. Recent economic data amplified worries over deflation fears in Europe and bets on Federal Reserve might not be in a position to raise interest rates until late 2015. Further with mid-term election in November this year and the long awaited victory by the republicans in the senate would rein in budget cuts which in turn would require less debt issuance. With demand for treasuries still in place, less supply would lead to higher prices and lower yield. On technical parlance US 10 year bond seems to have provided a breakdown situation from the downward sloping channel line and hence reinstating of a negative outlook in yield. Declining US bond yield might act positively to Indian equity market as fund inflow to emerging countries can be witnessed.

Indian Rupee: On the back of success for ruling party in two state elections and governments removal of diesel subsidies and hike in natural gas price sparked hopes of additional reforms which supported an upside for the currency. Reformist approach by the government will significantly improve country's finances as the oil subsidy will come down by Rs. 150 bn. Further with inflation coming down would create space for RBI to ease its policy stance and cut policy rate sooner than hitherto believed. On technical front Nifty since May 2014 onward had been trading amidst the rising trendline taking support for a multiple number of times. The elevated trendline support presently seen around 61, inability to sustain above it would drag the currency further lower till the 38.2% retracement of the entire rise at 60.50 and further lower till 60. Further presence of double top formation in daily chart reinstates of a negative structural buildup in the currency. Hence with inflation coming down and growth steadily improving and with expected strengthening of rupee and cut in policy rate would attract huge fund flow.

Summing it up

Positives:

1. Bullish Channel formation Since June 2014
2. Bullish Downward sloping wegde formation since September 2014
3. Rising trendline support since the start of the calendar year at 7700.
4. Buy crossover in oscillator in daily and weekly chart in oversold price condition.
5. Nifty took support from the lower band of the Bollinger in daily chart and breached past the mid band.
6. Nifty trading decisively above all the crucial moving averages notably (20/50/100/200)
7. According to retracement principle narrow range of 7650-7950 has been breached on the upside denoting positive bias.
8. DJIA took support from the rising trendline since January 2009 onward.
9. 10 year bond yield for US also had been declining which might result in fund inflow to Indian equity market.
10. Double top formation in Rupee might lead to further appreciation in rupee.

Negatives:

1. Indian VIX trading at its historical low level and any pullback in the Index would act negatively for Indian equity market.
2. Bullish Symmetrical triangle still remains in Dollar Index and hence might react negatively for Indian equity market.
3. Crude oil prices trading in oversold price region indicating of a possible reversal in trend.
4. India's 10 year bond yield had been gradually declining denoting fund outflow.

To sum up Global equity market were seen tiring after posting decent gains during the year as investors remained skeptical and were trying to gauge the health of the world economy and as regards the overall rally was driven majorly due to abundant liquidity. Further falling crude oil and metal prices owing to lower demand and increasing supply dictates the overall anomaly of what the stock market had been stating and the actual strength of the economy. Concern on end of bond purchase by US Fed by October and interest rate hike by next calendar continued to daunt world economy. IMF too lowered global growth forecast to 3.8% for next year from its earlier forecast of 4% in July further indicates the weakness in the world economy and stated that the euro area faces the risk of recession which lead to a sharp sell across the global market and hence the domino effect too was felt in India. In Europe growth had been weakening as core economies like Germany saw Industrial contraction of 4%, a steep decline since 2009 while concern of Greece on likely default looms. On the Asian front Chinese Finance minister made a statement of no policy adjustment dampened hope of stimulus measure to spur the growth while Bank of Japan maintained its bond purchase at an annual pace of 60 to 70 trillion yen and would continue to unveil more measure to spur growth and in turn is likely to fill the void as US fed unwinds its bond purchase program. Back to Indian equity market started on a negative note after Supreme Court's judgment of all coal-blocks allotted via screening panel since 1993 as illegal as fate of investment done so far in coal blocks lacks clarity. Indian equity market came off sharply during the month on global growth concern and slowdown in FII flows also remained a major concern. The month kick started the result season with Index major Infosys coming with better than expected result with bonus announcement of 1:1 came as a positive surprise which resisted index to trade lower, however on overall basis result so far saw flat growth. Contrary to global fundamentals Indian economy witnessed shrinking Current account deficit due to declining crude oil prices, improving forex reserve and easing inflation which is expected to retain a bullish outlook in the market. Further opposing to global projection, IMF continued to maintain an identical 5.6% growth this year and a higher target of 6.4% in 2015 for India which acted positively for Indian equity market. However bigger boost came after the ruling BJP govt. witnessed favorable Assembly election result in both Haryana and Maharashtra. The recently concluded assembly election will help to push reform measures in Rajya Sabha in the upcoming winter session where the ruling party had just 43 against 68 members of Congress in the 250 members house. Modi led government regained confidence over the promises made for a better government, before election, after coming out with the mother of all reform that included hike in natural gas tariff and decontrolling diesel prices. Going ahead, with the fall in crude oil prices and deregulation of diesel prices will ease pressure on twin deficit and channelize resources to productive asset in medium to long term and would ease inflationary pressure in the economy and hence will leave room for RBI to ease policy rate to spur economic growth. On the technical front Nifty saw its biggest fall since the start of the dream bull run. However it recovered to end the month almost flat with a decline of 3.25%. Stocks underperformed the overall market while Nifty maintains its positive stance therefore individual stocks need to be accumulated for longer term perspective. Seasonality effect propped in as the month of October had the track record of triggering correction even so during the bull period of 2003-2007. The recent correction in Nifty acted favorably in technical parlance with confirmation of twin fold pattern, first being rising channel formation in weekly chart while the second being the bullish downward sloping wedge formation in daily chart. Both the pattern has a positive implication in the market and is likely to pull the index further higher. On the oscillator front due to the presence of oversold reading provided the necessary pullback in the market and hence restore the bullish outlook in Nifty. Further lower band of the Bollinger in daily chart coincided with panel of the channel line indicating of Nifty in a base building mode. On the retracement principle too Nifty breached past the congestion zone and hence direction might have changed to positive. Now resistance lies around 8070 which is the 78.6% retracement of the entire fall from 8160 to 7723, decisive close above would boost the momentum in the market. Other correlated market too had been acting favorably while the bigger boost is coming from the crude oil prices trading at its four year low. The long term uptrend might be under threat only if 7550 level is lost with high volume and vigor participation. Till then Nifty is likely to consolidate with positive bias. In the forthcoming month corporate results, institutional activity, movement of the domestic currency and crude oil prices would be the guiding factors for the domestic markets.

Market Diary

BEST PERFORMERS FOR THE MONTH (CNX 100)

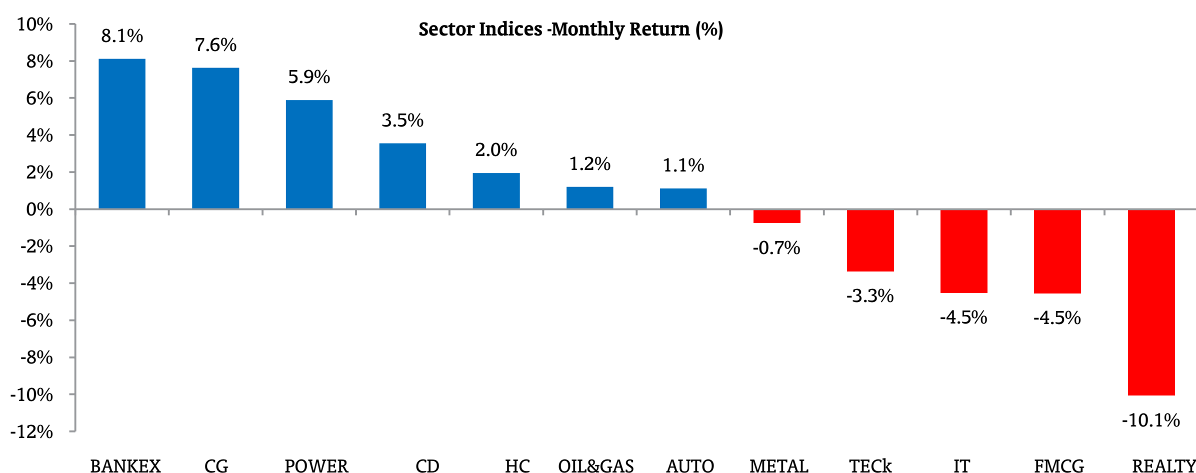
Sl No.	Co. Name	Cl. Price 25.09.2014	Cl. Price 27.10.2014	Cl. Price Var (%)
1	BHEL	203.05	252.7	24.5%
2	SAIL	67.4	82.15	21.9%
3	UNIONBANK	190.2	228.4	20.1%
4	RECLTD	240.5	285.7	18.8%
5	YESBANK	543.9	644.35	18.5%
6	PFC	233.8	276	18.0%
7	INDUSINDBK	611.55	696.35	13.9%
8	CANBK	341.6	387.85	13.5%
9	MCDOWELL-N	2346.7	2663	13.5%
10	FEDERALBNK	122.15	138.5	13.4%
11	AXISBANK	377.85	426.05	12.8%
12	HINDPETRO	458.95	513.45	11.9%
13	BANKINDIA	242.05	270.1	11.6%
14	BPCL	620.3	685.7	10.5%
15	LICHSGFIN	302.2	334.05	10.5%
16	INGVYSYABK	586.35	642	9.5%
17	SBIN	2377.7	2597.8	9.3%
18	LT	1447.1	1566.55	8.3%
19	ZEEL	306.1	330.1	7.8%
20	TATACHEM	373.65	402.5	7.7%

WORST PERFORMERS FOR THE MONTH (CNX 100)

Sl No.	Co. Name	Cl. Price 25.09.2014	Cl. Price 27.10.2014	Cl. Price Var (%)
1	DLF	155.6	110	-29.3%
2	JINDALSTEL	174.9	151.85	-13.2%
3	HCLTECH	1708.45	1495	-12.5%
4	CROMPGREAV	197.7	178.05	-9.9%
5	SSLT	273.2	247.75	-9.3%
6	TCS	2708.6	2458.15	-9.2%
7	CAIRN	303.9	276.5	-9.0%
8	IDEA	170.05	156.4	-8.0%
9	MPHASIS	437.25	403.3	-7.8%
10	GODREJCP	988.65	912	-7.8%
11	DABUR	225.6	208.6	-7.5%
12	ITC	376.65	349.1	-7.3%
13	TECHM	2501.95	2324	-7.1%
14	M&M	1353	1260.4	-6.8%
15	OFSS	3435.95	3208	-6.6%
16	DRREDDY	3310.4	3094	-6.5%
17	HINDUNILVR	759.35	715.8	-5.7%
18	EXIDEIND	165.75	156.5	-5.6%
19	ULTRACEMCO	2574	2435	-5.4%
20	WIPRO	582.55	555.9	-4.6%

(Source: BSE)

Indices Performance 25.09.2014 –27.10.2014



Source: BSE

Commodities - Monthly Round up

"Keep your face to the sunshine and you cannot see a shadow "

Helen Keller

Gold

We all know that currently Gold is one of the worst performed asset class among all the financial instruments. The reasons may be ranging from near zero inflation in the US coupled with the deflation threat in the Euro zone and then comes record high equity markets throughout the globe. But one interesting issue is flaring up in Switzerland which has a potential to change the depressed landscape of Gold. A proposal to prohibit the Swiss National Bank from selling any of its gold reserves. That proposal has sparked jitters in both gold and currency markets. If approved, the SNB (Swiss National Bank) would have to massively bolster its gold holdings, which stood at 1,040 tonnes this month according to the World Gold Council, representing 7.8 percent of reserves. The right-wing Swiss People's Party (SVP) proposed the measure, which would require the SNB to hold at least 20 percent of its assets in Gold. It would also prevent the bank from selling any of its gold, even if the ratio of gold to other assets climbs above 20 percent. To get to 20 percent, the SNB would have to go on a buying spree that could push gold prices significantly higher. It could also endanger the three-year cap on the value of the Swiss franc against the Euro imposed by the SNB to prevent the Swiss currency from appreciating, ward off deflation and boost growth.

If it is adopted, the government would have up to three years to write the proposal into law, subject to consultation with stakeholders. The SNB would then have five years to up its holdings to at least 20 percent. The SVP gold initiative is opposed by the Swiss government, the central bank and several influential parties, and one of the SNB's board members this week again stressed its disagreement with the proposal.

Technical Analysis

At the start of October, market made a low near $1180 which is really a significant support zone for gold. If it was breached then it might trigger more selling into the market. From there onwards market bounced and made a high near $1256 at COMEX. Now weekly chart pattern is showing Bullish Engulfing pattern after $1180 tested by market. Now REVERSAL word doesn't mean that it will change its course from bearish to bullish but that's a possibility and another possibility is that market may enters into sideways condition after some sharp fall. But one thing is clear that until and unless gold breached $1180 area, there is no question of shorting the market.

Again in the weekly chart itself we have a Channel formation whose base is $1180 from where the market bounced. The Channel resistance is now around $1290 in COMEX. So logical traders may opt to long in the market with stop just below $1180 and primary objective to get it near $1280. It's advisable to go long within $1130-1120 range.

Weekly Stochastic is also showing some up move and gave a positive crossover from the oversold region which indicates some bullishness may be a possible in the near term.

In MCX same sort of bullish picture can be seen after prolonged down move. Here the support can be seen near 26400 level. Here the upside is near 28500 level which can be taken as primary objective of the market if the support of 26400 holds. Though weekly RSI is below 50 which is generally taken as bearish reading but some turn around can be noticed. Here also weekly Stochastic is coming out from its oversold area with positive crossover.

Weekly Chart: Gold COMEX Continuous

JPY

Nearly half of Japanese firms think that the government should start defending the yen after last month's dollar high of 110, a Reuters survey shows, underscoring the threat that rising fuel and other import costs pose to a fragile economy. Over the past two years, Prime Minister Shinzo Abe has sought to boost the economy and cure deflation with bold monetary stimulus that has successfully wrought a much weaker yen. But the yen's descent against the greenback to a six-year low of 110.09 on Oct 01 - a rapid 8 percent decline over three months - has prompted a chorus of complaints from companies that Abe's medicine could become poison. While the yen has since regained some ground to around 106 on expectations that the Federal Reserve may put off raising U.S. interest rates, the potential for further weakness is a major concern for many firms.

Technical Analysis

Weekly chart of the pair is showing that in the mid of October it made a Hammer pattern and that's also on the top of 100 Weekly EMA which is itself a good support point for any kind of trending market. And just after the Hammer we have another bullish candle which is confirming the Hammer action. So in the coming days from the chart it's clear that some more upside is left for the pair.

Now 110.70 level is working as a good resistance too as we have one significant swing high in the past and from there only the current rally made a pause. So it's prudent to book profit of longs if any near 110 and wait for some decisive breakout action from the 110.70 area. Our suggestion in this case is to go long near 107.80 - 108.20 range with stop at 106.10 areas (which is again a swing low in daily chart). The whole bullish assumption will be jeopardy if the Hammer low which is 105 is taken out by the market and then the move can take the pair down at 102.50 level.

Weekly Chart: USD/JPY

World Economic Event Calender – November 2014

Monday	Tuesday	Wednesday	Thursday	Friday
3	4	5	6	7
US: ISM Manufacturing CH: HSBC China Manufacturing PMI IN: HSBC India Manufacturing PMI EC: Markit Eurozone Manufacturing PMI	JN: Markit/JMMA Japan Manufacturing PMI US: Factory Orders US: Trade Balance UK: Markit/CIPS UK Construction PMI	US: MBA Mortgage Applications US: ADP Employment Change JN: Monetary Base YoY US: ISM Non-Manf. Composite EC: Retail Sales MoM	UK: Bank of England Bank Rate US: Initial Jobless Claims EC: ECB Main Refinancing Rate UK: Industrial Production MoM UK: Manufacturing Production MoM	US: Change in Nonfarm Payrolls US: Unemployment Rate US: Change in Manufact. Payrolls UK: Trade Balance
10	11	12	13	14
CH: CPI YoY CH: PPI YoY IN: Exports YoY	JN: BoP Current Account Balance JN: Machine Tool Orders YoY US: NFIB Small Business Optimism	UK: Jobless Claims Change IN: Industrial Production YoY US: MBA Mortgage Applications UK: Claimant Count Rate US: Wholesale Inventories MoM	JN: Industrial Production MoM US: Initial Jobless Claims CH: Industrial Production YoY US: Continuing Claims US: Bloomberg Consumer Comfort	EC: CPI YoY US: Univ. of Michigan Confidence EC: GDP SA QoQ US: Retail Sales Advance MoM US: Import Price Index MoM
17	18	19	20	21
JN: GDP SA QoQ US: Industrial Production MoM US: Empire Manufacturing UK: Rightmove House Prices MoM US: Capacity Utilization	UK: CPI YoY US: PPI Final Demand MoM UK: PPI Output NSA MoM UK: RPI MoM EC: ZEW Survey Expectations	US: MBA Mortgage Applications US: Housing Starts JN: All Industry Activity Index MoM US: Net Long-term TIC Flows US: Building Permits	US: Initial Jobless Claims US: CPI MoM US: Existing Home Sales EC: Consumer Confidence US: Leading Index	UK: PSNB ex Banking Groups UK: Public Finances (PSNCR) US: Kansas City Fed Manf. Activity
24	25	26	27	28
UK: Nationwide House PX MoM US: Markit US Services PMI US: Dallas Fed Manf. Activity US: Chicago Fed Nat Activity Index JN: Small Business Confidence	US: GDP Annualized QoQ US: Consumer Confidence Index US: Richmond Fed Manufact. Index US: Personal Consumption US: Core PCE QoQ	US: Initial Jobless Claims UK: GDP QoQ US: MBA Mortgage Applications US: Durable Goods Orders US: New Home Sales	EC: Consumer Confidence EC: Economic Confidence EC: Business Climate Indicator	JN: Industrial Production MoM JN: Tokyo CPI Ex-Fresh Food YoY EC: CPI Estimate YoY IN: GDP YoY EC: Unemployment Rate

IN: India, US: United States, EC: European Union, UK: United Kingdom, CH: China, JN: Japan

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CIN No. L67120WB1994PLC062159

Ashika Global Securities Ltd.
(Formerly Known As Ashika Global Securities Ltd.)

(RBI Registered NBFC)
CIN No. U65929WB1995PLC069046

Ashika Capital Ltd.

(SEBI Authorised Merchant Banker)
CIN No. U30009WB2000PLC091674

Ashika Stock Broking Ltd.

(Member : NSE, BSE, MCX-SX, Depository participant of CDSL / NSDL)
CIN No. U65921MH1994PLC171897

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