

## Opportunity lying outside the index

Who says Black swan events always have a negative impact? They can also work well on the positive side, as is the case of the outcome of the Indian general elections. Who could have predicted the clean sweep by the UPA in the elections? However, the UPA is indeed about to form a government at the Centre with the Indian National Congress being the major political party in the coalition with 206 seats.

Much to the consensus relief, the new government formed will not need the support of the Left and the alliances of local regional parties, which would have otherwise impacted the decision making process of the government had they been party to the coalition. This will indeed send huge positive signals to the economy and the capital markets.

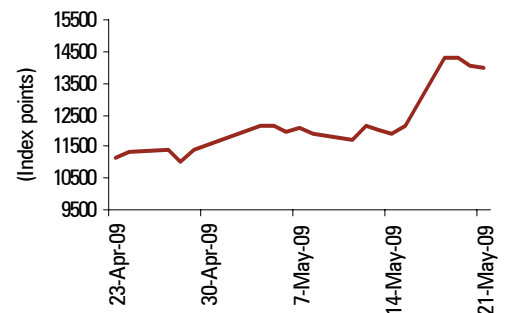
**So, the big question that remains is where does the market head from here?**

In our recent strategy report, we had mentioned that if the election results are favourable then the markets may reach 14500 levels on the upside in the short run. It did that within two trading sessions after May 16 2009. However, on the first day when markets opened, within a few seconds, for the first time ever, the market hit the 15% upper circuit followed by an additional 5% rise. This gave no chance to the investors to buy into the markets. As large caps have rallied substantially, mid caps soon followed suit. Since the substantial appreciation in large caps has created a huge valuation divergence between large caps and mid caps, the ongoing run in the mid caps is simply a case of catching up.

We believe that within the midcap universe only quality midcaps will witness sustainable buying interest. Within this segment, PSU banks, private regional banks, power companies and high leveraged plays will be preferred. In addition, we are of the view that one should view any deep correction in the markets as an opportunity to accumulate quality stocks at reasonable valuations.

However, one thing is for sure. This black swan result has indeed increased the visibility of the India growth story in front of the international investor community. Now, on the back of expectations of better policy reforms, increased focus on fiscal deficit and high probability of PSU divestments and prudent & speedy executions related to the important bills like that of FDI in insurance will result in increased FII participation in India.

Movement of BSE in May 2009



### Key expectations from the new government:

- Improvement in fiscal management/public finances via disinvestments
- Increased focus on infrastructure spending especially power and road/highways.
- Thrust on agriculture and rural development
- Financial sector reforms like increasing FDI in retail and insurance sector
- Increased focus on education and healthcare
- Providing ample liquidity to corporates and individuals at affordable rates

We believe the above factors will help in bringing fresh capital into the country in terms of FDI, FII flows and ECB flows

### Key Beneficiaries

- Insurance plays like SBI, Kotak Mahindra Bank and Reliance Capital
- Infrastructure plays like Bhel, L&T, NTPC etc.
- PSU banking stocks with trigger of government stake dilution for example: OBC, Dena Bank, etc.
- PSU space will be in limelight on expectations of divestments and new IPOs

## Sectoral impact: Who wins and who wins a little less...

Sector	Likely triggers	Key Beneficiaries
<b>Automobiles</b>	<p>Possible tax cuts in excise for different segments in passenger vehicles</p> <p>Levy of import duty on cheap imports in the form of knuckles, auto axle, forgings and truck radials from China</p> <p>Extending credit availability to rural and semi urban market effected through rate cuts</p> <p>Infrastructure investment and flexible labour laws</p>	<p>OEMs like Maruti, Honda Siel, M&amp;M, Tata Motors, etc</p> <p>Auto component makers</p> <p>The whole automobile and auto ancillary industry</p> <p>The whole automobile and auto ancillary industry</p>
<b>Banking &amp; financial services</b>	<p>Possible FDI increase in insurance, which is currently at 26% to 49%</p> <p>Revival of credit demand in system and lower risk</p> <p>Govt. may dilute stake in certain PSU banks where there is need of capital. (plan of reducing present requirement of min. govt stake from 51% to 33% may also be looked at)</p>	<p>Positive for banks or NBFCs having insurance business like HDFC, SBI, Max New York Life, Reliance Capital, Kotak Mahindra Bank, Bajaj Finserv</p> <p>This should help the banking sector due to higher credit growth and only moderate rise in NPAs</p> <p>OBC, Dena, SBI, Andhra Bank</p>
<b>Metals</b>	<p>Among metals, the steel sector would indirectly benefit from the government's continuous focus on infrastructure development in terms of demand growth</p> <p>Without any Left element the new government is likely to go for some divestment of some of the entities</p>	<p>SAIL would be biggest beneficiary being a PSU. Also, JSW Steel because of its domestic market focus and efficiency would be key beneficiary</p> <p>Bharat Aluminium (Balco) &amp; Hindustan Zinc</p>
<b>Telecom</b>	<p>Rationalisation of spectrum fees</p> <p>Possible IPO of BSNL</p> <p>More thrust on rural expansion</p> <p>Increase in base price of 3G Auction</p>	<p>Across sector - Positive (more for GSM players)</p> <p>Across sector Negative — GSM Players</p>
<b>Media</b>	<p>Possible FDI increase in media Currently - radio - 20%, News broadcasting - 26%</p> <p>General broadcasting - 29%, DTH - 49%</p>	<p>NDTV, TV 18, DISH TV and Wire &amp; Wireless</p>

	Allowing news on private FM channels	ENIL, Sun TV,
<b>Power</b>	Possibility of disinvestment in major companies	NTPC, Neyveli Lignite, PowerGrid
	Speed-up of reforms on the regulatory front	NTPC, PowerGrid, Suzlon, Bhel
	Speeding up issues on the nuclear deal	BHEL, L&T, Alstom, Areva T&D
<b>Retail</b>	Reforms expected, which would boost investment in the sector	Positive for Pantaloon Retail, which has just restructured its business. The reforms would enable higher flow of capital, which would enable rapid scaling up of business operations.
<b>IT</b>	On the positive side, infrastructure development would lead to creation of additional IT parks. Extension of tax benefit beyond March 2010 would be the key trigger	Across sector
	Greater emphasis on e-governance projects	3i-infotech
	Higher thrust on education also likely	NIIT
	Overall, higher money flow may lead to rupee appreciation key negative for the sector as a whole.	Across sector

Source: ICICIdirect.com Research

## ***A stable government after so many years...***

**Stable government:** This is the first election after 1984 when a single party has won more than 200 seats: This outcome has paved the way towards a stable UPA government at the centre, which would be crucial for the execution of progressive policies. The government would be aggressive on reforms (banking and pension) and divestment of government's stake in PSUs, which would help in controlling the fiscal deficit.

### **Left debacle & regional party's failure to raise expectations: smooth governance**

The formation of a new government without Left parties influence would eliminate the major barriers in policies like allowing foreign investment in sectors such as insurance, retail and aviation, which earlier the communist parties objected to.

### **Speed-up in economic reforms**

Implementation of policy reforms and divestment of government's stake in PSUs would not only help in controlling the fiscal deficit but would help in increasing the governments spending on infrastructure, which would attract more FDI and increase the visibility of the India growth story to the international community.

### **Smaller but strong coalition: hassle free governance**

UPA		NDA		Third Front		Fourth Front	
INC	206	BJP	116	BSP	21	SP	23
Trinamool Congress	19	JD(U)	21	CPI-M	16	RJD	3
DMK	18	Shiv Sena	11	BJD	14		
NCP	9	RLD	5	AIADMK	9		
JMM	2	Shiromani Akali Dal	4	TDP	6		
Others	7	TRS	2	Others	6		
		AGP	1	CPI	4		
				JD(S)	3		
<b>Total</b>	<b>261</b>	<b>Total</b>	<b>160</b>	<b>Total</b>	<b>79</b>	<b>Total</b>	<b>26</b>
						<b>Others</b>	<b>17</b>

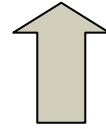
### **Key portfolios**

The Congress party-led UPA government won 261 seats out of 543 seats, which would pave the way forward for a clear majority for the government. The Congress party became the single largest party with more than 200 seats. It is likely to hold key portfolios in the government, which would result in smooth functioning. This would also avoid any conflict with allies on key policy issues. The key portfolios, which are likely to be held by the Congress, are Finance, Home, External Affairs, Commerce and Oil & Gas.

## Where did Congress/UPA buck the trend?

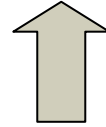
### Tamil Nadu

One of the big surprises was Tamil Nadu's result where DMK + Congress alliance won 28 out of 39 seats. The major factor of this win has been 12% vote earned by DMK, which came third in most of the seats and ate up AIADMK's vote share.



### Andhra Pradesh

Andhra Pradesh is another state, which threw a positive mandate for the UPA. It has not only sustained its 2004 performance, but exceeded its tally to 33. Another debutant party *Praja Rajyam* has benefited the Congress in the state as it has cut the votes of the Third Front (TDP + TRS + Left).



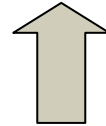
### West Bengal

West Bengal's election results were a big boost for the UPA as Left parties faced its biggest defeat in 30 years. Left parties have gone down from 35 seats to 15 seats and the major beneficiary was the Trinamool Congress that significantly improved its tally from one to 19.



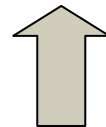
### Uttar Pradesh

The largest state in the country saw a dramatic change in the region's polity. The Congress party, which was fourth largest party with nine seats in 2004 elections, won 21 seats in 2009 elections. Congress' win, at the expense of BSP and SP, has reduced the influence of regional parties in the national politics, which would help the government in executing progressive policies.



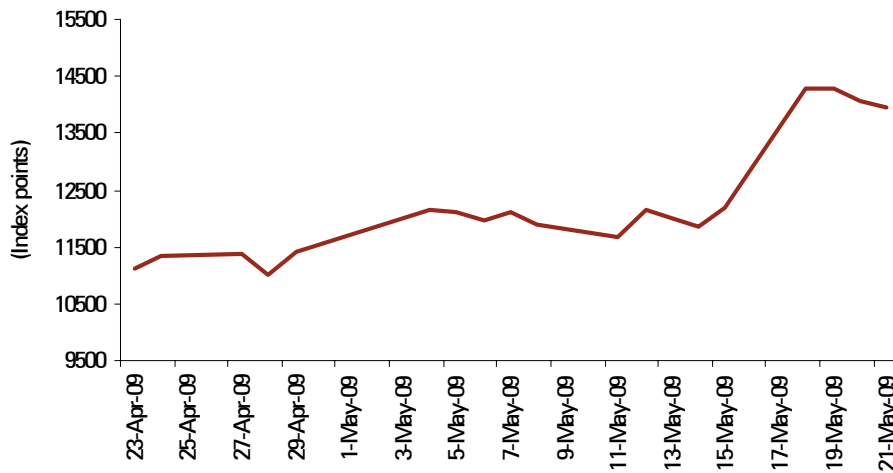
### Rajasthan

Rajasthan became a major contributor to the UPA's number after the Congress won 20 out of 25 seats in the state. After the Assembly election win by the Congress, a benefit to the Congress in parliamentary elections was likely. However, a clean sweep by the Congress was one of the surprises.



## ... Leads to significant re-rating of the markets

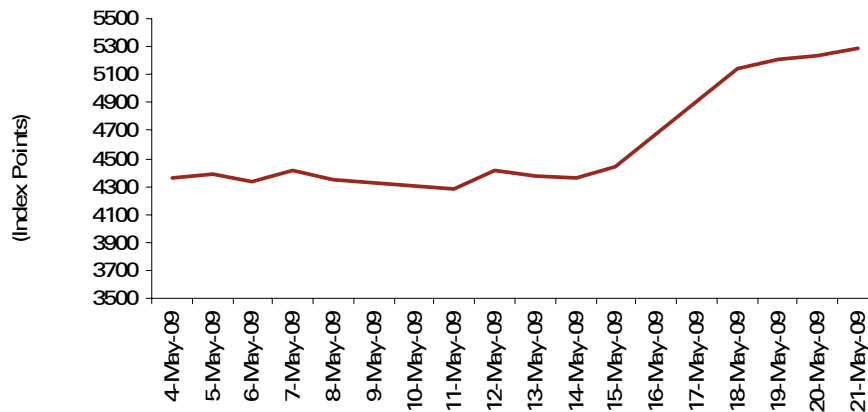
**Exhibit 1: Movement of BSE Sensex in May 2009**



**The BSE Sensex created history on May 18 2009 when the index after a few seconds of opening hit the upper circuit of 15% followed by additional 5% rise on the same day**

Source: Bloomberg.com, ICICIdirect.com Research

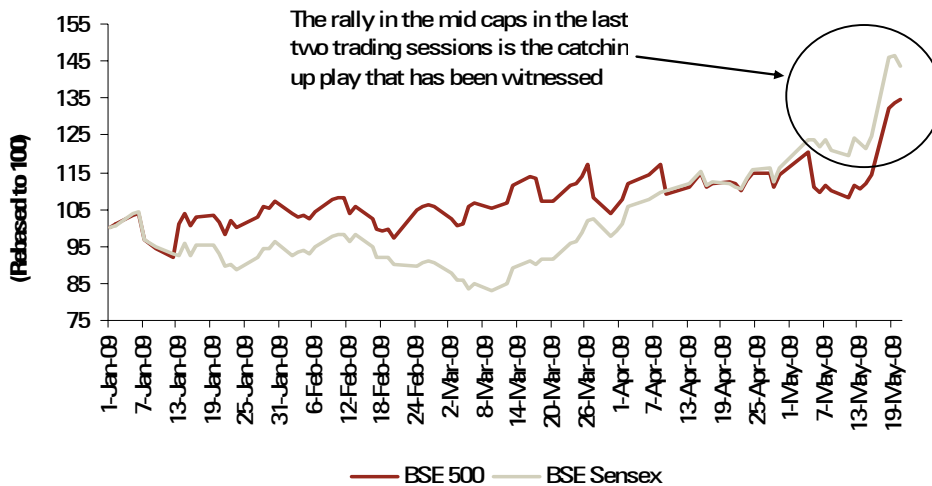
**Exhibit 2: Movement of BSE 500**



**The BSE 500 rallied significantly from May 18 2009 till date, thereby delivering 20% returns in four trading sessions.**

Source: Bloomberg.com, ICICIdirect.com Research

### Exhibit 3: Large caps have significantly outperformed mid caps



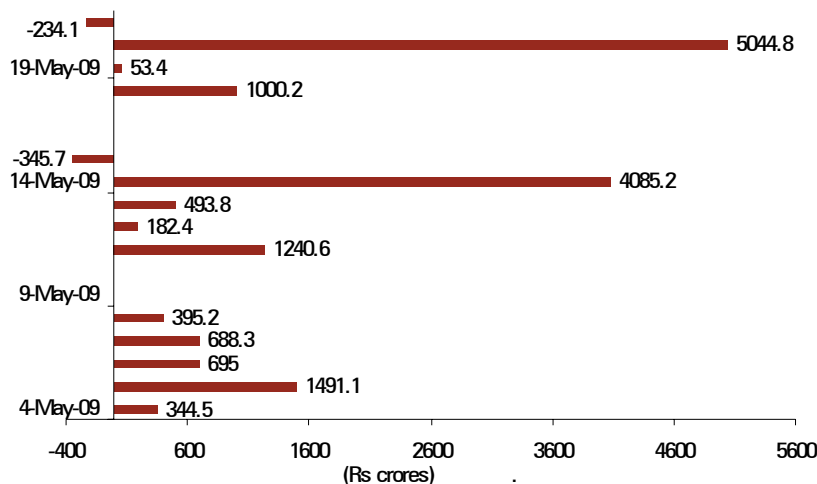
Source: Bloomberg, ICICIdirect.com Research

As the large caps have rallied substantially, the suit was soon followed by mid caps. Since the substantial appreciation in large caps have created a huge valuation divergence between the large caps and the mid caps, the ongoing run in the mid caps is simply the catching up by the latter on the valuation front. We believe within the mid cap universe only quality mid caps will witness sustainable buying interest. Within these segment PSU banks, private regional banks, power companies and high leveraged plays will be preferred. We are of the view that any deep correction in markets should be viewed as opportunity to accumulate quality companies at reasonable valuations

Apart from the Mid cap banks, infrastructure and power companies we also like high leverage companies who will now find favourable environment to raise capital and bring their balance sheet gearing under control.

### Sentiment of FII flows has provided steroids to the markets

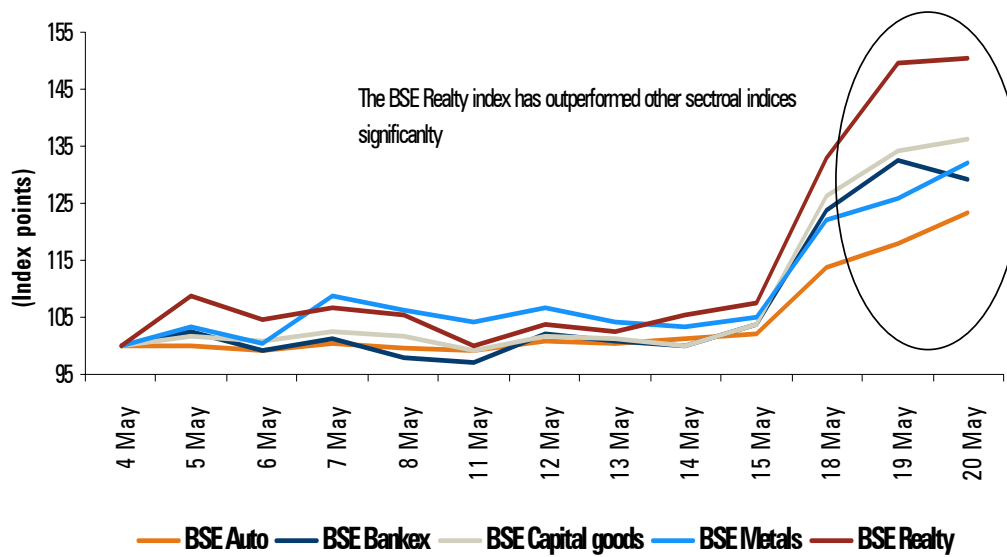
#### Exhibit 4: FII sentiment has turned positive as lot of funds are waiting on the sidelines to invest



Source: SEBI, ICICIdirect.com Research

## Sectoral performances: Auto, banking, capital goods, realty and metals steal the show

Exhibit 5: Performances of various sectoral indices



Source: BSE, ICICIdirect.com Research



## Stocks on radar...

		Technical			Fundamental		
	ICICIdirect.com Code	Avoid	Buy on dips	Buy	Avoid	Buy on dips	Buy
<b>Stocks</b>							
<b>PSU Banks</b>							
Oriental Bank of Commerce	ORIBAN						
Andhra Bank	ANDBAN						
Indian Overseas Bank	INDBAN						
J&K bank	JAMKAS						
IDFC	IDFC						
Power Finance Corporation	POWFIN						
Dena Bank	DENBAN						
<b>Infrastructure</b>							
GMR Infrastructure	GMRINF						
GVK Power	GVKPOW						
Larsen & Toubro	LARTOU						
Thermax	THERMA						
Neyveli Lignite	NEVLIG						
Gujarat Industrial Power	GUJIP						
Power Trading Corporation	POWTRA						
Reliance Infrastructure	BSES						
<b>High leveraged companies</b>							
SCI	SCI						
Varun Shipping	VARSHI						
Mercator Lines	MERLIN						
JSW Steel	JINVIJ						
Bajaj Hindustan	BAJHIN						
Visa Steel	VISSTE						
<b>Others</b>							
JK cement	JKCEME						
UltraTech cement	ULTCEM						
Welspun Gujarat	WELUJ						

Source: ICICIdirect.com Research

### Index

Buy

Buy on decline

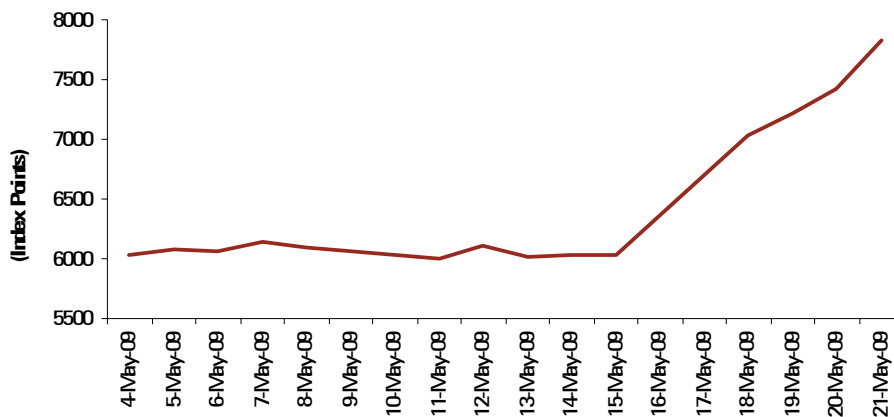
Avoid

### Levels to watch out for...

Stock	ICICIdirect Code	Market Price (May 21 2009)	Buying Range
<b>Banks</b>			
OBC	ORIBAN	179.5	149-156
Andhra Bank	ANDBAN	88.25	70-74
IOB	INDBAN	85.05	67-72
J&K	JAMKAS	469.6	370-390
IDFC	IDFC	119.1	91-99
PFC	POWFIN	203.1	172-177
Dena Bank	DENBAN	49.6	38-41
<b>Infrastructure</b>			
GMR Infra	GMRINF	170	133-138
GVK Power	GVKPOW	38.5	29-31
L&T	LARTOU	1238	950-1010
Thermax	THERMA	387.4	285-305
Neyveli Lignite	NEVLIG	123.3	104-106
PTC	GUJIP	80.3	69-72
Reliance Infrastructure	POWTRA	1110	920-950
	BSES		
<b>High leverage plays</b>			
SCI	SCI	115.5	97-101
Varun	VARSHI	58.9	48-50
Mercator Lines	MERLIN	54.6	45-47
JSW Steel	JINVIJ	495	390-410
Bajaj Hindustan	BAJHIN	133.75	110-115
Visa Steel	VISSTE	28.3	22-24
<b>Others</b>			
JK Cement	JKCEME	81.2	67-69
UltraTech Cement	ULTCEM	689.2	550-590
Welspun Gujarat	WELUJ	144.75	118-124

## Disinvestment story back in the reckoning

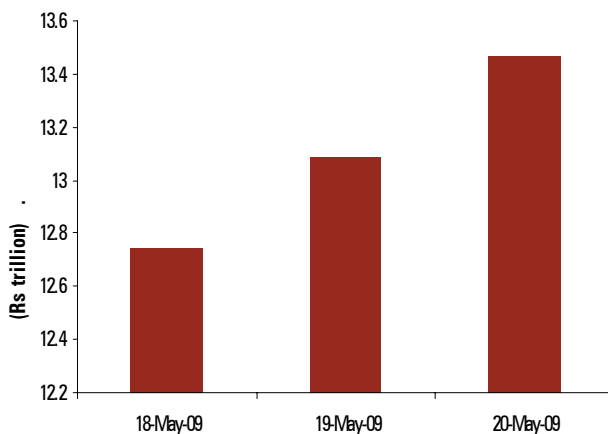
Exhibit 6: BSE PSU Index has risen almost perpendicularly



*The BSE PSU index has gained almost 30% in the last four trading sessions on the back of expectations that the new government will implement disinvestment process in the PSU sector*

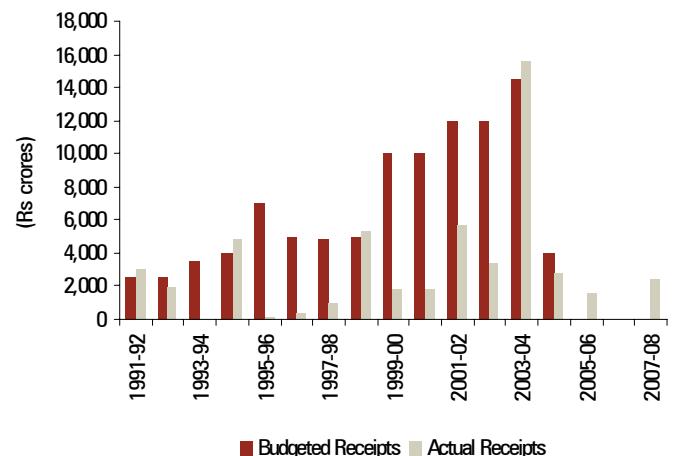
Source: BSE, ICICIdirect.com Research

Exhibit 7: Market cap of BSE PSU Index



Source: Bloomberg, ICICIdirect.com Research

Exhibit 8: Receipts of disinvestment by Gol



Source: Department of Disinvestment, ICICIdirect.com Research

**Let us consider a hypothetical scenario where the government decides to divest up to 10% of the PSU holdings. If we assume the current market cap of Rs 13.47 trillion to be the value of all the listed PSU entities then (10% of Rs 13.47 trillion) Rs 1.34 trillion will be added to the government kitty. This will help the government to reduce the fiscal deficit to a considerable extent.**

**We have not included unlisted entities like BSNL, NHPC, RITES and Oil India where we might see divestment. This, in turn, will add to the corpus of the government kitty.**

### Probable divestment candidates

Company	Government (% stake)	I-Direct Code	Sector
Canara Bank	73.17	CANBAN	Banks
Syndicate Bank	66.47	SYNBN	Banks
Bank of India	64.47	BANIND	Banks
UCO Bank	63.59	UCOBAN	Banks
Indian Overseas	61.23	INDOVE	Banks
State Bank of India	59.41	STABAN	Banks
Punjab Natl Bank	57.8	PUNBAN	Banks
Corporation Bank	57.17	CORBAN	Banks
Union Bank (I)	55.43	UNIBAN	Banks
Allahabad Bank	55.23	ALLBAN	Banks
Vijaya Bank	53.87	VIJBAN	Banks
Bank of Baroda	53.81	BANBAR	Banks
J & K Bank	53.17	JAMKAS	Banks
IDBI Bank	52.67	IDBI	Banks
Andhra Bank	51.55	ANDBAN	Banks
Dena Bank	51.19	DENBAN	Banks
Oriental Bank of Comm.	51.09	ORIBAN	Banks
PFC	89.78	POWFIN	Finance
REC	81.82	RURELE	Finance
ITI	92.98	ITI	Telecomm
Punjab Commun	71.21	PUNCOM	Telecomm
Andrew Yule & Co	94.42	ANDYUL	Diversified
Neyveli Lignite	93.56	NEYLIG	Power
NTPC	89.5	NTPC	Power
Power Grid Corp	86.36	POWGRI	Power
Hind Organ Chem	58.61	HINORG	Chemicals
HMT	98.88	HMT	Automobile
Scooters India	95.38	SCOIND	Automobile
F A C T	98.11	FACT	Fertilizers
Natl. Fertilizer	97.64	NATFER	Fertilizers
R C F	92.5	RCF	Fertilizers
NMDC Ltd	98.38	NATMIN	Mining
Hind Copper	99.59	HINCOP	Non Ferrous Metals
Natl. Aluminium	87.15	NATALU	Non Ferrous Metals
MMTC	99.33	MINERA	Trading

Source: Capitaline, ICICIdirect.com Research

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