

India Equity Strategy

Owning India Inc: Foreign Money Monsoon

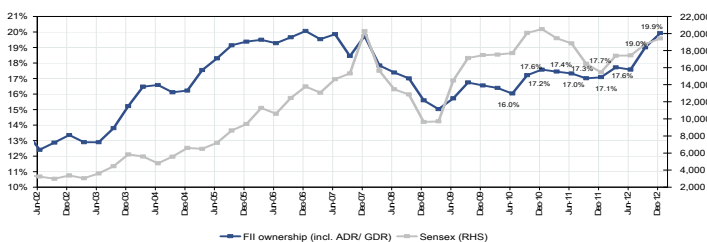
■ Equities

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- **Foreign money is pouring in** — It's the FII money monsoon: \$24bn in 2012 (second-highest ever), \$8bn in 4Q2012 and \$4bn+ in Jan – and FII ownership (19.9%) now accounts for 44% of the market's free-float. This is big, making foreigners even more dominant, and should suggest a very strong equity market. But, money and the mood apart, India's market performance has been soft (+4.6%) since Oct 2012, lagging peers/benchmarks: we have to look beyond foreign flows.
- **And domestic money is flowing out** — India's domestic Institutional Investors (DII's) are doing almost the opposite of foreigners. They are selling (-\$10bn+ in 2012, \$3.4bn in 4Q12 and \$3bn in January 13); limiting net institutional flows to \$5bn in 4Q12. And it's a mixed set of reasons; Insurers becoming sellers for the first time on a FY basis (big one), investors 'breaking even and getting out', and building liquidity for divestments. A contra trend, but it does dampen the impact of FII flows.
- **Portfolio positioning is divergent – only a little convergence**— FIIs have taken on aggressive portfolio positions; unsurprisingly, DII outflows are on the back of relatively defensive positioning. This dichotomy remains fundamentally the same – but, incrementally, FIIs are cutting some of their more aggressive positions (financials) while domestic are trimming defensives a bit (MFs more than Insurers). Still divergent; though extreme positioning might be losing some ground.
- **Peak to Peak?** — We wouldn't call the current high a peak (this presupposes a material market fall). But relative to previous market peaks (Dec07, Dec10) – FII ownership levels are at a high (% holding, rupee values), market multiples at a low, and portfolio value (\$ terms) is also at a low (weaker INR). This mix would suggest downside risks relative to previous foreign 'ownership highs' are low.
- **Follow flows or fundamentals?** — It's always tempting to call flows and expect the market to follow. In which case 2012 (and 4Q12) would have been difficult to call (near record foreign inflows, domestic outflows), and we do not believe 2013 will be any easier. We would stick with fundamentals; a Dec 2013 Sensex target of 20,800 (+6%) – with a rate-cyclical-biased portfolio to drive outperformance.

Figure 1. FII ownership and the Sensex



Source: Bloomberg, CMIE and Citi Research

See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

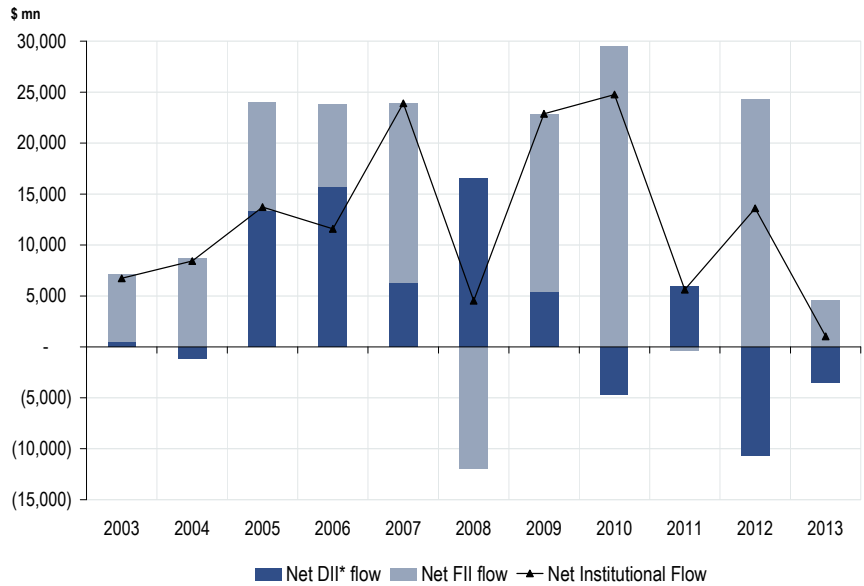
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Owning India Inc – 3QFY13 (Oct-Dec 2013)

FII Money is pouring in and domestic cash is flowing out

2012 has been a big foreign flow year (\$24bn), and particularly 4Q2012.....but its been a record selling year for DII's, and that has limited institutional flows to \$13.6bn, only the third best in the last four years. January 2013 has been somewhat similar

Figure 2. Institutional Equity flows

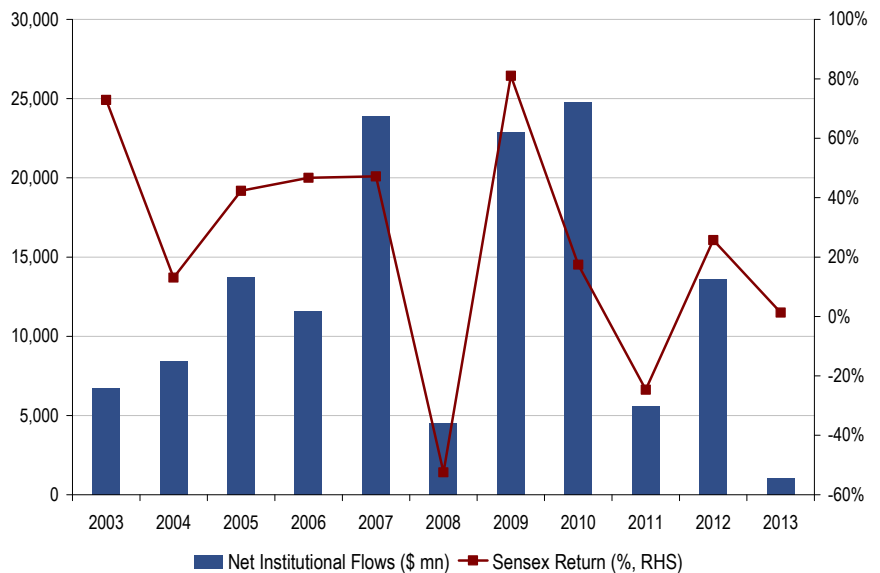


Source: Bloomberg and Citi Research

* Prior to 2007, DII data comprises only of DMF flows. Post 2007, DII data is only exchange flows and excludes primary market flows.

The market performance in essence is reflective of net institutional flows, rather than purely foreign flows

Figure 3. Institutional equity flows and market return

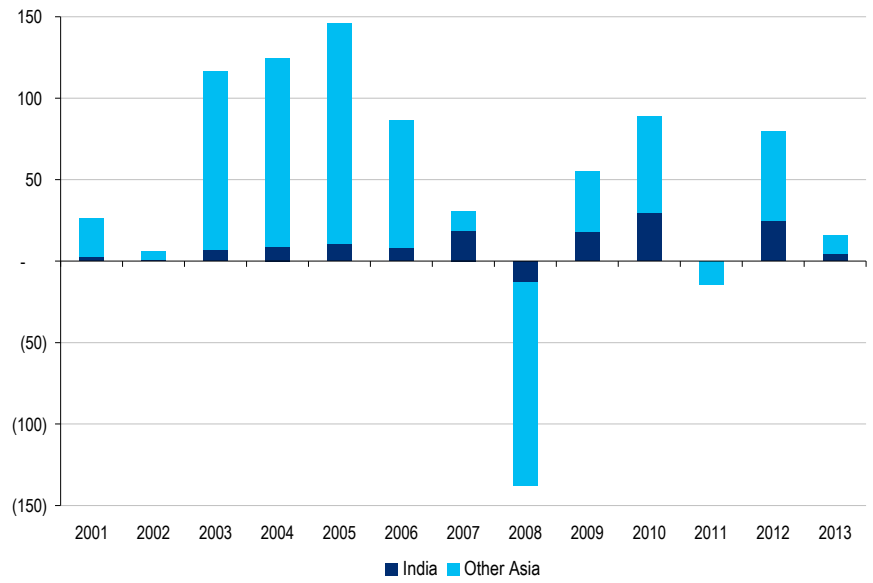


Source: Bloomberg and Citi Research

* Prior to 2007, institutional flows data doesn't include insurers. Post 2007, DII data is only exchange flows and excludes primary market flows.

India gained for 31% of the FII inflows into key Asian equity markets (ex of China) in 2012

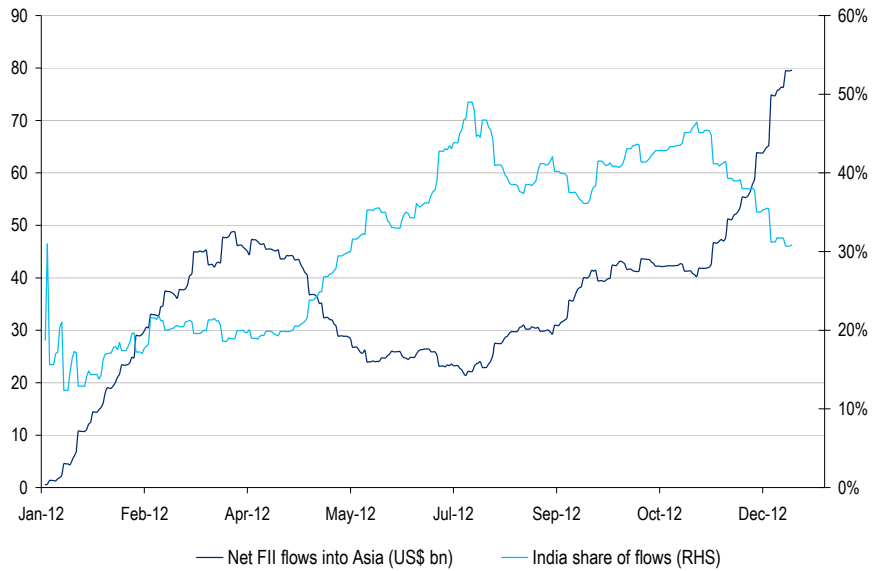
Figure 4. FII flows into Asian* equities



Source: Bloomberg; * excludes China

However, India's share of incremental flows has moderated in 4Q12, from 41% at Sep end

Figure 5. FII flows into Asian* equities in 2012



Source: Bloomberg; * excludes China

This is somewhat reflected in India's modest underperformance (-1% relative to MSCI EM) since October 2012

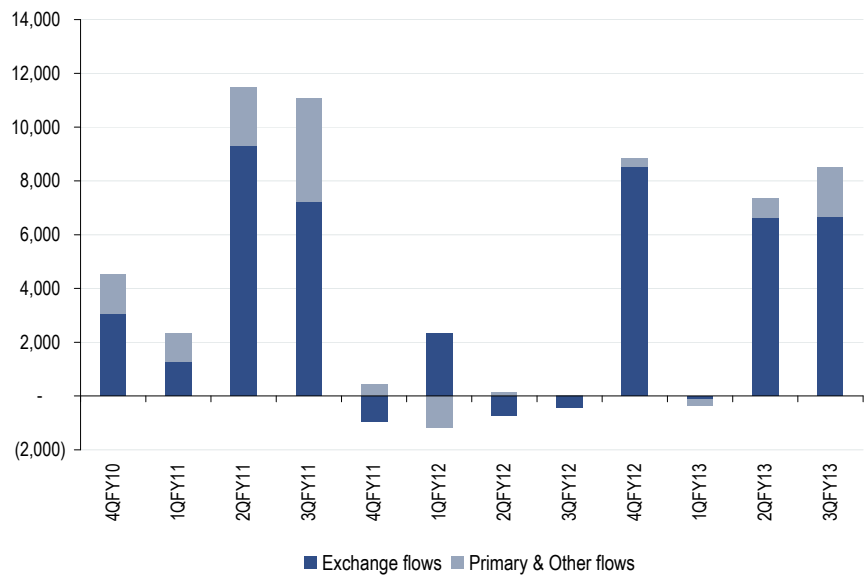
Figure 6. MSCI India's performance relative to MSCI EM (local currency): 2012 through 2013 ytd



Source: MSCI, Datastream and Citi Research

Primary market activity at 11% of the \$24bn FII inflows in 2012 vs. 29% in 2010, when FII inflows stood at \$29bn....although there were chunky secondary market exits (PE/FDI) which would probably raise this cumulative level beyond 2010's 29%

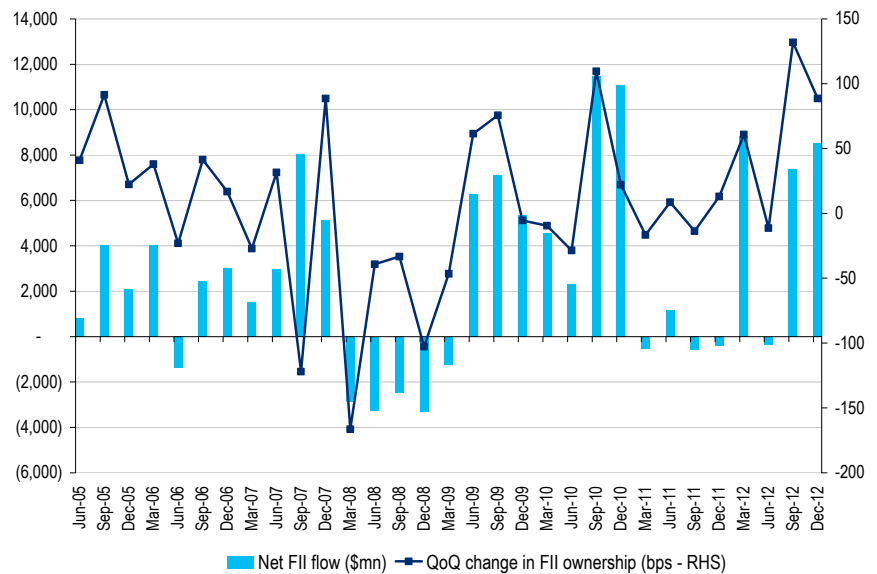
Figure 7. Net FII flows (\$mn) in Indian equities



Source: SEBI

FII ownership has gone up for the second consecutive quarter and was up 193bps in 2H2012.....but 4Q12 gains were less than in the previous quarter

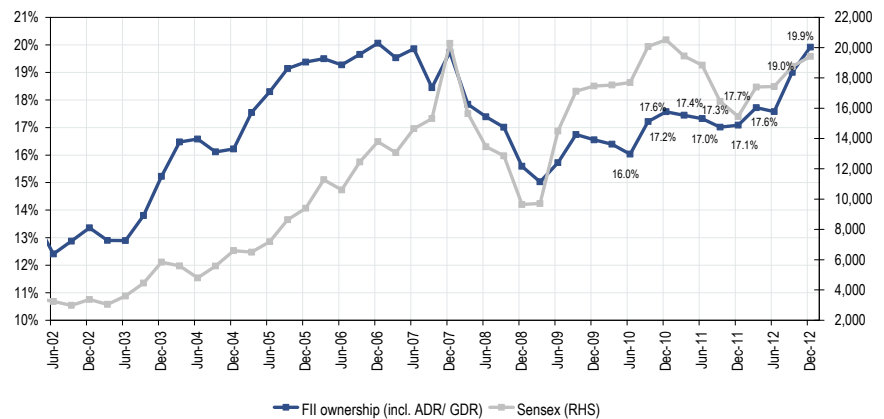
Figure 8. FII flows and change in FII ownership of BSE500



Source: CMIE, Bloomberg and Citi Research

You cannot technically call it a peakFII ownership has been higher before.....but the gains have been pretty steady and consistent

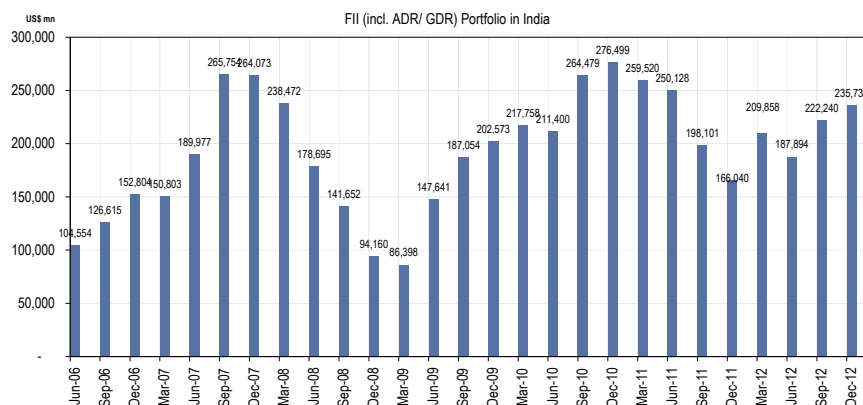
Figure 9. FII ownership and the Sensex



Source: Bloomberg, CMIE and Citi Research

FII portfolio value is still 15% lower than its all time high in Dec 2010, despite \$24bn more inflows in 2011-12....it's a lot about the currency, and possibly a little about performance

Figure 10. Value of FII portfolio in India



Source: CMIE and Citi Research

Peak to Peak

FII portfolio values have fallen over the last five years...in spite of \$60bn incremental inflows over this period.....ownership levels are comparable.....though valuations at least are not

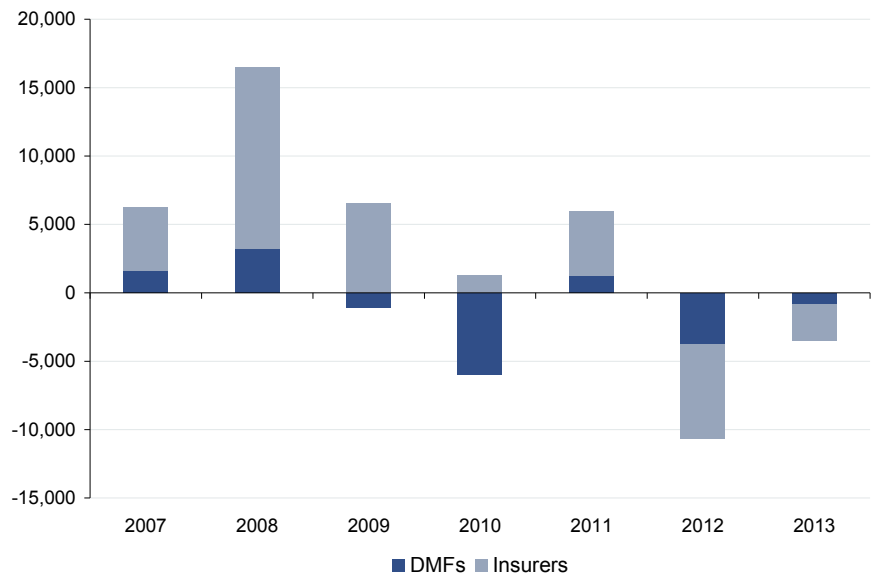
Figure 11. FII ownership: Dec'07 vs Dec'10 vs Dec'12

FII inflow (2008- 2012) - USD mn	59,948			Change (Dec'12 vs. Dec'07)
	Dec '07	Dec '10	Dec '12	
FII ownership of BSE500 (%)	19.7%	18.06%	19.92%	
Sensex	20,287	20,509	19,427	-4%
Sensex 1-Yr fwd P/E	22.5	17.2	14.8	-34%
USD/ INR	39.41	44.71	55.00	-28%
Value of FII equity portfolio				
- Rs mn	10,405,798	12,362,966	12,964,368	25%
- USD mn	264,073	276,499	235,737	-11%

Source: CMIE, Bloomberg , Factset and Citi Research

It's the domestics...it's the biggest negative year ever, and it's the Insurers that have turned direction....and it has been even more extreme in 2013 ytd

Figure 12. Domestic institutional net inflows into equities: DMFs vs insurers

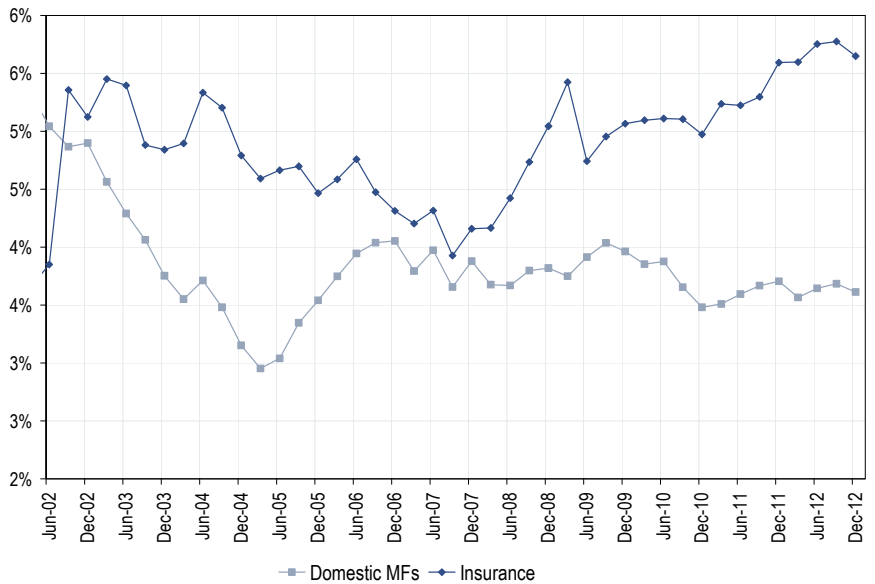


Source: Bloomberg and Citi Research

* Flows for insurers are computed by subtracting DMF flows from institutional flows from exchange (exclude primary flows) and thus are understated

Mutual funds ownership levels seem to have stabilized.... it is the insurers that are now seeing a dip, and making an impact

Figure 13. Mutual fund and insurance ownership of the BSE500

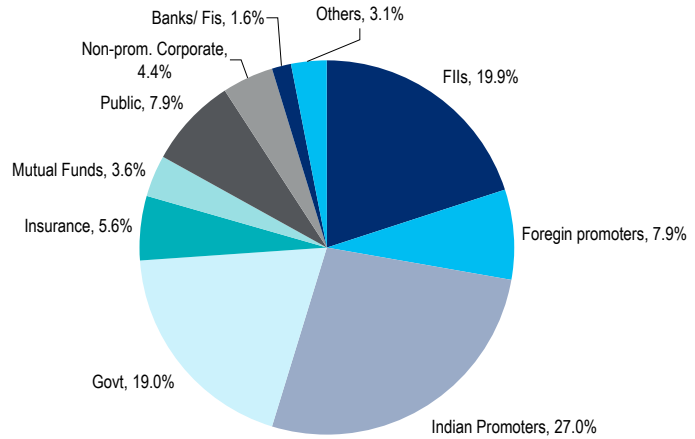


Source: CMIE and Citi Research

Who Owns What?

Total foreign ownership is at record highs for the broader market

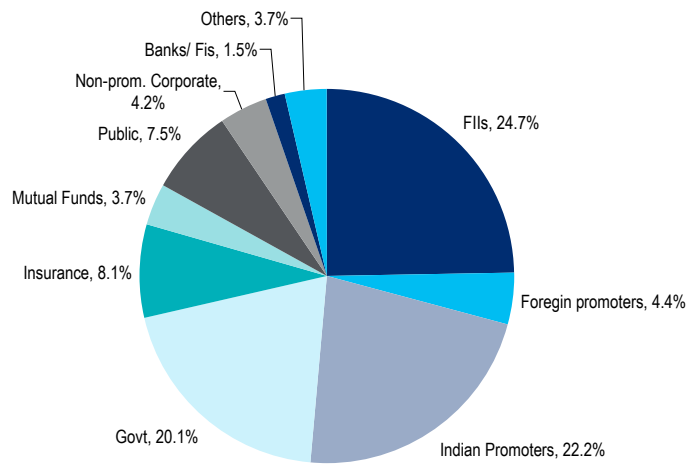
Figure 14. BSE500 Ownership, 31 Dec 2012



Source: CMIE, Bloomberg and Citi Research

And it's at 29% for the narrower Sensex set of 30 companies

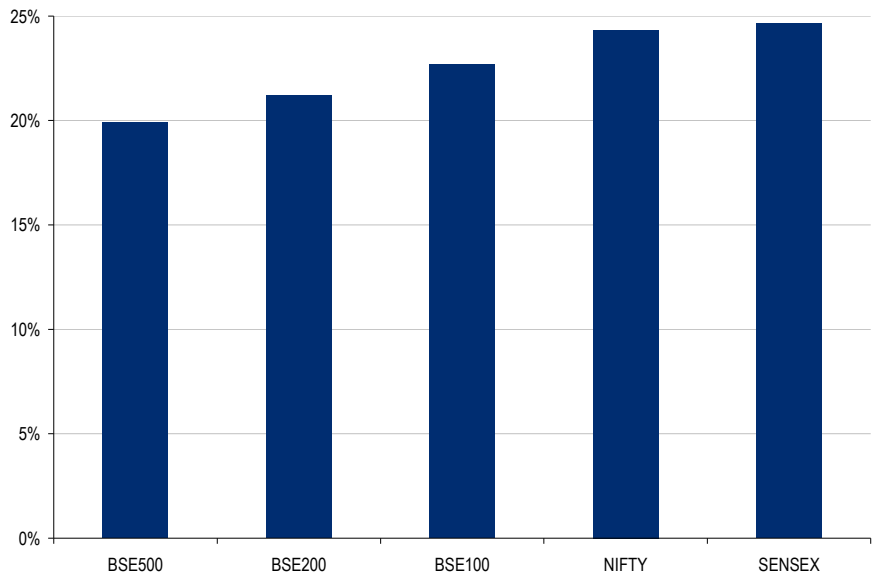
Figure 15. Sensex Ownership, 31 Dec 2012



Source: CMIE, Bloomberg and Citi Research

FII's do own more of the biggest companies...but not that much more than a fairly broader set

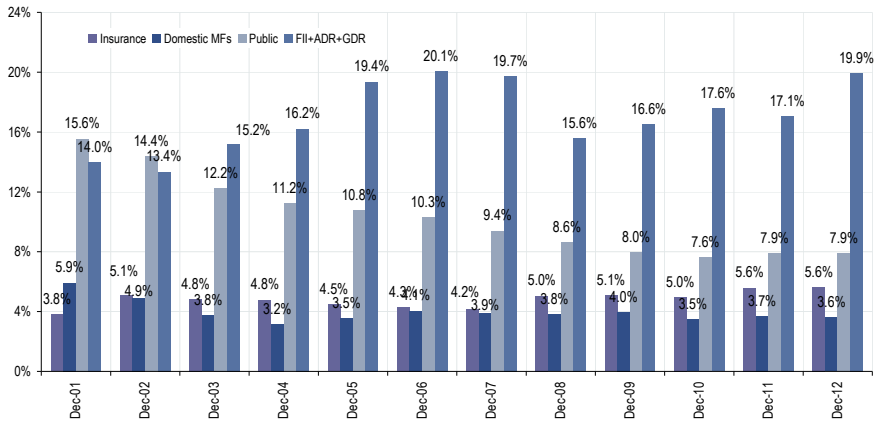
Figure 16. FII ownership (incl. ADR/ GDR) for various indices, Dec '12



Source: CMIE, Bloomberg and Citi Research

The second-highest FII ownership level ever

Figure 17. Trends in ownership of BSE500

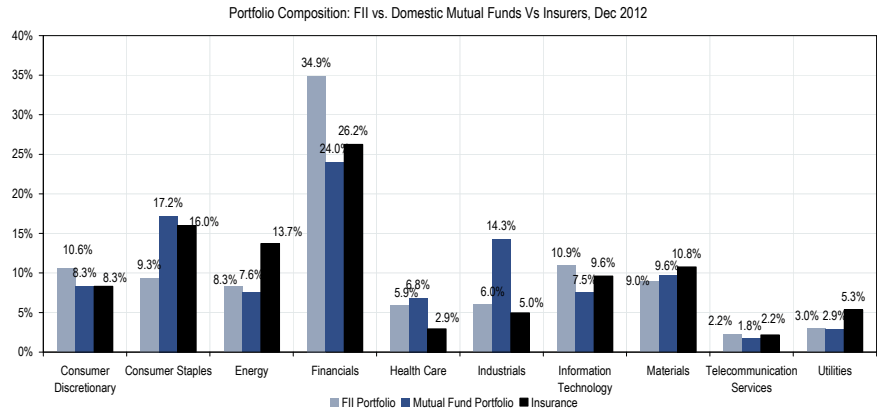


Source: CMIE and Citi Research

Investor Portfolio Stance

There are differences between Insurers' and DMFs' portfolios, but they are relatively similar...

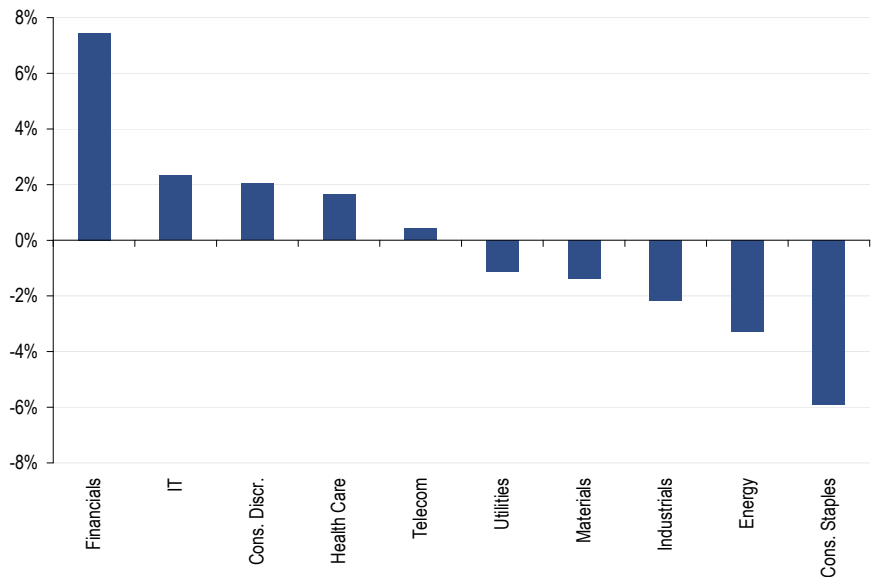
Figure 18. Portfolio composition: FIs (incl. ADR/ GDR) vs DMFs vs Insurers



Source: CMIE and Citi Research

Financials and Consumer staples is where we see the biggest dichotomy....reflecting the aggressive vs defensive approach between FIs and Domestic

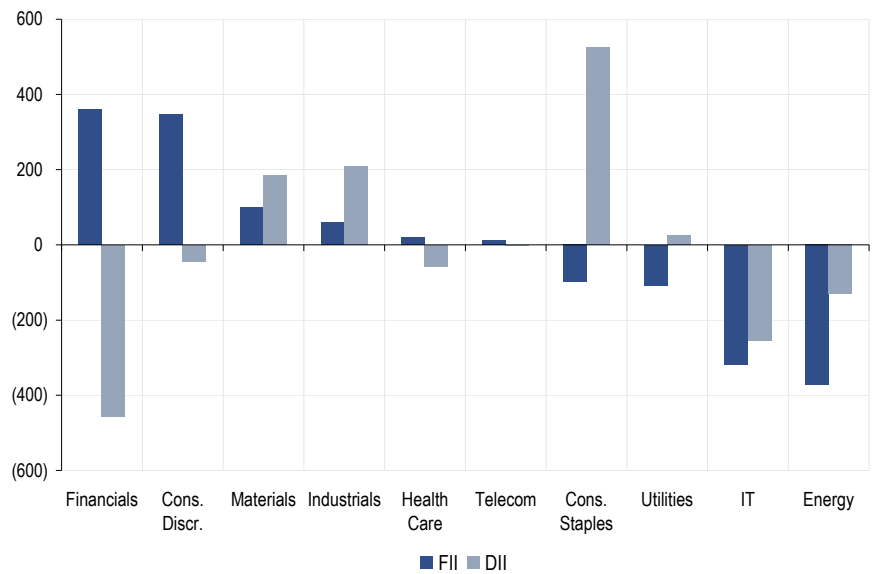
Figure 19. Relative positioning: FIs vs DIs



Source: CMIE and Citi Research; * not considering respective benchmarks

For FIIs, the biggest plays are on energy (-373 bps) and financials (+361bps); in contrast, DIIs are positioned mostly in consumer staples (+525bps) and financials (-456bps)

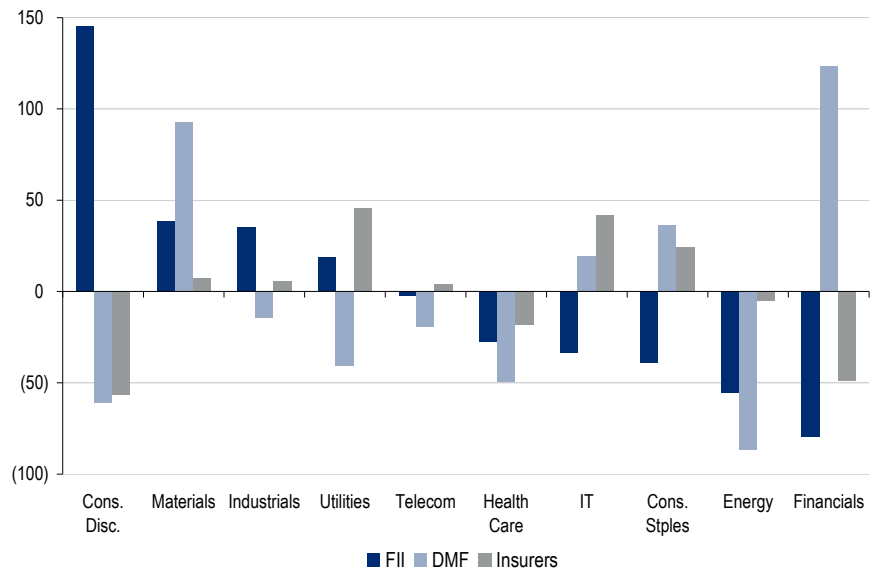
Figure 20. Portfolio OW/ UW (bps) for FIIs and DIIs, Dec 2012



Source: MSCI, Bloomberg, CMIE and Citi Research

FIIs continue to take aggressive positions....and Domestic remain relatively defensively biased...but there's a little bit of convergence

Figure 21. Change in portfolio OW/ UWs (bps) in Dec quarter: FIIs vs DMFs vs Insurers



Source: CMIE, Bloomberg, MSCI and Citi Research

And there's churn.....FII's ownership changes generally driving stock direction

Figure 22. BSE100 stocks with the largest changes in FII ownership in Dec quarter

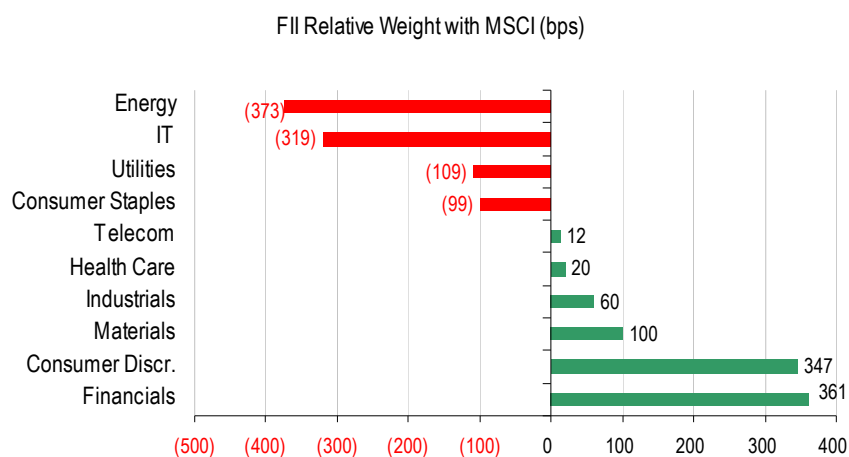
Company Name	RIC	FII ownership (%)		Change (bps)	Stock return (Oct-Dec'12)
		Sep-12	Dec-12		
Stocks with the highest increase in FII ownership					
HDFC	HDFC.BO	68.72	73.17	445	7%
N M D C Ltd.	NMDC.NS	0.66	4.4	374	-15%
Federal Bank Ltd.	FED.BO	42.17	45.66	349	21%
Indusind Bank Ltd.	INBK.NS	48.04	51.44	340	17%
Mahindra & Mahindra Ltd.	MAHM.BO	35.39	38.3	291	8%
Maruti Suzuki India Ltd.	MRTI.BO	20.45	23.13	268	10%
Tata Global Beverages Ltd.	TAGL.BO	17.54	20.16	262	12%
L I C Housing Finance Ltd.	LICH.BO	31.89	34.35	246	3%
Adani Enterprises Ltd.	ADEL.BO	15.08	17.4	232	35%
Ashok Leyland Ltd.	ASOK.BO	28.22	30.36	214	12%
Stocks with the highest decrease in FII ownership					
United Phosphorus Ltd.	UNPO.BO	35.75	31.59	-416	-1%
Crompton Greaves Ltd.	CROM.BO	19.57	18.12	-145	-8%
J S W Steel Ltd.	JSTL.BO	20.62	19.28	-134	7%
Cairn India Ltd.	CAIL.BO	16.17	14.97	-120	-4%
D L F Ltd.	DLF.BO	15.87	14.87	-100	-1%
Reliance Capital Ltd.	RLCP.BO	21.13	20.23	-90	11%
Exide Industries Ltd.	EXID.BO	17.57	16.69	-88	-6%
G M R Infrastructure Ltd.	GMRI.BO	11.35	10.78	-57	-22%
Canara Bank	CNBK.BO	13.24	12.76	-48	15%
United Spirits Ltd.	UNSP.BO	46.53	46.07	-46	56%

Source: CMIE and Citi Research

Investor Portfolio Stance – FIIs

FIIs are long Financials / Cons Disc and short Energy / IT

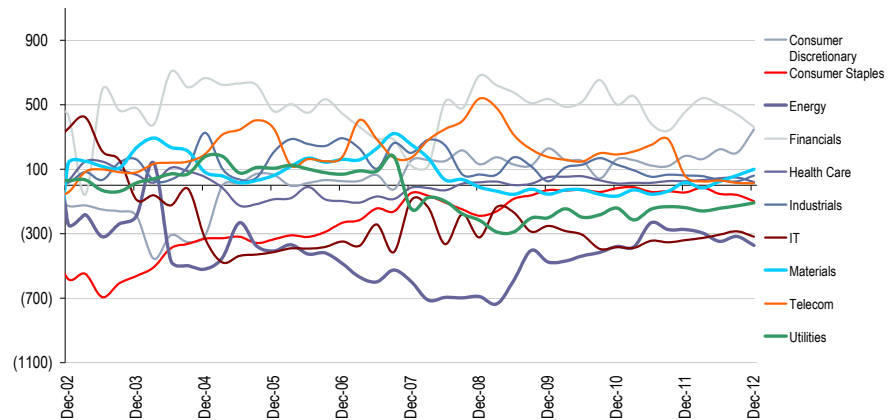
Figure 23. FII OW/ UW vs. MSCI India by sector (bps), Dec 2012



Source: MSCI, CMIE and Citi Research

Interestingly the big OWs are trimmed
...other than consumer discretionary

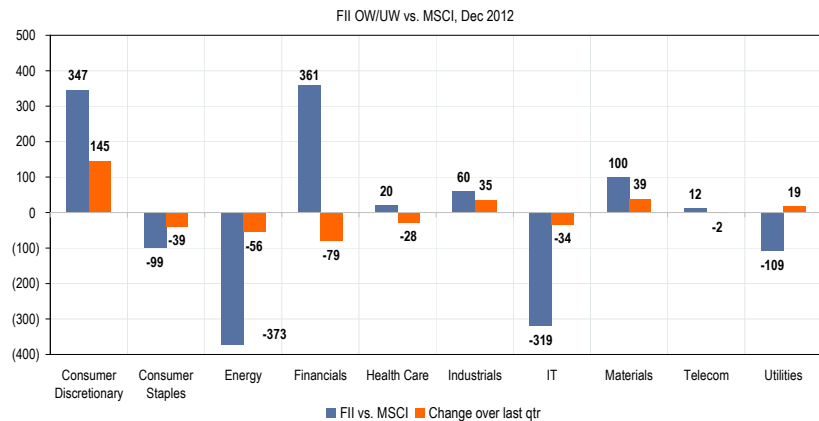
Figure 24. FIIs vs. MSCI India – OW/ UW by sector



Source: MSCI, CMIE and Citi Research

Have cut Financials a bit, further reduced
consumer staples...and are seeking
upsides on cons discretionary

Figure 25. FII portfolio OW/ UW change, Dec 2012



Source: MSCI, CMIE and Citi Research

Figure 26. FIIs OW/ UW near-term trends by sector

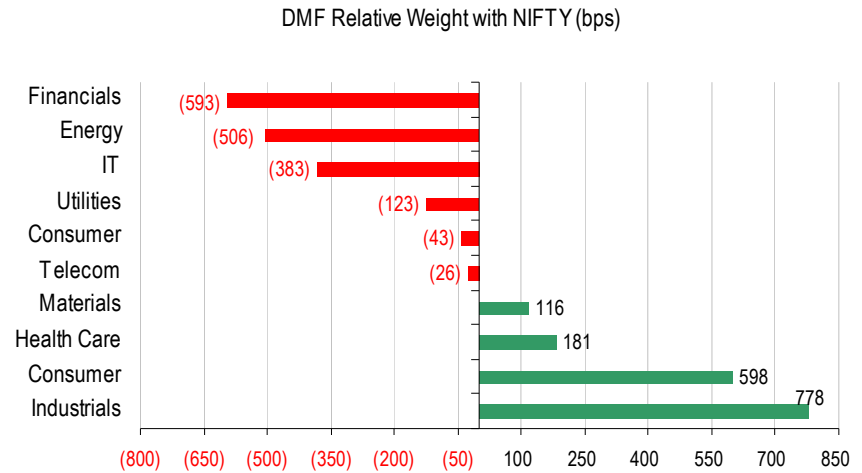
Sector	Shareholding						OW/ UW rel. MSCI					
	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12
Consumer Discr.	9.4%	9.8%	10.3%	10.1%	10.1%	10.6%	119	182	162	223	201	347
Consumer Staples	7.1%	8.0%	7.7%	8.9%	9.2%	9.3%	(36)	(44)	(16)	(54)	(60)	(99)
Energy	10.2%	9.5%	8.7%	8.8%	9.0%	8.3%	(275)	(275)	(296)	(348)	(317)	(373)
Financials	31.3%	29.4%	31.7%	32.2%	33.7%	34.9%	339	456	540	498	440	361
Health Care	5.0%	5.5%	5.5%	5.8%	5.7%	5.9%	26	25	32	43	48	20
Industrials	8.0%	6.2%	6.5%	6.1%	5.9%	6.0%	66	61	56	33	24	60
IT	12.7%	15.5%	13.9%	13.1%	12.2%	10.9%	(354)	(340)	(327)	(306)	(285)	(319)
Materials	9.5%	9.2%	9.5%	9.4%	9.1%	9.0%	(36)	17	(17)	25	61	100
Telecom	3.2%	3.3%	2.7%	2.4%	1.9%	2.2%	285	57	24	30	15	12
Utilities	3.6%	3.6%	3.4%	3.3%	3.2%	3.0%	(132)	(138)	(160)	(143)	(128)	(109)

Source: MSCI, CMIE and Citi Research

Investor Portfolio Stance – DMFs

Domestics don't seem have lost their preference for Industrials, and show continued caution on Financials

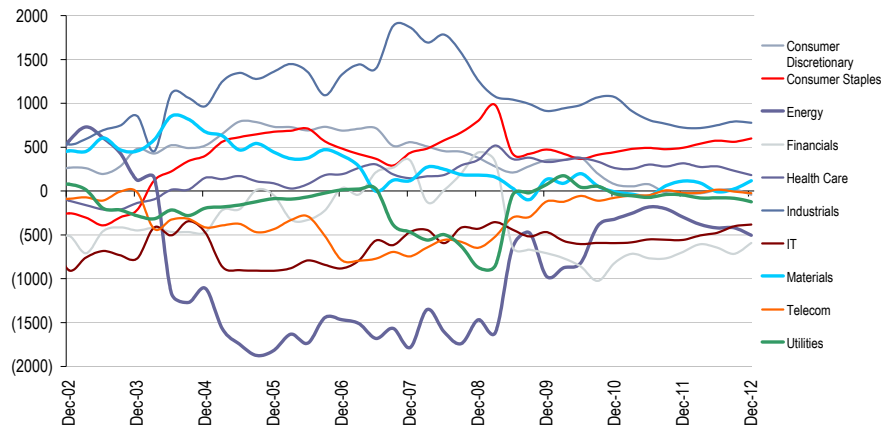
Figure 27. DMF OW/ UW vs. NIFTY by sector (bps), Dec 2012



Source: Bloomberg, CMIE and Citi Research

Still away from benchmarks, but not straying further

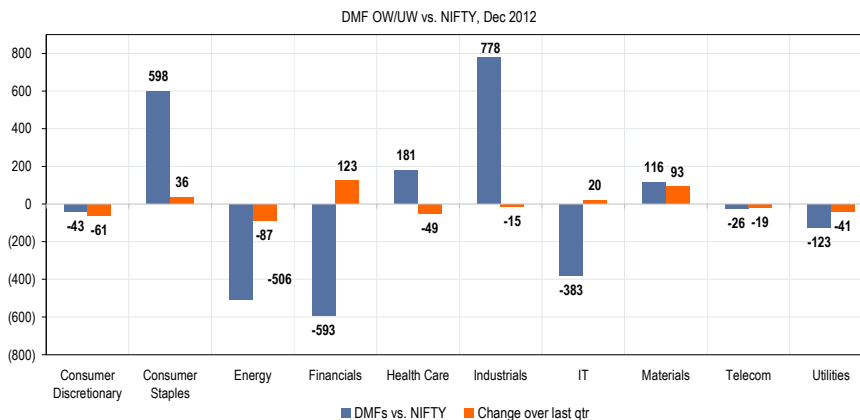
Figure 28. DMFs vs NIFTY – OW/ UW by sector



Source: Bloomberg, CMIE and Citi Research

Have cut the Financials UW.....but sticking with a more defensive script

Figure 29. DMF portfolio OW/ UW change, Dec 2012



Source: Bloomberg, CMIE and Citi Research

Figure 30. DMFs OW/ UW near-term trends by sector

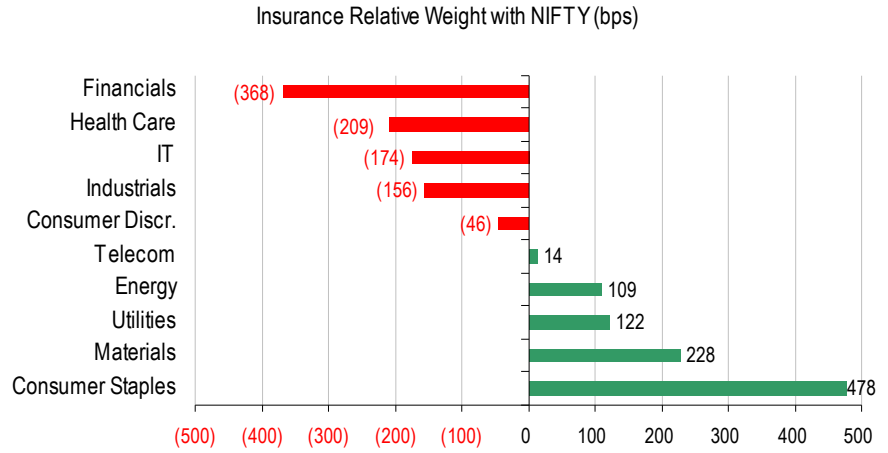
Sector	Shareholding						OW/ UW rel. NIFTY					
	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12
Consumer Discr.	7.7%	7.9%	8.3%	8.0%	8.4%	8.3%	(24)	(26)	(27)	10	18	(43)
Consumer Staples	14.3%	15.6%	15.5%	17.1%	16.9%	17.2%	477	493	539	574	561	598
Energy	10.8%	10.3%	9.5%	9.0%	8.8%	7.6%	(204)	(299)	(381)	(421)	(419)	(506)
Financials	19.3%	17.9%	20.6%	21.2%	21.7%	24.0%	(768)	(693)	(608)	(646)	(717)	(593)
Health Care	6.7%	7.5%	6.8%	7.0%	7.2%	6.8%	280	316	274	281	230	181
Industrials	15.4%	13.2%	13.7%	14.1%	14.7%	14.3%	766	723	718	749	793	778
IT	8.1%	10.3%	9.1%	8.5%	8.3%	7.5%	(557)	(558)	(507)	(476)	(402)	(383)
Materials	9.4%	9.4%	9.5%	9.0%	8.7%	9.6%	61	113	93	(7)	24	116
Telecom	3.5%	3.1%	2.6%	2.4%	1.7%	1.8%	8	(22)	(21)	14	(6)	(26)
Utilities	5.0%	4.8%	4.3%	3.9%	3.6%	2.9%	(40)	(47)	(80)	(79)	(82)	(123)

Source: Bloomberg, CMIE and Citi Research

It's still safety, and caution on the financials

Investor Portfolio Stance – Insurers

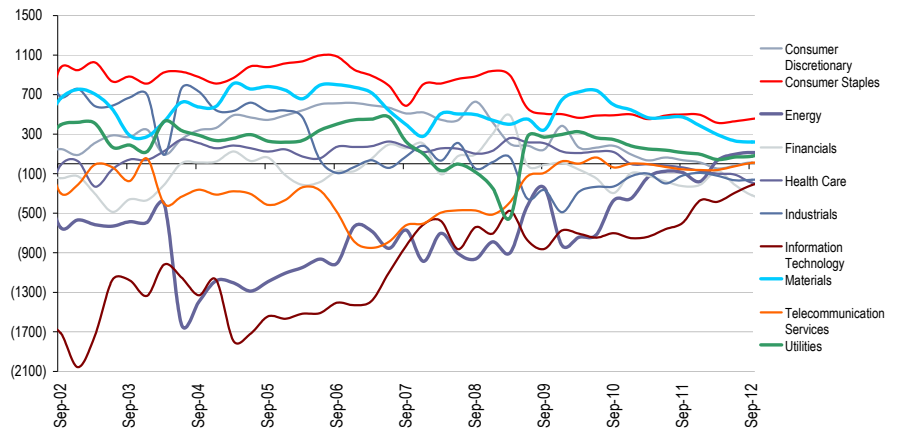
Figure 31. Insurers OW/ UW vs. NIFTY by sector (bps), Dec 2012



Source: Bloomberg, CMIE and Citi Research

But a move closer to the benchmark

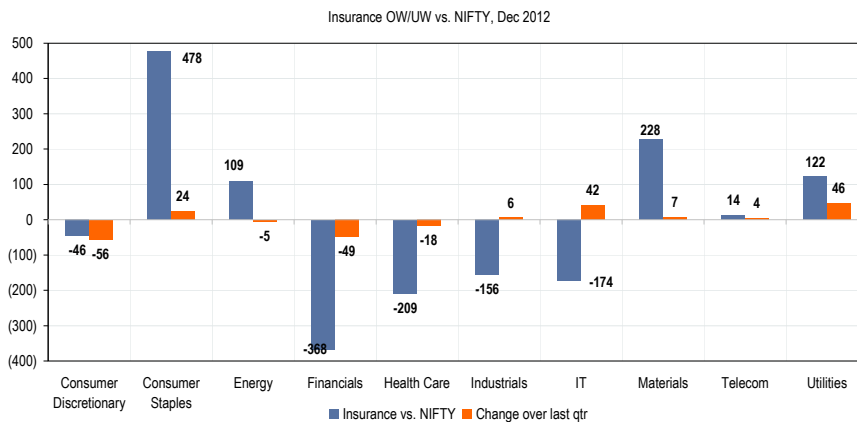
Figure 32. Insurers vs. NIFTY – OW/ UW by sector



Source: Bloomberg, CMIE and Citi Research

No material swings in portfolio positioning

Figure 33. Insurer portfolio OW/ UW change, Dec 2012



Source: Bloomberg, CMIE and Citi Research

Figure 34. Insurers OW/ UW near-term trends by sector

Sector	Shareholding						OW/ UW rel. NIFTY					
	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12
Consumer Discr.	8.3%	8.3%	8.1%	7.7%	8.3%	8.3%	37	14	(47)	(18)	11	(46)
Consumer Staples	14.5%	15.6%	14.2%	15.6%	15.8%	16.0%	500	495	415	430	454	478
Energy	12.0%	11.5%	13.6%	14.2%	14.2%	13.7%	(89)	(180)	34	97	114	109
Financials	24.7%	22.8%	26.0%	25.5%	25.7%	26.2%	(227)	(212)	(72)	(213)	(318)	(368)
Health Care	3.6%	3.6%	3.1%	3.1%	3.0%	2.9%	(37)	(73)	(101)	(108)	(190)	(209)
Industrials	6.5%	5.0%	5.3%	4.9%	5.1%	5.0%	(117)	(92)	(120)	(167)	(162)	(156)
IT	7.7%	12.1%	10.4%	10.3%	10.2%	9.6%	(596)	(371)	(385)	(294)	(216)	(174)
Materials	13.5%	12.1%	11.6%	11.3%	10.7%	10.8%	473	383	296	232	221	228
Telecom	2.8%	2.7%	2.2%	2.0%	1.9%	2.2%	(57)	(63)	(62)	(25)	9	14
Utilities	6.5%	6.2%	5.5%	5.3%	5.2%	5.3%	113	97	42	68	77	122

Source: Bloomberg, CMIE and Citi Research

Appendix A-1

Analyst Certification

The research analyst(s) primarily responsible for the preparation and content of this research report are named in bold text in the author block at the front of the product except for those sections where an analyst's name appears in bold alongside content which is attributable to that analyst. Each of these analyst(s) certify, with respect to the section(s) of the report for which they are responsible, that the views expressed therein accurately reflect their personal views about each issuer and security referenced and were prepared in an independent manner, including with respect to Citigroup Global Markets Inc and its affiliates. No part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) expressed by that research analyst in this report.

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