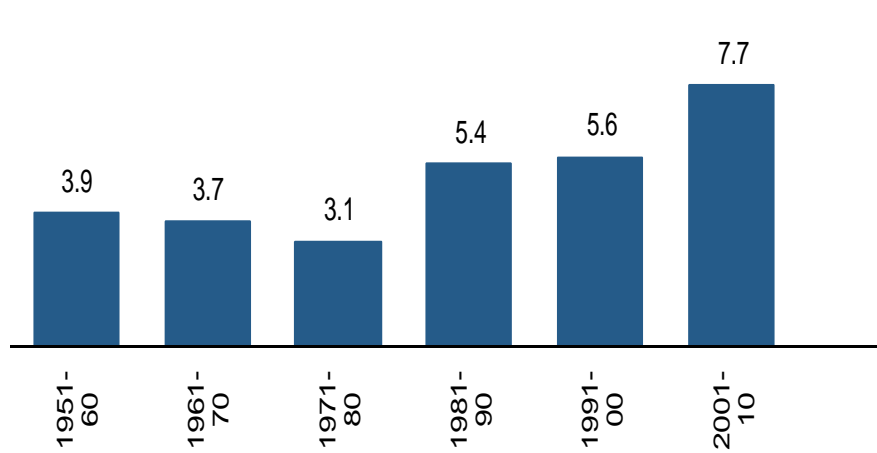


Pessimistic markets, low P/E's

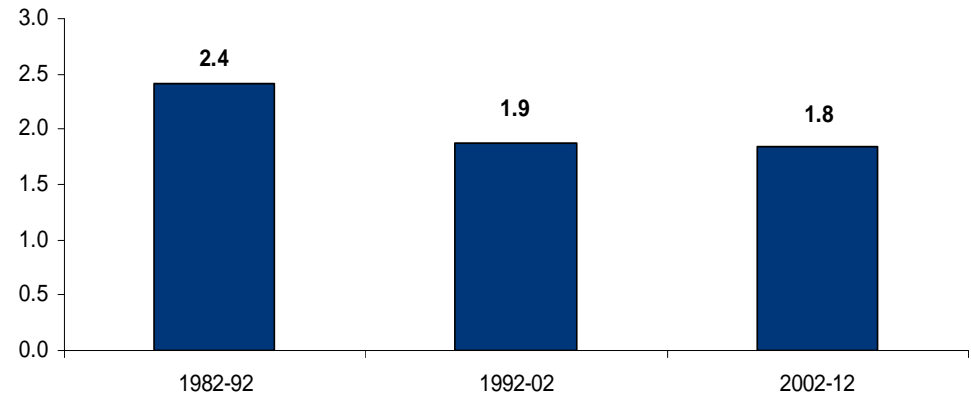
An opportunity for the long term investor

India - A Sustainable, High Growth Economy

GDP (average % change)



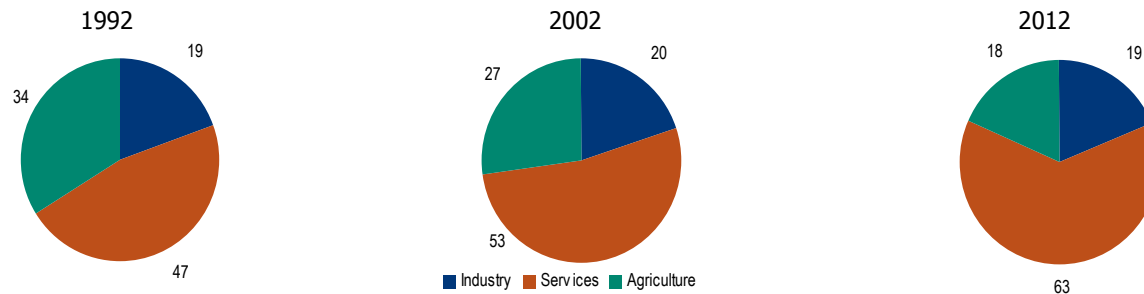
Standard Deviation of Annual GDP Growth



Source: India Ministry of Statistics and Programme Implementation Annual Report 2010-2011.

GDP Composition (1982 – 2012)

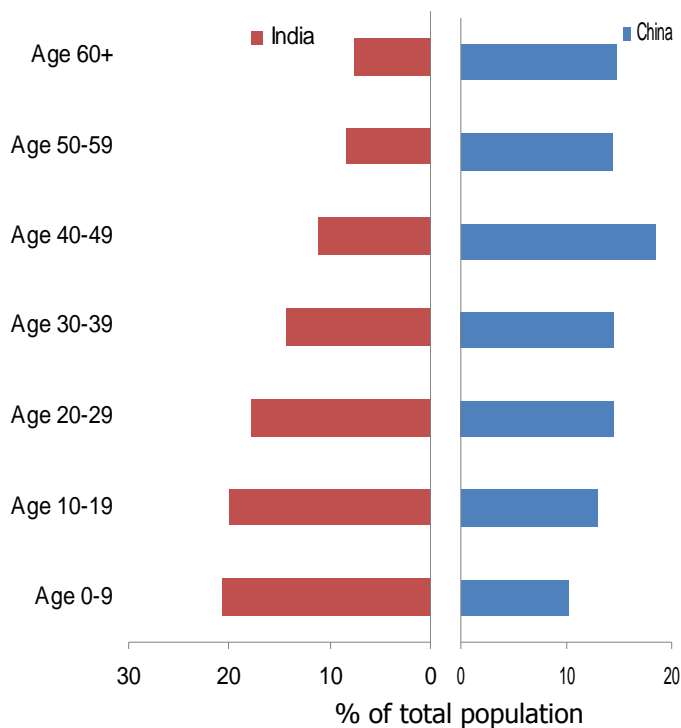
Source: BoA ML



India's growth trend has continued to increase and volatility of GDP growth rates has been trending downwards

India Economy - Demographics & Rising Affordability

India and China – Population Structure 2010



India has a very young population; a large number should move into working age in next 10 years

Key parameters	Past	Present	Future?
	FY 2001	FY 2011	FY 2020E
Mobile connections in Million	3.6	811	2031
Mobile Teledensity	0.40%	68%	135%
Price per minute of Airtime in Rs	5.18	0.43	0.37
2 Wheeler unit sales in Million	3.6	11.8	24.8
% Penetration per household	20%	35%	70%
Price per unit (Splendour) (\$)	800	1023	1500
2 Wheeler price to PC GDP	1.80	0.69	0.30
Car unit Sales in Million	0.6	2.5	7.2
% Penetration per household	3%	7%	20%
Price per unit (Alto) (\$)	7000	6250	8000
Car price to PC GDP	15.7	4.2	1.6

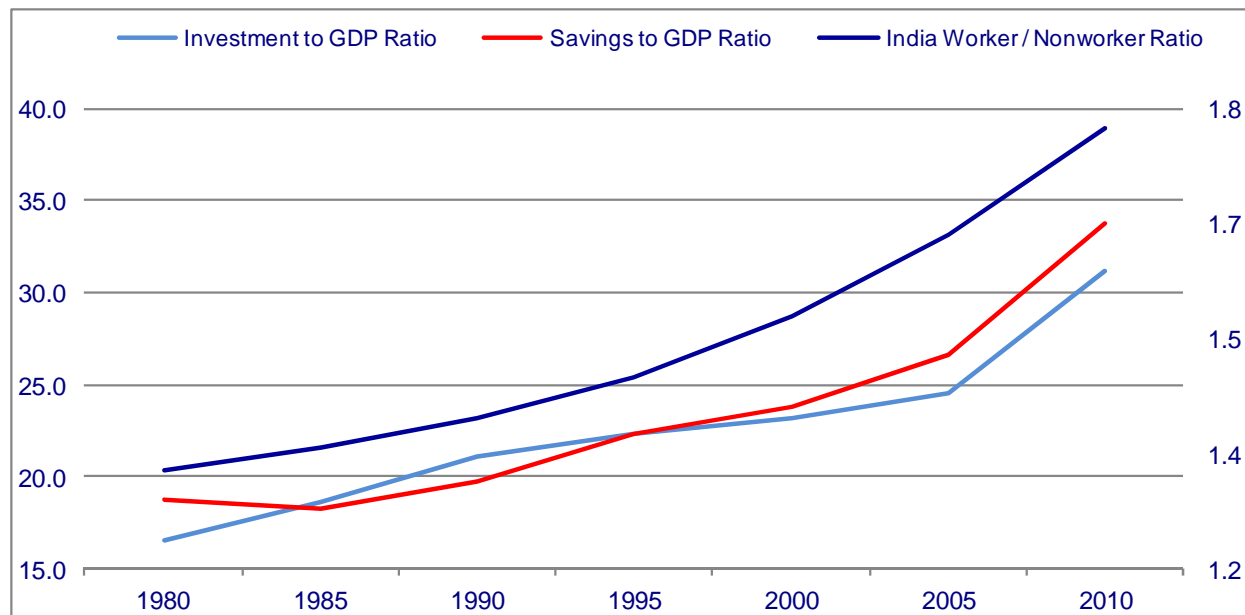
Source: BoA ML

Increasing affordability, low penetration of consumer goods, increasing credit, & favourable demographics point to sustained economic growth ahead...

Source: Euromonitor International from national statistics, UN / MOSL

India Economy – Rising Savings / Investment Rate

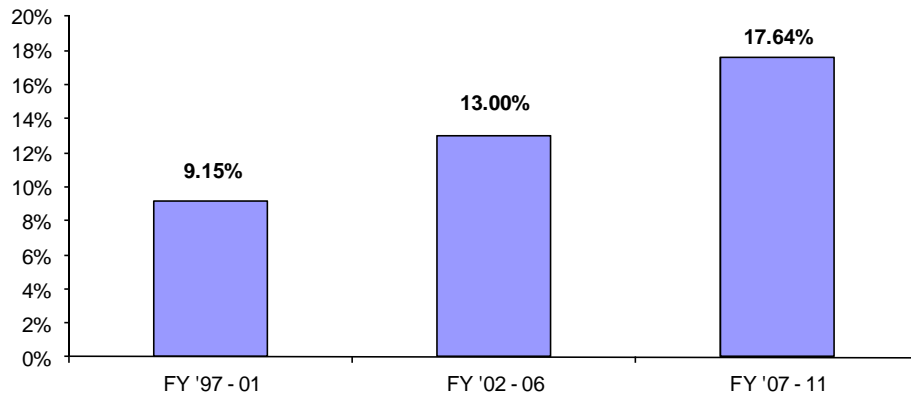
India's dependency ratio continues to fall, savings rate continues to rise, facilitating higher investments



Source: CLSA research

India Economy – Exports, An Opportunity

Consistent uptrend in Exports to GDP ratio*



* Exports data includes software earnings

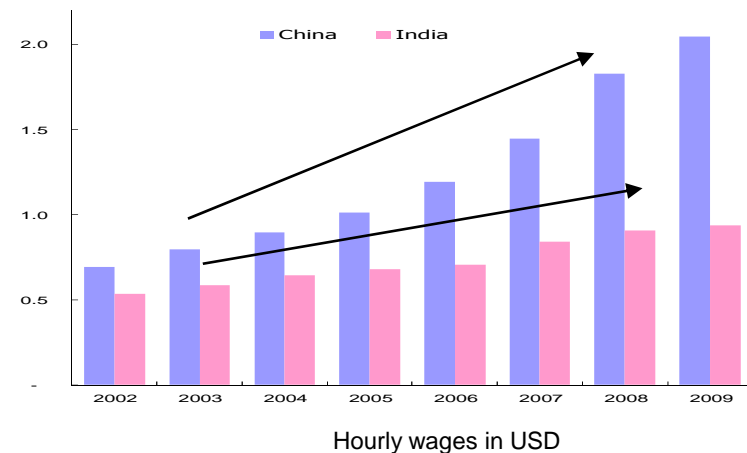
Source: Citi Investment Research & Analysis

Indian currency has depreciated against Yuan by ~50% in last 5 years
This is a big opportunity as China is 9.5% & India is 1.6% of global exports



Source: Bloomberg

Wage inflation in China is higher than in India



Source: US Bureau of Labour Statistics and Citi Investment Research and Analysis

Indian Economy – Current Issues



Twin deficits – (1) Fiscal deficit

As % of GDP	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY12 over FY08
GDP Growth Rate	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total Taxes	9.0	9.4	9.9	11.0	11.9	10.8	9.7	10.3	10.1	-1.8
Social spend & Subsidies	6.9	7.9	9.8	9.5	11.1	12.5	11.9	13.4	13.2	2.1
Fiscal Deficit	4.3	3.9	4.0	3.3	2.5	6.0	6.5	4.9	5.9	3.4

3.4

3.9

Falling tax to GDP & rising social spends have equally contributed to deterioration in fiscal deficit

Twin deficits – (2) Current account deficit

As % of GDP	FY01	FY02	FY03	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12
Current a/c deficit	-0.6	0.7	1.3	2.3	-0.3	-1.2	-1.0	-1.3	-2.3	-2.8	-2.6	-3.8
Net Gold Imports	0.3	0.3	0.2	0.5	0.9	0.5	0.6	0.4	0.8	1.2	1.9	2.3
Net Oil Imports	3.0	2.5	3.0	2.8	3.2	3.9	4.0	4.1	5.4	4.1	4.1	4.9
Fx reserve	9.2	11.3	15.0	18.8	19.6	18.2	21.0	25.0	20.6	20.5	18.0	15.6
External debt	22.0	20.7	20.7	18.8	18.6	16.7	18.2	18.1	18.3	19.2	18.1	NA

NA – Not available

Avg. prices	FY01	FY02	FY03	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12
Gold price (\$ per troy oz.)	272.1	277.7	325.5	377.6	413.9	476.6	628.4	765.8	867.2	1023.0	1293.5	1634.7
Oil (\$/bbl) - Brent	24.9	25.0	28.5	38.0	55.3	66.1	72.7	98.5	62.7	80.3	110.9	118.8

Bulk of the deterioration in current account deficit is on account of gold imports.

Source: BofA-ML

Worst of Current Account & Fiscal Deficit behind us ?

Current Account Deficit

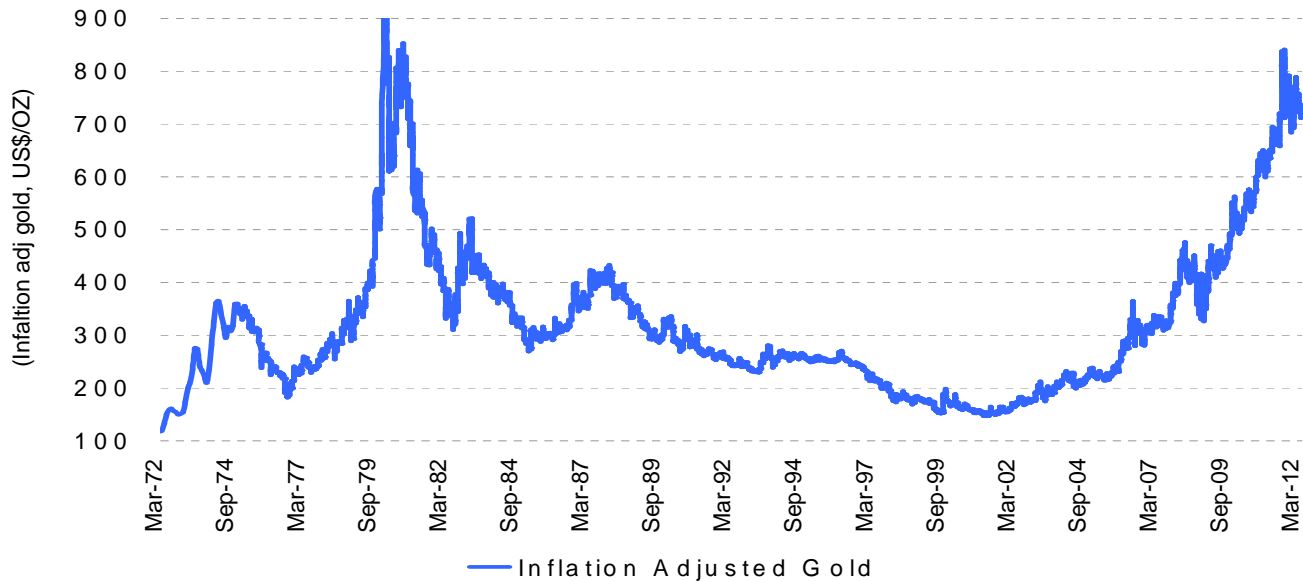
	<u>FY12</u>	<u>Remarks</u>
Net Gold imports as % of GDP	2.3	- Current trend ~ 30% drop in volumes - Reduces ~ 0.5% Current account deficit
<hr/>		
	<u>FY12</u>	<u>Remarks</u>
Net Oil imports as % of GDP (avg. Brent \$115)	~5.0	- Current price ~ \$95 - Reduces ~ 1% Current account deficit

Fiscal Deficit

US\$ Bn.	FY12	Rs. at 50		Rs. at 55	
		US\$90	US\$100	US\$90	US\$100
Oil Price					
Gross Under-recovery	28.7	12.8	20.5	19.4	26.5
Govt. Share	17.3	7.7	12.3	11.7	15.9
Govt. Share % of GDP	0.93	0.40	0.64	0.61	0.83

Besides, govt. has been increasing diesel prices in June each year (Rs. 3/- in Jun'11 & Rs. 2/- in Jun'10)

Peaking Gold Prices ?



Source: Anand Rathi securities

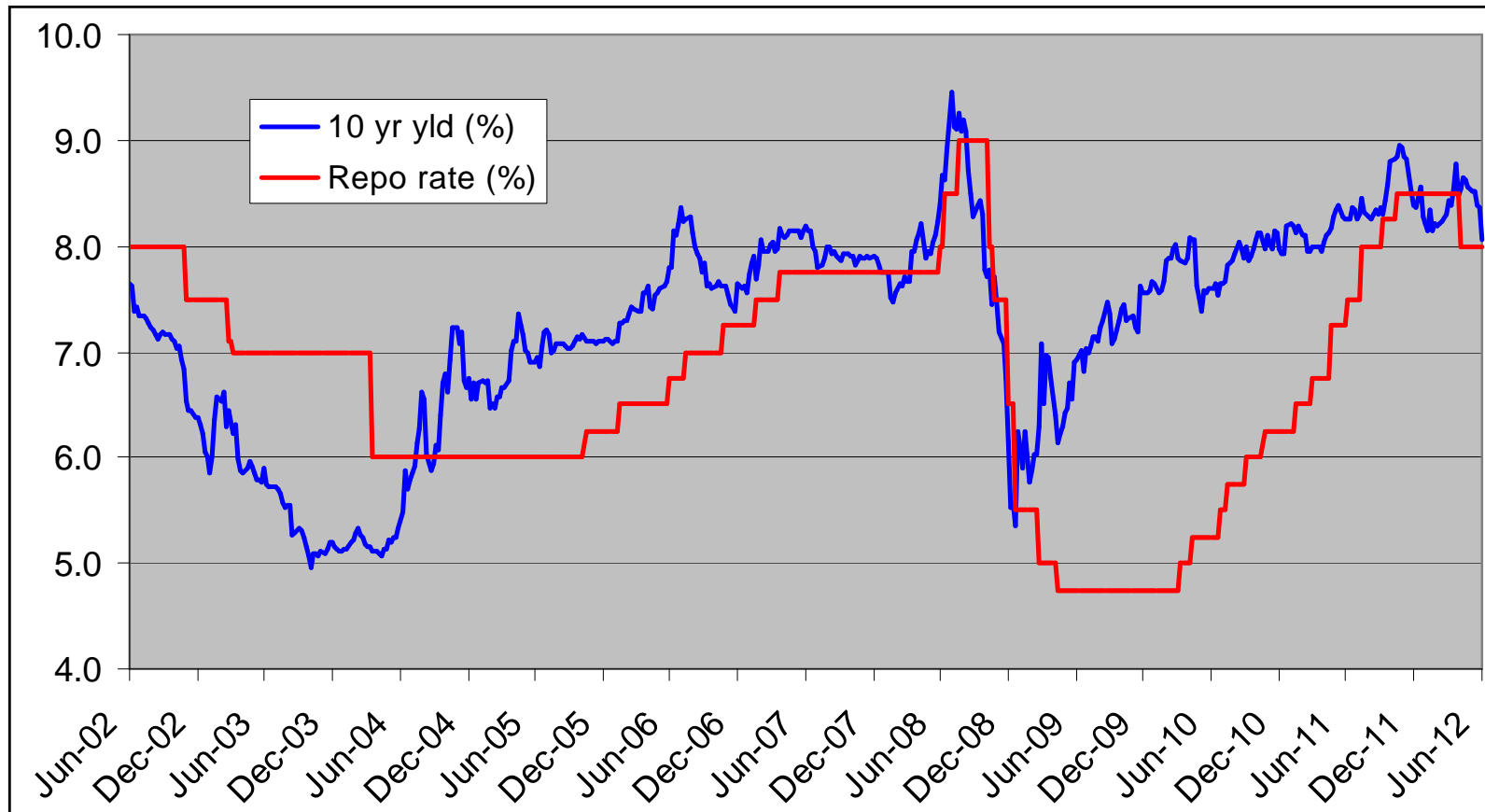
Last 2 quarters gold import volumes have dropped significantly year on year

	Volume in tonnes	Value in USD Bn.	Year on year	
			Volume	Value
Oct - Dec '11	173	9.1	-42.1%	-28.4%
Jan - Mar '12	208	10.9	-28.5%	-12.9%

Source: World Gold Council

Are Interest Rates Peaking ?

10 year G-sec yield



Source: Bloomberg

Government Policy Inaction

Change is slow and difficult in a democracy ruled by a coalition government

- Pending policy on FDI in Retail, Insurance, and Aviation
- Pending Pension Reforms, Mining policy, etc.

Every crisis has in the past resulted in change

- Opening of economy in 1992, triggered by BOP crisis
- Increase in diesel prices, led by unsustainably high subsidy burden
- Improving internal security set up, driven by repeated terrorist attacks

Current challenging environment should lead to changes for better

- Transparency in land acquisition policy
- Competitive bidding for natural resources
- Reforms in power distribution, due to high SEB losses
- High subsidy burden / fiscal deficit should lead to changes in prices and subsidies (UID linked, etc.)

India – Right Direction, Slow Pace

- In India, things do happen but take more time
- Following table illustrates that things move slowly initially, however over time implementation accelerates

Sector	Particulars	8 th Plan(FY92-97)	9 th Plan(FY97-02)	10 th Plan (FY02-07)	11 th Plan (FY07-12)	Remarks			
Power Generation	Power Capacity Addition (MW)	16,423	19,015	21,110	53,922	Sector was opened to private sector in early 90's but introduction of Electricity Act, 2003, access to fuel and market prices of power led to significant jump in capacity addition only in 2007 - 2012			
Sector	Particulars	FY01	FY03	FY05	FY07	FY09	FY11	FY12E	
Roads	Roads Awarded (kms)	895	671	1305	1735	643	5083	7000	Roads awarded in FY 11 and FY 12 were more than the entire period from FY 2001 – FY 2010
Telecom	Average outgoing per minute (Rs.)	6.4	3.2	2.4	1.2	0.8	0.5	0.5	<ul style="list-style-type: none"> • Though opened to private sector in mid 90's, growth picked up only after 2003 as Calling Party Pays and revenue sharing was introduced • Last 5 years' growth has been explosive; teledensity has gone up by 5 times in the last 5 years
	Mobile Subs (mn)	4	13	56	162	393	812	910	
	Mobile teledensity (%)	0.4%	1.2%	5.1%	14.3%	33.3%	67.1%	75.0%	

Source: Planning Commission of India, NHAI, TRAI, BoFA Merrill Lynch and internal estimates

India - Equity Markets

Adverse times => low valuations => good investments

- Good returns are seldom made on investments made in good times; rather, good returns are typically made on investments made in adverse times
- In good times when the stock markets are doing well, companies typically trade above fair values; in adverse times when markets are not doing well they tend to trade below fair values
- Therefore, investments made in adverse times typically yield above average returns and vice versa
- The tables on the next page illustrate this clearly

Investments made in good times

- ❖ This table summarises the 3 and 5 year returns for the Sensex from times when the environment was good, market sentiment was positive and valuations were expensive, post year 2000

Time	Sensex Level	1 year forward P/E	Main news / reasons	Total Returns after 3 years#	Total Returns after 5 years#
Jan-00	5205	25	High optimism in technology stocks	-38%	26%
Dec-07	20287	26	Booming global economy, optimistic markets	1%	-15%*

Investments made in adverse times

- ❖ This table summarises the 3 and 5 year returns for the Sensex from times when the environment was challenging, market sentiment was negative and valuations were low, post year 2000

Time**	Sensex Level	1 yr forward P/E	Main news / reasons	Total Returns after 3 years#	Total Returns after 5 years#
Oct-01	2989	11	9/11 attack on WTC, global markets collapse	91%	334%
June-04	4795	10	Unexpected defeat of BJP in general elections	206%	202%
Nov-08	9093	11	Sub-prime crisis - Lehman collapse	77%	N.A.

Dividends not accounted for ; Past Performance of the Sensex may or may not be sustained in future.

** Index level is taken as on the next month end after the crisis; * This return is from Dec 2007 till April 2012

The above tables are for illustration purposes only and should not be construed as an investment advice. It does not in any manner imply or suggest current or future performance of any HDFC Mutual Fund Scheme(s). N.A. – Not available

An investment paradox : Mistiming by majority

- Buy low and sell high is what everyone suggests and that is what everyone would like to do; the reality however for a typical investor in equity mutual funds is exactly the opposite

This behavior is best illustrated by the following table

Annual net sales of equity funds across different phases of the market

	FY03	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12
Equity Net Sales (Rs crs)	118	7205	7398	36155	29916	52701	4084	1456	-11795	504
BSE Sensex (March end)	3049	5591	6493	11280	13072	15644	9709	17528	19445	17404
Average forward P/E	10.34	11.39	11.62	13.14	15.79	20.56	15.69	17.24	17.74	14.75

(Source: Equity net sales – AMFI ; Average forward P/E is the monthly average P/E for the year – Bloomberg)

Only Rs. 118 crs
invested at P/E's ~10

Over Rs. 50,000 crs
invested at P/E's ≥ 20

Only Rs. 500 crs
invested
at P/E's < 15

Markets – negatives priced in ?



P/E's are significantly lower than long term averages; thus there is room for P/E's to increase over time

God and Equities

दुःख में सुमिरन सब करे सुख में करै न कोय।
जो सुख में सुमिरन करे तो दुःख काहे को होय।।

This is a couplet by Saint Kabir, a much loved and revered saint of 15th century. It means the following:

[In anguish everyone prays to Him, in joy does none
To One who prays in happiness, how sorrow can come]

Stock markets and God do not have much in common. Probably, that's why, the above does apply to stock markets but in reverse.

An adapted version of the above for stock markets would be as follows:

[In good times everyone invests, in adverse times does none
To the wise one who invests in bad times, wealth should come]

The moral of this is that remember God in good times and equities in bad times. If this is done, then chances are one will avoid both - bad times in life and poor returns on investments.

Summary

- Indian economy is a long term growth economy and is likely to be the 5th largest in the world by 2020*
- The current challenges facing us are mostly internal and the economy should do well again, when these are overcome
- Lower crude prices and falling gold import volumes should improve current account and fiscal deficits
- There appears to be a sense of urgency amongst policy makers to take steps that are conducive to growth
- Low P/E's of today represent an opportunity for the long term investor
- Key risks are spike in oil prices and lack of serious effort to curtail fiscal deficit

*Source: BofA ML



Thank You

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