

CONTACT

A Monthly Fund Update from JM Financial Mutual Fund

Details as on December 31, 2009

Market Update - Equity

ECONOMY

The trade deficit for October 2009 came in at USD8.8 billion, declining on a year-on-year (y-o-y) basis while expanding on a sequential basis. On a y-o-y basis, the trade deficit fell by 25% whereas the sequential increase stood at 13.3%. Notably, the pace of decline (year on year [yoy]) in exports moderated in October 2009 as exports contracted by 6.6% yoy. According to provisional data, the exports have registered a turn around with 18% y-o-y growth during November 2009, though driven by lower base effect.

In October 2009, the Index for Industrial Production (IIP) registered a growth of 10.3% yoy, which stood well below the consensus estimate of 12% yoy. The manufacturing segment posted the highest growth at 11.1% yoy followed by the mining and electricity segments with 8.2% and 4.7% growth respectively. From a use-based perspective, the growth in the capital goods segment continued its upward trend, registering a stellar growth of 12.2% vs the 4.2% rise seen during October 2008. The growth in consumer goods stood strong at 11.8% vs the 0.9% contraction seen during the previous year.

The inflation rate for November 2009 came in at 4.78%, against the street estimate of 4.2%. This indicates a 344-basis-point increase from the October 2009 inflation rate of 1.34%, led primarily by rising prices of food products and articles. Excluding the food products and articles, the inflation rate is quite contained.

Globally, the macro economic data continues to point towards signs of economic recovery, pushing central banks to ponder over the withdrawal of various stimulus measures announced earlier.

STOCK MARKET

As expected by us, markets continued their listless performance from previous month and moved in a tight range for most of December 2009. However last couple of trading sessions for 2009 saw the market crossing its previous highs for 2009 and thus breaking the range in high it operated for the last 3 months. Nifty closed 2009 at 5201 and Sensex moved to 17464. Flows from both FII and FI remained strong and cash levels have been steadily going down.

MARKET OUTLOOK

Sensex is now over 17000 and at current levels trades at over 16x FY11 which now puts it in a historically traded average band. India has been a beneficiary of strong flows like the rest of the Asian peers and there is a strong likelihood of the continuation of the flows in the near future. On the other hand, there appears to several large offerings lined up through the IPO, QIP routes etc as a consequence of corporates trying to use the optimism in the environment to raise equity capital. We expect the markets to remain strong for the initial part of Q1CY10 till the deluge of IPOs/FPOs/QIPs arrive towards the end of fiscal 2010. We believe that Q3 results would not be of much consequence as market is focusing on broader macro factors which appear quite robust. The Credit Policy of January 2010 will be a keenly watched event and may have a bearing on the interest rate sensitives in the market.

Broadly we are reasonably confident of the indices to continue their uptrend for 2010. We might see reduced volatility on the benchmark indices. We see that risk appetite has increased dramatically and the action has decisively moved to midcap and small cap end of the market. It is expected that stock specific action will pick up substantially and which appears to be a major trend for 2010. Our portfolios are well positioned to take benefit of the changed environment.

Market Update - Derivatives

Both the Nifty and the Sensex traded in a narrow range throughout the month of December, thanks to lower participation by market players on the back of holiday season. With volumes dwindling in the market, the cost-of-carry remained low and rangebound. Rollovers to the January settlement were better in the single stock futures and happened at similar levels of the previous expiry. The cost-of-carry for January has started on a lower note. As we have been saying, increase in volatility will be helpful to unwind the existing arbitrage positions and churn the portfolio, thus enhancing the returns of the scheme. With the 3rd Quarter results, Credit Policy and Budget expectations as the key triggers it is expected that market volatility will increase, which may help in boosting returns in the fund.

Indicators	Current Month	Last Month	M-o-M Variation
Forex Reserves* USD Bln	283	285	(2)
Credit Off take* - Rs Crs	2,941,293	2,891,713	49,580.00
Credit Deposit Ratio *	70.34	69.39	0.95
WPI Inflation*(%)	4.78%	1.34%	3.44%
10-Year Yield - India* (%)	7.60%	7.20%	0.40%
10-year Yield - USA* (%)	3.78%	3.20%	0.58%
Exchange Rate* USD/INR	46.75	46.64	0.11
Brent Crude per/bbl*	77.50	77.91	-
Reverse Repo-Daily Avg Rs Crs	70,000.00	103,000.00	(33,000.00)
Repo Average-Daily Avg Rs Crs	-	-	-

* Data Reported as on month-end, Source RBI, WSS & Bloomberg.

Government bond yields have hardened on back of stronger than expected economic data and fear of an earlier than expected monetary tightening by the RBI. Though the concerns of supply of government bonds have receded, the market is now caught with the fear of monetary tightening. Announcement of an additional spending to the tune of INR 27000 crores by the finance minister during the FY 2009-10 have also spooked the market. India's Q2 2008-09 GDP rose at 7.9% much faster than the market expectation of 6.9%. Most Research agencies have now revised the year end GDP target in the range of 7.00-7.50% for the FY 2009-10. The Index of industrial production is growing at around 10.00% since the last 3 months and is expected to remain strong in the coming months. Headline inflation was at 4.78% for the month of November-09 on back of a sharp rise in primary articles-(Primary articles have registered a growth of 11.85% in the month of November 09). The 10-year benchmark bond rose by about 40-45 basis points to end at 7.60% as compared to the previous close of 7.20%.

Factor: Inflation

Short Term: Negative

Medium Term: Negative

Headline inflation for the month stood at 4.78% as compared to 1.34% in the month of October-09. Headline inflation continued to remain higher on account of sharp rise in food prices. The absolute index level rose to 245.4 as compared to 242.2 in the previous month. Primary index rose to 284 from 280 during the last month. The revisions for previous week inflation has been sharply higher by about 100-150 basis points. In the recent policy statement RBI has raised concern on rising inflation expectation and raised the year end target of inflation from 5.00% to 6.00%. For the month of December 2009 inflation is likely to be higher in the range of 6.25%-6.75% on account of higher food prices.

Factor: Liquidity

Short Term: Positive

Medium Term: Neutral

Domestic liquidity situation continued to remain surplus. Easy liquidity

conditions were evident as RBI received average bids of Rs. 70000 crores during the month in the daily reverse repo auction. Inter bank call rates & CBLO rates continued to remain soft on account of surplus liquidity. Going forward in the month of January 2009, domestic liquidity situation expected to remain comfortable. Money market rates are expected to remain range bound on back of ample liquidity. In the medium term it is expected that there may be pressure on liquidity as RBI decides to exit of the easy monetary policy stance.

Factor: Global interest rates

Short Term: Neutral

Medium Term: Negative

Global interest rates firmed up during the month as the 10 year benchmark US treasury yield rose about 50 basis points on good economic data and huge supply of US treasuries. Though the Federal Reserve has assured the market of lower policy rates till the time economy is on a firm footing. US dollar continued to remain firm during the month on expectation of recovery in the US economy. The Dollar index touched a high of 77.91 as compared to 74.87. Reversal of interest rate cycle in developed countries will be slower than developing countries and most developed central banks are likely to keep policy rates low till the time clear signs of growth emerge.

Factor: Forex

Short Term: Positive

Medium Term: Positive

India's Forex reserves stood at a \$ 283 billion as on 25th December. INR remained under pressure during the month and traded in narrow range of 46.54-46.75. Despite strong economic data, the INR weakened due to strong rebound in the dollar index and heavy positioning in INR. Sharp rise in the dollar index also led to weakening of the INR. INR is expected to remain in the range for the next month with a positive bias on weakness in the USD and strong inflows.

OUTLOOK

Recent statements from Finance ministry and RBI has given indication that RBI may be close to the end of the easy monetary cycle and is prepared to reverse the cycle if macro economic data continues to remain robust. It is expected that the RBI would take a preemptive step and hike the CRR by 50 basis points as a first step towards monetary tightening followed by a hike in repo and reverse repo rate in view of the rising inflation. The timing of this monetary action will depend on the impending macro economic data. The market has discounted a CRR hike in the impending policy meet scheduled in the month of January 2010. Government bond yields are expected to remain under pressure as the market prepares itself for tight monetary policy. Impending macro economic data and appetite for government securities in the impending auctions will give further direction to the yield movement. Credit spreads are expected to remain in the band of 100-125 basis points. Domestic liquidity situation is expected to remain comfortable in the term. Money market asset rates are expected to trade in a range on easy liquidity conditions.