

Monthly Market Round-up - Equity

December 2008

Christmas cheer to end the year

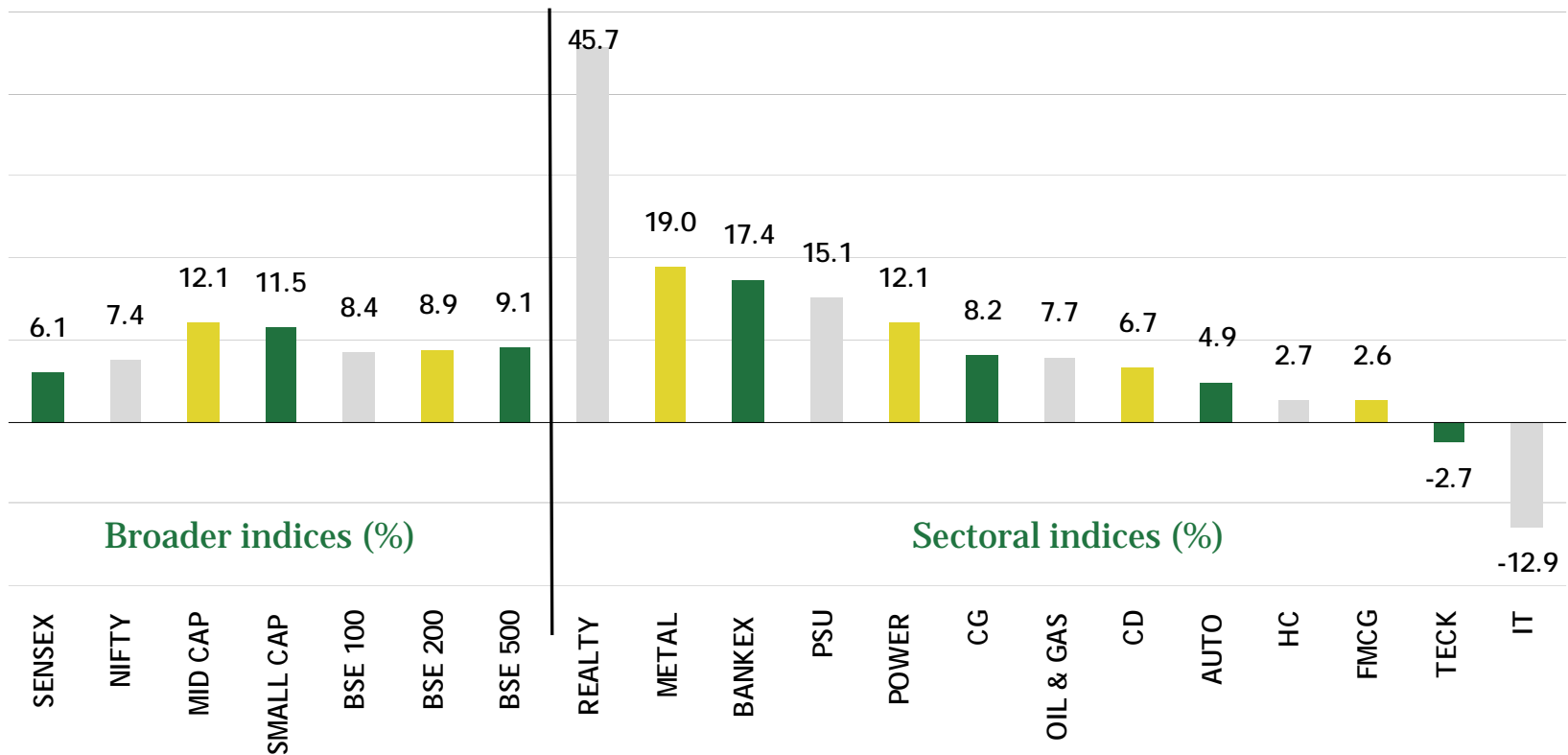
- Equity markets rally in most parts of the world
- This was in spite of economic data from the developed nations as well as emerging economies indicating a marked deceleration in growth
- World GDP growth forecast for 2009 has dropped to below 1%
- Credit markets start to unthaw and normalize but appetite for risk remains low
- Lead economic data for India (exports, IIP) also indicate a sharp slowing
- India unveils a series of monetary and fiscal measures to boost growth

Global Equities

Index	Country	Closing Price*	1 Month Return (%)	YTD Return (%)	Category
SSE Composite Index	China	1820.81	-2.69%	-65.39%	EM - Asia
BSE Sensex	India	9647.31	6.10%	-52.45%	EM - Asia
Kospi	South Korea	1124.47	4.50%	-40.73%	EM - Asia
Taiwan Weighted	Taiwan	4591.22	2.93%	-46.03%	EM - Asia
Thailand SET 50 Index	Thailand	316.45	13.09%	-49.83%	EM - Asia
Jakarta Composite Index	Indonesia	1355.41	9.17%	-50.64%	EM - Asia
KLSE	Malaysia	876.75	1.22%	-39.33%	EM - Asia
Ibovespa Sao Paulo Index	Brazil	37550.31	2.61%	-41.22%	EM
Mexico IPC	Mexico	22380.32	8.99%	-24.23%	EM
Russian RTS Index	Russia	631.89	-3.99%	-72.41%	EM
Philippine PSEi	Philippines	1872.85	-5.01%	-48.29%	EM
Merval Buenos Aires Index	Argentina	1079.66	8.62%	-49.82%	EM
HangSeng	Hong Kong	14387.48	3.59%	-48.27%	Developed - Asia
Nikkei	Japan	8859.56	4.08%	-42.12%	Developed - Asia
Strait Times	Singapore	1761.56	1.67%	-49.41%	Developed - Asia
Dow Jones	USA	8776.39	-0.60%	-33.84%	Developed
CAC 40 Index	France	3217.97	-1.37%	-42.68%	Developed
All Ordinaries Index	Australia	3659.30	-0.36%	-43.01%	Developed
DAX Index	Germany	4810.20	3.01%	-40.37%	Developed
Swiss Market Index	Switzerland	5534.53	-4.85%	-34.77%	Developed
FTSE 100	UK	4434.17	3.41%	-31.33%	Developed
MSCI World Index	--	920.23	3.06%	-42.08%	--

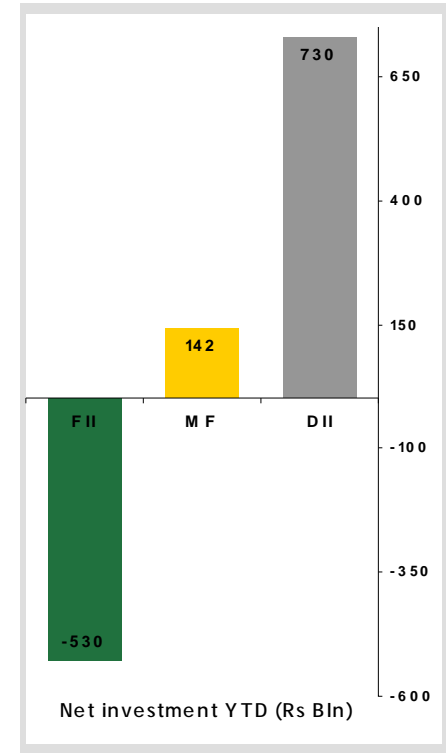
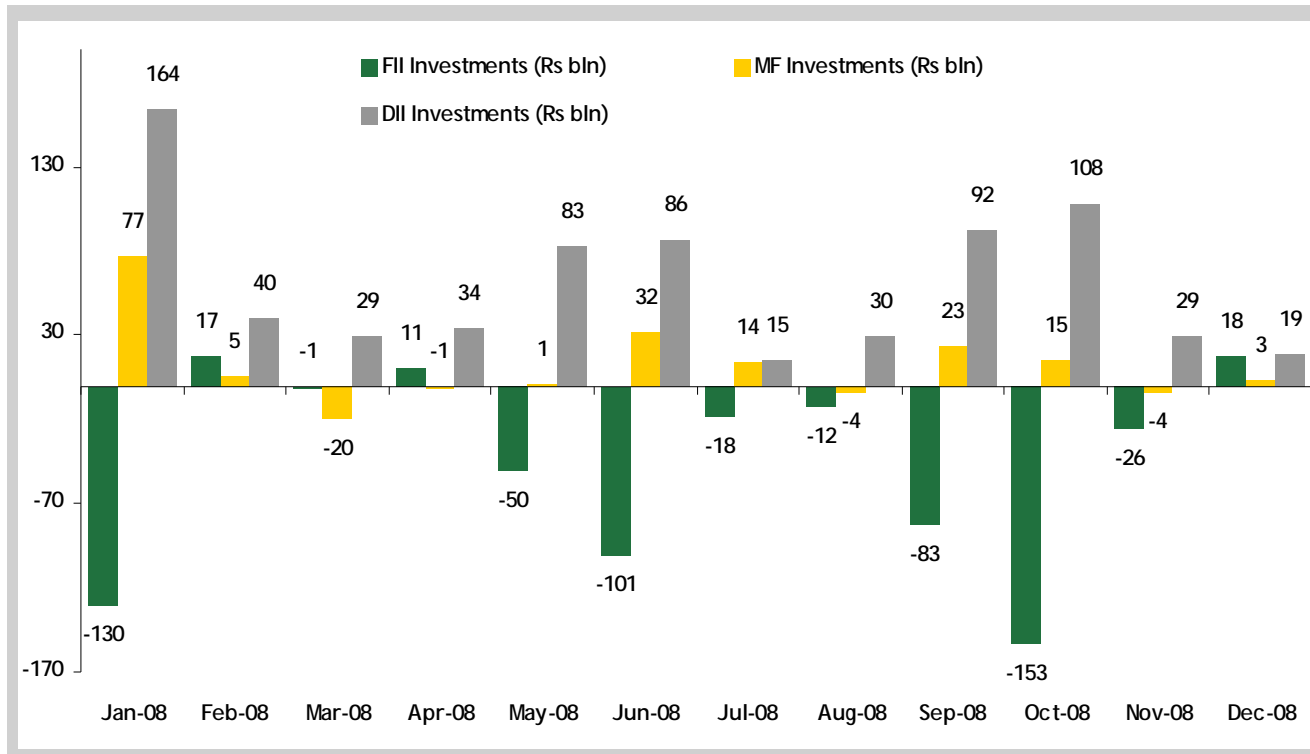
* as on 31st December 08. Source : Bloomberg
EM - emerging markets, Developed - developed markets.

Role reversal in sector performance



- The worst performing sectors of the year bounced the hardest
- Banking continued to do well due to improved liquidity and mtm gains in gilts
- IT was worst hit due to fears about growth
- The best performing sectors of the year brought up the rear this month

Domestic Institutional buying matches FII selling



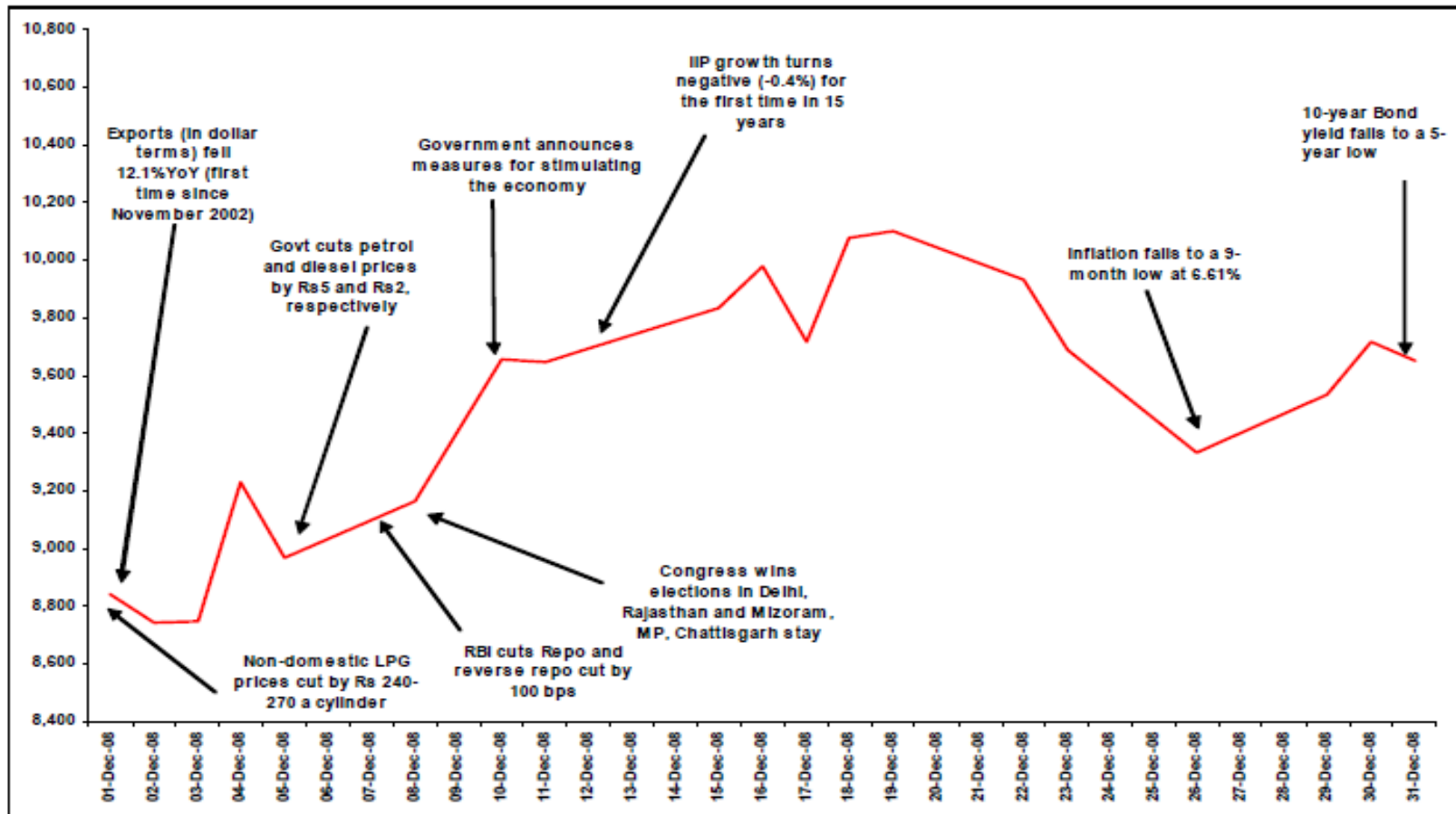
- FII selling abates as they turn net marginal buyers after 7 months
- Total domestic institutional buying YTD exceeds FII selling, but worryingly data for November indicates a decline in insurance inflows

Top Gainers / Losers - Nifty

Top Gainers for the month			
Gainers	52 week H/L	Last Price#	% Gain*
Unitech Ltd.	538 / 23	40.65	75.59%
Suzlon Energy Ltd.	2273 / 37	62.30	49.58%
Tata Steel Ltd.	935 / 149	217.20	43.46%
D L F Ltd.	1208 / 179	282.15	42.21%
Grasim Industries Ltd.	3765 / 886	1,219.85	37.65%
Top Losers for the month			
Losers	52 week H/L	Last Price#	% Loss*
Satyam Computer Services Ltd.	525 / 135	170.80	-29.7%
H C L Technologies Ltd.	330 / 104	115.30	-16.1%
Tata Consultancy Services Ltd.	1077 / 454	477.90	-14.6%
Infosys Technologies Ltd.	1994 / 1102	1,115.45	-10.3%
Cipla Ltd.	241 / 160	186.60	-6.8%

closing price as on 31st December 08.* one month performance as on 31st December 08. Source: nseindia.com

December timeline



Source: Bloomberg, Economic Times, Business Standard, Morgan Stanley Research

India Market Summary

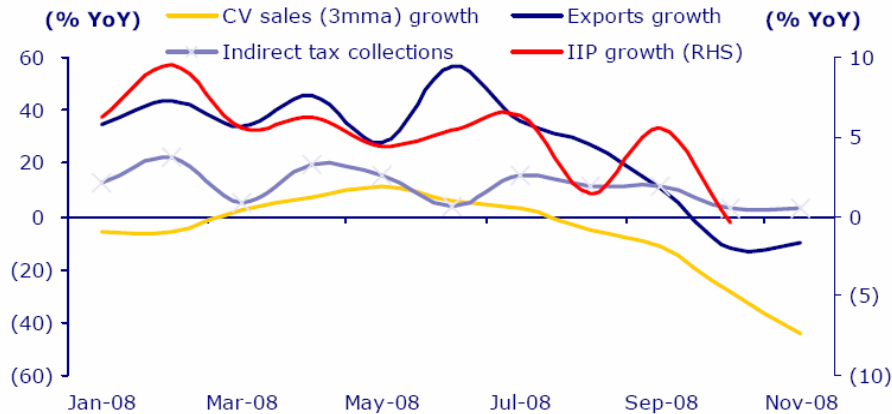
- BSE Sensex rose 6.1% for the month outperforming most equity markets for the month. In 2008 it lost 52.4% and unlike 2007, India finished as the third worst performing market. The MSCI India index (\$ denominated) is down by 65.1% for 2008.
- Key benchmark indices- the BSE Sensex and S&P CNX Nifty closed below the psychological 10,000 and 3,000 level respectively for the year.
- Market activity picked up in December underscored by rising trading volumes in the cash and the derivatives market and a 24% rise in market breadth. Average implied volatility fell 27% MoM as did the Put-call ratio.
- In December the Large cap index underperformed the mid and small-cap indices for the first time in four months. BSE Midcap and Small Cap index gained by 12.1% and 11.5% respectively
- FII Inflow in the cash market turned positive after seven successive months of selling. FIIs bought equities worth over US\$ 0.27bn in December. For 2008 the total outflow is over US\$ 12.6bn. Domestic Institutional investors (DIIs) were net buyers to the tune of Rs 19.1bn. Domestic MFs also bought shares worth Rs 3.4bn during the month
- Corporate governance issues also surfaced during the month as regards the proposed buy by Satyam Computers for two related companies. The move was finally aborted by the management.

Highlights for the month

- Inflation based on the wholesale price index (WPI) dropped to 6.38% for the week ended 20th December - a ten month low.
- The Index of Industrial Production (IIP) turned negative (-0.4%) for the first time in 15 years.
- Exports (in dollar terms) fell 12.1% YoY for the first time since November 2002.
- Reserve Bank of India announced Repo and Reverse Repo cut by 100 basis points during the month. It also announced measures to stimulate the economy.
- The 10 year bond yield slid to near 5%.
- The government also unveiled a set of fiscal measures to support growth
- A sharp drop in advance tax payment by Indian companies in the third quarter points to the pressure on profits

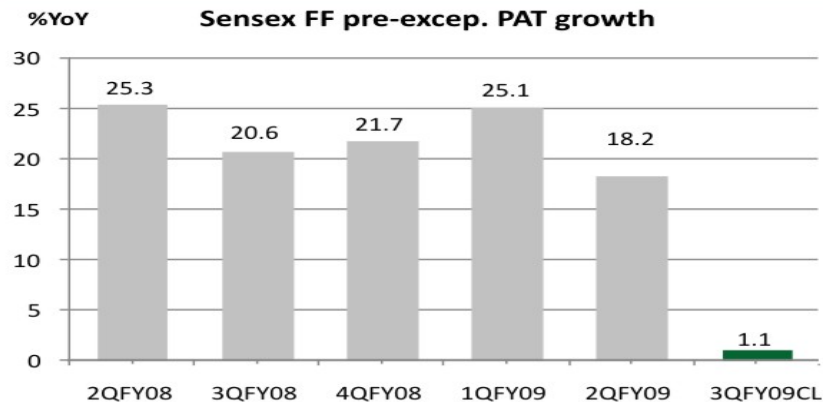
Preview of Earnings for Quarter ending Dec 2008

Sharp slowdown since Oct-08



Source: CLSA Asia-Pacific Markets

Earning growth trend for the Sensex

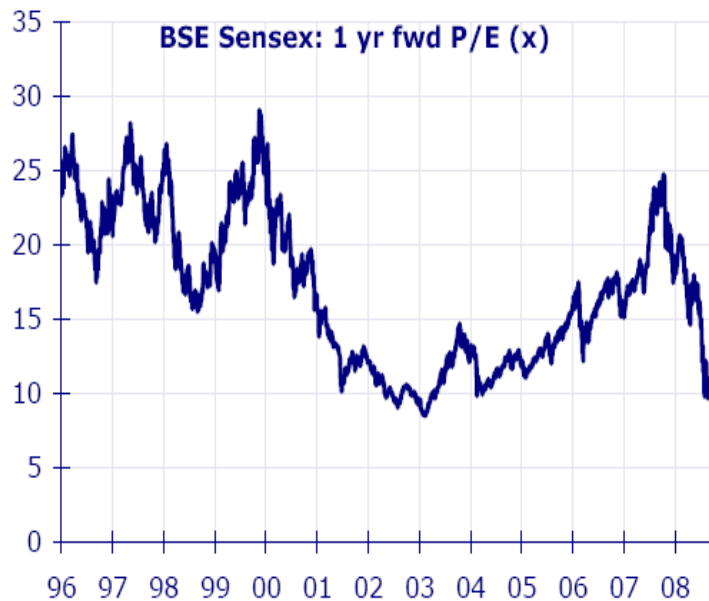


Source: CLSA Asia-Pacific Markets

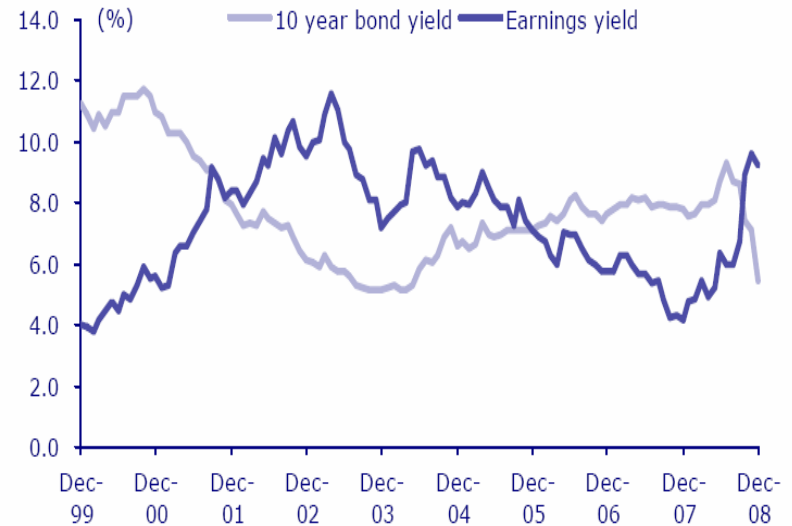
- Lead economic data such as commercial vehicle sales, exports, industrial production and tax collections indicate a sharp slowdown in the quarter gone by
- The quarter was dominated by news flow on production cuts, cost cutting measures, layoffs, closures and freeze/review in investment plans
- As a result earnings growth for the Sensex is likely to slow abruptly and dramatically to just above 1% in the quarter ended December
- These numbers may be at further risk if companies account for costs/losses from balance sheet and off balance sheet items

Valuations

Sensex 1 yr forward P/E



Earnings yield vs bond yields

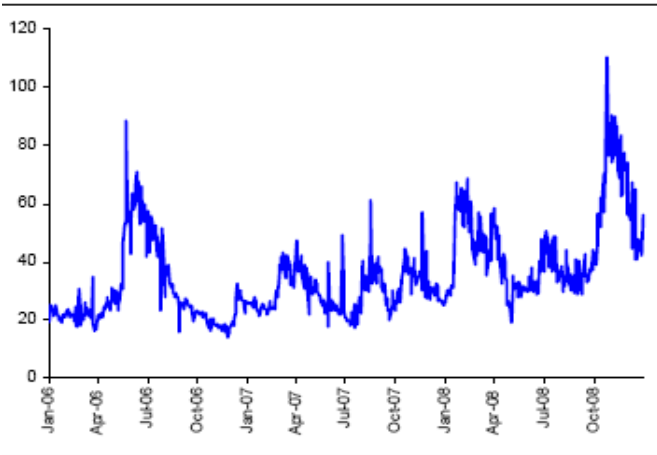


Source: CLSA Asia-Pacific Markets

- On trailing P/E (11.5x) the Sensex is trading within 15% of its all time low
- Forward P/B multiple, at 1.8x, is within 18% of the all time low
- The earnings yield gap (Inverse of P/E - 10 year bond yield) is significantly positive

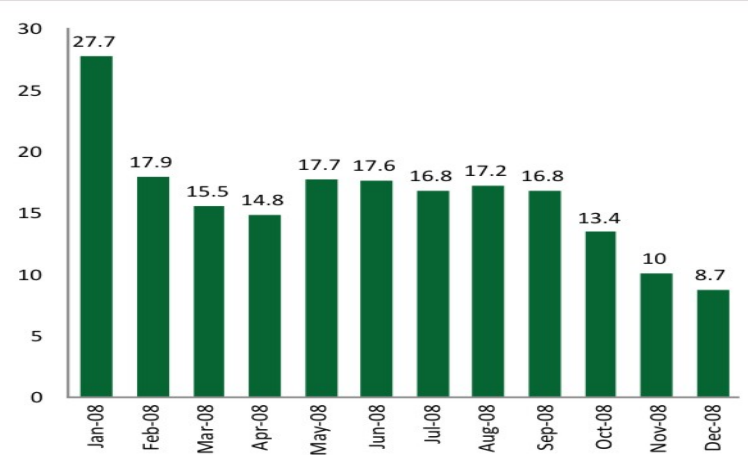
Market indicators- Panic is subsiding, volumes pick up

S&P CNX Nifty Index: Implied Volatility



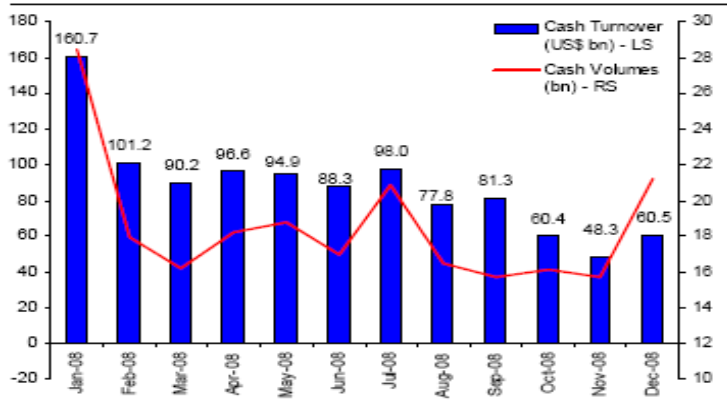
Source: Bloomberg, Morgan Stanley Research

Average Open Interest for the Month



Source: Bloomberg, Morgan Stanley Research

Cash Trading: Turnover and Volumes

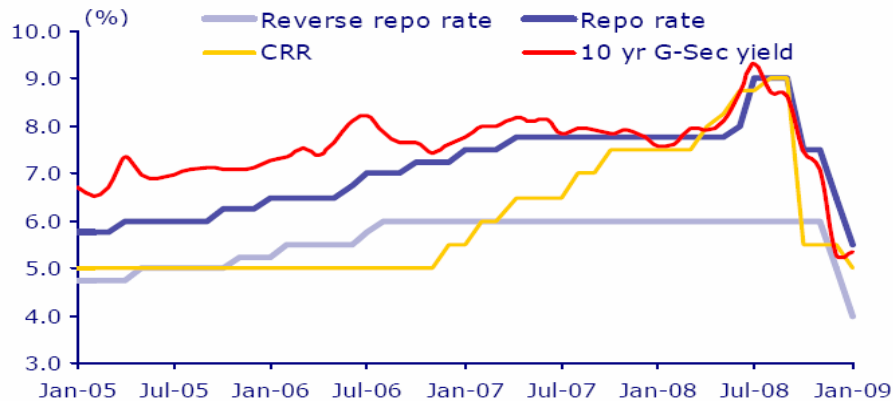


Source: BSE, NSE, Morgan Stanley Research

- On a monthly average basis, implied volatility continued to fall from its peak in October falling 22.4% to 54.3% in December
- The Average open interest was down 13% MoM in December, a 27-month low and is 64% off its January 2008 peak
- In December, cash trading volume rose 25% MoM but still remains a good 63% below its December 2007 peak

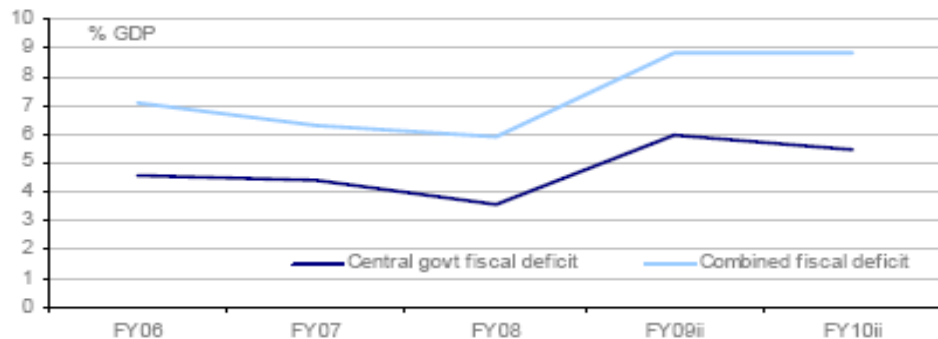
Spotlight : stimulus package

Policy rates and 10 yr G-sec yield



Source: CLSA Asia-Pacific Markets

Figure 23: Fiscal deficit will remain high next year, limiting fiscal room for stimulus



Source: IIFL Research

- Cumulatively the RBI has cut CRR by (50bps), repo (200bps) and reverse repo (200bps) since December
- On the fiscal front the government has cut excise duties, relaxed the borrowing limit of the states and allowed IIFCL to raise a total of Rs 400bn of tax free bonds for refinancing bank lending to infrastructure projects.
- Further it also plans to support state owned banks with new capital and promote a separate funding window for NBFCs
- The governments ability to provide a large fiscal stimulus is constrained by the fiscal deficit
- The monetary and fiscal measures have a single objective - to increase the quantum of credit and capital available for lending

Looking Ahead....

- Earnings deceleration will be visible during the corporate earnings announcements for the quarter ended December 2008
- Save and except extreme company specific shocks we believe the markets have discounted a poor earnings season
- The markets will focus on signs that the monetary easing is converting into lower interest rates and a pickup in demand for interest rate sensitives
- We believe that most macro risks in India are now well discounted by the price - but company level risk remains heightened
- The new US president takes charge late in January and is expected to announce a large stimulus package which could keep global markets buoyant in expectation.

Investment view

Short term

- Challenging growth environment with GDP growth likely to decelerate next year to under 6%
- We now estimate that earnings during FY08-10 are likely to be unchanged
- Inter-sector and Intra-sector performance variations are likely to increase

Long term

- India will double in size, adding \$1trillion to GDP over the next 5-7 years.
- Over the same period earnings should match nominal GDP growth @12-14% p.a but will be back ended
- If growth accelerates from 2010 then returns would be boosted by an improvement in valuations

Events Calendar

Date	Economy	Data release / Event	Period	Prior
12-Jan	India	Industrial production (% ,Y-o-Y)	November	-0.40
27-Jan	India	RBI Policy Meeting	--	--
	India	WPI Inflation	Every Thursday	--

Date	Economy	Data release / Event	Period	Expectations	Prior
8-Jan	Euro zone	Real GDP (% , Y-o-Y)	Q3 FY08	0.60	0.60
8-Jan	UK	BoE interest rate announcement	8-Jan	1.50	2.00
9-Jan	US	Unemployment Rate	Dec	7.0	6.7
15-Jan	Euro zone	ECB interest rate announcement	15-Jan	--	2.5
22-Jan	Japan	BoJ interest rate announcement	22-Jan	--	0.10
29-Jan	US	FOMC interest rate decision	29-Jan	--	0-0.25

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