JM FINANCIAL

Bull's Eye

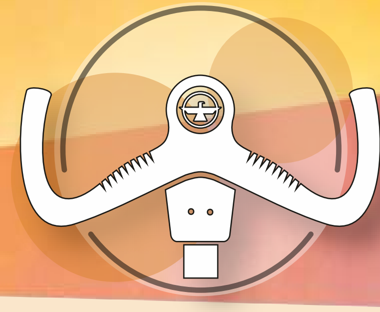
A COMPREHENSIVE MARKET WATCH

SOAR TO NEW HEIGHTS
WITH OUR EXPANSIVE RESEARCH

Vol. 101 | June 2018

CONTENTS

1. PIECE OF MIND



Global equities continue to face headwinds around growth cycle, protectionism, geopolitical risk and elevated valuations. We are witnessing a rise in the risk premium specifically in case of twin deficit countries like India, amidst rising crude prices. As we move to the second half of CY18, we see a rise in the risk premium of India even further on account of rising political uncertainty, higher inflationary environment, beginning of RBI's rate hike cycle and rich valuations.

As investors continue to await broad-based earnings turnaround, India Inc. disappoints yet again in the current quarter. For the 4Q, MSCI India EPS grew merely by 2%YoY against market expectation of 10%+ growth, dragged down by disappointing earnings reported by SOE banks. Since the start of 4Q, MSCI consensus EPS (CY18) has been cut by 2.6%, driven by the earnings cut in Pharma (-9%), Auto (-9%) & Banks (-7%). Metals being is the only sector witnessing large scale earnings upgrades (+8%). Since February, 2018 consensus has downgraded MSCI India earnings estimates by 5%, largest cut in Non-Japan Asia region.

Despite a rise in the global crude oil production (96-97mbpd), looming threat of U.S. sanctions against Venezuela and Iran remains key headwinds for the supply side of the market. Absolute U.S. oil inventories have continued to fall and are well below their 5 year' average. Global oil demand is expected to increase by 1.5 - 1.8 mbpd in 2018 to reach to 99.3 mbpd. IEA forecast U.S., China and India to account for 73% of incremental oil demand in 2018.

For India, an under budgeted oil subsidy of ₹208 billion in the budget is further putting a pressure on fiscal situation (weak rupee, lower GST collection). Although, crude prices have softened in recent days the trend structurally remains upwards. The inflationary pressure further exerted from rising crude will have a large bearing on RBI's decision on policy rates. We expect RBI to turn hawkish and see possibility of it raising inflation expectations sooner than later. The difference between the RBI's repo and short-term bond yields now stands at 90 bps as against 10 years average of 25 bps. This indicates bond markets are already pricing in, two 25 bps rate hike in this calendar year. However bond yields & earnings yield gap indicates equity markets have not factored in the beginning of the rate hike cycle yet.

The political uncertainty continues to be on rise in India. After debacle in Karnataka elections, BJP lost another parliamentary bypoll (the 3rd in three months) in the important state of UP. Bypolls were held for four national and 10 state assembly seats. In the assembly seats, the BJP/allies won just one of the 10 seats, down from four earlier. BJP and its key ally lost a seat in important state of Maharashtra and Bihar as well. The next important political event will be the state elections in the four states in December, 2018.

Despite the disappointment in earnings, markets still continue to trade at over 19x NTM earnings. The difference between the risk free and the earnings yield has, in the past, been a good indicator of risk-reward between the bond and equity markets. The yield gap has been higher than 250 bps over the past few weeks, the highest since December, 2007. With the persistence of high crude prices, focus on India's fiscal deficit and currency will increase in the coming months. From market standpoint, either the inflation has to give in or growth has to surprise on the upside for the valuations to be sustained at the current levels. Based on the past few quarters' results, the risks of an upgrade to earnings growth appear low. If inflation risks are also on the upside, the obvious casualty could be the broader market multiples.

2. TECH DESK

Positive Trend Remains Intact

The Nifty lost 3 points over the month to close at 10,736. It closed on a negative note compared to previous month. After closing almost positive for 2 consecutive months on the monthly chart, last month Nifty closed on a marginally weaker note. The only positive key takeaway is that the intensity of fall was minimal. In line with our presented view, the markets witnessed a corrective last month that saw the Nifty test our target support zone of 10,400 - 10,500. The damage in the broader markets was far greater with many stocks losing anywhere between 3-5%. Global markets' news flow, high crude oil prices and bond yields were partly responsible for the same. The index heavyweight banking index outperformed while the midcap index underperformed in the month of May.

Coming back to Nifty, the index saw a mini capitulation when it briefly moved around the level of 10,400. On most technical parameters too it turned oversold calling for a sharp recovery. The expected recovery has played out very well in the last 5-7 days. The bank Nifty once again led the recovery and it was also one of the leading sector which was responsible for taking Nifty higher.

The Nifty is still forming higher tops & higher bottoms on the weekly charts which is a positive signal as per Dow Theory. It is also making higher high on the monthly charts. Presently, Nifty is trading around a make or break resistance zone of 10,700 to 10,730 levels and a movement of 150 to 200 points can be expected on either side from this zone, preferably on the higher side. The resistance zone of 10,700 to 10,730 holds a lot of significance because the Nifty has shown a lot of resilience near this zone in the past. Once past 10,700 to 10,730 resistance zone on a closing basis, the Nifty would not take much time to hit the Karnataka result day high of 10,929 and then towards new life highs.

Technical studies - Fibonacci retracement and moving averages

The Nifty has risen continuously month after month after testing 9,950 levels in the month of March, 2018. The recent correction which started in the month of May, 2018 has almost retraced 0.50% Fibonacci retracement level of the entire rally starting from 9,950 levels to 10,929 levels. On the downside, the immediate support level for Nifty is at 10,400 and next support is at 10,200 levels. On the higher side, the zone of 10,900 - 10,930 is likely to act as a stiff resistance. The slope of the moving averages used by us in determining trend is sloping marginally upward and has also given bullish crossover few weeks ago i.e. short term moving average crossing above longer term moving average. Any weekly decisive close below 10,200 (plus/minus 50 points) would change the equation back in favor of the bears.

Conclusion

Overall, we think the month of June could see volatility with a positive bias. This is on account of the fact that the set-up is strong. Overall, we think that the markets are likely to continue the rally that started off a couple of months ago. We feel that the current leg could take the index into the 10,900-10,930 area on an immediate basis and in the best case scenario it can test a level of 11,100-11,200 on the higher side where the strongest medium-term resistance exists. The above view would be negated provided Nifty closes below 10,200 (plus/minus 50 points). The Bank Nifty is likely to face major resistance around the 27,500-27,700 mark on an immediate basis and in the best case scenario it can test a level of 28,600 on the higher side. The Banking index (Nifty Bank) is likely to find support in the 26,000-26,200 area where fresh longs may be considered for the medium-term target of 28,500-28,600. The IT, Banking, Capital Goods and FMCG sectors are likely to outperform.

3. FRESH PICK

Aditya Birla Capital

BUY
12 Months Price Target - ₹170/-

A diversified financial play with several growth drivers
Aditya Birla Capital Limited (ABCL) is a diversified financial company that operates across NBFC, housing finance, asset management, insurance and financial advisory business segments. The strength of the ABCL franchise lies in the following: a) End-to-end product offerings across customers' lifecycles to address their financial, protection and investment needs; this helps customer retention and cross-selling while providing operating leverage. b) Strong parentage has kept cost of funds competitive, while stringent underwriting norms have helped maintain healthy asset quality. c) A rapidly expanding market share, in key segments such as in lending (5th largest in terms of AUM among private NBFC players as of FY18), life insurance (8th largest in terms of APE as of FY18 with a market share of 3.1% among private insurers and 1.6% in the industry) and AMC (3rd largest in terms of AUM as of FY18 with a market share of 10.8%).

With a strong management team under the leadership of Mr Ajay Srinivasan, we expect ABCL to deliver profitable growth across various business segments going forward.

We believe there are multiple growth drivers in place for each segment and we expect market share gains to continue, driven by i) improving geographical presence for its NBFC/HFC businesses, ii) product expansion and increasing penetration in retail/SME (NBFC business), iii) affordable housing/construction finance (HFC business), iv) focus on banca tie-ups and protection (life insurance), v) strong brand positioning and vi) sustained outperformance in equity MF schemes.

AB Finance (ABFL): Fastest-growing multi-product NBFC with a pan-India presence slated to deliver healthy earnings with 2.1%/16% of RoA/RoE by FY20E. We value ABFL at 15x FY20E PE (implied PB of 2.3x FY20E), implying a value of ₹194bn.

AB Housing Finance (ABHFL): Rapidly gaining market share with rising penetration of affordable housing; poised to achieve PAT CAGR of 170% over FY18-20E. We value ABHFL at 2.0x FY20 BV, implying a value of ₹40bn.

Birla Sun Life Insurance (BSL): In FY18, it became the first non-banca player to report positive post-overruns NBV margins of 4.3%. Expected to touch 12% operating RoEV by FY20E. We value BSL at 2.0x FY20EV, implying a value of ₹107bn.

Birla Sun Life AMC (BSL AMC): Market leader in debt MFs (13.5% share) and 3rd largest in equity MFs, well-positioned to clock in a 22%/28% CAGR in overall MF AUM/PAT over FY18-20E. We value BSL AMC at 25x FY20E P/E, implying a value of ₹134bn.

Initiate coverage on ABCL with a BUY rating and SOTP-based TP of ₹170/share: We assign ₹89 per share for AB Finance, ₹31 per share for the 51% stake in the AMC business, ₹25 per share for the 51% stake in life insurance, ₹18 per share for AB Housing Finance and ₹7 per share for other businesses - Aditya Birla Health Insurance, PE Advisors and insurance brokers.

Key risks: Higher-than-expected credit costs, tightening liquidity, interest rate volatility, an increase in tax rate for the life insurance business and sustained weakness in the stock market adversely impacting MF inflows.

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3. FRESH PICK

Aditya Birla Capital - Key Financial Highlights

	FY16	FY17	FY18	FY19E	FY20E	CAGR/Change (FY16-18)	CAGR/Change (FY18-20)
Aditya Birla Finance							
Networth (₹ bn)	35	50	63	73	87	34%	17%
Loan book (₹ bn)	249	333	432	553	697	32%	27%
PAT (₹ bn)	4.1	5.9	7.7	10.3	13.1	37%	30%
Gross NPL (%)	0.7%	0.5%	1.0%	0.9%	0.9%	0.3%	-0.2%
Net NPL (%)	0.2%	0.2%	0.7%	0.6%	0.5%	04%	-0.1%
RoA (%)	1.8%	1.9%	1.9%	2.0%	2.1%	0.1%	0.12%
Leverage (x)	7.5	7.1	7.0	7.7	8.2		
RoE (%)	15%	14%	14%	15%	16%	-1.3%	2.7%
Aditya Birla AMC							
Networth (₹ bn)	8.3	9.9	12.2	15.1	18.8	21%	24%
AUM (₹ bn)	1,233	1,869	2,301	2,803	3,439	37%	22%
Equity as % of total AUM	27%	30%	37%	43%	46%	10.0%	9.3%
Cost to Income (%)	58%	66%	62%	61%	58%	4.1%	-4.1%
PAT (₹ bn)	2.1	2.2	3.3	4.1	5.4	25%	28%
RoE (%)	28.9%	24.3%	29.4%	30.1%	31.6%	0.6%	2.1%
Aditya Birla Life Insurance							
APE (₹ bn)	8	11	12	14	17	21%	17%
Mkt share - industry (%)	1.6%	1.7%	1.6%	1.7%	1.7%	0.0%	0.0%
Mkt share - pvt (%)	3.4%	3.5%	3.2%	3.2%	3.2%	-0.2%	0.0%
NBV (₹ bn)	-3.03	-0.54	0.52	0.99	1.42	NM	65%
NBAP Margins (%)		-5.5%	1.2%	7.8%	9.4%	1.2%	8.2%
Opex ratio (%)	21.9%	19.6%	18.4%	18.0%	17.8%	-3.5%	-0.6%
PAT (₹ bn)	1.4	1.2	1.7	1.8	2.0	9%	9%
EV (₹ bn)	33	38	43	48	54	14%	12%
Oper. RoEV (%)	0.5%	8.0%	10.7%	11.6%	12.3%	10.2%	1.6%
Aditya Birla Housing Finance							
Networth (₹ bn)	2	4	8	13	20	91%	64%
Loan book (₹ bn)	20	41	81	133	200	103%	57%
PAT (₹ bn)	-0.3	-0.2	0.2	0.8	1.7	NM	170%
Gross NPL (%)	0.2%	0.3%	0.5%	0.7%	0.8%	0.4%	0.3%
Net NPL (%)	0.0%	0.3%	0.4%	0.5%	0.6%	0.4%	0.1%
RoA (%)	-2.8%	-0.5%	0.4%	0.8%	1.0%	3.2%	0.64%
Leverage (x)	9.8	11.4	10.9	10.1	10.0		
RoE (%)	-24%	-5%	4%	8%	10%	NM	6.1%
Market share	0.1%	0.2%	0.3%	0.4%	0.6%	0.21%	0.28%

Source: Company data, JM Financial.

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4. DERIVATIVES DIARY

Topsy-Turvy May Series

The Nifty Index had a roller coaster journey in the month of May with the prices oscillating between the 10,400-10,900 levels. The Nifty index had a flat close over its previous month.

Low rollovers seen for Nifty in June series

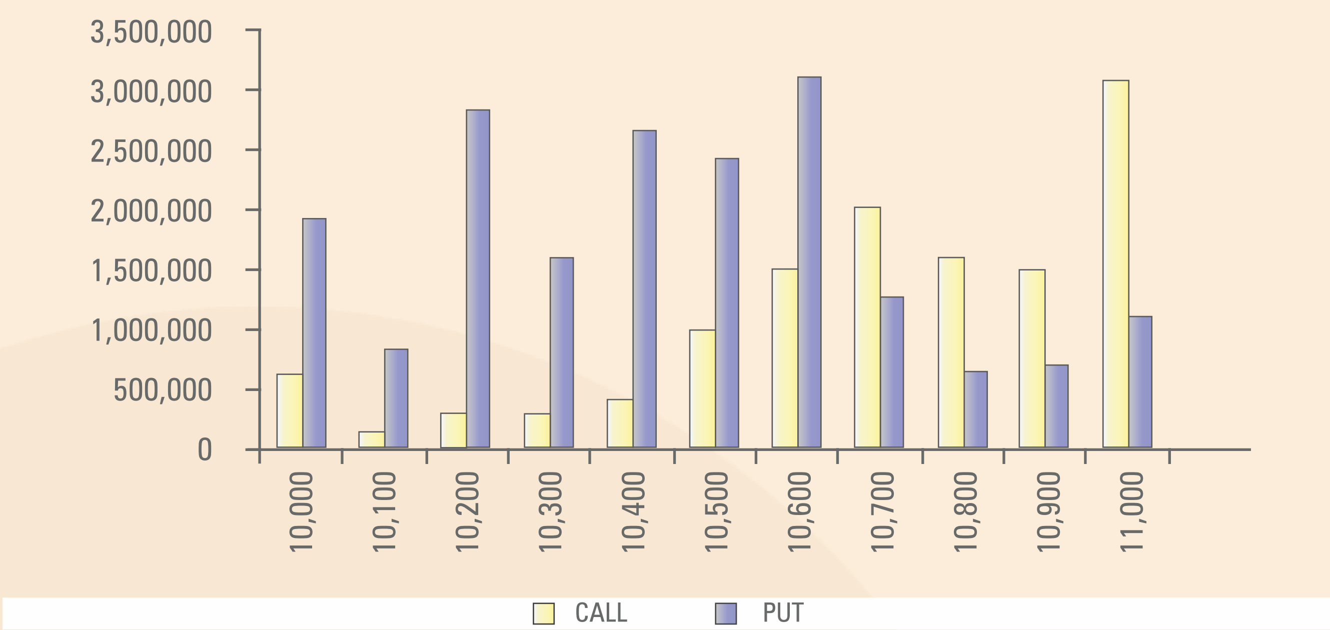
Rollovers for June series were seen at 62% in Nifty compared to its 3-month historical average readings which stand at 67%. Rollover cost for Nifty was noted at discount of 24 basis points on an OIPCR reading of 1.11 for the June series. INDIA VIX trades around 13.25.

FII open interest positioning at the start of June series has been almost even steven with long short ratio of 1:1 (almost 1 long to 1 short) slightly biased in favor of shorts in terms of open interest positioning. The FII presence of put longs is significant in options space. Client's data signals significant bets being placed in put shorts in the options segment.

Highest Open interest stood at 11,000 strikes in calls and 10,600 strikes in puts. 10,700 straddle pricing is around 280 points defining a price range of 10,420-10980.

Majority of sectors saw low rollovers compared to its historical 3 month averages. The highest sector wise rollover is evident in Engineer, Cement.

Nifty Total Open interest May series as on 31/05/2018



Source: Nseindia.com

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4. DERIVATIVES DIARY

Sector Rollover Statistics (In %)

Particulars	June	May	3mth Avg
Auto	81.21	85.10	86.17
Banking	84.43	88.98	86.22
Cement	89.60	88.19	87.52
FMCG	84.25	80.99	83.19
Oil & Gas	76.70	81.83	81.82
Metals	87.43	88.79	86.75
Textiles	87.19	89.55	89.10
IT	83.08	86.71	85.05
Telecom	86.43	88.99	88.76
Engineering	85.06	78.47	81.63
Pharma	88.09	91.84	90.31
Power	80.24	86.48	85.19
Finance	90.71	92.16	90.99
Infra	86.65	93.12	91.14
Media	79.40	92.30	89.41

Source: Nseindia.com

Conclusion

The price volatility seen in May have still not have dampened the trader sentiments going by the INDIA VIX reading which has steadied around 13 odd levels. Also the additional margin requirement which was due to be implemented in June has been postponed to July which will provide a temporary relief to the F&O community. However, low rollover numbers in the index at a discount signals low participation in the new series for the Index. 10,450-10,500 continues to be the trading base. 10,950/11,100 would be the resistance. Index is again expected to oscillate directionless between the 10,500-11,000 ranges. Only a break of this range would possibly be the trigger for the next directional move.

5. COMMODITY BUZZ

NAFTA Ambiguity...

Mexican Economy Minister Ildefonso Guajardo said President Donald Trump "shot himself in the foot" with the tariffs. Worries are mounting about the prospect of a trade war as the Trump administration also considers tariffs on U.S. auto imports -- which could hit top suppliers from Mexico, Canada, Japan and Germany -- and plans to levy duties on $50 billion in Chinese goods. The rising trade tensions come as Group of Seven finance ministers including U.S. Treasury Secretary Steven Mnuchin and central bank governors prepare to meet in the Canadian resort town of Whistler this week. Growing trade tensions have clouded a benign outlook for the global economy, which is on track to grow at its fastest pace since 2011 this year and next, according to the International Monetary Fund.
(Source: Bloomberg)

Crude has lost about 5% since last week when Saudi Arabia and Russia said they were considering supply boost to ease concerns over potential supply disruptions in Iran and Venezuela. Investors are now awaiting signs whether Saudi Arabia and Russia will reach a consensus with fellow producers to ease curbs when they meet in late June.

This has caused extreme volatility in energy markets and the commodities space. The currency markets are perturbed too. Hence a look at silver as a bull view is imperative.

Silver July 2018

Source: Ticker plant

Silver is trading in an upward sloping channel since February, 2018. At the current juncture, prices are hovering in a narrow range. However, silver is struggling to surpass immediate resistance at ₹40,300/kg as prices are holding above the crucial support level of ₹39,600/kg. If silver manages to surpass ₹40,300/kg, this may pave the path towards ₹41,200/kg in the near term.

On the contrary, if silver fails to surpass this resistance we may see prices will be trading in the same upward sloping channel.

We advise buying on closing basis above ₹40,300/kg with a target of ₹41,200/kg and ₹41,500/kg, while stop loss placed below ₹39,700/kg on the closing basis.

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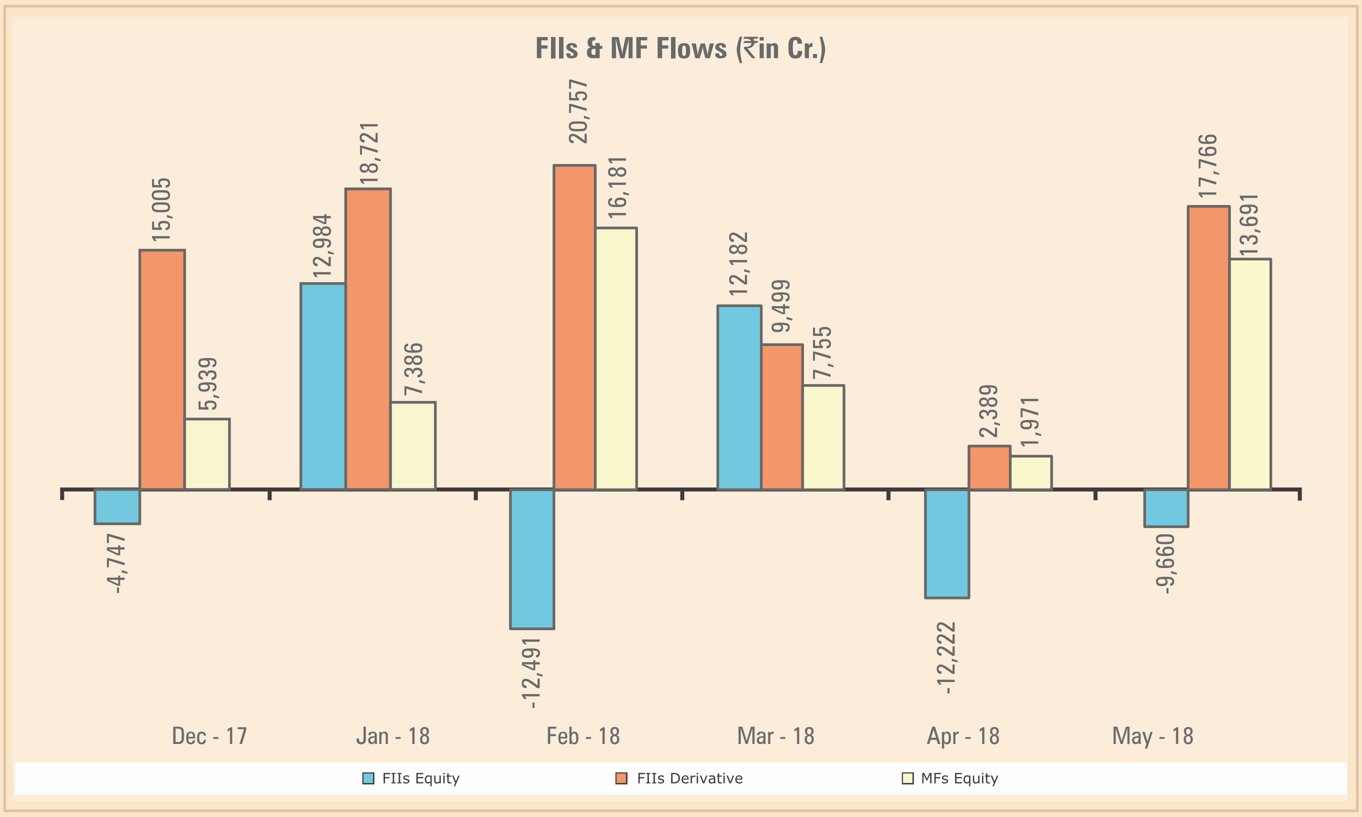
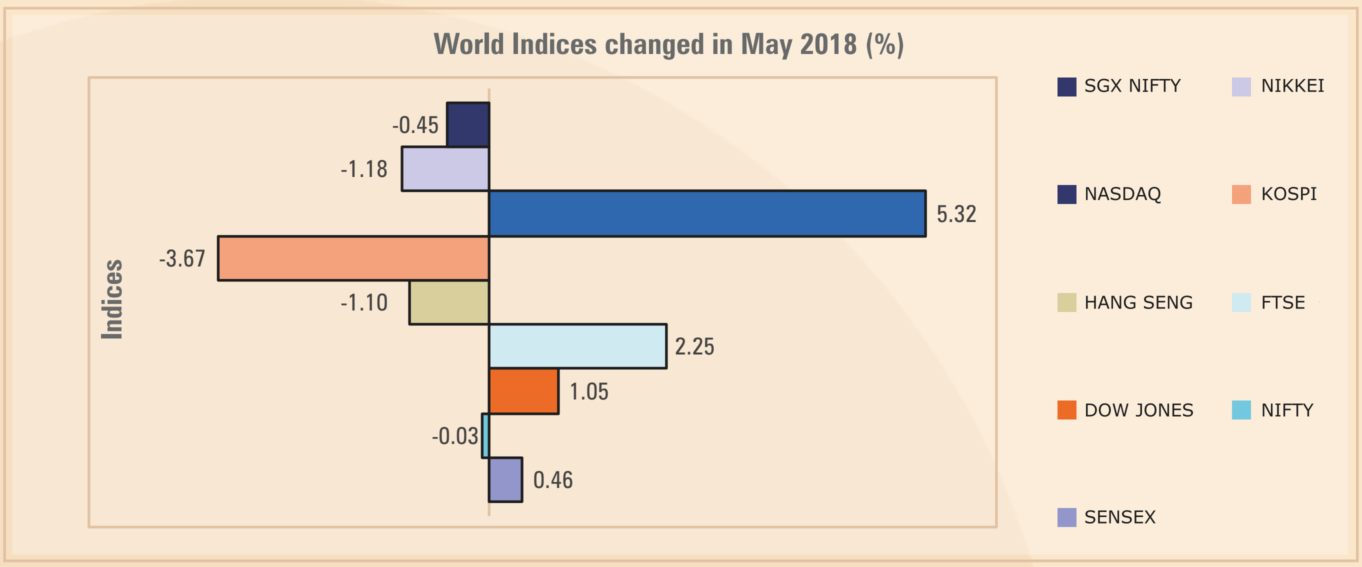
6. MARKET WATCH

FIIs & MFs Activity



Source: Bloomberg

World Indices



Source: Bloomberg

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6. MARKET WATCH

India Economic Calender: June - 2018

Date	Event	For the Period	Survey	Actual	Prior
01-Jun-2018	Nikkei India PMI Mfg	May	--	51.2	51.6
05-Jun-2018	Nikkei India PMI Services	May	--	--	51.4
05-Jun-2018	Nikkei India PMI Composite	May	--	--	51.9
05-Jun-2018	BoP Current Account Balance	1Q	-$12.50b	--	-$13.50b
06-Jun-2018	RBI Repurchase Rate	6-Jun	6.00%	--	6.00%
06-Jun-2018	RBI Reverse Repo Rate	6-Jun	5.75%	--	5.75%
06-Jun-2018	RBI Cash Reserve Ratio	6-Jun	4.00%	--	4.00%
12-Jun-2018	Manpower Survey	3Q	--	--	16%
12-Jun-2018	CPI YoY	May	--	--	4.58%
12-Jun-2018	Industrial Production YoY	Apr	--	--	4.40%
14-Jun-2018	Wholesale Prices YoY	May	--	--	3.18%
15-Jun-2018	Trade Balance	May	--	--	-$13716.8m
15-Jun-2018	Exports YoY	May	--	--	5.20%
15-Jun-2018	Imports YoY	May	--	--	4.60%
25-Jun-2018	Eight Infrastructure Industries	May	--	--	4.70%
27-Jun-2018	Bloomberg June India Economic Survey				
29-Jun-2018	Fiscal Deficit ₹ Crore	May	--	--	151967

Source: Bloomberg

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6. MARKET WATCH

U.S. Economic Calender: June - 2018

Date	Event	For the Period	Survey	Actual	Prior
01-Jun-2018	Change in Nonfarm Payrolls	May	190k	--	164k
01-Jun-2018	Unemployment Rate	May	3.90%	--	3.90%
01-Jun-2018	Markit U.S. Manufacturing PMI	May F	56.6	--	56.6
01-Jun-2018	ISM Manufacturing	May	58.2	--	57.3
04-Jun-2018	Factory Orders	Apr	-0.50%	--	1.60%
04-Jun-2018	Durable Goods Orders	Apr F	--	--	-1.70%
05-Jun-2018	Markit U.S. Services PMI	May F	--	--	55.7
05-Jun-2018	Markit U.S. Composite PMI	May F	--	--	55.7
05-Jun-2018	ISM Non-Manf. Composite	May	58	--	56.8
07-Jun-2018	Initial Jobless Claims	2-Jun	--	--	221k
12-Jun-2018	CPI MoM	May	--	--	0.20%
12-Jun-2018	CPI YoY	May	--	--	2.50%
13-Jun-2018	FOMC Rate Decision (Upper Bound)	13-Jun	2.00%	--	1.75%
13-Jun-2018	FOMC Rate Decision (Lower Bound)	13-Jun	1.75%	--	1.50%
14-Jun-2018	Import Price Index YoY	May	--	--	3.30%
14-Jun-2018	Initial Jobless Claims	9-Jun	--	--	--
15-Jun-2018	Industrial Production MoM	May	--	--	0.70%
20-Jun-2018	Current Account Balance	1Q	--	--	-$128.2b
20-Jun-2018	Existing Home Sales	May	--	--	5.46m
21-Jun-2018	Initial Jobless Claims	16-Jun	--	--	--
22-Jun-2018	Markit U.S. Manufacturing PMI	Jun P	--	--	--
27-Jun-2018	Pending Home Sales MoM	May	--	--	-1.30%
27-Jun-2018	Pending Home Sales NSA YoY	May	--	--	0.40%
28-Jun-2018	GDP Annualized QoQ	1Q T	--	--	2.20%
28-Jun-2018	Initial Jobless Claims	23-Jun	--	--	--

Source: Bloomberg

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APPENDIX I

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Definition of ratings

Rating	Meaning
Buy	Total expected returns of more than 15%. Total expected return includes dividend yields.
Hold	Price expected to move in the range of 10% downside to 15% upside from the current market price.
Sell	Price expected to move downwards by more than 10%

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APPENDIX I

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Rating	Meaning
Buy	Total expected returns of more than 15%. Total expected return includes dividend yields.
Hold	Price expected to move in the range of 10% downside to 15% upside from the current market price.
Sell	Price expected to move downwards by more than 10%

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• Stock Lending & Borrowing Scheme • Systematic Investment Plans in Stocks, Mutual Funds and Exchange Traded Funds • Commodity Broking
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2017, 2015, 2014, 2013

Amongst the Top Performers in the Primary Market Segment (Equity – IPO/FPO Bids - Members) by BSE
2017, 2016, 2015, 2013, 2011

Amongst the Top National Distributors in Mutual Fund Segment by BSE
2017, 2014, 2011

Market Achievers Awards in the Highest IPO Bidding - Non Institutional Category by NSE
2017

Best Company to Work for in the Investments Industry by Great Place To Work® Institute
2017, 2016, 2015, 2012

Ranked No. 2* Best Private Banks - India in Asiamoney Private Banking Poll
2016

Amongst the Top Performers in Sovereign Gold Bonds by BSE
2016

Best Performing National Financial Advisor (Institutional) by UTI & CNBC
2016, 2015, 2014, 2012

Amongst the Top Performers in Cash Market by NSE
2016

Ranked Amongst the Top 100 India's Best Companies to Work for by Great Place to Work® Institute
2015, 2014, 2013, 2012

Amongst the Top Performers in Debt ETFS by NSE
2015

Highest Broker Grading of BQ1 For Quality of Services and Operations by CRISIL
2012, 2011

Fastest Growing Equity Broking House (large Firms) by BSE and DUN & BRADSTREET
2010

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