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ONE-FOURTH FISCAL

2017-18 • Volume 3

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FOREWORD

In the last few months, the Indian stock markets have been holding strong on a path of determined growth. Both the Nifty and Sensex have surged to their record highs in the past months. India emerged as one of the most lucrative markets to invest in, despite bumps such as the stress in the banking sector and a choppy GDP growth. For investors, last year's positivity flowed through into this year with reforms taking effect and the inflation being under control.

The last quarter marked the 70th anniversary of Indian independence. The whole world has been drawing some interesting parallels with India right now and China at the turn of the millennium saying that this may be an advantageous time for investors to join the Indian market. A lot of it has to do with the government policies.

Our quarterly report, One-Fourth Fiscal, continues to capture the sentiments of the stock markets in the context of the country's changing macro-economic landscape and sectorial performance. In addition to it, One-Fourth Fiscal also covers two major game-changers for the current quarter: The state of Indian banking sector and buybacks. The report provides a special coverage on cryptocurrency and muhurat trading.

One-Fourth Fiscal also takes you through the extraordinary and remarkable journey of ace stock market investor, Dr. Vijay Kedia.

India's stocks and currency have outperformed most large economies in the past six months as renewed confidence in the country's relative economic and political stability have made it an emerging market-haven in uncertain times. The faith showed by investors in the Indian economy has been due to its strong fundamentals and future growth prospects. Investment activity is supposed to pick up as the NPA issue is gradually resolved and earnings may grow to support the market performance.

As we move towards the 2nd half of FY 2017-18, it would be interesting to observe the market sentiment. The market events are essential in correlating the impact of global and domestic events on stock performance. One-Fourth Fiscal continues to accurately capture the market trends and actions in-depth. It strives to get the facts right, letting the data speak for itself and focusing on specifics that will help you sort through the clutter in the market.

Happy reading!

Mr. Kamlesh Rao
Managing Director and CEO
Kotak Securities

EXECUTIVE SUMMARY

Stock markets scaled fresh highs in the last quarter riding on corporate earnings and positive global cues. The market rally came after a string of solid domestic quarterly results and renewed optimism about the US economy, while escalating geopolitical tensions and the GST implementation kept the market correcting itself repeatedly. However, the market performance is also dependent on various macro-economic scenarios which may include international events, panning of monsoon, commodity prices, domestic reforms and consumption factor. Hence, investors must look at market opportunities with a holistic view on the past and upcoming domestic and international events. In an effort to bring key insights of the market to the investors, Kotak Securities is publishing the third edition of the report One-Fourth Fiscal with the help of professional services firm Ernst & Young LLP (EY).

The positive indicators of economic growth in India are reflected in the notably upbeat market sentiment. This growth can be contributed to the well-crafted monetary policy of RBI, various Government reforms and improvements in transparency and ease of doing business. The recent implementation of GST brings the added benefit of reducing leakage in tax collections. As the future of Indian Economy looks positive, the accumulation of bad debt in the banking sector may act as a barrier to growth. Indian equity market has shown a notable uptrend in FY18, led by high returns in the realty sector and financial services sector. Buying in metal, FMCG and auto stocks is a sign of improvement in demand added impetus to the market.

The banking sector in India has been impacted by the worsened asset quality due to high NPAs. In Q1 FY18, NPAs of major banks increased by a sharp 34.2% on a Y-o-Y basis. Also, the NPA ratio increased to 10.21% in June 2017 from 8.42% in June 2016, which is the highest in the last six quarters. To tackle this issue, the RBI imposed Prompt Corrective Action (PCA) on 6 public sector banks, which restricts these banks on dividend distribution, remittance of profits and branch expansion, capital expansion and other management actions. Also, the government is working on the agenda for consolidation of PSBs, in a bid to reduce the number of state-owned lenders. The major focus being the creation of fewer and larger banks. Five associates became part of the largest Indian PSB on April 1, 2017 as a part of the last consolidation drive. With the regulators springing into action to improve the state of Indian banking industry, the sector seems all poised for sustained growth.

Buybacks have acted as a game-changer in the global and Indian stock market for many companies. Between April 2016 and July 2017, 69 companies have proposed or undertaken buybacks worth INR 58,592 crore, the majority of which have been tender offers. Such buybacks are an important signalling mechanism on the future prospect of the company. This report provides investors with the insights on how to evaluate the benefits and risks of a proposed buyback.

One-Fourth Fiscal also analyses the implications of the latest buzz: Cryptocurrencies. Bitcoin and Ethereum have become a global craze, with their valuations and market capitalization shooting through the roof. Cryptocurrencies like Bitcoin are extremely volatile in nature, with price swings of more than 5% in a day as a common phenomenon. A number of trading platforms for Bitcoins have sprung up globally, with the trend catching up in India as well. Recently in an official statement, the RBI has warned users, holders and traders of Bitcoin or any other virtual currency, "about the potential financial, legal, and security risks arising from their use". There is a still a lack of consensus on the regulatory and legal framework to govern or regulate the use of Bitcoin in India. It has raised concerns regarding the validity and authenticity of the Bitcoin holdings of investors.

As Diwali nears, the auspicious Muhurat trading is considered by many investors to bring prosperity and higher returns. For the business community, the new 'Vikram Samvat' will begin with Diwali when old account books or ledgers will be closed and new ones will be opened. In the coming months, Indian markets are expected to continue their upward trend given the strong fundamentals for long-term economic growth and it would be interesting to observe the investor sentiments in the last quarter of FY 2017-18. Although the India story looks good, investors must be cautious about global events and must implement a long-term approach while strategizing their portfolio.

STATE OF THE ECONOMY

India has emerged as the fastest growing economy in the world in 2016-17, with the Government of India predicting GDP growth of 7.1% for the full fiscal year. This view has been corroborated by the IMF's World Economic Outlook Update, which further estimates that growth will accelerate to 7.7% for 2017-18. Unemployment is down to 4.8% from 9.5% in 2016, and Nielsen's Consumer Confidence Index places India at the top of the global rankings for 2017. All these positive indicators are reflected in the notably upbeat market sentiment, with the NIFTY closing above 10,000 points for the first time in July.

Key enabling factors contributing to India's economic growth:

1. RBI's accommodative yet well-crafted monetary policy has given Indian businesses access to affordable credit while keeping inflation at bay.

2. Supportive government policy reforms like Make in India have given a boost to the local economy.

3. Improvements in transparency and ease of doing business through initiatives like Digital India, de-monetization, and the recent implementation of GST have encouraged greater foreign investment.

4. De-monetization and the introduction of GST bring the added benefit of reducing leakage in tax collections. This should ultimately translate into greater government investment, providing a double-whammy for economic growth.

All these factors paint a fairly rosy picture for the future of the Indian economy. A key sticking point that could play spoil sport to India's growth story is the accumulation of bad debt in the banking sector. Until India's Financial Services Sector is able to clean up its balance sheet, lending activity may remain muted in spite of the Reserve Bank of India's (RBI's) accommodative monetary policy. However, markets may continue their upward trend in the coming quarters, given the strong fundamentals for long-term economic growth.

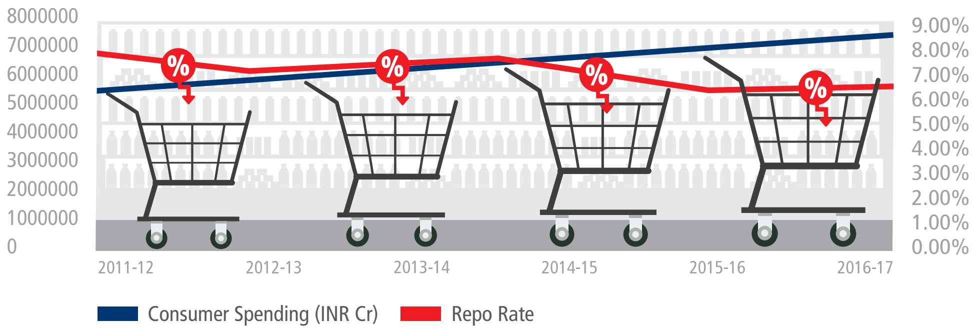
Easier access to capital

The RBI has been following an aggressive expansionary monetary policy since early 2014 - they reduced the benchmark repo rate by 175 basis points from 8% to 6.25% between Jan'14 and June'17. The RBI appears to have proceeded with prudence, and followed a well thought-out strategy to keep inflation at bay. June 2017 retail inflation was reported at a record low of 1.54%. The RBI's approach of carefully reducing rates has also given India's small businesses and start-ups greater access to capital. In conjunction with supportive government initiatives, this has allowed them to build and grow their businesses and contribute to better, more meaningful economic growth.

Retail inflation is at an all-time low of 1.54%, supporting greater real economic growth.

Consumer spending is an important indicator of economic growth - RBI's expansionary monetary policy is supporting a steady increase in consumer spending.

Interest rates vs. consumer spending in India



Source: 1) Ministry of Statistics and Program Implementation; 2) Reserve Bank of India

India's consumer spending is expected to triple by 2025, and surpass that of the US by 2040, making India the second largest economy in the world.

Strong economic fundamentals has motivated robust equity market growth, with NIFTY growing 56% since 2014. Future growth is contingent on successful implementation of key initiatives like GST.

The above chart shows the growth in consumer spending along with the prevailing repo rate over the last 5 years. The trend indicates that consumer spending has steadily increased as the RBI embarked on its expansionary monetary policy. While per capita spending is still considerably lower compared to developed economies, this gap is also closing at a rapid rate. This economic success has been rewarded by investors contributing to the strong equity market performance. While fundamentals point to further market appreciation, this is contingent on India continuing on the right path of monetary and fiscal responsibility and successful adoption of key initiatives like GST for businesses.

GST feedback – Shift from unorganized to organized

Our previous issue talked about how the GST is expected to simplify the tax system, thereby reducing regulatory and compliance costs in the long run. GST is expected to play an important role in formalizing the highly unorganized and fragmented sectors of India's economy like textile, cement and steel that operate largely on cash basis with very few manufacturers meeting regulatory and tax compliance requirements. The long-run impact of GST is expected to be positive, with a larger portion of the unorganized sector being incentivized to become tax compliant and facilitate increase in overall tax revenues. However, some teething issues are to be expected across the board:

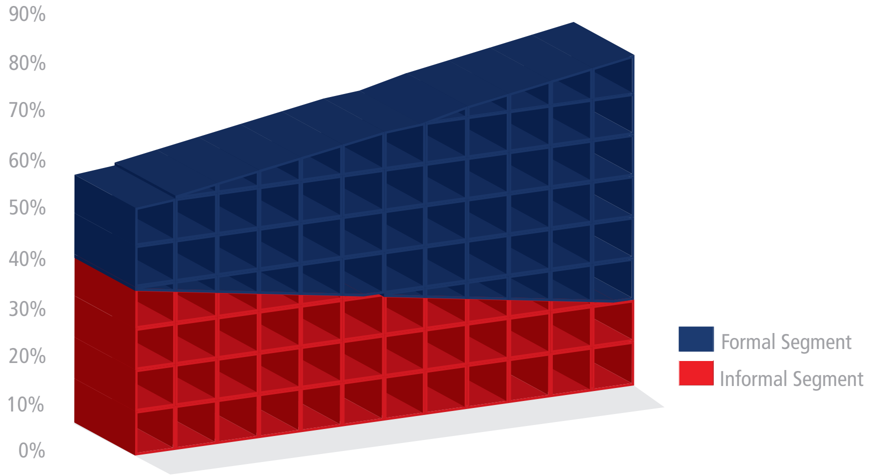
Barriers to GST compliance

1. GST is a highly technology driven taxation system - companies have invested large amounts to become compliant. This is a particular barrier to the unorganized sector.

2. Lack of clarity on regulations which has created uncertainty in the market and hindered economic growth in the short term - GDP growth declined to 5.7% in Q1 FY18 from 7% in the previous quarter, though part of this decline can be attributed to de-monetization.

As mentioned, the lack of technological readiness is a key constraint to businesses in the informal sector achieving GST compliance. Larger companies in the organized sector have a strong incentive to partner with GST compliant suppliers so that they can claim their input tax credit. The only other alternative for them is to pay GST on their supplier's behalf via the Reverse Charge Mechanism, which is an additional compliance burden that businesses in the organized segment may not be willing to take on. As a result, GST compliant companies in the organized sector may steal market share from the unorganized sector, particularly in the traditionally unorganized industries like batteries, tile making etc.

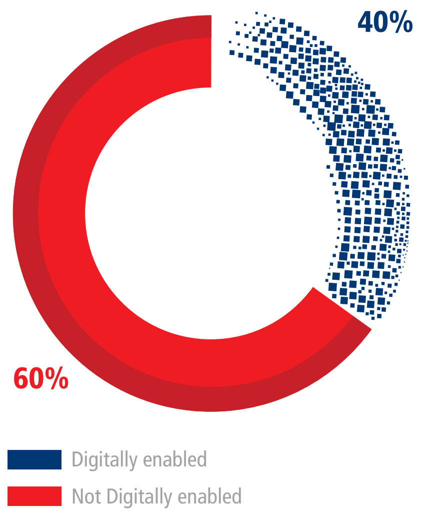
% Market share of formal vs. informal segment of tile industry



GST competitive bushesses in organized sector are taking market share from the unorganized sector

Source: The flip side of GST: its impact on the informal economy www.livemint.com

% of digitally enabled business in informal sector



60% of businesses have yet to adopt digitally enabled business models

Source: Confederation of All India Traders

Without outside financial support in becoming GST compliant, the informal segment runs the risk of losing competitiveness to larger companies

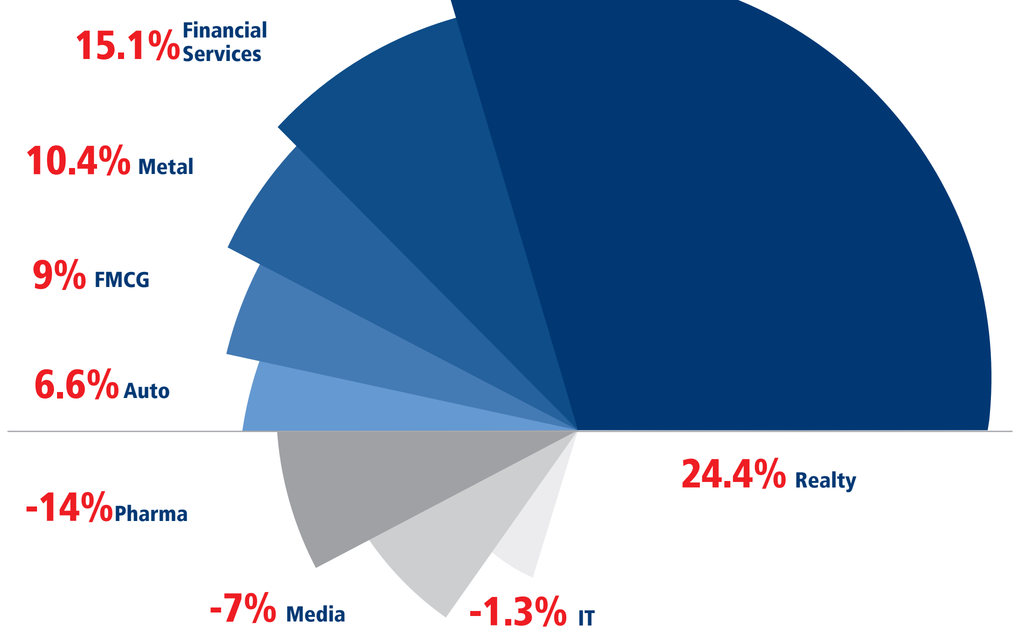
While it remains to be seen how the unorganized segment copes, it seems apparent that these smaller players will need help from the government in order to be competitive during this initial teething period. Otherwise, the organized segment of the economy that the government is trying to bring under the tax net through GST may very well cease to exist.

MARKETS - SECTORIAL RESULTS AND FUTURE OUTLOOK

A marked upsurge has been observed in the performance of the Indian equity market in FY18, with the NIFTY surpassing 10,000 points for the first time in July. The charge has been led by the realty sector, which has benefited from the recent implementation of GST through a significant reduction in their input costs. The financial services sector follows closely behind, with private banks reporting healthy first-quarter results. Performance of some key sectors are assessed in detail below.

Realty, financial services and metals have provided more than 10% returns in the first four months of this financial year.

NIFTY sector indices return % FY18 (till Aug, 2017)



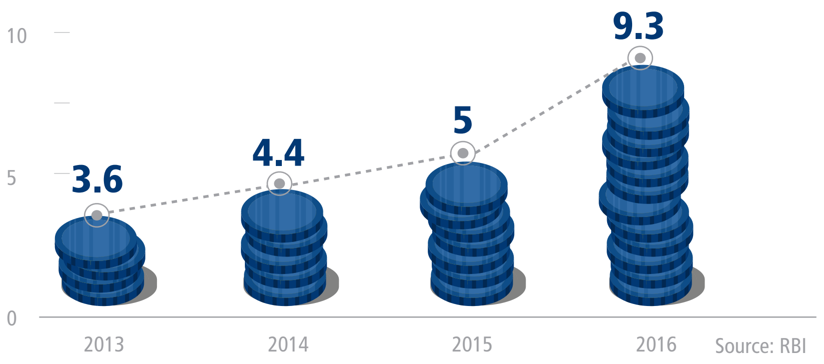
Financial services

The Indian government's privatisation program, which includes the sale of stakes in the insurance industry has fuelled growth in equities. This has contributed to the 15.1% growth in the NIFTY Financial Services Index during FY18 (till August'17). However, the sector continues to be burdened by high NPL ratios, particularly among Public Sector Banks (PSBs) which account for 80% of gross bank credit extended by banks.

Furthermore, the re-classification of stressed assets as NPLs may further squeeze lending.

While the Indian government is making efforts to improve asset quality in PSBs through various recapitalization and insolvency measures, these may not have a significant impact due to lack of enforcement capacity and a slow judicial process. Recent efforts toward consolidation of PSBs will take time to take effect.

Rise in gross NPL ratios of PSBs



Source: RBI

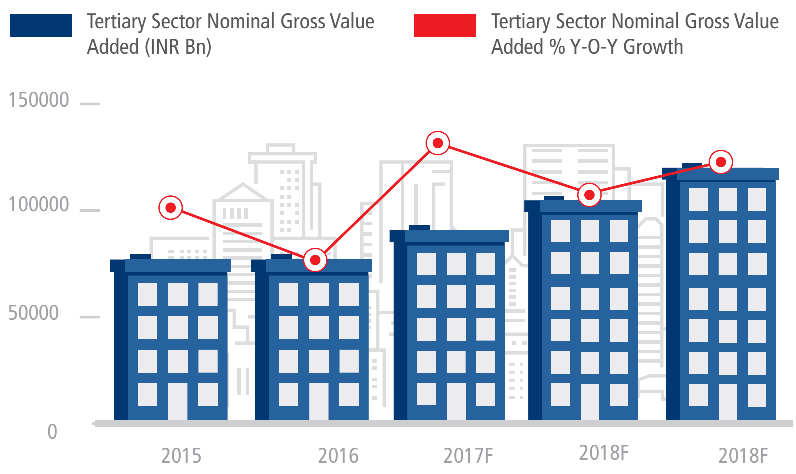
High NPLs continue to squeeze lending and restrict long-term growth potential of Financial Services sector.

Real estate

India's real estate sector has traditionally been dominated by cash-based transactions. Therefore the de-monetization in Q3'FY16 hit the sector hard, staving off liquidity and slowing demand. However, policy initiatives like RERA have provided comfort to the investors and GST implementation has reduced the cost of raw material for the industry. The Digital India movement has created an influx of new IT companies, increasing demand for office space in prime areas across Hyderabad, Bengaluru and Mumbai. Also implementation of GST is supporting consolidation of the industrial real estate segment and increasing demand for warehouse space. The long-term outlook, particularly for commercial real estate, remains positive.

An influx in Office and Warehouse demand has driven growth in the Real Estate sector, with the NIFTY Real Estate Sector Index returning 27.4% FY18 till Aug'17

Services growth supporting office demand



Source: Central Statistics Organization, BMI

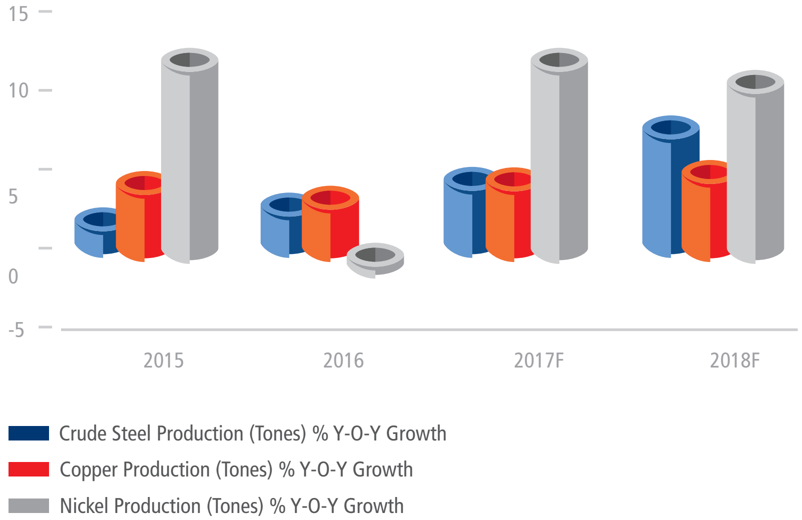
Metals

The metals industry is expected to reap considerable benefits from the implementation of GST through a reduction in input costs and simplification of tax structure. All ores and concentrates have been placed in a lower tax bracket. Electricity, which constitutes 30-35% of the cost of producing metals, is also expected to be considerably cheaper with coal being placed in a lower tax bracket as well. This particularly benefits India's sizeable steel Industry.

Key inputs in steel production	Pre-GST Rate	GST Rate
Iron ore	11-12%	5%
Electricity/power (coal)	12%	5%

GST has supported a reduction in input costs, giving a sizeable boost to the Metals sector with the NIFTY Metals Sector Index returning nearly 10.4% FY'18 (till Aug'17)

GST to buoy metals production via lower input costs



Source: USGS, Bloomberg, BMI

Information Technology

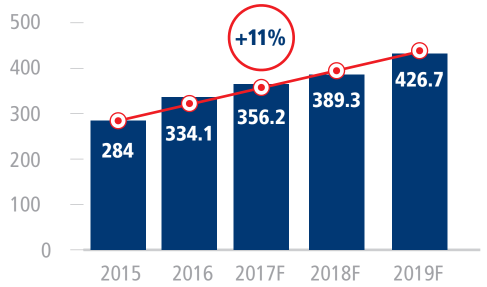
The Indian IT sector is an INR 2 Trillion industry, with projected growth of 6.7% in FY17-18. This growth is supported by several favourable underlying trends:

1. Increasing adoption of basic cloud computing solutions by India's SME sector. The Financial Services sector will continue to be lucrative for vendors of more complex software solutions. Total Software sales are expected to grow at CAGR 11%

India emerges as 4th largest base for start-ups

2. Vibrant environment for IT start-ups with Indian companies introducing unique solutions in the areas of Internet of Things, augmented reality, smart hardware and business intelligence

Software sales (INR bn)

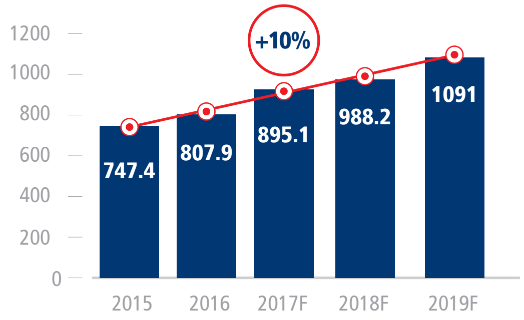


Source: BMI

3. The IT Services segment remains a key source of enterprise spending, with India's BPO industry growing at a rate of 40% per annum. The overall services segment is growing at CAGR 10%

Increasing adoption of cloud computing solutions by SME and continued strong growth in IT services are enabling factors for IT sector growth

Services sales (INR bn)



FMCG

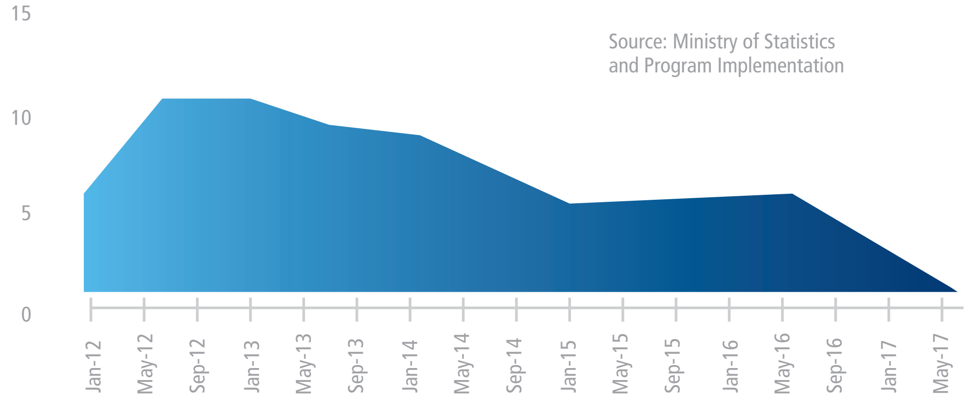
The NIFTY FMCG returns for FY'18 (till Aug'17) are up by 9%. NIFTY FMCG index rose to ~28,000 in July'17 from 23,600 in Apr'17 and again showed a downtrend post GST implementation, closing at 25,761 in August'17.

Long-term outlook for this sector however remains positive as real private consumption is expected to grow 6.5% in 2017 and 6% in 2018, which is a strong showing in the context of India's global peers and the size of its consumer market.

A key driver behind this strong growth in consumer spending is the significant decline in India's headline inflation, which has eased from an all-time high of 11.16% in November 2013 to 3% in April 2017.

Decline in headline inflation-%
Y-O-Y Change in CPI

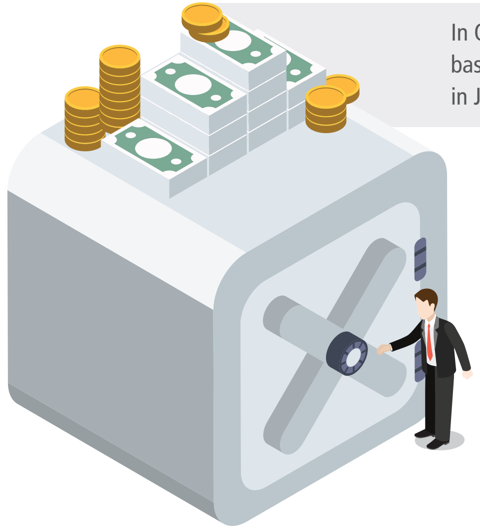
Declining inflation has triggered boost in spending, which is expected to contribute to positive growth in FMCG Sector



Source: Ministry of Statistics and Program Implementation

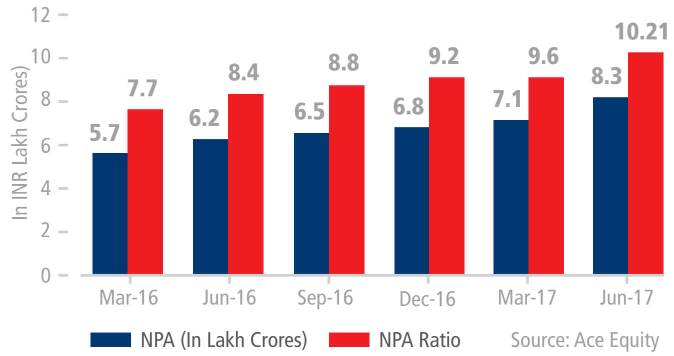
STATE OF INDIAN BANKING SECTOR

The banking sector in India is reasonably well-regulated and capitalized. Also, the economic and financial conditions in India seem considerably better than those in the other countries in the world. However, NPAs damage the health of banking systems. The worsened asset quality due to high NPAs negatively impacts the profitability of the banks and reduces their lending capability significantly. And in India, growing NPAs is currently the biggest hindrance that has damaged effective operations of Indian lenders.



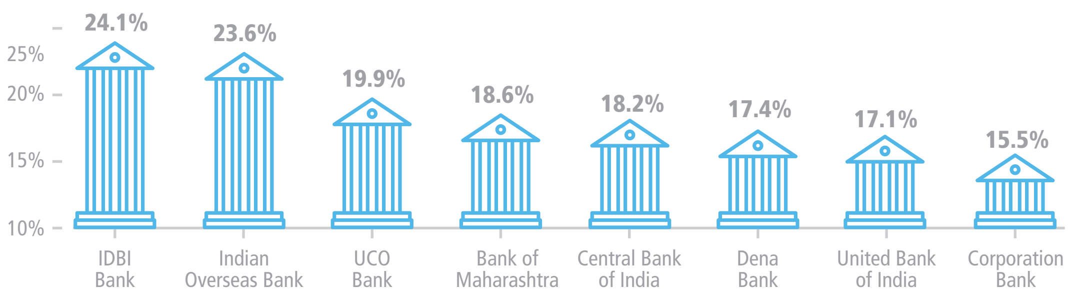
In Q1 FY18, NPAs of major banks increased by a sharp 34.2% on a Y-o-Y basis. Also, the NPA ratio increased to 10.21% in June 2017 from 8.42% in June 2016, which is the highest in the last six quarters.

Struggle of Indian banks with NPAs



Source: Ace Equity

Top 8 Banks basis NPA Ratio (as on Jun '17)



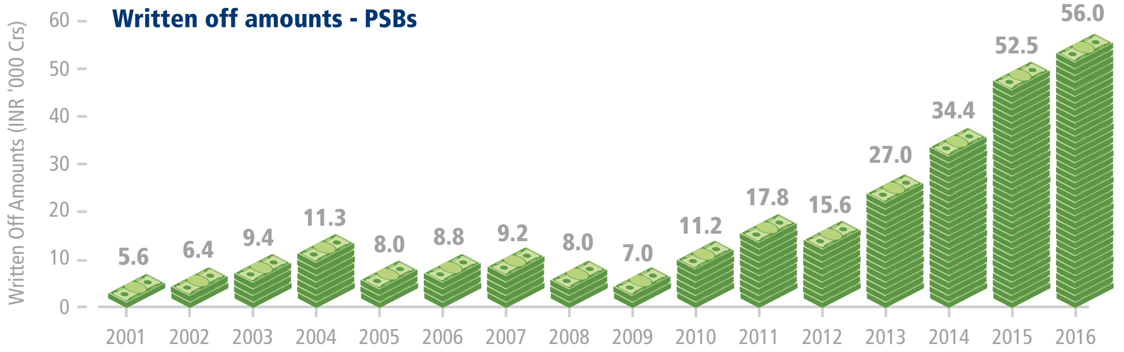
In terms of NPAs, PSBs have seen significant increase in their NPAs in the past few years. To give a context, only six state-owned banks had more than 3% gross NPA in March 2012. (Three other associates of the largest PSB lender having more than 3% gross NPAs got merged with their parent). However, as of Jun 2017, 8 banks had crossed the NPA ratio of 15% and all of them were PSBs.

Private banks seem to have a better asset quality than PSBs. NPAs in private sector banks have been less volatile and some of the banks have even been able to improve their asset quality in the last few years.

However, all those expecting that the worst is behind the Indian banking industry are expected to be a disappointed lot. The performance of banks with respect to NPAs has not been too positive of late. While it was largely expected that the NPA ratios would have settled by March 2017 as there were indications of stabilization relative to December 2017, it is evident from the data of Q1- FY 18 that the NPAs have deteriorated further for the system as a whole.

Even the written-off amounts have grown substantially in the last few years, more so amongst the PSBs. The table below gives an overview about the alarming increase in write-offs amongst PSBs in the last few years.

Written off amounts - PSBs



Prompt Corrective Action (PCA)

RBI, under its supervisory framework, uses various tools to maintain sound financial health of banks and PCA framework is one of such supervisory tools.

Some salient features of PCA are as follows:

- Capital, asset quality and the profitability continue to be the key areas for monitoring in the revised framework.
- The PCA framework does not preclude the Reserve Bank of India from taking any other action as it deems fit in addition to the corrective actions prescribed in the framework.
- Breach of 'Risk Threshold 3' of CET1 by a bank could identify the bank as a likely candidate for resolution through tools like amalgamation, reconstruction, winding up, etc.

As on Jul '17, PCA had been imposed on 6 banks. Under PCA, the mandatory actions of the RBI are as follows:

- Restriction on dividend distribution, remittance of profits and branch expansion
- Promoters / Owners to bring in capital
- Higher provisions as part of coverage regime
- Restriction on Management compensation/ Directors' Fees etc.

Further some of the discretionary actions that can be taken by RBI are as follows:

- Undertake Business Process Reengineering (BPR) in any bank.
- RBI can remove any managerial person from any bank as per Sec 36AA of the BR Act 1949 and supersede Bank Board as per Sec 36ACA of the BR Act.
- Restriction on/reduction in credit expansion to borrowers under certain rating grades, sale of assets, costly deposits, staff expansion and capital expenditure.
- Time bound plan and commitment for reduction of stock of NPAs and containing generation of fresh NPAs etc.

Consolidation of banks

9 of the 21 PSBs reported losses during 2016-17 while 13 of the PSBs had reported losses during FY 16. In a bid to reduce the number of state-owned lenders, most of them suffering from high losses and poor asset quality, the government is working on the agenda for consolidation of PSBs. The major focus of the government is to create a few banks, approximately the size of India's largest PSB, as well as reduce the number of PSBs.
Five associate became part of the largest Indian PSB on April 1, 2017 as a part of the last consolidation drive.

The key reasons for these mergers are considered to be multifold, spread across revenue enhancement, improvement in efficiency, diversification of customers and assets, to gain international recognition and achieve economies of scale. However, mergers could also lead to job cuts, branch closures, and, in some cases, a lowering of the quality and quantity of services. It is yet to be seen whether the consolidation on such a large scale would impact the Indian economy in a positive or a negative way, which only time will tell.

The banking sector in India has now started laying greater emphasis on providing improved services to the clients and upgrading their technology infrastructure, in order to enhance the customer's overall experience as well as give banks a competitive edge. Government of India (GoI) and RBI have undertaken several measures to strengthen the Indian banking sector including amendment of Section 35A of the Banking Regulation Act to allow the RBI to direct banks for the recovery of non-performing assets (NPAs).

With the RBI springing into action early by identifying banks for PCA, accounts for insolvency proceedings and consolidation of banks into larger and more competitive entities, India's banking sector seems all poised for sustained growth. This is expected to keep the market sentiments positive and ensure faith in the Indian banking sector among the investors.

BUYBACKS: HOW COMPANIES MAKE IT WORK

A share buyback is an action whereby the company repurchases its own publicly issued shares from existing investors. This can be done in two ways:

1. The company can make a tender offer to the shareholders, usually offering a premium to the prevailing market price as incentive for selling their shares.
2. The company can repurchase its shares on the open market winding up, etc.

Buybacks are generally considered as a way of returning excess cash to the shareholders, similar to paying dividends. While buybacks are a relatively new phenomenon in India, they are fast gaining prominence in Indian equity markets making it important for investors to understand their implications.

Between April 2016 and July 2017, 69 companies have proposed or undertaken buybacks worth INR 58,592 crore, majority of which have been tender offers. This surge in buybacks may be attributed to changes in Indian tax norms implemented in the 2016 Union Budget, making it more tax efficient for companies to re-pay their investors via buybacks than dividends.

Buybacks are also an important signalling mechanism to the market - after all, what does the returning of excess capital indicate about the future prospects of the company? This is an important consideration investors should keep in mind when evaluating a proposed buyback.

The following box highlights scenarios in which buybacks may generate positive shareholder value and scenarios in which they may deplete shareholder value.

Cases when buybacks generate
Positive value

Management believes the company is undervalued
This could be because management has inside information that the market has not priced in. In this case, the buyback is indicative of management's confidence in the company's long term potential, particularly if they are also buying shares for themselves.

Shedding Excess Capital
A Company may have experienced a year of abnormal profits. A share repurchase is a tax-efficient way of making one time returns of excess cash to shareholders without setting a precedent for higher dividends in future years.

Market Timing
A company can maximize return to shareholders by timing buybacks during market down cycles when stocks are relatively under-priced.

Cases when buybacks
Destroy value

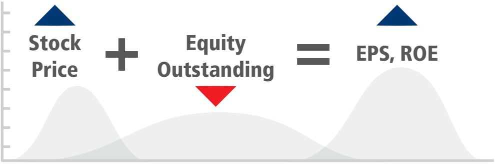
Management attempt to boost performance metric
A share buyback reduces value of total equity outstanding, raising certain metrics like EPS and ROE regardless of any improvement in operating performance. Management may issue a buyback solely to boost such metrics, particularly if they are tied to compensation.

Premium is too high
Management may set the premium higher than the perceived intrinsic value of the company to make the buyback more lucrative to investors. This only serves to erode value, particularly if shareholders equity is used to finance the buyback.

Lack of Investment Opportunities
A buyback could signal to the market that management is unable to identify new investment opportunities for the company, indicating a decline in future growth.

Market impact of buybacks

Positive signal
Improvement in shareholder value reflected in EPS and ROE



Negative signal
Eroding of shareholder value not accurately reflected in EPS and ROE

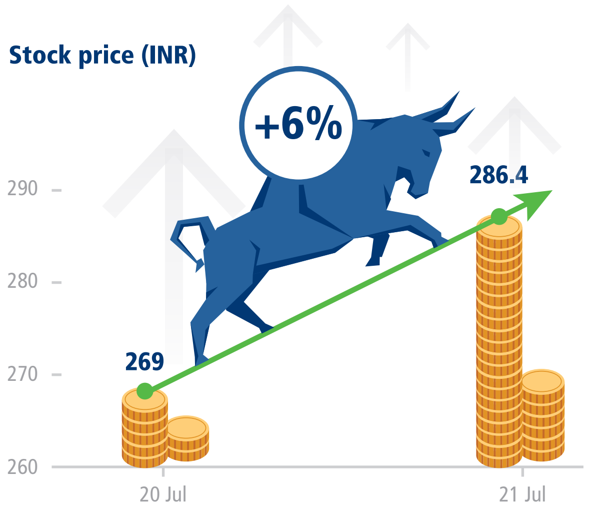
An illustration of market forces at play

Scenario A

Buyback supported by legitimate decline in investment opportunities

Earlier this year, a leading global IT Services provider announced a buyback worth INR11,000 crore. The reason for this, as outlined by management, was a decline in spending by healthcare clients in the US due to regulatory uncertainty over attempts by President Trump to repeal certain provisions of the 2010 Affordable Care Act.

The company's stock price shot up immediately following the announcement. This is an example of a company shedding excess capital due to a legitimate decline in investment opportunities as a result of geopolitical factors outside their control. The market took this as a positive signal reflective of a responsible management, contributing to the rise in share price.



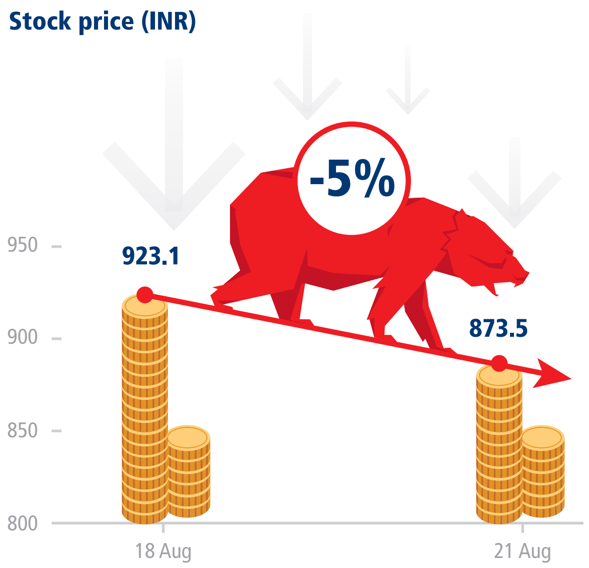
Scenario A – Positive Market Reaction to Responsible Buyback Policy

Scenario B

Buyback not supported by strong fundamental growth drivers

Later this year, another leading IT company issued a buyback worth INR13,000 crore. The announcement came amidst news of the company battling major corporate governance issues as well as being the target of regulatory scrutiny in one of its major markets, which had sent their stock price into a nose dive. The offer price of INR1,150 represented a 25% premium to the stock's closing price for - the day the average premium offered by competitors has been in the range of 17-18%.

The market interpreted this as a sign that management was trying to divert the shareholders' attention away from their corporate governance issues and artificially boost their share price to combat recent losses in market value. The market responded by sending the company's stock plummeting further 5%.



Scenario B – Negative Market Reaction to Poorly Motivated Buyback

Buybacks are a means for adding shareholder value when the company is undervalued. If management's motivations are any different, the market usually picks up on it and the buyback is unlikely to be successful.

GLOBAL SCENARIO

As markets have opened up with increasing foreign access to developing markets through financial instruments like mutual funds and ETFs, correlations between global markets have risen significantly. As a result, changes in economic and geopolitical factors in any one part of the world can have significant market impact on other parts of the world. Therefore, it is becoming increasingly important to examine the impact of world events on local economies.

Much has happened in the world over the past one year. Here are some of the highlights:

1. The election of a new US President whose policies may arguably be hurting the credibility of the US as a responsible world power.

2. Growing influence of developing economies like India in the global landscape, with India emerging as the fastest growing economy in the world. Certain controversial measures taken by India's own leadership such as de-monetization and implementation of GST may actually be setting the stage for a shift in the global balance of power, with India becoming a far more robust and transparent economy to invest in.

3 At the same time, rising geopolitical tensions like the Doklam border dispute threaten to disrupt these changing trends in unpredictable ways.

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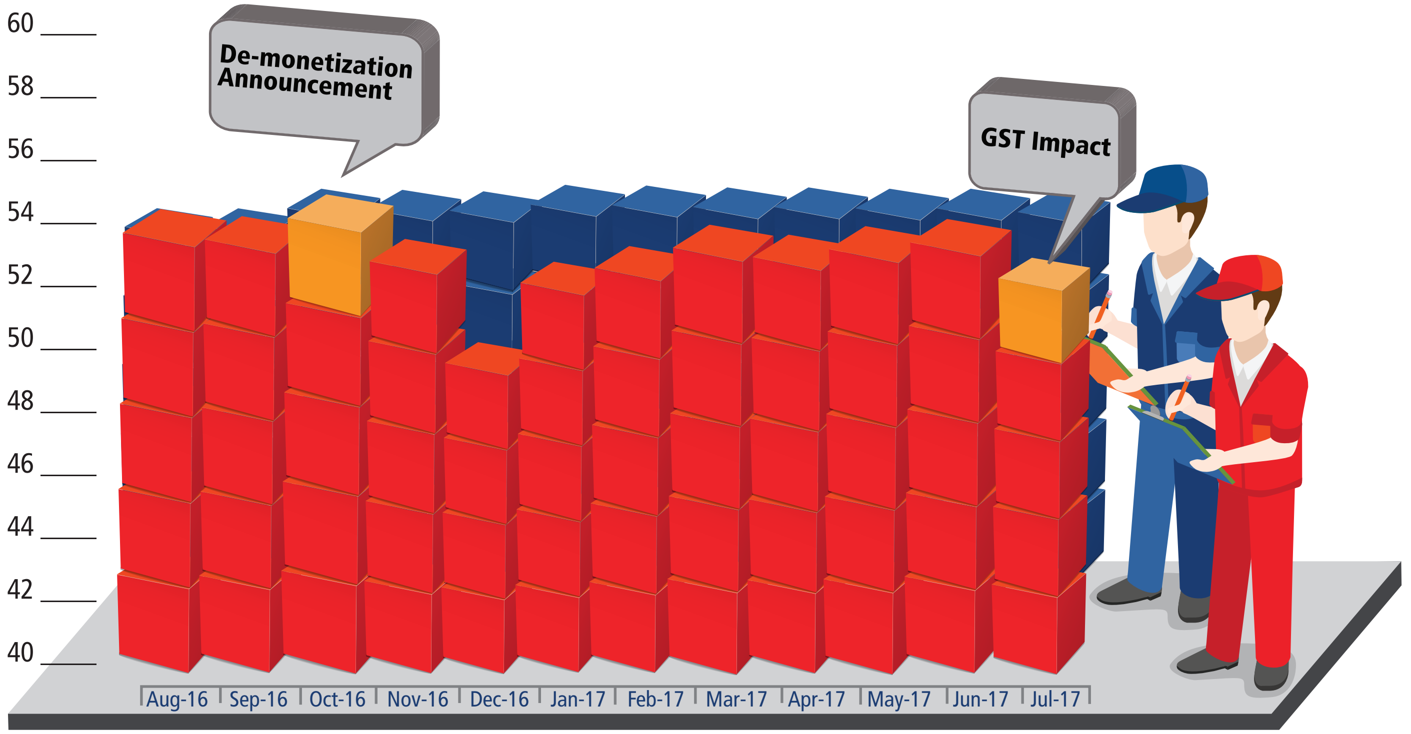
This section evaluates the prospects for the Indian stock market in a global context.

Expanding global PMI: Where does India stand?

The Composite Purchasing Manager's Index (PMI) is widely regarded as a measure of the health of an economy and is driven by key economic indicators such as inflation, exports, employment and inventories. The index is prepared on a monthly basis and is available both at the country and global level. Generally a value above 50 indicates economic expansion for the period, whereas a value below 50 suggests economic contraction.

Global composite PMI - India vs. World



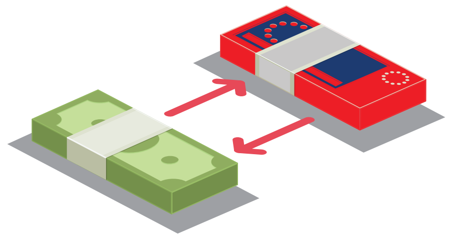
India Composite PMI   Global Composite PMI   Source: www. markiteconomics.com

Trends in Global vs. India PMI during FY17 reveal the following insights:

India PMI marginally under-performed Global PMI through most of FY'17 due to impact of de-monetization and GST. However, long-term fundamentals for Indian economy remain strong which is a positive sign for Indian markets.

Global Growth: The Global PMI has tracked above 50 throughout the previous year averaging 53.3, signalling robust global economic growth.

De-Monetization Effect: The India PMI lied above the Global PMI for the period Aug-Sept '16, signalling strong fundamentals of the Indian economy. The month of November did see a sudden drop in India's PMI below 50 – this reflects the shock of de-monetization as the sudden drop in liquidity caused Indian businesses to temper their output. However, this impact was only temporary as the India PMI returned to above 50 levels by Feb'17.



GST Effect: India's PMI fell back below 50 in July'17. This occurred due to implementation of the GST earlier in the month, which again generated some economic uncertainty regarding clarification of rules and the precise impact on different types of businesses.

In spite of the dips in India's PMI in 2016-17, the index has still averaged above 50 for the period signalling overall economic expansion. Moreover, policy initiatives like de-monetization and GST that may have contributed to these temporary declines are likely to improve India's investment climate in the long run through improved transparency and enforcement of rules and regulations.

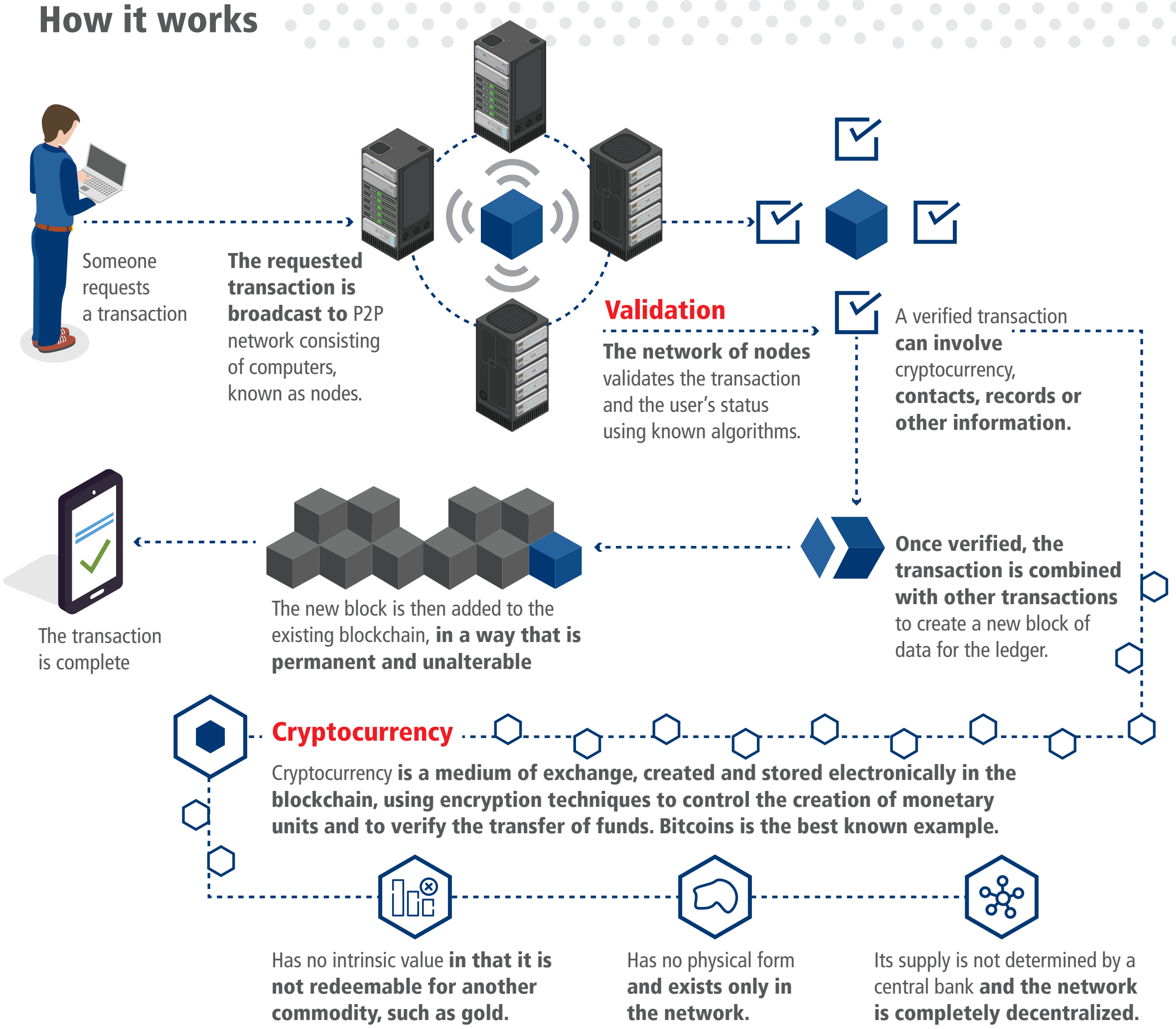
CRYPTOCURRENCY: BITCOIN AND ETHEREUM

Today, cryptocurrencies, Bitcoin and Ethereum being the most prominent among them, are a global craze, with their valuations and market capitalization shooting through the roof. A cryptocurrency is a digital or virtual currency that uses cryptography for security. Cryptocurrency is de-centralized and organic in nature i.e. it is theoretically immune to any interference or manipulation by any central authority, even government or regulatory authorities.

Cryptocurrencies use a distributed public ledger called blockchain, a record of all transactions updated and held by currency holders, in order to keep the faith and everything in check. Units of cryptocurrency are created through a process called "mining," which uses complicated mathematical formulas to generate coins. Bitcoin was the first cryptocurrency, then came a host of successors, including Ethereum, Ripple and Bitcoin Cash - all running on their own distributed ledger systems.

Cryptocurrencies emerged in 2008, when Satoshi Nakamoto invented Bitcoin, the first and still the most important cryptocurrency. Satoshi never intended to invent an asset class for investment but a "peer-to-peer electronic cash system' to prevent double spending.

How it works



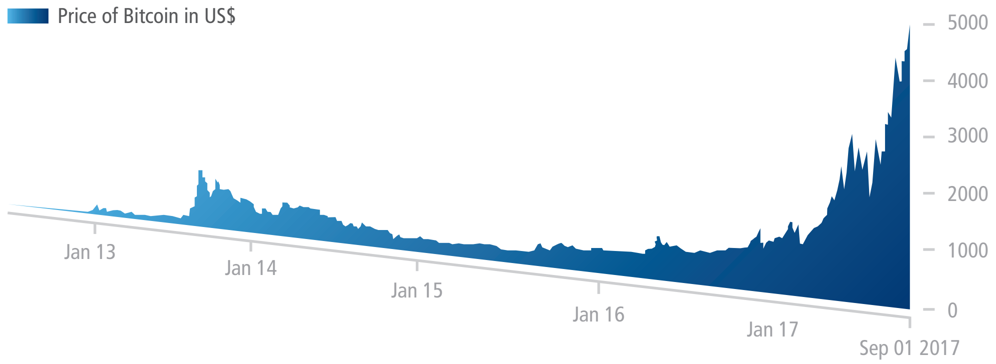
Because of its unique and secure features, cryptocurrencies as well as their underlying blockchain technology is being increasingly adopted by banks and financial institutions across the world, with new use cases like international remittances, machine to machine payments and micro-payments. Several large multinational companies have started accepting payments in Bitcoin, whereas thousands of localized merchants are accepting Bitcoin payments, be it pizza outlets or online music stores. This has led to a significant increase in awareness and interest among people and its potential as a means of making huge trading profits for slightly longer horizon.

Volatile prices and increasing market capitalization

The prices of the major cryptocurrencies have sky-rocketed in the past one year, with Bitcoin already witnessing a price surge of more than 200% in 2017 alone. However, it is also extremely volatile, with price swings of more than 5% in a day not being an uncommon phenomenon. A number of trading platforms for Bitcoins has sprung up globally, with the trend catching up in India as well. Most of them also offer Bitcoin exchange, where the trader/investor can store the purchased Bitcoins in digital form.

The market capitalization of cryptocurrencies has grown at an exponential pace, with the total market capitalization of top 100 cryptocurrencies touching 140 billion USD as of August 2017.

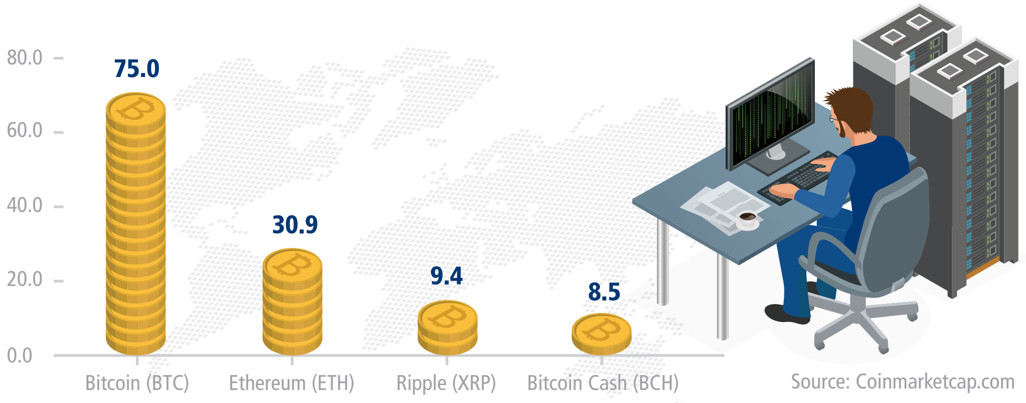
USD price of Bitcoin



Source: Investing.com

Market price of Bitcoin vs USD from February 2012 to August 2017 indicates huge price surge and volatility in 2017.

Market capitalization (billion USD)



Source: Coinmarketcap.com

The number of transactions on the Bitcoin or Ethereum trading platforms in India has also increased exponentially. Leading Bitcoin platforms are reporting 3-5 lakh downloads and adding few thousand users every day. Around 1,000 Bitcoins are traded on a daily basis on an average.

Bitcoin remains the most prominent and widely accepted cryptocurrency, with almost 50% of the total cryptocurrency market capitalization at ~ 70 billion dollars.

Risks associated with cryptocurrencies

Of late, the government and the regulator i.e. the RBI has started taking notice of the burgeoning interest in Bitcoin and its trading activity. Recently in an official statement, RBI has warned users, holders and traders of Bitcoin or any other virtual currency, "about the potential financial, legal, and security risks arising from their use". There is a still a lack of consensus on the regulatory and legal framework to govern or regulate the use of Bitcoin in India.

There are also other pitfalls, such as the recent Bitcoin hard fork on 1st August, wherein Bitcoin experienced a high-profile hard fork when a subset of the community split off the software and created a new version called Bitcoin Cash. It raised concerns regarding the validity and authenticity of the Bitcoin holdings of investors. Immediately after the split of Bitcoin, the newly created Bitcoin Cash as well as the original Bitcoin currency witnessed large scale volatility. Launched on August 1, Bitcoin Cash's value shot up as much as $7.6 billion in market cap before wiping out more than half its value in the proceeding days.

In the light of extreme volatility as well as unpredictability about the regulatory environment, investors need to be extremely careful about investing in cryptocurrencies.

INVESTOR SUCCESS STORIES

Investor success story: Dr. Vijay Kedia, Managing Director- Kedia Securities

Dr Vijay Kedia is one of India's most successful stock market investors, who has built a multi-crore portfolio starting from scratch. He is a common man with an extraordinary mind. His investing success could be an inspiration for potential investors.

Investment journey

Mr. Kedia, born in a family of stockbrokers, entered the stock market at the age of 18 after his father passed away. He joined the stock market as a broker not because of his interest but because of compulsion, as he had to support his family business of stock broking. However, he soon left the family business and decided to trade for himself, as he always dreamt of making it big in life and trading was one place where he did not require any infrastructure or huge capital.

At Kolkata he traded in stocks for next 11 years, sometimes making money and sometimes losing it. One day, he reached a point where he was about to sell his mother's jewellery to pay-off his trading losses, but later he recovered the losses without having to sell them. However, this incident was an eye-opener for him and he realized that it was not possible to become a billionaire overnight. The biggest lesson that he learned from his 11 years of trading was the importance of using stop loss. He believes that proper risk rewards and stop loss are important, as a trader cannot survive in the market without stop loss.

Mr. Kedia realized the potential of long-term investments, and he managed to save INR 35,000 to begin his investment journey. After doing his research, he selected an auto stock and invested all his money in that company. The stock did not move for the first year but it tripled in value in the second year, giving him a profit of more than INR 1 lakh on his initial investment. This kicked off a journey of identifying multi-baggers and investing in them for the long term, which has built him a multi-crore portfolio.

From his investment journey, Mr. Kedia identified knowledge, courage and patience as the three most important weapons to win the battle of stock markets. He believes that knowledge is required to identify quality stocks, and to acquire this knowledge one has to read a lot. Mr. Kedia adds that investment should be courageous and investors should invest a meaningful amount, when they find something good to invest in. He also believes that controlling emotion and keeping patience is extremely important in the stock market. According to him, mental strength and financial strength should complement each other and investors should know themselves before knowing the stock market.

Investment style / market preferences

Mr. Kedia has a knack for spotting unpopular and ground-breaking stocks. Short-term investment is a big no-no for him, he invests with a 5+ year horizon. He has a preference for companies that are 10 to 12 years old, as he believes that learnings from these years help the companies to build a strong foundation. Throughout his investment journey, Mr. Kedia has avoided buying junk shares, which has also kept him immune from the various scams in the market.

In his personal life, Mr. Kedia likes to travel alone as he believes that an investor must understand what is happening around the world and always have a fresh perspective. He has been a key speaker in top business universities of India, including IIM Ahmedabad and IIM Bangalore. He also likes to watch news related to stock markets across the world. He enjoys playing badminton and squash and identifies the 3M — music, meditation and markets – as the core of his life. He is very passionate about singing and manages a YouTube channel for his audio-recorded cover songs.

A trader can make money in many trades but can lose all the money in a single trade if he doesn't uses stop loss.

An investor should chase the story behind his investment, not the money on the table. Money can make you rich, but the story can make you wealthy.

In trading, one should remember that, "Rome was not built in a day but Hiroshima and Nagasaki were destroyed in a day".

SUCCESS MANTRA

Mr. Kedia says he strictly adheres to SMILE as a principle in investing; which translates to "small in size, medium in experience, large in aspiration and extra-large in market potential." He looks at the economy as a highway, company as a car and investor as a passenger, with management driving the car. He cautions against buying a stock without a thorough study of the stock's fundamentals, as a bad management is capable of driving a good company into danger.

He believes that stock market investment is a risky affair and the fear of losing money stops many people from investing in the stock market. He prefers investing for the long term to mitigate the risk of volatility and investing in fewer shares so that the company fundamentals can be tracked easily. Mr. Kedia also warns investors against regrets, which he believes is a lifetime disease for stock market investors that affects future judgement and long-term vision.

SMILE

S	M	I	L	E
SMALL IN SIZE	MEDIUM IN EXPERIENCE		LARGE IN ASPIRATION	EXTRA-LARGE IN MARKET POTENTIAL

Never be dependent on the stock market for day-to-day livelihood. Have an alternative source of income. This will insulate you from the volatility of the market and give you holding power.

India is going to be the world's biggest "Bull market" with the largest population of investors.

Future perspective

Mr. Kedia has a bullish view on the market in the long-term and is not bothered about the short-term corrections in the market. He says that the market may be overvalued or overheated for investors who are entering the market for the first time. For people already invested in good stocks, it does not matter.

Mr. Kedia says that he is not sure what is going to happen in the next five to six months but the market should remain bullish for the next five years or 10 years. The market is undergoing a revolution and there are good times ahead.

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2017-18 • Volume 3