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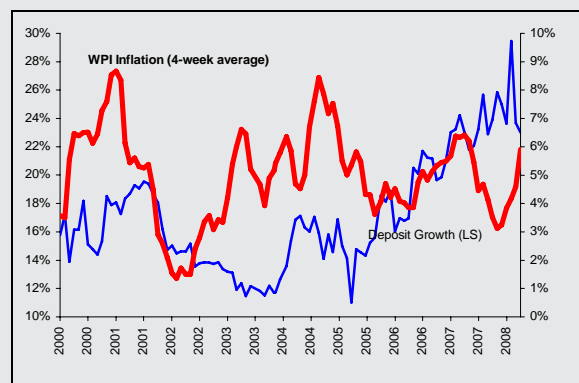
India Strategy

Retrospective – Mar 2008: Macro Slips

Conclusion: March 2008 was a third successive month of underperformance by Indian equities versus emerging and regional markets. India underperformed emerging markets and Asia-Pac by more than 7% and was the second worst performing emerging market for a second month running. The following were notable market indicators in March:

- Pharma, staples and tech sectors were among the top four performers for a second successive month whereas financials and utilities finished at the bottom once again. Sector rotation was markedly low in March and sector performance is being driven by valuations. Mid- and small-cap continued to underperform large cap.
- Institutional flows were mixed with FIIs buying futures and domestic institutions selling cash.
- Market metrics were mixed. Trading activity dropped again. Cash trading, derivatives trading, open interest are now down 45%, 56% and 44%, respectively from their recent highs. Breadth improved and ended March up 25% MoM. Inter-day volatility continues to rise and is now 75 bps higher than its July 2007 low.
- The yield curve rose 57 bps to a 5-month high; corporate bond spreads widened noticeably.
- Rupee depreciated by more than 4% against the euro to its lowest level ever.
- The consensus revised earnings down by over 2% during March.
- Inflation spiked up sharply and, is now higher by 275 bps in eight weeks, whereas deposit growth fell to a seven month low.

India Macro Slips: Growth Slowing, Inflation Rising



Source: CSO, RBI, Morgan Stanley Research

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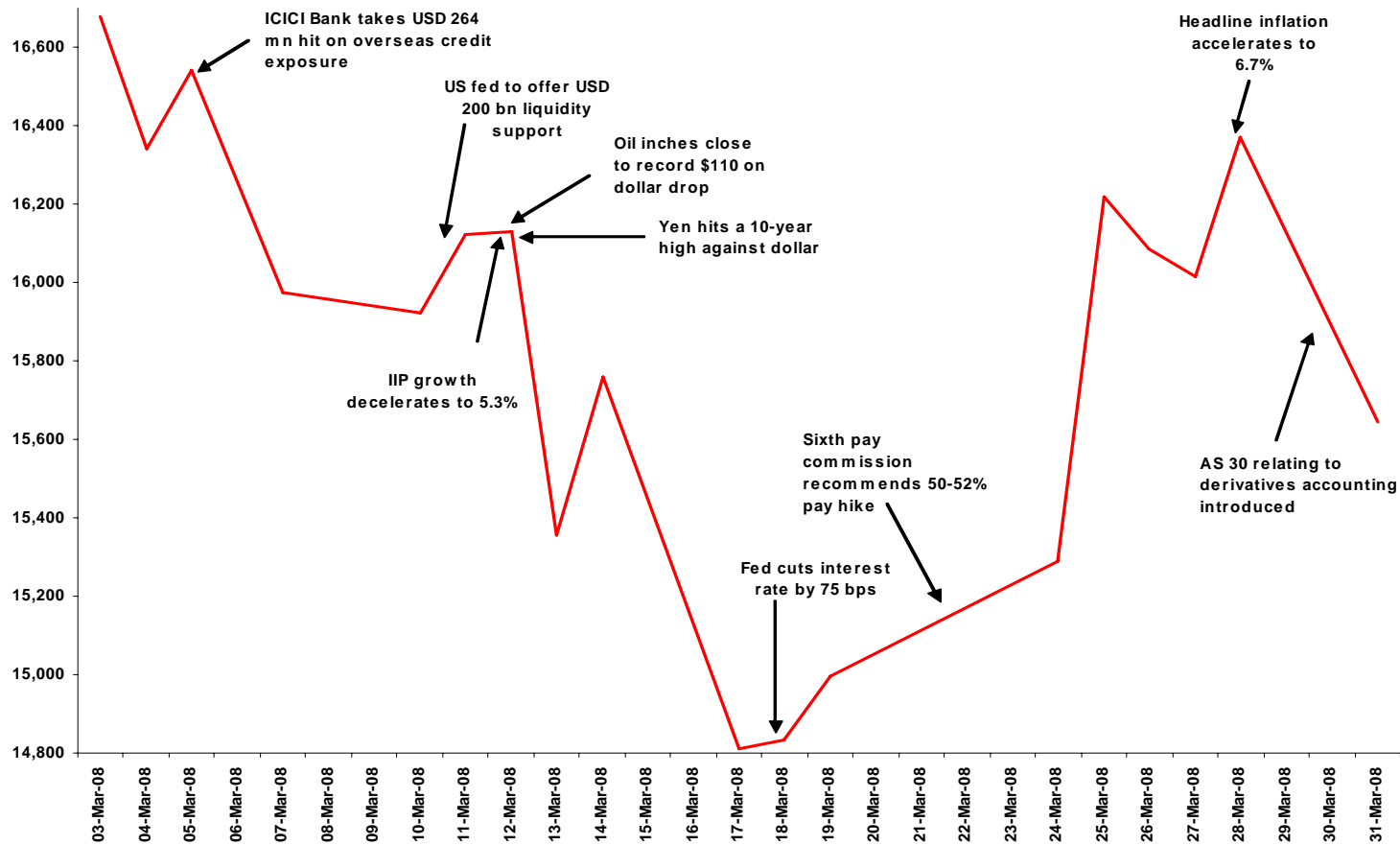
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News Flow and Market Performance



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

Market Performance

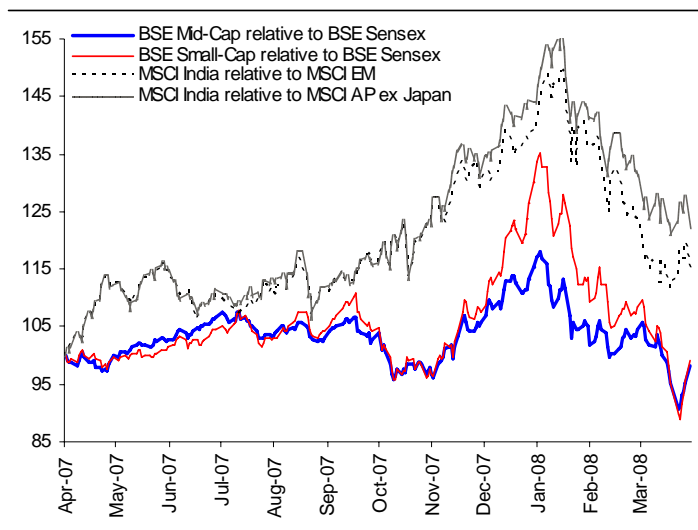
India underperformed emerging markets and Asia-Pac markets for the third successive month in March, underpinning India's high beta status in falling markets. India finished the month almost at the bottom, as the 24th-worst performer in the EM universe. Mid- and small-cap stocks underperformed large caps for the third month running. Despite underperforming emerging markets by 17% in 1Q08, India has still outperformed by about 3% from the August 2007 lows. The Sensex has outperformed the mid- and small-cap indices by 15% and 22%, respectively, since the start of the year.

Equity Markets

	Current	1 Mth	3 Mths	6 Mths	12 Mths	YTD
MSCI India	488	-12.7%	-27.1%	-10.2%	29.6%	-27.1%
MSCI EMF	1,105	-5.4%	-11.3%	-8.3%	18.9%	-11.3%
MSCI EM Asia	439	-6.8%	-14.5%	-14.5%	18.6%	-14.5%
MSCI Europe	107	-4.2%	-16.2%	-19.1%	-18.1%	-16.2%
MSCI ACWI	364	-1.7%	-9.7%	-11.6%	-3.0%	-9.7%
MSCI Asia Pacific	455	-6.1%	-14.2%	-14.9%	11.2%	-14.2%
BSE Sensex	15,644	-11.0%	-22.9%	-9.5%	19.7%	-22.9%
BSE 100 Index	8,233	-12.5%	-26.2%	-8.2%	25.0%	-26.2%
BSE 200 Index	1,932	-12.9%	-27.3%	-8.8%	24.1%	-27.3%
BSE 500 Index	6,157	-13.4%	-28.3%	-9.1%	24.3%	-28.3%
BSE Midcap Index	6,428	-16.3%	-34.3%	-13.4%	19.4%	-34.3%
BSE Smallcap Index	7,842	-18.6%	-41.3%	-13.8%	21.2%	-41.3%
Dow Jones	12,263	0.0%	-7.6%	-11.8%	-0.7%	-7.6%
Nasdaq	2,279	0.3%	-14.1%	-15.6%	-5.9%	-14.1%
India's Rank In 25 EM countries		24	24	19	8	24

Note: All MSCI Indices are in US\$. Source: Bloomberg, MSCI, Morgan Stanley Research

Relative Performance



Source: Bloomberg, MSCI, Morgan Stanley Research

Sector Performance

Healthcare was the best performing sector in March with consumer staples in the second spot. Financials was the worst performing sector in the month followed by utilities. There was very little sector rotation with only telecoms and materials changing performance month-on-month. All MSCI India sectors except Consumer Staples and healthcare underperformed the respective EM sectors. Valuation is clearly a theme driving sector performance with the richly valued sectors performing poorly in 1Q08 and vice versa.

India: Sector Performance

	Weights	Absolute Performance					Rank		
		1 Mth	2 Mths	3 Mths	12 Mths	YTD	1 Mth	12 Mths	YTD
MSCI India	100%	-12.5%	-13.2%	-25.7%	19.7%	-25.7%			
Cons. Discretionary	3.7%	-4.2%	-4.5%	-18.2%	-11.5%	-18.2%	3	9	3
Consumer Staples	4.6%	0.2%	5.8%	-0.2%	22.0%	-0.2%	2	6	1
Energy	19.2%	-8.0%	-7.5%	-21.7%	52.2%	-21.7%	5	2	5
Financials	29.1%	-21.6%	-25.7%	-32.8%	29.7%	-32.8%	10	5	9
Healthcare	3.1%	1.4%	12.3%	-6.1%	6.9%	-6.1%	1	8	2
Industrials	11.8%	-12.9%	-16.1%	-29.2%	44.1%	-29.2%	7	3	7
Information Tech.	11.5%	-6.9%	-2.6%	-18.2%	-26.5%	-18.2%	4	10	4
Materials	7.6%	-13.2%	-7.7%	-28.8%	43.9%	-28.8%	8	4	6
Telecommunication	4.0%	-10.9%	-14.1%	-33.0%	16.6%	-33.0%	6	7	10
Utilities	5.3%	-13.3%	-17.4%	-31.8%	93.1%	-31.8%	9	1	8

All MSCI indices in local currency. Source: Bloomberg, MSCI, Morgan Stanley Research

India: Relative to EM Sectors

	Relative Performance					Rank		
	1 Mth	2 Mths	3 Mths	12 Mths	YTD	1 Mth	12 Mths	YTD
MSCI India	-7.7%	-17.5%	-17.3%	-2.0%	-17.7%			
Cons. Discretionary	-1.8%	-6.8%	-8.5%	-3.7%	-10.2%	4	9	4
Consumer Staples	3.5%	0.7%	4.1%	13.6%	3.3%	2	6	1
Energy	-0.7%	-9.9%	-9.6%	21.1%	-9.9%	3	4	3
Financials	-15.4%	-25.0%	-19.8%	33.0%	-20.2%	10	2	7
Healthcare	6.3%	7.3%	-0.8%	1.3%	-3.2%	1	7	2
Industrials	-5.3%	-19.2%	-15.8%	22.9%	-16.1%	5	3	6
Information Tech.	-7.4%	-12.7%	-17.2%	-20.6%	-15.8%	7	10	5
Materials	-8.6%	-18.1%	-27.3%	13.8%	-28.1%	8	5	10
Telecommunication	-8.8%	-20.5%	-25.7%	-3.2%	-27.0%	9	8	9
Utilities	-7.3%	-21.7%	-21.5%	82.5%	-23.0%	6	1	8

Source: Factset, MSCI, Morgan Stanley Research

NSE's Best- and Worst-Performing Stocks in March with Market Cap Above US\$500mn**India: Best-Performing Stocks**

Company	Price (Rs)	1-Mth (%)	YTD Perf (%)
ICI India Ltd	663	17.3	16.2
Nicholas Piramal	306	11.5	0.9
Dabur India Ltd	111	11.0	-3.0
Asian Paints Ltd	1,200	7.6	9.1
Marico Limited	68	7.5	-1.3
Kansai Nerolac Paints	751	7.3	-14.6
Monnet Ispat & Energy	490	6.7	-18.4
ABG Shipyard	735	6.5	-26.0
Cipla Ltd	220	6.2	3.5
Panacea Biotec Ltd	338	5.8	-13.0

Source: Bloomberg, Morgan Stanley Research

India: Worst-Performing Stocks

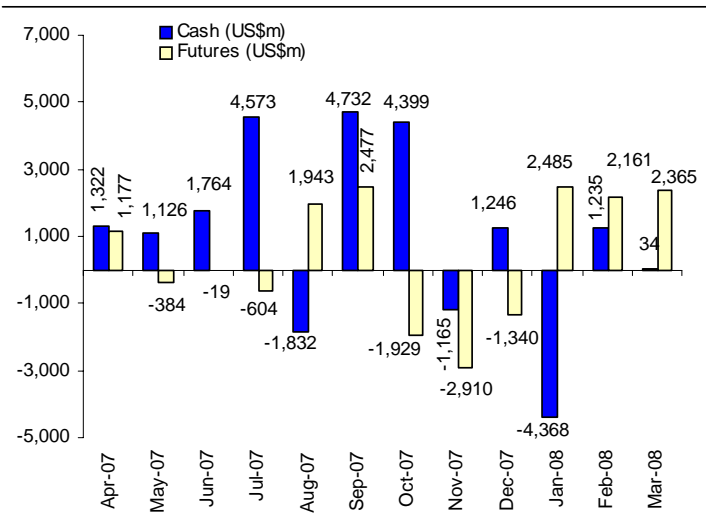
Company	Price (Rs)	1-Mth (%)	YTD Perf (%)
Yes Bank	169	-31.6	-32.3
Indiabulls Financial Services	417	-31.9	-30.1
Reliance Capital	1,229	-32.6	-52.5
Kirloskar Bros	228	-33.4	-56.1
IFCI Ltd	44	-34.2	-52.7
Bhushan Steel	666	-35.2	-57.1
BGR Energy System Ltd	342	-35.8	NA
Rashtriya Chemical services	52	-38.3	-55.7
JM Financial Ltd	1,322	-40.9	-54.4
Jai Corp Ltd	515	-41.5	-57.1

Source: Bloomberg, Morgan Stanley Research

Flows

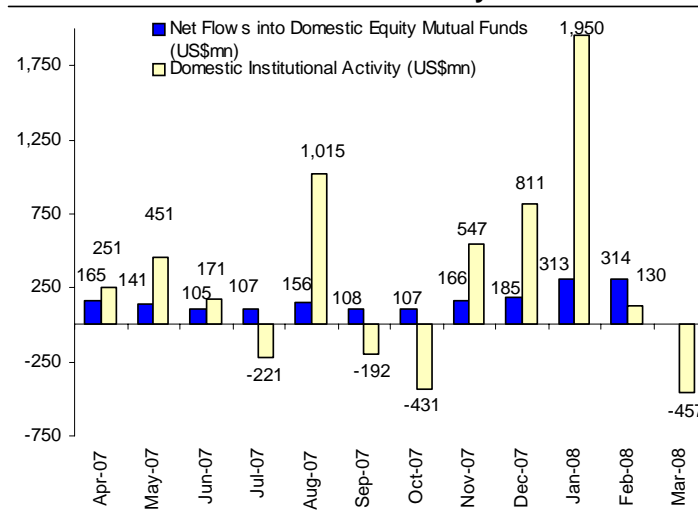
FII flows in the cash segment were flat in March whereas there was net buying in the futures market. Domestic institutions turned sellers having been net buyers for four months running. FIIs have bought US\$3.9 billion worth of stocks and derivatives since the start of the year whereas domestic institutions have purchased US\$1.6 billion in 1Q08 (just marginally less than what they bought in the whole of 2007).

India FII Flows: Equity & Derivatives



Source: SEBI, Morgan Stanley Research

Flows into Domestic Equity Mutual Funds & Domestic Institutional Activity

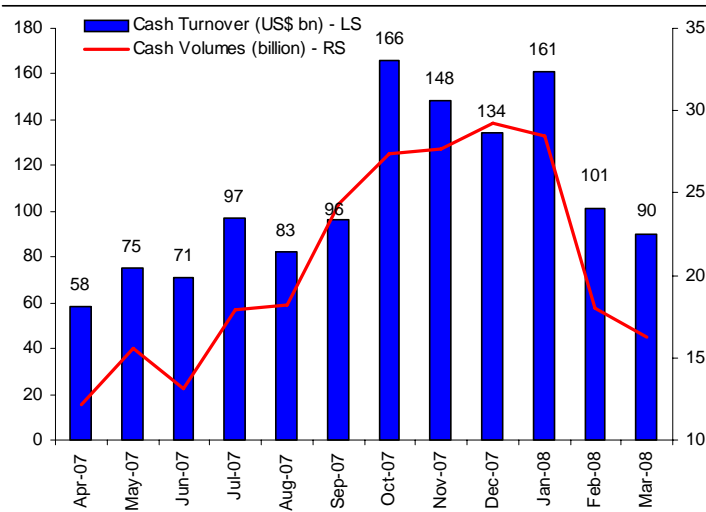


Source: AMFI, SEBI, Morgan Stanley Research

Cash Trading

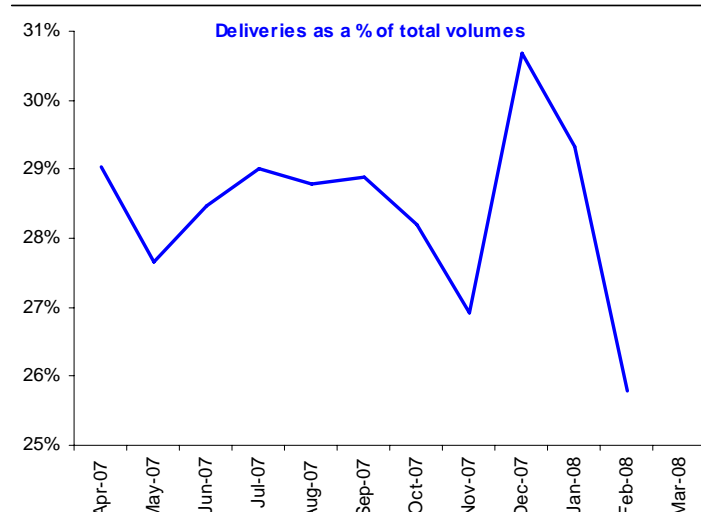
Cash trading volume (number of shares) dropped by 10% in March to a nine month low – off 45% from its Dec-07 peak. Trading volumes (value), also fell by 10% over February to reach a seven month low and 45% below its January peak. Shares purchased for delivery (as a percentage of total trading) continued to decline and hit a 20-month low in February (data comes with a month's lag).

Cash Trading: Turnover and Volumes



Source: BSE, NSE, Morgan Stanley Research

Deliveries to Total Trading

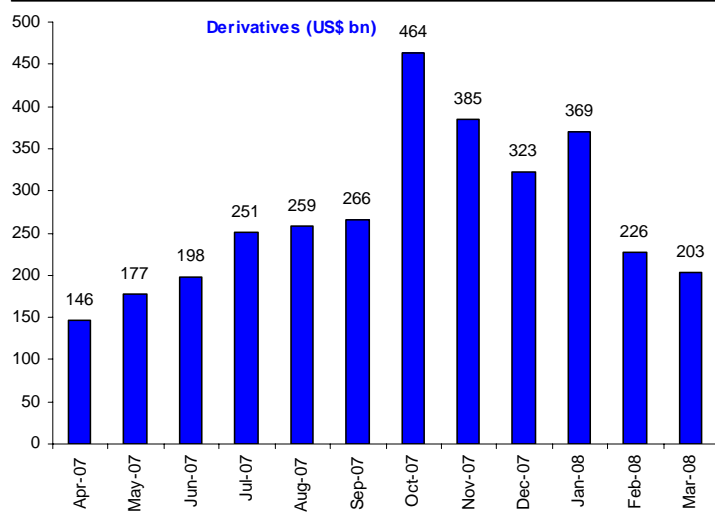


Source: BSE, NSE, Morgan Stanley Research

Futures Market

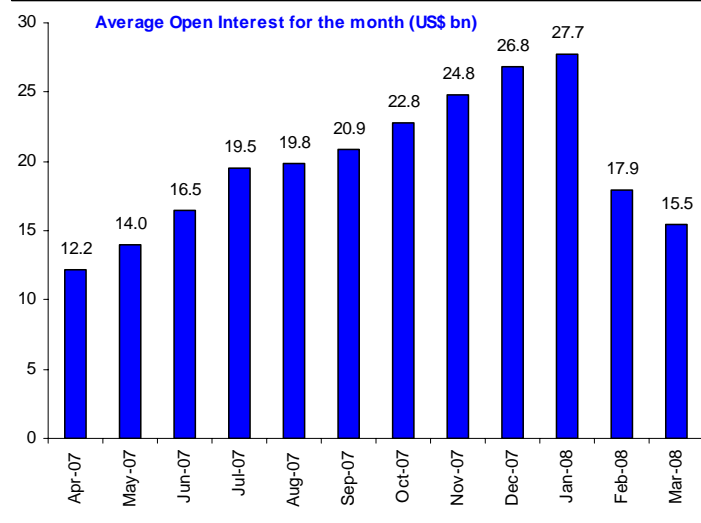
Futures market activity was also depressed in March with derivative volumes falling another 10% points MoM. Derivative volumes are now 56% off their Oct-07 peak. Average open interest for the month of March fell 14% MoM and is now at a 10-month low. Average open interest is 44% off its peak.

Derivatives Volumes



* Only NSE Source: Bloomberg Morgan Stanley Research

Average Open Interest for the Month

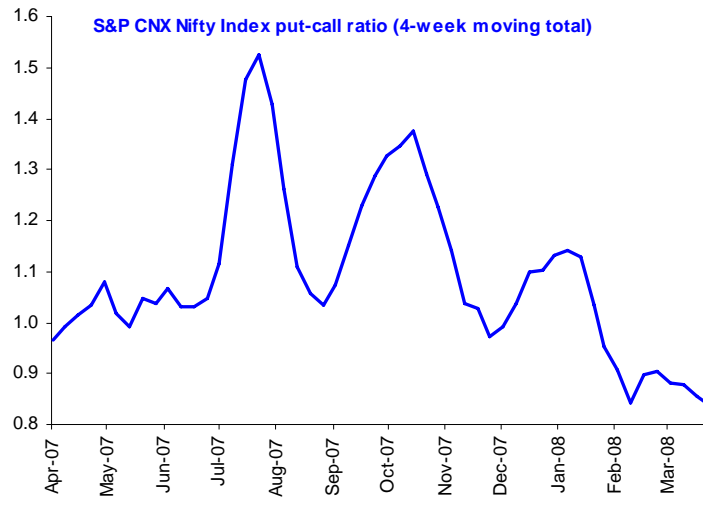


Source: Bloomberg, Morgan Stanley Research

Futures Market

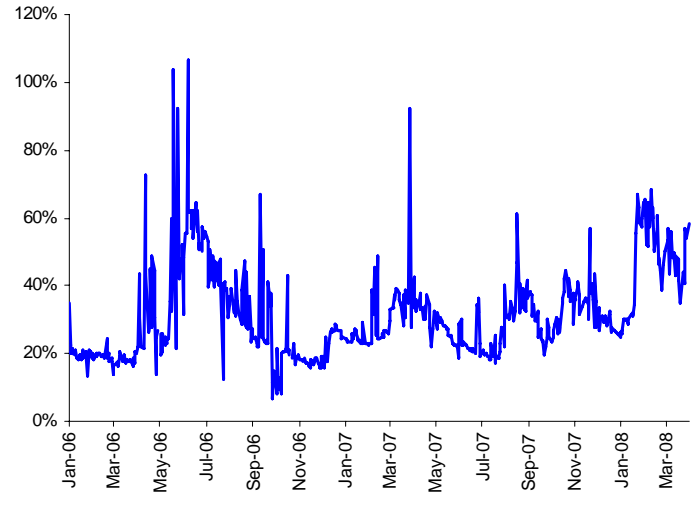
The put-call ratio fell 7% MoM in March and is now down 45% from its Jul-07 peak. On a monthly average basis, the implied volatility increased 6 pp to 49% in March. However, implied volatility is up 23% from its intra-month low in March.

S&P CNX Nifty Index Options: Put-Call Ratio



Source: ASA, Morgan Stanley Research

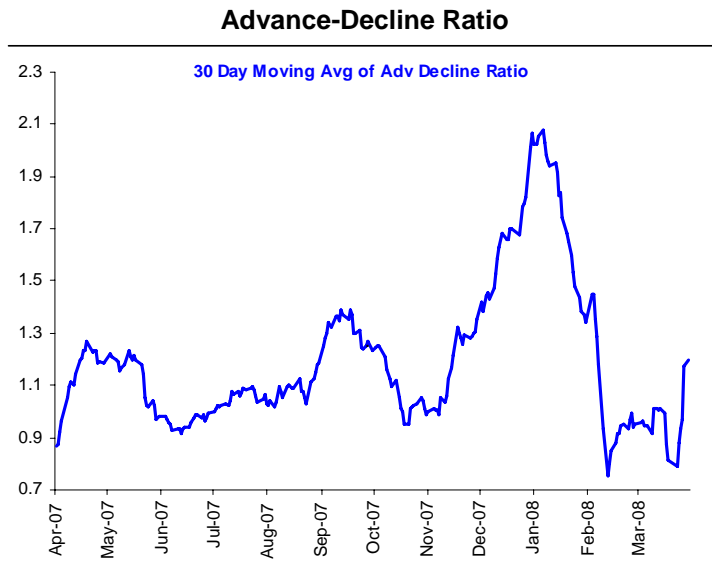
S&P CNX Nifty Index: Implied Volatility



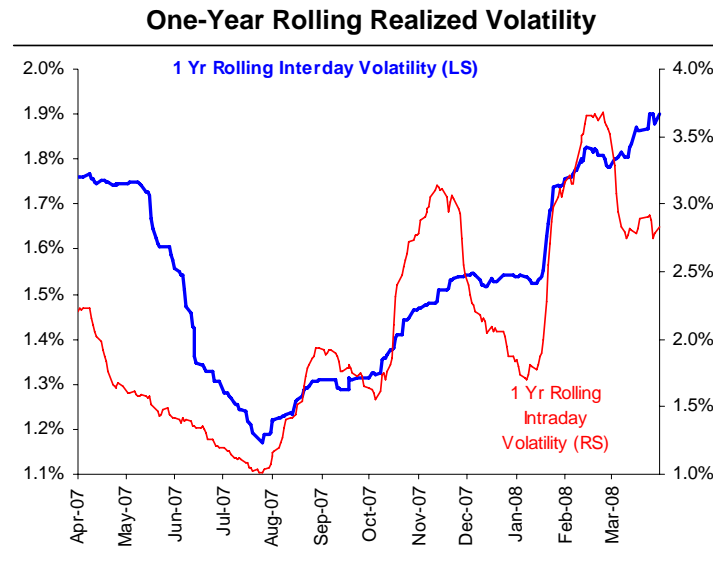
Source: Bloomberg, Morgan Stanley Research

Breadth and Volatility

Market breadth improved in late March and closed the month up 25% from its February end level. Realized intraday volatility stopped its ascent and fell 64 bps (MoM). However, it is still up more than 100 bps from its January lows. In contrast, inter-day volatility continued to rise and was up 12bps (MoM). Inter-day volatility is up 75 bps from its Jul-07 low.



Source: ASA, Morgan Stanley Research

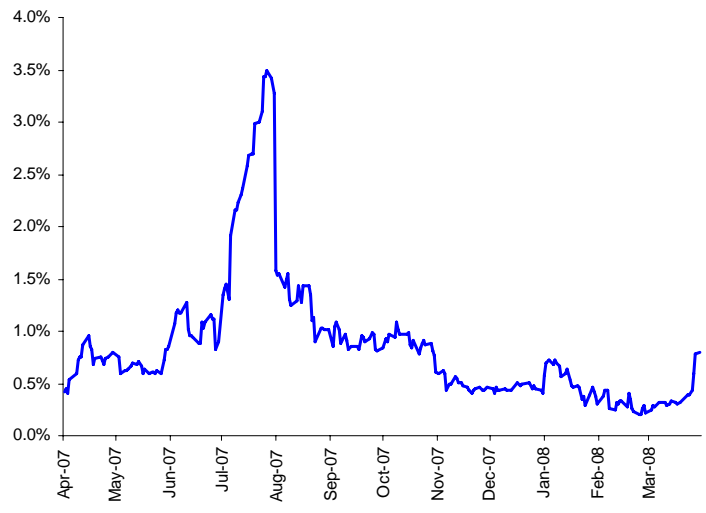


Source: ASA, Bloomberg, Morgan Stanley Research

Bond Market

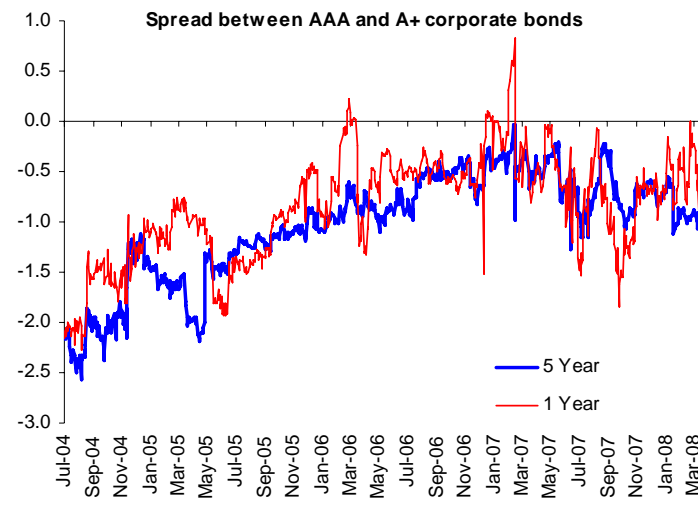
Bond market activity spiked up, having been flat for a few months. The yield curve steepened 57 bps in March to hit a five month high. The spread between Corporate AAA and A+ bonds for five-year maturity also widened 14 bps to 105 bps in March to close to July 2007 levels. The spread between Corporate AAA and A+ bonds for one-year maturity widened by 72 bps to 98 bps – a three month high.

**India: Yield Curve –
Spread versus 10-year and 91-day Yield**



Source: Bloomberg, Morgan Stanley Research

India: Corporate Bond Spread

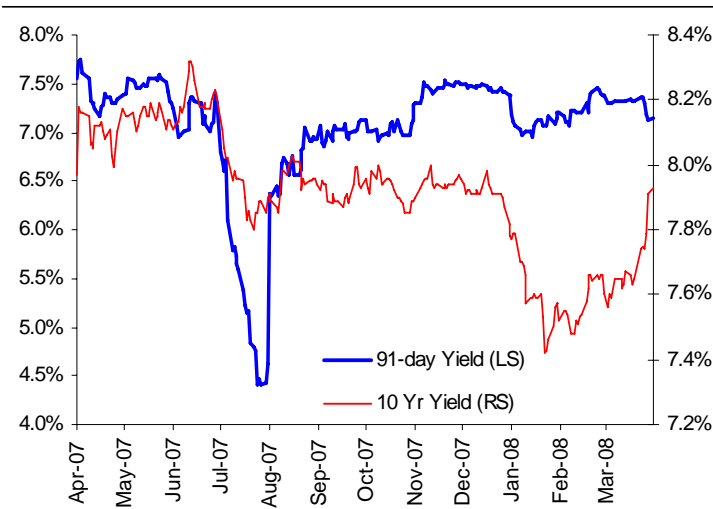


Source: Bloomberg, Morgan Stanley Research

Bond Market

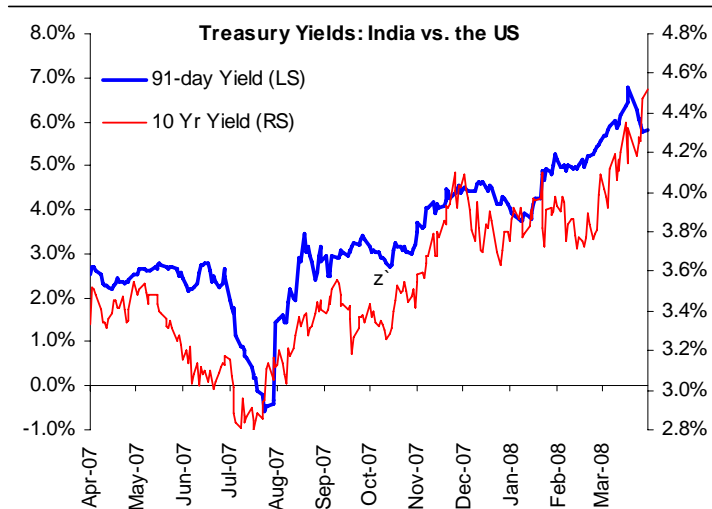
The 10-year bond yield rose 33 bps MoM – its biggest monthly move since Jun-06, while the 91-day yield was down 24 bps in March.

India: 10-year and 91-day Yield



Source: Bloomberg, Morgan Stanley Research

Treasury Yields: India versus the US

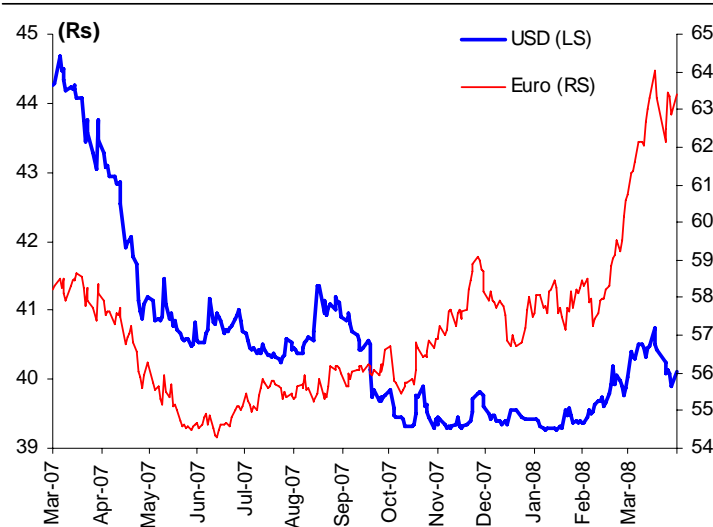


Source: Bloomberg, Morgan Stanley Research

Currency

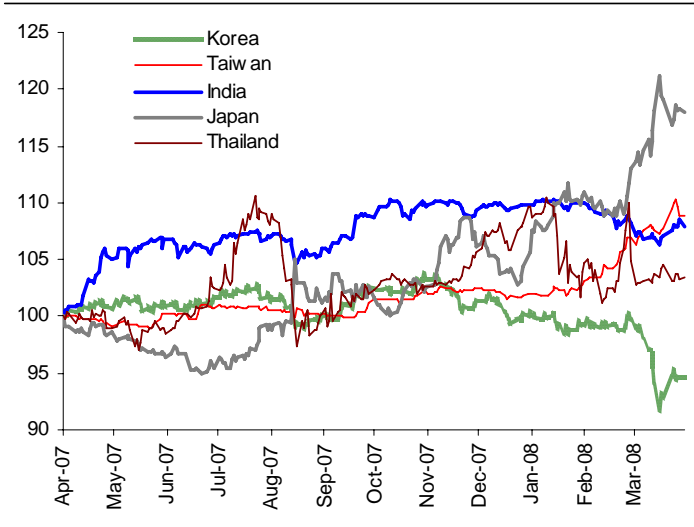
The rupee depreciated by 0.2% against the USD and 4.4% against the Euro (MoM). Year to date, the rupee has depreciated by 10.4% against the Euro and is at an all-time low.

Currency: India versus USD and Euro



Source: Bloomberg, Morgan Stanley Research

Currency: Asian Countries (Rebased)

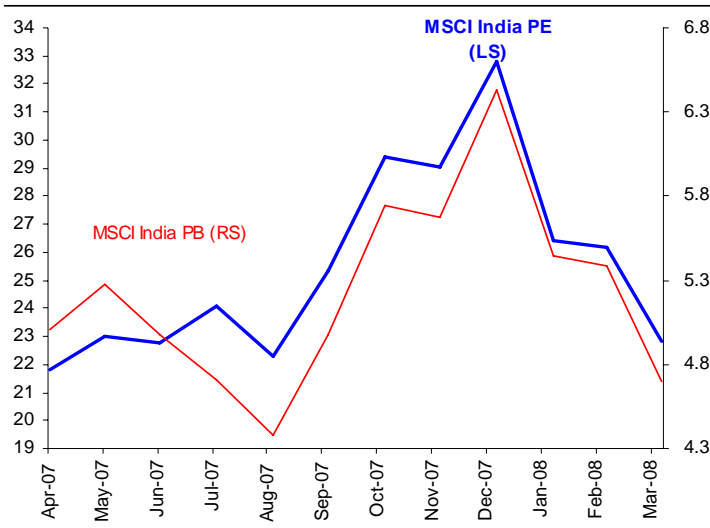


Source: Bloomberg, Morgan Stanley Research

Equity Valuation Snapshot

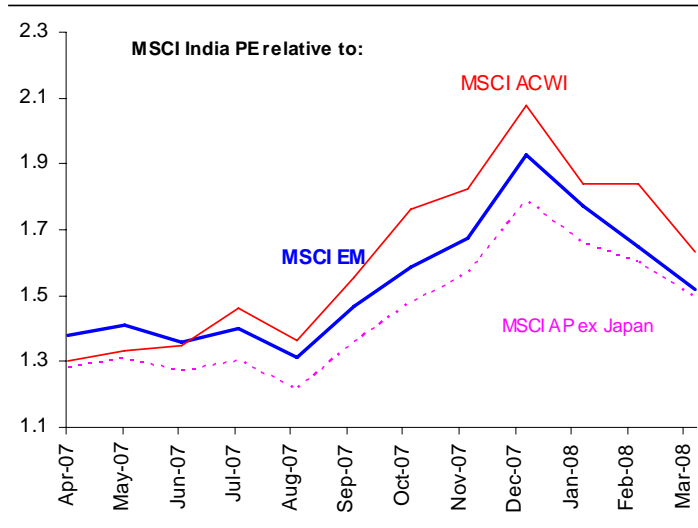
With the MSCI India underperforming MSCI EM and MSCI ACWI during the month, its relative P/E premiums declined to 52% and 63%, respectively. The MSCI India's absolute trailing P/E is close to a 12-month low and 22% off its high but still 32% above its 10-year average.

MSCI India: P/E and P/B



Source: FactSet, Bloomberg, MSCI, Morgan Stanley Research

MSCI India P/E Relative to EM, ACWI, and Asia Pacific ex-Japan

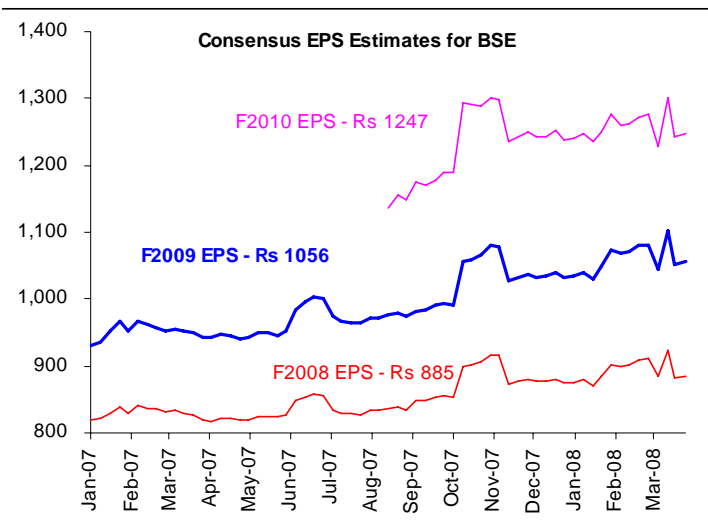


Source: FactSet, Bloomberg, MSCI, Morgan Stanley Research

Earnings Snapshot

In February, aggregate consensus EPS estimates for the BSE Sensex constituents were lowered 2.9%, 2.4% and 2.3% for F2008, F2009 and F2010, respectively. Consensus estimates for F2008 and F2009 have been raised 8% and 12%, respectively, over the past 12 months.

BSE Sensex: Consensus EPS Estimates



Source: IBES, Morgan Stanley Research

Top Earnings Revisions for 2008 by Consensus for Our Coverage Universe

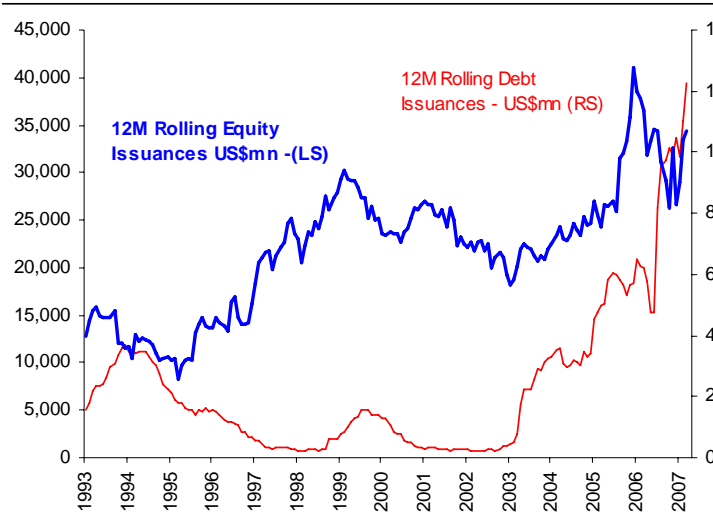
Company	Earnings Revision		Rel. Price Perf	
	1M	3M	1M	3M
Wockhardt Limited	33.0%	32.0%	-11.2%	-17.3%
Nestle India	23.8%	20.5%	22.7%	29.5%
Pantaloon Retail	9.2%	8.6%	-8.4%	-33.0%
Sesa Goa	7.2%	24.4%	1.5%	6.3%
Shoppers' Stop	6.4%	44.4%	-2.0%	-4.8%
Tata Steel	-16.9%	-19.2%	-2.8%	-3.8%
Patni Computer Systems	-9.9%	-9.9%	3.8%	-12.9%
Suzlon Energy	-9.0%	-8.5%	5.3%	-11.7%
Hindalco Industries	-8.3%	-19.4%	-8.8%	-0.6%
Polaris Software Lab Ltd.	-6.9%	-14.6%	-0.6%	-19.3%

Source: IBES, Morgan Stanley Research

Corporate Activity

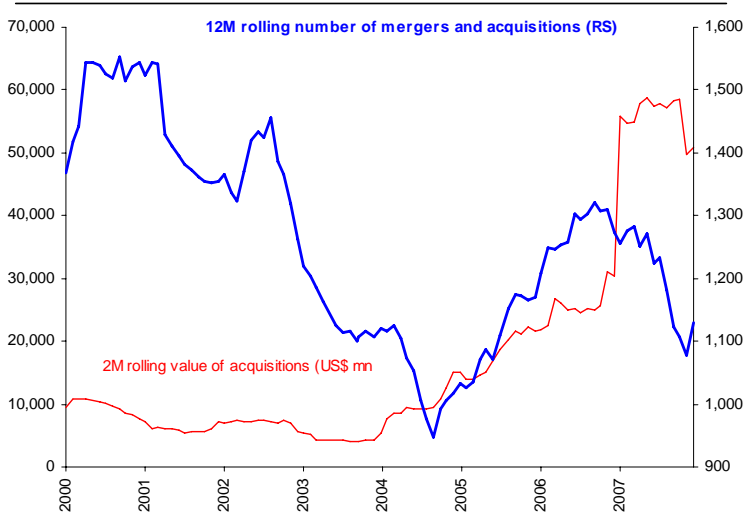
Debt issuances and equity issuances remained strong during February. M&A activity picked up marginally (data available only until January). The primary markets cooled off significantly in March.

Debt Issuances: On a Roll



Source: CMIE, Morgan Stanley Research

M&A Activity

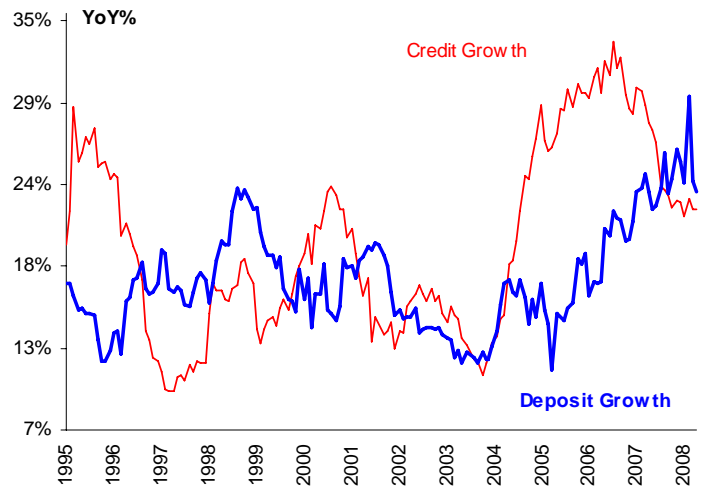


Source: CMIE, Morgan Stanley Research

Macro Indicators

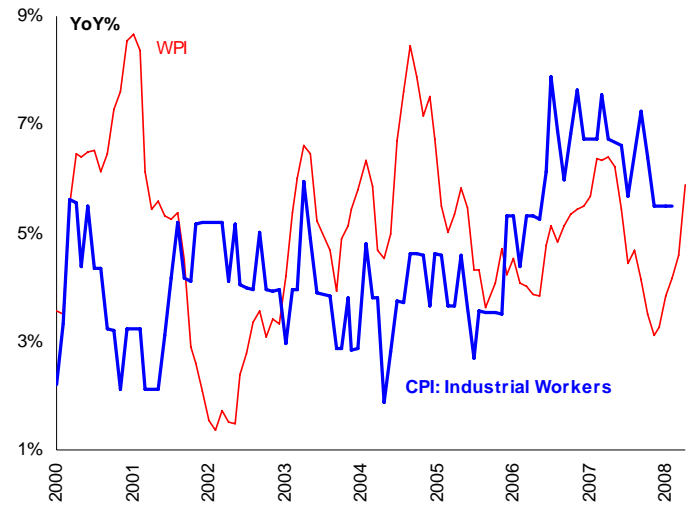
Credit growth at 21.% has slowed to its lowest level since Aug-04. Deposit growth has also come off sharply from its all-time high in January and is now just marginally higher than credit growth. Inflation, as measured by the Wholesale Price Index, continues to accelerate and is now up 275 bps in eight weeks.

Slowdown in Credit Growth



Source: RBI, Morgan Stanley Research

Inflation Spikes



Source: CSO, Morgan Stanley Research

Macro Indicators

	Apr-07	May-07	Jun-07	Jul-07	Aug-07	Sep-07	Oct-07	Nov-07	Dec-07	Jan-08	Feb-08	Mar-08
Trade Balance (US\$billion)	-7.0	-6.2	-7.3	-5.0	-6.9	-4.4	-7.5	-7.4	-5.4	-9.4	-4.2	NA
Exports (US\$billion)	10.6	11.9	11.9	12.5	12.7	12.8	13.3	12.4	12.3	13.1	14.2	NA
Exports (YoY)	23.1%	18.1%	14.1%	18.5%	18.9%	19.3%	35.6%	26.8%	16.0%	20.5%	35.3%	NA
Imports (US\$billion)	17.6	18.1	19.2	17.5	19.6	17.2	20.8	19.8	17.7	22.5	18.5	NA
Imports (YoY)	40.5%	26.4%	36.7%	20.4%	32.6%	2.3%	24.3%	29.3%	18.1%	63.6%	30.5%	NA
Foreign Direct Investment (US\$million)	1551.0	2120.0	1238.0	705.0	831.0	713.0	2027.0	1864.0	1558.0	NA	NA	NA
Foreign Exchange Reserves (US\$billion)	203.7	204.5	213.0	224.9	228.4	247.3	262.0	273.1	272.3	284.5	300.8	306.1
Net FII Flow s (US\$million)	1322.1	1126.2	1764.5	4572.8	-1832.4	4731.8	4399.0	-1165.2	1246.4	-4368.1	1234.9	33.5
Rs/US\$1 (period average)	42.31	40.79	40.78	40.42	40.83	40.35	39.51	39.44	39.44	39.37	39.73	40.38
M3 (YoY)	20.6%	19.9%	21.3%	21.6%	20.6%	20.7%	22.1%	23.3%	22.1%	22.4%	21.2%	NA
Bank Loans (Non-food credit, YoY)	27.0%	26.6%	23.7%	23.4%	23.2%	22.1%	23.0%	22.9%	21.9%	23.2%	22.5%	NA
Money Multiplier	4.5	4.6	4.6	4.5	4.6	4.5	4.7	4.5	4.6	4.7	4.5	4.4
Deposit Growth Rate (YoY)	21.8%	22.1%	23.2%	25.7%	22.9%	23.9%	25.8%	25.0%	23.6%	29.5%	23.7%	NA
Prime Lending Rate	12.8%	12.8%	12.8%	12.8%	12.8%	12.8%	12.8%	12.8%	12.8%	12.8%	12.3%	12.3%
One Year Deposit Rate	8.3%	8.3%	8.3%	8.3%	8.0%	8.0%	8.0%	8.0%	8.3%	8.8%	8.8%	8.8%
364 day T-Bill Yield	7.9%	7.8%	7.8%	7.1%	7.4%	7.4%	7.5%	7.7%	7.7%	7.4%	7.5%	7.5%
91 day T-Bill Yield	7.4%	7.5%	7.2%	5.4%	6.7%	7.0%	7.0%	7.4%	7.5%	7.1%	7.3%	7.3%
10 yr Government Bond Yield	8.1%	8.1%	8.2%	7.9%	7.9%	7.9%	7.9%	7.9%	7.9%	7.6%	7.6%	7.7%
Manufacturing(in %)	12.4%	11.3%	9.7%	8.8%	10.7%	7.4%	13.8%	5.0%	8.3%	5.9%	NA	NA
Consumer Goods	14.7%	8.7%	3.6%	7.1%	0.0%	-0.2%	13.7%	-2.4%	8.4%	7.0%	NA	NA
Basic Goods	8.6%	10.3%	9.2%	8.7%	12.7%	6.5%	6.7%	5.2%	3.6%	3.5%	NA	NA
Capital Goods	10.9%	22.4%	23.1%	12.3%	30.8%	20.9%	20.9%	24.3%	16.6%	2.1%	NA	NA
Intermediate Goods	10.6%	8.8%	8.6%	7.7%	13.8%	10.1%	13.9%	5.7%	7.4%	7.0%	NA	NA
Consumer Price Index (YoY)	6.7%	6.6%	5.7%	6.5%	7.3%	6.4%	5.5%	5.5%	5.5%	5.5%	NA	NA
Wholesale Price Index (YoY)												
- All Commodities	6.0%	4.9%	4.4%	4.7%	3.9%	3.4%	3.1%	3.1%	3.5%	4.1%	4.1%	4.4%
- Manufactured Products	6.0%	5.1%	4.9%	5.1%	4.6%	4.4%	4.2%	3.5%	3.7%	4.2%	4.1%	4.3%

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April 1, 2008
India Strategy

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