MODEL PORTFOLIO

IL&FS INVESTSMART | INDIA'S FINANCIAL MULTIPLEX |

August 2008

Central Bank's new measures make outlook grim for corporate India as it tackles with double whammy of slowing growth and rising financial costs. With earnings season behind and Political equation settled, global cues, progress on reform, progress on nuclear deal and monsoon will decide trend in near term. As markets consolidate in near term, it is likely to remain a trader's delight.

July saw market surviving through the trust vote. It managed to sail through amidst speculation of blatant horse trading and cross voting. Fought on the issue of nuclear deal, we believe, Indo US nuclear deal would turn out to be a turning point in Indian History. The move is more of economic necessity as current hydrocarbon resources are insufficient to meet country's energy need. Hopes that government will be in position to proceed with the reform process, saw market recovering from a low of 3790 seeing a swing of 20% during the month and closing on positive note – up 11.19%.

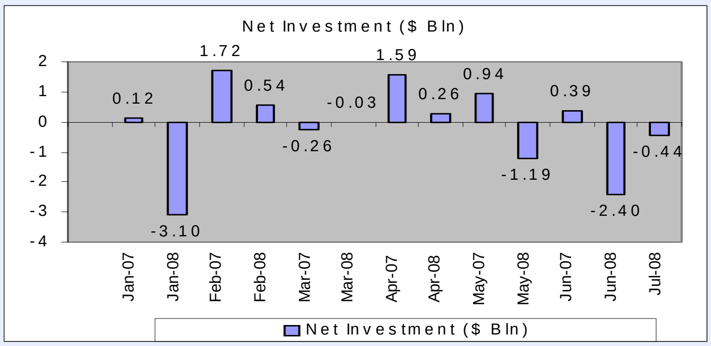
Announcement of merger of SB of Travancore with SBI, modalities for allocation of 3G licenses, Defense Procurement Policy are case in point on progress on reform front. Expectation that government will take forward select increase in FDI, as also banking, pension and insurance sector reform are likely to be positive sentiment provider. Farm sector loan waiver, rising fertilizer and oil subsidies as also VIth pay commission will force Centre to bring divestment back on track. It is likely to target Rs. 200 bn by March next through divestment of 5-10% in Navratnas/ Mini Navratnas including NHPC, OIL and NMDC. BSNL board has also cleared divestment to the tune of $ 10 bn.

Q1 results were in line with expectation. While top line showed healthy growth of 30% plus partly contributed by conversion of order book and higher prices, EBIDTA was under pressure because of spike in input costs, particularly oil and other commodities. 75% increase in financial costs saw bottom-line moving up by a modest 12%, clearly indicating that corporate sector was absorbing large part of cost increase. Impact of MTM losses recognized by a number of companies on their forex transactions/loans also trimmed profit growth which however is cash neutral. Clearly, operating environment is turning very challenging. On the positive side, growth in sales is indicating that demand continues to be strong contradicting the slowdown suggested by IIP numbers.

In a shocking move, RBI increased CRR by 25 bps to 9% and Repo rate by 50 bp to 9%. Signal was clear that government is willing to sacrifice growth for Inflation as it gets ready for election in next 9-10 months. As inflation is more imported in nature, it will take more time to moderate. Thus we believe that as growth rate expectation slows down, impact of rising interest rate will be felt through 2010. Inspite of rising input prices, forex losses and provision, Q1 is likely to emerge as the best quarter for FY09 as going gets more difficult hereon. Lower EBIDTA margins are a major challenge for companies at a time when banks are affecting further increase in lending rates which will increase interest outgo. As analysts adjust to new environment and downgrade EPS, markets could remain volatile as FIIs and investors continue to press sales at every rise.

FII Activity :

FIIs have been sellers through the past few months with outflow for July being $ 0.44 bn, having sold stocks worth $ 6.37 bn. in the calendar. On the other hand, DIIs continued to be on buy side having bought stocks worth Rs 14.12 bn. Probably aggressive marketing of SIP by their marketing teams has seen net inflows during this uncertain period.



Equity market outlook in near term:

Inflation, which is at a 14 year high at 11.98%, seems to be showing signs of peaking out. Any further movement on that and IIP numbers for month of June which are due around August 11th will be watched keenly for possible direction. IIP numbers for May were a major disappointment. Against 7% for April, month of May saw a growth of 3.8% way below the expectation of 6.5%.

Other key positives are continued softening of crude oil prices which is flirting with $ 120 mark amidst reports of US slowdown and oil consumption showing de-growth. It looks set for further down trend due to OPEC increasing supply and slowing global economy squeezing demand.

With IAEA giving its approval for India Specific safeguards – a key step towards operationalizing Indo-US nuclear deal, capital goods sector will stay in limelight. Next in line is the 45 member NSG meeting due on August 21st to consider a waiver for India to allow it to resume nuclear commerce with International community. With centre expected to press forward with reforms in financial sector – Banking (Abolition of 10% voting cap for private sector bank, lowering government holding in state owned bank), - Pension and - Insurance(raising overseas investment limit from 26% to 49%), sentiment is likely to remain positive particularly for financial sector stocks.

Fundamentally things are not looking good incrementally. As banks tighten the lending norms and with slowing consumer spend, off-take has become a question mark. With rising bond yields, markets at 15X 09 are not cheap. Thus markets in near term, will remain a trader's market. There could be a 10-15% upside, with immediate resistance around 4550 and a possibility of 4650-4750 during the month. But investors are likely to sell into upside. Immediate support exists around 4250. Market could broadly oscillate between a low of 4000-4200 and 4650-4750 on upper side during the month. For market to rise, crude price need to drop further to probably $ 110 and below. For investor class looking at LT view, one needs to be cautious and do stock picking slowly. Good bargains to buy strong franchisees are likely on correction.

Our portfolio for July was up 6.01% while index was up 10.76%. We started with 15% cash and increased it to 24% during the month leading to relative underperformance of 4.75%. For the current month, while we are maintaining more or less the same portfolio, we are keeping a cash of 10% in order to take advantage of any correction during the course of the month.

IL&FS INVESTSMART
INDIA'S FINANCIAL MULTIPLEX

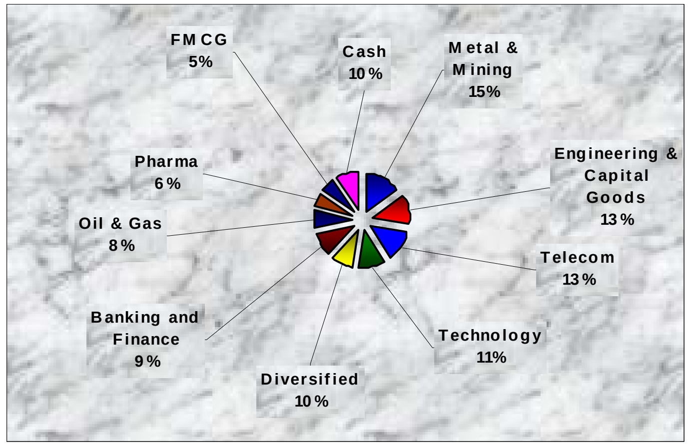
MODEL PORTFOLIO August 2008

Risk: High To Medium Risk
(For Private Circulation Only)

Security Name	% of Total Portfolio	CMP	Target	EPS 08	EPS 09	PE 08	PE 09
Banking and Finance	**9**						
HDFC	4	2277	2480	85	100	26.79	22.77
ICICI Bank*	5	634	700	37	40	17.28	15.90
Diversified	**10**						
Reliance Industries	10	2207	2450	134	160	16.47	13.79
Engineering & Capital Goods	**13**						
Larsen & Toubro	5	2605	2850	76	110	34.50	23.68
Bhel	5	1682	1800	59	80	28.51	21.03
Voltas	3	123	145	6	9	19.52	14.47
FMCG	**5**						
ITC	5	187	205	8	10	22.53	19.08
Metal & Mining	**15**						
Godavari Power	5	201	230	34	48	5.91	4.19
Tata Steel	4	655	710	89	110	7.36	5.95
Jindal Steel & Power	3	2076	2300	82	168	25.32	12.36
Sesa Goa *	3	3372	3750	302	528	11.17	6.39
Oil & Gas	**8**						
Aban Lloyd	5	2502	2950	117	400	21.38	6.26
RPL	3	165	185	5	35	33.00	4.71
Telecom	**13**						
Reliance Communi	**5**	501	520	26	36	19.05	14.11
Bharti Airtel	**5**	798	850	35	45	23.08	17.58
MTNL*	**3**	103	118	7	8	14.45	12.88
Technology	**11**						
Infosys	3	1583	1720	80	97	19.79	16.32
Tanla Solution	**5**	217	240	16	23	13.40	9.43
KLG Systel	3	361	420	45	60	8.02	6.02
Pharma	**6**						
Gleenmark Pharma	3	647	675	24	29	27.53	22.31
Ranbaxy Lab	3	498	550	18	24	27.67	20.75
Cash	**10**						
	100						

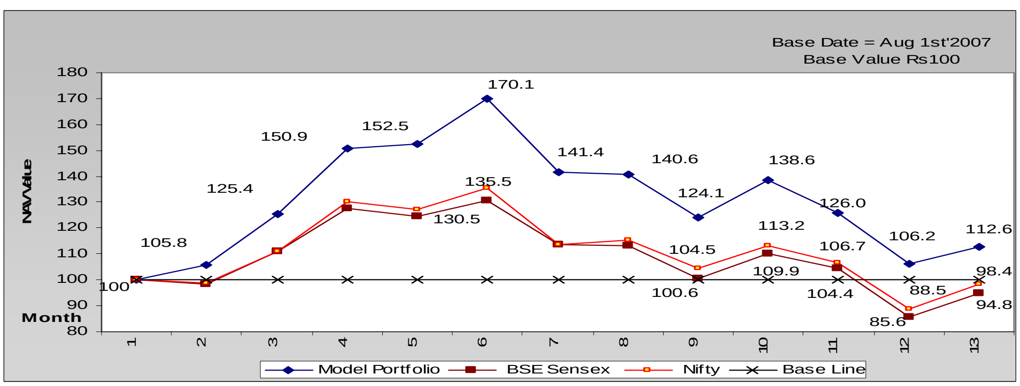
Sectoral Holding :

Sectoral Holding (High Risk) Sector	% of Total Portfolio
Metal & Mining	15
Engineering & Capital Goods	13
Telecom	13
Technology	11
Diversified	10
Banking and Finance	9
Oil & Gas	8
Pharma	6
FMCG	5
Cash	10
Total	**100.00**



Performance Snapshot:

Model Portfolio Vs Sensex & Nifty



Nav Based Return:	Nav Value 1st Aug 08	Nav Value 31st July 08	Absolute Return	JULY 2008 Returns
Model Portfolio	**100**	112.6	**12.63%**	**6.01%**
BSE Sensex	**100**	94.8	**-5.20%**	**10.76%**
Nifty	**100**	98.4	**-1.55%**	**11.19%**