



Sharekhan's top equity fund picks

August was a good month for the markets. Strong corporate earnings, continued capital investments by Indian companies and buoyant global sentiments cheered the Sensex and the Nifty up by almost 9% each. The market saw the Sensex successfully crossing the 11,000 mark and thereafter rising way above the 11,500 level.

Currently nearing the 12,000 mark, the Indian market, as represented by the Sensex appears fairly valued at 16x FY2007E earnings. However, even though the market may seem reasonably valued, with most of the positives already priced in, not all companies in the market may be fairly valued. The trick is to identify and invest in the undervalued companies with good growth prospects.

India's growth story continues to remain strong as the economic indicators continue to reflect the buoyancy in the economy. The Index of Industrial Production, for instance, grew by a strong 10.1% year on year for the first quarter of FY2007. Even the manufacturing sector grew by 11.2% during the same period. The Infrastructure Index, on the other hand, grew by 6.3% for the April-June period.

The capital expenditure spree of Indian companies too, continues unabated. Investments worth Rs500,000 crore have been lined up by India Inc in various sectors. Driven by the expansion activities of Indian companies as well as the growing consumer demand owing to the rising salary levels, increasing employment and rising savings rate in the country, the earnings of the corporate sector should continue to grow in the quarters ahead.

Trading activities of mutual funds (MF) and foreign institutional investors (FIIs) too, reflect the positive sentiment in the market. Mutual funds have been net buyers to the tune of Rs1,000 crore in the previous one month and of Rs12,000 crore during the current year. Retail investors are also returning to the market, as is evident from the surge in the BSE Mid-Cap index and the BSE Small-Cap index, which typically mirror retail activity in the market. In August the two indices rose by 12% and 13% respectively.

Encouraged by the decision of the US Federal Reserve (Fed) to take a break from the rate hike exercise as well as the ceasefire in the

Middle East and the resulting softening of crude oil prices, FIIs too are slowly coming back to the markets. In the past one month they have bought Indian equities worth over Rs3,000 crore, reaffirming their faith in the India story. The FIIs are still net buyers of equities worth Rs1,764.3 crore in our markets in the year till date.

Going forward, the direction of the market in the short-term is likely to be determined by global cues. Even though it seems that the Fed is done with its rate hike exercise for the present, it is not clear as to whether the Fed's pause is temporary or the rate hikes may resume again. Even though the US housing market and employment data is indicating that the US economy might be cooling off, the inflation level in the USA still remains above the Fed's comfort level of 1-2%. This might prompt the Fed to hike rates once again, which will lead to immense volatility in the market. Hence we advise caution in the mid term. However with the domestic economy going great guns, the outlook for the long term remains bullish.

We have identified the best equity-oriented schemes available in the market today based on the following parameters: the past performance as indicated by the returns, the Sharpe ratio and Fama (net selectivity).

The past performance is measured by the returns generated by the scheme. Sharpe indicates risk-adjusted returns, giving the returns earned in excess of the risk-free rate for each unit of the risk taken.

FAMA measures the returns generated through selectivity, ie the returns generated because of the fund manager's ability to pick the right stocks. A higher value of net selectivity is always preferred as it reflects the stock picking ability of the fund manager.

For our selection of funds, we have given 50% weightage to the past performance as indicated by the returns, 25% weightage to the Sharpe ratio of the fund and the remaining 25% to the FAMA of the fund.

All the returns stated below, for less than one year are absolute and for more than one year the returns are annualised.

We present below our recommendations in the equity-oriented mutual fund category.

Aggressive Funds

Mid-cap Category

Scheme Name	NAV	Returns as on August 31, 2006 (%)				
		3 months	6 months	1 year	2 years	3 years
Sundaram Select Midcap	77.40	-4.04	17.22	54.09	69.15	67.89
Birla Mid Cap Fund	52.99	-0.53	4.79	28.77	49.94	50.80
Reliance Growth	215.98	-2.07	4.98	28.93	60.30	61.56
Indices						
S&P Nifty	3413.90	11.16	11.03	43.16	44.64	35.91
BSE Sensex	11699.05	12.51	12.81	49.88	50.11	40.08

Opportunities Category

Scheme Name	NAV	Returns as on August 31, 2006 (%)				
		3 months	6 months	1 year	2 years	3 years
Prudential ICICI Dynamic Plan	52.84	4.79	14.31	42.88	67.90	50.00
DSP ML Opportunities Fund	46.84	6.17	7.70	43.50	54.12	50.85
Indices						
S&P Nifty	3413.90	11.16	11.03	43.16	44.64	35.91
BSE Sensex	11699.05	12.51	12.81	49.88	50.11	40.08

Equity Diversified/Conservative Funds

Scheme Name	NAV	Returns as on August 31, 2006 (%)				
		3 months	6 months	1 year	2 years	3 years
SBI Magnum Global Fund 94	33.85	-4.19	6.98	40.87	74.40	75.39
SBI Magnum Multiplier Plus 93	44.04	3.28	6.79	45.30	68.94	63.13
HDFC Equity Fund	127.40	10.56	9.03	50.00	57.14	50.33
DSP ML Equity Fund	37.66	3.78	8.75	39.59	58.80	51.43
Birla SunLife Equity Fund	146.67	6.21	5.15	35.55	57.76	55.99
Indices						
S&P Nifty	3413.90	11.16	11.03	43.16	44.64	35.91
BSE Sensex	11699.05	12.51	12.81	49.88	50.11	40.08

Thematic/Emerging Trend Funds

Scheme Name	NAV	Returns as on August 31, 2006 (%)				
		3 months	6 months	1 year	2 years	3 years
DSP ML Tiger Fund	26.25	3.75	7.32	46.08	56.19	--
Tata Infrastructure Fund	19.20	0.58	10.35	47.16	--	--
SBI Magnum Sector Umbrella - Contra	31.43	2.75	10.55	43.45	71.63	72.93
HDFC Core & Satellite Fund	22.42	2.38	5.95	42.75	--	--
Templeton India Growth Fund	57.67	6.46	9.08	34.43	42.58	41.33
Indices						
S&P Nifty	3413.90	11.16	11.03	43.16	44.64	35.91
BSE Sensex	11699.05	12.51	12.81	49.88	50.11	40.08

Balanced Funds

Scheme Name	NAV	Returns as on August 31, 2006 (%)				
		3 months	6 months	1 year	2 years	3 years
DSP ML Balanced Fund	33.77	5.70	6.77	32.90	35.00	33.66
HDFC Prudence Fund	97.93	8.46	9.47	32.55	43.65	39.13
JM Balanced	19.87	2.69	7.87	34.08	34.40	27.35
Kotak Balance	22.31	-0.33	3.45	30.57	43.38	37.92
SBI Magnum Balanced Fund	30.67	2.13	7.43	29.63	48.17	45.57
Indices						
Crisil Balanced Fund Index	2209.15	7.37	8.05	26.65	26.84	22.93

Tax Planning Funds

Scheme Name	NAV	Returns as on August 31, 2006 (%)				
		3 months	6 months	1 year	2 years	3 years
SBI Magnum Tax Gain Scheme 93	44.72	5.15	6.99	30.00	78.44	79.87
HDFC Tax saver	125.08	3.31	7.70	31.81	66.03	61.56
Prudential ICICI Taxplan	85.41	1.36	9.53	27.92	64.01	59.88
Birla Equity Plan	48.05	1.26	5.79	30.47	51.23	48.87
HDFC Long Term Advantage Fund	80.08	1.42	1.17	25.23	47.35	56.81
Indices						
S&P Nifty	3413.90	11.16	11.03	43.16	44.64	35.91
BSE Sensex	11699.05	12.51	12.81	49.88	50.11	40.08

Every individual has a different investment requirement, which depends on his financial goals and risk-taking capacities. We at Sharekhan first understand the individual's investment objectives and risk-taking capacity, and then recommend a suitable portfolio. So, we suggest that you get in touch with our Mutual Fund Advisor before investing in the best funds.

Risk-Return analysis

The charts on the following pages give you a snapshot of how the mutual funds have performed on the risk-return parameters in the past. We have used the bubble analysis method to measure their performances on three parameters viz risk, return and fund size. The risk is measured by standard deviation, which measures the average deviation of the returns generated by a scheme from its mean returns. We have tried to explain the same with the help of a diagram, which is divided into four quadrants, with each quadrant containing funds of a particular risk-return profile. The size of the bubble indicates the size of the fund.

The funds in the **high-risk high returns** quadrant follow a very aggressive approach and deliver high absolute returns compared to the peers albeit at a higher risk.

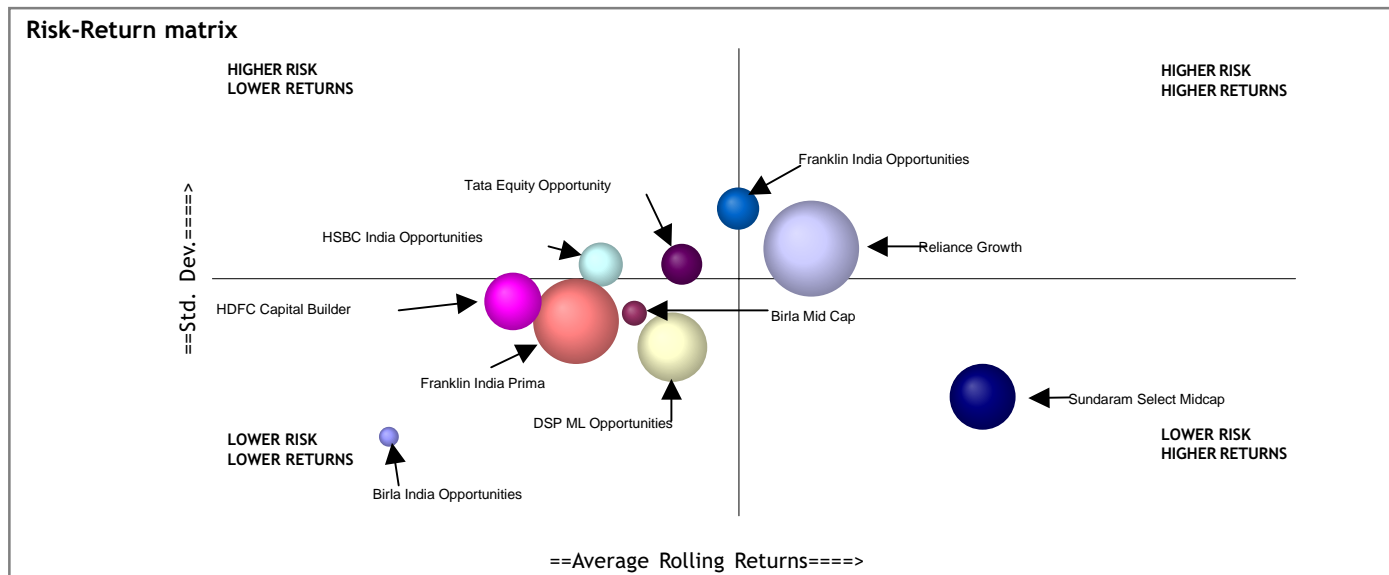
The funds in the **low-risk high returns** quadrant outperform the peer group on the risk-adjusted returns basis as they deliver higher returns compared to the peers without exposing the portfolio to very high risk.

The funds in the **low-risk low returns** quadrant are not very aggressive and provide lower absolute returns, taking lower risks.

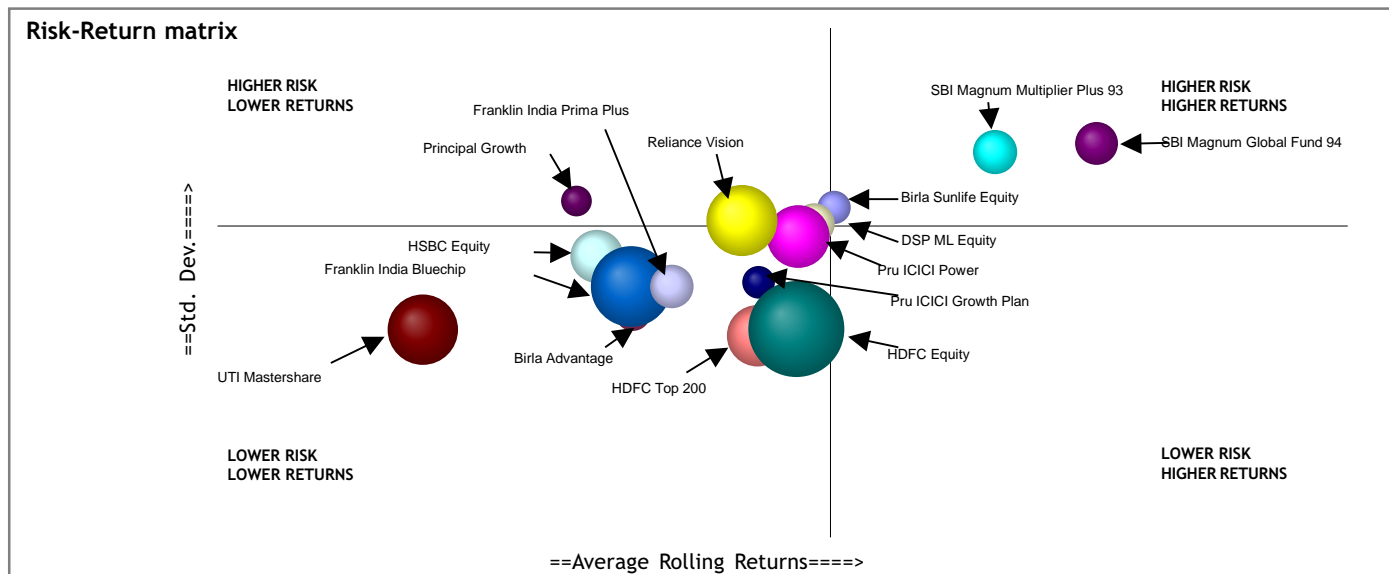
The funds in the **high-risk low returns** quadrant underperform the peers on the risk adjusted returns basis as they adopt a high-risk strategy but the returns fail to compensate the risk taken by the fund.

For aggressive, conservative and tax planning funds, risk is measured in terms of two years' volatility while returns are measured as two years' average rolling returns as on August 31, 2006. For thematic and balanced funds, risk is measured in terms of one year's volatility while returns are measured as one year's average rolling returns as on August 31, 2006.

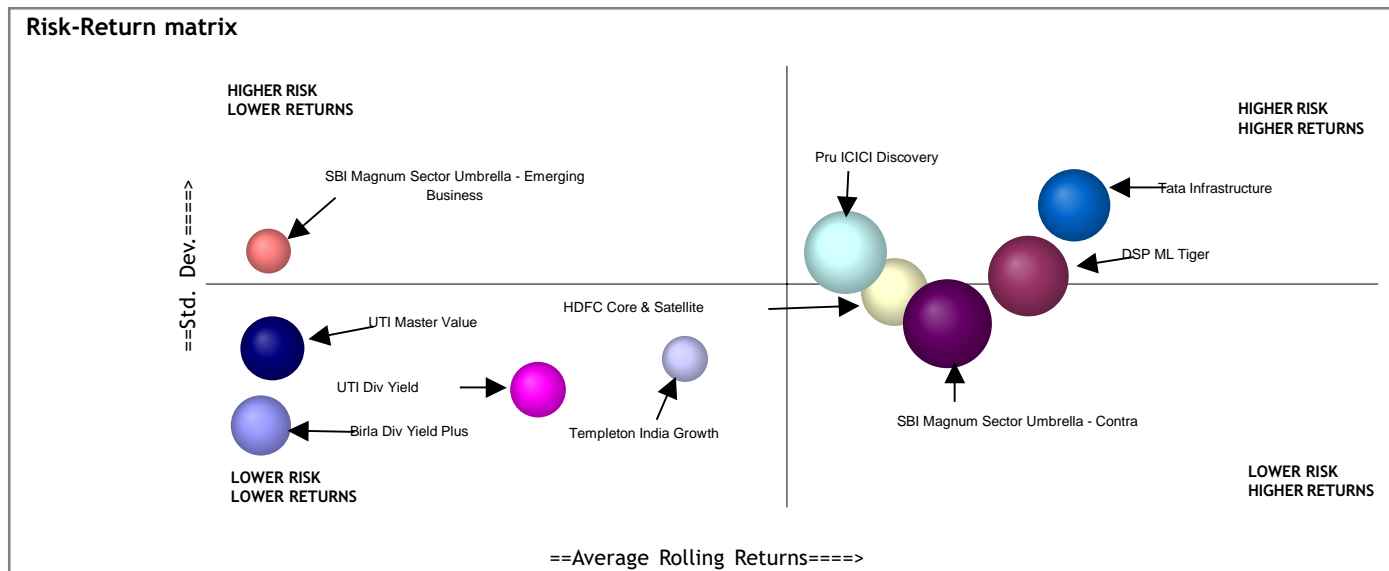
Aggressive Funds



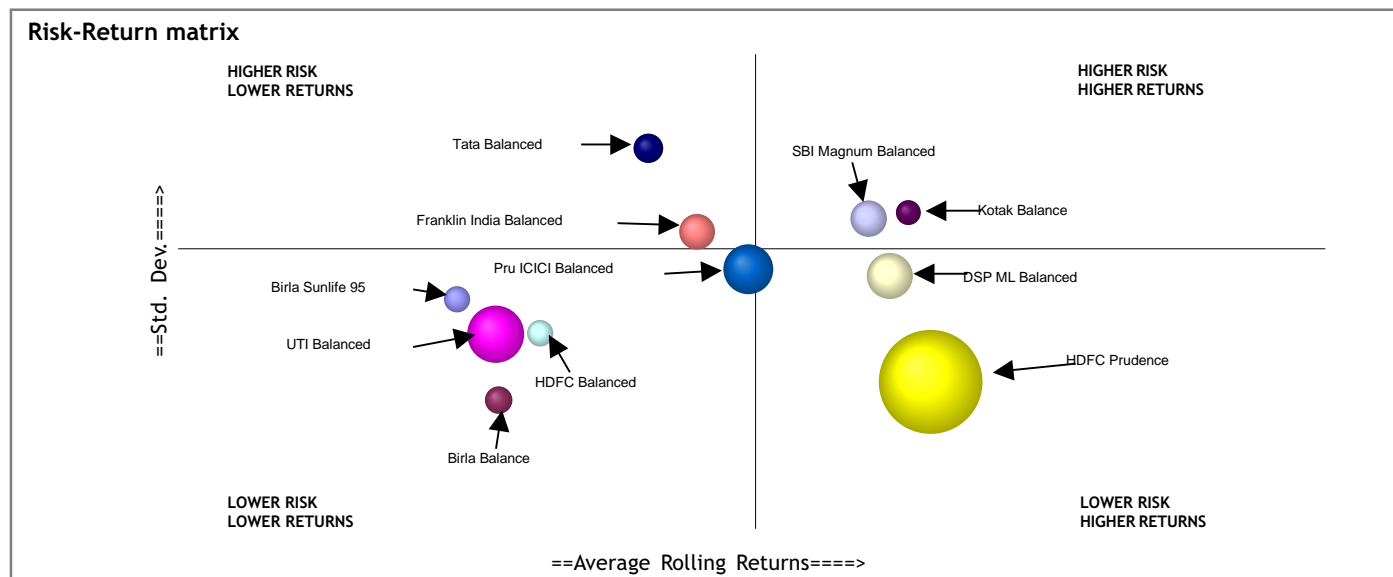
Equity Diversified/Conservative Funds



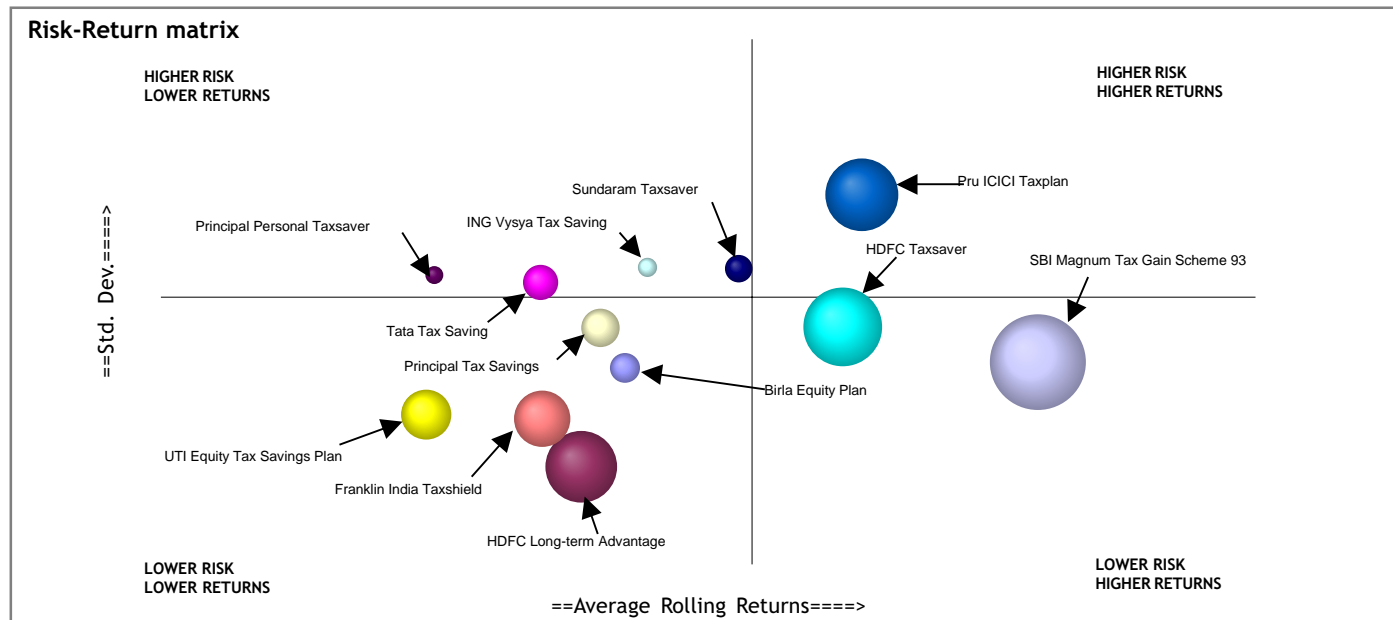
Thematic/Emerging Trend Funds



Balanced Funds



Tax Planning Funds



Disclaimer: mutual fund investments are subject to market risk. Please read the offer document carefully before investing. Past performance may or may not be sustained in the future.

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