investor's eye

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Take Five

Scrip	Reco Date	Reco Price	CMP	Target
BASF India	18-Sep-06	220	**240**	300
BEL	26-Sep-06	1,108	**1,155**	1,525
ICICI Bank	23-Dec-03	284	**695**	770
Orient Paper	30-Aug-05	214	**593**	800
UltraTech	10-Aug-05	384	**893**	1,000

Ahmednagar Forgings

Ugly Duckling

Stock Idea

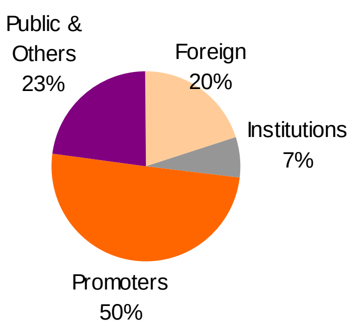
Forging ahead

Buy; CMP: Rs250

Company details

Price target:	Rs380
Market cap:	Rs830 cr
52 week high/low:	Rs265/122
NSE volume: (No of shares)	26,452
BSE code:	513335
NSE code:	AHMEDFORGE
Sharekhan code:	AHMDFORG
Free float: (No of shares)	1.7 cr

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	6.7	48.9	8.2	74.1
Relative to Sensex	2.9	26.0	0.2	17.9

Key points

- The business of Ahmednagar Forgings Ltd (AFL) is growing at a spectacular pace on the back of a buoyant domestic climate and bulging export orders. At present, the company has an order book of Rs850 crore, executable over the next twelve months. Of these, orders worth Rs650 crore are from the domestic market and the balance are export orders.
- To cater to this demand, AFL is more than trebling its forging capacity from 46,000 tonne per annum (tpa) in FY2006 to 165,000tpa by FY2008. The machining capacity is also being expanded from 10,000tpa to 25,000tpa.
- After the acquisition of Amforge's Chakan unit by Mahindra Automotive Steels, some of its original equipment manufacturer (OEM) customers have shifted to AFL. This is expected to generate additional revenues of Rs100 crore.
- AFL's export revenues should get a boost with the acquisition of the two forging lines from Anvil International. At peak levels these lines should generate revenues of Rs300 crore. AFL would also be meeting the outsourcing needs of GWK, UK, the Amtek group's global business.
- With increased contribution of the machined products and higher revenues from the non-automotive segment, we expect the margins to expand by 120 basis points over the next two years.
- At the current market price of Rs250, the stock discounts its FY2008E earnings by 6.5x. Considering the company's future growth potential and the stupendous increase in its size, we believe that such a discount to its peers is unjustified and recommend a Buy on the stock with a price target of Rs380.

Company background

Incorporated in 1976, AFL manufactures small and medium-sized forged components such as connecting rods, gear blanks, shafts, transmission components, flanges and hubs. Amtek Auto acquired a 50.17% stake in AFL in FY2002. AFL has three plants, one each at Ahmednagar, Chakan and Kuruli. AFL is a Tier-I supplier to large domestic OEMs like Tata Motors, Ashok Leyland, Eicher Motors, Force Motors, Bajaj Auto, HMSI Pvt Ltd and MUL.

Key financials

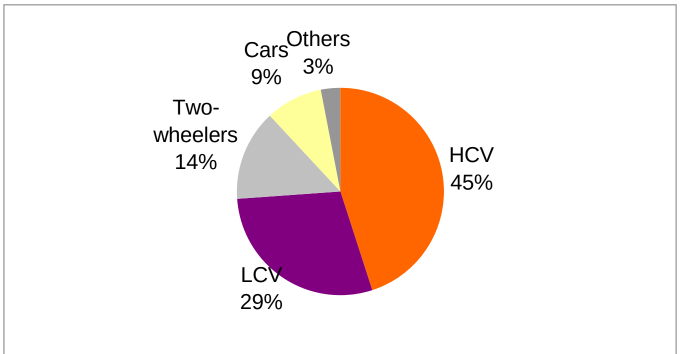
Particulars	FY2005	FY2006E	FY2007E	FY2008E
Net profit (Rs crore)	20.6	38.8	72.6	126.7
EPS (Rs)*	6.2	11.7	21.9	38.1
% y-o-y growth	*64.6*	*88.7*	*86.9*	*74.5*
PER (x)	40.3	21.4	11.4	6.6
P/B	2.6	3.2	2.5	1.8
EV/EBIDTA	-	11.1	6.2	3.6
RoCE (%)	31.0	25.3	29.8	38.6
RoNW (%)	27.2	14.8	21.9	28.0

*On fully diluted equity

AFL also supplies for non-automotive applications like locomotives, stationery engines and earth-moving equipment to players like L&T and BEML.

It currently has a forging capacity of 86,000tpa and plans to increase the same to 165,000tpa by FY2008. The current capacity, about 10,000tpa is for machined products and plans are afoot to raise this capacity to 25,000tpa. On the export front, AFL has been catering to the requirements of Cummins and Fairfield Atlas. It also exports to some of its group companies like GWK, UK and Zelter.

Revenue break-up



Source: Company and Sharekhan Research

Investment arguments

Strong growth in domestic CV and two-wheeler segments

The Indian automobile sector has witnessed a phenomenal growth in the last four years, led primarily by a booming economy, improving per capita income, easy availability of finance and increasing affordability of vehicles.

Going forward, we expect the good performance of the ancillary sector to continue for the following reasons.

- *Increasing capex of the domestic OEMs:* Automobile majors like Tata Motors, Maruti Udyog, Bajaj Auto, Ashok Leyland and Force Motors have lined up huge capital expenditure (capex) plans for the next two to three years. These investments should translate into high growth for the ancillary companies.

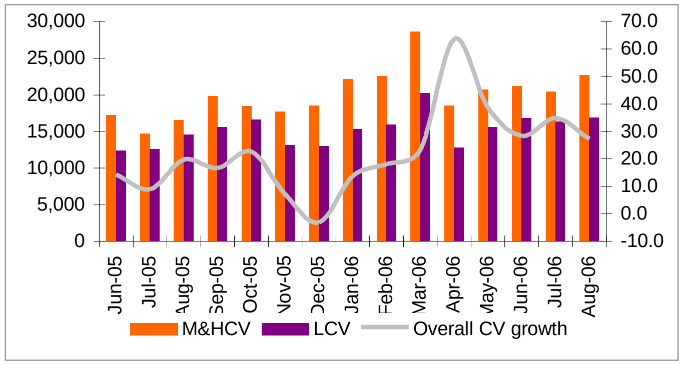
Capex plans of major OEMs

Company	Capex (Rs cr)	By
Tata Motors	12,000	2008
Maruti Udyog	9,000	2009
M&M	1,500	2008
Bajaj Auto	3,750	2010
Hero Honda	1,900	2010
Ashok Leyland	550	2008
Force Motors - Man	500	2008
HMSI	400	2008

Source: Sharekhan Research

- *Rising freight rates and overloading ban:* The rise in the freight rates and the Supreme Court's ban on the overloading of trucks have triggered a strong growth in the commercial vehicle (CV) segment. We have witnessed a brilliant growth in the CV sales in the current fiscal and the growth is likely to continue despite the higher base of the previous fiscal. Since the bulk of AFL's revenues accrue from the CV segment, the growth in the segment should lead to higher growth for the company.

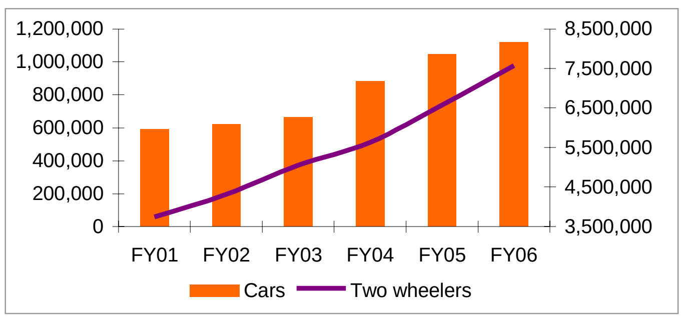
Buoyancy in the CV segment continues



Source: Sharekhan Research

- *New launches and increasing affordability:* In the passenger car segment, a slew of new launches planned in the coming two years, increasing affordability and reduction in excise duty will drive the growth.

Growth in the car and motorcycle segments



Source: Sharekhan Research

The high growth in the automobile industry should translate into a strong growth for the auto ancillary industry in India.

Being the largest manufacturer of small and medium-sized forging components in the domestic market, AFL would benefit the most from the strong demand from its main OEM clients like Bajaj Auto and Tata Motors. We estimate the domestic business of AFL to grow at a compounded annual growth rate of more than 40% over the next two to three years. At present, AFL has a very healthy order book of Rs850 crore, executable over the next twelve months. Of these, orders worth Rs600 crore are from the domestic market while the balance orders worth Rs250 crore are export orders.

The domestic business has got a boost with the acquisition of Amforge's Chakan unit by Mahindra Automotive Steels.

The OEM clients of this particular unit have shifted their orders to AFL. The company expects about Rs100 crore of revenues as a result of the shift.

Exports to grow at break-neck speed

Export of components promises to be a key growth driver for the Indian ancillary manufacturers. The Amtek group is expected to be one of the key beneficiaries of this opportunity. AFL currently exports to some of its customers in Europe and the USA, like John Deere, Cummins and Fairfield Atlas. The company also has huge outsourcing orders from GWK. GWK is a UK-based company, which was taken over by Amtek Auto in 2003. AFL would be catering to the bulk of GWK's outsourcing requirements. Overall, we expect the exports to rise to Rs250 crore by FY2008 from Rs45 crore in FY2006.

In FY2006, AFL acquired a forging line from Anvil International, part of Tyco International. Anvil International is the world's largest and most complete manufacturer of piping connections and support systems. The unit, previously located in Texas, is being shifted to Pune and the operations are slated to begin by December 2006. This line has the capability to generate sales of Rs300 crore at peak levels.

Capex plans to meet the incremental demand

In keeping with the huge demand prospects, the company is trebling its capacity. From 46,000tpa in FY2006 the company has increased its capacity to 86,000tpa currently It plans to further increase the capacity to 130,000tpa by December 2006. Another 35,000tpa would be added by June 2007, taking the total capacity to 165,000tpa. The company is also increasing its machining capacity from the current levels of 10,000tpa to 25,000tpa by next year.

The capex has been financed through the private placement of 9.22 million equity shares at Rs151 each to foreign institutional investors, corporate bodies and promoters on a preferential basis which mobilised Rs130 crore. The company would be incurring a capex of Rs50 crore in FY2007 and of Rs30 crore in FY2008. The same would be funded through internal accruals. After the placement, the company has a huge cash balance on its balance sheet; the same might also be used for new acquisitions and to fund the capacity expansions. The company maintains that there would be no further equity dilution going forward.

Better product mix and higher non-auto revenues to expand margins

At present, machined products contribute 10% of the sales. With the expansion of the machining facility, their contribution is expected to go up to 20% of sales by FY2008, leading to an expansion in the margins.

As mentioned earlier, apart from the automobile industry, the company's products are also used in other industries such as locomotives, earth moving equipment, railways, aeronautics and defence. The company plans to increase the contribution of the non-auto segment to its overall sales in the next two years. The Anvil International forging line caters to the non-automotive sectors like oil & gas. It has also bagged an order of Rs80 crore from GE Locomotives. The contribution from non-automotive products is likely to rise to 20-25% of sales from about 5-6% currently.

Since the margins in the non-auto segment are higher and the contribution of machined products to the overall product mix is expect to rise, we expect the EBIDTA margins to improve by about 120 basis points in the next two years. We expect the EBIDTA margin to rise from 19.5% currently to 20.7% by FY2008.

Tax benefits to aid PAT growth

The company is putting up a finishing plant in Baddi, which should render tax benefits to the company. The tax rate for the company is expected to be around 25%. The Amtek group as a whole follows a conservative debt policy and hence post-dilution the debt/equity ratio has come down considerably to about 0.3:1. We expect the ratio to come down further in the coming two years. Consequently, the interest cost would also remain low going forward.

Outlook and valuation

In view of the buoyancy in the domestic automobile industry, the company's huge outsourcing potential, the acquisition of two forging lines from Anvil International and the shifting of Amforge's clients to AFL, we believe AFL's business prospects are bright. The rising contribution of machined products and higher revenues from the non-auto segment should boost Its profit margins going forward.

Higher utilisation and margin expansion should help improve the return ratios in the next two years. The return on capital employed should rise from 25.3% in FY2006 to 38.6% by FY2008; the return on equity should improve from 14.8% to 28.0% in the same period.

Comparative valuations

	PER		EV/EBIDTA	
	FY2007	FY2008	FY2007	FY2008
Bharat Forge	21.8	17.0	10.8	8.8
RK Forgings	13.8	8.5	8.5	5.3
AFL	11.8	6.8	6.4	3.7

On the valuation front, the stock appears to be very cheap in comparison with its peers. At the current market price of Rs250, it discounts its FY2007E earnings by 11.4x and its FY2008E earnings by 6.5x. The valuations are at a considerable discount to that of some of its peers in the forging industry. Considering the growth potential of AFL, we believe that such a discount is unjustified and recommend a Buy on the stock with a price target of Rs380.

Financials

Profit and loss account

Rs (cr)

Particulars	FY05	FY06E	FY07E	FY08E
Net sales	**166.2**	**375.5**	**635.0**	**934.2**
Operating expenses	167.3	302.4	508.0	740.4
Operating profit	-1.0	73.1	127.1	193.8
Other income	39.2	0.0	0.0	0.0
EBIDTA	38.2	73.1	127.1	193.8
Depreciation	4.2	10.5	15.7	18.9
Interest	4.4	5.9	7.7	6.0
PBT	29.7	56.7	103.7	168.9
Tax	9.1	17.9	31.1	42.2
PAT	**20.6**	**38.8**	**72.6**	**126.7**

Balance sheet

Rs (cr)

Particulars	FY05	FY06E	FY07E	FY08E
Share capital	8.0	33.2	33.2	33.2
Reserves & surplus	67.8	229.9	298.8	419.8
Shareholders fund	75.8	263.2	332.0	453.0
Total debt	62.3	93.3	60.0	60.0
Total liabilities	**138.1**	**356.4**	**392.0**	**513.0**
Gross block	106.3	263.9	313.9	343.9
Net fixed assets	66.1	213.2	247.5	258.6
C/w in progress	37.1	0.0	0.0	0.0
Investments	1.6	1.6	1.6	1.6
Gross current assets	95.2	286.3	387.2	611.9
Gross current liabilities	63.2	146.1	245.7	360.4
Net current assets	32.0	140.2	141.6	251.5
Misc exp not w/o	1.3	1.3	1.3	1.3
Deffered tax liability	0.0	0.0	0.0	0.0
Total assets	**138.1**	**356.4**	**392.0**	**513.0**

Key ratios

Particulars	FY05	FY06E	FY07E	FY08E
OPMS (%)	-0.6	19.5	20.0	20.7
EBIDTA (%)	23.0	19.5	20.0	20.7
PAT (%)	12.4	10.3	11.4	13.6
RoCE (%)	31.0	25.3	29.8	38.6
RoNW (%)	27.2	14.8	21.9	28.0
Debt equity (X)	0.8	0.4	0.2	0.1

Valuations

Particulars	FY05	FY06E	FY07E	FY08E
EPS*	6.2	11.7	21.9	38.1
PER	40.3	21.4	11.4	6.6
P/B	2.6	3.2	2.5	1.8
EV/EBIDTA	-	11.1	6.2	3.6
EV/Sales	1.5	2.2	1.2	0.7
M cap/Sales	1.2	2.2	1.3	0.9

*On fully diluted equity

The author doesn't hold any investment in any of the companies mentioned in the article.

Shree Cement

Cannonball

Stock Update

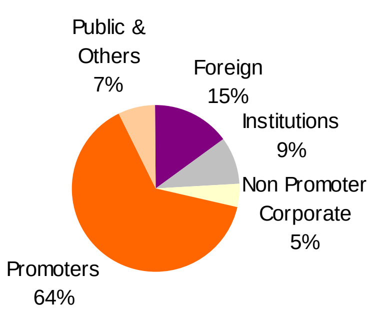
Superlative performance at operating level

Buy; CMP: Rs1,100

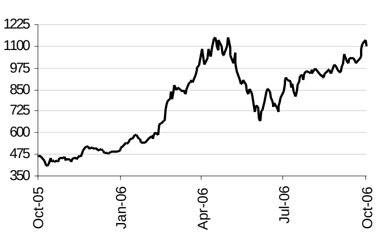
Company details

Price target:	Rs1,400
Market cap:	Rs3,832 cr
52 week high/low:	Rs1,189/352
NSE volume: (No of shares)	25,130
BSE code:	500387
NSE code:	SHREECEM
Sharekhan code:	SHREECEM
Free float: (No of shares)	1.3 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	17.9	32.1	16.3	145.7
Relative to Sensex	13.6	21.1	7.7	66.3

Result highlights

- On the operating front Shree Cement has reported a superlative performance. The operating profit jumped 173% to Rs142.66 crore as the operating profit margins (OPMs) expanded by 11.1% to 45.2%.
- Shree Cement's Q2FY2007 net profit increased by 108% at Rs78 crore, marginally below our expectation of Rs83 crore.
- The revenues for the quarter jumped by a whopping 103% to Rs315.95 crore. This was on the back of a 45.5% growth in the cement volumes and a 39.7% growth in the cement realisations. The volumes jumped as the company commissioned its new 1.5 million tonne plant during March 2006.
- Shree Cement has reported a very handsome Rs1,276 of earnings before interest, depreciation, tax and amortisation (EBIDTA) per tonne ie a growth of 88% year on year (yoy).
- On the cost front, the total cost increased by 15.4% largely because of a 20.7% increase in the power and fuel cost and a 22% increase in the raw material cost. Surprisingly the company's freight cost stayed absolutely flat as the company moved a higher proportion of its dispatches through the cost efficient railway transport.
- The depreciation charge increased by 176% to Rs33.8 crore on account of the new plant and the tax outgo for the quarter was Rs32.6 as against no tax in Q2FY2006 (last year the company had changed its depreciation policy on account of which it had some deferred tax benefits).

Result table Rs (cr)

Particulars	Q2FY07	Q2FY06	% yoy chg	H1FY07	H1FY06	% yoy chg
Net sales	**316.0**	**155.4**	**103.3**	**625.3**	**297.9**	**109.9**
Total expenditure	173.3	103.2	67.9	345.2	201.4	71.4
Operating profit	**142.7**	**52.2**	**173.4**	**280.2**	**96.5**	**190.4**
Other income	4.3	0.8	474.7	7.3	1.0	611.7
EBIDTA	147.0	52.9	177.7	287.5	97.5	194.9
Interest	2.7	3.3	-18.7	8.1	7.2	11.9
PBDT	144.3	49.6	190.8	279.4	90.3	209.5
Depreciation	33.8	12.3	175.8	60.1	24.5	145.0
PBT	**110.5**	**37.4**	**195.7**	**219.3**	**65.8**	**233.5**
Tax	32.6	0.0		51.1	2.4	2037.2
Profit after tax	**77.8**	**37.4**	**108.3**	**168.2**	**63.4**	**165.5**
EPS (Rs)	22.3	10.7				
Margins						
OPM (%)	45.2	31.1		44.8	34.1	
EBT (%)	35.0	19.9		35.1	23.8	
EAT (%)	24.6	18.2		26.9	23.2	
Tax rate (%)	29.5	8.4		23.3	2.6	

Even though Shree Cement's Q2FY2007 earnings are marginally lower than our expectation, we are not changing our full year estimates. Going forward, firm cement prices in the wake of the narrowing demand-supply scenario in the country in general and the northern region in particular would drive Shree Cement's cement realisations. This coupled with the continuous volume growth over the next two years would maintain the momentum in Shree Cement's earnings growth. At the current market price (CMP) of Rs1,100, the stock is trading at 10.5x its FY2008 earnings and 6.5x its FY2008 EBIDTA. On enterprise value (EV)/tonne basis the stock is trading at EV/tonne of USD147 per tonne of cement. On account of a sanguine outlook for the company, we maintain our Buy recommendation on the stock with a price target of Rs1,400.

New plant boosts volumes by 45.5%

Shree Cement commissioned its third unit with a capacity of 1.5 million tonne during March 2006. This boosted Shree Cement's Q2FY2007 cement volumes by a huge 45.5% yoy. This coupled with an almost 40% jump in the cement realisations to Rs2,825 per tonne of cement led to a whopping 103% jump in the top line to Rs315 crore. Buoyed by the improving cement realisations the company reported a very handsome EBITDA per tonne of Rs1,276, ie a growth of 88%. On the cost front, the total cost increased by 15.4% largely because of a 20.7% increase in the power and fuel cost and a 22% increase in the raw material cost. Surprisingly the company's freight cost stayed absolutely flat as Shree Cement moved a higher proportion of its dispatches through the cost efficient railway transport.

Per tonne analysis

Particulars	Q2FY07	Q2FY06	% yoy chg
Raw material	325	266	22.2
Stocks	7	-26	-126.6
Employee	105	98	7.5
Power and fuel	478	396	20.7
Freight	347	347	0.0
Other exp	287	262	9.8
Total cost per tonne	1549	1343	15.4
Realisation	2825	2022	39.7
EBIDTA	1276	679	87.9

Net profit up 108%

Shree Cement's net profit for Q2FY2007 increased by 108% yoy to Rs.77.8 crore. This is marginally below our expectations primarily because of a higher-than-expected tax rate. During FY2006, the company had changed its accounting policy (from WDV company law to WDV as per the Income Tax Act) and accordingly had provided a higher depreciation (extraordinary depreciation) to reconcile its depreciation charge on unit II as per the IT books. This had resulted in the company incurring a negligible tax outgo in FY2006. However this year the company could no longer avail of the benefits of extraordinary depreciation and as a result had paid almost full tax at the rate of 30%.

Capex on track—new 1.5 million capacity to become operational by April 2007

To achieve its target of becoming a 10-million-tonne cement producer, Shree Cement has charted out a big capital expenditure (capex) plan to set up unit V, which will have a clinker capacity of 1 million tonne and a split grinding facility of 2 million tonne, near Gurgaon. This is over and above the 1.5 million tonne Unit IV, which shall commence production by April 2007. Further the company plans to set up a captive power plant (CPP) of 36MW to cater to the requirements of units IV and V. The total capex on the units IV and V, the grinding unit and the 36MW CPP is Rs800 crore, which would be funded through a mix of debt and internal accruals. Shree Cement's capex plan is well on track and the company targets to produce 9 million tonne of cement in FY2009.

Valuation and view

Going forward, firm cement prices in the wake of the narrowing demand-supply scenario in the country in general and the northern region in particular would drive the company's cement realisations. This coupled with the continuous volume growth over the next two years would maintain the momentum in Shree Cement's earnings growth. At CMP of Rs1,100, the stock is trading at 10.5x its FY2008 earnings and 6.5x its FY2008 EBIDTA. On EV/tonne basis the stock is trading at EV/tonne of USD147 per tonne of cement. On account of a sanguine outlook for the company, we maintain our Buy recommendation on the stock with a price target of Rs1,400.

Earnings table

Particulars	FY2005	FY2006E	FY2007E	FY2008E
Net profit (Rs cr)	109.6	152.6	281.0	363.6
% y-o-y growth	*169.0*	*39.0*	*84.0*	*29.0*
Shares in issue (cr)	3.5	3.5	3.5	3.5
EPS (Rs)	31.5	43.8	80.6	104.4
% y-o-y growth	*169.0*	*39.0*	*84.0*	*29.0*
PER (x)	35.0	25.1	13.6	10.5
P/BV (Rs)	15.0	14.7	13.6	4.4
EV/EBIDTA (x)	23.9	18.3	9.0	6.5
RoCE (%)	21.2	26.5	38.0	36.2
RoNW (%)	45.3	51.5	50.1	40.2

The author doesn't hold any investment in any of the companies mentioned in the article.

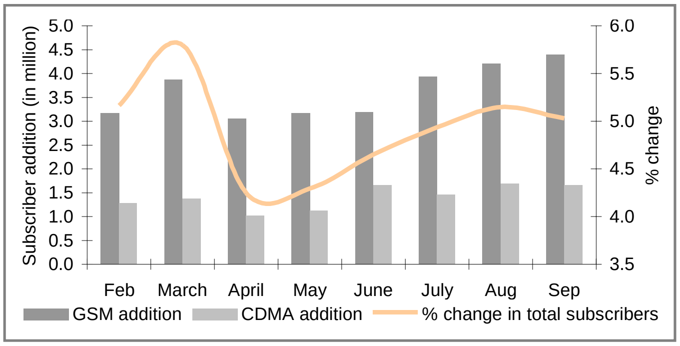
Telecom

Sector Update

India records the highest addition ever

On the back of falling tariff rates and lucrative offers, the Indian telecom service providers continue to shine. The industry added 6.1 million subscribers in September, taking the total subscriber base to 126.7 million. Both the GSM and CDMA industries witnessed a robust growth in subscriber add-ins during the month.

GSM and CDMA subscriber growth: positive trend continues



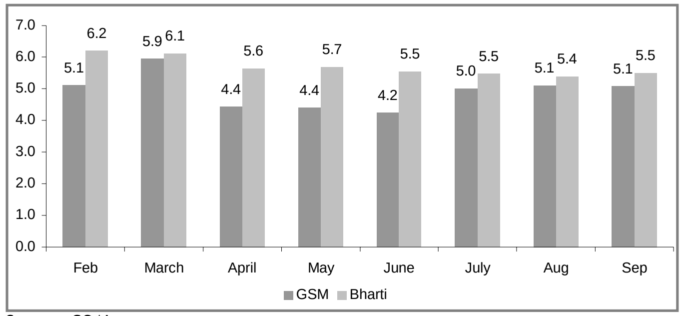
Source: COAI, AUSPI

For the month, the GSM industry reported a healthy growth of 5.1% in the subscriber base. It added a record 4.4 million new subscribers, taking its subscriber base to 91.0 million as of September 2006. Likewise, the CDMA players added 1.7 million users (marking a growth of 4.9%) for the month, taking the total user base to 35.6 million.

Bharti leading the pack...

Bharti Airtel continues to lead the GSM pack with the addition of 1.4 million subscribers. Its subscriber base grew by 5.5% month on month (mom). With a total of 27.1 million mobile users, Bharti has maintained its leadership position, commanding a 21.4% market share.

Subscriber growth (%): GSM & Bharti



Source: COAI

The state-owned Bharat Sanchar Nigam Ltd (BSNL) and Idea Cellular too reported strong numbers during the month. BSNL added 0.9 million users, which amounts to a growth of 4.3% mom. Likewise, Idea Cellular managed to post another good month with a growth of 6.5%, taking its user base to 10.4 million. Hutch added 1.0 million subscribers during the month, taking its total subscriber base to 20.4 million with a market share of 16.1%.

Reliance Communication added 1.2 million new users in September, recording a growth of 4.9% mom. It added 0.98 million subscribers (up 4.4% mom) in the CDMA segment and 0.22 million subscribers (up 8.1% mom) in the GSM segment. Its market share currently stands at 20.5%. On the other hand, Tata Tele-services added 0.7 million new users in September, recording a strong growth of 6.1% mom.

Mobile subscriber: September 2006 **In million**

	Sep-06	Aug-06	% chg	Additions	Market share (%)
Bharti	27.1	25.6	5.5	1.4	21.4
Reliance	26.0	24.8	4.9	1.2	20.5
BSNL	20.9	20.1	4.3	0.9	16.5
Hutch*	20.4	19.4	5.0	1.0	16.1
Idea	10.4	9.7	6.5	0.6	8.2
Tata Tele	12.4	11.7	6.1	0.7	9.8
Total	**126.7**	**120.6**	**5.1**	**6.1**	

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Mutual Gains

Mutual Fund

Sharekhan's top equity fund picks

After falling steeply in the beginning of the month, the Sensex has regained much of its lost ground with the domestic demand-driven story continuing and the foreign institutional investor (FII) sentiment improving. Thus despite the heavy selling in the beginning of the month, FIIs were net buyers of Indian equities for September as well with purchases worth Rs6,231 crore compared with that of Rs4,774 crore in August. Mutual funds (MFs), too have contributed to the sharp run-up in the Sensex by remaining aggressive buyers in the market. The strong inflows from FIIs and mutual funds have enabled the Sensex to pierce the 12k mark.

In the last quarter, the earnings of the Sensex companies had grown by a good 22.8%. A look at the corporate advance tax collections, which have grown by 30% indicate that the second quarter earnings will be equally good, if not better. The economic indicators vindicate the strength of the Indian economy and the earnings potential for Indian companies going forward. For instance, in July industrial production saw the strongest growth in the last ten years, with the Index of Industrial Production growing by a strong 12.4%. The growth was led by the manufacturing sector, which grew by an impressive 13.3%. The underlying capital expenditure theme too remains strong, as is evident from the 19% rise in the Index of Capital Goods in the year till date. Most importantly, India's growth story is reinforced by the gross domestic product (GDP) numbers that were released recently. Driven by the twin engines of manufacturing and service sectors, India's GDP grew by a strong 8.9% in the first quarter of this fiscal. The growth was the highest for the first quarter since 2000-01. The economy thus seems poised to grow at the rate of 7.5-8.0% this year as well.

Other than Indian Inc's second quarter results, the market will be influenced by global factors as well. Crude oil has fallen from a high of $78.4 per barrel in mid-July to $60 per barrel levels currently. Meanwhile, the US Federal Reserve (Fed) has kept the Fed rate unchanged at 5.25% in its last meeting, and is expected to maintain the status quo in its next meeting as well, on account of the slowdown in the US economy. However, signals emerging from the US economy continue to be mixed. While there are clear indications that the housing market and the manufacturing sector are slowing down, retail sales and consumer confidence remain visibly buoyant.

Considering everything, we believe that our stock market should be able to hold the attention of the foreign and local investors alike going forward. In the medium term, ie in the next two to three months, the market might react to volatility in crude prices and the fluctuations in the other global markets. In the near term, we expect a good run in the market triggered by India Inc's second quarter results, which are expected to be of good quality. The slide in the energy prices, the pause in the Fed rate hikes and strong foreign fund inflows should also boost the market sentiment in the near term. The long-term outlook looks extremely bright with the economy charging ahead at an unimaginably fast pace (9.3% in Q1CY2006 and 8.9% in Q2CY2006).

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 September 30, 2006 (%)				
		3 months	6 months	1 year	2 years	3 years
Sundaram Select Midcap	82.88	11.89	10.73	60.63	71.48	66.89
Birla Mid Cap Fund	58.02	21.69	3.66	36.02	53.17	52.56
Reliance Growth	234.80	17.68	3.23	34.84	62.87	63.16
Indices						
BSE Sensex	12454.42	17.39	10.15	44.39	49.43	40.89

Opportunities Category

Scheme Name	NAV	Returns as on September 30, 2006 (%)				
		3 months	6 months	1 year	2 years	3 years
Prudential ICICI Dynamic Plan	55.82	17.82	5.18	45.41	64.15	50.60
Kotak Opportunities Fund	25.49	12.71	0.11	42.10	58.43	--
Indices						
BSE Sensex	12454.42	17.39	10.15	44.39	49.43	40.89

Equity Diversified/Conservative Funds

Scheme Name	NAV	Returns as on September 30, 2006 (%)				
		3 months	6 months	1 year	2 years	3 years
SBI Magnum Global Fund 94	36.35	17.56	3.92	41.35	73.96	74.72
SBI Magnum Multiplier Plus 93	46.26	16.47	0.78	42.87	70.05	61.40
HDFC Equity Fund	133.81	17.56	5.32	43.94	56.50	50.99
Birla SunLife Equity Fund	158.44	21.29	2.80	35.49	59.37	56.33
DSP ML Equity Fund	39.94	16.48	3.26	37.10	58.32	52.01
Indices						
BSE Sensex	12454.42	17.39	10.15	44.39	49.43	40.89

Thematic/Emerging Trend Funds

Scheme Name	NAV	Returns as on September 30, 2006 (%)				
		3 months	6 months	1 year	2 years	3 years
Prudential ICICI Infrastructure Fund	16.19	25.12	9.91	51.06	--	--
SBI Magnum Sector Umbrella - Contra	33.43	15.32	5.72	45.24	74.24	73.99
DSP ML Tiger Fund	28.26	19.29	4.09	45.44	58.52	--
Tata Infrastructure Fund	20.74	17.27	4.14	48.06	--	--
HDFC Core & Satellite Fund	23.68	13.85	0.17	37.94	52.58	--
Indices						
BSE Sensex	12454.42	17.39	10.15	44.39	49.43	40.89

Balanced Funds

Scheme Name	NAV	Returns as on Septembr 30, 2006 (%)				
		3 months	6 months	1 year	2 years	3 years
HDFC Prudence Fund	103.20	15.85	8.53	32.39	44.56	40.04
JM Balanced	21.08	11.65	6.04	36.29	35.92	28.89
DSP ML Balanced Fund	35.20	11.99	3.44	31.10	35.00	34.71
Kotak Balance	22.00	7.43	-0.90	30.48	43.22	38.93
SBI Magnum Balanced Fund	31.87	10.78	1.66	29.80	48.18	46.64
Indices						
BSE Sensex	12454.42	17.39	10.15	44.39	49.43	40.89

Tax Planning Funds

Scheme Name	NAV	Returns as on September 30, 2006 (%)				
		3 months	6 months	1 year	2 years	3 years
SBI Magnum Tax Gain Scheme 93	47.26	16.38	3.80	33.80	80.63	79.12
HDFC Taxsaver	131.68	14.31	1.85	32.69	63.49	62.51
Prudential ICICI Taxplan	90.19	23.35	4.63	30.60	64.36	57.53
Birla Equity Plan	52.87	21.09	3.34	37.66	54.63	51.10
ING Vysya Tax Saving Fund	23.39	20.50	-2.09	29.46	54.43	--
Indices						
BSE Sensex	12454.42	17.39	10.15	44.39	49.43	40.89

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.

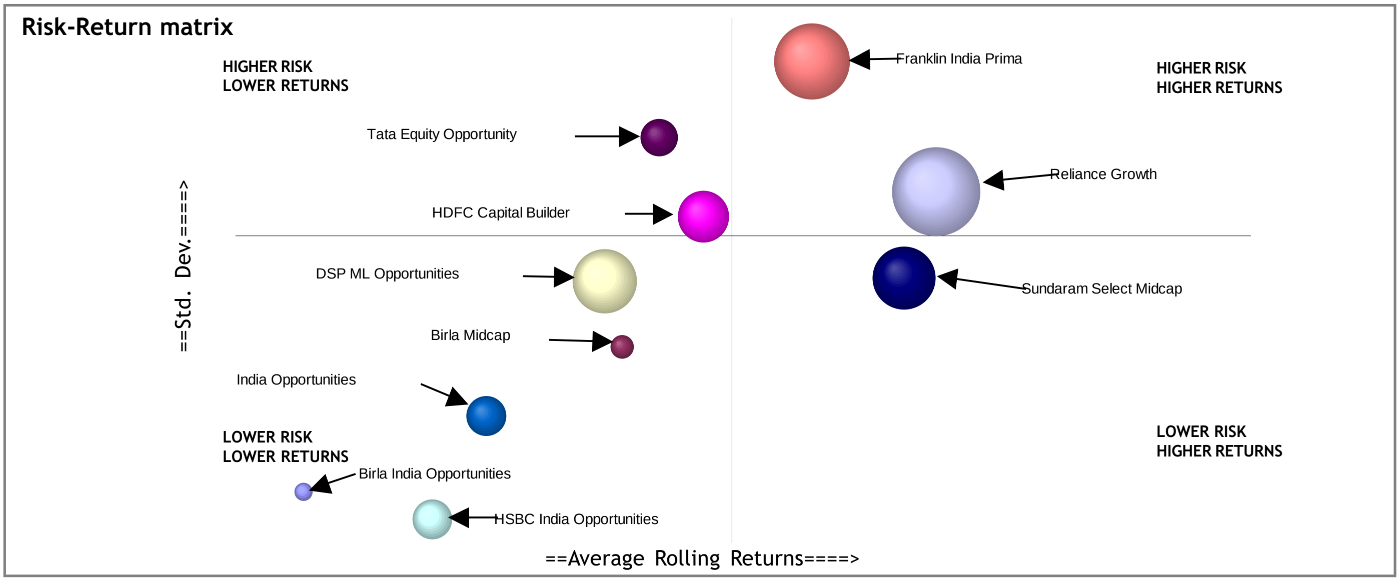
The funds in the **low-risk high returns** quadrant outperform the peer group on the risk-adjusted returns basis as they deliver higher returns compared to the peers without exposing the portfolio to very high risk.

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

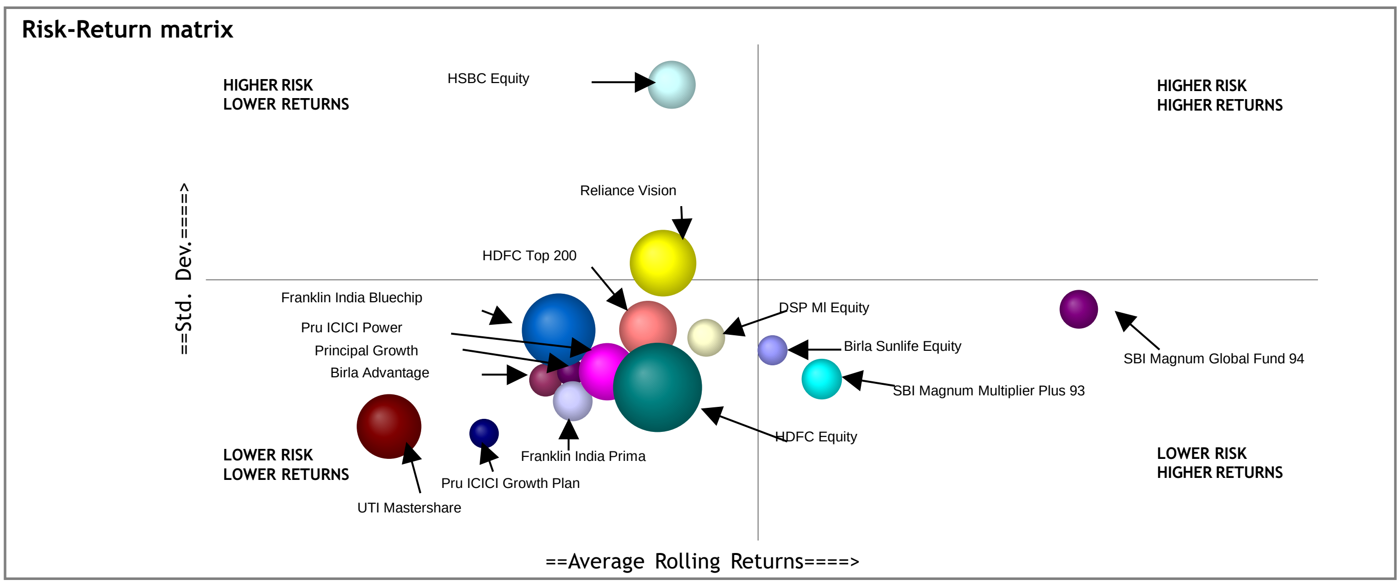
The funds in the **high-risk low returns** quadrant underperform the peers on the risk adjusted returns basis as they adopt a high-risk strategy but the returns fail to compensate the risk taken by the fund.

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 September 30, 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 September 30, 2006.

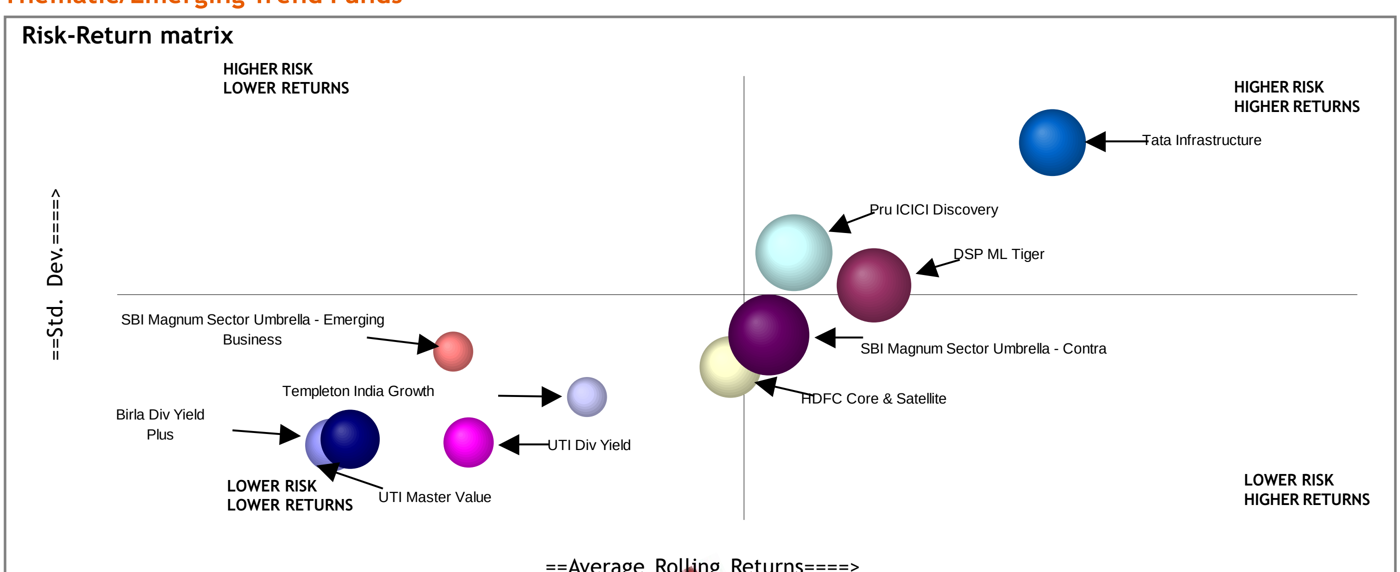
Aggressive Funds



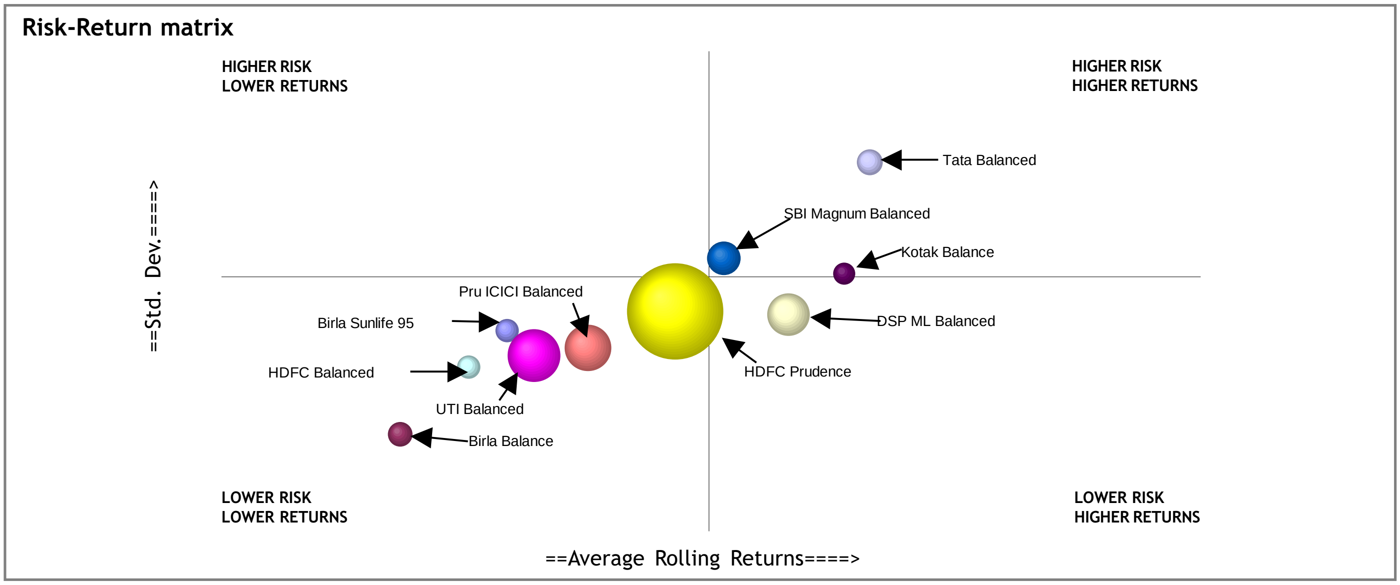
Equity Diversified/Conservative Funds



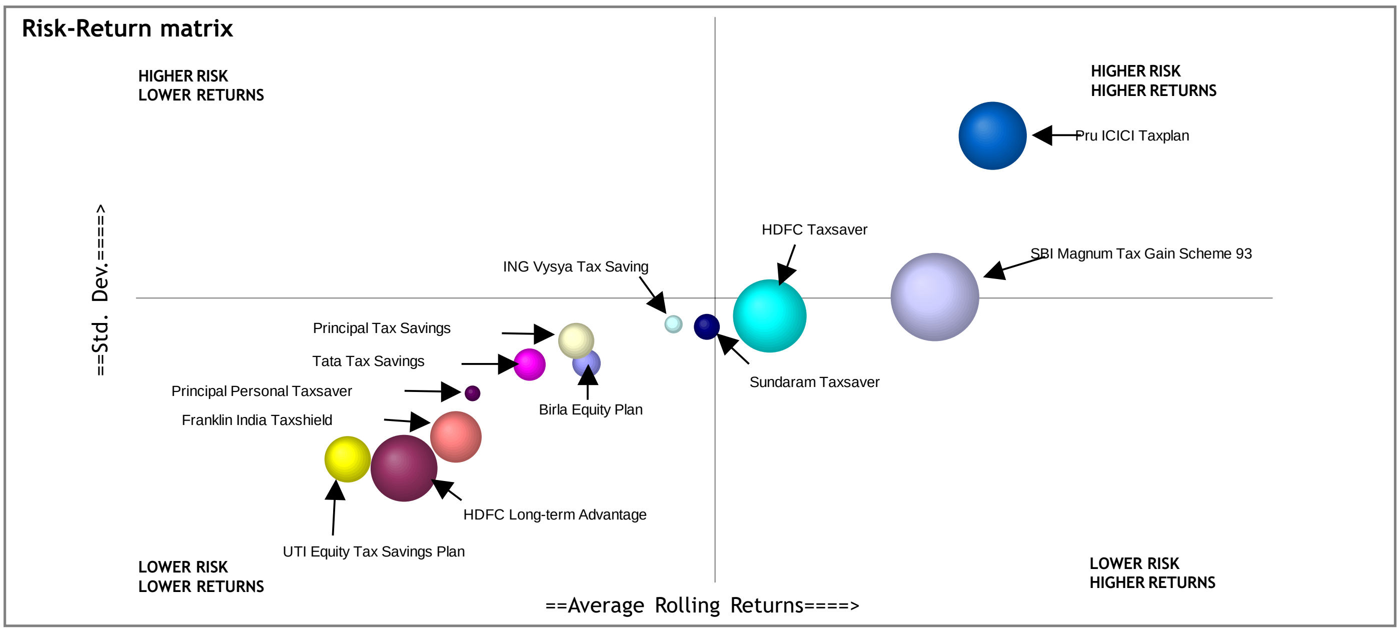
Thematic/Emerging Trend Funds



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.

Sharekhan Stock Ideas

Evergreen

HDFC Bank
Infosys Technologies
Reliance Industries
Tata Consultancy Services

Apple Green

Aditya Birla Nuvo
Associated Cement Companies
Bajaj Auto
Balrampur Chini Mills
Bank of Baroda
Bank of India
Bharat Bijlee
Bharat Electronics
Bharat Heavy Electricals
Canara Bank
Corporation Bank
Crompton Greaves
Elder Pharmaceuticals
Godrej Consumer Products
Grasim Industries
Hindustan Lever
Hyderabad Industries
ICICI Bank
Indian Hotels Company
ITC
Mahindra & Mahindra
Marico Industries
Maruti Udyog
Lupin
Nicholas Piramal India
Omax Auto
Ranbaxy Laboratories
Satyam Computer Services
SKF India
State Bank of India
Sundaram Clayton
Tata Motors
Tata Tea
Unichem Laboratories
Wipro

Cannonball

Allahabad Bank
Andhra Bank
Cipla
Gateway Distriparks
International Combustion (India)
JK Cement
Madras Cement
Shree Cement
Transport Corporation of India

Emerging Star

3i Infotech
Aban Offshore
Cadila Healthcare
KSB Pumps
Marksans Pharma
Navneet Publications (India)
New Delhi Television
Orchid Chemicals & Pharmaceuticals
ORG Informatics
Solectron Centum Electronics
Television Eighteen India
Thermax
TVS Motor Company
UTI Bank
Welspun Gujarat Stahl Rohren

Ugly Duckling

Ahmednagar Forgings
Ashok Leyland
BASF India
Deepak Fertilisers & Petrochemicals Corporation
Genus Overseas Electronics
HCL Technologies
ICI India
India Cements
Jaiprakash Associates
JM Financial
KEI Industries
NIIT Technologies
Punjab National Bank
Ratnamani Metals and Tubes
Sanghvi Movers
Saregama India
Selan Exploration Technology
Subros
Sun Pharmaceutical Industries
Surya Pharmaceuticals
UltraTech Cement
Union Bank of India
Universal Cables
Wockhardt

Vulture's Pick

Esab India
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