The Return Of The Small Stock

They grow fast and often provide multi-bagger returns for investors. Here's how to profit from them. By Kapil Bajaj

If you follow smart money and chase growth, now is a good time to go for bargain hunting in the small- and mid-cap stocks. Big companies are acquiring global scale, but it's the small companies that are playing a stellar role in the economy and where the true growth story is. They (the small companies) straddle a wide variety of growing and sometimes niche business that big companies usually don't get into. And these businesses are extremely profitable.

While the BSE Sensex companies recorded a solid revenue growth of 34 per cent in 2006-07 over the previous financial year, the growth in profits in the same period was 36 per cent. Profits were higher at 42 per cent in the companies that constitute the BSE's Mid-cap Index, despite a lower revenue growth of 22 per cent. But the biggest growth, by far, came in the BSE's small-cap companies that saw revenues increase by just 16 per cent, but profits zoom by an astounding 381 per cent. Little wonder then, the BSE's small- and mid-cap indices have been outperforming the dominant Sensex stocks since the beginning of this year (see Smaller Stocks Shining).

The Right Option

A Realty Check

Cut The Card Debt

News Round-up

Now, smart money too is chasing these stocks. Mutual funds are increasingly launching new funds that are targeted purely at the small- and mid-cap space. ICICI Prudential, Reliance, Franklin, and HDFC have launched small- and mid-cap funds and are expected to invest about Rs 3,500-4,000 crore in these stocks. The flows will keep interest alive in this segment. Brokers, too, have begun to get bullish about the sector-and with good reason. Rajen Shah, Chief Investment Officer, Angel Broking, says he is "extremely bullish" on small- and mid-caps because there are dozens of such stocks that have been 'under-owned' and have underperformed the market despite great potential.

The Time Has Come

For a long time, the markets focussed on large companies. Foreign institutional investors were investing in big companies because they could buy and sell large quantities of these stocks without disrupting the daily trading. As a result, small companies underperformed the markets. "Since October 2005, the BSE Sensex moved from a level of about 7,500 to around 14,500, but these smaller stocks have barely grown by 5-10 per cent. Many currently trade at P-E multiples of only 7-10, represent fast growing businesses, and are also attractively priced. In the next few months, there's about 20-30 per cent upside to their valuations,"

On Attractive Grounds

» Small- and mid-cap companies have outperformed the Sensex since January

» Fund houses are launching funds, increasingly targeting this segment

» Foreign investors and high networth individuals are increasingly buying smaller stocks

» Companies with the ability to scale up will get higher valuations

» Many good and growing businesses are available at attractive prices

» Selectively build a portfolio with growth stocks and monitor it periodically says Shah.

Among his favourites are Ballarpur Industries, Coromandel Fertilisers, Atlas Cycles Haryana, Finolex Industries and VST Tillers. Some small-caps are in booming segments and also own undervalued assets. Bangalore-based farm equipment company VST Tillers, for example, has a market cap of about Rs 80 crore (in early June), but its land holding in Bangalore alone is worth Rs 160 crore, notes Shah. The company, which posted a net profit of Rs 3.6 crore on gross sales of Rs 40.73 crore in Q3 of 2006-07, is also expected to gain from the government's increased investment in the farm sector.

"Small- or mid-sized companies are the ones that represent great investment opportunity"
Ajay Parmar
Head (Research), Emkay Share and Stock Brokers

HIS FAVOURITES
AIA Engineering, Elecon Engineering, Everest Kanto, Garware Offshore and Great Offshore

"The value driver of a stock is its business scalability. This requires a lot of commitment from the company"
Rajat Rajgarhia
Head (Research), Motilal Oswal Securities

HIS FAVOURITES
Ashapura Minechem, Dena Bank, Sasken Comm. Technologies, Shasun Chemicals & Drugs, and Shriram Transport

"You must do your homework in picking the stocks with strong fundamentals. Accurate stock selection is very important"
D.D. Sharma
Senior VP (Research), Anand Rathi Securities

HIS FAVOURITES
BOC, Hind Dorr Oliver, India Glycols, Jupiter Bioscience and Tayo Rolls

"Poor liquidity of smaller stock has been a concern, particularly among institutional investors, who for that reason prefer large-cap stocks"
Pranav Parekh
Analyst, Edelweiss Securities

HIS FAVOURITES
Chambal Fertilisers, Greenply Industries, Indo Asian Fusegear,

Oriental Hotels and Sirpur Paper Mills

"If the stock is good, money has to chase it. Liquidity takes care of itself"
Rajen Shah
Chief Investment Officer, Angel Broking

HIS FAVOURITES
Atlas Cycles, Ballarpur Industries, Coromandel Fertilisers, Escorts and Finolex Industries

Shah's investment principles are based on under-owned companies, compelling p-e multiples (in the range of 7-11), a good management, and significantly underperforming stocks. Others in the market concur with his views. Says Rajat Rajgarhia, Head (Research), Motilal Oswal Securities: "With robust growth in the economy, there are many companies that have made large investments in their businesses. Their business models are also sound and scalable. These companies can offer very good return on the stock market." The valuations of many of these companies are already increasing. Rajgarhia prefers stocks such as Shriram Transport, Dena Bank, Sasken Communication Technologies and Ashapura Minechem. He looks in a stock for a sound business model, its scalability, management's vision, expected earnings, and a reasonable price.

There are many small companies in it, auto, pharma and the entertainment industries with good potential to grow. Says Ajay Parmar, Head (Research), Emkay Share and Stock Brokers: "Today, money is not a problem for talent and enterprise in India. Many pharma companies in India, for example, are still small- or mid-sized companies, but have excellent managements and growing businesses. Companies of this kind are the ones that represent great investment opportunity." He also looks for a unique business model where the companies have a profitable niche. His picks include AIA Engineering, Everest Kanto, Nucleus Software Exports, Panacea Biotech and NIIT Technologies.

Select Stocks Only

Sometimes the going may get tough in the middle. Smaller stocks could be volatile over the short-to-middle term. In a market downturn, they tend to get battered more than the large-cap stocks. Their returns also may be poor over small-to-medium-term because of low liquidity. So, a time horizon of less than three years could prove to be disastrous. Says D.D. Sharma, Senior Vice President (Research), Anand Rathi Securities: "Mid-cap stocks tend to offer good returns in the time horizon of at least 3-5 years. So, you have to be patient." Sharma, too, is bullish on the segment with a long view; some of his great investments include Elecon Engineering, Moser Baer, and Balaji Telefilms.

Price Matters

If you invest during peaks and things don't go as expected, you may end up losing money; so have a careful look at the entry price. "Poor liquidity (tradability) of smaller stocks has been a concern, particularly among institutional investors, who for that reason prefer large-cap stocks. But things are already changing," says Pranav Parekh, Analyst, Edelweiss Securities, who likes Sirpur Paper Mills, Chambal Fertilisers, Oriental Hotels, and Indo Asian Fusegear, among others. "Of late, institutional investors are increasingly showing interest in these stocks, some of which can give pretty good returns," he adds. Shah says mutual funds and FIIs are already "rediscovering" small- and mid-cap stocks, infusing money into them and boosting their valuations and liquidity. That's good news for the retail investors who worry that their investments in smaller stocks risk poor liquidity. "The next six months will see unlocking of a lot of value in these stocks. If the stock is good, money has to chase it. Liquidity takes care of itself," adds Shah.

It's not that the entire small- and mid-cap space will do well. So, investors need to tread carefully. Many companies in this segment are family-run businesses that tend

Next up: Micro-caps

They have market capitalisations of less than Rs 1,500 crore, according to the recently concluded DSP Merrill Lynch Mutual Fund's Micro-cap Fund. "Within this criteria (of micro-cap), we will focus on those companies that have had a consistent record of net profit and have shown a tendency towards going after good quality management," says Soumendranath Lahiri, Senior VP & Co-head (Equities), DSP Merrill Lynch Mutual Fund. "The businesses of these companies should obviously be scalable and show a strong possibility of getting re-rated."

Companies, whose net profits have consistently grown by over 30 per cent, stand a good chance of getting re-rated. However, micro-cap companies are typically ones that are open to higher risks as compared to mid- or large-cap companies. Says Lahiri: "Largely, micro-cap companies are promoter-driven and have shown erratic growth. The risk associated with this segment is greater. There are chances that some of these companies may fail to make the transition."

Micro-caps are likely to be a big area of activity, believes Lahiri, and companies within this category will also offer the opportunity for multi-fold increase in investments. Large-cap companies (market cap over Rs 5,500 crore) have seen a net profit growth of only 20 per cent on average. Mid-caps (market cap of up to Rs 2,500 crore) have seen an average net profit growth of 25 per cent, while the small- and micro-caps are likely to witness a profit growth in excess of 30 per cent, feels Lahiri.
-Shamni Pande

to compromise on corporate governance and disclosures. "Don't think that the entire mid-cap segment is worth investing; you must do your homework in picking the stocks with strong fundamentals. Accurate stock selection becomes more important in a well-priced market like we have currently," says Sharma. There are also risks in scaling up a business. Only those companies that can add capacities and expand their businesses deliver handsome shareholder returns. "The value driver of a stock is its business scalability. This requires a lot of commitment on the part of the company, which is not easy to assess," says Rajgarhia.

Don't just invest in a stock here or there. The key is to get a decent mix in your portfolio. "Start with the right sector and drill down to good-quality companies with competent management. Have a portfolio of at least 10 stocks, not just 2-3. It's the whole basket that will give you returns. Two-three stocks could become multi-baggers, 3-4 could go up modestly, and the rest could just fail," says Sharma. Parekh, on the other hand, advises a bottom-up approach to building a portfolio, starting from the right company rather than the right sector. "There can't be any hard and fast rules in picking the stocks. You could start with a fast growing sector of the industry. Or you could treat an individual stock on its own merit," says Rajgarhia.

"In building my portfolio, I won't allot more than 10 per cent to any one industry and more than 7 per cent to any one company," says Shah. With the broader markets meandering, now's the time to accumulate smaller stocks at lower prices. They are well poised to pay back.

The Right Option
As markets zoom higher, volatility increases and so does risk. But options offer a hedge against risk.

By Nitya Varadarajan

Worried about stock market volatility? Concerned that a downturn in the stock market will wipe out your gains? Well, worry not. A simple hedging strategy in the stock market could save you lots of money. Despite the seemingly rocket science-like appellation, options are a lot easier to understand and use than rocket science itself. And thanks to the rapid use of them, investors can protect their portfolio for a fraction of the cost. Of late, the volumes in the futures and options segment have increased to more than three times the turnover of the regular cash market. For regular long-term investors, a continuous use of options purely for hedging could become an expensive affair. Yet, once in a while, when market forces are aligned on the downside, these can turn into handy hedging tools. Here's a primer on options.

What's Your Option?
A primer on the world of options.

Call option: A contract that gives the investor the right (but not the obligation) to buy a stock or index at a specified price within a specific time period

Put option: A contract that gives the investor the right (but not the obligation) to sell a specified amount of a stock or index or an underlying security at a specified price within a specified time. This is the opposite of a call option

European option: This is an option that can be exercised only at maturity. You must ride the volatility of the market. All the index options trading in India are European options

American option: This one can be exercised anytime during its tenure. All company-specific stock options trading in the country are American options

Strike price: It is the price of the option fixed by the exchange for a specific underlying asset such as Nifty. It could be higher, lower or equal to the spot market price of the same. Typically, there are many options with different strike prices

Premium: It's the price at which the underlying option is traded in the market

The Option Advantage
How do options help?

» Options have slightly low risk, as the outcome is pre-determined
» Help in effective trade management as they discipline trading due to expiry
» The option prices have a low initial cash outflow
» They also help harness the power of leverage and get more exposure for less
» When can you use it?
» If you want to speculate with low risk
» To manage portfolios effectively
» When you want downside protection

What are Options?

But before you go on to hedge that risk, what really are options? True to its term, stock market options essentially give you an option to buy or sell a stock or index like Nifty at a pre-determined price. You don't have to compulsorily buy or sell. In stock market lingo, you are not obligated to buy or sell. You can back out of the deal at expiry. Since all option contracts have to be settled at one time, they have a pre-determined expiry date. In Indian markets, there are one-, two-, and three-month expiries on options. Not all of them are liquid, though.

Options expiring earlier are traded more frequently than ones of longer duration. Besides, index options, which are derivatives of indices such as Nifty, are more liquid than individual stock options, which are essentially derivatives of individual stocks. For investors, hedging with options provides an alternative solution to otherwise liquidating a portfolio. Says P.L. Lakshmanan, Proprietor, Prognosis Consultancy Services, a boutique stock broking firm: "For the retail investor, options are better as they cater to a variety of requirements."

What is Strike Price?

But what one must remember is the strike price. A strike price is fixed by the exchange for the underlying asset of the option which could be higher, lower or equal to the spot market price of the same. These would be favourable to the buyer (in the money) if the current market price is higher than the strike price; not favourable to the buyer (out of money) if it's lower, or neutral (at the money) at the same level.

Who is Writer?

If you have to buy, say, a call option, someone has to sell it. These sellers are called option writers. This is a very risky exercise and usually high networth or financial institutions use this tool as it can lead to unlimited losses. Option trading is possible between the 'writer' of the option or the seller and the 'buyer' of the option. Premium is paid by the buyer to the 'writer' or seller.

What is a Call Option?

There are two types of options: call and put options. In the former, the buyer has the right but not obligation "to buy" an agreed quantity of shares from the seller before the expiry date at the strike price for a premium that is market driven. Should the buyer decide later, the writer or the seller is obligated to sell. Buyers make money if the stock price increases more than the premium paid. On the other hand, if the spot price falls below the strike price, the buyer of the option will not be bound to exercise the option, but he forfeits the premium. Calls are bought when the underlying index or stocks are expected to go up.

What is a Put Option?

On the flip side, in a put option a buyer expects the stock market to go down. Here, the buyer is given the right (by paying up a premium) but not the obligation to sell the option on or before expiry date. The writer is obligated in "buying back" that option at the strike price if the buyer chooses to exercise his option. In this case, the buyer benefits if there is a substantial drop in spot price of the asset against the strike price. So when he is exercising his option, he buys the stock at a lower price in the spot market after factoring his premium, and sells it at the 'contracted strike rate' to the writer, pocketing the profit.

"People with idle assets, who have no intentions of selling the same, could write an out-of-money call option"

Amitabh Chakraborty

President (Equities)/ Religare Securities

How do Writers Profit?

There are various ways in which a seller or writer can profit. If he expects the price of an asset to fall, he could place a "call" option. He gets a premium and gets to cushion his asset at the strike price. The premium which is paid upfront is his profit, provided the market does not move upwards and the price crosses the premium paid over and above the strike price. After this point, the seller makes a loss, which could be unlimited. Some high networth individuals try and profit from this if they have idle assets by writing or selling calls with a strike-price that is way above that of the market. "People with idle assets, who have no intentions of selling the same, but desirous of generating some returns out of them, could write an out-of-money call option," says Amitabh Chakraborty, President (Equities), Religare Securities.

When is a put option Profitable?

» Puts are profitable when the current market price falls below the strike price
» You break-even when you recover your premium from the fall in current market price
» You lose the premium when the current market price is higher than the strike price
» Loss is restricted to the premium paid

When is a Call option profitable?

» A call bought by you makes money when the current market price goes above the strike price
» The current market has to go above your premium paid for you to break-even
» You lose premium when the current market price is lower than the strike price
» Loss is restricted to the premium paid

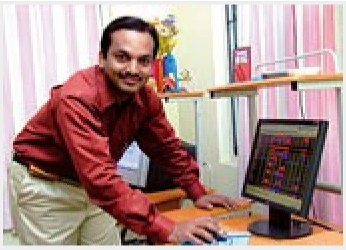
The Hedge Strategy
How to hedge with Put options.

» When you buy a Put option, you get downside protection for a premium
» If the market falls, the Put option becomes profitable
» But if the market rises, you will lose the premium
» Regular hedging is a costly affair and negates the gains made on the portfolio
» Usually, most pros hedge only a part of their portfolios when there's extreme volatility
» Buy Puts judiciously by looking at the premiums and how much it will cost you

If the writer expects the asset price to go up, he could place a 'put' option. If the price indeed goes up, he has his premium, and the buyer is unlikely to exercise that option. However, if the price goes down, and the buyer exercises his option, the writer's loss is to the extent the price has gone down, which could be substantial, wiping out the premium cushion, and more. He has to make good the difference between spot price and strike price to the buyer. Usually, writing options is very risky, as mentioned earlier, and is best left to the financial institutions or high networth individuals.

How to Gain?

On the other hand, if you expect the market to go up from the current levels, a simple strategy is to buy a call option. In case the market falls, at worst you lose the premium. But one gains if the market rises over and above the premium paid.



"For the retail investor, options are better as they cater to a variety of requirements"
P.L. Lakshmanan
Proprietor/ Prognosis Consultancy Services

How to Hedge?

Retail investors can, however, protect their assets with a simple strategy. They can buy put options and cover the risk of the falling market. Simply put, when one buys a put option, one locks-in the portfolio at the current market. If the market falls, there's no loss on the side of the buyer. Usually, hedges such as this tend to be more costly in a falling market, but in a rising market, the cost of a put option tends to be cheaper. Of course, options have their risks, and it will cost you the premiums. So if you hedge all the time, you continue to lose premiums. But when the downturn comes, you will have saved yourself a bundle.

A Realty Check
Real estate stocks have soared to sky-high levels. But with growth staggering, it's time for a reality check.

By Krishna Gopalan

If there is any sector in the news for a while now, it's real estate. Sustained demand for housing coupled with large-scale development from IT/ITEs, hotels and business parks has fuelled the appetite for growth in real estate. That could just be one side of the story. With the slew of SEZ projects certain to generate massive demand for large tracts of land, the sector is headed just one way: forward.

Much of the hoopla surrounding the sector in recent times has been due to the initial public offering (IPO) of DLF, which was due to open on the day BT went to press. This largest ever issue could mop up a record Rs 9,625 crore at the higher end of the price band (Rs 500-550 is the price band). Not surprisingly, the issue generated a great deal of media buzz. And millions of eyes are tracking its progress.

That apart, real estate, so far, has not had a fair representation in the market. The sector-where annual transactions are estimated at about $12 billion-is now set to have a bigger say with the DLF listing; the company is worth Rs 93,720 crore at the higher end of the price band. "The sector is underrepresented at the stock markets and there is, therefore, a need for large listings," points out First Global's Director Shankar Sharma. He cites the case of a place like Greater Noida where land prices remained almost unchanged for around a decade before the movement upwards started. "In that sense, it is the catch-up effect that is prevailing in the sector," adds Sharma.

On Diverse Grounds

This industry's business models are diverse. Pure-play companies like DLF form one end of the spectrum and quasi-real estate companies like IVRCL form another. "A third category includes companies like Bata, which has large tracts of land, though real estate may not be their primary business," says P. Phani Sekhar, analyst, Angel Broking. Companies, in the latter category, acquired land at low prices a long time ago, and the upside on that at current levels is, therefore, huge. High EBITDA margins have been prevailing for sometime due to rising property prices and increasing sales.

Yet there are a few looming threats and the rising interest rate is high among them. A recent First Global's report states: "Hardening interest rates will put further pressure on the pat (profit after tax) margin since real estate developers carry enormous debts on their books." The rising interest rates, it adds, will impact the affordability of housing loans. Highly leveraged companies will face additional payouts on account of interest obligations.

Behind the Realty Boom

» Real estate stocks have soared on the back of rising land bank prices
» Better profit margins for companies that have got land on the cheap
» Real estate companies are also diversifying into hotels and SEZs
» Current valuations factor in future projects and current land banks

Besides, First Global's Sharma points out that the hardening interest rates and rising prices in overheated markets coupled with an oversupply situation in some areas could lead to an inevitable price correction. The current situation in the market has seen soaring interest rates that has made housing expensive. This is at a time when the real estate boom has clearly percolated to Tier-II and even Tier-III cities.

Analysts tracking the sector do think there is some hype which has resulted in some stocks being quite stretched in terms of valuations. Citigroup, for instance, in a recent report has put a sell/medium risk on the Unitech stock with a target price of Rs 430; the stock was quoting at Rs 596 on May 28 when the report was put out. Commenting on the sector, the report, while terming the situation as "tough times continue", states: "Transaction activity has slowed significantly where volumes sold over a quarter last year are now sold over 9-10 months. Property prices are stagnating given affordability issues, while some pockets in the north have seen declines."

Rich Valuations

Another threat is rich valuations. Most stocks trade at sky-high P-Es. The DLF issue is priced at a p-e of 42.97. These seemingly steep valuations factor in the land banks of real estate companies. DLF has about 10,255 acres of developable land that translates to a saleable area of 574 million square feet. But if the land prices begin to fall, it could impact stock market valuations.

Real estate, according to Sharma, is a pure commodity sector. "It is necessary for the business model to change and companies need to become more infrastructure focussed in their approach," he says. Therefore, it's necessary to be choosy when looking at the sector. Companies whose land banks are not factored in their market capitalisation appear better valued than those that have. It's best to look for cheap stocks.

For real estate companies, on the other hand, the key is execution of developmental plans. But ideally, investors can look at a medium-term horizon with some high-profile companies with good projects on hand. "The investor will need to have a time horizon of at least 3-5 years. It will be necessary to stick with the big names," says Sekhar of Angel Broking.

With high levels of sustained foreign investment flowing into the sector, the going could not have been better. That apart, the growth in businesses like IT/ITEs and retail, besides a housing boom, makes the Indian real estate sector quite strong. The question is, how long can the story hold out? For now, there are no clear answers. But investors can do well with a cautious, focussed and selective long-term approach.

Cut The Card Debt
Interest costs on credit cards cost a fortune. Here's how to pay it back.

By Clifford Alvares

When you are buried deep in credit card debt, making card repayments can be a dauntingly expensive affair. After all, this debt is charged at 2.95 per cent per month, which is a whopping 41.75 per cent per annum. Add to that service tax that is charged on interest and the cost goes up to a nightmarish 48 per cent per annum. For all its advantages (convenience and a standby during emergency), the disadvantages are far greater, that is if you choose to roll over your credit and pay only the outstanding minimum balance.

A simplistic comparison against other forms of debt shows how big the gap is between credit card and other loans. The cheapest loan, a home mortgage, costs around 11 per cent, while a car loan costs around 14-15 per cent. In fact, banks are more than willing to lend without any collateral in the form of a personal loan at 18-20 per cent, provided there's a regular income and the paperwork is clear. Rates on consumer durable loans range around 16-18 per cent. Yet, when it comes to buying, say, a laptop, most people are prone to quickly flashing that credit card.

How to Save a Bundle

» Cards cost a staggering rate of 2.95 per cent per month or 41.75 per cent per annum

» Service tax on interest rates adds to the monthly outflows

» A personal loan costs far lower at around 18-20 per cent per annum

» If you have a huge outstanding, switch to a personal loan

» It's possible to save more than 60 per cent on interest costs

But using that card too often is terribly expensive. Assume you have run up a bill of Rs 1 lakh on your card, purchasing laptops and computer equipment, and are rolling over the balance outstanding, paying only 5 per cent per month. The total interest and service tax cost in the first year is a staggering Rs 35,920. But worse is when you choose to continue to pay the minimum balance payment, it could take 30 years for you to repay the balance. Continue paying the minimum balance for three years and eight months, you are weighed down by interest cost of an overwhelming Rs 1,00,193-the cost of your original laptop.

Needless to say, the best thing to do is to pay off credit card debt at the earliest. Here are some ways to pay it off.

Tap Savings

Money parked in a savings account earns just 5 per cent per annum or if it's a fixed deposit, about 10-11 per cent per annum. That means you get only Rs 5,000 per annum on a Rs 1 lakh deposit as against paying Rs 35,920 in interest cost in the first year.

Draw on Relatives

Friends and relatives are likely to finance you at no interest cost. If you can obtain such a credit line, take it and pay off the card debt.

Switch to Cheaper Loans

Loans that are cheaper than your credit cards are a better option for those who don't have access to other financing alternatives. On a three-year personal loan of Rs 1 lakh, you only pay Rs 30,148 as interest cost for three years as against Rs 35,920 of credit card interest in the first year. In fact, paying the first month's minimum payment of Rs 5,165 (see How Much a Card Costs) due towards your personal loan EMI (equated monthly installments) can wind up your card loan in a quick 23-24 months.

NEWS ROUND-UP

Triple Advantage

For the first time, there is an endowment plan that combines three features.

Normally, endowment plans don't offer these triple benefits: flexibility, guaranteed additions and guaranteed survival benefits. But for those who like insurance endowment plans, which is a combination of insurance and savings, there's a new product with enhanced features in Aviva Life's Dhanvriddhi. This product is for the conservative investor and comes with easy steps to calculate probable returns.

"There are endowment policies which offer a combination of any two, but not all three put together"
Vivek Khanna
Head (Marketing)/Aviva Life

For every Rs 1,000 sum assured, Dhanvriddhi offers a guaranteed addition of Rs 70 for every year of policy term. But the premium paying term is five years lower than the term of the policy. However, there's no single premium option. Vivek Khanna, Head (Marketing), Aviva Life, points out that this is the only policy which combines three features-flexibility to increase sum assured in multiples of Rs 10,000, guaranteed additions as mentioned above and guaranteed survival benefits which amount to 20 per cent of the sum assured payable every five years. "There are endowment policies in the market which offer a combination of any two," says Khanna, "but not all three put together."

But the plan is not without its cost. It has a high premium payout-a new entrant has to take a call on whether it would be sustainable for him to remit a regular premium for a term of 20 or 25 years. For instance, on a sum assured of Rs 3 lakh, a 35-year-old male pays a premium of Rs 27,381 for 20 years with a policy term for 25 years. By comparison, a 25-year-old pays Rs 26,775, just Rs 606 less. The difference in total outgo of premium between the two at the end of 20 years is just Rs 12,120. The maximum policy term is only 25 years, it reduces further for those who have crossed 45.

"By taking advantage of its corpus size, it (LIC) is able to give better returns for policyholders"
Rahul Aggarwal
CEO/ Optima Risk Management Services

However, the rate of return upon maturity works out to around 7.5 per cent for the maximum payable term of 20 years, and reduces progressively for lower tenures and terms. In case of death, the full sum assured along with the accrued additions till the year of death is paid out irrespective of whether survival benefits have been taken earlier.

But how does an endowment policy of LIC compare? One that comes close is the Endowment Assurance Limited Payment which charges a lower premium, but there are no guaranteed additions. It has a single premium option. On a sum assured of Rs 3 lakh, a 35-year-old male pays a premium of Rs 13,392 for 20 years for a policy term of 25 years. Therefore, this is far easier on the purse. Bonus is declared every year (profits distributed among policyholders) and it gets accrued to the sum assured at regular intervals. A final maturity benefit is a single payout at the end of term.

Says Rahul Aggarwal, CEO of Optima Risk Management Services: "A study reveals that the rate of return offered by LIC is generally higher. By taking advantage of its corpus size, it is able to give better returns for policyholders."

For those keen to know exactly what they are getting, Dhanvriddhi may be a good alternative.

- Nitya Varadarjan

On a Roll
Mutual funds assets under management have hit a new landmark.

It's raining cash in mutual funds. The industry's assets under management (AUM) crossed a staggering Rs 4 lakh crore in May 2007 as investors, corporates and even banks parked their surplus into all types of funds. Though the mutual fund industry is about 17 years old, the growth has been particularly impressive in the last five years. From Rs 98,124 crore, the industry's corpus has more than quadrupled to a whopping Rs 4,14,171.61 crore.

"The growth in the industry is inevitable with more and more retail investors coming on board"
R. Swaminathan
VP, IDBI Capital

The reasons for this growth are not too far to seek. New fund launches with new features and a host of fixed maturity plans launched in recent times are finding plenty of takers. "A simultaneous growth in debt and equity markets has led to this boom," says R. Swaminathan, Vice President, IDBI Capital. "Generating interest in the debt market, particularly issuance of new debt in the fixed maturity plans and liquid funds plus the overall interest in the equity market, have helped the industry cross this Rs 4 lakh crore mark."

But the question is whether the growth is here to stay. In the short-term, it seems there could be some profit booking. Says Swaminathan: "In the coming days, there may be a blip in AUMs due to profit booking." Over the long haul though, there's plenty of room on the upside. "But the growth in the industry is inevitable with more and more retail investors coming on board," concurs Swaminathan. With the tax benefits on equity funds, and the lack of alternative investments for retail investors, players are confident that the interest in mutual funds will not wane.

The debt segment of the fund industry is not seeing as much action. Income funds have grown from Rs 58,000 crore in the last five years to Rs 1,26,097 crore, while liquid funds corpus has increased from Rs 20,314 crore to Rs 79,936 crore. But the biggest growth has come from the equity segment. aums of growth funds increased 10-fold from Rs 11,069 crore to Rs 1,17,047 crore, suggesting that investors are comfortable with more risky equity investing.

Last month, however, saw a spectacular jump in AUMs, mainly due to investments pouring into liquid, floaters and fixed maturity plans (FMPs), driven by the rising interest rates. Industry AUMs zoomed by 18 per cent or Rs 63,704.25 crore-this was the first time the industry witnessed such a big growth in AUMs. Over 70 new FMPs were launched last month, with 42 of them of 90-day duration and 18 of more than a year. This seems to suggest there's a relative attraction of fixed return products in a volatile market.

Liquid funds garnered huge subscriptions towards the end of the month as call rates fell to near zero and corporate and institutional investors, especially banks, rushed to park surplus funds with liquid funds that gave much higher returns than call money. Says Sameer Kamdar, Head (Mutual Funds), Mata Securities: "Mark to market gains of around Rs 7,000 crore in equity funds due to a 4.5 per cent jump in Sensex also helped to increase the AUMs of the industry." On the other hand, the equity NFO market was quite subdued with two closed-end funds managing subscriptions of only Rs 1,815 crore. So far growth rates have been steady, but it remains to be seen how fast they can grow from here on.