Hop, Skip…Jump?

BSE-30 Index on course to a 21,000 level by July, 2010;

(Don't miss the ride!)

Honest Truth, May 17th, 2009

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Victory for Democracy

- The Congress surprises once more
- Regional parties will stay regional
- Is this 1991? Finance Minister Manmohan Singh had unveiled a budget that loosened the shackles under which Indians lived
- The Index surged 400% in 10 months – but that was the Harshad Mehta scam; not all due to reforms
- An Index of 21,000 is "only" 75% more from May 15th close; we just need a small dose of reforms

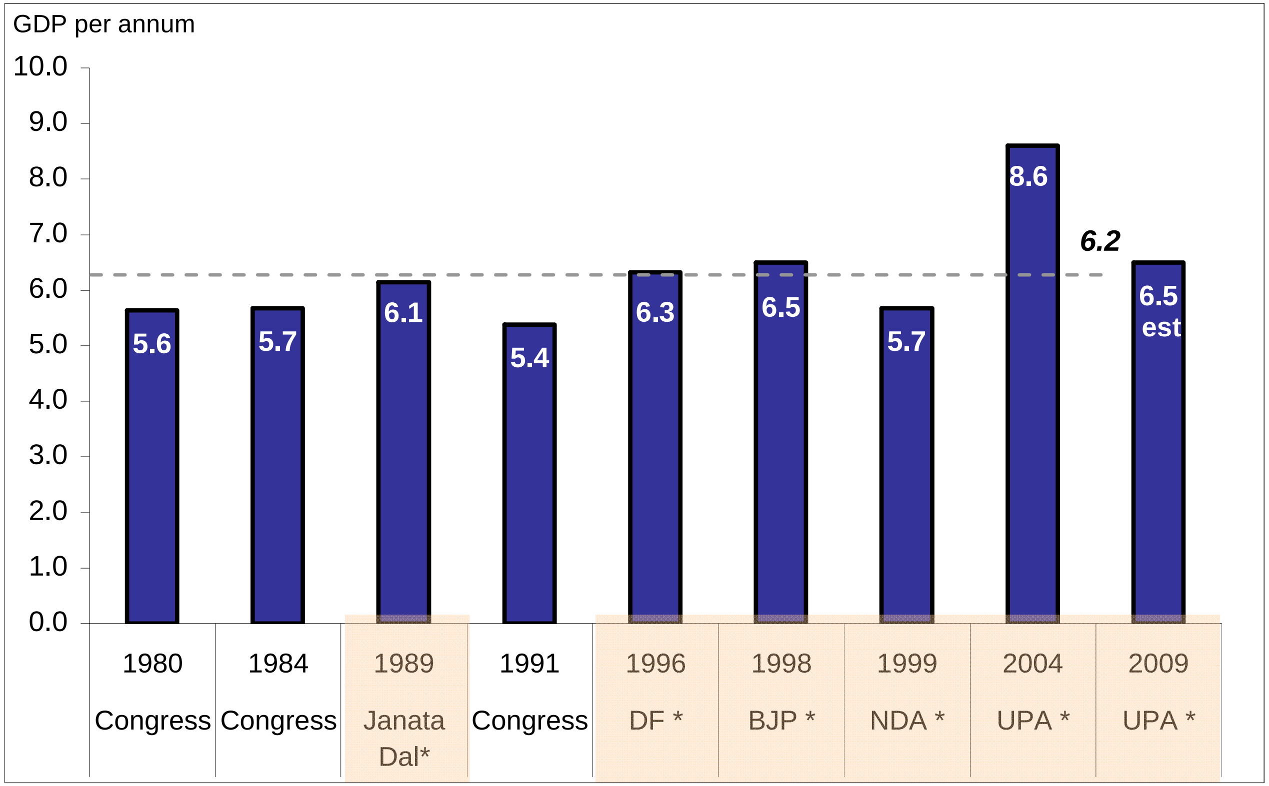
Table 1: A big election

	1999	2004	2009 est.
Total voters	620 million	672 million	710 million
Who voted	60%	58%	58%
Electronic machines	Na	1,140,000	1,183,543
Poll stations	Na	690,670	834,944
Seats	543	543	543
Candidates	4,648	5,435	8,070
Congress Party won	114	145	204
	21%	27%	38%
BJP won	182	138	121
	34%	25%	22%
Regional/Others	247	260	218
	45%	48%	40%
Coalition govt led by	BJP	Congress	Congress

Source: Election Commission of India,

India will grow…as it has

Chart 1: GDP Growth rate across 8 governments has been 6.2% p.a. over the past 28 years.



- This is the 6th coalition government of the past 9 governments since 1980
- GDP has grown by 6.2% each year for the past 28 years
- Under single party governments (1980, 1984, 1991) growth rate of GDP has been lower than growth under coalition governments

Global pessimism…local facts

- The respected global institutions are forecasting a subdued rate of GDP growth for the Indian economy - maybe they are so immersed in the global problems that they see less light?
- CMIE, India sees GDP growth rate of 6.5% this financial year
- If we have a "good" budget in July 2009, people will be scrambling to make more "bullish" forecasts
- Is there any reason to doubt that the July 2009 budget will be a "bad" budget?

Table 2: *Mirror, mirror, on the wall…*

Agency	**Est. of March 2010 GDP**
Asian Development Bank	5.0%
IMF	5.3%
OECD	5.8%
World Bank	4.0%
CMIE, India	6.5% - the one we believe in

Catch me if you can!

Table 3: The Global markets head to positive territory, India lags BRC.

(all in USD)	**% change for month ended Apr 30, 2009**	**% change YTD in CY 2009**	**% Gain/Loss since July 31, 2007 (Bear Stearns funds in trouble)**
India - BSE-30 TRI	+19.2%	+14.1%	-39.5%
Brazil - Bovespa	+22.8%	+35.3%	-25.2%
China - SHCOMP	+4.6%	+36.2%	-37.6%
Russia - RTSI$	+20.8%	+31.9%	-57.9%
MSCI EM Free	+16.6	+17.4%	-38.3%
S&P 500	+9.6%	-2.5%	-37.4%
MSCI World	+11.9%	-0.1%	-39.9%
Berkshire Hathaway	+8.4%	-2.7%	-14.5%
Gold	-3.4%	+0.7%	+33.7%
Oil	+2.9%	+14.6%	-34.6%

- India has dramatically underperformed its peers in BRIC - Brazil, Russia, and China have done really well compared to India
- Because political uncertainty made investors nervous
- That is gone – there will be an immediate 20% surge in the market this week; the BSE-30 Index will cross 14,000 comfortably

Hello, I have a bad connection

- Ranked by Economic Connection to global economy
  1) China
  2) Brazil
  3) Russia
  4) India

India has the lowest Exports / GDP ratio
Yet, when the world was in trouble – the Indian stock markets were hit the most!

- Ranked by capital market connection and ease of market entry/exit (yes, the infamous P-Notes)
  1) India
  2) Brazil
  3) China
  4) Russia

It's not always a positive to have smart Indians working with hedge funds in Wall Street, London, Dubai, Singapore, and Hong Kong!

The gambling den

Table 6*: Foreign flows turn positive after the sell-off in CY 2008 – but need to ban P-Notes*

Period	Foreign Activity (US$ m)	Local Fund Activity (US$ m)	Total (US$ m)	Change in BSE-30 TRI in that period (%)
CY 2003	6,940	93	7,033	+ 86.3%
CY 2004	8,958	-261	8,697	+ 23.1%
CY 2005	10,896	3,089	13,985	+ 42.2%
CY 2006	7,994	3,442	11,435	+53.3%
CY 2007	17,235	3,121	20,357	+68.5%
CY 2008	-13,136	2,037	-11,099	-60.7%
Cumulative	38,888	11,520	50,407	231.1%
2009 YTD 2009	+58	-151	-93	+14.1%

CY = Calendar Year;

- Foreign money will come rushing back to India – and it does not take a lot to move this market; The BSE-30 Index surged 40% between March 9th and May 15th on inflows of USD 2 billion
- Unfortunately, much of this foreign money will be P-Note, short-term, unreliable and gambling money – obviously policy makers don't read The Honest Truth and still rely on misguided advice ☺

Step back…see what happened

1. From its peak in Jan, 2008 the Index declined through June, 2008 largely because of the view that the surge in prices of oil, wheat, metals would hurt the Indian economy;
2. Between June and September 2008 commodity prices had peaked and data flows confirmed a slowing US and global economy; in India the government had to scramble for support to pass the Indo-US nuclear deal;
3. After September 15, 2008 global credit markets went into a freeze hurting many Indian companies which had accessed international capital; speculative P-Note money rushed out of India;
4. March 9, 2009 was the bottom of this bear market; Everyone called it a bear-market rally that could not sustain; May 18th will go down in history as the day the next bull market began: India's fundamental framework has dramatically improved

Junk is King?

- When gamblers come rushing in, they don't stop to think
- They will buy and sell anything which they can make money on; bulls in heat are not choosy
- Even companies that have: highly suspect businesses, suspect managements, and/or companies whose only claim to fame is their ability to bribe and loot the national exchequer
- Stay disciplined; like we do – investing is <u>NOT</u> about returns, it is about knowing the <u>*risk*</u> you take to make a potential return

Revival…or a sucker's rally?

Does a rising tide lift the driftwood: can you figure out those companies which are "junk"?

Companies	Price as on April 30, 2009	All time high	Low Price of Stock	%change from Low	% change from High
Anant Raj	81.65	378.60	39.00	109.4%	-78.4%
Suzlon Energy	63.06	454.71	33.30	89.4%	-86.1%
Reliance Capital	524.50	2,860.00	280.85	86.8%	-81.7%
ICICI Bank	479.20	1,439.90	262.95	82.2%	-66.7%
Tata Motors	243.80	954.24	136.65	78.4%	-74.5%
Unitech	44.05	538.20	24.80	77.6%	-91.8%
Pantaloon	189.70	856.60	107.05	77.2%	-77.9%
DLF	230.25	1,205.55	136.65	68.5%	-80.9%
Sterlite	410.05	1,104.80	244.45	67.7%	-62.9%
Reliance Communication	214.80	820.80	132.75	61.8%	-73.8%
Siemens	308.10	1,035.68	193.10	59.6%	-70.3%
Reliance Infrastructure	695.20	2,584.15	439.20	58.3%	-73.1%
Reliance Industries	1,806.25	3,216.30	1,153.35	56.6%	-43.8%
Tata Steel	238.10	934.80	152.35	56.3%	-74.5%
BSE 30 Index	11,403.25	20,873.33	8,160.40	39.7%	-45.4%
HDFC Bank	1,100.35	1,787.90	798.65	37.8%	-38.5%
ONGC	864.75	1,366.10	666.04	29.8%	-36.7%

..fool's gold?

- Just because we are bullish on the stock market, don't put all your money in stocks
- The lesson of the 2008/2009 crash was to always have a diversified portfolio
- Invest money that you don't really need in stocks (80%) and gold (20%)

Table 4: Gold's performance in times of crisis

(all in USD)	**% Gain/Loss since July 31, 2007 (Bear Stearns funds in trouble)**
India - BSE-30 TRI	-39.5%
Brazil - Bovespa	-25.2%
China - SHCOMP	-37.6%
Russia - RTSI$	-57.90%
MSCI EM Free	-38.3%
S&P 500	-37.4%
MSCI World	-39.90%
Berkshire Hathaway	-14.5%
Gold	**+ 33.7%**
Oil	-34.60%

Source: Bloomberg

Back to square one…unless you buy more

	Quantum Long Term Equity Fund	Quantum Gold Fund	Quantum Liquid Fund	Total
Allocation	80%	15%	5%	100%
Return since January 2008	-36%	+25%	+6%	-24%
How did that do?	Ouch!	Yes!	Good!	Oh, no!

What if the market is 21,000?

	Quantum Long Term Equity Fund	Quantum Gold Fund	Quantum Liquid Fund	Total
Allocation	80%	15%	5%	100%
Return since January 2008	-0%	+25%	+6%	+3%
How did that do?	Recovered	Yes!	Good!	Money back!

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Don’t miss this run up!

- Economy will pick up – companies will report better earnings through March 2010
- Politics – stability, continuity, and growth
- Foreign investors will seek India exposure
- These are milestone markers on the road to a new peak
- And, yes, there are risks: negative news flow from USA; oil price shocks; terrorist attacks;

In the final assessment: Upside potential is +75%; downside is -20%

The train is moving – but still in the station

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Note:

The Honest Truth is a column penned by Ajit Dayal, a well known investment advisor who has managed global equity portfolios and India-dedicated portfolios. Ajit is the founder of the Bombay-based investment advisory firm, Quantum Advisors and is also the founder of www.equitymaster.com

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