

From the CEO's Desk

Dear Reader

Greetings!

Phew! A 20% relief rally – marked by two events – one positive, about a 20% fall in oil prices and the other promising, with the trust vote won, the government may press forward on economic reforms.

But too early to open the champagne. Global cues remain negative. Recession, housing slump and financial sector woes in US, Europe joining the slow down wagon and oil remains vulnerable to geopolitical events.

Made in India issues of highs in inflation, interest rate and fiscal deficit cannot be wished away quickly. Time to continue to tread with caution.

Hiren had raised cash for two purposes – first to provide hedge against a falling market. And second, to selectively deploy to take advantage of opportunities – some long term and a few more tactical and shorter term. His long term strategy to invest for long term growth remains intact. But, in this volatile environment, he would use some tactical measures to protect the portfolio and benefit from opportunities.

Happy Reading.

Warm Regards

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CAPITAL MANAGEMENT

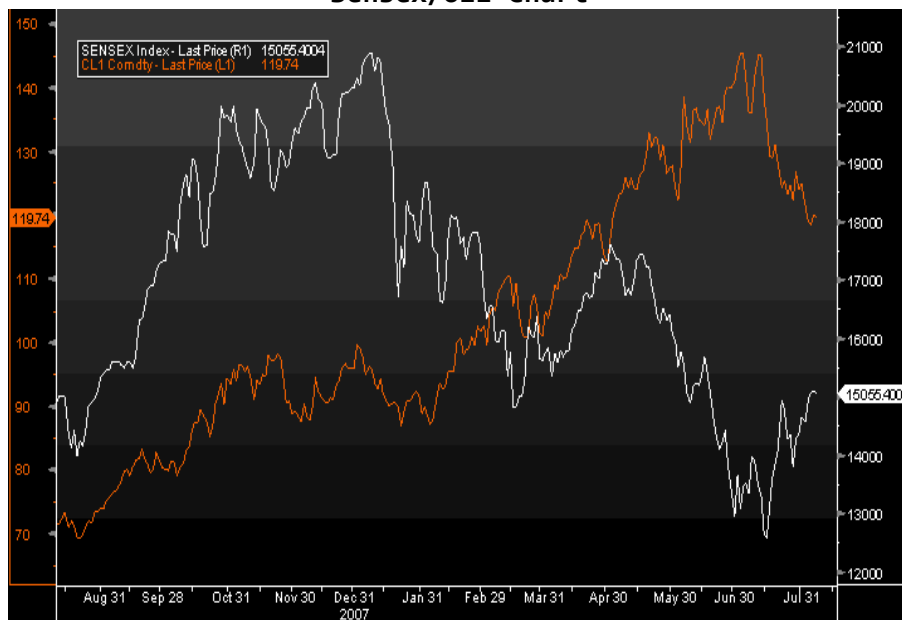
INVESTMENT MATTERS

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August 7, 2008
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Oil prices finally relented. Markets have responded. And with the government winning the trust vote, there is cautious optimism on the probability of reforms. The heavy hammer rate hike by RBI has also been taken on the chin. So, a few silver linings in the dark clouds and heavily oversold markets have got some relief.

Sensex/Oil Chart



Source: Bloomberg

But I think an interesting dichotomy is likely to persist in the short run. Markets could look very resilient as the underlying economy and corporate growth slows. The two cycles can move quite independently in the short run. Early in the year overall fundamentals were still looking good when markets were correcting and now as fundamentals weaken, markets will be on some recovery path. The extent and strength of the recovery would depend on how much crude further corrects and the extent of *real reforms* the government is able to push through when parliament reconvenes later this monsoon session.

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But amongst all this macro cacophony there are a few interesting underlying trends that I see, which I intend to use as a backdrop for finding interesting investment ideas.

1. The chemical industry (especially the integrated players) is making money hand over fist. This is because there is major dislocation in supplies from China for all polluting and hazardous substances in the run-up to the Olympics. So companies which were dependent on China for raw materials/intermediates are scampering for supplies elsewhere. India is the only other significant manufacturer of chemicals. And even though China may restart exports post Olympics, buyers now want to diversify away from a single source. So longer term, there is good opportunity for Indian companies to capture market share. And with gas supplies coming from later this year, the feedstock availability problem will also be solved, thereby aiding capacity utilisation and profitability.
2. Global increase in food prices and intensive use of agri feedstock for fuel will intensify investments in the entire agri value chain - agricultural land, seeds, agrochemicals, fertilizers, tractors and farm implements, storage and logistics.
3. The "small car" will be a global phenomenon - the two big markets which hitherto were largely large car markets, USA and China, have started to adopt small cars. This trend will only accelerate in the future. Indian car and auto component companies have a great opportunity ahead of them. While the numbers will not be visible currently as there is a compensating impact of slowing domestic demand due to rising interest rates, exports are beginning to get stronger. So if and when rates fall, domestic volumes should rise and coupled with exports should deliver stronger than before volume growth for Indian auto and auto component companies.
4. The next phase of investments for telcos will start + increased competition. Drivers being, GSM rollout by CDMA players, entry of MVNO (more competition for end customer), number portability (better deals and more advertising spending to reduce customer churn). So I think that the time has come to possibly move from the frontline telcos to the service providers (capex beneficiaries).
5. The construction/infrastructure and capital goods companies may be an interesting universe but we will need to be very selective. Investment capex will be more resilient than consumer spending (despite some slowdown). Most of them have learnt to deal with rising raw material prices by having escalation clauses/pass-throughs. Orderbooks are still strong and hence visibility is good. Competitive dynamics will shift to large players who are well funded as small players have working capital constraints and execution issues. Valuations have corrected to more reasonable levels.

We will research and test some of these hypotheses as we go forward. Not all of these trends will result in immediate actionable ideas, some of them may have to wait till some headwinds abate, but these (and some new) trends will certainly form the basis for the next few.

We have had extreme volatility in oil, commodities, forex and every other asset class. This is not an enabling environment to judge critical variables that impact business and their values - therefore, clearly not the most conducive for long term investment decisions. While we find such long term opportunities to deploy cash, we would -alongside and tactically - take advantage of a few shorter term opportunities. These are only tactical deviation from our longer term strategy - buy and hold, always being significantly invested and low churn. As markets stabilize, we will revert to our traditional strategy.

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Global Equity Market Performance

Index Performance as on August 8, 2008	1 month	3 months	6 months	1 year	YTD Returns
Emerging Market Indices					
a) BRIC countries					
Brazil Bovespa	-3.504	-17.387	-3.304	5.976	57017.55
Russian RTS	-14.41	-16.584	-7.06	-20.99	2533.37
BSE Sensex	12.21	-12.079	-12.948	2.458	15117.25
China Se Shang Composite	-2.225	-22.936	-40.003	-40.647	2713.147
b) Other EM					
Korea Kospi	-0.995	-15.641	-7.812	-14.633	1569.45
Taiwan TAIEX	-1.716	-18.239	-4.896	-17.017	7195.207
KL Composite	0.8	-11.131	-18.335	-8.195	1122.85
Stock Exch of Thai	-3.845	-5.973	-14.965	4.049	2207.672
Jakarta Composite	11.222	-1.568	-14.789	-17.375	2694.98
PSEi - Phillipine Se IDX	6.752	2.507	11.275	-6.015	2983.823
Chili IPSA	-4.503	-11.704	-2.236	-8.249	26986.98
Mexico BOLSA	1.336	5.149	17.167	2.187	39489.87
Venezuela	-0.995	-15.641	-7.812	-14.633	1569.45
Developed Market Indices					
Japanese Nikkei 225	-1.755	-6.867	0.285	-21.345	13156.81
Dow Jones Indl Avg.	2.042	-10.191	-5.489	-13.168	11431.43
NASDAQ Composite	5.089	-3.196	3.174	-7.28	2355.73
German DAX	2.31	-7.529	-2.825	-12.912	6543.49
UK: FTSE 100	-0.263	-11.547	-1.66	-9.308	5477.5
France: CAC 40	2.685	-9.951	-2.735	-17.966	4457.43
Singapore: Straits Times	-2.931	-11.284	-1.136	-10.521	2823.48
HK: Hang Seng Index	0.872	-12.884	-4.029	3.934	22133.17

Source: Bloomberg

Know an Alchemist



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Sharan joined Alchemy in January 2008. An undergraduate in Management, Sharan is currently completing his final level CMT program from Market Technicians Association, New York. Sharan has nearly four years experience in trading in bond and commodities markets. Sharan enjoys travelling and adventure sports alongside his love for Sindhi Kadhi with Aloo Tuk.

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