

The Week Gone By

Weekly Newsletter

Parag's Views

Understanding Worry - Behavioral Trait

I came across a very good write-up which I thought I should share.

The Worry Never Leaves

I thought I should throw out a "blanket definition" of wealthy before I begin. I describe "wealthy" to myself and to my clients as a state of financial life whereby the individual can simply live off of financial assets. There is no need to work. If wealthy people work, it's because they want to, not because they have to. Big difference.

Once we understand "wealthy," I would supercharge that definition to describe what I would call the "super wealthy." These would be individuals who have a personal net worth not just in the millions but in the tens or even hundreds of millions of dollars (perhaps even billions).

As a student of behavioral finance, I'm always searching for links between our state of wealth and our state of health and happiness. Having one, doesn't necessarily lead to having the others.

One thing that most "non wealthy" experience, even on a daily basis is the emotion of "worry." We worry about everything. We worry about paying the mortgage, our jobs, our retirement, our time (or lack thereof to spend on personal items), our wants and desires and what can be taken away from us. In simple terms; humans are "worry-warts."

When I study those who are "non-wealthy" I often ask why they want more money or more financial wealth. A common answer I get is, "So I don't have to worry anymore." Their thought process is that by obtaining more wealth, the worrying goes away.

But I've had an opportunity to study the wealthy as well and what I am finding is, they worry too (and sometimes a lot.) What do they worry about? Here's some examples;

- They worry that some of the top performing private equity funds are closed and won't take their money. There are so many super wealthy individuals trying to invest in the same private equity funds that require sometimes \$5 to \$10 million in minimum investment amounts that these private equity funds are turning investors away.
- They worry about running out of money due to inflation (I am not kidding on this one). The cost of living for the wealthy is rising in double digits even though the core inflation rate is much lower. Financial markets are down and their spending behavior is not being adjusted accordingly. I know you feel sorry for the cost increases in maintaining a Lear Jet and associated jet fuel prices for these people...
- They worry about staying competitive with their peer group. When they go to the Hampton's, or Palm Beach, or Jackson Hole, or on their yacht while flying their private jet, the guy next door has a bigger house, a bigger yacht, a newer jet. These are driven people that are used to being at the top of the food chain. It kills them to see someone pull ahead of them. They all want to be the kingpin, the big cheese. So they worry about how they will pull ahead of others in their peer group or they worry about falling behind in their peer group as in, "I feel like a loser since I only am worth \$25 million and these people are all worth \$50 to \$100 million..."

So what motivates them is a combination of fear and greed and while they deal with both of them, their lives are still full of worry. The worry in their lives never left. What is worrying you and is it something that is controllable or non-controllable? Are the things we worry about really important in the scheme of life. If we were 85 years old, dying on our death bed while lying in a nursing home bed, will we look back on our current life and say, "I'm glad I worried about all that stuff 40 years ago... Oh wait... what was I so worried about?"

Gold Exchange Traded Fund (ETF)

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Gold Exchange Traded Fund (ETF):

Gold is seen as an ideal way to diversify the risk in an investment portfolio, thanks to its strong negative correlation with stocks. At the same time, it has a positive correlation to oil, and with oil prices ruling above \$116 a barrel (compared to \$70 last year), gold prices have risen during last 2- 3 years. The metal has delivered 28% positive returns compared to a negative 2% delivered by the equity markets during last one year.

Metal or paper?

The good news for investors in gold: In the past few months, the choices in the mode of investment in the metal have grown. There are now five Gold ETFs in India Viz Benchmark Gold BEES, UTI gold Exchange Traded Fund, Kotak Gold ETF, Quantum Gold fund, Reliance Gold Fund.

Gold ETFs offer investors an innovative, cost-efficient and secure way to access the gold market. Gold Exchange Traded fund is intended to offer investors a means of participating in the gold bullion market through Stock Exchanges without taking physical delivery of gold. The investment objective of Gold ETF is to provide returns that closely correspond to the returns provided by domestic price of gold through physical gold.

India has historically been among the largest consumers of gold. As an investor, we tend to buy physical gold in the form of coins, bars and jewellery. You could buy gold in the form of jewellery but if you wish to invest into gold for the long term then buying physical gold may not be an ideal option.

Physical gold typically comes with drawbacks like concerns on purity, cost of storage and security. The most authentic source of gold is buying through banks, which certify its authenticity but cost 8-10% more than local jeweller. While banks sell gold, they don't buy it back. Likewise buying gold in the form of jewellery would cost an additional 15-20%, depending on the jeweller; branded jewellery comes with mark-ups of over 25%.

If you want gold as an investment, you will most likely be better off with options such as gold funds. Since these funds invest their corpus into gold, they mirror the performance of spot gold. Your holding in these funds is denoted in units, transferred to your demat account and listed on the stock exchange.

To buy an ETF from the exchange, you would pay a one-time brokerage charge of 0.25%, depending on your broker, which turns out cheaper than buying these funds during an NFO where you would end up paying an entry load of 1.5%. Also, since these funds are passively managed, the annual expense ratio is only 1%, much lower than other mutual funds.

Fund of Funds

There is a new class of funds that invest in global companies involved in the mining and production of gold. They invest in units of their international funds, which, in turn, invest in gold mining and production companies. There are two Gold funds viz. DSPML World Gold Fund, and AIG World Gold Fund, which invest in such gold mining companies. Buying gold funds makes more sense since one is buying into a business and participating in profits as well as the price movement of gold. When gold prices rise, the profitability of gold companies tends to increase more than proportionately. On the downside, a slump in gold prices will impact returns in a similar way.

Tax implications

Gold funds are more tax-efficient than physical gold. If held for more than a year, these funds qualify for a long-term capital gains tax (LTCG) of 10% compared to a three-year holding period for physical gold after which it qualifies for LTCG tax at the applicable tax rate. Also, holding physical gold of more than Rs 15 lakh attracts a wealth tax of 1% of the gold value at the end of every year.

One must keep in mind that over the long term, gold may not outperform other asset classes like equities. If you are a gold investor, you should hold with the objective of portfolio diversification and a hedge against inflation.

Indian Shipbuilding Sector

Update

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The market turmoil has taken its toll on the shipbuilding companies like ABG Shipyard & Bharati Shipyard & the scrip prices have been butchered since the time of our initiating coverage report on the shipbuilding sector. We, however maintain our positive outlook for the shipbuilding sector as a whole, on the back of the order inflow seen for shipbuilding companies the world over, both from the shipping & offshore companies. We reiterate our BUY rating for both ABG Shipyard & Bharati Shipyard.

ABG Shipyard Ltd. (ABG)

ABG Shipyard Ltd. (ABG) is today India's largest private sector shipyard, with existing facilities at Magdalla, Surat. ABG has acquired Vipul Shipyard near its Surat yard & a small repair unit named Cross Ocean Ship Repair Ltd. in UAE. ABG has commenced operations at its new yard at Dahej & has already booked revenues for the past two quarters. The rigyard at Dahej is on schedule & the company is in talks with offshore drilling companies for taking orders to build rigs. The planned expansion at its existing yard at Surat is expected to be completed by March 2009. The total order book for the company currently stands at Rs. 89,922 Mn. comprising of 94 vessels for the shipping & the offshore sector. Almost 90% of the orders are for the international clients.

The current order book at almost 10x its FY08 revenues, and the upcoming rigyard & new expansion at Surat, we believe that the company can easily scale new heights. Even on our forward estimates, ABG has secured its next 3.5 - 4 years sales with its current order book position. We still maintain our positive outlook for the company.

We have not made any changes in our earnings estimates for the company, but looking at the current market conditions, we hereby lower our target multiple from 18x FY10E earnings earlier to 10x FY10E earnings. We reiterate our BUY call for ABG Shipyard Ltd. with a target price of Rs. 525, valued at 10x FY10E EPS of Rs. 52.5.

Summary Financial

| CMP : 376.2 | | Recommendation: BUY | | Target: Rs. 525.0 | | | | | |
|--------------------|---------|---------------------|---------|-------------------|----------|----------|----------|----------|----------|
| Particulars | FY06 | FY07 | FY08 | FY09E | FY10E | FY11E | FY12E | FY13E | FY14E |
| Revenues (Rs. Mn.) | 4,687.4 | 6,242.2 | 8,851.6 | 13,946.1 | 20,863.1 | 33,684.4 | 40,727.0 | 47,421.6 | 49,066.9 |
| EBITDA (Rs. Mn.) | 1,470.7 | 2,006.4 | 2,990.7 | 4,499.8 | 6,697.8 | 10,758.3 | 12,975.1 | 15,154.8 | 15,941.3 |
| PAT (Rs. Mn.) | 837.1 | 1,163.1 | 1,606.8 | 2,418.6 | 3,563.3 | 5,468.5 | 6,798.8 | 8,214.3 | 8,710.2 |
| EBITDA (%) | 31.4% | 32.1% | 33.8% | 32.3% | 32.1% | 31.9% | 31.9% | 32.0% | 32.5% |
| PAT (%) | 17.9% | 18.6% | 18.2% | 17.3% | 17.1% | 16.2% | 16.7% | 17.3% | 17.8% |
| EPS (Rs.) | 16.4 | 22.8 | 28.2 | 38.4 | 52.5 | 80.5 | 100.1 | 120.9 | 128.2 |
| P/E (x) | 22.9 | 16.5 | 13.3 | 9.8 | 7.2 | 4.7 | 3.8 | 3.1 | 2.9 |
| EV/EBITDA | 10.9 | 10.9 | 8.3 | 6.4 | 5.1 | 4.2 | 3.5 | 3.0 | 2.8 |
| ROCE (%) | 24.6% | 19.5% | 18.4% | 16.9% | 17.4% | 19.5% | 20.9% | 21.8% | 20.5% |
| RONW (%) | 17.4% | 19.8% | 13.7% | 12.7% | 13.5% | 17.4% | 18.0% | 18.2% | 16.4% |

Bharati Shipyard Ltd. (BSL)

Currently, number two on the list of private shipbuilding companies, Bharati Shipyard has maintained its position operating from its yards located at Ratnagiri, Ghodbunder, Kolkata & Goa. BSL has started building vessels at its new yard at Dabhol & is also on schedule to deliver the rig being built for Great Offshore Ltd. The company is also building a shipyard at Mangalore which will be able to build vessels upto 60,000 DWT. The current order book for the company stands at Rs. 48,703 Mn. comprising of 51 vessels, largely geared towards the offshore sector.

BSL's current order book stands at about 7.6x its FY08 revenues & on our forward estimates, the company has almost 3.5 years of sales on hand. With such robust & strong revenue visibility, we believe that the company should be able to deliver better performance in the future. We maintain our positive outlook for Bharati Shipyard.

We have not made any changes in our earnings estimates for the company, but looking at the current market conditions, we hereby lower our target multiple from 18x FY10E earlier to 10x FY10E. We reiterate our BUY call for Bharati Shipyard Ltd. with a target price of Rs. 578, valued at 10x FY10E earnings of Rs. 57.8 per share.

Summary Financial

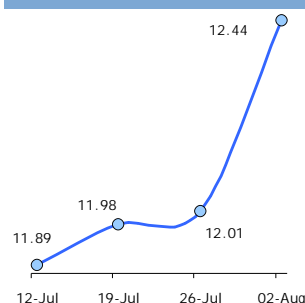
| CMP : 329.5 | Recommendation: BUY | | Target: Rs. 578.0 | | | | | | |
|--------------------|---------------------|---------|-------------------|---------|----------|----------|----------|----------|----------|
| Particulars | FY06 | FY07 | FY08 | FY09E | FY10E | FY11E | FY12E | FY13E | FY14E |
| Revenues (Rs. Mn.) | 2,608.2 | 3,610.2 | 6,400.9 | 9,555.4 | 13,055.4 | 17,555.4 | 26,055.4 | 36,555.4 | 43,805.4 |
| EBITDA (Rs. Mn.) | 893.2 | 1,303.5 | 1,914.6 | 3,043.0 | 4,149.9 | 5,572.4 | 8,259.4 | 11,576.9 | 13,864.8 |
| PAT (Rs. Mn.) | 510.3 | 732.0 | 1,073.2 | 1,606.3 | 1,851.8 | 2,406.9 | 3,720.0 | 5,557.3 | 7,119.4 |
| EBITDA (%) | 34.2% | 36.1% | 29.9% | 31.8% | 31.8% | 31.7% | 31.7% | 31.7% | 31.7% |
| PAT (%) | 19.6% | 20.3% | 16.8% | 16.8% | 14.2% | 13.7% | 14.3% | 15.2% | 16.3% |
| EPS (Rs.) | 22.7 | 32.5 | 38.9 | 50.1 | 57.8 | 75.1 | 116.1 | 173.4 | 222.2 |
| P/E (x) | 14.5 | 10.1 | 8.5 | 6.6 | 5.7 | 4.4 | 2.8 | 1.9 | 1.5 |
| EV/EBITDA | 9.1 | 6.9 | 6.2 | 4.9 | 5.1 | 4.5 | 3.8 | 3.1 | 2.4 |
| ROCE (%) | 12.1% | 15.7% | 18.8% | 20.2% | 17.1% | 17.3% | 19.5% | 22.2% | 24.2% |
| RONW (%) | 29.0% | 30.4% | 18.6% | 17.0% | 16.5% | 17.8% | 21.9% | 25.1% | 24.9% |

Our confidence on this sector & more on both these companies is driven by the fact that both ABG & BSL have secured orders enough to cover their sales for the next 3.5 to 4 years on the expanded capacity. Also they have in place a back to back sourcing arrangement for critical bought out components. Other materials like steel are already bought & secured upon order confirmation. So these companies have been able to secure their margins as well, along with the revenues. With orders coming in from genuine users & also with advance payments made, we feel that the possibility of order cancellation is low. Overall, we observe that these two companies have much stronger visibility for growth & margins as compared to any other engineering player. All the other engineering companies, we observe have secured revenues/have order books, equivalent to the next 9 to 15 months of sales. Also there is no 100% hedging for margins due to fluctuations in input costs.

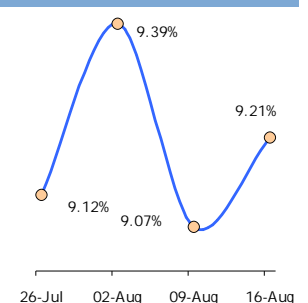
Shipbuilding companies have been generally trading at a significant discount to the engineering plays. While we do not expect this to change, we clearly perceive that these two companies deserve better valuations given the high visibility.

| Local Equity Market | | | | | | Top Gainers & Losers of the Week | | | |
|-----------------------------|-----------|-----------|------------|-------------------|-------------------|---|------------|---------|----------|
| INDICES | 18-Aug-08 | Week Ago | % Chng | Month Ago | % Chng | Top Gainers | Aug 18, 08 | % Chng | |
| Sensex | 14,724.18 | 15,167.82 | (2.92) | 13,635.40 | 7.98 | Noida-Toll Bridge Co. Ltd. | 45.45 | 21.04 | |
| Nifty | 4,430.70 | 4,529.50 | (2.18) | 4,092.25 | 8.27 | Zuari Industries Ltd. | 313.35 | 14.89 | |
| CNX Nifty Junior | 7,173.60 | 7,465.40 | (3.91) | 6,395.35 | 12.17 | Federal-Mogul Goetze (India) Ltd. | 62.25 | 11.96 | |
| S&P CNX500 | 3,551.30 | 3,635.00 | (2.30) | 3,248.05 | 9.34 | H.E.G. Ltd. | 265.80 | 11.42 | |
| CNX Midcap 200 | 5,804.90 | 5,904.00 | (1.68) | 5,149.20 | 12.73 | Rallis India Ltd. | 565.70 | 11.22 | |
| CNX IT | 3,907.40 | 3,916.40 | (0.23) | 3,571.60 | 9.40 | Shriram Transport Finance Co. Ltd. | 347.10 | 10.79 | |
| International Equity Market | | | | | | Top Losers | | | |
| INDICES | 18-Aug-08 | Week Ago | % Chng | Month Ago | % Chng | Zandu Pharmaceutical Works Ltd. | 15,542.60 | (14.07) | |
| DJIA | 11,659.90 | 11,734.32 | (0.63) | 11,496.57 | 1.42 | Industrial Development Bank of India Ltd. | 81.25 | (11.64) | |
| Nasdaq | 2,452.52 | 2,414.10 | 1.59 | 2,282.78 | 7.44 | Ingersoll Rand (India) Ltd. | 371.85 | (11.12) | |
| S&P 500 | 1,298.20 | 1,296.32 | 0.15 | 1,260.68 | 2.98 | State Trading Corporation of India Ltd. | 272.95 | (10.99) | |
| FTSE 100 | 5,454.80 | 5,489.20 | (0.63) | 5,376.40 | 1.46 | Power Finance Corporation Ltd. | 130.45 | (10.50) | |
| Nikkei 225 | 13,019.41 | 13,168.41 | (1.13) | 12,803.70 | 1.68 | Bombay Dyeing & Manufacturing Co. Ltd. | 564.15 | (10.28) | |
| Hang Seng | 21,160.58 | 21,885.21 | (3.31) | 21,874.19 | (3.26) | DLF Ltd. | 500.00 | (10.23) | |
| HSCEI | 11,170.20 | 11,742.39 | (4.87) | 12,123.88 | (7.87) | Bank of Baroda | 255.00 | (10.04) | |
| MSCI Indices | | | | | | Sectoral Performance | | | |
| MSCI Indices | 18-Aug-08 | Week Ago | % Chng | Month Ago | % Chng | Sectors | Week | Month | 3 Months |
| The World Index | 1,342.96 | 1,357.83 | (1.10) | 1,362.52 | (1.44) | Refractories | 7.47 | 22.72 | (14.36) |
| Emerging Market | 971.89 | 990.02 | (1.83) | 1,022.16 | (4.92) | Bearings | 4.66 | 16.13 | (5.94) |
| EM Asia | 373.85 | 383.86 | (2.61) | 376.02 | (0.58) | Personal Care | 4.59 | 9.85 | (5.47) |
| EM India | 423.30 | 444.13 | (4.69) | 391.02 | 8.25 | Pesticides And Agrochemicals | 4.51 | 25.75 | 4.38 |
| Commodities | | | | | | Travel And Transport | 3.68 | 20.93 | (6.32) |
| Commodities | 18-Aug-08 | Week Ago | % Chng | Month Ago | % Chng | Dyes And Pigments | 2.84 | 23.39 | 9.68 |
| GOLD (\$/oz) | 797.00 | 823.85 | (3.26) | 955.00 | (16.54) | Fertilisers | 2.34 | 27.73 | (4.19) |
| SILVER (\$/oz) | 13.23 | 14.67 | (9.87) | 18.13 | (27.06) | Mining | 2.13 | 8.86 | (22.73) |
| ALUMINIUM (\$/t) | 2,780.00 | 2,833.00 | (1.87) | 3,033.00 | (8.34) | Detergents | 1.40 | (1.32) | (19.63) |
| COPPER (\$/t) | 7,360.00 | 7,330.00 | 0.41 | 8,085.00 | (8.97) | Electrodes | 1.34 | 12.95 | (8.08) |
| CRUDE - BRENT (\$/bbl) | 114.00 | 114.07 | (0.06) | 131.11 | (13.05) | Auto Ancillaries | 1.21 | 9.78 | (16.93) |
| CRUDE - WTI (\$/bbl) | 115.12 | 114.45 | 0.59 | 129.47 | (11.08) | Leather And Leather Products | 1.13 | 14.83 | (9.39) |
| Transportation | | | | | | Tyres | 1.13 | 14.01 | (22.14) |
| Transportation | 18-Aug-08 | Week Ago | % Chng | Month Ago | % Chng | Computers - Software | 1.01 | 13.67 | (14.38) |
| World SCALE | 87.50 | 92.50 | (5.41) | 240.00 | (63.54) | Cycles | 0.60 | 21.67 | (3.64) |
| BALTIC FREIGHT INDEX | 7,557.00 | 7,055.00 | 7.12 | 9,012.00 | (16.15) | Computers - Hardware | 0.50 | 5.23 | (25.34) |
| Forex | | | | | | Chemicals - Speciality | 0.41 | 6.68 | (4.69) |
| FOREX | 18-Aug-08 | Week Ago | % Chng | Month Ago | % Chng | Finance | 0.18 | 13.12 | (16.71) |
| USD | 42.69 | 42.06 | 1.48 | 42.79 | (0.23) | Electrical Equipment | 0.02 | 17.88 | (9.39) |
| GBP | 80.90 | 81.13 | (0.28) | 84.99 | (4.81) | Printing And Publishing | (0.02) | 12.07 | (19.48) |
| EURO | 63.68 | 63.38 | 0.48 | 67.38 | (5.50) | | | | |
| YEN | 39.23 | 38.33 | 2.35 | 39.75 | (1.31) | | | | |
| Global Listings | | | | | | | | | |
| Scripts | 16-Aug-08 | Week Chng | Month Chng | Premium/D iscount | Share per ADR/GDR | | | | |
| Infosys ADR | 42.42 | 2.61 | 7.60 | 6.02% | 1 | | | | |
| Wipro ADR | 11.68 | 0.17 | 7.86 | 16.12% | 1 | | | | |
| ICICI Bank ADR | 31.12 | (12.76) | 18.90 | 1.42% | 2 | | | | |
| Satyam ADR | 22.93 | (3.57) | 7.89 | 18.64% | 2 | | | | |
| HDFC Bank ADR | 84.70 | (9.07) | 20.97 | 4.29% | 3 | | | | |
| MTNL ADR | 5.14 | (2.10) | 16.15 | 3.88% | 2 | | | | |
| Dr. Reddy ADR | 14.07 | (4.87) | (6.98) | 2.89% | 1 | | | | |
| Reliance GDR | 107.00 | (4.89) | 12.22 | 3.07% | 2 | | | | |
| ITC GDR | 4.36 | (4.39) | 12.59 | -0.71% | 1 | | | | |
| Ranbaxy GDR | 11.36 | (4.22) | 16.85 | -0.85% | 1 | | | | |
| L & T GDR | 62.80 | (9.12) | 16.33 | 2.41% | 1 | | | | |

Inflation (%)



10 year G-Sec Bond Yield



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