

Betting on infrastructure

Renu Yadav looks at this popular theme and analyses the best picks

As we write this, fears are mounting that India may not be ready for the Commonwealth Games, reflecting the slow pace of the country's infrastructure development. India had initially promised to hand over the venues to the organisers by December 31, 2009. But targets have consistently been missed.

This is just a minor reflection of the poor state of affairs where India's overall infrastructure is concerned. There's no denying that infrastructure, or rather the lack of it, is the biggest bottleneck for improving India's march towards matching China's growth, the world's fastest growing economy. Globally, India ranks low on the quality of its infrastructure. In fact, it ranks even below war-ravaged Ivory Coast on this parameter. Blame it on the bureaucracy, red tape and difficulty in acquiring land.

Experts estimate that the country's poor infrastructure shaves an estimated 1-2 percentage points off India's annual economic growth. Prime Minister Manmohan Singh's ambitious target of 10 per cent economic growth has prompted the government to announce the setting up of a Rs 50,000 crore (\$11 billion) fund to build roads, ports and bridges to drive economic growth. The basic premise of the proposed fund is to facilitate adequate and smooth funding for the sector. Considering that India's underdeveloped bond market — with limited funding options from a long-term perspective — has restricted the flow of funds to this sector, this is a step in the right direction.

A good start, but insufficient. Much more needs to be done.

India spent 6.5 per cent of its gross domestic product (GDP) in 2009 on infrastructure. Though we are way behind China in infrastructure spend (the corresponding figure for China in 2009 was 11%), it still comprises a significant amount. In the last Budget, the finance minister allocated nearly 46 per cent (Rs 1,73,552 crore) of the total planned expenditure to the infrastructure sector. The government has pegged infrastructure investment at 7.5 per cent (2009-10), 7.94 per cent (2010-11) and 8.37 per cent (2011-12) of GDP.

So what does this mean for you as an investor? Should you bet on this sector? With the amount of money slated to go into it, why not?

Is there money to be made?

Where thematic funds are concerned, the most popular of the lot has been infrastructure. As of now, the amount of money in infrastructure funds is Rs 14,133 crore (May 31, 2010), distributed amongst 20 schemes. In fact, the assets of

Category Performance Analysis

Annual Returns (%)

Year	2005	2006	2007	2008	2009
Category Average	55.29	53.38	81.00	-58.21	79.25
Worst Performer	53.57	34.16	67.17	-72.14	6.71
Best Performer	57.00	61.48	92.92	-51.27	127.18
Top Quartile Average	-	60.90	91.93	-52.37	102.63
Bottom Quartile Average	-	34.16	69.59	-66.01	52.65
Deviation from BSE 100 (%)	16.94	12.42	21.25	-2.93	-5.79

Trailing Returns (%)

Period	Cat Avg	Range		BSE 100
		Min	Max	
6-Month	2.55	-3.30	10.58	1.42
1-Year	17.83	-0.89	31.49	18.65
2-Year	2.83	-28.53	11.74	2.04
3-Year	6.63	-19.52	12.33	6.58
5-Year	23.39	21.24	25.31	20.21
Bull Run	82.73	39.63	145.18	88.21
Bear Run	-59.42	-75.59	-52.25	-58.04

Category Portfolio Analysis

Top 10 Holdings

Company	Funds Invested*	% of Net Assets
Reliance Industries	11	6.87
BHEL	11	4.03
ONGC	10	3.81
NTPC	7	3.30
Larsen & Toubro	10	3.29
Tata Power Co.	9	2.86
Bharti Airtel	7	2.82
Sterlite Industries	8	2.45
ICICI Bank	4	2.03
GAIL	9	1.80

Bull Run: (09/03/09 - 31/05/10)

*Total number of funds is 21

Top 10 Sectors

Sectors	Funds Invested*	% of Net Assets
Energy	13	27.44
Financial	13	13.30
Engineering	14	12.16
Metals	14	10.26
Construction	14	9.45
Diversified	12	8.13
Services	12	4.81
Telecom	9	3.39
Automobile	6	1.03
Health Care	3	0.33

Bear Run: (08/01/08 - 09/03/09)

Portfolio Concentration

	Cat Avg	BSE 100
Number of Stocks	42	100
Top 10 Holdings (%)	42.84	46.75
Top 20 Holdings (%)	66.95	62.71
Top 3 Sectors (%)	60.59	55.26

Investment Style

	Cat Avg	BSE 100
Portfolio P/E Ratio	24.89	28.10
Portfolio P/B Ratio	3.52	4.84
Market Cap (Rs cr)	17,731	103,808

All data as on May 31, 2010

EXPERT SPEAK

M Venugopal

Fund Manager
Tata Infrastructure



Consolidation in the industry took place starting end 2007. Stock prices have bounced back to some extent since May 2009 but have underperformed the broad market and other sectors. Things are expected to pick up now. In the last two quarters we have seen an improvement in fundamental performance and on ground activity levels. Industrial production has been improving over the past several months and these numbers are also expected to remain buoyant as we go ahead, though there could be some cooling off later due to higher base effect. Also, GDP growth numbers are getting revised ahead for FY11. Infrastructure will be one the key drivers of GDP growth. Naturally, corporate performance too would be in line with these numbers.

Many of these companies have raised capital in the last 18 months or so. Their balance sheets are much cleaner today. However, some did get stuck in real estate and BoT projects which resulted in capital getting mis-allocated or to projects with a lower ROCE. As a result, valuations do look fairly high in certain cases, so selective stock picking is required.

By and large, activity levels have picked up, balance sheets have improved, the government is in a better position to give out orders, order flows are picking up across sectors and industrial capex is seeing some improvement. By the second half of this year all these aspects are expected to gain further momentum. The only caveat is that the global economy should improve or at least remain in the same trajectory. A repeat of 2008 will hit the sector badly.



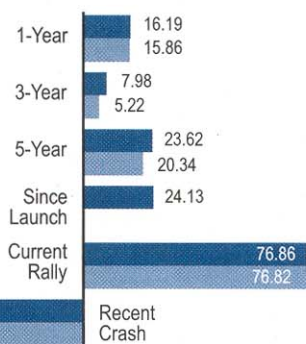
Steady, not spectacular

Average Net Assets: Rs 2,144 cr

Launch: December 2004

Fund Manager: M Venugopal

Returns (%)



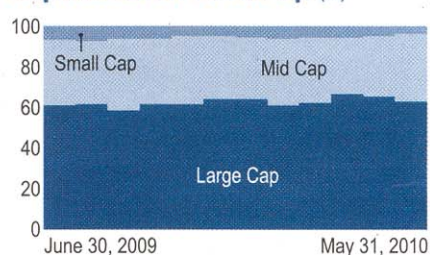
■ Fund ■ Sensex
Current Rally: 09/03/2009 - 09/06/2010
Recent Crash: 08/01/2008 - 09/03/2009

Fund Top Holdings (%)

Company	Fund	BSE Sensex
Reliance Industries	5.82	14.22
Rural Electrification	4.25	-
HDFC Bank	4.10	5.24
BHEL	3.94	3.05
Crompton Greaves	3.92	-

The last column indicates the holdings' allocation in the benchmark

Capitalisation Break-up (%)



Fund Style

Investment Style	Capitalisation		
	Growth	Blend	Value
Large	■	■	■
Mid	■	■	■
Small	■	■	■

All data as on May 31, 2010

What you find here is a huge and diversified portfolio with a distinct large-cap flavour. Even the derivatives exposure, which is not often, is never huge and only in Nifty Futures. Naturally, such a portfolio cannot be expected to deliver astounding returns, but will give investors a good night's rest and add to their bank balance.

This bent is the result of the fund's size. In a big fund, the top exposures by default have to be in larger stocks. A Rs 3,000 crore fund would have an exposure of Rs 120 crore to a stock if it amounted to just 4 per cent of its portfolio. Exposure to mid- and small-caps would have to be done wisely. Hence the top holdings are in large caps and the tail end of the portfolio is allocated to smaller caps. "Being a reasonably large thematic fund, we prefer to form a view and ride it out and do not keep shuffling the portfolio like a small fund. But there are ample good quality large caps, which form my top picks from a longer-term perspective," says Venugopal. While he does not churn his portfolio rapidly, he shifts positions amongst the top 10 stocks whose rankings change constantly.

After an impressive 2006, this fund's returns have been in line

with the category average with a slight underperformance in 2009. But again, that was simply because funds with smaller-cap stocks rallied on ahead. By and large, Venugopal has always been on track with his sector picks.

The rally in Construction and Basic Engineering in 2006 where the fund held a total average exposure of 52 per cent, for instance. The next year, he increased his exposure to Metals, even when the sector was languishing, which paid off as it later gained tremendous momentum. Surprisingly, he got out of Construction pretty early in 2007. Had he stayed on in this sector, his returns would have been astounding. However, valuations were going haywire. In 2008, he dropped exposure to Financials between January and May but later increased it, a move that again paid off.

Though his exposure to Energy and Metals is now more or less in line with the category average, he is pretty bullish on Financials. He cites "reasonable valuations, strong growth in corporate banking, and credit growth as corporate capex improves" as the reason. Venugopal looks for strong growth companies, but does so cautiously. A sound bet and good track record make it stand out in this space.

Performance

