

June 14, 2007

FOR PRIVATE CIRCULATION

Equity

	13 June 07	% Chg		
		1 Day	1 Mth	3 Mths
Indian Indices				
Sensex	14,003	(0.9)	0.3	11.8
Nifty	4,113	(1.0)	(0.5)	13.0
Banking	7,369	(1.1)	4.2	17.6
IT	3,683	(0.6)	(0.1)	7.1
Healthcare	3,748	0.2	1.0	8.4
FMCG	1,773	(1.0)	(2.2)	9.8
PSU	6,376	(0.8)	(2.4)	16.1
CNX Midcap	5,507	(0.4)	2.4	19.1
World indices				
Nasdaq	2,582.3	1.3	1.4	8.9
Nikkei	17,733	(0.2)	1.0	7.0
Hangseng	20,579	(0.3)	(1.2)	10.1

Value traded (Rs cr)

	13 June 07	% Chg - 1 Day
Cash BSE	4,090	10.4
Cash NSE	8,096	(1.0)
Derivatives	34,009.3	(9.6)

Net inflows (Rs cr)

	11 June 07	% Chg	MTD	YTD
FII	545	1,099	(71)	17,196
Mutual Fund	(340)	(1,265)	(318)	(794)

FII open interest (Rs cr)

	11 June 07	% chg
FII Index Futures	16,859	6.1
FII Index Options	6,807	0.3
FII Stock Futures	19,471	2.1
FII Stock Options	37	(1.1)

Advances/Declines (BSE)

	13 June 07	A	B1	B2	Total	% Total
Advances	78	296	417	791	42	
Declines	129	420	463	1,012	54	
Unchanged	5	21	35	61	3	

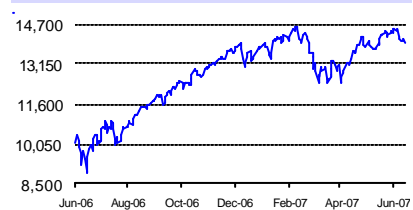
Commodity

	13 June 07	% Chg		
		1 Day	1 Mth	3 Mths
Crude (NYMEX) (US\$/BBL)	66.2	(0.0)	6.0	13.9
Gold (US\$/OZ)	651.8	0.7	(2.8)	1.0
Silver (US\$/OZ)	13.1	0.7	(0.3)	2.1

Debt/forex market

	13 June 07	1 Day	1 Mth	3 Mths
10 yr G-Sec yield %	8.34	8.33	8.18	8.00
Re/US\$	41.0	40.8	40.9	44.2

Sensex



Source: Bloomberg

ECONOMY NEWS

- ❑ Civil Aviation Minister Praful Patel has proposed that even start-ups should be allowed to operate international flights. As of now, airlines are permitted to launch international operations only after completing five years of service in the domestic circuit. (ET)
- ❑ The Commerce Ministry has proposed a relief package that would see duty entitlement pass book and duty drawback rates being enhanced by 5%. In addition, the interest rate on pre- and post-shipment credit would be reduced to 6% from the 9-11% range now. (BS)
- ❑ The big-ticket comprehensive economic partnership agreement with Japan has hit a roadblock with the Finance Ministry opposing any cut in tariffs. Japan's demand for scrapping export duties has also been rejected by the ministry. (ET)
- ❑ The Centre may consider sharing a portion of the recently imposed export duty on iron ore with states. The move is aimed at providing additional revenues to mineral rich states, where royalty rates have remained abysmally low. (ET)
- ❑ Concerned over a shortfall in meeting the targets of its flagship Bharat Nirman scheme, the Government is proposing an additional funding of Rs.20 bn for the Accelerated Irrigation Benefit Program during the current fiscal. (ET)

CORPORATE NEWS

- ❑ **ONGC's** foreign arm ONGC Videsh is all set to acquire around 33% stake in Shell's high-prospective block in the Northeast Mediterranean deepwater (Egypt). (ET)
- ❑ Hyderabad-based bulk drug major **Aurobindo Pharma** is looking at acquiring a European company of size not exceeding \$100 mn to have a 'launch pad' in the continent. (BS)
- ❑ **Tata Tea** has sued **Hindustan Unilever** over a patent granted by the Indian Government for the process of making instant tea from cold water. HUL claims its parent company, Unilever, owns the invention and has already patented it in Europe and the US. (BS)
- ❑ **ICICI Bank** will raise Rs.87.5 bn in the domestic stock market through a follow-on public issue. The bank said it would issue equity shares of Rs.10 each for cash at a price to be determined by book building (including a share premium per equity share) aggregating to Rs.87.5 bn. (BL)
- ❑ **Simplex Infrastructures** announced it had bagged two overseas orders aggregating to Rs.10.07 bn. (BL)
- ❑ With a view to enhancing output to meet the power generation commissioning schedule during the current Plan, **Bhel** is operating critical machines round-the-clock on three shift operations, a company release said. (BL)
- ❑ The **Indian Hotels Company**, which operates the Taj group of hotels and resorts, would be doubling its existing room count from 6,500 to around 13,000 rooms in the country. (BL)
- ❑ **Wyeth** has posted over seven fold increase in net profit at Rs.132.5 bn for the quarter ended March 31, as compared to Rs.17.7 mn for the same quarter last year. The total income (net of excise) of the company grew 36.63% to Rs.638.1 mn for the quarter ended March 31, from Rs.467 mn for the corresponding quarter a year ago. (ET)
- ❑ With growth on the agenda, **Reliance Life Sciences** and its fledgling subsidiary **Reliance Pharmaceuticals Ltd** are looking at options, including roping in a strategic partner or an outright acquisition. (BL)

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, BL = Business Line, ToI: Times of India, BSE = Bombay Stock Exchange

FROM OUR RESEARCH TEAM

SECTOR UPDATE

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CONSTRUCTION SECTOR REVIEW POST FY07

The construction sector posted an excellent set of numbers for Q4FY07 as well as FY07 with strong revenue growth and remarkable improvements in their operating margins. The order books of the companies surged ahead to provide revenue visibility for the next two and a half to three years, along with diversification into new sectors such as oil and gas exploration, real estate, power etc.

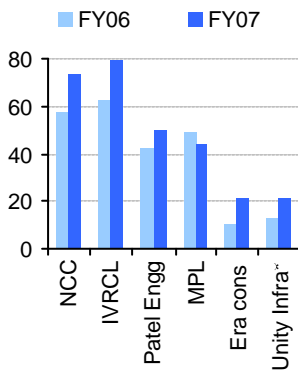
Though the order inflow momentum in different segments is expected to be maintained, we expect it to start gathering pace once road BOT projects get awarded to players. The removal of the benefits of section 80IA has impacted the profitability of the companies. However, going forward, bids would correspondingly take into account higher tax rate. We continue to maintain our positive bias for the sector. Our top picks are Patel Engineering, Nagarjuna Constructions, Unity Infraprojects and Era Constructions.

Key highlights of FY07 results

■ Robust order books

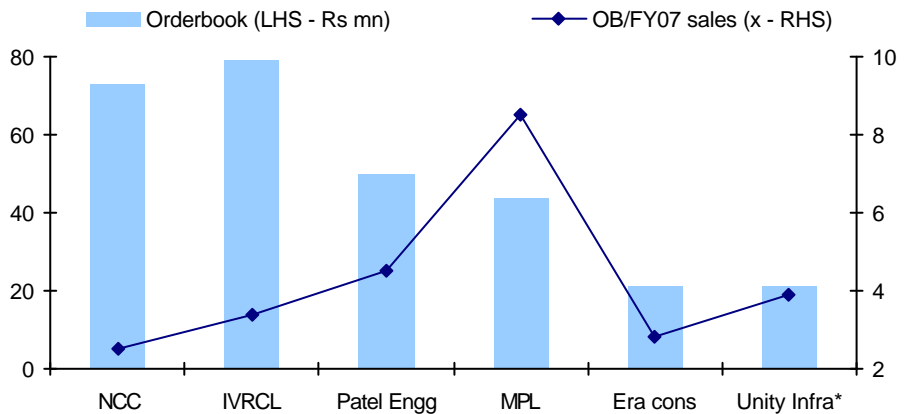
Despite slower order inflows in the roads segment, construction companies grew their order books by approximately 30% as compared to last year. Smaller companies have seen much higher growth in their order books. With the continuous thrust of the Government on infrastructure development across all segments such as roads, water, irrigation, buildings, oil and gas etc, we expect companies to witness a similar trend in their order books in the coming years.

Orderbook (Rs bn)



Source: Companies

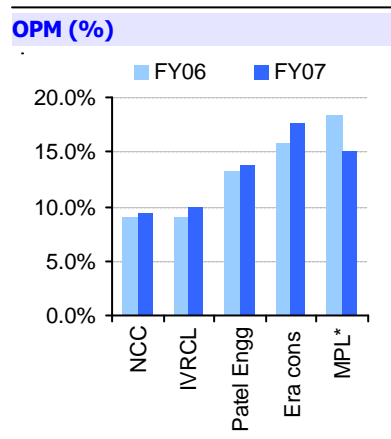
Order book to sales



*Expected sales for unity infraprojects
Source: Companies, Kotak Securities - Private Client Research

■ Improving profitability

The companies have shown a remarkable improvement in operating margins over the last year. This trend has been witnessed for the last two years. The companies have been able to improve their profitability despite rising raw material prices. This improvement is the result of continuous diversification and variable pricing clauses with the clients. The net profit margins of the company are not comparable with the last year due to an increase in effective tax rates.



Source: Companies; * Madhucon projects changed its expense classification in FY07

Margin improvements

	OPM (%)		Change
	FY06	FY07	
NCC	8.9	9.4	50bps
IVRCL	9.0	10.0	100bps
Patel Engg	13.2	13.7	50bps
Era cons	15.70	17.70	200bps
MPL*	18.30	15.10	- 320 bps

*Madhucon projects changed its expense classification in FY07

■ Impact OF 80IA withdrawal

With the removal of Section 80IA benefits, the profitability of the companies has been impacted in a negative way. Companies like Nagarjuna Construction and Madhucon Projects have provided for the changes in the tax structure but IVRCL and Patel Engineering have not made any provisions since these companies are waiting for the final decision of the Appellate Tribunal of Income Tax that is expected by July 2007.

Era Constructions was not impacted since the company was already paying tax at a higher rate. Going forward, however, we have assumed a higher tax rate for these companies. Hence, any decision to relax the tax burden by the tax authorities can result in some positive trigger.

■ Real estate development plans

Construction companies are looking at real estate development as another growth area apart from their core construction business. Nagarjuna Constructions is carrying out real estate projects through NCC Urban Infrastructure. NCC Urban Infrastructure has a land bank of 530 acres and would be carrying out the real estate development of 286 acres over the next two to three years.

Patel Engineering has formed a wholly-owned subsidiary Patel Realty India Ltd (PRIL) to carry out real estate development in cities like Mumbai, Bangalore, Hyderabad, Chennai and others to develop its land bank of 500 acres. Era Constructions is carrying out real estate development through its subsidiary Era Infrastructure Ltd. Since the current land bank was acquired at a very low cost some years ago, these projects of the companies are expected to be profitable in the longer run.

■ Fund raising plans

With the rise in working capital requirements of the companies due to the rapid scaling up of operations and upcoming large sized BOT projects, the companies would have to depend upon fund raising for equity investments in large size BOT projects. IVRCL had raised \$125 mn through a QIP issue last year. Era Constructions has raised \$75 mn through an FCCB issue, the pricing of which will be decided in a year.

Nagarjuna Constructions is planning to raise \$180 mn through a QIP issue. These fundraising activities impact the RoEs and RoCE of the companies in the short-term but returns start improving once the proceeds are invested in profitable ventures. Patel Engineering and Unity Infraprojects are currently not looking at raising funds since they have sufficient funds available to be invested in the next one to one-and a half years.

■ Future focus areas

Construction companies have been forming separate SPVs for their new ventures such as BOT projects, real estate projects, etc and would look to expand those new verticals in an aggressive way. Future areas of focus, in terms of new verticals, would be real estate, power, coal mining, oil and gas and international ventures.

Relative Valuations

	P/E (x)		EV/EBITDA (x)		Price (Rs)	Target (Rs)	Reco
	FY08E	FY09E	FY08E	FY09E			
Nagarjuna constructions	16.9	13.2	8.9	7.2	160	210	BUY
Patel Engineering	22.0	18.4	11.9	9.9	405	424	HOLD
Unity Infraprojects	10.3	8.3	5.4	4.3	467	636	BUY
Era Constructions	7.3	5.6	3.5	2.7	335	500	BUY
Madhucon Projects	14.7	9.7	7.4	5.7	198	251	HOLD

Source: Kotak Securities - Private Client Research

We continue to maintain our positive bias on the sector given the revenue visibility, improvement in margins and venture into other growing and profitable areas. Due to the run up in the stock price, we currently have a **HOLD** on Patel Engineering and a **BUY** on Nagarjuna Constructions, Unity Infraprojects and Era Constructions.

EVENT UPDATE

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We maintain BUY on Megasoft with a price target of Rs.180 (upside 36%)

MEGASOFT LTD

PRICE : Rs.132
TARGET PRICE : Rs.180

RECOMMENDATION : BUY
CY07E PE : 11x

Highlights

- Megasoft's ASP deal with Keystone adds further visibility to telecom product revenues; to start accruing from CY08.
- The continuing scale up in existing accounts is also positive.
- The services business consolidated into a separate SBU namely, BlueAlly.
- We maintain our CY07 EPS estimates at Rs.12 and target price at Rs.180. We recommend **BUY**.

Deal with Keystone Wireless

- Megasoft has announced that it has signed a multi-million dollar deal with the US-based mobile service provider Keystone Wireless.
- We understand that this US-based carrier will deploy the VOISE platform and also the other IN products of Megasoft on its network, for usage by the subscriber base of its clients, on an application service provider (ASP) basis. This will turn Keystone into a Mobile Virtual Network Enabler (MVNE).
- Keystone is an existing telecom service provider in the US and is foraying into providing ASP services to MVNOs.
- However, this agreement does not restrict Megasoft from approaching the US-based MVNOs directly for business.
- The company, on its part, has said it would look to replicate this model in Europe and in Asia to increase its client penetration for its suite of products.
- This ASP deal is expected to start bringing revenues to Megasoft from CY08, for a period of 24-30 months.
- The deal, according to the management, has a minimum guarantee component of close to \$5 mn across the contract tenor.
- The management is confident of garnering revenues of close to \$30-35 mn over the contract period, starting CY08E at margins similar to those currently enjoyed by the company in the telecom segment.
- Keystone has already started dialogues with several MVNOs and expects to sign a few of them in the near term.
- Further, Megasoft has also picked up a 5% stake in the US service provider for a consideration of \$5 mn.
- This will allow it to share future revenues of Keystone, which is also expected to attach the Xius brand to itself for all services provided by it in the MVNO space. This will further the brand building initiatives of Megasoft in the US.

Services business consolidated into BlueAlly

- Megasoft has consolidated its own services business and that of VisualSoft into a separate SBU - BlueAlly.
- BlueAlly will focus on providing end-to-end product development support with a view to reducing the time-to-market for its clients in various verticals.
- The business currently employs about 700 people and has net margins of about 12%.

VOISE: Expected to contribute significantly to telecom products

- During CY06, the company announced its first win for VOISE, in the form of the US-based XERO Mobile, a new entrant into the US MVNO space. Currently, the Xero network is in the beta stage and is expected to ramp up in terms of subscriber base from H2CY06. The XERO mobile network hopes to ramp up its nascent subscriber base to around 3 mn by the end of CY2007 (Source: Xero's website).
- VOISE revenues have started kicking in from Q2CY06 and are expected to scale up commensurately as and when Xero grows its subscriber base. We expect this deal to garner revenues of close to \$8.3 mn over the next two years. We feel there could be potential upsides to our revenue projections from Xero, based on their subscriber additions in the future.
- Including the engagement with Keystone, the current client base for the VOISE platform stands at six.
- We believe this client engagement with Keystone is not exclusive in nature from Megasoft's point of view and lets Megasoft approach other MVNOs/mobile operators for VOISE and its suite of telecom products. We feel there could be potential upsides to our revenue projections from this deal based on their subscriber additions for Keystone Wireless in future.
- Megasoft has also said that it is in talks with other mobile virtual network enablers (MVNEs)/MVNOs for its VOISE platform and hopes to close some more arrangements in the current financial.

Rollout of IN billing solutions for current accounts in progress

- Within the telecom vertical, Megasoft has been focusing on the network side (roaming products) as well as on the billing side (INfinet) of the business. These billing products are built on the company's proprietary WISE platform.
- We believe the company's rollouts for its billing solutions are progressing well in the African geography (Gamcel), West Asia and in India (Hutchison Essar). We believe these geographies enjoy strong growth rates in terms of mobile subscriber additions. Megasoft has a sizeable opportunity to scale up its revenues in line with subscriber additions made by service providers.

VisualSoft acquisition consummated

- The acquisition of VisualSoft has been consummated both from the financial and operational angles. New shares of Megasoft have already been issued to the erstwhile shareholders of VisualSoft.
- VisualSoft had close to 600 employees of which, nearly half were trained on telecom technologies. Megasoft has retrained a significant number of them and has already absorbed more than 100 employees in the Xius division.
- In our opinion, the recent deals won by Megasoft are more of enterprise deals, which involve implementation and integration services. The company will thus, be able to utilize the employees of VisualSoft in this process of implementation and integration of its own products at client sites.

Visual's assets could help finance planned acquisitions

- Also, VisualSoft had significant assets in Vishakhapatnam as well as at Madhapur (Hi-Tec City) in Hyderabad. Megasoft can utilize these assets, which are currently not revenue earning, for its planned acquisitions.
- According to our discussions with the management, a decision on the asset sale in Vishakhapatnam could be around the corner. The company is also developing a property in Madhapur. A part of this it plans to utilize for its own facility while a chunk will be available for commercial sale.
- The expected cash accruals out of VisualSoft's assets can provide Megasoft more financial muscle when it goes out for acquisitions in the telecom vertical. The management has indicated that it has narrowed down its search for companies in the telecom space, which can give it customer access and scale. Megasoft is looking to acquire only profit making entities.

Future prospects		
(Rs mn)	CY06	CY07E
Sales	1783.5	2983.9
Growth (%)	55	67
EBITDA	462.4	831.1
EBITDA margin (%)	25.9	27.9
Net profit	341.5	518.5
Net cash (debt)	348.6	512.0
EPS (Rs)*	7.7	11.7
Growth %	-2.5	51.9
CEPS	9.6	16.2
DPS (Rs)	3.0	4.0
ROE %	34.8	39.0
ROCE %	24.6	32.3
EV/Sales (x)	3.6	2.2
EV/EBITDA (x)	14.0	8.0
P/E (x)	17.9	11.8
P/Cash Earnings	14.4	8.5
P/BV (x)	4.9	4.3

Source: Company, Kotak Securities - Private Client Research

* The fully diluted equity is Rs.443 mn, which is post the amalgamation with VisualSoft (Rs.324 mn previously)

Our earnings estimates factor in the following changes in our assumptions:

- **Greater visibility in the telecom vertical:** We expect the telecom vertical to contribute close to Rs.1.2 bn in CY07 from the Rs.700 mn reported in CY06.
- Growth in telecom vertical is expected to be driven by the implementation of VOISE for clients like Xero Mobile in addition to healthy offtake in products like INfinet and Insta-Roam.
- We have assumed VisualSoft will contribute revenues of Rs.730 mn for CY07 in line with the current quarterly run rate. We believe Visual's contribution to profitability will be minimal; expect low profitability (3% @ EBITDA level) of Q1CY07, going ahead.

With an increasing proportion of the high margin telecom business, overall margins (23.5% for CY05 and 25.9% in CY06) are expected to improve, going forward. These are expected to be around 27.8% in CY07.

Valuations & recommendation

- We like Megasoft due to its positioning in the fast-growing telecom space and its active R&D facility. The company's strong R&D backbone has developed the 'first of its kind' VOISE platform in addition to other telecom software products.
- We believe the recent engagement with Keystone could add significantly to revenues from the VOISE platform.
- We expect the telecom products business to spur revenue and profit growth for Megasoft in CY07. The VisualSoft merger is also expected to provide a pool of trained telecom professionals for the company, in addition to adding significantly to the company's asset base.
- We maintain **BUY** on Megasoft with a price target of Rs.180, upside of 36% from current levels. At our target price of Rs.180, the stock will trade at 15x its consolidated CY07 earnings.

We maintain BUY on Megasoft with a price target of Rs.180 (upside 36%)

Concerns

- An accelerated slowdown/recession in major user economies can impact Megasoft.
- Appreciation of the rupee v/s the US dollar beyond our expectations can impact the revenue growth and profitability of Megasoft.

Bulk deals

Trade details of bulk deals					
Date	Scrip name	Name of client	Buy/ Sell	Quantity of shares	Avg. Price (Rs)
13-Jun	Ambika Coton	HSBC Global Investment Fund	S	30,000	126.85
13-Jun	AMD Metplast	Anand Yagesh Shares and Consult	B	500,000	56.53
13-Jun	AMD Metplast	Lotus Global Investments Limited	S	491,301	55.00
13-Jun	Autolite Ine	Gurmeet S Kaur	B	27,758	37.04
13-Jun	Chamatkar.Nt	Maruti Securities Ltd	B	200,000	23.00
13-Jun	Chamatkar.Nt	Sainath Herbal Care Marketing P Ltd	S	200,000	23.00
13-Jun	Dollex Indut	SPJ stockbroker	B	39,977	128.79
13-Jun	Gemstone Inv	Shantoshima Lease Finance and Inv	B	45,000	20.90
13-Jun	Gemstone Inv	Hemant Madhusudan Sheth	S	50,000	20.90
13-Jun	Gremac Infra	Lehman Brothers Asia Ltd Ac			
		LB India Holding Cayman Ii Ltd	B	500,000	146.00
13-Jun	Gremac Infra	Lotus Global Investments Limited	B	350,000	140.00
13-Jun	Gremac Infra	Anand Yagesh Shares and Consult	S	395,989	146.08
13-Jun	Kadamb Const	Somani Dinesh Bajranglal	B	15,000	22.10
13-Jun	Kadamb Const	K K Patel Finance Ltd	S	15,000	22.10
13-Jun	Kailash Fico	Mangilal Hiralal Jain	S	76,129	10.10
13-Jun	Kalptaru	Ashlesh Gunvantbhai Shah	B	43,132	82.25
13-Jun	Koff Br Pict	Vasant Meghji Chheda	B	73,738	27.85
13-Jun	Koff Br Pict	Maruti Baburao Jadhav	S	26,200	26.91
13-Jun	Koff Br Pict	Ketan R Asher	S	26,423	26.84
13-Jun	Koff Br Pict	Jignesh Chinubhai Shah	S	38,000	26.71
13-Jun	Nestle Ltd	Halbis Capital Management HK Ltd	S	750,531	1,200.00
13-Jun	Pasari Spin	Hardik M Mithani	S	69,614	14.42
13-Jun	Pasari Spin	Spjstockbroker	S	51,601	14.42
13-Jun	Rasoya Protn	Aditya Saraf	S	50,000	115.83
13-Jun	Sandur Man	IDBI Ltd	S	50,000	78.90
13-Jun	ShreePacetr	Own Leasing and Finance Pvt Ltd	B	32,497	31.00
13-Jun	Shri Bajrang	Vasant M Chheda HUF	S	135,412	39.25
13-Jun	TN Newsprint	Goldman Sachs Invests Mauritius I	B	1,327,998	95.00
13-Jun	TN Newsprint	Prudential ICICI MF Discovery	S	1,310,000	95.00
13-Jun	Time Techno	Deutsche India Equity Fund	B	350,000	480.40
13-Jun	Time Techno	Prudential ICICI Mutual Fund	B	150,000	470.33
13-Jun	Tripex Over	Shreeji Securities	S	50,000	33.16
13-Jun	Tripex Over	Rajiv Gautambhai Patel HUF	S	50,000	30.90
13-Jun	Visisth Merc	Nishivin Finance and Inves Pvt Ltd	S	4,000	20.55

Source: BSE

Gainers & Losers

Nifty Gainers & Losers				
	Price (Rs)	% change	Index points	Volume (mn)
Gainers				
Satyam Computers	486.8	1.7	1.0	4.9
DRL	627.7	2.7	0.5	1.1
Dabur India	101.6	2.1	0.3	1.0
Losers				
Reliance Ind	1,675	(1.4)	(6.4)	2.2
Reliance Com	486	(2.5)	(4.9)	3.3
SBI	1,290	(3.1)	(4.3)	1.5

Source: Bloomberg

Forthcoming events

COMPANY/MARKET	
Date	Event
14-Jun	Wipro Infotech holds press conference; GE Healthcare & Healthcare Global holds conference to tie-up; Samsung Telecommunications India holds press conference; Container Corp. of India to announce earnings and dividend; Tata Tele Services holds press conference.
15-Jun	Shipping Corporation of India to announce earnings; EIH Ltd to announce earnings and dividend; Yes Bank and Reuters jointly holds press conference; ICICI Bank holds press conference to announce public issue.
17-Jun	Cadila Healthcare to consider raising of fund overseas
18-22 Jun	Initial Public Offer of Celestial Labs opens
18-Jun	Tata Motors holds press conference in Pune to launch vehicles
22-Jun	Amara Raja Batteries to announce earnings and dividend; Infosys Technologies holds share holders meeting in Bangalore
25-Jun	Annual General Meeting of SBI
26-Jun	Apollo Hospitals enterprise to announce earnings and dividend
29-Jun	TCS holds annual shareholders meeting
30-Jun	Tata Tele Services, Colgate Palmolive to announce earnings and dividend; Tata Coffee and Castrol earnings expected

Source: Bloomberg

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