

10 March 2008

ACCUMULATEPrice
Rs 2,729Target Price
Rs4,381

Sensex - 15,924

Price Performance

(%)	1M	3M	6M	12M
Absolute	(33)	(36)	6	90
Rel. to Sensex	(18)	(16)	3	50

Source: Capitaline

Stock Details

Sector	Engineering
Reuters	LART.BO
Bloomberg	LT@IN
Equity Capital (Rs mn)	584
Face Value (Rs)	2
52 Week H/L	4,670/1,412
Market Cap (Rs bn)	797.0
Daily Avg Vol. (No of shares)	865400
Daily Avg Turnover (US\$m)	81.5

Shareholding Pattern (%)

Promoters	0.0
FII/NRI	24.0
Institutions	36.1
Private Corp.	3.6
Public	36.3

Source (31st Dec'07)

Source: Capitaline

Pritesh Chhedapritesh.chheda@emkayshare.com
+91-22-6612 1273**Larsen & Toubro**Event
Update**Commodity hedging losses blown out of proportion**

The Indian Equity Markets are abuzz with rumors and news on LNT- its 100% international subsidiary LNT FZE will report substantial losses on account of commodity trading and/or hedging transactions. The quantum is pegged at US\$100 Mn to US\$250 Mn as reported by media channels. We always knew about trading gains in commodity derivatives transactions during FY2007 and had already factored for its non-recurrence in earnings of consequent years. We spoke to the management of LNT to get specific inputs of above transaction and its impact on FY2008E-F2010E earnings estimates.

Brief background on LNT FZE

- LNT FZE is a holding company for all the international subsidiaries- mainly subsidiaries in Middle East and South East Asia.
- LNT FZE undertakes commodity hedging, equipment leasing and equipment rentals, besides holding investments in international subsidiary companies.
- The main revenue stream of LNT FZE (Standalone) is a) income from lease rental and b) income/loss from derivative transactions in commodity markets.
- LNT FZE has earned profits from commodity transactions for last two years. In FY2007 alone, LNT FZE earned Rs1.3 bn from commodity derivatives, significant portion in FY2007.

What has happened in LNT FZE?

LNT management has guided for a loss of Rs2.0-Rs2.5 bn on account of commodity derivative transactions. Considering the profits in FY2007, the incremental loss is calculated at Rs1.0 bn. The nature of commodity transactions is unknown, but we will not rule out possibility of speculative transactions as LNT is a net buyer of commodity (like Steel, Copper and Aluminum). Also in a rising commodity price scenario, hedging transactions undertaken by LNT should have a made trading profits in an ideal scenario.

We were always on defensive and were fully aware of trading profits in operations of international companies earned during FY2007. Accordingly, we had pegged the growth in international subsidiaries like LNT FZE at -3% in FY2008E with net profit of Rs0.75 bn. For our FY2008E earnings estimates, we had assumed a neutral scenario with no gains or losses on trading.

We believe that, commodity trading losses will impact the consolidated estimates of LNT to the tune of Rs1.0 bn. We believe that, the above transactions are ongoing business transactions, accurate forecasts are not possible. Also, LNT management has clarified that all commodity derivative transactions have been squared off, with no outstanding positions warranting any write-offs or provisioning.

Key Financials

YE-Mar	Net	EBITDA	EBITDA	PAT	EPS	EPS	ROCE	PE
(Rs. mn)	Sales		(%)		(Rs)	Growth %	%	(%)
FY2007	203,857	27,279	13.4	22,401	62.2	(18.8)	23.8	43.9
FY2008E	276,750	41,033	14.8	24,947	90.6	45.8	24.2	30.1
FY2009E	359,659	55,323	15.4	32,559	115.1	27.0	22.2	23.7
FY2010E	469,428	75,671	16.1	43,071	157.7	37.0	22.4	17.3

Breakdown of LNT Consolidated Earnings Estimates

In Rs Million		FY2006	FY2007	FY2008E	FY2009E	FY2010E
L&T Standalone		8651	13803	18538	23452	29111
	Growth	49%	60%	34%	27%	24%
L&T Infotech (100% Holding)		702	1511	1898	2378	3384
	Growth	53%	115%	26%	25%	42%
L&T Finance (100% Holding)		351	626	841	1126	1502
	Growth	46%	78%	34%	34%	33%
HPL Cogeneration (51% Holding)		971	845	876	975	975
	Growth	67%	-13%	4%	11%	0%
Tractors Engineers (100% Holding)		55	133	127	167	219
	Growth	-1%	143%	-5%	32%	31%
Property Business (L&T Urban IDPL)		53	236	3272	6308	12380
	Growth	NA	347%	1286%	93%	96%
Other Subsidiaries (In Conso)		-374	775	752	940	1175
	Growth	NA	NA	-3%	25%	25%
L&T Consolidated (Before Minority and Associate Profit/Loss)		10408	17930	26303	35344	48745
	Growth	45%	72%	47%	34%	38%

Other Subsidiaries includes the numbers of LNT FZE and its subsidiaries

Jump in net profit inw other subsidiaries was triggered by gain in commodity trading (Loss of Rs0.37 bn in FY2006 to Profit of Rs0.77 bn in FY2007

Net profit growth in other subsidiaries is pegged at -3% - we were already on defensive- Profit of Rs0.75 bn against Rs0.77 bn in FY2007

We always knew this— only 4% downward revision in FY2008E consolidated net profit

In a nutshell, the impact on account of losses in commodity derivatives is around Rs2.0-2.5 bn and incremental loss is approximately Rs1.0 bn, only at consolidated level.

LNT is extremely confident on the standalone numbers – (1) Robust order booking and (2) strong Ebitda margin expansions will trigger a better than expected (Higher than EMKAY and Consensus Estimates) earnings growth during FY2008E. We expect a 34% growth in net profit or Rs18.5 bn in FY2008E. The net profit for FY2009E and FY2010E is pegged at Rs23.4 bn and Rs29.1 bn with growth of 27% and 24% respectively.

The management believes that, consolidated earnings will get impacted by the losses incurred on account of commodity derivatives transactions. Also, higher interest and depreciation expenditure in subsidiary companies during FY2008E, will impact earnings. The management has not hedged its yen-payables (for its yen denominated bonds), hence in an appreciating yen versus dollar scenario, the net payables will increase substantially. This will trigger forex losses as seen in Q3FY2008, where gains of H1FY2008 were reversed completely.

Our ratings will not change by 4% downward revision in net profit

On rough-cut calculations, consolidated earnings are likely to get revised downwards by Rs1.0 bn or 4% in FY2008E. The negative impact on our earnings estimates is lesser (versus consensus), since we had already factored for trading gains in commodity transactions and probability of its occurrence. We have not revised our FY2009E and FY2010E earnings estimates. We shall review our price target after the release of FY2008E consolidated numbers. Also, 20% correction in stock price in recent trades

has upfront factored for any negative surprises from currency and commodity derivatives transactions.

Our ratings will depend on management stance

Our ratings for LNT will not change by revision in earnings estimates. But, we would closely watch the management stance and validation for above commodity trading transactions, leading to losses of Rs2.0 – Rs2.5 bn. We have not ruled out the possibility of speculative interests or nature behind such commodity derivatives transactions.

DISCLAIMER: This document is not for public distribution and has been furnished to you solely for your information and may not be reproduced or redistributed to any other person. The manner of circulation and distribution of this document may be restricted by law or regulation in certain countries, including the United States. Persons into whose possession this document may come are required to inform themselves of, and to observe, such restrictions. This material is for the personal information of the authorized recipient, and we are not soliciting any action based upon it. This report is not to be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. No person associated with Emkay Share & Stock Brokers Ltd is obligated to call or initiate contact with you for the purposes of elaborating or following up on the information contained in this document. The material is based upon information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied upon. Neither Emkay Share & Stock Brokers Ltd, nor any person connected with it, accepts any liability arising from the use of this document. The recipient of this material should rely on their own investigations and take their own professional advice. Opinions expressed are our current opinions as of the date appearing on this material only. While we endeavor to update on a reasonable basis the information discussed in this material, there may be regulatory, compliance, or other reasons that prevent us from doing so. Prospective investors and others are cautioned that any forward-looking statements are not predictions and may be subject to change without notice. We and our affiliates, officers, directors, and employees world wide, including persons involved in the preparation or issuance of this material may; (a) from time to time, have long or short positions in, and buy or sell the securities thereof, of company (ies) mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company (ies) discussed herein or may perform or seek to perform investment banking services for such company(ies) or act as advisor or lender / borrower to such company(ies) or have other potential conflict of interest with respect to any recommendation and related information and opinions. The same persons may have acted upon the information contained here. No part of this material may be duplicated in any form and/or redistributed without Emkay Share & Stock Brokers Ltd's prior written consent. No part of this document may be distributed in Canada or used by private customers in the United Kingdom. In so far as this report includes current or historical information, it is believed to be reliable, although its accuracy and completeness cannot be guaranteed.

Emkay Share and Stock Brokers Ltd.,
Paragon Center, Ground Floor, C-6
Pandurang Budhkar Marg, Worli, Mumbai – 400 013. , Tel no. 66121212. Fax: 66121299