DLF (DLF.BO)

Equity

Buy: Weak But Operationally A Better Quarter

- **1Q better than est.** – While revenues and profits were down 55% and 79% YoY respectively in 1QFY10, this was better than our est. 70-90% fall. EBITDA margins of 45% surprised positively, driven by part revenue recognition (Rs6bn) of its high margin SBM, Delhi project and rentals of Rs2bn. Interest costs were higher as capitalized assets started leasing – expected to trend lower as debt levels reduce.
- **Operationally a better qtr** – Construction activity picked up, with 42msf under construction (vs. 36.5msf in 4Q), particularly resi projects, and also delivered 1msf of comm. space. Pre-sales were healthy at ~2.5msf in the qtr, with good progress on non-core asset sales (raised Rs5bn). De-notified 5-SEZs as IT space demand muted – provides flexibility in asset portfolio, where enquiries are picking up.
- **Key conf call takeaways** — Mgmt recognized signs of revival, but still cautious on calling this a strong recovery. Focus remains on liquidity and de-leveraging – non core asset sales of Rs30bn in adv stages; reduced debt to Rs116bn (vs. Rs139bn in Mar-09) and targeting to cut to <Rs60bn by end-FY10. ~16msf of new launches expected shortly, with thrust on city centre/mid-income projects. Expects leasing mkts to pick-up in next 6-8mths; more upbeat on mall leasing.
- **DAL receivable worries largely addressed** — Receivables down to Rs26bn (vs. Rs49bn in Mar-09), and this could be lowered by another Rs5bn. Other events underway are: 1) De-Shaw likely to retain part investment, 2) DLF's stake in DAL still being deliberated, and 3) Potential DAL listing. Timings still uncertain.
- **Our best play** — While stock has outperformed the Sensex by 16% in the last 1-month it remains our best relative play in the sector on track record, asset-geographic mix, BS strength and valuations. Further, we see likely pick-up in leasing activity as a catalyst for the stock.

Buy/Low Risk	**1L**
Price (31 Jul 09)	Rs396.15
Target price	Rs464.00
Expected share price return	17.1%
Expected dividend yield	0.0%
Expected total return	**17.1%**
Market Cap	Rs672,343M
	US$13,932M

Price Performance (RIC: DLF.BO, BB: DLFU IN)

Statistical Abstract

Year to 31 Mar	Net Profit (RsM)	Diluted EPS (Rs)	EPS growth (%)	P/E (x)	P/B (x)	ROE (%)	Yield (%)
2007A	19,326	12.74	3.3	31.1	23.1	108.7	0.0
2008A	78,120	45.82	259.6	8.6	3.6	73.2	1.0
2009E	46,292	27.28	-40.5	14.5	2.9	22.0	0.0
2010E	20,084	11.83	-56.6	33.5	2.6	8.2	0.0
2011E	24,368	14.36	21.3	27.6	2.4	9.1	0.0

Source: Powered by dataCentral

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Fiscal year end 31-Mar	2007	2008	2009E	2010E	2011E
Valuation Ratios					
P/E adjusted (x)	31.1	8.6	14.5	33.5	27.6
P/E reported (x)	31.1	8.6	14.5	33.5	27.6
P/BV (x)	23.1	3.6	2.9	2.6	2.4
Dividend yield (%)	0.0	1.0	0.0	0.0	0.0
Per Share Data (Rs)					
EPS adjusted	12.74	45.82	27.28	11.83	14.36
EPS reported	12.74	45.82	27.28	11.83	14.36
BVPS	17.18	109.92	138.02	149.85	164.21
NAVps ordinary	na	na	na	na	na
DPS	0.01	4.00	0.00	0.00	0.00
Profit & Loss (RsM)					
Net operating income (NOI)	**15,949**	**100,148**	**59,472**	**33,603**	**40,684**
G&A expenses	-1,051	-2,998	-4,592	-4,821	-5,786
Other Operating items	-591	-636	-2,566	-2,910	-3,467
EBIT including associates	**14,307**	**96,514**	**52,315**	**25,871**	**31,432**
Non-oper./net int./except.	11,083	-636	1,394	908	1,059
Pre-tax profit	**25,389**	**95,878**	**53,708**	**26,779**	**32,491**
Tax	-6,052	-17,391	-7,115	-6,695	-8,123
Extraord./Min. Int./Pref. Div.	-11	-367	-302	0	0
Reported net income	**19,326**	**78,120**	**46,292**	**20,084**	**24,368**
Adjusted earnings	19,326	78,120	46,292	20,084	24,368
Adjusted EBIT	14,319	96,250	52,525	25,871	31,432
Adjusted EBITDA	14,897	97,151	54,881	28,781	34,898
Growth Rates (%)					
NOI	209.4	527.9	-40.6	-43.5	21.1
EBIT adjusted	225.7	572.2	-45.4	-50.7	21.5
EPS adjusted	3.3	259.6	-40.5	-56.6	21.3
Cash Flow (RsM)					
Operating cash flow	**-39,232**	**-26,960**	**-4,560**	**94,078**	**11,812**
Depreciation/amortization	578	901	2,355	2,910	3,467
Net working capital	-62,932	-105,815	-51,290	71,084	-16,022
Investing cash flow	**-19,136**	**-60,142**	**-42,020**	**6,522**	**-4,174**
Capital expenditure	-25,329	-47,678	-39,450	-3,478	-4,174
Acquisitions/disposals	0	0	0	0	0
Financing cash flow	**60,572**	**104,368**	**37,880**	**-93,580**	**-15,000**
Borrowings	58,007	23,177	41,890	-93,580	-15,000
Dividends paid	-18	-7,979	-4,010	0	0
Change in cash	**2,205**	**17,266**	**-8,700**	**7,020**	**-7,361**
Balance Sheet (RsM)					
Total assets	**181,237**	**396,065**	**494,240**	**433,624**	**432,473**
Cash & cash equivalent	4,155	21,421	11,980	19,000	11,639
Net fixed assets	41,851	100,031	137,160	137,728	138,435
Total liabilities	**145,596**	**195,287**	**240,860**	**160,160**	**134,641**
Total Debt	99,327	122,771	163,580	70,000	55,000
Shareholders' funds	**35,641**	**200,778**	**253,380**	**273,464**	**297,832**
Profitability/Solvency Ratios					
EBIT margin adjusted (%)	54.3	66.7	52.3	39.7	36.8
ROE adjusted (%)	108.7	73.2	22.0	8.2	9.1
ROA adjusted (%)	15.4	27.1	10.4	4.3	5.6
Net debt to equity (%)	267.0	50.5	59.8	18.6	14.6
Interest coverage (x)	4.8	31.3	15.4	11.2	25.4

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1QFY10 Results Beat Estimates

Figure 1. DLF — 1QFY10 Results Summary (RsM)

	4QFY09	1QFY10	1QFY09	YoY	QoQ	CIRA Comments
Net Sales	11,223	16,499	38,106	-57%	47%	Received Rs5bn from sale of non-core assets. Improvement in execution. Area under construction now 42m sq ft vs. 36.5m sq ft in 4QFY09
Operating Profit	1,546	7,441	23,445	-68%	381%	
OPMs	13.8%	45.1%	61.5%			Aims to maintain healthy margins through launch of city-centre residential projects
Interest	1,625	2,874	541	431%	77%	Interest cost to reduce going forward with repayment of debt from sale of non-core assets
Other Income	2,291	961	357	169%	-58%	
Depreciation	516	734	546	34%	42%	
PBT	1,695	4,794	22,715	-79%	183%	
PAT	1,697	3,801	18,948	-80%	124%	
Less: Minority Int	100	165	107			
Add: Share of Associates	-7	-6	-201			
PAT after Minority	1,591	3,960	18,855	-79%	149%	

Source: Company, Citi Investment Research and Analysis

DLF

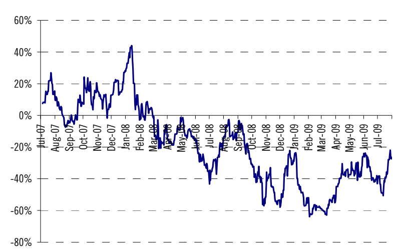
Company description

DLF is one of India's oldest real estate developers. Established in Delhi in 1946, it has continued to expand and diversify its real estate businesses, and is among the largest developers in India. It has historically built its businesses in Delhi and adjoining areas, known as the National Capital Region (NCR). DLF has diversified into other geographic locations over the past few years. These expansions are spread across India, with a focus on the Northern India belt, Kolkata, Mumbai, Chennai, and a number of other large and rapidly growing cities. DLF enjoys a strong brand franchise with a good track record in execution and delivery. This is the flagship company of the KP Singh family, with the founders holding a 78.6% stake. It is one of India's largest developers, with a diversified asset portfolio and an emerging pan-India presence.

Investment strategy

We rate DLF Buy/Low Risk (1L), with a target price of Rs464. DLF's proactive measures to address receivable worries, boost pre-sales by cutting prices/launching city centre projects along with steps to ensure liquidity has differentiated itself. Further, promoters bringing in additional capital to address liquidity concerns without dilution augur well and remove concerns about high receivables from DLF Assets (DAL). While risks to the company's business model are on the rise in this tough environment, given DLF's execution track record, growing rental income and geographic-asset mix, we believe it's strongly positioned vs. peers. We recommend a Buy rating for the stock and believe the stock should be a core holding for exposure to the Indian real estate sector.

Figure 2. DLF NAV Discount



Source: Citi Investment Research and Analysis

Figure 3. DLF Valuation Summary (RsM)

Gross NAV Residential	754,150
Gross NAV Non-Residential	417,435
Total Gross NAV	**1,171,585**
Less: Amt outstanding for land	2,540
Less: Tax @ 25%	292,261
Less: Debt outstanding	151,560
Less: Customer Advances	37,172
Add: Cash Balance	15,000
Add: Cash from DAL	35,000
Add: Cash from Sale of non-core assets	35,000
Net NAV	**773,052**
11m of existing owned/leased assets	85,800
7.2m sq ft in Plots	37,440
74% stake in Hotel JV - 13m sq ft	30,784
Total Value	927,076
No. of Shares Outstanding (m)	1,697
NAV Per Share (Rs)	**546**

Source: CIRA estimates

Valuation

Our target price of Rs464 is based on a 15% discount to our Mar'10 NAV of Rs546. Our NAV includes Rs455 for the development portfolio and Rs91 for other asset holdings and new JV businesses (Rs73/share for the existing 11m sq ft of leased assets and 7.2m sq ft of plots and Rs18/share for DLF's share in the hotel JV). The lower discount vs. peers (30-35%) is attributed to: 1) relatively healthy balance sheet vs. peers; 2) superior business model, strong execution track record; and 3) relatively better disclosure standards. We believe an NAV-based valuation methodology is most appropriate for developers, as it factors in the varied development projects and the spread-out time frame. Our March 2010E NAV is based on: 1) 20% decline in prices from peak levels; 2) development volume of 397msf ; 3) cap rate of 10% for commercial/IT Park, IT SEZs in Super Metros and Metros, and 11% for other locations; 4) average cost of capital of 13% given tight liquidity; and 5) a tax rate of 25%.

Risks

We rate DLF Low Risk since with the funds from recent stake sale by promoters being invested in DAL, visibility of DLF's cash flows improves substantially. The main downside risks to our investment thesis and target price include: 1) The company's asset sale strategy remains contingent on capital flows; 2) Response to DLF's new mid-income project launches in FY10 is crucial for growth ahead; 3) Slowdown in the IT/ITES industry could lead to a decline in demand for commercial real estate; and 4) Slowdown in capital inflows or measures to regulate FDI in the real estate sector.

Appendix A-1

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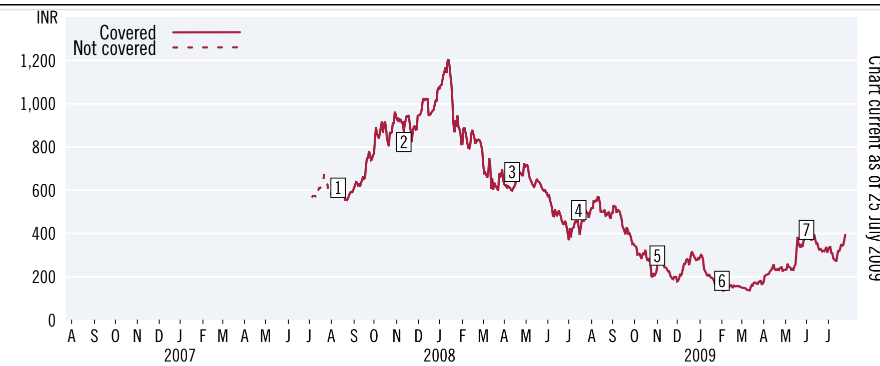
DLF (DLF.BO)

Ratings and Target Price History
Fundamental Research

Analyst: Ashish Jagnani
Covered since August 11 2007



	Date	Rating	Target Price	Closing Price
1	10-Aug-07	*1M	*725.00	584.45
2	12-Nov-07	1M	*1,046.00	871.20
3	11-Apr-08	1M	*846.00	598.00
4	15-Jul-08	1M	*585.00	426.95
5	2-Nov-08	1M	*340.00	220.25
6	1-Feb-09	1M	*240.00	177.20
7	1-Jun-09	*1L	*464.00	414.85

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

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