kotak Institutional Equities

INDIA DAILY

October 24, 2007

EQUITY MARKETS

India	23-Oct	Change, % 1-day	1-mo	3-mo
Sensex	18,493	5.0	9.8	17.1
Nifty	5,474	5.6	11.0	18.5
Global/Regional indices				
Dow Jones	13,676	0.8	(0.6)	(0.3)
Nasdaq Composite	2,799	1.6	4.9	6.0
FTSE	6,514	0.8	0.7	0.2
Nikkie	16,579	0.8	1.6	(7.9)
Hang Seng	29,866	1.7	12.5	27.2
KOSPI	1,992	2.3	3.8	(0.0)

Value traded - India

	23-Oct	Moving avg, Rs bn 1-mo	3-mo
Cash (NSE+BSE)	244.8	279.4	200.8
Derivatives (NSE)	714.5	759.3	510.1
Deri. open interest	972.9	943.4	927.5

Forex/money market

	23-Oct	Change, basis points 1-day	1-mo	3-mo
Rs/US$	39.6	1	(6)	(61)
6mo fwd prem, %	0.7	(25)	71	24
10yr govt bond, %	7.9	-	-	10

Net investment (US$mn)

	22-Oct	MTD	CYTD
FIIs	(300)	3,384	16,403
MFs	(82)	(972)	(291)

Top movers -3mo basis

Best performers	23-Oct	Change, % 1-day	1-mo	3-mo
Reliance Energy	1,523	11.2	39.3	96.5
Tata Power	1,059	6.2	27.3	55.0
Neyveli Lignite	121	7.1	14.4	49.8
Tata Tele	43	6.4	2.0	47.6
SAIL	237	10.9	19.4	47.1
Worst performers				
i-Flex	1,581	(0.2)	(14.7)	(32.5)
Punjab Tractors	218	2.1	(7.2)	(19.9)
Britannia	1,403	0.2	(5.5)	(18.4)
Container Corp	1,864	0.3	(14.5)	(17.4)
Glaxosmithkline	1,038	1.1	(7.2)	(16.9)

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- General Motors India is in the process of setting up a new facility to manufacture engine and transmission parts in the country. (BL)
- Dubai Holding, an investment firm of the Dubai government has threatened to come out with an open offer for Orient Express Hotels if the Tatas acquire a significant stake in the hotel chain. (BS)

Economic and political

- Worried over the substantial inflows of foreign funds into the real estate sector, the Reserve Bank has asked the government to allow FDI into the sector only after the clearance from Foreign Investment Promotion Board (FIPB). (ET)

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, BL = Business Line.

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Technology

SATY.BO, Rs462	
Rating	OP
Sector coverage view	Attractive
Target Price (Rs)	550
52W High -Low (Rs)	525 - 402
Market Cap (Rs bn)	309.8

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	64.9	83.2	106.2
Net Profit (Rs bn)	14.0	17.0	20.9
EPS (Rs)	21.4	25.4	31.1
EPS gth	*41.7*	*18.3*	*22.5*
P/E (x)	21.5	18.2	14.9
EV/EBITDA (x)	17.6	14.3	10.8
Div yield (%)	1.7	2.2	2.6

Shareholding, June 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	8.8	-	-
FIIs	67.4	3.1	2.1
MFs	5.9	1.6	0.6
UTI	-	-	(1.0)
LIC	1.5	0.4	(0.6)

Satyam Computer Services: On a roll. Maintain Outperform

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- **Outstanding revenue growth; pricing improvement is impressive**
- **Investments paying off, highest US$ revenue growth likely among peers in FY2008**
- **OPM performance is somewhat disappointing, can be managed through pricing**
- **Valuation gap to larger peers will likely narrow down; maintain OP**

Satyam's Sep '07 results (12.7% qoq US$ revenue growth) and FY2008 guidance (42% yoy revenue growth) was remarkably strong and reflects the rapid strides made by the company on execution, large deal strategy, maturity of service offerings and breadth of vertical capabilities. We expect the business momentum to continue and forecast strong growth in FY2009. We believe slippage in operating margin performance, while disappointing (qoq decline of 260 bps, FY2008 OPM guidance down to 175 bps from 125 bps earlier), is understandable in the context of the rupee appreciation and shift in revenue mix to onsite. In any case, we expect improvement in realization to compensate for relatively lesser levers to manage operating margin. We forecast EPS of Rs25.3 for FY2008 (guidance is Rs25.1), Rs31.1 for FY2009 and Rs32.8 for FY2010. Valuations, in our view, are attractive relative to our strong earnings growth forecast. We maintain our Outperform rating with an end-March DCF-based target price of Rs550/share.

Outstanding revenue growth; pricing improvement is impressive. Satyam outperformed its 2QFY08 US$ revenue growth guidance by 6.7% reporting 12.7% qoq revenue growth (US$ terms) to US$509.6 mn, 4.4% ahead of our expectation. Revenue growth was driven by both volumes (up 9.1% qoq) and pricing (up 2.2% onsite and 1.3% offshore). Revenues in Re terms grew 11% qoq to Rs20.3 bn. We note that the 12.7% qoq growth and 6.7% guidance outperformance are the highest for the company. Operating margin declined 260 bps qoq and 280 bps yoy to 19.8%. The margin decline is higher than our expectations. The company attributes the decline to (1) wage revision impact of 450 bps (2) rupee appreciation impact of 30 bps; and (3) onsite shift in revenues (impact of 70bps). Impact on account of these factors was offset by (1) lower visa costs of 110bps (2) price improvement of 120 bps and (3) other operational factors of 60 bps. Net income of Rs4.09 bn was 11% higher than our expectations and led by higher forex gain of Rs430 mn.

Investments paying off, highest US$ revenue growth likely among peers in FY2008: Satyam's investments in front end, domain experts, creation of strategic deals group and improvement in incentive structures appear to be paying off. The company has guided for 42% US$ revenue growth in FY2008, highest in the industry. It would be the fastest growing company in our coverage universe for FY2008. We once again highlight the likely growth drivers for the company in FY2008 and FY2009

a) **Reaping benefits through strategic deals group**: The pipeline in the strategic deals group has multiplied in the last twelve months. The company has announced several large deals over the past few months. Some of the recent deals announced include Reuters, a US$50 mn three year deal with Nestle and a US$100 mn multi-year deal with a large retail customer. More important, some of the large deals won by the company have made it to the Top10 list of clients. We note that the strategic deals group is focused on both large deals and conversion of existing relationships in large deals with committed revenues. This group owes part of the success to increasing maturity of some of the newer offerings including infrastructure management, BPO and engineering services.

b) **Sustaining strong positioning in the package implementation practice.** SAP in our view is a multi-year growth opportunity. Pipeline in the package implementation business continues to be strong and has improved further. Package implementation continues to be a high growth area for the industry; Satyam as a leader is better positioned than peers. Strong relationships with SAP, market share gains, investments in Netweaver platform and increasing participation in end-to-end implementations will likely contribute to strong growth. Package implementation practice has grown 14.3% qoq and 62.2% yoy in the Sep '07 quarter.

c) **New services offerings are getting acceptance:** While it is difficult to sustain growth on a qoq basis in all new service offerings, we believe that these offerings have gained critical mass and would be a critical element of growth. Satyam BPO has grown 26.8% in Sep' 07 quarter, Engineering services is also gaining traction; infact, Satyam highlights that it is now participating in standalone large deals in the engineering services space. Scale in IMS is improving, as the company executes on IMS work embedded in large deals. More important, we highlight that Satyam has signed some deals offering integrated services involving one or more of the new service offerings.

OPM performance is somewhat disappointing, can be managed through pricing: Satyam's OPM decline 260 bps qoq and 280 bps yoy to 19.8%. More important, the company has assumed OPM reduction of 175 bps in its FY2008 guidance as compared to 125 bps earlier. We attribute the negative surprise to one more year of above industry average wage revision (5% onsite and 16% offshore). We believe that the Satyam's onsite wages still continue to be lower than peers. However, this can be absorbed in our view through pricing improvements. Satyam has greater headroom for pricing given its higher concentration to hot skill areas and opportunity to correct historically lower pricing. Improvement on this front is visible in 2.2% qoq and 4.6% yoy onsite realization and 1.3% qoq and 3.7% yoy increase in offshore realization. We forecast 200 bps OPM decline in FY2008, 30 bps in FY2009 and 60 bps in FY2010.

Update on guidance: Emphasizing strong growth in core business, Satyam has raised US$ revenue growth guidance to 41.5-42%, from 34-35.5% earlier. The guidance implies a 5.9% sequential revenue growth in 4QFY08, robust in our view. The full year revenue guidance is the highest in the industry. The company has also increased US$ EPS growth guidance to 36% from 29.5% earlier and its Re EPS growth guidance to 17% (Rs25.1 FY2008 EPS) from 14% earlier. The guidance is based on a Re/ US$ rate of 39.5 (Re 40.5 earlier); this factors in 12.5% appreciation in rupee in FY2008 over FY2007 average. For 3QFY08, Satyam has guided for 6.1% US$ revenue growth and 4.1% rupee revenue growth. The company needs to achieve 5.9% US$ revenue growth and 14.2% Re EPS growth in 4QFY08 to achieve its FY2008 guidance.

Acquisition of Nitor and buy out of stake of private equity players in the BPO subsidiary: Satyam reached a definitive agreement to acquire UK-based Nitor Global Solutions for a consideration upto GBP 2.76 mn in an all cash deal. Nitor is a niche infrastructure management services firm that helps clients design, implement and manage Microsoft technologies and will strengthen Satyam's growing IMS practice. The company has 20 consultants, 10 important relationships and annual revenue of US$3 mn. Satyam also bought out the stake held by Olympus BPO Holdings Ltd and Nipuna's employees in Nipuna, Satyam's BPO subsidiary, for a total consideration of Rs1.5 bn.

Revising estimates. We are revising our FY2008 revenue growth forecast to US$2.09 bn (43% growth), FY2009 to US$2.73 bn (31% growth) and FY2010 to US$3.38 bn (25% growth). We are lowering our OPM forecast to build in further appreciation of the rupee; we now assume Re/US$ rate 39 for FY2009, 38 for FY2010 and a further appreciation of 1% in the subsequent years. As a result we reduce our FY2009 EPS estimate by 1.4% to Rs31.1 and FY2010 EPS estimate by 1.7% to Rs32.8. Maintain OP with an end-March 2009 DCF-based target price of Rs550/share.

Revision in FY2008 guidance and 2QFY08 performance versus actuals

FY2008 (Revised versus earlier)	Revised		Earlier (end of 1QFY08)	
	Lower end	Upper end	Lower end	Upper end
Revenues (US$ mn)	2,067.7	2,075.6	1,958.0	1,980.0
Growth yoy (%)	**41.5**	**42.0**	**34.0**	**35.5**
Revenues (Rs bn)	81.9	82.2	78.5	79.4
Growth yoy (%)	26.3	26.7	21.1	22.5
EPS (Rs) (a)	25.0	25.1	24.14	24.46
Growth yoy (%)	16.5	17.0	12.5	14.0
EPADS (US$)	1.24	1.24	1.17	1.19
Growth yoy (%)	36.0	36.0	28.3	29.7
Re/US$ rate		39.5		40.5

Source: Company reports

Sequential revenue growth and guidance outperformance were the highest for the company

Guidance and actual revenues, 2QFY06-2QFY08

	2QFY06	3QFY06	4QFY06	1QFY07	2QFY07	3QFY07	4QFY07	1QFY08	2QFY08
Revenues (US$ mn)									
Guidance	259	280	299	310	339	373	395	434	479
Actual	268	282	301	323	352	376	411	452	510
Growth qoq (%)									
Guidance	5.2	4.5	6.0	3.1	5.0	6.1	5.1	5.6	6.0
Actual	8.9	5.2	6.7	7.2	9.1	6.7	9.4	10.0	12.7
Outperformance (% pts)	**3.6**	**0.7**	**0.7**	**4.2**	**4.2**	**0.6**	**4.3**	**4.5**	**6.7**

Note:
(a) Consolidated US GAAP guidance and actuals

Source: Company, Kotak Institutional Equities estimates

Satyam's large deal focus has resulted in some significant deal wins

List of large deals annouced by Satyam in the past 24 months

Deal	Size (US$ mn)	Country
GM	150	North America
Nissan	100	North America
Qantas	54	Australia
Applied Materials	200	North America
Nestle	75	Switzerland
Large retailer	100	
Reuters (a)		UK

Note:
(a) As a sub-contractor to Fujitsu

Source: Company reports, Kotak Institutional Equities estimates

Traction in enterprise solutions practice remains strong
Satyam's revenues from package implementation practice

	1QFY06	2QFY06	3QFY06	4QFY06	1QFY07	2QFY07	3QFY07	4QFY07	1QFY08	2QFY09
Revenues (US$ mn)	88.8	100.4	106.2	111.4	121.8	134.3	150.4	166.0	190.6	217.9
% of revenues	37.4	39.4	39.4	39.3	40.3	40.4	42.0	42.6	44.2	45.0
Growth qoq (%)	13.9	13.1	5.7	4.9	9.3	10.3	12.0	10.4	14.8	14.3
Growth yoy (%)	**59.4**	**54.0**	**50.1**	**43.0**	**37.2**	**33.8**	**41.7**	**49.0**	**56.5**	**62.2**

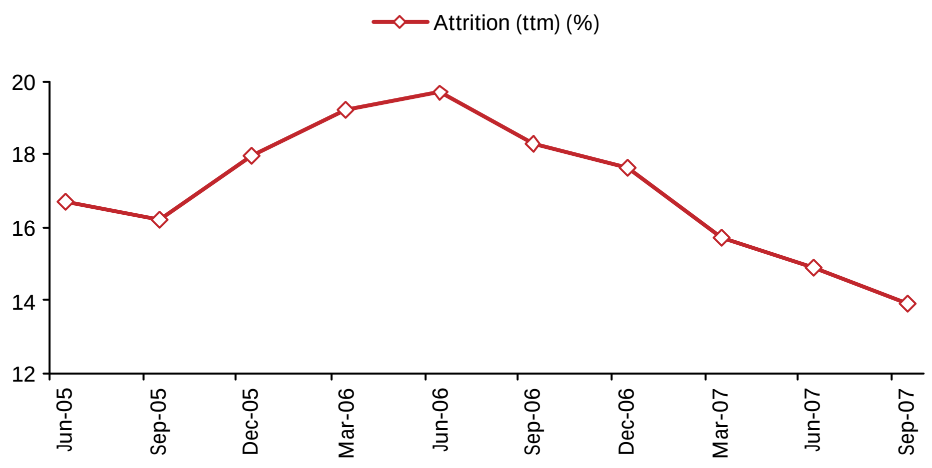
Source: Company, Kotak Institutional Equities

Positive trend in pricing continues both onsite and offshore; pricing remains the key to margin performance going forward
Satyam's onsite and offshore realizations (US$/ hr), 2QFY06-2QFY08

Per capita revenue productivity	Sep-05	Dec-05	Mar-06	Jun-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07
Onsite (US$/ hr)	55.8	55.9	55.9	56.1	56.2	56.4	56.8	57.5	58.8
Offshore (US$/ hr)	23.0	23.0	23.0	23.0	23.1	23.2	23.3	23.7	24.0
Growth qoq (%)									
Onsite	0.1	0.1	0.1	0.3	0.2	0.4	**0.6**	**1.3**	**2.2**
Offshore	0.2	0.0	0.1	0.2	0.4	0.1	**0.7**	**1.5**	**1.3**
Growth yoy (%)									
Onsite	0.4	0.5	0.4	0.6	0.7	1.0	**1.5**	**2.6**	**4.6**
Offshore	0.5	0.5	0.5	0.5	0.8	0.9	**1.5**	**2.8**	**3.7**

Source: Company reports

Satyam's attrition rates have been declining for the past four quarters



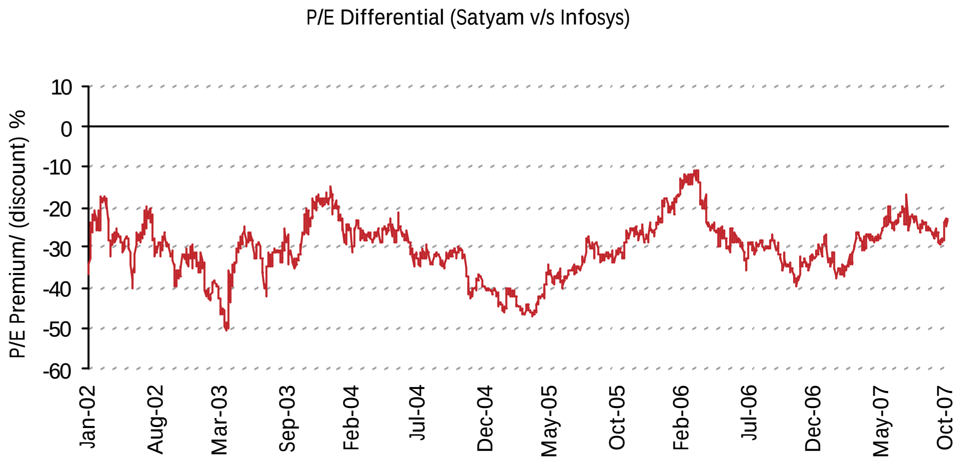
Source: Company

Nipuna posted strong revenue growth in Sep '07 quarter; Satyam has guided for US$60 mn revenues for Nipuna in FY2008

	1QFY06	2QFY06	3QFY06	4QFY06	1QFY07	2QFY07	3QFY07	4QFY07	1QFY08	2QFY08
Revenues (Rs mn)	145	182	221	338	364	416	434	503	487	609
Revenue (US$ mn)	3.3	4.2	4.9	7.6	7.9	9.0	9.7	11.5	11.9	15.1
US$ growth qoq (%)	1.9	25.8	17.1	56.8	4.1	13.4	8.3	17.8	4.0	26.8
US$ growth yoy (%)	**112.9**	**72.9**	**74.8**	**135.2**	**140.3**	**116.6**	**100.4**	**50.6**	**50.4**	**68.2**

Source: Company reports

We expect Satyam's P/E discount to Infosys to narrow down



Source: Bloomberg, Kotak Institutional Equities estimates

Key changes in FY2008-10 estimates

	Revised			Earlier			Change (%)		
Rs mn	FY2008E	FY2009E	FY2010E	FY2008E	FY2009E	FY2010E	FY2008	FY2009	FY2010
STANDALONE									
Revenues	**79,680**	**101,432**	**122,074**	**78,460**	**100,112**	**122,199**	**1.6**	**1.3**	**(0.1)**
EBITDA	17,937	22,113	25,436	18,218	22,485	26,143	(1.5)	(1.7)	(2.7)
Depreciation	(1,443)	(1,916)	(2,377)	(1,469)	(1,910)	(2,379)	(1.7)	0.3	(0.1)
EBIT	16,493	20,197	23,059	16,749	20,575	23,764	(1.5)	(1.8)	(3.0)
Net Profit	**17,200**	**20,570**	**21,212**	**17,141**	**20,780**	**21,625**	**0.3**	**(1.0)**	**(1.9)**
EPS (Rs/ share)	**25.6**	**30.7**	**31.6**	**25.5**	**31.0**	**32.2**	**0.3**	**(1.0)**	**(1.9)**
Revenue (US$ mn)	**2,000**	**2,603**	**3,216**	**1,936**	**2,502**	**3,054**	**3.3**	**4.0**	**5.3**
Revenue Mix (%)									
Onsite	49	49	48	48	49	49			
Offshore	51	51	52	52	51	51			
Volumes growth (%)	39.9	28.2	22.8	37.3	26.8	21.3			
Re/US$ rate	**39.8**	**39.0**	**38.0**	**40.5**	**40.0**	**40.0**	**(1.7)**	**(2.6)**	**(5.1)**
CONSOLIDATED									
Revenues (US$ mn)	**2,087**	**2,726**	**3,377**	**2,017**	**2,614**	**3,197**	**3.5**	**4.3**	**5.6**
Revenues	**83,155**	**106,225**	**128,199**	**81,758**	**104,603**	**127,943**	**1.7**	**1.6**	**0.2**
EBITDA	18,074	22,736	26,723	18,310	23,159	27,349	(1.3)	(1.8)	(2.3)
EPS (Rs/ share)	**25.4**	**31.1**	**32.8**	**25.3**	**31.5**	**33.4**	**0.3**	**(1.4)**	**(1.7)**
EBITDA margin	**21.7**	**21.4**	**20.8**	**22.4**	**22.1**	**21.4**			

Source: Kotak Institutional Equities Estimates

Satyam Computer Services- Comments on consolidated 2QFY08 results

Rs mn	2QFY07	1QFY08	2QFY08	QoQ % chg.	YoY % chg.	Kotak Estimates	% Deviation	Comments on QoQ performance
Revenues	**16,019**	**18,302**	**20,317**	**11.0**	**26.8**	**19,455**	**4.4**	US$ revenue growth of 12.4% qoq (6.4% ahead of guidance and 4.1% ahead of our expectation of 8.3%) driven by volume increase of 9.1% and realization improvements of 2.2% onsite and 1.3% offshore. Growth in Re terms at 11% on account of 1.3% appreciation in Re/US$ rate
Personnel Expenses	(9,827)	(11,062)	(13,028)	17.8	32.6	(12,367)	5.3	
Administrative Expenses	(2,567)	(3,137)	(3,263)	4.0	27.1	(3,152)	3.5	
Total Expenses	(12,394)	(14,199)	(16,290)	14.7	31.4	(15,519)	5.0	
EBITDA	**3,625**	**4,103**	**4,027**	(1.8)	11.1	**3,936**	**2.3**	EBITDA margin decline of 260bps higher than our expectations of a 220bps decline. Wage hikes, onsite shift in revenues and rupee appreciation led to the decline in margins. Margin pressure was partly mitigated by improved realizations, both onsite and offshore
Depreciation	(375)	(387)	(391)	1.0	4.1	(410)	(4.6)	
EBIT	**3,250**	**3,716**	**3,636**	(2.1)	11.9	**3,527**	**3.1**	
Interest	(27)	(33)	(41)			-		
Other Income	282	632	1,105	74.8	291.3	692	59.5	Forex gains of Rs430 mn versus previous quarter's loss of Rs50 mn.
Profit Before Tax	3,505	4,315	4,700	8.9	34.1	4,219	11.4	
Provision for Tax	(307)	(532)	(609)	14.6	98.5	(528)	15.3	Tax rates in line with expectations
Net Profit	**3,198**	**3,783**	**4,091**	**8.1**	27.9	**3,691**	**10.8**	
Income from associates	-	-	-			-		
Net Profit- Reported	**3,198**	**3,783**	**4,091**	**8.1**	**27.9**	**3,691**	**10.8**	Net income 11% above our expectations on the back of higher than expected revenue growth and gains
EPS (Rs/ share)	4.90	5.66	6.12	8.1	25.0	5.5	10.9	
Margins (%)								
OPM	22.6	22.4	19.8			20.2		
EBIT	20.3	20.3	17.9			18.1		
Net income	20.0	20.7	20.1			19.0		
As % of revenues								
Staff Cost	61.3	60.4	64.1			63.6		
Other Expenses	16.0	17.1	16.1			16.2		
Billing Rates/ hr (US$)								
Onsite	56.2	57.5	58.8	2.2	4.6	58.2		
Offshore	23.1	23.7	24.0	1.3	3.7	24.0		
Revenues from GE (Rs mn)	1,027.2	995.6	1,131.9	13.7	10.2	-		
Total Employees (standalone)	31,659	38,836	41,423	6.7	30.8	-		3,037 employees added during the quarter including 1,889 trainees

Guidance (consolidated)	**3QFY08**		**FY2008**		
	Lower end	**Upper End**	**Lower end**	**Upper End**	
Revenues (Rs mn)	**21,045**	**21,145**	**81,890**	**82,200**	FY2008 revenue growth guidance revised to 41.5-42% from 34-35.5% in US$ terms (our expectation was a revision to 38% at the upper-end); revised in Re terms to 26.7% from 22.5% at the upper band
Growth (%)	3.6	4.1	26.3	26.7	3QFY08 revenue growth guidance of 5.6-6.1% in US$ terms to US$538-541 mn
					Guidance factors in a Re/ US$ rate of 39.5 versus 40.5 earlier
Revenues (US$ mn)	**538.0**	**540.6**	**2,068**	**2,076**	
Growth (%)	5.6	6.1	41.5	42.0	
EPS	*6.18*	*6.21*	*25.00*	*25.10*	Re EPS growth guidance revised upwards to 16.5-17% from 12.5-14% earlier
Growth (%)	0.9	1.4	16.5	17.0	

Source: Company, Kotak Institutional Equities

Satyam- Consolidated Indian GAAP Income Statement, Fiscal year ends March (Rs mn)

Rs mn	2004	2006	2007	2008E	2009E	2010E
Revenues	**25,605**	**47,926**	**64,851**	**83,155**	**106,225**	**128,199**
Personel Expenses	(13,455)	(28,053)	(38,602)	(51,650)	(66,212)	(81,175)
Administrative Expenses	(5,377)	(8,212)	(10,872)	(13,430)	(17,277)	(20,302)
Total Operating Expenses	(18,832)	(36,265)	(49,474)	(65,080)	(83,489)	(101,477)
Operating Profits	**6,773**	**11,661**	**15,377**	**18,074**	**22,736**	**26,723**
Depreciation	(1,188)	(1,373)	(1,484)	(1,707)	(2,239)	(2,790)
EBIT	**5,585**	**10,289**	**13,893**	**16,367**	**20,497**	**23,933**
Interest	(10)	(55)	(159)	(74)	—	—
Other Income	751	1,168	1,833	3,193	3,413	3,730
Profit Before Tax	**6,326**	**11,401**	**15,566**	**19,485**	**23,910**	**27,662**
Provision for Tax	(1,063)	(1,509)	(1,520)	(2,460)	(3,053)	(5,628)
Net Profit	**5,263**	**9,892**	**14,046**	**17,026**	**20,857**	**22,034**
Share of loss in associate company	(129)	(73)	1	—	—	—
Net Income	**5,134**	**9,819**	**14,047**	**17,026**	**20,857**	**22,034**
Extraordinaries	—	1,598	—	—	—	—
Net Profit- Reported	**5,134**	**11,417**	**14,047**	**17,026**	**20,857**	**22,034**
EPS (Rs/ share)	**8.1**	**15.1**	**21.4**	**25.4**	**31.1**	**32.8**
Margins (%)						
EBITDA Margin	26.5	24.3	23.7	21.7	21.4	20.8
EBIT Margin	21.8	21.5	21.4	19.7	19.3	18.7
NPM	20.0	20.2	21.1	19.7	19.0	16.7
Growth Rates (%)						
Revenues		36.1	35.3	28.2	27.7	20.7
EBITDA		34.3	31.9	17.5	25.8	17.5
EBIT		36.7	35.0	17.8	25.2	16.8
Net Profit		37.2	42.0	21.2	22.5	5.6

Source: Kotak Institutional Equities estimates

Media

ZEE.BO, Rs339	
Rating	U
Sector coverage view	Cautious
Target Price (Rs)	260
52W High -Low (Rs)	363 - 186
Market Cap (Rs bn)	146.9

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	15.2	17.2	19.4
Net Profit (Rs bn)	2.4	3.6	5.1
EPS (Rs)	5.5	8.3	11.8
EPS gth	*11.2*	*52.0*	*41.7*
P/E (x)	62.1	40.8	28.8
EV/EBITDA (x)	46.5	26.6	19.4
Div yield (%)	0.4	0.6	0.8

Shareholding, June 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	43.2	-	-
FIIs	30.3	0.6	0.2
MFs	10.8	1.2	0.8
UTI	-	-	(0.4)
LIC	4.8	0.5	0.1

Zee Entertainment Enterprises: In-line results but line items somewhat disappointing

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- **Lower costs (qoq and versus expectations) helped overcome weak qoq (1.8%) revenue growth**
- **Subscription revenues continue to struggle; cut subscription revenues, fine-tuned earnings**
- **Find valuations expensive despite strong projected growth in earnings**

ZEEL reported 2QFY08 net income at Rs925 mn versus our expected Rs959 mn and EBITDA at Rs1.32 bn versus our estimated Rs1.46 bn. The negative variance reflects weaker-than-expected revenues, which grew 1.8% qoq only to Rs4 bn versus our expected Rs4.2 bn. In particular, subscription revenues struggled (-3.3% qoq) with domestic pay-TV revenues rising a modest 2.8% and overseas subscription revenues declining 8.3%. Higher other income and lower interest and depreciation expenses made up for the weaker-than-expected revenues and EBITDA. We have fine-tuned our FY2008E, FY2009E and FY2010E EPS to Rs8.3, Rs11.8 and Rs15 from Rs8.4 and Rs11.8 and Rs14.7, respectively, previously. Our 12-month DCF-based target price is Rs260 (Rs250 previously) and we find it hard to justify ZEEL's valuation without making more aggressive assumptions on revenues. As of now, we see potential downside risks to our estimates given (1) entry of several new players in broadcasting and (2) limited progress on addressable systems in India.

Key highlights of 2QFY08 results

20% qoq increase in net income. ZEEL's 2QFY08 EBITDA grew 10.4% qoq to Rs1.32 bn reflecting savings in costs (2%) and modest revenue growth (1.8%). However, higher other income and steep decline in interest expense (28%) and depreciation (17%) contributed to a 20% qoq increase in net income. We note that 2QFY07 results were pulled down by large cricket-related losses; as such, yoy comparisons are not very meaningful.

Subscription revenues declined 3.3% qoq despite the higher number of paying subs; overseas revenues disappointed again. ZEEL's 2QFY08 subscription revenues declined 3.3% qoq to Rs1.63 bn (+10.2% yoy), which we find disappointing. Domestic pay-TV revenues increased a modest 2.8% qoq to Rs775 mn despite higher number of DTH paying subs. We continue to be surprised by the sluggish pace of growth in domestic pay-TV revenues given the strong pick-up in the number of DTH subscribers. Overseas subscription revenues declined 8.3% qoq to Rs850 mn, the second quarter of successive decline. The decline is more than can be explained by the appreciation in the rupee and may be a cause for concern, in our view.

Ad revenues increased 7.4% qoq, which is a tad lower versus expectations. ZEEL's ad revenues increased 7.4% qoq to Rs2.2 bn, which reflects improved ratings in 2QFY08; the modest qoq growth despite strong improvement in ratings reflects one-off revenues from telecast of *Zee Cine Awards* program in early 1QFY08. We note that ZTV's ratings were helped by the telecast of the final rounds of a blockbuster program (talent show) as shown in Exhibit 2. ZEEL's ad revenues have increased 28% yoy but this reflects one-off revenues in 2QFY07 due to telecast of cricket matches.

2% qoq decline in operating costs helped compensate for weaker-than-expected revenues. ZEEL's employee costs declined 10% qoq to Rs338 mn, which reflects incentives paid in 1QFY08. SG&A expense declined by 12% qoq to Rs668 mn; we believe this reflects lower marketing expenses although the management did not give a specific reason for the same.

Subsidiaries have done better in 2QFY08. ZEEL's consolidated PBT increased Rs180 mn qoq but its standalone PBT increased just Rs71 mn, suggesting that profitability of subsidiaries improved significantly in the quarter (see Exhibit 3). We are pleasantly surprised by this change since international subscription revenues, a key component of subsidiary businesses, declined qoq in 2QFY08.

Earnings revisions

We discuss below the changes and key assumptions behind our ZEEL earnings model.

1. **Advertisement revenues.** We have fine-tuned FY2008E ad revenues to Rs9.2 bn (+31% yoy) from Rs9.4 bn previously. 1HFY08 ad revenues increased 36.3% yoy but we expect the growth to slow down in subsequent quarters given higher base in 2HFY07; note 1QFY08 yoy growth was 47% and 2QFY08 28%. The performance of ZTV had improved strongly from 2HFY07, which reflected in improved ad revenues in 2HFY07. For FY2009E and FY2010E, we model ad revenues at Rs10.5 bn and Rs12 bn, virtually unchanged. The key issue would be ZEEL's ability to sustain the extant high market share of ZTV (32% in prime time), once three new general entertainment channels start operations over the next few months. We model ZEEL's ad revenues to grow 13% in FY2009E in line with market growth but this would depend on ZTV sustaining its high market share.

2. **Domestic-pay TV subscription revenues.** We have cut FY2008E domestic pay-TV revenues to Rs3.43 bn from Rs3.68 bn previously noting the sluggish pace of growth in ZEEL's domestic pay-TV revenues. ZEEL's 1HFY08 domestic pay-TV revenues were Rs1.53 bn (+24% yoy). We have reduced this figure from Rs4 bn since the beginning of the year, which shows that the then optimism regarding rollout of CAS and its favorable impact on domestic pay-TV revenues has not really played out. We have reduced our domestic pay-TV revenue forecasts in the future years but still assume pay-TV revenues to increase 23% and 27% in FY2009E and FY2010E, respectively to Rs4.2 bn (Rs4.6 bn previously) and Rs5.3 bn (Rs5.7 bn), respectively.

   The key would be (1) pace of implementation of a CAS on cable in India (mandatory or voluntary) or (2) ARPUs in DTH, which continue to be surprisingly depressed; Dish's ARPUs continue to be very low and we suspect the entry of new entrants may result in low ARPUs continuing for some time even through the number of subscribers may explode. From the perspective of broadcasters, low ARPUs would lead to likely lower revenues (for content) for broadcasters.

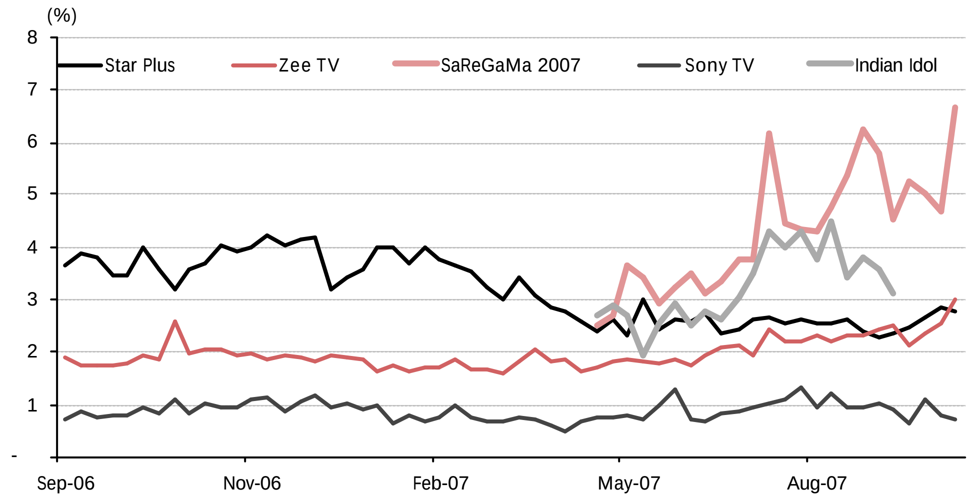
3. **International subscription revenues.** We have reduced FY2008E international subscription revenues to Rs3.8 bn from Rs4.2 bn on the back of (1) stronger rupee and (2) weak 1HFY08 reported revenues (Rs1.78 bn). For FY2009E and FY2010E, we have reduced international subscription revenues to Rs4 bn and Rs4.2 bn, respectively, from Rs4.4 bn and Rs4.5 bn previously.

Zee Entertainment (ZEEL) consolidated interim results, March fiscal year-ends (Rs mn)

		qoq			yoy			yoy		
	2008E	2Q 2008	1Q 2008	*% chg.*	2Q 2008	2Q 2007	*% chg.*	1H 2008	1H 2007	% chg.
Net sales	**17,178**	**3,986**	**3,916**	***1.8***	**3,986**	**3,496**	***14.0***	**7,902**	**6,391**	**24**
Advertisement revenues	9,236	2,195	2,044	*7.4*	2,195	1,717	*27.8*	4,239	3,109	36
Subscription revenues	7,243	1,625	1,681	*(3.3)*	1,625	1,474	*10.2*	3,306	2,801	18
Domestic pay-TV	3,430	775	754	*2.8*	775	—		1,529	1,234	24
International	3,813	850	927	*(8.3)*	850	—		1,777	1,567	13
Other sales	700	166	191	*(12.9)*	166	305	*(45.5)*	358	480	(26)
Total expenditure	**(11,684)**	**(2,665)**	**(2,719)**	***(2.0)***	**(2,665)**	**(3,279)**	***(18.7)***	**(5,384)**	**(5,512)**	**(2)**
Transmission and programming cost	(7,511)	(1,660)	(1,585)	*4.7*	(1,660)	(2,403)	*(30.9)*	(3,245)	(4,001)	(19)
Staff cost	(1,395)	(338)	(375)	*(10.0)*	(338)	(239)	*41.0*	(712)	(484)	47
Administrative & other costs	(2,778)	(668)	(759)	*(12.0)*	(668)	(636)	*5.0*	(1,427)	(1,027)	39
EBITDA	**5,495**	**1,321**	**1,197**	***10.4***	**1,321**	**217**	***507.5***	**2,518**	**879**	**186**
EBITDA margin (%)	**32.0**	**33.1**	**30.6**		**33.1**	**6.2**		**31.9**	**13.8**	
Other income	849	225	213	*5.5*	225	152	*48.3*	438	298	47
Interest	(365)	(85)	(118)	*(28.1)*	(85)	(34)	*147.8*	(203)	(143)	42
Depreciation	(252)	(55)	(67)	*(16.7)*	(55)	(51)	*8.8*	(122)	(103)	19
Pretax profits	**5,727**	**1,405**	**1,225**	***14.7***	**1,405**	**284**	***395.3***	**2,630**	**932**	**182**
Extraordinaries	—	—	—		—	—		—	—	—
Tax	(1,916)	(435)	(412)	*5.4*	(435)	(74)	*490.4*	(847)	(182)	364
Net income	**3,812**	**971**	**813**	***19.4***	**971**	**210**	***362.0***	**1,783**	**749**	**138**
Minority interest	(206)	(46)	(42)		(46)	12		(88)	(33)	
Net income after minority interest	**3,606**	**925**	**771**	***20.0***	**925**	**222**	***316.1***	**1,696**	**716**	**137**
Tax rate (%)	33.4	30.9	33.7		30.9	25.9		32.2	19.6	

Source: Kotak Institutional Equities estimates.

Talent show *'SaReGaMa 2007 challenge* ' has been the driver of Zee TV's resurgance in recent times
Prime time (7:30-11:30 PM) ratings for Hindi general entertainment channels and programs (%)



Source: TAM Media Research, compiled by Kotak Institutional Equities.

ZEEL "rest" tax rate has declined sharply

Key financials of ZEEL, consolidated and standalone (Rs mn)

	ZEEL consolidated			ZEEL standalone			ZEEL "rest"		
	2QFY08	1QFY08	1HFY08	2QFY08	1QFY08	1HFY08	2QFY08	1QFY08	1HFY08
Revenues	**3,986**	**3,916**	**7,902**	**2,291**	**2,244**	**4,535**	**1,695**	**1,671**	**3,367**
EBITDA	1,321	1,197	2,518	942	879	1,821	379	317	697
EBITDA margin (%)	**33.1**	**30.6**	**31.9**	**41.1**	**39.2**	**40.2**	**22.4**	**19.0**	**20.7**
Pre-tax profits	1,405	1,225	2,630	1,050	979	2,029	355	246	601
Tax	435	412	847	353	338	691	81	74	156
Net income	**971**	**813**	**1,783**	**696**	**641**	**1,338**	**274**	**171**	**446**
Tax rate (%)	**30.9**	**33.7**	**32.2**	**33.7**	**34.5**	**34.1**	**22.8**	**30.3**	**25.9**

Note:
(a) ZEEL "rest" comprises overseas operations primarily.

Source: Company data.

Our DCF-based valuation of ZEEL is Rs260

DCF analysis for ZEEL (Rs mn)

	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E
EBITDA	**5,495**	**7,397**	**9,393**	**11,555**	**13,530**	**15,288**	**16,802**	**18,270**	**19,714**	**21,112**
Tax expense	(2,034)	(2,663)	(3,404)	(4,197)	(5,005)	(5,758)	(6,420)	(7,081)	(7,748)	(8,478)
Changes in working capital	329	(1,078)	(1,178)	(1,245)	(1,264)	(1,234)	(1,137)	(1,135)	(1,166)	(1,197)
Cash flow from operations	**3,789**	**3,656**	**4,812**	**6,113**	**7,261**	**8,295**	**9,246**	**10,054**	**10,799**	**11,437**
Capital expenditure	(200)	(200)	(200)	(200)	(200)	(200)	(200)	(200)	(200)	(200)
Free cash flow	**3,560**	**3,417**	**4,555**	**5,838**	**6,968**	**7,991**	**8,937**	**9,738**	**10,514**	**11,124**
Discounted cash flow- now	3,382	2,885	3,419	3,895	4,131	4,212	4,186	4,055	3,890	3,659
Discounted cash flow-1 year forward		3,246	3,847	4,382	4,649	4,738	4,710	4,562	4,378	4,116
Discounted cash flow-2 year forward			4,327	4,930	5,230	5,332	5,298	5,132	4,925	4,632

	Now	+ 1-year	+ 2-years
Total PV of free cash flow (a)	37,714	42,523	48,340
PV of terminal value (b)	64,942	69,163	73,659
Total company value (a) + (b)	102,656	111,687	121,999
Net debt/(cash)	2,271	(796)	(3,497)
Value to equity holders	100,385	112,483	125,497
Value to equity holders (Rs/share)	**231**	**259**	**289**

Assumptions for WACC and growth in perpetuity	
Growth from 2017 to perpetuity (%)	6.5
FCF multiple (X)	**16.7**
Exit EV/EBITDA multiple (X)	**10.0**
WACC (%)	**12.5**

Source: Kotak Institutional Equities estimates.

Consolidated profit and loss statement for Zee Telefilms, March fiscal year-ends, 2004-2006, ZEEL, 2007-2012E (Rs mn)

	2004	2005	2006	2007	2008E	2009E	2010E	2011E	2012E
Revenues									
National Hindi (Zee TV)	2,539	1,826	2,119	3,303	4,894	5,518	6,358	7,270	8,218
National Hindi (Zee Cinema)	756	914	996	1,574	1,830	2,063	2,378	2,719	3,073
Niche channels (News, English, Music, ETC Music and ZED)	965	956	1,081	400	504	601	711	837	939
Regional channels (incl. ETC Punjabi)	1,365	1,324	1,486	—	—	—	—	—	—
Zee Sports + Taj TV	—	—	72	1,279	1,536	1,792	2,024		
Cable TV (Siti)	220	266	261	—	—	—	—	—	—
Overseas - ZMWL	460	505	557	526	472	490	488	499	510
Others	50	(92)	(6)	(47)	—	—	—	—	—
Advertisement	**6,355**	**5,698**	**6,566**	**7,035**	**9,236**	**10,464**	**11,959**	**13,605**	**15,301**
Domestic pay-TV	2,173	2,696	2,742	3,064	3,430	4,220	5,346	6,587	7,742
Overseas	2,569	2,909	3,030	3,933	3,813	3,974	4,156	4,335	4,521
Domestic subscription	1,168	1,002	978	—	—	—	—	—	—
Others	115	(74)	423	(349)	—	—	—	—	—
Subscription	**6,026**	**6,533**	**7,174**	**6,648**	**7,243**	**8,194**	**9,502**	**10,922**	**12,263**
Education	131	106	162	205	218	240	264	290	319
Others	1,190	742	2,641	1,271	481	528	553	581	609
Total revenues	**13,702**	**13,079**	**16,544**	**15,159**	**17,178**	**19,426**	**22,279**	**25,398**	**28,493**
Programming/Content	(2,520)	(2,611)	(4,247)	(4,783)	(4,570)	(4,578)	(5,035)	(5,548)	(6,091)
Broadcasting	(618)	(675)	(515)	(564)	(516)	(513)	(509)	(519)	(530)
Distribution	(1,837)	(1,534)	(2,565)	(1,967)	(1,657)	(1,756)	(1,813)	(1,886)	(1,962)
Other direct operating	—	—	(262)	(766)	(768)	(808)	(850)		
Employees	(727)	(858)	(1,089)	(1,017)	(1,395)	(1,516)	(1,624)	(1,749)	(1,887)
SG&A	(3,691)	(3,051)	(3,431)	(2,858)	(2,778)	(2,858)	(3,054)	(3,246)	(3,553)
Total expenses	**(9,393)**	**(8,728)**	**(13,848)**	**(11,955)**	**(11,684)**	**(12,029)**	**(12,886)**	**(13,843)**	**(14,963)**
EBITDA	**4,309**	**4,351**	**2,695**	**3,204**	**5,495**	**7,397**	**9,393**	**11,555**	**13,530**
Other income	776	521	639	747	849	934	1,026	1,266	1,575
Interest expense	(583)	(207)	(188)	(334)	(365)	(134)	(2)	—	—
Depreciation	(320)	(329)	(360)	(185)	(252)	(271)	(283)	(290)	(300)
Amortization	—	—	—	—	—	—	—	—	—
Pretax profits	**4,183**	**4,336**	**2,787**	**3,432**	**5,727**	**7,927**	**10,134**	**12,531**	**14,806**
Extraordinary items	26	(140)	19	—	—	—	—	—	—
Tax	(1,103)	(1,123)	(528)	(926)	(1,912)	(2,619)	(3,403)	(4,197)	(5,005)
Deferred tax	54	99	(9)	(76)	(3)	6	12	16	19
Minority interest	(192)	(50)	(117)	(58)	(206)	(203)	(243)	(286)	(330)
Net income	**2,969**	**3,123**	**2,153**	**2,373**	**3,606**	**5,110**	**6,501**	**8,063**	**9,490**
Recurring net income	**2,942**	**3,263**	**2,134**	**2,373**	**3,606**	**5,110**	**6,501**	**8,063**	**9,490**
Fully diluted EPS	**7.1**	**7.5**	**4.9**	**5.5**	**8.3**	**11.8**	**15.0**	**18.6**	**21.9**

	2004	2005	2006	2007	2008E	2009E	2010E	2011E	2012E
Key ratios									
EBITDA growth (%)	**14.7**	**1.0**	**(38.1)**	**18.9**	**71.5**	**34.6**	**27.0**	**23.0**	**17.1**
EPS growth (%)	**18.2**	**5.2**	**(34.6)**	**11.2**	**52.0**	**41.7**	**27.2**	**24.4**	**17.7**
EBITDA margin (%)	31.5	33.3	16.3	21.1	32.0	38.1	42.2	45.5	47.5
Tax rate (%)	24.9	24.4	19.1	29.2	33.4	33.0	33.5	33.4	33.7
Shares o/s year end (mn)	412	412	413	434	434	434	434	434	434
Shares o/s fully diluted (mn)	412	435	435	435	435	435	435	434	434

Source: Kotak Institutional Equities estimates.

Consolidated profit model, balance sheet, cash model of Zee Telefilms 2006 and of ZEEL 2007-2012E, March fiscal year-ends (Rs mn)

	2006	2007	2008E	2009E	2010E	2011E	2012E
Profit model (Rs mn)							
Total revenues	**16,544**	**15,159**	**17,178**	**19,426**	**22,279**	**25,398**	**28,493**
EBITDA	**2,695**	**3,204**	**5,495**	**7,397**	**9,393**	**11,555**	**13,530**
Other income	639	747	849	934	1,026	1,266	1,575
Interest	(188)	(334)	(365)	(134)	(2)	—	—
Depreciation	(360)	(185)	(252)	(271)	(283)	(290)	(300)
Amortization	—	—	—	—	—	—	—
Pretax profits	**2,787**	**3,432**	**5,727**	**7,927**	**10,134**	**12,531**	**14,806**
Extraordinary items	19	—	—	—	—	—	—
Tax	(528)	(926)	(1,912)	(2,619)	(3,403)	(4,197)	(5,005)
Deferred tax	(9)	(76)	(3)	6	12	16	19
Minority interest	(117)	(58)	(206)	(203)	(243)	(286)	(330)
Net income	**2,153**	**2,373**	**3,606**	**5,110**	**6,501**	**8,063**	**9,490**
Recurring net income	**2,134**	**2,373**	**3,606**	**5,110**	**6,501**	**8,063**	**9,490**
Earnings per share (Rs)	**4.9**	**5.5**	**8.3**	**11.8**	**15.0**	**18.6**	**21.9**
Balance sheet (Rs mn)							
Total equity	21,286	26,181	28,659	32,170	36,637	42,177	48,698
Deferred tax balance	(148)	(75)	(72)	(78)	(91)	(106)	(125)
Minority interest	458	819	1,024	1,227	1,470	1,757	2,087
Total borrowings	4,901	3,226	3,226	274	—	—	—
Currrent liabilities	4,346	5,106	3,216	3,266	3,452	3,681	3,922
Total capital	**30,844**	**35,256**	**36,053**	**36,860**	**41,469**	**47,508**	**54,581**
Cash	1,286	955	4,022	3,771	7,100	11,756	17,423
Current assets	13,574	17,133	14,914	16,043	17,406	18,879	20,385
Net fixed assets	12,948	14,841	14,789	14,719	14,635	14,546	14,446
Investments	3,024	2,326	2,326	2,326	2,326	2,326	2,326
Deferred expenditure	12	2	2	2	2	2	2
Total assets	**30,844**	**35,256**	**36,053**	**36,860**	**41,469**	**47,508**	**54,581**
Free cash flow (Rs mn)							
Operating cash flow, excl. working capital	1,931	1,812	3,217	4,645	5,988	7,358	8,525
Working capital	(3,950)	(486)	329	(1,078)	(1,178)	(1,245)	(1,264)
Capital expenditure	(383)	(460)	(200)	(200)	(200)	(200)	(200)
Investments	418	(4,289)	—	—	—	—	—
Other income	488	469	849	934	1,026	1,266	1,575
Free cash flow	**(1,496)**	**(2,954)**	**4,195**	**4,300**	**5,636**	**7,179**	**8,636**
Revenue model (Rs mn)							
Advertising	6,566	7,035	9,236	10,464	11,959	13,605	15,301
Subscription-domestic	2,742	3,064	3,430	4,220	5,346	6,587	7,742
Subscription-overseas	3,030	3,933	3,813	3,974	4,156	4,335	4,521
Subscription-cable	978	—	—	—	—	—	—
Others	3,227	1,127	700	768	817	871	928
Total revenues	**16,544**	**15,159**	**17,178**	**19,426**	**22,279**	**25,398**	**28,493**

Source: Kotak Institutional Equities estimates.

Automobiles

ASOK.BO, Rs38

Ashok Leyland: 2QFY08 net profit declines 16% yoy on account of lower volumes

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- **2Q net profit at Rs803 mn declines 16% yoy and 9% qoq**
- **2Q EBITDA margin at 9.7% improves 160 bps yoy as net realizations are up by 10%**
- **CV volume growth to be under pressure, bus volumes to grow**

Ashok Leyland (ALL) 2Q net profit at Rs803 mn declined 16% yoy and 9% qoq. 2Q EBITDA margins at 9.7% grew 160 bps yoy but dropped 110 bps qoq as average realization per vehicle was higher by 10% yoy. Net sales at Rs17.5 bn grew 4% yoy mainly on account of higher realization even as overall sales volume for 2Q dropped 5% yoy.

EBIDTA margin improves as realization increases 10%

Net realization per vehicle improved 10% yoy for 2Q. This has lead to a 160 bps yoy improvement in margins. However, on a qoq basis, EBITDA margin was lower by 110 bps. Raw material costs as a percentage of sales were lower by 100 bps yoy, improving margins. Employee costs, however, increased 200 bps on account of bonus payments made during the quarter. We believe that margins would remain stable as ALL has effected a price increase of 2% across models effective November.

Net profit lower on account of higher interest costs

Net profit at Rs803 mn was lower 16% yoy and 9% qoq mainly on account of a substantial increase in interest costs as the company is undertaking a capacity expansion plan—interest cost was Rs126 mn for 2QFY08 as against Rs4 mn a year ago. Other income at Rs111 mn was lower 67% yoy as the company booked a one-time profit on sale of shares in IndusInd Bank in 2QFY07.

CV volume growth to be under pressure, bus volumes to grow

CV volumes declined 19% yoy while bus volumes grew 99% yoy in 1HFY08. ALL has indicated in its con-call that pressure on CV volume growth would continue on account of higher interest rates. Bus volumes are expected to grow as demand from State Transport Corporations (STC) as well as private operators is expected to grow. ALL expects to receive orders from STCs in the coming months.

Key takeaways from conference call

1) ALL is expanding capacity at its Ennore facility as well as in Uttaranchal—capacity to increase from to 180,000 vehicles in mid-FY2009 from 100,000 vehicles currently.

2) Total capex spending to be Rs10 bn and Rs12 bn for FY2008 and FY2009 respectively.

3) ALL has indicated that CV sales are under pressure—however, the company expects volumes to pick up in the festival season

4) Pressure on raw material costs to continue on account of higher steel prices

Ashok Leyland, Quarterly results, March fiscal year-ends (Rs mn)

			qoq			yoy	
	2007	2Q 2008	1Q 2008	Change (%)	2Q 2008	2Q 2007	Change (%)
Net sales	**71,682**	**17,459**	**16,211**	**7.7**	**17,459**	**16,757**	**4.2**
Expenditure	(64,655)	(15,774)	(14,468)	9.0	(15,774)	(15,407)	2.4
(Increase)/decrease in stocks	647	876	1,267	(30.8)	876	554	58.1
Consumption of raw materials	(54,038)	(13,585)	(12,937)	5.0	(13,585)	(13,216)	2.8
Staff cost	(4,807)	(1,619)	(1,391)	16.4	(1,619)	(1,203)	34.5
Other expenditure	(6,457)	(1,447)	(1,408)	2.8	(1,447)	(1,542)	(6.2)
EBITDA	**7,027**	**1,685**	**1,743**	**(3.3)**	**1,685**	**1,350**	**24.8**
Other income	708	111	76	47.5	111	337	(66.9)
Interest (net)	(53)	(126)	(128)	(1.0)	(126)	(4)	3,303.0
Depreciation	(1,506)	(466)	(413)	12.9	(466)	(365)	27.9
Profit before extra-ordinary items	**6,176**	**1,204**	**1,278**	**(5.8)**	**1,204**	**1,319**	**(8.7)**
Extra-ordinary items	(131)	(27)	(35)		(27)	(31)	
Profit before tax	**6,045**	**1,177**	**1,243**	**(5.3)**	**1,177**	**1,288**	**(8.6)**
Tax	(1,632)	(374)	(361)	3.5	(374)	(334)	11.8
Profit after tax	**4,413**	**803**	**882**	**(8.9)**	**803**	**954**	**(15.8)**
Adjusted PAT	**4,498**	**821**	**905**	**(9.3)**	**821**	**974**	**(15.7)**
Sales volume (number of vehicles)	**83,133**	**18,891**	**18,163**	**4.0**	**18,891**	**19,869**	**(4.9)**
Average net realisation (Rs/vehicle)	862,249	924,194	892,552	3.5	924,194	843,385	9.6
Margins (%)							
OPM	9.8	9.7	10.8	(1.10)	9.7	8.1	1.59
NPM	6.2	4.6	5.4	(0.84)	4.6	5.7	(1.09)
Key ratios							
RM costs (% of net sales)	75.4	77.8	79.8	(1.99)	77.8	78.9	(1.06)
Staff costs (% of net sales)	6.7	9.3	8.6	0.69	9.3	7.2	2.09
Effective tax rate (%)	27.0	31.8	29.1	2.71	31.8	26.0	5.80

Source: Company data, Kotak Institutional Equities estimates.

Cement

SHCM.BO, Rs1417	
Rating	IL
Sector coverage view	Cautious
Target Price (Rs)	1,300
52W High -Low (Rs)	1695 - 851
Market Cap (Rs bn)	49.3

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	13.5	18.6	22.2
Net Profit (Rs bn)	3.5	4.4	4.7
EPS (Rs)	101.6	125.5	135.9
EPS gth	*114.9*	*24.1*	*8.5*
P/E (x)	13.9	11.3	10.4
EV/EBITDA (x)	9.1	6.7	6
Div yield (%)	0.4	0.4	0.4

Shareholding, June 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	63.7	-	-
FIIs	6.8	0.0	(0.1)
MFs	6.0	0.2	0.1
UTI	-	-	(0.1)
LIC	-	-	(0.1)

Shree Cement: 2QFY08—Results in line with expectations, capacity increased to 9 mn tpa

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- **Maintaining healthy volume growth**
- **Commissioned 3 mn tpa capacity during the quarter - total capacity 9 mn tpa**
- **Other income boosted by Rs160 mn sale of Certified Emission Rights (CER)**
- **Retain In-Line with target price of Rs1,300/share**

Shree Cement reported 47.6% increase in sales at Rs4.6 bn (our est. Rs4.3 bn), 41% increase in EBITDA at Rs2 bn (our est. Rs1.8 bn) and a 22% increase in net income at Rs1.06 bn (our est. Rs1.06 bn). Net income was boosted by Rs160 mn received upon the sale of carbon emission rights. The operating performance of the company was largely in line with our estimates with volumes growth of 28% yoy due to the increased production capacity. We retain our In-Line rating on the stock. Our target price of Rs1,300/share implies EV/EBITDA of 8.2X and P/E of 10.4X on FY2008E. We will revisit our estimates and target price after the analyst call with the management.

Maintaining healthy volume growth. Shree Cement sold 1.4 mn tonnes of cement during 2QFY08, an increase of 28% yoy. EBITDA margins declined by 200 bps yoy though profitability on a per tonne basis improved 10% yoy to Rs1,406/tonne. Price increases have helped Shree Cement effectively counter the increasing cost of petroleum coke.

Commissioned 3 mn tpa capacity during the quarter—total capacity 9 mn tpa. We expect Shree Cements to benefit from increased cement consumption in its northern markets due to construction activity in the build up to the Commonwealth Games in FY2010. During the quarter Shree Cement commissioned a 2 mn tpa grinding unit near Gurgaon and a 1 mn tpa clinkering unit in Rajasthan, in addition to a 1.4 mn tpa capacity that was commissioned in March 2007. Shree Cement also commissioned an 18 MW captive power plant in order to meet the increased power requirements to support additional capacities.

Other income boosted by Rs160 mn sale of Certified Emission Rights (CER). Other income for the quarter was boosted by Rs160 mn from the sale of CER's which accrued to the company from the "Optimal Utilization of Clinker" project under the Clean Development Mechanism registered by United Nations Framework Convention on Climate Change. We note that these CERs shall accrue to the company upto July 2010.

Retain In-Line with target price of Rs1,300/share. We retain our target price of Rs1,300/share with an earnings estimate of Rs125.5/share for FY2008 and Rs135.9/share for FY2009, which implies a P/E of 10.4X on FY2008E and 9.6X on FY2009E. We will revisit our estimates and target price post the analyst call with the management. Our target price has a downside of about10% from the current market price of Rs1,417/share.

Shree Cement - quarterly performance, March fiscal yearends (Rs mn)

	y-o-y			q-o-q	
	Sep-07	**Sep-06**	**Change (%)**	**Jun-07**	**Change (%)**
Net sales	**4,664**	**3,160**	**47.6**	**4,258**	**9.5**
Raw materials	(413)	(372)		(442)	
Power & fuel	(883)	(535)		(823)	
Freight	(706)	(388)		(620)	
Personnel	(161)	(117)		(154)	
Others	(485)	(321)		(395)	
Total expenditure	(2,649)	(1,733)		(2,434)	
EBITDA	**2,015**	**1,427**	**41.2**	**1,824**	**10.5**
EBITDA (%)	*43*	*45*		*43*	
Other income	291	43		126	
Interest	(85)	(27)		(39)	
Depreciation	(688)	(248)		(358)	
Pre-tax profits	**1,534**	**1,195**	**28.4**	**1,553**	**(1.2)**
Tax	(447)	(326)		(383)	-
Net income	**1,066**	**868**	**22.7**	**1,170**	**(8.9)**
Extraordinary	-	-		(1)	
Reported income	**1,066**	**868**	**22.7**	**1,169**	**(8.8)**
Sales ('000 tonnes)	1,433	1,116	28.4	1,403	2.1
Realization (Rs/tonne)	3,254	2,831	14.9	3,034	7.3
Cost (Rs/tonne)	1,848	1,553	19.0	1,734	6.6
Raw materials	288	333	(13.5)	315	(8.5)
Power & fuel	616	479	28.7	587	5.1
Freight	492	348	41.6	442	11.5
Personnel	113	105	7.0	110	2.6
Others	339	288	17.7	282	20.3
Operating profit (Rs/tonne)	1,406	1,278	10.0	1,300	8.2
Tax rate (%)	30.5	27.3	-	24.7	-

Source: Company data, Kotak Institutional Equities.

Shree Cement Limited, Profit model, March fiscal year-ends, 2005-2009E

(Rs mn)

	2005	2006	2007	2008E	2009E
Net sales	**5,821**	**6,677**	**13,500**	**18,583**	**22,208**
Raw materials	(721)	(896)	(1,626)	(2,245)	(2,897)
Power costs	(1,385)	(1,373)	(2,224)	(3,444)	(4,484)
Freight cost	(904)	(1,005)	(1,675)	(2,402)	(2,923)
Employee costs	(264)	(330)	(528)	(712)	(950)
Other expenses	(757)	(702)	(1,502)	(1,892)	(2,281)
Operating profits	**1,790**	**2,371**	**5,945**	**7,888**	**8,673**
Operating margin %	30.7	35.5	44.0	42.4	39.1
Other income	21	35	142	107	107
EBITD	1,811	2,406	6,088	7,995	8,780
Interest	(213)	(141)	(176)	(402)	(442)
Depreciation	(541)	(503)	(1,014)	(1,421)	(1,680)
Pretax profits	**1,058**	**1,761**	**4,898**	**6,172**	**6,658**
Tax	(24)	(29)	(1,178)	(1,667)	(1,801)
Deferred tax	4	(59)	(179)	(134)	(124)
Net profits	**1,037**	**1,674**	**3,541**	**4,371**	**4,733**
Extraordinaries	(497)	(1,483)	-	-	-
Reported net profits	**540**	**190**	**3,541**	**4,371**	**4,733**
Diluted EPS (Rs)	**29.8**	**48.0**	**101.6**	**125.5**	**135.9**
Reported EPS (Rs)	**15.5**	**5.5**	**101.6**	**125.5**	**135.9**
Diluted avg shares (mn)	34.8	34.8	34.8	34.8	34.8
Growth (%)					
Sales	23.0	14.7	102.2	37.7	19.5
EBITDA	31.9	32.8	153.0	31.3	9.8
Net income	150.1	61.4	111.6	23.4	8.3
EPS	150.1	61.4	111.6	23.4	8.3
Tax rate (%)	2.3	1.6	24.0	27.0	27.0
Total Tax rate	2.0	5.0	27.7	29.2	28.9

Source: Company data, Kotak Institutional Equities estimates.

Calculation of target prices using our multi-stage valuation process

	Shree Cement
March 2008 CROGCI/WACC (x)	2.28
Assigned premium of EV/GCI to CROGCI/WACC (%)	(30)
Assigned EV/GCI (x)	1.61
GCI (Rs bn)	28.8
EV (Rs bn)	46.2
Net debt (Rs bn)	1.57
Market capitalization (Rs bn)	44.6
No. of shares (fully diluted)	34.8
Target price (Rs)	**1,300**

Source: Kotak Institutional Equities estimates.

Consumer Products

GOCP.BO, Rs120	
Rating	OP
Sector coverage view	Neutral
Target Price (Rs)	185
52W High -Low (Rs)	193 - 118
Market Cap (Rs bn)	27.1

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	9.3	11.1	12.6
Net Profit (Rs bn)	1.3	1.6	1.8
EPS (Rs)	5.9	7.0	8.1
EPS gth	*11.4*	*18.9*	*16.0*
P/E (x)	20.4	17.1	14.8
EV/EBITDA (x)	15.9	12.9	11.1
Div yield (%)	3.1	3.3	3.5

Shareholding, June 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	67.8	-	-
FIIs	19.0	0.1	(0.0)
MFs	1.3	0.0	(0.1)
UTI	-	-	(0.1)
LIC	-	-	(0.1)

Godrej Consumer Products: 2QFY08—Clear view in the rear view mirror, bumpy road ahead

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- **Price hikes drive sales growth**
- **210 bps EBITDA margin improvement, propped by price hikes**
- **The ITC factor - growth may get tougher in a more competitive scenario**

GCPL reported 15.2% growth in standalone sales as against our estimate of 26.0%. Soap sales grew 17.2% yoy - the lowest in two years (after a record 28.7% growth in 1QFY08), aided by two rounds of price hikes (about10%) in the past year. Hair color growth at 12% disappointed as it also had the benefit of price increase taken during December 2006 on powder sachet hair dye. GCPL reported an EBITDA growth of 28.3% (we expected 22.5%) and a 28.9% increase in net profit (we expected 25.0%) for 2QFY08. Price hikes seemed to have aided in the 210 bps expansion of EBITDA margins to 20.6%. We will revisit our estimates after the analyst conference call. We retain our earnings estimates at Rs7.0 for FY2008 and Rs8.1 for CY2008 and target price at Rs185/share (15% discount to our DCF value). We also keenly await the market response to ITC's new launches in soaps which pits it directly against the fast growing soaps business of GCPL.

Price hikes drive sales growth. Significant price increases (about10%) in soaps and hair color have driven GCPL's topline growth. GCPL recorded 17.2% yoy growth in soap sales, the lowest growth in two years, coming after record growth in 1QFY08. Market sources indicate soap industry value growth during the quarter at about 8% implying that, adjusting for the price increases, the volume growth is marginally negative in this highly penetrated category. GCPL's improved its market share to 10.2%, compared to 9.3% in 2QFY07. The company is now a clear second in the soaps segment with a 10.2% value market share with Godrej No.1 (an all-time high of 6.5% market share) continuing to gain from HUL's Breeze and regional players in the popular segment.

Hair color sales grew a disappointing 12.0% yoy. We note that hair color had the benefit of about 7% average price increase due to Re1 increase in price of its main SKU—powder sachet hair dye. The market share in hair color continues to decline (slipped 270 bps yoy to 34.9% -- the lowest in over five years) due to better growth at the high-end fashion color segment.

210 bps EBITDA margin improvement, propped by price hikes. EBITDA margins during 2QFY08 improved by 210 bps yoy to 20.6%. The margin improvement was on the back of about 10% price increases. We believe there are operating leverage benefits as well, as the company has crossed Rs10 bn topline on an annualized basis. However, the input cost scenario continues to be challenging with prices of palm oil and variants hitting all-time highs recently. The management had earlier indicated that appropriate price increases will be considered to counter input cost inflation. We note that the higher depreciation expenditure is on account of the Katha (Himachal) and Sikkim factories, which were commissioned in December 2006 and March 2007, respectively.

The ITC factor—growing may get tougher in a more competitive scenario. Over the past year, measured price hikes by HUL and GCPL have helped mitigate higher palm prices (up over 70%). GCPL has expanded the portfolio in personal products range—launched the 'Godrej No. 1' shampoo and 'Fair Glow' facewash in June 2007. However, ITC's entry could possibly cap further price increases and the requirement for higher ad spends could adversely impact the margin profile as well. We believe that incremental growth will come at significantly higher cost than before. ITC has recently launched the 'Superia' brand of soaps at the lower end ('popular' segment) of the category in four variants. The product and pricing is in direct competition with GCPL's 'Godrej No.1' (estimated sales about Rs3 bn) and HUL's Lifebuoy (estimated sales Rs9 bn), Breeze (estimated sales Rs2 bn). We keenly await market response to ITC's new launches in soaps and shampoos.

Global operations contribute about 25% to the consolidated turnover and 20% to EBITDA. Consolidated sales and EBITDA during 2QFY08 were up 20.9% and 42.5%, respectively, on a yoy basis. Global operations of GCPL – Keyline Brands and Rapidol International, together contributed about 25% to the consolidated turnover of GCPL during 2QFY08. Sales for Keyline Brands grew 17% yoy, though there were marginal disruptions in sales of P20 (sun protection screen). The Cuticura skincare range was relaunched during the quarter with significant brand investments resulting in PBIT compression of 620 bps to 9.8%.

Exhibit 1: Godrej Consumer Products Limited -Quarterly summary, March yearend (Rs mn)

		yoy		Our est.	yoy		Consolidated yoy	
	2Q FY08	2Q FY07	% chg	2Q FY08	% chg	2Q FY08	2Q FY07	% chg
Sales	**2,103**	**1,825**	**15.2**	**2,300**	**26.0**	**2,804**	**2,318**	**20.9**
Material costs	(1,028)	(922)				(1,340)	(1,183)	
Employee costs	(109)	(103)				(153)	(134)	
A&P expenditure	(123)	(97)				(230)	(158)	
Other expenses	(408)	(365)				(516)	(447)	
Total expenses	(1,669)	(1,487)				(2,239)	(1,922)	
EBITDA	**434**	**338**	**28.3**	**413**	**22.0**	**565**	**397**	**42.5**
Depreciation	(41)	(29)		(35)		(46)	(31)	
EBIT	**393**	**310**		**377**		**519**	**366**	
Other income	15	6		8		14	28	
Interest	(21)	(16)		(16)		(32)	(26)	
PBT	**387**	**299**	**29.3**	**370**	**23.7**	**501**	**369**	**35.9**
Tax	(50)	(38)		(43)		(67)	(59)	
Net profit	**337**	**261**	**28.9**	**327**	**25.0**	**434**	**310**	**40.1**
Exceptional item	-	-		-		-	-	
EBITDA margin (%)	20.6	18.5		17.9		20.2	17.1	
Tax rate (%)	13.0	12.7		11.7		13.3	15.9	
Sales break up								
Soaps	1,453	1,240	17.2	1,637	32.0			
Hair Colour	445	397	12.0	451	13.5			
Toiletries	137	113	21.4	131	16.1			
Liquid Detergents	28	39	(28.0)	42	8.0			
Total Godrej Brands	**2,062**	**1,789**	**15.3**	**2,260**	**26.4**			
Contract manufacturing	-	-		-				
Sale of by-products/others	40	36	10.7	40	10.0			
TOTAL	**2,103**	**1,825**	**15.2**	**2,300**	**26.0**			

Source: Company data.

Exhibit 2: Keyline Brands, Quarterly summary (Rs mn)

	1Q FY2007	2Q FY2007	3Q FY2007	4Q FY2007	1Q FY2008	2Q FY2008
Sales	460	463	258	493	391	541
EBIT	67	74	25	77	36	53
PBT	52	64	15	68	27	41
Tax	(15)	(20)	(5)	(19)	(8)	(14)
Net profit	37	44	10	49	19	27
Sales growth (%)				76	(15)	17
EBIT growth (%)				285	(46)	(28)
EBIT margin (%)	14.6	16.0	9.7	15.6	9.2	9.8

* represents financial performance for 2 months

Rapidol Pty Limited, Quarterly summary (Rs mn)

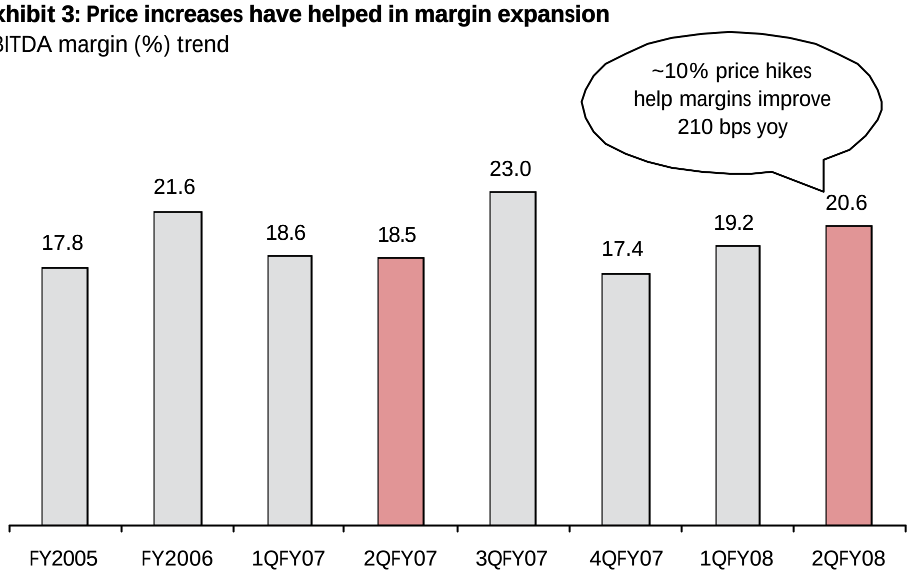
	2Q FY2007 *	3Q FY2007	4Q FY2007	1Q FY2008	2Q FY2008
Sales	30	145	101	119	117
EBIT	5	27	9	17	12
PBT	5	27	10	18	11
Tax	(1)	(8)	(3)	(5)	(4)
Net profit	4	19	7	13	7
EBIT margin (%)	16.7	18.6	8.9	14.3	10.3

* represents performance for 1 month w.e.f September 1, 2006

Source: Company data.

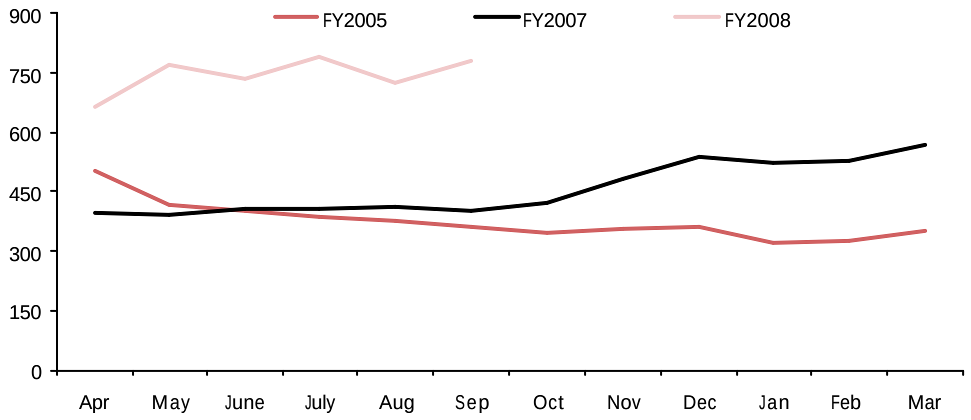
Exhibit 3: Price increases have helped in margin expansion

EBITDA margin (%) trend



Source: Company data.

Exhibit 4: Prices of Palm Stearin has doubled yoy and will impact EBITDA margins going forward



Source: Bloomberg, Kotak Institutional Equities.

Exhibit 5: Competitive positioning in soaps

Soaps (Low-end/Popular segment) - Brands and price points

		MRP for 75 gm	TFM (c)
Brand	**Company**	**Rs**	**%**
Breeze (a)	HUL	6	66
Godrej No.1	Godrej Consumer	7	76
Superia	**ITC**	**6.50**	**70**

(a) Banded pack of 4 soaps of 75 gm for Rs 25
(b) Banded pack of 4 soaps of 75 gm for Rs 27
(c) Total Fatty Matter (TFM) content indicates the oil content in soap.
Typical consumer perception is higher TFM = higher quality

Source: Company, Kotak Institutional Equities.

Exhibit 6: Soaps brands (segmentwise)

Segment	Brand	Company
Premium	Dove	HUL
	Pears	HUL
	Mysore Sandal	Karnataka Soaps
	Fairglow	GCPL
	Lux International	HUL
Mid-priced	Lux	HUL
	Hamam	HUL
	Rexona	HUL
	Cinthol	GCPL
	Lifebuoy Plus	HUL
	Santoor	Wipro
Low-end	Breeze	HUL
	Lifebuoy	HUL
	Nima	Nirma
	Nirma	Nirma
	Godrej No.1	GCPL
	Superia	ITC

Source: Company, Kotak Institutional Equities.

Exhibit 7: Business under threat from ITC's products
Segment contribution of categories

		Contribution to	
Company	**Category**	**Sales (%)**	**PBIT (%)**
HUL	Soap	20	22
HUL	Shampoo	7	12
GCPL	**Soap**	**64**	**35**

Source: Company, Kotak Institutional Equities estimates.

Consumer Products

GLSM.BO, Rs626	
Rating	IL
Sector coverage view	Neutral
Target Price (Rs)	720
52W High -Low (Rs)	670 - 500
Market Cap (Rs bn)	26.3

Financials

December y/e	2006	2007E	2008E
Sales (Rs bn)	11.1	13.0	14.7
Net Profit (Rs bn)	1.3	1.7	2.0
EPS (Rs)	30.2	40.9	47.4
EPS gth	*18.5*	*35.5*	*15.8*
P/E (x)	20.8	15.3	13.2
EV/EBITDA (x)	10.6	8.1	6.6
Div yield (%)	1.6	2.2	2.5

Shareholding, June 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	43.2	-	-
FIIs	3.6	0.0	0.0
MFs	11.7	0.2	0.2
UTI	1.6	0.3	0.3
LIC	8.8	0.2	0.2

Glaxo SmithKline Consumer India: 3QCY07—Healthy growth and margin expansion

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- **Heady mix of pricing power and volume growth**
- **Multiple margin expansion drivers**
- **It was getting lonely at top for Horlicks - Dabur enters malted foods drinks category**

GlaxoSmithkline Consumer (GSK) reported y-o-y sales growth of 16.7% (our est. 14.7%) and EBITDA increase of 28.1% (our est. 18.0%) during 3QCY07. Higher-than-anticipated operating margins and other income during the quarter resulted in a strong PAT growth of 39.4%. EBITDA margins improved to 19.3% compared to 17.5% in the 3QCY06 and our estimate of 18.0%. The margins benefited from reduction of tax in Tamil Nadu and Kerala on implementation of VAT and price increases. We have revised our estimates to factor in the higher margins. Our revised EPS estimates are at Rs40.9/share (Rs35.9/share earlier) for CY2007E and Rs47.3/share (Rs40/share earlier) for CY2008E. We retain our In-Line rating on the stock with a revised target price of Rs720/share (Rs625/share previously) implying a P/E of 15.2X on CY2008E. Our target price offers a 15% upside to the current market price of Rs626.

Heady mix of pricing power and volume growth. Highest ever monthly sales in Horlicks & Boost have resulted in robust 17% yoy growth in sales. Volume growth was however lower at about 7%. We estimate Horlicks and Boost recorded good volume growth, Viva and Maltova registering specific activation driven volume growth of over 10%. Volumes for the biscuits division were flat yoy. During the quarter, the company witnessed significant cost inflation – skimmed milk powder about 25% and wheat about 15%. GSK has taken a price increase of Rs5 per 500g in Horlicks during June 2007 to counter the increasing raw material costs. Management expects prices of skimmed milk powder (SMP) to strengthen further by about 20% for 2HCY07. According to the management, the ban on exports of SMP has helped tone down the price increases. However, the recent lifting of SMP exports ban is expected to adversely impact the input prices.

Multiple margin expansion drivers. EBITDA margins improve by 180 bps to 19.3% (17.5% in 3QCY07). Improvement in EBITDA margins was due to higher price realizations, cost containment and the benefit of transition from sales tax to VAT in the states of Tamilnadu and Kerala. Advertising and promotion expenses were marginally higher at 13% of sales (12% in 3QCY07).

It was getting lonely at top for Horlicks—Dabur enters malted foods drinks category. Horlicks account for over two-thirds of the malted drinks category. Dabur has recently launched Chyawan Junior (ingredients of Chyawanprash with chocolate flavour in malted food base) priced at Rs120 / 500 gm, in line with competition. We expect Dabur to create a niche with this differentiated product. However, given the distribution reach and association with ayurvedic/health products, it could be a serious competitor to GSK if it chooses to enter the mainstream malted drinks market. We note that GSK derives almost 90% of its sales from the malted beverage category (Horlicks biscuits and exports account for about 5% each). Nestle and Amul had entered the category earlier with Milo and Nutramul, respectively. Despite strong synergies with their current portfolio and having distribution set-ups, both companies had limited success in the malted food drink category. We believe that there are two reasons for the continued dominance of incumbent brands—(1) it's a product for kids and hence the taste has to be popular, (2) intake of health drink is linked to habit and hence it is difficult to persuade customer switching.

We retain our In-Line rating on the stock with a revised target price of Rs720/share (Rs625/ share previously) implying a P/E of 15.2X on CY2008E. Our target price offers a 15% upside to the current market price of Rs626. The company has cash/share of Rs107 (17% of current market price) as of 3QCY07.

Quarterly results of Glaxo SmithKline Consumer, December yearends (Rs mn)

		yoy		Our est.	yoy
	3Q CY07	**3Q CY06**	**% chg**	**2Q CY07**	**% chg**
Gross sales	**3,841**	**3,291**	**16.7**	**3,773**	**14.7**
Excise duty	(325)	(276)			
Net sales	**3,516**	**3,015**	**16.6**	**3,456**	**14.7**
Material cost	(1,240)	(1,124)	*10.3*		
Employee cost	(398)	(328)	*21.3*		
Advertising & promotion expenses	(465)	(366)	*27.1*		
Other overheads	(736)	(668)	*10.2*		
Total operating expenses	(2,839)	(2,486)	*14.2*		
EBITDA	**677**	**528**	**28.1**	**623**	**18.0**
Depreciation	(111)	(109)			
EBIT	**566**	**419**			
Other income	209	139			
Net interest	(12)	(10)			
PBT	**763**	**548**	**39.4**	**654**	**19.5**
Deferred tax	-	-	-	-	-
PAT	**505**	**362**	**39.4**	**433**	**19.5**
Extraordinary income (loss)	-	-	-	-	-
EBITDA margin (%)	19.3	17.5		18.0	
Costs as % of net sales					
Material cost	35.3	37.3			
Employee cost	11.3	10.9			
Advertising & promotion expenses	13.2	12.1			
Other overheads	20.9	22.2			

Source: Company data, Kotak Institutional Equities

Glaxo Smithkline Consumer, Profit model, December yearends, 2005-2008E (Rs mn)

	2005	2006	2007E	2008E
Net revenues	**9,668**	**11,119**	**13,043**	**14,695**
Cost of goods sold	(5,155)	(6,112)	(7,011)	(7,788)
Gross profit	4,514	5,008	6,032	6,907
SG&A expenses	(2,672)	(3,161)	(3,635)	(4,094)
EBITDA	**1,842**	**1,846**	**2,398**	**2,812**
Depreciation and amortization	(419)	(427)	(446)	(493)
EBIT	1,423	1,419	1,951	2,320
Interest (expense)	(42)	(35)	(41)	(47)
Interest income	89	130	240	274
Other income/(expense)	154	392	449	464
Pre-tax profit	**1,624**	**1,906**	**2,599**	**3,012**
Income tax	(553)	(636)	(879)	(1,020)
Net profit	**1,072**	**1,269**	**1,720**	**1,992**
EPS (Rs)	**24.8**	**30.2**	**40.9**	**47.4**
CEPS (Rs)	32.4	38.1	48.8	55.2
Dividend per share (Rs)	8.0	10.0	13.5	15.7
Shares outstanding (m)	42.1	42.1	42.1	42.1
Ratios (%)				
Revenue growth	12.1	15.0	17.3	12.7
EBITDA margin	19.0	16.6	18.4	19.1
PBT growth	35.3	17.3	36.4	15.9
Income tax rate	34.0	33.4	33.8	33.9
EPS growth	45.5	21.5	35.5	15.8

Source: Company data, Kotak Institutional Equities estimates.

Technology

MINT.BO, Rs486	
Rating	IL
Sector coverage view	Attractive
Target Price (Rs)	530
52W High -Low (Rs)	1022 - 425
Market Cap (Rs bn)	18.8

Financials

April y/e	2007	2008E	2009E
Sales (Rs bn)	5.9	7.3	9.7
Net Profit (Rs bn)	0.9	1.0	1.3
EPS (Rs)	22.8	24.5	32.4
EPS gth	*23.3*	*7.6*	*32.2*
P/E (x)	21.3	19.8	15.0
EV/EBITDA (x)	16.8	15.3	11.0
Div yield (%)	0.2	0.5	0.7

MindTree Consulting: Good quarter, no guidance revision - some questions answered, some still remain

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- **Results above expectations**
- **No upward revision in FY2008 total income guidance surprising**
- **Good client addition, Europe business picks up**
- **Reduce estimates, upgrade to IL on valuations, fine-tune target price to Rs530/ share**

MindTree's (MT) 2QFY08 results were ahead of our expectations. Net income at Rs272 mn (+31.8% qoq, +18.6% yoy) was 26% higher than our estimates and primarily aided by forex gains, interest income and higher revenue growth. Revenues grew 15.3% qoq to US$45 mn versus our expectation of 10.5% growth. While the strong 2QFY08 revenue growth allayed some of our fears around demand slowdown from some large European clients, we find no upward revision in US$ 'total income' (revenues + other income) guidance of US$178-180 mn surprising. The guidance implies a 2% qoq decline in 'total income' over 3Q-4QFY08, rather surprising and extremely conservative in our view despite the seasonally weak December quarter. Nonetheless, we maintain our FY2008 revenue estimates, which in any case are higher than the company guidance. We maintain our view on strong 'core revenue' growth (39% for FY2008 and 37% for FY2009 in US$ terms) and near-term margin pressure for MT (220bps OPM decline in FY2008). We have reduced our fully diluted FY2008E and FY2009E EPS estimates for MT to Rs24.5 and Rs32.4 from Rs25.7 and Rs33.8 earlier to factor in our revised Re/US$ assumption (40.1 and 39 for FY2008 and FY2009 against 40.5 and 40 earlier, respectively). However, we upgrade the stock to In-Line from Underperform earlier noting the recent run-down in stock price. Our fine tuned target price is Rs530 (Rs550 earlier) implies an upside of 9% over the CMP.

Results above expectations: MT's 2QFY08 results were ahead of our expectations. Revenues grew 15.3% qoq in US$ terms to US$45 mn, higher than our expectations of US$43.1 mn. Revenue growth was driven by a volume growth of 12.7% and 3% blended pricing improvement. Net income at Rs279 mn grew 31.8% qoq (18.6% yoy) and was aided by forex gains of Rs32.5 mn versus a marginal loss in the previous quarter. EBITDA margins improved 60bps qoq to 16.4% (our expectation was a 20bps improvement to 16%). Margin increase was driven by higher realizations and SG&A efficiencies and offset the impact of partial wage hikes and rupee appreciation.

Unchanged US$ revenue growth guidance—a conservative stance: MT has maintained its US$ 'total income' guidance for FY2008 at US$178-180 mn, implying a yoy growth of 36% at the upper end. Note that MT includes other income (interest income + forex gains) in its guidance. We find no upward revision in MT's 'total income' guidance surprising given its strong revenue performance in 1HFY08. MT's guidance implies a total income CQGR of -2% over 3Q-4QFY08. The company indicates that it has factored in a seasonally weak December quarter (lower number of billing days) in its guidance. We believe that the guidance is conservative. Our 'total income' estimate of US$189 mn (core revenue estimate of US$182 mn) for FY2008 is higher than the company guidance. Our net income estimate of US$24.1 mn is 6.6% higher than the company guidance of US$22.6 mn.

Other metrics—good client addition, Europe slowdown likely behind now: We highlight some of the other key metrics for the quarter—(a) revenue growth from Europe picked (up 26% qoq, 4.5% yoy) after several quarters of sluggish growth (b) client addition pace continues to be good with 28 new clients added during the quarter. More important, the company now has 39 F-500 clients, up from 38 in the previous quarter; US$1 mn and US$5 mn accounts grew to 41 and 5 in the Sep '07 quarter from 34 and 4 at the end of Jun '07 quarter, respectively.

We like the management and business model but are constrained by valuations: We like the business model of Mindtree and believe that the company has put in place building blocks critical for growth—an illustrious management team, excellent systems and processes, preferred employer brand and quality clients. We like the growth story of the company but are unable to justify an Outperform rating. Nonetheless, after a 34% correction in stock price in the last 3 months, we believe that the worst is also factored in. Upgrade to In-Line. We have fine-tuned our EPS estimates to factor in our revised Re/US$ assumptions (40.1 and 39 for FY2008 and FY2009 versus 40.5 and 40 earlier). Our revised full diluted EPS estimates for FY2008E and FY2009E stand at Rs24.5 and Rs32.4 respectively (Rs25.7 and Rs33.8 earlier). Our end-March 2009 DCF-based target price of Rs530 (Rs550 earlier) share implies an earnings multiple of 21.6xFY2008E and 16.4xFY2009E.

Key changes to FY2008-10 estimates

	New			Old			Change (%)		
Rs mn	**FY2008**	**FY2009**	**FY2010**	**FY2008**	**FY2009**	**FY2010**	**FY2008**	**FY2009**	**FY2010**
Revenues (Rs mn)	**7,285**	**9,683**	**12,522**	**7,351**	**9,737**	**12,820**	**(0.9)**	**(0.6)**	**(2.3)**
Revenues (US$ mn)	**182**	**248**	**329**	**182**	**243**	**320**	**0.0**	**2.0**	**2.9**
EBITDA	1,177	1,585	2,035	1,247	1,675	2,200	(5.6)	(5.3)	(7.5)
Net Profit	967	1,278	1,506	1,017	1,334	1,615	(4.9)	(4.2)	(6.7)
EPS (Rs/ share)	**25.0**	**32.6**	**38.3**	**26.3**	**34.0**	**41.1**	**(4.9)**	**(4.2)**	**(6.7)**
Fully diluted EPS	**24.5**	**32.4**	**38.1**	**25.7**	**33.8**	**40.9**	**(4.9)**	**(4.2)**	**(6.7)**
Re/ $ rate	40.1	39.0	38.0	40.5	40.0	40.0	(0.9)	(2.5)	(5.1)
EBITDA margin	16.2	16.4	16.3	17.0	17.2	17.2			

Source: Kotak Institutional Equities estimates

Mindtree Consulting: Indian GAAP consolidated quarterly earnings statement

Rs mn	Sep-06	Jun-07	Sep-07	qoq (%)	yoy (%)	Kotak E	Deviation	Comments
Revenues	**1,537**	**1,615**	**1,819**	**12.7**	**18.4**	**1,746**	**4.2**	Revenues grew 15.3% in US$ terms to US$39 mn versus our expectation of 10.5% growth. Driven by volume growth of 12.7% and blended pricing improvement of 3%.
Software development expenses	(924)	(1,018)	(1,177)	15.7	27.4	(1,110)	**6.0**	
Gross profit	**614**	**597**	**643**	**7.6**	**4.7**	**636**	**1.1**	
SG&A expenses	(339)	(342)	(343)	0.5	1.3	(357)	**(3.7)**	
EBITDA	**274**	**256**	**299**	**17.0**	**9.0**	**279**	**7.1**	EBITDA margin improvement of 60bps higher than our expectations
Depreciation	(64)	(79)	(81)	2.6	26.3	(82)	**(2.0)**	
EBIT	**210**	**177**	**218**	**23.4**	**3.8**	**197**	**10.9**	
Interest	(8)	(9)	(18)	89.3	119.9	(9)	**89.3**	
Other income	20	62	99	58.4	390.8	59	**68.9**	Includes forex gains of Rs32.3 mn versus a marginal loss in 1QFY08
Profit before tax	**222**	**230**	**299**	**30.2**	**34.6**	**246**	**21.7**	
Tax	7	(24)	(28)	16		(32)		
Net profit	**229**	**206**	**272**	**31.8**	**18.6**	**214**	**26.8**	
Minority interest	-	-	-			-		
Net income	**229**	**206**	**272**	**31.8**	**18.6**	**214**	**26.8**	Net income significantly ahead of expectations primarily aided by forex gains and higher revenue growth
Extraordinaries	-	-	-			-		
Net profit- reported	**229**	**206**	**272**	**31.8**	**18.6**	**214**	**26.8**	
Chk								
EBITDA margin	**17.8**	**15.8**	**16.4**			**16.0**		
EPS (Rs/ share)	**7.6**	**5.5**	**7.2**	**31.8**	**(5.5)**	**5.7**	**26.8**	
Shares outstanding (mn)	30.0	37.6	37.6			37.6		
Fully Diluted EPS (Rs/ share)	**7.3**	**5.2**	**6.9**	**31.8**	**(5.4)**	**5.4**	**26.8**	
Fully DilutedShares outstanding (mn)	31.5	39.5	39.5			39.5		
Guidance (FY2008)	**Lower end**		**Upper end**					
Revenues (US$ mn)	178.0		180.0					Revenue guidance for FY2008 maintained.
Growth (%)	36.8		38.4					
Net Income (US $mn)	22.5		22.6					Net income guidance maintained at US$22.5-22.6 mn, though at a lower Re/USD assumption

Source: Kotak Institutional Equities estimates

Mindtree Consulting- consolidated Indian GAAP profit & loss statement. March fiscal year ends

Rs mn	2006	2007	2008E	2009E	2010E
Revenues	**4,488**	**5,904**	**7,285**	**9,683**	**12,522**
Software development expenses	(2,735)	(3,509)	(4,677)	(6,271)	(8,161)
Gross profit	**1,753**	**2,395**	**2,608**	**3,412**	**4,362**
Administrative and other expenses	(999)	(1,309)	(1,431)	(1,827)	(2,326)
EBITDA	**754**	**1,086**	**1,177**	**1,585**	**2,035**
Depreciation	(209)	(244)	(327)	(390)	(468)
EBIT	**544**	**841**	**849**	**1,195**	**1,567**
Interest	(53)	(30)	(63)	-	-
Other income	66	82	284	228	310
Profit before tax	**558**	**893**	**1,070**	**1,423**	**1,877**
Tax	(15)	7	(103)	(144)	(370)
Net profit	**542**	**899**	**967**	**1,278**	**1,506**
Minority interest	-				
Net income	**542**	**899**	**967**	**1,278**	**1,506**
Extraordinaries	-	-	-	-	-
Net profit- reported	**542**	**899**	**967**	**1,278**	**1,506**
EPS (Rs/share)	**18.5**	**23.8**	**25.0**	**32.6**	**38.3**
Fully Diluted EPS (Rs/Share)	**17.1**	**22.8**	**24.5**	**32.4**	**38.1**
No of shares outstanding (mn)	29.4	37.8	38.6	39.2	39.3
Fully diluted number of shares (mn)	31.6	39.5	39.5	39.5	39.5
Margins (%)					
Gross profit margin	39.1	40.6	35.8	35.2	34.8
EBITDA margin	16.8	18.4	16.2	16.4	16.3
EBIT margin	12.1	14.3	11.7	12.3	12.5
NPM	12.1	15.2	13.3	13.2	12.0
Growth rates (%)					
Revenues	82.1	31.5	23.4	32.9	29.3
Gross profit	102.8	36.6	8.9	30.8	27.8
EBITDA	204.4	44.0	8.4	34.7	28.4
EBIT	281.1	54.5	1.0	40.7	31.1
Net profit	221.2	65.9	7.6	32.2	17.8
Net income					

Source: Kotak Institutional Equities estimates

Industrials

SUZL.BO, Rs1741	
Rating	IL
Sector coverage view	Attractive
Target Price (Rs)	1,850
52W High -Low (Rs)	1825 - 932
Market Cap (Rs bn)	525.4

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	79.9	131.2	190.6
Net Profit (Rs bn)	8.7	12.5	21.6
EPS (Rs)	30.1	41.4	71.7
EPS gth	*14.4*	*37.8*	*73.1*
P/E (x)	57.9	42.0	24.3
EV/EBITDA (x)	39.6	26.0	16.9
Div yield (%)	0.3	0.3	0.3

Suzlon Energy: Strong performance led by operating leverage; plans for Hansen listing and enhanced capex add catalysts

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- **Beats expectations based on operating leverage led margin expansion because of higher-than-expected execution**
- **Strong order inflows, repeat orders as well as orders from new geographies, builds visibility**
- **Upgraded capacity expansion plan highlights strong global demand environment and Suzlon's intention to gain market share aggressively**
- **Announces plans for listing of Hansen on the London Stock Exchange and capacity expansion to 14,600 MW**
- **Revise estimates based on higher execution and margin expectations, revise target price to Rs1,850 (from Rs1,450 earlier), retain In-Line on strong outperformance recently**

Suzlon beat expectations with consolidated revenues of Rs36.4 bn (up 75% yoy) and PAT of Rs3.9 bn (up 69% yoy). The impressive performance was led by (1) higher execution, (2) reduction in in-transit inventory, (3) resolution of issues at Dhule and Sangli and (4) improvement in tower supplies in the US market. Consolidated EBITDA margins in 2QFY08 were 16.1%, down 110 bps yoy. The margin decline is attributable to (1) one-time restoration costs in Dhule and Sangli, (2) increased hiring for the capacity ramp up and (3) increasing proportion of lower-margin EPC business. Suzlon's order book stands at Rs166 bn and 3,251 MW as of Oct 20, 07, ensuring a visibility of two years based on FY2007 revenues. Suzlon has secured repeat orders as well as orders from new geographies. Suzlon has revised its capacity expansion plans upwards to 3,000 MW (from 1,500 MW earlier), potentially highlighting strong global demand environment. Suzlon plans to list its gearbox subsidiary, Hansen Transmission, on the London Stock Exchange and also proposed to enhance its capacity to 14,600 MW. We revise our estimates based on higher execution based on strong order booking. We revise our target price to Rs1,850 (from Rs1,450 earlier). We retain our In-Line rating on the back of strong outperformance of the stock recently.

Beats expectations based on operating leverage led margin expansion because of higher-than-expected execution

Suzlon has reported consolidated revenues of Rs36.4 bn (up 75% yoy) and PAT of Rs3.9 bn (up 69% yoy) versus our expectation of revenues of Rs34.4 bn and PAT of Rs3.07 bn. Outperformance versus our expectation is based on execution of 688 MW of wind power capacity versus our expectation of 625 MW. On a standalone basis, Suzlon's revenues of Rs16.9 bn were up 31% yoy and PAT at Rs3.6 bn was up 40% yoy. Resolution of problems faced in Dhule and Sangli site as well as tower supply issues in US market are in line with our expectations. The impressive performance (both yoy and qoq) was also aided by reduction in in-transit inventory (from 178 MW in 1QFY08 to 38 MW in 2QFY08, which aided in achieving higher revenues. The consolidated numbers are not comparable on a yoy basis to the extent that (1) the EPC business which was earlier housed in an associate company is now being carried through a 100% owned subsidiary and (2) Repower profit has been consolidated at a PAT level (for the period 6-30 June 07).

Consolidated EBITDA margins in 2QFY08 were 16.1%, down 110 bps yoy and up 890 bps qoq. The yoy margin decline is attributable to (1) one-time restoration costs in Dhule and Sangli, to the extent of Rs660 mn in 1HFY08 (booked in other expenditure), (2) increased hiring for the capacity ramp up (employee costs are up 35%, though as a % of sales they have declined as expected) and (3) increasing proportion of lower-margin EPC business. Effective tax rate in the quarter has declined to 10.3% (from 12.6% a year ago) as some manufacturing facilities were converted in to export oriented units (which enjoy tax benefits on exports). (Exhibits 1 and 2)

Strong order inflows, led by repeat orders from large clients as well as new geographies, builds growth visibility further

Suzlon's order book stands at Rs166 bn and 3,251 MW as of 20 Oct 07, ensuring a visibility of 2 years based on FY07 revenues (Exhibit 3). Suzlon has secured repeat orders from PPM Energy and Edison Mission Group, highlighting the confidence that customers have in Suzlon's products and its delivery capabilities (Exhibit 4). The order book is also diversified in geographical terms, with inclusion of orders from Brazil and Australia (Exhibit 5). It plans to now start booking orders for capacity available in FY2010 and FY2011, highlighting the global demand momentum for wind energy equipment and also Suzlon's position as a major global supplier.

Upgraded capacity expansion plan highlights strong global demand environment and Suzlon's intention to gain market share aggressively

Suzlon has revised its capacity expansion plans in India to 3,000 MW from 1,500 MW earlier (enhancing its global capacity to 5,700 MW by 4QFY09; facilities are expected to come on-stream gradually between 1Q09 to 3Q09). The doubling of the capacity expansion plan highlights Suzlon's intention to aggressively add capacity to gain market share from global leaders such as Vestas. Vertically integrated capacity expansion with facilities for various components spread over Kandla, Vadodara, Coimbatore and Udupi further insulate Sizlon from vagaries form component supply issues (Exhibit 6). All facilities are located in SEZs, enabling Suzlon to avail of tax benefits and keep the effective tax rates low beyond the earlier expected FY2009E. Suzlon will hence be able to cater to the global demand, from its low-cost Indian manufacturing base.

De-bottlenecking capacity for Repower by leveraging Suzlon's vertically integrated components manufacturing capabilities

Repower's capacity is expected to be enhanced to 1,700 MW by 2008 (from 1,200 MW). Repower is largely design and assembly focused, sourcing components from various suppliers and hence, supply chain constraints pose the major challenge in its capacity expansion plans. Suzlon proposes to leverage its integrated supply chain and enhance Repower's capacity. It plans to supply blades from India and gearboxes through Hansen. This will enable Suzlon to cater to the large European market (with relatively lower sales for Suzlon, compared to the US and India) through Repower. Repower is also moving closer to its goal of serial production of 5 MW offshore wind turbine with total orders for about 75 MW of offshore wind turbines.

Plans for listing of Hansen on the London Stock Exchange and capacity expansion to 14,600 MW

Suzlon plans to list its gearbox subsidiary, Hansen Transmission, on the London Stock Exchange. As highlighted in our earlier note (on 18 Sep 07), we believe the listing decision is led by (1) value unlocking for Hansen's gear box business when wind power equipment industry is going through component supply crunch, particularly since Hansen supplies to Suzlon's customers as well, (2) management of Suzlon's debt-equity ratio, particularly when it is on a large capacity expansion program and also needs to pay Martifer and Areva for acquisition of Repower's stake and (3) funding the capacity expansion at Hansen (to 14,600 MW from 3,600 at the end of FY07, with an investment of EUR600 mn). The massive capacity expansion program at Hansen further highlights Suzlon's strong belief of significant growth in global wind energy and also the shortage of gearbox supply globally.

Revise estimates based on higher execution, revise target price to Rs1,850 (from Rs1,450 earlier)

We have revised our total deliveries by Suzlon in FY2008 and FY2009 to 2,370MW and 3,410 MW from 2,295MW and 3,116 MW earlier based on strong execution and order book position. We revise our FY2008E to Rs41.4 (from Rs46 earlier) and FY2009E EPS upwards by about 12% to Rs71.7 (from Rs63.1 earlier) (Exhibit 5 and 6). Our EPS is based on full dilution of recently issued foreign currency convertible bonds. We revise our target price to Rs1,850/share from Rs1,450 earlier. Our target price is based on about 25.5X FY2009E earnings which is about 5% discount to traded FY2009E P/E multiple for industrial sector coverage universe. (Exhibits 7-9).

Retain Inline rating on back of recent strong performance even though we believe in Suzlon's positioning to gain from favorable demand momentum

We reiterate our Inline rating on the back of strong stock performance in recent times. Key upside risks arise from (1) valuation of Hansen on listing, (2) global momentum in wind power equipment demand which creates opportunities for Suzlon to grow rapidly while gaining market share and leverage the benefits of vertically integrated manufacturing as well as broad geographical presence. Key downside risks arise from (1) rupee appreciation (10% rupee appreciation potentially effect margins by 150-200 bps), (2) supply chain constraints (that continue to confront the industry globally) hindering execution, (3) delays in execution of the large capacity expansion plans, across Suzlon, Hansen and Repower, (4) emergence of competitors (attracted by the high equity returns), especially from low-cost manufacturing countries like China and (5) new technologies, like gearless wind-turbines, becoming more competitive.

Exhibit 1. Suzlon Energy - 2QFY08 standalone results (Rs mn)

			yoy			qoq			yoy		
	FY07	FY08E	2QFY08	2QFY07	% change	2QFY08	1QFY08	% change	1HFY08	1HFY07	% change
Income from operations	**53,804**	**94,623**	**16,875**	**12,855**	**31.3**	**16,875**	**8,392**	**101.1**	**25,267**	**22,192**	**13.9**
Total Expenditure	(41,861)	(76,008)	(13,013)	(9,832)	32.4	(13,013)	(7,264)	79.1	(20,278)	(16,776)	20.9
(Increase) / Decrease in stock in trade	686	-	532	458	16.1	532	1,452	(63.4)	1,984	1,437	38.0
Raw material consumption	(33,011)	(58,653)	(10,580)	(8,316)	27.2	(10,580)	(6,276)	68.6	(16,856)	(14,686)	14.8
Staff cost	(1,115)	(2,488)	(328)	(286)	14.8	(328)	(336)	(2.4)	(664)	(487)	36.3
Other expenditure	(8,421)	(14,867)	(2,637)	(1,688)	56.2	(2,637)	(2,105)	25.3	(4,742)	(3,040)	56.0
Operating profit	**11,943**	**18,615**	**3,861**	**3,023**	**27.7**	**3,861**	**1,128**	**242.4**	**4,989**	**5,416**	**(7.9)**
Other income	881	1,117	313	127	146.2	313	237	31.9	550	256	114.5
EBIDTA	12,824	19,732	4,174	3,150	32.5	4,174	1,365	205.8	5,539	5,672	(2.4)
Interest	(893)	(1,702)	(282)	(210)	34.1	(282)	(289)	(2.4)	(571)	(374)	52.9
Depreciation	(735)	(1,176)	(190)	(164)	16.1	(190)	(177)	7.5	(367)	(313)	17.3
Profit before tax	11,196	16,855	3,702	2,776	33.4	3,702	899	311.9	4,600	4,986	(7.7)
Tax	(584)	(2,261)	(146)	(241)	(39.5)	(146)	(5)	3,067.4	(150)	(515)	(70.8)
Net profit	**10,611**	**14,593**	**3,556**	**2,535**	**40.3**	**3,556**	**894**	**297.7**	**4,450**	**4,471**	**(0.5)**
Extraordinary items	-	-	-	-		-	-		-	-	
Reported profit	**10,611**	**14,593**	**3,556**	**2,535**	**40.3**	**3,556**	**894**	**297.7**	**4,450**	**4,471**	**(0.5)**
Key ratios											
Material cost	60.1	62.0	59.5	61.1		59.5	57.5		58.9	59.7	
Staff cost	2.1	2.6	1.9	2.2		1.9	4.0		2.6	2.2	
Other expenditure	15.7	15.7	15.6	13.1		15.6	25.1		18.8	13.7	
OPM	**22.2**	**19.7**	**22.9**	**23.5**		**22.9**	**13.4**		**19.7**	**24.4**	
EBIDTA margin	23.8	20.9	24.7	24.5		24.7	16.3		21.9	25.6	
Pre-tax margin	20.8	17.8	21.9	21.6		21.9	10.7		18.2	22.5	
Tax rate	5.2	13.4	3.9	8.7		3.9	0.5		3.3	10.3	
PAT margin	19.7	15.4	21.1	19.7		21.1	10.7		17.6	20.1	
MW delivered											
Domestic	955	1,064	238	216	10.2	238	125	90.4	363	386	(6.0)
Export	501	1,307	445	172	158.7	445	192	131.8	637	198	221.7
Total	**1,456**	**2,370**	**683**	**388**	76.0	**683**	**317**	**115.5**	**1000**	**584**	71.2

Source: Company data, Kotak institutional equities estimates.

Exhibit 2. Suzlon Energy - 2QFY08 consolidated results (Rs mn)

			yoy			qoq			yoy		
	FY07 Cons	FY08E Cons	2QFY08	2QFY07	% change	2QFY08	1QFY08	% change	1HFY08	1HFY07	% change
Income from operations	**79,858**	**131,200**	**36,413**	**20,870**	**74.5**	**36,413**	**19,446**	**87.2**	**55,859**	**31,560**	**77.0**
Total Expenditure	(66,898)	(109,937)	(30,543)	(17,270)	76.9	(30,543)	(18,048)	69.2	(48,592)	(26,100)	86.2
(Increase) / Decrease in stock in trade	3,936	-	(2,841)	578	(591.4)	(2,841)	2,323	(222.3)	(518)	-	
Raw material consumption	(52,054)	(81,344)	(20,689)	(13,882)	49.0	(20,689)	(14,501)	42.7	(35,190)	(18,990)	85.3
Staff cost	(6,501)	(9,949)	(2,271)	(1,684)	34.9	(2,271)	(2,228)	1.9	(4,499)	(2,860)	57.3
Other expenditure	(12,280)	(18,644)	(4,743)	(2,282)	107.9	(4,743)	(3,642)	30.2	(8,385)	(4,250)	97.3
Operating profit	**12,960**	**21,263**	**5,870**	**3,600**	**63.0**	**5,870**	**1,398**	**319.9**	**7,268**	**5,460**	**33.1**
Other income	967	1,287	535	69	672.5	535	426	25.4	961	250	284.4
EBIDTA	13,927	22,550	6,404	3,669	74.5	6,404	1,824	251.0	8,229	5,710	44.1
Interest	(2,520)	(5,020)	(1,387)	(547)	153.4	(1,387)	(1,079)	28.5	(2,466)	(910)	170.9
Depreciation	(1,733)	(2,472)	(583)	(428)	36.2	(583)	(585)	(0.3)	(1,168)	(790)	47.9
Profit before tax	9,675	15,058	4,434	2,694	64.6	4,434	161	2,662.7	4,595	4,010	14.6
Tax	(1,035)	(2,561)	(457)	(340)	34.3	(457)	40		(417)	(690)	(39.6)
Net profit	**8,641**	**12,497**	**3,978**	**2,354**	**69.0**	**3,978**	**200**	**1,885.9**	**4,178**	**3,320**	**25.8**
Key ratios											
Material cost	60.3	62.0	64.6	63.7		64.6	62.6		63.9	60.2	
Staff cost	8.1	7.6	6.2	8.1		6.2	11.5		8.1	9.1	
Other expenditure	15.4	14.2	13.0	10.9		13.0	18.7		15.0	13.5	
OPM	**16.2**	**16.2**	**16.1**	**17.3**		**16.1**	**7.2**		**13.0**	**17.3**	
EBIDTA margin	17.4	17.2	17.6	17.6		17.6	9.4		14.7	18.1	
Pre-tax margin	12.1	11.5	12.2	12.9		12.2	0.8		8.2	12.7	
Tax rate	10.7	17.0	10.3	12.6		10.3	(24.8)		9.1	17.2	
PAT margin	10.8	9.5	10.9	11.3		10.9	1.0		7.5	10.5	
MW delivered											
Domestic	955	1,064	238	173	37.6	238	125	90.4	363	386	(6.0)
Export	501	1,307	445	25	1,680.0	445	192	131.8	637	198	221.7
Total	**1,456**	**2,370**	**683**	**198**	244.9	**683**	**317**	115.5	**1000**	**584**	71.2

Source: Company data, Kotak institutional equities estimates.

Exhibit 3. Suzlon sales and order book data in MW and Rs mn

			1Q07	2Q07	3Q07	4Q07	1Q08	2Q08
Order book	Physical MW	Domestic	207	206	372	267	315	369
		Export	610	1,237	1,271	1,692	2,567	2,882
		Total	**817**	**1,443**	**1,643**	**1,958**	**2,882**	**3,251**
	Rs mn	Domestic	8,000	8,242	15,443	14,083	17,100	19,889
		Export	29,590	58,137	61,719	80,780	117,900	143,392
		Total	**37,590**	**66,379**	**77,162**	**94,863**	**135,000**	**163,280**
Sales	Physical MW	Domestic	171	216	190	379	125	238
		Export	25	172	149	154	192	445
		Total	**196**	**388**	**339**	**533**	**317**	**683**

Source: Company data, Kotak Institutional Equities

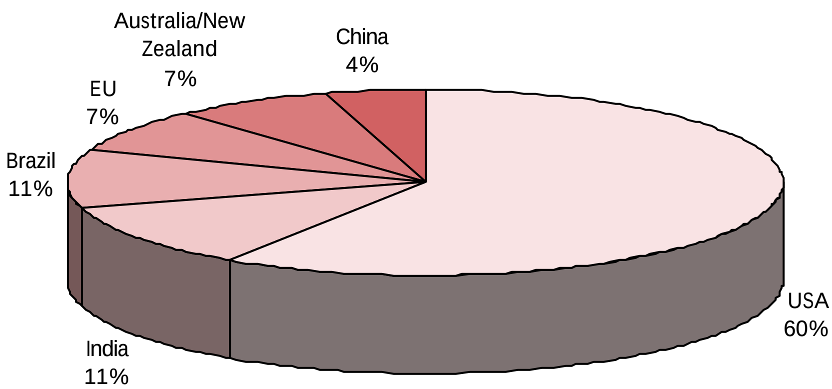
Exhibit 4. Order inflows for Suzlon from FY07 onwards have remained strong

Major orders booked by the Suzlon group from FY2007 so far

Announcement date	Customer	Capacity (MW)	Delivery schedule (MW)		
			CY07	CY08	CY09
8-Oct-07	Horizon Wind of Houston, Texas, USA	400.0	-	200.0	200.0
5-Oct-07	Servtec Instalacoses E Sistemas Integrados Ltda, Brazil	155.0	-	155.0	-
3-Oct-07	DLF Limited, India	150.0	-	150.0	-
27-Sep-07	Ayen Enerji Co. Inc, Turkey	31.5	-	31.5	-
29-Jun-07	PPM Energy of Portland, Oregon, USA	300.0	-	-	300.0
6-Jun-07	Edison Mission Group of Irvine, California, USA	630.0	-	315.0	315.0
3-May-07	PPM Energy of Portland, Oregon, USA	400.0	-	300.0	100.0
10-Apr-07	Tierra Energy of Austin, Texas, USA	88.2	-	88.2	-
6-Mar-07	Reliance Energy Limited, India	150.0	112.5	37.5	-
29-Jan-07	British Petroleum	40.0	40.0	-	-
29-Jan-07	Snowtown Wind Farm Pty Ltd, Australia	88.2	88.2	-	-
27-Oct-06	China	50.0	50.0	-	-
13-Oct-06	SIIF Energies do Brasil Ltda, Brazil	225.0	150.0	75.0	-
18-Sep-06	John Deere Wind Energy, USA	247.0	247.0	-	-
4-Sep-06	Edison Mission Group of Irvine, California, USA	105.0	52.5	52.5	-
23-Aug-06	Maestrale Green Energy, Italy	21.0	21.0	-	-
23-Aug-06	Tecneira - Technologias Energeticas SA, Portugal	39.9	39.9	-	-
18-Jul-06	Datang International	40.0	40.0	-	-
18-Jul-06	Edison Mission Group of Irvine, California, USA	105.0	52.5	52.5	-
	Total large order booking from FY2007 so far	**3,265.8**	**893.6**	**1,457.2**	**915.0**

Source: Company, Kotak Institutional equities estimates.

Exhibit 5. Suzlon has managed to diversify its order book through orders from Brazil and Australia
Geographical break-up of order book



Source: Company data

Exhibit 6. Details of incremental capital expenditure program of Suzlon Energy

Expected utilisation of funds	Locations	Approx Incremantal capex (Rs bn)	Capacity	Timeline for completion
Forging unit for components	Vadodra, Gujarat	11.0	70,000 MT	2QFY09
Forging and Foundary unit for components	South India		120,000 MT	2QFY09
WTG manufacturing facility in SEZs	(Udupi, Coimbatore, Vadodara, Kandla)	15.0	3000 MW	Q1FY09-Q3FY09
Hansen Transmission	Belgium	8.2	2300 MW	4QFY08
Hansen Transmission	India	9.8	3500 MW	4QFY09
Total		**44.0**		

Source: Company data, Kotak Insttutional Equities estimates

Exhibit 7. Segmental numbers for Suzlon Energy Ltd. (Rs mn)

Wind business						
	2QFY08	**2QFY07**	**% YoY**	**FY07**	**FY2008E**	**FY2009E**
MW sales	**683**	**388**	**76**	**1,456**	**2,370**	**3,410**
Domestic	238	216	10	955	1,064	1,223
Export	445	172	159	501	1,307	2,186
Sales	30,830	16,504	87	61,300	108,000	161,630
EBITDA	4,890	3,073	59	10,210	17,783	29,408
EBITDA margin	**15.9**	**18.6**		**16.7**	**16.5**	**18.2**
Realisation per MW	45.1	42.5	6.1	42.1	45.6	47.4
Hansen Transmission						
Sales	5,276	4,368	20.8	18,560	23,200	29,000
EBITDA	653	472	38.4	2,770	3,480	4,640
EBITDA margin	**12.4**	**16.7**		**14.9**	**15.0**	**16.0**
Consolidated						
Sales	36,410	20,872	74.4	79,860	131,200	190,630
EBITDA	5,870	3,545	65.6	12,980	21,263	34,048
EBITDA margin	**16.1**	**17.0**		**16.3**	**16.2**	**17.9**

Source: Company data, Kotak Insttutional Equities estimates

Exhibit 8. Profit Model (consolidated) of Suzlon, March year-ends, 2005-2009E (Rs mn)

	2005	2006	2007	2008E	2009E
Net revenues	**19,425**	**38,410**	**79,857**	**131,200**	**190,630**
Total RM & erection exps	(11,377)	(23,091)	(48,114)	(81,344)	(118,190)
Employee expenses	(618)	(1,216)	(6,496)	(9,949)	(12,789)
Preliminary expenses w/o	(2)	0	0	0	0
Other expenses (admin)	(2,533)	(5,263)	(12,032)	(18,644)	(25,603)
Total expenditure	(14,530)	(29,570)	(66,641)	(109,937)	(156,582)
Operating profit	**4,895**	**8,840**	**13,216**	**21,263**	**34,048**
Other income	234	556	965	1,287	1,581
EBIDTA	5,130	9,397	14,181	22,550	35,630
Interest	(458)	(508)	(2,763)	(5,020)	(6,221)
PBDT	4,671	8,889	11,418	17,530	29,408
Depreciation	(424)	(716)	(1,735)	(2,472)	(3,781)
Amortisation of VRS expenses					
PRETAX PROFITS	**4,248**	**8,173**	**9,683**	**15,058**	**25,627**
Tax (incl deferred tax provision)	(391)	(568)	(1,035)	(2,561)	(3,985)
PAT (A)	**3,856**	**7,605**	**8,648**	**12,497**	**21,642**
Adj for minority interest etc	2	42	(7)	(7)	(7)
Preference dividend	(20)	(20)	-	-	-
Extraordinary items, net of tax	(1)	0	-	-	-
PAT (R)	**3,858**	**7,605**	**8,648**	**12,497**	**21,642**
Per share (Rs)					
EPS	**44.2**	**26.4**	**30.0**	**43.4**	**75.2**
% of sales					
Raw material & erection expenses	58.6	60.1	60.2	62.0	62.0
Employee expenses	3.2	3.2	8.1	7.6	6.7
Other expenses	13.0	13.7	15.1	14.2	13.4
OPM	25.2	23.0	16.5	16.2	17.9
Pre-tax margin	21.9	21.3	12.1	11.5	13.4
PAT margin	19.9	19.8	10.8	9.5	11.4
Effective tax rate	9.2	7.0	10.7	17.0	15.5
Dividend payout ratio	9.0	19.1	16.7	11.5	6.6
Div tax rate	14.7	14.3	14.7	17.0	17.0
Growth (%)					
Net revenues	126.5	97.7	107.9	64.3	45.3
PAT	292.2	97.6	13.9	44.6	73.2
EPS	9.8	(40.3)	13.8	44.6	73.2
Weighted avg. shares o/s (mn)	55.6	187.2	287.6	287.8	287.8
Period end outstanding shares (mn)	86.9	287.5	287.8	287.8	287.8

Source: Company data, Kotak Institutional Equities Estimates

Exhibit 9. Balance sheet model (consolidated) of Suzlon, March year-ends, 2005-2009E (Rs mn)

	2005	2006	2007	2008E	2009E
Share capital	869	2,875	2,878	2,878	2,878
Reserves & surplus	7,089	24,323	32,233	43,047	63,006
Total shareholders funds	**7,958**	**27,198**	**35,111**	**45,925**	**65,883**
Preference capital	1,153	175	25	25	25
Minority interest	0	75	141	141	141
Secured loans	3,567	3,899	19,844	15,844	24,844
Unsecured loans	391	608	31,776	51,776	51,776
Total debt	**3,958**	**4,507**	**51,620**	**67,620**	**76,620**
Total liabilities	**13,069**	**31,955**	**86,897**	**113,710**	**142,669**
Gross block	3,597	6,293	25,582	37,080	67,080
Less: accum. depreciation	(808)	(1,536)	(7,016)	(9,488)	(13,269)
Net block	**2,789**	**4,757**	**18,566**	**27,591**	**53,810**
Capital work in progress	289	1,668	4,498	15,000	5,000
Investments	78	76	156	156	156
Current assets	17,477	41,705	84,526	114,579	154,999
of which, cash	1,545	5,515	15,383	6,743	928
Less: Current liabilities	7,809	17,078	38,339	61,107	88,786
Net current assets	**9,668**	**24,627**	**46,187**	**53,472**	**66,212**
Misc expenses	4	9	39	39	39
Deferred tax assets	241	818	(177)	(177)	(177)
Total assets	**13,069**	**31,955**	**86,897**	**113,710**	**142,669**
Key ratios					
BVPS	91.5	94.6	122.0	159.6	229.0
Fixed asset T/O ratio	2.0	2.0	0.9	0.7	0.7
RoE	66.7	43.2	27.7	30.8	38.7
RoCE	44.4	35.8	18.7	16.6	21.0

Source: Company data, Kotak Institutional Equities Estimates

Economy

Sector coverage view	N/A

Sixth Pay Commission—blow for fiscal gains; bonanza for select sectors (automobile, consumer products and real estate)

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- **Expect Rs1,211 bn additional disposable income in the hands of Indians during FY2009-11 as a result of the Sixth Pay Commission report likely in early FY2009**
- **Increased wages and salaries could wipe out State fiscal gains made in recent years**
- **Windfall could boost automobiles, consumer durables and real estate stocks**

Payments to government employees to the tune of Rs1,211 bn are likely to boost consumer spending significantly in the next 4-5 years, while hitting Centre and State finances with an additional wage bill of Rs513 bn and Rs698 bn, respectively. We expect the Sixth Pay Commission report to be announced in early FY2009. A large part of these arrears are likely to be given to government employees through one-time bullet payments, which we believe will likely find their way into housing, consumer durables and a bit in non-durables as well. Sectors likely to benefit from this bonanza are automobiles, consumer durables and real estate. Investors with a 3-5-year horizon could gain from staying invested in these stocks during any correction which may follow in the near term.

Historical precedents bode well for market but not for fisc

When the Fifth Pay Commission submitted its report in 1997, the fisc went haywire even as the bonanza contributed to consumer spending. History repeats itself. Fiscal gains could be reversed by the payouts though, on the flip side, the resultant higher discretionary income could change the fortunes of quite a few companies.

Sixth Pay Commission report likely in early FY2009; implementation a tangled web

We expect the Sixth Pay Commission report to submit its report sometime in 1QFY09. However, the Left could strongly oppose some recommendations (like administrative reforms, downsizing of government, performance-related pay), compelling the government to water down some proposals. Expect percentage wage revisions of the 3/4th of the size we saw in case of the fifth pay commission with symbolic administrative reforms. We believe the Congress would be keen to announce the windfall before the summer of 2009, preceding general elections. As in the past, we expect the financial impact of the Sixth Pay Commissions to increase exponentially (see Exhibit 1).

Burden manageable for Centre; tough for States

From FY2003, there has been a distinct improvement in fiscal position of the Centre and the states. The combined deficit fell to 6.4% last year and is budgeted at 5.6% this year (Exhibit 2).

- **Centre's wage bill to climb, but fisc manageable.** The centre's wage bill is expected to climb by about 70% over the three-year period ending FY2011 as result of the Sixth Pay Commission bonanza. Following the non-implementation of reforms suggested by the Fifth Pay Commission, the Sixth may insist that an increase of about 70% be linked to administrative reforms, with a lower increase of about 35% could suggested for the interim. We expect the latter scenario to come to pass given the impending elections, moderating our expectation of the financial impact on the Centre at Rs380 bn for salaries and wages by FY2011 (Rs513 bn including spillovers of wage hikes to departmental commercial undertakings). GFD is likely to remain in the range of 3.0-3.5% of GDP in the three years after the Sixth Pay Commission award.

- **Fisc gains for States could be washed away.** The less resilient state governments could see their fiscal gains of the past three years wiped out—reversing their GFD/GDP ratio improvements (currently 2.7%, could rise to 3.5%). We expect the State's wage bill to rise more moderately at 8-10% each in FY2008 and FY2009, but as much as 15-20% in each of the succeeding two years (Exhibit 3). We anticipate the total wages and salaries bill for the States to rise by 50% in the three years to FY2011, modest compared to the 90% hike seen at the time of the Fifth Pay Commission. Even this modest increase, however, would be enough to pump in close to Rs700 bn of increased disposable income to state government employees.

Likely release of pent-up demand to propel automobiles, consumer durables, real estate

Contrary to traditional economic theory which maintains that the propensity to save is higher in the case of transitory income, observed behaviour has been that transitory income, especially in the form of windfall gains, prompts consumers to spend more to meet their pent up demand for consumer durables such as cars, refrigerators, TVs (LCD or plasma?), laptops, etc or for real estate acquisitions. We could see a significant turnaround in fortunes of the stocks of firms in these sectors.

- **Automobiles**. Our automobiles analyst believes three factors make the sector attractive for investors with a 3-5-year horizon—(1) the positive impact of the Sixth Pay Commission, (2) rising income levels and (3) lower interest rates. Regarding the first potential catalyst, our analysis suggests the following: (1)At a conservative estimate, 10 per cent of the additional disposable income (about Rs90 bn) could go towards auto sales of which at least 3/4ths could go towards four-wheelers, mainly car sales. (2) At a price point of Rs0.3-0.4 mn for entry-level cars, the Sixth Pay Commission would lead to an additional demand of 0.5 mn cars. (3) We expect car sales to increase by 6% annually after the sixth commission payouts, taking annual passenger-car volumes past the 2 mn mark by FY2011.
- **Real estate**. As stock prices correct in this sector, our real estate analyst believes that a huge buying opportunity could emerge on the back of the surge in disposable income and elevated salary levels. This could, in turn, help service EMI's better and so boost demand. It would act as a catalyst for the sector, which has in recent times been hit by restrictions on ECB finance, decelerated credit availability from banks and plateauing of real estate prices in key urban areas.
- **Consumer durables**: The impact of the Sixth pay commission award on the consumer durables sector could be relatively moderate, but positive nevertheless. consumer durables stocks have been trailing market benchmarks of late and conventional wisdom in times has advised staying away from these stocks. In spite of their underperformance, their fortunes could change with a good monsoon this year followed by the expected pay commission bonanza. The impact on fast moving consumer electronics, an important subset of consumer durables, could be huge. Demand for innovative electronic products such as MP3 players, digital cameras, laptops and household white/ brown goods such as refrigerators, TVs, stereos, etc could rise. The impact on the processed food industry could be relatively lower.

Exhibit 1: Financial impact rises 10 fold each successive pay commission

Financial impact of successive pay commissions

	Constituted	Submitted	Estimated financial impact (Rs bn)
First Pay Commision	May-1946	1946 (month n.a.)	n.a.
Second Pay Commision	Aug-1957	Aug-1959	0.40
Third Pay Commision	Apr-1970	Mar-1973	1.45
Fourth Commision	Jun-1983	3 reports till 1987	12.82
Fifth Pay Commision	Apr-1994	Jan-1997	170.00
Sixth Pay Commision	Oct-2006	-	1362.00 (Projected)

Source: GOI.

Exhibit 2: Fiscal gains of last 5-years: would they again go askew?

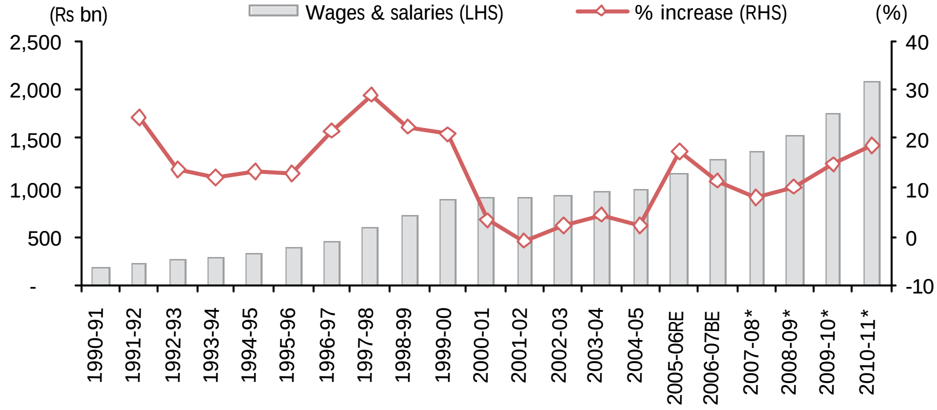
Fiscal deficits of Centre & States as % of GDP

	Centre			States			Combined		
	Gross fiscal deficit (GFD)	Gross primary deficit (GPD)	Revenue deficit (RD)	Gross fiscal deficit (GFD)	Gross primary deficit (GPD)	Revenue deficit (RD)	Gross fiscal deficit (GFD)	Gross primary deficit (GPD)	Revenue deficit (RD)
1995-96	5.07	0.86	2.50	2.65	0.80	0.69	6.54	1.57	3.19
1996-97	4.88	0.53	2.39	2.72	0.85	1.18	6.38	1.25	3.56
1997-98	5.84	1.53	3.05	2.90	0.93	1.07	7.27	2.13	4.12
1998-99	6.51	2.04	3.85	4.27	2.20	2.51	9.02	3.67	6.35
1999-00	5.36	0.74	3.46	4.69	2.37	2.76	9.47	3.81	6.22
2000-01	5.65	0.93	4.05	4.26	1.80	2.55	9.51	3.57	6.60
2001-02	6.18	1.47	4.39	4.21	1.47	2.59	9.93	3.68	6.99
2002-03	5.90	1.11	4.39	4.15	1.30	2.24	9.56	3.09	6.63
2003-04	4.46	-0.03	3.55	4.45	1.49	2.21	8.48	2.05	5.76
2004-05	4.02	-0.04	2.51	3.49	0.68	1.16	7.51	1.36	3.67
2005-06	4.11	0.39	2.59	2.52	0.12	0.08	6.71	0.94	2.66
2006-07(RE)	3.69	0.15	2.02	2.77	0.40	0.03	6.41	0.79	2.05
2007-08(BE)	3.26	-0.17	1.54	2.37	0.10	-0.37	5.57	0.11	1.17

Source: Reserve Bank of India.

Exhibit 3: Relatively modest increase in wages & salaries of state governments could take their wage bill from Rs1,279 bn budgeted for FY2007 to Rs2,080 bn in FY2011

Expenditure on wages & salaries by state governments



Source: Projections based on State Finances data.

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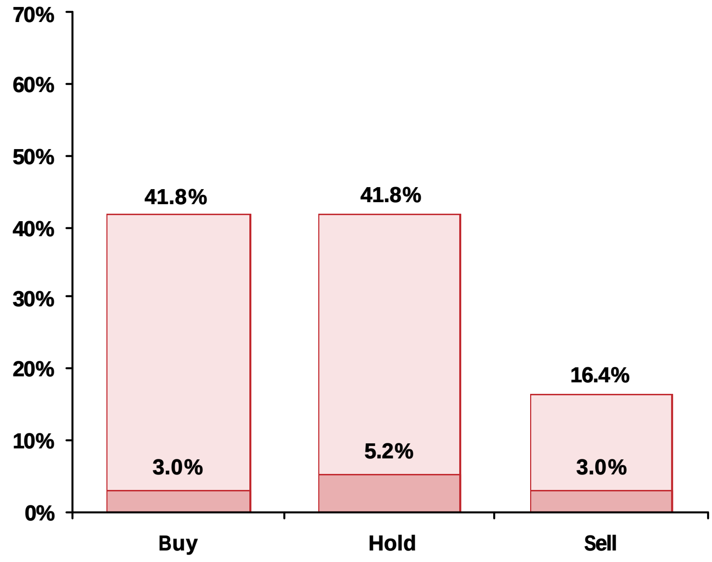

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Source: Kotak Institutional Equities. As of September 30, 2007

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