

Contents

New Release

Real Estate: Skyline hits the ceiling

News Roundup

Corporate

- The country's largest private insurer ICICI Lombard has bagged a contract from the railways to provide personal accident cover at a premium of just 4.75 paise per passenger. The personal cover is for a year starting from September 20, 2007. (BS)
- Lupin has acquired Rubamin Laboratories, a contract research and production firm, for an undisclosed sum. (BS)
- After the opposition to its retail stores, Reliance Fresh is learnt to be shelving its proposed Rs13,000-crore rollout in the stakes, putting 10,000 jobs at stake. (BS)
- New Delhi-based IT company NIIT technologies is learned to be in preliminary discussions with private equity players Carlyle and TPG to sell a majority stake. (ET)
- Reliance Retail is investing about Rs1,500 crore for setting up 1,800 pharmacy stores across the country over the next 4 years. (FE)
- MTNL has submitted a bid to acquire Sri Lanka-based fixed-line wireless operator Sutel. (BS)
- Prime Focus, a Mumbai-based post production services provider, has bought Ronnie Screwvala-promoted UTV Software Communications' post-production business. UTV decided to hive off its post production unit in a bid to save costs and focus on its core business of developing content. (BS)

Economic and political

- "It is only a matter of time before the policy is tweaked to allow FDI in retail," Finance Minister P Chidambaram told students of Wharton School of University of Pennsylvania. (FE)
- The European Central Bank's emergency lending fund, which attracts a penal interest rate, was tapped on Wednesday for E3.9 billion. The surge in demand for the ECB's 'marginal lending facility' pointed to the difficulties still being faced by European banks as a result of the global credit squeeze. (FT)

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

EQUITY MARKETS

India	Change, %			
	27-Sep	1-day	1-mo	3-mo
Sensex	17,151	1.4	15.0	18.2
Nifty	5,001	1.2	15.7	16.8
Global/Regional indices				
Dow Jones	13,913	0.3	6.7	3.7
Nasdaq Composite	2,710	0.4	8.4	3.9
FTSE	6,486	0.8	6.3	(1.3)
Nikkie	16,785	(0.3)	3.1	(6.4)
Hang Seng	27,052	(0.1)	15.8	23.3
KOSPI	1,941	(0.2)	6.1	10.8
Value traded - India				
		Moving avg, Rs bn		
	27-Sep	1-mo	3-mo	
Cash (NSE+BSE)	282.8	182.0	169.8	
Derivatives (NSE)	862.3	527.5	562.6	
Deri. open interest	1,060.2	851.6	809.9	

Forex/money market

	Change, basis points			
	27-Sep	1-day	1-mo	3-mo
Rs/US\$	39.7	-	(145)	(112)
6mo fwd prem, %	0.7	(25)	71	24
10yr govt bond, %	7.9	(5)	(1)	(28)

Net investment (US\$m)

	26-Sep	MTD	CYTD
	FIs	246	3,193
MFs	(108)	(92)	669

Top movers -3mo basis

Best performers	Change, %			
	27-Sep	1-day	1-mo	3-mo
Reliance Energy	1,117	8.9	45.8	92.4
Neyveli Lignite	104	(3.2)	38.9	72.1
Tata Tele	44	(0.1)	38.8	70.6
Chambal Fert	55	(4.9)	16.6	58.4
SAIL	201	0.5	31.4	53.2
Worst performers				
i-Flex	1,894	2.0	(6.0)	(25.4)
Polaris	123	5.0	10.0	(19.3)
Novartis India	308	(1.0)	9.7	(17.6)
Punjab Tractors	236	(4.2)	2.6	(17.0)
Glaxosmithkline	1,116	(0.7)	(1.6)	(14.1)

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Real Estate

Sector coverage view

Neutral

Company	Rating	Price, Rs	
		27-Sep	Target
DLF	OP	742	750
Unitech	L	314	305
MGesco	OP	609	920
Sobha	L	856	870

Skyline hits the ceiling

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- **Declining affordability to trigger price correction despite strong housing demand**
- **Initiate coverage on Unitech with target price of Rs305 and IL rating**
- **Lower our rating on Sobha Developers to IL; target price of Rs870**

Skyline hits the ceiling. We believe current street expectations of high volume growth along with high prices of real estate are unlikely to pan out. We expect prices of residential property to correct to the tune of 10% over the next few months. We adjust valuations of our companies and initiate coverage on Unitech with an In-Line rating and target price of Rs305.

Declining affordability to trigger price correction despite strong housing demand

The slowdown in home loan disbursements, among other factors, underpins our view that the residential real estate market has slowed down considerably. Thus, current expectations of high volume growth as well as high residential prices are unlikely to pan out. We remain bullish on demand on account of rapidly improving demographics (rising urban income, young population) and growing urbanization. On the pricing front, we forecast a correction of 10% from current prices in the next 12 months but do not rule out steeper correction.

We initiate coverage on Unitech with an IL rating and target price of Rs305

We estimate the March 2009 NAV for Unitech at Rs275/share. Unitech's residential division has the largest volumes under development amongst Indian listed real estate companies with more than 25 mn sq. ft under construction in National Capital Region and Kolkata. Unitech has access to a low-cost land bank of 480 mn sq. ft across 14 cities. Our target price leaves little upside from current levels and we initiate coverage with an In-Line rating.

We lower our rating on Sobha Developers to IL; target price of Rs870

We rework our NAV estimate for Sobha and DLF for a 10% reduction in selling price in the next 12 months. Our new fair price for Sobha Developers, based on March 2009 NAV, is Rs870/share and we change our rating to In-Line (Outperform previously). Our revised target price for DLF is Rs750/share (Rs705 previously) based on a 15% premium (5% earlier) to our March 2009-based NAV of Rs646.

Key risks: Property prices, interest rates, economic growth, land purchase

(a) A sharper-than-expected decline in property prices could derail our earnings forecasts; property prices have risen sharply over the past two years and the business is cyclical; (b) Any further increase in interest rates may curtail demand for housing—housing finance companies have raised lending rates by 350-400 bps over the past 24 months; (c) Any unexpected slowdown in economic growth in India may also result in lower-than-expected demand for both retail and commercial real estate; and (d) Real estate companies may not be able to acquire land at reasonable prices in the future because of increased competition from other real estate developers.

We estimate March 2009E NAV for Unitech at Rs275/share

NAV sensitivity for various growth rate in selling prices (Rs bn)

	March '09 based NAV			
	Growth rate in selling prices			
	0%	3%	5%	10%
Valuation of land reserves	294	378	440	621
Residential projects	168	222	262	383
Commercial projects	64	80	91	124
Retail projects	63	76	86	115
Add: Hotel business	15	15	15	15
Add: Construction business	10	10	10	10
Add: Investments as on March 31, 2008	10	10	10	10
Add: Fees received from Unitech Corporate Parks	5	5	5	5
Less: Net debt as on March 31, 2008	(23)	(23)	(23)	(23)
Less: Land cost to be paid as on March 31, 2008	(10)	(10)	(10)	(10)
NAV	302	385	447	629
Total no. of shares (mn)				1,624
NAV/share (Rs)				275

Source: Kotak Institutional Equities

We estimate March 2009E NAV for DLF at Rs646/share

NAV sensitivity for various growth rate in selling prices (Rs bn)

	March '09 based NAV			
	Growth rate in selling prices			
	0%	3%	5%	10%
Valuation of land reserves	767	946	1,084	1,505
Residential projects	268	357	427	652
Commercial projects	266	306	335	416
Retail projects	233	284	322	437
Add: 22 Hotel sites	25	25	25	25
Add: Construction JV	20	20	20	20
Add: Other properties (plots in Gurgaon - 7.2 mn sq. ft, hotel site in Gurgaon)	22	22	22	22
Add: Investments as on March 31, 2008	20	20	20	20
Less: Net debt as on March 31, 2008	(28)	(28)	(28)	(28)
Less: Land cost to be paid as on March 31, 2008	(30)	(30)	(30)	(30)
NAV	795	975	1,112	1,533
Total no. of shares including ESOPs of 17 mn shares (mn)				1,722
NAV/share (Rs)				646

Source: Kotak Institutional Equities

We estimate March 2009E NAV for Sobha at Rs867/share

NAV sensitivity for various growth rate in selling prices (Rs bn)

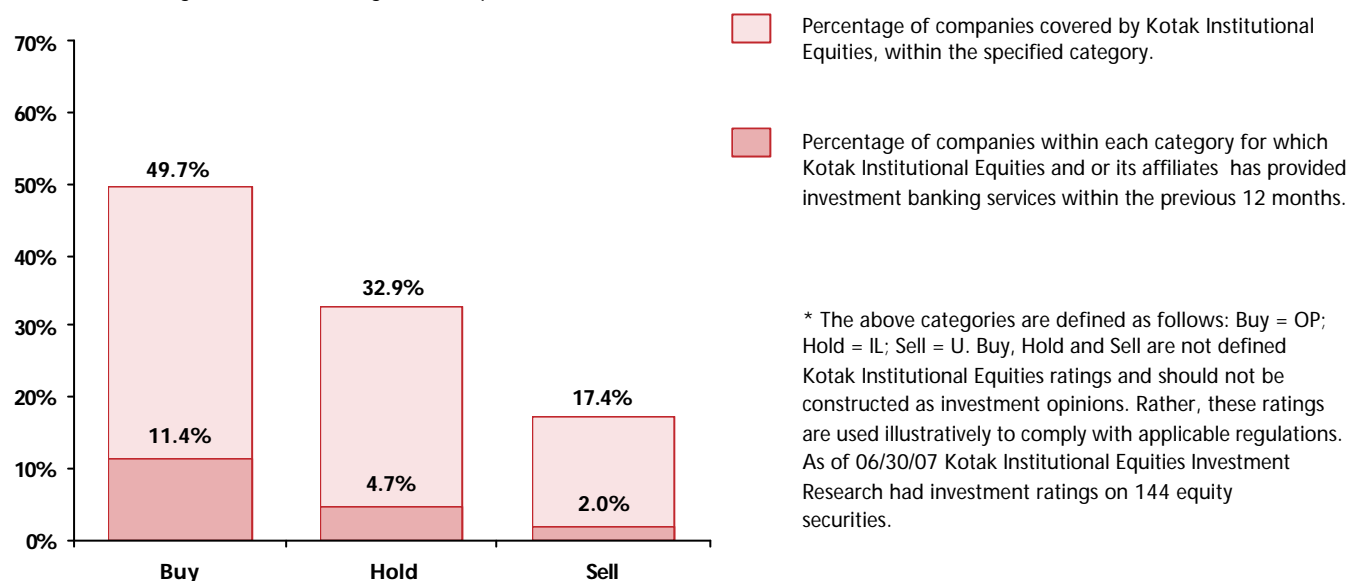
		Valuation	
		(Rs bn)	(Rs/share)
Land reserves valuation	NAV	75.2	1,032
Less: Land cost to be paid		(8.0)	(110)
Less: Net debt		(10.6)	(145)
Contractual business	14X P/E multiple	6.6	90
Total			867

Source: Kotak Institutional Equities

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Kotak Institutional Equities Research coverage universe

Distribution of ratings/investment banking relationships



Source: Kotak Institutional Equities.

As of June 30, 2007

Ratings and other definitions/identifiers

Current rating system

Definitions of ratings

OP = Outperform. We expect this stock to outperform the BSE Sensex over the next 12 months.

IL = In-Line. We expect this stock to perform in line with the BSE Sensex over the next 12 months.

U = Underperform. We expect this stock to underperform the BSE Sensex over the next 12 months.

Our target price are also on 12-month horizon basis.

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