



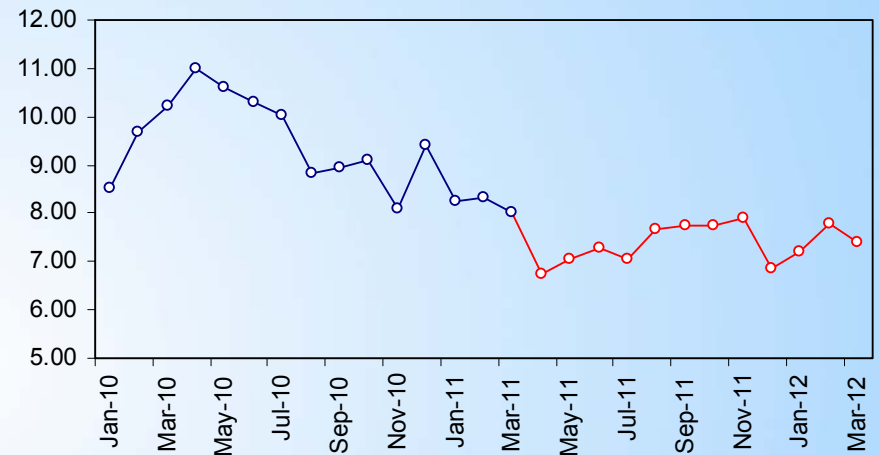
The B&K Strategy for Q1FY12

"Grow or perish, political compulsion... Await the dawn"

After the induced slowdown in H2FY11 we are forecasting a thaw of the liquidity squeeze

- Runaway inflation forced the Govt to hike the interest rates.
- In our view, we are nearing the end of this tightening cycle with a maximum upside of 25-50 bps from the current level.

WPI - Inflation



- In theory, the Indian economy can log-in a higher incremental GDP growth rate of 2-3%, if the Govt channelised the 3% of GDP it spends on subsidies into infrastructure.
- If India grows sustainably at levels exceeding 8%; it turns inflationary as infra growth does not keep pace with incremental demand.
- To preserve the social harmony in the country, a lesser growth rate is settled for. Thus, there is a lag in infrastructure growth in the country.

Resumption of Government Capex now a political compulsion

- The current UPA Government realizes that the only two states delivering high growth in India (Bihar, Gujarat) are non UPA governed states, this puts additional pressure on the Government to deliver growth.
- Changes at the top in Maharashtra politics demonstrates the pressure that the UPA Government faces for non growth.
- Evidence of migration of business houses to states which provide infrastructure and platform for growth.
- From April onwards, the Government Capex cycle has to re-emerge. This will receive tremendous fillip from the return of the 3G proceeds. This will immediately reduce the liquidity crunch.
- The sectors benefiting the most, and will be first of the block, benefitting from this Capex spend will be: Materials, Cement, Banking.
- About 30-35% of the total capex takes place in the last year of the 5 year plan, FY12 is the last year of the current 5 year plan.

India's GDP growth 15.5% in USD terms

GDPmp (at current prices) (2004-05 series)

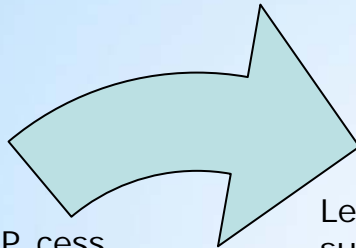
Year	GDP (INR bn)	YoY (%)	USD/INR	GDP (USD bn)	Avg Inflation India	Avg inflation in USA	Inflation differential
Mar-05	32,422	N.A.	44.95	721.2	6.47	3.2	3.27
Mar-06	36,924	13.89	44.279	833.9	4.42	3.4	1.02
Mar-07	42,936	16.28	45.285	948.1	5.43	2.7	2.73
Mar-08	49,864	16.13	40.241	1,239.1	4.66	4	0.66
Mar-09	55,826	11.96	45.917	1,215.8	8.41	1	7.41
Mar-10	65,502	17.33	47.413	1,381.5	3.85	2.3	1.55
Mar-11	78,500	19.8	45.58	1,722.2	9	2	7
Mar-12	89,490	14	45	1,988.6	7	2.5	4.5

GDP in current market price terms has grown by 15.5% average in the last 6 years and real GDP by 8.5%. Since the USD has been generally around 45 levels since 2005, the growth rate in INR terms (had there been the sort of depreciation in the INR versus the USD as warranted by India's inflation differential with US) can be construed to be higher.

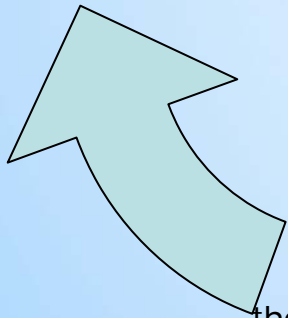
The virtuous Indian cycle?

What has been happening

The Govt accepts GDP cess of -2-3% to prevent inflation, and maintain social harmony. This lower growth throws lesser resources in the hands of Govt



Lesser resources means sub-optimal creation of Infrastructure. Lesser Infra leads to non-solution of supply-side problems



the final outcome of all this is that, inflation in India, sustains in the band of 5-7 %

FY12 What will be different

- Government targeting an inflation rate of 7.7.5%



- Therefore, post state elections we forecast a hike in prices of Urea, Kerosene, LPG, Diesel etc to bring down the subsidy burden as high base effect provides leverage



- The savings made to be spent on achieving the target infrastructure growth of the current 5 year plan

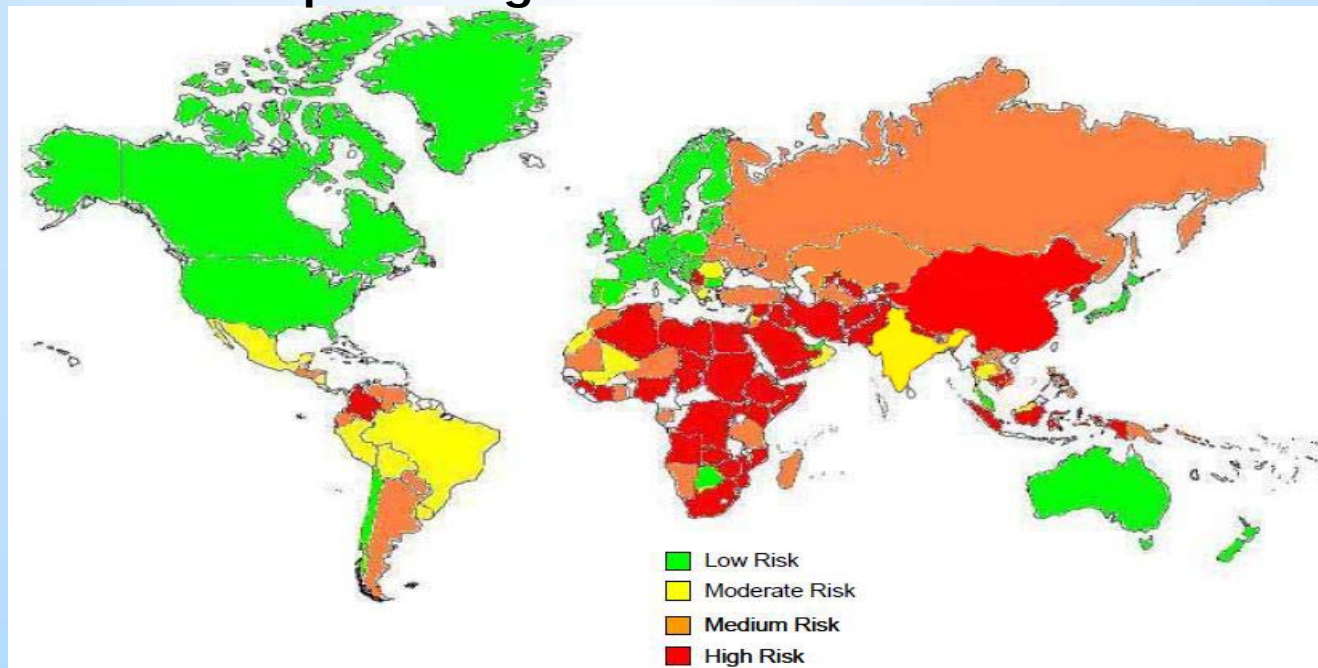
In India, mild Inflation is actually healthy...

- Supply-side constraints will remain a reality in the Indian economy, well into the future.
- Inflation will sustain in the range of 5-7% going ahead. This is above the comfort zone of 4-5%.
- Given the inflationary conditions that the world is currently facing, India's expected inflation for FY12 at 7-7.5% is not too bad.
- Mild inflation, in the Indian context, has aided demand upliftment, and creation of capital.
- Instances of excessive speculative demand build up noticed, whenever interest rates below 5.5-6%.

India: Perfect model under current environment?

- India is, and has been paying, an annual figurative tax of, approximately, 3% of GDP as it pursues the policy of inclusive growth. This is to maintain peace, stability and social harmony.
- We are seeing others countries like China, Saudi Arabia, Egypt, Yemen showing distinct signs of gravitating towards the Indian model of 'inclusive growth' by starting to spend a significant percentage of their GDPs (by some estimates – 1-2%) on socio economic projects.
- The Indian Model deserves a premium over majority of emerging economies.

B&K's Perception of global risk



What are we saying...?

- Growth agenda will come back to the fore in FY12, post state elections of April.
- Government will have to meet the capex requirements for the current five-year-plan guidelines, if it wants to maintain a GDP growth of 8% for future.
- Quality of governance will become very important. We feel that this will be the big challenge, which India will have to address over the next 3 to 5 years.
- Some key infrastructural bottlenecks are now emerging for the Indian economy viz. the rail & road Infrastructure. Investment imperative in infrastructure.
- The big hurdle, which India faces, is in the repetition of that extraordinary feat; doubling of its economy from USD 1 trillion to USD 2 trillion over the past five years.

But, what about the various risks... Have they all vanished - NO

Risks are very much present, and this strategy piece has been arrived at after taking acute cognizance of them. The two risks, which are prime from our side:

- Oil rising above 120 USD range as the geopolitics of the Arab states does not stabilize..
- Fiscal deficit, running ahead of the figure of 5.5%. If that happens, the Inflationary pressure on the economy will intensify. The probability of the same happening is not more than 10-15%.

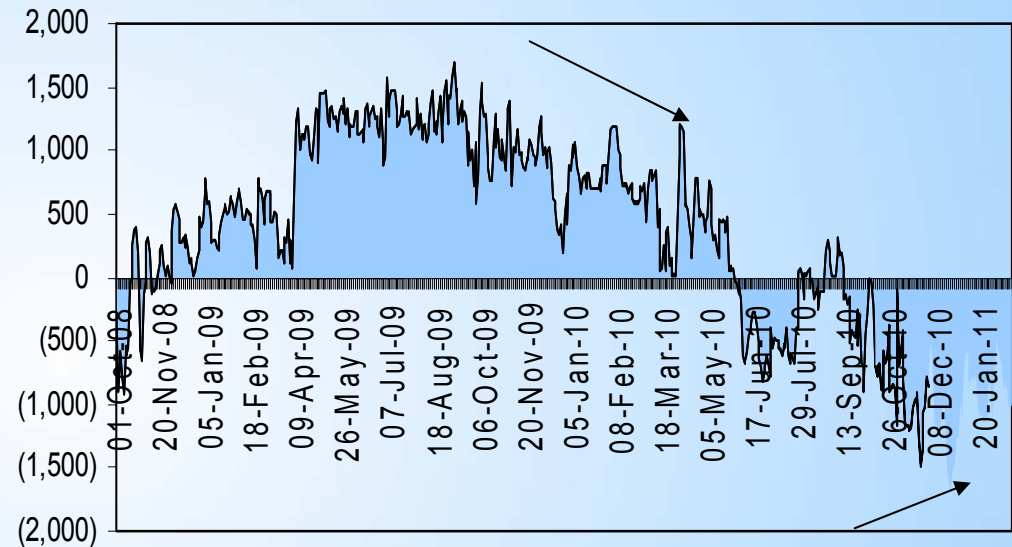
What do we like...

- Banks
- IT
- Materials (with a bias on Cement)
- Infrastructure: Play on improved execution capability to capitalize on Infra spend

Banks

- Acceleration in capex, improved liquidity and capitalisation levels, should support next leg of growth.
- Liquidity crunch due to rising inflation (thus monetary tightening), strong credit growth and lower money supply, is likely to ease on the back of increased government spending and better deposit mobilisation (with real interest rate turning positive).

Net LAF liquidity (Rs bn)



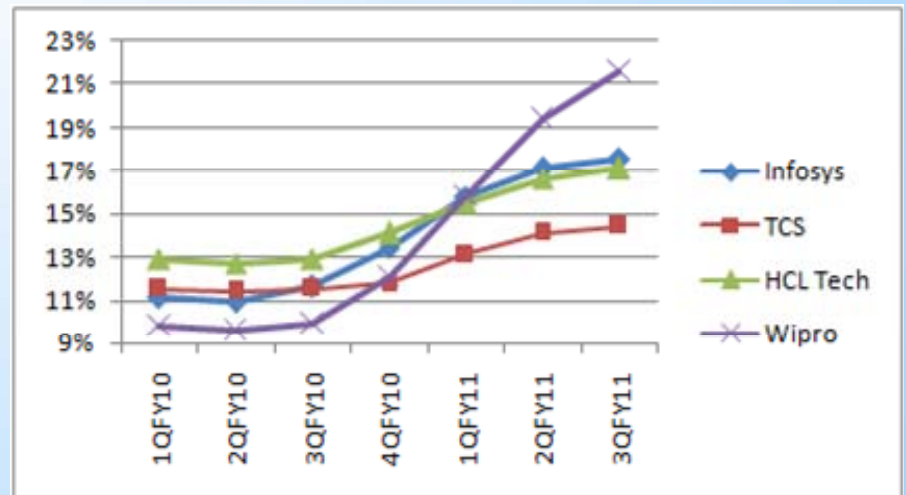
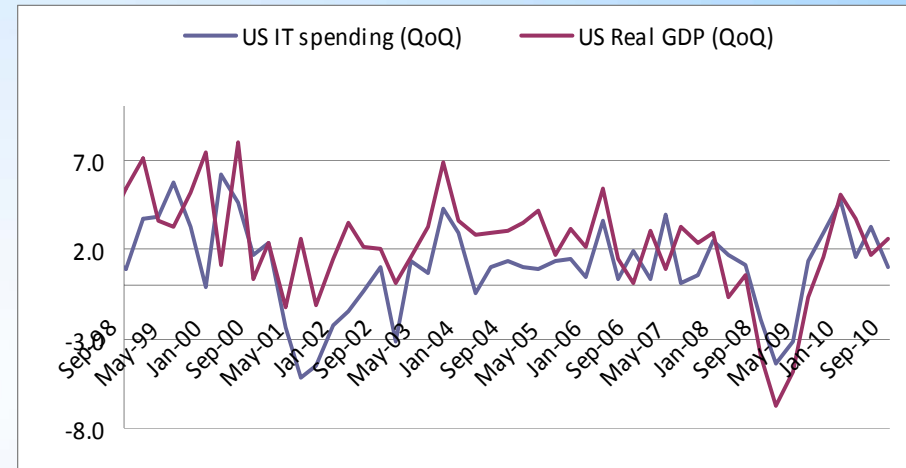
Interaction with bankers suggest that banks have better pricing power (increased rates by 175-200 bps) and there is a further headroom for 25-50 bps hike in lending rates. Thus commensurate increase in lending rates and gradual shift towards base rate coupled with healthy growth should lead to lower margin contraction than market expectation. Further, lower credit charges should support profitability.

Recapitalisation in PSU Banks

Banks	Fresh Capital Infusion (Rs mn)	Tier 1 (3QFY11) - Pre-funding (%)	Tier 1 (3QFY11) - Post-funding (%)	Increase in Tier I
Allahabad	6,700	8.1	8.9	0.7
Andhra	11,730	7.1	8.9	1.9
BOB	24,610	7.7	9.0	1.3
BOI*	10,100	8.0	8.5	0.6
Bank of Maharashtra	3,520	7.4	8.3	0.9
Corporation	3,090	8.1	8.5	0.4
Dena	5,390	7.2	8.8	1.6
IOB	10,540	7.3	8.4	1.1
OBC	17,400	9.1	11.0	1.9
PNB	1,841	7.6	7.7	0.1
Syndicate	6,330	7.8	8.7	0.8
Uco*	9,400	7.5	8.7	1.2
Union Bank	6,820	7.4	8.0	0.5
United	3,080	8.2	8.9	0.7
Vijaya	3,680	9.3	10.1	0.9
Total	124,231			

Information Technology - Momentum is ON

- Improvement in developed country → discretionary spend returning in other verticals
- COLA (cost of living adjustments) increases with existing clients and a favourable change in the business mix should ensure slight up-tick in portfolio-wide pricing.
- Wage inflation and attrition to be lower in FY12E than FY11
- Penetration into new geographies and verticals, adoption of new technologies and focus on non-linear initiatives are the steps in the right direction for the next leg of profitable growth.



Materials (Cement)

- Government spending is set to gain momentum as FY12E being the last year of 11th 5 year plan. (On an average ~35% of the entire budgeted capex happens in the last year of a 5 year plan).
- We expect demand-supply balance to become favourable in FY13E with certain pockets likely to witness cement shortages, particularly due to logistical bottlenecks (shortage of wagons and trucks) which will impede cement movement.
- Aggressive price hikes of ~Rs 40-50 per bag undertaken across regions since January 2011 will ensure strong improvement in EBITDA per tonne and overall profitability in 4QFY11E and 1QFY12E.

Infra Execution: So important in Indian Context

Infra Execution: So important in Indian context

- Inadequate capacity and capability built up, a key reason for large slippages in targeted investments in India.
- Strong expertise in the core sector with required capacity ramp up will help select companies to be resilient to macro uncertainties and drive strong growth with higher efficiencies.

Companies on the execution high-scale:

BHEL, BGR Energy, Crompton Greaves, Mundra Port and SEZ, Petronet LNG

Infra Execution: Targets for the 11th plan

	Capex			Mix (%)	
(Rs bn)	10th Plan (A)	11th Plan (R) *	Growth (%)	10th Plan	11th Plan
Electricity	3,402	6,586	94	37	32
Roads & Bridges	1,271	2,787	119	14	14
Telecom	1,019	3,451	239	11	17
Railways	1,021	2,008	97	11	10
Irrigation	1,199	2,462	105	13	12
Water Supply & Sanitation	601	1,117	86	7	5
Ports	230	406	77	3	2
Airports	69	361	424	1	2
Storage	56	90	59	1	0
Oil & gas pipelines	324	1,273	293	4	6
Total	9,192	20,542	123	100	100

* at 2006-07 prices

Source: Planning Commission report, 2011

Our Conviction List

Top Buys:

Large Caps	Mid Caps	Small Caps
ACC	Allahabad Bank	ELGI Equipment
Hindalco	BGR Energy	ENIL
ICICI Bank	Cadilla Healthcare	Century Textile
Infosys Technologies	Indian Bank	Sundaram Finance
Mundra Port	Petronet LNG	Unichem Labs
Tata Motors	Rallis	Vardhaman Textiles

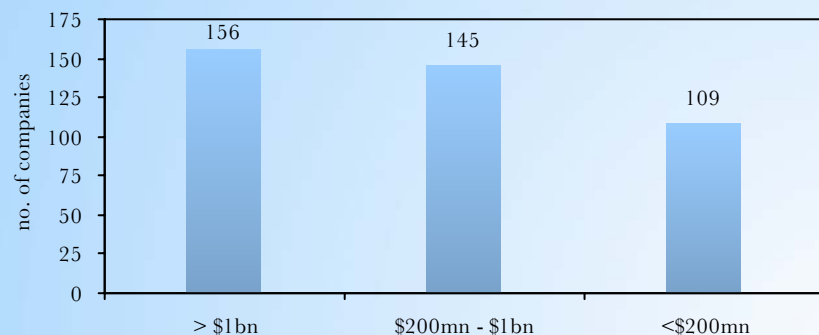
Top Sells:

JSW Energy	ABB	CONCOR
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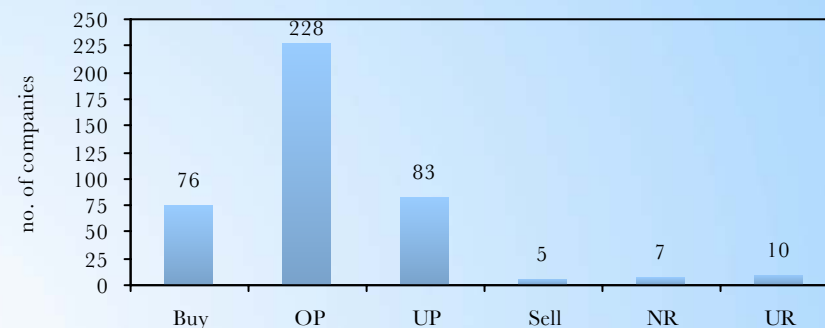
Thank You

B&K Universe Profile

By Market Cap (US\$ mn)



By Recommendation



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B&K Investment Ratings:

1. **BUY:** Potential upside of > +25% (absolute returns)
2. **OUTPERFORMER:** 0 to +25%
3. **UNDERPERFORMER:** 0 to -25%
4. **SELL:** Potential downside of < -25% (absolute returns)

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