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Results

BPCL: Strong FY2007 results; FY2008 may be as good although uncertainties exist

Centurion Bank of Punjab: Operating profit on track, net suffers due to higher provisioning, retain Underperform

News Roundup

Corporate

- France's Areva has stated that it would not raise its bid for REpower, conceding defeat after a five-month battle with India's Suzlon Energy for the German wind turbine maker. (BS)
- ABG Shipyard, the country's biggest private sector shipbuilder has said that it will acquire Vipul Shipyard for an undisclosed amount which would enable the company to enhance its shipbuilding capacity from the present 32 to 40 vessels on modular basis in future. (FE)
- NTPC Ltd has signed a memorandum of understanding with Nigeria to buy up to 3 mn tonnes of LNG per year on a long-term basis. (ET)
- VSNL and Teleglobe have tied up for Voice Termination Service (VTS) to provide call termination for SkypeOut. (ET)
- Bharti Airtel said it has tied up with Hong Kong-based PCCW Global Ltd for offering international connectivity to its customers. (FE)

Economic and political

- The Mayawati Govt has sent a report to the Centre saying that the 1,200 acres of land that was to be acquired by Reliance's Anil Ambani for an SEZ project was not contiguous. (FE)
- With the Central Sales Tax (CST) phase-out beginning this fiscal, the state governments are negotiating with the Centre to get a 50% share of the service tax collection pie, instead of the current 30.5%. (BS)
- The Cabinet Committee on Economic Affairs (CCEA) today approved the proposal for implementation of the skill development initiative at a total cost of Rs5.5 bn. This move would help in employment generation and enable growth in basic infrastructure. (BS)

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

EQUITY MARKETS

India	Change, %			
	24-May	1-day	1-mo	3-mo
Sensex	14,218	(1.0)	0.0	4.3
Nifty	4,205	(1.0)	0.9	6.8
Global/Regional indices				
Dow Jones	13,441	(0.6)	2.7	6.3
Nasdaq Composite	2,538	(1.5)	(0.4)	0.9
FTSE	6,565	(0.8)	1.6	2.6
Nikkei	17,428	(1.5)	1.1	(4.2)
Hang Seng	20,799	(0.2)	1.1	0.4
KOSPI	1,632	(0.9)	4.9	11.1
Value traded - India				
		Moving avg, Rs bn		
	24-May	1-mo	3-mo	
Cash (NSE+BSE)	138.1	142.5	126.8	
Derivatives (NSE)	347.6	508.7	364.2	
Deri. open interest	640.4	610.9	446.5	

Forex/money market

	Change, basis points			
	24-May	1-day	1-mo	3-mo
Rs/US\$	40.6	-	(39)	(362)
6mo fwd prem, %	0.7	(25)	71	24
10yr govt bond, %	8.2	3	16	21

Net investment (US\$m)

	23-May	MTD	CYTD
FIs	106	1,257	40
MFs	4	240	(303)

Top movers -3mo basis

Best performers	Change, %			
	24-May	1-day	1-mo	3-mo
Balaji Telefilms	226	4.1	34.1	84.4
Reliance Cap	969	0.4	30.6	48.4
Tata Tea	879	0.4	13.6	35.2
Balrampur Chini	76	(0.3)	19.7	35.0
Bol	211	(1.0)	6.0	33.9
Worst performers				
Bajaj Auto	2,171	(0.5)	(10.9)	(23.5)
Polaris	164	(1.2)	(16.2)	(18.2)
Wipro	532	(0.6)	(4.3)	(14.7)
Cipla	207	(0.8)	(18.1)	(14.5)
M&M	735	(0.1)	(3.7)	(14.2)

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Energy**BPCL.BO, Rs371**

Rating	OP
Sector coverage view	Attractive
Target Price (Rs)	450
52W High -Low (Rs)	448 - 255
Market Cap (Rs bn)	134.1

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	976	968	980
Net Profit (Rs bn)	18.1	18.5	21.1
EPS (Rs)	50.1	51.3	58.5
EPS gth	548.6	2.4	14.0
P/E (x)	7.4	7.2	6.3
EV/EBITDA (x)	4.4	3.3	3.0
Div yield (%)	4.3	4.3	4.9

Shareholding, March 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	64.3	-	-
FIs	13.1	0.2	(0.1)
MFs	2.2	0.2	(0.1)
UTI	-	-	(0.4)
LIC	11.0	1.1	0.7

BPCL: Strong FY2007 results; FY2008 may be as good although uncertainties exist

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- **Healthy 4QFY07 results due to oil bonds, inventory gains**
- **FY2008 performance would depend on government policy on pricing, subsidies but no reason to assume any change as yet**
- **Retain OP with 12-month target price of Rs450**

BPCL reported 4QFY07 net income at Rs6.7 bn versus our expected Rs7.8 bn. BPCL has got Rs9 bn of oil bonds in 4QFY07, about Rs960 mn lower versus the figure reported in the press in April 2007. Other line items are largely in line with expectations. BPCL's FY2007 net income is Rs18.1 bn (Rs50.1 EPS). We have made modest earnings revisions for FY2008-FY2010E EPS based on FY2007 results. Our revised FY2008, FY2009 and FY2009 EPS estimates are Rs51.3, Rs58.5 and Rs57.5, respectively versus Rs48.6, Rs55 and Rs58.1, respectively, previously. We currently assume that the government will follow the same system for distribution of under-recoveries as it has done in FY2007. However, we will have to wait for more clarity on the vital issues of oil bonds and share of upstream companies. We retain our 12-month target price of Rs450 based on 30% discount to 5X normalized EBITDA plus value of investments. Key downside risks stem from higher-than-expected subsidy losses.

4QFY07 results helped by oil bonds, discount from upstream companies and inventory gains. We see little merit in comparing BPCL's 4QFY07 results with either 3QFY07 or 4QFY06 results. For the record, BPCL's 4QFY07 EBITDA increased 85% qoq but declined 35% yoy; the large movements in quarterly results primarily reflect the timing of receipt of oil bonds. BPCL's 4QFY07 refining margin was US\$5.6/bbl versus US\$3.1/bbl in 3QFY07; the improvement is in line with improvement in global refining margins. BPCL had an inventory gain of Rs2 bn in 4QFY07. Exhibit 1 gives details on the results.

Full year results comparison may be more meaningful. BPCL's FY2007 EBITDA stood at Rs34.2 bn compared to Rs9.6 bn. The remarkable turnaround reflects a steep decline in net under-recovery to Rs10.4 bn in FY2007 from Rs35.5 bn in FY2006. BPCL's refining margin improved to US\$3.6/bbl from US\$1.6/bbl in FY2006, which reflects (1) improvement in underlying global refining margins and (2) nil discount from BPCL's refining division to the marketing division on internal sales of products unlike discounts in FY2006. BPCL's marketing volumes have grown a strong 9.5% to 25.2 mn tonnes.

Interim results of Bharat Petroleum (Rs mn)

	2008E	qoq			yoy			yoy		
		4Q 2007	3Q 2007	% chg	4Q 2007	4Q 2006	% chg	2007	2006	% chg
Net sales (a)	967,947	241,265	242,056	(0.3)	241,265	213,188	13.2	975,602	770,359	26.6
Increase/(decrease) in stock		(343)	1,950		(343)	1,230		2,054	7,544	
Raw material	(429,042)	(97,597)	(98,250)	(0.7)	(97,597)	(53,425)	82.7	(422,033)	(323,660)	30.4
Trading purchase	(476,014)	(113,433)	(126,491)	(10.3)	(113,433)	(128,636)	(11.8)	(463,904)	(389,844)	19.0
Staff cost	(10,740)	(2,885)	(2,651)	8.8	(2,885)	(2,212)	30.4	(10,037)	(8,816)	13.8
Other expenses	(15,925)	(14,269)	(9,722)	46.8	(14,269)	(10,512)	35.7	(47,522)	(46,010)	3.3
Total expenditure	(931,720)	(228,527)	(235,164)	(2.8)	(228,527)	(193,555)	18.1	(941,442)	(760,786)	23.7
EBITDA	36,227	12,738	6,892	84.8	12,738	19,633	(35.1)	34,160	9,573	256.8
Other income	7,181	2,547	1,487	71.3	2,547	1,112	129.0	7,332	4,653	57.6
Interest	(5,894)	(1,648)	(1,298)	27.0	(1,648)	(756)	118.0	(4,774)	(2,474)	93.0
Depreciation	(9,423)	(2,778)	(2,484)	11.8	(2,778)	(1,967)	41.2	(9,041)	(7,680)	17.7
Pretax profits	28,090	10,859	4,597	136.2	10,859	18,022	(39.7)	27,677	4,072	579.7
Extraordinary item	—	(68)	—		(68)	—		(68)	10	
Tax	(8,084)	(3,951)	(2,183)		(3,951)	(78)		(9,286)	(141)	
Deferred tax	(1,464)	(140)			(140)	(61)		(268)	(1,025)	
Net income	18,543	6,700	3,035	120.8	6,700	17,883	(62.5)	18,055	2,916	519.2
Adjusted net income	18,543	6,742	3,035	122.1	6,742	17,883	(62.3)	18,099	2,909	522.2
Tax rate (%)	34.0	37.9			37.9	0.8		34.6	28.6	
Volume data										
Crude throughput (mn tonnes)		5.3	4.7	13.1	5.3	2.9	80.6	19.8	17.2	14.7
Domestic sales volume (mn tonnes)		6.3	5.9	6.2	6.3	5.5	15.6	23.5	21.6	8.4
Refining margin (US\$/bbl)		5.6	3.1		5.6	(0.3)		3.6	1.6	
Inventory gain/(loss)		2,000	(3,000)		2,000	100		1,000	2,000	
Receipt from upstream companies		11,845	5,590		11,845	14,819		44,622	35,819	
Receipt from refining companies		—	(350)		—	1,246		—	3,468	
Receipt of oil bonds from government		9,009	11,350		9,009	21,631		52,479	21,631	
Subsidy gain/(loss)		(9,170)	(17,970)		(9,170)	(31,214)		(107,501)	(96,437)	

Source: Company, Kotak Institutional Equities estimates.

Consolidated profit model, balance sheet, cash model of BPCL, March fiscal year-ends, 2004-2010E (Rs mn)

	2004	2005	2006	2007	2008E	2009E	2010E
Profit model (Rs mn)							
Net sales	479,840	578,774	755,333	975,602	967,947	979,579	997,727
EBITDA	38,686	26,231	9,407	34,160	36,227	39,000	38,633
Other income	4,348	4,015	4,653	7,332	7,181	7,002	6,705
Interest	(1,447)	(1,748)	(2,474)	(4,774)	(5,894)	(4,445)	(3,415)
Depreciation	(6,754)	(7,130)	(7,680)	(9,041)	(9,423)	(9,535)	(10,412)
Pretax profits	34,833	21,368	3,906	27,677	28,090	32,023	31,510
Extraordinary items	(420)	810	176	(68)	—	—	—
Tax	(12,026)	(7,250)	(140)	(9,286)	(8,084)	(9,964)	(8,343)
Deferred taxation	(805)	(1,230)	(1,025)	(268)	(1,464)	(920)	(2,368)
Net profits	21,582	13,698	2,916	18,055	18,543	21,138	20,800
Net profits after minority interests	19,086	11,334	2,916	18,055	18,543	21,138	20,800
Earnings per share (Rs)	64.6	37.2	7.6	50.1	51.3	58.5	57.5

Balance sheet (Rs mn)							
Total equity	69,960	82,887	91,394	102,708	114,483	127,906	141,114
Deferred taxation liability	11,304	12,533	13,558	13,826	15,290	16,211	18,578
Total borrowings	32,701	46,589	83,736	103,286	67,316	54,135	41,522
Current liabilities	95,495	104,462	94,070	95,108	97,800	99,764	103,208
Total liabilities and equity	209,459	246,472	282,758	314,929	294,889	298,015	304,422
Cash	9,319	6,644	4,921	4,007	4,106	4,295	3,566
Current assets	97,729	130,393	128,208	130,478	100,382	100,983	102,877
Goodwill	—	—	—	—	—	—	—
Total fixed assets	88,484	98,542	110,855	122,754	127,712	140,048	155,290
Investments	13,927	10,893	38,774	57,689	62,689	52,689	42,689
Total assets	209,459	246,472	282,758	314,929	294,889	298,015	304,422

Free cash flow (Rs mn)							
Operating cash flow, excl. working capital	30,727	21,118	9,275	18,081	21,919	24,591	26,875
Working capital	1,025	(18,393)	1,577	(1,231)	32,788	1,363	1,550
Capital expenditure	(17,001)	(17,120)	(19,945)	(18,990)	(14,051)	(21,872)	(25,654)
Investments	1,278	2,992	(28,146)	(18,915)	(5,000)	10,000	10,000
Other income	1,985	2,445	1,785	7,332	7,181	7,002	6,705
Free cash flow	18,015	(8,957)	(35,455)	(13,723)	42,837	21,084	19,476

Ratios (%)							
Debt/equity	40.2	48.8	91.6	100.6	58.8	42.3	29.4
Net debt/equity	28.8	41.9	86.2	96.7	55.2	39.0	26.9
RoAE	28.8	14.4	3.3	16.3	15.1	15.4	13.7
RoACE	21.2	12.0	4.1	10.5	11.6	12.7	12.9

Key assumptions (standalone until FY2005)							
Crude throughput (mn tonnes)	8.8	9.1	17.2	19.8	19.8	20.0	20.5
Effective tariff protection (%)	7.2	4.8	2.9	1.4	1.2	1.3	1.2
Net refining margin (US\$/bbl)	4.2	3.9	2.2	2.9	3.7	3.5	2.8
Sales volume (mn tonnes)	20.9	21.5	23.3	24.6	25.4	26.1	26.9
Marketing margin (Rs/tonne)	1,893	1,732	(671)	(1,138)	(1,326)	387	1,442
Subsidy under-recoveries (Rs mn)	(13,518)	(25,821)	(31,847)	(17,918)	(14,235)	(9,499)	(2,403)

Source: Kotak Institutional Equities estimates.

Earnings sensitivity of BPCL to refining margins, import tariffs and marketing margins (Rs mn)

	Fiscal 2008E			Fiscal 2009E			Fiscal 2010E		
	Downside	Base case	Upside	Downside	Base case	Upside	Downside	Base case	Upside
Refining margins									
Refining margins (US\$/bbl)	2.7	3.7	4.7	2.5	3.5	4.5	1.8	2.8	3.8
Net profits (Rs mn)	14,286	18,543	22,800	16,900	21,138	25,376	16,471	20,800	25,129
EPS (Rs)	39.5	51.3	63.1	46.7	58.5	70.2	45.6	57.5	69.5
% upside/(downside)	(23.0)		23.0	(20.0)		20.0	(20.8)		20.8
Import tariffs									
Tariff protection	0.7	1.2	1.7	0.8	1.3	1.8	0.7	1.2	1.7
Net profits (Rs mn)	17,701	18,543	19,384	20,286	21,138	21,990	19,918	20,800	21,682
EPS (Rs)	49.0	51.3	53.6	56.1	58.5	60.8	55.1	57.5	60.0
% upside/(downside)	(4.5)		4.5	(4.0)		4.0	(4.2)		4.2
Marketing margins									
Auto fuels marketing margin (Rs/tonne)	(2,650)	(2,500)	(2,350)	(150)	0	150	1,396	1,546	1,696
Net profits (Rs mn)	17,789	18,543	19,296	20,355	21,138	22,476	19,413	20,800	22,187
EPS (Rs)	49.2	51.3	53.4	56.3	58.5	62.2	53.7	57.5	61.4
% upside/(downside)	(4.1)		4.1	(3.7)		6.3	(6.7)		6.7

Source: Kotak Institutional Equities estimates.

Banking**CENB.BO, Rs44**

Rating	U
Sector coverage view	Neutral
Target Price (Rs)	35
52W High -Low (Rs)	47 - 19
Market Cap (Rs bn)	75.2

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	10.1	14.5	19.7
Net Profit (Rs bn)	1.2	1.9	3.1
EPS (Rs)	0.8	1.1	1.7
EPS <i>gth</i>	28.9	39.3	55.4
P/E (x)	55.3	39.7	25.6
P/B (x)	7.0	5.8	4.8
Div yield (%)	-	-	-

Centurion Bank of Punjab: Operating profit on track, net suffers due to higher provisioning, retain Underperform

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- **CBoP reported a PAT of Rs280 mn, up 8% yoy, but 31% lower than our estimates**
- **Higher credit provisions impact PAT**
- **Reiterate U rating on the stock**

Centurion Bank of Punjab (CBoP) reported a PAT of Rs280 mn, up 8% yoy, but 31% lower than our estimates. Higher credit provision (both on standard asset and bad loans) was the key reason for the subdued growth in PAT. On the positive front the bank has been able to maintain its NIM at a high 4.6% and report a robust growth in non-interest income (ex-treasury) of 64%. However, it is to be noted that CASA ratio has shown a sharp drop to 31% compared to 37% as of March 2006. We are marginally tweaking our earnings estimates and reiterate our U rating on the stock given high valuations of 40.7X PER and 4.9XPBR FY2008 for bank with low RoE.

NIM remains high – likely due to focus on riskier assets. CBoP reported a NIM of 4.6% for FY2007-highest amongst the banks under coverage. This was likely aided by its focus on the high yielding loan segments like personal loans (witnessed a 161% growth), and SME loans (89% yoy growth). The high NIM was achieved despite the rise in cost of deposits to 5.6% in FY2007 from 4.6% in FY2006.

Loan growth was high, could impact cost of funding. CBoP reported a loan growth of 72% yoy, which increased its reliance on the bulk deposits and consequently led to the CASA ratio declining to 31% from 37% as of March 2006. We expect CBOP's FY2008 margins to be impacted by this high cost funding.

Higher provisions impact profits and will likely burden future profitability. CBoP made credit provisions of Rs560 mn for 4QFY07, which impacted the PAT at the bank. It is to be noted that CBoP used up Rs234 mn of floating provisions in 4QFY07 to meet some of its NPL provision requirements. Further, the bank also eased its internal accelerated provisioning norm on its retail portfolio, continuation of which would have led to an additional provisioning of Rs260 mn. CBoP still continues to have a provisioning policy that is more aggressive than RBI requirements and continues to hold Rs514 mn of provisions in excess of the RBI requirements. We believe that given CBoP's focus on the riskier loan segments, credit provisions could continue to remain high and have factored an increase of 22% and 14% in FY2008 and FY2009 over our previous estimates.

Fee income growth remained robust. Non-interest income (ex-treasury) growth was a robust 64% yoy and provided support for the profits. Given the likely pressure on NIM and higher provisions at CBoP, higher fee income will likely enable CBOP to drive its growth in PAT

Centurion Bank of Punjab

In Rs mn	3Q06	4Q06	1Q07	2Q07	3Q07	4Q07	% chg	4Q07KS	Actual Vs KS
Interest earned	2,082	2,247	2,534	2,870	3,324	3,957	76.1	3,768	5.0
Interest on advances	1,533	1,657	1,923	2,227	2,611	3,076	85.6	3,211	(4.2)
Income on investments	426	459	501	573	634	729	58.7	455	60.1
Interest on balances with RBI	113	120	101	69	77	144	20.4	102	40.8
Others	11	12	9	1	2	9	(20.0)		
Interest expense	1,037	1,095	1,302	1,519	1,860	2,309	110.8	2,106	9.6
Net interest income	1,045	1,152	1,232	1,351	1,465	1,649	43.1	1,663	(0.9)
Other operating income	591	911	950	881	1,018	1,558	71.0	1,393	11.9
Trading income	8	7	18	8	25	72	930.0	9	701.1
non-interest income (ex-treasury)	583	904	932	873	993	1,486	64.4	1,384	7.4
Total income	1,636	2,063	2,182	2,231	2,483	3,207	55.4	3,056	4.9
Operating expenses	1,293	1,498	1,586	1,609	1,778	2,086	39.2	1,961	6.3
Employee expenses	372	428	537	510	557	610	42.4	598	1.8
Other operating expenses	922	1,070	1,050	1,099	1,221	1,476	38.0	1,363	8.3
Operating profit	343	565	596	623	705	1,121	98.3	1,095	2.4
Provisions and contingencies	33	919	280	116	162	651	(29.2)	462	41.0
Standard asset provisions	14	160	NA	NA	NA	317	98	320	(1)
NPL provisions	(60)	667	NA	NA	NA	246	(63)	55	348
Investment amortization	86	87	NA	NA	NA	88	1	87	2
Extraordinary income from sale of shares held in Centurion Bank stock trust		625	-	-			(100.0)		
PBT	311	271	316	506	543	470	73.3	633	(25.7)
Tax	78	11	29	195	208	190	1,644.0	228	(16.5)
PAT	233	260	287	311	335	280	7.6	405	(30.9)
PBT - extr income	311	(354)	316	506	543	470	(232.9)	633	(25.7)
PBT - extr income + provisions	265	473	316	506	543	1,033	118.3	1,008	2.5
Tax rate (%)	25.1	4.0	9.2	38.5	38.3	40.4		36	

Loan book details (Rs bn)

Advances	56.9	65.3	74.5	83.8	94.2	112	71.8		
Retail advances	40.6	46.8	51.9	57.0	65.0	77	65.0		
CV/CE	9.0	10.2	11.2	11.9	13.0	NA			
Auto	4.5	4.2	3.6	2.9	2.6	NA			
3W vehicles	0.4	NA	0.5	0.6	0.6	NA			
Personal	4.8	5.8	6.8	8.0	10.3	15	161.0		
Mortgages	6.0	7.6	9.7	12.6	15.7	20	166.0		
Loans against sec	2.8	3.3	3.1	2.9	3.2	NA			
Others	1.6	1.4	1.0	0.6	0.6	NA			
2W vehicles	10.7	12.4	13.7	14.3	15.4	NA			
Agri	1.6	2.3	2.1	2.9	3.2	NA			
Corporate/SME advances	16.5	19.6	22.7	26.8	29.2	35	78.8		
ELC	5.1	3.3	NA	9.2	10.4	NA			
SME	6.3	6.5	NA	10.1	11.3	12	89.0		
Corp	5.1	9.8	NA	7.5	7.5	NA			

Deposit book details (Rs bn)

Deposits	85.9	94.0	103.7	113.8	125.3	149	58.1		
CASA(%)	37.8	38.7	35	33	34	31			

Yield measures (%)

Cost of deposits	4.7	4.6	5.1	5.4	5.6	5.6			
NIM	4.8	4.8	4.7	4.7	4.7	4.6			

Capital adequacy (%)

CAR	10.2	12.5	12.6	11.6	12.1	11.1			
Tier I	7.9	10.8	11.4	10.5	11.1	9.9			
Tier II	2.3	1.7	1.2	1.1	1.0	1.2			

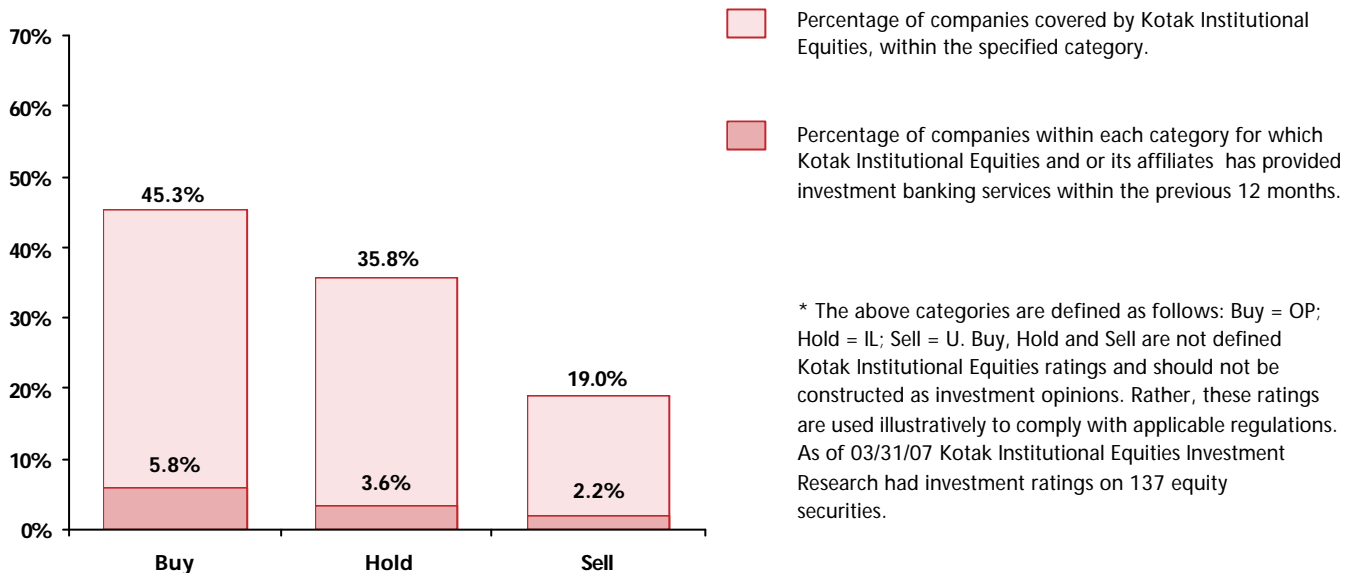
Asset quality details

Net NPL (%)	2.6	1.1	1.2	1.3	1.2	1.1			
Net NPL (Rs bn)	1.5	0.7	0.9	1.1	1.1	1.3			
Gross NPL (%)	NA	4.6	NA	NA	NA	2.8			
Gross NPL (Rs bn)	NA	3.1	NA	NA	NA	3.1			

"Each of the analysts named below hereby certifies that, with respect to each subject company and its securities for which the analyst is responsible in this report, (1) all of the views expressed in this report accurately reflect his or her personal views about the subject companies and securities, and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report: Sanjeev Prasad, Nischint Chawathe."

Kotak Institutional Equities Research coverage universe

Distribution of ratings/investment banking relationships



Source: Kotak Institutional Equities.

As of March 31, 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.

Other definitions

Coverage view. The coverage view represents each analyst's overall fundamental outlook on the Sector. The coverage view will consist of one of the following designations: Attractive (A), Neutral (N), Cautious (C).

Other ratings/identifiers

NR = Not Rated. The investment rating and target price, if any, have been suspended temporarily. Such suspension is in compliance with applicable regulation(s) and/or Kotak Securities policies in circumstances when Kotak Securities or its affiliates is acting in an advisory capacity in a merger or strategic transaction involving this company and in certain other circumstances.

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