RESULT PREVIEW Q1FY11

Moderation ahead!

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Earnings growth trajectory shows some softening

On a Y-o-Y basis, Q1FY11E earnings growth for the Sensex is expected to come in at 6.1%, lower than the 10.8% expected for our coverage universe (ex OMCs). Although on a Y-o-Y basis, growth is expected to be strong for some sectors, there seems to be some softening in earnings growth trajectory. Y-o-Y growth is expected to be robust for discretionary sectors (hospitality, retail media and auto), while cement and telecom are expected to show decline.

On a QoQ basis, there could be some declines as well. Sequentially, earnings for coverage universe is expected to come in lower by 7.9% (ex OMCs), led by sharp declines in engineering & capital goods and construction, among others. This is largely due to comparative Q4FY10 being the year end quarter where large projects get booked.

Sales growth to be strong; margins may come under pressure

Y-o-Y revenue growth is expected to be strong both for the coverage universe (23.8%) and Sensex (26.4%); however, Q-o-Q, it is expected to decline 5.8% and 5.9%, respectively, driven partly by negative effects of seasonality factors in engineering & capital goods, construction and to some extent, in autos, as well. Y-o-Y, growth is expected to be strong in discretionary sectors (auto, retail, media, and hospitality), real estate and oil & gas, among others.

For the companies in our coverage, EBITDA margins are expected to decline both Q-o-Q and Y-o-Y. Margins for Q1FY11E is expected to be under pressure for auto (higher raw materials costs), metals (sequential decline in base metal prices and rising cost push for steel), real estate (cost overruns) and cement (price correction and oversupply concerns) and to some extent, tech as well (increasing salary costs and foreign exchange headwinds).

Outlook positive for earnings; but expect moderation ahead

We expect the Sensex earnings to grow 28.2% in FY11, to INR 1,052. Although Y-o-Y growth is expected to be strong for commodity-driven sectors (oil & gas and metals), recent downgrades in earnings estimates for metal companies (on the back of rising global uncertainties) pose risks to the earnings outlook. BFSI and engineering & capital goods are also expected to post strong growth rates, while cement and telecom earnings are expected to remain weak. For FY12, we expect the Sensex earnings to grow 20.4% Y-o-Y, to INR 1,267.

Although seasonality may have some role to play in Q1FY11E for select sectors (e.g. cap goods, construction), what emerges as a point of concern is that Q1FY10 was a quarter where earnings were relatively lower; in that context, 6.1% Y-o-Y growth seems sub-par. At ~28% Y-o-Y growth, we expect FY11E earnings for Sensex to be robust. However with first quarter earnings expected to come in at just 6.1%, we would need strong set of numbers in the subsequent quarters for actual earnings to keep up with expectations.

Table 1: Growth expectations for earnings, revenue and EBITDA margin for Q1FY11E

Sector	PAT growth		Revenue growth		EBITDA margin	
	Y-o-Y (%)	Q-o-Q (%)	Y-o-Y (%)	Q-o-Q (%)	Y-o-Y (bps)	Q-o-Q (bps)
Agro related	9.3	(31.3)	23.5	(9.7)	(262)	(410)
Auto	42.0	(3.3)	45.3	(2.8)	(18)	(30)
BFSI	16.1	5.9	16.4	(3.4)	NM	NM
Cement	(23.1)	(7.5)	(1.3)	(5.1)	(644)	(6)
Construction	(6.4)	(51.9)	20.0	(22.0)	(29)	107
Engg & Cap Goods	17.4	(37.1)	22.6	(26.3)	11	(260)
FMCG	13.3	2.0	13.9	2.1	1	115
Hospitality	56.4	(15.5)	22.6	(9.7)	861	(46)
IT	6.1	(8.0)	11.7	3.8	(85)	(92)
Media	38.2	(3.8)	23.5	0.8	484	(66)
Metals & Mining	38.5	(25.1)	20.7	(13.1)	376	(129)
Miscellaneous	28.0	(23.9)	25.8	(17.2)	42	(137)
Oil & Gas	(56.5)	(62.4)	31.9	(5.7)	(836)	(649)
Pharmaceuticals	30.2	7.3	14.2	5.7	141	44
Pipes	(10.8)	(21.7)	(27.4)	(12.2)	307	16
Power	13.5	9.1	20.4	15.5	194	223
Real Estate	8.7	(2.7)	31.7	(14.1)	(1,120)	(201)
Retail	48.8	(20.0)	29.1	(5.5)	(40)	39
Telecom	(38.9)	(23.9)	1.4	4.0	(446)	19
Coverage	**(6.8)**	**(23.7)**	**23.8**	**(5.8)**	**(432)**	**(305)**
ex-OMCs	**10.8**	**(7.9)**	**24.7**	**(4.1)**	**(192)**	**15**
Sensex	**6.1**	**(7.8)**	**26.4**	**(5.9)**	**(367)**	**58**

Source: Edelweiss research

Note: OMCs includes BPCL, HPCL and IOCL

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Revenue growth is expected to be strong Y-o-Y for both Sensex (26.4%) as well as Edelweiss coverage companies (23.8%). For the coverage companies, Y-o-Y growth is expected to be strong in discretionary sectors (auto, retail, media, and hospitality), real estate and oil & gas, among others. Q-o-Q, there could be a slight decline in revenues, driven by negative effects of seasonality factors in some sectors, especially in engineering and capital goods, construction, and to some extent, in autos, as well.

The Sensex revenues are likely to rise 26.4% Y-o-Y in Q1FY11, with contribution from many sectors. However, cement is expected to post sluggish growth, while telecom could register decline in revenues.

Table 2: Revenue growth expected to show an uptick Y-o-Y

Sector	# of companies	Q1FY11E INR bn	Q1FY10 INR bn	Y-o-Y (%)	Q4FY10 INR bn	Q-o-Q (%)
Agro related	5	44	35	23.5	48	(9.7)
Auto	7	360	248	45.3	371	(2.8)
BFSI	25	407	350	16.4	421	(3.4)
Cement	5	118	120	(1.3)	124	(5.1)
Construction	10	102	85	20.0	131	(22.0)
Engg & Cap Goods	18	336	274	22.6	456	(26.3)
FMCG	10	171	150	13.9	167	2.1
Hospitality	5	10	8	22.6	11	(9.7)
IT	9	273	244	11.7	263	3.8
Media	6	15	12	23.5	15	0.8
Metals & Mining	11	427	354	20.7	492	(13.1)
Miscellaneous	4	21	16	25.8	25	(17.2)
Oil & Gas	12	2,307	1,750	31.9	2,448	(5.7)
Pharmaceuticals	7	82	72	14.2	77	5.7
Pipes	3	29	40	(27.4)	33	(12.2)
Power	10	384	319	20.4	333	15.5
Real Estate	7	36	27	31.7	41	(14.1)
Retail	4	39	30	29.1	42	(5.5)
Telecom	4	198	195	1.4	190	4.0
Coverage	**162**	**5,359**	**4,330**	**23.8**	**5,689**	**(5.8)**
ex-OMCs	**159**	**4,039**	**3,238**	**24.7**	**4,211**	**(4.1)**
Sensex	**30**	**2,290**	**1,812**	**26.4**	**2,434**	**(5.9)**

Source: Edelweiss research

Note: (1) Revenue for BFSI = Net Interest Income + Other Income

(2) OMCs includes BPCL, HPCL and IOCL

EBITDA margins may come under pressure

For the coverage companies, EBITDA margins are expected to decline both Q-o-Q and Y-o-Y. Margins are expected to be under pressure for auto (higher raw materials costs), metals (sequential decline in base metal prices and rising cost push for steel), real estate (cost overruns), cement (price correction and oversupply concerns) and tech (rising wage pressures and cross-currency impact).

For the Sensex companies, margins are expected to decline by ~367bps Y-o-Y. This contraction in margins is expected to be led by companies in telecom and cement sector.

Table 3: EBITDA margins may come under pressure

Sector	# of companies	Q1FY11E (%)	Q1FY10 (%)	Y-o-Y (bps)	Q4FY10 (%)	Q-o-Q (bps)
Agro related	5	17.3	19.9	(262)	21.4	(410)
Auto	7	13.5	13.7	(18)	13.8	(30)
Cement	5	25.1	31.5	(644)	25.1	(6)
Construction	10	16.9	17.2	(29)	15.8	107
Engg & Cap Goods	18	11.4	11.3	11	14.0	(260)
FMCG	10	21.5	21.5	1	20.3	115
Hospitality	5	34.1	25.5	861	34.6	(46)
IT	9	25.8	26.7	(85)	26.8	(92)
Media	6	40.2	35.4	484	40.9	(66)
Metals & Mining	11	30.6	26.8	376	31.9	(129)
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Oil & Gas	12	6.5	14.8	(836)	13.0	(649)
Pharmaceuticals	7	21.7	20.3	141	21.3	44
Pipes	3	18.2	15.1	307	18.0	16
Power	10	24.4	22.4	194	22.2	223
Real Estate	7	36.2	47.4	(1,120)	38.2	(201)
Retail	4	10.2	10.6	(40)	9.8	39
Telecom	4	34.4	38.8	(446)	34.2	19
Coverage	**137**	**15.0**	**19.3**	**(432)**	**18.1**	**(305)**
ex-OMCs	**134**	**22.3**	**24.2**	**(192)**	**22.1**	**15**
Sensex	**26**	**24.4**	**28.1**	**(367)**	**23.8**	**58**

Source: Edelweiss research

Note: (1) Coverage and Sensex aggregate excludes BFSI, as EBITDA margin is not relevant for the sector

(2) OMCs includes BPCL, HPCL and IOCL

Earnings likely to register modest uptick

Y-o-Y earnings growth is expected to come in at 6.1% for the Sensex and at 10.8% (ex OMCs) for the coverage universe. For the coverage universe, discretionary sectors (auto, media, retail, hospitality) are expected to show strong growth, while cement and telecom are expected to show a decline.

For the Sensex, earnings growth is expected at 6.1% Y-o-Y. Although BFSI, auto, engineering & capital goods and metals are expected to show a healthy growth, earnings from telecom and cement sectors could be a dampener.

Table 4: Earnings likely to show an uptick across most sectors in Q1FY11

Sector	# of companies	Q1FY11E INR bn	Q1FY10 INR bn	Y-o-Y (%)	Q4FY10 INR bn	Q-o-Q (%)
Agro related	5	3.9	3.5	9.3	5.6	(31.3)
Auto	7	29.4	20.7	42.0	30.3	(3.3)
BFSI	25	119.2	102.7	16.1	112.6	5.9
Cement	5	16.1	21.0	(23.1)	17.4	(7.5)
Construction	10	4.8	5.1	(6.4)	10.0	(51.9)
Engg & Cap Goods	18	24.2	20.6	17.4	38.4	(37.1)
FMCG	10	25.0	22.0	13.3	24.5	2.0
Hospitality	5	1.5	0.9	56.4	1.7	(15.5)
IT	9	51.3	48.3	6.1	55.7	(8.0)
Media	6	3.4	2.5	38.2	3.5	(3.8)
Metals & Mining	11	82.6	59.6	38.5	110.2	(25.1)
Miscellaneous	4	2.2	1.7	28.0	2.9	(23.9)
Oil & Gas	12	64.5	148.4	(56.5)	171.6	(62.4)
Pharmaceuticals	7	14.0	10.8	30.2	13.0	7.3
Pipes	3	2.6	3.0	(10.8)	3.4	(21.7)
Power	10	41.6	36.7	13.5	38.1	9.1
Real Estate	7	7.4	6.8	8.7	7.6	(2.7)
Retail	4	1.4	0.9	48.8	1.8	(20.0)
Telecom	4	27.6	45.2	(38.9)	36.2	(23.9)
Coverage	**162**	**523**	**560**	**(6.8)**	**685**	**(23.7)**
ex-OMCs	**159**	**566**	**511**	**10.8**	**615**	**(7.9)**
Sensex	**30**	**344**	**324**	**6.1**	**373**	**(7.8)**

Source: Edelweiss research

Note: OMCs includes BPCL, HPCL and IOCL

Outlook positive for earnings; but expect moderation ahead

We expect the Sensex EPS to grow 28.2% in FY11, to INR 1,052. Although Y-o-Y growth is expected to be strong for commodity-driven sectors (oil & gas and metals), recent downgrades for metal companies on the back of rising global uncertainties pose risks to the earnings outlook. BFSI and engineering & capital goods are also expected to post strong growth, while cement and telecom earnings could remain weak. For FY12, we expect the Sensex earnings to grow ~20%, to INR 1,267.

Table 5: Earnings growth for Sensex FY11E and FY12E

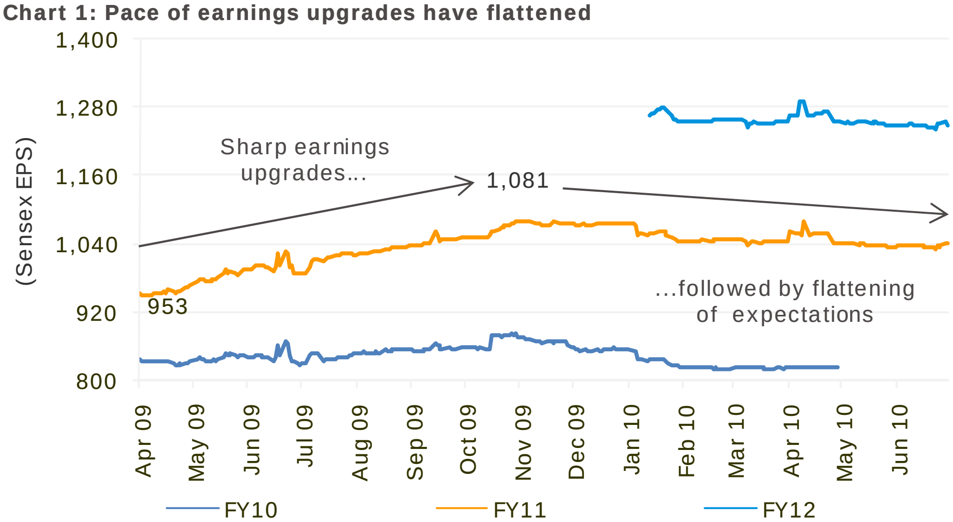
Sector	Wt in Index (%)	Contribution to EPS (INR)			Growth (%)	
		FY10	FY11E	FY12E	FY11E	FY12E
Oil & Gas	19.8	170	252	309	48.2	22.4
BFSI	20.6	147	182	234	24.3	28.1
Metals	9.4	115	194	237	68.5	22.6
Capital Goods	8.3	49	60	75	22.9	25.0
Auto	7.6	68	77	85	13.4	10.8
IT	15.6	115	129	149	11.9	15.6
FMCG	7.9	49	55	63	13.0	15.3
Telecom	2.8	48	39	43	(19.5)	10.9
Power	4.3	32	35	37	8.1	7.8
Pharma	1.2	7	8	10	12.5	14.4
Real Estate	0.9	6	8	9	32.5	12.4
Cement	1.7	15	14	16	(9.1)	12.9
Sensex	**100.0**	**821**	**1,052**	**1,267**	**28.2**	**20.4**

Source: Edelweiss research

Upward revisions in estimates have stalled

The trend of earnings upgrades by consensus, which looked strong until November 2009, has become sluggish of late. Consensus EPS for the Sensex for FY11E is at INR 1,038 and has declined from INR 1,081 recorded in November 2009. In case of global uncertainties increasing or earnings for subsequent quarters disappointing, there is a risk of downgrades to consensus estimates.

Chart 1: Pace of earnings upgrades have flattened

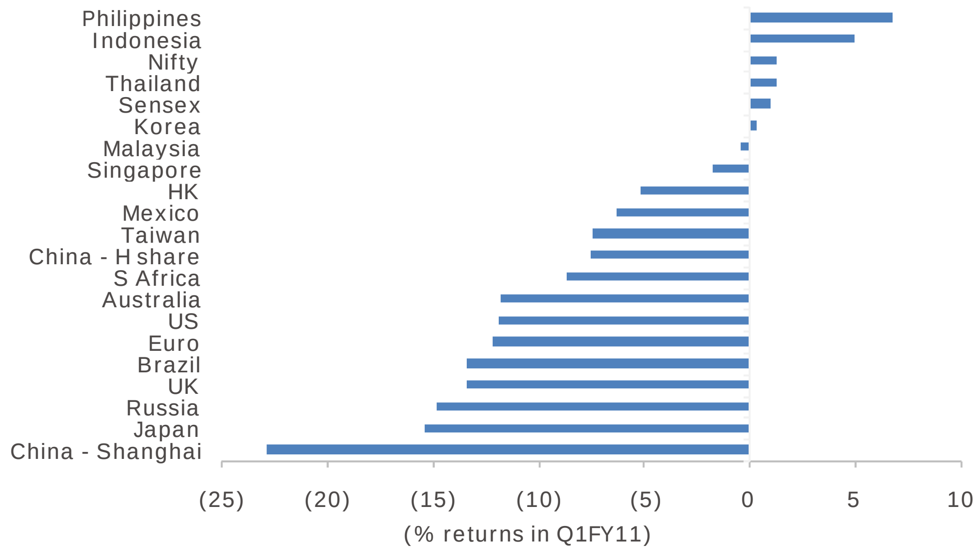


Source: Bloomberg, Edelweiss research

Market Review

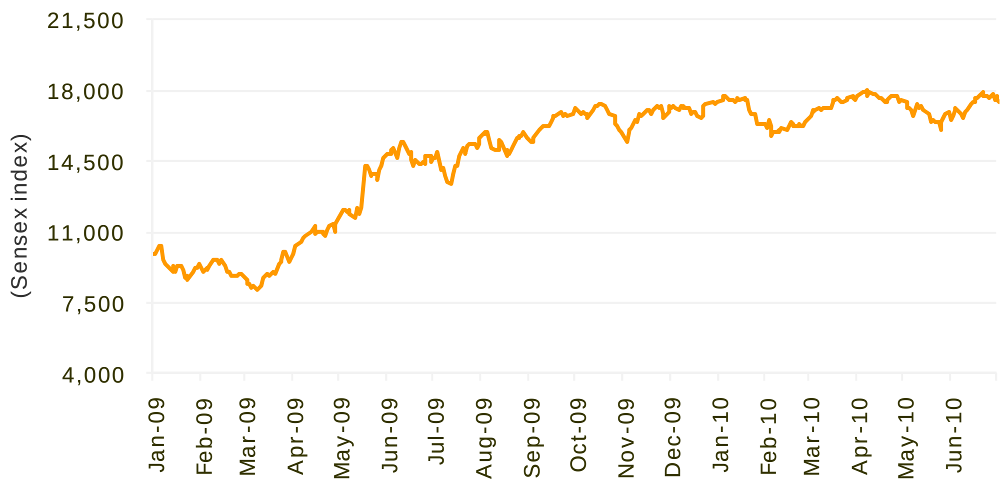
India was one of the top performers this quarter as compared to a subdued performance in the previous two quarters. On a whole, there was a wide variation in the performance among EM markets. While China's markets fell sharply over concerns around tightening and slowdown in growth, commodity driven EM countries such as Russia underperformed as fears about a fresh bout of weakness in global growth gathered pace. On the other hand, India along with Philippines and Indonesia displayed a resilient performance over the quarter.

Chart 2: Performance of Indian stock markets was among the best in Q1FY11



Source: Bloomberg, Edelweiss research

Chart 3: Sensex since January 2009



Source: Bloomberg, Edelweiss research

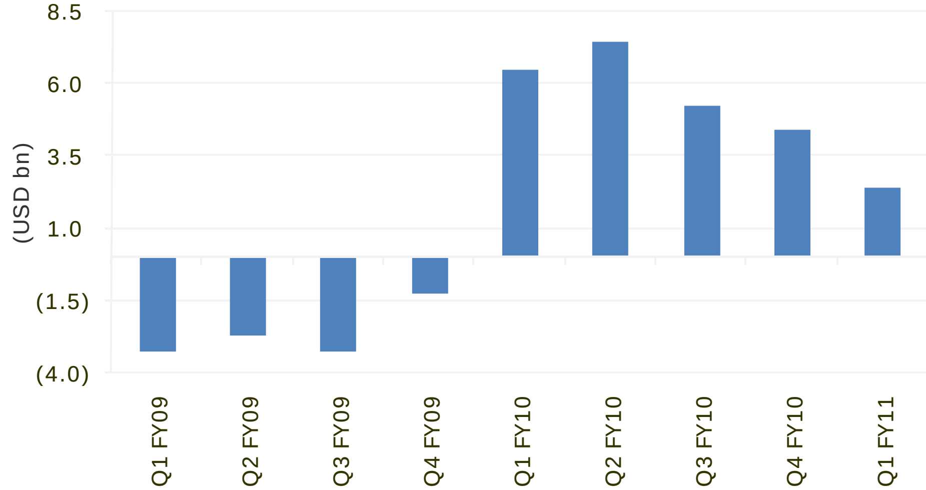
FII and DII net flows slow down but remain positive

FIIs were net buyers of USD 2.3 bn during the quarter vis-à-vis net buyers of USD 4.4 bn in Q4FY10. In the backdrop of renewed concerns on the pace and sustainability of the global recovery, this quarter saw the lowest net inflows since Q4FY09.

DIIs have been net buyers of USD 0.8 bn in Q1FY11 against USD 1.8 bn in Q4FY10.

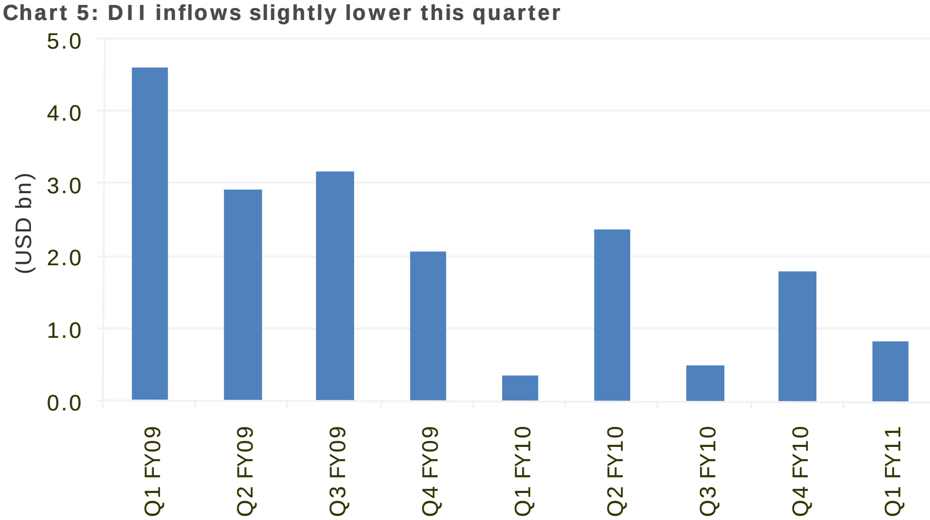
Overall, institutional investors continued to remain net buyers of USD 3.2 bn in Q1FY11 vis-à-vis USD 6.2 bn in Q4FY10.

Chart 4: FIIs remain net buyers



Source: Bloomberg, Edelweiss research

Chart 5: DII inflows slightly lower this quarter



Source: Bloomberg, Edelweiss research

ECONOMY

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Ideas create, values protect

India - impervious to global uncertainties

July 5, 2010

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Global economy: A fresh bout of uncertainty

The current global backdrop is once again full of uncertainties. The recovery in global economy which had gathered pace in Q4CY09 has started tapering off again during H1CY10. Outlook for global growth is one of caution with high unemployment and excess capacities still prevalent in several countries along with risks of withdrawal of fiscal stimulus. On one hand, the bailout of troubled European nations will come with a stringent clause of tightening their fiscal discipline. Likelihood of demand slowdown in several European economies and a prolonged weakening of EUR will pose fresh challenges for global recovery. On the other hand, there are increasing signs of a renewed bout of weakness in the US economy. In US, the saving grace so far had been recovery in the manufacturing sector. But, dodgy housing and retail sales data suggests a drag on the speed and shape of US recovery.

It is against this macroeconomic backdrop that the G20 met, which brought out sharp trans-Atlantic differences, primarily between the US and Germany. The US believes that the economic recovery is still tentative and, therefore, hurried removal of fiscal stimulus could derail recovery as private sector demand remains weak. Germany, on the other hand, is worried about the situation in PIIGS economies and financial markets' losing appetite for high fiscal deficits. Therefore, it is pushing for fiscal consolidation at the earliest to gain market confidence back. Thus, uncertainties in developed economies coupled with a sharp division in opinions on future course of macro-policy can potentially act as a dampener on growth worldwide.

India looks largely impervious to global uncertainties

India, for the time being, seems to be in a better position compared to most peers. While the concern of several economies still remains kick-starting growth, India has moved much ahead wherein tackling inflation has become a bigger issue. Relatively high insularity of the Indian economy, on the back of its relatively lower dependence on exports, is a buffer against the current global backdrop. A few other developments in the past couple of months have also been markedly positive for the macro story. Pressure on the fiscal side seems to have eased significantly on the back of higher than expected licencing fees from the telecom auctions and de-regulation of petroleum products. Such a de-regulation also signifies strong government will for reforms. Monsoon is projected to be normal (~102% of Long Period Average).

Inflation continues to bother policy-makers in the near-term. However, we feel that while inflation currently is at elevated levels, fresh global uncertainty would not be supportive of global commodity prices. This would help to ease imported inflationary pressures, which currently are high due to elevated metals and energy prices. Further, if IMD's expectations of near normal monsoon materialize, it would also help to check the inflation expectations in the economy and the pressure on RBI to hike rates aggressively could ease in the next 3-4 months.

We believe that the current rate hikes will not act as a dampener to growth given the rate hikes signal RBI's growing confidence on the economic recovery, given the healthy incoming economic data on GDP growth, industrial production and capital goods sector and credit growth. While we expect RBI to increase policy interest (repo and reverse repo) rates by 25bps each in the July 27 policy meet, we keep unchanged our earlier expectations of 100-125bps tightening in policy rates in FY11. This will take the repo rate to ~6% by March 2011. However, with CRR already at the higher end of its long-run "steady-state" level of 5.5-6.0%, further hike in this policy instrument is unlikely.

In sum, conditions appear reasonably strong for steady economic growth in India, barring the likely knock-on effects of a global slowdown.

- **Expect strong growth to be reported in Q1FY11; consolidation during Q2-Q3**

Overall growth had been strong in the economy in the recent quarters. Non-agri GDP growth rates have accelerated for almost all successive quarters since Q4FY09. In Q4FY10, non-agri GDP growth had been 10% Y-o-Y. Our proprietary Edelweiss-ET Now Lead Indicator Index (EELII) suggests over 10% growth in non-agri GDP in Q1FY11 as well. Several other indicators coincident with GDP, viz., IIP growth, core sector growth, Purchase Manufacturer's Index (PMI) have continued to indicate robustness in recovery. In fact, recent GDP and IIP data is showing early signs that capex may have started picking up, indicating that peaking capacity utilisation may be prompting corporates to make fresh investments.

During Q2-Q3FY11, the growth trajectory is likely to settle a tad lower. For example, the IIP growth rate is set to moderate from the current mid-teen levels to high single digits by June. However, this should not be mistaken for a slowdown. Rather, over the next six months growth in India will consolidate around a more steady-state and sustainable path.

AUTOMOBILES

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Strong topline growth; margins may dip

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Key highlights of the sector during the quarter

Volumes for the quarter continued to remain strong across segments. Despite the first quarter being seasonally weaker than Q4, two wheelers reported strong sequential volume growth. In the passenger vehicle space Maruti Suzuki India (MSIL) continued to maintain its market position despite the launch of new products such as the Ford *Figo*, Volkswagen's *Polo,* and GM's *Beat*. Demand for commercial vehicles remained robust with volumes rising 61% Y-o-Y, albeit, on a low base. Price hikes in the 2-3% range were taken by all OEMs to partially mitigate against rising raw material costs. While discounts continue to remain extremely high in the car segment (specifically MSIL), in the two wheeler and MHCV segments pricing power has sustained.

Result expectations for the sector and stocks under coverage

We expect margins to remain under pressure considering the rise in commodity prices. MSIL's margins could additionally be impacted by adverse currency movements (depreciation of EUR and appreciation of Yen vis-à-vis INR) and increased competition restricting pricing power. Ashok Leyland (ALL) though could see the highest sequential decline in EBITDA margin (down 280bps) due to its higher operating leverage in a seasonally weak quarter. We expect EBITDA margins of MSIL, Hero Honda (HH), Bajaj (BAL), and Mahindra & Mahindra (M&M) to decline around 40-100bps sequentially.

Outlook over the next 12 months

Growth in automobile sector is expected to be strong across all segments primarily driven by commercial vehicles (CV) which in our view will outperform the overall industry growth rate on back of robust IIP data (which strongly correlates the growth in CV space) and a lower base. A normal monsoon will benefit tractor manufacturers (M&M, Escorts). While BAL could outpace HH on Y-o-Y growth rates, we believe the latter has the potential to surprise on the upside with stronger-than-expected volume growth.

While demand in the passenger vehicle market remains strong, we believe competitive intensity in this segment is on the rise. Recent aggressively priced model launches (*Figo, Polo, Beat*) by competitors will prove challenging for MSIL.

BUY

Mahindra & Mahindra, Ashok Leyland, Hero Honda, Escorts

Recommendations

Top picks: Mahindra & Mahindra, Ashok Leyland, Hero Honda and Escorts

Stocks to avoid: Tata Motors

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
Ashok Leyland	Revenues	24,576	9,125	169.3	29,390	(16.4)	Operating leverage could be high and negative for EBITDA magin sequentially.
	EBITDA	2,713	122	2,123.8	4,163	(34.8)	
	Core PAT	1,375	(427)	422.0	2,610	(47.3)	
Bajaj Auto	Revenues	39,304	23,385	68.1	33,995	15.6	Realisaton per vehicle as two-wheeler sales has got skewed towards executive segment.
	EBITDA	8,578	4,554	88.4	7,771	10.4	
	Core PAT	6,327	3,175	99.3	5,780	9.5	
Escorts	Revenues	7,923	5,834	35.8	6,756	17.3	Volumes have increased 16% Q-o-Q. Expect EBITDA margins to improve by 70bps, despite increasing raw material prices on high operating leverage.
	EBITDA	829	633	30.9	661	25.4	
	Core PAT	465	223	108.3	444	4.6	
Hero Honda Motors	Revenues	43,416	38,224	13.6	41,223	5.3	Margin pressure on account of increase in raw material prices.
	EBITDA	7,318	6,501	12.6	7,117	2.8	
	Core PAT	5,948	5,003	18.9	5,988	(0.7)	
Mahindra & Mahindra	Revenues	53,995	42,426	27.3	53,047	1.8	Tractor sales were slightly disappointing sequentially. Margins could come under pressure as tractors realise higher margins.
	EBITDA	7,614	6,936	9.8	8,458	(10.0)	
	Core PAT	4,970	4,855	2.4	5,705	(12.9)	
Maruti Suzuki India	Revenues	84,202	64,930	29.7	84,246	(0.1)	Impact on margins on account of movements in Yen and Euro vis-à-vis Indian Rupee.
	EBITDA	10,185	7,932	28.4	10,535	(3.3)	
	Core PAT	6,298	5,835	7.9	5,990	5.1	
Tata Motors	Revenues	106,973	64,046	67.0	122,297	(12.5)	Besides operating margins, interest costs and depreciation will be key thing to be watched.
	EBITDA	11,464	7,280	57.5	12,551	(8.7)	
	Core PAT	3,969	2,007	97.8	3,823	3.8	

Valuation snapshot

		Mkt Cap	Price (INR)	PAT growth (%, Y-o-Y)		P/E		P/B		RoE		Div yld	
	Reco	USD mn		FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E
Ashok Leyland	Buy	1,781	63	35.0	19.2	14.9	12.5	2.1	1.9	14.6	15.9	2.4	2.4
Bajaj Auto	Hold	7,601	2,455	15.1	7.8	16.5	15.3	7.9	5.5	59.7	42.4	0.0	0.0
Escorts	Buy	427	197	56.8	21.5	13.1	10.8	1.2	1.1	9.2	10.2	0.5	0.5
Hero Honda Motors	Buy	8,636	2,021	11.8	10.9	16.2	14.6	7.5	5.5	56.5	43.6	1.2	1.7
Mahindra & Mahindra	Buy	7,456	602	7.1	12.0	15.9	14.2	3.4	2.8	24.5	21.8	1.0	1.0
Maruti Suzuki India	Hold	8,753	1,416	9.1	9.5	15.0	13.7	2.8	2.4	20.8	19.0	0.5	0.6
Tata Motors	Reduce	8,987	766	33.7	10.3	25.3	23.0	2.4	2.3	10.4	10.7	1.3	1.3

Source: Edelweiss research

BANKING AND FINANCIAL SERVICES

Edelweiss
Ideas create, values protect

Margins to come off; lower NIMs and lower treasury gains

July 5, 2010

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Key highlights of the sector during the quarter

- Liquidity was a key monitorable during the quarter. Liquidity situation that was extremely comfortable (in fact excessive) till mid-May, came under significant pressure (net repo position of INR 530 bn at June 2010 end) due to 3G auction payments, advance tax outflow and slow deposit mobilsation.
- Credit growth has been strong at 19.5%, led by demand from telecom companies for 3G and BWA auctions. Deposit growth, on the other hand, was muted at 14% (net deposits mobilisation of INR 310 bn in April-June 2010 against INR 1.4 tn in April-June 2009 and INR 576 bn in April-June 2008).
- In the past two months, benchmark Gsec yields have traded in a very narrow range of 7.3-7.7%, after touching a high of 8.1% in April end. We do not expect any significant trading gains or mark-to-market depreciation hit on the banks' investments during the quarter. Possibility of write-backs is limited.
- Banks interest margins will come off marginally in Q1FY11 due to change in interest calculation on banks saving deposits. However, benefit should come from improvement in LDR.
- Growth momentum in disbursements for NBFCs (including HFC, power financiers and auto financing companies) remained strong through Q1FY11 (we expect disbursements to grow at 20% plus Y-o-Y). Margins may come off marginally due to rise in wholesale borrowing cost. Asset quality to trend positively in housing, auto and infra segment.

Result expectations for the sector and stocks under coverage

- Overall earnings for the quarter are likely to be subdued sequentially on the back of lower treasury income and lower NII growth.
- Overall NII to be flat Q-o-Q in Q1FY11 due to impact of saving rate which would negate improvement in loan deposit ratio (3G and BWA auctions).
- Provisions to remain high, led by slippage from the restructured book.
- For banks under coverage, earnings could grow 16% Y-o-Y and 10% Q-o-Q.

Outlook over the next 12 months

- We expect credit growth to step up further in H2FY11; leading indicators, IIP and GDP, indicate positive trend.
- Considering the slow deposit mobilisation and tight liquidity, we expect upward pressure on retail deposit rates.
- Margins in the immediate term may be adversely impacted due to lag effect on asset re-pricing; however, as credit offtake picks up and liquidity situation improves, margins will trend positively towards the latter half of FY11.
- NPL formation in retail is coming off, reducing credit costs, especially for private banks. However, we expect slippages on restructured asset pool to continue in H1FY10 and PSU banks credit cost to be relatively higher.

Recommendations

Top picks: Axis Bank, State Bank of India, ING VYSYA Bank, Federal Bank

Stocks to avoid: IOB

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
Allahabad Bank	NII + OI	10,086	9,986	1.0	11,446	(11.9)	Lower treasury gains and investment depreciation write-back will pull down overall PAT. Margins are expected to be benign.
	PPOP	5,256	3,766	39.6	5,969	(11.9)	
	Core PAT	2,676	3,029	(11.6)	2,245	19.2	
Axis Bank	NII + OI	24,125	20,042	20.4	23,936	0.8	NII buoyed by higher loan book average during the quarter. Asset quality is expected to be stable.Will maintain the 30% run-rate in profits.
	PPOP	13,191	8,503	55.1	12,808	3.0	
	Core PAT	7,387	5,620	31.4	7,649	(3.4)	
Bank of Baroda	NII + OI	24,571	19,077	28.8	25,118	(2.2)	Strong NII growth, led by improving domestic margins; marginal hit on CDO/CLN of INR .2bn.
	PPOP	13,820	7,545	83.2	14,220	(2.8)	
	Core PAT	8,258	6,854	20.5	9,063	(8.9)	
Federal Bank	NII + OI	5,235	4,375	19.7	5,403	(3.1)	Margins are expected to be sustained at 4%. Credit growth has seen pick-up with participation on BWA, 3G and real estate.
	PPOP	3,183	2,204	44.4	3,468	(8.2)	
	Core PAT	1,573	1,364	15.3	1,169	34.6	
HDFC	NII + OI	11,628	8,350	39.3	12,938	(10.1)	We expect disbursements to grow 25% Y-o-Y, leading to loan growth of 11%; margins are expected to come off from 4% levels in Q4FY10; NPLs would remain under control.
	PPOP	10,416	7,286	43.0	12,199	(14.6)	
	Core PAT	7,677	5,649	35.9	9,258	(17.1)	
HDFC Bank	NII + OI	32,778	28,992	13.1	32,549	0.7	Core fee income will be better, offsetting lower treasury income; no deviation from historical run-rate of 30%.
	PPOP	16,391	12,627	29.8	17,417	(5.9)	
	Core PAT	7,962	6,061	31.4	8,366	(4.8)	
ICICI Bank	NII + OI	36,159	40,751	(11.3)	39,258	(7.9)	NII will dip due to decline in loan book and impact of saving bank impact.Treasury income would be limited, coupled with marginal hit on CDO/CLNs. PAT to be supported by lower loan loss provisions.
	PPOP	20,848	18,151	14.9	22,029	(5.4)	
	Core PAT	9,536	8,782	8.6	10,056	(5.2)	
IDFC	NII + OI	4,693	4,010	17.0	5,000	(6.1)	Disbursement expected to be strong, led by BWA and 3G auctions. Expect margins to slightly come off. Standard provisions to pick up due to higher disbursement.
	PPOP	3,593	2,980	20.6	2,710	32.6	
	Core PAT	2,630	2,779	(5.4)	2,282	15.2	
Indian Overseas Bank	NII + OI	10,315	9,991	3.2	11,024	(6.4)	Margins will remain near Q4 levels. Upgradations and recovery is expected to be strong.
	PPOP	3,179	3,416	(6.9)	4,186	(24.0)	
	Core PAT	1,050	3,018	(65.2)	1,274	(17.6)	
ING Vysya Bank	NII + OI	4,060	3,316	22.4	4,258	(4.6)	Growth is expected to keep pace sequentially. Margins will come off due to the saving bank impact. Provisioning cost is expected to be high.
	PPOP	1,755	1,172	49.7	1,797	(2.4)	
	Core PAT	804	603	33.4	679	18.4	
Kotak Mahindra Bank	NII + OI	17,066	15,859	7.6	16,385	4.2	We expect advances to grow 30%, margins to sustain at 6%+ levels and NPL formation to come off; however, provisioning coverage will be increased to meet RBI's 70% mandate; Kotak Mahindra Prime will continue to maintain strong growth momentum; earnings of securities business will remain under pressure.
	PPOP	6,389	5,690	12.3	7,081	(9.8)	
	Core PAT	3,608	2,562	40.8	3,742	(3.6)	
LIC Housing Finance	NII + OI	3,681	2,110	74.4	3,469	6.1	We expect disbursement to grow at 40% plus; following historical trend, gross NPLs are expected to be higher in Q1FY11 as well.
	PPOP	2,793	1,780	56.9	2,856	(2.2)	
	Core PAT	1,750	1,238	41.4	2,135	(18.0)	
Manappuram General	NII + OI	1,583	NA	-	1,633	(3.1)	Disbursement momentum to continue at 20%+ levels.
	PPOP						
	Core PAT	368	NA	-	406	(9.5)	
Oriental Bank	NII + OI	12,143	8,760	38.6	12,548	(3.2)	Marigns will sustain at high levels of Q4. Asset quality is expected to deteriorate with slippages in the restructured pool.
	PPOP	7,183	2,809	155.7	7,494	(4.2)	
	Core PAT	2,881	2,574	11.9	3,170	(9.1)	
Power Finance Corp	NII + OI	7,345	7,053	4.1	7,702	(4.6)	Disbursements to grow at 25% plus; margins to come off due to rise in wholesale funding cost; MTM loss expected on forex borrowings compared with INR 630 mn profits in Q1FY10.
	PPOP	7,139	6,873	3.9	7,305	(2.3)	
	Core PAT	5,226	5,082	2.8	5,378	(2.8)	
Punjab National Bank	NII + OI	31,712	28,320	12.0	33,511	(5.4)	Treasury gains are expected to moderate. We expect credit growth at 22% Y-o-Y.
	PPOP	18,388	12,109	51.9	21,130	(13.0)	
	Core PAT	9,410	8,321	13.1	10,536	(10.7)	
REC	NII + OI	8,155	6,355	28.3	8,011	1.8	Disbursements to grow at 25% plus; margins to come off due to rise in wholesale funding cost.
	PPOP	7,825	6,056	29.2	7,529	3.9	
	Core PAT	5,790	4,720	22.7	5,612	3.2	

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
Reliance Capital	NII + OI	15,103	14,693	2.8	17,162	(12.0)	Limited investment gain in absence of stake sale in operating business; consumer financing book to grow to INR 93 bn; general premium expected to de-grow by 25% plus Y-o-Y.
	PPOP	1,885	1,786	5.5	1,140	65.4	
	Core PAT	1,159	1,533	(24.4)	637	81.9	
SBI	NII + OI	109,489	85,936	27.4	112,300	(2.5)	NII is expected to be strong with the improvement in LDR . Provisioning is expected to fall sequentially as the extension for provisioning coverage has come through.
	PPOP	49,740	29,651	67.8	47,683	4.3	
	Core PAT	28,406	23,304	21.9	18,666	52.2	
Shriram City Union	NII + OI	1,601	1,585	1.0	1,566	2.2	Disbursments run-rate expected at INR 5 bn plus per month on an average in Q1FY11; NPLs to remain under control; margins may come under pressure due to rise in wholesale funding cost.
	PPOP	1,076	958	12.3	986	9.1	
	Core PAT	523	451	16.2	454	15.2	
South Indian Bank	NII + OI	2,163	2,084	3.8	1,227	76.2	Margins are expected to improve sequentially, but settle at lower levels. Credit growth is expected to sustain at 25% +.
	PPOP	1,031	813	26.9	456	126.2	
	Core PAT	655	601	9.0	386	69.6	
SREI Infrastructure	NII + OI	930	878	5.9	1,195	(22.2)	Equipment finance business is estimated to generate PAT of INR 280 mn (where SREI holds 50% stake); balance profitability will flow from project financing and advisory business.
	PPOP	580	582	(0.3)	833	(30.3)	
	Core PAT	301	384	(21.7)	462	(34.8)	
Syndicate Bank	NII + OI	10,399	10,018	3.8	10,886	(4.5)	Growth is expected to be steady on the outflow on 3G auctions. Margins will come off due the saving bank impact.
	PPOP	5,273	3,058	72.4	5,509	(4.3)	
	Core PAT	2,116	2,616	(19.1)	1,682	25.8	
Union Bank	NII + OI	18,257	13,303	37.2	18,887	(3.3)	Margins are expected to be sustained due to better LDR. However, the key monitorable would be slippages from the restructured pool.
	PPOP	11,110	5,785	92.1	9,755	13.9	
	Core PAT	6,053	4,422	36.9	5,935	2.0	
Yes Bank	NII + OI	4,035	3,089	30.6	4,043	(0.2)	NII growth is expected to be strong as benefit of higher loan averages kicks in. Fee income growth is expected to sustain at high levels.
	PPOP	2,615	1,528	71.1	2,576	1.5	
	Core PAT	1,441	1,001	44.0	1,400	2.9	

Valuation snapshot

		Mkt Cap	Price (INR)	PAT growth (%, Y-o-Y)		P/E		P/B		RoE		Div yld	
	Reco	USD mn		FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E
Allahabad Bank	Buy	1,529	160	9.7	40.4	5.4	3.8	1.0	0.8	20.7	24.1	3.4	3.4
Axis Bank	Buy	10,773	1,237	29.5	28.0	15.4	12.0	2.7	2.3	18.8	20.5	1.2	1.4
Bank of Baroda	Buy	5,578	716	(5.3)	36.2	9.0	6.6	1.6	1.4	19.6	22.4	2.1	2.1
Federal Bank	Buy	1,207	330	35.6	23.5	9.0	7.2	1.1	1.0	12.8	14.2	1.8	2.1
HDFC	Hold	18,129	2,916	20.8	19.6	24.5	20.5	4.4	3.9	20.0	20.2	1.2	1.5
HDFC Bank	Hold	18,816	1,913	31.8	29.7	22.5	17.4	3.6	3.1	16.9	19.0	0.8	1.0
ICICI Bank	Buy	20,051	840	26.8	29.6	18.3	14.2	1.7	1.6	9.6	11.5	1.5	1.7
IDFC	Hold	5,008	180	8.1	27.3	20.4	16.0	2.9	2.6	15.4	17.1	0.8	0.8
Indian Overseas Bank	Hold	1,203	103	(20.3)	71.6	10.0	5.8	0.8	0.7	8.4	13.2	1.9	3.9
ING Vysya Bank	Buy	912	355	25.8	29.5	14.0	10.8	1.7	1.5	12.9	14.9	0.8	1.1
Kotak Mahindra Bank	Buy	5,665	759	10.7	20.5	19.3	16.0	3.0	2.5	16.1	16.6	0.2	0.3
LIC Housing Finance	Buy	1,967	968	20.5	23.4	11.5	9.3	2.2	1.9	21.3	22.0	1.8	2.1
Manappuram General Finance	Buy	519	71	71.8	44.5	11.8	8.2	3.1	2.4	29.4	32.3	0.8	1.2
Oriental Bank	Buy	1,717	320	13.8	36.7	6.2	4.5	1.0	0.8	16.4	19.4	1.9	1.9
Power Finance Corp	Buy	7,224	294	17.4	16.6	13.5	11.6	2.2	1.9	17.6	18.0	1.7	1.9
Punjab National Bank	Buy	7,059	1,046	14.3	30.6	7.7	5.9	1.7	1.4	23.9	25.7	2.4	3.2
REC	Buy	6,204	294	20.6	21.4	12.0	9.9	2.3	1.9	20.3	21.2	2.2	2.2
Reliance Capital	Hold	3,980	757	162.9	(9.5)	16.7	18.5	2.2	2.0	0.0	0.0	0.9	0.9
SBI	Buy	30,772	2,265	19.4	33.7	13.1	9.8	1.9	1.7	15.6	18.4	1.8	2.0
Shriram City Union Finance	Buy	496	471	14.1	25.3	10.5	8.4	2.0	1.6	20.3	21.2	0.8	0.8
South Indian Bank	Buy	413	171	14.4	22.8	7.2	5.9	1.1	1.0	17.0	18.0	2.3	2.3
SREI Infrastructure	UR	200	81	4.5	19.3	6.6	5.6	0.7	0.6	10.9	11.9	1.9	1.9
Syndicate Bank	Buy	1,022	92	24.2	20.7	4.7	3.9	0.8	0.7	17.9	18.6	3.3	4.4
Union Bank	Buy	3,359	311	2.7	36.4	7.4	5.4	1.5	1.2	21.9	24.4	1.8	1.8
Yes Bank	Buy	1,951	268	36.8	30.7	13.9	10.6	2.5	2.0	19.3	20.9	0.6	0.6

Source: Edelweiss research

CEMENT

Edelweiss
Ideas create, values protect

Cautious outlook

July 5, 2010

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Key highlights of the sector during the quarter

Q1FY11 has been a mixed bag for the sector in terms of pricing and demand. Prices increased (up ~INR 5-20/bag) across regions in the first half of the quarter. Cement off take was robust with average inventory at ~3-5 days with dealers across regions. Non-availability of rail wagons curbed inter-regional movement, thereby helping prices to sustain. In the second fortnight of May and in June prices corrected by ~INR 5-35/bag (price corrections being highest in AP), thereby negating price increases in the first half of the quarter. Our interactions with dealers and industry participants suggest that pricing pressure re-surfaced due to drop in demand and excess supply hitting markets.

Result expectations for the sector and stocks under coverage

Volume growth for our coverage universe has been in the range of (7%)-3%. We expect realisations to dip by ~INR 3-5/bag for our coverage universe. While we expect the EBITDAM to be in the 22-30% range for pan India players, ICEM is likely to report EBITDAM of 15% because of its high exposure to South where pricing pressure has been severe in the recent past. While we expect margins to dip by ~50-300bps for our coverage universe, UTCL's margins are likely to expand 180bps since they were subdued in Q4FY10 due to higher one-off expenses.

Outlook over the next 12 months

Our sector outlook remains cautious as we expect supply influx to lead to weaker pricing power for cement companies on the back of increased costs. We expect FY11 to be marked by supply pressures on account of ramping up of recently commissioned capacities along with commissioning of new capacities. We expect available capacity addition of ~48 mtpa in FY11E (our supply projections factor in 50% utilisation rate for the first two quarters of operation of a new capacity). After factoring an 11% demand growth in FY11, we expect 47.5 mtpa of surplus. Accordingly, all-India utilisation rates will correct from ~91% in FY10 to ~82% in FY11E. Inter-regional movement is likely to remain a key threat to the pricing power of cement companies going forward.

Recommendations

Top picks: Grasim

Stocks to avoid: India Cements

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
ACC	Revenues	19,817	20,813	(4.8)	21,018	(5.7)	Realisations are expected to decrease by ~1.5 % Q-o-Q on account of price corrections across regions because of lower demand and inter-regional movement. Volumes are also expected to be down for the quarter by 4% and EBITDA/tonne is expected to be flat at ~INR 1,090.
	EBITDA	5,800	7,175	(19.2)	6,095	(4.8)	
	Core PAT	3,538	4,854	(27.1)	4,051	(12.7)	
Ambuja Cements	Revenues	20,215	18,474	9.4	19,902	1.6	Realisations are expected to be down by 2% Q-o-Q because of low presence in the southern region where price correction has been the maximum. Revenues are expected to increase by 10% Y-o-Y on account of higher volumes, which are expected to rise because of strong demand from the northern and western regions.
	EBITDA	6,123	4,817	27.1	6,227	(1.7)	
	Core PAT	3,638	3,267	11.4	4,421	(17.7)	
Grasim Industries	Revenues	51,798	51,228	1.1	54,750	(5.4)	VSF prices are expected to rise by ~INR 3-5/kg and VSF volumes to be lower on account suspension of production at Nagda (Madhya Pradesh) plant due to non- availability of water. Cement volumes would be healthy and EBITDA margins are expected to be lower on account of higher power and fuel and freight cost.
	EBITDA	12,519	15,675	(20.1)	13,668	(8.4)	
	Core PAT	6,660	7,440	(10.5)	6,419	3.8	
India Cements	Revenues	8,737	9,535	(8.4)	9,643	(9.4)	Revenues are expected to be down by 9% Q-o-Q because of very low demand and lower realisations in the southern market (92% of the sales). EBITDA/tonne is expected to lower at ~INR 432 for the quarter.
	EBITDA	1,223	2,863	(57.3)	1,260	(3.0)	
	Core PAT	284	1,232	(77.0)	262	8.5	
UltraTech Cement	Revenues	17,457	19,528	(10.6)	19,094	(8.6)	Realisations and volumes are expected to decline by ~3% and ~5% Q-o-Q, respectively. EBITDA/tonne is expected at ~INR 735.
	EBITDA	3,941	7,168	(45.0)	4,026	(2.1)	
	Core PAT	2,016	4,179	(51.8)	2,285	(11.8)	

Valuation snapshot

		Mkt Cap	Price (INR)	PAT growth (%, Y-o-Y)		P/E		P/B		RoE		Div yld	
	Reco	USD mn		FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E
ACC	Reduce	3,467	863	38.0	(32.6)	10.1	15.0	2.7	2.4	29.4	17.0	2.6	2.1
Ambuja Cements	Reduce	3,679	113	11.3	(21.9)	14.1	18.1	2.6	2.4	19.9	13.7	1.6	1.4
Grasim Industries	Hold	3,585	1,827	(17.7)	(10.8)	6.3	6.9	1.0	0.9	19.4	15.2	1.6	1.5
India Cements	Reduce	700	107	(6.3)	(12.9)	8.1	9.3	0.8	0.8	10.6	8.5	1.2	1.1
UltraTech Cement	Reduce	2,319	871	(24.9)	(20.7)	11.5	14.6	1.9	1.7	18.1	12.5	0.6	0.4

Source: Edelweiss research

CONSTRUCTION

Bright outlook

July 5, 2010

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Key highlights of the sector during the quarter

Q1FY11 was a strong quarter for the construction sector with healthy order inflows amidst an improving economic outlook. Order activity was particularly strong in the urban infra segment. Road projects (from NHAI) also contributed to bulging order books of companies. In addition, a large number of NHAI projects are in the bidding stage, holding promise of continued traction in the future. Orders from the industrial capex space are picking up. However, uncertainty regarding Andhra irrigation projects continues; most companies have adopted a 'wait-and-watch' attitude towards these projects with some slowing /stopping their execution. Interest rates remained flat with abundant liquidity, which aided financial closure of BOT projects. Reduced risk perception of these projects with an uptick in economic indicators also worked in their favour. With commodity prices in check, we expect margins to remain stable after a good show in FY10.

Result expectations for the sector and stocks under coverage

After disappointing performance by some companies in FY10 on the top line front, we expect things to improve in the current year. For our coverage universe, we expect top line to grow 20% Y-o-Y. Owing to seasonality, we, however, expect revenues to decline 22% Q-o-Q (ex JPA). Execution on Andhra irrigation projects will be a key moniterable for HCC, IVRCL, and Patel Engineering.

We expect EBITDA margins to be more or less flat Y-o-Y as commodity prices have remained stable. Similarly, PAT margins are also likely to post a marginal 20bps increase over Q1FY10. As a result of lower base on which capital charges will be absorbed, PAT margins are expected to decline sequentially.

Outlook over the next 12 months

Outlook for the construction sector is positive over the next year. We expect order inflows to remain strong with the government's emphasis on infrastructure development. We expect traction in the roads space to continue with a large number of projects slated to be awarded by NHAI in the near future. Irrigation, urban infra, and power sectors are also expected to corner a fair share of government focus. With improvement in the realty scenario, we expect the building contracting space to see enhanced action in FY11. After a benign FY10, we expect both commodity prices and interest rates to increase in FY11. However, the impact on construction companies is expected to be minimal as the changes are more or less expected and are unlikely to catch companies by surprise. Fund availability is not expected to be a concern; this is likely to aid the funding-intensive construction sector, both in the form of working capital availability and long-term funds for BOT projects. A spate of BOT projects wins as well as foray by many companies into the power development space implies that FY11 is likely to see a significant fund raising exercise by many companies.

Recommendations

Top picks: IRB Infra and Patel Engineering

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
BL Kashyap & Sons	Revenues	3,063	2,131	43.8	2,919	4.9	Any possible expansion in margins need to be watched
	EBITDA	260	171	51.8	232	12.1	
	Core PAT	106	79	33.4	142	(25.3)	
C&C	Revenues	4,081	1,742	134.3	3,170	28.7	Ability to maintain margins is a key concern
	EBITDA	717	470	52.6	817	(12.3)	
	Core PAT	120	196	(38.6)	109	10.6	
Gammon India	Revenues	9,398	8,617	9.1	16,678	(43.6)	Execution is a key moniterable since management has given an aggressive guidance for FY11
	EBITDA	874	1,001	(12.7)	1,102	(20.7)	
	Core PAT	259	251	3.3	548	(52.8)	
IRB Infrastructure	Revenues	6,290	4,141	51.9	5,017	25.4	Execution on EPC projects needs to be watched
	EBITDA	2,642	1,662	59.0	2,310	14.4	
	Core PAT	1,251	851	46.9	1,487	(15.8)	
IVRCL Infra	Revenues	12,974	10,860	19.5	18,904	(31.4)	Execution emerges as a key moniterable after disappointment in the last year
	EBITDA	1,246	996	25.1	1,984	(37.2)	
	PBT	437	351	24.5	853	(48.7)	
Jaiprakash Assoc.	Revenues	25,592	21,169	20.9	33,465	(23.5)	Declared cement volumes at ~3.7 mn tonnes, with a marginal dip in realisations of ~INR 5/bag. Construction revenues are likely to be contributed from the Yamuna Expressway and the Karcham Wangtoo projects. Real estate has recorded good pre-sales in Noida during the quarter.
	EBITDA	6,769	5,915	14.4	8,668	(21.9)	
	Core PAT	1,223	2,181	(43.9)	4,314	(71.7)	
Nagarjuna Const.	Revenues	12,607	10,010	25.9	15,227	(17.2)	Ability to maintain margins need to be watched out for
	EBITDA	1,286	1,038	23.9	1,528	(15.8)	
	Core PAT	485	382	26.9	1,026	(52.7)	
Patel Engg	Revenues	7,471	6,430	16.2	11,971	(37.6)	Revenue growth is a concern due to sizeable share of Andhra irrigation projects
	EBITDA	1,188	1,057	12.4	1,510	(21.3)	
	PBT	385	381	0.9	649	(40.7)	
Simplex Infra	Revenues	11,581	11,309	2.4	12,811	(9.6)	Pickup in revenues needs to be seen after a soft performance in FY10
	EBITDA	1,170	1,161	0.7	1,325	(11.7)	
	Core PAT	323	284	13.7	439	(26.4)	
HCC	Revenues	9,119	8,760	4.1	10,850	(16.0)	Revenue growth is a concern due to sizeable share of Andhra irrigation projects
	EBITDA	1,094	1,151	(4.9)	1,230	(11.1)	
	Core PAT	222	182	22.0	430	(48.3)	

Valuation snapshot

	Reco	Mkt Cap USD mn	Price (INR)	PAT growth (%, Y-o-Y) FY11E	FY12E	P/E FY11E	FY12E	P/B FY11E	FY12E	RoE FY11E	FY12E	Div yld FY11E	FY12E
BL Kashyap & Sons	Buy	150	340	23.6	41.1	13.5	9.6	1.2	1.1	9.6	12.1	0.3	0.3
C&C Construction	Buy	110	239	(30.7)	0.0	13.0	0.0	1.0	0.0	7.9	0.0	1.1	0.0
Gammon India	Buy	597	219	(9.0)	13.0	17.9	15.8	1.2	1.1	7.5	7.8	0.2	0.2
HCC	Buy	763	118	27.1	45.0	34.4	23.8	2.2	2.1	6.7	9.1	0.7	0.7
IRB Infrastructure	Buy	1,870	263	37.5	0.0	16.1	0.0	3.5	0.0	23.8	0.0	0.6	0.0
IVRCL Infra	Buy	1,068	187	22.6	18.1	19.5	16.5	2.4	2.1	13.0	13.5	0.4	0.4
Jaiprakash Associates	Buy	5,778	127	(33.0)	15.0	27.2	20.2	2.7	2.4	11.5	12.6	0.9	1.1
Nagarjuna Construction	Buy	1,029	187	16.8	20.6	22.5	18.6	2.0	1.8	9.2	10.2	0.7	0.7
Patel Engg	Buy	619	414	15.2	23.3	12.6	10.2	1.8	1.6	15.9	16.9	0.5	0.5
Simplex Infra	Hold	497	469	15.9	25.4	16.0	12.7	2.0	1.8	13.7	15.1	0.4	0.4

Source: Edelweiss research

ENGINEERING & CAPITAL GOODS

Gaining momentum

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Key highlights of the sector during the quarter

The overall order flow across various infrastructure verticals like power, oil & gas, etc. has seen an improving traction in the past three-four quarters, which has led to healthy revenue visibility for many companies operating in the space. This, we believe, should augur well for overall execution growth in the sector, especially in segments like power. Also, with private sector expected to increasingly participate in key infrastructure verticals like power, roads, among others, the overall activity level in the industrial space is further expected to improve. We do not foresee any major input cost blues impacting sector margins.

Result expectations for the sector and stocks under coverage

We expect the overall sector to report a healthy revenue growth of 24% and PAT growth of 20% Y-o-Y. L&T and BHEL are expected to report strong execution growth with some input cost benefits. In the T&D space, we expect profit growth to be primarily driven by strong execution; order book accretion will be the key aspect to watch out for. In the EPC space, revenue visibility will drive the earnings growth. While European revenues could be a drag for Crompton Greaves, its domestic revenues are likely to report healthy growth.

Outlook over the next 12 months

We remain upbeat about overall growth prospects of the engineering and capital goods space and expect the same to benefit from the industrial revival. Growth visibility has improved over the past few quarters, with several large ticket orders being awarded in power generation equipment, T&D, oil & gas, industrial infrastructure segments, etc.

Our interactions with a few companies suggest a strong pipeline of orders in the power sector in both generation and T&D due for award in the next three-five quarters. Also, mining, construction and other allied activities are expected to see decent traction, which augurs well for the sector. The corporate top brass across industrials space seems to be much more confident of their growth numbers than earlier.

Recommendations

Top picks: BHEL, ABB, Cummins, Voltas, and Havells

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
ABB	Revenues	17,919	15,148	18.3	14,752	21.5	We expect an improving revenue trend for ABB.
	EBITDA	2,005	1,401	43.1	223	799.1	
	Core PAT	1,252	966	29.6	722	73.4	
AIA Engineering	Revenues	2,540	2,267	12.0	2,501	1.5	We expect realisation to remain flat Q-o-Q and volumes to grow 2%.
	EBITDA	546	563	(3.0)	483	13.1	
	Core PAT	413	407	1.4	392	5.5	
Bajaj Electricals	Revenues	4,765	3,654	30.4	7,842	(39.2)	Expect strong revenue growth on the back of execution in the project business. Higher commodity prices likely to impact margin.
	EBITDA	432	357	21.0	923	(53.2)	
	Core PAT	214	164	30.5	425	(49.6)	
BGR Energy	Revenues	8,062	3,111	159.1	16,598	(51.4)	We expect the pick-up in order execution seen in Q4FY10 to continue during the current quarter for both the BoP and EPC orders, thus recording strong growth in revenue and earnings.
	EBITDA	921	422	118.2	1,752	(47.4)	
	Core PAT	500	202	147.5	1,083	(53.8)	
BHEL	Revenues	77,661	56,714	36.9	139,446	(44.3)	Strong execution, coupled with input cost benefits, expected for the quarter.
	EBITDA	8,709	5,920	47.1	28,728	(69.7)	
	Core PAT	5,884	4,706	25.0	19,096	(69.2)	
Crompton Greaves	Revenues	23,883	21,975	8.7	25,079	(4.8)	Domestic revenues to see a healthy growth; European revenues could be a drag this quarter.
	EBITDA	2,760	2,476	11.5	4,027	(31.5)	
	Core PAT	1,706	1,604	6.4	2,713	(37.1)	
Cummins India	Revenues	8,037	6,256	28.5	7,883	2.0	Volumes to improve in Q1FY11 for Cummins from domestic market.
	EBITDA	1,288	1,037	24.2	1,609	(20.0)	
	Core PAT	1,007	897	12.3	1,183	(14.9)	
Havells India	Revenues	6,863	5,899	16.3	7,080	(3.1)	Expect moderate growth in revenue and strong growth in earnings. Exports to Sylvania expected to pick up.
	EBITDA	827	724	14.2	866	(4.5)	
	Core PAT	598	493	21.3	644	(7.1)	
Jyoti Structures	Revenues	5,584	4,858	14.9	5,477	2.0	Expect 10-12% exuection growth. Order flows to remain crucial for valuations.
	EBITDA	590	539	9.5	717	(17.7)	
	Core PAT	250	224	11.6	253	(1.2)	
KEC International	Revenues	8,319	7,266	14.5	13,451	(38.2)	Expect muted profit growth due to high-margin quarter last year.
	EBITDA	906	856	5.8	1,239	(26.9)	
	Core PAT	393	382	2.9	544	(27.8)	
Kalpataru Power	Revenues	6,685	4,873	37.2	8,383	(20.3)	Execution to drive profit growth in Q1. Fresh orders to remain key to valuation in the near term.
	EBITDA	769	584	31.7	926	(17.0)	
	Core PAT	410	321	27.7	574	(28.6)	
L&T	Revenues	90,187	73,627	22.5	133,749	(32.6)	Execution to pick up for L&T as order book piles up during H2FY10.
	EBITDA	11,031	8,319	32.6	20,508	(46.2)	
	Core PAT	7,389	5,783	27.8	13,374	(44.8)	
Punj Lloyd	Revenues	30,402	29,728	2.3	17,765	71.1	PLL is further expected to report provisions for subsidiaries, which could impact Q1FY11 profits adversely.
	EBITDA	2,246	3,094	(27.4)	(5,147)	143.6	
	Core PAT	597	1,250	(52.2)	(6,233)	109.6	
Siemens	Revenues	20,152	19,177	5.1	22,261	(9.5)	Expect a muted Q3 for Siemens; execution growth to come in Q4FY10E.
	EBITDA	2,492	2,573	(3.1)	2,861	(12.9)	
	Core PAT	1,546	1,680	(8.0)	1,811	(14.6)	
Techno Electric	Revenues	1,559	1,235	26.2	2,040	(23.6)	Renewable energy portfolio expected to continue to help the company post higher revenues and earnings during the quarter.
	EBITDA	162	123	31.7	240	(32.5)	
	Core PAT	208	194	7.2	275	(24.4)	
Thermax	Revenues	7,170	5,376	33.4	12,193	(41.2)	Strong revenue visibility to drive earnings growth.
	EBITDA	1,028	689	49.2	1,466	(29.9)	
	Core PAT	688	465	47.9	(157)	538.2	

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
Voltamp	Revenues	1,227	1,042	17.8	1,821	(32.6)	Capacity utilisation to watch out for, given excess capacity in the small transformer range. Margins expected to be under pressure. Expect volumes to improve, while realisations could be under pressure.
	EBITDA	185	162	14.2	369	(49.9)	
	Core PAT	151	149	1.3	265	(43.0)	
Voltas	Revenues	14,799	11,789	25.5	17,269	(14.3)	Expect growth momemtum to continue in the UCP division. Execution could pick for the large order backlog during the current and next few quarters.
	EBITDA	1,290	1,007	28.1	1,856	(30.5)	
	Core PAT	976	709	37.7	1,485	(34.3)	

Valuation snapshot

		Mkt Cap	Price (INR)	PAT growth (%, Y-o-Y)		P/E		P/B		RoE		Div yld	
	Reco	USD mn		FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E
ABB	Buy	3,906	861	64.1	23.8	30.8	24.9	6.1	5.0	21.7	21.9	0.3	0.3
AIA Engineering	Hold	743	368	20.4	14.3	16.7	14.6	3.1	2.6	20.2	19.2	0.4	0.5
Bajaj Electricals	Buy	461	221	31.2	27.0	13.3	10.5	3.4	2.7	28.4	28.9	1.5	1.9
BGR Energy	Buy	1,110	721	41.8	28.1	18.2	14.2	5.2	3.9	33.4	31.1	0.4	0.4
BHEL	Buy	25,055	2,392	28.5	22.3	21.1	17.3	5.8	4.6	30.6	29.6	0.9	1.1
Crompton Greaves	Buy	3,454	252	2.5	12.8	19.1	14.0	5.3	4.4	30.3	28.4	1.9	2.3
Cummins	Buy	2,513	593	13.8	34.2	23.2	17.3	6.1	4.8	29.0	30.9	1.5	1.5
Havells India	Buy	811	630	NM	22.1	14.1	11.5	5.1	3.5	43.9	36.0	0.4	0.4
Jyoti Structures	Hold	265	151	16.1	16.1	11.6	10.0	2.1	1.7	19.5	18.9	0.6	0.6
KEC International	Buy	511	473	31.8	21.8	10.4	8.5	2.6	2.1	29.2	27.9	1.3	1.3
Kalpataru Power	Hold	690	1,050	(1.5)	10.5	16.6	15.0	2.0	1.8	15.0	12.7	0.7	0.7
L&T	Hold	23,052	1,786	21.1	26.3	25.5	20.2	4.4	3.7	18.7	20.0	0.7	0.8
Punj Lloyd	Hold	949	134	(40.1)	34.2	11.1	8.2	1.1	1.0	3.2	8.7	0.2	0.2
Siemens	Hold	5,189	719	1.5	8.0	29.7	27.5	6.0	5.1	21.9	20.1	0.7	0.7
Techno Electric	Buy	333	273	7.5	15.4	12.0	10.4	3.4	2.6	32.9	28.4	0.4	0.4
Thermax	Buy	1,904	747	36.6	18.3	25.1	21.2	6.5	5.2	29.2	27.2	0.7	0.7
Voltamp	Hold	201	929	4.4	9.3	10.9	10.0	2.3	1.9	23.4	21.2	1.3	1.3
Voltas	Buy	1,430	202	(5.5)	25.8	17.3	13.8	5.5	4.3	35.8	34.9	0.9	0.9

Source: Edelweiss research

FMCG

FY10 momentum continues in Q1FY11

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Key highlights of the sector during the quarter

The cigarettes segment of ITC saw weighted average price increase of ~13%, to offset increase in excise duties. Volume growth is, however, likely to be only marginally negative as cigarette demand is largely inelastic. Asian Paints has undertaken price hikes of ~4% (in May) and then another ~2.8% (w.e.f. July 01), to offset input costs inflation. Intensive promotional activities were seen in several FMCG categories.

Result expectations for the sector and stocks under coverage

We expect good volume growth from HUL, Dabur, Emami, USL, and Asian Paints. As most FMCG companies were gaining from COGS deflation in the past few quarters, we believe, Q1FY11 will see a return of inflation, albeit not to an extent as feared by the market. As a result, we believe, margins have peaked, and Q1FY11 will see some pressure on margins. Higher advertising and sales promotion (A&P) spend will add pressure on margins. HUL is likely to report flat growth in profits, following price cuts in mass segments and higher A&P spend. ITC is likely to be slightly impacted by cigarettes price hikes, while all other businesses (agri, paper and hotels) are likely to continue to grow at more than 15%. Colgate will be impacted by higher tax rate, resulting in muted profit growth.

Outlook over the next 12 months

We believe volumes (with benign pricing) will drive revenue and profitability growth in FY11. While pricing power will be limited, cost inflation is currently a concern for some FMCG players; there will be decline in costs for some companies like USL. The India Meteorological Department (IMD) has revised up the forecast for rainfall to 102% of the Long Period Average (LPA) from 98% of the LPA projected in April. If this holds true, then prices of agri commodities will cool down, benefiting FMCG companies. We expect both rural and urban India to drive the FMCG demand. As competition from regional and MNC players is heating up, the FMCG sector is witnessing higher A&P spend. We expect these higher levels of A&P to continue in the medium term. Dabur and Emami are likely to announce outbound M&A deals in FY11.

Recommendations

Top picks: ITC, Asian Paints, Dabur, United Spirits and Emami

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
Asian Paints	Revenues	16,900	14,602	15.7	18,768	(10.0)	Domestic paints volume to continue the Q4FY10 momentum. Y-o-Y numbers will look slightly muted on a strong base.
	EBITDA	3,172	2,758	15.0	3,109	2.0	
	Core PAT	2,050	1,761	16.4	1,926	6.4	
Colgate	Revenues	5,600	4,680	19.7	5,166	8.4	Colgate should report continued steady sales growth while maintaining its toothpaste market share. Gross margins likely to be stable. However, key monitorable will be ad spends.
	EBITDA	1,350	1,052	28.4	1,247	8.2	
	Core PAT	1,160	1,028	12.9	1,144	1.4	
Dabur	Revenues	8,700	7,427	17.1	8,488	2.5	Dabur is expected to maintain good volume growth and steady EBITDA margins.
	EBITDA	1,431	1,182	21.0	1,620	(11.7)	
	Core PAT	1,150	910	26.3	1,353	(15.0)	
Godrej Consumer	Revenues	7,200	4,389	64.1	5,092	41.4	Volume growth in soaps likely to be weak following intense competition, growth rates likely to dip due to food inflation and higher base. Margins to be slightly impacted from rise in palm oil prices.
	EBITDA	1,400	864	62.0	1,075	30.2	
	Core PAT	1,050	697	50.7	918	14.4	
Hindustan Unilever	Revenues	46,995	44,757	5.0	43,158	8.9	We expect HUL to post 7% volume growth with market share gain in few categories. PAT is, however, likely to be muted following price cuts and higher ad spends.
	EBITDA	6,950	6,881	1.0	5,310	30.9	
	Core PAT	5,450	5,394	1.0	5,291	3.0	
ITC	Revenues	47,200	40,827	15.6	50,538	(6.6)	All businesses expected to do well. Cigarette volumes are expected to be flat following ~13% price increase post budget. Hotels, along with agri and paper product businesses, are expected to contribute meaningfully to profitability.
	EBITDA	15,377	13,371	15.0	15,401	(0.2)	
	Core PAT	10,200	8,787	16.1	10,282	(0.8)	
Marico	Revenues	7,700	6,967	10.5	6,023	27.9	Volume growth is expected to be strong, but taper down Q-o-Q and Y-o-Y because of higher base. Kaya is expected to be a drag on overall business growth.
	EBITDA	1,090	965	13.0	849	28.4	
	Core PAT	700	600	16.6	569	23.1	
Nestle India	Revenues	14,100	12,095	16.6	14,798	(4.7)	Volume growth is expected to be strong with a steady margin outlook, despite recent input cost inflation — likely due to price hikes and long-term sourcing contracts. No major surprises expected.
	EBITDA	3,050	2,618	16.5	3,040	0.3	
	Core PAT	1,890	1,620	16.7	2,019	(6.4)	
United Spirits	Revenues	14,200	12,417	14.4	12,521	13.4	Volume growth expected to be strong with a steady margin outlook. Numbers to look strong due to lower base in Q1FY10. Expect W&M FY11 EBITDA guidance.
	EBITDA	2,500	2,219	12.7	1,813	37.9	
	Core PAT	1,110	1,076	3.2	569	95.3	
Emami	Revenues	2,245	1,871	20.0	2,803	(19.9)	Emami is expected to maintain good volume growth and steady EBITDA margins. Q1FY11 to reap benefits of strong sales of Navratna Cool Talc.
	EBITDA	381	305	25.0	564	(32.4)	
	Core PAT	201	149	35.0	394	(49.0)	

Valuation snapshot

	Reco	Mkt Cap USD mn	Price (INR)	PAT growth (%, Y-o-Y) FY11E	FY12E	P/E FY11E	FY12E	P/B FY11E	FY12E	RoE FY11E	FY12E	Div yld FY11E	FY12E
Asian Paints	Buy	4,747	2,314	14.6	14.0	25.8	22.6	10.8	9.1	45.8	42.9	1.6	2.2
Colgate	Hold	2,440	839	4.0	11.1	25.9	23.3	43.3	40.2	173.0	179.0	3.2	3.5
Dabur	Buy	3,748	202	18.6	19.6	29.2	24.4	12.7	9.9	49.1	45.5	1.3	1.6
Emami	Buy	1,288	795	34.8	19.3	27.3	22.9	7.2	6.1	28.6	28.8	1.3	1.5
Godrej Consumer	Buy	2,288	345	28.4	15.7	24.4	21.1	13.1	10.9	58.7	56.6	2.4	2.8
Hindustan lever	Buy	12,532	268	8.9	12.9	25.7	22.8	21.6	17.3	90.1	84.3	2.8	2.8
ITC	Buy	24,719	303	14.5	16.1	24.9	21.4	6.2	5.4	26.8	27.1	1.7	2.0
Marico	Buy	1,650	127	24.5	21.4	26.7	22.0	9.4	7.3	39.9	37.4	1.1	1.3
Nestle India	Hold	6,169	2,990	22.6	22.4	44.0	36.0	49.6	40.4	124.2	123.8	1.6	2.0
United Spirits	Buy	3,420	1,273	37.3	22.0	25.7	21.1	3.0	2.6	12.3	13.3	0.6	0.6

Source: Edelweiss research

HOSPITALITY

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Ideas create, values protect

Good times to continue

July 5, 2010

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Key highlights of the sector during the quarter

Hotels across cities are witnessing better occupancies Y-o-Y due to strong revival in business sentiment. As per DGCA, air traffic rose 22% during January-May 2010 against the corresponding period in 2009, signaling strong revival in business. Occupancies are up 10-15% across major cities Y-o-Y, with Delhi and Kolkata witnessing more than 70% occupancy in April 2010. With the on-set of off-season, hotels are planning to maintain ORs at 65% plus. ARRs are likely to rise in August-September as demand continues to be strong. FTA growth in January-May was 11.3% (2.26 mn arrivals) against 15.5% during May Y-o-Y.

Result expectations for the sector and stocks under coverage

With ORs of 60-65% and 5-10% Y-o-Y increase in ARRs, we expect hotel companies to report strong EBIDTA margins of 30-35%. We expect Indian Hotels Company (IHCL) to provide some guidance of increase in ARRs, effective August-September onwards. We expect Mahindra Holidays (MHRIL) to report moderate jump over Q1FY10 (5,400 membership addition) and maintain 35% plus EBIDTA margin. With April-June being the holiday season in India, we expect Cox & Kings (CNK) to report strong numbers from Indian operations.

Outlook over the next 12 months

With strong revival in economic conditions, we expect hotel companies to report robust ORs and ARRs over the next 12 months. Strong revival in domestic air traffic during January-May is indicative of buoyancy in leisure and business traffic. Sports events like Commonwealth Games in Q3FY11 and the Cricket World Cup in Q4FY11 are expected to be conducive to hotels for reporting strong numbers. With increasing disposable incomes and increasing trend of holidaying, MHRIL is expected to benefit by way of increased memberships. With international operations already contributing more than 50% to sales, we expect CNK to report strong growth in numbers (we have not factored in any acquisition).

Recommendations

Top picks: Indian Hotels Company

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
Indian Hotels	Revenues	3,772	2,849	32.4	4,434	(14.9)	ORs to show strong growth Y-o-Y. Strong EBIDTA margins should continue.
	EBITDA	1,056	345	206.1	1,435	(26.4)	
	Core PAT	373	164	127.4	599	(37.7)	
Mahindra Holidays	Revenues	1,532	1,353	13.2	1,302	17.7	Membership addition is expceted to remain subdued. EBIDTA margins of 35%+ should continue.
	EBITDA	582	526	10.6	508	14.6	
	Core PAT	353	274	28.8	322	9.6	
East India Hotels	Revenues	2,472	2,181	13.3	2,743	(9.9)	ORs are expected to show strong jump Y-o-Y. Strong EBIDTA is expected to continue.
	EBITDA	791	675	17.2	835	(5.3)	
	Core PAT	228	191	19.4	255	(10.6)	
Hotel Leela ventures	Revenues	1,078	847	27.3	1,326	(18.7)	ORs are expected to show strong jump Y-o-Y. Strong EBIDTA is expected to continue.
	EBITDA	474	189	150.8	367	29.2	
	Core PAT	153	3	NM	95	61.1	
Cox and Kings	Revenues	1,234	996	23.9	1,369	(9.9)	Indian operations are expected to show strong performance. EBIDTA margins of 45% is expected to continue.
	EBITDA	540	364	48.4	720	(25.0)	
	Core PAT	349	299	16.7	452	(22.8)	

Valuations snapshot

		Mkt Cap	Price (INR)	PAT growth (%, Y-o-Y)		P/E		P/B		RoE		Div yld	
	Reco	USD mn		FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E
Indian Hotels	Buy	1,621	105	NM	76.7	NM	18.1	2.8	2.5	8.7	14.1	0.8	0.8
Mahindra Holidays	Reduce	946	525	32.2	36.1	28.6	21.0	8.2	6.4	31.7	34.2	0.8	0.9
EIH	Hold	1,017	121	128.6	22.0	30.3	24.8	3.2	3.0	11.0	12.5	1.2	1.2
Hotel Leela ventures	Reduce	387	48	22.3	(4.4)	44.0	46.0	3.1	3.0	6.5	6.0	0.6	1.1
Cox and Kings	Hold	631	469	33.9	25.4	19.3	15.4	2.9	2.5	16.4	17.7	0.3	0.5

Source: Edelweiss research

IT

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Ideas create, values protect

Robust demand environment continues

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Key highlights of the sector during the quarter

Demand recovery for large Indian vendors has strengthened as pent-up demand is now supported by revival of spend on revenue strategies (discretionary) in select verticals. Troubled verticals have also turned the corner and will start aiding revenue growth. There has been a surge in the order book and visibility for all large Indian vendors as clients now not only look to cut their IT costs and but also invest in developing and implementing solutions/ applications. These trends are clearly evinced from the recent Accenture results that saw solid demand for technology outsourcing and consulting services. However, this strong demand is also leading to supply side pressures that has led to higher wage hikes and also high attrition rates across the industry.

The recent global imbalance caused by the European sovereign crisis is used by companies to push faster offshore adoption and build front-end capabilities. Though business volumes are unlikely to be impacted by this crisis, the currency depreciation (EUR and GBP) will have a bearing on the financials.

Result expectations for the sector and stocks under coverage

We expect the Big-3 Indian IT players to report strong 5.1-6.5% surge in volumes Q-o-Q. However, due to cross-currency impact, revenue growth in INR terms may be restricted to 3.0-4.4%. EBITDA margins are expected to decline by 100-150bps Q-o-Q due to salary increases effective from April 01 (TCS and Infosys). Wipro will have full quarter impact of salary increases (effected in February). HCLT, with its highest exposure to Europe, will have the most impact in terms of revenue growth. Further, INR's 2.7% depreciation against USD on a quarter end closing basis will lead to MTM loss accumulation in OCI for all companies, particularly Wipro (as it has huge hedge position).

Infosys guidance: We see Infosys surpassing its revenue guidance of 2.6-3.4% Q-o-Q growth, despite currency impact. However, the full year FY11 guidance of 16-18% in USD terms is unlikely to be raised, in our view. Nevertheless, as the company rebases its INR/USD assumption from 44.5 to ~46.0, we see a **5% upgrade in INR EPS to 116 from INR 111 at upper band**.

Expect tier 2 companies to post revenue traction as client specific impact recedes. Infotech and Hexaware are expected to post strong 6-8% constant currency growth Q-o-Q. However, margin hit (due to salary increases) and loss on hedge maturing during the quarter will negatively impact net profits.

Outlook over the next 12 months

There seems to be limited room for upside for tier-1 companies, while value emerges in tier-2 companies, as business traction improves. We see the valuations at P/E of 19-22x for tier-1 companies factoring in 22% plus revenue growth, offering limited upside hereon. On the other hand, tier-2 companies with healthy cash position and improving business traction can offer significant upside. We see companies such as Hexaware ('BUY') and Sasken Communication ('Not Rated') offering opportunity to play the valuation re-rating story, while returns in Infotech Enterprises ('BUY') will be driven by earnings growth.

Recommendations

Top picks: TCS, Hexaware Technologies, and Infotech Enterprises

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
HCL Tech	Revenues	32,305	29,085	11.1	30,757	5.0	Cross currency impact of 1.5% on US$ revenues, EAS deals won in previous quarter have been ramping up, BPO business to hit bottom due to ramp down in voice business. EBITDA margin to be impacted by cross currency movement, hiring of sub-contractors for EAS and spend on global customer meet.
	EBITDA	5,960	6,441	(7.5)	6,073	(1.9)	
	Core PAT	2,512	3,088	(18.7)	3,215	(21.9)	
Hexaware	Revenues	2,370	2,591	(8.5)	2,220	6.8	Volumes to return as new projects ramp-up, margins likely to remain under pressure, any attrition challenges. Key would be the revenue outlook for Q3 and order book built-up.
	EBITDA	201	558	(63.9)	183	9.9	
	Core PAT	79	396	(80.0)	117	(32.3)	
InfoEdge	Revenues	684	529	29.4	653	4.9	Strong hiring trend to continue to drive revenues, reinvestment in non-recruitment verticals. Strategies to overcome increased competition in recruitment. Progress in offline centres for matrimony vertical.
	EBITDA	222	129	72.7	216	3.1	
	Core PAT	176	133	32.1	132	32.7	
Infosys	Revenues	61,858	54,720	13.0	59,440	4.1	Strong volume momentum due to ramp up of large deals won in earlier quarters, impact of salary hikes on margins to be modest due to improvement in utilisation and tighter cost control. FY11 EPS revision to Rs116 likely from Rs 111 at the higher-end due to INR depreciation but US$ revenue growth of 16-18% for FY11 likely to be maintained due to cross-currency impact and cautious global economic data.
	EBITDA	20,300	18,680	8.7	20,220	0.4	
	Core PAT	14,833	15,270	(2.9)	16,170	(8.3)	
Infotech	Revenues	2,562	2,326	10.1	2,441	5.0	Ramp up of Hamilton deal, traction in Daxcon's revenue run-rate, UTG segment's performance, margin to decline due performance with headwinds from wage hike and cross-currency. Demand trend in top-10 clients.
	EBITDA	526	524	0.4	526	(0.1)	
	Core PAT	433	462	(6.3)	514	(15.7)	
Mphasis	Revenues	12,395	11,056	12.1	12,205	1.6	Pricing - revision in Application segment and any further renegotiation. Volume outlook whether to be compensated for pricing decline. BPO reaching bottom, Recovery in BFSI segment and US.
	EBITDA	3,099	2,919	6.2	3,150	(1.6)	
	Core PAT	2,704	2,292	18.0	2,673	1.2	
Patni	Revenues	7,803	7,729	1.0	7,745	0.7	Supply constraint to continue to preclude growth uptick. Margins to be impacted due to salary hikes. Net hiring is key for improvement in growth.
	EBITDA	1,515	1,549	(2.2)	1,594	(5.0)	
	Core PAT	1,352	1,368	(1.2)	1,497	(9.7)	
TCS	Revenues	79,701	72,070	10.6	77,365	3.0	Trends in discretionary services, large deal wins, margin levers going forward, hiring trends. Expect 6.1% volume growth and 180bps margin delcine due to salary hike and cross currency headwinds. Forex loss of INR 980mn factored in for the quarter.
	EBITDA	22,634	19,620	15.4	23,121	(2.1)	
	Core PAT	17,150	15,203	12.8	19,320	(11.2)	
Wipro	Revenues	72,821	63,868	14.0	69,772	4.4	Expect USD 1,214mn revenues post USD 14mn cross currency impact. Better than expected volumes to negate the salarly impact as well. Huge hedge position to result in MTM losses in OCI. Outlook for Q2 - expect 3-5% guidance. Hiring expected to be strong.
	EBITDA	15,956	14,703	8.5	15,194	5.0	
	Core PAT	12,012	10,104	18.9	12,091	(0.7)	

Valuation snapshot

	Reco	Mkt Cap USD mn	Price (INR)	PAT growth (%, Y-o-Y) FY11E	FY12E	P/E FY11E	FY12E	P/B FY11E	FY12E	RoE FY11E	FY12E	Div yld FY11E	FY12E
HCL Tech	Hold	5,117	353	33.9	22.0	14.2	11.6	2.9	2.4	23.5	23.7	1.1	1.4
Hexaware	Buy	232	75	(36.7)	80.4	13.1	7.3	1.1	1.0	9.4	15.3	1.9	1.9
InfoEdge	Buy	517	885	37.2	32.3	32.3	24.8	5.3	4.4	17.0	18.7	0.2	0.2
Infosys	Hold	33,495	2,728	12.4	16.5	22.3	19.2	5.5	4.6	27.3	26.2	1.1	1.3
Infotech	Buy	444	187	5.8	12.5	11.7	10.7	1.9	1.6	17.7	16.7	1.3	1.2
Mphasis	Hold	2,678	597	20.3	(1.6)	11.5	11.7	3.8	2.9	38.5	28.2	0.7	0.8
Patni	Hold	1,413	508	30.7	(3.6)	11.6	12.3	1.9	1.7	18.3	15.0	0.6	0.5
TCS	Buy	31,151	744	9.4	12.7	19.3	17.2	5.5	4.5	31.8	28.7	1.1	1.3
Wipro	Buy	20,211	386	10.5	15.4	18.7	16.2	4.0	3.4	23.6	22.9	1.3	1.4

Source: Edelweiss research

MEDIA

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Ideas create, values protect

Positive trend continues

July 5, 2010

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Key highlights of the sector during the quarter

Momentum in media spends continues with recovery in the overall economy. The TV medium, in particular, has benefited from increased competitive intensity in the FMCG space (one of the largest ad spenders). *Star Plus* has consolidated its No. 1 position in the GEC space, with *Zee TV* at No.3. Increasing digitisation and DTH penetration continue to boost subscription revenues for all broadcasters. Newsprint prices have continued to trend upwards this quarter.

Result expectations for the sector and stocks under coverage

An improving business scenario and increased ad spends will lead to increased ad-revenues for Hindi GECs. ZEEL's flagship channel, *Zee TV,* continues to figure among the top 3 GEC channels. Sun TV continues to dominate the South Indian market. GECs' viewership is likely to dip as a result of IPL and FIFA World Cup matches during the quarter. However, TV ad revenues are expected to increase by INR ~12.74 bn in CY10 and IPL and FIFA World Cup are expected to take away INR ~3.5 bn out of this incrementally. Increasing digitisation is expected to continue to benefit subscription revenue stream of broadcasters. IPL has impacted the occupancies in multiplexes in March-April 2010 and the viewership of IPL in multiplexes has not been strong. Jagran Prakashan is expected to post good growth in ad revenues. Increasing competition could impact subscription revenues to some extent.

Outlook over the next 12 months

We maintain a positive outlook on ZEE Entertainment, Sun TV and Jagran Prakashan. With improvement in the overall economy and media spends, TV and print media are expected to grow at 15% and 9%, respectively, in CY10E. Internet and radio are expected to outperform the industry with 50% and 20% Y-o-Y growth, respectively. On the broadcasting front, we are bullish on companies in the GEC space. ZEEL is among the top three Hindi GEC channels and also has a strong presence in the regional GEC space. Sun TV enjoys dominance in three out of the four South Indian markets. Broadcasting companies are also expected to benefit from the increased share of subscription revenues with increasing digitisation and rapid rise in DTH subscriber numbers. TV-18 is also likely to benefit from the expected momentum in ad spends. Performance of multiplexes is expected to improve on the back of improving occupancies and ATP continuing to trend upwards. Competitive intensity in print space is expected to increase. Newsprint prices are likely to trend upwards marginally.

Recommendations

Top picks: Zee Entertainment, Sun TV, Jagran Prakashan

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
Jagran Prakashan	Revenues	2,650	2,318	14.3	2,363	12.2	Print ad revenues will continue to grow with ad spends improving across sectors, especially education. Subscription revnues could be under pressure as a result of increasing competition. Newsprint prices have gone up marginally by ~8%.
	EBITDA	750	705	6.4	633	18.6	
	Core PAT	500	495	1.0	364	37.4	
PVR	Revenues	890	345	157.9	784	13.6	Q1FY11 was also impacted by IPL tournaments in April 2010, but is expected to benefit from movie releases post IPL.
	EBITDA	164	(89)	284.5	98	68.0	
	Core PAT	40	(109)	136.7	10	296.0	
Sun TV	Revenues	3,750	2,877	30.4	3,919	(4.3)	IPL and FIFA World Cup are likely to impact viewership of GECs. Ad revenue growth expected to remain strong. Subscription revenue growth to be driven largely by contribution from DTH.
	EBITDA	3,050	2,236	36.4	3,309	(7.8)	
	Core PAT	1,450	1,198	21.0	1,651	(12.2)	
TV-18	Revenues	749	569	31.7	841	(10.9)	Performance of TV18's news business in Q1FY11 is expected to be muted compared with Q4FY10 as Q4FY10 had benefited from the budget related coverage.
	EBITDA	192	61	217.5	217	(11.5)	
	Core PAT	40	(264)	115.1	213	(81.2)	
Zee News	Revenues	625	1,374	(54.5)	601	4.0	Zee News is expected to benefit from increase in ad spends. Subscription revenue growth is expected to remain robust on the back of DTH growth. Numbers won't be comparable with Q1FY09, as Zee News trades ex R-GECs.
	EBITDA	73	248	(70.5)	39	88.3	
	Core PAT	36	119	(69.7)	21	75.1	
ZEEL	Revenues	6,450	4,759	35.5	6,493	(0.7)	IPL and FIFA World Cup are likely to impact viewership of GECs. However, ad revenues are expected grow with increase in ad volumes and incrementally higher ad rates. Subscription revenue growth is expected to remain robust on the back of DTH growth. Numbers won't be comparable with Q1FY09 as Q1FY11E will include R-GECs.
	EBITDA	1,849	1,170	58.0	1,836	0.7	
	Core PAT	1,331	1,019	30.6	1,273	4.6	

Valuation snapshot

		Mkt Cap	Price (INR)	PAT growth (%, Y-o-Y)		P/E		P/B		RoE		Div yld	
	Reco	USD mn		FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E
Jagran Prakashan	Buy	794	123	14.3	16.3	18.5	15.9	5.1	4.3	27.5	27.2	2.8	2.8
PVR	Buy	84	154	244.4	60.4	16.7	10.4	1.2	1.1	7.3	10.7	0.6	0.6
Sun TV	Buy	3,620	430	33.9	20.8	24.9	21.3	7.2	5.8	32.0	30.7	1.0	1.3
TV-18	Hold	367	94	125.4	260.6	150.3	41.7	1.9	1.8	1.6	4.4	0.0	0.0
Zee News	Buy	72	14	(66.4)	61.2	20.7	12.9	1.2	1.2	5.9	9.2	3.6	3.6
ZEEL	Buy	3,033	293	42.4	20.3	22.7	18.7	2.6	2.3	12.0	13.1	0.7	0.7

Source: Edelweiss research

METALS AND MINING

Edelweiss
Ideas create, values protect

Near term headwinds

July 5, 2010

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Key highlights of the sector during the quarter

Ferrous: In Q1FY11, average flat steel prices rose 8% while long product prices increased 2% sequentially (*Source: steelprices-india, CRISIL*). Post price hikes in April and May, steel prices corrected by ~INR 1,500-3,000/t in June due to destocking, global macro concerns and buyers adopting a "wait-and-watch" attitude. Also, higher raw material cost, especially coking coal is expected to start denting margins. However, on a 1-year basis we expect demand to remain strong and margins to recover.

Non-ferrous: LME prices are up 30-50% on a Y-o-Y basis. However, prices have declined sequentially by 3-12% across base metals due to global economic concerns and near term denting of demand. Margins of base metal companies are likely to get squeezed Q-o-Q (average 400 bps) due to price declines with costs being same and seasonally lower volumes during the quarter.

Result expectations for the sector and stocks under coverage

For ferrous companies, we expect EBITDA/t to start trending downwards (at INR 500-1,000/t) due to higher raw material cost (except JSPL as 50% capacity is sponge iron based) and demand softening towards the end of the quarter.

For steel companies under our coverage, EBITDA and PAT could decline Q-o-Q by 18% and 32%, respectively. However, the same will be higher Y-o-Y considering the much lower base of Q1FY10. We do not expect any production cuts, but anticipate inventory accretion. Sesa Goa's EBITDA is likely to rise ~4x Y-o-Y due to high iron ore volumes (6.2 mt, up 30% Y-o-Y) and iron ore prices (up 2.5x Y-o-Y).

In the non-ferrous space, production volume for most companies except Hindustan Zinc is estimated to be flat or dip marginally Q-o-Q. Hindustan Zinc and Sterlite are likely to witness steepest decline in margins among non-ferrous companies in Q1FY11 due to 12% Q-o-Q dip in zinc-lead prices with costs remaining unchanged. With aluminium prices declining only 3% Q-o-Q, impact on Hindalco is relatively lower. For non-ferrous companies, EBITDA and PAT could decline 27% Q-o-Q.

Outlook over the next 12 months

Ferrous: In H1FY11 we expect steel prices to remain subdued due to slower than expected growth. However, raw material prices during this period will continue to remain high causing a hit in EBITDA/t margins. H2FY11 should witnessing correction in iron ore and coking coal prices leading to margin improvement for steel players. Overall we believe, FY11 will be a difficult year as (1) demand will be sluggish in the developed world; (2) greater than expected slowdown in China; and (3) raw material prices correcting with a lag to steel prices

Non-ferrous: With sharp correction in LME prices in last month, we estimate ~25% of China aluminium capacity to be unviable at these prices. We expect marginal producers to undertake production cutbacks globally especially in aluminium and zinc which should provide some support to prices. Thus, we expect some squeeze in margins in H1FY11 while some uptick in demand and prices is likely in H2FY11.

Recommendations

Top picks: Ferrous: JSW Steel, Tata Steel

Non-ferrous: Hindalco, Sterlite

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
Bhushan Steel	Revenues	14,987	13,047	14.9	16,087	(6.8)	Degree of backward integration from recently commissioned facilities of HR coil, slabs and metalllics. Realisations should be ~INR 2,500/t higher than Q4FY10 average as product profile is flat product oriented. Raw material costs to be higher.
	EBITDA	4,400	2,969	48.2	4,192	5.0	
	Core PAT	2,068	1,719	20.3	2,409	(14.2)	
Hindalco (Standalone)	Revenues	50,883	38,995	30.5	54,044	(5.8)	3% Q-o-Q decline in aluminium prices, but stable costs. Blended TcRc assumed at 10 c/lb. Sharp oQ fall in Pat due to no tax write back
	EBITDA	7,725	7,578	1.9	8,354	(7.5)	
	Core PAT	4,767	4,806	(0.8)	6,639	(28.2)	
Hindustan Zinc	Revenues	19,357	15,266	26.8	25,449	(23.9)	12% Q-o-Q decline in zinc-lead prices to impact profitability.
	EBITDA	9,545	7,823	22.0	15,482	(38.3)	
	Core PAT	7,685	7,188	6.9	12,390	(38.0)	
JSPL (Consolidated)	Revenues	31,545	27,486	14.8	31,756	(0.7)	Realisations to be higher than Q4FY10 average by ~INR 1,000/t. Inventory build up possible due to soft demand towards quarter end. Possible volumes from the pellet plant. Coking coal costs increase as new contracts start to trickle in.
	EBITDA	15,846	15,973	(5.0)	14,587	8.6	
	Core PAT	9,892	9,885	0.1	9,634	2.7	
JSW (Consolidated)	Revenues	55,556	40,138	38.4	54,807	1.4	Assumed volumes of 1.42 mt and estimated EBITDA/t of USD 166 in standalone business. Realisations to increase by INR 2,000/t Q-o-Q.
	EBITDA	10,983	6,884	59.5	13,234	(17.0)	
	Core PAT	3,616	2,341	54.5	6,110	(40.8)	
Nalco	Revenues	14,638	9,352	56.5	16,260	(10.0)	Revenues to fall Q-o-Q due to 10% Q-o-Q decline in aluminium volumes (to 102 kt) and 3% Q-o-Q decline in prices.
	EBITDA	5,101	1,674	204.7	5,411	(5.7)	
	Core PAT	3,220	1,265	154.5	3,915	(17.7)	
SAIL	Revenues	87,101	91,528	(4.8)	119,552	(27.1)	Possible inventory accretion due to soft demand in end of May-June (est 0.6 mt). Realisations for the quarter to be higher by ~INR 1,000/t Q-o-Q. However, margins could possibly be under pressure due to higher coking coal/ staff costs.
	EBITDA	19,462	18,756	3.8	28,225	(31.0)	
	Core PAT	13,701	13,261	3.3	20,849	(34.3)	
Sesa Goa (Consolidated)	Revenues	28,494	10,115	181.7	24,189	17.8	Assumed iron ore sales volume of 6.2 mt and realisations of USD 96/t.
	EBITDA	17,818	4,531	293.2	15,030	18.5	
	Core PAT	14,107	4,223	234.1	12,129	16.3	
Sterlite (Consolidated)	Revenues	56,542	45,789	23.5	72,278	(21.8)	Earnings to be impacted by Q-o-Q fall in zinc-lead prices and 20% Q-o-Q decline in copper production due to a 20-day shutdown.
	EBITDA	15,101	10,209	47.9	21,855	(30.9)	
	Core PAT	11,110	6,727	65.2	13,811	(19.6)	
Tata Steel (Standalone)	Revenues	60,853	56,156	8.4	71,017	(14.3)	Extent of low-cost coking coal remaining to offset the higher current coking coal contracts. Inventory build-up likely. Sale of shares in associate companies might boost other income. Any updates on the Dhamra port.
	EBITDA	22,908	17,422	31.5	28,930	(20.8)	
	Core PAT	11,762	7,898	48.9	21,623	(45.6)	
Usha Martin (Consolidated)	Revenues	7,363	6,151	19.7	6,530	12.8	Asssumed saleable volumes at 120 kt and blended realisations of INR 61,200/t. No benefit of tax write backs
	EBITDA	1,719	1,091	57.6	1,398	23.0	
	Core PAT	666	320	108.1	693	(3.9)	

Valuation snapshot

	Reco	Mkt Cap USD mn	Price (INR)	PAT growth (%, Y-o-Y) FY11E	FY12E	P/E FY11E	FY12E	P/B FY11E	FY12E	RoE FY11E	FY12E	Div yld FY11E	FY12E
Bhushan Steel	Buy	1,287	1,416	35.5	26.4	5.9	4.7	1.5	1.1	31.2	29.4	0.4	0.5
Hindalco	Buy	5,886	144	(16.9)	11.4	8.5	7.5	1.1	1.0	13.6	13.5	0.7	0.7
Hindustan Zinc	Buy	8,505	941	50.9	2.3	6.5	6.4	1.7	1.3	29.1	23.3	0.6	0.6
Jindal Steel & Power	Hold	12,295	615	3.5	34.5	15.2	11.3	4.3	3.4	31.9	33.2	0.2	0.3
JSW	Buy	4,122	1,030	7.1	69.2	12.0	6.8	1.9	1.6	17.7	25.6	0.9	0.9
Nalco	Reduce	5,919	429	119.6	14.9	15.1	13.2	2.4	2.1	16.8	16.8	1.2	1.2
SAIL	Buy	16,797	190	4.8	10.2	11.1	10.1	2.0	1.7	19.6	18.6	1.7	1.8
Sesa Goa	Buy	6,382	347	88.3	9.1	6.2	5.7	2.3	1.6	41.4	32.1	0.9	0.9
Sterlite	Buy	11,557	161	81.9	17.7	6.6	5.3	1.3	1.0	20.7	21.6	0.6	0.6
Tata Steel	Buy	9,017	475	NM	27.5	8.2	6.5	1.5	1.2	19.2	20.8	2.5	3.4
Usha Martin	Buy	530	81	100.8	35.7	7.3	5.4	1.2	1.0	18.0	20.5	1.2	1.2

Source: Edelweiss research

OIL & GAS

Edelweiss
Ideas create, values protect

Govt support uncertainty continues

July 5, 2010

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Key highlights of the sector during the quarter

Q1FY11 has been a landmark quarter—resolution of RIL-RNRL issue, RIL entering the telecommunications space and announcing petrochemicals capacity additions, power roadmap, and two acquisitions in the shale gas space. Also, on the regulatory front, it was a momentous quarter with the hike in APM price to USD 4.2/mmbtu, freeing of petrol prices, intent to deregulate diesel (currently price hike taken), and higher cooking fuel prices. IGL also increased CNG prices during Q1FY11. WTI crude prices averaged USD 77.2/bbl (down 0.8% Q-o-Q and up 30.8% Y-o-Y) in Q1FY11. INR appreciated slightly with respect to the USD, with the INR/USD average being 45.6 (up 0.7% Q-o-Q and 6.5% Y-o-Y). Indian simple refining margins eased slightly to USD 1.7/bbl (USD 1.9/bbl in Q4FY10). Indian complex margins followed similar trend and eased a bit to USD 8.7/bbl (down 5.2% Q-o-Q). The simple-complex spread was lower at USD 7.1/bbl. While LPG and gasoline cracks were a bit lower, middle distillates cracks like that for HSD and jet fuel improved Q-o-Q. Hence, under-recoveries for the quarter were higher because of a slight increase for HSD and kerosene. In petrochemicals, it was a mixed with slight change in margins Q-o-Q. Ethylene cracker margins cracked.

Result expectations for the sector and stocks under coverage

We estimate Q1FY11 under-recoveries at ~INR 190 bn. We have assumed that upstream companies will share 33.0% of total under-recoveries or INR 63.2 bn and OMCs will bear ~66.7%. We have currently not assumed any GoI sharing. Uncertainty remains on the overall sharing within the sector. Hence, under-recoveries could result in a loss for all OMCs (assuming ~66.7% sharing for OMCs of total under-recoveries) in Q1FY11, leading to unfavorable results for all three OMCs. For IGL, we expect strong sales volumes—~15% for CNG; it recently took a price hike to pass on high APM prices. For GAIL, we assume average transmission volumes of 115 mmscd and subsidy sharing of INR 4.74 bn. For RIL, we expect high refining throughput and GRMs of USD 7.75/bbl. O&G contribution could improve with KG-D6 crude production at 26 kbpd and gas production at 59.5 mmscmd. Overall PAT will be maintained. For ONGC, crude production could improve on Rajasthan block ramp up. Gas sales could marginally improve and net realisation is expected at USD 54.5/bbl. We assume subsidy sharing at INR 52.2 bn. Cairn's overall hydrocarbon production will improve Q-o-Q as Rajasthan production is likely to average ~47-48 kbpd in Q1FY11. Crude realisation will remain flat Q-o-Q; hence, favorable PAT growth for the company. CPCL results could be muted on the refinery capacity shutdown (for debottlenecking) till May 2010. Aban may report lower core earnings Q-o-Q, as Aban Abraham and Deep Venture came off contract and Aban Pearl sank. There could be possible gains on Deep Venture contract cancellation and write-offs on differential between insured claims/recovery and BV of Aban Pearl (one-offs not included in our estimates).

Outlook over the next 12 months

Overall, crude prices could remain range bound over medium term and then gradually inch up. Further clarity may emerge as US demand numbers peak in the summer season. On refining, we continue to have a long-term positive outlook. Potential for further regulatory changes includes clarity on diesel de-regulation and possible sharing or formulae for sector companies and GoI.

Recommendations

Top picks: RIL, GAIL, ONGC

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
Aban Offshore	Revenues	8,909	7,935	12.3	10,210	(12.7)	DD1, DD8 were idle this quarter; Aban Abraham and Deep Venture came off contract. Aban Pearl sank mid quarter. Hence, PAT will be lower Q-o-Q. Possible gains from Deep Venture contract cancellation and write-offs on differential between insurance recovery and BV of Aban Pearl (one-offs not included in our estimates).
	EBITDA	5,568	4,689	18.7	6,592	(15.5)	
	Core PAT	1,658	1,109	49.5	2,801	(40.8)	
BPCL	Revenues	350,527	255,144	37.4	375,703	(6.7)	Expect under-recovery of INR 43.7 bn for BPCL (gross). We assume overall sharing by upstream at 33.3%. Company to report loss on same. Expect lower throughput. Indian simple GRMs in Q1FY11 averaged USD 1.65/bbl.
	EBITDA	(18,878)	7,670	(346.1)	11,466	(264.6)	
	Core PAT	(12,783)	6,141	(308.1)	7,032	(281.8)	
Cairn India	Revenues	13,112	2,050	539.8	6,928	89.3	Rajasthan production to average ~47-48kbpd in Q4FY11. Crude realisation to remain flat Q-o-Q. Hence, favourable PAT growth.
	EBITDA	6,743	1,321	410.4	3,678	83.3	
	Core PAT	4,447	454	878.8	2,452	81.4	
CPCL	Revenues	67,553	56,604	19.3	54,653	23.6	CPCL to report poor results, as its throughput to be impacted by maintianence shutdown till May 2010.
	EBITDA	1,096	4,677	(76.6)	(568)	292.9	
	Core PAT	222	3,047	(92.7)	(611)	136.3	
Essar oil	Revenues	106,433	65,970	61.3	104,820	1.5	Results will be muted
	EBITDA	4,955	6,580	(24.7)	6,180	(19.8)	
	Core PAT	45	1,690	(97.4)	1,800	(97.5)	
GAIL India	Revenues	68,897	60,214	14.4	65,221	5.6	Assume subsidy sharing of INR 4.74 bn. Transmission volumes at 114.8 mmscmd. Petrochemical may be impacted by lower margins on some products.
	EBITDA	10,743	10,655	0.8	13,168	(18.4)	
	Core PAT	7,081	6,558	8.0	9,108	(22.3)	
HPCL	Revenues	275,673	244,362	12.8	315,584	(12.6)	Expect under-recovery of INR 41.6 bn for HPCL (gross). We assume overall sharing by upstream at 33.3%. Company to report loss on the same. Indian simple GRMs in Q1FY11 averaged USD 1.65/bbl.
	EBITDA	(14,885)	13,262	(212.2)	15,510	(196.0)	
	Core PAT	(11,782)	6,491	(281.5)	7,575	(255.5)	
IGL	Revenues	3,088	2,326	32.8	2,878	7.3	Continue to expect strong sales volumes, ~15% for CNG. Company recently took a price hike to pass on high APM prices.
	EBITDA	962	849	13.3	925	4.1	
	Core PAT	530	483	9.7	515	2.9	
IOCL	Revenues	693,348	591,796	17.2	785,770	(11.8)	Expect under-recovery of INR 104.6 bn for IOCL (gross). We assume overall sharing by upstream at 33.3%. Company to report loss on the same. Indian simple GRMs in Q1FY11 averaged USD 1.65/bbl.
	EBITDA	(31,466)	49,990	(162.9)	86,457	(136.4)	
	Core PAT	(19,072)	36,828	(151.8)	55,568	(134.3)	
ONGC	Revenues	147,759	148,793	(0.7)	147,133	0.4	Crude production to improve on Rajasthan block ramp up. Gas sales to marginally improve. Net realisation of USD 54.5/bbl. Subsidy assumption at INR 52.2 bn. Also, other expenses may normalise.
	EBITDA	90,112	95,010	(5.2)	81,290	10.9	
	Core PAT	46,458	48,479	(4.2)	37,764	23.0	
RIL	Revenues	568,858	311,870	82.4	575,700	(1.2)	Expect high refining throughput and GRMs of USD 7.75/bbl. O&G contribution to improve. KG-D6 crude production at 26 kbpd and gas production at 59.5 mmscmd. Overall PAT to be maintianed.
	EBITDA	93,203	63,840	46.0	91,360	2.0	
	Core PAT	47,271	36,660	28.9	47,100	0.4	
Shiv-Vani Oil	Revenues	3,294	2,812	17.1	2,994	10.0	~10% top-line growth Q-o-Q. However, expect EBITDA margins at ~44-45%. Seismic order execution may be slower in the quarter.
	EBITDA	1,453	1,173	23.8	1,515	(4.1)	
	Core PAT	415	421	(1.3)	470	(11.6)	

Valuation snapshot

	Reco	Mkt Cap USD mn	Price (INR)	PAT growth (%, Y-o-Y) FY11E	FY12E	P/E FY11E	P/E FY12E	P/B FY11E	P/B FY12E	RoE FY11E	RoE FY12E	Div yld FY11E	Div yld FY12E
Aban Offshore	Hold	776	834	20.5	11.7	5.8	5.2	1.6	1.3	30.8	27.9	0.4	0.4
Cairn India	Hold	12,013	296	NM	92.6	12.9	6.7	1.5	1.2	12.2	19.9	0.0	0.0
CPCL	Hold	837	263	(19.7)	30.9	8.1	6.2	1.1	1.0	13.8	16.9	3.7	4.9
Essar oil	Buy	4,103	140	NM	89.4	19.1	10.1	9.5	7.7	21.7	31.9	0.4	0.7
GAIL India	Buy	12,535	462	0.2	24.5	17.8	14.3	2.6	2.3	17.5	19.4	1.7	1.9
IGL	Buy	850	284	5.3	13.4	9.6	9.3	2.2	1.9	25.8	22.5	2.7	2.9
ONGC	Hold	59,787	1,306	47.8	2.8	10.6	10.2	2.3	2.0	24.0	21.4	2.7	2.8
RIL	Buy	74,812	1,069	48.0	27.8	14.9	10.9	1.5	1.4	8.9	10.8	1.5	2.2
Shiv-Vani Oil & Gas Exploration Service	Buy	439	443	38.4	1.4	14.7	12.0	1.2	1.2	8.0	10.1	1.9	2.4
BPCL	Reduce	5,158	667	(2.2)	36.2	5.7	5.1	1.4	1.2	31.0	28.0	0.4	0.4
HPCL	Reduce	3,443	475	(26.9)	22.7	17.7	15.6	4.2	3.6	25.6	24.7	1.7	1.9
IOCL	Reduce	20,849	401	(17.5)	20.1	15.1	11.8	2.2	1.9	15.5	17.0	0.7	0.8

Source: Edelweiss research

PHARMACEUTICALS

Core earnings growth to remain robust

Edelweiss
Ideas create, values protect

July 5, 2010

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Key highlights of the sector during the quarter

Revenue growth is likely to remain stable with positive bias from strong growth in domestic formulations and continued growth in base US formulations business. Some companies may, however, face challenges from Europe, with negative impact from decline in the EUR/INR. Other ROW markets are likely to continue to show double–digit growth, and Russia is expected to stabilise. Margin outlook remains stable for most companies, while some companies could benefit from lower fixed costs coming off a higher base due to restructuring charges and write-offs incurred in Q1FY10.

Result expectations for the sector and stocks under coverage

We expect most companies under our coverage to post strong earnings growth (except Cipla). Dr. Reddy's (DRRD) is likely to report marginal decline in sales and margins, despite high base effect of exclusivity sales in Q1FY10, as strong growth in domestic formulations and contribution from GSK deal to Mexico and Brazil offset decline in US generics. DRRD's core margins are likely to benefit from lower fixed costs coming off a high base due to betapharm write-offs in Q1FY10 last year. Lupin (LPC) is expected to show strong growth in US branded formulations, positively impacted by low base of Antara sales last quarter, while margin are expected to remain stable over last quarter (Q4FY10). Sun Pharma's (SUNP) domestic formulations will be a critical growth driver, positively impacted by low base effect of Q1FY10 domestic sales, while Caraco could benefit from generic eloxatin. Aurobindo pharma (ARBP) will see increased ramp up in Pfizer sales in Europe, and Torrent Pharma (TRP) will benefit from high growth in branded generics business of India and Brazil. We have maintained neutrality on forex gains/losses.

Outlook over the next 12 months

We expect robust outlook for the next year. The domestic formulations business is expected to deliver healthy double-digit growth with increasing consolidation of market shares and expansion into Tier-II markets, while the US formulation business will continue to offer niche opportunities to large Indian players. ROW markets are expected to grow sharply. CRAM-based companies, which were affected by de-stocking and credit issues with some of their partners, are likely to post revenue growth as the overall global growth outlook improves. The sales ramp-up from strategic partnerships with innovators will be critical for companies that have entered into such deal. Forex trends will play an important role in the sector, given the large contribution of exports to overall revenues. An appreciating EUR/ INR could have a negative operational impact for companies with substantial exposure to Europe. MTM loss/gain on forex should be treated as non-recurring in our view and, hence, we do not factor in such impact on companies in our universe. We also expect companies to continue to focus on deleveraging balance sheets and capex to moderate from FY12.

Recommendations

Top picks: Lupin, Torrent, Aurobindo Pharma

Stocks to avoid: Cipla

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
Aurobindo	Revenues	9,611	8,097	18.7	9,011	6.7	Pfizer ramp-up and strong base business growth in Europe and ROW markets. Milestone income low form high base in Q1FY10. EBITDA margins (excl. milestones) expected to remain stable. No forex impact assumed in our estimates.
	EBITDA	1,810	1,526	18.6	1,479	22.4	
	Core PAT	1,156	1,089	6.2	932	24.0	
Cipla	Revenues	14,808	13,504	9.7	13,611	8.8	Revenue growth to be stable with tech income of INR 335 mn, higher than Q1FY10. Margins to remain stable sequentially. No forex impact assumed in our estimates.
	EBITDA	3,418	3,428	(0.3)	2,644	29.3	
	Core PAT	2,808	2,687	4.5	2,005	40.0	
Dr Reddy's	Revenues	18,016	18,189	(1.0)	16,424	9.7	Lower fixed costs to positively impact margins. PAT to improve q-o-q from high margins and low tax rate. US generics to be impacted from base effect of sumatriptan sales in Q1FY10. Strong growth in domestic business and recovery in Russia (28% y-o-y) to offset decline in US generics. No forex impact assumed in our estimates.
	EBITDA	3,092	3,295	(6.2)	2,114	46.3	
	Core PAT	2,515	2,529	(0.6)	1,711	47.0	
Lupin	Revenues	13,810	11,005	25.5	13,282	4.0	Strong growth in revenues and profit. US branded formulations to be positively impacted from low base effect due to antara sales this quarter. Expect margins to remain stable Q-o-Q. No forex impact assumed in our estimates.
	EBITDA	2,834	2,091	35.5	2,924	(3.1)	
	Core PAT	1,966	1,451	35.5	2,251	(12.7)	
Piramal Healthcare Ltd	Revenues	9,626	8,215	17.2	9,418	2.2	Revenue growth for ex-domestic formulation business at 14% Y-o-Y, aided by strong recovery in CRAMs from India assets offsetting marginal decline in outside Indian assets and ramp up in GCC. Operating margins to improve Y-o-Y. No forex impact assumed in our estimates.
	EBITDA	1,953	1,557	25.4	2,163	(9.7)	
	Core PAT	1,234	806	53.1	1,560	(20.9)	
Sun Pharma	Revenues	10,567	7,876	34.2	11,092	(4.7)	Expect strong revenue growth from sharp increase in domestic formulations. Caraco sales to see positive impact from full quarter eloxatin sales. Higher margins Y-o-Y due to exclusivity sales and recovery in domestic business. No forex impact assumed in our estimates.
	EBITDA	3,578	1,689	111.8	4,185	(14.5)	
	Core PAT	3,607	2,042	76.6	3,945	(8.6)	
Torrent Pharmaceuticals	Revenues	5,271	4,658	13.2	4,484	17.6	Domestic and Brazil expected to ramp up significantly. Heumann and Europe to be challenging due to volitality in EUR/INR rate. PBT margins to be stable. No forex impact assumed in our estimates.
	EBITDA	1,084	963	12.6	969	11.9	
	Core PAT	715	151	373.5	645	10.9	

Valuation snapshot

		Mkt Cap	Price (INR)	PAT growth (%, Y-o-Y)		P/E		P/B		RoE		Div yld	
	Reco	USD mn		FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E
Aurobindo	Buy	1,109	918	26.4	12.0	9.2	7.3	2.3	1.9	31.9	29.0	0.7	0.6
Cipla	Reduce	5,787	337	7.0	9.0	23.1	21.2	4.0	3.5	18.7	17.8	1.0	1.1
Dr Reddy's	Hold	5,189	1,436	NM	16.7	25.8	20.9	4.6	3.8	23.9	23.0	0.7	0.8
Lupin	Buy	3,679	1,932	22.7	17.2	21.0	17.9	5.6	4.5	29.7	28.0	1.0	1.1
Piramal Healthcare	Buy	2,187	489	22.4	27.2	17.9	14.1	5.0	4.0	30.7	31.2	1.3	1.7
Sun Pharma	Hold	7,739	1,756	42.5	12.2	23.9	21.3	3.8	3.3	17.3	16.8	0.8	0.8
Torrent Pharma	Buy	1,016	561	24.4	25.0	15.8	12.6	4.4	3.5	31.6	30.8	1.1	1.4

Source: Edelweiss research

PIPES

Tepid quarter

July 5, 2010

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Key highlights of the sector during the quarter

- Raw material prices (HR coil /plates and billets) continued to rise through Q1FY11. The INR appreciated slightly with respect to the USD, with the INR/USD average at 45.6 (up 0.7% Q-o-Q and 6.5% Y-o-Y). It may partly limit the INR income of companies whose export orders and margins are USD denominated.
- While, Welspun Gujarat has been continuously announcing new order accretion of smaller ticket sizes, order momentum for other players like Jindal Saw and PSL has been tepid in the quarter.
- While companies are focusing on getting new orders, international order announcements have been lower in Q1FY11. Domestic pipe orders have also been slower than expected. This may make the domestic environment quite competitive.

Result expectations for the sector and stocks under coverage

Results of pipe companies will continue to be mixed. While we expect Welspun Gujarat to report better sales volumes on US capacity ramp-up and higher new orders, its margins are likely to be maintained. Jindal Saw's earnings, as expected, are likely to dip in Q1FY11, as EBITDA margins normalise to ~USD 225/MT from earlier benefits of high margin seamless orders and favorable sales mix. Over the past few quarters, PSL has reported coating income. We expect the trend to continue. However, production volumes in the domestic capacity may remain flat, with improvements in US sales. Margins for the company will continue to remain competitive.

Outlook over the next 12 months

Our long term crude price outlook is positive, which is one of the catalysts for spending on pipeline infrastructure. However, while only some new international orders have been coming through, overall momentum has slowed slightly. We expect some lumpiness in new orders for a quarter, after which things may revive again. The large TransCanada order, in which Welspun Gujarat is a contender, seems to be moving forward with government approval. Pipe orders are likely by H2CY10. On the domestic front, GAIL orders have been slower than expected. However, over a 1-2 years' horizon, GAIL expects significant capacity expansion. Domestic margins are expected to remain competitive.

Recommendations

Top Picks: Welspun Gujarat

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
Jindal Saw	Revenues	10,355	15,002	(31.0)	10,863	(4.7)	Sales at 210 KMT and blended margins to ease to USD 223/MT, as seamless and other favourable SAW pipe margins normalise. Hence, PAT will be lower Q-o-Q.
	EBITDA	2,171	2,381	(8.8)	2,880	(24.6)	
	Core PAT	1,198	1,360	(11.9)	1,803	(33.5)	
PSL	Revenues	5,604	6,166	(9.1)	8,183	(31.5)	Expect ~INR 1.5-2.0 bn of coating revenues. Domestic sales volumes are likely at ~72 kMT. Margins will be competitive.
	EBITDA	520	638	(18.5)	530	(1.8)	
	Core PAT	140	226	(38.0)	238	(41.2)	
Welspun Gujarat	Revenues	13,049	18,798	(30.6)	14,006	(6.8)	Expect production of ~180 kMT and slightly higher plate volumes. We continue to expect pipes EBITDA at INR 11k/MT. PAT to almost be maintained.
	EBITDA	2,589	3,030	(14.5)	2,554	1.4	
	Core PAT	1,309	1,382	(5.3)	1,341	(2.3)	

Valuation snapshot

		Mkt Cap	Price (INR)	PAT growth (%, Y-o-Y)		P/E		P/B		RoE		Div yld	
	Reco	USD mn		FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E
Jindal Saw	Hold	1,167	198	(28.3)	8.6	10.7	9.9	1.3	1.1	13.4	12.2	0.7	0.7
PSL	Buy	144	126	2.4	(0.1)	5.4	5.4	0.7	0.6	13.2	12.4	4.0	4.0
Welspun Gujarat	Buy	1,000	229	10.3	14.5	7.8	6.8	1.3	1.1	19.8	18.2	0.9	1.1

Source: Edelweiss research

POWER

Business as usual

July 5, 2010

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Key highlights of the sector during the quarter

Returns for pure-play utilities are expected to be flat due to nominal increase in capacity. EPC margins are likely to remain stable. Sharp jump in passenger traffic and sustained growth in cargo tonnage at airports with revival in the economic environment are expected to boost non- aero revenues, but earnings would be lower due to higher capex related expenses.

Result expectations for the sector and stocks under coverage

Marginal growth is expected from pure-play utilities such as NTPC, Power Grid, Tata Power, and CESC. EPC margins and order book accretion along with higher other income will be key aspects to watch out for in Reliance Infrastructure. Merchant sales could boost profits of Lanco Infratech. Adani Enterprises may sustain earnings growth due to commercialisation of the second 330 MW unit by its power subsidiary. However, stay on merchant sales of power and delay in implementation of the regulated regime for airports is likely to impact earnings of GMR and GVK.

Outlook over the next 12 months

Fund raising: Following NTPC's FPO, Power Grid is expected to tap the market in Q2/Q3FY11 aggregating ~ INR 35 bn. This should boost earnings and aid higher equity funding share for its INR 550 bn capex programme.

Capacity commissioning: Timely commissioning of power projects will be a key to watch out for. Delay in commissioning could hurt earnings of NTPC and Lanco Infratech. Availability of fuel (both coal and gas) is also key to sustain earnings.

Expansion of EPC business: With rise in pace of capacity addition we expect order books of Reliance Infrastructure and Lanco Infratech to increase. We also expect greater stability in their margins due to wider portfolio of projects.

Passenger traffic at airports: Passenger traffic is likely to pick up in the backdrop of improving economic conditions. Commonwealth Games in 2010 will also aid traffic growth at the Delhi airport.

Appointment of airport regulator: Earlier the airport regulator (AERA) was expected to permit return on capital employed-based model to determine airport charges from FY11. However, based on the draft paper soliciting views on regulations, it seems the terms of agreement entered with developers could be renegotiated.

Recommendations

Top picks: Tata Power, CESC and Reliance Infrastructure

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
Adani Enterprises	Revenues	86,124	63,862	34.9	78,257	10.1	Merchant revenues and high PLFs from the first 2 units of 330 MW each from the power subsidiary. Sustaining higher margins from the trading business.
	EBITDA	7,664	2,869	167.1	5,154	48.7	
	Core PAT	3,219	1,277	152.1	3,398	(5.3)	
CESC	Revenues	8,588	8,200	4.7	7,700	11.5	Budge-Budge addition of 250 MW will enhance earnings.
	EBITDA	2,432	2,010	21.0	2,000	21.6	
	Core PAT	1,192	1,050	13.5	1,000	19.2	
GMR Infrastructure	Revenues	15,179	11,775	28.9	11,250	34.9	Due to delayed commissioning of the barge mounted plant, we expect GMR to report lower earnings . With airport regulations yet to be enforced, lower aero earnings will be depressed as bulk of the capex has been incurred in Delhi airport.
	EBITDA	4,289	3,213	33.5	3,146	36.3	
	Core PAT	(12)	225	(105.3)	731	(101.6)	
GVK Power and Infra	Revenues	4,911	3,322	47.8	4,886	0.5	Reduction in road capex will enhance earnings and also aided by higher non-aero income in Mumbai airport. Delay in implementing the airport regulations is expected to impact aero revenues.
	EBITDA	1,641	944	73.8	737	122.6	
	Core PAT	697	327	113.2	431	61.7	
Lanco Infratech	Revenues	35,065	21,954	59.7	24,160	45.1	Merchant revenues from Kondapalli unit II and Amarkantak units 1 & 2. EPC margins. Financial closure of the pipeline projects aggregating ~3 GW.
	EBITDA	9,072	2,769	227.6	6,731	34.8	
	Core PAT	2,899	1,159	150.2	1,133	155.9	
NTPC	Revenues	131,124	125,280	4.7	127,315	3.0	Limited capacity addtion while PLF remains at 90% plus levels.
	EBITDA	40,436	37,010	9.3	30,439	32.8	
	Core PAT	22,388	21,936	2.1	20,177	11.0	
Power Grid	Revenues	23,106	16,230	42.4	22,305	3.6	Limited commissioning of projects.
	EBITDA	19,565	13,299	47.1	18,205	7.5	
	Core PAT	5,281	4,953	6.6	5,915	(10.7)	
Reliance Infra.	Revenues	33,488	24,463	36.9	26,439	26.7	EPC margins to be low since projects being implemented are in initial stages; power business will be stagnant.
	EBITDA	4,176	2,995	39.4	2,714	53.9	
	Core PAT	3,707	3,516	5.4	3,171	16.9	
Tata Power	Revenues	19,260	20,156	(4.4)	17,951	7.3	Flat numbers as sales mix of merchant and regulated power remains unchanged.
	EBITDA	4,216	6,323	(33.3)	4,491	(6.1)	
	Core PAT	1,981	1,874	5.7	2,042	(3.0)	
PTC	Revenues	27,326	23,725	15.2	12,435	119.8	Higher volumes of power traded, while margins will be relatively flat. Other income may also fall because of more funds being diverted towards coal mine acquisition and equity commitments.
	EBITDA	182	156	16.7	95	91.6	
	Core PAT	232	334	(30.5)	135	71.9	

Valuation snapshot

		Mkt Cap	Price (INR)	PAT growth (%, Y-o-Y)		P/E		P/B		RoE		Div yld	
	Reco	USD mn		FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E
Adani Enterprises	Hold	6,268	537	79.5	83.1	21.6	12.1	3.4	2.6	17.7	24.5	0.2	0.3
CESC	Buy	1,076	377	8.0	(1.0)	10.1	10.2	1.1	1.0	11.3	10.1	1.2	1.2
GMR Infrastructure	Hold	5,038	60	72.0	90.8	66.0	94.0	2.7	2.7	4.6	2.9	0.0	0.0
GVK Power and Infra	Hold	1,503	44	34.1	23.6	21.8	16.2	2.0	1.8	9.6	11.5	0.0	0.0
Lanco Infratech	Hold	3,598	66	72.0	41.0	16.2	11.5	3.6	2.7	22.2	23.9	0.0	0.0
NTPC	Hold	37,479	200	15.7	11.2	16.4	14.7	2.4	2.2	14.7	14.7	1.8	1.8
Power Grid	Reduce	9,757	102	13.0	12.0	17.5	15.7	2.4	2.1	13.7	13.7	1.4	1.6
PTC	Buy	662	99	16.0	(4.0)	31.4	32.7	1.4	1.3	4.3	4.1	1.3	1.2
Reliance Infra.	Buy	6,272	1,190	1.3	4.6	19.4	18.6	2.0	1.9	10.4	10.0	0.9	0.9
Tata Power	Buy	7,039	1,304	(13.0)	2.0	38.5	37.6	3.3	3.1	8.5	8.2	0.7	0.7

Source: Edelweiss research

REAL ESTATE

Edelweiss
Ideas create, values protect

Recovery continues

July 5, 2010

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This quarter marked the return of speculators into the property market, specifically in Gurgaon and pockets of Mumbai, even as overall volumes in Mumbai continued to soften. Prices are stable Q-o-Q and robust Y-o-Y; those in NCR were ~15% below peak levels and above peak in Mumbai. Prices in Bengaluru have appreciated ~5%.

Result expectations for the sector and stocks under coverage

Anant Raj: The company has launched its residential project at Kapashera, which will lead to significant contribution to revenue in Q1FY11. We expect rental income of ~INR 180 mn during the quarter as Grand-Papillon hotel earns rental income for an entire quarter. Anant Raj could post revenue and net profit of INR 823 mn and INR 408 mn, respectively, with EBIDTA margin of 77%.

DLF: DLF has done a soft launch for its entire project at Chennai. Besides, it has not launched any other project. Key things to watch out for are pre-leasing of commercial space and asset monetisation. We expect DLF to post revenue and net profit of INR 18.0 bn and INR 4.1 bn, respectively, with EBIDTA margin of 42%.

Orbit: It did not have any new launches. Consequently, transaction volumes are expected to be lower, and revenues could be driven by execution volumes. The company had guided for a soft launch of Mandwa project in Q1FY11 and the response to the same will be a key monitorable. We expect Orbit's revenue and net profit for the quarter to be at INR 984 mn and INR 226 mn, respectively.

Sobha Developers: We estimate a marginal slowdown in sales volumes Q-o-Q, largely due to lack of newer launches. We expect the company to post revenue and net profit of INR 3.3 bn and INR 0.5 bn, respectively, with EBIDTA margin of 25%. Any asset monetization will provide upsides to our estimates.

Unitech: Margins could remain suppressed due to revenue booking from older projects facing cost overruns. Revenue is pegged at 7.9 bn and PAT at INR 1.6 bn. The key monitorable for the company is debt reduction.

Parsvnath Developers: Revenues and profits are expected to remain flat Q-o-Q. Key monitorables are ongoing asset moneitsation and debt reduction.

Mahindra Lifespaces: Revenues are expected to be broadly in line with those reported in Q4FY10 as run-rates in construction and volume are steady. Revenues from *Aura* are yet to kick in, while, for *Splendor,* they began to come in the previous quarter. Hence, revenues might be lower than reported in Q4FY10.

Outlook over the next 12 months

As expected, we note the return of NRI investors and speculators into property markets. Also, construction activity has picked up and developers are receiving robust milestone payments on achieving construction milestones. With a robust economy and jobs market, we expect prices to remain robust and underlying demand steady (quarterly variations notwithstanding). We expect developers' cash flow to continue to improve, while lower inventory levels will keep prices robust and new launches well received.

Recommendations

Top picks: DLF, Anant Raj and Orbit Corporation

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
Anant Raj Industries	Revenues	823	825	(0.2)	341	141.3	The company has launched its residential project at Kapashera, which will lead to significant contribution to revenue in Q1FY11. Other key monitorables are the leasing status of Manesar IT Park and Kirti Nagar mall.
	EBITDA	635	760	(16.5)	262	142.3	
	Core PAT	408	689	(40.9)	309	31.9	
DLF	Revenues	18,003	16,499	9.1	19,944	(9.7)	DLF has done a soft launch for its entire project at chennai. Besides, it has not launched any other project. Key things to watch out for DLF will be pre-leasing of commercial spaces and asset monetisation.
	EBITDA	7,561	7,441	1.6	10,000	(24.4)	
	Core PAT	4,051	3,960	2.3	4,264	(5.0)	
Orbit Corporation	Revenues	984	1,103	(10.8)	865	13.8	Orbit Corporation has not launched any project during the quarter; consequently, revenue booking can be sluggish. The key monitorables are debtors position and approval status for Mandwa project.
	EBITDA	472	474	(0.4)	412	14.6	
	Core PAT	226	180	25.7	200	13.2	
Parsvnath Developers	Revenues	3,515	1,153	204.9	3,585	(2.0)	Revenues and profits are expected to remain flat Q-o-Q. Key monitorables are asset moneitsation and debt reduction.
	EBITDA	857	431	98.8	874	(2.0)	
	Core PAT	375	138	171.7	347	8.1	
Sobha Developers	Revenues	3,274	1,771	84.9	4,008	(18.3)	Further land monetisation in Q1FY11 is an upside risk to our estimates. Further, Sobha's ability to sustain a quarterly run-rate of ~0.5 msf of new sales will be a key factor to watch out.
	EBITDA	819	423	93.5	965	(15.2)	
	Core PAT	491	127	286.7	557	(11.8)	
Unitech	Revenues	7,890	5,149	53.2	11,581	(31.9)	Margins will continue to remain suppressed on account of revenue booking from older projects, which are facing cost overruns. Key monitraoble is debt reduction.
	EBITDA	2,231	3,151	(29.2)	2,981	(25.2)	
	Core PAT	1,588	1,578	0.6	1,657	(4.2)	
Mahindra Lifespaces	Revenues	1,030	473	117.9	1,010	2.0	Revenues are expected to be broadly in line with those reported in Q4FY10 as run-rates for construction and volume are steady. Aura is yet to kick in, while Splendor began previous quarter. Consequently, revenues might be lower than those reported in Q4FY10.
	EBITDA	280	104	169.7	296	(5.5)	
	Core PAT	230	104	120.7	237	(2.9)	

Valuation snapshot

		Mkt Cap	Price (INR)	PAT growth (%, Y-o-Y)		P/E		P/B		RoE		Div yld	
	Reco	USD mn		FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E
Anant Raj Industries	Buy	748	118	33.1	33.1	13.5	13.5	0.9	0.9	7.6	7.6	0.0	0.0
DLF	Buy	10,255	282	11.4	53.2	18.4	12.0	1.6	1.5	9.1	12.6	0.6	0.7
Mahindra Lifespaces	Buy	399	458	64.0	72.5	15.9	9.5	1.7	1.4	11.2	16.4	0.8	0.8
Orbit Corporation	Buy	298	131	32.8	114.9	8.4	3.8	1.4	1.0	18.5	30.6	1.0	2.1
Parsvnath Developers	Buy	520	122	76.9	77.2	10.0	5.6	1.0	0.8	10.1	15.9	1.2	1.6
Sobha developers	Hold	604	288	110.0	19.7	8.2	6.9	1.3	1.1	17.6	17.7	0.0	0.0
Unitech	Buy	3,785	73	12.2	63.5	18.1	11.0	1.5	1.4	9.7	14.0	0.0	0.0

Source: Edelweiss research

RETAIL

Edelweiss
Ideas create, values protect

Robust Urban demand driving profitability

July 5, 2010

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Key highlights of the sector during the quarter

Q1FY11 saw the continuation of urban consumer demand momentum seen in earlier quarters. Premiumisation trend is evident as consumers become more brand conscious and are willing to increase their discretionary spending. Following this, higher same store sales were seen in both value and lifestyle retailing. Pantaloon Retail raised INR 4 bn by issuing 10 mn convertible warrants to its promoter group entity on a preferential basis. Shopper's Stop increased it's stake in Hypercity to 51% while planning to put the airport retailing (JV with Nuance Group) plans on the back burner considering the slow offtake in the business. Titan Industries is planning to set up a lens-making plant in Bangalore with an initial investment of INR 120 million and is also planning to invest about INR 1 bn for opening 50 premium watch outlets *Helios* in next five years. Rentals, salaries, and store renovation costs have dipped and this has helped retailers. Rentals remained soft though service tax on rentals (introduced in FY11 Union Budget) is a negative for the sector. Store expansion plans will help increase revenues and profitability in the longer term.

Result expectations for the sector and stocks under coverage

We expect revenue growth to benefit from better same store sales growth in Q1FY11. Pantaloon Retail's (PRIL) revenue is expected to grow robustly, largely driven by value retailing. However, interest costs will impact earnings. We expect Titan Industries' revenues to grow as gold volumes picked up during the quarter despite higher gold prices. Demand on *Akshay Tritiya* (auspicious day to buy gold) in May was good and company is seeing good demand following higher number of days in summer wedding season. Rebound in urban consumer demand will also help Shoppers Stop's (SSL) and Koutons Retail (KRIL) as higher same store sales will drive profitability in the quarter.

Outlook over the next 12 months

We believe momentum of urban demand is going to continue in FY11 on back of overall buoyancy in the economy. With better liquidity for developers, improving consumer sentiments, and consolidation of retailers, we believe the next few quarters will continue to see strong profit growth for retailers. Also, cost savings from cheaper inputs, soft rentals, lower salary levels, cheaper procurement and higher share of private labels will help improve margins. Increase in tax rate on rentals will be slightly negative for the sector. We continue to maintain our positive stance on the retail sector.

Recommendations

Top picks: Shoppers Stop, Pantaloon Retail and Titan Industries

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
Koutons Retail	Revenues	2,300	2,013	14.2	3,854	(40.3)	We expect sales and profit momentum to continue. Due to recent re-financing of high-cost debt, we expect interest costs to start trending down. Some inventory reduction is also expected.
	EBITDA	550	478	15.0	742	(25.9)	
	Core PAT	138	115	20.0	327	(57.8)	
Pantaloon Retail	Revenues	20,784	16,627	25.0	20,576	1.0	Expected to be strong as urban demand is back on track. Due to strong internal accruals and recent QIP, we expect interest costs to start trending down.
	EBITDA	2,150	1,832	17.3	2,156	(0.3)	
	Core PAT	530	365	45.3	559	(5.2)	
Shoppers Stop	Revenues	3,884	2,988	30.0	4,057	(4.3)	SSS is expected to be strong as urban demand is back on track. Margins will be strong on back of low-cost structure; profit growth will be strong, following lower base last year.
	EBITDA	147	113	30.0	166	(11.4)	
	Core PAT	100	9	1,024.7	126	(20.6)	
Titan	Revenues	12,361	8,829	40.0	13,110	(5.7)	Jewellery sales will be good, despite increase in gold prices. Expect to hear more on expansion plans in watches segments.
	EBITDA	1,151	794	45.0	1,001	15.0	
	Core PAT	644	460	40.0	753	(14.5)	

Valuation snapshot

		Mkt Cap	Price (INR)	PAT growth (%, Y-o-Y)		P/E		P/B		RoE		Div yld	
	Reco	USD mn		FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E
Koutons Retail	Buy	208	319	20.4	19.1	9.7	8.1	1.6	1.3	18.0	17.9	0.5	0.5
Pantaloon Retail	Buy	1,803	419	50.8	38.5	25.7	18.6	2.5	2.2	10.2	12.6	0.1	0.1
Shoppers Stop	Buy	410	549	61.2	38.6	33.1	23.9	5.7	4.6	18.6	21.4	0.2	0.2
Titan	Buy	2,206	2,323	20.8	28.9	30.8	23.9	9.6	7.0	36.1	34.0	0.4	0.4

Source: Edelweiss research

TELECOM

Muted quarter

July 5, 2010

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Key highlights of the sector during the quarter

We expect healthy industry wireless adds of ~50 mn in Q1FY11, though adds are ~16% lower Q-o-Q from record high of ~59 mn in Q4FY10. From our recent interactions with all operators, we understand that focus is shifting from subscriber additions to revenue market share and profitability as further investments in business are being capped. Among the key operators, we expect BSNL, Tata Docomo (TD), Idea and Aircel to report a sequential decline in their net adds this quarter. Among new entrants, net adds for both Uninor and Stel continue to taper off; in May 2010, Uninor even reported an M-o-M decline in its wireless subscriber base. We believe that the decline in industry adds is partially on account of gradual decline in multiple-SIMs as tariffs plans gradually equalize across operators (though there were no major tariff cuts in the past two quarters). Multiple-SIMs, in the last couple of quarters, were estimated at ~20% of incremental wireless subscribers as per industry sources.

Result expectations for the sector and stocks under coverage

We expect healthy traction in overall traffic growth in the range of 5-12% for the listed telecos. While there were no material tariff cuts during the quarter, blended tariffs are likely to continue to decline (albeit at a lower pace) with increasing adoption of cheaper schemes by the existing subscriber base. We estimate blended RPM at INR 0.45 for BHARTI and Idea (down 4% Q-o-Q), and that for RCOM at ~INR 0.44 (flat Q-o-Q). We expect ~3-8% growth in revenues for the listed telecos, led by healthy growth in minutes. ARPUs are, however, expected to continue to trend downwards (1.5-3% Q-o-Q decline) led by lower tariffs. For integrated operators (BHARTI and RCOM), we expect 80-100bps improvement in consolidated EBITDA margin, primarily led by margin expansion in non-mobility businesses. We understand that the interest cost on debt raised for 3G and BWA license payments will be capitalised until commercial operations are launched. For BHARTI, interest cost will rise due to debt raised for the acquisition of Zain. For Idea, after excluding the impact of one-offs in Q4FY10 and including 100% consolidation of Spice Telecom (versus 41.09% in FY10), we expect EBITDA margin to remain flat Q-o-Q. For Tulip Telecom (TTSL), revenues/EBITDA are expected to decline Q-o-Q, given seasonal nature of the business (for NI and partially for IP VPN). Higher contribution from the fibre business poses an upside risk to our quarterly estimates.

Outlook over the next 12 months

We remain cautious on the sector owing to high competitive intensity that leads to revenue and margin pressures and regulatory concerns, which could materially increase business costs for operators. Besides core business concerns, balance sheets for most leading telecos are stretched following the 3G & BWA auction cash outflow. We believe telecom stocks are likely to continue to underperform the broader market owing to core business pressures, though possible monetisation of tower assets poses an upside risk to valuations (particularly in light of the recent deal valuations between Reliance Infratel and GTL), especially Idea.

Recommendations

Top picks: Bharti Airtel

Stocks to avoid: MTNL

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
BHARTI	Revenues	103,732	99,416	4.3	100,557	3.2	Continued decline in RPM, though, slower than earlier quarter, as circle-level lower tariff schemes continue. Demand elasticity expected to play-out, as reflected in higher MOUs. EBITDA margin to be impacted by one-time costs associated with Zain acquisition. Interest cost to rise due to debt assumed for Zain.
	EBITDA	40,222	41,518	(3.1)	38,222	5.2	
	Core PAT	19,458	25,167	(22.7)	20,551	(5.3)	
Idea	Revenues	36,144	29,759	21.5	33,478	8.0	RPM, MOU to remain stable. Consolidation of Spice for quarter to lead to higher revenue growth. Operating losses in new circles increased in previous quarter due to tariff declines, but expected to be lower due to stable tariffs and higher traffic growth. EBITDA margins were higher in previous quarter due to certain one-off items.
	EBITDA	9,229	8,599	7.3	9,236	(0.1)	
	Core PAT	1,969	2,971	(33.7)	2,666	(26.1)	
RCOM	Revenues	52,859	61,452	(14.0)	50,928	3.8	RPM expected to remain stable with MOU decline continuing. EBITDA magin likely to expand due to improvement in global and broadband businesses on the back of a significant decline in the previous quarter. Forex losses in the quarter to impact net profit.
	EBITDA	17,169	24,525	(30.0)	16,020	7.2	
	Core PAT	5,501	16,366	(66.4)	12,210	(54.9)	
TTSL	Revenues	5,135	4,429	15.9	5,303	(3.2)	NI and IP VPN segments impacted by seasonality; hence, Q1 revenue/EBITDA will be lower sequentially.
	EBITDA	1,373	1,086	26.4	1,545	(11.1)	
	Core PAT	644	655	(1.7)	795	(19.0)	

Valuation snapshot

	Reco	Mkt Cap USD mn	Price (INR)	PAT growth (%, Y-o-Y)		P/E		P/B		RoE		Div yld	
				FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E
BHARTI	Buy	21,510	265	(13.7)	10.0	12.8	11.6	2.1	1.8	17.8	16.7	0.4	0.4
IDEA	Hold	4,096	58	(42.5)	26.0	38.3	30.4	1.6	1.5	4.3	5.2	0.0	0.0
RCOM	Hold	8,429	191	(25.3)	7.2	12.7	11.9	0.9	0.8	6.5	6.6	0.5	0.5
TTSL	Buy	556	896	2.4	15.7	9.7	8.4	2.4	2.0	24.7	23.3	0.4	0.4

Source: Edelweiss research

Miscellaneous

Stock		Q1FY11E (INR mn)	Q1FY10 (INR mn)	Y-o-Y (%)	Q4FY10 (INR mn)	Q-o-Q (%)	Key highlights and things to watch out for
Jain Irrigation	Revenues	7,315	5,730	27.6	9,586	(23.7)	Performance of domestic MIS business; Q-o-Q Improvement in operating margins; Betterment in the onion dehydration division
	EBITDA	1,609	1,261	27.6	1,981	(18.8)	
	Core PAT	578	351	64.9	834	(30.7)	
Shree Renuka Sugars	Revenues	15,902	8,935	78.0	17,814	(10.7)	Pricing outlook of sugar; Production outlook of sugar in SS11; Operational details of Equipav
	EBITDA	1,931	1,557	24.0	3,545	(45.5)	
	Core PAT	1,109	776	42.9	2,247	(50.6)	
United Phosphorus	Revenues	14,499	16,377	(11.5)	15,160	(4.4)	Revenues to decline by ~10% Y-o-Y due to very high base of Q1FY10 (revenue growth of 25% Y-o-Y in FY11). Europe (28% of sales) is expected to be challenging due to decline in EUR/INR. EBITDA margins to remain stable. No forex impact assumed in our estimates.
	EBITDA	2,716	3,070	(11.5)	3,498	(22.4)	
	Core PAT	1,531	1,763	(13.2)	1,870	(18.1)	
Lakshmi Energy and Foods	Revenues	2,800	1,785	56.8	2,413	16.0	Offtake of FCI rice and sale of Pusa rice; operating margin to be stable Q-o-Q.
	EBITDA	588	563	4.4	500	17.6	
	Core PAT	244	258	(5.1)	230	6.3	
Deepak fertilisers	Revenues	3,028	2,424	24.9	3,238	(6.5)	Higher capacity utilisation for fertilisers; steady capacity utilisation for chemicals.
	EBITDA	696	578	20.5	803	(13.2)	
	Core PAT	403	391	3.1	445	(9.5)	
Opto Circuits India	Revenues	3,450	2,304	49.8	3,345	3.1	Growth in the non-invasive segment will be the key trend to watch out for, given its tepid performance last quarter.
	EBITDA	1,156	770	50.0	1,110	4.2	
	Core PAT	863	593	45.6	701	23.1	
Sintex Industries	Revenues	8,076	6,624	21.9	10,936	(26.1)	Q1 no.s are not comparable sequentally on account of strong revenue booking, particulalry in the monolithic segment last quarter. Y-o-Y, we expect healthy growth metrics.
	EBITDA	1,153	874	31.9	1,932	(40.3)	
	Core PAT	740	606	22.1	1,387	(46.7)	
Sterlite Technologies	Revenues	5,294	4,362	21.4	6,624	(20.1)	With slower order flows from Power Grid, we expect contribution from high-margin telecom segment to increase, thus improving the overall margin for the quarter.
	EBITDA	797	777	2.6	1,101	(27.6)	
	Core PAT	501	455	10.1	722	(30.6)	
TCI	Revenues	3,820	3,113	22.7	4,021	(5.0)	Topline degrowth Q-o-Q due to seasonality; however, PAT margins likely to be higher due to lower tax rate.
	EBITDA	310	225	37.8	324	(4.3)	
	Core PAT	130	92	42.0	125	3.6	

Valuation snapshot

		Mkt Cap	Price (INR)	PAT growth (%, Y-o-Y)		P/E		P/B		RoE		Div yld	
	Reco	USD mn		FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E
Deepak fertilisers	Buy	281	149	11.0	31.8	8.4	6.4	1.3	1.1	15.8	18.4	3.0	3.4
Jain Irrigation	Buy	1,767	1,083	66.2	26.6	23.7	18.6	5.6	4.4	26.6	26.7	0.4	0.5
Lakshmi Energy and Foods	Buy	135	100	(42.7)	9.5	6.9	6.3	1.1	1.0	17.8	16.6	0.5	0.5
Opto Circuits India	Buy	925	236	37.8	18.4	12.2	10.3	3.2	2.6	29.2	27.8	2.3	2.7
Shree Renuka Sugars	Buy	985	69	(38.4)	0.0	10.0	0.0	1.7	0.0	17.9	0.0	1.5	0.0
Sintex Industries	Hold	921	315	13.6	22.8	11.4	9.3	1.8	1.5	17.4	17.8	0.0	0.0
Sterlite Technologies	Buy	863	113	38.2	0.0	19.0	0.0	3.0	0.0	23.8	0.0	0.3	0.0
TCI	Buy	189	122	19.6	10.4	16.7	15.2	2.6	2.3	16.0	15.9	0.3	0.3
United Phosphorus	Buy	1,712	182	33.5	19.6	12.0	10.1	2.0	1.8	19.6	18.9	0.9	1.0

Source: Edelweiss research

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