

SEPTEMBER 18, 2009

UPDATE

 Sector view: **Cautious**

 Price (Rs): **869**

 Target price (Rs): **915**

 BSE-30: **16,711**

Highlights from Systech management meeting. Systech's cost rationalization measures place it well for good earnings upside from improvement in European CV volumes. Domestic volumes have doubled since the March quarter and European markets are expected to show sequential improvements within this month. Systech should be a key beneficiary of the growing trend of component sourcing from lower-cost countries, given its existing relationships with global OEMs

Company data and valuation summary

Mahindra & Mahindra

Stock data		Forecasts/Valuations			
		2009	2010E	2011E	
52-week range (Rs) (high,low)	944-235	EPS (Rs)	28.7	51.1	53.3
Market Cap. (Rs bn)	253.5	EPS growth (%)	(23.3)	78.1	4.2
Shareholding pattern (%)		P/E (X)	30.3	17.0	16.3
Promoters	29.0	Sales (Rs bn)	130.9	159.6	172.3
FIs	28.6	Net profits (Rs bn)	8.3	14.9	15.5
MFs	3.8	EBITDA (Rs bn)	10.9	22.5	23.6
Price performance (%)		EV/EBITDA (X)	25.5	12.4	11.6
Absolute	1M 3M 12M	ROE (%)	17.4	23.8	19.4
Rel. to BSE-30	1.7 (0.1) 26.0	Div. Yield (%)	1.1	1.1	1.1

Mahindra's Systech operations poised to benefit from rebound

Cost reduction actions taken over the past year to reduce Systech's breakeven level has placed the company well to take advantage of any rebound in European commercial vehicle production. Systech's management indicated that it is seeing some signs of a rebound in order intake and we could see production levels increase 20% from current levels. Systech has cut its workforce by more than a third, leading to a 45% reduction in personnel expenses. Other fixed costs have been cut by 40%. These expense reduction measures have lowered the breakeven levels significantly and should help the company see good upside in profits as volumes improve. Systech's domestic operations are also seeing a strong rebound with current production levels twice as much as those of the March quarter.

Systech should emerge stronger coming out of this downturn

As a survivor, Systech should be better positioned to gain new business from distressed competitors. For instance, Systech has got additional content under Daimler's newer generation Altros truck. Additionally, the need to cut costs at the OEM level in Europe has resulted in increased enquiries for sourcing components from India. The landed cost for components is 15% cheaper than for those made in Europe. Systech is in advance talks with Renault to supply crankshafts by leveraging the existing JV of parent Mahindra with Renault. Management sees multiple opportunities in the CV space as well with Mahindra Navistar and Daimler. Daimler currently makes up 20% of revenues at Systech's European subsidiaries and this existing relationship should help win domestic orders for Indian operations.

Shareholder value enhancement is a focus area

Systech management is focused in creating shareholder value and has set a goal of achieving €80 - 90 mn in EBITDA, with €60 mn coming from Europe and the rest from India. Management believes this is achievable even at 30% below peak levels. Separately, advanced talks are on with a private equity investor and a strategic investor, both of which are interested in taking a stake at Systech.

Jairam Nathan CFA
 jairam.nathan@kotak.com
 Mumbai: +91-22-6634-1327

Amit Agarwal
 agarwal.amit@kotak.com
 Mumbai: +91-22-6634-1390

M&M, SOTP-based valuation, FY2011E basis

	EPS (Rs/share)	Multiple (X)	Value per share (Rs)	Comment
M&M stand-alone business	51	13.0	660	Based on 13X FY2010E EPS less dividend income/share from subs
Subsidiaries			256	
Tech Mahindra			125	Based on KIE current price of Rs850/share
Mahindra Lifespace Developers Ltd			17	Based on KIE target price of Rs410/share
M&M Financial Services Ltd			38	Based on KIE target price of Rs240/share
Other investments			75	Based on current price of Mahindra Holidays, Forgings
SOTP-based value			915	
Target price			915	

Note

(1) The subsidiaries have been valued at a holding company discount of 20%.

Source: Kotak Institutional Equities

M&M, Profit model, balance sheet and cash flow model, March fiscal year-ends, 2006-2011E (Rs mn)

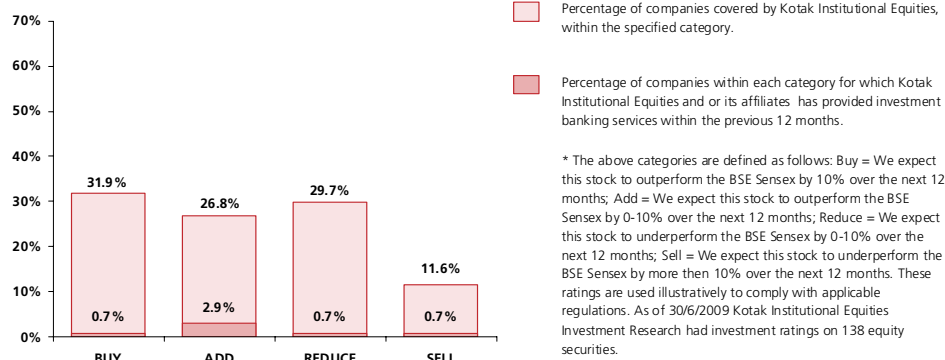
	2006	2007	2008	2009E	2010E	2011E
Profit model (Rs mn)						
Net sales	82,513	100,682	115,413	130,937	159,625	172,315
EBITDA	9,958	13,048	13,666	10,926	22,491	23,615
Other income	753	1,530	1,304	2,703	1,914	2,189
Interest	184	675	(242)	(453)	(682)	(807)
Depreciation	(2,000)	(2,096)	(2,387)	(2,915)	(3,849)	(4,286)
Profit before tax	8,895	13,157	12,340	10,262	19,875	20,711
Current tax	(2,854)	(3,657)	(2,788)	(585)	(2,981)	(3,107)
Deferred tax	430	157	(247)	(1,412)	(1,988)	(2,071)
Net profit	8,571	10,684	11,034	8,368	14,906	15,533
Earnings per share (Rs)	34.8	43.0	44.4	28.7	51.1	53.3
Balance sheet (Rs mn)						
Equity	30,556	35,727	44,068	52,621	73,033	87,337
Total Borrowings	8,834	16,360	25,871	40,528	42,578	45,078
Current liabilities	20,516	26,656	32,400	47,978	44,318	46,819
Total liabilities	59,906	78,743	102,339	141,126	159,928	179,234
Net fixed assets	15,544	18,712	23,609	32,143	44,295	56,008
Investments	16,691	22,375	42,151	57,864	56,853	51,853
Cash	7,303	13,261	8,612	15,744	16,519	25,729
Other current assets	20,188	24,221	27,831	35,249	42,135	45,518
Miscellaneous expenditure	181	176	135	126	126	126
Total assets	59,906	78,743	102,339	141,126	159,928	179,234
Free cash flow (Rs mn)						
Operating cash flow excl. working capital	6,919	9,712	10,730	10,395	19,510	20,509
Working capital changes	(50)	1,978	(2,472)	5,918	(10,729)	(881)
Capital expenditure	(2,747)	(4,819)	(7,171)	(9,152)	(16,000)	(16,000)
Free cash flow	4,122	6,870	1,087	7,161	(7,219)	3,627
Ratios						
Operating margin (%)	12.1	13.0	11.8	8.3	14.1	13.7
PAT margin (%)	10.4	10.6	9.6	6.4	9.3	9.0
Debt/equity (X)	0.3	0.5	0.6	0.8	0.6	0.5
Net debt/equity (X)	0.1	0.0	0.0	(0.1)	(0.1)	(0.1)
Book Value (Rs/share)	123.3	142.9	176.6	180.0	250.0	299.0
RoAE (%)	32.9	32.4	27.8	17.4	23.8	19.4
RoACE (%)	23.6	22.4	18.4	10.7	14.8	13.0

Source: Company, Kotak Institutional Equities estimates

"I, Jairam Nathan, hereby certify that all of the views expressed in this report accurately reflect my personal views about the subject company or companies and its or their securities. I also certify that no part of my compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this report."

Kotak Institutional Equities Research coverage universe

Distribution of ratings/investment banking relationships



Source: Kotak Institutional Equities

As of June 30, 2009

Ratings and other definitions/identifiers

Definitions of ratings

BUY. We expect this stock to outperform the BSE Sensex by 10% over the next 12 months.

ADD. We expect this stock to outperform the BSE Sensex by 0-10% over the next 12 months.

REDUCE. We expect this stock to underperform the BSE Sensex by 0-10% over the next 12 months.

SELL. We expect this stock to underperform the BSE Sensex by more than 10% over the next 12 months.

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

Other definitions

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

Other ratings/identifiers

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

CS = Coverage Suspended. Kotak Securities has suspended coverage of this company.

NC = Not Covered. Kotak Securities does not cover this company.

RS = Rating Suspended. Kotak Securities Research has suspended the investment rating and price target, if any, for this stock, because there is not a sufficient fundamental basis for determining an investment rating or target. The previous investment rating and price target, if any, are no longer in effect for this stock and should not be relied upon.

NA = Not Available or Not Applicable. The information is not available for display or is not applicable.

NM = Not Meaningful. The information is not meaningful and is therefore excluded.

Corporate Office

Kotak Securities Ltd.
Bakhtawar, 1st Floor
229, Nariman Point
Mumbai 400 021, India
Tel: +91-22-6634-1100

Overseas Offices

Kotak Mahindra (UK) Ltd
6th Floor, Portsoken House
155-157 The Minories
London EC 3N 1 LS
Tel: +44-20-7977-6900 / 6940

Kotak Mahindra Inc
50 Main Street, Suite No.310
Westchester Financial Centre
White Plains, New York 10606
Tel:+1-914-997-6120

Copyright 2009 Kotak Institutional Equities (Kotak Securities Limited). All rights reserved.

Kotak Securities Limited and its affiliates are a full-service, integrated investment banking, investment management, brokerage and financing group. We along with our affiliates are leading underwriter of securities and participants in virtually all securities trading markets in India. We and our affiliates have investment banking and other business relationships with a significant percentage of the companies covered by our Investment Research Department. Our research professionals provide important input into our investment banking and other business selection processes. Investors should assume that Kotak Securities Limited and/or its affiliates are seeking or will seek investment banking or other business from the company or companies that are the subject of this material and that the research professionals who were involved in preparing this material may participate in the solicitation of such business. Our research professionals are paid in part based on the profitability of Kotak Securities Limited, which include earnings from investment banking and other business. Kotak Securities Limited generally prohibits its analysts, persons reporting to analysts, and members of their households from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover. Additionally, Kotak Securities Limited generally prohibits its analysts and persons reporting to analysts from serving as an officer, director, or advisory board member of any companies that the analysts cover. Our salespeople, traders, and other professionals may provide oral or written market commentary or trading strategies to our clients that reflect opinions that are contrary to the opinions expressed herein, and our proprietary trading and investing businesses may make investment decisions that are inconsistent with the recommendations expressed herein. In reviewing these materials, you should be aware that any or all of the foregoing, among other things, may give rise to real or potential conflicts of interest. Additionally, other important information regarding our relationships with the company or companies that are the subject of this material is provided herein.

This material should not be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. We are not soliciting any action based on this material. It is for the general information of clients of Kotak Securities Limited. It does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients. Before acting on any advice or recommendation in this material, clients should consider whether it is suitable for their particular circumstances and, if necessary, seek professional advice. The price and value of the investments referred to in this material and the income from them may go down as well as up, and investors may realize losses on any investments. Past performance is not a guide for future performance, future returns are not guaranteed and a loss of original capital may occur. Kotak Securities Limited does not provide tax advice to its clients, and all investors are strongly advised to consult with their tax advisers regarding any potential investment.

Certain transactions -including those involving futures, options, and other derivatives as well as non-investment-grade securities - give rise to substantial risk and are not suitable for all investors. The material is based on information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied on as such. Opinions expressed are our current opinions as of the date appearing on this material only. We endeavor to update on a reasonable basis the information discussed in this material, but regulatory, compliance, or other reasons may prevent us from doing so. We and our affiliates, officers, directors, and employees, including persons involved in the preparation or issuance of this material, may from time to time have "long" or "short" positions in, act as principal in, and buy or sell the securities or derivatives thereof of companies mentioned herein. For the purpose of calculating whether Kotak Securities Limited and its affiliates holds beneficially owns or controls, including the right to vote for directors, 1% of more of the equity shares of the subject issuer of a research report, the holdings does not include accounts managed by Kotak Mahindra Mutual Fund. Kotak Securities Limited and its non US affiliates may, to the extent permissible under applicable laws, have acted on or used this research to the extent that it relates to non US issuers, prior to or immediately following its publication. Foreign currency denominated securities are subject to fluctuations in exchange rates that could have an adverse effect on the value or price of or income derived from the investment. In addition, investors in securities such as ADRs, the value of which are influenced by foreign currencies affectively assume currency risk. In addition options involve risks and are not suitable for all investors. Please ensure that you have read and understood the current derivatives risk disclosure document before entering into any derivative transactions.

This report has not been prepared by Kotak Mahindra Inc. (KMInc). However KMInc has reviewed the report and, in so far as it includes current or historical information, it is believed to be reliable, although its accuracy and completeness cannot be guaranteed. Any reference to Kotak Securities Limited shall also be deemed to mean and include Kotak Mahindra Inc.