

April 29, 2008

GITANJALI GEMS LIMITED (GITANJALI)

CMP: Rs278; STRONG BUY

Eyeing value creation

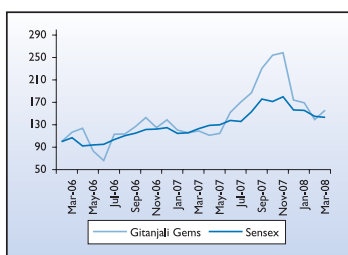
**Initiating Coverage
Target Price: Rs455 (Sep'09)**

Bloomberg Code	GITG IN
Reuters Code	GTGM.BO
BSE	532715
Sensex	17,016
52-week H/L (Rs)	480/177
Monthly H/L (Rs)	291/212
6 Mth Avg Vol	403,957
Shares O/s (MM)	85.1
MCap (Rs MM)	23,647
MCap (US\$ MM)	584
EV (Rs MM)	25,395

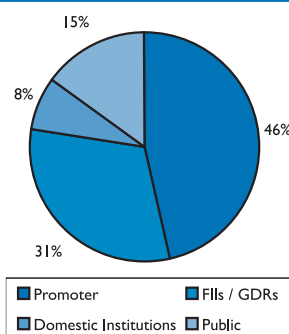
Valuation Parameters (FY09)

EV/EBITDA (x)	8.0
Mkt Cap/EBITDA (x)	8.2
EV/Sales (x)	0.5
Mkt cap/Sales (x)	0.5

Price Chart



Shareholding Pattern



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INVESTMENT RATIONALE

World class scale in diamond jewelry manufacturing...

Over FY02-07, Gitanjali has established world class scale in diamond & jewelry mfg., clocking 28% revenue CAGR & 36% PAT CAGR. Gitanjali's broad product range, strong brand equity & significant retail presence along with sightholder status & strong network have enabled it a strong hold in domestic & international markets. **We expect diamond mfg. share in revenues to shrink to 41% in FY10E (FY07: 68%) as high margin jewelry business picks up pace.**

...Time to leverage this scale to improve margins

Management focus now is on leveraging this scale advantage to move up the value chain. To this end, Gitanjali has identified the following growth engines:

Jewelry retail: 1,400 outlets at present; to expand to 3,000 outlets in 3 yrs, to leverage on strong brand equity to improve margins. EBITDA margins for jewelry retailing are 10-12% vs. 4-5% for diamond mfg.

US foray: Company's adoption of inorganic route to establish its footprint in the world's largest jewelry market of the US, by acquiring *Samuels & Rogers* will add ~US\$200 MM revenues to top line in FY10E. The company will avail of value chain benefits accruing out of increased sourcing from India, leading to margin expansion. **We believe jewelry & international businesses to contribute 59% revenues & 77% EBITDA in FY10E vs. 32% & 53% in FY07, with overall margins rising from 4.8% in FY07 to 6.9% in FY10E.**

Hyderabad SEZ valued at Rs129 per share

This SEZ is one of the few in country which is clear of all regulatory hurdles, and is set to create value in the medium term. We believe our estimates are conservative and once visibility increases, this valuation is slated to improve.

VALUATIONS & OUTLOOK

At CMP of Rs278, Gitanjali's FY09E and FY10E EPS of Rs21.5 & Rs30.2 are discounted at 12.9x and 9.2x. We recommend **STRONG BUY** on Gitanjali with a **price target of Rs455 (64% upside)** based on **12x FY10E EPS, valuing core business at Rs363, plus Rs129 for SEZ less net debt of Rs37.** Gitanjali's strong track record & mgmt. gives us comfort in our estimates.

Year End	Net Sales	EBITDA	EBITDA %	PAT	PAT %	No. of shares (MM)	EPS (Rs)	P/E (x)	EV/EBITDA (x)
FY07(A)	34,674	1,679	4.8%	918	2.6%	59.0	8.6		
FY08(E)	47,400	2,607	5.5%	1,583	3.3%	85.1	14.8	14.9	9.7
FY09(E)	58,050	3,618	6.2%	2,300	4.0%	107.1	21.5	12.9	8.0
FY10(E)	69,465	4,814	6.9%	3,239	4.7%	107.1	30.2	9.2	6.8

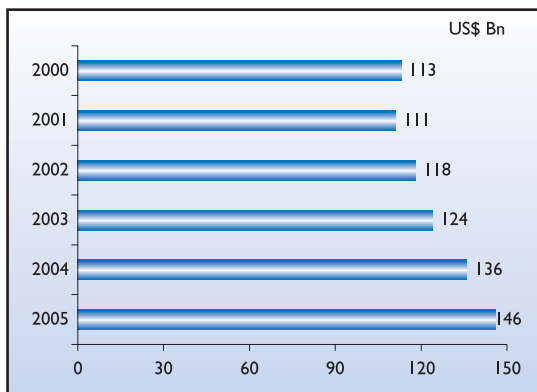
(A) Audited; (E) Estimated; FV = Rs 10

INDUSTRY OVERVIEW

Global Gems & Jewelry Industry

The size of the global gems and jewelry industry is estimated at US\$146 Bn in 2005 (according to a KPMG-GJEPC report 2006), with industry sales growing at 5.2% CAGR over 2000-05.

Global Jewelry Industry Growth

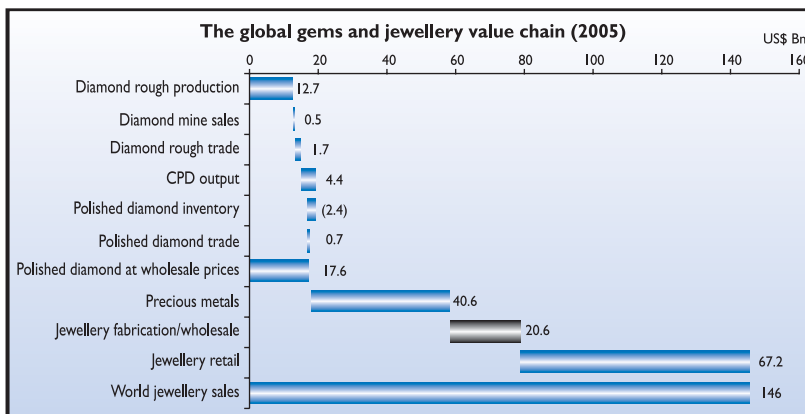


Source: KPMG-GJEPC Report 2006

The global jewelry industry is divided based on the natural or competitive advantage each market has. The mining of gold and diamonds is focused in Australia, South Africa, other African nations and some parts of Russia. India, Turkey and Israel lead in diamond processing. For jewelry fabrication, India and Italy dominate, with China establishing its footprint rapidly. US, India, Europe, Middle East and now China lead in jewelry consumption.

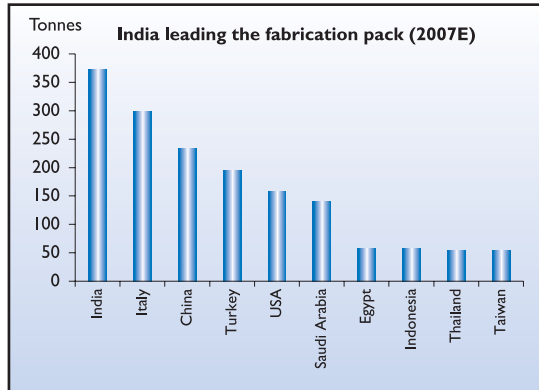
India leads the pack in jewelry fabrication

Jewelry manufacturing and jewelry retailing constitute close to 75% of the jewelry value chain. Value addition continues to be the highest for the players with an integrated presence in the jewelry value chain. Jewelry fabrication forms the third largest pie in the value chain. Over the years, India has emerged as the largest jewelry fabrication centre in the world forming ~16% of the world jewelry fabrication in 2007E, led by the presence of skilled craftsmen, processing skills and historical gold heritage.

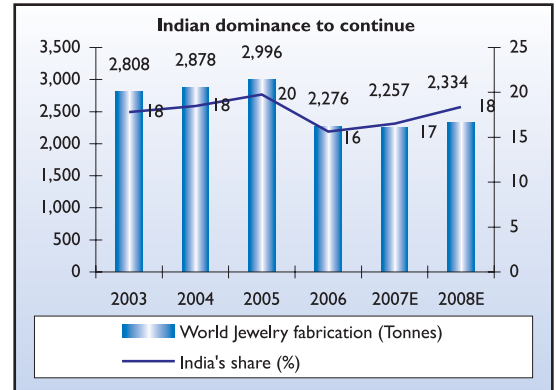


Source: KPMG-GJEPC Report 2006

Going forward, India is expected to maintain its leadership in the fabrication part of the value chain as cost pressures compel fabrication to move to low cost countries like India and China.



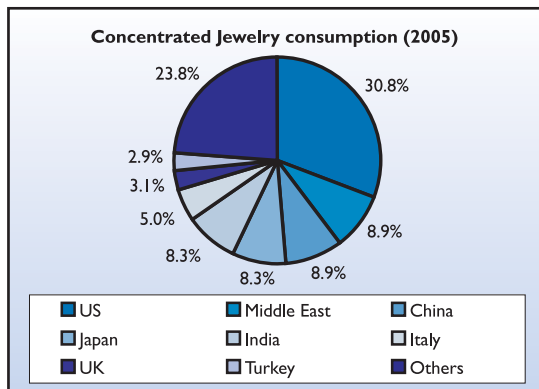
Source: Yellow Book, Dec 2007



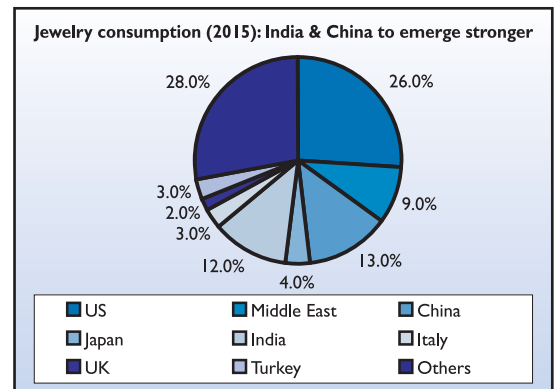
Source: Yellow Book, Dec 2007

Concentrated jewelry consumption: China & India to emerge stronger

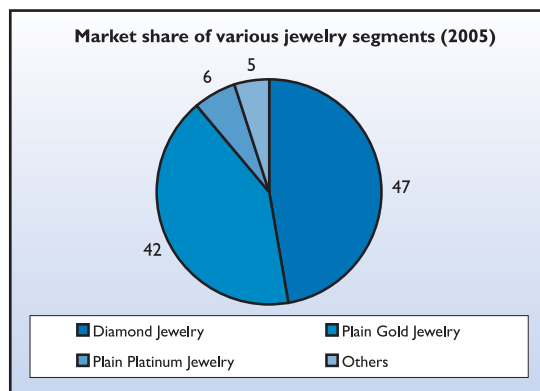
Global jewelry sales is concentrated in 8 key world markets, with US being the largest market with 30.8% share in 2005. India and China are the emerging centres of jewelry consumption and have steadily increased their share in the total pie. Going forward, China and India together are expected to emerge as a market equivalent to the US market by 2015.



Source: KMPG-GJEPC Report 2006



Source: KMPG-GJEPC Report 2006



Source: Company

Diamond-studded jewelry contributes close to 50% of the total gems and jewelry demand, followed by plain gold jewelry with over 40% share. **United States represents over 45% of total worldwide diamond jewelry sales.**

Indian Gems & Jewelry Industry

Gems and jewelry play a significant role in Indian customs and traditions, making this sector integral to the economy and one of the fastest growing industries in the country. It is a leading foreign exchange earner (US\$17.1 Bn in FY07) with >15% share in India's total exports and provides employment to 1.3 MM people directly and indirectly.

Apart from being the world's largest diamond processing (cutting and polishing) centre with an 80% share in world market, India's favorable trade policies have made India the hub for gems and jewelry. Rising disposable incomes and traditional affinity towards precious metals has resulted in 11% CAGR in jewelry consumption over FY02-07.

The industry is predominantly divided into two segments: **Gold jewelry and fabricated studded jewelry (diamonds as well as gemstone studded jewelry)**. Gold jewelry forms 80% of the Indian jewelry market, with the balance comprising fabricated studded jewelry. While a major part of gold jewelry manufactured in India is for domestic consumption, a large portion of fabricated studded jewelry is exported.



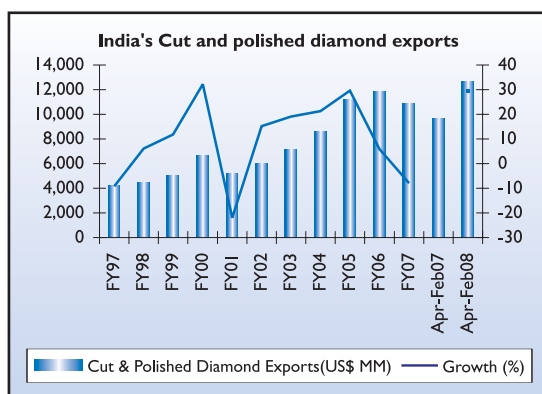
Source: GJEPC

Gold Highlights

- Indian gold market is valued at US\$18 Bn and has been growing at 10% CAGR over the last 5 years.
- Indian gold demand is firmly embedded in cultural and religious traditions. Apart from its historical religious significance, gold is valued as an important savings and investment avenue.
- India consumes nearly 850 tonnes of gold accounting for 25% of the world gold consumption of which nearly 75% goes into making jewelry.
- Cumulative holding in India is estimated at 15,000-16,000

tonnes of gold as against the estimated cumulative holdings of all central banks in the world at 35,000 tonnes.

Diamond Highlights

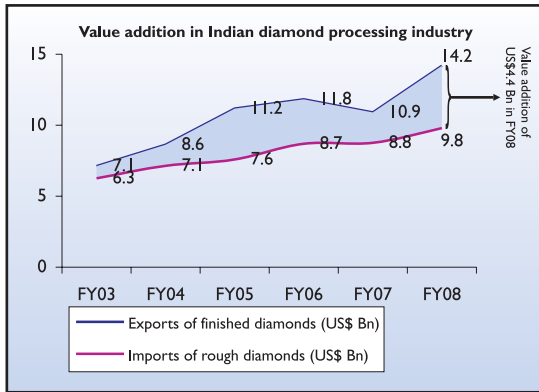


Source: GJEPC

The Indian diamond trade generated over US\$10 Bn per annum in exports in FY07 and its large skilled labour force has been instrumental in catapulting the country as the world's biggest diamond cutting center for small roughs. India, China, Israel and Belgium are the leading countries engaged in the global diamond cutting and polishing industry. India accounts for approximately 60% of the global polished diamonds in value terms, 80% in caratage and 92% in pieces.

In the area of diamonds, Indian jewelers have been focusing on moving up the value chain, from being a polisher of rough diamonds to a manufacturer of jewelry. Exports of diamond

jewelry are expected to increase in the future. The central and various state governments in India have come out with policy incentives to promote jewelry manufacturing. For example, Andhra Pradesh's New Industrial Policy declares gems and jewelry as a thrust area and a package of incentives are being offered for setting up manufacturing park facilities for value addition and export of gems and jewelry.

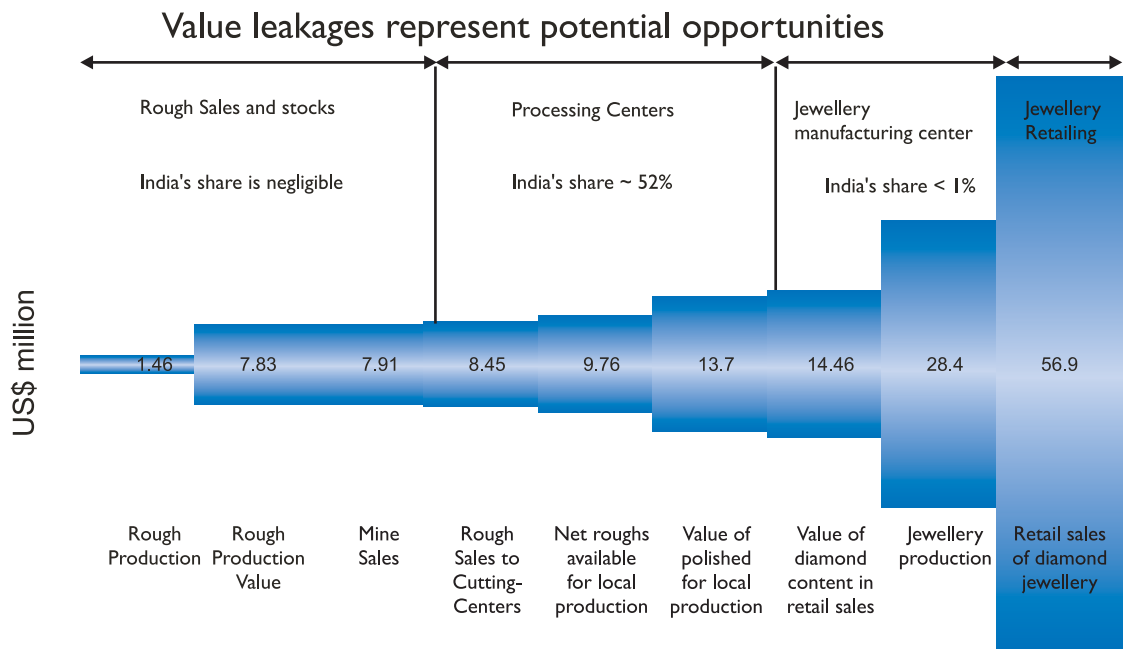


Source: GJEPC

India's significance in the global gems and jewelry industry can be largely attributed to its strength in diamond processing. Value enhancement by the Indian diamond processing industry is the highest among other countries. The value addition in diamonds by Indian industry was worth US\$4.4 Bn in FY08 compared to US\$2.1 Bn in FY07.

The diamond industry pipeline depicted in the figure below indicates the value addition across different stages from rough diamonds to diamond jewelry, and demonstrates how US\$1.46 Bn of rough production is transformed into US\$57 Bn of global diamond jewelry sales annually. India's share in the global

market is highest in diamond processing. **Both value addition and margins increase as the firms move up the value chain, adding to the profits of the companies in the sector. The opportunity for Indian players in the diamond processing segment is to move up the value chain into jewelry manufacturing, where India has a minimal share at present.** Equally, new players can enter the diamond jewelry manufacturing

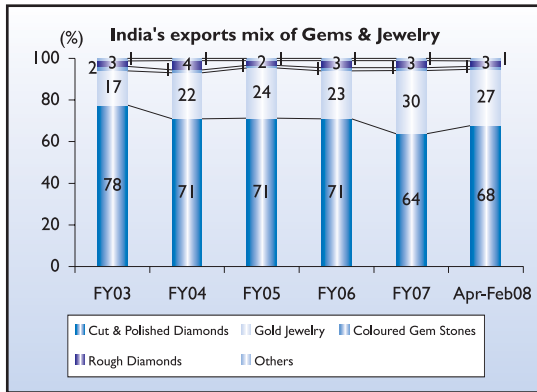


Note: The width of each block represents the value at each stage

Source: KPMG Analysis, International diamond exchange, Tacy Ltd. Chaim Evan – Zohar, IBEF

space, leveraging the diamond processing capabilities that already exist in the country.

Diamonds leading the exports front

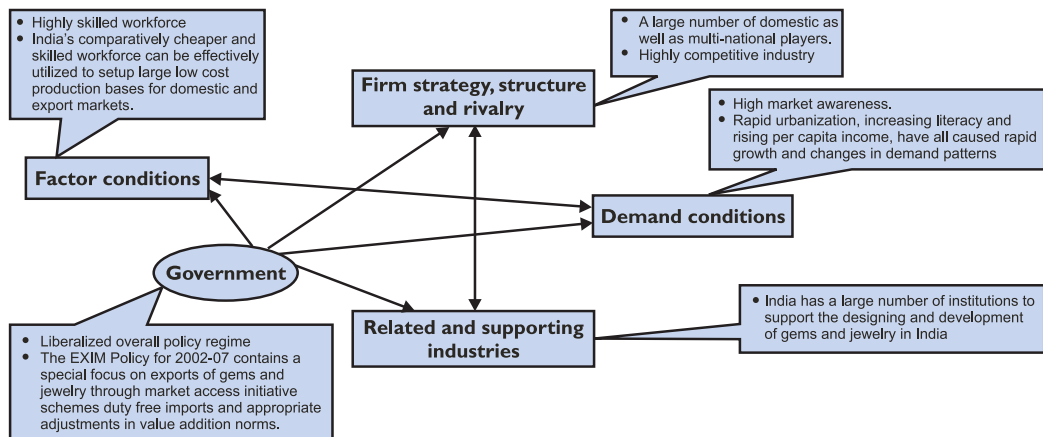


Source: Company, Prime Broking

In terms of exports, diamonds have led the overall gems and jewelry exports over the years. Diamonds accounted for 71% of the total exports, while gold jewelry accounted for 27% during FY08.

India's competitiveness in the gems and jewelry industry can be assessed as follows:

Porter Diamond Analysis Indian Gems & Jewelry Industry



Source: IBEF

Indian Retail Industry Overview

Organized retail in India is on a high growth trajectory and is growing at 24-26% p.a. The size of the total retail industry market is estimated to be ~Rs10 trillion in FY05, with organized retailing accounting for a mere 3.5% of the India's total retail market. As per Vishal Retail's RHP, CRISIL Research has estimated the organized retail penetration to increase to 8% by 2010 at 26% CAGR. The organized retail penetration is projected to increase to 5.8% by FY08. The main drivers for growth in retailing are higher disposable incomes, higher level of working women, increase in nuclear families, favourable demographics, higher growth in urban population and change in outlook on branded products & growth in the number of retail malls.

Retail as a whole can be broken into various categories, depending on the types of products serviced.

Category	Total Retail		Organized Retail		
	Market size	Market share	Market size	Market share	Penetration
	(Rs Bn)	(%)	(Rs Bn)	(%)	(%)
Food, beverage & tobacco	7738	77.4	65	18.6	1
Clothing & textile	716	7.2	141	40.4	20
Consumer durables	416	4.2	43	12.3	10
Jewelleries & watches	416	4.2	25	7.2	6
Home décor & furnishing	300	3.0	25	7.2	8
Beauty care products	214	2.1	7	2.0	3
Footwear	104	1.0	32	9.2	31
Books, music & gifts	87	0.9	11	3.2	13
Total	9991	100	349	100	

Source: Vishal Retail RHP

Indian Retail Jewelry Overview

India is one of the largest jewelry markets, with 96% share being held by the unorganized sector. In the recent past, India has witnessed a strong shift in preference from gold jewelry to diamond jewelry and from unbranded to branded jewelry. **The retail revolution that introduced the Indian middle classes to malls and organized retail has contributed to rising expectations in the gems and jewelry market.** No longer is the 'family jeweler' the accepted norm. Indian consumers are increasingly buying branded and certified jewelry in a contemporary retail setting. There is a growing perception among Indians of jewelry being a fashion accessory rather than an investment avenue. Branded jewelry is therefore positioned as a lifestyle and personality statement. There has also been a shift in consumer preference towards diamond jewelry due to extensive positioning of diamond jewelry as both affordable and contemporary. Another key development in branded jewelry has been the introduction of value added services such as the certification of gold and diamonds, and lifetime return and buy-back schemes.



Source: Company

These trade practices have resulted in the perception of superior quality associated with branded jewelry. The new generation of jewelry purchasers do not have ongoing relationships with local jewelers and prefer to buy branded jewelry. Today the share of branded and organized retail jewelry stands at 4% and there is a vast opportunity for early movers like Gitanjali in this domain.

The share of organized retail jewelry is expected to increase rapidly with organized retail jewelry sales expected to grow at 60% CAGR from US\$350 MM in 2006 to US\$2.28 Bn by 2010. A brief snapshot of how branded jewelry dynamics have changed is shown in the adjacent chart.

We believe that the key elements for development of a successful brand are:

- Brand image
- Aesthetic designs
- Marketing and Promotion
- Distribution network

We believe Gitanjali is well-equipped with its range of successful brands and the management ability to create and nurture brands. The company is well positioned to exploit the huge retail opportunity and will benefit from the increasing shares of organized retail and branded sales. In percentage terms, the retail sector is the point of maximum value addition and increasing the proportion of retail sales will dramatically increase the company's profitability.

US Retail Jewelry Market

US is the world's largest jewelry consumer with ~31% share in world gems and jewelry sales and 45% share in the global diamond jewelry sales. Total US jewelry sales, including watches and fashion jewelry, are estimated by the US Department of Commerce to have been US\$63.1 Bn in 2006 (2005: US\$58.9 Bn). The US jewelry market has grown at 5.7% CAGR over the last 25 years and in 2006 grew by 7.1%. The US retail jewelry industry is highly fragmented. The broader total US retail jewelry market includes formats such as department stores, discount outlets, television home shopping, internet retailers and general merchandise, apparel and accessory stores.

Diamond jewelry sales

Diamond jewelry accounts for ~55% of total jewelry sales in the US market (*Source: Diamond Information Centre*). About 50% of worldwide diamond jewelry sales are made in the US according to the International Diamond Exchange. During the last ten years diamond jewelry sales have grown at 6.4% CAGR compared to 4.5% for the total jewelry market.

China's emergence as an important market

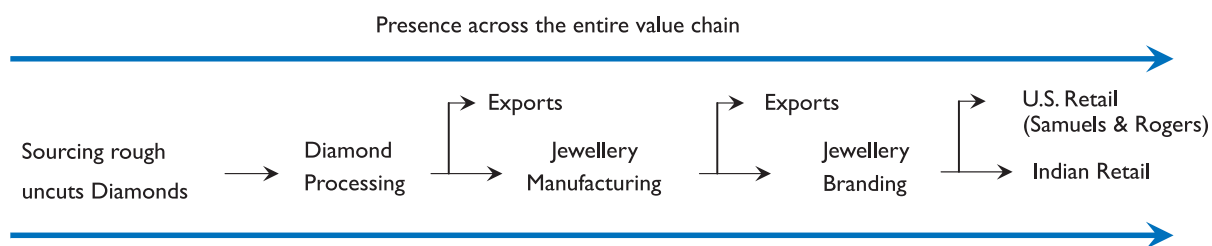
China through Hong Kong has emerged as the largest importer of cut and polished diamonds from India with a share of 35% of total exports, while the US and United Arab Emirates accounted for 24% and 13%, respectively. The share of Hong Kong and US in India's overall gem and jewelry exports was at 26% each, while United Arab Emirates accounted for 21% (*Source: news article*).

PRIME BROKING

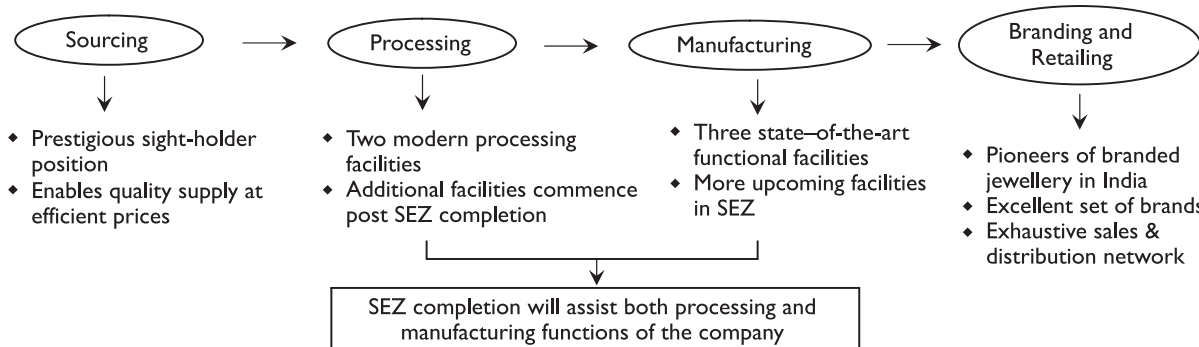
PRIME

COMPANY OVERVIEW

Gitanjali Gems is an integrated diamond and jewelry manufacturing company and one of the largest manufacturers and retailers of diamonds and jewelry in India. The company's operations include sourcing of rough diamonds from primary and secondary source suppliers in the international market, cutting and polishing the rough diamonds for export to international markets and the manufacture and sale of diamond and other jewelry through its retail operations in India as well as in international markets.



Its operations are extensive and cover every step in the end to end process



Source: Company

Gitanjali procures ~25% of its rough diamonds requirements at competitive prices from DTC, the rough diamond marketing arm of De Beers S.A., through Digico Holdings Limited, one of the promoter group companies that enjoys a "sightholder" status with DTC. The company has, either directly or through promoter group companies, enjoyed sightholder status with DTC for more than three decades. It sources remaining rough diamond requirements from secondary source suppliers in the international market. The company exports cut and polished diamonds and diamond and other jewelry products to various international markets in Europe including to Antwerp and Italy, the United States, the Middle East as well as to several diamond and jewelry markets in Asia including Japan, China, Hong Kong and Thailand. It also sells branded diamond and other jewelry products in India through its nationwide sales and distribution network.

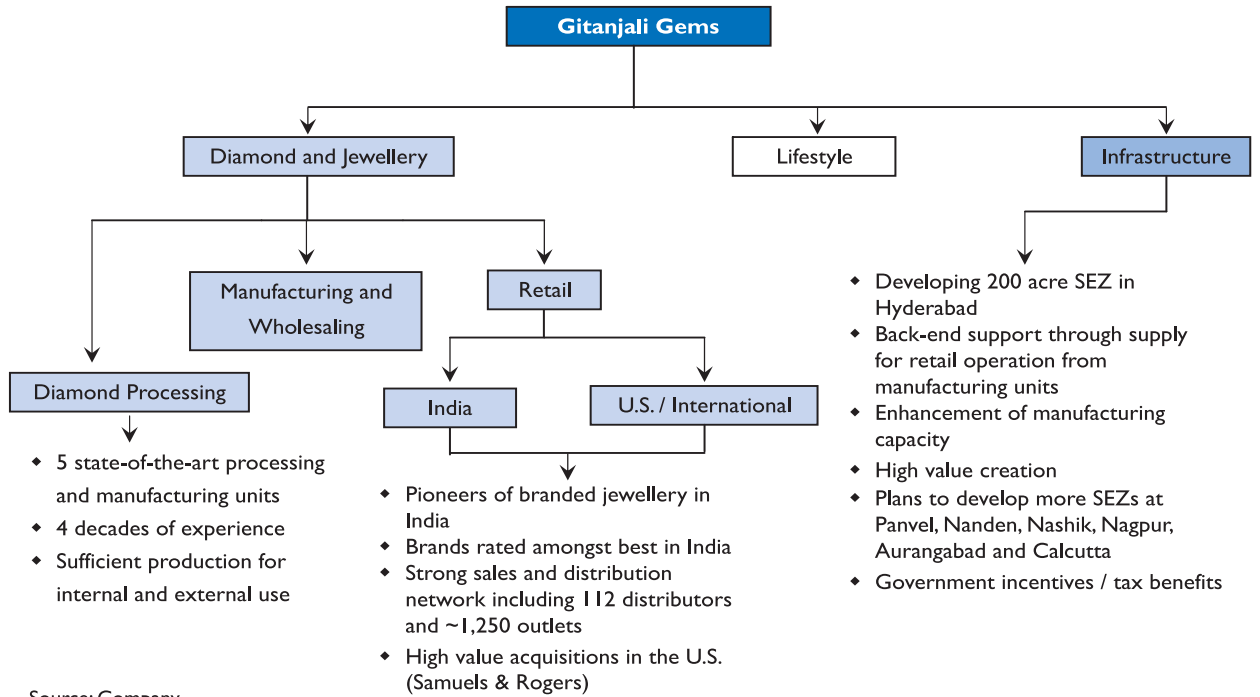
Gitanjali's branded jewelry lines were among the first branded jewelry products introduced in India. Its brands and sub-brands are aimed at different customer profiles, various market and price segments and for various uses and occasions and enjoy significant brand equity and market share in their respective market segments. According to the July 2005 edition of Solitaire International, a publication of the Gem and Jewelry Export Promotion Council of India, four of its brands - *Nakshatra*, *Asmi*, *Gili* and *D'Damas* - feature among the ten best known jewelry brands in India. The company's first jewelry brand *Gili* was selected as a Superbrand in 2004.

The company has been diversifying into high growth / value space by moving up the jewelry value chain. Moreover, it has also forayed into SEZ development, which will provide back end support and create value. Expansion to lifestyle retailing products is also expected to compliment its retail jewelry operations. Gitanjali's organizational

PRIME BROKING

PRIME

structure looks as under:



Source: Company

SWOT Analysis

<p>Strengths</p> <ul style="list-style-type: none"> • Large, integrated diamond and jewelry company with strong international credentials • Broad product range, strong brand equity and significant retail operations • Strong marketing and distribution network • Sightholder status with DTC and access to other primary source diamond suppliers • Well-developed manufacturing capabilities • Proven management team 	<p>Weaknesses</p> <ul style="list-style-type: none"> • Execution of retail expansion plans • Timely completion and commencement of SEZ operations • Substantial currency appreciation • Profitability of its overseas operations • Gold price fluctuations • Lifestyle changes
<p>Opportunities</p> <ul style="list-style-type: none"> • Consumer shift towards diamond jewelry due to rising disposable incomes • Favourable demographic profile in India • Enhanced trust as a result of certification of gold and diamonds and lifetime return and buyback policies • The contemporary jewelry buyers do not have a continuing relation with the traditional family jewelers and are more inclined to purchase branded jewelry 	<p>Threats</p> <ul style="list-style-type: none"> • A reduction in demand for jewelry products • Ability to retain existing customers or encourage repeat purchases and management of inventory • Consumer tastes and preferences for diamonds and fine jewelry • General economic conditions • Lack of control on advertising and other marketing costs • Costs to acquire raw materials • Pricing and marketing strategies vis-à-vis competition • Conditions or trends in the diamond and fine jewelry industry • Currency fluctuation risk

Source: Company

INVESTMENT HIGHLIGHTS

Strengthening the back-end of the jewelry value chain

One of the largest integrated diamond and jewelry companies in India

Gitanjali is an integrated diamond and jewelry manufacturing company and one of the largest manufacturers and retailers of diamonds and jewelry in India. The company is one of ~90 sightholders globally and procures ~25% of its rough diamonds requirements from DTC at competitive prices and better quality. The company has been in this business for over four decades and has a well established presence in international markets in Europe, including to Antwerp and Italy, the United States, the Middle East as well as to several diamond and jewelry markets in Asia, including Japan, China, Hong Kong and Thailand. The design and quality of its diamond and jewelry products and large customer base outside India, including jewelry manufacturers, large department store chains, retail stores and wholesalers, have enabled Gitanjali to develop strong credentials in international markets.

Sightholder status with DTC to ensure steady supply of quality rough diamonds

Gitanjali sources ~25% of its rough diamond requirements from the DTC, the rough diamond sales arm of De Beers S.A. and the primary world-wide marketing mechanism of the rough diamond industry. As a sightholder under the DTC's Supplier of Choice program, **Gitanjali benefits from an assured and steady source of quality rough diamonds from the DTC at competitive prices, continued advertising and marketing support from DTC to develop its brands and access to DTC's consumer research knowledge base.** It procures its remaining rough diamond requirements from secondary source suppliers in the international market to ensure that there is no shortfall in the supply of rough diamonds for our operations. The company has good relations with its suppliers, including the DTC, and that its reputation and established customer base should continue to ensure access to primary sources of diamonds.

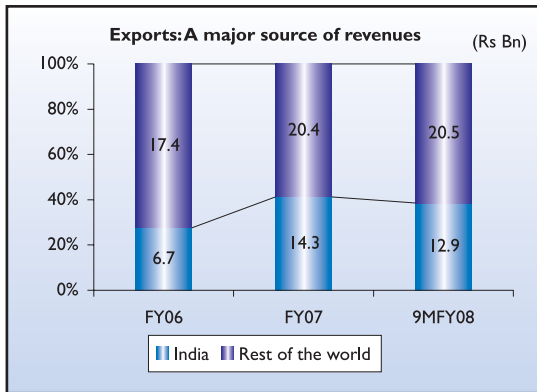
Significant manufacturing capabilities

Gitanjali has 2 modern **diamond manufacturing** facilities located at Borivali in Mumbai and at the Special Economic Zone (SEZ) in Surat. Its diamond cutting and polishing facility at Borivali employs more than 1,200 skilled employees or labourers while the facility at Surat is an export oriented facility aimed at export markets. In addition, it has 2 large sophisticated **jewelry designing and manufacturing** facilities at the SEEPZ at Andheri, Mumbai for exports and 4 **jewelry manufacturing** facilities at MIDC at Andheri, Mumbai for 4 different brands - *Gili, Nakshatra, Asmi* and *D'damas*. The company has also recently commenced manufacturing at its Hyderabad SEZ

Strengthening presence in existing businesses

The sustained growth in the Indian economy and growing employment levels, income levels and availability of credit in India resulting in greater consumer spending and disposable income, together with the strong growth in retail operations in India provides significant opportunities for Gitanjali's diamond and jewelry businesses. These factors are expected to result in an increased demand for the company's products. The company intends to leverage its significant diamond processing and strong jewelry design and manufacturing capabilities, its ability to provide a wide range of branded and unbranded diamond and jewelry products of various grades, designs and price segments, its strong branded jewelry lines and its wide retail distribution operations to increase its market share in the diamonds and jewelry business in India. It also intends to capitalize on the gradual shift of consumer preferences in India from traditional unbranded gold jewelry to diamond studded and other branded jewelry.

Continue to maintain focus on international markets



Source: Company

The company exports a significant part of its cut and polished diamonds and its branded and unbranded diamond and other jewelry products to various international markets in Europe including Antwerp and Italy, the United States, the Middle East as well as to several diamond and jewelry markets in Asia including Japan, China, Hong Kong and Thailand. Exports have been an important source of the company's growth and it intends to continue to focus on its international markets.

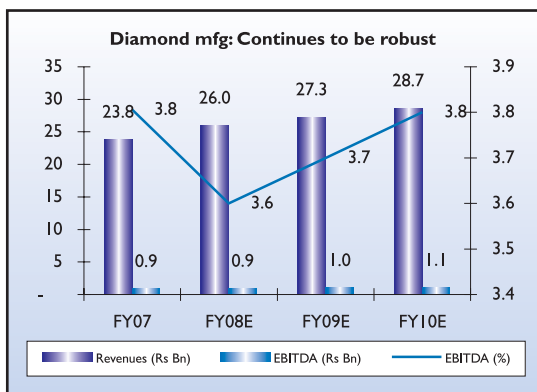
Sales to international markets have enabled the company to access a wider customer base and reduce its dependence on domestic customers. The company intends to continue to

leverage its quality products and its long-standing relationships and credentials with its international customers to further develop its international presence.

Strong Management team

Gitanjali's well-qualified senior management with significant industry experience has been instrumental in the consistent growth in its revenues and operations. The company's Chairman and Managing Director, Mr. Mehul Choksi, has been involved in the diamond and jewelry industry for more than 25 years and has driven the strong growth the company has experienced since inception.

Till recently, the company has been focusing on diamond processing and has gradually moved into jewelry manufacturing and retailing, thus moving up the value chain. We believe Gitanjali will continue to focus on its diamond manufacturing business and leverage the expertise gained in this business.



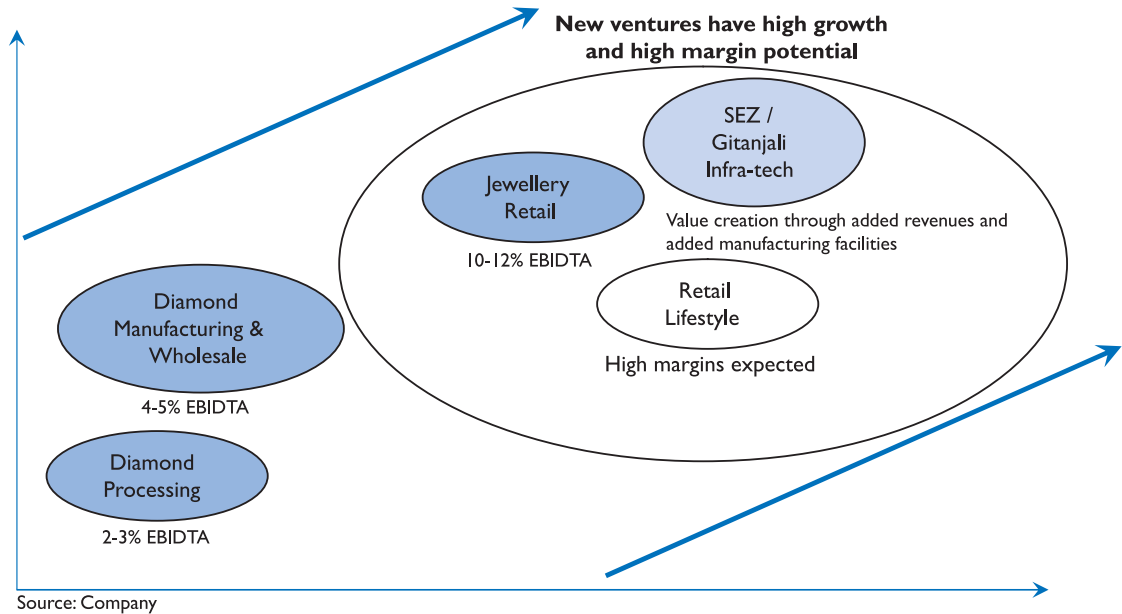
Source: Company, Prime Broking

We expect Gitanjali's diamond manufacturing business to clock 6.3% revenue and EBITDA CAGR over FY07-10E and form ~41% of FY10E revenues, with EBITDA margin of 3.8% in FY10E.

Focus on the higher end of the value chain to improve profitability

The company now intends to garner a larger share of the jewelry value chain pie and targets to increase its presence in the higher-end of the value chain, i.e. jewelry manufacturing and retailing, from its traditional focus on diamond processing. We believe that its strong jewelry designing and manufacturing capabilities, significant experience in branding and sale of branded jewelry lines (pioneer in introducing the concept of branded jewelry in India way back in 1994), strong marketing capabilities and well developed retail operations in India will enable Gitanjali to pursue this strategy with utmost success, thereby improving margins. We believe that Gitanjali is well positioned to

capitalize on the growing demand for diamonds and jewelry in the Indian and international markets.



Expanding multi-channel distribution network: to increase retail presence

Gitanjali has a multi-channel distribution network of 1,389 outlets. About 40-45% of sales occurs through exclusive distributors, which sell the products through local jewelers. About 30-35% of sales occur through various department stores and malls. Rest of the sales happen through company owned or franchisee stores.

Multi Channel Distribution Network

Sales through exclusive Distributor Network	Sales to Department Stores and Reputed Jewellery Retailers	Sales through Retail Stores owned/managed by the Group
<ul style="list-style-type: none"> • Exclusive distributor network for each brand to sell to jewellery retailers across the country • Once delivered, the distributor assumes the responsibility of selling the product • Commission paid depends on the brand and sale value of the final product 	<ul style="list-style-type: none"> • Large jewellery stores, shopping malls and department stores <ul style="list-style-type: none"> • Shoppers Stop • Globus • Westside • Gold Souk • Directly serviced by the Gitanjali Group 	<ul style="list-style-type: none"> • The retail operations of the group are classified into three different formats <ul style="list-style-type: none"> • Retail Stores owned by the group • Shop in shop outlets in department stores • Franchisee stores

Source: Company

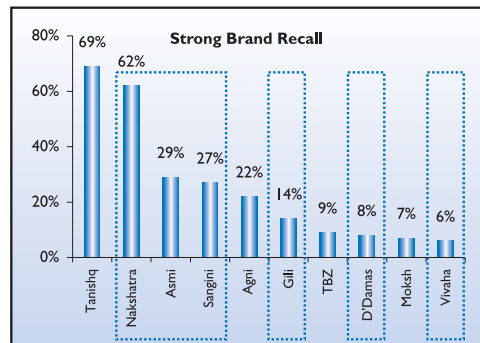
Multi-channel distribution network

Brand	Exclusive stores	Retailers	Shop in malls	Franchisee	Total
Gili	3	130	123	0	256
Asmi	2	102	0	0	104
Nakshatra	0	374	0	1	375
Sangini	0	69	5	6	80
D'damas	2	380	3	21	406
Desire Lifestyle	0	12	10	0	22
Gitanjali	3	0	0	0	3
Samuels (US)	17	0	80	0	97
Rogers (US)	46	0	0	0	46
Total	73	1,067	221	28	1,389

Source: Company

The company intends to further expand its retail operations by leveraging its existing sales and distribution network and apply innovative retail marketing initiatives in marketing its diamond and fine jewelry products. It plans to expand its distribution network from ~1,400 outlets at present to ~3,000 outlets in the next 3 years, which implies a space expansion from ~4 lac sq. ft. to 7.5 lac sq. ft.




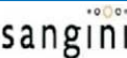

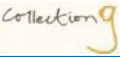





Strong brand equity



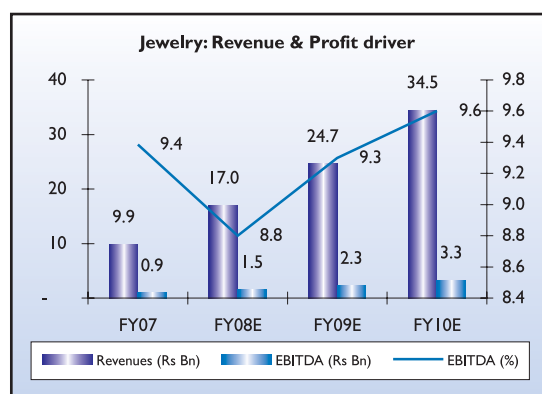
Source: The Solitaire TNS Survey 2005, Company

Gitanjali has over the years strengthened its brand portfolio with the launch of new brands and sub-brands aimed at different customer profiles, various market and price segments and for various uses & occasions. *Gili* brand of jewelry introduced in 1994 was among the first branded jewelry introduced in India. According to the July 2005 edition of *Solitaire International*, a publication of the Gem and Jewelry Export Promotion Council of India, 4 of its brands, *Nakshatra*, *Asmi*, *Gili* and *D'Damas*, feature among the ten best known jewelry brands in India. *Gili*, the company's oldest brand was selected as a *Superbrand* by Times of India in 2004. Gitanjali's brands enjoy significant brand equity in their respective market segments developed through aggressive advertising and marketing campaigns.

Leading Brands addressing diverse consumer segments

	Easy Elegance	<input type="checkbox"/> Diamond studded branded jewellery at reasonable prices <input type="checkbox"/> Pan-India retail presence with approximately 150 outlets <input type="checkbox"/> Awarded Superbrand status in 2004 by ICSC
	The Fire Within	<input type="checkbox"/> Was originally introduced by DTC <input type="checkbox"/> Premium work wear collection
	The Enchanting Enigma	<input type="checkbox"/> Includes entire range including bridal jewellery <input type="checkbox"/> Awarded Superbrand status in 2004 by ICSC
	Partners for Life	<input type="checkbox"/> Brand focus on couples <input type="checkbox"/> Covers entire product range including bridal jewellery
	The Art of Beauty	<input type="checkbox"/> Designs combine international quality and Indian values
	The Art of the Different	<input type="checkbox"/> Gold jewellery brand under D'Damas <input type="checkbox"/> Offers contemporary and modern designs in gold jewellery
	The Wedding Collection	<input type="checkbox"/> Plain gold as well as diamond jewellery for weddings
	Pure. Proud. Precious	<input type="checkbox"/> Gold jewellery aimed at Indian wedding market and other similar events
	Unique International Allure	<input type="checkbox"/> High-end jewellery brand
	Lifestyle Redefined	<input type="checkbox"/> Offers branded jewellery, watches and other lifestyle accessories
		<input type="checkbox"/> Source of "Mined in Canada" branded diamonds <input type="checkbox"/> Canadia branded diamond jewellery sold by retailers in the U.S., Canada, U.K. and Australia

Source: Company



Source: Company, Prime Broking

With Indian consumer's growing preference for branded jewelry, we believe Gitanjali has the wherewithal in place to capitalize on this booming growth opportunity.

We expect the jewelry business to clock 52% revenue CAGR and 53% EBITDA CAGR over FY07-10E and contribute 49% of revenues and 69% of EBITDA in FY10E, with EBITDA margins of 9.6% in FY10E.

Beyond India: Eyeing the world's largest jewelry market through Samuels' acquisition

In order to establish its presence in the world's largest jewelry market of the US, Gitanjali has acquired 97% stake in Samuels Jewelers, 8th largest jewelry chain in the US, for ~US\$12 MM in cash (US\$9 MM upfront and US\$1.5 each by the end of 1st and 2nd years) & 1.55 MM shares of Gitanjali @ Rs275 per share in Dec '06. Samuels Jewelers was established in 1891 and offers exclusive designer collections and a large selection of loose and mounted diamonds. It has 97 retail stores across 18 states in the US, with 17 exclusive stores and 80 shop in department stores and its products are primarily targeted at the middle and upper middle class consumers.

By way of this acquisition the company has got access to a large US consumer base and it offers a range of synergies to the company's existing operations. Leveraging Samuels' existing retail infrastructure gives the company

control over the entire value chain in the jewelry business. Moreover, Gitanjali will benefit from Samuels' 116-year old heritage and leading market position and establish an able platform for further retail expansion in the US. Samuels is expected to source a significant portion of its jewelry products from Gitanjali (40-45% of Samuels' requirement was met captively in FY08, which is expected to go up to 70-75% during FY09 and 80-85% thereafter), thus improving its operating margins. Samuels' seasoned management team and expert employees have allowed the company a smoother entry into the US market.

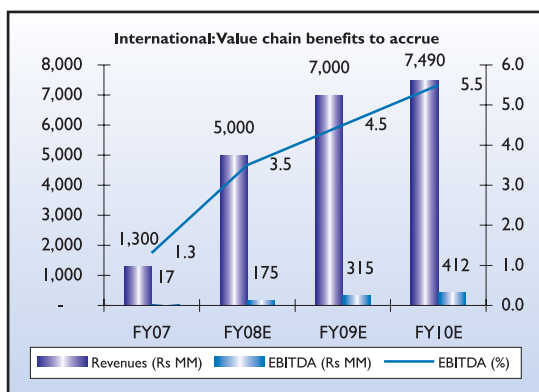
Samuels earned revenues of US\$100 MM in FY07 and was EBITDA neutral during that period. Gitanjali seems to be progressing well in integrating Samuels' operations and expects to earn 5.5% EBITDA margins by FY10E from its international business (i.e. Samuels + Rogers), as value chain benefits start accruing.

Expanding presence in the US through Rogers' acquisition

In Nov '07, Gitanjali acquired 100% stake in Rogers Jewellers, one of the oldest family run jewelry chains in the US, for an investment of US\$20 MM. Rogers is a 'Speciality Retailer', which operates 46 stores spread across 11 states in the US with revenues of US\$80.6 MM in FY07. Rogers offers exclusive designer collections, primarily targeted at the middle and upper middle class consumers.

This acquisition establishes Gitanjali's footprint in the US jewelry market, which commands 35% of the global jewelry market, making it a landmark step for the Indian gems and jewelry industry. With the US accounting for over 50% of the global diamond jewelry sales, it also marks a significant consolidation in Gitanjali's global footprint. With this, Gitanjali has acquired crucial footprint in North Central and Mid West American market & control over value chain and strengthened its unique vertically integrated 'Roughs to Retail' business model.

The above acquisitions of Samuels and Rogers will benefit the group, enabling them to manage both Samuels and Rogers, with the same back-end supply chain from India. By providing back-end integration both the chain stores have the unique benefit of cost-efficient sourcing and deeper control of marketing and merchandising.



Source: Capitaline Plus

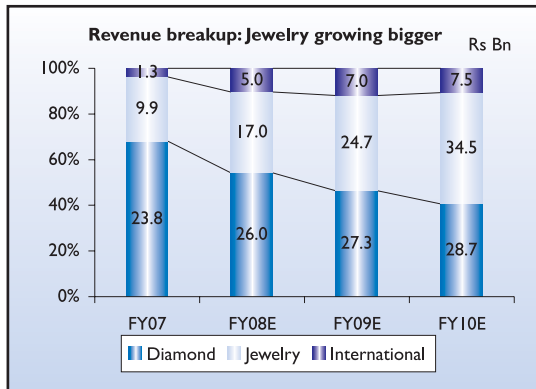
We believe that Gitanjali will continue to look for such acquisitions to strengthen its foothold in the world's largest jewelry market of the US and continue to avail of the value chain benefits in the process. Moreover, the company is also targeting the Chinese market for such alliances while China's share in the global jewelry demand rises rapidly.

We expect the international business to contribute 11% of revenues and 9% of EBITDA in FY10E, with EBITDA margins improving from 1.3% in FY07 to 5.5% in FY10E, led by value chain benefits.

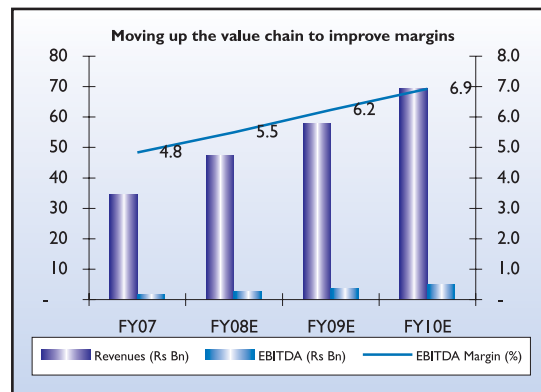
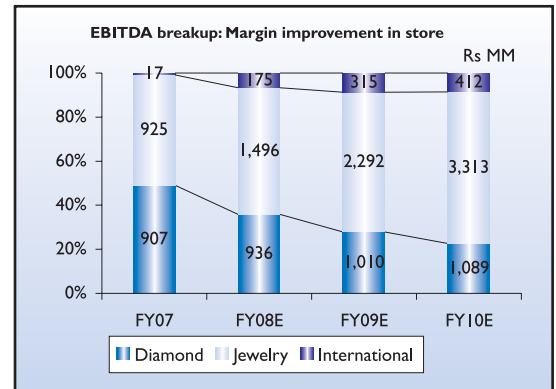
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PRIME

We believe all this to result in strengthening the company presence in the jewelry manufacturing and retailing part of the value chain and thereby lead to improvement in the overall EBITDA margins from 4.8% in FY07 to 6.9% in FY10E.



Source: Company, Prime Broking



Source: Company, Prime Broking

Looking into high growth / value space

The company intends to diversify into high growth / value space through its foray into lifestyle retailing and SEZ development. We believe these to be huge profitability boosters for the company in the years to come.

Foray into lifestyle retailing: Tapping the premium end of the market

The company has set up a wholly owned subsidiary Gitanjali Lifestyles Limited (GLL) during FY08, as its lifestyles arm. GLL aspires to tap the unexplored luxury and premium retail segment of the society through products like Premium Jewelry, Watches, Silverware, Perfumes & Cosmetics, Leather & Accessories.

The company operates through three service verticals, Retail, Media & Distribution with over 2,000 existing points of sales. It intends to open 200 lifestyle stores in metros and mini-metros across industries i.e. lifestyle, fashion, jewelry, food & beverages and health & beauty. The company has entered into various acquisitions and joint ventures to expand its presence in lifestyle retailing.

Acquisitions and tie-ups in lifestyle retailing

Company	Acqn./JV	Product range	Distribution	Key Brands
Morellato & Sector	JV	Watches, Leather goods, Writing Instruments, Jewelry	Through distinguished & prestigious jewelry & watch shops in India and dedicated stores	Morellato, Molecule, Sector, Philip, Just Cavalli, Miss Sixty, Roberto Cavalli, John Galliano & Pirelli Pzero Tempo
Mariella Bitrani Fashion Group, Italy	JV	Luxury goods		Mariella Burani, Baldinini, Rosato, Calgaro & Facco
Renaissance Retail Ventures	Acqn.	Premium Silver Jewelry	9 flagship stores and 32 shops in India, plans to open 5 more stores	Lucera
Trinity Watch Company	Acqn.	Premium Watches	100 locations	Iris, Saint Hanore, Umbro & Everlast
Hoop Silver Jewelry	Acqn.	Fashion Jewelry	10 stores	Hoop

Source: Company

SEZ foray to diversify revenue stream: Hyderabad SEZ to be a huge value trigger

Gitanjali plans to diversify into SEZ development and is developing sector specific Gems & Jewelry SEZs and multi-product SEZs at different locations in India.

Gitanjali's Gems' SEZ projects

Location	Type of SEZ	Area (hectares)	Approval status
Hyderabad, AP	Gems & Jewelry	80.9	Formal approval received. Notified by the central govt. Land acquired
Raigad, Maharashtra	Gems & Jewelry	10.2	Formal approval received from central govt.
Nanded, Maharashtra	Gems & Jewelry	50	In-principle approval received from state and central govt.
Aurangabad, Maharashtra	Gems & Jewelry	50	In-principle approval received from state govt.
Nagpur, Maharashtra	Multi-product	1000	In-principle approval received from state govt.
Nashik, Maharashtra	Multi-services	100	In-principle approval received from state and central govt.

Source: Company

Gitanjali has already received notification for an exclusive 200-acre gems and jewelry SEZ in Hyderabad and has been allotted land for the same. The company plans to operate this SEZ through 100% subsidiary Hyderabad Gems SEZ Ltd. This will be the contemporary destination for manufacturers, businessmen and entrepreneurs in the field of Gems & Jewelry for both gold & diamonds. The facility would house cutting and polishing units, testing laboratories, certification centres, banks, merchandising centres and other services relevant to the trade. The park is strategically located where India's finest jewelry craftsmen are based. It has already set up a dedicated training centre at Hyderabad SEZ with present capacity to train up to 1,200 employees.



We believe this location is ideal for the jewelry industry because of its

- 1) Proximity to international airport (distance of 3 kms)
- 2) Tax benefits available to the developer and user of SEZ
- 3) Abundant supply of quality labour

In addition to setting up its own manufacturing operations at this SEZ (one facility is already operational), Gitanjali also plans to leverage its international reach to attract global players to start their manufacturing activities in the SEZ. India offers unique advantages in terms of lower costs and ample skilled labour, which may attract these players. Apart from this, the company will also build factory sheds for many small diamond and jewelry manufacturers.

The company has already invested Rs1 Bn in the SEZ and plans an additional capex of Rs500 MM over the next 2 years. It is looking for a development partner (which will henceforth fund the SEZ project by selling stake in 100% subsidiary, thereby resulting in no further capex on Gitanjali's account). The company is already in talks for tie up with a couple of international players who have experience in developing SEZs.

Of the 200 acres of land, 125 acres is the developable area, which translates into a developable area of ~40 MM sq. ft. (msf) (as indicated by the management). We have taken a 30% discount to this available area, which gives a saleable area of 28 msf. On that we have taken a further 25% discount to arrive at an area sold of 21 msf. We have assumed the development to complete by FY11. The cost of acquiring this land to the company is Rs100 MM. We have assumed a lease model for this SEZ and have assumed lease rentals of Rs25 psf per month starting from FY09 and to grow at 3% p.a. We have assumed a development cost of Rs1,500 psf expected to grow at 5% p.a. We have also assumed overhead costs of 10% of the development cost in the first year of development, which is expected to increase by 10% p.a. thereafter.

Hyderabad SEZ valuation

Year	Cashflow	WACC PV Factor	Discounted cashflow
FY08	(100)	1.00	(100)
FY09	(9,450)	0.87	(8,217)
FY10	(7,854)	0.76	(5,939)
FY11	(6,163)	0.66	(4,052)
FY12	5,487	0.57	3,137
Terminal Value	45,722	0.57	26,142
WACC	15.0%	DCF Value (Rs MM)	10,970
		Shares O/s (MM)	85.1
		Value per share (Rs)	129

Source: Prime Broking

We have valued Hyderabad SEZ at Rs11 Bn, which gives a value per share of Rs129. We believe that we have been pretty conservative in our valuation estimates and once there is increased visibility over the company's SEZ business and / or the company enters into a tie-up with an international SEZ developer, there will be a significant upside potential for this part of Gitanjali's business.

Moreover, once this SEZ is operational and the company shift its existing manufacturing facilities to this SEZ, ~5 lac sq. ft. of land at Mumbai will become free, with ~3.2 lac sq. ft. of commercial space. We believe that the company will give this land on lease, which will add directly to the bottom line.

We believe that Gitanjali's strategy of expanding its existing business (by expanding its retail operations and US presence), moving up the value chain and diversifying into real estate business should hold itself in good stead to ride the growth momentum and take itself to the next league of the jewelry value chain.

Aggressive Expansion across the Value Chain



Source: Company

PRIME BROKING



CAPEX

Gitanjali plans to spend Rs2 Bn over FY09-10, on core business to expand its manufacturing facilities and increase its store rollout. In addition, it also plans to invest Rs500 MM on Hyderabad SEZ. The company has significant cash (Rs12.2 Bn estimated in FY08E) lying with itself to fund this capex following its recent FCCB and GDR issuance. We expect the company's return ratios to improve significantly with RoCE improving from 11% in FY07 to 14.8% in FY10E and gearing to reduce from 1.7 in FY07 to 0.4 in FY10E, once it increases its retail presence and integration benefits from its US acquisitions start creeping in.

VALUATIONS & OUTLOOK

We have valued Gitanjali using the sum-of-the-parts valuation method. We have segregated Gitanjali's operations into two business - (i) core jewelry business and (ii) SEZ development. For its jewelry business, we have used a P/E multiple and for its SEZ development, we have used the DCF method to arrive at the target price.

Peer Valuations

FY09E	Gitanjali	Rajesh Exports	Titan	Vaibhav Gems	Gems TV	Chow Sang Sang	Zale
Revenues (Rs MM)	58,050	86,696	51,008	13,553	14,494	47,071	83,191
YoY growth	22.5%	9.6%	28.1%	32.5%	31.3%	8.7%	-0.4%
EBITDA Margins	6.2%	5.3%	8.4%	10.8%	12.7%	8.8%	7.7%
PAT Margins	4.1%	3.2%	5.1%	5.2%	10.2%	7.3%	1.3%
PAT YoY growth	42.6%	56.2%	33.4%	2256.7%	-0.2%	12.4%	-258.8%
P/E (x)	12.9	7.6	20.4	3.2	4.2	8.9	19.4
EV/EBITDA (x)	8.0	-1.8	12.7	2.3	n.a.	7.5	6.1
EV/Sales (x)	0.5	-0.1	1.0	0.1	0.4	0.7	0.4

Note: US\$1 = Rs40.15; HKD1 = Rs5.15

Gems TV - Year ending Jun '09; Chow Sang - Year ending Dec '09; Zale - Year ending July '09

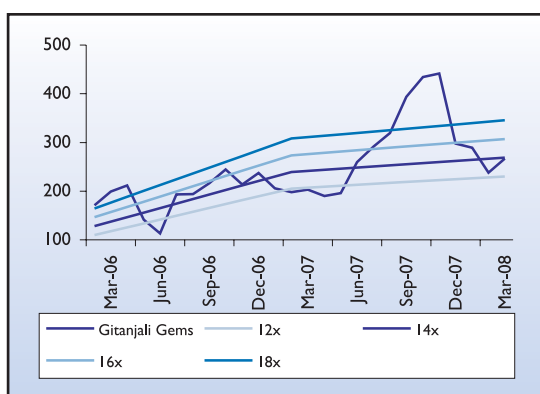
Source: Bloomberg, Prime Broking

We believe that there is no strictly comparable Indian peer for Gitanjali, when we take the size and scope of operations of these companies into consideration. However, Titan and Rajesh Exports (both engaged in jewelry business) are the closest comparables. If we see the performance of all the three stocks in 2008 so far, has been weak, led by growth concerns in the US and off late in the domestic market, gold price volatility and an overall weak market sentiment. After outperforming the Sensex for majority of 2007, the recent turn of events in the global economy has had a significantly negative impact on jewelry sales and has resulted in Gitanjali's valuations getting hammered by almost 54% from the highs of Dec '07. We believe such underperformance has been led by the general market weakness and the stock should gain its lost momentum, considering the strong prospects of the branded jewelry business and the value chain benefits to accrue from its recent US acquisitions, which has supported by the fact that the share price recently has started gaining the lost momentum. We also believe that the market has overestimated the impact that US' slowing growth will have on Gitanjali's business prospects, especially in the wake of its recent acquisitions in the US, as the major positive for the company from these acquisitions will be in terms of value chain benefits led by increasing sourcing from India, which we believe is to an extent insulated from this slowing US growth. Moreover, with US being the largest jewelry market in the world and India having a

miniscule share in that market, we believe that there is a huge potential for players like Gitanjali to make the most of the value chain benefits available in such markets due to the cost advantage that a fully integrated player like Gitanjali has over its peers globally.

The company has been able to drive a rapid growth path with 28% revenue CAGR and 36% PAT CAGR over FY02-07, in the process becoming the one of the largest integrated diamond and jewelry manufacturers in India.

We expect Gitanjali to clock 26% revenue CAGR and 25% earnings CAGR over FY07-10E, led by fully integrated nature of its jewelry business, world class scale in diamond manufacturing, capitalizing on the scale and expertise achieved in diamond processing to move up the jewelry value chain by increasing its presence in jewelry manufacturing and retailing, thereby boosting its margins. **We expect the company to improve its EBITDA margins to 6.9% in FY10E from 4.8% in FY07 and PAT margins to 4.7% in FY10E from 2.6% in FY07.**



Source: Capitaline Plus

The company's rolling P/E chart shows that the company has been trading at a broad 1-yr P/E range of 12-24x. However, recent market correction has resulted in the stock trading at a P/E range of 12-16x for the last 2-3 months. Based on Gitanjali's strong growth traction (20% CAGR in earnings), a P/E multiple of 12x looks reasonable with a PEG ratio of 0.6x, considering company's integrated nature of business, value chain enhancement, establishing footprint in the US and diversifying into SEZ development.

SOTP valuation

Part	Parameter	Value (Rs Bn)
Core Business	P/E of 12x FY10E EPS	30.8
Hyderabad SEZ	DCF Valn. @ 15% WACC	11.0
Total EV		41.8
Net Debt		3.2
Market Cap		38.7
No. of shares (MM)		85.1
Value per share (Rs)		455

Source: Prime Broking

We believe that once the company successfully increases its presence in the branded jewelry space and its share in the total revenues increase, the company should be a potential candidate for valuation re-rating. Moreover, we have considered execution discount, while valuing Hyderabad SEZ due to the company's lack of experience in SEZ development. However, any increased visibility over Gitanjali's SEZ business and the company entering into a tie-up with an international developer(s) should provide a significant upside to the valuations.

At CMP of Rs278, Gitanjali's FY09E cons. EPS of Rs21.5 is discounted 12.9x & FY10E EPS of Rs30.2 is discounted 9.2x. We recommend **STRONG BUY** on Gitanjali with a **price target of Rs455 (64% upside) based on 12x FY10E EPS** valuing jewelry business at Rs363, plus Rs129 for Hyd. SEZ less net debt of Rs37. Gitanjali's strong track record and experienced management gives us comfort to our estimates.

Our sum-of-the-parts valuation gives a target price of Rs455, with the core jewelry business valued at Rs363 per share, Hyderabad SEZ valued at Rs129 less net debt of Rs37 per share.

Annexure I: Profit & Loss A/c

Rs MM	FY06(A)	FY07(A)	FY08(E)	FY09(E)	FY10(E)
Net Sales	24,033	34,674	47,400	58,050	69,465
<i>YoY Growth</i>	77.7%	44.3%	36.7%	22.5%	19.7%
Total Cost	22,980	32,996	44,870	54,559	64,745
EBITDA	1,054	1,679	2,607	3,618	4,814
<i>EBITDA Margin</i>	4.4%	4.8%	5.5%	6.2%	6.9%
Depreciation	27	70	190	292	417
EBIT	1,041	1,649	2,517	3,375	4,447
Interest	409	496	600	643	648
PBT	631	1,153	1,916	2,732	3,799
Tax	92	143	230	328	456
PAT	539	1,009	1,686	2,404	3,343
PAT (after minority interest)	514	918	1,583	2,300	3,239
<i>PAT Margin</i>	2.1%	2.6%	3.3%	4.0%	4.7%
<i>YoY Growth</i>	487.5%	78.4%	72.5%	45.3%	40.8%
Shares Outstanding (MM)	59.0	59.0	85.1	107.1	107.1
EPS (Rs)	4.8	8.6	14.8	21.5	30.2

(A) Audited; (E) Estimated

Source: Company, Prime Broking

Annexure II: Balance Sheet

SOURCES OF FUNDS	FY06(A)	FY07(A)	FY08(E)	FY09(E)	FY10(E)
SOURCES OF FUNDS					
Shareholders Fund	8,313	9,668	23,984	32,680	35,925
Loan Funds	6,969	14,589	13,991	11,726	12,726
Total Funds Employed	15,282	24,257	37,975	44,406	48,651
APPLICATION OF FUNDS					
Net Fixed Assets	344	1,770	2,177	3,134	3,967
Investments	101	229	1,229	2,229	3,229
Net Current Assets	14,834	22,013	34,324	38,797	41,209
Current Assets	20,413	31,844	47,733	55,135	60,619
Current Liabilities	5,221	9,313	12,731	15,591	18,657
Provisions	358	519	679	747	753
Miscellaneous Expenditure	1	245	245	245	245
Deferred Tax Assets	2	0	0	0	0
Total Net Assets	15,282	24,257	37,975	44,406	48,651

Rs MM; (A) Audited; (E) Estimated

Source: Company, Prime Broking

Annexure III: Cash Flow Statement

Rs MM	FY07(A)	FY08(E)	FY09(E)	FY10(E)
Profit Before Tax	1,153	1,916	2,732	3,799
Add -				
Depreciation and Amortisation	70	190	292	417
Inc/(Dec) in Sundry Creditors	4,092	3,418	2,860	3,066
Inc/(Dec) in other liabilities	0	0	0	0
Inc/(Dec) in Provisions	161	160	68	6
Less -				
Inc/(Dec) in Inventory	5,168	5,189	4,508	5,343
Inc/(Dec) in Sundry Debtors	2,813	3,645	1,845	2,162
Inc/(Dec) in Loans & Advances	1,389	986	825	885
Tax Paid	143	230	328	456
Operational Cash Flow	-4,037	-4,366	-1,554	-1,559
Add -				
Proceeds from issue of equity	0	261	220	0
Share Premium Received	0	12,931	6,213	0
Net Secured Borrowings	2,757	1,000	1,000	1,000
Net Unsecured Borrowings	4,863	-1,598	-3,265	0
Less -				
Dividend Paid (including tax)	110	160	228	234
Net Investment	128	1,000	1,000	1,000
Net Fixed Assets incl. Adj. for CWIP	807	1,000	1,250	1,250
NET CASH FLOW	2,538	6,068	137	-3,043
Opening Cash Balance	4,113	6,175	12,243	12,379
Closing Cash Balance	6,175	12,243	12,379	9,337

(A) Audited; (E) Estimated

Source: Company, Prime Broking

Annexure IV: Ratios

	FY06(A)	FY07(A)	FY08(E)	FY09(E)	FY10(E)
Profitability Ratios					
EBITDA Margin	4.4%	4.8%	5.5%	6.2%	6.9%
EBIT Margin	4.3%	4.8%	5.3%	5.8%	6.4%
PAT Margin	2.2%	2.9%	3.6%	4.1%	4.8%
Return Ratios					
RoCE	10.3%	11.0%	10.0%	11.7%	14.8%
RoE	7.0%	11.6%	7.4%	7.7%	9.7%
RoA	3.5%	4.2%	4.4%	5.4%	6.9%
Leverage Ratio					
D/E	90.6%	167.2%	61.1%	37.3%	37.0%
Valuation Ratios					
P/E	31.9	17.9	14.9	12.9	9.2
P/BV	2.1	1.9	1.0	0.9	0.9
EV/EBITDA	18.3	14.8	9.7	8.0	6.8
EV/Sales	0.8	0.7	0.5	0.5	0.5

(A) Audited; (E) Estimated

Source: Company, Prime Broking

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PRIME BROKING



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STOCK OWNERSHIP / CONFLICT DISCLOSURE

Prime / Prime Subsidiaries	No
Key Prime Management &/or Other Employees	No
Any Other Corporate Finance Conflict of Interest	No

ANALYSTS' RATINGS DEFINITIONS

STRONG BUY	Expect \geq 25% CAGR return
BUY	Expect a CAGR return \geq 15% and $<$ 25%
HOLD	Expect $<$ 15% CAGR return
SELL	Expect \leq 5% CAGR return

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