kotak® Institutional Equities

INDIA DAILY

October 15, 2007

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News Roundup

Corporate

- Oracle has made an unsolicited offer to buy BEA Systems for US$6.66 bn in cash, as it aims to overtake rivals SAP and IBM. (BS)
- Global car makers such as BMW, Nissan, Toyota, and Honda are in talks with India's National Automotive Testing and R&D Infrastructure Project to avail themselves of its facilities for testing the durability and performance of their vehicles for the global market. (BL)
- Coal India Ltd is planning to regulate supplies to four central and state-run power utilities for non-payment of coal dues accumulating up to Rs1,062 crore till September 30. (BS)
- ICICI Bank is likely to exit the sub-prime business because of the high reputation risk the business poses to the country's second-largest lender. (ET)
- France-based Ethypharm has said it will start supplying its drug delivery system from India to pharmaceutical companies in regulated markets of the US and Europe by mid next year. The company expects overseas business to contribute US$50 mn to its topline from India. (BL)

Economic and political

- After two months of uncertainty, the threat of midterm elections appeared to recede today as the United Progressive Alliance (UPA) government and the Congress party acknowledged that they had decided to halt negotiations on the Indo-US civil nuclear agreement. (BS)
- In the past one year, the government has become wealthier by US$78 bn, thanks to the appreciation in the stock prices of PSUs and new listings. (ET)
- After showing a lacklustre performance in April-August 2007, bank credit shot up by Rs65,326 crore in September on demand from corporates, SME and agriculture. Retail demand remained weak. (BS)

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

EQUITY MARKETS

		Change, %		
India	**12-Oct**	**1-day**	**1-mo**	**3-mo**
Sensex	18,419	(2.1)	18.0	20.6
Nifty	5,428	(1.7)	20.1	20.5
Global/Regional indices				
Dow Jones	14,093	0.6	4.8	1.3
Nasdaq Composite	2,806	1.2	7.8	3.6
FTSE	6,731	0.1	7.0	0.2
Nikkie	17,375	0.3	7.7	(4.7)
Hang Seng	28,938	0.3	16.2	25.3
KOSPI	2,022	(0.2)	8.1	3.0

Value traded - India

			Moving avg, Rs bn	
	12-Oct		**1-mo**	**3-mo**
Cash (NSE+BSE)	330.4		232.0	184.3
Derivatives (NSE)	904.2		405.6	431.9
Deri. open interest	959.5		824.2	800.5

Forex/money market

		Change, basis points		
	12-Oct	**1-day**	**1-mo**	**3-mo**
Rs/US$	39.3	-	(123)	(103)
6mo fwd prem, %	0.7	(25)	71	24
10yr govt bond, %	7.9	-	5	(2)

Net investment (US$mn)

	11-Oct		**MTD**	**CYTD**
FIIs	246		2,775	15,794
MFs	(90)		(448)	176

Top movers -3mo basis

		Change, %		
Best performers	**12-Oct**	**1-day**	**1-mo**	**3-mo**
Reliance Energy	1,636	2.4	85.4	142.3
Neyveli Lignite	107	(0.5)	12.9	62.8
Tata Power	1,049	(3.7)	41.0	53.1
Reliance Cap	1,817	(1.2)	30.5	52.5
Arvind Mills	69	4.3	33.0	46.4
Worst performers				
i-Flex	1,808	(2.7)	(5.4)	(28.0)
Polaris	117	(3.0)	0.6	(22.3)
Punjab Tractors	225	(0.2)	(5.4)	(21.2)
Novartis India	303	(0.8)	4.3	(16.8)
Britannia	1,412	(1.1)	(7.6)	(16.7)

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Banking

HDBK.BO, Rs1431	
Rating	IL
Sector coverage view	Attractive
Target Price (Rs)	1,300
52W High -Low (Rs)	1465 - 875
Market Cap (Rs bn)	496

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	52.3	71.8	92.0
Net Profit (Rs bn)	11.4	16.5	21.8
EPS (Rs)	35.7	47.7	61.2
EPS gth	*28.5*	*33.5*	*28.3*
P/E (x)	40.0	30.0	23.4
P/B (x)	7.7	4.2	3.7
Div yield (%)	0.5	0.7	0.9

Shareholding, June 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	24.7	-	-
FIIs	44.5	2.5	1.3
MFs	5.4	1.8	0.6
UTI	-	-	(1.2)
LIC	2.9	0.8	(0.4)

HDFC Bank: Reports higher PAT, but lower-than-expected operating profit, retain IL

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- **HDFC Bank reported net profit of Rs3.68 bn, which was up 44% yoy and 5% higher than our estimate**
- **Strong NII growth and moderate growth in fee income drove most of the growth in income**
- **We believe HDFC Bank will likely continue to show strong growth in earnings over the next few years, which will keep its valuations high and retain our IL rating on the stock**

HDFC Bank reported net profit of Rs3.68 bn, which was up 44% yoy and 5% higher than our estimate. However, the company exceeded our target largely due to treasury gains. Core operating performance was 7% below our estimate as the bank reported lower other income and higher expenses. Strong NII growth and moderate growth in fee income drove most of the growth in income. We have tweaked our earnings estimates marginally, so too our target price—to Rs1,300 from Rs1,250. The stock trades at 23X PER and 3.7X PBR FY2009. We believe HDFC Bank will likely continue to show strong growth in earnings over the next few years, which will keep its valuations high and retain our IL rating on the stock.

NII growth high reflects loan growth and equity issuance

- HDFC Bank's NII growth of 44% was likely driven by similar balance sheet growth.
- The bank reported a 20 bps improvement in NIM yoy to 4%. However, this is likely due to equity issuance of US$1 bn in July 2007, while spreads remained flat qoq.

Loan growth remains strong, higher than industry

- HDFC Bank reported loan growth of 46% yoy to Rs623 bn
- Growth in retail assets, though relatively lower, was healthy at 37%, driven by business banking (small trade finance), car loans (likely gained market share), personal loans and credit cards
- Around 52.5% of HDFC Bank's loans were retail loans, of which 23% were personal loans and credit card outstanding
- Despite this, the bank maintained asset quality with gross NPL at 1.2% (rising 25% yoy) and net NPLs at 0.4%

CASA ratio maintained

- Deposits grew by 43.5% to Rs910 bn, and overall CASA ratio remained high at 52.5%
- The composition of CASA has, however, changed with current account deposit growing by a hefty 71% and savings by a lower 23%
- The higher growth in current account deposits was supported by float funds (HDFC Bank being collection bank for initial public offerings)

Fees and treasury drives other income growth

- HDFC Bank's reported a healthy growth of 25% in fee income to Rs3.9 bn, though this was 4% below our estimate
- Forex income has been a showing volatile trend, and was disappointing at Rs387 mn, down 34% yoy and 62% below our estimate
- We believe a part of income from swap book on forex operations is reflected in the treasury income. The bank booked Rs462 mn in treasury gain in 2QFY08 v/s Rs206 bn 2QFY07.

Employee cost remains high

- HDFC Bank has seen a 70% jump yoy in its employee base, translating into a 76% increase in employee cost
- This reflects the transfer of employees from its associate on its own payroll and general increase in employees due to branch and business expansion
- Simultaneously, other expense growth has moderated to around 25%, likely reflecting lower commission payments to associate on transfer of employees

Forecasts and valuation (Rs mn)

March y/e	Profit after tax (Rsmn)	EPS (Rs)	P/E (x)	BVPS (Rs)	P/B (x)	Adjt. BVPS fully diluted (Rs)	P/B (x)	RoA (%)	Equity/assets (%)	RoE (%)
2007	11,416	35.7	40.0	201.4	7.1	229.3	6.2	1.4	7.1	19.5
2008E	16,539	47.7	30.0	334.9	4.3	420.5	3.4	1.5	9.4	18.0
2009E	21,773	61.2	23.4	381.8	3.7	478.7	3.0	1.5	8.1	17.1
2010E	27,890	78.4	18.3	441.8	3.2	553.2	2.6	1.5	7.5	19.0

Price	1,431

Performance	1 month	3 month	6 month	12 month	Ytd
Absolute	21.1	19.1	49.4	49.2	33.8
Relative	1.9	(2.4)	6.3	1.6	0.1

Source: Bloomberg, Company, Kotak Institutional Equities estimates.

HDFC Bank quarterly performance

(Rsmn)	1QFY07	2QFY07	3QFY07	4QFY07	1QFY08	2QFY08	% chg	2QFY08KS	Actual Vs KS
Interest income	15,043	16,357	17,593	19,898	21,259	24,216	48.0		
Interest on advances	9,058	9,958	11,373	12,953	14,536	16,369	64.4		
Interest on invt	5,195	5,933	5,848	6,010	6,172	7,226	21.8		
Other interest	790	465	372	936	551	621	33.4		
Interest expense	6,867	7,901	8,307	8,721	10,836	12,001	51.9		
Net interest income	**8,176**	**8,456**	**9,286**	**11,177**	**10,422**	**12,215**	**44.5**	**11,941**	**2.3**
NII - post investment amortization	**7,577**	**7,880**	**8,682**	**10,545**	**9,782**	**11,627**	**47.5**	**11,291**	**3.0**
Non-int.income	3,508	3,977	3,733	3,944	5,798	4,824	21.3	5,083	(5.1)
- fee income	2,906	3,141	3,314	3,563	3,722	3,919	24.8	4,083	(4.0)
- exchange income	558	582	630	1,033	1,465	387	(33.5)	1,000	(61.3)
- sale of invts.	(23)	206	(211)	(656)	599	462	124.3	-	
Non treasury income	3,531	3,771	3,944	4,600	5,199	4,362	15.7	5,083	(14.2)
Total income	**11,684**	**12,433**	**13,019**	**15,121**	**16,221**	**17,039**	37.0	**17,024**	0.1
Op. expenses	5,527	5,791	6,050	6,839	7,744	8,184	41.3	8,171	0.2
Employee cost	1,664	1,813	2,138	2,153	2,839	3,190	75.9	3,000	6.3
Other cost	3,864	3,978	3,912	4,686	4,905	4,993	25.5	5,171	(3.4)
Operating profit	**6,157**	**6,642**	**6,969**	**8,282**	**8,477**	**8,855**	**33.3**	**8,853**	**0.0**
Provisions and cont.	2,639	3,057	2,664	3,303	3,711	3,482	13.9	3,450	0.9
Investment Amortization	599	576	604	632	640	588	2.1	650	(9.5)
NPLs	1,854	2,207	1,929	2,609	2,997	2,732	23.8	2,800	(2.4)
PBT	3,518	3,585	4,305	4,979	4,766	5,373	49.9	5,403	(0.5)
Tax	1,125	955	1,349	1,544	1,553	1,688	76.7	1,891	(10.7)
Net profit	**2,393**	**2,629**	**2,956**	**3,436**	**3,212**	**3,685**	**40.1**	**3,512**	**4.9**
Tax rate (%)	32.0	26.6	31.3	31.0	32.6	31.4	17.9	35.0	0.0
Op.profit excl treasury gains	**6,180**	**6,436**	**7,180**	**8,938**	**7,878**	**8,393**	**30.4**	**8,853**	**(5.2)**
PBT-invt gains+depreciation	**4,140**	**3,955**	**5,120**	**6,267**	**4,807**	**5,499**	**39.0**	**6,053**	**(9.1)**
PBT-Investment gains (gross) + NPL provisions	5,994	6,162	7,049	8,876	7,804	8,231	33.6	8,853	(7.0)
PBT-invt gains+ Prov	**5,395**	**5,586**	**6,445**	**8,244**	**7,164**	**7,643**	36.8	**8,203**	(6.8)
Fees/total income	29.6	30.4	29.8	29.1	33.2	26.0		29.9	
Rs bn									
Total Deposit	606.3	634.5	667.5	683.0	816.0	910.7	43.5		
Savings deposits	172.4	182.4	192.4	195.9	209.3	223.7	22.7		
Current deposits	146.7	148.5	174.3	198.1	210.9	254.6	71.4		
Term deposits	287.2	303.6	300.8	289.0	395.9	432.4	42.4		
CASA ratio (%)	52.6	52.2	54.9	57.7	51.5	52.5			
Customer assets	457.6	493.3	539.0	499.9	590.9	658.1	33.4		
Direct credit	405.7	427.8	482.0	469.4	538.4	622.8	45.6		
Investments	52.0	65.5	57.0	30.5	52.5	35.3	(46.0)		
Retail credit	231.2	252.1	260.0	283.3	306.9	345.7	37.1		
Housing loans	0	0	0	0	0	0	0		
Car loans	50.0	56.0	61.0	70.0	80.0	98.0	75.0		
Loan against sec	13.5	13.0	13.0	12.5	11.0	11.5	(11.5)		
Personal loans	37.0	41.0	40.0	44.0	54.0	57.0	39.0		
Two wheeler	18.0	18.5	19.5	20.0	18.0	17.0	(8.1)		
Credit cards	15.0	17.0	18.0	20.0	21.0	23.5	38.2		
Commercial vehicles	52.0	58.0	47.0	48.0	47.0	52.5	(9.5)		
Business Banking	33.0	38.0	44.0	52.0	54.0	67.5	77.6		
Yield measures (%)									
NIM	4.1	4.0	4.0	4.5	4.2	NA			
NIM (adj for HTM amortz)	NA	3.8	NA	NA	NA	4.0			
Capital adequacy ratios (%)									
CAR	11.7	12.1	12.8	13.1	13.1	14.9			
Tier I	8.3	8.2	8.4	8.6	9.2	11.3			
Tier II	3.4	3.9	4.4	4.5	3.9	3.6			
Other key details									
Branches	535	535	583	684	753	754			
ATM network	1,348	1,382	1,471	1,605	1,716	1,800			
Cities covered	228	228	263	316	320	327			
Asset quality measures									
Gross NPL(Rs mn)	NA	6,172	NA	6,578	NA	7,683	24.5		
Gross NPL (%)	NA	1.4	NA	1.3	NA	1.2			
Net NPLs (Rsmn)	1,831	1,857	2,156	2,000	2,364	2,437	31.3		
Net NPL (%)	0.40	0.4	0.4	0.4	0.4	0.4			
Balance sheet snapshot (Rs bn)									
CAPITAL AND LIABILITIES									
Capital	3.1	3.1	3.2	3.2	3.3	3.5	12.4		
Reserves and surplus	52.5	55.4	58.7	61.1	77.6	105.3	90.3		
ESOPs outstanding	0.0	0.0	-	-	-	-	(100.0)		
Deposits	606.3	634.5	667.5	683.0	816.0	910.7	43.5		
Borrowings	41.4	29.8	45.1	28.2	27.8	48.1	61.5		
Subordinated debt	20.9	28.1	30.9	-	-	32.5	15.4		
Other liabilities and provisions	72.8	92.7	90.7	136.9	132.2	115.3	24.3		
Total	**797.0**	**843.6**	**896.1**	**912.4**	**1,057.0**	**1,215.4**	44.1		
ASSETS									
Cash and balances with RBI	48.7	43.9	45.2	51.8	84.7	120.3	173.9		
Balances with banks, money at call and short notice	21.9	19.2	35.3	39.7	36.3	18.2	(4.7)		
Investments	284.4	310.7	297.2	305.6	351.7	402.9	29.7		
Advances	405.7	427.8	480.2	469.4	538.4	622.8	45.6		
Fixed assets	9.0	9.2	9.6	9.7	10.4	10.5	14.3		
Other assets	27.3	32.8	28.5	36.1	35.4	40.7	24.2		
Total	**797.0**	**843.6**	**896.1**	**912.4**	**1,057.0**	**1,215.4**	44.1		

Source: Company, Kotak Institutional Equities estimates.

Banking

IDFC.BO, Rs177	
Rating	IL
Sector coverage view	Attractive
Target Price (Rs)	120
52W High -Low (Rs)	194 - 68
Market Cap (Rs bn)	229

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	7.1	10.4	14.3
Net Profit (Rs bn)	4.9	6.7	9.3
EPS (Rs)	4.4	5.2	7.2
EPS gth	*25.8*	*19.8*	*38.3*
P/E (x)	40.6	33.9	24.5
P/B (x)	7.8	4.1	3.7
Div yield (%)	0.5	0.7	1.1

Shareholding, June 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	-	-	-
FIIs	34.6	0.7	0.3
MFs	4.4	0.6	0.1
UTI	-	-	(0.5)
LIC	2.9	0.3	(0.1)

IDFC: Growth on track; lower fees and capital gains pull down profits

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- **IDFC's 2QFY08 PAT was up 27% yoy to Rs1.79 bn, 8% below our estimates**
- **Strong loan growth, likely stable spreads but fees and capital gains were below estimates**
- **We will revisit our estimates after today's conference call with management, retain IL**

IDFC's reported standalone net profit for 2QFY08 of Rs1.79 bn, up 27% yoy but 8% below estimates. IDFC's net operating income was up 43% yoy, mainly supported by strong loan growth, likely stable spreads but higher NIMs—on the back of recent capital issuance. Standalone fees, a lumpy income stream, have grown considerably but below our estimates. The company has booked lower-than-expected capital gains during the quarter. While provisions have been higher, reported operating expenses were lower as IDFC adjusted share issue expenses with share premium account. We will revisit our earnings estimates after discussing the results with the management.

- **Infrastructure lending—key growth driver.** IDFC's net interest income on infrastructure loans has increased to Rs1.46 bn 51% yoy, 8% above estimates. This was largely driven by loan growth of 37% and likely stable spreads. However, equity infusion of Rs21 bn in July 2007 has improved NIMs. Disbursement growth was moderate at 16% in 2QFY08.
- **Fee income—lower than expected.** IDFC's standalone fee income (Rs296 mn) was 34% below our estimates. We note that this avenue has been lumpy in the past and we will need to monitor the same in the forthcoming quarters. IDFC's consolidated fee income (Rs790 mn in 2QFY08) is not comparable with 2QFY07 since the income from SSKI was not included in the previous year.
- **Capital gains were also lower.** Despite buoyant capital markets, IDFC has booked lower capital gains (Rs450 mn in 2QFY08—down 26% yoy and 31% below our estimates). Consequently, unrealized gain on its portfolio has increased by 33% qoq to Rs3.24 bn.
- **Higher than expected provisions and lower reported expenses.** IDFC has made provisions of Rs163 mn, considerably above our estimate of Rs70 mn. The company has provided 0.5% on incremental gross disbursements during 1HFY08. Operating expenses have been considerably below our estimates since IDFC has adjusted share issue expenses of Rs229 mn with its share premium account.

IDFC quarterly results
In Rs mn

	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	YoY(%)	2Q08E	Actual vs KS (%)
Total Income	3,218	3,876	3,863	4,104	5,568	6,044	56	6,758	(11)
Operating Income	3,211	3,863	3,863	4,058	5,568	6,028	56	6,758	(11)
Treasury									
Other Income	6	13		45	0	17	27	25	(34)
Interest and Other Charges	1,643	1,960	2,291	2,660	3,106	3,298	68	3,725	(11)
Net operating income	**1,574**	**1,916**	**1,572**	**1,443**	**2,462**	**2,747**	**43**	**3,008**	**(9)**
Net operating inc excl cap gains	**1,234**	**1,306**	**1,282**	**1,443**	**1,682**	**2,297**	**76**	**2,358**	**(3)**
Net interest income on infr	930	970	1,050	970	1,040	1,460	51	1,358	8
Treasury	60	160	120	30	300	500	213	550	(9)
Fees and advisory	110	150	140	420	400	296	97	450	(34)
Dividend	10	20	-			40	100		
Profit on sale of equity	**340**	**610**	**290**	**-**	**780**	**450**	**(26)**	**650**	**(31)**
Miscellaneous income	10	-							
Total Expenditure	**103**	**124**	**181**	**341**	**288**	**394**	**217**	**485**	**(19)**
Staff Expenses	59	95	90	117	151	154	62	140	10
Other Expenses	44	54	48	66	74	77	41	275	(72)
Provisions and Contingencies	0	(25)	43	158	63	163		70	133
PBDT	**1,472**	**1,791**	**1,391**	**1,102**	**2,174**	**2,352**	**31**	**2,523**	**(7)**
Depreciation	10	10	10	11	10	10	-	10	1
Profit before Tax	**1,462**	**1,781**	**1,381**	**1,091**	**2,164**	**2,342**	**31**	**2,513**	**(7)**
Provision for Tax	250	367	229	240	486	548	49	565	(3)
Profit after Tax	**1,212**	**1,414**	**1,152**	**851**	**1,678**	**1,794**	**27**	**1,948**	**(8)**
PBT before treasury, provisions and share issue expenses	1,122	1,146	1,134	1,249	1,447	2,056	79	2,133	(4)
Tax rate	17.1	20.6	16.6	22.0	22.5	23.4	13.4	22.5	
Other details	**1Q07**	**2Q07**	**3Q07**	**4Q07**	**1Q08**	**2Q08**	**YoY(%)**		
Gross approvals (Rs bn)	26	37	28	39	42	43	18		
Gross disbursements (Rs bn)	13	21	19	19	24	25	16		
Loan book (Rs bn)	112	123	134	142	148	168	37		
Unrealized gains (Rs bn)	1.9		2.2	2.2	2.4	3.2			
Borrowings - incremental (Rs bn)	20				36				
Borrowings - o/s (Rs bn)	111	169	134						
Consolidated numbers	**1Q07**	**2Q07**	**3Q07**	**4Q07**	**1Q08**	**2Q08**	**YoY(%)**		
Total Income	3,395	4,021	4,023	4,277	6,097	6,567	63		
Operating Income	3,388	4,008	4,023	4,232	6,096	6,551	63		
Treasury									
Other Income	6.3	13.1	0.4	45.4	0.7	16.3	24.4		
Interest and Other Charges	1,643.3	1,960	2,291	2,660.4	3,111.5	3,305.9	68.6		
Net operating income	1,751	2,061	1,733	1,617	2,986	3,261	58		
Net operating inc excl cap gains	1,251	1,451	1,443	1,617	2,206	2,811	94		
Net interest income on infr	930	970	1,050	970	1,040	1,460	51		
Treasury	60	160	120	30	300	500	213		
Fees and advisory	260	290	270	520	870	790	172		
Dividend	10	20				40	100		
Profit on sale of equity	340	610	290	-	780	450	(26)		
Miscellaneous income	160	-							
Total Expenditure	132	156	225	443	549	650	318		
Staff Expenses	76	117	112	176	348	344	195		
Other Expenses	55	64	70	108	138	142	122		
Provisions and Contingencies	0	(25)	43	159	63	164	(758)		
PBDT	1,620	1,905	1,508	1,174	2,437	2,611	37		
Depreciation	10	11	11	12	12	13	18		
Profit before Tax	1,610	1,894	1,496	1,161	2,425	2,598	37		
Provision for Tax	298	404	268	271	582	620	53		
Current Tax	336	334	263	360	553	635	90		
Deferred Tax	(40)	69	0	(92)	24	(18)	(126)		
Fringe Benefit Tax	1	1	1	3	5	4	169		
Profit after Tax	1,312	1,490	1,228	890	1,843	1,978	33		
Share of profit in associates / minority interest		56	22	39	(33)	3			
Profit after Tax (incl minorities share/ a	1,312	1,546		930	1,810	1,946			
PBT treasury and provisions	1,270	1,259		1,321	1,708	2,313			
PBT bef treasury provisions and mi	1,110	1,259		1,321	1,708	2,313			
Breakup of outstanding borrowings									
Short term	15%		19%		18%	17%			
LT Rupee loans	41%		31%		26%	33%			
LT bonds	38%		41%		41%	44%			
Foreign currency loans			6%		7%	2%			
Sub debt	6%		5%		4%	4%			
Fee income (break up)									
Consolidated	260	280	270	530	870	790	182		
AMC	150	130	130	120	130	130			
SSKI					340	380			
Standalone	110	150	140	420	400	280			

Source:Company, Kotak Institutional Equities estimates.

Transportation

CCRI.BO, Rs1945	
Rating	IL
Sector coverage view	Neutral
Target Price (Rs)	2,200
52W High -Low (Rs)	2444 - 1750
Market Cap (Rs bn)	126

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	30.5	35.3	38.7
Net Profit (Rs bn)	6.9	8.2	9.3
EPS (Rs)	106.3	126.6	143.7
EPS gth	*32.8*	*19.7*	*13.9*
P/E (x)	18.3	15.4	13.5
EV/EBITDA (x)	12.6	10.6	9.3
Div yield (%)	0.9	1.0	1.2

Shareholding, June 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	63.1	-	-
FIIs	27.6	0.6	0.1
MFs	4.4	0.6	0.1
UTI	-	-	(0.5)
LIC	-	-	(0.5)

Container Corporation: Margin decline due to discounts and empties; Revise target price, maintain In-Line rating

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- **Lower-than-expected traffic growth in the exim segment despite discounts; Domestic volumes surprise**
- **Margin decline due to discounts, higher number of empties and additional charges by Indian Railways**
- **Competition has commenced operations; market share and margins to be affected**
- **Fresh and Healthy, Concor's cold chain subsidiary likely to start sales from January next year; however, near-term contribution to earnings remain modest**
- **Revise target price to Rs2,200 (from Rs2,425 earlier), maintain In-Line rating**

Concor reported revenues of Rs8,188 mn (up 6.4% yoy) and PAT of Rs1,742 mn (down 8% yoy). Operating margins reduced significantly—by 690 bps on a yoy basis to 25.9%. Exim volume growth at 12.6% was lower than our expectation of 14%. This was despite the discounts given on FEUs in an effort to take traffic away from roads. However, domestic volume growth at 38.4% was a positive surprised (we expected 15%). The steep margin decline is attributable to discounts, higher number of empties (due to imbalance in exim trade and repositioning of containers in the domestic segment) and additional charges by Indian Railways. 5 competitors have commenced operations. Volumes and margins of Concor are likely to be affected as competitors scale up. Fresh and Healthy, Concor's cold chain subsidiary is likely to start sales from January next year. However, near-term contribution to earnings remains modest. We revise our target price to Rs2,200 (from Rs2,425 earlier) based on lower margins and volumes and reiterate our In-Line rating.

Lower-than-expected traffic growth in the exim segment despite discounts; Domestic volumes surprise

Concor reported revenues of Rs8,188 mn (up 6.4% yoy) versus our expectation of Rs9,288 mn and PAT of Rs1,742 mn (down 8% yoy) versus our expectation of Rs2,141 mn. Operating margins reduced significantly by 690 bps on a yoy basis to 25.9% (decline of 350 bps on a qoq basis). PAT has been boosted by higher other income of Rs325 mn versus Rs169 mn in 2QFY07 (Rs351 mn in 1QFY08) (Exhibits 1 & 2).

Concor offered discounts on FEUs to catalyze volumes and take traffic away from roads (which had gained market share in the quarter due to a fall in freight rates by approximately 5%). Indian Railways had lowered haulage charges on FEUs by 10% and Concor passed on the benefit to its customers. Further, Concor lowered its terminal handling charges on FEUs by 15%. This, combined with a yoy traffic growth in the exim segment at 12.6% (versus our expectation of 14%), resulted in lower-than-expected revenue growth. However, growth on the domestic segment was an impressive 38.4% (yoy), versus our expectation of 15%. For 1HFY08, Concor has thus managed a yoy traffic growth of 10.7% on the exim segment and 30.3% in the domestic segment.

Margin decline due to discounts, higher number of empties and additional charges by Indian Railways

As expected, the margin decline was due to discounts and higher number of empties. The rise in empties resulted due to a greater imbalance in import-export volumes for Concor (with a fall in exports due to the appreciating rupee). Concor estimates a higher freight expense of Rs172 mn due to the same. In the domestic segment too repositioning of containers was required, resulting in movement of empties. This resulted in additional haulage charges of Rs74 mn without corresponding revenues. Further, Indian Railways imposed brake-van charges (to be paid on a bi-annual basis), that resulted in an outflow of Rs45 mn. There was also an imposition of a 2% surcharge by Indian Railways, which Concor passed on to its customers with a 40-day lag, resulting in lower margins for the interim period. We expect margins of Concor to trend down as the lower-margin domestic segment experiences higher growth than the higher-margin exim business.

Competition has commenced operations; market share and margins to be affected

5 competitors have started their rail operations. Concor believes that it still handles approximately 95% of the containerized exim traffic transported by rail. Management highlighted in the conference call that 2 operators are operating from Concor's terminals, including Hind Terminals, which carries 50% of the non-Concor volumes. Concor earns access and handling charges from such operations out of its terminals. Concor's market share is expected to be impacted by increasing competition intensity as more players start operations, gain experience in rail operations and gradually develop their infrastructure. Margins for all players are likely to be lower, than what Concor has managed till now, due to competitive pricing.

Fresh and Healthy, Concor's cold chain subsidiary likely to start sales from January next year; however, near-term contribution to earnings remain modest

Fresh and Healthy, Concor's cold chain subsidiary, is likely to start sales of apples from January next year and hopes to achieve a turnover of Rs600 mn in the first full year of operations. It plans to sell 12,000 tons of apples in the first year (through its own branding) and has already procured 10,000 tons so far. Though volumes and realizations may increase significantly going forward, we are now estimating a PAT of Rs41 mn in FY2009E. Thus, the near term contribution to EPS is not significant. (Exhibit 3)

Revise target price to Rs2,200 (from Rs2,425 earlier), maintain Inline rating

We revise our earnings estimates based on the results of 2QFY08. We lower our exim volume estimates for Concor – growth for FY2008 lowered to 13% (earlier 14%), growth for FY2009 revised to 11% (earlier 14%) and lower market share in later years. We have increased domestic segment growth estimate to 25% (earlier 15%) for FY2008 and maintained the FY2009 estimate at 15%, based on the revised outlook. We adjust our freight and terminal handling charges downwards by 5% to reflect discounts offered by Concor. We also revise our other income estimates of FY2008 to Rs1.2 bn (Rs869 mn earlier) and of FY2009 to Rs1.5 bn (Rs1.1 bn earlier) on the back of healthy cash balances of Concor.

We have revised our March 09 DCF-based target price to Rs2,200 (from Rs2,425 earlier) factoring in lower market share and margins for Concor. We retain our Inline rating as we expect competition to gain a foothold in the rail business. (Exhibit 4)

Exhibit 1: Concor - 2QFY08 key numbers (Rs mn)

		yoy			qoq			yoy		
	FY08E	2QFY08	2QFY07	% change	2QFY08	1QFY08	%change	1H08A	1H07A	% change
Net Sales	**35,252**	**8,188**	**7,693**	**6.4**	**8,188**	**7,759**	**5.5**	**15,947**	**14,907**	**7.0**
Staff cost	(445)	(110)	(86)	27.7	(110)	(110)	0.4	(220)	(168)	30.8
Rail freight exp	(20,308)	(4,949)	(4,239)	16.8	(4,949)	(4,393)	12.7	(9,342)	(8,323)	12.2
Others	(4,082)	(1,006)	(846)	18.9	(1,006)	(975)	3.2	(1,981)	(1,732)	14.4
Total exp	**(24,835)**	**(6,065)**	**(5,171)**	**17.3**	**(6,065)**	**(5,478)**	**10.7**	**(11,543)**	**(10,224)**	**12.9**
Operating profit	**10,417**	**2,123**	**2,522**	**(15.8)**	**2,123**	**2,281**	**(7.0)**	**4,404**	**4,683**	**(6.0)**
Other Income	1,234	325	169	92.6	325	351	(7.5)	675	331	104.0
EBIDTA	**11,651**	**2,447**	**2,691**	**(9.0)**	**2,447**	**2,632**	**(7.0)**	**5,079**	**5,014**	**1.3**
Interest	-	-	-		-	-		-	-	
Depreciation	(1,208)	(260)	(232)	12.0	(260)	(258)	0.9	(519)	(455)	13.9
PBT	**10,443**	**2,187**	**2,458**	**(11.0)**	**2,187**	**2,374**	**(7.9)**	**4,561**	**4,559**	**0.0**
Tax	(2,216)	(445)	(563)	(21.0)	(445)	(503)	(11.5)	(948)	(1,000)	(5.2)
Prior period		-	(2)		-	(0)		(0)	(2)	
PAT	**8,227**	**1,742**	**1,893**	**(8.0)**	**1,742**	**1,871**	**(6.9)**	**3,613**	**3,557**	**1.6**
Key ratios (%)										
Rail freight exps / sales	57.6	60.4	55.1		60.4	56.6		58.6	55.8	
Rail freight exps / TEU (Rs)	-	-	-		-	-		-	-	
Other exp / Sales	11.6	12.3	11.0		12.3	12.6		12.4	11.6	
Operating profit margin	29.5	25.9	32.8		25.9	29.4		27.6	31.4	
Effective tax rate	21.2	20.3	22.9		20.3	21.2		20.8	21.9	
Segmental analysis										
	FY08E	2QFY08	2QFY07	% change	2QFY08	1QFY08		1H08A	1H07A	% change
Volumes (TEUs)										
Exim	1,938,445	504,748	448,387	12.6	504,748	443,147	13.9	947,895	856,029	10.7
%	79.9	81.6	84.5		81.6	79.2		80.4	82.9	
Domestic	487,006	113,846	82,278	38.4	113,846	116,657	(2.4)	230,503	176,916	30.3
%	20	18	16		18	21		20	17	
Total	2,425,451	618,594	530,665	16.6	618,594	559,804	10.5	1,178,398	1,032,945	14.1
Sales (Rs mn)										
Exim	28,149.7	6,558.7	6,382.6	2.8	6,558.7	6,103.6	7.5	12,662.3	12,163.0	4.1
%	79.9	80.1	83.0		80.1	78.7		79.4	81.6	
Domestic	7,102.1	1,629.0	1,293.3	26.0	1,629.0	1,655.7	(1.6)	3,284.7	2,726.2	20.5
%	20.1	19.9	16.8		19.9	21.3		20.6	18.3	
Per TEU realisation (Rs)										
Exim	14,522	12,994	14,235	(8.7)	12,994	13,773	(5.7)	13,358	14,209	(6.0)
Domestic	14,583	14,309	15,719	(9.0)	14,309	14,193	0.8	14,250	15,410	(7.5)
Overall	14,534	13,236	14,465	(8.5)	13,236	13,861	(4.5)	13,533	14,414	(6.1)
PBIT margin (%)										
Exim	28.3	26.8	33.8		26.8	29.4		28.1	32.2	
Domestic	17.6	10.9	14.5		10.9	19.7		15.3	15.8	

Source: Company data, Kotak Institutional Equities estimates.

Exhibit 2: Key numbers for Concor, March fiscal year ends 2006-09E

	2006	2007	2008E	2009E
Operating parameters				
Exim TEUs (nos)	1,556,714	1,715,438	1,938,445	2,151,674
% growth	13.1	10.2	13.0	11.0
Domestic TEUs (nos)	373,848	389,605	487,006	560,057
% growth	6.4	4.2	25.0	15.0
Total TEUs (nos)	**1,930,562**	**2,105,043**	**2,425,451**	**2,711,731**
% growth	**11.7**	**9.0**	**15.2**	**11.8**
TEU-mix (%)				
Exim	80.6	81.5	79.9	79.3
Domestic	19.4	18.5	20.1	20.7
Revenue mix (%)				
Exim	78.3	81.2	79.9	79.7
Domestic	21.7	18.8	20.1	20.3
Income statement extracts (Rs mn)				
Revenues	24,332	30,460	35,252	38,666
EBIDTA	6,976	9,109	10,417	11,453
EBITDA margin (%)	28.7	29.9	29.5	29.6
PBT	6,701	8,874	10,443	11,588
Tax	(1,465)	(1,969)	(2,216)	(2,249)
Effective tax rate (%)	21.9	22.2	21.2	19.4
PAT	5,237	6,906	8,227	9,338
EPS (Rs)	**80.6**	**106.3**	**126.6**	**143.7**

Source: Kotak Institutional Equities estimates.

Exhibit 3: Fresh and Healthy's to scale up significantly, however, EPS contribution in the near term would be maginal

Estimate of EPS contribution of Fresh and Heathy's

	FY2009E
Fruits handled (Tonnage)	**12,000**
Revenues (Rs mn)	**600**
Operating profit (Rs mn)	**180**
Depreciation (Rs mn)	80
Interest	39
Profit before tax (Rs mn)	62
Tax (Rs mn)	21
Profit after tax	**41**
Potential EPS contribution (Rs)	**0.6**
Revenues/Kg	50
Operating profit/Kg	15
Debt (Rs mn)	350
Equity (Rs mn)	650
Interest rate (%)	11
Tax rate (%)	34

Source: Kotak Institutional Equities estimates.

Exhibit 4: We have changed Concor's DCF-based target price to Rs2,200/share
DCF valuation (Rs mn)

Year to March	2007	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E
Revenue	**30,460**	**35,252**	**38,666**	**45,267**	**53,966**	**57,556**	**63,356**	**69,740**	**76,767**	**84,503**	**93,018**	**102,391**
Growth (%)	25.2	15.7	9.7	17.1	19.2	6.7	10.1	10.1	10.1	10.1	10.1	10.1
EBIT	8,189.8	9,208.7	10,063.6	10,411.4	11,332.9	11,511.2	12,671.1	13,947.9	15,353.4	16,900.6	18,603.6	20,478.2
EBIT margin	26.9	26.1	26.0	23.0	21.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0
Tax rate	22.2	21.2	19.4	34.0	34.0	34.0	34.0	34.0	34.0	34.0	34.0	34.0
EBIT*(1-tax rate)	**6,373**	**7,255**	**8,110**	**6,872**	**7,480**	**7,597**	**8,363**	**9,206**	**10,133**	**11,154**	**12,278**	**13,516**
Depreciation	919	1,208	1,390	1,450	1,500	1,450	1,450	1,450	1,450	1,450	1,450	1,450
Change in working capital	(702)	(131)	(102)	(198)	(261)	(108)	(174)	(192)	(211)	(232)	(255)	(281)
Capital expenditure	(3,543)	(4,260)	(4,260)	(4,950)	(6,525)	(2,692)	(4,350)	(2,000)	(2,000)	(2,000)	(2,000)	(2,000)
Free Cash Flows	**3,047**	**4,072**	**5,138**	**3,173**	**2,194**	**6,248**	**5,289**	**8,464**	**9,372**	**10,372**	**11,473**	**12,684**
Growth (%)	41	34	26	(38)	(31)	185	(15)	60	11	11	11	11
Years discounted	-	-	-	1	2	3	4	5	6	7	8	9
Discount factor	1.00	1.00	1.00	0.90	0.80	0.72	0.65	0.58	0.52	0.47	0.42	0.38
Discounted cash flow	**3,047**	**4,072**	**5,138**	**2,846**	**1,765**	**4,507**	**3,422**	**4,911**	**4,878**	**4,841**	**4,803**	**4,762**

Target price calculation	**Rs mn**
Sum of free cash flow	39,426
Discounted terminal value	89,248
Enterprise value	128,674
Add Investments	-
Net debt	(13,910)
Net present value-equity	142,584
Shares o/s	65
Target price /share(Rs)	**2,194**

WACC calculation	
Risk-free rate (Rf)	7.0%
Beta (B)	0.93
Equity risk premium	5.0%
Cost of Equity (Ke)	11.7%
Cost of Debt (Kd) (Post-tax)	8.0%
WACC (beta implied)	**11.5%**
WACC used	**11.7%**

Terminal value Calculation	**Rs mn**
Cash flow in terminal year	11,473
Growth to perpetuity (g)	**5.5%**
Capitalisation rate (WACC-g)	6.0%
Terminal value	191,215
Discount period (years)	7
Discount factor	0.47
Discounted terminal value	**89,248**

Terminal multiples	
EV/EBIDTA	9.5
P/FCF	17.6

Equity value per share assuming perpetual growth rates and WACC of

		Perpetual growth rate			
		5.0%	**5.5%**	6.0%	6.5%
WACC	11.0%	2,246	2,375	2,530	2,719
	11.5%	2,088	**2,194**	2,319	2,469
	12.0%	1,953	2,041	2,143	2,264
	13.0%	1,735	1,797	1,869	1,951

Source: Company data, Kotak Institutional Equities Estimates

Media

SUTV.BO, Rs323	
Rating	U
Sector coverage view	Cautious
Target Price (Rs)	310
52W High -Low (Rs)	462 - 278
Market Cap (Rs bn)	127.3

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	6.8	9.5	12.2
Net Profit (Rs bn)	2.5	3.9	5.3
EPS (Rs)	6.3	10.0	13.4
EPS gth	*20.8*	*57.4*	*34.6*
P/E (x)	50.9	32.4	24.1
EV/EBITDA (x)	28.4	17.9	13
Div yield (%)	0.5	0.8	1.2

Shareholding, June 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	93.0	-	-
FIIs	4.4	0.0	(0.1)
MFs	0.9	0.0	(0.1)
UTI	-	-	(0.1)
LIC	-	-	(0.1)

Media

ZEE.BO, Rs344	
Rating	U
Sector coverage view	Cautious
Target Price (Rs)	250
52W High -Low (Rs)	363 - 186
Market Cap (Rs bn)	149.3

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	15.2	17.9	20.2
Net Profit (Rs bn)	2.4	3.6	5.1
EPS (Rs)	5.5	8.4	11.8
EPS gth	*11.2*	*53.7*	*40.8*
P/E (x)	63.1	41.1	29.2
EV/EBITDA (x)	47.3	26.4	19.1
Div yield (%)	0.4	0.6	0.8

Shareholding, June 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	43.2	-	-
FIIs	30.3	0.6	0.2
MFs	10.8	1.2	0.8
UTI	-	-	(0.4)
LIC	4.8	0.5	0.1

Sun TV Network, Zee Entertainment Enterprises: Advertisers versus broadcasters—nobody wins

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- **Advertisers contemplate legal action against broadcasters' attempt to implement 25% surcharge on ad rates**
- **Broadcasters cite increase in costs, reach for higher ad rates**
- **We doubt broadcasters will be able to push through such a high increase at one go**

We do not expect the attempt by broadcasters to impose a 25% surcharge on advertisement rates (effectively increase ad rates by 25%) to succeed. We do not think advertisers will accept the increase and in fact the Indian Society of Advertisers (ISA) is reportedly considering legal action to counter the 25% surcharge on TV ad rates announced by the Indian Broadcasting Federation (IBF). We expect advertisers to maintain their budgets even if they are forced to accept higher rates, use their 'fixed' budgets more effectively, use new channels perhaps and even switch to other forms of media if the situation so warrants. We will wait for further developments on this issue before reviewing our earnings models for Sun TV and ZEEL. Our 12-month DCF-based target prices for Sun and ZEEL are Rs310 and Rs250. Key upside risks stem from stronger-than-expected ad and subscription revenues.

Fight of equals—expect status quo to continue. We expect market forces to eventually determine ad rates. We assume that market forces have been doing so for the past few years and assume that extant ad rates reflect market dynamics. Thus, we believe that the extant ad rates will likely continue and individual broadcasters' rates will depend on the popularity of the channel and not on any unilateral action of a set of market players.

We also note that new entrants may not accept the IBF's stance and may prefer to negotiate with advertisers directly to establish their fledgling channels. In fact, we see the continued fragmentation of the market as a plausible reason for ad rates being lower versus the expectations of broadcasters. Finally, the fact that over 100 channels want to start operations shortly suggests that they find the business economically viable and current rates acceptable.

Broadcasters' viewpoint. The IBF has cited (1) a steep increase in programming and other costs and (2) an increase in the reach of channels to demand higher ad rates from advertisers. The 25% surcharge is effective from October 16, 2007. We accept the arguments about increase in costs and reach but assume that the rates reflect these and other market issues. We do not find much merit in the IBF's argument given that the broadcasters have been part of the market for a long time, have participated in negotiations (monthly, annual) with advertisers and have revised rates depending on market dynamics (popularity of a channel versus other channels in that genre, growth in ad spend, increase in reach of channels).

Advertisers' viewpoint. The ISA has threatened legal action against the IBF and has sent a letter to its members to take legal action against the increase, if required. We are not sure about the validity of a legal change. We note that broadcasters are within their legal rights to increase the rates for new contracts. However, advertisers may not accept the revised rates and look at other types of media or other channels, which may not have taken a price increase.

We model strong growth in revenues for both Sun and ZEEL but revenues may face competition from new entrants. We model Sun's FY2008E, FY2009E and FY2010E ad revenues at Rs4.6 bn (+32% yoy growth), Rs5.4 bn (+17.6% yoy) and Rs6.2 bn (+14.8% yoy). Similarly, we model ZEEL's FY2008E, FY2009E and FY2010E ad revenues at Rs9.4 bn (+33% yoy growth), Rs10.6 bn (+13.1% yoy) and Rs12.1 bn (+14.3% yoy).

The key to the performance of both Sun TV and ZEEL would be their ability to defend the high market shares of their flagship general entertainment channels (Sun TV and ZTV) against new competition. We note that a few new Hindi and regional language general entertainment channels have started operations recently and some more will start operations over the next few months. We expect them to likely take some market share from incumbent operators; the strong debut of Kalaignar TV in the Tamil market is a point in case. These new channels have remarkably good pedigree and fall into two categories—(1) companies with established track records in other genres and strong financials or (2) companies with experienced professionals, backed by sharp private equity investors or other entities (political parties). Thus, we would take the competitive threat posed by the new entrants seriously.

We model Sun's revenues to grow strongly led by growth in pay-TV and FM radio revenues

Derivation of revenues of Sun TV/Sun TV Network, March fiscal year-ends, 2006-2012E (Rs mn)

	2006	2007	2008E	2009E	2010E	2011E	2012E
Advertisement revenues							
Sun TV	1,085	1,491	1,858	2,130	2,442	2,799	3,147
K TV	123	141	162	182	205	226	248
Sun News	39	47	55	62	70	78	86
Sun Music	94	122	163	183	206	232	255
Sun Kids	—	—	151	209	249	297	345
Sun Documentary	—	—	64	164	196	233	271
Sun Sports	—	9	58	65	73	82	91
Surya TV	386	476	574	663	764	881	1,003
Kiran TV	28	40	59	82	92	104	114
Gemini TV	—	467	596	686	789	907	1,032
Teja TV	—	44	51	57	64	70	77
Gemini News	—	35	41	46	52	58	64
Gemini Music	—	75	100	113	127	142	157
Udaya TV	—	428	535	615	708	814	926
Udaya Movies	—	43	49	55	62	68	75
Udaya Varthegulu (News)	—	25	29	33	37	42	46
Udaya TV 2	—	30	40	45	51	57	63
Total TV ad revenues	**1,755**	**3,472**	**4,584**	**5,389**	**6,187**	**7,091**	**7,999**
Radio	158	168	658	1,375	1,862	2,304	2,816
Total advertisement revenues	**1,913**	**3,640**	**5,242**	**6,764**	**8,048**	**9,395**	**10,815**
Broadcast revenues (or slot sales)							
Sun TV	531	607	698	768	845	930	1,023
Surya TV	60	60	69	75	83	91	100
Gemini TV	—	332	381	419	461	507	558
Udaya TV	—	86	101	111	123	135	148
Total broadcast revenues	**591**	**1,085**	**1,250**	**1,375**	**1,512**	**1,663**	**1,830**
Total ad and broadcast revenues	**2,504**	**4,725**	**6,491**	**8,139**	**9,560**	**11,058**	**12,644**
Pay-TV revenues							
Sun TV	447	659	1,335	2,016	2,473	2,874	3,196
Surya TV	—	—	—	162	208	249	284
Gemini TV	—	643	767	911	1,113	1,328	1,555
Udaya TV	—	373	447	535	656	785	920
Total pay-TV revenues	**447**	**1,675**	**2,549**	**3,624**	**4,449**	**5,235**	**5,956**
International revenues	183	339	355	371	386	399	409
Others	18	42	70	100	130	154	178
Sumangali Cable Vision (SCV)	—	—	—	—	—	—	—
Total revenues	**3,152**	**6,781**	**9,465**	**12,234**	**14,525**	**16,847**	**19,188**
Growth (%)	**9**	**115**	**40**	**29**	**19**	**16**	**14**

Source: Company, Kotak Institutional Equities estimates.

Consolidated profit model, balance sheet, cash model of Sun TV, 2006 and SunTV Network, 2007-2012E, March fiscal year-ends (Rs mn)

	2006	2007	2008E	2009E	2010E	2011E	2012E
Profit model (Rs mn)							
Net sales	3,219	6,780	9,465	12,234	14,525	16,847	19,188
EBITDA	**2,035**	**3,874**	**5,977**	**8,073**	**9,951**	**11,795**	**13,617**
Other income	172	411	789	910	1,196	1,550	1,974
Interest (expense)/income	(65)	(64)	(18)	—	—	—	—
Depreciation	(147)	(294)	(525)	(630)	(515)	(436)	(381)
Amortization	—	(56)	(235)	(235)	(235)	(235)	(195)
Pretax profits	**1,995**	**3,871**	**5,989**	**8,118**	**10,398**	**12,675**	**15,015**
Tax-cash	(709)	(1,509)	(2,059)	(2,852)	(3,614)	(4,377)	(5,163)
Tax-deferred	16	108	(18)	51	38	27	17
Minority interest	—	(9)	21	(25)	(50)	(72)	(96)
Net profits after minority interests	**1,302**	**2,461**	**3,932**	**5,292**	**6,771**	**8,253**	**9,773**
Earnings per share (Rs)	**5.3**	**6.3**	**10.0**	**13.4**	**17.2**	**20.9**	**24.8**
Balance sheet (Rs mn)							
Total equity	3,071	11,932	14,714	18,277	22,628	27,930	34,210
Deferred Tax	32	(56)	(38)	(88)	(127)	(153)	(170)
Total borrowings	2,333	867	—	—	—	—	—
Currrent liabilities	741	1,693	1,633	1,766	1,845	1,930	2,023
Total capital	**6,209**	**14,478**	**16,329**	**19,999**	**24,441**	**29,874**	**36,325**
Cash	732	6,494	6,348	9,522	13,507	18,355	24,121
Current assets	2,440	3,221	5,143	6,338	7,356	8,397	9,458
Total fixed assets	2,830	3,543	2,910	2,405	2,040	1,779	1,599
Intangible assets	206	1,220	1,927	1,732	1,537	1,342	1,146
Total assets	**6,209**	**14,478**	**16,329**	**19,999**	**24,441**	**29,874**	**36,325**
Free cash flow (Rs mn)							
Operating cash flow, excl. working capital	1,722	3,239	4,721	6,350	7,579	8,784	9,956
Working capital	(251)	(1,992)	(1,982)	(1,063)	(938)	(956)	(968)
Capital expenditure	(2,091)	(433)	(793)	(125)	(150)	(175)	(200)
Investments	(326)	(849)	(821)	(1,129)	(1,242)	(1,366)	(1,503)
Other income	80	402	789	910	1,196	1,550	1,974
Free cash flow	**(619)**	**814**	**1,946**	**5,161**	**6,490**	**7,654**	**8,788**
Ratios (%)							
Debt/equity	76.0	7.3	—	—	—	—	—
Net debt/equity	52.1	(47.2)	(43.1)	(52.1)	(59.7)	(65.7)	(70.5)
RoAE	36.1	32.9	29.6	32.2	33.3	32.8	31.6
RoACE	**26.6**	**26.8**	**29.9**	**33.0**	**34.1**	**33.6**	**32.3**

Source: Kotak Institutional Equities estimates.

Consolidated profit and loss statement for Zee Telefilms, March fiscal year-ends, 2006, ZEEL, 2007-2012E (Rs mn)

	2006	2007	2008E	2009E	2010E	2011E	2012E
Revenues							
National Hindi (Zee TV)	2,119	3,303	4,894	5,518	6,358	7,270	8,218
National Hindi (Zee Cinema)	996	1,574	1,830	2,063	2,378	2,719	3,073
Niche channels (News, English, Music, ETC Music and ZED)	1,081	400	504	601	711	837	939
Regional channels (incl. ETC Punjabi)	1,486	—	—	—	—	—	—
Zee Sports + Taj TV	72	1,279	1,636	1,904	2,149		
Cable TV (Siti)	261	—	—	—	—	—	—
Overseas - ZMWL	557	526	490	489	487	498	510
Others	(6)	(47)	—	—	—	—	—
Advertisement	**6,566**	**7,035**	**9,354**	**10,575**	**12,084**	**13,745**	**15,458**
Domestic pay-TV	2,742	3,064	3,682	4,587	5,715	6,790	7,791
Overseas	3,030	3,933	4,202	4,377	4,505	4,701	4,905
Domestic subscription	978	—	—	—	—	—	—
Others	423	(349)	—	—	—	—	—
Subscription	**7,174**	**6,648**	**7,883**	**8,965**	**10,220**	**11,492**	**12,697**
Education	162	205	210	221	232	243	255
Others	2,641	1,271	460	482	505	530	556
Total revenues	**16,544**	**15,159**	**17,907**	**20,242**	**23,041**	**26,010**	**28,966**
Programming/Content	(4,247)	(4,783)	(4,942)	(4,954)	(5,506)	(6,060)	(6,647)
Broadcasting	(515)	(564)	(516)	(513)	(509)	(519)	(530)
Distribution	(2,565)	(1,967)	(1,824)	(1,890)	(1,932)	(2,007)	(2,086)
Other direct operating	(262)	(766)	(804)	(844)	(886)		
Employees	(1,089)	(1,017)	(1,361)	(1,472)	(1,575)	(1,695)	(1,827)
SG&A	(3,431)	(2,858)	(2,845)	(2,925)	(3,113)	(3,291)	(3,589)
Total expenses	**(13,848)**	**(11,955)**	**(12,292)**	**(12,598)**	**(13,521)**	**(14,504)**	**(15,655)**
EBITDA	**2,695**	**3,204**	**5,615**	**7,644**	**9,520**	**11,506**	**13,311**
Other income	639	747	723	812	937	1,179	1,488
Interest expense	(188)	(334)	(240)	(89)	(2)	—	—
Depreciation	(360)	(185)	(269)	(288)	(301)	(307)	(317)
Amortization	—	—	—	—	—	—	—
Pretax profits	**2,787**	**3,432**	**5,829**	**8,079**	**10,154**	**12,378**	**14,482**
Extraordinary items	19	—	—	—	—	—	—
Tax	(528)	(926)	(1,952)	(2,686)	(3,460)	(4,193)	(4,921)
Deferred tax	(9)	(76)	(3)	6	12	16	19
Minority interest	(117)	(58)	(227)	(263)	(306)	(351)	(396)
Net income	**2,153**	**2,373**	**3,647**	**5,136**	**6,400**	**7,850**	**9,184**
Recurring net income	**2,134**	**2,373**	**3,647**	**5,136**	**6,400**	**7,850**	**9,184**
Fully diluted EPS	**4.9**	**5.5**	**8.4**	**11.8**	**14.7**	**18.1**	**21.2**
Key ratios							
EBITDA growth (%)	**(38.1)**	**18.9**	**75.3**	**36.1**	**24.5**	**20.9**	**15.7**
EPS growth (%)	**(34.6)**	**11.2**	**53.7**	**40.8**	**24.6**	**23.0**	**17.0**
EBITDA margin (%)	16.3	21.1	31.4	37.8	41.3	44.2	46.0
Tax rate (%)	19.1	29.2	33.5	33.2	34.0	33.7	33.9
Shares o/s year end (mn)	413	434	434	434	434	434	434
Shares o/s fully diluted (mn)	435	435	435	435	435	434	434

Source: Kotak Institutional Equities estimates.

Consolidated profit model, balance sheet, cash model of Zee Telefilms, 2006 and of ZEEL, 2007-2012E, March fiscal year-ends (Rs mn)

	2006	2007	2008E	2009E	2010E	2011E	2012E
Profit model (Rs mn)							
Total revenues	**16,544**	**15,159**	**17,907**	**20,242**	**23,041**	**26,010**	**28,966**
EBITDA	**2,695**	**3,204**	**5,615**	**7,644**	**9,520**	**11,506**	**13,311**
Other income	639	747	723	812	937	1,179	1,488
Interest	(188)	(334)	(240)	(89)	(2)	0	0
Depreciation	(360)	(185)	(269)	(288)	(301)	(307)	(317)
Amortization	—	—	—	—	—	—	—
Pretax profits	**2,787**	**3,432**	**5,829**	**8,079**	**10,154**	**12,378**	**14,482**
Extraordinary items	19	—	—	—	—	—	—
Tax	(528)	(926)	(1,952)	(2,686)	(3,460)	(4,193)	(4,921)
Deferred tax	(9)	(76)	(3)	6	12	16	19
Minority interest	(117)	(58)	(227)	(263)	(306)	(351)	(396)
Net income	**2,153**	**2,373**	**3,647**	**5,136**	**6,400**	**7,850**	**9,184**
Recurring net income	**2,134**	**2,373**	**3,647**	**5,136**	**6,400**	**7,850**	**9,184**
Earnings per share (Rs)	**4.9**	**5.5**	**8.4**	**11.8**	**14.7**	**18.1**	**21.2**
Balance sheet (Rs mn)							
Total equity	21,286	26,181	28,687	32,216	36,613	42,006	48,317
Deferred tax balance	(148)	(75)	(72)	(78)	(91)	(106)	(125)
Minority interest	458	819	1,045	1,308	1,615	1,965	2,361
Total borrowings	4,901	3,226	2,226	274	0	0	0
Currrent liabilities	4,346	5,106	3,408	3,449	3,661	3,904	4,161
Total capital	**30,844**	**35,256**	**35,293**	**37,168**	**41,798**	**47,770**	**54,713**
Cash	1,286	955	3,150	3,909	7,311	11,988	17,609
Current assets	13,574	17,133	15,044	16,249	17,577	18,979	20,419
Net fixed assets	12,948	14,841	14,772	14,683	14,582	14,475	14,358
Investments	3,024	2,326	2,326	2,326	2,326	2,326	2,326
Deferred expenditure	12	2	2	2	2	2	2
Total assets	**30,844**	**35,256**	**35,293**	**37,168**	**41,798**	**47,770**	**54,713**
Free cash flow (Rs mn)							
Operating cash flow, excl. working capital	1,931	1,812	3,423	4,870	6,058	7,313	8,390
Working capital	(3,950)	(486)	390	(1,164)	(1,115)	(1,159)	(1,184)
Capital expenditure	(383)	(460)	(200)	(200)	(200)	(200)	(200)
Investments	418	(4,289)	—	—	—	—	—
Other income	488	469	723	812	937	1,179	1,488
Free cash flow	**(1,496)**	**(2,954)**	**4,336**	**4,318**	**5,679**	**7,133**	**8,494**
Revenue model (Rs mn)							
Advertising	6,566	7,035	9,354	10,575	12,084	13,745	15,458
Subscription-domestic	2,742	3,064	3,682	4,587	5,715	6,790	7,791
Subscription-overseas	3,030	3,933	4,202	4,377	4,505	4,701	4,905
Subscription-cable	978	—	—	—	—	—	—
Others	3,227	1,127	670	703	737	773	811
Total revenues	**16,544**	**15,159**	**17,907**	**20,242**	**23,041**	**26,010**	**28,966**

Source: Kotak Institutional Equities estimates.

Banking

Sector coverage view	Attractive

Company	Rating	Price, Rs 12-Oct	Target
SBI	L	1,862	1,450
HDFC	L	2,471	1,700
HDFC Bank	L	1,431	1,300
ICICI Bank	OP	1,053	1,200
Corp Bk	L	371	360
BoB	-	311	-
PNB	OP	512	610
OBC	L	227	240
Canara Bk	L	266	250
LIC Housing	OP	229	240
Axis Bank	U	743	570
IOB	OP	132	150
Shriram Transp	OP	220	200
SREI	L	121	110
MMFSL	L	237	265
Andhra	OP	89	120
IDFC	L	177	120
PFC	U	212	150
Centurion Bank	U	45	35
Federal Bank	OP	379	340
J&K Bank	OP	707	875
India Infoline	U	991	670
Indian Bank	L	150	135

ICICI Bank and SBI reduce rates on special deposit schemes, a positive for margin

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- **ICICI Bank and SBI cut deposit rates**
- **Higher liquidity and slowdown in credit offtake key reasons**
- **Banks with bulk deposits, lower CASA, higher leverage to benefit**

As mentioned in our note dated October 3, 2007 titled *'Higher liquidity increases the possibility of a deposit rate cut'*, both ICICI Bank and SBI have announced cuts in their deposit rates. ICICI Bank has cut rate on its special deposit schemes (390 day, 590 day and 890 day) by 50 bps while SBI has cut the rate on its special deposit scheme by 25 bps to 9%. Both banks appear have also cut their lending rate on new housing loan schemes by 50 bps. The impact of this cut should therefore be net positive on margin for the banks as the rate cut applies on new loans and not the existing book. As stated in our previous note we believe banks will cut lending rates as well but with a lag and to a lesser extent than deposits. The excess liquidity in the system along with slowdown in credit demand (latest data indicates further slowdown in credit offtake to 22%), is likely leading to this move. We expect other banks to follow. We maintain our positive stance on ICICI Bank, PNB, IOB Andhra BoB and Federal, all rated OP. Among banks not on our Outperform rating, OBC may benefit given its high leverage and low CASA ratio.

Strategy

Sector coverage view	N/A

A week is a long time in politics; mid-term -election chances recede

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- **Political power wins over nuclear power**
- **Government backs down in confrontation with Left Parties on India-USA nuclear deal**
- **Coalition politics and its 'compromise' economic agenda to continue for some time**

The Congress (I) leadership appears to have decided against early national elections perhaps pressured by its other senior leaders and members of the ruling coalition United Progressive Alliance (UPA) government. In a dramatic turnaround from its stance of a week ago, the UPA chairperson and the prime minister stated that they are not in favor of early national elections and would prefer the government complete its normal term of five years. We assume that the government is willing to sacrifice the India-USA civil nuclear cooperation deal in the process. More important, the development may have further compromised the government's stance versus the Left Parties. As such, we doubt the government would be in a position to push through major economic and social reforms during the remaining period (about 18 months) of the current parliament.

Political power versus nuclear power

The sudden about-turn by the Congress (I) leadership on the India-USA nuclear cooperation issue probably means that the nuclear deal is unlikely to proceed in its current form. The UPA chairperson and prime minister have expressed hope that the government can work with the Left Parties on the issue. However, we note that the Left Parties have been very adamant on the issue and we are doubtful that the government can get the support of the Left Parties on the issue.

Outcome of Gujarat state assembly elections may decide the future course of action

We expect the government to potentially review its ‘off-on’ view on national elections after the forthcoming state assembly elections in Gujarat in December 2007. If the Congress does well in this opposition-ruled state (a stronghold of the BJP), it may be emboldened to pursue elections. However, this looks unlikely given the popularity of the ruling BJP government.

We expect the government to present a normal union budget in February 2008. However, the budget is unlikely to contain any path-breaking economic proposals and will likely have populist measures to bolster the government’s popularity. It has already started the process with the announcement of a series of social packages recently——(1) National Rural Employment Guarantee Scheme extended to all 604 districts from 330; (2) Rashtriya Swastha Bima Yojna (health insurance) for unorganized sector workers; (3) extension of midday meal scheme to upper-primary students; (4) increase in dearness allowance to central government staff; (5) National Old Age Pension Scheme eligibility criteria changed to include more families; and (6) sharp increase in the minimum support price for rice and wheat to be purchased for government stock from farmers.

There's never a dull day in Indian politics

Forthcoming state assembly elections

State	Expected election schedule
Gujarat	Dec-07
Tripura	Feb-08
Nagaland	Feb-08
Meghalaya	Feb-08
Himachal Pradesh	Feb-08
Rajasthan	Dec-08
Mizoram	Dec-08
Madhya Pradesh	Dec-08
Delhi	Dec-08
Chhattisgarh	Dec-08

Source: Election Commission of India, Kotak Institutional Equities estimates.

Economy

Sector coverage view	N/A

Industrial output up, inflation down—RBI could train guns on asset prices, but can RBI disrupt figure skating and stadia building?

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- **IIP for the month of August jumps to 10.7% from 7.1% last month; confirms no slowdown as yet**
- **Headline inflation for week-ended Sept. 29,'07 drops to 3.26% from 3.42% last week on account of fall in prices of manufacturing products**
- **New numbers imply that investment boom continues**
- **RBI could train guns on SENSEX-Nifty figure skating—not cut policy rates and raise CRR by 50 bps**

August IIP a positive surprise

IIP for the month of August came a positive surprise. We had earlier maintained that the July IIP could be more of an aberration than a cyclical slowdown in industrial growth. The Aug '07 IIP growth could be close to 9.5%, reaffirming our viewand indeed, surpassing expectations.

Industrial growth remains robust with capital goods growing at a whopping 30% in August. Consumer durables sector, however, appear to have been hit with a 6.2% dip this month. Elevated industrial growth in August was also aided by strong base effects for mining sector, which jumped 17.1% this month against an average growth of 2.1% in preceding fourth months. However, manufacturing, which accounts for nearly 80% of the weight in the IIP, has maintained a double digit growth trajectory so far.

Inflation drops further, but could rise somewhat from November

Headline inflation rate for the week-ended Sep 29, '07 dropped to 3.26% from 3.42% last week. The fall has come about from manufacturing inflation, which has dropped to 4.23% from 4.52% last week, indicating that demand side pressures are presently contained. We expect that softening of primary articles inflation, contained manufacturing inflation, coupled with Government's clear communication on freezing oil prices, are big positives which would offset much of the base effects ahead arising from flat indices last year. However, development-related spending in the run up to elections in FY2009 could exert some pressures ahead. Along with the base effects arising from flat indices from November 2006, inflation could start rising moderately. The RBI's medium-term comfort level of 4.0-4.5% could be met in FY2008 itself.

New numbers imply that investment boom continues

New IIP numbers implies that the investment boom continues. Capital goods production has risen by 30% in August and 21% in the first five months of FY08. The investment cycle in Indian economy began its uptrend in 2002-03 and has been unprecedented in length and size. Last year top 1000 odd corporates had fixed investments exceeding Rs.2000 bn. (about US$50 bn). They also came up with new projects that year with fixed investments of about US$ 70 bn. planned over the next few years. In FY08 corporate fixed investment is expected to top that of last year.

However, the central bank's discomfort with the present investment boom has been that unduly large money is flowing into real estate activities resulting in elevated asset prices in stock and real estate market. In consultation with the Ministry of Finance, it has already come down hard on External Commercial Borrowings (ECBs). It is now concerned that over last two years close to half of FDI has come into real estate, construction and business services and manufacturing accounts for just 23%. Portfolio flows through the FII route have been unmanageable from the macroeconomic point of view with over US$16 bn having come in this FY so far of which US$7.5 bn has come in less than a month after the US Fed cut its policy rate on Sept. 18,'07. Indian economy has not seen this size of inflows ever before. The central bank knows that with an open capital account and compulsions to defend rupee which has already seen over 9% nominal appreciation this FY, the monetary policy efficacy has declined. Interest rates have softened on the back of large interventions estimated at about US$35 bn so far in FY08 (firm data for first five months places it at US$23 bn). However, it fears that any rate cut could lead to further sharp fall in interest rates in the near term. It also knows that far too much of global liquidity surpluses are now reflected in Indian money market surpluses.

RBI may seek to disrupt figure skating, stadia building

In this backdrop, the central bank would:

- Shy way from easing monetary policy and retain policy rates (repo and reverse repo at present levels). While, the Ministry may encourage central bank to cut repo rate to contain its cost of sterilization, the central bank is likely to see this as a confusing monetary policy signal and one which is likely to further fuel asset prices. A repo rate cut could soften gilt yields in the MSS tenor segment. But it could also lead to CP, Cd rates falling and then transmitting to the lending side rates.
- Training its guns on asset prices, RBI may raise CRR by 50 bps to kill the short-term hot flows presently entering the Indian stock and real estate markets. However, while the move may in short run raise bank lending costs, is unlikely to arrest the trend of softening interest rates over the FY. A 50 bps CRR hike would only mop up about Rs. 170 bn from primary liquidity. This is equal to the net FII investment in the first seven trading days this month. It may also trigger the much needed correction in the equity market, especially if the monetary measures are backed by prudential measures like further increase in risk weights. But if only monetary measures trigger occur, the equity markets could rebound quickly in the second half of Nov. Neverthless, RBI may still like some breathing space and slowdown the SENSEX-Nifty figure skating in which each appear to be lifting the other, while the real estate companies make merry building more stadia than the spectator demand.

Exhibit 1: Industrial Growth (based on IIP)

	Mining (10.47)		Manufacturing (79.36)		Electricity (10.17)		General (100.00)	
Month	2006-2007	2007-2008	2006-2007	2007-2008	2006-2007	2007-2008	2006-2007	2007-2008
Aug	-1.7	17.1	11.9	10.4	4.1	9.2	10.3	10.7
Apr-Aug	3.0	5.4	12.2	10.3	5.7	8.3	11.0	9.8

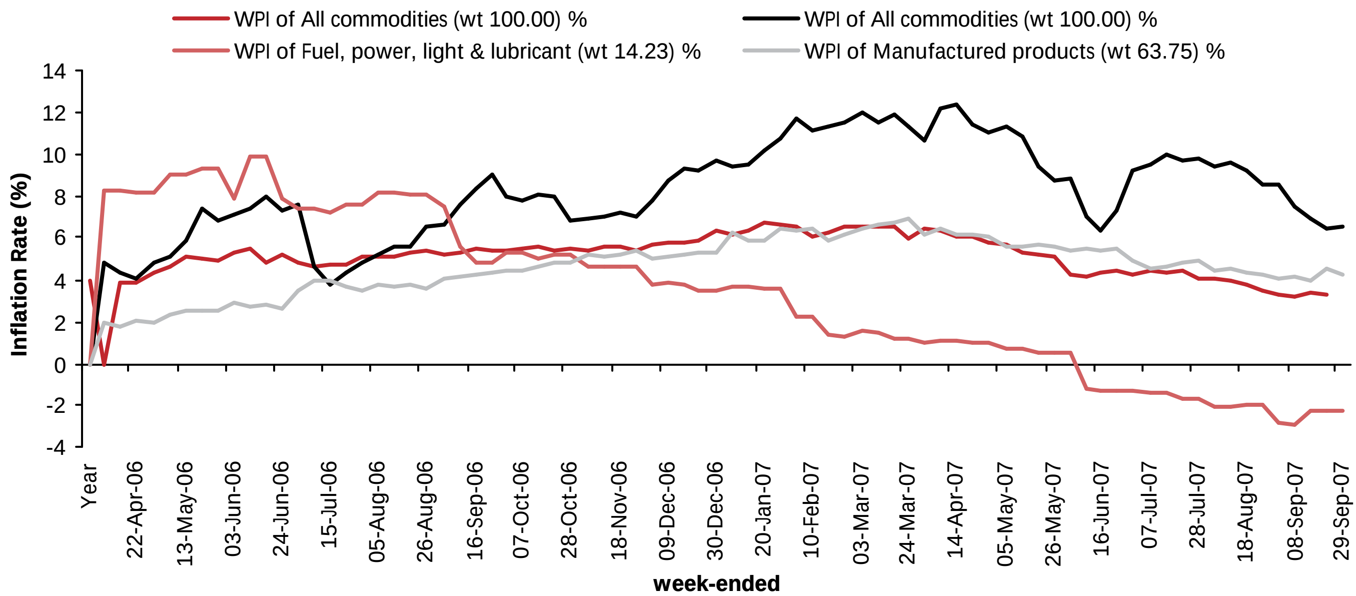
Source: Office of t

Exhibit 2: Industrial Growth (based on use-based IIPs)

Month	Basic goods (35.57)		Capital goods (9.26)		termediate goo (26.51)		Consumer goods (28.66)		Consumer durables (5.37)		Consumer non-durables (23.30)	
	2006-2007	2007-2008	2006-2007	2007-2008	2006-2007	2007-2008	2006-2007	2007-2008	2006-2007	2007-2008	2006-2007	2007-2008
Aug	4.8	13.3	16.6	30.0	8.7	12.3	15.0	0.5	19.0	-6.2	13.6	3.2
Apr-Aug	8.3	10.0	19.5	21.3	10.4	9.3	11.4	6.2	16.1	-2.3	9.8	9.3

Source: Office of

Exhibit 3: WPI of Primary articles (wt 22.03)



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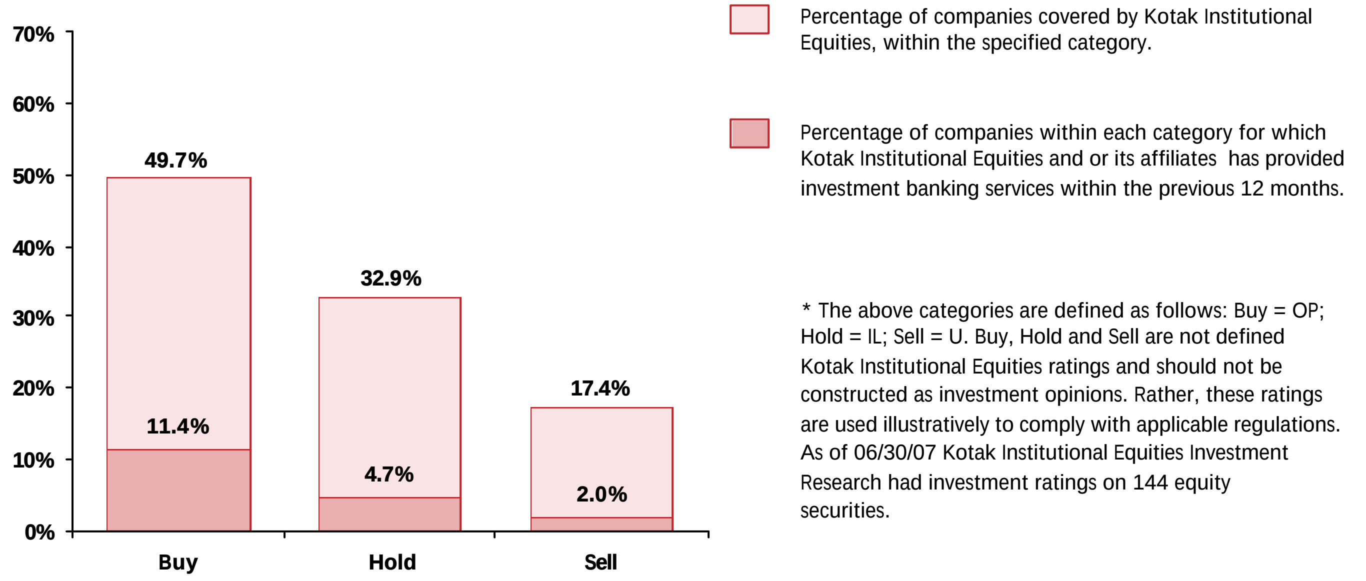

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Source: Kotak Institutional Equities. As of June 30, 2007

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