30 July 2007 | 5 pages

Unitech (UNTE.BO)

Sell: Strong 1Q FY08, but No Surprises

- Strong growth, but below estimates — Unitech's standalone 1Q FY08 revenue and earnings recorded strong growth in 1Q, with volumes pre-sold at higher price realizations early on, now recognized in 1Q FY08. On a consolidated basis revenues and earnings were higher, but 10% lower than our estimates. Traditionally, this is a weak quarter as residential project sales are slow.

- Significant margin expansion — Standalone EBITDA margins grew 36ppts yoy to 64%, while consolidated margins were lower at 58%. Sale of high-end products, some commercial projects and increased consultancy fees contributed to this. With new residential project launches in Kolkatta, Gr.Noida, where price realizations are lower, we believe margins will decline to ~50% by FY08-09E.

- New developments — 1) Construction is on-going at 50m sq.ft of development, 2) The Grande, a premium luxury project was launched in Noida - 500 units of 2400-3000 sq.ft units in phase I for Rs.7250/sq.ft, 2) new projects in Kolkatta, Gr.Noida were launched; 3) plans for 28 hotels – 5000 rooms, across key cities.

- Market conditions still tough — 1) Pre-sale volumes are down significantly, particularly in NCR, 2) primary sale prices are stagnating, but secondary-market prices are down 15-20% across markets; and 3) potential supply risk remains.

- Maintain Sell/Medium Risk — While Unitech's scale, low-risk/high return model deserves 10% premium, with stock already trading at 37% premium to our NAV of Rs391, upside looks priced in. Valuations do not leave any margin for error from potential execution delays; as a result risk/reward looks unfavorable.

Sell/Medium Risk	3M
Price (30 Jul 07)	Rs536.80
Target price	Rs430.00
Expected share price return	-19.9%
Expected dividend yield	0.1%
Expected total return	**-19.8%**
Market Cap	Rs435,714M
	US$10,786M

Figure 1. Consolidated Statistical Summary

Year to 31-Mar	Net Profit (Rs. bn)	EPS (Rs.)	P/E (x)	ROCE (%)
FY05	0.3	0.4	nm	11%
FY06	0.8	1.0	nm	12%
FY07E	11.2	13.7	39.1	46%
FY08E	16.4	20.2	26.6	34%
FY09E	27.5	33.9	15.8	37%

Source: Citigroup Investment Research estimates

Figure 2. 1Q Earnings Summary

Rs in Mn	Standalone			Consolidated
	1QFY07	1QFY08	YoY	1QFY08
Net Sales	2677.6	7636.6	185%	8655.9
EBITDA	760	4911.8	546%	5005.4
Margin	28%	64%		58%
Interest	158.5	688.6	334%	600.8
Other Inc	384.5	250.7	-35%	340.8
Depreciation	9.5	13.4	41%	31.6
PAT	739.2	3478.3	371%	3667.4

Source: Company Reports, CIR

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See Appendix A-1 for Analyst Certification and important disclosures.

[1]Citigroup Global Markets India Private Limited

Unitech

Company description

Unitech is one of India's largest, most diversified real estate developers with an emerging pan-India presence. It enjoys leadership in markets of NCR and Kolkata. Its core strengths of land acquisition, reputation in building townships and relationships with governments and customers have enabled it to build a diversified portfolio. Unitech has a land bank of 10,761 acres with a total saleable area of ~490m sq.ft. spread over Chennai (24%), NCR (20%), Kolkata (19%) and Tier III cities (32%). Residential projects account for about 66% of the saleable area, commercial 6%, IT Parks 6% and retail 6%. In addition, it also has a small presence in power transmission, prefabricated construction, paving block and ready mix concrete. The promoter family holds a 75% stake in the company.

Investment thesis

We rate Unitech Sell/Medium Risk (3M). Recent efforts to monetize 6 of its IT parks by selling stakes to a REIT has provided it with healthy cash flows — more such structures are expected. Additionally, initiatives to reduce concentration in NCR and introduce new revenue streams from lease/management fees look positive. That said, management's development plan of ~490mn sq.ft. is aggressive and does raise execution risks, in our view. We forecast exponential growth in profitability in FY07-09E. Valuations, however, would be determined on NAV value, rather than profitability, in our view. With stock already at a premium to estimated NAV, risk/reward looks unfavorable.

Valuation

Our target price of Rs430 is based on a 10% premium to our NAV value of Rs391 (excluding SEZs). The premium is attributed to: 1) Unitech's competitive advantage of large diversified land bank, while peers are still aggregating land; 2) a dynamic business model with thrust on recycling capital faster; and 3) strong brand positioning and proven track record. Our assumptions are: a) current market price levels to sustain with no price inflation; b) development volume of 471m sq.ft (~19mn recognized as revenue in FY07); c) all projects undertaken will be completed largely as per schedule though given the scale of the roll-out, we expect risk of delays; d) average cost of capital of 14%; e) tax rate of 28%; and f) does not include any value attributed towards SEZs.

Risks

We rate Unitech Medium Risk. This is different from the High Risk rating assigned by our quantitative risk-rating system which measures the stock's volatility over a 260-day period. We rate Unitech shares Medium Risk based on: 1) low-risk/high-return business model; 2) pan-India land bank with initiatives to reduce weighting on NCR; 3) relatively healthy cash flows. Main company-specific upside risks include: 1) Developments on monetization of retail and hotel assets similar to IT Parks, could result in healthy cash flows and should positively drive profitability and valuations; 2) While we have not factored the value of the SEZs, any developments providing higher visibility on execution of these project is likely to create long-term value; 3) Any interest rate reversals, would positively impact earnings growth assumption. If any of these risk factors plays out, Unitech's share price may continue to trade above our target price.

Appendix A-1

Analyst Certification

We, Ashish Jagnani and Aditya Narain, CFA, research analysts and the authors of this report, hereby certify that all of the views expressed in this research report accurately reflect our personal views about any and all of the subject issuer(s) or securities. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

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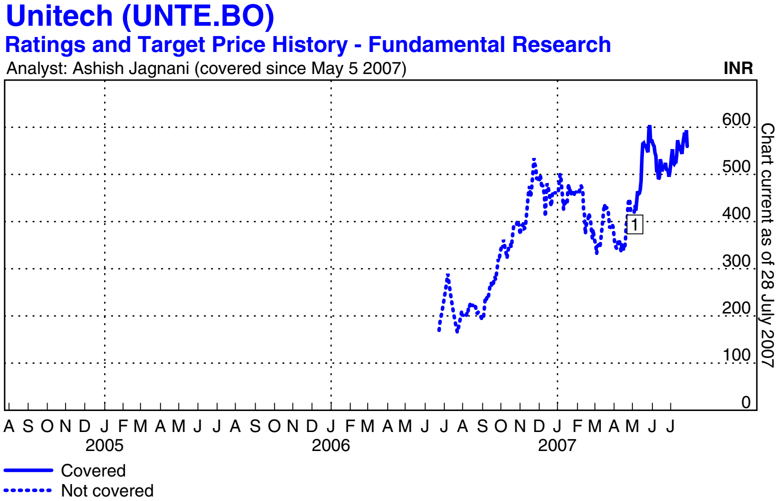

#	Date	Rating	Target Price	Closing Price
1:	4 May 07	3M	430.00	432.15

*Indicates change.

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