

We conducted a study to search top dividend yield stocks across the BSE 500 universe and the results were interesting. Traditionally, high dividend yield stocks, are considered 'Safe Havens' and are preferred by a particular sect of investors. This happens more so when equity markets are in a bearish phase and growth stories are scarce. However, the pertinent questions to ask before buying are whether such high dividend yield stocks can sustain current level of dividends and are they insulated from capital loss (attractively priced on fundamentals). To make it a single question, are they a Value Buy or a Value Trap? Though we started with the intention of searching for recommendable 'Value Buys', we ended with concluding most of them as 'Value Traps'.

The screening methodology we followed was simple. From the broad universe of BSE 500, we tried to select the most appropriate sample by keeping different hurdle rates of dividend yields for different capitalizations. We used hurdle rates of 3.5%, 4.5%, 5.5% and 6.5% for companies belonging to Category I (M-Cap >Rs50bn), Category II (M-Cap Rs30-50bn), Category III (M-Cap Rs10-30bn) and Category IV (M-Cap <Rs10bn) respectively. By doing this, we have evened out, to an extent, the risk-reward in the selection. Therefore, our results are not skewed towards smaller capitalization stocks (which are inherently risky), unlike others.

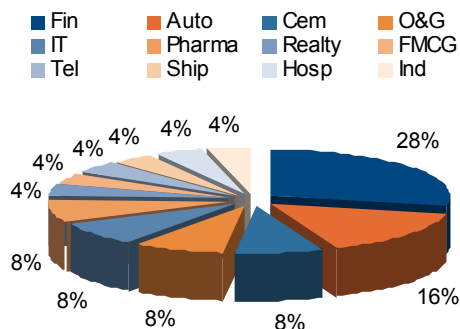
Selected Universe

Category	M-Cap (Rs bn)	Div Yield Hurdle Rt (%)	No. of Comp	Companies
I	>Rs50bn	3.5	8	Indiabulls Real, Ambuja Cements, MTNL, Canara Bank, Bajaj Auto, Tata Motors, ACC, HCL Tech
II	Rs30-50bn	4.5	4	Syndicate Bank, Ashok Leyland, Castrol, Chennai Petro
III	Rs10-30bn	5.5	9	Bongaigaon Ref, Varun Ship, Andhra Bank, HCL Info, Wyeth, Bk of Mah, Wochardt, Vijaya Bank, Allahabad Bank
IV	<Rs10bn	6.5	4	Royal Orchid, GIC, Ador Welding, Mirc Electronics

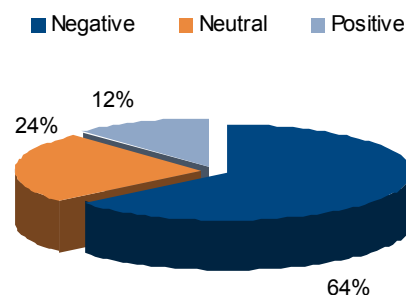
Source: India Infoline Research, Bloomberg, Capitaline, NSE, Annual Reports

After the selection, we addressed two important questions; is the high dividend yield due to fundamental mispricing of the security and would the current level of dividend be sustained. To assess, we relied on, earnings growth of the latest quarter, dividend history and fundamental outlook for each company. **About 60% (15 companies) of the 25 companies selected have reported significant yoy decline in profits in the latest quarter. Almost 64% (16 companies) of the selection belonged to sectors such as Financials, Auto, Cement, Realty and IT where our fundamental view is negative. Except IT, all of them are cyclicals facing difficult business conditions due to slowing economic activity.** Only 12% (3 companies) companies belong to sectors such as Telecom and Oil & Gas where we have a positive view. Majority of the companies (14 companies) have been a stable dividend (absolute DPS) payer, but to a great extent aided by the strong economic growth in the last 3-4 years.

Sector-wise break-up of selection



House view on the sectors featured



Source: India Infoline Research, Bloomberg, Capitaline, NSE, Annual Reports

Clearly, most of these high dividend yield stocks are 'Value Traps', often difficult to discern from outside. Fundamentally, they face multiple earnings headwinds and should continue to carry a high dividend yield. The probability of making a capital loss is high from holding them and that can easily offset the returns in the form of dividends. **However, there are a couple of exceptions that one can consider – Chennai Petro and HCL Tech (Q4 F6/08 PAT decline attributable to forex accounting). We are also fundamentally bullish on these stocks.**

Key Table

Category I - Above Rs50bn market cap									
Company	CMP (Rs)	M-Cap (Rs mn)	DPS FY08 (Rs)	Div Yield (%)	Hurdle Rt (%)	OPF** (%)	June Qtr - yoy PAT grth*	Company Outlook	Dividend History
Indiabulls Real	283	72,956	13.5	4.8	3.5	1.3	(4.0)	Negative	-
Ambuja Cements	80	121,803	3.5	4.4	3.5	0.9	(35.1)	Negative	Increasing
Canara Bank	201	82,308	8.0	4.0	3.5	0.5	(49.0)	Negative	Stable
MTNL	102	64,040	4.0	3.9	3.5	0.4	15.1	Neutral	Stable
Bajaj Auto	532	76,950	20.0	3.8	3.5	0.3	(7.5)	Negative	-
ACC	559	104,925	20.0	3.6	3.5	0.1	(22.7)	Negative	Increasing
HCL Tech	223	148,360	8.0	3.6	3.5	0.1	(20.4)	Positive	Stable
Tata Motors	427	164,805	15.0	3.5	3.5	-	(34.1)	Negative	Stable

Category II - Between Rs30-50bn market cap									
Company	CMP (Rs)	M-Cap (Rs mn)	DPS FY08 (Rs)	Div Yield (%)	Hurdle Rt (%)	OPF** (%)	June Qtr - yoy PAT grth*	Company Outlook	Dividend History
Castrol India	304	37,587	15.5	5.1	4.5	0.6	25.6	Neutral	Increasing
Syndicate Bank	57	30,102	2.8	4.9	4.5	0.4	(60.3)	Negative	Stable
Ashok Leyland	31	41,706	1.5	4.8	4.5	0.3	(41.7)	Negative	Increasing
Chennai Petro	268	33,938	12.0	4.5	4.5	-	117.6	Positive	Increasing

Category III - Between Rs10-30bn market cap									
Company	CMP (Rs)	M-Cap (Rs mn)	DPS FY08 (Rs)	Div Yield (%)	Hurdle Rt (%)	OPF** (%)	June Qtr - yoy PAT grth*	Company Outlook	Dividend History
Bongaigaon Refinery	56	11,169	5.0	8.9	5.5	3.4	37.8	Neutral	Stable
Andhra Bank	55	26,528	4.0	7.3	5.5	1.8	(44.9)	Negative	Stable
Varun Shipping	69	10,320	5.0	7.3	5.5	1.8	(83.2)	Neutral	Stable
HCL Infosys	115	19,755	8.0	7.0	5.5	1.5	(52.1)	Negative	Stable
Wyeth	444	10,091	30.0	6.8	5.5	1.3	7.3	Neutral	Stable
Bank of Maharashtra	34	14,659	2.0	5.9	5.5	0.4	(14.2)	Negative	Stable
Wockhardt	198	21,635	11.3	5.7	5.5	0.2	1.2	Neutral	Increasing
Allahabad Bank	62	27,896	3.5	5.6	5.5	0.1	(53.2)	Negative	Stable
Vijaya Bank	37	15,888	2.0	5.5	5.5	-	(168.8)	Negative	Stable

Category IV - Below Rs10bn market cap									
Company	CMP (Rs)	M-Cap (Rs mn)	DPS FY08 (Rs)	Div Yield (%)	Hurdle Rt (%)	OPF** (%)	June Qtr - yoy PAT grth*	Company Outlook	Dividend History
Royal Orchid	79	2,154	6.0	7.6	6.5	1.1	10.9	Neutral	Stable
GIC	54	2,907	4.0	7.4	6.5	0.9	18.5	Negative	Increasing
Ador Welding***	129	1,759	8.0	6.2	6.5	(0.3)	1.7	Positive	Decreasing
Mirc Electronics***	16	2,314	1.0	6.1	6.5	(0.4)	11.2	Neutral	Increasing

Source: India Infoline Research, Bloomberg, Capitaline, NSE, Annual Reports

*Consolidated numbers wherever available; **OPF - Outperformance; *** Despite missing the hurdle rate, Ador Welding and Mirc Electronics have been included in Category IV as we wanted at least four companies in each category.

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