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News Round-up

- ▶ NTPC (NATP IN) is hopping to raise its installed capacity to 128 gigawatts (gw) by 2032 from the current level of 32 GW planned in the long term. The company has targeted a share of 16% in gas-based power generation capacity. *(FNLE)*
- ▶ Glenmark Pharmaceuticals (GNP IN) said it had entered into an agreement with Sepracor, which could pave way for the Indian firm to launch generic eszopiclone tablets, used in treating insomnia, in the US market. *(BSTD)*
- ▶ BHEL (BHEL IN) said it had bagged a contract worth USD 549 mn from Abhijeet Infra for setting up a 1,080 Mw thermal power plant in Jharkhand. *(BSTD)*
- ▶ Dr Reddy's Laboratories (DRRD IN) launched Cresp, the first generic version of darbepoetin alfa in the world and the only darbepoetin alfa in India. *(BSTD)*
- ▶ Bajaj Auto (BJAUT IN) will re-enter the segment which gave it the identity of a performance motor-cycle maker, with the launch of a range of high-end Pulsars planned for next year. *(BSTD)*
- ▶ M&M (MM IN) is likely to put a bid of around USD 480mn for acquisition of the South Korean SUV maker SsangYong Motor co. as part of its plan to establish itself as a global SUV co. *(ECNT)*
- ▶ Tata Power (TPWR IN) that is locked in a bitter battle with competitor Anil Ambani led Reliance Infra (RELI IN) & the Maharashtra govt., received a shot in the arm after the Bombay High Court allowed it to approach the central regulatory agency against the State Load Dispatch Centre. *(ECNT)*
- ▶ Lupin (LPC IN) sues Ranbaxy (RBXY IN) for patent infringement. *(BSTD)*
- ▶ Coal India files IPO papers with Sebi. CIL alone accounts for over 80% of the country's coal output. *(BSTD)*
- ▶ GMR Airports Holding Ltd plans to raise around USD 100 mn to buy out the holdings of its parent, GMR Infrastructure (GMRI IN), in the airports business. *(BSTD)*
- ▶ MindTree (MTCL IN) eyes USD 1 bn revenue by 2014. *(FNLE)*
- ▶ Omnitech Info Solutions (OMIS IN) is likely to complete acquisition of a Netherlands company for USD 15 mn in the next one-two months. *(FNLE)*
- ▶ Allahabad Bank (ALBK IN) to raise USD 304 mn debt. *(FNLE)*

Source: ECNT= Economic Times, BSTD = Business Standard, FNLE = Financial Express, THBL = Business Line.

EQUITY MARKETS

India	Change %			
	9-Aug	1-day	1-mo	3-mo
Sensex	18,288	0.8	2.5	5.5
Nifty	5,486	0.9	2.5	5.6
Global/Regional indices				
Dow Jones	10,699	0.4	4.9	(0.8)
Nasdaq Composite	2,306	0.8	5.0	(2.9)
FTSE	5,411	1.5	5.4	0.4
Nikkie	9,632	0.6	0.5	(8.5)
Hang Seng	21,802	0.6	7.0	6.7
KOSPI	1,785	(0.3)	3.6	6.4
Value traded – India				
Cash (NSE+BSE)	172		172	169
Derivatives (NSE)	591		663	1,033
Deri. open interest	1,522		1,387	1,244

Forex/money market

	Change, basis points			
	9-Aug	1-day	1-mo	3-mo
Rs/US\$	46.1	(2)	(54)	127
10yr govt bond, %	7.8	(1)	16	18
Net investment (US\$mn)				
	6-Aug		MTD	CYTD
FIs	180		530	11,007
MFs	(70)		(66)	(282)

Top movers -3mo basis

Best performers	Change, %			
	9-Aug	1-day	1-mo	3-mo
HPCL IN Equity	446.1	0.5	(8.7)	35.4
BOI IN Equity	438.7	0.9	17.2	31.2
BHFC IN Equity	344.7	2.6	4.4	30.1
BJAUT IN Equity	2705.3	(0.2)	11.7	27.5
APNT IN Equity	2661.7	2.1	11.6	25.7
Worst performers				
PUNJ IN Equity	120.2	(0.0)	(13.3)	(22.4)
RNR IN Equity	39.7	0.8	(11.6)	(20.9)
SUEL IN Equity	56.7	1.3	(3.6)	(18.8)
FTECH IN Equity	1211.1	(1.7)	(11.3)	(14.9)
ABAN IN Equity	912.4	0.7	5.1	(14.9)

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AUGUST 09, 2010
INITIATING COVERAGE

Coverage view: **Attractive**

Price (Rs): **120**

Target price (Rs): **140**

BSE-30: **18,288**

Niche blazer. Continuing good growth in Parachute, likely faster growth in Saffola and scaling-up of international operations are key drivers for Marico over FY2010-13E. We are positive about the company's ability to grow its core business and reposition Kaya (from 'cure' to 'care') to address consumer perception issues. Indians associate hair oil usage with nutrition and hence it is early days to worry about product substitution risk from conditioners etc., in our view. Recommend ADD.

Company data and valuation summary

Marico

Stock data

52-week range (Rs) (high,low)	137-78
Market Cap. (Rs bn)	72.8

Shareholding pattern (%)

Promoters	63.5
FIs	22.9
MFs	4.9

Price performance (%)

	1M	3M	12M
Absolute	(8.8)	11.6	45.1
Rel. to BSE-30	(11.0)	2.3	20.3

Forecasts/Valuations

	2010	2011E	2012E
EPS (Rs)	4.5	5.4	6.4
EPS growth (%)	33.8	19.6	20.4
P/E (X)	26.7	22.3	18.6
Sales (Rs bn)	26.6	31.2	36.3
Net profits (Rs bn)	2.7	3.3	3.9
EBITDA (Rs bn)	4.2	4.9	5.7
EV/EBITDA (X)	17.5	14.9	12.2
ROE (%)	50.8	43.9	38.8
Div. Yield (%)	0.8	0.9	1.1

We like Marico for several reasons, hence our ADD rating and target price of Rs140

We arrive at a FY2012E target price for Marico at Rs140 based on 22XFY2012E EPS. We like the unique ability demonstrated by Marico in (1) building a strong domestic portfolio with good franchise value, (2) meaningfully differentiated offerings in the portfolio, (3) good pricing power, (4) presence in niche segments, (5) good growth opportunity in international markets and (6) successful inorganic growth track record.

21% PAT CAGR over FY2010-13E

With improving product diversification, we expect the proportion of coconut oil in the sales mix to decline. We forecast modest EBITDA margin improvement of 50 bps over FY2010-13E on the back of (1) slowing input cost inflation, (2) international business margins moving closer to domestic margins and (3) increasing contribution of value-added hair oils. We expect modest operating leverage and estimate PAT CAGR of 21% over FY2010-13E. Strong operating cash flows and moderate capex will likely drive 3X improvement in free cash over FY2010-13E.

Branding a commodity—a successful story

Marico has demonstrated successful new consumer recruitment in Parachute, having converted most from unbranded hair oil. We expect Saffola to benefit from rising income levels, growing awareness of lifestyle diseases and the opportunity for penetration-led growth. Its international business is strengthening its geographical distribution expansion and cross-pollination of products, which should help sustain good growth.

Key worry—entry into bigger categories key for incremental growth, hence higher risk

Marico dominates both the key segments in which it operates (coconut oil and high-end edible oil), regardless, its product pricing is closely linked to underlying commodity prices—implying likely timing mismatch in input costs and product pricing. Other worries include exposure to currency risk, a lack of meaningful success in new ventures, threat of decline in hair oil usage and increasing competition in core brands.

QUICK NUMBERS

- Moon chart analysis of Marico's portfolio
- 21% PAT CAGR over FY2010-13E

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Growth opportunity exists

Category	Potential growth	Market share	Comments
Coconut oil			Coconut oil is a highly penetrated category (>80%) with low category growth rate (~12%). To encourage consumers to convert from loose to branded oil, the company has reduced price of converter packs, introduced low unit packs and is promoting its low priced Nihar brand in price sensitive regions. We model 12% sales CAGR between FY2010-13E
Edible oil			Edible oil industry valued at Rs750 bn is under penetrated with 31% urban penetration and 9% rural penetration. Saffola positioned as a preventive for cardiac problems is synonymous with the category and has a market share of 7% in the edible oil market. Increasing health consciousness among consumers is aiding growth. We model 12% sales CAGR between FY2010-13E
Hair oil			Hair oil segment is growing at a much faster rate (~20%) than coconut oil. While Marico has made an entry in light hair oil, perfumed non-sticky oil and almond oil, it has not been able to replicate its success in coconut oil to this segment. We estimate sales CAGR of 15% between FY2010-13E
Functional food			Marico has entered the fast growing functional foods segment under the Saffola brand. This category is presently at a nascent stage and we expect Marico to benefit from early mover advantage as and when the category develops
Skin care services			Skin care services is a highly unorganised and fragmented market in India. Marico's entry under the Kaya brand has been well received in Middle East but has not met much success in India likely due to the high price point for the services offered and the 'problem solution' positioning that is associated with it. We estimate sales CAGR of 34% between FY2010-13E primarily led by the Middle East operations and the recent Derma Rx acquisition

Note:

(a) The above moon chart may be assessed on a scale of 0 to 1, where 0 is the lowest score and 1 is the highest score.



Denotes 0



Denotes 1

Source: Kotak Institutional Equities estimates

Where does Marico fit in our coverage universe?

Valuation - KIE FMCG coverage, March fiscal year-ends, 2010-12E

	Price	Rating	Target	Mkt. cap.	Upside	EPS growth (%)			P/E (X)		
	(Rs)		(Rs)			(Rs mn)	(%)	2010	2011E	2012E	2010
Marico	120	ADD	140	75,010	17	33.8	19.6	20.4	26.8	22.4	18.6
Asian Paints	2,662	BUY	3,000	255,310	13	85.3	24.4	20.4	37.2	29.9	24.8
Colgate-Palmolive (India)	846	REDUCE	830	115,104	(2)	44.2	10.9	14.6	27.2	24.5	21.4
Dabur India	202	REDUCE	210	174,861	4	28.1	17.6	20.8	34.8	29.6	24.5
GlaxoSmithKline Consumer (a)	1,824	ADD	2,000	76,709	10	23.6	23.9	18.6	33.0	26.6	22.4
Godrej Consumer Products	364	ADD	400	117,900	10	69.5	14.4	33.1	32.1	28.1	21.1
Hindustan Unilever	256	REDUCE	250	558,621	(2)	(0.9)	8.4	15.3	27.2	25.1	21.7
ITC	159	BUY	165	1,216,054	4	22.6	18.2	15.8	29.9	25.3	21.9
Jubilant Foodworks	461	REDUCE	370	29,457	(20)	340.6	75.7	24.6	83.3	47.4	38.0
Jyothy Laboratories (b)	280	NR	—	20,308	—	99.6	17.0	18.3	25.4	21.7	18.3
Nestle India (a)	2,791	REDUCE	3,000	269,077	7	27.0	16.4	20.9	37.5	32.2	26.6
Tata Global Beverages	113	ADD	125	69,786	11	23.4	11.1	13.8	17.0	15.3	13.5
Titan	2,818	ADD	3,000	125,089	6	29.3	45.6	32.2	49.2	33.8	25.6
KS universe		Attractive		2,976,025		24.2	16.4	17.5	30.3	26.1	22.2

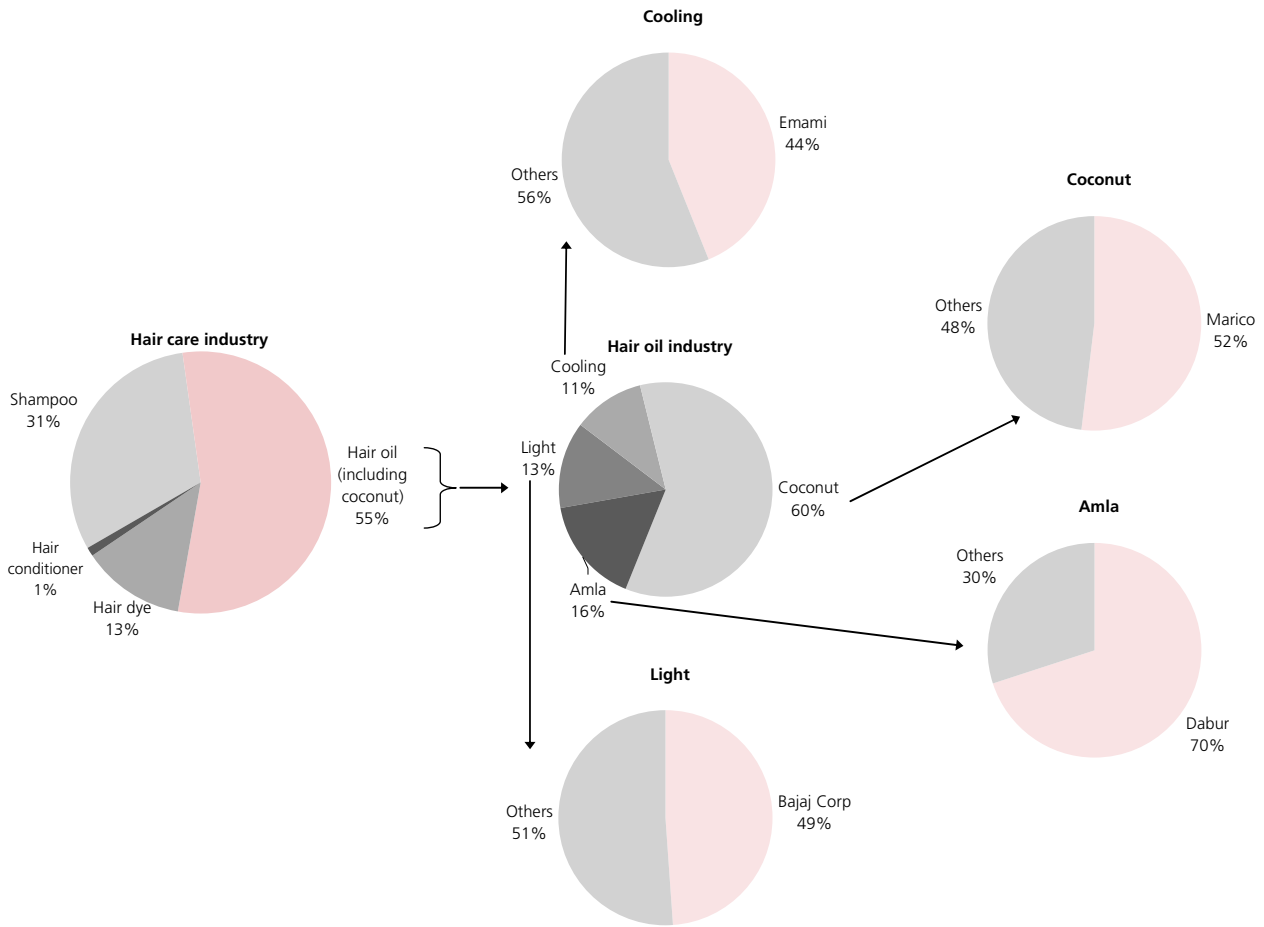
Note:

(a) 2010 calendar year means 2009, similarly 2011E and 2012E for these particular companies

(b) NR - Not Rated. Jyothy Laboratories is currently in the restricted list, hence we do not have a rating on the stock

Source: Kotak Institutional Equities estimates

Hair oil market is characterised by high entry barriers
 Structure of the hair oil market



Source: Kotak Institutional Equities

Marico has not achieved much success beyond its coconut oil and edible oil business

List of ventures/products that Marico has launched over the years

Year	New product / venture launched	Present status
FY2001	Sil	In 2008, the company divested its Sil brand to Good Food Group as it was unable to scale up the business
FY2002	Kaya	Kaya operations are yet to stabilize - weak economic environment, imposition of service tax and intense competition from the unorganized sector have hampered its growth. We believe that any further slowdown in Kaya operations will impact margins.
FY2003	Sundari LLC	Acquired Sundari LLC which was engaged in the manufacturing and marketing of skincare cosmetics and accessories in the USA and Europe. However due to lack of focus of Marico on the US market it divested it in FY2009.
FY2005	Parachute Sampoorna	Withdrew Parachute Sampoorna, a coconut oil with hibiscus and almond blend, due to lack of consumer acceptance
FY2007	Sparsh Baby Care Products	Withdrawn from the market due to poor response. The company could not break Johnson and Johnson's hold on the baby care market
	Parachute Advansed After Shower Hair Gels	Nationally launched. As this category is still at a nascent stage, overall contribution to sales mix is small
FY2008	Revive Liquid Stiffener	Revive was initially launched in powder form. The liquid stiffener was launched in response to Jyothy Laboratories's Stiff & Shine. Given, Marico's first mover advantage and Revive's strong brand equity, it managed to retain its market leadership
	Saffola Atta Mix	Nationally launched. However success has been muted
	Parachute Advansed Starz	Nationally launched
	Maha Thanda	Marked Marico's entry in the cooling oil segment but due to subdued response the product was not nationally launched
FY2009	Parachute Advansed Night Repair Cream	Still at prototype stage. Not launched nationally as yet
	Hair & Care Almond Gold	Not yet a success. We believe it will be difficult to encroach in the almond proposition, given Bajaj Corp's strong foothold in the market
	Parachute Advansed Revitalizing Hot Oil	Presently being marketed in North India
	Saffola Zest	Withdrawn from the market due to poor response at the test launch stage. The company plans to rework on the taste and flavour of the brand
FY2010	Parachute Aftershower Antidandruff Hair Oil For Men	Positioned as non-sticky hair oil for men with antidandruff properties. Consumer response, yet to be gauged
	Saffola Arise	Nationally launched

Source: Kotak Institutional Equities

Profit model, balance sheet, cash model of Marico, March fiscal year-ends, 2007-2013E (Rs mn)

	2007	2008	2009	2010E	2011E	2012E	2013E
Profit model							
Net revenues	15,569	19,050	23,884	26,608	31,234	36,287	41,617
EBITDA	1,986	2,462	3,040	4,045	4,684	5,485	6,526
Other income	102	67	65	183	190	238	262
Interest (expense)/income	(206)	(276)	(301)	(257)	(274)	(230)	(166)
Depreciation	(521)	(308)	(358)	(601)	(524)	(584)	(652)
Pretax profits	1,361	1,945	2,447	3,370	4,076	4,909	5,969
Tax	(372)	(360)	(409)	(643)	(815)	(982)	(1,194)
Net income	989	1,586	2,037	2,727	3,261	3,927	4,775
Earnings per share (Rs)	1.7	2.6	3.3	4.5	5.4	6.4	7.8
Balance sheet							
Total shareholder's equity	1,923	3,146	4,535	6,196	8,651	11,606	15,201
Total borrowings	2,510	3,579	3,750	3,750	3,250	2,250	2,000
Deferred tax liability	(1,152)	(982)	(641)	(641)	(641)	(641)	(641)
Minority interest	—	1	—	—	—	—	—
Total liabilities and equity	3,281	5,745	7,643	9,305	11,259	13,215	16,559
Net fixed assets	1,654	2,573	3,111	3,584	3,685	3,827	4,008
Goodwill	450	842	850	850	850	850	850
Investments	—	—	121	121	621	621	621
Cash	429	753	922	1,934	2,972	4,377	7,056
Net current assets	747	1,577	2,639	2,815	3,131	3,539	4,024
Total assets	3,281	5,745	7,643	9,305	11,259	13,215	16,559
Free cash flow							
Operating cash flow, excl. working capital	1,788	2,055	2,319	2,950	3,795	4,521	5,440
Working capital changes	(68)	(896)	(1,007)	(232)	(383)	(490)	(589)
Capital expenditure	(3,030)	(1,226)	(916)	(1,074)	(625)	(726)	(833)
Free cash flow	(1,310)	(67)	396	1,644	2,787	3,305	4,017
Ratios							
Net debt/equity (%)	108.2	89.8	62.4	29.3	—	cash	cash
Net debt/EBITDA (X)	104.8	114.8	93.0	44.9	5.9	(38.8)	(77.5)
Return on equity (%)	43.6	62.5	53.1	50.8	43.9	38.8	35.6
Book value per share (Rs)	3.2	5.2	7.4	10.2	14.2	19.1	25.0
ROACE (%)	27.8	40.6	34.9	34.6	34.6	34.3	33.7

Source: Kotak Institutional Equities estimates

AUGUST 10, 2010

RESULT

Coverage view: **Attractive**

Price (Rs): **59**

Target price (Rs): **65**

BSE-30: **18,288**

In line results; strong traffic growth and progress in projects. Reported revenues of Rs12.3 mn– broadly in line with estimates. Revenue growth was led by strong traffic growth in all three airports, start of commercial operations of terminal building at SGIA and Ulunderpet road project. Key developments during the quarter include (1) completed relocation process of GMR Energy, (2) achieves financial closure of two road projects and (3) successfully completed InterGen refinancing transaction. Reiterate ADD.

Company data and valuation summary

GMR Infrastructure

Stock data

52-week range (Rs) (high,low) 77-51

Market Cap. (Rs bn) 209.4

Shareholding pattern (%)

Promoters 74.9

FIs 8.9

MFs 0.4

Price performance (%)

Absolute (3.1) (7.6) (13.4)

Rel. to BSE-30 (4.8) (14.6) (27.6)

Forecasts/Valuations

	2010	2011E	2012E
EPS (Rs)	0.4	0.2	0.1
EPS growth (%)	(43.8)	(48.9)	(40.0)
P/E (X)	132.5	259.4	431.9
Sales (Rs bn)	45.7	44.5	47.2
Net profits (Rs bn)	1.6	0.8	0.5
EBITDA (Rs bn)	13.6	20.7	22.6
EV/EBITDA (X)	23.4	15.1	14.1
ROE (%)	2.4	1.2	0.7
Div. Yield (%)	0.0	0.0	0.0

In line results-high other income leads to PAT-level outperformance; closes InterGen refinance

GMRI reported revenues of Rs12.3 bn, up 4.6% yoy, slightly higher than our estimate of Rs11.6 bn. Start of commercial operations of Ulunderpet road project, increase in traffic levels at all three airports, and start of operations of the new terminal building at Turkey airport led revenue growth in the quarter. High other income of Rs672 mn (driven by forex gains of Rs260 mn) led to net PAT of Rs318 mn versus our estimate of a net loss of Rs487 mn in the quarter.

GMR successfully completed the refinancing transaction of US\$737 mn of short-term debt for the InterGen acquisition. The remaining US\$100 mn (ff the total US\$837 mn of debt) was infused as equity from GMR. Total equity investment of GMR in InterGen now stands at US\$300 mn.

Segment highlights: Airport traffic growth, power project relocation, road project financial closures

- ▶ **Airports segment:** Strong airport segment revenue growth of 32.4% yoy to Rs4.25 bn was primarily led by (1) strong traffic growth at Delhi and Hyderabad airport of about 19-20%, (2) start of commercial operations of the new terminal building at the Turkey airport and (3) very strong passenger traffic growth of 93% yoy at the Turkey airport.
- ▶ **Power segment:** GMRI reported 7% yoy decline in power revenues in 1QFY11 as the GMR Energy plant was out of operation for relocation. The management has cited completion of the relocation process and the plant has started operations from July 2010 -- it should contribute to revenues from 2QFY11. Power segment PAT boosted higher other income due to high treasury income in GMR Energy.
- ▶ **Roads segment:** GMRI reported a strong roads segment revenue growth of 28.7% yoy led by start of commercial operations of the Ulunderpet highway project. GMRI has achieved financial closure for Hyderabad-Vijaywada (already commenced construction operations) and the Chennai outer ring road projects. GMRI is also close to achieving financial closure of the recently secured Rs17 bn Hungund-Hospet.

Maintain earnings estimates and SOTP-based target price of Rs65/share; reiterate ADD rating

We maintain our earnings estimates and retain our SOTP-based target price to Rs65. We reiterate our ADD rating on the stock based on (1) incremental visibility on identified projects, (2) likely pick up in demand across assets led by broad economic revival and (3) incremental project wins.

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Results in line; high other income helps beat PAT-level estimates

GMRI reported revenues of Rs10.7 bn, up 5% yoy, slightly higher (about 6.3%) than our estimate of Rs11.6 bn. Increase in traffic levels at the Delhi and Hyderabad airports, the start of operations of the Sabiha Gokcen airport and of commercial operations for four road projects were the key drivers of the revenue growth. Margins expanded by 340 bps yoy to 30.7% led by lower generation & operating expenses, employee and admin expenses as a percentage of sales. This was about 130 bps lower than our EBITDA margin expectation of 32%. The slight miss on EBITDA level led to an in line operating profit of Rs3.8 bn in 1QFY11. Higher-than-expected other income of Rs673 mn (versus our estimate of Rs150 mn and 1QFY10 level of Rs121 mn) led to a net PAT of Rs318 mn versus our estimate of a net loss of Rs487 mn in the quarter. The higher other income in the quarter was driven by (1) Rs260 mn of foreign exchange gains, and (2) Rs270 mn financial income from mutual funds.

Results inline at EBITDA level; higher-than-expected other income boosts bottom line

GMR Infrastructure 1QFY11 consolidated results - key numbers (Rs mn)

	1QFY11	1QFY11E	1QFY10	4QFY10	% change			FY2011E	FY2010	% change
					vs est.	yoy	qoq			
Total operating income	12,313	11,581	11,775	11,250	6.3	4.6	9.5	44,541	45,635	(2.4)
Generation and operating exp.	(7,316)	—	(7,204)	(5,990)		1.5	22.1	(27,698)	(25,760)	7.5
Admin and other expenses	(650)	—	(701)	(975)		(7.4)	(33.4)	(4,899)	(3,326)	47.3
Employees	(574)	—	(657)	(1,139)		(12.7)	(49.7)	(5,670)	(2,937)	93.1
Total operating costs	(8,539)	(7,875)	(8,563)	(8,104)	8.4	(0.3)	5.4	(23,856)	(32,022)	(25.5)
EBITDA	3,775	3,706	3,213	3,146	1.9	17.5	20.0	20,685	13,613	52.0
Other income	673	150	121	1,071	348.6	458.0	(37.1)	250	1,664	(85.0)
PBDIT	4,448	3,856	3,333	4,216	15.3	33.4	5.5	20,935	15,277	37.0
Financial charges	(2,383)	(2,638)	(1,598)	(2,227)	(9.7)	49.2	7.0	(13,188)	(7,223)	82.6
Depreciation	(1,648)	(1,705)	(1,373)	(1,642)	(3.3)	20.1	0.4	(8,524)	(6,122)	39.2
Pre-tax profit	416	(487)	363	348	NA	14.7	19.7	(778)	1,931	(140.3)
Taxation	(98)	—	(123)	762		(19.9)	(112.9)	(1,102)	323	(441.4)
PAT	318	(487)	240	1,109	NA	32.4	(71.3)	(1,880)	2,254	(183.4)
Minority interest	(23)	662	(15)	(300)				2,647	(454)	
Reported PAT	295	175	225	809	68.4	30.8	(63.6)	768	1,800	(84)
Profit from JVs/associates	(10)	—	—	(79)				40	(216)	
Reported PAT	284	175	225	731		26.2	(61.1)	807	1,584	(49.0)
Key ratios (%)										
Generation & operating exp./sales	59.4		61.2	53.2				62.2	56.4	
Admin & other exp./sales	5.3		6.0	8.7				11.0	7.3	
Employees/ sales	4.7		5.6	10.1				12.7	6.4	
EBITDA margin	30.7	32.0	27.3	28.0	(1.3)	3.4		46.4	29.8	
Pre-tax margin	3.4	(4.2)	3.1	3.1				(1.7)	4.2	
PAT margin	2.6	(4.2)	2.0	9.9				(4.2)	4.9	
Effective tax rate	23.6	—	33.8	(219.1)				(141.7)	(16.7)	

Source: Company, Kotak Institutional Equities estimates

Airports and roads sectors drive revenue growth

Yoy revenue growth in 1QFY11 was primarily led by the airports and roads sectors. The airports segment reported a 32% yoy growth in revenues to Rs4.3 bn in 1QFY11 from Rs3.2 bn in 1QFY10. Airport revenue growth was driven by (1) start of operations of the new terminal building in Saiha Gokcen Airport and (2) strong pick up in traffic growth at the Delhi and Hyderabad airports - partially aided by low base effect of 1HFY10. The roads segment revenues recorded a 28.7% yoy growth to Rs984 mn, primarily led by start of revenues from Ulunderpet Highway Project which was absent in 1QFY10. Non operation of the 235 MW GMR Energy plant led to a 7% decline in power segment revenues.

Increase in capital employed in the power business - driven by new power projects and private equity infusion

Total capital employed in the power business increased by about 39% on a sequential basis from Rs39 bn at the end of 4QFY10 to Rs54 bn at end-1QFY11. Increased investments into the new projects and private equity infusion in GMR Energy were the primary reasons behind the increase. GMR raised about US\$200 mn from Temasek Holdings and about US\$100 mn from IDFC Group in the form of private equity investment in its power subsidiary (GMR Energy).

GMR Infrastructure 1QFY11 segmental numbers (Rs mn)

	1QFY11	1QFY10	4QFY10	% change	
				yoy	qoq
Segment revenues	12,545	11,865	11,376	5.7	10.3
Power	5,838	6,293	4,288	(7.2)	36.2
Airports	4,251	3,212	4,335	32.4	(1.9)
Highways	984	764	909	28.7	8.2
EPC	405	1,150	176	(64.8)	130.2
Others	1,067	446	1,668	139.5	(36.0)
Segment EBIT	2,957	1,960	2,575	50.9	14.9
Power	544	608	780	(10.5)	(30.3)
Airports	861	442	948	95.0	(9.2)
Highways	487	353	370	38.2	31.5
EPC	70	273	331	(74.4)	(78.9)
Others	995	286	145	248.2	586.6
Capital employed	167,344	84,376	86,567	98.3	93.3
Power	54,213	32,025	39,048	69.3	38.8
Airports	29,589	29,860	29,904	(0.9)	(1.1)
Highways	9,804	7,076	9,244	38.5	6.1
EPC	721	—	2,311		(68.8)
Others	73,017	15,416	6,061	373.7	1,104.7
Revenue mix (%)					
Power	46.5	53.0	37.7		
Airports	33.9	27.1	38.1		
Highways	7.8	6.4	8.0		
EPC	3.2	9.7	1.5		
Others	8.5	3.8	14.7		
EBIT margin (%)					
Power	9.3	9.7	18.2		
Airports	20.3	13.7	21.9		
Highways	49.5	46.1	40.7		
EPC	17.2	23.7	188.0		
Others	93.2	64.1	8.7		

Source: Company, Kotak Institutional Equities

Successfully completed Interagen refinancing transaction

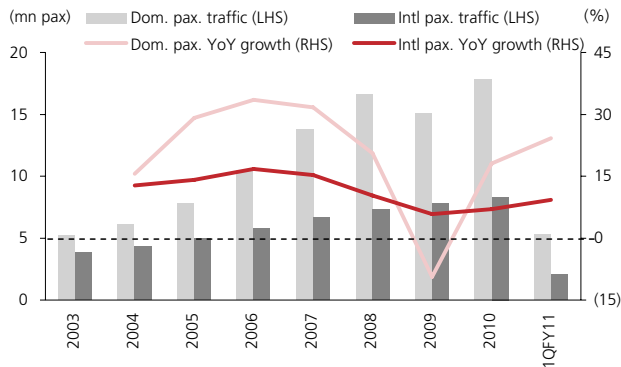
GMR successfully completed refinancing for the short term loan of US\$737 mn by a five-year facility. The refinancing was done by a consortium of banks led by Axis Bank and ICICI Bank. The new debt has a two year moratorium period and is repayable only from the third year. The average rate of the refinanced debt is Libor +425 bps.

The remaining US\$100 mn, of the total US\$837 mn of Interagen loan was infused as equity by GMR's sister entity. GMR's total equity investment in Interagen now stands at US\$300 mn (includes investment for interest payments). GMR has received US\$32 mn as dividend from Interagen so far.

Strong traffic growth in airport continues; growth partially led by low base

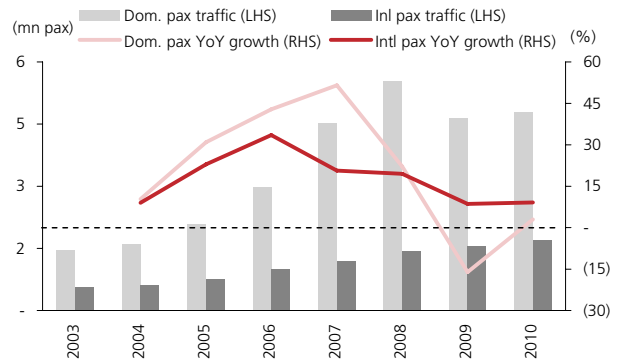
Both the Delhi and Hyderabad airports reported strong traffic growth in 1QFY11. This is a likely reflection of the pick up in the economic environment although part of the growth was also boosted by low base effects of 1HFY10. The Hyderabad airport reported a growth of 20% yoy in passenger traffic while Delhi airport witnessed a strong passenger traffic growth of 19% yoy. This is versus declines of 24% and 13.5%, respectively, in 2HFY09.

Domestic and international passenger traffic statistic at Delhi airport, March fiscal year-ends 2003-1QFY11



Source: Airports Authority of India, DGCA, Company, Kotak Institutional Equities

Domestic and international passenger traffic statistic at Hyderabad airport, March fiscal year-ends 2003-1QFY11



Source: Airports Authority of India, DGCA, Company, Kotak Institutional Equities

Airport segment: 1QFY11 financial performance - key numbers (Rs mn)

	1QFY11	1QFY10	4QFY10	% change	
				4QFY09	3QFY10
Gross revenues	5,548	4,446	6,093	24.8	(8.9)
Aero	1,932	1,687	1,861	14.5	3.8
Non-aero	3,185	2,165	3,851	47.1	(17.3)
Cargo operations	432	595	382	(27.4)	13.1
Less: revenue share	(1,297)	(1,235)	(1,758)	5.0	(26.2)
Net revenue	4,251	3,211	4,335	32.4	(1.9)
Total expenditure	(2,709)	(2,066)	(2,815)	31.1	(3.8)
EBITDA	1,542	1,145	1,520	34.7	1.4
Other income	231	18	403	1,183.3	(42.7)
PBDIT	1,773	1,163	1,923	52.5	(7.8)
Financial charges	(1,115)	(836)	(1,243)	33.4	(10.3)
Depreciation	(911)	(722)	(975)	26.2	(6.6)
Pre-tax profit	(253)	(395)	(295)	(35.9)	(14.2)
Taxation	(30)	54	(18)	(155.6)	66.7
PAT	(283)	(341)	(313)	(17.0)	(9.6)
Minority interest	62	(116)	(16)	(153.4)	(487.5)
Reported PAT	(221)	(225)	(329)	(1.8)	(32.8)
Key ratios (%)					
Aero revenue share	34.8	37.9	30.5		
Non-aero revenue share	57.4	48.7	63.2		
EBITDA margin	27.8	25.8	24.9		
Pre-tax margin	(4.6)	(8.9)	(4.8)		
PAT margin	(5.1)	(7.7)	(5.1)		
Effective tax rate	0.5	(1.2)	0.3		

Source: Company, Kotak Institutional Equities

DIAL: Marginal revenue growth; cargo business outsourced to cargo JV

DIAL reported a marginal revenue growth of about 4% yoy to Rs2.7 bn in 1QFY11. The aero and non-aero revenue streams of the airport recorded moderate growth of 8.6% and 5.8% yoy in the quarter. The non-aero revenues were partly impacted by lower duty free income due to a shift from Minimum Amount Guaranteed (MAG) model to the revenue share model. Sedate revenue growth in the quarter was primarily led by a 37.5% decline in cargo revenues to Rs312 mn on account of cargo operations being handled by the cargo JV. The existing cargo operations were handed over to Celebi while greenfield cargo operations were handed over to Cargo Service Centre with effect from 4QFY10 - GMR has 26% stake in the cargo business.

EBITDA margin for the quarter expanded significantly from 32.5% in 1QFY10 to 46.3% in 1QFY11. This expansion was primarily led by lower employee costs due to roll-over of AAI staff to AAI's payroll from GMR's. DIAL reported a net profit of Rs95 mn in 1QFY11 versus a loss of Rs79 mn in 1QFY10.

Delhi Airport:1QFY11 financial and operational performance - key numbers (Rs mn)

	1QFY11	1QFY10	4QFY10	% change	
				yoy	qoq
Gross revenues	2,673	2,577	3,581	3.7	(25.4)
Aero	1,091	1,005	1,014	8.6	7.6
Non-aero	1,072	1,013	2,024	5.8	(47.0)
Cargo	312	499	270	(37.5)	15.6
Less: revenue share	(1,248)	(1,189)	(1,716)	5.0	(27.3)
Net revenue	1,425	1,388	1,865	2.7	(23.6)
Total expenditure	(765)	(937)	(1,008)	(18.4)	(24.1)
EBITDA	660	451	857	46.3	(23.0)
Other income	55	7	383	685.7	(85.6)
Financial charges	(318)	(327)	(327)	(2.8)	(2.8)
Depreciation	(291)	(247)	(323)	17.8	(9.9)
Pre-tax profit	106	(116)	590	NA	(82.0)
Taxation	(11)	37	(68)	NA	(83.8)
PAT	95	(79)	522	NA	(81.8)
Key ratios (%)					
Aero share	40.8	39.0	28.3		
Non-aero share	40.1	39.3	56.5		
EBITDA margin	46.3	32.5	46.0		
PAT margin	3.6	(3.1)	14.6		
Effective tax rate	10.4	31.9	11.5		
Operational performance					
Passenger (mn)	7.3	6.1	6.8	19.2	7.2
Domestic	5.3	4.2	4.6	24.1	15.6
International	2.0	1.9	2.3	8.2	(9.7)
Cargo ('000 tons)	101.0	86.8	98.8	16.4	2.2
Domestic	45.8	37.2	44.6	23.0	2.7
International	55.3	49.6	54.3	11.4	1.8
ATMs ('000)	61.4	55.5	57.6	10.6	6.6
Domestic	43.7	40.1	41.2	9.1	6.2
International	17.6	15.4	16.4	14.5	7.4

Source: Company, Kotak Institutional Equities

GHIAL – moderate revenue growth likely led by traffic growth

GHIAL reported yoy revenue growth of 7.4% in 1QFY11 to Rs1.2 bn from Rs1.1 bn in 1QFY10. Both the aero and non-aero revenues recorded a growth of about 7.5% yoy likely led by the passenger traffic growth of 19.8% at the Hyderabad airport. The EBITDA margin for the quarter remained relatively flat at 52.6% in 1QFY11 (down 120 bps yoy). High interest and depreciation cost in the quarter led to a net loss of Rs102 mn in 1QFY11 versus a net loss of Rs219 mn in 1QFY10. The management expects to break even at the PAT level in the next year.

Hyderabad Airport: 1QFY11 financial performance - key numbers (Rs mn)

	1QFY11	1QFY10	4QFY10	% change	
				yoy	qoq
Gross revenues	1,216	1,132	1,149	7.4	5.8
Aero	619	577	581	7.3	6.5
Non-aero	596	554	568	7.6	4.9
Less: revenue share	(49)	(46)	(42)	6.5	16.7
Net revenue	1,167	1,086	1,107	7.5	5.4
Total expenditure	(553)	(502)	(527)	10.2	4.9
EBITDA	614	584	580	5.1	5.9
Other income	137	7	24	1,857.1	470.8
Financial charges	(532)	(495)	(507)	7.6	5.0
Depreciation	(326)	(315)	(343)	3.6	(4.8)
Pre-tax profit	(108)	(219)	(246)	(50.8)	(56.2)
Taxation	6	—	—		
PAT	(102)	(219)	(246)	(53.5)	(58.6)
Key ratios (%)					
Aero share	50.9	51.0	50.6		
Non-aero share	49.0	48.9	49.4		
EBITDA margin	52.6	53.8	52.4		
PAT margin	(8.4)	(19.3)	(21.4)		
Operational performance					
Passenger (mn)	1.8	1.5	1.6	19.8	14.1
Domestic	1.4	1.1	1.2	24.3	15.1
International	0.4	0.4	0.4	7.5	11.0
Cargo ('000 tons)	19.0	15.4	17.9	24.0	6.2
Domestic	8.6	6.3	7.8	37.1	10.0
International	10.5	9.1	10.1	15.0	3.3
ATMs ('000)	20.1	20.3	20.3	(0.7)	(0.8)
Domestic	16.8	17.1	16.9	(1.5)	(0.5)
International	3.3	3.2	3.4	3.4	(2.4)

Source: Company, Kotak Institutional Equities

Operationalization of new terminal and strong traffic growth at SGIA boosts revenue growth

ISGIA (Turkey airport) reported strong revenue growth of 132% yoy to Rs1.4 bn in 1QFY11 from Rs604 mn in 1QFY10. The strong revenue growth was led by (1) very strong passenger growth of about 94% yoy, (2) the start of operations of the new terminal building and (3) increase in Passenger Service Fees (PSF). Capitalization of the new terminal building led to high interest and depreciation costs during the quarter -- ISGIA reported a net loss of Rs229 mn in 1QFY11.

SGIA: 1QFY11 financial performance - key numbers (Rs mn)

	1QFY11	1QFY10	4QFY10	% change	
				yoy	qoq
Gross revenues	1,401	604	1,129	132.0	24.1
Total expenditure	(1,130)	(491)	(1,007)	130.1	12.2
EBITDA	271	113	122	139.8	122.1
Financial charges	(212)	(10)	(400)	2,020.0	(47.0)
Depreciation	(283)	(148)	(299)	91.2	(5.4)
Pre-tax profit	(215)	(45)	(577)	377.8	(62.7)
Taxation	(14)	22	47	(163.6)	(129.8)
PAT	(229)	(23)	(530)	895.7	(56.8)
Key ratios (%)					
EBITDA margin	19.3	18.7	10.8		
PAT margin	(16.3)	(3.8)	(46.9)		
Effective tax rate	1.0	(3.6)	(4.2)		
Operational performance					
Passenger (mn)	2.8	1.5	2.2	93.1	27.3
Domestic	1.9	1.0	1.6	91.9	21.8
International	0.9	0.5	0.6	95.7	40.6
Cargo ('000 tons)	5.5	2.2	3.8	147.1	45.8
Domestic	0.4	0.7	0.4	(47.0)	(10.3)
International	5.2	1.6	3.4	228.7	52.2
ATMs ('000)	23.4	11.9	18.6	96.4	25.9
Domestic	15.4	7.8	12.8	96.9	20.1
International	8.0	4.1	5.8	95.4	38.8

Source: Company, Kotak Institutional Equities

Power -- revenue decline due to non-operation of GMR Energy plant

Power segment revenues recorded a 7.2% yoy decline to Rs5.8 bn in 1QFY11, primarily due to non-operations of the 235 MW GMR Energy plant. The barge mounted power plant was relocated to Kakinada (AP) in April 2010. The plant has started operations from July 2010 and should start contributing to revenues again from 2QFY11. The lower EBITDA margin in the quarter (down about 410 bps yoy to 9.8%) was attributed to higher power trading revenues. The bottomline of the power segment was boosted by high other income of Rs264 mn (versus Rs31 mn in 1QFY10) led by higher treasury income in GMR Energy. GMR reported a power segment net PAT of Rs265 mn, up 13.2% yoy.

Power segment: 1QFY11 financial performance - key numbers (Rs mn)

	1QFY11	1QFY10	4QFY10	% change	
				yoy	qoq
Gross revenues	5,838	6,293	4,288	(7.2)	36.1
Contracted	3,934	4,064	4,228	(3.2)	(7.0)
Merchant sale	—	912	—		
Power trading	1,904	1,317	60	44.6	3,073.3
Total expenditure	(5,265)	(5,416)	(3,767)	(2.8)	39.8
Cost of fuel	(4,855)	(5,006)	(3,238)	(3.0)	49.9
Other operating expenses	(410)	(410)	(529)	-	(22.5)
EBITDA	573	877	521	(34.7)	10.0
Other income	264	31	538	751.6	(50.9)
PBDIT	837	908	1,059	(7.8)	(21.0)
Financial charges	(222)	(310)	(194)	(28.4)	14.4
Depreciation	(292)	(300)	(278)	(2.7)	5.0
Pre-tax profit	323	298	587	8.4	(45.0)
Taxation	(58)	(64)	670	(9.4)	(108.7)
PAT	265	234	1,257	13.2	(78.9)
Minority interest	64	95	278	(32.6)	(77.0)
Reported PAT	201	139	1,535	44.6	(86.9)
Key ratios (%)					
Cost of fuel/sales	83.2	79.5	75.5		
Other expenses/sales	7.0	6.5	12.3		
EBITDA margin	9.8	13.9	12.2		
Pre-tax margin	5.5	4.7	13.7		
PAT margin	4.5	3.7	29.3		
Effective tax rate	1.0	1.0	(15.6)		

Source: Company, Kotak Institutional Equities

GMR also highlighted progress across several of its upcoming power projects. Key details of the status of these projects are given below.

Recent developments and status of various power projects of GMR

GMR Energy (235 MW)	- Plant shifted to Kakinada; started operations from July 2010 - Gas allocation received from KG Basin
Vemagiri Expansion (768 MW)	- Land and water available at the existing site - EPC contract awarded to L&T - STG contract finalized with Alstom
Kamalanga (1,050 MW)	- Achieved financial closure for ~Rs. 45 bn - EPC contract awarded to SEPCO, China - Construction activities commenced - Approval obtained from Govt. of Orissa for enhancement of capacity by 350 MW
Chattisgarh (1,320 MW)	- Land acquired - EPC contract for BTG awarded to Doosan, Korea - Recommended for Coal Linkage by CEA
EMCO Energy (600 MW)	- Financial Tie-up for ~ Rs. 26 bn; first disbursements made by all banks - Land acquired and water allocation received - Coal Linkages and MOEF approval received for both phases - BTG supply contract awarded to Shanghai Electric Corporation, China - Construction commenced in May 2010
Alaknanda (300 MW)	- CEA concurrence received for DPR - Environmental Clearance received - Forest Clearance & Private Land Acquisition in progress
Other hydro projects (1,840 MW)	- DPR & EIA studies completed for BajoliHoli - Approval obtained from Govt of Nepal for capacity enhancement of Upper Karnali (900 MW) & Upper Marsyangdi (600 MW) projects

Source: Company

Roads– revenue boosted by start of operations of Ulunderpet Highway project

GMRI reported a 29% yoy growth in road segment revenues in 1QFY11. This strong growth was led by the start of commercial operations of the Ulunderpet Highway Project. The annuity income remained relatively flat on a yoy basis at Rs618 mn. GMRI reported toll revenues of Rs366 mn versus Rs147 mn in 1QFY10. However, high interest costs and depreciation due to capitalization of the project led to a net loss of Rs138 mn in 1QFY11 versus a loss of Rs41 mn in 1QFY10.

Roads segment: 1QFY11 financial performance - key numbers (Rs mn)

	1QFY11	1QFY10	4QFY10	% change	
				yoy	qoq
Gross revenues	984	764	909	28.8	8.3
Annuity income	618	617	616	0.2	0.3
Toll collection	366	147	293	149.0	24.9
Total expenditure	(176)	(111)	(211)	58.6	(16.6)
EBITDA	808	653	698	23.7	15.8
Other income	63	7	24	800.0	162.5
PBDIT	871	660	722	32.0	20.6
Financial charges	(617)	(379)	(553)	62.8	11.6
Depreciation	(384)	(308)	(352)	24.7	9.1
Pre-tax profit	(130)	(27)	(183)	381.5	(29.0)
Taxation	(8)	(14)	(8)	(42.9)	-
PAT	(138)	(41)	(191)	236.6	(27.7)
Minority interest	20	35	(11)		
Reported PAT	(158)	(76)	(202)		
Key ratios (%)					
Annuity income share	62.8	80.8	67.8		
Toll collection share	37.2	19.2	32.2		
EBITDA margin	82.1	85.5	76.8		
PAT margin	(14.0)	(5.4)	(21.0)		
Effective tax rate	(6.2)	(51.9)	(4.4)		

Source: Company, Kotak Institutional Equities

Achieves financial closure of two road projects; commences construction in Hyderabad-Vijayawada project

The GMR management cited that the company has achieved financial closure for the two new road projects i.e. Hyderabad –Vijayawada and Chennai Ring Road. Financial closure for the Hyderabad-Vijayawada project was completed in April 2010 (awaiting confirmation from NHAI) and the company has already started construction operations of the same. The financial closure of the Chennai Outer Ring road was achieved in June 2010. The average interest rate for the loans is likely to be around 10.5% on a fixed basis for the construction period of the project - to be reset after CoD. The management also cited that the company is close to achieving financial closure of its new Rs16.5 bn Hospet-Hungud road project - expects to be completed over the next few months.

Retain earnings estimates and target price of Rs65/share; reiterate ADD

We retain our earnings estimates of Rs0.2 and Rs0.1 for FY2011E and FY2012E, respectively. We retain our SOTP-based target price to Rs65/share and reiterate our ADD rating on the stock based on (1) incremental visibility on identified projects, (2) likely pick up in demand across assets led by broad economic revival and (3) incremental project wins.

Value = Existing + identified projects + opportunities

Our SOTP-based target price of 65/share comprises of value from existing operational projects as well as partial value (about 50%) of projects identified by GMRI.

We value the existing projects of GMRI at Rs58/share comprised of (1) Rs24/share from the Delhi airport and associated real estate development, (2) Rs11/share from Hyderabad airport and associated real estate & SEZ development, (3) Rs3.1/share from road projects, (4) Rs14/share from power plants under development, (5) Rs0.8/share from Krishnagiri SEZ development and (7) Rs3.6/share of net cash. We estimate that the power projects under initial phase of development could potentially contribute Rs11/share while the coal mines could add an additional Rs3.6/share to the value of GMRI. However, we currently attribute 50% of the value of such identified projects in to the SOTP. We have not attributed any value to future development opportunities despite the strong execution track record of the company.

We arrive at SOTP-based value of Rs65/share for GMRI
SOTP-based valuation of GMRI

	Total asset value		GMR's stake (%)	Value of GMR's stake			
	(Rs bn)	(US\$ mn)		(Rs bn)	(US\$ mn)	(Rs/share)	(% Contribution)
Airports							
Delhi Airport	161.3	3,506	54.0	87.1	1,893	23.8	36.4
Core	27.2	591		14.7	319	4.0	6.1
Real estate	134.1	2,915		72.4	1,574	19.7	30.3
Hyderabad Airport	62.6	1,362	63.0	39.5	858	10.8	16.5
Core	32.7	710		20.6	447	5.6	8.6
Commercial real estate	21.9	477		13.8	300	3.8	5.8
Airport SEZs	8.0	175		5.1	110	1.4	2.1
Sabiha Gocken	19.3	420	40.0	7.7	168	2.1	3.2
Total for airports (A)	243.2	5,288		134.3	2,919	36.6	56.1
Roads	14.8	322					
GTTEPL	1.7	38	60.8	1.1	23	0.3	0.4
GTAEPL	1.3	29	60.8	0.8	17	0.2	0.3
GPEPL	1.0	22	100.0	1.0	22	0.3	0.4
GACEPL	0.8	17	100.0	0.8	17	0.2	0.3
GJEPL	3.5	76	100.0	3.5	76	1.0	1.5
GUEPL	6.4	140	100.0	6.4	140	1.8	2.7
GCORRPL	(2.6)	(57)	90.0	(2.4)	(51)	(0.6)	(1.0)
GHVEPL	0.2	4	74.0	0.1	3	0.0	0.1
Total for roads (B)	12.4	269		11.4	247	3.1	4.8
Power							
Vemagiri	16.4	356	100.0	16.4	356	4.5	6.8
Mangalore	7.3	160	100.0	7.3	160	2.0	3.1
Basin Bridge	4.2	91	51.0	2.1	46	0.6	0.9
Kamalanga (Orissa)	15.8	344	100.0	15.8	344	4.3	6.6
Alakananda	3.9	85	100.0	3.9	85	1.1	1.6
EMCO project	4.5	97	100.0	4.5	97	1.2	1.9
Projects in operation or substantial progress (X)	52.1	1,132		50.0	1,088	13.6	20.9
Chattisgarh	10.7	233	100.0	10.7	233	2.9	4.5
Vemagiri expansion	11.2	243	100.0	11.2	243	3.1	4.7
Coastal Power	11.3	245	100.0	11.3	245	3.1	4.7
Talong	1.1	23	88.0	0.9	20	0.3	0.4
Bajoli Holi	0.6	14	100.0	0.6	14	0.2	0.3
Upper Karnali	1.9	42	100.0	1.9	42	0.5	0.8
Marsyangdi	4.9	106	100.0	4.9	106	1.3	2.0
Projects yet to make substantial progress (Y)	41.7	907		41.6	904	11.3	17.4
Total for power projects (C = X+ 50% Y)	72.9	1,586		70.8	1,540	19.3	30
SEZ (D)	2.9	63		2.8	62	0.8	1.2
Krishnagiri	2.9	63	98.0	2.8	62	0.8	1.2
Coal mines (E)	18.3	398		13.0	283	3.6	5.5
South Africal coal mines	8.6	187	38.5	3.3	72	0.9	1.4
Indonesian coal mines	9.7	212	100.0	9.7	212	2.7	4.1
Net cash at parent level (F)	13.3	290	100.0	13.3	290	3.6	5.6
Grand total (A + B+ C+ D + 50% E +F)	353.9	7,694		239.2	5,199	65.2	100.0

Source: Company, Kotak Institutional Equities estimates

Consolidated financials of GMR Infrastructure, March fiscal year-ends, 2005-12E (Rs mn)

	2006	2007	2008	2009	2010	2011E	2012E
Income statement							
Operating income	10,590	16,967	22,948	40,192	45,665	44,541	47,186
Total operating expenses	(6,086)	(11,531)	(16,963)	(29,524)	(32,022)	(23,856)	(24,608)
EBITDA	4,504	5,437	5,985	10,668	13,643	20,685	22,577
Other income	315	183	698	214	1,634	250	592
Interest expense	(1,558)	(1,441)	(1,687)	(3,682)	(7,223)	(13,188)	(12,612)
Depreciation	(2,200)	(1,346)	(1,785)	(3,898)	(6,122)	(8,524)	(10,294)
Pre-tax profit	1,061	2,833	3,210	3,301	1,931	(778)	263
Tax	(125)	(415)	(584)	(530)	323	(1,102)	(819)
Net profits	705	1,744	2,101	2,795	1,800	768	1,716
EPS (Rs)	0.5	1.1	1.2	0.8	0.4	0.2	0.1
Balance sheet							
Shareholders funds	5,704	19,923	61,172	64,780	66,386	67,193	67,678
Equity share capital	2,644	3,311	3,641	3,641	3,667	3,667	3,667
Reserves and surplus	3,060	16,612	57,531	61,139	62,719	63,526	64,011
Minority interest	4,243	5,261	11,126	18,061	14,591	15,369	13,098
Deposit from real estate and ADF	—	—	—	—	24,364	40,113	42,717
Loan funds	29,217	37,057	79,769	120,238	140,929	152,230	158,597
Secured	25,438	30,220	68,438	106,602	139,859	151,160	157,527
Unsecured	3,778	6,837	11,331	13,636	1,070	1,070	1,070
Total sources of funds	39,166	62,385	152,492	203,271	246,461	275,097	282,282
Net block	13,508	29,000	52,699	96,516	202,874	209,334	212,661
Capital work in progress	16,318	19,060	45,227	67,909	459	4,353	8,697
Net fixed assets	29,826	48,059	97,927	164,426	203,333	213,687	221,358
Investments	2,557	2,625	48,996	13,109	13,109	13,109	13,109
Net current assets (excl. cash)	29	(1,300)	(3,375)	1,071	11,782	12,011	11,985
Cash	6,754	13,000	8,945	24,665	18,237	36,290	35,830
Total application of funds	39,166	62,385	152,492	203,271	246,461	275,097	282,282
Free cash flow							
Net profit before tax and extraordinary items	1,061	2,833	3,210	3,301	1,931	(778)	263
Add: Depreciation / amortisation / non-cash prov	2,200	1,346	1,785	3,898	6,122	8,524	10,294
Tax paid	(126)	(241)	(261)	(701)	(664)	(1,102)	(819)
Operating profit before working capital change	3,135	3,938	4,735	6,499	7,390	6,644	9,738
Change in working capital / other adjustments	(2,400)	1,328	2,076	(4,446)	(10,711)	(229)	26
Net cashflow from operating activities	735	5,266	6,810	2,053	(3,321)	6,415	9,764
Fixed Assets	(8,654)	(19,589)	(51,679)	(70,091)	(47,567)	(18,877)	(17,965)
Investments	(802)	(68)	(46,371)	35,887	—	—	—
Cash (used) / realised in investing activities	(9,456)	(19,656)	(98,050)	(34,204)	(47,567)	(18,877)	(17,965)
Free cash flow	(8,722)	(14,391)	(91,240)	(32,151)	(50,888)	(12,462)	(8,201)
Ratios							
EBITDA margin (%)	42.5	32.0	26.1	26.5	29.9	46.4	47.8
Debt/equity	5.1	1.9	1.3	1.9	2.1	2.3	2.3
Net debt/equity	3.9	1.2	1.2	1.5	1.8	1.7	1.8
RoAE (%)	14.0	13.6	5.2	4.4	2.4	1.2	0.7
RoACE (%)	6.3	5.9	3.2	3.3	4.5	12.5	(9.4)

Source: Company, Kotak Institutional Equities estimates

AUGUST 09, 2010

RESULT

Coverage view: **Attractive**

Price (Rs): **770**

Target price (Rs): **NA**

BSE-30: **18,288**

Facing challenges across financial services. Reliance Capital continued to work towards building its core businesses during 1QFY11. Increasing focus on the traditional segment of the life insurance business will buffer NBAP margins in the new regulatory regime. Key highlights in other businesses: Moderate growth in NBFC loan book, challenging environment for asset management, broking and general insurance business tempered earnings.

Company data and valuation summary

Reliance Capital

Stock data

52-week range (Rs) (high,low)	977-611
Market Cap. (Rs bn)	189.5

Shareholding pattern (%)

Promoters	54.0
FIs	21.5
MFs	0.6

Price performance (%)

	1M	3M	12M
Absolute	1.3	12.5	(9.2)
Rel. to BSE-30	(1.3)	3.2	(24.8)

Forecasts/Valuations

	2010	2011E	2012E
EPS (Rs)	12.9	13.7	9.8
EPS growth (%)	(67.3)	6.5	(28.6)
P/E (X)	59.9	56.2	78.8
NII (Rs bn)	5.6	2.4	1.1
Net profits (Rs bn)	3.2	3.4	2.4
BVPS	279.0	286.3	291.5
P/B (X)	2.8	2.7	2.6
ROE (%)	4.7	4.8	3.4
Div. Yield (%)	0.8	0.7	0.5

Life Insurance: Focus on universal life policies to buffer margins

Reliance Life Insurance is increasingly pushing for traditional business in order to maintain profitability in the new regulatory framework. A strategy to focus on low ticket business (Rs10,000-12,000 per policy as compared to Rs25,000-Rs30,000 in case of most private players) has helped the company improve its franchise in the traditional segment. During 1QFY11, universal life policies accounted for about 42% of its overall new business; the non-ULIP business accounted for about 50% of the overall new business. Reliance Life reported NBAP margin of 17.7% (down 1% yoy) during 1QFY11; management does not expect a significant decline in margins after IRDA guidelines are implemented as most of its business (traditional) is beyond the scope of the guidelines.

The focus on this (lower-end of the market that has higher appetite for traditional business) market segment is positive. However, the high cost of distribution in this segment, changing competitive dynamics (especially since several players will now focus on this segment) and risk of revised regulations for the universal life policies makes its challenging to project NBAP margin at the current juncture.

We will revisit our valuation estimate for Reliance Life after taking a call on the sector. Reliance Life has been a large value driver for the stock, we will revisit our target price and recommendation after reviewing the insurance business; in the interim, revise rating to NR from ADD.

NBFC, asset management and broking businesses subdued

Reliance Capital proposes to be a holding company of various financial businesses over time, hence the standalone financials will not accurately reflect the performance of its businesses. We highlight the key operating highlights of various businesses of Reliance Capital.

- **Loan book flat.** Reliance Capital's loan book was almost flat qoq and up 7% yoy. The home finance business was up 8% sequentially, asset finance business was flat qoq; unsecured lending book declined (as expected).

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- ▶ **Home finance-Profitability down qoq.** Profitability of the home finance business (PBT/ average assets) moderated to 4% in 1QFY11 from 9.4% in 4QFY10 largely on the back of one-time income on securitization booked by the company in 4QFY10. Consequently, PBT was down to Rs364 mn in 1QFY11 as compared to Rs652 in 4QFY10.
 - High provisions in the unsecured lending business continued to temper the overall earnings of the financing business.
- ▶ **Lower AUMs affect earnings of AMC business.** Pressure on redemptions in the debt segment and challenges in raising equity AUMs affected the earnings of the asset management business- income down 15% qoq and PBT down 30% qoq. AUMs of the mutual fund business were down to Rs1 tn from Rs1.1 tn in 4QFY10.
 - Reliance Asset Management has made seed investments for its offshore fund in Singapore; during the quarter the company has booked MTM losses of about Rs50-60 mn (~10% PBT of the asset management business) on the same.
- ▶ **Business restructuring affects Reliance Money.** Reliance Money reported marginal PBT of Rs34 mn. Reported market share was almost stable at about 2%. Episodic businesses (like IPO funding) and money exchange business boosted income in 4QFY10; the closure of exchange business tempered the income in 1QFY11.
- ▶ **Performance of general insurance remains a concern.** Despite a shift in business strategies, Reliance General Insurance continues to report losses - Rs386 mn in 1QFY11 on the back of competitive pressure in the industry. The company had reduced dependence on the third party auto segment and increased focus on health insurance. However, losses in health insurance affected earnings during the quarter, the combined ratio remained high at 124%. Reliance Capital has infused capital of Rs950 mn during the quarter; thus the aggregate invested capital now stands at Rs11 bn. The company is conscious of the risks in the business and focusing on niche segment segments; the retention ratio during the quarter was 56% as compared to 65-85% in the past.

Reliance Capital - Quarterly results (Rs mn)

	1Q10	2Q10	3Q10	4Q10	1Q11	YoY (%)
Income statement (standalone)						
Operational income	6,165	6,813	5,347	5,577	2,270	(63)
Capital gains	1,329	2,113	733	670	100	-
Interest and finance cost	3,576	3,501	3,177	2,342	1,411	(61)
Net income (pre provisions)	2,589	3,312	2,170	3,235	859	(67)
Net total income (post provisions)	1,996	3,002	2,031	1,715	859	(57)
Operating expenses	943	1,494	1,526	493	467	(51)
PBT	1,053	1,508	504	1,222	393	(63)
Tax	10	417	92	375	(112)	(1,220)
Net profit	1,043	1,091	412	848	505	(52)
Other details						
Consumer finance business						
Loan book (Rs bn)	85,100	82,900	78,000	92,000	91,000	7
Mortgages	30,636	32,331	32,750	34,960	37,310	22
Auto	15,318	10,777	6,240	6,440	4,550	(70)
CV loans	14,467	13,264	11,700	14,720	13,650	(6)
SME	13,616	16,580	11,310	26,680	25,480	87
SME- unsecured (a)	-	-	8,980	-	-	-
Personal loans	11,063	8,290	7,020	5,520	4,550	(59)
Extracts of P&L (Rs mn)						
Interest income	2,764	2,759	2,600	2,594	2,732	(1)
Other income	118	687	663	661	250	112
Interest expenses	1,589	1,732	1,476	1,332	1,473	(7)
Net interest income	1,293	1,714	1,787	1,923	1,509	17
Provisions	631	715	681	709	514	(19)
Net interest income (post provisions)	662	1,000	1,106	1,214	995	50
Operating expenses	575	772	724	562	631	10
Employee expenses	190	221	242	269	234	23
Other expenses	385	551	482	293	397	3
PBT	87	228	382	652	364	319

Notes.

(a) SME loan book has been split into secured and unsecured from 3QFY10,

Source: Company

Reliance Capital - Quarterly data (Rs mn)

Reliance Capital - Quarterly results	1Q10	2Q10	3Q10	4Q10	1Q11	YoY (%)
Reliance Money						
Key operational details						
Branches (#)	8,637	6,233	5,116	5,116	5,103	(41)
Market volume (Rs bn/ day)	915	933	925	983	1,103	21
Average daily volumes (Rs bn)	16	15	16	22	23	
Days (#)	59	58	61	61	62	
Total volume (Rs bn)	944	870	970	1,342	1,426	51
Market share (%)	1.7	1.6	1.7	2.2	2.1	19.2
Extracts of P&L						
Operating income	682	609	537	758	390	(43)
Operating expenses	577	566	536	757	356	(38)
Sub-brokerage	57	40	35	99	93	63
Personnel costs	299	255	168	270	133	(55)
Other operating expenses	221	271	333	388	130	(41)
PBT	105	43	1	1	34	(68)
Reliance Asset Management						
AUMs						
Mutual fund (Rs mn)	1,083,000	1,183,000	1,200,000	1,100,000	1,000,000	(8)
Offshore fund (US\$ mn)	255	193	185	202	203	(20)
PMS (Rs mn)	30,000	31,000	32,000	18,000	22,000	(27)
No. of investors (mn)	7.1	7.3	7.2	7.5	7.4	4.2
Market share (%)	16.0	16.0	16.0	16.0	16.0	16.0
Extracts of P&L						
Income	1357.6	1560	1964	1936	1642	21
Operating expenses	887	881	1,184	1,083	1,036	17
Employee costs	317	359	488	323	385	21
Marketing expenses	386	262	466	642	418	8
Administrative expenses	184	261	230	117	233	27
PBT	471	679	780	853	606	29
PBT margins (%)	35	44	40	44	37	6
Reliance General Insurance						
	1Q10	2Q10	3Q10	4Q10	1Q11	YoY (%)
Gross underwritten premium	5,575	4,881	5,182	4,159	4,293	(23)
Net underwritten premium	3,418	3,188	4,130	3,552	2,412	(29)
PBT	10	1	(70)	(445)	(386)	
Net underwritten premium/ gross underwritten premium (%)	61	65	80	85	56	(8)
Reliance Life Insurance						
First year premium	4,430	6,775	8,150	16,260	5,630	27
Adjusted premium	4,493	6,842	8,256	16,384	6,053	35
Renewal premium	3,980	5,232	6,859	10,770	5,956	50
Average premium/ policy (Rs)	11,039	13,650	12,746	18,758	11,457	4
Branches (#)	1,145	1,145	1,247	1,247	1,247	9
Assets under management	80,060	99,829	112,595	137,000	144,232	80
Persistency (%)	67	67	64	63	71	6
NBAP margin- reported (%)	19	19	19	19	18	(5)

Source: Company

Reliance Consumer Finance - SBU wise analysis
Quarterly data (Rs mn)

Home finance SBU	1Q10	2Q10	3Q10	4Q10	1Q11	YoY (%)
Extracts of P&L (Rs mn)						
Interest income	692	689	689	662	762	15
Other income	44	195	258	406	63	(84)
Interest expenses	403	451	430	383	447	17
Net interest income	333	432	518	685	378	(45)
Provisions	17	12	5	(5)	3	(160)
Net interest income (post provisions)	316	420	513	690	375	(46)
Operating expenses	74	103	57	136	122	(10)
Employee expenses	30	44	48	67	57	(14)
Other expenses	44	60	8	69	65	(6)
PBT	242	316	456	554	253	(54)
Loan book	26,000	32,331	23,000	24,000	26,000	8
PBT/average assets (%)	3.4	4.0	6.6	9.4	4.0	
PBT- other income/average assets (%)	2.8	1.5	2.9	2.5	3.0	
Auto finance SBU						
Extracts of P&L (Rs mn)	-				-	-
Interest income	1,337	1,352	1,275	1,455	1,563	7
Other income	61	452	379	227	172	(24)
Interest expenses	819	899	727	747	857	15
Net interest income	579	904	927	935	878	(6)
Provisions	61	45	28	257	98	(62)
Net interest income (post provisions)	518	859	899	678	780	15
Operating expenses	270	452	447	277	402	45
Employee expenses	84	109	137	158	149	(6)
Other expenses	186	343	310	118	253	114
PBT	248	407	452	401	378	(6)
Loan book	56,000	42,279	39,000	56,000	56,000	
PBT/average assets (%)	NA	3.8	4.4	3.4	2.7	
Personal loans SBU						
Extracts of P&L (Rs mn)	-				-	-
Interest income	743	719	637	477	406	(15)
Other income	28	41	25	28	16	(44)
Interest expenses	367	382	320	203	170	(16)
Net interest income	404	378	342	303	252	(17)
Provisions	577	657	649	457	413	(10)
Net interest income (post provisions)	(173)	(279)	(306)	(154)	(161)	5
Operating expenses	228	217	221	150	107	(29)
Employee expenses	70	69	57	44	28	(37)
Other expenses	158	149	164	106	79	(26)
PBT	(401)	(496)	(527)	(304)	(268)	(12)
Loan book	13,818	8,290	16,000	11,000	8,973	(18)
PBT/average assets (%)	NA	(20.5)	(17.4)	(9.0)	(10.7)	

Source: Company

Sensitivity analysis indicating value of Reliance Life and Reliance Capital at different margin and multiple assumptions

Structural value (Rs bn) = NBV X multiple

Multiple (X)	Margin (%)					
	9.0	11.0	13.0	15.5	18.5	20.5
14.0	53	65	77	92	110	122
15.0	57	70	83	98	118	130
16.0	61	75	88	105	125	139
17.0	65	79	94	112	133	148
19.0	72	89	105	125	149	165

Appraisal value (Rs bn) = Structural value + Embedded value

Multiple (X)	Margin (%)					
	9.0	11.0	13.0	15.5	18.5	20.5
14.0	89	101	113	128	145	157
15.0	93	105	118	134	153	166
16.0	97	110	124	141	161	175
17.0	100	115	129	147	169	183
19.0	108	124	140	160	185	201

Contribution to sum-of-parts assuming full value for 100% (Rs per share of Reliance Capital)

Multiple (X)	Margin (%)					
	9.0	11.0	13.0	15.5	18.5	20.5
14.0	326	369	412	467	532	575
15.0	339	386	432	491	560	607
16.0	353	403	453	515	589	639
17.0	367	420	473	539	618	670
19.0	395	454	513	587	675	734

Sensitivity to our target price (Rs / share)

Multiple (X)	Margin (%)					
	9.0	11.0	13.0	15.5	18.5	20.5
14.0	675	719	762	817	882	925
15.0	689	736	782	841	910	957
16.0	703	753	803	865	939	989
17.0	717	770	823	889	968	1,020
19.0	745	804	863	937	1,025	1,084

Other assumptions

Embedded value (Rs mn)	35,601
No of shares o/s of Reliance Capital (mn)	246
Holding company discount	10%

Source: Kotak Institutional Equities

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UPDATE

 Coverage view: **Attractive**

 Price (Rs): **31**

 Target price (Rs): **28**

 BSE-30: **18,144**

Aligning the return profile. We met the management of NHPC to get their perspective on proposals made to the regulator to align the return profile of cost-plus hydro projects to those of their coal-based counterparts. Management contended that while there was no assurance on what form the incentives would take, there was an acceptance on the disparity of return profile. We maintain our REDUCE rating and target price of Rs28/share, as CMP already factors in benefits of a benign return profile.

Company data and valuation summary

NHPC

Stock data

52-week range (Rs) (high,low)	42-28
Market Cap. (Rs bn)	378.9

Shareholding pattern (%)

Promoters	86.4
FIs	1.5
MFs	1.1

Price performance (%)

	1M	3M	12M
Absolute	(2.1)	3.9	0.0
Rel. to BSE-30	(3.7)	(4.0)	0.0

Forecasts/Valuations

	2010	2011E	2012E
EPS (Rs)	1.9	1.3	1.6
EPS growth (%)	74.9	(27.5)	20.6
P/E (X)	16.6	22.9	19.0
Sales (Rs bn)	52.3	47.1	62.8
Net profits (Rs bn)	21.8	16.5	19.9
EBITDA (Rs bn)	41.3	39.2	52.4
EV/EBITDA (X)	12.4	13.5	10.3
ROE (%)	9.7	6.4	7.4
Div. Yield (%)	1.8	1.1	1.4

Contending for an improved return profile versus thermal projects

We recently met with the management of NHPC to get their perspective on (1) likely reimbursement of returns on CWIP, and (2) proposal for having differential tariffs during peak and off-peak hours and other alternate measures that could help improve the returns for the country's largest hydro developer.

NHPC's basic contention is that returns for hydro projects are inferior to those of cost-plus thermal power projects, despite (1) higher execution risks and the potency of geological surprises in hydro projects, and (2) higher capital cost and a longer gestation period in the case of hydro projects. We discuss each of the proposals in greater detail, though note that an improvement in overall profitability by 300 bps increases our fair value estimate by Rs3/share, already factored in CMP.

Standing up to private sector participation in hydro projects

NHPC affirmed that sale of power on a merchant basis was not an option available to counter the incessant competition from the private sector, which was offering higher upfront premiums for allocation of project sites on the back of significant proportion of merchant sale. The management, though, highlighted that transition to competitive bids for hydro projects may not happen in the near term as envisaged by the Tariff Policy, as high execution risks in hydro power projects from geological surprises make it difficult to estimate project cost and timelines.

CMP already factors benign return profile, maintain REDUCE rating

We retain our REDUCE rating with a target price of Rs28/share, though concede that approval of any of the proposed norms may lead to an upward revision in our target price, already factored in CMP. In our view, NHPC is richly valued at a P/B of 1.5X on FY2012E book (our target price implies a P/B of 1.3X) and risk to earnings from delayed project execution remain an area of concern.

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Return on CWIP seems counter intuitive, differential tariffs more plausible

Coal-based regulated projects make an effective yield of 21-22% on invested equity, superior to the ~18% yield earned by NHPC. The key differentiator in the earnings profile of coal-based cost plus projects is savings on fuel cost (versus normative re-imbursements) made by coal-based projects that is absent in hydel projects. We note that (1) higher capital cost and (2) elongated implementation schedule also requires a higher investment in CWIP, which further dilutes the equity IRR of hydro-based projects. We evaluate the key proposals, which may fructify allowing NHPC to improve its return profile, though concede the improvement that the CMP already factors in the benefit of a 300 bps improvement in return profile.

Exhibit 1: CMP already factors in 4% improvement in returns on invested equity
Sensitivity of EPS and fair value for improved returns on invested equity

	EPS (Rs/share)			Valuation (Rs/share)
	2011E	2012E	2013E	
Standard return (15.5%+Incentives)	1.3	1.6	1.8	28
Extra 3% return	1.5	1.9	2.1	30
Extra 4% return	1.6	1.9	2.2	31

Source: Kotak Institutional Equities estimates

Return on CWIP—disincentivises timely commissioning

On the issue of allowing return on CWIP, the core contention remains that allowing return on CWIP would (1) inflate the overall project cost for the end-consumer, on which a recurring regulated return would be paid for the life of the project, (2) may disincentivise timely commissioning of projects, and (3) may have to be allowed for thermal projects as well, thereby defeating the purpose of reducing the disparity between the returns of thermal and hydel projects.

However, if the regulator were to consider RoE on CWIP, NHPC's FY2011E earnings would be higher by 18% for earning a Rs8.8 bn return on Rs57 bn of CWIP as of end-FY2011E. Alternatively, if RoE during construction period were to be capitalized as project cost, it would inflate project cost by ~Rs37 bn (for projects under construction) implying an extra 0.2X value accretion on invested equity.

Differential tariffs—a more plausible solution

An alternate solution proposed to reduce the return disparity is to allow NHPC to sell power during peak hours at market-determined rates, thereby allowing incremental returns. As hydro projects are better positioned to step up generation to meet peaking demand, the solution seems more plausible from reducing the disparity of returns. Exhibit 2 highlights the likely accretion to value based on varying proportion of peak hour sale and incremental tariffs. We note that even under the most benign assumption of Rs2/kwh premium for 25% of overall sales volume can add Rs7/share to our target price.

Exhibit 2: CMP implies 15% sale during peak hours earning an incremental tariff of Rs1.5/kwh
Sensitivity of fair value to differential peak-hour sale

	Proportion of peaking power sale (%)					
	5	10	15	20	25	
Premium over base tariff (Rs/kwh)	1.0	28	29	30	30	31
	1.5	29	30	31	32	33
	2.0	29	30	32	33	35
	2.5	29	31	33	35	37
	3.0	30	32	34	36	38

Source: Kotak Institutional Equities estimates

Competing private sector participation in the hydro space

Competitive bid-based project allotment will take some time

The management indicated a low probability of introducing competitive bids for hydro projects and phasing out of the extant cost-plus tariff mechanism. We highlight that high execution risks in hydro power projects from geological surprises make it difficult to estimate project cost and timelines, hence making it difficult for the developer to commit both, price (due to cost overruns) and time (due to delays) for eventual sale of power.

Advance to state, an alternative to upfront payments

On the issue of private sector competition in allotment of hydro project sites from the state government, NHPC highlighted that they are overcoming the handicap of not being able to pay 'upfront premiums' for project allocations by giving interest-bearing loans and advances. However, NHPC conceded that being a public enterprise always limits the options NHPC has when competing with the private sector.

Exhibit 3: SOTP-based target price of Rs28/share

	Value (Rs mn)	Value per share (Rs/share)
SOTP of power projects (Rs mn)	228,970	19
Cash (Rs mn)	79,392	6
Investments (Rs mn)	12,783	1
Loans and advances (Rs mn)	17,137	1
Total value (Rs mn)	338,282	28

Source: Kotak Institutional Equities estimates

Profit model, balance sheet, cash model of NHPC, March fiscal year-ends, 2008-2015E (Rs mn)

	2008	2009	2010	2011E	2012E	2013E	2014E	2015E
Profit model								
Net revenues	29,726	34,767	52,273	47,100	62,822	77,852	94,289	96,903
EBITDA	22,150	23,110	41,290	39,181	52,412	65,589	76,559	78,688
Other income	4,572	5,953	6,473	6,738	8,423	8,310	8,778	10,448
Interest expense	(6,377)	(7,760)	(7,394)	(6,977)	(14,106)	(19,551)	(21,695)	(19,481)
Depreciation	(5,455)	(6,441)	(12,827)	(13,647)	(16,085)	(19,704)	(22,802)	(23,919)
Pretax profits	14,890	14,863	27,542	25,295	30,644	34,644	40,839	45,737
Tax	(1,896)	(1,552)	(2,245)	(5,107)	(6,179)	(6,982)	(8,752)	(9,894)
Deferred taxation	—	—	(2,521)	(1,466)	(2,151)	(2,670)	(2,017)	(702)
Minority interest	(1,533)	(1,462)	(1,020)	(2,204)	(2,388)	(2,581)	(2,516)	(2,622)
Net income	11,462	11,849	21,756	16,518	19,927	22,411	27,554	32,520
Extraordinary items	—	—	—	—	—	—	—	—
Reported profit	11,462	11,849	21,756	16,518	19,927	22,411	27,554	32,520
Earnings per share (Rs)	1.0	1.1	1.9	1.3	1.6	1.8	2.2	2.6
Balance sheet								
Paid-up common stock	111,825	111,825	123,007	123,007	123,007	123,007	123,007	123,007
Total shareholders' equity	189,310	197,678	251,072	262,521	276,242	291,638	310,354	332,328
Advance against depreciation (AAD)	13,033	14,245	15,398	14,238	13,078	11,918	10,758	9,598
Minority interest	13,968	14,944	15,895	18,099	20,487	23,068	25,584	28,206
Total borrowings	128,555	149,310	163,515	203,705	216,810	208,238	193,719	179,201
Deferred tax liabilities	—	—	2,521	3,987	6,137	8,808	10,825	11,526
Total liabilities and equity	344,865	376,177	448,402	502,551	532,754	543,670	551,240	560,860
Net fixed assets	236,171	238,323	225,568	248,000	293,945	349,306	368,800	344,881
Capital work-in progress	74,098	105,050	138,068	161,691	147,993	90,524	56,824	65,420
Investments	20,468	17,912	33,455	12,783	10,218	7,654	5,089	2,525
Miscellaneous expenses not w/o	3	23	—	—	—	—	—	—
Cash	23,459	26,061	61,895	87,825	88,632	96,940	121,066	151,490
Net current assets (incl. cash)	14,124	14,868	51,311	80,077	80,598	96,186	120,527	148,033
Total assets	344,865	376,177	448,402	502,551	532,754	543,670	551,240	560,860
Free cash flow								
Operating cash flow, excl. working capital	20,594	20,964	39,277	32,675	39,390	46,206	53,729	58,602
Working capital changes	5,017	1,858	(608)	(2,836)	286	(7,279)	(216)	2,918
Capital expenditure	(35,010)	(39,565)	(33,066)	(59,702)	(48,331)	(17,596)	(8,596)	(8,596)
Free cash flow	(9,400)	(16,743)	5,602	(29,863)	(8,656)	21,331	44,918	52,924
Ratios								
Net debt/equity (%)	34	33	26	25	24	22	21	19
Return on equity (%)	6.7	6.5	10.3	6.8	7.8	8.3	9.5	10.5
Book value per share (Rs)	16	17	20	21	22	23	25	27
ROCE (%)	5.7	5.7	7.8	5.0	6.3	7.3	8.4	9.0

Source: Company, Kotak Institutional Equities estimates

AUGUST 10, 2010

UPDATE

BSE-30: 18,288

Would June 2010 IIP be a major macro turning point? We do not think the markets have factored in a major drop in India's industrial growth as yet. We expect June IIP growth to dip further to 6.7% after it fell to 11.5% in May from 16.5% in April. We see this as a possibility for a major turning point for the Indian macro. It may prompt RBI to go slow on further tightening, but not signal a move over to a neutral policy stance as yet, as we expect inflation to remain sticky and at about 11% in July.

Risk that markets may be jolted by June IIP negative surprise on July 12

We expect June IIP at 6.0-7.4%, with a baseline projection of 6.7% (see Exhibits 1 & 2), lower than consensus of about 8.5%. When May IIP growth dropped to 11.5%, we had cautioned that it may further drop to about 6.5% in June (see our Economy note of July 12, 2010, 'May 2010 IIP: What goes up must come down'). We also said that as a base case, we see single digit IIP growth for almost all the months for the rest of the year, resulting in FY2011E IIP growth falling to 8-9%. We do not think the markets have factored in this possibility and see a risk of markets getting jolted on July 12, 2010 when the June IIP numbers are released at 11.00 am. We see a reversal to single-digit IIP growth factoring in (1) base effects waning, (2) seasonal m/m decline in June, (3) muted investment cycle recovery and (4) falling government consumption.

Core sector growth rate drop in June have reinforced our view of June IIP dropping sub-7%

The six core industries data released on July 28, 2010 have reinforced our view of a sharp drop IIP growth in June. Core industries growth slipped further to 3.4% in June – the third straight month of deceleration (see Exhibit 4). Output in all six core industries fell m/m, though crude oil production surprised on the up with a 6.8% y/y growth — the highest in five months. Finished steel production growth accelerated to 3.5% y/y but it fell 3.6% m/m. Coal production continued to be weak, improving marginally to 1.4% y/y from 0.3%. Refinery, cement and electricity production growth rates dropped perceptibly in June. Electricity sector growth rate came in at 3.2% after staying above 5% for the past six months. Auto numbers remain strong, but on an m/m basis are unlikely to significantly improve consumer durables growth (see Exhibit 3).

Second negative surprise likely on August 16: July IIP may prove to be sticky at 11% (new base)

If markets do not sufficiently react to a dip in growth in June IIP, the following week could start with a new trigger. July WPI due for release at noon on August 16 may show that India's headline inflation is proving to be sticky. We project headline inflation to soften marginally to 10.35% in July from 10.55% in June on the current base (FY1994=100), confirming persistence of high inflation. However, we expect GOI to release new WPI series with a new base (FY2004=100). The number of items in this new series can go up 685 from 435 and with a wider coverage and more up-to-date prices it can cause an upward bias to the current inflation estimates. We expect that to increase the June inflation rate by about 0.7 ppt to 11% (see Exhibits 5 & 6). If this is not bad enough, May inflation even in old base is likely to be revised upwards to 11.23% from 10.16%.

Monetary policy may go slow on tightening in September

In our assessment, lower IIP growth may prompt RBI to go slow on further tightening. It may not as yet prompt RBI to change its stance from tightening to neutral as inflation may prove to be sticky. With July inflation likely to remain in double digits, RBI may on September 16 settle for some more action — (a) 25 bps hike in reverse repo rate to 4.75% leaving the repo rate unchanged at 5.75% and (2) 25 bps hike in CRR to 6.25% effective fortnight beginning September 25. Despite recent indications from RBI that it has done enough to manage inflation, we expect another 75 bps hike in both policy rates thereafter on the back of inflation remaining above the RBI's projected trajectory (see Exhibit 7).

QUICK NUMBERS

- We expect June IIP at $\approx 6.7\%$ to be a major negative surprise for the markets
- We expect July 2010 inflation at $\approx 10.3\%$ (current base); $\approx 11\%$ (new base)
- RBI likely to go slow in tightening; may raise reverse repo & CRR by 25 bps each on September 16

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Exhibit 1: IIP growth likely to decelerate sharply in June 2010
Sectoral classification of IIP growth, March fiscal year-ends, 2009-2011 (%)

	Mining (%)			Manufacturing (%)			Electricity (%)			General (%)		
	2009	2010	2011	2009	2010	2011	2009	2010	2011	2009	2010	2011
Weights (%)	10.5			79.4			10.2			100.0		
April	6.1	3.4	11.7	6.7	0.4	17.9	1.4	7.1	6.5	6.2	1.1	16.5
May	5.5	3.4	8.7	4.5	1.8	12.3	2.0	3.3	6.1	4.4	2.1	11.5
June	0.1	14.2	7.9E	6.1	8.0	7.0E	2.6	8.0	3.2E	5.4	8.3	6.7E
July	2.8	8.7		6.9	7.4		4.5	4.2		6.4	7.2	
August	2.8	11.0		1.7	10.6		0.8	10.6		1.7	10.6	
September	5.8	7.4		6.2	9.7		4.4	7.5		6.0	9.3	
October	3.2	9.1		(0.6)	10.9		4.4	4.0		0.1	10.2	
November	0.7	10.7		2.7	13.1		2.6	1.8		2.5	12.0	
December	2.2	11.1		(0.6)	19.4		1.6	5.4		(0.2)	17.7	
January	0.7	15.3		1.0	17.4		1.8	5.6		1.0	16.3	
February	(0.2)	11.0		0.2	15.7		0.7	7.3		0.2	14.7	
March	1.9	11.8		(0.3)	14.7		6.3	7.7		0.3	13.9	
April-March (FY)	2.6	9.8	8.9E	2.7	10.9	8.8E	2.8	6.0	5.6E	2.7	10.4	8.5E

E: Kotak Institutional equities estimates for June IIP due for release on August 12, 2010
Source: GOI and Kotak Institutional Equities estimates

Exhibit 2: Capital goods production registered a sharp fall
Use-based classification of IIP growth, March fiscal year-ends, 2009-2011 (%)

	Basic goods			Capital goods			Intermediate goods			Consumer goods			Consumer durables			Consumer non-durables		
	2009	2010	2011	2009	2010	2011	2009	2010	2011	2009	2010	2011	2009	2010	2011	2009	2010	2011
Weights (%)	35.6			9.3			26.5			28.7			5.4			23.3		
April	4.0	4.5	9.0	12.4	(5.9)	69.9	3.1	7.9	10.6	8.5	(4.6)	11.9	3.2	17.6	32.8	10.0	(10.5)	4.5
May	3.0	3.8	7.9	4.3	(3.6)	34.3	1.9	6.6	10.1	7.4	(1.1)	8.2	2.8	13.2	23.7	9.0	(5.5)	2.4
June	2.2	10.7	3.1E	7.8	13.4	13.8E	2.8	7.9	8.8E	9.9	4.4	5.3E	4.6	16.2	25.8E	11.6	0.7	(2.1)E
July	5.3	4.7		17.9	1.7		3.0	9.8		5.9	9.7		13.9	22.1		3.4	5.3	
August	3.9	7.7		0.9	9.2		(5.5)	14.4		6.4	10.9		3.9	24.7		7.3	6.1	
September	5.0	5.3		20.8	13.5		(2.5)	11.0		7.4	9.7		14.7	24.1		4.8	4.1	
October	3.2	4.0		4.2	10.2		(4.4)	15.5		(0.9)	12.1		(1.6)	20.0		(0.6)	9.0	
November	2.2	6.0		0.5	11.1		(3.9)	19.6		9.4	12.2		0.3	38.1		12.4	4.5	
December	2.0	8.4		6.6	38.7		(8.9)	22.8		1.7	13.1		(4.2)	45.9		3.2	5.2	
January	(0.7)	11.5		15.9	53.7		(7.2)	21.9		3.6	3.0		2.1	31.7		4.0	(4.7)	
February	(0.1)	8.5		11.8	44.0		(3.0)	14.8		(1.3)	8.4		6.0	30.3		(3.4)	1.6	
March	1.9	10.4		(6.3)	28.4		1.9	13.1		1.3	10.7		8.4	32.6		(1.0)	3.3	
April-March (FY)	2.6	7.1	5.4E	7.3	19.1	17.8E	(1.9)	13.6	7.3E	4.7	7.3	7.9E	4.5	26.2	18.4E	4.8	1.3	3.8E

Source: GOI and Kotak Institutional Equities estimates

Exhibit 3: June automobile production marginally better than May
Production of cars, CVs and 2-wheelers consolidated across firms

Month	YOY % growth				MoM % growth			
	Automobiles	Cars	CVs	2-wheeler	Automobiles	Cars	CVs	2Ws
Apr-10	1,353,518	227,602	55,548	1,010,344	37	40	63	29
May-10	1,361,671	216,483	50,668	1,041,642	31	31	51	34
Jun-10	1,376,296	209,191	56,845	1,053,323	33	25	57	29
Jul-10	1,478,909	245,153	60,869	1,108,145	31	31	45	33

Source: SIAM, Kotak Institutional Equities

Exhibit 4: Core sector growth rate falls further to 3.4% in June

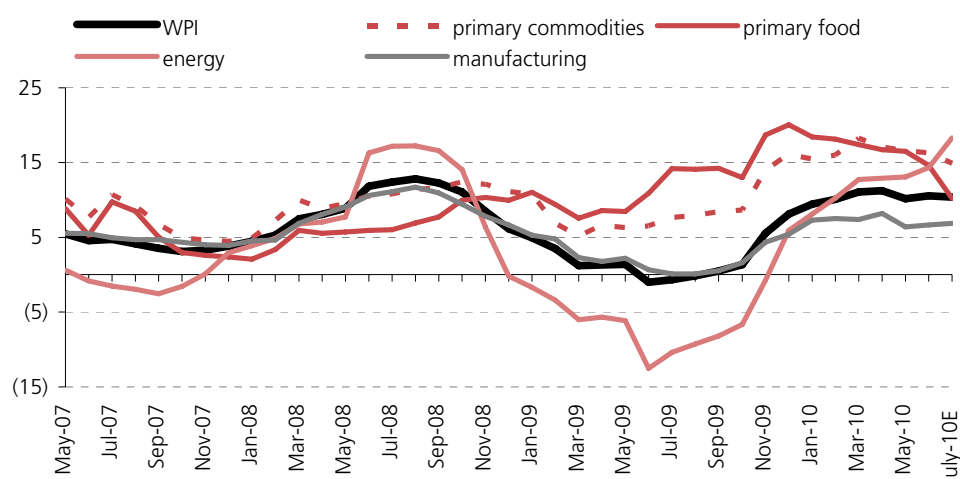
Sector-wise growth rates in production for six infrastructure industries, March fiscal year-ends, 2009-2011 (%)

	Crude Oil			Refinery			Coal			Electricity			Cement			Finished Steel			General		
	2009	2010	2011	2009	2010	2011	2009	2010	2011	2009	2010	2011	2009	2010	2011	2009	2010	2011	2009	2010	2011
Weights (%)	4.2			2.0			3.2			10.2			2.0			5.1			26.7		
April	1.0	(3.1)	5.2	4.3	(4.5)	5.3	10.3	14.3	(2.3)	1.4	6.7	6.9	6.9	11.9	8.7	7.5	(1.3)	4.7	4.6	3.7	5.4
May	3.2	(4.3)	5.8	0.1	(4.3)	7.7	8.8	10.2	0.3	2.0	3.3	6.1	3.8	11.8	8.6	8.3	2.8	2.5	4.4	3.2	5.0
June	(4.7)	4.0	6.8	5.6	(3.8)	2.9	6.1	14.7	1.4	2.6	8.0	3.2	6.6	12.7	3.6	8.1	3.6	3.5	4.4	6.3	3.4
July	(3.0)	(0.4)		11.8	(14.4)		5.5	9.7		4.5	4.2		5.5	13.8		6.3	4.0		5.2	3.2	
August	(1.0)	(2.6)		2.5	3.1		5.9	12.9		0.8	10.6		1.9	17.5		3.3	0.3		2.0	6.5	
September	(0.4)	(0.5)		2.8	3.4		11.2	6.5		4.4	7.9		8.1	6.5		2.3	0.8		4.1	4.5	
October	(0.2)	(2.2)		5.0	7.2		10.6	5.0		4.4	4.7		6.2	5.3		(3.8)	2.5		2.4	3.8	
November	0.5	(1.5)		(1.1)	4.9		9.7	4.7		2.6	3.3		8.7	9.0		(6.3)	11.7		0.8	6.0	
December	(0.3)	1.1		3.0	0.8		11.2	2.5		1.5	6.7		11.6	11.0		(8.0)	9.6		0.7	6.4	
January	(8.1)	9.7		(1.3)	3.8		6.7	5.9		1.8	6.7		8.3	12.4		3.2	15.3		2.2	9.5	
February	(6.2)	3.9		0.5	0.7		6.0	6.8		0.6	7.3		8.3	7.9		2.4	0.9		1.9	4.7	
March	(2.3)	3.5		3.3	(1.1)		5.3	9.2		6.3	7.8		10.1	7.8		(1.8)	9.2		3.3	7.3	
April-March (FY)	(1.8)	0.5		3.0	(0.5)		8.0	8.2		2.7	6.4		7.2	10.5		1.6	4.9		3.0	5.5	

Source: GOI and Kotak Institutional Equities

Exhibit 5: We expect July 2010 WPI inflation (base FY1994) at 10.35%

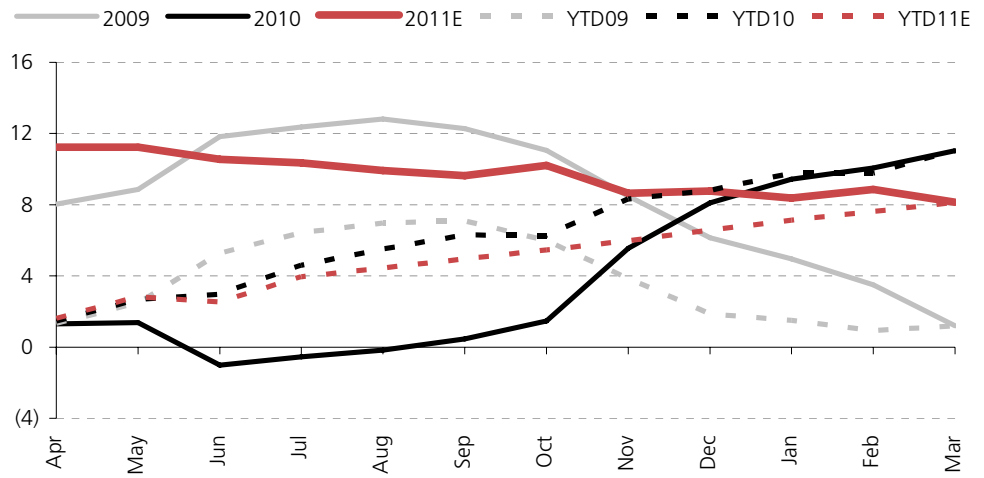
Inflation rate (yoy change in WPI) for major commodity groups (%)



Note: July 2010 inflation estimate is based on (1) primary commodities 14.86% (16.28% in June), (2) energy 18.3% (14.32%) and manufacturing 6.88% (6.66%). Food inflation is expected to fall to 10.18% (14.60%).

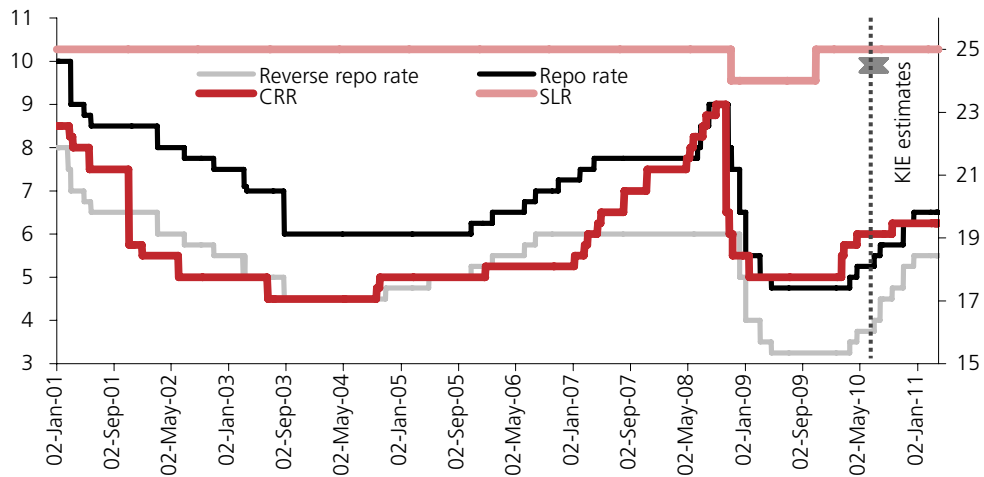
Source: GOI and Kotak Institutional Equities estimates

Exhibit 6: Inflation may average $\approx 9.5\%$ in FY2011E and fall to $\approx 8\%$ by end-year
 Headline WPI inflation rate (yoy), YTD price level change, March fiscal year-ends, 2009-2011E (%)



Source: GOI and from July 2010: Kotak Institutional Equities estimates

Exhibit 6: We expect reverse repo & CRR hiked 25 bps each on September 16
 RBI's repo, reverse repo rates and cash reserve ratio on LHS, SLR on RHS (%)



Source: RBI and Kotak Institutional Equities estimates

June 2010: Earnings announcement calendar

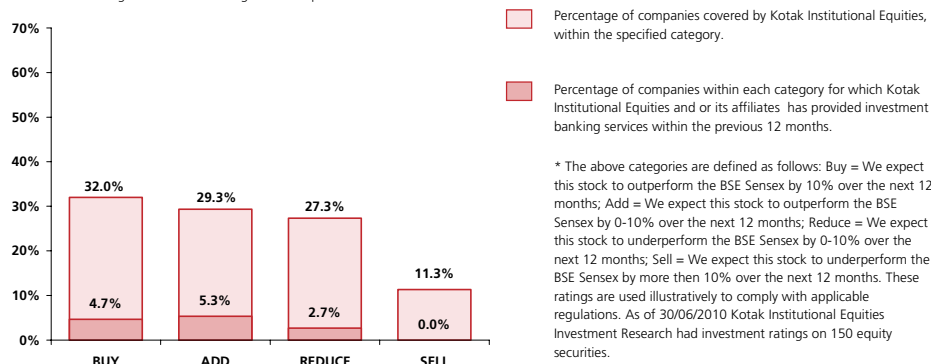
Mon	Tue	Wed	Thu	Fri	Sat
9-Aug	10-Aug	11-Aug	12-Aug	13-Aug	14-Aug
Jain Irrigation	Educomp Solutions	Bharti Airtel	Apollo Hospitals	Ackruti City	Lanco Infratech
Opto Circuits	IVRCL Infra	Bosch	Cummins India	Adani Enterprises	National Aluminium
Reliance Capital	Jai Corp	Financial Technologies	Divis Laboratories	Koutons Retail	Unitech
Tulip Telecom	Nagarjuna Constructions	Videocon Industries	Hindustan Copper	Suzlon Energy	
	Piramal Healthcare		Indiabulls Real Estate		
	Rashtriya Chemicals & Fertilisers		Moser Baer		
	Rolta India		MTNL		
	Tata Motors		Ranbaxy Laboratories		
			Shree Renuka Sugar		
			State Bank of India		
			Tata Power		
			Tata Steel		

Source: BSE, Kotak Institutional Equities

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As of June 30, 2010

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

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

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

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