Angel Broking™

Service Truly Personalized

July 4th, 2008

1QFY2009 - Result Preview

It does not Rain Forever...

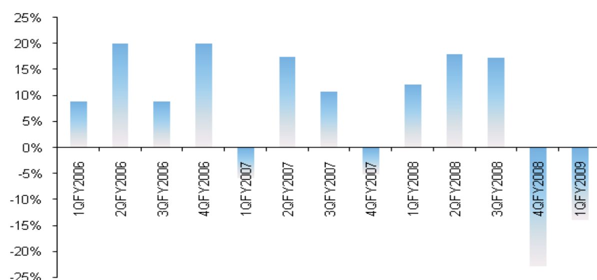
Research Team

Strategy

Bear sprint continues

The correction that began in January 2008 in the Indian stock markets showed no signs of reversal during 1QFY2009 with the Sensitive benchmark index, the Sensex, correcting by 14%. Notably, there was a consistent deterioration in the case for investment in equities owing to the several challenges that prevailed during 4QFY2008. Hence, there were severe headwinds in 1QFY2009 that marred the rationale of opting for equities as an investment class. In fact, towards early July 2008, the Sensex dipped below the 13,000 mark for the first time since April 2007 before recovering some ground.

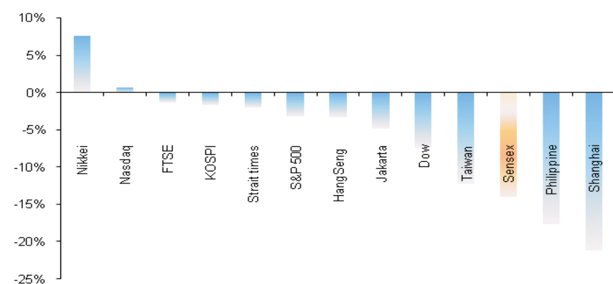
Exhibit 1: Sensex quarterly returns - No solace!



Source: Angel Research

This adversity, however, was not restricted to Indian equities alone as is evident from the performance of this asset class in 2008 year-to-date (YTD) across geographies. However, India was amongst the worst hit during the quarter as it lost 14% compared to its Emerging market peers, which lost in the region of 4-15%. The developed economies declined 1-5%, with indices like the Nikkei and Nasdaq actually giving positive returns.

Exhibit 2: Sensex - Among the leading losers



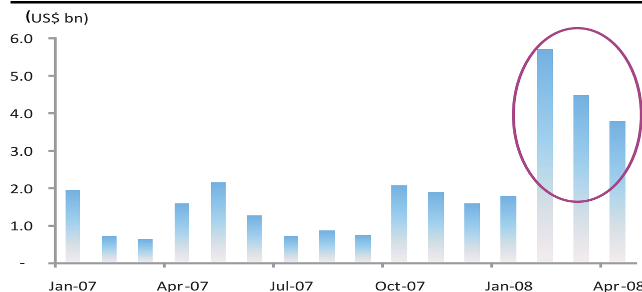
Source: Bloomberg

While adjusting to the global challenges, India also had to combat with its own set of challenges like uncertain political environment and deteriorating fiscal situation owing to the heavy dependence on oil imports. Further, since the Indian stock markets were commanding premium valuations on account of their 9%+ GDP growth and 20%+ corporate profit growth prospects, at the slightest hint of a slowdown in these led to evaporation of the premium and valuations got aligned to the relatively slower growth prospects.

Global capital flows robust, but FIIs pull back

Global capital flows, notwithstanding the FII pulling back from the country in recent months, have remained strong. A good indicator of this is the foreign direct investments (FDI), which are long-term committed funds, that is making its way into the country.

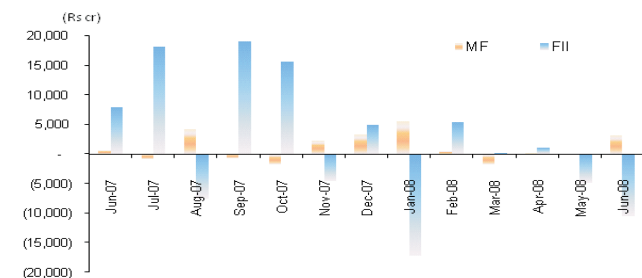
Exhibit 3: Strong FDI flows



Source: Bloomberg, Angel Research

However, FII inflows, some of which would be opportunistic and short-term in nature, headed back home as near term concerns overshadowed the long-term prospects of the Indian economy. The domestic Mutual Funds (MF) have also stayed largely on the sidelines over the last few months sensing the opportunity to buy into equities at lower levels. For the quarter, while FIIs were net sellers to the tune of Rs14,516cr (US $3.5bn), MFs did little to salvage the situation as they bought stocks worth a mere Rs3,380cr (US $800mn).

Exhibit 4: FIIs retreat; MFs wait-and-watch



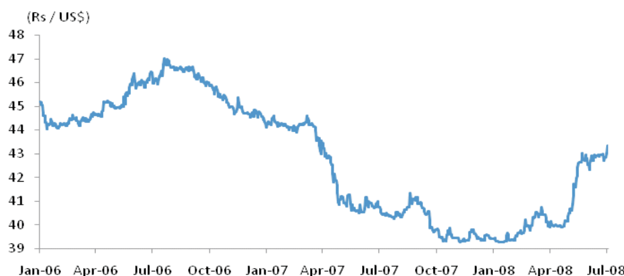
Source: SEBI, Angel Research

Strategy

Oil - The Sultan of headwinds…

The reason for the risk averseness of the global and domestic financial investors is not difficult to fathom. With crude scaling newer peaks, breaching the US $145 per barrel mark, the risk appetite of investors took a serious setback. Geo-political tensions in Iran, supply disruptions in Nigeria and North Sea, strong demand for oil, low inventories and spare capacity with the OPEC, and a depreciating Dollar were the key factors that precipitated the fears of an oil shortage and consequently the record spike in the crude oil prices.

Exhibit 5: USD / INR



Source: Bloomberg, Angel Research

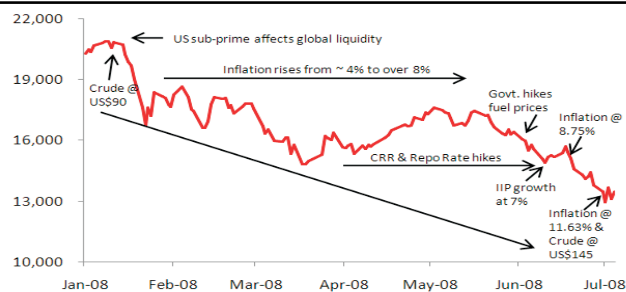
Seemingly what is also aiding the surge in oil prices is a study currently in progress by the International Energy Agency (IEA), which has hinted that the future oil supplies would not be as easy to come by was the case previously. Also, the investments required would be far higher than what estimates suggest, thus suggesting that the 'Black Gold' could get dearer over the years. This has led a certain faction of the market to predict oil prices to hit the US $200 per barrel in the coming years.

Exhibit 6: Global Oil Prices (US $/barrel)

Source: Bloomberg, Angel Research

High oil prices have a negative impact on equities as it has the potential to significantly dent corporate earnings, which tends to make investors averse to relatively risky assets like Equities. Hence, a higher degree of risk is attached to equities which in the current scenario has led to valuation downgrades.

Exhibit 7: Sensex - Impacted by multiple concerns



Source: Angel Research

Shifting concerns…

The US sub-prime imbroglio starts it all…

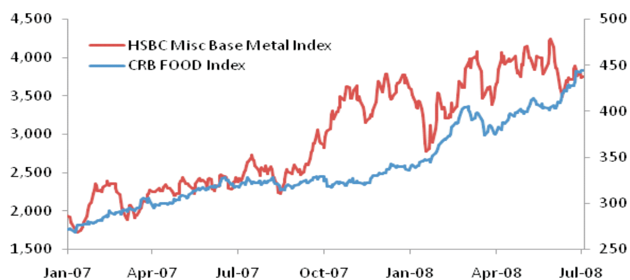
It all began with the blow-up of the sub-prime issue, the epicenter of which was the US, and which sent shockwaves across global financial markets. A series of write-downs and heavy losses ensued thereafter, resulting in severe constraints on liquidity requirements of the global financial world as investments into innovative financial instruments witnessed significant erosion in value. This consequently led to global investment managers pulling out of their most profitable avenues (until then equities) leading to the beginning of the downward spiral in equities. This prompted the US Federal Reserve to spring into action, which, after 17 consecutive rate hikes of 25bp each (June 2004 - 2006) taking the Fed Funds Rate from 1% to 5.25%, went into reverse gear. Thus, considering the criticality of sub-prime problem, the Fed swiftly cut its benchmark rate in 7 tranches (September 2007- April 2008) to the current 2% to inject liquidity into the system and save the economy from a recession. It also infused billions of Dollars to aid the cash-strapped US financial system to recover from the credit mess.

…with Inflation taking charge

The global investment managers thus regained confidence, with the US interest rates declining and capital getting cheaper. However, this time round, considering the supernormal profits that equities as an asset class had delivered over the past few years and the historically above average valuations that these were trading at, the focus shifted to commodities, leading to a bull-run in Oil, Metals and Agri Commodities.

Strategy

Exhibit 8: Metals. Food Index



Source: Bloomberg, Angel Research

What presumably has been helping investors is the leveraging effect (aided by rising asset prices), which not only helped them sustain a bull-run in global equities in a Fed tightening era in 2004-2006, but has also helped them repeat the performance in the commodities market. This is not to say that the entire rise in prices was liquidity driven as increasing demand on account of the strong global economic activity (much of it from Asia) since the last few years has played an important role. The flare up in commodity prices has consequently led to inflationary pressures building up across geographies, including India.

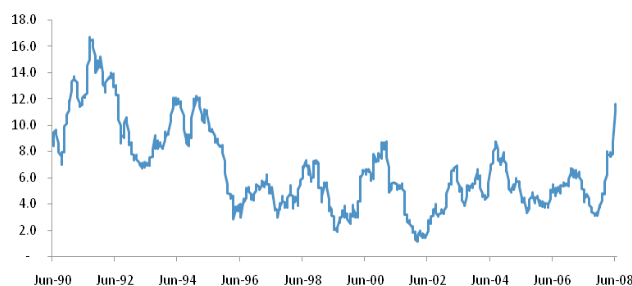
Exhibit 9: Global Inflation (%)

Country	Current	1-yr ago
India	11.6	4.4
Philippines*	10.2	2.3
China	8.1	3.4
Singapore	7.5	1.0
HongKong	5.7	1.2
S. Korea*	5.6	2.6
US	4.2	2.7
Malaysia	3.8	1.4
UK	3.4	2.5
Taiwan	3.2	0.7
Japan	1.4	-

*Source: Bloomberg, Angel Research; *for June 2008*

In fact, inflation is the most critical challenge being faced by the Indian government at the current juncture. Notably, inflation has had an uninterrupted run from the lows of 3% in 3QFY2008 and to current above the 11% mark, which is much above the government's and RBI's comfort zone of around 5.5% for FY2009 (revised upward from 5% in FY2008). The latest number (11.63%) reflects the continued impact of the fuel price hike, which contributes 20%+ to overall inflation. On a yoy basis, Food and Metals also continued to account for around 45% of overall inflation.

Exhibit 10: India - Inflation Trend (%)



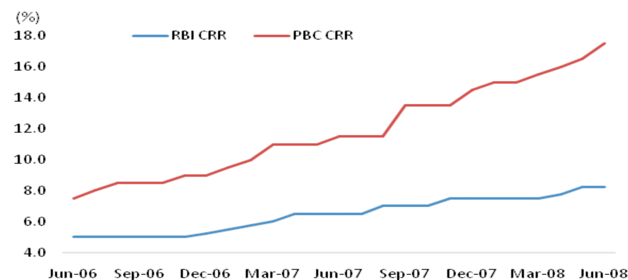
Source: Bloomberg, Angel Research

Evidently, the genesis of the current inflation problem lies in global commodity prices. We believe that diplomatic efforts by major countries to address the Crude Oil issue with the OPEC will play a decisive role in determining a resolution to the inflation problem.

Tighter Monetary Policy action

The repercussions of high inflation are threatening to de-rail, not just India, but also several global economies. High food inflation is not a welcome development partuicularly for the Emerging economies, considering that food items have a telling weightage in their inflation baskets. As a result, this issue is now being dealt with top priority. Countries like China and India have already initiated Monetary Policy measures in terms of a hike in the cash reserve ratio (CRR) and Repo Rates. With the intention of keeping a check on liquidity, China hiked its CRR 17 times in the last 24 months. Back home,even the RBI has taken recourse to this path of raising the CRR and Repo Rates. The RBI has further indicated its intention to clamp down on any inflationary pressures or expectations driven by excess demand in the economy. Hence, In such a scenario, further hikes by the RBI cannot be ruled out.

Exhibit 11: India, China CRR hikes



Source: Bloomberg, Angel Research

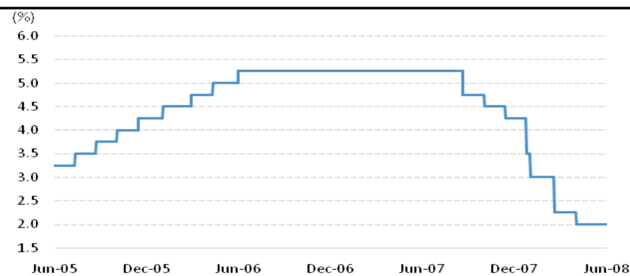
Strategy

Monetary stance in major economies

Sub-prime collapse forces loose Monetary Policy

During June 2006 to September 2007, all major central banks except the US Federal Reserve (US Fed) promulgated measures to tighten the money supply in their respective economies using either their policy rates or reserve requirement ratio. In September 2007, the US Fed cut its Targeted Fed Funds Rate by 50bp as the sub-prime problem snow-balled. Since then however, the ECB (seemingly reluctantly) has paused while the Bank of England (BOE) has been reducing rates since December 2007. Evidently, the problems in the housing sector of the US, and to a lesser extent UK, and the consequent impact on their financial sectors, have pushed the respective banks into a tight spot.

Exhibit 12: US Fed Rates



Source: Bloomberg, Angel Research

Notably, the Fed had been reducing rates to tackle its domestic problems. It recently however, acknowledged - probably too late - that it expects inflationary repercussions to prompt a tight policy stance going forward (it paused monetary softening recently). According to the Fed, although the downside risks to growth appeared to have diminished somewhat, the upside risks to inflation and inflation expectations have increased. However, it must be noted that the labour markets had further softened while the financial markets remained under considerable stress. According to Fed, tight credit conditions, the ongoing housing contraction and the rise in energy prices are likely to weigh down on economic growth over the next few quarters. This suggests that the Fed is still maintaining a watered down stance on inflationary pressures.

BOE's stance somewhat volatile

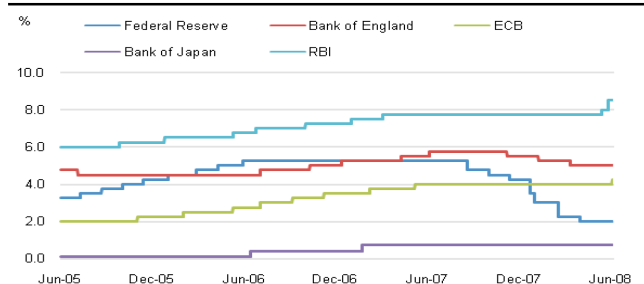
While the short and medium-term inflationary pressures have been emphatically acknowledged by all the central banks, monetary tightening has not been forthcoming. For instance, the BOE feels that there are 'conflicting risks to inflation', viz the slowdown in growth could lead to inflation declining (downside risks), while the high commodity prices could lead to inflationary expectations, in which case inflation could increase (upside risks). It did conclude in its latest policy that overall, there are more upside risks (with CPI touching 3%, above its comfort level of 2%).

Going by the BOE's stance, one cannot rule out monetary tightening mneasures by the BOE going forward. However, some dissenting members on its board have been pointing out that the delay in increasing the rates pre-emptively would only increase the costs of bringing inflation back to target. Probably, the relevant question is whether some portion of these costs of delayed decision-making will be faced by Emerging market economies - where, there are no 'conflicts' about the direction of inflation ie., upwards.

ECB firmly hawkish

The European Central Bank's (ECB) stance clearly remains hawkish. As expected, it increased its policy rate from 4% to 4.25% on July 3, 2008. It noted that risks to price stability over the medium term (18-24 months) have further increased. Inflation rates have risen significantly (to 3.6% vis-à-vis its comfort level of 2%) owing mainly to strong increases in energy and food prices. Importantly, the bank expects inflation to remain high for a more protracted period than previously envisaged.

Exhibit 13: Global Bank Rates



Source: Bloomberg, Angel Research

Strategy

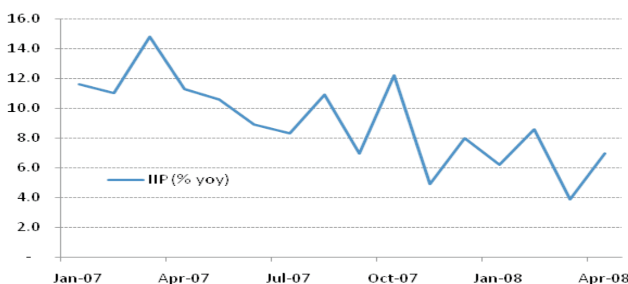
The RBI - Amongst the most prudent central banks

While supply-side measures are being explored, one has to address the scenario that supply-side relief maybe elusive in the near term. At some point, the central banks will have to consider the option of painstaking tightening money supply to bring down demand to a point where prices have to cool off even at the cost of growth.

As stated in our Monetary Poiicy Preview, notwithstanding that the current inflation is mainly driven by international commodity prices, the rate of inflation being as high as it is, the RBI has virtually no leeway to risk demand-driven inflation also emerging. Money supply (M3) continues to grow at 21%+, well above the RBI's comfort level of 16.5-17%. Aggregate deposits grew by 23% yoy on June 6, 2008, which is above its comfort level of 17% while credit growth was 25%, again above the indicative projection of 20%. In fact, while justifying the twin rate hikes, the RBI observed that aggregate demand pressures appear to be strong.

It noted that investment demand continues to be strong, growing at 14-19% annually since 2002-03 and currently constitutes 36% of GDP. This is also reflected in the pick-up in the growth of domestic capital goods production in April 2008 after some deceleration in January-March 2008.

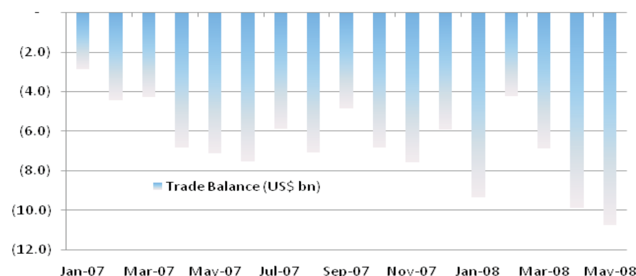
Exhibit 14: Monthly IIP growth



Source: Bloomberg, Angel Research

The trade deficit widened sizeably in 2007-08 and continued to expand in April and May 2008.

Exhibit 15: Trade Deficit



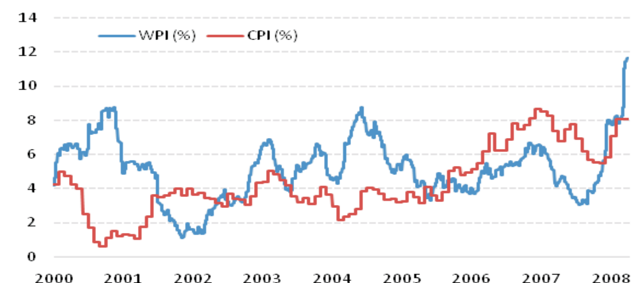
Source: Bloomberg, Angel Research

Although large oil imports are the main driver, the RBI observed that non-oil imports have also increased considerably contributing more than 60% of the overall import growth in April and May 2008, and reflecting the pressure of domestic demand.

Concerns over second-round effects of inflationary expectations

All central banks, including the RBI, are in a state of vigil with respect to the second-round inflationary effects ie., this far the wholesale price inflation (WPI) has been increasing due to high global commodity prices. Eventually, there is a risk that prices of consumer goods and services, wages, etc., could start showing an upward trend if the inflationary expectations are not appropriately anchored.

Exhibit 16: WPI v/s CPI



Source: Bloomberg, Angel Research

For instance, in India, a year ago WPI was 4.3%, while the consumer price inflation (CPI) was in the range of 6.7-7.7%. Now, WPI has increased to 11.4%, while CPI is in the range of 7-7.8%. Similar concerns are evident in ECB's stance and to a lesser extent in the stance of the BOE, BOJ (Bank of Japan) and the US Fed.

Strategy

Can the RBI control Inflation single handedly?

'Unilateral' tightening by the RBI may not work

The RBI's problem lies in the fact that it can only control Rupee supply and put the brakes on domestic aggregate demand. However, commodities are being chased by global liquidity. Hence, merely controlling Rupee supply may not be enough.

Exploring various scenarios

Currently, the stance of most central banks, including the RBI, suggests that they are poised to either maintain rates (in case of those where downsides to domestic growth are more pronounced) or increase rates (where inflation is unequivocally the major concern).

In case of the US economy, it has gone through a period of substantial turbulence. The US labour, housing and capital markets continue to witness a slowdown. It is possible that demand in the US economy (especially for imported goods and oil) will progressively unwind and will consequently impact exporting regions like China and the Middle East. Once the second-round effects of decelerating growth in China and the Middle East start takes root, it is possible that the rise in global commodity prices will start reversing.

If the US consumption does not come down meaningfully, we believe that concerted monetary tightening by all major central banks could address the global inflation problem far more effectively than unilateral tightening by few banks.

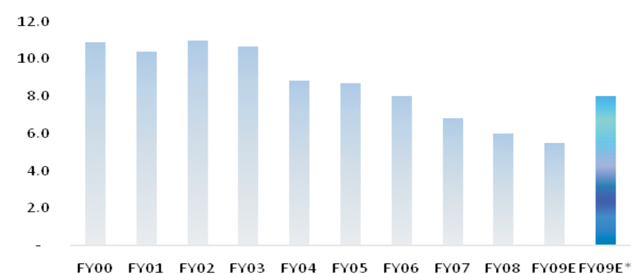
For instance, there is a possibility that rigorous tightening of Rupee supply by the RBI may choke domestic growth, reduce domestic consumption and demand, make imports more expensive for domestic consumers and corporates and yet fail to tame inflation, which is being caused by global demand-supply mismatches and will continue unless all central banks clamp down on aggregate demand.

On the other hand, if the major central banks were to initiate monetary tightening, it would mean some pain in the short term (by way of credit contraction, fall in asset prices due to a shrinking pool of global capital and possibly short-term recession). However, there would atleast be visibility of resolution of economic imbalances and subsequent economic recovery.

It all adds up to pressure on Fiscal Deficit…

Over the last few years, India has done exceedingly well at reducing its fiscal deficit. However, higher crude oil prices, a depreciating Rupee, greater oil subsidies in the form of higher issuance of oil bonds, fertiliser subsidies, farm loan waiver, the Sixth Pay Commission, reduction in effective tax rates, etc., will all eventually contribute in adversely impacting the fiscal position of the economy, even though some of these are off-balance sheet items.

Exhibit 17: Gross Fiscal Deficit as % of GDP

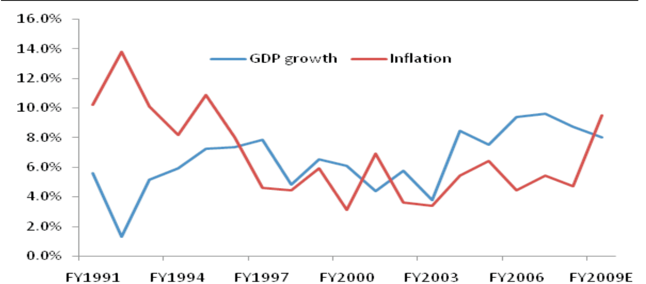


*Source: RBI, Angel Research; * Including off - balance sheet items*

…and consequently India's economic growth

Overall, In the wake of the global economic slowdown, increasing global and domestic interest rates scenario on account of high inflation and increasing pressure on government finances, there is no denial of the fact that India's economic growth is headed for a slowdown and this is supported by past experiences. The GDP growth numbers have already been scaled down from 9%+ to 7-8%, with some estimates suggesting a 6.5% growth.

Exhibit 18: Inflation v/s GDP



Source: Bloomberg, Angel Research

Strategy

Silver lining...

Admittedly, the going has been tough for investors in 2008 to-date. However, to wish away equities just because it has given negative returns over the last 12-months, would be not doing justice to this asset class considering that the equity as an asset class gives good returns over a longer period of time. Further, despite the steep correction witnessed in 2008, the Sensex has moved up 272% (point-to-point) since July 2003 and is up 85% since July 2005, which is no small feat by any standards!

Exhibit 19: Sensex returns (%)

1m	3m	6m	1yr	2yrs	3yrs	4yrs	5yrs
(13.3)	(12.3)	(35.0)	(9.6)	26.2	84.9	176.2	271.5

Source: C-line

We believe, oil, which is the biggest concern at the current juncture, has led to other challenges. But, we believe that hereon oil will not move much higher. If we look back in history, we can gauge the direction that the oil prices are headed towards.

Consider, oil's weightage to the global GDP has risen from 3% to over 6% - reaching levels similar to the one witnessed during the oil crisis of the 1980s, which pushed the world into an economic slowdown. Thus, repercussions are not unpredictable. Nonetheless, while the record high crude oil prices will cause a dent in the global economic growth, we firmly believe that a slowdown in economic growth and soaring oil prices cannot go hand-in-hand for long.

Further, unlike earlier oil crises, in which economic growth was affected owing to the rising oil prices, today the developed economies are already facing challenging times, which was triggered by the sub-prime crises and now the global property market collapse. US, the largest consumer of oil at 25% of the global oil output, is already facing a tough economic scenario. Rising crude oil prices will further de-rail its economic growth alongside that of many other countries.

Not surprisingly, developed countries have already started raising concerns against the high crude oil prices urging other countries to deliberate on the use of alternate energy sources and, if need be, make collective representation to the crude oil-producing countries. Notably, the OPEC nations are restricting incremental supplies which would have otherwise met the rising global demand (OPEC countries' marketshare has started to fall). If the OPEC countries sustain such practices, we believe they may be headed for direct confrontation with the developed countries.

Our optimism however, stems from the fact that even in the absence of significant pressure; Saudi Arabia has decided to increase its output by 0.5mn barrels/day. Further, the recent oil summit in Jeddah saw further co-operation by Saudi Arabia, which agreed to increase oil supply 'if customers request', with the intention of arresting the crude price rise. **These developments signal that it is only a matter of time before the oil prices cool down - either through increased supply from OPEC or lessened demand for oil as a result of economic conditions.** Notably, early signs of *'demand destruction'* are already visible in the US and Europe, where car sales and driver miles have been falling. In fact, recently, as per the Energy Information Administration (EIA), US oil consumption came in at six-year lows on account of the rising oil prices and slowing economy.

We believe, once the oil prices start to cool off, the global economies will start to stabilise. Inflationary expectations and inflation would start to recede and policy makers would start to incorporate a more 'non-hawkish' stance (not necessarily 'dovish' until clearly out of the woods), which would come as a respite for investors and equities.

However, considering that the damage to the economy has already been done, we believe that India's GDP growth rate will slowdown going forward over the next couple of years and could settle in the 7-8% range, which would still be the strongest in the world, second only to China.

Strategy

So, what should investors do?

Ultimately, it is the Earnings that matters!

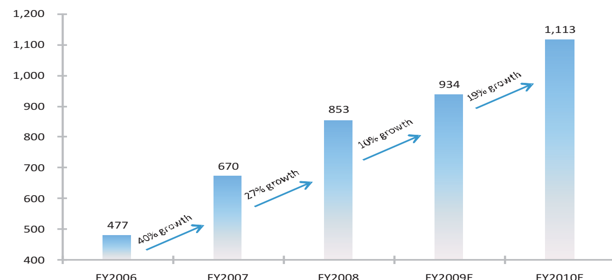
One has often come across the words *'Irrational Exuberance'.* The markets are termed to be irrationally exuberant when, positive sentiment is armed with strong liquidity and cannot be justified by conventional valuation tools. This was witnessed in the bull run until it came to halt in January 2008. We beleive that while a correction is always healthy, one would expect corrections at periodic intervals rather than the one we are currently witnessing, which tends to overshadow investor sentiments and their belief in equities. It sometimes leads to *'Irrational Apathy'*. We believe that we are current ly witnessing irrational apathy in the markets.

Admittedly, while the current correction has been a severe one , however, we believe that it is a cyclical downturn and is part of the structural bull-run that Indian equities would witness over several years to come. The most important barometer that justifies this stance is the Earnings momentum that the Indian companies will be able to sustain over the next few years.

Our calculations reveal that despite the headwinds that India Inc. is currently facing, the Sensex companies will deliver a healthy 16.6% CAGR in Net Profit over FY2008-10E. However, this is lower than our previous estimates (21.1% CAGR over FY2008-10E) on account of two reasons viz., FY2008 Sensex EPS was higher than our estimate and, factoring in of the new challenges that the Indian companies are faced with going forward. However, we believe that the Sensex Earnings will gather pace FY2011 onwards as the current investment phase of India Inc., starts to reflect in their Sales and Profits.

It must however, be noted that compared to our previous Sensex EPS estimates, we have now factored in the Earnings of Reliance Petroleum (RPL) in Reliance Industries (RIL), which is scheduled to commence production from 2HFY2009. Thus, while on a like-to-like basis, we have downgraded our Sensex EPS estimate for FY2009E to Rs963 from Rs976, down 1.3% and for FY2010E to Rs1,123 from Rs1,193, down 5.9%, considering the inclusion of RPL in our Sensex Earnings estimate, the actual impact is lower. Consequently, our Sensex EPS estimates stand lowered by only a marginal 0.2% for FY2009E from Rs976 to Rs974 and for FY2010E from Rs1,193 to Rs1,160, down 2.8%.

Exhibit 20: Sensex EPS (Rs), EPS growth



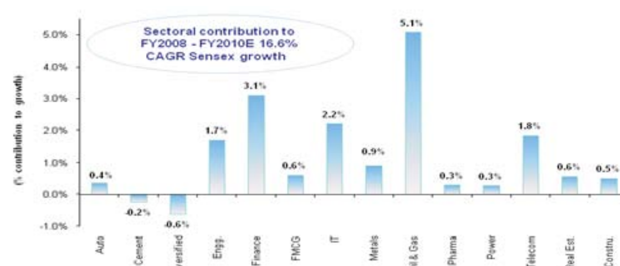
Source: Angel Research

However, an important point to note here is that some Sensex companies have dilutions in the offing, which will dilute the Sensex EPS going forward. Thus, if we take into account this factor, we expect the Sensex EPS to log in a CAGR of 14.2% over FY2008-10E, from the current Rs853 to Rs1,113.

On the sectoral front, we expect the Sensex growth (pre-dilution) over the ensuing years to be contributed by sectors like Oil & Gas, Banking & Finance, Telecom and IT.

For the Sensex over the next couple of years, while RIL would be the biggest contributor, on account of the commencement of facilities of RPL, in which the former has a 70% stake, Banking (despite the recent downgrades) would deliver a robust performance, which is underpinned by strong GDP growth and increasing credit penetration, especially for the large private banks. In the case of IT, apart from the favorable currency movement, we believe that deal visibility remains strong for top-tier IT companies, which would translate into good volume growth. On the Telecom front, there remains tremendous potential for mobile companies to increase teledensity. Thus, volume growth is likely to remain strong. Operating leverage would aid Margins, consequently leading to strong growth in Earnings.

Exhibit 21: Sensex- Sector-wise contribution



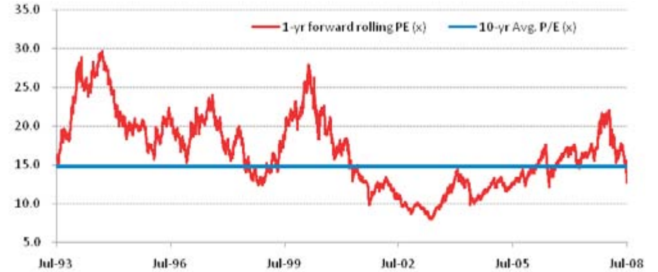
Source: Angel Research

Strategy

Exhibit 22: Sensex - Sectoral Performance

Source: Angel Research

Exhibit 23: Sensex P/E band



Source: Angel Research

Valuations leave little scope for de-rating

Considering current valuations of the Sensex, we believe that there is little scope for further correction. The Sensex is currently trading at 12.1x FY2010E diluted EPS. The long-term (10-year) average P/E of the Sensex is at 14.8x, considering which fair valuation of the Sensex can be pegged at 15x. Thus, we arrive at the fair value of the Sensex at 14,500 (including 500 points for embedded value in Sensex companies) on diluted EPS of Rs934 for FY2009E and fair value of 17,200 (including 500 points for embedded value in Sensex companies) on diluted EPS of Rs1,113 for FY20010E, translating into an upside of 28% from current levels of 13,450.

At current valuations, we believe that the markets have factored in majority of the concerns viz., impact of high crude prices, inflation and rising interest rates. Thus, we believe that we are in a cyclical downturn of a structural bull-run. Hence, any correction in the markets should be used as an opportunity by investors to build a long-term portfolio.

It must be noted that sometimes when it rains it pours, but, *It does not Rain forever*.

Angel Research Model Portfolio

Sector	Top Buys	Recommended Weightage (%)	Sector Comment
Automobile	Maruti Amtek Auto	6% 4%	After significant underperformance in FY2008, high interest rates coupled with rising cost pressures will continue to put pressure on auto volume growth in the near-term. However, the additional fillip provided to disposable incomes during the Budget and reduction in Excise Duty will aid Auto growth in the long run, especially in the small car segment. Relatively, passenger vehicles (PVs) have low elasticity to movement in macro factors. Maruti, being the leader, is expected to outperform the industry, considering the lower penetration in domestic market along with increasing thrust of the company towards exports. On the other hand, Amtek Auto is expected to clock good upside in volumes on the back of enhanced capacity at its Indian plants and added overseas capacities through multiple acquisitions. It is the most attractive stock on valuation parameters in the Auto Ancillary industry.
Banking	ICICI Bank HDFC Bank Axis Bank	12% 7% 6%	The margin-growth trade-off for Indian Banks continues to deteriorate and we expect margins and asset quality to be under pressure in the next few quarters, especially for PSU Banks. Under such circumstances, stock performance may remain under pressure in the near-term. Nonetheless, we believe long-term prospects remain strong, especially for large private banks that continue to gain market share, have strong core profitability and are available at attractive valuations. In the current environment, we prefer these banks also for their high CASA ratios (or the expected improvement in the case of ICICI Bank) and strong momentum in gaining CASA market share.
Infrastructure	Reliance Infrastructure IVRCL	5% 4%	Despite constraints like high commodity prices and firm interest rates, India's long-term growth story is intact. Further, infrastructure players (including IVRCL and Reliance Infra., erstwhile Reliance Energy) have an order book backlog sufficient enough to take care of revenue growth for the next few quarters. Players (like IVRCL) with greater share of orders with price escalation clause are relatively better placed. The interplay of these two forces - revenue growth and margin pressure - will lead to a dichotomy in performance among infrastructure sector players.

Continued...

Angel Research Model Portfolio

Sector	Top Buys	Recommended Weightage (%)	Sector Comment
FMCG	Godrej Consumers GSK Consumer	4% 4%	We continue to remain bullish on the overall prospects of the FMCG sector but prefer a select set of stocks, which are better placed to combat the rising inflationary pressures and sustain margins. Marico is likely to witness moderation in Topline growth and also pressure on Margins. Hence, we suggest a shift to Godrej Consumer as we believe it is likely to surprise the street with positive earnings momentum in the following quarters on the back of aggressive advertising, inorganic growth and new launches.
Oil & Gas	Reliance Ind	11%	Soaring crude oil prices likely to impact the downstream sector which is governed by government policies and regulations. Private upstream companies are expected to benefit from the high crude oil prices while PSU upstream companies don't have significant positive impact. GRMs across the refining sector are likely to remain firm over medium term. Gas sector, being out of the ambit of government policies, is relatively a safe bet. We believe that Reliance stands to benefit from both - higher GRMs and its upstream initiatives.
Pharma	Cadila Piramal Healthcare	3% 3%	Lower penetration of generic drugs in some Regulated markets along with US $100bn worth of drugs going off-patent in the next five years would drive growth. Further, restructuring initiatives undertaken would add to the profitability. Apart from generics, CRAMS provides another opportunity as lower penetration of Indian players along with the cost competitiveness would drive growth and profitability. However on the bourses, the Generic players, especially the large caps (including Dr. Reddy's) have witnessed a huge outperformance mainly aided by positive news flow, which later on got a further boost on back of a stake sale of Ranbaxy. Thus barring a few, the upsides in the generic space is limited. Hence we advice a switch to the CRAMS players (like Piramal Healthcare), which provide good risk-adjusted opportunity.

Continued...

Angel Research Model Portfolio

Sector	Top Buys	Recommended Weightage (%)	Sector Comment
Software	Infosys	6%	Volume growth expected to remain reasonably strong in the region of 20-22% yoy going ahead. Initiatives like platform-based BPO and SaaS are likely to drive non-linear growth in future. Wage inflation and Rupee appreciation are clearly concerns of a much lesser magnitude now than they were before. There has been a slight fall in salary hikes in FY2009, which is likely to continue going ahead. Attrition rates also seem to have stabilised to an extent. With crude hitting record highs, the Rupee will remain under pressure, even as we expect it to appreciate over the longer-term. The extension of STPI tax benefits by one year provides welcome relief on the tax front also. Satyam replaces Wipro in our Model Portfolio due to greater consistency in volume growth and better margin management.
	TCS	6%	
	Satyam	5%	
Telecom	Bharti Airtel	5%	There is tremendous potential for mobile companies to increase mobile teledensity (25% currently), which will aid robust volume growth. With India growing at a strong pace, there is strong growth potential in the enterprise space also, apart from ILD and NLD services. Operating leverage and scale benefits will defend Operating Margins, thus ensuring strong Bottomline growth. Positive triggers like hiving off of the tower business to enable value unlocking are also likely to sustain stock price movements. The upcoming 3G spectrum auction will also provide new business opportunities and the launch of 3G services will help sustain ARPUs. Newer business opportunities like DTH and IPTV will also drive growth in the future. We believe that Bharti and Reliance Communication are the best placed to capitalize on the available opportunities.
	Reliance Comm	5%	
Mid-Cap	Bharati Shipyard	4%	Bharati Shipyard is a great beneficiary of the booming capex and replacement demand in the Shipping Industry. Further India currently enjoys 1% of the overall global pie, the same would increase on back of labour cost competitiveness. Expanding capacities and robust order book position would benefit the company post robust growth and maintain its profitability.

Note: Godrej Consumers replaces Marico, Piramal Healthcare replaces Dr. Reddy's and Satyam Computers replaces Wipro in Model Portfolio.

Results Preview - 1QFY2009

Sectoral Outlook

Sector	Key Expectations	Comments
Automobile	● Auto companies witnessed slightly better volume growth during 1QFY2009 despite a quarter full of pessimistic macro economic scenario. In the near term, due to high inflation and rising interest rates, volume growth in sector would be tracked closely over the next couple of quarters. ● Also, we believe going ahead success of the new launches, both in the two-wheeler and four-wheeler segment, will determine the sales fortune of the players.	● For 1QFY2009, we expect the OEMs to post a disappointing Earnings performance owing to high raw material costs and rising interest rates albeit on moderate volumes and realisations. ● OPMs are expected to remain under pressure on higher input costs and intensifying competition.
Auto Ancillary	● Auto Ancillaries are expected to witness moderate growth on slightly better Auto volumes. ● Margins are expected to be under pressure due to high input costs and price hikes not being fully passed on to OEMs. ● A depreciating Rupee is expected to pull up realisation of the companies with high exports exposure.	● Broadly, the sector is expected to deliver a moderate set of numbers for 1QFY2009. ● Amongst the pack, Amtek Auto and Exide Industries could surprise on either side in 1QFY2009.
Banking	● We expect banks' Earnings (especially PSU banks) to be under considerable pressure in the near term as Credit and GDP growth will continue to slow down perceptibly and Asset quality becomes a real concern. With G-Sec yields shooting up in June, banks will have to take substantial mark-to-market (MTM) hits on their bond portfolios in this quarter. As per our estimates, PSU banks under our coverage may suffer MTM losses in the range of 30-50% of their 1QFY2009E pre-provisioning Profits, while private banks' MTM losses may be in the range of 5-20% of their 1QFY2009E pre-provisioning Profits. ● We have reduced our earnings estimates in the range of 17-32% for PSU banks and in the range of 2-15% for private banks under our coverage to take into the MTM losses as well as lower NIMs and higher slippages, following the severity of RBI's stance. We have also reduced our Target prices in the range of 20-30% for PSU and private banks under our coverage.	● The Margin-growth trade-off for Indian Banks continues to deteriorate. We expect Margins and Asset quality to be under pressure over the next few quarters, especially for the PSU Banks. ● Under such circumstances, stock performance may remain under pressure in the near term. ● Nonetheless, we believe long-term prospects continue to be strong, especially for the large private banks that continue to gain market-share, have strong core Profitability and are available at attractive valuations. In the current environment, we also prefer these banks for their high CASA ratios (or the expected improvement in the case of ICICI Bank) and strong momentum in gaining CASA market-share.

Sectoral Outlook

Sector	Key Expectations	Comments
Cement	● Despatchs clocked a decent growth of 7.1% yoy at 43.5mtpa (40.6mtpa) during the quarter. However, production during the quarter clocked relatively slower growth. Exports declined by a substantial 70% during the quarter at 0.3mtpa (1mtpa) due to the ban. However, the ban on exports has been relaxed at the Gujarat Ports and to Nepal. Cement prices were firm during the quarter albeit with some downward pressure. Average all-India prices were higher by around 4.7% yoy and are currently ruling at Rs246/bag (Rs235/bag). However, qoq, all-India average cement prices were almost flat.	● We expect the cement companies to underperfrom the broader markets due to fears of oversupply owing to huge capacity additions over the next 2-3 years. While the raw material costs like coal, freight are rising, players are not able to hike the prices due to the government intervention. However, we believe that cement consumption in India will continue to grow at over 10% CAGR over the next 3-4 years with GDP growth expected to be at 7-5-8% levels. Also, higher allocation for Housing and Infrastructure by the government and private players will boost cement demand in the country.
FMCG	● For 1QFY2009, we expect our FMCG universe to report a robust Topline growth of 15-16% driven by rising consumer spends and higher value growth. However, Earnings for the universe are expected to grow 12-13% dragged by ITC. ● Margins are expected to come under pressure barring a few companies, as a low base, rising crude prices (impacting packaging costs) and input cost inflation will have an impact.	● Nestle, GSK Consumer, Godrej Consumer and Marico are expected to report the strongest Earnings growth during the quarter. Leader, HUL, is expected to report strong numbers owing to pickup in its Personal care portfolio. We expect ITC to post a decline in cigarette volumes (owing to its exit from non-filter cigarette segment). ITC is expected to deliver muted Earnings growth of 6% owing to exaggerated losses in its Non-cigarette FMCG business. ● We remain bullish on the overall prospects of the FMCG sector but prefer select stocks, which are better placed to combat the rising inflationary pressures and sustain Margins. Amongst the Midcaps, we prefer GSK Consumer, Godrej Consumer and Marico. Among the heavyweights, we prefer Nestle, a strong play on the food processing sector in India.
Infrastructure	● For Q1FY2009, we expect all Infra companies to post a healthy growth in Topline in the range of 20-30% on the back of robust order inflows and changing industry dynamics. However, on the Margin front, we expect the pressures to continue. For 1QFY2009, we expect all companies to post a decline in Margins. Margin pressure is expected owing to higher-than-expected commodity prices and rising interest rates.	● Despite constraints like high commodity prices and high interest rates, India's medium-to-long-term growth story is intact. Further, all the infrastructure players in our universe have an order book backlog sufficient to take care of Revenue growth for the next few quarters. Players with a greater share of orders with price escalation clauses are relatively better placed. The interplay of these two forces - Revenue growth and Margin pressure - will lead to a dichotomy in performance among the players. Our Top Picks in the sector are Simplex Infrastructure and IVRCL.

Continued...

Results Preview - 1QFY2009

Sectoral Outlook

Sector	Key Expectations	Comments
Metals	● Metal prices were strong during the quarter. The benchmark HRC prices were higher by 27% yoy and 18% qoq in 1QFY2009. On the non-ferrous front, base metal prices recovered during the quarter, owing to the earthquake in China, power shortage in South Africa, which led to a decline in production and warehouse inventory. Aluminium prices averaged higher by 9% qoq and 7% yoy in 1QFY2009. Spot alumina prices are however, showing signs of stability. Copper prices increased by a substantial 11.5% yoy in 1QFY2009 and higher by 9.3% qoq . Raw material pressures are expected to continue due to supply side constraints and strong demand from China and India.	● We expect demand to have been reasonably strong, particularly in steel, which would aid the Topline of these companies. Higher steel prices during the quarter would also contribute to the Topline growth of the steel companies. However, due to raw material cost pressures during the quarter, Margins of non-integrated players would be under pressure. ● On the Base Metals front, we expect Nalco and Hindalco to deliver decent Topline growth due to strong aluminum and alumina prices. However, they would continue to indicate pressure on Profitability front due to rising input costs and lower Tc/Rc margins.
Oil & Gas	● GRMs for the private as well as PSU refiners are expected to remain firm with RIL once again likely to report over US $15/ bbl while standalone refiners and OMCs would follow their 4QFY2008 GRMs ● Marketing Margins continue to remain under pressure for the OMCs owing to the spike in global crude oil prices With the rise in crude oil prices, we expect ONGC to realise around US $60/ bbl during 1QFY2009 ● Gas transmission and distribution companies will maintain double-digit volume growth except Gujarat Gas, which will report flat growth.	● ONGC's subsidy burden would be higher owing to the surging crude oil prices, hence not much cushioning from high oil prices ● Gas sector is likely to perform better amidst the high oil price environment. Excepting Gujarat Gas, all the Gas sector companies are expected to report healthy Earnings growth
Pharmaceutical	● During the quarter, large cap pharmaceutical companies barring Sun Pharma would post subdued performance. ● On the Operating front, barring few, Margins are expected to remain under pressure. Amongst the large caps Cipla is expected to witness significant Margin pressures, on the other hand Sun Pharmaceutical will witness significant Margin expansion. Among the Mid-caps, Piramal Healthcare and Indoco Remedies are expected to post Margin expansion on the back of increased contribution from the CRAMS segment.	● Among the Indian pack, Sun Pharmaceuticals, Piramal Healthcare and Indoco Remedies are expected to post robust growth on the back of significant Margin expansion.

Continued...

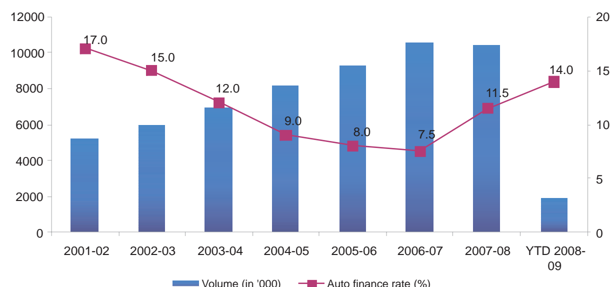
Sectoral Outlook

Sector	Key Expectations	Comments
Power	● We expect the power companies to report decent revenue growth during the 1QFY2009, primarily due to the steep increase in fuel costs. For the companies in our universe, the growth in Top-line is estimated to be 12%. Margins however, are expected to de-growth due to higher employee and other costs.	● The Power sector is witnessing substantial capital expenditure from both public and private sector players. We expect the growth in capacity addition to result in impressive Top-line growth during the next couple of years. Further, the huge correction in the broader index has resulted in the reduction of P/B multiple for these stocks. Nonetheless, we remain positive on the sector even though we are de-rating all the companies in our universe. Our Top Picks in the Power space remain CESC and GIPCL.
Software	● Volumes to grow at 4-5% qoq, with total Revenues, in Rupee terms, expected to grow by 7.5% qoq (including only combined IT Services Business for Wipro); the balance growth is expected to come from favourable currency movements, with the Rupee having depreciated by nearly 5% against the Dollar. Billing rates to be largely stable. ● Margin performance is expected to be encouraging. With an expansion in the region of 40-175bp qoq expected from the top-four software companies. EBITDA in absolute terms is expected to grow by 11% qoq. However, on account of forex losses, Net Profits are expected to grow by 5.9% qoq, considerably slower than EBITDA growth.	● The environment seems to have improved a bit this quarter for the IT Sector, with companies alluding to clients having begun to loosen their purse strings and started spending and offshore continuing to receive greater attention as a move for cost cutting and improving efficiencies. The Rupee depreciation and extension of STPI tax benefits by one year are also positive factors. Wage inflation also seems to have moderated and attrition seems to have stabilised. Sector fundamentals remain strong and we maintain our positive stance on the sector. It is advisable to stick to Top-tier stocks and Mid-cap IT stocks should be selectively picked.
Telecom	● Topline growth is expected to remain strong in the region of 38% yoy on continued buoyancy in subscriber additions, even as ARPUs continue to witness downward pressure. Growth to remain strong in the other business segments as well, namely Enterprise, Broadband and Long Distance. ● Operating leverage in terms of subscriber additions, aided by cost saving initiatives are likely to enable continued Margin strength. However, Idea is expected to report a decline in Margins on account of significant network expansion costs. ● Net Profits are expected to grow by around 25% yoy. However, Idea is likely to record a fall on account of significant forex gains recorded in 1QFY2008.	● Monthly mobile net adds continue to strengthen. We expect telecom majors to continue to report healthy numbers. Mobile teledensity is still at low levels of 25%, leaving strong scope for growth. The government is also progressing well on the spectrum issue, having given spectrum to existing and newer players in several circles. With good GDP growth, we expect the Enterprise segment to also grow at a fast pace. Faster progress on 3G is likely to enable a better experience for consumers. With Idea acquiring Spice, this is a positive for consolidation. However, regulatory uncertainty remains a key risk for the sector. We maintain our positive stance on the sector.

Automobile

The Indian Automobile Sector faced challenging times in FY2008 which has been turning harsher in the beginning of FY2009. We believe the Auto sector will witness near-term pressures with inflation expected to continue to remain high in the ensuing months. In the last three months, the RBI has also hiked cash reserve ratio (CRR) by 125bp and Repo Rate by 75bp (incuding the recent 50bp hike in CRR and Repo Rate, respectively). As a result, lending rates also moved up by 300bp YTD in 2008. Further, following contraction in the availability of finance, conversion ratio (loans approved to loan applied) has dropped by 45% over the past 4-5 months and is expected to remain at low levels in the near future. Volume growth would have to be tracked closely over the next couple of quarters. The scenario was further aggravated by the hike in diesel and petrol prices, which increased the ownership cost of vehicle. Nonetheless, long-term key demand drivers remain intact though, optimal utilisation of new capacity and higher cost of operation are the major constraining factors in FY2009 and continue to be the likely dampeners for the auto companies going ahead.

Exhibit 1: Interest Rates v/s Volumes

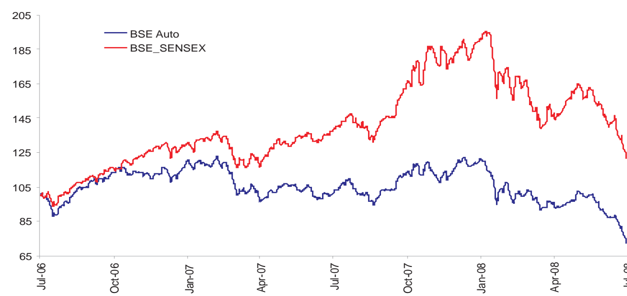


Source: Industry, Angel Research

Overall, while rising input costs, interest rates and fuel costs are concerns, our cost of ownership analysis suggests that the impact this far has been moderate. We believe that it will come with a lag effect and would change the near-term demand outlook for the industry.

Auto Index underperforms 6.8% in 1QFY2009: The Auto Index underperformed the BSE Sensex by 6.8% during the quarter. Sentiment for the Auto stocks had turned negative on concerns over Interest rates rising and players expected to register lower volumes following increasing input costs and low finance availability. The Auto Index declined 20.8% during 1QFY2009. However,Two-wheelers registered a better performance in (volume terms) duirng 1QFY2009 with Bajaj Auto, Hero Honda and TVS combined witnessing a 10.2% yoy rise in total volumes albeit on a low base. Hero Honda outperformed the Auto Index by 19.6% during the quarter on better volume growth.

Exhibit 2: BSE Sensex v/s Auto Index



Source: C-line

Four-wheeler stocks registered a sharp correction on the bourses in 1QFY2009 due to interest rate concerns, though volumes reported were in line with our estimates. However, passenger vehicle (PV) major, Maruti, declined sharply hitting its 52-week low during the quarter. In fact, Maruti was the lone player that surprised with a positive yoy growth during FY2008. However, it suffered a setback in volumes in the last two quarters due to the high base effect. Concerns of slow down due to high base and intensifying competition in FY2009 is expected to keep the stock range bound during 1HFY2009, though some cheer could return with the launch of *A-Star* during 2HFY2009. Tata Motors also hit its 52-week low in 1QFY2009, despite a recovery in commercial vehicle (CV) volume growth. Uncertainties surrounding Tata's acquisition of *Jaguar* and *Land Rover* (J&LR) ended towards end FY2008, though integrated financials are awaited.

Commercial vehicles - Uncertain scenario persists: The M&HCV Goods segment has been on a downtrend since the beginning of FY2008 slipping 0.4% yoy. Freight rates however, started moving up during 2HFY2008 and CV volumes registered a recovery in 4QFY2008. Nonetheless, key risks to CV recovery are contraction in available finance followed by an almost 10% hike (in June 2008) in the diesel prices. These may force truck operators to suspend new purchases till freight rates go up proportionately to compensate for the rise in operating costs. This, combined with the 250-300bp increase in the truck finance rates to around 13% since the start of 2008, is putting a break on growth in FY2009. Tata Motors registered 11% yoy growth in

Automobile

CV volumes during 1QFY2009 on the back of the 15.2% yoy growth witnessed in the LCV segment even as the M&HCV segment grew 6.9% yoy during the quarter.

Exhibit 3: Tata Motors, Ashok Leyland - Quarterly volumes

Segment	1QFY2009					
	2008	2007	%chg	FY2008	FY2007	%chg
Tata Motors	**131,733**	**127,361**	***3.4***	**582,428**	**579,137**	***0.6***
M&HCV	38,369	35,887	*6.9*	179,427	184,948	*(3.0)*
LCV	40,797	35,404	*15.2*	173,434	149,255	*16.2*
Total CV	**79,166**	**71,291**	***11.0***	**352,861**	**334,203**	***5.6***
Utility Vehicles	12,563	10,635	*18.1*	50,299	49,526	*1.6*
Cars	40,004	45,435	*(12.0)*	179,268	195,408	*(8.3)*
Total PV	**52,567**	**56,070**	***(6.2)***	**229,567**	**244,934**	***(6.3)***
Exports (Inc Above)	**9,159**	**13,822**	***(33.7)***	**54,272**	**53,302**	***1.8***
Ashok Leyland	**18,488**	**18,163**	***1.8***	**83,331**	**83,044**	***0.3***
MDV Passenger	4,793	5,128	*(6.5)*	22,271	15,445	*44.2*
MDV Goods	13,450	12,876	*4.5*	60,235	67,296	*(10.5)*
LCV	245	159	*54.1*	825	303	*172.3*
Export (Inc Above)	1,280	1,424	*(10.1)*	7,286	6,025	*20.9*

Source: Company; Angel Research

Passenger Vehicles - Halting growth: As expected, Maruti witnessed a halt in volume growth during 4QFY2008 recording a flat 1.1% yoy growth in volumes. For 1QFY2009 however, on lower base the company recorded 13.5% yoy growth. On qoq basis however, volumes declined by 4.8%. Tata Motors also reported a decline of 6.2% yoy in PV volumes during 1QFY2009.

Exhibit 4: Maruti, M&M - Quarterly volumes

Segment	1QFY2009					
	2008	2007	%chg	FY2008	FY2007	%chg
Maruti Udyog	**192,584**	**169,669**	**13.5**	**764,848**	**674,924**	**13.3**
A1 M800	16,649	17,994	(7.5)	69,543	79,245	(12.2)
C Omni, Versa	20,761	20,631	0.6	89,737	83,091	8.0
A2Alto, Wagon R, Zen,Swift	125,427	110,413	13.6	499,280	440,375	13.4
A3 SX4, Dezire	15,940	11,056	44.2	49,335	29,697	66.1
Total Passenger Cars	**178,777**	**160,094**	**11.7**	**707,960**	**632,408**	**11.9**
MUV Gypsy, Vitara	1316	510	158.0	3927	3221	21.9
Domestic	**180,093**	**160,604**	**12.1**	**711,824**	**635,629**	**12.0**
Exports	**12,491**	**9,065**	**37.8**	**53,024**	**39,295**	**34.9**
M&M	**90,160**	**75,855**	**18.9**	**330,509**	**280,758**	**17.7**
Utility Vehicles	37,919	31,171	21.6	148,759	127,856	16.3
Exports	3,187	2,436	30.8	12,359	8,021	54.1
LCV	2,957	2,681	10.3	10,402	8,652	20.2
Logan	4,595	4,940	(7.0)	25,666	0	-
Three wheelers	11,396	7,336	55.3	33,927	33,700	0.7
Total Automotive	**60,054**	**48,564**	**23.7**	**231,113**	**178,229**	**29.7**
Domestic Tractor	28,004	25,232	11.0	90,723	95,004	(4.5)
Exports Tractor	2,102	2,059	2.1	8,673	7,525	15.3
Total Tractor	**30,106**	**27,291**	**10.3**	**99,396**	**102,529**	**(3.1)**

Source: Company; Angel Research

Two-wheelers - Up on low base: During FY2008, the Two-wheeler segment reported 4.9% yoy decline primarily owing to high inflation, rising interest rates and contraction in availability of finance. However, the Excise duty cut from 16% to 12% came as a relief for the segment. FY2009 began with a positive 10.2% growth albeit on a low base. Combined motorcycle sales for the top-three companies increased by 11.8% yoy during 1QFY2009. Competition continued to intensify between the two-wheeler majors viz., Bajaj Auto (BAL), TVS Motor (TVS) and Hero Honda (HH) with the players announcing launch of new products in different segments. We maintain our cautious view on the segment.

Exhibit 5: BAL, HH, TVS - Quarterly volumes

Segment	1QFY2009					
	2008	2007	%chg	FY2008	FY2007	%chg
Bajaj Auto	**620,095**	**571,113**	**8.6**	**2,450,750**	**2,717,795**	**(9.8)**
Motorcycles	558,633	493,565	13.2	2,139,156	2,376,519	(10.0)
Scooters	3,344	6,212	(46.2)	21,293	19,480	9.3
Total 2 Wheelers	**561,977**	**499,777**	**12.4**	**2,160,449**	**2,395,999**	**(9.8)**
Three Wheelers	58,118	71,336	(18.5)	290,301	321,796	(9.8)
Hero Honda	**894,244**	**802,853**	**11.38**	**3,336,575**	**3,336,756**	**(0.0)**
TVS Motors	**331,789**	**320,161**	**3.6**	**1,288,668**	**1,528,603**	**(15.7)**
Motorcycles	164,328	150,530	9.2	617,801	925,123	(33.2)
Scooters and Mopeds	167,461	169,631	(1.3)	670,867	603,480	11.2

Source: Company; Angel Research

Auto-Ancillaries to track Auto: Post the boom in the domestic Auto sector, the Auto Components segment also registered strong growth till FY2007. During the last five years, the segment clocked CAGR growth of 16%, while Exports grew at a CAGR of over 25%. However, continued appreciation in the Rupee has halted the growth in Exports, which has emerged as a big risk for the Auto Ancillaries. Exports is the key growth driver for the Auto Component manufacturers. Exports largely cater to the US and European markets, and are targeted to meet the requirements of the global OEMs and replacement market. However, high growth visibility in the domestic industry and increasing number of global OEMs entering the segment is expected to aid growth of the Auto Ancillary sector. We estimate the sector to clock a CAGR growth of 15% over the next four-five years. Growth

Automobile

would be driven by OEMs (12%), Replacement market (16%) and Exports (30%). However, we believe the players will have to take a hit on Margins owing to higher investments, raw material costs and stiff competition from Auto Ancillary suppliers from countries like China.

Outlook

Volume growth to be tracked closely in near term: Automobile demand will continue to be driven by new model launches, rising household incomes and increasing affordability. However, due to high inflation and rising interest rates, volumes will be tracked closely over the next couple of quarters. Barring the PV segment, the CV and Two-wheeler segments posted lacklustre performance in FY2008. We believe going ahead success of the new launches and easy availability of finance both in the Two-wheeler and Four-wheeler segments will determine the sales fortune of the players therein. However, in 1HFY2009 players are unlikely to turn in a good performance.

OPM pressures to continue: Input costs have spiraled in the last two years following spurt in the steel, rubber and aluminum prices. FY2008 was no different with the players continuing to face pressure in input costs. Persistent volatility in the metal prices continued during 1QFY2009 as well exerting cost pressures on the companies. As most of the suppliers' contracts are renewed in the first quarter of a fiscal, we estimate OPMs to continue to be under pressure during FY2009. Net Profit growth for most of the players would primarily depend on average realisations and the cost-cutting measures adopted by them.

Moderate growth in the Auto Components segment: The Auto Ancillary sector tracks growth of the Auto sector. Going ahead, increasing efficiencies and supplies by the segment would see more outsourcing opportunities. But, players would have to adjust to any appreciation in the Rupee in the long run while increasing their export targets. This could prove to be an uphill task as countries like China are offering products at comparatively better prices. Broadly, the sector is expected to deliver a not-so-good performance in 1QFY2009 due to the slowdown in overall Auto demand and input cost pressures.

Our Top Picks in the sector are Maruti Suzuki, Amtek Auto, Bosch India and Exide Industries.

Exhibit 6: Quarterly Estimates — Rs cr

Company	CMP	Net Sales		OPM (%)		Net Profit		EPS (Rs)		EPS (Rs)			P/E (x)		Target	Reco
Y/E March	(Rs)	1QFY09E	%chg	1QFY09E	chg bp	1QFY09E	% chg	1QFY09E	% chg	FY09E	FY10E	%chg	FY09E	FY10E	Price (Rs)	
Ashok Leyland	28.7	1,723.5	6.3	12.2	(100.1)	83.4	(5.4)	0.6	(5.4)	3.5	4.0	14.9	8.3	7.2	-	Neutral
Bajaj Auto	420	2,312.9	9.7	12.5	(55.6)	197.5	(12.8)	13.6	(39.0)	60.0	68.4	14.1	7.0	6.1	-	Neutral
Hero Honda	661	2,781.3	13.6	13.3	253.4	253.1	33.3	12.7	33.3	54.7	58.5	6.9	12.1	11.3	-	Neutral
Maruti	550	4,548.1	15.7	12.2	(247.3)	441.3	(11.7)	15.3	(11.7)	66.2	77.6	17.2	8.3	7.1	853	Buy
M&M	475	3,320.1	27.1	11.1	49.5	260.2	36.1	10.9	35.6	40.1	45.5	13.4	11.9	10.5	660	Buy
Tata Motors	401	6,670.3	10.1	10.1	(200.0)	432.8	(7.3)	11.2	(7.3)	52.6	55.3	5.3	7.6	7.2	-	Neutral
TVS Motor	26	844.3	7.8	2.0	(44.1)	6.2	(17.5)	0.3	(17.5)	1.2	2.7	116.9	21.1	9.7	-	Neutral

Source: Company, Angel Research; Price as on July 4, 2008. Note: M&M and Tata Motor Earnings adjusted for extraordinary items.

Exhibit 7: Quarterly Estimates — Rs cr

Company	CMP	Net Sales		OPM (%)		Net Profit		EPS (Rs)		EPS (Rs)			P/E (x)		Target	Reco
Y/E March	(Rs)	1QFY09E	%chg	1QFY09E	chg bp	1QFY09E	% chg	1QFY09E	% chg	FY09E	FY10E	%chg	FY09E	FY10E	Price (Rs)	
Bosch India#	3,753	1,172.4	10.0	18.4	(230.0)	143.1	(12.9)	44.7	(12.9)	186.9	216.6	15.9	20.1	17.3	4,336	Buy
Bharat Forge*	228	1,061.4	1.0	16.0	218.6	68.9	(14.4)	3.1	(14.4)	18.2	20.2	11.1	12.5	11.3	300	Buy
Motherson Sumi*	75	564.6	25.0	15.0	(85.2)	44.3	16.3	1.2	16.3	5.4	6.3	17.6	13.9	11.8	111	Buy
Exide Industries	64	863.1	30.0	14.3	(549.2)	63.9	(11.3)	0.8	(16.8)	3.6	4.5	24.6	17.6	14.1	80	Buy
Rico Auto*	18	224.9	5.0	8.5	(550.0)	(1.3)	(115.4)	(0.1)	(115.0)	2.0	2.7	33.6	8.9	6.7	-	Neutral
Automotive Axle^	209	184.3	25.0	13.0	(166.9)	12.0	0.1	7.9	0.1	35.7	40.7	14.0	5.8	5.1	350	Buy
Subros	28	168.6	6.9	11.9	(26.2)	5.9	(10.5)	1.0	(10.5)	5.4	6.2	15.8	5.2	4.5	42	Buy
Sona Koyo	29	168.1	10.1	6.6	(390.8)	3.4	(57.7)	0.3	(57.7)	3.5	4.4	28.8	8.4	6.5	45	Buy
Amtek Auto@	229	1,375.2	5.0	18.0	147.4	108.2	29.6	7.6	28.2	30.9	36.2	17.2	7.4	6.3	330	Buy
Amtek India@	91	291.2	5.0	22.5	(284.6)	31.8	(15.9)	2.8	(31.0)	11.7	13.4	14.6	7.8	6.8	135	Buy
Ahmednagar Forge@	90	165.7	10.0	18.0	(293.3)	14.0	(15.7)	4.0	(19.8)	18.5	22.5	21.7	4.9	4.0	135	Buy
FAG bearing#	366	162.8	5.0	18.0	(419.8)	18.4	(13.2)	11.1	(13.2)	48.3	52.7	9.3	7.6	6.9	575	Buy

*Source: Company, Angel Research; Price as on July 4, 2008.; * Consolidated Results; # Y/E December ; ^ Y/E September ; @ Y/E June ; Note: FY09E and FY10E Earnings calculated on fully diluted Equity Shares.*

Analyst **- Vaishali Jajoo**

Banking

NIMs to be under pressure; MTM losses expected

We expect banks' earnings, especially PSU banks, will be under considerable pressure in the near term as Credit and GDP growth continue to slow down perceptibly and Asset quality becomes a real concern. Moreover, with G-Sec yields shooting up in June, banks will have to take substantial mark-to-market (MTM) hits on their Bond portfolios this quarter. As per our estimates, the PSU banks under our coverage may suffer MTM losses in the range of 30-50% of their 1QFY2009E Pre-provisioning Profits, while MTM losses of the private banks may range between 5-20% of their 1QFY2009E Pre-provisioning Profits.

Earnings and Target Prices reduced

We have reduced our Earnings estimates for our universe of stocks (by 17-32% for the PSU banks and by 2-15% for the private banks) to factor in the MTM losses, lower NIMs and higher slippages, following RBI's severe stance. We have also reduced our Target Prices by 20-30% for the PSU and private banks under our coverage.

Key developments during 1QFY2009

Runaway Inflation overshadows all concerns

The Wholesale Price Index (WPI) breached 13-year highs, increasing 11.4% yoy for the week ended June 14, 2008. This runaway inflation prompted severe tightening by the RBI in the form of 50bp hike each in CRR and Repo Rate. The RBI has further indicated its intention to clamp down on any inflationary pressures or expectations driven by aggregate demand. In such a scenario, further tightening action by the RBI cannot be ruled out.

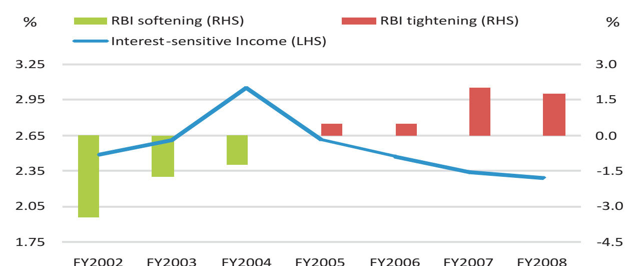
Monetary tightening and Earnings pressures

The RBI has more or less been in tightening mode over the past 3 years. During this period, balance sheet growth has been strong across the Banking sector, especially for private banks. With demand for credit having been strong, banks progressively increased deposit rates with commensurate hikes in Prime Lending Rates (PLR), as the RBI continued to tighten money supply.

Clearly though, growth in Net Interest Income (NII) has increasingly lagged growth in earning assets since FY2006, with NII growth being 12% in FY2008 as against 24% growth in earning assets. Analysing the Interest-sensitive portion of banks' income (comprising NII, Treasury and Provisioning expenses, including credit costs and MTM losses), as a percentage of average earning assets, the ratio has clearly trended downwards since FY2005 notwithstanding strong demand for credit, due to its stronger correlation with the RBI's monetary stance and consequent softening/hardening of interest rates, juxtaposed with inevitable market share dynamics.

Already, in FY2009 so far, the Repo rate and CRR have been hiked by 75bp each. Against the backdrop of high inflation, we expect further tightening measures by the RBI in the form of CRR and/or Repo rate hikes. We believe the Margin-growth trade-off for Indian Banks continues to deteriorate and we expect Margins and Asset quality to be under pressure in FY2009E, especially for the PSU Banks.

Exhibit 1: Interest-sensitive income



Source: Company, Bloomberg, Angel Research; Note: RBI softening/tightening calculated as cumulative CRR and/or Repo rate cut / hike during a year only to show the degree and direction of RBI's monetary stance

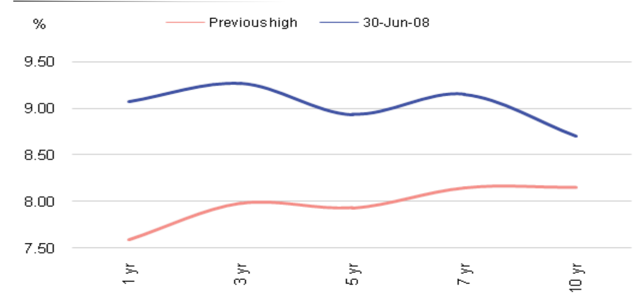
G-Sec yields shot up in June: Yields on G-secs shot up considerably in June as inflation crossed 11% and it became evident that the economy was headed for another round of monetary tightening. Yields have hardened far more at the short-end of the curve, with the yield curve being inverted at present (indicating that the market expects inflation and interest rates to recede in the medium term).

Large MTM losses: In this scenario, banks will have to take substantial mark-to-market (MTM) hits on their bond portfolios in this quarter. Banks have to mark down the investments in SLR securities held in the Available For Sale (AFS) and Held For Trade (HFT) portfolios, as well as all non-SLR securities at the end of every quarter.

Banking

Securities held in the AFS and HFT portfolios usually have a lower duration (1.5 to 3 years at present) than in the Held To Maturity (HTM) portfolio. At the shorter end, yields have gone up by as much as 100-125bp. Although most banks have pared down their holdings in the AFS and HFT portfolios substantially in the past 1-2 years, the % of investments in the same still remain in the range of 25-30% for most . This is partly because excess SLR holdings (above 25% of Net Demand and Time Liabilities (NDTL)) have to compulsorily be held in the AFS portfolio. This stipulation will hurt banks like Indian Overseas Bank (IOB) and Indian Bank the most as they had substantial excess SLR holdings (almost 5% of NDTL) at the end of FY2008.

Exhibit 2: Current yield curve (G-Sec) v/s previous 3-yr highs



Source: Bloomberg,

AFS-to-HTM transfers probable: It is probable that a number of banks may have transferred a portion of their AFS portfolio to the HTM category (to the maximum limit of 25% of NDTL) during the 1QFY2009, when the yields had not yet shot up and the mark down would have been far lower.

Earnings estimates reduced: We have reduced our Earnings estimates across the board to take into account the MTM losses, lower NIMs and higher slippages, following the RBI's severe stance.

Exhibit 3: Reduction in earnings estimates

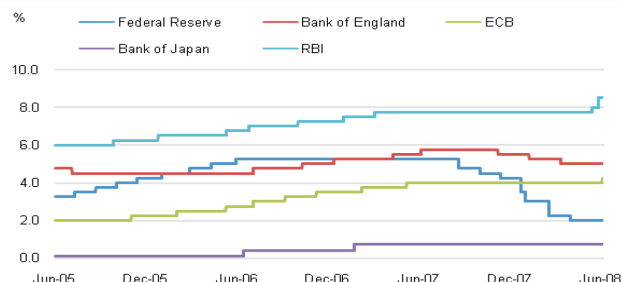
	FY09E EPS		
	New	Earlier	% chg
Axis Bank	38.6	40.6	(5.0)
HDFC Bank	52.2	53.3	(2.1)
ICICI Bank	39.8	46.9	(15.1)
Yes Bank	8.9	8.3	7.5
Corp Bank	46.1	57.5	(19.9)
Indian Bank	16.8	24.7	(31.8)
IOB	21.5	26.0	(17.4)

Source: Company, Angel Research

Global Monetary Stance

RBI can only control rupee supply. However, commodities are being chased by global liquidity and unilateral tightening by RBI may not be enough. With the Banking sector's fortunes hinging on inflation in the near-term, we analyze the monetary stance of major central banks to understand whether a solution lies on the horizon.

Exhibit 4: Policy rates of major central banks



Source: Bloomberg, Angel Research

Fed's stance on inflation still watered down: The US labour, financial and housing markets continue to soften. Accordingly, the US Federal Reserve is still maintaining a watered down stance towards inflationary pressures. **BOE's stance has been somewhat volatile:** The Bank of England (BOE) observed in its latest policy statement, conflicting risks to inflation from demand slowdown (potentially bringing down inflation) and high commodity prices (potentially leading to inflationary expectations). Importantly, it concluded that overall, their were more upside risks to inflation.

ECB remains firmly hawkish: The European Central Bank's (ECB) stance clearly remains hawkish. As expected, it hiked its policy rate to 4.25% to tackle second-round inflationary expectations, given that inflation has risen significantly to 3.6% vis-à-vis the comfort level of 2%. The bank expects inflation to remain high for a more protracted period than previously envisaged.

Second-round inflationary effects: All central banks, including the RBI, are in a state of vigil with respect to second-round inflationary effects ie., so far the WPI has been increasing due to high global commodity prices. Eventually, there is a risk that prices of consumer goods and services, wages, etc., could start showing an upward trend if inflationary expectations are not appropriately anchored. For instance, in India, a year ago, WPI was 4.3%, while CPI was

Banking

in the range of 6.7-7.7%. Now, WPI has increased to 11.4%, while CPI is still in the range of 7-7.8%, indicating incomplete pass-through so far.

Exploring scenarios: The stance of most central banks, including the RBI, suggests that they are poised to either maintain rates (in case of those economies where downside risks to domestic growth are more pronounced) or increase rates (in economies where inflation is unequivocally the major concern).

a) The inflation problem takes care of itself: It is possible that demand in the US economy (especially for imported goods and oil) will trend downwards, having a consequent impact on exporting regions like China and the Middle East. Once the second-round effects of decelerating demand / growth in China and the Middle East start taking root, it is possible that the rise in global commodity prices will start to reverse.

b) Global monetary tightening: If major central banks were to initiate monetary tightening, it would entail some pain in the short term (in the form of credit contraction, fall in asset prices due to a shrinking pool of global capital and possibly short-term cyclical recession). However, there would at least be visibility of resolution of economic imbalances and subsequent economic recovery.

c) Global accommodation, while the RBI tightens further: On the other hand, if major central banks (mainly the Fed and BOE) maintain an accommodative monetary stance to support their domestic economies, while the RBI continues to tighten money supply to anchor inflationary expectations, then the Indian economy could be headed for a more prolonged period of monetary tightening with increasing downside risks to growth as well as longer-than-expected upside risks to inflation.

Outlook

The Margin-growth trade-off for Indian Banks continues to deteriorate. We expect Margins and Asset quality to be under pressure over the next few quarters, especially for the PSU Banks. In fact, the severity of RBI's monetary tightening raises the spectre of sharper-than-expected deceleration in credit growth. Moreover, with an upward bias in respect of Interest rates, MTM losses on banks' bond portfolios will also hurt Profitability in the near-term.

Interest-linked income apart, some degree of deceleration is also expected in Fee income linked to buoyant capital markets. Deterioration in Asset quality of banks' agri-loan portfolios this quarter and for the subsequent few quarters, following the farm loan waiver scheme's impact on repayment culture, will also bear down on sentiment (although we believe repayments will improve once farmers are convinced that new schemes will not be forthcoming and they need funds for the next crop season). The overhang of credit losses related to forex derivative exposures will remain in the near term as well until all losses are quantified and settled one way or the other. Under such circumstances, stock performance may remain under pressure in the near-term. Hence, we are downgrading our Target Prices by 20-30%. Nonetheless, we maintain that the long-term prospects remain strong, especially for the large private banks that continue to gain market-share, have strong core profitability and are available at attractive valuations. In the current environment, we also prefer these banks for their high CASA ratios (or the expected improvement in the case of ICICI Bank) and strong momentum in gaining CASA market-share. **Our Top Picks in the Banking Sector are ICICI Bank, HDFC Bank and Axis Bank.**

Exhibit 5: Quarterly Estimates Rs cr

Company	CMP	Total Income		Net Profit		EPS (Rs)		EPS (Rs)			Adj. B/Value		P/E (x)		P/ABV		Target	Reco
	(Rs)	1QFY09E	*%chg*	1QFY09E	*%chg*	1QFY09E	*%chg*	FY09E	FY10E	*%chg*	FY09E	FY10E	FY09E	FY10E	FY09E	FY10E	Price (Rs)	
Axis Bank	580	1,141	*44.5*	160	*(8.4)*	4.5	*(8.4)*	38.6	49.4	*28.1*	274.4	309.6	15.0	11.7	2.1	1.9	929	Buy
HDFC Bank*	984	2,024	*29.9*	363	*13.0*	10.2	*13.0*	52.2	66.4	*27.2*	447.9	497.9	18.9	14.8	2.2	2.0	1,494	Buy
ICICI Bank	574	4,185	*22.0*	610	*(21.3)*	5.5	*(21.3)*	39.8	52.0	*30.5*	423.8	451.2	14.4	11.0	1.4	1.3	907	Buy
Yes Bank	104	189	*47.3*	42	*16.9*	1.4	*16.9*	8.9	12.1	*35.3*	53.5	75.4	11.7	8.6	1.9	1.4	166	Buy
Corp Bank	263	573	*16.7*	149	*(15.9)*	10.4	*(15.9)*	46.1	58.7	*27.3*	329.9	374.7	5.7	4.5	0.8	0.7	337	Buy
Indian Bank	88	727	*9.4*	61	*(71.4)*	1.4	*(70.1)*	16.8	21.4	*26.9*	121.4	139.3	5.2	4.1	0.7	0.6	-	Neutral
IOB	75	951	*23.4*	132	*(50.7)*	2.4	*(50.7)*	21.5	27.2	*26.8*	101.6	122.9	3.5	2.8	0.7	0.6	123	Buy

*Source: Company, Angel Research; Note: Price as on July4, 2008. * HDFC Bank nos. do not reflect merger with Centurion Bank of Punjab.*

Analyst **- Vaibhav Agrawal**

Cement

Results Preview - 1QFY2009

Cement Stocks tumbled- Challenging times ahead

Cement stocks have been underperforming the broader market since past several quarters, due to the fear of oversupply and rising input costs. The same sentiment rolled over in 1QFY2009 as well, leading to a severe under-performance of cement stocks. Cement stocks underperformed the market in a big way with the relative fall of 15-25% for large cement companies. However in the absolute terms, stocks tumbled more than 30% on an average.

The severe under-performance, in our view was due to the fear of oversupply in the domestic market, rising input costs, which players are unable to pass on (witnessed in last quarter), rising fuel prices during the quarter and the government intervention in the prices due to rising inflation. We believe that the cement stocks continue to under perform and industry to face the tough times ahead.

Exhibit 1: Sensex v/s Cement stocks (1QFY2009)

Cement majors	Abs. returns (%)	Relative to Sensex (%)
Sensex	(14.0)	-
ACC	(36.7)	(22.8)
Grasim	(28.3)	(14.4)
Ultratech	(30.1)	(16.2)
Gujarat Ambuja	(37.4)	(23.5)

Source: BSE, Angel Research

Cement sector was in news through lots of buzzes like cost pressure, cement export ban, import threat, correcting prices and capacity additions. As witnessed in the March quarter, cement players margins were under pressure due to rising input costs and firm cement prices as players were unable to pass on the same to the customers, due to government intervention. We expect this to continue in this quarter as the input cost continues to rise, however the players could not increase the prices. Infact, export ban by the government led to correction in the prices, especially in Gujarat by Rs3-5/Bag. Also on the government request, major cement players had announced the price cuts in the range of Rs5-7/Bag, which will lead to decline in their realizations.

Exhibit 2: All-India Cement Scenario (mtpa)

Particulars	Q1FY2009E	Q1FY2008	*% chg*
Capacity	48.2	42.2	14.2
Production	44.3	43.0	3.0
Cap. Utilization (%)	**92**	**102**	
Despatches	43.5	40.6	7.1
Export	**0.3**	**1.0**	**(70.0)**

Source: Cris Infac, Angel Research

Despatch for the quarter shown the decent growth and grew 7.1% yoy at 43.5mtpa during the quarter from 40.6mtpa in 1QFY2008. However the production during the quarter has shown relatively slower rate. All India Capacity utilization for the quarter declined to 92% from 102%, mainly due to the fresh capacity addition and lower demand ahead of monsoon. Exports, on the other hand, continued to de-grow during the quarter, as companies diverted their supplies to the domestic market to take advantage of the strong demand and prices prevailing in the country. Also export ban in the month of May led to significant decline in exports. Thus, export posted a decline of around 70% during the quarter at 0.3mtpa from 1mtpa in 1QFY2008.

Exhibit 3: Cement prices (Rs/ bag)

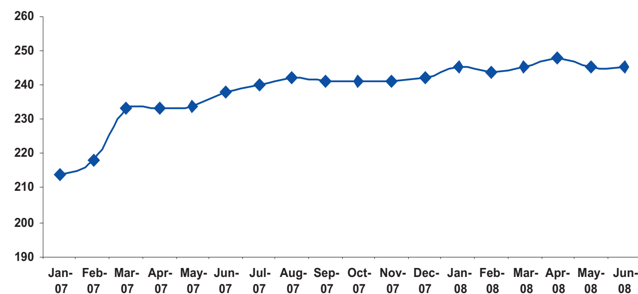
Market	Q1FY2009E	Q1FY2008	*% chg*
Mumbai	270	264	*2.1*
Delhi	240	234	*2.2*
Kolkata	221	212	*4.0*
Chennai	255	230	*11.1*

Source: Cris Infac, Angel Research

All India average cement prices have been firm during the quarter. Major players have been holding the prices in past three months on the government request, due to rising inflation. Average all-India prices were higher by around 4.7% yoy and are currently ruling at around Rs246/bag (Rs235/bag). However, on a qoq basis, all-India average cement prices were almost flat.

Cement

Exhibit 4: All-India average Cement Prices (Rs/bag)



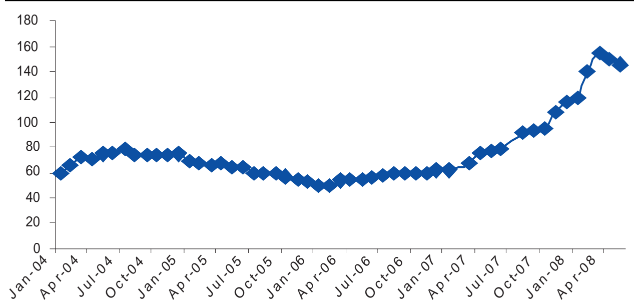
Source: CMA, Angel Research

Cost pressures continues

Cement companies are expected to face considerable pressure on the cost front. Not only did the international coal prices spiked sharply during the quarter which was exacerbated by strengthening freight rates, the domestic coal prices also moved up. The hike in petrol and diesel prices in May 2008 also increased the operating costs for the cement manufacturers as freight costs constitute 20-25% of the operating cost of cement manufacturers.

Cost pressures also witnessed in the previous quarter, led to fall in the operating margins by 500- 600bp for cement companies.

Exhibit 5: MCCLOSKEY - Thermal Coal CIF Asia prices(US $/t)



Source-Bloomberg

Key Developments

Players cut the prices on Government request

In May, the government succeeded in making cement manufacturers to roll back prices by up to Rs7.5/ bag in most of the states. Gujarat saw a cut of Rs5-7/ bag of cement early this month and Rajasthan, along with the central part of the country, witnessed a cut of Rs3-4/ bag. The Andhra Pradesh government also asked cement manufactures to sell at Rs200/ bag. It, however, allowed them to add Rs5 to Rs10/ bag for transporting it to far-off places. Cement companies agree to supply cement at Rs210/ bag in the open market following the discussions held with the Andhra Pradesh Chief Minister

Relaxation of Export Ban - some relief to cement players

Government had banned export of cement on April 11, in a move to check the rising price of cement in the domestic market. However, on May 27, 2008, the government decided to allow export of cement through Gujarat ports, including Mundra and Pipavav. The relaxation was made as construction activity would slow down in the next few months because of the monsoon.

Gujarat accounts for about 90% of the country's cement exports, the move to disallow other states from exporting from Gujarat ports would not make a major impact.

Cement companies based in Gujarat, including Gujarat Ambuja, Binani Industries, Ultratech, Sanghi Cement and Gujarat Siddhee, are understood to have benefited from the move. India exported 3.64mtpa of cement and 2.37mtpa of clinker in 2007-08

Fuel Price hikes also came as a Burden

Fuel price hikes during the quarter has come as yet another burden for the cement industry whose margins are already under pressure, due to rising input costs and firm prices. Cement manufacturers had earlier decided to hold the prices for the next 2-3 months in a move to mitigate inflationary pressures. During the quarter, the government decided to raise petrol prices by Rs5/litre and diesel by Rs3/litre, which will result in freight charges going up. Currently, freight charges are about Rs1.40/tonne/km with an average of about 450-500km.

Cement prices will be impacted by about Rs3-4/ bag and we believe that the cement companies would not be able to pass this burden to the customers, due to government intervention. Also the demand supply situation in India will not warrant companies to increase the prices in the long run.

Cement

Lafarge acquires L&T's unit for US $349mn

Lafarge has acquired engineering giant Larsen & Toubro's concrete business at US $349mn which would give Lafarge a 25% marketshare and leadership in the fast growing readymix concrete market in India. The acquisition will give Lafarge access to 66 concrete plants across the country. Some of these plants are located in key markets such as Delhi, Kolkata, Mumbai and Bangalore, with estimated volumes of 4.1mn cubic metres (in 2008). The acquisition increases Lafarge's presence in the country significantly.

Cement Sector Outlook

We expect cement companies to go through the challenging times due to pressure on the prices and rising input costs. New capacities which are expected to come on stream would put pressure on the prices going forward. While the raw material costs like coal, freight are rising and the players are not able to increase prices due to government intervention. We expect cement companies to post decline in their margins and a de-growth in Bottomline in 1QFY2009. However we expect their topline to grow marginally due to volume growth and firm prices.

Cement consumption in India grew at cagr of 9% in the last five years driven by strong economic growth and booming real estate and infrastructure sectors. We believe that cement consumption in India would continue to grow at over above 10% cagr in next 3-4 years with the GDP growth expected to be at 7-5-8% in next couple of years. Also higher allocation for housing and infrastructure by government and private players will boost cement demand in India.

Over the next 5 years (XIth Plan) investments in construction are expected to be nearly double those that were made in the previous 5 years (Xth Plan). Infrastructure, key industrial and real estate investments reveals that the industry is expected to witness total investments of Rs26, 473bn over the next 5 years as compared with total investments of Rs14, 043bn made in the previous 5 years. Nonetheless, expected capacity additions of 80-85mtpa in next 2 years, is bound to cause disruptions in the cement industry's dynamics and put pressure on the prices. **We maintain our Neutral view on the Sector.**

Exhibit 6: Capacity Addition - Player wise

Companies	Capacity Addition (mtpa)		
	FY09	FY10	Total
ACC	4.2	3.0	7.2
Ambuja Cement	3.0	2.5	5.5
Ultratech	4.9	0.0	4.9
Grasim Ind.	10.2	2.2	12.4
India Cements	3.0	1.3	4.3
Madras Cement	3.0	2.0	5.0
Shree Cement	2.0	5.9	7.9
Jaypee Group	6.5	4.5	11.0
Binani Cement	2.6	0.0	2.6
Others	7.0	18.7	25.7
	46.4	**40.1**	**86.5**

Source: Industry, Angel Research

Exhibit 7: Quarterly Estimates — **Rs cr**

Company	CMP	Net Sales		OPM (%)		Net Profit		EPS (Rs)		EPS (Rs)			EV/Tonne(US $/t)		Target	Reco
	(Rs)	1QFY09E	*%chg*	1QFY09E	*chg bps*	1QFY09E	*% chg*	1QFY09E	*% chg*	FY09E	FY10E	*%chg*	FY09E	FY10E	Price (Rs)	
ACC*	478	1,788	*(4.3)*	24.9	*(420)*	295	*(16.1)*	15.7	*(16.1)*	53.9	60.3	*12.0*	94	81	-	**Neutral**
Ambuja *	75	1,508	*3.0*	30.8	*(640)*	290	*(28.1)*	1.9	*(28.1)*	8.8	8.8	*(0.1)*	135	119	-	**Neutral**
Ultratech	538	1,501	*9.9*	31.1	*(70)*	268	*3.1*	21.5	*3.1*	81.7	68.1	*(16.6)*	88	86	-	**Neutral**
Grasim**	1,693	3,830	*(6.3)*	26.5	*(190)*	469	*(16.0)*	51.1	*(16.0)*	194.9	201.2	*3.2*	98	97	-	**Neutral**

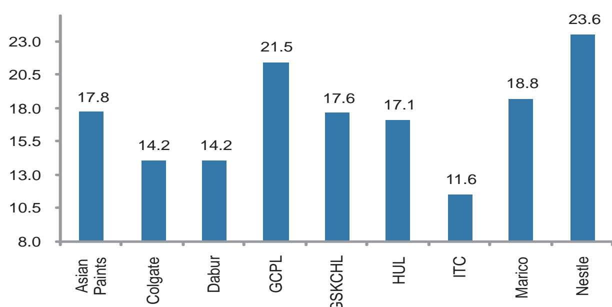
*Source: Company, Angel Research; Note: Price as on July 4, 2008. * December ending; ** Consolidated*

***Analyst* - Pawan Burde**

FMCG

For 1QFY2009, we expect the FMCG sector to clock another quarter of steady growth driven by rising consumer spends, better pricing power, increased levels of promotions and new product launches. However, rising inflation and interest rates coupled with a slowdown in overall economic growth could lead to moderation in consumer spending in the ensuing quarters. For 1QFY2009, we expect our universe of stocks to register a robust 15-16% growth in Topline led by companies like Nestle, Godrej Consumer and Marico.

Exhibit 1: Revenue Trend (1QFY2009E)



Source: Company; Angel Research; Note: HUL, Nestle and GSKCHL figures are for 2QCY2008E

Input cost inflation - 'A manageable threat'

Rising input prices continue to post the biggest threat for the FMCG sector. However, over the past several quarters, most FMCG companies have been able to maintain their Gross Margins. While, price hikes has been the most widely adopted strategy to combat input cost inflation, several companies have resorted to more innovative cost management strategies like tinkering with product size/ weight, forward covers, change in product mix and better supply chain mechanics to tackle this challenge.

Home-care products like detergents and soaps have been the most badly hit owing to constant rise in Palm oil prices and firming LAB prices. Other raw materials, which are on an uptrend, include vegetable oils, milk powder, green coffee, copra and cocoa. Rise in packaging material costs on account of higher crude prices has emerged as another concern area for most FMCG companies.

Pricing Power - 'The magic wand'

Over the last couple of years, FMCG companies have witnessed improved pricing power owing rising consumer spending and their strong brand equity. Most FMCG companies have initiated a weighted average price hike of 5-10% during the last 12 months across product categories to arrest their Margin fall. Categories like Soaps, Laundry, Sunflower Oil, Coffee and Dairy products are some popular categories which have witnessed the maximum rise in prices. ITC raised prices of select brands like *Classic*, *Gold Flake* and *Silk Cut* by 10% during 1QFY2009 to offset rising input costs and compensate for volume loss in non-filter cigarettes category.

We expect this trend to continue, albeit on a lower scale owing to rising competition and adverse impact on volume growth particularly in mass categories. We believe companies like Nestle, HUL, ITC and Colgate are best placed to mitigate input cost inflation via price hikes owing to their dominant market position, diverse product portfolio and strong brand equity.

New Product launches - 'The fuel for growth'

New product launches in the form of variants, extensions or a completely new product will continue to remain the key growth driver for FMCG companies for long-term sustainability. We prefer Personal care and Processed Foods as the two most promising categories.

1QFY2009 was a slightly dull quarter in terms of new launches. In a bid to strengthen its personal care portfolio, ITC announced the launch of *Vivel* shampoos in three variants. Nestle launched *Polo* Xtra *Strong*, an innovation on its existing brand, *Polo*. It also introduced *Maggi Cuppa Mania* instant noodles in two flavours. Dabur is expected to launch a host of new products in Oral and Personal care. It is also assessing opportunities to enter the men's grooming market as well as the ready-to-cook segment.

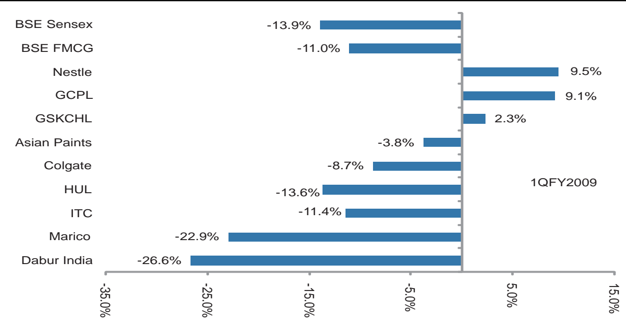
Market Returns - 'Select stocks stand out'

In terms of stock market performance, 1QFY2009 continued to be another strong quarter as the BSE FMCG Index outperformed the BSE Sensex by 2.9%. However, only selective stocks like GCPL, GSK Consumer and Nestle were able to deliver positive returns during the quarter. Amongst the heavyweights, HUL witnessed some profit booking after a strong rally in the previous quarter while ITC dropped on account of concerns regarding its possible volume loss due to exit from the non-filter cigarettes segment and increasing losses in its non-cigarette FMCG business. Among the Midcaps, Marico and Dabur faced the

FMCG

maximum selling pressure during the quarter due to heightened Margin pressures.

Exhibit 2: Stock Performance (1QFY2009)



Source: Company, Angel Research

While we have been overweight on the FMCG sector since the last several quarters, we change our stance to selective stock picking in the future as we expect high inflation and rising interest rates to partially start impacting consumer spending. Hence, companies with leadership in their product categories, diverse product portfolio and stronger pricing power are better placed to combat the inflationary scenario.

Nonetheless, we believe the FMCG sector's defensive nature remains intact owing to its strong Balance Sheets, better Earnings visibility, high Cash Flow generation and rich Dividend yield. **We expect FMCG stocks to continue to command a premium though the overall P/E band could fall in line with Sensex valuations. Hence, we have marginally de-rated the P/Es commanded by our universe of FMCG stocks and have reduced our Target Prices.**

Outlook

According to a recent FICCI report, the FMCG sector is poised to deliver a 16% growth to Rs95,150cr in FY2009 aided by a combination of modest volume growth and higher value growth. Moreover, broad measures like thrust on agriculture, debt waiver to farmers and increase in the threshold limit of income tax are bound to boost consumer spending and in turn benefit the Sector.

For 1QFY2009, we expect our FMCG universe to report a robust Topline growth of 15-16% yoy. However, Earnings growth is expected to remain slightly muted at 12-13% owing to Margin contraction in case of most companies (mainly on account of rising input costs and media inflation). Sector leader, HUL, is expected to report a robust 17.1% Topline growth backed by pickup in its Personal care portfolio and steady growth in its Soaps & Detergents segment. Earnings growth (recurring) is expected to be steady at 14.4% partially impacted by higher base. ITC is expected to witness a 2-3% volume decline in cigarettes during the quarter owing to its exit from the non-filter cigarette segment. ITC is expected to deliver a 11.6% Revenue growth during the quarter. However, Earnings growth is expected to remain muted at 6% owing to exaggerated losses in its Non-cigarette FMCG business. We believe it will be a tough year for ITC. We remain Neutral on the stock.

We maintain our bullish stance on the overall prospects of the FMCG sector but prefer a select set of stocks. Among the Midcaps, we prefer GSK Consumer and Marico which are available at attractive valuations given their steady Earnings growth. We also like Godrej Consumer as we believe it is likely to surprise the street with positive Earnings momentum on the back of aggressive advertising, inorganic growth and new launches. **Among the heavyweights, we prefer Nestle.**

Exhibit 3: Quarterly Estimates — **Rs cr**

Company	CMP	Net Sales		OPM (%)		Net Profit		EPS (Rs)		EPS (Rs)			P/E (x)		Target	Reco
	(Rs)	1QFY09E	*%chg*	1QFY09E	*chg bp*	1QFY09E	*% chg*	1QFY09E	*% chg*	FY09E	FY10E	*%chg*	FY09E	FY10E	Price (Rs)	
Asian Paints ^	1,025	1,131.0	*17.8*	13.3	*(79)*	95.7	*16.8*	10.0	*16.8*	47.6	57.1	*20.0*	21.6	18.0	1,142	**Accumulate**
Colgate	369	400.3	*14.2*	17.4	*(12)*	68.8	*11.2*	5.1	*11.2*	19.0	22.4	*17.5*	19.4	16.5	448	**Buy**
Dabur India ^	76	605.1	*14.2*	14.9	*(9)*	71.5	*14.8*	0.8	*14.8*	4.4	5.1	*15.9*	17.1	14.8	92	**Buy**
GCPL ^	125	347.8	*21.5*	19.2	*134*	51.6	*33.6*	2.3	*33.6*	8.3	9.9	*18.9*	15.0	12.6	168	**Buy**
GSK Cons *	606	371.3	*17.6*	18.7	*16*	50.3	*18.8*	11.9	*18.8*	45.2	52.6	*16.3*	13.4	11.5	789	**Buy**
HUL *	196	4,077.6	*17.1*	14.6	*(15)*	539.7	*14.4*	2.5	*14.4*	9.4	10.7	*14.2*	20.9	18.3	247	**Buy**
ITC	169	3,710.7	*11.6*	32.9	*(101)*	829.9	*6.0*	2.2	*6.0*	9.0	10.4	*15.7*	18.8	16.3	-	**Neutral**
Marico ^	53	557.1	*18.8*	14.0	*(12)*	49.1	*22.2*	0.8	*22.2*	3.0	3.6	*20.9*	17.7	14.6	65	**Buy**
Nestle *	1,616	1,036.5	*23.6*	20.9	*137*	130.4	*36.2*	13.5	*36.2*	57.2	68.0	*18.8*	28.2	23.8	1,767	**Accumulate**

*Source: Company, Angel Research; Note: Price as on July 4, 2008. ; Note: * Y/E December; ^ Consolidated*

***Analyst* - Anand Shah**

Infrastructure

Earnings Outlook

The Infrastructure sector has embarked on a secular growth path led by strong investments by both the government and private sector players across segments including Roads, Ports, Power, Airports, Railways, Urban Planning, etc. We expect the robust order inflows and changing industry dynamics to drive more than 20-30% CAGR growth in Revenues of the infrastructure companies in our universe, for at least the next couple of years. However, on the Margin front we expect the pressures to continue until and unless the commodity prices cool off and interest rates are cut.

Roads on Fast Track

Success in the first few privatisation projects has established the attractiveness of infrastructure as an asset class. Public Private Partnership (PPP) model is the flavour of the season to secure orders in the Road segment as major orders floated by NHAI . Accelerated development of roadways under NHDP has been the bread and butter for major construction companies. Though this entails huge investments, it still plays a crucial role in the order book of the players. NHAI has invited tenders for 34 road projects (3,703kms) at an estimated cost of Rs47,100cr on BOT basis, which is significantly higher than in the last two years ie., FY2008 (1,256kms) and FY2007 (1,624kms). Also, of the 1,256kms awarded in FY2008, 882kms were awarded in January 2008, clearly indicating increasing momentum in terms of projects awarded. Considering the expansion plans chalked out by NHAI, we believe that the pie would keep on increasing going ahead. And as the pie goes up and the order size increases, it's very likely that the organised Infrastructure players would be among the beneficiaries the same. Going ahead, we expect huge orders to flow from the Road segment.

ECB - A sigh of relief

The government has hiked the external commercial borrowing (ECB) limits for the Indian infrastructure companies to US $100mn for Rupee expenditure for permissible end-uses under the approval route. The earlier limit was US $20mn, which was imposed in August 2007. The move is aimed to lend a boost to the Infrastructure sector, which requires US $500bn worth of investments during the Eleventh Five-Year Plan (2007-12), of which US $30bn is expected to come through ECBs.

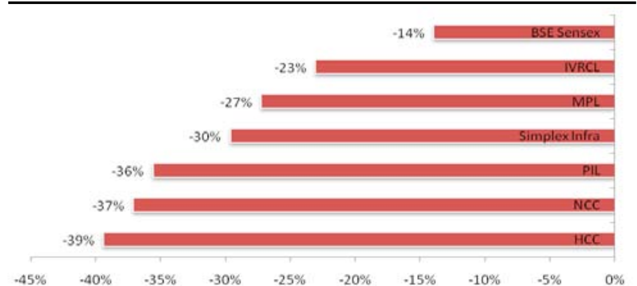
The government has also increased the all-in-cost ceilings for over six months LIBOR in respect of ECBs for an average maturity period between 3-5 years to 200bp from 150bp at present. For borrowings above five years, the cost has increased to 350bp from 250bp at present.

Infrastructure is a capital intensive sector and regular inflow of funds is required to maintain growth. This move will be beneficial for the sector as it would help companies to procure funds at lower interest rates and thereby aid their Margin profile.

Sensex v/s Infrastructure stocks

In terms of stock market performance 1QFY2009 was one of the worst quarters for the Infrastructure space. None of the stocks were able to outperform the BSE Sensex during the quarter. Since the start of the bull-run in May 2003 and till the sharp correction in May-June 2006, all Infrastructure stocks, big and small, had outperformed the Sensex by a huge margin. However, in the quarter under reveiw, there has been clear-cut de-rating of the sector.

Exhibit 1: Relative 'Underperformance' to Sensex



Source: C-Line

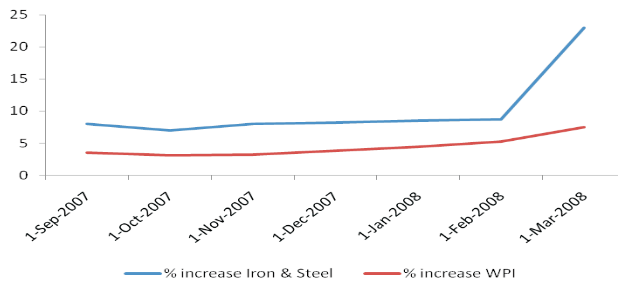
Why this Underperformance?

Infrastructure stocks have registered an underperformance to the Sensex owing the exorbitant commodity prices especially steel (major component in construction work) and high interest rate scenario resulting in contraction of margins of most of the companies. Though 75-80% of the orders have an in-built cost escalation clause (either linked to the WPI or are Star rated contacts) in the contracts, the rise in the steel prices have been above the WPI resulting in contraction of Margins. The HRC steel prices have risen by 26% YTD in CY2008, which are primarily used in pipeline projects. The reinforcement steel (wire rods, primarily used in structural work) prices have also increased by 28% .

Infrastructure

Cement prices have risen by 3% YTD. The diesel prices, which are regulated in India, have risen by 7% YTD. While the construction contractors do build in raw material cost escalations while bidding for the projects, clearly no one had estimated such a sharp rise in the steel prices.

Exhibit 2: Commodity Price Movement v/s WPI



Source: Bloomberg

In the ongoing quarter also we expect margins to be under pressure as there has been no softening in the steel prices and the steel players are expected to further hike the prices. Aggravating these problems, there seems to be no signs of softening of the interest rates, which was expected a few quarters back. On the contrary, certain liquidity tightening measures by the Apex bank has only seen the interest rates firming up in turn exerting further pressure on margins.

Outlook and Valuation

The Infrastructure sector has embarked on a strong PPP mode transforming from the earlier public investment driven mode. Growing number of complex jobs have also given way to the domestic construction companies joining hands with the global leaders to better their pre-qualifications for bagging orders. Investment in infrastructure is expected to be in the range of US $500bn over the next 4-5 years, which would provide substantial opportunity to players in the segment. Further, the overseas markets such as the Middle East continues to tick in strong order inflows for the domestic construction majors.

India is witnessing a slowdown in GDP growth. This is yet to trickle down significantly to the Infrastructure sector. Inflationary pressures deteriorating government finances and political risks led by the upcoming elections could lead to a significant slowdown in the government capex plans. Furthermore, central and most state elections are planned for CY2008-09. Just before or during the elections there could be considerable slowdown in order inflows (FY2009-10E). In past too, during the May 2004 elections, most of the construction companies witnessed a slowdown in order inflow growth particularly in the last quarter preceding the elections (4QFY2004). The ordering substantially picked up during 2HFY2005 leading to significant growth in order inflows for FY2005. General election in a year's time and state elections in Rajasthan and Madhya Pradesh round the corner are some of the factors that could hamper finalisation of orders in the sector. Furthermore, considering that the equity markets are currently not conducive for fund-raising , there is a possibility of slippages for the project owners in achieving financial closures, reflecting a slowdown in order inflow growth.

Despite these constraints, India's medium-to-long-term growth story remains intact. Further, all the infrastructure players in our universe have an order book backlog sufficient to take care of revenue growth for the next few quarters. Players with a greater share of orders with price escalation clauses are relatively better placed. The interplay of these two forces - Revenue growth and Margin pressure - will lead to a dichotomy in performance among the players. **Our Top Picks in the sector are Simplex Infrastructure and IVRCL.**

Exhibit 3: Quarterly Estimates Rs cr

Company	CMP	Net Sales		OPM (%)		Net Profit		EPS (Rs)		EPS (Rs)			P/E (x)		Target	Reco
	(Rs)	1QFY09E	*% chg*	1QFY09E	*chg bp*	1QFY09E	*% chg*	1QFY09E	*% chg*	FY09E	FY10E	*% chg*	FY09E	FY10E	Price (Rs)	
Simplex Infra	449	763.3	*28.4*	9.2	*(66.9)*	19.6	*(0.5)*	3.6	*(22.4)*	24.3	44.5	*83.1*	18.5	10.1	566	Buy
HCC	86	913.1	*25.2*	9.7	*(110.7)*	14.9	*(57.3)*	0.6	*(57.3)*	3.5	6.5	*85.7*	24.6	13.2	140	Buy
NCC	125	978.4	*28.4*	8.7	*(171.2)*	37.2	*(25.5)*	1.6	*(25.5)*	8.6	12.5	*45.3*	14.5	10.0	189	Buy
IVRCL	304	1024.2	*48.4*	8.3	*(44.7)*	38.1	*(47.9)*	2.9	*(47.9)*	18.3	25.0	*36.6*	16.6	12.2	413	Buy
MPL	301	192.3	*34.1*	12.7	*(184.3)*	9.7	*(15.7)*	2.6	*(15.7)*	15.3	18.7	*22.2*	19.7	16.1	477	Buy
PIL	201	105.1	*59.4*	10.5	*(176.9)*	2.3	*(64.5)*	1.4	*(64.5)*	19.8	27.1	*36.9*	10.2	7.4	299	Buy

Source: Company, Angel Research; Note: Price as on July 4, 2008.

***Analyst -* Shailesh Kanani / Neha Soni**

Metals

Metals Index relatively better off

The BSE Metal Index relatively outperformed the broader markets during 1QFY2009, after having underperformed during 4QFY2008 in a big way. The Metal Index declined by a mere 5.2% during 1QFY2009 and outperformed the Sensex by 6.6%. Steel stocks like JSW Steel and Tata Steel out-performed the market. However, base metal stocks like Hindalco and Nalco underperformed the market.

Metals stocks were in the limelight during the quarter abuzz with news-flow such as removal of export tax on flat steel, imposition of ad valorem duty on iron ore exports, rising aluminium prices due to Chinese earthquake, etc.

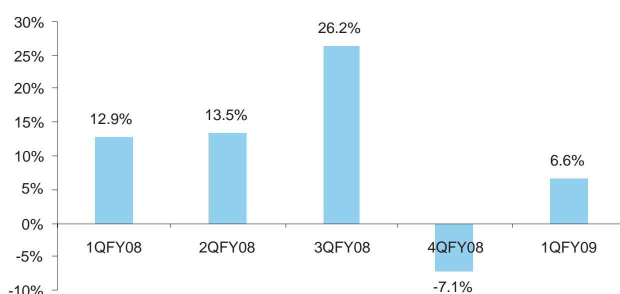
Base metal stocks tumbled despite the aluminium prices ruling strong on the LME due to supply side constraints on account of the Chinese earthquake. However, global slowdown, high interest rates and fears of oversupply led to some sort of profit booking in base metal stocks. Steel stocks performed comparatively better due to anticipation of a hike in the prices, government's move of removal of export tax on flat products and imposition of 15% ad valorem tax on iron ore exports. We expect the steel companies to deliver a relatively stronger performance compared to the non-ferrous players for the quarter owing to the strong pricing scenario and volume growth.

Exhibit 1: Sensex v/s Metal stocks (1QFY2009)

Metal Majors	Abs. Returns (%)	Relative to Sensex (%)
Sensex	(11.8)	0.0
BSE Metals	(5.2)	6.6
SAIL	(22.2)	(10.4)
Tata Steel	4.9	16.7
JSW Steel	19.8	31.6
Hindalco	(15.2)	(3.4)
Nalco	(26.3)	(14.5)

Source: BSE, Angel Research

Exhibit 2: Metal Index Relative Returns to Sensex



Source: BSE, Angel Research

We expect demand to have been reasonably strong, particularly in steel, which would aid the Topline of these companies. Higher steel prices during the quarter would also contribute to the Topline growth of the steel companies. In perspective, the benchmark HRC prices were higher by 27% yoy and 18% qoq in 1QFY2009. On the non-ferrous front, base metal prices also recovered during the quarter mainly due to the earthquake in China, power shortage in South Africa, which led to a decline in production and ultimately warehouse inventory. Average aluminium prices ended 9% higher qoq and 7% yoy during 1QFY2009. Spot alumina prices however, showed signs of stability. Copper prices meanwhile increased by a hefty 11.5% yoy in 1QFY2009 and 9.3% on a qoq basis. Notably, Indian copper manufacturers like Hindalco and Sterlite are primarily custom smelters and hence their performance is linked to the TcRc margins earned by them, which continued to remain under pressure during the quarter.

Steel sector in 1QFY2009

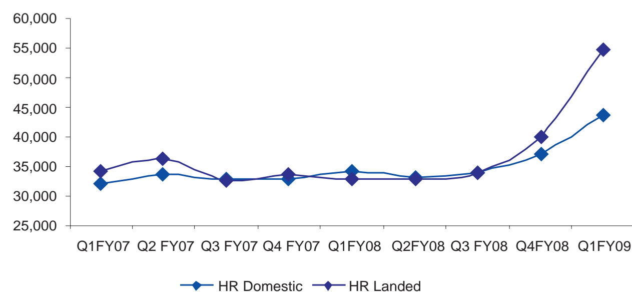
Demand for Steel ruled strong during the quarter mainly due to the robust demand from Emerging countries like India and China. Steel prices have been on an upward trajectory both domestically and globally. Riding input costs like iron ore, coking coal and met coke have led to an unprecedented increase in the steel prices globally. Also, higher freight, and power and fuel costs increased the production costs for the steel manufacturers globally.

In tandem with this, the average domestic HR steel prices also increased by almost 18% during the quarter. However, the major domestic companies have been holding the prices in the past three months at the behest of government to control inflation. But average prices were much higher in 1QFY2009 due to the hefty price hikes effected in March and April. Notably, the average domestic HR prices during the quarter stood at Rs43,753/tonne, up 27% yoy and 18% qoq. However, the global prices have been ruling much higher having increased by 35% yoy and 20% qoq in 1QFY2009. The domestic prices have been trading at almost 25% discount to the international prices giving the steel

Metals

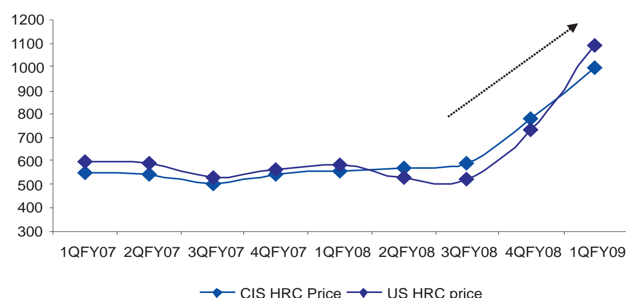
players a hope to increase the prices going ahead. It may be noted here that the difference between the domestic HR and landed prices have widened in the recent past.

Exhibit 3: Domestic HRC Steel Prices (Rs/tonne)



Source: Cris Infac

Exhibit 4: Global Price Trend (US $/tonne)



Source: Bloomberg

Steel prices are on their way up across the globe on the back of the price hikes announced by several players globally. Pertinently, in the US and Europe, steel prices were seen strengthening in the region of US $100-150/tonne during the quarter. The CIS HRC prices increased to US $85/tonne and are currently hovering in the range of US $1,050/tonne. The US HRC prices have increased by a hefty US $300/tonne from US $830/tonne in March to US $1,125/tonne in June. This was partially attributed to the rising input costs of iron ore and met coke even as declining exports from China also aided the uptrend.

Key Developments

After announcing the several stringent measures like restricting exports, removal of DEPB benefits to contain the steel prices, in the last quarter, as a harsh measure to control inflation, Government had introduced an export tax upto 15% on steel products.

Export tax upto 15% on steel

After intense battle of nerves with the steelmakers, in the month of April, government had imposed up to 15% export duty on various steel products to contain rise of steel prices, a move that will hit industry hard. However after that steel players had reduced the prices by as much as Rs4000/tonne on the government's request. To compensate the same, government had promised steel players not to introduce an export tax, but finance minister passed the same in the finance bill, as a move to control inflation.

Ban of export tax on steel; ad valorem tax on iron ore

Thereafter the removal of export tax was under serious consideration, and government finally in June, removed an export tax on flat products, including galvanized products and pipes and tubes. However, rate of export duty on long products such as bars and rods, angles, shapes and sections and wire has been increased from 10% to 15%, to improve their availability in the domestic market.

Also at the same time, government imposed a uniform export tax of 15% on all grades of iron ore, a move which will hit iron ore exports. Export duty on iron ore was so far being levied at specific rates. Lumps and fines having iron content exceeding 62% were charged to duty of Rs300/tonne, while the duty livable on fines with iron content up to 62% was Rs50/tonne.

Removal of export tax on flat products and ad valorem export tax on iron ore came as a relief to steel players during the quarter.

Iron ore becomes more costly

In a recently signed contract, Baosteel has agreed to pay Rio Tinto, iron ore price at 96.5% higher levels from the previous contract price. This is the largest price rise in more than a decade, suggesting the commodities boom is still accelerating. Earlier in February, CVRD has entered into the contract with Asian steel mils for 65% higher price than the earlier price. This indicates that the demand for iron ore in china continues to be strong.

Results Preview - 1QFY2009

Metals

Steel sector outlook

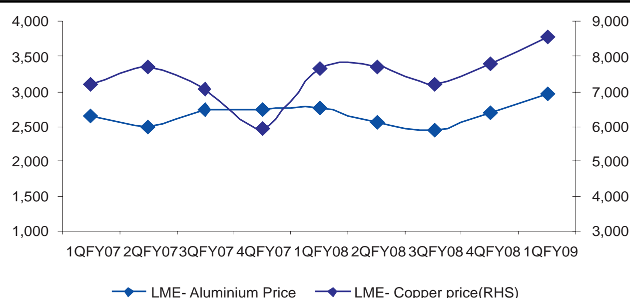
Demand from Emerging markets like India and China is expected to remain strong. We expect strong global demand for steel and U.S. slowdown alone would not be enough to upset the global steel pricing mechanism. Strong demand in regions like the Middle East could offset some softening in US demand. Change in the cost base globally will also keep the prices strong in the short to medium-term. China's initiatives to curb exports and shutting down of inefficient steel mills will also be positive for the global steel industry.

Steel prices remained strong during the quarter and we expect the trend to continue in the medium-term chiefly on account of the strong demand from Emerging markets like India and China, rising input costs of iron ore and met coke and Chinese government's efforts to reduce steel exports. **We recommend a Buy on Tata Steel and JSW Steel.**

Non-ferrous metals in 1QFY2009

Non ferrous metal prices recovered during the quarter led by the supply side constraints from China due to the earthquake during the quarter. Also, power shortage in South Africa led to limited production. In the last quarter too, base metal prices recovered owing to short-term supply problems caused by heavy storms in China and power shortage in South Africa. Average LME Aluminium prices were at US $2,954/tonne during the quarter, up by 9.5% qoq and 7% yoy. On the other hand, average copper prices rose 9.3% yoy at US $8522 in 1QFY2009 from US $7640 in 1QFY2008. However, we believe that the recent recovery in Aluminium and copper prices is due to a short-term supply side problems like earthquake in China, power shortage in Africa, and long term outlook on base metal prices remains weak, due to the surplus in Aluminium market and rising copper inventory. On the alumina front, with China having considerably reduced its import requirements on account of a rise in domestic production, downward pressure has been continued in the alumina prices since the last one year.

Exhibit 5: LME Aluminium and Copper prices (US $/tonne)



Source: LME

Non-Ferrous Metals sector outlook

Demand for base metals is expected to remain strong with China and India maintaining their consumption growth pattern. However, we believe that the expected slowdown in the US and other parts of the world, tightening of interest rates globally would be key risks for base metal consumption. On the domestic front, robust outlook for end user industries viz., automobile, consumer durables, construction, power and packaging, and an estimated GDP growth of 7.5-8% will ensure that demand for metals will remain buoyant. However, we maintain that despite the robust demand outlook, excess supply pressures will lead to a correction in the base metal prices and impact profitability of the companies in these sectors. **Hence, we remain Neutral on Base Metals.**

Exhibit 6: Quarterly Estimates — Rs cr

Company	CMP	Net Sales		OPM (%)		Net Profit		EPS (Rs)		EPS (Rs)			P/E (x)		Target	Reco
	(Rs)	1QFY09E	*%chg*	1QFY09E	*chg bps*	1QFY09E	*% chg*	1QFY09E	*% chg*	FY09E	FY10E	*%chg*	FY09E	FY10E	Price (Rs)	
Hindalco*	138	5,142	*9.9*	15.6	*(330)*	486	*(19.4)*	3.9	*(21.3)*	15.4	15.7	*2.0*	9.0	8.8	-	**Neutral**
Nalco	346	1,387	*19.1*	40.7	*(1,220)*	418	*(6.4)*	6.5	*(6.4)*	24.2	30.4	*25.5*	14.3	11.4	-	**Neutral**
Tata Steel*	640	5,130	*22.2*	42.0	*150*	1,141	*30.6*	15.0	*4.6*	98.6	95.0	*(3.6)*	6.5	6.7	875	**Buy**
SAIL	128	9,959	*23.9*	24.3	*(530)*	1,545	*1.3*	3.7	*1.3*	19.0	17.7	*(6.5)*	6.7	7.2	-	**Neutral**
JSW Steel*	752	3,708	*69.2*	23.0	*(1,008)*	389	*(9.1)*	21.2	*(15.3)*	100.4	131.5	*30.9*	7.5	5.7	1,100	**Buy**

*Source: Company, Angel Research; Note: Price as on July 4, 2008; Note - Full year EPS calculations based on fully diluted equity; Tata Steel Net Profit is adjusted for exceptional items; * FY2009, FY2010 numbers are consolidated*

***Analyst* - Pawan Burde**

Results Preview - 1QFY2009

Oil & Gas

Crude oil has held the entire world in its sway scaling new highs in a short time span and swiftly. India, which imports 75% of its oil requirement, adopted strict measures including retail fuel hikes, duty re-jigs, etc., to bail out the bleeding oil marketing (OMCs) PSUs. The 4QFY2008 results posted by the oil and gas companies were however, satisfactory except for the OMCs.

Finally, a bail out package for the OMCs

The bleeding OMCs received some respite after the Indian government resorted to an all-round bail out package for them. Gross under-recoveries for FY2009 have been envisaged at around Rs2,45,000cr considering the oil price at around US $125/ bbl. The government lowered the Customs Duty and Excise Duty on crude oil and petroleum products. It also hiked the retail prices of Petrol and Diesel by Rs5/ litre and Rs3/ litre, respectively. Although the price of Kerosene (PDS) was left untouched, the government raised price of Domestic LPG by Rs50/ cylinder. Even after these measures, the government has agreed to shell out over Rs94,600cr as oil bonds. The upstream companies breathed a sigh of relief as the government capped their subsidy burden to Rs45,000cr.

Exhibit 1: New under-recovery sharing mechanism

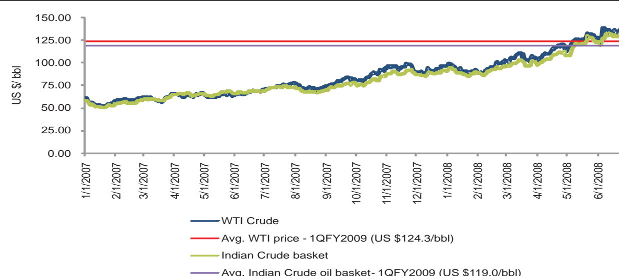
Gross Under-recoveries (Rs cr)	**2,45,000**
Benefit from duty rejig	21,000
Benefit from price hike of Petrol, Diesel and LPG	21,010
Net under-recoveries	2,02,990
Upstream share	45,000
Downstream burden	20,000
To be borne by government	1,37,990
Oil bonds	94,600
Differential to be disbursed later	**43,390**

Source: Petroleum Ministry, Ministry of Finance, Angel Research

Crude - going up, up…

During 4QFY2008, the crude marched past the high of US $110/bbl. But, during 1QFY2009, crude prices shocked the world by breaching US $120/bbl and crossing US $130/bbl and more recently breaching the US $140/bbl mark. Soaring crude oil prices further stoked inflation across geographies. OPEC's emergency meeting failed to assuage the situation even though Saudi Arabia, the world's largest crude oil producer, agreed to raise its production by 2,00,000bbls/day. In fact, OPEC's President forecast the oil prices to hit US $150-170/ bbl in the near term. This reaffirms the belief that oil will continue to rule firm in the near future. Back home, the country's crude basket has appreciated in sync with the international prices and averaged at US $119/ bbl during 1QFY2009.

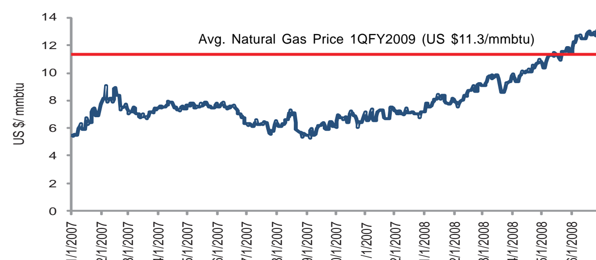
Exhibit 2: WTI Crude, Indian Basket of Crude oil



Source: Bloomberg, Petroleum Ministry, Angel Research

Natural gas prices moving in tandem with crude

Exhibit 3: Henry Hub Natural Gas Price



Source: Bloomberg, Angel Research

Besides the surge in crude oil prices, natural gas prices also spiked during 1QFY2009. A couple of nuclear power plants in Japan have shut down owing to which Japan is resorting to gas-based power, which is driving the natural gas prices. Demand from Korea and some Asian economies has also been rising thus keeping the natural gas prices at high levels.

NELP VII - saved by new players

Even after several postponements, the NELP VII round received a poor response. Out of 57 blocks on offer, 12 blocks failed to receive any bid while 19 blocks received only a single bid. Oil biggies like Chevron, ExxonMobil, Total, etc., shied away from the round while new entrants like LN Mittal, BHP Billiton along with partners showed some interest. A severe blow came in from the Finance Ministry about denial of 7-year tax holiday on gas production, which will impact the existing players as well as the new entrants.

Oil & Gas

Outlook

During 4QFY2008, ONGC's gross realisation was US $100.5/bbl while during 1QFY2009 we expect ONGC to partially gain from the high oil price environment and earn around US $117/bbl of gross realisations. Net realisation is expected at around US $60/bbl, which will be higher sequentially by over US $5.5/bbl. The cap on upstream share in the bailout package is in favour of ONGC, which is expected to shell out around Rs38,000cr of subsidies (about 85% of the total upstream share) to the OMCs. Had it been the normal 33% sharing mechanism, ONGC's performance would have been under threat.

During the beginning of the quarter, the Singapore GRMs declined significantly owing to the spike in crude prices. Indian refiners follow Singapore GRMs. Hence, we believe that the GRMs for Indian refiners would have declined during the early part of 1QFY2009. But, the GRMs have picked up after the initial downturn and expect all the players to report strong GRMs for the quarter. Petrochemical major, Reliance Industries, is expected to once again register strong GRMs for the quarter at around US $15/bbl while firm petchem prices will boost up its overall performance.

The downstream sector is marred by the government policies and decisions and although the government has extended a bail out package, we expect the performance of these companies to be under a threat owing to the ever increasing crude oil prices. Hence, we continue to remain Neutral on all the OMCs.

While crude oil is changing all equations globally and locally, we believe the Gas sector offers a safe bet. The much-awaited city gas distribution (CGD) Policy has been announced and actual effects of the regulations will be observed soon. The Gas Transmission Policy is also awaited. We believe the Policy will further improve visibility of the Gas sector.

From April 1, 2008, GAIL commenced marketing the entire gas output from the PMT field as per the government directive. As a result, Gujarat Gas' volumes were affected as it was sourcing over 80% of its requirement from PMT field. Average daily volumes for Gujarat Gas are expected to drop from around 3.4mmscmd in 1QCY2008 to around 3.0mmscmd in 2QCY2008. Lower gas volumes coupled with higher gas sourcing costs will impact the performance of the company during the quarter. GAIL, which received the rights to market PMT gas, will benefit from marketing this additional gas at a higher price. We expect GAIL's transmission as well as trading volumes to jump from this quarter. Margins on Petrochemicals, and LPG and Liquid Hydrocarbons are expected to remain firm during the quarter.

We expect GSPL to register over 9% yoy volume jump in its transmission business. Average realisations have risen during the last few quarters, which will help the company report over 24% Top-line growth. IGL's CNG volumes are expected to improve by over 15% yoy while PNG volumes (on a lower base) are likely to report over 35% growth. Overall, volume growth will translate into around 16% yoy jump in Top-line. The company is confident of maintaining its OPMs at around 42%. But, sustaining such high Margins over the long term remains a concern. Re-gasification player, Petronet LNG, is expected to report flat volume growth as the new capacity is expected to be operational during 2QFY2009. We expect Revenues to increase by over 8% yoy primarily due to the Rupee depreciation, while Bottom-line will also move up in tandem. We remian positive on the gas sector and **GSPL, GAIL and Gujarat Gas remain our top picks.**

Exhibit 4: Quarterly Estimates — Rs cr

Company	CMP	Net Sales		OPM (%)		Net Profit		EPS (Rs)		Diluted EPS (Rs)			P/E (x)		Target	Reco
	(Rs)	1QFY09E	*% chg*	1QFY09E	*chg bps*	1QFY09E	*% chg*	1QFY09E	*% chg*	FY09E	FY10E	*% chg*	FY09E	FY10E	Price (Rs)	
GAIL	312	5,082	*19.7*	23.4	*(110)*	772.2	*12.7*	9.1	*12.7*	34.6	40.0	*15.7*	9.0	7.8	447	Buy
GSPL	56	119	*24.1*	87.2	*10*	27.0	*50.8*	0.5	*45.5*	2.5	4.1	*64.0*	22.8	13.9	80	Buy
Gujarat Gas *	232	290	*2.3*	20.9	*(320)*	36.0	*(14.3)*	5.6	*(14.3)*	21.7	28.4	*30.9*	10.7	8.2	340	Buy
IGL	108	188	*16.0*	42.3	*(20)*	46.7	*21.6*	3.3	*21.6*	13.6	15.2	*11.8*	7.9	7.1	-	Neutral
Petronet LNG	54	1,680	*8.3*	11.1	*(50)*	116.0	*7.4*	1.6	*7.4*	7.4	7.7	*4.1*	7.2	7.0	80	Buy
ONGC ^	876	15,640	*14.3*	58.2	*30*	5,042.1	*9.4*	23.6	*9.4*	101.0	108.1	*7.0*	8.7	8.1	1135	Buy
RIL ^	2,099	37,657	*27.5*	17.1	*(210)*	4,047.9	*11.5*	29.0	*11.5*	122.0	170.9	*40.1*	17.2	12.3	3344	Buy

*Source: Company, Angel Research, Price as on July 4, 2008;Note - * Calender year, ^ standalone numbers for the quarter and consolidated numbers for full year*

Analyst - **Rohit Nagraj/ Amit Vora**

Pharmaceutical

It's Ranbaxy all the way

Ranbaxy was the news-maker during 1QFY2009. The stake sale by Ranbaxy to Diiachi Sankyo took one and all by surprise. It is the largest deal in the Indian Pharma space this far. At $8.5bn (on fully diluted Equity), Ranbaxy would be valued at 4x EV/Sales and 24.7x EV/EBITDA on CY2009E Earnings. Pertinently, among other firsts, it is the first of its kind of deal between an Innovator and a Generic player.

Contours of the deal: As per the deal, Daiichi has taken over the entire 34.8% stake held by the promoters of Ranbaxy at Rs737 per share. With this, Daiichi would make an open offer for up to 20% additional stake in Ranbaxy. Daiichi would also be issued preferential shares and warrants of 46.3 Mn and 23.8 Mn. respectively, at Rs737/share. Daiichi can exercise the warrants within 6-18 months after the issue. Assuming conversion of the FCCB, fully diluted Equity of Ranbaxy would increase from to 48.6cr, a dilution of 27%.

Benefits accruing to the companies: Post acquisition, Ranbaxy-Daiichi would become the 15th largest Pharmaceutical company in the world. Besides, the acquisition will benefit both companies.

- Daiichi, with sales of $8bn, is ranked 22nd in the global pecking order. The company derives majority of its revenues from the Regulated markets with Japan being the key market. Thus, with this acquisition, Ranbaxy would get access to the proprietary drug portfolio of Daiichi.
- The fund infusion by Daiichi to the tune of $1.2bn through the preferential issue and warrants would enable Ranbaxy to retire its debt. Ranbaxy also expects to have cash surplus of around Rs3,000cr, which would further strengthen its Balance Sheet.
- Acquisition of Ranbaxy would provide Daiichi Sankyo a presence in high-growth Emerging markets like India, China and Eastern Europe. Further, with Ranbaxy being present in more than 40 countries provides a strong front for Daiichi Sankyo to launch its products.
- Along with providing a front-end, the deal also provides Daiichi a strong generic product portfolio with strong visibility on First-To-File (FTF) product (20 FTF products addressing a market opportunity of $26bn) launches over the next few years. Ranbaxy is well-positioned to capture the upsides from the same drawing from its product pipeline. In fact, Ranbaxy's FTF product pipeline is the best in the space and captures major upsides from the large blockbuster drugs going off patent in next few years. Daiichi would leverage Ranbaxy's strengths in the generic markets to strengthen its presence in the emerging generic market in Japan.
- Daiichi would also benefit by leveraging the low-cost advantage of Indian assets both in Manufacturing and R&D. Thus, Daiichi could use Ranbaxy as an out-sourcing hub for its products.

Out-of-court settlements continue: During CY2007, Ranbaxy was at the forefront of inking out-of-court settlements. The trend has continued in CY2008 with the signing of two major out-of-court settlement deals. During the quarter, the company effected out-of-court settlements for *Nexium* and *Lipitor*. These settlements are among the biggest in the space. While *Nexium* sold by AstraZeneca is a $3.8bn opportunity in the US, *Lipitor* (sold by Pfizer) is the world's largest drug grossing sales of $8bn in the US markets.

Agreement with AstraZeneca: According to the deal on *Nexium*, Ranbaxy would be allowed to start exclusive sales of a generic version of the drug in May 2014 in the US. Accordingly, Ranbaxy will be able to sell its copy with 180-day exclusivity on the product. In another pact signed by the two companies, with respective to *Nexium*, Ranbaxy will formulate a significant portion of AstraZeneca's US supply of *Nexium* from May 2010. We have conservatively factored in a 30% supply off-take by AstraZeneca. The agreement also includes provision for supply of raw material for producing Esomeprazole Magnesium from 2009.

Agreement with Pfizer : During the quarter, Ranbaxy also entered into an out-of-court settlement with Pfizer covering *Lipitor, Caduet* and *Quinapril*. With *Lipitor* grossing sales of $12bn globally, it is one of the biggest out-of-court settlement in the Global Generic space. With this settlement in place, Ranbaxy can now launch the product in the US market ($8bn in Sales) after November 2011 with 180-day exclusivity.

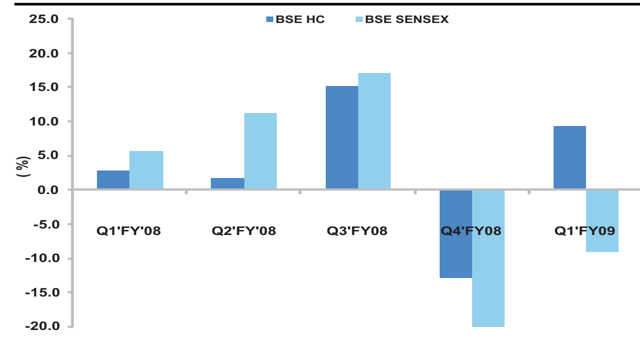
The company also gets 2-4 month exclusivity for other regions including Canada, Belgium, Netherlands, Germany, Sweden, Italy and Australia. Cumulatively, these seven countries gross sales of $2.5bn. Along with Lipitor, the deal also covers Caduet. For Caduet, which has sales of $500mn in the US, the company will get 180-day exclusivity in the US market. Ranbaxy would launch Caduet after November 2011.

Pharmaceutical

Overall, the deal increases visibility about the launch of the products in the US markets. As for the upsides from the products, *Lipitor* is expected to gross Sales of $1.6-1.8bn, while Caduet is expected to gross Sales of $70-80mn during the 180- day exclusivity period.

BSE HC continues out-performance: During the quarter the BSE Healthcare Indice continued its out-performance. Positive news flow from Ranbaxy in terms of out-of-court settlements and the Daiichi deal provided the required fillip to the pharmaceutical counters. Weak markets also aided a shift towards the defensive sectors, which aided a significant outperformance by the Pharmaceutical sector.

Exhibit 1: BSE HC V/s Sensex



Source: C-Line

1QFY2009 expectations: Performance of the Pharma sector during 1QFY2009 is expected to remain lacklustre. Among the Indian large caps, barring DRL, the companies in the space are likely to post a double-digit sales growth, notable among them being Sun Pharmaceuticals. Sun would benefit from launch of *Pantaprazole* in the US markets. The product launch in the US would aid a significant Sales growth and improvement on the Profitability front. Among the other companies, Piramal Healthcare is expected to post robust performance mainly on the back of strong sales growth and better operating performance. Operating Margins are expected to expand on the back of improved sales mix and reduced R&D expenditure during the period. Another pack in the pharmaceutical space, the MNC pharmaceutical companies, are likely to post a subdued performance owing to single digit sales growth and pressure on the operating front.

Outlook and Valuation

The Healthcare Sector has not participated in the bull-run, which was justified as it came on the back of most generic players clocking poor performance. While the Industry pricing woes continue unabated, we believe the worst is over as the Industry has consolidated significantly. While the Indian players continue to be highly competitive, the trend emerging in the global Generic Industry favours only some of them. The same was reflected in the performance of the Pharmaceuticals on the bourses. Over the last six months, the Pharmaceutical companies, especially the large caps, have seen an outperformance on the bourses, while the Mid-cap Pharmaceutical space has not participated in the rally. Going forward, we maintain our stance that the overall macro environment in the generic space favours few and that as a segment within Pharmaceuticals, the CRAMS players would provide better risk-adjusted returns to investors. Hence, in spite of an underperformance, we would advice selective Buying in the space. Currently, we recommend a Buy on **Cadila Healthcare, Alembic, Piramal Healthcare and Indoco Remedies.**

Exhibit 2: Quarterly Estimates **Rs cr**

Company	CMP	Net Sales		OPM (%)		Net Profit		FDEPS (Rs)		FDEPS (Rs)			P/E (x)		Target	Reco
	(Rs)	1QFY09E	*%chg*	1QFY09E	*chg bps*	1QFY09E	*% chg*	1QFY09E	*% chg*	FY09E	FY10E	*%chg*	FY09E	FY10E	Price (Rs)	
Alembic	44	238	*39.6*	14.4	*(260)*	16.9	*(0.8)*	1.2	*(0.8)*	7.2	8.2	*14*	6.2	5.4	74	BUY
Aventis #	720	236	*2.3*	16.0	*(330)*	32.6	*(12.6)*	14.2	*(12.6)*	68.1	80.6	*18*	10.6	8.9	1209	BUY
Cadila	314	675	*20.3*	18.0	*20*	90.4	*22.3*	7.5	*22.3*	25.4	31.5	*24*	12.4	10.0	450	BUY
Cipla	208	1009	*14.6*	18.8	*(500)*	129.3	*7.9*	1.7	*7.9*	10.1	11.1	*10*	20.6	18.7	-	Neutral
Dr. Reddys	646	1293	*9.0*	19.9	*(110)*	175.0	*(6.4)*	10.4	*(6.4)*	41.8	43.0	*3*	15.4	15.0	755	Accumulate
Glaxo #	1139	426	*8.9*	31.2	*(4)*	102.7	*6.5*	12.1	*6.5*	51.6	57.9	*12*	22.1	19.7	1250	Accumulate
Indoco	263	141	*40.5*	27.4	*240*	32.2	*36.8*	24.6	*36.8*	49.1	56.5	*15*	5.4	4.7	460	BUY
Piramal	299	761	*25.1*	19.3	*550*	97.3	*124.2*	4.7	*124.2*	20.0	22.3	*12*	14.9	13.4	430	BUY
Ranbaxy #	538	1858	*15.3*	10.5	*110*	134.2	*(49.1)*	3.6	*(49.1)*	14.7	19.3	*31*	36.6	27.9	-	Neutral
Sun Pharm	1326	961	*56.2*	50.4	*1540*	503.4	*120.9*	26.9	*120.9*	68.6	68.7	*0*	19.3	19.3	-	Neutral
Wockhardt #	182	791	*25.6*	22.4	*(170)*	117.7	*15.3*	10.8	*15.3*	42.1	48.6	*15*	4.3	3.7	300	BUY

Source: Company, Angel Research; Note: Price as on July 4, 2008; Note # -Q2'08, All Price Targets are for 15 Months

***Analyst* - Sarabjit Kour Nangra**

Power

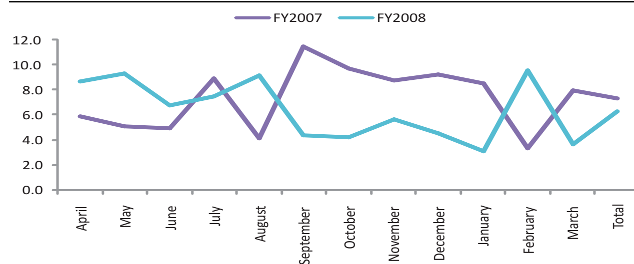
The Indian Economy has been registering healthy average growth of 9% in the last couple of years. However, an overall improvement in the Infrastructure sector is essential to sustain the growth rate. This being the case, development of the Indian Power sector has not been very promising over the years due to inadequate capacity additions in power generation as well as transmission and distribution. Many power projects have suffered road blocks due to various legal, environment and other disputes. The sector has however shown some signs of improvement in the recent past. There has been annual growth in terms of per capita electricity usage, MW of generation, length of transmission and distribution lines and private participation. The total installed power generation capacity in India stood at 143GW as of March 31, 2008. The Eleventh Plan has envisaged capacity addition of 78,577MW. It is pertinent to note here that in the Tenth Plan total capacity added was 21,000MW as against the target of 34,000MW. FY2008 saw a considerably high capacity addition of 10,732MW, as compared to an average modest addition of 3,000MW annually five years earlier. Inadequate capacity addition and huge continuing losses in the Transmission and Distribution (T&D) sector has resulted in the continuing power shortages

Although many private companies have announced huge capacity addition plans with the Top-15 private players alone expected to add 120GW, wherein no significant additions are expected to be made during the Eleventh Plan period. In fact, only a small portion (around 30%) of this is expected to be operational even in the Twelfth Plan. In FY2007-08, the base load deficit was at 9.8% while the peak load deficit was at 16.6%. Even after five years of the enactment of the Electricity Act 2003, benefits of the same are yet to accrue to the consumers. Implementation of substantial changes in the system by way of competition and open access, have not yielded desired results. In Transmission, capacities are expected to be added by the private players through joint ventures with Power Grid in the Eleventh Plan. During the Twelfth Plan, 100% private participation in Transmission is expected.

Power Generation

Power Generation has improved over the last two financial years, though it has failed to meet the targets. In FY2008, total power generation stood at 7,04,451 million units (MU) as against 6,62,693 million units (MU) in FY2007. Power generation grew at 7.3% and 6.3% in FY2007 and FY2008, respectively.

Exhibit 1:Growth in Power Generation (%) (FY2007, FY2008)



Source: CEA, Angel research

Fuel shortage - Order of the day

Coal-fired stations account for 53% of the total installed capacity in India. Around one-third of the 77 thermal stations in the country have now been bracketed as having "critical stocks", of which 13 are reported to be "super critical", with precariously low levels of coal stocks of under four days, according to the Government's latest data on coal stock positions at power stations (up to May 5th, 2008). While coal shortage has been brewing since the beginning of 2007, domestic production is unlikely to be ramped up significantly in the near future. The import option too has been increasingly getting tougher as China, which is also facing low domestic reserves and acute power shortage, has stepped up coal purchases internationally. Lower coal production by Coal India, higher-than-anticipated power generation at some stations and unloading constraints at others, combined with lower imports, have further compounded the problem. Increasing Coal shortage has resulted in the Indian Power companies acquiring coal mines abroad. Reliance Power (RPL) has invested around $1bn (Rs4,300cr) in acquiring and developing a coal mine in the South Sumatra province of Indonesia. The sub-bituminous coal would be supplied to the company's 4,000MW ultra mega power project (UMPP) at Krishnapatnam in Andhra Pradesh, which would go on stream by FY2013. Coal would also be supplied to the 4,000MW Shahapur power project in Maharashta, which has a thermal power component of 1,200MW.

Ultra Mega Power Projects on track

The proposed UMPPs have increased to nine from the four that were initially planned for. There has been a significant improvement in the pace at which the projects are being

Power

awarded. Tata Power, which was awarded the Mundra UMPP, has secured fuel linkages by acquiring equity in two coal mines in Indonesia. The company has also signed equipment contracts with Doosan Heavy Industries and Construction Company and Toshiba Corporation for the supply of super critical boilers and turbines, respectively. Tata Power's Mundra UMPP achieved financial closure in April 2008, becoming the first UMPP to tie up funds. The UMPP, which is expected to cost Rs17,000cr, is being financed at a 75:25 debt-equity ratio. As a positive development, commissioning of the first and second units of the Mundra project have been advanced by 11 and 17 months, from the earlier schedule of April 2012, at the behest of the Central Government.

The Sasan UMPP, which was re-awarded to Reliance Power in August 2007, was awarded the Chattrasal coal block in Madhya Pradesh, with estimated reserves of 150mmt. RPL's Krishnapatnam UMPP, which was awarded in November 2007, received coastal regulation zone clearance during FY2008 and the project is expected to be commissioned between September 2013 and October 2015.

Growth in Power Consumption

The National Electricity Policy envisages that the per capita availability of electricity will increase to over 1,000 units by 2012. The per capita consumption in India has already increased to over 660 units. However, the per capita availability of power in India would be woefully short of the corresponding figures of the developed nations even in 2012. Burgeoning demand for power is largely on account of growth in the commercial and industrial sectors coupled with more villages getting access to electricity as well as increase in the number of electrical and electronic durables. This has resulted in power shortages despite consistent generation growth of over 5%. The fresh generation capacity additions and improvements in plant load factor (PLF) have still not been sufficient to meet the demands of a growing economy resulting in a wide demand-supply gap. The problem is further compounded by an aggregate T&D loss of 34% in the country owing to negligence or lack of the needed investment in the T&D network and power theft.

Performance on the Bourses (1QFY2009)

During 1QFY2009, Power stocks under-performed the benchmark BSE Sensex. While concerns continued to prevail over valuation of the power companies, the sector was impacted by the overall poor performance of the stock markets led by concerns over record inflation, rising high crude oil prices and domestic political uncertainty. In terms of stock-specific performance, CESC was an underperformer during the quarter losing around 4.8%. GIPCL too declined 16.5% while NTPC lost ground by a whopping 23%. BHEL, Reliance Power and Reliance Infrastructure (formerly Reliance Energy) also proved to be a big drag on the Power Index. All this resulted in big FII's exerting selling pressure.

Exhibit 2: Power stocks underperform during 1QFY2009

Power majors	Absolute Returns (%)	Relative to Sensex (%)
Sensex	(14)	
BSE Power	(29)	(15)
NTPC	(23)	(9)
CESC	(4.8)	9.2
GIPCL	(16.5)	(2.5)

Note: Prices as on 30th June '08

Fall in the power pack was the worse in 1QFY2009 with the BSE Power Index declining 29% or double the pace at which the main indices (Sensex fell by 14%) have fallen. The power stocks had witnessed a runaway rally on the bourses primarily due to the investors valuing them like growth stocks. For instance, any announcement of capacity addition for any particular power stock was being factored into its stock price irrespective of possible execution delays and financial closures.

Key developments

NTPC: The company and its subsidiary Nabinagar power plant awarded BHEL a Rs3,500cr contract for supplying boiler-turbine-generator (BTG) for two different projects at Bongaigoan and Nabinagar aggregating to 1,750MW. Total cost of setting up these units will be around Rs8,700cr. NTPC's 500MW Unit-I at Sipat Super Thermal Power Project, Stage-II commenced commercial operations during the quarter. NTPC is expected to add 3,000MW for commercial purposes during FY2009. It has lined up over Rs13,200cr capex for the current fiscal. Power Finance Corporation (PFC) would be lending Rs10,000cr for various projects to be completed by the company during the Eleventh Five Year Plan. The PFC loans would be partially utilised for the projects being undertaken in FY2009.

Power

CESC: Progress on the 250MW project (third unit) at Budge Budge has been satisfactory and loan disbursements for the project are continuing. The company has acquired 70% of the land to be used for Phase I of the Haldia Project (600MW). Coal linkage has also been obtained. The company is in the process of complying with the terms of reference to obtain the final environmental clearance. Joint allocation of the coal block (110mt) was obtained in Jharkhand for setting up a 1,000MW merchant power plant. It is also exploring opportunities both in and outside West Bengal for more merchant power plants.

GIPCL: Unit-1 of the company's Rs1633cr, 250MW Surat Lignite Power Plant (SLPP) is likely to be commissioned as per schedule by December 2008 while Unit 2 is expected to be commissioned by March 2009. The company has tied up funds for the project. The debt component for the project works out to Rs1,225cr. The balance would be met through equity. The company has front loaded equity in this project.

Strong Capacity addition to power Top-line growth

We expect the power companies under our coverage viz., NTPC, GIPCL and CESC to report strong Topline growth of 12.7% yoy during 1QFY2009. We expect market leader, NTPC to report a 16.5% yoy increase in Net Revenues. Key growth drivers would be capacity addition and improvement in tariff realization. We expect NTPC to add capacity to the tune of 3,000MW during FY2009.

GIPCL is also adding capacities this year. For 1QFY2009, the company is expected to clock 15% yoy growth in Net Revenues led by an increase in fuel cost. However, we expect PAT to de-grow by 10% yoy,

CESC is expected to record a robust 6.5% yoy growth in Top-line in 1QFY2009. As in the case of NTPC and GIPCL, we expect this strong growth to be driven chiefly by continued steep increase in fuel cost for the company. Average tariff for FY2008 stood at Rs3.75/kwh, However, tariff was provisionally increased by 10 paise/kwh with effect from Feb. 1, 2008 to cover the increase in fuel prices.

We believe the Indian Power Sector has a long way to go as the peak demand-supply scenario continues to be bad. Future growth is likely to come primarily from capacity additions. There exists enormous potential given that India has one of the lowest per capita consumption of power globally. We expect NTPC to add substantial capacity going ahead. Top-line growth of the companies in our universe continues to be impressive. We expect this growth momentum to be maintained in the medium term as well.

Margins to remain stable-to-positive

We expect NTPC to clock a 124bp yoy contraction in EBITDA Margins for the quarter under review. As for CESC, we expect it to record a 37bp yoy improvement in Margins, led by operating leverage. We expect GIPCL to report a 500bp yoy contraction in EBITDA Margins.

Companies to report flat Bottom-line growth

We expect our universe of stocks to report a de-growth in Bottom-line for this quarter at (3.6)% yoy, for NTPC we expect bottmline to decline by 13.7% and a de-growth of 10.3% yoy for GIPCL. However, we expect CESC to report a 13.2% yoy rise in Net Profits mainly on account of higher realisation recorded in 1QFY2009.

Remain positive on Power Sector

We expect the power companies to report healthy revenue growth going ahead due to robust investments in the sector. In our universe, we expect the companies to clock impressive Top-line growth during the next couple of years. Further, the broader index has witnessed a huge correction due to which the P/E multiple for these stocks have contracted. Nonetheless, we remain positive on the sector even though we are de-rating all the companies in our universe. **Our Top Picks in the Power space remain CESC and GIPCL.**

Exhibit 3: Quarterly Estimates **Rs cr**

Company	CMP	Net Sales		OPM (%)		Net Profit		EPS (Rs)		EPS (Rs)			P/E (x)		Target	Reco
	(Rs)	1QFY09E	*% chg (yoy)*	1QFY09E	*chg bps (yoy)*	1QFY09E	*% chg (yoy)*	1QFY09E	*% chg (yoy)*	FY09E	FY10E	*% chg*	FY09E	FY10E	Price (Rs)	
NTPC*	155	10,270.3	*14.5*	28.8	*(124.0)*	2045.0	*(13.7)*	2.5	*(13.7)*	9.7	10.6	*9.0*	15.9	14.6		**Neutral**
CESC	375	763.6	*6.5*	18.5	*37*	92.8	*13.2*	7.4	*(23.7)*	28.0	32.2	*14.7*	13.4	11.7	559	**Buy**
GIPCL	72	247.4	*15.0*	27.7	*(510)*	33.9	*(10.3)*	2.2	*(10.3)*	6.8	8.2	*20.1*	10.7	8.9	105	**Buy**

*Source: Company; Angel Research; Note: Price as on July 4, 2008; * Consolidated*

***Analyst* - Girish Solanki / V. Srinivasan**

Software

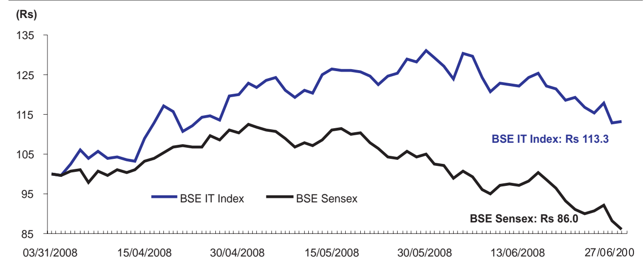
BSE IT Index - Falling Rupee, soaring index!

The June 2008 quarter saw the BSE IT Index recording a robust out-performance vis-à-vis the BSE Sensex. The IT Index gained over 13% over the quarter, while the Sensex lost around 14% in value terms over the same period, thus indicating an out-performance of over 27%. This has been the first comprehensive out-performance by the IT Index since 3QFY2007, when the index gained around 20% v/s nearly 11% gains for the Sensex. In 4QFY2008 too, the IT Index had 'out-performed' the Sensex, however, only on account of the fact that it had 'lost less' than the Sensex and even this was only a marginally better performance (IT Index lost 22% v/s 23% loss recorded by the Sensex). Taking a broader perspective, the Indian stock markets performed poorly during the quarter on account of several factors, chief among them being continued risk aversion, FII selling, global concerns about the US recession, high inflation across countries including India and record crude oil prices. Political uncertainty back home also impacted the markets.

For the IT Sector, however, some amount of positive news flow did come in. Tax benefits under the Software Technology Parks of India (STPI) scheme were extended by one year to March 31, 2010, which leads to an immediate 4-5% improvement in Earnings for these companies for FY2010. A cooling off in wage inflation was witnessed and top-tier companies have also indicated that US corporates have started loosening their purse strings a little and started spending, with offshoring continuing to receive attention as a key driver for cost-cutting and improving efficiencies. Finally, substantial Rupee depreciation was witnessed over the quarter, with the domestic currency losing 4-5% in value against the Dollar.

Going ahead, volume growth is likely to remain reasonably strong in the region of 20-22% yoy, as we believe offshoring will continue to gain market-share in the overall scheme of things. The overall penetration of Indian IT companies in the Global IT Industry still remains in mid-single digits, which is likely to inch further upwards at the expense of incumbent service providers like Accenture and IBM Global Services (IBM GS). As for Margins, we expect these to be positive in FY2009 on account of the significant Rupee depreciation witnessed. However, we expect a gradual tapering down moving into FY2010, as we believe the Rupee will resume its appreciating trend against the Dollar over the medium-to-long term. We expect the Rupee to depreciate in FY2009 on account of the increasingly worsening fiscal position of the country driven by several 'populist' measures including the farm loan waiver, record high crude prices leading to increased subsidies and the likely lack of any firm economic policy decisions in wake of the upcoming general elections.

Exhibit 1: BSE IT Index - Currency-fuelled rise



Source: C-line

In terms stock performance, the top-tier IT stocks fared reasonably well. It was clearly the stock of Infosys that soared ahead of the rest, gaining over 21% during the quarter. Satyam also clocked gains of nearly 11%. TCS, Wipro and Tech Mahindra gained 5.9%, 3% and 1.3%, respectively. HCL Technologies however, clocked a significant under-performance, losing around 1% over the quarter. Mid-cap IT stocks recorded a mixed performance, with Prithvi Info losing as much as 15%, while Zensar Technologies managed to gain 6%.

Rupee depreciation - C'rude' fall

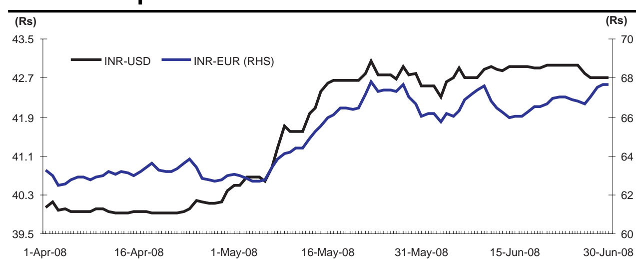
During 1QFY2009, the Indian Rupee witnessed substantial depreciation against all major currencies including the US Dollar, Euro and British Pound. This was primarily on account of crude oil prices, which hit record highs crossing US $142 per barrel. This led to deterioration in the country's fiscal situation. Even as only a fraction of the total rise in the cost of crude oil has been passed on to the consumers leading to oil marketing companies (OMCs) like BPCL and HPCL coming to the brink of bankruptcy, the government's subsidy bill has ballooned significantly. The government issues oil bonds to OMCs, which mature in the future and lead to a 'contingent liability' for future governments. They are in the nature of 'off-balance sheet transactions' and adversely impact the country's fiscal health.

Overall, a combination of global factors and poor fiscal

Software

management has resulted in the recent fall in the Rupee. On a quarterly average basis, the Rupee ended lower by around 4.6% against the Dollar, by as much as 9.1% against the Euro and by 4.2% against the Pound. On an end-of-period basis, the depreciation was to the tune of 7.1% against the Dollar and 7.4% each against the Euro and Pound. While this certainly spells bad news for OMCs in particular and the overall economy in general, as it fuels inflation, IT companies stand to benefit from this trend.

Exhibit 2: Rupee movement - Crude-led fall in value



Source: Oanda.com

Volumes, Rupee depreciation to drive growth in 1QFY2009

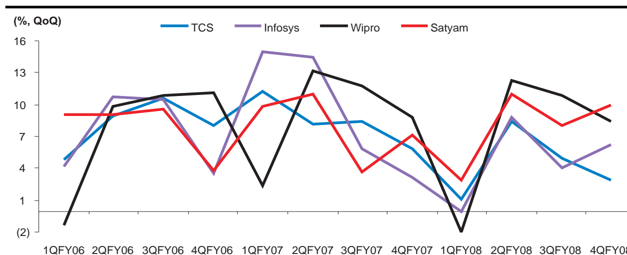
We expect the top-tier IT companies to report decent sequential Topline growth in 1QFY2009, driven mainly by volumes and the significant Rupee depreciation witnessed over the quarter. We have assumed a flat trend in billing rates. We expect a 7.5% qoq Topline growth (including only combined IT Services Businesses for Wipro), driven by volume growth of 4-5% qoq, with the balance coming from favourable currency movements. Thus, nearly half of the sequential Topline growth this quarter is likely to be contributed by currency movements. On the other hand, we estimate conservative growth in Dollar terms of around 3.2% qoq and around 29% yoy. The Rupee growth rate is expected to be 32% on account of a higher realised Rupee rate. It should be noted here that it was in 1QFY2008 that the Rupee first started its dramatic appreciation trend, which continued through FY2008.

Exhibit 3: Dollar v/s Rupee growth of Top-tier IT companies

Particulars	1QFY08	4QFY08	1QFY09E	*%chg qoq*	*%chg yoy*
Dollar revenues (mn)**	3,431	4,302	4,440	*3.2*	*29.4*
Rupee revenues (cr)**	13,971	17,172	18,466	*7.5*	*32.2*
Realised Rupee rate	40.72	39.92	41.60	*4.2*	*2.1*

*Source: Company, Angel Research; Note: Companies include TCS, Infosys, Wipro and Satyam; ** For Wipro, only combined IT Services revenues are included.*

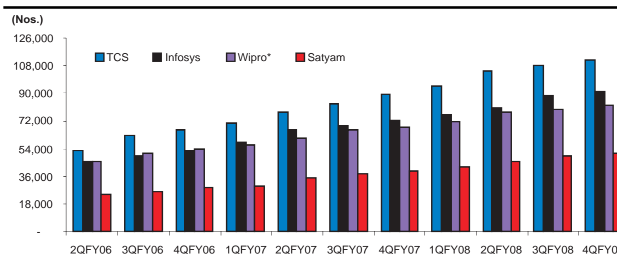
Exhibit 4: Sales growth - Quarterly trends



Source: Companies, Angel Research

We have been conservative on the pricing front, assuming flat billing rates given the current uncertainty in the US economy and the likelihood that clients will ask for greater value for every IT Dollar spent. However, we believe over the longer term, pricing will witness an up-tick led mainly by an improving service mix and productivity enhancements. We believe billing rates could get a further boost going forward owing to the ever-increasing trend of output-based pricing catching on amongst Indian IT companies who are showing greater willingness to share risks with their clients.

Exhibit 5: Employee additions



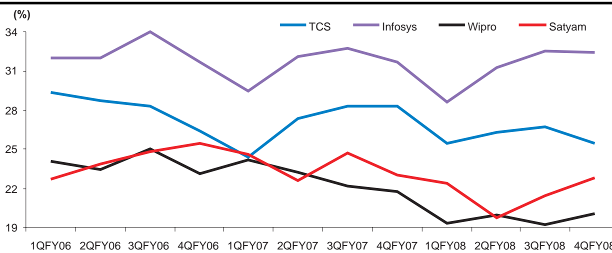
*Source: Companies, Angel Research; * For Wipro, the employee bases in the IT and BPO businesses are considered.*

Margins to witness upside aided by currency depreciation

We believe the depreciation in value seen in the Rupee against all major currencies including the Dollar, Euro and Pound this quarter will have a significant positive impact on the Margin profile of the top-tier software companies. Given that the Rupee has fallen by 4.6% against the Dollar (quarterly average), the impact from this could be 1.5-2% on Margins. This would, to a considerable extent, mitigate the pressures on account of the salary hikes being carried out by Infosys and TCS. Apart from the currency benefits, we expect SG&A leverage, productivity improvements and a tight control on costs to lead to further Margin defence. On a company-specific basis, we expect Infosys to report a 121bp qoq Margin expansion, TCS 41bp qoq, Wipro 174bp qoq and Satyam 91bp qoq.

Software

Exhibit 6: EBITDA Margin - Quarterly trends

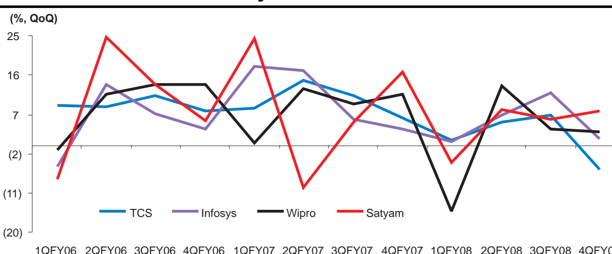


Source: Companies, Angel Research

Net Profit to clock good growth albeit restricted by hedging losses

We expect the top-tier IT companies to report decent Bottomline growth of 5.9% qoq in 1QFY2009. We expect decent Margin expansion, but lower Other Income is likely to lead to slower Bottomline growth compared to EBITDA. We expect Other Income, as a percentage of Net Profit, to hit just 2.5%, a significant fall from 7.8% levels seen last quarter (v/s our expectation of 7.7%). On an absolute basis, we expect Other Income to fall by over 66% qoq for the top-tier software companies.

Exhibit 7: PAT - Quarterly trends



Source: Companies, Angel Research

Key points to watch - US economic updates, client spending patterns, guidance upgrades

In the upcoming results season, greater clarity as regards the situation in the key US economy will be expected, given the criticality of that market to Indian IT companies' businesses. More information regarding clients' spending patterns will also be tracked, particularly the offshore component of spends. In the near-term, uncertainty could be a feature in the US as it heads for elections, with the next likely US president alluding to having to decide on 'whether to give tax breaks to companies that ship jobs out of the US or to companies that invest in the US'. This is a clear indication that offshoring might not have an easy ride at least until the US elections scheduled for November 2008.

Any upgrades in guidance by the top-tier companies will also be watched. It should be noted that at the end of FY2008, Infosys and Satyam had pegged their FY2009 guidance based on a Rupee rate of 40 to a Dollar. With the average rate in FY2009 very likely to be much above this, it remains to be seen if these companies translate it into higher guidance. We believe there could be a slight upgrade provided volume growth remains on track. Growth trends in the key Banking, Financial Services and Insurance (BFSI) vertical will also be tracked, given that it is by far the largest contributor to the revenues of top-tier software companies like Infosys and TCS. Overall, we remain positive on the IT sector. **Our Top Picks are Infosys, Satyam and Tanla Solutions.**

Exhibit 8: Quarterly Estimates **Rs cr**

Company	CMP	Net Sales		OPM (%)		Net Profit		EPS (Rs)		EPS (Rs)			P/E (x)		Target	Reco
	(Rs)	1QFY09E	*% chg (QoQ)*	1QFY09E	*chg bps (QoQ)*	1QFY09E	*% chg (QoQ)*	1QFY09E	*% chg (QoQ)*	FY09E	FY10E	*% chg*	FY09E	FY10E	Price (Rs)	
Infosys	1,755	4,899	*7.8*	33.7	*121*	1,338	*7.1*	23.3	*7.2*	99.0	114.7	*15.8*	17.7	15.3	2,064	Buy
TCS	844	6,512	*6.8*	25.9	*41*	1,312	*4.5*	13.4	*4.5*	62.6	73.8	*18.0*	13.5	11.4	1,181	Buy
Wipro	429	5,918	*3.5*	21.8	*174*	928	*5.5*	6.4	*5.5*	27.4	32.5	*18.6*	15.7	13.2	520	Buy
Satyam	462	2,615	*8.2*	23.7	*91*	500	*7.0*	7.3	*7.0*	30.3	35.4	*16.9*	15.3	13.1	530	Buy

Source: Company; Angel Research; Note: Price as on July4, 2008.

Analyst **- Harit Shah**

Telecom

Telecom stocks under-perform in 1QFY2009

During the June 2008 quarter, Telecom stocks under-performed the benchmark index, the BSE Sensex. There is currently no separate index of telecom stocks. However, if we take a basket of major telecom stocks, the basket marginally under-performed the Sensex, giving negative returns of nearly 16% (negative 14% for the Sensex). While concerns persisted over the possible impact of intensifying competition in the sector with the impending entry of newer operators and the potential entry of mobile virtual network operators (MVNOs), the sector was impacted by the overall poor performance of the stock markets led by FII selling, risk aversion globally, high levels of inflation across nations including India and record high crude oil prices, apart from domestic political uncertainty.

Exhibit 1: Telecom Stocks - Performance during 1QFY2009

(Rs)	March'08	June'08	*chg (%)*
Bharti Airtel	826.1	721.7	*(12.6)*
Reliance Communications	508.3	442.4	*(13.0)*
Idea Cellular	102.8	93.1	*(9.4)*
MTNL	96.6	90.2	*(6.6)*
Tata Communications	513.8	373.2	*(27.4)*
Tata Teleservices (Maharashtra)	28.1	24.2	*(14.1)*
BSE Sensex	**15,644.4**	**13,461.6**	***(14.0)***

Source: C-line

In terms of stock-specific performances, both Bharti Airtel and Reliance Communications (RCOM) declined by around 13%. The two stocks were affected by concerns about the potential impact that a takeover of the South African telecom major, MTN Group would have on their financials. It may be recalled that Bharti Airtel and MTN Group held talks for a takeover of the latter by the former, a move that would have created an emerging market telecom giant with over 130mn subscribers across 23 countries of operations. However, the talks fell through, with Bharti stating that it withdrew from the talks since MTN wanted a transaction done through a convoluted way that would make Bharti its subsidiary and this would not be in the interests of minority shareholders. After Bharti, RCOM started talks with MTN. The talks are still in progress, with a takeover of RCOM being the likely outcome, even as the ADA Group would be the largest shareholder in MTN through a share-swap. However, Reliance Industries has put a spanner in the works, claiming the Right of First Refusal (ROFR) over RCOM shares. Thus, the quarter was marked by the high-voltage drama involving the top-two Indian mobile companies.

As for the other players, Idea Cellular 'out-performed', losing just 9%. It has acquired regional operator, Spice Communications and will merge it with itself, in the process gaining Telekom Malaysia as a strategic partner through a 14.99% stake sale to the latter. This transaction will benefit Idea over the long-term. The stock of Tata Communications lost the maximum ground (over 27%), while Tata Teleservices (Maharashtra) also slipped by over 14%. The PSU telecom major, MTNL ended 7% lower.

Key sector developments - Start-up spectrum, 3G issues and acquisitions…

The quarter was indeed an eventful one for the Indian Telecom Sector. The government seems to be finally progressing on the spectrum issue, with start-up spectrum issued to newer operators like Datacom, Unitech, Swan, Loop and Shyam in circles like Tamil Nadu (including Chennai), Orissa and Maharashtra. This will lead to heightened competitive intensity in these circles as and when these operators begin to roll out full-fledged services. Uncertainty currently prevails with regards to the participation of foreign players in the 3G spectrum auctions as and when they are conducted, with the Department of Telecommunications (DoT) in favour of allowing foreign players, while the sector regulator, the Telecommunications Regulatory Authority of India (TRAI) is of the view that only existing players should be allowed to offer 3G services, given the numerous legal tangles that are likely to come up if foreign players are allowed to offer 3G services. Overall, it was a quarter of acquisitions and acquisition-led talks, with Idea Cellular snapping up Spice Communications, while Bharti was briefly in talks with MTN, which fell through, even as RCOM is still in talks with the company.

- Bharti Airtel and MTN Group, a major South Africa-based mobile operator with operations across 21 countries, held talks for a possible deal. Bharti had mentioned in the past that it is looking to expand globally and is open to both organic and inorganic opportunities. Goldman Sachs and Standard Chartered had pledged to underwrite US $6bn each of the amount that Bharti Airtel would need to fund the purchase of a controlling stake in MTN (US $20bn), if the deal would take place. A deal with MTN would have led to Bharti getting more

Telecom

of a global presence, with operations in 23 countries. The combined entity would be an emerging market telecom 'Goliath', with over 220mn mobile subscribers, Revenues of over US $27bn, EBITDA of US $11.6bn and Net Income of around US $4.5bn by FY2010E. However, the talks broke down after MTN wanted a convoluted transaction that would make Bharti its subsidiary, a move that the latter said was not in the best interests of minority shareholders.

- Even as Bharti's talks with MTN Group collapsed, RCOM almost immediately began discussions with the South African telco, which are still in progress. The deal at the moment envisages a share swap between the two companies that will eventually make the ADA Group the largest shareholder in MTN, even as RCOM itself becomes a subsidiary of the company, triggering the Indian takeover code and an open offer from MTN for RCOM minority shareholders. Such a deal is precisely the convoluted route that Bharti Airtel avoided and it remains to be seen as to what will happen in this case. However, rather unexpectedly at the last moment, Reliance Industries (RIL), India's most valuable company by market capitalisation, threw a spanner in the works, claiming Right of First Refusal (ROFR) over RCOM shares. Thus, such a move is likely to lead to a prolonged courtroom battle between the two feuding brothers and puts in some jeopardy the fruition of any deal between RCOM and MTN Group.

- Idea Cellular snapped up Spice Communications, a regional telecom operator with a presence in the Punjab and Karnataka circles. This was a three-way deal between Idea, Spice and Telecom Malaysia International (TMI), a key shareholder in Spice. Idea Cellular will acquire the 40.8% stake of the promoter group in Spice Communications for a price of Rs77.30 per share and will also pay Rs544cr as non-compete fee. It will then make an open offer along with TMI and its affiliates and associates for a further 20% stake in Spice. The Boards of Idea and Spice have also approved the merger of Spice with Idea and the swap ratio has been determined at 49 shares of Idea for every 100 shares of Spice. Idea will make a preferential allotment to TMI of 46.473cr equity shares at Rs156.96 per share, which represents 14.99% of Idea's equity capital post allotment. TMI will get further shares in Idea through a share swap in the determined ratio of 49:100, with its eventual stake in Idea being around 18-20%. This deal signals consolidation in the sector and is a long-term positive for Idea.

Subscriber growth to power Topline

We expect the major telecom companies under our coverage, Bharti Airtel, RCOM and Idea Cellular, to report strong Topline growth to the tune of 38% yoy and 6.5% qoq during 1QFY2009. We expect Bharti Airtel to report a 40.9% yoy and 6.4% qoq increase in Net Revenues. This is expected to be driven by the key Mobile Services Business, which we estimate will grow by 47% yoy and 7.6% qoq. The key growth driver of this business is expected to be strong accretion to the mobile subscriber base, which we expect will grow by 62% yoy and by 12% qoq to 69.3mn, implying quarterly net additions of 7.3mn, the company's highest-ever. On a yearly basis, the net additions are expected to be 26.6mn, implying average net adds of over 2.2mn a month, reflecting admirable consistency.

Bharti continues relentlessly on its network expansion plan and has left far behind all other mobile operators in terms of market share. In May 2008, the company added nearly 2.5mn subscribers, it's highest-ever and we expect this to continue in the near-term. We expect average revenues per user (ARPUs) to decline by 4% qoq and 11% yoy to Rs351 per user per month. We expect the company's other business segments to also record robust growth, with Telemedia Services estimated to clock a 24% yoy growth, Enterprise Services (Carriers) 44% yoy and Enterprise Services (Corporates) a 25% yoy growth.

RCOM is expected to clock a 32% yoy and 6.5% qoq growth in Net Revenues. This is again expected to be led by the key Wireless Business, which is estimated to grow at a similar rate to overall revenues. We expect the mobile subscriber base to grow by 59% yoy and 11% qoq to 50.7mn, implying quarterly net additions of nearly 5mn. Yearly net additions are estimated at 18.8mn. ARPUs are expected to fall by around 4% qoq and 18% yoy to Rs307 per user per month. As regards the other business segments of the company, we expect the Global Business to grow by 22% yoy and the Broadband Business by 49% yoy.

Idea Cellular is expected to record a robust 43% yoy and 7% qoq growth in 1QFY2009 Topline. As is the case for Bharti and RCOM also, we expect the strong growth to be driven

Telecom

chiefly by continued strong subscriber numbers recorded by the company. We estimate the mobile subscriber base of Idea to grow by 69% yoy and 13.5% qoq to hit 27.2mn, implying quarterly net adds of 3.2mn. On a yearly basis, net adds are estimated at over 11mn. We estimate ARPUs to fall by 4% qoq and 14% yoy to Rs275.5 per user per month.

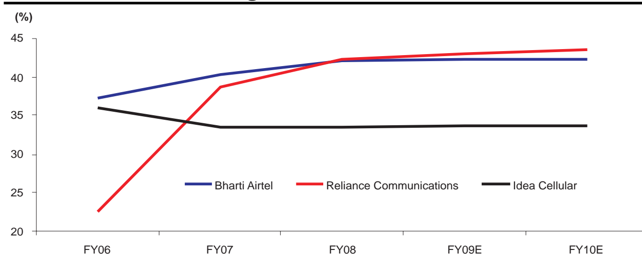
Going ahead, the Indian Mobile Telephony Sector remains at a relatively nascent and under-penetrated stage, with penetration levels of around 25%. Going forward, there exists immense scope for growth. With future growth likely to come primarily from the rural areas, there lies enormous potential, given that rural teledensity is still in single digits. We expect the top-2 players in the industry, Bharti and RCOM, to remain major beneficiaries of this growth in the future. Idea Cellular has also proven its execution skills, particularly after it overcame management issues over ownership of the company and is likely to witness accelerated growth on commencement of operations in newer circles. The company's acquisition of Spice Communications is also likely to accelerate its network roll-out process and quicken the pace for it to become a pan-India operator.

Subscriber growth continues to be impressive for all these companies. Bharti has maintained 2mn-plus monthly net adds for the past eleven consecutive months and nearly touched 2.5mn in May 2008. Going forward, we expect this growth momentum to be maintained in the medium-term, as the company rapidly rolls out its network into the remote areas of the country. RCOM also continues to record strong monthly net adds and with expansion of coverage area, is likely to see an improvement here. The GSM roll-out is expected to provide a further kicker to growth. Idea Cellular is also expected to continue to grow at a fast pace.

Margins to remain stable-to-positive on operating leverage; Idea to record decline

We expect RCOM to clock a 289bp yoy and 133bp qoq expansion in EBITDA Margins for the quarter. This is likely to be driven by continuing scale benefits and operating leverage. We expect Bharti to record a 64bp yoy and 49bp qoq improvement in Margins, again led by operating leverage. We expect Idea Cellular, to report a 136bp yoy contraction in EBITDA Margins, while sequentially the fall is expected to be to the tune of 14bp. This is on account of significant costs incurred towards expansion of coverage area. EBITDA, in absolute terms, is expected to grow by 43% yoy and 7.6% qoq for Bharti, by 41% yoy and 10% qoq for RCOM and by 38% yoy and 7% qoq for Idea Cellular.

Exhibit 2: EBITDA Margin trends



Source: Companies, Angel Research

Bottomline to grow at a decent rate

We expect Bottomline to grow at a decent pace of 31% yoy and 7% qoq for Bharti. For RCOM, growth is expected to come in at 27% yoy and 3% qoq. However, we expect Idea Cellular to report a 9% yoy decline in Net Profits (2% qoq growth) mainly on account of the significant forex gains recorded by it in 1QFY2008 of Rs32.9cr, which significantly pushed up Bottomline in that quarter.

Maintain positive stance on Telecom Sector

We maintain our positive view on the sector and expect the strong growth in telecom subscriber numbers to continue going ahead. We estimate the total Indian mobile subscriber base to grow at a CAGR of 33.6% over the period FY2008-10E to hit 457.3mn by FY2010. **Our Top Picks in the Indian Telecom space remain Bharti Airtel and RCOM.**

Exhibit 3: Quarterly Estimates Rs cr

Company	CMP	Net Sales		OPM (%)		Net Profit		EPS (Rs)		EPS (Rs)			P/E (x)		Target	Reco
	(Rs)	1QFY09E	*% chg (YoY)*	1QFY09E	*chg bps (YoY)*	1QFY09E	*% chg (YoY)*	1QFY09E	*% chg (YoY)*	FY09E	FY10E	*%chg*	FY09E	FY10E	Price (Rs)	
Bharti Airtel	716	8,317	*40.9*	42.1	*64*	1,980	*31.0*	10.4	*31.0*	44.1	53.9	*22.2*	16.2	13.3	1,125	Buy
RCOM	438	5,590	*31.6*	44.3	*289*	1,551	*27.0*	7.2	*26.7*	31.2	39.5	*26.7*	14.0	11.1	763	Buy
Idea Cellular	88	2,118	*43.4*	33.4	*(136)*	282	*(8.6)*	1.1	*(8.5)*	4.9	7.1	*43.5*	18.0	12.5	146	Buy

Source: Company; Angel Research; Note: Price as on July 4, 2008

Analyst **- Harit Shah**

Fund Management & Investment Advisory	(☎ 022 - 4040 3800 / 2835 9600)	
P. Phani Sekhar	Fund Manager - (PMS)	phani.sekhar@angeltrade.com
Devang Mehta	AVP - Invesment Advisory	devang.mehta@angeltrade.com
Research Team	(☎ 022 - 4040 3800 / 2835 9600)	
Hitesh Agrawal	Head - Research	hitesh.agrawal@angeltrade.com
Sarabjit Kour Nangra	VP-Research, Pharmaceutical	sarabjit@angeltrade.com
Vaishali Jajoo	Automobile	vaishali.jajoo@angeltrade.com
Harit Shah	IT, Telecom	harit.shah@angeltrade.com
Rohit Nagraj	Oil & Gas	rohit.nagraj@angeltrade.com
Pawan Burde	Metals & Mining, Cement	pawan.burde@angeltrade.com
Vaibhav Agrawal	Banking	vaibhav.agrawal@angeltrade.com
Girish Solanki	Power, Mid-cap	girish.solanki@angeltrade.com
Shailesh Kanani	Infrastructure, Real Estate	shailesh.kanani@angeltrade.com
Anand Shah	FMCG , Media	anand.shah@angeltrade.com
Sulabh Agrawal	Mid-cap	sulabh.agrawal@angeltrade.com
Puneet Bambha	PMS	puneet.bambha@angeltrade.com
Amit Bagaria	PMS	amit.bagaria@angeltrade.com
Jaydeep Mavani	Research Associate (Automobile)	jaydeep.mavani@angeltrade.com
Amit Vora	Research Associate (Oil & Gas)	amit.vora@angeltrade.com
Richa Chandak	Research Associate (Banking)	richa.chandak@angeltrade.com
Neha Soni	Research Associate (Infra, Real Estate)	neha.soni@angeltrade.com
Shweta Boob	Research Associate (FMCG , Media)	shweta.boob@angeltrade.com
V Srinivasan	Research Associate (Power, Mid-cap)	v.srinivasan@angeltrade.com
Neha Idnany	Research Associate - (PMS)	neha.idnany@angeltrade.com
Aniruddha Mate	Research Associate - (PMS)	aniruddha.mate@angeltrade.com
Sandeep Wagle	Chief Technical Analyst	sandeep@angeltrade.com
Ajit Joshi	AVP Technical Advisory Services	ajit.joshi@angeltrade.com
Milan Sanghvi	Sr. Technical Advisor	milan.sanghvi@angeltrade.com
Nitin Kunte	Technical Advisor	nitin.kunte@angeltrade.com
Brijesh Ail	Technical Analyst	brijesh@angeltrade.com
Vaishnavi Jagtap	Technical Analyst	vaishnavi.jagtap@angeltrade.com
Siddharth Bhamre	Fund Manager - Derivatives & Equities	siddarth.bhamre@angeltrade.com
Commodities Research Team		
Amar Singh	Research Head (Commodities)	amar.singh@angeltrade.com
Samson P	Sr. Technical Analyst	samsonp@angeltrade.com
Anuj Gupta	Sr. Technical Analyst	anuj.gupta@angeltrade.com
Girish Patki	Sr. Technical Analyst	girish.patki@angeltrade.com
Commodities Research Team (Fundamentals)		
Badruddin	Sr. Research Analyst (Agri)	badruddin@angeltrade.com
Mandar Pote	Research Analyst (Energy)	mandar.pote@angeltrade.com
Bharathi Shetty	Research Editor	bharathi.shetty@angeltrade.com
Bharat Patil	Production	bharat.patil@angeltrade.com

Research & Investment Advisory: Acme Plaza, 3rd Floor 'A' wing, M.V. Road, Opp Sangam Cinema, Andheri (E), Mumbai - 400 059

Disclaimer

This document is not for public distribution and has been furnished to you solely for your information and must not be reproduced or redistributed to any other person. Persons into whose possession this document may come are required to observe these restrictions.

Opinion expressed is our current opinion as of the date appearing on this material only. While we endeavor to update on a reasonable basis the information discussed in this material, there may be regulatory, compliance, or other reasons that prevent us from doing so. Prospective investors and others are cautioned that any forward-looking statements are not predictions and may be subject to change without notice. Our proprietary trading and investment businesses may make investment decisions that are inconsistent with the recommendations expressed herein.

The information in this document has been printed on the basis of publicly available information, internal data and other reliable sources believed to be true and are for general guidance only. While every effort is made to ensure the accuracy and completeness of information contained, the company takes no guarantee and assumes no liability for any errors or omissions of the information. No one can use the information as the basis for any claim, demand or cause of action.

Recipients of this material should rely on their own investigations and take their own professional advice. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult their own advisors to determine the merits and risks of such an investment. Price and value of the investments referred to in this material may go up or down. Past performance is not a guide for future performance. Certain transactions - futures, options and other derivatives as well as non-investment grade securities - involve substantial risks and are not suitable for all investors. Reports based on technical analysis centers on studying charts of a stock's price movement and trading volume, as opposed to focusing on a company's fundamentals and as such, may not match with a report on a company's fundamentals.

We do not undertake to advise you as to any change of our views expressed in this document. While we would endeavor to update the information herein on a reasonable basis, Angel Broking, its subsidiaries and associated companies, their directors and employees are under no obligation to update or keep the information current. Also there may be regulatory, compliance, or other reasons that may prevent Angel Broking and affiliates from doing so. Prospective investors and others are cautioned that any forward-looking statements are not predictions and may be subject to change without notice. Angel Broking Limited and affiliates, including the analyst who has issued this report, may, on the date of this report, and from time to time, have long or short positions in, and buy or sell the securities of the companies mentioned herein or engage in any other transaction involving such securities and earn brokerage or compensation or act as advisor or have other potential conflict of interest with respect to company/ies mentioned herein or inconsistent with any recommendation and related information and opinions.

Angel Broking Limited and affiliates may seek to provide or have engaged in providing corporate finance, investment banking or other advisory services in a merger or specific transaction to the companies referred to in this report, as on the date of this report or in the past.

Ratings (Returns) :	Buy (Upside > 15%)	Accumulate (Upside upto 15%)	Neutral (5 to -5%)
	Reduce (Downside upto 15%)	Sell (Downside > 15%)	

Corporate & Marketing Office	: 612, Acme Plaza, M. V. Road, Opp. Sangam Cinema. Andheri (E), Mumbai - 400 059	Tel: (022) 4000 3600 / 2835 9600
Wealth Management	: e-mail : wmshelpdesk@angeltrade.com	Tel: (022) 4035 3100
Investment Advisory Helpdesk	: e-mail : advisory@angeltrade.com	Tel: (022) 4040 3800
Commodities	: e-mail : commodities@angeltrade.com	Tel: (022) 4035 8600
Brand Promotion & PR Helpdesk	: e-mail : brandpromotion@angeltrade.com	Tel: (022) 4000 3600
Customer Helpdesk	: e-mail : feedback@angeltrade.com	Tel: (022) 2835 5000

Regional Offices:

Ahmedabad - Manoj Johnson
Tel: (079) 3007 0749 - 751

Bengaluru - Dhiraj Pandey
Tel: (080) 4153 6700 - 03

Chennai - Thiruneer Selvan
Tel: (044) 4226 9000. Fax: 2498 1742

Coimbatore - Lakshminarayanan R
Tel: (0422) 4294 801 - 26

Hyderabad - Mohsin Ahmed
Tel: (040) 6673 3573 / 74

Indore - Avtar Singh Grewal
Tel: (0731) 3013 360 - 65

Jaipur - Ranveer Singh
Tel: (0141) 222 3334

Kanpur - Vivek Singh
Tel: (0512) 3017 700

Kolkata - Vikram Malik
Tel: (033) 4009 9899

Lucknow - Ejaz Mohyi
Tel: (0522) 3057 700

Ludhiana - Pooja Jain
Tel: (0161) 4697 400

Nagpur - Sanchit Tiwari
Tel: (0712) 6461 678.

Nashik - Nilesh Supekar
Tel: (0253) 6614 235 / 236 / 2506 276 / 604

Mumbai (Powai) - Vishal Mishra
Tel: (022) 4079 6000.

New Delhi - Rohit Pateria
Tel: (011) 4605 6600 / 4151 2555 / 2666

Pune - Sunita Magnani / Sulbha Shinde
Tel: (020) 2551 3143 / 3071 0250

Rajkot - Vijay Popat
Tel: (0281) 2490 847

Surat - Pratik Sanghvi / Dinesh Maheshwari
Tel: (0261) 6696 666

Visakhapatnam - Vamshi Krishna
Tel: (0891) 6620 572 - 75

Private Client Group Offices:

Mumbai - Prakarsh Gagdani
Tel: (022) 4040 3800 Fax: (022) 4040 3899

Ahmedabad(C. G. Road) - Arpit Shah
Tel: (079) 3007 4049 / 50

Surat - Amit Keshwani
Tel: (0261) 6696 666

Rajkot(Race Course) - Nishit Maniar
Mobile: 99989 59982

Sub - Broker Marketing:

Premier House - Pankaj Mungre
Tel: (022) 4035 8600

Branch Offices:

Andheri (Lokhandwala) - Muskaan Doultani
Tel: (022) 2639 2626 / 3255 0987

Andheri (W) - Dinesh Nihalani
Tel: (022) 2635 2345 / 6668 0021

Bandra (W) - Rohit Marathe
Tel: (022) 2655 5560 / 70

Bandra (W) - Faruq Wakani
Tel: (022) 6643 2694 - 99

Borivali (W) - Deepak Jagtap
Tel: (022) 2895 2600 / 1 / 2

Borivali (Punjabi Lane) - Gautam Agarwal
Tel: (022) 4075 6000 / 01.

Borivali (W) - Tarun Dhami
Tel: (022) 3092 1969 / 2892 8890

Chembur - Rajesh Mehta
Tel: (022) 6703 0210 / 11 / 12

Chembur(Basant) - Ashita Raman
Tel: (022) 3267 9114 / 15 / 16

Fort - Hitesh Jain
Tel: (022) 2263 4050 - 55

Ghatkopar (E) - Ashwin Thakkar
Tel: (022) 6799 3185 - 88 / 2510 1525

Goregaon (W) - Sanjiv Dhami
Tel: (022) 2878 9401 / 02

Kalbadevi - Viren Ved
Tel: (022) 2243 5599 / 2242 5599

Kandivali (W) - Sachin Ghelani
Tel: (022) 2867 3800 / 2867 7032

Kandivali(Thakur Village) - Akharam Chaudhary
Tel: (022) 2846 1267 / 1654 / 2056 / 2076

Malad (E) - Satish Kanwarjani
Tel: (022) 2880 4440

Malad (W) - Tushar Shah
Tel: (022) 2880 0960 / 68

Mulund (W) - Niraj Anand
Tel: (022) 2562 2282

Nerul - Arun Sharma
Tel: (022) 2771 9012 - 17

Powai - Prashant Auti
Tel: (022) 4026 2170 - 3

Sion - Pritesh Bhatt
Tel: (022) 2404 1054.

Thane (W) - Diksha Khushalani / Rajesh Kumar
Tel: (022) 2539 0786 / 0650 / 0651

Vashi - Amit Jain
Tel.: (022) 2765 4749 / 2251

Vile Parle (W) - Dimple Shah
Tel: (022) 2610 2894 / 95

Wadala - Tushar Dharmashi
Tel: (022) 2414 0607 / 08

Ajmer - Amit Kumar Garg
Mobile: 9784599807

Alwar - Ajay Khandelwal
Tel: (0144) 2703 561 / 99826 23223

Ahmedabad(Bapu Nagar) - Milan Kanabar
Tel: (079) 3026 0204 / 0205

Ahmedabad(C. G. Road) - Ritesh Patel
Tel: (079) 4021 4023

Ahmedabad(Gurukul) - Kaivalya Shah
Tel: (079) 6522 5510 / 3012 5492 - 94

Ahmedabad(Kalupur) - Jicky Thomas
Tel: (079) 3022 6782 / 83

Ahmedabad(Maninagar) - Ashok Kumar
Tel: (079) 3048 0241 / 0242 / 0245

Ahmedabad(Ramdevnagar) - Krunal Pandya
Tel: (079) 4006 5842 / 43

Ahmedabad(Sabarmati) - Kaushik Rathi
Tel: (079) 2751 6788 / 97243 00677

Ahmedabad(Satellite) - Rishi Parghi
Tel: (079) 4000 1000

Ahmedabad(Shahibaug) - Chirag Raghvani
Tel: (079) 2286 1053 / 5 / 6

Amreli - Nishith Hemani
Tel: (02792) 228 800 / 231 039 / 40 / 41 / 42

Amritsar - Gautam Seth
Tel: (0183) 3987 000

Anand - Alay Brahmbhatt
Tel: (02692) 267 041 - 45

Ankleshwar - Ankit Mathur
Tel: (02646) 652 681 - 85

Baroda - Rashmikant Thakar
Tel: (0265) 2226 103 - 04 / 6624 280

Baroda(Akota) - Jaydeep Shah
Tel: (0265) 2355 258 / 6499 286

Baroda(Manjalpur) - Raja Upadhyay
Mobile: (0265) 6454280 - 3 / 98251 11712

Bengaluru (Jayanagar) - Umapathi K.
Tel: (080) 4072 0800 - 29

Bhavnagar - Apurva Dhami
Tel: (0278) 2512 099 / 2512 755 / 3001 717 / 18

Bhopal - Sandeep Kothana
Tel: (0755) 3256 663 / 4024 000

Bikaner - Sharad Acharya
Tel: (0151) 2207 148 / 98281 03988

Chandigarh - Naveen Bansal
Tel: (0172) 4697 400

Deesa - Sandip Nayak
Mobile: 98795 19881

Erode - Sherman Saphroni Gracias
Tel: (0424) 4065 555 - 65

Faridabad - Pankaj Jugia
Tel: (0129) 4281 401 - 23

Gajuwaka - Shaik Meera
Tel: (0891) 2541 571 - 4

Gandhinagar - Vivek Thakker
Tel: (079) 4010 1010 - 31

Gondal - Lenin Trivedi
Tel: (02825) 240 693 / 4

Gurgaon - Pankaj Verma
Tel: (0124) 4218 704

Himatnagar - Sanjay Patel
Tel: (02772) 241 008 / 241 346

Hyderabad (A S Rao Nagar) - G J Sharma
Tel: (040) 4222 2070 - 5

Hubli - Aftab Kamalapur
Tel: (0836) 4267 500 - 22

Indore (Sapna Sangeet Rd)- Sourabh Kasliwal
Tel: (0731) 4238 600.

Indore - Alok Rathi
Tel: (0731) 4042 242 / 4044 366 / 4087 966

Jaipur (Rajapark) - Abhimanyu Singh
Tel: (0141) 4000 500, 94143 14448

Jalgaon - Naresh Kulkarni
Tel: (0257) 3200 906

Jamnagar - Jwalant Shingala
Tel: (0288) 2664 941 - 44, 3217 790

Jodhpur - Bharat Purohit
Tel: (0291) 5100 941 - 948 / 98284 26786

Junagadh - Nimesh Raichura
Tel: (0285) 2622 483 / 2622 484

Kota - Sumit Maheshwari
Tel: (0744) 5100 470 / 2365 200

Mansarovar - Rakesh Yadav
Tel:(0141) 4000 600 / 98280 90009.

Mehsana - Alipt Doshi
Tel:(02762) 645 291 / 92

Mysore - Ajay Kumar
Tel: (0821) 4004 200 - 30

Nadiad - Vipul Patel
Tel: (0268) - 2527 230 / 31

Nashik (College Road) - Sanchit Patunkar
Tel: (0253) 6614 252 / 3048 908

New Delhi(Bhikaji Cama Place) - Sumit Bhuttan
Tel: (011) 4165 9711 / 12

New Delhi(Lawrence Rd.) - Sanjeev Kumar
Tel: (011) 3262 8699 / 8799

New Delhi (Nehru Place) - Muneesh Chauhan
Tel: (011) 4651 2900 / 11

New Delhi(Pitampura) - Roopal Agarwal
Tel: (011) 4700 2380 / 84

New Delhi(Preet Vihar) - Gulshan Khurana
Tel: (011) 4242 1105 - 07

Noida - Amit Gupta
(0120) 4639 900 / 1 / 9

Palanpur - Paresh Patel
Tel: (02742) 645 171 / 72

Patan - Shikha Saxena
Tel: (02766) 222 306

Patel Nagar - Harpreet Singh
Tel: (011) 45030 600

Porbandar - Ketan Thanki
Tel: (0286) 2215 310 / 31, 2215 450

Pune(Pentagon) - Ishwar Magnani / Rohit Shinde
Tel: (020) 66408300 / 30523217

Pune(Camp) - Shardul Kulkarni / Viral Shah
Tel: (020) 3058 2862 / 3

Pune - Sameer Amrute / Shraddha Gadekar
Tel: (020) 6620 6591 / 6620 6595

Rajamundhry - G. Padmavathi
Tel: (0883) 2477 571 - 5

Rajkot(Ardella) - Hitesh Rupareliya
Tel.: (0281) 2926 568 / 99049 10001

Rajkot(University Road) - Prashant Ukani
Tel: (0281) 2577 408

Rajkot(Bhaktinagar) - Dhaval Dave
Tel: (0281) 2361 935 / 3296 881

Rajkot(Indira Circle) - Denish Patel
Tel: (0281) 2585 751, 99258 84848

Rajkot(Orbit Plaza) - Hitesh Popat
Tel: (0281) 2463 291- 94

Rajkot(Pedak Road) - Murtuja Sadikot
Mobile: (0281) 2925 055, 98245 00252

Rajkot(Star Chambers) - Manish Baradia
Tel: (0281) 2233 230 / 50

Rajkot(Star Chambers - 519) - Kiran Marthak
Tel: (0281) 2225 401 - 04

Salem - Alagurajan
Tel: (0427) 4065 555 - 62

Secunderabad - Srinivas
Tel: (040) 6690 5192 / 3 / 4

Surat (Mahidharpura) - Sameet Kapadia
Tel: 2402 911 - 915

Surat (Parle Point) - Akshay Panwala
Tel: (0261) 2257 909 / 990

Surat (Ring Road) - Piyush Bothra
Tel: (0261) 6696 666

Surendranagar - Prashant Jani
Tel: (02752) 325 905 / 223 305

Udaipur - Anurag Jain
Tel: (0294) 5104 701 - 708

Valsad - Vinod Kumbarwadia
Tel: (02632) 645 344 / 45

Vapi - Jalpa Desai
Tel: (0260) 2400 210 / 214 / 236

Varachha - Naimesh Bhavsar
Tel: (0261) 2551 633 - 39

Vijaywada - Badrinath Majeti
Tel: (0866) 6636 900 / 901 / 902 / 903

Warangal - Santosh Kumar Kaja
Tel: (0870) 6452 223 / 7

Central Support & Registered Office: G-1 Akruti Trade Centre, Road No.7, MIDC Marol, Andheri (E), Mumbai - 400 093. Tel: 2835 8800 / 3083 7700

Angel Broking Ltd : BSE Sebi Regn No : INB 010996539 / CDSL Regn No: IN - DP - CDSL - 234 - 2004 / PMS Regn Code: PM/INP000001546 Angel Capital & Debt Market Ltd: INB 231279838 / NSE FNO: INF 231279838 / NSE Member Code: 12798
Angel Commodities Broking (P) Ltd: MCX Member ID: 12685 / FMC Regn No: MCX / TCM / CORP / 0037 NCDEX : Member ID 00220 / FMC Regn No: NCDEX / TCM / CORP / 0302

For Private Circulation Only