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Stock Rating
Equal-weight

Industry View
In-Line

Suzlon Energy

Rising Risks to Business Model; Downgrade to EW

What's Changed	
Rating	**Overweight to Equal-weight**
Price Target	**Rs450.00 to Rs52.45**
F2009 EPS	**From Rs12.7 to Rs9.1**
F2010 EPS	**From Rs17.7 to Rs10.6**

Rising risk to Wind Energy business from Changing Macro: With the massive downtick in oil prices, the delay in the renewal of PTC in the US and the difficulty in financing wind power projects, we are lowering our growth for the industry to 5% for C2009E. On the back of low visibility in a slowing market, we cut our volume estimate for Suzlon by 17% and 24% in F2009 and F2010 respectively, resulting in a 29% and 40% drop in EPS. We still model a market share gain (though smaller than earlier) for Suzlon in F2010 despite recent blade quality issues.

Access to REpower Technology Is Critical in Face of Slowing Order Flow: Suzlon has decided not to try to exercise the domination and profit transfer agreement with REpower, due to opposition from lenders who will be financing the next rounds of growth for REpower. However, with Suzlon struggling to bag any orders in the last 6 months, we remain sanguine on the belief that the next stage of growth at Suzlon would be powered by REpower technology (3MW, 5MW and 6MW turbines), which looks unlikely in the short term.

Significant Risk to Leveraged Balance Sheet in the Near Term: We believe that with the cancellation of the rights issue, debt will become the primary source of funding the growth at Suzlon. We believe that Suzlon is doing the right things; i.e., trying to delay the purchase of Martifer’s stake in REpower and cutting back on capex. However, on our reduced numbers, we still perceive risk to Suzlon’s debt covenants. If the Martifer stake purchase cannot be pushed back, we expect Suzlon to breach its debt covenants, potentially resulting in punitive action from lenders.

Key Ratios and Statistics

Reuters: SUZL.BO Bloomberg: SUEL IN
India Capital Goods

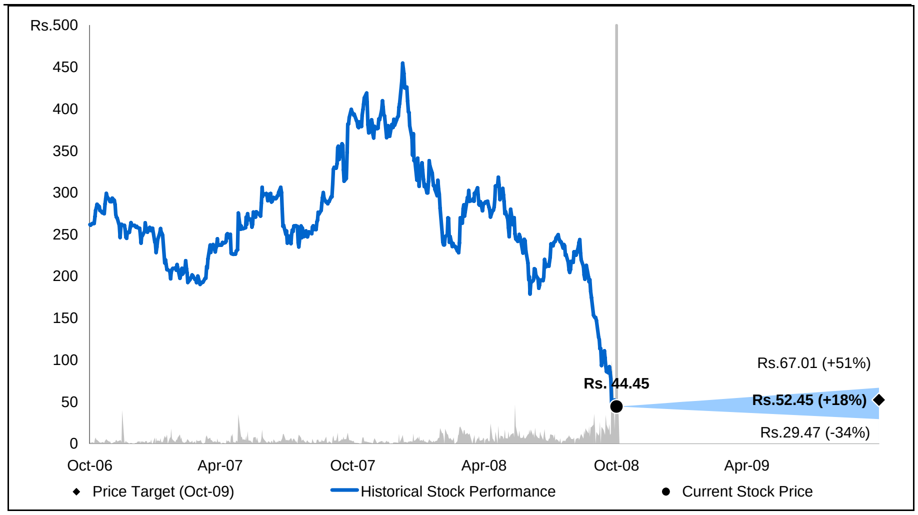
Price target	Rs52.45
Upside to price target (%)	14
Shr price, close (Nov 3, 2008)	Rs45.95
52-Week Range	Rs460.00-42.00
Sh out, dil, curr (mn)	1,499
Mkt cap, curr (mn)	Rs68,869
EV, curr (mn)	Rs108,882
Avg daily trading volume (mn)	Rs624

Fiscal Year ending	**03/07**	**03/08**	**03/09e**	**03/10e**
ModelWare EPS (Rs)	5.92	7.89	9.06	10.61
Prior ModelWare EPS (Rs)	-	8.17	12.74	17.68
Consensus EPS (Rs)§	5.98	7.35	10.43	15.23
Revenue, net (Rs mn)	79,857	136,794	178,282	208,238
EBITDA (Rs mn)	13,199	19,894	24,540	31,032
ModelWare net inc (Rs mn)	8,524	11,815	13,581	15,904
P/E	33.8	33.4	5.1	4.3
P/BV	8.3	4.9	0.7	0.6
EV/EBITDA	24.6	21.8	6.6	5.1
Div yld (%)	0.5	0.4	3.5	3.9

Unless otherwise noted, all metrics are based on Morgan Stanley ModelWare framework (please see explanation later in this note).
§ = Consensus data is provided by FactSet Estimates.
e = Morgan Stanley Research estimates

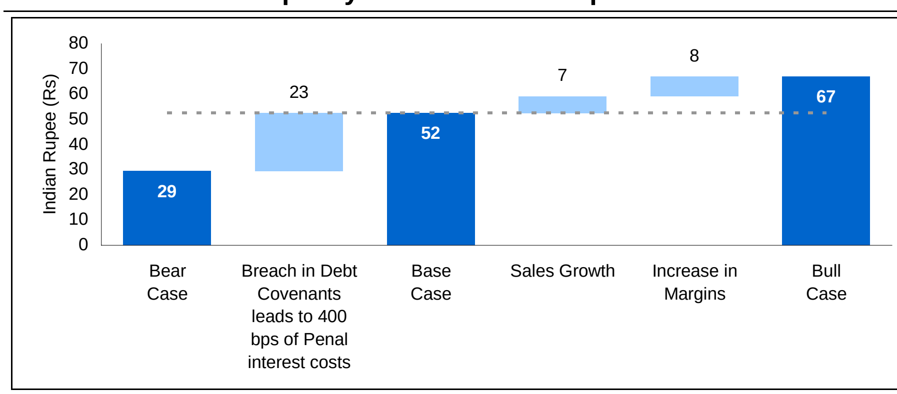
Risk-Reward: Suzlon Energy: (SUZL.BO, Rs44.45, EW, PT Rs52.45)

Too Much Risk on the Table despite High Rewards



Price Target Rs52.45		**Derived from our RI model**, with the base-case assumptions.
Bull Case Rs67.01	Implies 5.8x Bull Case F2010E EV/EBIDTA	There is a significant pickup in the global alternative energy market in F2011 and Suzlon's volumes rise 20%. Given high fixed costs, the company's margins expand by 20 bps to 15.1%
Base Case Rs52.45	Implies 5.1x Base Case F2010E EV/EBIDTA	Suzlon's volume growth slows down to 26% in F2009 and 15% over F2010-11E, in line with the global slowdown in alternative energy. Margins fall 80 bps in F2009 to 13.8% from already depressed levels in F2008. The company continues to grow strongly over 25 years, after which its revenues grow at 1.5% annually, given the industry's global nature.
Bear Case Rs29.47	Implies 35.8x Bear Case F2009E P/E	The Martifer stake purchase goes through (without delay) in F2009, resulting in a breach of the company's debt covenants. Suzlon's lenders charge a penal rate of interest of 400 bps.

From Bear to Bull: Capacity Additions Drive Upside



Source: FactSet, Morgan Stanley Research

Investment Thesis

- We expect a slowdown in global wind turbine market in C2009, with growth moving down to only 6% from 25% in C2008.
- We do not expect Suzlon to get access to REpower technology in the short term, thus resulting in customer concerns on Suzlon's technology remaining unresolved.
- We believe that unless the payment for the stake purchase (in REpower) from Martifer can be delayed, Suzlon might breach its debt covenants in F2009, potentially resulting in punitive action from lenders.
- Suzlon's in-house manufacturing facilities and high backward integration help control costs and avoid supply disruptions.
- Suzlon continues to remain one of the cheapest ways to play wind energy across the world.
- Longer term, we expect Suzlon to create an impressive franchise in the business as it rolls out its vision for REpower and Hansen.

Potential Catalysts

- A stake sale in Hansen could ease pressure on Suzlon's balance sheet, and be used towards financing the Martifer stake purchase.
- Order inflow growth will likely be the main catalyst for stock price on both the upside and downside. Suzlon's bookings against our expectations of around 1,250 MW over the next 6 months, should determine the potential of upside/downside surprise to numbers.

Key Long-Term Risk

- Other clean energy sources becoming more cost competitive.

Suzlon Financial Summary

Income Statement

Rs Mn ,March End	2007	2008	2009E	2010E
Revenue	79,857	136,794	178,282	208,238
Cost of Materials	47,882	88,702	117,235	133,387
Manufacturing and Operating Expenses	5,206	7,624	12,384	14,907
Employees Remuneration	6,682	10,430	13,619	16,700
Selling & Admin costs	6,889	10,145	10,504	12,213
Total Operating Expenses	**66,658**	**116,901**	**153,742**	**177,206**
Operating Profit	**13,199**	**19,894**	**24,540**	**31,032**
OPM Margin (%)	*16.5*	*14.5*	*13.8*	*14.9*
Interest	2,763	5,969	9,795	11,675
Depreciation & Amortization	1,722	2,894	4,515	6,681
Amortization of Goodwill	(4)	-	-	-
Non Operating Income	965	2,646	4,029	3,912
Profit Before Tax	**9,683**	**13,676**	**14,259**	**16,588**
Tax	1,146	1,991	1,887	2,134
Net Profit before Minority Interest	8,536	11,686	12,372	14,454
Share in associate's profits after tax	-	558	1,847	2,391
Minority Interest	(8)	(428)	(638)	(941)
Consolidated Net Profit	**8,528**	**11,815**	**13,581**	**15,904**
Exceptional Items	112	(1,514)	-	-
Reported Net Profit	**8,640**	**10,301**	**13,581**	**15,904**

Balance Sheet

	2007	2008	2009E	2010E
Share Capital	2,878	2,994	2,998	2,998
Reserves & Surplus	31,226	77,917	89,472	103,004
Employee Stock Options	117	102	-	-
Mgmt option certificates	890	-	-	-
Shareholders' Funds	**35,111**	**81,013**	**92,470**	**106,002**
Preference Share Capital	25	25	25	25
Deferred Tax Liability	1,625	2,059	2,093	2,120
Minority Interest	141	10,244	10,882	11,822
Loan Funds	**51,620**	**99,346**	**94,367**	**88,836**
TOTAL LIABILITIES	**88,522**	**192,687**	**199,836**	**208,805**
Gross fixed assets	25,568	42,075	63,471	92,708
Less: Depreciation	(7,016)	(10,318)	(14,833)	(21,514)
Add: Capital WIP	4,537	11,197	30,296	13,718
Net Fixed Assets	**23,089**	**42,954**	**78,933**	**84,911**
Net Goodwill	17,643	13,923	13,923	13,923
Investments	156	31,418	55,351	55,361
Cash and Marketable Securities	15,383	69,602	11,240	9,827
Deferred Tax Asset	1,448	1,841	1,841	1,841
Debtors	25,704	46,906	47,316	55,266
Loans & Advances	12,076	18,250	24,587	28,717
Inventory	31,363	40,848	47,720	54,294
Sundry Creditors	16,029	30,435	30,705	34,936
Other Liabilities and Provisions	22,310	42,620	50,369	60,400
Net Current Assets	**30,804**	**32,949**	**38,548**	**42,942**
Total ASSETS	**88,522**	**192,687**	**199,837**	**208,806**

Cash Flow Statement

	2007	2008	2009E	2010E
Cash Flow from Operations				
Reported PAT	8,640	10,301	13,581	15,904
Add: Depreciation & Amortization	1,718	2,894	4,515	6,681
Add: Deferred Tax	(126)	(23)	(34)	(27)
Less: Misc Expenditure w/off	(25)	-	-	-
Change in working capital	(11,691)	(2,146)	(5,599)	(4,394)
Operating cash flow	(1,434)	11,026	12,464	18,164
Cash Flow from Inv Activities				
Capital Expenditure	(18,416)	(22,759)	(40,495)	(12,659)
Acquisition of Goodwill	(17,625)	3,720	-	-
Investments	(80)	(31,262)	(23,934)	(10)
Others	2,088	9,262	603	995
Total	(34,032)	(41,039)	(63,826)	(11,673)
Cash Flow from Fin Activities				
Equity Issuance	45	38,269	4	-
Dividend Paid	(1,674)	(1,763)	(2,026)	(2,372)
Net issuance of Pref Capital / Debt	46,963	47,726	(4,979)	(5,531)
Total	45,334	84,232	(7,000)	(7,903)
Net Change in Cash	9,868	54,219	(58,362)	(1,413)
Opening Cash Balance	5,515	15,383	69,602	11,240
Closing Cash Balance	15,383	69,602	11,240	9,827

Key Ratios

	2007	2008	2009E	2010E
EPS (Rs)	5.9	7.9	9.1	10.6
P/E	33.8	5.8	5.1	4.3
BVPS (Rs)	24.4	54.1	61.7	70.7
P/BV	8.2	0.8	0.7	0.6
DPS	1.0	1.0	1.6	1.8
Dividend Yield (%)	0.5	2.2	3.5	3.9
EV/EBITDA	24.6	5.5	6.6	5.1
Profitability(%)				
NPM (%)	10.7	8.6	7.6	7.6
OPM (%)	16.5	14.5	13.8	14.9
EBIT Margin (%)	14.4	12.4	11.2	11.7
ROE (%)	27.4	20.3	15.7	16.0
ROCE (%)	18.7	12.6	11.9	13.5
Gearing				
Debt/Equity (%)	147.1	122.7	102.1	83.8
Net Debt/Equity (%)	103.3	36.7	89.9	74.5
Others				
Effective Tax Rate(%)	11.8	14.6	13.2	12.9
CEPS	7.0	9.8	12.1	15.1
Growth (%)				
Sales Growth (%)	107.9	71.3	30.3	16.8
EBIDTA Growth (%)	50.1	50.7	23.4	26.5
Net Profit Growth (%)	12.3	38.5	14.9	17.1
BVPS Growth (%)	29.1	121.8	14.0	14.6

E = Morgan Stanley Research estimates
Source: Company data, Morgan Stanley Research

Investment Case

Summary & Conclusions

Over the last six months Suzlon has been hit by quality perception issues, with around 104 blades on the company's workhorse turbine (Exhibit 1), the 2.1MW (V2 version) cracking due to the inability of the design to handle the stress created in operations. While the company has diagnosed the problem and come up with a solution (retrofitting/strengthening the blades) which is backed up by the results of RCA (root cause analysis), and has begun to sell an advanced version (V3) which does not have the same issues, we believe it has had a severe impact on order flow.

Despite Suzlon's problems in the recent past, we had faith in the company on the back of two arguments – namely that drawing a trend from one quarter of low order inflows was incorrect and that the company would soon get access to REpower's technology taking the concerns away from the medium and long term scenarios. We believed that to the next stage of growth at Suzlon being powered by REpower technology (3MW, 5MW and 6MW turbines).

The latter clearly looks unlikely in the short term, with Suzlon deciding to cancel its plan to exercise a domination agreement (necessary for transfer of technology) on the back of opposition from lenders who will be financing the next stage of growth at REpower. The former argument on the other hand has also fallen through with the order inflows for F2Q09 (down 73% YoY and 29% QoQ) actually worsening from F1Q09 levels. We believe that measuring quality is a preserve of the customers rather than the equity market, and the slowdown in order inflows (Exhibit 5) clearly indicates that customers are concerned.

Suzlon's quality perception problem is compounded by the headwinds the wind energy industry is beginning to face globally. With oil selling off dramatically, the standalone viability of wind power, which had begun to look reasonable in the high fuel price environment, has gone back to earlier levels. More importantly in our view, the credit crisis has become a significant challenge to growth with downstream wind power producers struggling to access capital (both debt and equity) in these markets. We believe that the risk is spreading from only small developers to utilities and large developers scaling back their capex plans. We believe Suzlon's large exposure to the Indian market (composed of small corporate developers), makes this issue even more critical for the company.

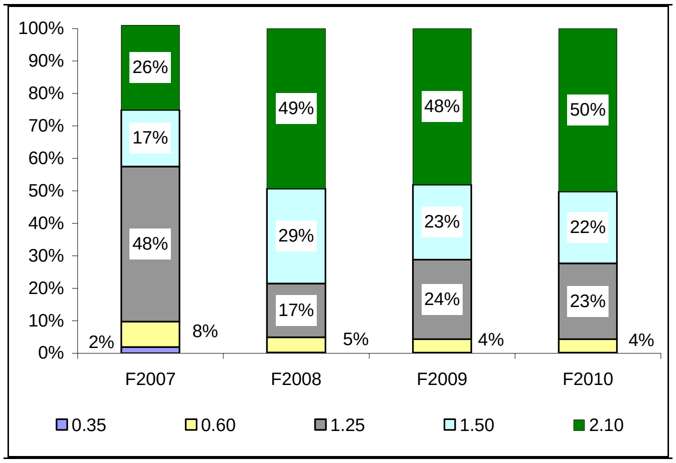
Based on the low visibility of Suzlon's order book in this challenging environment, we have scaled down our volume growth assumptions significantly for Suzlon (Exhibit 11). We lower our volume estimates in F2009 and F2010 by 17% and 24% respectively, which still assumes that the company will gain market share in the slowing global market. Our new estimates also require Suzlon's bagging 1,259 MW of foreign orders in the next 6 months (for execution in F2010), which appears challenging vs. 1,115 MW (after adjusting for the 315 MW Edison order cancellation) of orders won in the last 12 months.

We also add REpower into the financials for the first time (albeit through a single line item rather than a full consolidation), given that the company is now a subsidiary with Suzlon's acquisition of Areva's stake. Despite the added support of profits from REpower, our volume downtick and assumption of a pricing cut of 2% in F2010 (as companies pass on the benefit of lower commodity costs to customers), along with the higher interest costs on Suzlon's debt results in a downtick in EPS estimates for F2009 and F2010 by 29% and 40% respectively.

We believe that with the cancellation of the US$400 million rights issue, debt will become the primary source of funding the growth at Suzlon. We believe that Suzlon management is doing all the right things - trying to delay the purchase of Martifer's stake in REpower and cutting back on capex (from Rs16.43 billion to Rs9.74 billion for F2H09). However, on our reduced numbers, we still perceive risk to Suzlon's debt covenants, which potentially could result in punitive action by lenders. If the Martifer stake purchase cannot be pushed back, we could see Suzlon breaching its debt covenants (both the Net Debt to Equity and DSCR requirements), which potentially might lead to punitive action from lenders.

While the longer-term story for the wind energy sector and Suzlon continues to look excellent, we believe that the challenge to growth has gone up dramatically in the short term. Hence we downgrade to an Equal-weight rating based on the attractive valuations (F2010 EV/EBIDTA of 4.7x) being balanced by the high risk in the short term. While the stock, given its high beta and depressed valuations, could rebound strongly on any good news, given the increasing risk on the table (especially on the balance sheet), we would prefer to stay on the sidelines until we have more clarity on the movement in order inflows and on the delay on the stake (in REpower) purchase from Martifer.

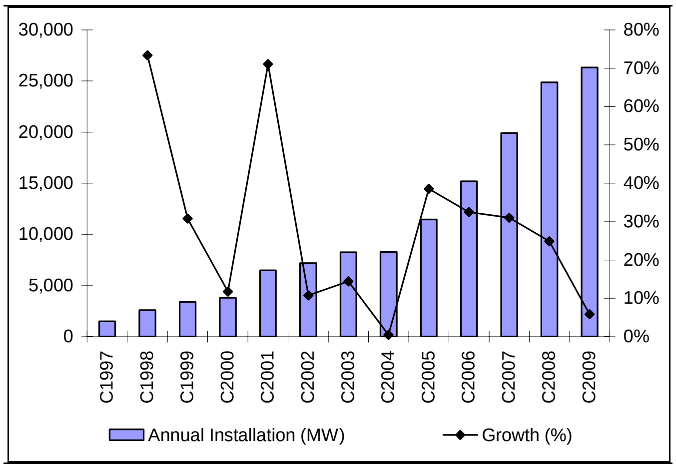
Exhibit 1
2.1 MW Turbine is the Workhorse of Suzlon's Portfolio – Sales (MW), F2007-10E



Source: Company data, Morgan Stanley Research

For Suzlon, the situation is even more challenging as around 40% of its business comes from India (Exhibit 4), mainly a market of small developers – corporates who are looking for tax benefits from the development of wind power. Our interaction with some of the Indian companies who were planning to put up wind power projects over the next 18-24 months indicates that in an environment where they are struggling to raise capital for funding their core business itself, plans for wind power have clearly been put on the back burner. While in the longer term the market appears to be transitioning towards the more traditional utility players (trying the reach the alternative energy targets set by various state governments), we expect the market over the next 24 months to continue to be driven by the small corporate developers.

Exhibit 2
Slowdown in Wind Power Installations in C2009



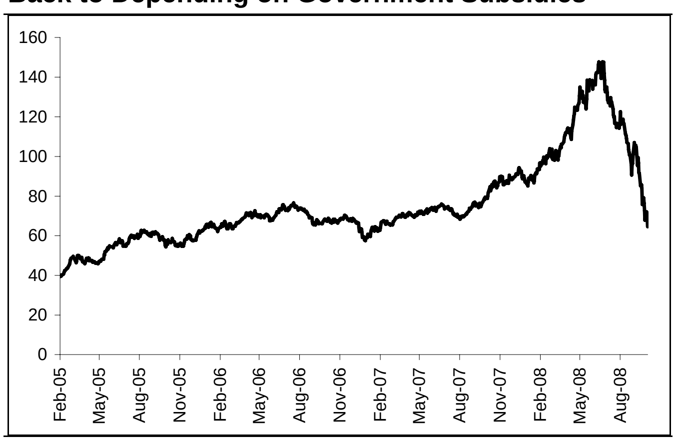
Source: Company data, Morgan Stanley Research

Slowdown around the Corner in the Global Market

With oil prices selling off dramatically, the standalone viability of wind power, which had begun to look reasonable in the high fuel price environment, has gone back to earlier levels. However, with government support continuing based on the twin factors of a cleaner environment and energy security, the wind sector should continue to do well. Unfortunately, we believe the credit crisis has become a significant challenge to growth with downstream wind power producers struggling to access capital (both debt and equity) in these markets. While we had been only concerned with small developers' ability to access the project finance market, now we are becoming wary of utilities and large developers scaling back their capex plans. While most of the large customers across the top companies have not announced a delay or cancellation, some have begun to talk of flexibility in the capex.

In our view, the key question for investors is how much could the wind market slow down as a result of the credit environment, and whether we could even see a contraction like in C2004. While our European clean energy team does not believe that the environment is not as bad as in C2004 (when a sharp drop in demand in both the US and Germany resulted in a decline in global demand), they have lowered their growth forecasts for the industry in C2009 to 5% from 25% in C2008 (Exhibit 2). Given our interaction with Suzlon, which indicates that unless the credit crisis eases out in the next 6 months, F2010 could actually be a flat year for the global market, there still seems to be potential downside risk to our global growth numbers.

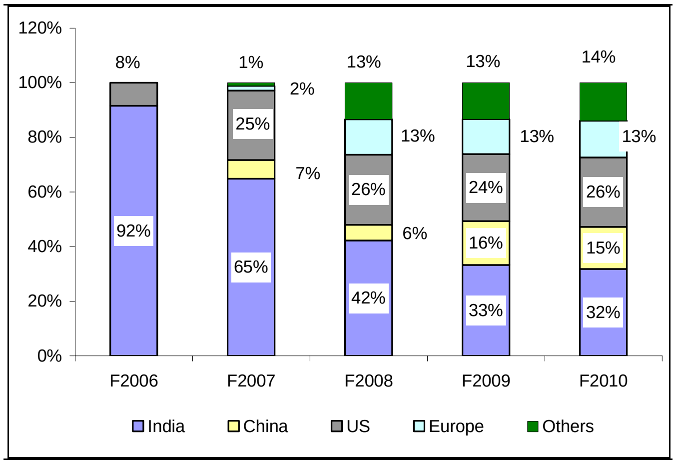
Exhibit 3
Oil (Brent) Retracing its Rise Takes Clean Energy Back to Depending on Government Subsidies



Source: Company data, Morgan Stanley Research

Exhibit 4

Geographical breakup of Suzlon's Sales, F2006-10E



Source: Company data, Morgan Stanley Research

Suzlon Continue to Lag Peers in Order Flows in F2009
Over the last six months Suzlon has been hit by quality perception issues, with around 104 blades on the company's workhorse turbine, the 2.1MW (V2 version) cracking due to the inability of the design to handle the stress created in operations. While the company has diagnosed the problem and come up with a solution (retrofitting/strengthening the blades) which is backed up by the results of RCA (root cause analysis), we believe it has had a severe impact on order flow.

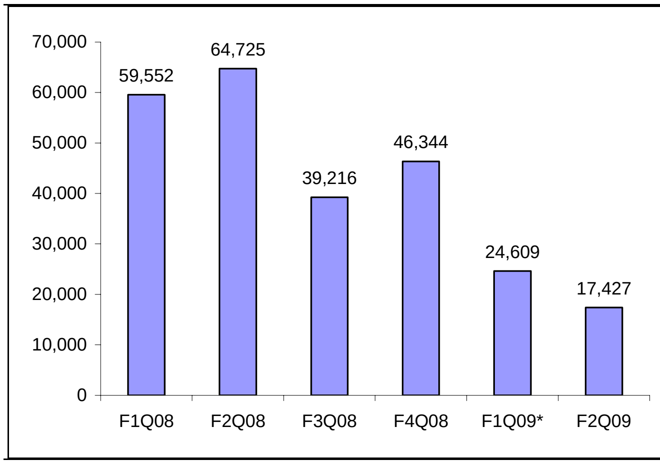
In F1Q09, while the order backlog was up 22% YoY, new order inflows were down 68% YoY (after adjusting for the Edison order cancellation.) However, on the conference call the management said that the company is negotiating some large sized, multi year contracts with existing and new customers, easing our concerns. Also past history lent strength to the management's contention, with a similar fall in F3Q08 having been followed by a significant recovery in F4Q08.

However, F2Q09 order inflows have actually worsened, with inflows at Rs17.4 billion moving down 73% YoY and 29% QoQ. The order book is actually down 14% YoY, which posed a massive risk to the high volume growth (CAGR of 38% over F2008-10E) we had built into our earlier forecasts for the company. While the exposure to India (42% of F2008 MW sales and 9% of MW order book), where orders are placed relatively close to the time of delivery, can explain some of this decline most of it is lead by the foreign order book, which is down 11% YoY. When seen vs. our expectations that foreign sales will grow to 68% of MW delivered in F2010 (from 58% in F2008), this clearly highlighted the risk to our volume estimates.

While some of the slow down can be blamed on the tougher environment for wind power, the company has significantly lagged its peers (even smaller ones) on order flows over the last 6 months, indicating that it has issues over and above the general slowdown. After having comfortably outstripped its peers in revenue growth over the last few years (Exhibit 7), Suzlon looks likely to underperform them as its share of orders in F1H09 moves significantly lower than its current market share (Exhibit 9).

Exhibit 5

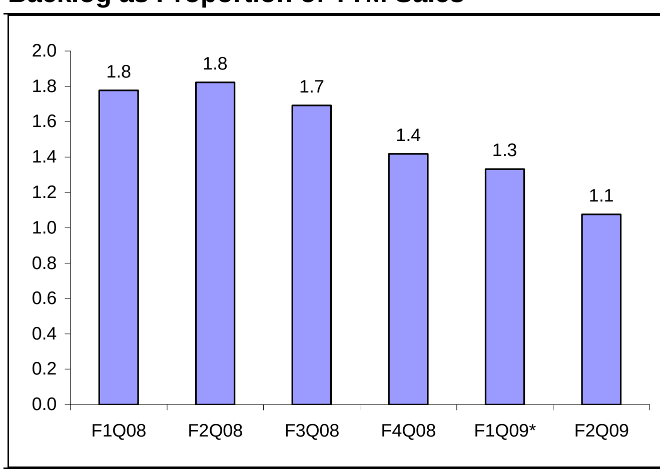
Sharp Decline in Suzlon's Order Inflows (Rs Mn) Over Last Six Months



Source: Company data, Morgan Stanley Research

Exhibit 6

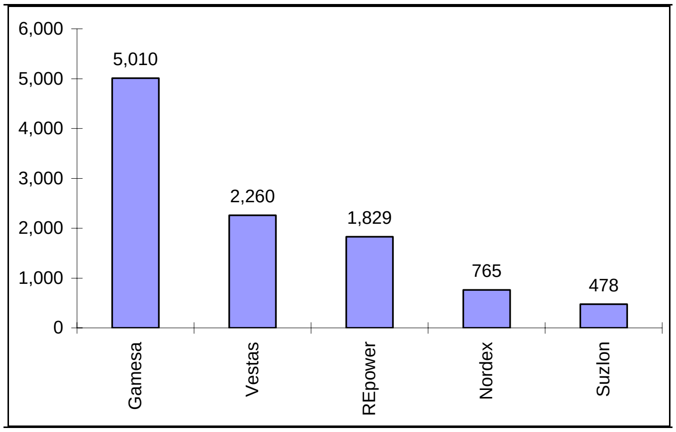
Backlog as Proportion of TTM Sales



Source: Company data, Morgan Stanley Research, * Adjusted for Edison order cancellation

Exhibit 7

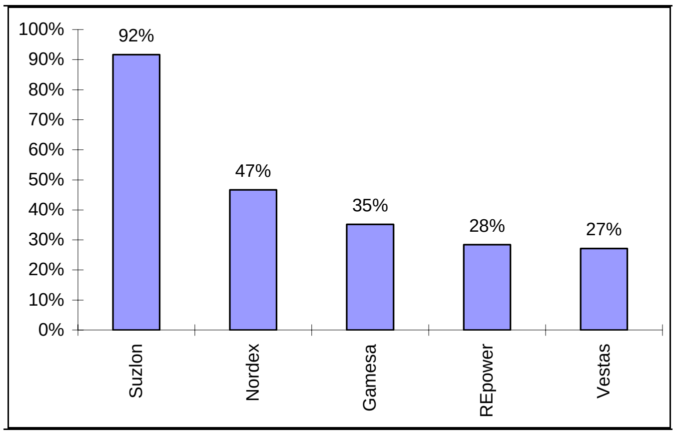
Share of Orders, based on F2009 Announcements



Source: Company data, Morgan Stanley Research

Exhibit 8

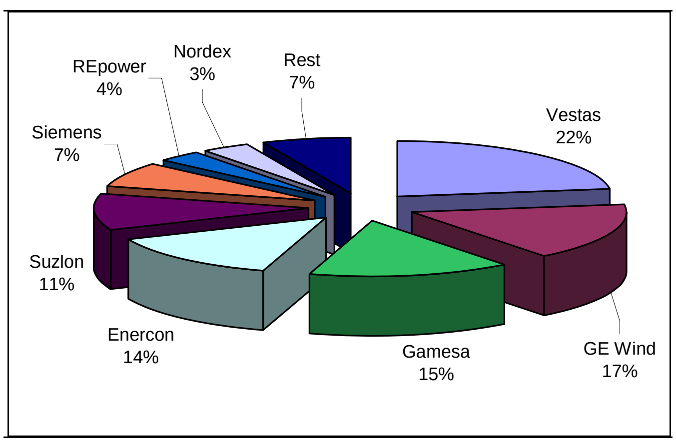
Revenue CAGR over F2005-08 / C2004-07



Source: Company data, Morgan Stanley Research

Exhibit 9

C2007 Market Share in Wind Installations



Source: Company data, Morgan Stanley Research

Making Access to REpower Technology Critical

In May 2007, Suzlon acquired a controlling stake in REpower, the eighth-largest wind turbine manufacturer in the world in terms of MW sold in 2006. In our opinion, REpower was a good strategic fit. REpower was struggling to mange its supply chain, as it sources most of its components from outside suppliers, but has a strong brand name in Europe. Suzlon, on the other hand, has a ready-made supply chain to help boost REpower's margins and the financial strength to help REpower grow its revenues, in our view. Suzlon also got access to offshore technology (the growth area of the future, in our opinion) through this acquisition, as well as REpower's recently developed 5MW turbine.

Suzlon paid around €450 million for a 33.6% stake in REpower and had agreements with Areva (29.9% stake) and Martifier (23% stake) for transfer of their stakes. Under the arrangement with Areva, Areva had a put option on its stake in REpower and could exercise it any time after May 2008. As per Areva's press release, the company has an exit guarantee ensuring value creation of over €350 million for its investment in REpower. We estimate Suzlon paid around €420 million to purchase this stake in F1Q09. Martifier (the original promoters of REpower) had a 23% stake in REpower and we expected Suzlon to pay around €270 million for it by May 2010.

While Suzlon struggled to bag orders in the last six months, REpower on the other hand started signing larger orders leveraging on Suzlon's delivery chain, which should ensure that the company would no longer have supply chain based hiccups in growth. This led us to believe that the transfer of the technology, possible after a domination agreement would have eased concerns on Suzlon's technology issues leading to the next stage of growth at Suzlon being powered by REpower technology (3MW, 5MW and 6MW turbines.)

The company also moved the acquisition schedule up on the Martifer stake from May 2009 to November 2008. However, the company ran into funding issues on the debt front with the credit crunch leading to the debt's potential cost moving up too much for comfort. To avoid the high cost debt and ease an already geared balance sheet, Suzlon announced a rights issue of US$400 million to fund the acquisition of the stake from Martifer. They also announced that they were going to pursue a domination agreement, which would have entailed making an open offer to the minority shareholders of REpower. Last week however, Suzlon cancelled its plan to exercise the domination and profit transfer agreement with REpower. This is due to opposition from lenders who will be financing the next rounds of growth for REpower.

Despite Suzlon's problems in the recent past, we had faith in the company on the back of two arguments – namely that drawing a trend from one quarter of low order inflows was incorrect and that the company would soon get access to REpower's technology taking the concerns away from the medium and long term scenarios. We believed that which now looks unlikely in the short term.

Assumptions Look Challenging Even After the Cut

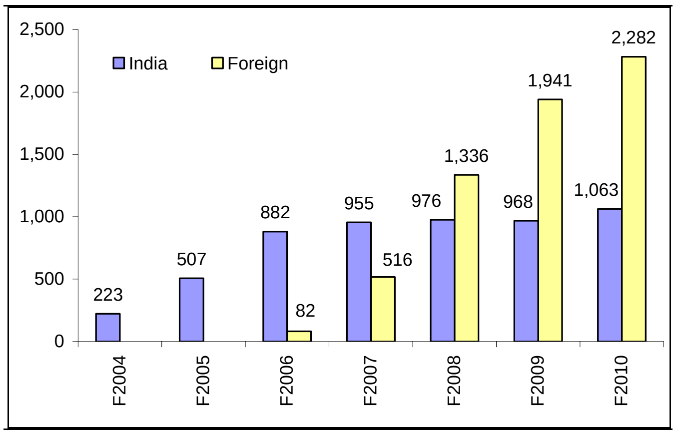
We have scaled down our volume growth assumptions significantly for Suzlon (Exhibit 11) to account for the current order book position as well as for the worsened global environment. Our new estimates assume that the majority of the 2,269 MW foreign order book gets executed in F2H09, in line with the delivery schedule communicated by the Suzlon management. This leaves 1,023 MW outstanding for F2010, vs. our estimates of execution of 2,282 MW of foreign orders in F2010, thus meaning that the company needs to bag 1,259 MW of foreign orders (mainly from Europe and China) over the next 3-6 months. Given that the foreign orders bagged over the last 12 months total up to only 1,115 MW (after adjusting for the 315 MW Edison order cancellation), we believe that this is a challenging task, especially in the slowing environment. We also do not account for any delays on the current foreign order book, which looks optimistic in the current credit environment.

The impact of the decline in volume estimates is exacerbated by the assumption of a decline in pricing, which looks likely as customers begin to pressure companies to pass on the benefits of the dip in steel. Our Hansen numbers on the other hand move up significantly, as we incorporate the model of our Hansen analyst, Allen Wells, vs. our earlier estimates (before the initiation of coverage on Hansen). We also incorporate the financials for REpower in our model (albeit through a one line entry rather than a line-by-line consolidation) since REpower has moved to being a subsidiary rather than an associate with the stake purchase from Areva in F1Q09.

Our EBIDTA estimates for Suzlon's business ex-Hansen and REpower (i.e. the WTG division) move down 19% and 26% for F2009 and F2010 respectively, driving the net income estimates down 44% and 53% for the two years. However, the support from the robust subsidiary numbers results is keeping the decline in our total net income estimates for the consolidated company in F2009 and F2010 down to 29% and 39% respectively. There could be upside risk potential to our numbers if Suzlon ends up bagging more than 1,259 MW of foreign orders for delivery before March 2010, or if its performance in the Indian market beats our expectations (Exhibit 10), both of which seem likely only in the event of an quick easing of the credit crunch.

Exhibit 10

Sulzon's Sales in India (in MW), F2004-10E



Source: Company data, Morgan Stanley Research

Exhibit 11

Change in Numbers

	Earlier Estimates		New Estimates		Change	
	F2009	F2010	F2009	F2010	F2009	F2010
Volumes (MW)	3,489	4,388	2,909	3,345	-17%	-24%
WTG Revenues	152,391	197,232	139,126	156,488	-9%	-21%
WTG EBIDTA	23,771	31,145	19,302	23,025	-19%	-26%
WTG Margin (%)	12.7	12.6	10.8	11.1	-1.9	-1.5
Total Revenues	187,469	247,693	178,282	208,238	-5%	-16%
Total EBIDTA	28,188	38,027	24,555	31,047	-13%	-18%
Total Margin (%)	15.0	15.4	13.8	14.9	-1.3	-0.4
Interest	5,472	6,506	9,795	11,675	79%	79%
WTG PAT	17,493	23,056	9,711	10,529	-44%	-54%
Share in REpower PAT	0	0	1,847	2,391	NA	NA
PAT (Incl REpower in new est.)	19,073	26,482	13,581	15,904	-29%	-40%

Source: Company data, Morgan Stanley Research estimates

Risk on the Balance Sheet Increasing

In this credit-crunched environment, we believe that bankruptcy risk has become the new benchmark to measure companies. We expected an easing of the leverage on Suzlon's balance sheet through the rights issue of US$400 million. We believed that the lowering of the debt: equity ratio from 1.2:1 in F2008, would ease investors concerns on the financial risk at the company. We believe that the main covenants on Suzlon's debt are as follows:

- Limiting the Net Debt to Equity ratio to lower than 1:1
- Limiting the Net Debt to EBIDTA Ratio to lower than 4:1
- Maintaining a Debt Service Coverage Ratio of over 1.33

With these covenants at group level rather than only for the standalone company, Suzlon gets the benefit of Hansen and REpower's financials, both of which score better than Suzlon on these parameters, and help in pushing the company over the bar.

We also believe that Suzlon's management team is cognizant of the risks on this front and is clearly taking the right steps. Given the cancellation of the rights issue and the plans to exercise the domination agreement, Suzlon is trying to negotiate with Martifer to push back the stake purchase (which had been advanced by nearly 6 months). It has also scaled back on its aggressive capex plan deciding to cut out a tower manufacturing facility in favour of continuing to source locally in its various markets, which reduced its F2H09 capex by Rs6.69 billion to Rs9.74 billion.

Based on our current numbers, Suzlon at group level should manage to deliver on its covenants in F2009, though it could be a close shave with Net Debt to Equity Ratio at 0.87x and DSCR at 1.34x for F2009. However, if the Martifer stake purchase cannot be delayed, then we believe there is potential risk of the company violating the covenants on Net Debt to Equity and DSCR (Debt Service Coverage Ratio) as shown in Exhibit 12. In our view, such a violation could lead to a variety of potential punitive actions from lenders including calling back loans and charging penal interest rates, both of which could have significant detrimental impact on Suzlon's P&L and balance sheet.

Recent news articles suggest that the company is looking for private equity infusion at the parent (Suzlon) level to finance stake purchase from Martifer (in case it cannot be delayed). While the company has refused to comment on this matter, this could be a way to ease the pressure on the balance sheet. Another option open to the company in our opinion is the sale of a stake in Hansen. With Hansen's current market cap of around GBP700 million, if Suzlon could reduce its stake to a bare majority of 50.1%, it could end up raising Rs12 billion, which could help finance around 60% of the stake purchase, and result in Suzlon's not violating its DSCR covenant. Also, given that the profit from the sale of a stake in Hansen would count towards an increase in equity, the net debt to equity covenant would not be violated either. Suzlon's stake in

Hansen comes out of the lock-in period on December 11, 2008 (12 months after Hansen's IPO date.)

Exhibit 12

Suzlon's Debt Covenants at Risk of Violation if Stake Purchase from Martifer Cannot Be Delayed

Group Level	F2009	If Stake Purchase Happens
Gross Debt	95,555	112,485
Cash	15,544	15,544
Net Debt	80,011	96,941
Equity	92,470	92,470
Net Debt : Equity	**0.87**	**1.05**
Interest Payments	9,873	11,622
Debt Servicing Requirements	11,050	11,050
EBIT	28,039	28,039
DSCR	**1.34**	**1.24**
EBITDA	29,347	29,347
Net Debt to EBITDA	**2.73**	**3.30**

Source: Company data, Morgan Stanley Research
Highlighted ratios mark breach of covenants

Downgrading Rating to EW, TP Lowered to Rs52.45

The stock has underperformed the Indian market massively from its peak led by the quality perception issues flowed by the meltdown in emerging markets and lastly followed by the meltdown in the wind energy space (on the back of the fears of slowing demand). We believe that most of the bad news is priced into the stock, but believe that the incremental negative news in the market could continue to hurt the stock in an environment in which investors have no patience for bad news.

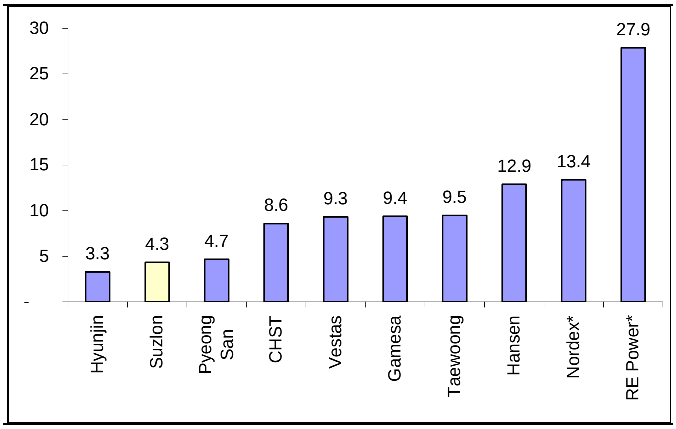
In addition, unless the Martifer stake purchase issue is resolved, we believe Suzlon is at risk of violating its covenants to its lenders. We find the risk hard to price in since the lenders will have a variety of resorts open to them in case of a breach, some of which might end up damaging the company's P&L and balance sheet. We believe an outcome worse than this scenario is unlikely, even on our lowered projections, but hesitate to completely rule it out in this capital-starved environment.

We continue to value the company on a residual income model, though the increase in the cost of debt (risk free rate), the risk premium for India as well as the beta for the company drives the cost of equity up massively. Finally, given the balance sheet issues, we assume that the beta of the stock will rise another 10% to 1.52 (from 1.38 for the last 12 months and 1.11 when we last priced the stock in March, 2008.) Given the new cost of equity of 18.6% (vs. 12.6% when we last priced the stock) as well our the massive reduction in our earnings estimates, our target price moves down 88% to Rs52.45, implying a 22% return from current price.

While the stock continues to look extremely cheap vs. mainline peers (Vestas and Gamesa) on PE multiples, its trading more or less in line with them on EV/EBIDTA multiples, which we think are a better benchmark given the concerns on the balance sheet. At our target price, the company will trade at an F2010E EV/EBIDTA of 5.5x, which while attractive on an absolute basis, will imply a 18-24% premium to the C2009E EV/EBIDTA ratios for its nearest peers, Vestas and Gamesa.

Exhibit 13

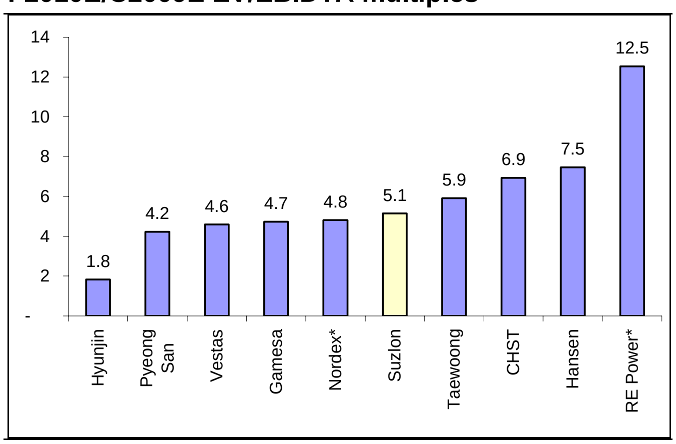
Still Trading at Significant Discount to Mainline Peers on F2010E/C2009E P/E Multiples



Source: Company data, Morgan Stanley Research

Exhibit 14

However, Trading in Line with Mainline Peers on F2010E/C2009E EV/EBIDTA multiples



Source: Company data, Morgan Stanley Research

Company Description

Suzlon Energy, now combined with REpower, is the third-largest wind energy solutions provider globally. It has substantial manufacturing facilities in India, the US, China, and Belgium. Its fully integrated business model includes consultancy, site development, design, manufacturing, and overhaul and maintenance services. Suzlon has had a market share above 50% in India in the past six years. It expects the majority of its revenues to come from international markets, primarily the US and China. Promoters own a 68.9% stake in Suzlon Energy.

India Capital Goods

Industry View: In-Line

MSCI Country: India

Asia Strategist's Recommended Weight: 2.7%
MSCI Asia/Pac All Country Ex Jp Weight: 6.5%

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Overweight/Buy	**869**	**39%**	**275**	**42%**	**32%**
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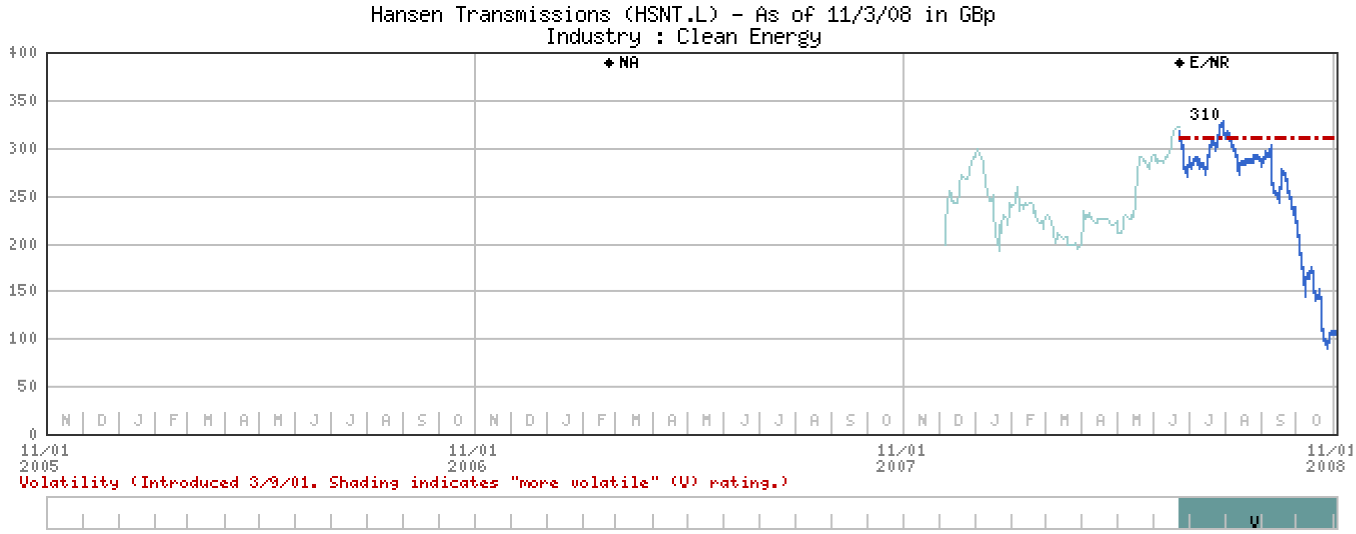
Stock Price, Price Target and Rating History (See Rating Definitions)



Stock Rating History: 2/23/07 : NA; 6/24/08 : E/NR

Price Target History: 6/24/08 : 310

Source: Morgan Stanley Research   Date Format : MM/DD/YY   Price Target   No Price Target Assigned (NA)

Stock Price (Not Covered by Current Analyst)   Stock Price (Covered by Current Analyst)

Stock Ratings abbreviated as below (Effective 3/18/02, ratings appear as Stock Ratings/Industry View) ◆

Stock Ratings as of 3/18/02: Overweight (O) Equal-weight (E) Underweight (U) More Volatile (V) No Rating Available (NAV)

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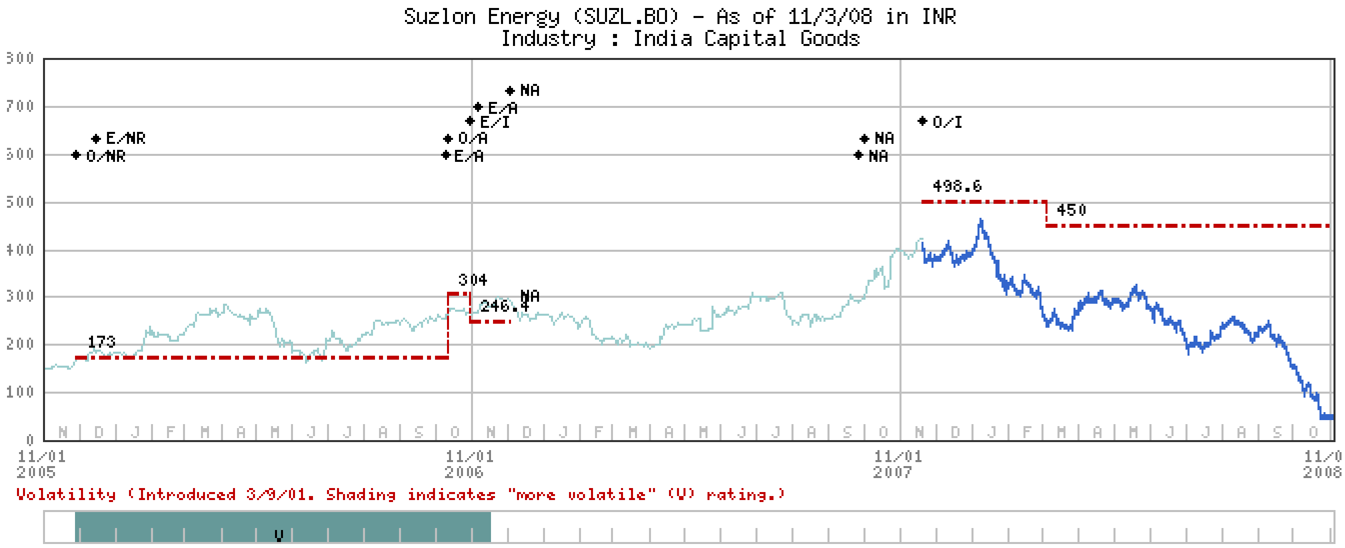
Industry View: Attractive (A) In-line (I) Cautious (C) No Rating (NR)



Stock Rating History: 11/28/05 : O/NR; 12/15/05 : E/NR; 10/9/06 : E/A; 10/11/06 : O/A; 10/30/06 : E/I; 11/6/06 : E/A; 12/4/06 : NA; 9/27/07 : NA; 10/2/07 : NA; 11/20/07 : O/I

Price Target History: 11/28/05 : 173; 10/11/06 : 304; 10/30/06 : 246.4; 12/4/06 : NA; 11/20/07 : 498.6; 3/4/08 : 450

Source: Morgan Stanley Research Date Format : MM/DD/YY Price Target -- No Price Target Assigned (NA)
Stock Price (Not Covered by Current Analyst) Stock Price (Covered by Current Analyst)
Stock Ratings abbreviated as below (Effective 3/18/02, ratings appear as Stock Ratings/Industry View) ◆
Stock Ratings as of 3/18/02: Overweight (O) Equal-weight (E) Underweight (U) More Volatile (V) No Rating Available (NAV)
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Industry Coverage:India Capital Goods

Company (Ticker)	Rating (as of)	Price (11/03/2008)
Akshay Soni		
BHEL (BHEL.BO)	E (10/02/2007)	Rs1,341.15
Suzlon Energy (SUZL.BO)	E (11/04/2008)	Rs45.95

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