MORNING INSIGHT

Kotak Securities

PRIVATE CLIENT RESEARCH

JULY 15, 2010

Economy News

- A panel headed by the finance minister will only be an arbiter of last resort in disputes between regulatory bodies, as the government seeks to allay concerns among financial sector regulators, particularly the central bank, that their autonomy is under threat, a senior government official has said. (ET)
- Stiff competition from cheap quality Chinese goods is compelling Indian electrical equipment manufacturers to press for imposition of anti-dumping duties. According to the Indian Electrical and Electronics Manufacturers Association (IEEMA), China has over 90% share in the quantity of imports of such products into India. (ET)
- The annual rate of inflation for June fell shy of expectations, but stayed put above 10% for a fifth month, raising the prospect of the Reserve Bank of India increasing key rates later this month to rein in galloping prices. The wholesale price index rose to 10.55% in June from a year ago, just short of 10.81% forecast by analysts in a Reuters poll, data released on Wednesday showed. (ET)

Corporate News

- Ajay Piramal-led **Piramal Healthcare Ltd (PHL)** is gearing up for major acquisitions in the contract manufacturing segment. The decision comes after hiving off its flagship formulation division to multinational drug maker Abbott for over Rs 17,500 crore and its ailing pathology and radiology laboratory network to Super Religare Laboratories Ltd (SRL) for Rs 600 crore. (BS)
- Financial services firm **Religare Enterprises** has agreed to buy a part of Citigroup's home loan portfolio in India for nearly Rs 500 cr. snapping up a key asset that promises to amplify its presence in the consumer lending business. (ET)
- Construction major **L&T** is all set to bag the mandate to develop the Rs12,132-crore Hyderabad Metro Rail Project Ltd (HMRL), by virtue of seeking the lowest viability gap funding (VGF) support of Rs 1,458 crore. L&T's bid emerged the lowest among the financial bids of six consortia, which were opened on Wednesday at the HMRL office here. (BS)
- Housing finance major **HDFC Ltd** posted a net profit of Rs 695 crore for the quarter ended June 30, 2010, an increase of 23 per cent over Rs 565 crore in the same period last year. The rise in profits was on account of growth in interest income as the company had nil profit from sale of investments in the just-ended quarter, said Mr Keki Mistry, CEO and Vice-Chairman. Last year, the profit from sale of investments was Rs 51 crore. (BL)
- Nearly 13 years after it had last issued bonus shares, India's second largest two-wheeler maker **Bajaj Auto** today said it was planning a similar move, for which its board would meet on July 22. (BS)
- State-owned **Oil & Natural Gas Corporation (ONGC)** plans to invest $4 billion to develop the ultra-deepwater gas find and produce about two trillion cubic feet (tcf) of gas from its Krishna-Godavari basin block. (ET)
- **Reliance Communications** may have to lower the value of its tower assets being sold to GTL Infrastructure in view of a likely stake sale in the Indian telecom service operator to Dubai-based Etisalat. The cut in valuation could range between Rs 2,500 crore to Rs 4,000 crore. (ET)
- **ICICI Bank's** plan to sell its 19.49 per cent stake in business process outsourcing company Firstsource is facing a road block. Its recent talks to sell the stake to private equity firm KKR have also failed. Its outstanding convertibles are a big bone of contention." Firstsource raised $275 million (around Rs 1,265 crore) through foreign currency convertible bonds (FCCBs) in 2007 to fund the acquisition of MedAssist. Since then, Firstsource has bought back FCCBs worth $62.6 million, bringing down the total outstanding issue size to $212 million (around Rs 990 crore). (BS)

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, BL = Business Line, ToI: Times of India, BSE = Bombay Stock Exchange

Equity

		% Chg		
	14 Jul 10	1 Day	1 Mth	3 Mths
Indian Indices				
SENSEX Index	17,938	(0.3)	3.0	1.7
NIFTY Index	5,386	(0.3)	3.1	2.1
BANKEX Index	11,335	0.3	4.4	7.4
BSET Index	5,325	(1.4)	0.0	(3.6)
BSETCG INDEX	15,076	1.1	6.0	7.2
BSEOIL INDEX	10,643	(0.7)	3.3	4.9
CNXMcap Index	8,347	(0.3)	4.8	5.4
BSESMCAP INDEX	9,370	(0.3)	6.2	3.7
World Indices				
Dow Jones	10,367	0.0	(0.4)	(7.0)
Nasdaq	2,250	0.3	(2.4)	(10.6)
FTSE	5,254	(0.3)	0.7	(9.8)
Nikkei	9,795	2.7	(2.0)	(14.0)
Hangseng	20,561	0.6	2.7	(7.0)

Value traded (Rs cr)

	14 Jul 10	% Chg - Day
Cash BSE	4,309	5.0
Cash NSE	15,269	8.6
Derivatives	84,914.4	5.8

Net inflows (Rs cr)

	13 Jul 10	% Chg	MTD	YTD
FII	804	(28)	7,076	37,320
Mutual Fund	(137)	(27,420)	(244)	(8,371)

FII open interest (Rs cr)

	13 Jul 10	% Chg
FII Index Futures	16,979	0.6
FII Index Options	52,610	2.2
FII Stock Futures	31,455	(0.3)
FII Stock Options	1,507	2.8

Advances / Declines (BSE)

14 Jul 10	A	B	S	Total	% total
Advances	70	812	194	1,076	40
Declines	134	1110	247	1,491	56
Unchanged	0	86	15	101	4

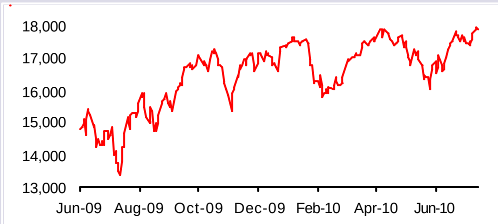
Commodity

			% Chg		
		14 Jul 10	1 Day	1 Mth	3 Mths
Crude (NYMEX)	(US$/BBL)	77	(0.5)	(0.4)	(10.4)
Gold	(US$/OZ)	1,208	(0.3)	(1.8)	4.6
Silver	(US$/OZ)	18	0.3	(1.1)	(0.3)

Debt / forex market

	14 Jul 10	1 Day	1 Mth	3 Mths
10 yr G-Sec yield %	7.63	7.62	7.65	N/A
Re/US$	46.68	46.78	46.49	44.47

Sensex



RESULT UPDATE

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INFOTECH ENTERPRISES LTD (IEL)

PRICE: RS.175 **RECOMMENDATION: ACCUMULATE**
TARGET PRICE: RS.189 **FY11E P/E: 12.4X**

Infotech's results for 1QFY11 were below expectations. While revenues were in-line, EBIDTA margins were significantly lower. Revenue growth of 6.5% in CC terms is a positive. UTG revenues de-grew for the third successive quarter and this is of concern to us. However EMI (70% of revenues) continued to report strong growth (10.6% volume growth QoQ). The results reflect concerns which we had expressed on margins of Infotech. The impact on margins has been higher than our expectations. Salary increments had an impact; currency fluctuations and higher direct costs further impacted margins. We expect EBIDTA margins to fall to 18.5% in FY11. Overall, we reduce our earnings estimates on relatively lower margin assumptions. Our FY11 EPS estimate stands revised to Rs.14.1 (Rs.15.4 earlier). Consequently, our PT stands revised to Rs.189 v/s Rs.220 earlier. We downgrade the stock to ACCUMULATE due to limited upside. We believe that, Infotech will have to address concerns on proportion of project-based revenues (in UTG), client concentration for IEL (Top 5 makes 42% of revenues) in addition to currency fluctuations before we turn more positive. Exit multiple works out 14x FY11E EPS, about 40% discount to sector leaders.

Summary table

(Rs mn)	FY09	FY10E	FY11E
Sales	8898	9531	10849
Growth (%)	32.0	7.1	13.8
EBITDA	1785	2083	2010
EBITDA margin (%)	20.1	21.8	18.5
PBT	985	2079	1809
Net profit	925	1708	1561
EPS (Rs)*	16.7	30.9	14.1
Growth (%)	9.6	84.7	-54.3
Net debt	-3139	-4888	-6055
ROE (%)	12.8	20.1	15.7
ROCE (%)	13.6	24.2	18.0
CEPS	25.2	38.8	18.5
Op cash flow	1785	2239	2118
Net working capdays	74.1	68.7	65.6
P/E (x)	20.9	11.3	12.4
P/BV (x)	2.5	2.1	1.8
DPS (Rs)	1.5	2.0	2.0
EV/Sales (x)	1.8	1.5	1.2
EV/EBITDA (x)	9.1	6.9	6.6
P/Cash Earnings	13.9	9.0	9.5

Source: Company, Kotak Securities - Private Client Research

** FY11 EPS on post-bonus equity (1:1)*

1QFY11 results - disappointing

	4QFY10	1QFY11	QoQ (%)	1QFY10	YoY (%)
Income	2440.7	2528.0	3.6	2326.0	8.7
Expenditure	1914.5	2124.9		1802.4	
EBDITA	**526.2**	**403.1**	**-23.4**	**523.6**	**-23.0**
Depreciation	92.9	116.8		117.6	
EBIT	**433.3**	**286.3**	**-33.9**	**406.0**	
Interest	25.0	2.4		2.4	
Other income	178.4	80.7		163.2	
PBT	**586.7**	**364.6**	**-37.9**	**566.8**	**-35.7**
Tax	102.7	74.0		149.7	
PAT	**484.0**	**290.6**	**-40.0**	**417.1**	**-30.3**
Sh of profit	29.5	36.8		41.4	
MI	-0.1	1.5		4.1	
Adj PAT	513.4	328.9	-35.9	462.6	-28.9
EPS (Rs)*	**4.65**	**2.98**		**4.19**	
Margins (%)					
EBDITA	21.6	15.9		22.5	
EBIT	17.8	11.3		17.5	
PAT	19.8	11.5		17.9	

*Source : Company; * On post-bonus equity*

Revenues were up 3.6% - EMI grows faster but UTG de-grows likely due to client issues

- Revenues for the quarter were higher by about 3.6% on a sequential basis. Daxcon financials were consolidated for the full quarter v/s 2.5 months in the previous quarter.
- Within verticals EMI grew 6.3% QoQ; this vertical contributes c67.5% of company revenues. UTG vertical on the other hand de-grew by 6% QoQ, after a 2.4% de-growth in Q3FY10. We believe this helped revenues growth by __%.
- In terms of volumes, UTG reported a 2% decline QoQ. We believe this was likely due to continuing client issues and the projects based nature of UTG revenues.
- The management did indicate that, one of the large orders from a leading client (Swisscom) continued to scale down during the quarter and new projects will start only in 2QFY11.
- This is the third successive quarter of declining revenues in UTG and is of concern to us.
- However, the management has indicated that, the business will report about 4 - 5% QoQ growth in INR revenues in 2QFY11.
- EMI, on the other hand, continued to report strong sequential revenue growth. During the quarter, volumes grew by 10.6% QoQ.
- We understand this was due to the scale up is existing accounts and scale up in new accounts from Hamilton Sunstrand and Westinghouse. However, the scale up in Westinghouse will be more gradual.
- Infotech has penetrated the UTC group well with cumulative revenues of more than $250mn. It now operates at ACE Gold level across all divisions of UTC.
- The management has developed initiatives for broadening its concentrated revenue base (Top 5 make 41.4% of revenues in 1Q); we have seen early results as this concentration is down from 43.4% in Q4FY10.
- We opine results of this 'diversification and growth' strategy will be important for IEL's broad based growth, and also to break past the Rs.2.4bn quarterly revenue mark, where the company looks to have stagnated for the last four-five quarters.
- We note cross currency headwinds impacted IEL meaningfully given the Europe revenue concentration (42.7% of Q4FY10 revenues and 38.4% of 1QFY11 revenues). INR revenues grew by 3.6% v/s a 6.5% CC growth.
- Infotech bagged 12 new accounts during the quarter comprising 6 in the EMI vertical and 6 in the UTG vertical. In addition to the Hamilton, Westinghouse and Seawell contracts in 2QFY10, the company notched up impressive client wins in the UTG vertical in 1QFY11.
- The company believes the Hamilton engagement has the potential to scale up to 400 engineers in the next three years.
- Management believes the coming quarters are likely to see healthy net employee additions and is targeting a net addition of close to 1600 over FY11E as the macro for IT services is expected to improve meaningfully starting CY10. We believe this will be largely back-ended.

EBIDTA margins were a major negative surprise; fall was larger than expected

- EBITDA margins for the quarter were down by about 561bps QoQ. While we had raised concerns on Infotech's margins in the previous quarter, the fall was larger than expected.
- According to the management, currency movements impacted margins by about 390bps. Apart from this, the salary increments at 10% for off-shore employees and 2-3% for on-site (500bps impact) and investments in delivery infrastructure also impacted margins. Higher revenues off-set this severe impact to some extent.
- We had indicated that, Salary increments, higher levels of utilization (EMI) and need to invest in business generating initiatives will put pressure on margins.

Wage hikes, higher S&M expenses - margin headwinds

- Going forward, as the company looks to invest in S&M, in an improving macro environment, we believe this cost head could see inflation.
- An appreciating INR can be another headwind, in our opinion. We have assumed rupee to appreciate to 45.5/USD by FY11E end.
- The company plans to add higher number of employees (>1600) over the coming quarters and this may impact utilization levels.
- However, the broadening of the pyramid, control on costs and higher revenues may lead to a sequential improvement in margins.
- For FY11, we expect margins to move to close to 18% v/s 21.8% in FY10.

Higher 'other income' and lower tax set off some reduction in EBIDTA

- Infotech reported a other income component of Rs.80mn comprising of interest and dividend income of Rs.40mn and a marginal Rs.2mn gain on forex. There was a one time service tax write back of Rs.23mn.
- On the forex front IEL currently employs a cover of $21mn, Euro 6.3mn and 3.3mn GBP. These are expected to mature over the coming months, going up to October 2010, according to the company. Average contract rates for the USD cover are at INR 40.6-40.7 for about $7mn and INR 47.62 for the remaining ($14mn), according to the management.
- The company has stated that its forward contracts FY11E onwards qualify for cash flow hedge accounting, and as such will sit in the exchange fluctuation reserve in the balance sheet and will be expensed through the P&L as and when they come up for expiry. We believe this is likely to make the other income line less volatile in a dynamic currency environment.
- The company provided tax at the rate of 20% of PBT and expects the same to move up to about 22 - 23% in FY11.

Reduce FY11 estimates

- We have moderated our earnings expectations for FY11, on the back of lower margins for the fiscal.
- We forecast a 14% rise in revenues YoY on the back of a 23% rise in EMI revenues. UTG revenues are expected to remain largely stable in FY11. .
- However, we believe that, margins will be under pressure and expect the same to fall to 18.5% v/s 21.9% in FY10. This is despite an improvement assumed over 1QFY11 levels.
- PAT is expected to fall by about 9% in FY11E to Rs.1.56bn.

Deep relationships with existing customers and differentiated service offering augur well over the longer term

- Infotech has managed to deepen client engagement for clients like SP AusNet, P&W, Bombardier, Tele-Atlas & Swisscom over the recent quarters and enjoys relationships with marquee clients in its verticals.
- Management continues to see opportunities in the higher thrust which aero-space companies (bombardier, etc are major clients) are giving to efficient and light engine design skill sets- areas where IEL has domain expertise and existing impressive client roster.

We recommend ACCUMULATE on 189 with a price target of Rs.189

- Its JV with HAL has started netting small sized contract wins of close to Rs.10-15mn. This part of the business is expected to materially benefit from opportu-nities in the domestic aero business.
- We have in our DCF model built in higher growth rates for Infotech over the medium term, given the improving demand environment.

Concerns

- A sharp acceleration in the rupee from our assumed levels will impact earnings estimates negatively for the company.
- Belying of hopes of a pick up in the economic outlook of major user economies could impact revenue growth of Infotech.

RESULT UPDATE

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HDFC LTD

PRICE: RS.3077 **RECOMMENDATION: ACCUMULATE**
TARGET PRICE: RS.3125 **FY11E P/E: 26.5x; P/ABV: 5.5x**

- **Advances growth remained healthy during Q1FY11 on the back of improved disbursements; up by 17% yoy to Rs.1016bn.**
- **Core interest income growth remained steady, supported by lower interest cost leading to stable interest spreads at 2.34% as compared to 2.3% in FY10;**
- **Net profit grew by 23% yoy to Rs. 6.9bn; which was lower than our expectation of Rs. 7.3bn; lower than expected bottom-line growth was mainly due to higher operating expenses and absence of treasury profits.**
- **Long term outlook appears positive for HDFC; we continue to maintain our earnings estimates. Based on SoTP valuations we arrive at a price target of Rs.3125 (Rs.2002 +Rs.1124).**

Summary table

(Rs bn)	2010	2011E	2012E
Int. Income	109.0	128.8	156.2
Int. expenses	70.6	81.9	99.2
NII	38.3	46.9	57.0
Non-Int Income	4.6	5.9	7.0
Total Income	42.98	52.75	64.10
Optg Profit	39.7	48.3	59.1
PAT	28.3	33.4	40.6
GNPA - 6 mths(%)	0.7	0.6	0.5
NNPA (%)	0.2	0.1	0.1
Spreads (%)	2.2	2.2	2.2
RoA (%)	2.7	2.7	2.7
RoE (%)	20.0	21.3	23.7
Divi. Payout (%)	29.5	25.8	21.2
EPS (Rs)	98.4	116.2	141.3
BV (Rs)	529.3	562.8	631.7
Adj. BV (Rs)	524.1	559.5	633.2
P/E (x)	31.3	26.5	21.8
P/ABV (x)	5.9	5.5	4.9

Source: Company, Kotak Securities - Private Client Research

Quarterly performance

(Rs bn)	Q1FY11	Q4FY10	Q1FY10	YoY%	QoQ %
Interest income	26.2	26.9	26.3	-0.6	-2.6
Interest expenses	17.2	15.6	19.6	-12.4	10.3
Net Income	**9.0**	**11.3**	**6.7**	**34.2**	**-20.5**
Other Income	1.9	1.7	2.2		
Total Income	**10.8**	**12.9**	**8.9**	**22.1**	**-16.4**
Operating Expense	1.0	0.6	0.9		
Operating profit	**9.8**	**12.4**	**7.9**		
Loan loss provision	0.2	0.2	0.1		
Profit before tax	9.7	12.2	7.8	23.9	-20.9
Provisions for taxes	2.7	3.4	2.2		
Profit after tax	**6.9**	**8.8**	**5.7**	**22.9**	**-21.2**
PAT incl. extr-ordi gains	6.9	9.2	5.7	22.9	-24.7
EPS	**24.4**	**32.5**	**19.9**		
Cost/Income ratio (%)	9.3	4.4	10.6		
Effective Tax rate (%)	28.1	27.8	27.6		
Mortgaged Loan (Rs bn)	1,016.3	979.7	870.5	16.7	3.7

Source: Company

Healthy growth in Disbursements led to 16.7% yoy and 3.7% qoq growth in mortgage loan book to Rs. 1016bn.

- HDFC continued to witness healthy growth in mortgage loan growth following the special home loan rate offered in competition with the leading banks and housing finance companies. Its mortgaged loan book grew by 16.7% yoy and 3.7% qoq during Q1FY11 to Rs.1016bn.
- Its individual loan approvals during the Q1FY11 grew by 55% yoy and its individual disbursements grew by 65% yoy. Given the steady demand for real estate, baring few pockets, HDFC has clocked a healthy growth in its individual portfolio.
- We opine that the 8.25% home loan scheme will continue to benefit HDFC in sourcing individual loans. On the other hand, the scheme is less likely to have a significant impact on its interest spread because of the reset after 6 months to 9.25% and an applicable floating rate thereafter.

- HDFC sources loan through its own network of 277 outlets (including 64 offices of HDFC distribution company and HDFC Sales Private Ltd), and has also tied-up with HDFC Bank.

Core interest income growth remained steady, supported lower interest cost leading to stable interest spreads; higher than expected operating expenditure and absence of treasury gains impacted bottom-line growth

- HDFC's core earnings improved on the back of decline in cost of funds. Its interest spread on loans for Q1FY11 remained firm at 2.34% as compared to 2.3% in Q4FY10. HDFC has benefit from being a bulk borrower and a superior credit rating (AAA) raising funds at competitive rates.
- NII for Q1FY11 grew by 34% yoy and to Rs. 8.9bn as compared to Rs.6.7bn in Q1FY10. This was largely at the back of a 12% yoy decline in interest cost and for Q1FY11. Its overall operating income grew by 22% to Rs. 10.8bn, which are relatively lower than our expectation due to lower than expected income from other operating and absence of treasury profits during Q1FY11.
- Operating expenses during Q1FY11 relatively higher than our expectation; operating expenses increased by 7.3% yoy to Rs. 1008mn as compared to Rs. 940mn in Q1FY10. Provision for loan loss stood at Rs. 150mn, up by 25% yoy as compared to Rs.120 mn in Q1FY10.
- Treasury gains during Q1FY11 were absent, as compared to Rs. 510mn in Q1FY10. As we had indicated in our earnings preview, our estimates will continue to remain sensitive to treasury gains.
- **Asset quality** - remained largely stable at 0.9%, with provision coverage of around 77%. Its Net NPA also remained lower at 0.2% during Q1FY11 at Rs. 2.07bn (Rs 1.94bn in Q1FY10).

Increased stake in Credila Financial Services

HDFC has acquired additional 10% stake in the education loan arm Credila Financial Services, to increase its stake to 51%. It has acquired close to 41% stake in November 2009 from DSP Merrill Lynch. HDFC will leverage on its network and tie-ups to source education loans. The book size is miniscule and therefore we have not factored any value from this company.

Valuation at current levels offer limited upside, recommend accumulating the stock on declines

- HDFC approved a stock split in the ratio of 5:1 i.e. from face value of Rs. 10 to Rs. 2, with the view to increase liquidity and increase retail investor's participation in the company.
- Given the improved performance of HDFC Standard Life insurance, we have marginally tweaked our valuations and estimates for HDFC's life insurance arm. We HDFC Standard Life at Rs. 385 (Rs 356 earlier)

We recommend ACCUMULATE on HDFC with a price target of Rs.3125

- Our valuation for the stock is based on sum-of-the-parts (SOTP) methodology. We have valued the core business on dividend discount model at Rs. 2002, which is 3.5x its FY11 adjusted book value of Rs.559. We have valued HDFC subsidiaries- life insurance, AMC, general insurance, HDFC bank and other investments at Rs. 1125 (factoring in a 15% holding company discount). This leads to a price target of Rs.3125.
- On the back of limited upside from current levels we recommend investors to accumulate the stock on declines. Value unlocking from its life insurance business is impending and will be solid trigger for the stock. At the current market price, the stock is trading at 3.5x its FY11 P/ABV (stripping the value of investments and subsidiaries). We recommend accumulating the stock with a price target of Rs.3125.

COMPANY UPDATE

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BAJAJ AUTO LTD (BAL)

PRICE: RS.2439 **RECOMMENDATION: BUY**
TARGET PRICE: RS.2680 **FY11E P/E: 15.5x**

We are increasing BAL's earnings estimate for FY11 in view of the company's strong performance YTD coupled with buoyant outlook for the 2W industry in general. We are increasing our FY11 volume estimates by 10% from 3.42mn units to 3.77mn units. Net profit estimates for FY11 now stands at Rs22,808mn versus our earlier estimate of Rs.20,609mn. Our revised FY11E EPS stands at Rs157.6 (earlier Rs142.4). Due to positive revision in our FY11 earnings estimates, we are revising out target price on the stock upward to Rs2,680 (from earlier Rs2,280) and upgrade the stock to BUY.

Summary table

(Rs mn)	FY09	FY10	FY11E
Sales	88,435	119,482	153,312
Growth (%)	(1)	35	28
EBITDA	12,385	26,232	32,264
EBITDA margin (%)	14.0	22.0	21.0
Net Profit	6,545	17,036	22,808
Debt	15,700	13,386	13,457
EPS (Rs)	45.2	117.8	157.6
DPS (Rs)	22.0	40.0	40.0
RoE (%)	47.5	79.1	61.1
RoCE (%)	35.4	67.5	62.8
EV/Sales (x)	4.0	2.8	2.2
EV/EBITDA (x)	28.8	12.7	10.3
P/E (x)	53.9	20.7	15.5
P/BV (x)	20.9	12.1	7.8

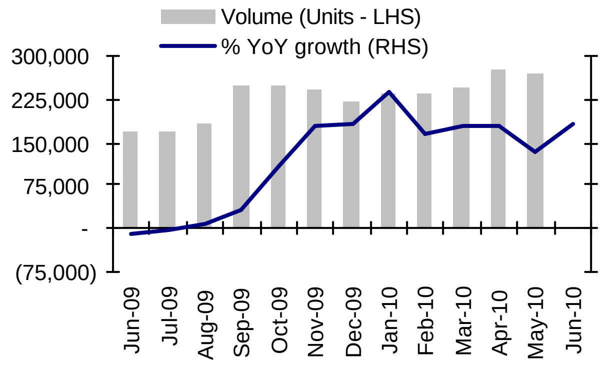
Source: Company, Kotak Securities - Private Client Research

Company looks firm on chasing the 4mn volume target

BAL has set for itself a target of selling 4mn units in FY11 representing a huge 40% jump over FY10 volumes of 2.9mn units. Given the company's performance during 1QFY11 the company looks very much firm on its guidance. To achieve the 4mn volume mark, the company expects to sell ~300,000 motorcycles on a monthly basis (3.6mn annually) and the remaining 400,000 units is expected to come from the 3W sales. The company is looking to export 1mn units in FY11.

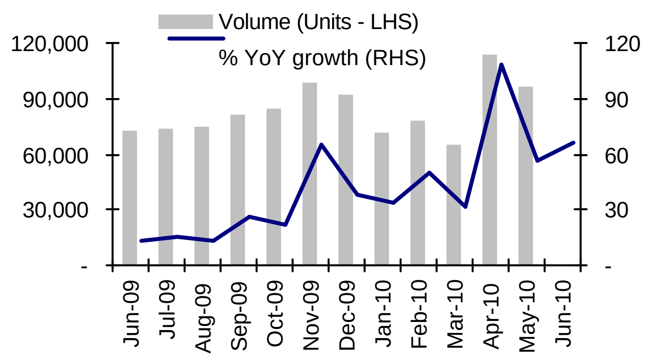
During 1QFY11 the company sold 928,336 units translating into a monthly run-rate of 309,445 units. 2W sales during 1QFY11 stood at 828,418 units (monthly run-rate 276,139 units). Volumes during 1QFY11 were to a certain extent impacted by production constraint and vendors inability to keep pace with the demand. However with production constraint issue sorted out, monthly production is expected to increase from July 2010 onwards. In the 3W segment the company sold ~100,000 units in 1QFY11 in line with their FY11 annual target of 400,000 units. With export volumes of 323,899 units in 1QFY11, we expect the company to surpass its export volume guidance of 1mn units in FY11.Demand outlook for the 2W's remains optimistic and we expect BAL to continue its strong performance on the volume front for the remaining part of FY11E.

2W sales volume trend



Source: Company

Export volume trend

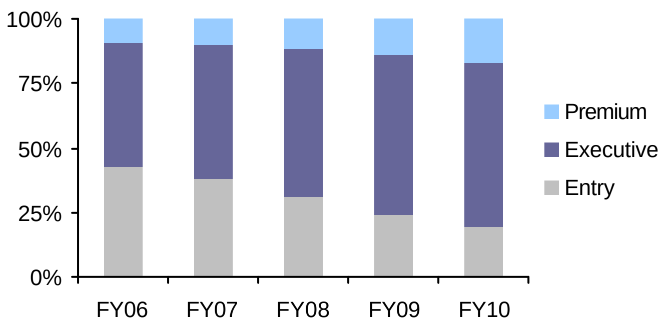


Source: Company

Dual brand strategy doing wonders for the company

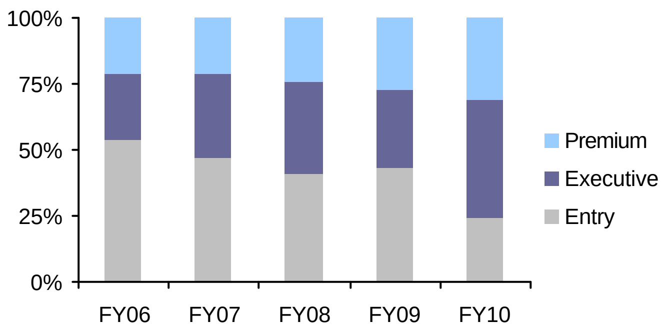
In FY10, the company adopted a significant shift in its strategy and the same has paved the growth path for the company. Changing its stance from focusing on the 125cc+ segment to dual brand strategy has improved the company's fortunes considerably. In addition to that the company has successfully reduced its exposure in the entry level segment in favor of the executive and the premium segment. As a result the company has shown notable improvement in market share and profitability.

Segment share - Industry



Source: Company

Segment share - BAL



Source: Company

BAL has created a strong franchise in the motorcycle segment through it's emphasize on Discover and Pulsar brand. Discover brand is positioned as a commuter bike where it is competing with the world's best selling model - Splendor. Currently the company is selling more than 100,000 units of Discover per month and it accounts for close to 40% of the company's motorcycle sales. Launch of Discover 150cc at competitive price point has further consolidated its position in the key executive segment. On the other hand, Pulsar, the company's sport bike model has received further boost with the launch of Pulsar135LS. Currently the company is selling more than 80,000 units per month and it accounts for almost 30% of the motorcycle volumes. Together they contribute ~70% of the company's motorcycle volumes. We expect BAL will continue to leverage on Discover and Pulsar brand and strengthen its position in the motorcycle industry.

Rationalizing operations to extract maximum advantage

BAL is looking to maximize its production from the Pantnagar plant in order to take advantage of various tax and duty related benefits. In FY10, the company produced 577,947 units from its Pantnagar plant, an increase of 82% over FY09. During 4QFY10 the company average monthly production was 60,000 units which are expected to have increased to 80,000 units per month in 1QFY11. BAL expects to further enhance the production to 120,000 units on a monthly basis from 3QFY11. Furthermore in order to maximize tax benefits the company has shifted manufacturing of products like Discover and Pulsar135 to Pantnagar. We are increasing our production estimates for the Pantnagar facility by 29% from 0.84mn to 1.08mn. Benefits from higher volume assumption from Pantnagar will have a positive impact on the company's FY11 earnings.

Plant Details

Plant	Capacity (mn units)		Products Manufactured	
	FY09	FY10	FY09	FY10
Waluj	1.86	1.86	Boxer, Platina, XCD, 3W	Boxer, Platina, Discover, 3W
Chakan	1.2	1.2	Pulsar, Avenger, Discover	Pulsar, Avenger, Discover
Pantnagar	0.9	1.2	Platina, Platina125, XCD	Platina, Platina125, Discover, Pulsar135

Source: Company

Subsidiaries continue to incur losses

- **Bajaj Auto International Holding BV (BAIH BV)**. BAIH BV is the Netherland based 100% subsidiary of Bajaj Auto formed with a view to focus on international ventures including acquisition opportunities. During FY08, BAIH BV acquired 24.45% stake in KTM Power Sports AG of Austria and has subsequently increased its stake to 35.67% with a total investment of Euro 140mn. In FY11 it is expected to launch the 1st product from the joint development exercise between BAL and KTM. BAIH BV posted net loss of Rs1,019mn in FY10.
- **PT Bajaj Indonesia (PT BAI).** PT BAI is the company's Indonesia based subsidiary with BAL holding 99% stake. PT BAI currently assembles semi-knocked down parts of Pulsars and markets them in Indonesia. During 2HFY11, it is expected to assemble complete knocked down parts which attracts lower customs duties in Indonesia. During 1QFY11 the company introduced Pulsar 135LS in the Indonesian markets. Since its incorporation in FY07, this subsidiary has been incurring losses. In FY10, PT BAI posted loss of Rs159mn as compared FY09 loss of Rs615mn. The company expects to further reduce its losses in FY11.

Issue of Bonus shares

BAL has announced that it is considering a proposal for declaration of bonus shares. The company will discuss the same at its Board meeting to be held on 22nd July 2010.

Upgrading estimates

We are increasing BAL's earnings estimate for FY11 in view of the company's strong performance YTD coupled with buoyant outlook for the 2W industry in general. We are increasing our FY11 volume estimates by 10% from 3.42mn units to 3.77mn units. We are now assuming 2W volume of 3.4mn units as against our earlier estimates of 3mn units. Due to higher sales proportion from executive segment and Pulsar135, we are lowering our realization estimates by 2% from our earlier assumptions.

We are increasing our revenue estimates for FY11 from Rs142,011mn to Rs153,312mn. We have marginally increased our EBITDA margin estimates by 20bps to 21%. Our revised EBITDA estimate of Rs32,264mn now stands 23% higher than FY10 EBITDA of Rs26,232mn.

We recommend BUY on Bajaj Auto with a price target of Rs.2680

In view of increase in our production estimates from the Pantnager facility, we are lowering our effective tax rate estimate to 28.3% from our earlier estimate of 29.1%. Accordingly our net profit estimates for FY11 now stands at Rs22,808mn versus our earlier estimate of 20,609mn. Higher estimated profit will leave additional free cash flows with the company. This will lead to higher income from investment activity and the same will percolate directly to the bottomline. Our revised FY11E EPS now stands at Rs157.6 (earlier Rs142.4).

Due to positive revision in our FY11 earnings estimates, we are revising out target price on the stock upward to Rs2,680 (from earlier Rs2,280) and upgrade the stock to BUY. Due to higher growth forecast, we value the stock at PE of 17x as against our earlier valuation multiple of 16x.

COMPANY UPDATE

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VOLTAMP LTD

PRICE: RS.1041 **RECOMMENDATION: REDUCE**
TARGET PRICE: RS.1050 **FY11E P/E: 10.9x**

The Voltamp stock has gained 18% in past few trading sessions. In the process the stock has achieved our target price. In view of this, we downgrade the stock to Reduce.

Management maintains that EBITDA margins may continue to remain under pressure atleast in the near-term. Cash generation has been lower due to expansion in working capital.

Downgrade to REDUCE with price target of Rs.1050 based on DCF. (Rs.1010 earlier)

Highlights

- For the year, the company sold 10009 MVA of transformers compared to 9540 MVA in FY09. For Q4, volumes were higher at 3485 MVA compared to 2450 MVA in Q4 FY09.

Summary table

(Rs mn)	FY09	FY10	FY11E
Sales	6431	5420	6483
Growth (%)	16	-16	20
EBITDA	1511	1058	1262
EBITDA margin (%)	24	20	19
PBT	1689	1223	1465
Growth (%)	36	-28	20
Net profit	1148	823	967
Net cash (debt)	60	43	1062
EPS (Rs)	114	81	96
Growth (%)	44	(28)	18
CEPS	118	87	104
DPS (Rs)	13	13	13
ROE (%)	53.0	27.6	25.9
ROCE (%)	79.0	41.2	39.3
EV/Sales (x)	1.5	1.7	1.3
EV/EBITDA (x)	6.0	8.5	6.4
P/E (x)	9.2	12.8	10.9
P/Cash Earnings	8.8	11.9	10.0
P/BV (x)	4.3	3.4	2.7
CEPS (Rs)	118.1	87.4	103.9

Source: Company, Kotak Securities - Private Client Research

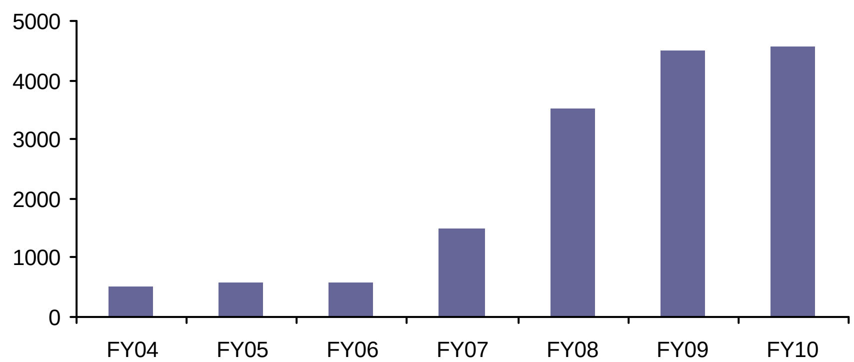
Product range

	Revenue mix (%)	
Power Transformer	49%	5-100 MVA, 33-220 KV
Distribution transformer	32%	0.5-5 MVA, 11-33 KV
Dry type transformer	19%	63 KVA-7.5 MVA, 11-33 KV

Source: Company

- Order backlog stands at Rs 4.1 bn, which is healthy as the company tends to maintain six months of revenue visibility. The management has indicated that demand scenario is improving consistently and this is reflecting in higher number of enquiries. However, the management is cautious in taking orders. Hence, the order backlog is sluggish at Rs 4.0-4.5 bn. We believe pace of order backlog may not accurately reflect future revenue growth trend as the product mix consists of several distribution transformers and dry-type transformers which are fast moving. The company has in FY10 raised its installed capacity to 13000 MVA from 9000 MVA and should be able to capitalize on acceleration in transformer demand. However, demand scenario for dry-type transformers continues to remain subdued due to the lackluster commercial real estate activity.

Order book (Rs mn)



Source: Company

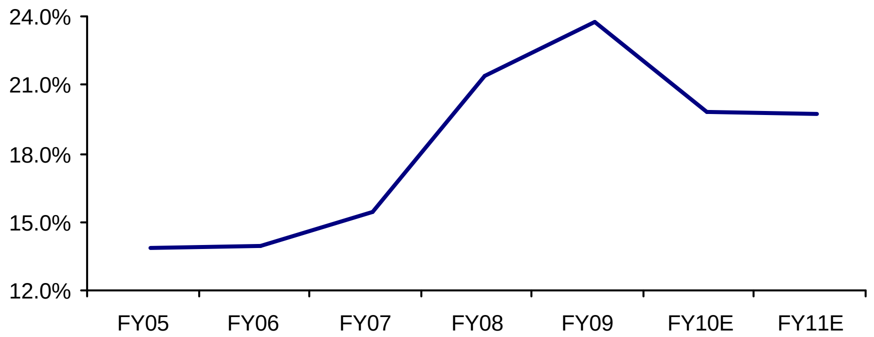
Top 7clients (close to 30% of revenues)

- GETCO
- BHEL
- Torrent Power
- ABB
- Siemens
- L&T
- Reliance Energy

Source: Company

- **Price scenario remains subdued:** Owing to increase in manufacturing capacity of transformer industry coupled with subdued demand from the industries, the realisations of transformer sector eroded by close to 12-15%. Areva T&D has set up its largest manufacturing plant in Vadodara, which has significantly increased competitive pressure in the market. The company expects realizations to recover from H2 FY11. The Voltamp management has indicated that Areva and ABB have also started to compete in 132 KV and 220 KV tenders and there has been pressure on pricing.
- **Margins likely to be maintained:** The company reported 19.5% EBITDA margins in FY10 and expects to maintain margins through value engineering.

EBITDA margins (%)



Source: Company, Kotak Securities - Private Client Research

- **Working Capital cycle has increased:** For FY10, net working capital cycle has increased from 51 DSO (Days of Sales) to 93 DSO mainly due to higher debtors which has increased from 51 DSO to 81 DSO.
- **Lower cash conversion due to expansion in working capital cash remains at high levels:** Cash and liquid investments at the end of FY10 stood at Rs 1.5 bn, equivalent to Rs 150 per share. The company remains debt free.

Transformer Industry Scenario

- Transformer makers had expanded capacities in anticipation of robust demand from the Power/Industrial sector. However, the economic slowdown in FY08-09 has decelerated corporate capex as well as spending on T&D thus translating into lower capacity utilization (close to 70%).
- On several occasions, customers are delaying taking deliveries of equipment that they had ordered, thus resulting in inventory build-up. Voltamp has been cautious in taking orders.
- Competition is intense in extra-high KV segment of 765 KV especially due to Chinese and Korean manufacturers. There are indications that PGCIL may impose import duty on T&D equipments.
- PGCIL - the prime transmission utility, needs to accelerate spending on transmission lines as it nears the end of XIth plan. It is reported that the company has planned spending worth Rs 130 bn in FY11 as compared to Rs 257 bn in FY08-10.

Valuation

We recommend REDUCE on Voltamp with an unchanged price target of Rs.1050

- Voltamp is currently trading at 10.9x FY11 earnings and a forward EV/EBITDA of 6.4x.
- Valuations are not expensive given stable margins, higher ROE and strong balance sheet of the company.
- We move rating to Reduce in view of recent stock movement and achievement of our target price. Maintain target price of Rs 1050 (Rs 1010 earlier).

Bulk deals

Trade details of bulk deals

Date	Scrip name	Name of client	Buy/ Sell	Quantity of shares	Avg. price (Rs)
14-Jul	Aishwarya Tele	Patel Vipul	B	114,847	29.7
14-Jul	Ajel Info	Arikatla Srinivasa Reddy	S	150,000	33.7
14-Jul	BF Utilities	T Rowe Price International Inc			
		A/C T Rowe Price New Asia Fund	S	266,018	740.8
14-Jul	Birla Shloka	Mohan Lal Agarwal	B	187,558	67.7
14-Jul	Birla Shloka	Sarswati Vincom Limited	B	100,000	66.5
14-Jul	Birla Shloka	Mohan Lal Agarwal	S	97,741	66.3
14-Jul	Birla Shloka	Param Commodities Private Limited	S	75,000	66.5
14-Jul	Birla Shloka	Apurva Commodities Private Limited	S	75,000	66.5
14-Jul	Dazzel Conf	Gale Inc-(Prop. Hemant S Lokhnade)Golden	B	30,000	29.5
14-Jul	Dmc Intl	Chetan Dogra HUF	S	111,836	14.2
14-Jul	Dynemic Prod	Ashutosh P Mehta	B	75,000	31.9
14-Jul	Filatex Fash	Sunita Bhansali	B	150,000	14.5
14-Jul	Filatex Fash	Epoch Synthetics Private Limited	B	100,000	14.3
14-Jul	Filatex Fash	Sanju Kabra	S	196,900	14.4
14-Jul	Filatex Fash	Mohta Securities Private Limited	S	56,582	14.5
14-Jul	Filatex Fash	M.P.Vora Shares & Sec P Ltd	S	56,835	14.6
14-Jul	Goldcrest Fin	Tarun Chmanlal Mehta	B	100,000	24.8
14-Jul	Goldcrest Fin	Prabha Dharamshi Pujara	S	100,000	24.8
14-Jul	Golden Sec	Manish Mehra	S	31,100	10.9
14-Jul	Hindustan Ever	Ashok Kumar Mehta.	B	12,167	19.6
14-Jul	IFL Promoters	Balwantsingh Bisht	B	20,000	20.1
14-Jul	IFL Promoters	Chetan Dogra	B	72,500	19.9
14-Jul	IFL Promoters	Seema Ramakant Parasrampuria	B	30,000	19.9
14-Jul	IFL Promoters	Ramakant Basudeo Parasrampuria	B	28,000	20.1
14-Jul	IFL Promoters	Inder Pal Dogra	S	30,000	20.1
14-Jul	IFL Promoters	Bibhash Bhubneshwar Jha	S	19,500	20.0
14-Jul	IFL Promoters	Chetan Dogra Huf	S	50,000	20.0
14-Jul	Indiaco Vent	Harshad Ichhashanker Bhatt	S	104,350	49.4
14-Jul	Jaihind Syn	Harsh Vadann Shah	B	25,000	21.0
14-Jul	Jaihind Syn	Jignesh J Dhabalia	S	75,000	21.1
14-Jul	Jaihind Syn	Dinesh Harji Patel	S	33,018	20.3
14-Jul	Kadvani Sec	Ashwinbhai Prabhudas Ruparel	B	19,011	20.6
14-Jul	Kailash Ficom	Shingar Dyes And Chemicals Ltd	B	95,000	49.7
14-Jul	Kailash Ficom	Nilesh Krushna Palande	S	55,000	49.9
14-Jul	Kailash Ficom	Abhijai Investment	S	60,000	49.8
14-Jul	Katare Spin	Seetha Bai	S	23,501	29.1
14-Jul	Kay Power	Prakashchand Gupta	B	208,400	20.5
14-Jul	Kddl	Kayimotradinginvestment	S	40,000	46.1
14-Jul	Kilpest India	Fatelal Bansilal Shah	B	42,800	12.3
14-Jul	Kilpest India	Kamleshgiri Mansukhgiri Goshwa	S	36,759	12.3
14-Jul	Kz Leasing	Eshin Rajnikant Patel	B	20,000	13.0
14-Jul	Kz Leasing	Jyotikaben Maheshbhai Hadvani	S	50,000	13.0
14-Jul	Liberty Phos	Jmp Securities Pvt Ltd	S	171,436	53.2
14-Jul	Liberty Phos	Hitesh Shashikant Jhaveri	S	82,240	53.1
14-Jul	Mahalaxmi Rub	Anurag Singh	B	52,439	182.6
14-Jul	Manugraph Ind	Ameeta Sanjay Shah	S	190,000	51.2
14-Jul	Marathwada Re	Raghu Hari Dalmia	S	5,050	452.8
14-Jul	Morganite Cruc	Sharad Shah	B	17,540	333.3

Trade details of bulk deals

Date	Scrip name	Name of client	Buy/ Sell	Quantity of shares	Avg. price (Rs)
14-Jul	Nexxoft Info	Samir Ashok Bhanushali	B	35,000	100.2
14-Jul	Nexxoft Info	C Geetha	S	28,000	100.4
14-Jul	Noida Medicare	Dheerajkumar Lohia	B	44,236	21.9
14-Jul	Noida Medicare	Hemant Kumar Motihar	S	50,000	21.9
14-Jul	Omkar Overseas	Madhusudan Sarda Huf	B	42,000	80.5
14-Jul	Omkar Overseas	Hitesh Kanabhai Bhutiya	S	31,314	80.5
14-Jul	Oregon Comm	Bhavesh Shantilal Trivedi	B	8,000	423.0
14-Jul	Oregon Comm	Harshil Dipak Shah	B	23,500	423.5
14-Jul	Oregon Comm	Nilesh Rasiklal Pandya	B	20,000	423.5
14-Jul	Oregon Comm	Sanjay Jethalal Soni	S	5,081	413.3
14-Jul	Oregon Comm	Amul Gagabhai Desai	S	5,285	413.7
14-Jul	Oregon Comm	Jimish Jitendrabhai Soni	S	5,245	417.7
14-Jul	PG Foils	Prem Cables Pvt Ltd	B	49,241	50.7
14-Jul	Piramal Glass	India Discovery Fund Limited	B	1,250,000	96.5
14-Jul	Piramal Glass	Glass Engineers Private Limited	S	1,441,944	96.5
14-Jul	Pithampur Steel	Komal Sharma	B	26,100	22.8
14-Jul	Pithampur Steel	Parminder Kaur	S	25,000	22.9
14-Jul	Polypro Fibrils	Hitesh Shashikant Jhaveri	B	35,350	20.4
14-Jul	Pondy Oxides	Aartiben Arvindkumar Thakkar	B	100,000	32.0
14-Jul	Pondy Oxides	Jnj Holding	B	73,000	29.8
14-Jul	Pondy Oxides	Dheerajkumar Lohia	S	62,502	30.2
14-Jul	Priyadarshini Sp	Usha Jindal	S	55,000	54.7
14-Jul	Ranklin Sol	Chiranjeevi Nandyala	B	39,000	127.5
14-Jul	Ranklin Sol	Anjaiah Chakali	S	27,924	118.1
14-Jul	Rich Capital	Ankit Jain	S	60,000	80.3
14-Jul	Rishi Laser	Ushadevi R Sanwalka	B	40,000	58.9
14-Jul	Sancia Glob	Wise Investments Private Limited	S	142,000	24.0
14-Jul	Shakti Pumps	Yaminiben Maheshbhai Pandya	B	61,000	204.0
14-Jul	Shakti Pumps	Hardik Maheshbhai Pandya	B	53,000	204.0
14-Jul	Shakti Pumps	Sunil Bhandari	B	31,000	211.0
14-Jul	Shakti Pumps	Prakash Laljibhai Patel	B	34,477	224.0
14-Jul	Shakti Pumps	Kamlesh Nahar	B	30,000	211.0
14-Jul	Shakti Pumps	Sanjay Kantibhai Baria	B	42,000	208.0
14-Jul	Shakti Pumps	Dynamic Stock Broking India Pvt Ltd	B	33,197	218.1
14-Jul	Shakti Pumps	Santosh Vishram Ghadshi	S	61,000	203.5
14-Jul	Shakti Pumps	Amar Premchand Walmiki	S	53,000	203.5
14-Jul	Shakti Pumps	Sanjay Kantibhai Baria	S	42,000	207.9
14-Jul	Shakti Pumps	Ashish Saboo Huf	S	50,000	213.0
14-Jul	Shakti Pumps	Dynamic Stock Broking India Pvt Ltd	S	31,182	218.0
14-Jul	SKS Logistics	Ace Shipping & Offshore Co.Pvt.Ltd.	S	82,790	35.6
14-Jul	Sky Inds	Jimeet Dilipkumar Shah	B	20,000	135.1
14-Jul	Socrus Bio	Vidhata Securities Pvt Ltd	B	180,000	10.3
14-Jul	Socrus Bio	Vrp Financial Services Pvt Ltd	S	164,374	10.3
14-Jul	Socrus Bio	Avinash Arvind Jagushte	S	180,000	10.3
14-Jul	Tamboli Cap	Yuma Financial Services Pvt Limited	B	100,000	24.7
14-Jul	Zylog Systems	Argonaut Ventures	S	100,000	502.6

Source: BSE

Gainers & Losers

Nifty Gainers & Losers

	Price (Rs)	chg (%)	Index points	Volume (mn)
Gainers				
L&T	1,884	2.5	8.2	2.0
SBI	2,465	1.5	3.2	1.8
HDFC Bank	2,086	0.7	1.7	1.1
Losers				
Infosys Tech	2,743	(1.9)	(9.0)	1.8
ICICI Bank	891	(0.9)	(3.2)	2.6
M&M	617	(2.4)	(2.3)	1.7

Source: Bloomberg

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