INDIA DAILY

March 14, 2008

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News Roundup

Corporate

- Telecom regulator Trai has come down heavily on Vodafone Essar, directing it to refund within 15 days the value-added service charges that it levied for services provided without its customer's explicit consent. (ET)
- GE Water & Processing Technologies said it has formed a JV with Eureka Forbes—Infinite Water Solutions—to manufacture and sell water purifiers in the domestic market. (ET)

Economic and political

- As the dollar slipped below Y100 for the first time since 1995, hundreds of corportaes and institutions were exposed to a brutal currency market. (ET)
- The government is all set to bring in a law to regulate the booming real estate sector in Delhi, that could be a model for the rest of the country. (BS)
- Weighed down by higher taxes in the past three years, cigarette production has declined for the first time in 2007-08 (by 1.74%). (BS)

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, BL = Business Line.

EQUITY MARKETS

		Change, %		
India	**13-Mar**	**1-day**	**1-mo**	**3-mo**
Sensex	15,357	(4.8)	(13.6)	(23.3)
Nifty	4,624	(5.1)	(11.1)	(23.5)
Global/Regional indices				
Dow Jones	12,146	0.3	(1.9)	(9.0)
Nasdaq Composite	2,264	0.9	(3.0)	(14.1)
FTSE	5,692	(1.5)	(3.2)	(11.0)
Nikkie	12,519	0.7	(8.1)	(19.3)
Hang Seng	22,302	(4.8)	(7.2)	(19.1)
KOSPI	1,627	0.7	(4.2)	(14.2)

Value traded - India

		Moving avg, Rs bn		
	13-Mar		**1-mo**	**3-mo**
Cash (NSE+BSE)	195.9		189.4	189.5
Derivatives (NSE)	448.7		375.6	702
Deri. open interest	667.4		679	1,122

Forex/money market

		Change, basis points		
	13-Mar	**1-day**	**1-mo**	**3-mo**
Rs/US$	40.5	0	86	112
6mo fwd prem, %	0.7	(25)	71	24
10yr govt bond, %	7.6	1	12	(28)

Net investment (US$mn)

	12-Mar		**MTD**	**CYTD**
FIIs	36		317	(4,271)
MFs	(122)		(410)	1,954

Top movers -3mo basis

		Change, %		
Best performers	**13-Mar**	**1-day**	**1-mo**	**3-mo**
Asian Paints	1,138	(1.3)	(1.4)	13.7
Ranbaxy	457	(1.5)	20.3	8.3
Sun Pharma	1,226	(3.3)	10.5	7.8
Thomas Cook	96	(1.0)	43.9	4.9
NALCO	468	(5.3)	33.9	4.1
Worst performers				
Arvind Mills	39	(5.8)	(19.1)	(53.4)
Tvs Motor	38	(5.0)	(4.2)	(51.1)
Tata Tele	30	(7.1)	(16.8)	(50.6)
Neyveli Lignite	126	(6.7)	(17.6)	(49.5)
Moser Baer	148	(7.8)	(14.7)	(49.3)

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Media

HTML.BO, Rs166	
Rating	BUY
Sector coverage view	Cautious
Target Price (Rs)	225
52W High -Low (Rs)	266 - 152
Market Cap (Rs bn)	38.8

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	10.4	12.1	14.7
Net Profit (Rs bn)	1.0	1.4	1.8
EPS (Rs)	4.1	5.8	7.6
EPS gth	*53.6*	*41.4*	*29.5*
P/E (x)	40.1	28.4	21.9
EV/EBITDA (x)	21.9	15.9	11.9
Div yield (%)	0.2	0.6	1.2

Shareholding, December 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	68.7	-	-
FIIs	19.0	0.1	0.1
MFs	7.7	0.3	0.3
UTI	-	-	-
LIC	-	-	-

HT Media: Patience will pay over time

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- **New initiatives in print, radio and alternate media will likely create value over time**
- **Near-term financials depressed; growth to accelerate as new businesses turn around**
- **Strong global newsprint prices negative for all newsprint publishers**
- **Upgrade to BUY with reduced 12-month DCF-based TP of Rs225 (Rs260 previously)**

We are upgrading HT Media (HTML) to BUY from ADD with a reduced 12-month DCF-based target price of Rs225 (Rs260 previously); the lower target price largely reflects higher newsprint prices. HTML's near-term financials are considerably depressed due to its many new media initiatives; however, value creation in these businesses will increasingly become visible over the next few years as they start contributing meaningfully to earnings. The key negative for HTML during its expansion phase would be higher global newsprint prices, which are being driven by consolidation and capacity rationalization in the North American market. We have reduced our FY2009E and FY2010E EPS to Rs7.6 (Rs9.8 previously) and Rs10.4 (Rs13.2), respectively, to reflect higher newsprint prices, expansion in the Hindi belt and higher rupee-dollar rate which is partially offset by higher expected ad revenues from Hindustan, the Hindi language daily.

Multiple growth drivers but financials will be depressed in the near term. We note that HTML has expanded its portfolio of media brands in the past few years to include a business newspaper, radio, events and internet properties; it has also expanded geographically, launching its flagship HT edition in Mumbai and Hindi daily Hindustan in the UP market. We note that all the new media initiatives launched by HTML during the past three years are not contributing to earnings; this is especially true for print media as any new launch takes between three and five years to break even but starts generating significant free cash flows once the newspaper is well established. We note that HTML's flagship HT Delhi edition generates substantial free cash flows; we estimate HT Delhi's EBITDA contribution for FY2008E and FY2009E at Rs2.7 bn and Rs3.0 bn, respectively, versus HTML's consolidated EBITDA of Rs2.3 bn and Rs3.0 bn, respectively. However, we expect the value creation potential of HTML's new media initiatives to become more visible over time as they turn around and start contributing significantly to earnings.

1. **HT Mumbai.** We estimate HT Mumbai's EBITDA loss for FY2008E at Rs700 mn and expect it to achieve EBITDA breakeven by end-FY2011E. HT Mumbai continues to scale up well and its monthly ad revenue run-rate has reached Rs100-120 mn. We note that Mumbai is the most lucrative print market in India with ad revenue potential of Rs10.0-11.0 bn currently; we expect HT Mumbai's revenues in FY2009E and FY2010E at Rs1.6 bn and Rs1.8 bn, respectively.
2. **Mint business newspaper.** We estimate Mint's EBITDA loss for FY2008E at Rs400 mn and expect it to achieve EBITDA breakeven by FY2010E; its monthly ad revenue run-rate has reached Rs30 mn. We expect FY2009E and FY2010E revenues from Mint at Rs500 mn and Rs650 mn; our estimates may be conservative if Mint establishes itself as a strong number two in the business news market in India with ad revenue potential of Rs6.5-7.0 bn by FY2010E.
3. **Hindi daily Hindustan.** We expect Hindustan's contribution to HTML's earnings to increase meaningfully driven by expansion into new markets and reduction in the ad rate gap between English and regional press; HTML is expanding the brand in the large UP and lucrative Delhi markets. Hindustan is already the leader in the state of Bihar and Jharkhand (see Exhibit 1) but the ad revenue potential is small given the readership profile in these markets.

4. **Radio Fever.** We expect the radio business to report FY2009E and FY2010E EBITDA of Rs178 mn and Rs242 mn, respectively. HTML has four operational radio stations in Delhi, Mumbai, Bangalore and Kolkata, all of which were launched in the past two years; it is planning to bid for more cities in the next round of bidding.

Rising global newsprint prices—negative. We have previously noted the strong likelihood of increase in newsprint price in the North American market (see our note *"Newsprint price update—strong likelihood of price increases starting 1QCY08"* on December 14, 2008). The North American market was suffering from a large demand-supply gap in CY2007 which kept prices under check. However, the supply surplus vanished with Abitibi and Bowater merging to create AbitibiBowater, the largest North American newsprint producer accounting for about 50% market share. AbitibiBowater immediately announced the closure of 600,000 tons/year of capacity as part of its post-merger rationalization plan and a US$60/ton price hike effective 1QCY08. The wave of consolidation and capacity rationalization in the North American newsprint market has continued; Catalyst Paper has acquired AbitibiBowater's 375,000 tons/year Snowflake mill with the result that the top five newsprint producers now account for over 80% of newsprint capacity in the North American market (see Exhibit 2).

All large North American newsprint producers have recently announced another US$60/ton price hike effective 2QCY08 even as the market was adjusting to the 1QCY08 increase. Newsprint prices continued their upward trend in February with the 30-lb benchmark US East Coast price rising another US$20/ton to US$620/ton (see Exhibit 3). If the recently-announced price hike is fully implemented through to the newspaper publishers, it would imply a newsprint price of US$700/ton by end-2QCY08. However, the demand for newsprint in the North American market also continues to decline (11% decline in CY2007 versus CY2006), led by declining circulation and sluggish ad revenue growth, which would necessitate further capacity rationalizations; we expect prices to rise from present levels but the point at which they will likely stabilize will only be determined by market forces. However, we also note the many mitigating actions (1) cover price increase, (2) reduction in page levels and (3) change in newsprint mix, which are available to newspaper publishers in case newsprint prices increase further.

Earnings revisions. Exhibit 4 shows our revised earnings estimates, which factor in strong global newsprint prices, greater circulation of Hindustan and higher rupee-dollar exchange rate partially offset by higher-than-expected ad revenues. The key changes to our model are as follows.

1. **Higher newsprint prices.** We have revised our landed newsprint price for FY2008E, FY2009E and FY2010E to US$615/ton (US$610/ton previously), US$680/ton (US$620/ton) and US$680/ton (US$620/ton), respectively. Thereafter, we model a newsprint price of US$650/ton in perpetuity versus US$620/ton, previously.
2. **Higher circulation of Hindustan.** HTML plans to launch Hindustan in about 10-12 cities of UP and Uttaranchal in FY2009E and FY2010E. We have increased our expected daily circulation of Hindustan for FY2009E and FY2010E to 1.7 mn copies (1.4 mn copies previously) and 1.9 mn copies (1.4 mn copies), respectively.
3. **Weaker Rupee.** We model rupee-dollar exchange rate for FY2009E and FY2010E at Rs39.5/US$ (Rs38.5/US$ previously) and Rs38.5/US$ (Rs37.5/US$), respectively. We model exchange rate at Rs38/US$ in perpetuity versus Rs37/US$ previously.
4. **Capex on Hindustan and HT Mumbai.** We have factored in increased capital expenditure for FY2009E and FY2010E at Rs1.3 bn and Rs0.8 bn, respectively, to factor in the expansion into the UP market and the new printing facility for the HT Mumbai edition.
5. **Higher ad revenues from Hindustan.** We have increased our expected ad revenue from Hindustan for FY2009E and FY2010E to Rs2.0 bn (Rs1.8 bn previously) and Rs2.4bn (Rs2.1 bn), respectively.
6. **Modest changes to other ad revenues.** We have made minor changes to our expected ad revenues from HT Delhi, Mint and Radio business.

Dainik Jagran is the leader in the Hindi market but Dainik Bhaskar has a better spread

Readership data of Hindi dailies in key Hindi-speaking states ('000)

	Aj	Amar Ujala	Dainik Bhaskar	Dainik Jagran	Hari Bhoomi	Hindustan	Lokmat Samachar	Navbharat	Navbharat Times	Prabhat Khabar	Punjab Kesari	Rajasthan Patrika	Total
Bihar	501	—	—	2,595	—	**4,547**	—	—	—	323	—	—	**7,966**
Chandigarh	—	59	**216**	—	—	—	—	—	—	—	31	—	**306**
Chhattisgarh	—	—	**1,095**	—	723	—	—	790	—	—	—	—	**1,885**
Haryana	—	296	**1,669**	898	80	18	—	—	—	—	867	—	**3,748**
Himachal Pradesh	—	**435**	36	72	—	—	—	—	—	—	418	—	**961**
Jammu & Kashmir	—	**114**	—	37	—	—	—	—	—	—	65	—	**216**
Jharkhand	70	—	—	801	—	**1,086**	—	—	—	1,014	—	—	**2,971**
Madhya Pradesh	—	—	**3,314**	332	—	—	—	739	—	—	—	—	**4,385**
Maharashtra	—	—	511	—	—	—	**680**	678	542	—	—	—	**2,411**
National Capital Region	2	274	113	973	—	892	—	—	**1,768**	—	1,009	—	**5,031**
Punjab	—	219	265	1,096	—	—	—	—	—	—	**1,132**	—	**2,712**
Rajasthan	—	—	5,745	—	—	—	—	—	—	—	140	**7,353**	**13,238**
Uttar Pradesh	1,024	6,080	186	**9,419**	—	2,037	—	—	—	—	62	—	**18,808**
Uttaranchal	—	**872**	—	547	—	—	—	—	—	—	25	—	**1,444**
Total	**1,597**	**8,349**	**13,150**	**16,770**	**803**	**8,580**	**680**	**2,207**	**2,310**	**1,337**	**3,749**	**7,353**	**66,082**

Note:
(a) Fieldwork period: July 2006 to June 2007.

Source: Indian Readership Survey 2007 Round 2, compiled by Kotak Institutional Equities.

North American newsprint capacity is now concentrated in the hands of few producers

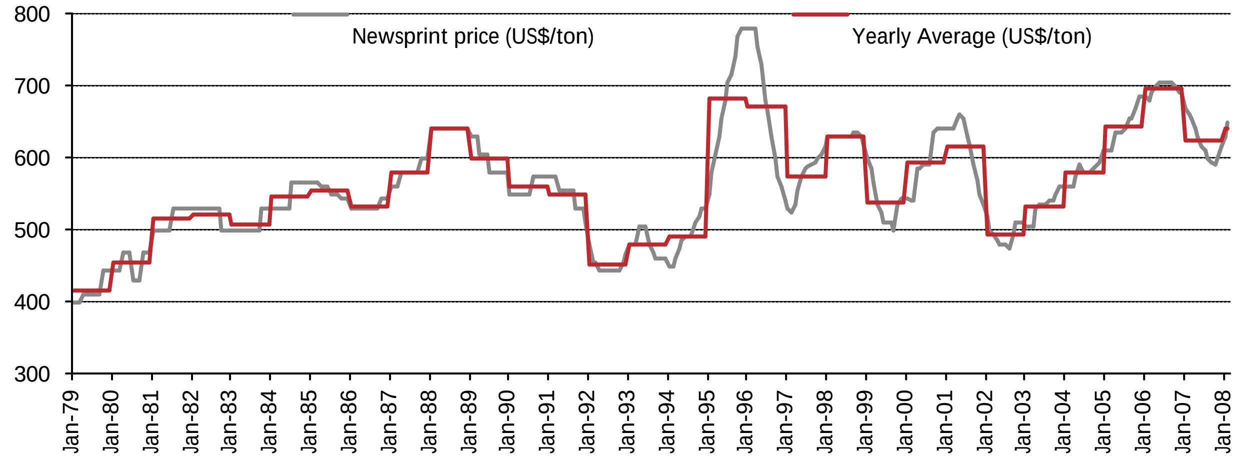
Newsprint capacity of key North American newsprint manufactures ('000 tons)

Company	Newsprint capacity
AbitibiBowater	4,980
White Birch	1,150
Kruger	1,115
Catalyst Paper	990
SP Newsprint	960
NORPAC	650
Tembec	400
Stora Enso	95
Total capacity	**10,340**

Source: Canadian Paper Analyst, Pulp and Paper Weekly, compiled by Kotak Institutional Equities.

Newsprint prices have risen sharply led by industry consolidation and capacity rationalization in North America

Historical newsprint price, US East Coast, 1979-2008 (US$/ton)



Source: PPPC, Pulp and Paper Weekly, compiled by Kotak Institutional Equities.

Reducing our earning estimates for HT Media largely on the back of strong newsprint prices

Revised and previous earnings estimates for HT Media, March fiscal year-ends, 2008-2010E (Rs mn)

	Revised			Previous			Change (%)		
	2008E	2009E	2010E	2008E	2009E	2010E	2008E	2009E	2010E
Advertisement revenues	10,484	12,598	14,433	10,544	12,570	14,264	(0.6)	0.2	1.2
Circulation revenues	1,449	1,925	2,330	1,440	1,729	1,986	0.6	11.3	17.3
Total sales	**12,150**	**14,742**	**17,011**	**12,200**	**14,518**	**16,496**	**(0.4)**	**1.5**	**3.1**
Production cost	5,629	6,904	7,551	5,469	5,989	6,394	2.9	15.3	18.1
Employee cost	1,947	2,232	2,526	1,959	2,249	2,522	(0.6)	(0.8)	0.1
SG&A expenses	2,289	2,568	2,847	2,328	2,548	2,796	(1.7)	0.8	1.8
Total expenditure	**9,865**	**11,704**	**12,924**	**9,757**	**10,786**	**11,712**	**1.1**	**8.5**	**10.3**
EBITDA	**2,285**	**3,039**	**4,088**	**2,443**	**3,733**	**4,784**	**(6)**	**(19)**	**(15)**
EPS (Rs)	**5.8**	**7.6**	**10.4**	**6.2**	**9.8**	**13.2**	**(6)**	**(23)**	**(21)**

Source: Kotak Institutional Equities estimates.

Our DCF-based target price for HTML is Rs225

Discounted cash flow analysis of HT Media (Rs mn)

	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
EBITDA	**2,285**	**3,039**	**4,088**	**5,383**	**6,257**	**6,945**	**7,676**	**8,482**	**9,352**	**10,245**	**10,331**	**10,951**	**11,608**
Tax expense	(673)	(1,007)	(1,376)	(1,824)	(2,146)	(2,410)	(2,685)	(2,984)	(3,306)	(3,641)			
Changes in working capital	(634)	(374)	(329)	(312)	(273)	(257)	(278)	(304)	(329)	(352)			
Cash flow from operations	**977**	**1,658**	**2,383**	**3,247**	**3,838**	**4,277**	**4,713**	**5,194**	**5,717**	**6,251**			
Capital expenditure	(460)	(1,270)	(770)	(520)	(270)	(270)	(520)	(520)	(520)	(520)			
Cash flows for minority interest	16	(14)	(25)	(34)	(51)	(55)	(60)	(65)	(70)	(69)			
Free cash flow to the firm	**533**	**373**	**1,588**	**2,692**	**3,517**	**3,952**	**4,133**	**4,610**	**5,128**	**5,662**	**5,473**	**5,801**	**6,150**
Dicounted cash flow-now	528	329	1,243	1,873	2,174	2,171	2,018	2,001	1,978	1,941			
Discounted cash flow-1 year forward		370	1,398	2,107	2,447	2,443	2,271	2,251	2,226	2,184	1,877		
Discounted cash flow-2 year forward			1,573	2,370	2,752	2,749	2,554	2,533	2,504	2,458	2,111	1,989	

Discount rate (%)	12.5												
Growth from 2017 to perpetuity (%)	6.0												

	+ 1-year		+ 2-years	
Total PV of free cash flow (a)	**19,572**	**39%**	**23,594**	**42%**
FCF in terminal year	5,801		6,150	
Exit FCF multiple (X)	15.4		15.4	
Terminal value	89,253		94,608	
PV of terminal value (b)	**30,603**	**61%**	**32,439**	**58%**
EV (a) + (b)	**50,175**		**56,033**	
EV (US$ mn)	**1,091**		**1,218**	
Net debt	(2,441)		(2,554)	
Equity value	**52,617**		**58,587**	
Implied share price (Rs)	**225**		**250**	
Exit EV/EBITDA multiple (X)	8.6		8.6	

Sensitivty of share price to different levels of WACC and growth rate (Rs)

	WACC (%)						
Growth rate (%)	**11.0**	**11.5**	**12.0**	**12.5**	**13.0**	**13.5**	**14.0**
1.0	187	177	168	161	153	147	141
1.0	187	177	168	161	153	147	141
2.0	198	187	177	169	161	153	146
3.0	213	200	188	178	169	161	153
4.0	232	216	202	190	179	170	161
5.0	257	237	220	205	192	181	171
6.0	292	265	243	**225**	209	195	183
7.0	344	307	276	251	231	213	198
8.0	432	371	326	290	262	238	219

Source: Kotak Institutional Equities estimates.

Profit model, balance sheet, cash model of HT Media 2005-2012E, March fiscal year-ends (Rs mn)

	2005	2006	2007	2008E	2009E	2010E	2011E	2012E
Profit model								
Net sales	6,247	8,210	10,397	12,150	14,742	17,011	19,157	21,061
EBITDA	**753**	**1,184**	**1,680**	**2,285**	**3,039**	**4,088**	**5,383**	**6,257**
Other income	91	177	367	346	369	352	340	378
Interest	(72)	(135)	(143)	(171)	(140)	(70)	—	—
Depreciation	(227)	(385)	(436)	(514)	(561)	(629)	(488)	(512)
Pretax profits	**546**	**841**	**1,468**	**1,946**	**2,707**	**3,740**	**5,235**	**6,123**
Extraordinary items	(106)	(229)	2	—	—	—	—	—
Tax	(22)	(65)	(573)	(607)	(963)	(1,351)	(1,824)	(2,146)
Deferred taxation	(142)	(174)	27	13	43	80	45	65
Net income	**274**	**373**	**924**	**1,352**	**1,787**	**2,469**	**3,456**	**4,042**
Minority interest	—	—	(46)	(16)	14	25	34	51
Adjusted net income	**349**	**537**	**969**	**1,368**	**1,772**	**2,444**	**3,421**	**3,991**
Earnings per share (Rs)	**1.8**	**2.4**	**4.1**	**5.8**	**7.6**	**10.4**	**14.6**	**17.0**
Balance sheet								
Total equity	4,114	6,932	7,642	8,736	9,961	11,582	12,202	12,924
Minority interest	—	—	—	(16)	(1)	23	58	108
Deferred taxation liability	132	296	273	259	216	137	92	27
Total borrowings	1,716	1,696	1,658	1,650	1,650	—	—	—
Current liabilities	1,406	1,809	2,113	2,104	2,433	2,600	2,687	2,823
Total liabilities and equity	**7,367**	**10,733**	**11,685**	**12,734**	**14,258**	**14,342**	**15,039**	**15,882**
Cash	489	2,678	1,104	1,581	1,694	1,141	1,406	2,083
Other current assets	1,889	3,276	2,863	3,489	4,192	4,688	5,087	5,496
Total fixed assets	3,823	3,736	4,109	4,130	4,914	5,130	5,237	5,070
Intangible assets	158	182	1,098	1,023	948	873	797	722
Investments	1,009	861	2,510	2,510	2,510	2,510	2,510	2,510
Total assets	**7,367**	**10,733**	**11,685**	**12,734**	**14,258**	**14,342**	**15,039**	**15,882**
Free cash flow								
Operating cash flow, excl. working capital	540	757	1,194	1,508	1,936	2,666	3,559	4,111
Working capital changes	78	(232)	(226)	(634)	(374)	(329)	(312)	(273)
Capital expenditure	(1,085)	(327)	(867)	(460)	(1,270)	(770)	(520)	(270)
Investments	(566)	388	(319)	—	—	—	—	—
Other income	27	130	197	346	369	352	340	378
Free cash flow	**(1,006)**	**716**	**(21)**	**759**	**660**	**1,919**	**3,067**	**3,946**
Ratios (%)								
Debt/equity	40.4	23.5	20.9	18.3	16.2	—	—	—
Net debt/equity	28.9	(13.6)	7.0	0.8	(0.4)	(9.7)	(11.4)	(16.1)
ROAE (%)	9.8	9.4	12.8	16.2	18.5	22.3	28.5	31.6
ROACE (%)	**11.1**	**12.1**	**10.6**	**14.4**	**16.3**	**20.7**	**28.4**	**31.5**

Source: Kotak Institutional Equities estimates.

Metals

TISC.BO, Rs697	
Rating	REDUCE
Sector coverage view	Neutral
Target Price (Rs)	800
52W High -Low (Rs)	970 - 372
Market Cap (Rs bn)	599.5

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	175.5	199.2	241.5
Net Profit (Rs bn)	43.7	46.1	63.6
EPS (Rs)	50.9	53.6	73.9
EPS gth	*(20.9)*	*5.4*	*37.9*
P/E (x)	13.7	13.0	9.4
EV/EBITDA (x)	8.4	7.4	5.9
Div yield (%)	1.6	1.7	1.7

Shareholding, December 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	33.7	-	-
FIIs	20.5	1.1	(0.0)
MFs	4.2	1.3	0.2
UTI	-	-	(1.1)
LIC	9.8	2.8	1.7

Tata Steel: 3Q conference call highlights; Retain REDUCE

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- **In its 3Q conference call, the management has highlighted reasons for Corus' lower qoq EBITDA—anomalies exist between the proferred rationale and our calculations based on the implied results**
- **Management clarifies several variables relating to profitability forecasts—we discuss our assumptions on those issues and their variance from management guidance**
- **We continue to believe that higher costs will not be completely passed on to finished steel consumers and Tata's consolidated margins will reduce**
- **Retain our REDUCE rating on the stock despite 15% upside to our target price**

In its 3Q conference call to discuss consolidated results, Tata Steel's management highlighted reasons for Corus' lower qoq operating performance, which we are unable to reconcile with our findings based on the interpretation of implied results. In this note, we discuss several aspects of profitablity that the management has commented on—we show how our model differs and reasons thereof. We continue to maintain that increases in steel prices globally will not be high enough to accommodate increased costs. We retain our REDUCE rating on the stock despite the current market price being lower than our target price.

We list our understanding of management communication on major issues relating to profitability and balance sheet items in Exhibit 1. We are unable to reconcile the management's rationale for a cost increase of US$1 bn in FY2008, in a scenario where iron ore costs increased by just 9.6% and coking coal costs reduced 20%. In our opinion, our estimates of cost increases in FY2009 might be conservative (under scenario where iron ore rises 65% and coking coal by 100%) if the cost increases seen in FY2008 are of a recurring nature. See Exhibit 1 for more details.

We also express our inability to model the performance improvement program that will likely save costs by £300 mn each year. We reproduce a similar table (in Exhibit 2) that we had put forth in our analysis of Tata Steel standalone 3QFY08 results. We are calling for several clarifications into the source of the performance improvement program that will better equip us to model such improvements. If the merged entity delivers the improvement, under the current set of assumptions, we will have to raise our FY2009 EBITDA estimates to factor that change.

We continue to maintain that higher steel prices will not be able to accomodate the increase in costs. We expect steel making costs to increase in FY2009E following (a) 65-71% increase in iron ore prices already settled, (b) probable increase of 100% in coking coal prices (spot prices at US$350/ton versus US$98 contracted last year) and (c) probable increase in freight rates.

Our projections for lower operating margins for Corus Group (and therefore the consolidated entity) prevent us from raising our rating on Tata Steel despite 15% upside to our target price. We retain REDUCE rating on the stock.

Exhibit 1: We list our views on major issues discussed in 3QFY08 mangement conference call on consolidated results

Details of our understanding of management communication versus our model assumptions

Issues	Management communication	Our model assumptions
Relating to current quarter results		
Lower implied operating margins of Corus	Lower volumes in UK following winter season	Analysis of implied EBITDA (see Exhibit 3) arrives at a varying inference
	Coke purchases on spot basis increased costs	
	Higher winter tariffs increased power costs	
Relating to Income statement		
Interest costs	High-cost bridge loans largely repaid	We assume interest costs as US$900 mn for FY2009; some upside to our numbers here
	One-time financing costs impacted FY08 results	
	US$750-800 mn is continuing financing costs for FY2009	
Pension costs	Change in actuarial assumptions does not impact IFRS statements	Provisions on account of mortality rate changes will have to be made on Income statement; though it is cash neutral
	Change in mortality rates will impact liability	We have not yet built in these numbers
	Clarity will emerge over the next two quarters	
Tax rates	Cash tax rates will reduce following (a) capital spending in Indian ops and (b) benefits from accumulated losses in Dutch sub	
	Effective tax rate will stay close to maximum rate; at over 30% for FY2009	Our model assumes ETR of over 33%
Costs increase in FY2008 and 09	Costs increase US$1 bn in FY2008	Our model assumes stable costs for FY2008; with iron ore prices increasing 9.6% and coal prices decreasing 20%, unable to explain the difference
		If ongoing costs increase by US$1 bn, our assumptions for cost increase next year sounds conservative based on 65% iron ore price increase and 100% coal price increase
Performance improvements of GBP300 mn	Corus has delivered continuing cost improvements (not related to merger) amounting to £300 mn in FY2008 and will deliver similarly in FY2009	We admit our inability to effectively model these benefits since we are unaware of the sources for such improvements
		If such benefits are delivered in FY2009, our EPS will have to be revised upwards to reflect that
Relating to Balance sheet		
Consolidated net debt	Net debt as of Dec-07 stands at US$11 bn	Our estimate for Mar-08 stands at US$10.8 bn
	Incremental debt will be taken for new projects	Our model assumes net debt to decline over the next couple of years
New foreign equity offering	Foreign offering of US$0.8 bn might have to be made as planned earlier	We have not built the foreign offering into our fully diluted shares, which will likely increase as (see Exhibit 6)
	Tata Steel management will wait for market stability to issue equity as financing is otherwise arranged from internal resources	Infusion of equity will lower our net debt assumption, hence EV will remain unchanged if offering is priced closer to our target price

Source: Company data, Kotak Institutional Equities

Exhibit 2: Clarity required on 'performance improvements' guidance in 2008; similar calculation for CY2007 yields puzzling results

KIE calculations of performance improvements, December fiscal year-ends (£ mn)

		Remarks
CY2006 EBITDA	**766**	Pre-aluminium business losses
CY2007E EBITDA	**1,158**	
1QCY07 reported	254	Reported numbers; transaction costs added back
2QCY07 implied	387	Implied from consolidated Tata Steel results
3QCY07 implied	217	Implied from consolidated Tata Steel results
4QCY07 estimated	300	
Incremental EBITDA	**392**	CY2007 over CY2006
On performance improvement account	**300**	Encompasses growth in volumes and cost changes (other than raw material costs)
1. Volume growth	**61**	
CY2007 volumes growth (mn tons)	1.0	Assumed by KIE
CY2007 EBITDA/ton (£/ton)	61	
2. Other factors	**239**	What (besides volumes growth) gets reported as performance improvement is not known; management guided for performance improvement to the tune of £300 mn in CY2007
On pricing/cost account		Encompasses change in pricing less change in costs (largely raw material costs)
1. Pricing related growth on old volumes	**844**	
CY2006 volumes (mn tons)	21	
Assumed change in realization (£/ton)	40	Assumed to be in line with change in prices
2. Pricing related growth on incremental volumes	**434**	
CY2006 volumes (mn tons)	1	
Realiztion less EBITDA (£/ton)	434	
3. Assumed change in costs	**1,186**	**Balancing figure**
CY2006 total costs (£ mn)	8,755	
Average increase in costs (%)	13.5	Looks extremely high considering that iron up went up just 10% and coal prices were lower by 20%
Average annual increase in costs (CY2004-06) (£ mn)	650	Over this period, iron ore and coking coal has increased by 30% on average

Exhibit 3: Drop in Corus Group's revenues lead to sequential drop in consol. EBITDA

Calculation of implied EBITDA of Corus Group, March fiscal year-ends (Rs mn)

	1QFY08	2QFY08	3QFY08
Implied Corus Group EBITDA			
Consolidated EBITDA	49,043	47,277	39,428
Tata Steel standalone EBITDA	16,992	20,254	20,966
Assumed other subsidaries EBITDA	1,112	1,112	1,112
Implied Corus Group EBITDA	**30,939**	**25,910**	**17,349**
Sequential change in EBITDA		(5,029)	(8,561)
Sequential change in EBITDA (%)		**(16.3)**	**(33.0)**
Implied Corus Group revenues			
Consolidated revenues	311,546	324,249	318,985
Tata Steel standalone revenues	41,976	47,851	49,739
Assumed other subsidaries revenues	26,000	26,000	26,000
Implied Corus Group revenues	**243,570**	**250,398**	**243,246**
Sequential change in revenues		6,829	(7,152)
Sequential change in revenues (%)		**2.8**	**(2.9)**
Implied Corus Group revenues			
Implied Corus Group costs	**212,630**	**224,488**	**225,897**
Sequential change in revenues		11,858	1,409
Sequential change in revenues (%)		**5.6**	**0.6**

Source: Company data, Kotak Institutional Equities

Exhibit 4: We maintain that Consolidated net earnings will likley reduce in FY2009E

Summary consolidated statement of Tata Steel, March fiscal year-ends (Rs mn)

	2008E	2009E	2010E
Summary income statement			
Net revenues	1,289,715	1,422,639	1,519,797
EBITDA	178,500	161,299	167,374
Pre-tax profits	101,041	86,800	93,905
Continuing recurring net earnings	62,041	54,208	58,002
Continuing recurring EPS (Rs)	72.1	63.0	67.4
Summary balance sheet statement			
Liabilities	**779,811**	**870,101**	**904,183**
Share capital	8,600	8,600	8,600
Reserves	309,846	426,541	469,571
Net borrowings	461,364	434,959	426,012
Assets	**779,811**	**870,101**	**904,183**
Net fixed assets	597,303	662,607	751,990
Investments	75,638	75,638	50,000
Net working capital	106,870	131,855	102,193

Source: Kotak Institutional Equities

Exhibit 5: Tata Steel, SOTP valuation, March fiscal year-ends, 2009E basis (Rs mn)

	EBITDA		Multiple	Enterprise value		EV	Vauation basis
	(Rs mn)	(£ mn)	(X)	(Rs mn)	(USD mn)	(Rs/share) (a)	
Tata Steel standalone	106,183	-	7.0	722,041	18,051	840	Valued on FY2009E EBITDA
Corus Group standalone (b)	52,640	658	6.5	342,160	8,554	398	Valued on CY2008E EBITDA
Present value of synergies				41,326	1,033	48	Probability adjusted
Total Enterprise Value				**1,105,527**	**27,638**	**1,286**	
Tata Steel standalone net debt				43,495	-		FY2009E, adjusted for cash and marketable securities
Corus Group standalone net debt				52,820	-		December 2008E, adjusted for cash and marketable securities
Borrowings in Tata Steel Asia Holdings' account				44,000	-		
Borrowings in Tulip UK's account				24,000	-		
Senior debt at Tata Steel UK's account (d)				160,000	-		
Mezannine debt at Tata Steel UK's account (d)				124,000	-		
Total borrowings				**448,316**	**11,208**	**521**	
Arrived market capitalization				**657,211**	**16,430**	**764**	
Value of investments				**36,114**	**903**	**42**	
Market capitalization (including Investments)						**806**	
Target price (Rs)						**800**	Maintain target price

Notes:

(a) Based on fully diluted number of shares.

(b) Based on 2007 December-ended forecasted EBITDA.

(c) Currency conversion from GBP and USD into INR is based on current exchange rates.

(d) Refinanced by US$6.2 bn by way of non-recourse debt, of which US$3.3 bn is five year amortizing loan and balance is 7 year amortizing loan.

Source: Company, Kotak Institutional Equities estimates.

Exhibit 6: Tata Steel, fully-diluted shares, March fiscal-year end (Rs mn)

Shares as of Mar-07 (mn)	**553.0**

Confirmed issuance (mn shares)	**312.8**	**Comment**
Preferential allotment to Tata Sons	27.0	
Warrants issued to Tata Sons	28.5	Yet to be fully converted into equity
Rights issuance	121.8	Offerred at Rs300/share; yet to be issued
CARS (a)	44.1	Convertible at Rs877/share
CCPS (b)	91.4	Convertible at Rs600/share

			If issued at (Rs/share)		
Issuances where pricing yet to be decided	Amount (US$ mn)	**Comment**	**600**	**800**	**1,000**
Foreign issue in Tata Steel's books	800	Company declines to comment on exact	57.3	43.0	34.4
Probable issue of shares (mn)		timing/details of the probable issue	**57.3**	**43.0**	**34.4**
Range of fully-diluted number of shares (mn)			**923.1**	**908.8**	**900.2**
Dilution based on Mar-07 number of shares (%)			66.9	64.3	62.8

Notes:

(a) CARS stands for Cumulative Alternative Reference Securities

(b) CCPS is Cumulative Convertible Preference Shares

Consumer Products

HLL.BO, Rs222	
Rating	ADD
Sector coverage view	Attractive
Target Price (Rs)	230
52W High -Low (Rs)	244 - 170
Market Cap (Rs bn)	484.2

Financials

December y/e	2006	2007E	2008E
Sales (Rs bn)	121.0	137.2	154.7
Net Profit (Rs bn)	15.5	17.7	20.0
EPS (Rs)	7.0	8.1	9.2
EPS gth	*18.3*	*15.3*	*13.3*
P/E (x)	31.6	27.4	24.2
EV/EBITDA (x)	24.6	22.0	18.7
Div yield (%)	3.1	4.8	3.9

Shareholding, December 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	52.1	-	-
FIIs	14.3	0.6	(0.3)
MFs	2.5	0.6	(0.3)
UTI	-	-	(0.9)
LIC	7.5	1.7	0.8

Hindustan Unilever: Annual price hike

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- **First leg of annual price hike—HUL soaps prices up 9%, detergents 4%**
- **Godrej Consumer likely to follow HUL**
- **Likely organization restructuring is a welcome move**
- **Near-term business performance secured, short-term stock outperformance likely to continue**

During the first two months of CY2008, HUL has taken aggressive price hikes in soaps portfolio (we estimate about 9%) and modest hikes in detergents (about 4%) and skin (about 3%). We believe that the price increases in soaps is primarily cost-led, while the pricing action in detergents and personal care signifies the changed competitive scenario. We believe HUL will at best grow in line with industry and deliver 15% earnings CAGR over 2007-2009E. Near-term performance would have a favorable base effect as well as benefit from the extended winter this year. We believe the stock will likely trade at our DCF-based target price of Rs230 in the near term and has positive news flow as tailwind. The stock has delivered a relative performance (versus the Sensex) of 22% and 23% over the past one month and three months, respectively. At the current market price of Rs222, the stock trades at 25XCY08 and 21XCY09. We retain our ADD rating and target price of Rs230/share.

First tranche of annual price hikes

HUL has effected significant price hikes in its core HPC portfolio during the first two months of CY2008. The company typically opts for price increases in its soaps and detergents portfolio in the beginning of its financial year (in January/February) and for its personal care portfolio in July/August. Aggressive price hikes in the soaps portfolio (we estimate blended increase of about 9%) were followed by modest hikes in detergents (about 4%) and skin (about 3%). We believe that the price increases in soaps are primarily cost-led (palm oil prices have increased over 100% yoy), while the pricing action in detergents and personal care signifies the changed competitive scenario and brand salience. However, we note that the company has left-out the 'price sensitive' segments/ SKUs from price increases—Breeze soap portfolio, Lifebuoy 55g pack, Fair & Lovely 9gm pack, shampoo sachets etc. Please refer Exhibit 1 & 2 for the list of price hikes.

Godrej Consumer likely to follow HUL

HUL being the market leader with 55% value market share, leads the way in setting prices. HUL has increased the prices on its soap portfolio excluding the price sensitive 'Breeze' which is in the low-end popular segment. Godrej Consumer's brand 'Godrej No.1' is directly pitted against HUL's 'Breeze'. Godrej Consumer (GCPL) typically follows HUL's pricing action for its 'Godrej No.1' brand. GCPL has not yet taken any price increase in CY2008 in its soap portfolio. We believe GCPL is likely to increase the retail prices of its soap brands to maintain margins in times of hardening palm oil prices.

Favorable tidings in detergents

We highlight that the detergent category is in a sweet spot for growth now with gross margins returning to the 20-25% bracket. The bitter price battle between HUL and P&G from 2004, coupled with a tough input-cost scenario (caustic soda, soda ash, linear alkyl benzene) had brought down profitability for this category to ~15% at the gross margin level. In the past three years, HUL and P&G have gained a combined market share of over 5% mostly from regional players. We believe that with P&G gaining substantially in urban areas and in distribution depth in rural, tidings are favorable in this category for sustained albeit slow margin improvement. However, the recent uptrend in LAB prices may limit the margin improvement in the near term.

Organization restructuring mildly positive

We view the recent appointments of Mr Nitin Paranjpe (MD & CEO) and Dr R.A. Mashelkar (Independent Director) as very positive steps. We believe these appointments will bring much-needed agility to HUL in developing new categories and in staving off the competition. In line with taking the 'One Unilever' strategy (announced in 2005) a step forward, Unilever announced the merger of the two business divisions HPC and Foods into one. The company had already integrated the support functions like Finance, HR and IT. We believe that the integration of both the business units into one is likely in HUL as well. We believe the efficacy of the new structure will likely be dependent upon the degree of business and financial autonomy provided to the business segment heads (soaps, detergents, beverages etc.). Integration at middle and top management levels will result in a leaner organization, while HUL will likely continue with the current sales organization (matrix) focused on channels as well as categories. We note that Unilever's global competitors, Nestle and P&G, already have similar organization structures and hence directionally it was imperative for Unilever to follow suit. However, the key difference is that P&G predominantly has a HPC portfolio and Nestle has Foods.

Near-term performance likely secured, short-term outperformance likely to continue

We believe several factors will aid near-term performance—(1) beneficial base effect (personal products business grew at 6% for the first three quarters of CY2007), (2) strong underlying growth in detergents, (3) extended and harsh winter in the North and East favoring the personal products sales in 1QCY08 and (4) incremental fiscal benefits from new manufacturing facilities for Lakme in Haridwar. We believe that the stock will likely trade at our DCF-based target price of Rs230 in the near term, supported by positive news flows. The stock has delivered a relative performance (versus the Sensex) of 22% and 23% over the past one month and three months, respectively. We believe HUL will grow in line with industry at best and deliver 15% earnings CAGR over 2007-2009E. At the current market price of Rs222, the stock trades at 25X CY2008 and 21X CY2009. We retain our ADD rating and target price of Rs230/share.

Signifant price hikes across the portfolio in soaps…
Retail price changes in YTD CY08

Soap brand	Pack size (gms)	Latest MRP (Rs)	Increase (%)
Lifebuoy	115	14	7.7
Lifebuoy	3*90g	33	10.0
Lifebuoy	4*115g	52	8.3
Lifebuoy	90	12	9.1
Lifebuoy Clear	125	25	13.6
Lifebuoy Clear	75	16	14.3
Lifebuoy Plus	100	14	12.0
Lifebuoy Skinguard	75	16	6.7
Liril	75	18	12.5
Liril	125	30	15.4
Lux International	125	27	12.5
Lux International	75	17	13.3
Lux	100	17	6.3
Lux	150	24	14.3
Lux	4*100g	64	6.7
Lux	4*125g	75	17.2
Lux Whiteglow	3*125g	63	10.5
Lux Whiteglow	75	14	16.7
Rexona	100	17	6.3
Rexona	150	24	14.3
Hamam	100	17	6.3
Hamam	150	24	14.3
Hamam	4*150g	92	7.0
Dove	3*100g	114	14.0
Dove	75	30	11.1
Total soaps			

Source: Kotak Institutional Equities.

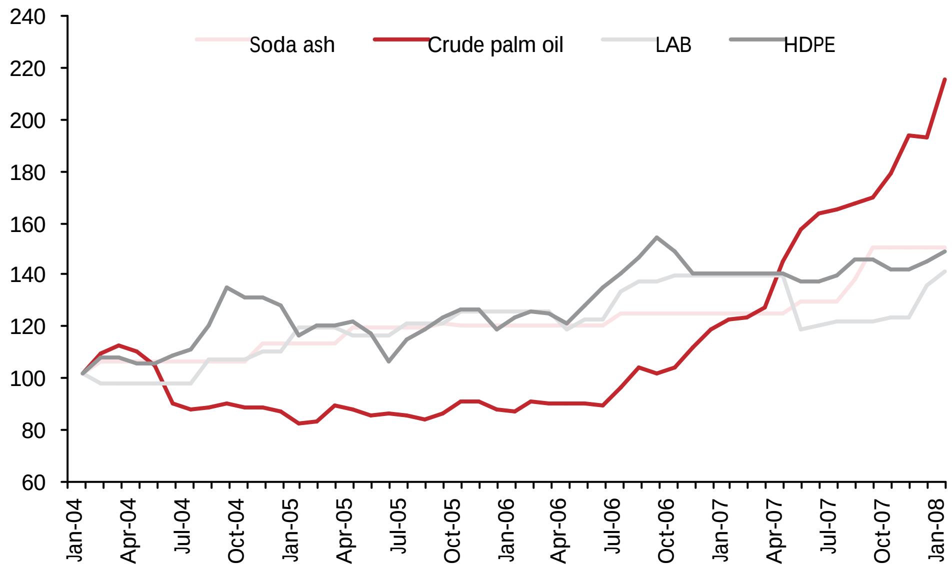
… and rest of the HPC portfolio
Retail price changes in YTD CY08

Category/brand	Pack size	Old MRP (Rs)	Latest MRP (Rs)	Increase (%)
Detergents	blended price-hike			4.0
Homecare-Vim	380g	16	17	6.3
Shampoo-Sunsilk	200ml	45	49	8.9
Shampoo-Sunsilk	400ml	85	89	4.7
Skin-Fair&Lovely	25g	32	33	3.1
Skin-Fair&Lovely	50g	57	59	3.5

Source: Kotak Institutional Equities.

High commodity prices necessitate price increases in soaps and detergents

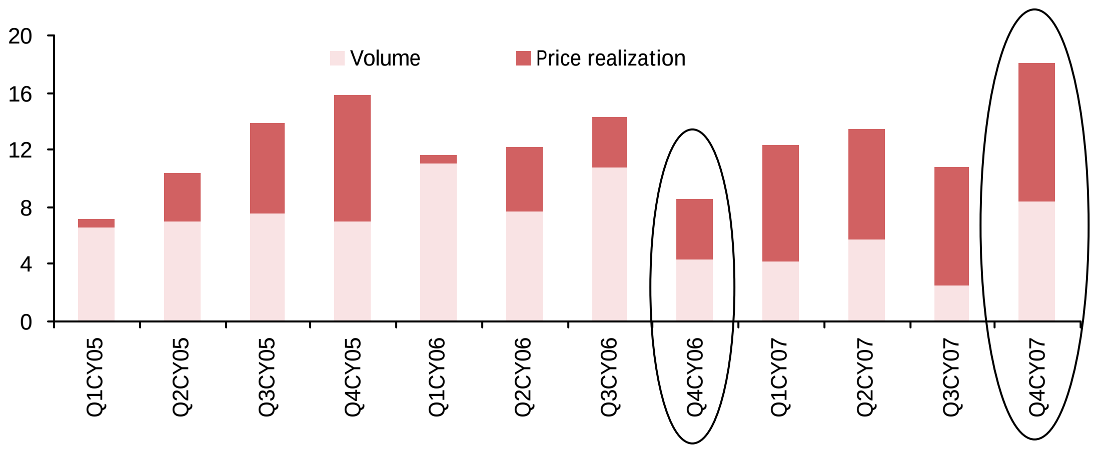
Key raw material price trends (January 2004 = Index 100)



Source: FAO, Cris Infac, Reliance Industries, Kotak Institutional Equities.

Robust macro conditions will likely aid sustaining 6% volume growth

Volume, price realization growth for HUL FMCG (%)



Source: Company data, Kotak Institutional Equities.

HUL: Profit model, balance sheet, cash model 2005-2009E, December year-ends (Rs mn)

	2005	2006	2007	2008E	2009E
Profit model (Rs mn)					
Net sales	110,605	121,034	137,178	154,745	174,811
EBITDA	**14,433**	**16621**	**18857**	**22239**	**26278**
Other income	3,048	3,545	4,627	4,417	4,767
Interest	(192)	(107)	(255)	(208)	(58)
Depreciation	(1,245)	(1,302)	(1,384)	(1,528)	(1,697)
Extraordinary items	976	3,155	1,581	-	-
Pretax profits	17,021	21,912	23,426	24,920	29,290
Tax	(2,530)	(2,950)	(3,812)	(4,531)	(5,850)
Deferred taxation	(410)	(268)	(359)	(364)	(385)
Net profits	**14,081**	**18,694**	**19,255**	**20,026**	**23,055**
Earnings per share (Rs)	**6.0**	**7.0**	**8.0**	**9.2**	**10.6**
Balance sheet (Rs mn)					
Total equity	23,056	27,235	17,193	18,276	19,524
Total borrowings	569	726	726	726	726
Currrent liabilities	41,183	45,231	54,205	57,338	64,609
Total liabilities and equity	**64,809**	**73,191**	**72,124**	**76,341**	**84,858**
Cash	3,550	4,169	4,682	4,299	7,396
Current assets	24,080	27,527	31,309	34,961	39,259
Total fixed assets	14,835	15,110	16,248	17,559	19,068
Investments	20,142	24,139	17,999	17,999	17,999
Deferred tax asset	2,201	2,245	1,886	1,523	1,137
Total assets	**64,809**	**73,191**	**72,124**	**76,341**	**84,858**
Free cash flow (Rs mn)					
Operating cash flow, excl. working capital	15,908	20,209	21,202	22,072	25,426
Working capital	5,858	(471)	1,513	1,121	1,428
Capital expenditure	(904)	(1,576)	(2,522)	(2,838)	(3,206)
Investments	2,452	(4,309)	6,141	-	-
Free cash flow	**23,314**	**13,852**	**26,334**	**20,355**	**23,647**
Key assumptions					
Revenue Growth (%)	11.4	9.4	12.3	13.9	13.0
EBITDA Margin(%)	13.2	13.9	14.1	14.4	15.0

Source: Kotak Institutional Equities estimates.

Consumer Products

NEST.BO, Rs1420	
Rating	ADD
Sector coverage view	Attractive
Target Price (Rs)	1,560
52W High -Low (Rs)	1676 - 878
Market Cap (Rs bn)	136.9

Financials

December y/e	2006	2007E	2008E
Sales (Rs bn)	28.2	34.7	40.7
Net Profit (Rs bn)	3.3	4.3	5.4
EPS (Rs)	33.9	44.5	55.7
EPS gth	*(0.7)*	*31.3*	*25.2*
P/E (x)	41.9	31.9	25.5
EV/EBITDA (x)	24.5	19.2	15.5
Div yield (%)	1.8	1.9	2.4

Shareholding, December 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	61.8	-	-
FIIs	7.9	0.1	(0.2)
MFs	5.5	0.4	0.2
UTI	-	-	(0.3)
LIC	3.4	0.2	(0.0)

Nestle India: Nestle S.A raises growth outlook--Nestle India appears to follow suit

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- **Nestle S.A reiterates strong outlook, similar contours seen in Nestle India**
- **Price increases ahead of cost inflation**
- **Reiterate ADD rating and target price of Rs1,560/share**

Nestle S.A has reiterated the strong organic growth projection for 1QCY08 and significant improvement in margins for CY2008. The company forecasts organic growth similar to CY2007 levels with margin improvement led by pricing action. We believe that the contours for Nestle India are very similar. We believe that the trend of pricing action ahead of cost increases will help Nestle India improve EBITDA margins by 100 bps to 21% in CY2008E. We model 17.2% sales growth driven by robust volume growth and net profit growth of 25.2% driven by EBITDA margin expansion. Prices of skimmed milk powder appear to be declining after peaking in July 2007. The benchmark Oceania export SMP in January 2008 at US$4,250/ton was 18% lower than the peak of US$5,150/ton in July 2007. The stock has delivered a relative performance (versus the Sensex) of 17% and 18% over the past one month and three months, respectively. At the current market price of Rs1,420, the stock is trading at 25X CY2008E and 21X CY2009E. We reiterate our ADD rating and target price of Rs1,560/share.

Nestle S.A reiterates strong outlook, similar contours seen in Nestle India

Nestle S.A has reiterated the strong organic growth projection for 1QCY08 and significant improvement in margins for CY2008. The company forecasts organic growth similar to CY2007 levels with margin improvement led by pricing actions. We quote the relevant portion from the company's investor communication:

"During 2007 and in the current year, commodity markets have been characterized by sharp upward movements and increased volatility. This reflects strong global demand for food, accelerating usage of food raw materials for biofuels and the decisive presence in the market of non-traditional speculative players. Consequently, the Group was forced to advance price increases for finished goods in order to partially absorb the higher input costs. Combined with the pricing effects in place at the end of last year, this accounts for a strong pricing element in organic growth for the first two months of 2008."

We believe that the contours for Nestle India are very similar. A strong macro environment and healthy business model helped Nestle India deliver 24% growth in topline and 31% growth in PAT in CY2007—aided by 90 bps expansion in EBITDA margins. We had highlighted in our earlier note dated March 7, 2008 that the sales increase during CY2007 has been on account of both price increase and higher volumes across categories. We estimate the company has instituted over 10% blended price increases with certain categories like infant foods witnessing the maximum traction w.r.t. price increases at over 15%.

Price increases ahead of cost inflation

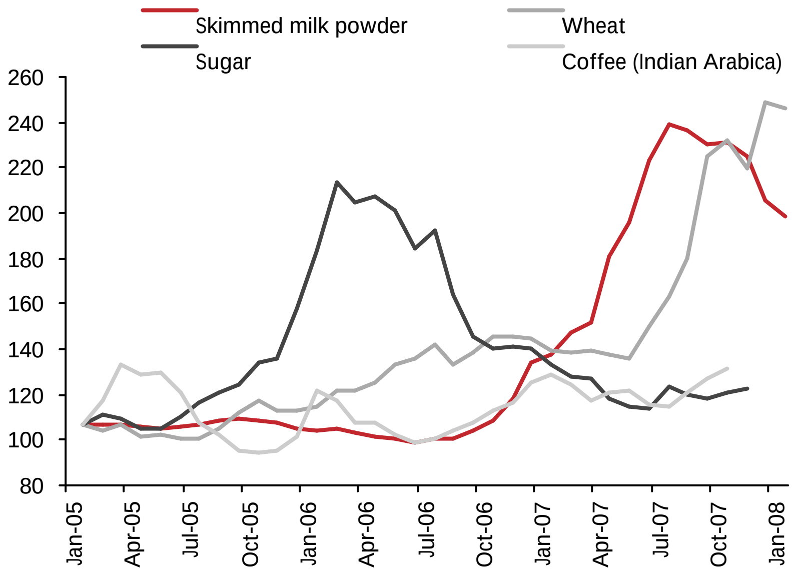
We note that margins continue to be under pressure due to hyper-inflation in key commodities such as skimmed milk powder (SMP), green coffee and wheat flour. However, current prices indicate that SMP prices seem to be declining after peaking in July 2007. The benchmark Oceania export SMP was quoting 18% lower at US$4,250/ton in January 2008 after touching a peak of US$5,150/ton in July 2007. We believe that the trend of pricing action ahead of cost increases will help the company improve EBITDA margins by 100 bps to 21% in CY2008E. We are confident of the company's ability to pass on raw material and packing material cost inflation if required. We like the innovation capabilities of the company (e.g., launch of probiotic yoghurts) and the multiple growth drivers it possesses. We note that Nestle's product portfolio and target audience offer pricing elasticity.

Reiterate ADD rating and target price of Rs1,560/share

We model 17.2% sales growth driven by robust volume growth and net profit growth of 25.2%, driven by a further 100 bps expansion in EBITDA margin to 21%. Our DCF model uses a WACC of 14% and a terminal year growth rate of 6%. The stock has delivered a relative performance (versus the Sensex) of 17% and 18% over the past one month and three months, respectively. At the current market price of Rs1,420, the stock is trading at 25X CY2008E and 21X CY2009E. We reiterate our ADD rating on the stock with a target rice of Rs1,560.

Cooling down of skimmed milk powder prices likely aid margin expansion in CY2008

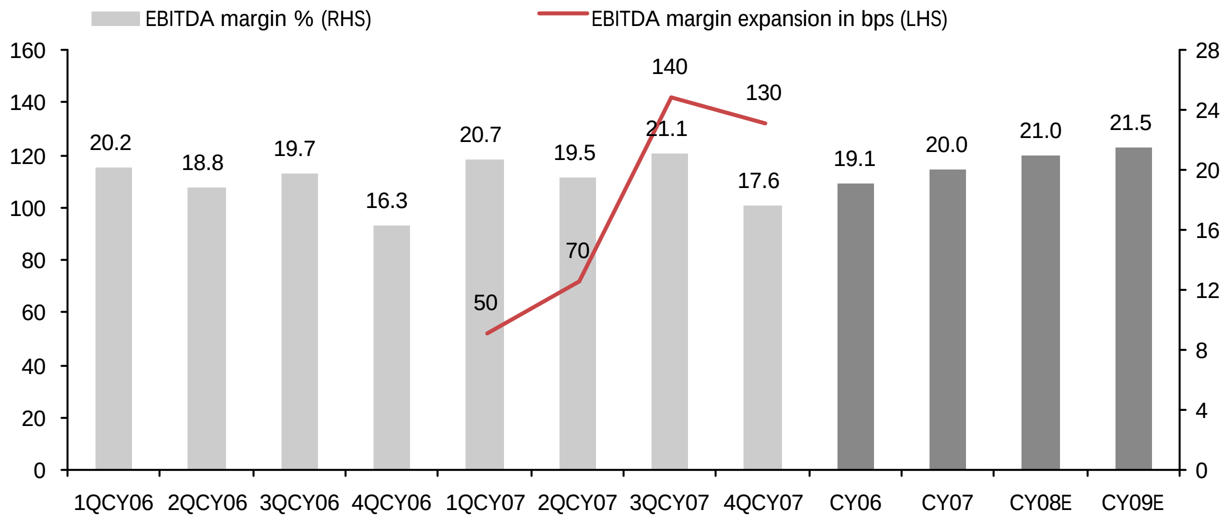
Key raw material price trends (January 2005 = Index 100)



Source: FAO, International Coffee Organisation, Kotak Institutional Equities.

EBITDA margin expansion driven by price increases ahead of cost inflation

EBITDA margins for Nestle India for the last 8 quarters and for CY06-09E



Source: Company, Kotak Institutional Equities.

Pipes

JIND.BO, Rs724	
Rating	BUY
Sector coverage view	Attractive
Target Price (Rs)	1,150
52W High -Low (Rs)	1225 - 458
Market Cap (Rs bn)	40.6

Financials

September y/e	2007	2008E	2009E
Sales (Rs bn)	67.0	49.0	73.1
Net Profit (Rs bn)	5.7	4.2	6.8
EPS (Rs)	115.9	77.0	120.4
EPS gth	*276.9*	*(33.6)*	*56.3*
P/E (x)	6.2	9.4	6.0
EV/EBITDA (x)	5.5	5.4	3.3
Div yield (%)	0.8	1.2	1.9

Shareholding, December 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	44.6	-	-
FIIs	12.4	0.1	(0.0)
MFs	16.9	0.5	0.4
UTI	-	-	(0.1)
LIC	-	-	(0.1)

Jindal Saw: Incorporate latest annual report and fine tune numbers; maintain TP and BUY rating

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- **We incorporate the latest annual report numbers and fine-tune our estimates for increasing raw material and resultant linepipe prices**
- **Continuing global demand for linepipes to keep conversion margins robust in the near term; we increase conversion spreads (but EBITDA margins drop due to higher base)**
- **We do not incorporate the recently-announced initiatives in our estimates given the absence of details**
- **We revise our EPS estimates higher to Rs73.7 and Rs120.4 for CY2008E and CY2009E from Rs68.6 and Rs114.2, respectively; maintain rating and target price**

We incorporate the latest annual report numbers for FY2007 (15-month period) and fine-tune our estimates for the higher raw material and resultant linepipe prices. We expect strong demand for linepipes on the back of higher crude prices to keep linepipe conversion margins robust. We marginally increase our conversion margin estimates for CY2008E and CY2009E but EBITDA margin estimates drop on account of higher raw material and resultant linepipe prices. We highlight that plate and coil prices continue to rise in the USA, Europe and Japan on account of increasing raw material prices and limited API approved capacities for slabs, coils and plates. However, we highlight that increasing capacity additions for linepipes and plates should bring down conversion margins across linepipes in the next two years. We model lower conversion margins in CY2010E. We maintain our volume estimates but revise our revenue and net earnings estimates for increasing raw material and resultant pipe prices. We revise our EPS estimate for CY2008E and CY2009E to Rs73.7 and Rs120.4 from Rs68.6 and Rs114.2, respectively.

Adjusted EBITDA margin for FY2007 was 12.5% versus earlier reported 11.8%

We incorporate the latest annual report numbers and highlight that adjusted EBITDA margins were higher at 12.5% versus the earlier reported 11.8%. We adjust extraordinary items of Rs444 mn on account of liquidated damages and provision for bad and doubtful debts, which were earlier reported as part of other expenses. As a result, adjusted PAT for FY2007 was Rs5.7 bn versus earlier reported Rs5.2 bn.

Revise pricing assumptions for raw materials and finished products

Increasing steel prices across categories continue to increase raw material prices for JSAW. We revise our pricing assumptions higher for raw material—coils and slabs for linepipes—and finished linepipes. We also increase prices of DI pipes for higher coke and iron ore prices. We also revise our gross and conversion spreads higher on account of continuing demand for linepipes, capacities for which continue to be in short supply in high-demand regions such as USA and the Middle-East.

Revise estimates higher

We revise our revenue and net earnings estimates higher for CY2008E-10E for higher raw material and resultant finished goods prices. We maintain our volume estimates but increase conversion spreads mainly for linepipes. We revise net earnings estimates higher by 7.3% and 5.4% for CY2008E and CY2009E, respectively.

Exhibit 1: Forecasts and valuation (consolidated)

December year-end	Sales (Rs mn)	EBITDA (Rs mn)	Adj. PAT (Rs mn)	EPS (Rs)	RoAE (%)	P/E (X)	EV/EBITDA (X)
2006 (1)	38,731	4,066	1,563	29.5	15.3	24.6	11.4
2007 (2)	66,957	8,371	5,745	105.2	23.3	6.9	5.0
2008E	48,955	7,695	4,205	73.7	14.8	9.8	5.5
2009E	73,103	11,922	6,819	120.4	20.3	6.0	3.3
2010E	79,930	13,009	7,801	138.3	19.4	5.2	2.6

Note:
(1) September fiscal year-ends.
(2) 15 month period ending December 2007.

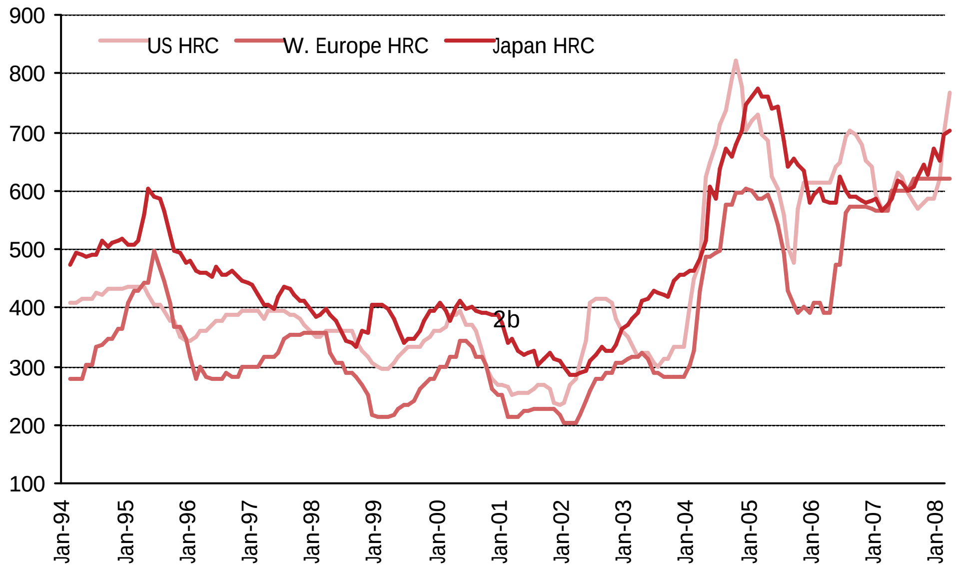
Source: Company data, Kotak Institutional Equities estimates.

Exhibit 2: Jindal Saw Ltd., change in estimates, December year-ends, (Rs mn)

	2008E			2009E			2010E		
	New	Old	Change (%)	New	Old	Change (%)	New	Old	Change (%)
Financials									
Revenue	48,955	42,736	14.6	73,103	63,830	14.5	79,930	69,519	15.0
EBITDA	7,695	7,072	8.8	11,922	11,033	8.1	13,009	11,996	8.4
EBITDA margin (%)	15.7	16.5	—	16.3	17.3	—	16.3	17.3	—
Adjusted net profit	4,205	3,918	7.3	6,819	6,472	5.4	7,801	7,423	5.1
Diluted EPS	73.7	68.6	7.4	120.4	114.2	5.4	138.3	131.6	5.1
Sales ('000 tons)									
HSAW	100	100	—	238	238	—	288	288	—
LSAW	360	360	—	480	480	—	560	560	—
Seamless	96	96	—	188	188	—	188	188	—
DI	221	221	—	234	234	—	239	239	—
Realisation (US$/ton)									
HSAW	1,416	1,303	8.7	1,487	1,342	10.8	1,480	1,328	11.4
LSAW	1,719	1,459	17.9	1,788	1,502	19.1	1,779	1,487	19.7
Seamless	1,537	1,406	9.3	1,587	1,434	10.7	1,587	1,434	10.7
DI	1,002	866	15.7	1,022	910	12.3	1,022	910	12.3
Raw material cost (US$/ton)									
HR coil	900	867	3.8	945	893	5.9	945	884	6.9
Plates	1,168	983	18.8	1,215	1,013	19.9	1,215	1,003	21.1
Billets	731	600	21.9	717	612	17.1	717	619	15.7
Iron ore	105	78	33.9	125	80	56.8	120	81	49.1
Coke	205	96	113.0	180	98	84.7	171	99	72.9
Gross spread (US$/ton)									
HSAW	469	391	20.0	492	402	22.4	485	398	21.9
LSAW	515	445	15.7	536	458	17.1	527	453	16.3
Seamless	656	683	(4.0)	724	697	3.8	724	688	5.2
DI	653	654	(0.1)	660	694	(4.9)	676	691	(2.3)

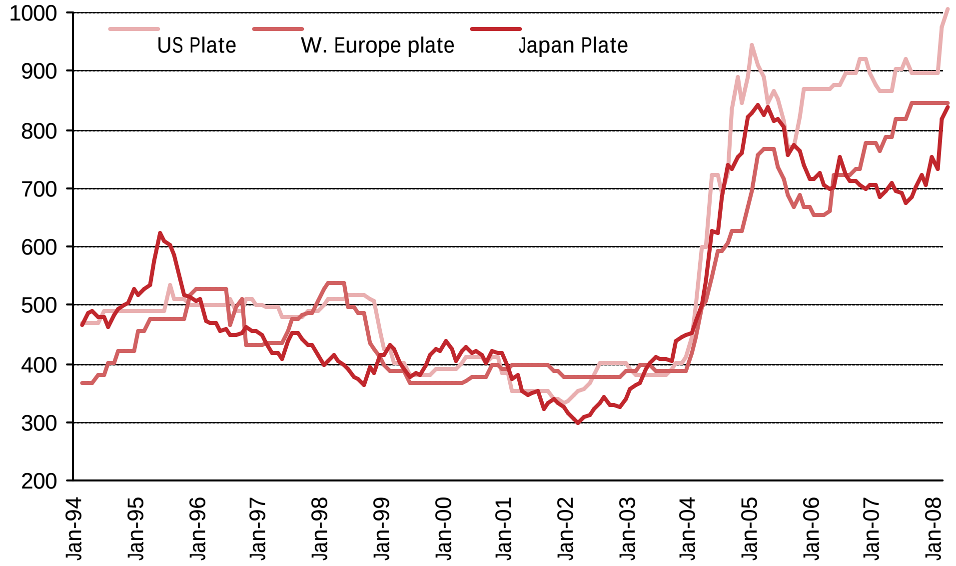
Source: Kotak Institutional Equities estimates.

Exhibit 4: Non-API hot-rolled coil prices (US$/ton)



Source: CRU

Exhibit 3: Non-API plate prices (US$/ton)



Source: CRU

Exhibit 5: Profit model, balance sheet, cash model for Jindal Saw, September fiscal year-ends, 2005-2006, December fiscal year-ends, 2007E-2010E (Rs mn)

	2005	2006	2007(1)	2008E	2009E	2010E
Profit model						
Net revenues	23,138	38,731	66,957	48,955	73,103	79,930
EBITDA	**2,802**	**4,066**	**8,371**	**7,695**	**11,922**	**13,009**
Other income	105	144	112	100	100	100
Interest (expense)/income	(985)	(1,290)	(1,684)	(399)	(353)	57
Depreciation	(365)	(537)	(773)	(998)	(1,309)	(1,310)
Amortization	—	—	—	—	—	—
Pretax profits	**1,558**	**2,383**	**6,026**	**6,397**	**10,360**	**11,856**
Tax	(374)	(704)	(2,777)	(1,809)	(3,024)	(3,819)
Deferred taxation	(133)	(164)	(63)	(383)	(517)	(236)
Minority intt	—	2	56	—	—	—
Adjusted consolidated net income	**1,032**	**1,563**	**5,745**	**4,205**	**6,819**	**7,801**
Diluted earnings per share (Rs)	**21.3**	**29.5**	**105.2**	**73.7**	**120.4**	**138.3**
Balance sheet						
Total equity	6,922	8,631	22,750	29,242	35,009	41,656
Deferred taxation liability	599	763	826	1,209	1,726	1,962
Total borrowings	12,979	17,217	13,455	7,750	5,500	3,200
Minority Interest	—	151	95	95	95	95
Current liabilities	5,012	12,303	10,429	14,063	20,427	22,260
Total liabilities and equity	**25,512**	**39,066**	**47,555**	**52,359**	**62,757**	**69,172**
Cash	1,526	3,922	6,586	5,274	5,951	9,898
Other current assets	15,256	24,055	25,496	27,238	38,476	41,843
Total fixed assets	7,862	10,254	13,380	18,073	17,057	16,159
Miscl. Exps. not w/o	1	—	—	—	—	—
Investments	868	836	2,093	1,772	1,272	1,272
Total assets	**25,512**	**39,066**	**47,555**	**52,359**	**62,757**	**69,172**
Free cash flow						
Operating cash flow, excl working capital	1,371	2,375	14,450	5,486	8,545	9,248
Working capital changes	(6,135)	(2,231)	(4,635)	1,649	(5,234)	(1,637)
Capital expenditure	(2,108)	(2,815)	(3,909)	(5,734)	(335)	(454)
Investments	(94)	345	(718)	320	500	—
Other income	177	351	311	100	100	100
Free cash flow	**(6,872)**	**(2,671)**	**5,906**	**1,401**	**2,975**	**7,157**
Ratios (%)						
EBITDA margin (%)	12.1	10.5	12.5	15.7	16.3	16.3
Debt/equity		172.6	106.8	39.8	25.8	15.2
Net debt/equity		152.3	76.5	10.0	5.2	(2.3)
RoAE		18.1	15.3	23.3	14.8	20.3
RoACE		**10.5**	**10.2**	**22.3**	**11.8**	**17.5**

Note: (1) 15 months period ended December 2007.

Source: Company, Kotak Institutional Equities estimates.

Exhibit 6: Our 12-month target price for JSAW is Rs1,150

	Rs/share
DCF-based business value	944
Value of quoted investments	199
Total equity value	1,143
Target price	**1,150**

Source: Kotak Institutional Equities estimates.

Jindal SAW, DCF valuation, December year-ends, (Rs mn)

DCF valuation of Jindal Saw, December fiscal year-ends

	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	Terminal Value
EBITDA	7,695	11,922	13,009	12,616	12,382	11,385	11,070	11,094	11,119	11,145	11,170	
Tax expense	(1,903)	(3,107)	(3,776)	(3,975)	(4,001)	(3,739)	(3,628)	(3,536)	(3,444)	(3,455)	(3,443)	
Changes in working capital	1,649	(5,234)	(1,637)	(534)	(116)	1,146	784	(13)	(13)	(13)	(13)	
Cash flow from operations	**7,441**	**3,581**	**7,597**	**8,107**	**8,265**	**8,791**	**8,225**	**7,545**	**7,662**	**7,676**	**7,714**	
Capital expenditure	(5,734)	(335)	(454)	(579)	(593)	(608)	(623)	(639)	(655)	(1,208)	(1,262)	
Free cash flow to the firm	**1,706**	**3,245**	**7,143**	**7,528**	**7,672**	**8,183**	**7,602**	**6,906**	**7,007**	**6,468**	**6,452**	**59,533**
Dicounted cash flow-now	1,553	2,625	5,136	4,812	4,359	4,133	3,412	2,756	2,485	2,039	1,808	
Discounted cash flow-1 year forward		2,954	5,778	5,413	4,904	4,649	3,839	3,100	2,796	2,294	2,034	
Discounted cash flow-2 year forward			6,500	6,090	5,517	5,230	4,319	3,488	3,146	2,581	2,288	
Discount rate	12.5%											
Growth from 2017 to perpetuity	1.5%											
Discount factor at WACC	**0.91**	**0.81**	**0.72**	**0.64**	**0.57**	**0.51**	**0.45**	**0.40**	**0.35**	**0.32**	**0.28**	

	+ 1-year		+ 2-years	
Total PV of free cash flow (a)	**37,762**	**69%**	**39,160**	**68%**
PV of terminal value (b)	16,684	31%	18,770	32%
EV (a) + (b)	54,446		57,930	
EV (US$ mn)	**1,344**		**1,430**	
Net debt	1,570		(856)	
Equity value	**52,876**		**58,786**	
No. of shares	56.0		56.0	
Implied share price (Rs)	**944**		**1,050**	
Exit EV/EBITDA multiple (X)	5.3			
Exit FCF multiple (X)	**9.2**			

Sensitivity of share price to WACC and growth rate (Rs)

Growth Rate	WACC 11.5%	12.0%	12.5%	13.0%	13.5%
0.0%	984	943	905	869	837
0.5%	1,000	956	917	880	846
1.0%	1,017	971	930	892	857
1.5%	1,036	988	**944**	904	868
2.0%	1,057	1,006	960	918	880
2.5%	1,080	1,026	977	933	893
3.0%	1,106	1,048	996	950	907

Source: Company, Kotak Institutional Equities estimates.

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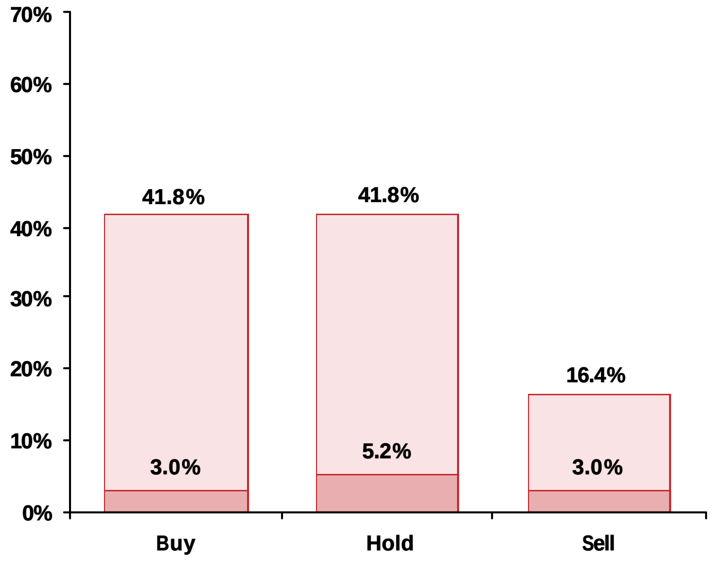

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* The above categories are defined as follows: Buy = OP; Hold = IL; Sell = U. Buy, Hold and Sell are not defined Kotak Institutional Equities ratings and should not be constructed as investment opinions. Rather, these ratings are used illustratively to comply with applicable regulations. As of 09/30/07 Kotak Institutional Equities Investment Research had investment ratings on 144 equity securities.

Source: Kotak Institutional Equities. As of September 30, 2007

Ratings and other definitions/identifiers

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Old rating system

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

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