## Economy News

- The country's industrial growth has slowed down to 7.1 per cent in June. This follows eight consecutive months of double-digit year-on-year increases in the official index of industrial production (IIP). (BL)
- Parliament has passed a law for stricter regulation of export of sensitive dual-use technology. It has also allowed the government to impose restrictions on imports of farm goods in the face of import surges. (ET)
- The Centres indirect tax collections grew a strong 46.2% in the first four months of the current fiscal from a year ago,pointing at a pick up in economic activity in July after industrial production growth in June came in below expectation. (ET)

## Corporate News

- The Reserve bank of India has approved the amalgamation of the Bank of Rajasthan with the **ICICI Bank**. (ET)
- **Oil and Natural Gas Corporation (ONGC)** proposes to set up 102 mw capacity wind power project in Rajasthan at an estimated cost of 6.5 bn. (ET)
- Auto major **Tata Motors,** said it plans to expand its commercial vehicles business globally and is contemplating a new plant for small trucks in India. (BL)
- **Essar Shipping** on Thursday said it plans to demerge its shipping,logistics and oil fields business into a separate entity, which will push the ports growth plans independently. (BS)
- **UB Engineering,** the engineering, procurement & construction (EPC) company ,has marked its foray into the infrastructure sector by establishing a subsidiary UB Infrastructure. (ET)
- A unit of **Jindal Steel and Power (JSPL)** has discovered coal reserves of 1,650 mt in north-west Mozambique. (ET)
- **Reliance Power (R-Power)** would seek shareholders' approval for raising more funds, via share sale to institutions or by issuing securities overseas, after spending half of the Rs 116 bn raised in the country's biggest initial public offer (IPO) in 2008. (BS)
- **Mahindra & Mahindra (M&M),** India's largest maker of sports utility vehicles (SUV), said that it has been selected the preferred bidder for the acquisition of a majority stake in South Korean SUV maker Ssangyong Motor Company (SYMC). (BS)
- Edinburgh, UK-based Cairn Energy Plc on Thursday said it was in talks with Vedanta Resources Plc to sell a stake in its Indian unit, **Cairn India**, which operates oil and gas fields in Rajasthan and Andhra Pradesh. (BS)

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

### Equity

| | | % Chg | | |
|---|---|---|---|---|
| | 12 Aug 10 | 1 Day | 1 Mth | 3 Mths |
| **Indian Indices** | | | | |
| SENSEX Index | 18,074 | 0.0 | 0.5 | 4.7 |
| NIFTY Index | 5,416 | - | 0.3 | 4.6 |
| BANKEX Index | 12,028 | 1.7 | 6.4 | 8.9 |
| BSET Index | 5,496 | (0.9) | 1.8 | 3.5 |
| BSETCG INDEX | 14,655 | (0.2) | (1.7) | 8.8 |
| BSEOIL INDEX | 10,059 | 0.2 | (6.2) | (0.1) |
| CNXMcap Index | 8,610 | - | 2.8 | 8.1 |
| BSESMCAP INDEX | 9,645 | 0.0 | 2.7 | 8.0 |
| **World Indices** | | | | |
| Dow Jones | 10,320 | (0.6) | (0.4) | (4.3) |
| Nasdaq | 2,190 | (0.8) | (2.3) | (8.5) |
| FTSE | 5,266 | 0.4 | (0.1) | (3.1) |
| Nikkei | 9,213 | (0.9) | (3.7) | (13.5) |
| Hangseng | 21,106 | (0.9) | 3.0 | 3.0 |

### Value traded (Rs cr)

| | 12 Aug 10 | % Chg - Day |
|---|---|---|
| Cash BSE | 5,143 | (0.2) |
| Cash NSE | 15,897 | 0.2 |
| Derivatives | 104,776.8 | 14.7 |

### Net inflows (Rs cr)

| | 11 Aug 10 | % Chg | MTD | YTD |
|---|---|---|---|---|
| FII | 193 | (68.6) | 4,028 | 51,930 |
| Mutual Fund | 115 | (129.6) | (779) | (13,310) |

### FII open interest (Rs cr)

| | 11 Aug 10 | % Chg |
|---|---|---|
| FII Index Futures | 17,388 | 2.4 |
| FII Index Options | 59,030 | 2.8 |
| FII Stock Futures | 36,184 | 1.7 |
| FII Stock Options | 1,761 | 7.0 |

### Advances / Declines (BSE)

| 12 Aug 10 | A | B | S | Total | % total |
|---|---|---|---|---|---|
| Advances | 100 | 820 | 163 | 1,083 | 42 |
| Declines | 99 | 1040 | 268 | 1,407 | 55 |
| Unchanged | 5 | 73 | 13 | 91 | 4 |

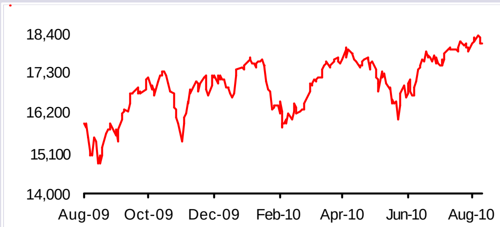
### Commodity

| | | % Chg | | |
|---|---|---|---|---|
| | 12 Aug 10 | 1 Day | 1 Mth | 3 Mths |
| Crude (NYMEX) (US$/BBL) | 76 | 0.8 | (1.0) | 2.6 |
| Gold (US$/OZ) | 1,214 | 1.3 | 0.2 | (1.5) |
| Silver (US$/OZ) | 18 | 0.9 | (0.5) | (6.6) |

### Debt / forex market

| | 12 Aug 10 | 1 Day | 1 Mth | 3 Mths |
|---|---|---|---|---|
| 10 yr G-Sec yield % | NA | | | |
| Re/US$ | 46.78 | 46.70 | 46.78 | 45.11 |

### Sensex



ECONOMY UPDATE

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# JUNE IIP: GREW AT 7.1%

## June IIP slows to 7.1% YoY; index is flat MoM though, in a seasonally weak month

**The IIP for June 2010 grew by 7.1% YoY, slower than our and consensus estimates. However, on a MoM basis, the index remained almost flat, despite a seasonally weak month (June v/s May), providing some comfort. Growth rates in Capital Goods moderated to 9.7% v/s 34.3%, largely due to the base effect, we believe. On a MoM basis, the CG index rose 6.3%. With several companies operating at near peak utilization levels, we can expect CG index to rise at a faster pace in the future months, as capacities are increased. On the other hand, the Consumer Durables index continued to report robust growth (27.4%), reflecting continued consumer demand. A pick up in the economy has resulted in inflation breaching the 10% mark. Inflation which was initially driven by high food prices (supply side effect) is now getting push from other segments as well (demand side effect). We expect RBI to act again, in case the demand side push continues in the future.**

## Key highlights

After posting double digit growth over the last ten consecutive months, manufacturing production moderated to 7.3%YoY in Jun10 vs. 12% the previous month (and 8%YoY in Jun09). IIP internals show slowing broad based growth, as 13 out of 17 industry groups have shown positive growth during the month of June 2010 compared with 15 out of 17 industry groups in past few months.

## Sectoral growth - capital goods saw moderation in growth rates; consumer durables continued the strong showing

The sectoral growth (use-based classification) was as under :

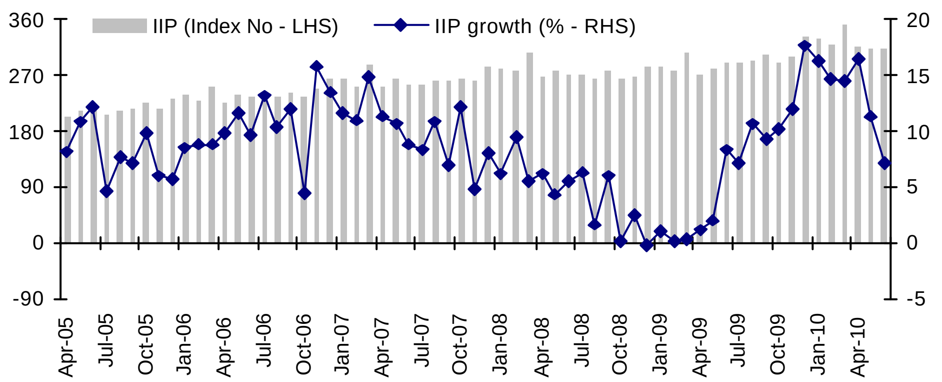
- Basic goods: 3.4% (against 7.9% in April 2010), 3-month moving average: 6.9%
- Capital goods: 9.7% (against 34.3% in April 2010), 3-month moving average: 37.9%
- Intermediate goods: 8.7% (against 10.2% in April 2010), 3-month moving average: 9.8%
- Consumer goods: 8.3% (against 8.2% in April 2010), 3-month moving average: 9.2%
- Consumer durables: 27.4% (against 23.7% in April 2010), 3-month moving average: 27.9%
- Consumer non-durables: 1.3% (against 2.4% in April 2010), 3-month moving average: 2.4%

**Index of Industrial Production**

| Month | Mining Index | Growth (%) | Mfg Index | Growth (%) | Electricity Index | Growth (%) | General Index | Growth (%) |
|---|---|---|---|---|---|---|---|---|
| Weight | 10.47% | YoY | 79.36% | YoY | 10.17% | YoY | 100.00% | YoY |
| Apr-09 | 176.9 | 3.39 | 286.1 | 0.39 | 232.9 | 6.70 | 269.3 | 1.13 |
| May-09 | 183.4 | 3.38 | 298.5 | 1.84 | 237.6 | 3.26 | 280.3 | 2.08 |
| Jun-09 | 181.4 | 14.23 | 313.5 | 7.95 | 234.4 | 7.97 | 291.6 | 8.32 |
| Jul-09 | 175.5 | 8.74 | 313.1 | 7.37 | 235.4 | 4.21 | 290.8 | 7.19 |
| Aug-09 | 178.1 | 11.03 | 314.0 | 10.56 | 245.1 | 10.60 | 292.8 | 10.62 |
| Sep-09 | 174.9 | 7.37 | 327.2 | 9.65 | 235.8 | 7.52 | 302.0 | 9.34 |
| Oct-09 | 191.1 | 9.14 | 309.0 | 10.91 | 240.4 | 3.98 | 289.7 | 10.19 |
| Nov-09 | 194.2 | 10.72 | 323.9 | 13.13 | 220.4 | 1.85 | 299.8 | 12.03 |
| Dec-09 | 209.0 | 11.11 | 363.5 | 19.38 | 235.2 | 5.42 | 334.3 | 17.71 |
| Jan-10 | 216.9 | 15.31 | 357.9 | 17.42 | 240.6 | 5.57 | 331.2 | 16.29 |
| Feb-10 | 203.3 | 11.0 | 344.1 | 15.7 | 228.3 | 7.3 | 317.6 | 14.7 |
| Mar-10 | 235.6 | 12.3 | 377.0 | 15.3 | 261.4 | 8.3 | 350.4 | 14.5 |
| April-Mar 09-10 | 9.8% | | 10.8% | | 6.1% | | 10.3% | |
| Apr-10 | 197.6 | 11.7 | 337.4 | 17.9 | 248.9 | 6.9 | 313.8 | 16.5 |
| May-10 | 201.9 | 10.1 | 334.3 | 12.0 | 252.2 | 6.1 | 312.1 | 11.3 |
| Jun-10 | 198.6 | 9.5 | 336.4 | 7.3 | 242.6 | 3.5 | 312.4 | 7.1 |

*Source: Ministry of Statistics and Programme Implementation and Kotak Securities - Private Client Research*

**Trend in IIP**




*Source: Ministry of Statistics and Programme Implementation and Kotak Securities - Private Client Research*

In May 2010, capital goods posted moderate growth of 34.3% against whopping 70% in April 2010, which further moderated to 9.7% in June 2010. However, Consumer durables have continued to show significant improvement by posting growth of 27.4% against that of 23.7% in May and 32.8% in April 2010). This likely suggests that, domestic consumer demand growth continues to be strong outpacing investment demand, reflecting higher consumer confidence.

## Capital goods growth moderates - index grows 6.2% MoM, though

Capital goods segment, which has 9.25% weights in IIP, took a breather from stellar performance by growing at 9.7% in June from 34.2% in May, growing at 37.9% on 3 month moving average basis.

However, on a MoM basis, this segment reported a 6.3% growth and this, in our view is a comforting factor. Moreover, with several companies / industries likely operating at peak capacity utilizations, we expect this segment to witness further growth as capacities are hiked. Also, we believe that, the moderation is a result of the high base of June 2009, where the index had risen by 30.2% MoM.

Intermediate goods posted 8.7% growth in June from 10.2% in May against 9.8% on 3 month moving average basis. In our opinion, the numbers suggest that the RBI's measures (taken in past few months) are showing effect in form of cooling down the economy towards its long term trend growth; hence narrowing the output gap.

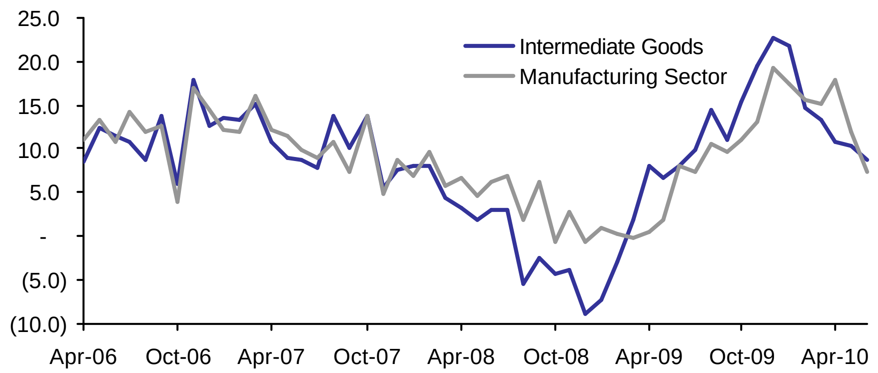
We would wait for few more months' numbers and monsoon's progress before concluding whether the growth is likely to taper off from here on, on real basis or not!

## Intermediate goods continued to report steady growth - should lead to higher capital goods growth

Intermediate goods reported a 8.7% rise during the month on a YoY basis. Though this was lower as compared to 10.2% reported in the previous month, it is still decent, in our opinion.

The accompanying chart shows that there is a high correlation between growth of intermediate goods and manufacturing goods (Correlation: 0.86). Output of Intermediate and basic goods are used for production by the final user sectors like capital goods and consumer goods. However, divergence between intermediate and manufacturing sector in past few months had shown that the internals are not as strong as suggested by the headline numbers.

**Intermediate goods vs Manufacturing goods**




*Source: Ministry of Statistics and Programme Implementation and Kotak Securities - Private Client Research*

## Strong growth in consumer durables continues - RBI action in focus

Consumer durables have grown at 27.4% in June from 23.7 in May, growing by over 27.9% on 3 month moving average basis. However, consumer non-durables segment is still showing mixed signs it grew by meager 1.3% in June from 2.4% in May 2010.

The continuing strong growth in consumer durables indicates continued spending by people. This, in turn, likely reflects the continued optimism on the economy and income levels.

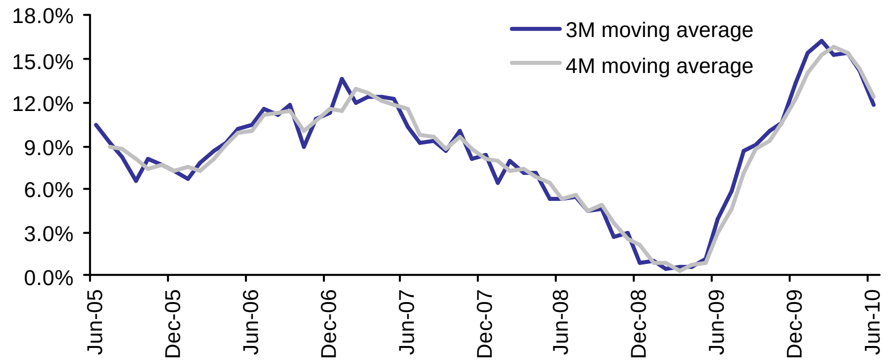
This optimism has led to the demand-pull effect on inflation. The RBI has also submitted that, the inflation has spread from food and primary articles (largely supply - led) to other parts of the economy, because of the higher demand.

The continued rise in consumer demand led inflation may induce the RBI to continue with tightening.

## Extended V-shaped recovery soften, likely to remain flat in H2FY11

In line with expectations the V-shaped industrial recovery is extending and is likely to be sustained till H1FY11, even though next year the growth rate may flatten a bit towards a higher single digit number on a significantly higher base. MoM IIP growth in June was 10 basis points lower against 54 basis point MoM decrease in May keeping 4-month IIP growth to 12.4% in June, on moving average (MA) basis. (see Exhibit 5).

### 3M & 4M moving average



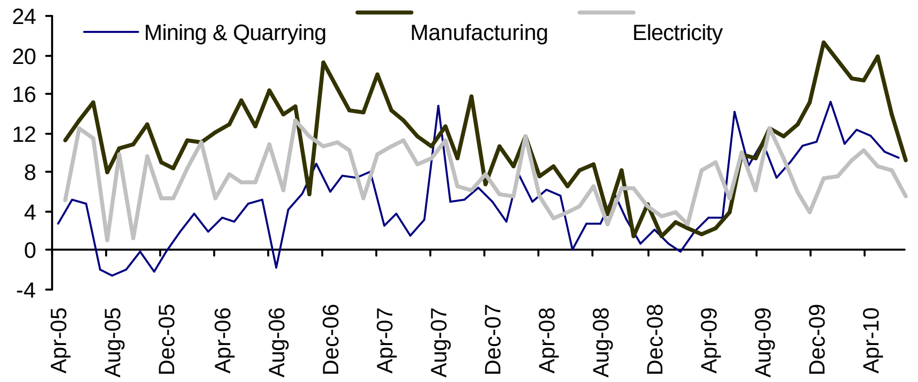

*Source: Ministry of Statistics and Programme Implementation and Kotak Securities - Private Client Research*

## Conclusion

The strong trends in IIP growth are reflective of trends seen in various sectors like auto sales, cement dispatch and fuel consumption. IIP seems to have peaked in March, and we expect moderate improvements in IIP going forward. In our view IIP growth would likely flatten towards higher single digit growth rate once base effect benefits wane. Also, credit growth pick up and higher non-oil import bodes well for the economy going forward.

In our view, continued high IIP growth along with high inflation is likely to facilitate in RBI's focus on managing price stability. We expect WPI based inflation for July month to remain in higher territory; due to higher primary article prices. Expectation of near normal monsoon bodes well for prices of food articles. We expect RBI to act appropriately on the policy date, indicating tightening policy stance.

### Break up of Index of Industrial Production




*Source: Ministry of Statistics and Programme Implementation and Kotak Securities - Private Client Research*

**RESULT UPDATE**

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# GREAVES COTTON LTD

**PRICE: RS.375** **RECOMMENDATION: BUY**
**TARGET PRICE: RS.421** **FY11E P/E: 13.9x**

- **GCL has reported strong set of numbers, which are ahead of expectations mainly on account of higher revenues. EBITDA margins have dipped on a sequential basis mainly on account of higher staff costs, which is up 31% on a sequential basis. Apart from this, increase in excise duty also added to the margin decline.**
- **The company has changed its accounting year from June to March, thus the current fiscal will have only 9M numbers. Company has approved stock split into face value Rs 2. (Rs.10 earlier)**
- **We maintain BUY with target price of Rs 421.**

**Summary table**

| (Rs mn) | FY10** | FY11E* | FY12E* |
|---|---|---|---|
| Sales | 13,472 | 11,730 | 18,004 |
| Growth (%) | 29.9 | -12.9 | 53.5 |
| EBITDA | 2,064 | 1,621 | 2,752 |
| EBITDA margin (%) | 15.3 | 13.8 | 15.3 |
| Net profit | 1,186 | 942 | 1,660 |
| Net cash (debt) | 360 | 465 | 799 |
| EPS (Rs) (cons) | 24.3 | 19.3 | 34.0 |
| Growth (%) | 203.6 | -20.6 | 76.3 |
| CEPS | 29.7 | 24.0 | 41.1 |
| DPS (Rs) | 4.0 | 15.0 | 7.5 |
| ROE (%) | 26 | 20 | 30 |
| ROCE (%) | 38 | 29 | 42 |
| EV/Sales (x) | 1.3 | 1.5 | 1.0 |
| EV/EBITDA (x) | 8.7 | 11.0 | 6.4 |
| P/E (x) | 15.5 | 19.4 | 11.0 |
| P/Cash Earnings | 12.6 | 15.7 | 9.1 |
| P/BV (x) | 4.7 | 4.1 | 3.2 |

*Source: Company, Kotak Securities - Private Client Research*

** March ending; ** June ending*

**Quarterly performance**

| (Rs mn) | Q4 FY10 | Q4 FY09 | YoY (%) |
|---|---|---|---|
| **Gross sales** | **3796** | **2634** | **44** |
| Excise duty | 340 | 247 | 37 |
| SalesTurnover | 3457 | 2619 | 32 |
| other op income | 20 | 7 | 214 |
| Expenditure | 3023 | 2379 | 27 |
| RM costs | 2268 | 1822 | 25 |
| Purchase of traded goods | 132 | 47 | 181 |
| Staff costs | 295 | 218 | 35 |
| Other costs | 328 | 293 | 12 |
| **Operating profit** | **454** | **246** | **84** |
| Other income | 38 | 35 | 8 |
| Interest | 27 | 43 | -37 |
| Gross Profit | 465 | 238 | 95 |
| Depreciation | 68 | 64 | 7 |
| **PBT** | **397** | **175** | **127** |
| Tax | -119 | -50 | 138 |
| **Adjusted PAT** | **278** | **124** | **123** |
| extraordinary items | 0 | 8 | -100 |
| Reported PAT | 278 | 133 | 110 |
| **EPS Rs** | **5.7** | **2.5** | |
| Excise rate (%) | 8.9 | 9.4 | |
| **EBITDA (%)** | **13.1** | **9.4** | |
| RM costs to sales (%) | 69.4 | 71.4 | |
| Other exp to sales (%) | 9.5 | 11.2 | |
| Tax rate (%) | -30 | -29 | |

*Source: Company*

## Strong revenue growth driven by engines

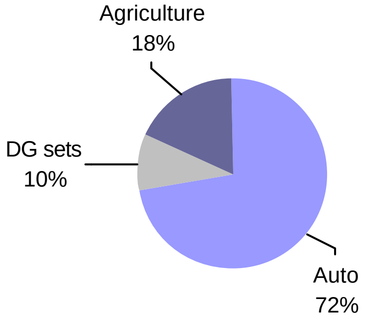
- For the quarter, net revenue grew 32% yoy driven mainly by the engines and infrastructure segment.
- The company is the sole supplier of light diesel engines to OEMs like Piaggio and Atul Auto. Piaggio is the prime client. For the quarter, 3W volumes for the company's client OEMs were up 22% yoy.
- The company is thus a play on the 3W segment (passenger and cargo) which in turn is driven by rising urbanization and usage of light cargo vehicles for intra-city transportation.
- In the infrastructure equipment segment, the company makes concrete mixers and pavers. This segment is driven by the construction and road building activity and has been on a cyclical revival.

**Segment Revenues**

| (Rs mn) | Q4FY10 | Q4FY09 | YoY (%) | FY09 | FY10E | YoY (%) |
|---|---|---|---|---|---|---|
| Engines | 2956 | 2055 | 44 | 8679 | 11441 | -24 |
| Infrastructure | 377 | 235 | 61 | 1264 | 1469 | -14 |
| Others | 144 | 103 | 40 | 466 | 563 | -17 |
| **Total** | **3477** | **2393** | **45** | **10408** | **13472** | **-23** |

*Source: Company*

**Application-wise revenue mix in engines**




*Source: Company*

**Market Shares**

| (%) | Concrete Pump | Batching plant | Concrete mixer |
|---|---|---|---|
| Stetter | 38 | 55 | 69 |
| Greaves | 11 | 3 | 22 |
| Aquarius | 26 | 5 | 0 |
| Sany | 16 | 0 | 0 |

*Source: Company*

## EBITDA margins declined sequentially

- For the quarter, EBITDA margins declined 320 bps on a sequential basis mainly due to the combined impact of higher employee costs and increase in excise duty. Material costs were under control.
- Staff costs rose 31% on a sequential basis and was the main reason for decline in margin on a sequential basis.
- Infrastructure segment reported decline in loss on higher revenues. This segment bore the brunt of credit crisis as demand fell off the cliff. The segment is still well below the peak revenue clocked in FY08. However, we expect strong growth in FY11 led by ongoing road building and infrastructure activity. We expect the segment to turnaround in FY11 with some marginal profits.

**PBIT margins**

| (%) | Q4 FY10 | Q4 FY09 | Q3 FY10 | Q2 FY10 | FY10 | FY09 |
|---|---|---|---|---|---|---|
| Engines | 17.1 | 13.2 | 19.6 | 20.8 | 19.0 | 14.7 |
| Infrastructure | -3.0 | 48.9 | -2.7 | -6.0 | -4.5 | -4.1 |
| Others | 26.6 | | 31.3 | 22.5 | 26.6 | 19.8 |
| **Total** | **15.3** | **16.8** | **17.3** | **18.1** | **16.7** | **12.7** |

*Source: Company*

## Return ratios have improved in FY10

Capital employed across engines as well as infrastructure segment has remained stable despite the robust increase in revenues indicating that working capital cycle has remained under control. We expect robust cash generation in FY10. Interest cost has been on a secular decline for the year.

**Segment Capital Employed**

| (Rs mn) | FY10 | FY09 |
|---|---|---|
| Engines | 2,821 | 2,793 |
| Infrastructure | 762 | 807 |
| Others | 13 | (33) |
| **Total** | **3,595** | **3,567** |

*Source: Company*

## Valuation

- GCL has changed its accounting year from June to March thus FY11 will be a truncated fiscal with 9M numbers. We have accordingly presented annual numbers as per revised format.

**We recommend BUY on Greaves Cotton a price target of Rs.421**

- GCL is currently trading at 11x FY12 earnings (Since FY11 has only 9M and is not comparable). The stock is trading at 6.4x FY12 EV/EBITDA basis.
- We maintain **BUY** on the stock with a DCF based price target of Rs 421.

**RESULT UPDATE**

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# CUMMINS INDIA LTD

**PRICE: RS.657** **RECOMMENDATION: REDUCE**

**TARGET PRICE: RS.620** **FY11E P/E: 21.6X**

- **CIL reported revenues ahead of our expectation; significant expansion in operating margins helped exceeding profit estimates.**
- **Revenues are up by 45% YoY growth mainly on account of engine business that grew 45%YoY in revenue terms mainly due to meaningful recovery in automotive as well as industrial segment.**
- **EBITDA margins improved significantly to 21.3% due to higher revenues and effective cost control measures undertaken leading to improved efficiency, lower manpower cost and prolific six sigma drive.**
- **Outlook for the revenue growth in FY11E has improved driven by robust outlook for domestic market, which currently contributes 80-85% of revenues. Exports revenues are likely to post recovery going forward on account of lower base in FY10 when majority of it were eroded due to holdup in the economic recovery in the US and European markets.**
- **We expect that company would maintain its dominant position in the domestic market, registering a revenue growth of 31% in FY11E mainly driven by tremendous up tick in revenues from domestic sales along with recovery in the exports segment against a weaken base of FY10.**
- **We expect traction in both power and industrial segments; growth in infrastructure space coupled with increasing capex from corporate India would drive the revenue growth for FY11E.**
- **While we tweak upward our estimates accounting for the favouable macro environment for the business reflected by Q1FY11 results, we continue to maintain reduce in view of fair valuations and downside to our target price of Rs 620 (Rs.580 earlier).**

**Summary table - Consolidated**

| (Rs mn) | FY09 | FY10 | FY11E |
|---|---|---|---|
| Sales | 35,285 | 31,260 | 40,907 |
| Growth (%) | 33 | -11 | 31 |
| EBITDA | 6,001 | 6,207 | 8,036 |
| EBITDA margin (%) | 17 | 20 | 20 |
| Net profit | 4,257 | 4,804 | 6,022 |
| Net cash (debt) | 1,739 | 1,739 | 1,739 |
| EPS (Rs) | 21.5 | 24.3 | 30.4 |
| Growth (%) | 42.5 | 3.8 | 25.3 |
| CEPS | 25.8 | 26.2 | 32.6 |
| DPS (Rs) | 9.0 | 9.0 | 9.0 |
| ROE (%) | 34.0 | 29.7 | 30.9 |
| ROCE % | 43.4 | 39.4 | 42.4 |
| EV/Sales (x) | 3.6 | 4.0 | 3.0 |
| EV/EBITDA (x) | 20.9 | 19.9 | 15.2 |
| P/E (x) | 29.3 | 27.1 | 21.6 |
| P/Cash Earnings | 25.5 | 25.0 | 20.1 |
| P/BV (x) | 8.8 | 7.4 | 6.1 |

*Source: Company, Kotak Securities - Private Client Research*

**Quarterly performance**

| (Rs mn) | Q1FY11 | Q1FY10 | YoY (%) |
|---|---|---|---|
| **Net Sales / Income from Operations** | **9,279** | **6,398** | **45** |
| Other Income | 97 | 166 | -42 |
| **Total Income** | **9,376** | **6,564** | **43** |
| Purchase of traded goods | 266 | 167 | |
| Consumption of Raw Materials | 5,460 | 3,849 | 42 |
| Staff Cost | 530 | 514 | 3 |
| Other Expenditure | 1,049 | 694 | 51 |
| Operating Expenditures | 7,305 | 5,223 | 40 |
| **PBDIT** | **1,975** | **1,175** | **68** |
| Interest & Finance Charges | 4 | 6 | -32 |
| Depreciation | 93 | 89 | 5 |
| **Profit / (Loss) before tax** | **1,974** | **1,246** | **58** |
| Tax provision | 572 | 350 | 64 |
| **Profit / (Loss) after tax** | **1,402** | **897** | **56** |
| **EPS** | **7.08** | **4.53** | **56** |
| OPM (%) | 21.3 | 18.4 | |
| Raw material cost to sales (%) | 58.8 | 60.2 | |
| Tax rate (%) | 29.0 | 28.1 | |

*Source: Company*

- Revenues grew by 45% YoY to Rs 9.3 bn in Q1FY11 mainly driven by engine business that grew by 45%YoY in revenue terms mainly due to meaningful recovery in automotive as well as industrial segment.
- Lately in addition to the power generation segment that accounts for approximately 50% of the company's revenue, stroke in domestic IT, Telecom and manufacturing sectors have widened the scope for company's operations.

- For FY11E we expect a sustainable thrust in the growth momentum on account of strong performance in the power generation and industrial segment backed with increasing spending on infrastructure projects and considerable improvement in capital expenditure by the corporate India.
- We believe that higher productivity, implementation of various cost rationalization measures across the board and focused six sigma implementation drive resulted in margin expansion for the company. EBITDA% for the quarter stood at 21.3% vis-à-vis 18.4% in Q1FY10.
- We opine that a proportion of margin improvement is also attributed to the fact that the company took a price increase in its product prices before commodity prices had gone down last year which was not rolled back later.
- Going forward, despite raw material prices that are likely to move up, we are positive on the margin outlook given management's efficient cost control measures and ongoing initiatives related to six sigma implementation.
- Company has managed to grow without increasing the cost overheads reflected by just a 3% YoY growth in the staff cost.
- While improved efficiency and optimum utilization of resources led to increased operating profits, muted financial and depreciation charges resulted in a 56% YoY PAT growth at Rs 1402 mn in Q1FY11.

## Power Generation Business offers immense growth on account of mandatory emission norms compliance gaining ground coupled with immense thrust for power back up by sectors such as Telecom, Commercial construction, IT, ITES, Retail etc.

- The company comprehends a sharp recovery in power generation business and expects the resurrection of USD 15 bn market size (before economic meltdown in FY08) going forward given the enormous demand stimulated by sectors such as Telecom, Commercial construction, IT, ITES, Retail etc.
- Moreover, company has reiterated its positive outlook for the segment from long term perspective mainly driven by 1) implementation of stringent emission norms inducing demand for Tier II emission compliant power generators 2) increasing cost of power increases viability for alternate sources of power 3) tremendous potential demonstrated by Indian infrastructure development programme.
- The management expects to maintain its dominant market presence in higher KV (600KV+) segment that accounts for nearly 60% of segment sales composition. Demand for these products remains strong and we expect that Cummins has an inherent advantage by having a local manufacturing capability over its peer group which is mainly dominated by multinational corporations.
- CIL has been constantly deploying capacity in sub KV (125KV-600KV) segment where competition is mainly established by local manufacturers. We expect that the company would sustain the pricing premium over domestic peer group, given its strong brand perception and superior value proposition offerings in terms of product quality, compliant with laid emission norms and superior post sales services to the end users.

## Industrial segment is expected to grow substantially in FY11E; driven by demand stimulation by construction, mining and railway space.

- We expect the segment to grow by 25% in FY11E on account of sustained investments in infrastructure projects propelling demand for efficient earth moving and other equipment determining future prospects for company's products.
- We also believe that the massive investments in road construction activity with increasing interest of global OEMs in the Indian market auger well for company's 130-150 HP engines due to probable increase in the market potential for 20T/21T class excavators by the construction sector and 450 CFM portable compressor market.

- Though high pressure water well market lacks activity, mining sector is likely to register resilience in demand for Parts & ReCon engine manufactured by the Company. We expect that impetus would continue to persist in strengthening of railway infrastructure giving boost to demand for 500 KVA generator sets and 40-50 liter engine sets.
- Recent developments indicate emphasis on vertical integration by the major OEMs adding to their in house manufacturing capacity for the critical components including few products that are manufactured by companies like CIL.
- From the technical view point and in accordance with the regulatory perspective, we opine that given the technological edge provided by company's long standing position in the industry with constant emphasis on enhancing product quality through various R&D initiatives would act as a key differentiator for the company's products.

## Capacity expansion at Phaltan

- CIL is getting ready to establish another incremental capacity of 60,000 of 5.9 litre. engines (mainly used in medium to heavy trucks) and this facility should be in place by roughly October-December quarter of next year
- The company is also contemplating setting up a rebuild center for complete overhaul, repairs, and upgrades for engines.
- Aside from that, CIL is also investing in a reconditioning operation, that of engines, generators as well as components, engine components.

## Earnings Outlook

- We tweak upward our estimates accounting for the favouable macro environment for the business reflected by Q1FY11 results
- Our earnings outlook has improved in view of the recovery in domestic market. Export sales should report high growth in FY11E albeit on a low base as the global economy is also on a recovery path.
- We project a 31% growth in revenues in FY11E mainly driven by growth in domestic market. The table below highlights the changes we have now build in our earnings forecast.

**FY11E Estimates**

| (mn) | Old | New | Change (%) |
|---|---|---|---|
| Revenues | 39,428 | 40,907 | 3.8 |
| EBITDA | 7,573 | 8,036 | 6.1 |
| PAT | 5,695 | 6,022 | 5.7 |
| EPS (Rs) | 28.8 | 30.4 | 5.7 |

*Source: Kotak Securities - Private Client Research*

## Valuation

- Cummins is trading at 21.6x FY11E earnings. The stock has traded in a PE band of 8x to 20x one year forward earnings with the average PE of 15x.

**We recommend REDUCE on Cummins India with a revised price target of Rs.620**

- In view of the significant earnings revision effected by us and the improved growth outlook, we have arrived at a price target of Rs 620 based on DCF.
- On an EV/EBITDA basis, the stock is trading at 15.2x FY11E.
- We recommend reducing positions in view of rich valuations relative to the sector and broad market.

**RESULT UPDATE**

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# AIA ENGINEERING LTD. (AIA)

**PRICE: RS.352** **RECOMMENDATION: ACCUMULATE**
**TARGET PRICE: RS.375** **CONS. FY11E P/E: 15.6X**

- **AIA reported Q1FY11 results which are marginally below our estimates on profitability front**
- **Export of mill internals for mining segment doubles on QoQ basis to 9000 MT**
- **Operating margin expected to improve going forward as it has passed on rise in its raw material prices**
- **Maintain FY11 earning estimates with EPS of Rs.22.5**
- **Stock down 11% since our SELL recommendation at Rs.396 on 23rd June 2010**
- **Due to 6% upside potential we upgrade AIA from SELL to ACCUMULATE with revised price target of Rs.375 (Rs.340 earlier)**

**Cons. summary table - FV Rs.2**

| (Rs mn) | FY09 | FY10 | FY11E |
|---|---|---|---|
| Revenues | 10,233 | 9,497 | 12,735 |
| Growth (%) | 48.0 | (7.2) | 34.1 |
| EBITDA | 2,467 | 2,289 | 2,940 |
| EBITDA margin (%) | 24.1 | 24.1 | 23.1 |
| Net profit | 1,736 | 1,707 | 2,126 |
| Net debt | (2,146) | (2,011) | (2,099) |
| EPS (Rs) | 18.4 | 18.1 | 22.5 |
| Growth (%) | 30.3 | (1.6) | 24.5 |
| DPS (Rs) | 1.5 | 2.5 | 3.0 |
| ROE (%) | 22.5 | 18.9 | 21.4 |
| ROCE (%) | 30.8 | 26.2 | 30.1 |
| EV/Sales (x) | 3.0 | 3.3 | 2.4 |
| EV/EBITDA (x) | 12.6 | 13.6 | 10.6 |
| P/E (x) | 19.1 | 19.4 | 15.6 |
| P/CEPS (x) | 17.1 | 17.2 | 13.9 |
| P/BV (x) | 4.3 | 3.7 | 3.1 |

*Source: Company, Kotak Securities - Private Client Research*

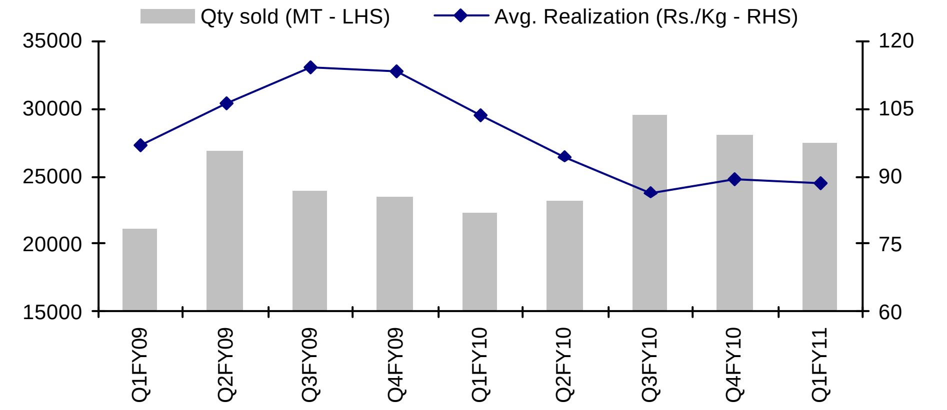
**Consolidated performance - AIA**

| (Rs mn) | Q1FY11 | Q1FY10 | YoY (%) | Q4FY10 | QoQ (%) |
|---|---|---|---|---|---|
| **Net Sales** | **2,425** | **2,267** | **7.0** | **2,501** | **(3.0)** |
| Inc/dec in stock | (180) | 220 | (181.9) | 109 | - |
| Raw materials | 1,416 | 685 | 106.7 | 1,347 | 5.1 |
| Staff cost | 117 | 100 | 17.6 | 122 | (4.0) |
| Other exp. | 580 | 699 | (17.0) | 440 | 31.8 |
| **Total exp.** | **1,933** | **1,704** | **13.5** | **2,018** | **(4.2)** |
| **EBIDTA** | **492** | **563** | **(12.6)** | **483** | **1.9** |
| Other income | 107 | 87 | 23.0 | 82 | 31.0 |
| Depreciation | 57 | 58 | (1.9) | 57 | 0.3 |
| **EBIT** | **543** | **593** | **(8.4)** | **508** | **6.7** |
| Interest | 2 | 9 | (82.4) | 2 | (8.9) |
| **PBT** | **541** | **583** | **(7.2)** | **507** | **6.8** |
| Extraord loss/ (gain) | - | - | - | - | - |
| Tax & deferred tax | 141 | 176 | (19.8) | 115 | 22.8 |
| **PAT** | **400** | **407** | **(1.8)** | **392** | **2.1** |
| Minority Interest | 2 | 1 | 95.9 | 1 | 87.5 |
| **NPAT** | **398** | **406** | **(2.0)** | **391** | **1.9** |
| Equity shares o/s (mn) | 94.3 | 94.3 | | 94.3 | |
| FV Rs.2 | | | | | |
| **Ratios** | | | | | |
| **Operating profit margin (%)** | **20.3** | **24.8** | **-6.1%** | **19.3** | **+100 bps** |
| Raw Materials / Sales (%) | 51.0 | 39.9 | | 58.2 | |
| Staff cost / Sales (%) | 4.8 | 4.4 | | 4.9 | |
| Other Exp. / Sales (%) | 23.9 | 30.8 | | 17.6 | |
| **EPS (Rs)** | **4.2** | **4.3** | | **4.1** | |
| CEPS (Rs) | 4.8 | 4.9 | | 4.7 | |
| Tax / PBT (%) | 26.1 | 30.1 | | 22.7 | |
| Qty Produced (MT) | 28129 | 22619 | 24.4 | 28500 | (1.3) |
| **Qty Sold (MT)** | **27400** | **22300** | **22.9** | **28000** | **(2.1)** |
| Avg. Realisations (Rs/kg) | 88.5 | 101.6 | (12.9) | 89.3 | (0.9) |

*Source: Company, Kotak Securities - Private Client Research*

- The company produced 28129 MT of mill internals in Q1FY11, up 24.4% on YoY basis and it sold 27400 MT in Q1FY10, up 22.9% on YoY basis. The growth is on account of sale of 9000 MT of mill internals for the mining segment.
- The export of mill internals for mining segment has doubled on sequential basis to 9000 MT in Q1FY11. Out of 9000 MT ~40% is for iron ore, 30% is for platinum, 17% is for copper and gold and balance is for other mines.
- The average realizations are down 12.9% on YoY basis to Rs.88.5 per kg. This was due to combination of higher raw material prices and change in product mix in favour of mill internals for the mining segment which typically enjoy lower average realizations then mill internals for the cement segment.
- In Q1FY11, the company reported revenues of Rs.2.4 bn, up 4.8% YoY and down 3.0% on sequential basis. Exports contributed 62.9% of total revenues.
- The operating margins were down sharply by 610 basis points on YoY basis to 20.3% primarily due to rise in the prices of its key raw material i.e. Ferro chrome which the company was unable to pass on to its customers. This is well supported by the fact that the raw materials to sales ratio increased sharply from 39.1% in Q1FY10 to 51.0% in Q1FY11.
- The company has taken hit due to rupee appreciation against US dollar and Euro. Euro account for ~30% of its export realizations. The company has also provided for forex derivative loss of Rs.37 mn, which is recorded in other expenditure. As of 30th June 2010 the mark to market forex derivative loss stands at Rs.290 mn.
- EBIDTA for Q1FY11 was at Rs.492 mn down 19.4% YoY and up 1.9% on sequential basis.
- PBT for Q1FY11 was at Rs.541 down 7.2% YoY and up 6.8% on sequential basis.
- PAT for the Q1FY11 was at Rs.398 mn down 2.0% YoY and up1.9% on sequential basis thereby translating into quarterly EPS of Rs.4.2 and CEPS of Rs.4.8.

**Quantity Sold & Avg. Realizations**

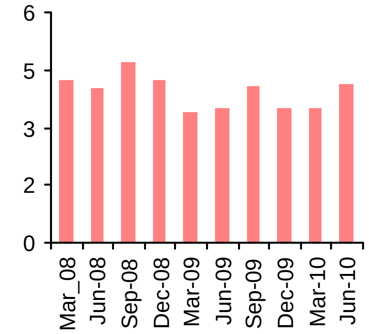



*Source: Company, Kotak Securities - Private Client Research*

## Capacity expansion

During FY09 the company has successfully expanded its capacity from 65000 TPA to 165000 TPA. However looking at the potential demand for mill internals from the mining segment it had decided to further expand the production capacity by 35000 TPA to a total of 200000 TPA. This would be done at a capex of Rs.400 mn which would be fully funded through internal cash generations as it enjoys healthy cash flows. Out of this ~25000 MT has commenced commercial production in the current month and balance would be operational by December 2010.

**Order book (Rs bn)**




*Source: Company*

## Sale of mill internal for the mining segment to pick up in FY11E

The company has successfully ramped up the export of mill internals for the mining segment for iron ore, gold, copper and platinum mines. It has successfully dispatched ~3500 MT of mill internals to CVRD Vale of Brazil which is a very large mining group and this can potentially scale upto annual demand of 20000 MT. Going forward the company is hopeful of getting large orders from various large global mining groups. Considering this we expect the sale of mill internals for the mining segment to increase sharply by 100% to ~40000 MT in FY11E.

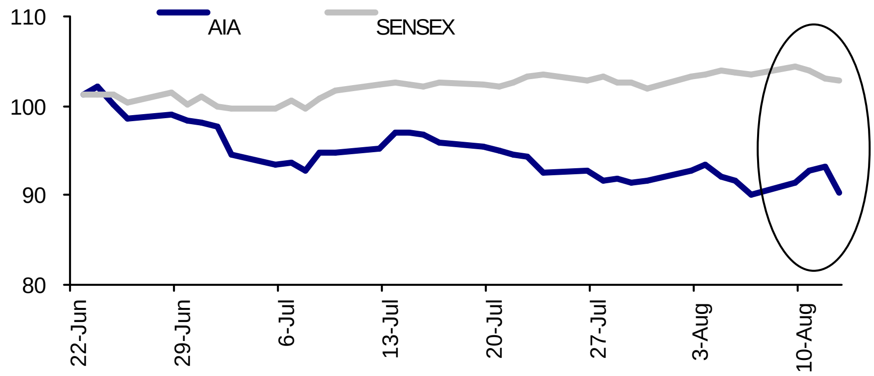
## Order book

As of 30th June 2010 the company has an order book of Rs.4.1 bn. Out of this order book, more then 95% is for the replacement demand and more then 60% of the order book is for exports. It has already got its products approved for various mines abroad and thus going forward we expect growth in the order book for the export of mill internals for the mining segment.

## Maintain earning estimates and increase price target to Rs.375

We maintain our earning estimates and expect AIA to sell 1.4 lakh MT of mill internals and report Cons. EPS of Rs.22.5 in FY11E. We have updated the balance sheet and accounted for working capital changes. The company has been successful in reducing inventories and reducing debtor days. We have valued AIA on DCF method of valuation with 13.1% WACC and 4.0% terminal growth rate (no change) based on FY11 earning estimates. Thus the price target is increased from Rs.340 to Rs.375.

**Price performance comparison**




*Source: Bloomberg*

## Valuation and recommendation

- As of 30th June 2010, AIA has net cash of Rs.3.4 bn thereby translating into cash of Rs.36 per share.
- We continue to remain positive on the medium to long term growth prospects of AIA due to strong business model with quality products, rising operating margins and expanding markets of mill internals for the mining segment.
- At the current market price of Rs.352, the stock of AIA is fairly valued at 3.1x book value, 15.6x earnings and 13.9x cash earnings based on FY11E.

**We upgrade AIA Engineering to ACCUMULATE with a revised price target of Rs.375**

- The stock of AIA is down 11% since our SELL recommendation at Rs.396 on 23rd June 2010.
- Due to 6% upside potential from the current levels we upgrade AIA from SELL to **ACCUMULATE** with revised price target of Rs.375.

**RESULT UPDATE**

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# INDRAPRASTHA GAS (IGL)

**PRICE: RS.304** **RECOMMENDATION: SELL**
**TARGET PRICE: RS.250** **FY11E P/E: 16.4X**

- **IGL reported excellent set of Q1FY11 results which are above our estimates on the profitability front**
- **CNG volumes up 17.8% YoY and PNG volumes up sharply 102.9% YoY**
- **Key concern remains in terms of expansion into other cities through bidding by PNGRB**
- **Revise FY11 earning estimates with EPS of Rs.19.1 (Rs.18.0 earlier)**
- **Stock richly valued at 8.7x EV/EBIDTA and 16.4x P/E based of FY11 earning estimates**
- **Due to 18% downside potential we continue to recommend SELL on IGL with revised price target of Rs.250 (Rs.210 earlier)**

**Summary table**

| (Rs mn) | FY09 | FY10 | FY11E |
|---|---|---|---|
| Sales | 8528 | 10781 | 17016 |
| Growth (%) | 20.8 | 26.4 | 57.8 |
| EBIDTA | 3001 | 3808 | 4922 |
| EBIDTA margin (%) | 35.2 | 35.3 | 28.9 |
| Net profit | 1725 | 2155 | 2668 |
| EPS (Rs) | 12.3 | 15.4 | 19.1 |
| Growth (%) | -1.14 | 24.95 | 23.82 |
| CEPS (Rs) | 17.1 | 20.9 | 26.1 |
| DPS (Rs) | 4.0 | 4.5 | 5.0 |
| ROE (%) | 25.2 | 28.6 | 29.0 |
| ROCE (%) | 36.5 | 40.8 | 41.1 |
| EV/Sales (x) | 5.0 | 4.0 | 2.5 |
| EV/EBIDTA (x) | 14.3 | 11.3 | 8.7 |
| P/E (x) | 25.3 | 20.3 | 16.4 |
| P/BV (x) | 6.4 | 5.3 | 4.3 |
| P/CEPS (X) | 18.2 | 14.9 | 12.0 |

*Source: Company, Kotak Securities - Private Client Research*

- Net sales for Q1FY11 were at Rs.3.4 bn up by 44.1% YoY and up 16.4% on sequential basis. Higher sales were a result of increase in volumes of both CNG and PNG and also due to price revision undertaken by IGL in June 2010.
- During the Q1FY11, IGL sold 142 mn kg of CNG thereby registering 17.8% YoY and 4.6% sequential growth. IGL sold 36 mn SCM of PNG in Q1FY11 showing strong 102.9% YoY and 42.0% sequential growth. However this includes ~10 mn SCM sold to Adani and Haryana City gas distribution for their CGD network in Faridabad and Gurgaon.
- The company recorded lower EBIDTA margin of 31.9%, which is down 460 bps on YoY and down 20 bps on QoQ basis primarily due to higher gas prices. Basically to meet its additional requirements IGL is now buying gas from RIL KG basin at $4.2 / MMBTU as against it APM gas price of $2.1 / MMBTU which is impacting the margins. However going forward the APM gas price has also been increased to $4.2 / MMBTU and simultaneously IGL has also increased the selling prices between 19 - 29% depending on location and taxes.
- The profitability of PNG segment has fallen sharply in Q1FY11 due to the fact that now IGL is supplying CNG to Adani and Haryana City gas distribution for their CGD network in Faridabad and Gurgaon at a marginal profit. Basically IGL is not doing any value addition and thus it gets only trading margins which are very low as compared to its own CGD margins.
- Other income of the company is down 70.8% on YoY basis to Rs.19 mn due to use of funds for the capex of the company to expand into adjoining areas of Delhi.
- The depreciation cost has gone up by 24.3% on YoY basis to Rs.231 mn as the company has expanded the number of stations in and around Delhi.
- PBT for Q1FY11 was at Rs.855 mn up 17.6% YoY and up 10.9% on sequential basis
- PAT for Q1FY11 was at Rs.571 mn up 18.4% YoY and up 11.0% on sequential basis thereby translating into Q1FY11 EPS of Rs.4.1 and CEPS of Rs.5.7.

**IGL - Q1FY11 Results Table**

| (Rs mn) | Q1FY11 | Q1FY10 | YoY (%) | Q4FY10 | QoQ (%) |
|---|---|---|---|---|---|
| **Net Sales** | **3,350** | **2,326** | **44.1** | **2,878** | **16.4** |
| Inc / dec in stock | (3) | (0) | 932.9 | 4 | - |
| raw materials | 1,670 | 1,041 | 60.4 | 1,378 | 21.1 |
| staff cost | 92 | 62 | 46.8 | 96 | (4.9) |
| other exp. | 524 | 373 | 40.4 | 475 | 10.4 |
| total exp. | 2,283 | 1,477 | 54.6 | 1,954 | 16.9 |
| **EBIDTA** | **1,067** | **849** | **25.7** | **925** | **15.4** |
| Other income | 19 | 64 | (70.8) | 45 | (58.4) |
| Depreciation | 231 | 186 | 24.3 | 198 | 16.5 |
| **EBIT** | **855** | **727** | **17.6** | **771** | **10.9** |
| Interest | - | - | - | - | - |
| **PBT** | **855** | **727** | **17.6** | **771** | **10.9** |
| Tax & deferred tax | 283 | 244 | 16.1 | 256 | 10.7 |
| **PAT** | **571** | **483** | **18.4** | **515** | **11.0** |
| Equity shares o/s (mn) | 140 | 140 | | 140 | |
| **Ratios** | | | | | |
| Operting profit margin (%) | 31.9 | 36.5 | -460 bps | 32.1 | -20 bps |
| **EPS (Rs)** | **4.1** | **3.4** | | **3.7** | |
| CEPS (Rs) | 5.7 | 4.8 | | 5.1 | |
| Raw Materials / Sales (%) | 49.8 | 44.7 | | 48.0 | |
| Staff cost / sales | 2.7 | 2.7 | | 3.4 | |
| Other exp / sales | 15.6 | 16.1 | | 16.5 | |
| Tax / PBT | 33.2 | 33.6 | | 33.2 | |

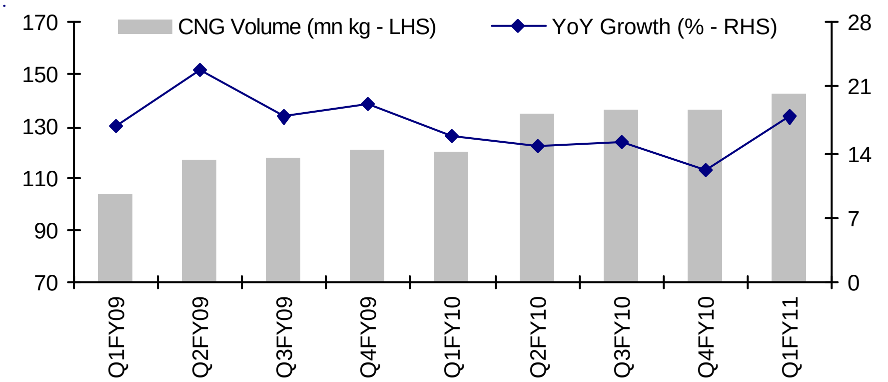
*Source: Company*

**Segmental**

| | Q1FY11 | Q1FY10 | YoY (%) | Q4FY10 | QoQ (%) |
|---|---|---|---|---|---|
| Volume performance | | | | | |
| CNG mn kg | 142 | 121 | 17.8 | 136 | 4.6 |
| PNG mn scm | 36 | 18 | 102.9 | 25 | 42.0 |
| Value (Rs. mn) | | | | | |
| CNG | 3180 | 2296 | 38.5 | 2850 | 11.6 |
| PNG | 572 | 320 | 79.1 | 390 | 46.7 |
| Average Realisations | | | | | |
| CNG (Rs./Kg) | 22.4 | 19.1 | 17.6 | 21.0 | 6.6 |
| PNG (Rs./SCM) | 16.1 | 18.3 | (11.7) | 15.6 | 3.3 |

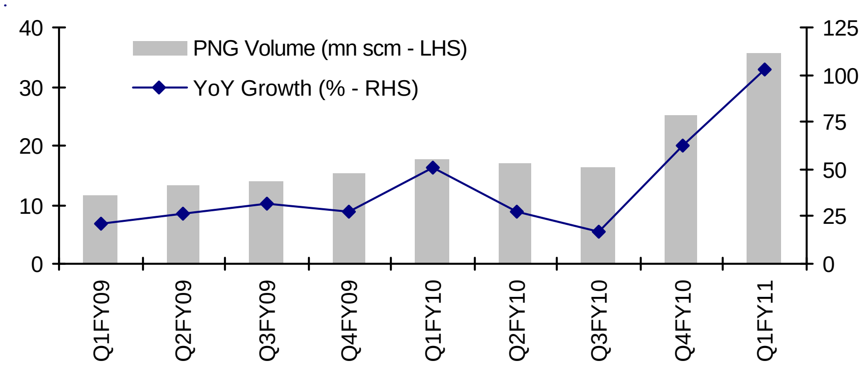
*Source: Company*

**CNG Volume and YoY growth**



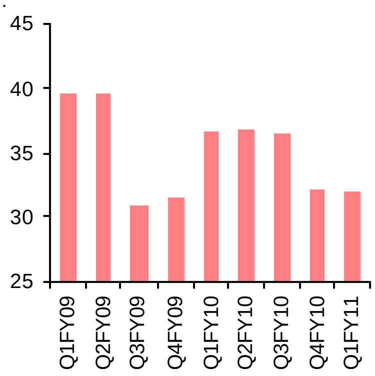

*Source: Company*

**PNG Volume and YoY growth**




*Source: Company*

**Quarterly EBIDTA margin (%)**




*Source: Company*

## IGL has increased prices of CNG in June 2010

- IGL has hiked the Compressed Natural Gas (CNG) prices by over 19% to 29% in response to the price hike of Administered Price Mechanism (APM) gas by the government.
- The CNG price in NCT of Delhi has gone up by 25.6% from Rs.21.9 per Kg to Rs.27.5 per kg. The CNG price in Noida and greater Noida in Uttar Pradesh has gone up by 29.1% from Rs.23.7 per Kg to Rs.30.6 per kg. The CNG price in Ghaziabad in Uttar Pradesh has gone up by 19.1% from Rs.25.7 per Kg to Rs.30.6 per kg.
- It has also increased the prices of PNG to Rs.16.85 per SCM upto consumption of 90 SCM in four months. For consumption greater then 90 SCM in four months the rate would be Rs.21.12 per SCM.
- The hike in the prices was primarily to cover the increase in price of natural gas from Rs.3.2 per cubic meter to Rs.7.5 per cubic meter or $4.2 per MMBTU. The price hike was necessary as IGL buys ~90% of its total requirements of natural gas at APM prices for its city gas distribution network in Delhi and adjoining areas.

## CNG still attractive despite price hikes

We feel that even after the price hikes CNG would still lead to savings of 59% in terms of running cost compared to petrol driven vehicles at the current level of prices in Delhi. While use of CNG would be 28% cheaper as compared to diesel driven vehicles. As per the management the increase in CNG prices will marginally impact the per kilometer running cost for the vehicles as for autos, the increase would be 16 paisa per km, for car and taxi it would be 27 paisa per km and in case of buses, the increase would be Rs.1.60 per km, which translates to less than 3 paisa per passenger km.

## IGL did not win any City Gas Distribution (CDG) project in first round

IGL did not get any CDG project in the first round of bidding by Petroleum Natural Gas and Regulatory Board (PNGRB). This is a major concern as going forward as any future expansion outside Delhi and its adjoining areas will be only on bidding by PNGRB. Thus its growth would be dependant on its ability to win the CGD projects. Due several players bidding we expect the margins to be under pressure which is well supported by the fact that some of the previous bids have happened at zero or NIL pipeline tariffs. Thus we need to wait and see how the bidding scenario emerges in the second round of bidding for CGD by PNGRB.

### Change in earning estimates - FY11E

| (Rs mn) | Old | Revised | % shift |
|---|---|---|---|
| Net Sales | 16593 | 17016 | 2.6 |
| EBIDTA (%) | 28.0 | 28.9 | 3.4 |
| **PAT** | **2516** | **2668** | **6.0** |
| EPS (Rs.) | 18.0 | 19.1 | 6.0 |
| CEPS (Rs.) | 25.0 | 26.1 | 4.4 |
| CNG mn SCM | 791 | 791 | - |
| PNG mn SCM | 121 | 145 | 19.7 |
| CNG (Rs./Kg) | 27.0 | 27.0 | - |
| PNG (Rs./SCM) | 20.0 | 20.0 | - |
| WACC (%) | 12.6 | 12.6 | 0.0 |
| Terminal Growth (%) | 4.0 | 4.0 | - |
| **Target Price** | **210** | **250** | **19.0** |

*Source: Kotak Securities - Private Client Research*

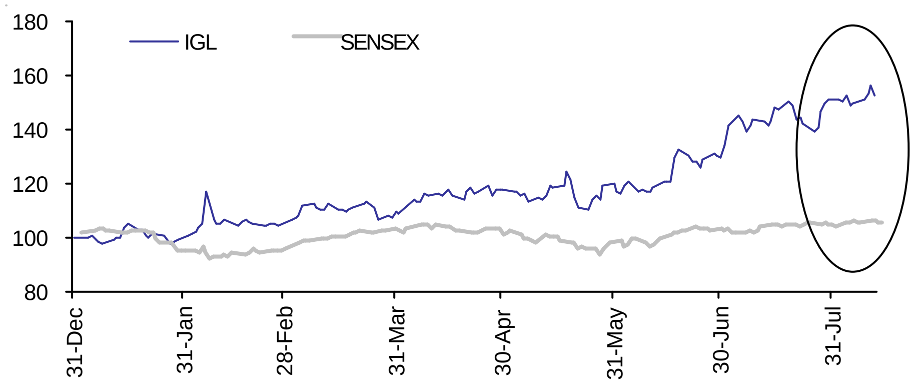
## Revise FY11 earning estimates

- We have revised our FY11 earning estimates to account for higher then expected PNG volume growth due to gas trading and higher then expected margins in both CNG and PNG segment.
- In FY11E we now expect IGL to sell 791 mn SCM of CNG (no change) at an average realization of Rs.27 per kg (no change). Also we expect IGL to sell 145 mn SCM of PNG (up 19.7%) at an average realization of Rs.20.0 per SCM (no change).
- For FY11E we now expect IGL to report revenues of Rs.17.0 bn (up 2.6%), EBIDTA margin of 28.9% (up 90 bps) and PAT of Rs.2.7 bn (up 6.0%).
- Accordingly we expect IGL to report higher EPS of Rs.19.1 and CEPS of Rs.26.1 in FY11E as against our earlier estimate of Rs.18.0 and Rs.25.0 respectively.

## Price target revised to Rs.250

We have valued IGL on DCF method of valuation with 12.6% WACC and 4.0% terminal growth rate (no change). Due to earnings revision the price target is revised from Rs.210 to Rs.250 per share for IGL. We have already accounted for the likely regulation and competition post FY11 where we have considered post tax ROCE of 14.0% i.e. pre tax ROCE of 21.2%.

**Price performance comparison**



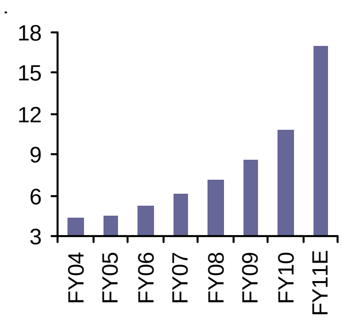

*Source: Bloomberg*

## Recommendation and Valuation

**We continue to maintain SELL on IGL with a revised price target of Rs.250**

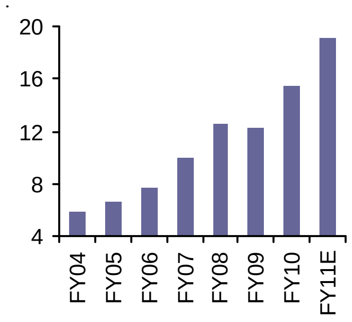
- Since January 2010 the stock of IGL has significantly outperformed the SENSEX as it has risen by 53% as against just 3% rise in SENSEX during the same period.
- At the current market price of Rs.304, the stock is richly valued at 8.7x EV/EBIDTA, 4.3x book value, 16.4x earnings and 12.0x cash earnings based on FY11E.
- Due to 18% downside potential from the current levels we continue to recommend **SELL** on IGL with revised price target of Rs.250.

**Revenues (Rs bn)**




*Source: Company, Kotak Securities - Private Client Research*

**EPS (Rs)**




*Source: Company, Kotak Securities - Private Client Research*

RESULT UPDATE

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# STATE BANK OF INDIA (SBI)

**PRICE: RS.2784** **RECOMMENDATION: ACCUMULATE**
**TARGET PRICE: RS.2762** **FY11E P/E: 16.0X; P/ABV: 2.7X**

## We recommend ACCUMULATE with every decline....

**Q1FY11: Stellar performance on core operating front; however, higher slippage (Rs.40.8 bn) than the average run rate of ~Rs.25 bn during last two quarters, is slight negative. Downgrading SBI to ACCUMULATE from BUY earlier with recent spike in its stock price...**

- **SBI reported strong growth in its net interest income (45.4%) buoyed by 88 bps (YoY) improvement in margins along with strong growth in its loan book (20.7% YoY). Its net profit grew 25.1% on back of robust growth in its core business along with marginal decline in opex (decline of 1.2%) despite muted non-interest income (growth of only 3.4%) and sharp rise in provisions and contingencies (Rs.15.51 bn in Q1FY11 as against Rs.1.73 bn in Q1FY10).**
- **Higher loan growth vis-à-vis deposit growth has enhanced the domestic C/D ratio from 64.8% at the end of Q1FY10 to 74.9% at the end of Q1FY11. However, it still holds Rs.280.8 bn of excess liquidity which earns negative carry (1.83% i.e. Rs.1.28 bn during Q1FY11), although, this is down from the peak of Rs.970.5 bn during Q1FY10.**
- **NIM of the bank bottomed out in Q1FY10 and since then it has been witnessing consistent improvement. It improved to 3.18% in Q1FY11 as against 2.96% in Q4FY10, 2.82% in Q3FY10, 2.55% in Q2FY10 and 2.30% in Q1FY10. We are factoring in ~2.95% NIM during FY11-12E.**
- **Slippage during Q1FY11 (Rs.40.8 bn) was higher than the average run rate of ~Rs.25 bn witnessed during last two quarters. Sequentially, gross NPA and net NPA rose marginally at 6.6% and 1.9%, respectively. Its PCR (provision coverage ratio) including AUCA stands at 60.7% at the end of Q1FY11. Management has also indicated that they have received extension from RBI to reach 70% provision coverage mark by Q2FY12, positive for the stock, as excess provision could be spread over next 5 quarters with lesser impact on its near term earnings.**
- **We have slightly tweaked our earning estimates for FY11E and FY12E. We are revising the target price upward to Rs.2762 (Rs.2470 earlier); however, we downgrade the stock to ACCUMULATE from BUY earlier with the recent spike in its stock price. Our fair value estimate is based on SOTP methodology where core business is valued at Rs.2027 (2.0x FY11E ABV) and subsidiaries are valued at Rs.735 (after giving 20% holding company discount).**

## Stellar performance on core operating front

SBI reported strong growth in its net interest income (45.4%) to Rs.73.0 bn in Q1FY11 from 50.2 bn in Q1FY10 buoyed by 88 bps (YoY) improvement in margins along with strong growth in its loan book (20.7% YoY).

Its net profit grew 25.1% to Rs.29.1 bn in Q1FY11 (vs. Rs.23.3 bn in Q1FY10) on back of robust growth in its core business along with marginal decline in operating expenses (decline of 1.2%) despite muted non-interest income (growth of only 3.4%) and sharp rise in provisions and contingencies (Rs.15.51 bn in Q1FY11 as against Rs.1.73 bn in Q1FY10).

**Result Performance**

| (Rs bn) | Q1FY11 | Q1FY10 | YoY (%) |
|---|---|---|---|
| Interest on advances | 134.2 | 123.6 | 8.6 |
| Interest on Investment | 44.7 | 43.4 | 3.1 |
| Interest on RBI/ banks' balances | 1.4 | 6.5 | -78.8 |
| Other interest | 4.2 | 1.3 | 228.0 |
| **Total interest earned** | **184.5** | **174.7** | **5.6** |
| Interest expense | 111.5 | 124.5 | -10.4 |
| **Net interest income** | **73.0** | **50.2** | **45.4** |
| Other Income | 36.9 | 35.7 | 3.4 |
| **Net Revenue (NII + Other income)** | **109.9** | **85.9** | **27.9** |
| Total Operating Expenses | 48.6 | 49.2 | -1.2 |
| Payments to / Provisions for employees | 30.7 | 34.1 | -9.9 |
| Other operating expenses | 17.9 | 15.1 | 18.4 |
| **Operating profit** | **61.3** | **36.7** | **67.0** |
| Provisions & contingencies | 15.5 | 1.7 | 798.1 |
| Provision for taxes | 16.7 | 11.7 | 42.5 |
| **Net profit** | **29.1** | **23.3** | **25.1** |
| **EPS (Rs)** | **45.90** | **36.71** | **25.0** |

*Source: Company*

## Moderate business growth due to conscious strategy of lower deposit growth

Total business of the bank increased moderately at 12.6% to Rs.14791.3 bn at the end of Q1FY11 from Rs.13133.6 bn at the end of Q1FY10.

- Deposits rose at a modest pace (6.8% YoY) to Rs.8153.0 bn at the end of Q1FY11 from Rs.7635.6 bn at the end of Q1FY10. Its CASA mix improved from 38.45% at the end of Q1FY10 to 47.51% at the end of Q1FY11 on back of strong traction in saving deposits (33.8% growth YoY) and healthy growth in current account float (12.5% growth YoY) along with conscious strategy of running down term deposits (decline of 5.8% YoY). Its bulk deposit has further declined to 1.36% at the end of Q1FY11 as against 3.0% at the end of Q1FY10 and 10.74% at the end of Q4FY09.
- Gross advances grew 20.7% (YoY) to Rs.6638.3 bn at the end of Q1FY11 from Rs.5498.0 bn at the end of Q1FY10 on back of strong growth in retail book (39.6%), large corporate book (34.7%) and International banking (22.1%). The share of retail book increased from 19.95% at the end of Q1FY10 to 23.74% at the end of Q1FY11.

Higher loan growth vis-à-vis deposit growth has enhanced the domestic C/D ratio from 64.8% at the end of Q1FY10 to 74.9% at the end of Q1FY11. However, it still holds Rs.280.8 bn of excess liquidity which earns negative carry (1.83% i.e. Rs.1.28 bn during Q1FY11), although, this is down from the peak of Rs.970.5 bn during Q1FY10.

## Muted non-interest income on back of lower trading profit

Non-interest income was muted (growth of 3.4%) at Rs.36.9 bn during Q1FY11 as against Rs.35.7 bn during Q1FY10 on back of 75.5% decline in trading profit (Rs.1.73 bn in Q1FY11 as compared to Rs.7.1 bn in Q1FY10).

However, core fee income (C/E/B & Forex) delivered strong growth of 24.9% (YoY) from Rs.23.3 bn in Q1FY10 to Rs.29.1 bn in Q1FY11.

**Trend in non-interest income**

| (Rs bn) | 1QFY10 | 2QFY10 | 3QFY10 | 4QFY10 | 1QFY11 | YoY gth (%) |
|---|---|---|---|---|---|---|
| Commission, Exchange & Brokerage | 18.6 | 21.0 | 21.9 | 34.9 | 24.1 | 29.4 |
| Profit on sale of Investment | 7.1 | 5.5 | 4.4 | 4.3 | 1.7 | -75.5 |
| Forex Income | 4.7 | 5.2 | 4.0 | 1.9 | 5.0 | 6.8 |
| Dividend | 3.6 | 1.7 | 0.0 | 0.5 | 3.8 | 5.3 |
| Income from Leasing | 0.1 | 0.1 | 0.0 | 0.0 | 0.0 | -87.9 |
| Others | 1.6 | 1.8 | 3.3 | 3.7 | 2.3 | 39.7 |
| **Total Non-Interest Income** | **35.7** | **35.3** | **33.7** | **45.1** | **36.9** | **3.4** |
| **Core Fee Income (C/E/B & Forex)** | **23.3** | **26.3** | **26.0** | **36.8** | **29.1** | **24.9** |

*Source: Company*

## NIM bottomed out in Q1FY10; improvement witnessed in last 4 consecutive quarters

NIM of the bank bottomed out in Q1FY10 and since then it has been witnessing consistent improvement. It improved to 3.18% in Q1FY11 as against 2.96% in Q4FY10, 2.82% in Q3FY10, 2.55% in Q2FY10 and 2.30% in Q1FY10. We are factoring in ~2.95% NIM during FY11-12E.

This has come on the back of improvement in CASA mix from 38.45% at the end of Q1FY10 to 47.51% at the end of Q1FY11. The improvement in CASA has come on the back of strong traction in saving deposits (33.8% growth YoY) and healthy growth in current account float (12.5% growth YoY) along with conscious strategy of running down term deposits (decline of 5.8% YoY).

The improvement in margin is also due to decline in excess liquidity which earns negative carry along with re-pricing of high cost deposits. This excess liquidity has come down from Rs.970.5 bn during Q1FY10 to Rs.280.8 bn during Q1FY11. (Q2FY10: Rs.839.9 bn, Q3FY10: Rs.677.8 bn, Q4FY10: Rs.441.0 bn) leading to decline in the negative carry. Its negative carry has also come down from 3.34% during Q1FY10 to 1.83% during Q1FY11.

Management has also guided that Rs.170 bn of high cost deposits (having cost of 10%+) would come for re-pricing in next three quarters which in turn would provide kicker to the margins, going forward. We are factoring in NIM of 2.94% and 2.98% for FY11E and FY12E, respectively.

## Slippage higher than the average run rate of last two quarters; extension till Q2FY12 to meet 70% provision coverage is positive for the near term earnings of the bank

Slippage during Q1FY11 (Rs.40.8 bn) was higher than the average run rate of ~Rs.25 bn witnessed during last two quarters.

**NPA Movement**

| (Rs bn) | Q1FY11 | Q4FY10 | Q3FY10 |
|---|---|---|---|
| Opening Balance | 195.35 | 188.61 | 173.76 |
| **Slippage** | **40.81** | **25.04** | **26.21** |
| Reduction | 27.91 | 18.30 | 11.36 |
| Upgradation + Recovery | 21.64 | 10.66 | 7.90 |
| Write Off | 6.27 | 7.64 | 3.46 |
| **Closing Gross NPA** | **208.25** | **195.35** | **188.61** |
| Increase in Gross NPA | 12.90 | 6.74 | 14.85 |
| **Slippage ratio (%)** | **2.5** | **1.8** | **1.9** |

*Source: Company*

Sequentially, gross NPA and net NPA rose marginally at 6.6% and 1.9%, respectively. In percentage terms, gross NPA slightly deteriorated from 3.05% at the end of Q4FY10 to 3.14% at the end of Q1FY11. At the same time, net NPA improved from 1.72% at the end of Q4FY10 to 1.70% at the end of Q1FY11.

**Trend in NPAs**

| (Rs bn) | 1QFY10 | 2QFY10 | 3QFY10 | 4QFY10 | 1QFY11 | Growth YoY (%) | Growth QoQ (%) |
|---|---|---|---|---|---|---|---|
| Gross NPA | 153.18 | 173.76 | 188.61 | 195.35 | 208.25 | 36.0 | 6.6 |
| Gross (%) | 2.79 | 2.99 | 3.11 | 3.05 | 3.14 | | |
| Net NPA | 84.02 | 99.27 | 112.71 | 108.70 | 110.74 | 31.8 | 1.9 |
| Net (%) | 1.55 | 1.73 | 1.88 | 1.72 | 1.70 | | |

*Source: Company*

Its PCR (provision coverage ratio) including AUCA stands at 60.7% at the end of Q1FY11. Management has also indicated about the extension from RBI to reach 70% provision coverage mark by Q2FY12. We believe this would be positive for the stock, as excess provisions (~Rs.28 bn) could be spread over next 5 quarters with lesser impact on its near term earnings.

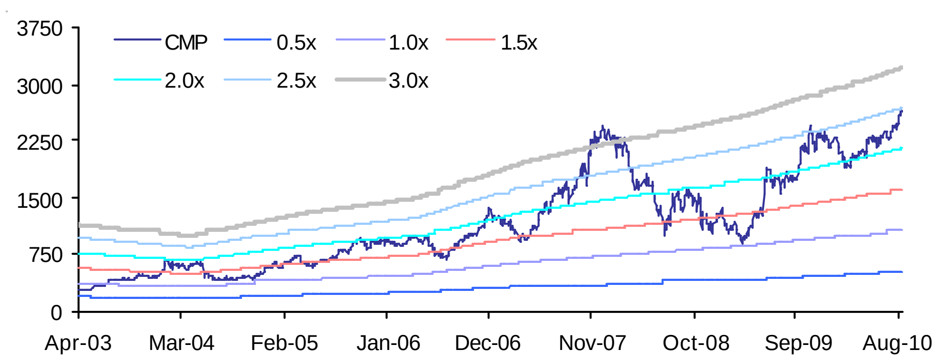
## Valuation & Recommendation

**We recommend ACCUMULATE on SBI with a price target of Rs.2762**

We have slightly tweaked our earning estimates for FY11E and FY12E and expect net profit for FY11E and FY12E to be Rs.110.55 bn and 141.85 bn, respectively.

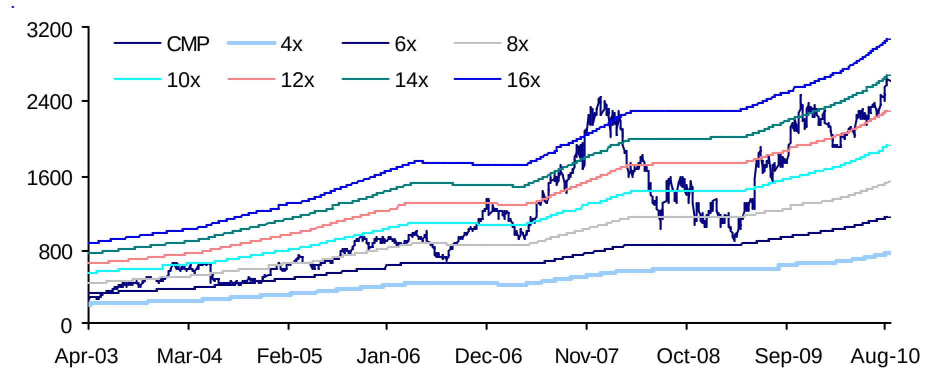
This would result into an EPS of Rs.174.1 and Rs.223.4 for FY11E and FY12E, respectively. Adjusted book value for FY11E and FY12E is estimated to be Rs.1013.4 and Rs.1172.5, respectively.

**Rolling 1-year forward P/ABV band**




*Source: Company, Kotak Securities - Private Client Research*

**Rolling 1-year forward P/E band**




*Source: Company, Kotak Securities - Private Client Research*

At current market price of Rs.2784, stock is trading at 2.0x its FY11E adjusted book value and 11.8x its FY11E earnings, after stripping the value of its subsidiaries.

We are revising the target price upward to Rs.2762 (Rs.2470 earlier). However, we downgrade the stock to **ACCUMULATE** from BUY earlier with the recent spike in its stock price. Our fair value estimate is based on SOTP methodology where core business is valued at Rs.2027 (2.0x FY11E ABV) and subsidiaries are valued at Rs.735 (after giving 20% holding company discount).

We advise our clients to **ACCUMULATE** this stock with every decline...

## Sum of Parts Valuation

| | Basis | Multiple | Year | Value per Share |
|---|---|---|---|---|
| Core Banking Business (standalone) | ABV | 2.00 | FY11 | 2,027 |
| Associate Banks | ABV | 2.00 | FY11 | 599 |
| Life Insurance Business | NBAP | 16 | FY11 | 202 |
| SBI Capital Market | P/E | 10 | FY11 | 24 |
| Asset Management | AUM | 5% | FY11 | 21 |
| SBI DFHI | P/E | 6 | FY11 | 10 |
| SBI Factors | P/E | 10 | FY11 | 7 |
| SBI Cards & Payment services | P/E | 10 | FY11 | 6 |
| Other Investments (UTI MF, NSE, GTF etc) | | | | 50 |
| **Total Value of subsidiaries** | | | | **919** |
| After 20% Holding company discount | | | | 735 |
| **Total Value** | | | | **2,762** |

*Source: Kotak Securities - Private Client Research*

## Key data

| (Rs bn) | 2009 | 2010 | 2011E | 2012E |
|---|---|---|---|---|
| Interest income | 637.88 | 709.94 | 800.01 | 954.08 |
| Interest expense | 429.15 | 473.22 | 506.53 | 602.80 |
| **Net interest income** | **208.73** | **236.71** | **293.49** | **351.28** |
| Other income | 126.91 | 149.68 | 164.65 | 190.77 |
| Gross profit | 179.15 | 183.21 | 234.91 | 289.34 |
| **Net profit** | **91.21** | **91.66** | **110.55** | **141.85** |
| Gross NPA (%) | 2.8 | 3.1 | 2.8 | 2.6 |
| Net NPA (%) | 1.8 | 1.7 | 1.4 | 1.3 |
| Net interest margin (%) | 2.9 | 2.7 | 2.9 | 3.0 |
| RoE (%) | 17.1 | 14.8 | 15.7 | 17.6 |
| RoAA (%) | 1.1 | 0.9 | 1.0 | 1.1 |
| Dividend Yield (%) | 1.0 | 1.1 | 1.1 | 1.1 |
| **EPS (Rs.)** | **143.7** | **144.4** | **174.1** | **223.4** |
| Adjusted BVPS (Rs) | 762.3 | 867.5 | 1,013.4 | 1,172.5 |
| P/E (x) | 19.4 | 19.3 | 16.0 | 12.5 |
| P/ABV (x) | 3.7 | 3.2 | 2.7 | 2.4 |

*Source: Company, Kotak Securities - Private Client Research*

**MANAGEMENT MEET UPDATE**

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# GATEWAY DISTRIPARKS LTD (GDL)

**PRICE: RS.100** **RECOMMENDATION: BUY**
**TARGET PRICE: RS.122** **CONS. FY11E P/E: 12.0X**

- **Indian Railways to offer 15% rebate on freight to transport automobiles by railways**
- **No major impact on CFS operations due accident near JNPT port**
- **Cold chain business to grow with increased profitability**
- **IFC money to be used for expanding capacity by 71% to 24000 MT**
- **Pick up in economy positive for long term growth prospects**
- **Stock has underperformed broader markets**
- **Due to 22% upside potential from current levels we upgrade GDL to BUY with unchanged price target of Rs.122**

**Summary table - Cons.**

| (Rs mn) | FY09 | FY10 | FY11E |
|---|---|---|---|
| Sales | 4,629 | 5,266 | 6,583 |
| Growth (%) | 70.6 | 13.8 | 25.0 |
| EBITDA | 1,580 | 1,433 | 1,804 |
| EBITDA margin (%) | 34.1 | 27.2 | 27.4 |
| Net profit | 796 | 790 | 901 |
| Net debt | 1,417 | 1,329 | 1,872 |
| EPS (Rs) | 7.4 | 7.3 | 8.4 |
| Growth (%) | 8.2 | -0.7 | 14.0 |
| DPS (Rs) | 3.5 | 3.5 | 3.5 |
| ROE (%) | 12.8 | 12.2 | 13.4 |
| ROCE (%) | 13.7 | 10.9 | 14.7 |
| EV/Sales (x) | 2.6 | 2.3 | 1.9 |
| EV/EBITDA (x) | 7.7 | 8.5 | 7.0 |
| P/E (x) | 13.5 | 13.7 | 12.0 |
| P/CEPS (x) | 8.7 | 8.4 | 7.6 |
| P/BV (x) | 1.7 | 1.7 | 1.6 |

*Source: Company, Kotak Securities - Private Client Research*

## Indian Railways to offer rebate to private sector for transport of vehicles - long term positive for GRFL

- The Indian Railways has formulated a policy, which will allow logistics service providers like GRFL to induct special wagons on the railway network and avail of freight rebates in return. This is done to increase its share in the transportation of automobiles by 10% over next five years. The railways have already decided to set up 10 automobile hubs across the country where auto components will be assembled.
- Under the Automobile Freight Train Operator (AFTO) scheme the private players would be required to invest in inducting and operating special wagons on the Indian Railways network. In order to make it attractive as compared to road transport the private players would be offered 15% rebate on freight rates for every rake loaded. In case of high capacity wagons, for every increase in throughput of 10%, an additional 2% rebate on freight rates would also be offered.
- The rebate can be enjoyed for 20 years, or till recovery of the cost of investment, whichever is earlier. The maintenance of wagons would be undertaken by the railways at their own cost.
- AFTOs can either operate private car trains between private terminals equipped to handle the traffic or use their own sidings. They are also allowed to use the rail terminals on the Indian Railway network on payment of prescribed terminal charges.
- Globally major chunk of automobiles is transported by railways. For instance, 70% of automobile transport in US is done via railways, while it is 35% in Europe and 16% in China. On the other hand just 5% of 2 mn cars sold in India are transported by railways. Thus we see a huge opportunity in India for transportations of automobiles through railways.
- We feel this is very positive for GRFL (subsidiary of GDL) in long term as it is already operating with 21 rakes and has rail linked terminals at Delhi, Ludhiana and Mumbai. Another terminal at Faridabad is expected to be operational by December 2010.

## CFS operations unaffected at JNPT

Recently there was an accident outside JNPT port at Mumbai. Due this the traffic was disrupted at JNPT for around ~7 days. However the government has said that the port should be operational in next couple of days. In fact port has slowly started operating with limited number of ships being allowed to pass thorough with the help of Indian Navy and Coastguard. GDL operates two CFS at JNPT. We have spoken with the management and they have said that the effect would be very limited as they feel that the container cargo for Mumbai area will not be diverted to other ports as then it would lead to additional transportation costs. Since the port is likely to be fully operational by next week we do not expect any major negative impact on the CFS operations of the company.

## Cold chain business run by Snowman frozen Foods

- The cold chin business of GDL group is being run by its 53.2% subsidiary, i.e. Snowman Frozen Foods Limited (Snowman). It is a joint venture between GDL group, Mitsubishi Corporation, Mitsubishi Logistics Corporation and Nichirei Logistics Group Inc. of Japan
- The Company currently has 16 cold storage facilities with a total capacity of over 14000 MT spread across the country. Currently it operates about ~120 refrigerated trucks (reefers) in its transportation division out of which ~70 trucks are owned and rest are on contract.
- The company offers the complete and unique facilities for transportation, storage, handling, inventory management, documentation, secondary transportation and retail distribution of frozen and chilled foods.
- Snowman has the capability of providing cold chain services to the entire spectrum of products including processed foods, fast foods, seafood, meats, ice creams and pharmaceutical products apart from fruits and vegetables.
- Typically, it either builds its own facility on land obtained under a long term lease or leases existing warehouses for a long term and undertakes appropriate retrofitting to convert it into a cold storage facility.

## Business division - Refrigerated transport

- Transportation through the Snowman reefer vehicle ensures temperature reliability and prompt delivery. Snowman ensures delivery of frozen and chilled products from the processing plant to the main distribution cold storage and further to the retail outlets. A well trained and experienced team of drivers ensures that the product is transported at required temperature ensuring food safety.
- Snowman also possesses a well connected communication network which provides immediate information to the client on the movement of goods. A professional team of Refrigeration Operators, vehicle supervisors and Truck maintenance mechanics ensure that the cold chain is never broken.
- Currently it operates with fleet of ~120 trucks with refrigeration units. It covers ~100 cities in India and operates with fixed schedules.

## Business division - Cold Stores - Freezer division

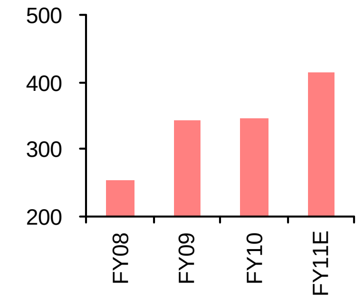
- The Snowman frozen and chilled stores are built with State-of-the-art technology by Huurre Group of Finland, a world leader in turn key freezer store supply and management
- The Snowman stores are built to meet international standards of temperature and hygiene for frozen foods. The stores are operated under process control systems which can maintain specific temperature for different products.
- It has Palletized storage system, racked storage system and concept of sharing the cold store. The storage facilities also provide for computer controlled inventory management system.

- Some of the other features include separate storage of vegetarian and non-vegetarian products, full power back-up, environment friendly refrigerated gas, First in first out system (FIFO), air Locked truck docking system and trained manpower ensuring guaranteed safe storage

## Business division - Consignment agency

Consignment Agency business offers a basket of services to producers, importers, wholesalers etc of food products, in reaching their produce to the retailers, hotels, caterers etc. It is a perfect solution for factory to consumer supply chain management, with ideal cold chain. The infrastructure is capable of handling products requiring temperature controlled environment from +15 degree celsius to -20 degree celsius.

**Revenues of Cold chain business (Rs. mn)**




*Source: Company, Kotak Securities - Private Client Research*

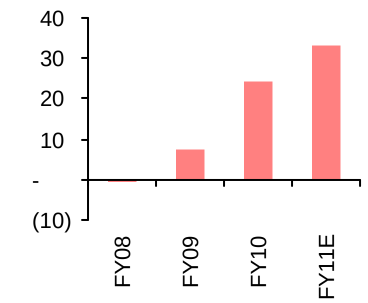
## Technology used by Snowman

- The basic specification for Snowman cold storage is to maintain the air temperature for storage at -20 degree celsius in order to retain the temperature of product stored at -18 degree celsius which is international standard for frozen foods. Since there could be variation in the temperature of incoming products and to provide better safeties the cold storage has been designed for operation at -25 degree celsius with flexibility of incoming materials up to -15 deg celsius.
- The material storage arrangement is on standard two deep racking system which can store materials on Euro pallets of size 1000 X 1200 X 1500 mm with vertically 4 high arrangements.
- The pallet movement is with the help of battery operate electric forklift reach truck suitable for lifting the material from 4th level and second depth of the rack.
- The loading and unloading of the materials from or into the refrigerated truck is done with the help of suitable dock levelers and dock shelters. The dock shelters are air locking the trucks into the cold storage area while the leveler matches the floor level of the truck with that of the cold storage.

## Strengths of Snowman

- Large network helps to operate with economies of scale and thereby keep the costs low
- Own vehicle fleet helps to have better control on the daily operations of the business
- Having process driven approach helps it to offer customized solutions to its clients
- With access to best technology it is able to have greater visibility in the fast growing markets

**PAT of Cold chain business (Rs. mn)**




*Source: Company, Kotak Securities - Private Client Research*

## Infrastructure of Snowman

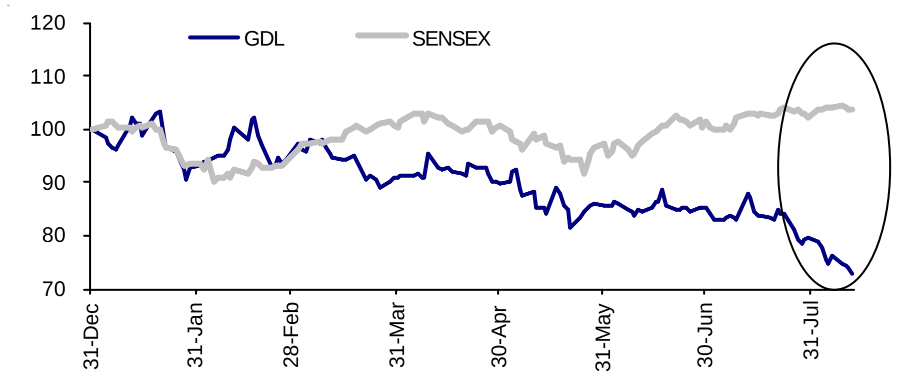
- Snowman's temperature controlled storage infrastructure is currently spread across 16 facilities across the country and the company operates over 120 owned and contracted refrigerated trucks in its transportation division. Currently it has capacity to handle 14000 MT and it plans to ramp it upto 24000 MT by September 2011.
- As of March 2010, it has capacity to handle 11000 MT. In May 2010 it commissioned 3000 MT capacity cold chain warehouse at Chennai and this would be followed by 3000 MT capacity cold chain warehouse at Bangalore by December 2010. Going forward it would commission two more cold chain warehouses at Taloja near Mumbai and Vallabgarh (North India) by September 2011. This would take the total capacity to 24000 MT by September 2010.
- IFC's investment of Rs.249 mn for 19.99% equity stake will support Snowman's capital needs during its strategic growth phase, helping the company become more efficient and expand at both existing and new locations in India.

- We believe that above is very positive for the long term growth prospects of snowman as with IFC as a partner, it will continue to expand and seek the highest standards in the operations. This is also positive for the shareholders of GDL as it would be profit accretive to the overall consolidated PAT of GDL.

## Financials of Snowman

For Q1FY11 the cold chain business reported revenues of Rs.105 mn (up 34.3% YoY) with EBIDTA of Rs.23 mn (up 28.7% YoY) and PAT of Rs.8 mn (as against loss of Rs.1 mn in Q1FY10). This was on account of expansion of Chennai facility and improved business environment.

**Price performance**




*Source: Bloomberg*

## Valuation & Recommendation

- We maintain FY11 earning estimates and expect GDL to report Cons. EPS of Rs.8.4 and CEPS of Rs.13.1.
- At the current market price of Rs.100, the stock of GDL is trading at 1.6x P/BV, 12.0x P/E and 7.6x P/CEPS based on FY11 earning estimates.

**We upgrade GDL to BUY with unchanged price target of Rs.122**

- We continue to remain positive on the medium to long term growth prospects of the company due to increasing containerization, export import trade and company's presence at all the major ports, rail linked ICD, running of private container trains and expansion in booming cold chain business would keep its position stronger in the future as well.
- Since January 2010 the stock of GDL has significantly underperformed the markets as during the period GDL is down 27% as against 3% rise in SENSEX. We use this is underperformance as an opportunity and upgrade GDL to BUY.
- Due to 22% upside potential from the current levels, we upgrade GDL to BUY for with unchanged price target of Rs.122.

## Gainers & Losers

**Nifty Gainers & Losers**

| | Price (Rs) | chg (%) | Index points | Volume (mn) |
|---|---|---|---|---|
| **Gainers** | | | | |
| State Bank of India | 2,784 | 7.1 | 16.4 | 6.4 |
| ONGC | 1,266 | 2.4 | 3.4 | 1.3 |
| Axis Bank | 1,316 | 2.1 | 2.3 | 1.2 |
| **Losers** | | | | |
| Infosys Tech | 2,773 | (1.4) | (6.4) | 0.9 |
| Reliance Ind | 973 | (1.1) | (6.2) | 5.7 |
| ITC | 153 | (1.3) | (3.6) | 4.9 |

*Source: Bloomberg*

## Forthcoming events

**Company/Market**

| Date | Event |
|---|---|
| 13-Aug | Adani Ent, Bank of Rajasthan, Cipla, Deccan Chronicle, Finolex Inds, HMT, Patel Engineering, Reliance Comm, Saregama India, Suzlon Energy, Tanla Solutions, Trigyn Tech, Wockhardt earnings expected |

*Source: Bloomberg*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