

### Contents

#### New Release

**Banks/Financial Institutions:** Mid-size public banks—attractively positioned

#### Results

**Tata Consultancy Services:** Picture perfect

**Axis Bank:** Focused on growth; retain ADD

**Colgate-Palmolive (India):** Good quarter; valuations leave little upside

**Castrol India:** Better-than-expected results but valuations hard to justify

**LIC Housing Finance:** Business remains in sweet spot; retain positive outlook

**Polaris Software Lab:** Margin pressures surface

#### Updates

**Reliance Industries:** Cash deployment continues to be an issue

**Technology:** Volume momentum strong but watch out for wage pressure

**Energy:** Buying opportunity

### News Round-up

- ▶ Reliance Power (RPWR IN) has managed to get a change of mind from the Export-Import Bank of the US (Ex-Im Bank), on the latter's decision just three weeks earlier to refuse finance for the Sasan ultra mega power project in Madhya Pradesh. *(BSTD)*
- ▶ IOC (IOCL IN) set to enter gas pipeline business. Technical bids opened today for Mallavaram-Vijaipur line, winner in three weeks. IOC plans to acquire oil-fields in Africa as part of a US\$1 bn overseas investment plan. *(BSTD)*
- ▶ Indian Oil, (IOCL IN) Hindustan Petroleum Corporation, (HPCL IN) and Bharat Petroleum Corporation (BPCL IN) are expected to post net losses of nearly US\$2.12 bn combined for the first quarter of this fiscal. *(THBL)*
- ▶ M&M (MM IN) delayed a decision on the bid for South Korea's Ssangyong Motors as promoters look for ways to maintain at least 26% in the company, while it contemplates fund-raising for the purchase. M&M may need US\$212.77 mn to maintain their stake at 26%. *(ECNT)*
- ▶ L&T (LT IN) plans to raise US\$600 mn from institutional investors to fund future programmes that include building a large metro rail network & setting up power plants. *(ECNT)*
- ▶ The government has allowed Essar Steel to surrender its steel SEZ in Gujarat as the units decided to opt out of the enclave on account of global downturn. *(BSTD)*
- ▶ Tata Motors (TTMT IN) said its global sales increased by 46% in June to 91,608 units on robust demand from both commercial and passenger vehicles. *(BSTD)*
- ▶ JSW Energy (JSW IN) to raise US\$2.87 bn debt this year. The loan will finance two coal-based power projects under development. *(BSTD)*
- ▶ Infosys (INFO IN) closes BPO in Bangkok. Moves work to India, China. *(BSTD)*
- ▶ M&M (MM IN) is looking to roll out the country's first sub INR 0.5 mn sports utility vehicle, a compact version of Xylo, this year. *(ECNT)*

Source: ECNT= Economic Times, BSTD = Business Standard, FNLE = Financial Express, THBL = Business Line.

### EQUITY MARKETS

India	Change %			
	15-Jul	1-day	1-mo	3-mo
Sensex	17,909	(0.2)	2.6	1.8
Nifty	5,379	(0.1)	2.8	2.2
<b>Global/Regional indices</b>				
Dow Jones	10,359	(0.1)	(0.5)	(6.0)
Nasdaq Composite	2,249	(0.0)	(2.5)	(9.4)
FTSE	5,211	(0.8)	(0.5)	(9.3)
Nikkie	9,527	(1.6)	(5.4)	(14.2)
Hang Seng	20,256	(1.5)	1.0	(7.4)
KOSPI	1,740	(0.6)	2.0	0.3
<b>Value traded – India</b>				
Cash (NSE+BSE)	167		170	171
Derivatives (NSE)	791		1,027	737
Deri. open interest	1,501		1,424	1,246

#### Forex/money market

	Change, basis points			
	15-Jul	1-day	1-mo	3-mo
Rs/US\$	46.7	0	13	225
10yr govt bond, %	7.6	-	(4)	(45)

#### Net investment (US\$mn)

	13-Jul	MTD	CYTD
FIs	171	1,512	8,212
MFs	(25)	(52)	(282)

#### Top movers -3mo basis

Best performers	Change, %			
	15-Jul	1-day	1-mo	3-mo
HPCL IN Equity	445.6	(6.0)	30.4	47.0
BJFIN IN Equity	416.3	(1.2)	(8.5)	35.2
IOCL IN Equity	374.5	(3.8)	12.2	32.8
BPCL IN Equity	656.3	(6.3)	22.8	31.4
AL IN Equity	71.4	4.1	14.3	29.3
<b>Worst performers</b>				
ABAN IN Equity	860.7	(0.9)	21.5	(29.5)
RNR IN Equity	45.5	(0.3)	(33.2)	(28.6)
SESA IN Equity	339.7	(3.3)	(4.1)	(28.0)
TATA IN Equity	512.8	1.4	5.6	(26.3)
STLT IN Equity	166.2	(0.9)	(3.7)	(20.7)

Kotak Institutional Equities Research  
kotak.research@kotak.com . Mumbai: +94-22-6634-1100

JULY 16, 2010

UPDATE

BSE-30: 17,909

**Mid-size public banks—attractively positioned.** Our positive outlook on the mid-size public banking space is led by three factors (1) attractive valuations compared to larger banks and private banks despite similar return ratios, (2) capital infusion in the form of preference shares—positive for shareholders, RoEs and growth, and (3) lower credit-deposit ratios, which will result in reasonable margin expansion in a tight-liquidity environment. We see Vijaya Bank, Dena Bank, Allahabad Bank, Central Bank of India and IOB as key beneficiaries of these trends.

#### PSU banks are primary beneficiaries of the capital infusion

Under a recapitalization program, PSU banks with tier-1 capital under 8% have been receiving capital, mainly in the form of preference shares, from the Government of India (with US\$4.2 bn support from World Bank). In the past two years, Gol has done this for Central Bank of India, Vijaya Bank, UCO Bank and United Bank of India. We expect Dena Bank, Syndicate Bank, BOI, IOB, Bank of Maharashtra and Union Bank to receive the next round of capital as their tier-1 is close to 8% and have little headroom to raise capital through other instruments.

#### Preference shares offer higher RoE through leverage; positive for PSU banks

Preference shares qualify for tier-1 capital and are inexpensive (100 bps over Repo and even lower than other capital instruments). Moreover, they are not shareholder dilutive and can increase leverage leading to sustainable RoE improvement. We are comfortable with higher leverage in the current environment as it will result in higher RoEs through faster and profitable growth, without an immediate commensurate increase in NPLs. Further, being quasi government entities, we do not expect borrowings costs / default risks to increase despite higher leverage.

#### New capital to result in faster balance sheet growth

The availability of capital should make banks more confident of balance sheet growth (to a lesser extent, this reduces net worth constraints, especially for large ticket loans). Our estimates show that banks should be able to grow their risk weighted assets by over 50% excluding internal accruals, sufficient to fund growth for the next 18 months. However, a bulk of this has to be infused through preference shares.

#### Near-term margins to remain strong, despite somewhat expensive debt

We expect near-term margins (FY2011E) to improve with new capital and lower CD ratios for smaller public banks. This is despite the higher savings deposit costs and higher contribution on IPDI. PSU banks, as a means to conserve capital have been conservative on their exposure with nearly 60% of risk weighted assets below 100%. With the capital commitment available from Gol, we expect these banks to increase their risk exposures marginally resulting in high lending yields.

#### Valuations are attractive at less than 1X FY2012E PBR but risk persists

We see valuations at fairly attractive levels for some mid-tier PSU banks like Dena Bank, Vijaya Bank, Central Bank of India, IOB and Allahabad Bank. We are cognizant of the fact that (1) higher RoEs are coming at higher leverage, and (2) regulatory risk persists given the recent working papers and comments from RBI on the quality of capital held by banks. However, with Gol being the only investor in preference shares, we believe that the essence of the instruments remains intact (long term and importantly less likely to be called at inopportune times).

Manish Karwa  
manish.karwa@kotak.com  
Mumbai: +91-22-6634-1350

M B Mahesh  
mb.mahesh@kotak.com  
Mumbai: +91-22-6634-1231

Nischint Chawathe  
nischint.chawathe@kotak.com  
Mumbai: +91-22-6634-1545

Kotak Institutional Equities Research  
kotak.research@kotak.com  
Mumbai: +91-22-6634-1100

**JULY 15, 2010**
**RESULT**

Coverage view: **Attractive**

Price (Rs): **782**

Target price (Rs): **965**

BSE-30: **17,909**

**Picture perfect.** Impressive qoq revenue growth of 6.4% and better-than-expected margin performance drove significant earnings outperformance. Our view that industry is not operating in a demand-constrained environment is best demonstrated through TCS results. Credit to TCS for outstanding execution and managing the supply-side challenges. We raise our FY2011E and FY2012E earnings to Rs42.1 and Rs48.2 (2.4-4% upgrade) and target price to Rs965. Maintain BUY rating.

**Company data and valuation summary**

TCS

**Stock data**

52-week range (Rs) (high,low)	835-405
Market Cap. (Rs bn)	1,530.7

**Shareholding pattern (%)**

Promoters	74.1
FIs	12.4
MFs	2.3

**Price performance (%)**

	1M	3M	12M
Absolute	2.1	(3.6)	87.2
Rel. to BSE-30	(0.7)	(5.0)	49.0

**Forecasts/Valuations**

	2010	2011E	2012E
EPS (Rs)	35.1	42.1	48.2
EPS growth (%)	32.8	19.8	14.5
P/E (X)	22.3	18.6	16.2
Sales (Rs bn)	300.3	360.4	434.3
Net profits (Rs bn)	68.7	82.3	94.3
EBITDA (Rs bn)	86.8	106.3	125.1
EV/EBITDA (X)	16.7	13.5	11.2
ROE (%)	37.6	35.6	33.9
Div. Yield (%)	2.6	2.2	2.5

**Picture perfect, strong volumes and significant net income outperformance**

TCS reported outstanding 1QFY11 performance. Net income of Rs18.4 bn exceeded our expectations by 3.8%. Key aspects of strong performance include

- ▶ Revenue growth of 6.4% to US\$1,794 mn. Volumes grew 8.1% qoq, impressive noting its scale of operations. Growth was broad-based with benefits from ramp-up of large deal wins.
- ▶ Operating margin decline of 36 bps was lower than our expectations. This is impressive noting significant headwinds from revision in compensation and currency appreciation. Operating margin performance was helped by 90 bps swing in provision for doubtful debts.
- ▶ The company indicated benefits of rate productivity despite adverse shift in business mix towards low realization services.

**Outstanding execution against the backdrop of supply-constrained environment**

We maintain that the sector is not operating in a demand-constrained but a 'supply-constrained' environment. TCS demonstrated its leadership in an often under-appreciated area, supply chain management. Strong execution (profitability, volumes, utilization etc), against the backdrop of increasing attrition and supply constraints is a testament of its preferred employer brand, smooth recruitment engine and solid delivery infrastructure. FY2011E growth will be decided on ability to deal with supply-side pressures, an area where TCS is neck and crop above the rest.

**Raise FY2011-12E estimates by 2.4-4%, target price to Rs965**

We raise our FY2011E and FY2012E earnings estimates by 2.4% and 4% to Rs42.1 and Rs48.2, respectively. The revision is driven primarily by increase in margin assumptions (60 bps each for both FY2011E and FY2012E). We increase our end-FY2012E target price to Rs965 from Rs900 earlier. Our target multiple of TCS at 20X is at a 5% discount to Infosys.

Kawaljeet Saluja  
kawaljeet.saluja@kotak.com  
Mumbai: +91-22-6634-1243

Rohit Chordia  
rohit.chordia@kotak.com  
Mumbai: +91-22-6634-1397

Vineet Thodge  
vineet.thodge@kotak.com  
Mumbai: +91-22-6634-1225

Kotak Institutional Equities Research  
kotak.research@kotak.com  
Mumbai: +91-22-6634-1100

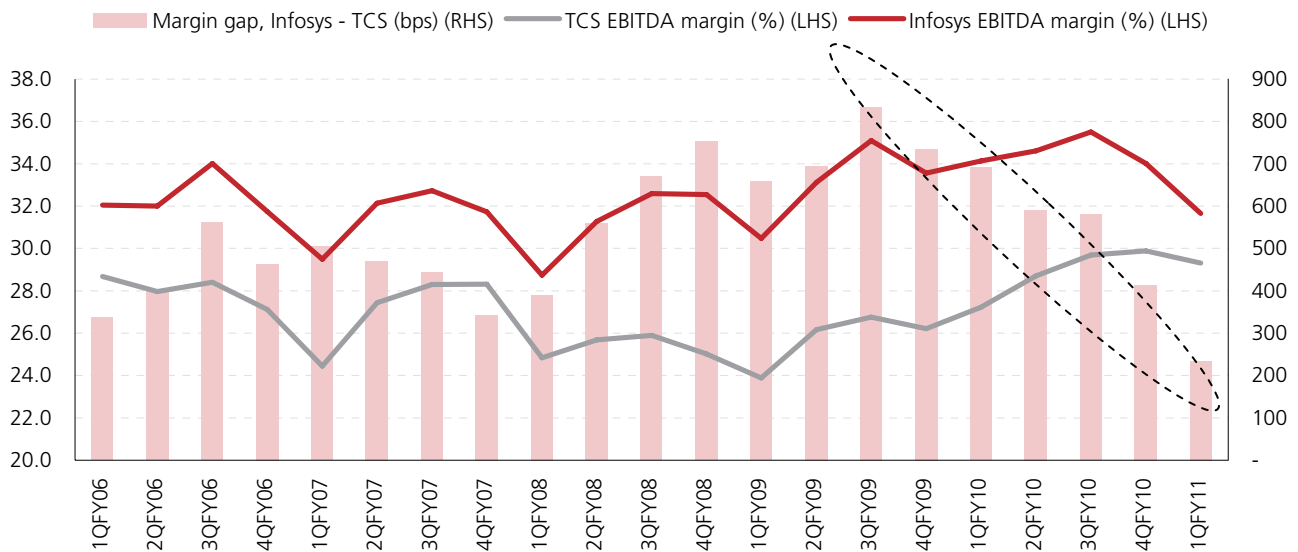
**Management earnings commentary lends confidence to our thesis**

Management commentary on (1) large active deal pipeline of multi-million dollar deals; (2) initial signs of increase in discretionary spending, (3) continued market share gains vis-à-vis global vendors and (4) FY2011E gross hiring guidance raised to 40,000 from 30,000 earlier, lends confidence on demand environment and growth. TCS won 10 large deals in the quarter in addition to the 10 signed in the previous quarter. We are also impressed with revenues from new clients that stood at 1.6% of the overall revenues; this equates to US\$29 mn revenues from clients signed in Apr-Jun 2010. This is the highest ever for a quarter in absolute terms, clearly indicating the quality of new client signings.

**Bridging the margin gap with Infosys**

Exhibit 1 presents the operating margin trend of Infosys and TCS over the last few quarters. The gap in margin has reduced to just 234 bps in 1QFY11 from the peak of 834 bps in the past few years. While lack of disclosures on key operational parameters by TCS makes analysis of the reasons for change difficult, we can possibly think of the following reasons (1) change in mix of business of TCS with considerable de-emphasis from low-margin yielding domestic systems integration projects; (2) better execution and move away by TCS from deals involving upfront investments and margin dilution and (3) delivery efficiencies. Adjusted for TCS' India revenues, we suspect that margins of TCS will be similar to Infosys.

TCS has bridged the margin gap versus Infosys substantially over the past few quarters



Source: Companies, Kotak Institutional Equities

## TCS: key changes to FY2011E-12E estimates

Rs mn	New		Old		Change (%)	
	FY2011E	FY2012E	FY2011E	FY2012E	FY2011E	FY2012E
<b>Revenues</b>	<b>360,438</b>	<b>434,330</b>	<b>353,939</b>	<b>425,783</b>	<b>1.8</b>	<b>2.0</b>
EBIT	98,279	115,469	94,414	110,908	4.1	4.1
<b>Net Profit</b>	<b>82,338</b>	<b>94,309</b>	<b>80,373</b>	<b>90,698</b>	<b>2.4</b>	<b>4.0</b>
<b>EPS (Rs/ share)</b>	<b>42.1</b>	<b>48.2</b>	<b>41.1</b>	<b>46.3</b>	<b>2.4</b>	<b>4.0</b>
<b>Revenues (US\$ mn)</b>	<b>7,828</b>	<b>9,442</b>	<b>7,861</b>	<b>9,408</b>	<b>(0.4)</b>	<b>0.4</b>
<b>Revenue growth (%)</b>	<b>23.5</b>	<b>20.6</b>	<b>24.0</b>	<b>19.7</b>		
<b>Re/\$ rate</b>	<b>46.0</b>	<b>46.0</b>	<b>45.0</b>	<b>45.3</b>	<b>2.3</b>	<b>1.6</b>
<b>EBIT margin</b>	<b>27.3</b>	<b>26.6</b>	<b>26.7</b>	<b>26.0</b>		

Source: Kotak Institutional Equities estimates

## Comments: TCS Interim Results (consolidated, US GAAP)

Rs mn	1QFY10	4QFY10	1QFY11	% chg.		1QFY11E	% dev.	Comments
				qoq	yoy			
<b>Revenues (US\$ mn)</b>	<b>1,481</b>	<b>1,686</b>	<b>1,794</b>	<b>6.4</b>	<b>21.1</b>	<b>1,762</b>	<b>1.8</b>	Driven by volume growth of 8.1% qoq and impacted to the tune of 0.9% by adverse cross-currency movements
<b>Revenues</b>	<b>72,070</b>	<b>77,365</b>	<b>82,173</b>	<b>6.2</b>	<b>14.0</b>	<b>80,571</b>	<b>2.0</b>	
Cost of revenues	(39,238)	(41,160)	(45,155)	9.7	15.1	(43,719)	3.3	
<b>Gross profit</b>	<b>32,832</b>	<b>36,205</b>	<b>37,018</b>	<b>2.2</b>	<b>12.7</b>	<b>36,852</b>	<b>0.5</b>	
SG&A expenses	(14,940)	(14,925)	(14,711)	(1.4)	(1.5)	(15,645)	(6.0)	
<b>EBIT</b>	<b>17,892</b>	<b>21,280</b>	<b>22,307</b>	<b>4.8</b>	<b>24.7</b>	<b>21,207</b>	<b>5.2</b>	EBIT margins at 27.1% 80 bps better than expectations
Other Income	194	1,636	831	(49.2)	328	774	7.4	Other income includes forex loss of RS470 mn
Profit Before Tax	18,086	22,916	23,138	1.0	27.9	21,981	5.3	
Provision for Tax	(2,655)	(3,284)	(4,423)	34.7	66.6	(3,932)	12.5	
<b>Net income before minority interest</b>	<b>15,431</b>	<b>19,632</b>	<b>18,715</b>	<b>(4.7)</b>	<b>21.3</b>	<b>18,049</b>	<b>3.7</b>	
Income from affiliates	(2)	(8)	(3)			—		
Minority Interest	(226)	(312)	(272)	(12.8)	20.4	(291)	(6.6)	
<b>Net income</b>	<b>15,203</b>	<b>19,312</b>	<b>18,440</b>	<b>(4.5)</b>	<b>21.3</b>	<b>17,758</b>	<b>3.8</b>	
Extraordinary items	—	—	—			—		
<b>Net income</b>	<b>15,203</b>	<b>19,312</b>	<b>18,440</b>	<b>(4.5)</b>	<b>21.3</b>	<b>17,758</b>	<b>3.8</b>	Net income 3.8% ahead of expectations
EPS (Rs/ share)	7.8	9.9	9.4	(4.5)	21.3	9.1	3.8	
No of shares outstanding (mn)	1,957.2	1,957.2	1,957.2	—	—	1,957.2	—	
<b>As % of revenues</b>								
Gross Profit Margin (%)	45.6	46.8	45.0			45.7		
Operating Margin (EBIT)	24.8	27.5	27.1			26.3		
EBITDA (%)	27.2	29.9	29.3			28.7		
SG&A Expenses (%)	20.7	19.3	17.9			19.4		
Tax Rate	14.7	14.3	19.1			17.9		
<b>Revenue Mix (%)</b>								
Onsite	44.4	43.6	43.6					
Offshore	55.6	56.4	56.4					
<b>Revenues (Rs mn)</b>								
Onsite	29,085	30,728	32,665	6.3	12.3			
Offshore	36,421	39,750	42,255	6.3	16.0			
<b>International Revenues</b>	<b>65,506</b>	<b>70,478</b>	<b>74,920</b>	<b>6.3</b>	<b>14.4</b>			
Domestic Revenues	6,564	6,887	7,253	5.3	10.5			

Source: Company, Kotak Institutional Equities estimates

## Quality of new client additions impressive

	FY2008 1Q	FY2009 1Q	FY2010 1Q	FY2011 1Q
Revenues (US\$ mn)	1,262	1,525	1,481	1,794
<b>Repeat business (%)</b>	<b>99.2</b>	<b>99.3</b>	<b>99.7</b>	<b>98.4</b>
<b>Revenues from new clients (US\$ mn)</b>	<b>10.1</b>	<b>10.7</b>	<b>4.4</b>	<b>28.7</b>
New clients added (#)	54	35	26	36
Cumulative new clients in the fiscal (#)	54	35	26	36
<b>Annualized revenue per new client (US\$ mn)</b>	<b>1.5</b>	<b>2.4</b>	<b>1.4</b>	<b>6.4</b>

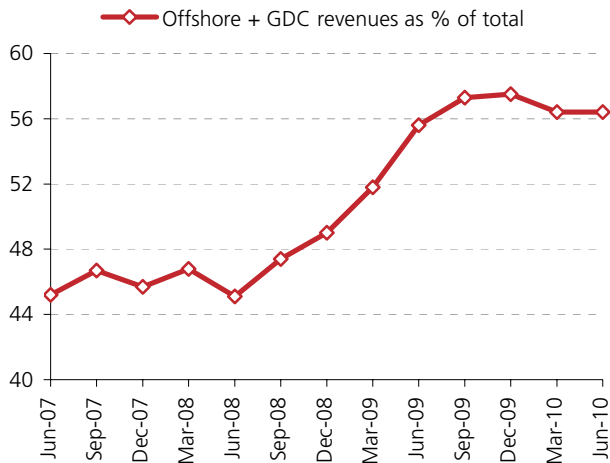
Source: Company, Kotak Institutional Equities estimates

## TCS continues to outperform Infosys on EBITDA and net income growth

	Sep-08	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
<b>yoy US\$ revenue growth (%)</b>								
TCS	13	(0)	(6)	(3)	(2)	10	18	21
Infosys	19	8	(2)	(3)	(5)	5	15	21
<b>yoy Rupee net income growth (%)</b>								
TCS	1	2	5	22	29	33	47	21
Infosys	30	34	30	20	8	0	(2)	(3)
<b>yoy Rupee EBITDA growth (%)</b>								
TCS	27	28	24	28	17	17	23	23
Infosys	40	46	28	26	8	0	7	5

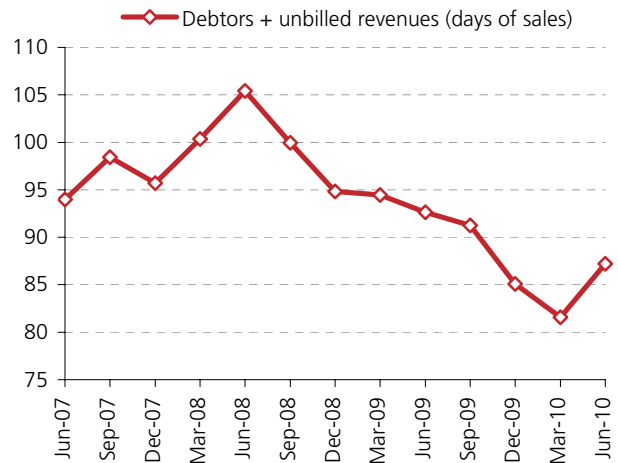
Source: Companies, Kotak Institutional Equities

Offshore shift in revenues has been a major margin driver for TCS



Source: Company

Increase in receivables days possibly the only blip in an excellent quarter



Source: Company

Key assumptions driving TCS earnings model, 2009-2012E, March fiscal year-ends

	2009	2010	2011E	2012E
<b>Key assumptions</b>				
<b>Revenue growth (US\$ terms) (%)</b>	6.1	5.4	23.5	20.6
<b>Volume growth yoy (%)</b>	15.8	22.1	25.0	18.9
<b>Pricing change yoy (%)</b>				
Onsite	(7.8)	(7.8)	(0.5)	1.2
Offshore	(3.7)	(7.6)	(1.7)	2.5
Blended	(6.8)	(14.4)	(1.4)	1.5
<b>Total employees (#) - excl subsidiaries</b>	140,011	156,329	186,387	224,381
<b>Employee additions</b>	32,313	16,318	30,058	37,994
<b>Utilization rate (%)</b>	72.5	74.2	75.5	76.1
<b>SG&amp;A expense as % of revenues</b>	20.0	18.7	17.7	18.0
<b>Re/US\$ rate</b>	46.3	47.4	46.0	46.0

Source: Company, Kotak Institutional Equities estimates

Profit model, balance sheet, cash model of TCS, 2008-2012E, March fiscal year-ends (Rs mn)

	2008	2009	2010	2011E	2012E
<b>Profit model</b>					
<b>Revenues</b>	<b>228,614</b>	<b>278,129</b>	<b>300,289</b>	<b>360,438</b>	<b>434,330</b>
Cost of sales	(126,194)	(154,420)	(161,668)	(195,669)	(237,497)
SG&A expenses	(48,769)	(57,694)	(59,030)	(66,490)	(81,363)
<b>EBIT</b>	<b>53,651</b>	<b>66,015</b>	<b>79,591</b>	<b>98,279</b>	<b>115,469</b>
Other income	4,450	(4,673)	2,255	4,801	7,120
<b>Pre-tax profits</b>	<b>58,101</b>	<b>61,342</b>	<b>81,846</b>	<b>103,081</b>	<b>122,589</b>
Provision for tax	(7,494)	(9,012)	(12,089)	(19,531)	(27,091)
<b>Recurring net income</b>	<b>50,607</b>	<b>52,330</b>	<b>69,757</b>	<b>83,549</b>	<b>95,498</b>
Equity in earnings of affiliates	8	(8)	(10)	(3)	—
Minority Interest	(424)	(569)	(1,018)	(1,208)	(1,190)
<b>Reported net income</b>	<b>50,183</b>	<b>51,761</b>	<b>68,739</b>	<b>82,341</b>	<b>94,309</b>
<b>EPS (Rs)</b>	<b>25.6</b>	<b>26.4</b>	<b>35.1</b>	<b>42.1</b>	<b>48.2</b>
<b>Balance Sheet</b>					
Shareholders funds	123,820	156,545	209,404	253,209	303,384
Borrowings	6,727	2,762	111	—	—
Minority interest	2,300	3,098	3,768	4,976	6,166
Other non-current liabilities	756	2,744	6,732	3,556	4,285
<b>Total liabilities</b>	<b>133,602</b>	<b>165,149</b>	<b>220,015</b>	<b>261,742</b>	<b>313,835</b>
Net fixed assets	30,214	37,494	41,706	55,620	67,757
Goodwill	11,105	25,913	25,333	25,333	25,333
Intangibles	3,633	8,232	7,082	7,082	7,082
Investments	26,475	17,271	37,822	37,822	37,822
Other non-current assets	10,427	17,370	26,120	26,117	26,117
Cash and bank balances	10,352	24,742	46,773	62,981	97,594
Net current assets excluding cash	41,396	34,127	35,178	46,786	52,129
<b>Total assets</b>	<b>133,602</b>	<b>165,149</b>	<b>220,015</b>	<b>261,742</b>	<b>313,835</b>

Source: Company, Kotak Institutional Equities estimates



## TCS: Quarterly operating metrics

	Jun-08	Sep-08	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
Revenues (US\$ mn)	1,525	1,574	1,483	1,433	1,481	1,538	1,635	1,686	1,794
Revenues (Rs mn)	64,107	69,534	72,770	71,718	72,070	74,351	76,503	77,365	82,173
Exchange rate (Re/US\$)	42.0	44.2	49.1	50.0	48.7	48.3	46.8	45.9	45.8
<b>Revenue by geography (%)</b>									
North America	51.1	49.7	52.2	52.4	52.3	52.5	52.5	54.0	55.0
Latin America	4.1	4.7	5.1	4.8	4.6	5.0	4.9	4.4	4.3
UK	19.5	20.2	18.5	17.9	16.9	16.5	16.0	15.2	15.1
Continental Europe	10.1	10.5	10.7	10.8	11.0	10.6	10.4	10.0	8.9
India	8.7	7.8	6.8	8.2	9.1	8.1	8.5	8.9	8.8
Asia Pacific	4.9	5.3	5.0	3.9	4.3	5.4	5.6	5.6	5.9
MEA	1.6	1.8	1.7	2.0	1.8	1.9	2.1	1.9	2.0
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
<b>Vertical split of revenues (%) - % of international revenues till 3QFY10, % of overall revenues from 4QFY10 onwards</b>									
BFSI	42.5	41.9	41.9	42.8	43.9	45.0	45.0	45.6	44.7
Telecom	15.5	15.3	13.8	13.1	12.6	12.0	12.1	12.2	12.7
Retail & Distribution	8.6	9.0	11.2	12.0	12.2	12.0	12.0	10.9	11.0
Manufacturing	10.7	11.0	10.6	9.8	9.2	8.7	8.3	7.8	7.4
Hi-Tech	7.0	6.9	6.7	5.5	4.9	4.8	5.0	4.4	4.6
Life sciences & healthcare	5.3	4.8	5.2	5.7	5.7	6.0	5.9	5.2	5.2
Transportation	4.3	4.6	3.7	3.8	3.7	3.5	3.4	3.2	3.1
Energy & Utilities	2.9	3.0	2.6	2.7	2.7	2.8	3.4	3.0	3.3
Media & Entertainment	1.7	1.7	2.0	2.1	2.2	2.2	2.1	1.8	1.9
Others	1.5	1.8	2.3	2.5	2.9	3.0	2.8	5.9	6.1
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
<b>Revenues by project type (%)</b>									
Time and material basis	57.2	56.6	54.5	52.9	52.6	52.8	52.0	51.3	50.9
Fixed price, fixed time basis	42.8	43.4	45.5	47.1	47.4	47.2	48.0	48.7	49.1
<b>Client concentration (%)</b>									
Top client	6.2	5.9	5.1	4.7	5.7	6.8	8.1	8.2	8.1
Top 5 clients	18.5	17.8	17.3	18.6	19.4	20.5	21.5	21.8	22.0
Top 10 clients	28.3	26.9	26.3	26.9	28.0	28.9	29.9	30.2	30.5
US\$1 mn clients	362	397	395	405	423	409	419	409	409
US\$5 mn clients	147	168	166	172	178	171	178	183	191
US\$10 mn clients	105	108	112	111	113	111	112	118	122
US\$20 mn clients	54	55	59	62	59	62	61	63	65
US\$50 mn clients	21	22	23	24	23	23	23	23	24
US\$100 mn clients	—	—	—	7	6	6	6	7	7
Number of active clients	885	920	965	985	933	896	917	917	930
New clients added in the period	35	51	41	36	26	30	32	39	36
Revenue from repeat business (%)	99.3	97.6	96.3	95.6	99.7	98.2	96.5	95.7	98.4
<b>Onsite-offshore split (%)</b>									
Onsite	54.9	52.6	51.0	48.2	44.4	42.7	42.5	43.6	43.6
Offshore	40.9	42.8	43.6	47.7	50.4	51.1	51.3	51.0	51.2
GDC / RDC	4.2	4.6	5.4	4.1	5.2	6.2	6.2	5.4	5.2
<b>Revenue by service offerings (%)</b>									
IT solutions and services									
- ADM	46.9	49.2	49.0	48.6	48.7	49.6	49.1	47.6	47.9
- Business intelligence	9.0	8.6	8.1	6.8	6.1	5.7	5.7	5.4	5.4
- Enterprise solutions	13.0	12.5	12.6	11.8	10.9	10.3	10.5	10.1	9.8
- Assurance business	4.5	4.4	4.2	3.8	4.4	4.8	5.1	5.8	6.4
Engineering & Industrial services	5.6	6.0	6.3	5.8	5.2	5.0	4.9	4.8	4.8
Infrastructure services	7.7	7.5	8.3	8.3	9.3	8.0	7.9	8.3	8.7
Global consulting	3.7	2.9	2.5	1.7	1.4	1.6	2.1	2.5	2.1
Asset leverage solutions	3.5	3.1	3.2	2.1	2.6	3.2	3.2	4.0	3.7
BPO	6.1	5.8	5.8	11.1	11.4	11.8	11.5	11.5	11.2
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
<b>Utilization rates (%)</b>									
- Including trainees	74.6	74.7	71.8	69.4	71.3	73.6	77.2	74.3	74.8
- Excluding trainees	78.3	81.1	79.9	79.7	79.2	79.5	81.1	81.8	82.6
<b>Employee metrics</b>									
Total employees - incl Indian subsidiaries	116,308	121,610	130,343	143,761	141,642	141,962	149,654	160,429	163,700
Total employees - TCS limited	112,593	117,921	126,613	126,613	123,404	123,092	130,509	140,619	142,939
Gross addition	8,982	9,682	11,773	17,489	2,828	5,530	12,854	16,851	8,464
Net addition	4,901	5,302	8,733	13,418	(2,119)	320	7,692	10,775	3,271
Attrition rate (%)	12.1	12.4	11.9	11.4	10.7	10.8	11.5	11.8	13.1
Attrition rate - qtrly annualized, incl Indian subsidiaries (%)					13.9	14.7	14.2	15.7	12.8

Source: Company, Kotak Institutional Equities

**JULY 15, 2010**
**RESULT**

Coverage view: **Attractive**

Price (Rs): **1,350**

Target price (Rs): **1,500**

BSE-30: **17,909**

**Focused on growth; retain ADD.** Axis Bank reported strong earnings for 1Q, with better than expected margins at 3.7% along with a strong loan book growth of 39% yoy. While delinquency was higher (1.6%) and is a minor concern, we believe that higher margins and fees will take care of the higher provisioning requirement. We maintain our positive bias on the stock, but expensive valuations (at 2.5XFY2012E PBR) do not leave much room for upside. Retain ADD with a TP of Rs1,500.

**Company data and valuation summary**

Axis Bank

**Stock data**

52-week range (Rs) (high,low)	1,356-761
Market Cap. (Rs bn)	547.1

**Shareholding pattern (%)**

Promoters	38.5
FIs	41.5
MFs	5.4

**Price performance (%)**

	1M	3M	12M
Absolute	8.4	17.6	71.2
Rel. to BSE-30	5.4	15.8	36.3

**Forecasts/Valuations**

	2010	2011E	2012E
EPS (Rs)	62.1	78.1	98.3
EPS growth (%)	22.7	25.9	25.9
P/E (X)	21.8	17.3	13.7
NII (Rs bn)	50.0	62.6	77.6
Net profits (Rs bn)	25.1	31.7	39.8
BVPS	396.0	456.5	532.6
P/B (X)	3.4	3.0	2.5
ROE (%)	19.2	18.3	19.9
Div. Yield (%)	0.9	1.1	1.4

**Retain positive bias, but upside is limited**

We like the bank's focus on growth, being supported by healthy margins and fee income. While risk on asset quality continues, we are not unduly worried given the improving economic environment. We expect Axis Bank to deliver earnings CAGR of 25% over FY2010-13E.

The stock has been one of the best performing banking stocks, delivering a 36% outperformance over past 12 months, and 16% over past six months. Current valuations at 2.5XFY2012E PBR are expensive and leave little room for upside. Thus, while we remain positive on the business, we are getting uncomfortable with valuations now.

We largely maintain our net earnings for FY2011E and FY2012E. Loan loss provisions are likely to decline to 1.2% of average loans in FY2011E and 1% in FY2012E, down from 1.5% in FY2010. We expect loan growth momentum to continue in FY2011E (growth of 25%). We have rolled over our valuations to FY2012E and have revised our target price to Rs1,500 (from Rs1,360 earlier), giving an upside of 10%. At our target price, the stock will trade at 2.8XFY2012E PBR. ADD.

**Strong loan growth – driven largely by telecom disbursements in 1Q**

Axis Bank continued to see a healthy growth in loan book in 1QFY11 at 39% yoy and 4% qoq to Rs1,086 bn led by large corporate segment, which was aided mainly by strong disbursements to the 3G/BWA auction participants. Funded telecom exposure which was close to 3% of loan book as of March 2010, has increased to 10% as of June 2010. SME and agricultural loans declined qoq as the bank shed some of its priority sector exposure. Retail growth was strong at 26% led by housing which was up 37% yoy.

The bank's deposits increased by 34% yoy (4% qoq) to Rs1,475 bn while CD ratio was flat qoq at 74%. CASA deposit growth remained strong (savings deposit grew 38% yoy). However, CASA proportion declined to 40% from 47% in March 2010, a seasonal trend witnessed during 1Q.

**QUICK NUMBERS**

- **Growth in loan book (39% yoy) driven by large corporates.**
- **Margins decline to 3.7%. Slippages remain high**
- **Maintaining estimates; revising TP to Rs. 1,500**

Manish Karwa  
manish.karwa@kotak.com  
Mumbai: +91-22-6634-1350

M B Mahesh  
mb.mahesh@kotak.com  
Mumbai: +91-22-6634-1231

Nischint Chawathe  
nischint.chawathe@kotak.com  
Mumbai: +91-22-6634-1545

Kotak Institutional Equities Research  
kotak.research@kotak.com  
Mumbai: +91-22-6634-1100

### NIMs decline 38 bps qoq to 3.7%, but better than expected

Axis Bank's net interest margin (NIM) was 3.7% in 1QFY11—a decline of 38 bps (better than our expectations) from 4QFY10 but remains higher than 3.34% margin reported in 1QFY10. NII grew by 44% yoy, 8% ahead of our expectations. Higher savings deposit cost, impact of priority commitments made in 4QFY10 and higher reserve requirements led to lower margins. Deposit costs which has been declining for the past 5 quarters reversed in the current quarter with an increase of 7 bps. We expect margins to remain stable in the range of 3.6-3.7%, as pricing power remains strong in the system, which should allow banks to pass on the higher deposit costs.

### Reported asset quality stable but slippages remain high

Axis Bank reported higher slippages at 1.6% (annualized) for the quarter mainly from the SME/mid corporate segment. However, in line with its policy, it chose to write off NPLs (1.1%) aggressively during the quarter – resulting in stable absolute NPLs for the quarter. Gross NPLs were at Rs13.4 bn (1.1% of loans) while net NPLs were at Rs4.1 bn (0.35% of loans) compared to Rs13.2 bn and Rs4.2 bn in the previous quarter. Retail and the large corporate segment continue to remain healthy with lower slippages. Loan loss provisions for the quarter were at 1.2% (annualized). We are building loan loss provisions at 1.2% for FY2011E and 1% for FY2012E.

### Other highlights

- ▶ Growth in fee income was relatively slower at 19% mainly due to change in reporting (adjusted growth would be at 28% yoy) and also due to lower fee income from retail, business banking and agri/SME banking. Growth in large corporate continues to remain healthy at about 75% yoy.
- ▶ Treasury income of Rs2 bn for the quarter was mainly from corporate bonds (Rs1.2 bn).
- ▶ Capital adequacy ratio stands comfortable at 14.5% with tier-1 ratio at 10.3% (excludes the profits for 1QFY10, else would be 10.8%).
- ▶ Cost-income ratio for the quarter was flat qoq at 42%. Branch expansion was slower with the bank adding just 15 branches with total branches being at 1,050. Management highlighted that they are likely to open over 200 branches during the current fiscal.

Axis Bank quarterly results-- key parameters  
March fiscal year-ends, 1QFY10-1QFY11

	1QFY10	2QFY10	3QFY10	4QFY10	1QFY11	yoy growth (%)	1QFY11 (KIE estimate)	Actual Vs KS
Interest income	29,056	28,604	28,837	29,885	33,256	14.5	29,998	10.9
Advances	19,736	19,502	19,879	20,750	23,109	17.1	20,667	11.8
Investments	8,673	8,596	8,454	8,560	9,353	7.8	8,731	7.1
Balance with RBI	354	300	274	272	325	(8.3)	300	8.3
Interest expenses	18,599	17,107	15,345	15,284	18,118	(2.6)	15,972	13.4
<b>Net interest income</b>	<b>10,456</b>	<b>11,497</b>	<b>13,491</b>	<b>14,601</b>	<b>15,138</b>	<b>44.8</b>	<b>14,026</b>	<b>7.9</b>
Non-interest income	9,586	10,656	9,881	9,335	10,008	4.4	9,107	9.9
Treasury income	3,260	2,240	1,700	1,030	1,960	(39.9)	1,200	63.3
Income excl treasury	6,326	8,416	8,181	8,305	8,048	27.2	7,907	1.8
<b>Total income</b>	<b>20,042</b>	<b>22,153</b>	<b>23,372</b>	<b>23,936</b>	<b>25,146</b>	<b>25.5</b>	<b>23,134</b>	<b>8.7</b>
Operating expenses	8,278	9,095	9,626	10,098	10,645	28.6	10,770	(1.2)
Employee cost	3,093	3,042	3,085	3,338	4,164	34.6	3,671	13.4
Other operating cost	5,185	6,053	6,540	6,761	6,481	25.0	7,099	(8.7)
Pre-prov profit	11,764	13,058	13,746	13,838	14,501	23.3	12,364	17.3
Provisions	3,153	4,989	3,731	2,019	3,330	5.6	2,200	51.4
Loan loss	3,700	4,989	3,580	1,797	3,050	(17.6)	2,200	38.6
Investment depreciation	(480)	(55)	110	206	280	—	—	—
<b>Profit before tax</b>	<b>8,611</b>	<b>8,069</b>	<b>10,015</b>	<b>11,819</b>	<b>11,171</b>	<b>29.7</b>	<b>10,164</b>	<b>9.9</b>
Tax	2,990	2,752	3,455	4,171	3,752	25.5	3,151	19.1
<b>Profit after tax</b>	<b>5,621</b>	<b>5,316</b>	<b>6,560</b>	<b>7,649</b>	<b>7,419</b>	<b>32.0</b>	<b>7,013</b>	<b>5.8</b>
Tax rate (%)	34.7	34.1	34.5	35.3	33.6			
<b>PBT- treasury gains</b>	<b>5,351</b>	<b>5,829</b>	<b>8,315</b>	<b>10,789</b>	<b>9,211</b>	<b>72.1</b>	<b>8,964</b>	<b>2.8</b>
<b>PBT- treasury gains+provisions</b>	<b>8,504</b>	<b>10,818</b>	<b>12,046</b>	<b>12,808</b>	<b>12,541</b>	<b>47.5</b>	<b>11,164</b>	<b>12.3</b>
<b>Key balance sheet items (Rs bn)</b>								
Deposits	1,103	1,156	1,139	1,413	1,475			
Demand deposits	442	495	519	660	592			
Savings	252	280	296	339	347			
Current	190	215	223	322	245			
Term deposits	661	661	619	753	882			
CASA ratio (%)	40.1	42.8	45.6	46.7	40.2			
Customer assets	895	926	934	1,164	1,181			
Loans	781	810	848	1,043	1,086			
Retail loans	168	180	189	208	211			
Non-retail loans	613	631	659	835	875			
SME loans	149	159	165	195	168			
Agricultural loans	75	71	78	115	106			
Retail excld CVs	164	178	187	208	211			
Housing	109	120	134	147	150			
Auto	18	18	26	27	27			
CV	3	2	2	1	—			
Others	10	11	8	9	8			
Investments	463	521	493	560	560			
Total assets	1,411	1,517	1,505	1,806	1,895			
<b>Asset quality</b>								
Gross NPA	9	11	12	13	13			
Net NPA	4	4	4	4	4			
Gross NPA (%)	1.01	1.21	1.23	1.13	1.13			
Net NPA (%)	0.41	0.45	0.46	0.36	0.35			
Provision coverage (calc, %)	59.9	63.2	63.4	68.2	69.2			

Source: Kotak Institutional Equities

Axis Bank-- estimate changes  
March fiscal year-ends, 2011-2012E, Rs mn

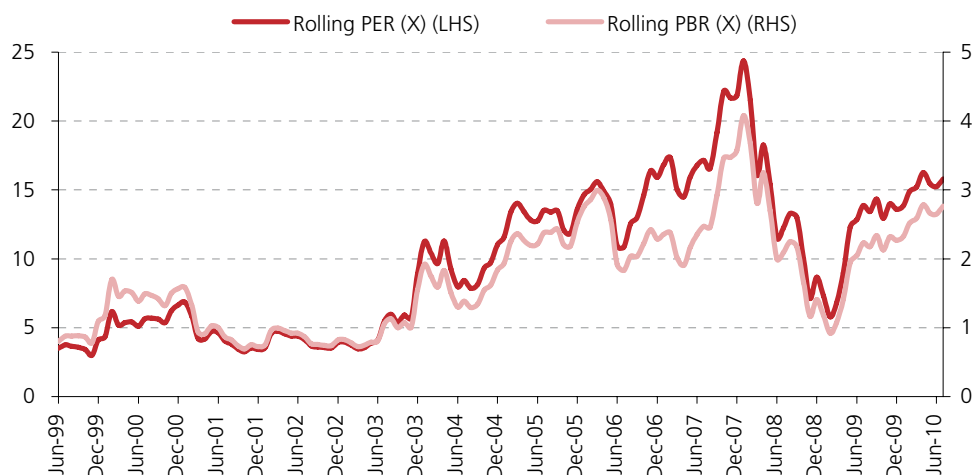
**Axis Bank-- old and new estimates**

	Old estimates		New estimates		% change	
	FY2011E	FY2012E	FY2011E	FY2012E	FY2011E	FY2012E
Net interest income	60,631	75,898	62,607	77,600	3.3	2.2
NIM (%)	3.09	3.15	3.19	3.23	3.3	2.3
Customer assets	1,448,125	1,781,369	1,445,546	1,778,779	(0.2)	(0.1)
Loan loss provisions	11,166	13,266	14,104	14,739	26.3	11.1
Other income	44,656	54,828	45,912	54,292	2.8	(1.0)
Fee income	33,292	41,948	33,348	40,017	0.2	(4.6)
Treasury income	5,000	5,500	5,000	5,500	—	—
Operating expenses	45,611	55,650	45,428	55,429	(0.4)	(0.4)
Employee expenses	15,313	19,042	15,313	19,043	—	—
PBT	48,009	61,111	48,487	61,024	1.0	(0.1)
Tax	16,664	21,212	16,833	21,185	1.0	(0.1)
<b>Net profit</b>	<b>31,345</b>	<b>39,899</b>	<b>31,654</b>	<b>39,838</b>	<b>1.0</b>	<b>(0.2)</b>

Source: Company, Kotak Institutional Equities estimates

**Rolling PER and PBR for Axis Bank**

March fiscal year-ends, June 1999-July 2010 (X)



Source: Company, Kotak Institutional Equities

Axis Bank, growth rates, key ratios and Du Pont analysis, March fiscal year-ends, 2008-2013E (%)

	2008	2009	2010	2011E	2012E	2013E
<b>Growth rates (%)</b>						
Net loan	61.8	36.7	27.9	25.3	25.5	23.1
Total Asset	49.6	34.8	22.3	23.1	21.5	19.8
Deposits	49.1	33.9	20.4	25.3	23.2	20.8
Current	77.3	23.8	29.6	21.1	12.0	20.8
Savings	64.8	29.2	31.1	31.1	23.5	20.7
Fixed	34.6	40.2	12.8	24.5	27.7	20.8
Net interest income	65.0	42.6	35.8	25.1	23.9	19.7
Loan loss provisions	151.4	81.6	56.4	(0.2)	4.5	11.7
Total other income	78.7	60.0	36.2	16.4	18.3	18.2
Net fee income	69.5	64.6	18.0	30.0	20.0	20.0
Net capital gains	261.8	31.0	147.6	(30.0)	10.0	9.1
Net exchange gains	66.2	73.3	30.2	15.0	16.0	16.0
Operating expenses	77.4	32.6	29.8	22.5	22.0	19.2
Employee expenses	75.8	48.8	25.9	21.9	24.4	21.6
<b>Key ratios (%)</b>						
Yield on average earning assets	8.0	8.7	7.3	7.9	8.1	8.2
Yield on average loans	9.8	10.6	8.6	9.0	9.3	9.3
Yield on average investments	7.1	7.7	6.8	7.1	7.4	7.3
Average cost of funds	5.3	6.1	4.5	5.0	5.2	5.3
Interest on deposits	5.1	6.1	4.4	4.9	5.1	5.2
<b>Difference</b>	<b>2.7</b>	<b>2.6</b>	<b>2.9</b>	<b>2.8</b>	<b>2.9</b>	<b>2.8</b>
Net interest income/earning assets	2.9	3.0	3.1	3.2	3.2	3.2
New provisions/average net loans	1.0	1.3	1.5	1.2	1.0	0.9
Interest income/total income	58.8	56.0	55.9	57.7	58.8	59.1
Fee income/total income	30.0	33.0	28.7	30.7	30.3	30.6
Operating expenses/total income	49.0	43.4	41.4	41.9	42.0	42.1
Tax rate	35.0	34.8	34.7	34.7	34.7	34.7
Dividend payout ratio	19.0	19.8	19.3	19.3	19.3	19.3
Share of deposits						
Current	22.9	21.1	22.8	22.0	20.0	20.0
Fixed	54.3	56.9	53.3	52.9	54.9	54.9
Savings	22.8	22.0	24.0	25.1	25.1	25.1
Loans-to-deposit ratio	68.1	69.5	73.8	73.8	75.2	76.7
Equity/assets (EoY)	8.0	6.9	8.9	8.3	8.0	7.8
<b>Dupont analysis (%)</b>						
Net interest income	2.8	2.9	3.0	3.1	3.1	3.1
Loan loss provisions	0.5	0.7	0.9	0.7	0.6	0.6
Net other income	2.0	2.3	2.4	2.3	2.2	2.2
Operating expenses	2.4	2.2	2.3	2.3	2.3	2.2
Invnt. depreciation	—	—	(—)	—	—	—
(1- tax rate)	65.0	65.2	65.3	65.3	65.3	65.3
ROA	1.2	1.4	1.5	1.6	1.6	1.6
Average assets/average equity	15.0	13.6	12.5	11.7	12.3	12.7
ROE	17.6	19.1	19.2	18.3	19.9	20.6

Source: Company, Kotak Institutional Equities estimates

Axis Bank, income statement and balance sheet, March fiscal year-ends 2008-2013E, Rs mn

	2008	2009	2010	2011E	2012E	2013E
<b>Income statement (Rs mn)</b>						
Total interest income	70,053	108,355	116,380	153,711	194,570	236,746
Loans	47,457	74,659	79,866	106,257	137,320	170,211
Investments	21,023	30,515	34,283	43,697	54,450	63,354
Total interest expense	44,200	71,493	66,335	91,103	116,969	143,895
Deposits from customers	37,425	62,089	57,145	78,745	101,615	125,491
Net interest income	25,853	36,862	50,045	62,607	77,600	92,851
Loan loss provisions	4,975	9,032	14,126	14,104	14,739	16,467
Net interest income (after prov.)	20,879	27,830	35,919	48,503	62,861	76,384
Other income	18,107	28,969	39,458	45,912	54,292	64,199
Net fee income	13,207	21,733	25,652	33,348	40,017	48,021
Net capital gains	2,203	2,884	7,140	5,000	5,500	6,000
Net exchange gains	2,075	3,595	4,681	5,383	6,244	7,243
Operating expenses	21,549	28,582	37,097	45,428	55,429	66,048
Employee expenses	6,702	9,977	12,558	15,313	19,043	23,148
Depreciation on investments	65	1,078	(222)	—	—	—
Other provisions	754	(716)	(15)	500	700	700
Pretax income	16,465	27,855	38,517	48,487	61,024	73,836
Tax provisions	5,755	9,701	13,372	16,833	21,185	25,633
<b>Net Profit</b>	<b>10,710</b>	<b>18,154</b>	<b>25,145</b>	<b>31,654</b>	<b>39,838</b>	<b>48,202</b>
% growth	62.5	69.5	38.5	25.9	25.9	21.0
<b>PBT+provisions-treasury</b>	<b>20,208</b>	<b>34,364</b>	<b>45,265</b>	<b>58,091</b>	<b>70,963</b>	<b>85,002</b>
% growth	52.4	75.1	25.7	38.6	27.7	22.2
<b>Balance sheet (Rs mn)</b>						
Cash and bank balance	125,042	150,169	152,064	174,631	198,703	225,383
Cash	15,203	15,415	19,007	20,908	22,998	25,298
Balance with RBI	57,853	78,777	75,732	96,398	118,379	142,759
Balance with banks	11,181	5,406	7,916	7,916	7,916	7,916
Net value of investments	337,051	463,304	559,748	686,934	804,295	930,998
Govt. and other securities	201,788	284,182	341,959	467,449	582,690	706,743
Shares	5,856	4,201	5,296	5,296	5,296	5,296
Debentures and bonds	108,212	133,797	138,233	138,233	138,233	138,233
Net loans and advances	596,611	815,568	1,043,431	1,307,313	1,640,546	2,018,729
Fixed assets	9,229	10,729	12,224	14,966	17,488	18,422
Net owned assets	8,864	10,729	12,224	14,966	17,488	18,422
Other assets	27,845	37,451	39,011	40,634	42,325	44,086
<b>Total assets</b>	<b>1,095,778</b>	<b>1,477,220</b>	<b>1,806,478</b>	<b>2,224,479</b>	<b>2,703,357</b>	<b>3,237,618</b>
Deposits	876,262	1,173,741	1,413,002	1,770,348	2,180,467	2,633,427
Borrowings and bills payable	111,556	174,566	200,800	236,943	274,854	318,831
Other liabilities	20,253	26,765	32,230	32,230	32,230	32,230
<b>Total liabilities</b>	<b>1,008,072</b>	<b>1,375,072</b>	<b>1,646,032</b>	<b>2,039,522</b>	<b>2,487,552</b>	<b>2,984,488</b>
Paid-up capital	3,577	3,590	4,052	4,052	4,052	4,052
Reserves & surplus	84,130	98,558	156,394	180,905	211,753	249,078
<b>Total shareholders' equity</b>	<b>87,707</b>	<b>102,148</b>	<b>160,446</b>	<b>184,957</b>	<b>215,805</b>	<b>253,130</b>

Source: Company, Kotak Institutional Equities estimates

**Good quarter; valuations leave little upside.** 14% volume growth in toothpaste is a result of successful market development activities by Colgate, in our view. 1QFY11 – impressive sales growth, the cost line items are not comparable as the company merged the contract manufacturing facilities. We are surprised at the level of overheads savings (EBITDA margin expansion of 380 bps) due to integration of contract manufacturing facilities in Goa and would seek clarity from management on the sustainability of same.

### Company data and valuation summary

Colgate-Palmolive (India)

Stock data		Forecasts/Valuations			
		2010	2011E	2012E	
52-week range (Rs) (high,low)	868-550	EPS (Rs)	31.1	34.5	39.6
Market Cap. (Rs bn)	114.9	EPS growth (%)	44.2	10.9	14.6
Shareholding pattern (%)		P/E (X)	27.1	24.5	21.4
Promoters	51.0	Sales (Rs bn)	19.6	22.5	25.7
FIs	15.5	Net profits (Rs bn)	4.2	4.7	5.4
MFs	1.3	EBITDA (Rs bn)	5.0	6.1	7.0
Price performance (%)		EV/EBITDA (X)	22.2	18.1	15.5
Absolute	1M 3M 12M	ROE (%)	156.1	132.3	129.4
Rel. to BSE-30	(0.7) 16.2 5.0	Div. Yield (%)	2.4	3.1	3.5

### 1QFY11: Volume growth of 14% impressive, cost line items not comparable due to merger impact

Colgate reported sales of Rs5.3 bn (+13%, KIE estimate Rs5.3 bn), EBITDA of Rs1.6 bn (+30%, KIE estimate of Rs1.5 bn) and PAT Rs1.2 bn (+19%, KIE estimate of Rs1.1 bn). The cost line items are not comparable as the company merged the contract manufacturing facilities—the full impact was effected in this quarter. The company had also booked the savings due to integration of factories in Goa (likely reversal of provisions as well).

During the quarter, Colgate's toothpaste volumes grew 14%; adspends as a percentage of sales were marginally higher at 13.1% versus 12.5% in 1QFY10 (typically adspends in 1Q is the lowest in the year due to phasing issues; 2Q and 3Q are higher as the company invests in 'Oral Health Month' program in October).

### Maintain REDUCE

We are surprised at the level of overheads savings (contributing to EBITDA expansion of 380 bps) due to integration of contract manufacturing facilities in Goa and would seek clarity from management on the sustainability of same. While we like the market development activities undertaken by the company, our key worries remain, (1) premium valuations for sub-par earnings growth in FY2010-12E (12% EPS growth forecast, stock trades at 22X FY2012E), (2) deterioration in competitive position as effective excise rates increases, (3) limited pricing power, (4) mix deterioration (faster growth in Cibaca) and (5) higher tax rates (excise and income tax) starting from FY2011E.

### North East and Sikkim offer opportunities for capacity expansion

Industry sources indicate that North East and Sikkim are likely to emerge as manufacturing destinations (post the expiration of benefits in Himachal and Uttaranchal on March 31, 2010) with 100% excise and income tax benefits. In our view, consumer companies may consider setting up new facilities in Assam / Sikkim to take advantage of fiscal benefits, particularly companies in high-value, low-volume businesses (personal care products, mostly).

## REDUCE

JULY 15, 2010

### RESULT

Coverage view: **Attractive**

Price (Rs): **845**

Target price (Rs): **830**

BSE-30: **17,909**

### QUICK NUMBERS

- **Toothpaste volume growth of 14%, as expected**
- **Toothpowder volumes declined**

Manoj Menon  
manoj.menon@kotak.com  
Mumbai: +91-22-6634-1391

Amrita Basu  
amrita.basu@kotak.com  
Mumbai: +91-22-6634-1147

Kotak Institutional Equities Research  
kotak.research@kotak.com  
Mumbai: +91-22-6634-1100



**Modest change in estimates**

We have marginally increased our EPS estimates for FY2010-12E by 4% as we model further cost savings due to more in-house production and integration of facilities. We have increased our target price to Rs830 (Rs760 previously) in line with earnings revision and rollover to FY2012E. Key risks to our REDUCE rating are (1) muted competitive activity, which would provide pricing power to Colgate, (2) any inorganic activity or expansion of capacity in tax-exempt locations and (3) higher-than-expected volume growth.

## Interim results of Colgate Palmolive India Ltd, March fiscal year-ends (Rs mn)

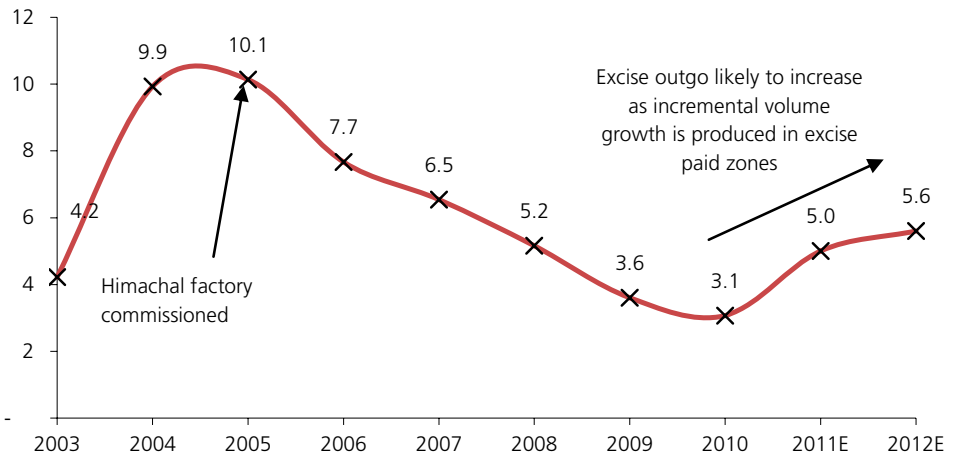
	1QFY11	1QFY11E	1QFY10	4QFY10	(% chg)		
					1QFY11E	1QFY10	4QFY10
<b>Net sales</b>	<b>5,288</b>	<b>5,360</b>	<b>4,680</b>	<b>5,166</b>	<b>(1)</b>	<b>13</b>	<b>2</b>
Operational other income	209	192	174	194		20	8
<b>Net revenue</b>	<b>5,497</b>	<b>5,552</b>	<b>4,854</b>	<b>5,360</b>	<b>(1)</b>	<b>13</b>	<b>3</b>
Total expenditure	3,898	4,075	3,628	3,919	(4)	7	(1)
Material cost	1,966	2,119	2,050	1,543	(7)	(4)	27
Staff cost	444	408	391	421	9	14	5
Advertising & promotion	694	734	583	834	(5)	19	(17)
Other expenditure	795	815	605	1,121	(3)	31	(29)
<b>EBITDA</b>	<b>1,599</b>	<b>1,476</b>	<b>1,226</b>	<b>1,441</b>	<b>8</b>	<b>30</b>	<b>11</b>
<b>OPM (%)</b>	<b>29.1</b>	<b>26.6</b>	<b>25.3</b>	<b>26.9</b>			
<b>EBITDA excl other oper income</b>	<b>1,390</b>	<b>1,285</b>	<b>1,052</b>	<b>1,247</b>	<b>8</b>	<b>32</b>	<b>11</b>
Other income	54	108	86	28		(37)	93
Interest	3	3	5	4		(24)	(15)
Depreciation	79	102	56	206		41	(61)
<b>Pretax profits</b>	<b>1,570</b>	<b>1,479</b>	<b>1,251</b>	<b>1,259</b>	<b>6</b>	<b>26</b>	<b>25</b>
Tax	350	359	223	10	(3)	57	3,438
<b>Net income</b>	<b>1,220</b>	<b>1,119</b>	<b>1,028</b>	<b>1,249</b>	<b>9</b>	<b>19</b>	<b>(2)</b>
Extraordinary items	—	—	-	(105)			
<b>Reported PAT</b>	<b>1,220</b>	<b>1,119</b>	<b>1,028</b>	<b>1,144</b>	<b>9</b>	<b>19</b>	<b>7</b>
Income tax rate (%)	22.3	24.3	17.8	0.8			
<b>Cost as a % of sales</b>							
Material cost	37.2	39.5	43.8	29.9			
Staff cost	8.4	7.6	8.3	8.1			
Advertising & promotion	13.1	13.7	12.5	16.1			
Other expenditure	15.0	15.2	12.9	21.7			

Note:

(a) 1QFY11 numbers are not comparable due to merger of contract manufacturing units (acquired) wef April 1, 2009.

Source: Company, Kotak Institutional Equities estimates

**Excise outgo will increase as incremental volumes go to excise-paid zones**  
 Excise as % of gross sales



Source: Company, Kotak Institutional Equities estimates

Colgate: Profit model, balance sheet, cash model 2006-2012E, March fiscal year-ends (Rs mn)

	2006	2007	2008	2009	2010	2011E	2012E
<b>Profit model (Rs mn)</b>							
<b>Net sales</b>	<b>11,239</b>	<b>12,892</b>	<b>14,683</b>	<b>16,942</b>	<b>19,622</b>	<b>22,493</b>	<b>25,723</b>
<b>EBITDA</b>	<b>2,018</b>	<b>2,089</b>	<b>2,295</b>	<b>2,665</b>	<b>4,254</b>	<b>5,243</b>	<b>6,129</b>
Other income	196	670	848	1,078	985	1,268	1,401
Interest	(6)	(10)	(14)	(11)	(15)	(12)	(14)
Depreciation	(149)	(153)	(198)	(229)	(376)	(401)	(437)
Pretax profits	2,059	2,596	2,930	3,502	4,848	6,098	7,079
Tax	(558)	(606)	(607)	(567)	(615)	(1,405)	(1,700)
<b>PAT</b>	<b>1,501</b>	<b>1,990</b>	<b>2,324</b>	<b>2,935</b>	<b>4,233</b>	<b>4,693</b>	<b>5,379</b>
<b>Earnings per share (Rs)</b>	<b>11.0</b>	<b>14.6</b>	<b>17.1</b>	<b>21.6</b>	<b>31.1</b>	<b>34.5</b>	<b>39.6</b>
<b>Balance sheet (Rs mn)</b>							
Total equity	2,711	2,805	1,622	2,163	3,261	3,827	4,475
Total borrowings	44	43	47	47	46	46	46
Current liabilities	3,511	4,226	5,342	5,513	5,515	6,603	7,687
<b>Total liabilities and equity</b>	<b>6,265</b>	<b>7,074</b>	<b>7,011</b>	<b>7,723</b>	<b>8,822</b>	<b>10,476</b>	<b>12,208</b>
Cash	880	1,117	1,443	2,511	3,476	4,875	6,315
Current assets	2,135	2,447	2,574	2,866	2,426	2,682	2,911
Total fixed assets	1,691	1,920	1,990	1,786	2,531	2,530	2,593
Investments	1,559	1,590	1,004	560	389	389	389
<b>Total assets</b>	<b>6,265</b>	<b>7,074</b>	<b>7,011</b>	<b>7,723</b>	<b>8,822</b>	<b>10,476</b>	<b>12,208</b>
<b>Free cash flow (Rs mn)</b>							
Operating cash flow	1,348	1,411	2,015	3,137	4,003	4,692	5,199
Working capital	427	71	163	(204)	754	395	630
Capital expenditure	(332)	(600)	(290)	76	(1,123)	(400)	(500)
<b>Free cash flow</b>	<b>1,443</b>	<b>883</b>	<b>1,889</b>	<b>3,008</b>	<b>3,634</b>	<b>4,687</b>	<b>5,330</b>
<b>Key assumptions, growth %</b>							
Revenue growth	17.0	14.7	13.9	15.4	15.8	14.6	14.4
EBITDA margin(%)	18.0	16.2	15.6	15.7	21.7	23.3	23.8
EPS growth	23.6	32.6	16.7	26.3	44.2	10.9	14.6

Source: Company, Kotak Institutional Equities estimates

JULY 15, 2010

#### RESULT

Coverage view: **Cautious**

Price (Rs): **454**

Target price (Rs): **380**

BSE-30: **17,909**

**Better-than-expected results but valuations hard to justify.** Castrol reported better-than-expected 2QCY10 results with net income at Rs1.5 bn (+17% yoy) versus our estimate of Rs1.24 bn. The positive variance was due to lower-than-expected raw material cost which resulted in better-than-expected EBITDA margins. The yoy increase in earnings was led by (1) higher sales volumes at 60.2 mn liters (+7.5% yoy) and (2) higher gross realization at Rs124/liter versus Rs114/liter in 2QCY09. We maintain REDUCE rating on Castrol noting the stock is trading at 21.4X CY2011E EPS and 19% above our 12-month target price of Rs380.

#### Company data and valuation summary

Castrol India (a)

Stock data		Forecasts/Valuations			
		2010	2011E	2012E	
52-week range (Rs) (high,low)	466-182	EPS (Rs)	15.4	20.7	21.2
Market Cap. (Rs bn)	112.2	EPS growth (%)	44.6	34.1	2.4
<b>Shareholding pattern (%)</b>		P/E (X)	29.4	22.0	21.5
Promoters	25.1	Sales (Rs bn)	23.2	27.9	29.3
FIs	45.2	Net profits (Rs bn)	3.8	5.1	5.2
MFs	9.6	EBITDA (Rs bn)	6.1	7.9	8.2
<b>Price performance (%)</b>		EV/EBITDA (X)	17.5	13.6	13.1
Absolute	1M 3M 12M	ROE (%)	83.8	107.4	103.7
Rel. to BSE-30	8.9 19.2 143.9	Div. Yield (%)	2.8	3.6	3.7
	5.9 17.4 94.1				

#### Strong margins boosted by lower-than-expected raw material costs

Castrol reported 2QCY10 net income at Rs1.5 bn (+28.2% qoq, +17.1% yoy) versus our expected Rs1.24 bn. The positive variance was due to (1) lower-than-expected raw material cost and (2) moderately higher-than-expected realization. Revenues increased to Rs7.46 bn (+16.5% yoy) due to (1) higher volumes at 60.2 mn liters versus 56 mn liters in 2QCY09 and (2) higher realizations at Rs123.9/liter versus Rs114.3/liter in 2QCY09. Castrol's 2QCY10 EBITDA margin was at 30.4% versus 31% in 2QCY09. We highlight that qoq results comparison is not valid due to seasonality; 2Q and 4Q in a calendar year are the best quarters.

#### Valuations running ahead of fundamentals; retain REDUCE

We currently assume an EBITDA margin of 26.6% for CY2011E which is higher than Castrol's EBITDA margin of 24.8% in CY2009 and an average EBITDA margin of 16.4% over CY2001-08. We note that our revised 12-month target price of Rs380 (Rs365 previously) is based on 18X CY2011E EPS. We also note that the stock has historically traded in a P/E band of 14-18X (see Exhibit 2). The current valuations reflect a situation of ascribing an all-time high multiple to peak level of earnings. We believe that the stock provides unfavorable risk-reward balance at current levels and would advise investors to book profits and wait for better opportunities at lower levels to get back in.

#### Fine-tuned earnings; revised target price to Rs380

We have fine-tuned our CY2010E and CY2011E EPS estimates to Rs20.7 and Rs21.2 from Rs19.6 and Rs20.6 to reflect (1) higher sales volumes (+ve impact), (2) lower LOBS prices (+ve impact), (3) moderately higher realizations (+ve impact), (4) weaker rupee (-ve impact) and (5) other changes to reflect 2QCY10 results. We have revised our target price to Rs380 from Rs365 previously based on 18X CY2011E EPS of Rs21.2. The upward revision in target price reflects (1) roll-forward to CY2011E and (2) upward revision of earnings.

#### QUICK NUMBERS

- Volumes higher by 7.5% yoy
- 2QCY10 EBITDA margin at 30.4% versus 31% in 2QCY09
- Castrol stock has outperformed Sensex by 17.4% in past three months

Gundeep Singh  
gundeep.singh@kotak.com  
Mumbai: +91-22-6634-1286

Sanjeev Prasad  
sanjeev.prasad@kotak.com  
Mumbai: +91-22-6634-1229

Tarun Lakhotia  
tarun.lakhotia@kotak.com  
Mumbai: +91-22-6634-1188

Kotak Institutional Equities Research  
kotak.research@kotak.com  
Mumbai: +91-22-6634-1100

## Interim results of Castrol, calendar year-ends (Rs mn)

	2QCY10	2QCY10E	2QCY09	1QCY10	(% chg.)			yoy			2010E
					2QCY10E	2QCY09	1QCY10	1HCY10	1HCY09	(% chg.)	
<b>Net sales</b>	<b>7,458</b>	<b>7,378</b>	<b>6,402</b>	<b>6,560</b>	<b>1.1</b>	<b>16.5</b>	<b>13.7</b>	<b>14,018</b>	<b>11,489</b>	<b>22.0</b>	<b>27,919</b>
Raw materials	3,621	3,965	2,810	3,224	(8.7)	28.9	12.3	6,845	5,547	23.4	14,054
Employees	244	225	296	216	8.4	(17.6)	13.0	460	572	(19.6)	920
Others	1,328	1,340	1,313	1,320	(0.9)	1.1	0.6	2,648	2,235	18.5	5,380
Advertisement	361		426	464		(15.3)	(22.2)	825	633	30.3	—
CIF costs	227		181	220		25.4	3.2	447	344	29.9	—
Other exp	740		706	636		4.8	16.4	1,376	1,258	9.4	—
Total expenditure	5,193	5,530	4,419	4,760	(6.1)	17.5	9.1	9,953	8,354	19.1	20,354
<b>EBITDA</b>	<b>2,265</b>	<b>1,848</b>	<b>1,983</b>	<b>1,800</b>	<b>22.6</b>	<b>14.2</b>	<b>25.8</b>	<b>4,065</b>	<b>3,135</b>	<b>29.7</b>	<b>7,565</b>
<b>EBITDA margin (%)</b>	<b>30.4</b>	<b>25.0</b>	<b>31.0</b>	<b>27.4</b>				<b>29.0</b>	<b>27.3</b>		<b>27.1</b>
Other income	73	80	66	81	(8.8)	10.6	(9.9)	154	161	(4.3)	375
Interest	6	15	6	5	(60.0)	—	20.0	11	15	(26.7)	20
Depreciation	60	60	67	58	—	(10.4)	3.4	118	133	(11.3)	268
<b>Pre-tax profits</b>	<b>2,272</b>	<b>1,853</b>	<b>1,976</b>	<b>1,818</b>	<b>22.6</b>	<b>15.0</b>	<b>25.0</b>	<b>4,090</b>	<b>3,148</b>	<b>29.9</b>	<b>7,652</b>
Extraordinaries	—	—	—	—				—	—		—
Tax	769	615	692	646	24.9	11.1	19.0	1,415	1,101	28.5	2,589
Deferred tax	—	—	—	—				—	—		(47)
<b>Net income</b>	<b>1,503</b>	<b>1,237</b>	<b>1,284</b>	<b>1,172</b>	<b>21.5</b>	<b>17.1</b>	<b>28.2</b>	<b>2,675</b>	<b>2,047</b>	<b>30.7</b>	<b>5,110</b>
<b>Adjusted net income</b>	<b>1,503</b>	<b>1,237</b>	<b>1,284</b>	<b>1,172</b>	<b>21.5</b>	<b>17.1</b>	<b>28.2</b>	<b>2,675</b>	<b>2,047</b>	<b>30.7</b>	<b>5,110</b>
Effective tax rate (%)	33.8	33.2	35.0	35.5				34.6	35.0		33.2
<b>Other details</b>											
Sales volumes (mn lt)	60.2	60.5	56.0	54.6	(0.5)	7.5	10.3	114.8	101.2	13.4	227.6
Gross realization (Rs/lt)	123.9	121.9	114.3	120.1	1.6	8.4	3.1	122.1	113.5	7.6	122.6
Raw material (Rs/lt)	60.1	65.5	50.2	59.0	(8.2)	19.9	1.9	59.6	54.8	8.8	60.4
<b>Segment details</b>											
<b>Revenues</b>											
Automotive	6,507		5,615	5,664		15.9	14.9	12,171	9,996	21.8	
Non-automotive	933		760	876		22.8	6.5	1,809	1,438	25.8	
<b>Total</b>	<b>7,440</b>		<b>6,375</b>	<b>6,540</b>		<b>16.7</b>	<b>13.8</b>	<b>13,980</b>	<b>11,434</b>	<b>22.3</b>	
<b>EBIT</b>											
Automotive	1,937		1,707	1,506		13.5	28.6	3,443	2,689	28.0	
Non-automotive	286		232	256		23.3	11.7	542	385	40.8	
<b>Total</b>	<b>2,223</b>		<b>1,939</b>	<b>1,762</b>		<b>14.6</b>	<b>26.2</b>	<b>3,985</b>	<b>3,074</b>	<b>29.6</b>	
<b>EBIT margin (%)</b>											
Automotive	29.8		30.4	26.6				28.3	26.9		
Non-automotive	30.7		30.5	29.2				30.0	26.8		
<b>Total</b>	<b>29.9</b>		<b>30.4</b>	<b>26.9</b>				<b>28.5</b>	<b>26.9</b>		
<b>Capital employed</b>											
Automotive	1,519		1,571	1,973		(3.3)	(23.0)	1,519	1,571	(3.3)	
Non-automotive	911		871	893		4.6	2.0	911	871	4.6	
Unallocable assets less liabilities	3,183		2,914	3,256		9.2	(2.2)	3,183	2,914	9.2	
<b>Total</b>	<b>5,613</b>		<b>5,356</b>	<b>6,122</b>		<b>4.8</b>	<b>(8.3)</b>	<b>5,613</b>	<b>5,356</b>	<b>4.8</b>	

Source: Company, Kotak Institutional Equities estimates

Castrol stock has historically traded at 14-18X forward earnings  
12-month forward P/E for Castrol India



Source: Bloomberg, Company, Kotak Institutional Equities estimates

### Automotive segment volumes remain strong; modest yoy decline in margins

Castrol's 2QCY10 automotive lubes segment's revenues increased 15.9% yoy to Rs6.5 bn led by (1) increase in volumes and (2) higher realization. EBIT increased 13.5% yoy to Rs1.9 bn. The automotive segment's EBIT margin was at 29.8% in 2QCY10 compared 30.4% in 2QCY09.

### Industrial segment maintains its strong performance

Castrol's industrial lubes segment reported 22.8% yoy growth in revenues to Rs933 mn. EBIT increased 23.3% yoy to Rs286 mn. Industrial segment's EBIT margin was at 30.7% in 2QCY10 compared to 30.5% in 2QCY09.

### Other key details of 1QCY10 results

- ▶ **Modest increase in raw material cost qoq.** We are surprised by a modest 2% qoq increase in unit raw material cost to Rs60.1/liter versus Rs59/liter in 1QCY10. This increase in raw material cost is modest compared to 8-9% qoq increase in global LOBS prices (across various grades). The management attributed this to its strong procurement capabilities which enabled it to source cargoes at attractive prices.
- ▶ **Higher realization qoq.** Castrol's 1QCY10 gross realization was at Rs124/liter versus Rs120/liter in 1QCY10 and Rs114/liter in 2QCY09. The yoy increase in realization reflects the price hikes effected by the company in January 2010. The management attributed the qoq increase in gross realization to a better product mix.

### Key assumptions

Exhibit 3 gives our key assumptions for our earnings. We discuss the same in detail below.

## Castrol: Key assumptions, December year-ends, 2004-2012E

	2004	2005	2006	2007	2008	2009	2010E	2011E	2012E
<b>Volume (Kilo litres)</b>									
Industrial grades	50,306	50,788	50,585	43,773	31,928	28,003	30,804	31,728	32,362
Automotive grades	173,277	174,936	174,236	175,093	180,927	174,919	195,034	198,935	202,914
Traded items	621	747	1,055	1,114	1,723	1,614	1,808	1,808	1,808
<b>Total</b>	<b>224,204</b>	<b>226,471</b>	<b>225,875</b>	<b>219,980</b>	<b>214,578</b>	<b>204,536</b>	<b>227,646</b>	<b>232,470</b>	<b>237,084</b>
<b>Growth (%)</b>	<b>5.8</b>	<b>1.0</b>	<b>(0.3)</b>	<b>(2.6)</b>	<b>(2.5)</b>	<b>(4.7)</b>	<b>11.3</b>	<b>2.1</b>	<b>2.0</b>
<b>Raw material prices (US\$/ton)</b>									
<b>LOBS prices</b>	<b>423</b>	<b>520</b>	<b>815</b>	<b>786</b>	<b>1,041</b>	<b>721</b>	<b>890</b>	<b>930</b>	<b>950</b>
<b>Macro assumptions</b>									
INR/US\$	45.3	44.1	45.3	41.3	43.6	48.4	46.0	46.0	46.0
<b>Realization (Rs/lt)</b>									
Gross realization	58.2	63.2	77.6	85.8	102.8	113.3	122.6	126.2	128.6
Raw material cost	34.6	39.1	53.3	48.5	62.1	52.2	60.4	63.2	64.6
<b>Net realization</b>	<b>23.6</b>	<b>24.1</b>	<b>24.2</b>	<b>37.3</b>	<b>40.7</b>	<b>61.1</b>	<b>62.2</b>	<b>63.0</b>	<b>64.0</b>

Source: Company, Kotak Institutional Equities estimates

- ▶ **Volumes.** We currently model 11.3% yoy increase in sales volumes in CY2010E. We note that the company achieved a volume growth of 13.4% yoy in 1HCY10. We model a 2.1% yoy increase in sales volumes in CY2011E.
- ▶ **Lubes prices.** We model lube realizations to increase by 8.2% in CY2010E to reflect the price hikes taken by Castrol in January 2010. However, the company has not effected any price changes post-Budget to pass through the higher import duty of 10.3% on base oils.
- ▶ **LOBS prices.** We model CY2010E LOBS prices at US\$890/ton (+US\$169/ton yoy) to reflect higher crude prices yoy. We model yoy increase of US\$40/ton in LOBS prices in CY2011E.
- ▶ **Exchange rate assumption.** We have revised our exchange rate assumptions for CY2010E and CY2011E to Rs46/US\$ and Rs46/US\$ versus Rs45/US\$ and Rs45.3/US\$.

### Key risks—weakening rupee and higher diesel prices

We see downside risk to Castrol's earnings from (1) weakening of rupee and (2) lower lubes consumption due to higher diesel prices. A Re1/US\$ increase would reduce Castrol's CY2010E and CY2011E EPS to Rs20.1 (-2.5%) and Rs20.6 (-2.6%). In addition, the recent hike in diesel prices by Rs2/liter may hurt the economics of freight operators who may delay consumption of replacement products such as lubes and tyres.

Castrol has high leverage to exchange rate and raw material prices

Sensitivity of Castrol's earnings to key variables

	CY2010E			CY2011E			CY2012E		
	Downside	Base case	Upside	Downside	Base case	Upside	Downside	Base case	Upside
<b>Exchange rate</b>									
Rupee dollar	47.0	46.0	45.0	47.0	46.0	45.0	47.0	46.0	45.0
Net profits (Rs mn)	4,982	5,110	5,238	5,093	5,231	5,368	5,220	5,363	5,507
EPS (Rs)	20.1	20.7	21.2	20.6	21.2	21.7	21.1	21.7	22.3
<b>% upside/(downside)</b>	<b>(2.5)</b>		<b>2.5</b>	<b>(2.6)</b>		<b>2.6</b>	<b>(2.7)</b>		<b>2.7</b>
<b>Raw material price</b>									
Raw material price (US\$/ton)	915	890	865	955	930	905	975	950	925
Net profits (Rs mn)	4,945	5,110	5,276	5,061	5,231	5,401	5,189	5,363	5,537
EPS (Rs)	20.0	20.7	21.3	20.5	21.2	21.8	21.0	21.7	22.4
<b>% upside/(downside)</b>	<b>(3.2)</b>		<b>3.2</b>	<b>(3.3)</b>		<b>3.3</b>	<b>(3.2)</b>		<b>3.2</b>

Source: Kotak Institutional Equities estimates

Castrol: Profit model, balance sheet, cash model, calendar year-ends, 2004-2012E (Rs mn)

	2004	2005	2006	2007	2008	2009	2010E	2011E	2012E
<b>Profit model (Rs mn)</b>									
Net sales	13,051	14,304	17,524	18,883	22,057	23,182	27,919	29,338	30,499
<b>EBITDA</b>	<b>2,082</b>	<b>2,117</b>	<b>2,200</b>	<b>3,296</b>	<b>3,997</b>	<b>5,754</b>	<b>7,565</b>	<b>7,795</b>	<b>7,972</b>
Other income	221	201	344	348	418	361	375	400	425
Interest	(29)	(30)	(41)	(38)	(37)	(35)	(20)	(50)	(50)
Depreciation	(249)	(189)	(180)	(208)	(257)	(272)	(268)	(313)	(316)
Pretax profits	2,026	2,098	2,322	3,398	4,122	5,808	7,652	7,833	8,031
Tax	(687)	(694)	(889)	(1,455)	(1,568)	(2,075)	(2,589)	(2,663)	(2,734)
Deferred taxation	9	56	57	236	86	78	47	61	66
<b>Net profits</b>	<b>1,275</b>	<b>1,468</b>	<b>1,545</b>	<b>2,184</b>	<b>2,624</b>	<b>3,811</b>	<b>5,110</b>	<b>5,231</b>	<b>5,363</b>
<b>Earnings per share (Rs)</b>	<b>5.3</b>	<b>5.9</b>	<b>6.1</b>	<b>8.8</b>	<b>10.7</b>	<b>15.4</b>	<b>20.7</b>	<b>21.2</b>	<b>21.7</b>
<b>Balance sheet (Rs mn)</b>									
Total equity	3,601	3,901	4,177	4,302	4,756	4,950	5,303	5,631	5,948
Deferred taxation liability	174	119	61	(182)	(268)	(346)	(393)	(454)	(520)
Total borrowings	37	28	28	28	28	—	—	—	—
Current liabilities	2,830	3,238	3,619	5,116	4,690	6,812	6,587	6,850	7,028
<b>Total liabilities and equity</b>	<b>6,642</b>	<b>7,285</b>	<b>7,885</b>	<b>9,264</b>	<b>9,205</b>	<b>11,416</b>	<b>11,496</b>	<b>12,027</b>	<b>12,456</b>
Cash	297	399	892	3,179	2,556	5,258	4,458	4,858	5,220
Current assets	3,558	4,422	5,271	4,546	5,199	4,778	5,781	6,074	6,307
Total fixed assets	1,498	1,383	1,297	1,333	1,445	1,375	1,257	1,094	928
Investments	1,289	1,081	425	206	5	5	—	—	—
<b>Total assets</b>	<b>6,642</b>	<b>7,285</b>	<b>7,885</b>	<b>9,264</b>	<b>9,205</b>	<b>11,416</b>	<b>11,496</b>	<b>12,027</b>	<b>12,456</b>
<b>Free cash flow (Rs mn)</b>									
Operating cash flow, excl. working capital	1,576	1,544	1,403	2,046	2,772	3,834	4,956	5,082	5,189
Working capital	24	(465)	(506)	1,484	(1,193)	1,792	(1,227)	(31)	(55)
Capital expenditure	(57)	(89)	63	(243)	(371)	(344)	(150)	(150)	(150)
<b>Free cash flow</b>	<b>1,542</b>	<b>991</b>	<b>960</b>	<b>3,287</b>	<b>1,208</b>	<b>5,281</b>	<b>3,578</b>	<b>4,902</b>	<b>4,984</b>
Investments	(402)	258	687	224	201	—	5	—	—
Other income	37	25	9	151	210	188	375	400	425
<b>Ratios (%)</b>									
Debt/equity	1.0	0.7	0.7	0.7	0.6	—	—	—	—
Net debt/equity	1.0	0.7	0.7	0.7	0.6	—	—	—	—
RoAE	34.3	37.7	37.4	52.3	61.0	83.8	107.4	103.7	101.1
<b>RoACE</b>	<b>35.7</b>	<b>37.7</b>	<b>37.0</b>	<b>52.4</b>	<b>61.4</b>	<b>84.1</b>	<b>107.7</b>	<b>104.4</b>	<b>101.8</b>
<b>Assumptions</b>									
Volume (mn litres)	224.2	226.5	225.9	220.0	214.6	204.5	227.6	232.5	237.1
Gross realization (Rs/lt)	58.2	63.2	77.6	85.8	102.8	113.3	122.6	126.2	128.6
<b>Net realization (Rs/lt)</b>	<b>23.6</b>	<b>24.1</b>	<b>24.2</b>	<b>37.3</b>	<b>40.7</b>	<b>61.1</b>	<b>62.2</b>	<b>63.0</b>	<b>64.0</b>

Source: Company, Kotak Institutional Equities estimates



JULY 15, 2010

RESULT

Coverage view: **Attractive**

Price (Rs): **1,074**

Target price (Rs): **1,250**

BSE-30: **17,909**

**Business remains in sweet spot; retain positive outlook.** LIC Housing Finance continued to report strong earnings growth on the back of a buoyant real estate market. PAT was up 70% yoy and 11% above estimates. Margins moderated somewhat sequentially, but were higher 55 bps yoy. A strong traction in the retail business will likely drive earnings for LICHF. We revise earnings, retain ADD with a price target of Rs1,250.

#### Company data and valuation summary

LIC Housing Finance

Stock data		Forecasts/Valuations			
		2010	2011E	2012E	
52-week range (Rs) (high,low)	1,083-519	EPS (Rs)	69.7	100.7	109.9
Market Cap. (Rs bn)	102.0	EPS growth (%)	11.5	44.5	9.1
<b>Shareholding pattern (%)</b>		P/E (X)	15.4	10.7	9.8
Promoters	36.5	NII (Rs bn)	9.5	13.0	16.3
FIs	33.8	Net profits (Rs bn)	6.6	9.6	10.4
MFs	13.0	BVPS	341.0	411.0	487.5
<b>Price performance (%)</b>		P/B (X)	3.1	2.6	2.2
Absolute	1M 3M 12M	ROE (%)	23.6	25.5	23.2
Rel. to BSE-30	7.4 24.1 36.1	Div. Yield (%)	1.4	2.0	2.2

**Core earnings above estimates, retain ADD with price target of Rs1,250**

LIC Housing Finance (LICHF) reported core PBT (PBT excluding provisions) at Rs2.9 bn, up 67% yoy and 10% above estimates. Loan growth was strong at 37% yoy and 2% above estimates. Margins were up 55 bps yoy but down 30 bps qoq to 3%.

We are revising our earnings estimates up by 8% for FY2011E and 6% for FY2012E to factor somewhat better margin traction and asset quality performance. We are revising our price target to Rs1,250 from Rs1,050 to factor higher earnings and FY2012E rollover. At our price target, the stock will trade at 2.4X PBR and 11.4X PER FY2012E. We expect LICHF to report RoE of about 23-24% in the near term with 30% CAGR in core PBT between FY2010 and FY2013E.

#### Business going strong

LICHF reported loan growth of 37% in 1QFY11. Disbursements growth moderated to 40% (retail disbursements 32%) on the back of 60% disbursements growth in 1QFY10. Non-retail loan book was flat due to high repayments—the share of non-retail loans decreased to 10% of overall loans from 12% in 4QFY10.

Our real estate analysts team expects revenue from real estate sales (for the industry) to rise by about 40% yoy in FY2011E on the back of strong traction in new property bookings over the last few quarters; this will in turn drive disbursement growth for mortgage finance companies. On the large base, new retail property bookings will likely rise by about 20-25% (will drive retail loan approvals). We are modeling about 27% disbursements growth in FY2011E (25% earlier) and 20% in FY2012E for LICHF. Consequently, we are building loan growth of 35% and 30% in FY2011E and FY2012E, respectively.

#### QUICK NUMBERS

- **PAT up 71% yoy and 11% above estimates**
- **Loan book up 37% yoy**
- **Disbursements up 40%, retail disbursements up 32%**

Nischint Chawathe  
nischint.chawathe@kotak.com  
Mumbai: +91-22-6634-1545

Manish Karwa  
manish.karwa@kotak.com  
Mumbai: +91-22-6634-1350

Kotak Institutional Equities Research  
kotak.research@kotak.com  
Mumbai: +91-22-6634-1100

**Better-than-expected traction in margins despite interest rate risk in the horizon**

LICHF reported higher-than-expected margins of 3.0% (up 55 bps yoy and down 30 bps qoq). Incremental spreads were equal to spreads in its outstanding business, i.e. at 2.2%. The decline in incremental spreads was due to 40 bps qoq rise in borrowings cost and 10 bps decline in yields (due to lower disbursements to the non-retail segment). In light of the current traction, we are now modeling an NIM of 2.7% for FY2011E (2.8% for next nine months versus 3% reported in 1QFY11).

According to the company, a majority of its incremental business is driven by its 'fix-o-floaty' product, i.e. home loan rates fixed at 8.9% (up to March 2012). The company has recently launched a five-year fixed rate home loan product at 9.25%. Incrementally, this product will boost LICHF's asset yield though pose ALM risk. While it may be challenging to tie up back-to-back five-year fixed rate borrowings, the management has highlighted that the share of this product in their overall portfolio may not be very high and they will consciously monitor the ALM risk on account of this product.

**NPL ratio in line**

LICHF reported gross NPLs of 0.9% in June 2010 versus 0.7% in March 2010 and 1.5% in June 2009. NPLs typically decline in 4Q and again rise in 1Q. The company expects to achieve gross NPL ratio of 0.5% by March 2011—lower than our estimate of 0.65%.

**Income from MF sale likely in 2QFY11E**

LICHF expects to realize capital gains of Rs1.4 bn from 17% stake sale in LIC MF. The deal, signed last year, was pending regulatory approvals. Notably, most approvals have been obtained and LIC MF will now issue 30-day intimation to its investors before executing the deal.

LIC Housing Finance  
Quarterly data (Rs mn)

	1Q10	2Q10	3Q10	4Q10	1Q11	YoY (%)	1Q11E	Actual vs KS (%)
Operating income	7,819	8,391	8,805	9,682	10,149	30	11,094	(9)
Interest on loans	7,451	7,854	8,336	9,193	9,716	30	10,654	(9)
Fees and other charges	225	337	369	343	300	33	300	—
Other income	143	200	100	146	134	(7)	140	(5)
Interest expenses	5,709	5,979	6,057	6,214	6,772	19	7,878	(14)
<b>Net operating income</b>	<b>2,110</b>	<b>2,413</b>	<b>2,748</b>	<b>3,469</b>	<b>3,377</b>	<b>60</b>	<b>3,216</b>	<b>5</b>
Total Fund based income	7,594	8,054	8,436	9,339	9,849	30	10,794	(9)
Net interest income	1,742	1,876	2,279	2,980	2,943	69	2,776	6
Other exp.	408	119	566	471	468	15	550	(15)
Establishment exp.	209	392	285	477	230	10	250	(8)
Staff expenses	99	144	123	120	149	50	150	(1)
Provisions	100	(417)	158	(126)	89	(11)	150	(40)
<b>PBDT</b>	<b>1,703</b>	<b>2,294</b>	<b>2,182</b>	<b>2,998</b>	<b>2,909</b>	<b>71</b>	<b>2,666</b>	<b>9</b>
Depreciation	14	16	17	16	15	6	15	1
PBT	1,688	2,278	2,165	2,982	2,893	71	2,651	9
Tax	450	566	629	845	773	72	742	4
<b>PAT</b>	<b>1,238</b>	<b>1,712</b>	<b>1,536</b>	<b>2,137</b>	<b>2,120</b>	<b>71</b>	<b>1,909</b>	<b>11</b>
Tax rate (%)	27	25	29	28	27	—	28	(5)
PBT excl. extraordinary item	1,688	2,416	2,165	2,982	2,893	71	2,651	9
PBT excl. extraordinary item+provisions	1,788	1,999	2,323	2,856	2,983	67	2,801	6

**Other details****Business growth**

Approval for the quarter (Rs bn)	35	54	45	46	53	51	44	21
Disbursements (Rs bn)	24	38	36	51	34	40	33	3
Individual (Rs bn)	23	34	30	38	30	32		
Others (Rs bn)	2	4	6	13	4	155		
Outstanding portfolio (Rs bn)	292	319	342	381	400	37	394	2
Individual (Rs bn)	267	292	313	339	360	35		

**NPLs**

Gross NPLs (Rs mn)	4,416	4,085	4,908	2,632	3,670	(10)		
Gross NPL ratio (%)	1.5	1.3	1.4	0.7	0.9			
Net NPLs (Rs mn)	1,906	1,982	2,636	464	1,398	(29)		

**Capital adequacy**

CAR (%)	13	16	15	15	15			
Tier I	10	12	12	12	10			

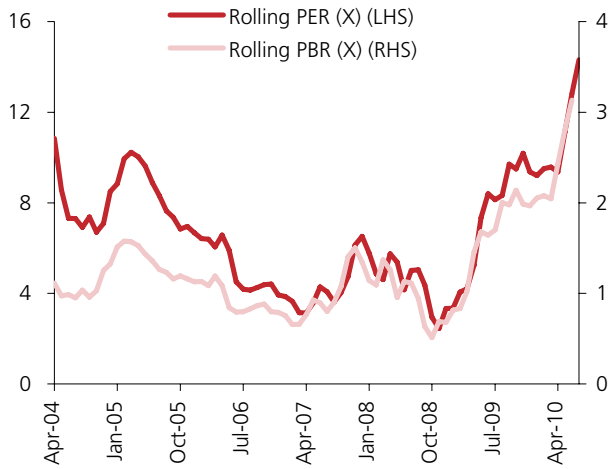
**Spreads/ margins (%)**

NIM( Reported -%)	2.5	2.4	2.8	3.3	3.0			
NIMs (KS estimate- %)	2.5	2.5	2.8	3.3	3.0		2.9	
Average lending rate (%)	10.5	10.0	10.0	10.2	10.1			
Average cost of funds (%)	8.7	8.4	8.1	7.8	7.8			
Average spreads (%)	1.8	1.7	2.0	2.4	2.2			
Incremental lending rate (%)	9.4	9.5	10.0	10.2	9.6			
Incremental cost of fund (%)	7.2	7.2	7.0	7.0	7.5			
Incremental spreads (%)	2.2	2.4	3.0	3.1	2.2			

Source: Company, Kotak Institutional Equities estimates

## Valuations are close to peak

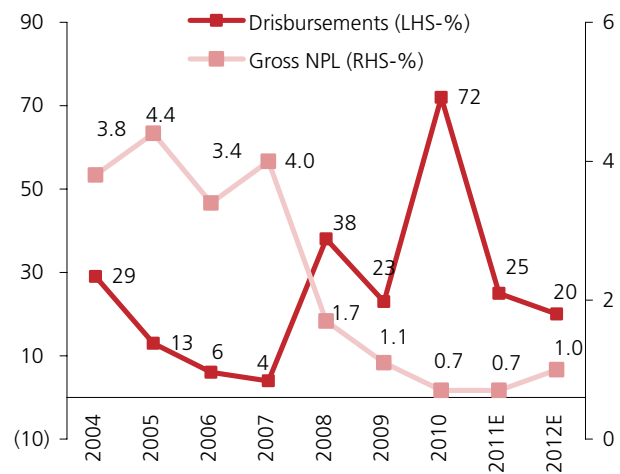
LICHF: Rolling PER and PBR, April 2004-July 2010 (X)



Source: Bloomberg, Company, Kotak Institutional Equities estimates

## ...so is operating performance

LICHF: Growth in disbursements (LHS) and gross NPL ratio (RHS), March fiscal year-ends, 2004-2013E (%)



Source: Company, Kotak Institutional Equities estimates

## LIC Housing Finance- old and new estimates

March fiscal year-ends, 2011-2012E (Rs mn)

	Old estimates		New estimates		Old vs New (%)		YoY(%)	
	2011E	2012E	2011E	2012E	2011E	2012E	2011E	2012E
NIMs(%)	2.6	2.6	2.8	2.7				
Loan growth (%)	33.9	28.8	33.9	29.7				
Net interest income	11,730	15,382	12,415	15,752	6	2	40	27
Other income	3,485	2,441	3,472	2,427	(0)	(1)	85	(30)
Fee income	1,529	1,835	1,528	1,834	(0)	(0)	20	20
Other income	1,956	606	1,943	593	(1)	(2)	220	(69)
Total income	15,216	17,823	15,886	18,179	4	2	48	14
Loan loss provisions	668	1,167	445	878	(33)	(25)	(257)	97
Operating expenses	2,343	2,872	2,355	2,888	1	1	23	23
Employee expenses	567	664	567	664	(0)	—	17	17
Other expenses	1,776	2,209	1,788	2,224	1	1	25	24
PBT	12,204	13,784	13,086	14,413	7	5	44	10
Tax	3,347	3,887	3,518	3,976	5	2	41	13
<b>PAT</b>	<b>8,858</b>	<b>9,896</b>	<b>9,568</b>	<b>10,437</b>	<b>8</b>	<b>5</b>	<b>44</b>	<b>9</b>
<b>PBT bef. Prov, extraordinary</b>	<b>11,523</b>	<b>14,950</b>	<b>12,181</b>	<b>15,291</b>	<b>6</b>	<b>2</b>	<b>38</b>	<b>26</b>
<b>EPS (Rs per share)</b>	<b>93</b>	<b>104</b>	<b>101</b>	<b>110</b>			<b>44</b>	<b>9</b>

Source: Company, Kotak Institutional Equities estimates

LICHF: Key ratios, March fiscal year-ends 2008-2013E

	2008	2009	2010E	2011E	2012E	2013E
<b>Growth (%)</b>						
Total assets	24	24	37	32	29	36
Housing loans	25	26	38	34	30	37
Total borrowings	24	26	36	35	31	38
Net Income before provision	49	27	19	37	26	29
Fee income	9	55	56	20	20	20
Total expenses	19	16	24	23	23	23
PBT	50	37	25	44	10	26
PAT	39	37	25	44	9	23
<b>Spread calculation (%)</b>					0	0
Average cost of funds	8.0	8.8	8.0	8.1	8.4	8.5
Average yield on assets	10.0	10.7	9.6	9.9	10.2	10.3
Spreads	1.9	1.9	1.6	1.8	1.8	1.8
Difference on housing loan	2.3	2.3	2.0	2.1	2.1	2.0
NIM	3.0	3.0	2.7	2.8	2.7	2.6
<b>Other ratios (%)</b>						
Tax rate	27	27	27	27	28	29
Debt/equity (X)	11	12	10	11	13	14
Total expenses/assets	0.6	0.5	0.5	0.4	0.4	0.4
Total expenses/total income	20	18	18	16	16	15
Divd payout ratio	22	22	22	22	22	22
<b>Du Pont analysis (% of average assets)</b>						
Net interest income	3.0	3.0	2.7	2.8	2.7	2.6
Loan loss provisions and Inv pro	0.1	—	(0.1)	0.1	0.1	0.2
Net other income	0.3	0.3	0.4	0.6	0.3	0.3
Gains on securitization	—	—	—	—	—	—
Operating expenses	0.6	0.6	0.6	0.5	0.5	0.4
(1- tax rate)	72.8	73.2	72.7	73.1	72.4	70.7
<b>ROA</b>	<b>1.8</b>	<b>2.0</b>	<b>1.9</b>	<b>2.0</b>	<b>1.7</b>	<b>1.6</b>
Average assets/average equity (X)	12.5	13.0	12.4	12.5	13.5	15.0
<b>ROE (%)</b>	<b>22.9</b>	<b>26.2</b>	<b>23.6</b>	<b>25.5</b>	<b>23.2</b>	<b>23.9</b>

Source: Company, Kotak Institutional Equities estimates

LICHF: Income statement and balance sheet, March fiscal year-ends 2008- 2013E

	2008	2009	2010E	2011E	2012E	2013E
<b>Income statement</b>						
Total income excluding fee income	20,365	27,476	32,827	45,647	61,488	82,186
Other operating income	127	634	597	593	593	593
Interest payable	14,744	20,155	23,957	33,232	45,737	61,754
Provision	243	53	-283	445	878	1,565
Fee income						
<b>Net total income</b>	<b>6,554</b>	<b>8,716</b>	<b>11,023</b>	<b>14,091</b>	<b>17,301</b>	<b>21,661</b>
<b>Total expenses</b>	<b>1,338</b>	<b>1,552</b>	<b>1,920</b>	<b>2,355</b>	<b>2,888</b>	<b>3,545</b>
Staff expenses	345	447	485	567	664	777
Establishment expenses	182	166	131	164	205	256
Other expenses	774	890	1,241	1,551	1,939	2,424
Depreciation	37	49	64	73	80	88
Other income	105	100	10	1,350	—	—
<b>Profit before tax</b>	<b>5,321</b>	<b>7,264</b>	<b>9,112</b>	<b>13,086</b>	<b>14,413</b>	<b>18,116</b>
Tax	1,450	1,948	2,490	3,518	3,976	5,314
<b>Net profit</b>	<b>3,871</b>	<b>5,316</b>	<b>6,622</b>	<b>9,568</b>	<b>10,437</b>	<b>12,801</b>
EPS (Rs)	46	63	70	101	110	135
BVPS (Rs)	215.5	262.0	356.6	432.0	514.3	615.1
ABVPS (Rs)	184	233	341	411	488	587
<b>Balance sheet</b>						
<b>Disbursements</b>	<b>70,710</b>	<b>86,800</b>	<b>149,000</b>	<b>189,975</b>	<b>227,970</b>	<b>341,955</b>
YoY growth (%)	38	23	72	28	76,479	99,202
<b>Net loans</b>	<b>219,360</b>	<b>276,793</b>	<b>380,814</b>	<b>509,859</b>	<b>661,350</b>	<b>904,102</b>
<b>Total Investments</b>	<b>7,746</b>	<b>11,293</b>	<b>13,886</b>	<b>13,886</b>	<b>13,886</b>	<b>13,886</b>
Cash & deposits	3,617	1,353	2,669	2,669	2,669	2,669
Loans and advances and other assets	1,597	3,093	3,803	3,803	3,803	3,803
Deferred tax assets	929	948	890	890	890	890
Fixed assets owned	300	324	356	378	408	410
<b>Total assets</b>	<b>233,549</b>	<b>293,804</b>	<b>402,418</b>	<b>531,484</b>	<b>683,006</b>	<b>925,760</b>
<b>Total liabilities</b>	<b>215,232</b>	<b>271,483</b>	<b>368,540</b>	<b>490,447</b>	<b>634,157</b>	<b>867,329</b>
Share capital	850	850	950	950	950	950
Reserves	17467	21491	32927	40087	47899	57480
<b>Shareholders fund</b>	<b>18,317</b>	<b>22,341</b>	<b>33,877</b>	<b>41,037</b>	<b>48849</b>	<b>58431</b>

Source: Company, Kotak Institutional Equities estimates

JULY 15, 2010

#### RESULT

Coverage view: **Attractive**

Price (Rs): **193**

Target price (Rs): **180**

BSE-30: **17,909**

**Margin pressures surface.** Polaris reported in-line revenues for 1QFY11 of US\$78.9 mn (+3.3% qoq) but saw a sharp 320 bps decline in EBITDA margins on the back of wage inflation and rising attrition pressure. In-line net profit of Rs466 mn, despite EBITDA miss, was mainly driven by higher other income and lower depreciation. Supply side constraints are impacting the margins and we believe Tier-II IT companies stand at a significant risk. Maintain SELL with an unchanged target price of Rs180/share.

#### Company data and valuation summary

Polaris Software Lab

Stock data		Forecasts/Valuations			
		2010	2011E	2012E	
52-week range (Rs) (high,low)	215-88	EPS (Rs)	15.4	19.1	18.8
Market Cap. (Rs bn)	19.3	EPS growth (%)	16.9	24.3	(1.7)
<b>Shareholding pattern (%)</b>		P/E (X)	12.6	10.1	10.3
Promoters	25.1	Sales (Rs bn)	13.5	15.4	17.7
FIs	45.2	Net profits (Rs bn)	1.5	1.9	1.9
MFs	9.6	EBITDA (Rs bn)	2.2	2.1	2.3
<b>Price performance (%)</b>		EV/EBITDA (X)	6.4	8.1	7.0
Absolute	1M 3M 12M	ROE (%)	18.6	20.1	17.2
Rel. to BSE-30	8.0 9.2 90.9	Div. Yield (%)	1.8	1.9	2.0
	5.0 7.5 51.9				

#### Revenues in line, wage pressure impacts margins

Polaris reported revenues of US\$78.9 mn (+3.3% qoq, +18.4% yoy), in line with our expectations. The major negative surprise came on the margin front – EBITDA margins declined 320 bps qoq to 13.4%. The company attributed the drop in margins to reversal of salary cuts done last year (7-8%) and further increase in offshore salaries by 15%. Polaris' margin performance is an indicator of pressure likely to be felt by most mid-sized companies in the tight supply market, in our view. Net Income of Rs466 mn was driven mainly by significantly higher other income of Rs142 mn (Rs55 mn in 4QFY10). SG&A expenses also declined at an absolute level, aiding EBITDA.

#### Little cushion on margins drives our negative stance on the stock and the Tier-II pack

Sharp and sudden surge in demand with several companies operating on thin bench strength has led to a strong pick-up in the lateral hiring with laterals being offered anywhere between 30% and 80% premium over their current base salaries. This would put pressure on gross margins across the industry – Tier I companies to absorb the margin pressures better, in our view. For Polaris, we do not expect margins to increase after a sharp qoq drop mainly due to (1) impact of wage cut reversal to be felt in the coming quarter as well and (2) wage hike effected from May 1 (impact of 2 months this quarter). Polaris is already running at a high utilization of 79% and the company indicated it is shifting its focus on demand fulfillment engine from demand generation one.

#### Broadly maintain estimates, Retain SELL

We broadly maintain our EPS estimates of Rs19.1 for FY2011 while EPS estimate for FY2012 stands at Rs18.8 (Rs18.6 earlier). EPS estimates build in strong forex gains of Rs238 mn for FY2011E and Rs164 mn for FY2012E; the company has US\$75 mn and US\$70mn outstanding hedges booked at 48-49 for FY2011/12, respectively. We believe the Tier-II companies face a daunting task of maintaining their margins in the current scenario of increased wage pressures. We further cut our margin estimates for FY2011E by 60 bps to 13.6%. We retain our target price of Rs180/share and SELL rating on the back of significant concerns on sustainability of margins.

Kawaljeet Saluja  
kawaljeet.saluja@kotak.com  
Mumbai: +91-22-6634-1243

Rohit Chordia  
rohit.chordia@kotak.com  
Mumbai: +91-22-6634-1397

Vineet Thodge  
vineet.thodge@kotak.com  
Mumbai: +91-22-6634-1225

Kotak Institutional Equities Research  
kotak.research@kotak.com  
Mumbai: +91-22-6634-1100

Exhibit 1: Key changes to estimates, FY2011E-FY2012E

	Revised		Earlier		Change (%)	
	FY2011E	FY2012E	FY2011E	FY2012E	FY2011E	FY2012E
Revenues (US\$ mn)	335	384	330	374	1.5	2.8
Revenues (Rs mn)	15,409	17,673	14,848	16,914	3.8	4.5
Revenue growth, US\$ (%)	17.3	14.7	15.5	13.3		
EBITDA (Rs mn)	2,100	2,330	2,112	2,323	(0.6)	0.3
EBIT (Rs mn)	1,744	1,930	1,713	1,871	1.8	3.1
Net profit (Rs mn)	1,905	1,873	1,906	1,854	(0.1)	1.0
EPS (Rs)	19.1	18.8	19.1	18.6	(0.1)	1.0
EBITDA margin (%)	13.6	13.2	14.2	13.7		
EBIT margin (%)	11.3	10.9	11.5	11.1		
Re/US\$ rate	46.0	46.0	45.0	45.2	2.3	1.7

Source: Kotak Institutional Equities estimates

Exhibit 2: Polaris Software Interim Results Q1FY2011 (Rs mn)

	1QFY10	4QFY10	1QFY11	qoq % chg.	yoy % chg.	Kotak estimates	% Deviation
<b>Revenues (US\$ mn)</b>	<b>66.6</b>	<b>76.4</b>	<b>78.9</b>	<b>3.3</b>	<b>18.4</b>	<b>78.9</b>	<b>(0.0)</b>
<b>Total Revenues</b>	<b>3,255</b>	<b>3,510</b>	<b>3,606</b>	<b>2.7</b>	<b>10.8</b>	<b>3,608</b>	<b>(0.1)</b>
<b>Cost of Revenues</b>	(2,079)	(2,231)	(2,430)	8.9	16.9	(2,308)	5.3
<b>Gross Profit</b>	<b>1,177</b>	<b>1,279</b>	<b>1,176</b>	<b>(8.1)</b>	<b>(0.1)</b>	<b>1,300</b>	<b>(9.5)</b>
SG&A Expenses	(624)	(698)	(694)	(0.5)	11.2	(720)	(3.6)
<b>EBITDA</b>	<b>552</b>	<b>581</b>	<b>482</b>	<b>(17.1)</b>	<b>(12.7)</b>	<b>580</b>	<b>(16.9)</b>
Other income	(90)	55	142	161.1	(258.0)	94	50.7
EBIDTA	462	636	624	(1.8)	35.1	674	(7.4)
Interest expense	(2)	(3)	(2)			—	
EBDT	460	632	622	(1.7)	35.1	674	(7.8)
Depreciation	(84)	(92)	(78)	(15.1)	(7.5)	(94)	(16.6)
Minority interest			1				
<b>Pretax profits</b>	<b>376</b>	<b>540</b>	<b>545</b>	<b>0.8</b>	<b>44.8</b>	<b>581</b>	<b>(6.2)</b>
Provision for Tax	(58)	(83)	(79)	(5.5)	36.2	(106)	(25.7)
<b>Net Profit</b>	<b>318</b>	<b>457</b>	<b>466</b>	<b>1.9</b>	<b>46.4</b>	<b>475</b>	<b>(1.9)</b>
Extraordinaries	—	—	—			—	
<b>Net Profit reported</b>	<b>318</b>	<b>457</b>	<b>466</b>	<b>1.9</b>	<b>46.4</b>	<b>475</b>	<b>(1.9)</b>
<b>EPS - recurring (Rs)</b>	<b>3.2</b>	<b>4.6</b>	<b>4.7</b>	<b>1.9</b>	<b>46.4</b>	<b>4.8</b>	
EPS - reported (Rs)	3.2	4.6	4.7	1.9	46.4	4.8	
<b>Margins (%)</b>							
Gross margin	36.1	36.4	32.6			36.0	
SG&A expenses	19.2	19.9	19.3			20.0	
EBITDA margin	17.0	16.6	13.4			16.1	
EBIT margin	14.4	13.9	11.2			13.5	
Net profit margin	9.8	13.0	12.9			13.2	

Source: Company, Kotak Institutional Equities estimates



## Condensed consolidated financials for Polaris, 2009-2012E, March fiscal year-ends (Rs mn)

	FY2009	FY2010	FY2011E	FY2012E
<b>Profit &amp; Loss Model</b>				
Revenues	13,779	13,538	15,409	17,673
EBITDA	2,335	2,220	2,100	2,330
Depreciation	(505)	(350)	(356)	(401)
EBIT	1,830	1,870	1,744	1,930
Other Income	(316)	(73)	532	506
PBT	1,507	1,788	2,274	2,435
Tax	(209)	(255)	(369)	(562)
Net Profit	1,298	1,533	1,905	1,873
<b>Balance Sheet (Rs mn)</b>				
Total Equity	7,727	8,725	10,198	11,616
Borrowings	4	25	—	—
<b>Total capital</b>	<b>7,730</b>	<b>8,749</b>	<b>10,198</b>	<b>11,616</b>
Net fixed Assets	2,157	2,271	2,351	2,643
Investments	2,442	3,897	3,897	3,897
Goodwill	199	506	506	506
Working Capital	2,901	2,041	3,410	4,536
- Cash	1,054	1,237	2,185	3,054
- Current Assets	4,356	3,830	4,644	5,375
- Current Liabilities	2,509	3,026	3,419	3,892
Deferred Expenditure	30	34	34	34
<b>Total assets</b>	<b>7,730</b>	<b>8,749</b>	<b>10,198</b>	<b>11,616</b>
<b>Free Cash Flow (Rs mn)</b>				
Cash generated from operations	2,364	2,163	2,335	2,335
Working Capital Changes	884	871	(421)	(257)
Capital expenditure	(578)	(429)	(436)	(692)
Tax	(209)	(290)	(369)	(562)
<b>Free Cash Flow</b>	<b>2,462</b>	<b>2,315</b>	<b>1,109</b>	<b>823</b>

Source: Company, Kotak Institutional Equities estimates

JULY 15, 2010

UPDATE

Coverage view: **Cautious**

Price (Rs): **1,073**

Target price (Rs): **985**

BSE-30: 17,909

**Cash deployment continues to be an issue.** We do not expect RIL's recent moves to create meaningful value, which raises issues about use of large FCF over the next few years. The market has been generous in ascribing value to the recent announcements, in our view, without factoring in risks to earnings from (1) weaker-than-expected margins or lower-than-expected volumes in its extant businesses and (2) adoption of IFRS from FY2012. The stock is trading near our FY2012E-based fair valuation of Rs1,060.

#### Company data and valuation summary

Reliance Industries

Stock data		Forecasts/Valuations			
		2010	2011E	2012E	
52-week range (Rs) (high,low)	1,185-841	EPS (Rs)	49.6	62.9	80.2
Market Cap. (Rs bn)	3,194.6	EPS growth (%)	(1.8)	26.6	27.5
<b>Shareholding pattern (%)</b>		P/E (X)	21.6	17.1	13.4
Promoters	41.1	Sales (Rs bn)	1,924.6	2,495.6	2,624.2
FIs	21.3	Net profits (Rs bn)	162.4	205.6	262.2
MFs	2.6	EBITDA (Rs bn)	309.4	397.9	449.7
<b>Price performance (%)</b>	<b>1M</b> <b>3M</b> <b>12M</b>	EV/EBITDA (X)	11.6	8.6	7.1
Absolute	0.7	(1.6)	14.4	ROE (%)	11.4
Rel. to BSE-30	(2.1)	(3.1)	(8.9)	Div. Yield (%)	1.2
					1.6
					1.9

#### Core businesses will likely remain under pressure over the next 12-24 months

We see continued pressure on chemical and refining margins over the next 12-24 months in light of (1) large global over-supply in chemicals and refining in CY2010-11E, (2) ongoing large capacity additions particularly in petrochemicals and base chemicals and (3) increased supply of NGLs, which would make up for any slowdown in refining capacity addition.

#### KG D-6 gas business—volumes may disappoint in the short term

We see downside risks to our volume assumptions and that of the street for RIL's KG D-6 gas production volumes. Recent press articles have reported technical issues in increasing production beyond 60 mcm/d in the short term. We model 72 mcm/d in FY2011E and 80 mcm/d in FY2012E. Our FY2011E and FY2012E EPS would decline by Rs4.1 and Rs7.8 if gas production is 60 mcm/d. Readers may recall street speculation of 120 mcm/d of gas production at one point of time. Also, higher-than-expected taxation poses further downside risks to earnings.

#### Adoption of IFRS may have negative implications for earnings

We see two areas of risks to RIL's earnings from implementation of IFRS from April 1, 2011. (1) A likely switch to Successful Efforts Method of Accounting for E&P business from the current Full Cost Method of Accounting may result in lower earnings. (2) RIL will have to account for the impact of changes in liabilities and assets denominated in a foreign currency through the P&L versus its current practice of capitalizing the same in the balance sheet.

#### We still find the stock expensive even if things run according to plan

We would note that our FY2012E-based fair valuation of Rs1,060 includes Rs135/share contribution (US\$8.5 bn) from gas blocks other than the KG D-6 block. We model mid-cycle chemical and refining margins in FY2012E. Finally, we note that the RIL stock is trading at 12.1X FY2012E adjusted EPS of Rs88 (adjusted for treasury shares), which is quite high in the context of (1) mid-cycle chemical and refining margins assumed by us and (2) probably peak earnings of the E&P segment based on 80 mcm/d of gas production and 10% government share of profit petroleum.

#### QUICK NUMBERS

- **US\$1/bbl change in refining margin impacts FY2012E EPS by 6.8%**
- **Lower gas production at 60 mcm/d in FY2011E and FY2012E to impact EPS by Rs4.1 and Rs7.8**
- **Stock trading at 12.1X FY2012E adjusted EPS implying significant addition to oil and gas reserves**

Sanjeev Prasad  
sanjeev.prasad@kotak.com  
Mumbai: +91-22-6634-1228

Gundeep Singh  
gundeep.singh@kotak.com  
Mumbai: +91-22-6634-1286

Tarun Lakhotia  
tarun.lakhotia@kotak.com  
Mumbai: +91-22-6634-1188

Kotak Institutional Equities Research  
kotak.research@kotak.com  
Mumbai: +91-22-6634-1100

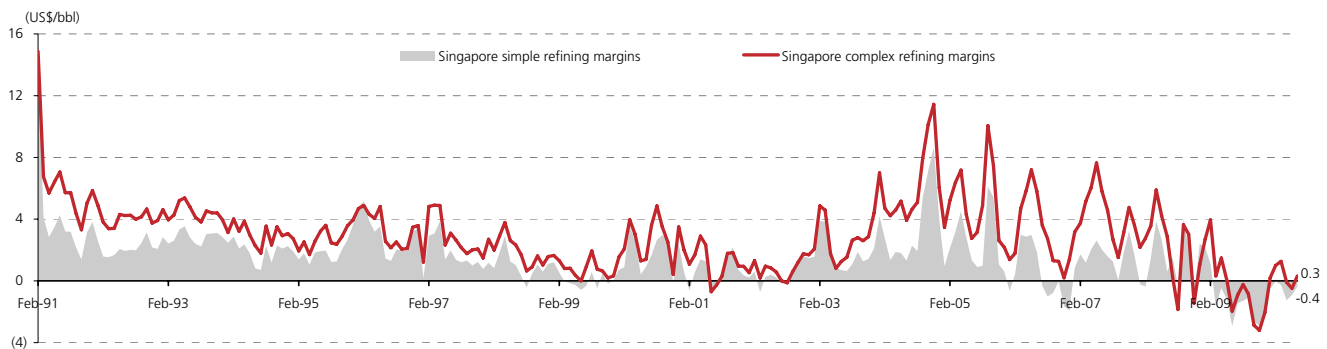
### Too many issues facing earnings and valuations

The following factors underpin our SELL rating on RIL stock.

- ▶ Limited scope for positive earnings surprise in core business. We rule out positive surprises in the earnings of the chemical and refining segments and do not rule out downside risks from lower-than-expected margins.
  - **Refining margins.** We model a sharp improvement in refining margins over the next two years and assume RIL's FY2011E and FY2012E refining margin at US\$8.8/bbl and US\$9.8/bbl versus the US\$6.6/bbl reported in FY2010. YTD FY2011 refining margins remain subdued (see Exhibit 1) although RIL will likely benefit from (1) use of more gas to run its refineries and (2) moderate expansion in light-heavy differentials over the past few months.

#### Complex refining margins remain subdued in the current year

Singapore refining margins (US\$/bbl)



Simple refining margins, March fiscal year-ends (US\$/bbl)											
	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011 YTD
1Q	1.3	0.5	0.3	1.0	1.7	3.0	2.5	2.3	2.4	(1.5)	(0.9)
2Q	2.5	0.4	0.1	1.2	3.1	2.8	(0.7)	1.0	1.7	(1.3)	0.1
3Q	1.7	1.1	1.4	1.6	6.5	2.2	(1.2)	2.3	1.3	(2.5)	
4Q	0.2	(0.0)	3.0	2.9	2.1	1.1	1.2	0.2	0.7	(0.3)	
Average	1.4	0.5	1.2	1.7	3.3	2.3	0.5	1.5	1.5	(1.4)	(0.8)

Complex refining margins, March fiscal year-ends (US\$/bbl)											
	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011 YTD
1Q	1.9	1.3	0.8	1.2	4.6	4.9	6.2	6.6	4.3	(0.1)	(0.1)
2Q	4.0	0.6	0.1	2.3	5.8	6.1	2.5	2.9	0.7	(0.7)	0.7
3Q	2.3	1.2	1.6	3.2	9.0	3.9	1.0	3.9	1.0	(2.7)	
4Q	1.6	0.6	3.7	5.4	5.0	2.8	4.1	2.8	2.4	0.8	
Average	2.4	0.9	1.5	3.1	6.1	4.4	3.4	4.0	2.1	(0.7)	0.0

Weekly margins				
Current	-1 Wk	-2 Wk	-3 Wk	-4 Wk
0.3	(0.1)	0.4	(0.6)	(0.6)

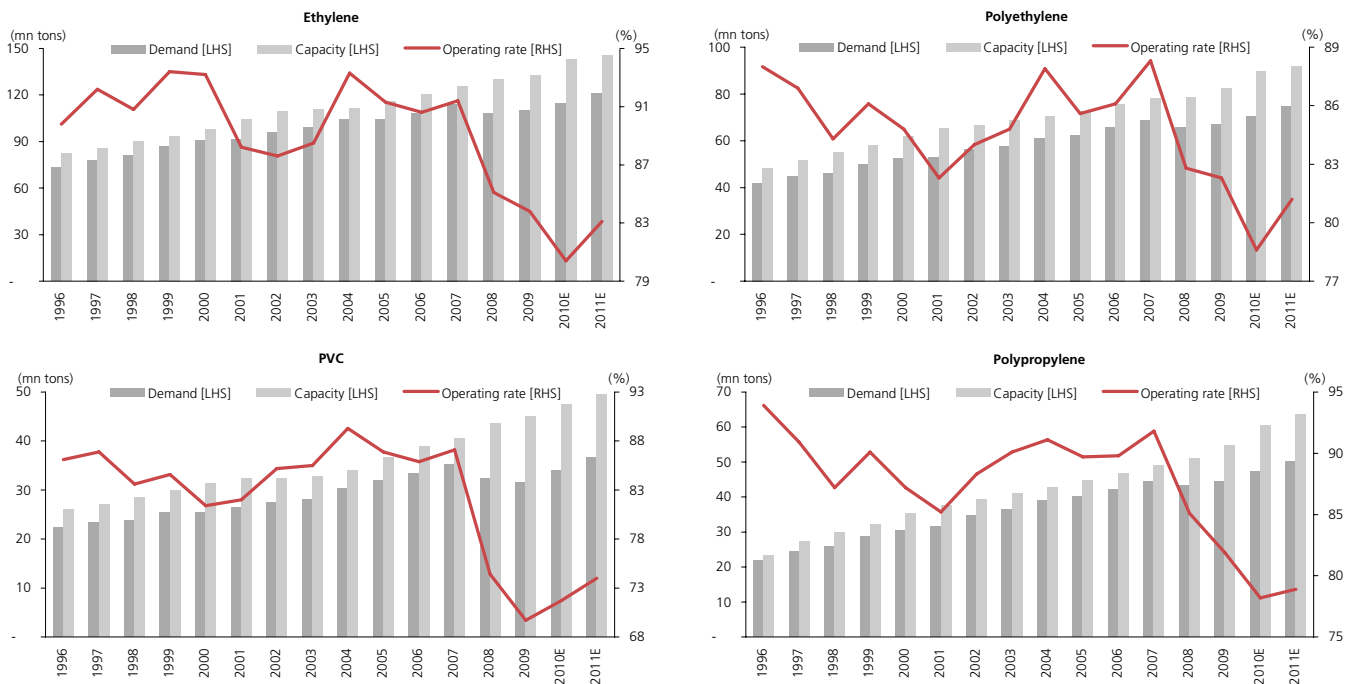
Weekly margins				
Current	-1 Wk	-2 Wk	-3 Wk	-4 Wk
0.7	0.6	1.1	0.2	(0.0)

Source: Bloomberg, Kotak Institutional Equities

- **Chemical margins.** We model chemical margins improving to mid-cycle levels in FY2012E from a downturn in FY2011E. However, we expect global operating rates to be well below historical levels in CY2010-11E (see Exhibit 2). We do not rule out chemical margins declining from current low levels given the ongoing large additions to global capacity.

### Global operating rates for key chemical products remain well below their historical levels

World demand and capacity (mn tons), operating rate (%), 1996-2011E



Source: CMAI, Kotak Institutional Equities estimates

- ▶ **Earnings from KG D-6 gas face production and taxation risks.** We discuss these issues below but highlight that the street has been very sanguine about any negative development in RIL's E&P business. In fact, the street has (1) extrapolated RIL's exploration success in the KG D-6 blocks to other blocks and (2) speculated on gas production eventually rising to 120 mcm/d based on inputs from Niko Resources' management.
  - **Gas production may be stuck at 60 mcm/d for some time.** We note that recent press articles have reported technical difficulties in increasing gas production beyond 60 mcm/d in the short term. RIL management has not provided any clarification on the press reports. We are accordingly holding on to our current assumptions of 72 mcm/d and 80 mcm/d of gas production in FY2011E and FY2012E. We note a potential negative impact of Rs4.1 and Rs7.8 on FY2011E and FY2012E EPS of RIL in a scenario of 60 mcm/d of gas production versus our base-case assumptions.
  - **Tax on gas production poses additional risks to earnings.** We and the street have assumed that RIL will avail of 100% income tax exemption on gas production from its KG D-6 (and other blocks) and thus, pay income tax at the MAT rate of taxation. We note a potential negative impact of Rs6.1 and Rs8.2 on FY2011E and FY2012E EPS of RIL in case it has to pay income tax on gas production.
- ▶ **Adoption of IFRS may also have negative implications.** We discuss the implications from implementation of IFRS on two areas for RIL but note that it is difficult to quantify the impact given limited information available.

- E&P accounting. We note that RIL will likely have to adopt the Successful Efforts Method (SEM) of Accounting under IFRS versus the current Full Cost Method (FCM) of Accounting used by it. We note that it is one of the few companies globally that still follows the Full Cost Method of Accounting.

The change in accounting method could have significant implications on RIL's future earnings since it has historically capitalized all E&P costs including geological and geophysical costs. In the future it will have to write off survey expenses and costs of any dry wells in the year they are incurred. This could make its earnings numbers more volatile. Also, it remains to be seen how RIL will account for survey and dry wells costs of the past years. We assume it will adjust the same against its equity or continue to write them off through DD&A as it is doing currently.

It is difficult to quantify the impact of the change in accounting method on RIL's book value and future earnings. RIL does not disclose the breakdown of assets between fixed assets and producing properties. We have highlighted RIL's low disclosures in the E&P segment repeatedly in the past.

- **Foreign currency assets and liabilities accounting.** We note that RIL will have to necessarily account for the impact of any change in assets and liabilities due to change in foreign exchange rates through the P&L. It has historically accounted for the same through its balance sheet by capitalizing the amount of FX-related changes. We note that 85% of RIL's total loans are denominated in various foreign currencies. However, this issue may become less relevant in the future as RIL will generate large FCF and will likely pay down the debt. Also, it will benefit through FX gains in the case of appreciation of the local currency against the currencies of its FX loans.
- ▶ Valuations are full even without factoring in aforementioned risks. We note that RIL stock is trading near our FY2012E SOTP-based fair valuation of Rs1,060. Also, we have factored Rs135 (US\$8.5 bn) of value of new E&P assets (NEC-25, CBM, KG D-3, KG D-9 MN D-4 blocks); we assume 38 tcf of recoverable reserves of gas from these blocks. We also use 7X and 7.5X EBITDA for the chemical and refining segments, which may be a bit generous since we model mid-cycle margins as discussed earlier. We would normally ascribe 6-6.5X for mid-cycle earnings of chemical and refining companies.

Finally, we are not very enthused by RIL's recent moves to use its large FCF. We expect the telecom initiative (BWA foray) to destroy value and do not expect the shale gas initiatives to create meaningful value. We are thus reluctant to ascribe large value to RIL's large FCF and treat the same as cash unless RIL can use the same for developing E&P assets in India.

RIL has been strangely reluctant to pursue E&P opportunities within India recently and has delayed several of its projects (see Exhibit 3). We note that the market expects these projects to create meaningful value over the next few years; we observe that most SOTP valuations on the street ascribe meaningful value to new and potential E&P discoveries. Thus, continued delays in establishing reserves of oil and gas (if any) in these blocks and developing the same may result in the market reducing the value of prospective blocks such as KG D-3, KG D-9 and MN D-4.

Delay in E&P activities does not augur well  
Exploration program of RIL

Blocks	Drilling schedule	E&P activity status
NEC-OSN-97/2 (NEC-25)	Six-well drilling program is in progress	1 Acquired 3,200 sq. kms of 3D seismic data 2 Drilled three successful wells (AJ2, AJ3 and AJ5 ) 3 Recently spud AJ6, AJ7 and AJ9 exploration wells
GS-OSN-2000/1	Appraisal drilling postponed to August 2010	1 Acquired 1,216 sq. kms of 3D seismic data from the block 2 Recently carried out advanced technical and geophysical studies 3 Currently undertaking Phase-II of the work program
AS-ONN-2000/1	Drilling postponed to mid-2011	1 Concluded interpretation of around 400 line kms of 2D seismic data 2 To drill one exploration well in CY2010-11E
CY-DWN-2001/2 (D-5)	Commencement of drilling program in April 2010	1 Drilled three wells; struck hydrocarbon in one 2 Abandoned second well due to a technical snag
KG-DWN-2001/1 (D-9)	Re-commencement of drilling expected in 2HCY10	1 Acquired and processed 4,188 sq. kms of 3D seismic data 2 Drilled the first (A-1) of four exploration wells; plugged and abandoned 3 Plans to drill one exploration well in CY2010E and two wells in CY2011E
KG-DWN-2003/1 (D-3)	Appraisal program to start from December 2010	1 Acquired 3,231 sq. kms of 3D seismic data 2 Drilled three successful exploration wells (Dhirubhai 39, 41 and 44) 3 Pre-drilled fourth well G1 and will re-enter later to target depth 4 Suspended drilling of fifth well (W1) due to exit of rig
MN-DWN-2003/1 (D-4)	Three-well drilling program postponed to April 2011	1 Acquired 3,600 sq. kms of 3D seismic data 2 Three wells indentified for drilling 3 To drill a total of fifteen exploratory wells under MWP
CB-ONN-2003/1	Drilling program in progress	1 Seven discoveries out of 17 exploratory wells drilled 2 Acquired 3D seismic data for 80% of the block

Source: Kotak Institutional Equities estimates

Reliance's earnings have high leverage to refining margins  
Sensitivity of RIL's earnings to key variables

	Fiscal 2011E			Fiscal 2012E			Fiscal 2013E		
	Downside	Base case	Upside	Downside	Base case	Upside	Downside	Base case	Upside
<b>Rupee-dollar exchange rate</b>									
Rupee-dollar exchange rate	44.0	45.0	46.0	44.3	45.3	46.3	44.3	45.3	46.3
Net profits (Rs mn)	196,785	205,606	214,428	252,355	262,222	272,089	273,542	283,679	293,817
EPS (Rs)	60.2	62.9	65.6	77.2	80.2	83.2	83.6	86.7	89.8
<b>% upside/(downside)</b>	<b>(4.3)</b>		<b>4.3</b>	<b>(3.8)</b>		<b>3.8</b>	<b>(3.6)</b>		<b>3.6</b>
<b>Chemical prices</b>									
Change in prices (%)	(5.0)		5.0	(5.0)		5.0	(5.0)		5.0
Net profits (Rs mn)	200,960	205,606	210,253	257,355	262,222	267,089	278,701	283,679	288,658
EPS (Rs)	61.4	62.9	64.3	78.7	80.2	81.7	85.2	86.7	88.3
<b>% upside/(downside)</b>	<b>(2.3)</b>		<b>2.3</b>	<b>(1.9)</b>		<b>1.9</b>	<b>(1.8)</b>		<b>1.8</b>
<b>Blended refining margins (US\$/bbl)</b>									
Margins (US\$/bbl)	7.8	8.8	9.8	8.8	9.8	10.8	9.3	10.3	11.3
Net profits (Rs mn)	187,871	205,606	223,326	244,361	262,222	279,977	265,847	283,679	301,413
EPS (Rs)	57.4	62.9	68.3	74.7	80.2	85.6	81.3	86.7	92.2
<b>% upside/(downside)</b>	<b>(8.6)</b>		<b>8.6</b>	<b>(6.8)</b>		<b>6.8</b>	<b>(6.3)</b>		<b>6.3</b>

Source: Kotak Institutional Equities estimates

SOTP valuation of Reliance is Rs915 per share on FY2011E estimates

Sum-of-the-parts valuation of Reliance Industries, FY2011E basis (Rs)

	Valuation base (Rs bn)		Multiple (X)		EV (Rs bn)	Valuation (Rs/share)
	Other	EBITDA	Multiple	EV/EBITDA		
Chemicals		96		7.0	675	228
Refining & Marketing		131		7.5	981	331
Oil and gas—producing (PMT and Yemen)		18		5.0	92	31
Gas—producing and developing (DCF-based) (a)	816				816	276
KG D-6	464				464	157
NEC-25	92				92	31
CBM	53				53	18
KG D-3	56				56	19
KG D-9	84				84	29
MN D-4	66				66	22
Oil—KG-DWN-98/3 (b)	81				81	27
Investments other than valued separately	105				105	35
Loans & advances to affiliates	4				4	1
Cash with subsidiary from sale of treasury shares	86				86	29
Retailing	52		80%		42	14
SEZ development	30		80%		24	8
<b>Total enterprise value</b>					<b>2,905</b>	<b>981</b>
Net debt adjusted for 50% of C-WIP of E&P assets					202	68
<b>Implied equity value</b>					<b>2,704</b>	<b>913</b>

Note:

(a) We value KG D-6, NEC-25, CBM, KG D-3, KG D-9 and MN D-4 blocks on DCF.

(b) 180 mn bbls of recoverable reserves based on gross OOIP of 0.5 bn bbls.

(c) We use 2.976 bn shares (excluding treasury shares) for per share computations.

Source: Kotak Institutional Equities estimates

SOTP valuation of Reliance is Rs1,060 per share on FY2012E estimates

Sum-of-the-parts valuation of Reliance Industries, FY2012E basis (Rs)

	Valuation base (Rs bn)		Multiple (X)		EV (Rs bn)	Valuation (Rs/share)
	Other	EBITDA	Multiple	EV/EBITDA		
Chemicals		103		7.0	718	242
Refining & Marketing		151		7.5	1,134	383
Oil and gas—producing (PMT and Yemen)		20		5.0	98	33
Gas—producing and developing (DCF-based) (a)	800				800	270
KG D-6	400				400	135
NEC-25	99				99	34
CBM	53				53	18
KG D-3	69				69	23
KG D-9	100				100	34
MN D-4	79				79	27
Oil—KG-DWN-98/3 (b)	81				81	27
Investments other than valued separately	105				105	35
Loans & advances to affiliates	4				4	1
Cash with subsidiary from sale of treasury shares	86				86	29
Retailing	52		80%		42	14
SEZ development	30		80%		24	8
<b>Total enterprise value</b>					<b>3,091</b>	<b>1,044</b>
Net debt adjusted for 50% of C-WIP of E&P assets					(35)	(12)
<b>Implied equity value</b>					<b>3,126</b>	<b>1,056</b>

Note:

(a) We value KG D-6, NEC-25, CBM, KG D-3, KG D-9 and MN D-4 blocks on DCF.

(b) 180 mn bbls of recoverable reserves based on gross OOIP of 0.5 bn bbls.

(c) We use 2.976 bn shares (excluding treasury shares) for per share computations.

Source: Kotak Institutional Equities estimates

RIL: Profit model, balance sheet, cash model, March fiscal year-ends, 2006-2014E (Rs mn)

	2006	2007	2008	2009	2010	2011E	2012E	2013E	2014E
<b>Profit model (Rs mn)</b>									
Net sales	809,113	1,114,927	1,334,430	1,418,475	1,924,610	2,495,632	2,624,219	2,724,442	2,738,544
<b>EBITDA</b>	<b>139,991</b>	<b>198,462</b>	<b>233,056</b>	<b>233,139</b>	<b>305,807</b>	<b>394,344</b>	<b>446,093</b>	<b>475,950</b>	<b>474,360</b>
Other income	6,829	4,783	8,953	20,599	24,605	22,242	18,850	29,700	49,547
Interest	(8,770)	(11,889)	(10,774)	(17,452)	(19,972)	(24,183)	(9,511)	(6,497)	(5,555)
Depreciation & depletion	(34,009)	(48,152)	(48,471)	(51,953)	(104,965)	(131,342)	(125,123)	(143,021)	(147,844)
Pretax profits	104,041	143,205	182,764	184,332	205,474	261,062	330,310	356,132	370,507
Extraordinary items	3,000	2,000	47,335	—	—	—	—	—	—
Tax	(9,307)	(16,574)	(26,520)	(12,634)	(31,118)	(54,394)	(70,513)	(85,076)	(91,336)
Deferred taxation	(7,040)	(9,196)	(8,999)	(18,605)	(12,000)	(1,061)	2,425	12,624	18,010
Net profits	90,693	119,434	194,580	153,093	162,357	205,606	262,222	283,679	297,181
<b>Adjusted net profits</b>	<b>88,152</b>	<b>117,789</b>	<b>152,605</b>	<b>153,093</b>	<b>162,357</b>	<b>205,606</b>	<b>262,222</b>	<b>283,679</b>	<b>297,181</b>
<b>Earnings per share (Rs)</b>	<b>31.6</b>	<b>40.5</b>	<b>52.5</b>	<b>50.6</b>	<b>49.6</b>	<b>62.9</b>	<b>80.2</b>	<b>86.7</b>	<b>90.9</b>
<b>Balance sheet (Rs mn)</b>									
Total equity	430,543	673,037	847,853	1,263,730	1,371,706	1,512,531	1,695,575	1,885,681	2,089,288
Deferred taxation liability	49,708	69,820	78,725	97,263	109,263	110,324	107,899	95,276	77,265
Minority interest	—	33,622	33,622	—	—	—	—	—	—
Total borrowings	218,656	332,927	493,072	739,045	624,947	337,340	130,999	128,774	128,514
Current liabilities	164,545	192,305	251,427	357,019	404,148	383,752	400,931	411,346	411,771
<b>Total liabilities and equity</b>	<b>863,452</b>	<b>1,301,712</b>	<b>1,704,700</b>	<b>2,457,057</b>	<b>2,510,064</b>	<b>2,343,947</b>	<b>2,335,403</b>	<b>2,521,076</b>	<b>2,706,838</b>
Cash	21,461	18,449	42,822	221,765	134,626	19,215	49,827	290,474	545,981
Current assets	224,283	286,566	402,721	325,358	489,165	503,780	517,367	530,380	531,775
Total fixed assets	626,745	899,403	1,081,638	1,693,869	1,653,987	1,588,666	1,535,924	1,467,935	1,396,795
Investments	(9,038)	97,294	177,519	216,065	232,286	232,286	232,286	232,286	232,286
Deferred expenditure	—	—	—	—	—	—	—	—	—
<b>Total assets</b>	<b>863,452</b>	<b>1,301,712</b>	<b>1,704,700</b>	<b>2,457,057</b>	<b>2,510,064</b>	<b>2,343,947</b>	<b>2,335,403</b>	<b>2,521,076</b>	<b>2,706,838</b>
<b>Free cash flow (Rs mn)</b>									
Operating cash flow, excl. working capital	119,520	164,285	180,718	174,508	222,605	311,559	360,290	381,159	373,474
Working capital	(32,188)	(13,075)	(31,071)	(37,983)	(53,015)	(35,011)	3,591	(2,597)	(971)
Capital expenditure	(94,273)	(247,274)	(239,691)	(247,128)	(219,427)	(61,550)	(65,645)	(72,772)	(71,754)
Investments	(32,364)	(105,760)	(78,953)	(10,392)	14,206	—	—	—	—
Other income	5,159	4,143	6,132	16,195	22,043	22,242	18,850	29,700	49,547
<b>Free cash flow</b>	<b>(34,146)</b>	<b>(197,681)</b>	<b>(162,865)</b>	<b>(104,800)</b>	<b>(13,587)</b>	<b>237,240</b>	<b>317,087</b>	<b>335,490</b>	<b>350,296</b>
<b>Ratios (%)</b>									
Debt/equity	45.5	44.8	53.2	54.3	42.2	20.8	7.3	6.5	5.9
Net debt/equity	41.1	42.3	48.6	38.0	33.1	19.6	4.5	(8.2)	(19.3)
RoAE	19.9	20.3	18.9	13.6	11.8	13.5	15.5	15.2	14.5
<b>RoACE</b>	<b>13.8</b>	<b>13.9</b>	<b>12.7</b>	<b>11.2</b>	<b>9.3</b>	<b>11.2</b>	<b>13.9</b>	<b>13.8</b>	<b>13.0</b>

Source: Company, Kotak Institutional Equities estimates



JULY 16, 2010

UPDATE

BSE-30: 17,909

**Buying opportunity.** We see the sharp slump in stock prices of downstream companies as a good opportunity to buy these stocks given decent potential upside from current levels. We are surprised by the sharp decline in stock prices over oil secretary's statement on the possible subsidy-sharing mechanism with (1) upstream bearing 33.3% of the under-recoveries and (2) government providing atleast 50% of the under-recoveries. We see this in line with expectations and do not see merit in the sharp correction in stock prices. We retain our ADD ratings on BPCL, HPCL and IOCL.

#### Oil secretary's statements provide more clarity on subsidy-sharing scheme, if anything

We are surprised by the sharp decline in stock prices for BPCL (-5.8%), HPCL (-6%) and IOCL (-3.7%) following a statement of India's petroleum ministry secretary on the possible subsidy-sharing mechanism—(1) upstream companies to bear one-third of the overall subsidy burden and (2) government to provide compensation for at least 50% of the under-recoveries. We see this in line with our expectations. If anything, it provides clarity on the subsidy-sharing mechanism. Also, the government is committed to deregulating diesel at a later in line with the announcement made on June 25, 2010. We had highlighted that current high inflation and diesel's use as the main transportation fuel in India may prevent the government from deregulating prices in the near term. We believe that the government may have more flexibility to deregulate prices later once inflation subsides in India in 2HFY11E. Current under-recovery on diesel is quite marginal (see Exhibit 1).

#### Net under-recoveries of downstream companies is the pertinent metric

We note that the absolute amount of net under-recoveries to be borne by downstream companies is the critical variable as opposed to the % share of gross under-recoveries. The % share of downstream companies/government will vary depending on the absolute amount of gross under-recoveries in the system. We currently assume that downstream companies will bear a fixed amount of ~Rs50 bn in FY2011E and ~Rs40 bn in FY2012-14E (compared to Rs56 bn in FY2010).

#### Do not overlook government's stance historically; government has protected earnings

We note that the government has historically given adequate compensation to the downstream companies to ensure a decent level of profitability for these companies (see Exhibit 2). The downstream companies did not bear any subsidy burden in FY2009 when the subsidy burden had ballooned to Rs1.1 tn. Thus, there is no reason to believe that the government would unduly increase the burden on downstream companies. The government's philosophy is supported by the petroleum secretary's statement that the under-recovery of the downstream companies will be decided after reviewing the operational performance of these companies.

#### Decent potential upside from current levels

We believe that the recent correction offers a good buying opportunity with the stocks offering a decent upside (9-28%) to our fair valuation based on 8X FY2012E EPS (see Exhibit 3). We note that the current stock prices are already discounting a hypothetical scenario of government restricting its share to 50% of the under-recoveries (see Exhibit 4). Finally, our blue-sky scenario shows 26-61% upside to our blue-sky fair valuations for the stocks. Our blue-sky scenario assumes full deregulation of diesel and gasoline prices (not so unrealistic) and full compensation of under-recoveries on cooking fuels to the companies from the government.

#### QUICK NUMBERS

- 9-28% upside for OMCs from current levels on FY2012E basis
- 26-61% upside from current levels for OMCs assuming nil subsidy burden
- 33.3% share of subsidy burden on upstream companies in line with our estimate

Sanjeev Prasad  
sanjeev.prasad@kotak.com  
Mumbai: +91-22-6634-1229

Gundeep Singh  
gundeep.singh@kotak.com  
Mumbai: +91-22-6634-1286

Tarun Lakhota  
tarun.lakhota@kotak.com  
Mumbai: +91-22-6634-1188

Kotak Institutional Equities Research  
kotak.research@kotak.com  
Mumbai: +91-22-6634-1100

**Current under-recovery on regulated products**  
Marketing margins on regulated petroleum products, June 2010

Crude price (US\$/bbl)	74.8
Exchange rate (Rs/US\$)	46.6
LPG (Rs/cylinder)	(224.8)
Gasoline (Rs/liter)	(1.1)
Kerosene (Rs/liter)	(16.2)
Diesel (Rs/liter)	0.1

Note:

(a) We have assumed actual global prices for June 2010.

Source: Bloomberg, Kotak Institutional Equities

**Downstream oil companies may bear low subsidy burden in FY2011-12E**

Share of various participants of under-recoveries, March fiscal year-ends, 2007-12E (Rs bn)

	2007	2008	2009	2010	2011E	2012E
Dated Brent crude oil price (US\$/bbl)	65	79	89	67	75	75
<b>Gross under-recoveries</b>	<b>521</b>	<b>798</b>	<b>1,061</b>	<b>490</b>	<b>539</b>	<b>400</b>
<b>Direct budgetary support</b>	<b>27</b>	<b>27</b>	<b>29</b>	<b>30</b>	<b>32</b>	<b>30</b>
<b>Payment by government (oil bonds/cash)</b>	<b>241</b>	<b>353</b>	<b>713</b>	<b>260</b>	<b>278</b>	<b>227</b>
Share of BPCL	53	86	162	53	56	46
Share of HPCL	49	77	147	56	59	49
Share of IOCL	138	190	404	152	162	132
<b>Net under-recovery of oil companies</b>	<b>253</b>	<b>418</b>	<b>319</b>	<b>200</b>	<b>229</b>	<b>173</b>
Share of refining companies	—	—	—	—	—	—
<b>Share of upstream companies</b>	<b>205</b>	<b>257</b>	<b>329</b>	<b>144</b>	<b>180</b>	<b>133</b>
Share of ONGC	170	220	282	116	144	107
Share of GAIL	15	14	18	13	16	12
Share of Oil India	20	23	29	15	20	15
<b>Net under-recovery of R&amp;M companies (BPCL, HPCL, IOCL)</b>	<b>48</b>	<b>161</b>	<b>(10)</b>	<b>56</b>	<b>50</b>	<b>40</b>

Source: Company, Kotak Institutional Equities estimates

**Fair valuation of government-owned oil companies on FY2012E basis**

EPS estimates and fair valuation, March fiscal year-end, 2012E (Rs)

	EPS (Rs)	P/E (X)	Value of investments (Rs)	Fair value (Rs)	Current stock price (Rs)	Upside (%)
<b>Downstream companies</b>						
BPCL	68	8	173	714	656	9
HPCL	62	8	74	570	446	28
IOCL	37	8	124	423	374	13
<b>Upstream companies</b>						
GAIL India	39	NA	NA	525	448	17
Oil India	152	10	27	1,547	1,346	15
ONGC (a)	141	10	55	1,533	1,237	24

Note:

(a) Fair value of ONGC includes value of new discoveries.

Source: Kotak Institutional Equities estimates

Current stock prices of OMCs assuming 16.7% share of overall subsidy burden  
EPS estimates and fair valuation, March fiscal year-end, 2012E (Rs)

	Current stock price (Rs)	16.7% subsidy burden			Nil subsidy burden		
		EPS (Rs)	Fair value (Rs)	Upside (%)	EPS (Rs)	Fair value (Rs)	Upside (%)
BPCL	656	57	625	(5)	84	847	29
HPCL	446	50	472	6	80	716	61
IOCL	374	33	391	4	43	472	26

Source: Kotak Institutional Equities estimates

### Upstream companies share at 33.3%; lower-than-expected 1QFY11 subsidy burden on upstream

In our view, the recent decision of the government regarding the upstream companies bearing 33.3% of the overall under-recoveries will likely allay concerns on upstream companies being asked to bear higher-than-expected subsidy burden. We already assume that upstream companies will bear 33.3% of the overall under-recoveries. The petroleum secretary also stated that upstream companies will bear Rs60 bn of subsidies in 1QFY11. This is lower versus our expectation of Rs66 bn. Exhibit 5 gives our estimates of net income and subsidy burden for upstream companies for 1QFY11E.

Rs60 bn of subsidy burden on upstream companies is lower than our estimate  
Net income and subsidy burden for upstream companies, 1QFY11E (Rs bn)

	Net income	Subsidy burden
ONGC	46.4	52.6
OIL	4.7	7.2
GAIL	7.5	5.9
<b>Total</b>		<b>65.7</b>

Source: Kotak Institutional Equities estimates

Indian energy companies valuation analysis, March fiscal year-ends, 2009-2013E

	Price (Rs) 15-Jul-10	Target price (Rs)	P/E (X)					P/CEPS (X)				
			2009	2010	2011E	2012E	2013E	2009	2010	2011E	2012E	2013E
BPCL	656	660	32.2	10.6	12.1	9.7	8.7	12.0	44.6	11.1	8.7	7.3
GAIL (India)	448	495	20.3	18.1	17.1	11.6	10.2	18.7	17.1	16.9	10.3	8.6
HPCL	446	500	26.3	8.1	9.9	7.2	6.7	(12.4)	9.7	8.4	6.4	5.0
IOCL	374	410	32.5	7.7	11.0	10.0	9.8	(2.6)	9.6	9.7	8.4	7.9
Oil India	1,346	1,440	13.3	11.7	10.3	8.9	8.2	11.9	13.1	11.6	9.5	8.7
ONGC	1,237	1,450	13.5	13.5	9.9	8.8	7.4	9.8	10.2	8.1	7.0	6.4

	KS rating	Market cap. (US\$ mn)	EV/EBITDA (X)					EV/DACF (X)				
			2009	2010E	2011E	2012E	2013E	2009	2010E	2011E	2012E	2013E
BPCL	ADD	5,089	9.6	8.5	7.6	5.8	5.1	12.6	11.8	9.8	8.0	7.0
GAIL (India)	ADD	12,190	13.0	10.9	11.6	8.8	7.4	17.0	15.5	16.7	11.2	9.3
HPCL	ADD	3,240	16.3	6.6	8.0	6.7	6.2	12.0	7.8	9.1	7.8	6.7
IOCL	ADD	19,499	17.4	6.6	7.9	6.6	6.0	22.6	9.0	10.0	8.6	8.0
Oil India	BUY	6,941	9.1	5.9	4.7	3.7	3.2	15.7	8.5	7.1	5.5	4.7
ONGC	BUY	56,744	6.0	5.3	4.3	3.6	2.9	8.1	6.6	5.6	4.6	3.7

Source: Bloomberg, Kotak Institutional Equities estimates

## Consolidated profit model, balance sheet, cash model of BPCL, March fiscal year-ends, 2006-2014E (Rs mn)

	2007	2008	2009	2010E	2011E	2012E	2013E	2014E
<b>Profit model (Rs mn)</b>								
Net sales	965,569	1,102,081	1,340,734	1,223,599	1,331,561	1,414,562	1,572,277	1,649,107
<b>EBITDA</b>	<b>35,362</b>	<b>28,472</b>	<b>27,507</b>	<b>35,495</b>	<b>37,887</b>	<b>47,684</b>	<b>51,515</b>	<b>52,631</b>
Other income	7,332	13,954	15,087	21,563	14,997	12,548	10,789	9,032
Interest	(4,774)	(6,725)	(21,664)	(10,109)	(9,466)	(9,097)	(6,584)	(3,954)
Depreciation	(9,041)	(10,982)	(10,755)	(12,423)	(13,999)	(14,521)	(15,047)	(15,503)
Pretax profits	28,879	24,719	10,176	34,526	29,419	36,614	40,673	42,206
Extraordinary items	(68)	—	—	(10,865)	—	—	—	—
Tax	(9,286)	(9,059)	(5,103)	(8,284)	(6,982)	(11,317)	(12,299)	(13,124)
Deferred taxation	(268)	(1,108)	2,421	—	(2,790)	(845)	(1,212)	(895)
<b>Adjusted net profits</b>	<b>18,101</b>	<b>15,806</b>	<b>7,359</b>	<b>22,437</b>	<b>19,647</b>	<b>24,452</b>	<b>27,162</b>	<b>28,186</b>
<b>Earnings per share (Rs)</b>	<b>50.1</b>	<b>43.7</b>	<b>20.4</b>	<b>62.1</b>	<b>54.3</b>	<b>67.6</b>	<b>75.1</b>	<b>78.0</b>
<b>Balance sheet (Rs mn)</b>								
Total equity	102,735	116,768	121,281	130,736	142,841	157,907	174,643	192,010
Deferred taxation liability	13,826	14,814	12,392	12,392	15,183	16,028	17,240	18,135
Total borrowings	108,292	150,224	211,714	214,686	153,186	116,686	77,686	37,994
Current liabilities	112,767	145,803	128,313	122,514	144,598	147,699	155,835	158,882
<b>Total liabilities and equity</b>	<b>337,620</b>	<b>427,608</b>	<b>473,701</b>	<b>480,327</b>	<b>455,807</b>	<b>438,320</b>	<b>425,403</b>	<b>407,020</b>
Cash	8,640	9,616	4,416	2,459	2,459	2,487	2,205	2,272
Current assets	127,698	187,457	148,469	164,813	178,886	183,726	195,130	199,811
Goodwill	—	—	—	—	—	—	—	—
Total fixed assets	118,334	127,354	140,033	166,935	173,341	175,986	176,948	178,816
Investments	82,949	103,182	180,784	146,121	101,121	76,121	51,121	26,121
<b>Total assets</b>	<b>337,621</b>	<b>427,608</b>	<b>473,701</b>	<b>480,328</b>	<b>455,807</b>	<b>438,320</b>	<b>425,403</b>	<b>407,020</b>
<b>Free cash flow (Rs mn)</b>								
Operating cash flow, excl. working capital	29,920	22,988	19,717	5,325	21,439	27,270	32,631	35,553
Working capital	11,451	(25,161)	20,585	(17,221)	7,946	(1,739)	(3,268)	(1,635)
Capital expenditure	(17,908)	(20,665)	(23,323)	(38,414)	(20,405)	(17,166)	(16,008)	(17,371)
Investments	(45,481)	(21,684)	(82,456)	34,663	45,000	25,000	25,000	25,000
Other income	4,337	6,434	6,655	16,640	15,063	12,548	10,789	9,032
<b>Free cash flow</b>	<b>(17,682)</b>	<b>(38,088)</b>	<b>(58,822)</b>	<b>993</b>	<b>69,042</b>	<b>45,914</b>	<b>49,144</b>	<b>50,579</b>
<b>Ratios (%)</b>								
Debt/equity	105.4	128.7	174.6	164.2	107.2	73.9	44.5	19.8
Net debt/equity	97.0	120.4	170.9	162.3	105.5	72.3	43.2	18.6
RoAE	16.3	12.7	5.5	11.1	13.0	14.7	14.9	14.0
<b>RoACE</b>	<b>11.0</b>	<b>7.9</b>	<b>5.1</b>	<b>8.2</b>	<b>8.9</b>	<b>10.5</b>	<b>11.8</b>	<b>12.3</b>
<b>Key assumptions (standalone until FY2005)</b>								
Crude throughput (mn tons)	19.8	20.9	20.0	20.4	22.3	22.3	22.3	22.3
Effective tariff protection (%)	1.6	1.4	2.4	2.3	1.1	1.1	1.1	1.1
Net refining margin (US\$/bbl)	3.2	5.6	5.2	3.0	3.8	4.7	5.2	5.2
Sales volume (mn tons)	24.5	26.7	28.1	29.3	31.1	32.9	34.9	37.0
Marketing margin (Rs/ton)	(1,140)	(3,010)	(5,944)	571	229	1,536	1,514	1,511
Subsidy under-recoveries (Rs mn)	(10,400)	(33,354)	2,728	(12,375)	(11,474)	(8,951)	(9,187)	(8,977)

Source: Company, Kotak Institutional Equities estimates

## Profit model, balance sheet, cash model of HPCL, March fiscal year-ends, 2006-2014E (Rs mn)

	2006	2007	2008	2009	2010E	2011E	2012E	2013E	2014E
<b>Profit model (Rs mn)</b>									
Net sales	708,609	889,959	1,043,130	1,249,348	1,084,977	1,201,760	1,282,260	1,428,604	1,496,265
<b>EBITDA</b>	<b>8,056</b>	<b>24,036</b>	<b>15,757</b>	<b>28,707</b>	<b>41,603</b>	<b>35,227</b>	<b>46,867</b>	<b>52,505</b>	<b>54,373</b>
Other income	3,285	6,845	11,980	9,057	7,859	7,347	8,343	8,348	7,473
Interest	(1,587)	(4,230)	(7,925)	(20,828)	(9,038)	(9,112)	(12,607)	(13,183)	(13,412)
Depreciation	(6,902)	(7,040)	(8,508)	(9,813)	(11,644)	(10,593)	(11,117)	(13,448)	(15,321)
Pretax profits	2,851	19,611	11,303	7,122	28,781	22,869	31,486	34,223	33,112
Extraordinary items	2,201	3,030	—	—	(7,530)	—	—	—	—
Tax	(898)	(6,625)	(1,799)	(2,416)	(5,615)	(4,558)	(8,930)	(6,821)	(8,500)
Deferred taxation	(97)	(365)	(2,025)	(343)	(2,046)	(3,069)	(1,528)	(5,000)	(2,499)
Prior period adjustment	—	61	3,870	1,387	(575)	—	—	—	—
<b>Adjusted net profits</b>	<b>2,247</b>	<b>13,568</b>	<b>11,349</b>	<b>5,750</b>	<b>18,555</b>	<b>15,242</b>	<b>21,027</b>	<b>22,402</b>	<b>22,113</b>
<b>Earnings per share (Rs)</b>	<b>6.6</b>	<b>40.0</b>	<b>33.5</b>	<b>17.0</b>	<b>54.7</b>	<b>45.0</b>	<b>62.0</b>	<b>66.1</b>	<b>65.2</b>
<b>Balance sheet (Rs mn)</b>									
Total equity	87,357	95,987	105,633	107,306	115,561	125,247	138,610	152,846	166,899
Deferred tax liability	13,844	14,209	15,960	16,034	18,080	21,149	22,677	27,677	30,175
Total borrowings	66,638	105,175	167,867	227,552	202,052	204,173	209,673	228,173	188,173
Current liabilities	79,549	101,195	124,337	117,558	96,165	111,171	117,809	126,132	128,300
<b>Total liabilities and equity</b>	<b>247,389</b>	<b>316,566</b>	<b>413,797</b>	<b>468,450</b>	<b>431,857</b>	<b>461,740</b>	<b>488,768</b>	<b>534,827</b>	<b>513,548</b>
Cash	426	868	2,940	6,083	1,601	1,620	1,477	1,796	1,476
Current assets	109,674	113,779	190,034	153,844	160,958	180,585	190,411	207,145	212,818
Total fixed assets	97,013	130,644	152,452	166,558	179,317	189,554	206,900	235,906	234,272
Investments	40,276	71,275	68,371	141,965	89,981	89,981	89,981	89,981	64,981
<b>Total assets</b>	<b>247,389</b>	<b>316,566</b>	<b>413,796</b>	<b>468,450</b>	<b>431,857</b>	<b>461,740</b>	<b>488,769</b>	<b>534,828</b>	<b>513,548</b>
<b>Free cash flow (Rs mn)</b>									
Operating cash flow, excl. working capital	10,126	23,966	(18,679)	(12,139)	15,579	17,885	23,482	30,416	31,317
Working capital changes	(5,351)	8,936	(6,504)	48,461	(25,373)	(4,663)	(3,467)	(8,411)	(3,505)
Capital expenditure	(25,298)	(38,510)	(31,638)	(19,275)	(21,137)	(17,157)	(26,615)	(40,369)	(12,544)
Investments	(22,884)	(31,704)	(1,851)	(70,386)	51,984	—	—	—	25,000
Other income	941	2,067	4,692	3,187	4,724	7,388	8,623	8,348	7,473
<b>Free cash flow</b>	<b>(42,466)</b>	<b>(35,246)</b>	<b>(53,980)</b>	<b>(50,151)</b>	<b>25,777</b>	<b>3,453</b>	<b>2,022</b>	<b>(10,016)</b>	<b>47,741</b>
<b>Ratios (%)</b>									
Debt/equity	65.8	95.4	138.1	184.5	151.2	139.5	130.0	126.4	95.5
Net debt/equity	65.4	94.7	135.6	179.6	150.0	138.4	129.1	125.4	94.7
RoAE	4.1	14.9	9.8	4.7	10.1	10.9	13.7	13.1	11.7
<b>RoACE</b>	<b>2.5</b>	<b>8.8</b>	<b>6.4</b>	<b>5.8</b>	<b>8.1</b>	<b>7.5</b>	<b>8.8</b>	<b>9.7</b>	<b>8.7</b>
<b>Key assumptions</b>									
Crude throughput (mn tons)	14.0	16.7	16.8	15.8	15.8	17.0	18.5	19.3	19.3
Effective tariff protection (%)	3.1	1.4	1.3	2.4	2.3	0.9	0.9	0.9	0.9
Net refining margin (US\$/bbl)	3.9	4.3	6.6	4.0	2.7	3.5	4.4	5.0	5.0
Sales volume (mn tons)	20.1	23.4	26.2	27.0	27.5	28.8	30.3	32.1	33.9
Marketing margin (Rs/ton)	(463)	(710)	(2,345)	(5,021)	620	306	1,525	1,492	1,487
Subsidy under-recoveries (Rs mn)	(23,372)	(7,685)	(31,191)	5,587	(12,297)	(11,342)	(9,234)	(9,450)	(9,219)

Source: Company, Kotak Institutional Equities estimates

## Consolidated profit model, balance sheet, cash model of IOCL, March fiscal year-ends, 2006-2014E (Rs mn)

	2006	2007	2008	2009	2010E	2011E	2012E	2013E	2014E
<b>Profit model (Rs mn)</b>									
Net sales	1,729,474	2,149,428	2,444,378	3,041,265	2,691,360	3,273,638	3,513,919	3,950,311	4,177,345
<b>EBITDA</b>	<b>82,044</b>	<b>110,451</b>	<b>120,872</b>	<b>61,445</b>	<b>178,821</b>	<b>151,844</b>	<b>175,479</b>	<b>182,789</b>	<b>185,216</b>
Other income	21,310	27,451	43,748	45,155	37,890	31,809	31,679	33,046	32,093
Interest	(12,101)	(17,058)	(17,556)	(41,758)	(16,638)	(9,976)	(18,620)	(19,570)	(16,095)
Depreciation	(24,711)	(28,686)	(29,918)	(31,389)	(34,943)	(47,929)	(49,470)	(52,786)	(53,696)
Pretax profits	66,542	92,157	117,145	33,453	165,130	125,749	139,068	143,479	147,518
Extraordinary items	5,590	24,757	5,374	—	(17,232)	—	—	—	—
Tax	(19,975)	(25,834)	(38,293)	(13,316)	(46,713)	(31,493)	(39,774)	(44,455)	(48,016)
Deferred taxation	(1,282)	(8,040)	(473)	1,435	5,556	(10,278)	(6,421)	(3,205)	(985)
Net profits	51,125	82,729	83,430	25,523	108,238	83,978	92,873	95,819	98,516
<b>Net profits after minority interests</b>	<b>45,362</b>	<b>62,469</b>	<b>74,573</b>	<b>27,437</b>	<b>117,688</b>	<b>82,567</b>	<b>90,855</b>	<b>93,061</b>	<b>95,586</b>
<b>Earnings per share (Rs)</b>	<b>19.4</b>	<b>26.2</b>	<b>31.3</b>	<b>11.5</b>	<b>48.5</b>	<b>34.0</b>	<b>37.4</b>	<b>38.3</b>	<b>39.4</b>
<b>Balance sheet (Rs mn)</b>									
Total equity	317,977	378,117	450,449	470,654	547,803	588,835	648,323	709,719	772,846
Deferred tax liability	50,602	59,859	60,331	58,876	54,072	63,598	70,019	73,224	74,210
Total borrowings	292,395	290,215	382,818	465,250	497,523	502,859	427,813	368,168	288,273
Current liabilities	286,716	330,791	386,724	376,107	472,991	503,799	518,662	546,294	556,187
<b>Total liabilities and equity</b>	<b>947,691</b>	<b>1,058,981</b>	<b>1,280,322</b>	<b>1,370,888</b>	<b>1,572,389</b>	<b>1,659,091</b>	<b>1,664,817</b>	<b>1,697,405</b>	<b>1,691,517</b>
Cash	8,080	9,385	8,413	8,076	13,501	10,176	10,212	10,288	9,454
Current assets	413,904	437,178	599,256	473,965	648,895	739,624	764,794	825,787	849,029
Total fixed assets	383,717	415,014	460,307	565,545	690,165	705,381	710,901	682,420	654,125
Investments	141,990	197,403	212,345	323,301	219,828	203,910	178,910	178,910	178,910
<b>Total assets</b>	<b>947,691</b>	<b>1,058,981</b>	<b>1,280,322</b>	<b>1,370,888</b>	<b>1,572,389</b>	<b>1,659,091</b>	<b>1,664,817</b>	<b>1,697,405</b>	<b>1,691,517</b>
<b>Free cash flow (Rs mn)</b>									
Operating cash flow, excl. working capital	(10,334)	(44,660)	(107,263)	(345,677)	95,357	97,307	112,864	122,426	104,055
Working capital changes	(8,136)	2,237	(1,414)	76,881	(36,589)	(68,428)	(6,210)	(46,854)	7,919
Capital expenditure	(49,042)	(50,969)	(79,586)	(135,923)	(126,405)	(55,429)	(51,507)	(24,262)	(26,853)
Investments	(17,778)	99,768	92,665	299,410	98,991	14,188	25,015	14	849
Other Income	10,317	13,582	18,253	16,413	7,950	31,166	30,649	31,871	30,875
<b>Free cash flow</b>	<b>(74,973)</b>	<b>19,958</b>	<b>(77,346)</b>	<b>(88,896)</b>	<b>39,303</b>	<b>18,805</b>	<b>110,811</b>	<b>83,195</b>	<b>116,845</b>
<b>Ratios (%)</b>									
Debt/equity	79.3	66.3	74.9	87.9	82.7	77.1	59.6	47.0	34.0
Net debt/equity	77.1	64.1	73.3	86.3	80.4	75.5	58.1	45.7	32.9
RoAE	13.7	16.1	16.3	5.5	21.5	13.6	13.6	12.7	12.0
<b>RoACE</b>	<b>9.3</b>	<b>11.3</b>	<b>11.2</b>	<b>4.8</b>	<b>12.4</b>	<b>9.0</b>	<b>9.8</b>	<b>9.8</b>	<b>9.7</b>
<b>Key assumptions (IOC standalone)</b>									
Crude throughput (mn tons)	38.5	44.0	47.4	51.3	50.7	51.8	51.8	51.8	51.8
Effective tariff protection (%)	3.1	1.6	1.3	2.8	2.2	0.8	0.8	0.8	0.8
Net refining margin (US\$/bbl)	4.8	4.2	8.2	3.6	4.5	4.9	5.9	6.4	6.4
Sales volume (mn tons)	50.4	53.4	57.4	61.0	63.6	67.2	71.0	75.1	79.5
Marketing margin (Rs/ton)	26	(633)	(2,203)	(5,253)	850	357	1,509	1,471	1,463
Subsidy under-recoveries (Rs mn)	(47,740)	(21,900)	(97,738)	—	(31,588)	(27,056)	(21,917)	(21,997)	(21,221)

Source: Company, Kotak Institutional Equities estimates

## Profit model, balance sheet, cash model of GAIL, March fiscal year-ends, 2006-2014E (Rs mn)

	2006	2007	2008	2009	2010E	2011E	2012E	2013E	2014E
<b>Profit model (Rs mn)</b>									
Net sales	163,513	160,472	180,082	237,760	250,404	421,536	606,813	745,270	788,122
<b>EBITDA</b>	<b>35,981</b>	<b>30,649</b>	<b>39,275</b>	<b>40,647</b>	<b>47,761</b>	<b>49,660</b>	<b>75,121</b>	<b>89,655</b>	<b>95,066</b>
Other income	4,555	5,450	5,564	7,966	4,343	5,369	4,975	5,327	5,573
Interest	(1,174)	(1,071)	(796)	(870)	(700)	(1,150)	(5,049)	(7,213)	(5,866)
Depreciation	(5,595)	(5,754)	(5,710)	(5,599)	(5,618)	(6,607)	(9,628)	(12,866)	(14,864)
<b>Pretax profits</b>	<b>33,767</b>	<b>29,274</b>	<b>38,333</b>	<b>42,144</b>	<b>45,785</b>	<b>47,272</b>	<b>65,419</b>	<b>74,904</b>	<b>79,908</b>
Tax	(9,221)	(7,941)	(12,525)	(13,941)	(13,750)	(13,148)	(11,799)	(11,920)	(13,065)
Deferred taxation	(445)	(190)	(10)	(62)	(636)	(900)	(4,445)	(7,294)	(6,340)
<b>Net profits</b>	<b>23,350</b>	<b>24,619</b>	<b>26,015</b>	<b>28,037</b>	<b>31,399</b>	<b>33,225</b>	<b>49,175</b>	<b>55,690</b>	<b>60,504</b>
<b>Earnings per share (Rs)</b>	<b>18.4</b>	<b>19.4</b>	<b>20.5</b>	<b>22.1</b>	<b>24.8</b>	<b>26.2</b>	<b>38.8</b>	<b>43.9</b>	<b>47.7</b>
<b>Balance sheet (Rs mn)</b>									
Total equity	99,733	113,929	130,049	147,696	167,991	188,643	219,329	253,571	291,148
Deferred taxation liability	12,997	13,187	13,197	13,259	13,896	14,795	19,240	26,534	32,874
Total borrowings	19,166	13,379	12,659	12,001	14,804	53,253	131,053	133,853	81,653
Current liabilities	37,522	45,512	60,604	81,548	103,784	116,199	100,427	115,928	120,553
<b>Total liabilities and equity</b>	<b>169,418</b>	<b>186,007</b>	<b>216,509</b>	<b>254,505</b>	<b>300,475</b>	<b>372,891</b>	<b>470,049</b>	<b>529,885</b>	<b>526,228</b>
Cash	44,959	26,604	44,730	34,562	41,720	26,100	20,298	21,212	24,776
Other current assets	28,309	50,851	59,370	87,804	95,408	122,577	148,828	165,979	168,043
Total fixed assets	81,716	93,913	97,500	114,767	142,617	203,484	280,193	321,965	312,679
Investments	14,434	14,638	14,909	17,373	20,730	20,730	20,730	20,730	20,730
<b>Total assets</b>	<b>169,418</b>	<b>186,007</b>	<b>216,509</b>	<b>254,505</b>	<b>300,475</b>	<b>372,891</b>	<b>470,050</b>	<b>529,886</b>	<b>526,228</b>
<b>Free cash flow (Rs mn)</b>									
Operating cash flow, excl. working capital	25,165	23,920	33,692	30,456	33,152	33,699	55,226	65,945	72,368
Working capital changes	5,950	(10,151)	(388)	(5,573)	14,632	(14,754)	(42,023)	(1,651)	2,561
Capital expenditure	(5,811)	(20,449)	(12,419)	(25,535)	(33,310)	(65,810)	(83,290)	(50,060)	(1,810)
Investments	(6,462)	(205)	(270)	(2,464)	(3,358)	—	—	—	—
Other income	3,995	3,884	4,042	5,243	4,343	5,369	4,975	5,327	5,573
<b>Free cash flow</b>	<b>22,837</b>	<b>(3,002)</b>	<b>24,658</b>	<b>2,127</b>	<b>15,459</b>	<b>(41,496)</b>	<b>(65,112)</b>	<b>19,561</b>	<b>78,691</b>
<b>Ratios (%)</b>									
Debt/equity	17.0	10.5	8.8	7.5	8.1	26.2	54.9	47.8	25.2
Net debt/equity	(22.9)	(10.4)	(22.4)	(14.0)	(14.8)	13.3	46.4	40.2	17.6
ROAE (%)	22.1	20.5	19.2	18.4	18.3	17.2	22.3	21.5	20.0
<b>ROACE (%)</b>	<b>19.9</b>	<b>16.1</b>	<b>17.8</b>	<b>17.5</b>	<b>17.2</b>	<b>15.0</b>	<b>16.9</b>	<b>15.6</b>	<b>15.8</b>

Source: Company, Kotak Institutional Equities estimates

## Profit model, balance sheet, cash model of OIL, March fiscal year-ends, 2006-2014E (Rs mn)

	2006	2007	2008	2009	2010E	2011E	2012E	2013E	2014E
<b>Profit model (Rs mn)</b>									
Net sales	55,502	53,892	60,819	72,414	80,728	89,526	102,379	108,778	110,424
<b>EBITDA</b>	<b>26,554</b>	<b>22,292</b>	<b>23,852</b>	<b>28,339</b>	<b>38,756</b>	<b>46,967</b>	<b>56,295</b>	<b>60,558</b>	<b>60,779</b>
Other income	3,639	5,335	6,770	9,372	7,869	9,223	9,906	10,931	12,135
Interest	(152)	(151)	(383)	(26)	(37)	(24)	(9)	—	—
Depreciation and depletion	(3,314)	(2,595)	(3,093)	(3,768)	(7,638)	(9,110)	(11,455)	(12,641)	(13,975)
Pretax profits	26,728	24,881	27,145	33,916	38,951	47,056	54,737	58,848	58,939
Tax	(9,347)	(7,406)	(8,538)	(11,910)	(11,598)	(15,505)	(18,204)	(19,565)	(19,591)
Deferred tax	(498)	(1,020)	(707)	(343)	(1,211)	(125)	22	17	13
<b>Net profits</b>	<b>16,883</b>	<b>16,454</b>	<b>17,901</b>	<b>21,663</b>	<b>26,142</b>	<b>31,425</b>	<b>36,555</b>	<b>39,300</b>	<b>39,361</b>
<b>Earnings per share (Rs)</b>	<b>78.9</b>	<b>76.9</b>	<b>83.6</b>	<b>101.2</b>	<b>115.0</b>	<b>130.7</b>	<b>152.0</b>	<b>163.4</b>	<b>163.7</b>
<b>Balance sheet (Rs mn)</b>									
Total equity	58,483	68,491	79,330	93,310	137,697	156,785	179,320	203,198	227,138
Deferred tax liability	7,013	8,033	8,655	8,998	10,209	10,334	10,312	10,296	10,283
Liability for abandonment cost	10	11	11	15	19	19	19	19	19
Total borrowings	3,341	8,140	1,749	565	375	213	—	—	—
Current liabilities	11,668	10,320	17,541	30,914	32,693	32,496	33,437	34,106	34,165
<b>Total liabilities and equity</b>	<b>80,515</b>	<b>94,995</b>	<b>107,286</b>	<b>133,801</b>	<b>180,992</b>	<b>199,846</b>	<b>223,088</b>	<b>247,619</b>	<b>271,605</b>
Cash	31,015	32,757	42,808	60,700	85,487	92,205	105,047	121,547	139,206
Current assets	14,540	22,350	18,957	22,853	37,266	40,015	42,370	43,542	43,843
Total fixed assets	30,658	35,813	40,633	45,361	49,460	58,848	66,893	73,752	79,777
Investments	4,302	4,075	4,887	4,887	8,594	8,594	8,594	8,594	8,594
Deferred expenditure	—	—	—	—	184	184	184	184	184
<b>Total assets</b>	<b>80,515</b>	<b>94,995</b>	<b>107,286</b>	<b>133,801</b>	<b>180,992</b>	<b>199,846</b>	<b>223,088</b>	<b>247,619</b>	<b>271,605</b>
<b>Free cash flow (Rs mn)</b>									
Operating cash flow, excl. working capital	19,843	18,357	20,104	27,246	24,645	27,938	34,082	36,994	37,188
Working capital changes	5,884	(8,696)	7,435	2,368	(12,813)	(2,946)	(1,413)	(503)	(242)
Capital expenditure	(6,108)	(9,370)	(9,492)	(8,496)	(9,224)	(14,998)	(15,500)	(15,500)	(16,000)
Investments	(2,482)	226	(811)	—	(3,708)	—	—	—	—
Other income	1,670	2,892	4,214	5,470	7,869	9,223	9,906	10,931	12,135
<b>Free cash flow</b>	<b>18,807</b>	<b>3,409</b>	<b>21,450</b>	<b>26,587</b>	<b>6,769</b>	<b>19,217</b>	<b>27,074</b>	<b>31,921</b>	<b>33,081</b>
<b>Ratios (%)</b>									
Debt/equity	5.7	11.9	2.2	0.6	0.3	0.1	—	—	—
Net debt/equity	(33.1)	(32.8)	(31.9)	(31.9)	(38.3)	(38.1)	(39.9)	(43.0)	(46.2)
RoAE	28.1	23.2	21.8	22.8	20.9	20.0	20.5	19.5	17.5
<b>RoACE</b>	<b>28.0</b>	<b>23.0</b>	<b>21.5</b>	<b>22.7</b>	<b>20.9</b>	<b>19.9</b>	<b>20.5</b>	<b>19.5</b>	<b>17.5</b>
<b>Key assumptions</b>									
Rs/dollar rate	44.3	45.3	40.3	45.8	47.4	45.0	45.3	45.3	45.3
Crude fob price (US\$/bbl)	57.2	64.8	78.9	83.0	67.1	75.0	75.0	80.0	80.0
Ceiling/actual natural gas price (Rs/'000 cm)	3,515	3,200	3,200	3,200	3,200	6,783	7,500	7,500	7,500
Subsidy loss (Rs bn)	9.8	19.9	23.1	30.2	15.5	19.8	14.7	17.0	17.6

Source: Company, Kotak Institutional Equities estimates



## Consolidated profit model, balance sheet, cash model of ONGC, March fiscal year-ends, 2006-2014E (Rs mn)

	2006	2007	2008	2009	2010E	2011E	2012E	2013E	2014E
<b>Profit model (Rs mn)</b>									
Net sales	807,603	966,542	1,091,644	1,200,176	1,090,473	1,216,504	1,342,039	1,502,009	1,500,352
<b>EBITDA</b>	<b>310,054</b>	<b>357,707</b>	<b>407,481</b>	<b>418,299</b>	<b>468,954</b>	<b>529,826</b>	<b>595,843</b>	<b>650,822</b>	<b>643,377</b>
Other income	27,350	45,378	53,565	56,197	29,934	33,332	48,601	65,255	80,598
Interest	(537)	394	(12,027)	(11,442)	(6,212)	(1,454)	(1,382)	(6,860)	(6,140)
Depreciation and depletion	(97,726)	(119,550)	(138,624)	(153,985)	(186,996)	(167,845)	(200,524)	(195,662)	(188,121)
Pretax profits	239,141	283,928	310,395	309,069	305,680	393,858	442,538	513,555	529,713
Tax	(71,196)	(88,986)	(102,908)	(111,333)	(94,961)	(122,189)	(137,424)	(153,040)	(155,432)
Deferred tax	(13,612)	(9,264)	(6,471)	(3,495)	(12,077)	(2,149)	(953)	(4,094)	(5,548)
Net profits	154,596	178,119	202,767	200,063	198,832	269,520	304,160	356,421	368,733
<b>Net profits after minority interests</b>	<b>153,542</b>	<b>176,627</b>	<b>199,156</b>	<b>196,679</b>	<b>195,675</b>	<b>267,240</b>	<b>301,814</b>	<b>355,219</b>	<b>366,937</b>
<b>Earnings per share (Rs)</b>	<b>71.8</b>	<b>82.6</b>	<b>93.1</b>	<b>92.0</b>	<b>91.5</b>	<b>124.9</b>	<b>141.1</b>	<b>166.1</b>	<b>171.6</b>
<b>Balance sheet (Rs mn)</b>									
Total equity	578,830	670,137	786,657	929,353	1,045,186	1,207,091	1,388,672	1,598,389	1,814,000
Deferred tax liability	71,557	80,976	87,227	92,076	104,153	106,302	107,255	111,349	116,897
Liability for abandonment cost	128,675	151,857	129,325	171,451	175,368	175,368	175,368	175,368	175,368
Total borrowings	28,767	21,826	22,039	73,633	57,256	39,724	119,124	111,274	96,674
Current liabilities	142,435	187,051	251,797	293,480	237,041	243,772	258,662	284,445	293,919
<b>Total liabilities and equity</b>	<b>950,264</b>	<b>1,111,847</b>	<b>1,277,045</b>	<b>1,559,994</b>	<b>1,619,004</b>	<b>1,772,257</b>	<b>2,049,081</b>	<b>2,280,826</b>	<b>2,496,858</b>
Cash	90,743	206,262	249,807	224,671	212,010	339,207	572,045	834,646	1,094,768
Current assets	240,210	192,652	257,384	309,494	295,048	329,942	346,390	371,749	376,334
Total fixed assets	565,722	643,219	695,227	871,287	950,589	936,809	964,348	908,133	859,458
Goodwill	14,172	27,686	22,847	111,108	111,108	111,108	111,108	111,108	111,108
Investments	35,753	36,888	45,041	36,926	43,744	48,684	48,684	48,684	48,684
Deferred expenditure	3,663	5,141	6,739	6,506	6,506	6,506	6,506	6,506	6,506
<b>Total assets</b>	<b>950,264</b>	<b>1,111,848</b>	<b>1,277,045</b>	<b>1,559,994</b>	<b>1,619,005</b>	<b>1,772,257</b>	<b>2,049,081</b>	<b>2,280,826</b>	<b>2,496,859</b>
<b>Free cash flow (Rs mn)</b>									
Operating cash flow, excl. working capital	216,736	252,772	284,517	274,321	262,045	327,885	382,382	417,414	408,297
Working capital changes	46,461	(4,990)	(24,929)	(109,306)	(41,073)	21,836	58,443	33,489	4,888
Capital expenditure	(113,738)	(135,049)	(166,427)	(208,137)	(154,415)	(75,767)	(153,409)	(65,938)	(65,938)
Investments	(28,912)	53,822	(7,348)	(92,159)	(6,817)	—	—	—	—
Other income	14,537	20,422	22,822	31,612	29,934	33,332	48,601	65,255	80,598
<b>Free cash flow</b>	<b>135,083</b>	<b>186,976</b>	<b>108,636</b>	<b>(103,668)</b>	<b>89,674</b>	<b>307,285</b>	<b>336,017</b>	<b>450,219</b>	<b>427,844</b>
<b>Ratios (%)</b>									
Debt/equity	5.0	3.3	2.8	7.9	5.5	3.3	8.6	7.0	5.3
Net debt/equity	(10.7)	(27.5)	(29.0)	(16.3)	(14.8)	(24.8)	(32.6)	(45.3)	(55.0)
RoAE	25.9	25.5	24.8	21.0	18.3	22.0	21.8	22.4	20.4
<b>RoACE</b>	<b>22.0</b>	<b>22.0</b>	<b>21.9</b>	<b>18.3</b>	<b>16.1</b>	<b>19.2</b>	<b>19.3</b>	<b>20.3</b>	<b>18.7</b>
<b>Key assumptions</b>									
Rs/dollar rate	44.3	45.3	40.3	45.8	47.4	45.0	45.3	45.3	45.3
Crude fob price (US\$/bbl)	57.2	64.8	78.9	83.0	67.1	75.0	75.0	80.0	80.0
Ceiling/actual natural gas price (Rs/'000 cm)	3,515	3,200	3,200	3,200	3,200	6,783	7,500	7,500	7,500
Subsidy loss (Rs bn)	119.6	170.2	220.0	282.3	115.5	143.7	106.7	124.0	128.0

Source: Company, Kotak Institutional Equities estimates

JULY 15, 2010

UPDATE

BSE-30: 17,938

**Volume momentum strong but watch for wage pressures.** We see increasing probability of another round of wage hikes across the Indian IT industry, putting pressure on the cost of delivery for the companies. We expect strong volume momentum to sustain; however, increased confidence in demand and rising attrition makes bench correction an immediate priority for several companies, leading to substantial premium for lateral hires in the market. We expect the Tier-I companies to better absorb the cost pressures and reiterate our positive stance on the Tier-I pack.

#### Strong demand momentum likely to sustain

Signals of strong demand momentum abound, the latest being (1) strong sequential volume growth reported by the industry bellwether Infosys, mid-size companies like iGate & Infotech, and (2) positive outlook on enterprise IT spending from the likes of Intel, SAP, Oracle, and Accenture. As highlighted in some of our earlier notes, strong demand outlook is being driven by sustained spending uptick across verticals, return of secular offshoring trend, as well as some uptick in discretionary spending.

#### However, wage pressures are intensifying

A sudden surge in demand at a time of thin benches in several companies (a result of the downturn-driven caution) has led to a sharp increase in activity in the lateral hiring market. We note that the 'target bench levels' for IT services companies are a function of projected growth rates, attrition levels and time-to-hire in the market. Indian companies, in our view, are stretching to build their benches on account of three simultaneous developments:

- ▶ Sharp improvement in demand outlook – better pipelines, faster conversion
- ▶ Sharp jump in attrition levels across the board. The market has clearly turned into an employee's market
- ▶ Time-to-hire has also increased, with several companies increasing the notice period for the leaving employees (to as much as three months).

In addition, there is increased pressure from clients – existing ones do not want any disruption to ongoing projects on account of attrition, while new ones are keenly evaluating the readiness of vendors to ramp up projects.

All of this has led to a situation where lateral hires are being offered 30-80% premiums over their current base salaries as companies (especially the mid-sized ones) look to back-fill attrition and correct their bench levels. In addition, the MNC captives are back in the hiring mode, in good numbers – this typically exacerbates wage pressure in the market. Importantly, we also fear internal rumblings in workforces as lateral hires enter in at higher wages than incumbents at the same levels.

#### Cannot rule out another round of wage hike; Tier-I's better positioned to manage margins

We see an increasing possibility of another round of wage hike in the industry over the next six months. This would pressure gross margins across the industry – better volume growth and greater execution efficiency should enable Tier-I companies to absorb this pressure better, in our view. We remain positive on demand environment and the Tier-I pack.

Kawaljeet Saluja  
kawaljeet.saluja@kotak.com  
Mumbai: +91-22-6634-1243

Rohit Chordia  
rohit.chordia@kotak.com  
Mumbai: +91-22-6634-1397

Vineet Thodge  
vineet.thodge@kotak.com  
Mumbai: +91-22-6634-1225

Kotak Institutional Equities Research  
kotak.research@kotak.com  
Mumbai: +91-22-6634-1100

Exhibit 1: Increase in utilization and attrition - leading to thin bench strengths

	Mar-08	Jun-08	Sep-08	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
Infosys Technologies	68.9	68.3	69.2	66.9	65.2	64.3	64.6	66.2	67.4	71.9
Tata Consultancy Services	75.8	74.6	74.7	71.8	69.4	71.3	73.6	77.2	74.3	
Wipro (a)	73.9	74.4	77.0	76.6	75.4	77.1	78.2	80.7	79.3	
Patni Computer Systems	70.0	72.9	75.0	73.1	70.3	74.4	77.0	77.4	79.9	TBA
Tech Mahindra	72.9	74.2	69.0	67.0	68.3	69.2	72.8	71.1	70.8	
Hexaware Technologies	66.2	63.7	65.9	73.8	72.2	74.8	75.7	75.2	69.1	
Mphasis BFL	69.1	70.2	76.8	73.1	74.4	74.9	81.8	78.0	74.7	

(a) Wipro Technologies only

Note: Capacity utilization rate, excluding support but including trainees

Source: Companies, Kotak Institutional Equities

Exhibit 2: Wage hikes announced by companies in recent months

Company	Comments
Infosys	Wage hike of 8% offshore and 2% onsite in Oct 2009, Another hike of 14% offshore, and 2-3% onsite in April 2010
TCS	Wage hike of 13% offshore and 2-4% onsite in April 2010
Wipro	Hike of 8-10% offshore in Feb 2010
HCL Tech	0-10% from Oct 2009
Patni	Wage hike of 12% offshore and 3% onsite in Apr 2010
Mindtree	Hike of 13-15% offshore and 2-4% onsite in Apr 2010, also changed the leave policy
Hexaware	Reversed the wage cuts done in last year in Jan 2010, announced a 15% offshore wage hike in Apr 2010
Polaris	Not announced a wage hike yet
Mphasis BFL	Wage hike effected from May-10, quantum not yet known
KPIT Cummins	8-12% offshore wage hike for selected people in Oct 2010
Infotech Enterprises	Wage hike of 10% offshore and 2-3% onsite in Apr 2010
Zensar Technologies	9.5% offshore and 2-2.5% onsite effective Jul 2010

Source: Company reports, Kotak Institutional Equities

Exhibit 3: Increased attrition: Key metric to watch for

	Mar-08	Jun-08	Sep-08	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
Infosys (LTM) (standalone)	13.4	13.6	12.8	11.8	11.1	11.1	10.9	11.6	13.4	15.8
Infosys (qtr annualized) (consol)	15.0	17.2	17.2	12.7	12.2	17.2	17.3	15.9	19.3	27.4
Tata Consultancy Services	12.0	12.1	12.4	11.9	11.4	10.7	10.8	11.5	11.8	
Wipro (a)	18.3	16.6	13.5	13.9	10.5	10.3	13.6	14.3	17.6	
Cognizant Technology Solutions	12.4	15.0	17.6	11.5	8.3	11.3	12.3	11.2	16.4	
Patni Computer Systems	23.0	21.2	20.2	18.6	15.5	13.2	11.3	13.8	17.7	TBA
Polaris Software Lab	15.2	15.2	15.2	14.1	9.5	11.0	12.0	15.4	17.4	
Hexaware Technologies	19.5	24.3	28.3	28.5	17.2	16.9	19.5	19.4	19.5	
MindTree Consulting	15.8	16.3	15.0	13.8	11.8	11.4	9.7	10.7	14.1	

(a) Wipro Technologies only

Source: Companies, Kotak Institutional Equities

## June 2010: Earnings announcement calendar

Mon	Tue	Wed	Thu	Fri	Sat
<b>12-Jul</b>	<b>13-Jul</b>	<b>14-Jul</b>	<b>15-Jul</b>	<b>16-Jul</b>	<b>17-Jul</b>
			Axis Bank	BASF India	Canara Bank
			Castrol India	Chambal Fertilisers & Chemicals	Development Credit Bank
			Colgate-Palmolive	Nava Bharat Ventures	Godrej Properties
			LIC Housing Finance	Rallis India	Sterlite Tech
			Magma Finance	State Bank of Travancore	Vardhman Textiles
			Polaris Software Lab	Supreme Industries	
			TCS	Zydus Wellnus	
			Uflex		
			UTV Software Communications		
<b>19-Jul</b>	<b>20-Jul</b>	<b>21-Jul</b>	<b>22-Jul</b>	<b>23-Jul</b>	<b>24-Jul</b>
Aventis Pharma	Jindal Hotels	Alstom Projects	ACC	Allahabad Bank	Balrampur Chini Mills
Balaji Telefilms	United Spirits	Aries Agro	Ambuja Cements	Areva T&D	Indian Bank
Container Corp	Zee Entertainment Enterprises	Century Plyboard	Bajaj Auto	BHEL	IOCL
Crompton Greaves		Kotak Mahindra Bank	Bajaj Holdings & Investments	Biocon	Maruti Suzuki
Escorts		Rural Electrification Corp	Crisil	CESC	Godrej Consumers
HDFC Bank		Thermax	Dr Reddy Laboratories	HPCL	
Jindal Saw		TVS Motor	IDBI Bank	Jaiprakash Associates	
Mindtree		United Breweries	Idea Cellular	Jet Airways	
PTC India		Yes Bank	ITC	Mahindra & Mahindra Financials	
Sesa Goa			Power Finance	Praj Industries	
			Punjab National Bank	Wipro	
			Shriram Transport	IFCI	
			Thermax		
			Varun Industries		
<b>26-Jul</b>	<b>27-Jul</b>	<b>28-Jul</b>	<b>29-Jul</b>	<b>30-Jul</b>	<b>31-Jul</b>
Bharat Forge	Ashok Leyland	Chennai Petroleum	Alok Industries	ABB	GVK Power & Infra
Century Textiles	Asian Paints	Gujarat Mineral Development Corp.	Hero Honda	Bharat Electronics	ICICI Bank
Dabur India	Cadila Healthacare	Mahindra & Mahindra	Tata Tea	BPCL	
Glaxosmithkline Pharma	Cairn India	Phoenix Mills	Siemens	Indian Hotels	
Mahindra Holidays	Godrej Industries	Sun Pharmaceuticals	Ultratech Cement	PSL	
Tech Mahindra	Manglore Refinery and Petrochemicals	Lupin		Max India	
NTPC	Titan Industries	SunTV Network			
Union Bank	L&T	Sobha Develpoers			
Sterlite Industries					
<b>2-Aug</b>	<b>3-Aug</b>	<b>4-Aug</b>	<b>5-Aug</b>	<b>6-Aug</b>	<b>7-Aug</b>
India Cements	Hindalco Industries				
Madras Cement					
<b>9-Aug</b>	<b>10-Aug</b>	<b>11-Aug</b>	<b>12-Aug</b>	<b>13-Aug</b>	<b>14-Aug</b>
			Ranbaxy Laboratories		

Source: BSE, Kotak Institutional Equities

## Kotak Institutional Equities: Valuation summary of key Indian companies

Company	15-Jul-10		Mkt cap.		O/S shares (mn)	EPS (Rs)			EPS growth (%)			PER (X)			EV/EBITDA (X)			Price/BV (X)			Dividend yield (%)			RoE (%)			Target price		Upside (%)	ADVT-3mo (US\$ mn)
	Price (Rs)	Rating	(Rs mn)	(US\$ mn)		2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E		
<b>Automobiles</b>																														
Ashok Leyland	71	ADD	94,983	2,034	1,330	2.8	4.1	5.5	84.5	46.1	34.3	25.3	17.3	12.9	14.7	10.6	8.8	2.4	2.2	2.0	2.1	1.4	1.4	11.1	13.4	16.2	65	(9.0)	10.1	
Bajaj Auto	2,422	ADD	350,431	7,504	145	117.5	166.0	182.9	159.8	41.3	10.1	20.6	14.6	13.2	12.9	9.8	8.7	10.9	6.6	4.6	0.8	0.8	0.8	66.6	56.3	41.0	2,500	3.2	11.1	
Bharat Forge	331	ADD	79,701	1,707	240	0.7	11.4	18.7	(92.0)	1,553.7	64.6	482.0	29.1	17.7	23.9	11.3	7.9	2.2	2.0	1.8	—	—	—	0.9	13.9	18.2	335	1.1	4.5	
Hero Honda	1,977	SELL	394,767	8,454	200	111.8	121.5	135.7	74.1	8.7	11.7	17.7	16.3	14.6	11.4	10.7	9.2	11.0	7.5	5.6	1.5	1.6	1.8	59.1	56.6	43.8	1,800	(8.9)	19.1	
Mahindra & Mahindra	616	BUY	356,439	7,633	578	34.9	40.7	48.7	132.5	16.6	19.8	17.7	15.1	12.6	11.7	9.9	8.2	4.4	3.5	2.8	1.5	1.5	1.6	30.0	25.9	24.7	680	10.3	26.5	
Maruti Suzuki	1,375	ADD	397,447	8,511	289	86.4	94.1	104.2	104.9	8.9	10.8	15.9	14.6	13.2	8.6	8.0	6.9	3.3	2.7	2.3	0.4	0.5	0.5	23.3	20.6	18.9	1,400	1.8	19.2	
Tata Motors	810	ADD	482,608	10,335	596	23.9	27.2	35.5	138.9	13.5	30.6	33.8	29.8	22.8	13.2	13.2	11.6	2.4	2.1	1.8	0.7	0.7	0.7	8.1	7.5	8.6	900	11.2	90.7	
<b>Automobiles</b>		<b>Cautious</b>	<b>2,156,375</b>	<b>46,179</b>					<b>109.8</b>	<b>21.0</b>	<b>17.4</b>	<b>21.1</b>	<b>17.5</b>	<b>14.9</b>	<b>11.9</b>	<b>10.5</b>	<b>9.0</b>	<b>3.9</b>	<b>3.2</b>	<b>2.7</b>	<b>1.0</b>	<b>1.0</b>	<b>1.1</b>	<b>18.6</b>	<b>18.6</b>	<b>18.1</b>				
<b>Banks/Financial Institutions</b>																														
Andhra Bank	137	BUY	66,518	1,424	485	21.0	21.1	25.4	56.1	0.6	20.0	6.5	6.5	5.4	—	—	—	1.4	1.2	1.0	3.1	3.1	3.7	24.4	20.2	20.7	160	16.7	4.9	
Axis Bank	1,350	ADD	547,107	11,716	405	62.1	77.4	98.5	22.7	24.7	27.3	21.8	17.5	13.7	—	—	—	3.4	3.0	2.5	0.9	1.1	1.4	18.9	18.1	19.9	1,360	0.7	49.7	
Bank of Baroda	717	BUY	261,992	5,611	366	83.7	93.2	114.7	37.3	11.4	23.0	8.6	7.7	6.3	—	—	—	1.9	1.6	1.3	2.1	2.3	2.9	24.4	22.6	23.2	825	15.1	10.4	
Bank of India	391	REDUCE	205,422	4,399	526	33.1	42.7	56.7	(42.1)	28.9	32.8	11.8	9.2	6.9	—	—	—	1.6	1.4	1.2	1.8	2.3	3.1	14.2	16.4	19.1	360	(7.8)	6.4	
Canara Bank	474	ADD	194,299	4,161	410	73.7	77.0	93.6	45.8	4.5	21.4	6.4	6.2	5.1	—	—	—	1.5	1.3	1.0	1.7	2.1	2.5	23.0	19.6	20.1	500	5.5	7.1	
Corporation Bank	534	BUY	76,567	1,640	143	81.6	86.7	100.3	31.1	6.3	15.7	6.5	6.2	5.3	—	—	—	1.3	1.1	1.0	3.1	3.3	3.8	21.9	19.9	19.8	650	21.8	1.1	
Federal Bank	354	BUY	60,554	1,297	171	27.2	38.7	48.0	(7.2)	42.3	24.2	13.0	9.2	7.4	—	—	—	1.3	1.2	1.0	1.4	2.0	2.5	10.3	13.4	14.8	360	1.7	6.0	
HDFC	3,045	ADD	874,149	18,720	287	98.4	116.1	138.9	22.7	17.9	19.6	30.9	26.2	21.9	—	—	—	5.8	5.1	4.5	1.2	1.3	1.6	20.0	20.6	21.7	3,450	13.3	38.7	
HDFC Bank	2,063	BUY	944,141	20,219	458	64.4	84.1	110.4	22.1	30.6	31.2	32.0	24.5	18.7	—	—	—	4.4	3.8	3.3	0.6	0.8	1.0	16.1	16.7	19.1	2,200	6.7	31.0	
ICICI Bank	882	REDUCE	983,165	21,054	1,115	36.1	47.5	58.4	6.9	31.7	22.9	24.4	18.6	15.1	—	—	—	1.9	1.8	1.7	1.4	1.8	2.2	8.0	10.0	11.5	980	11.1	87.0	
IDFC	191	ADD	278,622	5,967	1,459	8.2	9.2	11.3	41.1	13.3	22.8	23.4	20.7	16.8	—	—	—	4.0	2.6	2.2	0.7	0.9	1.1	16.1	15.2	14.5	205	7.3	23.4	
India Infoline	99	BUY	30,962	663	312	8.1	8.9	10.0	59.2	9.8	12.5	12.2	11.1	9.9	—	—	—	2.0	1.6	1.3	3.2	1.9	2.4	16.4	15.9	16.1	140	41.0	4.1	
Indian Bank	240	BUY	103,209	2,210	430	35.1	35.5	43.8	25.5	1.1	23.6	6.8	6.8	5.5	—	—	—	1.5	1.3	1.1	2.5	2.5	3.1	24.0	20.3	21.2	280	16.6	4.3	
Indian Overseas Bank	111	BUY	60,200	1,289	545	13.0	15.4	26.4	(46.7)	18.9	71.3	8.5	7.2	4.2	—	—	—	0.9	0.8	0.7	3.7	4.1	4.5	9.6	10.6	16.3	120	8.6	4.0	
J&K Bank	818	BUY	39,643	849	48	105.7	112.3	140.6	25.1	6.3	25.2	7.7	7.3	5.8	—	—	—	1.4	1.2	1.1	2.7	2.9	3.6	17.3	16.9	18.5	850	4.0	0.5	
UC Housing Finance	1,074	ADD	102,019	2,185	95	69.7	93.2	104.2	11.4	33.8	11.7	15.4	11.5	10.3	—	—	—	3.1	2.7	2.2	1.4	1.9	2.1	23.6	23.8	22.4	1,050	(2.2)	20.1	
Mahindra & Mahindra Financial	492	BUY	47,227	1,011	96	35.7	42.6	49.8	59.3	19.3	16.8	13.8	11.5	9.9	—	—	—	2.8	2.4	2.0	1.5	1.8	2.2	21.4	21.7	21.6	500	1.6	1.3	
Oriental Bank of Commerce	363	ADD	90,908	1,947	251	45.3	52.8	58.6	25.3	16.5	11.0	8.0	6.9	6.2	—	—	—	1.3	1.1	1.0	2.5	2.9	3.3	14.1	15.4	15.3	400	10.2	4.4	
PFC	312	REDUCE	358,449	7,676	1,148	20.5	22.5	25.9	53.5	9.9	15.1	15.3	13.9	12.1	—	—	—	2.8	2.5	2.2	1.6	1.8	2.1	18.8	18.0	18.2	240	(23.2)	3.0	
Punjab National Bank	1,062	BUY	334,930	7,173	315	123.8	138.8	169.6	26.3	12.1	22.2	8.6	7.7	6.3	—	—	—	2.1	1.7	1.4	2.1	2.6	3.2	26.4	24.5	24.7	1,150	8.3	8.4	
Reliance Capital	801	ADD	197,113	4,221	246	13.8	16.1	14.1	(64.9)	17.0	(12.4)	58.0	49.6	56.6	—	—	—	2.9	2.8	2.7	0.8	0.8	0.7	5.0	5.7	4.8	875	9.3	39.1	
Rural Electrification Corp.	297	ADD	293,452	6,284	987	20.3	24.6	30.7	23.2	21.2	24.9	14.7	12.1	9.7	—	—	—	2.7	2.3	2.0	2.2	2.5	3.1	22.0	20.5	22.2	300	0.9	14.2	
Shriram Transport	592	ADD	132,110	2,829	223	39.2	49.1	62.4	30.1	25.4	27.2	15.1	12.1	9.5	—	—	—	3.6	3.0	2.5	2.0	2.5	3.2	28.4	26.1	27.8	600	1.3	4.0	
SREI	86	NR	9,995	214	116	8.3	7.9	9.9	17.8	(4.8)	25.8	10.4	10.9	8.7	—	—	—	0.8	0.8	0.7	1.4	1.4	1.4	11.1	10.5	12.3	—	—	3.9	
State Bank of India	2,440	BUY	1,549,018	33,172	635	144.4	170.9	210.6	0.5	18.3	23.2	16.9	14.3	11.6	—	—	—	2.3	2.1	1.8	1.2	1.3	1.4	14.8	15.5	16.7	2,900	18.9	99.5	
Union Bank	325	BUY	164,365	3,520	505	41.1	45.8	57.3	20.2	11.5	25.0	7.9	7.1	5.7	—	—	—	1.9	1.5	1.3	1.7	2.1	2.6	26.2	23.7	24.3	380	16.8	4.3	
Yes Bank	287	BUY	97,366	2,085	340	15.0	17.9	22.7	46.7	18.9	27.0	19.1	16.1	12.6	—	—	—	3.2	2.7	2.3	0.5	0.6	0.8	20.3	18.1	19.4	335	16.9	19.6	
<b>Banks/Financial Institutions</b>		<b>Attractive</b>	<b>8,103,504</b>	<b>173,537</b>					<b>14.7</b>	<b>17.9</b>	<b>23.7</b>	<b>16.1</b>	<b>13.7</b>	<b>11.1</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>2.5</b>	<b>2.2</b>	<b>1.9</b>	<b>1.4</b>	<b>1.6</b>	<b>1.9</b>	<b>15.5</b>	<b>15.9</b>	<b>17.1</b>				
<b>Cement</b>																														
ACC	809	SELL	152,079	3,257	188	83.2	61.8	63.4	47.9	(25.7)	2.6	9.7	13.1	12.8	5.2	6.1	5.3	2.4	2.1	1.8	2.9	2.9	2.9	29.3	19.4	17.7	830	2.5	8.2	
Ambuja Cements	110	SELL	167,766	3,593	1,522	8.0	7.9	8.1	11.4	(1.8)	2.6	13.8	14.0	13.7	7.7	8.0	7.2	2.4	2.1	1.9	1.7	1.9	1.9	19.3	16.7	15.3	98	(11.1)	5.4	
Grasim Industries	1,810	ADD	166,000	3,555	92	301.0	240.1	282.0	26.1	(20.2)	17.5	6.0	7.5	6.4	3.9	3.9	3.0	1.3	1.2	1.0	1.8	1.9	1.9	22.9	16.4	16.7	2,150	18.8	8.6	
India Cements	108	SELL	33,081	708	307	10.0	11.8	12.9	(43.5)	17.7	9.0	10.7	9.1	8.4	5.4	5.0	4.8	0.8	0.7	0.7	2.0	3.0	3.0	8.2	8.7	9.0	110			

## Kotak Institutional Equities: Valuation summary of key Indian companies

Company	15-Jul-10		Mkt cap.		O/S	EPS (Rs)			EPS growth (%)			PER (X)			EV/EBITDA (X)			Price/BV (X)			Dividend yield (%)			RoE (%)			Target price	Upside	ADVT-3mo
	Price (Rs)	Rating	(Rs mn)	(US\$ mn)	(mn)	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	(Rs)	(%)	(US\$ mn)
<b>Consumer products</b>																													
Asian Paints	2,440	BUY	234,059	5,012	96	71.5	81.5	101.1	85.3	13.9	24.2	34.1	30.0	24.1	21.0	18.6	14.8	14.6	11.6	9.3	1.1	1.4	1.8	51.8	44.4	44.0	2,500	2.5	3.0
Colgate-Palmolive (India)	845	REDUCE	114,900	2,461	136	31.1	34.5	39.6	44.2	10.9	14.6	27.1	24.5	21.4	22.2	18.1	15.5	35.2	30.0	25.7	2.4	3.1	3.5	156.1	132.3	129.4	830	(1.8)	2.3
Dabur India	212	BUY	184,000	3,940	866	5.8	6.8	8.2	28.1	17.6	20.8	36.6	31.2	25.8	27.2	21.9	18.1	17.5	14.4	11.8	1.4	1.7	2.0	54.3	51.1	50.7	200	(5.8)	2.6
GlaxoSmithKline Consumer (a)	1,761	ADD	74,060	1,586	42	55.4	70.0	82.9	23.6	26.5	18.4	31.8	25.2	21.2	17.5	14.8	12.1	8.3	6.9	5.7	1.0	1.3	1.5	27.9	29.6	29.2	1,800	2.2	0.6
Godrej Consumer Products	375	NR	115,433	2,472	308	8.7	9.8	11.6	29.7	13.2	18.2	43.2	38.1	32.3	30.6	27.3	23.0	9.8	8.6	8.6	1.1	1.1	1.1	30.7	24.1	27.8	—	—	3.5
Hindustan Unilever	263	REDUCE	573,962	12,291	2,179	9.7	10.4	11.8	1.7	7.3	14.0	27.2	25.4	22.3	18.3	17.3	14.5	22.5	19.4	16.7	2.9	3.2	3.7	91.6	82.2	80.8	230	(12.7)	12.6
ITC	300	BUY	1,130,960	24,220	3,769	10.8	12.4	14.5	24.4	15.2	17.0	27.8	24.2	20.6	17.1	15.1	12.7	7.9	6.8	5.8	3.3	1.8	2.0	29.9	32.2	32.1	315	5.0	22.5
Jubilant Foodworks	334	REDUCE	21,650	464	65	5.5	7.7	9.7	340.6	39.3	25.3	60.3	43.3	34.5	32.6	22.8	16.1	18.4	12.9	9.4	—	—	—	46.6	35.1	31.5	290	(13.2)	7.3
Jyothy Laboratories	271	NR	19,641	421	73	11.0	12.9	15.3	99.6	17.0	18.3	24.5	21.0	17.7	18.9	14.4	11.8	4.8	4.1	3.5	1.7	1.3	1.7	18.6	20.2	20.5	—	—	1.3
Nestle India (a)	2,977	REDUCE	287,054	6,147	96	74.4	87.0	105.5	27.0	17.0	21.3	40.0	34.2	28.2	26.4	23.4	20.1	49.4	39.2	31.0	1.6	2.0	2.5	136.0	127.8	122.7	3,000	0.8	2.2
Tata Global Beverages	116	BUY	71,518	1,532	618	6.6	7.4	8.4	23.4	11.1	13.8	17.5	15.7	13.8	11.2	9.1	8.2	1.4	1.3	1.3	1.9	2.1	2.4	10.9	11.4	12.0	125	8.1	3.7
<b>Consumer products</b>	<b>Attractive</b>		<b>2,827,236</b>	<b>60,545</b>					<b>23.7</b>	<b>13.6</b>	<b>17.3</b>	<b>29.7</b>	<b>26.1</b>	<b>22.3</b>	<b>19.1</b>	<b>16.9</b>	<b>14.2</b>	<b>10.1</b>	<b>8.8</b>	<b>7.6</b>	<b>2.5</b>	<b>2.1</b>	<b>2.4</b>	<b>34.1</b>	<b>33.5</b>	<b>34.0</b>			
<b>Constructions</b>																													
IVRCL	188	BUY	50,064	1,072	267	7.8	10.3	12.4	(7.7)	32.4	19.7	24.0	18.1	15.1	12.5	10.3	8.7	2.5	2.2	1.9	0.2	0.2	0.2	10.9	12.8	13.5	215	14.7	7.1
Nagarjuna Construction Co.	180	BUY	46,301	992	257	7.1	11.5	14.3	6.1	61.1	24.1	25.3	15.7	12.7	12.3	9.3	7.6	2.1	1.9	1.7	0.9	1.1	1.1	9.3	12.5	13.9	210	16.4	3.7
Punjab Lloyds	138	REDUCE	46,834	1,003	339	(12.9)	9.8	12.0	79.2	(175.4)	22.4	(10.7)	14.2	11.6	37.7	7.4	6.8	1.5	1.4	1.3	(0.1)	0.3	0.8	(15.8)	10.3	11.4	140	1.3	12.5
Sadbhav Engineering	1,311	BUY	19,665	421	15	43.1	62.0	84.0	(15.8)	43.9	35.5	30.4	21.2	15.6	17.0	11.0	9.0	4.7	3.2	2.7	0.3	0.5	0.5	13.3	14.1	17.4	1,450	10.6	0.3
<b>Construction</b>	<b>Attractive</b>		<b>162,864</b>	<b>3,488</b>					<b>(96.9)</b>	<b>14,481</b>	<b>24.4</b>	<b>2,405.4</b>	<b>16.5</b>	<b>13.3</b>	<b>17.0</b>	<b>8.9</b>	<b>7.7</b>	<b>2.1</b>	<b>1.9</b>	<b>1.7</b>	<b>0.3</b>	<b>0.5</b>	<b>0.7</b>	<b>0.1</b>	<b>11.3</b>	<b>12.5</b>			
<b>Energy</b>																													
Aban Offshore	861	ADD	37,440	802	43	106.6	172.3	103.6	10.0	61.6	(39.8)	8.1	5.0	8.3	8.4	6.2	6.8	1.7	0.9	0.9	0.4	0.4	0.5	24.3	20.8	11.1	900	4.6	49.9
Bharat Petroleum	656	ADD	237,279	5,081	362	62.1	54.3	67.6	201	(12)	24.5	11	12	9.7	5.8	5.9	5.0	1.7	1.5	1.4	2.1	2.7	3.4	15.6	12.3	13.9	660	0.6	23.8
Cairn india	313	SELL	593,656	12,713	1,897	5.5	28.5	40.0	29.0	413.9	40.5	56.5	11.0	7.8	44.5	7.5	5.3	1.7	1.5	1.3	—	—	4.8	3.1	14.6	18.1	250	(20.1)	17.5
Castrol India (a)	454	REDUCE	112,216	2,403	247	15.4	19.6	20.6	45	27	5.3	29	23	22.0	17.5	14.2	13.4	24.4	22.8	21.0	2.8	3.4	3.5	83.8	101.6	99.2	365	(19.6)	1.2
GAIL (India)	448	ADD	568,342	12,171	1,268	24.8	26.2	38.8	11.7	5.8	48.0	18.1	17.1	11.6	10.1	10.6	8.3	3.1	2.8	2.4	1.7	1.9	2.8	17.4	16.3	21.1	495	10.5	17.2
GSPL	101	REDUCE	56,639	1,213	562	7.4	8.9	9.1	235	22	1.3	14	11	11.1	7.1	5.9	5.3	3.3	2.7	2.4	1.0	2.2	3.6	27.3	26.3	22.5	80	(20.6)	4.2
Hindustan Petroleum	446	ADD	151,063	3,235	339	52.6	45.0	62.0	210.1	(14.5)	38.0	8.5	9.9	7.2	3.1	3.5	2.7	1.1	1.0	0.9	2.7	3.2	4.4	13.3	10.3	13.0	500	12.2	29.2
Indian Oil Corporation	374	ADD	909,146	19,469	2,428	49.9	34.0	37.4	407	(32)	10.0	8	11	10.0	5.1	6.1	5.0	1.7	1.5	1.4	3.5	2.8	3.0	22.7	13.8	14.0	410	9.5	16.9
Oil India	1,346	BUY	323,604	6,930	240	115.1	130.7	152.0	13.8	13.5	16.3	11.7	10.3	8.9	4.9	4.0	3.2	2.2	1.9	1.7	2.5	3.3	3.7	16.7	17.8	18.2	1,440	7.0	7.3
Oil & Natural Gas Corporation	1,237	BUY	2,645,696	56,658	2,139	91.4	124.9	141.1	1	37	12.9	14	10	8.8	4.9	4.1	3.3	2.0	1.8	1.6	2.7	3.4	3.9	14.6	17.9	18.0	1,450	17.2	37.2
Petronet LNG	81	REDUCE	60,713	1,300	750	5.4	5.5	8.2	(22.0)	2.6	47.8	15.0	14.6	9.9	9.1	8.5	6.8	2.4	2.1	1.8	2.2	2.5	3.4	15.9	14.3	18.6	82	1.3	3.6
Reliance Industries	1,073	SELL	3,194,587	68,412	2,976	49.6	62.9	80.2	(2)	27	27.5	22	17	13.4	10.9	8.2	6.8	2.2	2.0	1.8	1.4	1.7	2.1	11.4	13.2	15.3	985	(8.2)	118.8
<b>Energy</b>	<b>Cautious</b>		<b>8,890,380</b>	<b>190,388</b>					<b>38.0</b>	<b>20.9</b>	<b>20.8</b>	<b>14.7</b>	<b>12.2</b>	<b>10.1</b>	<b>7.2</b>	<b>6.1</b>	<b>5.0</b>	<b>2.0</b>	<b>1.8</b>	<b>1.6</b>	<b>2.0</b>	<b>2.4</b>	<b>3.1</b>	<b>13.8</b>	<b>15.0</b>	<b>16.3</b>			
<b>Industrials</b>																													
ABB	870	REDUCE	184,403	3,949	212	16.7	23.3	37.2	(35.2)	39.2	59.8	52.0	37.3	23.4	29.8	22.0	13.6	7.6	6.5	5.2	0.2	0.4	0.4	15.6	18.8	24.7	840	(3.5)	6.5
BGR Energy Systems	742	BUY	53,453	1,145	72	16.0	28.0	39.7	32.2	74.6	41.9	46.3	26.5	18.7	26.0	15.1	10.9	9.5	7.6	5.8	0.4	0.9	1.1	22.3	31.8	35.1	800	7.8	3.3
Bharat Electronics	1,780	REDUCE	142,424	3,050	80	93.9	111.8	127.4	(9.6)	19.1	13.9	19.0	15.9	14.0	9.1	7.3	6.2	3.2	2.8	2.4	1.4	1.4	1.4	17.9	18.7	18.5	1,790	0.5	2.4
Bharat Heavy Electricals	2,439	REDUCE	1,193,743	25,564	490	88.1	113.1	137.5	37.9	28.4	21.6	27.7	21.6	17.7	15.5	11.6	9.5	7.5	5.9	4.8	0.8	1.0	1.2	29.9	30.8	29.8	2,500	2.5	28.8
Crompton Greaves	263	BUY	168,920	3,617	642	12.8	13.3	15.8	46.5	3.2	19.0	20.5	19.9	16.7	11.9	10.9	9.0	6.4	5.1	4.0	0.7	0.7	0.8	36.8	28.5	26.8	290	10.1	7.8
Larsen & Toubro	1,874	BUY	1,126,159	24,117	601	58.1	71.2	90.4	16.0	22.4	27.0	32.2	26.3	20.7	17.1	14.5	11.9	5.0	4.2	3.6	0.6	0.6	0.8	18.6	17.5	18.7	1,900	1.4	54.4
Maharashtra Seamless	398	BUY	28,039	600	71	40.2	43.6	49.8	12.1	8.5	14.2	9.9	9.1	8.0	5.3	4.6	3.6	1.8	1.5	1.3	1.5	2.0	2.5	19.3	17.9	17.7	450	13.2	0.4
Siemens	740	REDUCE	249,397	5,341	337	25.0	29.6	34.3	55.2	18.6	16.0	29.6	25.0	21.5	17.5	14.4	12.1	7.3	6.0	4.9	0.7	0.8	0.9	27.3	26.3	25.1	635	(14.2)	7.1
Suzlon Energy	60	REDUCE	95,712	2,050	1,594	(5.9)	0.3	5.3	(182.3)	(104.4)	1,931.8	(10.1)	231.5	11.4	17.2	8.9	5.8	0.9	0.9	0.8	—	—	0.3	(8.8)	0.4	7.5	70	16.6	27.3

## Kotak Institutional Equities: Valuation summary of key Indian companies

Company	15-Jul-10		Mkt cap.		O/S	EPS (Rs)			EPS growth (%)			PER (X)			EV/EBITDA (X)			Price/BV (X)			Dividend yield (%)			RoE (%)			Target price	Upside	ADVT-3mo
	Price (Rs)	Rating	(Rs mn)	(US\$ mn)	(mn)	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	(Rs)	(%)	(US\$ mn)
<b>Infrastructure</b>																													
Container Corporation	1,435	REDUCE	186,482	3,994	130	61.1	74.3	85.9	0.3	21.7	15.6	23.5	19.3	16.7	16.7	13.6	11.4	4.3	3.7	3.2	1.0	1.2	1.4	19.6	20.6	20.5	1,250	(12.9)	1.8
GMR Infrastructure	62	ADD	225,887	4,837	3,667	0.4	0.2	0.1	(43.8)	(48.9)	(40.0)	142.9	279.8	466.0	24.6	15.9	14.9	2.1	1.8	1.8	—	—	—	2.4	1.2	0.7	65	5.5	6.1
GVK Power & Infrastructure	46	BUY	72,486	1,552	1,579	0.8	1.1	1.4	6.7	33.5	32.4	56.4	42.2	31.9	19.0	17.3	17.7	2.3	2.2	2.1	—	0.7	0.7	4.7	5.3	6.7	54	17.6	5.5
IRB Infrastructure	274	RS	91,118	1,951	332	9.7	12.6	12.1	83.8	29.2	(3.7)	28.2	21.8	22.7	13.3	11.8	11.0	3.9	3.0	2.4	—	—	—	15.6	15.7	11.9	—	—	5.1
Mundra Port and SEZ	747	REDUCE	301,306	6,452	403	15.1	24.1	35.7	40.8	59.5	48.4	49.5	31.0	20.9	31.7	20.4	14.5	8.3	6.4	4.8	—	—	—	18.5	23.2	26.1	725	(2.9)	6.3
<b>Infrastructure</b>		<b>Attractive</b>	<b>877,279</b>	<b>18,787</b>		<b>12.7</b>	<b>29.5</b>	<b>24.1</b>	<b>43.6</b>	<b>33.6</b>	<b>27.1</b>	<b>21.7</b>	<b>16.0</b>	<b>13.8</b>	<b>3.7</b>	<b>3.1</b>	<b>2.8</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>0.3</b>	<b>0.3</b>	<b>0.3</b>	<b>18.5</b>	<b>19.2</b>	<b>14.6</b>	<b>9.2</b>	<b>10.2</b>	
<b>Media</b>																													
DB Corp	235	ADD	42,623	913	181	10.6	12.9	15.7	276.4	21.0	22.3	22.1	18.3	14.9	12.2	10.1	8.0	6.1	4.9	4.1	0.9	1.7	2.6	38.2	29.6	29.9	280	19.2	0.3
DishTV	46	ADD	48,438	1,037	1,063	(2.5)	(1.2)	0.5	(62.6)	(49.9)	(141.4)	(18.5)	(37.0)	89.4	60.4	21.9	12.0	11.7	17.0	14.3	—	—	—	250.2	(37.4)	17.4	47	3.2	3.5
HT Media	155	NR	36,413	780	235	6.1	7.8	9.4	623.3	27.0	20.9	25.4	20.0	16.5	12.7	10.5	8.7	3.7	3.3	3.0	0.6	1.3	2.6	15.6	17.6	19.2	—	—	0.3
Jagran Prakashan	125	ADD	37,556	804	301	5.8	6.4	7.5	91.9	9.5	16.7	21.4	19.5	16.7	12.9	11.3	9.7	6.1	5.5	4.9	2.8	2.8	3.2	30.0	29.8	31.0	130	4.3	0.6
Sun TV Network	441	REDUCE	173,789	3,722	394	13.1	17.9	22.8	44.8	36.0	27.5	33.5	24.7	19.3	19.0	14.2	11.3	9.0	7.6	6.3	1.7	1.7	2.0	28.4	33.5	35.5	420	(4.8)	1.7
Zee Entertainment Enterprises	305	REDUCE	132,327	2,834	434	10.5	12.0	14.7	24.4	14.4	22.2	29.0	25.4	20.7	21.6	17.1	13.6	3.6	3.4	3.3	0.8	1.0	1.2	13.0	14.1	16.4	265	(13.1)	9.4
<b>Media</b>		<b>Neutral</b>	<b>471,146</b>	<b>10,090</b>					<b>185.0</b>	<b>40.2</b>	<b>36.2</b>	<b>38.8</b>	<b>27.7</b>	<b>20.3</b>	<b>18.7</b>	<b>14.3</b>	<b>11.1</b>	<b>5.7</b>	<b>5.2</b>	<b>4.6</b>	<b>1.2</b>	<b>1.4</b>	<b>1.8</b>	<b>14.6</b>	<b>18.7</b>	<b>22.8</b>			
<b>Metals</b>																													
Hindalco Industries	151	ADD	288,815	6,185	1,914	5.7	12.6	15.1	(64.5)	122.5	19.4	26.6	12.0	10.0	7.9	8.3	8.5	1.3	1.2	1.1	0.9	0.9	0.9	10.3	10.4	11.2	185	22.6	42.4
Hindustan Zinc	974	BUY	411,440	8,811	423	95.6	102.5	116.0	48.2	7.2	13.1	10.2	9.5	8.4	6.3	4.9	3.3	2.2	1.8	1.5	0.6	0.6	0.6	24.1	20.8	19.4	1,240	27.3	4.3
Jindal Steel and Power	630	SELL	584,309	12,513	928	38.5	48.7	50.8	17.2	26.5	4.3	16.4	12.9	12.4	10.3	8.3	7.7	5.1	3.7	2.8	0.2	0.2	0.2	37.3	33.0	25.7	575	(8.7)	29.9
JSW Steel	1,096	REDUCE	217,850	4,665	199	80.4	106.4	136.9	447.0	32.3	28.7	13.6	10.3	8.0	8.5	7.1	5.7	1.9	1.5	1.3	0.8	0.4	0.4	15.4	16.4	17.3	1,150	4.9	54.3
National Aluminium Co.	430	SELL	277,086	5,934	644	10.1	28.0	27.7	(49.0)	178.6	(1.2)	42.7	15.3	15.5	18.9	7.5	6.9	2.5	2.2	1.9	0.5	0.5	0.5	6.1	15.4	13.3	320	(25.6)	1.2
Sesa Goa	340	REDUCE	302,187	6,471	890	29.6	61.4	62.4	32.2	107.6	1.8	11.5	5.5	5.4	9.3	3.3	2.7	3.9	2.3	1.7	0.9	0.9	0.9	36.7	48.0	34.1	420	23.7	79.6
Sterilite Industries	166	ADD	558,539	11,961	3,362	12.0	14.2	19.2	2.8	18.3	35.1	13.8	11.7	8.7	11.8	10.2	6.7	1.5	1.3	1.2	0.6	0.6	0.6	12.9	12.2	14.5	210	26.4	49.2
Tata Steel	513	BUY	455,015	9,744	887	3.2	78.7	93.5	(97.1)	2,331.6	18.7	158.3	6.5	5.5	17.6	5.9	5.0	1.8	1.5	1.2	1.6	1.6	1.6	1.1	24.7	23.8	700	36.5	110.2
<b>Metals</b>		<b>Cautious</b>	<b>3,095,240</b>	<b>66,285</b>					<b>(28.9)</b>	<b>81.0</b>	<b>15.1</b>	<b>17.3</b>	<b>9.6</b>	<b>8.3</b>	<b>10.7</b>	<b>6.8</b>	<b>5.7</b>	<b>2.1</b>	<b>1.8</b>	<b>1.5</b>	<b>0.7</b>	<b>0.7</b>	<b>0.7</b>	<b>12.3</b>	<b>18.4</b>	<b>17.7</b>			
<b>Pharmaceutical</b>																													
Biocon	316	BUY	63,140	1,352	200	14.7	18.7	23.0	212.6	27.7	23.0	21.5	16.9	13.7	12.3	10.3	8.4	3.5	3.0	2.6	—	—	0.1	17.9	19.7	20.7	345	9.3	3.6
Cipla	328	REDUCE	263,037	5,633	803	13.5	12.8	15.6	35.9	(4.9)	21.9	24.3	25.5	21.0	18.0	16.9	14.2	4.5	3.9	3.4	0.8	0.8	0.8	19.9	16.3	17.4	280	(14.5)	9.9
Cadila Healthcare	637	REDUCE	130,415	2,793	205	24.7	29.6	34.9	66.9	20.0	17.6	25.8	21.5	18.3	16.6	13.9	12.1	8.1	6.2	5.0	0.8	0.9	1.1	36.1	32.8	30.3	535	(16.0)	1.7
Dishman Pharma & chemicals	217	BUY	17,629	378	81	14.4	17.2	28.8	(19.7)	19.4	67.0	15.0	12.6	7.5	10.8	9.0	6.3	2.2	1.9	1.5	—	—	—	15.5	16.3	22.7	300	38.4	0.6
Divi's Laboratories	771	ADD	101,928	2,183	132	25.8	34.3	43.9	(18.3)	33.3	27.9	30.0	22.5	17.6	22.4	16.5	12.6	6.8	5.6	4.5	—	—	—	24.8	27.2	28.4	800	3.7	3.2
Dr Reddy's Laboratories	1,469	REDUCE	248,910	5,330	169	48.1	66.7	70.8	48.3	38.8	6.1	30.6	22.0	20.8	16.9	12.8	11.9	6.6	5.2	4.3	0.5	0.5	0.6	22.2	26.3	22.6	1,150	(21.7)	16.2
GlaxoSmithkline Pharmaceuticals (a)	2,074	REDUCE	175,687	3,762	85	59.1	69.1	79.2	8.1	17.0	14.5	35.1	30.0	26.2	20.2	17.3	14.8	9.8	8.4	7.2	—	—	—	29.8	30.2	29.5	1,800	(13.2)	1.5
Glenmark Pharmaceuticals	279	NR	76,398	1,636	274	12.7	19.2	20.3	14.7	50.6	5.6	21.9	14.5	13.8	14.0	9.1	8.8	3.2	2.7	2.3	—	—	—	16.7	19.9	17.6	—	—	4.8
Jubilant Organosys	365	BUY	57,929	1,241	159	26.5	34.2	39.3	49.0	29.1	14.9	13.7	10.7	9.3	9.9	8.7	7.2	2.6	2.1	1.8	0.5	0.7	0.8	26.3	22.3	21.0	400	9.6	2.6
Lupin	1,853	ADD	164,157	3,515	89	76.9	104.1	122.5	27.8	35.3	17.6	24.1	17.8	15.1	20.6	14.9	11.7	7.1	5.3	4.1	0.7	0.8	0.8	36.6	34.4	30.7	1,920	3.6	6.9
Piramal Healthcare	507	REDUCE	106,036	2,271	209	23.4	13.4	11.0	35.5	(42.9)	(17.6)	21.7	38.0	46.1	15.9	6.4	4.8	6.3	1.1	1.0	1.1	1.2	0.7	32.1	141.2	16.6	490	(3.4)	32.0
Ranbaxy Laboratories	450	SELL	192,673	4,126	428	7.1	28.0	11.7	(128.4)	297.1	(58.3)	63.8	16.1	38.5	15.7	9.4	18.6	4.9	3.9	3.6	—	0.9	0.9	6.9	24.6	9.1	220	(51.1)	10.6
Sun Pharmaceuticals	1,748	REDUCE	362,035	7,753	207	65.2	67.7	77.6	(25.7)	3.8	14.6	26.8	25.8	22.5	20.3	18.2	15.4	4.4	3.8	3.4	0.8	0.8	0.8	17.8	16.2	16.2	1,560	(10.8)	8.6
<b>Pharmaceuticals</b>		<b>Attractive</b>	<b>1,959,975</b>	<b>41,973</b>					<b>44.7</b>	<b>27.4</b>	<b>5.8</b>	<b>27.2</b>	<b>21.4</b>	<b>20.2</b>	<b>17.0</b>	<b>13.1</b>	<b>12.3</b>	<b>5.2</b>	<b>3.7</b>	<b>3.2</b>	<b>0.5</b>	<b>0.6</b>	<b>0.6</b>	<b>18.9</b>	<b>17.3</b>	<b>15.6</b>			
<b>Property</b>																													
DLF	319	ADD	544,484	11,660	1,708	9.6	16.3	25.1	(64.0)	69.4	53.8	33.1	19.5	12.7	20.8	13.2	9.9	2.0	1.9	1.7	0.9	0.9	1.6	6.4	9.9	13.8	340	6.7	50.4
Indiabulls Real Estate	166	RS	66,744	1,429	401	1.6	4.0	8.0	109.7	151.7	101.7	104.9	41.7	20.7	(74)	37.0	9.6	0.7	0.7	0.7	—	—	—	0.8	1.8	3.5	285	71.3	21.0
Mahindra Life Space Developer	492	ADD	20,708	443	42	18.9	20.3	27.5	82.4	7.3	35.8	26.1	24.3	17.9	22.1	18.5	10.3	2.2	2.1	1.9	0.8	0.8	0.8	8.					



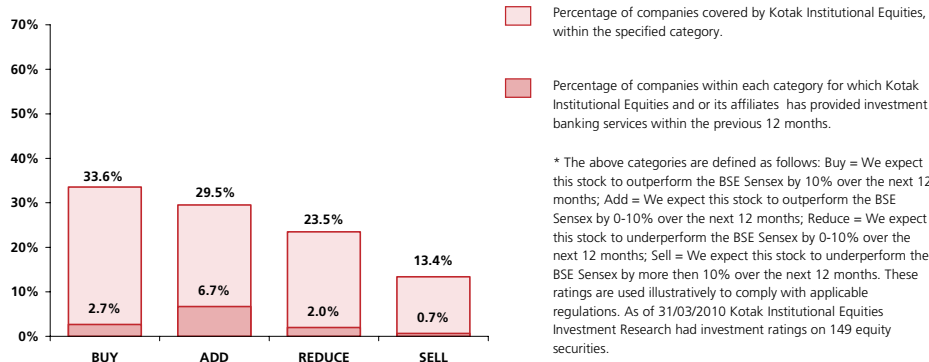
**Kotak Institutional Equities: Valuation summary of key Indian companies**

Company	15-Jul-10		Mkt cap.		O/S shares (mn)	EPS (Rs)			EPS growth (%)			PER (X)			EV/EBITDA (X)			Price/BV (X)			Dividend yield (%)			RoE (%)			Target			
	Price (Rs)	Rating	(Rs mn)	(US\$ mn)		2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	price (Rs)
<b>Retail</b>																														
Titan Industries	2,692	ADD	119,480	2,559	44	62.7	76.1	96.2	41.5	21.3	26.5	42.9	35.4	28.0	30.4	23.9	18.7	15.1	11.3	8.5	0.4	0.4	0.5	40.7	36.6	34.8	2,400	(10.8)	4.7	
<b>Retail</b>		<b>Neutral</b>	<b>119,480</b>	<b>2,559</b>					<b>41.5</b>	<b>21.3</b>	<b>26.5</b>	<b>42.9</b>	<b>35.4</b>	<b>28.0</b>	<b>30.4</b>	<b>23.9</b>	<b>18.7</b>	<b>15.1</b>	<b>11.3</b>	<b>8.5</b>	<b>0.4</b>	<b>0.4</b>	<b>0.5</b>	<b>35.2</b>	<b>32.0</b>	<b>30.5</b>				
<b>Sugar</b>																														
Bajaj Hindustan	118	SELL	22,542	483	191	9.7	9.9	8.9	201.1	2.2	(10.4)	12.1	11.9	13.2	7.1	5.8	5.5	0.9	0.9	0.8	0.6	0.6	0.6	8.1	7.5	6.3	99	(16.0)	6.6	
Balrampur Chini Mills	83	ADD	21,182	454	257	3.7	10.4	7.0	(51.9)	183.7	(32.7)	22.5	7.9	11.8	9.5	5.4	5.9	1.5	1.3	1.2	0.5	0.5	0.5	7.0	18.1	11.0	92	11.5	6.2	
Shree Renuka Sugars	69	BUY	46,451	995	670	9.9	7.6	7.8	196.4	(23.2)	3.1	7.0	9.1	8.8	4.8	5.4	4.7	1.8	1.5	1.3	0.6	0.5	0.5	32.0	18.1	15.7	76	9.6	15.1	
<b>Sugar</b>		<b>Cautious</b>	<b>90,175</b>	<b>1,931</b>					<b>96.1</b>	<b>2.5</b>	<b>(9.4)</b>	<b>9.6</b>	<b>9.3</b>	<b>10.3</b>	<b>6.2</b>	<b>5.6</b>	<b>5.2</b>	<b>1.4</b>	<b>1.2</b>	<b>1.1</b>	<b>0.6</b>	<b>0.5</b>	<b>0.5</b>	<b>14.9</b>	<b>13.3</b>	<b>10.8</b>				
<b>Technology</b>																														
HCL Technologies	358	REDUCE	246,779	5,285	690	17.8	25.1	28.5	2.0	40.6	13.6	20.0	14.3	12.6	10.2	8.7	7.2	3.9	3.2	2.7	1.1	1.1	1.7	20.8	24.9	23.3	370	3.5	12.8	
Hexaware Technologies	85	REDUCE	12,261	263	144	9.3	5.1	9.4	127.7	(45.4)	84.0	9.1	16.7	9.1	4.7	9.6	5.3	1.4	1.4	1.2	1.2	1.2	1.2	17.8	8.4	14.0	72	(15.6)	3.1	
Infosys Technologies	2,760	BUY	1,584,010	33,922	574	108.3	124.1	150.0	5.7	14.5	20.9	25.5	22.2	18.4	18.6	15.2	12.3	6.9	5.7	4.7	0.9	1.3	1.5	30.1	28.0	28.0	3,100	12.3	62.5	
Mphasis BFL	607	REDUCE	126,564	2,710	208	43.6	49.0	45.6	207.5	12.5	(7.0)	13.9	12.4	13.3	11.1	9.9	9.0	5.4	3.9	3.1	0.6	0.7	0.7	48.1	36.4	25.8	550	(9.4)	8.9	
Mindtree	574	REDUCE	23,609	506	41	52.2	38.9	51.6	294.3	(25.5)	32.6	11.0	14.7	11.1	9.4	9.1	6.4	3.5	2.9	2.3	0.4	0.7	0.9	35.2	21.4	23.1	550	(4.1)	2.2	
Patni Computer Systems	530	REDUCE	70,563	1,511	133	36.6	42.3	38.6	36.4	15.6	(8.7)	14.5	12.5	13.7	7.7	6.7	5.9	2.0	1.9	1.7	1.3	1.6	1.5	18.2	15.8	12.8	450	(15.1)	6.6	
Polaris Software Lab	193	SELL	19,257	412	100	15.4	19.1	18.8	16.9	24.3	(1.7)	12.6	10.1	10.3	6.4	8.1	7.0	2.2	1.9	1.7	1.8	1.9	2.0	18.6	20.1	17.2	180	(6.8)	4.6	
TCS	782	BUY	1,530,726	32,781	1,957	35.1	42.1	48.2	32.8	19.8	14.5	22.3	18.6	16.2	16.7	13.5	11.2	7.3	6.0	5.0	2.6	2.2	2.5	37.6	35.6	33.9	965	23.4	29.5	
Wipro	402	ADD	983,560	21,063	2,447	18.9	21.9	25.0	22.1	16.2	14.4	21.3	18.4	16.1	16.1	13.2	10.9	5.0	4.1	3.4	0.9	1.1	1.3	26.5	24.6	23.2	465	15.7	15.3	
<b>Technology</b>		<b>Attractive</b>	<b>4,597,328</b>	<b>98,452</b>					<b>22.9</b>	<b>17.3</b>	<b>15.0</b>	<b>22.0</b>	<b>18.7</b>	<b>16.3</b>	<b>15.8</b>	<b>13.1</b>	<b>10.8</b>	<b>5.9</b>	<b>4.9</b>	<b>4.1</b>	<b>1.5</b>	<b>1.5</b>	<b>1.8</b>	<b>26.7</b>	<b>25.9</b>	<b>24.8</b>				
<b>Telecom</b>																														
Bharti Airtel	298	REDUCE	1,131,685	24,235	3,798	24.0	21.4	24.2	7.5	(10.8)	13.2	12.4	13.9	12.3	7.0	6.6	5.7	2.6	2.2	1.9	1.0	1.3	1.7	24.1	17.0	16.5	290	(2.7)	51.1	
IDEA	64	REDUCE	211,352	4,526	3,300	2.7	1.3	2.3	(5.8)	(51.7)	71.9	23.4	48.5	28.2	8.2	8.1	6.6	1.9	1.8	1.7	—	—	—	7.2	3.8	6.3	50	(21.9)	11.1	
MTNL	65	SELL	40,667	871	630	(15.6)	(10.4)	(9.1)	(750.8)	(33.7)	(11.9)	(4.1)	(6.2)	(7.1)	(0.4)	(0.5)	(0.7)	0.4	0.4	0.4	—	—	—	(8.5)	(6.1)	(5.7)	50	(22.5)	2.7	
Reliance Communications	184	SELL	391,637	8,387	2,133	22.1	14.1	18.2	(30.2)	(36.2)	29.1	8.3	13.1	10.1	7.5	8.3	6.2	1.0	0.9	0.9	0.4	—	—	11.7	7.4	8.9	175	(4.7)	41.0	
Tata Communications	289	REDUCE	82,237	1,761	285	14.0	15.2	15.7	3.2	8.2	3.5	20.6	19.0	18.4	8.4	7.7	7.4	1.2	1.1	1.1	2.3	2.6	2.9	5.2	5.5	5.5	225	(22.0)	1.7	
<b>Telecom</b>		<b>Cautious</b>	<b>1,857,578</b>	<b>39,780</b>					<b>(15.1)</b>	<b>(19.8)</b>	<b>20.7</b>	<b>13.0</b>	<b>16.2</b>	<b>13.4</b>	<b>7.6</b>	<b>7.5</b>	<b>6.1</b>	<b>1.7</b>	<b>1.5</b>	<b>1.4</b>	<b>0.8</b>	<b>0.9</b>	<b>1.2</b>	<b>12.7</b>	<b>9.3</b>	<b>10.2</b>				
<b>Utilities</b>																														
Adani Power	127	ADD	276,315	5,917	2,180	0.8	4.9	16.4	—	524.1	235.3	161.8	25.9	7.7	125.5	17.2	6.2	5.0	4.2	2.7	—	—	—	4.4	17.7	42.8	130	2.6	3.0	
CESC	410	ADD	51,230	1,097	125	35.2	42.2	45.7	9.3	19.6	8.4	11.6	9.7	9.0	7.3	6.6	7.4	1.2	1.1	1.0	1.1	1.3	1.4	11.1	11.7	11.4	439	7.1	1.9	
Lanco Infratech	67	BUY	160,654	3,440	2,405	2.0	3.6	4.5	35.1	82.2	26.4	34.0	18.7	14.8	20.2	8.6	8.4	4.7	3.8	3.0	—	—	—	15.8	20.6	21.0	70	4.8	8.8	
NHPC	31	REDUCE	379,478	8,127	12,301	1.9	1.3	1.6	74.9	(27.2)	20.1	16.6	22.9	19.0	10.7	10.9	8.9	1.5	1.4	1.4	1.8	1.1	1.4	9.7	6.5	7.4	28	(9.2)	19.6	
NTPC	199	REDUCE	1,639,611	35,112	8,245	10.6	12.4	14.7	7.8	16.8	18.9	18.8	16.1	13.5	14.6	12.4	10.4	2.6	2.4	2.1	2.0	2.3	2.8	14.2	15.3	16.6	200	0.6	10.5	
Reliance Infrastructure	1,150	ADD	282,945	6,059	246	61.8	62.7	80.3	(1.5)	1.6	28.0	18.6	18.3	14.3	19.9	19.1	13.1	1.5	1.4	1.3	0.7	0.8	0.9	6.3	7.3	10.1	1,100	(4.3)	48.9	
Reliance Power	175	SELL	419,671	8,987	2,397	2.9	3.1	5.4	179.7	7.4	76.4	61.4	57.1	32.4	98.9	34.0	2.9	2.8	2.5	—	—	—	—	4.8	5.0	8.2	135	(22.9)	23.0	
Tata Power	1,342	ADD	331,252	7,094	247	60.2	69.2	88.5	20.1	15.0	27.8	22.3	19.4	15.2	13.9	12.6	10.8	2.5	2.3	2.1	0.9	1.0	1.1	12.9	12.5	14.3	1,420	5.8	10.6	
<b>Utilities</b>		<b>REDUCE</b>	<b>3,541,156</b>	<b>75,834</b>					<b>22.3</b>	<b>16.5</b>	<b>35.6</b>	<b>22.6</b>	<b>19.4</b>	<b>14.3</b>	<b>17.9</b>	<b>14.3</b>	<b>10.8</b>	<b>2.4</b>	<b>2.2</b>	<b>2.0</b>	<b>1.3</b>	<b>1.4</b>	<b>1.6</b>	<b>10.5</b>	<b>11.3</b>	<b>13.8</b>				
<b>Others</b>																														
Havells India	650	SELL	39,082	837	60	5.3	31.6	45.0	3.7	497.9	42.6	122.9	20.6	14.4	17.0	10.5	8.5	10.8	7.1	4.8	—	—	—	6.6	41.6	39.7	480	(26.1)	7.1	
Jaiprakash Associates	129	BUY	275,044	5,890	2,129	1.5	5.9	7.9	(27.2)	305.4	34.4	88.7	21.9	16.3	22.1	14.0	10.3	3.2	2.9	2.5	—	—	—	4.1	13.9	16.3	183	41.6	33.7	
Jindal Saw	201	ADD	59,255	1,269	294	27.5	19.3	17.9	121.9	(29.8)	(7.2)	7.3	10.4	11.3	5.3	6.0	5.8	1.5	1.3	1.2	—	—	—	20.5	12.9	11.1	243	20.6	4.7	
PSL	137	BUY	7,311	157	53	22.9	25.4	28.2	3.3	10.6	11.0	6.0	5.4	4.9	3.3	2.8	3.0	0.8	0.7	0.6	4.8	4.8	5.1	12.6	11.7	12.0	175	28.0	0.7	
Sintex	344	BUY	46,975	1,006	136	24.1	28.3	33.3	0.5	17.4	17.5	14.3	12.2	10.3	11.9	8.0	6.8	2.2	1.9	1.6	—	—	—	15.5	15.3	15.2	380	10.4	4.0	
Tata Chemicals	325	ADD	79,079	1,693	243	26.4	32.4	37.3	(27.1)	22.6	15.1	12.3	10.0	8.7	6.6	5.6	4.8	1.7	1.5	1.3	2.7	2.8	2.8	16.0	18.4	18.3	360	10.8	3.1	
Welspun Corp	244	REDUCE	50,124	1,073	205	25.1	23.0	24.4	44.9	(8.1)	5.8	9.7	10.6	10.0	5.4	5.5	4.9	1.7	1.5	1.3	0.8	0.8	0.9	20.6	14.8	13.5	245	0.4	6.3	
United Phosphorus	175	BUY	80,924	1,733	463	11.9	15.6	19.0	18.8	30.2	22.1	14.6	11.2	9.2	8.5	7.1	5.7	2.4	2.0	1.7	0.9	1.1	1.1	17.7</						

"Each of the analysts named below hereby certifies that, with respect to each subject company and its securities for which the analyst is responsible in this report, (1) all of the views expressed in this report accurately reflect his or her personal views about the subject companies and securities, and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report: Sanjeev Prasad, Kawaljeet Saluja, Manish Karwa, Manoj Menon, Nischint Chawathe."

**Kotak Institutional Equities Research coverage universe**

Distribution of ratings/investment banking relationships



Source: Kotak Institutional Equities

As of March 31, 2010

**Ratings and other definitions/identifiers**

**Definitions of ratings**

**BUY.** We expect this stock to outperform the BSE Sensex by 10% over the next 12 months.

**ADD.** We expect this stock to outperform the BSE Sensex by 0-10% over the next 12 months.

**REDUCE.** We expect this stock to underperform the BSE Sensex by 0-10% over the next 12 months.

**SELL.** We expect this stock to underperform the BSE Sensex by more than 10% over the next 12 months.

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

**Other definitions**

**Coverage view.** The coverage view represents each analyst’s overall fundamental outlook on the Sector. The coverage view will consist of one of the following designations: **Attractive, Neutral, Cautious.**

**Other ratings/identifiers**

**NR = Not Rated.** The investment rating and target price, if any, have been suspended temporarily. Such suspension is in compliance with applicable regulation(s) and/or Kotak Securities policies in circumstances when Kotak Securities or its affiliates is acting in an advisory capacity in a merger or strategic transaction involving this company and in certain other circumstances.

**CS = Coverage Suspended.** Kotak Securities has suspended coverage of this company.

**NC = Not Covered.** Kotak Securities does not cover this company.

**RS = Rating Suspended.** Kotak Securities Research has suspended the investment rating and price target, if any, for this stock, because there is not a sufficient fundamental basis for determining an investment rating or target. The previous investment rating and price target, if any, are no longer in effect for this stock and should not be relied upon.

**NA = Not Available or Not Applicable.** The information is not available for display or is not applicable.

**NM = Not Meaningful.** The information is not meaningful and is therefore excluded.

## Corporate Office

Kotak Securities Ltd.  
Bakhtawar, 1st Floor  
229, Nariman Point  
Mumbai 400 021, India  
Tel: +91-22-6634-1100

## Overseas Offices

Kotak Mahindra (UK) Ltd  
6th Floor, Portsoken House  
155-157 The Minories  
London EC 3N 1 LS  
Tel: +44-20-7977-6900 / 6940

Kotak Mahindra Inc  
50 Main Street, Suite No.310  
Westchester Financial Centre  
White Plains, New York 10606  
Tel:+1-914-997-6120

Copyright 2010 Kotak Institutional Equities (Kotak Securities Limited). All rights reserved.

1. Note that the research analysts contributing to this report may not be registered/qualified as research analysts with FINRA; and
2. Such research analysts may not be associated persons of Kotak Mahindra Inc and therefore, may not be subject to NASD Rule 2711 restrictions on communications with a subject company, public appearances and trading securities held by a research analyst account.

Kotak Securities Limited and its affiliates are a full-service, integrated investment banking, investment management, brokerage and financing group. We along with our affiliates are leading underwriter of securities and participants in virtually all securities trading markets in India. We and our affiliates have investment banking and other business relationships with a significant percentage of the companies covered by our Investment Research Department. Our research professionals provide important input into our investment banking and other business selection processes. Investors should assume that Kotak Securities Limited and/or its affiliates are seeking or will seek investment banking or other business from the company or companies that are the subject of this material and that the research professionals who were involved in preparing this material may participate in the solicitation of such business. Our research professionals are paid in part based on the profitability of Kotak Securities Limited, which include earnings from investment banking and other business. Kotak Securities Limited generally prohibits its analysts, persons reporting to analysts, and members of their households from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover. Additionally, Kotak Securities Limited generally prohibits its analysts and persons reporting to analysts from serving as an officer, director, or advisory board member of any companies that the analysts cover. Our salespeople, traders, and other professionals may provide oral or written market commentary or trading strategies to our clients that reflect opinions that are contrary to the opinions expressed herein, and our proprietary trading and investing businesses may make investment decisions that are inconsistent with the recommendations expressed herein. In reviewing these materials, you should be aware that any or all of the foregoing, among other things, may give rise to real or potential conflicts of interest. Additionally, other important information regarding our relationships with the company or companies that are the subject of this material is provided herein.

This material should not be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. We are not soliciting any action based on this material. It is for the general information of clients of Kotak Securities Limited. It does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients. Before acting on any advice or recommendation in this material, clients should consider whether it is suitable for their particular circumstances and, if necessary, seek professional advice. The price and value of the investments referred to in this material and the income from them may go down as well as up, and investors may realize losses on any investments. Past performance is not a guide for future performance, future returns are not guaranteed and a loss of original capital may occur. Kotak Securities Limited does not provide tax advice to its clients, and all investors are strongly advised to consult with their tax advisers regarding any potential investment.

Certain transactions -including those involving futures, options, and other derivatives as well as non-investment-grade securities - give rise to substantial risk and are not suitable for all investors. The material is based on information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied on as such. Opinions expressed are our current opinions as of the date appearing on this material only. We endeavor to update on a reasonable basis the information discussed in this material, but regulatory, compliance, or other reasons may prevent us from doing so. We and our affiliates, officers, directors, and employees, including persons involved in the preparation or issuance of this material, may from time to time have "long" or "short" positions in, act as principal in, and buy or sell the securities or derivatives thereof of companies mentioned herein. For the purpose of calculating whether Kotak Securities Limited and its affiliates holds beneficially owns or controls, including the right to vote for directors, 1% of more of the equity shares of the subject issuer of a research report, the holdings does not include accounts managed by Kotak Mahindra Mutual Fund. Kotak Securities Limited and its non US affiliates may, to the extent permissible under applicable laws, have acted on or used this research to the extent that it relates to non US issuers, prior to or immediately following its publication. Foreign currency denominated securities are subject to fluctuations in exchange rates that could have an adverse effect on the value or price of or income derived from the investment. In addition, investors in securities such as ADRs, the value of which are influenced by foreign currencies affectively assume currency risk. In addition options involve risks and are not suitable for all investors. Please ensure that you have read and understood the current derivatives risk disclosure document before entering into any derivative transactions.

This report has not been prepared by Kotak Mahindra Inc. (KMInc). However KMInc has reviewed the report and, in so far as it includes current or historical information, it is believed to be reliable, although its accuracy and completeness cannot be guaranteed. Any reference to Kotak Securities Limited shall also be deemed to mean and include Kotak Mahindra Inc.