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Inside

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DLF curtain raiser

DLF (Mach II) at a glance

We take a detailed look at DLF, prior to its proposed IPO of ~10% of the company (~US$1.9bn). The overall story is becoming well known – DLF is one of the leading real estate developers in India, with a land bank of 10,225 acres and a saleable area of 574m sqf. Founded in 1946, it has the distinction of being the largest real estate company in India on a completed projects basis and has developed a 3,000-acre township in Gurgaon called DLF City.

Key changes with DLF (Mach I)

There are substantial changes in the newly filed prospectus relative to DLF's previously filed prospectus of May 2006. Among the notable changes: both land bank and debt levels have doubled and there are no land valuations in the offer document (unlike May 2006, when 220m sqf was valued at US$19.2bn). The macroenvironment has also undergone a change; equity markets have increased by 15%, interest rates by 150bp and property prices by ~30–40%. We examine the differences in detail.

DLF makes Unitech appear cheap

Unitech (UT IN, Rs384, OP, TP, Rs501) is trading at almost one-third of DLF's expected valuation of US$19bn, even though the size of the land bank is similar. Clearly size isn't everything, but applying to Unitech the multiple of EV/per sqf of land bank that DLF is looking at, we derive a Unitech share price of Rs976. If we apply a discount of 30% to Unitech based on its arguably inferior land bank quality, we arrive at a share price of Rs683. This implies upside of ~90% from current levels. It is also worth highlighting that these valuations do not include SEZ development plans for either company.

DLF – What we like… and what we think is risky

We like DLF for its larger geographical presence (in 31 cities) and for its land bank in the high-priced locations of Mumbai and New Delhi, though very small. We think the new, recently-announced JVs are strategic for its execution capabilities – Hilton for its hotel business and Laing O'Rourke for infrastructure.

What we think is risky: DLF development plans for next three years are aggressive and we think its product mix is not in sync with overall market demand. DLF focuses more on relatively smaller commercial and retail markets instead of the larger residential segment. Even in residential, DLF focuses only on super luxury apartments which have a small market. Also, ownership of 200m sqf of total saleable area is not very clear. Finally, with 50% of the total land bank in Gurgaon, DLF becomes susceptible to any adverse development in Gurgaon.

Top 10 questions to ask

We read between the lines and frame key questions about the company, including: How has DLF's land bank doubled in the eight months from May 2006 to Jan 2007? How much time does DLF estimate it will require developing nearly 5,000 acres of land bank in Gurgaon? At what rate and for what consideration has DLF sold its commercial assets to DLF Assets Private Ltd (DAL)?

DLF (Mach II) at a glance

DLF is likely to be valued at ~US$19bn with saleable area of 574m sqf

DLF is the largest real estate company in India on a completed projects basis. DLF, founded in 1946 has developed approximately 220m sqf, including 195m sqf of plots, 17m sqf of residential properties (such as villas and apartments), 6m sqf of commercial properties and 2m sqf of retail properties. DLF has so far focussed its development in Delhi and Gurgaon. DLF has developed 22 urban colonies as well as a 3,000-acre township in Gurgaon by the name of DLF City.

Fig 1 DLF key metrics

Bloomberg code	Expected timing	Tot. land bank (m sqf)	Estimated mkt cap. (US$m)	Asset value (US$m)	Current debt (US$m)	Gearing ratio* (%)	EV/sqf of landbank (US$)	Land cost to be paid (US$m)
DLFU IN	TBC	574	19,200	1,238.2	2,132.1	323%	37.16	1,251

* Net debt to historical equity (essentially historical book value)
Source:DLF prospectus filed in Jan-07, Macquarie Research, March 2007.

DLF is the largest real estate company in India on a completed projects basis

Presently, DLF is involved in all three business segments of residential, commercial and retail. For residential development, DLF follows a ‘build and sell’ model, however, for commercial development, it follows a ‘builds and sell or lease’ model and for retail development, it follows a ‘build and lease model’. Going forward, the company is looking to expand/diversify into related real estate business, such as infrastructure (JV with Laing O’Rourke), development of Special Economic Zones (SEZ), multiplex cinema (DT cinemas) and hotel businesses (JV with Hilton).

A look at the DLF land bank

- DLF has one of the largest land banks among all of the developers in India. It has land bank of 10,255 acres, resulting in developable area of approximately 574m sqf, of which 46m sqf is already under construction.

Fig 2 DLF and Unitech are the two largest players among Indian developers

	Land size (acres)
DLF (as per prospectus filed in Jan 2007)	**10,255**
Unitech	10,332
Sobha Developers	6,059
Ansal properties	5,924
Mahindra Gesco	1,637

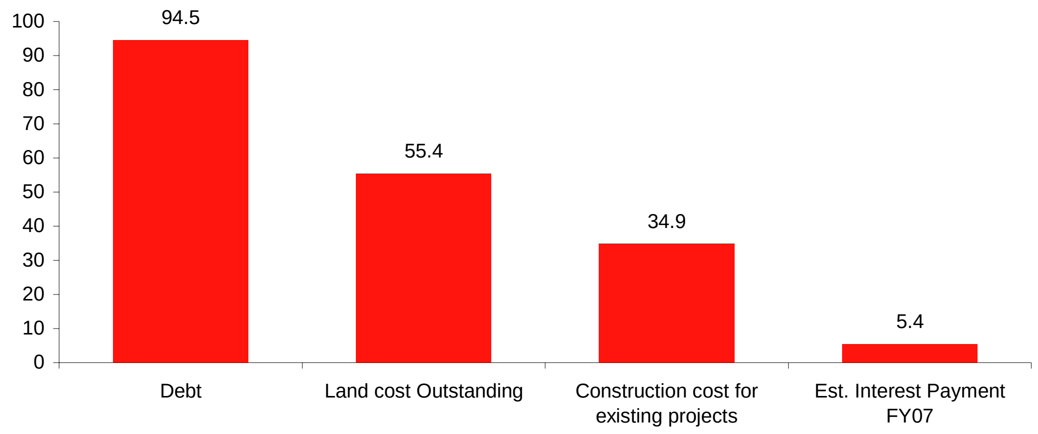
Source: DLF prospectus filed in Jan-07, Company reports, Macquarie Research, March 2007

Land cost and current debt levels

Total debt is Rs94.5bn and outstanding land cost is Rs55.4bn

- DLF has a total debt of Rs94.5bn and an outstanding amount of Rs55.4bn towards land cost. Of the total debt of Rs94.5bn, 75% is on a floating rate basis which is a risk in a rising interest rate environment. DLF had capitalised Rs1.1bn out of the total interest charge of Rs2.8bn for FY06. We estimate the interest charge for FY07 would be Rs5.4bn, on a conservative basis, as interest rates have gone up by roughly 150bp in the last nine months.

Fig 3 Significant debt and land cost outstanding (Rs bn)



Source: DLF prospectus filed in Jan-07, Macquarie Research, February 2007

A quick snapshot on area developed, under construction and planned

Current development in progress is 46m sqf and 150m sq is planned between FY07–09F

- A total of 10,255 acres translates into 574m sqf of saleable area. The total 574m sqf involves the development of plots of 46m sqf, residential apartments of 377m sqf, commercial development of 88m sqf and retail development of 56m sqf. DLF is of the opinion that its present land bank is sufficient for the next 10–11 years.
- Out of 574m sqf, DLF has a total of 46m sqf under development as of 30 November 2006, with 9m sqf under residential; 26m sqf under commercial and 11m sqf under retail development.

Fig 4 Snapshot of DLF past and future development plans

Development	Completed (m sqf)	In progress (m sqf)	Planned (m sqf)	Plan for FY07-09 (m sqf)
Plots	195	-	46	-
Residential	17	9	375	69.8
Commercial	6	26	62	48.2
Retail	2	11	45	31.7
Total	**220**	**46**	**528**	**149.7**

Source: DLF prospectus, Macquarie Research, February 2007

Key changes with DLF (Mach 1)

In this section, we list the key changes between the two prospectuses that have been filed by DLF – DLF (Mach 1), filed in May 2006 and DLF (Mach 2) filed in January 2007.

Key changes in prospectus

Both land bank and debt have doubled since the previous prospectus of May 2006

- **Land bank has more than doubled**: DLF has disclosed a land bank of 10,255 acres in the January 2007 prospectus, more than double the land bank declared in its first filing. DLF had declared 4,265 acres as per the original offer document filed in May 2006. The developable area has now been increased to 574 million square feet as against 220m sqf declared in the original offer document filed in May 2006.
- **Outstanding land cost and debt has also doubled**: DLF had a Rs28.7bn outstanding obligation towards the acquisition of land as per its filing in May 2006, which has now almost doubled to Rs55.4bn. DLF debt has also more than doubled in the interim period, from Rs41.3bn in FY06 to Rs94.5bn as of 30 November 2006.

No land valuations this time, unlike the last time when valuation was US$19.2bn for 220m sqf

- **No land valuation in offer document unlike last time**: Notably unlike last time, the current offer document is silent on the valuation of the land bank. In the document filed in May, DLF had published valuations made by Cushman & Wakefield valuing DLF between US$17.4–19.2bn and by Jones Lang LaSalle of US$19.2bn for 4,265 acres.
- **Size of the issue is reduced**: The size of the issue has been reduced to 175m shares (from 202m shares of Rs2 each earlier). An offer for sale by the promoter and promoter group has now been withdrawn, although that alone is not the reason for the smaller issue size. Further, there is no mention of any green shoe option now. Pricing is still unknown.
- **Post-issue shareholding of promoter group is reduced**: Post-issue, the holding of promoter group would be reduced to 87.49%. The existing paid-up capital increased in the interim period due to conversion of debentures and consequent bonus issue being part of the recent settlement with debenture-holders. This settlement of debenture holders is the same issue which acted as a hurdle when DLF was planning to come to market in May 2006.
- **More clarity on SEZ**: The recent prospectus throws more clarity on DLF's plans for development of special economic zones in Gurgaon, Chennai, Pune and Amritsar. DLF has plans for four large SEZs, covering a total of 26,100 acres. The details of all the SEZ plans are outlined in the table below:

Fig 5 SEZ development plans

SEZ	Area (Acres)	Development Status
Amritsar Multi-sector SEZ	1,100	Land acquisition notifications issued
Ludhiana Multi-product SEZ	2,500	In principal approval obtained
Gurgaon SEZ	20,000	Approval from Haryana Investment Promotion Board
Ambala SEZ	2,500	Approval from Haryana Investment Promotion Board

Source: DLF prospectus, Macquarie Research, February 2007

New JVs with Hilton, Laing O'Rourke plc for infrastructure business

- **New JVs and business added**: According to the latest document, DLF has formed a new joint venture with US-based hospitality company Hilton for a few of its hotels. DLF has also announced the expansion of operations in multiplex cinemas, ie, DT cinemas are planned for its retail outlets. Finally, a foray into possible wind power business was also announced in the January 2007 prospectus.
- **Significant improvement in business income:** DLF has reported in the new prospectus net profit of Rs18.3bn for the eight months ended November 2006, versus Rs11.5bn for FY06. This is mainly due to the one-time sale of commercial assets from DLF to DLF Assets Ltd. (DAL – Promoter Group Company) which accounted for Rs21.6bn and Rs17.4bn in revenue and profit before tax, respectively.

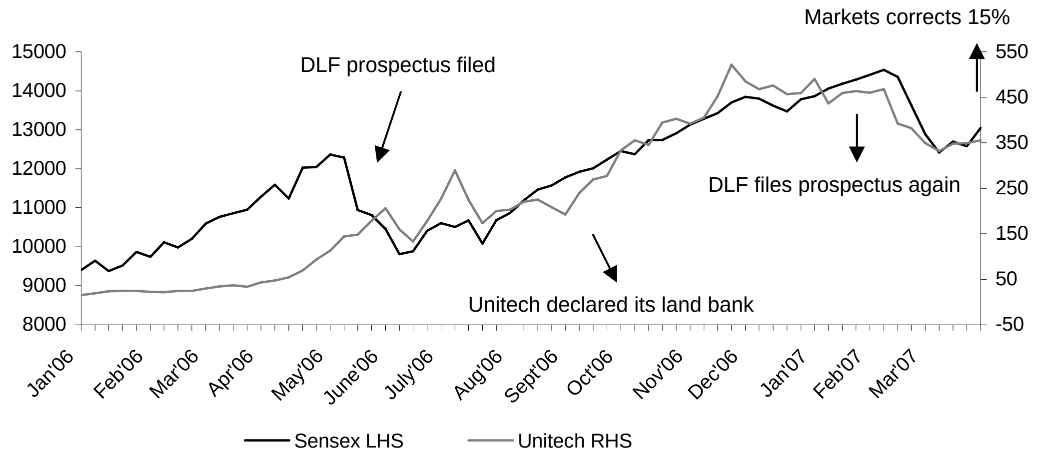
Macro environment has also undergone a change in the interim period

- Equity markets (Sensex) have risen by 15% since May 2006: Last May, post the filing of the prospectus by DLF the there was a correction in broad markets correcting by almost 30% in a month. By contrast this time, the markets were stable until early February but since then they have corrected by 15%.

Equity markets have increased 15% in the interim period despite correcting twice

The story with property stocks is no different; they corrected by roughly 55–60% in May 2006, versus a 30–35% correction in Feb 2007. Unitech, however, is one exception – it did not fall in the May 2006 correction and has declined by 30% this time around.

Fig 6 Sensex has risen by 15% between May 2006 and now, while Unitech has increased 3x

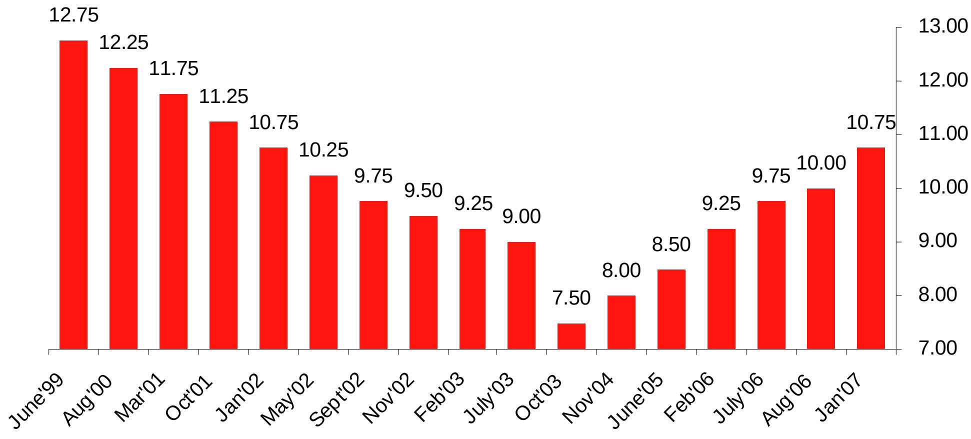


Source: Bloomberg, Macquarie Research, March 2007

Unitech has also increased 3x since the revelation of land bank details in September 2006

- Unitech's Valuation in the interim period has increased three times: The only direct comparable to DLF in the listed space is Unitech, and it is interesting to note that since May 2006, Unitech's valuation has increased 3x to US$7bn, touching a high of $9.8bn on 23 November 2006. This huge run-up was mainly on the back of details revealed by the company of its 10,334-acre land bank in September 2006. This takes us to the next section – DLF vs Unitech, which is a very interesting and increasingly sought-after comparison.
- Interest rates have also increased by roughly 150bp in the interim period: The mortgage rates have increased by 150bp, mainly due to tightening of liquidity by the Central Government. This, along with the run up in property prices, has decreased the transaction volume in the last three months. This is likely to dampen the residential demand and could affect the overall real estate market. The increase in interest rate affects DLF in two ways, first by dampening the prospects of new customers for residential development and second by increasing the interest liability of the company due to the huge floating rate debt of Rs 70.8bn.

Fig 7 Mortgage rates...rising again



Source: HDFC, Macquarie Research, February 2007

Property market has also increased by 30–40%

- The property market in India has appreciated by 30–40%: The last month has not been particularly good for Indian property stocks, yet the same weakness has not been reflected in the physical market. However, transaction volumes are witnessing a decline on the back of an interest-rate increase and appreciation in property prices. The property prices in general have increased by 30–40% since DLF last filed its prospectus. The Indian property story in May 2006 was nascent as compared to today and in the interim period approximately US$11bn of foreign capital has been garnered for the Indian property sector.

DLF makes Unitech appear cheap…

Unitech trades at one-third the valuation for same key metrics

In this section, we compare DLF and Unitech. We conclude from the following analysis that DLF, in its current proposed form, makes Unitech look attractive at today's market pricing.

Fig 8 Snapshot comparison between DLF and Unitech

	Bloomberg code	Total land bank (m sqf)	Market cap. (US$m)	Asset value (US$m)	Current debt (US$m)	Gearing ratio (%)	EV/sqf of landbank (US$)	Land cost to be paid (US$m)
DLF	DLFU IN	574	19,200	1,238	2,132	323%	37.16	1,251
Unitech	UT IN	500	6,724	1,015.0	693.3	317%	14.83	903

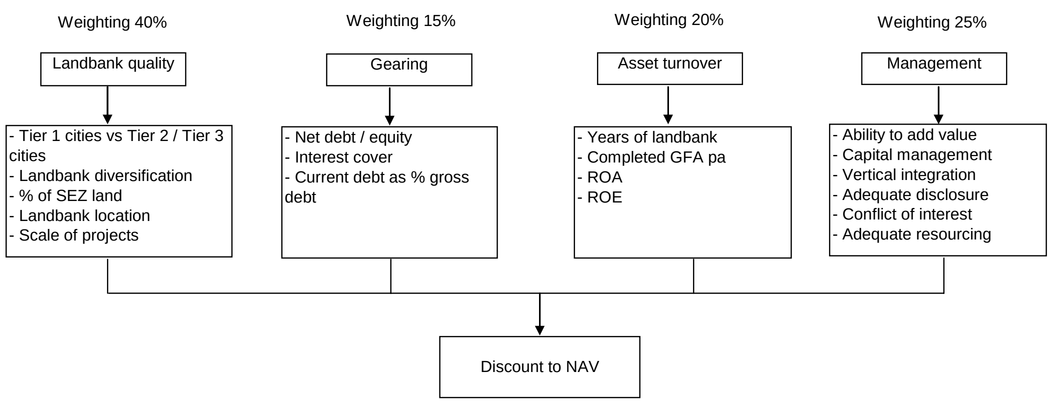
Source: DLF prospectus, Company data, Macquarie Research, March 2007

Macquarie DiNAV Model (India) – effective tool to evaluate property companies

We have identified the Macquarie DiNAV model (India) as an effective tool for comparison between the two largest property developers in India. Regionally, we also use the model (with different weightings for different countries) for relative evaluation of property developers. The Macquarie DiNAV Model utilises key factors that are important to the success of a property developer, utilising weightings on every factor. We think these characteristics are common across the region, it is just that the weighting that varies.

Macquarie DiNAV model used for relative evaluation of DLF and Unitech

Fig 9 Macquarie DiNAV Model (India) – effective tool to evaluate property companies



Source: Macquarie Research, March 2007

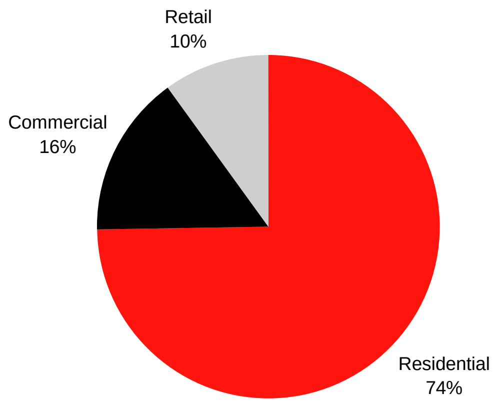
Land bank quality (40%)

We would spend most of the discussion comparing the land bank of DLF and Unitech. This is the most important factor, as property is about 'location, location, location'. If the location is good and the land bank has been substantially acquired at prices well below current levels, developments may see a very good response even if all the other qualities are substandard.

Size is similar with DLF having 15% more saleable area at 574m sqf

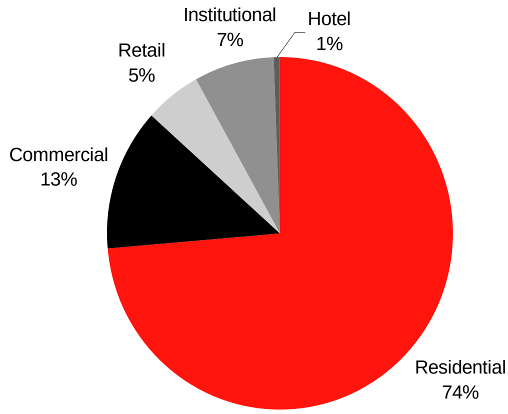
1. **Size of land bank and nature of development are similar:** Both DLF and Unitech have land bank of similar size, at roughly 10,000+ acres. DLF has 15% more saleable area at 574m sqf, as compared to Unitech at 500m sqf. Both of the companies are expected to take 10–11 years to exhaust their present land bank. Their total land development plans are very similar, with 74% of development focussed towards the residential segment. The commercial segment comes next and is then followed by retail, but DLF has larger plans for retail as compared to Unitech.

Fig 10 DLF development plan for total 574m sqf



Source: DLF prospectus, Macquarie Research, February 2007

Fig 11 Unitech development plan for total 500m sqf



Source: Unitech data, Macquarie Research, February 2007

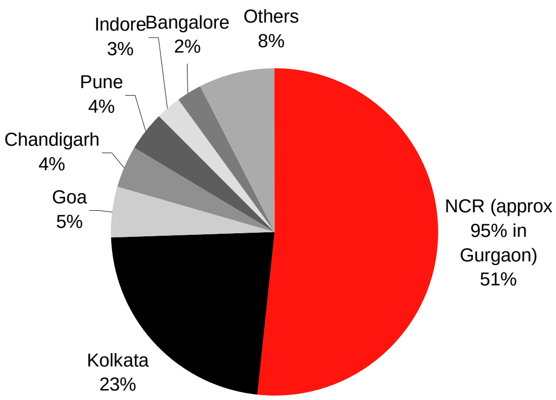
2. **Unitech has better land bank diversification:** In terms of diversification, we think Unitech's land bank is better diversified as compared to DLF, as can be seen from figures 13 and 14. DLF's total land bank of 10,225 acres is highly skewed in favour of Gurgaon and to some extent Kolkata, too. DLF has approximately 72% of its total land bank in Gurgaon (49%) and in Kolkata (23%). By comparison, Unitech's land bank is better diversified with presence across the country, except for western India. Even within the NCR region it is well diversified between Gurgaon, Noida and Greater Noida.

We think Unitech has better land bank diversification. DLF has high exposure to Gurgaon at 5,000 acres

We think DLF has a large concentration of 5,000 acres in Gurgaon, given that it has a 3,000-acre satellite town that took DLF almost 30 years to develop (DLF City). We estimate that it would not take proportionate time to develop 5,000 acres, yet a 10-year horizon is also a very aggressive estimate for such a large land mass in a single satellite township. As a result of 49% of the total land bank in Gurgaon, DLF becomes susceptible to any adverse developments in Gurgaon, such as a change in land use regulations, zoning laws, taxes, natural calamity or any social or political development that depresses the real estate sentiment in Gurgaon.

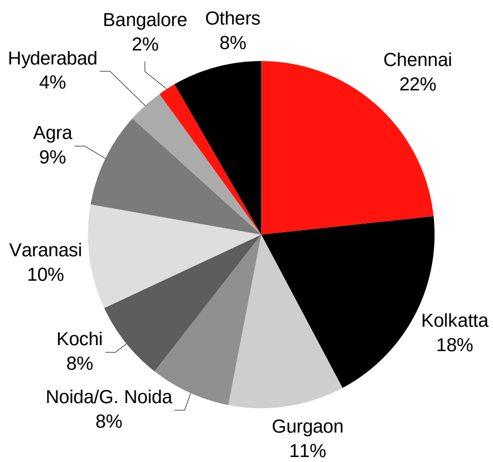
We also recognise that the presence of DLF in 31 cities is positive as compared to Unitech which is present in half as many cities. Although the presence is small in many cities, it will not require much effort on the part of DLF to make in-roads in these cities.

Fig 12 DLF – breakdown of total 10,225 acres – by city



Source: DLF Prospectus, Macquarie Research, February 2007

Fig 13 Unitech – breakdown of total 10,500 acres – by city



Source: Unitech data, Macquarie Research, February 2007

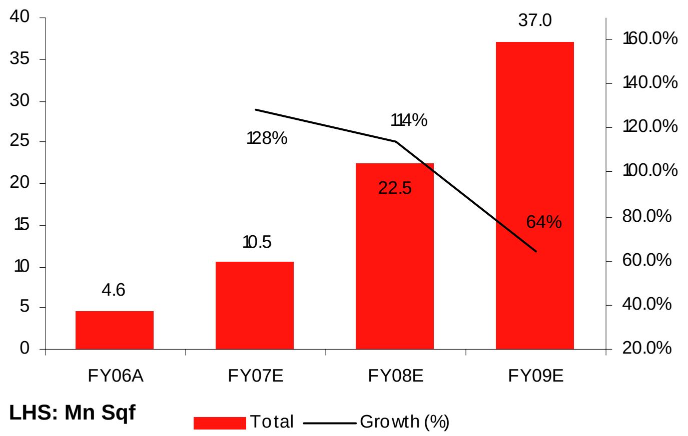
3. **DLF has a better quality of land bank but not significantly better**: About of 30% of Unitech's land bank is very similar to DLF's. 18% is in Gurgaon where both companies' landholdings are in areas with comparable selling price. 11% is in Kolkata where both companies share the same parcel of land ie the Dankuni project. One difference worth highlighting is DLF's 22 acres of land in Mumbai, which is certainly the one of the most profitable landholdings but only forms a very small part of DLF's total landholdings. Also DLF has paid a reasonable price for this land which is close to Rs 400m/acre.

Although DLF has a land bank of better quality, it is not significantly better

The main difference between the two companies' land banks lies in the last 40% distribution. DLF holds all of this in Gurgaon, whereas Unitech holds 22% in Chennai, 10% in Varanasi and 9% in Agra. We believe this could work both in favour and against DLF relative to Unitech. It could work in DLF's favour as Gurgaon presently is more urban than Chennai, Varanasi and Agra. It could act against DLF as the company might find the absorption of such a large land mass in a single city difficult.

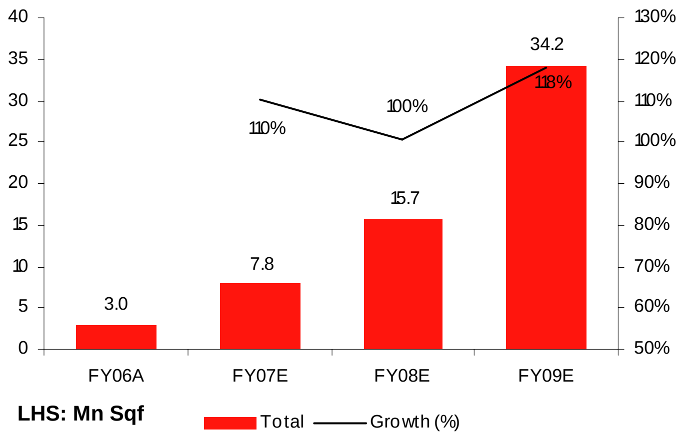
4. **DLF's forecast delivery schedule between FY07–09 is 21% higher than our forecasts for Unitech**: Details provided in the new DLF prospectus indicate the 150m sqf is proposed to be made available for sale or lease between FY07–09. We estimate that DLF will deliver 70m sqf of saleable area between FY07–09. This estimate of 70m sqf is 21% more than Unitech's forecast delivery of 58m sqf during the same period. The plans for both companies are little aggressive and to that extent there remains execution risk. We find Unitech's forecasts slightly more comforting as we estimate it has delivered 5.5–6m sqf in first nine months of FY07. However we have no such data available for DLF and hence cannot comment much on DLF's progress on its forecast delivery schedule.

Fig 14 DLF forecast schedule of 70m sqf – FY07–09



Source: Macquarie Research, March 2007

Fig 15 UT forecast schedule of 58m sqf – FY07–09

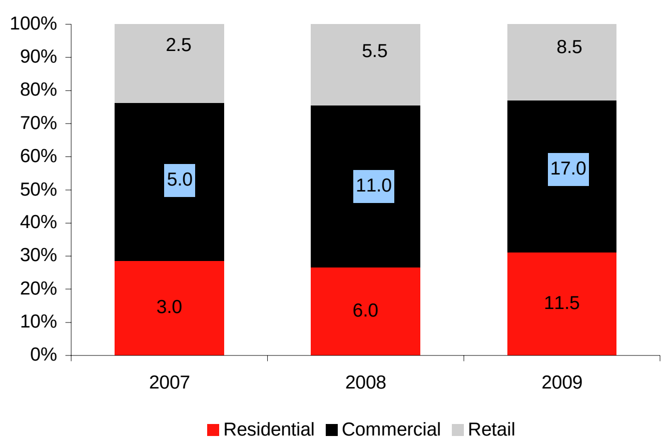


Source: Macquarie Research, March 2007

We feel Unitech's product mix is better than DLF's

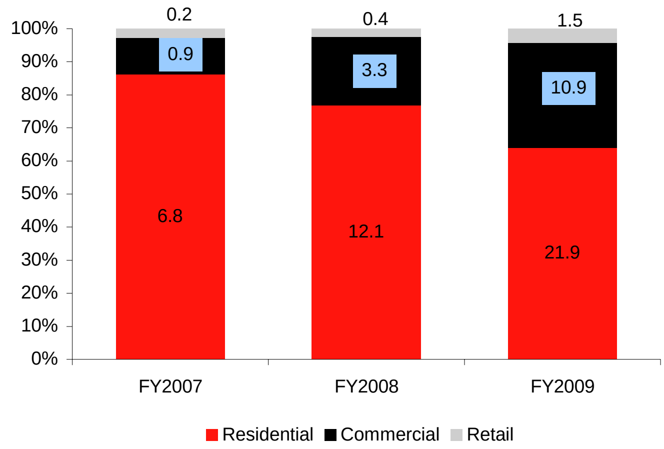
5. **Unitech's product mix is better between FY07–09:** Based on details provided in the new DLF prospectus regarding product mix of 150m sqf of saleable area between FY07–09, we think DLF will focus more on the commercial and retail segments (together 53%). In comparison, Unitech will focus more on the residential segment (71%), which is in line with overall Indian real estate demand. Industry reports suggest the total real estate demand for the commercial and retail segments cumulatively would be at best 400m sqf, implying that DLF aims to capture 12.5% of the total commercial and retail real estate demand. In our view 12.5% market share is very optimistic considering real estate in India is still a very fragmented market.

Fig 16 DLF forecast product mix FY07–09



Source: DLF prospectus, Macquarie Research, March 2007

Fig 17 UT forecast product mix FY07–09



Source: Macquarie Research, March 2007

DLF focuses more on super luxury apartments, which has low absorption

6. **Unitech's residential products have better absorption than DLF products**: Not only is DLF focusing less on residential in the short term, but it is also offering only high-end residential apartments. A closer look at DLF's residential offering tells us that the minimum price for a unit is US$400,000 (Rs 17.5m) and goes up to US$1m (Rs 44.1m). DLF focuses on development of luxury residential accommodation and is offering theme-based projects such as The Magnolias development in DLF city, which includes a golf course. All of DLF's below-mentioned projects were started in 2006 and we estimate the company has still not been able to sell 50% of total 1,754 apartments. The absorption for such high end luxury products in the market of Gurgaon is limited and we think DLF will find it difficult to sell these apartments.

Fig 18 Snapshot of DLF and Unitech current residential projects in Gurgaon

Project name	No. of Units	Avg unit Size (sqf)	Scheduled Completion	Avg. Sale Value (Rs/ sqf)*
DLF				
DLF Park Place	988	2,250	2010	6,567
The Belaire	364	3,600	2010	7,407
The Magnolias	402	6,200	2009	5,898
*** Sales in progress**				
Unitech				
Unitech Escape	400	2,000	2010	4,500
Unitech Harmony	340	2,600	2010	4,500
The Close - North	660	2,400	2008	3,000
Unitech Fresco	798	1,700	2009	3,750

Note: DLF prospectus filed in January 2007.

Source: DLF prospectus, Unitech data, Macquarie Research, March 2007

In contrast Unitech caters to middle to high end consumers for their residential products. Unitech's product range is very competitive in terms of size, facilities, location and is priced reasonably in comparison to DLF, thereby targeting a relatively larger customer base. We feel absorption of such products is better especially at a time when property prices have run up significantly and interest rates are also rising.

Both DLF and Unitech have similar SEZ plans

7. **SEZ plans are very much comparable**: DLF and Unitech have similar SEZ plans both in terms of size and location except for Unitech's New Kolkata Development Project. We do not see much difference between the ability of two players to execute these SEZ plans. Unitech is partnering with Salim group of Indonesia in Kolkata project; Salim group has established itself as credible player in Public Private Partnership (PPP) format in Indonesia.

Fig 19 SEZ development plans

SEZ	Area (Acres)	Status
DLF		
Amritsar Multi-sector SEZ	1,100	Land acquisition notifications issued
Ludhiana Multi-product SEZ	2,500	In principal approval obtained
Gurgaon SEZ	20,000	Approval from Haryana Investment Promotion Board
Ambala SEZ	2,500	Approval from Haryana Investment Promotion Board
Unitech		
New Kolkata Dev Project (SEZ portion)	22,500	UT share is 40%, Land acquisition notifications issued
Kundli Multi-sector SEZ	10,000	In principal approval obtained
Gurgaon Auto component SEZ	250	In principal approval obtained
Gurgaon Apparel SEZ	250	In principal approval obtained

Source: DLF and Unitech company data, Macquarie Research, March 2007

Management (25%)

Our assessment of management takes into account factors such as ability to add value, management of capital, conflict of interest, vertical integration of the business and adequate resources for business operations. Adequate disclosure is also a crucial component recently lacking in India's property market.

Broadly speaking, management of both companies lie in the Tier-1 category

Broadly speaking, management of both companies falls into the Tier-1 category, especially considering other real estate players in India. We believe DLF's edge over Unitech lies in its execution capabilities and resources for business operations, mainly because it has more experience in the industry and larger area developed to date.

However on factors such as conflict of interest and management of capital we rate Unitech a shade above DLF, recognising better capital management by Unitech through AIM listing and poor management of conflict by DLF, evidenced by its minority shareholder debenture conversion issue.

Asset turnover (20%)

Rapid asset turnover minimises the impact of market changes and recycles cash faster. Asset turnover is determined by the years of land bank, completed GFA pa, FY07 ROA and ROE.

Both DLF's and Unitech's existing land bank is sufficient for the next 10 years. This is a long time relative to the industry average. We view this as a positive as it indicates that both companies have enough capability to scale up their production according to demand for a longer period of time.

DLF has a better ROA and Unitech a better ROE

For the FY06 DLF's ROA of 6% is better than Unitech's ROA of 3.4% on account of better margin products from DLF. However Unitech's ROE of 58.7% is better than DLF's ROE of 22.5% because of its lower equity as proportion of total assets. Further, we expect these ratios to undergo significant improvement in FY07 for both DLF and Unitech.

Fig 20 Snapshot of key financial metrics

FY06	DLF	Unitech
ROA	6.1%	3.4%
ROE	22.5%	58.7%
PAT (Rs m)	1,917	846
Avg. total Assets for FY06 (Rs m)	48,467	33,610
Avg. net-worth for FY06 (Rs m)	8,535	1,442
Total Assets to Equity (x)	5.7	23.3

Source: DLF prospectus, Macquarie Research, March 2007

Gearing (15%)

Gearing is high for both DLF and Unitech but interest coverage ratio is comfortable

In valuations for property companies where the cost of debt is lower than the cost of equity, DCF valuations generally suggest that the higher the gearing, the lower the discount rate used in valuations. This may overlook stretched balance sheets, low interest coverage or short loan maturity, which may have an impact on the sentiment of companies when markets are difficult. We have adopted information from the latest annual results of each company for the comparison.

As at the end of FY06, DLF has a high gearing of 414%, compared to Unitech at 248% (we note though that the underlying asset bases of both have not been revalued, so these gearing levels are not as bad as they seem). However, Unitech's short-term debt is larger than DLF's, hence DLF's gearing is better than Unitech's. Both the companies enjoy a similar interest cover ratio of 4x, signifying a better interest servicing capability. A high gearing level is very typical of a developer's financial profile, especially in a developing market where all the property companies are looking to increase their operations many times over. In terms of cost and easy availability of debt, both DLF and Unitech are better placed in comparison to their peers on the back of their larger size, long track records and brand names.

Implications for Unitech

DLF makes Unitech look cheap…

Applying a multiple similar to DLF's and a further 30% discount, Unitech should trade at Rs683/share

We think DLF certainly makes Unitech look cheaper as Unitech is trading at almost one-third of DLF's expected valuations of US$19bn. Having compared Unitech and DLF above we can confidently conclude that the companies are close competitors both in terms of size and quality of land bank.

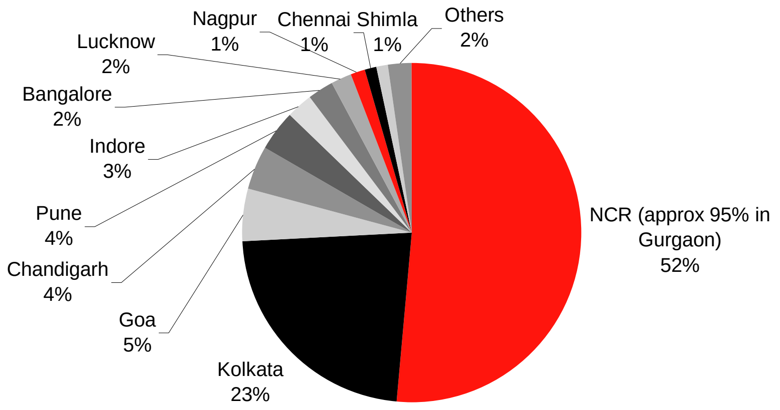
Applying the multiple of EV/per sqf of land bank that DLF is looking at and Unitech's share price of Rs 976/share and if we further apply a discount of 30% to Unitech on account of its arguably inferior land bank quality, indicates a share price of Rs683/share. This implies upside of approx. 90%. It is also worth highlighting that these valuations do not contain any valuation for SEZ plans for the companies.

DLF – What we like

DLF presence in 31 cities is a definite advantage

1. **Presence in larger number of cities**: DLF presently has its land bank in 31 different cities, though with a small presence (less than 100 acres) in 20 of these. In addition to the 574m sqf land bank, DLF has 23 super luxury/luxury hotel sites, a golf course and clubs. We think even a small presence in larger number of cities would help DLF make in-roads in those cities without much effort.

Fig 21 Presence in a large number of cities…

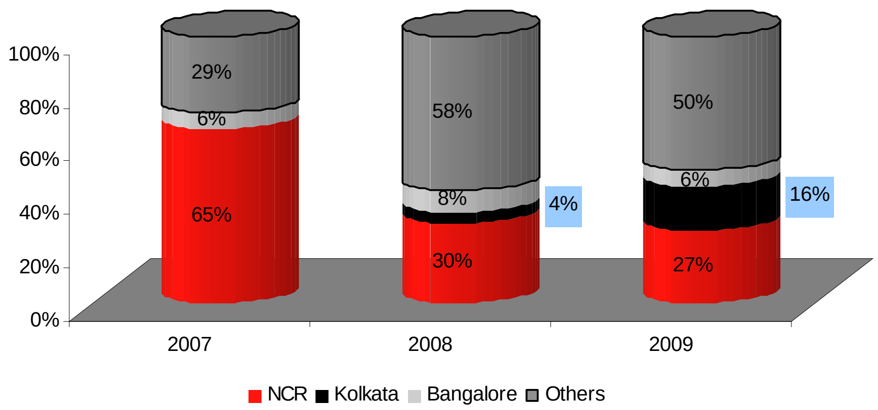


Source: DLF prospectus, Macquarie Research, March 2007

Focusing on favourable locations for FY07–09 development

2. **Favourable locations targeted for FY07–09 development:** DLF's next three years of development mainly focus on NCR (mainly Gurgaon), Kolkata and Bangalore. These are high margin locations where significant commercial, retail and residential demand is expected. We think DLF has timely positioned itself in these markets to reap the benefits of supply demand mismatch for next three years.

Fig 22 City wise DLF devlopmental plan FY07–09



Source: DLF prospectus, Macquarie Research, March 2007

Though small, DLF's presence in New Delhi and Mumbai is positive

3. **DLF's land bank includes one of the most prime locations in Mumbai and New Delhi**: DLF has 23 acres of land in one of the most expensive localities in New Delhi, aggregating to nearly 1.5m sqf of saleable area. DLF plans to develop this land bank for super luxury apartments and hence would be able to register high margins on this project. Similarly DLF has total of 22 acres in Mumbai including 17.5 acres acquired in 2006 in NTC mills in Mumbai at a cost of Rs 400m/acre. The Mumbai land bank is also located in Central Mumbai in a high priced location. DLF plans to utilise the majority of Mumbai land bank for high end retail development and would be able to attract high rentals from this development.

Joint ventures will help in better execution of projects

4. **Joint ventures with strategic partners:** DLF has struck JVs with strategic partners for its infrastructure and hotel business. It has also bought a stake in a leading firm in management consulting for its infrastructure, SEZ and townships. We recognise this as positive as execution is one of the main risks with all the Indian developers, so partnering with experienced players would reduce the execution risk to some extent.

⇒ **JV with Laing O'Rourke plc for infrastructure business**: DLF has recently entered into a joint venture with Laing O'Rourke plc, which is a leading UK-based construction company to expand its operations in infrastructure development. The joint venture has already commenced construction on 11 projects covering 20.4 million square feet and had an order-book of Rs39 billion. The JV will work on DLF's development projects such as the Magnolias, the Belaire and participate in infrastructure projects including roads, bridges, tunnels, pipelines, harbours, runways and power projects.

⇒ **JV with Hilton for hotel business**: DLF recently entered into joint venture with Hilton, to set up operations in hotel segment and serviced apartments in India. DLF is looking to enter into joint ventures with other hotel companies to develop hotels in the budget, business, four star, five star and deluxe segments.

⇒ **Purchased equity stake of 19% in Feedback Ventures**: Feedback Ventures is in business of providing consulting, engineering, project management and project development services for infrastructure projects in India. DLF is looking to obtain management consulting services from the company. DLF also intends to benefit from Feedback Ventures' experience by streamlining their planning and execution capabilities, particularly in relation to our infrastructure, SEZs and townships.

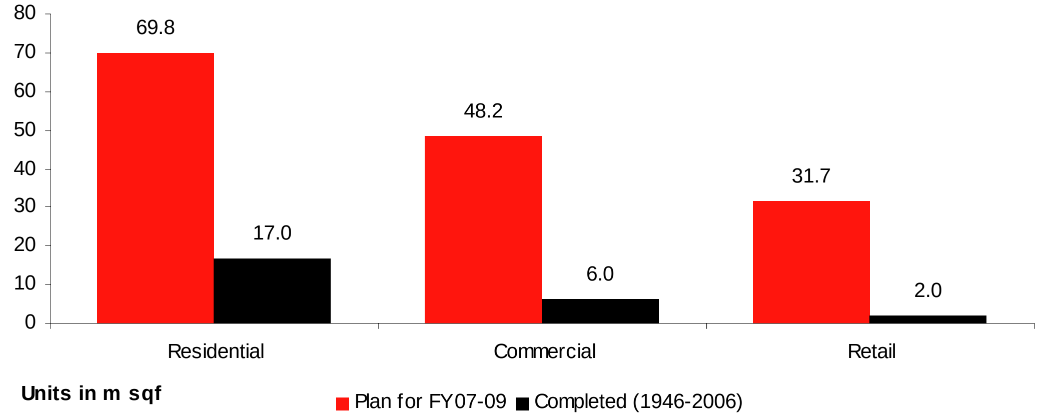
⇒ Additionally DLF has recently signed a memorandum of understanding with Nakheel LLC, United Arab Emirates to develop, through a joint venture, two townships in India, each spread over an area of approximately 20,000 acres.

DLF – what we think is risky

We think estimates of 150m sqf in FY07–09 are aggressive

- **Aggressive forecast development guidance**: DLF estimates it will be able to make available 150m sqf for sale or lease between FY07 and FY09. We think this is a very optimistic target considering that the company presently has about 46m sqf under construction. DLF effectively has developed 25m sqf (excluding plots) since its inception in 1946. Plots sales do not require lot of execution capabilities and hence we think 150m sqf is aggressive as it is 6x of what DLF has executed so far.

Fig 23 Business segment-wise DLF development plan for FY07–09



Source: DLF propectus, Macquarie Research, March 2007

Ownership or arrangement for 200m sqf is not clear

- **Lack of clarity on ownership of 200m sqf of saleable area**: Of the total developable area of 574m sqf, 29m sqf represents DLF's equity interest in joint ventures with third parties; 200m sqf provides benefits of ownership of the development but the land is not owned by DLF, and for the remaining 345m sqf, DLF has both ownership and sole development rights. In the absence of clarity on ownership of 200m sqf we cannot estimate the margins DLF would make on such development as the cost of transfer of development rights cannot be ascertained.

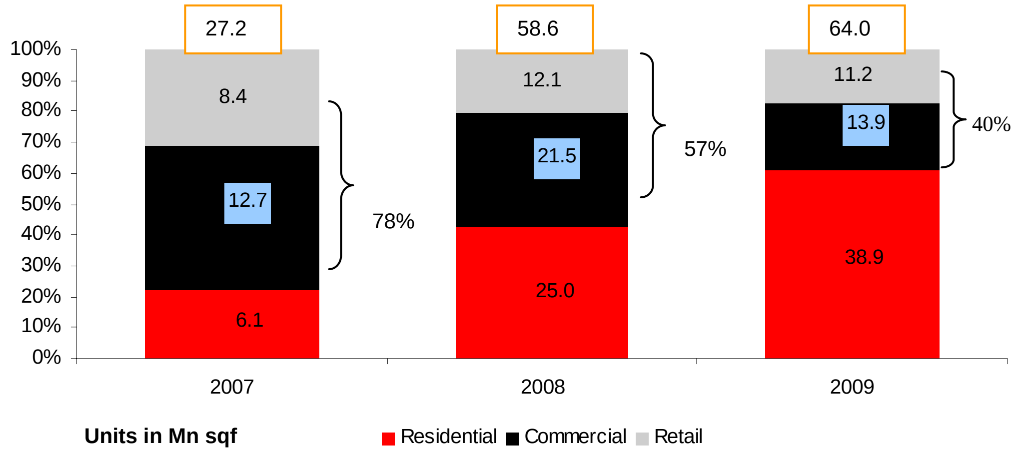
- **Too large dependence on Gurgaon**: The total land bank of 10,225 acres is highly skewed in favour of Gurgaon and to some extent Kolkata too. DLF has approximately 72% of its total land bank in Gurgaon (49%) and in Kolkata (23%) together. We think this is a big concentration in one city considering Gurgaon is a satellite town and it took DLF almost 30 years to develop 3,000 acre township – DLF city.

DLF has 5,000 acres (~50% of total land bank) in Gurgaon, which is worrying

As a result of 49% of the total land bank in Gurgaon, DLF becomes susceptible to any adverse development is in Gurgaon like change in land use regulations, zoning laws, taxes, natural calamity and any social or political development that depresses real estate sentiment in Gurgaon.

- **More focus on commercial & retail and less on residential between FY07–09**: DLF plans to make available 150m sqf for sale or lease between FY07–09 with 47% as residential, 32% as commercial and the remaining 21% as retail development. This mix is different to total industry demand mix where more than 75% of total demand is from residential sector. Between FY07–09 total commercial and retail demand is expected to be around 160–190m and 210–240m respectively.

Fig 24 Commercial and retail accounts for 53% of FY07–09 development



Source: DLF prospectus, Macquarie Research, March 2007

We believe DLF focus on premium residential is not sustainable

- **Focus on premium residential product:** DLF focuses on development of luxury residential accommodation and are offering theme based projects such as The Magnolias development in DLF city, which includes a golf course. A look at DLF's residential offering tells us that minimum price for a unit is US$400,000 (Rs17.5m) and goes up to US$1m (Rs44.1m). In case of such expensive and large sized apartments, investors/speculators buy such apartments when the companies offer Rs700–800/ sqf discount on the first day of the launch and then sell them at a discount of Rs300–400 per sqf to another customer later. Essentially investors gains at the company's expense in case of such high-priced products.

One-time income of Rs 21.6bn has spurred 8mth Nov-06 results

- **Strong growth in 8m November 2006 results not sustainable:** The financial results of eight months ending November 2006 are spurred by the inclusion of one time income of Rs21.6bn on account of sale of commercial properties to DLF Assets Private Limited, a promoter group company. This sale accounted for 65% of the total revenue for the period and an addition of Rs17.4bn to profit before tax figure. Such stream of revenue is not a regular feature as DLF earlier operated on 'develop and lease' model for its commercial development. However with effect from FY07 the company has decided to follow 'develop and sale or lease' model and as a result the company has sold its existing commercial assets and recorded one time income of Rs21.6bn.

Top ten questions to ask

We list ten questions worth asking DLF based on our analysis of the company information that is publicly available.

1. **How has DLF's land bank doubled in the eight months from May-06 to Jan-07?**

   DLF has disclosed a land bank of 10,255 acres this time which is more than double of land bank declared by DLF in its first filing. DLF had declared 4,265 acres as per the original offer document filed in May 2006. The developable area has now been increased to 574 million square feet as against 220m sqf declared in the original offer document filed in May 2006.

2. **How much time does DLF estimate it will require to develop nearly 5,000 acres of land bank in Gurgaon?**

   DLF has specifically mentions in its prospectus that its current land bank should be sufficient for the next ten years. We estimate DLF would have to deliver approx. 28m sqf every year for next ten years. What is the time horizon for the total development of its Gurgaon land bank of 5,000 acres?

3. **What are the transfer fees for the development rights of 200m sqf, as noted in the prospectus?**

   Of the total 574m sqf, 200m sqf is land where DLF has sole developing rights but does not own the land. These development rights would be transferred from land owning companies to DLF with some transfer fees. Without quantifying the transfer fee, it is difficult to ascertain at what price those development rights would be transferred from land owning companies to DLF. If the transfer fee charged is higher than the land owning companies' land acquisition cost, DLF would not be able to reap the benefits of the low cost of land. This concern can be validated by the increase in goodwill amount from Rs522m in FY05 to Rs8,489m in FY06 on account of the difference between the purchase price of the land owning companies and the book value of the net assets of those companies.

4. **At what rate has DLF sold its commercial assets to DLF Assets Private Ltd (DAL)?**

   DLF prospectus specifies that Rs21.6bn has been realised on account of sale of commercial properties to DAL but it does not specify the area sold. Hence one cannot ascertain at what rate/sqf DLF has sold its commercial assets to DAL. Also these assets were not sold in open auction and therefore there is a question mark over whether the assets were sold at market price.

5. **Why was there no independent valuation included in the 2007 prospectus when such a valuation was included in the 2006 prospectus?**

   Notably unlike last time, the current offer document is silent on the valuation of the land bank. In the document filed in May, DLF had published valuations made by Cushman & Wakefield valuing DLF between $17.4–19.2bn and by Jones Lang LaSalle at $19.2bn for 4,265 acres.

6. **How does DLF estimate to make available for sale 69.8m sqf of residential space in FY07–09 from the present 9m sqf?**

   Presently DLF has 9m sqf of residential space under construction and it aims to make available for sale 69.8m sqf by the end of March 2009. Even after taking into account that India allows pre-sale of residential projects, we think the estimate of 69.8m sqf is very optimistic, especially considering DLF's focus on premium residential development which is more of a margin business rather than volume business. More clarification needs to be sought from DLF on its residential projects.

7. **How does DLF intend to ensure fair open market auction for future sale of commercial assets?**

   Going forward, DLF plans to follow ‘develop and sell’ model for some of its commercial assets. DLF has indicated it will sell its commercial assets in open auction with group promoter company DLF Assets Ltd (DAL) participating. In FY07, leased commercial assets were sold to DAL without an open auction and we fear that if assets are sold without open auction DLF might not be able to realise the market value of the assets.

8. **Why has DLF adopted a strategy to focus on premium residential development?**

   DLF is focusing on luxury residential development in a market where the bulk of the demand originates from middle income group households. By ignoring middle income group residential demand DLF is foregoing volume business. It would also be fair to understand the customer profile of the buyers for such high end residential development in Gurgaon.

9. **How does DLF intend to overcome the technical hitch of the issue price not being less than Rs500/share?**

   A SEBI circular dated 28 May 2004 could act as a hurdle to the DLF issue price. The circular was an attempt by the regulator to discourage private companies from planning a stock split just before a public offer. It allows companies with shares of face value below Rs10 to issue a public offer only if the share price is to be higher than Rs500. This circular reduces DLF's flexibility to price below Rs500 unless it wants to restructure its share capital once again. Also it has the option of valuing the company at $19.2bn without any capital restructuring.

10. **Can we have more insight into the recent JV with Prudential Financial Inc.?**

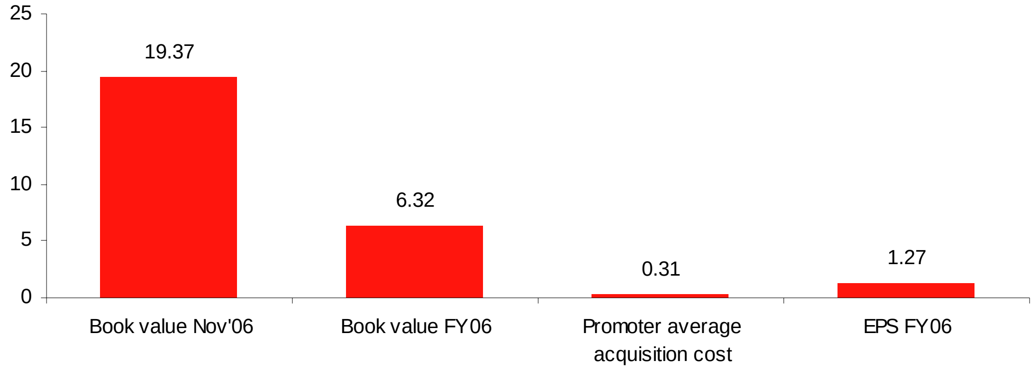
    DLF has recently announced a JV with Prudential Financial, Inc. (PFI), a financial services leader headquartered in the United States. They plan to establish a joint venture life insurance company in India. DLF is expected have a 74% stake and PFI a 26% stake in DLF Pramerica.

Financial summary

Book value per share and capital raising history

- **One-time income tripled DLF's net-worth**: DLF's book value per share has increased 206% from Rs6.32/share in FY06 to Rs19.37 as at 30 November 2006. This is mainly due to one-time income from the sale of commercial assets to a promoter group company.
- **Promoter's acquisition cost is very low:** The average cost of acquisition by promoters is Rs0.31/share (of face value of Rs2 each). The number of shares has increased 87x since March 2006 on account of the 1:10 conversion of debentures into shares and a further 1:7 bonus issue. The debentures were issued in January 2006 and were then converted into shares in March 2006.
- **DLF had de-listed from DSE in 2003 and from BSE in 1982:** DLF has a history of delisting its shares from both Bombay Stock Exchange (BSE) in 1982 and Delhi Stock Exchange (DSE) in 2003. The shares from BSE were delisted due to substantial increase in listing fees and shares of the company were delisted from DSE consequent to level of public shareholding falling below a prescribed level.

Fig 25 Book value vs promoter acquisition cost per share



Source: DLF prospectus, Macquarie Research, February 2007

One-time income has spurred 8m Nov'06 results – sale of commercial assets

- The financial results for the eight months ending November 2006 were boosted by the inclusion of one-time income of Rs21.6bn from the sale of commercial properties to DLF Assets Private Limited, a promoter group company. This sale accounted for 65% of the total revenue for the period and resulted in the addition of Rs17.4bn to profit before tax.
- This type of revenue stream is not a regular feature as DLF earlier operated on 'develop and sell' model for its commercial development. However, with effect from FY07 the company has decided to follow a 'develop and sale or lease' model and as a result the company has sold its existing commercial assets and recorded one-time income of Rs21.6bn. The consolidated total income and net profit for the eight months ending November 2006 was Rs 33.2bn and Rs 18.3bn respectively.

Fig 26 DLF: Profit and loss summary

	8M Nov'06 (Rs m)	% of Total Income	FY03/06 (Rs m)	% of Total Income	FY03/05 (Rs m)	% of Total Income	FY03/04 (Rs m)	% of Total Income
INCOME								
Sales & other receipts	**19,708**	**59%**	**11,536**	**93%**	**6,081**	**97%**	**5,058**	**96%**
- Sales Revenue	17,310	52%	9200	74%	4087	65%	3134	60%
- Rent & License Fee	939	3%	422	3%	375	6%	340	6%
- Maintenance Income	556	2%	481	4%	306	5%	209	4%
- Power Supply	653	2%	1087	9%	1035	17%	1149	22%
- Others	250	1%	346	3%	278	4%	226	4%
Investment Income	**-**	**0%**	**163**	**1%**	**0**	**0%**	**78**	**1%**
Other Income	**13,531**	**41%**	**721**	**6%**	**179**	**3%**	**130**	**2%**
- Interest	997	3%	553	4%	76	1%	84	2%
- Others	12,534	38%	168	1%	103	2%	46	1%
Total Income	**33,239**		**12,420**		**6,260**		**5,266**	
EXPENDITURE								
Cost of Revenue	**5,148**	**15%**	**5,243**	**42%**	**3,165**	**51%**	**2,685**	**51%**
- Project Cost	4,616	14%	4416	36%	2517	40%	2200	42%
- Other costs	532	2%	827	7%	648	10%	485	9%
Establishment Costs	460	1%	397	3%	447	7%	313	6%
Finance Charges	2,480	7%	1685	14%	390	6%	330	6%
Other expenses	1,675	5%	1139	9%	787	13%	848	16%
Depreciation	352	1%	361	3%	333	5%	288	5%
Total Expenditure	**10,115**	**30%**	**8,825**	**71%**	**5,122**	**82%**	**4,464**	**85%**
Profit before tax	23,124	70%	3,595	29%	1,138	18%	802	15%
Provision for tax	4,816	14%	1668	13%	259	4%	250	5%
Net profit after tax	18,308	55%	1,927	16%	879	14%	552	10%
Minority Interest	8	0%	10	0%	14	0%	14	0%
Net Profit	**18,300**	**55%**	**1,917**	**15%**	**865**	**14%**	**538**	**10%**
EPS (Rs)	**12.11**		**1.27**		**0.57**		**0.36**	

Source: DLF prospectus, Macquarie Research, March 2007

Fig 27 DLF: Balance sheet

	8M Nov'06 (Rs m)	As % of Total Assets	FY03/06 (Rs m)	As % of Total Assets	FY03/05 (Rs m)	As % of Total Assets
ASSETS						
Gross Block	13,135	9%	11,237	16%	8,253	30%
Less: Acc. Depreciation	2,213	1%	1,891	3%	1,549	6%
Net Block	10,922	7%	9,346	13%	6,704	24%
Capital Work-in-progress	11,116	7%	6,239	9%	3,506	13%
Total fixed assets	**22,038**	**14%**	**15,585**	**22%**	**10,210**	**37%**
Investments	**1,280**	**1%**	**8,300**	**12%**	**400**	**1%**
Current Assets, Loans & Adv.						
Stocks	54,852	36%	17,873	26%	7,049	26%
Sundry debtors	15,508	10%	6,580	9%	2,852	10%
Cash & bank balances	6,160	4%	1,950	3%	424	2%
Other current assets	95	0%	23	0%	20	0%
Loans and advances	44,192	29%	10,637	15%	6,019	22%
Total Current Assets	**120,807**	**79%**	**37,063**	**53%**	**16,364**	**60%**
Goodwill	**8,733**	**6%**	**8,489**	**12%**	**522**	**2%**
Total Assets	**152,858**		**69,437**		**27,496**	
LIABILITIES & PROVISIONS						
Secured loans	85,298	56%	39,560	57%	7,952	29%
Unsecured loans	9,152	6%	1,760	3%	1,724	6%
Current liabilities & provisions	28,847	19%	18,469	27%	9,344	34%
Deferred tax liability (net)	303	0%	93	0%	962	3%
Total Liabilities & Provisions	**123,600**	**81%**	**59,882**	**86%**	**19,982**	**73%**
NET WORTH						
Share capital	3,026	2%	378	1%	35	0%
Reserves	26,030	17%	9,123	13%	7,436	27%
Minority interest	202	0%	54	0%	43	0%
Net worth	**29,258**	**19%**	**9,555**	**14%**	**7,514**	**27%**

Source: DLF prospectus, Macquarie Research, March 2007

Fig 28 DLF: Cashflow summary

Summary cash flow information	8M Nov'06 (Rs m)	FY03/06 (Rs m)	FY03/05 (Rs m)
Net cash from operating activities	(62,274)	(10,951)	5,754
Net cash from investing activities	14,313	(18,660)	(7,681)
Net cash from financing activities	51,283	30,520	1,934
Cash at beginning of the year	1,105	197	191
Cash generated during the year	**3,322**	**909**	**7**
Cash at end of the year	**4,427**	**1,106**	**198**

Source: DLF prospectus, Macquarie Research, March 2007

Important disclosures:

Recommendation definitions

Macquarie Australia/New Zealand
Outperform – return >5% in excess of benchmark return (>2.5% in excess for listed property trusts)
Neutral – return within 5% of benchmark return (within 2.5% for listed property trusts)
Underperform – return >5% below benchmark return (>2.5% below for listed property trusts)

Macquarie Asia
Outperform – expected return >+10%
Neutral – expected return from -10% to +10%
Underperform – expected return <-10%

Macquarie First South Securities (South Africa)
Outperform – expected return >+5%
Neutral – expected return from -5% to +5%
Underperform – expected return <-5%

Recommendations – 12 months

Note: Quant recommendations may differ from Fundamental Analyst recommendations

Recommendation proportions

	AU/NZ	Asia	RSA
Outperform	43.12%	58.91%	42.20%
Neutral	48.98%	22.92%	46.80%
Underperform	11.90%	18.17%	11.00%

For quarter ending 31 December 2006

Volatility index definition*

This is calculated from the volatility of historic price movements.

Very high–highest risk – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.

High – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.

Medium – stock should be expected to move up or down at least 30–40% in a year.

Low–medium – stock should be expected to move up or down at least 25–30% in a year.

Low – stock should be expected to move up or down at least 15–25% in a year.
* Applicable to Australian/NZ stocks only

Financial definitions

All "Adjusted" data items have had the following adjustments made:
Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives & hedging, IFRS impairments & IFRS interest expense
Excluded: non recurring items, asset revals, property revals, appraisal value uplift, preference dividends & minority interests

EPS = adjusted net profit / efpowa*
ROA = adjusted ebit / average total assets
ROA Banks/Insurance = adjusted net profit /average total assets
ROE = adjusted net profit / average shareholders funds
Gross cashflow = adjusted net profit + depreciation
*equivalent fully paid ordinary weighted average number of shares

All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).

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Ulrike Pollak-Tsutsumi (Frankfurt)	(49) 69 7593 8747
Daniel Fust (Geneva)	(41) 22 818 7710
Thomas Renz (Geneva)	(41) 22 818 7712
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Stuart Smythe (India)	(9122) 6653 3200
Eugene Ha (Korea)	(822) 3705 8643
K.Y. Nam (Korea)	(822) 3705 8607
Derek Wilson (London)(N Asia)	(44) 20 7065 5856
Julien Roux (London)	(44) 20 7065 5887
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Sales Trading cont'd

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Depository Receipts - Robert Ansell	(852) 2823 4688
Derivatives - Vipul Shah	(852) 2823 3523
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