MORNING INSIGHT

PRIVATE CLIENT RESEARCH

JULY 17, 2009

Economy News

- The government intends to borrow Rs.1.1trn over the next 75 days, which will push up its first-half borrowings by Rs.580bn from the earlier planned level. This means that the government will now borrow Rs.2.99trn by the end of September through bond issues, which would account for around two-thirds of the Rs.4.51trn the Centre proposes to borrow during the current financial year. (BS)
- China's pace of economic expansion sped up to hit 7.9% in the second quarter, fueled by state spending and bank lending, reinforcing hopes it will lead the world economy out of its deepest recession in 80 years. With help from $580 billion in government pump priming, the world's third-biggest economy picked up pace again after the global economic crisis dragged growth down to 6.1% in the first quarter. (ET)

Corporate News

- British Telecom (BT) will move back some 4,000 call centre jobs outsourced to Indian service providers, as the company seeks to ensure more employment opportunities for British workers and protect jobs of those employed directly by the company. Both **Infosys** and **Tech Mahindra,** which count BT as one of their top customers, are expected to see a decline in back office outsourcing business from the phone firm. (ET)
- **Sterlite Industries** has said that, it has raised over Rs.70bn from the American market as equity to part finance its power projects entailing an investment of Rs.500bn. "We are raising about Rs.70bn through ADR to mainly fund the power project. The issue is complete today," Vedanta Resources Chairman Anil Agarwal told in an interview from London. (ET)
- The government is considering divestment of stake in four PSUs, **NMDC, KIOCL, MOIL** and **RINL,** administered by the steel ministry, as part of a broader plan to mobilise resources to meet their funding needs. In a written reply in Lok Sabha today, Minister of State for Steel A Sai Prathap said the ministry has received proposals to divest its equity in steel firm Rashtriya Ispat Nigam Ltd, besides Manganese Ore Ltd. (BS)
- **Sobha Developers Ltd** is looking to raise about Rs.12bn-14bn by selling part of its land parcels in a bid to reduce its outstanding debt. The developer has a timeline of around two years to raise funds and is looking at outright sale or by selling stake to private equity investors. Sobha' managing director J C Sharma could not be contacted for comment. (DNA Money)
- The government has ordered a special audit of the country's five leading private-sector mobile telecoms firms to check whether there had been any misreporting of revenue, the junior telecoms minister said on Thursday. "Certain phone firms have been charged with misreporting their revenue," Gurudas Kamat said in a written reply to law makers in the upper house of the Parliament. "Hence, the Department of Telecom has decided to conduct special audit of **Bharti Airtel, Reliance Communications, Vodafone Essar Ltd, Idea Cellular Ltd** and **Tata Teleservices Ltd,**" he said. (ET)
- **GAIL** will lay down a 600-km long gas pipeline from Jhabua to Kailaras in Madhya Pradesh. "The proposed gas pipeline from Jhabua to Kailaras covering a distance of nearly 600 km will be laid at an estimated cost of Rs.30bn," GAIL Chairman U D Choubey told reporters at the company's Vijaypur plant. (ET) ·
- Stricter cost control measures by **Bajaj Auto** helped it post a growth of 67% in net profit at Rs.2.93bn for the first quarter ended June 30. High margins from its Pulsar range of bikes, which were only recently given a face-lift, further pushed the bottom-line of India's second-biggest motorcycle maker (BS)
- **Polaris Software** has reported 18% growth in net profit for the first quarter to Rs 318mn as against Rs 270mn in the same quarter last year. Income from sales has increased to Rs 3.25bn as against Rs 3.17bn in the same quarter last year (BS)

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

Equity

		% Chg		
	16 July 09	1 Day	1 Mth	3 Mths
Indian Indices				
SENSEX Index	14,250	(0.0)	(1.9)	29.3
NIFTY Index	4,231	(0.0)	(2.9)	25.0
BANKEX Index	7,763	(0.2)	(3.2)	40.5
BSET Index	3,367	0.3	5.3	36.8
BSETCG INDEX	11,818	(1.6)	(2.9)	50.7
BSEOIL INDEX	9,151	1.9	(3.8)	16.2
CNXMcap Index	5,352	(0.1)	0.2	38.5
BSESMCAP INDEX	5,546	0.4	(4.2)	40.3
World Indices				
Dow Jones	8,712	1.1	2.5	7.1
Nasdaq	1,885	1.2	4.3	12.7
FTSE	4,362	0.4	1.9	6.6
Nikkei	9,344	0.8	(4.6)	5.3
Hangseng	18,362	0.6	2.5	18.8

Value traded (Rs cr)

	16 July 09	% Chg - Day
Cash BSE	6,474	21.0
Cash NSE	19,784	18.6
Derivatives	68,847	18.8

Net inflows (Rs cr)

	15 July 09	% Chg	MTD	YTD
FII	1,031	128	5,116	30,005
Mutual Fund	249	12	230	2,759

FII open interest (Rs cr)

	15 July 09	% Chg
FII Index Futures	7,648	(4.1)
FII Index Options	23,979	(1.7)
FII Stock Futures	18,290	0.1
FII Stock Options	859	1.1

Advances / Declines (BSE)

16 July 09	A	B	S	Total	% total
Advances	98	767	184	1,049	53
Declines	103	613	163	879	44
Unchanged	2	44	14	60	3

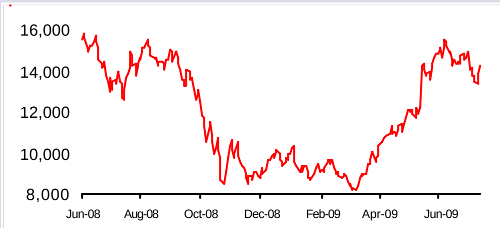
Commodity

			% Chg		
		16 July 09	1 Day	1 Mth	3 Mths
Crude (NYMEX)	(US$/BBL)	61.7	(0.6)	(13.2)	22.5
Gold	(US$/OZ)	937.3	(0.2)	(0.2)	7.9
Silver	(US$/OZ)	13.3	0.2	(7.3)	11.8

Debt / forex market

	16 July 09	1 Day	1 Mth	3 Mths
10 yr G-Sec yield %	7.30	6.98	7.04	6.61
Re/US$	48.70	48.65	47.75	49.76

Sensex



RESULT UPDATE

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ZEE ENTERTAINMENT ENTERPRISES LTD (ZEEL)

PRICE: RS.180 **RECOMMENDATION: ACCUMULATE**
TARGET PRICE: RS.212 **FY10E: EV/EBITDA: 14X; P/E: 17X**

ZEEL- advertising revenues decline 29% YoY; robust DTH revenue pick up spurs subscription revenue growth. Cost containment, lower interest and depreciation outgo help bottom line exceed estimates.

- **Q1FY10 numbers are a mixed bag- revenues disappoint, cost containment surprises positively. Advertising revenue (down 29% YoY) leads the 12% YoY decline in overall revenues. Subdued macro, relatively weak ratings in Q1 and rival sporting properties contribute to decline in advertising revenues.**
- **Lower than expected interest and depreciation outgo lead to profits modestly higher than estimates. Recurring PAT is down 12% YoY at Rs.913mn. We expect Q1FY10E to be the likely bottom, in terms of advertising revenue growth and opine the base effect should start getting better Q3 onwards. Advertising spend growth in FMCG & Telecom, the key drivers for GEC ad revenues, continues to be firm even in an uncertain environment, as per our channel checks.**
- **We note ZEEL's improved program performance in Q2FY10 is likely to sustain and reflect on advertising revenues with a lag. Renewed optimism on a faster recovery in the economy and corporate earnings will likely be encouraging for advertising revenue trends too.**
- **Subscription revenues- 23% QoQ and 88% YoY growth in DTH stream for the quarter; we remain positive on the structural changes in the market and expect an18% CAGR over FY08-10E. We also reiterate they offer a counter-cyclical growth opportunity, expect domestic subscriptions to grow led by increasing DTH penetration.**
- **We tweak earnings to reflect better than estimated cost management and higher DTH revenue. Increase FY10E EPS by 3%; raise price target to Rs.212 (Rs.198). Noting upside to our fair value and also stock's recent under-performance, we move recommendation to ACCUMULATE (REDUCE previously).**
- **Price target works out to a c30% premium to the market multiple; the ZEEL stock in better times (stronger competitive positioning and advertising revenue environment) has traded at a c50% premium to the market. Belied hopes on a faster than expected revival in advertising revenue trends and/or loss in viewer ratings remain key risks.**

Summary table

(Rs mn)	FY08	FY09E	FY10E
Sales	18,354	21,729	22,009
Growth (%)	27.4	18.4	1.3
EBITDA	5,423	5,331	6,025
EBITDA margin (%)	29.5	24.5	27.4
Recurring PAT	3,833	3,749	4,558
Net debt (cash)	815	507	(7,245)
EPS (Rs)*	8.8	8.6	10.5
Growth (%)	61.6	(2.2)	21.6
CEPS	9.4	9.3	11.3
DPS (Rs)	2.0	2.0	2.0
ROE (%)	14.0	12.5	13.8
ROCE (%)	19.8	18.7	18.3
EV/Sales (x)	4.4	3.7	3.7
EV/EBITDA (x)	15.0	15.2	13.5
P/E (x)	20.4	20.8	17.1
P/Cash Earnings	19.2	19.3	16.0
P/BV (x)	2.7	2.5	2.2

*Source: Company, Kotak Securities - Private Client Research; * Stripped of tax write-backs of Rs.1.42bn in FY09*

Result Highlights- Revenues disappoint, quantum of cost containment surprises, other line items like lower interest and depreciation also prop bottom line. Revenues de-grow 12% YoY, comparable profits also drop 12% YoY.

- For the quarter ZEEL's advertising revenues contracted by 29% YoY and 13% QoQ to Rs.1.98bn. Subscription growth on the other hand was a better performance with a 12% YoY growth to Rs.2.4bn. 'Other' services came in at Rs.370mn, down 21% YoY, these include revenues from the movie business (ZES), syndication revenues and ad space selling among others. Put together revenues were Rs.4.76bn for the quarter, down 12% YoY and 7.4% QoQ.
- Within the subscription revenue stream, international revenues (Rs.1.09bn) continued to disappoint by remaining flat; domestic pay revenues were up 25% YoY at Rs.1.32bn. DTH collections grew strongly by 88% YoY and 23% QoQ to Rs.467mn for the quarter. International pay revenues have failed to reflect currency gains, largely on account of the sub churn, in our opinion and also seasonality of the network's sport property.

- We attribute the sharp advertising revenue contraction to the deteriorated macro environment for ad spends and the high competitive intensity that has led to a fragmented market. Flagship Zee TV's weak ratings and also telecast of rival sporting properties in the period (IPL) also impacted advertising revenues adversely during the period; the quantum though surprised us.
- EBITDA margins at 24.6% were up 120bps QoQ despite revenue contraction on the back of sharp cost containment initiatives. Operating costs declined by 10%- there was a 12% reduction in selling costs YoY, while employee costs declined 11% QoQ. The larger cost- program and operating was also flat YoY while rising 7% QoQ.
- Of these costs, we believe program and operating costs are likely to rise in the ensuing quarters as programming investments rise to safeguard Zee TV's competitive positioning. The management has indicated that it aims at keeping the cost base at current levels- aided by saving on Zee Next expenses that has been discontinued as well as rationalization across cost heads like selling and carriage fees.
- Below the EBITDA line, there were items that boosted the PAT. Interest was sharply down at Rs.91.1mn (Rs.214mn in Q1FY09 and Rs.509mn in Q4FY09). The management has explained the above as benefits of a much lower borrowing rate on restructured debt as well as the absence of any losses to be provided for on forex instruments.
- At a debt of Rs.4.5bn as of quarter end and if lower rates sustain ZEEL could report significant savings on this line in FY10. Its FY09 interest outgo including Rs.450mn of forex loss was Rs.1.3bn.
- Net profits as a result came in at Rs.913mn, down 12% YoY, on a comparable basis. Core EPS was Rs.2.1 for Q1FY10 and was Rs.8.7 in FY09.

Financial performance

(Rs mn)	Q1FY10	Q1FY09	% chg	Q4FY09	% chg
Revenues	**4759.4**	**5419.5**	**-12.2**	**5137.5**	**-7.4**
Expenditure	3589.2	3978.0		3935.8	
EBDITA	**1170.2**	**1441.5**	**-18.8**	**1201.7**	**-2.6**
Depreciation	75.0	55.0		98.9	
EBIT	**1095.2**	**1386.5**	**-21.0**	**1102.8**	**-0.7**
Net Interest	91.1	214.0		508.6	
Other Income	325.1	278.0		638.7	
PBT	**1329.2**	**1450.5**	**-8.4**	**1232.9**	**7.8**
Tax	415.9	417.0		329.7	
PAT	**913.3**	**1033.5**	**-11.6**	**903.2**	**1.1**
Minority Int	-105.8	0.0		3.4	
PAT after M I	1019.1	1033.5	-1.4	899.8	13.3
EO items	0.0	-574.0		-65.0	
PAT after EO items	1019.1	1607.5	-36.6	964.8	5.6
EPS* (Rs)	**2.1**	**2.4**		**2.1**	
OPM (%)	24.6	26.6		23.4	
GPM (%)	23.0	25.6		21.5	
NPM (%)	21.4	29.7		18.8	

*Source: Company, *-Core EPS, stripped of one-times*

Consistent improvement in ratings over the quarter; Zee TV banks on fresh content for a further push

- ZEEL's flagship Zee TV's GRPs have improved significantly 31% to an average of 231 in Q1FY10, from a low of 174 on an average in Q3FY09. Its share of GRPs has also increased to 19.2% in Q1FY10 from 16.1% in Q3FY09. In prime time, Zee TV's improved performance has been more impressive with the share of GRPs increasing to 23% in Q1FY10 from 19% in Q3FY09.
- For the week ended June 21, '09, Zee TV had regained the No.1 slot, which it held jointly with Colors at 243 GRP's. Star Plus with 218 GRP's, at No.3 has seen the impact of the competitive intensity, with a decline in GRP's over the quarter.
- For Zee TV, we note the improvement in ratings has come from new program traction and not from blockbuster movies. For now, Zee TV seems to have shifted focus from blockbuster movies. STAR Plus and Colors continue to focus on movies for maintaining GRPs.
- Opportunity exists for Zee TV to become the leader in more primetime slots, in our opinion. Zee TV is embarking on further changes in its programming slate. It has also added to its prime time programming that has met with a decent initial response; from a financial perspective we expect this revival in ratings to reflect on advertising revenues with a lag.
- A show by Balaji Telefilms (BTL), Pavitra Rishta, has replaced the long running 'Saat Phere' in the 9-9:30pm slot. We note that 'Pavitra Rishta' is a remake of the hugely successful Tamil serial, Thitumarhi Selvam of Sun TV, currently the top-rated show in the Tamil market with average TRPs of ~20. Our recent interaction with the content producer pointed to an equal optimism regarding the prospects for this show's popular approval.

When there is a recovery in corporate earnings outlook and sentiment, traditional media will be early beneficiaries.

- Consensus view for the Indian advertising market growth has been between 5% and 10% for FY10. On a wider basis expectations have been of around 6-8% for the overall advertising market, for CY09E. This estimate of around 8% growth for the advertising market, we note, would be the lowest since 2001.
- Industry expectations have been of c8%YoY growth in the advertising market to be led by double digit growth in FMCG, telecom and nascent categories like DTH.
- In recent times there have been renewed expectations of decisive policy action that is expected to lead to a faster recovery in economic growth and also corporate earnings.
- If the same do materialize we see a swift recovery in corporate sentiment to invest and consequently an up tick in advertising revenue trends. While it may be too early to re-calibrate industry growth outlook for CY09, we do believe the macro has seen material improvement and expect a revenue pickup 2HFY10E onwards.

Media- ad outlook, (Rs mn)

Media Segment	2008	2009E	% Change
TV	84000	93530	11.3
Newspaper	100330	107700	7.3
Radio	8800	10560	20.0
Magazine	8030	7220	-10.1
Internet	6300	8500	34.9
Outdoor	16900	16900	0.0
Cinema	800	720	-10.0

Source: BS, GroupM report

- We also believe the early beneficiaries of this revival to be the more traditional and established forms of media- print and TV broadcasting. We also expect spends in metros to gain traction as advertisers return in the backdrop of an improved macro environment.

Advertising revenue revival will be the; while visibility for FY10E spends may have increased the jury is out on the sustainability of trends. More visibility key for incremental upgrades in revenue outlook.

- We have consistently highlighted the strong correlation between advertising revenue growth and the economic growth trajectory. Our concerns on the economic growth trajectory and corporate earnings outlook were the key factors that have contributed to our cautious outlook on advertising -dependent media businesses.
- For ZEEL, the rising competitive intensity and falling ratings were an added pressure point that saw the company's financial reporting tame growth for the last 2Q's. Stock performance too has been lower than peers.
- We note that the ZEEL stock for the first time post 2005 (after improvement in Zee TV's rankings), was trading at a ~20%+ discount to the market, till early May 2009- on these concerns. Even after the recent rally YTD the stock has underperformed vis-à-vis the Sensex.

Projected financials- improved ratings will help with a lag; advertising to pick up only in 2HFY10, in our opinion

- ZEEL's FY08 ad revenues grew at 32% and in FY09 it clocked a growth of 14%- slowed by hyper-competitive market place, a slowing economy and loss in ratings.
- Given the formation of a stable government there now renewed expectations of decisive policy action that is expected to lead to a faster recovery in economic growth and also corporate earnings.
- If the same do materialize we see a swift recovery in corporate sentiment to invest and consequently an up tick in advertising revenue trends. While it may be too early to re-calibrate industry growth outlook for CY09, we do believe the macro has seen material improvement and expect a revenue pickup 2HFY10E onwards.
- Nevertheless we believe that revival in advertising revenues is likely to be back ended; the recent quarter Q1 we expect will be the likely bottom in terms of advertising revenue growth. We expect improvement thereafter - Q1 has been challenging in multiple ways, as expected by us with muted domestic advertising market growth and problems for GEC's further compounded by IPL and elections.
- However, we expect Q1FY10E to be the bottom, in terms of reported revenue growth and opine the base effect should start getting better Q3 onwards. We now expect advertising revenues to grow at a CAGR of 115% over FY08-10E. For FY10E we are factoring in an 8% decline in overall ad revenues; with the H1 declining by 25% and H2 growing by 10%.
- We believe this revenue growth assumption is backed by a better macro environment that may support ad revenues; more critically improved and sustained ratings could add more upside to the forecast, in our opinion.

Subscription revenues- we expect an 18% CAGR over FY08-10E. Pay revenues- a counter-cyclical growth opportunity, expect domestic subscriptions to grow led by increasing DTH penetration. DTH may be the game changer

- Going forward over FY08-10E we expect subscription revenues to grow at an 18.5% CAGR. We believe pay revenues will likely become the next enabler/supporter for ZEEL financials as we expect ad revenue growth to tumble over the medium term.
- We expect this counter-cyclical growth to be driven by a revamp of the domestic cable distribution business and strong growth in the DTH subscriber base. We also believe ZEEL's international subscription revenues are likely to benefit from the recent INR depreciation; and expect a 10% CAGR in the same over the period.
- While initial CAS off-take has been muted, the opportunity in our opinion will be led by a strong traction in DTH services, which is expected to have 21mn subscribers by FY11E, up from the c9mn currently.
- We expect DTH collections to rise at a 91% CAGR over FY08-FY10E, aided by strong growth in the DTH sub count, growing realizations from new operators and still relatively reasonable positioning of the ZEEL bouquet.

Margins- Revenue growth to slow, increasing pay revenue- a buffer for margins given low associated costs. Cost cutting measures to add significantly.

- Cost savings in FY10E will likely be driven by savings on programming costs and closure of Zee Next. We note that Zee TV programming hours have been trimmed with most of the programming cut in the afternoon slot. Zee TV reduced the weekly number of afternoon programming hours from 10 at its peak in Q3FY09 to 7.5 at the beginning of Q4FY09 and further to zero by end-Q4FY09.
- Also Zee TV does not plan to add original programming in the afternoon slots before September '09 since repeats of prime-time shows are gaining better TRPs.
- While the management has stated its intent to curtail costs, we believe the need to counter competition through content investments will likely keep margin gains under check, till the time revenue outlook improves materially.
- On the margin front, we are estimating EBITDA margins to gain over FY09-10E as operating leverage from the growing subscription revenue stream that does not have significant associated costs is expected to be a buffer for margins.
- We consequently estimate an EPS CAGR of 9% over FY08-10E; an EPS of Rs.10.5 (Rs.10.1 earlier) in FY10E from Rs.8.8 in FY08.

Valuations while being lower than historic premium to broader market look ample. Upsides will depend on news-flow on viewer ratings, macro-environment.

- At 17x FY10E EPS ZEEL, valuations look ample and are at an 8% premium to the average market multiple. Advertising revenue trends and program ratings, we opine will remain earnings and share catalysts over the medium term.
- A further gain in Zee TV ratings, and sustenance, in our opinion will likely be the game changer for the stock. It is likely to enhance visibility on the outlook for FY10-11E advertising revenues and could see the stock trading closer to its historic 50% premium to the market multiple.
- Prior to losing its competitive positioning and in a stronger advertising revenue environment, the stock has traded at 23-25x one year forward EPS. Historically in such a period, the stock has traded at a c50% premium to the average market multiple.

- Strong domestic subscription growth is something we remain hopeful that has likely been validated in the traction exhibited in Q1FY10. We see sustained performance on this count as another likely re-rating trigger for the stock, in addition to viewer ratings.

Upside to fair value and recent underperformance can be used to ACCUMULATE. Preferred pick on the strong subscription opportunity for leading broadcasters.

- We raise our target price for the ZEEL stock to Rs.212 (Rs.198) as we increase FY10E EPS by 3-5%.
- Our DCF based price target is also positively impacted by the expected improvements in working capital, post liquidity issues for group companies (Dish TV) looking to be resolved to an extent.
- Our target multiple is on par with ZEEL's five- year average trading multiple-20x one year forward EPS. It is also at a 30% premium to the market multiple- the stock has historically traded at a c53% premium to the market.

We recommend ACCUMULATE on ZEEL with a price target of Rs.212

- A discount is justified in our opinion after factoring in the increased competitive intensity through new GEC launches, accompanying fragmentation of the Indian TV broadcasting industry and also our inclination to monitor renewed expectations of the ad-revenue growth trajectory.
- Noting upside to our fair value and also stock's recent under-performance, we move recommendation to **ACCUMULATE** (REDUCE previously).

Key Concerns:

- Belied hopes on a faster than expected revival in the economic growth trajectory and advertising revenue trends, will impact advertising revenue growth and company financials negatively
- Loss in ratings and competitive positioning
- Hyper-competition impacting player and industry profitability negatively
- Lower than estimated pick-up in the subscription revenue stream

Change in FY10 estimates

	FY09A	FY10E		
		Old	New	% Chg
Revenues, Rs.mn	21728.5	24172.9	22009.1	-9.0
Advertising revenues, Rs.mn	10617.3	11466.7	9767.9	-14.8
Subscription revenues, Rs.mn	9013.6	10440.8	10405.8	-0.3
EBITDA, Rs.mn	5331.1	6024.5	6024.9	0.0
EBITDA %	24.5	24.9	27.4	
PAT, Rs.mn	3749.0	4362.6	4557.8	
EPS, Rs.	8.6	10.1	10.5	4.1

Source: Company, Kotak Securities - Private Client Research

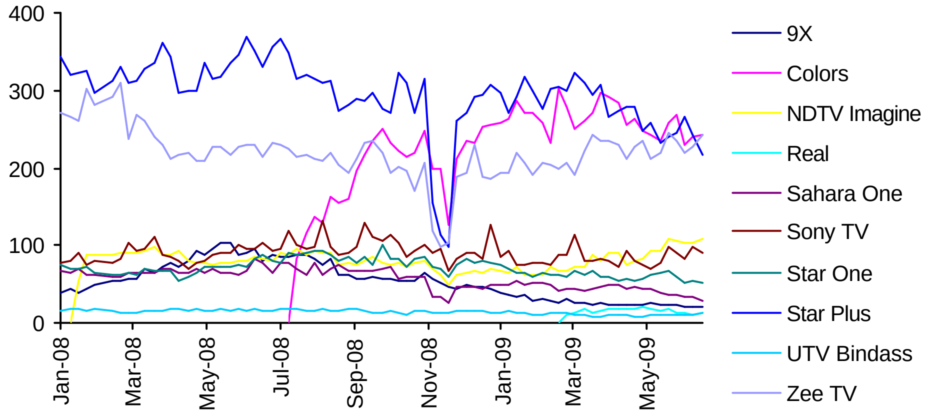
DTH revenue trajectory- heartening; sustained growth will likely be a game changer for the stock

	FY08	Q1FY09	Q2FY09	Q3FY09	Q4FY09	Q1FY10
DTH revenues, Rs.mn	613.0	248.9	271.0	283.0	381.1	467.0
Domestic sub revenues, Rs.mn	3487.0	1053.3	1111.0	1130.0	1230.0	1318.0
DTH as a % of sub revenues	17.6	23.6	24.4	25.0	31.0	35.4
Growth YoY, %		99.1	116.8	61.3	103.3	87.6

Source: Kotak PCG Estimates

ZEEL ratings have improved; good news for advertising revenue visibility

Zee TV ratings have improved consistently; the race for No.1 gets closer



Source: TAM data; compiled by Kotak Private Client Research

RESULT UPDATE

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LARSEN & TOUBRO LTD

PRICE: RS.1342 **RECOMMENDATION: ACCUMULATE**
TARGET PRICE: RS.1470 **FY10E P/E: 22.6X**

- **Lower than expected revenue growth compensated by higher margins.**
- **Profit is ahead of expectations aided by higher margins and robust other income.**
- **Target of 25% growth in order inflows maintained for the year. However, order booking would be essentially back-ended, which exposes the company's guidance to risk of slippages/delays in order booking.**
- **Management maintains 15-20% growth guidance in revenues in FY10.**
- **Maintain ACCUMULATE given sharp outperformance in the first quarter. On a near-term basis, the stock looks close to fairly priced. Hence, we maintain our recommendation.**

Summary table

(Rs mn)	FY09	FY10E	FY11E
Sales	404,799	486,560	595,336
Growth (%)	37.9	20.2	22.4
EBITDA	49,587	61,855	73,477
EBITDA margin (%)	12.2	12.7	12.3
Net profit	37,895	35,663	42,306
EPS (Rs)	51.4	61.1	72.4
Growth (%)	25.1	18.9	18.6
DPS (Rs)	8.5	8.5	8.5
ROE (%)	30.7	23.1	22.5
ROCE (%)	15.6	17.1	18.4
EV/Sales (x)	2.2	1.8	1.5
EV/EBITDA (x)	17.6	14.3	11.9
P/E (x)	26.8	22.6	19.0
P/BV (x)	5.8	4.8	3.9

Source: Company, Kotak Securities - Private Client Research

Financial performance

(Rs mn)	Q1 F10	Q1 FY09	% YoY
Net sales	**73627**	**69014**	**7**
Other op income	456	404	13
Total op expenses	65,864	62,318	6
Raw material	16,809	16,096	4
Sun-contracting charges	19,283	14,573	32
Construction materials	13,724	15,395	-11
purchase of trading goods	2,750	4,104	-33
Other operating expenses	4,754	4,984	-5
sales and admin exp	3,431	3,193	7
Personnel	5,115	3,974	29
Operating Profit	**8219**	**7101**	**16**
Other income	2228	1614	38
Interest	1,096	505	117
Gross Profit	**9,351**	**8,210**	**14**
Depreciation	837	659	27
PBT	**8514**	**7551**	**13**
current Tax	2,730	2,526	8
Adjusted PAT	5783	5024	15
Extraordinary gains	10198.8	0	
Reported PAT	15982	5024	
EPS	**9.9**	**8.6**	
EBITDA (%)	11.2	10.3	
Raw Matl costs to sales (%)	22.8	23.3	
Sub-contracting costs to sales (%)	26.2	21.1	
Construction materials costs to sales (%)	18.6	22.3	
Purchase of trading goods costs to sales (%)	3.7	5.9	
Other op expenses costs to sales (%)	6.5	7.2	
Sales and admin costs to sales (%)	4.7	4.6	
Personnel costs to sales (%)	6.9	5.8	
Current tax rate %	32	33	

Source: Company

Segment Performance

	Q1 FY10	Q1 FY09	YoY (%)
Segment revenues (Rs mn)			
Engg and Construction	65729	55417	19
Electronics	5759	5776	0
Mach and ind products	4370	6335	-31
Others	771	3760	-79
Total	**76628**	**71287**	**7**
PBIT margins (%)			
Engg and Construction	10.6	9.7	
Electronics	11.8	11.5	
Mach and ind products	21.8	23.1	
Others	5.4	6.6	
Capital employed (Rs mn)			
Engg and Construction	69789	48167	45
Electronics	11511	10526	9
Mach and ind products	2943	4075	-28
Others	2154	3022	-29
Total capital employed in segments	86397	65790	31

Source: Company

- Revenue growth during the quarter has moderated to 7% yoy to Rs 73.6 bn. The Engineering and Construction (E&C) business, which contributes 85% of revenues grew 19% yoy and was the prime growth driver.
- Revenue growth in this division has clearly moderated in line with overall slow-down in order inflows.
- Revenue growth could also be lower due to decline in material prices since Q1 FY09.
- Adjusted for divestment of RMC business, the net sales have grown 11% for the quarter.
- The electrical business which had been growing at a fast pace till FY08 has continued to slow down in FY10. Revenues in this segment were flat for the quarter. Moderation in industrial production is reflecting in the lower offtake of electrical products (low voltage switchgear, metering and medical equipment) and petrol dispensing machines. This business segment has slowed down due to curtailment in capex plans of petrol marketing companies impacting petrol dispensing machines business.
- The machinery and industrial products reported 31% fall in revenues in the quarter. This division includes mining equipments (L&T Komatsu, L&T Case Equipments and TENGL), Rubber Processing Machinery, Voith paper Technology, plastics machinery, Valves (Audco India), welding products and EWAC Alloys. The recessionary trend witnessed in the manufacturing and the Industrial sectors continued to severely affect the demand for the range of products of MIP segment.
- Others segment include Technology Services division, e-Engineering solutions and embedded systems. Due to the divestment of RMC business in FY09 the revenues are down 79% yoy.

Operating margins ahead of expectations

- EBITDA margins for the quarter came at 11.2% up 90 bps on a yoy basis.
- The company's margins have received a boost as a higher number of its projects have crossed the profit recognition stage.
- Around 70% of the company's projects have material price escalation clause and hence profitability may remain largely neutral to material price movement. The management does not expect to accrue any benefit from the material price softening.
- The company reported sharp rise in subcontractor charges and a dip in consumption of construction materials, which could be due to higher work being executed through subcontractors.
- The company should have benefited from lower commodity prices.

Sharp increase in interest costs

Interest expenses rose 117% yoy to Rs 1096 mn. The increase has been on the back of overall increase in borrowings. The average cost of borrowing is 6.5%.

Other income higher due to dividends from liquid MF investments

The company booked treasury gains on liquid investments, which has boosted the other income for the quarter. There was no dividend payout from L&T Komatsu during the quarter which reduced income from dividends from Associate companies.

Details of other income

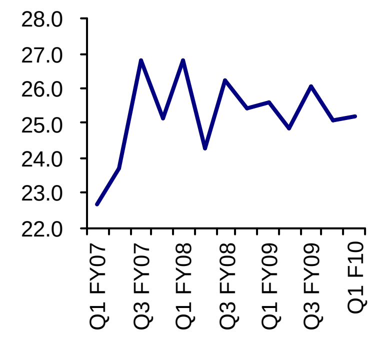
(Rs mn)	Q1 FY10	Q1 FY09
Interest income	302	104
Dividend from S&A companies	109	435
Dividend/income from investments	636	628
Profit on sale investments	824	0
Misc income	357	447
Total	2228	1614

Source: Company

Company disappoints on Order booking

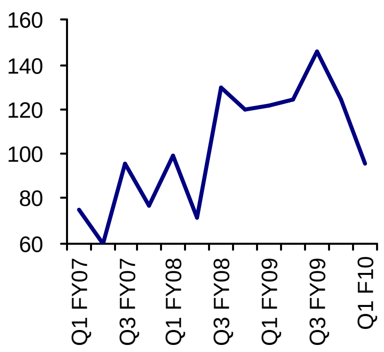
- Order backlog for L&T is up 23% yoy to Rs 716 bn, equivalent to revenue visibility of 25 months based on trailing four quarters revenues.
- Order inflows for Q1FY10 came in at Rs 95bn, down 22%.
- Growth in order inflows was impacted by deferral of some large value orders (ONGC orders etc) and also election related protocols.
- The management has cited cautious "wait and watch" approach on the part of project developers as mainly responsible for relatively lower order Inflows during the quarter.
- Order mix is also changing in favour of power and infrastructure sector orders. As against this, the share of process and oil and gas orders has declined. The slowdown in petro-products consumption and decline in crude prices have affected projects in oil and gas sector, thus hurting the order inflows. L&T has responded by increasing its presence in power transmission related orders.
- Around 13% of the orders are from group infrastructure companies.
- The management expects the ONGC related orders (USD 1 bn in size) to get finalized in a few weeks time.

Revenut visibility months



Source: Company

Quarterly order booking (Rs bn)



Source: Company

We maintain ACCUMULATE recommendation on L&T with a price target of Rs.1470

Order mix

(%)	Q1 FY08	Q1 FY09	Q1 FY10
Process	11	15	9
O&G	22	22	12
Power	14	19	30
Infrastructure	36	34	38
Others	17	10	11

Source: Company

Subsidiary Performance

	Revenues			PAT		
	Q1 FY10	Q1 FY09	YoY (%)	Q1 FY10	Q1 FY09	YoY (%)
L&T IT	4.7	4.5	4	0.62	0.61	2
L&T Fin	1.98	1.8	10	0.24	0.25	-4
L&T Infra	0.86	0.75	15	0.22	0.18	22

Source: Company

Outlook

- Management expects to grow at 15-20% in FY10.
- Growth in order inflows is targeted at 25%. Despite the shortfall in order inflows in Q1 FY10, the management has maintained the target. It has indicated that bulk of order inflows is expected to be booked in H2 FY10. This exposes the company to the risk of slippage in order guidance.
- Margins are expected to be maintained.
- Revenue outlook for FY11 has improved given stable political scenario likely spurring investment decisions.
- The Boiler and Turbine facility is expected to be commissioned by Dec 2009 and June 2010 respectively.
- Capex for the current year has been planned at Rs 15-20 bn.

Valuation:

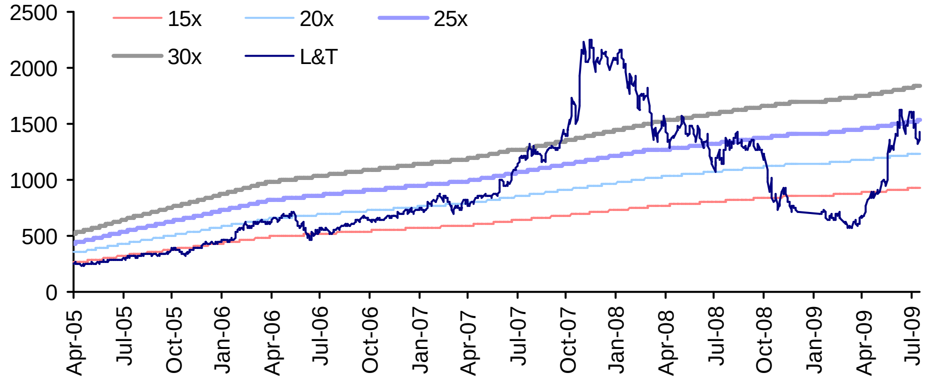
L&T is trading at 22.6x and 19x FY10 and FY11 earnings respectively. We maintain **ACCUMULATE** with a target price of Rs 1470 (Rs 1350 earlier).

Valuation

	Parameter	Fair Value	Per share
L&T Infotech	10x FY10 earnings	23,760	41
L&T Finance	10x FY10	11,880	20
Infrastructure/overseas subs/property			
subsidiaries	12x FY10	17,342	30
L&T Standalone	DCF		1380
Total			**1470**

Source: Kotak Securities - Private Client Research

PE Band



Source: Capitaline, Kotak Securities - Private Client Research

Bulk deals

Trade details of bulk deals

Date	Scrip name	Name of client	Buy/ Sell	Quantity of shares	Avg. price (Rs)
16-Jul	Aarey Drugs	Shaishil Tushar Kumar Jhaveri	B	25,000	45.00
16-Jul	Aarey Drugs	Nikhil Vinukant Shah	S	25,000	45.00
16-Jul	Avon Corp	Ravi Shet	S	89,000	8.56
16-Jul	Betala Glo S	Biswanath Mondal	S	8,586	4.17
16-Jul	Cat Technol	S V Enterprises	S	165,000	6.56
16-Jul	Enrich Indut	Jayeshkumar Jayantilal Pandya	B	70,000	3.15
16-Jul	Enrich Indut	Hitesh Arjunbhai Ahir	B	65,000	3.15
16-Jul	Enrich Indut	Dinesh Madhukar Bhanarkar HUF	B	50,000	3.15
16-Jul	Enrich Indut	Kavita Dinesh Bhanarkar	B	45,000	3.15
16-Jul	Enrich Indut	Hemant R Shah	S	300,000	3.15
16-Jul	Jumbo Bag Lt	Rushab Ravji Patel	B	53,695	65.46
16-Jul	Kaman Hsg	Nisha Suman Jain	B	110,000	30.66
16-Jul	Katare Spg.	Ramesh G Gokani	B	30,001	13.25
16-Jul	Katare Spg.	Ami Stock & Share Brokers Pvtltd	S	30,000	13.25
16-Jul	Kay Pow Pap	Sunder Dass Agarwal	S	88,766	6.24
16-Jul	Koff Br Pict	Kamlesh Kusumchandra Shah	B	300,000	3.78
16-Jul	Kuvam Intl	Sanjiv V Aroraa	B	19,000	12.75
16-Jul	Kuvam Intl	Mayurbhai Gordhanbhai Patel	S	25,000	12.75
16-Jul	Kuvam Intl	Govind Mathuradas Kotak	S	45,000	12.75
16-Jul	Kuvam Intl	Alka Dilip Rathod	S	29,800	11.55
16-Jul	Liberty Phos	Sadiqua Banu	B	50,000	24.88
16-Jul	Liberty Phos	Siraj Rahimtula	S	50,000	24.87
16-Jul	Moldtek Tech	Rajendar Reddy Narra	S	20,290	76.65
16-Jul	Passari Cell	Primex	B	30,000	30.70
16-Jul	Passari Cell	Paras Kanwar	S	37,000	30.70
16-Jul	Riba Textile	Manjula Nilkhanth Shah	B	50,000	48.50
16-Jul	Riba Textile	Shailesh Somabhai Patel	B	60,199	49.72
16-Jul	Riba Textile	Patel Nitaben Shaileshbhai	S	124,801	50.12
16-Jul	Rishabhdev	JMP Securities Pvt Ltd	S	145,949	19.88
16-Jul	Splash Media	Bhanumati Dharamraj Giri	S	12,920	109.83
16-Jul	Supertex Ind	Archita Jignesh Shah	B	60,000	55.99
16-Jul	Supertex Ind	Harish Ratilal Shah	S	56,750	56.01

Source: BSE

Gainers & Losers

Nifty Gainers & Losers

	Price (Rs)	chg (%)	Index points	Volume (mn)
Gainers				
Reliance Ind	1,935	3.2	15.5	5.5
NTPC	205	3.2	2.0	8.0
Gail India	339	3.6	2.0	3.5
Losers				
L&T	1,379	(3.6)	(11.1)	5.1
HDFC	2,378	(2.0)	(4.4)	0.7
Sterlite Ind	590	(6.3)	(4.0)	10.5

Source: Bloomberg

Forthcoming events

Company/Market

Date	Event
17-Jul	TCS, Container Corporation, Crompton Greaves, India Infoline, Colgate Palmolive, Kirloskar Brothers, Sasken Communication, SKF earnings expected
18-Jul	Petronet LNG, Gujarat NRE Coke, Apollo Hospitals, Rel Ind. infra earnings expected
20-Jul	JSW Steel, GTL Infra, RCF, Essar Oil earnings expected
21-Jul	Chambal Fertilizer, Ultratech, Thermax, Dr. Reddy's Lab, LIC Housing Finance, Yes Bank, OBC earnings expected
22-Jul	Wipro, Canara Bank, India Cements, GTL, Tech Mahindra earnings expected
23-Jul	Maruti, Biocon, Ambuja Cements, Siemens, Alstom Project, MRPL, Indian Bank, Union Bank of India, Bharti Airtel, Madras Cements earnings expected
24 Jul	HCC, Bharat Electronics, Gail Inda, CESC, Bharat Forge earnings expected

Source: Bloomberg

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